Auto-enrollees don't 'borrow to save,' researchers say

By Editorial Staff *Thu, May 30, 2019*

In a departure from their preliminary findings of three years ago, economists found that middle-income government workers didn't increase their debt levels after being auto-enrolled in the Thrift Savings Plan.

Middle- and low-income American workers often say that they can't afford to save, so questions have arisen about the effects of auto-enrolling them into defined contribution and defaulting them into saving 3% or more of their pre-tax pay.

Would they reduce their spending by 3% to offset the new savings? Or would they maintain the same standard of living by borrowing money through credit cards, home equity loans or other forms of credit? In other words, could auto-enrollment leave certain people worse off than they were without it?

A group of Ivy League university researchers has been studying the savings and borrowing habits of a group of participants in the federal Thrift Savings Plan (TSP) workers for several years, in hopes of answering those questions. Their most recent **report** shows "that automatic enrollment has no impact on the probability of financial distress."

The authors took advantage of a natural experiment, made possible by the adoption of auto-enrollment in the TSP program for civilian employees of the U.S. Army in 2010. They compared the savings and debt outcomes of participants hired in the year before the inception of auto-enrollment with the outcomes of participants hired in the first year of auto-enrollment. The participants' average annual salary was about $55,000.

"Automatic enrollment in the TSP at a 3% of income default contribution rate is successful at increasing contributions to the TSP," the authors write. "At 43-48 months of tenure, this policy raises cumulative contributions to the TSP by 4.1% of first-year annualized salary. We find that little of this accumulation is offset by increased debt excluding first mortgages and auto debt, and there is no impact on credit scores or debt in third-party collections."

The paper, "Borrowing to Save? The Impact of Auto-Enrollment on Debt," was written by John Beshears (Harvard Business School), James J. Choi (Yale School of Management), Brigitte C. Madrian (Brigham Young University), David Laibson (Harvard), and William L. Skimmyhorn (College of William & Mary).

These new results update the results reported in an October 2016 version of the same paper. At that time, they wrote, "Automatic enrollment in the TSP at a 3% of income default contribution rate is extremely successful at increasing contributions to the TSP at the left tail of the distribution while leaving the middle and right of the distribution unchanged." By "left tail," they meant lower-income participants.

"At four years of tenure," they added, "this policy raises cumulative contributions to the TSP as a percent of first-year annualized income by 5.2% at the mean, 13.9% at the 25th percentile, and 21.5% at the 10th percentile. However, once crowd-out along debt margins is considered, the effect of automatic enrollment is considerably more modest."