Managing Risks in the Retirement Red Zone

Common Risks to Retirement Assets & Income

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What is The Retirement Red Zone?

Prudential has defined

The Retirement Red Zone

as the critical time period when you need a strategy for turning your assets into income that can last a lifetime.

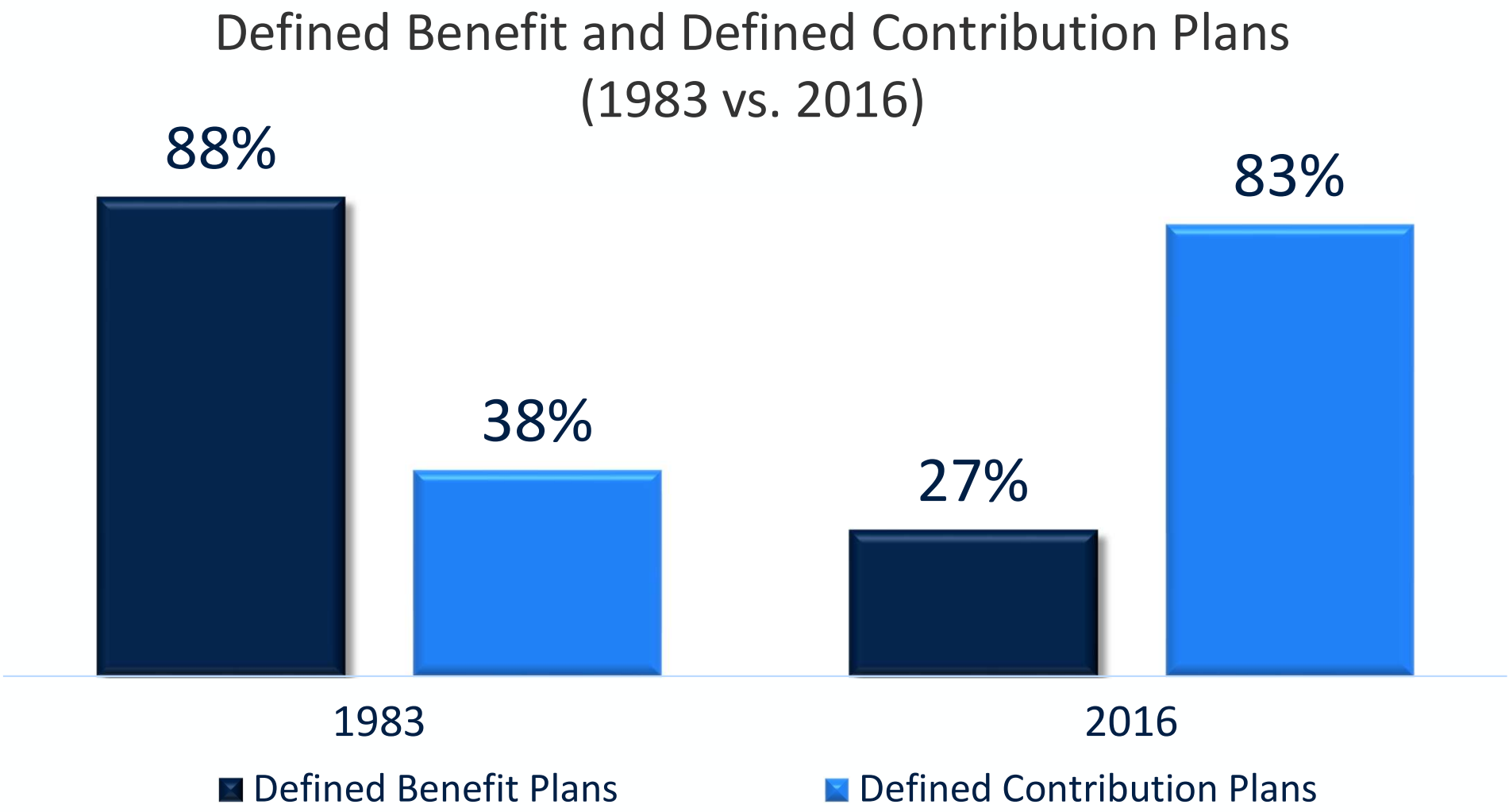
Managing Retirement Income Risks

Retirement Income Then and Now

Seven Risks to Retirement Income

Managing Risk in Retirement

Decline of the Defined Benefit Pension Plan



Source: Center for Retirement Research; "401(k)/IRA Holdings in 2016: An Update from the Survey of Consumer Finances"; Munnell and Chen; October 2017, No. 17-18
Columns include participants with access to both plan types. The Survey of Consumer Finances is a tri-annual survey. Data from the 2019 Survey has not yet been released.

The Decline of Pensions

- **According to PBGC, the average single-employer Defined Benefit Plan is only 73% funded***
- **The average State Public Pension fund is only 40% funded****
- **Under the Budget Act of 2015, PBGC premiums increased:†**
  - Funded Plans: **40%** between 2015 and 2019
  - Unfunded Liabilities: **75%** between 2015 and 2019
- **In 2018, 85% of companies asked were planning a divestment of pension obligations within the next 2 years, up from 43% one year earlier.‡**

* PBGC Annual Pension Insurance Data Tables 2018, Table S-48; rev. 6-19-20; Single employer plans only; Weighted average underfunded pensions only. If overfunded plans are included 82.9%. Multi-employer plans Table M-13, 44.2%
** American Legislative Exchange Council; "*Unaccountable and Unaffordable 2019: Unfunded Public Pension Liabilities Total Nearly $5 Trillion*"; June 5, 2020. Average is an unweighted average.
† The Bipartisan Budget Act of 2015, Section 501;
‡ Ernst and Young; "*How Can Divesting Fuel Your Future Growth? Global Corporate Divestment Study 2018;*

Health of the Social Security System

$981 Billion
Added to Trust Fund in 2021‡

$2.8 Trillion
Trust Fund†

$993 Billion
in Benefits Paid in 2021‡

* The 2021 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Trust Funds; Table IV.B3
† Trust fund balance at year end 2021
‡ Figures do not include DI trust fund; Funds added include OASI payroll tax revenue ($873 Billion), income taxes collected on benefits paid ($38 Billion) and interest on trust fund assets ($70 Billion).

Future of Social Security

"Social Security benefits are **not intended to be your only source of income when you retire**. On average, Social Security will replace about 40 percent of your annual pre-retirement earnings. You will need other savings, investments, pensions, or retirement accounts to live comfortably when you retire."

Your payment would be about
$1,986 a month
at full retirement age

WANDA WORKER
456 ANYWHERE AVENUE
MAINTOWN, USA 11111-1111

May 1, 2020

Your Social Security Statement

Your Estimated Benefits

***Retirement**	You have earned enough credits to qualify for benefits. At your current earnings rate, if you continue working until…
	your full retirement age (67 years), your payment would be about ..... $ 1,986 a month
	age 70, your payment would be about ..... $ 2,468 a month
	age 62, your payment would be about ..... $ 1,376 a month
***Disability**	You have earned enough credits to qualify for benefits. If you became disabled right now, your payment would be about ..... $ 1,956 a month
***Family**	If you get retirement or disability benefits, your spouse and children also may qualify for benefits.
***Survivors**	You have earned enough credits for your family to receive survivors benefits. If you die this year, certain members of your family may qualify for the following benefits:
	Your child ..... $ 1,467 a month
	Your spouse who is caring for your child ..... $ 1,467 a month
	Your spouse, if benefits start at full retirement age ..... $ 1,956 a month
	Total family benefits cannot be more than ..... $ 3,568 a month
	Your spouse or minor child may be eligible for a special one-time death benefit of $255.
Medicare	You have enough credits to qualify for Medicare at age 65. Even if you do not retire at age 65, be sure to contact Social Security three months before your 65th birthday to enroll in Medicare.

* **Your estimated benefits are based on current law. Congress has made changes to the law in the past and can do so at any time. The law governing benefit amounts may change because, by 2035, the payroll taxes collected will be enough to pay only about 79 percent of scheduled benefits.**

We based your benefit estimates on these facts:

Your date of birth (please verify your name on page 1 and this date of birth)	April 5, 1960
Your estimated taxable earnings per year after 2018	$50,653
Your Social Security number (only the last four digits are shown to help prevent identity theft)	XXX-XX-1234

Source: Form SSA-7005-SSM-SI.

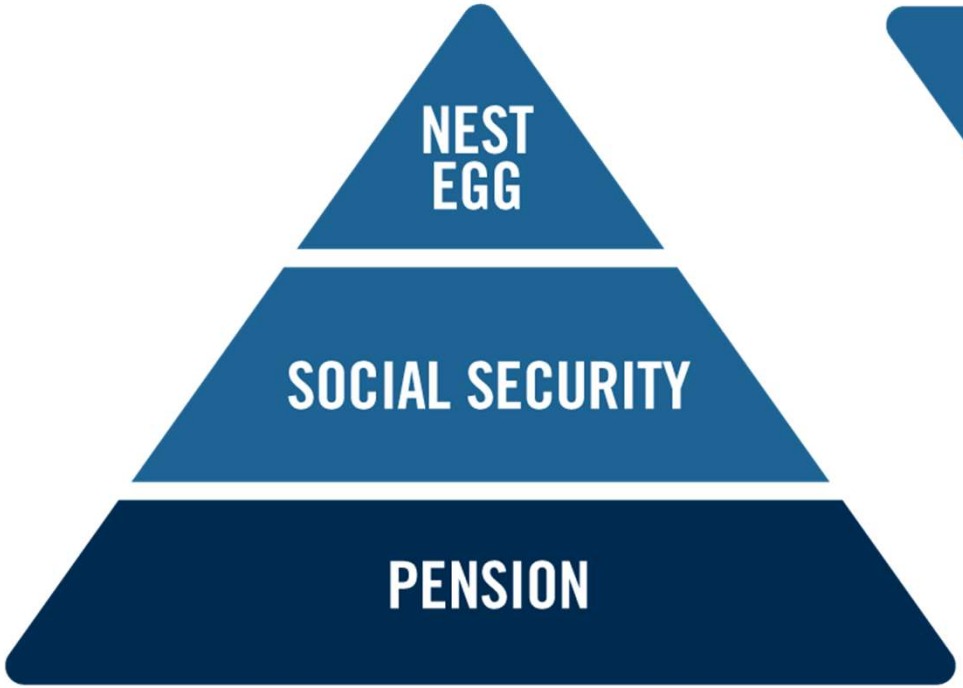
Proposed Changes

- Higher Payroll Tax
- Higher Taxable Wage Base
- Higher Retirement Age
- Means Testing
- Recalculating COLA
- Raise Earliest Eligibility Age
- Base Benefits on Highest 40 years of Earnings

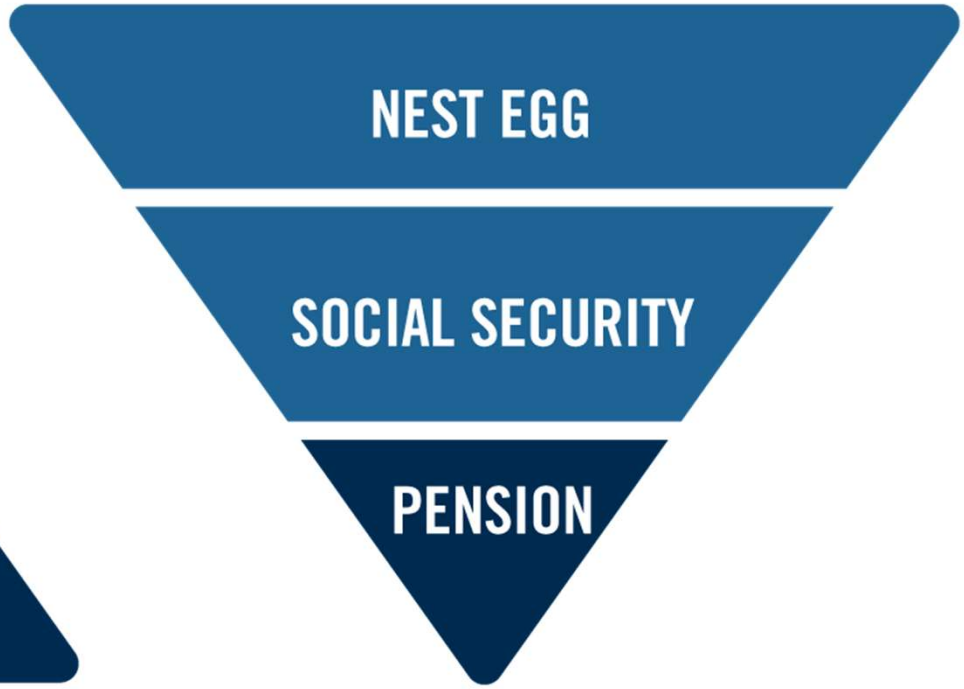
The law governing benefits **may change** because, by 2035, the payroll taxes collected will be enough to pay only **about 80 percent** of scheduled benefits.

Retirement Income Then and Now

Then



Now



Your Retirement is Your Responsibility

Common Risks to Retirement Assets

1. Market Risk
2. Sequence of Returns Risk
3. Interest Rate Risk
4. Investor Behavior Risk
5. Inflation Risk
6. Longevity Risk
7. Withdrawal Rate Risk

1. Market Risks

1

What is a market correction?

– 10% loss from the most recent market peak
– 26 markets corrections since 1945
– 42% of corrections became bear markets*

2

What is a bear market?

– 20% loss from the most recent market peak*
– 11 bear markets since 1945*

3

What is the average bear market loss since 1945?

– 35%*

4

How many bear markets will a retiree face on average?

– 4 bear markets**

5

How long does the average bear market last?

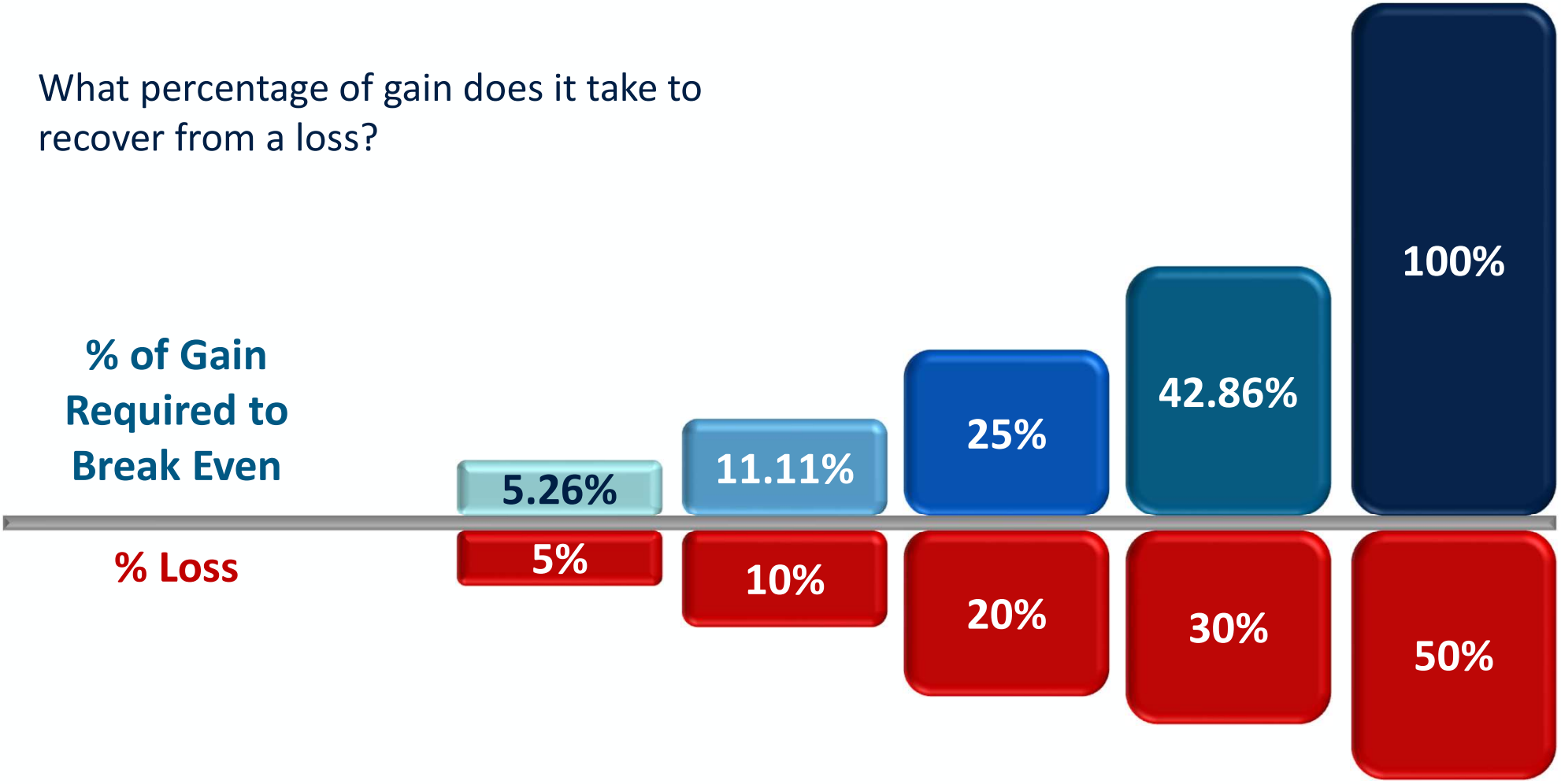
– 17 months*

* JP Morgan "Guide to the Markets®, 4Q 2020; based on market activity post-WWII
** Assumes retiree age 65 with anticipated death at age 90, and an average 6.8 years between market peaks in the post-WWII era.

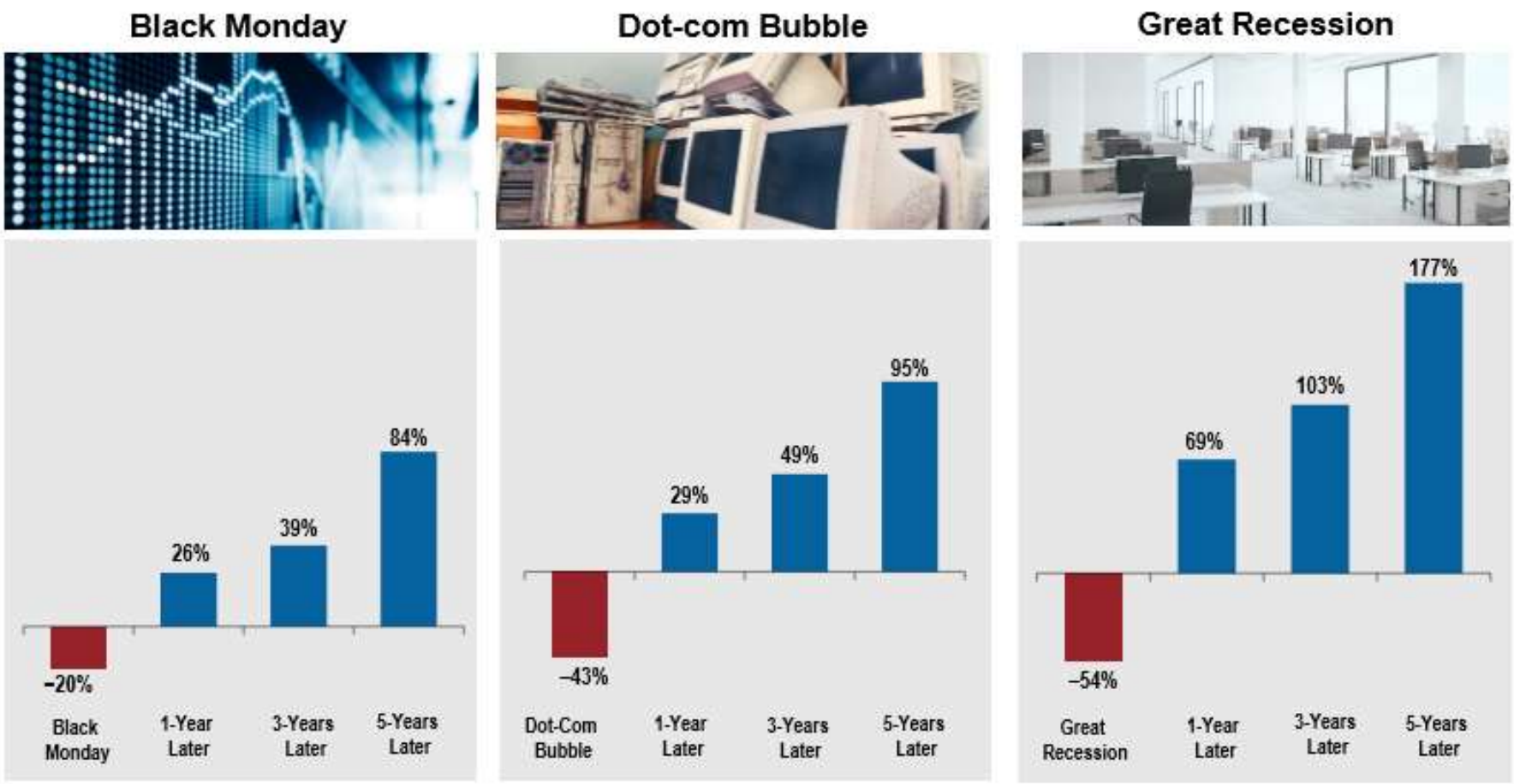
Market Risk

Mathematics of loss in accumulation

What percentage of gain does it take to recover from a loss?



Stay the Course

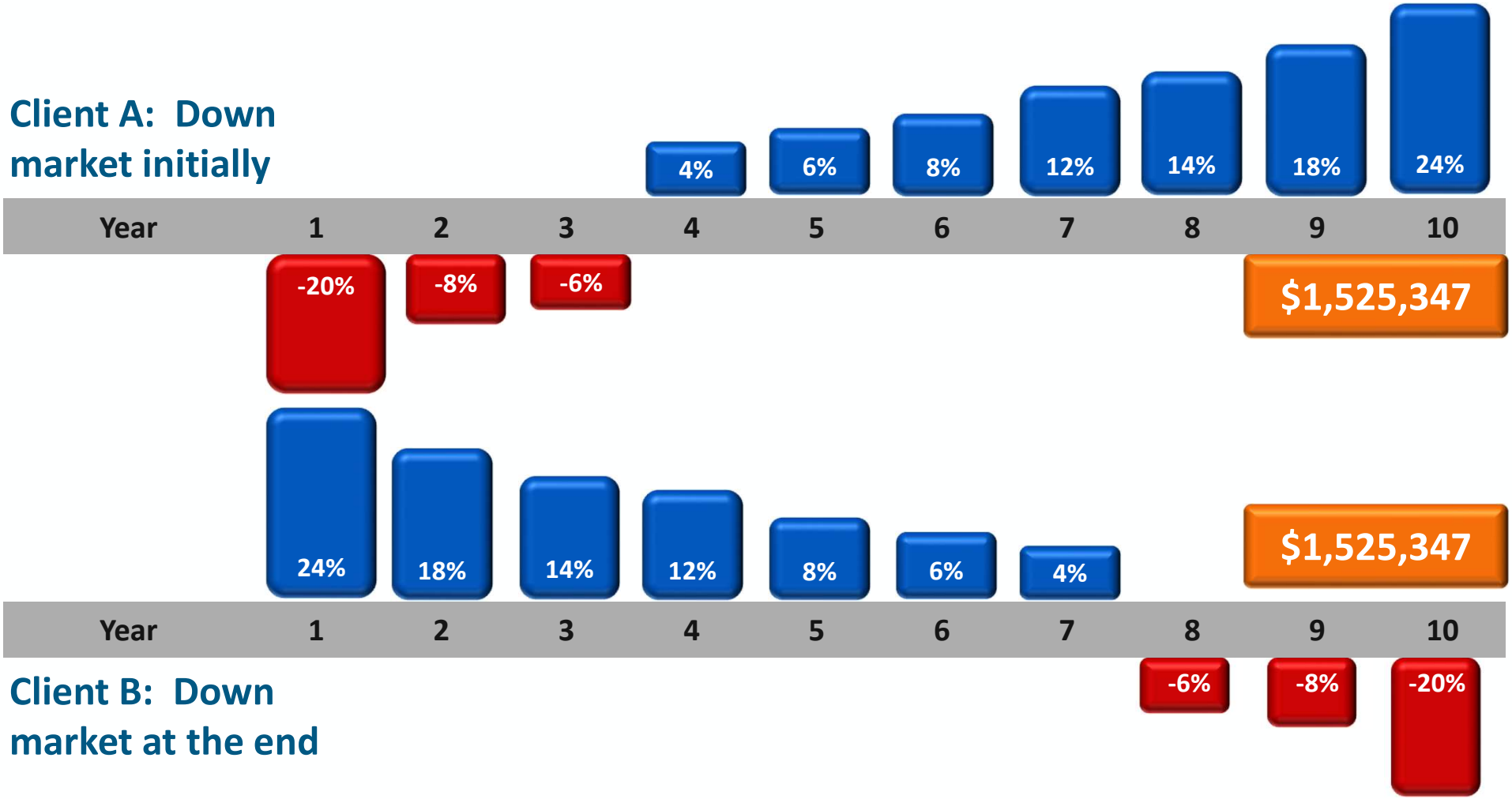


Stock market returns have historically rebounded substantially in the following year after a market decline.

Source: As of 12/31/2019. Calculated by PGIM Investments using data presented in Morningstar software products. All rights reserved. Used with permission. Based on cumulative price returns for the S&P 500. Past performance is no guarantee of future results.

2. Sequence Of Returns Risk

Accumulation

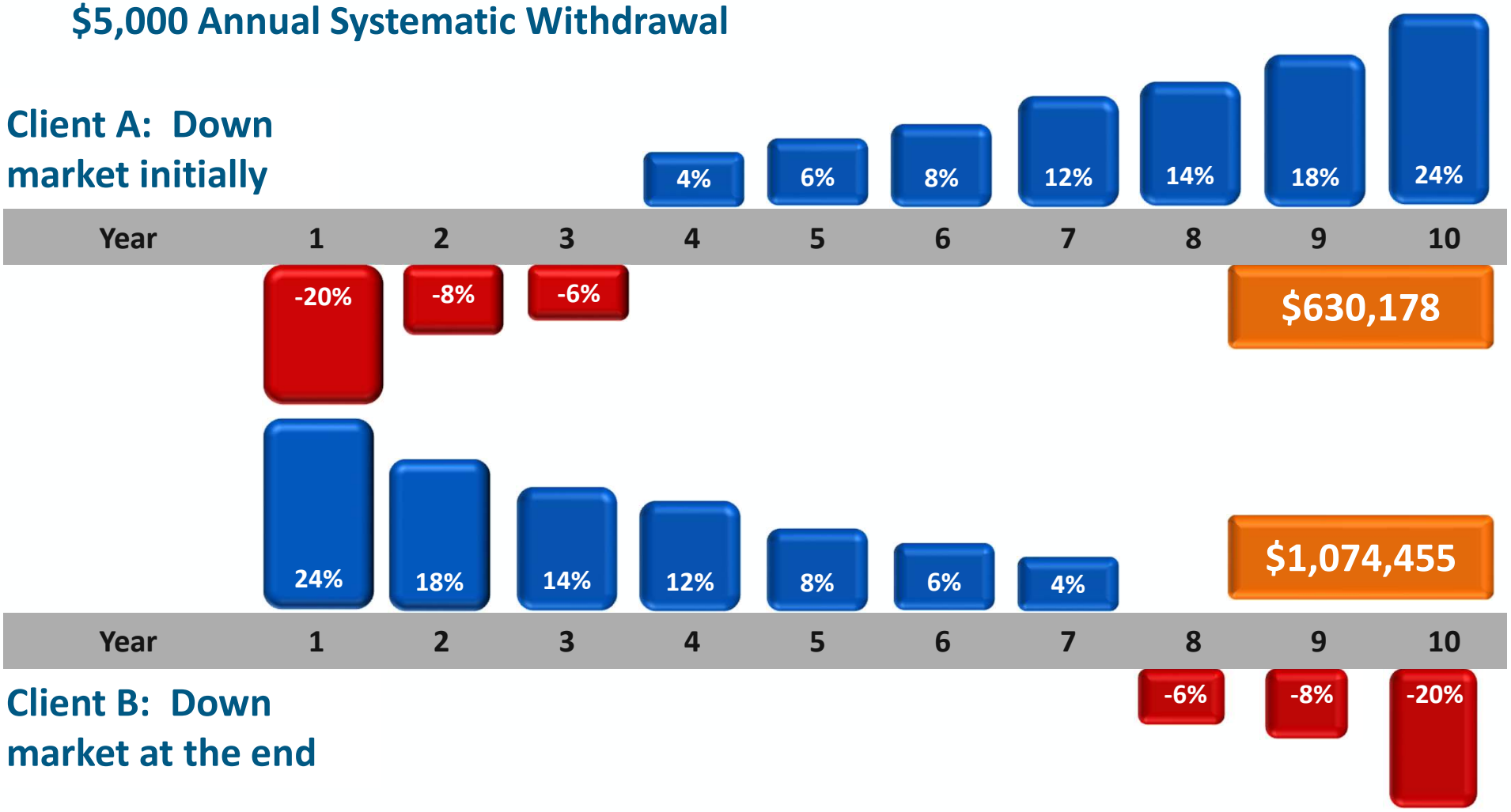


For Illustration Purposes Only: $1,000,000 investment, and a 5.2% average rate of return

Sequence Of Returns Risk

Distribution

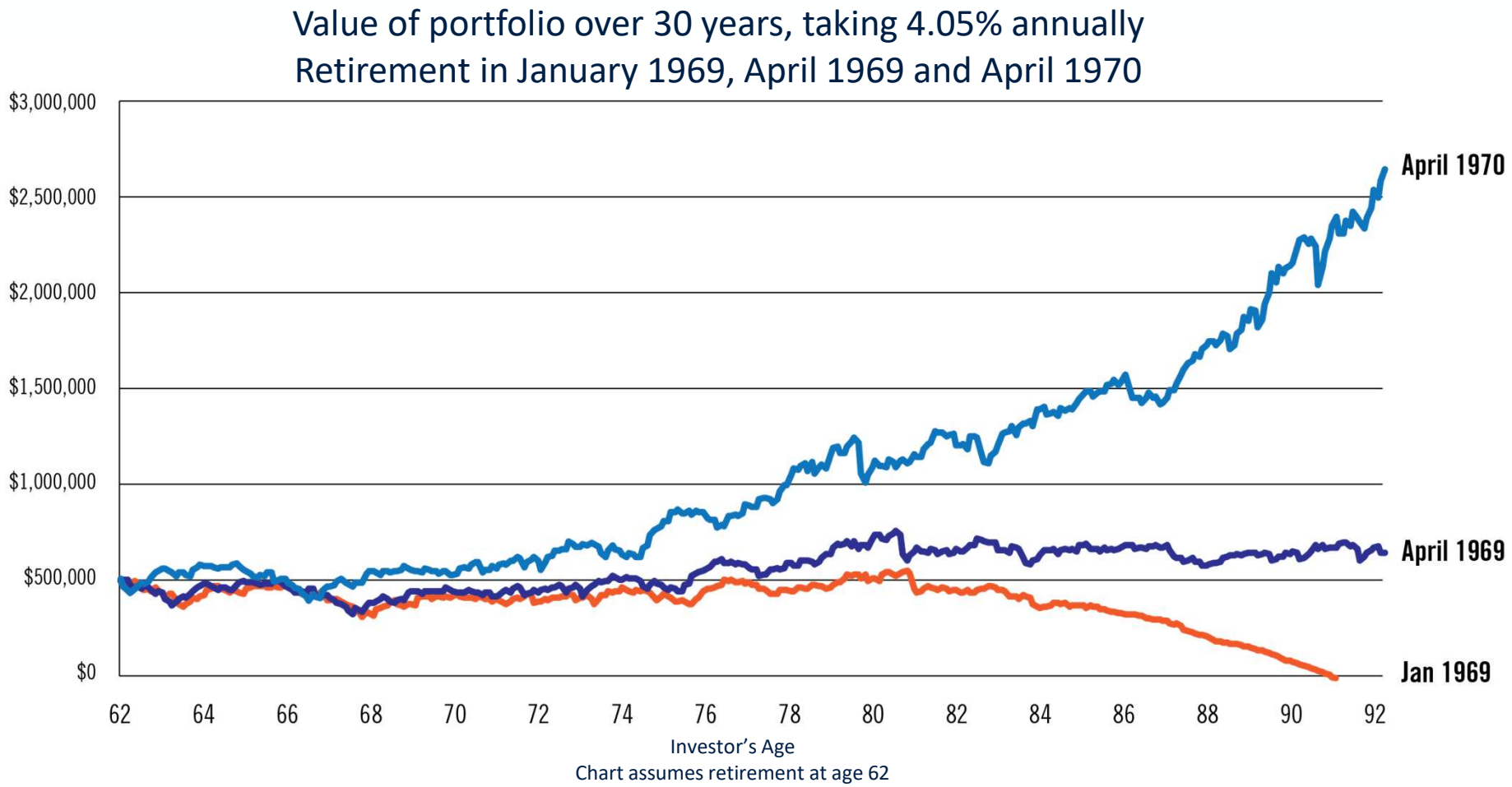
$5,000 Annual Systematic Withdrawal



For Illustration Purposes Only: $1,000,000 initial investment 5.2% average rate of return, $5,000 annual systematic withdrawal.

Sequence of Returns Risk

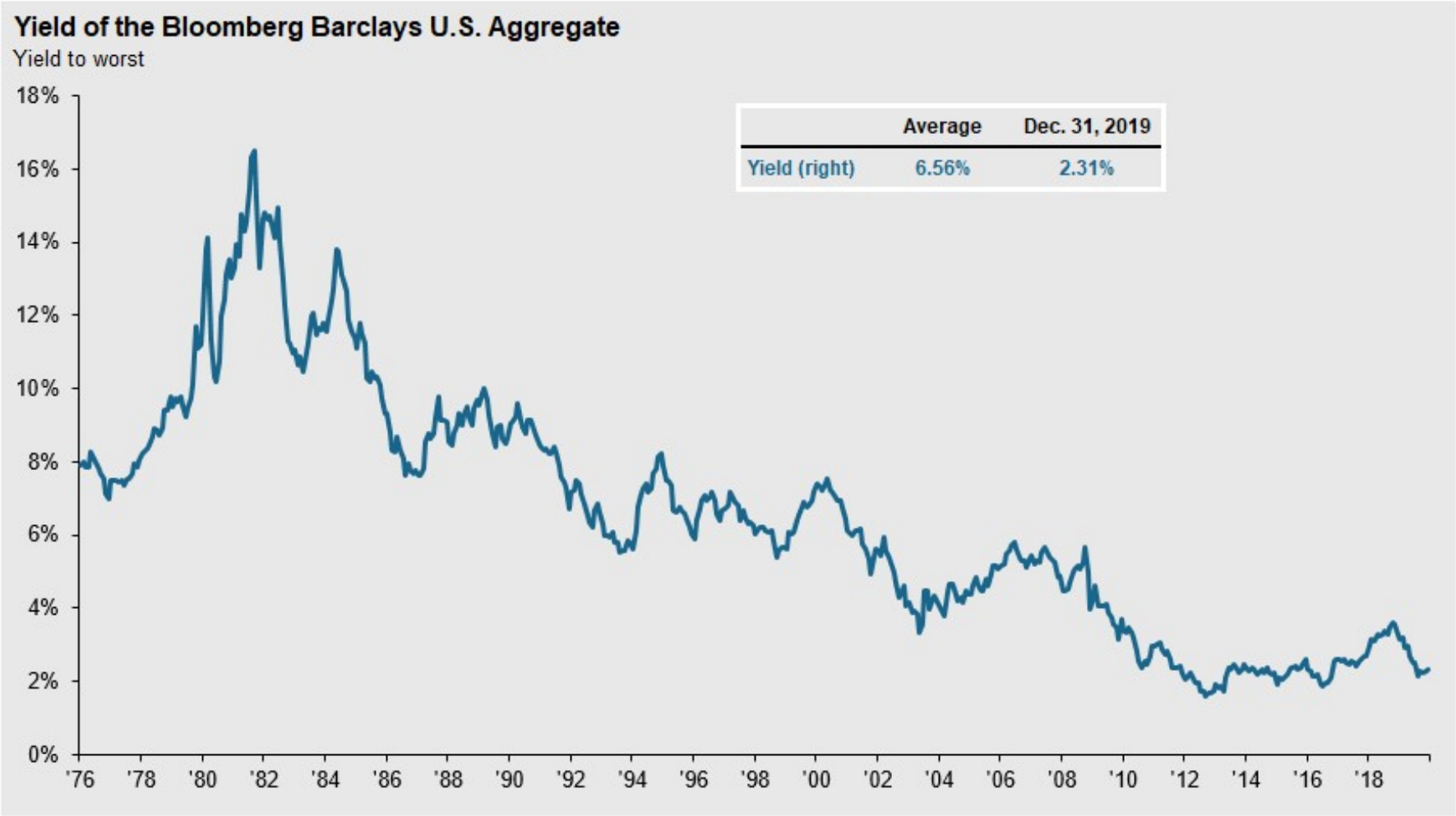
Timing is important



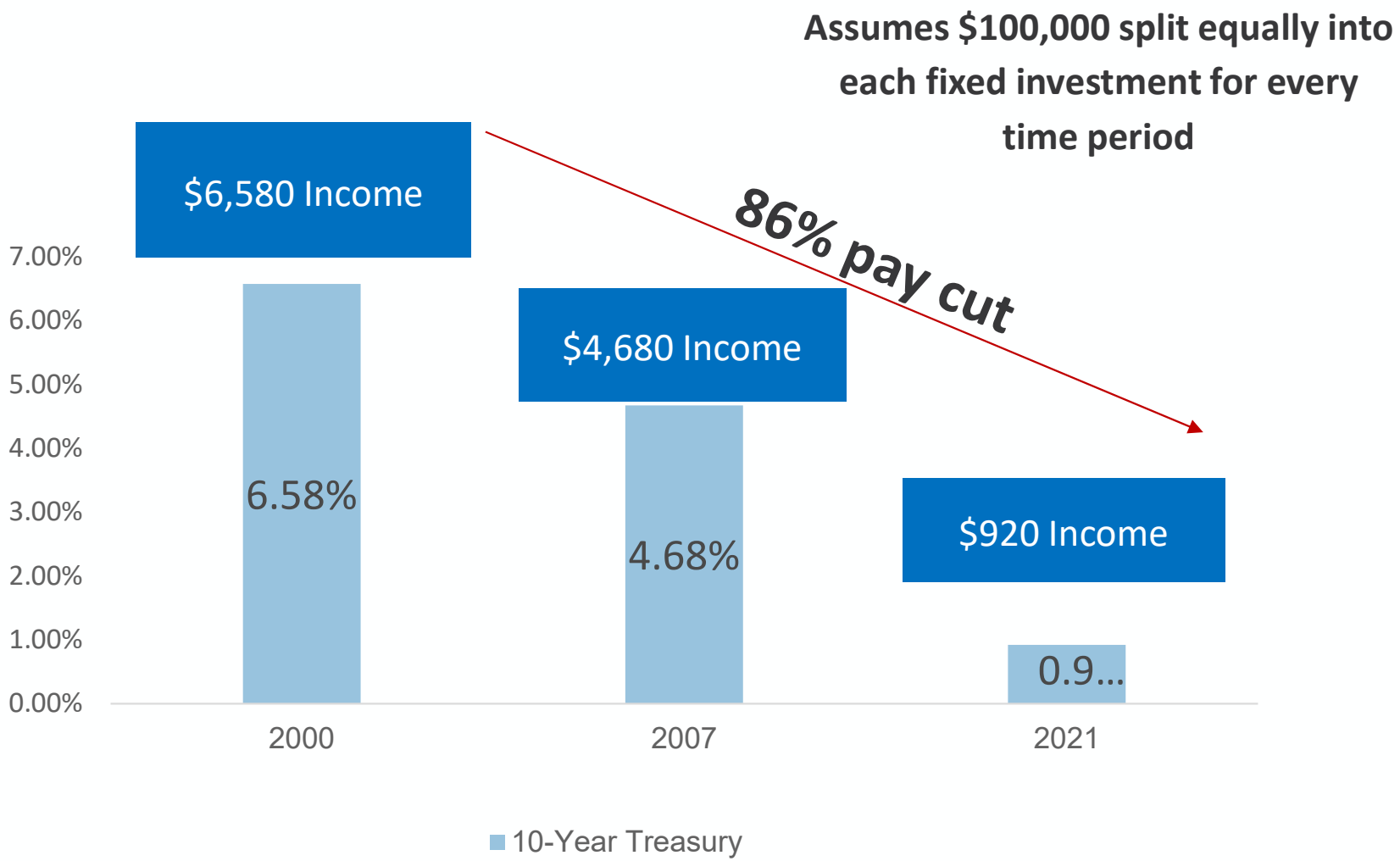
LIMRA Retirement Income Reference Book; LIMRA Secure Retirement Institute, October 2018; chart assumes $500,000 initial investment, 4.05% withdrawal adjusted annually for inflation; 42.5% Large Cap, 17.5% Small Cap, 40% Intermediate Government Bond, rebalanced annually

3. Interest Rate Risk

Over the last 35 years yields have continued to decrease

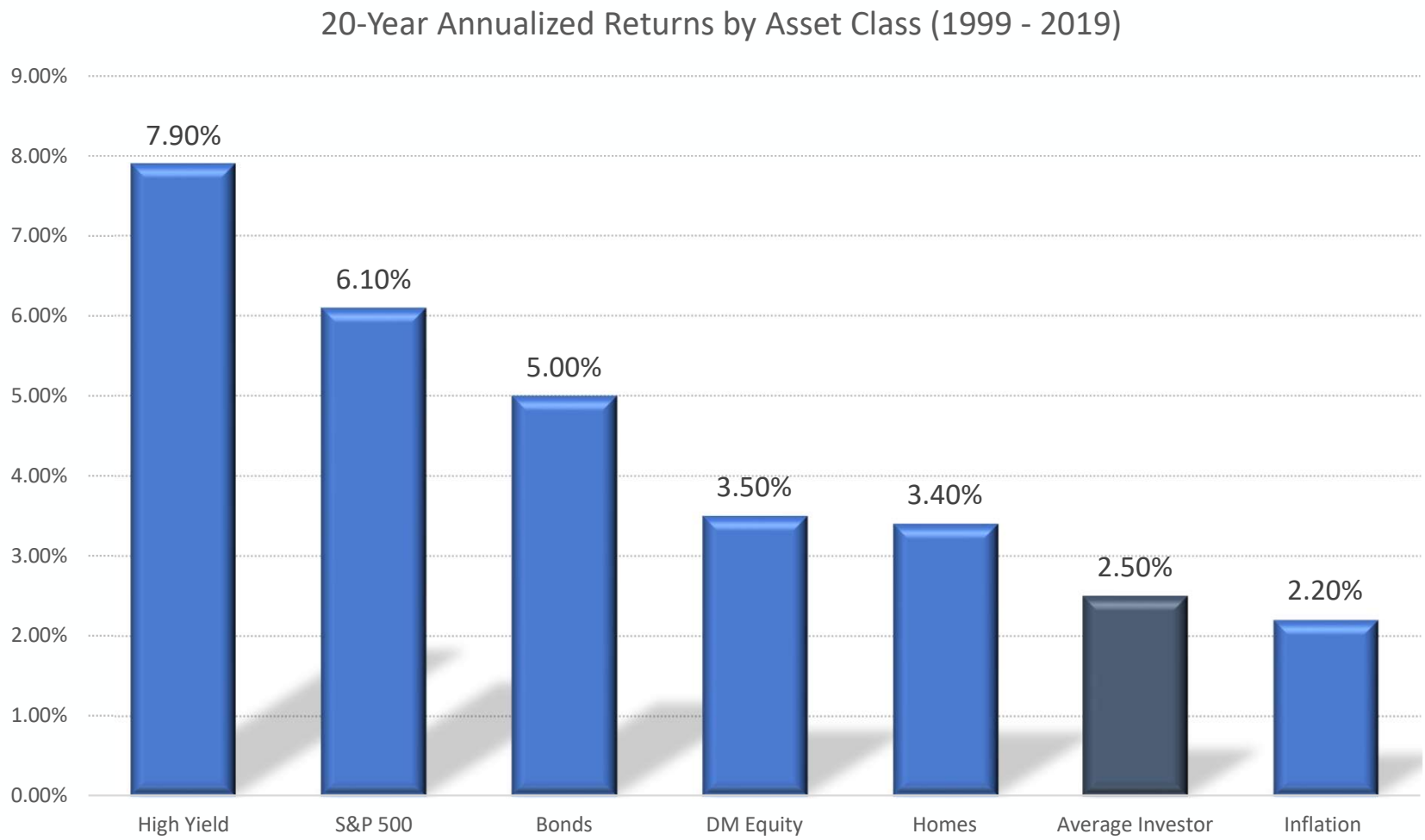


Low Interest Rates Impact in Retirement Income



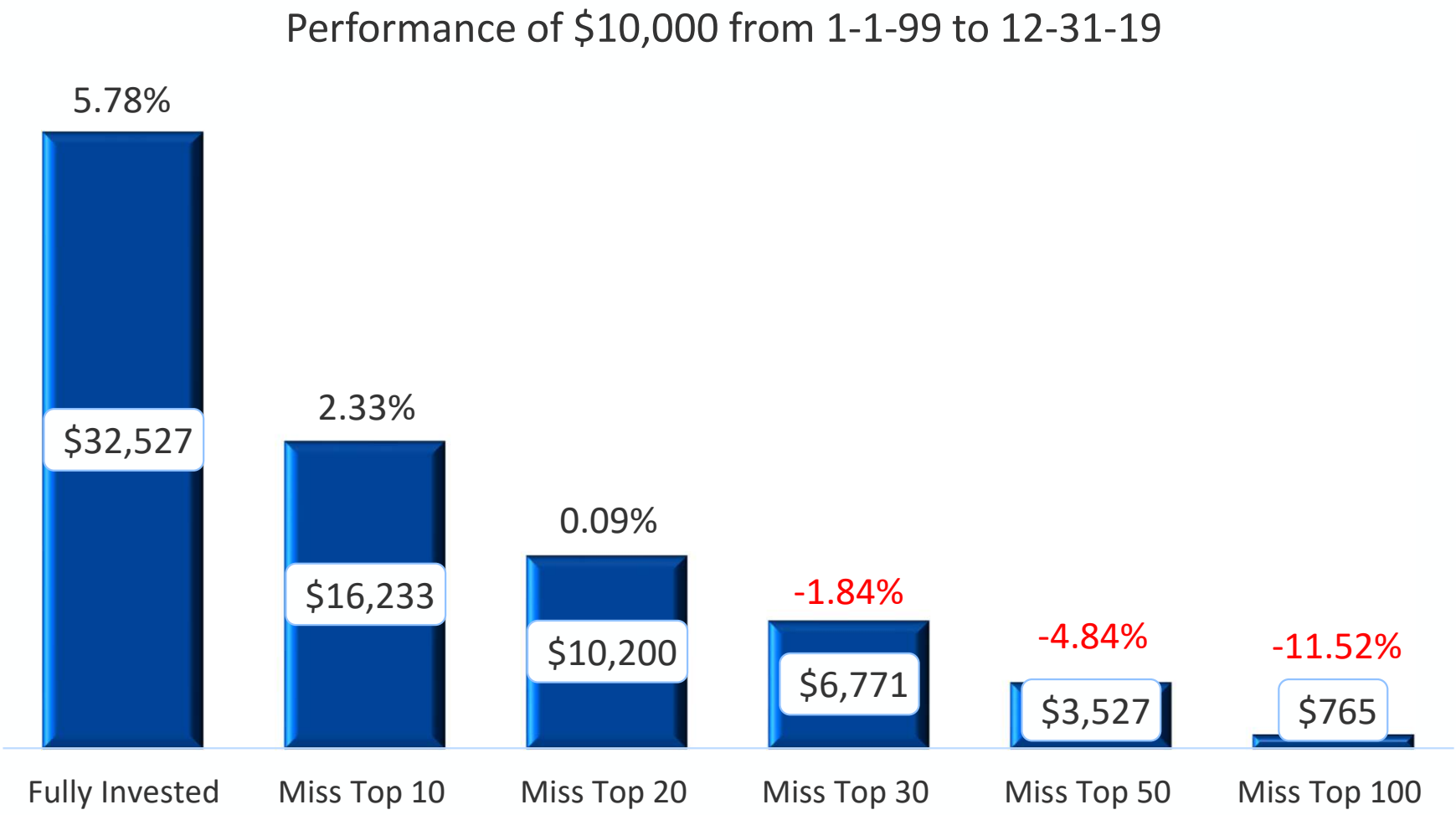
Source: U.S. Federal Reserve. All rates are market yield on US Treasury securities at 10-year constant maturity as of first trading day of the year

4. Investor Behavior Risk



Source: Barclays, Bloomberg, FactSet, Standard & Poor's, J.P. Morgan Asset Management; (Bottom) Dalbar Inc, MSCI, NAREIT, Russell.
Indices used are as follows: DM Equity: MSCI EAFE, Commodity: Bloomberg Commodity Index, High Yield: Bloomberg Barclays Global HY Index, Bonds: Bloomberg Barclays U.S. Aggregate Index, Homes: median sale price of existing single-family homes, Inflation: CPI. Average asset allocation investor return is based on an analysis by Dalbar Inc., which utilizes the net of aggregate mutual fund sales, redemptions and exchanges each month as a measure of investor behavior. Returns are annualized (and total return where applicable) and represent the 20-year period ending 12/31/19 to match Dalbar's most recent analysis. Guide to the Markets – U.S. Data are as of September 30, 2020.

Impact of Being Out of the Market

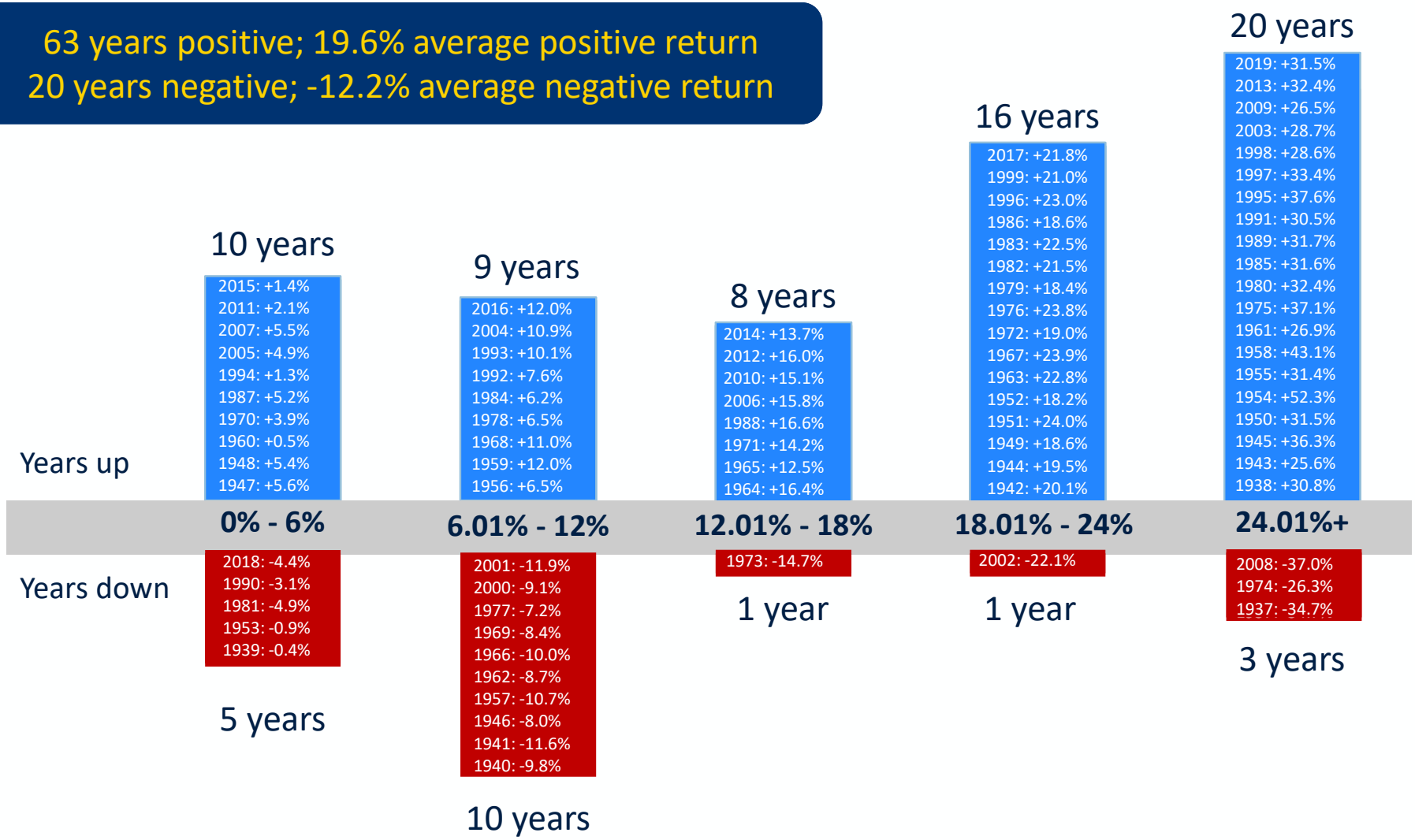


Yields are annualized over the 21-year period. Dollar values are final value of $10,000 at period end.
Source: Legg Mason. **Past performance is no guarantee of future results.** All investments involve risks, including loss of principal. The chart provided is for illustrative purposes only and represents an unmanaged index in which investors cannot directly invest. The data in the chart are based on 260 trading days in a year.

Rewards of Long-Term Investing

Positive versus negative average annual returns for the S&P 500 (1937-2019)

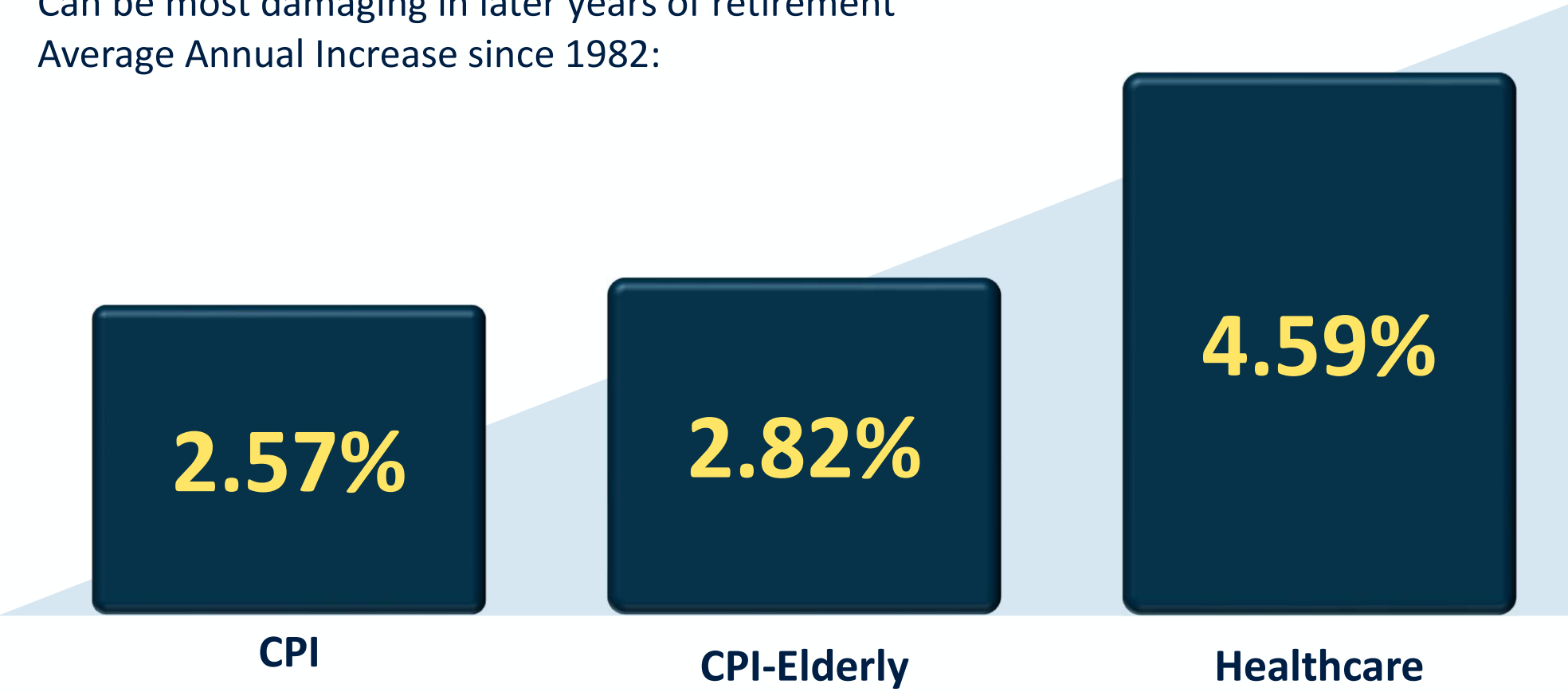
63 years positive; 19.6% average positive return
20 years negative; -12.2% average negative return



Source: Legg Mason. Each calendar year listed in chart reflects average annual performance from December 31 of prior year to December 31 of listed year.

5. Inflation Risks

Creates an increased income demand for the remainder of a retiree's life.
Can be most damaging in later years of retirement
Average Annual Increase since 1982:



1. Source: US BLS; based on CPI-W from 12/1982 through 12/2019; http://data.bls.gov/timeseries/CWUR0000SA0?output_view=pct_1mth
2. Source: US BLS; CPI-E is an experimental index, public and unpublished data; 12/1982 through 12/2019
3. Source: US BLS; based on Medical Care index from 12/1982 through 12/2019: http://data.bls.gov/timeseries/CUUR0000SAM?output_view=pct_1mth

6. Longevity Risks

Expected life span of individuals and couples age 65*

50% are expected to live to age:

MEN	88
WOMEN	90
COUPLES (Surviving spouse)	93

25% are expected to live to age:

MEN	93
WOMEN	95
COUPLES (surviving spouse)	98

51% chance one spouse will outlive the other by 10 years†

*Source: U.S. 2012 IAM Period Table, Society of Actuaries
† LIMRA Retirement Income Reference Book; LIMRA Secure Retirement Institute; October 2018

7. Withdrawal Rate Risk

[Not for use with Edward Jones]

What is a Safe and Sustainable Withdrawal Rate?

The rate one can safely withdraw from their retirement portfolio without prematurely depleting the account

Opinions on Safe Withdrawal Rates have varied over time

Bengen (1994)[1]:	**4%**
Guyton (2004)[2]:	**3.6% - 5.8%**
Milevsky & Huang (2010)[3]:	**3%**
Pfau (2020)[4]:	**2.1%**

1. "Determining Withdrawal Rates Using Historical Data", William Bengen, Journal of Financial Planning, October 1994
2. "Decision Rules and Portfolio Management for Retirees: Is the 'Safe' Initial Withdrawal Rate Too Safe?", Jonathan Guyton; FPA Journal; October 2004
3. "Spending Retirement on Planet Vulcan: The Impact of Longevity Risk Aversion on Optimal Withdrawal Rates"; M.A. Milevsky & H. Huang; Retirement Income Journal, March 2010
4. "Retirement Income Dashboard For a Benchmark Couple Both Turning 65 in July 2020"; Conservative portfolio (25% stock allocation) with 2% spending COLA; Wade Pfau at https://retirementresearcher.com/dashboard/

30 Year Retirement

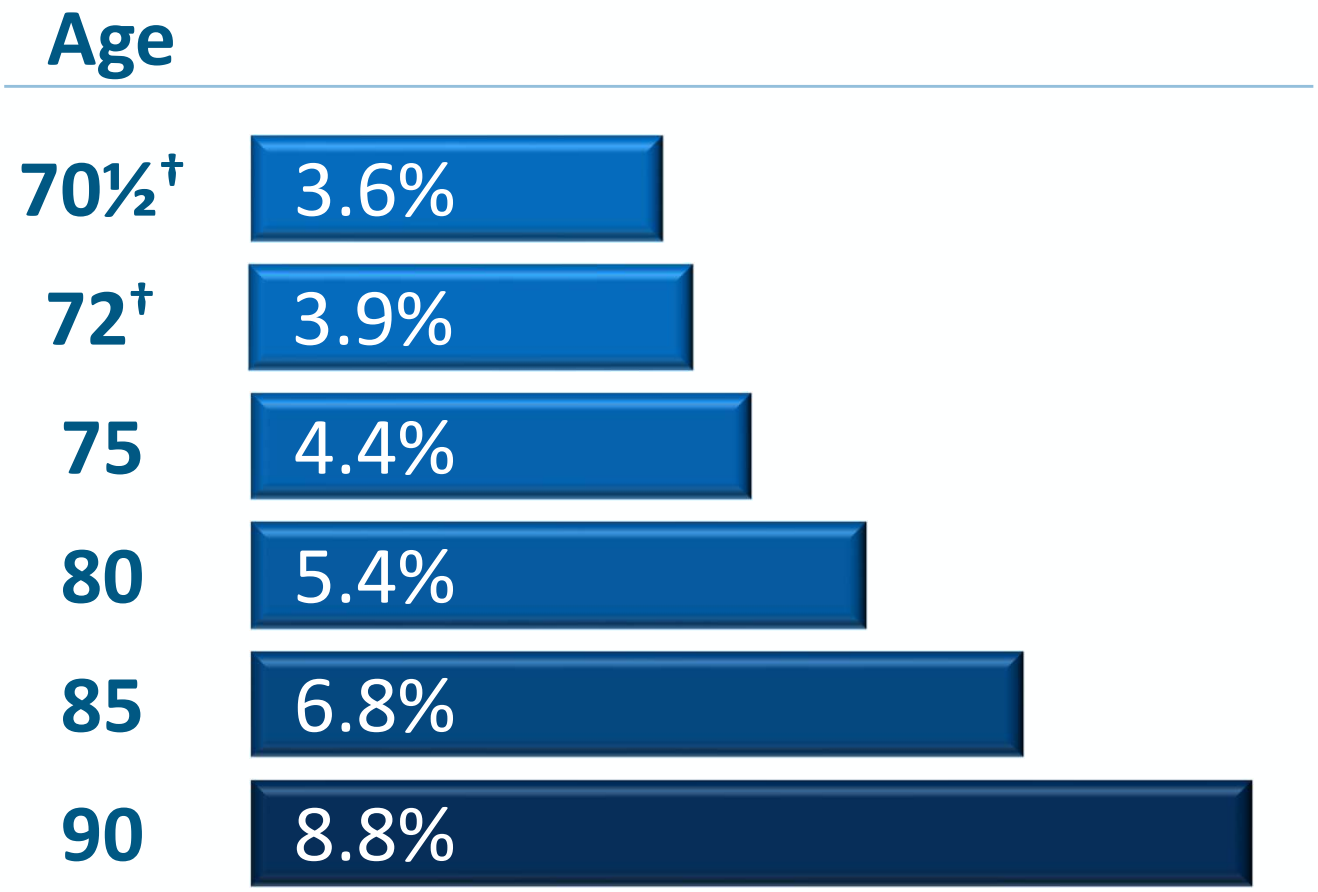
Likelihood of Success

Withdrawal Rate[1]	Stock/Bond Mix				
	100/0	80/20	60/40	40/60	20/80
3%	97%	98%	99%	99%	99%
4%	85%	87%	90%	89%	85%
5%	69%	69%	66%	57%	43%
6%	52%	49%	41%	26%	10%
7%	38%	30%	21%	7%	1%
8%	25%	17%	7%	1%	0%

1. Assumes withdrawal is increased 3% annually for inflation.
Source: T. Rowe Price 2020. Analysis of 30 year period. IMPORTANT: The information regarding the likelihood of various investment outcomes is hypothetical in nature, does not reflect actual investment results, and is not a guarantee of future results. The simulations are based on a number of assumptions. There can be no assurance that the results shown will be achieved or sustained. The charts present only a range of possible outcomes. Results may vary, and such results may be better or worse than the simulated scenarios. Clients should be aware that the potential for loss (or gain) may be greater than demonstrated in the simulations.
*Calculations only considered stock/bond mixes; short-term bonds were not included.
The probabilities shown are the likelihood of having at least $1 remaining in the portfolio at the end of the retirement period.

RMDs and Sustainable Withdrawals

RMDs Increase Each Year*



*If the spouse is the sole beneficiary and is more than 10 years younger, the RMD distribution rate is lower.at each age

† IRA owners who attained age 70½ prior to 1/1/2020 have a Required Beginning Date of age 70½. IRA owners who attained age 70½ after 12/31/2019 have a Required Beginning Date of age 72

Managing Retirement Risks

Managing Risks

A	Avoid
R	Retain
T	Transfer

Transferring Risk Can Help

- Manage the impact of volatility on retirement savings
- Provide opportunities for growth of retirement assets while hedging downside risk
- Increase the probability of a successful retirement
- Minimize the stress that comes from volatility and market corrections

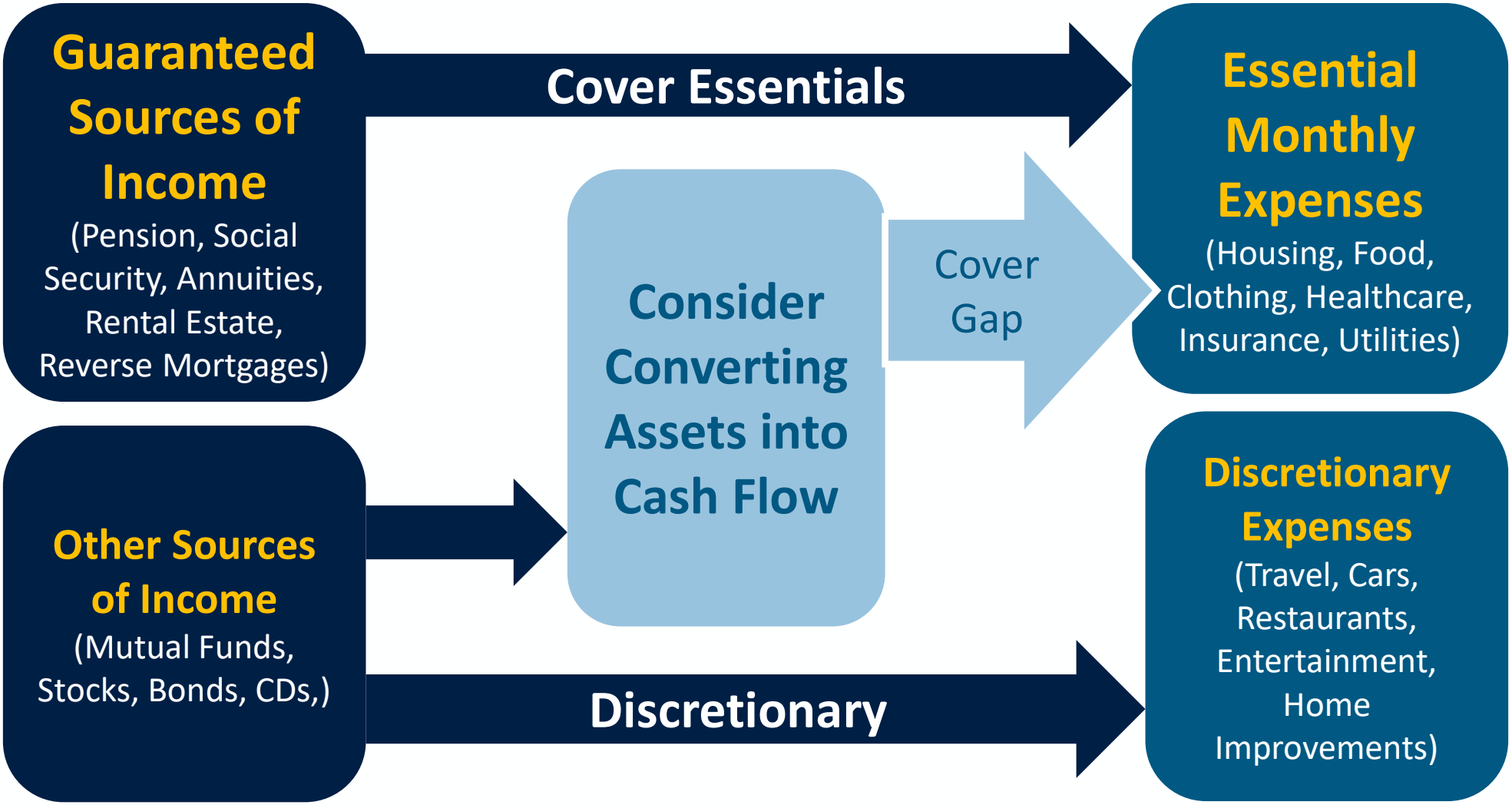
Bucketing Strategy

Protected Strategy Can Help Manage:

- Market Risk
- Sequence of Return Risk
- Investor Behavior Risk

…and can be leveraged to protect a portion of a client's portfolio.

Retirement Income Planning Example



Covering Essential Costs

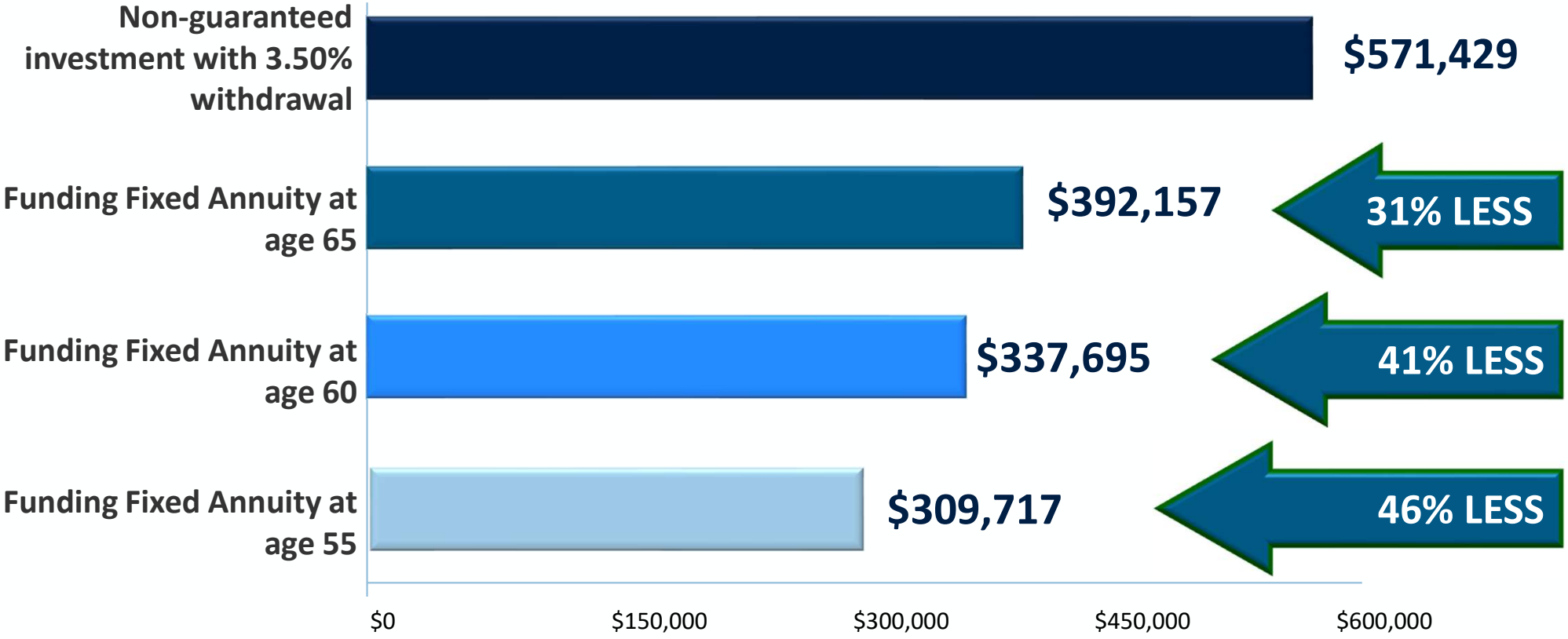
Essential Expenses	$57,000
• Housing/Food/Clothing/Transportation	$46,000
• Healthcare	$11,000

Guaranteed Income Sources	$37,000
• Pension	$15,000
• Social Security	$22,000

Income Gap to Cover Essential Expenses	**($20,000)**

Converting Assets to Cash Flow

Investment needed to generate $20,000/year at age 65



These hypothetical examples assume income percentages of 5.1% at age 65, 4.6% at age 60, 4.1% at age 55, and an income growth rate of 5.75%, and all are for illustrative purposes only. They do not reflect a specific annuity, an actual account value or the performance of any investment, please refer to the following slide for additional information.

Creating Lifetime Income

$1,000,000 to invest for retirement at Age 67

$1,000,000	X	4.0%	=	$40,000
Invested in equity and bond investments		Annual withdrawal rate		Annual income, not guaranteed, affected by market swings

How does adding a **guaranteed** income option change the picture?

This is a hypothetical example for illustrative purposes only.

Reducing Withdrawal Rates from Non-Guaranteed Investments

RETIREMENT PORTFOLIO OF $1,000,000

A two-part investment strategy

PART ONE

$500,000

Fixed Annuity

$26,000

Guaranteed income for life

PART TWO

$500,000

Other Investments

$14,000

2.80% withdrawal rate

Over 99% probability of success*

These hypothetical examples assume income percentages of 5.2% at age 67 and withdrawal rate of 2.80% and are for illustrative purposes only. A fixed annuity is suitable for long-term investing, particularly when saving for retirement; however it is possible to lose money investing in securities.

* Based on T. Rowe Price study cited on slide [42], assuming a 3% annual withdrawal and an allocation of 60% stocks and 40% bonds. Success defined as having at least $1 remaining in the portfolio at the end of the retirement period. Assumes withdrawal is increased 3% annually for inflation.

Summary

- Be careful of retirement income strategies that rely on basic time value of money assumptions
- Develop an income strategy based on your income needs, assets, risk tolerance and personality
- Ensure your planning addresses the seven risks to retirement income
- Consider covering fixed expenses with guaranteed income
- When possible, consider transferring risks you don’t want to ignore or retain

Disclosures

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Bloomberg Barclays U.S. Aggregate Bond Index covers the USD-denominated, investment grade, fixed rate, taxable bond market of SEC-registered securities. The index includes bonds from the Treasury, Government-Related, Corporate, Mortgage-Backed Security (MBS), Asset-Backed Security (ABS) and Commercial Mortgage-Backed Security (CMBS) sectors.

MSCI EAFE (Europe, Australasia, Far East) is a widely accepted benchmark for international stock performance. It is a free float-adjusted market capitalization index that is designed to measure the equity market performance of 21 developed markets, excluding the U.S. and Canada.

S&P 500® Index is a market capitalization-weighted index of the 500 widely held stocks often used as a proxy for the stock market. S&P chooses the member companies for the 500 based on market size, liquidity and industry group representation.

Withdrawals and distributions of taxable annuities are subject to ordinary income tax and, if made prior to age 59½, may be subject to an additional 10% federal income tax penalty, sometimes referred to as an additional income tax. Withdrawals reduce the Account Value. Withdrawals taken during the surrender charge period, excluding any Required Minimum Distributions (RMDs) may be subject to any applicable surrender charges and a Market Value Adjustment (MVA).

Withdrawals in excess of the income amount impact the value of a product or benefit and can also affect the certainty of the income. An excess withdrawal occurs when cumulative Lifetime Withdrawals exceed the income amount in an annuity year. If an excess withdrawal is taken, only the portion of the Lifetime Withdrawal that exceeds the remaining income amount for that year will proportionally and permanently reduce future guaranteed amounts. If an excess withdrawal reduces the account value to zero, no further amount would be payable and the contract terminates.

Fixed income investments are subject to risk, including credit and interest rate risk. Because of these risks, a subaccount's share value may fluctuate. If interest rates rise, bond prices usually decline. If interest rates decline, bond prices usually increase.

Disclosures

Diversification does not ensure against loss in a declining market.

The value or price of a particular stock or other equity or equity-related security owned by a portfolio could go down and you could lose money.

Fixed indexed annuities are not FDIC-insured; they also have limitations and surrender charges.

It is not possible to invest directly in an index.

Equity Securities Risk – The value of a particular stock or equity-related security held by a Portfolio could fluctuate, perhaps greatly, in response to a number of factors, such as changes in the issuer's financial condition or the value of the equity markets or a sector of those markets. Such events may result in losses to the Portfolio.

Investments in real estate investment trusts (REITs) and real estate-linked derivative instruments are subject to risks similar to those associated with direct ownership of real estate. Poor performance by the manager of the REIT and adverse changes to or inability to qualify with favorable tax laws will adversely affect the Portfolio. In addition, some REITs have limited diversification because they invest in a limited number of properties, a narrow geographic area, or a single type of property.

Investment in fixed income securities involves a variety of risks, including that: an issuer or guarantor of a security will be unable to pay obligations when due; due to decreases in liquidity, the Portfolio may be unable to sell its securities holdings at the price it values the security or at any price; and the Portfolio's investment may decrease in value when interest rates rise. Volatility in interest rates and in fixed income markets may increase the risk that the Portfolio's investment in fixed income securities will go down in value. Risks associated with rising interest rates are currently heightened because interest rates in the U.S. are at or near historic lows but may be expected to increase in the future with unpredictable effects on the markets and the Portfolio's investments.

[Firm Disclosures]