



A WAY TO ENCOURAGE SAVING

A timely reminder may be the key to increasing the personal savings rate.

Why don't people save? That's a perplexing question, since there's ample evidence that without savings, people have a hard time achieving their financial goals. It's also a question many have sought to answer—and to remedy—without notable success.

In "Getting to the Top of Mind: How Reminders Increase Savings," Dean Karlan and his colleagues at the Center for Retirement Research at Boston College report on one very specific approach to increasing the amount people save and the likelihood they will reach their financial goals. What the authors tested was the effectiveness of timely reminders to encourage saving, especially reminders that linked the saving to a specific goal.

Karlan's underlying thesis is that even people who are attentive to paying their bills and meeting their current financial responsibilities may consistently ignore their future needs. This failure isn't the result of a willful lack of self-control, the Karlan team contends, but rather of inattention. That is, rather than rejecting saving in favor of having more to spend now, people simply don't think about what they'll need in the future.

Failure to anticipate, and therefore to save, often has serious consequences. In this case, non-savers must borrow, which increases the cost of achieving their goals. When borrowing is not possible, they must go without. The more important and costly the goal, the greater the problem becomes.

ENCOURAGING SAVING

The authors of the study also point out certain successes with goal-oriented saving. In developed markets, for example, saving for retirement has been enhanced by requiring participation in an

→ A QUICK LOOK

- In a recent study, people saved 6% more when they were reminded to save.
- Goal-specific reminders are twice as effective as general reminders.
- Savers can be encouraged to increase the rate at which they contribute to a salary deferral plan.
- Reminders to save or to save more can be delivered efficiently in online statements or through a range of electronic devices.

employer plan and by offering opt-out automatic enrollment programs. Systematic savings plans, where money is debited directly from a paycheck or bank account, have shown similar positive results. And, in less sophisticated financial environments, a deposit collection service that contacts savers individually for their contribution works too.

What happens, though, when someone must take the initiative to make regular deposits? If the Karlan theory of benign forgetfulness has any credence, those deposits are likely to be erratic.

TESTING THE THESIS

To test their hypothesis that (1) regular reminders increase savings and (2) reminders that mention a specific goal boost savings more than general reminders, the Karlan team designed three parallel but not identical field studies in collaboration with local banks in the Philippines, Peru, and Bolivia.

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In each case, the bank divided new account holders into two randomly selected groups and sent savings reminders before the due date to the test group but not to the control group. Two of the three banks also sent reminders to a separate, randomly selected group of account holders who were late making their deposits. The tone of the messages from all three banks was sometimes positive—what would be gained by saving—and sometimes negative—what would be lost by not saving. The positive and negative messages were also assigned randomly.

The study showed that—customers who received monthly reminders saved 6% more than those who did not. The results suggest that the timing and the content of the messages not only got the savers' attention but also produced the desired action. Analysis of the responses also indicated that reminders highlighting a specific goal were twice as effective as a general reminder. In addition, reminders that arrived regularly—before the date the deposit was due—were also more effective than other types of incentives, such as gifts for opening an account or making a deposit.

WIDER HORIZONS

Are Karlan's findings, which are based on limited field studies of short-term savers in three developing markets, relevant for encouraging saving in other environments? The answer, on two levels, is yes.

First, the study offers a new way of thinking about the failure to save. When viewed as the result of limited attention to future needs, rather than lack of self control, failure to save may be remedied, it's

reasonable to conclude, by maintaining top-of-mind awareness of the benefits of saving.

For example, once someone has taken the step of signing up for a payroll deduction retirement savings plan, reminders should be a valuable tool in boosting the rate at which he or she agrees to contribute. The reminder might be as simple as prompting an annual 1% increase in the savings rate or as detailed as a graphic displaying the projected accumulations for different contribution rates.

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Second, widespread use of online statements and other electronic messages to reach account holders simplifies the delivery of timely, cost-efficient, and goal-centric reminders. The messages may be ignored. But even a modest increase in the rate at which people save justifies the time to craft and deliver these messages.

The messages themselves might follow a predetermined schedule, linking increased long-term savings to specific retirement goals. Alternatively, the messages might be more individualized, based on the age, account balance, or contribution rate of the participant.

One observation about this research is warranted, however. Since the savers in the study had taken the initiative to open an account, they presumably had a positive view of saving. There is no way to tell from Karlan's research if reminders would work for those who are not predisposed to save and have not signed up for an automatic saving plan.

The study, titled "Getting to the Top of Mind: How Reminders Increase Saving," was written by Dean Karlan, Margaret McConnell, Sendhil Mullainathan, and Jonathan Zinman. It was published in April 2010 by the Center for Retirement Research at Boston College and funded by a grant from the US Social Security Administration as part of the Retirement Research Consortium.