Active or passive management in defined contribution plans?

It doesn't have to be either/or[1]

Defined contribution plan sponsors are wondering which makes best sense for their plans – active management, or passive. In the absence of certainty, many are expressing a strong preference for the lower fees associated with passive management.

We'll explore four points we believe are worth considering in the very important active/passive decision:

1. **Passive may not be the safe fiduciary option.**

   Implication: Do not automatically dismiss attractive active management opportunities.

2. **Active management is worth considering.**

   Implication: Carefully consider the alternatives to passive on a case-by-case basis.

3. **Cap-weighted is not the only way to invest passively.**

   Implication: Choosing the flavor of passive is an "active" decision.

4. **There's no "passive" option for target date funds.**

   Implication: Understand your plan's target date offering, and monitor and periodically reconfirm its appropriateness.

1. Passive may not be the safe fiduciary option.

Some DC plan sponsors express the view that passive investing is safer than active because it lowers their fiduciary risk. Common arguments for this view invoke the typically lower fees of passive investing and never having to explain below-benchmark performance. Yet the ERISA "standard of care" that governs DC plans does not identify passive as the safe fiduciary option. Rather, it states that the fiduciary must act "solely in the interest of the participants and beneficiaries and

A. for the exclusive purpose of:

i. providing benefits to participants and their beneficiaries; and

ii. defraying reasonable expenses of administering the plan;

B. with the care, skill, prudence, and diligence…that a prudent man acting in a like capacity and familiar with such matters…would use…"[2]

The standard of care clause extends further, but this passage provides some key points. It emphasizes the need to make careful, informed decisions that are exclusively in the interests of plan participants, while keeping expenses at reasonable levels.

Let's address the perceived safety of passive management from the fiduciary's perspective, as summarized above. To begin, we must agree on what, exactly, is in the participants' interests. Participants have different reasons for investing in the plan, but "saving enough to retire" likely articulates a reasonable goal that most participants share. A "safe" investment, then, would help mitigate the risk of savings not meeting that retirement goal. Passive management, as a general criterion for selecting investment options, does not precisely address this risk. The typically low cost of passive management, taken in isolation, does support participants' efforts to meet the goal. Yet focusing overmuch on this particular aspect of passive investing and glossing over the other aspects – especially to the point of excluding non-passive options from consideration in the plan's fund lineup – can have unintended consequences.

- **Participants aren't assured safety simply because they're invested passively.** The market exposure of many passive funds means investors take on the full systematic risk of the market. As we've all been reminded over the past few years, that systematic risk can be very significant. It caused many participants invested via both active and passive strategies to delay or cancel their retirement. At a minimum, passive management is no panacea for managing participants' risks. So, plan sponsors need to dig deeper than "is it passive?" when considering what's best for participants.
- **Systematically excluding non-passive options from consideration can deprive participants of the sponsor's best thinking.** Referring back to ERISA's language on "reasonable expenses": in light of the directive to act in participants' sole interests, we believe an expense that furthers those interests can be reasonable. In the context of active vs. passive management, if the benefit to participants from choosing a non-passive option outweighs the opportunity costs,[3] it makes sense to select that option. This decision often hinges on the question "Do you believe alpha can beat active management fees?" On average, the answer will be no, as Bill Sharpe famously observed way back in 1991.[4] But in a specific case, a fiduciary acting in accordance with ERISA's "prudent man" standard, who is well versed in active manager selection and has undertaken extensive due diligence, can answer "yes." And in these specific cases, paying for active management can be reasonable. Fiduciaries need to imbed their best thinking in their DC plans. Dogmatically excluding an entire set of strategies from consideration inevitably deprives participants of that best thinking.

To summarize: mandating passive management *as a hard-and-fast rule* is not the safe fiduciary option.

…if the benefit to participants from choosing a non-passive option outweighs the opportunity costs, it makes sense to select that option.

A fiduciary needs to imbed their best thinking into their DC plan. Dogmatically excluding an entire set of strategies from consideration inevitably deprives participants of that best thinking.

SO, WHAT SHOULD A FIDUCIARY DO?

For fiduciaries who want to pursue the "safe" option, there's a better way forward than selecting all-low-cost passive options. PIMCO's 2012 Defined Contribution Consulting Support and Trends Survey asked 35 consultants about the best ways for sponsors to mitigate litigation risk, and the top three responses were "document investment policies and processes," "evaluate and confirm reasonable plan investment fees" and "establish an engaged DC investment oversight committee."[5] In fact, "move to low-cost passive strategies" ranked near the bottom of the list, with one third of consultants deeming it "not important."

Plan sponsors have a difficult job. On the one hand, they want to do the right things – for example, increase participation, boost contribution rates and increase diversification of investment options. On the other, they fear "getting into trouble" – whether the fear is of incurring liability or inviting the disapproval of colleagues.

Yet ultimately, a plan sponsor's loyalty is due to the plan participants. They rely on the sponsor, as the ERISA prudent expert, to provide them with a solution designed to be in their best interests. Sponsors need to diligently consider their available options, whether active or passive, and select what they believe are the best alternatives for their participants.

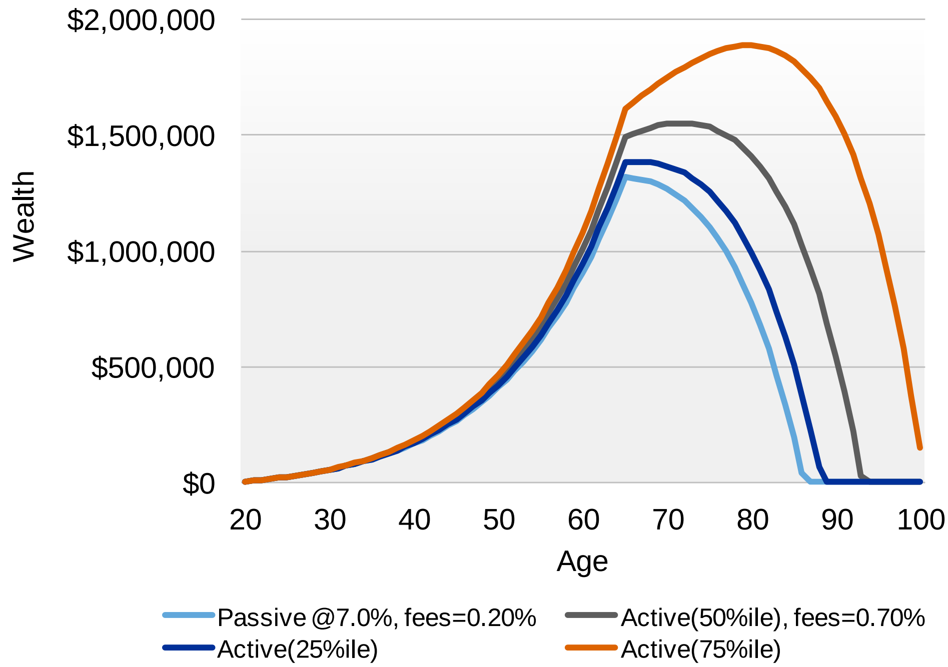
2. Active management is worth considering.

DC plan sponsors tend to be particularly sensitive to fee considerations, due to participant concerns, government policy and/or legal worries. Many plan sponsors who may believe in active management (as expressed, perhaps, in their defined benefit plan) feel pressure to reduce fees and active risk on the DC side. Yet, since active management pays off if benefits exceed costs, even a few extra basis points of return each year can make a meaningful difference in what participants have accrued at retirement and beyond.

Consider the chart below, which is a hypothetical analysis comparing wealth over time for a participant in a stylized plan who attains a 7% compounded passive return with 0.20% fees (blue) and another participant who attains the same passive return (gross of fees), but with alpha of 1.0%, tracking error of 3.0% and fees of 0.70%. The different colors represent the 25th-percentile outcome (green), 50th-percentile outcome (red) and 75th-percentile outcome (purple).

Even modest amounts of alpha generation can add years of retirement spending potential. 0.17% annual returns net of the passive fund return (the 25th percentile in Exhibit 2) can add two years of retirement spending, while 0.46% net (the 50th percentile) can add seven years of spending. From another perspective, the performance of the passive option provides retirement income equal to the 14th percentile outcome from active management.

Exhibit 1. Stylized evolution of wealth over time for DC plan participants



Source: Russell Investments. Other assumptions include an initial age of 20, initial salary of $30,000, 3% annual salary growth, a 10% savings rate and withdrawals beginning at age 66. The initial withdrawal is equal to 80% of final salary of $113,448, and subsequent withdrawals include a 3% annual cost-of-living adjustment. Tracking error of 3.0% is normally distributed. Annualized net of passive fund returns, including management fees, are as follows: 0.17% (25th percentile), 0.46% (50th percentile) and 0.74% (75th percentile).

This is a hypothetical analysis shown for illustrative purposes only.

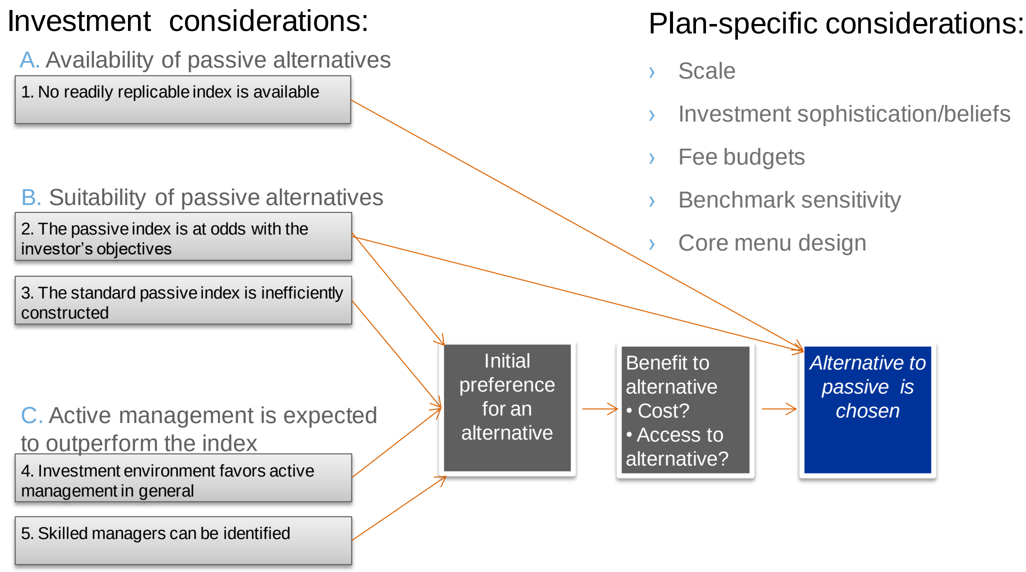
Plan sponsors should not take a dogmatic either/or position on active vs. passive. Fee pressures may make active management unattractive to many plan sponsors, and the easiest decision may be to go all-passive in every asset class. Yet given the potential benefits of active, it's worth exploring whether it can benefit participants in certain cases. While such exploration is not the easiest path to travel, it's the right one.

….it's worth exploring whether [active management] can benefit participants in certain cases. While such exploration is not the easiest path to travel, it's the right one.

SO, WHAT SHOULD A FIDUCIARY DO?

Rather than rely on a simple binary yes/no decision on active and passive, plan sponsors should have a pragmatic framework to help them decide where and when to go active. As the title of this paper denotes, the decision between active and passive can best benefit participants when it is not regarded as an either/or choice. Plan sponsors with fee budget or other constraints can certainly benefit their participants by mixing active and passive exposures. Russell has developed a decision-making framework for plan fiduciaries considering this issue, detailed in the diagram below.[6] In this framework, the fiduciary starts with passive as the default assumption and considers whether another approach may make sense.

Exhibit 2. Framework for choosing an alternative to passive investing



Our framework identifies five investment considerations. Typically, active management is the alternative to passive. Below, we'll provide an example for each of these considerations. Then we'll discuss plan-specific factors that can influence the decision.

1. **No readily replicable index is available.** This is certainly true of non-public asset classes, such as private real estate. Even though there are private real estate benchmarks, it would be impossible to replicate a benchmark's return, given the relative illiquidity of the market. This can also apply to more liquid asset classes to varying degrees.

2. **The passive index is at odds with the investor's objectives.** Plan sponsors have unique beliefs and objectives. For instance, a plan sponsor who wants to offer representative, diversified exposure to real assets may not be satisfied with implementing a passive fund based on one or more of the available benchmarks. In the listed infrastructure space, active managers often produce a more "pure play" exposure to infrastructure than the available passive benchmarks do.[7] Pure play listed infrastructure companies can be desirable, because they typically have more stable cash flows than typical public companies do. They operate in regulated industries with significant barriers to entry – industries that provide services essential to the functioning of a society (such as utilities, airports and cell phone towers).

3. **The standard passive index is inefficiently constructed.** For example, passive collateralized commodities futures (CCFs) indexes may face two major headwinds. First, there's no clear equivalent to the market-cap weighting often used in equity indexes, which can lead to construction of indexes that lack commodity exposure diversification. Production-weighted indexes, such as the S&P Goldman Sachs Commodity Index, will be highly concentrated in energy commodities.[8] In addition, rules-based approaches to rolling over expiring futures contracts can lead to undesirable exposure to short-term market trends. "Roll yield," or the return an investor earns in the process of rolling over an expiring futures contract, can have a significant negative or positive effect on the ultimate return from CCF investing. Active managers may be able to take account of these market dynamics to potentially benefit investors.

4. **Investment environment favors active management in general.** Russell's research shows that we can expect good active managers to perform better when returns of individual securities can be explained more by security-specific risks than by macroeconomic events. One way Russell interprets which sort of public equity return regime prevails is via cross-sectional volatility, or "cross vol." Cross vol measures the returns dispersion of a universe of securities – whether the returns are moving in lockstep (low cross vol) or diverging (high cross vol). Russell's research has found a strong positive relationship between cross vol and active manager dispersion – in other words, the payoff to good active management is higher when cross vol is higher.[9] Cross vol can be persistently high in a market, or high on a merely transitory basis. Small cap stocks have exemplified persistently high cross vol relative to large cap, which indicates a greater payoff to good active management in the small cap space.[10]
5. **Skilled managers can be identified.** It is difficult to identify skilled active managers, but the payoff can be quite significant. As discussed earlier, generating even a small amount of active return in excess of fees can enhance the chances of a palatable retirement for participants. Selecting a good manager requires not only rigorous quantitative analysis of the manager's performance record, but qualitative, ongoing judgment of the manager's abilities and resources. Plan sponsors who do not have the skills to evaluate managers or the resources to hire third-party manager research experts may be best served by limiting their plans' active management exposures.

Plan sponsors who do not have the skills to evaluate managers or the resources to hire third-party manager research experts may be best served by limiting their plans' active management exposures.

Plan-specific considerations matter just as much as the investment considerations described earlier. Let's examine the five considerations provided in Exhibit 2: scale, plan sponsor investment sophistication/beliefs, fee budgets, benchmark sensitivity, and core menu design.

- **Scale.** The plan sponsor's scale significantly impacts not only access to certain asset classes, but the fees charged for those options. The expense gap between active and passive fees varies depending on the asset class, as well as the vehicle (mutual fund, collective trust or separate account).
- **Plan sponsor investment sophistication/beliefs.** Let's assume a plan sponsor has decided to add an asset class exposure to the plan. Now, set to one side whether or not attractive active management opportunities exist in a given asset class. If, after performing objective due diligence, the sponsor cannot get comfortable with the notion of active management in a given asset class, then passive management should be chosen over the alternative of no exposure at all. One caveat to this conclusion is that it may not be possible to passively invest cheaply and efficiently in all asset classes.
- **Fee budgets.** Even when attractive opportunities for active management exist in all asset classes under consideration, fee budgets can constrain the use of active management to only the absolute best of the opportunities. In the context of a multi-asset-class option, such as a target date fund, if a plan sponsor has fee constraints, the decision to include or exclude an asset class can impact the budget available for other asset classes and, consequently, the active vs. passive decision in those asset classes. So, the focus should be on those areas with the greatest potential for net-of-fees alpha.
- **Benchmark sensitivity.** Benchmark sensitivity could discourage a plan sponsor from taking active risk in asset classes where good active managers' returns can deviate significantly from the benchmark. Taking multi-manager approaches, and

combining active and passive investment in a single fund, can help reduce tracking error relative to returns of a single active manager.

- **Core menu design.** Unique to DC plans, the design of the core menu intertwines with the active or passive decision. To offer participants a variety of choices, many plans offer both an active and a passive tier of fund options. In contrast, Russell believes a more streamlined menu design works best for most participants. Many, if not most, participants lack the skills and level of attention required to make sound investment decisions when faced with a large number of options. At best, offering separate active and passive tiers complicates their decision-making. At worst, it can lead to increased performance chasing among investment options. A strong core menu design can be the foundation of a well-designed plan. A simplified core menu could include one to three equity options, a fixed income option, a capital preservation option and a diversified real assets strategy. Within each of these options, the mix of active and passive approaches should reflect the sponsor's best thinking.

3. Cap-weighted is not the only way to invest passively.

Although the definition of passive management hasn't changed, a proliferation of innovative indexes and products has emerged in recent years. "Passive management" simply means investing in a rules-based manner. In practice, investors often add the additional criterion of "aims to replicate the returns of a specified benchmark index," and we'll include it for our purposes as well. The most popular application of passive management involves replicating the returns of a "market portfolio" via low-cost mechanical trading rules. Yet there are other ways to invest on the basis of a set of rules and an index. Today, investors can choose from a staggering array of options that fall on different points in the spectrum between traditional, capitalization-weighted passive investing and traditional active management. Let's examine several which may be relevant to DC plans:

- **Passive options tracking different slices of a cap-weighted index.** Examples include size, valuation and region-specific index-based products. While still passively managed, they can offer return patterns that significantly differ from each other. Even indexes designed to provide similar exposures can deliver different returns. Providers utilize different methodologies, which can lead to different weightings and numbers of issues in a benchmark.
- **Passive options tracking slices of an alternatively weighted index.** Any product based on a non-cap-weighted index falls into this category. One example of this approach is a fundamentally weighted index product, where securities are weighted on the basis of company fundamental measures of size (such as cash flow), as opposed to market capitalization. Even if implemented with the transparency and liquidity of cap-weighted passive products, these products may be considered active management by proponents of the capital asset pricing model.
- **"Enhanced indexing."** Enhanced indexing describes a broad category of strategies that attempt to produce modest returns above an index. While the funds deploying these strategies tend to exhibit much lower turnover than actively managed funds do and trade based on rules, returns can also differ significantly from those of their index benchmarks, since the strategies attempt to add value to the benchmark. It's difficult to classify them as either active or passive.

SO, WHAT SHOULD A FIDUCIARY DO?

It appears, then, that selecting a passively managed product may be an "active" decision unto itself. So, when considering passive options for a plan, a sponsor should consider looking beyond the traditional passive option of a cap-weighted index fund. A sponsor may have very good reasons for opting for an alternative. As an example, Russell's research has identified "the third dimension of style" – Stability – which focuses on the high-quality, low-volatility ("Defensive") stocks / low-quality, high-volatility ("Dynamic") stocks spectrum.[11] We see potential for the practical application of this research to give investors better management over their equity risk in a passive vehicle, which may appeal to DC plan sponsors and their participants.

Simply selecting any target date fund series does not fulfill fiduciary obligations.

4. There's no "passive" option for target date funds.

The selection of a target date fund (TDF) demands an "active" decision on the part of the plan sponsor. A TDF's glide path – the split between risky assets and relatively safe assets, such as fixed income, over time – will be the single most important factor in determining the return pattern of the fund.[12] However, unlike weights to securities within a single asset class, there is no default starting point for setting the glide path – particularly, for the pace and timing of the transition to a more conservative portfolio over time.[13] While the market capitalization-based approach to passive is very popular (in, for example, public equity portfolios), there's no well-established corollary for TDFs. Different plan sponsors desire different asset class "building blocks" for inclusion in a TDF, adding to the difficulty of determining a passive benchmark.

This need for an "active" decision ties back to our first major point: passive may not be the safe fiduciary option. Participants invested in a TDF will feel the difference between a 70% allocation to equity and a 40% allocation to equity, regardless of whether the underlying strategies are managed actively or passively. For many plan sponsors, the hard lesson of the 2008 stock market drop was that the selection of a TDF matters a great deal. In 2008, even TDFs with "2010" in their names (funds designed for participants nearing or already in retirement) showed significant variations in returns.[14]

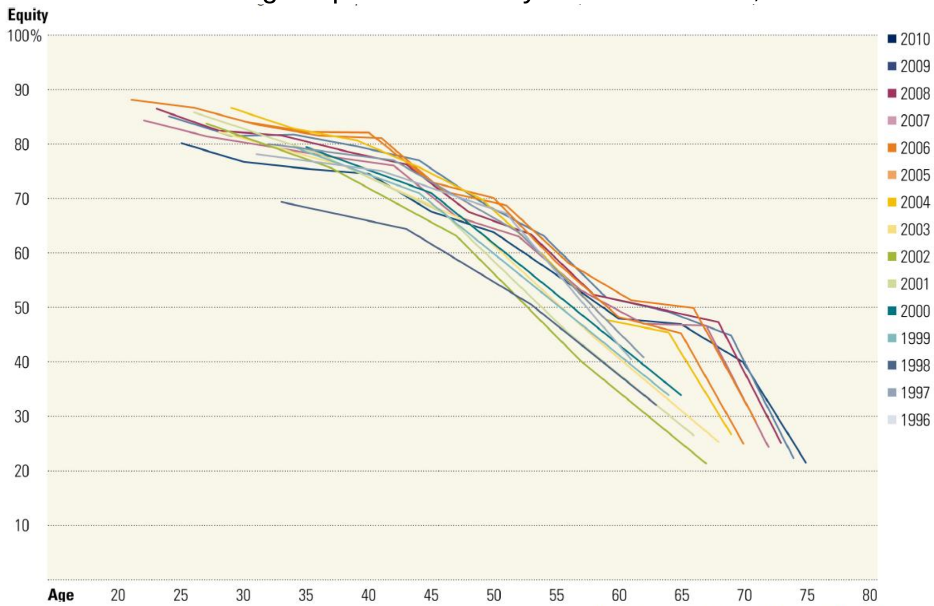
The regulators who oversee DC plans responded by holding a hearing on TDFs[15] and issuing guidance on them.[16] Some of the key points from the guidance are that investors need to:

- Monitor a TDF's investments over time;
- Look at the fund's prospectus to see where the fund will invest their money; and
- Understand how the investments will change over time.

Unfortunately, it is not clear that sponsors have embraced the recommendation to understand their plans' glide paths. A recent survey indicated that about half of plan sponsors did not know what their funds' glide path is – and yet 70% believed that their *participants* understood the structure and purpose of target date funds.[17] Although plan sponsors have safe harbor protections for use of TDFs as default investment vehicles, they still have a fiduciary duty to understand how the fund works and whether it is best for plan participants. Simply selecting any TDF series does not fulfill fiduciary obligations.

Confounding plan sponsors' efforts to understand and evaluate their target date offerings is the fact that the fund families *themselves* can change over time. Recent research from Ibbotson/Morningstar[18] illuminates how the historical allocations of several TDF series have shifted over time. In general, potential reasons for these shifts include methodological changes, a tactical asset allocation overlay, loose rebalancing bands, and more. See Exhibit 3 for an example of these shifts in one TDF series, where the glide path seems to change significantly over time – especially near the target date of age 65, where equity exposure fluctuates between about 25% and 50%. We note the allocations shown in Exhibit 3 are adjusted for the annual "roll-down" of the glide path, and so if there are no changes to the glide path the chart would show the same allocations for each year.

Exhibit 3. Observed glide paths of Fidelity Freedom Funds, 1996–2010



Source: Ibbotson Associates and Morningstar Direct.
This material contains information concerning investments other than those offered by Russell Investment Group, its affiliates or subsidiaries. Some mutual fund products may not offered by Russell Investments. Neither Russell nor its affiliates are responsible for investment decisions made with respect to such investments or for the accuracy or completeness of information about such investments.

While it's tempting to go with the decision that "feels safe," this is not the same thing as making a safe fiduciary decision.

Even if the reasons for shifts are valid, a target date series that shows a wide variety of allocations over time is difficult to judge. Worse yet, the fund provider's glide path can, per the Morningstar paper, "change dramatically over time, often with no explanation." These findings underscore the importance of performing ongoing due diligence of target date funds.

SO, WHAT SHOULD A FIDUCIARY DO?

For plan sponsors with TDFs in their lineups, the best course of action begins with becoming familiar with the funds. Important characteristics of a target date fund include:

- The shape of the overall glide path over the life of the fund, particularly around the retirement date;
- The potential for change in the glide path;
- Which asset classes are included, and how the mix changes over time;
- Whether the fund is managed passively, actively, or with a combination of both approaches;
- The skill levels of any active managers in the fund; and
- Fees.

Then, a sponsor must decide whether a given fund remains best for the plan's participants, and should consider alternatives if it doesn't. Of course, sponsors should always document their decision rationale.

Conclusion

To properly address the simple question "active or passive?" requires complex thinking – the kind ERISA's standard of care asks of plan fiduciaries. Hopefully, we've made clear there's no blanket answer to the question. While it's tempting to go with the decision that "feels safe," this is not the same thing as making a safe *fiduciary* decision. So, what should plan sponsors consider as they decide between active or passive in their DC plans? To reiterate the points we've been discussing throughout:

1. **Passive may not be the safe fiduciary option.** Do not automatically dismiss attractive active management opportunities.
2. **Active management is worth considering.** Carefully consider the alternatives to passive on a case-by-case basis.
3. **Cap-weighted is not the only way to invest passively.** Choosing the flavor of passive is an "active" decision.
4. **There's no "passive" option for target date funds.** Understand your plan's target date offering, and monitor and periodically reconfirm its appropriateness.

The importance of (and the potential payoff from) conducting careful due diligence on whether active or passive management works best, and in which asset classes, has never been greater than in this fee-sensitive environment. That's why Russell's framework for considering an alternative to passive investment is, we believe, a great starting point for that process. It can help sponsors put into place processes for conducting critical reviews of the alternatives within each asset class and for making informed decisions on behalf of their plan participants.

---

[1] Parts of this document are based on a 2007 *Russell Research* paper, "The Risks and Benefits of Active Management in Target Date Funds: It Doesn't Have to Be Either/Or," by Bob Collie.
[2] See Cornell University Law School."U.S. Code 1104 – Fiduciary Duties", accessed on April 10, 2012 at http://www.law.cornell.edu/uscode/text/29/1104
[3] The value of explicit and implicit opportunities forgone by choosing one option over the next best alternative
[4] Sharpe, William F. "The Arithmetic of Active Management." *Financial Analysts' Journal*, 47(1), January/February 1991.
[5] PIMCO, 2012 Defined Contribution Consulting Support and Trends Survey.
[6] Ezra, Don, and Geoff Warren. "When should investors consider an alternative to passive investing?" *Russell Research*, January 2010.
[7] Characteristics of a "pure play" infrastructure exposure include a steady cash flow profile tied to a long-lived, semi-monopolistic market position. For more information, we refer the reader to Adam Babson's "Structuring a listed infrastructure portfolio." *Russell Research*, May 2011.
[8] The S&P GSCI holds 70% of assets in energy commodities as of December 31, 2011.
[9] Bouchey, Paul, Mary Fjelstad and Hemambara Vadlamudi, "Measuring alpha potential in the market: Using the Russell-Parametric Cross-Sectional Volatility Indexes," *Russell Research*, September 2010.
[10] See the Russell-Parametric Cross-Sectional Volatility Indexes at http://www.parametricportfolio.com/crossvol. On the left hand side, select "Large Cap" in one menu and "Small Cap" in the other. Small cap cross vol appears to be significantly higher in all periods going back 15-plus years.
[11] Hintz, Dave. "The third dimension of style: Introducing the Russell Stability Indexes." *Russell Research*. December 2010.
[12] Here, we are really speaking of asset allocation in general. There have been several studies of the effects of asset allocation on both portfolio variance and return, including Roger Ibbotson and Paul Kaplan's "Does Asset Allocation Policy Explain 40%, 90% or 100% of performance?" in the January/February 2000 edition of *The Financial Analysts Journal*.
[13] One reasonable counterpoint to this claim is that the market portfolio is a starting point. One potential approach is to allocate an investor's target date fund assets such that, along with the present value of the investor's future savings, their total portfolio of assets and future savings resembles the market portfolio. However, this is hardly representative of the common industry view, chiefly because there *is* no common industry view at this time.
[14] Powell, Robert. "Target-date funds missed the target in 2008." Published February 2009, accessed on March 27, 2012 at http://articles.marketwatch.com/2009-02-04/finance/30781807_1_target-date-target-date-funds-target-maturity
[15] United States Department of Labor. "DOL/SEC Hearing On Target Date Funds And Similar Investment Options", accessed on March 27, 2012 at http://www.dol.gov/ebsa/regs/cmt-targetdatefundshearing.html
[16] United States Department of Labor. "Investor Bulletin: Target Date Retirement Funds", accessed on March 27, 2012 at http://www.dol.gov/ebsa/pdf/TDFinvestorbulletin.pdf
[17] Janus Capital Group Press Release, "Survey Reveals Plan Sponsors May Have a False Sense of Security with Target-Date Funds." Published November 15, 2011, accessed March 27, 2012 at Bloomberg.com: http://tinyurl.com/7ufzdjg.
[18] Idzorek, Thomas, CFA; Jeremy Stempien and Nathan Voris, "Bait and Switch: Glide Path Instability." Published September 2011, accessed April 2, 2012 at http://tinyurl.com/7v5pb6y.

Author: Daniel Gardner

For more information:

Call Russell Investments at **800-426-8506** or
visit **russellinvestments.com/institutional**

Important information

Nothing contained in this material is intended to constitute legal, tax, securities or investment advice, nor an opinion regarding the appropriateness of any investment, nor a solicitation of any type. The general information contained in this publication should not be acted upon without obtaining specific legal, tax and investment advice from a licensed professional.

These views are subject to change at any time based upon market or other conditions and are current as of the date at the beginning of the document. The opinions expressed in this material are not necessarily those held by Russell Investments, its affiliates or subsidiaries. While all material is deemed to be reliable, accuracy and completeness cannot be guaranteed. The information, analysis and opinions expressed herein are for general information only and are not intended to provide specific advice or recommendations for any individual or entity.

Please remember that all investments carry some level of risk, including the potential loss of principal invested. They do not typically grow at an even rate of return and may experience negative growth. As with any type of portfolio structuring, attempting to reduce risk and increase return could, at certain times, unintentionally reduce returns.

Diversification does not assure a profit and does not protect against loss in declining markets.

Target date fund investing involves risk, principal loss is possible. The principal value of the fund is not guaranteed at any time, including the target date. The target date is the approximate date when investors plan to retire and would likely stop making new investments in the fund.

Investments that are allocated across multiple types of securities may be exposed to a variety of risks based on the asset classes, investment styles, market sectors and size of companies preferred by the advisors. Investors should consider how the combined risks impact their total investment portfolio and understand that different risks can lead to varying financial consequences, including loss of principal.

Target date funds are not intended to be a complete solution to investors retirement income needs. Investors must weigh many factors when considering to invest in these funds, including how much an investor will need, how long will the investor need it for, what other sources the investor will have and, if the investor is purchasing shares in an IRA account, whether the fund's target distributions will meet IRS minimum distribution requirements once age 70-1/2 is reached.

Russell Investments’ ownership is comprised of a majority stake held by funds managed by TA Associates with minority stakes held by funds managed by Reverence Capital Partners and Russell Investments’ management.

Frank Russell Company is the owner of the Russell trademarks contained in this material and all trademark rights related to the Russell trademarks, which the members of the Russell Investments group of companies are permitted to use under license from Frank Russell Company. The members of the Russell Investments group of companies are not affiliated in any manner with Frank Russell Company or any entity operating under the “FTSE RUSSELL” brand.

For use with institutional investors only.

First used: May 2012 (Reviewed for continued use: August 2017) AI-25811-08-20