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Which Factors Influence 401(k) Investing?

Below are the characteristics found to have a high correlation with equity investing in defined contribution plans.

• **Marital status.** Married couples tend to invest more in equities, perhaps because the security of two potential wage earners allows for more risk taking with investments.

• **Education level.** Households headed by someone with no high school degree allocate 10 percentage points less to equities.

• **Have defined benefit pension plan in addition to 401(k).** The correlation between likelihood to invest in equities and whether a household is also covered by a traditional pension in addition to a 401(k) is positive.

For every $10,000 in present value within a traditional pension, a household allocates 0.05 percentage point more to equities. Participants in defined benefit plans have a more secure base of retirement income and therefore can afford to take more risk with their supplementary savings.

• **Income.** The correlation between the likelihood of investing in equities and household income is surprisingly weak—for every $1,000 in household income, the equity share increases by 0.002 percentage point (for instance, 0.2 percentage point for $100,000 income).

One explanation is that wage earners at lower income levels will receive a relatively higher share of their retirement income from Social Security—a guaranteed benefit—and thus are willing to take on more risk with the 401(k) portion of savings than usually thought.

• **Personal planning horizon.** Households that report planning horizons of at least a few years allocate 5 percentage points more to equities.

• **Age.** There is a negative but not a linear relationship between age and percentage of assets invested in equities. For example, the average household headed by a 55-year-old allocates 6.5 percentage points less to equities than one headed by a 25-year-old, but only 1.5 percentage points less than a household headed by a 35-year-old, and 8 percentage points more than one headed by a 70-year-old.

• **Union membership.** Households headed by union members are more likely to avoid equities altogether. Could union membership foster distrust toward management that plays out in avoiding stock ownership, to the detriment of union members' financial well-being?

• **Public vs. private sector.** Those working in the public sector allocate 4 percentage points less of their retirement accounts to equities. This is somewhat surprising given the relative security of public-sector jobs. But people working in the public sector might be inherently more risk-averse. They tend to retire earlier, so they have shorter investment timeframes, which tends to discourage equity investment.

• **Large vs. small company.** Households headed by those who work for large companies are less likely to invest 100 percent of plan assets in equities. This could be because those who seek employment at large, stable companies might be more risk-averse than those who work for small companies. Or it might mean that large companies are doing a better job of providing investment advice.

• **Health status.** Those in poor health are more likely to avoid equities. That's likely because the healthy feel more certain about their future earnings potential and thus take on more risk. Also, they might not need to keep savings in relatively safe investments because a hardship withdrawal is less likely for them.

• **Risk tolerance.** Compared with households that report lower tolerance for risk, highest-risk-tolerance households allocate almost 20 percentage points more to equities.

Source: Watson Wyatt Worldwide