GUARANTEED RETIREMENT INCOME: COVER YOUR WANTS, NOT JUST YOUR NEEDS

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Many retirees want more covered than just their essential needs, and that means they should be rethinking how much guaranteed income they need for a comfortable retirement.

Everybody needs a steady retirement paycheck to cover the basics: shelter, clothing, food, transportation and healthcare. But what about wants beyond those five basic needs? "People aren't happy just meeting those living expenses. They say, 'I want more. I want to live a comfortable life,'" says Michael R. Harris, a senior educational financial professional with the Alliance for Lifetime Income. "You've got to have clothes on your back. If you have that, you can survive and have a life. But it's not a full life."

Essentially, people are creating a new definition for essential needs. Wants become needs. Call it "comfort creep." It's a bit like keeping up with the Joneses, but instead of craving what your neighbors have, it's a matter of acknowledging what you personally need to be comfortable in retirement—and then figuring out how to fund it securely.

A TEXAS COUPLE AND THEIR HORSES

Consider a 65-year-old couple in Texas with $600,000 in assets who tally up their projected annual retirement needs with the help of their financial advisor. Their mortgage is $12,000; utilities and home maintenance run $14,000; groceries cost $6,000; health insurance is $6,000; transportation is $5,000; and their horses cost them $7,000. Horses? To them, keeping their horses in retirement is a must.

So how can this couple cover their bases? Their annual retirement income basics total $49,500, and they get $40,800 in Social Security. That leaves them with a $9,200 shortfall—a security gap. "That's the amount that a guaranteed lifetime income stream can fill in," says Harris. If the couple buys an annuity for $200,000, a third of their assets, it could generate guaranteed income of $9,821 annually.[1] They can stay in their house and keep their horses—for a richer, worry-free retirement. And they still have $400,000 to generate income to pay for other expenses.

NEEDS, WANTS, WISHES

How can you set yourself up for a comfortable retirement like this couple? The best way to approach this is to think about how you're spending money and divide it into three categories: needs, wants and wishes. Draw a pyramid and put needs at the base. Needs are the basics, the foundation, your nonnegotiables.

Next, wants are in the middle of the pyramid. Think of this as comfort money. Wants are things that would be nice to have if everything works out. I want to be able to play golf. I want to pay for my granddaughter's college education. You might be surprised by how much fits into this category. Think visits and vacations with family or friends, tickets to sports or cultural events, or hobbies like ballroom dancing or collecting.

Finally, add wishes at the apex of your needs, wants and wishes pyramid. Think of this as dream money. Wishes are what you'd like to do if you had enough income beyond your wildest expectations. I want to buy a motor home and visit all the national parks out West. I want to donate to my library's expansion and get my name on a supporters' plaque.

TALK TO YOUR FINANCIAL PROFESSIONAL

Next, talk to your financial professional about how you can best fund your needs, wants and wishes. Start at the bottom of the pyramid. Typically, you want guaranteed income—Social Security, a pension if you have one, and possibly annuities—to cover your needs. An investment portfolio, which generates fluctuating or probable income, can cover your wants and wishes. But for wants that are really needs in your mind, that's risky. Probable income isn't guaranteed. CDs and bonds may offer some level of relatively stable income, but they do eventually mature, and interest rates change. Harris notes he just had a big CD come due that was generating 3.5% interest, and now the comparable interest rate is below 1%.[2]

Depending on how important it is to you to fund your wants, it can make sense to guarantee more, moving up the pyramid, and leave less to probable income sources. "Maybe you need annuities for wants and not just needs," Harris says. That's why the Texas couple used guaranteed income to cover the expenses to keep their horses in retirement. They don't need to keep horses, but they sure want to.

Whatever your wants are, covering those wants with guaranteed of your income can lead to a more comfortable retirement.

[1] Data sourced by CANNEX Financial Exchanges Limited as of June 5, 2020. The estimated annual income amount of $9,821 is for a single premium immediate annuity (SPIA). This is based on an average of the top five highest annual income amounts from 18 insurance companies that provided data to CANNEX Financial Exchanges Limited. The data reflects a joint life annuity with annual payments, with a premium of $200,000, for two annuitants, a male born on June 5, 1955 and a female born on June 3, 1955, both residing in Texas. This is for illustrative purposes only. Please contact a financial professional for information on costs and details on annuity options available to you.

[2] A certificate of deposit (CD) is a bank product that offers a specified interest rate over a specified time period. CDs are insured by the FDIC up to the $250,000 legal limit. Interest earned from CDs is considered taxable income.

Expenses are based on state averages, U.S. Census Data and certain assumptions.

Annuities are long-term investments designed for retirement purposes. The value of variable annuities is subject to market risk and will fluctuate. Product guarantees are subject to the claims-paying ability of the issuing insurance company.

Earnings, when withdrawn, are subject to federal and/or state income tax, including a 10% tax penalty for withdrawals before age 59½.

Some income guarantees offered with annuities take the form of optional riders and carry charges in addition to the fees and charges associated with annuity products.

There is no guarantee that any investment will achieve its objectives, generate positive returns, or avoid losses. Investments in annuity contracts may not be suitable for all investors.