These emotions get in the way of saving and planning for the future

Reasonable people can be illogical when it comes to saving and spending, says Dr. Marina Rain, PhD in psychology and manager of behavioural economics at Sun Life. "We often make irrational decisions that defy what traditional economic models predict, namely that our decision-making maximizes financial benefit."

The emerging science of behavioural economics is shedding light on the errors people commonly make around money, including their workplace retirement plans. Going from accumulation and earning income to decumulation and drawing a retirement income isn't just a financial transition, it's a highly emotional one. Many emotions get in the way of sound choices.

Dr. Rain helps design retirement products and accompanying information that enable plan members to make better choices. Plan sponsors and providers can support members in understanding the emotions that hinder or assist with retirement planning decisions that lead to positive action.

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Life's brighter under the sun

Group Retirement Services are provided by Sun Life Assurance Company of Canada, a member of the Sun Life group of companies.

Sun Life

1. Default bias

Our brains are wired to seek easy choices to expend less energy, Dr. Rain says. "Most people go with the flow."

That's one reason we tend to stick with the same choices for breakfast or replace a worn-out pair of jeans with the same familiar brand. Those are low-stakes decisions. Not all are. Default behaviour means carrying on as before, even when circumstances should dictate a change.

The current default or status quo for many Canadians is to not save for retirement. One role for plan sponsors is to help individuals set up new, beneficial default behaviours such as automatic deposits to group retirement plans.

2. Perceived hassle costs

We perceive complex activities as time-consuming and a hassle. Planning for retirement is filled with unknowns and lots of moving parts.

"As soon as we get a whiff of perceived effort, we're less likely to pursue it," Dr. Rain explains.

Breaking down retirement planning into small steps and simple language can counter the complexity. Plan sponsors can encourage discussions that start with broad retirement goals, the benefits of compounding interest, and saving in a group plan sooner than later. Digest that, and the details can follow.

3. The ostrich effect

Retirement planning often brings up negative emotions for plan members, from worries about aging, to whether they have enough savings. Most people would rather avoid these thoughts.

"Because of this ostrich effect, when people see an email with subject line 'plan for retirement,' they almost automatically pass over it," Dr. Rain says.

How can you avoid having plan members bury their heads in the sand? Dr. Rain says storytelling is often more effective at conveying retirement concepts. It makes the topic more relatable and less complex than just information backed by facts and figures.

4. Hyperbolic discounting

People value short-term rewards over long-term ones, even when the latter offer greater benefit. The desire for instant gratification is one reason why saving for retirement can take a back seat to, say, splurging on this year's winter holiday.

That's called hyperbolic discounting. Studies show that people would rather get $50 now than $100 next year. This discounting effect does not just pertain to money, it also affects how we perceive our future well-being, Dr. Rain says. "On a neurological level, brain activity when talking about our future selves looks very much like brain activity when talking about strangers."

Plan sponsors can make future selves feel more 'real' by helping members talk about their goals and dreams and imagine their future selves achieving them. "It creates a stronger emotional connection and a sense of responsibility – our future selves depend on our present actions," Dr. Rain says.

> "People value short-term rewards over long-term ones, even when the latter offer greater benefit. The desire for instant gratification is one reason why saving for retirement can take a back seat to, say, splurging on this year's winter holiday."

5. Choice overload

People may say they want more options, but they often feel overwhelmed by them. “That translates to avoidance. Our minds overload, and most of us walk away without making a decision,” Dr. Rain says.

Sponsors can consider the effectiveness of presenting plan members with fewer choices at a time for retirement planning, backed by concise, basic information.

“People may say they want more options, but they often feel overwhelmed by them. “That translates to avoidance. Our minds overload, and most of us walk away without making a decision,””

6. Social proof

When facing something new, such as retirement planning, we want to know how other people have handled the same situation. “We look to what others are doing for social proof,” Dr. Rain says.

One problem is that a lot of retirement messaging focuses on people who don’t save enough. If you assume everyone else isn’t saving, “there’s actually less pressure to save.”

Dr. Rain says messaging should focus on the many people who are saving smartly for retirement, and how, which offers beneficial social proof.

7. Loss aversion

Psychologically, saving for tomorrow can feel like losing money today. The perceived “loss” can loom larger than the actual gain. Such loss aversion is often even more profound at retirement, when individuals are reluctant to decumulate – to “lose” assets they’ve been accumulating for decades.

Dr. Rain says plan sponsors can promote the **SMART** approach to retirement planning, using **s**pecific, **m**easurable, **a**chievable, **r**elevant and **t**ime-bound goals. Research shows that plans using these criteria are more motivating and fulfilling, offering a clear roadmap with milestones to reach along the retirement journey.

8. The endowment effect

People overvalue assets they own, Dr. Rain says. “So when we have spent many years accumulating savings, at retirement it feels like a treasure we don’t want to let go of.”

Plan sponsors can help members see how their finances can support new daily rituals, along with bigger goals such as extensive travel. That realization can offer a better “sense of well-being and control over retirement,” Dr. Rain says, and make plan members more comfortable with this transition and the asset decumulation that inevitably comes with it.

9. Optimism bias

Plan members can be optimistic about many things in retirement, including high returns on investments, lower expenses, long lives and great health. These may or may not come to pass. To harness this optimism, plan sponsors can design their retirement plans using a framework called **EAST**: **e**asy, **a**ttractive, **s**ocial and **t**imely.

Easy might entail automated deposits or withdrawals to “reduce friction,” Dr. Rain explains. Attractive can mean infusing retirement plans with personally meaningful goals, like volunteering or summers at the cottage. The social component might involve framing beneficial actions such as estate planning as something everyone is doing. And timely might mean getting individuals to consider retirement when they’re most receptive, perhaps after returning from vacation, when memories of leisure are fresh on their minds.

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