

Pricing Mortality-linked Securities with Dependent Lives under the Multivariate Threshold Life Table

Hua Chen, Samuel H. Cox, and Jian Wen

Hua Chen

Department of Risk, Insurance and Healthcare Management
Temple University
1801 Liacouras Walk, 625 Alter Hall
Philadelphia, PA 19122
Phone: (215) 204-5905
Fax: (215) 204-4712
Email: hchen@temple.edu

Samuel H. Cox

Warren Centre for Actuarial Studies and Research
University of Manitoba
181 Freedman Crescent
Winnipeg, Manitoba R3T 5V4, Canada
Phone: (204) 474-7426
Fax: (204) 474-7545
Email: scox@cc.umanitoba.ca

Jian Wen

Chinese Academy of Finance and Development
Central University of Finance and Economics
39 College Road South, Haidian,
Beijing, 100081
Phone: 0086-10-62288275
Fax: 0086-10-62288779
Email: jwen@cufe.edu.cn

Abstract

In the standard insurance industry practice, actuaries usually assume independence of lives when valuing mortality-linked securities that more than one life, say, couples, are involved with. Empirical studies, however, have illustrated a significant dependence between joint lives. Another pitfall in traditional insurance pricing is that life tables are usually closed at an earlier age due to the inaccuracy and unavailability of data. The increasing number of supercentenarians makes the old-age mortality modeling crucial to life insurance industry. In this paper, we adopt copulas to capture life dependency, and establish the multivariate threshold life table for dependent lives. We use last-survivor annuities and reverse mortgages as pricing examples to illustrate the effectiveness of our model framework. Assuming independence of lives overestimates annuity values, while using traditional life table underestimates annuity values.