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In this Issue

Transforming Tomorrow: Awakening the Super Saver

By Randy Myers

Stig Nybo has spent most of his career promoting best practices for qualified retirement plans, but his commitment to that task took a more personal and passionate turn about four years ago. The catalyst was an incident that occurred during a simple walk through a parking lot with his two young sons. En route to their car, they passed an elderly woman who got out of an old Volvo, folded a blanket, and placed it inside the trunk of her car—a car filled with personal belongings. Nybo recognized that the woman was living in her car, and he had a long and ultimately unsatisfactory conversation about the incident during the ride home with his sons. The conversation was unsatisfactory, he explains, because he couldn't point to the usual culprits for the woman's circumstances: vagrancy, for example, or drug addiction. "In fact, when I looked at this woman, she reminded me of my own mom, who is comfortably retired."

It was at that point, Nybo told participants at the 2013 SVIA Fall Forum, "that I realized

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Dodd Describes His Work on Signature Bill as Once-in-a-Lifetime Opportunity

By Randy Myers

Former U.S. Senator, Christopher Dodd

Groundbreaking legislation generally springs from extraordinary circumstances. In the case of the far-reaching Dodd-Frank Wall Street Reform

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Stable Value Seen Outperforming Other Fixed-Income Sectors in Rising Rate Environment

By Randy Myers

Rising interest rates are generally bad for fixed-income investments, but perhaps not as bad for stable value funds as for some other short-term sectors of the bond market.

Researchers at New York Life Investment Management recently looked at how six different asset classes have performed in the past during periods of steadily rising interest rates and modeled how they might perform during a four-year period of rapidly rising rates.

In those models, U.S. equities generated the highest returns by far—about 9 percent annually, on average, said Michael Sipper, director of stable value investments for New York Life Investment Management, speaking at the 2013 SVIA Fall Forum. The next best performing asset classes were high-yield fixed income and international equities, both generating average annual returns of about 5 percent. Stable value funds followed with performance a little under 5 percent annually, then 3-month Treasury bills (a proxy for money market funds), then long-term bonds, and finally intermediate-term bonds.

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Dodd's Once-in-a-LIfetime Opportunity

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and Consumer Protection Act of 2010, the extraordinary circumstance was the worst financial crisis since the Great Depression, a debacle that cost the U.S. trillions of dollars, millions of jobs, millions of homes lost to foreclosure, and the failure of some of the nation's biggest financial institutions.

The 2008 credit crisis that triggered the 2008-2009 recession was not an accident, former Senator Chris Dodd told participants at the 2013 SVIA Fall Forum. Rather, he said, it was a consequence of an outdated banking regulatory system that had its roots in the 19th century. He reasoned at the time that if such a crisis could happen once, it could happen again—absent a major overhaul of the regulatory regime.

But a major overhaul would not be easy. Over the prior 60 years, most financial industry reforms had been incremental in nature, and the nation seemed to have little appetite for major change. But after the credit crisis, Dodd said, "the question was, are we going to just move on and assume that the world as it existed in 2007 and 2008 didn't need to be reviewed?" His answer was "no."

"You need to move at certain moments legislatively; the window is only open at certain times," he said. "You never could have passed anything like this bill in 2005, 2006, or 2007, and you couldn't have passed it today."

As chairman of the Senate Banking Committee (he's now chairman and CEO of the Motion Picture Association of America), Dodd began working with Barney Frank, then chair of the House Financial Services Committee, to try to construct a financial architecture that would be more reflective of the 21st century. They were spurred to action in part, Dodd said, by the release in April 2008 of reform recommendations from the Group of Twenty, which includes finance ministers and central bankers from 19 countries plus the European Union. "I felt it was critically important that the U.S. lead," he said. "If we didn't act, someone else would, and we would be playing by somebody else's rules, not ours."

The bill that Dodd and Frank drafted was not perfect, Dodd conceded, noting that it included some provisions that he didn't like but that were necessary to win support from a sufficient number of legislators for passage. But he said he believed that passage was critical, and that he did not want perfection to be the enemy of the good. The resulting legislation was widely recognized as the most far-reaching since the reforms that followed the Great Depression. Among other things, it created stronger capital and liquidity standards for financial institutions, imposed new regulations on derivatives, and created new protections for American consumers against predatory lending practices. Most importantly, Dodd said, it helped restore faith in the U.S. financial system.

As originally written, many in the financial services industry worried that the Dodd-Frank Act's regulations pertaining to derivatives trading might be construed to include stable value contracts. Dodd noted that Congress inserted language in their bill requiring regulators to study that issue, and gave them authority to conclude that stable value contracts are not derivatives, or, in the language of the legislation, "swaps." Further, the bill said that if regulators conclude that stable value contracts are swaps, they have authority to exempt them from the new regulations. Regulators have not yet completed that study, but the stable value industry has consistently maintained that stable value contracts are not derivatives. Until regulators complete the study and make a final ruling, the contracts remain exempt from the new regulations. SVIA

Awakening the Super Saver

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our business is not about fiduciary responsibility, although certainly that is an important part of it. It's not even about stable value. What it's about is making sure people have enough to retire on. And the fact is, that's an area where we're simply failing. By we, I mean all of us, collectively, as a society. We have not formed the habits that will get us to where we need to get. And unless we go to an additional mandatory (savings) system, like an additional Social Security system where people have no choice, we're going to have to do better with a voluntary system."

Since that day, Nybo, president of pension sales and distribution at Transamerica Retirement Solutions, has become an emphatic proponent of encouraging Americans to save more for retirement, even going so far as to author a book with writer and consultant Liz Alexander, entitled *Transform Tomorrow: Awakening the Super Saver in Pursuit of Retirement Readiness* (John Wiley & Sons, 2013). He has pledged that any profits from the book will be donated to a public service campaign to promote retirement saving.

Speaking at the SVIA Fall Forum, Nybo said three issues go a long way toward explaining why many Americans have not saved enough for a financially secure retirement: longevity, consumerism, and leverage. Americans are living longer, they spend voraciously, and they rely extensively on debt to finance their spending.

To combat these problems, Nybo wants to create a nation of "super savers." Some of these people already exist. In the 12th Annual Retirement Survey conducted by the Transamerica

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Center for Retirement Studies in 2011, Nybo said, about 20 percent of those polled had built spending and savings habits that would afford them a financially secure retirement. These people were not characterized by exceptional educational levels or earnings, but rather by giving priority to consistent saving.

The lesson, he said, is simply that it is possible for many people to save adequately. And they have the tools to do it, he insists, in the form of defined contribution plans like the 401(k). While it is customary to complain that the 401(k) plan is failing the retirement needs of Americans, Nybo said some of the numbers frequently cited to support that argument are misleading. For example, data from the Employee Benefit Research Institute indicate that the average 401(k) account balance is about $60,000. But that doesn't take into account the fact that many people have access to more than one 401(k) account, including some domiciled with former employers, and to IRAs and accounts held by spouses. In fact, he said, the average accumulated total retirement assets for people over age 60 in 2010, including traditional and rollover IRAs, was about $275,000. "And I believe it is well over $300,000 now, which is still insufficient," he noted. He added that participants currently are deferring 3 percent of salary into their plans (in line with what companies typically match), but that it should be 6 percent. Additionally, he said, auto-escalation is 1 percent per year, but should be 2 percent.

Still, given the projected cost of healthcare alone in retirement, it's clear that most Americans need to save more. In searching for ways to change their behavior, Nybo said he and Alexander were inspired by previous public service campaigns that had successful outcomes. Among these was an anti-littering campaign launched in 1971 that was spearheaded by a television ad featuring a Native American with a tear in his eye as he surveyed scene after scene of littering. Surveys indicate that from 1969, just before the ad's launch, to 2009, littering in the U.S. decreased by 61 percent.

It turns out, though, that littering didn't go down just because people were advised to stop doing it, but also because communities made it easier for people not to litter by making waste receptacles much more widely and readily available—much the way automatic enrollment in 401(k) plans make retirement savings more widely and readily used.

Nybo is pushing the financial services industry to launch a public service campaign that will rival the successful anti-littering campaign that started in 1971. He is also promoting financial literacy classes in the nation's high schools. The consequences of failing in these efforts would go beyond financially difficult retirements for older Americans, he warned, since their reduced spending power would also harm the country's consumer-driven economy.

"It's a massive issue, the biggest social issue of our time, and it's our responsibility," Nybo told his SVIA audience. SVIA

Attendees at the Stable Value Investment Association Fall Forum 2013

Stable Value: Challenges and Opportunities

By Randy Myers

By almost any objective measure, the stable value industry is doing well. From 2000 through 2012, assets in stable value funds increased significantly to an all-time high of $701 billion. This represents about 14 percent of the $5.1 trillion of assets in defined contribution plans at the end of that period. Stable value wrap capacity, which became constrained following the 2008 credit crisis, has rebounded. A survey conducted in 2012 indicated available wrap capacity of about $100 billion, and year-to-date industry sales statistics support that finding.

But while stable value remains "the safe asset class of choice," the industry cannot become complacent, James J. King Jr., chairman of the Stable Value Investment Association, said in his opening address to the 2013 SVIA Fall Forum, Putting Together the Pieces of a Financially Secure Retirement. Target-date funds continue to gain market share in the defined contribution plan marketplace, for example, and from a modest start in 2008 have grown to more than $500 billion in assets as of the first quarter of 2013. Yet stable value funds are sparsely represented in those investment vehicles. More recently, a number of financial services firms have introduced guaranteed income products for the defined contribution plan market, and while sales have been modest so far, they represent another type of protected investment that could compete with stable value.

"Our challenge is not only to keep our market share, but to grow it," King told his audience. "And to grow it, we're going to need to be creative, we're going to need to be adaptive, and we're going to need to react effectively to changing conditions." As part of that effort, he said, stable value providers will have to work with others in the defined contribution industry to encourage retirement plan participants to save enough money for retirement.

"The defined contribution industry is in competition for savings dollars," explained King, who is also managing director and senior client

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The Big Picture: Trends in Defined Contribution Plans

By Randy Myers

From the left: Elizabeth Heffernan, Fidelity Employer Services Company; Sara Richman, Great-West; Philip Maffei, TIAA-CREF

Investors in 401(k) plans may not be saving enough for retirement, on average, but they're saving more than headline numbers would suggest.

In a wide-ranging panel discussion at the 2013 SVIA Fall Forum, Elizabeth Heffernan, vice president of investment product management at Fidelity Investments, said the average account balance in plans for which Fidelity provides recordkeeping services is about $80,000. But that figure has been depressed, she observed, by the trend among plan sponsors to adopt automatic enrollment policies. Automatic enrollment brings into their plans new participants with very low account balances.

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portfolio manager in the Stable Value Markets Group for Prudential Retirement. "And it's tough competition. We're looking at competing against paying the bills, buying a new car, the apartment with a balcony. There's also a significant amount of participant inertia to overcome."

To address the issues, King said the retirement industry must continue to embrace the use of automatic features in defined contribution plans, including automatic enrollment of workers, automatic escalation of participant contributions, and automatic rebalancing of their portfolios so as to maintain an appropriate asset allocation mix over time.

"We need to address the needs of our Millennials, who actually outnumber Baby Boomers and think very differently," King said. Millennials, the generation born between roughly 1985 and 2000, are hyper-connected, fully-integrated, and socially-networked. A recent survey sponsored by Merrill Lynch concluded that Millennials take nothing at face value and want to remain in the driver's seat when it comes to investments, among other things. "So hopefully SVIA's recent forays into social media, specifically LinkedIn and Twitter, will help to educate this important cohort about the benefits of stable value," King said. "The industry must continue to educate and inform fiduciaries and policy makers, too, to ensure that they understand the asset class."

The industry also needs to get involved with target date funds, King said. "Stable value can be an allocation in customized target-date funds," he argued. "It is important for the asset class to grow with those funds. We have the ability to compete in that space." According to Morningstar, target date funds grew from about $157 billion in 2008 to $508 billion in the first quarter of 2013, and retirement industry consensus suggests this is a trend that will likely continue.

King encouraged stable value providers to continue working to increase penetration in defined contribution plans that don't currently offer stable value, as well as in 529 tuition assistance plans. Current market conditions should help in that effort, he added, noting that stable value funds have a significant return advantage over money market funds, which have been yielding nearly zero percent for about four years, and have a regulatory horizon that can be described as "stormy at best."

"We can also try to crack the code for the Individual Retirement Account (IRA) market," he said. "If we can do that, we can more than double our opportunity set." Under the current regulatory regime, stable value funds cannot be offered to IRA investors.

In summary, King said stable value as an asset class is in great shape. "We have a significant share of the marketplace," he said. "We have new wrap capacity in the market. We have new entrants providing contracts that meet the new conditions of the marketplace. We have several existing providers continuing to grow their business. We also have some wrap providers who are holding pat and not exiting the market. We also have demographics in our favor; Boomers are retiring at a rate of 10,000 a day, and data from the Investment Company Institute and the Employee Benefit Research Institute show the 60-year and up age cohort saving up to 30 percent of their assets in stable value. So we have some excellent tailwinds.

"We've also gone from the defensive to the offensive in the press," he concluded. "Through the financial crisis, and until very recently, we were reacting to negative press in the marketplace. Now, we are posting positive articles on our website from publications like *Barron's, The Wall Street Journal, Pensions & Investments,* and *Forbes*. The asset class is in a good place." SVIA

The Big Picture

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When Fidelity looks only at actively employed participants who have been enrolled and contributing to their plans for at least 10 years, Heffernan said, the average account balance is much higher: $211,000. "If you keep people in (the plans)," she observed, "the numbers do get much better."

Heffernan was part of a panel discussion that examined trends in each of the three main segments of the defined contribution plan marketplace: 401(k) plans, which are sponsored by private employers; 457 plans, offered primarily by government employers; and 403(b) plans, which are sponsored by public education organizations and some non-profit employers. Among the highlights:

The 401(k) market

In the 401(k) market, Heffernan said, automatic enrollment is increasingly becoming the norm, especially among larger plans. Only about 24 percent of the plans on its books use it, she said, but those plans cover 55 percent of plan participants.

Other key trends Heffernan cited:

- Target-date funds are the most common default investment option in plans for which Fidelity provides record-keeping services. Also, just over half of the Millennials in those plans, who represent about a third of the overall participant base, contribute 100 percent of their money to target-date funds.

- Stable value funds are widely used by Fidelity clients, particularly in the larger corporate plan market, although they also enjoy a "fair amount of exposure" in the private employer market. However, Heffernan said, among new plans coming onto Fidelity's platform, only a small percentage is choosing to offer a stable value investment option. "That's a bit of a concern," she said, "although certainly plan sponsors are still committed to it (stable value) in the private employer market."

The 457 market

Sara Richman, vice president of product management at Great-West Financial, said one of the characteristics of the 457 marketplace is that they tend to be paternalistic. The 457 market includes state and local government plans and also plans sponsored by quasi-governmental employers such as water systems, public schools and public hospitals.

Still, participation rates in 457 plans are lower than they are for 401(k) plans. About 26 percent of eligible employees participate in 457 plans, Richman said, versus about 89 percent in the 401(k) market. Richman attributed the difference in part to the fact that many employees in the 457 market have access to a defined benefit plan at work, and so they view the 457 as a supplemental savings vehicle. Also, automatic enrollment is a fairly rare feature in 457 plans, with only about 8 percent of participants covered.

Although 457 plans are not subject to ERISA—the Employee Retirement Income Security Act—457 plan sponsors often look to ERISA as a guide, Richman noted. Investment options tend to look much like those available in 401(k) plans, with most plans including a stable value fund in their lineup. Target-date funds are also popular, and are often customized for larger plans.

While most 401(k) plans have a designated default investment option, Richman said about 30 percent of 457 plans have none. Among those that do, about 50 percent use target-date funds, and about 10 percent use stable value.

Like their corporate counterparts, sponsors of 457 plans are concerned about the ongoing funding burden associated with their defined benefit plans, Richman said. Despite this, thus far sponsors have made few changes on that front, in part because they often must be negotiated with unions. Sponsors are also increasingly focused on the fees associated with the investment options they offer and are becoming more resistant to "proprietary" products offered by their plan provider, including rollover IRAs, funds and other services. She said multi-manager funds are in demand among large plans. This is also true within the stable value sector.

The 403(b) market

Philip Maffei, senior director in charge of the Stable Value Solutions team at TIAA-CREF, observed that 403(b) plans are offered by over 85 percent of not-for-profit employers in all industry sectors except healthcare, where the figure is

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Attendees at the Stable Value Investment Association Fall Forum 2013

Shields Says Income Inequality Could Be "Sleeper Issue" of 2016 Election

By Randy Myers

There are plenty of issues that could define the 2016 presidential election. Republicans and Democrats could still be fighting about taxes and spending, foreign policy, and even healthcare. But nationally known columnist and political commentator Mark Shields says that income equality could be the issue that determines who will occupy the White House next.

According to a recent white paper by the Economic Policy Institute, the average CEO now earns 273 times more than the average worker, up from 20 times in 1965. Meanwhile, a recent analysis of IRS data by economists Emmanuel Saez and Thomas Piketty found that the bottom 90 percent of American taxpayers earned only $59 more in 2011 than they did in 1966, adjusted for inflation. By contrast, incomes for the top 10 percent of taxpayers grew by $116,071.

"I believe there is a festering sense among voters that the economic system is rigged, and that nobody is really standing up for them," Shields told participants at the 2013 SVIA Fall Forum in Washington, D.C. "I think income equality could be the sleeper issue in 2016, just as Iraq was the issue in 2008 that defined and determined the Democratic nominee for president."

Shields did not predict which political party would benefit from this sentiment, observing that while Republicans are in worse shape than Democrats, neither party is popular right now. In fact, he said, a recent NBC/Wall Street Journal poll found Republicans at their lowest point in the history of the poll in terms of public favorability, with 51 percent of voters blaming them for the recent federal government shutdown, and only 31 percent blaming the Democrats and President Obama.

Still, Shields said, "This is not a time for Democrats to pop the champagne bottles; they are far from out of the woods. The Democrats are, and historically have been, the party of government; they believe it can be an engine of economic progress and social justice. But we are witnessing an erosion of public trust in government, which does not help the Democrats. Even if the Democrats win back a majority in the House, I do not have the sense that people are ready to march under any banner of enlarged public action."

One thing that is helping the Democrats, Shields noted, is a shift in the nation's demographics. When George H.W. Bush won the presidency in 1988, he said, the country was 89 percent white. Now it is 71 percent white. Republicans have generally been losing the battle for the hearts and minds of non-whites, in part because of the GOP's opposition to immigration reform. Republicans won only a quarter of the Latino vote in the 2012 presidential election, Shields noted, "and prospects going forward are even more dire."

While Americans have always been an optimistic people, Shields said that's no longer uniformly the case. For the first time, he said, a majority of Americans believe their children's lives will not be as bright as theirs have been, and that China, not the U.S., will lead the next century.

To reverse sentiment like that, and to improve cooperation in Washington, Shields said the country will need to find a presidential candidate "with a program that is straightforward and understandable, so that people can say, 'Yes, I believe that's in the best interests of the country,' and at the same time can rekindle that optimism." SVIA

The Big Picture

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66 percent. Historically, 403(b) plans have used multiple record-keeping and investment vendors, although regulatory changes in 2009 and 2012 have resulted in many plans reducing the number of vendors they use, with some moving to a single record-keeper.

About 67 percent of not-for-profit employees who have access to a defined contribution plan—usually a 403(b)—participate in their plan, and on average contribute 8.1 percent of their salary, Maffei said.

Most 403(b) plans are limited by federal regulation to using mutual funds or annuity contracts; collective funds typically cannot be used. Other than public K-12 school systems, Maffei noted, a stable value option is available in about three-quarters of all plans. In the public K-12 market, that number is only 47 percent.

Since the Department of Labor issued rules spelling out what counts as a qualified default investment option (QDIA), the percentage of TIAA-CREF participants contributing to multi-asset class investments such as target-date funds has increased, to 34 percent in 2011 from 15 percent in 2005, Maffei said. During that same period, the percentage contributing to a principal preservation option decreased to 47 percent from 63 percent.

Like their 457 counterparts, 403(b) plans have been slow to embrace automatic enrollment. Only 14.6 percent use it, Maffei said, even though participation rates are significantly higher—by anywhere from six to 22 percentage points—among those that do. Automatic escalation of deferrals is used by only about a third of those plans that use automatic enrollment.

Even with these innovations only 44 percent of 403(b) plan participants say they are confident of being financially ready for retirement, he said, mirroring findings in other parts of the defined contribution plan marketplace. To improve outcomes, Maffei said more plan sponsors need to improve their plan design to incorporate features such as automatic enrollment and automatic deferral escalation; switch to a single plan-management platform to reduce complexity and minimize expenses; provide participants with access to low-cost fixed and variable annuities, mutual funds, and lifetime income solutions; provide objective, outcomes-based advice and education; and offer supplemental benefits such as retiree healthcare savings plans. SVIA

Evaluating Fiduciary Risks

By Randy Myers

Over the past decade, the retirement plan industry has been subject to a wave of litigation under the Employee Retirement Income Security Act. Allegations have included breaches of fiduciary duty in connection with excessive fees for both investment management and record-keeping services.

In a presentation at the 2013 SVIA Fall Forum, Jeremy Blumenfeld, a partner in the Labor and Employment Practice Group at Morgan, Lewis & Bockius LLP, said these ERISA lawsuits can be segmented into three categories. In the first, cases tend to be filed only against plan sponsors. In the second, service providers are named as defendants, too, making all communications between sponsors and vendors subject to discovery. In the third, claims are brought against service providers by class-action lawyers representing groups of small retirement plans.

A few trends can be discerned, Blumenfeld said. One is that while there is no “magic number” in terms of what is a reasonable investment management fee, plaintiffs’ attorneys have tended to focus on actively managed investment options, which are usually more expensive than passively managed options. Another is that plaintiffs’ attorneys often try to discern which retirement plans are most profitable to service providers, and allege that those are the plans being overcharged.

Three current cases bear close watching, Blumenfeld said. One is a lawsuit filed by plan participants against ABB Inc. in which a U.S. district court in Missouri awarded $35.2 million in damages against ABB and related defendants. That case is on appeal, Blumenfeld said. It revolves around an allegation that the plan substituted one investment option for another not because it thought the new option would outperform but because it would generate revenue for one of the plan’s service providers. “There wasn’t proof of this,” said Blumenfeld, whose firm represented ABB. “The principal evidence the plaintiffs offered was the fact that the investment option selected underperformed the option that was taken out. That led to roughly half of the damages in that case. The case is now on appeal and is certainly something that will affect the industry and how these cases are brought and litigated.”

From the left: Stephen Kolocotronis, Fidelity Investments; Jeremy Blumenfeld, Morgan Lewis & Bockius LLP; Michael Richman, Morgan Lewis & Bockius LLP

Another case to watch, he said, is a lawsuit pending against ING Life Insurance and Annuity Co. relating to whether or not ING was a fiduciary with respect to the investment options selected by its plan sponsor clients. It is similar to another suit that was brought against John Hancock Life Insurance Co., which was dismissed without trial by a district court in New Jersey earlier this year, and is also now on appeal.

There has been no particular focus on stable value funds in the fee litigation cases filed to date, Blumenfeld said. Rather, stable value has been treated like other investment options. In an ongoing class-action case involving Lockheed Martin, for example, plaintiffs have charged that they didn’t earn as much as they could have in their stable value fund because its portfolio of safer, less risky investments underperformed one of the Hueler stable value indexes, which averages results for multiple stable value

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Stable Value Outperforms

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To further explore how this might impact investor outcomes, the researchers used these results to create three optimal model portfolios—conservative, moderate, aggressive—and plot them along an efficient frontier. Only two asset classes were needed to create the optimal portfolios, Sipper said: stable value and U.S. equities. The conservative portfolio had an 85 percent allocation to stable value and a standard deviation risk of about 1.5 percent. The moderate portfolio had a 59 percent allocation to stable value and a standard deviation risk just under 5 percent, while the aggressive portfolio had a 21 percent allocation to stable value and a standard deviation risk about 9 percent.

Two important conclusions could be drawn from the research, Sipper said. One was that whether an investor had a conservative or moderate tolerance for risk, stable value could play a significant role in their portfolio—whether interest rates rose steadily or quickly. The other was that without stable value, the only way an investor could hope to achieve the same returns achieved by the model portfolios would be by assuming more risk.

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funds. "Of course, if you're picking an index that is based on an average of a lot of different investment options, by definition about half will underperform," Blumenfeld noted. He said the case includes other absurdities. For example, of the four named plaintiffs, three had not invested in the Lockheed Martin stable value fund at all, and the one who had did so during a period in which it outperformed the Hueler Index.

In yet another case, involving Cigna Corp., participants in the company's 401(k) plan challenged not only the performance of the plan's stable value fund, but also argued that it should have had a more diverse collection of wrap contracts. The plaintiffs also complained about the fund's crediting rate not matching the performance of the fund's underlying investments. Cigna denied liability but settled the suit for $35 million. As part of the settlement, it agreed to hire an independent consultant to monitor and advise on the stable value fund and other investments in its 401(k) plan.

The lesson for service providers, Blumenfeld said, is to make sure their clients understand the products and services they're buying, and, to the extent possible, put that information in writing and keep reminding clients of it. "It doesn't do them any good if they forget or don't understand, and it doesn't do you any good," he said.

Blumenfeld also recommended that service providers and plan sponsors alike establish and document prudent processes for choosing and managing stable value products. Areas to be mindful of include performance, fees, wrap costs, wrap diversification, and crediting rates.

On the regulatory front, Michael Richman, of counsel to Morgan, Lewis & Bockius, updated Forum participants on what's been happening in the year since plan sponsors and service providers became subject to new disclosure requirements under ERISA sections 408(b)2 and 404(a)5. The former requires service providers to disclose information about their fees and fiduciary status to their plan sponsor clients, while the latter requires sponsors to disclose information about plan expenses to plan participants.

Richman noted that 408(b)2 allows service providers to make disclosures once and forego annual updates unless something changes. However, he said, a number of providers are doing annual updates anyway to make sure they didn't miss any changes and to ensure that all their clients have up-to-date information. Meanwhile, the Department of Labor is considering mandating a new "Form of Disclosure" guide under 408(b)2 that could serve as a roadmap for finding disclosures in the documents provided to plan sponsors. However, he said, the initiative is apparently on hold under pressure from industry trade associations.

In other regulatory developments, Richman said the DOL is still considering whether to broaden the circumstances under which a service provider could be deemed a fiduciary under ERISA. The DOL has said it will re-propose such a rule, but it has not done so yet and action, Richman said, does not appear imminent.

Elsewhere, both the DOL and the Securities and Exchange Commission are considering new rules for target-date fund disclosures. The DOL had expected to issue a final rule in November of this year, Richman said, but it now appears that will not happen.

Finally, Richman noted, the DOL has issued an advance notice of proposed rulemaking that would impact defined contribution plans. Plans would be required to include in the benefit statements sent out to plan participants an estimate of what a participant's account balance might be worth in terms of lifetime income. The DOL is currently reviewing comments on its proposal.

In terms of Department of Labor investigations, Richman said it's hard to discern trends because little information about them is made public. He did note, though, that the DOL has made a number of general requests to service providers asking for broad amounts of information. "When you drill down, it turns out that, in some of the ones we've seen, the focus is on certain issues: abandoned plans, which is an issue for the Department of Labor if a company is gone and there is no fiduciary to wind down the plan," he said. "There's a DOL initiative, and some regulations out there, that allow the Department of Labor to step in, or for a process where a service provider appoints someone to take over the plan and wind it down."

The DOL also appears to be looking into trade errors made when a plan moves its assets to another provider, Richman said. SVIA

Stable Value Roundtable

By Randy Myers

What's happening in the stable value market? Seven experts from diverse sectors of the industry brought participants at the 2013 SVIA Fall Forum up to speed during a lively roundtable discussion in Washington, D.C. Among the highlights:

Wrap diversification: A preference for having multiple wrap contract providers for a stable value fund still persists among retirement plan sponsors, said Warren Howe, national sales director for stable value markets at Metropolitan Life Insurance Co. But he said the fact that some plan sponsors embraced single-wrap insurance-company stable value products in the aftermath of the 2008 credit crisis, when wrap capacity was constrained, demonstrated that many have become more comfortable with that approach, too.

Unwrapped stable value portfolios: A few defined contribution plans introduced market-value sleeves of securities into their stable value funds prior to the 2008 financial crisis, and interest in such structures increased after the crisis when stable value wrap capacity became constrained, said Jessica Mohan, managing director with Bank of Tokyo-Mitsubishi UFI Ltd., where she oversees its stable value business. Mohan says her firm hasn't done any new transactions with funds that have included market-value sleeves, but "we're ready to." She suggested that these unwrapped portfolios should generally adhere to the investment guidelines established for the wrapped portion of a stable value fund, and that plan sponsors who offer such funds should communicate to their plan participants that their fund is "not 100 percent a stable value fund."

Tom Schuster, vice president of stable value management with Metropolitan Life, warned that there is headline risk associated with such structures if they lose money and plan participants later say they thought they had been getting traditional stable value guarantees. "It's not a stable value fund," he said, adding that he doesn't think the structures make much sense

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for any plan that can secure sufficient wrap coverage to offer a "100 percent" stable value option.

Shorter-duration portfolios: Douglas Barry, executive vice president with Standish Mellon Asset Management Co., said that like many stable value managers, his firm has been managing to some shorter-duration benchmarks for many clients, typically in the range of 3.5 to 4 years. "We're incorporating more 1-to-5 year (maturity) strategies, with a duration of about 2.5 years," he said, "and we're okay with that given where we are in the interest-rate cycle."

Wrap capacity and pooled fund closings: A contraction in stable value wrap capacity following the 2008 financial crisis forced some pooled stable value funds to close or limit new deposits. Steve LeLaurin, senior client portfolio manager for Invesco Advisors Inc., said wrap capacity has since improved. Metropolitan Life's Schuster said that while some smaller, top-heavy pooled funds may continue to find it difficult to secure sufficient wrap capacity to do new business, he thinks well-diversified, transparent funds, especially those with longer put structures, will continue to get all the capacity they need. (A top-heavy pooled fund is one in which a handful of plans account for the bulk of the fund's assets. A "put" refers to the length of time—usually 12 months—that a defined contribution plan must give a pooled fund to carry out the plan's exit from the fund.) LeLaurin said that his own firm "had a limited soft close for a while until we could get additional wrap capacity, allowing us to reopen on a cautious basis."

The impact of rising rates on wrap capacity: If interest rates began to rise sharply, market-value-to-book-value ratios for stable value funds would likely fall, at least temporarily. Schuster said Metropolitan Life's appetite to write new business might become constrained if those ratios fell too much. "At a ratio of around 98 percent, assuming cash flow remains strong, we'd still be in the market," he said. "When you start hitting 95 percent, that's where you hit a bit of a pause, at least from MetLife's perspective. At 95 percent I believe you see wrap capacity start to become a little constrained." Mohan

From the left: Angelo Auriemma, Plan Sponsor Advisors; Douglas Barry, Standish Mellon Asset Management; Matt Gleason, Dwight Asset Management; Stephen LeLaurin, Invesco; Jessica Mohan, Bank of Tokyo-Mitsubishi UFJ Ltd.; Warren Howe, Metropolitan Life Insurance Company; Thomas Schuster, Metropolitan Life Insurance Company

agreed that ratios in the 98 percent to 102 percent range—typical historically—are very comfortable for wrap issuers.

Wrap capacity for 403(b) plans: Schuster said the challenge to wrap providers interested in the 403(b) market is the minimum non-forfeiture rate that applies to those plans. "In a very low interest-rate environment, like the one we're in, that one percent guarantee with an annual rate reset presents some challenges to a wrap provider," Schuster said. "My belief is that if interest rates were to rise and that one percent non-forfeiture rate could be safely met, there would be more interest in pursuing 403(b) opportunities."

A smaller community of wrap providers: While stable value wrap capacity has been improving for several years now, there still are not as many wrap issuers as there were before the credit crisis. But there are more than there were at the market's bottom. "We love the fact that there's more choice now," said Standish Mellon's Barry. "The way I characterize it for our clients is there was a period of time when our portfolio managers had one option, and that was the option to put money to work that day. Today we have choice, which is a wonderful thing to bring to our clients and our portfolios. We love the fact that there are new competitors in this marketplace and that we can diversify portfolios broadly."

Tighter investment guidelines: permanent or temporary? Invesco's LeLaurin said his firm views the tightening of investment guidelines in the wake of the 2008 credit crisis as a temporary phenomenon. "Maybe guideline allowances were just too liberal for a while, and now we've reined in the outliers," he said. "We don't anticipate there will be new investment restrictions, and hopefully going forward we'll be able to manage in a way that produces the best results for clients."

"Portfolios have changed," added Mohan, "and (those changes) are here to stay, with a stricter compliance network, for the time being. If there is pushback, wrap providers will respond, but I don't think we're going to go back to (riskier) asset classes or concentrations we saw in 2008."

Schuster said he also thinks the more explicit investment guidelines now in place are "here to stay for the foreseeable future." But he added that his firm is willing to liberalize investment guidelines if an asset manager it's hiring as a sub-advisor can demonstrate capabilities in a given sector of the marketplace, such as collateralized mortgage securities or asset-backed securities.

Longer put provisions: While some pooled stable value funds have been lengthening the standard 12-month put—the notice period a

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plan must give before exiting the fund—Howe said he's not sure that it's a trend. However, he said, funds that stick with a 12-month put may find themselves forced to maintain a shorter duration in their investment portfolios and accept additional investment restrictions. Schuster noted that, all other things being equal, his firm will wrap a greater percentage of a pooled fund with a 24-month put than it will for one with a 12-month put. Matt Gleason, managing director of Dwight Asset Management Co., said his firm decided to stick with the 12-month put in its book of business. "We didn't want to give up liquidity beyond that 12-month period," he said. Barry said Standish Mellon made the same decision, as it was not convinced that much more wrap capacity would be available if it extended the put period. LeLaurin said his company, which operates several pooled funds, concluded that a 24-month put could benefit its plan sponsor clients by providing greater protection for retirement plan participants who stay in the fund. Many of its clients adopted a 24-month put with little pushback, he said, although a few did exercise their right to leave Invesco funds rather than adopt the longer 24-month put.

Stable value's role during decumulation phase of retirement: Roundtable participants as a group weren't certain what role stable value will play as retirement plan participants segue into the decumulation phase of investing—withdrawing, rather than accumulating, assets. However, LeLaurin observed that some retirement plan record-keepers have the ability to send regular monthly payments to plan participants once they are ready to begin making withdrawals, and, he said, "stable value could be the conservative, non-volatile asset from which those withdrawals are taken."

Outlook for stable value funds: Investment professionals generally agree that with interest rates near historic lows, rates have almost nowhere to go but up once the economy regains full steam. But the 2013 SVIA Fall Forum panelists said plan sponsors shouldn't be overly concerned about the impact on stable value funds. LeLaurin noted that stable value funds were designed to cope with rising rates, and that the effects of even a rapid rise in rates would likely be transitory. Howe noted that a rising rate environment could send market-value-to-book-value ratios for stable value funds below 100 percent for a time, but said this, too, is normal and manageable. Schuster agreed, noting that the stable value crediting rate mechanisms amortize investment gains or losses over time, cushioning investors from sudden market moves. And Mohan observed that rising interest rates can be negative for other asset classes too, so that singling out stable value funds for worry probably doesn't make much sense.

Stable value roundtable discussion at the Fall Forum 2013.
From the left: Angelo Auriemma, Plan Sponsor Advisors; Douglas Barry, Standish Mellon Asset Management; Matt Gleason, Dwight Asset Management; Stephen LeLaurin, Invesco; Jessica Mohan, Bank of Tokyo-Mitsubishi UFJ Ltd.; Warren Howe, Metropolitan Life Insurance Company; Thomas Schuster, Metropolitan Life Insurance Company

Building an Optimal Investment Lineup for a Defined Contribution Plan

By Randy Myers

Are you a plan sponsor or consultant looking to create a great investment lineup for a defined contribution plan? David Blanchett, head of retirement research for Morningstar Investment Management, offers this advice: Don't start with a goal of building the best lineup possible. Instead, start with your end point in mind: building the lineup that will give your plan participants the best opportunity for success. Why? Because every participant population is different, and what's best for one group of participants may not be best for another. Their education levels, engagement in the investment process and their experience with investing should all factor into your decisions.

Easier said than done, right? Well, yes. But there are some fundamental guidelines to follow no matter what your participant demographics and circumstances may be, Blanchett said in a presentation at the 2013 SVIA Fall Forum.

Morningstar helps build investment lineups for all types of plan sponsors, Blanchett said, and in each case it starts with the basics required to comply with Section 404(c) of the Employee Retirement Income Security Act, which requires that plan sponsors offer at least three different, diversified investment options with materially different risk and return characteristics. At a minimum, Blanchett said, this means offering a cash option, a stock option, and a bond option. In plans that it designs, he added, Morningstar almost always includes at least five options: a cash fund, a bond fund, a large-cap stock fund, a small-cap stock fund, and a foreign stock fund.

Morningstar will often include investment options beyond those basics, Blanchett noted, but he cautioned sponsors to think carefully before adding too many investment choices to their

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Columnist Sees "Crescendo of Errors" in Washington

By Randy Myers

The political divisiveness that has characterized Washington, D.C. over the past few years reached new highs in October 2013, first when Congress allowed the federal government to shut down, and then when it came perilously close to allowing the U.S. to default on its debt. To Michael Barone, syndicated columnist and senior political analyst with the *Washington Examiner,* those developments stemmed from "a crescendo of errors" on both sides of the political aisle.Addressing the 2013 SVIA Fall Forum, Barone said one reason for the nation's political differences is that there are genuine disagreements between the Republicans and Democrats on important issues of public policy. But he also argued that both sides have made political mistakes and miscalculations, including over-interpreting the mandates they received from voters in the 2012 elections, and failing to understand the needs or views of the other side.

President Obama, Barone said, came to office believing that in a time of economic distress, Americans would be more supportive of, or at least more amenable to, government. But Barone characterized that as a misguided interpretation of what happened in the 1930s, when Franklin Roosevelt won four successive terms as president in part on a platform of expanding government to help the poor. Roosevelt also led the country through World War II, though, and his third and fourth reelections, Barone contended, can more properly be attributed to him being a strong leader in extreme times.

Barone also called Obama's decision to push national healthcare reform through a Democratic Congress during his first two years in office a partisan gamble for which Democrats have been paying a price ever since—including, in 2012, the biggest gain of seats in the House of Representatives by Republicans since the late 1940s.

But Republicans have miscalculated too, Barone suggested. For example, he said, they failed to recognize that when Democrats earlier this year called for a "clean" continuing resolution to keep the federal government open past September 30, with no material changes to government spending, the Democrats were actually making a concession; they didn't ask for higher taxes nor did they insist on reining in the sequestration spending cuts. Yet instead of accommodating the Democrats, a minority of House Republicans refused to vote for a continuing resolution unless it defunded Obamacare, the president's signature legislative achievement. Polls showed that voters liked the idea of delaying Obamacare, but not defunding it. Republicans ultimately lost the showdown, but only after forcing the federal government into a much-maligned partial shutdown.

"In my view, both sides were blundering," Barone said. "There were a critical number of Republicans under the delusion they could rally the country to defund Obamacare or get the Senate to cave." Their stance, he theorized, may have had more to do with the politics of 2016—the year of the next presidential election—than the politics of 2013 or 2014.

Meanwhile, Barone said he thought a critical number of Democrats were under the delusion that the Republican tactics would prove suicidal for that party. "I think Republicans are hurt, but that's exaggerated," he said. "Most polls show Republicans doing worse than Democrats, but by a small margin. I'm not inclined to think there will be huge changes in Congressional numbers as a result of these things."

Barone also ascribed some of the blame for Washington's gridlock to the nation's founding fathers, who devised a system of checks and balances by creating three separate branches of government. "I also blame the American people," he said, "for electing a divided government and expecting them all to get along."

While having different parties control different parts of the government has actually been quite common over the past several decades, Barone said the trend has been exacerbated of late not just by an influx of Latin American immigrants to the U.S., but also by the migration of affluent Americans to "culturally congenial" locales, where like-minded communities can deliver big majorities for one party or another. When Jimmy Carter was elected president in 1976, for example, he narrowly carried the San Francisco Bay area by a 51 percent to 49 percent margin, Barone said. Obama, by contrast, won the Bay area with 73 percent of the vote in 2012.

Having supporters clustered in central cities, liberal suburbs, and college towns "gives Democrats a huge advantage in the electoral college," Barone said, leaving fewer "target states" in

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Building an Optimal Lineup

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plans, since having too many options could confuse plan participants. Sponsors also should consider whether they want to offer funds that are actively or passively managed; the latter are generally cheaper. One bad idea, he said, is to offer funds that invest in a specific industry; they concentrate risk and can be highly volatile.

In choosing specific investment options, Blanchett recommended that plan sponsors look for investments that are high quality with reasonable risk, and make sure that any funds of funds, such as target-date funds, follow similar criteria when selecting the funds in which they invest. All funds should be analyzed relative to asset allocation targets and performance benchmarks, he said. In terms of quantitative screening, sponsors should look at performance and style consistency, manager tenure and expenses. But they should also perform a fundamental analysis, looking at things like the people and processes behind a fund. Target-date funds merit special scrutiny, he said, requiring not only all the normal due diligence, but also a review of other factors, such as the "glide path" they follow as they become more conservative over time. SVIA

Potential Regulatory Changes Cloud Outlook at Front End of Yield Curve

By Randy Myers

The front end of the yield curve—home to conservative investments such as money market funds, short-term investment funds (STIFs), and even stable value—has been challenging for the past few years, not just for individual investors, but for institutions as well, including corporate sponsors of defined contribution plans. Corporations have record amounts of cash on their balance sheets, but the yields available to them at the front end of the curve have been languishing at or near historic lows. Meanwhile, proposed regulatory reforms could soon change the way money market funds operate.

"People are struggling with what's going on," Laurie Brignac, senior portfolio manager and co-head of North American Global Liquidity for Invesco Fixed Income, said at the 2013 SVIA Fall Forum. "Where do you put your money? Corporate treasurers are asking us all the time, 'What's the next step?'"

The answers aren't entirely clear. The Federal Reserve has indicated that it plans to keep short-term interest rates at extraordinarily low levels until unemployment falls to 6.5 percent, which many economists don't anticipate happening until late 2014 or early 2015. But there are some bright spots on the horizon, Brignac said.

Perhaps most intriguingly, the Fed announced in September that it is going to start testing a new tool—fixed-rate, full allotment, overnight reverse repo facilities—that should help establish a floor on money market rates. And the U.S. Treasury, Brignac noted, has announced that it will hold its first floating-rate note auction in January 2014, creating securities that could provide extra yield to investors when interest rates move higher.

"In this low-rate environment, everybody is pushing for yield and looking for new places to invest money," Brignac said. "We're seeing a lot of clients max out as much as they can in money market funds, but where are they putting (the excess)? We're getting record requests for separately managed accounts."

From the left: Stephen Kolocotronis, Fidelity Investments; Laurie Brignac, Invesco; Gina Mitchell, SVIA; Timothy Keehan, American Bankers Association

Meanwhile, government regulators are considering changes in the way money market funds operate, particularly with respect to maintaining a constant net asset value of $1 per share. As Brignac explained, the Securities and Exchange Commission has proposed three alternative approaches. In the first, institutional prime money market funds and tax-exempt money market funds would have to allow their net asset values to float daily with market values, out to four decimal places, rather than hold constant, as is currently done. Government funds and funds catering to retail investors would be exempt from the change. Proponents argue that a floating NAV would give institutional investors a truer picture of the value of their money market holdings. "It sounds deceptively

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"Crescendo of Errors"

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presidential elections. Republican supporters, by contrast, are dispersed more widely across the country, giving the GOP more of an advantage in House elections. Both George W. Bush in 2004 and Barack Obama in 2012 won the popular vote for the presidency, Barone noted, but Obama got many more electoral votes in his race. It was the opposite story in the House, he said, with Bush carrying 225 Congressional districts but Obama only 209.

Despite all that has happened, Barone said he thinks Democrats will face an uphill battle to regain the House in 2014, noting that only 17 Republican House districts were carried by Obama in 2012.

"Blame the government shutdown on the incompetence of both parties, but spare some blame for the framers of the Constitution and the American people as well," he concluded. "We have met the enemy, and he is us." SVIA

Potential Regulatory Changes

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simple," cautioned Brignac, arguing that it would, in fact, represent a very big shift for the money market industry, with challenges around recordkeeping on the part of buyers, sellers and intermediaries.

Stephen Kolocotronis, Fidelity Investments and Chair of the SVIA Government Relations Committee

A second alternative proposed by the SEC would keep stable net asset values for money market funds but create liquidity fees and redemption gates that would kick in if funds sustained substantial losses. Yet a third alternative would blend the first two approaches.

On an unrelated front, Brignac said, the SEC also is reviewing comments right now on a separate proposal that would require enhanced stress testing by money market funds, something she said the industry could easily handle.

While they are still looking at money market reform, regulators have already issued new rules for Short Term Investment Funds (STIFs), which are collective investment funds operated by banks. Like money market funds, they invest in short-term, high-quality, low-risk, fixed-income securities. Unlike money market funds, STIFs are available only to a bank's fiduciary customers, such as personal trusts and employee benefit plans, said Tim Keehan, vice president and senior counsel at the American Bankers Association's Center for Securities, Trusts and Investments. Also unlike money market funds, STIFs are not sold directly, but are typically provided as a component of another bank service. STIFs can serve, for example, as a sweep vehicle for the cash balance of another bank-maintained collective fund.

In July 2013, STIFs became subject to new rules issued by the Office of the Comptroller of the Currency. The rules are aimed at preventing any loss of principal in STIFs. Among other things, they require OCC-regulated banks to set and monitor limits on portfolio quality and diversification, stress test their portfolios at least monthly, and provide monthly disclosures about their portfolios to both fund participants and the OCC. The process has proved largely manual rather than automated, Keehan noted, requiring input from many departments within the banks that offer STIFs.

If the SEC goes forward with its proposed money market reforms, Keehan said the OCC may revisit its regulations for STIFs and consider whether more are needed.

Regulatory changes with STIFs and money market funds may make stable value even more of a go-to fund for retirement plan participants and plan sponsors looking for capital preservation as well as predictable, positive returns. However, even stable value was touched by the Dodd-Frank Act of 2010, despite its stellar performance in the financial crisis. Stable value was swept into Dodd-Frank's call for tighter oversight of derivatives, or what the Act calls "swaps," even though it seemed clear that legislators recognized that stable value was not a swap. As SVIA President Gina Mitchell pointed out, legislators simply ran out of time to change the bill's language, and were afraid that if they carved out stable value investment contracts, they would be overrun with other product requests. Instead, SVIA was able to achieve something no other group did: an exemption that required the CFTC and SEC to take a deliberative and thorough review of stable value investment contracts to determine if stable value was a swap, and if the Commissions determined stable value was a swap, whether it was in the public interest to exempt them from regulation as a swap. She noted that the Commissions have requested information from the public twice and have not yet completed their study of the subject. Even if they conclude that stable value contracts are swaps—a view the SVIA has contested—the regulators have the authority under Dodd-Frank to exempt stable value contracts from the new regulations. Until a final decision, the Act provides certainty that all stable value contracts are not swaps. SVIA

Wells Fargo Economist Sees US Consumer Spending in Seventh Inning of Rebound

By Randy Myers

The U.S. still hasn't recovered fully from the Great Recession of 2008-2009, but it's getting closer.

Jay Bryson, managing director and global economist for Wells Fargo, told participants at the 2013 SVIA Fall Forum that he foresees real U.S. gross domestic product growing by about 2.5 percent in 2014 and 2.75 percent in 2015. That would be down from the 3.2 percent growth rate averaged from 1992 through 2007, but up from the 2 percent or so averaged over the past few years. In short, it's sluggish but improving.

A key component of that forecast, Bryson says, is his expectation that consumer spending, which accounts for about two-thirds of GDP, will continue to gradually grow as well. Stronger gains in consumer spending would translate into stronger economic growth, of course, but several factors are working against that, Bryson said. Although many Americans have successfully deleveraged their personal balance sheets—shrunk their debt, in other words—relatively few are showing any sign of wanting to leverage up again. While more have been willing to take on car loans, the biggest driver of non-revolving credit over the last few years has been student loans. "That's not a sign that people want to leverage up, but that they are desperate to improve their earnings power," he said. In terms of consumers deleveraging, he said, "my sense is that we're in the seventh inning,"

The biggest potential for better-than-expected economic growth, Bryson suggested, lies in the chance that Americans begin saving less and spending more. But he said that isn't likely to happen

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US Consumer Spending in Seventh Inning of Rebound

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unless employment growth accelerates. While the country has been creating about 180,000 jobs per month on average, despite declining employment in the government sector, that rate would have to accelerate to 250,000 to 300,000 a month to make a real difference in savings rates, consumer spending and the economy.

Bryson said there is pent-up demand among consumers, especially for cars and houses. He noted that the average car on American highways is now 11 years old and that the country has been building just under a million new housing units per year. Just to keep pace with household formations, he said, we need to be building between 1.25 million and 1.5 million units annually.

Given this sluggish economic outlook, Bryson said he doesn't expect the Federal Reserve to begin raising short-term interest rates anytime soon, especially since inflation is running at about half the Fed's target rate of 2 percent. Besides, he noted, the Fed has specifically said it won't push short rates higher until unemployment hits 6.5 percent. The unemployment rate stood at 7.2 percent in September, and Bryson said he doesn't expect it to fall to 6.5 percent until early 2015.

Bryson said the Fed could act sooner to end its quantitative easing program aimed at holding down longer-term interest rates. That program involves the Fed buying $85 billion of bonds monthly, and the Fed has said it will begin to taper its bond buying once the economy looks stronger. Bryson said the earliest he expects the Fed to start tapering is December of this year, and that it might not begin until early 2014.

There are no guarantees the economy will continue its slow recovery without slipping back into a recession, of course. Bryson identified three potential threats, the first being an extraordinary event, such as a Middle East war that sends oil prices soaring to $200 a barrel, for example, or the federal government defaulting on its debt. Europe is the second, he said. It has only recently emerged from its second recession since the 2008 credit crisis and it continues to face troubling debt issues in some of its member countries.

The third threat is China, whose economic growth has slowed as it tries to transition from an economy based almost entirely on capital investment to one based more equally on capital spending and consumer spending. Bryson said his firm is in the camp that believes China's economy, which had been growing at 10 percent or more annually until recently, will make a "soft landing," growing in the 7 percent to 8 percent range over the next couple of years.

"To sum up, assuming we don't shoot ourselves in the head, and Europe and China don't blow up anytime soon, the outlook for the global economy is not bad," Bryson concluded. SVIA

Attendees at the Stable Value Investment Association Fall Forum 2013

How United Technologies Revamped its 401(k) Plan

By Randy Myers

Plenty of employers offer 401(k) plans because it seems like a good idea. Maybe the competition does it. Maybe employees like them. Perhaps the boss wants one.

United Technologies Corp., a global manufacturer that generated $57.7 billion in revenue in 2012, has bigger ambitions for its 401(k). As Kevin Hanney, the company's director of defined contribution plan portfolio investments, explained at the 2013 SVIA Fall Forum, one of United Technologies' goals is to create a secure retirement benefit for the vast majority of its employees for whom the 401(k) is their only retirement plan. But it also wants that plan to be flexible enough to provide opportunities for attractive investment returns for other workers using it to supplement a defined benefit plan. And, for those employees investing in the plan's stable value fund, they want to be sure that fund delivers a steady crediting rate that helps them to maintain their lifestyle in retirement.

To achieve those goals, United Technologies began thinking in 2006 about how it wanted to revamp its plan, Hanney said. In 2011, it streamlined the plan's investment menu, reducing the number of investment options, replacing actively managed equity funds with passively managed alternatives and reducing fees. In 2012, it introduced a lifetime income option within the plan, delivered through a target-date portfolio. For plan participants who choose that option, the retirement income is guaranteed by insurance contracts, which combine a guaranteed income floor with upside potential, liquidity, and optional joint life and beneficiary features. The total cost, at about 119 basis points, is about one-third what a similar income guarantee would cost in the retail marketplace, Hanney said.

The United Technologies plan uses custom target-date funds as the default investment option for participants who don't select investments on their own. While it still has a relatively streamlined menu of low-cost, core investment options for people who wish to construct their own investment portfolios, Hanney said it will be adding two additional options in 2014: a multi-strategy real asset fund and multi-manager risk parity fund.

"In a nutshell, what we are now offering through our 401(k) is a pension plan for the 21st century," Hanney said. "We embraced the idea that a 401(k) plan can be a pension plan." SVIA

Paradigm Shift: Changing Demographics Bode Well for Stable Value

By Randy Myers

The stable value industry has benefitted from data showing that stable value funds historically have generated higher returns than their chief competitors, money market funds. It's a good marketing pitch, and an especially potent one right now, as money market returns have hovered near zero percent for the past four years. But Michael Davis, head of the stable value business for Prudential Retirement, argues that the industry is short-selling itself if it makes that distinction the focus of its marketing efforts.

Returns that outpace those available from money market funds, Davis told participants at the 2013 SVIA Fall Forum, merely represent the tactical case for stable value funds. "This is not where we as an industry want to be making our case," he said. "If we do, we're only making half the case we should be making. There are more fundamental reasons to be in stable value."

Those reasons include, of course, principal preservation guarantees and steady returns that, while outpacing money market returns, have at the same time exhibited similarly low volatility. Those characteristics, Davis said, make stable value attractive to retirement plan participants who are conservative investors, are at or near retirement age, those that need to diversify their retirement investment portfolio, or are seeking attractive, risk-adjusted returns as part of an overall asset allocation strategy.

Davis emphasized that there are also important demographic shifts taking place in the U.S. that should ensure a receptive market for stable value funds for decades to come. According to projections by the Census Bureau, the fastest-growing age group in the U.S. between now and 2050, on a percentage basis, will be those age 85 and older. And by the end of that period, Americans 65 and older should account for 20 percent of the population, up from 10 percent in 1970 and 13 percent as recently as 2009.

That's a promising trend for the stable value industry, which historically has captured the bulk of its assets from older retirement-plan participants. Research by the Employee Benefit Research Institute, for example, shows that in 2011, 401(k) plan participants in their 20s allocated just 7.1 percent of their plan assets to stable value. That percentage increased with every age cohort, however, peaking at 30 percent for participants in their 60s.

The impending retirement of the 76 million Baby Boomers born between 1946 and 1964 also suggests there will be plenty of people looking for conservative investment options in the decades ahead. Equally noteworthy, younger plan participants are sensitive to the need to save for retirement, and also receptive to the appeal of conservative investment options such as stable value funds. A 2012 study by Prudential Retirement found that 83 percent of Millennials—loosely defined as the 86 million Americans born from the early 1980s to the early 2000s—said that seeing what can happen to people who don't save enough for retirement makes them want to save more for their own retirement. And 81 percent said contributing to one's retirement account is a must, even during an economic recession.

"They're a generation of savers," Davis said of the Millennials. Pair that character trait with the fact that many are carrying burdensome levels of student loan debt, he added, and it's not surprising that many of them tend to be conservative investors, too. In fact, in a 2013 study by Accenture, 43 percent of Millennials identified themselves that way, versus 31 percent of Boomers and 27 percent of Generation X investors, the generation born immediately after the Baby Boomers.

The trend toward an older population, which is being mirrored in many other countries around the world, coupled with the mindset of the Millennial generation, suggests that conservative investments, centered on fixed-income securities, will play a prominent role in the retirement savings marketplace for decades to come, Davis concluded.

"A lot of people are saying that the really interesting things are going to be happening in the next few decades within the fixed-income arena," Davis said. "I would absolutely agree with that, and I think stable value is better positioned than any other fixed-income option to meet the needs of investors." SVIA

Attendees at the Stable Value Investment Association Fall Forum 2013

Survey Offers Clues to Broader Adoption of Stable Value Funds

By Randy Myers

Stable value funds are a core component of the defined contribution plan marketplace. Addressing the 2013 SVIA Fall Forum, Robin Andrus, director of stable value marketing for Prudential Retirement, noted that stable value funds are offered by about half of all defined contribution plans, and represent about 20 percent of the total assets in those plans. From 2000 through 2012, assets in stable value funds more than tripled to $701 billion.

Still, that leaves millions of participants in defined contribution plans without access to a stable value fund. Last year, Prudential surveyed more than 300 plan sponsors and 200 intermediaries, including investment advisors and consultants, to learn more about why some of them adopt stable value funds and others do not. A key goal of this research was to glean insights into how the industry might spur broader adoption of the asset class.

Familiarity with the asset class was the key differentiator between adopters and non-adopters, the survey found. The more familiar they were with the asset class, the more likely plan sponsors were to offer it to plan participants, or, in the case of intermediaries, the more likely they were to recommend it to their plan sponsor clients.

Complexity of stable value funds was a key barrier to adopting stable value, as were concerns about their fees and the strength of their guarantees. Intermediaries also cited concerns about liquidity, or the difficulty of transferring money out of the funds under certain circumstances. Plan sponsors who don't offer stable value mentioned liquidity concerns too, as well as a lack of familiarity with the funds among plan participants, their own insufficient understanding of the funds, and concerns about the transparency of fees, the stability of the bank or insurer providing the fund's guarantee, and the difficulty of adding stable value to their existing investment menu.

Intermediaries who consistently recommend stable value to their plan sponsor clients said their top reasons for endorsing the asset class include its ability to preserve capital while providing steady returns, the historically better long-term returns stable value funds have delivered relative to money market funds, and the return guarantees that stable value funds offer.

Plan sponsors cited similar reasons for offering stable value funds in their plans, including better returns than other fixed-income investments and money market funds, the proven financial stability of their fund's insurance provider, and recommendations from financial advisors and benefits consultants.

Plan sponsors who don't currently offer stable value indicated that education is a critical component to wider adoption of stable value funds, Andrus noted. Because they consider their retirement plan providers and intermediaries, such as financial advisors and benefits consultants, as primary sources of information, the stable value industry has an opportunity to promote wider adoption of its products by targeting educational efforts at them. Intermediaries said they consider meetings and in-person conferences as the best places to learn more about stable value funds, followed by plan provider websites and hardcopy brochures.

"The biggest issue cited by those who have not adopted stable value was familiarity with the asset class; that determines whether adoption is going to happen," Andrus summarized. "And the biggest barrier to familiarity is the complexity of the asset class. That's why education is key." SVIA

Survey Shows Consistent Allocation to Stable Value Over 20 Quarters

By Gina Mitchell

The SVIA Stable Value Funds Quarterly Characteristics Survey just hit a milestone. The survey, which covers the synthetic portfolios of 23 stable value managers, now has 20 quarters under its belt. It was first run covering the fourth quarter of 2008 and now covers all the way to the third quarter of 2013. The survey shows a consistent and steady allocation to stable value, with assets under management that totaled $347 billion in the fourth quarter of 2008 and which have risen to $459 billion in the third quarter of 2013; a 32 percent increase for the 20 periods. The survey found that the third quarter of 2013 crediting rates had a weighted average of 2.08 percent, which remains significantly higher than returns from money market funds. SVIA