Are Peer-to-Peer Comparison Tools the Answer to America's Retirement Savings Crisis?

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Everybody knows they need to save for retirement, but knowing and doing are two different things. Everything else seems to come first, the house, college for the kids, just about anything. How to get people to save for retirement is the big question that financial gurus are desperately trying to answer.

One of the newer ways to incent people to save is peer comparison tools. Basically these tools allow people to compare where they are in savings, to people who are somewhat like them in terms of factors like income and age.

The hope is that seeing the numbers of others will give rise to a competitive spirit. "This is a form of gamification. Most people like competition, especially the Millennials," says Chad Carmichael, lead of the U.S. retirement practice at North Highland's financial services network.

Carmichael says he has seen research that peer-to-peer tools make a difference. "After using the tools, 25% of the people increased their contribution." On the other hand there has also been research that found that some people who compared themselves to others were discouraged and less motivated to save.

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"The peer-to-peer comparison tools are, in theory, a good idea. But in practice, those using the tools are the individuals who need the tools the least. And, the individuals concerned about saving for retirement are actually heartened by how much better off they are than their peers," says Robert Johnson, PhD., president and CEO of The American College of Financial Services. "The tools actually provide those who have saved for retirement, but who have under saved, a false sense of security. It is the reverse of 'keeping up with the Joneses'. People rationalize that they aren't bad off and don't increase their retirement contributions."

Chris Carosa, author of Hey! What's My Number? How to Increase the Odds You Will Retire in Comfort says the tools are highly ineffective, "The best example of how misleading this can be is the use of target date funds. Although increasingly popular, they are predicating on a single factor that, by itself, doesn't contain enough information on what's needed to retire in comfort."

He points to the fact that target date funds are based on your age. "Should a 50 year-old with no savings be investing the same way as a 50 year-old, who is already independently wealthy? The answer is obviously no."

The issue is that everyone's situation is different. "There are so many variables that make a big difference in how much somebody needs to have saved for retirement. In my opinion, using peer-to-peer comparisons is not much better than using the 80% rule," says Tony D'Amico, CEO of The Fidato Group.

It's easy to dismiss the numbers if you don't think it applies to you. "People discount the data because they believe their situation is truly unique and the comparison doesn't account for all facets of their financial life, for example, they have a pension or they don't have kids and most of their co-workers have two kids so they spend more, or their salary is lower than most people in their company so they can't compare their savings to others in their company because they afford to save more," explains Lidia Shong, head of market at aboutLife, a company that provides free online financial planning services to Baby Boomers.

She says that unless the data is customized and it takes into account more data points than just retirement savings, people are not going to take it seriously.

aboutLife has built peer-to-peer comparison that's more targeted and more personalized to the individual, says Shong. "That level of detail is generating better results and acceptance, although not 100 percent."

aboutLife aggregates data from the Census, Bureau of Labor Statistics and Federal Reserve to calculate how much people are spending on each household category (groceries, utilities, transportation, etc.). They then break it down by age, household income and neighborhood. "That way, we can show customers how much their neighbors, who are about the same age and have a similar household income and household composition (number of people), are spending on groceries, for example, and how much they are saving."

She says that level of detail makes the comparison more powerful and actionable by the customer. "It helps people visualize themselves saving the same amount if the subjects of the comparison are truly similar to them. In other word, they rationalize it by saying, 'My neighbor X has the same number of kids, their household income is probably similar to ours – if they are spending this much less on their cable bill, that means I can do it too!"

While the experts debate about whether peer-to-peer comparison tools are effective, some are just glad people are looking at the numbers. Says Carmichael, "The earlier they get a smack in the face, versus finding out at 65 that they aren't on track for retirement, the better."