TIAA-CREF Asset Management

The Goldilocks plan: How big of an investment menu is just right?

Key highlights

- How many investment choices should a plan sponsor offer?
- The answer: it depends.
- Participants are overwhelmed by choice.
- Retirement specialists and plan sponsors should consider a mix of investments.

It's one of the industry's most frequently asked questions: How many investment choices should a plan sponsor offer?

Surprisingly, the answer seems to depend on whom you ask. Nearly 40% of Americans feel they have either too many or too few options in their retirement plan, according to the TIAA-CREF 2015 Investment Options Survey.[1] Almost one in five feel overwhelmed by too many choices, and an equal number feel they don't have enough. It's no wonder plan sponsors and participants both feel confused.

That confusion can have serious consequences. As another TIAA-CREF study revealed, those who feel they have the wrong number of investment choices are also more worried about running out of money in retirement.[2] Nearly two-thirds of those who think they have too many investment choices, as well as 55% who don't think they have enough, are very or somewhat concerned about running out of money. By contrast, 40% of respondents who feel they have the right number of investment choices are "not at all concerned" about outliving their savings.

The question is, what number is the right number? For sponsors to meet their fiduciary obligations, they must offer a prudent selection of investments. At minimum, that includes enough choices to suit a variety of risk tolerances and objectives—from long-term growth to lifetime retirement income. But as sponsors are beginning to realize, more is not necessarily merrier.

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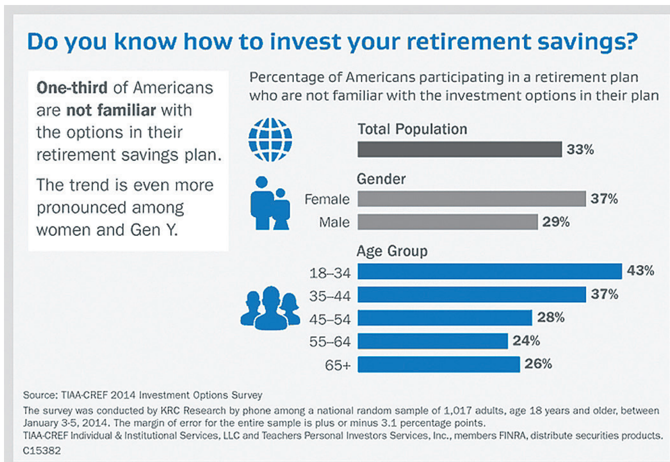
[1] TIAA-CREF, Investment Options Survey, January 2015.

[2] TIAA-CREF, "Fiduciary Responsibility Series, Part 4 Investments: Laying a foundation for lifetime income."

Participants overwhelmed by choice

There is a mountain of research suggesting that having too many options leads to poor outcomes. In psychological experiments, subjects who were offered more choices were less likely to take action than those offered a limited set.[3] Retirement plan investment lineups that are too large actually decrease participation rates.[4] In the TIAA-CREF 2015 Investment Options Survey, nearly 40% of Americans said they were not familiar with the investment options in their retirement plan—an increase from 33% in 2014. As a testament to the alarming magnitude of participants' confusion, 85% said they were comfortable with the choices they made, even though many didn't even understand what those choices were.



Approaching the problem from a different angle

If some participants think their plans offer too few options, and others think they offer too many, perhaps it's time to stop looking for one single answer to suit everyone. Instead, a well-designed investment menu can address the goals and personalities of a variety of investors—from diehard do-it-yourself types to those easily overwhelmed by choice. Such a menu might include:

- Target-date funds, which simplify asset allocation
- Lifetime income solutions, such as annuities, for participants focused on meeting their basic needs in retirement
- Mutual funds for participants who want to create their own mix

[3] Iyengar, Sheena S.; Lepper, Mark R., "When choice is demotivating: Can one desire too much of a good thing?" Journal of Personality and Social Psychology, Vol 79(6), Dec 2000, 995-1006.

[4] Iyengar, Huberman, and Jiang, "How much choice is too much: determinants of individual contributions in 401(k) retirement plans," in O.S. Mitchell and S. Utkus, Editors, Pension Design and Structure: New Lessons from Behavioral Finance, Oxford University Press, Oxford, pp. 83-95, 2004

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With a target-date fund on the menu, any participant who feels dazed by too many options can select a simpler alternative. With a single investment, they can acquire a diversified, professionally managed portfolio, with asset allocations automatically shifted over time to become more conservative as retirement approaches. Target-date funds relieve participants of the need to make complicated investment, portfolio allocation and rebalancing decisions. By their very nature, they can be appropriate for individuals at every life stage, alleviating the need to load up a plan with an excessive number of investment choices. Current investors in target-date funds say they particularly like the lower fees, ease, convenience, professional management and automatic rebalancing, according to the TIAA-CREF Investment Options Survey.

It's important that participants feel they have an appropriate number of investment choices. Too few or too many, and employees' confidence may suffer. However, the secret to designing a plan that's just right—a "Goldilocks" plan—is about more than simply the size of a menu. The menu's structure matters as well. By including target-date funds, you can help even overwhelmed participants feel that their retirement plan fits them just right.

To learn more about growing your business with target-date funds, download our target-date value-add practice management program (**www.tiaa-cref.org/lifecycle**) or call us at **888 842-5433**, option 2.

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