Pension sense

Annuity vs pension drawdown

The main aim of a pension is to provide you with an income when you retire. Generally, there are two main ways to do this using a defined contribution (DC) pension.

Annuity: more security

When you buy an annuity, you are selling part or all your DC pension pot to an insurance company in return for a guaranteed income, either for life or a fixed term.

Pension drawdown: more flexibility

With pension drawdown, you take an income from your pot while keeping the rest of your savings invested so they have the potential to grow.

Let's have a look at how these two options compare.

	Income guarantees
Annuity	You receive a set guaranteed income for the duration of your annuity; this could be for life or a fixed term.
Pension drawdown	Your income is not guaranteed. Depending on investment performance and how much you take, you could run out of money.

	Flexibility
Annuity	You cannot change the terms of your annuity, which means the income you receive and when you receive it are fixed. The amount of income you get will rise if you choose an annuity that increases in line with inflation.
Pension drawdown	You can increase or decrease your income as needed. You can also withdraw ad-hoc lump sums as and when you like.

	Ease of use
Annuity	Once you have set up your annuity, there is nothing else you need to do.
Pension drawdown	You need to regularly check and manage your income to make sure you do not run out of money.

	Investment risk
Annuity	Your money is not invested, so investment risk is not a concern.
Pension drawdown	Your money is invested in different assets, which means your income will almost certainly be affected by periods of poor investment returns.

	Inheritance
Annuity	An annuity cannot be inherited. Although, you can choose to buy an annuity that continues to pay a reduced income to your spouse when you die.
Pension drawdown	You can pass on remaining funds in a drawdown pension to one or more beneficiaries when you die. Any remaining funds are free from inheritance tax, although, this will almost certainly change in 2027.

The retirement specialists

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