From Accumulation to Decumulation
Why It Matters and What Plan Sponsors Should Know

Key takeaways

• Through conversations with Fidelity clients—and consistent with industry surveys—we have noted increasing interest from DC plan sponsors in allowing retirees to stay in plan.

• Retirees and pre-retirees need help balancing risks—including investment, longevity, liquidity, and utilization risk—to translate accumulated savings into sustainable income.

• Fidelity’s recordkeeping data shows that older DC participants may not fully appreciate the importance of appropriate asset allocation and diversification as they age.

• Sponsors wanting to allow participants to stay in plan should consider offering post-retirement tools and education along with strategies and products that can help retirees to allocate their assets appropriately, generate income, and safely draw down savings during retirement.

Authors

Marcelle Daher, CFA
Investment Strategist
Workplace Investing

Dick Dahling, CFA, CAIA
Investment Strategist
Workplace Investing

Ruthann Pritchard, CFP®
Institutional Portfolio Manager
Global Asset Allocation

Bryan Tseng, CFA
Director, Investment Products
Global Asset Allocation
Introduction

Defined contribution (DC) plan sponsors historically have focused on enhancing participation and savings rates, but more recently they are paying closer attention to an aging workforce where many employees may not be financially prepared or emotionally confident in their ability to retire. Fidelity’s 2018 Plan Sponsor Attitudes Survey\(^1\) found that roughly a third of sponsors cited “effectively preparing employees for retirement financially” as their top concern, a shift from the prior year when “reducing business costs” related to the plan was cited most often.

Primary concerns for DC plan participants include “How much can I spend each year in retirement?” and “Will my savings last a lifetime?” To help participants answer these questions, plan sponsors must first develop an understanding of the challenges and risks participants face in addressing retirement income. Our research indicates that in addition to providing education on this topic, plan sponsors may have other resources available to help bolster employees’ confidence in retiring—and even to facilitate decumulation, the process of converting retirement savings into a durable income stream that may need to last for decades.

Fidelity’s recordkeeping platform services more than 16 million corporate DC participants. Through observations from the platform, combined with other Fidelity and industry research, this paper offers insights into how well participants, both those approaching and those already in retirement, are set up for the post-employment phase of their lives. Additionally, we offer some strategies and suggestions for plan sponsors wishing to help.

We focused our research on two growing populations: “retirees” and “pre-retirees.” For the purpose of this analysis, we deemed retirees as participants on our recordkeeping platform aged 60 years or older who have separated from service but remain in their DC plan, and pre-retirees as participants aged 50–59 who have separated from service but also still remain in plan. (In certain instances, we limited our analysis to those with a minimum balance of $50K to exclude smaller accounts that perhaps may not function as a primary source of retirement savings.) The need for understanding is growing: Over the past 10 years, we have observed a nearly 50% increase in the number of retirees and pre-retirees on the recordkeeping platform, and a near tripling of the assets held by these two populations combined.

The pivot to decumulation: How did we get here and where should we go?

DC plans surpassed defined benefit (DB) plans as workers’ primary source of retirement savings more than 20 years ago. At the end of 2018, DC assets exceeded $7.5 trillion, up from $3 trillion at the end of 2000 (Exhibit 1).

**EXHIBIT 1: DC assets reach 28% of U.S. retirement market**

U.S. Retirement Market Assets: $27 Trillion Total as of Year-End 2018

IRA: Individual retirement account. DC Plans include 401(k) plans, 403(b) plans, 457 plans, and the Federal Employees Retirement System (FERS) Thrift Savings Plan (TSP). Annuity Reserves: All fixed and variable annuities held outside of retirement plans and IRAs. Source: Investment Company Institute (www.ici.org); data through 2018.
Moreover, the Employee Benefit Research Institute (EBRI) recently estimated that, among private-sector employees whose employers offer a retirement savings benefit program, more than 70% have access solely to a DC plan.\(^2\)

Historically, traditional DB programs took the guesswork out of retirement cash flows and generally offered stable, lifetime retirement income with little participant involvement. Defined contribution plans, on the other hand, require employee engagement through both the accumulation and decumulation phases.

DC sponsors’ efforts to support plan participants in the accumulation phase are focused primarily on three key pillars: increasing plan participation, increasing savings and savings rates, and promoting prudent and diversified asset allocation solutions.

The shift to the decumulation phase, however, requires solving for a broader—and arguably more complex—set of risks, with important implications for DC plan design. Financial challenges facing all DC participants, but particularly those in or nearing retirement, include insufficient savings, suboptimal asset allocation, and a limited understanding of how much of their savings can safely be spent annually in retirement.

We summarize these significant potential and interrelated risks into four broad categories: longevity risk, investment risk, liquidity risk, and utilization risk (Exhibit 2), each of which can undermine a participant’s retirement success.

Plan innovations for the accumulation phase of retirement saving—such as auto-enrollment, auto-escalation, and the use of qualified default investment alternatives (QDIAs)—have proven beneficial to younger participants and are likely to have a substantial, positive effect on their overall retirement outcomes.

Older participants, however, may not have benefited from these savings features to the same extent, either because their DC plan adopted improvements too late in their careers to materially affect their retirement outcome or because such changes were not implemented at all for those closer to retirement. This has left many retirees and pre-retirees facing potentially greater post-employment challenges than participants in younger demographics. Plan participants of all ages, however, share similar financial worries.

For example, the 2019 EBRI Retirement Confidence Survey found that only 21% of employees and retirees felt “very confident” that they will have enough money

EXHIBIT 2: Retirees face significant potential and interrelated financial risks

<table>
<thead>
<tr>
<th>Longevity Risk</th>
<th>Investment Risk</th>
<th>Liquidity Risk</th>
<th>Utilization Risk</th>
</tr>
</thead>
<tbody>
<tr>
<td>With the benefit of increasing life expectancy comes increased risk that some retirees may outlive their retirement benefits. This is one of the most pressing issues facing DC plan participants today.</td>
<td>Prudent investment management and diversified portfolios are key to supporting participants and helping provide them the retirement income they seek.</td>
<td>Plan participants may need access to their money when unexpected emergencies occur. Products such as annuities and CDs may be less liquid and thus can restrict participants’ access to their savings.</td>
<td>Assisting retirees in managing how (and at what rate) to draw down their savings can help them make effective use of their assets and maintain a similar standard of living throughout their retirement years.</td>
</tr>
</tbody>
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Source: Fidelity Investments. For illustrative purposes only.
to last their lifetime (Exhibit 3). This highlights one of the most pressing concerns for defined contribution plan participants today: longevity risk.

In the same survey, less than a quarter of respondents felt confident they could maintain their standard of living in retirement, and the vast majority felt they needed help calculating how much monthly income they might need in retirement. These data points highlight two additional risks participants face: liquidity risk and utilization risk.

According to a separate EBRI study on spending patterns in retirement, many retirees have shown a disinclination to spend down their DC plan assets in retirement. The EBRI report cited uncertainties regarding life span, future medical expenses, and the variability of market returns as possible concerns, all of which can feed into follow-on uncertainty and doubt around determining a safe rate at which a retiree could spend down accumulated retirement savings. This lack of confidence may also influence a participant’s desire to keep retirement savings highly liquid and thus available for unanticipated events and spending needs.

Fidelity’s recordkeeping data suggests many savers may not be considering asset allocation or the effects of inflation as an important part of their retirement solution. Our research finds that large numbers of retirees and pre-retirees may hold an allocation outside a range that many sponsors—as well as Fidelity—would consider prudent to maintain throughout retirement, highlighting the fourth risk we identified: investment risk. We believe thoughtful implementation of a decumulation program addressing each of these risks can help those participants who are permitted to, and choose to, stay in plan past retirement.

Developing retirement income solutions involves recognition of the needs and concerns of both a plan’s participants and its sponsor, as well as an understanding of current participant behaviors and existing DC plan practices. Industry research and observations from Fidelity’s recordkeeping platform can offer valuable insights that may provide plan sponsors a starting point in evaluating whether and how to allow participants to stay in plan past retirement and how to support them throughout the decumulation phase.

EXHIBIT 3: What is top of mind for participants when thinking about the future?

<table>
<thead>
<tr>
<th>Will I be able to maintain my standard of living?</th>
<th>Will I even have enough money to last my lifetime?</th>
<th>How much money do I need each month in retirement?</th>
</tr>
</thead>
<tbody>
<tr>
<td>77%</td>
<td>79%</td>
<td>82%</td>
</tr>
</tbody>
</table>

Source: EBRI 2019 Retirement Confidence Survey.
Stay-in-plan benefits and challenges

According to a recent Fidelity survey, a majority of plan sponsors indicated they would prefer retirees have the flexibility to keep some or all of their assets in their employer-sponsored DC plan throughout their retirement years, whereas less than 10% preferred that retirees take all their assets out of the plan (Exhibit 4).

For retirees, staying in their DC plan can offer several benefits, including continued communications from the same trusted employer and recordkeeper they’ve had for some time, as well as potential access to more specialized offerings within the investment menu and the plan. For DC plans of all sizes, we found that participants holding company stock, invested in a stable-value option, or making use of a workplace managed account (WMA) showed higher stay-in-plan (SIP) rates relative to plans without these options.

Outside of the DC plan, such offerings can be more expensive or, in the case of stable value, unavailable. We also observed that DC plans of the largest employers historically have experienced SIP rates 7 to 9 percentage points higher than average. Larger plans may benefit from an ability to offer investment options with lower fees relative to those in a direct-sold or retail environment.

For plan sponsors, the SIP decision may be more complex. As a recruiting tool, for example, allowing retirees to stay in plan and offering them retirement support may be perceived positively by both current and prospective employees. In addition, plan sponsors may be better able to negotiate and maintain reduced recordkeeping fees that often come with a larger participant and asset base. Lower-cost investment options also may be more viable if higher-balance, older participants stay in plan.

On the other hand, SIP participants could incur additional fees for the sponsor depending on whether such costs accrue to the plan or to the participant. SIP participants may also necessitate a broadening of the investment lineup to offer options suitable for an older demographic.

Early indications are that participants may be embracing the opportunity to stay in plan past their separation from service (Exhibit 5). As of December 2018, 55% of retirees remained in their plan past the first year of retirement, compared with approximately 48% three years ago. Pre-retirees show a similar shift, with 66% remaining in plan last year as compared with about 55% to 60% in years prior. The percentage of participants staying in plan two years past retirement also has been rising.

Withdrawal strategies: room for improvement

According to EBRI, more than three-quarters of participants surveyed feel they need help calculating how much they can afford to spend each month in retirement. To date, full withdrawals have been the most common form of distribution from defined contribution plans, likely influenced by plan designs that disallow partial withdrawals. Without the flexibility to take just a portion of their assets, participants are effectively forced out of their plan when they want or need to access their savings.

For plan sponsors interested in supporting a SIP option, one area of opportunity may be to offer and educate...
participants on systematic withdrawal plans (SWPs), which historically have accounted for the smallest proportion of withdrawal activity from DC plans on Fidelity’s platform. SWPs commonly take the form of level dollar payments or variable payments over a fixed time period during which a participant’s entire account is distributed. Having additional types of SWPs available, such as payments based on a calculated percentage of a participant’s account balance or computed using an actuarial life expectancy, may better support participants’ cash-flow needs and bolster their confidence to retire.

We believe providing education on SWP availability along with tools and calculators to help model different SWPs’ potential impact on retiree cash flow and balances is key. Robust modeling capabilities can help answer many of the important questions that retirees face: How much will I have? How long can it last? How much will be left?

Innovation in this area has been gaining momentum. Many plan sponsors have shown interest in offering retirement income solutions that can help optimize participant withdrawals over the course of retirement while still allowing full access to their savings. These types of solutions can effectively address not only withdrawals but also asset allocation, another area where we have found participants need help. While guaranteed income solutions may be of interest, EBRI found that only 9% of retired workers favored investing all their DC assets in guaranteed options such as annuities. In addition to concern over costs, this reluctance highlights the importance of having ready access to, and full portability of, retirement assets.

**EXHIBIT 5: Stay-in-plan: an emerging trend?**
Retiree and Pre-Retiree SIP Rates One Year After Termination Date

Pre-retirees: participants aged 50–59, separated from service but remaining in plan; minimum balance of $50K. Retirees: participants aged 60+, separated from service but remaining in plan (deemed retired); minimum balance of $50K. Source: Fidelity Investments; stay-in-plan rates as of 12/31/18.
DC plan participant behavior: asset allocation

Plan participants can find the process of allocating their savings among investment options bewildering; many do not have the will, skill, or time to select and monitor their investments. Asset allocation and fund selection can be influenced by age, risk tolerance, and time horizon, among other factors, and a lack of diversification across asset classes relative to a participant’s circumstances and goals can materially impact retirement outcomes.

At Fidelity, we separate DC plan participants’ investment behaviors into two broad categories:

- Do-it-yourself (DIY) savers who retain accountability for investment decisions, both asset allocation and fund selection. DIY participants include not only those actively engaged in managing their assets but also those that have not engaged over the years and, as a result, may hold an asset allocation that is not consistent with the recommendations of their DC plan.
- Do-it-for-me (DIFM) participants, 100% invested in a multi-asset class solution such as a target date fund (TDF) or workplace managed account.

Since 2006, when the Pension Protection Act offered “safe harbor” to sponsors defaulting participants into a QDIA such as a TDF or WMA, younger participants have increasingly shifted to the DIFM model. For older savers, who were less likely to have been defaulted into a QDIA, the majority remain DIY. As of year-end 2018, more than half of terminated participants on the recordkeeping platform over the age of 40 were DIY investors (Exhibit 6). For those over the age of 70, the proportion rises to 83%.

**EXHIBIT 6: Older participants are more likely to be DIY investors**

Terminated Participants by Age and Investment Classification

![Terminated Participants by Age and Investment Classification](image-url)

*100% TDF* and “100% WMA” investors represent participants who hold their entire balance in a target date strategy or a workplace managed account, respectively. “Do-It-Yourself” (DIY) investors represent participants who hold less than 100% of their balance in a target date strategy or managed account. Source: Fidelity Investments; investment allocations as of 12/31/18.
As participants age, their relative portfolio exposures may become more concentrated and less diversified: Many DIY participants on Fidelity’s recordkeeping platform maintain an asset mix outside of that recommended by their respective DC plans (Exhibit 7). A risk in having too high an allocation to equity or to cash is that investors may experience favorable investment results in certain market environments but leave themselves more vulnerable in others. For example, depending on the market environment, having too high an equity allocation could expose retirees to large market drawdowns and potentially result in a more volatile income stream; conversely, a higher-than-recommended allocation to cash could result in less retirement income overall.

One simple and common approach to assessing asset allocation is to review equity exposure. As of March 31, 55% of both retirees and pre-retirees had higher equity allocations than what might represent an appropriate mix for investing throughout retirement; 31% and 22%, respectively, had lower-than-recommended allocations. These investors also held the highest level of what Fidelity considers “extreme” allocations compared with other age groups: About 14% of retirees and 17% of pre-retirees were 100% invested in stocks; roughly 15% and 8%, respectively, had zero equity exposure. While measuring a DC participant’s equity assets may be a simple way to gauge exposure, it should be remembered that equity levels may not represent a complete picture of the risks and diversification within an individual’s full portfolio.

As retirement savers age, their financial affairs may grow more complex. Some DC participants may have unique circumstances, including access to savings or investments beyond a 401(k) plan. In such cases, an asset mix outside

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**EXHIBIT 7: Many older participants may not hold a diversified portfolio suitable for retirement investing**

A Simplified View of Diversification: Equity Allocations of Different DIY Age Cohorts

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DIY: Do-it-yourself. Participants represented have been terminated from service but remain in their plan. The equity band represents an interval of ±10 percentage points (not to exceed 95%) around the equity allocations of each corporate DC plan’s respective target date provider on Fidelity’s recordkeeping platform. Participants with a diversified portfolio falling within the band may hold an asset allocation consistent with saving for retirement. This analysis used the equity allocations of the target date provider within each specific plan (e.g., Fidelity, Vanguard, BlackRock, JPMorgan, etc.). Source: Fidelity Investments; investment allocations as of 3/31/19.
of sponsor-recommended ranges may be appropriate. In other cases, however, a concentrated portfolio may be the result of inattention or inaction.

Consider, for example, participants invested primarily in equities over the past 10 years of extraordinary U.S. stock market gains: They may not have updated or rebalanced their holdings and, as a result, may not hold a diversified portfolio appropriate for investing throughout retirement.

Plan sponsors can assist with participants’ asset allocation needs through educational materials and tools, but also via more proactive strategies. Consider participants that have just entered retirement and choose to stay in plan: In many cases, “resetting” their allocation by defaulting them into a QDIA with an age-appropriate asset mix could set them up for a better retirement outcome.

Conclusion
While innovation in decumulation is slowly reaching the marketplace, DC plan sponsors can take steps today to better equip aging participants to achieve retirement success. For example, plan sponsors can:

• Consider allowing participants to stay in plan past their retirement date.
• Review plan documents to ensure they include features that support participants’ staying in plan.
• Consider adding investment options aimed at income generation and whether a QDIA could “reset” retirees’ asset allocation to help improve retirement outcomes.
• Explore the availability of decumulation options on the recordkeeping platform, including SWPs and partial withdrawals, to provide participants with flexibility.
• Provide targeted training, education, workshops, webinars, tools, and calculators for DC participants nearing and in retirement.

Please contact your relationship manager to learn more about retirement income solutions.

Authors

Marcelle Daher, CFA | Investment Strategist
Marcelle Daher is vice president of Investment Strategy within Fidelity’s Workplace Investing division. In this role, she provides investment services to Fidelity’s 401(k) clients, including helping plan sponsors with performance monitoring and measurement, investment fund selection, and investment menu design.

Dick Dahling, CFA, CAIA | Investment Strategist
Dick Dahling is vice president of Investment Strategy within Fidelity’s Workplace Investing division. In this role, he provides investment services to Fidelity’s 401(k) clients, including helping plan sponsors with performance monitoring and measurement, investment fund selection, and investment menu design.

Ruthann Pritchard, CFP® | Institutional Portfolio Manager
Ruthann Pritchard is an institutional portfolio manager in the Global Asset Allocation group at Fidelity Investments. In this role, she serves as a member of the investment management team and is also a principal liaison for portfolio management to a broad range of current and prospective clients. Ms. Pritchard’s focus is U.S. and Canadian target date strategies and retirement income solutions.

Bryan Tseng, CFA | Director, Investment Products
Bryan Tseng is a director in the Investment Products group (Global Asset Allocation) at Fidelity Investments. In this role, he is responsible for product management, development, strategy, and advocacy for Fidelity’s asset allocation strategies with a focus on retirement income solutions.

Fidelity Thought Leadership Director David Risgin, CFA, provided editorial direction for this article.
Endnotes:

1 The ninth annual Fidelity Plan Sponsor Attitudes Survey can be viewed at go.fidelity.com/attitudes.


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