Abstract:

Why are pension products so complicated?

In a defined contribution pension scheme,

the final pension amount depends not only on the amount paid into the pension but also on the performance of the

individual specific investment strategy. Due to the involvement of financial advisers, asset managers and insurance companies, finding the optimal investment strategy is often complicated and expensive.

In this talk, I will propose a new way of handling and communicating the risk of uncertain pension income.

The key point is that by allowing the customer to propose a lower and upper bound, he effectively reveals his risk aversion.

This in turn leads to a simple investment strategy where everyone invests into the same derivative.

 Risk is balanced by the individual proportion that is invested into the risky derivative.

The investment optimization will be done by maximizing the expected utility of the final pension amount

under an exponential utility function. I will present properties and results in a simple Black-Scholes world,

and also compare those results to a power (isoelastic) utility function optimization.