

# Target Date Funds Are Popular— And Growing More So

Retirement plan advisors expect to increase their  
reliance on TDFs in the coming years



Target date funds are already a popular tool in the toolkits of retirement plan advisors. What's more, almost half of those surveyed expect to increase their use of TDFs in the next two years. This insight was one of the findings of a survey of 530 retirement plan advisors conducted by WealthManagement.com in February 2019.

**Among the study's additional findings:**

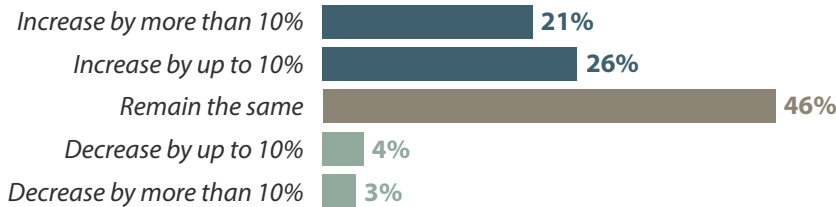
- TDFs' popularity is due in part to their ability to help retirement plan advisors address two of the biggest risks to successful retirement: longevity and volatility risk.
- Clients appear evenly divided between those who feel the fixed nature of the glide path and the mix of investments and allocations within the glide path are positive considerations, and those who feel these features are sources of concern.
- Most plan advisors feel that better customization would improve TDFs' usefulness.
- When evaluating TDFs, plan advisors focus primarily on the accounts' suitability for plan participants, while also taking into account a TDF's performance relative to its peers.

**TDFs are an important tool in many retirement plans**

Six in 10 plan advisors (61%) surveyed currently have clients invested in target date funds. And when a client is invested in a TDF, it typically represents an important component of their retirement plan. For example, among clients who use TDFs, an average of 68% of their retirement assets are invested in this type of fund. Many plan advisors expect the reliance on TDFs to increase in the coming years. In fact, there are slightly more advisors who expect to increase their use of TDFs (47%) than there are advisors who expect their usage to remain the same (46%). Both groups far outstrip those few (7%) who expect usage to decline.



**Percent of plan advisors who expect their use of TDFs to... (over the next two years)**



The general popularity of TDFs among retirement plan advisors may be linked to advisors' tendency to take a goals-based investment approach. Just over half of the plan advisors surveyed (51%) identified most strongly with a goals-based label, as compared to targeting outperformance against a benchmark (41%) or liabilities-driven investing (2%). It's perhaps not surprising that a group that favors the use of TDFs would also favor an investment strategy built around a specific target or outcome. This trend suggests that if goals-based investing is in fact gaining broader popularity, TDFs may benefit from increased usage as well.

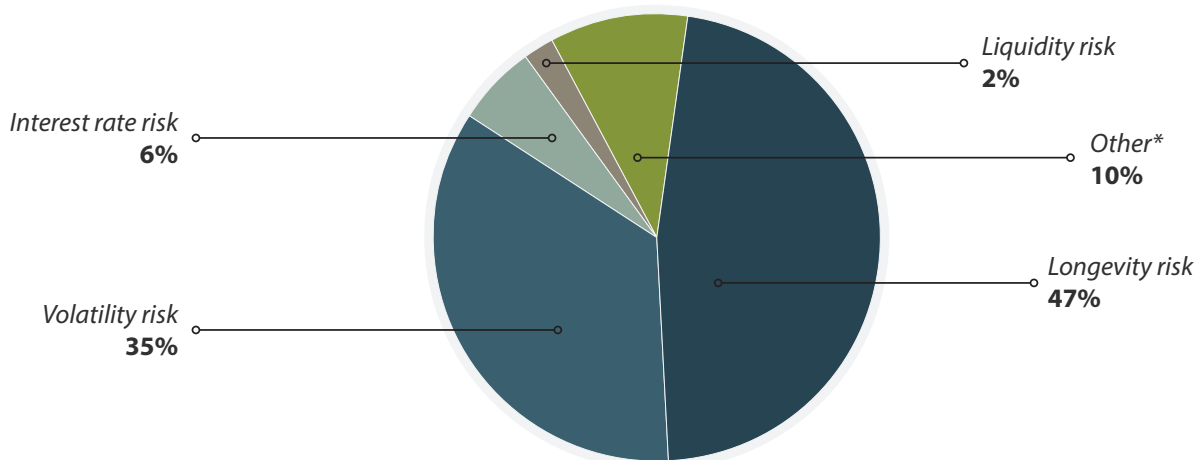
**Helping overcome risks to retirement**

Plan advisors do not agree on any one primary risk to individuals’ retirement savings, but a majority of advisors agree that the top two risks are longevity (47%) and volatility (35%). These two risks line up well with the strengths of the glide path concept. In particular, the gradual reduction in equity exposure over time seeks to minimize volatility in retirement, while the exposure to the growth potential of equities beyond retirement hedges against longevity risk.

TDFs also have a role to play in helping address some of the other risks plan advisors mentioned, including behavioral risk. Specifically, the glide path strategy essentially removes the risk that investors will adjust their allocations based on emotions.



**Percent of advisors who feel the following are the biggest risk to retirement**



\* includes behavioral, fear, inflation, sequence of return risk and not saving enough, among others.

Nearly two-thirds of plan advisors (63%) report favoring a “through” glide path for clients, over a “to” glide path (37%); the latter achieves and maintains a conservative allocation at the target date, while the former reduces its equity allocation gradually throughout retirement. Given that retirement can last for 30 years or more, and that more plan advisors prioritize longevity risk over volatility risk, a “through” glide path is logically the more attractive feature. Even so, most advisors (59%) still tell plan sponsors that the best type of glide path for their plan will depend on the characteristics of both the plan and its participants.



### **An issue of control**

One of the major appeals TDFs hold for investors is the ability to contribute money to an investment account that automatically shifts its asset allocation over time according to a pre-determined schedule. It is perhaps not surprising, therefore, that the mix of assets and allocation in the glide path, as well as the glide path itself, represent the top two motivating factors among clients considering a TDF.

### ***Percent of advisors who feel the following are the biggest risk to retirement***

	<b>Motivated</b>	<b>Concerned</b>
<i>Mix of investments/allocation within the glide path</i>	45%	39%
<i>Glide path</i>	42%	26%
<i>Fees</i>	26%	41%
<i>Reputation of firm</i>	26%	18%
<i>Active vs. passive strategy</i>	24%	34%
<i>Reputation of manager</i>	20%	14%
<i>Open vs. closed architecture</i>	8%	16%

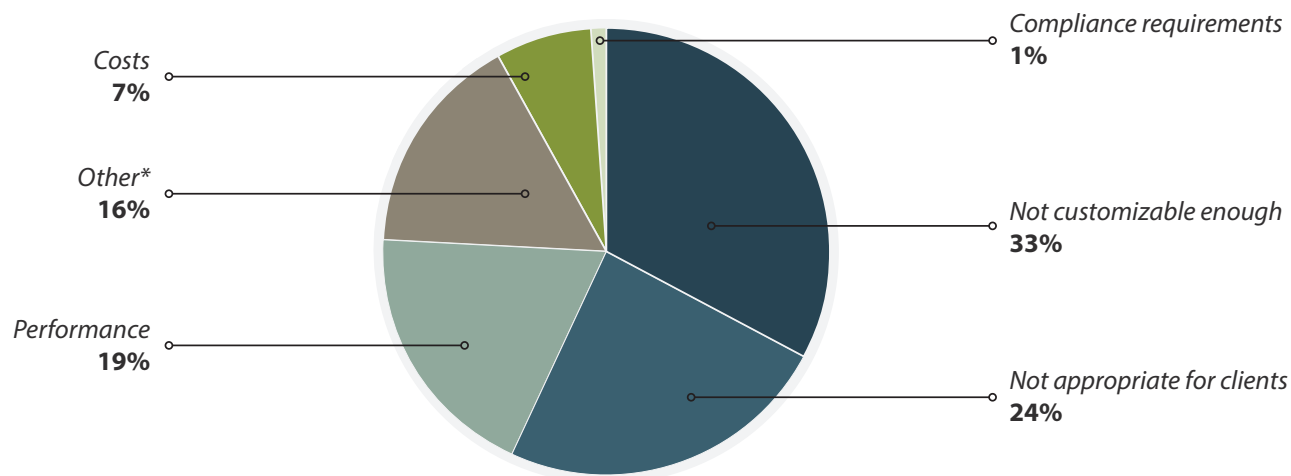
The very same factors that make TDFs attractive to certain clients are also among the ones that trigger the greatest amount of concern among other clients. While fees top the list of concerns, the mix of investments and the glidepath itself are both ranked among the four most concerning factors, according to the plan advisors surveyed. These results suggest that clients are relatively evenly divided on whether giving up control is the point of investing in TDFs or merely a necessary evil.

#### Customization can help

Plan advisors appear to agree, at least somewhat, with one subset of their clients: Most advisors surveyed (59%) believe that more customization versus off-the-shelf options would help make TDFs more useful and more attractive to clients. In fact, the most commonly cited reason advisors say they don't use TDFs in the plans they advise is the lack of customizability (33%).



#### The primary reasons plan advisors don't use TDFs



\* includes overly simplistic, too conservative and insufficient historical data, among others.

Many of the concerns advisors listed in the open-ended “other” category support the survey’s overall findings, particularly around a TDF’s suitability for a particular group of participants. A comment from one retirement plan advisor with more than 25 years of experience in the industry hits on multiple suitability issues at once. “TDFs look only at age and not where we are in the interest rate cycle,” he says. “Retirement date is not a terminus date, and many clients still need growth well after their retirement date.”

While most TDFs do not explicitly factor the interest rate cycle into their glide paths, many do address the need to maintain exposure to growth beyond the target retirement date—particularly through the choice of a “through” glidepath, although perhaps not at the level advisors would like to see.

### **Evaluating TDFs based on suitability**

There is no doubt that performance is important in any investment decision. TDFs are no exception, and performance is the second-most commonly cited top concern by plan advisors when it comes to evaluating TDFs. In keeping with the general tendency toward a goals-based approach identified earlier, however, it is noteworthy that advisors most commonly evaluate TDF performance relative to peer groups (40%) and not based on outperformance of a benchmark, whether an industry index (21%) or a custom benchmark (16%).



And yet, despite the importance of performance, suitability is the top concern among plan advisors who are evaluating TDFs. This is in keeping with many other survey findings, including the fact that many plan advisors discount their own preferences when dealing with TDFs, in favor of what is appropriate based on client preferences or objectives. In addition to the preferences surrounding glide path types mentioned earlier, plan advisors were most likely to reply “it depends” when asked about passive versus active (27%) or open versus closed architecture (46%). Of those advisors who did state a preference beyond deferring to participants’ needs, more advisors stated preferences for a mix of active and passive strategies in a TDF, versus one or the other, as well as a preference for open versus closed architecture funds.



**Percent of plan advisors who believe the following criteria are very important when evaluating TDFs.**

