Callan

The Cobbler's Shoes

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In a recent white paper I wrote with my colleague Matt Loster, "The Cobbler's Shoes: How Asset Managers Run Their Own 401(k) Plans," we used federal government data and Callan's database to examine the practices of asset managers in terms of how they operated their own 401(k) plans. The research identified areas in which manager-sponsored plans did exceptionally well compared to a broad universe of defined contribution (DC) plans, and other areas in which the practices of managers differed from the industry consensus on running 401(k) plans.

(Estimated reading time: 4 min 24 sec)

In this post I wanted to share some of the highlights from our research:

High Average Balances: Average balance is indisputably the most important retirement plan savings success metric. The average balance across the 157 asset manager-sponsored plans in our sample ($179,171) was roughly four times that of the average balance for the broad population of 55,000 plans ($42,394). Furthermore, the 90th percentile lowest average balance across the asset manager-sponsored plans ($74,844) would have ranked in the top quartile within the broad population.

High Employer Contributions: Asset managers place a strong emphasis on retirement savings as evidenced by high average employer contributions. The average employer contribution for asset manager-sponsored plans in 2016 ($5,938) was almost five times that of the broad population.

High Employee Contributions: Asset management employees are getting the message that retirement savings is important as evidenced by high employee contributions. The average employee contribution in asset management-sponsored plans in 2016 ($7,187) was roughly three times that of the broad population.

High Correlation Between Employer and Employee Contributions: The data for the asset management sample indicated that higher employer contributions led to higher contributions by employees, a virtuous cycle that ultimately led to higher balances.

High Correlation Between Private Ownership and High Balances: Privately held firms are more supportive of retirement savings than publicly held firms. This is evidenced by the fact that 8 out of the top 10 firms in terms of average balances and in terms of employer contributions in 2016 were privately held.

Asset Managers Offer More Choices: The average plan in the dataset offered 43 investment options, including 12 separate U.S. equity options. The plan with the greatest number of choices offered 250 options. This trend was persistent across the dataset, with

only 15 plans offering fewer than 20 choices. This is in contrast to the general 401(k) industry trend towards streamlined investment lineups.

Low Target Date Fund Adoption: The average allocation to target date funds (TDFs) across asset manager-sponsored plans was only 12%, well below the 32% allocation observed in the broad population. Of the plans in the dataset, 30% did not offer TDFs at all in the 2016 plan year. The maximum allocation to target date funds across the 157 plans was only 49%.

Largest TDF Managers Win: The most widely used TDFs by manager-sponsored plans were those of Vanguard, T. Rowe Price, and Fidelity. These three providers were employed by nearly 60 manager-sponsored plans and garnered $9 billion of the $23 billion in total assets allocated to TDFs (roughly 40%). BlackRock passive funds weren't as widely used but were favored by the largest plans, garnering a total of $3.5 billion in TDF assets.

Managers Like Active Management: The average allocation of non-TDF assets to actively managed strategies was 73% for investment manager-sponsored plans, versus 55% for the broad population of large plans represented in the Callan DC Index.™ Three-quarters of the plans in the dataset allocated 63% or more of total non-TDF assets to actively managed strategies.

Managers Employ Proprietary Products: Of the 157 investment manager-sponsored plans, 92 offered proprietary products managed by the firm. Allocations to proprietary products within this group ranged from roughly 1% of plan assets to 97%. The average was roughly 34%. We found no relationship (zero correlation) between the use of proprietary products and the weighted average investment expense for plans.

Managers Have Generally Managed Investment Expenses Well: The weighted average investment expense ratio across all of the plans in this dataset was 0.53%. This relatively low expense ratio is notable since plans in this dataset were generally under $500 million in assets, and their participants tended to make extensive use of active management.

Most Popular Recordkeepers Are No Surprise: Fidelity and Schwab were far and away the most popular choices for recordkeepers, together representing about 40% of the total population. This is not terribly surprising given the large number of smaller plans in the dataset, and the fact that manager-sponsored plans seem to value a breadth of investment choices including a powerful brokerage window.

Managers That the Managers Chose: Vanguard was the clear winner both in terms of the number of plans that use its funds and total assets. This is interesting for two reasons. First, Vanguard was the recordkeeper for only eight of the plans in this dataset. This means that for the other 107 plans that use at least one Vanguard fund, the plan likely specifically requested that it be added to its investment roster. Second, virtually all of the plans in this dataset are sponsored by firms that have staked their livelihood on the promise of active management. The prevalence of Vanguard funds on their investment rosters would suggest that they see the value of offering their employees low-cost passive strategies consistent with best practices as part of a well-diversified investment lineup.

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