Stable Value Roundtable

continued from page 9

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

continued on page 11

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

continued on page 12

Building an Optimal Lineup

continued from page 10

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