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Explaining Consumer's Progress Through Annuity Decision States

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UNSW Sydney, CEPAR
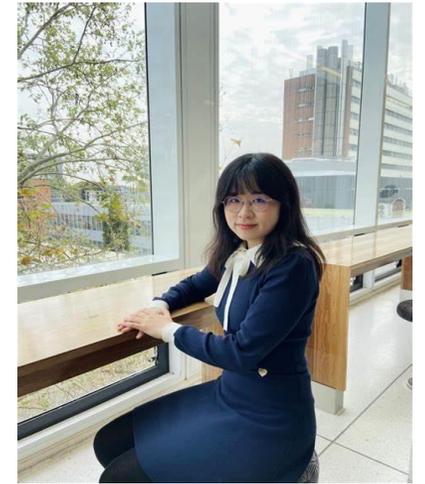May 2023

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Contents

Annuity Puzzles in Australia

Decision States Model

Eliciting Decision States for Lifetime Income Products

Regression Analysis to Predict Decision State Membership
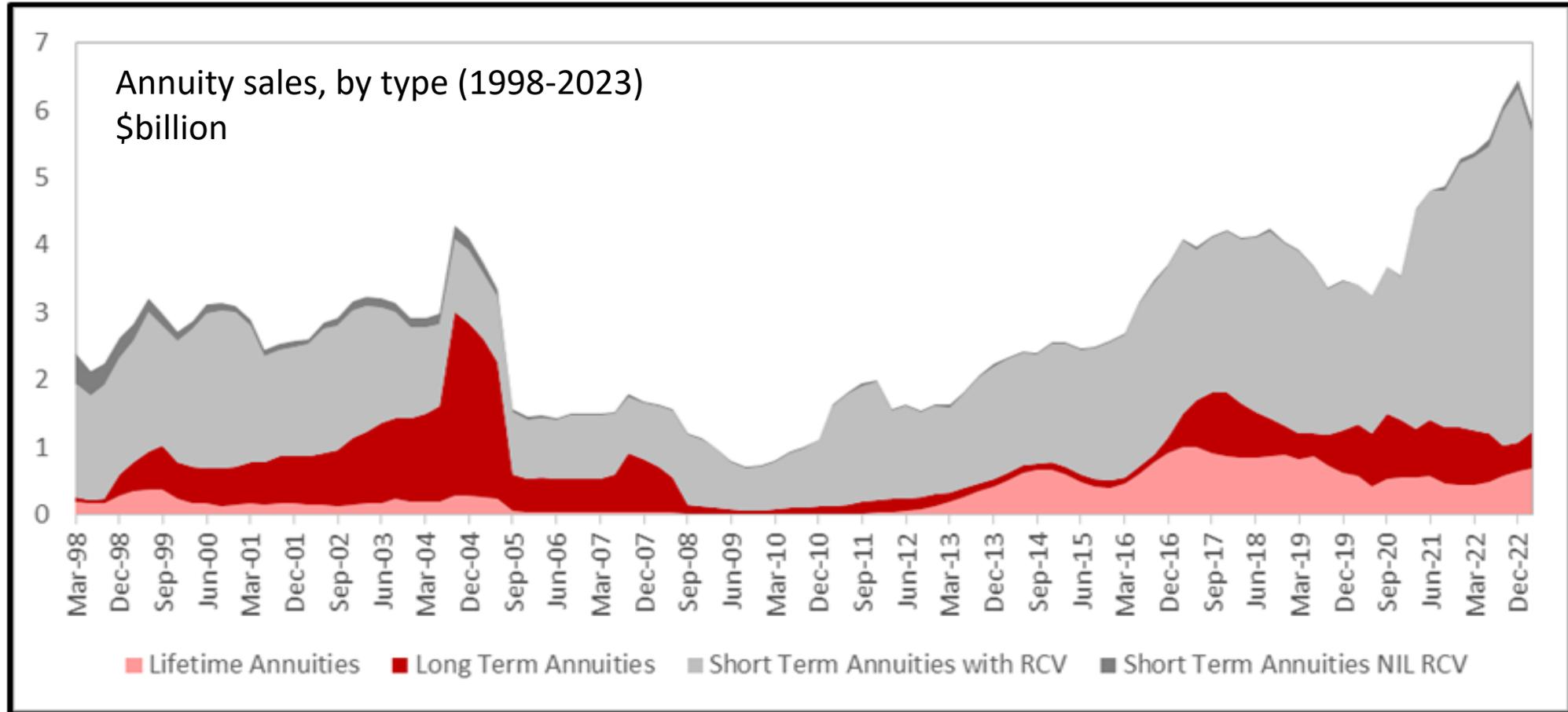
Discussion

Next Steps

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Annuity Puzzles in Australia

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The lifetime annuity market in Australia has always been small

Annuity sales, by type (1998-2023)
$billion

Legend: Lifetime Annuities | Long Term Annuities | Short Term Annuities with RCV | Short Term Annuities NIL RCV

Source: Plan for Life

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Annuities (lifetime income products) in Australia – Facts and myths

- Mandatory superannuation is still maturing

- The Age Pension provides full or partial annuitization for many: two-thirds of Australian retirees receive a full or part Age Pension

- Lifecycle models of optimal annuitization predict partial annuitization

- Behavioural impediments to annuity demand identified in the academic literature have been largely addressed by providers –consumption framing, reversible, death benefits, indexation, market-linked

- Recent academic literature focuses on non-standard preferences, poor financial literacy & product knowledge, subjective survival expectations **BUT does not explain such low levels of annuitization**
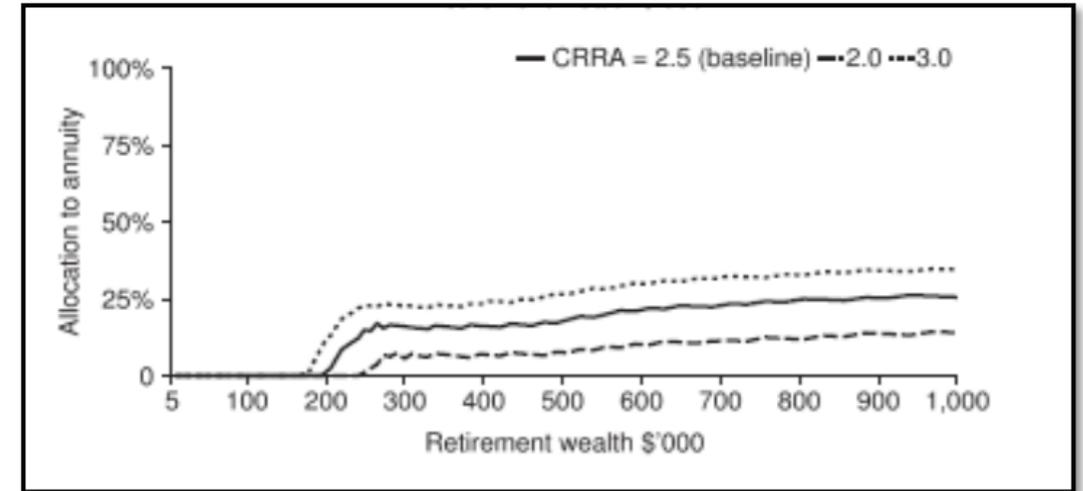
Iskhakov, Thorp, Bateman (2015), Optimal annuity purchases for Australian retirees, *Economic Record*.

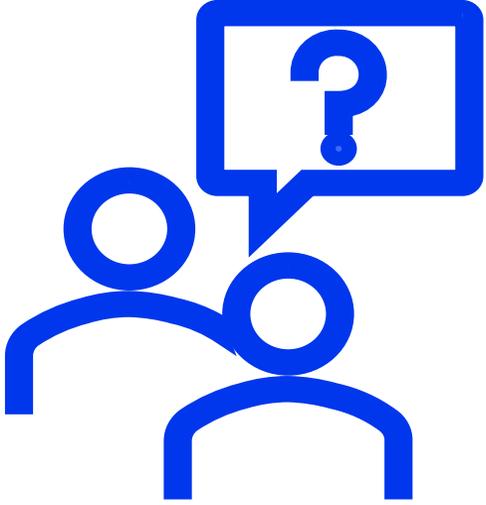Little evidence to suggest Australians 'do not like annuities'

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Decision States Model
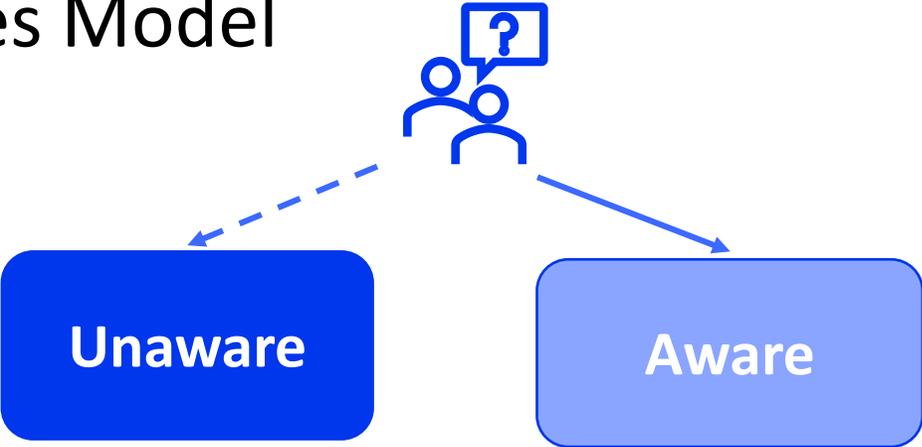
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The Decision States Model

- People go through a series of decision states before they are ready to purchase

- Particularly relevant for complex financial products

- Conceptual model: Bateman H, Louviere J and S Thorp (2014), 'Understanding How Consumers Make Financial Choices: A Cross-Disciplinary Learning Experience, *Routledge Companion to Financial Services Marketing.*

- Applied to Life Insurance Demand: Bateman H, P Gerrans, S Thorp and Y Zeng (2023), 'Explaining Consumers' Progress through Life Insurance Decision States: The Role of Personal Values and Consumer Characteristics', *Journal of Consumer Affairs.*

The Decision States Model

Unaware

Aware

The Decision States Model

The Decision States Model

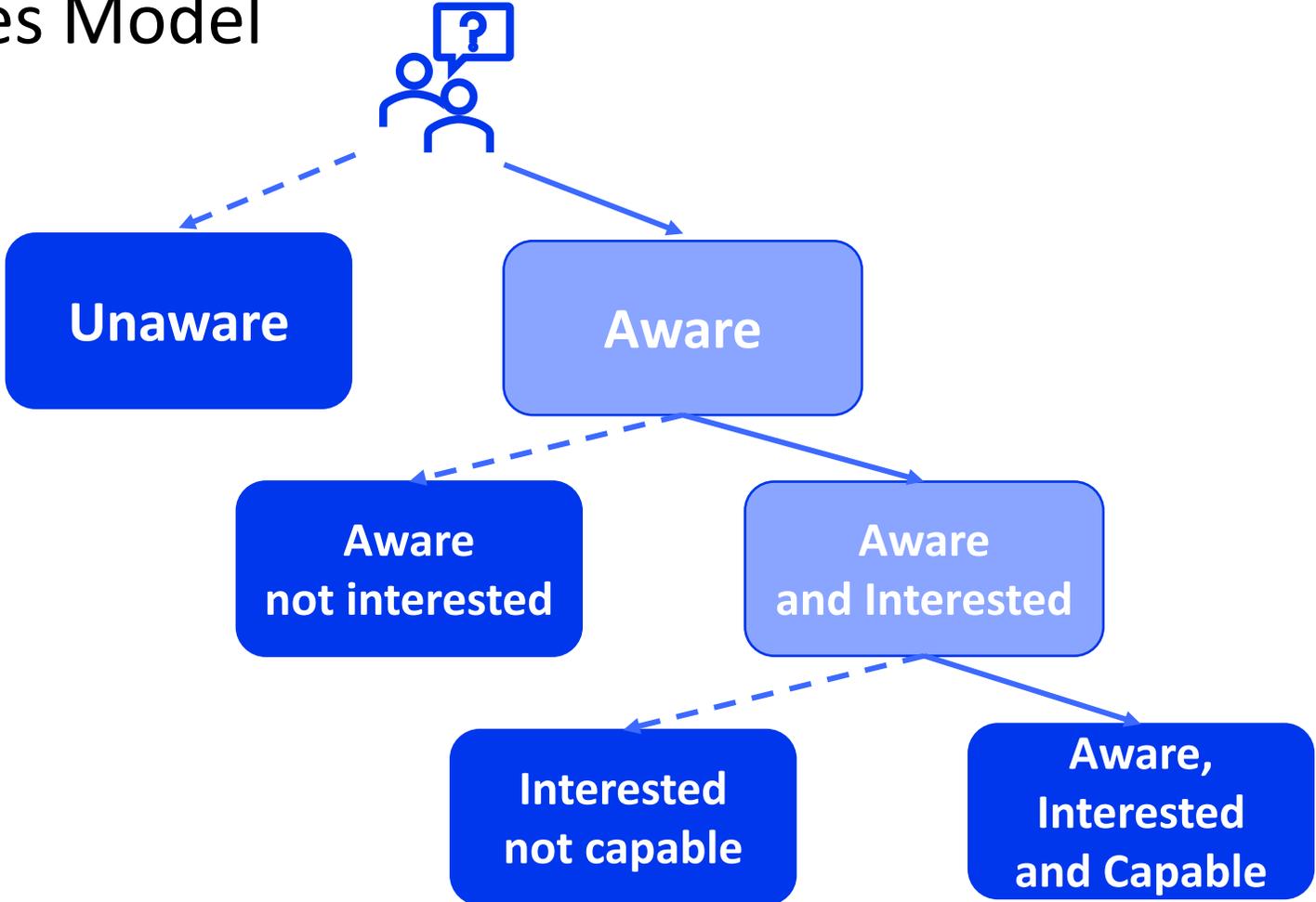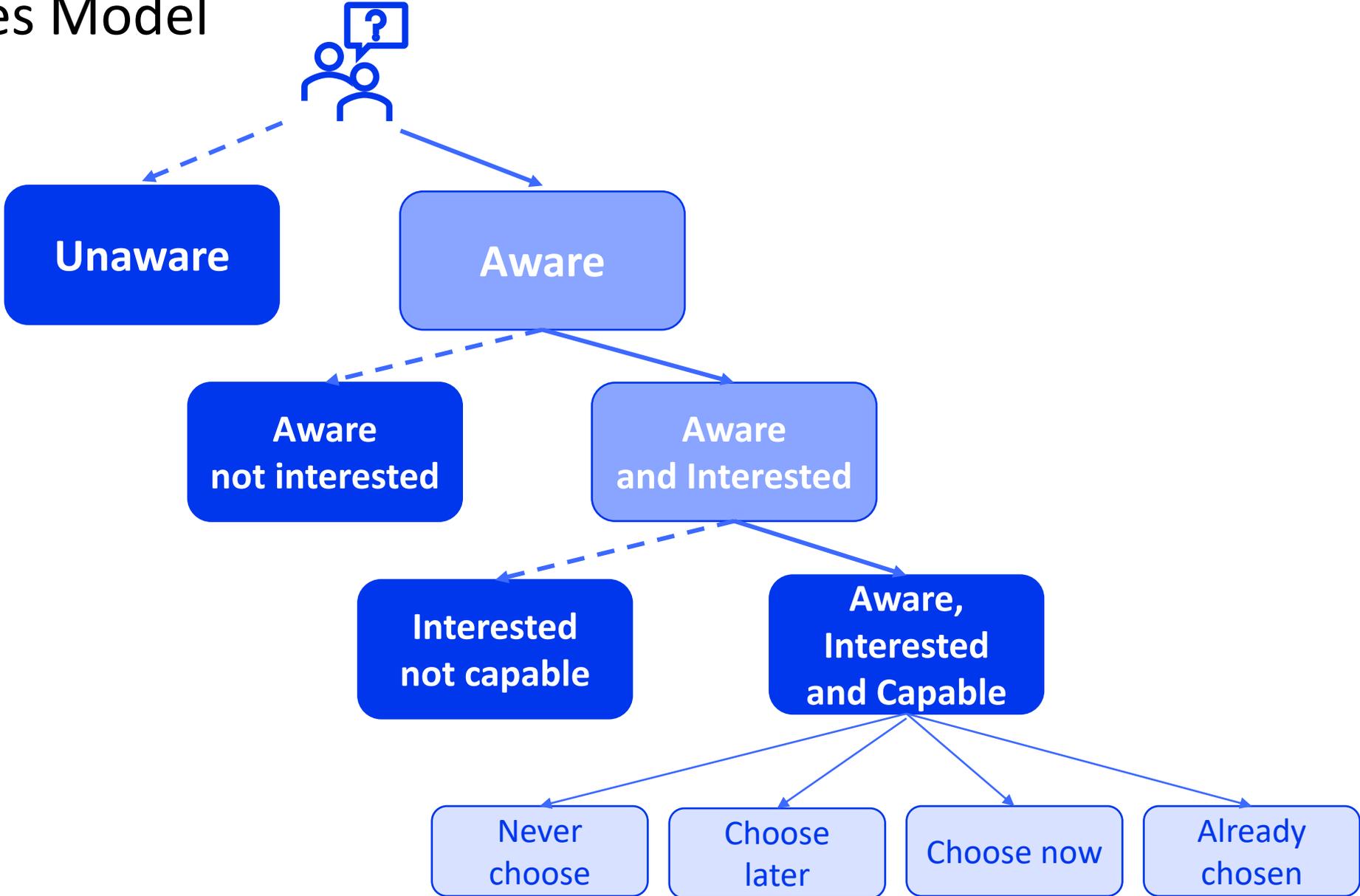# Eliciting Decision States for Lifetime Income Products

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We designed a survey to elicit Decision States for lifetime income products

Sample selection
▪ Online survey via Pureprofile
▪ n=1,216: Age 50-74, super account, representative gender & wealth

Strategic questions to elicit Decision State for lifetime income products
Unaware; Aware (not interested); Interested (not capable); Aware, Interested and Capable; (Capable - choose never; Capable - choose later; Capable - choose now; Capable - already chosen)

Questions on personal characteristics, knowledge, perceptions, attitudes						
Demographics	Preferences	Financial capability	Super arrangements	Personality traits	Retirement planning	Health, Subjective life expectancy, Longevity literacy

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For example: Questions to elicit subjective life expectancy, subjective survival probabilities & longevity literacy

Subjective Life Expectancy

To what age do you think you [an average person of the same age and sex as you] will live?

Subjective Survival Probabilities

How likely do you think it is that you [an average person of the same age and sex as you] will live to age X? (X: 65, 70, 75, 80, 85, 90, 95, 100, 105)

Please indicate your answer on a scale of 0 to 10, where 0 means "no chance at all" and 10 means "absolutely certain".

Life Expectancy Literacy

What is life expectancy among 65-year-old [men/women] in Australia?

- o About [12/15] more years (age 77/80])
- o About [16/19] more years (age 81/84])
- o About [20/34] more years. (age 85/88])
- o About [24/27] more years (age 89/92])
- o About [28/31] more years (age 93/96])
- o Don't know
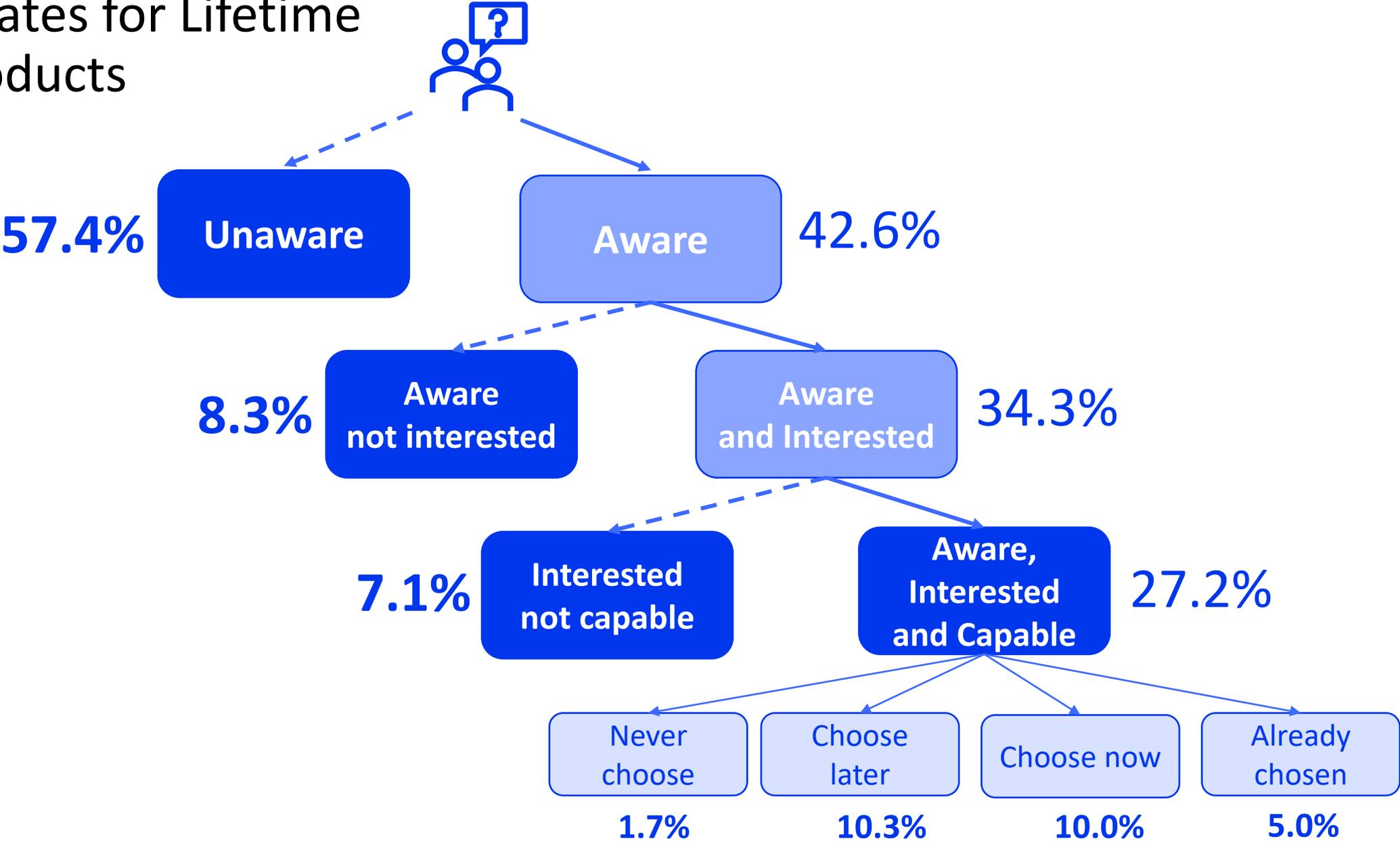
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Decision States for Lifetime Income Products

57.4% Unaware

Aware **42.6%**

8.3% Aware not interested

Aware and Interested **34.3%**

7.1% Interested not capable

Aware, Interested and Capable **27.2%**

Never choose	Choose later	Choose now	Already chosen
1.7%	**10.3%**	**10.0%**	**5.0%**

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n=2,016
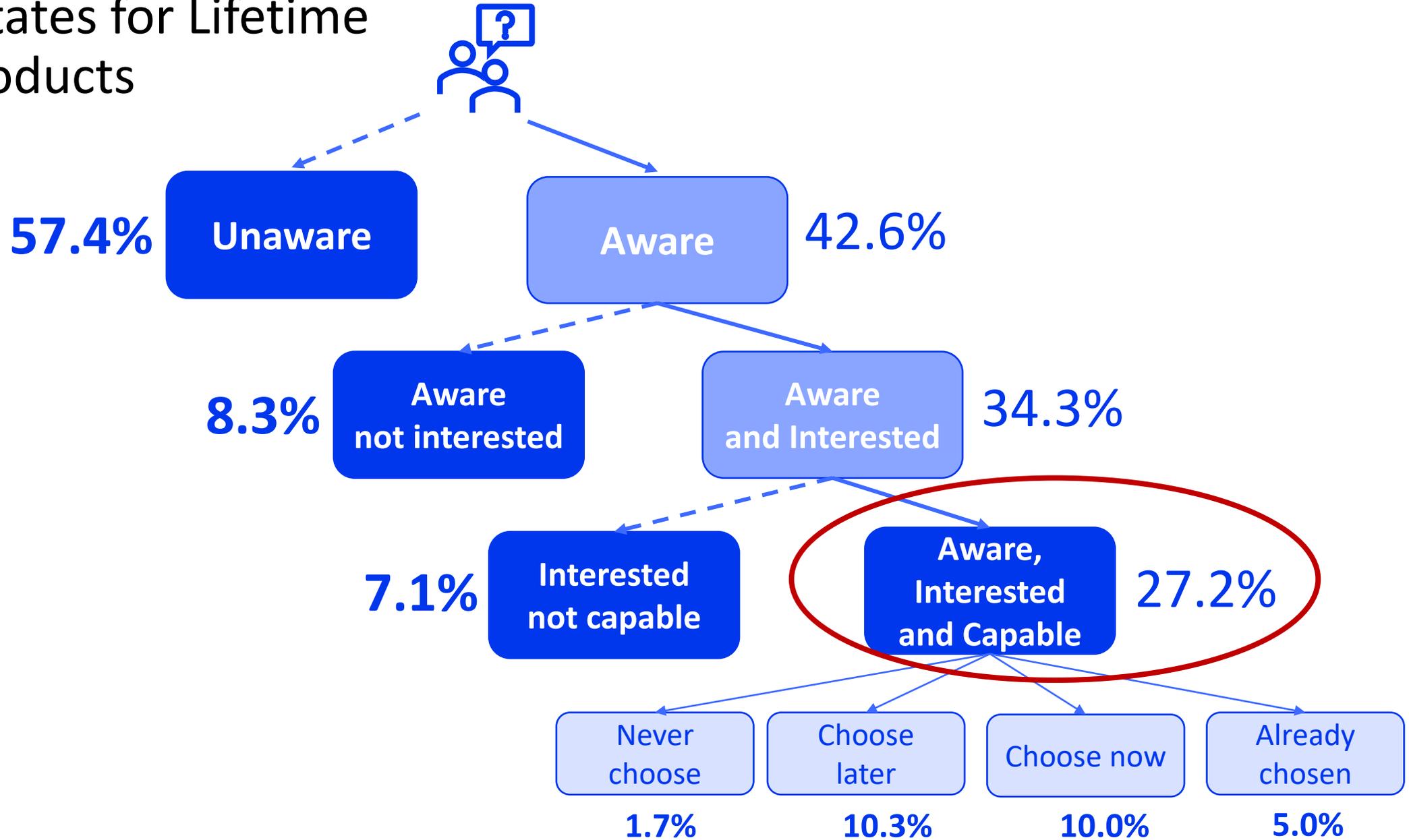
Regression analysis

Estimate sequential logit model to predict decision state membership

[[[	Unaware	Aware (not interested)	Interested (not capable)	Aware, Interested & Capable
Demographics	young**, female***	old***		young**, homeowner*
Tertiary education	[-]*			
Retired	[-]**	[+]*		
Household income		[+]**		
Age Pension			[+]*	
Subjective financial literacy	[-]***	[+]***	[-]***	
Objective financial literacy	[-]**			
Perceive understand lifetime income product (LIP)		[-]**	[-]***	[+]***
Perceive ABP riskier than LIP		[-]**		[+]**
Longevity tail literacy		[-]***		[+]**
Planned for retirement	[-]***			
Planned bequest	[-]*	[-]***		[+]***
Household decision maker			[-]*	[+]***
DB	[-]**			
Super fund offers lifetime income product	[-]***			

Demographics and h/hold finances more important for early decision states

[[[	Unaware	Aware (not interested)	Interested (not capable)	Aware, Interested & Capable
Demographics	young**, female***	old***		young**, homeowner*
Tertiary education	[-]*			
Retired	[-]**	[+]*		
Household income		[+]**		
Age Pension			[+]*	
Subjective financial literacy	[-]***	[+]***	[-]***	
Objective financial literacy	[-]**			
Perceive understand lifetime income product (LIP)		[-]**	[-]***	[+]***
Perceive ABP riskier than LIP		[-]**		[+]**
Longevity tail literacy		[-]***		[+]**
Planned for retirement	[-]***			
Planned bequest	[-]*	[-]***		[+]***
Household decision maker			[-]*	[+]***
DB	[-]**			
Super fund offers lifetime income product	[-]***			

Poor objective and subjective literacy associated with being **unaware**, **not capable**

[[[	Unaware	Aware (not interested)	Interested (not capable)	Aware, Interested & Capable
Demographics	young**, female***	old***		young**, homeowner*
Tertiary education	[-]*			
Retired	[-]**	[+]*		
Household income		[+]**		
Age Pension			[+]*	
Subjective financial literacy	[-]***	[+]***	[-]***	
Objective financial literacy	[-]**			
Perceive understand lifetime income product (LIP)		[-]**	[-]***	[+]***
Perceive ABP riskier than LIP		[-]**		[+]**
Longevity tail literacy		[-]***		[+]**
Planned for retirement	[-]***			
Planned bequest	[-]*	[-]***		[+]***
Household decision maker			[-]*	[+]***
DB	[-]**			
Super fund offers lifetime income product	[-]***			

Perceived understanding of lifetime income product and comparison with ABP important

[[[	Unaware	Aware (not interested)	Interested (not capable)	Aware, Interested & Capable
Demographics	young**, female***	old***		young**, homeowner*
Tertiary education	[-]*			
Retired	[-]**	[+]*		
Household income		[+]**		
Age Pension			[+]*	
Subjective financial literacy	[-]***	[+]***	[-]***	
Objective financial literacy	[-]**			
Perceive understand lifetime income product (LIP)		[-]**	[-]***	[+]***
Perceive ABP riskier than LIP		[-]**		[+]**
Longevity tail literacy		[-]***		[+]**
Planned for retirement	[-]***			
Planned bequest	[-]*	[-]***		[+]***
Household decision maker			[-]*	[+]***
DB	[-]**			
Super fund offers lifetime income product	[-]***			

Poor longevity tail literacy a barrier to **interest**

| [[[	Unaware	Aware (not interested)	Interested (not capable)	Aware, Interested & Capable
Demographics	young**, female***	old***		young**, homeowner*
Tertiary education	[-]*			
Retired	[-]**	[+]*		
Household income		[+]**		
Age Pension			[+]*	
Subjective financial literacy	[-]***	[+]***	[-]***	
Objective financial literacy	[-]**			
Perceive understand lifetime income product (LIP)		[-]**	[-]***	[+]***
Perceive ABP riskier than LIP		[-]**		[+]**
Longevity tail literacy		[-]***		[+]**
Planned for retirement	[-]***			
Planned bequest	[-]*	[-]***		[+]***
Household decision maker			[-]*	[+]***
DB	[-]**			
Super fund offers lifetime income product	[-]***			

Lack of retirement planning (including bequests) a barrier to **awareness/interest**

[[[	Unaware	Aware (not interested)	Interested (not capable)	Aware, Interested & Capable
Demographics	young**, female***	old***		young**, homeowner*
Tertiary education	[-]*			
Retired	[-]**	[+]*		
Household income		[+]**		
Age Pension			[+]*	
Subjective financial literacy	[-]***	[+]***	[-]***	
Objective financial literacy	[-]**			
Perceive understand lifetime income product (LIP)		[-]**	[-]***	[+]***
Perceive ABP riskier than LIP		[-]**		[+]**
Longevity tail literacy		[-]***		[+]**
Planned for retirement	[-]***			
Planned bequest	[-]*	[-]***		[+]***
Household decision maker			[-]*	[+]***
DB	[-]**			
Super fund offers lifetime income product	[-]***			

Less likely **unaware** if super fund offers a lifetime income product

[[[	Unaware	Aware (not interested)	Interested (not capable)	Aware, Interested & Capable
Demographics	young**, female***	old***		young**, homeowner*
Tertiary education	[-]*			
Retired	[-]**	[+]*		
Household income		[+]**		
Age Pension			[+]*	
Subjective financial literacy	[-]***	[+]***	[-]***	
Objective financial literacy	[-]**			
Perceive understand lifetime income product (LIP)		[-]**	[-]***	[+]***
Perceive ABP riskier than LIP		[-]**		[+]**
Longevity tail literacy		[-]***		[+]**
Planned for retirement	[-]***			
Planned bequest	[-]*	[-]***		[+]***
Household decision maker			[-]*	[+]***
DB	[-]**			
Super fund offers lifetime income product	[-]***			

Predicted Membership of Aware, Interested & Capable – **Choose Now**

Aware, Interested and Capable

- Never choose
- Choose later
- **Choose now**
- Already chosen
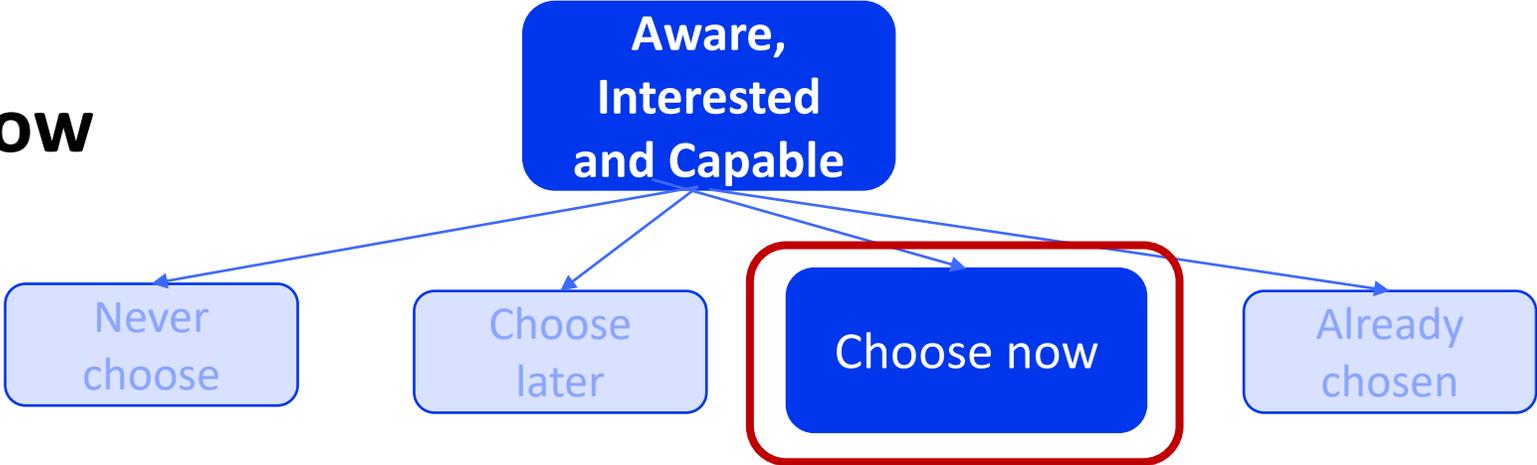
Demographics & household finances
(-ve) retired**
(-ve) super balance**
(+ve) net wealth**
(+ve) Age Pension**

Knowledge
(+ve) objective financial literacy*
(+ve) numeracy*

Preferences
(-ve) impatient*
(+ve) planned bequest***

Life expectancy literacy
(-ve) confused**

Experience
(+ve) super fund offers lifetime income product**
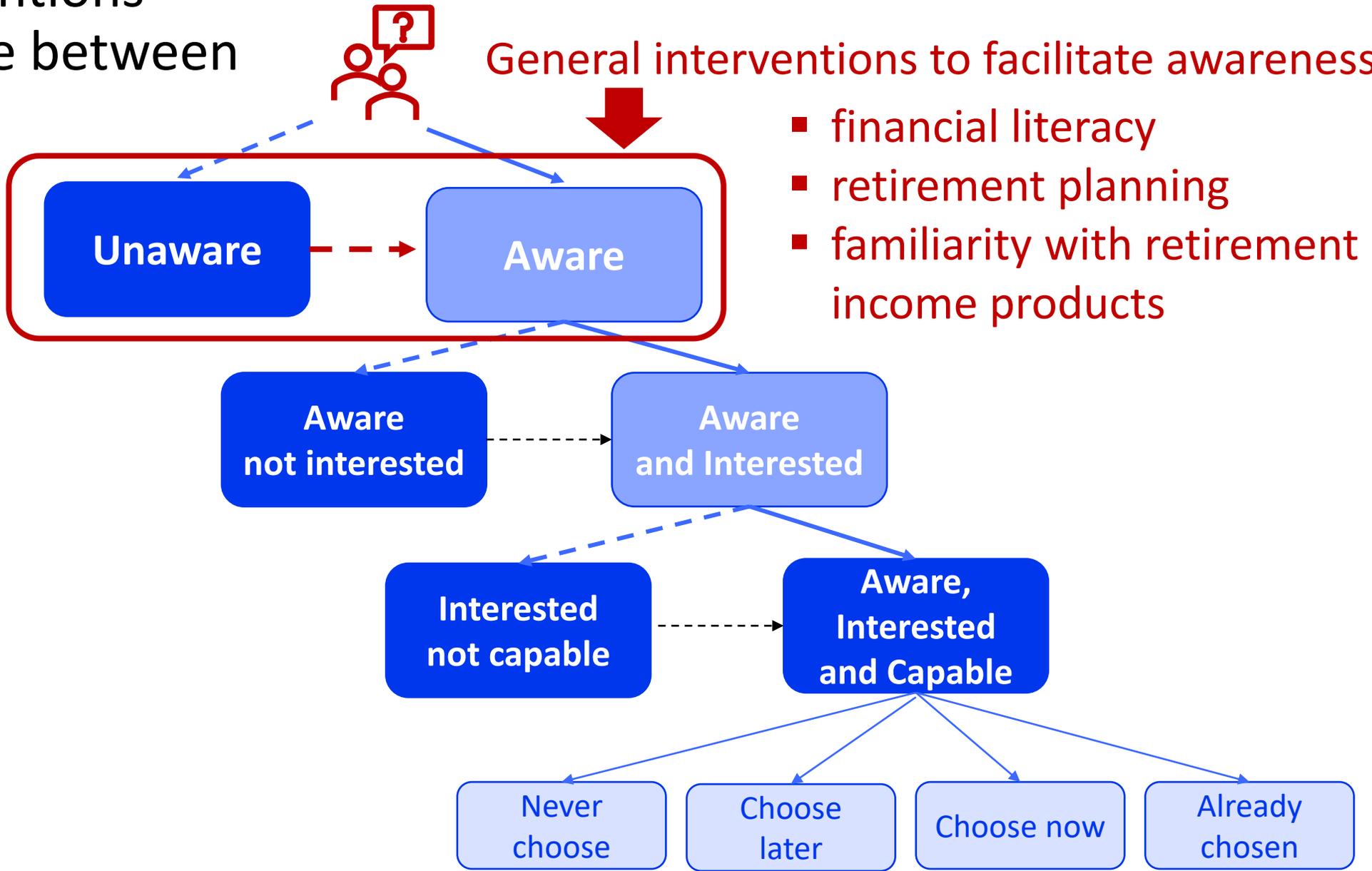
Retirement planning and attitudes
(-ve) confident finance retirement*
(+ve) financial advice*
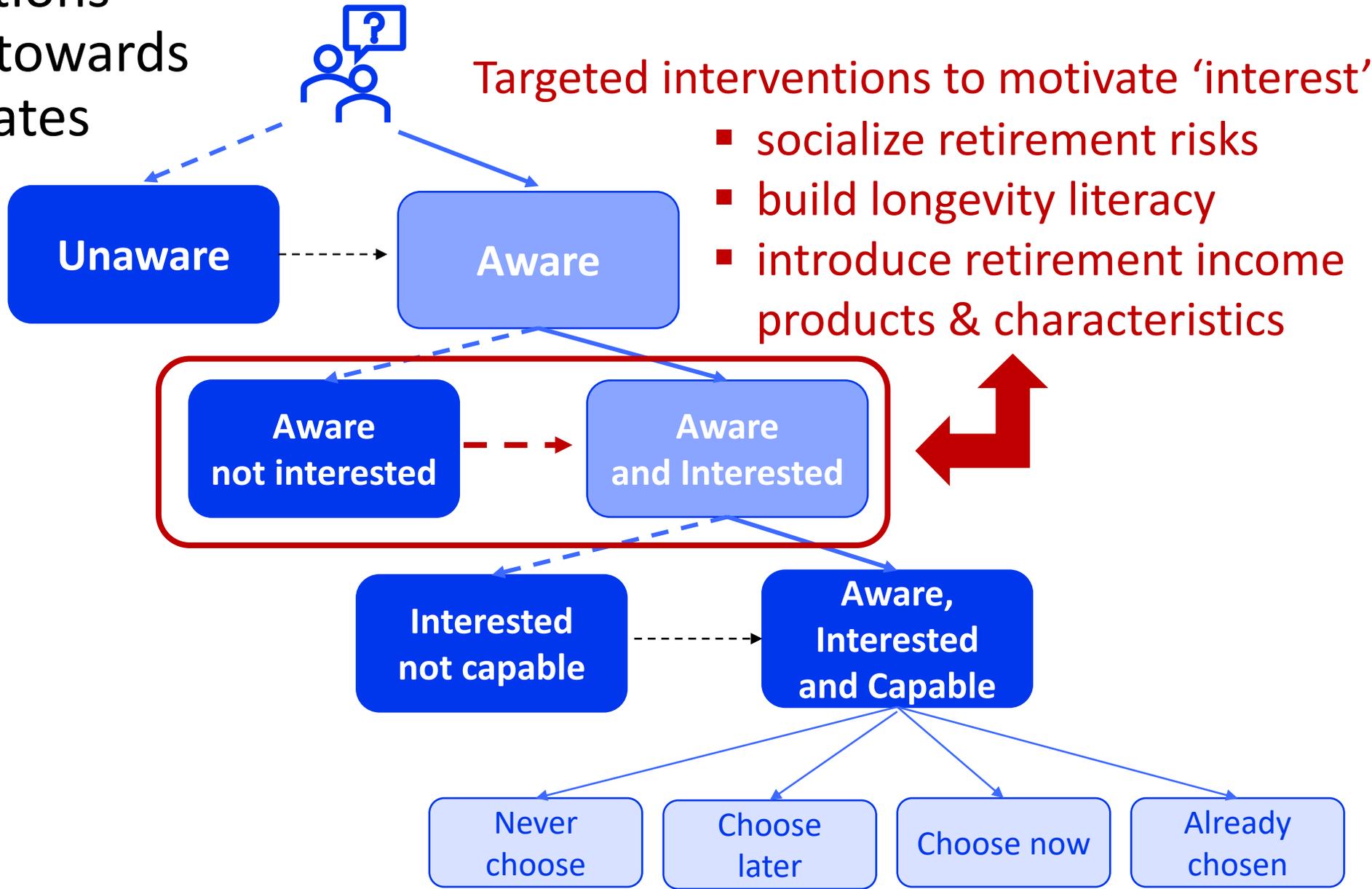(-ve) planned for retirement**
(+ve) primary decision maker***

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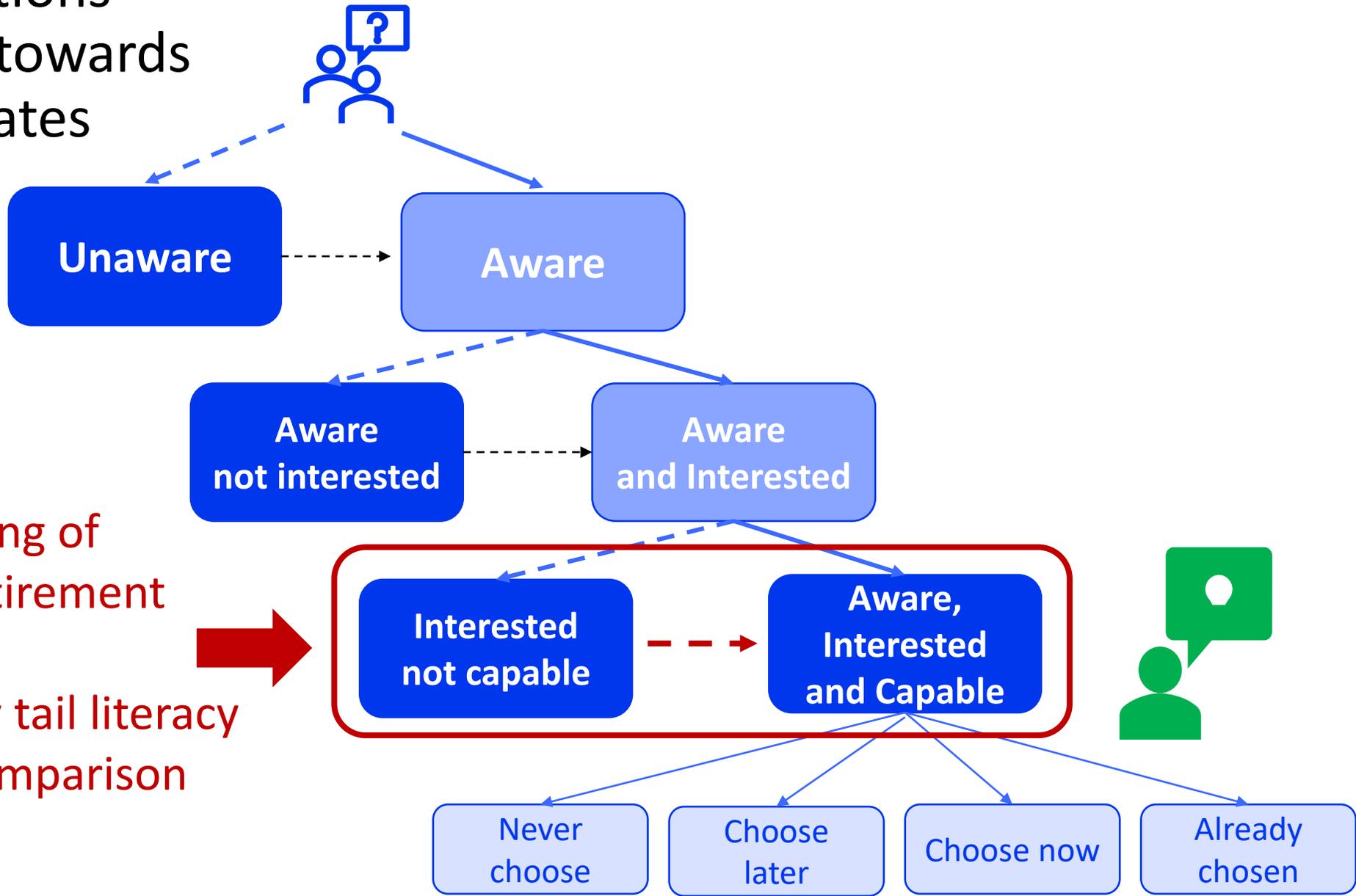Presented at the 2024 All Actuaries Summit

Discussion

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Different interventions required to move towards more advanced states

Targeted interventions to motivate 'interest'
- socialize retirement risks
- build longevity literacy
- introduce retirement income products & characteristics

Unaware → **Aware**

Aware not interested → **Aware and Interested**

Interested not capable → **Aware, Interested and Capable**

Never choose | Choose later | Choose now | Already chosen

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Different interventions required to move towards more advanced states

Build capability
- specific understanding of characteristics of retirement income products
- emphasize longevity tail literacy
- facilitate product comparison

Unaware → Aware

Aware not interested → Aware and Interested

Interested not capable → Aware, Interested and Capable

Never choose | Choose later | Choose now | Already chosen

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Next steps

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Next Steps

- Design and test communication interventions to move people between decision states **Unaware → Aware → Interested → Capable & ready to choose**

- Results suggest **different interventions for different decision states**: focus on retirement planning, financial literacy, longevity literacy, available products, at earlier decision states → moving towards detail and product comparisons at advanced decision states.

- Key Challenge –longevity literacy/awareness [Teppa, Thorp & Bateman, 2016]

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Next Steps

Proposed interventions - draw on (and extend) previous literature on communication of longevity risk, for example:

- Just in time **product information** [Bateman, Thorp et al., 2018]

- Retirement income product **fact sheets** [Bateman & Eberhardt, 2022]
    - Tested fact sheet information presented in the Treasury 'Retirement Income Disclosure Consultation Paper' (December 2018) → problematic

- Simple **calculator** to compare lifetime payments from ABP and lifetime annuity [Alonso Garcia et al., 2024]

- **Vignettes** to illustrate information on SLE and longevity [Hurwitz et al., 2022]

- **Interactive/experiential online tools** to facilitate longevity literacy/awareness???

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Concluding comments

- **57.5%** of representative sample of Australians aged 50-74 **Unaware** of lifetime income products, **8.3% Aware (not interested)**, **7.1% Interested (not capable)**

- Only **27.2% Aware, Interested & Capable to choose**

- Different factors predict membership of the different decision states → suggest different interventions from communication of **general information/interventions** to build awareness and interest to **specific interventions** to enhance capacity.

- Next steps: test interventions to **move people between decision states**

- Impact of findings: policy & regulation design, super fund Retirement Income Strategies, product providers

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Hurwitz A, O S Mitchell and O Sade (2022), Testing methods to enhance longevity awareness, Journal of Economic Behaviour and Organization, Testing methods to enhance longevity awareness – ScienceDirect.

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Thank you

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