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For consumers

SEARCHING FOR INCOME IN RETIREMENT?

A variable annuity can play an important role as part of your retirement plan if you're looking for the protection of steady income and upside potential.*

Where are you going to get the income to live on in retirement? People in their 60s and early 70s are looking for cash flow—money coming into their checkbook every month. If you need $25,000 or more a year to live on beyond what you'll get in Social Security benefits, what's your plan?

THE HUNT FOR YIELD

"The search for yield is hard," says Michael Harris, CFP, CLU, ChFC and a senior educational advisor with the Alliance for Lifetime Income. Many retirees have seen growth in their portfolios as the stock market climbed from the 2008 financial crisis as well as the pandemic lows of 2020. Yet the amount of yield—or income—that wealth can earn is disappointing as yields are still at historic lows. The S&P 500 dividend yield—the dividends you get from a diversified mix of stocks—is at a 20-year-low at just 1.3%.** Ditto for 10-year Treasury notes issued by the U.S. government.

What if there was a way to continue to grow your assets plus get a protected stream of retirement income? A variable annuity with an optional protected lifetime income benefit may satisfy your search for cash flow, without giving up control of your money.

ANNUITIES ARE AN ESSENTIAL PIECE OF THE RETIREMENT PUZZLE

If you think of your retirement portfolio as a puzzle, it's made up of many different pieces that fall into three broad categories: stocks, fixed income, and annuities. With stocks and fixed income investments, as the value goes up and down based on the markets and interest rates, the amount of income that's generated fluctuates too. By contrast, with some annuities, there is a set payment that

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you can get every month, based on how much money you put in and your age. The secret? Annuities allow for the efficient return of principal during retirement, thanks to tax deferral, age credits, something called the annuitization tax exclusion ratio, and the set payments you'll get for life.

That stable payment is intriguing for folks, especially as people are living longer. "Just like Social Security and a pension give you the security of knowing how much you'll get each month, an annuity provides peace of mind," says Suzanne Norman, CIMA, a financial literacy expert and senior educational advisor for the Alliance.

With the most basic type of annuity—a fixed immediate annuity—you purchase an annuity from an insurer in exchange for fixed payments for your lifetime. That type of annuity can make sense if you're trying to immediately maximize the monthly payments you'll get from the start—and you're okay with giving up control of the money you use to purchase the annuity.

By contrast, with a variable annuity, your money is invested in subaccounts where you choose the type of investments: any combination of a bond fund, a stock fund, or a fixed account that pays a fixed rate of interest. You can adjust the mix. You can also get an optional benefit that gives you a protected lifetime income stream. The income stops when the last covered person (typically you and a spouse) dies, but whatever is left in the annuity goes to your family.

Here's an example of how this could work. A couple, both 70, with a $250,000 variable annuity could get a 5% annual payment for life, until the last one passes away. The payment could be less if you're younger, or more if you're older because the insurance company uses your life expectancy to determine payments. The couple in our example will never get less than $12,500 a year—even if markets go down. That's called downside protection. "If it gets really ugly, in the annuity you still have protected income," Harris says. "You've got this $12,500 annual income for life." This protected lifetime income will never go down unless you take out an amount that exceeds it. Think of your protected income as a speed limit that you shouldn't exceed.

A VARIABLE ANNUITY GIVES YOU UPSIDE POTENTIAL

With a variable annuity, you're maintaining exposure to the markets. In some cases, if the market goes up and the value of the

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assets in your subaccounts goes up, your protected lifetime income amount could reset, and you could get higher payments going forward. Say your $250,000 in investments in the VA goes up to $300,000. Your payments could go up to $15,000 a year for life, depending on the parameters associated with the variable annuity's income benefit.

Can you take out more than the 5%? Theoretically, you could take it all. "You can surrender, pay taxes and walk away and buy a boat or a second home," says Harris. You could, but you probably don't want to. If you "exceed the speed limit" and take out more than the guarantee, you get an adjustment down. That means your payments could be reduced—possibly for life. The annuity is a great cash-flow producing investment, and it's only a slice of your portfolio. If you need an extra $5,000, it might be better to take it out of other investments within your portfolio, which you might be able to access without penalties.

FINDING THE RIGHT MIX

Once people reach their 60s, they often start reducing risk in their investment portfolio by keeping less money in stocks and more in bonds. Still, with decades ahead, it can make sense to keep higher stock allocations as a hedge against inflation. You might consider a 70/30 portfolio— that's a mix of 70% stocks and 30% bonds—or even a 60/40 mix. "It's tough to get people in my cohort to pull the trigger on that mix," says Harris.

Running a higher stock portfolio at older ages is counter-intuitive because of the risks associated with stocks. Having an annuity as part of your overall portfolio can help investors accept higher stock allocations. The annuity payments, along with Social Security benefits, can cover essential expenses. That means you might accept a higher stock allocation in the annuity subaccounts—as well as in the rest of your portfolio. "The annuity allows people to accept that allocation," says Harris. "It takes the pressure off." That can put you in a better position—where you get the potential upside of the underlying portfolio in the annuity, plus the protected income payouts—and higher stock allocations in the rest of your portfolio.

CONCLUSION

A financial professional can help you determine whether a variable annuity might make sense for you based on your retirement needs, and they can also advise you on choosing the underlying investments on an ongoing basis. There are costs associated with an annuity. Why? It's an insurance contract. It's there to manage your risks. It provides a value—insurance that you'll get protected lifetime income, along with other benefits—a value that's worth that cost.

*Annuities are long-term investments designed for retirement purposes. The value of variable annuities is subject to market risk and will fluctuate. Product guarantees are subject to the claims-paying ability of the issuing insurance company. Earnings, when withdrawn, are subject to federal and/or state income tax, including a 10% tax penalty for withdrawals before age 59½. Some income guarantees offered with annuities take the form of optional riders and carry charges in addition to the fees and charges associated with annuity products. There is no guarantee that any investment will achieve its objectives, generate positive returns, or avoid losses. Investments in annuity contracts may not be suitable for all investors.

**S&P 500 Dividend Yield Is Now at a 20-Year Low of 1.3% https://www.barrons.com/articles/s-p-500-dividend-yield-is-now-at-a-20-year-low-of-1-3-51627676200