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Individual versus Institutional Investing (pp. 1-8)

Harry M. Markowitz

This paper first describes the analytic approach that Markowitz used in developing his portfolio theory. Developing a game-of-life simulation is a parallel approach for modeling individual financial management. To develop a realistic simulator will require deciding what goals are essential to the family planning process, formulating optimizable subproblems, using technology to interpret and record decisions, and developing decision rules which prove robust in the model and can be implemented in practice.

The Optimal Allocation of Pension Fund Assets: An Individual's Perspective (pp. 9-22)

Tom L. Potts, William Reichenstein

This study asks which assets an individual should hold indirectly in a pension in order to maximize total portfolio return, where the total portfolio consists of assets held directly outside of pensions plus the pro rata share of pension assets. The answer depends upon whether the individual actively or passively manages the nonpension portion of the total portfolio. Most individuals should place high-yield stocks in the pension fund. But active investors should place low-yield growth stocks in the pension, while very passive investors should place bonds in the pension fund. Reinstatement of capital gains exclusion would usually make corporate bonds the optimal pension asset.

Life Insurance Companies as Investment Managers: New Implications for Consumers (pp. 23-34)

Robert T. Kleiman, Anandi P. Sahu

This paper examines the attractiveness of the equity portfolios of life insurance companies as an alternative investment to mutual funds. In particular, this study analyzes the risk-adjusted investment performance of the stock portfolios of life insurance companies, attributable to their stock selection and market timing abilities. Using conventional measures of risk-adjusted portfolio performance, we find that life insurance companies exhibit performance similar to mutual funds. The evidence suggests that the life insurance companies, like their mutual fund counterparts, fail to exhibit differential stock selection or market timing abilities that are statistically significant. While the risk-adjusted investment performance of the two investment vehicles is similar, the variable annuity contracts of life insurance companies may offer an edge over mutual funds due to their ability to defer taxes.

Determinants of Household Check Writing: The Impacts of the Use of Electronic Banking Services and Alternative Pricing of Services (pp. 35-44)

Neil B. Murphy

In recent years, there has been a simultaneous deregulation of interest ceilings on household deposits and a dramatic deployment of automatic teller machines (ATM's) by the banking industry. At one time, there was a belief that the U.S. would evolve into a "checkless society" because of the development of electronic funds transfer systems such as the ATM. That has clearly not happened. The purpose of this paper is to estimate the impacts of both the use of ATM's and the change in pricing due to deregulation on household check writing. The source of the data is a survey of households conducted by the Board of Governors of the Federal Reserve System. The results of the tests indicate that the use of electronic banking services had no discernible impact on check writing.

Real Estate Income and Relocation (pp. 45-59)

Peter Chinloy

This paper looks at the decision relationship between two major assets of the individual, residential real estate and human capital, the ability to generate income from labor. Empirical results indicate that labor income is not sufficient for defining income within the utility function; real estate income must also be included. The decision to relocate must be made after considering both the return and risk in the area's residential real estate as well as the potential income from salaries.

Disability Income Insurance and the Individual (pp. 61-78)

Larry A. Cox

In this article, both institutional and research literature pertaining to disability income insurance issues is reviewed from the perspective of the individual. Primary issues include the nature of the risk, the quantity of purchase decision, the choice of product, and the selection of supplier. An ultimate objective is to provide the reader with the foundation necessary to initiate future research efforts focusing on disability-related loss exposures. Potential areas for future research are suggested.

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Personal Financial Planning and the Allocation of Disposable Wealth (pp. 87-99)

Amy V. Puelz, Robert Puelz

In the process of personal financial planning individuals are confronted with a time dependent wealth allocation problem. Oftentimes the solution involves selecting financial products based on objective criteria, for example, product cost and expected return. While objective criteria are important to the selection process, an individual's subjective valuation of all criteria, objective and subjective, relevant to the decision plays the crucial role. A goal programming model parameterized by the analytical hierarchy process is presented to determine the allocation of an individual's disposable wealth to present and future consumption bundles and investable assets, conditional on the preference ordering of the individual.

Should Individual Investors Avoid the Stock Market Outside of January? (pp. 101-108)

Steven V. Mann, Donald P. Solberg

Recent studies suggest that there is no reward for bearing risk outside of January, implying that individuals should invest in common stocks only in January. The purpose of this study is to demonstrate that this conclusion is far too strong given existing empirical evidence. Our results suggest that inferences drawn from the evidence can be altered greatly through small changes in the way the empirical question is addressed. There is sufficient evidence to doubt the conclusion that individuals are not compensated for the risk of participating in the stock market outside of January.

Effective Credit Costs in Retail Financial Markets: Leasing Versus Borrowing (pp. 109-129)

D. Anthony Plath, Bennie H. Nunnally, Jr.

This study examines reported credit cost information in the automobile sales market to determine if vehicle leasing really is cheaper than installment borrowing. In addition, the study evaluates the accuracy of credit cost data furnished to consumers by commercial banks, vehicle leasing firms, and automobile dealers to gauge whether any systematic differences exist in the accuracy of reported credit cost information. Results of the study suggest that the cost of leasing is significantly different from borrowing, yet neither financing alternative is unilaterally cheaper than the other. In addition, suppliers of credit in consumer finance markets routinely and significantly understate effective credit costs reported to consumers.

Comparing Mortgages with Different Payment Frequencies (pp. 131-142)

Arefaine G. Yohannes

The biweekly-payment mortgage is an alternative to the monthly-payment mortgage. In this study, logistic regression is used to determine the influence of demographic characteristics on the choice between these two types of mortgages. Of the six independent variables that were considered, only two had significant influence on mortgage choice. They were the frequency of paydays and education.

Probabilistic Estate Planning (pp. 143-157)

Ronald R. Crabb

Probabilistic estate planning is based on the principle of maximizing expected net present value commensurate with the risk assumed. Rather than assuming that death occurs at life expectancy, probabilistic estate planning treats death as a random variable. Compounded to randomly chosen ages of death, estate assets are taxed and distributed to heirs. The purpose of probabilistic estate planning is to find the estate plan and asset/liability combination that maximizes the expected net present value of assets passing to heirs and to convey some idea of the risk associated with that estate plan.

International Diversification for the Individual: A Review (pp. 159-175)

Jeff Madura, Thomas J. O'Brien

This paper reviews aspects of literature on international investing that should be of interest to individual investors. Three modern issues are covered: (1) the benefits of international diversification as the global markets continue to integrate; (2) the problem of currency exposure; and (3) effective means of achieving international diversification. Strategies are discussed which enable the individual to apply suggestion from the research. By restricting the scope of the review to issues of most interest to the individual, we do not review research on international asset pricing theory and international market efficiency and "anomalies."