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Speaker: Sonja Kassenboehmer



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Financial Decision Making and Retirement: The Influence of Health and Cognitive and Non- cognitive Skills

David W. Johnston*, Sonja C. Kassenboehmer**, Michael A. Shields***

*ARC DECRA, Centre for Health Economics, Monash University

** Centre for Health Economics, Monash University

***ARC Future Fellow, Centre for Health Economics, Monash University

Motivation

- Research has shown that most people do not save enough for their retirement to maintain a comfortable lifestyle (U.S: Bernheim, Skinner and Weinberg, 2001; Lusardi and Mitchell, 2010; for Australia: Burnett et al, 2014)
- Households with same lifetime earnings hold very different amounts of wealth
- Common to make financial decisions that are irrational according to standard consumer finance theory (Agarwal and Mazumder, 2013)
- Critical to understand what shapes individual's behaviour related to financial decision making to prevent suboptimal behaviour and outcomes
- If people have suboptimal savings they are not prepared for health/unemployment shocks and retirement entry -> Pressure on age pension, new-start, medicare
- After recent financial crisis, policy focus on improving quality of household financial decision making
- Focus on the role of health, financial literacy, cognitive and non-cognitive skills in financial decision making

Papers on Financial Decision Making and Retirement

Paper No. 1: Who's calling the shots? Determinants of financial and economic responsibility within households

- We study the determinants of intra-household allocation of decision power over financial choices using a direct measure of financial decision making [HILDA]
- Who makes financial decisions is important for retirement wealth
- Special focus on health and cognitive skills important for ageing

Paper No. 2: The causal effect of education on financial decision making: Evidence from a national schooling reform

- We use the 1960/70's school reforms that increased compulsory school leaving age from 14 to 15 at various points in time in different states to use the differences in the minimum school leaving age laws as a source of exogenous variations in people's education levels

Papers on Financial Decision Making and Retirement

Paper No. 3: Alzheimer's and financial decision making

- How does (risk of) dementia affects people's ability to deal with finances [AIBL]

Paper No. 4: Effect of Mental Decline/Health Shocks on Savings and Investments

- We study the effects of Dementia/Alzheimer's/cognitive-decline on savings and investment decisions [ELSA]

Paper No. 5+6: Effect of non-cognitive skills and financial literacy on retirement wealth and insurance take-up [GSOEP+ELSA + NCDS]

Paper No. 1: Motivation

- Investment decisions are important in determining how much wealth is accumulated for retirement
- We see worse outcomes for women with respect to personal retirement savings and superannuation (Clare, 2004; Glass and Kilpatrick, 1998; Sunden and Surette, 1998) – usually attributed to low experience with financial decision making
- However if women are responsible for household financial decisions, savings and investment of the household are often greater and repayment of debt is more likely (Ashraf, 2009)
- Women also invest differently: more into education of the kids and housing (Thomas, 1990, Hoddinott and Haddad, 1995; Duflo, 2003)
- Increasing woman's decision making power may have positive effects on personal and household retirement wealth
- Crucial to understand what determines the allocation of intra-household decision making: black box

Paper No. 1: Research Question and Contribution

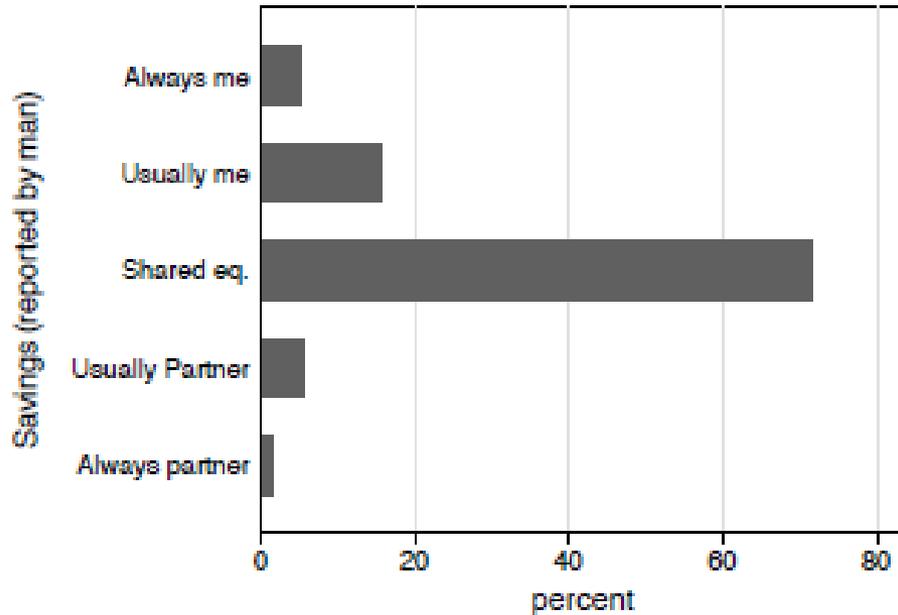
Research Questions

- What determines who is the financial DM? Standard economic variables such as education/wages? Cognitive or non-cognitive skills? Do households agree on who is the decision maker? Is DM responsibility fixed over the length of relationship? What influences changes in decision making responsibility when growing older (health shocks, financial shocks, baby, labour market shocks)?

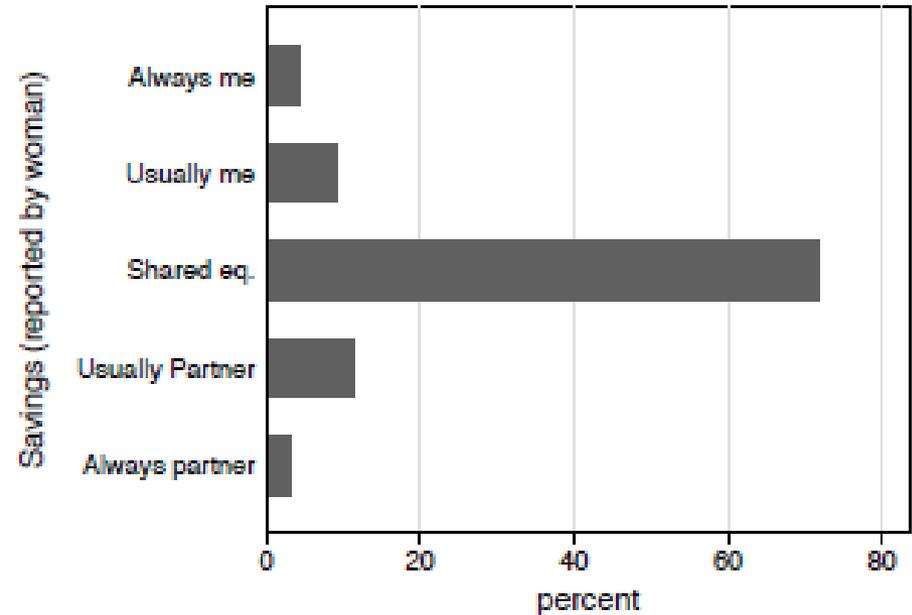
Contribution

- Unique information about intra household bargaining power from men and women for Australia: (1) savings, investment and borrowing; (2) large household purchases such as cars and major appliances
- DM responsibility reported by both men and women
- Information on health and cognitive and non-cognitive skills important for ageing process

Paper No. 1: Savings Decision Making Responsibility



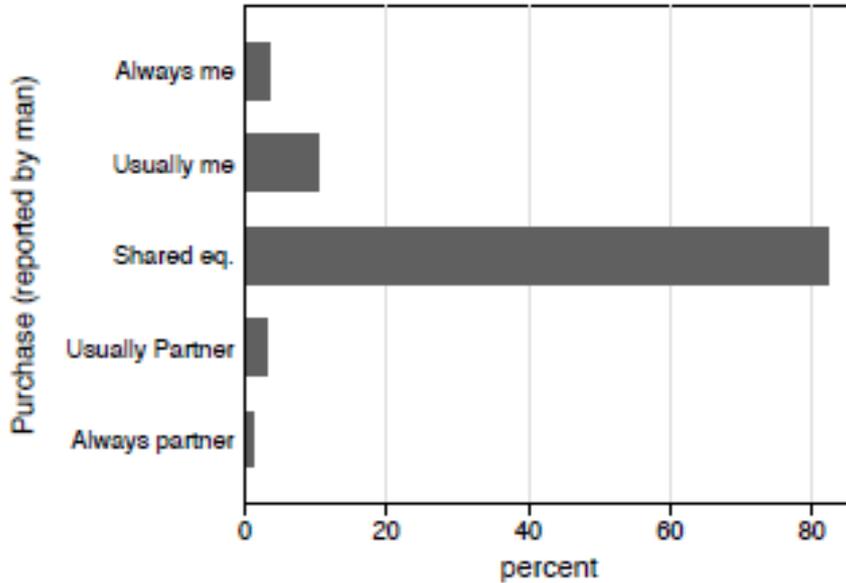
Reported by men



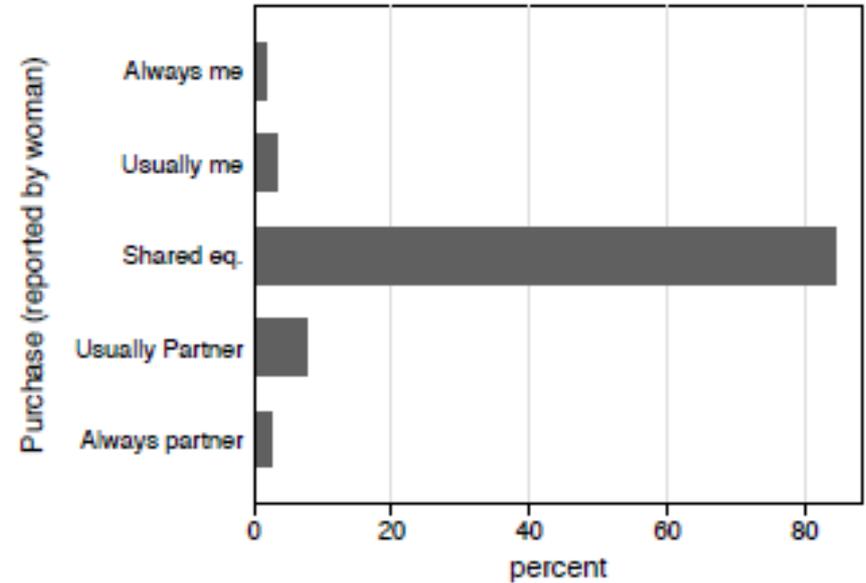
Reported by women

- Almost 70% agree
- 25% have minor difference

Paper No. 1: Purchases Decision Making Responsibility



Reported by man



Reported by woman

- Almost 80% agree
- 18% have minor difference

Paper No. 1: Results

Determinants of Disagreement

- Time-invariant unobserved factors most important for disagreement – most of the other effects are rendered insignificant in our fixed effects models: Disagreement is fixed over time and not influenced by a range of changes in characteristics such as wages, education, labour force status
- If mental health of man worse, more likely to disagree about financial DM

Determinants of DM responsibility

- Education and wages most important for DM responsibility allocation:
 - If man has higher education/wage than women, then man is more likely to be the DM
 - No effect for female's education/wages relative to men's
- Ability and personality (conscientiousness) increase DM power for both man and women

Paper No. 1: Results and Conclusion

Dynamics of DM responsibility

- Cohort effects: For older cohorts more likely that the man is the decision maker than younger cohorts
- However over length of the relationship, decision making very stable
- Only health shocks may alter responsibilities

Conclusions

- Good news: 75% agree on who is the decision maker and around 80% share decision making
- However, no simple solution for increasing DM power of women
- Once couples have agreed on DM power allocation, not much changes it
- However, health, cognitive and non-cognitive skills may influence DM power although difficult to target
- Given aging population, special support for older people with bad health and declining cognitive skills (typically men experience health shocks -> inexperienced women may be left with making important financial decisions)