REAL MONEY

GUARANTEED INCOME, WITH STRINGS

AN ANNUITY PROVIDES PEACE OF MIND, BUT INVOLVES TRADE-OFFS. BY JOHN MILEY

OUR READER

WHO: ROGER SALDANA, 75
WHERE: NEWBURGH, IND.
QUESTION: SHOULD I PUT PART OF MY RETIREMENT SAVINGS INTO A VARIABLE ANNUITY?

ROGER, A SUCCESSFUL lifelong investor, was surprised when his financial adviser suggested he move $500,000 of his retirement nest egg out of mutual funds and into a deferred variable annuity. The retired chemical engineer wonders whether it is the right move.

First, Roger should determine whether he needs a guaranteed source of income beyond Social Security benefits to cover his and his wife Leyte's essential expenses. The next question is trickier: Which type of annuity should he buy, and how much should he invest?

There are two kinds of annuities. With a deferred variable annuity, you invest a chunk of money in mutual-fund-like accounts and an insurance company promises to provide you with a stream of income at some future date. You get potential for growth when the market rises and income protection when the market declines. Your payout is based on the actual investment-account balance or a guaranteed amount that grows by a fixed percentage each year—whichever is higher.

Deferred variable annuities tend to work best for preretirees. The longer you delay payouts, the more the account balance—and future payouts—can grow through either market appreciation or guaranteed accumulations. But deferred variable annuities tend to be expensive, with annual insurance and investment fees averaging 3.5%.

Retirees, such as Roger, normally do better with an immediate-payout annuity. You give a lump sum to an insurance company and immediately start drawing monthly income for a fixed number of years or for the rest of your life. The size of your monthly payout is determined by how much you invest, your age and interest rates in effect at the time of purchase.

Consider your needs. Roger currently has 70% of his investment reserves in stock funds. Given the ongoing market volatility, he is taking a big chance because he has no guaranteed sources of income other than his Social Security benefits. He may want to lock in income with a low-cost immediate annuity.

TAMARA REYNOLDS

Despite today's rock-bottom interest rates, Roger could collect a 10% annual payout from an immediate annuity based on his current age of 75 (the payout includes earnings plus a partial return of his investment). If he invested $500,000, he would receive about $4,100 per month (with no survivor benefits) compared with a $2,500-per-month minimum guaranteed payout from the deferred variable annuity if he started payouts after one year. If he needs less guaranteed income, he could invest a smaller lump sum.

But given the fact that his wife is nearly 20 years younger, he needs to provide for her should he die before she does. An immediate annuity with a 20-year guarantee—which would continue to pay Leyte even if Roger died before then—would pay nearly $3,000 a month. Or an immediate annuity that refunds the balance of the premium if he dies before recovering the initial investment would pay out more than $3,400 per month. ■