Episode #315 – Test Drive an Annuity Calculator

Hi, welcome to another episode of Monday Script Monday. My name is Brian Manderscheid. Today I want to unveil the Test Drive an Annuity Calculator. We created this calculator, this tool, specifically for you so that you can calculate what an annuity may look like for your retirement plan. We firmly believe that annuities play a crucial part in a holistic retirement plan, essentially allowing you to provide an additional income stream over and above, let's say pensions and Social Security to provide enough income to help cover your essential retirement expenses.

This calculator essentially has five inputs, and the reason we did this was to create a tool that's simple enough to be able to very easily calculate what an annuity may look like for you and how much lifetime income it could potentially provide. Those five inputs are: your age and potentially your spouse's age as well, the amount of money that you're potentially looking to fund into an annuity, if you’d like the income to be just for your life or potentially for your spouse's life as well, how long you want to defer taking payments or receiving payments for the annuity, whether that's one year, five year or ten years, and lastly your contact information so that the advisor can get in touch with you and talk to you about your financial situation as well as how the annuity may fit.

Now after you run the calculator, it essentially provides you a shortened report to give you more information about the annuity and how much income it may potentially provide. In addition to providing, you with the potential income that the annuity could provide over your lifetime, it's also going to compare or anchor that amount against three hypothetical scenarios, basically allowing you to compare how much income the annuity can provide versus other scenarios that may be available to you. Keep in mind this calculator doesn't replace a full carrier illustration or the other ancillary reports that your advisor can provide, but instead just provides the snapshot of what an annuity may look like for you.

If you're interested in seeing more in-depth about what this annuity is or how it may fit for you, you can request a free income report from your financial advisor, essentially allowing you to get a more comprehensive comparison as well as look at multiple annuity options and additional information on how an annuity may look like for your financial situation. With that, we're going to go ahead and get to the screen here and give you a live demo of how this calculator works and the report it generates. Thank you.

Now that we're in the Test Drive an Annuity Calculator, I'm going to give you a quick run-through on how to use the tool itself, how to play around with it, and ultimately, what the report provides and how to view that information. For this scenario, I'm going to assume I'm sixty. I'm also going to do a joint life payment, meaning my spouse would get this income as well, and my wife is going to be sixty in this scenario. We're going to look at $100,000 for the annuity amount in this scenario and we're going to defer 5 years to age 65. Again, all this can be customized for your scenario. You can play with it and run multiple iterations, ultimately to provide the best option for yourself.

I’m going to go ahead and put my information here. Once I have all the information, I'm going to go ahead and hit “create a PDF,” and when you hit create a PDF, it's going to run the simulation and provide you some sample information up top and then the report below. A couple of things I look at first are how much income we could potentially get from this annuity at age 85, what the actual income amount is at that same age, what the internal rate return is, which basically is a required return needed or necessary to provide the same amount of income that the annuity provides in this scenario, and also what the annuity amount we're funding is.

A couple of things here. The first page is a breakdown of our illustrated values. You can see that there are two different buckets, one being our cash account or our accumulation value, and the second being our income account, which basically is used to calculate our lifetime income and also used to calculate a 5-year payout death benefit should we prematurely pass away. You can see this particular annuity; we're not necessarily lighting it up with returns. You can see single-digit returns in this hypothetical scenario. The account itself isn't necessarily growing all that substantially, but instead, most of the value in this annuity is in this income bucket. You can see when we turn on the lifetime income stream at age 65, this creates a joint life payment for my life and my wife's life with a starting paycheck being about $8,500 a year, which steadily rises over time based on the non-guaranteed and projected performance of this annuity.

You can also see that this protected income value, which is used to calculate our income stream and also a five-year spread death benefit if we were both to pass away prior to turning this income rider on, our beneficiaries would get $224,000 spread out over a 5-year time frame. That's a basic synopsis of how the annuity works. Again, you have two different buckets. Your cash account, your income account, your lifetime income on the far right as well as this potential death benefit should you prematurely pass.

The next page of this report is a comparison of the suggested annuity versus three different hypothetical portfolios: a steady 7% return every single year with a 1% fee, the last 20-year returns of the S&P 500 plus that same 1% fee, and a 7% average return using an unfavorable sequence also having a 1% fee. Now these aren't actual investments, but instead just hypothetical scenarios essentially so we can create benchmarks and see how favorable or unfavorable the annuity income is relative to these three other scenarios.

When you look at the income at age 85, you can see the annuity has $360,000 of cumulative income over that same time frame versus roughly

$200,000 and only $91,000 in the least favorable sequence. At age 95, the income is substantially higher than the annuity because of the 10 more years of income plus the income increases over that time frame with $800,000 of income. Again, the same numbers here because if you look to the notes in the far right, you can see when those other accounts ran out of money relative to the annuity. Said in another way, when we try to pull the same amounts of income that the annuity provides from these three hypothetical scenarios, they aren't able to provide the same income and run out of money prior to what we would call life expectancy.

Additionally, when we look at the internal rate of return out to age 95, which assumes that either you or your spouse lived to that age, the IRR is 10.33%, meaning that you would have to earn double-digit returns every single year over the next 35 years to provide the same income that was generated from the suggested annuity. The accumulation value of the annuity isn't very strong, and it does run out of money, however, with this type of annuity you can run out of money, but you can never run out of income. The other alternatives for the most part look better on an accumulation basis whereas the annuity looks best on an income basis, especially when you stretch out life expectancies out to age 95.

On the next page is a little bit more detailed view of this analysis. Again, you can see the hypothetical returns from the annuity, the account value, and the income that's being generated starting with about an $8,400 paycheck and steadily increasing from there, versus the 7% steady return with a 1% fee followed by the last 20 years of the S&P returns, also with a 1% fee, and lastly a 7% average return.

You can see an unfavorable sequence with losses heavy in the beginning years. Generally speaking, the losses during the first five years leading up to retirement, as well as the first five years of retirement, can create a huge burden in creating lifetime income if you're suffering heavy losses during your peak at or near retirement. Just to reiterate, while the annuity runs out of money at age 77 in this scenario, the income would continue and since we selected a joint life benefit, even if I were to pass away, my wife would receive the benefit upon my passing.

Lastly is a disclosure page at the back to go over some of the details of the report itself. That is the Test Drive an Annuity Calculator. Again, you can feel free to modify, play with these numbers, change the amounts, change the deferral lengths, and change whether you want a single or joint payment. Again, this isn't going to create an actual carrier illustration, you're going to want to work with your financial advisor to run through the various options available for you. This does at least allow you to test drive an annuity as well as giving you a starting point to working with your financial advisor to talk more about the various options you've looked at and how you want to work with your financial advisor.

Now that we reviewed and showed you how to use the test drive annuity calculator, the next step is for you to contact the advisor who sent you this video. They can essentially create a full income report for you, and again, that's going to give you a full comparison of what the annuity may look like for you, along with other various financial alternatives that you may consider. Additionally providing multiple annuity options, and the advisor can go over the pros and cons of each. Ultimately, your advisor can help determine what annuity is right for you. Lastly, it also includes additional information about how the annuity works as well as how it can be used to help supplement other sources of retirement income such as Social Security and pension. Thank you very much and we'll see you next time.