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The Valuation of Guaranteed Lifelong Withdrawal Benefit Options in Variable Annuity Contracts and the Impact of Mortality Risk

Gabriella Piscopo Ph.D. & Steven Haberman

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Abstract

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Scholes framework to insurance contracts, assuming the fund follows a geometric Brownian motion and the insurance fee is paid, on an ongoing basis, as a proportion of the assets. We develop a sensitivity analysis, which shows how the value of the product varies with the key parameters, including the age of the policyholder at the inception of the contract, the guaranteed rate, the risk-free rate, and the fund volatility. We calculate the fair fee, using Monte Carlo simulations under different scenarios. We give special attention to the impact of mortality risk on the value of the option, using a flexible model of mortality dynamics, which allows for the possible perturbations by mortality shock of the standard mortality tables used by practitioners. Moreover, we evaluate the introduction of roll-up and step-up options and the effect of the decision to delay withdrawing. Empirical analyses are performed, and numerical results are provided.

Related Research Data

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