

# The fall and fall of annuity rates

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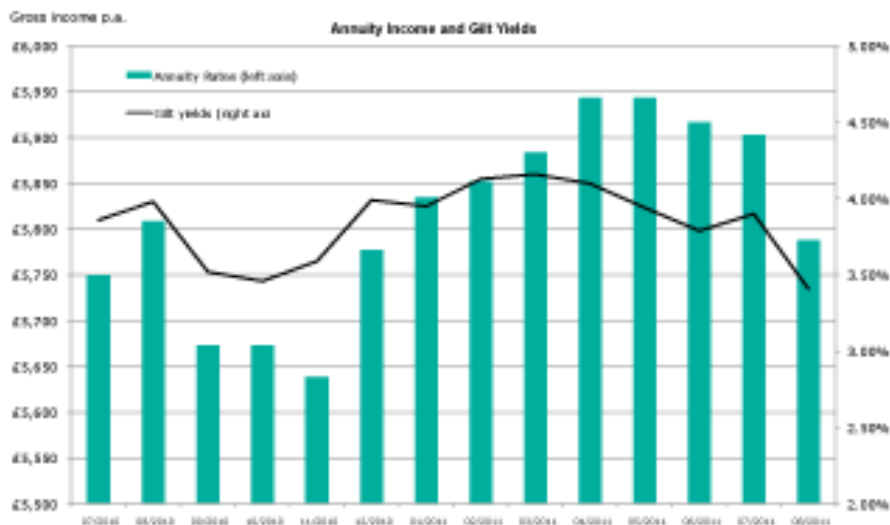
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## How to respond to falling rates

All the major annuity providers recently cut their rates for guaranteed annuities as corporate bonds and gilts fell following the turmoil in the global financial markets, which has been caused by the European debt crises and concerns about the US economy.

The chart below shows how our benchmark annuity rate has changed over the last 12 months. (The benchmark rate is male age 65, female 60, £100,000 purchase, joint life 2/3rds, guaranteed 5 years and level payments). Annuity and gilt yields fell at the end of last summer but picked up later in the year, but the ongoing economic turmoil is likely to have a further negative effect.



Enhanced annuity rates have also been cut because they too are priced in relation to the same yields.

In simple terms, this means an individual retiring now with a pension fund of £100,000 will secure a lifetime income £115 per year less than a few weeks ago.

The main reason for the sudden reduction in yields stems from the European and US debt problems. When investors are worried about global equities there is a strong demand for gilts. As the price of gilts rise, the yields fall - UK gilt yields are at their lowest level for many years.

## What can be done about falling rates?

At times of falling annuity rates I am always asked, "Should I hold off buying an annuity until rates increase?" My stock answer is that individuals should take as much time as they need to decide which type of annuity to invest in and once that decision is made they should not necessarily delay because rates could fall even further.

Although it's impossible to second guess the financial markets and accurately forecast future annuity trends, professional advisers and their clients can maximum the amount of lifetime annuity income by taking a few simple strategic and tactical steps in the right direction.

And remember, it's important to separate the strategy from the tactics.

### **Strategy**

It's important to have a plan. And, strategically there are two important questions:

- When is the best time to take tax free cash and income?
- What type of annuity or drawdown?

The timing is important because two factors come into play; what is the trend for annuity rates and what are the income requirements?

If an annuity is a long term investment then investors should think about their longer term income requirements and, in particular the issue of inflation.

Many advisers and their clients are taking decisions about a long term commitment based on short term considerations e.g. who is paying the highest income? A more sensible approach is to consider investment linked annuities which provide the potential for future income growth and flexibility.

### **Tactics**

In order to execute the plan it's necessary to make the right tactical decisions. These include shopping around using the open market option to find the best highest paying annuity and, where appropriate, applying for enhanced annuities which take health into consideration.

Other tactical decisions include the timing of annuity purchase to try and strike when rates are at their highest. If there is concern about purchasing annuities when rates / yields are low, another possible consideration is an investment-linked annuity where the initial income is not pegged to gilt yields.

With conventional annuities, income is set for life at the point of annuitising, with no potential for future income growth. An investment-linked annuity has the opportunity to benefit from the highs and lows of the markets over a 20 year period, not just at a single point in time when rates and markets could be low.

### **My view**

I have been following annuity rates for long enough to know that getting the timing right is difficult, if not impossible. My view is that advisers and their clients should take as much time as they need in order to decide on the strategy, but once a decision has been made it makes sense to arrange the annuity sooner rather than later because in my experience few people gain from deferring their annuity purchase.

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### **Expert view**

