Submission - ASIC Consultation Paper 351
Superannuation forecasts: Update to
relief and guidance

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Summary: Over the past decade our research group has examined financial behaviour across a range of settings that are relevant to ASIC's current proposals for superannuation forecasts. Here we briefly summarise what we think are the most useful findings in this context. Full references and Abstracts for all papers appear below this summary. A zip file containing PDFs of all papers is attached to this submission.

Perhaps our most relevant research investigates the impact of projections on retirement savings intentions and behaviour of members in a large industry fund **(Smyrnis et al., 2021)**. The key findings of this work are: 1) in an online experiment, providing participants with projections in the form of income-stream estimates alongside lump-sum balances increased their savings intentions; 2) in a field-trial, providing projections (income stream and lump-sums) increased voluntary savings and member-interaction with the fund. In recent related work examining the impact of projections on *spending* in retirement, we find provisional evidence in an online experimental study for increased rates of drawdown by participants shown income-stream projections (**Nian, 2021**).

In **Wang-Ly et al., 2021** we examined, via online experiments, the role of 'simple' and 'smart' calculators in aiding decisions about investment choices within a hypothetical superannuation fund. We find that although smart calculators help participants choose lowest-fee options, such benefits do not persist when decision support is removed. The results suggest that methods to improve competence and over-all financial literacy are more likely to have lasting impacts on improving consumer decision making.

Our group has also investigated the impact of different formats of risk presentation on understanding and choice in superannuation contexts. Illustrative examples include **Bateman et al. (2016a)** which highlights the naiveté of experimental participants in using information contained in prescribed investment disclosures; **Bateman et al. (2016b)** which demonstrates via discrete choice modelling experiments that when risk is described as the frequency of returns below or above a threshold more violations of expected utility are observed than for range and probability-based descriptions; and **Bateman et al. (2014)** which finds, again in discrete-choice experiments that risk-presentation formats (e.g., graphical vs textual) have more substantial impacts on superannuation portfolio preference than large changes in the actual underlying risk profile of different portfolios. In all cases these kinds of effects are more prominent in individuals with low financial literacy.

Our aim in this submission is to provide evidence-based responses to select questions informed by our academic research, as set out below. Abstracts to the specific papers from our group mentioned in this submission are included at Attachment A. At Attachment B we list academic references on retirement estimates from other jurisdictions. Attachment C is a zip file of our research papers mentioned in this submission.

Response to specific questions:

B8Q2. How do superannuation calculators and retirement estimates currently influence member behaviour? What data and evidence do trustees and other providers currently collect on how these forecasts, including their assumptions and presentation, influence member behaviour and outcomes?

In the field study and hypothetical experiments reported in Smyrnis et al., (2021) we find that retirement estimates raise both voluntary savings <u>and</u> member engagement. As such they provide a 'boost' to retirement planning without using mandatory measures (i.e., increasing the mandatory superannuation guarantee) or introducing default contribution rates (i.e., an x% voluntary contribution with opt-out) and are thus more likely to match member preferences.

We have not tested more complicated formulations that include variations to rates of return or other complications. We do, however, have positive evidence on the current format for retirement estimates and our study reported in Smyrnis et al., (2021) confirms that the current combination of retirement income <u>and</u> lump sum (account balance) estimates are essential to their effectiveness.

While we have not tested the effectiveness of retirement calculators, we can provide insights from related research reported in Wang-Ly et al., (2021). Here we show that analysis of the use of simple forms of digital advice such as 'standard' and 'smart' calculators in the choice of superannuation investment options, can assist with immediate decisions, but may not help people learn skills to apply when they confront similar problems later.

B8Q3. What reliable and robust data and evidence can trustees, and other providers collect on how their superannuation calculators or retirement estimates influence their members' behaviour or outcomes?

The best way to rigorously measure the impact on voluntary savings, investment switching and engagement of proposed presentation formats or approaches for retirement estimates, and calculators is via randomised control trials. In the absence of this approach, it is hard to establish causal effects.

Administrative panel studies using super fund member data (such as reported in Smyrnis et al., 2021) can help understand the influences of decision aids such as retirement estimates and calculators on member behaviour. However, comparison of average member data from different samples, without reference to a control (untreated) group is misleading. It is essential to follow the same individuals over time.

C3Q1. Is there evidence for how members understand or interpret differences in forecasts, either across types of forecast (superannuation calculators and retirement estimates) or across different trustees (or other providers of superannuation calculators)?

Our research shows that members respond differently to different formats for forecasts/estimates, such as investment outcomes including return and risk; and retirement estimates presented as income or lump sums (Smyrnis et al., 2021; Niam, 2021). In particular we have found that responses to risk presentation are highly sensitive to presentation format (Bateman et al., 2016b); presentation formats are interpreted differently by people with differing levels of financial literacy, numeracy and personal characteristics (Bateman et al., 2014); and people often use information designed by regulators in unexpected ways (Bateman et al., 2016a). We also find that retirement estimates presented as income streams or lump sums may have differing effects in accumulation and decumulation (Smyrnis et al., 2021; Niam, 2021).

Finally, we assert that it is unclear whether members will interpret returns presented without risk information (such as proposed in the Consultation Paper) as deterministic or random. Presentations of risky returns without associated risk information are possibly highly misleading to members. Our research suggests that people have difficulty understanding most common formats for risk presentation (Bateman et al., 2014; 2016b), so any risk information considered to be included with retirement estimates or calculators should be appropriately tested prior to implementation (Bateman et al., 2016a).

Attachment A: Abstracts of papers from our group mentioned in this submission

Bateman, H., Dobrescu, L. I., Newell, B. R., Ortmann, A., & Thorp, S. (2016a). As easy as pie: How retirement savers use prescribed investment disclosures. *Journal of Economic Behavior & Organization*, *121*, 60-76.

Abstract: Using a laboratory experiment, we study how retirement plan members choose investment options using five information items prescribed by regulators. We found that asset allocation information for pre-mixed investment options – normally presented as a pie chart or a table – had the largest impact on choices. Participants preferred investment options with more, and more evenly weighted, asset class allocations. This novel application of a 1/n strategy differs significantly from the existing findings of naïve diversification in 'mix-it-yourself' conditions where participants spread resources evenly across funds or categories. When asset allocation information was included, coefficients on return and risk information had unexpected signs, but when asset allocation was omitted, participants preferred options with high Sharpe ratios. We also demonstrate that none of the five prescribed information items was significant in explaining individual choices of more than 35% of participants. These findings highlight that information contained in prescribed investment disclosures might not be used in the manner intended by the regulator. The results raise important methodological questions about the way 'user-friendly' information prescribed by regulators is validated before being legislated.

Bateman, H., Eckert, C., Geweke, J., Louviere, J., Satchell, S., & Thorp, S. (2016b). Risk presentation and portfolio choice. *Review of Finance*, *20*(1), 201-229.

Abstract: Efficient investment of personal savings depends on clear risk disclosures. We study the propensity of individuals to violate some implications of expected utility under alternative "mass-market" descriptions of investment risk, using a discrete choice experiment. We found violations in around 25% of choices, and substantial variation in rates of violation, depending on the mode of risk disclosure and participants' characteristics. When risk is described as the frequency of returns below or above a threshold, we observe more violations than for range and probability-based descriptions. Innumerate individuals are more likely to violate expected utility than those with high numeracy. Apart from the very elderly, older individuals are less likely to violate the restrictions. The results highlight the challenges of disclosure regulation.

Bateman, H., Eckert, C., Geweke, J., Louviere, J., Satchell, S., & Thorp, S. (2014). Financial competence, risk presentation and retirement portfolio preferences. *Journal of Pension Economics & Finance*, *13*(1), 27-61.

Abstract: Financial regulators are weighing up the effectiveness of different templates for communicating investment risk to retirement savers since welfare depends on comprehension of risk information. We compare nine standard risk presentations using a discrete choice experiment where subjects choose between three retirement accounts. Switching between graphical or textual presentations, or between formats that emphasize benchmarks rather than return ranges or values at risk, affects predicted choices more than large changes in underlying risk. Innumerate individuals are more susceptible to presentation, and those with weak basic financial literacy are insensitive to increasing risk levels, regardless of presentation. Presentation effects are moderated but not eliminated as financial literacy improves.

Nian, R (2021). The Impact of Information Architecture on Decumulation of Retirement Savings. *Unpublished Honours Thesis, School of Psychology, UNSW.*

Abstract: Around the world, individuals consistently show tendencies of spending conservatively during their retirement. Policymakers and superannuation funds have become increasingly interested in understanding how to prompt retirees to spend feasibly. Previous research suggests that offering projections of future retirement wealth encourages individuals to increase their accumulation of retirement savings, so we flipped the setting and tested the effects of retirement projections in the context of decumulation of retirement savings (i.e., superannuation). Participants in our study received either no projection or retirement projections in different formats including, a lump sum wealth projection, income stream projection, or both projections. The results indicated that at the first choice, the average withdrawal amount of participants appears to adhere to the age pension they may be eligible to receive from the government, regardless of whether they received a projection and the projection format. Over the choice sets, receiving the income stream projection triggered a faster decrease in remaining superannuation compared to not receiving any projection. Overall, our findings provide preliminary evidence that policymakers and superannuation funds can prompt individuals to increase their withdrawal amounts during retirement by providing them with retirement projections in the income stream format.

Smyrnis, G., Bateman, H., Dobrescu, L. I., Newell, B. R., & Thorp, S. (2021). Motivated Saving: The impact of projections on retirement contributions. *Manuscript submitted for publication.*

Abstract: Can projections of retirement wealth and income motivate pension plan participants to save more? Results of field and online experiments show that participants who see both retirement balance and income projections increase voluntary savings in the first and subsequent years of treatment. In the field study, conducted by a large Australian pension plan in 2013-14, participants of the treatment group received current balance, projected retirement balance and projected retirement income information, while participants of the control received only current balance information. Within one year of the treatment, the frequency, and average amount, of voluntary savings by treated plan participants rose significantly, as did the rate of participants' interactions with the plan. These effects continued into the second year of the trial. In the related online experiment conducted in 2017, we tested the relative effect of information on (i) current balance; (ii) current balance and projected retirement balance; (iii) current balance and projected retirement income; and (iv) current balance, projected retirement balance and projected retirement income. Consistent with the field trial, the combination of retirement balance and income projections motivates a significantly higher retirement savings accumulation, after a sequence of ten savings decisions, than current balance information alone. Together our results strongly endorse recent changes to retirement plan benefit statement guidelines initiated by pension regulators globally.

Wang-Ly, N., Bateman, H., Dobrescu, L. I., Newell, B. R., & Thorp, S. (2021). Defaults, disclosures, advice and calculators: One size does not fit all. *Manuscript submitted for publication.*

Abstract: The effect of regulatory standards regarding the presentation of investment products on financial behaviour is poorly understood. In two incentivized online experiments (N = 2,221) we examine the impact of information-based and tool-based guidance on the selection of retirement plan investment funds. Participants chose between funds that followed identical investment strategies but charged different fees. Over multiple trials, participants were instructed to identify the fund which charged the lowest fees given their hypothetical plan balance. Defaults and disclosures were found to be situationally helpful, but highlighted participants' naivete with regard to the calculations underlying the fee structure. Advice tended to be underutilized but was beneficial when sought. Tool-based guidance in the form of a smart calculator had a moderate impact on accuracy but benefits did not persist. Together the results highlight the danger of taking a homogeneous approach to financial guidance and emphasize the need to build consumer competency.

Attachment B: Additional references on retirement projections (not from our group)

Dolls, M., Doerrenberg, P., Peichl, A., & Stichnoth, H. (2018). Do retirement savings increase in response to information about retirement and expected pensions? *Journal of Public Economics*, *158*, 168-179.

Fajnzylber, E., Plaza, G., & Reyes, G. (2009). *Better-informed workers and retirement savings decisions: impact evaluation of a personalized Pension Projection*, Working Paper No. 31, Superintendencia de Pensiones. https://ideas.repec.org/p/sdp/sdpwps/31.html

Goda, G. S., Manchester, C. F., & Sojourner, A. J. (2014). What will my account really be worth? Experimental evidence on how retirement income projections affect saving. *Journal of Public Economics*, *119*, 80-92.

Mastrobuoni, G. (2011). The role of information for retirement behavior: Evidence based on the stepwise introduction of the Social Security Statement. *Journal of Public Economics*, *95*(7-8), 913-925.

Villatoro, F., & Fuentes, O. (2017). Personalized Pension Projections: Effects on Workers Simulated and Actual Savings and Investment Decisions. Working Paper. Personalized Pension Projections: Effects on Workers Simulated and Actual Savings and Investment Decisions (researchgate.net)

Attachment C:
See zip file of our research papers discussed in this submission.