Is The Time Right For Income Annuities?

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You could say that Joseph Tomlinson practices what he preaches.

When he took early retirement from an insurance company a number of years ago, he bought an income annuity to provide a guaranteed income stream.

Along with some savings, it was meant to help cover his and his wife's basic living expenses.

Evidently, the strategy worked. Tomlinson, a retirement funding researcher, advises retirees to seek a guaranteed income stream.

The strategy involves covering ongoing basic retirement needs with predictable income from Social Security and any pension.

If they aren't enough, he advocates filling the gap with an income annuity. He specifies a single premium immediate annuity (SPIA), which is typically paid for from savings. Once their core needs such as food and rent are met, retirees can spend or invest remaining savings as they see fit.

"People are living longer in retirement, and ever fewer of them have a pension," said Tomlinson, who lives in Greenville, Maine. "To reduce the risk of running out of money in old age, they need to find other sources of guaranteed income, such as annuities."

Surveys show widespread concern about outliving one's money and fear that Social Security might not cover the basics. Signs show rising interest in supplementing those with income annuities. Experts say these are comparatively simple and low cost.

Surging Sales

Sales reflect rising popularity. From 2009 to 2013, sales of SPIAs and deferred income annuities (DIAs) surged almost 40% to $10.5 billion, the LIMRA Secure Retirement Institute says.

"By 2018, LIMRA projects that income annuity market (SPIAs and DIAs) will probably double to $22 billion," said Jafor Iqbal, the institute's associate managing research director. He links that growth to the rising tide of retirees, who increasingly will lack a pension.

But annuities inspire questions. As investment adviser Jonathan Duong of Denver puts it, "Annuities can be a good tool, but they aren't right for everyone."

Among their potential drawbacks: SPIAs can't be cashed in early. And payouts from income annuities hinge on current interest rates as well as a buyer's age. In today's low interest rate environment, SPIA investors can expect more modest payouts.

What might that amount to today? Tomlinson illustrates: If an unmarried 65-year-old woman buys a $200,000 income annuity, with a 10-year period-certain provision -- meaning that if she dies before age 75, a specified heir would receive the payouts until the 10-year period ended -- she would receive $1,014 a month, equal to an annual 6.08% payout rate.

If she had bought the same policy in late 2008, when corporate bond rates were higher, she'd have received $1,286 per month, or a 7.7% annual rate of payout, he says.

Age of the SPIA buyer is another factor. As Jonathan Duong points out, the older the SPIA buyer, the higher the income stream he'll get. Duong suggests potential SPIA buyers wait until reaching their 70s.

Financial planner Paula Hogan of Milwaukee suggests a way to deal with low interest rates. Ordinarily she suggests SPIA buyers stretch out purchases over five years.

By buying SPIAs even more gradually, retirees have a better chance of getting higher annuity payouts later if rates rise.

http://www.nasdaq.com/article/is-the-time-right-for-income-annuities-cm366077