

People who think annuities are 'fair' are more likely to buy one

By Editorial Staff Thu, Sep 27, 2018

People who worry about becoming a burden on family and people who are relatively less loss-averse are also more open to the idea of buying annuities, a study by UCLA and Duke behavioral economists showed.

A study by retirement researchers at UCLA and Duke found that older Americans who perceive annuities to be "fair" are the ones most likely to buy them. At the same time, they discovered that about one in five Americans ages 40 to 65 can be described as an "annuity hater."

"By far the strongest of all the individual differences we measured at predicting liking of annuities is the question of whether the individuals think annuities are 'fair,' wrote Suzanne Shu and Robert Zeithammer of UCLA and John Payne of Duke, three long-time contributors to research on the so-called "annuity puzzle."

"From a positive perspective for marketers of these products... this suggests that the annuity puzzle [i.e., the low demand for longevity insurance among retirees] is more a problem of perception than of the financial tradeoffs inherent in the product," they wrote.

Their [paper](#), "The Pivotal Role of Fairness: Which Consumers Like Annuities?" (NBER Working Paper 25067), also suggested that note their research conclusions might be useful "for financial planners hoping to help their customers with [their] decumulation challenges."

To determine perceptions of fairness, the authors first asked several hundred Americans ages 40 to 65 if they considered annuities "Completely unfair," "Acceptable" or "Somewhat Unfair." Then they asked them to indicate if they agreed or not with the following statements.

- I feel like I understand the life annuity market well.
- The system behind life annuities should be changed.
- I would avoid companies that sell life annuities if I could.
- It is clear where the money for this product comes from.
- It is fair that the company is allowed to keep the excess funds.
- I feel that I would have too little control over my retirement money if I bought an annuity.

"Prior research on consumer fairness has suggested that judgments of fairness are affected by the way that profits are shared between the firm and consumer, the intentions of the

firm, the firm's perceived wealth and power, and whether underlying costs are variable or fixed. In this project, our fairness measure was a simple one taken directly from [Kahneman, Knetsch, and Thaler](#) (1986)," the paper said.

The survey turned up two findings that diverged from past research. In this study, unlike some others, acceptance of annuities was found to be higher among people who were relatively less loss-averse and among those who had a strong wish to protect their heirs.

"Survey respondents... who clearly identify a family member as a potential beneficiary are significantly more likely to select annuities," the paper said. "This intriguing result could suggest instead that individuals who are worried about becoming a burden on family are more open to the idea of annuities; more research is needed to better understand the tradeoff between bequests and dependence."

At the same time, "Characteristics predicted to be important based on traditional economic models, such as health, life expectations, saved assets, and numeracy, are either insignificant or small in their effect," the paper said.

About one in five people in the study would never buy an annuity. "Some people simply dislike the idea of an annuity a priori, and are unwilling to consider these products even with a suggested substantial economic benefit," the authors wrote. The "annuity haters," as the authors called them, always said they would rather manage without an annuity than take any of the hypothetical annuity options offered to them.

The finding that 20% of people hate annuities doesn't mean that 80% of people intend to buy annuities, Zeithammer told *RIJ* in an email. "We define 'annuity haters' as people with a knee-jerk reaction to annuities, i.e. people who are rejecting even annuities with very high expected NPV. The opposite of 'annuity hater' is thus not necessarily an 'annuity lover.' For example, the 78% of people who are not 'annuity haters' includes people who pick only one or two annuities over the course of 20 choice-tasks."