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STRATEGY 4 SECURITY IN TIMES OF VOLATILITY.

CommInsure Guaranteed Annuity Strategy Series

Issued: 1 July 2017

AT A GLANCE

This strategy focuses on:

- Guaranteed income
- Budgeting for retirement and longevity protection
- Increases in interest rates and decreases in the share market
- Including annuities in a diversified portfolio.

The Australian share market can be volatile. Changing market conditions can create uncertainty, making it difficult for retirees who want to preserve their wealth and budget for retirement. A guaranteed annuity is a simple and secure income solution for clients who want an investment option with more certainty than an account based pension.

Guaranteed income

A guaranteed annuity provides guaranteed regular income. It can be set for a fixed term or a lifetime, either way your client is free from worrying about managing large sums of money. Unlike account based pensions, which rely on the performance of underlying investments, guaranteed annuities aren't generally affected by share market movements or interest rate fluctuations. Retirees can rely on a guaranteed annuity to provide a consistent source of income, knowing the payments won't reduce even in a market downturn.

What does a guarantee[1] mean?

When your client invests in a CommInsure annuity, they receive a guarantee to receive future income. CommInsure enters into a legally binding agreement to make payments at the predetermined interest rate (as agreed with the client at purchase) and in accordance with the payment schedule.

This is in contrast to income from account based pensions, which are dependent on market and investment performance.

Budgeting for retirement and longevity protection

When planning for retirement, clients who invest in an annuity can take comfort from knowing part of their future income is secure. As well as guaranteeing payments for a fixed number of years, clients can invest in an annuity that will pay an income for the rest of their life. This payment is also guaranteed and won't reduce as it isn't affected by changes to market conditions or the broader economy.

Increases in interest rates and decreases in the share market

When interest rates rise there is often a corresponding fall in the share market. This happens for a variety of reasons, one being that higher interest rates mean companies have to pay more money to service debts and therefore have less money to distribute to shareholders. Clients who invest in an annuity are less exposed to these market fluctuations, as the interest rate on their investment is locked in at the time of purchase, and are therefore assured a certain level of security on their income.

Annuity as part of a diversified investment

An important part of any retirement plan is how to manage risk. Advisers can help clients layer their income streams, diversify their investments and reduce their exposure to risk. It may be appropriate for your client to invest the cash and fixed interest component of their portfolio into a guaranteed annuity and use an account based pension for the growth component, for example shares and property. This means your client can use the guaranteed income from the annuity to pay for their everyday expenses (food, petrol and bills) and the account based pension for variable expenses, such as a new car or an overseas holiday. This 'smorgasbord' technique helps to balance their portfolio, allowing your client to better manage their cash flow, deal with the unexpected and plan for their future lifestyle with confidence.[2]

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MEET JUDY 63

Judy retired three months ago and has $295,000 in savings. This money is from superannuation and the sale of her home when she downsized after her divorce. She now lives in an apartment and enjoys twice yearly trips around Australia with her friends and new partner, Bill. Initially, Judy was concerned about the impact her divorce might have on her future financial security, so her financial adviser recommended she invest some of her retirement savings in a guaranteed annuity. This ensured a component of her income is guaranteed. This income helps Judy pay for fixed every day expenses, such as strata levies, council rates and phone bills. By investing $145,000 in a CommInsure Lifestream Long Term Guaranteed annuity for 20 years, Judy earns a tax free income of $8,012[3] in the first year (based on no adviser service fee and three percent indexation). Judy's lifestyle is not extravagant, but she would like to access some capital to fund renovations in her apartment, including a new kitchen and new furniture. In this situation, her financial adviser recommended investing her remaining $150,000 in an account based pension. This allows Judy to withdraw $10,000 per year, every year until she reaches the age of 84 (based on eight percent per annum return on a balanced option), and to pay for her new kitchen and furniture. By doing this, Judy's retirement income (not including the Aged Pension) becomes $18,012 per annum to help meet her needs.

Summary

Planning and budgeting for retirement can be a difficult task, especially during times of market volatility. Using guaranteed annuities as part of a retiree's portfolio, means your clients have peace of mind knowing they have guaranteed regular income, regardless of market movements. This minimises their exposure to investment risk and helps them better manage their cash flow. By using the 'smorgasbord' technique as highlighted in this strategy, your clients can take advantage of annuities for their everyday costs and earn variable income, perhaps from an account based pension, for other discretionary costs.

For more information please contact our Retirement Business Development Managers.

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1. CMLA guarantees all benefits under the Lifestream Guaranteed Income Annuities. The Commonwealth Bank of Australia and its subsidiaries (excluding CMLA) do not guarantee Lifestream Guaranteed Income Annuities or the repayment of capital interest by CMLA.
2. From 1 July 2017 the total amount of superannuation that can be transferred into retirement phase will be capped at $1.6 million. The cap will be indexed in $100,000 increments in line with the consumer price index (CPI).
3. Based on projected yield of 3.70 per cent, with nil adviser service fee, nil Residual Capital Value and 3 per cent indexation, and assumes Judy has not exceeded her general transfer balance cap. Rates are illustrative only. For current rates please call us on 1800 624 100 between 8.30 am and 6 pm (Sydney time), Monday to Friday.