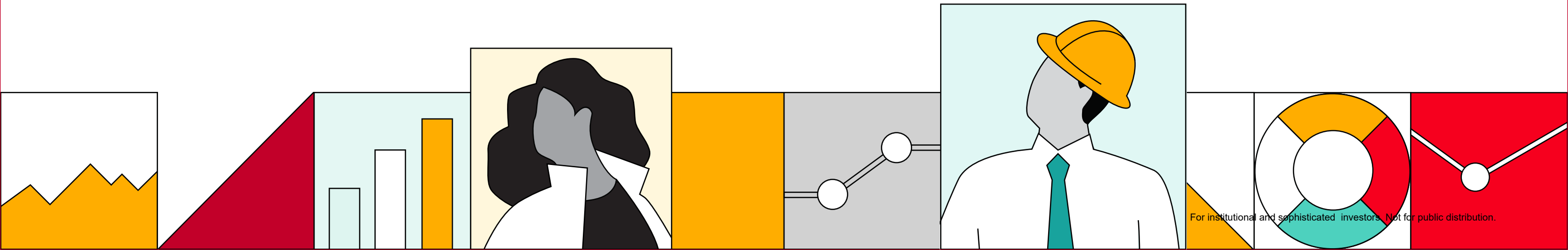


How America Saves 2022

# Insights to Action



## Insights 2022

We believe plan sponsors can use smart plan design to keep participants on the road to financial well-being.

# During times of uncertainty, widening the focus of retirement plans to encompass every phase of a plan participant's financial journey simply makes sense.

## Why?

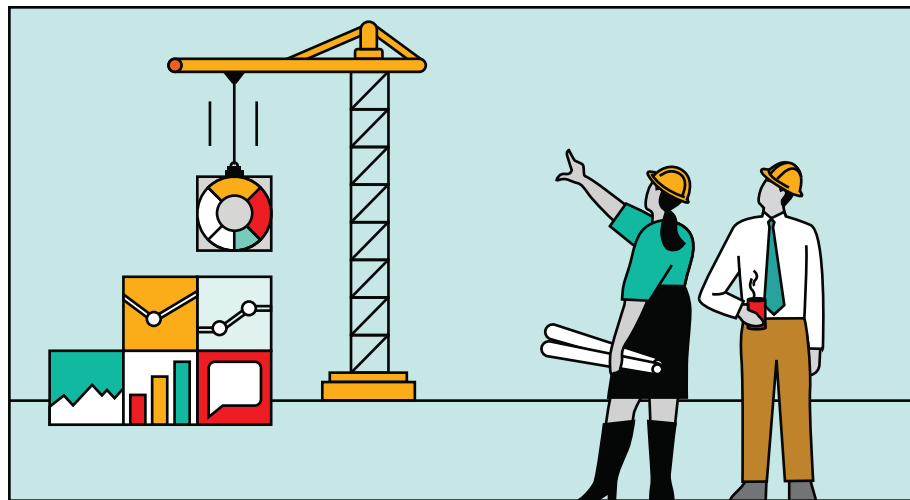
We know near-term financial challenges can jeopardize long-term retirement success. And participants continue to face what must seem at times like an unprecedented number of near-term challenges.

While the economy continued to recover from the COVID-19 pandemic in 2021, the challenges mounted: Inflation increased to its highest point in decades, supply-chain disruptions tempered economic growth, and a tightened labor market continued to test employers while their employees left in record numbers—either changing jobs or leaving the workforce entirely.

The good news: While these challenges remain, we believe plan sponsors can use smart plan design to keep participants on the road to financial well-being.

This year's *Insights to Action* focuses on three key themes we've identified from *How America Saves 2022* data—recommendations based on the belief that strong plan design serves participants well in all stages of their financial journey.

# Key themes



**01**

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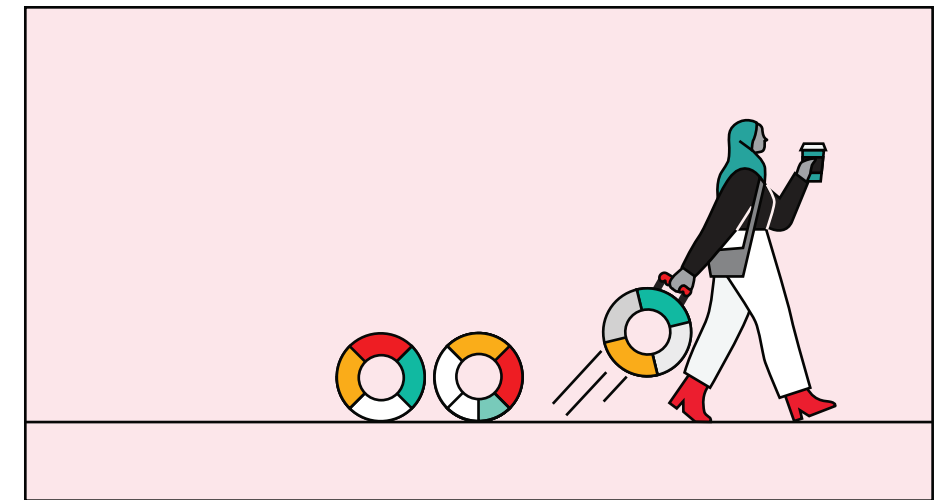
**Support financial well-being with professionally managed allocations**



**02**

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**Take smart plan design to the next level**



**03**

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**Plan for an increasingly mobile workforce**

# 01

## Support financial well-being with professionally managed allocations

### PLAN ACTIONS

- 1 Offer an advice option.
- 2 Make TDFs your default by using a QDIA and choosing TDFs as the option.
- 3 Reenroll participants into TDFs by sweeping them into an appropriate TDF, helping to ensure portfolios are age appropriate and properly diversified.

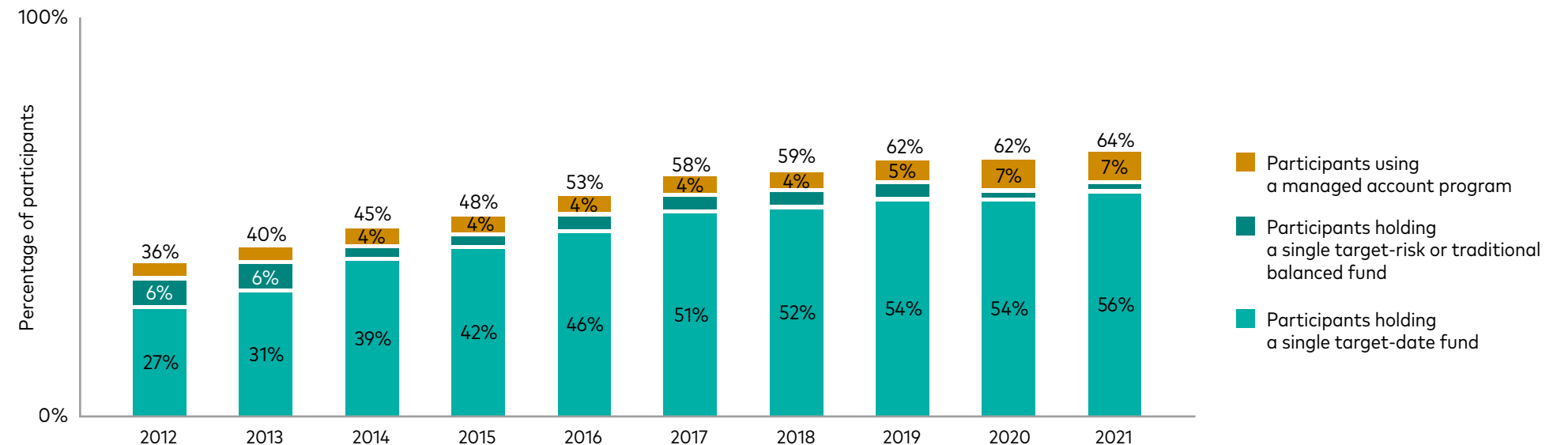


## Broaden the scope of retirement plans to support participants' financial well-being with self-directed solutions and advice that focus on every step of their journey to and through retirement.

An increasing number of participants are invested in a professionally managed allocation. In fact, the percentage of participants in either a target-date fund or an advised managed account program reached all-time highs in 2021.

This shift has contributed to improved participant behaviors and outcomes—progress that will likely continue to drive the use of professionally managed allocations.

### Participants with professionally managed allocations Vanguard defined contribution plans



Source: Vanguard 2022.

For example, in 2005, participants' age-based equity allocation was hump-shaped, with younger participants adopting more conservative allocations, middle-aged participants holding the highest equity exposure, and older participants having equity exposure on par with younger participants (see chart on next page).

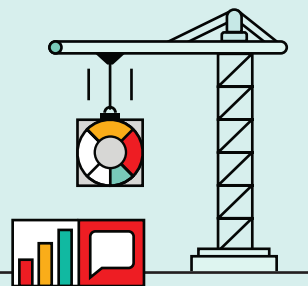
In 2021, the equity allocation among Vanguard DC participants was downward sloping by age. This is tied directly to the growing use of professionally managed allocations, which typically provide declining equity exposure with age.

# 01

## Support financial well-being with professionally managed allocations

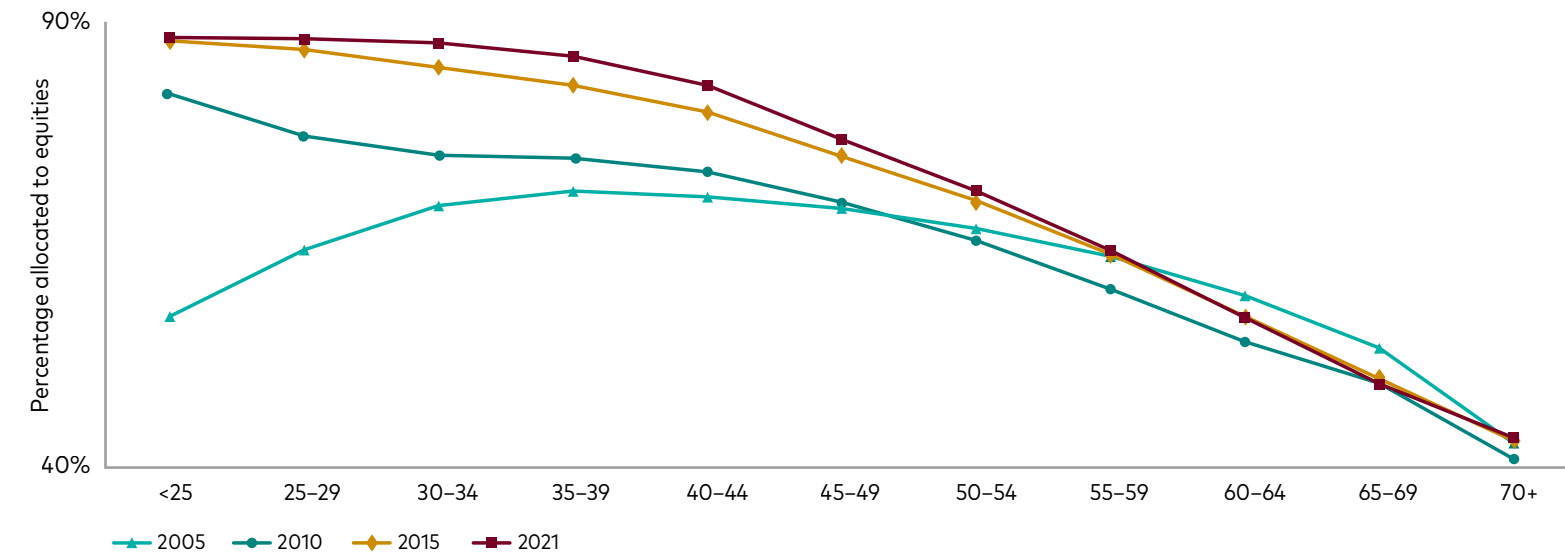
### PLAN ACTIONS

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### Trend in asset allocation by participant age

Vanguard defined contribution plans: Average equity allocation participant weighted



Source: Vanguard 2022.

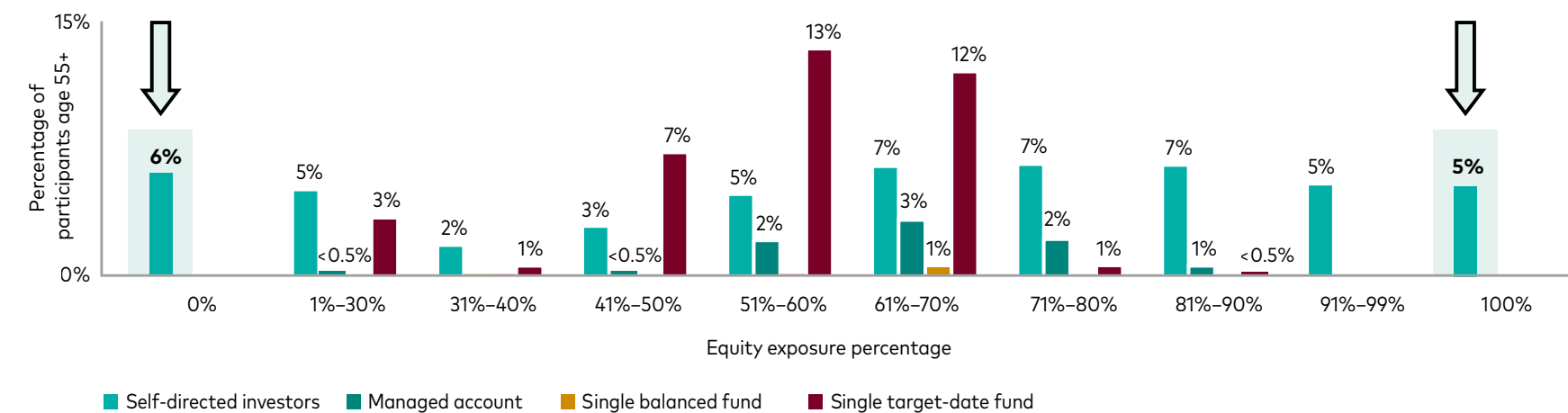
### An opportunity for improvement

Interestingly, younger participants are more likely to have a professionally managed allocation, which results in a higher percentage of them having an age-appropriate equity allocation.

Fifty-one percent of older participants, who were nearing or in retirement, were self-directed investors who constructed their own portfolio in 2021. And participants who construct their own portfolios have equity exposure with both wider dispersions and generally greater extremes.

### Distribution of equity exposure by older investors, 2021

Vanguard defined contribution plan participants age 55+



Source: Vanguard 2022.

# 02

## Take smart plan design to the next level

### PLAN ACTIONS

- 1 Implement automatic enrollment with automatic annual increases.
- 2 Default participants at 6%, or at least to the employer match.
- 3 Perform reenrollment, automatic escalation, and undersaver sweeps.



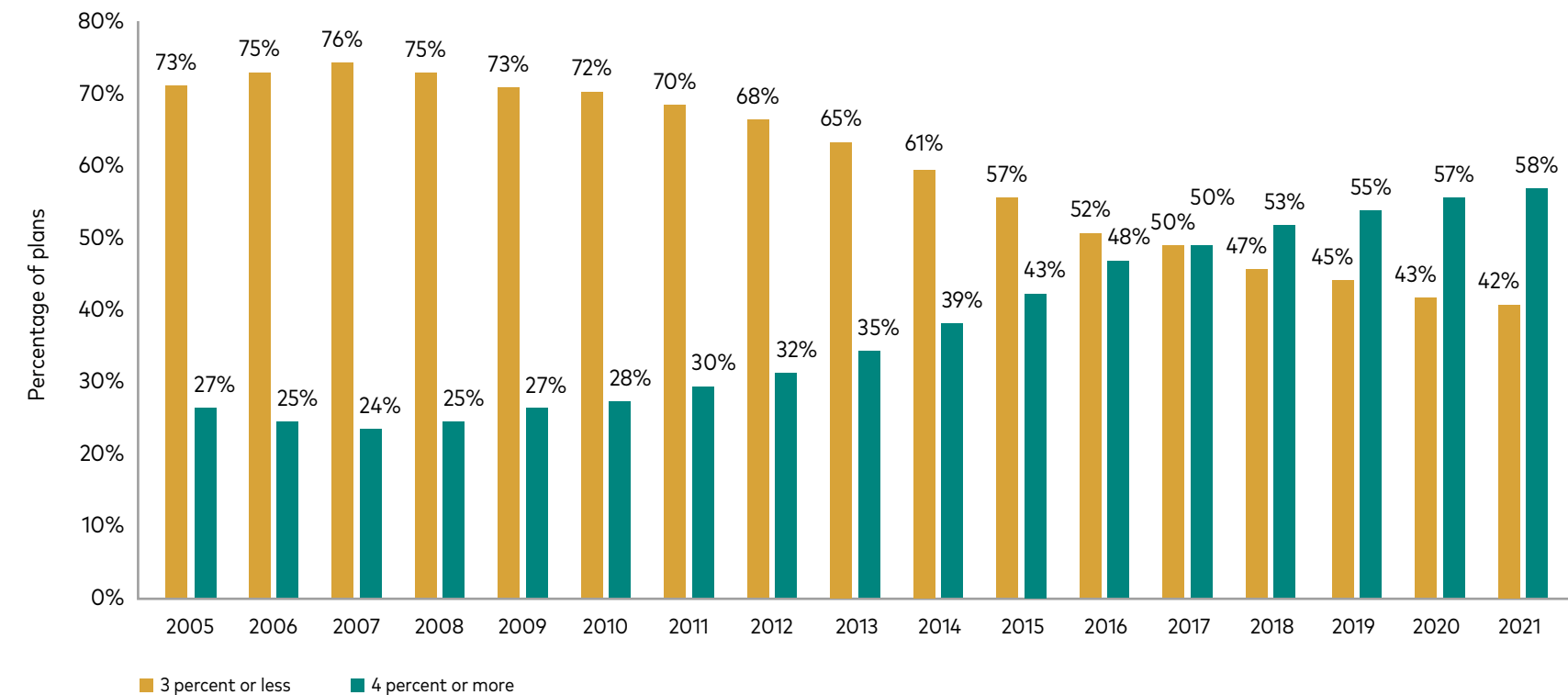
## Combine automatic plan features with a higher default rate for a powerful savings boost

Automatic solutions (automatic enrollment and automatic escalation) are proven to increase plan participation and saving rates, but the benefits of the strategies depend largely on how they are implemented.

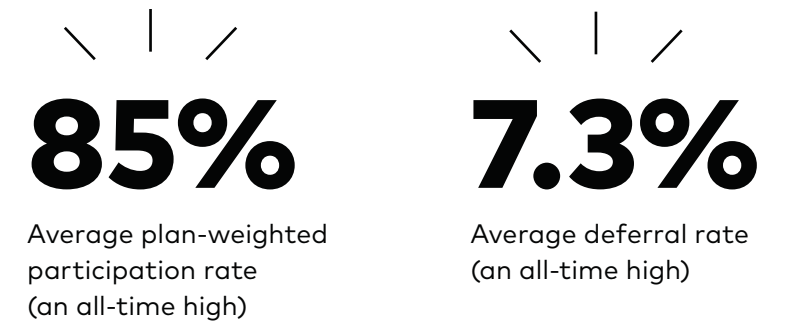
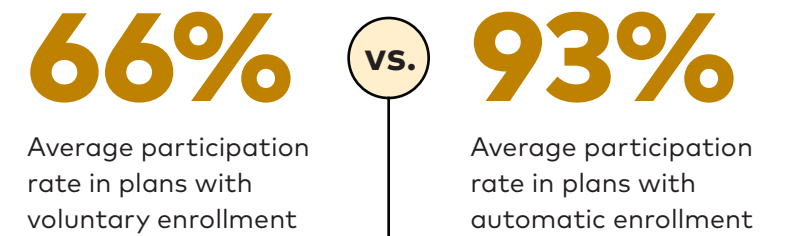
For example, Vanguard participants saved an all-time high 7.3% of their income, on average, in their employer's plan in 2021. This can partly be attributed to the fact that 58% of plans now default at rates of 4% higher—the continuation of an upward trend. We believe it's critical to maintain this momentum by increasing the initial default and marrying it to an automatic escalation feature.

### Automatic enrollment default trends

Vanguard defined contribution plans with automatic enrollment



Source: Vanguard 2022.



# 02

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### Why are automatic escalation features so important?

A modest increase in participant deferral rates of 1, 2, or 3 percentage points would enable an additional 20% of participants to attain a 75% replacement ratio in retirement, according to soon-to-be-published Vanguard research.

### The case is clear: Higher defaults lead to stronger savings.

But do higher deferral rates influence the likelihood that an employee will quit an automatic enrollment plan?

We might expect that plans with initial deferral rates of 2% or 3% would see fewer employees quitting the plan, given that these lower deferral rates have little impact on take-home pay. Conversely, we might think that deferral rates of 5% or 6% would lead to a higher opt-out rate because of their larger impact.

However, our research suggests that employee quit rates do not appear to vary in response to a plan sponsor's choice of the initial deferral rate.<sup>1</sup>

A modest increase in participant deferral rates of 1, 2, or 3 percentage points would enable an additional **20%** of participants to attain a **75%** replacement ratio in retirement.

<sup>1</sup> For an in-depth analysis of automatic enrollment, see Jeffrey W. Clark and Jean A. Young, *Automatic Enrollment: The Power of the Default*. Vanguard research. February 2021. [institutional.vanguard.com](https://institutional.vanguard.com)

# 03

## Plan for an increasingly mobile workforce

### PLAN ACTIONS

- 1 Consider new design strategies to attract workers.
- 2 Design your plan to ensure the cycle of strong saving and investing behavior continues uninterrupted through job changes.
- 3 Question your service provider about portability services.



## Ensure plan portability, protecting employee retirement assets for the future and preserving the work you've put into the plan.

As we emerge from the COVID-19 pandemic, the U.S. workforce is experiencing significant changes. Millions of employees are changing jobs or leaving the workforce entirely. This is creating both opportunities and challenges for employers.

Many employers are reviewing their retirement benefits and evaluating options to attract and retain employees.

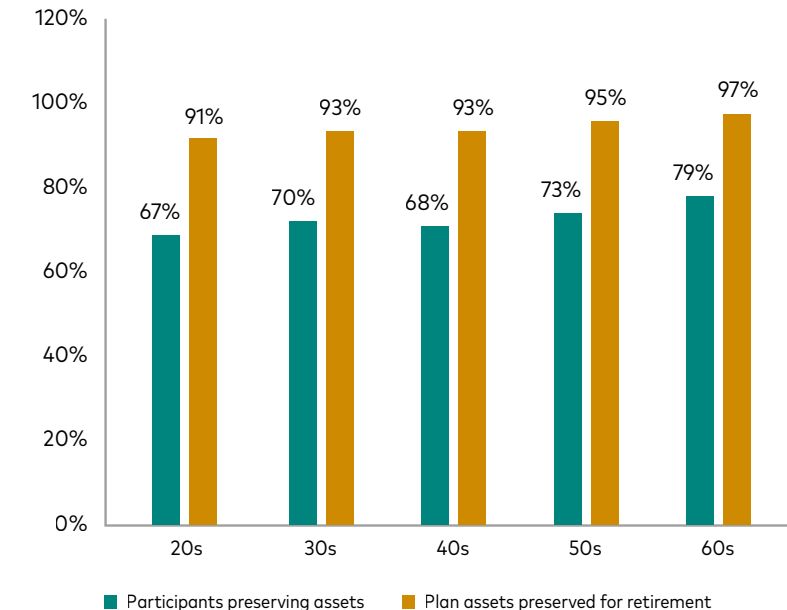
## In 2021, 14% of participants left their employer and were eligible for a distribution.

But higher attrition can lead to disruptions in retirement saving. When employees change employers, there is a risk that retirement assets will be cashed out, potentially spoiling the work you've put into the plan.

Younger participants are more likely to have smaller balances, which are more likely to be cashed out than preserved for retirement. And although these balances tend to be smaller, these cash-outs can negatively impact retirement readiness down the road because of the potential power of compounding growth.

Such numbers strongly suggest that plan sponsors consider design elements that promote smart and seamless retirement plan transitions for an increasingly mobile workforce.

### Assets preserved for retirement by age Vanguard defined contribution plans



Source: Vanguard 2022.

### The benefits of a portability solution

Instituting an automatic portability feature in the plan can help to make it easier for employees to preserve their retirement assets between employers.

For example, Vanguard has engaged a leading provider of consolidation services for defined contribution plans to provide plan sponsors with a new portability solution to simplify small-balance 401(k) rollovers, help more employees preserve their retirement savings, and improve their chances of investment success. The service is expected to launch in mid-2022.

Offering a portability solution is part of Vanguard's holistic focus on financial wellness solutions. These solutions are rooted in the idea that to achieve retirement readiness, plans should consider very specific challenges that often get in the way of successfully saving for retirement such as managing debt or paying for an emergency.

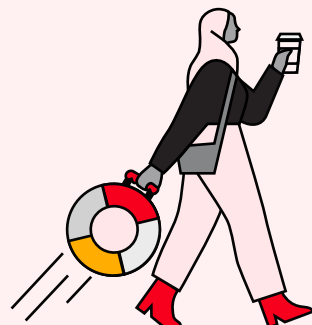


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### Automatic enrollment provides another solution

Defaulting at low rates, even with an automatic escalation feature, can lead to a cycle of employees continually undersaving if they change jobs every two to three years.

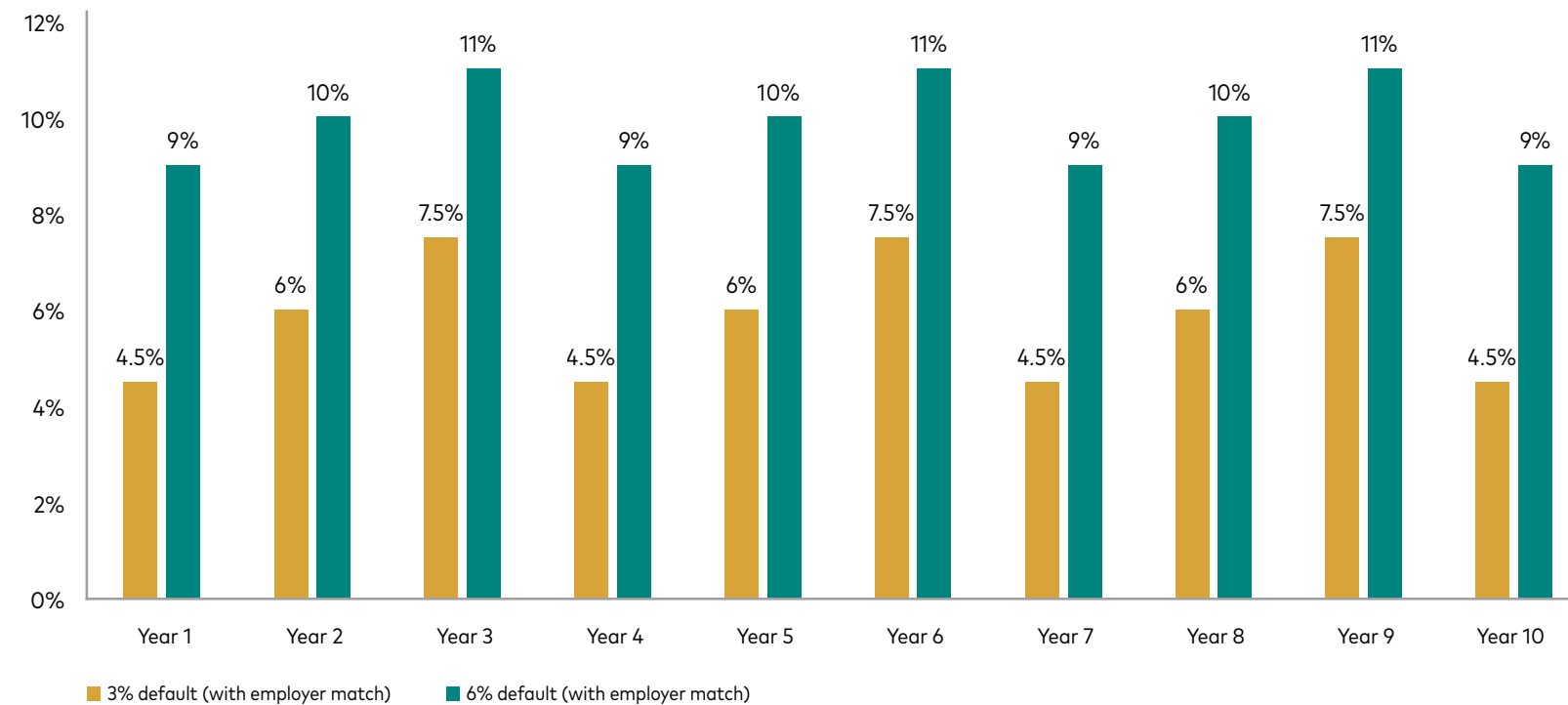
Setting defaults at a strong level (at least to the match) helps to ensure that new employees are saving at strong levels from day one. Consider that after 10 years, employees defaulted at 6% have an accumulated balance that is nearly 70% higher than those at a 3% default.

# 70%

After 10 years, employees defaulted at 6% have an accumulated balance that is nearly **70%** higher than those at a 3% default.

### Comparing impacts of defaults: 3% vs. 6%

Assumes an employer match of 50% on 6% employer matching contribution



Notes: Employees change jobs every three years. Automatically enrolled at either 3% or 6%. Automatically increased in both scenarios. Employer match of 50% on 6% in each scenario. Starting salary of \$50,000. Wage increases of 2% annual and 4% real return.

Source: Vanguard 2022.

# Conclusion

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## We believe plan sponsors must continue to focus on smart plan design.

Additionally, they should consider broadening the scope of retirement plans to support participants' financial well-being by focusing on every step of their journey to and through retirement. Finally, with an increasingly mobile workforce, sponsors may want to consider ways to keep participant assets in the plan.

The three key themes and recommended plan actions were identified by Vanguard Strategic Retirement Consulting (SRC) group. SRC helps defined contribution (DC) plan sponsors optimize their plan design, develop fiduciary best practices, ensure regulatory compliance, as well as share insights on investor behavior and collaborate on strategic communications.

Our complete analysis of Vanguard 2021 DC plan data can be found at [institutional.vanguard.com](https://www.institutional.vanguard.com). If you would like to learn more about the key themes surfaced in *Insights to Action*, or any of the data from *How America Saves 2022*, please reach out to a Vanguard representative.



How  
America  
Saves **2022**

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**Insights**  
**2022**

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