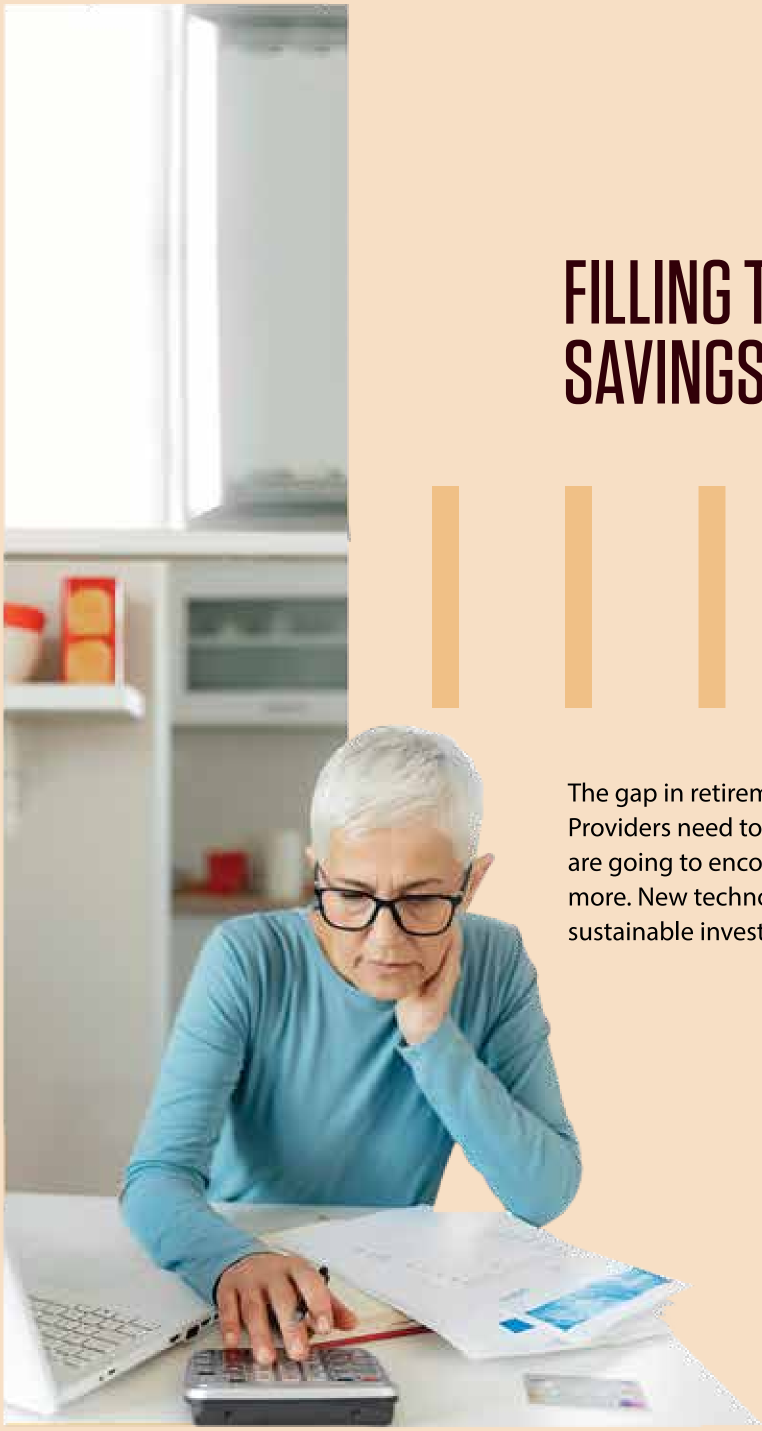
Infosys®
Navigate your next

VIEWPOINT



FILLING THE RETIREMENT SAVINGS GAP

The gap in retirement savings is growing globally. Providers need to modernize their approach if they are going to encourage more people to save and save more. New technology, combined with the rise in sustainable investing, could pave the way forward.

Infosys® | Knowledge Institute

A widening retirement savings gap

Workers are not saving nearly enough for their retirement, which is leading to a projected $70 trillion savings gap in eight of the world's largest markets, according to the World Economic Forum.[1] That staggering figure is predicted to increase to $400 trillion by 2050.

In the United States, nearly a quarter of working adults said they did not have any retirement savings or a pension, according to a Federal Reserve survey.[2] Participants acknowledged that they don't save as much as they should and are often caught in a web of debt, such as health care expenses. Saving for retirement is not seen as a priority — at least in comparison to more immediate needs.

Three challenges that make filling the gap difficult

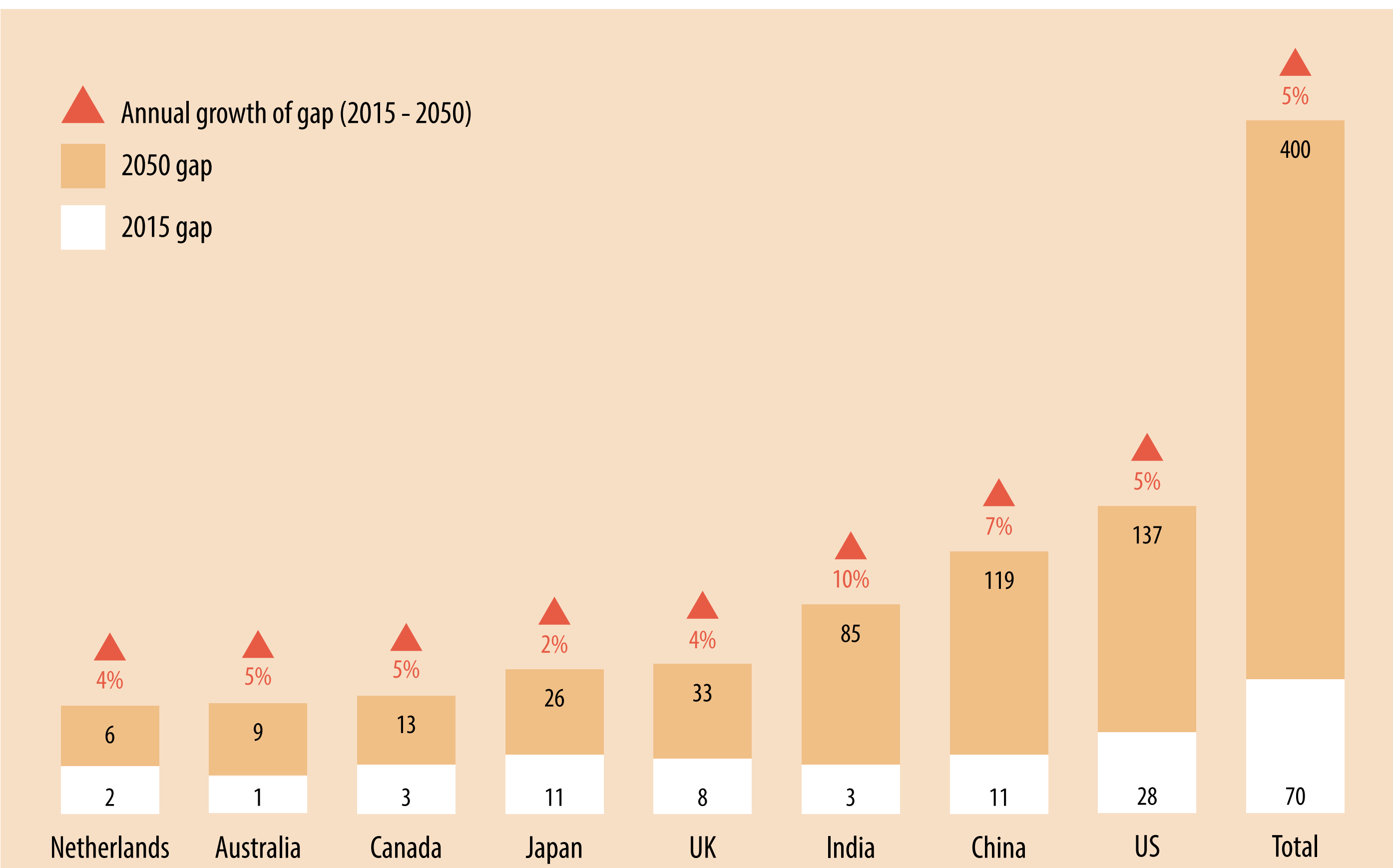
Narrowing this savings gap is possible but daunting. The difference between how much people save and how much they need to save isn't just a lack of will on the part of workers. Access, knowledge, and technology often create barriers.

Many small and midsized businesses, which employ nearly 61 million Americans, don't offer retirement plans to their staff.[3] The benefits are expensive, paper-intensive, and difficult to administer. Company executives would rather focus their time and effort on business priorities. A spring 2020 U.S. Bureau of Labor Statistics survey found that only 55% of employees participated in a workplace retirement plan.[4]

For those who do have plans, their lack of financial literacy creates more obstacles for them and the industry. Nearly 60% of non-retirees with self-directed retirement savings said they had low levels of comfort in making investment decisions, according to a Federal Reserve survey.[5]

Also, participants often find it difficult to obtain a holistic view of their finances, particularly as workers move from job to job. This is frequently the result of their retirement providers' aging technology infrastructure, which discourages efficient data sharing and integration. The retirement industry often relies on manual practices, legacy platforms, and paper-based communication. This makes it cumbersome and expensive for providers and offers clients a poor experience when compared with other consumer interactions.

Figure 1. Retirement savings gap increasing globally



Source: Mercer, World Economic Forum

With the existing systems and practices, retirement providers struggle to manage large amounts of complex data while navigating a tricky regulatory and cybersecurity landscape. However, the industry is now starting to change with the help of technology and a recognition that new directions are needed.

Regulatory steps

Regulatory efforts to promote retirement savings have been passive — until recently. In December 2019, U.S. lawmakers passed the SECURE Act, which changed a few retirement regulations and introduced the Pooled Employer Plans (PEPs).

PEPs allow employers from different businesses to collaborate on joint retirement plans for their employees while not being jointly liable. This change in the law encourages small and midsized businesses to offer retirement plans they could not afford — or thought they could not afford — previously.

> With PEPs, employers from different businesses can provide joint retirement plans without being jointly liable

These employers also benefit from lower administrative workloads, fiduciary risks, and fees, and better access to market-leading investment options that often improve participant outcomes. These advantages now make the plans attractive to larger employers as well.

Similar plans are already available and successful in other developed countries, including the Collective Defined Contribution plans in the U.K. and the Netherlands and superannuation funds in Australia.[6,7]

The faster these kinds of regulations are adopted, the sooner the retirement savings gap will narrow. However, wider adoption of such regulations is unlikely unless small and midsized businesses find these changes more cost-effective compared with other offerings. For example, employers are likely to embrace PEPs if they more effectively:

- Provide timely communication to participants.
- Furnish investor-related data to retirement providers.
- Offer retirement providers access to payroll system data that can help facilitate plan administration.

Automation for improved retirement savings and financial literacy

Plan sponsors are tapping into technology to provide better advice and goal-oriented financial plans for their employees. As part of these efforts, an increasing number of employers now offer auto-enrollment and auto-escalation.[8] By enrolling workers into a retirement plan by default and bumping up their contributions annually, savings rates improve by 56% and retirement savings readiness can increase by 33%, according to the World Economic Forum.[9,10]

Retirement providers are also warming up to the benefits of new technology. The pandemic-induced lockdowns affected the ways services were being accessed and forced the industry to accelerate their digital transformation.[11] In 2020, U.S. regulators allowed retirement providers to accept e-signatures for plan documents — a pandemic-era necessity.

At the same time, these changes provided broader benefits. Firms have learned that automation makes it easier for participants to understand their finances, quickly switch between plans or providers, and find answers on their own. Cloud platforms and other technologies are scalable, more cost-effective to maintain compared with legacy infrastructure, and provide the required flexibility needed to innovate. Analytics on participant data provides accurate real-time insights and predictive analysis to plan sponsors. These can be viewed through intuitive and configurable dashboards and automated compliance reporting solutions.

The industry is also looking to artificial intelligence for technology solutions. Robo-advisors provide financial advice, investment recommendations, and portfolio management services. Chatbots offer personalized communication and greater self-service. These new options can also provide participants with financial education, intervene when clients try to reduce contributions, and help them make smarter decisions. At the back end, automated solutions streamline onboarding and back-office operations, while behavioral analytics is used to offer participants customized plans.

ESG funds likely to entice participants to save

At its core, investing is about money and returns, but those are not the only factors. A growing number of investors want to put their money in companies and efforts they believe in. They are confident they can get good returns while doing good. As a result, investment firms and regulators are now looking at how environmental, social, and governance (ESG) factors figure into the investment of retirement assets.

Current laws require plan fiduciaries to select investments based solely on performance factors. In 2021, the U.S. government is considering regulatory changes that would repeal these laws.[12] If passed, new regulations would allow firms to consider nonperformance factors, including ESG, when investing retirement assets. These rules could further expand the reach of ESG funds.

Availability of these funds, however, is not the sole factor. European regulators created rules to boost transparency into and accountability of ESG investments.[13] These regulations have increased trust in these types of investments. For example, nearly half of European investors and 25% of Australian investors consider ESG to be a top-three consideration when investing, according to a JPMorgan Asset Management survey. That figure is only 11% in the U.S.[14]

Offering ESG investment options would not only appeal to purpose-minded investors, but it could also help motivate some participants to save more toward their retirement. The Schroders 2021 U.S. Retirement Survey revealed that 37% of defined contribution plan participants were offered ESG-related investments by their employer.[15] Among those respondents, 9 in 10 invested in those options. Among those whose employers did not offer ESG options or the workers weren't sure, more than two-thirds said they would or might increase their contribution rate if they could invest in ESG funds.

> ESG investment options can help motivate employees to save more toward retirement

For their part, retirement service providers are adopting responsible investment principles and fully integrating ESG factors into their decision-making. This includes assessing metrics and obtaining ratings from global networks, such as MSCI or Morningstar, to shape an ESG-compliant product range. Often, decisions seen through an ESG lens can help identify risks that may not be captured by a performance-based analysis. This creates further opportunities to diversify portfolios and offer better returns.

End-to-end transformation to spread financial well-being

Despite the dire warnings about savings gaps, many factors — from regulations to technology — should make workers and firms optimistic about closing the savings gap.

Combined, these changes can significantly increase the retirement readiness and financial well-being of millions of workers through employer-sponsored plans.

Retirement providers that accelerate their digital transformation with an end-to-end perspective can connect more effectively with plan sponsors and build a competitive advantage. At the same time, providers can engage with participants in a more meaningful way. The result will be greater productivity and efficiency, efficient resource management, and an agile approach that improves time to market.

To keep pace with the accelerated transformation, retirement providers are partnering with technology firms to achieve benefits more quickly. These partnerships can automate regulatory monitoring and reporting through machine learning-based fraud analytics or use blockchain for complex recordkeeping and accounting.

Changes don't always have to be digital. But any new effort should create a need-based approach that serves a broad range of customers, from millennials to employees nearing retirement. Easier access to investments and better experiences can lead to an increased willingness to invest and a greater comfort with those decisions. And eventually, the world could finally see the growth in the retirement gap slow — or even reverse.

References

1. Investing in (and for) Our Future, Amish Gandhi, June 2019, World Economic Forum
2. Report on the Economic Well-Being of U.S. Households in 2019, May 2020, Board Of Governors Of The Federal Reserve System
3. Small Business Statistics, July 9, 2021, Small Business Trends
4. National Compensation Survey: Employee Benefits in the United States, Eugene Scalia, William W. Beach, Sep. 2020, U.S. Bureau of Labor Statistics
5. Report on the Economic Well-Being of U.S. Households in 2019, May 2020, Board Of Governors Of The Federal Reserve System
6. Collective Defined Contribution, Willis Towers Watson
7. Superannuation Is Possibly The Most Important Factor Of Wealth Creation, Tag Financial Group
8. Auto-Enrollment And Auto-Escalation: Right For Your Retirement Plan?, Beth Garner, Luanne Macnicol, May 2018, BDO
9. How America Saves 2020, 2020, Vanguard
10. The Impact of Auto-enrollment and Automatic Contribution Escalation on Retirement Income Adequacy, Nov. 2010, Employee Benefit Research Institute
11. Accelerating Digital Transformation for Retirement Providers in the Post-Pandemic Era, May 2021, Infosys
12. EBSA Drops Off ESG, Proxy Voting Response at OMB, Aug. 10, 2021, The National Association Of Plan Advisors
13. ESG regulations in Europe map a clear path for the US, May 3, 2021, Investment News
14. Australia Funds Embrace ESG More Than U.S. Peers, Survey Shows, Andreea Papuc, Feb. 10, 2021, Bloomberg Quint
15. ESG Options in 401K plans could lead to higher contribution rates according to Schroders survey, May 13, 2021, Schroders

Authors

Anupam Sarkar

Principal Consultant, Financial Services, Domain Consulting Group
anupam.sarkar@infosys.com

Sachin Askar

Senior Consultant, Financial Services, Domain Consulting Group
sachin.askar@infosys.com

Devendra Shrihari Joshi

Senior Consultant, Financial Services, Domain Consulting Group
devendrashrihari.j@infosys.com

Sharan Bathija

Infosys Knowledge Institute
sharan_bp@infosys.com

About Infosys Knowledge Institute

The Infosys Knowledge Institute helps industry leaders develop a deeper understanding of business and technology trends through compelling thought leadership. Our researchers and subject matter experts provide a fact base that aids decision making on critical business and technology issues.
To view our research, visit Infosys Knowledge Institute at infosys.com/IKI