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Are Millennials on Track for a Secure Retirement?

Many under age 40 understand the need to save for retirement but juggle competing financial needs; auto features are helping.

Reported by ED MCCARTHY

MILLENNIALS—THOSE BORN BETWEEN 1981 AND 1996—are now the largest demographic group by age in the U.S. The oldest Millennials have reached age 41, which lands them in the decade when adequate retirement savings become more important. So how well are they doing with their retirement plans?

Multiple Challenges

Angie O'Leary, head of wealth planning with RBC Wealth Management–U.S. in Minneapolis-St. Paul, says that Millennials have multiple financial worries that can create retirement-savings obstacles. She cites a recent RBC survey of Millennial HENRYs—short for "high earner, not rich yet"—which found that this cohort's finances are often a juggling act. Besides trying to save for retirement, they're concerned with housing costs, starting families (or paying childcare expenses and starting college funds if they already have children), paying back their own college loans or taking on new debt to pay for graduate school. "Those are all very real issues that Millennials are dealing with," says O'Leary. "I think the good news is our research shows that most of them understand that saving for retirement is important. They may not understand if they're saving enough, but they do understand the importance of saving for retirement."

Mark Smrecek, senior director, retirement, Willis Towers Watson in Chicago, cites similar concerns. According to a Willis Towers Watson survey, nearly 7 in 10 employees under 40 are facing at least one retirement risk, such as under-saving for retirement, borrowing from retirement funds or withdrawing retirement funds. Nearly 4 in 10 employees under age 40 save less than 5% of their pay and would like to save more. "When these employees were asked what is keeping them from saving more, they reported prioritizing paying debts, saving for other reasons and paying for housing as the top three reasons for under-saving," says Smrecek.

High debt levels are a particular burden for this cohort. Forthcoming Alight research shows that 40% of Millennials feel that their level of debt is “ruining their lives,” according to Rob Austin, vice president, head of research at Alight in Charlotte, North Carolina.

Recent economic events, particularly the ongoing surge in inflation, also weigh on Millennials’ outlook, according to an April 2022 Voya Financial study . The survey notes that while Millennials were “often coined a generation likely to spend their hard-earned money on travel or entertainment,” they now express the most concern of any generation about the long-term impact of COVID-19 and inflation. Sixty-eight percent of Millennials agree or strongly agree that because of inflation, they are not able to pay down debt as quickly as they want to, according to Chrisinda Mowrer, vice president, customer success at Voya Financial in Atlanta. Additionally, 77% of Millennials agree or strongly agree that inflation has made them more aware of the need to save more for emergencies or unexpected events.

Autopilot to the Rescue

Given the pressures on Millennials’ finances, it wouldn’t be surprising if they postponed saving for retirement until they thought they could better afford to do so. But that delay could significantly reduce the value of compounding in their retirement plan balances. “When you’re not confident about your everyday finances, it can be really hard to visualize the future and allocate savings toward it,” observes Kirsten Hunter, vice president, thought leadership with Fidelity in Boston. “This is where auto-solutions have been particularly helpful in recent years to overcome some of this human inertia by getting people enrolled and saving in retirement accounts earlier.” In Fidelity’s experience, 90% of employees who are automatically enrolled in their employer’s plan do not opt out, Hunter adds.

Dave Stinnett, principal, strategic retirement consulting with Vanguard in Malvern, Pennsylvania, believes that Millennials have benefited significantly from modern plan-design best practices that many plan sponsors have adopted. These practices have helped in three specific ways, says Stinnett. First, auto-enrollment reduces the risk that an employee will choose not to participate in the plan. Second, default contribution rates and automatic escalation features lead to higher savings. The availability of broadly diversified, age-appropriate, professionally managed portfolios in the plan is the third benefit. As a result of these plan features, the retirement savings part of the financial decision calculus “has been made very easy for them to achieve the optimal results,” says Stinnett.

Contribution and Portfolio Decisions

According to Alight's 2022 Universe Benchmark report, most Millennials' contribution rates are sufficiently large enough to benefit from the company match. Only 22% are below the match threshold, while 32% are at the threshold and 46% are above it.

Target-date funds capture the bulk of Millenials' contributions, although reported percentages vary. The Millennial cohort has about half of its assets in TDFs, according to Graham Shippy, a Nationwide spokesperson in Columbus, Ohio, with roughly another 20% in U.S. large-cap funds. Hunter and Stinnett report Millennials' TDF-adoption rates at about 70% and 71%, respectively. According to Alight's 2022 data, Millennials' investments focus on growth. The Alight report notes Millennials have 51% of their assets in TDFs, with large-cap U.S. equity funds in second place at 21.8%. Equities account for 87% of balances; fixed income has 13%. In comparison to other age groups, Millennials hold more equities than older participants in Gen X (79% equity, 21% fixed income) and Baby Boomers (65%, 35%), which Alight attributes to a combination of Millennials' increased use of TDFs and long investing time horizon. That same logic holds for Gen Z, which has an allocation of 91% equity, 9% fixed income.

Growing interest in environmental, social and governance options also likely affects Millennials' investment decisions and preferences for retirement plan fund choices. The Natixis Global Survey of Individual Investors reports that 46% of U.S. Millennial survey participants are currently invested in ESG funds and another 42% are interested in ESG. "One of the things we see is that there's an interest in having ESG types of investments or investments that align with their values," says David Goodsell, executive director, Natixis Center for Investor Insight in Boston. "They see that as something that would motivate them to increase their contributions or begin participating in a plan. So, they see that personal connection as really important to their participation."

Effective Communications

Sources differed on whether plan sponsors should modify their communications practices to reach Millennials more effectively. Shippy says that in Nationwide's experience, employers communicate with Millennials just as they do with their other employees, using email as a primary communication vehicle. The communications delivery mix might be changing, though, he says: "We're starting to see some early research and data about Millennials and Gen X and the desire to go to peer-to-peer and social networks for financial advice, and we believe that this type of outreach through influencers could be an emerging trend in communication. We also know Millennials with $100,000 in investable assets or greater are actively seeking advice from financial professionals, with 66% already working with a financial adviser.”

Sources for this article emphasize that participant communications need to take a holistic financial wellness approach and go beyond solely emphasizing the need for retirement savings. “If you’re only talking about saving for retirement, for example, to all of those folks who are struggling with the more fundamental elements of financial wellness, like budgeting, emergency savings, managing student debt, you’re probably not going to engage them very well, because retirement might not be their top priority or where they’re able to spend their energy right away,” says Hunter.

Doing Well, Overall

Despite the obstacles to Millennials saving adequately for retirement, Stinnett says that Vanguard “largely sees encouraging things” when they consider the cohort. For starters, plan participation rates are good. Among Vanguard’s 1,700 plans and 5 million participants, employees under age 35 have a 75% participation rate, an increase from 62% in 2017. That rate jumps to 92% in plans with auto-enrollment. Over the same period, the average savings rate for this group increased from 5.9% to 6.3%. Finally, the extensive use of TDFs helps avoid the problem of an excessively conservative or aggressive asset allocation. “These three things together, I think, create a lot of optimism for Millennials,” Stinnett concludes.