Accepted Manuscript

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PII: S1057-5219(17)30216-8
Reference: FINANA 1173
Received date: 30 October 2017
Accepted date: 28 December 2017

Please cite this article as: Chris Brooks, Ivan Sangiorgi, Carola Hillenbrand, Kevin Money , Why are older investors less willing to take financial risks?. The address for the corresponding author was captured as affiliation for all authors. Please check if appropriate. Finana(2017), https://doi.org/10.1016/j.irfa.2017.12.008

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Why are older investors less willing to take financial risks?

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October 2017

Abstract

We investigate the link between age and tolerance of financial risks in the context of attitude to risk questionnaires completed by clients when meeting their financial advisors. Using a unique database comprising the responses to over half a million such questionnaires, we show that risk tolerance declines at an increasing, albeit slow, rate with age. We investigate the explanatory power of the ability to bear losses, declining investment horizon and retirement effects, finding that these variables have considerably greater explanatory power for the cross-section of risk aversion than age, and that they are only able to partially mediate the link between age and risk tolerance. We are unable to uncover any evidence that declining cognitive abilities among older investors are able to explain their lower willingness to take financial risks. Overall, our results are indicative of a modest age effect in risk tolerance that cannot be attributed to changes in other observable characteristics that differ between younger and older investors.

Keywords: retail investors, risk tolerance, attitude to risk, effect of ageing, cognitive decline

J.E.L. Classifications: G11, G20, J14, C25

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Acknowledgements: We are grateful to the ESRC for funding this research under grant number ES/P000657/1. We would like to thank Distribution Technology for supplying the data used in this paper. We are also grateful to seminar participants at the Behavioural finance Working Group and to Arthur Money and Heather Richards for their constructive comments.
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