Return Expectations and Risk Aversion Heterogeneity in Household Portfolios

November 2013

Alessandro Bucciol (University of Verona & Netspar)

Raffaele Miniaci (University of Brescia)

Sergio Pastorello (University of Bologna)

We develop a structural econometric model within the mean variance portfolio framework to elicit household-specific expectations about future financial market returns and risk attitude observed financial portfolio holdings, investments in real assets and the answers to self-assessed questions on the willingness to bear financial risk. We derive an explicit solution of the model, which we analyze using a combination of tobit and ordered probit estimation methods with two latent variables. We use US data from the Survey of Consumer Finance for the period 1995 to 2010. We find a positive relation of age with expectations on bonds returns but not on stocks; women are more optimistic than men about the stock market performances but less willing to bear risk; graduate people are more risk prone but pessimistic about financial markets returns; instead, after having controlled for demographic characteristics, wealth and income seem to have a negligible impact on expectation formation and risk aversion. Finally we show that expected returns from bonds investments react positively to positive past performances of the market, while stocks expected returns do not react to past performances.

JEL codes: G11, D81, D14.

Keywords: Household finance, mean variance analysis, risk aversion, maximum likelihood.