Please note: This is a transcription so there may be slight grammatical errors.

Hello and welcome to Revamping Retirement, a podcast brought to you by CAPTRUST, where we explore the opportunities and challenges facing today's retirement plan sponsors and fiduciaries. Our hosts, Jennifer Doss and Scott Matheson, lead CAPTRUST, one of the largest registered investment advisors in the U.S. and a thought leader in the retirement plan advisory and consulting space. We hope you enjoy Revamping Retirement.

Jennifer Doss:

Hello and welcome to another episode of Revamping Retirement. Scott is on vacation. Yes, again. So Dawn McPherson is my co-host again today, so welcome back, Dawn. We are going to spend a few minutes, Dawn and I, just recapping today what's happened in the DC industry the first half of the year, and then we're going to transition to get to the good part. We're going to get a mid-year market update from our colleague Kevin Fieldman. So let's dive in, Dawn, if you're ready.

Dawn McPherson:

I'm ready.

Jennifer Doss:

All right. I do feel like all that I've talked about at least this year is SECURE 2.0 Act. Both our first and second episodes of the podcast this year, actually, were dedicated to talking about SECURE Act, and I did some Google trend searching, 'cause I was wondering if I was maybe alone, if this was coming up for everybody else. And it looks like, unsurprisingly, the search activity for SECURE 2.0 Act content really peaked at the end of December, early January, and then by February it was about half as popular as a search term. And at this point it's about a quarter of its highest popularity, which feels about right. We're going to talk about SECURE Act for about 25 percent of the podcast. I think that's fair.

Dawn McPherson:

It does feel like that's all people in roles like ours are talking about. I'm embarrassed to admit, Jennifer, but I've actually had a few dreams about SECURE 2.0 Act. Not cool.

Jennifer Doss:

We can talk about that off the podcast, Dawn.

Dawn McPherson:

Fair, but your Google trend data does feel pretty right. If we think about the influx of questions we got when it first passed—and then it faded, as plan sponsors realized that there wasn't a lot that they had to do today and that the provisions strung out through the next 10 years. But we have seen a steady smaller stream and more focused SECURE questions, for sure, from plan sponsors.

Jennifer Doss:

Let's talk about the recordkeepers, actually, for a second, because that second episode that I talked about—I know everybody remembers, but we talked to Janet Luxton, senior ERISA consultant at Vanguard, whose life was really about to become just about this piece of legislation. And the general sentiment that I remember we got from her was that these provisions are really going to take a massive amount of money and programming and operational focus from these companies, and they really still

needed a lot of guidance too before they were even ready to get started and invest a ton of capital into those initiatives. I think, in the last couple of months, specifically, you and I have been part of some conversations.

We've heard a little bit more pointed [commentary] around the implementation of couple of things. So catch-ups as Roth, that mandate; just adding Roth to plans that don't have it, probably related to catch-ups as Roth; and student loan matching. Funny enough, and I know that a lot of the recordkeepers have already tackled the RMD updates earlier this year, so that's behind us. That one was pretty straightforward. Is that consistent with what you've been hearing?

Dawn McPherson:

Yes, I think that's right. Recordkeepers are starting to move forward on a few of these for the catch-ups as Roth, and adding Roth. They don't really have a lot of options, since they become effective 1/1 of 2024. So they're starting to send out communications, asking sponsors to affirm their intent to amend the plan to accommodate those new provisions. And in many cases, we're seeing deadlines for that affirmation being in July or August.

Jennifer Doss:

And the student loan matching one is just a funny one to lump in with those other ones, because it's optional and those are mandatory. You're being forced, to your point, to get it figured out before 1/1/24. So this student loan matching, I know it becomes effective 1/1/24, but again, it's optional. I think it was for some of these recordkeepers. It sounds like it was either focus on student loan debt or focus on emergency savings at this point. And to be fair, I feel like the emergency savings provisions are significantly more complicated to administer, and I think it's also easier to partner with a third party to do some of the heavy lifting for tracking and reporting the student loan matching, versus maybe programming everything in-house. So that's probably leading to some of that focus.

Dawn McPherson:

I would say you're right. It's most likely just the ease to market, and also timely, since student loan payments are set to start back in the fall. That's going to impact a lot of people, and I think it's going to make it tough for certain folks to save for retirement at the same time they're paying back their student loan debt. I feel like a lot of SECURE 2.0 interest surveys that I've seen are indicating that emergency savings is ranking higher than student loan. The interest for emergency savings is ranking higher than student loan matching. But to your point, a lot of recordkeepers seem uninterested in at least one of the emergency savings provisions. Do you get that sense?

Jennifer Doss:

I do. And the student loan payments starting back up in the fall is a really good point. I think some recordkeepers have even told us that they don't even intend to bill some of the emergency savings provisions. Either the emergency savings withdrawal, the thousand dollars, or it's the pension-linked emergency savings account. Some of them have had very strong feelings about one or both of those. I think in neither case do really any of the recordkeepers, though, seem to be in a rush to be first to market with the emergency savings provision, specifically.

Dawn McPherson:

You're right. It sounds to me like recordkeepers, or at least some of the recordkeepers, have spent some time and effort partnering with third parties to provide outside-the-plan emergency savings solutions,

and they just might not be convinced that either one of these in-plan solutions are going to move the needle much. It could also be that they just have far too many things on their plate right now.

Jennifer Doss:

There is a lot. There's about 93 things on their plate. No, I'm just kidding. That's a overestimation. Not all 93 are going to impact them, but it's a lot. Speaking of too many things on the plate, I do want to transition into another topic that I've been hearing a lot about the first half of the year. And that is small business retirement plans. And when I say that, I really don't mean just start-up plans. I think people equate those two. It doesn't have to be a start-up plan; it could just be a small business, and really, that's defined as talking about anything with less than a hundred employees. There's a big focus right now from Congress, from state government and our retirement industry, to really close that retirement coverage gap in America. So again, that leads us to talking about start-up plans sometimes, but I also think that this has bled into how can we better service some of the small business plans that are in existence today? How can we make sure that they have the best service possible?

Dawn McPherson:

I think we have a lot of complementary approaches happening all at the same time. We have the state-run auto IRA programs in 19 states. That's where small businesses have to enroll their workers in a state-managed IRA program. We also have new tax incentives with SECURE 2.0 that make starting a retirement plan very affordable for business owners. And we even have a new employee deferral-only starter 401(k) plan option that was created with the legislation.

Jennifer Doss:

And, I think, more where I was going too is we have pulled employer plans and we have [a] group of plan arrangements, which are actually a byproduct of the first Secure Act in 2019. But those arrangements, even though they haven't taken off, I would say, quite like the industry thought that they would, I think that they've done a few things for small plans that are really beneficial. First, they brought a focus from the retirement industry in really to how we could service or offer more services to these small businesses and plans. Advisory firms or recordkeepers, I mean us alike, we really had to sit down and figure out how we could service a market that maybe you'd avoided before because it maybe wasn't as profitable as some of the mid- and large-size plans. And no, small plans have not all of a sudden gotten more money and become more profitable from the top line.

But it's really about increasing that service scale and really thinking how you can do it smarter. That has contributed to a larger bottom line for some of those folks I just mentioned. And second, the thing I think gets done is those aggregate arrangements, they really created a lot of options for small businesses and plans to offload a lot of fiduciary responsibility that they just may not be equipped to handle, really allowing them in a cost-efficient way too. I think that's always the case, that there were always these options available, maybe they were cost prohibitive. And now it really allows them to focus more time on running their business versus the retirement plan, which is what a lot of these small businesses really want. And I think prior to Secure Act 1.0, we really didn't talk about. We talked about 3(38) investment management, that fiduciary offloading, we didn't really talk about—or at least I didn't hear a lot of discussion about—discretionary 316 administrators. And now I actually have a lot of conversations about that role.

Dawn McPherson:

I completely agree with you. There's so many more employers that are interested in fully bundled solutions—that includes 316 administrators, 3(38) investment managers, and payroll integrations—certainly more than we ever heard even three years ago. There's just so much going on right now that small plans and businesses have to navigate. And you think about the SECURE 2.0 items we talked about at the beginning, how do you navigate all of those without the resources and expertise in-house? I think that's a great segue to talking about the markets with Kevin, as those have been pretty challenging to navigate as well.

Jennifer Doss:

I don't know what you're talking about.

Dawn McPherson:

Let's take a quick break for our Minute with Mike, where Mike is going to continue covering SECURE 2.0 with an enhanced tax credit for small businesses that decide to start a retirement plan. Take it away, Mike.

Mike Webb:

This month we'll continue covering SECURE 2.0 Act with an enhanced tax credit for small businesses that decide to start a retirement plan. It was previously an existing tax credit in the first Secure Act—but it was quite modest—that did not incentivize many small businesses to start a retirement plan. The new two-part tax credit should greatly increase the likelihood that small employers that do not already have one will indeed sponsor a retirement plan. Now the first credit, also part of the original Secure Act, is a credit for startup costs. The credit was 50 percent of such costs up to $5,000, but was increased in SECURE 2.0 to 100 percent of costs for employers with up to 50 employees. The credit can be taken in the first three tax years of the plan's existence. The brand-new second credit is available for the first five years of the new plan, and it applies to employers with up to 50 employees and is phased out for employers with between 51 and 100 employees.

The credit is an applicable percentage of employee contributions made to the plan, up to $1,000 per employee earning wages of $100,000 or less. In the first two tax years of plan existence, this percentage is 100 percent, meaning the full credit of $1,000 can be taken if the employer contributes $1,000. In subsequent years, that percentage will decline to 75 percent in year three, 50 percent in year four, and 25 percent in year five. Employers cannot take a deduction and a tax credit for the same amounts, and tax-exempt employers are not eligible at all for this provision. A small business is also not eligible for the credit if it benefited from any retirement plan for the three years prior to the date the new retirement plan is established.

Dawn McPherson:

Thanks, Mike, and welcome back, loyal listeners—or Scott's mom? Jennifer, do you think Scott's mom listens when he is not co-hosting?

Jennifer Doss:

Yeah, her and I text all the time, so she's a big fan. Sometimes when he's not on here. I didn't want to tell him that, but now it's out of the bag. You made this awkward.

Dawn McPherson:

Well, I'm sorry to take that away from you. As mentioned, we have our colleague and market guru, Kevin Fieldman, here with us to get a mid-year market update. Welcome, Kevin.

Kevin Fieldman:

Hello Dawn and Jennifer. Glad to be here.

Dawn McPherson:

Kevin, the market's in a really different place than most people thought it might be. At the beginning of the year it was all about the pending recession, and then we had the regional banking issues, which shocked the market. Why has the market defied the odds and been so resilient?

Kevin Fieldman:

That's a great question. I think there's four things that we've gone through in the first half, and really it's somewhat of a continuation of the fourth quarter of 2022. Even though we had such a negative year in 2022, we had a positive quarter in the fourth quarter. So the first one is inflation ease. So the easing inflation, inflation peaked just a year ago in June of 2022. It came down the second half of last year. September of last year was the big moment when we had a bigger decline that anticipated. The market rallied from that, and that's continued with the anticipation that we're now in a disinflationary environment. And what that's really led to is the feeling that the Fed was going to slow down its rate of interest rate hikes, which we've seen so far this year.

And that, actually, coming into the year, they were actually pricing in—that we would see the Fed start to cut rates in the second half of this year. We probably don't see that. The markets priced some of that out. But that was really a big driver in the first half of the year. And then the other big thing that's happened is corporate earnings have really held up better than anticipated. People really thought we were going to see a big downturn in corporate earnings this year. We haven't seen that. We've seen that they're slower, but they're not anywhere near the levels that people thought coming into this year. So that's helped the market, and then really the promise of AI has been a big one. If you look at in May when Nvidia reported their earnings, really around the future guidance based on the number of chips they'd have to create for AI-type projects, that really changed the market as well.

The other thing about the market is, up until, really, that Nvidia announcement, it was really a very narrow market. So it was really seven stocks. We call it the magnificent seven. So the big ones, everyone knows Apple, Microsoft, Alphabet, Amazon, Meta, Tesla, and Nvidia. That really drove the market. But we have seen in the last six weeks or so a little bit more broader rally in the market as well. So that's a positive, but I think it's really the pace of inflation and really the feeling that the Fed was just about done or almost done with rate cuts, has been the biggest driver in terms of the turnaround.

Jennifer Doss:

Yeah, I think we've all been a little bit surprised about how resilient the consumer has been too. We're a consumer-driven economy, and I love that this soft landing is now part of our everyday vernacular. My grandmother was asking me the other day, "What is a soft landing?" And I was like, "I just love this." So Kevin, let's focus on inflation more a bit for a minute, because I think that's what's been in the headlines so much, and that's the number one thing you mentioned. Inflation is a really complicated measure and it includes a lot of different things. It's housing, it's energy, it's food, it's furniture. Can you help us clarify, maybe, what measure of inflation the Federal Reserve is most focused on, and how that measure, maybe specifically, is doing relative to their mandate? You mentioned that we're deflationary

at this point, but second question would be what is still driving inflation? Because we still have some, but what is still driving that?

Kevin Fieldman:

OK, yeah, that's great. What most people think of inflation, they think of CPI, which is the Consumer Price Index. That's what gets reported in the media, that's what most people think about. That's what was reported last week at 3 percent year over year for the month of June. But what the Fed uses is a different rate called the personal consumption expenditures or PCE. So they're two different measurements. The first one, CPI, is actually calculated by doing consumer surveys. So it's by the Bureau of Labor Statistics. They do consumer surveys to get information on prices and how much people are paying for stuff. The PCE is actually a business survey. So they survey businesses to get reactions on how much is being sold and what is being sold for and so forth. And there's really two reasons that the Fed prefers the PCE.

The first one is that it is business surveys, and they tend to be a little bit more reliable than consumer surveys. The other two is in the calculation of the PCE, they have the ability to calculate the difference of people's spending habits because of inflation. So for example, if the price of beef is up and people start buying more chicken, that change in behavior gets reflected in the PCE. It doesn't get reflected in the CPI. It's just the price of beef going up. So if something's going up and it's causing consumers to buy less of it or buy an alternative, that's factored into the PCE. So that, right now, that hasn't been released for June. I think that gets released on Friday, but the last month, the May one, was about 4.7 percent if I remember correctly.

And the Fed mandate is 2 percent. So we're still well above the Fed mandate, and I think that's where some of what's happening after the June CPI report where people are saying, "Oh, we're on the downside of inflation"—we still have a long way to go. And the biggest thing really driving inflation now is services inflation. We've seen a clear slowdown in goods inflation, so we're seeing supply issues that we had coming out of lockdowns have been resolved. We've seen shipping costs come down. I just saw a report today that shipping costs are actually back to pre-pandemic levels. We don't have some of the supply chain concerns we had before, but really a lot of this is in services. So things like airlines, hotels, restaurants, medical care, those types of things. And we've really seen consumers rotate from really a goods-driven economy, which we had during the lockdown with all the stimulus, to more of a services spending.

And the biggest factor in a lot of that services inflation is labor. Jerome Powell, if you hear him talk, he talks a lot about a measurement he looks at, which is core services minus housing, and that's really looking at those types of services we talked about, and really get an idea of seeing that inflation come down. That's been the stickiest part of inflation, and that's why the labor market is so important in terms of what the Fed's looking to do. Labor market is extremely tight. Wage growth is about 4.5 percent year over year, which is great for employees, but it's not good for a Fed that's trying to fight inflation. So that's why we'll probably see another rate increase next week at their next meeting. And I think they'll still leave a bias to be able to raise higher at some point this year. We'll talk about that a little bit more.

And that's really what's driving inflation, is services. And it's hard to get inflation down when people are employed. When we have 3.6 percent unemployment, it's hard to get inflation down, because if people are employed, they're making money. If they're making money, they're spending it, and that's creating increasing demand, which makes the Fed's job harder in terms of bringing that inflation down to their 2 percent target.

Dawn McPherson:

That's great information, Kevin. I started to think, when you first start talking, and I think Jennifer mentioned AI, I was just wondering if you think you talk about AI as much as we talk about SECURE 2.0.

Kevin Fieldman:

It's amazing, and I should have had the fact—somebody reported the number of companies that discussed AI in their earnings reports for the first quarter. And it's companies like Kroger and retail shops and consumer goods shops and so forth, and talking about how AI's going to benefit their businesses. It was like 60 percent of businesses had a mention of AI in their conference call after earnings.

Dawn McPherson:

That's incredible. Okay, let's tie this back to DC plans. Most of the assets are now invested in a pre-diversified portfolio, like a target date series. How are those funds faring in this market environment?

Kevin Fieldman:

They're faring much better. Last year was a really tough year for [inaudible 00:21:28], because diversification just didn't work, and the stock market was down double digits. The bond market was down double digits. The first time we saw that in over 50 years. So that was tough. We've seen that rebound. We've talked, the equity market has been up, the bond market's been up slightly, though not as robust as the equity market. So a lot of those people are starting to see some nice rebounds. I looked at TDF, just looking at the range from the income, and most conservative funds to the longer state funds, and the range in the first half of the year was the low end 2.5 percent on an income fund, to up to 16 percent out of a long-dated fund, a 2065, 2070 fund.

And just to give you an idea of the average target date return for three key indices. So for a 2025 fund, for those of your employees who are close to retirement or thinking about retirement, the average return was about 8.5 percent. For the 2045 fund, so your mid-career people looking about 20 years to retirement, average fund was about 13.75 percent, and for your 2065, your new employees who just started, those funds averaged 14.6 percent. So we're seeing a nice bounce back. We've had a positive market here so far in the third quarter as well. So people who stayed the course and stuck with the right target date fund are seeing some nice improvements after a tough year last year.

Dawn McPherson:

That certainly is good news. I know it's tough, but what are your best thoughts on what we expect to see for the rest of 2023? What's your crystal ball telling you?

Kevin Fieldman:

That's the million-dollar question. I wish I could tell you what the market's going to do the rest of the year. I can tell you the things that we're really focused on in terms of making determination from an investment standpoint, that will have probably the biggest impact on what both the economy and the market do in the second half of 2024. First is going to be inflation and the slope of inflation. Do we continue to have inflation slope downward? Do we get closer and closer to that 2 percent that we had with the CPI report, or is inflation going to continue to be sticky? We see a plateau at this 3 to 4.5 percent inflationary environment for a while, which is going to make the Fed's job more difficult. And then the Fed. It's almost universally agreed upon, they're going to raise rates about 25 basis points. And so then the big question is going to be, are they going to raise again at any other point in 2023?

So there’s no meeting in August. When September comes around, they’ll have two more months of data before their September meeting. So that’ll be big to see what the data tells us in that time frame, to get a read of if the Fed’s going to continue to raise. Coming into the June CPI report, the market anticipated two increases this year, July and September. July is still in play. September, it’s backed down a little under 50 percent from a market standpoint, but it’s going to be really driven by a lot of the data we get for the rest of the summer that the Fed will have before that September meeting. The labor market is going to be something to watch. Will employment start to loosen? Do we start to see unemployment rise? As I said, it’s hard to see recession when unemployment is this low, but at the same time it makes the job difficult in terms of trying to get inflation down to that 2 percent range. So we’ll be watching that real closely.

And then corporate earnings, do we continue to see this more positive corporate earnings environment than we anticipated coming in this year? We’ve had a couple. The banks outside of Goldman Sachs so far have reported for the second quarter and have done really well. So we’ll continue to watch that to see corporate earnings, and then I think, just like a normal quarter, we’ll see some volatility. I think we’ll see some movements in the market, based on what the numbers from some of these tracks come out to play. Fed communication after the meeting next week will play a big role.

So I think we’ll see some volatility throughout the quarter, but again, it’s going to get back to that soft landing. If we get that soft landing, and it looks like Fed was able to pull that off, we could have another robust quarter. If it looks like we start drifting toward recession as we head into 2024, then we could see some pullback in the marketplace. So unfortunately, it’s still a lot of unknown. We’ve gotten some clarity, but still a lot of unknowns in terms of what could happen in the market and the economy the rest of this year.

Dawn McPherson:

I think that’s still helpful to give us some things to keep an eye on. So you’re saying, us asking you to predict what’s going to happen in the markets for the rest of 2023 is like people asking us when the technical corrections or additional guidance will be available for SECURE?

Kevin Fieldman:

Absolutely.

Dawn McPherson:

All right. Last question, and we ask all our guests this at the end of the podcast. What does retirement look like for you, Kevin?

Kevin Fieldman:

That’s a great question. I’m at the point in my career where I’ve always said the retirement’s moving further and further up my brain. When you’re younger it’s at the back of your mind. You know it’s going to get there, but now it’s getting closer. So when I think about it, I don’t think of an age. I’m not a person who says, “I’m going to retire at 62 or 65.” When I look at it, I look at a number and I say, “This is the minimum number I need my retirement and investment accounts to be worth before I could even think about retiring.” So I have a minimum and then a goal. Once I get to that point, at that point then I will start doing a year-by-year consideration and thinking of all the things people think of, job and health and the family and so forth.

When I finally get there, I think I’m going to do what a lot of people say, I want to play some golf, I want to do a little bit of traveling. Depending on where my family and my kids are, hopefully spend a lot of

time with family and so forth. I don't think I'm the type of person who could just sit around and do nothing. I'll have to do something, either volunteer or maybe do some part-time something or consulting or so forth. I have to keep myself busy and keep my brain active. I think unfortunately our country is still focused on age-based retirement, which is back from pensions, because 65, you got your full pension, so you could walk out the door and you knew you're going to be getting paychecks for the rest of your life. If you're not in a position financially, 65 means nothing from a retirement standpoint. It's really being able to have that nest egg in place to be able to support your lifestyle for the rest of your life.

Jennifer Doss:

That's fair. Like you said, I know there's a lot of people out there, I think Mike Webb included, actually, who hate the term *retirement.* It's more about financial independence, and that's really what people mean when they say that. They want the ability to be able to do the things they want to do without worrying about cost and money, and like you said, health concerns and things like that. So that's great. All right. Well, thank you, Kevin. Thanks for joining us today and for providing an update, however unfair our questions were. And Dawn, thank you for not leaving me alone, since Scott abandoned me, and audience, thank you again for tuning into another episode of Revamping Retirement. Don't forget to like and subscribe wherever you get your podcasts, and we will see you all next time. Thanks, everyone.

Speaker 1:

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