Spending your money in retirement:

Rumors & reality





The idea of creating a practical financial plan for a retirement that is still many years away and has many unknowns can feel intimidating. Many of us don't know where we will end up living in retirement or what our expenses are likely to be, and none of us knows how long we will live. However, that doesn't mean we should put off any planning and promise to think about it later. Instead, we should make the best plan we can now, based on what we think is most likely to occur. That will allow us to take the necessary steps today to maximize the probability of achieving the goals we have for that phase of life. Here are a few things to keep in mind when thinking about how to best prepare for the life you want in the future:

- Stay informed about the different ways to generate income in retirement
- Learn and understand how to spend wisely in retirement so you can cover your needs and wants as you move through your 70s, 80s and maybe even 90s
- Set realistic expectations of what it will cost to live the way you want to live in retirement
- Make a good plan, stick with it, and your retirement goal will be more likely to happen

For this report, we'll address that second point in particular by discussing some major issues and concerns people have about spending their money in retirement. Some of us are likely to be overly cautious about using the income our investments will generate, while some of us may be less conservative than we probably should be.

With respect to different ways of generating income to meet your retirement lifestyle goals beyond what your Social Security benefits and 401(k) or IRA can provide, the advantages of tax-deferred[§] products can also come in the form of annuities[†]. Annuities are long-term, tax-deferred products, designed for retirement. Talk to your financial advisor to get more details on the advantages of tax deferral.

What is an Annuity?

Annuities are long-term, tax-deferred vehicles designed for retirement. Variable annuities involve investment risks and may lose value. Earnings are taxable as ordinary income when distributed and may be subject to a 10% additional tax if withdrawn before age 59½.

§ Tax deferral offers no additional value if an annuity is used to fund a qualified plan, such as a 401(k) or IRA. It also may not be available if the annuity is owned by a "non-natural person" such as a corporation or certain types of trusts.

RETIREMENT INCOME: RUMORS AND REALITY

It isn't always easy to separate rumors from facts about what you'll need to save enough for a comfortable income in retirement, taking into account your Social Security benefits and other sources such as a 401(k) or IRA. These are some of the commonly held beliefs about generating sufficient income to support the goals you have for your life during retirement:

- Social Security will run out of money by the time I retire.
- I can withdraw 4% of my retirement nest egg each year.
- I might outlive my savings.

Let's examine these assumptions one at a time.

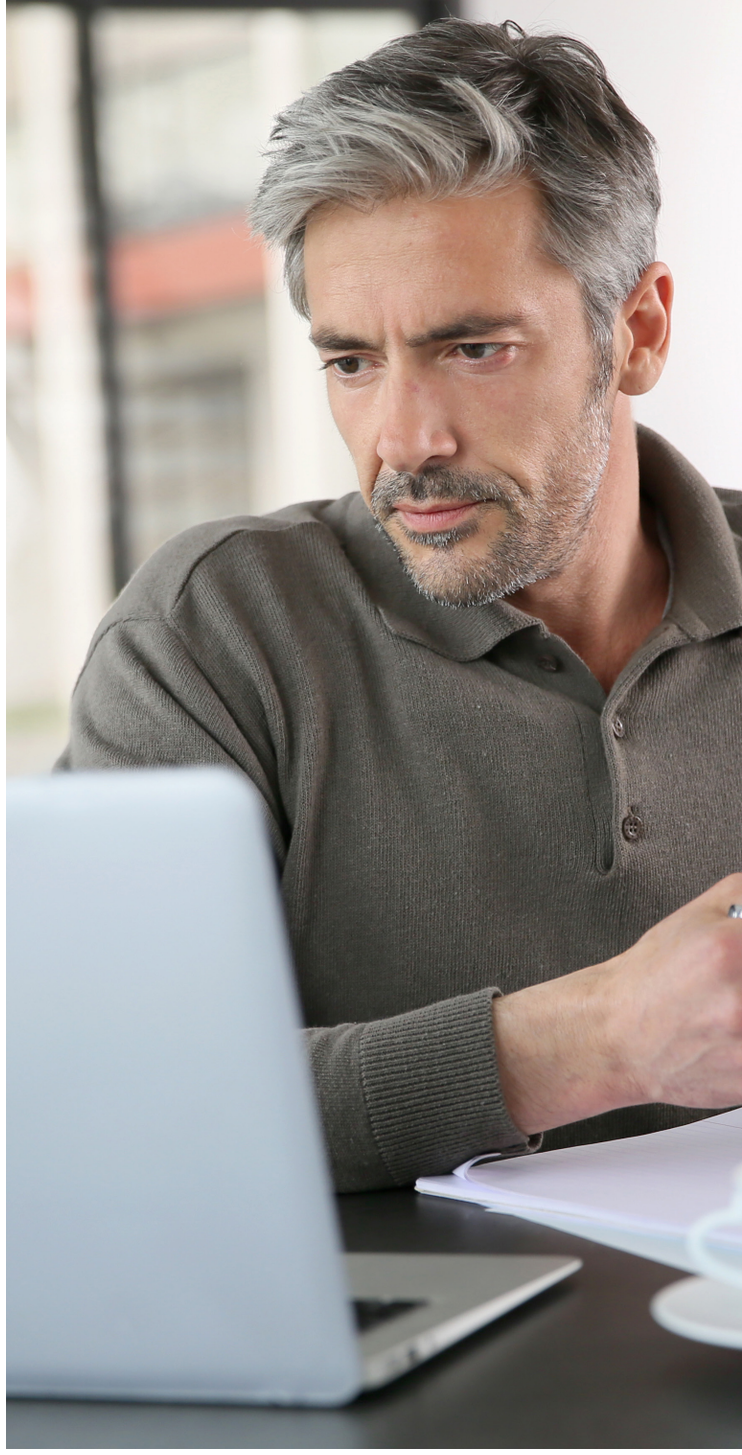
Is Social Security Secure?

First, will Social Security be able to pay benefits by the time you retire, 15, 20 or even 30 years from now? While no one can predict the future with 100% certainty, it's unlikely that Social Security as we know it will disappear during your lifetime. Here's why: Money paid out to current retirees comes from taxes collected from people who are still working. As long as the amount currently being collected in taxes is more than the amount being paid out, Social Security is "solvent." Any taxes collected in excess of amounts paid out goes into a reserve, to help fund future shortfalls.

According to the Social Security Administration, "benefits are now expected to be payable in full on a timely basis until 2037, when the trust fund reserves are projected to become exhausted."[1] At that point, when the reserve fund is projected to run out, ongoing tax collections are expected to be sufficient to pay 76% of scheduled benefits.

What can you do *today* to become less dependent on Social Security benefits in the future, especially if you want to stop working before reaching the official full- retirement age? An obvious answer is to save more now, well before you retire, but that's only part of the picture. What's also extremely important is to save "smart," which means investing wisely and taking full advantage of opportunities to increase your tax-deferred savings early, allowing them to grow for many years before you retire.

If you are already contributing the maximum amount possible to your 401(k) (or 403(b)) plan at work, or to an IRA, you already have some tax-deferred savings[§]. However, there are limits on the amount you can contribute to those accounts. Annuities can be a smart way to generate additional, secure income for the future. An annuity's ability to defer taxes on investment income offers a significant advantage over an investment account that is not tax-deferred. Annuities can be a sensible, flexible way to generate additional secure income in retirement beyond whatever Social Security provides, either for a specified number of years or for the rest of your life.



Past performance is no indication of future results

The question is, can you realistically and reliably earn an after-tax return of 4%, year after year?

The 4% rule

Next, let's examine the notion that you can safely withdraw 4% of your savings per year in retirement. That was the general understanding of retirement planning for a long time, but most financial professionals now acknowledge that 4% may be too generous. The reason to question the 4% guideline is that this withdrawal rate assumes you can earn at least 4% after taxes on the rest of your money, the amount that remains invested after you make those annual withdrawals.

Maybe not, and here's why:

Interest rates are low compared to where they've been for much of the past 100 years, largely because, during most of that period, inflation was much higher than it is today.[2] This means the returns offered today by low-risk, fixed-rate investments such as Treasury securities and corporate bonds, are low. For an investor in a 25% tax bracket to earn a 4% return from bonds *after taxes* would require a pre-tax return of about 5.33%. However, expecting to earn 4% after tax from low-risk bonds isn't realistic in today's environment.

Since bonds are unlikely to provide a 4% after-tax return, it might seem better to shift most of your savings to stocks. In most years, and certainly over the long term, the return from stocks has been higher than for bonds. But actually, in some years stocks have done worse than bonds—occasionally, a lot worse. If the market has a bad year (or two), and you are too heavily invested in stocks, your retirement nest egg would shrink considerably and could take a number of years to recover. That's not necessarily a huge problem when you are young and still working, but as you get closer to retirement it can be a more significant setback. And once you have retired, if your assets decline because you were heavily invested in the market in a down year, withdrawing money at that 4% rate will make it that much harder for those investments to recover. So, switching most of your money into the market is not a reliable way to generate all the additional income you will need to meet your retirement goals.Instead of counting on withdrawing 4%, it's a good idea to plan on being a bit more conservative. To compensate for a lower withdrawal rate, you can set up a variable annuity that offers a minimum guaranteed** lifetime income† to supplement those withdrawals. This type of annuity allows you to participate in the growth potential* of the stock market while guaranteeing a minimum level of income. In other words, while you plan to consume a smaller slice of your retirement savings pie every year, adding an annuity to your overall retirement portfolio can help provide income for life.

** Guarantees are backed by the claims-paying ability of the issuing insurance company

† Optional benefits are available for an extra charge in addition to the ongoing fees and expenses of the variable annuity.

* Investing involves risk, including possible loss of principal



Living longer

Finally, we consider the possibility of outliving our savings, a concept often referred to as "longevity risk." People are living longer than retirees did in previous generations. We used to expect retirement to last about 10 years; today, 20 years, or even more, is likely to happen. While that is good news, it means you will probably need your savings to cover more retirement years than any other generation in history.

We also expect to lead better, more active lives in retirement than previous generations. Advances in medicine and technology allow us to control medical conditions that used to leave us incapacitated or cut our lives short. We can travel, play tennis and go out dancing into our 80s, on replaced knees and hips. That's definitely something to look forward to, but since these activities cost money we should not expect our living expenses to drop dramatically after we retire. A variable annuity can be an effective way to generate extra income to help afford those activities, or new ones we discover, for a long time.

We should also expect out-of-pocket medical expenses to increase, especially as we move into our 80s and 90s. Medicare does not fully cover the cost of what can be expensive prescription medications—medications we are more likely to need as we get older. Medicare also does not cover the cost of a long-term care facility if it turns out that you or your spouse need that kind of care. A variable annuity that provides guaranteed lifetime income could be an effective way to help cover these higher medical expenses. And, if your expenses turn out to be lower than what your retirement income covers, you can leave a legacy for your heirs—not just a financial inheritance, but also the example you set for them by saving smart and spending responsibly.

Remember that even the longest journey begins with little steps, so you shouldn’t expect to have all your retirement savings in place by now.

But you can take an important step on the path to financial freedom by setting up an annuity that provides secure lifetime income for your future. When you’re ready to retire, that additional income will be there waiting for you, so you can continue to enjoy your journey with some peace of mind.

1 Social Security Administration, "The Future Financial Status of the Social Security Program", Nov 2010

2 Trading Economics, "United States Fed Fund Rate", Jun 2018

Before investing, investors should carefully consider the investment objectives, risks, charges and expenses of the variable annuity and its underlying investment options. The current contract prospectus and underlying fund prospectuses, which are contained in the same document, provide this and other important information. Please contact your Internal Wholesaler to obtain the prospectuses. Please read the prospectuses carefully before investing or sending money.

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