Retirement Income
JOURNAL

Does end-of-life family care ‘crowd out’ annuities?

By Editorial Staff *Thu, Oct 9, 2014*

In their study, “Annuitized Wealth and Post-Retirement Savings,” John Laitner and Dmitriy Stolyarov of the University of Michigan and Daniel Silverman of Arizona State call these late-life inter-family transfers “non-market annuities.”

Puzzled by conflicting data about the way that healthier, wealthier Americans dispose of their money in retirement, a team of three economists has proposed that, when these retirees become ill or disabled, many of them spend down their liquid savings to pay relatives for care.

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“The presence of non-market annuities can reconcile evidence of apparently thin annuitization with the relative paucity of bequests observed in inheritance surveys,” they write, concluding that:

“Informal arrangements in which elderly households in poor health status exchange liquid assets, perhaps inter vivos, for in-kind assistance from grown children and other relatives provide implicit annuity protection that may have substantial value and be widespread in practice.”

En route to this conclusion, the economists tried to reconcile several pieces of evidence about retirees who are healthy and have ample income from a combination of Social Security benefits and defined benefit pensions—two characteristics that statistically tend to go together.

These individuals tend to *increase* their hoard of liquid assets in retirement rather than spend it down or buy retail annuities with. Yet, when they die, fewer members of this group provide bequests to family members than you might expect.

So where does the hoarded money go? To pay relatives for late-life informal medical care, according to this paper.

The economists go so far as to call these payments “implicit” annuities. The implied annuities, according to this model, consume all or most of the retirees’ liquid assets. They present a kind of shadow annuitization that doesn’t show up in any statistical record.

“We might expect to see almost 100% of households leaving (accidental) bequests…. Yet only 20-40% of households report an inheritance,” the authors write. “Non-market annuities can provide the reason, as follows: a household that contracts with relatives for care obtains an implicit annuity; therefore, annuitization can, by the last stage of life, be far more widespread than purchases of market annuity instruments suggest.”

The authors suggest that these implied annuities crowd out the purchase of retail annuities, and would do so even if retail annuities were cheaper.

“When household portfolio options include standard annuities at retirement, non-market annuities at the last stage of life, and liquid assets at all ages, we find that non-market annuities tend to dominate standard annuities (even if the latter have zero load),” they write.