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Money-Back Guarantees in Individual Retirement Accounts: Are They Good Policy?

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WORKING PAPER 26406

DOI 10.3386/w26406

ISSUE DATE October 2019

REVISION DATE December 2024

Pension products embedding guarantees have been adopted worldwide, including in the Pan-European Personal Pension Products (PEPP) recently launched in the European Union. Using an economic life cycle model where investors have access to stocks, bonds, and tax-qualified retirement accounts, we show that abandoning the guarantee could enhance old-age consumption for over 75% of retirees without harming pre-retirement consumption. Life cycle funds offer an alternative for capital preservation, but they would produce lower average payouts. Investors averse to equity losses accumulate only moderately more in guaranteed accounts, as these offer only limited protection against market crashes.

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