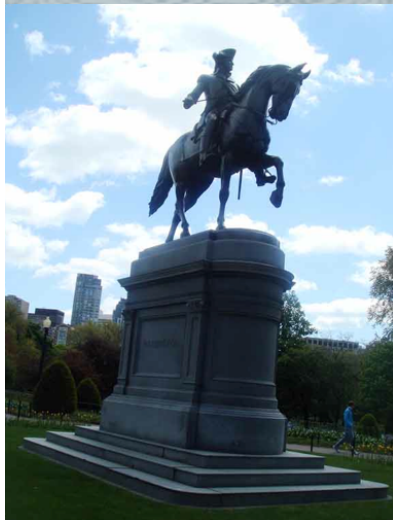


WM Monitor: Focus on Wealth Management

This edition: A recap of the FRC's 2009 Retirement Forum, Revitalizing Retirement—Navigating the New Market Reality



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ABOUT EZRA GROUP

Launched by Craig Iskowitz in 2005, Ezra Group is a consulting firm providing software development services, business strategy and operational expertise. Our focus is in the financial services industry, including wealth management, brokerage, private banking, equity research and hedge funds.

FRC's 5th Annual Retirement Conference

The Future Retirement Crisis

This edition of Ezra Group's WM Monitor is dedicated to the Financial Research Corporation's 2009 Retirement Forum, which was held in Boston on June 17, 2009.

As part of his opening remarks, Robert Hedges, Managing Partner at Mercatus, LLC, related a story about a dinner party he attended two weeks ago with Congressman Barney Frank (D-Mass.) chairman of the House Financial Services Committee. At the end of the evening, after a wide-ranging discussion about the financial crisis, someone asked him, "What is the biggest issue facing the US economy?" Rep. Frank replied, "Retirement. But that's not my committee."

While congressional recognition of the crisis is important, our readers are looking for real solutions to client retirement concerns, such as the recommendations from the panelists in The Mind of the Advisor & Consumer on page 3. In this edition, you'll find the answers to questions such as "What are clients top concerns?", "What should advisors do?" and "What would be an ideal, diversified investment fund lineup?"

Please send any comments or suggestions to craig@ezragroup.net.

Keynote Address

The Realities of the Global Economy

The speaker in this session was Zachary Karabell, President of River Twice Research. He is an economic analyst, political historian, author and former President of Fred Alger and Company and Chief Economist at Fred Alger Management.

The Globalization Disconnect

Karabell began by focusing on the connectedness of the global system and the theory that everything is connected. This theory has many ramifications and implications, he explained, but to some degree it's overstated. This is because a disconnect exists between what goes on in the world and the things we do.

The mantra of globalization has affected what everyone does without anyone being able to make sense out of it, insisted Karabell. The title of a new book published by a group of economists is a good example of an attempt to understand the effects. It's called, "globalization: n. the irrational fear that someone in China will take your job". The point is that globalization is an easy term to talk about, but no one really knows what it means.

Is Everything Really Connected?

Are things predictable or will there always be continuous change? Karabell asserted that one of the dangers of human society is its proclivity to regularly proclaim that a new paradigm exists and that everything has changed.

Sometimes things just don't obey patterns, Karabell noted. He then quoted Mark Twain who said, "History does not repeat itself, but it does rhyme." This is one of the biggest challenges today if what you need is predictability.

The world isn't as connected as people think, Karabell observed. If something happens in one place, everyone will find out about it only if it's dramatic enough to attract the attention of the world media. When this occurs, it creates a level of connectedness that makes us aware with a level of real-time immediacy which is unusual in human history.

Whatever happens politically in the world is not always connected to the global economy. The Nigerian civil war has been going on for 15-20 years, but it's had almost no effect on people in the rest of the world. This doesn't support the globalization thesis that "anything that happens anywhere, happens everywhere".

There's a temptation to try and connect everything, but maybe things aren't as connected as they seem, Karabell proposed. The danger in making connections where they don't exist is almost as dangerous as not making them when they do exist.

Capital Connects Everything

The flow of capital connects everything, Karabell observed. Capital has a mobility and fungibility that creates huge vulnerabilities. The greatest iteration

globally without knowing what is going on in China. Over the past ten-year period, China has been to the global system what the US was a hundred years ago. It's the change agent and the factor that wasn't accounted for in most models. It threw the global supply chain out of whack and upset the predictions of future global demand for commodities, which caused the tremendous spike in prices.

The problem, according to Karabell, was that the models were predicated on steady global growth, like the patterns established throughout much of the 20th century. The reality is that unexpected things happen.

China is the #1 foreign holder of US Treasuries.

The predictions our models are making now will most likely "crash into the shoals" of future events that we're unable to anticipate. It should give us pause regarding any prognostications as to what will happen even a year from now. Long term forecasts have less and less value the farther out they go.

No demographic forecasts over the past 220 years have proven to be true. Not since Thomas Malthus raised the alarm about the impending population boom and the inability of the planet to support it, have we had any accurate demographic forecasts. This isn't a knock again demographers, it's simply an observation, Karabell stated.

China broke all the rules as to what a society should do in order encourage stability and growth. It has a closed capital account, a largely closed banking system, and didn't adopt any of the recommendations of the IMF or World Bank as to how it should govern its

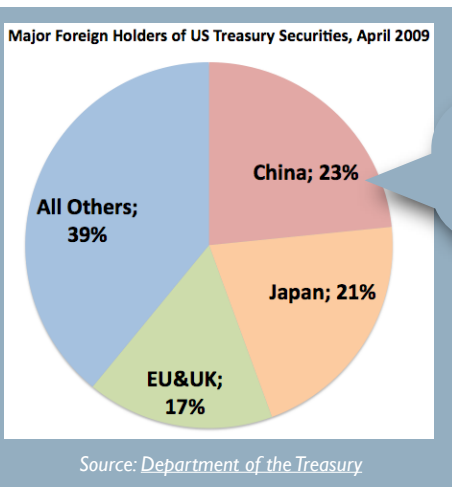
"It's impossible to gauge what's going on globally without knowing what's going on in China."
-- Zachary Karabell, River Twice Research

Their version of cradle-to-grave social support, often referred to as the "Iron Rice Bowl," has disappeared, which has led to a higher national savings rate.

China Controls Our Future

One reason that US interest rates have been lower than expected is because the Chinese have been plowing their surpluses into Treasuries and global bonds. The health of the US economy has become dependent on the growth of the Chinese economy as more US companies come to rely on the Chinese market for a large part of their sales.

The next ten year period is likely to be dominated by China. The global economy is around \$45-50 trillion and although China is just one part (approximately \$4-5 trillion), its effects can be felt throughout. Karabell used the analogy of a glass of water to represent the global economy. China's effect is like pouring in some coffee. The glass still contains mostly water, yet the entire composition of the glass has changed. In that sense, the global economy as a system may still be what it was, but with the impact of China impinging upon it, it changes the overall complexion dramatically. ♦



and transformation in the global system is that capital is now transferred electronically and allocated computationally. This kind of linkage leads to a disintermediation between people and the capital that's flowing. It also means that the flow of capital can no longer controlled by individual countries.

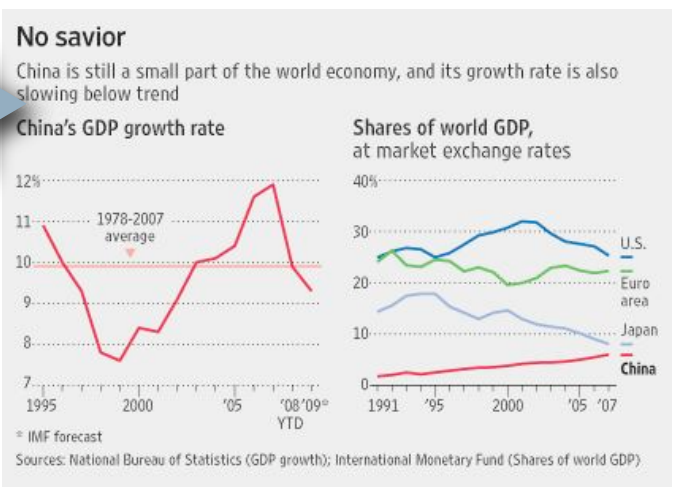
Karabell believes that the financial meltdown was almost guaranteed to occur due to the the systemic issues that resulted from the global capital connectivity. The sub-prime housing market was just the specifics. If it wasn't that, it would have been something else, he insisted. When capital is linked everywhere, then there's no longer any more regional crisis due to the mobility and globalization of capital.

Models Don't Work

A very important, but previously unexplained exception to this rule has been China, which is simultaneously both closed and open, Karabell explained. It's impossible to gauge what's going on

A slowing GDP growth rate may limit China's future impact on the global economy.

economy. It's dependent on state spending (approx. 50%), its consumer economy has been growing, but it's still mainly a savings culture.



You can read more from Zachary Karabell on his blog at blog.rivertwice.com

Making Sense of Retirement

The Mind of the Advisor & Consumer

The speaker for the first part of this session was Margaret Rorick, SVP, Market Research Director, FRC.

Retirement Research Results

The retirement demographics are changing, according to Margaret. In 1955, the average 65-yr-old could expect to live for another 14 years, to 79. In 2005, a 65-yr-old's life expectancy was 84, which is 26% increase to 19 years.

Margaret discussed the results of two FRC studies: Advisor Insight Series 2009, which interviewed 1,200 advisors, and the Consumer Retirement Income and Planning Study coming out later this summer containing in-depth consumer profiles.

Advisors were asked, "what are your client's top concerns?":

1. funding retirement
2. further market declines
3. health care costs
4. taxes
5. inflation

Investment Guarantees

94% of advisors have fielded questions from their clients about investments guarantees in the past year, Rorick noted. They ask about principal preservation twice as often as income levels or rate of return. Advisors say this is a hot topic today, but there are gaps in consumer knowledge. One is a fundamental misunderstanding about what investment guarantees offer. The recent declines in the market have redefined consumer's risk profiles, but advisors should ensure that clients don't overload on guarantees now.

Financial Planning

Rorick reported that only 45% of customers 45-64 believe their savings is on track for retirement while 26% feel they already have enough saved for retirement. Just over half think they have the right investment selections to meet their retirement goals.

Approximately 46% of consumers 45-65 have no financial plan. Of the ones that do, 62% did not use an advisor. 26% of consumers 65-74 are working full

or part time. While 48% of those 45-64 say they plan to work in their retirement.

Advisors Are Doing More With Less

Advisors reported the following changes at their firms over the past 12 months:

- Reduced support staff
- Reduced marketing budget
- Merged with another firm
- Reduced comp structure
- Reduced payout ratios

While these changes have put advisors between a rock and a hard place, it does present opportunities for business partners to step up and provide support.

All this represents a long-term shift in the market place, as retirement moves from one form to something that could take many forms for consumers, Rorick asserted.

"62% of consumers who own target date funds think they can retire on the fund's target date and 38% thought there was a guaranteed return."

-- [Survey](#) by Evestnet Asset Management

Panel Discussion: What Now?

The panelists were Don Froude, President, The U.S. Advisors Group, Ameriprise Financial Services, Steve Mitchell, COO, Retirement Income Industry Association (RIIA), and Ben Norquist, President & CEO, Convergent Retirement Plan Solutions.

How are advisors handling the concerns and shift in consumer risk profiles?

Don Froude -- "The advisors today are facing a conflict. For many years, the number one goal for investors has always been retirement. Because of what's happened, there's been this rush to abandon their plan and raise an enormous amount of cash. Cash, liquidity, stability and safety has become even more important than retirement holdings. Consequently, we've seen 41% of people have cutback on their retirement funding and of those, 15% have said that they intend to make the cuts permanent."

What should advisors do?

Steve Mitchell -- None of the tools or processes we created have protected our clients from the horrible losses that have been so widespread. We're very focused on working with our members to improve the advisor process to help protect our clients going forwards. The need for financial security has replaced retirement planning. You need to build a floor of financial security at a level that the client is comfortable with and then think about the upside.

What will it take to address all of the changing elements of retirement planning?

Ben Norquist -- Advisors are being constrained time-wise and resource-wise. A recent survey showed that 50% of advisors in the retirement space used a bucketing strategy, which is very labor-intensive. I think we'll see new technologies introduced to help streamline this process and make it more efficient.

We also believe there will be quite a bit of movement in tax management and tax alpha. There's an emerging consensus that significant advantages can be gained through tax-wise planning. LifeYield is working on tools to support client's decumulation phase.

What is the current state of guaranteed products?

Don Froude -- Two years ago, we created the concept of the Retirement Income Framework. This framework helps the advisor position the client to help create a "retirement paycheck". It's broken down into four components:

- Long & Short Term Assets
- Pension & Social Security
- Annuity Products
- Contingent Assets (i.e. Home Equity Loans)

Investor attitudes towards guarantees have changed dramatically. Back in 2004, only 28% were interested in some form of guaranteed income. It's

For more information on the FRC Advisor Insight Series or Consumer Retirement Income and Planning research study, email frcinfo@frcnet.com or call 866-532-8009.

up to 61% now. Unfortunately, as an industry, we haven't done a good job in positioning these products considering their overall complexity and the recent turmoil in the insurance industry.

What do consumers think needs to be changed in our industry?

Steve Mitchell -- One trend we've seen is that immediate income annuities haven't taken hold in large percentages of clients. It seems that many clients haven't been willing to make that irrevocable decision to turn over a big portion of their assets in return for a guaranteed income stream. We have seen that variable annuities (VA) combined with different forms of living benefits have recently become quite popular.

“Back in 2004, only 28% of investors were interested in some form of guaranteed income. It's up to 61% now.”

-- Don Froude, Ameriprise

However, given the current level of uncertainty, it's become very difficult to make these kinds of guarantees. There are major VA providers who were writing annuities with living benefits, sitting in board rooms now, feeling incredibly thankful they didn't sell more of them!

As an industry, we haven't figured out a reliable way of guaranteeing principal. We're seeing a significantly increased pricing level on living benefits within VAs. All types of principal protection, whether it's hedging strategies or various guarantees within insurance products aren't terribly efficient.

Therefore, when the advisor and the consumer are trying to decide between asset allocation and principal protection, neither option seems particularly attractive in many cases.

One thing that we can all focus on is, “How do we provide better downside protection? What does the product look like? Is it inside an annuity wrapper or some other kind of structured product?”

What are some winning strategies for supporting decision makers?

Ben Norquist -- Looking at it from a fund company perspective, regarding retirement wholesaling models, we've had

a pendulum swing between generalist wholesalers and retirement specialist wholesalers in delivering the retirement message in retail and institutional markets. It's challenging to take a generalist wholesaling team and have them deliver your retirement value proposition. A better approach would be a hybrid model, where you have some people with deep retirement expertise in the field working closely with your wholesalers and advisors.

Have you changed your advisor compensation grids in response to the financial crisis?

Don Froude -- We haven't changed our grids at all. Our core value proposition is the number of plan relationships an advisor has. This is combined with the overall asset base, the amount of high value clients acquired as well as the overall gross dealer commissions (GDC).

Financial planning is the lifeblood of our firm. Our average planning client is 75% more satisfied than our non-planning clients. They have 2x the assets with us and produce 2.8x the GDC of non-planning clients. Our planning clients are almost twice as likely to refer another high-value planning client. ♦

Product & Distribution Strategies The Retirement Plan of the Future

The speaker for this session was Jeffrey R. Carney, Head of Global Marketing, Products and Retirement, Putnam Investments.

Income Replacement Problem

“Putnam measures retirement success in terms of income replacement,” Carney began. “Today's retirees draw roughly 2/3 of their income from program sources such as traditional pension and social security. But as we know, both those sources are shrinking.”

Carney noted that the capacity of social security to replace pre-retirement income is on track to decline from 39%

to 29% by 2030. This is mainly due to the increases in the age of eligibility and the rising cost of Medicare benefits.

The retirement industry is at a crossroads, Carney announced. A way must be found to deal with these realities:

- people are living longer
- social security & pension incomes are declining
- responsibility for creating retirement income is shifting to the individual
- steady market returns are gone

Defined Contribution (DC) Plans

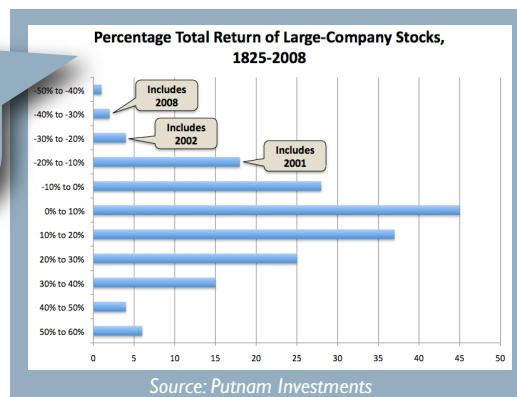
DC plans, such as 401(k)'s, were the first major breakthrough in retirement planning. They grew from roughly 10 million participants in the 1980's to over 70 million today, Carney explained.

But there were problems. 401(k) plans were voluntary, so not all employees took advantage of them. They also required participants to structure their own investment portfolios from a wide array of unfamiliar options. The assumption was that every working American could instantly become their own skilled pension fund manager!

Another major breakthrough was the Pension Protection Act (PPA) of 2006. The act endorse some of the plan methods that were working, such as auto-enrollment, escalation and the diversified default options. By bringing these methods into the mainstream, the PPA increased enrollment rates and reduced participant's risk through diversification.

Market volatility has increased tremendously the past decade. As shown in the chart below, three years since 2000 have seen declines of between 10% and 40%. There must be more focus put on volatility reduction in the next stage of workplace plans. This focus on volatility reduction should also include an equity

Three volatile years with negative returns occurred this decade.



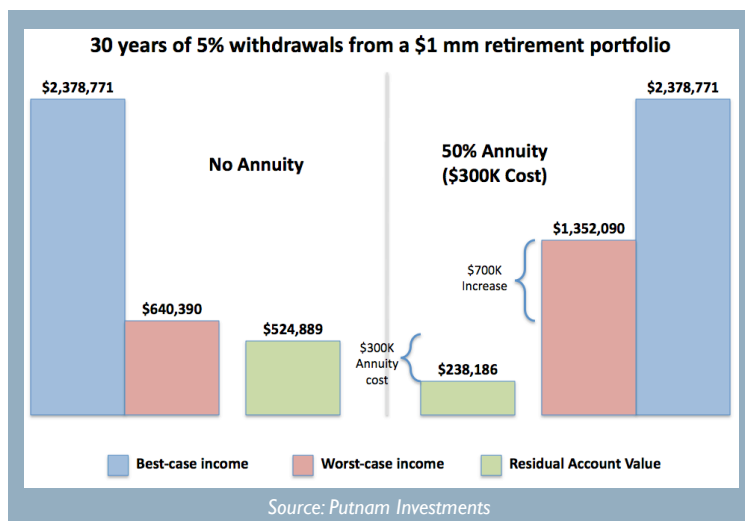
cap on mature-stage life cycle funds, asserted Carney.

Before the financial crisis, many mature-stage life-cycle funds had equity exposures over 50%. “We now know that this is a very risky place to be when a 100-year flood washes over the markets,” Carney stated. Putnam’s retirement-ready 2010 fund resisted the pressure and held to a conservative 28% allocation.

In addition to focusing on reducing volatility, there will be a new embrace of guaranteed income products, reported Carney. In fact, this idea has already arrived, in the form of new legislation introduced in Congress. The bill would allow retirees to take a portion of their savings in the form of an annuity and allows a 50% tax exclusion from non-qualified lifetime income for up to \$10,000 per year.

Annuities have not always been well-received, Carney noted. They’ve been plagued by complexity, high fees and a reluctance on the part of investors to hand over their life savings. However, he believes that with the right safeguards and transparencies, annuities can play a valuable role in providing a security net for retirees.

Carney provided an example (shown below) of an investor with a \$1 mm retirement portfolio that withdraws 5% annually for 30 years. By purchasing a 50% annuity for \$300K, the worst-case income scenario improves by over \$700K, although the residual value of the account is reduced by the amount of the annuity. ♦



Luncheon Keynote Address Research from CFO Magazine

The speaker was Sam Knox, Vice President and Director of Research at CFO Research Services.

DB Plans Funding Take a Hit

CFO Research has done a number of different studies of senior finance executives and some of the highlights were presented by Knox.

Among DB plans (conventional pensions), the funded ratio (asset value divided by liability value) has declined at more than 90% of US companies from 2007 to 2008, Knox reported. Half of plans saw their funded ratio decline by 25% or more.

The financial crisis has punished DB plans in two ways, Knox explained. First, it has driven down asset values dramatically. Second, interest rates used to discount pension liabilities haven't fallen, and as a result, pension liabilities remain high and the funded status of companies has fallen.

This funding deficit comes at a very difficult time, Knox said. Companies are under-funded in their pension plans, while cash is at a premium due to poor operating performance. It will be difficult for companies to pay in extra to their DB plans to restore them to health.

While DC plans account values have fallen significantly, Knox maintained, their structure shields companies from much of the risk.

Older Employees Retire on the Job

63% of companies surveyed reported that their working environment

is suffering due to employee concerns about personal finances, Knox reported. As result of the crash and economic downturn, many employees

are not able to retire as they originally planned. They instead “retire on the job” and in effect, wait out their employment while still drawing their paychecks, observed Knox. The productivity and efficiency of these workers would then be suspect.

This reduction in the number of retiring employees in turn creates a shortage of growth opportunities for younger workers and impacts the company’s human capital strategy, according to Knox.

Human Capital Strategy

When surveyed, 70% of employers said they were focused on the long-term viability of their current DB plans versus looking for alternatives, such as terminating the plan. Employers believe that having a DB Plan serves a human capital and financial purpose in their company’s overall strategy. A DB Plan improves employees sense of financial security, which has taken a beating lately. It also reduces the incidents of “retiring on the job,” by facilitating the retirement of older employees and making room at the company for “new blood”.

DB/DC Plans Becoming More Conservative

A survey of finance executives found that they anticipated changes that would make their DC plans more conservative in the next few years, such as:

- increasing automatic enrollment
- implementing contribution escalation programs
- offering fewer investment options
- eliminating high risk investments.

The same survey found the following risk-related changes were in store for many DB Plans:

- performing formal risk assessment
- adopting risk management method (i.e. duration matching)
- adopting a more conservative asset allocation strategy

Only 17% said they had already frozen or terminated benefits, 22% said they were very likely to do so and 31% said that they were **not** likely to do so. ♦

For more information, go to:
www.cforesearch.com

Stopping 401(k) Matches: The New No-brainer

At least 40 employers have stopped contributing to their employees' defined-contribution (DC) plans.

David M. Katz - CFO.com

On a day like Monday, when five big companies reported a total of at least 57,000 layoffs, it was easy to see why CFOs might want to stop providing a match to employees' 401(k) savings. In many cases, it's an easy way to cut a cost worth 2 or 3 percent of your payroll without having to give employees more than a week's notice.

A fast-rising group of big-name companies have taken the hint. Stretching from last June until January 26, 40 employers have announced plans to change or cease their 401(k) matches, according to a non-comprehensive list put together by the Pension Rights Center, a nonprofit consumer-rights organization.

(read the rest of this article at: <http://www.cfo.com/article.cfm/13045596?f=search>)

FRC Research Session

Charting IODC Distribution in a Changing Landscape

The speaker was Luis Fleites, VP, Director of Retirement Markets Research, FRC.

IO Assets Dominate Plans

According to the FRC Investment-Only Defined Contribution (IODC) Investment Manager Survey, March 2009, DC Plans are the primary retirement vehicle for American workers.

Open architecture continues to make progress in DC Plans, even as target date funds proliferate.

2008 was the first year that Investment-Only (IO) assets were larger than proprietary assets in DC Plans. IO is growing around 8% annually, while proprietary is growing at roughly 6%.

The tax subsidies for plan contributions are estimated to total \$76 billion this year. Inertia was a major factor that kept many participants from reducing their regular payroll contributions.

Recordkeepers Enter the Market

Fleites noted that recently there has been a noticeable increase in the number of proprietary recordkeepers with dedicated IODC teams entering the market. Leading full-service recordkeepers, such as Fidelity, Vanguard and T. Rowe Price, are also competing to capture third-party platform sales.

The average size of dedicated IODC Teams (sorted by IODC assets):

- Tier 1 (< \$10 bil) = 7.5
- Tier 2 (\$10-\$20 bil) = 13.5
- Tier 3 (> \$20 bil) = 14.1

Many firms are adding retirement product specialists to compliment their teams and add a deeper level of knowledge.

Where's the Money Going?

Fleites took the latest data on monthly contributions to IO funds from Hewitt Associates 401(k) Index and averaged their monthly contributions for different asset classes. What he found was that Lifestyle/Pre-Mix (Target Date Funds) was the leader with approximately 18% of flows. Large Cap US Equity was second with around 17% and GIC/Stable Value was third with almost 16.5% of new asset.

In the R-Share Market, Large Cap Growth saw \$14 bil in net flows, which was 30% of the category's total assets. This can be compared to Foreign Large Cap Growth, which saw only \$2 bil in net flows, but this was 113% of the category's assets. Target Date Funds saw net flows of almost \$4 bil, which increased current assets by over 75%. ♦

For more information on the FRC Investment-Only Defined Contribution research study see: <http://www.frcnet.com/pdfs/2009-FRC-IODC.pdf>



Afternoon Session

Evolving DC Investment Plan Line-Ups

The panelists were Hal Bjornson, head of Investment Services Group, J.P. Morgan Retirement Plan Services and Peter Gosselin, Senior Director / Manager - DC Investments, Mercer.

Speaker Overviews

JPM Retirement Services Group has over 1,000 employees, over \$90 bil in assets that are record-kept, and 1.5 mil plan participants according to Bjornson. Their platform is open architecture.

Mercer's Gosselin mentioned that they've seen a big trend in the past six months towards passive target date funds. 20% of their business is in custom target date funds. Participants are becoming more conservative and sponsors want to expand beyond Equity Core and Core+ to include fixed income. International has become more popular in 401(k) plans.

What would be an ideal, diversified investment fund lineup?

When working with plan sponsors, Bjornson said, their philosophy is to build a simple core menu. Starting with Large Cap Core, Growth and Value, they add Mid-Cap Growth and Value, but in Small Cap space they only look at Small Core. In International, they use Foreign Large Blend as part of a three-tier menu based on client sophistication.

7% of JPM plans offer passive target date funds and two plans exclusively use target date funds. 17% of plans are self-directed brokerage accounts.

"Simple is the way to go," opined Gosselin. People are realizing that they need more asset classes and are adding products such as TIPS and Emerging Markets. Space is an issue when a plan

already has 10 options along with their target date suite. People need to think about how many equity funds they offer. Maybe collapsing their Large Cap Growth and Value will free up space for more International options.

Will these new fund lineups be replacing existing asset classes or be offered in addition?

“It’s a little of both,” replied Bjornson. “We’ve seen a few plans look at TIPS funds, but emerging markets not so much”. One problem is how do you know if someone is allocating 30% of their portfolio there?

They’re seeing a lot of activity now around replacing underperforming managers, according to Bjornson. He also said that some plans are starting to look at the custom target date option. In those, there’s a possibility of seeing other things such as completion strategies, where you have the best of both worlds; the core menu that they’ve built and adding on a custom target date. However, this hasn’t seen the take-up that everyone’s talked about.

What is a Completing Strategy?

A completion strategy involves adding assets to an existing portfolio that would complete the mix from a diversification perspective, Bjornson explained.

Some clients are adding an additional tier of passive options, Gosselin stated, since they’re much cheaper than active funds.

Looking at how many RFP’s his team has responded to this year, Bjornson said they’ve received requests for the following asset classes:

- High Yield - 3%
- Emerging Markets - 8%
- Global - 10%
- Real Estate - 20%

Some of these choices clearly need limits on the percentage of assets that plan participants can invest. However, none of their plan sponsors do this.

One reason that plan sponsors are avoiding placing limits on amounts that participants can invest is that they don’t want to add another fiduciary responsibility to their list. Some are even walking away from setting any kind of asset allocations.

Congress Considers Index Annuities Regulation

Members of the House of Representatives have introduced a bill that would quash efforts by the SEC to claim jurisdiction over indexed annuities. The bill, H.R. 2733, exempts indexed annuities and indexed insurance policies from SEC regulation.

The bill has been referred to the House Financial Services Committee by its sponsors, Reps. Greg Meeks, D-N.Y., & Tom Price, R-Ga.,

SEC officials have argued for years that indexed annuities should be regulated as securities because they behave like other products they regulate. Critics of the SEC counter that subjecting annuities to dual state-federal regulation would harm the insurance industry, reduce competition and restrict consumer choice.

Late last year the SEC adopted its Rule 151A, which proposed reclassifying state-regulated indexed annuities as securities. Since 1995, when indexed annuities were introduced, their regulation had been the sole jurisdiction of the states.

The proposed law would specifically nullify Rule 151A.

For more information see: <http://thomas.loc.gov/cgi-bin/bdquery/z?d107:H.R.2733>:

How can mid- and small-market plans compete against ETFs and other investments with low expense ratios?

We just went through a tremendous period when the returns on passive funds beat those of active funds, Gosselin observed. He believes a big reason for this was because high-quality active managers didn’t want to take on the debt that a lot of these lower-quality companies had. They were right, but it just took too long to get there.

Passive has a place depending on the plan sponsor’s appetite for risk and the participant’s demand, he added.

Passive is one of those things that you’re likely to see, particularly in Large Cap Core, since it’s a way to provide a low-cost option, Bjornson said.

Is the 7% of plans that have passive target date funds a low or high figure?

We have a higher percentage in passive target date when compared to JP Morgan or Fidelity because we’re open architecture, Gosselin said. A lot of plan sponsors are doing this because they believe that their participants can meet their retirement goals by just using asset allocation. They also believe passive is a safer alternative to avoid underperformance. ♦

For more information on the FRC Investment-Only Defined Contribution research study see: <http://www.frcnet.com/pdfs/2009-FRC-IODC.pdf>

Consumer Focus

Initiatives in Retail Retirement

The speaker was Mark Jamison, Head of Core Client Experience, Retirement and Acquisition, Charles Schwab.

A Call to Action

Schwab commissioned an independent study of the consumer mindset that found that 1 in 4 retail investors is looking to switch their firm in the next 12 months. This is a call to action that says as an industry, we’re not engaging consumers in the right way.

Schwab considered the question, “What is it that the industry is delivering?” Based on the marketing messages of the top retail brokers, the industry is selling a mythology that can’t be matched by reality. This mismatch is what’s driving client’s desire to switch.

Six Key Points

1. Don’t get too fancy. Focus on basic blocking and tackling. Being able to answer simple consumer questions such as “How does the government know when I’m going to retire?”
2. Don’t discount optimism. Consumers have an incredible amount of optimism and often discover new career opportunities or figure out creative ways to save for retirement.
3. Recognize that retirement is an emotional topic. Their decision-making is driven by their emotional state. They can’t be thoughtful or logical about their decisions. McKinsey recently released a Retirement Perspectives Report that

said consumers are frightened and unsure what to do. If that's the case, then they're not in a rational mental state. One of Schwab's clients with over \$14 mil said, "I know it's irrational, but my biggest fear is that I'm going to end up broke and living in a cardboard box." Clients with these type of fears have a lot of anxiety about retirement.

4. Anxiety is caused when consumers don't know where they stand. People fall into two camps; those who are on track for retirement and those who aren't. However, both groups actually have huge amounts of anxiety that can be reduced by just validating their situation. If a client is underfunded for retirement, don't overwhelm him by saying "You're \$1 mil short." Instead, focus on the monthly increase needed to catch up. Also, reminding him that you've successfully helped other clients in the same situation can be very re-assuring.

"I know it's irrational, but my biggest fear is that I'm going to end up broke and living in a cardboard box."

-- Schwab retail investor with \$14 mm in assets

5. Virtue of Listening. Schwab's CEO is often quoted as saying, "I never learned anything while talking." Active listening is a part of Schwab's advisor training to help establish an empathetic connection. Clients don't typically call and ask to discuss retirement options. Advisors need to listen for key phrases that indicate a client is thinking about retirement and then be ready to offer ways to help.

6. Always pair problems with solutions. ♦

Is your firm struggling with operational inefficiencies?
Are technology issues reducing your ability to service your clients?

Ezra Group can help!

Risk & the New Product Landscape Adapting Products to Meet New Needs

The speaker was Maurice Leger, SVP, Director of Research, FRC.

March FRC Survey Results

The average equity fund allocation in 2010 Target Date Funds decreased by only 2% from the end of 2007 to March 2009. There are a few reasons for this low number. Most providers think of target date funds more as "target death" funds. The client will retire on the target date and then live 20-30 years before they die. So, a larger equity allocation is needed to handle the longevity risk.

Funds also have to consider the risk of underperforming their peers if they were to de-leverage now and then equities were to rally.

15% of target date net flows in DC plans are investment-only. This is up from 8% in just one year.

Surprisingly, active funds have gained market share versus passive in 2009. For the past ten years, active has been gaining market share versus passive. Active funds didn't perform particularly well in the downturn relative to indices. People are more conscious of low fees, which should favor passive.

What happened in 2009? The answer is that money shifted to fixed income and active managers have more share there. Advisors believe that active managers can add value through things like security selection and sector rotation. Fixed income managers, such as PIMCO and BlackRock, have actually come out stronger from the downturn. You can't say the same for equity managers.

Panel Discussion

The panelists were Stephen Deschenes, SVP, General Manager, Sun Life Financial Annuities, Jamie Cornell, SVP, Chief Marketing Officer, Prudential Retirement and Bruce Wolfe, Managing Director, Head of Special Projects, Allianz Global Investors.

How are you looking at things differently now?

Jamie Cornell -- Transparency is here to stay and will have a dramatic impact on both our retail and

institutional businesses. The voluntary DC system hasn't produced the outcome that we needed, so we think coverage could be mandated by Washington. There's a willingness now to pay for risk.

Bruce Wolfe -- We see the crisis as a godsend since it has highlighted the inefficiencies and inadequacies associated with the retirement space. In the long run, it's a good thing for all of us and for the industry as a whole. It also helps to level the playing field.

Our retirement framework has three layers; security, liquidity and capital appreciation. It encompasses insurance and asset management products.

Packaging is the biggest issue we have, more than product or distribution models. You must be able to define packaging consistently including branding, communications, and marketing. There also needs to be a fundamental shift in planning towards helping advisors handle decumulation.

Stephen Deschenes -- What has changed over the past twelve months? 1) the price of risk has gone up. 2) retirement preparedness is down. 3) the capacity to offer guarantees is lower due to insurance companies exiting the market for strategic reason or because they lack sufficient capital to deploy against those risks.

What hasn't changed? 1) Demographics. There will always be people that will need to generate income from their assets. 2) The role of advisors has become even more critical due to the breadth and complexity of new products on the market. There's more of a burden on them to synthesize and translate for the individual. 3) The underlying need for lifetime guarantees has gone up. Combined with reduced capacity, this should begin to increase prices. 4) IRA rollovers and 401(k) plans will still drive the vast majority of asset creation. 5) The key retirement risks of longevity, healthcare, inflation, and market risks will all continue to create a need for a more holistic retirement planning process.

For more information on the FRC Investment-Only Defined Contribution research study see: <http://www.frcnet.com/pdfs/2009-FRC-IODC.pdf>



Where do you think target date funds are going?

Stephen Deschenes -- They were designed to get to the retirement date, but didn't have the proper mechanisms to get through the next 25-30 years. They need to be adjusted to handle longevity risk.

Particularly in this context you begin to think about the opportunity to use asset liability modeling. When you're trying to defuse a future liability, once you've achieved your goal, the asset allocation should be changed to move stuff off to the side. This will facilitate building foundational income strategies that will be there no matter what.

You will see the integration of new asset classes such as absolute return and commodities as well as insurance guarantees both within the product and wrapping around.

How will providers react to potential regulatory changes?

Bruce Wolfe -- We all think the government is going to come at us with lots of mandates, but I think we're fooling ourselves. What the government has tried to do in the past is to look out for the consumer and increase transparency. They're not in the mandating business. We believe the changes that are going to occur will be mainly industry-driven, which will be a much slower process.

What is the role of guaranteed products in DC plans?

Jamie Cornell -- As Jeff Carney said, "if you focus on the customer need, you'll be a winner in the end." Participants have a fundamental need to manage risk. There's a huge industry retooling needed to properly handle decumulation.

I had a meeting with one of the largest recordkeepers who said they don't have the ability to do decumulation and they don't have the methodology to factor in guarantees into advice and guidance tools. Those are enormous challenges.

For some reason, Prudential can't get a plan beyond a 18-19% adoption rate. What could be qualified default

products. Today, we offer two of them. The first is GoalMaker, which is a custom target date fund that wraps with a plan's existing investment lineup. This product has \$10 bil in assets and ranks as the fifth largest target date fund in the U.S.

We recently rolled out IncomeFlex, which is a qualified default target date fund with income that begins accruing automatically. It's an enhanced index for which we charge 40 bps. We also have a guaranteed income wrap for 100 bps. Mercer has put this on their platform, although we did pay them a fee plus the cost of the build.

We're not seeing a big shift from current qualified defaults. The fiduciary standard is to review your current provider every three years. We think in 2009 - 2010 you're going to see more plans going out to bid and these companies will be looking at the next generation of qualified default products.

What types of alliances will we see among providers to deliver holistic retirement solutions?

Stephen Deschenes -- A partnership already exists within VA's since they have a wrap with an insurance-protection vehicle and underneath there's mutual funds and sub-advised structures that are typically outsourced to asset managers. What we're going to see is an extension of this into different product categories and different disciplines.

Is the VA business dead, wounded or stronger than before?

Bruce Wolfe -- The short answer is wounded, which is an improvement from a month ago when I thought it was dead. Up until the crisis, new product supply exceeded demand. Existing VA customers reaped the benefits by upgrading during the "arms race". One of the challenges now is how to expand the customer base? Demand has gone up dramatically, but can we supply products that are attractive and strike the right balance in the current low interest rate environment? That's the question. ♦

EZRA GROUP'S PROFESSIONAL SERVICES FOR THE SECURITIES INDUSTRY

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EZRA GROUP LLC

Craig Iskowitz
Managing Director
(732) 257-5735
craig@ezragroup.net