

Evaluating the Advanced Life Deferred Annuity – An Annuity People Might Actually Buy

Guan Gong
Anthony Webb
6 April 2008

ABSTRACT

Although annuities provide longevity insurance that should be attractive to households facing an uncertain lifespan, rates of voluntary annuitization remain extremely low. We evaluate the Advanced Life Deferred Annuity, an annuity purchased at retirement, providing an income commencing in advanced old age. Using numerical optimization, we show that it would provide a substantial proportion of the longevity insurance provided by an immediate annuity, at much lower cost. At plausible levels of actuarial unfairness, households should prefer it to both immediate and postponed annuitization, and an optimal decumulation of unannuitized wealth. Few households would suffer significant losses were it used as a 401(k) plan default.

JEL Codes: G11, J14, J26

Key words: annuity, longevity insurance, Advanced Life Deferred Annuity

Guan Gong, Shanghai University of Finance and Economics, 777 Guoding Road, Shanghai, People's Republic of China ggong@mail.shufe.edu.cn Anthony Webb (corresponding author): Center for Retirement Research at Boston College, Hovey House, 258 Hammond Street, Chestnut Hill MA 02467 webbaa@bc.edu. We would like to thank Garth Bernard, Timothy Benedict, Moshe Milevsky, and Alicia Munnell for very helpful comments and Wei Sun for research assistance.

The research reported herein was performed pursuant to a grant from the U.S. Social Security Administration (SSA) funded as part of the Retirement Research Consortium.

The findings and conclusions expressed are solely those of the authors and do not represent the views of the SSA or any agency of the Federal Government, or Boston College.