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Leibniz Institute for Financial Research SAFE

Dear Sir or Madam,

Welcome to the latest edition of SAFE Update, the Leibniz Institute SAFE digital newsletter. In this issue, we focus on concrete steps to improve the pensions system in Germany and look at research into investors' timing preferences.

We hope you find this newsletter of interest and would welcome your feedback to the editorial team at newsletter@safe-frankfurt.de.

Focus: How to improve Germany's pensions system

Financially viable and feasible measures are needed and possible

Germany's pensions system is in jeopardy. Due to the aging of German society and a historically long phase of low interest rates, many citizens face potentially inadequate pension provision. However, there are ways for decision makers to implement countermeasures quickly and effectively, as a post on the SAFE Finance Blog explains.

In their contribution, SAFE researcher Andreas Hackethal and SAFE Fellow Raimond Maurer suggest that policy makers take action in the following areas: the existing statutory pension system, a new “equity pension from birth”, the current “Riesterrente” supplementary pension scheme, and pension planning.

According to the authors, one possibility to improve incentives for voluntary later retirement is to offer an actuarial fair lump-sum payment for those opting to defer the point at which they start claiming their pension. Such a technically simple but effective measure does not involve pension cuts or additional costs for the state pension system, while at the same time providing a demonstrable benefit in that more people take advantage of this offer and work longer, the researchers argue.

The “equity pension from birth” is conceived as a state-financed single premium paid into an individual retirement account for all new-borns. The funds from this custody account are invested in a fiduciary capacity in globally diversified equity-portfolio and funds and are not paid out until retirement.

From the researchers’ perspective, in its current form, the existing “Riesterrente” supplementary pension scheme no longer represents an attractive and sustainable pension model. As such, there is no reason not to adjust the contribution guarantee: if government subsidies are withdrawn, but the minimum pay-out at the end of the contract term for personal contributions remains guaranteed, significantly higher equity exposures and returns can be achieved, even within a persistent low interest rate environment, argue the authors.

Finally, the authors would welcome a centralized digital pension overview in order to provide support for active pension planning; further, they suggest promoting “data trustees” who would offer people help in taking retirement-related decisions at an early stage

[Find the SAFE Finance Blog post here]

Research Highlight: Investor's timing preferences

Implied Volatility Duration: A Measure for the Timing of Uncertainty Resolution

by Christian Schlag, Senior Researcher at SAFE, Julian Thimme, Karlsruhe Institute of Technology (KIT), and Rüdiger Weber, WU Vienna.

In SAFE Working Paper No. 265, which has recently been published in the Journal of Financial Economics (Vol. 140, Issue 1), the authors investigate the timing of uncertainty resolution. Their results show that, between late and early resolution stocks, there is an average return differential of more than five percent per year. This leads them to conclude that investors are likely to prefer early resolution of uncertainty (PERU), such that they require higher average returns on late resolution stocks as a compensation. In terms of investor preferences, the authors show that investors actually need to exhibit PERU for "late" stocks to have higher returns than "early" stocks.

By measuring the return differential between stocks featuring late and early resolution of uncertainty and interpreting the difference as an indication for PERU, the authors can learn about investors' timing preferences.

To measure early or late resolution, the authors suggest a new approach by introducing the concept of "implied volatility duration" (IVD). The larger the share of total uncertainty that is resolved later, the higher the IVD value. According to the authors' findings, stocks with a higher IVD indeed feature higher average returns, representing a strong indication in the data for a premium for the late resolution of uncertainty.

By providing empirical evidence consistent with a substantial preference for early resolution of uncertainty, the paper presents valuable insights regarding a concept that is of great importance in asset pricing.

Find the research paper here

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Outlook
Among other international academic institutions and central banks, SAFE will co-organize the 8th International Conference on Sovereign Bond Markets on 7 and 8 April 2022, hosted by the Bank of England. The title and detailed program of the conference along with the registration form will soon be available here.

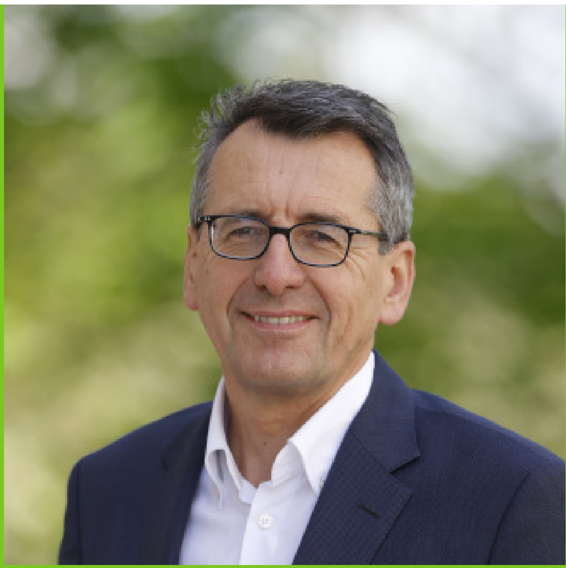
Review
SAFE and the Centre for Economic Policy Research jointly organized a SAFE-CEPR Policy Web Seminar with John Fell, Deputy Director General Macroprudential Policy & Financial Stability at the European Central Bank, who presented and discussed the latest ECB Financial Stability Review (FSR) with SAFE researcher Loriana Pelizzon. The FSR periodically assesses the financial stability vulnerabilities and their implications for the functioning of financial markets, debt sustainability, bank profitability, and the non-bank financial sector in the Euro area.

Read the follow-up report and rewatch the video here.

Handpicked

SAFE Director Jan Pieter Krahnen recommends a replication exercise published in this year's *Journal of Finance* Vol. 76, No. 5:

"Why believe in science when so many academic studies exist for every possible question and when there is disagreement between the findings? Is scientific evidence just an opinion among other opinions, as those who talk of 'alternative facts' would have us believe? Scientific evidence is based on systematic methodological analysis and so can in principle be subjected to replication. Over many years, I have asked students to replicate published papers in order to solidify the findings in the original and to find out whether small variations in the study design or the data set used have an impact on the findings. If yes, the original findings are not robust – and the replication exercise may be the starting point for their next big project. The disciplining power of replication can be gauged from the short letter written by the authors of an article published one year before who retract their piece because of a failed replication exercise."



Find the article here

News & Latest

- **News:** Alexander Hillert takes up new professorship for Finance and Data Science and coordinates the SAFE Research Data Center
- **Video:** SAFE-LawFin Policy Workshop “Pacemaker Brussels?”
- **SAFE Finance Blog:** A European regulation of credit scoring? (by Katja Langenbucher)
- All upcoming events and SAFE publications

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