

Institute for
Fiscal Studies



Raising household saving

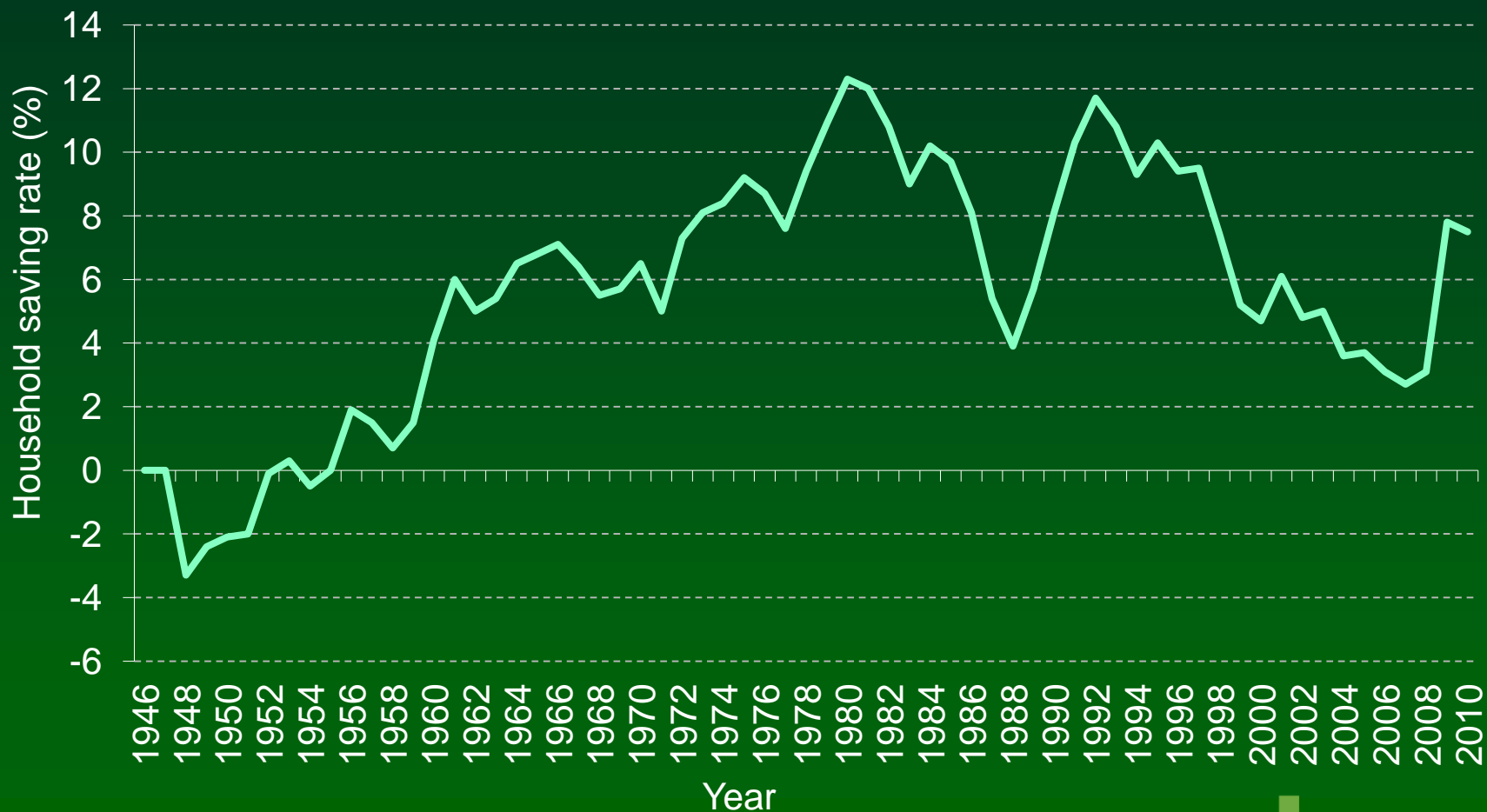
Thomas F. Crossley, Carl Emmerson and Andrew Leicester

Launch event, British Academy, London, 22 February 2012

Overview

- Concern that a significant number of individuals might not be saving enough for future needs
- What does economic theory tell us about why policymakers might or might not be concerned about low saving?
- Assess the evidence on a number of possible policy responses:
 - financial incentives
 - information, education & training
 - choice architecture
 - social marketing
- Conclusions

Aggregate household saving rate



Why do people save – and why don't they? (1/2)

- Standard economic models suggest that individuals save when:
 - income is high
 - needs are low
 - returns are high
- Might expect to see lower saving rates among those with apparently low current income
 - income might be temporarily low
 - income might be mis-measured
- Passive and active saving
- Low returns for low income households could mean that low saving might be privately optimal

Why do people save – and why don't they? (2/2)

- Individuals can only be expected to do the best they can with the information that is available to them
- Role for better information
 - avoid choice over-load
 - how it is provided
 - education to help individuals understand and use information
- Behavioural perspectives
 - bounded rationality
 - mental accounting
 - loss aversion and reference points
 - time inconsistency and self-control

Evaluation challenges

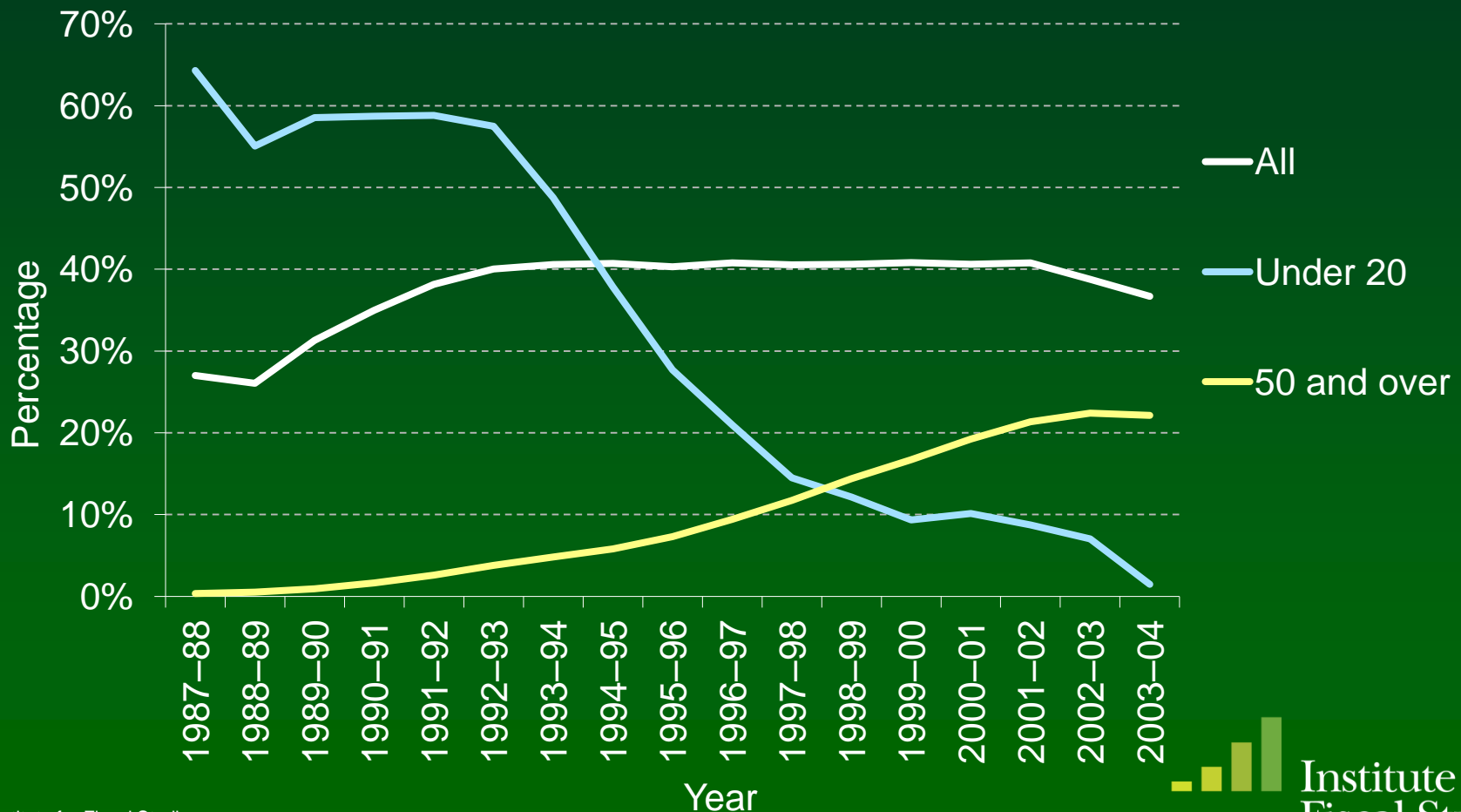
- Does an intervention boost saving?
 - example: introduction of new savings account
- Two questions to ask of any study
 - has an appropriate outcome been measured?
 - has a credible counterfactual been estimated?
- If new saving is this only a short-run impact or does it lead to an enduring impact on saving?

Financial incentives

- Financial incentive to save at all, and in different forms, affected by the tax, tax credit and benefit system
- Clear evidence these affect the form in which savings are held

Responsible teenagers?

% of employees with a second-tier pension choosing to contract out into a personal or stakeholder pension



Financial incentives

- Financial incentive to save at all, and in different forms, affected by the tax, tax credit and benefit system
- Clear evidence these affect the form in which savings are held
- Less clear is whether overall saving is increased
 - majority of funds in tax-favoured accounts not new saving, but some might represent new saving
- Those expecting to receive means-tested support in retirement can have particularly weak financial incentives to save
 - lack of evidence on whether this does lead to lower private saving
 - further research could be fruitful, but difficult to identify who might be affected by such policies
- Matched saving accounts attempt to target marginal saver
 - limited evidence of impact on total saving
 - no evidence on whether impact endures



Financial education

- No good evidence that adults' financial education raises savings
- Does educating children on financial matters affect adult saving?
 - need long-term data on adult saving and wealth to assess
 - with accurate information on financial education received at school
 - and random variation in the provision of such education
- Closest is US study by Bernheim *et al.* (2001)
 - survey of 2,000 adults aged 30 to 49
 - variation in 'consumer education' mandates at high school
 - exposure increases saving rate and wealth holdings
- Policy could be informed by workplace financial training
 - retirement planning seminars help raise retirement saving
 - may also have small spillover effects

Providing information

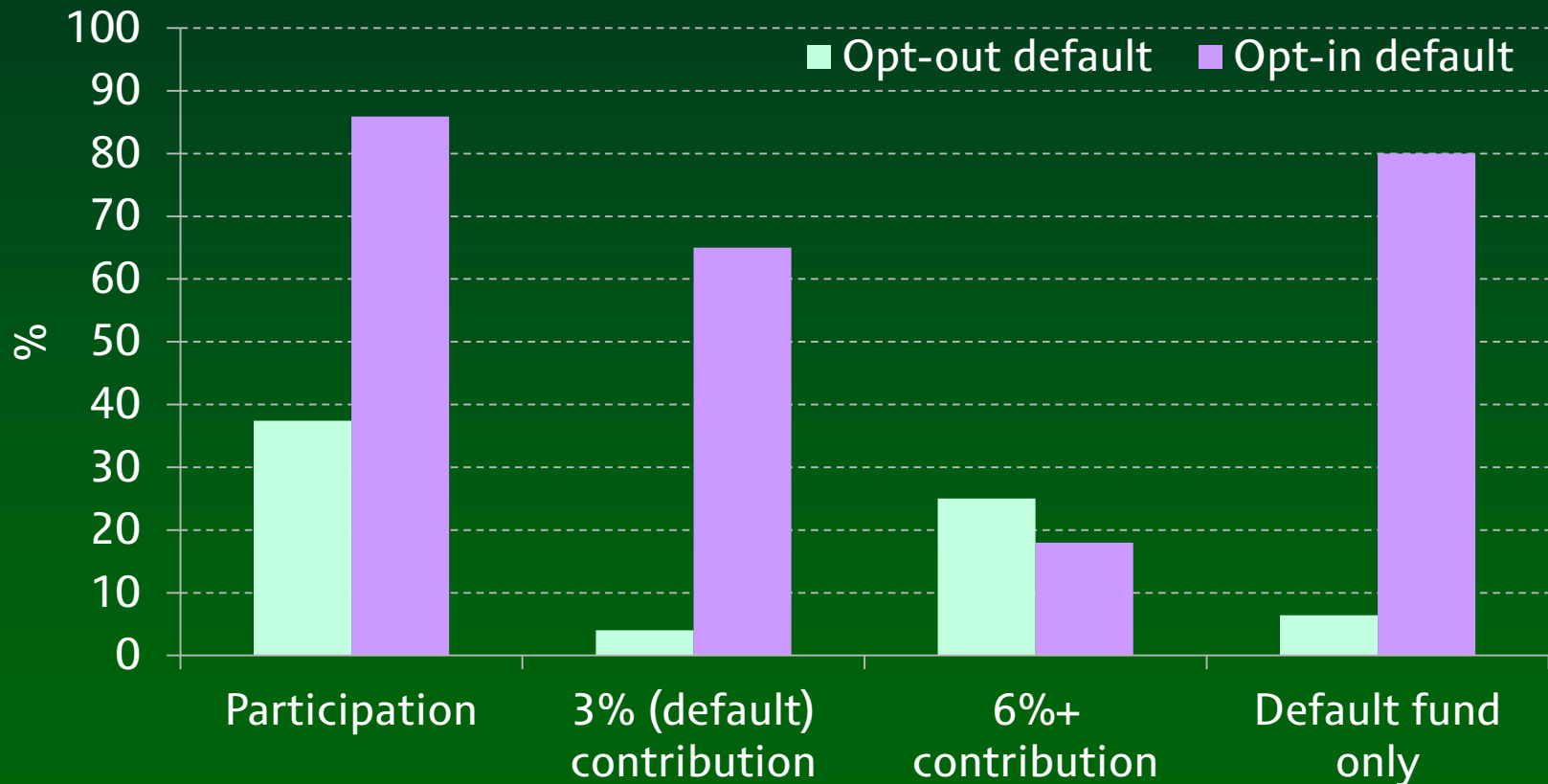
- Little evidence on whether information alone affects savings
- Most compelling study suggests not (Choi *et al.* 2011)
 - 689 workers in a firm not using full employer 401(k) match limits
 - age and tenure meant no penalty for immediate withdrawal
 - contributing to the limit raises wealth at potentially no cost
 - half given this information, half not
 - those treated raise contributions 0.1% more than those not
- Not just *what* information is provided but also *how* might matter
 - simplified information might improve investment decisions
 - evidence somewhat mixed

Choice architecture: changing default options

- Large US evidence base on 'opt-in' defaults for pensions saving
- Some empirical regularities: the default matters!
 1. Large increase in **participation**
 2. Many workers stick to default **contribution rate**
 3. The default **investment fund** is widely chosen

Madrian and Shea (2001)

Pensions saving behaviour 3–15 months after hire, single firm
Groups hired just before and just after move to opt-in default



Choice architecture: changing default options

- Large US evidence base on 'opt-in' defaults for pensions saving
- Some empirical regularities: the default matters!
 1. Large increase in **participation**
 2. Many workers stick to default **contribution rate**
 3. The default **investment fund** is widely chosen
- Overall effect on total saving not clear
 - some people will start to save, but others may save less
- 'Active decisions' – make people choose
 - smaller impact on uptake but less effect on contributions
- Default people into future increases in retirement saving?
 - Thaler and Bernartzi (2004) "Save More Tomorrow"
 - large rise in contributions but sometimes low take-up



Choice architecture: framing

- Presentation of savings options may affect choices (Saez 2009)
 - offer random one-off inducement to open a retirement savings fund
 - ‘match’ 50% of contribution or ‘rebate’ 33% - economically the same
 - take-up 3.3% if no inducement, 6.4% for rebate, 10.2% for match
- Laboratory evidence that framing matters for:
 - portfolio of retirement savings
 - willingness to investing in risky assets
- Field evidence for these effects not clear
- Framing could be built into evaluation design for future policy

Social marketing

- Draw on techniques from marketing to promote social goals
- Kotler and Zaltman (1971) summarise key features
 1. Identify target population
 2. Understand barriers to behaviour change
 3. Design, test and modify specific intervention based on barriers
- Application to retirement saving by Lusardi *et al.* (2009)
 1. **Target:** new employees at a US firm, opening retirement account
 2. **Barriers:** lack of information and complex online enrolment form
 3. **Intervention:** 'planning aid' leaflet breaking down application process into simple steps and providing information
 - 41% of treatment group enrolled within 2 months, 28% control
- Government to help fund and evaluate different schemes?

Final thoughts and conclusions

- Significant gaps in the evidence base remain
 - though obviously some individual high quality studies
- The main limitations are:
 1. A lack of randomised variation to give credible counterfactuals
 2. A failure to focus on comprehensive savings/wealth outcomes
 3. A focus on short-run, not long-run outcomes
 4. In general, a lack of UK-specific evidence
- An opportunity for policy makers
 - growing recognition of need for gold-standard randomised trials
- Trials not always possible or appropriate
 - need to develop models of behaviour change validated by evidence
 - crucial in assessing possible impact of new proposals





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