
Forgetful Elderly Should Own Income Annuities: Harvard Study

By Editor Test *Wed, Sep 9, 2009*

"People don't know what to do with their money in general," one advisor told Pensions and Investments. "It may get worse the older you get, but really this is a problem for all workers."

An authority on behavioral economics at Harvard has found that the rate of dementia among Americans "explodes" after age 60, doubling every five years to more than 30% of the population over age 85, *Pensions and Investments* magazine has reported.

And even adults without dementia experience "substantial cognitive impairment," making it difficult for them to manage their portfolios. Analytic cognitive function, according to the research, falls by about one percentile per year after age 20.

Nearly half of the population between 80 and 89 has dementia or cognitive impairment, according to a forthcoming paper, "The Age of Reason: Financial Decisions over the Life-Cycle with Implications for Regulation," by Harvard professor David Laibson.

"This is a huge problem, and we're really doing nothing to prepare for the large number of wealthy Americans nearing retirement," Laibson told *P&I*. "In fact, we've really gone the opposite way, by encouraging and liberating people to take care of their own finances."

Mandatory annuitization could help solve the problem, he said. "The vast majority of data says 30% to 40% of an individual's portfolio should be put in a reasonably priced fixed-income annuity," he said, adding that the U.S. should study the mandatory annuitization system in the U.K. "The issue is to make sure the financial services industry doesn't come up with solutions that are too costly."

According to the paper, the degeneration of a person's cognitive function can lead to poor financial decision-making. For example, research showed that middle-age adults tend to borrow at lower interest rates and pay fewer fees relative to investors who are either younger or older.

Younger borrowers tend to have high analytic function but little experience, while older borrowers have lots of experience but lower levels of analytic function, the report noted. Averaging across 10 credit markets, fee and interest rate payments are at their lowest among investors around age 53.

While the new research highlights the inability of older adults to make financial decisions, one financial consultant says most adults have difficulties managing their retirement portfolios. "People don't know what to do with their money in general," he said. "It may get worse the older you get, but really this is a problem for all workers."