

Costly Ignorance

Citation for published version (APA):

Eberhardt, W. (2018). *Costly Ignorance: Enhancing Consumer Financial Decision Making*. [Doctoral Thesis, Maastricht University]. Off Page Amsterdam. <https://doi.org/10.26481/dis.20180420we>

Document status and date:

Published: 01/01/2018

DOI:

[10.26481/dis.20180420we](https://doi.org/10.26481/dis.20180420we)

Document Version:

Publisher's PDF, also known as Version of record

Please check the document version of this publication:

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VALORIZATION ADDENDUM

If you would know today that your car has a 9/10 chance of breaking down in the future, would you buy an all risk car insurance? Probably yes. Of today's 30 year olds, 8 to 9 out of 10 will reach age 70 (Kiersz 2014), which is a 9/10 chance that they will reach retirement age. And yet, the majority of consumers in this group stays passive, and does not search for information on retirement in order to deal with the risk of insufficient retirement finances.

In this dissertation, I therefore look at one of the most challenging issues for policy makers and financial service providers in aging societies: how to activate more people to prepare for retirement, how to enhance consumer financial decision making. Avoiding taking action for retirement where it would be needed, ignoring essential financial information, or having too little knowledge to be able to handle a credit card in a responsible way are all examples of “costly ignorance”, as put in the title of my dissertation. In chapter 2 my co-authors and I employ a model to understand the underlying motives of pension plan participants to search for information about retirement, in chapter 3 we look at how communication framing can activate participants to take action for their retirement, and in chapter 4 we research how aging impacts the (non) cognitive skills we need to make wise financial decisions.

Next to the academic conferences in which I presented this research, I also frequently participated in Netspar (Network for Studies on Pensions, Aging and Retirement) discussion groups and conferences to disseminate our findings to a practitioner audience. As output commitment for the PhD funding we received from Netspar, my co-authors and I wrote two industry papers on chapter 2 and 3 of this dissertation. We received valuable feedback from industry members that we incorporated in the research design and interpretation of our findings. I elaborate further on what our findings mean in social and economic terms for society in the following.

Chapter 2 – Understanding Retirement Information Search: The Retirement Belief Model

In chapter 2, my co-authors and I look at why some pension plan participants search for information about their retirement while others do not. Before thinking about actions such as saving more, retiring sooner or spending less, participants need to know what they are currently saving, how they want to live later, and whether what they are saving will be enough to afford their desired lifestyle. In the past, financial service providers have mainly used socio-demographic factors to segment consumers and communicate with them accordingly. We take a broader approach and also look at the relative influence of beliefs, emotions and trust on the motivation to search for information.

Having conducted studies in two countries, the Netherlands and the UK, we can conclude that especially if participants perceive high benefits of information search (for

example experiencing a state of security when they are informed) and trust their pension provider, they are more likely to search for information. Our findings are highly relevant in these countries where the regulatory landscape surrounding pensions is changing. Both countries have experienced reforms recently such as the incremental increase of the state pension age (from 65 to 67 to a life expectancy adjusted age) in the Netherlands, and automatic enrollment in the UK. While automatic enrollment is surely an essential first step to ensure coverage, adequacy is the next challenge. More reforms are expected in the future and will put more responsibility and risk on the individual pension plan participant. Being informed about one's expected retirement situation is therefore getting more important. So understanding what drives consumers to search for information is essential to develop good communication in the following.

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Conducting the research, we worked closely together with an insurance company in the Netherlands, and a pension fund in the UK. These two pension providers use our findings to improve their communication. During frequent visits in which I presented my research to different audiences at the pension providers, we discussed several ways to apply the Retirement Belief Model we developed. Both pension providers want to adapt their communication by focusing on the participant, and we showed them which factors matter in their context. Analyzing results from two countries show for example that there are differences between participants and context specific factors such as perceived susceptibility, which do not play a role in the Dutch sample, but have a significant negative impact on information search in the UK sample. Perceived susceptibility, so the belief that one is vulnerable for having a pension gap, is also significantly higher in the UK. Other factors such as trust and perceived benefits play a positive, significant role in both countries. For pension providers in both countries, this implies that it is crucial to make people understand what they gain by looking up information. This may be more difficult in the Netherlands where participants have less choice than in the UK, but not less important. Recently, more and more pension plan participants in the UK have taken up their lump sums which is because of lack of trust in the system in light of current Brexit negotiations (Financial Conduct Authority 2017). Our findings underline the importance of creating trust around pension reforms as well, a responsibility that is shared by pension providers, governments as well as financial watchdogs such as the UK Financial Conduct Authority and Dutch Autoriteit Financiële Markten.

In addition, we used the Retirement Belief Model to segment pension plan participants (see Appendix of this dissertation). In the past, pension providers have mainly used socio-demographic characteristics to segment their participants. Taking a broader approach to segmentation by also including factors such as beliefs, emotions, and trust shows more differentiated segments, which really changed the mindset of the pension providers we worked with.

Chapter 3 – Framing the Future: Using Investment and Assurance Frames to Encourage Retirement Information Search

While I outline the factors that influence whether people search for financial information or not in chapter 2, I focus on how to improve pension communication in chapter 3. My co-authors and I chose to test a cost efficient communication: the way that emails are worded, or “framed”. We test two versions of an email: an investment frame, which emphasized that participants invest in tomorrow by looking up information, and an assurance frame, which emphasized that participants can assure themselves of insight into their pension. With the investment frame, 2.7% of participants clicked on an informational movie link while with the assurance frame, 6.7% clicked. Our findings exemplify that the frame that pension providers use has the power to double the response of participants. Assurance frames therefore prove to be an efficient low-cost alternative to expensive awareness campaigns.

Since the costs for pension communication are indirectly paid by participants’ contributions, it is in the pension providers’ interest to keep these as low as possible. The frames we develop are simple text frames that are ready-to-use in pension providers’ communication. These frames can easily and at low costs be applied to subject lines of emails, online and offline newsletters, campaigns, magazines and other elements of pension communication.

In the Netherlands, pension providers are required to communicate with their pension plan participants by law. In January 2017, the new European Pensions Directive came into force which gives member states until January 2019 to incorporate the directive into their legislation. One of the central points is clearer information and communication to participants of pension plans, underlining the importance of research on what communication works best to activate pension plan participants.

Chapter 4 – Aging and Financial Decision Making: The Benefit of Experience and Emotion

My final chapter is concentrated on one of the developments that make pension reforms necessary in the first place: aging of our societies. Due to medical innovations and overall improvement of living circumstances, people are getting older than ever before which means that the percentage of people in retirement age will also increase in the future. At the same time, the number of the financial decisions that consumers need to take increases as well and these decisions are getting more complex. News about older adults being the victim of financial fraud raises concerns about whether aging will play a positive or negative role with regard to financial decisions making. Previous research has shown that cognitive skills such as numeracy may decrease when we get older.

My co-authors and I look at how cognitive (numeracy and financial expertise) and non-cognitive (emotion and motivation to put effort in difficult tasks) factors influence financial decision making, and how age matters in these relationships. We find that across



all measures of financial decision making, older adults do better. What helps them especially with making financial decisions are their lower levels of negative emotions and higher levels of financial expertise: older adults have often experienced both positive and negative financial decision outcomes in their life, so they are better able to deal with it and focus more on the positive.

Our findings are in line with the aging and life span psychology literature, and show that aging can provide societies with advantages as well – if financial service providers and policy makers make use of this knowledge and create products, communications and programs such that both older and younger adults benefit. First, communications to older consumers should focus more on positive emotions and acknowledge that the audience has experience. Second, our research underlines the importance of numeracy and financial expertise, and therefore the importance of financial education in school and later on in working life. While financial literacy programs may not be the holy grail as recent research has indicated (e.g. Fernandes et al. 2014), just in time workshops on specific topics by employers or banks' children programs that introduce them to the world of finance can be a first step in improving consumers' numeracy and financial expertise, and therefore help enhancing their financial decision making. Third, more exchange and sharing experiences between older and younger people for example can help self-reflection of the elderly, and building up knowledge for younger adults. Dutch pension providers for example are currently experimenting with pensioners who tell their story to non-retirees in order to motivate them to think more about retirement. As we still have a relatively well-off group of pensioners at the moment, this sharing will be especially important and insightful in the future, when a large group of baby boomers (which is less well-prepared for retirement) retires.

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