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Title

Keep the Gains, Lose the Losses

Indexed Annuities Offer Market-Driven Performance with a Guaranteed Return

When people make financial decisions that involve the possibility of losing money, it can affect areas of the brain associated with stress, anxiety, and even physical pain. When the part of the brain that's responsible for creating anxiety is activated, many people are less willing to take on risk, which can affect their investment decisions.[1]

If your aversion to losing money is interfering with your ability to select investments that can help you pursue your long-term financial goals, it may be time to consider a guaranteed income product such as an indexed annuity (IA).

Over 75% of workers in a financial survey said they preferred guaranteed income products to higher-risk investments that could lose money.

Source: ThinkAdvisor, January 5, 2015

THE RETURN OF INVESTMENT RETURNS

An indexed annuity is a contract between an investor and an insurance company. It provides the investor with an opportunity to earn interest based on the performance of a market index such as the S&P 500. If the index rises during a specified period, the investor typically participates in the gain. If the market falls and the index posts a loss, the contract value is not affected.

However, an indexed annuity's guaranteed minimum return comes at a price. The amount of index gain that the insurance company credits to an IA is called the *participation rate*, which can be anywhere from 50% to 90% or more. A participation rate of 80%, for example, and a 10% gain by the index for the year would result in an 8% gain by the contract holder. In exchange for a minimum rate of return, some indexed annuities have a *cap rate*, which is the maximum rate of interest the annuity will earn; this could lower the contract holder's gain.

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Several formulas are used to calculate the earnings generated by an indexed annuity. These formulas can also have an effect on the annuity's return. On preset dates, the annuity holder is credited with a percentage of the performance of the index. The percentage is typically based on one of the following formulas.

Annual reset (or ratchet) compares the change in the index from the beginning to the end of each year, "locking in" an investor's gain annually. Any declines are ignored.

High water mark compares the index value at the beginning of the contract to its highest value at various points during the contract term (often anniversaries of the purchase date). This method may allow the annuity holder to receive more interest than other indexing methods. However, because interest is not credited until the end of the term, those who surrender the annuity early may not receive any index-linked gain.

Point-to-point looks at the change in the index value at two discrete points, such as the beginning and ending date of the contract term. This method may be combined with features such as higher cap and participation rates to yield more interest. However, because this method relies on a single point in time (i.e., the last day of the contract), a drastic decline in the index prior to that point may decrease the interest credited to the contract holder.

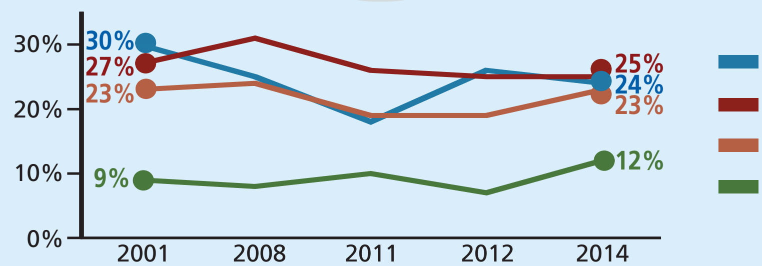
Indexed annuities are not appropriate for every investor. Participation rates are set and limited by the insurance company. Like most annuity contracts, IAs have certain rules, restrictions, and expenses. Some insurance companies reserve the right to change participation rates, cap rates, and other fees either annually or at the start of each contract term. These types of changes could affect the investment return. Based on the guarantees of the issuing company, it may be possible to lose money with this type of investment. Thus, you should understand how the contract handles these issues before you decide whether to invest.

Surrender charges may apply if the annuity is surrendered during the early years of the contract. In addition, withdrawals prior to age 59½ may be subject to a 10% federal income tax penalty. Any guaranteed minimum rate of return is contingent on holding the indexed annuity until the end of the term. Annuity guarantees are contingent on the financial strength and claims-paying ability of the issuing insurance company.

1) ThinkAdvisor, May 29, 2015

The Age of Caution?

Percentage of U.S. households willing to take substantial or above-average investment risk, by age of head of household (selected years shown)



Source: Investment Company Institute, 2013, 2015

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