

A

New

Generation of Income Annuities

By Gregory Falzon

In the coming decade, annuities will play a major role in helping people turn their nest eggs into guaranteed lifetime income in retirement.

People have come to realize that a missing ingredient in their retirement plans is an income that will last as long as they do. MetLife market research indicates that clients are more receptive to annuities once they understand their benefits. Furthermore, the insurance industry is beginning to see more innovative product designs that are intended to meet the needs of both today's and the future's retirees.

For financial advisors, opportunities will be tremendous in meeting the needs of current and prospective customers in retirement because of the large number of baby boomers entering this life stage. Boomers are also a segment generally more interested in seeking financial advice than previous generations. The impending retirement income distribution opportunity potentially could be the single biggest opportunity for advisors in decades.

Fortunately, the insurance industry has been preparing for this opportunity for quite some time. Insurers have introduced some of the most innovative retirement products during the past five years. This "new generation" of income annuities supported by a range of educational programs and tools allows individuals to convert their nest eggs into guaranteed income that they cannot outlive. To reflect the needs of today's and the future's retirees, income

annuities have become more flexible, more affordable and, in some cases, even portable, while retaining the product's core feature of ensuring guaranteed lifetime income.

A distinct advantage of annuities is that they are the only financial products specifically designed to generate a guaranteed lifelong stream of retirement income. Another key advantage of income annuities is that they generally have the ability to produce the highest level of guaranteed income per dollar of

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assets, which provides the participant with the ability to maximize income. That bodes well for financial advisors, especially when one considers that fixed guarantees are more attractive than ever, given the volatility of the financial markets.

According to the 2009 MetLife Study of the American Dream, based on more than 2,200 online surveys compiled in January, 80 percent of Americans report that they are now more concerned with guarantees and stability than they are with returns. Among the silent

generation (those born between 1933 and 1945) and baby boomers (those born between 1946 and 1964), the percentages opting for stability over returns climbs to 91 percent and 84 percent, respectively.

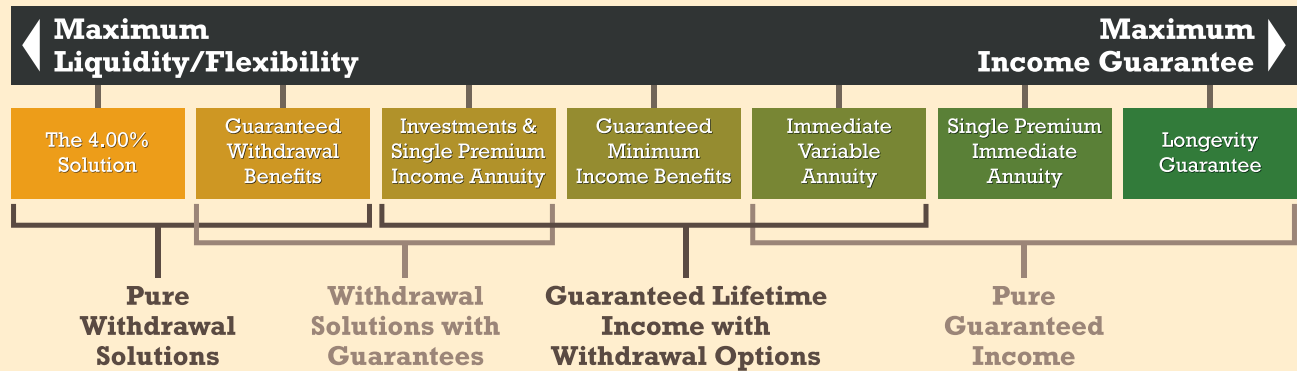
Income Annuities: Maximum Flexibility to Maximum Income

One of the most important ways in which advisors can help their clients figure out the most appropriate retirement income solutions is for the advisor to be well-versed in the spectrum of retirement income options, which range from maximum liquidity/flexibility at one end to maximum guaranteed income at the other.

The accompanying chart illustrates pure withdrawals to pure guaranteed income solutions. Once you've educated your clients on each option, including the trade-offs involved, you then can discuss the range of annuity features that help address their objectives. These features include fixed payments that never change (regardless of market conditions), withdrawal features (such as full or partial), a full range of income payout options, a return-of-premium guarantee, inflation protection options and a death benefit.

There are several newer income annuity products that have been introduced into the marketplace – some of which are offered on both a retail and an institutional basis, while others are offered only through the workplace.

Retirement Income Spectrum



- Must educate on each option and the trade-offs involved
- No absolute right or wrong choice
- Over time, perspective may change and move along the spectrum
- Some will likely implement combinations, but many use a one-product approach

From Personal Pensions to Longevity Insurance

Insurers have introduced income annuity products that are targeted to a younger audience. These new products allow employees to create their own “personal pensions.” Offered as an option in a 401(k) plan, this product, unlike traditional savings vehicles, ensures that every contribution an individual makes is immediately converted to a specific future income benefit that is guaranteed to last a lifetime. By making monthly contributions within a 401(k) plan, workers are able to invest over time and use a “dollar cost averaging” approach to purchase a future income stream.

As a recent development, income annuities are being added into defined contribution plan target date funds, with the annuity allocation automatically increasing as the plan participant gets closer to retirement. These are frequently referred to as hybrid 401(k)s, and the annuity allocation within the target date fund, for example, might start at 5 percent at age 25 and grow to more than 50 percent by the time the participant plans to retire.

We are also seeing more income annuity products that offer liquidity

options that allow purchasers to access money in an emergency and inflation options that link benefit increases to changes in the CPI. In addition, products are offering features (such as more investment choices, transfers and rebalancing) that provide individuals with the flexibility and control that they are used to seeing within their 401(k) plans.

Another recently introduced income annuity is a type of longevity insurance – designed to generate income starting at a later age, when an individual’s retirement savings may be running out. The individual may elect to start receiving the monthly income from the product, for example, at age 85 – which is the average life expectancy for Americans who have reached age 65 – or at any other point during her retirement. Since the individual would typically buy this income annuity between the ages of 55 and 65, she is deferring the income start date 20 or even 30 years into the future.

This allows her to set aside a smaller portion of her retirement savings in order to generate a steady stream of guaranteed income in later years, when it may be needed most. It also allows her to manage her remaining retirement

assets to a limited time horizon.

According to Financial Engines, which wrote and published the white paper titled “The Longevity Annuity: An Annuity for Everyone?” a typical retiree allocating 10 percent to 15 percent of wealth to a longevity annuity during the deferral period allows guaranteed spending to increase by 20 percent to 30 percent in retirement.

While economists predict that it may take some time for retirement savings to recover from the market events of the last year, the fact remains that a significant portion is likely to be converted into guaranteed lifelong income through the purchase of an income annuity. This will renew interest in an option that was popular in the earliest 401(k) retirement plans and provide a huge sales opportunity for advisors. By preparing now for the impending retirement income opportunity, advisors will be ready when this time comes. [INN](#)

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