The Annuity Puzzle

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**Defined Benefit Plan**
- Median Income in Virginia: About $75,000
- Works for the same employer for 20 years.
- Annual pension equals about $30,000 ($75,000 x 2% x 20)
- Monthly income: $2500

**Defined Contribution Plan**
- Median Income in Virginia: About $75,000
- Recommended Savings: $600,000 (Income x 8)
- If withdraws 4% annually, annual income about $24,000
- Monthly income: $2000
- Use $500,000 to buy a single life annuity, est. monthly payment: $2500
Reasons People Might Not Purchase an Annuity:

1. Failed to save sufficient funds to buy one
2. Motivated to leave a bequest to their heirs
3. Need to deal with health shocks – illiquid
4. Concerns about whether an annuity is a good investment
5. Concerns about the financial viability of the firm offering the annuity
6. Overestimating their ability to manage their funds in retirement
Reasons People Might Not Purchase an Annuity (cont.):

7. Too much choice which causes inertia:
   - Fixed annuities
   - Variable annuities
   - Equity-indexed annuities
   - Guaranteed annuity contracts
   - Two-tiered annuities
   - Annuities with death benefit options
   - Deferred vs. immediate annuities
   - Qualified vs. non-qualified annuities
Growing Alternatives or Substitutes for Annuities:

1. Reverse Mortgages
2. Managed payout funds or income replacement funds offered by mutual fund companies