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Prudence, risk aversion, and the demand for life insurance

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Abstract

We estimate the effect of household wealth on the demand for life insurance using survey data from a broad cross-section of the USA. This procedure allows us to test the Pratt-Arrow hypothesis of decreasing absolute risk aversion (DARA). Additionally, we estimate the relative magnitude of prudence, the propensity to take precautions when faced with risk. We find that life insurance purchases increase with wealth, and that on average American households exhibit about 94 per cent as much prudence as risk aversion. On the basis of this evidence, we reject the DARA hypothesis.

Related Research Data

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Precautionary Saving in the Small and in the Large

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Gender-Based Differences in Life Insurance Ownership

Source: Journal of Risk & Insurance

A test for the presence of precautionary saving

Source: Economics Letters

Absolute and relative risk aversion: An experimental study

Source: Journal of Risk and Uncertainty

The Demand for Life Insurance: An Application of the Economics of Uncertainty

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