

Love Hate

Relationship with Annuities....



By Karen Wentzel, CFP®
Head of Annuities, Sanlam Employee Benefits

Every financial product has advantages and disadvantages, benefits and costs. For this reason, annuities are no stranger to the love/hate relationship in the financial world. Incorrect product advice and a misunderstanding about the features of annuities may lead to mixed emotions and different opinions. Annuities are split into two categories: guaranteed life and living annuities.

Guaranteed life annuities: pros and cons

For all life annuities, pensioners carry no longevity or investment risk, as initial pensions and increases are guaranteed for life, and will never decrease.

✓ Income for life

A life annuity is a financial product sold by insurance companies that allows you to set aside money and then trigger a stream of future income payments. Life annuities therefore provide an income stream that you cannot outlive. This is more than just a marketing phrase; this is a promise for life. Insurers pool all annuity customers together, and although your insurer does not know exactly when you will die, it has a fairly good estimation of your lifespan by using mortality tables. An income for life is a major plus for budgeting – you know exactly what you are going to get in advance.

✓ Peace of mind for you and your family

Life annuities can be tailored to meet specific family needs, for example, by providing a benefit that equals 75% of the income of the main member to a surviving spouse, or dependent child. Life annuities give you and your family the peace of mind that however long you may live, your payment stream will continue.

✓ The road to financial independence

Guarantees reduce the need to rely on families, friends, charities and government to help make ends meet during retirement.

✓ Release you from the responsibility of making investment decisions

Insurers can invest in a wide range of assets. Not only do these insurers offer products with attractive returns that annuity holders could not access on their own, but they also release pensioners of the stress of having to make their own investment choices. This is especially important when cognitive ability starts to decrease during old age.

✗ Fix the problem of not having enough retirement savings

Since the movement from Defined Benefit to Defined Contribution schemes, the reality of the retirement crisis is that only about 20% of members have sufficient savings to maintain their current standard of living. And the problem is getting increasingly worse. A large share of households may be forced to significantly reduce their consumption in retirement and will have to rely heavily on their families, charities and government to help make ends meet. Results from Sanlam's 2016 BENCHMARK research show that more than two-thirds of pensioners indicate they do not preserve their saving when changing jobs. No annuity product can fix the problem of insufficient income in retirement!

✗ Give you the best of both worlds

Guaranteed annuities offer you an income for life, but no remaining capital is left as an inheritance or legacy in the event of your death after retirement.

✗ Inflation risk

Although life annuities provide an income for life that mostly increases annually, there is no guarantee that the increases in income will keep

In exchange for this flexibility, pensioners take on the risk that they may outlive their savings or experience poor investment returns (known as longevity and investment risk).
