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IN THIS ISSUE

Hybrid annuities in South Africa combine the security of guaranteed lifetime income with the flexibility and growth potential of market-linked investments. They're ideal for retirees who want stable income for essentials while still investing for growth and leaving a legacy.

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HYBRID ANNUITIES IN SA:

A SMARTER WAY TO SECURE RETIREMENT INCOME

MARISE REINACH, CERTIFIED FINANCIAL PLANNER®, BRENTHURST PRETORIA

Retiring comes with a big decision: How to turn your hard-earned nest egg into a sustainable income for life. Traditionally, when retiring from retirement funds, you had two main choices:

- a **life annuity** – a guaranteed pension for life; or
- a **living annuity** – an invested account from which you draw income.

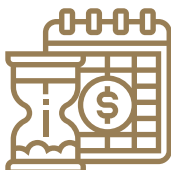
EACH HAS ITS PROS AND CONS:



A life annuity guarantees you an income until you die, but usually leaves no capital for heirs and doesn't let you withdraw lump sums after commencement.



A living annuity gives you control over how your money is invested and how much income you draw, with any remaining capital going to your beneficiaries. But it carries the risk that you could run out of money if your drawdowns are too high, or markets underperform.



Enter the hybrid annuity. This is an option that aims to offer the best of both worlds – combining features of both life and living annuities in one product.

WHAT IS A HYBRID ANNUITY?

A hybrid annuity, sometimes called a blended annuity, is essentially an arrangement that splits your retirement savings between a guaranteed lifetime income stream and a market-linked investment portion, in one single product.

WHY HYBRID? THE RETIREMENT INCOME DILEMMA

Most retirees face a difficult choice between a life annuity and a living annuity. Hybrid annuities merge the best of both. You secure a dependable income stream for life and still retain investment exposure and access to your money on the living annuity portion. It's about achieving peace of mind and portfolio resilience.

Hybrid annuities can come in a few different forms, but this article will focus on investment platform hybrid annuities – living annuity with a lifetime income portfolio. These are offered by investment platforms or LISPs (Linked Investment Service Providers) and essentially start life as living annuities with an added twist. You invest your retirement money on the platform, as per normal, but you have the option to allocate a portion of it to a special “guaranteed income” portfolio within the living annuity.

An example is Momentum's "Guaranteed Annuity Portfolio (GAP)" within their living annuity, which pays a lifelong income into your living annuity account. The rest of your money on the platform remains invested in unit trusts or other funds of your choice, the same as applies to a standard living annuity.

A key feature is flexibility. You can typically choose the percentage which must be allocated to the lifetime income portion – anywhere up to a certain limit, like 50% or even 80% – which you can adjust over time, or even transfer to another provider, if they support the same structure. Essentially, it's a single contract that combines an investment account with an income guarantee.

No matter the form, all hybrid annuities aim for the same goal: Providing a balance between “self-insuring” and being insured for longevity. Part of your retirement income is secured for life by an insurer, so that you won't outlive that portion, and part remains under your control, subject to market performance, so that you retain upside potential and flexibility and there is the option of leaving funds to beneficiaries.

MOMENTUM WEALTH'S GUARANTEED ANNUITY PORTFOLIO (GAP) IS A KEY EXAMPLE OF A HYBRID ANNUITY. HERE'S HOW IT WORKS:

- GAP is embedded within Momentum's Retirement Income Option (a living annuity).
- A portion of your investment is used to purchase a guaranteed life annuity from Momentum.
- This income is paid monthly into a money market fund in your living annuity, from where your total income is paid.
- You can choose the features of the GAP portion: single life or joint life, additional guarantee period and annual escalation, e.g., between 0% and 10% or inflation linked.
- The rest of your funds remain invested in unit trusts or other portfolios of your choice.
- For example, you might allocate 50% to GAP to cover essentials and keep 50% invested to grow capital.

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KEY BENEFITS

- **Income for life:** The GAP portion guarantees a monthly income for life, which can escalate annually to offset inflation.
- **Investment flexibility:** The living annuity portion remains invested and your annual income percentage (2.5% - 17.5%) can be changed yearly based on your GAP purchase amount plus your living annuity value.
- **Estate planning:** The living annuity portion and any remaining guaranteed period on the GAP can be transferred to beneficiaries.
- **Inflation protection:** Choose CPI-linked or fixed escalations to maintain your purchasing power.
- **Psychological comfort:** Knowing essential expenses are covered brings peace of mind, allowing greater freedom with remaining investments.

ANOTHER WAY TO THINK OF IT: A HYBRID ANNUITY LETS YOU COVER YOUR BASES AND SHOOT FOR GROWTH, SIMULTANEOUSLY.

The guaranteed income part can be thought of as the floor – it covers your basic expenses with certainty. The living annuity part is the upside – it gives you potential for growth and a chance to have extra income or leave an inheritance, if markets do well. If markets perform poorly, the living annuity portion might dwindle, but at least you still have the guaranteed income to fall back on. If markets perform well, you enjoy the gains on the invested part, over and above the secure base income.

CONSIDERATIONS

- **Irrevocable commitments:** The GAP portion cannot be withdrawn or altered once purchased.
- **Product complexity:** Hybrid annuities are more complex than traditional annuities and are best used with financial advice.
- **Fees:** Be aware of platform, advisor and fund management fees. GAP fees are embedded in the payout rate.
- **Interest rate and timing risk:** The annuity rates used to determine the guaranteed income (i.e., how much pension you get for a given lump sum) change with amendments to interest rates and as you age. The guaranteed portion's rate is locked in at time of purchase, so if you transfer additional money into the guaranteed portion at a later date, the annuity rate applied to that amount might differ from the original rate.
- **Not one-size-fits-all:** Finally, remember that a hybrid annuity, for all its appeal, may not suit everyone's situation. If your retirement savings is very small, keeping things simple might be better. (Some providers have minimum amounts for the hybrid features.) Conversely, if you have a very large fund and plenty of other guaranteed income, such as multiple pensions or rental income, you might not need a hybrid approach. Personal preference also matters – some people value certainty above all and would rather have as much guaranteed income as possible, while others hate giving up control and want to stay fully invested. A hybrid is a middle road; by definition, it involves compromise.

WHO SHOULD CONSIDER A HYBRID ANNUITY?

HYBRID ANNUITIES ARE IDEAL FOR RETIREES WHO:

- Want a secure income for life, especially for essential expenses.
- Still want growth and the flexibility of a living annuity.
- Are concerned about inflation and market volatility.
- Value leaving a financial legacy while protecting themselves.

FINAL THOUGHTS

Hybrid annuities represent an innovative way to balance security and growth in retirement income planning. For retirees who have seen volatile markets and worry about outliving their money, these products offer a reassuring middle ground. By combining a life annuity's guaranteed lifetime pension with a living annuity's investment flexibility, a hybrid annuity can provide both peace of mind and opportunity. You get a safety net of income that you cannot outlive, plus the freedom to invest part of your savings for additional growth and legacy planning.

In practice, a hybrid annuity lets you cover your essential expenses with a guaranteed income and still have a pool of invested money for discretionary spending and emergencies. It's about tailoring your retirement plan to have a bit of certainty and a bit of flexibility. As with any financial product, there are pros and cons to consider. Make sure you understand the costs, the conditions and the implications for your heirs. South Africa's market for hybrid annuities has grown, with reputable insurers and investment firms offering options to suit different needs. If used correctly, this approach can greatly improve the sustainability of your retirement income and reduce the stress of market ups and downs.

It's recommended to get independent financial advice to view projections for different annuity mixes. A qualified advisor can help determine the right balance (or whether to go hybrid at all) based on your longevity outlook, required income and desire to leave an inheritance.

MARISE REINACH, CERTIFIED FINANCIAL PLANNER®, BRENTHURST PTA

Phone: +27 (0) 12 347 8240 | Email: marise@brenthurstwealth.co.za

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EMAIL US:
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SATELLITE OFFICES:

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NORTH WEST: Maria Smit +27 79 696 6860
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