



The psychology of decumulation

➤ **Callum Conway explores how pensions policy and product design can work with – rather than against – human behaviour**

Retirement, by definition, is a financial milestone – marking the transition from working life to life after work. It's tempting, then, to view it purely through an economic lens: Contribute early to a pension, save steadily, and drawdown sensibly in later life. Simple, right?

Not quite. While retirement may be a financial event, the decisions surrounding it are deeply human and often irrational. From procrastination and indecision to impulsivity and short-term thinking, our psychological wiring often works against us when it comes to managing pension savings.

Auto-enrolment (AE), introduced to workplace pensions across the UK in 2012, tackled one of the most powerful behavioural barriers: Inertia. By making pension saving the default, it removed the need for individuals to actively opt in – a clever use of human nature to drive long-term benefit, which has had remarkable success.

By contrast, pension freedoms – rolled out in 2015 – granted individuals greater flexibility over how and when to access their savings. But freedom brings complexity, and many savers continue to struggle with the burden of choice.

Hymans Robertson head of DC markets, Paul Waters, says the reforms drove a major behavioural shift: Pension pots are often spent earlier, despite surveys consistently showing that what people value most is a secure income that will last a lifetime.

The two reforms illustrate the extremes of behavioural design: One aligned policy with human nature, to great

success, the other placed responsibility back on individuals, with mixed results.

Why guidance falls short

In theory, guidance services such as Pension Wise should help bridge this gap. In practice, uptake remains stubbornly low. Procrastination, choice overload and low perceived relevance all deter engagement, even when guidance is free.

The deeper issue is that policy often assumes people behave like rational economic actors. In reality, biases such as inertia, loss aversion, present bias and framing frequently derail decision-making.

Indeed, Waters observes that “a large part of the design work and analysis carried out by the pension industry is framed around optimal behaviour and rational economic models”.

Oxford Risk head of behavioural finance, Greg Davies, agrees that the biggest challenge is helping people engage and act in the face of complexity.

“Retirement isn't just a financial shift – it involves a series of emotionally charged high-stakes decisions. Yet many people reach this point under-informed, anxious, and without the structured support they need,” he explains.

Research from the Institute for Fiscal Studies (IFS) backs this up.

Its 2025 study found many retirees feel overwhelmed by the decisions they face, with some withdrawing funds in full, defaulting into cash or delaying choices simply to avoid stress.

The Financial Conduct Authority (FCA) *Retirement Outcomes Review*

reached a similar conclusion.

Since 2015, over half of pots accessed have been fully withdrawn – most under £30,000 – while annuity purchases have plummeted.

In addition, around 30 per cent of drawdown plans are now chosen without advice.

Davies says this creates a contradiction at the heart of UK pensions policy.

“While the success of AE is built on the behavioural truth that most people will not get around to saving unless the decision is made for them, we flip the model at retirement – presenting them with a maze of drawdown options, tax rules and investment risks, and expect them to make good decisions entirely on their own.”

“Defaults,” he argues, “are needed at retirement just as much as at enrolment, but must be flexible, offering strong nudges and safeguards for the disengaged while giving choice to those who want it.”

The nastiest, hardest problem

Decumulation is what Nobel Prize winner, William Sharpe, once called the “nastiest, hardest problem in finance”.

XPS senior investment consultant, Neil Maines, believes behavioural biases are central to addressing it.

One clear example, he notes, is decision paralysis – the tendency to freeze when faced with too many choices.

He describes how this has manifested in many members holding their entire decumulation pot in cash and drawing far lower amounts than they can afford.

Encouragingly, Maines says that

while decumulation design is still in its infancy, mechanisms to counter biases such as decision paralysis are emerging in the UK.

Guided retirement plans, targeted support, and 'flex and fix' income strategies all offer ways to reflect the varied needs of members.

Meanwhile, pensions dashboards and open finance could help reduce retirement complexity, helping savers to make more confident decisions.

Still, Maines cautions that progress will be iterative, and its unlikely solutions will hit the mark the first time.

"That makes it critical that providers sandbox decumulation strategies in advance – but even more importantly, that they collect a holistic set of metrics once the solution is in operation, to determine whether recalibration is needed," he explains.

With this in mind, Maines urges the industry not to let perfection become "the enemy of the good".

"Guided retirement solutions will by definition not be the panacea to the decumulation puzzle, and it's counter-productive to expect this," he adds.

Looking ahead, some believe that the proposed Pension Schemes Bill, which introduces default retirement solutions with built-in longevity protection, could mark a turning point.

Key behavioural biases in retirement

• Inertia

People delay or avoid decisions altogether, even when action is clearly needed.

• Loss aversion

The fear of losing money often outweighs the potential for gains.

• Choice overload

Too many options create paralysis.

• Present bias

Immediate rewards are valued over future security.

• Framing effects

The way options are presented influences decisions.

Waters welcomes the shift in policy, describing it as a "win for common sense" and a "move away from financial ideology to pensions policy designed for humans".

"Behavioural insights are now essential infrastructure in product design and oversight under consumer duty," he continues.

"AE shows how defaults can work, as people retain freedom to opt out, and the same principle can apply in decumulation.

"Develop a strong default that can work for most people, while leaving them the flexibility to do something different," adds Waters.

"Retirement isn't just a financial shift – it involves a series of emotionally charged high-stakes decisions"

The psychology of spending

Behavioural finance also helps explain how retirees spend.

"People are influenced by instinct, emotion and mental shortcuts, sometimes without realising it," suggests Pensions Policy Institute (PPI) senior policy analyst, John Adams.

He warns that these behaviours can have lasting consequences.

Loss aversion, for instance, often drives under-spending.

Research from Ignition House found 70 per cent of mid-retirees are more cautious with money than before, with a third spending less than they could.

By contrast, over-confidence and present bias can push others into over-spending, with three-quarters of savers in the UK underestimating their longevity.

Framing plays a role too, with the presentation of a choice influencing the decisions people make, even if the underlying facts are identical.

For example, annuities, often

dismissed as poor value, are judged more favourably when described as "long-life insurance", according to Ignition House.

Adams says design features in pension products can help overcome some of these negative human behaviours.

"Built-in transition points to guaranteed income can counter the risks of overspending, while steady withdrawal frameworks can help those prone to underspending feel confident in using their savings," he argues.

The policy analyst also advocates for products that avoid sudden income changes or return unused funds to estates, as they can work with status quo bias while protecting long-term income.

"Alongside these, amid-retirement check-up reviewing income, spending and life expectancy assumptions, could lead to adjustments while people still have flexibility," Adams concludes.

Designing for humans

The message is clear: Behavioural finance is no longer peripheral in pensions policy; it is central. AE demonstrated the power of aligning policy with human nature in accumulation. The challenge now is to build the same behavioural scaffolding around decumulation.

That means recognising that rational optimisation is rarely how people behave, and therefore pensions must be designed for humans, not economists' models.

However, as XPS, Hymans Robertson and the PPI all emphasise, solving the "nastiest, hardest problem" of decumulation will take time and testing.

But with dashboards on the way, consumer duty expectations strengthening, and default pathways gaining traction, the industry has more tools than ever to work with.

If used well, they could make the path to better retirement outcomes not only clearer, but also more human.

 Written by Callum Conway