

Internal transfer of longevity risk in households and its impact on household ability to participate in pension-related capital market

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Abstract

This article shows how internal transfer of life-length risk between household members may influence their ability to participate in pension-related capital market. The approach is based on a model of two-person household (or a household with two decision makers if more household members are considered). An original proposition of life-length risk aversion interpretation is used in the model, which facilitates significantly optimization of financial plan. Moreover, the model allows to reduce costs of pension plan contributions, which makes more households able to afford participation in systematic-investment programs. In the two-person case, two types of life-length risk need to be taken into consideration, namely - longevity risk and premature death risk. These two types of risk sometimes simply add, but in many cases rather offset. This contributes to portfolio diversification effect in the analysis of joint household risk, smoothing out differences in age, sex or job incomes between household members.

Key words

HOUSEHOLD, RISK AVERSION, FINANCIAL PLANNING, LONGEVITY RISK, PREMATURE-DEATH RISK

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