Annuities gain popularity as Baby Boomers age

Russ Wiles, The Arizona Republic 10:10 a.m. EDT August 22, 2015

(Photo: Getty Images/iStockphoto)

Six-plus years into a rising stock market, many Americans continue to crave financial certainty and shun risk, which helps to explain why annuity sales have held up so well.

It's not just the stock-market backdrop that makes solid annuity sales interesting — it's also the low interest rates. More investors are buying annuities even though they're paying some of the slimmest yields in decades. "Normally, declining rates hold down sales of interest-sensitive products," noted LIMRA, an insurance and annuity research group, commenting on a 3% rise in annuity sales in 2014.

There are different types of annuities, which makes it hard to generalize. Variable annuities that feature stock-market funds now account for more than half of overall sales, while conservative fixed or guaranteed-rate contracts pay steady, bondlike yields. Annuities in the latter category have enjoyed rising sales over the past couple of years despite paying yields of just 2% to 3% or so.

Clearly, annuity buyers aren't focused solely on yields. Here are other factors that help explain the improved popularity of annuities, including conservative products:

•All those Baby Boomers have moved into prime annuity-buying ages.

Buyers typically get interested in annuities when they reach their mid-50s or 60s, and nearly all Baby Boomers are now in this range.

The opportunities for insurance companies that sell annuities could continue for decades, as millions of other adults, now entering their 40s and early 50s, aren't far behind. In 2011, 42.5 million Americans were 55 and up, but that will rise to 64 million by 2025, LIMRA projects.

Nor is it just the graying trend per se that explains rising annuity sales — there's also a pronounced risk aversion among Americans generally. Despite a resurgent stock market now trading again near record heights, millions of Americans want nothing to do with it.

•Buyers might be acclimatized to low interest rates.

If you think interest rates will rise, it's smart to delay buying a fixed-rate annuity so that you can lock in a higher yield later. But after years of low interest rates, it's not a certainty that rates will budge by much anytime soon. The Federal Reserve plans to boost rates, of course, but nobody expects the changes to be dramatic. Other interest rate-sensitive investments, including bonds and bond mutual funds, also have remained popular despite low yields.

Besides, the Fed's influence is focused on short-term rates such as those affecting money-market yields and credit card interest rates. Annuity yields are more likely to reflect intermediate-term interest rates, as these investments are backed by the bond portfolios held by insurance companies, noted Andrew Murdoch, a senior vice president of AnnuityFYI, an annuity comparison and research website.

Still, Murdoch and others see a potential uptick in annuity sales should interest rates start climbing. "A lot of people are sitting in cash, waiting for rates to rise," he said. "The higher the interest rates, the more generous insurers can be."

•Many buyers may underestimate the annuity benefits of Social Security.

Most Americans have access to an annuity already. It's called Social Security. Granted, the federal retirement program isn't exactly the same as annuity contracts sold by insurance companies, but a primary feature — the ability to collect retirement income for as long as you live — is similar.

In fact, many analysts consider Social Security to be better than commercial annuities. For starters, the federal government, not individual companies, stands behind those payments. Despite chronic federal deficits, Uncle Sam is still widely viewed as a stronger credit bet than any insurance company.

Another advantage is that Social Security benefits rise over time, thanks to cost-of-living adjustments that often aren't available on commercial annuities. Further, Social Security benefits rise by up to 8% annually for younger seniors who delay taking them before age 70.

Because of the COLA features, Social Security could be viewed as a type of inflation-protected government bond, said Michael Kitces, a financial adviser and commentator in Reston, Va.

He suggests that retirees consider delaying the receipt of Social Security benefits upon reaching the eligibility age of 62, even if it means tapping into other investment accounts. "Do I really want to spend my portfolio down for my Social Security to grow bigger?" he asked in an online interview that can be seen on Morningstar.com. "The answer is yes — you really do."

This strategy, of younger retirees using savings to pay current living expenses while waiting for their Social Security benefits to increase, has been likened to buying an annuity from the Social Security Administration. In a report, the Center for Retirement Research at Boston College called it "generally the best deal in town, especially in today's low interest-rate environment."

http://www.usatoday.com/story/money/2015/08/22/annuities-gain-popularity-baby-boomers-age/31486595/