Building a Better Retirement

Five retirement trends to watch in 2024

TIAA

2024

The calendar may have flipped

to 2024, but many of the issues that caused consternation last year are still looming large. Retirement industry decision-makers remain focused on the ramifications of SECURE 2.0 and the challenges of recruiting and retaining talent. Interest rates remain perched near their highest levels in 15 years, causing savers to fixate on the potential for market volatility. The likelihood of an economic recession has ebbed, job creation remains strong and most experts say that the worst inflation is in the rearview mirror. Still, higher borrowing costs may yet take their toll on businesses and consumers.

Our second annual TIAA Trends report examines these economic and regulatory trends and more—such as how HR departments are rethinking their financial wellness programs and the questions they're asking about artificial intelligence.

Related to the design of retirement plans, this year may bring resolution to the cliffhanger left by the SECURE 2.0 Act and give 403(b) plans access to collective investment trusts (CITs), pooled investment accounts long used by 401(k) plans. Separately, a new crop of target-date-fund-like products that feature lifetime income could get fresh attention as a default investment option.

To build this report, we surveyed consultants, plan sponsors and experts in markets, benefits, and retirement trends both within TIAA and elsewhere to identify the major trends we expect to see play out in 2024.

1

Inflation is subsiding, but worries are not.

U.S. economy will keep chugging along in 2024, even as the global economy faces challenges.

The outlook for stock investors in 2024 is mixed. Higher interest rates will likely be a headwind for corporate earnings, and consumer spending may slow too due to higher borrowing costs, slower wage gains and rising delinquencies on credit cards, auto and mortgage loans. But TIAA CIO Neel Mukherjee believes better days are ahead for stocks in late 2024 and 2025.

Inflation has long been top of mind for many workers: TIAA's National Contact Center received more inquiries about inflation than any other topic in 2022, and those fears continued apace into 2023. But our chief investment officer, Niladri "Neel" Mukherjee, believes the price surge kicked off by the pandemic is nearly over and the Federal Reserve may be finished raising rates.

But don't expect rate cuts right away, he says: At 4%, inflation is still above the Fed's 2% target. As such, interest rates are likely to remain at elevated levels for longer than investors and consumers expect.

The immediate outlook isn't terrific for stock investors, who largely shook off 2023's persistently high rates, as well as challenges such as war in the Middle East and Ukraine and a handful of regional bank failures earlier in the year. Better-than-expected corporate earnings and enthusiasm around artificial intelligence (AI) helped drive a 22% total return for the Standard & Poor's 500 through December 11. Mukherjee is less sanguine about stocks for 2024: The lagging impact of higher interest rates will likely be a headwind for corporate earnings, and consumer spending may slow too due to higher borrowing costs, slower wage gains, and rising delinquencies on credit cards, auto and mortgage loans.

In the near term, bonds appear more attractive than stocks from a total return perspective. However, Mukherjee believes better days are ahead for stocks in late 2024 and 2025. The drivers of the next bull market may include:

- Members of the millennial generation aging into their prime years for earnings, consuming, investing and household formation.
- Accelerating innovation as artificial intelligence and robotics get further embedded into business practices, driving productivity throughout the economy.
- Geopolitical differences and national security concerns driving spending on manufacturing, semiconductors and healthcare.
- The transition to the new energy economy, including investments in traditional and green commodities that are projected to be in short supply relative to long-term demand.

2 Meet the new target date funds.

New default options in retirement plans will include annuities.

The all-important default option for defined contribution (DC) plans could start to get a widespread refresh as firms introduce new target date funds that include a fixed annuity or lifetime income component.

The default investment option is a crucial decision since as many as 8 in 10 plan participants stick with the default investment portfolio.[1]

Two factors in 2024 may accelerate consideration of target date funds that include a fixed annuity as part of the bond allocation. First, more plan sponsors are looking to minimize investment risk for employees, especially for those close to retirement. This view has been reinforced by market volatility: Both stocks and bonds fell by double digits in 2022, a one-two punch that delivered a 15.4% decline for the median 2025 target date fund—in other words, a fund that is supposed to be managed conservatively for investors who want to retire in or near 2025. Including a fixed annuity adds diversification beyond the typical split between stocks and bonds, which can help boost risk-adjusted returns, since fixed annuities never lose value. Ensuring a portion of a portfolio will never go down in value, even if the market drops, helps mitigate downside risk for the entire portfolio.

A second factor is that plan sponsors increasingly feel an obligation to help employees generate income in retirement. Many say the best place to generate that income is from the plan: 54% of 401(k) plan sponsors say they would prefer to keep their retired employees' assets in their plan, rather than seeing them rolled into an individual retirement account—more than double the 26% who said the same in 2019.[3]

DC plan sponsors say that both the desire to smooth the ride for savers and help retirees access income are compelling reasons to consider adding the new target date funds as the default option. Urgency is building. A recent Nuveen survey found that more than half of plan sponsors say that adding a "retirement income solution" was the most likely plan change they'd make over the next two years; the second-most popular choice was changing their default investment option.[4]

> "More plan sponsors are looking to minimize investment risk for employees, especially those close to retirement."

In the private sector, where only a sliver of DC plans provide access to in-plan guaranteed income, a survey from trade group LIMRA found that three in four sponsors say they could make a decision on whether to add guaranteed income to plans in the next 12 months.[5]

At the same time, DC consultants are most likely to recommend a target date fund with a guaranteed income component when asked about in-plan retirement income options, according to Cerulli Associates.[6]

[1] Jeremy Burke, Angela A. Hung, and Jill E. Luoto, "Opting out of Retirement Plan Default Settings," Rand Corporation, January 2017..

[2] Morningstar, "2023 Target-Date Funds and CITs Landscape," March 28, 2023.

[3] Cerulli Associates, "Cerulli Edge—U.S. Asset and Wealth Management Edition," April 12, 2023.

[4] Nuveen, "Global Institutional Investor Study," November 2022.

[5] LIMRA, "Are In-Plan Annuities at a Tipping Point?" November 28, 2023.

[6] Cerulli Associates, "U.S. Defined Contribution Distribution 2022: Tailing Solutions to the Consultant-Intermediated Fiduciary Landscape," December 2022.

Figure 4:

Planned changes

Which of the following changes did you make or do you plan to make? *(n = 69)*

54%
Addition of retirement income solution (such as target date type funds that include annuities as part of asset allocation)

35%
Change of primary default investment option (such as target date fund)

32%
Addition of ESG-related investments

25%
Addition of annuity option

29%
Change to plan design/ behavioral nudges (auto enrollment, auto escalation)

28%
Addition of inflation hedge (such as TIPS or other instruments)

28%
Addition of private markets-related investments

Adding an income solution is the top choice for those plans that intend to make changes to their DC investment lineup over the next two years.

3 New year, new options.

A lower-cost investment structure prevalent in 401(k) plans may become available to 403(b) plans.

Collective investment trusts,

better known as CITs, are ubiquitous in the 401(k) industry and barely nascent in the 403(b) world—but that's about to change. An act of Congress could give millions of nonprofit workers access to the same investments, and employers in the 403(b) space are actively monitoring the progress of the new legislation while performing the due diligence for bringing CITs onto their retirement plan menus.

CITs are pooled investment vehicles and set up as trusts that are maintained by a bank or a trust company. CITs are not subject to the same regulations as mutual funds and require less paperwork and marketing costs, leading to savings that can be passed on to plan participants. The fees for CIT funds are often half that of mutual funds, according to research from Morningstar.[7]

In 2017, target date mutual funds comprised 63% of total target date assets, compared with 37% for CIT-based products.[8] By the end of 2023, CIT assets in target date portfolios had overtaken mutual fund assets in 401(k) plans. CITs are already the most popular investment vehicle on plan menus, with 84% of plans offering CITs by late 2022.[9]

Employers with 403(b) plans have to wait until a final regulatory obstacle is removed, which could happen by year end. A new bill, the Retirement Fairness for Charities and Educational Institutions Act, finishes the regulatory approval details that the passage of the SECURE 2.0 Act began in December 2022. Once that barrier is removed, it may not take long for CITs to become the dominant menu item among 403(b) plans.

Lisa Frace, Michigan State University CFO and treasurer, says that if CITs can save participants more than 20 basis points in fees—that's $200 for every $100,000 invested—the university would certainly take a closer look, but that discounted costs don't necessarily mean faster adoption.

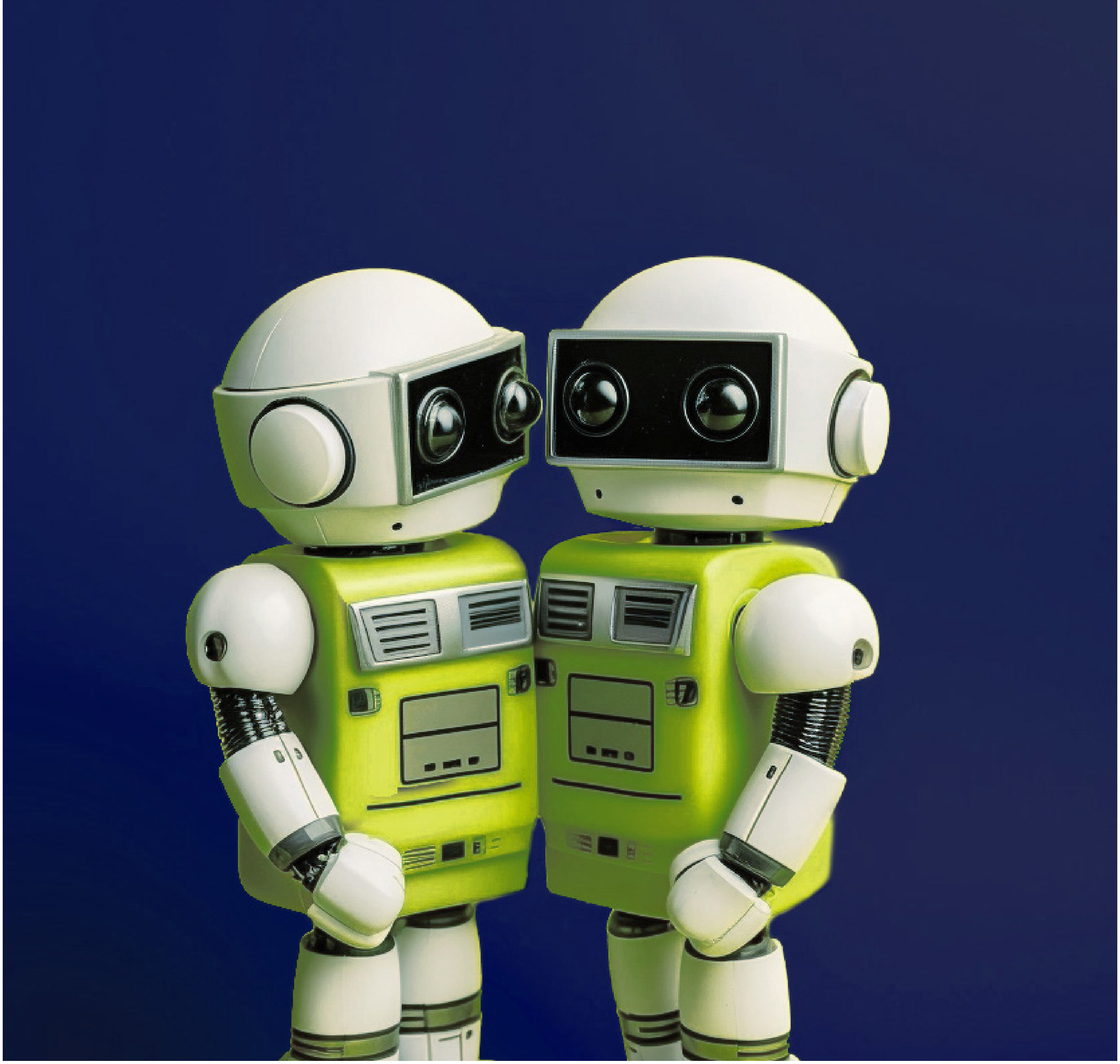
"We would want to be sure we continue to provide appropriate fiduciary oversight and support," Frace says, "including tracking performance, understanding the unique aspects of CITs, education for those interested, and any required regulatory or legal disclosures."

[7] Morningstar, "CITs: A Welcome Addition to 403(b) Plans" June 2020.

[8] Sway Research, "The State of the Target Date Market: 2023 ".

[9] Callan, "Defined Contribution Trends Survey," 2023.

401(k) Plans Offering CITs



4 The robots are coming for your retirement.

AI will increasingly be used to drive customization of products and services.

In 1947, British mathematician and WWII-era code breaker Alan Turing, credited as the father of artificial intelligence, distilled the concept in a lecture: “What we want is a machine that can learn from experience.”

Today, Turing’s incredible idea of smart computers is making strides across all aspects of culture. More advanced than its preprogrammed precursors, modern AI can “learn” from past experiences and make inferences drawn from the wide body of information available instantly on the internet.

Universities have already been facing the downsides of AI among the student population. “The new generation of AI in ChatGPT can now fool any software designed to identify AI-generated term papers, essays,” Ethan Mollick, AI lecturer and associate professor at the Wharton School of the University of Pennsylvania told attendees at a recent TIAA Institute event. “Anyone who tells you that their software can ferret out AI-created documents is lying.”

The ability to compose credible term papers, however, is more like a parlor trick compared with AI’s potential to lower costs and drive efficiencies for CHROs. Enthusiasts like Mollick say that in the next three years AI will:

- Reduce the labor cost of operations through call centers and other areas.
- Increase financial literacy and customize advice for plan participants.
- Customize plans for individuals in IRAs.
- Improve retirement plan design to make them more customized for the individual participant.

The attendees at the Institute event were intrigued, though cautious. Many appreciated the potential to drive down costs but were wary of technology replacing humans.

U.S. regulators have yet to weigh in on how various industries can use AI, yet it’s being adopted in a variety of ways. At hospitals, AI technology has been used to make instant and accurate patient diagnoses. In the retirement industry, AI is being implemented in call centers. TIAA, for example, recently announced that it will deploy AI technologies at its National Contact Center to enhance client experience, optimize self-service and improve analysis for more effective interactions.

AI will continue to grow as a tool, but it’s not likely to replace anyone reading this piece any time soon.

5 Forget the massage. Financial wellness is real self—care.

In a tight labor market, employers are getting personal about money.

More than half of full-time working Americans point to money as their top stressor, according to a 2023 PwC survey.[10] Anxiety levels are higher today than during the pandemic in 2021. The laundry list of financial worries includes escalating housing costs, student loan debt and retirement insecurity.

What's more, financial anxiety is consuming more of workers' time. According to research at the TIAA Institute and the Global Financial Literacy Excellence Center (GFLEC), the average American spent eight hours a week on financial matters in 2023, half during the workday. That's up from seven hours in 2022 and 2021. And it's even higher among those with lower financial literacy.[11]

Employers are increasingly feeling the financial pressure of their workers. A historically tight labor market and the desire to attract and retain a diverse workforce are pushing HR departments to adopt recruiting strategies that emphasize personal finance.

HR leaders are no strangers to financial wellness programs, but experts say their approach may need to change. Efforts to create a more diverse workforce must include accommodating different backgrounds, career paths and personal circumstances.

"Personal finance is personal," says Annamaria Lusardi at Stanford University and director of GFLEC. "In reality, we're all different, but for too long we've taken a one-size-fits-all approach to financial wellness. Personalization is critical."

Many employers see personalization as the next important step to evolving their financial wellness programs. Temple Health in Philadelphia is one example. According to Frederick Berger, vice president, benefits and retirement administration, employees have responded positively to programs aimed at student loan debt relief and retirement planning because it's relevant to their lives. "Now we need to continue to iterate on that success with other programs that match the unique financial circumstances of our employees and their families," Berger says.

> "Finance is for everyone, and with a focus on wellness, we can achieve our best in life."

But resources remain a factor at many organizations. More than one in three employers say cost is the biggest barrier to adding financial wellness programs, according to EBRI.[12]

Chianoo Adrian, managing director of new solutions and partnerships at TIAA, recommends employers focus on helping employees with the most immediate needs, such as spending and debt management, which may be barriers to saving, investing and income protection. "It all depends on where employees are in their financial lives," Adrian says. "Gains in one area can lead to improvements elsewhere, with the ultimate goal of better retirement readiness."

For Lusardi, it all comes back to overcoming the anxiety. "We need to take away the barriers to financial well-being," she says. "Finance is for everyone, and with a focus on wellness, we can achieve our best in life."

[10] PwC, 2023.

[11] "TIAA-Institute-GFLEC Personal Finance Index," 2023.

[12] EBRI, 2022.

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