TIAA-CREF Comments Ignore the Findings of the Investment Study

TIAA-CREF has chosen to comment on the release of the study commissioned by the Connecticut State Employees Retirement Commission (SERC) with a posting on their website at: http://www.tiaa-cref.org/about/press/about_us/releases/pdf/c39770FINAL.pdf .

TIAA-CREF makes three basic points:

1. "First, the authors use a 10-year period ending March 2007 to compare fund and account returns when a longer period would reflect a more realistic time frame for a retirement investor."

   Comment: The authors concluded that a 10-year period, which included both up and down markets, was the best choice to compare the achievable performance of the Connecticut ARP investment menu to TIAA-CREF retirement annuities. Given that a number of the investment vehicles on both the TIAA-CREF and Connecticut ARP menus did not exist prior to 1997, we found that choice appropriate. The current study also provides terminal wealth forecasts for 10, 15, and 20-year periods. In the original study, the authors made terminal wealth projections for an entire expected working career of 40 years. TIAA-CREF criticized that time frame as well. In light of recent comments, it is difficult to determine what time frame TIAA-CREF would consider suitable.

2. "Second, the authors rely on unrealistic assumptions about retirement investor behavior."

   Comment: As an academic study, the professors looked at three basic portfolio scenarios for participants: efficient frontier portfolios, naïve (equal weight) portfolios, and TIAA-CREF model portfolios vs. State of Connecticut model portfolios. As the fiduciaries for the Alternate Retirement Plan, SERC would expect to see the efficient frontier portfolios to judge possible return alternatives and to benchmark the model portfolios that our advisor constructed for plan participants to utilize. The naïve portfolio analysis was provided, as the authors said, as a lower bound benchmark and to eliminate the issue of selection bias. The model portfolios in the study were based on actual asset allocations suggested by TIAA-CREF using its retirement annuities or by the ARP's advisor using the current investment menu for participants with different risk tolerances. Unlike TIAA-CREF's claims, the model portfolios—

the very same ones communicated to participants—provide a reliable indicator of "retirement investor behavior". The summary provided to participants describes the results: *"The ARP/403(b) model portfolios based on the current investment menu outperformed the comparable TIAA-CREF models at every risk level. For example, $10,000 invested in the CT Aggressive Model over a 20-year period, was found to have an expected terminal value of $120,350, versus $69,300 using TIAA-CREF's Aggressive Model—a difference of 74% in terminal wealth. Over a 10-year period, the expected result for a $10,000 investment in the CT Aggressive Model was $65,900 compared to $42,700 using TIAA-CREF's Aggressive Model—a difference of 54% in terminal wealth. Under the CT Moderately Aggressive Model, over a 20-year period, a $10,000 investment would have yielded $100,260 as opposed to $59,000 using TIAA-CREF's Moderately Aggressive Model—a difference of 70% in terminal wealth . Over a 15-year period, $10,000 invested in the CT Moderately Aggressive Portfolio would yield $57,300 versus $42,700 using the similar TIAA-CREF portfolio—a difference of 34% in terminal wealth.* **In summary, the study shows that the Connecticut model portfolios outperform the TIAA-CREF annuity model portfolios at every risk level.**

3. "Third, the authors disregard actual choices available to plan sponsors who turn to TIAA-CREF for help in constructing a lineup and accounts to enable their employees to invest for a secure retirement."

Comment: In 2005, when the new fund menu and record keeper for the ARP and 403(b) plans was chosen TIAA-CREF was unable to provide the diversified investment menu we were seeking. However, we did add five institutional mutual funds (institutional share classes) from TIAA-CREF, along with lifecycle and index funds from Vanguard, and actively managed "best in class" institutional mutual funds from a number of fund families, totally replacing the existing annuity funds. This study confirms that total replacement of variable annuities with a diversified menu of institutional mutual funds (rather than tacking on additional funds) provides better results for participants. We are pleased to see from its new press release that TIAA-CREF is beginning to follow the model we adopted in 2005. They might serve colleges and universities and their participants better by replacing variable annuity products and the traditional TIAA account as retirement plan investment vehicles with the model that we adopted for the defined contribution plans in the State of Connecticut.

Other Comments

In additional comments on its website, TIAA-CREF repeats objections to the prior study, even though those concerns have nothing to do with the current study. In addition, TIAA-CREF's comments ignore the study's conclusion that a lineup of its annuity funds entails a significant overlap of holdings, a much higher correlation of results, and, therefore, offers poor diversification potential when compared to the Connecticut lineup of funds. For example, the CREF Equity Index fund tracks the Russell 3000, approximately 75% of the CREF Stock fund also tracks the Russell 3000, and the equity portion of the CREF Social Choice Fund starts with the Russell 3000 and then screens for social criteria. Even the CREF Global Equity Fund holds many of the same domestic stocks as the other funds.

Thomas C. Woodruff, Ph.D. Director, Retirement & Benefit Services Division
Margaret E. Haering, J.D., AIFA®, Assistant Director, Retirement & Benefit Services Division
10/23/2007