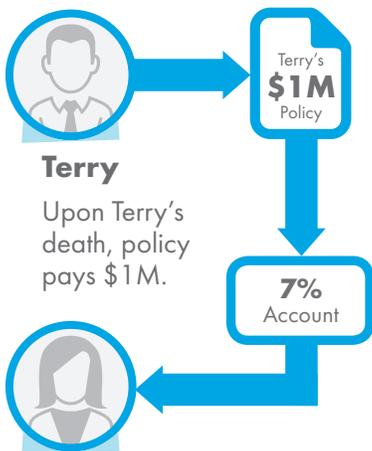# WHAT IF. . .the current interest rate environment made your life insurance coverage inadequate?

2007 PLAN:

Terry and Becky's[1] insurance professional calculated that approximately $1 million could provide the needed income.[2]

A $1 million dollar policy was purchased.

Terry

Terry's **$1M** Policy

Upon Terry's death, policy pays $1M.

7% Account

Becky

Amount: $45k per year
Inflation Adjustment: 4%
Duration: 45 years

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[1] Not an actual case, and is a hypothetical representation for illustrative purposes only.

[2] Using a net present value calculation, $1,082,822 is the amount one would need in an account, which is earning 7% each year, to provide $45,000 in the first year, then adjusting that amount each year for a 4% inflation rate. At this rate, the account would run out of money in 45 years.

BACKGROUND

In 2007, Terry (47) needed enough life insurance to provide his wife, Becky (45), $45,000 per year, adjusted each year for inflation, until Becky reaches age 90 (45 years).

To calculate the necessary insurance amount, two rate assumptions were used:

Long-term Inflation Rate: to determine how much to increase Becky's income each year. A 4% inflation rate made sense to them in 2007;

Long-term Investment Rate: to determine how much needed to be invested to generate Becky's inflating income stream. A 7% rate seemed conservative to them in 2007.

Their financial professional contacts them to review their policy. They explain that their coverage is still adequate because nothing significant has changed in their personal circumstances (same income, same home, etc.).

PROBLEM

But something *has* changed. In 2017, Terry and Becky are more conservative as a result of the economic turmoil and uncertainty of the last decade.

- They still want $45,000 per year, adjusted each year for inflation. That number is now $54,000, based on the Consumer Price Index over the last ten years;

- Terry still wants the income to last Becky to age 90 (36 years);

- The more-conservative Terry and Becky decide to change their rate assumptions:
  - **Inflation Rate:** Reduce the inflation rate from 4% to 3%;
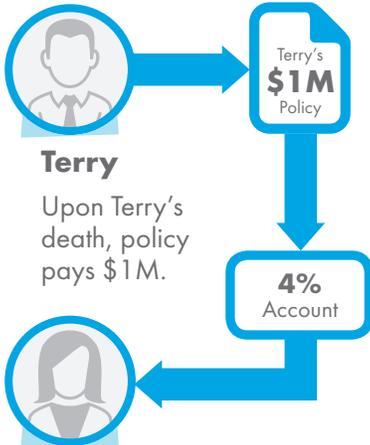 - **Investment Rate:** Reduce the investment rate from 7% to 4%.

Terry and Becky's financial professional calculates that, at these new rates, the $1 million will only last 21 years—Becky's age 75.

2007 PLAN IN 2017:

With the new rates, Becky's income would run out in 21 years!

Terry

Terry's **$1M** Policy

Upon Terry's death, policy pays $1M.

4% Account

Becky

Amount: $54k per year
Inflation Adjustment: 3%
Duration: 21 years

$500K additional funds needed to provide the income to Becky's age 90.[1]

[1] Using a net present value calculation, $1,549,388 is the amount one would need in an account, which is earning 4% each year, to provide $54,000 in the first year, then adjusting that amount each year for a 3% inflation rate. At this rate, the account would run out of money in 35 years. Since there is already a $1M policy in place, an addtional $500K should accomodate their needs.

FOR MORE INFORMATION

SOLUTION

Add $500,000 of coverage to provide Becky's income need – accommodating Terry and Becky's current, more-conservative, position.

RESULTS

While the couple saw no initial reason to review their insurance needs with their financial professional, they realize that their future was not simply impacted by their own actions. The economic forces around them have changed their needs– and life insurance can help provide for those needs.

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