nuveen
A TIAA Company

Investment Corner | Participant Engagement | Fiduciary Perspective | On the Horizon

Securing income through retirement

The future of defined contribution

next

Issue no. 8

next / *The future of defined contribution*

A change of plans

Dare we say, it feels like we're inching toward the next normal of a post-pandemic era; however, we will no doubt feel the impact for years to come. Today's labor market is just one example. US employees left their jobs in record numbers in 2021 and employers found themselves rethinking their benefits, including retirement plan design, as one way to help them in the war for talent.

In this issue of *next,* we'll explore topics making news in the defined contribution (DC) world as potential ways to innovate plan design. First, we'll discuss the increasing importance and innovation around guaranteed income in 401(k) plans. These capabilities are gaining more and more traction in the market. Next, we'll call out what to watch for, from a fiduciary perspective, within the upcoming Department of Labor environmental, social and governance (ESG) ruling, as ESG continues to grow as an increasingly important topic for employees. Third, as employers and employees grapple with returning to work, we seek to offer guidance on the flexible office/remote environment, and what steps might possibly be taken by employers to help employees, and plan participants, remain engaged. Finally, we look at the headline-making world of cryptocurrency and examine the impact of this rapidly evolving technology on DC plan menus.

We are in a period of rapid change for financial markets, but one constant is the role of a fiduciary. Our quest remains to direct clients towards securing income, addressing the basics of retirement early and repeatedly, and to strip away complexity where possible. This issue of *next* aims to bring together the right insights, resources and people to offer meaningful education and clarity.

Your Nuveen Team

INVESTMENT CORNER

Securing income through retirement

As employers continue to navigate the great resignation and subsequent war for talent, more and more are looking to their benefits packages, especially their defined contribution plans, as a strategic tool to help attract and retain talent. In doing so, there is increased interest in plan design innovation and a focus on participant outcomes. One area where we see significant potential for innovation and differentiation, fueled by growing attention from Washington D.C., is retirement plans incorporating guaranteed lifetime income.[1]

50%

of workers aged 60 and older now plan to work until they're at least

70 years old[2]

Continuous income in retirement

The disconnect between current retirement plans and the need for an income element goes back to the origins of the 401(k), which was never meant to entirely replace defined benefit retirement programs. In the 1980s and 1990s 401(k) plans were supposed to provide a supplemental savings arrangement to complement lifetime income from defined benefit (DB) plans. However, due to multiple factors, including DB liability actuarial funding challenges, the allocation of investment risk to individuals, the fact that newer generations of the workforce are not staying with a single company throughout their careers, and the abandonment of those DB plans at prior companies, the traditional DB pension plan all but disappeared.

This has shifted the burden to the participant. For example, the generation nearing retirement today likely does not have a defined income benefit to their retirement planning beyond social security. They are likely to just receive the lump sum from their defined contribution plans upon retirement that they will not only have to figure out how to invest prudently, but also make this sum of money last through their (unknown but increasing) lifespan. What is known is that at least 50% of workers aged 60 and older now plan to work until they're at least 70. And this additional delay in retiring can add to an employer's incremental costs.

Increasing life expectancy (if you remove the opioid crisis and the pandemic from the calculations) means that there are an increasing number of retirees facing a shortfall of predictable guaranteed income for life as they approach retirement. This is a problem that has the attention of Washington, D.C., and it is an area that plan sponsors have to decide now how they want to approach and solve.

The Setting Every Community Up for Retirement Enhancement Act (SECURE Act) passed in 2019 laid the groundwork, and worked toward a path for plans to offer guaranteed retirement income to participants. The Act included improved safe harbor protection for the inclusion of annuities within a 401(k) plan, which is a significant innovation in plan design. There were also sections that helped to address some of the portability concerns of lifetime income vehicles that were an ongoing issue. As a supplemental measure, the Act also requires plans to give participants projections of their current account balance as a monthly income benefit using assumptions prescribed by the Secretary of Labor. This illustration shifts the focus away from a lump sum payout to a projected, dependable monthly income stream, possibly helping participants realize the simplicity of and need for guaranteed income through retirement.

Without enhancements, the current 401(k) system poses several significant risks to participants. One is that participants will gain penalty-free access to a large (hopefully) sum of money without the expertise and discipline needed to make it last through retirement. There are multiple anecdotes explaining this risk, such that a participant upon gaining access to this sum sees it as a windfall cash prize akin to a lottery win, rather than a pool of assets that need to be carefully apportioned out to last throughout an indefinite period of retirement. This risk is one of financial education and a risk associated with misunderstandings of how retirement planning and asset allocation need to account for ever-increasing life expectancy and unexpected expenses.

The second significant concern is an investor realizing that they would like to apportion a percentage of their 401(k) balance to a vehicle like an annuity, to generate a portion of their retirement income that's guaranteed for life, but that the participant does not realize that they may already have access to institutionally priced annuities and other comparable vehicles within the structure of their 401(k). Instead the participant transfers a portion of the balance to a retail-priced annuity and may pay commissions or expense loads.

The solution: institutional priced annuities inside retirement plans

Keeping the participant's assets within the 401(k) ecosystem (not necessarily in the plan upon retirement), with the fiduciary oversight that accompanies that, and with the access to institutionally priced offerings, is key to helping participants grow and protect those assets. Further, if an in-plan annuity option is available, it can allow them to generate guaranteed retirement income. We see the 401(k) market bifurcating over the next decade or so into two types of plans: one is the current model of 401(k), which is simply a tax-advantaged savings plan. The other is a "retirement income" 401(k) plan, which provides participants with a holistic view on retirement income strategies, arms them with the tools needed to optimize their outcomes and allows them to use a portion of their balance to select guaranteed income for life in order to replace a predictable paycheck in retirement.

A significant consideration and way to communicate the need for lifetime income to participants is to evaluate recurring living expenses in retirement against guaranteed income from Social Security and, if available, a DB pension, and focus on covering the gap with income through an in-plan annuity product. Although we believe that fears that Social Security is going to go bankrupt are overblown, we do believe that it's likely that American workers in the future will receive less from Social Security than today's retirees. Additionally, we think that the amount of income generated from Social Security is not enough to fully replace essential income in retirement.

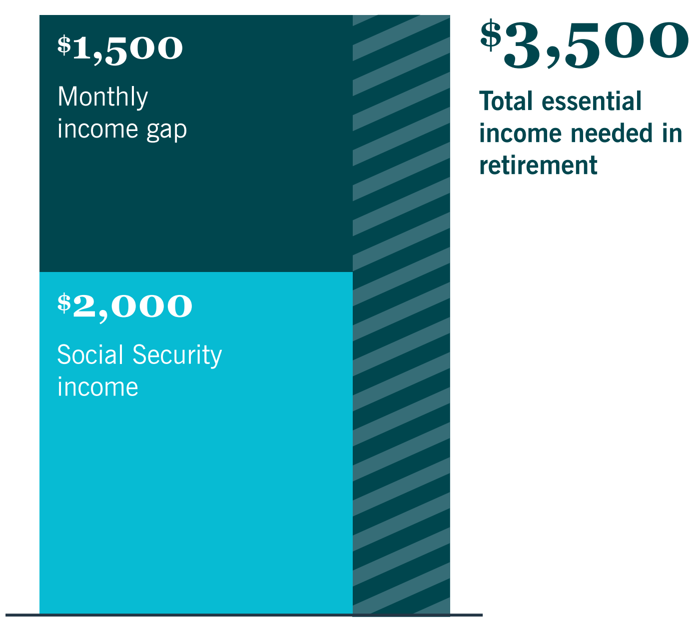
FOR EXAMPLE:

If Social Security provides $2,000 a month in retirement, but a participant has calculated that they need $3,500 to meet their essential expenditure, there needs to be a fresh element that amplifies guaranteed monthly income to cover the $1,500 gap and provide peace of mind.

It's important to note that participants shouldn't be expected to annuitize their entire 401(k) balances. The annuitization of a portion of a 401(k) balance can provide the missing link and fill the income gap. This then allows for discretionary income to be allocated from the rest of the 401(k) and its remaining balance. We believe the right method is to calculate the necessary monthly income required in retirement and annuitize to generate that monthly income. The calculations will be different for each participant but this shifts the burden away from just relying on the balance of a 401(k) to be managed through retirement.

FIGURE 1

In order to meet expected monthly expenditures, many retirees will need to supplement Social Security



These figures are for illustrative purposes only.

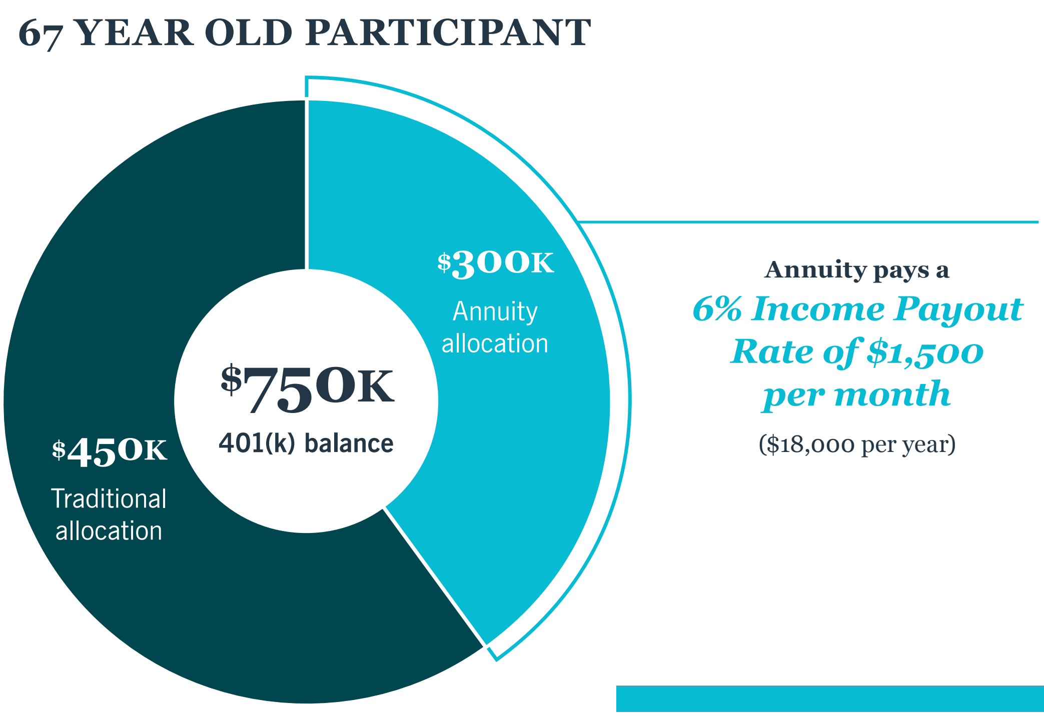
FOR EXAMPLE:

A 67 year old participant with a $750,000 401(k) account balance might annuitize $300,000 (40%) through a fixed annuity covering their own life product at age 67, and for illustrative purposes, let's say the annuity pays them $1,500 per month (i.e., $18,000 per year, or a 6% Income Payout Rate); they've created a more solid foundation of predictable income for life to complement Social Security and can meet their recurring living expenses.

As such, they can leave the remaining $450,000 invested and take systematic withdrawals, use it for discretionary purposes, emergency expenses, or pass down to heirs.

FIGURE 2

Participants may be able annuitize a portion of their 401(k) balance and achieve potential lifetime income



These figures are for illustrative purposes only.

It's important to note that participants shouldn't be expected to annuitize their entire 401(k) balances.

How plan sponsors can implement annuities

The ability to include guaranteed income in 401(k) plans is not a new concept, but is nascent in terms of actual implementation. As the legislation and best practices evolve in this regard, there will likely be two broad approaches taken by plan sponsors.

One idea is to approach securing income in retirement accounts in a way that simply checks the box ("yes we offer lifetime income"). This can be as simple as adding optionality to target date funds with a Single Premium Immediate Annuity (SPIA) or a Deferred Income Annuity such as a Qualified Longevity Annuity Contract (QLAC) available to be used to purchase lifetime income at retirement with a portion of a balance. This approach has the benefit of simplicity as the participant can convert a preset portion of a 401(k) balance into a lifetime income stream once the participant reaches the declared start date. We see this as the option that plan sponsors will choose if they want to say that they are offering something. It is better than nothing, but it is not a fully integrated plan that truly meets the needs of participants to guarantee lifetime income in retirement.

We see the second option as realizing the true benefit of wrapping income into a 401(k) plan throughout the participant's savings and investment journey in a much more integrated way. This would include an annuity that participants invest in during their entire working career that's coupled with robust education and lifetime income projections so that participants begin to think of a portion of their 401(k) balance as an income amount. By exposing the annuity vehicle to the participant earlier in their career, this can allow for the growth in accumulation units over a much longer period which can translate to more lifetime income in retirement.

This touches on one final consideration, which is the matter of timing and frequency of annuitization. For some products, the annuitization option is an all-or-nothing decision at retirement and if the interest rate environment isn't favorable then participants might get less income than if they waited several months to convert to lifetime income. However, there are other annuity vehicles that allow participants to annuitize multiple times during their retirement. In addition there are products that allow participants to select multiple payment frequencies to meet their financial needs. The benefit of an integrated annuity offering within a 401(k) plan is that participants become accustomed to thinking about lifetime income and with the right product with the right flexibilities coupled with expert guidance, a participant annuitizing through a 401(k) plan can have the same peace of mind in retirement that their parents with DB pensions had. After all, it's not likely that many DB pension recipients are dismayed when their income payment shows up in their bank account every month!

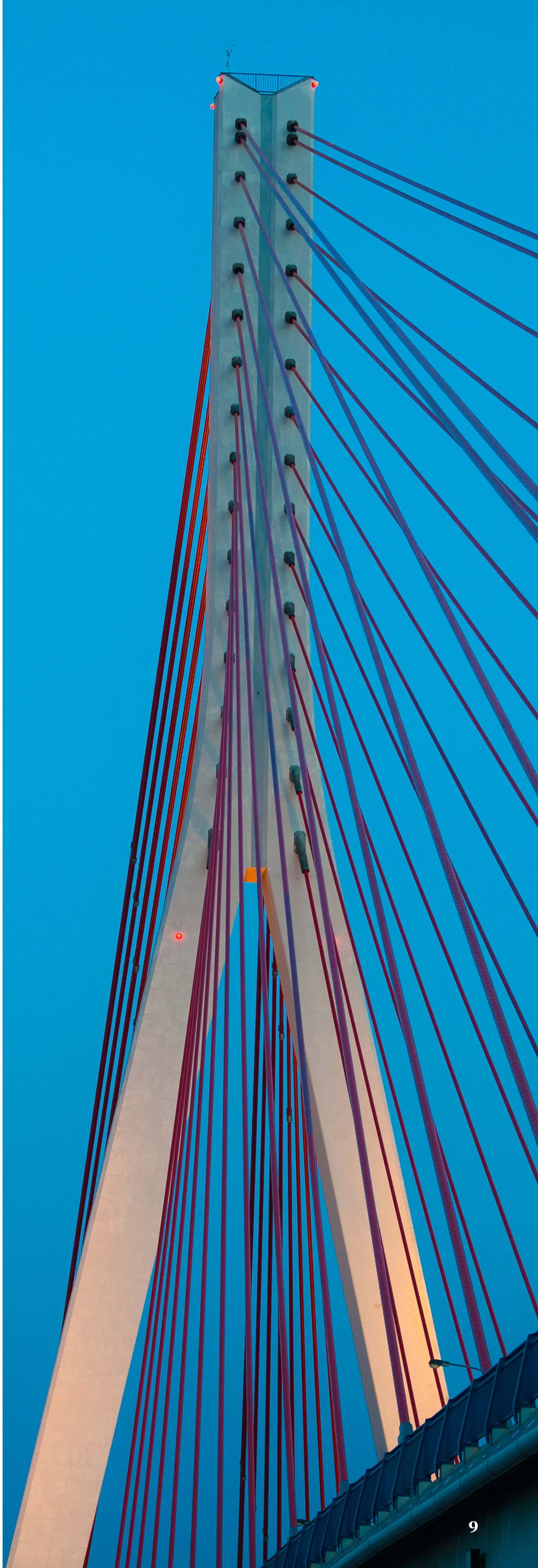
The SECURE Act is providing safe harbor for annuities, and we believe that we could see significant growth in annuities as a result.

Providing the security of a paycheck

To conclude, including guaranteed income more broadly in DC plans is a way of redressing the balance that shifted when defined benefit plans faded away. Increasing numbers of participants are entering retirement without a guaranteed income stream, and many are ending up going back to work to supplement retirement funds. Annuitizing a portion of a retirement balance can provide the second income that a job in retirement could, guaranteeing that income for the lifetime of the participant. It can provide the security of a paycheck in a way that participants are used to.

The inclusion of a guaranteed income element within a 401(k) plan is a development that is an inevitability. It has the attention of Washington to the extent that it is a matter of when, not if, new legislation is passed. The time is now for plan sponsors to start to think broadly about their retirement benefits philosophy and how a strong 401(k) “retirement income” plan can attract and retain talent. The sooner they can address questions of integration the better. Plan sponsors who are aligned on the value of in-plan, institutionally-priced lifetime income need to start addressing these questions to determine what partners they want, what technology providers they wish to integrate, and to what level of depth they want the integration to occur. There are still technological developments occurring in this area to allow for seamless integration into plans, and making the process as simple as possible for participants is most likely to lead to significant uptake, but work is developing rapidly.

In 2005 there were approximately $70B allocated to target date funds. Then the Pension Protection Act was passed, which provided safe harbor for asset allocation products. Now there is almost $3T allocated to target date funds. The SECURE Act is providing safe harbor for annuities, and we believe that we could well see similar growth in annuities as an asset class as a result. Plan sponsors have to decide now how they want to approach this coming change and how dignified a retirement they want their workers to be able to enjoy.



PARTICIPANT ENGAGEMENT

The challenge of being remote

for plan sponsors and participants

The pandemic has been a stressful period for plan participants and plan sponsors alike. Particularly jarring was the sudden end to the traditional office environment, with many of us moving to a work-from-home environment incredibly quickly sometime in March 2020. This has resulted in a more challenging workplace environment from an efficiency angle, as meetings, workflows and productivity has shifted to remote offices, Zoom calls with wandering cats and spouses and unmuted mics. There is growing awareness that employees have been under a particular period of stress lately.

A recent study from TIAA highlighted some of the difficulties people faced during the pandemic, and the overall encroachment of digital into our lives. The study found that half of Americans spend less than one hour a week on their finances, while spending more than four hours on social media. The study also found that the pandemic has significantly impacted Americans' financial wellness and financial habits, with one in three stating that their household finances have been negatively affected and over 40% feeling as though they need to manage their finances more closely.

63%

OF EMPLOYEES SAY

that their financial stress has increased since the start of the pandemic.[3]

Corporate culture has been one area that has suffered. There have also been struggles to onboard new employees, and engage current employees from a benefits and retirement planning perspective. Broad engagement had to shift from in-person meetings to remote and digital, without much time given to manage the transition. In fact, 2/3 of employees report having one foot out of the door, stating they are likely to job hunt in 2022. Further, 72% of employees would be attracted to another firm if they saw that it cared more about their financial well-being.

Plan sponsors have begun thinking about their retirement benefits as a strategic way to help attract, retain and engage their employees in an effort to improve their overall culture.

Helping participants meet their financial goals in a time efficient manner should be a priority.

There is also an emotional and mental wellbeing element that cannot be ignored. There is an extent to which we need to start utilizing new messaging and language that includes a nod to mental resiliency, while tying that back to retirement planning and financial management. Providing encompassing messaging on emotional and mental wellbeing will help to let employees know that what they are experiencing is human and normal. Everyone's life has been in a period of extreme flux and stress since March 2020. Keeping one eye on shortages at the grocery store has become a point of emotional stress, let alone planning decades into the future to keep an eye on retirement planning.

That stress has led to an upheaval of the conversations around financial planning, access and knowledge of benefits and overall mental and financial health. The impact of the pandemic on how employees interact with their firms has been profound, and there are more questions than ever from employees on what their firms can do to help, both longer-term and in the very immediate term.

What can plan sponsors do?

Plan sponsors know their employees have had a lot to deal with and focusing on the long term has been a challenge for the last couple of years. Below is a list of actions plan sponsors can take to help employees refocus on retirement.

Many are well known, but worth restating:

- Increase participation in the plan through auto enrollment and automatic contribution increases. If this isn't feasible, promote plan participation during new employee onboarding and as a part of your annual benefits renewal.
- Simplify your investment menu to potentially lower costs and reduce confusion for employees who choose their own funds by eliminating redundant asset classes.
- Set up your match to encourage greater saving without affecting your budget (e.g., offer a 50% match up to 12% of salary vs. 100% match up to 6% of salary).
- Add the flexibility of after-tax saving through Roth contributions.
- Provide easy online access to retirement plan accounts that includes performance and projected income.

These steps help alleviate the stress of engaging with retirement planning from employees at a time when they are already focused on multiple other aspects of their lives.

One way to focus the engagement with employees in this new era is to absolutely maximize the use of technology. Digital tools have come to the forefront of engagement over the last couple of years, to the detriment of in-person events.

There are a range of ways to engage with participants that have been utilized over recent months that make use of digital engagement technology. Webinars examining the link between the pandemic and market volatility, and reassuring investors that focusing on the long-term and managing through volatility is one way to engage and educate. Virtual financial counseling and benefits fairs should also be encouraged, which allows for either broader-reaching or more personal attention to financial matters. These methods again encourage participants to engage on matters of financial planning, while not adding to already elevated burdens.

However, we do know that some participants are checking their balances, adding to contributions and using available tools to help visualize their income in retirement. These participants are using available tools, such as income calculators, to try to figure out what they'll have in retirement.

While there is definitely a drive to get back to being in-person, many offerings should be shifted to a digital delivery to allow for greater participation and replayability. Since the pandemic began the use of videos has exponentially grown as a way to engage employees. Studies indicate that video conversations with advisors can be very effective since employees engage more when there is a visual component to interactions. Webinars are also another educational and interactive tool that are available. Long-term there is a pattern that will drive many in-person meetings again, once that is possible. In the meantime we find ourselves in a hybrid state of in-person and digital, but our focus has to be on providing the best tools to plan participants.

FIDUCIARY PERSPECTIVE

What to watch for *in the* DOL's upcoming ESG ruling

The more things change, the more they stay the same. This adage may come to mind when thinking about Washington's guidance on the factors an Employee Retirement Income Security Act of 1974 (ERISA) retirement plan fiduciary may consider when selecting investments for plan menus over the years. At the risk of oversimplifying, the guidance over the years is usually less about WHAT the critical factors are and more about HOW to consider factors as investment innovations continue to occur. This is especially true in terms of considering environmental, social and governance (ESG) factors.[4]

Over the past 30 years *(since the Clinton Administration), views on how fiduciaries should consider investments using ESG factors for inclusion in their plans have fluctuated with each new Administration. Regardless of advancements and innovation in ESG reporting, the guidance typically toes the party line. Republican administrations have typically used language that is more skeptical in their guidance while language from the Democrats' positions have been more accepting of ESG factors.*

The status quo of ESG rulings

The newly proposed version of the ESG rule, anticipated to be released by the Department of Labor (DOL) as early as this summer, would make changes to the current version, which was finalized in 2020 during the Trump Administration. Specifically, it's expected to provide guidance on the various factors a plan sponsor may consider when choosing investment options for plan menus, and seeks to roll back some of the language in the current rule that may be interpreted to have a chilling effect on plan fiduciaries' willingness to include ESG investments, forgoing the potential value those investments can bring to participants. There is general agreement across much of the retirement plan and investment management industries that the current proposal addresses many of the outstanding issues from the 2020 rule and would open up many more options for plan fiduciaries to include pertinent ESG factors when determining investment options.

Up until the Trump Administration, Washington's views were expressed as less binding "regulatory guidance" as opposed to the formal rules we've seen in 2020 and 2021, which are more binding and therefore more onerous to reverse or change. The hope is that the new version of the rule, when finalized, will contain sufficiently neutral language as to give it longevity across future presidential administrations; but there is still some risk that a future Republican administration could attempt to change the rule again if it is seen as too accepting of ESG.

For context, the DOL's 2020 rule (Financial Factors in Selecting Plan Investments) was actually less extreme than the proposed version of that rule. While the proposal did not outright prohibit plan fiduciaries from considering ESG factors, it included language that seemed to question whether such factors could be financially material. However, all references to "ESG" specifically were removed from the 2020 rule. The remaining language was much more neutral. It is encouraging that the final rule that emerged from the DOL under the Trump Administration was relatively balanced and aligned with prior DOL guidance regardless of administration. Perhaps this is an indicator that the new rule will be similarly even-handed, which will make it more likely to have a long shelf life.

i

See the comment letter we submitted to the DOL

Key points to look for

Specific examples

The new proposed rule included specific examples of factors that could be considered by plan sponsors when selecting investments for plan menus. Of note, all of the examples cited by the DOL were ESG-related, causing some commenters to wonder if the new rule might be too focused on ESG. We will be interested to see whether the final rule removes these ESG examples, adds additional examples that are not ESG-related or maintains the originally proposed examples.

Qualified Default Investment Alternative (QDIA)

As we stated in our comment letter, the DOL's proposal to remove the current prohibition on using ESG investment options as QDIAs, or as part of a QDIA, is one that we enthusiastically support. Removal of the QDIA provision was supported by many others in the industry as well. We expect to see it included as part of the final rule.

Tie breakers

The new proposal seeks to amend the so-called "tie-breaker test," which plan fiduciaries can use to guide their selection of an investment option when they deem two investments to have identical financial benefits for the plan and its participants. Under the new proposal, a plan fiduciary can break the tie by considering "collateral benefits other than investment returns," so long as those collateral benefits "equally serve the financial interests of the plan over the appropriate time horizon." This may give plan fiduciaries another opportunity to incorporate ESG factors into their investment selection process, to the extent they are faced with a tie between two investment options where ESG considerations are in play. However, some commenters argued that the tie-breaker test is rarely if ever used in practice, and questioned the wisdom of including it in the new version of the rule at all. We will be watching closely to see how the DOL decides to address this issue in the final rule.

FIGURE 3

Perception of employers who offer RI on retirement menu

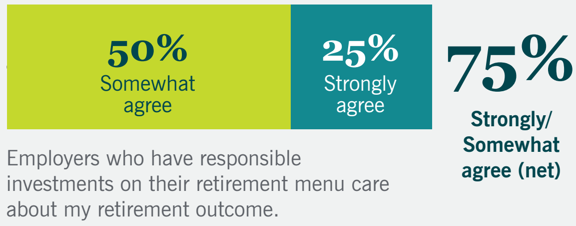
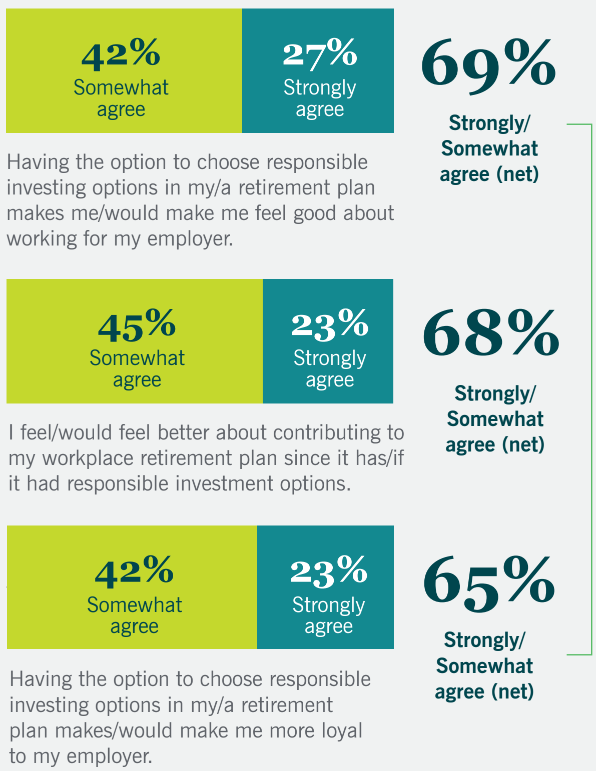


FIGURE 4

Impact on employers offering RI on retirement menu



Nuveen commissioned The Harris Poll to conduct an investor survey to further enhance the company's leadership position among investors, the media, customers, prospects, and the broader investment community. The investor survey was conducted online within the U.S. by The Harris Poll on behalf of Nuveen between 24 August and 03 September 2021 among 1,007 investors who met the following criteria: U.S. resident, age 21+, $100,000 in investable assets (excluding 401(k) or 403(b) accounts) or real estate, primary or joint decision-maker for household financial decisions, and currently working with a financial advisor.

From the fans (or increasing participant interest)

It also must be said that we know plan participants want a broader range of options in their retirement planning, especially with relation to ESG and responsible investing (RI) factors having a place on the menu.

Nuveen's 2021 RI survey[5] shows that 75% of employees believe that an employer that offers RI investment options cares about retirement outcomes. This goes across both millennials and non-millennial respondents. Our RI survey shows that 92% of millennials and 69% of non-millennials hold this view.

Further, investors currently investing in RI are more likely to agree that employers who have RI on their retirement menu care about their retirement outcome, compared to those not currently participating in RI (94% and 57%). Just as importantly, our survey shows that 68% of employees agree with the statement that they feel better about contributing to a workplace retirement plan if it has RI options available. The survey finds that RI options also increase employee loyalty and overall sentiment. RI options in retirement planning therefore have implications beyond just the fiduciary, and could aid employee retention and overall firm morale.

However, the U.S. Supreme Court has made it clear that participant desires are not necessarily a shield against a fiduciary failing to review and monitor investments — i.e., a plan fiduciary cannot add an inferior investment just because participants want the investment.

The wishes of plan participants are only part of the slew of considerations when it comes to investment menu construction and the overall regulatory and legislative environment around retirement planning. But it should still be a factor.

Conclusion

For many, the new proposed rule is generally a welcome update to the current version. Compared to the 2020 ESG Rule, the newly proposed version takes a more accepting approach to ESG investments, and should give plan fiduciaries greater confidence and clarity when selecting investments for plan menus. We hope the new rule will broaden participants' access to ESG investments, as it is clear that plan participants want these options to be available within their retirement options as well. The final version of the DOL's ESG Rule will hopefully strike an appropriate balance between taking an ESG-friendly approach and using sufficiently neutral language, so that the rule can survive throughout political changes in coming years. We also expect that the final rule will provide much-needed assurance that ESG investments can be included in QDIAs. We look forward to reviewing the final rule when it is issued.

ON THE HORIZON

Will cryptocurrencies make the cut in a retirement plan?

As a concept, cryptocurrencies have been around a little over a decade, and in that time many people have made — and lost — fortunes betting on the values of these virtual "tokens."

Given the stories around the price of bitcoin and headlines about their counter-inflationary characteristics, new entry into retirement plans and continued innovation, it is worth exploring what role, if any, cryptocurrencies can play in an investment portfolio, especially when it comes to retirement. But first, let's define the terms.

Understanding Bitcoin, blockchain and crypto

BLOCKCHAIN

A shared database or ledger that facilitates the process of recording transactions and tracking assets in a business network that are immutable once closed. As a database, a blockchain stores information electronically in digital format and is best known for its crucial role in cryptocurrency systems, such as Bitcoin, for maintaining a secure, chronological and decentralized record of transactions.

CRYPTOGRAPHY

An advanced encryption, along with permissions, that ensures privacy on the network, preventing unauthorized access to recorded transaction details, and deterring fraudulent activity. It is key to the security of the blockchain ledger. Each transaction is recorded on the blockchain using encrypted data. Each user can access their own information and buy and sell crypto securely, using their public and private key. (Source: Blockgeeks[6])

CRYPTOCURRENCY

A digital or virtual currency that is secured by cryptography, which makes it nearly impossible to counterfeit or double-spend. Many cryptocurrencies are decentralized networks based on blockchain technology — a distributed ledger enforced by a disparate network of computers. A defining feature of cryptocurrencies is that they are generally not issued by any central authority, rendering them theoretically immune to government interference or manipulation. (Source: Investopedia[7])

BITCOIN

A type of cryptocurrency because it uses cryptography to keep it secure. It was the first and is arguably the most well-known version. There are no physical bitcoins, only balances kept on a public ledger that everyone has transparent access to (although each record is encrypted). All Bitcoin transactions are verified by a massive amount of computing power via a process known as "mining;" however, Bitcoin is not issued or backed by any banks or governments, nor is an individual bitcoin valuable as a commodity. (Source: Investopedia[8])

Show me the money

Cryptocurrency is intangible. Its value is built upon there being a record of who owns the currency, as that allows for digital transfers without the involvement of a central backer, such as a government or a bank. So the question becomes, how do cryptocurrencies gain (or lose) value. Like any currency, they gain their value based on the scale of market interest: if the demand for it is higher than the supply. When a cryptocurrency is useful, people want to own more of it, driving up the demand. However, it's important to note that cryptocurrency has limited utility, meaning its applications are mainly industrial and rarely used in mainstream retail. So the assets speculative nature is built upon the limited overall amount of a specific currency, such as Bitcoin, that can ever be mined, and those who hold their bitcoins on the basis of this disinflationary nature creating a scarcity. Obviously as more types of currencies are created, such as Ethereum or Dogecoin or any of the myriad millions of other "coins," this scarcity element is arguably diminished, but as each coin is created separately there is a lively debate to be had as to the value of any individual coin.

The actual process of determining cryptocurrencies' valuations is another industry debate stemming from fundamental disagreement on the accuracy and validity of valuation models. Adding to the complexity is the lack of a consistent modeling approach applied across currencies. Hence why these assets are often called "speculative" in nature.

Cryptocurrency is intangible.

Its value is built upon there being a record of who owns the currency, as that allows for digital transfers without the involvement of a central actor, such as a government or a bank.

The Guardian

Bitcoin might well be the Amazon.com of cryptocurrencies: a huge institution in a relatively mature state. Therefore, it arguably could have a role in a retirement portfolio, which by its nature is supposed to be more conservative and driven by long-term asset class trends that de-risk over time. However, cryptocurrencies have only existed just over a decade and are still not even readily available for the individual investor to easily buy. So what's a fiduciary to do? The primary responsibility of fiduciaries is to run the plan solely in the financial interests of participants and beneficiaries and for the exclusive purpose of providing benefits and paying plan expenses, according to the Department of Labor. This includes carrying out duties with the care, skill, prudence and diligence of a prudent person familiar with the matters. So when considering how cryptocurrencies, or any new asset in its formative stages, may contribute to retirement savings, it's critical to do so through this lens even if participants advocate to include it.

As a stand-alone investment (via brokerage window or core menu)

- The lack of legal structures and regulatory regimes around these assets make it very challenging to ascribe a long-term value to any given cryptocurrency with any sort of certainty. Further, the asset class has been subject to high volatility during its limited lifespan and limited liquidity. This makes it more difficult to evaluate and measure from a risk/return standpoint and therefore it complicates a fiduciary's investment selection due diligence process and participant communications strategy, opening participants up to a hirer risk of making uninformed decisions and experiencing losses.

As part of an asset allocation strategy (via multi-asset class portfolios)

- The underlying blockchain technology is a fascinating area for development. A well-diversified portfolio will likely have some exposure to the underlying blockchain infrastructure through its financial sector holdings, and may even have exposure to cryptocurrencies through venture capital holdings. Therefore it is probable that many participants already have some form of exposure to crypto indirectly, which is likely the more prudent approach at this stage of development. Participants who access these holdings through professional money managers benefits from their research and expertise to conduct proper and thorough due diligence, including assessing the acceptable levels of risk and volatility.

In March 2022, the Department of Labor released Compliance Assistance Release (CAR) 2022-01, which relates to 401(k) plan investments in cryptocurrencies. The message to 401(k) plan fiduciaries is to exercise “extreme care” in considering cryptocurrencies as part of a 401(k) investment menu for plan participants. They cite speculative nature, valuation accuracy and custodian risks as just some of their primary concerns. Please visit the DOL website for additional information.[9] This came one day after the White House releases an executive order on digital assets, and we expect regulatory guidance to continue to evolve.

But I want a bitcoin now!

A difficulty facing advisors and plan sponsors is engaging a younger generation of investors who have experienced a long period of market growth and see value in YOLO’ing Gamestop short-dated options and buy-and-HODL (hold on for dear life) crypto forums that decry the traditional financial institutional structures. General mistrust and a lack of understanding around market makers and regulators are of deep concern.

It is our job as educators to encourage the younger generations to take retirement planning seriously. The old adage, “the best time to plant a tree is yesterday, the second best is today,” has not fundamentally changed and remains fundamentally true for retirement savings. Stories of crypto gains and the latest meme-stocks have greatly accelerated young people’s dismissal of the value that long-term, diversified investment strategies provide. Therefore the conversation has to begin with education. Is bitcoin attractive because it has gone up a lot in value? In that case we can talk to long-term asset growth and the benefits of compound interest. Or are there more fundamental questions about the growth of digital assets, decentralization and a lack of trust in the traditional structures of finance? In that case we have to educate and contribute to a participant’s knowledge, rather than dismiss their concerns. Engagement with participants and identifying where they are on their retirement journey is a significant part of the conversation around cryptocurrency allocations.

Fiduciaries have a duty to help guide participants toward a secure and comfortable retirement

Answering the questions that a younger generation has about retirement planning and constructing long-term portfolio allocations to grow assets with relatively low volatility are of equally critical importance.

There is a reason why a diversified portfolio of stocks and bonds that gently gravitates towards a more conservative portfolio allocation over time is the bread and butter of retirement planning. There are innovations being made and asset allocation models are taking into account more sophisticated assets all the time, but that is best left for the professional money managers, rather than for individuals to attempt alone.

Owning cryptocurrency may, in fact, produce some intangible benefit to the owner, which can be enjoyed for more than just their hard-to-determine monetary values. However, as fiduciaries, we need to heed the Department of Labor’s warnings while understanding and addressing participants’ concerns. Diversified portfolios, increasingly with income-producing asset classes, may effectively help participants’ address their retirement needs.

For more information, please visit us at nuveen.com

Endnotes

1 Any guarantees are backed by the claims-paying ability of the issuing company.

2 Mass Mutual, "Is delayed retirement impacting your bottom line," 2018

3 Source: PwC's 10th annual Employee Financial Wellness Survey, PwC US, 2021

4 Responsible investing incorporates Environmental Social Governance (ESG) factors that may affect exposure to issuers, sectors, industries, limiting the type and number of investment opportunities available, which could result in excluding investments that perform well.

5 https://www.nuveen.com/en-us/insights/responsible-investing/sixth-annual-responsible-investing-survey

6 **Cryptography:** https://blockgeeks.com/guides/blockchain-cryptography/#:~:text=Cryptography%20is%20key%20to%20the,their%20public%20and%20private%20key

7 **Cryptocurrency:** https://www.investopedia.com/terms/c/cryptocurrency.asp

8 **Bitcoin:** https://www.investopedia.com/terms/b/bitcoin.asp

9 https://www.dol.gov/agencies/ebsa/about-ebsa/our-activities/resource-center/information-letters/06-03-2020-supplemental-statement

nuveen
A TIAA Company

The future of defined contribution

next

GWP-2118892CG-Y0322D 33972