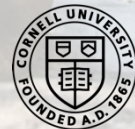CEPAR CAMA Policy Dialogue, 10 October 2022

Applying Behavioral Science to Decumulation Decision Making

Suzanne Shu, Cornell University and NBER

Cornell University
Cornell
SC Johnson College of Business

The Decumulation Problem

The nastiest, hardest problem in finance.

We've made good progress on the accumulation phase of retirement saving, but the decumulation phase hasn't received nearly enough attention… The spending-down phase is even harder for individuals to solve.

William Sharpe
1990 Nobel Prize

Richard Thaler
2018 Nobel Prize

Mistakes in getting decumulation decisions right

1. Predicting longevity

2. Decision making during retirement

3. Trust and fairness

Mistakes in getting decumulation decisions right

1. Predicting longevity

   - Years in retirement versus years at work

   - Life expectations versus longevity

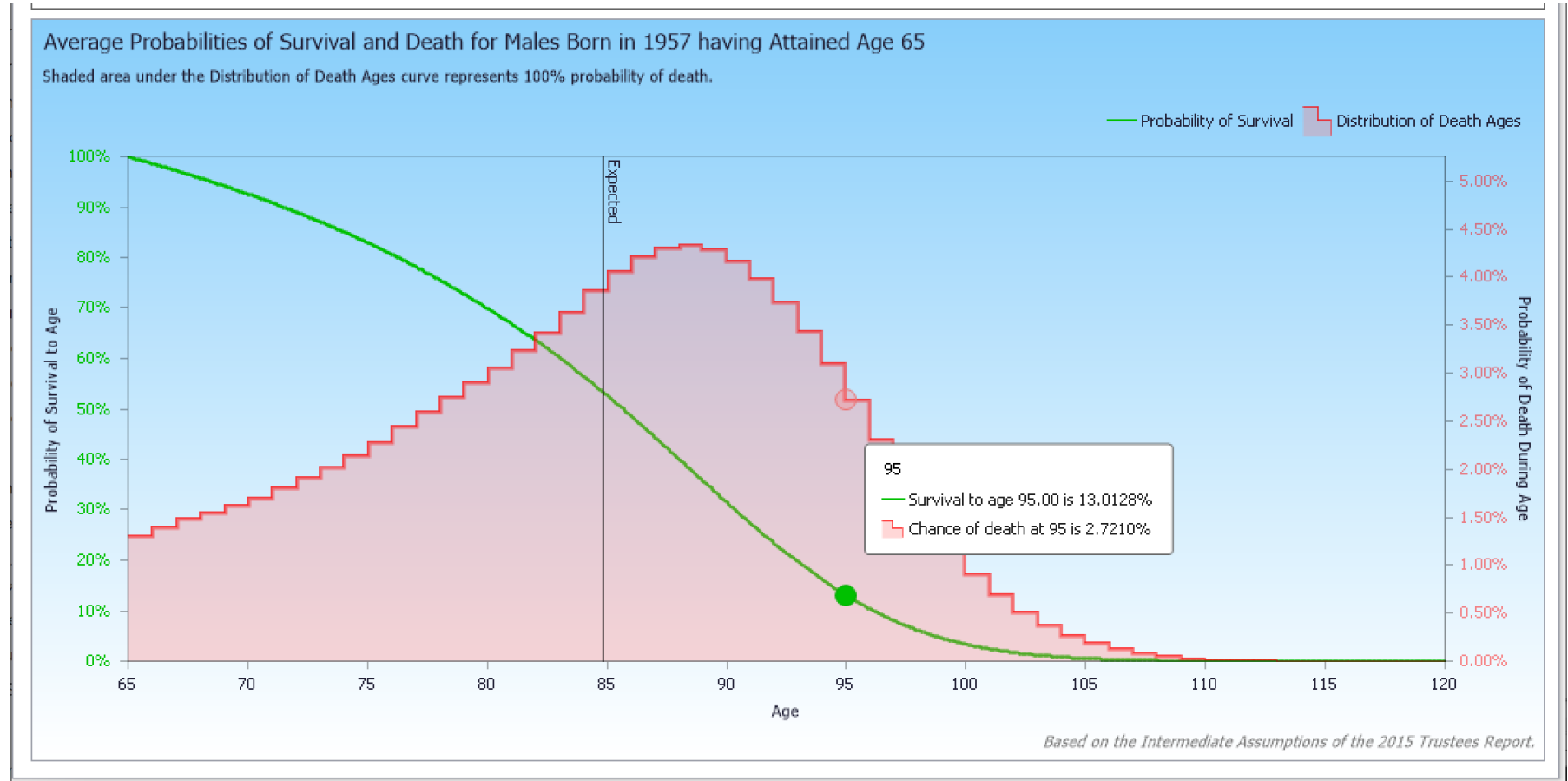2. Decision making during retirement

3. Trust and fairness

B. Smaller

"If we take a late retirement and an early death, we'll just squeak by."

Life expectancy versus probabilities

Male, current age = 65

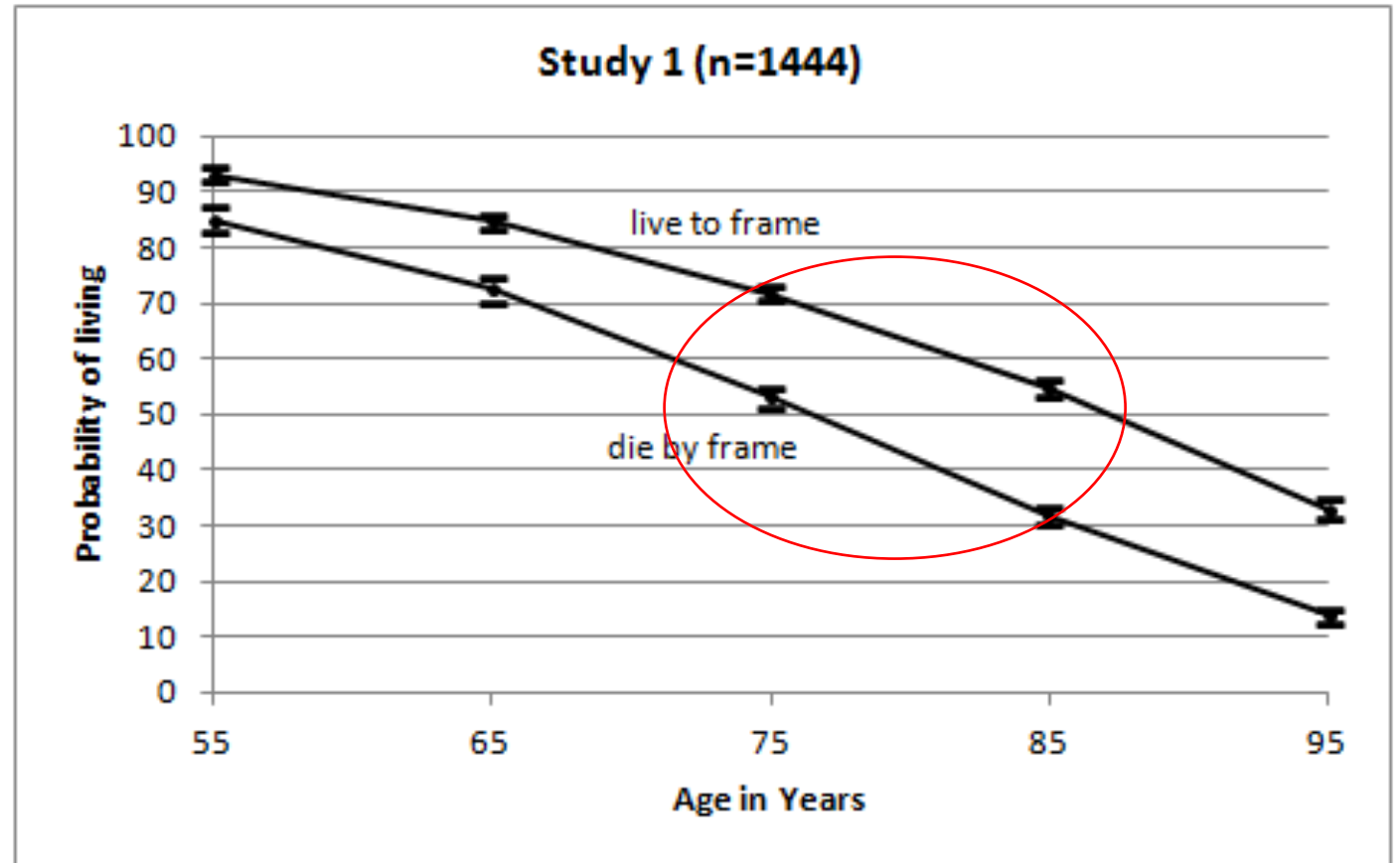Expected age at death = 84.1

Probability of living to age 95 = 13%

Average Probabilities of Survival and Death for Males Born in 1957 having Attained Age 65

Shaded area under the Distribution of Death Ages curve represents 100% probability of death.

— Probability of Survival   ⬜ Distribution of Death Ages

95
— Survival to age 95.00 is 13.0128%
⬜ Chance of death at 95 is 2.7210%

Based on the Intermediate Assumptions of the 2015 Trustees Report.

U.S. Social Security Administration's Longevity Visualizer

How you ask changes life expectations

What's the chance you live to age 85? (average = 55%)

What's the chance you die by age 85? (average = 68%)

Ten-year gap in median expected age of death: 75 years (die-by) versus 85 years (live-to).

Study 1 (n=1444)

live to frame

die by frame

Probability of living

Age in Years

Payne, Sagara, Shu, Appelt, and Johnson 2013

Mistakes in getting decumulation decisions right

1. Predicting longevity

2. Decision making during retirement

   - Large stakes decisions

   - Multiple sources of uncertainty

   - No chance to learn from feedback

   - Highly emotional tradeoffs

3. Trust and fairness

Shu and Shu 2018
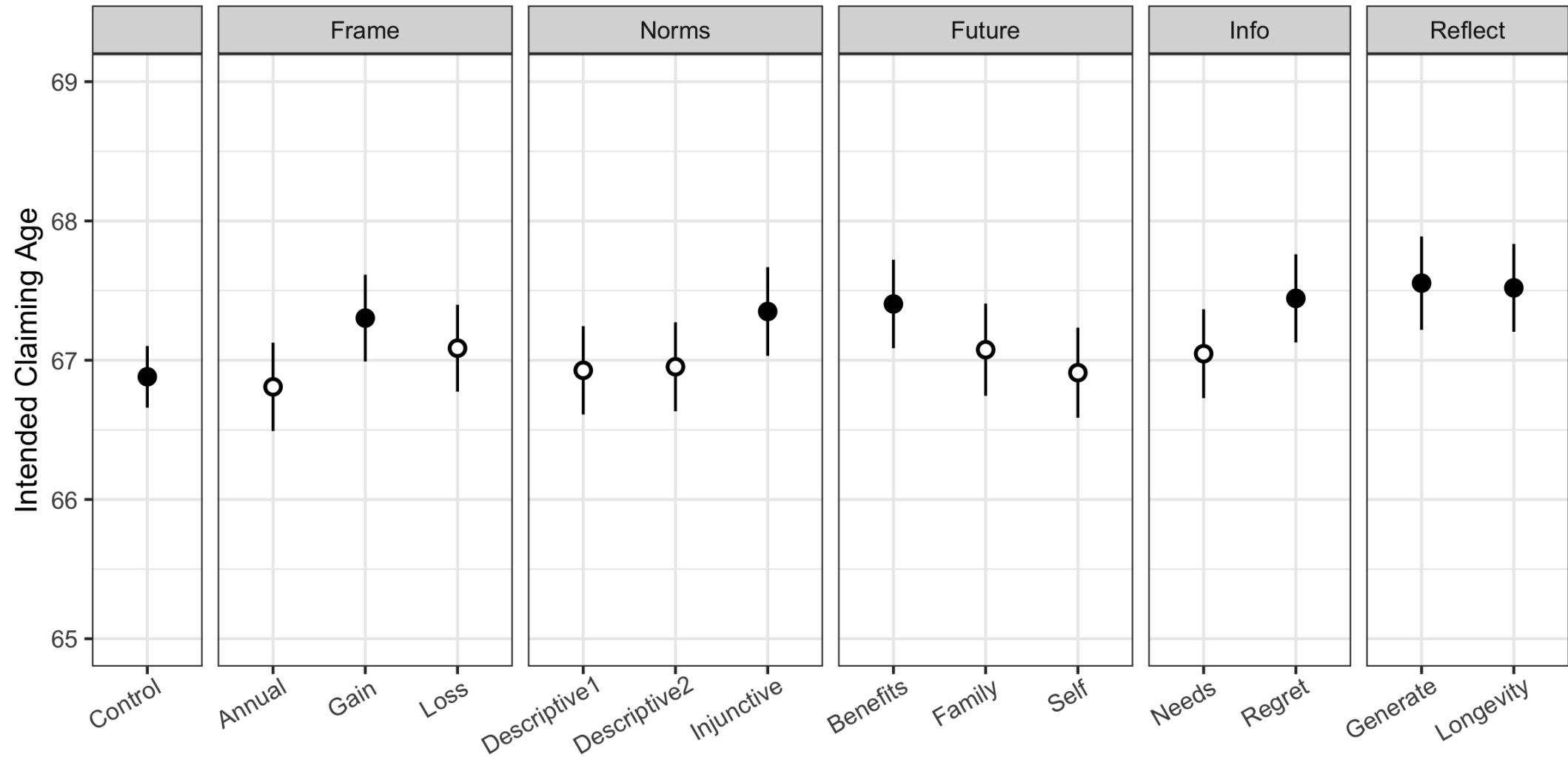
A Role for Custom Interventions?

- Retirement income decisions are more personalized than retirement savings

- Should interventions be tailored (targeted) to the individual's needs?

  - Personalized default rules – Sunstein 2013

  - "Nudge me right" for passwords – Peer et al 2019

  - UK BIT tax letters – Halpern 2016

  - Social norms for electricity use – Costa & Kahn 2013

- Testing multiple interventions simultaneously alongside individual differences

Testing interventions for U.S. SSA claiming decisions

Greenberg, Hershfield, Shu, and Spiller WP

Mistakes in getting decumulation decisions right

1. Predicting longevity

2. Decision making during retirement

3. Trust and fairness

- Concerns about firm risks

- Concerns about personal risks

A glimpse into U.S. retirement policy

- SECURE Act – passed & signed December 2019
- SECURE Act 2.0 – passed April 2022

The retirement crisis in America is real, and will only get worse without easier pathways to saving and encouraging workers to start planning for retirement earlier in life.

Annuity rollout in U.S. policy

- Included in the SECURE Act:
  - Promotion of lifetime income solutions such as annuities within employer retirem
  - Safe harbor prote uities
  - Annuities are por plans
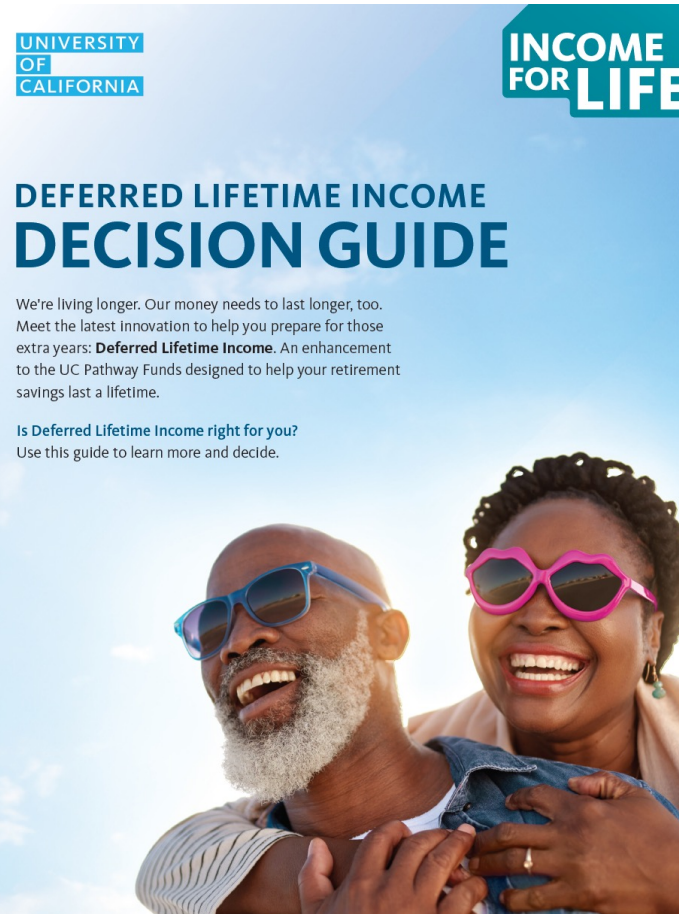
3 DECUMULATION TAKEAWAYS

- How questions are posed can affect predictions

- Retirement income solutions need to be highly personalized

- Trusted partners are an important element in delivering lifetime income solutions