Institute for Lifetime Income

RESEARCH. INSIGHTS. ADVOCACY.

DISCUSSION PAPER

Designing lifetime income stream options for members

Building better outcomes for a more secure retirement

SEPTEMBER 2026

01.

Designing lifetime income stream options for members

Superannuation funds looking to meet the regulators expectations of the Retirement Income Covenant have been helped by Treasury's publication of the Best Practice Principles for retirement income solutions.

These principles highlight the key requirements for delivering better member outcomes in retirement:

- **Know** your members
- **Build** a range of appropriate solutions
- **Guide** members to their best solution

Delivering better outcomes requires a constant feed-back loop. It is not a sequential task list. While building the right solution requires knowledge of the member base, it is also important to know how members will respond to various forms of guidance. This guidance could be in the form of education or advice provided through different channels.

Understanding how members think and behave can be just as important as understanding their balance and financial preferences. Member research can provide specific insights that might differ at a fund level particularly when members are mostly from the same industry or there is a geographical skew. However, learnings are available from the broader population that can assist in designing appropriate products.

02.

Know your members: what makes them happy?

The goal when saving for retirement is to accumulate a higher savings balance but the goals in retirement can be different. Money alone does not guarantee happiness.

When members have choices to make, they might not necessarily choose an option that maximises their financial position and can instead opt for choices that make them happier. Insights from the Challenger Retirement Happiness Index on what makes retirees happy can be useful.

According to the Happiness Index, designed in collaboration with Challenger and research house YouGov, there are a range of drivers for happiness in retirement, and based on the 2026 results, money was the lowest of the six key drivers of happiness. The top driver was the activities and hobbies that the retiree enjoys.

Many of these of course require money to participate, such as the cost of golf clubs and green fees. The message was clear; the key to improving happiness isn't to get more money, it is to do more with your money. Confidence and certainty can play a role in helping retirees do just that. Another key area was the importance of mental health, with retirees placing a greater emphasis on how mental health contributes to happiness in retirement.

Drivers of happiness in retirement

Figure 1: Drivers of happiness in retirement

Source: Challenger Retirement Happiness Index 2026

03.

More than money - the value of a purpose in retirement

Retirees report that having a purpose is a contributor to happiness. The Challenger Happiness index reported that more than seven in ten Australians aged 60+ had a clear sense of purpose[1].

For some people, retirement results in a loss of purpose, particularly where purpose was attached to their previous work, so finding a new sense of purpose in retirement can be important to improving happiness. Purpose is often related to how people spend their time in retirement. For some it is in activities or hobbies that they enjoy.

Volunteering is another way retirees find their purpose. It was also a strong predictor of purpose as 86% of volunteers reported a clear sense of purpose, but only 68% of those who don't volunteer reported this driver of retirement happiness. Most volunteering, by definition, doesn't provide payment, so it is important for retirees to feel secure in their income sources to fund their lifestyle so they can spend time volunteering.

While money isn't the end goal for happiness, income underpins the spending needed to enjoy activities in retirement. Having enough money to enjoy retirement was ranked as the most important factor (although not the biggest driver) for a happy retirement by 44% of Australians aged 60+.

While 72% rated having certainty that their money would last for life as a top priority for retirement finances. So, it is not surprising that 76% said that they would be happier if they had a guaranteed income for life in retirement. A secure income stream can provide the peace of mind that enables a retiree to enjoy their time in retirement.

[1] Challenger Retirement Happiness Index 2026.

04.

The cost of living remains a concern

While Australian retirees can be broadly described as happy, they still have many financial concerns.

A key concern is the cost of living as older Australians are worried that the cost of living will impact their ability to maintain their lifestyle (57%); have financial security (54%); and have income that lasts as long as they do (46%).[2]

Concerns over the cost of living can lead to hesitation and underspending that has the potential to derail a happy confident retirement. The latest report indicates that while current retirees have concerns over the cost of living, they are still relatively happy.

Providing a solution to retired members that helps with their cost-of-living concerns can improve financial outcomes in retirement. But for retirees to embrace the solution and get the benefit of improved outcomes, it is necessary that retirees can understand how it helps their overall retirement. This is where investor psychology needs to be considered.

48%
of women

Women who usually retire with less super, along with pre-retirees are more likely to rank fear of running out of money in retirement as one of the top three things impacted by the cost of living.[2]

[2] Based on responses from 2,015 Australians aged 60 and above as part of the Challenger Retirement Happiness Index 2026.

05.

The psychology of choice and control

One aspect of the provision of retirement income solutions that can be overlooked is that retirees make choices about their options.

A good retirement solution is one that will help a retiree make a decision that is best for them and to make it at the appropriate time. This issue was raised in a recent IFS whitepaper.[3] While this paper focussed on advice and pathways for retirees, the key learnings apply to development of retirement product solutions. People have their own biases, so it is incumbent on a solution provider to accommodate their preferences.

One of the challenges for managing superannuation in retirement is that during the accumulation phase the member does not need to interact with their super. Active members can make investment choices, or even manage their own superannuation fund, but that changes in retirement. Retirees need to make a choice with their retirement solution.

Variations in lifestyle and expectations mean that there needs to be a range of different solutions for retirees. Retirees also have more time available, and many want to actively engage in financial decisions, which they might not have done previously.

One key to a successful solution is simplicity. Retirees need to understand what their choices are and how these choices relate to their own goals in retirement. Solutions that aimed to solve all the retirement income challenges but had complicated structures, fees and/or interactions have not been successful in Australia.

[3] Industry Fund Services (IFS): Designing Smarter Retirement Pathways for Members.

One example is the guaranteed lifetime income benefits riders that were applied to variable annuities as launched in Australia in the 2000's. These were complex products with multiple fees that advisers found difficult to explain to retirees, resulting in limited uptake.

The alternative is a set of building blocks where the benefits are clear. The IFS paper highlights a three-model approach that can assist members meet their retirement income needs. Instead of product labels, simple comparisons such as those in Figure 2 are applied.

Figure 2: Simple retirement income components

Using clear labels and presenting understandable concepts to the retiree rather than highlight product complexity, enables retirees to engage with a retirement income solution. Having a range of building blocks enables retirees to mix the allocations to meet their own preferences.

There can still be value in a fund providing guidance on what a good solution might look like, or potentially different options for clearly defined cohorts. These options can provide good case studies for retirees to understand how the solution might work for 'people like me'.

Understanding more about member psychology can help funds to determine 'how' to produce a retirement income solution, but it is also important to understand 'what' the elements of that solution are.

06.

Build: understanding lifetime income streams

Innovations in retirement solutions in recent years have increased the range of lifetime income streams that can be available for retirees.

There are three broad forms that the lifetime income streams can take:

- **Guaranteed lifetime income stream** – where the income payment is either fixed or set to increase with inflation.
- **Investment-linked lifetime income stream with longevity insurance** – where the income payment will move up and down with the returns of the linked investment.
- **Investment-linked lifetime income stream with pooling only** – where the income payment will move up and down with investment returns, and the degree of protection depends on the longevity of the individuals in the pool as opposed to an insurer.

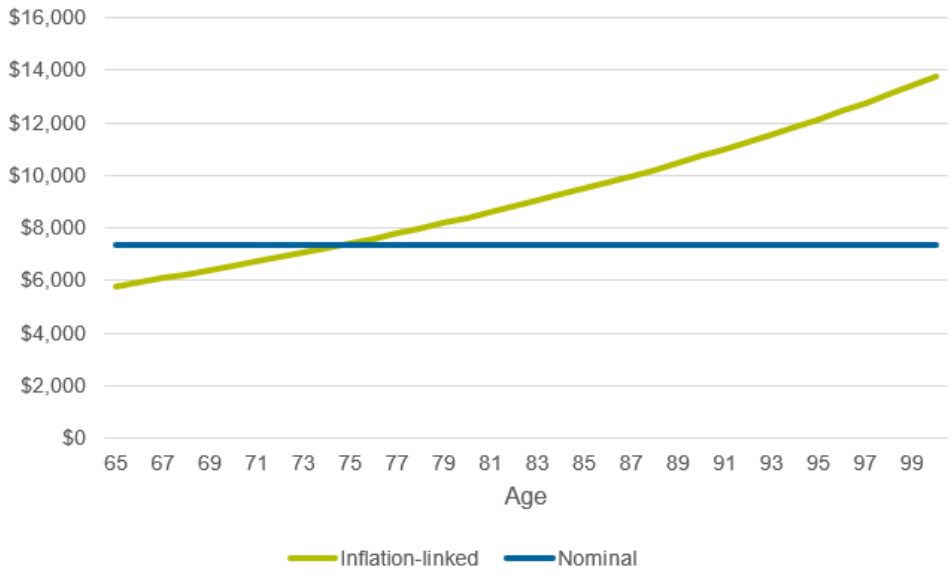
Guaranteed lifetime income stream

A guaranteed lifetime income stream is usually delivered through the purchase of a lifetime annuity. Either directly, or when embedded in a Superannuation Fund's retirement solution, the income stream is backed by an agreement with a life insurance company to provide the guarantee. The way it works is that the retiree will pay a purchase price, and in return receive a stream of income payments for as long as the retiree (and their spouse if the income stream is reversionary) lives. That commitment is guaranteed by the life insurer.

This income stream can be designed to increase over time. A common form is to increase payments in line with consumer inflation, but other options include fixed rate indexation or flat payments. When a retiree selects an income stream that doesn't increase over time, that will result in higher payments initially, but the indexed payment will increase and overtake the flat payments over time. Figure 3 highlights how the payments vary over time.

Taking a scenario of a $100,000 investment, income of $7,363[4] can be paid every year, even if the retiree lives past 100 years. For an inflation-linked lifetime income stream, the initial payment is lower, only $5,789 in the first year, but payments increase each year in line with CPI inflation. The projections in Figure 3 have used inflation of 2.5% p.a. and the indexed payments will exceed the fixed payment by age 75 with higher cumulative payments for someone living to age 84 or longer.

Figure 3: Guaranteed income payments: inflation-linked v nominal



Source: Challenger. Based on payments from a $100,000 investment for a 65-year-old male as at 25 May 2026. Death benefits and some capital access are included. Future inflation assumed to be 2.5% p.a.

[4] Payments quoted are for a 65-year-old male as at 25 May 2026.

Investment-linked lifetime income stream

An alternative to a fully guaranteed income stream is one that is flexible in its investment approach but still ensures that the income stream continues for the life of the retiree. This is not just spending a fixed proportion of a declining pool of savings so that it's never completely used, but sustaining the income stream that can support the intended lifestyle through retirement.

The role of any lifetime income stream is to convert a pool of savings (capital) to a stream of income. The income stream can be sustained when there is a broader pool share across a large number of people. The key risk is that the available capital is not enough to pay for people who live longer than average. This can be managed when some capital from participants who don't live as long supports the broader pool.[5]

This feature is maintained in an investment-linked lifetime income stream, but the dollar amount is not guaranteed. Where a guaranteed lifetime income stream will guarantee the payments in dollars, the investment-linked lifetime income stream effectively pays 'investment units' to the participants.[6] The value of these units goes up and down with the investment, just like any other unit price.

Insured v pooling only lifetime income streams

The design of lifetime income stream products is based on expected returns and estimated population mortality. Actual outcomes can vary depending on market movements and changes to the pool's population over time. An investment-linked lifetime income stream will pass through all the market movements, but there are two approaches to managing the population mortality experience:

1. Pooled. If there are enough participants in a pooled investment-linked lifetime income stream (as offered potentially by a large superannuation fund), then the population mortality outcomes might be stable. A pooled (only) approach relies on this stability but will need to change (up and down) when mortality outcomes do not align with expectations. These are expected to be small when the pool is sufficiently large and diversified.

2. Insured. Additional confidence in the mortality pooling can be achieved through longevity-insurance. A third-party life insurer can be used to add certainty to the mortality pooling process. The value will still move up and down with the investment, but the bonus to survivors (as an age-dependent percentage of the balance or the investment-linked indexation) will be agreed in advance. Deviations from expectation (higher and lower) are absorbed by the insurer which provides capital, at a cost, to ensure the stability of credits to investors.

[5] These are sometimes called mortality credits or survivor bonuses.

[6] Different approaches are used in different products currently available. Some products use an age-based percentage drawdown that increases over time, and others rely on indexing based on investment returns, but the different approaches provide the same effective investment-linked exposure.

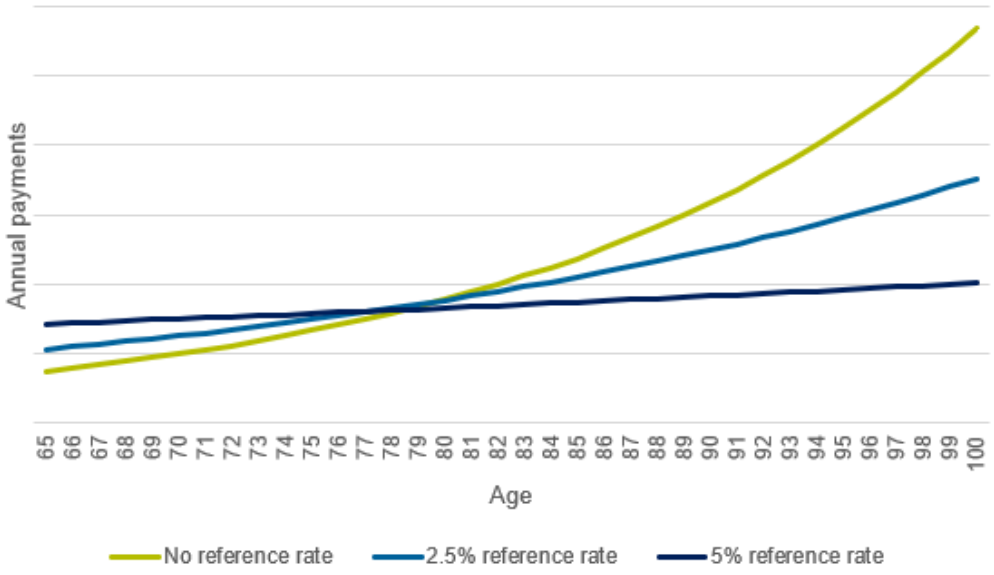
Adjusting the payment profile

One objective in an investment-linked lifetime income stream is to benefit from the (expected) higher returns on a portfolio over time.
The higher returns (if realised) generate more capital that can then be spent. As with any investment, risks of lower returns and income remain. However, the income profile from the expected returns does not match the typical spending profile of retirees.

Many studies have shown that spending tends to decline through retirement after adjusting for inflation.[7] It would be a better fit for the income stream to match this flat to falling (in real terms) profile.[8]

This is achieved by applying a reference rate to an investment-linked lifetime income stream. Payments are increased by the investment return less the reference rate, rather than the full gain. It returns are low (or negative) payments can fall. This is balanced by a higher initial payment. The overall value of the payments is equivalent, but the profile can be very different as seen in Figure 4. The profile can even decline over time if the reference rate is higher than average returns.

Figure 4: Reference rates and payment profiles



Source: Challenger. Indicative profiles assuming income stream starts at age 65. Investment returns are assumed to be 6% p.a.

[7] See for example: Blanchett, D, (2014). "Exploring the retirement consumption puzzle" Journal of Financial Planning, 27(5), pp34-42; Daley, J., B. Coates, T. Wiltshire, O. Emslie, & J. Nolan, (2018). Money in retirement: More than enough. Grattan Institute.
[8] The decline in spending in the studies is small, suggesting that nominal spending tends to increase.

Building the income stream into the retirement portfolio

Retirees generally need more than a lifetime income stream. The requirements of the retirement income covenant for superannuation funds include flexibility and access to capital when required in addition to maximising income and managing longevity risk. It is practically impossible for any single income stream to meet all these needs. The best solutions could include a lifetime income stream as part of the overall solution.

In many cases the combination of a lifetime income stream and an account-based pension can lead to better outcomes for retired members. Mercer demonstrated how portfolio outcomes are improved when a lifetime annuity is used as a substitute for the defensive assets in a retirement income portfolio.[9] This report provides specific Australian examples of the better portfolio outcomes that has also been reflected in other research.[10]

Taking a portfolio approach to delivering a retirement income solution enables a retiree to achieve their multiple goals. Having a range of components within the portfolio provides the opportunity for each component to meet a different need in the portfolio.

Capital flexibility

Flexible access to capital is a need for retirees who might require a lump sum for a renovation or a major overseas holiday. Personal loans might be possible, but difficult against an income stream alone, so it is preferable for a retiree to be able to access their capital for these lump sums. The total drawdown needs to be considered as part of the sustainability of the approach, but capital should be accessible.

However, this doesn't mean that every dollar needs to be available. If they were and the retiree used it all, perhaps to buy a sports car,[11] there wouldn't be anything left to fund the rest of their retirement. In practice this means that the capital flexibility does not need to be maintained for 100% of the retirement portfolio.

There is a trade-off between having the flexibility to access to all capital and having the certainty of a fixed income stream. As with many choices in life, having a bit of both can be more rewarding. There is also no need for a retiree to lock in all their income needs in a lifetime income stream. If spending declines, as noted in practice, at most only the lower income level needs to be protected.

Some of this could come from the Age Pension, so the allocation to a lifetime income stream can be a minority allocation in the portfolio. As a component of a portfolio, the choice of the lifetime income stream should depend on the other elements in the portfolio.

[9] Mercer May 2024 Principles of Retirement income Annuitisation: a report for Challenger: Chen, W., Minney, A., Toscas, P., Koo, B., Zhu, Z. and Pantelous, A.A., 2021.
[10] Personalised drawdown strategies and partial annuitisation to mitigate longevity risk. Finance Research Letters, 39, p.101644. or Pfau, W.D., 2012. An efficient frontier for retirement income. Available at SSRN 2151259.
[11] Minister fuels pension debate with Lamborghini comment - BBC News

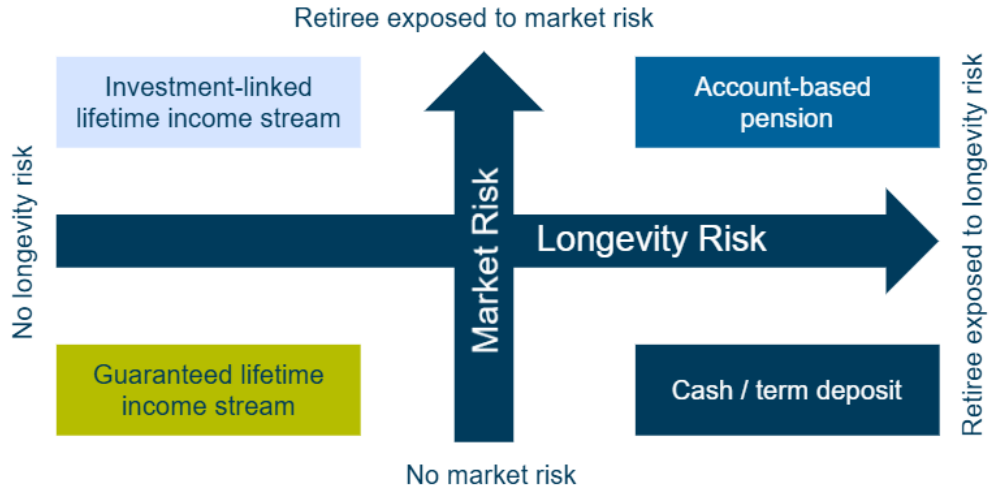
Portfolio trade-offs

In additional to flexible access to capital, a retirement income portfolio should include exposure to higher (expected) returns through an appropriate asset mix, protection from inflation and income that will last for the life of the retiree. With the increased range of lifetime income streams available, the market exposure and inflation protection can be provided within the lifetime income stream as well as through other, account-based income streams. This means that the retirement income solution for a member can involve a mix of income streams and exposures with allocations that are not tied to specific products.

Two of the trade-offs in any retirement portfolio are the exposures to market and longevity risks. Market exposure can lead to higher expected returns, but the risk is that returns could be lower than expectations leading to reduced income to spend. The trade-off for longevity risk management is flexibility. Protecting longevity risks means that capital needs to be committed. This can be kept to a reasonable level with a death benefit and some access to capital for a period.

Product innovation for lifetime income streams in recent years has filled out options that protect against longevity risk but maintain market exposure. These are the investment-linked lifetime income streams that can be seen in Figure 5.

Figure 5: Risk exposures for retirement income products



Source: Challenger

Stepping through a simple example can explain how this process works. Consider a retired member who, after considering all their preferences wants to have:

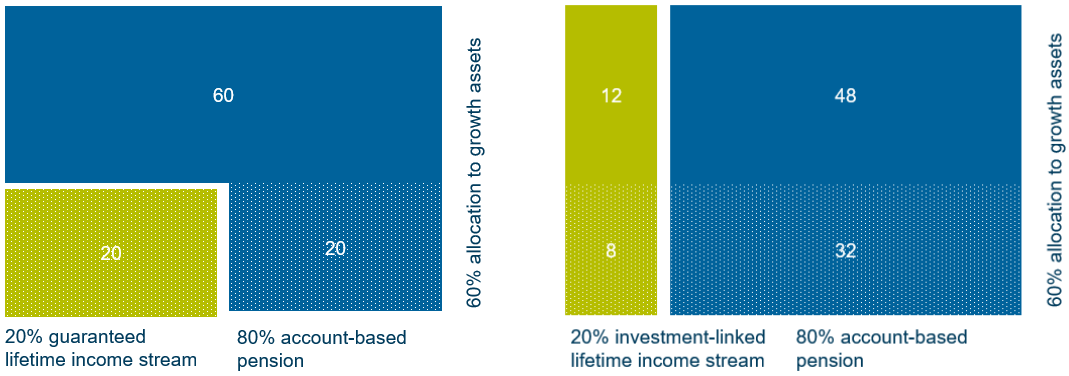
- An investment exposure that is 60% growth assets and 40% defensive;
- A desire to have 20% of the portfolio protected against longevity risk.

There are two alternative ways that the member will be able to achieve this. One role for a superannuation fund is to design the option that is appropriate for member cohorts who might prefer either to:

1. **Invest 20% into a guaranteed lifetime income stream** and 80% into an account-based pension that itself has an allocation of 75% to growth assets. Overall growth exposure is 60% = 80% * 75%.
2. **Invest 20% into an investment-linked lifetime income stream** which has an allocation of 60% to growth assets and 80% into and account-based pension that has the same 60% growth allocation.

Graphically the two portfolio concepts are represented in Figure 6. They both achieve the goals in longevity protection and market exposure, but the components can vary across the product choice.

Figure 6: Alternative retirement income portfolios



Either approach can meet the primary portfolio needs, which means that the best choice can be based on secondary considerations. This is where the member behaviours and preferences are important. Simplicity is always desirable and member preferences can vary. If members prefer to have the same exposure across the investment options, an investment-linked lifetime income stream will be easy to implement.

Many retirees prefer each option to have a purpose, such as one for flexibility and one for certainty. When the preference is to have components with distinct roles it is likely to be easier to implement a solution with a guaranteed lifetime income stream, leaving the market exposure to the remainder of the portfolio such as an account-based pension.

A retirement income solution that works for members

When designing a retirement income solution for fund members, it is important to understand what they are seeking and how the members will engage with the solution. It is important to engage members early with the concept, building up an understanding of generating retirement income over time.

Funds can keep retirement simple for members by containing the financial complexity within different components. Members will be able to make decisions about these components based on how they meet the member's needs.

Australia has a world class superannuation savings system, with the retirement assets portion forecast to grow four-fold over the next 20 years to $4.5trn. Australians overwhelmingly put their trust in their Superannuation Funds to help them navigate retirement and, ultimately, retire with dignity.

Having a simple solution, that provides members with the confidence to spend on what's important to them in retirement is no longer just important, it's now a retirement system imperative.

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Aaron Minney, CFA, F Fin, is Head of Retirement Income Research at Challenger. He leads research into retirement income, decumulation, portfolio construction and longevity risk, and is a frequent contributor to industry research, media commentary and policy discussion on Australia's retirement system. Aaron has held senior investment roles at major Australian financial institutions. He has been an Adjunct Fellow at Macquarie University since 2017 and is a Chartered Financial Analyst.

About the Institute

Institute for Lifetime Income
RESEARCH. INSIGHTS. ADVOCACY.

Why the Institute for Lifetime Income exists

The Institute for Lifetime Income is a research body dedicated to providing financial and longevity literacy focused on lifetime income, retirement plan design and lifelong financial well-being.

Established by Challenger Limited - Australia's largest retirement income provider - the Institute publishes research, data, and practical guidance on income in retirement. Our work is designed to inform pre-retirees, retirees, financial advisers, and policymakers navigating one of the most consequential financial decisions a person will ever make.

Australia has one of the world's great superannuation systems. But accumulating wealth is only half the challenge.
The harder question - how to convert that wealth into income that lasts a lifetime - remains underserved. Too many

Australians enter retirement without a plan for longevity risk, sequencing risk, or the steady erosion of inflation. The Institute exists to close that gap.

Our evidence-based research draws on Challenger's deep expertise in retirement income, annuity markets, and the regulatory landscape governing superannuation.

1. This report (the Report) has been prepared by Challenger Group Services Pty Ltd (Challenger) as at 8 September 2026. Challenger Life Company Limited ABN 44 072 486 938, AFSL 234670 is the issuer of lifetime annuities.

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