

Getting stuck in the status quo

✓ Mike Edwards reveals how status quo bias may be preventing schemes from reducing their longevity risk

People have a strong tendency to want to stick with the status quo. Anything that involves change or disruption is therefore by nature uncomfortable for our brains. When it comes to pension schemes, it can be hard to move away from existing solutions or break out of old processes and to think about taking action to reduce risks that have not been dealt with previously. One risk that many schemes have yet to take action on is longevity risk. Longevity risk is the risk that members live for longer than expected, which means that pensions are paid for longer than expected, which costs more and means assets have to work harder and/or additional contributions are required.

Longevity risk can be significant and is often the key remaining risk in schemes that have otherwise reduced investment risks. Removing longevity risk can be very beneficial, but not all trustees or sponsoring employers explore all of the options available to them.

Thinking hard burns more calories

Status quo bias is seen as one of the most powerful biases in behavioural science. People prefer to choose options that are the most obvious or usual. Preference for the status quo is frequently irrational (from a conventional economics perspective) because it depends on which option currently makes up the status quo. Whenever we try to do something new, we meet resistance from our brains because we hate uncertainty. It has been argued that making changes causes our brains to burn more calories, and that from a survival standpoint our brains are always in favour of the low-calorie, low-thinking option. The status quo bias can

be one reason why people typically stay with the same bank for many years – we simply stick with what we have always known.

Change the status quo, reverse your preferences

In order to fight our tendency to stick with the status quo, we need to break our mental deadlock. One very effective way to do this is to think about the actions we are going to take as already being reality. For example – imagine that you already have no longevity risk in your scheme. Now make the argument for ADDING longevity risk into your scheme. Can you justify it? Difficult isn't it? When we look at our options and imagine that the action we want to take is already reality, it makes it easier to break out of our comfort zone, and to avoid getting trapped in the status quo.

Behavioural insights

Aon commissioned research with behavioural insight agency Behave London to look into the behavioural biases that can get in the way of decisions around reducing longevity risk. (For more information or a copy of the research please email talktous@aon.com.)

How can your scheme tackle status quo and other behavioural biases?

We have created a guide to help you understand what is involved at each stage of reducing longevity risk, and how you can tackle status quo bias. For trustees or sponsoring employers at the very start of their longevity risk management journey, this process and the steps needed are not always clear; the guide sets out the process for you.



It covers the four key stages of reducing longevity risk: deciding strategy – should you reduce or remove longevity risk?; engaging with the market to obtain pricing; selecting a provider; and completing your transaction.

Throughout, we explain the behavioural biases that can trip up both trustees and sponsoring employers and help you to navigate through them to make confident and informed decisions for your scheme. The step-by-step practical guide removes the ambiguity from risk reduction and gives trustees a map of what to expect. Aon works with huge numbers of schemes each year; we therefore understand that not everyone is familiar with all the options available to them. So, pick up a copy of the guide; it can help you understand the process without burning too many calories!

Interested in finding out more?

For more information on Aon's step-by-step guide or to register for your copy please email us at talktous@aon.com.



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