Why Fixed Indexed Annuities Should Co-exist with Bonds in a Fee-Based Portfolio

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After a solid start to the year, financial markets have turned volatile, struggling for direction in recent months. Any time that happens, financial advisors and clients tend to have more in-depth conversations about portfolio construction.

Depending on the circumstances, these discussions normally touch on how, in an uncertain environment, a client can find growth potential without substantially upsizing risk. Whatever the case, RIAs have rarely introduced annuities as a potential strategy, which is natural: Until recently, not only was it unrealistic for them to do so based on their business model but these vehicles were primarily viewed as retirement income solutions.

But RIAs are now more easily able to recommend annuities, and annuities have evolved to meet the demands of various planning areas, including tax, retirement income and estate planning. With that in mind, conversations about portfolio construction could be very different going forward. Indeed, certain types of fee-friendly annuities could prove to be another way to position clients—and not just when economic and market storm clouds cause equities to decline.

Market Correlations

Most financial advisors today—whether they're registered reps or an RIA—understand that annuities can help clients build retirement savings, defer taxes, generate lifetime income, and provide a guaranteed death benefit to others. Beyond that, what an increasing number of them are coming to find is that certain fixed and indexed annuities are playing an important role alongside bonds in the defensive portion of a client's portfolio.

Nevertheless, most RIA-based financial advisors tend to be more comfortable providing financial advice on bonds or bond mutual funds, even as they might not be the best solution for clients. One big reason, of course, is that bonds are typically inversely correlated to equities. But even as recently as 2022, exceptions proved the rule; bonds and equities fell by 12.5% and 18.1%, respectively.[1]

While stocks and bonds have declined in tandem only two other times since 1931[2], there are a variety of reasons to believe that these asset classes dropping simultaneously may not be such an atypical phenomenon in the future. That's due to various factors, including the Fed winding down years of easy money policies, the prospect of a recession and the ratcheting up of geopolitical tensions that could further hinder trade with Russia, China and Mexico.

After 10 rate increases since the beginning of last year, it might seem like bond investment yields are more attractive—and many of them are. Yet as we all know, when rates go up, bond prices go down. To mitigate that, all you have to do is hold a bond to maturity. But, of course, that's not an option with widely popular bond funds, which do not have maturity dates.

This quandary underscores why a genuinely diversified portfolio calls for correlation-based defenses to exist alongside a structural one. This is particularly important for clients with risk tolerance and risk capacity dislocations.

Therefore, financial advisors can no longer rely on piling into bonds or bond funds for their clients every time the stock market gets wobbly. They must consider other options, and annuities could be one of them.

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Risk Dislocations

For example, some advisory clients may be near or in retirement—meaning their capacity for risk is presumably lower. Even so, they may still want to hold shares of large-cap stocks to pursue growth. Conversely, some clients in their 40s, whose risk capacity on paper may be higher, nonetheless have a low tolerance for risk and thus embrace a bond-heavy portfolio.

The fact is that despite the preconceived notions about certain groups of clients, there is often a big disconnect among those regarding their capacity for risk and their tolerance for it. By providing both upside growth potential and a downside floor, fee-friendly, fixed-indexed annuities can help financial advisors address those types of situations.

Use Cases

Of course, some clients will be who they appear to be, whether they're high earners in their prime working years or long-retired couples. They will have the exact risk capacity and tolerance you would think. So, a fixed—or, for that matter, any other type of annuity—may not be right for them. But then again, they might.

Between 2020 and 2025, the average annualized return of the Bloomberg U.S. Aggregate Bond Index was 80 basis points.[3] Over the longer term, bonds have generated approximately 6%–7% annualized returns since the mid-1970s, supported by decades of declining interest rates. But now consider that rates and caps on fixed indexed annuities currently range between 8% and 12%, often for five-year terms.

Whether bond yields go up, down or stay flat, all sorts of risk profiles could benefit from the new generation of indexed annuities. Ignoring for a second that such vehicles have outperformed bonds in recent years, how else is it possible to ensure that clients are diversifying their defensive portfolio with, both, correlation-based and structural-based defenses? In other words, what other strategy would allow them the opportunity to earn interest up to a specified cap and principal protection against downside losses (at worst, they would earn nothing for a year)?

Value Amid Volatility

Trust, in many ways, is basis of the wealth management industry. Financial advisors can build trust in many ways, including by listening carefully, being compassionate and showing that they care. Another way, however, is to recommend only the products and services clients need. With annuity providers delivering innovative solutions to the market, that task is becoming simpler each day.

[1]Noonan, Danny. "Bonds Reclaim Their Defensive Status," Morningstar. August 13, 2024.
[2]Historical Returns of Stocks, Bonds and Bills. NYU Stern. Updated January 5, 2026.
[3]Bloomberg U.S. Aggregate Bond Index 2020–2025. Bloomberg Professional. https://www.bloomberg.com/professional/products/indices/quote/LBUSTRUU:IND.

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