



BLUE PAPER

BUILDING FOR TOMORROW.

THE TALENT IMPLICATIONS OF THE
RETIREMENT SERVICES EVOLUTION

SpencerStuart

The retirement services market, always dynamic, is at a crossroads. Huge demographic changes are accompanying the aging of the baby boomers. Significant regulatory change affecting workplace retirement savings plans has changed the playing field. The retirement industry is rapidly moving away from traditional pension plans, and defined contribution plans also are evolving. The industry is shifting from a service model focused primarily on building retirement savings to one in which fostering retirement income and financial security will be an equally important, if not dominant, objective. Asset managers, insurance companies, banks, broker/dealers, registered investment advisers and private wealth managers all are striving to build new capabilities to address these changes — and to attract the right talent to respond to the opportunities and challenges created by them.

To learn more about how companies within the retirement services industry are responding to the changes occurring in the retirement plan market and to explore the talent implications for the industry, Spencer Stuart spoke with a number of leaders in retirement services. These leaders, who represent all facets of the retirement services business, discussed the changes they are seeing in the marketplace, the strategies their companies are pursuing and the skill-sets their organizations require as they face the challenges ahead.

THE CHANGING RETIREMENT SERVICES LANDSCAPE

DC PLANS DOMINATE — BUT ARE THEY ENOUGH?

Over the last quarter of a century, defined contribution (DC) plans have slowly but surely taken over defined benefit (DB) plans as the workplace retirement savings option of choice. Today, DB plans cover only about 21 million workers, or roughly 20 percent of active employees¹ — less than one-half the percentage of workers covered by these plans a quarter century ago. DC plans, which are less costly to administer and offer portability and investment control to plan participants, have increased in popularity in lock-step with the decline in DB plans. Today, the federal government reports that DC plans account for more than \$3 trillion in assets, up from \$1.1 billion in 1993.

The slow decline of the DB plan is expected to accelerate in light of several recent regulatory developments, including the Pension Protection Act (PPA), which are pushing the few plan sponsors still offering a DB plan option to consider whether maintaining it is still viable, observers say. These regulatory changes include more stringent funding requirements and new accounting standards that are expected to make pension costs more volatile and result in a greater impact on companies' balance sheets. It also may lead plan sponsors to consider outsourcing aspects of the DB plan or even to sell the DB liability to third parties.

¹ Hunt, D.; Ramji, S.; Catlin, T.; Erzan, D.; Revell, J. "The Coming Shakeout in the Defined Benefit Market." 2007. McKinsey & Company.

“Institutional investors develop a policy across asset classes and then move to an implementation stage to discover what assets meet their policy objectives. It’s a conscious strategy about beta and a thorough risk analysis for the pursuit of alpha. That’s a real investment strategy. The little guy gets none of that.”

The popularity of DC plans has accelerated and assets have ballooned; however, concern has grown that DC plans may not be as efficient and effective at ensuring adequate retirement savings for the average employee as the DB plan of the past. “The average 60-year-old has \$140,000 in his or her Defined Contribution plan; the average 50-year-old has a \$90,000 balance,” observed the head of the U.S. institutional business for a global asset management firm. “Twenty percent of people earning between \$30,000 and \$40,000 do not contribute to a DC retirement plan at all, and most people lack the skill and the time to steward their own investment portfolio.”

Unlike DB plans, DC plans require individual employees to decide whether to participate, how much they will contribute monthly to the plan and how to invest their savings. DC plans may or may not include a company contribution to add to the employee’s retirement savings. While plan sponsors and administrators have been working tirelessly since the inception of the 401(k) plan to better educate plan participants about their investments so that they can make proper investment decisions, there is growing acceptance that most individual plan participants will never be able to achieve the same investment results over the long term as a professional portfolio manager running a DB plan.

“The main disconnect between what investors need and what fund managers offer is a strategic asset allocation policy. Institutional investors develop a policy across asset classes and then move to an implementation stage to discover what assets meet their policy objectives. It’s a conscious strategy about beta and a thorough risk analysis for the pursuit of alpha. That’s a real investment strategy,” said the head of the DC unit of an investment management firm. “The little guy gets none of that. He gets a list of funds with very little education or discussion around how to build a true strategy from a total portfolio view.”

Although plan sponsors have recognized this limitation for some time, they have been unable to offer investment “advice” within the regulatory context of DC plans, for fear of being held liable for plan participants’ results. Last year, the Pension Protection Act took away much of this concern, creating a safe harbor for plan sponsors interested in offering their plan participants better investment advice. The PPA makes many important changes to the regulatory landscape for plan sponsors. In particular, it allows plan sponsors to automatically enroll employees in the plan and to put their investments in certain investment options (e.g., target-date maturity funds). It also offers a safe harbor for certain kinds of investment advice delivered through independent third-party institutions.

“The Pension Protection Act had many provisions that will accelerate the decline of DB plans, but it also addressed the advice problem in 401(k) plans,” commented the director of channel marketing of one provider of customized retirement and financial services. “The PPA authorized plan sponsors to use automatic enrollment to get participants in the plan and dealt with the quandary of what to invest them in. The PPA said that plan sponsors will be within the law if they use automatic enrollment with lifestyle funds or managed accounts.”

This regulatory change has led to a flurry of activity in the retirement services market as asset managers, insurance companies and other providers scramble to take advantage of the opportunities it creates. As a greater percentage of plan sponsors move toward automatic enrollment in their DC plans, they are looking to retirement services companies to provide new options, such as lifestyle funds and target-date funds, that determine asset mixes based on an individual’s age, risk profile and length of time until the principal will be drawn down. The industry has responded rapidly with a wide array of product options to meet this demand.

THE CHALLENGE OF DELIVERING FINANCIAL SECURITY TO RETIREES

Despite recent positive changes in the DC market, many market observers remain concerned about the overall financial security of retirees in a post-DB world. DB plans guaranteed a portion of the employee’s salary in his or her final working years

from the date of retirement until death. Many companies also offered health benefits to cover healthcare costs during retirement. DC plans do not offer lifetime income guarantees, and retiree healthcare coverage is becoming less and less common as healthcare costs rise. The need to deal with the complete range of issues affecting financial security in retirement is changing the landscape for retirement service providers as they prepare for the baby boomers to enter retirement.

Investors on the verge of retirement face a whole host of new financial concerns — how to ensure that their income will last throughout their retirement; how to ensure their purchasing power will not be eroded by inflation; how to pay for growing and unpredictable healthcare costs; how to finance or insure against the costs of long-term care; how to protect against catastrophic medical costs; and, for the wealthier, how to pass a portion of their life savings to their heirs in the most tax efficient way possible. These post-retirement needs present new opportunities and challenges for the money management industry.

“We are beginning to see investors thinking about what they want to do with their retirement savings and engaging in ‘de-accumulation’ conversations with phone representatives. The first boomers are turning 62 and are eligible for Social Security and withdrawal from DC plans. They are asking about risks to their plans, long-term care needs and how to ensure that they don’t outlive their savings,” said the former head of a retirement study group at a leading 401(k) provider.

“There is a whole new intellectual foundation that needs to be in place for our industry. We all have it covered on the investment side, but not many providers are prepared for these new discussions. Retirees also are looking to market participants to provide solutions to address their healthcare risks,” he said. According to another retirement services executive, the industry is searching for a new class of products to help investors manage these risks — for example, a hybrid health and market insurance plan in which the payout is based on market performance could be one such innovation on the horizon.

One outgrowth of the challenge of delivering financial security in retirement in a post-DB world is a growing interest in products that combine mutual fund products with the features of annuities to guarantee income for life. Mutual fund companies, which have dominated the DC plan market, are looking for ways to develop insurance-like features for their investment products. Insurers, for their part, seek to realize their vision of being full-service financial solutions providers to their clientele by stepping into the void. “While insurance companies are trying to find ways to look more like money managers, money managers are trying to do the opposite — find ways to bring cost-effective insurance-type services with guaranteed income to their clients,” said the chief marketing officer of a leading life insurance company.

BRIDGING THE GAP BETWEEN INSTITUTIONAL AND RETAIL RETIREMENT SERVICES

Developing new solutions to address the income needs, healthcare and longevity risks, as well as

the estate planning needs of retirees, will not be easy for any industry player. A key missing link for financial services providers seeking to bridge the gap between the 401(k) plan and retirement income solutions is the relationship with the individual investor. “The retirement income space is something that everyone talks about, but no one is doing a good job of addressing. The annuity industry is talking about this as their ‘utopia.’ The fact that more and more investors will use some kind of insurance wrap is a potential boom for them, but it’s a retail play, not an institutional worksite play. No one wants to leave their money with their employer,” said one retirement services industry consultant. “It’s very difficult to bring these sides of the business together effectively.”

Firms with a strong foothold in the 401(k) market are building capabilities to serve individual investors as the anticipated tidal wave of retirees prepare to roll over their 401(k) assets into individual retirement accounts (IRAs) — with mixed degrees of success. “Many firms are institutionally focused, but the shift to IRAs requires firms to facilitate relationships with individuals. Firms will need a phone, online or brick-and-mortar-based chassis with full-service capability in order to handle that client transaction,” said the president of an insurance company’s retirement services business. The industry has come full circle since he started in the business in the early 1980s. Back then, insurance companies and banks began losing assets to the fund companies as baby boomers began to invest in equity-based funds meant to help them accumulate funds for retirement. “Today, as this generation approaches retirement,

“The first boomers are turning 62 and are eligible for Social Security and withdrawal from DC plans. They are asking about risks to their plans, long-term care needs and how to ensure that they don’t outlive their savings. ... There is a whole new intellectual foundation that needs to be in place for our industry.”

they are looking for the guarantees and conservative features of the bank and insurance products,” he said.

Industry leaders agree that, while some companies are further ahead, no particular company or market participant has fully bridged the gap between the institutional and retail retirement services markets. Firms will continue to build internal bridges, but also may make acquisitions or seek partners in other sectors. For instance, some retirement services executives expect to see asset management firms and insurance companies partner to provide new kinds of products. “Insurance companies have a lot of assets under management and actuarial knowledge, but are not as cost effective in many cases. We think asset managers will partner with insurance companies to drive the change,” said one.

NEW CHALLENGES, NEW LEADERS: THE TALENT IMPLICATIONS OF THE CHANGING RETIREMENT LANDSCAPE

With so much change occurring in the retirement markets, companies are seeking new leaders to help them succeed in the retirement markets of the future. These leaders must possess the ability to think strategically, deep knowledge of all aspects of retirement services, experience in capital markets and risk management, an understanding of retail brands, and skills to leverage technology

effectively. What are some of the talent implications for retirement services firms in today’s market?

New challenges and opportunities drive demand for strategic and charismatic leaders. As they respond to the challenges in today’s retirement services market — and the new business opportunities these challenges represent — companies are seeking experienced, charismatic general managers with deep knowledge of the retirement services market and the ability to take a strategic view to lead them. These managers are expected to drive innovation and think beyond the traditional industry constructs.

While the specific leadership needs for organizations will vary depending upon their current service model in the retirement market, strong leadership will be in demand across the board. In fact, the industry has experienced a noticeable increase in firms, which previously had only been “fringe” players in the retirement industry, poaching senior-level talent from industry leaders to head up new retirement business units. The expectation is that these managers will get them into the market quickly and strongly, accelerating their capture of market share — while also sending a market signal of the seriousness with which they are taking their entry into the retirement market.

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Insurance companies increasingly are looking for retirement services leaders from outside their industry to help them move beyond a focus on traditional annuity-oriented products and services to a more holistic set of retirement products and services that leverages their ability to offer income guarantees and other forms of financial risk management. Companies in the 401(k) market, whether as full-service providers or as investment-only providers, will continue to look for leaders who can help them bridge the gap between the 401(k) plan and the retail retirement/rollover IRA market by cultivating strong individual relationships with plan participants. As they look to expand their offerings into new areas, insurance companies, asset managers and other industry participants will need leaders with experience cultivating strategic relationships across markets.

With only a limited pool of talented leaders who also have extensive experience in retirement services, recruiting and retaining the industry's best and brightest in this environment will become increasingly challenging.

Leadership to link institutional, retail and wealth management services. Retirement services providers can no longer maintain a siloed view of the investor's lifecycle, with institutional divisions serving plan participants, retail divisions serving

IRA holders and other retail investors, and wealth management units picking off the cream of the crop when balances have grown. Retirement market leaders of the future will devise strategies that take a holistic view of investors' retirement needs, seeking to build relationships within the 401(k) plan and maintain those assets through rollovers and well into the retirement income phase of investors' lives.

This means that companies will need managers with both the vision and the practical skill to bring together all of the services and capabilities within an organization suitable for serving the retirement needs of the individual investor. This requires a solid understanding of institutional, retail and wealth management service models and an ability to foster linkages among them. Firms offering 401(k) services, either on a full-service or investment-only basis, but lacking retail services, will be especially challenged in this regard. These firms will need leaders who are adept at identifying partnerships, joint ventures or potential acquisitions that will enable them to develop deeper and broader relationships with investors throughout their lives.

We expect to see growing “cross-fertilization” of talent across these industry segments (i.e., institutional, retail and wealth management). This will

occur as institutional firms hire leaders with experience in retail plan services, retail firms hire leaders with experience in institutional services, and private wealth managers seek leaders with experience in both retirement realms. The goal of this will be to bring a fresh perspective to these lines of business on how to best serve investors at each stage of their lifecycle.

Functional leadership needed across the value chain. Linking historically siloed business units to meet the needs of the changing retirement market will require more than strong general managers, however. Companies will need strong functional leaders to drive the change necessary to effectively bridge the gap between institutional plan services, retail retirement services and wealth management. Functional expertise also will be required to effectively introduce product and service solutions to meet new investment paradigms within DC plans and at retirement. This will require leadership in investment management, product development and management, sales, marketing and client service, and in technology. Specifically, we expect to see the following functional needs:

- > *Nimble and innovative investment management and product development.* Retirement services providers must address the formidable challenges of bringing together the best aspects of separate and distinct investment vehicles to produce better long-term results for investors at an efficient price. Portfolio managers and product strategists with the vision and technical expertise to bring the best investment features of DB plans to the DC plan and who can link the best features of annuities, mutual funds and managed
- > *Sophisticated, consultative institutional sales talent.* The changes in the DC marketplace over the last several years, which have been accelerated by the PPA, are driving demand for sales people with a greater degree of investment acumen and problem-solving orientation than ever before. DC sales talent must be collaborative and consultative in their approach to potential clients, equally facile discussing plan administration and investment issues with human resources, treasury and finance personnel. They also must be able to speak comfortably about the plan sponsor's DB plan needs, as plan sponsors consolidate decision-making authority for retirement savings plans. Indeed, it is likely in the next five years that the practice of having two separate sales forces for DB and DC products will no longer be commonplace. Finding and retaining top sales talent will not be easy, though, as DB managers and hedge funds also increase their demand for strong sales professionals with access to institutional investors.
- > *Cross-functional marketing and retooled client service.* One of the key challenges faced by many multiproduct financial services firms is the ability to link together in a comprehensive way the retirement services they offer and to build their brand as a retirement provider. Strong strategic marketers with the skill to help companies build their retirement

brands, while bringing together their product and service offerings into a complete package, will increasingly be in demand. Frontline client service — whether via phone representatives, financial advisers or private client advisers — will need to be retooled to meet the changing needs of the retirement investor. These individuals must be able to go well beyond a discussion of how to roll over a 401(k) balance to address the complex issues of income guarantee, risk management and health management faced by retirees. Enabling this will require both extensive training in the more complex products designed to meet retirement income investors' needs and a rethinking of the traditional profile of individuals managing and holding these frontline client service positions.

- > *Technology solutions leaders.* The role of technology in the retirement market of the future cannot be underestimated. Strong IT professionals with a deep understanding of the retirement services market and its associated technology challenges will continue to be in strong demand. This will be the case both in the institutional world, as 401(k) plan administrators face an increasingly competitive market and a need to control their costs and drive efficiency in service delivery, and in the retail market where technology offers great promise in empowering the frontline to deliver sophisticated financial planning services in a cost-efficient manner.

CONCLUSION

Companies across the financial services industry — asset managers, insurance companies, banks, brokers/dealers and private wealth advisers — all are looking to find new solutions for the evolving retirement services marketplace. Finding skilled talent at the general management and functional level will be critically important to every firm's ability to succeed in the new landscape. Retirement services companies are likely to face strong competition for talent from each other as demographic trends accelerate, as well as from other financial services sectors. Firms must prepare themselves for a fight to acquire and retain talent, taking care to make sure that they are well positioned to not only attract the best talent in the retirement services market, but also to retain the talent they have.

ABOUT THE AUTHOR



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Liz Fisher brings more than 20 years of experience to Spencer Stuart and specializes in recruiting senior executives in the financial services industry, with particular focus on asset management, sales and marketing, retirement services and consumer financial services. Based in San Francisco, Liz brings her experiences and knowledge from careers on both the East and West coasts to assist her clients in their recruitment efforts.

Liz joined Spencer Stuart after a diverse management career in financial services. She was managing director of JPMorgan Chase Asset & Wealth Management Group and president and CEO of BrownCo, its brokerage subsidiary. Liz was also an executive vice president with Fidelity Investments in Boston. Her responsibilities included marketing and product management for the banking, broker-dealer, RIA and capital markets client bases. Before joining Fidelity Investments, Liz was with Union Bank of California in Los Angeles, where she was CEO of the bank's broker-dealer and related activities.

Liz began her career at Fidelity Investments after earning her Bachelor of Science degree in marketing from Boston College. She currently serves on the board of directors of the Financial Women's Association of San Francisco.

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