Our retirement system needs work: Morningstar

By Kerry Pechter *Thu, Mar 3, 2022*

The content and tone of Morningstar's new Retirement Plan Landscape Report, from a new Morningstar retirement research group, reflects the crisp, business-like approach that Morningstar's broad audience needs and demands.

The newly launched **Morningstar Center for Retirement and Policy Studies** has released a "**Retirement Plan Landscape Report**," the first in a planned series of original reports on the status of the US defined contribution (DC) retirement plan system and the US retirement system as a whole.

The content and tone of Morningstar's new Retirement Plan Landscape Report, from a new Morningstar retirement research group, reflects a crisp, business-like approach to the topic–one well-suited to Morningstar's broad audience. Other resources in this space include the Employee Benefit Research Institute and the Vanguard, the Investment Company Institute, and Vanguard's annual "How America Saves" reports.

The executive summary of the new **report** says quite bluntly that the domestic DC system needs help. It hemorrhages assets, and not all plans are equal. If you work at a big, profitable company, your DC plan is likely cheap and generous. The implication is that semi-skilled worker at small companies have expensive plans or none at all.

The report explores four aspects of the US retirement system, including: trends across coverage, assets, and numbers of defined-contribution plans; costs to workers and retirees within these plans, as well as their investments; the kinds of investments held by these plans; and the continued role of defined-benefit plans for today's retirees. Key takeaways include:

- Almost $5 trillion flowed out of defined-contribution plans from 2011 to 2020. These constant outflows, due mostly to rollovers and cash-outs, reduce plan assets. The US DC system relies on new employers to offer retirement plans every year to compensate for the more than 380,000 plans that closed over the period from 2011 to 2020. New contributions and strong returns have masked outflows of more than $400 billion a year since 2015. The decline reduces the leverage that plan sponsors might otherwise have to bargain for lower fees from asset managers and lower costs for participants.

- The largest plans in the US today hold nearly 45% of their assets in collective investment trusts (CITs). These pooled vehicles resemble mutual funds but are less regulated and can be much less expensive for participants. Small and mid-sized plans continue to invest the majority of their assets in actively managed funds, with more assets in active strategies among smaller plans.
- People who work for smaller employers and participate in small plans pay around double the cost to invest as participants at larger plans, around 88 basis points (bps) in total compared with 41 bps, respectively. Small plans also feature a much wider range of fees between plans, with more than 30% of plans costing participants more than 100 bps in total.
- Defined benefit pension plans accounted for more than 30% of distributions paid to participants in 2019. About 12.8 million people, between family beneficiaries and retired participants, are collecting traditional pension benefits today. About 8.8 million people who are no longer working are still entitled to future benefits, and 11.7 million people who are still working will eventually receive benefits.
- US defined-contribution system in the aggregate tilted toward investments with more ESG risk—which is the degree to which companies fail to manage ESG risks, potentially imperiling their long-term economic value. Plan sponsors may wish to reexamine their investment choices using an ESG lens.

The Center’s primary research team includes Aron Szapiro, head of retirement studies and public policy at Morningstar, Jack VanDerhei, director of retirement studies for Morningstar Investment Management LLC, and Lia Mitchell, senior analyst of policy research for Morningstar, Inc.

VanDerhei joined Morningstar Investment Management LLC on March 1, 2022, after many years as research director of the Employee Benefit Research Institute. He’ll be responsible for modeling the impact policy changes and proposals might have on US retirement preparedness, as well as the effects of plan sponsors’ decisions on participants.

The Center is planning to shed light on a range of topics in the coming year, including lifetime income in defined-contribution plans, the new anticipated fiduciary package, and the state of overall retirement preparedness among older workers. For more information about the Morningstar Center for Retirement and Policy Studies, please visit