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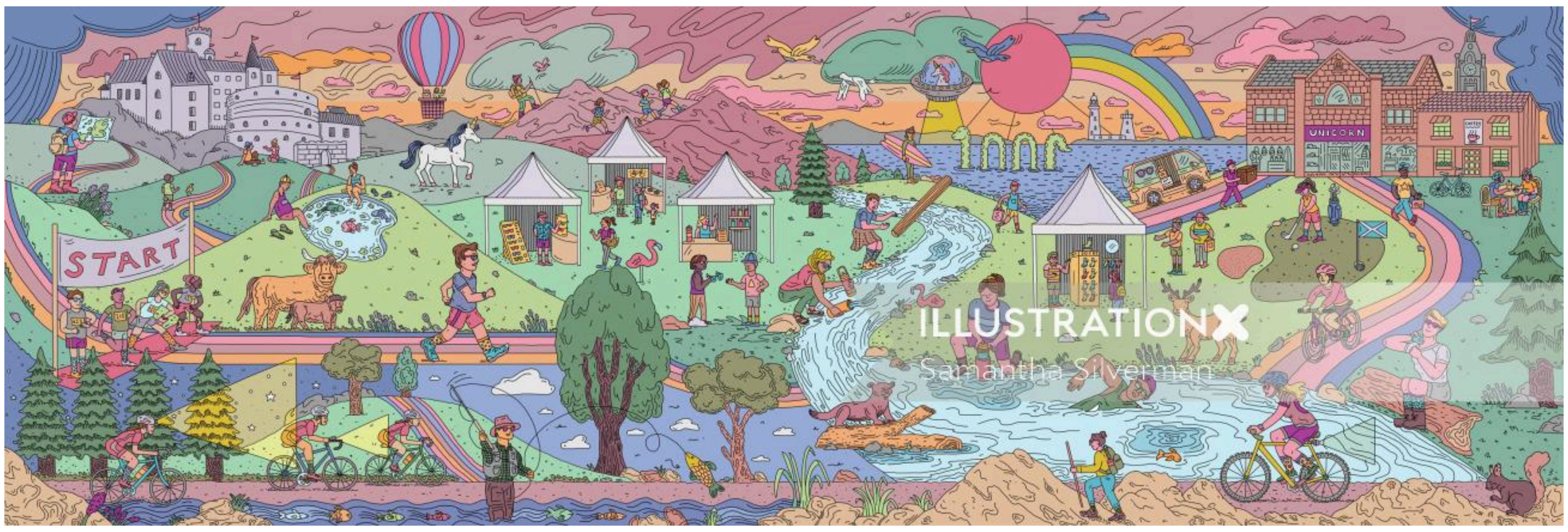

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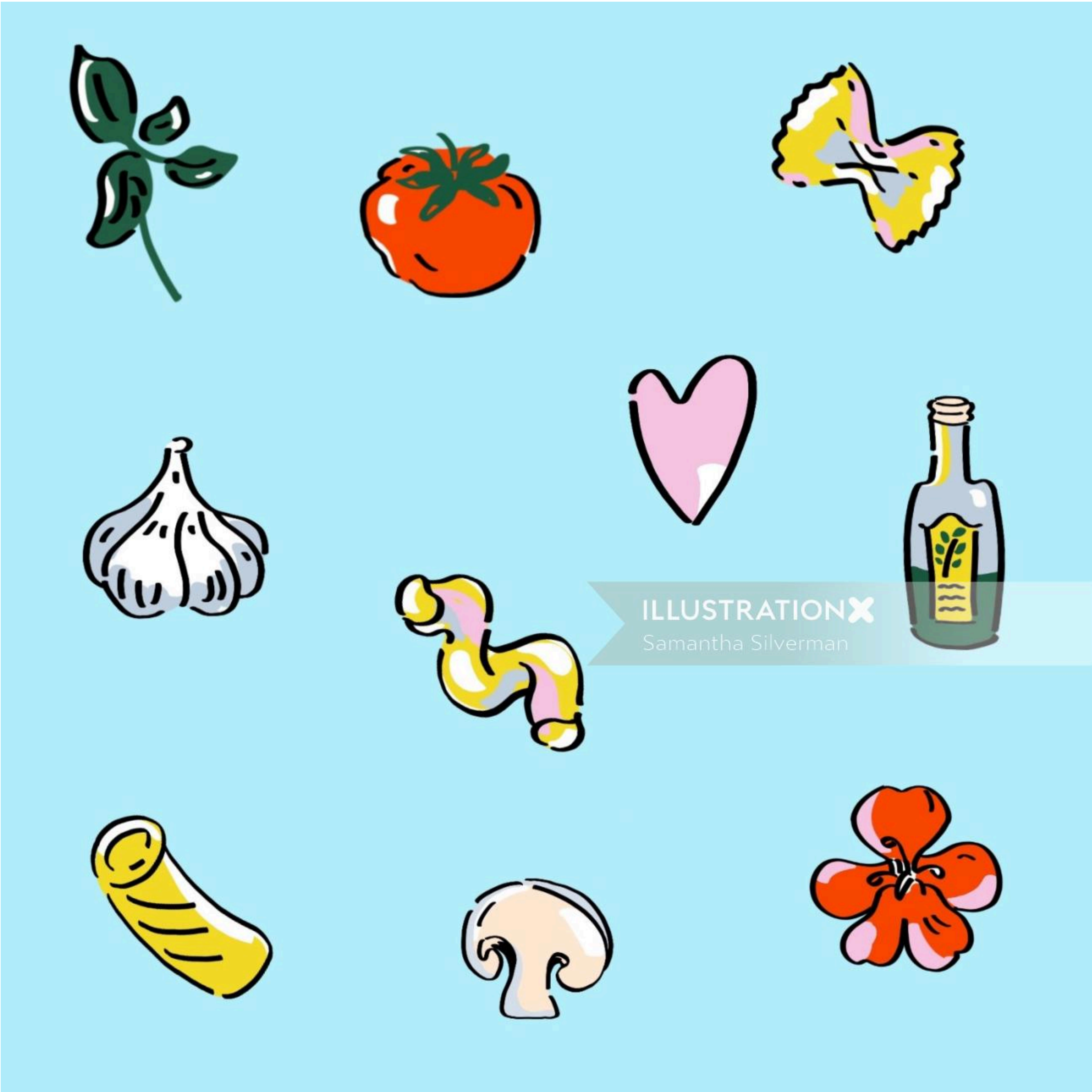

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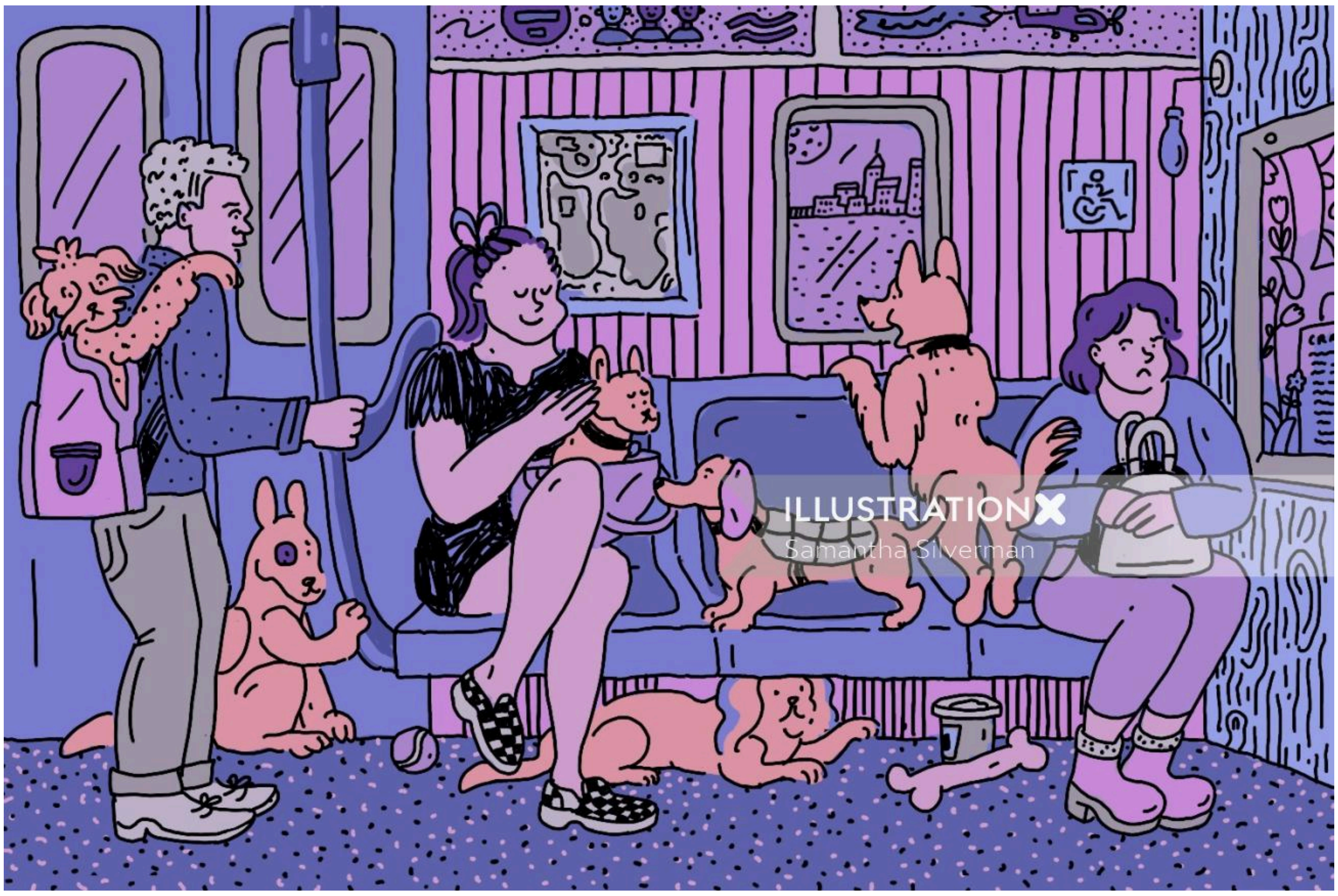

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INVESTMENTS | RETIREMENT INCOME

New Solutions

The demand for retirement income is increasing exponentially

The retirement wave keeps rolling. The Schwartz Center for Economic Policy Analysis reported that, from March 2020 through this February, the number of retiring workers between ages 55 and 74 expanded beyond the pre-pandemic trend by an additional 1.1 million people. Demographics indicate that the surge will likely continue.

"According to the U.S. Bureau of Labor Statistics, in 2020 approximately one-quarter (24%) of the workforce was over 55, versus 18.9% in 2008," says Josh Cohen, head of client solutions at PGIM DC Solutions in Newark, New Jersey. "The demographic shift is compounded by the fact that this generation of workers is more reliant on defined contribution plans than defined benefit plans."

At the same time, interest in guaranteed lifetime income investment options has grown, according to Nationwide's 2022 "In Plan Sponsor Survey Report." The survey for the study found that more than half of employees are interested in contributing to a guaranteed lifetime income investment option included as part of a target-date fund, an 11-point increase since last year—53% vs. 42%, respectively. Forty-eight percent reported they are interested in contributing to such an option included as part of a managed account. Roughly two in five employees (41%) said they would likely roll over retirement savings into a guaranteed lifetime income investment option if they could, a 6-point increase since last year.

Participants' interest in guaranteed income is understandable. Wei Hu, Ph.D., vice-president, financial research at Edelman Financial Engines in Santa Clara, California, notes that retirees and near-retirees face complicated choices and challenging economic conditions. "Previously, low interest rates made it infeasible to just 'spend the interest' from fixed-income portfolios," he says. "Now, though we are seeing higher interest rates, it comes with a new worry: high inflation. Also, falling bond and stock prices have taken a big bite out of retirement nest eggs, and bonds have had the worst year on record."

Early Efforts and Recent Developments

The interest in providing DC plan participants with retirement income options is not new. An August SEI white paper, "Innovations for In-Plan Retirement Income," described insurers' previous efforts to gain traction with DC plans. Between 2004 and 2009, Genworth, John Hancock, MetLife and Prudential introduced products that included annuities and some version of guaranteed lifetime income. These solutions failed to catch on. According to the SEI report, as of early this year, only Prudential's IncomeFlex Funds were still operating, but [illegible] $25 million [illegible] the product's target-date funds.

The SEI report cites interviews that the Retirement Leadership Forum conducted with retirement plan executives in 2018, to learn why these products largely failed. The executives cited five primary reasons: cost, complexity, portability, liquidity and fiduciary concerns.

Despite the early products' failures, plan sponsors still express interest in in-plan retirement income options. A 2021 BlackRock survey found that 96% of 225 sponsors of large 401(k) and 403(b) plans said they feel responsible to help participants with retirement income. Among sponsors that did not offer an income option such as an annuity, 82% said they would likely add one in the next 12 months.

The leadership forum's 2021 Rethinking In-Plan Retirement Income survey, fielded in 2020, found that 54% of defined contribution investment only asset managers had a retirement income solution, and 39% were building one.

SEI cites several reasons for the [illegible]:

• [illegible] actively working to keep retired participants' assets in the company plan—36% in 2020 vs. [illegible]. More assets can provide better pricing for plans, and retired participants can benefit from institutional pricing and product access.

• 2019's Setting Every Community Up for Retirement Enhancement Act created a safe harbor for plans looking to include annuity options, addressing sponsors' concern over fiduciary-status-related litigation. A reported 90% of retirement executives said they believe this legislation, referred to now as SECURE Act 1.0, will increase demand for retirement income somewhat or significantly.

• The bond and equity markets' volatility this year reminded participants and retirees of the difference between projected investment portfolio income and guaranteed income. Retirement assets lost an estimated $3 trillion-plus in value due to the market downturn from January to mid-June, according to the Center for Retirement Research at Boston College.

The widespread use of collective investment trusts is another factor driving retirement income product design, according to Robert Muse, president of SEI Trust Co. in Oaks, Pennsylvania. Muse cites CITs' ability to deliver asset management at a lower cost: High costs contributed to the early products' failure, and CITs help newer products overcome that hurdle.

CITs' flexibility makes it easier to include annuities with equities and fixed income in the same product. The SEI report notes that BlackRock and Income America both use a CIT structure, as do the periodic payout funds from Legal & General and Schroders.

The Retirement Leadership Forum survey found that 53% of asset managers offering in-plan retirement income products used CITs compared with 20% that used mutual funds and 13% each for managed and separate accounts.

Their specific features vary, but SEI says the TDF-based approaches address

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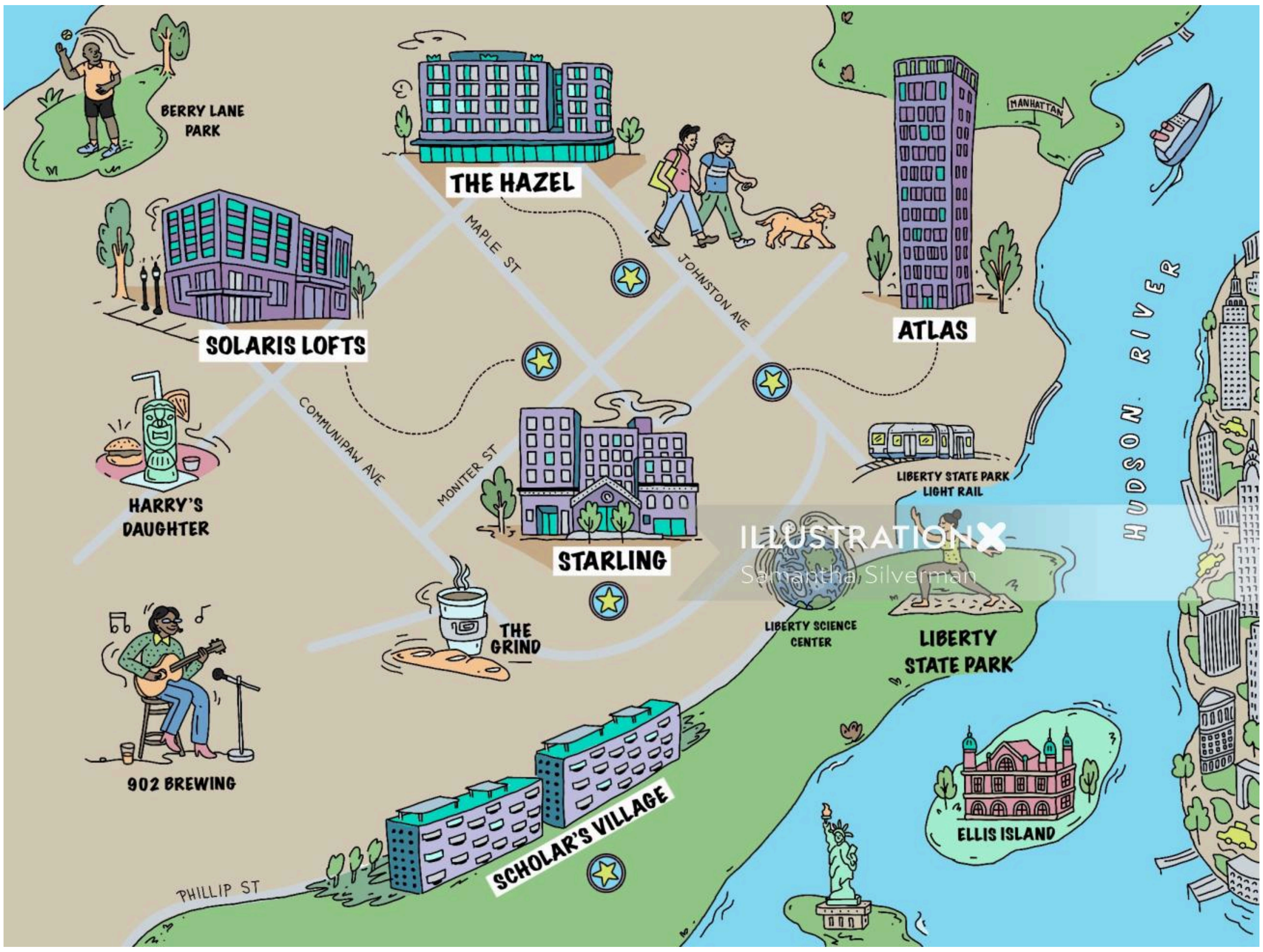

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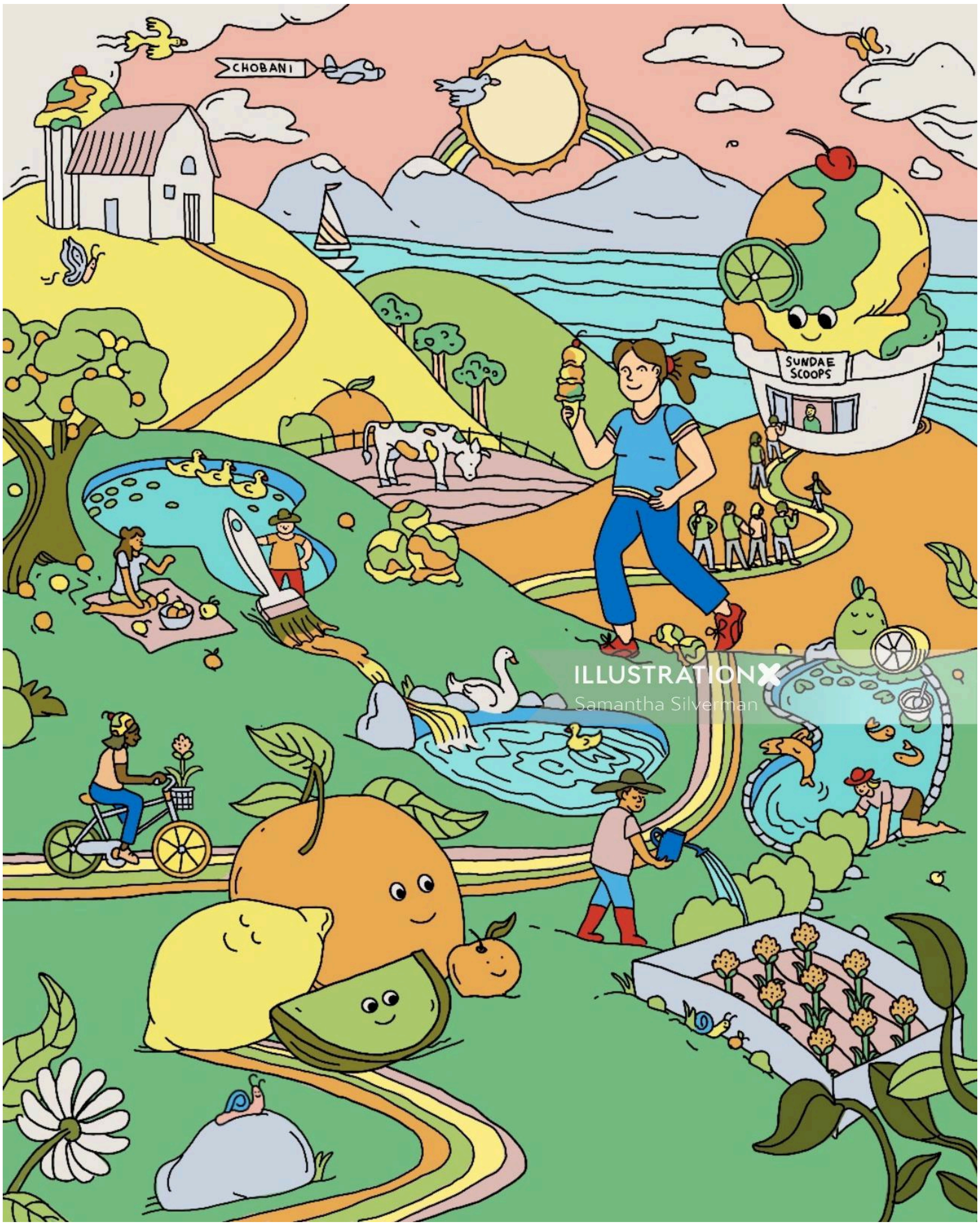

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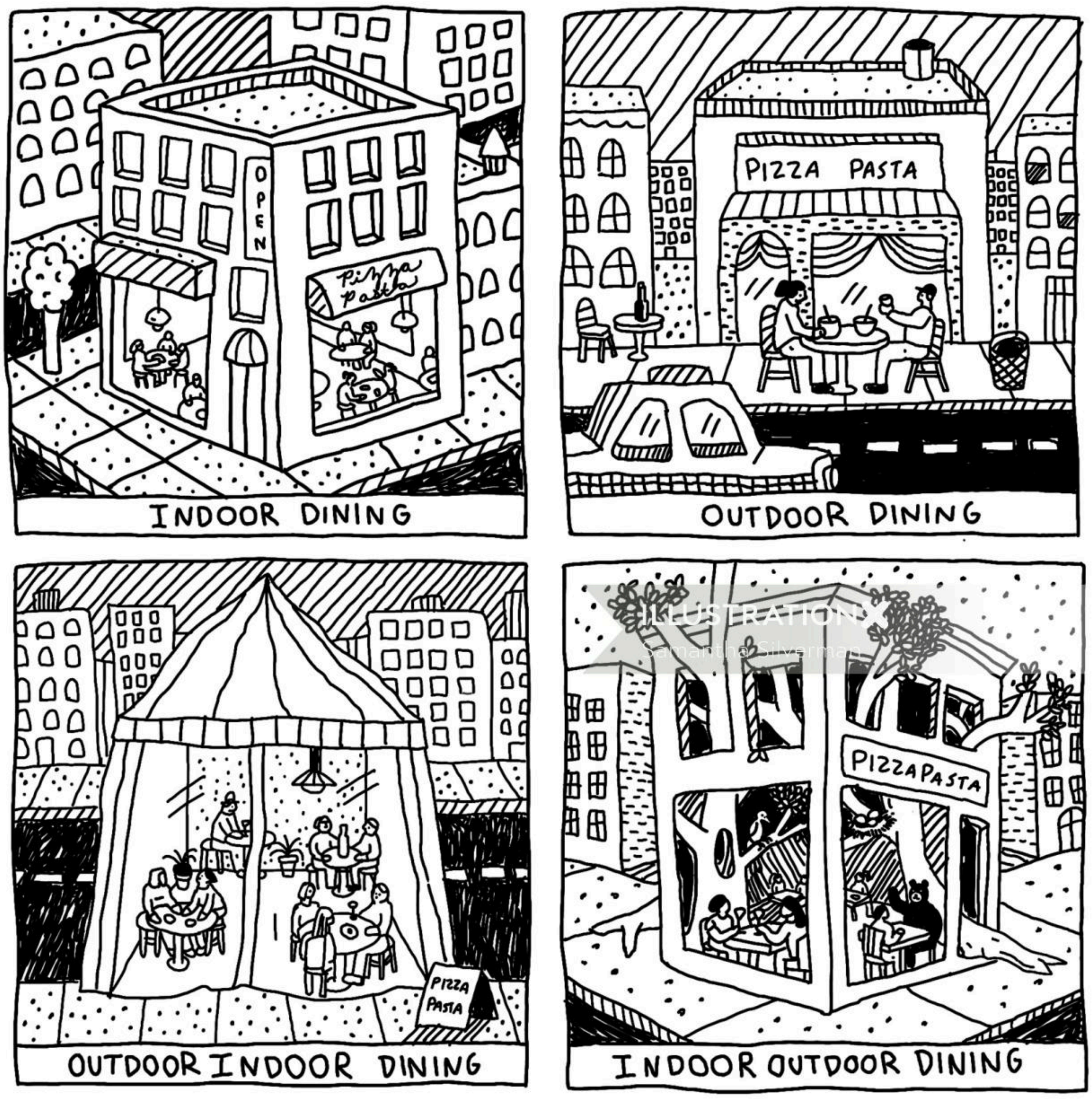

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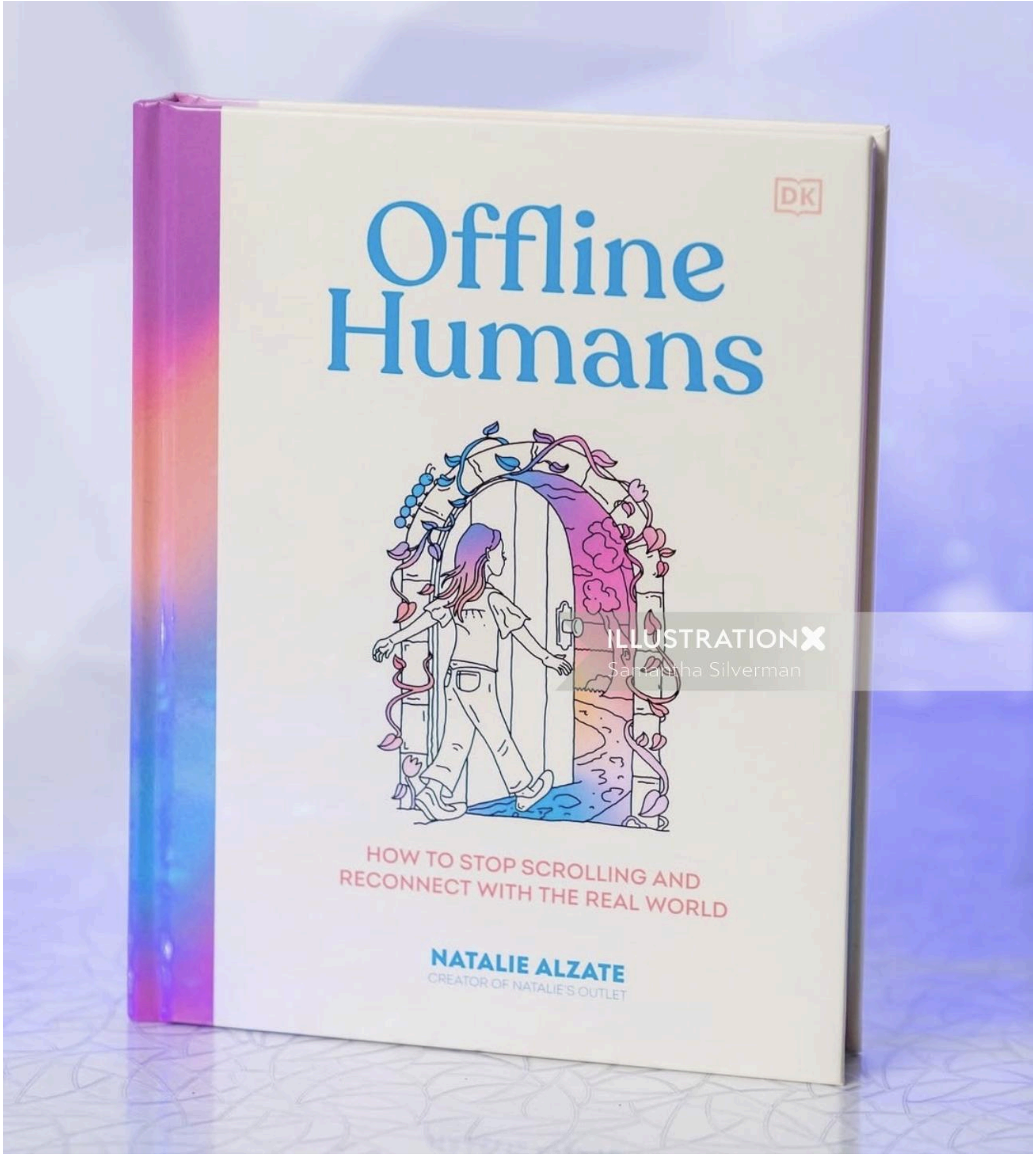

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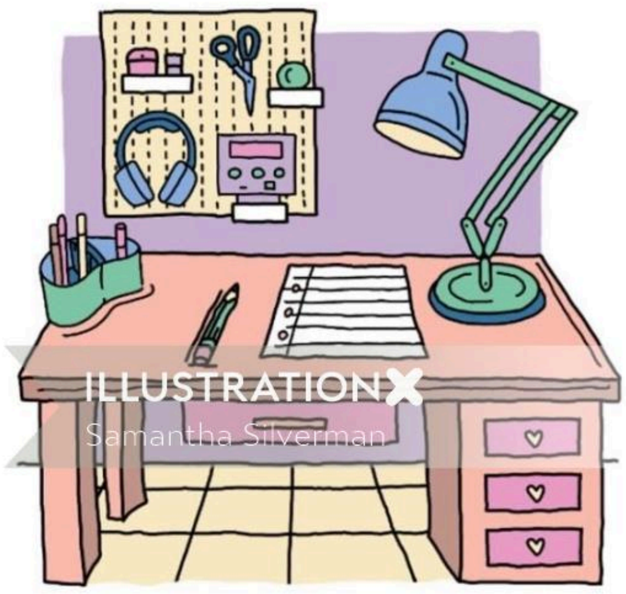

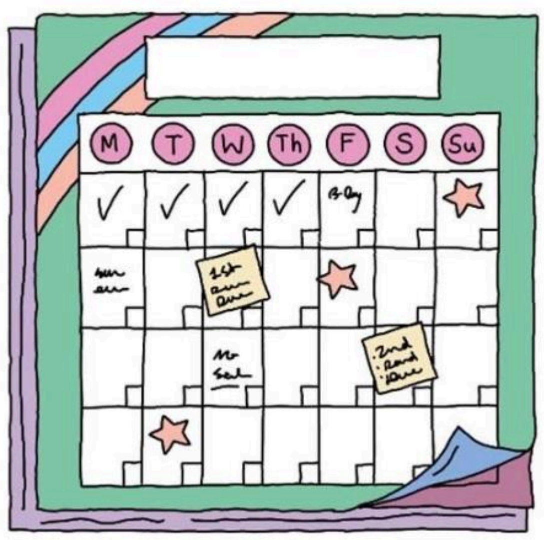

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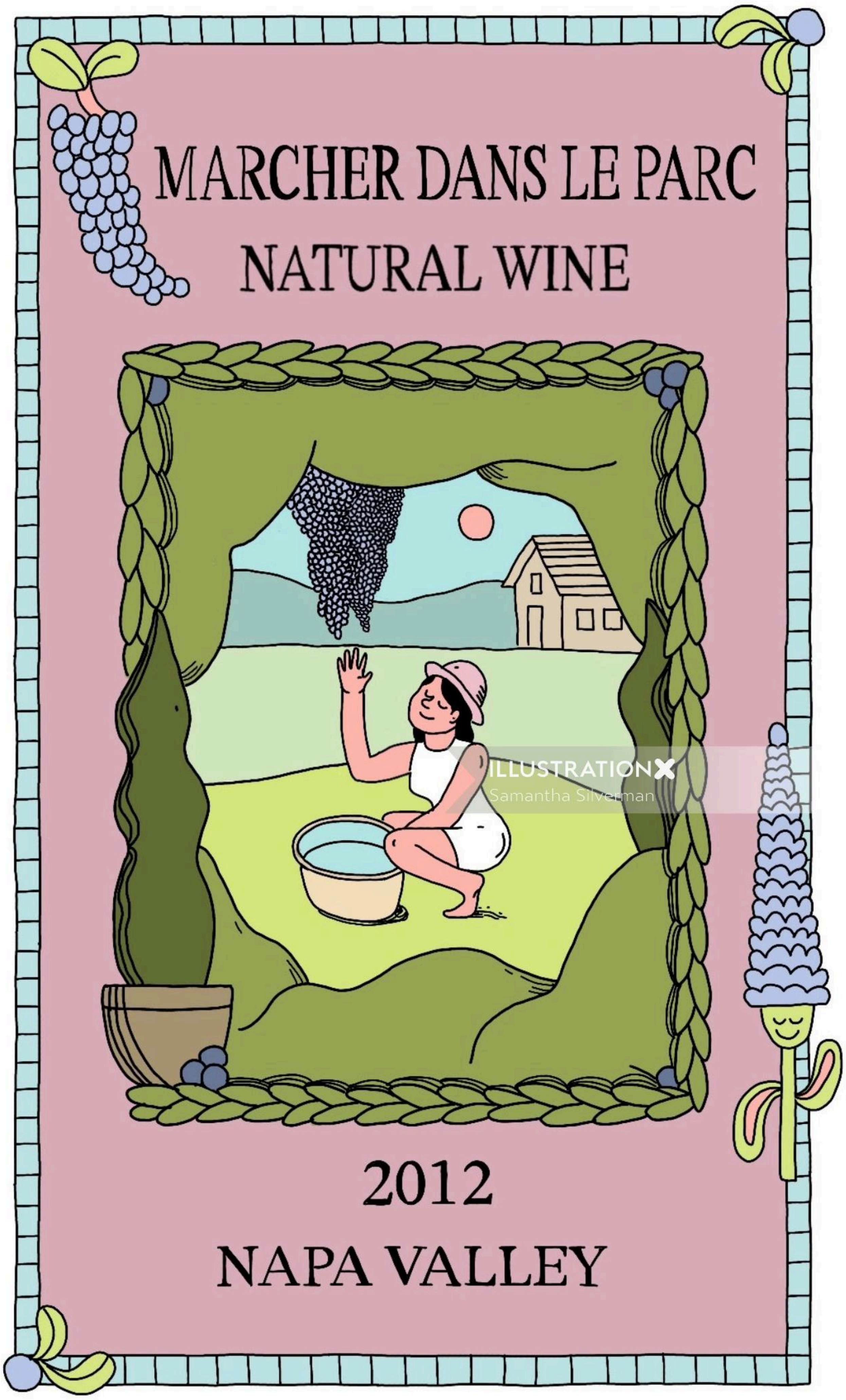

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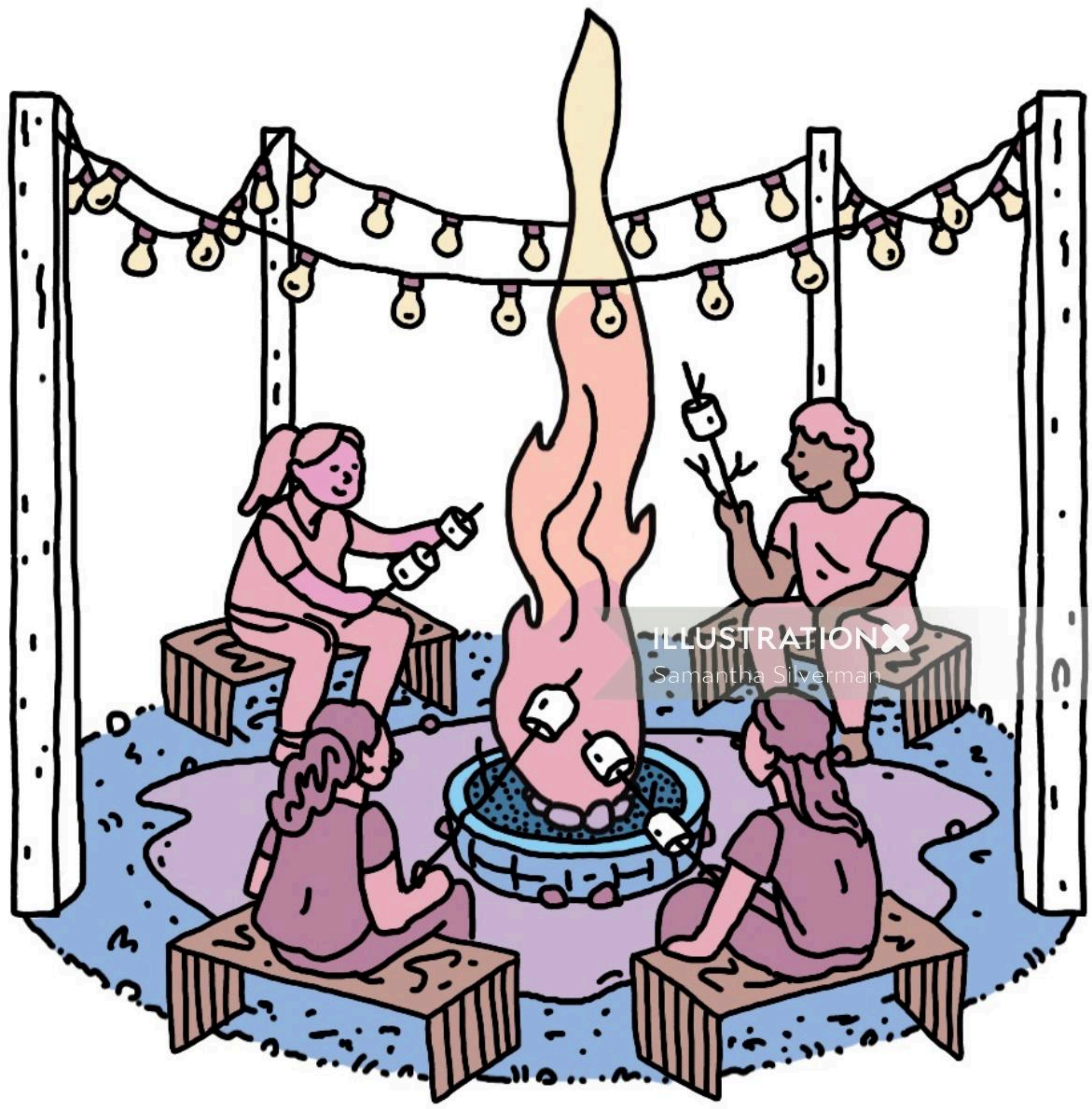

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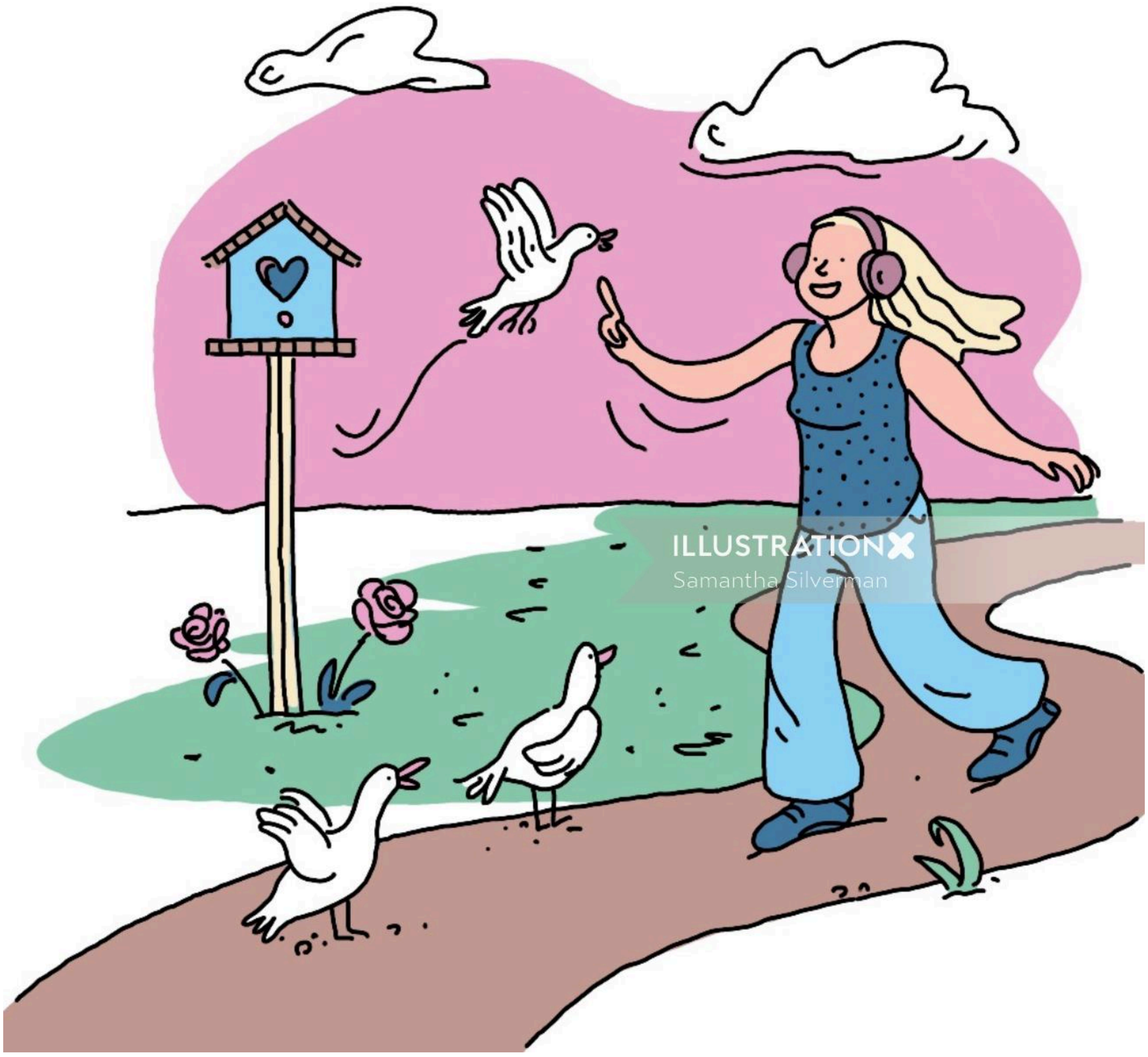

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