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## An Interview with Wharton Professor David Babel - Part One

By [tom](#) - Posted on **26 July 2009**

This is the first part of an interview with Wharton Professor David Babel.

Professor Babel led the [fixed indexed annuity](#) study that is discussed in several previous posts on Annuity Digest. These posts can be accessed by clicking [here](#).

Part 2 of this interview will be posted later this week. Annuity Digest would like to thank Professor Babel for spending time with us for the interview.

**Annuity Digest:** If you had a friend who knew very little about [annuities](#) or [investing](#), how would you communicate the gist of this study and its results to that person? In other words, the study was presumably developed for an industry and academic audience. What would you want or expect a [consumer](#) audience to take from the study? Is there a sort of distilled message that could be drawn from the study for a consumer audience?

**Professor Babel:** The genesis of the study is as follows. There has been a lot of misinformation in the popular press regarding FIAs. The vast majority of newspaper and magazine accounts vilify FIAs based on the results of alleged academic studies. The in-depth studies we conducted took over two years to complete and involved six Ph.D. financial economists and a pair of very well known senior actuaries. Our studies show that the products of at least some of the companies in this field are viable – indeed, rather attractive products. Our findings regarding actual products show that since their inception in 1995, they have performed quite well – in fact, some have performed better than many alternative investment classes (corporate and government bonds, equity funds, money markets) in any combination.

**Annuity Digest:** What was the catalyst for the study? What drove your curiosity? Was it the seeming disconnect between conventional financial media coverage of FIAs and what you thought might exist from a performance standpoint?

**Professor Babel:** FIAs hit the market like a storm and soon become one of the most popular [insurance](#) products. I had done several studies on deferred annuities prior to the arrival of FIAs in 1995, and had a natural curiosity to study the structure, behavior and performance of these new varieties.

**Annuity Digest:** [Asset decumulation](#) is front and center for a number of reasons— including demographics, social security/public policy, the financial crisis, etc. What role can professionals in academia play in changing the manner in which consumers are informed about annuity products and in overcoming some of the misperceptions and behavioral hurdles that exist in the industry?

**Professor Babel:** On the one hand, you have sales people and insurance marketing efforts to describe FIAs in a favorable light. On the other hand you have class action attorneys who do what they can to vilify FIAs. State regulatory bodies, appropriately, do not typically take a stand, one way or the other, except with regard to whether the products comply with regulations and whether the sponsoring companies meet solvency requirements. The Federal Government and [FINRA](#) have never regulated these products and currently have no expertise to comment, credibly, about the merits or defects in these products. Academicians generally “do not have a dog in this fight” and can look at the products dispassionately. They are not seeking to sell any products, nor expand their regulatory empires. Their studies are peer reviewed by disinterested experts. Therefore, the studies done in academia should not be fraught with bias one way or the other. Typically, academicians take years to study

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ABOUT THE AUTHOR



**Name**

Tom Cochran

**Biography**

Thomas Cochran, CFA, is the founder of [Annuity Digest](#). Tom launched his first company, Cordova Advisors, in 2002. The company was acquired by Vimo, a start-up focused on providing consumers information on healthcare products and services. Tom served as VP of Partnerships at Vimo for the past three years. Prior to his entrepreneurial endeavors, Tom worked as a VP at what is now Wells Fargo [Insurance Services](#), and he began his career at AIG. Tom is a chartered financial analyst (CFA) charterholder. Tom is from Minneapolis, graduated from Boston College and lives in San Francisco.

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products such as these, and one can see the literature meandering back and forth as greater understanding and more intelligent and appropriate analytical tools are employed to study the instruments. The main problems with academic studies are that they typically take a long time to get published, many of the best ones are not readable by a lay audience, and it typically takes an academician with expertise to sort through the varying methodologies and findings to make sense of them.

**Annuity Digest:** Asset decumulation and the annuity industry typically involve products that are heavily intermediated and sold rather than bought. How might investment professional use the information in your study to better serve their clients, and how might consumers use the information to better inform/prepare themselves for a very important decision and purchase?

**Professor Babel:** Our studies do not make predictions about how well FIAs will perform in the future. Rather, they undertake a rigorous analysis of the products and the alleged defects in the products. They found in the products that were examined in depth, they operated the way they were designed to operate and over the period of their existence, performed well.

**Annuity Digest:** Has the industry—either trade groups or marketing/wholesale organizations—approached you about the study? If not, why do you believe this might be the case?

**Professor Babel:** Yes, but I have thought it best not to write and publish a sponsored study on FIAs because of the litigation surrounding the issue. Rather, from time to time I have presented our findings in academic conferences and will ultimately publish something on the subject when I find time. Recently, some other academic articles have been written that largely corroborate our studies, and with an expanded purview and alternative methodology.

**Annuity Digest:** Why, in your opinion, has the FIA industry not jumped on this PR and marketing opportunity? It seems that either trade groups or asset managers within other asset classes would, to say the least, leverage a report like this from a marketing and PR standpoint?

**Professor Babel:** I do not undertake research to help market any company's specific products, nor do I endorse a product of a particular company publicly. I do, however, look at a genre of products, including average features and average pricing, and comment on the entire genre. For example, I may research whole [life insurance](#) contracts, participating and nonparticipating, and comment on their pricing and performance, but I won't comment publicly on a particular company's product.

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[Charitable gift annuities](#)

allow donors to make tax deductible contributions to a charitable organization. In exchange for the charitable contribution, donors receive a stream of regular, annuity-like payments for their lifetime(s). The gifts are *irrevocable*, so donors do assume *credit risk* as charitable organizations can become insolvent. Some charitable organizations will use their own assets to fund the payments to the donor, while others will purchase a commercial annuity to fund the payments. The rates on charitable gift annuities are typically a bit lower than what would be available through a commercial annuity.

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