

# It's Not About Asset Allocation, It's About Creating A Guaranteed Pension For Life

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In the past, it was not uncommon for many Canadians to spend their entire working careers with one employer. This long term employment was rewarded with participation in a defined benefit pension plan that provided guaranteed income for life in retirement.

According to Statistics Canada (2008) only one in four Canadians now have access to an employer-sponsored defined benefit pension plan. The trend away from defined benefit pension plans creates a huge challenge for today's retirees.

The lack of stable and guaranteed income in retirement is increasingly difficult as Canadians are living much longer, and traditional stock and bond portfolios have provided anemic returns over the past ten years. Historically low interest rates have also virtually eliminated real returns for fixed income investors.

It should come as no surprise that millions and millions of retirement dollars are sitting in zero interest savings accounts looking for a suitable home.

According to a 2011 Manulife Investments survey, 82% of Canadians feel that having at least a portion of their retirement income guaranteed for life was important.

The solution to this retirement income conundrum may lie in creating a defined benefit pension plan for one. ***Technically speaking this is referred to as a notional contributory pension plan.***

Contributory refers to the amount of money that is invested, and notional refers to the guarantees that protect this money. The guarantees preserve the existing capital, provide a guaranteed annual increase prior to income of 5%, and also provide a guaranteed level of income in retirement of either 5% or 5.5% depending on retirement age.

Yes, income is guaranteed for life and invested capital is liquid, and not locked-in. Residual capital flows to your estate/beneficiary on death.

This strategy essentially transfers the risk to an insurance company who provide a guarantee of capital, annual guaranteed increases on this capital, and ultimately guaranteed income for life.

As investment advisors, we believe a guaranteed income strategy is a complement and enhancement to traditional asset allocation. Guaranteed income becomes the foundation of retirement income as a defined benefit pension plan once did.

This strategy is not about asset allocation, but is a decision more about creating a guaranteed base level of growth on invested capital, and creating a base level of income in retirement.

In addition to guaranteed annual increases on invested capital, market value gains are locked-in every three years above the protected amount. This strategy obviously provides upside potential, but perhaps more importantly excellent downside protection.

***Hence the term defined benefit pension plan for one!***

Recent studies suggest a shift among people nearing retirement from an emphasis on growth and beating the market to preservation of capital and protecting themselves and their families against downside risk.

This thinking resonates with Ed Clark chief executive officer of Toronto-Dominion Bank. In a recent Toronto speech, Mr. Clark expressed concerns over the world's economic problems that include Canada.

*“After decades of growth that helped fuel social programs, countries around the world now face the reality of not being able to deliver on those same promises. Once you start to live in a world of 1 or 2 percent interest rates you change retirement incomes of people pretty dramatically.”*

*“In simple terms, in too many countries in the Western world, promises have been made that cannot be kept. Promises around health care, pensions and support systems.”*

According to the Society of Actuaries, Annuity 2000 Mortality Table a healthy couple now 65 years old has a 94% chance of one partner living to age 80 and a 63% chance of one partner living to age 90.

Statistics Canada estimates that nearly half of Canada's current population will retire in the next 20 years. Considering longevity risks, unfunded social benefit programs, global sovereign debt issues...is it any wonder why Canadians are looking for some type of guaranteed income in retirement.

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