

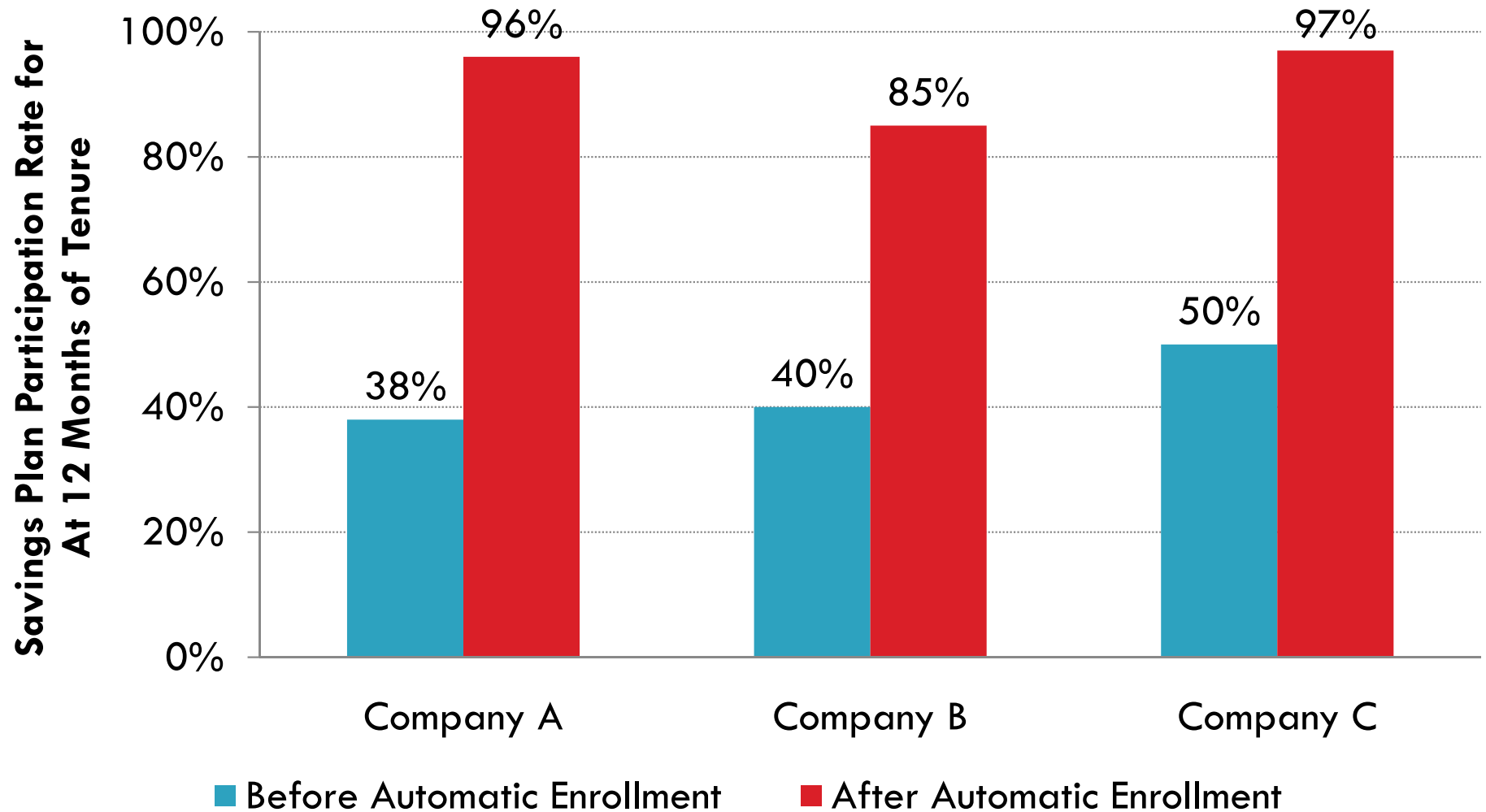
**THE POTENTIAL FOR MATCHING DEFINED  
CONTRIBUTION (MDC) DESIGN FEATURES  
IN PENSION SYSTEMS TO INCREASE  
COVERAGE IN LOW AND MIDDLE  
INCOME COUNTRIES:**

**LESSONS FROM BEHAVIORAL  
ECONOMICS**

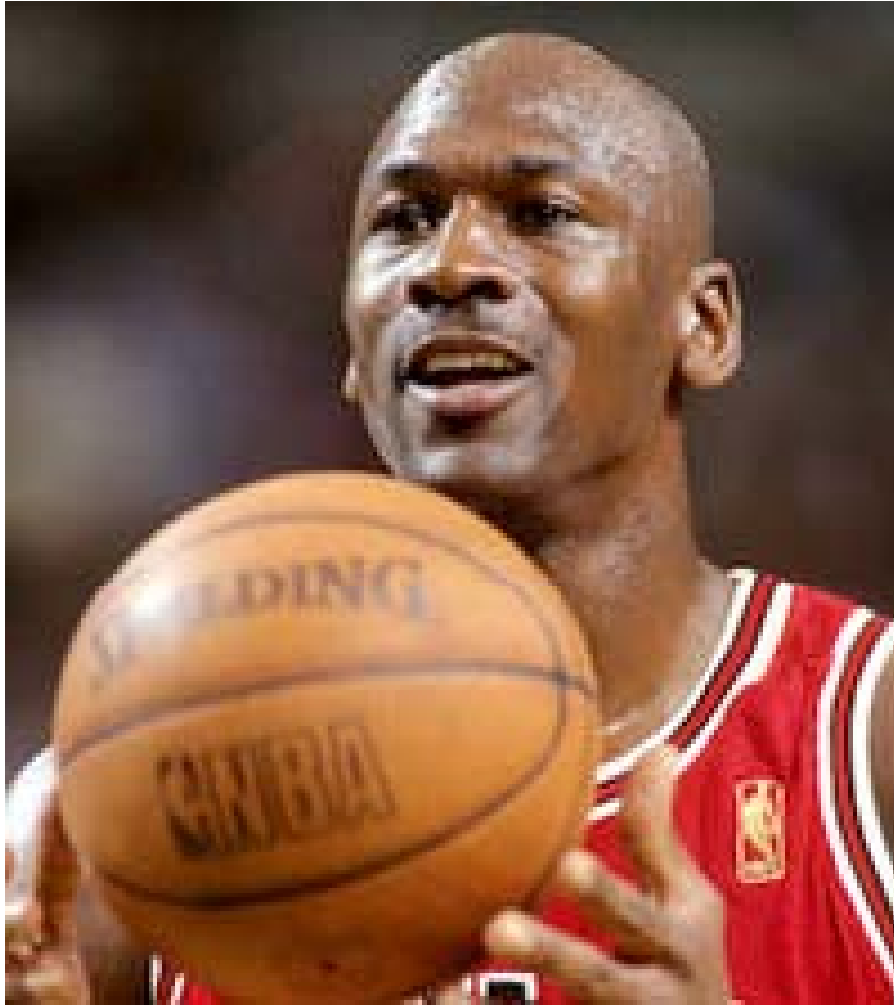
**BRIGITTE MADRIAN  
HARVARD UNIVERSITY**

The World Bank  
June 6-7, 2011

# Automatic Enrollment and Savings Plan Participation



# Michael Jordan



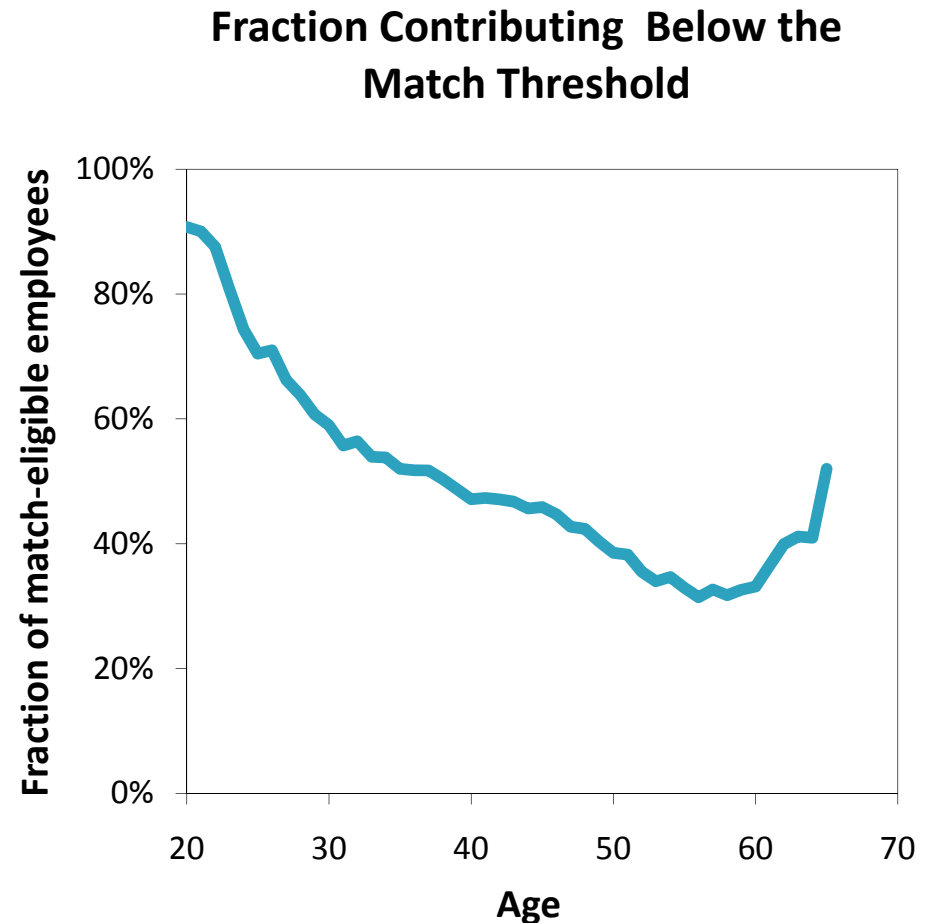
- ❑ 6x NBA champion
- ❑ 5x NBA MVP
- ❑ 14x NBA All-star
- ❑ 2x Olympic gold medal
- ❑ USBWA college player of the year
- ❑ Naismith college player of the year
- ❑ John R. Wooden award
- ❑ Etc., etc., etc., ....

# Why Does Automatic Enrollment Work So Well at Changing Outcomes?

- **Reason 1:** Most people **want** to save for retirement
  - Perceived need to save
  - Financial reward through employer match
  - Trust in the financial system
- **Reason 2:** Automatic enrollment **simplifies** doing what most people want to do

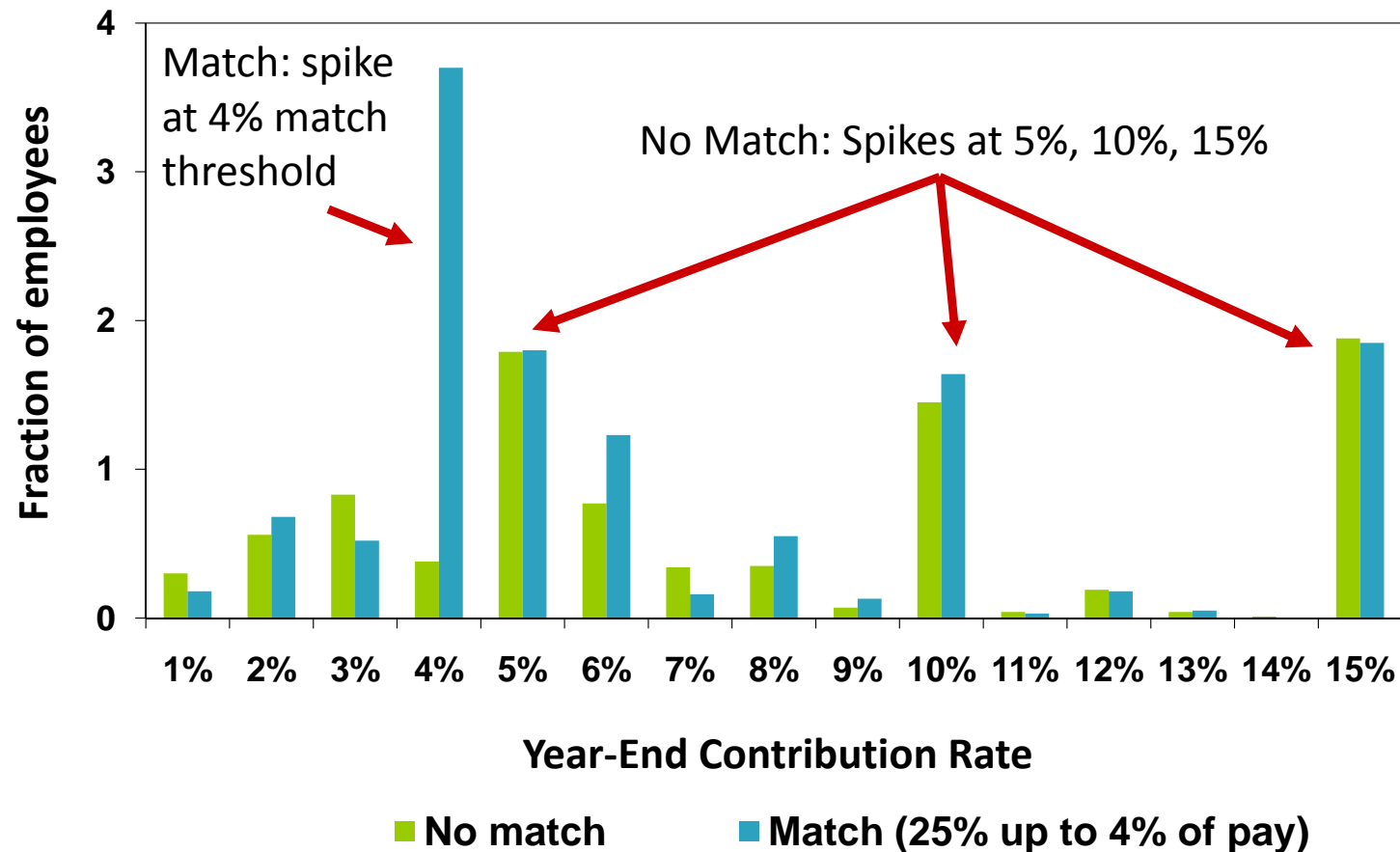
# How Well Do Financial Incentives Work in 401(k) Plans?

- Study of 401(k) plans at 7 companies
- All have a match
  - ▣ First dollar match rate: 20% to 100%
  - ▣ Maximum possible match: 0.75% to 6% of pay
- No automatic enrollment
- Many employees either do not participate, or contribute less than match threshold



# How Does the Match Matter?

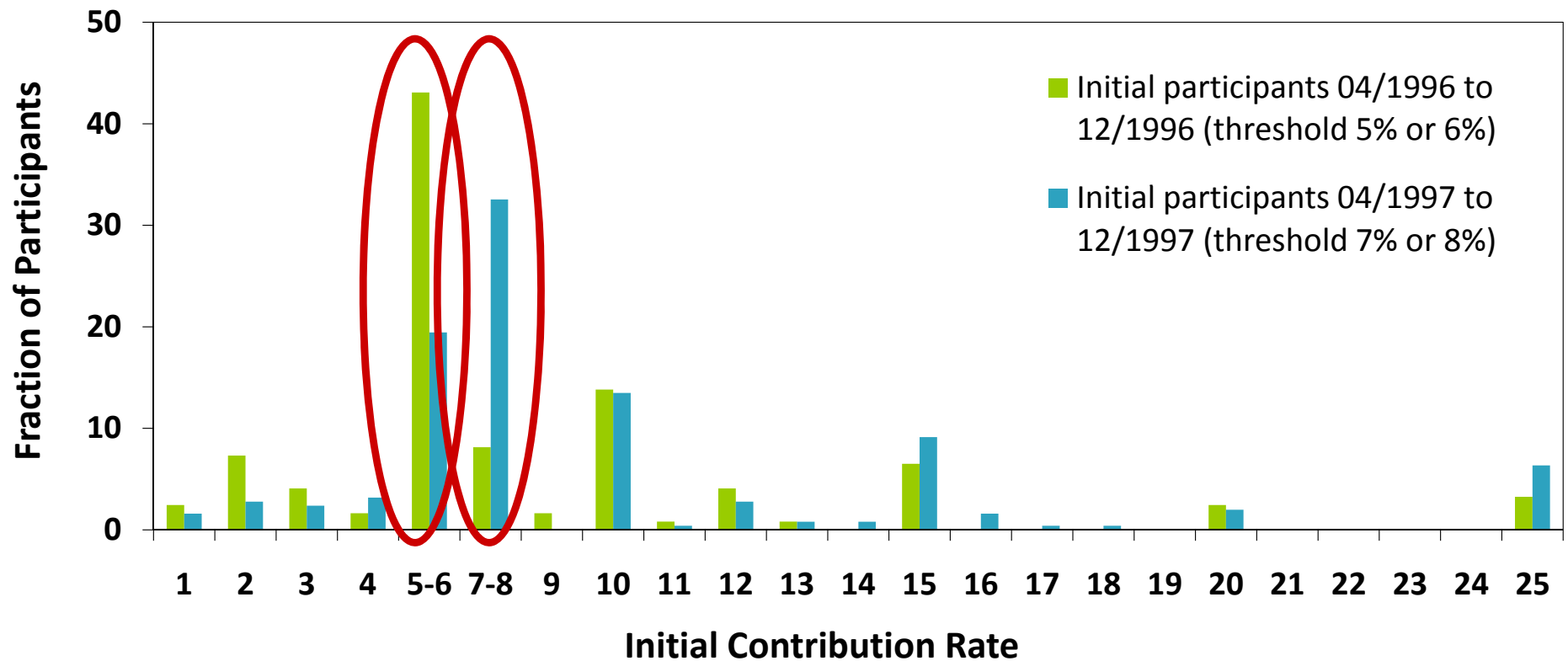
**The Distribution of Contribution Rates at a Firm that Added an Employer Match**



Source: Choi, Laibson, Madrian and Metrick (2006)

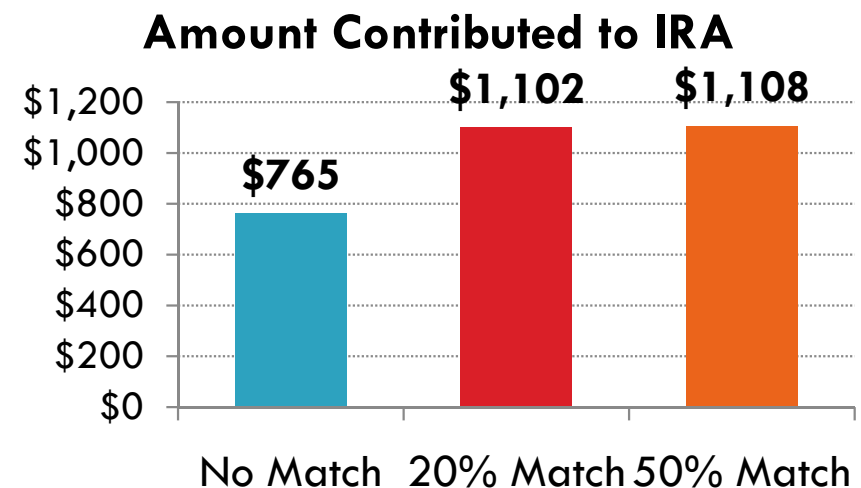
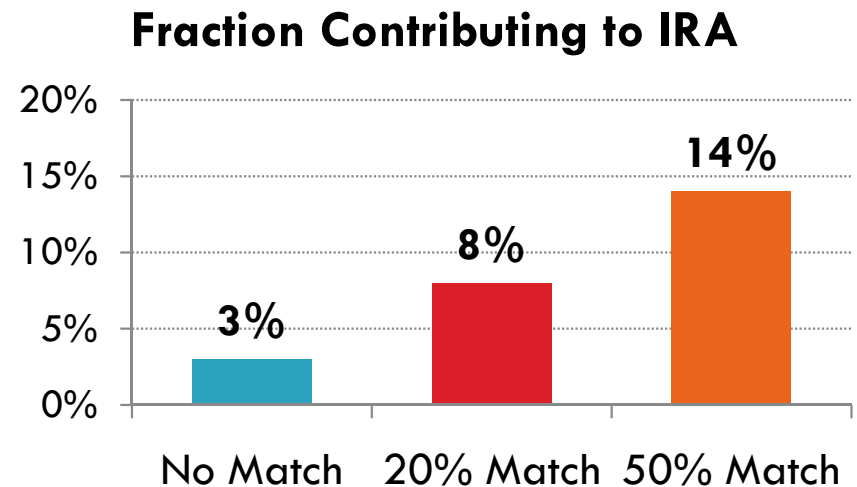
# How Does the Match Matter?

## The Distribution of Initial Contribution Rates at a Firm that Changed Its Match Threshold



# Matching and Savings in IRAs

- H&R Block Savings experiment
  - ▣ Tax filers offered opportunity to direct (part of) tax refund to an IRA
  - ▣ \$300 minimum contribution required
  - ▣ Randomized match: none, 20%, 50% on contributions up to \$1000



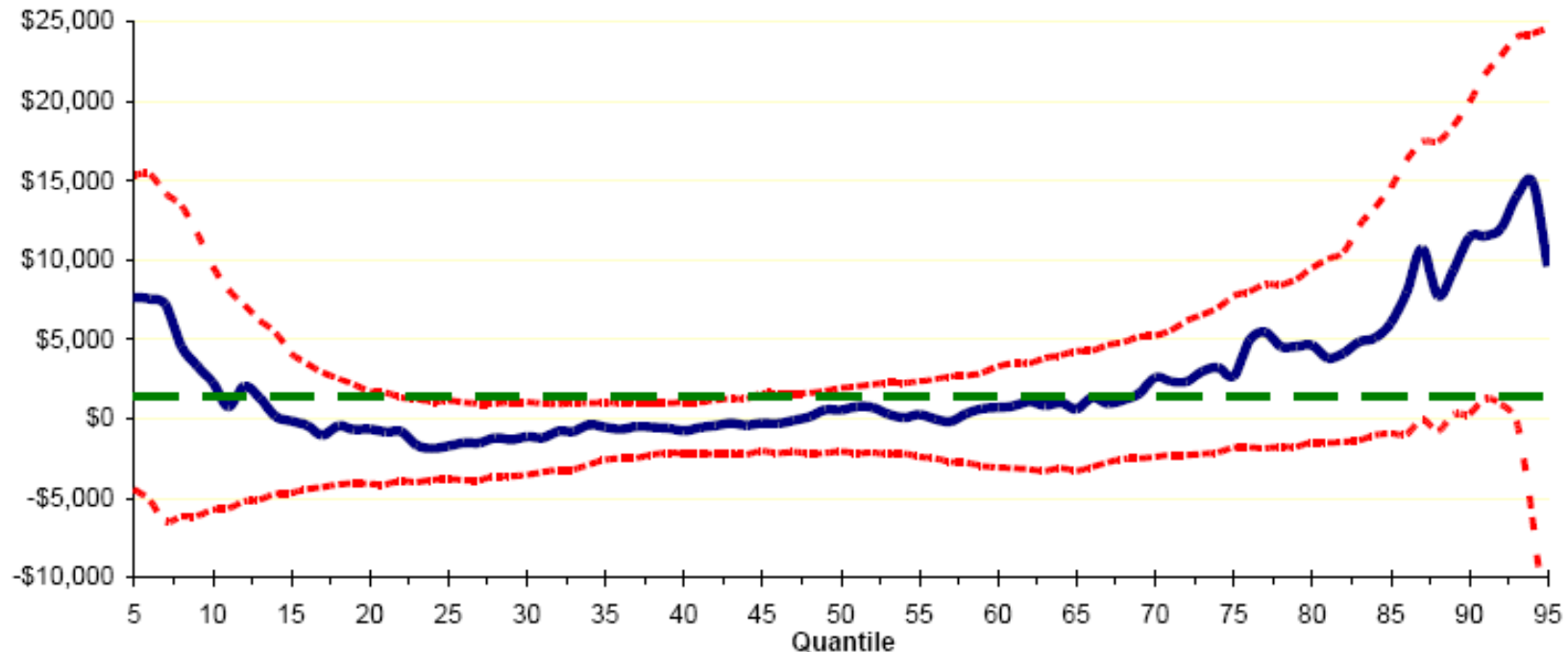
Source: Duflo, Gale, Liebman, Orszag and Saez (2006)



# Matching and Savings in IDAs

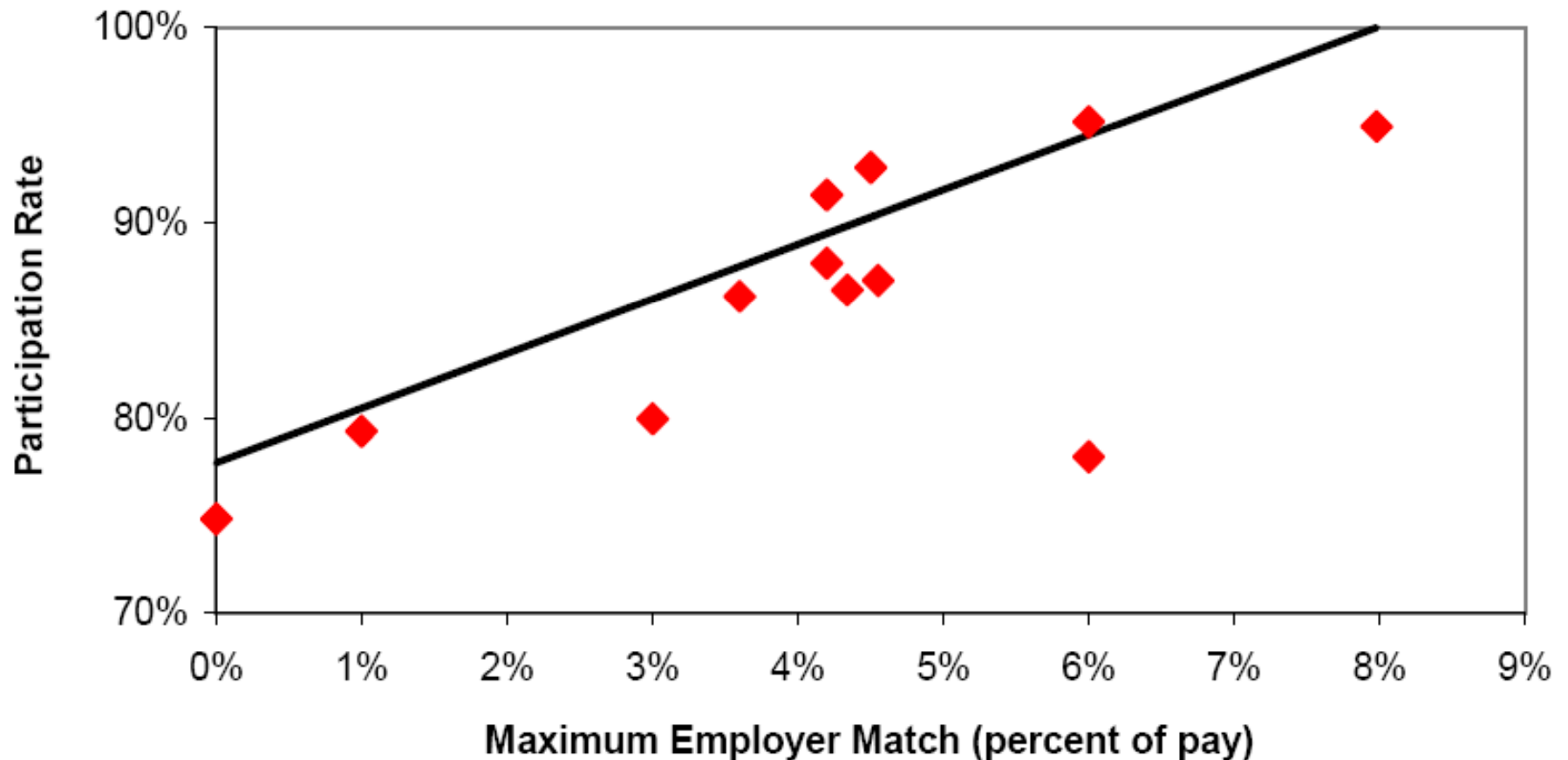
- Low income families interested in individual development accounts (IDAs) randomized into participation
- Match of 100% to 200% on contributions of up to \$750/year for three years

**Impact of IDA Participation Offer on Net Worth after Three Years**



Source: Mills, Gale, Patterson, Engelhardt, Eriksen and Apolstolov (2008)

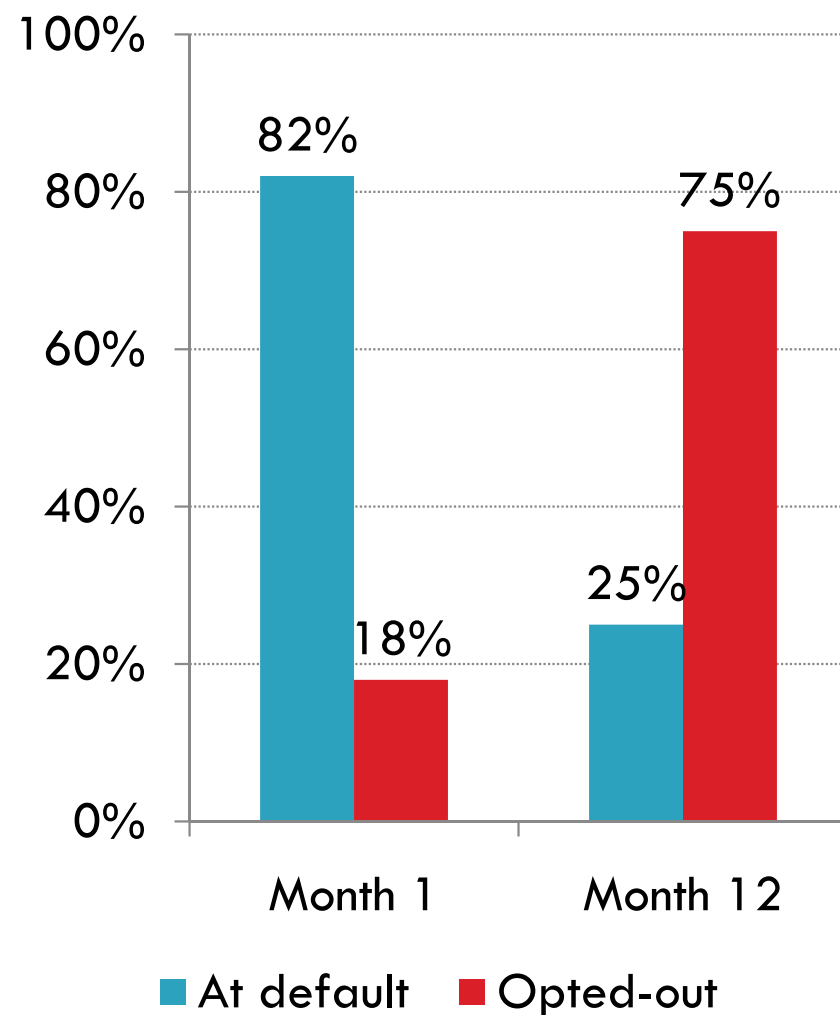
# How Much Does the Match Matter When Employees are Automatically Enrolled?



Source: Beshears, Choi, Laibson and Madrian, 2010.

# What If What is Easy and What People Want Are Not the Same?—A Bad Default

- Large UK Company
- Immediate automatic enrollment at 12% of pay
- 100% match on contributions of 12-18% of pay (no match on first 12% of contributions)
- 4% minimum contribution rate



Source: Beshears, Choi, Laibson and Madrian, 2011.

# How Do We Make Doing What People Want Easy to Do?



## **Change the product**

- ❑ Add a match
- ❑ Manage liquidity

## **Change the context**

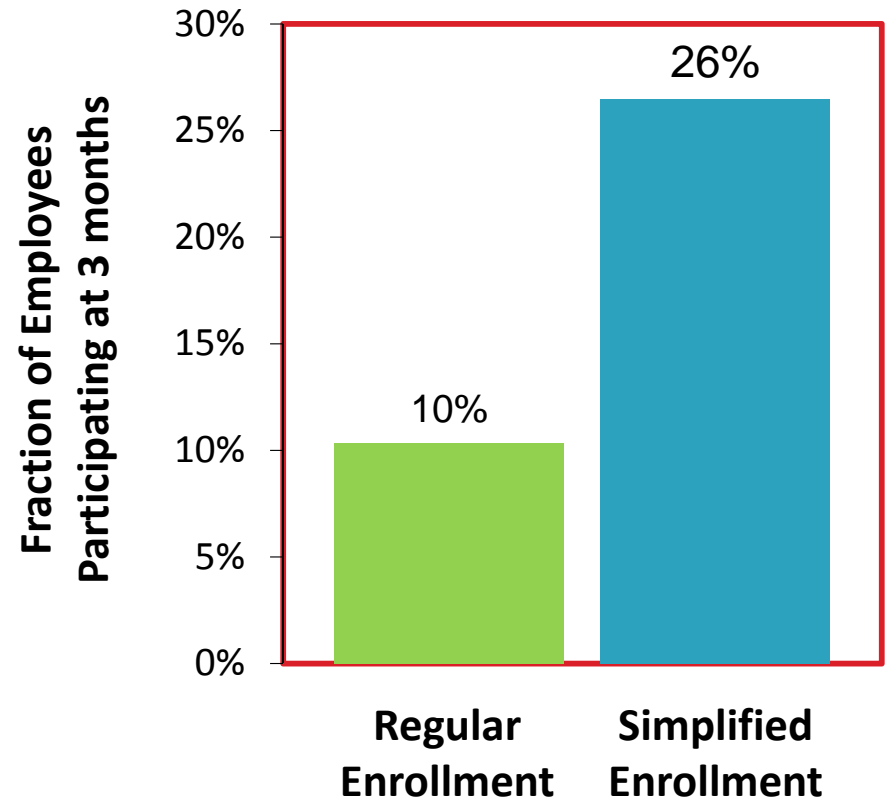
- ❑ Build trust

## **Change the process**

- ❑ Simplify
- ❑ Reminders
- ❑ Commitment devices
- ❑ Decision tools
- ❑ Social Support

# Simplifying 401(k) Enrollment and Savings Plan Participation

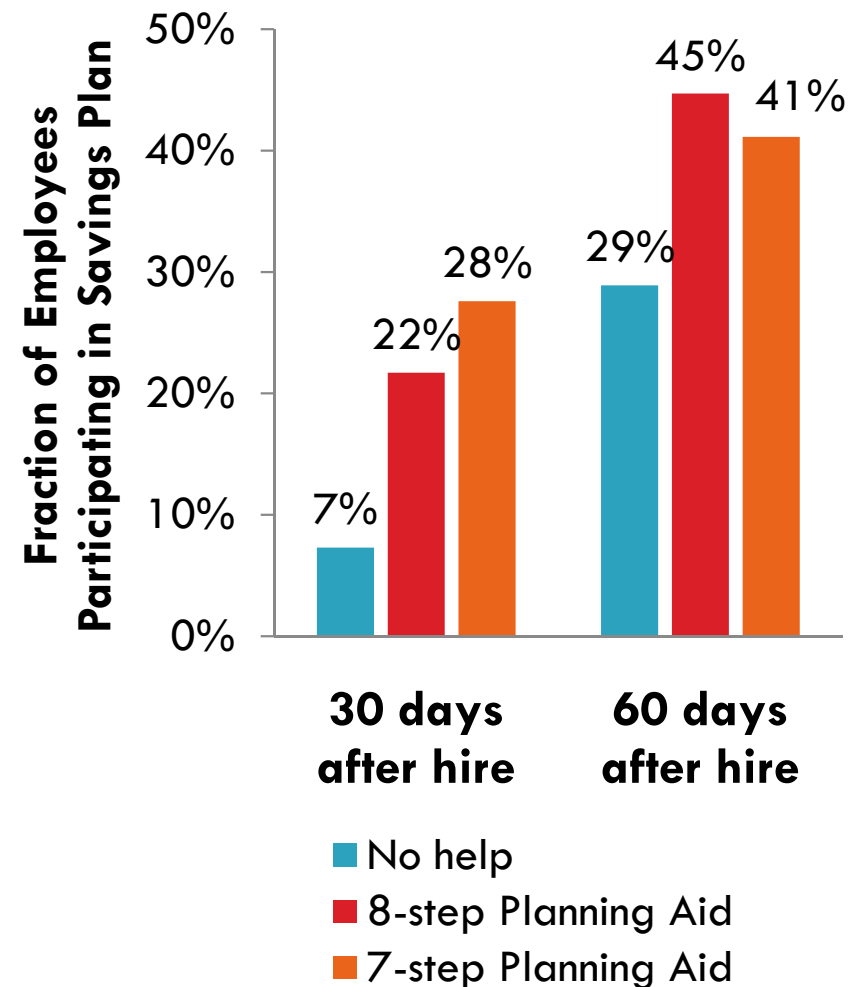
- 401(k) enrollment
  - ▣ Regular approach
    - ▣ Choose asset allocation
    - ▣ Choose contribution rate
  - ▣ Simplified approach
    - ▣ Pre-selected asset allocation and contribution rate
    - ▣ Simple check box



**Simplified enrollment process →  
16 pp. increase (260%)**

# Planning Aids and Savings Plan Participation

- Savings plan enrollment intervention
  - ▣ Control group: no special help
  - ▣ Treatment groups: one of two planning aid interventions
    - Outline steps to enroll
    - Time for each step
    - Tips

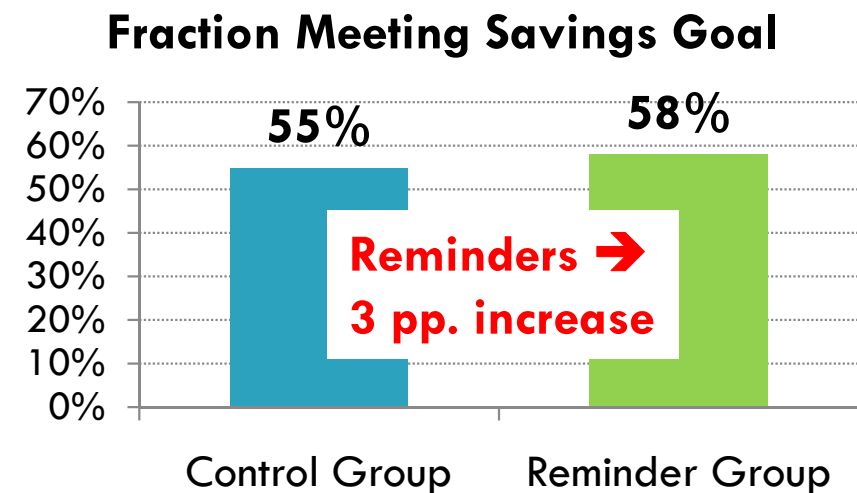
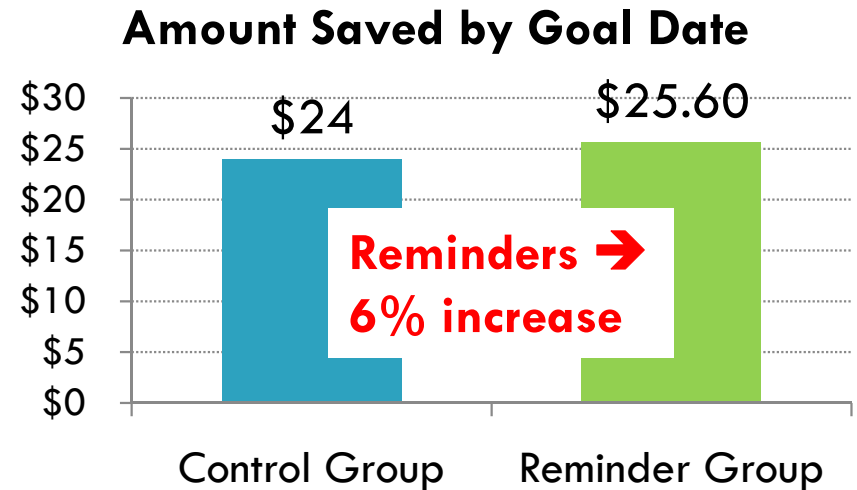


**Planning aids →  
12%-21% pp. increase**

Source: Keller, Keller and Lusardi

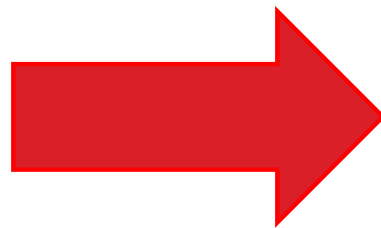
# Reminders and Savings Outcomes

- Savings experiments in three countries
  - ▣ Peru
  - ▣ Bolivia
  - ▣ Philippines
- New account openers set savings goals and make savings plan
- Treatment groups get periodic reminders (text message or letter)



Source: Karlan, McConnell, Mullainathan and Zinman (2011)

# How and When to Use the Tools of Behavioral Economics



- What is the job at hand?
- Which tools might help?
- What are the constraints?
- Given the constraints, which tool, or set of tools, is best?
- Some jobs require more than one tool and cooperation