Retirement Point
NEWS FOR PLAN SPONSORS AND PARTICIPANTS

May 2018

A Look at Target-Date Funds

Are these low-maintenance investments vital to retirement planning, or overrated?

THE MONTH IN BRIEF

April saw the S&P 500 advance 0.27% as a new earnings season unfolded – one in which investors grew uneasy about rising Treasury yields, protectionism, and privacy concerns involving tech giants. While the financial media largely focused on those anxieties, good news also appeared. The latest consumer spending and consumer confidence data was solid. Home buying picked up as listings increased slightly. Oil rallied, and so did the dollar. Overseas equity benchmarks saw big gains, even as some economists wondered if the boom in global growth was fading. One of the major financial news stories of April broke only hours before the start of May: a postponement of the tariffs planned for imported metals.[1]

% CHANGE	Y-T-D	1-YR CHG	5-YR AVG	10-YR AVG
DJIA	-2.25	+15.54	+12.57	+8.85
NASDAQ	+2.36	+16.00	+22.46	+19.29
S&P 500	-0.96	+10.87	+13.15	+9.11
REAL YIELD	**4/30 RATE**	**1 YR AGO**	**5 YRS AGO**	**10 YRS AGO**
10 YR TIPS	0.78%	0.41%	-0.64%	1.50%

Sources: wsj.com, bigcharts.com, treasury.gov – 4/30/1817,18,19,20
Indices are unmanaged, do not incur fees or expenses, and cannot be invested into directly. These returns do not include dividends. 10-year TIPS real yield = projected return at maturity given expected inflation.

MONTHLY QUOTE
"If you don't like something, change it. If you can't change it, change your attitude."

- Maya Angelou

MONTHLY TIP
Do you have a child or grandchild with a direct federal college loan? That loan may qualify for the Department of Education's Public Service Loan Forgiveness Program, which forgives loans for borrowers who have worked in public service for 10 years and kept up payments during that decade.

MONTHLY RIDDLE
Suzanne, a hair stylist, says that given the choice, she would prefer to cut and style the hair of two redheads instead of one brunette. She says there is a logical reason why. What is it?

Last month's riddle:
Through families it runs, and through bodies it flows. What is it?

Last month's answer:
Blood

A Look at Target-Date Funds

Are these low-maintenance investments vital to retirement planning, or overrated?

Do target-date funds represent smart choices, or just convenient ones? These funds have become ubiquitous in employer-sponsored retirement plans and their popularity has soared in the past decade. According to Morningstar, net inflows into target-date funds tripled during 2007-13. Asset management analysts Cerulli Associates project that 63% of all 401(k) contributions will be directed into TDFs by 2018.1,2

Fans of target-date funds praise how they have simplified investing for retirement. Still, they have a central problem: their leading attribute may also be their biggest drawback.

How do TDFs work? The idea behind a target-date fund is to make investing and saving for retirement as low-maintenance as possible. TDFs feature gradual, automatic adjustment of asset allocations in light of an expected retirement date, along with diversification across a wide range of asset classes. An investor can simply "set it and forget it" and make ongoing contributions to the fund with the confidence that its balance of equity and fixed-income investments will become more risk-averse as retirement nears.

In a sense, a TDF starts out as one style of fund for an investor and mutates into another. When he or she is young, it is an aggressive growth fund, with as much as 90% of the inflows assigned to equities. By the time the envisioned retirement date rolls around, the allocation to equities and fixed-income investments may be split closer to 50/50.2

With such long time horizons, TDFs are truly buy-and-hold investments. That has definite appeal for people who lack the time or inclination to take a hands-on approach to retirement planning. TDFs also usually have low turnover, with some distributions taxed as long-term capital gains.1

Are pre-retirees relying too heavily on TDFs? Putting retirement investing on "autopilot" can have a downside – and that may be worth an alarm or two, given Vanguard's forecast that 58% of its retirement plan participants (and 80% of its new plan participants) will have all of their retirement plan assets in TDFs by 2018. So in noting the merits of TDFs, we must also look at their demerits.2

The asset allocation of a target-date fund is not exactly dynamic. As it is geared to a time horizon rather than current market conditions, TDF investors may wince when a severe bear market arrives – it could be a case of "set it & regret it." They will need the patience to ride such downturns out. If they sell, they defeat the purpose of owning their TDF in the first place

Additionally, some investors are conservative well before they reach retirement age. A fortysomething risk-averse investor might not like having a clear majority of his or her TDF assets held in equities.

An investor will not be able to perform any tax loss harvesting with assets invested in a TDF (that is, selling "losers" in a portfolio to offset gains made by "winners") and if all of his or her retirement savings happen to be in the TDF, you have to pull money out of the TDF to put it in other types of investments that might generate tax savings.1

Fees can be high, because most TDFs are funds of funds – that is, multiple mutual funds brought together into one giant one. So this may mean two layers of fees.2

The glide path is very important. All TDFs have a glide path, the glide path being the rate or pace at which the asset allocation changes from aggressive toward conservative. With some TDFs, the glide path ends at retirement and the asset allocation approaches 100% cash. With others, the fund keeps gliding past a retirement date with the result that the retiree maintains a foot in the equities market – potentially very useful in the face of longevity risk, or as it is popularly known, the risk of outliving your money. The glide path of the TDF should be agreeable to the investor. The problem is that an investor may agree with it more at age 40 than at age 60.1

A new feature may make TDFs even more appealing. In October 2014, the IRS and the Treasury Department permitted TDFs held in 401(k) plans to add a lifetime income option. That would let a TDF investor receive a pension-like income beginning at the fund's target date. Companies sponsoring 401(k)s can even elect to make such TDFs the default plan investment; that is, employees who wanted to direct their money into other investment vehicles would have to inform their employers that they were opting out.2

Younger retirement savers should take a look at TDFs. If you are not enrolled in one already, you may want to weigh their pros and cons. While not exactly "the cure" for America's retirement savings problem, they are deservedly popular.

For more information on investment choices for your retirement plan, please call our plan's advisor at 202-618-3977 or email at dmakim@pointoak.com

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1 - money.usnews.com/money/blogs/the-smarter-mutual-fund-investor/2015/04/07/3-questions-to-ask-before-choosing-target-date-funds [4/7/15]

2 - time.com/money/3616433/retirement-income-401k-new-solution/ [12/5/14]

3 - nextavenue.org/article/2015-02/target-date-funds-pros-and-cons [2/8/15]

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