
Who buys income annuities, and why most people don't: EBRI

By Editorial Staff Thu, Feb 9, 2017

"Those with inadequate assets might value a regular stream of income very highly and those with the most [assets] might expect to live longer and can also afford it even after leaving a bequest," the Employee Benefit Research Institute said in a release this week.

In a U-shaped market pattern, immediate annuities are usually purchased by those with either the most or least personal savings, according to a new [study](#) by the Employee Benefit Research Institute.

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Overall demand for retail immediate annuities may be low because they are crowded out by Social Security and defined benefit pensions, EBRI suggested.

"A large majority—more than 70%—of households that are currently receiving Social Security benefit already get at least three-quarters of their income in the form of annuities, from Social Security, employer-provided pensions, and other annuity contracts," said Sudipto Banerjee, EBRI research associate and author of the study. "The fact that most retirees are already highly annuitized might help explain the lack of demand for additional annuity income."

While the decline of defined benefit (DB) pension plan coverage has stimulated interest in other options for generating retirement income, demand for annuities has remained low in the United States. EBRI conducted its analysis to understand the public's preferences for such products, with a focus on how savings levels affect preferences for immediate annuities (which begin paying out a regular stream of income as soon as they are purchased).

EBRI used an experiment from the Health and Retirement Study (HRS) to assess the effect of savings on the preference for immediate annuities among retirees (ages 65 and above).

Regression results show that effect of savings on annuity preferences follow a U-shaped pattern, meaning that people at the bottom- and top-ends of the savings distribution (those with the least and most assets) have a stronger preference for such annuities than people in the middle of the savings distribution.

But savings has a large positive effect on preference for annuities only for those in the highest-savings quintile (the top 20% in the wealth distribution).

The study notes that possible explanations for such behavior could be:

- People at the bottom of the savings distribution are very likely to run out of money in retirement and thus have a stronger preference for annuities.
- People at the top end of the savings distribution expect longer lifespans and can afford annuities even after leaving a financial legacy for their heirs.
- People in the middle generally face more uncertainty about their retirement adequacy and so they are more likely to hold on to their savings for precautionary purposes and perhaps also for some hope of leaving a financial legacy for their heirs.

The EBRI results also show annuity purchasers usually opt to annuitize less than half of their savings. Only 16.5% of retirees (ages 65 and above) preferred full annuitization; 43% preferred a one-quarter annuitization.

The full report, "How Does Level of Savings Affect Preference for Immediate Annuities?" is published in the Feb. 8, 2017 EBRI Issue Brief, online at www.ebri.org.

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