The Retirement Gamble

According to Frontline, one in three Americans has saved nothing for retirement. Additionally, the number of workers borrowing from their 401(k) has reached a 10-year high. With longer life expectancies and rising healthcare costs, the lack of retirement savings is alarming. On April 23rd, 2013, PBS aired a Frontline documentary entitled "The Retirement Gamble" aimed at demystifying the 401(k) plan as well as the retirement plan industry itself. The documentary featured examples of hard-working Americans and their retirement savings in addition to advice from authorities in the industry commenting on fees, management style, and investment education.

Fees

The documentary explained that fees can greatly decrease long-term returns. On average, actively managed mutual funds carry an expense ratio of 1.3% annually. To put that in perspective, an investor with $50,000 in their 401(k) would pay $650 in fees that year. Ron Lieber of The New York Times noted, "If you add that up over 20 or 30 or 40 or 50 years in a 401(k) plan, all of a sudden, [your fees] are well into the six figures as your balance grows. And that's the difference between running out of money before you die—or having a little money left to pass on to your heirs."

While there will always be some expenses in retirement planning, just like in any service industry, the fees should be as minimal as possible and reflect the value added in your retirement plan. Given the right provider, however, fees should always reflect value added in your retirement plan. Many 401(k) plans have several service providers that work on the plan and receive compensation. These service providers include brokers, broker dealers, investment companies, insurance companies, plan consultants, recordkeepers, and third party administrators. If a Plan Sponsor provider can bundle the services with a single provider, the result is cost savings for the investor.

Investment Selection

The documentary suggests that investing in index funds is a way to incur lower fees. Vanguard founder, John Bogle, talks about long-term, low-cost investing through index funds. Bogle states, "Get Wall Street out of the equation. Get trading out of the equation. Get management fees out of the equation."[1] Passively managed funds frequently do have lower transaction costs and management fees than actively managed funds due to less buying and selling of securities. The returns are sometimes more predictable as passive funds aim to track an index. Actively managed funds,

[1] The Retirement Gamble, PBS Frontline. Aired 23 April 2013.

however, provide the opportunity for investors to outperform a benchmark. Investors can take on additional risk with the potential to earn higher-than-market returns.

The question of whether the higher potential returns or lower associated fees are more advantageous for long-term investors has been debated for years. Proponents of passive funds state high fees and costs associated with actively managed funds can dilute long term returns. Supporters of active funds argue that passively managed funds follow the market and cannot be customized for specific market environments. The key is to review both fee levels and performance and to directly compare options to determine the best options for your retirement plan.

Education

Another major issue that the documentary found in the industry is that investors are not being educated to make informed decisions with their money. When investors aren't educated in how to best invest their money to meet their retirement plan needs, retirement does become a gamble. Professor and Economist Teresa Ghilarducci explains, "The 401(k) is one of the only products that Americans buy that they don't know the price of. It's also one of the products that Americans buy that they don't even know its quality."[2] Today, many baby boomers are finding that they do not have enough money to retire because they were not properly educated on when to start saving, where to invest their money, and how much they would need to save.

All participants should receive information about the plan as well as how to determine their personal risk profile and investment strategy. Furthermore, participants should have access to a personal plan specialist, who will know the Plan and be available when questions arise. Additionally, websites are useful to plan sponsors and participants, including an online guide to reading and understanding quarterly statements. Participants and sponsors should have full access to their account to view current balances and allocations, complete transactions, create a personalized investment strategy, and track their progress to retirement. A quarterly newsletter is beneficial to keep participants and sponsors informed on what is going on in the industry and in the economy. With all of these tools, participants and sponsors will be well educated to make informed decisions about their retirement plans.

Conclusion

With the majority of 401(k) providers, retirement planning can be a confusing and costly experience. However, given proper education and a trusted partner in the industry, it is possible to plan and save for retirement without unnecessarily high fees. Saving for retirement is important for the American worker, and having a provider that will inform, educate, and consult participants in the retirement journey is essential to success. As a result, investing for retirement won't be a gamble.

[2] The Retirement Gamble, PBS Frontline. Aired 23 April 2013.