



Keeping Promises

A View of the US Experience

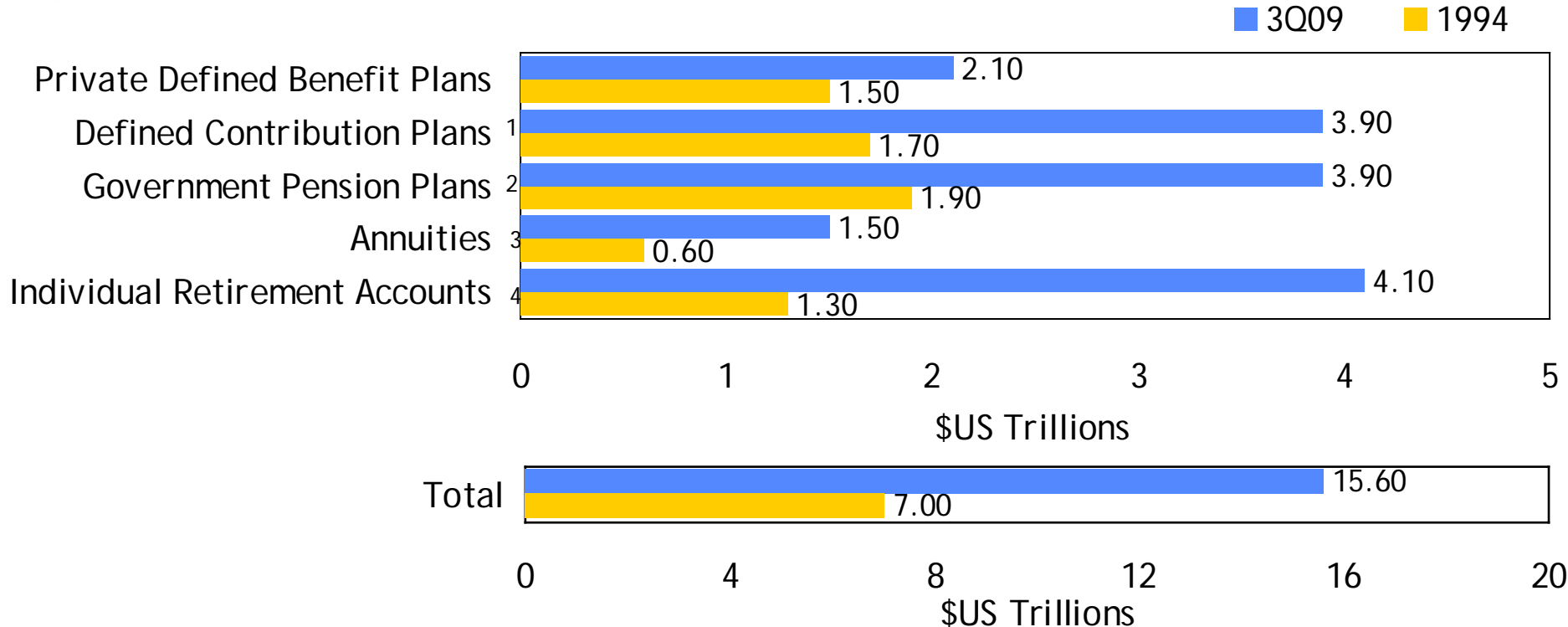
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US Retirement System

Long Term Shift From Defined Benefit to Defined Contribution



¹Defined contribution plans include private employer-sponsored defined contribution plan (including 401(k) plan), 403(b) plan, and 457 plan assets.
²Government pension plans include federal, state, and local pension plans. Federal pension plans include U.S. Treasury security holdings of the civil service retirement and disability fund, the military retirement fund, the judicial retirement funds, the Railroad Retirement Board, and the foreign service retirement and disability fund. These plans also include securities held in the National Railroad Retirement Investment Trust and Federal Employees Retirement System (FERS) Thrift Savings Plan (TSP).
³Annuities include all fixed and variable annuity reserves at life insurance companies less annuities held by IRAs, 403(b) plans, 457 plans, and private pension funds (including 401(k) plans).
⁴Estimated
 Source: Investment Company Institute, The US Retirement Market, Third Quarter 2009, Federal Reserve Board, National Association of Government Defined Contribution Administrators, American Council of Life Insurers, and Internal Revenue Service Statistics of Income Division
 Note: Components may not add to the total because of rounding.





Pension Protection Act of 2006

The Act and Its Implications

Pension Protection Act of 2006 – Defined Contribution Elements

- Qualified Default Investment Alternative

Investment fund or model portfolio designed to provide both long-term appreciation and capital preservation through a mix of equity and fixed income exposures. Options include

- Target Date Fund
- Balanced Fund (including Target Risk)
- Managed Account

Implications

- Auto-enrollment
- Auto-escalation
- Move from member to professional asset allocation



Defined Contribution Experience in the US



What Has Not Worked

Opt In

Target Risk

Participant
Investment Education



What Has Worked

Opt Out

Target Date

Bundling Investment
Solutions



What We Can Do Better

Income

Managing Volatility

Auto Escalation



US Defined Contribution Market

What Has Not Worked

Opt in – low participation rates of Defined Contribution plans in the 1970s – 1990s

- Delay taking action
 - I'll save next year
 - Defined Contribution plans don't work
-

Member directed investment menu

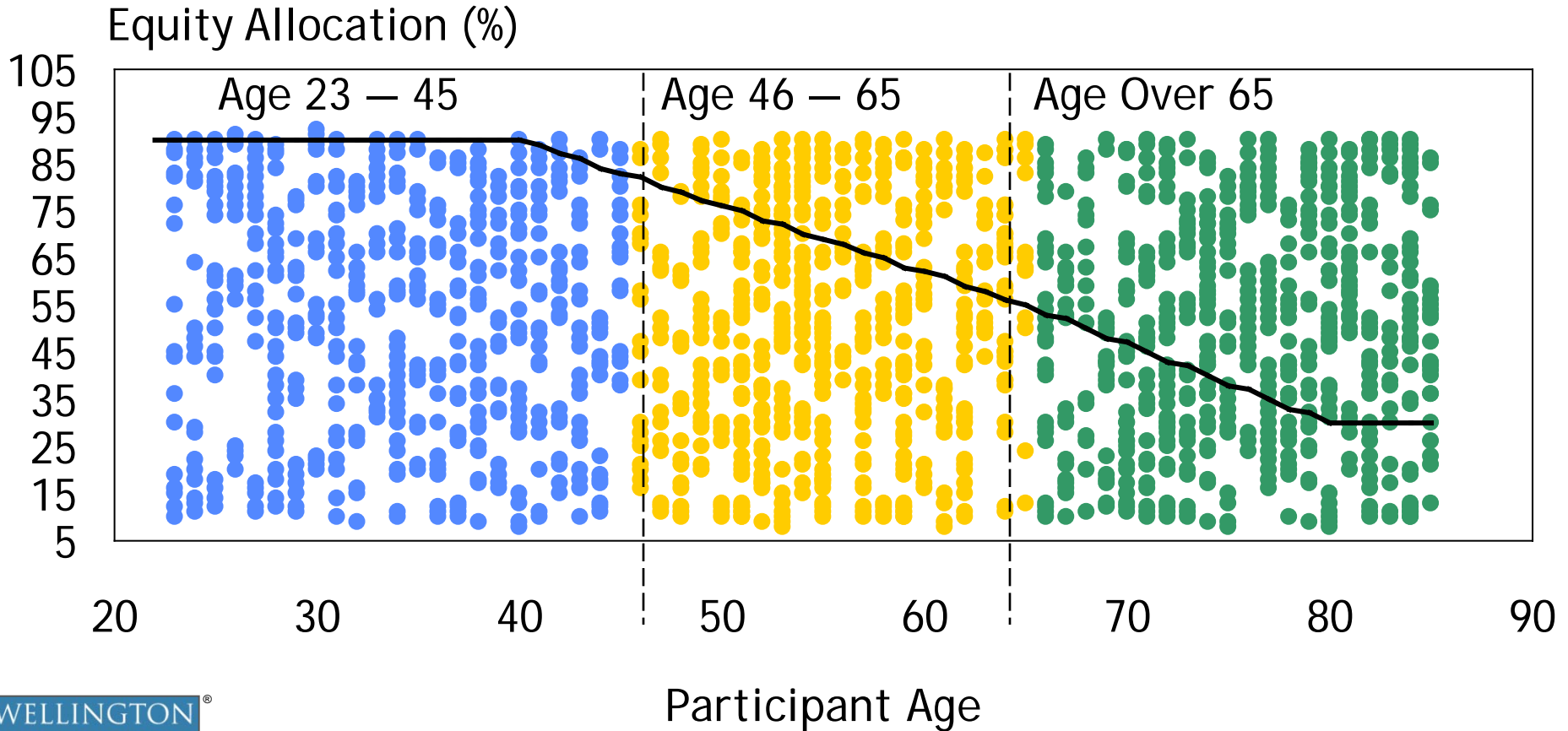
- Great presentation – but what should I do
 - The scatter plot – equity versus age
-

Target risk – low utilization

- What color is my parachute
- What day is it, what time is it
- When did I grow old



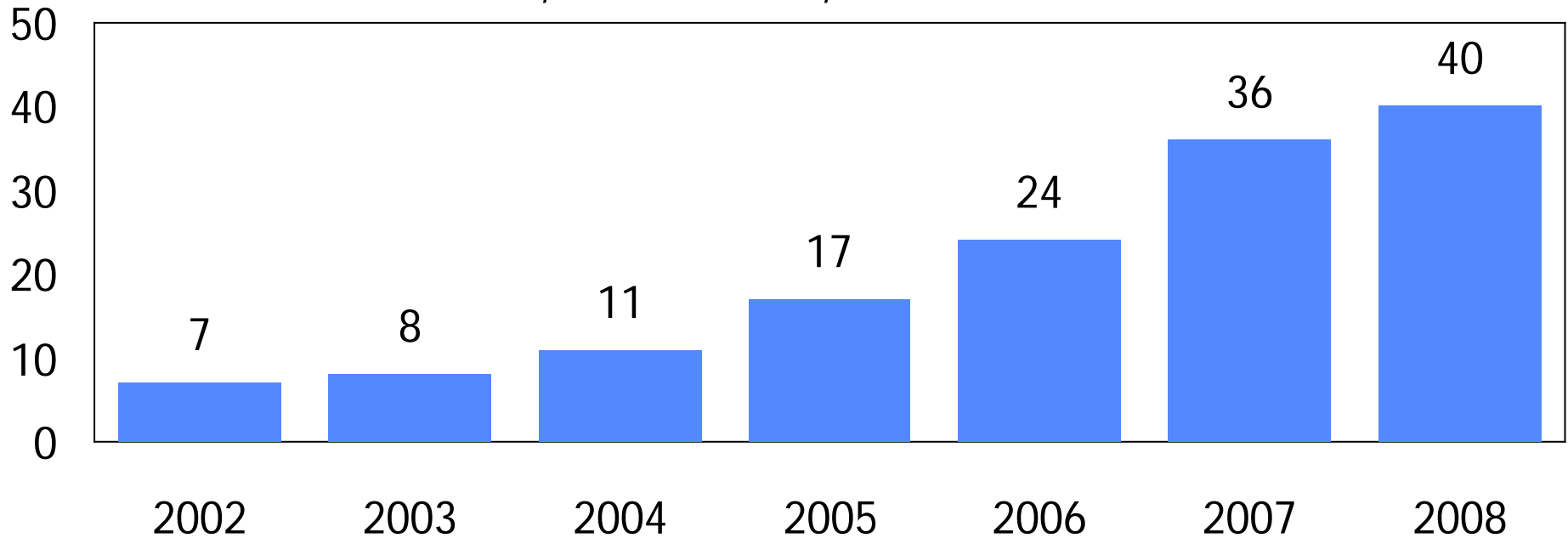
Illustrative Member Allocation





US Defined Contribution Market Automatic Enrollment Just Beginning to Catch on

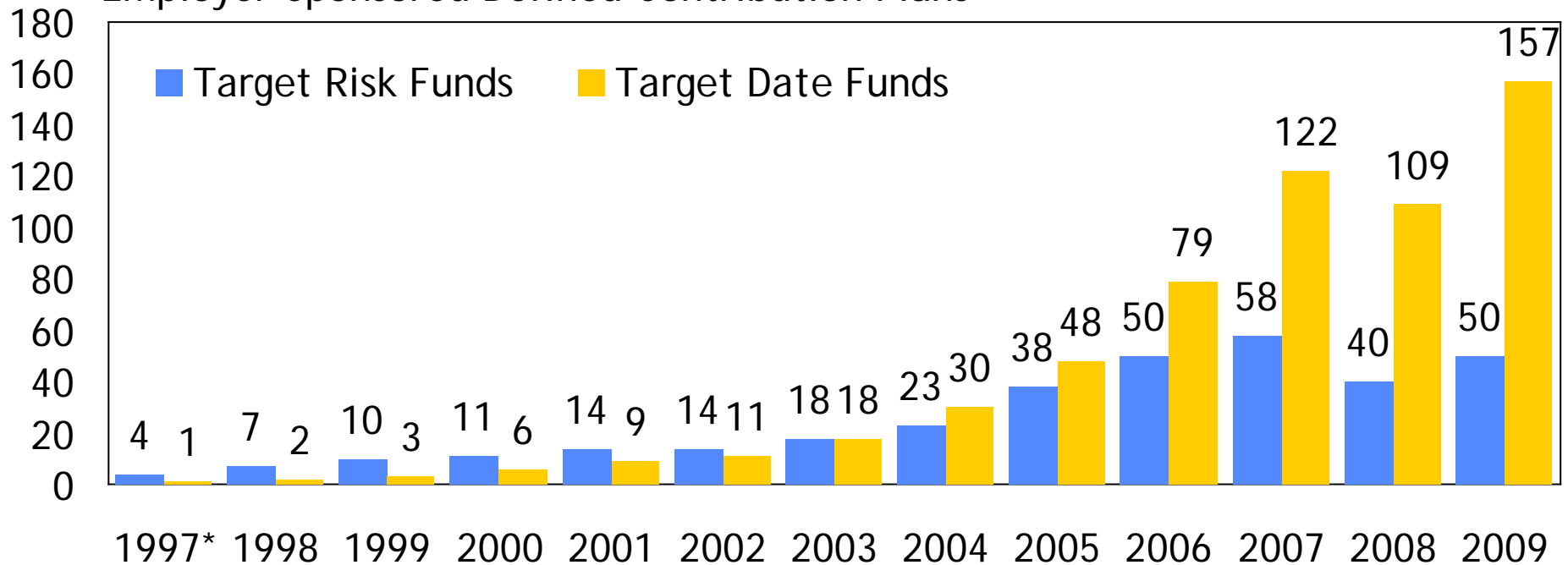
Percent of Defined Contribution Plans Implementing
Automatic Enrollment, 2002 – 2008, Percent





US Defined Contribution Retirement Market Target Date and Target Risk Fund Assets Continue to Grow Rapidly

Target Date and Target Risk Fund Assets Employer-Sponsored Defined Contribution Plans



*In 1997 target date assets were less than \$1 billion.

Note: a target risk fund maintains a predetermined risk level and generally contains "conservative," "aggressive," or "moderate" in the fund's name. A target date mutual fund is a hybrid fund that typically rebalances to an increasingly conservative portfolio as the target date of the fund (mentioned in its name) approaches.

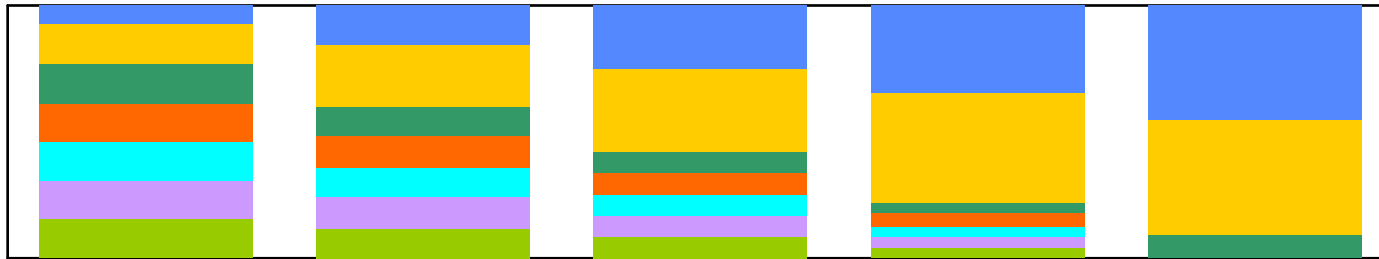
Source: Investment Company Institute; Research Fundamentals June 2009



US Defined Contribution Market

The New Standard in Plan Design

Tier 1: Target Date

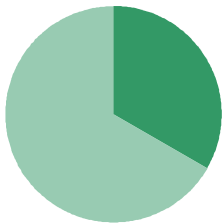


Funds get more conservative as they draw closer to retirement

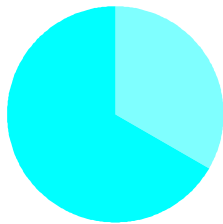
Age →

Tier 2: Core (Passive/Active Blend)

Large Cap



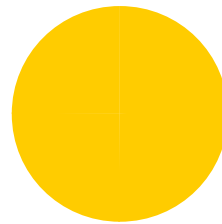
Small Cap



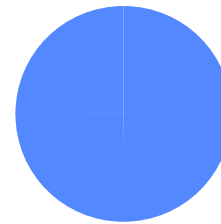
International



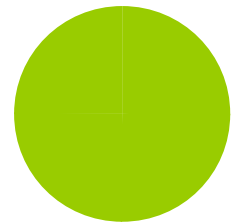
Bond/Income



Money Market/
Stable Value



Non-Core



Tier 3: (Optional) Self-directed brokerage account or mutual fund window



US Defined Contribution Market DC Plan Design Trends

Ten Years Ago

Self-direction



Today

Target date and
member advice

Mutual funds



Commingled pools and
separate accounts

Pension
administrator only



Multi-manager

Core assets



Some non-core assets



US Defined Contribution Market

What Has Worked

Opt out

- Few Defined Contribution members reverse their participation status and opt out suggesting that most employees do not object to saving for retirement*
-

Target date

- 39% CAGR over 6 years**
-

Combining menu options to simplify core

- Value + Core + Growth
- Small Cap Capitalization + Mid Capitalization
- Barclays Aggregate + High Yield + Emerging Markets Debt
- Inflation Linked Bonds + Commodities + Precious Metals + Natural Resource Related Equities

*Choi, Laison, Madrian, and Metrick (2001)

**Investment Company Institute; US Retirement Market Third Quarter 2009



US Defined Contribution Market What We Can Do Better

Improved savings rates – auto escalation
and higher default rates

Managing volatility to smooth member
experience

Income – annuities

- Guaranteed Minimum Withdrawal Benefit
- Deferred Annuities for Longevity



US Defined Contribution Market

Pension Protection Act: Plan Design

Plan design a sponsor/trustee can implement to avoid non-discrimination testing

Automatic enrollment at 3% minimum AND

Auto escalation at 1% per year, with resulting member contribution minimum of 6% and maximum of 10%

AND

Employer matching contribution formula of 100% of 1st 1% and 50% of next 5% of member contributions OR

Employer non-elective contribution of 3%



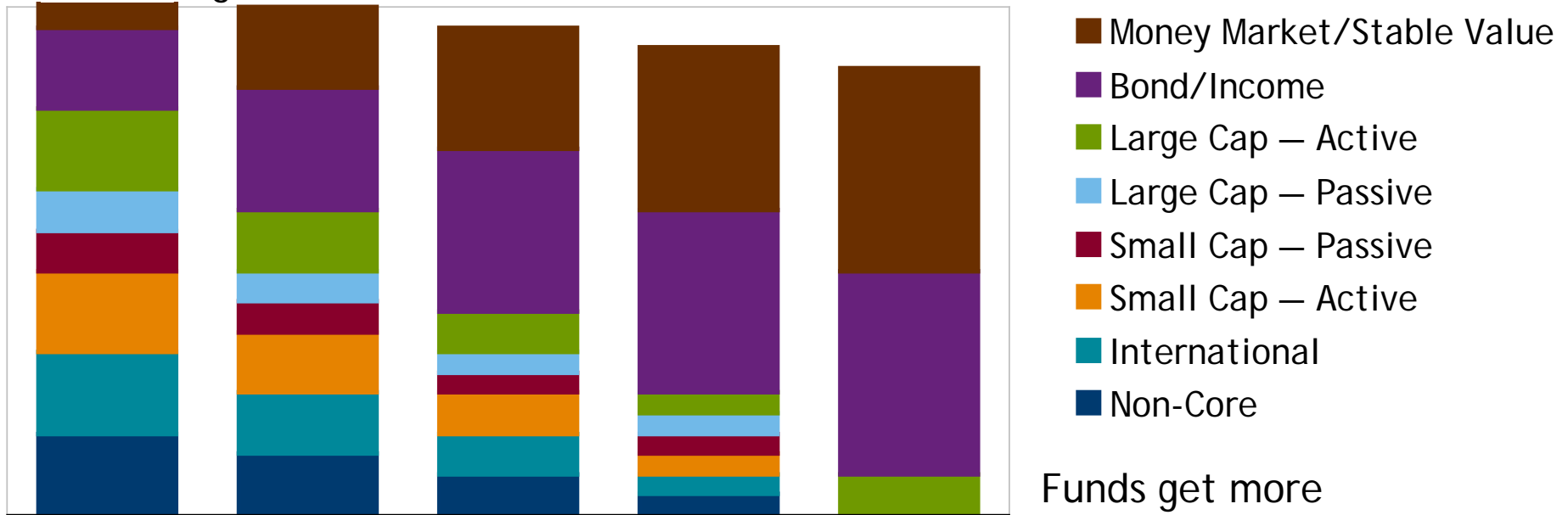
US Defined Contribution Market Investment Line Up — Future Asset Allocation

- ↓ Stable Value
- ↓ Company Stock
- ↑ Inflation-Linked Bonds
- ↑ High Yield
- ↑ Emerging Markets Debt
- ↑ Emerging Markets Equity
- ↑ Non-US Equity
- ↑ Real Estate
- ↑ Commodities



US Defined Contribution Market Future Plan Design: The Ultimate End Game?

Custom Target Date



Age →
Mutual Fund Window

Funds get more conservative as they draw closer to retirement



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Thank You

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