PGIM INVESTMENTS

EXECUTIVE THOUGHT LEADERSHIP

Interview with

David Blanchett

A (More) Personal Retirement

How will emerging trends, regulation, and participant behavior influence the future of retirement income?

Planning for a dependable post-career stream of income has always been challenging for American workers, and never more so than in the aftermath of the COVID-19 pandemic, alongside renewed concerns about inflation, volatile markets, and uncertain job markets. At the same time, there are fresh thoughts – and some exciting new developments – around retirement income.

We sat down with David Blanchett, Managing Director, Head of Retirement Research for PGIM DC Solutions, the Retirement Solutions Provider of PGIM, for some insights.

NNTM: WHAT ARE SOME OF THE FORCES OR EMERGING TRENDS EXPECTED TO SHAPE THE FUTURE OF RETIREMENT THAT PLAN ADVISORS, CONSULTANTS, AND PLAN SPONSORS SHOULD BE PAYING ATTENTION TO?

BLANCHETT: I think the biggest focus going forward will be on keeping participants in the plan post-retirement. Helping participants get through retirement is a different perspective than getting to retirement and I think it requires plan sponsors to rethink their approach to the defined contribution (DC) plan. While existing strategies work reasonably well for younger participants, they are less optimal for older participants, whose varying needs and expectations generally require increased personalization. While there is some regulatory focus on increasing access to longevity-protected income solutions in DC plans, such as annuities, and an acknowledgement that these solutions can provide value, it's important for plan sponsors – and those who support them – to make sure they've done everything else to make the DC plan "retirement friendly" before going down the route of simply adding an annuity option. I think the benefits of keeping participants in the plan post-retirement could be especially strong for mass affluent participants who may not have access to high quality advice outside the DC plan.

NNTM: WHAT'S STANDING IN THE WAY OF THAT FOCUS?

BLANCHETT: I'm not convinced that core menus are designed today with an eye toward participants who actually use them. Younger participants overwhelmingly tend to rely on prepackaged investment strategies such as target-date funds (i.e., the default investment) while older participants – whose participation often predates the advent of default investment alternatives – continue to gravitate towards the core menu. Therefore, I think it's essential that core menus are designed to give participants an opportunity to build a well-diversified portfolio that can be optimized to fund the retirement liability. This objective requires access to certain asset classes, especially real assets, which are still relatively uncommon in core menus today.

NNTM: WHAT ABOUT QUALIFIED DEFAULT INVESTMENT ALTERNATIVES AND THEIR ROLE IN IMPACTING RETIREMENT OUTCOMES?

BLANCHETT: I think default investments have definitely resulted in significantly improved investment outcomes for DC participants compared with self-direction, although I still think we have a way to go as an industry. For example, target-date funds typically differentiate allocations based entirely on age, though plan sponsors and recordkeepers increasingly have an expanded amount of information available on employees/participants age such as income, balance, savings rate, gender, etc., that can be used to design more personalized portfolios that are more appropriate for participants.

NNTM: YOU MENTIONED EARLIER THAT OLDER WORKERS TEND TO GRAVITATE TOWARD CORE MENU OPTIONS RATHER THAN TARGET-DATE FUNDS. IN VIEW OF RECENT MARKET VOLATILITY, WHAT ARE THE IMPLICATIONS?

BLANCHETT: One thing I've found in research, focusing on both the global financial crisis and the more recent market decline in 2020, is that older participants tend to trade more during times of heightened market volatility. This is somewhat counterintuitive, since older investors would generally be described as more sophisticated and experienced, but I think the importance of retirement nearing results in higher trading activity. To me, this suggests it's especially important to get older participants in some type of professionally managed portfolio. One problem, though, is older participants are the most likely to self-direct their accounts. Therefore, it's especially important to design solutions that are attractive for older participants, which can help them stay the course during periods of heightened volatility.

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NNTM: GIVEN THOSE COMMENTS, WHAT TRENDS DO YOU SEE EMERGING OR GATHERING STEAM SPECIFIC TO TARGET-DATE FUNDS, AS WELL AS DEFAULT INVESTMENTS IN GENERAL?

BLANCHETT: I think default investments need to evolve and become increasingly personalized. I really like target-date funds; it's just hard for me to think the truly optimal portfolio is identical for everyone within a five-year age cohort. Personalization is becoming increasingly common throughout multiple domains in our lives; I think this also needs to take place in DC plans. For now, I like the idea of hybrid (or dynamic) default investments, where older participants are defaulted into a more personalized solution, like managed accounts, while younger participants are defaulted into target-date funds.

NNTM: LET'S TALK ABOUT RETIREMENT INCOME SOLUTIONS. ARE THERE ANY RECENT CHANGES THAT WILL MAKE THEM MORE ATTRACTIVE?

BLANCHETT: Definitely. From a regulatory perspective, there have been changes that make annuities more attractive in DC plans. On the legislative front, the SECURE Act contained several provisions designed to both help participants better conceptualize the realities of retirement income, as well as lower some of the perceived barriers to plan sponsor adoption of those solutions. While I applaud the changes, I see annuities as the "endgame" when it comes to helping participants achieve a better retirement outcome, and that many plans should focus on other things to make their DC plan as "retirement friendly" as possible before going down the annuity route, such as allowing partial withdrawals, offering retirement-friendly core menus, and getting more participants to delay claiming Social Security retirement benefits.

NNTM: PGIM HAS BEEN TALKING ABOUT A "NEEDS/WANTS" FRAMEWORK AROUND RETIREMENT SPENDING FOR THE PAST FEW YEARS. CAN YOU DESCRIBE WHAT THIS IS AND HOW IT'S DIFFERENT?

BLANCHETT: I think a notable shortfall among most retirement income strategies is that they tend to assume the retiree spending goal is effectively a single static goal that is increased every year in retirement by inflation without any other considerations. In reality, the retirement spending goal should be viewed a as series of goals with varying levels of flexibility – what academics tend to call elasticity. Matching spending flexibility with retiree assets, which include pension benefits and savings, can result in notably different, and arguably more personalized, guidance and advice.

NNTM: HOW CAN RETIREMENT INCOME SOLUTIONS HELP DRIVE BETTER OUTCOMES FOR PARTICIPANTS?

BLANCHETT: Retirement finance is incredibly complex. Each retiree has their own unique situation and preferences, and I think it's really important that any type of retirement income solution incorporate this information. There are myriad unique decisions retirees have to make, like when to claim Social Security retirement benefits, how to invest the portfolio, how much can be withdrawn from the portfolio, etc., that are incredibly complicated – and often irreversible. Providing access to advisors or advice solutions can help retirees make more informed decisions and result in better retirement outcomes. NNTM

Note: Additional PGIM research and thought leadership perspectives can be found at pgiminvestments.com/DCIO.

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