nest insight

NEST Insight

Sidecar savings research trial

Vanguard

About the NEST Insight unit

The NEST Insight unit was set up by NEST Corporation to understand and address the challenges facing NEST's members, and the new generation of defined contribution (DC) savers. Our scale means that we're building up a rich store of data from a previously under-researched population, creating a platform from which to drive further insight about their needs and behaviours. NEST Insight works to ensure that these findings are available to the global academic, financial services and public policy communities. We do this through:

- rigorous quantitative and qualitative research, in collaboration with industry, academics and policy-makers
- a comprehensive programme of expert discussion events
- testing practical solutions
- a series of publications, briefing papers and online resources, complemented and promoted by a social media engagement programme.

Partnering with the NEST Insight unit

NEST Insight is comprised of a small core team within NEST Corporation. We believe that working in partnership enables us to deliver a more ambitious and impactful research agenda than would otherwise be possible. We look to work with organisations with similar research interests and organisational outlooks, who can bring their own research ideas, resources and funding to projects.

Contents

What's the problem we're trying to solve? 4

How does a lack of short-term savings affect your workers? 5

What's the solution? 8

The research programme 10

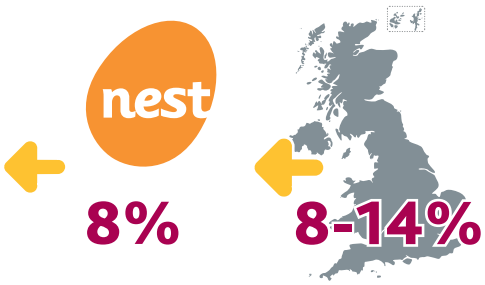
What's the problem we're trying to solve?

So far auto enrolment has been a huge success...

people are newly saving, or saving more, for their retirement[1]

was saved during 2016[2]

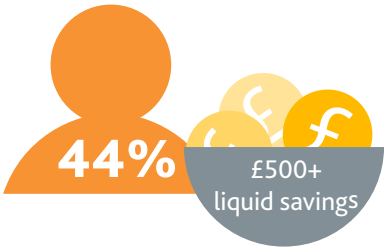
Opt outs have remained low at NEST[3] and throughout the UK[4]

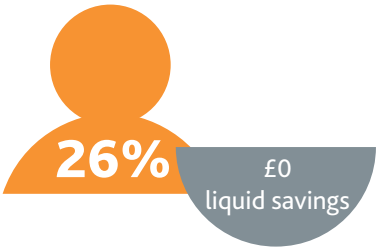


Since auto enrolment began in 2012, private sector saving has increased by **31%**[5]

However, whilst many low to medium earners are now building up meaningful retirement savings, some have little or no money put aside for emergencies.

In spite of initiatives to incentivise liquid savings, only 42 per cent of working-age adults have £500 or more on hand and 26 per cent have no savings at all.[6]





[1]The Pensions Regulator (2017)
[2]The Pensions Regulator (2017)
[3]NEST Corporation (2017)
[4]The Pensions Policy Institute (2016)
[5]The Pensions Regulator (2017)
[6]Money Advice Service (2016) and Department for Work and Pensions (2017)

How does a lack of short-term savings affect your workers?

Short-term financial shocks

When a high or unexpected cost occurs, it can have a severe impact on people who don't have enough 'emergency savings' put aside. We call this a 'financial shock'.

In order to cover the cost of a car repair, for example, people in this situation may have to:

cancel pension contributions to free up cash

borrow money from friends and family

reduce spending on essentials, such as food

take out a costly payday loan or use a credit card

not fix the car, which may mean they're unable to get to work and will incur a loss of earnings

Impacts on wellbeing and productivity

High-cost and unpredictable one-off expenses can cause acute short-term financial hardship for people whose disposable income after essentials is low.[7]

If not managed carefully, debts among low income groups can also lead to debt spirals which can cause acute financial stress. Any severe or persistent money pressures can have a detrimental effect on health, which can in turn affect productivity and earning capacity.[8]

Four in ten workers say money worries have made them feel stressed over the last year

A quarter (25 per cent) of workers say they have lost sleep over money worries

One in eight workers report that money worries have affected their ability to concentrate at work

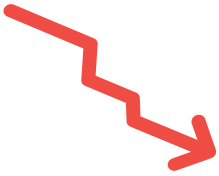
One in twenty workers (6 per cent) have missed work in the last year due to money worries[9]

[7]Money Advice Service (2016) and Packman, C. (2017)
[8]Money Advice Service, op cit; Chartered Institute of Personnel and Development (2017)
[9]Social Market Foundation (2016)

When employers were asked about the effects of poor financial wellbeing amongst workers:

54 per cent

said it's had an impact workers' behaviour



56 per cent

said it's had an impact on job performance

54 per cent

said it's had an impact on relationships at work

51 per cent

said it's had an impact on workers' relationships with management[10]

[10] Neyber (2017)

What's the solution?

This situation has, on occasion, led to suggestions that the defined contribution (DC) retirement system should be opened up to some degree of pre-retirement liquidity.

However allowing early access to retirement savings seeks to make a product designed for one purpose instead serve multiple purposes, which has negative consequences.

- DC accounts should be invested for most of a working life and have a relatively high risk exposure. Allowing access means an individual could withdraw money at a low point in asset value, leading to bad value for the member.
- The member may also withdraw a considerable amount of their money, leaving them with very little when they reach retirement.
- Administering early withdrawals from products not designed for that purpose creates potentially significant administration costs, which could reduce the value of the savings that are left.

Hybrid products and the sidecar model

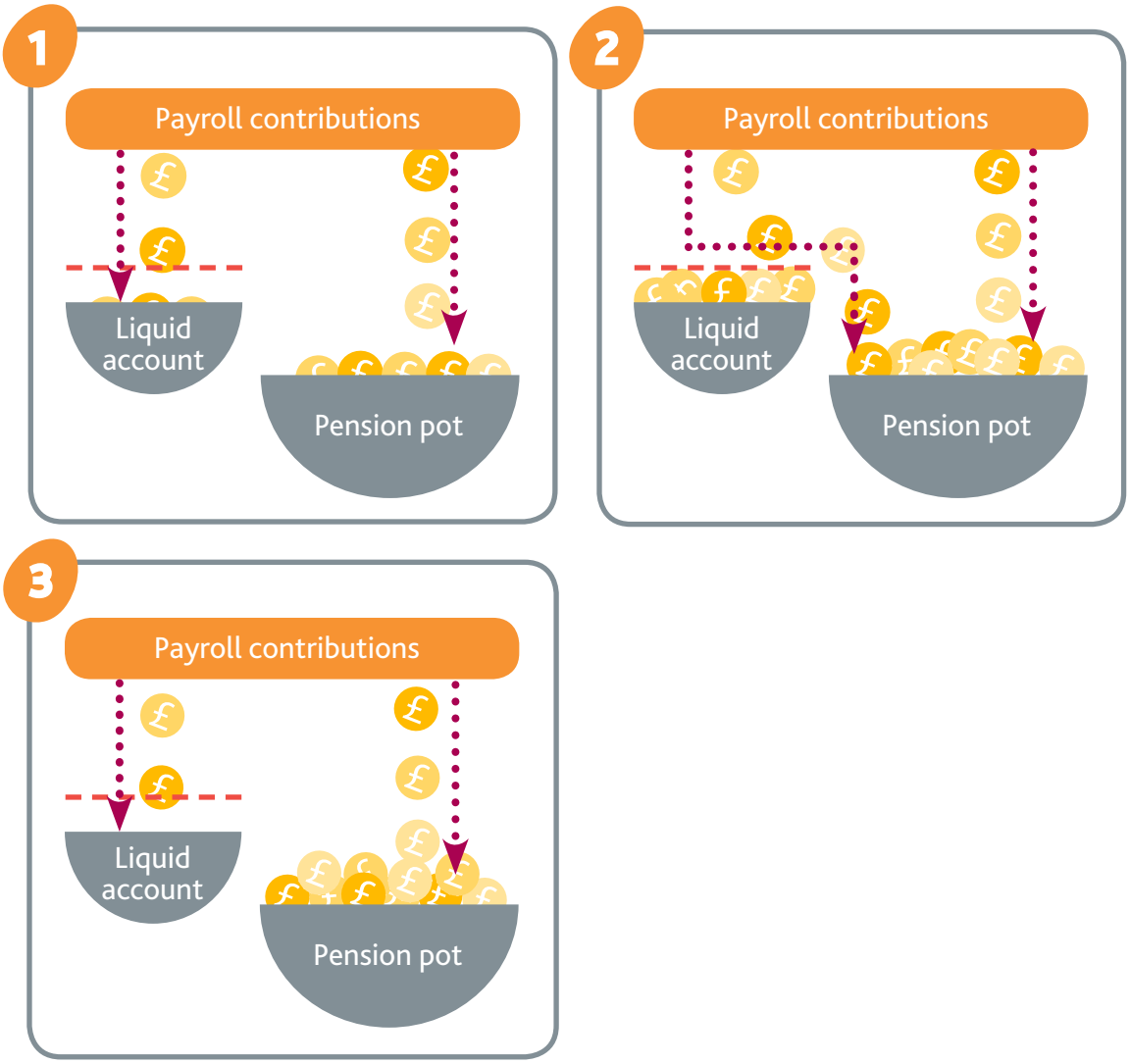
An alternative is to think about how to create an experience which fits with the saver's psychology and preferences, for example a solution that feels like a single 'product' but contains within it distinct 'jars' for different purposes.

US researchers have proposed a hybrid savings product which combines liquid 'emergency savings' in a sidecar account, with a traditional, illiquid, DC retirement savings product. The approach would allow the pension pot to remain locked up, and invested for the long term, while giving workers access to an amount of liquid savings.

How would the sidecar model work?

Contributions would be managed through a mechanism designed to create an optimal level of liquid savings, while also maximising long-term savings. This would be administered as follows:

1. Contributions paid into the combined account structure would at first be distributed between the liquid and illiquid accounts.
2. When the balance in the liquid account reaches a predetermined savings cap, all contributions would start 'rolling' into the illiquid retirement account.
3. If at any point the saver withdraws funds from the liquid account, and so reduces the balance to a level below the savings cap, future contributions would once again start being divided between the liquid and illiquid accounts.



- The product would be offered through payroll deduction in the workplace, using the idea of 'set and forget' to create a persistent flow of contributions to savings.
- Under this model, total contributions through payroll would be set higher than the auto enrolment minimum. This has the advantage of increasing the total amount saved, and therefore preserving the build-up of auto enrolment contributions, while potentially increasing retirement savings in the long term if the threshold is reached.
- It also has the attraction of keeping those new contributions accessible by creating an emergency buffer, helping to build short-term resilience.

The research programme

Why is NEST Insight conducting this research?

People with low to moderate incomes have not traditionally been the focus of the pensions industry so it's important to learn more about their needs and characteristics.

Many of NEST's members fall into this category and, with over 5 million members, our broad and unique data set puts us in an ideal position to conduct research.

The average income of a NEST member is around £18,300, approximately 80 per cent of the national median income. This is consistent with the fact that around 70 per cent of our members have incomes below that national median.

We also have evidence suggesting that a significant proportion of NEST's members have multiple sources of income and/or income that fluctuates considerably from month to month even as they maintain the employment relationship through which they were enrolled.

Understanding the needs of our members will help us solve the challenges they're facing and ensure the NEST pension scheme delivers good outcomes for them.

By working closely with others, and sharing the findings with global academic, financial services and public policy communities, our research could also help the industry understand the needs of the wider DC generation.

What are we aiming to find out?

The aim of this research is to examine whether creating a link between liquid and illiquid savings can create an appropriate balance of overall liquidity, and enhance the financial wellbeing of savers.

Since the concept has not been tested, we do not yet know whether the theory underpinning the concept would be borne out in practice.

- Would people take the idea up?
- Would they limit themselves to 'emergency' use of the sidecar account or would it become another current account?
- Would balances reach the threshold and lead to increased retirement savings?
- Would the availability of the sidecar lead to more optimal responses to financial emergencies, such as reducing reliance on high-cost debt?

Stage one: formative phase

The first phase of our research is already underway. We're addressing a range of design questions before the field trial takes place by reviewing existing evidence, analysing data on target populations and conducting qualitative research with focus groups. This research will establish:

- Which groups of workers have the greatest need for liquid savings?
- How are these groups represented in the NEST member population?
- How attractive would people in these groups find a workplace savings product that combines liquid and illiquid savings and where contributions are made via payroll deductions?
- What features would be attractive to workers? For example voluntary enrolment, tax relief, financial incentives, or flexibility of contribution level.
- What's the optimal level at which to set the savings cap and contribution rates? How does this differ for different groups of workers?

Stage two: field experiment

During stage two we'll test the combined liquid and illiquid structure with workers of a number of large UK employers.

The trial, which will be a longitudinal study, will be designed to test a range of factors, including:

- take up rates for the liquid account
- levels of savings within the liquid account
- impact on participants' financial well-being.

For each participating employer we'll run a control trial of the combined account structure with a group of randomly selected workers. This will involve randomising the participant population of each employer into two groups. Each group would be offered the same overall level of savings and employer match:

- **Control group**: would see 100 per cent of contributions would flow into their illiquid retirement account. This may be consistent with the existing workplace pension arrangements in place for these workers.
- **Combined account group**: would see contributions split between a liquid account and an illiquid retirement account.

For each employer, we'll use payroll data and management information from the pension and liquid savings providers to monitor the initial and longer term participation behaviours and savings rates of the two groups.

We'll also track the groups through a series of re-contact surveys over a longitudinal timeframe. The surveys will include wellbeing measures selected in the stage one research to understand whether their financial wellbeing and likely retirement outcomes differ according to the availability of a liquid account.

How your organisation can get involved

Working closely with Harvard University and the Money Advice Service, NEST Insight will start trialing the concept in 2019.

If you'd like to find out more information about the trial and how your organisation can take part, please contact Matthew Blakstad:

email: **matthew.blakstad@nestcorporation.org.uk**
phone: **020 3056 3795**

References

Department for Work and Pensions (2017) *Family Resources Survey.* London: Department for Work and Pensions

Money Advice Service (2016) *UK Financial Capability Strategy for working-age people.* London: Money Advice Service

NEST Corporation (2017) unpublished scheme member data as at September 2017.

Neyber (2017) *The DNA of Financial Wellbeing.* London: Neyber Ltd.

Social Market Foundation (2016). *Working well: how employers can improve the wellbeing and productivity of their workforce.* London: Social Market Foundation.

The Pensions Policy Institute (2016) *The impact of automatic enrolment in the UK as at 2016.* London: The Pensions Policy Institute

The Pensions Regulator (2017) *Automatic enrolment commentary and analysis: April 2016 - March 2017.* London: The Pensions Regulator

The Pensions Regulator (2017) *Automatic enrolment passes the eight million milestone* http://www.thepensionsregulator.gov.uk/press/automatic-enrolment-passes-the-eight-million-milestone.aspx, accessed 10/08/2017

Packman, C. (2017) *Savings for the Future: Solving the Savings Puzzle for Low Income Households.* London: Toynbee Hall

Contact us
insight@nestcorporation.org.uk

To find out more visit our website
nestinsight.org.uk

p50267v3 10418-2 10/17