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Retirement Solutions, not Products

Mitigating risks in the drawdown phase of retirement

LGIM America

RETIREMENT FOCUS IS MOVING FROM ACCUMULATION TO DECUMULATION

The focus within the defined contribution ecosystem continues to shift from the wealth accumulation (pre-retirement) timeframe to the wealth decumulation (post-retirement) timeframe. To judge trends more adequately in today's DC space, we examine the perspectives of key stakeholders.

From the participant perspective, research shows that 82% of respondents expect to draw down from their employer's retirement plan as a source of retirement income.[1] Similarly, 83% of plan sponsors now seek to retain participant assets within the DC plan.[2] Sixty-three percent of consultants are currently evaluating new investments specifically designed to offer retired participants diverse options complementary to traditional retirement options. This comes as a result of 80% of the respondents believing current retirement plan options do not sufficiently address retiree needs.[3]

HOLISTIC RETIREMENT SOLUTIONS NEED TO ADDRESS THE FOUR FUNDAMENTAL RISKS PARTICIPANTS ARE FACING

Today, "retirement" in some form is widely expected yet for many remains a persistent cause for concern. With current life expectancies, retirement can realistically stretch into a person's 90s. Better understanding how to financially plan for this unknown has become a priority for American employees. Furthermore, understanding their concerns and the risks they are facing helps us develop holistic retirement solutions that lead us to a goal that may be decades away in a changing and uncertain environment.

It will be imperative that a solution directly addresses the four fundamental risks employees have when it comes to retirement income concerns: ***Investment risk*** (ensuring that the same level of investment care that happens during accumulation also happens throughout their retirement); ***Longevity risk*** (longer life expectancies increase the risk of retirees outliving their assets); ***Liquidity risk*** (employees don't want to surrender all of their assets in case of emergencies); and ***Utilization risk*** (having great options available, but participants are not engaged).

DIVIDING THE UNKNOWN OF RETIREMENT TIMELINE INTO DISTINCT SEGMENTS CAN EASE THE PLANNING PROCESS

As people continue to live longer than any generation has seen, the idea of retirement presents new challenges when planning for the future. The greatest of these challenges is the unpredictability driven by 1) the general effects of aging and 2) how long their retirement will last. To help mitigate this unpredictability, we take a "divide and conquer approach": we divide the retirement planning into two distinct phases—early retirement (from 65-84) and later retirement (after age 85).

COMMUNICATION IS KEY TO DELIVERING THE HOLISTIC RETIREMENT SOLUTION

By the time a participant nears retirement, it has become entirely plausible that the participant has never actually made an active affirmative decision regarding their defined contribution plan. Furthermore, participant engagement markedly begins to ramp up as participants approach retirement age.[4] Recent research shows that older participants are more likely than younger participants to transact within their defined contribution plan.[5] Plan sponsors, recordkeepers and investment managers increasingly must provide the education and support participants desperately need.

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Communications and education must deliver relevant, intuitive information to participants who are looking for answers, particularly those nearest to retirement. Unlike the savings years, when the goal of accumulation is generally universal, the decumulation years feature increasingly diverse participants with heterogenous planning goals.

Today's communication and engagement outreach present a mixed bag of effectiveness. According to EBRI's 2022 Retirement Confidence Survey, participants' views on current efforts pose reason for optimism yet also room for improvement regarding educating participants about savings and distributed income. To effectively drive participant engagement and utilization, a robust communication platform is required, developed from a close partnership and commitment to better education between the investment manager, recordkeeper and plan sponsor. All must play a crucial role when communicating evolving retirement income solutions. Retirement income products must be incorporated as just pieces of the overall solution.

While in no way exhaustive, the below list highlights several requirements for robust participant support:

- **Multi-media:** Participants differ in their preferred communication methods and have moved beyond the paper-digital split.
- **Clear, relevant and concise:** As participants are increasingly busier and attention spans vary, the messages must remain clear, relevant and concise.
- **Filter the information to make it easy:** We have learned the importance of tiering the information sharing to ensure all questions are answered quickly and logically.

FORGED PARTNERSHIPS LEAD TO BETTER COMMUNICATION

The merit of the investment manager remains a central focus for those evaluating retirement income products; we need to be adequately describing the value the specific retirement product can potentially bring. Including a strong communication and education effort remains one of the best ways to reduce participant utilization risk and increase the participant engagement.[6]

WE WANT TO HELP

At LGIM America, we understand plan sponsors' concerns/risks, the importance of segmenting the retirement unknown, and the value of effective communication; we welcome this partnership. We have retirement solutions to help address these evolving needs, including communication and educational support strategies. For more information about this thought paper or LGIM America's retirement capabilities, please contact Jimmy Veneruso at Inquiry.DefinedContribution@lgima.com.

ABOUT LGIM AMERICA

LGIM America (LGIMA) was founded in 2006 with the purpose of helping people achieve their long-term financial goals. We offer a range of strategies to help our institutional clients (corporations, healthcare agencies, non-profit, education, public plans and Taft-Hartley) manage their investment objectives, which can range from market-based alpha-oriented strategies to those that are designed to be more liability-centric, derivative overlays, or indexed solutions. Encouraging a diverse and inclusive environment coupled with a solutions-focused culture allows us to increase our breadth of knowledge and the likelihood of improved client outcomes and stronger financial performance. We have teams of experienced, innovative professionals committed to helping plan sponsors meet their pension promises, managing investment exposures efficiently to seek enhanced returns while mitigating risks, and working to generate returns while making a positive societal difference. For further information about LGIM America, find us at www.lgima.com.

FOOTNOTES

[1] *Retirement Confidence Survey*, Employee Benefits Research Institute, 2022
[2] Callan 2022 DC Trends Survey, Callan LLC
[3] 2022 PIMCO US Defined Contribution Consultant Survey
[4] Clark, Fiaschetti and Gerrans, "The Demand for Advice in Defined Contribution Pensions Plans: Age, Gender and Size-of-Bet Effect. August 2015. https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2551819
[5] Blanchett, David, "What Helped Participants Stay the Course in 2020" February 2022. https://cdn.pficdn.com/cms/pgim4/sites/default/files/PGIM-DC-Solutions-Stay-the-Course-0422.pdf
[6] LGIMA defines utilization risk as the risk after a fiduciary's due diligence and effort to improve outcomes; participants will not use a plan option.