IN DEPTH Planning

3 guaranteed-income strategies for an uncertain economy

Investors are clamoring for guaranteed-income strategies this year primarily due to an uncertain stock market and spiraling inflation.

November 7, 2022 *By Gregg Greenberg*

All due respect to founding father Benjamin Franklin and his Almanack-writing alter ego “Poor Richard,” but there are some certainties in this world other than “***death and taxes***.” And believe it or not, they can be found emanating from Wall Street and Washington, D.C.

Guaranteed income strategies offered by financial companies have soared in popularity this year, primarily due to an uncertain stock market and spiraling inflation. Investor interest in inflation-adjusted government bonds and Social Security payments has also been piqued, as retirees desperately seek ironclad income streams to help make ends meet.

I BOND BREAKOUT

So for financial advisers seeking certainty for their clients in an uncertain world — or all those “Poor Richards” out there seeking to elevate themselves out of poverty — here are a few guaranteed income strategies to consider.

Just as gold shined in the late 1970s as investors sought a store of value in the face of runaway prices, ***Series I bonds*** emerged this year as a financial bright spot in a similar era of rampant inflation. And even better than gold and its 21st century progeny ***bitcoin*** (both of which have failed to whip inflation this time around), Series I bonds guarantee an income stream, and a fairly healthy one at that.

The Series I bond, which was first issued by the Treasury in 1998, is an accrual-type savings bond tied to inflation. The bond is issued at face value with a 30-year final maturity comprised of a 20-year original maturity period immediately followed by a 10-year extended maturity period. The earnings rate, which is made up of a fixed rate and an inflation rate, can change every six months. The fixed rate stays the same over the life of the bond, while the inflation rate can change every six months from the bond’s issue date.

The new rate on Series I savings bonds as of last Tuesday is 6.89%, which is down from the 9.62% rate for the six months ended last Monday, but still robust as a result of September’s elevated reading on consumer prices.

Sweetening the deal, I bond earnings are exempt from both state and local income taxes. Federal income taxes can be deferred until redemption, final maturity or other taxable disposition, whichever occurs first.

“With inflation staying at or near 40-year highs for most of 2022, Americans are hungry for ways to fight the impact of rising prices and maintain the purchasing power of their savings. With most bank savings accounts still paying little to no interest, Series I government savings bonds have become an attractive place to park extra funds that would otherwise be held in cash,” said Todd Stewart, managing director of investment research at SageView Advisory Group.

In a bummer for financial advisers, however, they can only be purchased through ***TreasuryDirect.gov***, where the maximum annual investment per person is $10,000. I bonds also can’t be purchased from inside a qualified retirement account. And while there’s actually a way to purchase an additional $5,000 worth of I bonds each year by using a tax refund, it requires overpaying taxes to ensure a refund of at least that amount.

“I Bonds may warrant consideration for investors who want to prioritize inflation protection, but some of the characteristics and constraints detract from what may initially seem like an attractive investment opportunity,” said Derek Vasko, senior director of investment strategy for Choreo Advisors.

ANNUITY EXPLOSION

Inflation-adjusted government bonds haven’t been the only standout guaranteed income strategy this year. Annuity sales have also skyrocketed in 2022 as investors pursued steady payouts amid a volatile equity market.

Total U.S. annuity sales increased 27% to $79.6 billion in the third quarter, the ***highest quarterly sales*** recorded since Limra began tracking annuity sales and nearly $9 billion above the previous record set in the fourth quarter of 2008 during the Great Recession.

Total fixed-rate deferred annuity sales were $29.8 billion in the third quarter, 159% higher than third quarter 2021 sales, according to ***Limra***. This is the best sales quarter for fixed-rate deferred annuities ever recorded. In the first nine months of 2022, fixed-rate deferred annuities totaled $74.4 billion, a 77% increase versus the same period last year.

Fixed indexed annuity sales also took off, totaling $21.4 billion in the second quarter, up 25% from the prior year. Year to date, FIA sales were $57.4 billion, a 22% increase from last year, according to Limra.

Fixed-rate products offer a specified crediting rate to consumers over a given period, such as three or five years. Indexed products are linked to the stock market, offering maximum and minimum returns over a specified period. Rising interest rates have made both types of annuities more attractive to financial advisers and consumers, since insurers are able to offer higher payouts.

“The combination of very attractive rates in fixed annuity products and the ongoing desire of investors for portfolio protection have been driving annuity sales. I expect this is just the beginning of a very long-term trend,” said David Lau, founder and CEO of DPL Financial Partners.

For his part, Lau has certainly benefited from the annuity explosion. ***DPL***, which specializes in commission-free annuities, recently announced two of its high-profile outside investors, Todd Boehly’s ***Eldridge*** and Robert Diamond’s ***Atlas Merchant Capital***, were ***investing a combined $20 million*** of additional capital into the company, more than doubling down on their initial investment.

“Low rates on savings accounts and CDs are making fixed-rate annuities the most attractive low-risk investment for investors looking for a place to park cash, so it’s no surprise to see continued growth from these products,” said Michael Finke, professor at the American College of Financial Services. “A reduced appetite for investment risk is also driving consumers’ demand for annuity products that offer structured returns such as RILAs and protection from losses offered by FIAs.”

SOCIAL SECURITY SPOTLIGHT

“Incorporating Social Security into a retirement plan is a must,” declared Michael Nakanishi, financial adviser at Kingswood US.