SAVING

Rewarding good behaviour

Getting people to put money aside for retirement is often a struggle against natural human impulses. Andy Knaggs **looks at what pension providers are doing to give people the necessary nudge to save**

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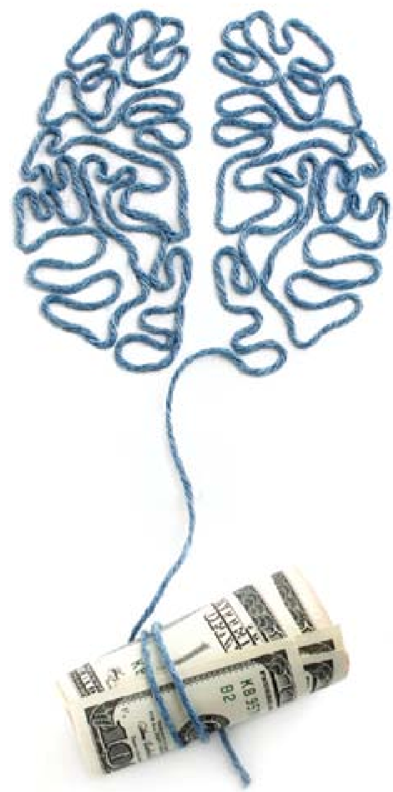
Behavioural finance leaped into the spotlight at the end of 2017, when pioneering US economist Richard Thaler was awarded the Nobel Memorial Prize in Economic Sciences for his work in the field. Thaler is renowned as the 'nudge' theorist, whose ideas on outflanking the inertia of the masses led to the UK's successful auto-enrolment project, with 7.5 million people enrolled in a workplace pension after five years of the implementation.



Human barriers

Impressive as the results have been in the UK example, however, nudge theory and other behavioural interventions are up against a powerful and complex foe, when it comes to battling human nature and driving increased engagement in, and contributions to, occupational pension schemes. Some deeply ingrained behavioural traits need to be overcome: present bias, for example, which is a preference for consumption today over saving for tomorrow; and anchoring, whereby pension contributors assume, often erroneously, that the minimum recommended contribution will deliver an adequate sum in retirement.

Across Europe there is a variety of approaches to occupational pension provision, ranging from mandatory (Denmark, for example) and quasi-mandatory schemes (Sweden and The Netherlands) delivering well-developed workplace pensions, to softer approaches with less government intervention, that might be ripe for auto-enrolment and other behavioural techniques that will drive greater response.

A number of European nations have watched auto-enrolment projects in the UK and elsewhere in the world (including the US, Canada, Chile and New Zealand) with considerable interest, according to PensionsEurope senior policy adviser Matthies Verstegen. "So far, auto-enrolment seems to be a success with only a small percentage of people opting-out, even though contribution rates will probably need to rise to deliver adequate pensions. Nevertheless, the Irish government is looking to auto-enrolment to boost pensions savings, and there is interest from other countries, especially where the workplace pension is not as well developed."

He notes, however, that behavioural economics has not been a major part of PensionsEurope lobbying of the European Institutions on behalf of its members. For example, it did not play a big role in the 2016 review of the EU rules covering pension funds, the Institutions for Occupational Retirement Provision Directive (IORP II). The directive focuses on the governance of pension funds and leaves policy choices where behavioural insights matter – for example on choice in accumulation and decumulation, as well as communication with members – to the individual member states.

"A lot of the pensions framework is still very much national, especially with tax being such a big part of it. It's very difficult to have cross-border provision," says State Street Global Advisors head of investment strategy, European defined contribution Alistair Byrne. "We are seeing some companies use the IORP structure to deliver a pension plan that can operate across borders. We have seen this in Belgium, for example, where individual compartments can be offered to employees, but those compartments still need to differ from country to country to comply with government regulations."

Go EAST

Given that the nations of Europe are not remotely in step with regards to approaches to workplace pension provision or current levels of engagement or contribution, it seems that central, national, government and the marketplace will provide the impetus and innovation for behavioural change.

Columbia Threadneedle's report *Mind the gap: Overcoming the cognitive barriers to saving for retirement*, recommends the EAST framework devised by the UK's behavioural insights team, established to pursue avenues in which nudge theory could be practically implemented, as a guiding tool for pension providers and policymakers. This suggests making pensions communication and engagement Easy (simplifying processes and messages), Attractive (personalisation and incentives), Social (encouraging public commitment via social networks, for example) and Timely (aligning attempts to change behaviour with moments of major personal change or special occasions).

The framework demonstrates that "by employing the simplest of tactics, even just changing the merest details to make an action simpler or outcome more attractive, behavioural interventions can often generate dramatic results", the report concluded.

Among those pension providers that seem to have followed at least some of this advice is Mercer, which has had great success in increasing engagement levels through the use of light-hearted, personalised videos. Its director of consulting Brian Henderson explains: "We know in the past that organisations have spent six-figure sums trying to communicate to people to get them to save more. Engagement levels were 4-5 per cent before they spent the money and 5-6 per cent afterwards.

"We worked with (US behavioural economist) Shlomo Benartzi on developing some ideas, and the highlight was personalised financial videos. They would say how much you and your company had paid in, what the pension was now worth, and what, based on the current level of savings, the future might look like. At the end was a very simple call to action: click here to increase your pension contributions.

"The results have been quite staggering. We have destroyed response rates of 6 per cent. The first company to use the videos was an engineering company. We sent them to thousands of employees, and in the first 24 hours, two-thirds had looked at it. In itself, that was amazing, but by the next day, half of those that had looked had increased their pension contributions. This turns engagement on its head. And those results have been repeated over and over."

One national initiative of note is the Dutch Pension3Days event, which takes place every October/November, and in 2018 will run for the eighth time. Aimed at providing consumers with information about their personal pension situations, and prompting them to take responsible behavioural action, the event draws participation from employers, financial advisers, and pension providers. Workshops, debates, plays and other interactive activities bring the subject to life. Messaging is targeted to core groups, such as age groups or the self-employed, to enhance the consistency of information and support offered.

As noted before, life stages can be an important trigger to the making of retirement plan decisions, with those such as moving house, getting married and having children being seen as key milestones where people will consider their future lives more readily. State Street Global Advisors works with a set of timelines, applied to auto-enrolled default pensions, which manage complex investment strategies for consumers, towards a target date that is appropriate to the person's lifestage.

Auto-escalation of contributions has also worked well in places such as the USA, although it is much less commonplace in Europe currently, and requires some heavy administrative lifting. "If people go from 0-10 per cent of their wages as a pension contribution straight away, that's quite a shock. So, don't do that; have them start at 2 per cent and have it escalate: 4 per cent the next year, then 6 per cent, and so on. That's very effective in getting people's savings rates up," says Byrne.

Getting smart

Technological advances in communication will very likely revolutionise how pension information is distributed. Already, the use of smartphone apps is starting to take off, and the power of personalisation can be harnessed in both print and digital channels. The future will be artificial intelligence and virtual reality, says Henderson.

"We're not quite there with AI but we are absolutely looking at it, and it's a fast-moving area. It will suit some people and not others. In two or three years' time we will be saying that the stuff we do now looks really old fashioned. With VR you will be able to touch and feel it almost. We have tried this before with aging software, showing what someone will look like in 20-30 years. It's fun but with a serious point, which is that they have to look after themselves." ■