Understanding Annuities

Overview of the unique types and strategies available to help you achieve your goals.

ASB Financial

What is an Annuity?

While annuities are the most commonly used investment product, they are probably the most misunderstood. Media stories often focus on only one type of annuity, resulting in misleading information.

So what exactly is an Annuity? Annuities date back to over 2,000 years ago when Romans gave their former soldiers a continual day to day allowance for the rest of their lives. Today, Annuities have evolved to two primary strategies and two core types, developed by the strongest financial institutions in the world. Stated simply, Annuities are structured insurance contracts regulated by states for the purpose of accumulation and lifetime income.

Primary Strategies

There are two strategies to select from to achieve your current and future retirement goals.

ACCUMULATION

If you have funds that you don't wish to access immediately, an accumulation strategy will maximize the growth potential of your money. Depending on the type of annuity this is paired with, the level of risk and return can range from very conservative to highly aggressive.

LIFETIME INCOME

The original and most common use of Annuities is to create an income stream that you can't outlive. This strategy can be designed to cover an individual life or a couple's combined lives. Some products will offer a locked-in guaranteed income while others have the option to grow incomes over time.

Types of Annuities

There are two main types of annuities; variable and fixed.

VARIABLE ANNUITIES

The Variable Annuity really stands on it's own in the annuity types. Unlike other annuities, a variable annuity comes with risk, including the potential for loss. The client's funds are invested in sub-accounts, which are tied to the highs and lows of the stock market. Variable annuities usually have more moving parts and available riders.

The trade-off for the potential stock market returns, other than the losses, are added management fees, policy fees and rider fees. This makes Variable Annuities more suitable to an individual who is still in the accumulation phase, has extended time on their side, and/or has extra funds to risk.

FIXED ANNUITIES

SINGLE PREMIUM IMMEDIATE ANNUITY (SPIA)

A Single Premium Immediate Annuity, commonly referred to as a SPIA, is designed to immediately take advantage of the Lifetime Income strategy. By transferring a lump sum to a SPIA, the insurance company pays you a fixed amount of money starting immediately, either monthly or annually, for a specific period of time. Typically, these are guaranteed lifetime income, meaning the income will continue as long as the Annuitant or Joint Annuitant are alive.

Period Certain options are available on SPIAs, which means they can be structured to have income last a set period of years, such as ten, twenty or thirty years. *Joint-Life* is another option that can spread the income to cover both lives of a married couple.

MULTI-YEAR GUARANTEED ANNUITY (MYGA)

MYGAs are the simplest types of annuities. They are commonly compared to CDs, but typically with a higher rate of return. The length of the contract can vary, usually between one and ten years.

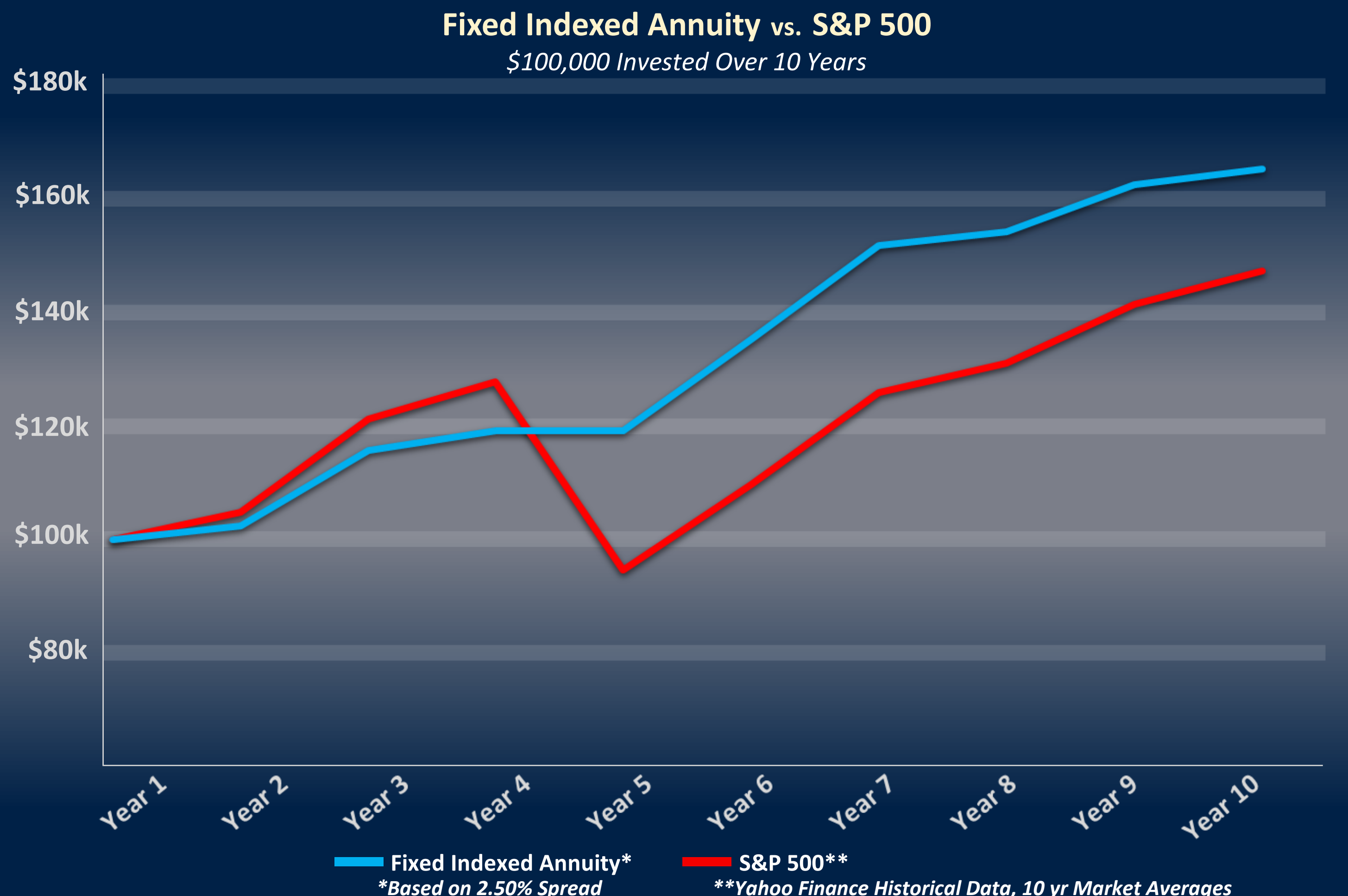
Many MYGAs are funded with a one-time lump sum, however some also have options for additional deposits over time. This ability to add funds after the contract is active makes this a popular option for individuals who are close to retirement, but are still accumulating savings.

FIXED INDEXED ANNUITY (FIA)

The Fixed Indexed Annuity is the newest type of annuity, having been created in 1995. It is also the fastest growing type of annuity today, experiencing a meteoric rise in popularity following the 2008/2009 market recession.

The attractive benefit of the FIA is its ability to participate in the market gains via indexes, without any risk for loss. The funds are linked to—but not directly invested in—stock market indexes, such as the S&P 500, NASDAQ, and others. Global indexes can also be available. The indexes allow the account to participate in a portion of the market upside. However, if the index experiences a loss, the account locks in at zero percent to protect the investment. These products can include riders such as Lifetime Income, Benefit Multipliers for Long Term Care and Enhanced Death Benefits.

The chart below demonstrates a $100,000 investment over 10 years using S&P 500 market averages. This time frame includes averages that saw both the 2008 extended crash as well as the 2020 quick crash. This shows that market investments take time to recuperate from a down-turn, while the FIA simply "freezes" during periods of loss but then gets to enjoy the upshot. This advantage is what drives the popularity of the FIA.



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