Q2 2021

ACTIVE VOICE *from Putnam Investments*

Retirement savings system alive with innovation

Q&A with Steven McKay, Head of DCIO, Putnam Investments

In this edition of *Active Voice*, Cathy Saunders, Head of Public Policy and Advocacy, hosts a conversation with Steve McKay, Head of DCIO at Putnam Investments, on current efforts to strengthen the workplace retirement savings system in the United States.

Putnam is establishing a business channel around defined contribution investment only [DCIO], and you're now reporting to CEO Bob Reynolds. You seem to have a deep passion and commitment to the DC savings space.

I've spent my whole career in DC savings, going back to 1993. My first job was in an individual retirement account [IRA] call center. Having a direct connection to individual retirement plan participants and working to improve outcomes for them still inspires me. Putnam has long a history in the retirement plan business, and the DCIO business is a strategic priority for the firm. We've been in growth mode for the past five years, drawing on expertise from across the organization, collaborating on thought leadership, product development, distribution — it's an exciting time.

I joined a recent panel on the impact of Covid-19 on DC savings at the joint U.S. Public Policy Conference of the SPARK Institute and Defined Contribution Institutional Investment Association [DCIIA]. I was struck by several industry studies showing that, in spite of the stock and bond market volatility of early 2020, most savers did not reduce their levels of deferral, nor did they alter their allocation strategies. What does this say about the system?

It's an extremely stable system, as it should be. We also saw last year that only a small number of savers took early withdrawals, despite a temporary suspension of penalties from the U.S. government. This adds to what we learned many years ago in the 2000 tech bubble collapse and the global financial crisis in 2008: DC savers understand temporal volatility, dollar cost averaging, and the power of compounding. Behavioral defaults, automatic enrollment, and automatic allocation to strategies like target-date funds [TDFs] — which are currently 70% of U.S. 401(k) inflows[1]— are very powerful. All these advancements over the years have contributed greatly to improving participant outcomes. And the system is about to get a lot larger and more innovative.

1 Sarah Holden, Jack VanDerhei, and Steven Bass, "401(k) Plan Asset Allocation, Account Balances, and Loan Activity in 2018," EBRI Issue Brief, no. 526, and ICI Research Perspective, vol. 27, no. 2 (March 2021).

Tell me more! What are some of these innovations?

We are about to experience the advent of open multiple employer plans [MEPs], also known as pooled employer plans [PEPs]. Companies can band together in a group 401(k) plan to gain economies of scale, simplify administration and reporting, and shift fiduciary liability to pooled plan providers [PPPs] led by dedicated plan professionals from the financial services industry. Savings rates have been stable and at high levels for workers in plans. But millions of Americans still do not have access. We think MEPs could result in a notable expansion of workplace plan coverage, particularly among small and medium-sized companies.

Over the years, we've seen a lot of innovation in retirement plan design and recordkeeping, particularly the rise of behavior-driven "automaticity" you mentioned. Today, does it seem the innovation energy has rotated to the asset management side?

Absolutely. Putnam has always been an innovator in the DC space — in asset management as well as in recordkeeping. A great example was our 2014 decision to unify the retirement businesses of Great-West Financial and Putnam Investments under Empower Retirement. Empower is a leading recordkeeper where I worked before returning to Putnam to lead the DCIO business in 2016.

For more than a decade, Putnam has been a leader in stable value [capital preservation], core equity, and target-date funds. These are all key strategies for retirement savings. We have also developed leading ESG [environmental, social, and governance] capabilities, an approach that is becoming more important to DC savers. And we've delivered these strategies through multiple "wrappers," including collective investment trusts [CITs], which are becoming a more popular investment vehicle for ERISA-regulated plans.

In a major innovation, we're seeing workplace savings strategies that can be designed for individual savers — some are calling this "mass customization." It begins with an assessment of individual savers' financial circumstances. This means their retirement savings, out-of-plan financial assets, their unique expenses and liabilities, anticipated educational or health expenses, and, perhaps, the income from a private defined-benefit pension. It's then a matter of applying financial-planning optimization technologies that take all of these factors into account, informing participant decision-making as they allocate their dollars across retirement and other benefits.

We see this as massively empowering for financial advisors. These investment strategies might be delivered through advisor-managed accounts [using both mutual funds and CITs] or they could be included in a "custom TDF" designed for individual savers. With the right data and technology, we could see "truly" personalized glide paths as the next evolution of target-date funds.

One of the most dynamic areas of financial product development turns on the withdrawal strategies or "decumulation" of assets in retirement. For years, the industry has focused on accumulation. But now, with $20 trillion in DC savings and baby boomers beginning to retire, are we seeing greater demand for support in retirement decision-making?

We sure are. There won't be a silver bullet for lifetime income — whether guaranteed or non-guaranteed. So, we favor an "open architecture" approach that might include traditional annuities, deferred income annuities [DIAs], and qualified longevity annuity contracts [QLAC]. We're also seeing new developments around algorithmic drawdown strategies, which is more of a technology play on optimizing withdrawals. Every retirement saver is unique and will deploy these strategies in their own way.

Will TDFs play a crucial role in the retirement phase?

With the advent of the Secure Act [2019], regulators gave the go-ahead for the industry to incorporate lifetime income strategies into workplace plans, bringing us closer to a holy grail of the retirement trade — retirement savings products that take savers not only "to" but also "through" retirement.

Some 40 million retirement savers hold target-date funds in their 401(k) plans; TDF strategies today account for most default investments in 401(k) plans; and total assets reached $2.8 trillion at year-end 2020.[2] The landscape of TDF products is expanding in both the number of funds and the diversity of their strategies, so clearly, they will play a role. Providing a personalized glide path right down to the participant level may be the future growth engine for target-date managers.

The solution for managing savings during retirement will turn on a combination of elements aimed at reducing longevity risk while retaining appropriate market exposure. The goal is to finance what could be a multidecade retirement. Many of these strategies will be incorporated into TDFs.

The number one priority of retirement savers is that they don't want to "outlast" their money. To provide this security, recordkeepers, asset managers, and financial advisors will all play a role. We need input from all three to make it happen.

2 Morningstar, 2021 Target-Date Strategy Landscape Report, https://www.morningstar.com/lp/tdf-landscape.

TargetDateVisualizer® — Greater perspective on retirement investing

New, dynamic lens on TDF glide paths, equity sensitivity, and performance

Putnam's TargetDateVisualizer guides advisors to select target-date mutual funds and collective investment trusts for use in workplace savings plans. Based on specific preferences for risk tolerance and investment philosophy, the tool provides transparent insight into the underlying investment glide paths of over 100 different TDF strategies and brings to light portfolio risk levels and key performance characteristics.

The tool ranks TDF strategies based on how aggressive or conservative advisors and plan sponsors would like to be in the early and late stages of participants' working lives — helping to clarify underlying glide paths, investment composition, and equity sensitivity at critical points along the glide path: the right level of risk at the right time.

For informational purposes only. Not an investment recommendation.

This material is provided for limited purposes. It is not intended as an offer or solicitation for the purchase or sale of any financial instrument, or any Putnam product or strategy. References to specific securities, asset classes, and financial markets are for illustrative purposes only and are not intended to be, and should not be interpreted as, recommendations or investment advice. The opinions expressed in this article represent the current, good-faith views of the author(s) at the time of publication. The views are provided for informational purposes only and are subject to change. This material does not take into account any investor's particular investment objectives, strategies, tax status, or investment horizon. The views and strategies described herein may not be suitable for all investors. Investors should consult a financial advisor for advice suited to their individual financial needs. Putnam Investments cannot guarantee the accuracy or completeness of any statements or data contained in the article. Predictions, opinions, and other information contained in this article are subject to change. Any forward-looking statements speak only as of the date they are made, and Putnam assumes no duty to update them. Forward-looking statements are subject to numerous assumptions, risks, and uncertainties. Actual results could differ materially from those anticipated. Past performance is not a guarantee of future results. As with any investment, there is a potential for profit as well as the possibility of loss.

Target-date strategies: Each target-date pooled vehicle has a different target date indicating when the pooled vehicle's investors expect to retire and begin withdrawing assets from their account, typically at retirement. The dates range from 2025 to 2065 in five-year intervals. The pooled vehicles are generally weighted more heavily toward more aggressive, higher-risk investments when the target date of the trust is far off, and more conservative, lower-risk investments when the target date of the pooled vehicle is near. This means that both the risk of your investment and your potential return are reduced as the target date of the particular pooled vehicle approaches, although there can be no assurance that any one pooled vehicle will have less risk or more reward than any other pooled vehicle. The principal value of the pooled vehicles is not guaranteed at any time, including the target date.

Mutual funds are offered and distributed by Putnam Retail Management. Collective investment trusts are managed and distributed by Putnam Fiduciary Trust Company, LLC ("PFTC"), a non-depository New Hampshire trust company. However, it is not FDIC insured; is not a deposit or other obligation of, and is not guaranteed by, PFTC or any of its affiliates. Collective investment trusts are not mutual funds registered under the Investment Company Act of 1940, and units are not registered under the Securities Act of 1933. Collective investment trusts are only available for investment by eligible, qualified retirement plan trusts, as defined in the declaration of trust and participation agreement.

Investing involves risk, including the loss of capital.

Investors should carefully consider the investment objectives, risks, charges, and expenses of a fund before investing. For a prospectus, or a summary prospectus if available, containing this and other information for any Putnam fund or product, call your financial representative or call Putnam at 1-800-225-1581. Please read the prospectus carefully before investing.

A world of investing.®

Putnam INVESTMENTS