Volume 8 | Number 4 | Spring 2021

the journal of retirement

RETIREMENT PLANNING AND BEHAVIOR

One of the more welcome trends in retirement research is greater attention to the entire savings and consumption lifecycle, particularly for the United States Australia New Zealand and the United Kingdom While contributions to post-retirement spending and asset management have never been absent from the pages of this journal, we have seen an uptick in interest and a new depth of analysis among research submissions. The powerful but slowly evolving forces driving this trend include reduced reliance on the defined benefit "paycheck," aging of the big baby boom cohort, increasing aggregate asset balances in defined contribution plans and IRAs, and growing interest among advisors, home offices sponsors and providers in improving post-retirement advice, products and financial management.

The other unsurprising thing about post-retirement planning is how it differs from its pre-retirement phase. While heterogeneity among participants or clients is always a challenge, it has a special saliency in the form of variations among retirees in expectations about and experiences with retirement age, health, mortality, morbidity, cognitive ability, post-retirement work and other activities, income needs and bequests. Research and solutions based on one-size fits all, or in some cases many, work less well amidst these variations, so we need to ask which ones matter most and how much customization is enough?

In that spirit, the article, entitled "Can Low Retirement Savings Rates be Rationalized?", by Jason Scott (currently of J.S. Consulting and formerly Financial Engines), John Shoven (Stanford), Sita Slavov (George Mason University) and John Watson (Stanford), directly links pre-retirement savings behavior to optimal retirement spending behavior by addressing differences in income as well as bringing in subjective versus actual time preferences, morbidity and mortality. In contrast to historically prevalent optimal lifecycle models, which are geared to maintaining a high proportion of pre-retirement consumption throughout retirement, their modeling finds that (1) optimal consumption declines with age and, consistent with that, (2) those in the bottom of the income scale would do better to spend their savings out early or not save at all and, instead, rely on Social Security. These findings should be of interest to anyone interested in improving financial security in retirement through better plan design and advice.

Focusing directly on improving retirement plan design, David Blanchett (Morningstar) takes an unusual tack in "Do Advisors Improve 401(k) Plans?" that goes beyond previous research confined to comparisons of investment menus and participant-level allocation decisions. Instead, he examines whether the presence of an outside consultant positively affects elements that have been well-documented to improve participant outcomes, including default investment availability and usage, plan governance, the adoption of automatic enrollment, the inclusion of employer securities, and fund diversity. He finds that, although plans employing consultants are more expensive than those without, participants, particularly those in small plans that are less likely to be able to employ in-house expertise, are better off when consultants are used to advise on plan design.

the journal of retirement

EXPLAINING TARGET DATE FUND RESULTS

The growing importance of target date funds (TDFs), which now represent about a quarter of assets in US defined contribution plans, is almost impossible to overstate. Two articles in this issue look at the performance of TDFs. In "An Analysis of the Performance of Target Date Funds," John Shoven and Daniel Walton (both of Stanford) employ returns-based style analysis over the past 10 years to show that lower-cost TDFs came close to matching comparable passive benchmark risk-adjusted returns, but that higher-cost TDFs fell behind. As with stand-alone equity funds, they also find that (1) past performance only weakly predicts future expected performance and (2) most TDFs with active funds trailed passive TDFs during the 2020 market crash and recovery.

Reaching a similar conclusion using a different approach, C. Edward Chang (Missouri State University), Thomas Krueger (Texas A&M University-Kingsville), and H. Doug White (Missouri State University) in "Importance of Costs in Target Date Fund Selection Using Three Morningstar Ratings," find that lower-cost TDFs have better historical risk-adjusted results than higher-cost TDFs, consistent with the backward-looking Morningstar Star ratings system. They also find that lower-cost funds get better ratings in the forward-looking Analyst Ratings and Quantitative Ratings systems. However, this research also finds that the human-powered Analyst Ratings gives less weight to historical TDF results and expense loads than the machine-learning oriented Quantitative Ratings. Readers should note that the TDFs covered by the two systems are different: TDFs covered by Analyst Ratings tend to be older, larger and to have produced better returns. Other research has shown that Analyst Ratings for individual equity funds have some predictive power and we look forward to additional research testing the predictive power of these ratings systems for TDFs.

Brett Hammond
Editor