DC SOLUTIONS

THE EVOLVING DC LANDSCAPE

April 2023

INTRODUCTION

DC plan sponsors play a significant role in shaping the retirement outcomes of American workers. With the continued decline in defined pension benefits, workers are increasingly dependent on the defined contribution system for a significant portion of their retirement savings. As this shift continues, so does the need for the DC system to evolve.

Savings accumulation has been the primary focus for DC plans, but as an increasing number of workers retire with DC accounts, they will be tasked with translating their savings into income. This will drive demand for better solutions that address the many unique risks that retirees face in retirement.

Plan sponsors have a huge opportunity to lead the charge in providing personalized retirement income solutions that address these risks and leverage institutional investment best practices.

As part of PGIM DC Solutions' research efforts to better understand the evolving DC landscape, we completed our second bi-annual survey of 155 plan sponsors that have at least one 401(k) plan and a minimum of $100 million in 401(k) assets. We covered everything from retirement readiness and retirement income to alternative investments and ESG. We encourage you to dive in!

CHAPTER 1

RETIREMENT READINESS: WORK TO DO

01

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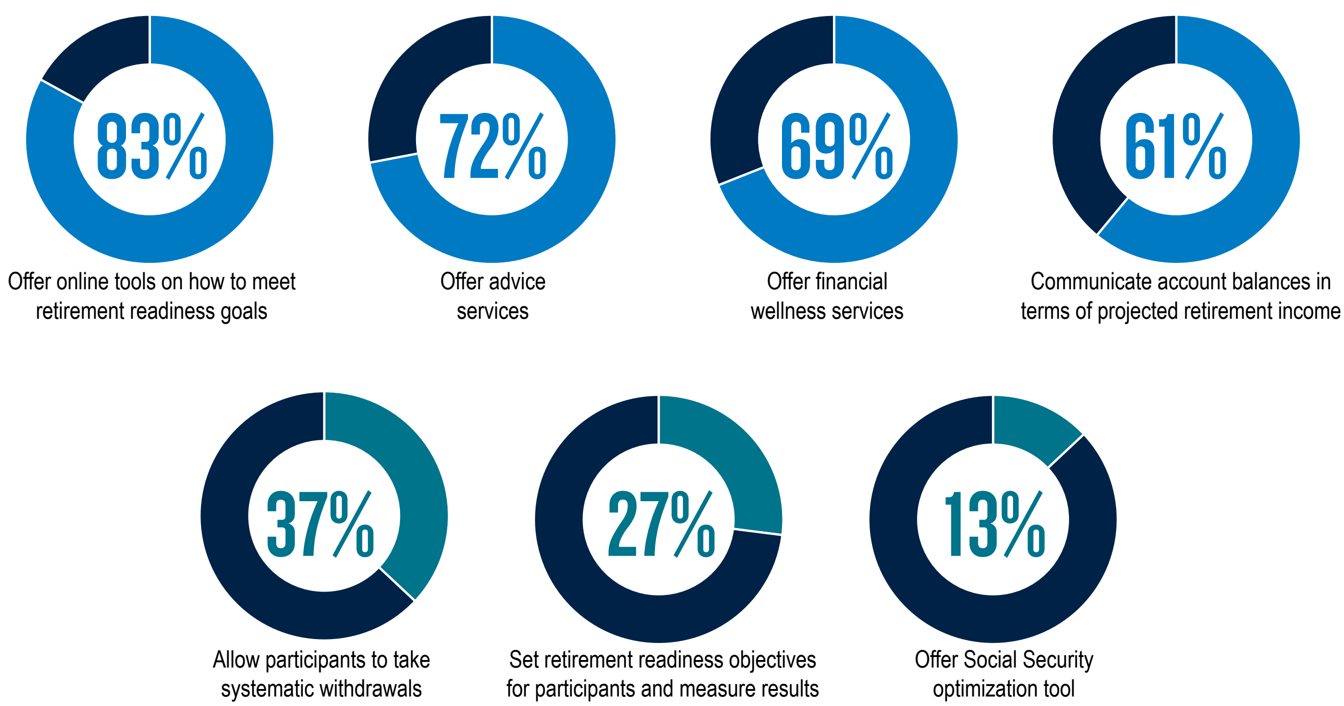
RETIREMENT READINESS: WORK TO DO

WHAT'S NEW

More than 60% of plan sponsors have not yet taken the following steps to increase retirement readiness for their participants:

- Expand distribution options to allow systematic withdrawals.
- Provide a Social Security optimization tool for participants.
- Determine retirement readiness objectives to help identify areas of focus.

Steps Taken to Facilitate and Increase Employee Understanding of Retirement Readiness



WHY IT MATTERS

- For plan sponsors looking to evolve their DC plans to better support their participants' retirement readiness, these less utilized steps can have a positive impact on certain factors, namely, improving participant retirement education and offering more flexible distribution options.
- These steps are "low hanging fruit," meaning they should be a lighter lift for most plan sponsors relative to adding new products and solutions.

ADDITIONAL THOUGHTS

- Consistent with our research from 2020[1], the most common retirement readiness step taken by plan sponsors is offering online tools to participants, followed by advice services and financial wellness.
- In 2022, the new Lifetime Income Disclosure went into effect for DC plans subject to ERISA. While this is still quite new, the disclosure communicates a participant's current account balance in terms of a monthly income amount. While not perfect, this is a step in the right direction to help participants think about their retirement savings in terms of an income stream, instead of a lump sum.
- For plan sponsors interested in exploring their plan's "retirement readiness," listed below are measurable and impactful factors designed to improve participant outcomes.

FACTORS	RETIREMENT READINESS GOAL
ACCESS	Provide participants access to a retirement plan as early as possible
SAVINGS	Provide incentives for optimal savings rates over time
INVESTING	Offer diversified and risk-appropriate portfolios that align with individuals' needs
EDUCATION	Provide incentives and services that improve financial literacy and retirement decision-making
RETENTION	Monitor leakage and educate participants on the benefits of remaining in plan
SPENDING	Provide solutions that are specifically designed to assist participants in achieving an income stream throughout retirement

1 PGIM 2020 Plan Sponsor Research: Total Respondents: 138. 35 plans with $100-$249M AUM, 41 plans with $250-$499M AUM, 29 plans with $500-$999M AUM, 26 plans with $1-$1.4B AUM, and 7 plans with over $5B AUM.

CHAPTER 2

CHIPPING AWAY AT THE RETIREMENT INCOME CHALLENGE

02

CHAPTER 2

CHIPPING AWAY AT THE RETIREMENT INCOME CHALLENGE

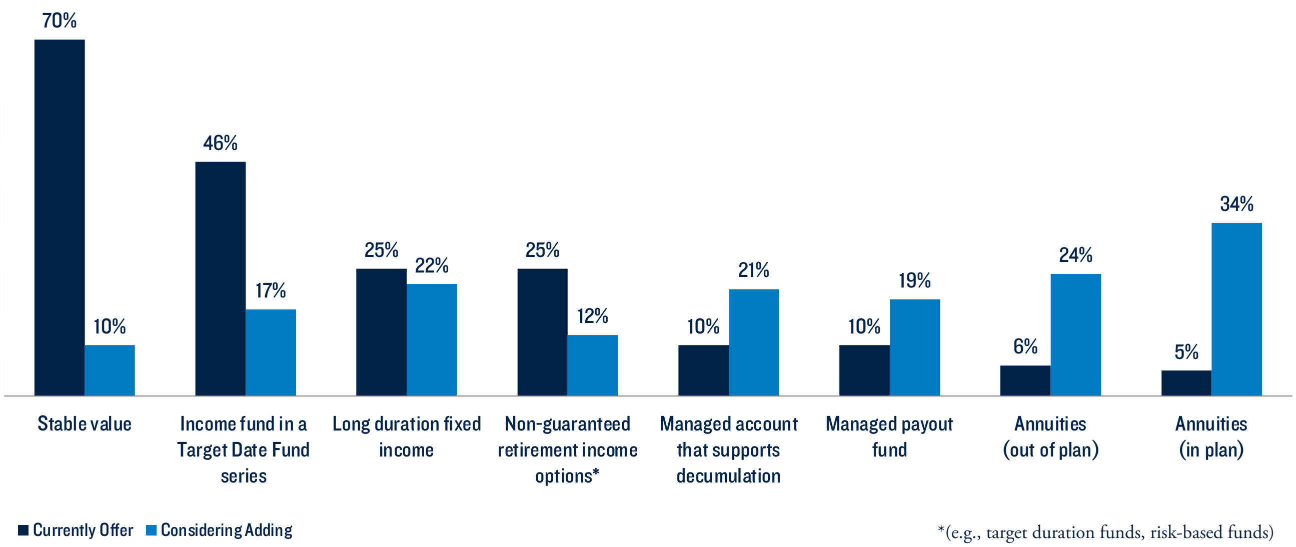
WHAT'S NEW

- 7 out of 10 DC plan sponsors have taken steps regarding retirement income, with the majority still in the education stages. 15% of plan sponsors are in the process of evaluating products or implementing a solution.
- Stable Value and the Income Fund of a Target Date Fund (TDF) series, while not generally designed to address the various risks that retirees face in retirement, continue to be the top solutions that plan sponsors cited as being offered to support retirement income.
- The top approaches plan sponsors are considering adding include annuities (in and out of plan), long duration fixed income, and managed accounts that support decumulation.
- 2 out of 3 plan sponsors believe that technology-enabled customized solutions for retirement income will be needed for pre-retirees and retirees.

STEP	ACTION	% OF PLAN SPONSORS
1	Initial stages of learning about retirement income approaches	34%
2	In the process of better understanding participants' retirement income needs	14%
3	Formally evaluating whether to add retirement income solutions to 401(k) investment menu	3%
4	In the process of evaluating specific retirement income solutions/products to add to plan	8%
5	Implementing (or already implemented) a retirement income solution/product	7%
Have evaluated retirement income solutions and decided not to pursue		8%
Not currently a topic of interest or need		27%

Need for Technology-Enabled Customized Retirement Income Solutions

Retirement Income Solutions Offered or Considering Adding



*(e.g., target duration funds, risk-based funds)

WHY IT MATTERS

- As DC plans continue to evolve from savings vehicles to true retirement plans, retirement income will become a more pertinent focus area for plan sponsors, requiring more research and action. Plan sponsors do not have to face this journey alone - leverage experts and lean on strategic partners for guidance.
- While target date funds have become the primary accumulation vehicle within DC plans, the challenge of solving for individuals' retirement income needs will require more personalized approaches and continued evolution and innovation within the space. Leveraging technology to bring more tailored advice and investment solutions will be critical.
- Despite plan sponsors indicating that annuities (in and out of plan) are the top areas of interest, only 14% agreed there is a significant amount of participant interest in adding in-plan annuities. This suggests that a critical step for every plan sponsor will be to gain a more holistic understanding of their participants' retirement income needs as they chip away at the retirement income challenge.

ADDITIONAL THOUGHTS

- Guaranteed income, such as annuities and protected income strategies, can and will play a role in solving a portion of the retirement income challenge. This may include optimizing social security claiming, pension payments, or income from an annuity product. But keep in mind that there are many solutions and tools outside of guaranteed income that plan sponsors should offer participants, including investment solutions that address the risks retirees face in retirement, comprehensive investment advice, and dynamic withdrawal guidance, to name a few.
- PGIM DC Solutions' David Blanchett has authored a white paper Redefining the Optimal Retirement Income Strategy which introduces our framework designed to improve retirement income outcomes.

CHAPTER 3

ACCESS TO ALTERNATIVE INVESTMENTS?

Not Yet for the Typical DC Participant

03

CHAPTER 3

ACCESS TO ALTERNATIVE INVESTMENTS? NOT YET FOR THE TYPICAL DC PARTICIPANT

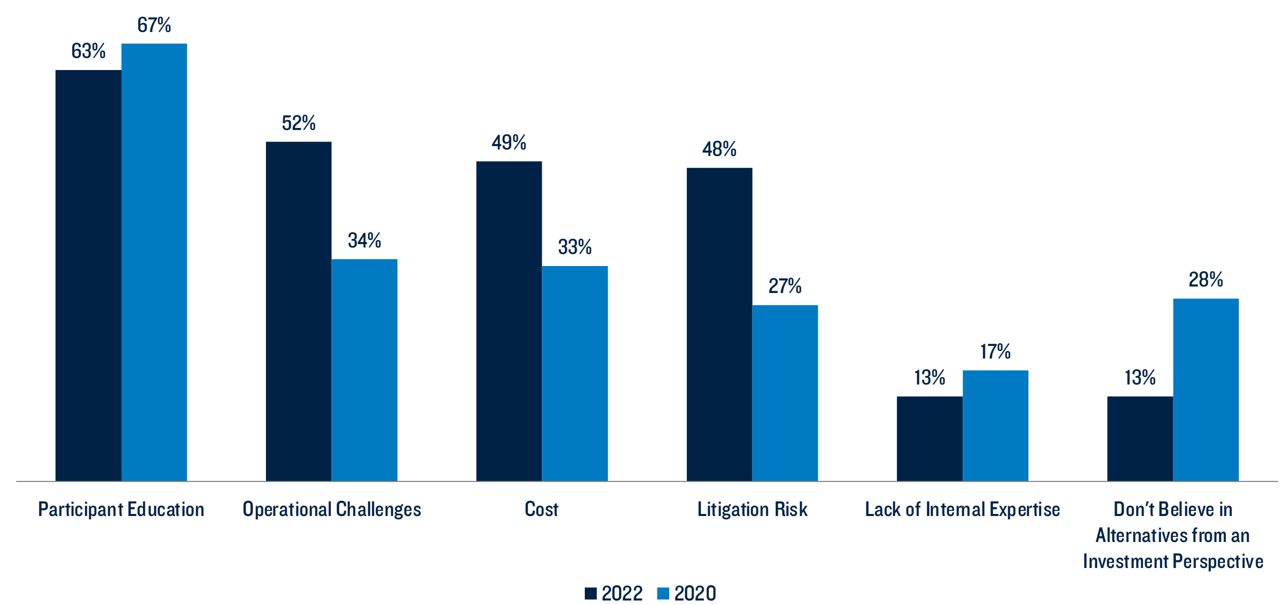
WHAT'S NEW

Most DC plan sponsors do not offer alternative investments as part of their TDF, although our research suggests a small uptick in usage and interest between 2020 and 2022.

- Just 6% of plan sponsors say they currently incorporate private credit or private real estate debt into their TDF, while 9% of plans use private real estate equity.
- More plan sponsors believe in alternatives from an investment perspective compared to 2020, but hurdles exist. The top three reasons sponsors are hesitant to offer alternative investments include a lack of participant education, operational challenges, and the associated costs for doing so – notably, litigation risk saw the biggest increase over the last two years.

9% of sponsors currently use private real estate in TDFs.

Reasons Plan Sponsors Don't Consider Alternatives



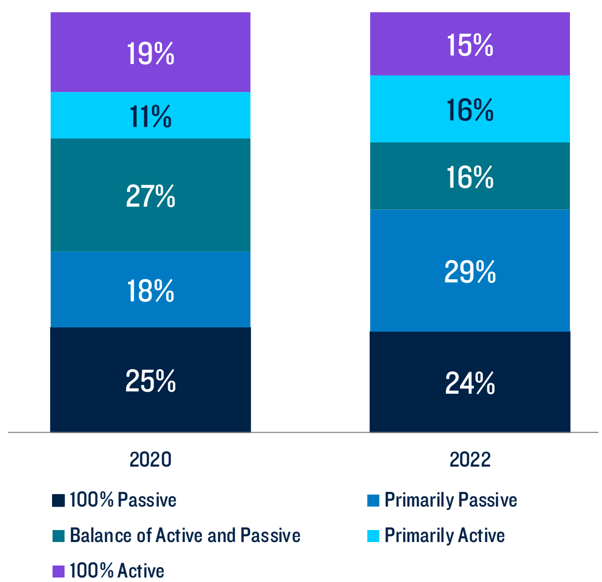
WHY IT MATTERS

- Private investments have been used in institutional and high-net worth portfolios for decades as a means for growing wealth and managing risk. Yes, certain operational limitations exist within DC plans, but significant progress has been made to integrate these more complex investments into DC investment solutions.
- Plan sponsors, consultants and investment managers are often the gatekeepers to providing access to alternative investments at more favorable institutional pricing – if there are suitable investments that are operationally feasible, this should be an area of exploration for plan sponsors and their advisors.
- Litigation risk is real, but it is a plan sponsor risk, not a participant risk. One driver of the trend towards simplified DC investments has been the perceived reduction in litigation risk; however, in 2022, we saw a spate of lawsuits against large plan sponsors who hired an all-passive target date manager. As fiduciaries, plan sponsors are required to do what is in the best interest of participants.
- To truly support participants' retirement outcomes, DC plan sponsors should learn from their DB counterparts and take an "institutional approach" that often includes a thoughtful mix of active and passive management, broad asset class diversification, and selective use of alternative investments.

ADDITIONAL THOUGHTS

- With 82% of plan sponsors using an off-the-shelf TDF, a meaningful increase in access to alternative investments would require a greater number of investment managers incorporating alternatives in their off-the-shelf TDF offerings.
- 6 out of 10 plan sponsors offer a TDF that has some mix of active and passive management. But size matters:
  - While custom TDFs are most popular within DC plans >$5B in AUM (16% of plans), many of these mega-size plans continue to use off-the-shelf solutions where passive or primarily passive management is more prevalent.
  - 100% active and primarily active TDF series tend to be more popular for DC plans < $1B in AUM.

Target Date Fund Management Style



CHAPTER 4

THE CHOICE IS YOURS (PARTICIPANTS)

Both Active and Passive Prevail on the Core Menu

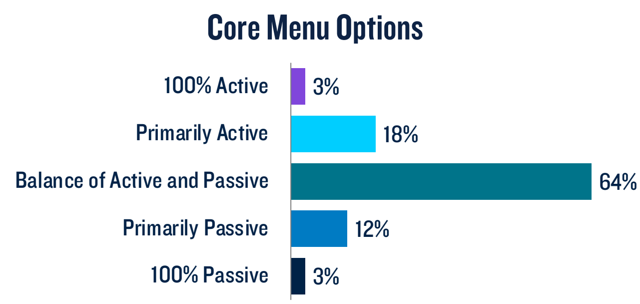
04

CHAPTER 4

THE CHOICE IS YOURS (PARTICIPANTS)- BOTH ACTIVE & PASSIVE PREVAIL ON THE CORE MENU

WHAT'S NEW

- 64% of DC plan sponsors offer participants a balance of active and passive options on the core menu, with 12% of plan sponsors leaning more towards active management, and 18% of plan sponsors leaning more towards passive management.
- Very few plan sponsors today offer 100% active or passive core menus.



WHY IT MATTERS

- If you look to institutional best practices, it will point towards a thoughtful mix of active and passive management when building multi-asset portfolios. There are certain asset classes that are inherently less efficient, including US small cap, emerging markets equity, fixed income, and real estate – where investors can benefit from actively managed strategies.
- Who is using the core menu? According to data from Prudential Retirement[1] participants who are approaching and in retirement tend to use the core menu more than their younger counterparts. These investors, given their proximity to retirement, require more diversified investments with better downside protection – all qualities that can often be found through actively managed options.

ADDITIONAL THOUGHTS

- There is a small percentage (less than 15%) of plan sponsors that are providing access to actively managed alternative investments via the core menu – whether direct or within multi-manager white label options.
- Liquid alternatives and private real estate equity are the most common with 12% of plan sponsors currently offering these, followed by private real estate debt with 6%. Despite cryptocurrencies making headlines in 2022, no plan sponsors reported it as an option, however, a few DC plan sponsors reported that they are considering it.

1 Prudential Retirement data on Professionally Managed Accounts vs. Self-Selectors as of 3/31/2021.

CHAPTER 5

THE MANY PATHS OF ESG

05

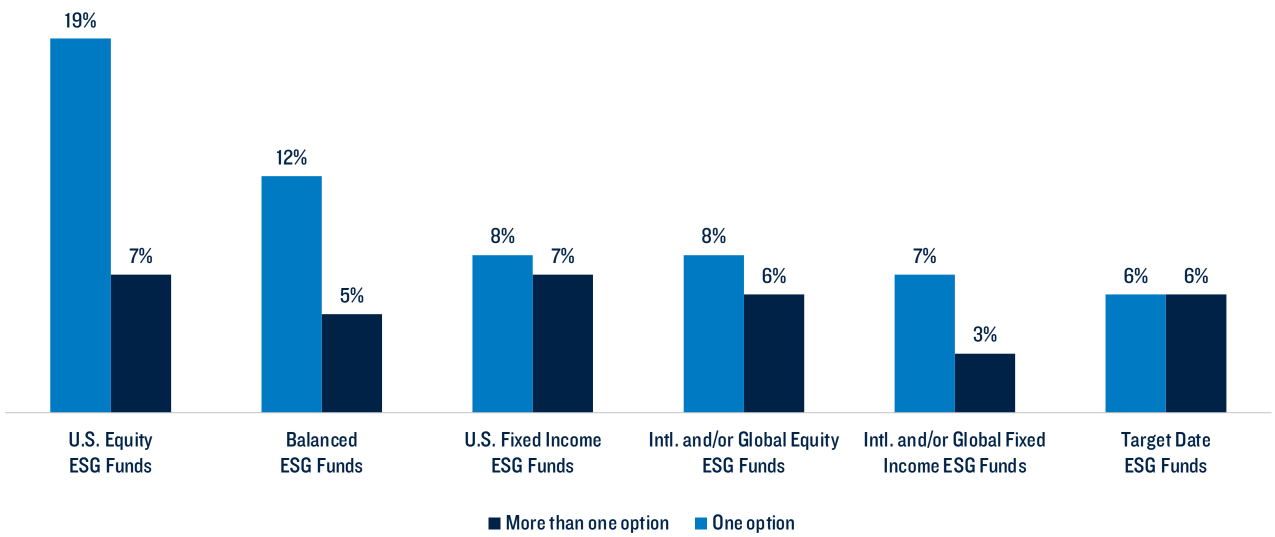
CHAPTER 5

THE MANY PATHS OF ESG

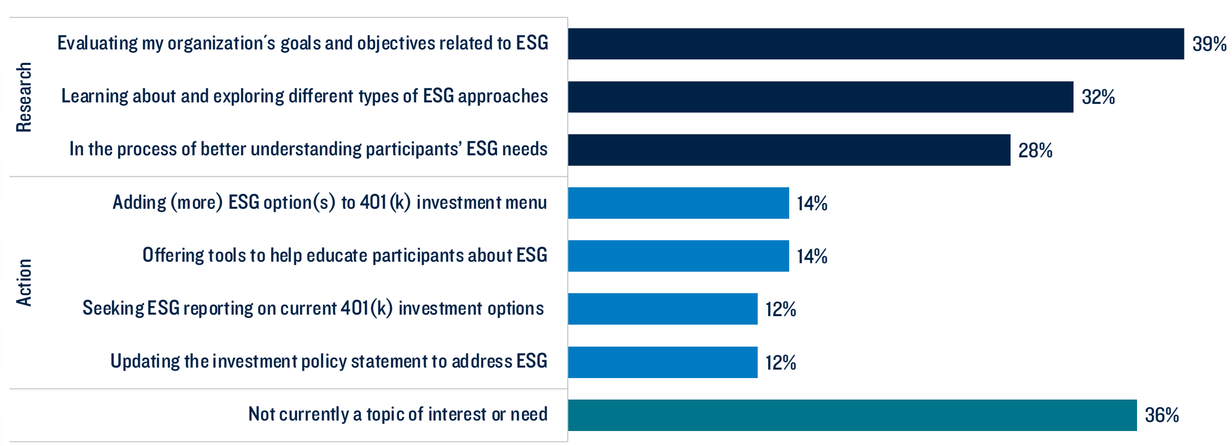
WHAT'S NEW

- 1 in 4 DC plan sponsors report offering an ESG option, with most offering a single US Equity ESG Fund or a single Balanced ESG Fund. While some plan sponsors offer multiple ESG options or even an ESG-oriented target date fund, it is much less common.
- ESG priorities vary for plan sponsors over the next 12 months – for 36% of respondents, ESG is not a topic of interest. For others, their ESG focus is centered around education, from identifying their internal organizational goals and learning about ESG approaches to understanding their participants' ESG needs.

ESG Investments in 401(k) Plans



ESG Steps in Next 12 Months



WHY IT MATTERS

- ESG continues to be an evolving area with differing views and changing definitions, a variety of approaches, and regulatory/legislative initiatives. Plan sponsors must balance participant demands with their fiduciary duty.
- With the Department of Labor's final Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights rule released in December 2022, we could see an increase in ESG interest and implementation within DC plans in the coming years. But the recent political contention in Washington over this rule may dampen any progress.

ADDITIONAL THOUGHTS

In 2022 we conducted comprehensive research of 9,000 new DC participants across 108 DC plans to understand their allocation decisions when provided access to at least one ESG fund in their plan[1]. Interested in our findings? The results of our research can be found here: A Review of ESG Fund Allocations Among New, Do-It-Yourself Defined Contribution Plan Participants

1 The recordkeeper providing the underlying data for this analysis is not identified due to privacy concerns, please reach out to the authors with additional questions regarding the source.

CHAPTER 6

WHAT'S TOP OF MIND FOR PLAN SPONSORS?

06

CHAPTER 6

WHAT'S TOP OF MIND FOR PLAN SPONSORS?

WHAT'S NEW

- Reported as a top priority in 2020, participant communications and engagement continue to rank as the primary focus for DC plan sponsors.
- 27% of plan sponsors listed retirement income as a top priority, with a greater focus (37%) from DC plans >$5B in AUM.
- Remarkably low on the list of priorities for the year are ESG and reviewing the Plan's QDIA (e.g., TDF).

PLAN SPONSOR SHORT-TERM PRIORITIES	ALL PLANS
Participant communications and engagement	58%
Plan and/or investment costs	52%
Investment menu design	41%
Plan design (e.g., auto enrollment, escalation)	37%
Financial wellness programs	36%
Retirement income solutions	27%
Evaluating your record keeper	18%
Evaluating your consultant/plan advisor	14%
ESG (Environmental, Social, Governance)	9%
Plan's qualified default investment alternative	6%

WHY IT MATTERS

- Despite multiple campaign efforts and the usage of different communication platforms, engaging participants continues to be a challenge for many plan sponsors. One of the 90 provisions include in the recently passed SECURE 2.0 legislation gives plan sponsors the ability to use small financial incentives. This presents a new opportunity for plans seeking to increase active plan engagement.
- Priorities differ depending on the plan sponsor role: Plan and investment costs ranked as the top priority (59%) for respondents who work in Treasury/Finance, while respondents from Human Resources ranked financial wellness as their second highest priority. This suggests that employers are focused on providing more holistic services that not only span retirement, but encompass financial planning, budgeting, and increased financial literacy – all areas that improve retirement readiness.

RESEARCH METHODOLOGY

- PGIM's 2022 plan sponsor research was conducted by Coalition Greenwich from May 23 to August 26, 2022, using an online, quantitative approach with DC plan sponsors in the United States who have at least one 401(k) plan and at least $100m in 401(k) assets.
- Total number of respondents was 155 plan sponsors; their AUM breakdown is as follows: 36 plans with $100-$249M AUM, 37 plans with $250-$499M AUM, 31 plans with $500-$999M AUM, 32 plans with $1-$4.9B AUM, 19 plans with over $5B AUM, and 31 plans using OCIO.
- The research was conducted on an unsponsored/blind basis with no mention of PGIM as the study sponsor.
- Participants were incentivized to participate with a summary of the research findings as well as a charitable donation to the American Red Cross or AMEX gift card ($100).
- Respondents had the option to determine whether to disclose their participation and/or individual responses.

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ABOUT PGIM DC SOLUTIONS*

As the retirement solutions provider of PGIM, we plan to deliver innovative defined contribution solutions founded on market-leading research and capabilities. Our highly-experienced team will partner with our clients on customized solutions to solve for retirement income. As of 12/31/2022, PGIM has $160 billion** DC assets under management.

* PGIM DC Solutions does not establish or operate pension plans.
** Reported data reflects the assets under management by PGIM and its investment adviser affiliates for defined contribution investment purposes only.

We look forward to sharing additional research results on plan governance and the usage of OCIOs that will shed additional light on the evolving DC landscape. Please look out for those findings later this year.

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