

Marketing Annuities as Investments to Finance Retirement Healthcare Expenses

Recent surveys of people planning for retirement have consistently revealed their concern for healthcare expenses in retirement and the need for financial planning that specifically addresses that concern. Many people now see that healthcare might be their largest single expense in retirement. These people are in the market for professional guidance in understanding how much healthcare might cost in retirement and exploring different investment options they could implement now to ensure an income to cover those expenses year after year as long as they live.

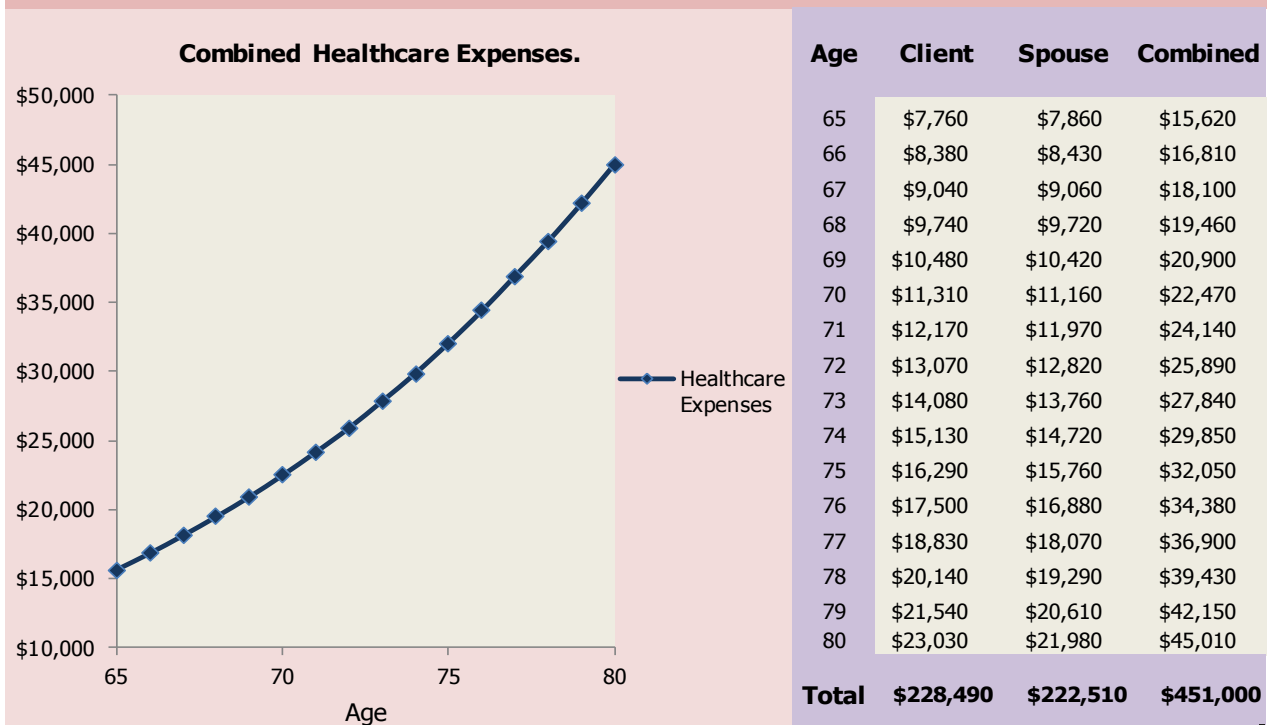
Estimating Healthcare Costs in Retirement

For most people, the concern about paying for healthcare in retirement starts with not having a realistic estimate of how much healthcare will actually cost. **RetireMark**, developed by **HealthView Services**, is a unique financial planning system that uses the most recent actuarial-based healthcare expense data to calculate an individual's out-of-pocket healthcare expenses. A financial advisor can use a client's age, gender, health condition, and so on to calculate the client's life expectancy and total healthcare expenses if the client retires at age 62, or 65 or whatever age the client chooses. RetireMark provides the advisor with estimates of how much healthcare is likely to cost the client year after year in retirement. With estimates of annual healthcare expenses in hand, the advisor is ready to create a concrete financial plan that will provide the client with an income to cover healthcare costs through retirement as long as the client lives.

Suppose a Financial Advisor meets with a couple, currently in very good health at age 55, who want to develop a plan to finance their retirement healthcare expenses. The Advisor uses RetireMark to estimate the likely cost of healthcare for the couple from age 65 to age 80, as shown in Figure 1. The Advisor emphasizes two important features in the expenses:

- 1. Healthcare expenses are expected to grow throughout retirement – at around 7.00%/year.**
- 2. Healthcare expenses for each member of the couple will continue as long each member lives – which is unknown.**

Figure 1. Individual and Combined Retirement Healthcare Expenses for a Couple.



Ensuring an Income to Cover Healthcare Costs

Annuities are unique among financial investments in being able to provide retirees with an income as long as they live. Just as there are different types of annuities – each with features designed to address specific needs – there are different ways annuities can be used either to create a single-purpose plan targeting healthcare expenses or a multi-purpose plan where healthcare is one expense among others.

Suppose the couple with the healthcare expenses in Figure 1 decide they need an investment that will provide an income sufficient to cover their healthcare costs, increase through retirement as healthcare costs increase and last as long they live.

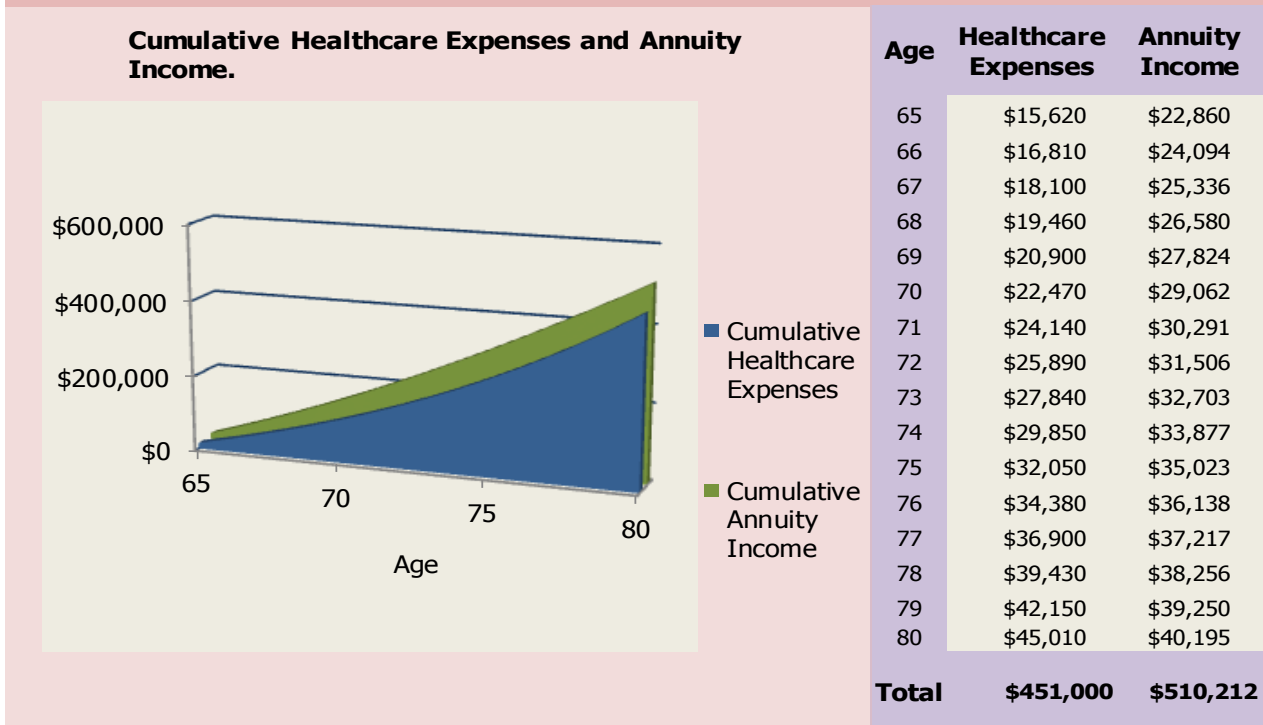
The Advisor describes how a Variable Annuity (VA) with a *Guaranteed Minimum Income (GMI)* option could provide an income stream that satisfies their needs:

- The GMI option guarantees that the *Income Base*, from which retirement Income will be withdrawn, will increase from one year to the next by *at least the Minimum Guaranteed Rate (MGR)*, e.g., 6%.
 - When the MGR exceeds the rate of return from the VA investment portfolio, the Income Base will increase by the MGR.
 - When the rate of return from the VA investment portfolio exceeds the MGR, the Income Base will increase by the investment rate of return.
- The GMI option starts at age 65 and continue to age 91, when the couple can renew it if they wish.

The Advisor then uses the *Annuity Simulation* feature in RetireMark to simulate the hypothetical income stream the GMI might provide.

Figure 2 summarizes the results where the Annuity Simulation has selected an Initial Investment of \$250,000 at age 55 and graduated withdrawal rate that increases from 4.00% at age 65 to 6.00% at age 80.

Figure 2. Annuity Income Provided each Year for Healthcare Expenses.



While the \$510,212 total income exceeds the \$451,000 total healthcare expenses, income in some years is less than healthcare expenses. The Advisor creates a low-risk (2% annual return) investment for the couple to manage excess income and unmet expenses:

- When income exceeds expense, excess income is *deposited* in the investment.
- When expense exceeds income, income is *withdrawn* from the investment to cover the unmet expense.

Table 1 details year by year annuity income, healthcare expenses and low-risk investment to manage excess income and unmet expenses.

The Advisor points out the \$79,785 at the bottom of the Low-Risk Investment column and summarizes: *\$250,000 invested in the Guaranteed Minimum Income Variable Annuity covers \$451,000 retirement healthcare expenses and provides an additional \$79,785 in savings.*

Table 1. Year by Year Annuity Income, Healthcare Expenses and Low-Risk Investment to Manage Excess Income and Unmet Expenses.

Age	Rate of Return	Account Value	Income Base	Income Withdrawn	Healthcare Expenses	Unmet Healthcare Expense	Excess Income	Low-Risk Savings Investment
55	7.66%	\$250,000	\$250,000	\$0	\$0	\$0	\$0	\$0
56	6.28%	\$266,650	\$266,650	\$0	\$0	\$0	\$0	\$0
57	15.27%	\$280,729	\$282,649	\$0	\$0	\$0	\$0	\$0
58	11.48%	\$320,789	\$320,789	\$0	\$0	\$0	\$0	\$0
59	9.71%	\$354,408	\$354,408	\$0	\$0	\$0	\$0	\$0
60	1.25%	\$385,277	\$385,277	\$0	\$0	\$0	\$0	\$0
61	4.95%	\$386,240	\$408,393	\$0	\$0	\$0	\$0	\$0
62	24.57%	\$401,496	\$432,897	\$0	\$0	\$0	\$0	\$0
63	9.67%	\$496,129	\$496,129	\$0	\$0	\$0	\$0	\$0
64	0.12%	\$539,144	\$539,144	\$0	\$0	\$0	\$0	\$0
65	5.96%	\$534,399	\$571,492	\$22,860	\$15,620	\$0	\$7,240	\$0
66	-10.70%	\$538,046	\$582,922	\$24,094	\$16,810	\$0	\$7,284	\$7,384
67	19.37%	\$451,000	\$593,803	\$25,336	\$18,100	\$0	\$7,236	\$14,962
68	25.55%	\$508,513	\$604,096	\$26,580	\$19,460	\$0	\$7,120	\$22,642
69	-17.19%	\$606,773	\$613,761	\$27,824	\$20,900	\$0	\$6,924	\$30,357
70	9.71%	\$468,577	\$622,763	\$29,062	\$22,470	\$0	\$6,592	\$38,026
71	3.75%	\$480,328	\$631,067	\$30,291	\$24,140	\$0	\$6,151	\$45,511
72	9.98%	\$463,246	\$638,640	\$31,506	\$25,890	\$0	\$5,616	\$52,696
73	4.32%	\$473,339	\$645,452	\$32,703	\$27,840	\$0	\$4,863	\$59,478
74	-7.64%	\$456,351	\$651,476	\$33,877	\$29,850	\$0	\$4,027	\$65,628
75	9.84%	\$383,046	\$656,688	\$35,023	\$32,050	\$0	\$2,973	\$71,048
76	-1.25%	\$381,883	\$661,066	\$36,138	\$34,380	\$0	\$1,758	\$75,501
77	5.67%	\$337,153	\$664,591	\$37,217	\$36,900	\$0	\$317	\$78,805
78	-11.68%	\$315,681	\$667,250	\$38,256	\$39,430	-\$1,174	\$0	\$80,704
79	7.40%	\$237,397	\$669,029	\$39,250	\$42,150	-\$2,900	\$0	\$81,121
80	0.00%	\$213,340	\$669,921	\$40,195	\$45,010	-\$4,815	\$0	\$79,785
Total				\$510,212	\$451,000			\$79,785

**\$79,785
Additional
Savings**