

Trends Impacting Defined Contribution Plans and Stable Value

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Workplace Overview

Within Morningstar Investment Management's Workplace Solutions group, we help our clients choose a retirement service that suits the unique needs of their employee population.

Overview of Workplace Solutions \$158.3 billion¹ total AUM/AUA



**MANAGED
ACCOUNTS**
\$76.9 BILLION

- 22 provider clients
- 107,000+ plans offer managed accounts
- 19 million participants with access to managed accounts
- 1.6 million+ participants enrolled



**TARGET-DATE
MODELS**
\$32.6 BILLION

- 8 provider clients
- 1,300+ plan sponsor clients



**FIDUCIARY
SERVICES**
\$48.8 BILLION

- 14 provider clients
- 19,000+ plan sponsor clients



In total, our Workplace Solutions are available to:

- Over 30 million participants
- More than 286,000 plans
- 60 plan providers, registered investment advisers, and broker-dealers

¹Assets above represent AUM and AUA through June 30, 2020. Morningstar Investment Management's total AUM/AUA as of 6/30/2020 was \$194.9 billion.

Managed Accounts Overview

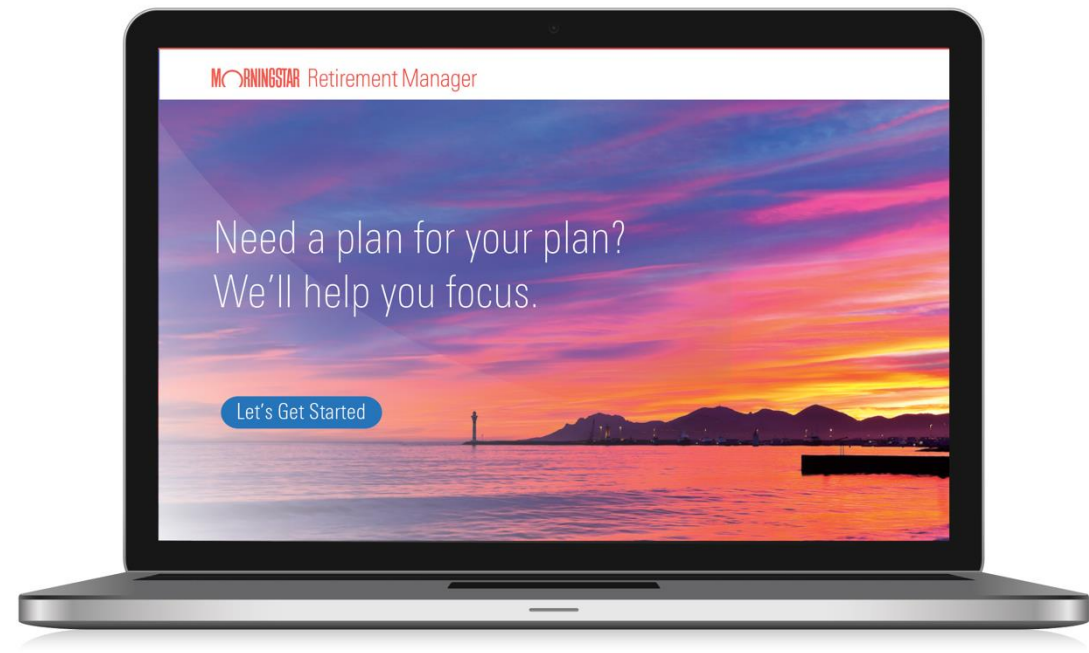
Managed Accounts Overview

What is a managed account?

- An online service that provides retirement advice and ongoing management of a participant's retirement portfolio
- It is designed to help participants save more and reach their retirement goals

What can it provide my participants with?

- Personalized asset allocation strategy
- Target retirement income goal
- Projected retirement income amount
- Savings rate recommendation
- Retirement date recommendation
- Professional investment selection
- Ongoing account monitoring
- Automatic account rebalancing

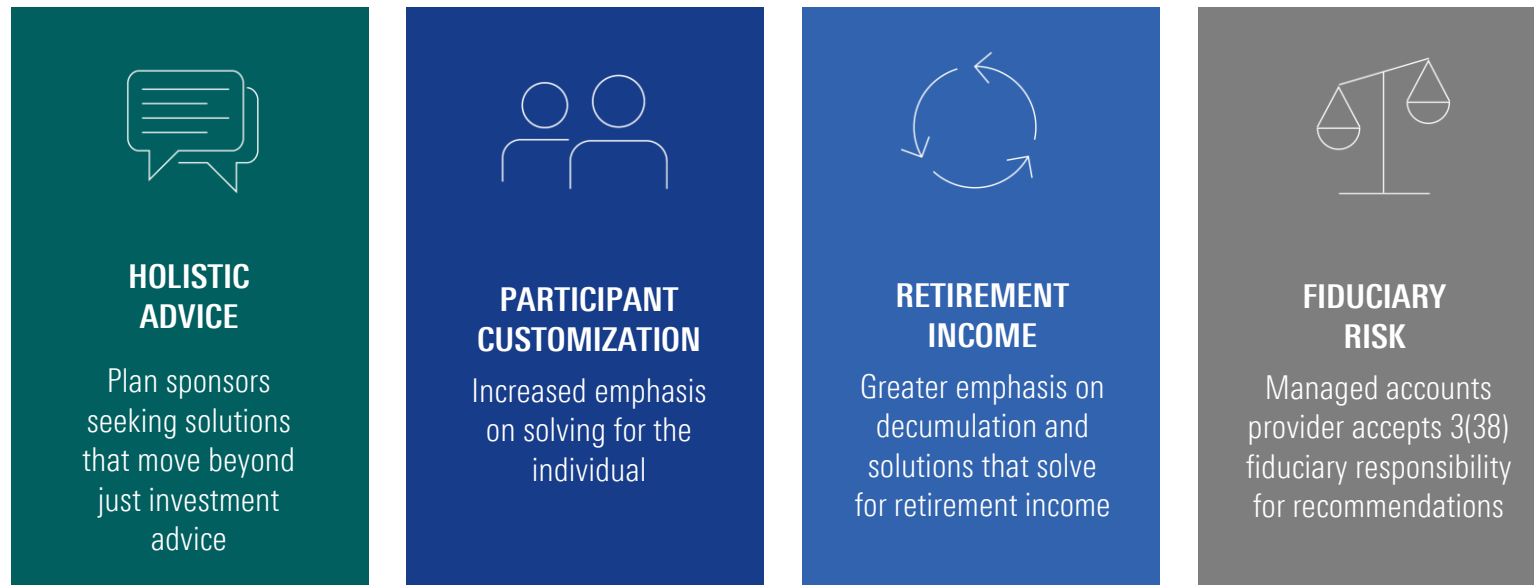


For illustrative purposes only.

Robust Level of Personalization and Management

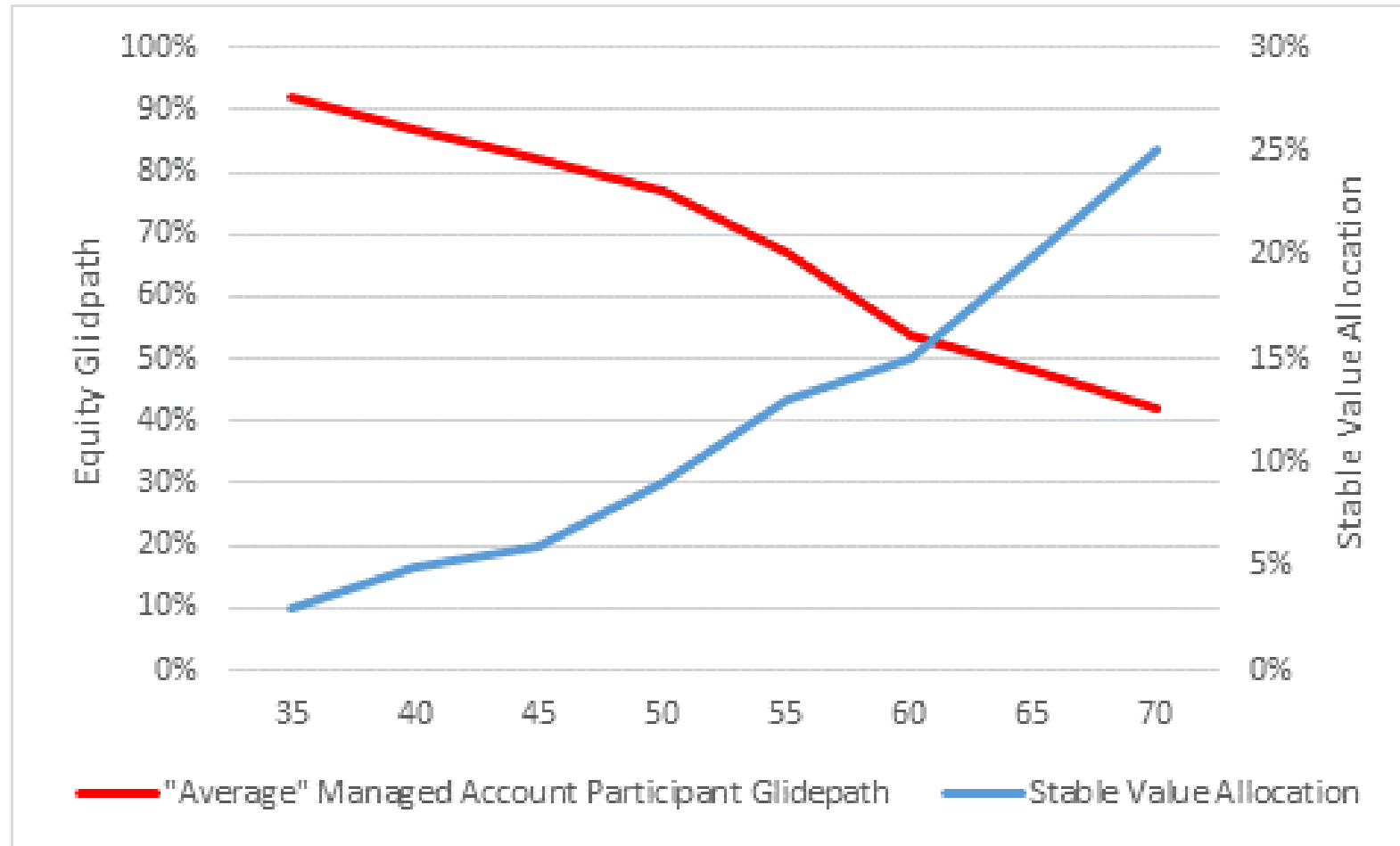
| | Managed Accounts | Target-Date Funds |
|-----------------------------------|------------------|-------------------|
| Customized at a Participant Level | ✓ | |
| Age-based/Retirement Horizon | ✓ | ✓ |
| Risk-based/Preference | ✓ | |
| Fund Preferences | ✓ | |
| Household Assets | ✓ | |
| Outside Assets | ✓ | |
| Retirement Goals | ✓ | |
| Ongoing Management | ✓ | |
| Fiduciary Support | ✓ | |

Managed Accounts Growth Drivers



Source: Cerulli Report, U.S. Defined-Contribution, 2018.

Managed Accounts Use of Stable Value



Source: Morningstar Investment Management LLC. For illustrative purposes only.

Morningstar Investment Management's Use of Stable Value in Managed Accounts


What are the potential benefits to stable value providers?

- Typical participant sees an increase in the allocation to stable value as they move toward and into retirement
- The allocation to stable value slowly increases in a predictable manner
- Given the strategic nature of our asset allocation methodology, short term swings into or out of stable value are unlikely
- We feel stable value provides good diversification in the portfolio due to low correlation to a number of other asset classes
- Our investment consultants spend significant time analyzing stable value funds

Research

Exploring Participant Decisions During Q1 2020

- Allocation changes for 635,116 participants and the enrollment decisions of 15,985 participants during the first quarter of 2020 are reviewed (as of 12/31/19 and 03/31/20)
- Original research focused only on the changes in allocations, an updated version, with Michael Finke and Jon Reuter, also incorporates changes in balances
- Equity risk level is based on the Morningstar Category or similar style proxy
- Participants are categorized into four broad groups based on whether the participant is self-directing his or her account, is using a target-date fund, was defaulted to managed accounts, or opted into managed accounts



Keep Your Distance
401(k) Participant Investment Behaviors (So Far) During the COVID-19 Crisis

Morningstar Research
Working Draft as of April 17, 2020

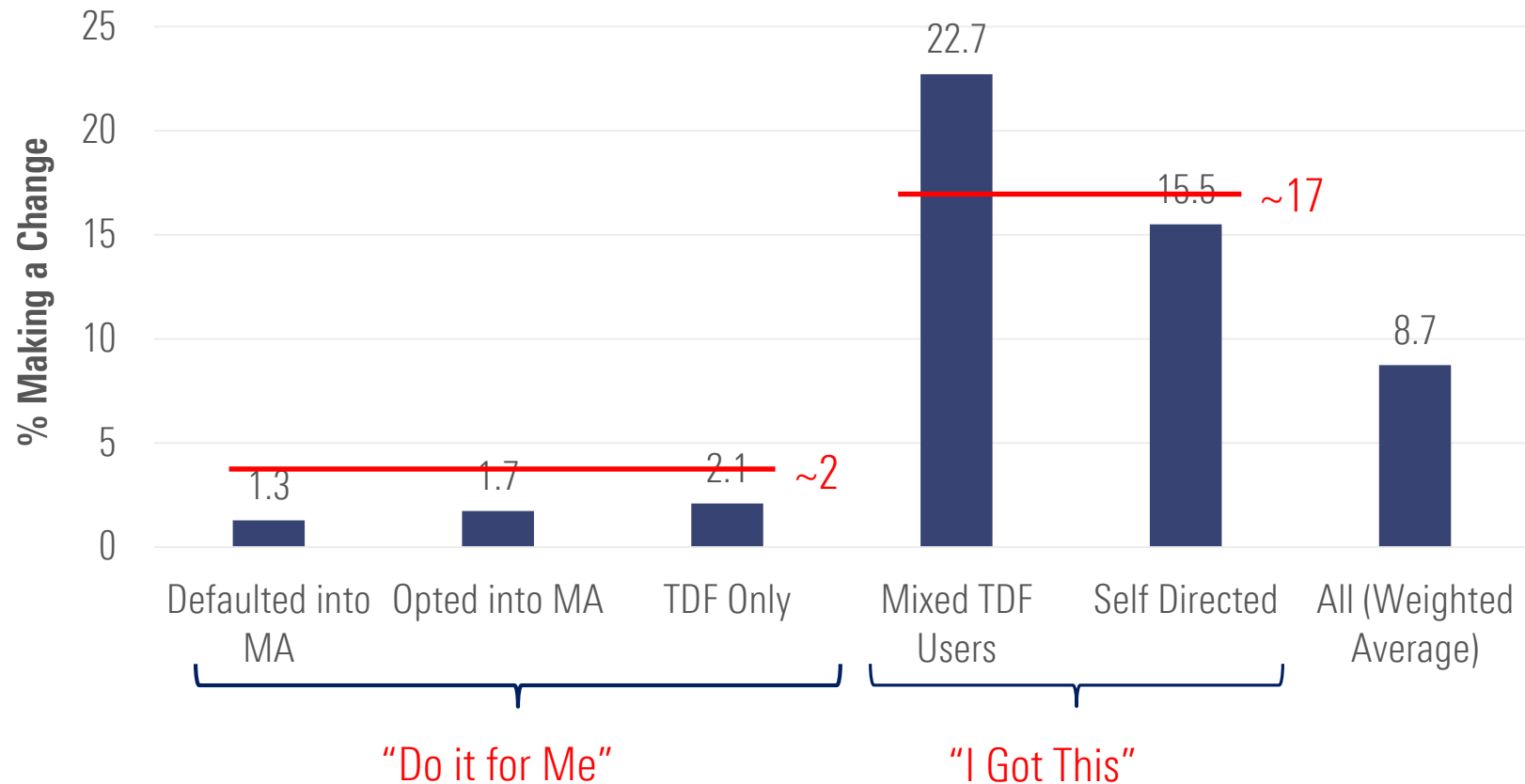
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Executive Summary

- Equity markets declined 20% in the first quarter of 2020 and, at one point, were down more than 30%.
- Median 401(k) balances declined 11.2% during the period, where participants with more-aggressive portfolios and larger balances saw the largest declines.
- This paper explores the allocation decisions of 401(k) participants during the first quarter of 2020, looking at potential allocation changes for 635,116 participants and the enrollment decisions of 15,985 participants.
- While only 5.6% of participants enrolled in a 401(k) plan as of December 31, 2019, changed their portfolio allocations during the quarter, there is significant variation based on how those participants were invested. Of participants self-directing their accounts, 10.8% made a change, compared with 2.4% of participants using a target-date fund, 1.8% of participants who opted into managed accounts, and 1.3% of participants who were defaulted into managed accounts.
- Participants who adjusted their portfolios changed equity levels by 18.9%, on average, with an aggregate decline of 9.4%. Most portfolio changes were relatively small, though, with roughly half of participants changing equity levels by less than 10%.
- The percentage of participants who selected the default investment declined throughout the first quarter, primarily among older participants.
- This analysis demonstrates that professionally managed solutions (for example, target-date funds and managed accounts) have been relatively “sticky” during the recent downturn, especially when compared with the decisions of participants self-directing their accounts.

Source: “Keep Your Distance: 401(k) Participant Investment Behaviors (So Far) During the COVID-19 Crisis” by David Blanchett. Working Morningstar White Paper. For financial professional use only. Not for public distribution. Contact David Blanchett at david.blanchett@morningstar.com with questions about this research.

Percentage of Participants Who Made A Change



Source: Working Paper by David Blanchett, Jon Reuter, and Michael Finke. For financial professional use only. Not for public distribution. Contact David Blanchett at david.blanchett@morningstar.com with questions about this research.

Equity Changes By Equity Allocation and Age Group Among Self-Directors

| Age Group | Equity Allocation (%) | | | | | | |
|-----------|-----------------------|-------|-------|-------|-------|-------|-------|
| | < 10 | 10-25 | 25-45 | 45-55 | 55-75 | 75-90 | >= 90 |
| < 25 | 92.4 | 30.7 | -2.3 | 17.5 | 0.7 | 0.3 | -3.9 |
| 25-29 | 74.3 | 16.1 | 8.0 | 25.7 | 0.2 | -1.0 | -9.8 |
| 30-34 | 71.6 | 13.9 | 4.3 | -0.5 | -1.2 | -1.6 | -13.7 |
| 35-39 | 51.5 | 27.5 | 9.4 | 3.9 | -4.1 | -5.9 | -16.9 |
| 40-44 | 57.5 | 19.9 | 9.7 | 8.5 | -3.5 | -7.5 | -22.6 |
| 45-49 | 56.1 | 17.3 | 7.2 | 3.2 | -5.4 | -9.0 | -22.6 |
| 50-54 | 54.6 | 16.7 | 3.1 | -0.2 | -7.6 | -13.3 | -27.0 |
| 55-59 | 47.8 | 4.5 | -0.3 | -5.1 | -8.3 | -20.7 | -33.5 |
| 60-64 | 35.7 | -0.6 | -4.4 | -5.6 | -15.4 | -26.9 | -42.8 |
| 65-69 | 23.0 | -1.1 | -9.1 | -10.8 | -18.1 | -28.6 | -41.8 |
| >= 70 | 21.3 | 11.6 | -7.9 | -8.9 | -13.1 | -36.4 | -41.3 |

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Research Summary

- Participants changed their portfolio allocations during the first quarter at rate that typically occurs over annual periods (or longer)
- Professionally managed services were significantly “stickier” than participants who were self-directing their accounts (2% vs 17%), with managed accounts being slightly stickier than target-date funds and mixed target-date fund investors making the most changes. Therefore, we think plan sponsors should consider making professionally managed investment solutions available to participants
- Older participants made the most extreme portfolio changes. Older participants are also the least likely to be using a professionally managed option

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New Distribution Channels

Advisor Managed Accounts

Leveraging Morningstar Investment Management’s managed accounts technology and interface, RIAs can now deliver their best investment thinking by creating the portfolios used in a personalized retirement account management service.



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