

INSIGHTS FROM THE
2015 Global Retirement Savings Summit

Japanese and International Experiences

23 APRIL 2015 • TOKYO

- **Japan's economy and asset management sector** •
 - **Japanese, UK, and US pension systems** •
 - **DC reforms in Japan** •
- **UK and US experiences with automatic enrolment and target date funds** •
- **Financial education and behavioural economics** •

INSIGHTS FROM THE
2015 Global Retirement Savings Summit
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ICI Global is the international arm of the Investment Company Institute (ICI). It serves a fund membership that includes regulated funds publicly offered to investors in jurisdictions worldwide, with combined assets of US\$19.0 trillion.

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This report is third in a series of publications about ICI Global's retirement savings events. Previous reports include:

*Insights from the 2014 Global Retirement Savings Conference:
Common Principles for a Diverse World*
Geneva
17–18 June 2014

*Insights from the 2013 Global Retirement Savings Conference:
The Role of Investment Funds*
Hong Kong
26–27 June 2013

These reports are available at www.iciglobal.org/retirementpublications.

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ABOUT ICI GLOBAL

The international arm of the Investment Company Institute, ICI Global serves a fund membership that includes regulated funds publicly offered to investors in jurisdictions worldwide, with combined assets of US\$19.0 trillion. ICI Global seeks to advance the common interests and promote public understanding of regulated investment funds, their managers, and investors. Its policy agenda focuses on issues of significance to funds in the areas of financial stability, cross-border regulation, market structure, and pension provision. ICI Global has offices in London, Hong Kong, and Washington, DC.

ABOUT THE INVESTMENT COMPANY INSTITUTE

The Investment Company Institute (ICI) is a leading, global association of regulated funds, including mutual funds, exchange-traded funds (ETFs), closed-end funds, and unit investment trusts (UITs) in the United States, and similar funds offered to investors in jurisdictions worldwide. ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of funds, their shareholders, directors, and advisers. ICI's US fund members manage total assets of US\$17.5 trillion and serve more than 90 million US shareholders. Members of ICI Global, the international arm of ICI, manage total assets of US\$1.5 trillion.

ICI has a deep interest in the retirement system and retirement policy. In the United States, ICI's mutual fund members manage roughly half of the US\$14.4 trillion in assets in defined contribution (DC) plans and individual retirement accounts (IRAs). The Institute has a large and active research programme on retirement trends, economics, and policy issues, and is the primary source for statistical data and research on retirement plans and the role of mutual funds in helping investors save for retirement.

TO LEARN MORE

Visit www.iciglobal.org/grsc to access all the materials from the 2015 Global Retirement Savings Summit, including panellists' slides, speaker biographies, and video testimonials.

Contact Anna Driggs, associate chief counsel, retirement policy, at anna.driggs@iciglobal.org with questions about this report or about global long-term savings and retirement.

Go to www.ici.org/retirement to read more about ICI's retirement research.

Letter from Dan Waters Managing Director, ICI Global

Economic conditions and demographic changes are straining government pay-as-you-go retirement systems worldwide, which is leading countries to reform their pension systems. This is particularly true in Japan, where a rapidly ageing population and uneven economic growth have spurred the government to initiate a series of reforms, most recently to its defined contribution (DC) system.

Given these developments, Tokyo was the ideal place for ICI Global to host its *Global Retirement Savings Summit: Japanese and International Experiences*, which took place on 23 April 2015 and examined Japanese, US, and UK experiences with retirement reform. The summit continued a discussion we have pursued through Global Retirement Savings Conferences in Hong Kong (2013), Geneva (2014), and Paris (2015).

In Tokyo, ICI President and CEO Paul Schott Stevens set the stage by discussing America's DC system and the role that investment funds have played in the system's success. Naoyuki Yoshino, dean of the Asian Development Bank Institute and professor emeritus at Keio University, offered an overview of Japan's economy, savings culture, and asset management industry in his keynote address.

During the first session, Japanese, UK, and US panellists spoke about each country's approach to designing and reforming their pension systems. For example, the panellists examined how the United States

and United Kingdom have used automatic enrolment in different ways to successfully increase participation. The panellists also explored the different emphases that their three countries have placed on behavioural economics and financial education to increase engagement: though all three are expanding financial education, the United Kingdom and United States have relied on behavioural economics as well.

The second session focused on appropriate asset allocation strategies for long-term savings. In Japan, 60 percent of household assets are allocated to bank deposits, and the panellists discussed Japanese savers' desire and need to have more diversified portfolios. The panellists also examined UK and US experiences with defaulting retirement savers into investment funds that adjust a participant's equity and fixed-income allocations based on the saver's age.

In each of these instances, and others, the differing experiences of these three countries offer fascinating insights, and I encourage you to read the report for full details.

Addressing global retirement savings issues is a daunting challenge, but ICI Global is committed to advancing the dialogue about how to improve retirement security worldwide. I hope the information in this publication will help foster solutions to meeting that challenge and that you will share this report with others.

Opening Remarks and Reflections on the US Pension System

PAUL SCHOTT STEVENS

President and CEO

Investment Company Institute

United States

Around the world, countries of every size and economic situation are grappling with how they can help their populations build resources for retirement. The challenge of amassing adequate retirement savings is an especially critical issue for Japan, given its rapidly ageing population, explained ICI President and CEO Paul Schott Stevens in his opening remarks for the summit. Stevens discussed ICI and ICI Global's work in the global pension space and some of the themes observed, including that more countries are examining defined contribution (DC) systems and considering how they can help their citizens save for the future. Using ICI research, Stevens spoke about the success of the US DC system, and the important role that regulated funds have played in that success.

The following is an edited transcript of his remarks.

Paul Schott Stevens: Good afternoon and welcome. Thank you for joining us as we discuss how retirement systems are evolving around the world and how DC plans and regulated funds can help build retirement resources. I first came to Tokyo in 1990 as a US-Japan Leadership Fellow. I've had many occasions to return to Japan since then, but none in recent years, so I am very happy to be back once again.

Of course, 25 years ago, I could not have predicted that I would return to Tokyo to discuss what has become an important issue for societies around the globe, the challenge of building adequate retirement resources—which is an especially critical issue for Japan. According to a 2013 economic survey by the Organisation for Economic Co-operation and Development [OECD], Japan has the oldest population in the world, and it continues to age rapidly. Thus, pension reform has a special urgency, which makes Tokyo an ideal place to hold a summit on how to create successful

retirement systems that can help people in a wide range of jurisdictions build adequate resources.

ICI in the United States and ICI Global internationally have done a great deal of work in this space. One of our core missions is to document the role that DC plans and regulated funds can and do play in helping meet retirement savings challenges. We've advanced this mission by studying the evolution of retirement systems in different countries and promoting dialogues among regulators, academics, and the fund industry through our previous global retirement savings conferences in Hong Kong and Geneva.

As a result of this work, we have noted many themes that current national debates over pension policy have in common. Perhaps the most important theme is that more and more countries are examining DC systems and considering how these systems can help their citizens save for the future. In

Australia, Chile, New Zealand, the United Kingdom, and elsewhere, DC systems have replaced or supplemented government-provided retirement schemes and defined benefit [DB] plans.

Why is that, you might ask? What makes DC plans so attractive? Well, of course, each country has its own circumstances. In the United States, DC plans are popular because they offer retirement savers many advantages. They empower individuals by helping them build savings over their working lives. They convey ownership of retirement assets to workers. They are transparent. They're also portable and accrue value throughout a participant's life.

During our first panel, we will hear about DC systems. Specifically, we will learn about the US, UK, and Japanese experience with these systems and how each country has designed, integrated, and reformed them. As our panellists discuss their experiences, it's important to keep in mind that each country's DC system is different, because every country has its own unique history, culture, institutional framework, domestic economy, and capital markets, among other factors, all of which may influence its approach towards retirement planning. Thus, I want to make clear that the ideas and viewpoints that emerge from one country's experience certainly are not meant to be prescriptions for any

other nation. Instead, they're meant to be part of an open dialogue to help us all learn from one another about how different societies are meeting the same challenge.

During our second panel, we will talk more about funds and their role in DC systems. In particular, we will learn about the Japanese, UK, and US experiences with funds, including how some funds, such as life-cycle funds, are helping savers diversify their investments.

Now the role of regulated funds is an important part of this dialogue. These funds, as part of DC plans, can play a crucial role in helping meet global retirement savings challenges, which I will illustrate through some ICI research. According to our data for worldwide total net assets of regulated funds, there has been a global increase in those assets of more than 700 percent within the past 20 years [Figure 1.1]. In meetings here in Japan, I've had occasion to point out that while the United States and Europe have relatively large fund sectors, the potential in the Asia-Pacific region is very clear. In relative terms, the current size is much smaller, certainly much smaller than it potentially might be.

If you look at worldwide long-term mutual fund assets by type of fund, excluding money market funds, there is a fantastic array of what we call hybrid or mixed

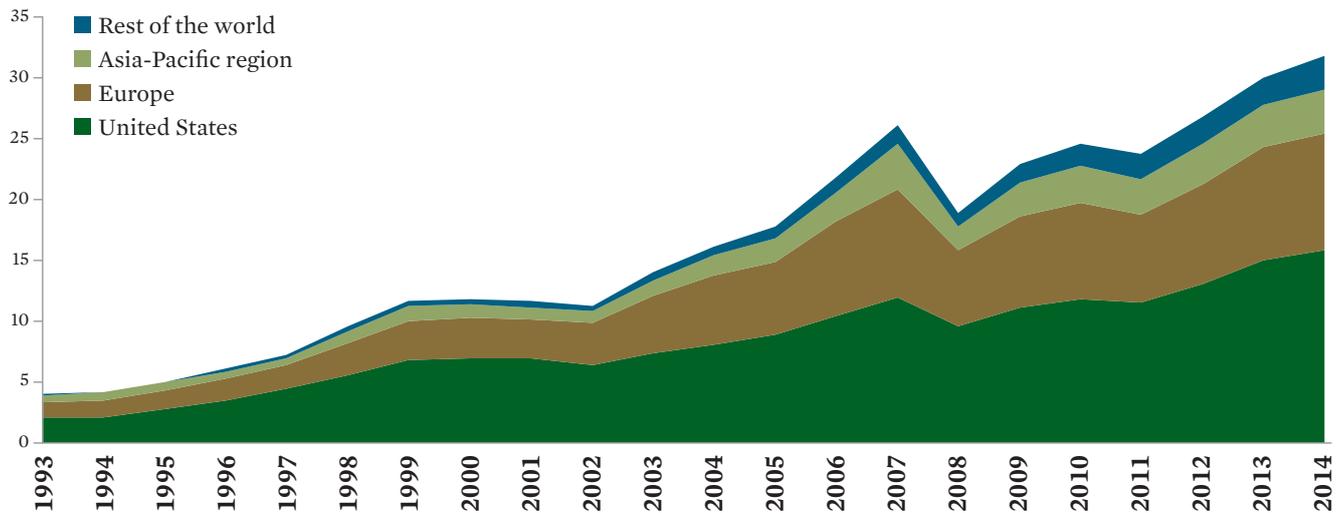
About the speaker

Paul Schott Stevens has served as president and CEO of the Investment Company Institute (ICI), a leading, global association of investment funds, since June 2004. He directed the 2011 launch of ICI Global to respond to the globalisation of fund investing and regulation, and has consistently championed the role of regulated funds in retirement savings. Stevens was ICI's general counsel from 1993 to 1997. Earlier in his career, he served as special assistant for national security affairs to US President Ronald Reagan.

FIGURE 1.1

Worldwide Total Net Assets of Regulated Funds Have Increased Nearly 700 Percent in 20 Years

Trillions of US dollars; year-end, 1993–2014



Source: International Investment Funds Association

Prepared by: Paul Schott Stevens, presentation at the 2015 Global Retirement Savings Summit (Tokyo, Japan)

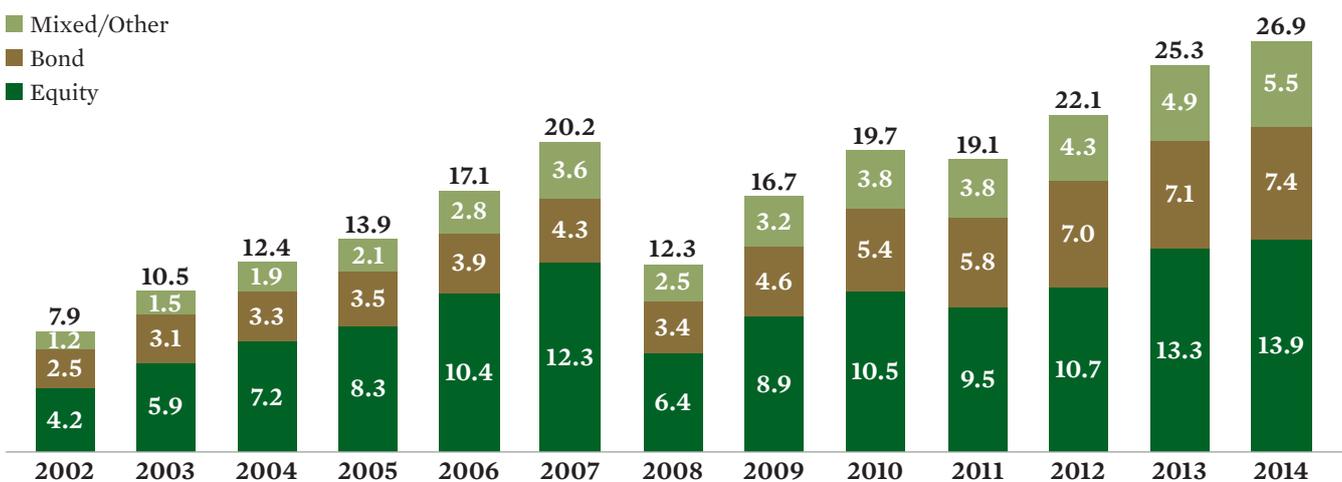
funds, bond funds, and equity funds. The story here is very significantly ‘an equity investing story’—a story where the growth of investments held over a longer period of time is an important part of the objective [Figure 1.2].

We certainly can see that in the context of the US retirement system, where US retirement assets have increased by 250 percent since 1995. When I say retirement assets, I am talking about all the assets that Americans have put aside for retirement in both

FIGURE 1.2

Composition of Worldwide Long-Term Mutual Fund Assets by Type of Fund

Trillions of US dollars; year-end, 2002–2014



Note: Data include home-domiciled funds, except for Hong Kong, the Republic of Korea, and New Zealand, which include home- and foreign-domiciled funds. Components may not add to the total because of rounding.

Source: International Investment Funds Association

Prepared by: Paul Schott Stevens, presentation at the 2015 Global Retirement Savings Summit (Tokyo, Japan)

public and private DB systems, DC systems, and in individual retirement accounts. Of the \$6.8 trillion in DC plan assets in the United States, 55 percent are invested in regulated funds. Fund companies in my country have a long history of interacting with investors and can provide valuable insights to them and to others about how to reach, educate, and serve retirement savers.

It's no accident that US investors place so much confidence in regulated funds as vehicles for very long-term investments. ICI has been surveying households for a long period of time now on these specific issues, including throughout the financial crisis, and according to our data, eight in 10 US households believe that investing in funds can help them meet their longest-term financial goals.

Another important aspect of US investing at large is the effect of strong competition on shareholder costs. The expenses incurred by mutual fund investors have declined substantially since 1990, both with respect to equity and bond funds [Figure 1.3]. For example, the average

expense ratio incurred by mutual fund investors declined from 0.99 percent in 1990 to 0.70 percent in 2014. For bond funds, the average expense ratio declined from 0.88 percent in 1990 to 0.57 percent in 2014. Part of the story about why US investors have strong confidence in funds as long-term retirement savings vehicles is illustrated by the expense ratios incurred by mutual fund investors in 401(k) retirement funds. These expenses have gone down even more substantially.

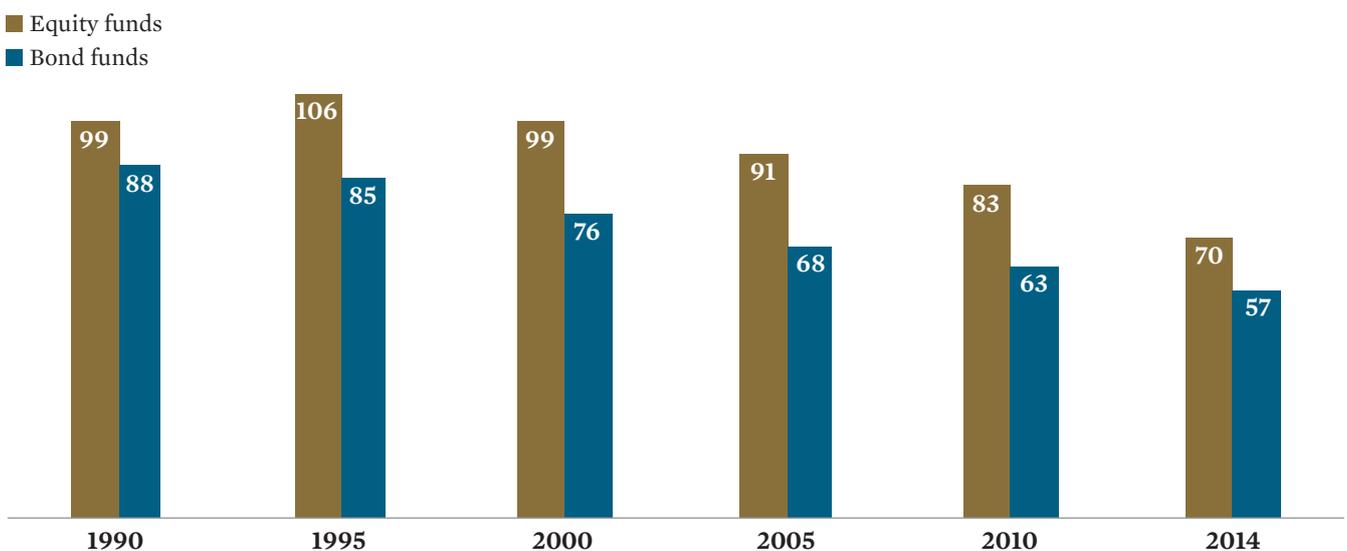
The use of funds as retirement vehicles is common in other jurisdictions around the world as well, which provides a global perspective that can inform policymakers as they consider needed reforms to their pension systems.

These are some perspectives out of the United States, and we will hear more perspectives today from other countries. ICI and ICI Global are dedicated to continuing this dialogue in years to come, as the issues at stake are very important and worthy of our continuing attention. 🌍

FIGURE 1.3

Expense Ratios Incurred by Mutual Fund Investors Have Declined Substantially Since 1990

Basis points, asset-weighted, selected years



Sources: Investment Company Institute and Lipper

Prepared by: Paul Schott Stevens, presentation at the 2015 Global Retirement Savings Summit (Tokyo, Japan)

Long-Term Savings Reforms in Japan: Asset Allocation, Pensions, and Defined Contribution Arrangements

NAOYUKI YOSHINO

Dean, Asian Development Bank Institute
Professor Emeritus, Keio University
Japan

According to a 2013 economic survey by the OECD, Japan has the oldest population in the world—and continues to age rapidly. In his keynote speech, Naoyuki Yoshino, dean of the Asian Development Bank Institute and professor emeritus at Keio University, Japan, discussed the country’s economic and long-term savings challenges as well as how Japan can meet them. Some of his recommendations included reducing the budget deficit, fostering asset diversification, improving financial education, developing a robust 401(k)-style system in Japan, and instilling self-responsibility for investment decisions among Japanese investors.

The following is an edited transcript of his remarks.

Naoyuki Yoshino: Good afternoon and thank you for having me. The first part of my presentation will be about the Japanese economy, and the second part will cover my proposals for Japan’s asset management industry.

Let me start by discussing household asset allocation in three countries: Germany, Japan, and the United States [Figure 2.1]. Japan has the highest percentage allocated to cash and deposits, close to 60 percent. The United States, by contrast, is well-balanced between cash and deposits, insurance and pensions, and securities and stocks. These differences in asset allocation led to the different amounts of time that it took for each country to recover from the 2008 financial crisis. Japan took longer to recover because banking is the dominant sector. In the United States, the banking sector is relatively small. Furthermore, in the United States, securitised assets were sold to other countries, so the damage to the US economy was much smaller compared to Japan. In Japan, we retained 100 percent of the bad loans within the country. So the US asset allocation model is a very

good way to diversify assets, and we need to bring Japan closer to this model.

Let’s discuss Japanese household allocation of assets over time [Figure 2.2]. Since the early 1990s, the main investments for most households have been deposits and insurance. They have only invested a small portion in ‘risky assets,’ which include investment trusts. One explanation for these trends in asset allocation is that a significant amount of assets are accumulated by those who are in their 60s, 70s, and older. These groups are very conservative, because they know their futures are short, so they mainly invest in common bonds.

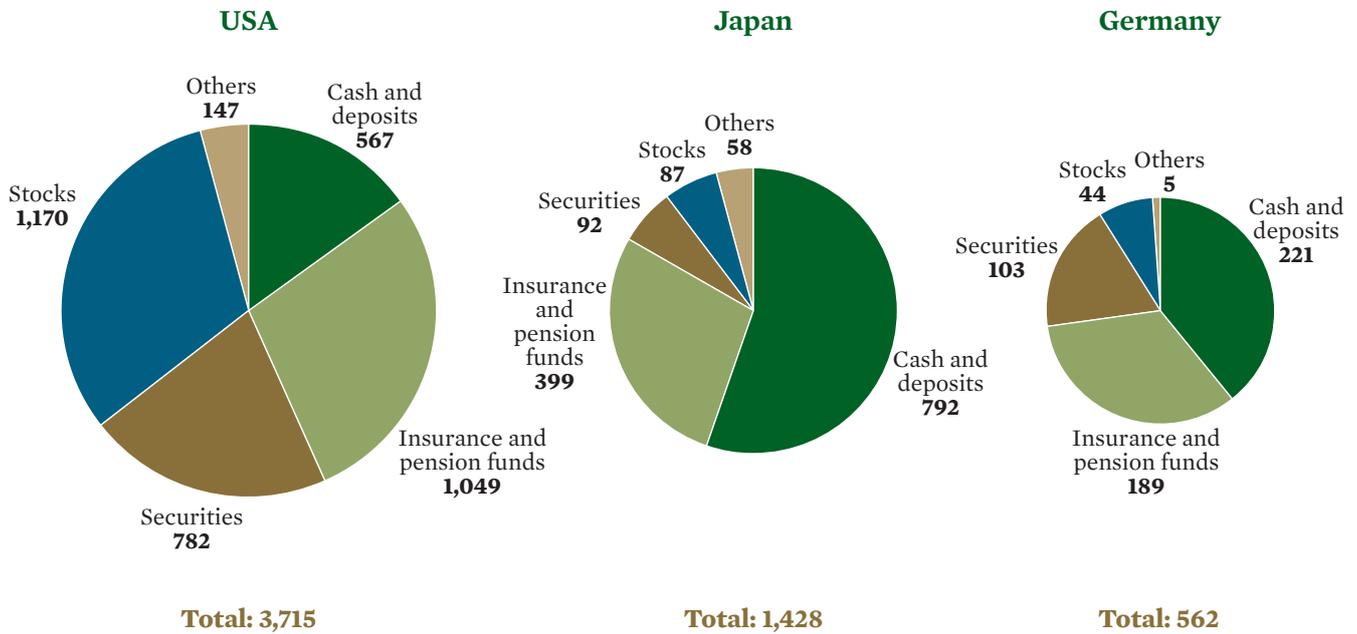
Furthermore, the Public Opinion Survey on Household Financial Assets and Liabilities found that about 50 percent of Japanese citizens choose financial institutions based on the ‘reliability and safety of [a] financial institution.’ Few rely on a high rate of return as a reason for selecting a financial institution, which is very different from the United States, where more than 70 percent of people look at the rate of return. So, there is a big difference between Japanese

FIGURE 2.1

Household Asset Allocation in Three Countries

Trillions of yen, 2010

In Japan, cash and deposits are nearly 60 percent of assets managed. The amount of marketable securities and shares is extremely small.



*The size of each pie chart reflects the total amount of personal-sector financial assets.

Source: Yoshino, Naoyuki and Kaji, Sahoko, eds. 2013. Hometown Investment Trust Funds; New York: Springer.

Prepared by: Naoyuki Yoshino, presentation at the 2015 Global Retirement Savings Summit (Tokyo, Japan)

investors and other investors. In addition, it is important to recognise that Japan's rate of return is very low compared to other countries, such as Germany (which has the highest rate of return), France, and the United States.

Let's discuss the Japanese stock market. Its peak performance was in 1989, but it has

been falling since then. After Prime Minister Abe came into power, the stock market slightly recovered, but then its downward trend continued. Many people say that if asset management companies continue to invest in Japan's domestic market, the stock market's performance will remain very low. Of course, then they should invest overseas. Unfortunately though, more than

About the speaker

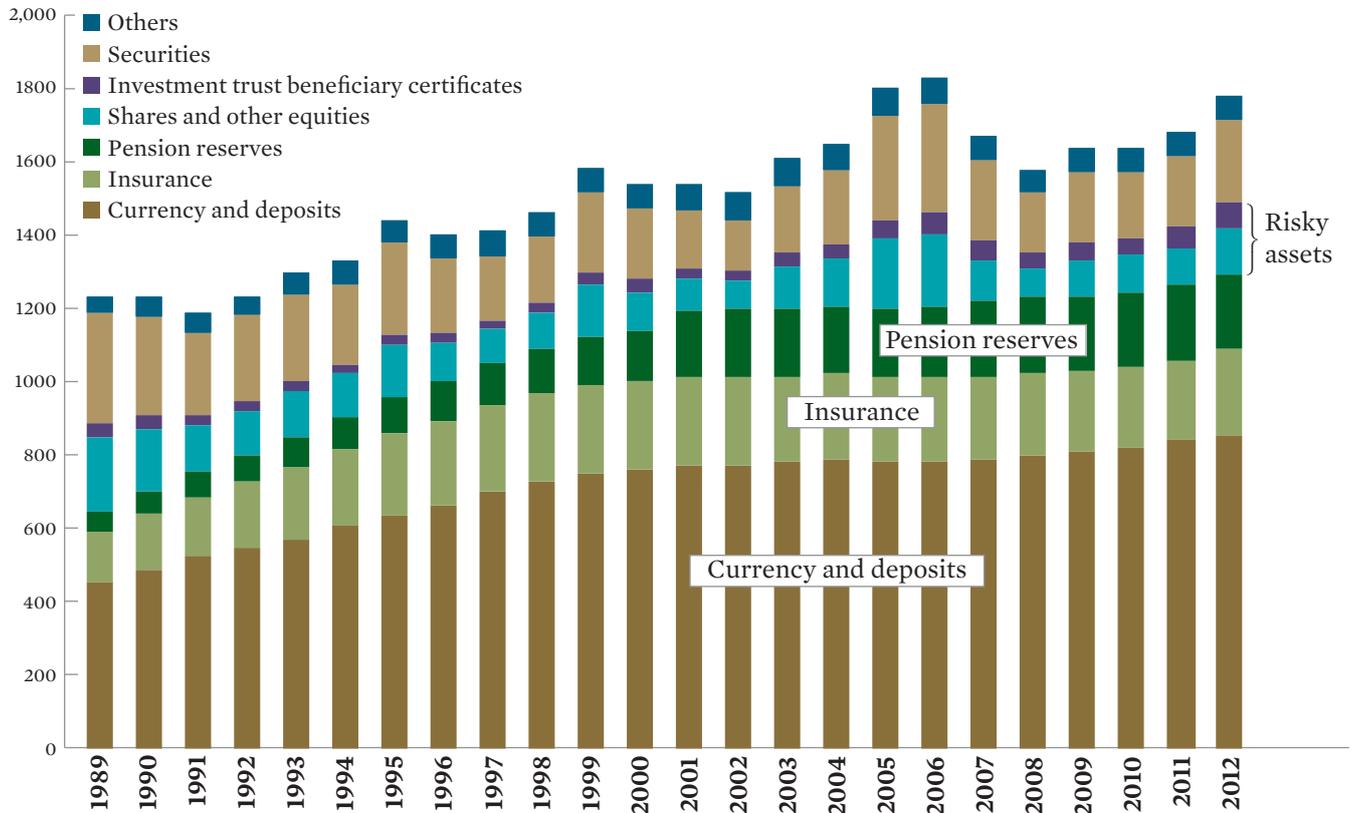
Naoyuki Yoshino is dean of the Asian Development Bank Institute; professor emeritus of Keio University, in Tokyo, Japan; and senior adviser at the Japan Financial Services Agency's Financial Research Center. In 2007, Yoshino was appointed chair of the Financial Planning Standards Board. He also served as chairperson of the Japanese Ministry of Finance's Council on Foreign Exchange and its Fiscal System Council. In addition, Yoshino was a board member of the Deposit Insurance Corporation of Japan, chairperson of the Meeting of Japanese Government Bond Investors, and was president of the Financial System Council of the government of Japan.

FIGURE 2.2

Household Asset Allocation in Japan

Trillions of yen

Around 80 percent of households' financial assets go to safe assets.



Source: Bank of Japan

Prepared by: Naoyuki Yoshino, presentation at the 2015 Global Retirement Savings Summit (Tokyo, Japan)

80 percent of Japan's assets managers specialise in the Japanese domestic market. There are very few overseas specialists compared to domestic specialists. All this makes Japan's asset management industry more domestic-market oriented, which keeps the rate of return low.

Next, let's talk about Japan's gross domestic product [GDP]. Again, the peak was around 1990, and since then, the real GDP has fallen. In my opinion, the main cause for this decline comes from the growing number of older people, many of whom are no longer working. So that creates a big problem for Japan. When the Japanese retirement age was introduced in 1950, 55 was the retirement age. At that time, life

expectancy was 59 years old, so many people died four years after they retired. But now people are retiring at 60 or 65, and many are living to be 88, 90, and 95 years old. Thus, our system does not work, partly because politicians are more concerned about getting votes from old people. Given that children cannot vote, the politicians have to be very good to the old people. This presents a conflict in terms of budget allocation. Social security for those 65 and older is about one-third of the Japanese budget, and it is only 6 or 7 percent for education. It should be reversed.

Because of the ageing population, tax expenditures have been increasing and tax revenues have been declining. This has

created huge budget deficits for Japan, and my presentation would not be complete without discussing Japan's budget deficit. In terms of debt to GDP ratio, Japan has the largest, and Greece has the second largest.

About one-third of Japan's budget goes to social security, while 16 percent goes to central and local government transfers. If we add these two categories together, we get about 45 percent. If we could reduce allocations to these two categories, we could reduce our budget deficit.

How can we reduce those allocations? With respect to reducing the social security budget, the easiest way is to postpone the retirement age. As a complement to that, the wage rate would have to be based on productivity. Currently, Japan's wage rate is mainly a seniority-based system. As a result, many companies do not want to keep old people because they are expensive and their productivity may be lower. So we need to change to a productivity-based wage rate and then make people work much longer. As to transfers from central to local governments, we could reduce this component by introducing private-sector money, especially regional mutual funds and regional investment trusts.

Let's turn to the pension asset management industry and pension system in Japan, which is particularly important because household savings rates have declined. Japanese people were famous for saving a lot. The peak savings rate was 23 percent in 1974, but this rate has rapidly and steadily declined. This is the result of three main factors: the economic growth rate, the growth rate of the population, and an increase in the number of retired people.

I now would like to talk about pension asset allocation. First, it appears that in the Japanese asset management industry, people rotate jobs every two or three years. So there isn't a lot of responsibility for the

assets that they're managing. Second, there is a lack of a corporate bond market. Currently, the two asset allocations in Japan are stocks and government bonds. Unfortunately, corporate bonds do not do well. This is partly related to the banking business. Banks want to keep good corporations and their bank loans, so if good corporations started to issue corporate bonds, then banks would lose their good customers. Therefore, there is not much development of the corporate bond market. However, to diversify asset portfolios, developing a corporate bond market is very important.

Another way to diversify pension asset allocation is to bring both a 401(k)-style pension system and self-responsibility to Japanese society.

– Naoyuki Yoshino

Another way to diversify pension asset allocation is to bring both a 401(k)-style pension system and self-responsibility to Japanese society. Currently in Japan, the majority of assets are allocated to government bonds. But in the United States, asset allocation is much more diversified. In my view, the difference in asset allocation stems from self-responsibility for investment decisions in the United States.

An additional reason for the current differences in pension asset allocation is the compensation and bonus system for asset managers. In Japan, if some asset managers do well, their bonus is not very large, but if they do badly compared to others, they are punished and criticised. So, poor performance has a significant negative downside, and good performance does not result in a significant upside. As a result, everyone wants to perform the same. So Japanese asset managers are always looking at the benchmark. For this reason, we have to change the performance-based salary system and we need to create incentives for asset managers. Otherwise, people will tend to just invest in government bonds.

It is important to mention that to fully introduce a 401(k)-type system in Japan, we need to improve our financial education. I'm really working hard in this area, but I've found that in Japan, most of the financial education classes are taught in the context of homemaking courses. Teachers instruct students how to cook and repair clothes, and those are the courses they teach as 'financial education.' We have to introduce some better financial education into primary and secondary schools so that people can decide for themselves how to allocate their assets. Our government is taking steps in the right direction. The Financial Services Agency [FSA] organised a study group on financial education in November 2012. In addition, the Central Bank of Japan is working on financial education reform, and I am chairing that effort.

Next, I would like to talk about how Basel capital requirements created opportunities for mutual funds. Basel capital requirements say that if a bank wants to make a loan to riskier sectors, then it must increase its capital. Before the Basel requirements, Japanese banks made a wide range of loans, including loans to venture businesses and riskier sectors. But after the Basel requirements were introduced, banks became very conservative in making loans. So banks no longer provide capital to start-ups or risky businesses.

As a result, the number of start-ups in Japan is very low, and that is another cause of the slow growth in Japan. So we need some channels to bring our assets to start-ups and small businesses, which can be funded by mutual funds or hometown investment trusts.

There are two kinds of investment trusts. One is a well-known and standard investment trust, which is nationwide. Another one is often used locally, and we call it the hometown investment trust. In Japanese,

it is called *urusato tōshi* fund. Prime Minister Abe is now trying to use these hometown investment trust funds to develop rural regions and local areas. In my book, *Hometown Investment Trust Funds*, I give several examples of how these funds work. One example is from the fishing industry. After the tsunami and earthquakes, many fishermen lost their ships. They had to repair them, but the banks wouldn't lend them the money. So many people helped the fishermen by investing in hometown investment trust funds. The fishermen repaired their boats, started to catch fish, and dividends are coming from their profits. So this system is working very well. Other examples of how home trust funds are used include businesses devoted to the production of solar power panels, Japanese sake, and seaweed products. These are start-ups and they are not financed by bank loans, but by hometown investment trust funds from various individuals.

So I think there are two kinds of investment categories for investors: local projects or businesses and large projects or businesses. Mutual funds may be more appropriate for large projects, while hometown investment trust funds could finance smaller projects and regional infrastructure, such as a local airport.

I would now like to talk about turnover in mutual funds. In Japan, turnover within mutual funds occurs almost once every two years. Thus, the holding period is very short. If Japanese people invested more for the long term, the rate of return would improve significantly. For example, if an individual did not make any transactions from 2000 to 2013, the net return would have been 10.7 percent. Switching funds every two years during the same period would result in a net rate of return of -0.26. We have to make people invest for the long term rather than for the short term. To do so, we need to solve some issues

surrounding commissions and fee structures, and we need to move away from encouraging frequent selling and reselling.

I'd also like to make a point about 'purposeful' investing and investing for the longer term [Figure 2.3]. In Japan, the largest number of mutual fund investors [36.7 percent] gave no specific reason for their investment; the investment was simply recommended by retailers. By contrast, in the United States, most of the mutual fund investors had a specific purpose for investing: retirement, tax reasons, an emergency, and so on. So US mutual fund investors are very purpose-oriented, whereas Japanese investors are not nearly as oriented to their own needs. Another part of this story is how long investors hold mutual funds. In the United States, 42 percent of

shareholders hold funds for longer than 10 years. In Japan, 40 percent of investors do not hold funds for any specific period, 21 percent hold funds for three to five years, and 14 percent hold funds for two to three years. To summarise, Japanese investors either hold mutual funds without any specific purpose, or they hold the funds for short periods. I believe that Japanese people need to have their own reasons to invest, and that we also have to start investing for the longer term.

I'd now like to conclude my remarks by summarising my suggestions for Japan's professional investment management industry and for the economy overall. First, the industry needs to change and we also need to change its bonus and salary systems. Second, the industry needs

FIGURE 2.3

Purpose of Holding Mutual Funds

Survey 2014

USA	91%	Retirement
	49%	Reduce taxable income
	49%	Emergency
Japan	36.7%	No specific reason, recommended by retailers
	30.4%	Prepare for after retirement
	17.7%	Asset diversification

Period of Holding Mutual Funds

Survey 2014

USA	42%	Longer than 10 years
	27%	6–10 years
	27%	1–5 years
Japan	40.7%	No specific period
	21.0%	3–5 years
	14.8%	2–3 years

Prepared by: Naoyuki Yoshino, presentation at the 2015 Global Retirement Savings Summit (Tokyo, Japan)

to develop expertise in investing overseas. Third, Japan needs to improve the rate of return on both financial and human capital. Fourth, we need a performance-based wage rate and people should work longer. Finally, we need to create incentives for product retailers and asset managers. As long as Japanese people have goals and objectives, Japan will be very strong. Thus, we need to bring all of our minds together to improve our economy, and that will create a recovery of the Japanese economy. Thank you very much.

Dan Waters: My name is Dan Waters, and I'm the managing director of ICI Global. Thank you very much, Professor Yoshino, and if you don't mind, we have a couple of questions for you from the audience. The first one is this: from the perspective of a young Japanese person, how should the pension system change?

Yoshino: I think a 401(k)-type system and self-responsibility will be very important, because savings rates are diminishing and the role of the government will be very important. So first I think we need education for young people and then we need to instill self-responsibility for asset allocation, taking into account longer lives postretirement.

Waters: As a follow-up of my own on this one: what is your impression or understanding of the risk appetite of young Japanese people? How do they feel about investments outside of deposits and guaranteed vehicles? Do they have a view? What's their approach?

Yoshino: The FSA compared a portfolio with the current asset allocation and a balanced portfolio in which one-sixth went to overseas stocks, one-sixth went to overseas bonds, one-sixth went to fixed-income assets, and the remaining one-sixth went to domestic bonds, stocks, and fixed assets. The balanced portfolio performed better than the portfolio with the current asset allocation, which teaches us that diversification is very important.

Waters: Thank you, and we have another question. What are the most important changes that Japan's asset management sector needs?

Yoshino: First, distributors have to think about investor behaviour. That is key. Usually, when investment trusts are doing well, Japanese investors tend to sell those good products. But as we have seen, long-term investment is always better compared to short-term investment. So I think educating people about these topics is important so we can show them that long-term investments produce higher rates of return for individuals. We need to create that confidence, which has been lacking in Japan for the past 10 to 20 years.

Audience member 1: I understand what you were saying, but over the past 20 years, the US equity market or bond market has performed well for Americans. That probably resulted in the prosperity of the US asset management industry. Is it realistic for the Japanese industry to experience the same level of success?

Yoshino: The performance of the Japanese economy has been very flat. That's why the performance of mutual funds didn't do very well. That said, Asia's economy is the fastest-growing in the world. I think China, India, and Southeast Asia will have very high performance in the next 10 to 30 years. Currently, Asia's GDP is very low, but if that growth were to keep going, about 40 percent of the world's GDP would be created from Asia. Japan is very close to other countries in Asia, so we can get the information in those countries much more quickly than US or European investors can. Thus, we should take advantage of that proximity and our access to information and invest in Asia's markets. So we should not just look at the Japanese market, but at overseas markets and our neighbors' markets as well.

Audience member 2: I was very interested in your statistics about why people invest in investment trusts, and it seemed like some people didn't know why. With that in mind, what can asset managers do to better win retail investors' trust? Is there a trust issue? Can they do something to improve that?

Yoshino: This is my own impression, and there are no statistics to support it, but in Japan, retail sellers have a much stronger position compared to asset management companies. So they choose the products that they think are good, but we need much

more information about various financial products than what we get from retailers.

Asset management companies can advertise their products through the Internet, and e-commerce, e-banking, and e-trading will become much more prevalent in Japan. When that happens, the managers won't need to rely on retail sales people. This could drastically change our portfolio allocation and asset management. So I think we should utilise e-commerce. That will be the key for asset management companies.

Audience member 3: In your presentation, you identified a high turnover ratio as one of the reasons why investors do not experience good investment performance. But how do the fees fit in? In Japan, a fee is charged against assets under management, but what is your view about the future? What kind of an approach would be most effective?

Yoshino: My own approach to fees and commissions is that first, the fixed fee, which includes the costs for producing a product, should be charged. Then there are the performance-based commissions. If investors make a profit, then retailers should also receive some of that money. But if investors lose some money, then part of their loss should be carried by the retail sellers. So I think fixed costs plus or minus performance-based commissions would be an effective approach. 🌱

PANEL 1

The Role of Private Pensions in Retirement Savings— Countries' Case Studies

PANELLISTS

STEPHEN P. UTKUS, Moderator
Principal, Vanguard Center for Retirement Research
The Vanguard Group
United States

TIM JONES
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NEST Corporation
United Kingdom

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Japan

More countries around the world are examining DC systems and considering how to successfully design them in a way that takes into account each country's particular history, culture, and economy. During this session, speakers from three different countries—Japan, the United Kingdom, and the United States—discussed each region's experiences with designing and reforming its DC system. The panellists also talked about some of the common challenges facing each system, including issues surrounding fees, automatic enrolment, financial education, and income during the decumulation phase.

The following is an edited transcript of the discussion.

Stephen P. Utkus: During this panel, we're going to have a comparative discussion about three countries whose DC systems are in different states of evolution. First we'll discuss Japan, where the system is at a pivotal point in its evolution, as the government is thinking about expanding the DC system to new participants. Next we'll examine the United States, where the system is a mature DC system, and which 10 years ago made a very significant structural change: a shift away from individual choice to one based on behavioural economics and on defaults set by employers and asset managers. Finally we will turn

to the United Kingdom, which has chosen a very innovative path, including adopting behavioural economic principles and also expanding its DC system to the country's entire workforce.

I'm pleased to be joined by two expert panellists: Akiko Nomura from the Nomura Institute of Capital Markets Research and Tim Jones, CEO of the NEST programme in the United Kingdom.

As we begin this discussion, I would like to remind you to think holistically about all the elements of a retirement system,

whether you're using the World Bank framework or the OECD's framework.

Let's briefly discuss the framework of a typical retirement system. There is a first pillar state-run pension system that needs to be considered when thinking about a DC system. Then there is a second pillar, either a mandatory or voluntary workplace retirement system. Finally, if applicable, there is a third pillar, which encompasses household retirement savings that are independent of workplace savings. Our panel will focus on the design of DC systems, including such elements as governance, coverage, fees, contribution policies, investment design, access to money before and during retirement, and a number of other features that influence the design of these systems [Figure 3.1]. So without further ado, I'd like to invite Akiko to speak.

Akiko Nomura: During my presentation I will discuss the ongoing reform of the Japanese DC system and the insights and lessons that Japan can learn from other countries, including the United States and United Kingdom.

Japan is at a turning point, as we are embarking upon a major reform of the DC system, and the bill to amend the system has been submitted to the Diet for deliberations by the parliament. Why is Japan trying to reform its system? In part, because of changes to the public pension system. Starting in fiscal year 2015, the Japanese government implemented a gradual reduction in public pension payments in response to Japan's low birth-rate and ageing society. Now that public pensions will be smaller, our citizens will need to rely more on private pensions to build their retirement resources, such as corporate-type DB and DC plans, as well as individual DB and DC plans.

There are two main components of the current reform bill [Figure 3.2]. The first component—under the umbrella of tax reform—is to expand coverage under the DC system. This component will make almost every Japanese citizen eligible to participate in a DC arrangement. It also will make benefits more portable. Under the current system, if a DC participant changes jobs or gets married and stays at home, then that

About the panellists

Tim Jones is CEO of the NEST Corporation. He has substantial experience in the financial sector, having previously held a variety of senior positions including non-executive director of Capital One Bank (Europe), chief executive of retail banking at NatWest Bank, and chief executive at Mondex, Purseus, and Simpay.

Akiko Nomura is a senior analyst at Nomura Institute of Capital Markets Research. Her research mainly focuses on pension schemes, the asset management industry, and securities regulation. Earlier in her career, she was a research analyst at Nomura Research Institute (NRI), and she worked in NRI America's Washington, DC, office from 1993 to 1995.

Stephen P. Utkus is principal and director of the Vanguard Center for Retirement Research, which assists employers, consultants, policymakers, and the media in understanding developments in the US retirement system. He is also a member of the senior leadership team of Vanguard's institutional retirement and investment business in the United States.

person's DC assets are frozen and that person is no longer able to contribute to his or her account. But with the reform, that person will be able to continue to contribute throughout his or her working life to build assets for postretirement life.

This expansion in coverage—when it's adopted—will be a meaningful accomplishment. Yet, while this reform will positively impact DC coverage, it also will create extra complexity to an already complicated system. So we hope there will be some simplification in the next round of reforms.

The second component of the current reform relates to investments. At the moment, even though retirement savers

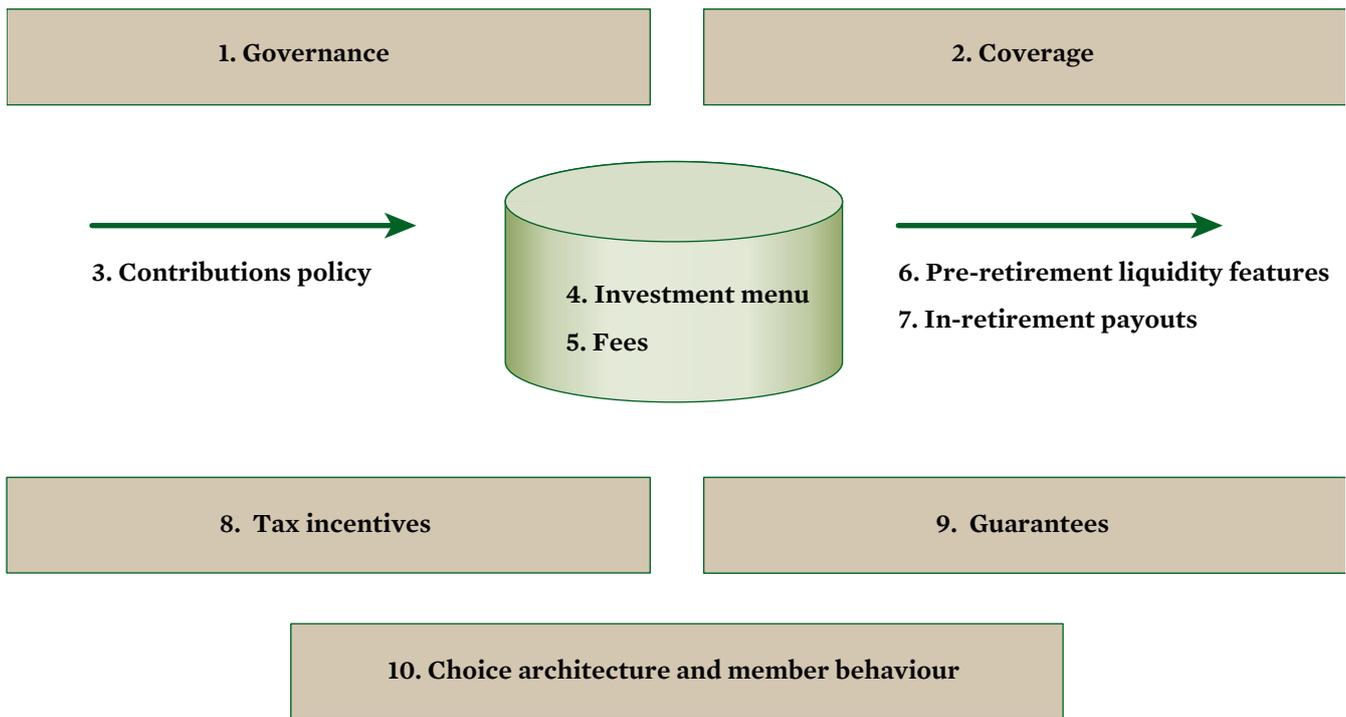
hold assets for the long term, 60 percent of assets are in deposits; insurance; and low-risk, low-return products. DC participants must be able to invest properly for the long term. One way to address this issue is to offer diversified default products. This particular idea will be discussed in more detail in the second panel.

In future reforms, we will need to increase our contribution limits. The contribution limits in Japan are low, which makes it difficult to build enough assets for retirement.

I am hopeful that the Japanese reforms will work, particularly in light of the US experience with 401(k) plans and IRAs [individual retirement accounts]. There

FIGURE 3.1

Factors to Consider When Designing a DC System



Prepared by: Stephen Utkus, presentation at the 2015 Global Retirement Savings Summit (Tokyo, Japan)

are similarities between where the United States used to be in the 1970s and 1980s versus where we are today in Japan. In the 1980s, public social security reform took place in the United States. At about the same time, IRA eligibility was expanded and 401(k)s grew. So that is an encouraging lesson for Japan.

The US experience with asset allocation in IRAs is also telling. Many Japanese think that Americans have been investing in mutual funds for decades, but that is not the case. IRAs used to be mainly invested in deposits, but changes took place in the 1980s and 1990s, and more assets began to flow into mutual funds or marketable securities [Figure 3.3]. So I think the Japanese

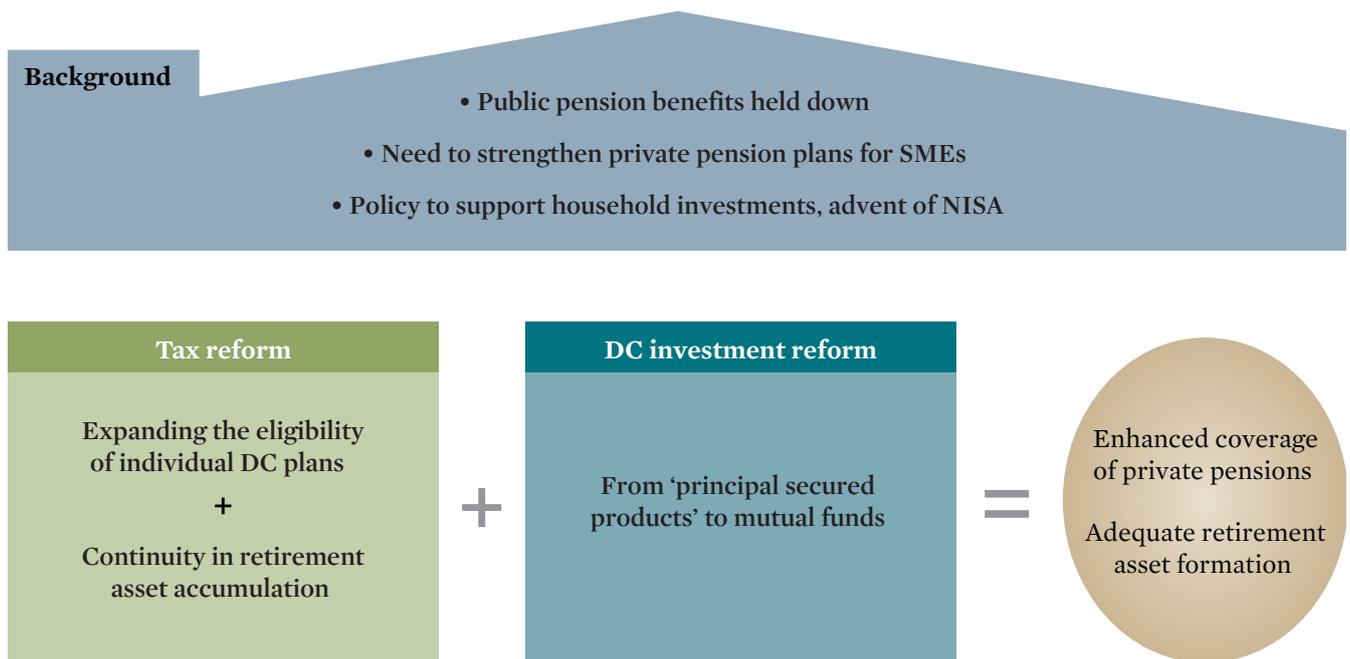
DC system, through various institutional reforms, can change significantly.

Utkus: In the US retirement system, there's a first pillar social security system provided by the federal government and financed through taxes [Figure 3.4]. The second pillar is a workplace system that was previously dominated by DB plans, but now, for private-sector workers, is the 401(k) system. It is a voluntary system; neither employers nor employees are required to contribute to these plans. And 401(k) assets now total \$4.3 trillion, with more than 80 million accounts.

The unique thing about our third pillar, which encompasses IRAs, is that a

FIGURE 3.2

Overview of DC Reforms in Japan



Source: NICMR

Prepared by: Akiko Nomura, presentation at the 2015 Global Retirement Savings Summit (Tokyo, Japan)

substantial portion of IRA assets are transfers from 401(k) accounts. In the United States, when you change jobs or retire, you can take your entire savings from your 401(k) plan and move it to an IRA at any regulated financial institution in the United States. So the 401(k) and IRA systems are complementary.

The size of the retirement marketplace is quite substantial. It's currently at 23 trillion dollars. In the United States, as Akiko mentioned, we have very generous tax incentives. For example, if you're younger than 50 in the United States, an employee can contribute on a pretax basis up to 18,000 dollars of his or her own salary, which is equivalent to 2.1 million yen.

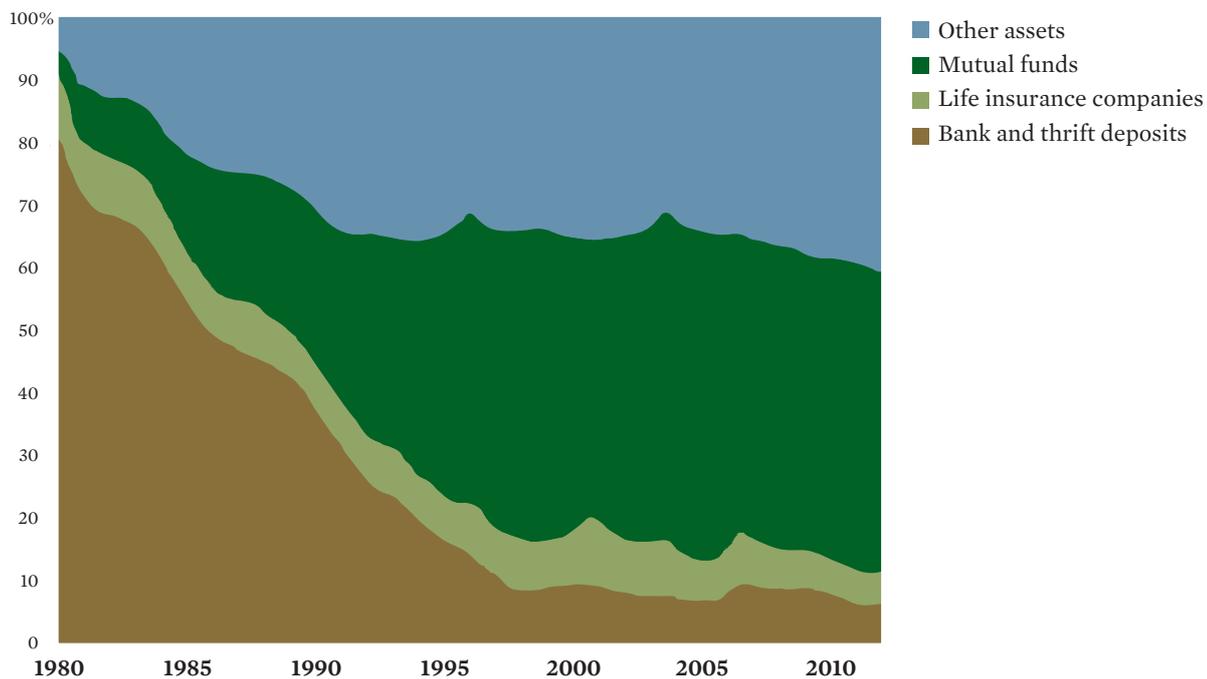
There's also a higher limit for individuals who are older than 50. And these are only employee contribution limits. There are separate and higher limits for employer and employee contributions combined.

The other thing I want to focus on is the significant policy change made in 2006, which adopted the principles of behavioural economics in pension plan design and introduced both automatic enrolment and default investing into retirement plans. The idea behind the default savings and investment approaches is that too few people contributed in a meaningful way, and when they diversified their portfolios, the portfolios were not professionally diversified.

FIGURE 3.3

Shift from Savings to Investments in IRAs

IRA investments started mainly in deposits. They shifted to mutual funds and other assets during the 1980s and 1990s.



Sources: ICI and NICMR

Prepared by: Akiko Nomura, presentation at the 2015 Global Retirement Savings Summit (Tokyo, Japan)

So let's start first with automatic enrolment. In a traditional voluntary system, the employee decides how much to contribute. In an automatic enrolment programme, the employee, upon joining the company, receives a notice saying, 'You are hereby automatically enrolled in the retirement plan at a certain percentage of pay. You can quit if you want to.' What we overwhelmingly see in these plans is that individuals tend to stay in an automatic enrolment plan. Let's discuss the particular populations who are least likely to save, which are young and low-income workers in the United States. Data show that automatic enrolment substantially increases the fraction of people who participate among these lower-wage groups. For example,

for employees younger than 25, automatic enrolment raises participation rates from 29 percent to 68 percent. And when you apply this pattern to the overall population, the effects of automatic enrolment are even higher.

Now, in the United States, automatic enrolment is a voluntary programme, which employers can choose to adopt. About one-third of all plans and half of all large companies have adopted an automatic enrolment programme. As a result, about half of all US workers with a 401(k) plan are in these arrangements.

The other question, of course, is if you're going to automatically enrol an employee in

FIGURE 3.4

US Retirement System Today (Private Workers)

<p>Social Security</p>	<ul style="list-style-type: none"> • OECD pillar 1: compulsory, 90 percent + coverage • PAYGO system: 12.4 percent payroll tax (split employer/employee) • Inflation-adjusted annuity; progressive benefits structure
<p>401(k) (DC) plans</p>	<ul style="list-style-type: none"> • OECD pillar 2: occupational, voluntary, 50 percent + coverage • Employee contributions as main funding • Lump-sum distributions (including to IRAs) • \$4.3 trillion • More than 80 million accounts
<p>Individual retirement accounts (IRAs)</p>	<ul style="list-style-type: none"> • OECD pillar 3: tax-advantaged household savings • Mostly funded from 'rollovers' from 401(k)s and DB plans • \$6.6 trillion

Prepared by: Stephen Utkus, presentation at the 2015 Global Retirement Savings Summit (Tokyo, Japan)

a pension plan, how should the employee's assets be diversified? As Akiko pointed out, there was a substantial structural change 20 years ago in the United States, in which workers began to hold more equity-oriented portfolios for retirement. However, one of the problems with those portfolios is that they tended to be weakly diversified. For example, participants would hold short-term cash deposits and not bonds. They would hold one equity mutual fund, not a diversified portfolio. As a result of the change in the law in 2006, the government has encouraged employers working with asset managers to establish diversified default portfolios.

Now, overwhelmingly, employers have chosen target date funds for these defaults, and Vanguard has data that show the growth of target date funds in the United States [Figure 3.5]. According to our data, virtually zero individuals held their entire portfolios in a single target date fund in 2004–2005; now it's about four in 10 participants. Then there are those who are defaulted into a target date fund, but who also add another type of asset or fund to that balanced strategy, which is nearly two-thirds of all investors. We forecast that within five years, the substantial majority of all 401(k) investors in the United States will no longer be making portfolio choices, but will be investing

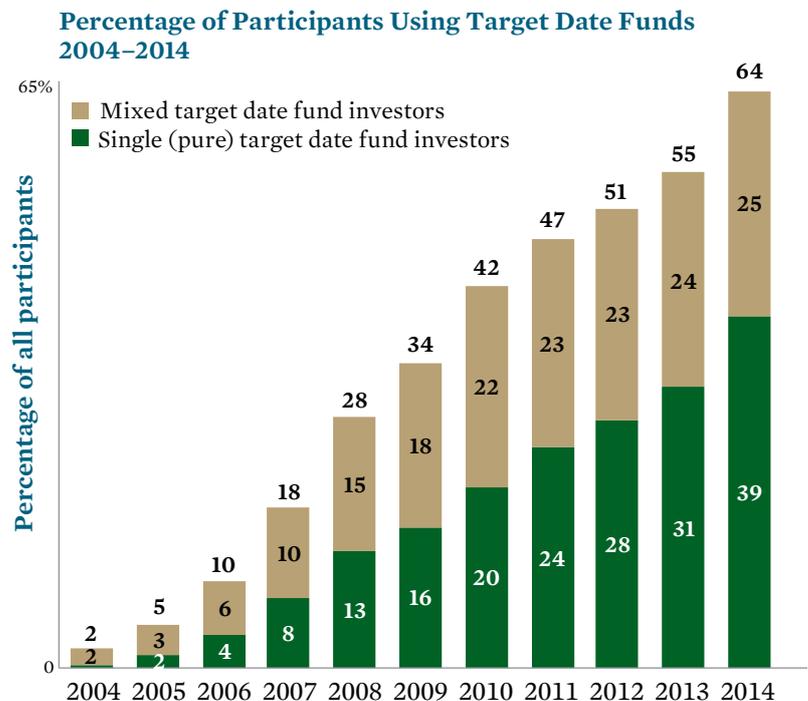
FIGURE 3.5

The Rise of Target Date Funds

Target date fund (TDF) adoption

- Participant use of TDFs is the result of both plan default (automatic enrolment) and own choice (voluntary enrolment)

NOTE: Investments in target date funds are subject to the risks of their underlying funds. The year in the fund name refers to the approximate year (the target date) when an investor in the fund would retire and leave the workforce. The fund will gradually shift its emphasis from more aggressive investments to more conservative ones based on its target date. An investment in a target date fund is not guaranteed at any time, including on or after the target date.



Source: *Target-Date Fund Adoption in 2014*, Young, 2015.

Prepared by: Stephen Utkus, presentation at the 2015 Global Retirement Savings Summit (Tokyo, Japan)

in target date funds designed by professional investors or in other asset allocation strategies available in the United States.

There are two other issues I want to highlight. First is the question of coverage: who is in the private DC system? In the United States, among large firms—large being 100 or more employees—roughly two-thirds of workers are both offered and participate in a plan. But among small firms, the fraction is substantially less. This is a well-known phenomenon among voluntary systems in other countries. It's the small-and medium-enterprise problem. In the United States, there have been a number of proposals. One is to create a multiple employer plan where small employers can join together in a single plan. Let's call it the 'Vanguard Small Employer American 401(k).' And there have been proposals that individual states within my country create their own plans. That is its own headache, because there are 50 states, which means 50 different state-run retirement programmes. Then there have been proposals for a universal pension system like ones in the United Kingdom, Australia, and other countries.

Finally, another question: as DC systems mature, how are assets going to be translated into a regular income stream during the decumulation or retirement phase? There are programmes in the United States and in other countries, from the regulatory side, designed to encourage lifetime income programmes. Although there's a lot of interest in annuitisation, consumer and employer demand for annuitisation remains low. One of the most interesting developments in the private market is the development of income-management services, where

technology and sophisticated algorithms are being used to help people guide the draw-down process. For example, Vanguard offers such a service, based on a participant's age and portfolio allocation. This service gives the participant a recommended monthly income to withdraw from his/her account, which is designed to ensure that his/her income will last for a long time.

Tim Jones: Good afternoon, ladies and gentlemen. It's a great pleasure to be here. When I became involved in pensions, the policy debate that I will now briefly go through was largely concluded. But I want to spend a few minutes talking about that policy debate to give you a sense of the challenges that the United Kingdom was facing when it adopted the National Employment Savings Trust [NEST]. The debate happened in 2005 and 2006, and it was driven by a Pensions Commission made up of three people: Lord Adair Turner, drawn from the centre right; Jeanie Drake, drawn from the centre left; and Professor Sir John Hills, an academic from the London School of Economics. The Pensions Commission was a Tony Blair initiative, the purpose of which was to create a commission that would command respect across the political landscape and that had a strong intellectual underpinning. And I think most people in the United Kingdom believe the commission did a great job. It issued its report in late 2004 but, of course, its recommendations were then debated in detail in 2005 and 2006.

So here we are then, after that commission and with its recommendations, which I will come to. What was the policy context [Figure 3.6]? Well, the good news is that we are all living a lot longer, and the bad news

is that we are all living a lot longer. That means we are trying to make our retirement savings last to when we are 98 years old and beyond. It's not that there are three or four years after work. For many people, there are 20, maybe 30 or 40 years. And although retirement ages around the world are shifting, the ratio of working adults to retired adults is changing adversely. So that's the first context, which is shared by Japan, the United Kingdom, and by many other countries.

Now, the second problem was unique to the United Kingdom. It had created a very complicated first pillar of public pension provision. It also was not very generous, and it had gradually become less generous over time. So more people were looking forward to a longer retirement in which pillar one was not going to do as good a job

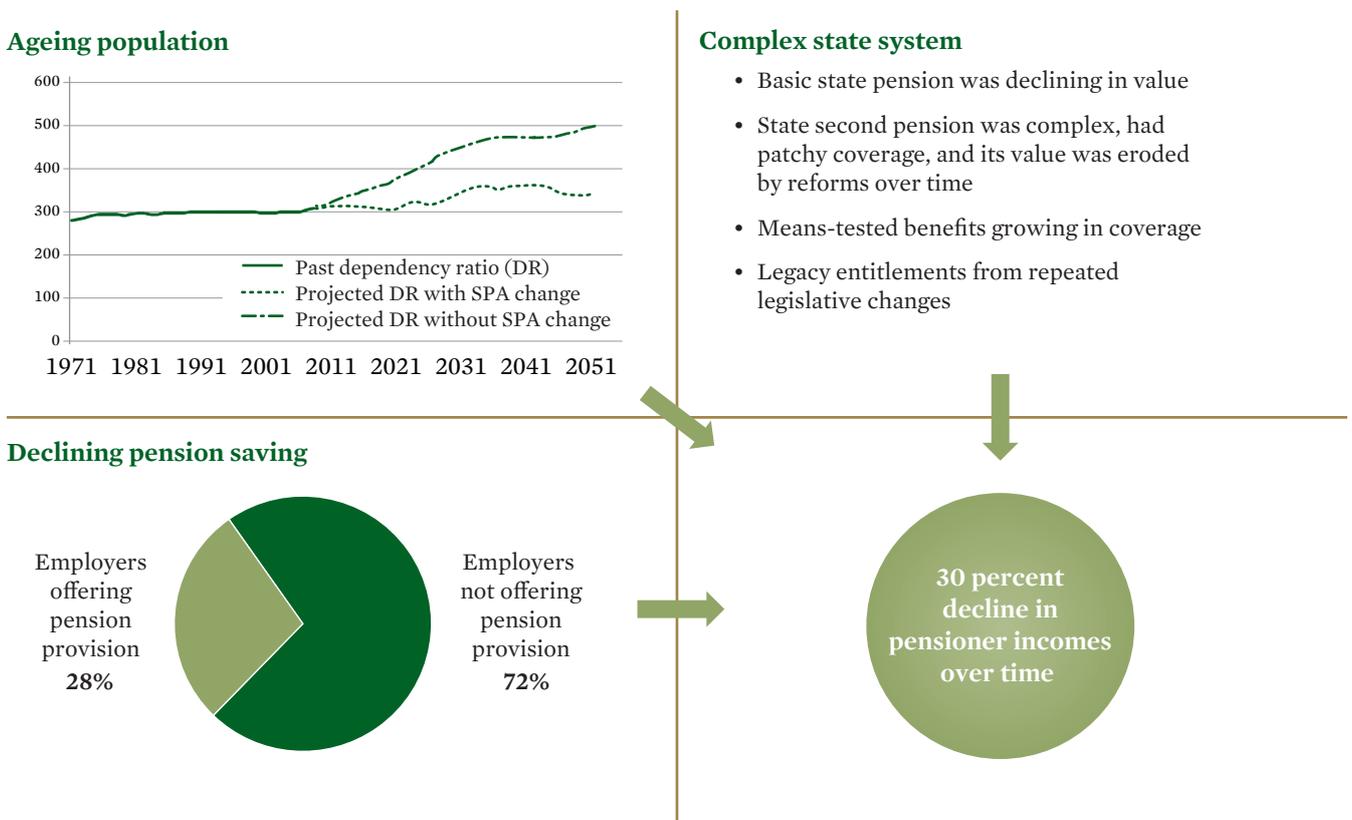
of securing their retirement income. Thus, something had to be done to simplify the first pillar.

Now, Steve just mentioned this third problem, which is often shared around the world. Major corporations and public bodies tend to be quite good at providing pillar two retirement coverage, or workplace pensions. Smaller firms are not as good, whether it's a mom and pop in America, a hairdresser's business in London, or a small business here in Tokyo. The workers in those firms typically do not benefit from a workplace pension.

And in the United Kingdom, with pillar one being weak, this was a particular problem. Together, these problems led to a risk that there would be, if nothing was done, a significant pension problem in years to

FIGURE 3.6

Context of UK Pensions Policy in 2006



Prepared by: Tim Jones, presentation at the 2015 Global Retirement Savings Summit (Tokyo, Japan)

come, with perhaps a 30 percent decline in incomes over time. So something had to be done. The Pensions Commission was very clever. It said, 'Okay, we now understand what is driving the challenge. As a society, what do we want to do about it? Well, here's something we can do. We can just tax the smaller working population to fund a better pillar one for everybody.' But the tax implications of that were frightening, because that smaller number of workers was going to have to pay more and more taxes to support the growing number of retired people.

The second way of fixing this problem was to encourage more private saving so that those workers who were getting older would bring the wealth that they built during their working life into their later life. And this was seen as a strong option. The third thing you could do was to push back the age at which people retire, and that would apply both to pillar one and pillar two.

Of course, the fourth choice was that we could just have poorer pensioners, but you won't find a politician willing to sign up to that fourth choice. So the commission was basically able to go round the circle and say, 'Okay, what are we going to do: higher taxes, more savings during the working life, or push back the retirement age? You don't like any of those? Okay, poorer pensioners.' 'No, we don't want poorer pensioners!' 'Okay then, what do you want?' These were uncomfortable but inevitable choices, and I think the commission framed the debate very elegantly and simply said, 'We just have to decide.'

So these challenges led to a series of recommendations from the commission, and there were two main recommendations. The first was to reform pillar one by stopping it from getting any worse by simplifying it and removing a lot of the means-tested benefits that were a feature of the pillar one system. The problem with

the means-tested benefits was that they made it very difficult to make the case for people to save in pillar two, because if you had pillar two savings, your means-tested benefits went down. And if you didn't have them, you got the means-tested benefits, so why save? So the reform of pillar one was very important because it created a baseline pension, which is not a very high amount. It's about 145 or 150 pounds in 2013/2014 money. It technically will take people above the poverty line, but not by very much, and people recognised that this level of wealth would not meet the aspirations and desires of most of the workforce.

The second recommendation that was accepted and is being implemented was to significantly reform workplace pensions, which is what I'm going to talk about now. How do you significantly change the actual level of savings in the workplace across society? The answer was automatic enrolment, but there was a challenge: how do we handle coverage for workers who are not paid a high amount or who have broken work experiences? People with broken work experiences are those who work for a while, then don't work, then come back to the workforce, leave again, and then maybe work part-time. Viewed from the private sector's perspective, this was not an attractive group of people. But viewed from the policymaker's perspective, this was a critically important group of people. So the government came up with two ideas, and the commission laid these out. The first was to divide the less attractive business between private providers, and the second was to create a pension plan that would have a legal duty to provide a pension for any sort of worker from any sort of employer. The Pensions Commission went for the idea that the government should create a plan that would have a duty to say 'yes' to any employer, regardless of how financially unattractive or attractive the business was. And the other option was some kind of sharing of the less attractive business.

This debate, called model choice, happened in 2006 [Figure 3.7]. The government decided that the commission was right and that the answer was that the government would create a pension plan that would be principally used in the private sector and a pension plan with a statutory obligation to say ‘yes’ to any employer that wanted to use it. The government then became even cleverer and decided they would get some idiot from the private sector—whose fault it would all be if this went wrong—to build and lead the growth of this pension plan, and you are looking at that idiot. I was hired in 2007 to build a pension plan that would serve roughly five million people from half a million employers. The employers are being subjected to the new automatic enrolment obligations in stages, beginning with 2012 for the biggest UK employers and by 2018 for all employers. The coverage is so deep that even if you are a parent employing a nanny to look after your children, you are technically an employer, and you are caught by these obligations. And so that’s why we believe we will have half a million employers in NEST by 2018. No employer *has* to choose NEST, and *any* employer can choose NEST.

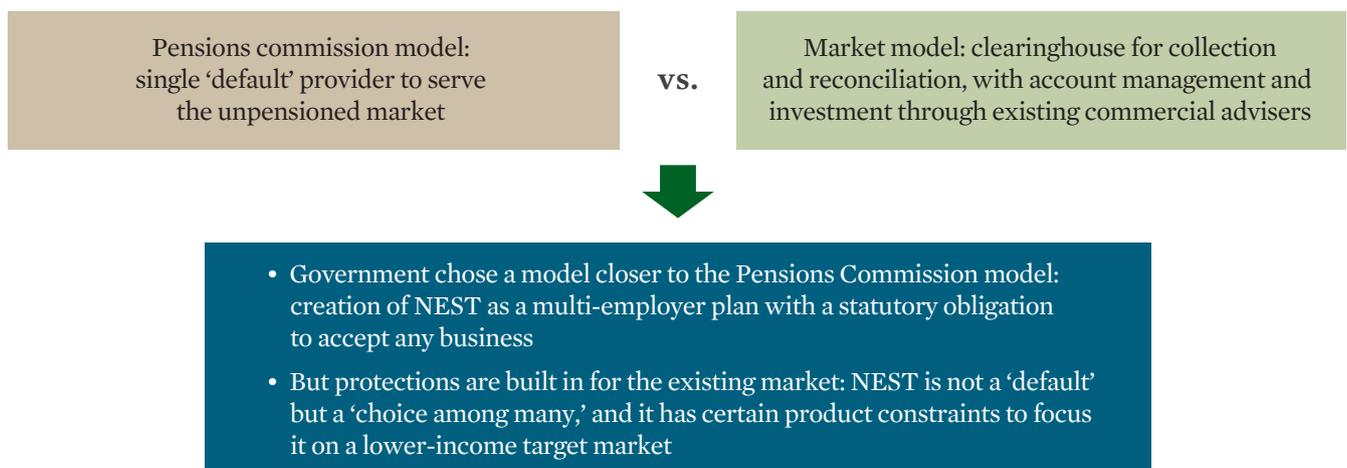
So that’s what NEST is. All of that was settled in 2008–2009, and we built it. There was a change of government, a centre-left government replaced by a centre-right coalition, and the coalition has continued with these reforms. The commission did a great job of building a consensus that has been sustained as politics have taken their course. But there were a number of very important issues which, as we came to the roll out, needed more work. And in hindsight, perhaps the right choices were not made for some issues. So the policy people got very complicated about who should be ‘in’ and who should be ‘out,’ and there is an argument that it would have been better to have a simpler solution. But I have now said to the government, ‘Don’t try to simplify it halfway through the rollouts. Let’s do the rollouts, pause, and then there will be a review of the policy in 2017.’

One issue is that the employer is choosing a scheme, and the employer says, ‘I’m a plumber. I’m a hairdresser. I run a restaurant. I’m a scaffolder. I’m good at that. I don’t know anything about pensions. It’s crazy that you are asking me to choose a scheme.’ So there’s the concept of a

FIGURE 3.7

‘Model Choice’ Debate

What should the ‘supply-side’ intervention look like?



Prepared by: Tim Jones, presentation at the 2015 Global Retirement Savings Summit (Tokyo, Japan)

qualifying scheme, where the employer will be okay if it chooses a qualifying scheme. Another issue revolves around all of these workers coming into a scheme. If they only stay in their job for six or nine months, there's a little pot of money that's created because the employer has to put the worker into a scheme within three months of the employee joining the firm. So we need a way of making these small pots come together. But unlike banking, the pensions industry does not have a low-cost transfer mechanism. So we are now discussing how we can design and build a low-cost transfer mechanism to consolidate the millions of tiny pots that are being created as this policy rolls out.

In March 2014, our chancellor of the exchequer changed the way in which DC pots are turned into a retirement income in the United Kingdom. We had a compulsory system that required most DC plan participants to purchase an annuity. They had to put 75 percent of their pot into an annuity and could take up to 25 percent as a tax-free lump sum. That requirement was abolished in April 2015, and now it's called the Freedom in Choice Agenda, which has opened up a new and lively area of policy debate in the United Kingdom.

Utikus: Thanks so much, Tim, for your discussion and we look forward to continued discussion about the features of NEST. I now have a question for Akiko though. One of the interesting questions in Japan is the size and scale of contributions in DC plans. And a unique feature in Japan is the notion that an employee can only contribute up to the size of the employer contribution. What was the historical reason for this 'I can only contribute up to what the employer puts in?'

Nomura: The short answer to your question is we originally only had DB systems first, and DB plans are based on employer contributions. The DC system was added later, but we followed the same pattern. The employer's contribution always

comes first, because it's an employer-provided corporate pension. Afterwards, the employee contribution was added on. Thus, because it's an employer-provided system, employee contributions are only up to the employer's contribution.

However, we are making proposals to abolish that ceiling. Also, the introduction of an individual DC plan is part of the answer to this issue, because employees in corporate DC plans would still be able to make additional contributions to their individual DC plans. Also, I would like to point out that at the moment, the focus is more on how to increase coverage, and an individual DC plan would do that. I actually would like to ask both of you a question though. Expanding eligibility is one thing. The next issue or challenge is how do you make people take advantage of this opportunity and join individual DC plans? Because we are not going to force them. So what are your thoughts coming from the voluntary system? Also, what is the response so far from employers and employees who have been automatically enrolled into the new system?

Utikus: The behavioural economics are clear in that you need to set up an automatic payroll deduction in some way. There have been a variety of proposals in the United States to create various types of voluntary saving schemes for households who don't have workplace plans. Those are important as supplemental, pillar three programmes. But if you want to deepen coverage in a substantial way, the question becomes, how do you connect people's wage income to automatic contributions? I think that seems to be one way to maximise coverage.

Jones: Each of our countries is very different, and you have to work within what will be culturally acceptable. The first thing that the United Kingdom tried before the Pensions Commission—so in the late 1990s and early 2000s—was called 'Informed Choice.' The thinking was that we would put these workers in front of a financial adviser who would tell them how good

joining a pension is, and they would join. They would go in front of the adviser and come out of the meeting saying, 'I've seen the light! I will join the plan.' But they didn't.

Each of our countries is very different, and you have to work within what will be culturally acceptable.

—Tim Jones

Pensions are one of the most difficult products in the world to sell because of another concept in behavioural economics, which is called hyperbolic discounting. That is a complicated way of saying that people massively discount a benefit that won't arrive for some time. So you're 25 years old. Great news. Buy a pension! 'When do I get my money back?' 'When you're 70 years old.' 'No.' It's the worst product in the world to try and sell to ordinary people who've got things to do with their money, so automatic enrolment—not compulsion—was seen as the only way of creating the desired amount of coverage. Compulsion has worked well in many other countries, so why not in the United Kingdom? Well, the answer was, 'It's a tax!' As soon as you make it compulsory, the press leap on it as a tax. So automatic enrolment was seen as a culturally appropriate way to bring people into a workplace pension, but to say to them, 'You can jump out if you want. It's not a tax. It's not compulsory. You're being put in, but you can jump out.' What we found is that when nobody is in the plan and you allow them to join, 30 percent join. But when everybody is in the plan and you allow them to jump out, 30 percent jump out. Same people, same amount of wealth, and same attitudes, but you shift the dial from 30 to 70 percent by changing the frame in which you're deciding. So far in the United Kingdom we have 92 percent staying in. So 30 percent has gone to 92 percent.

It's early days. Our contribution rates are being phased in. Now it's only 2 percent. It's tiny. So we may have a different experience as the contribution rates go up. But what appears to be happening so far is that for people who would never join a product when faced with the opportunity to come in, there seems to be a small voice inside those same people saying, 'I think this probably is the right thing to do, so I'm going to stay in.' Thus, we believe that automatic enrolment is a very powerful way of achieving coverage.

Utkus: Excellent. Thank you. We have an interesting question from the audience about developments in fees and fee structures.

In the United States, there have been two parallel developments in fees. On the regulatory side, there have been two substantial reforms. In the pension world, there has been a shift towards disclosure, a major disclosure effort to improve both employers and employees' knowledge of fees. Then, in the retail retirement world, the world of IRAs, there's been a growing emphasis on a different model of financial advice. For example, advisers use low-cost exchange-traded funds and then wrap that with advice, which is a more transparent model of providing investment advice to retirement investors in the retail market. So there's been a meaningful change in the United States and in other jurisdictions about disclosure of information in terms of fees and pensions, as well as retail retirement products.

The other thing is the growing use of indexing and passive strategies to lower the cost of investing. So that's a quick synopsis of what's been happening in the United States, and I'd be curious to get your reactions, both from a Japanese perspective and UK perspective.

Nomura: As far as DC plans in Japan are concerned, the level of fees tend to be very low because of competition. So, actually, it

tends to be a very good deal for the same person. If he or she is thinking about investing in the same type of mutual fund, then as far as fees are concerned, investing through a DC plan is much better deal.

Jones: In the United Kingdom, the media is very active. We are very proud of our free press. But the media is very harsh in its criticism of bad practices. Fees are the subject of a large amount of debate, and I'd like to make a couple of remarks. First, a DC plan is a very different from a DB plan. In a DB plan, the member doesn't care what the fees are. It's the employer paying them. The employer has made a contractual commitment to pay a stream of retirement income. Why should I bother about whether the employer is getting a good deal? It's his business. In a DC plan though, suddenly it's:

This is my money! How much are you charging me? Are those all the fees, or are you hiding some? What about my performance? Is the performance any good, or are you just rubbish at your job? Because it seems to me that you financial services types take out a lot of money whether the market goes up or down. I'm the person that suffers, so I want to know what you're doing with my money.

So a DC plan brings in a world of greater transparency and scrutiny, but prospectively it's a massive market. But it's not a market that is really that much different from selling a variety of other products to consumers. Holidays, cars, telephones, televisions—people want to know that they're getting value for their money. They want to know that the people managing their money are doing a good job, and that they're being fairly paid but not overpaid. Now, in the United Kingdom, this has led to legislation to reduce or cap the fees in workplace DC plans, and you have to do the job for less than 75 basis points.

The other thing is that there is an interesting second dimension to the presence of NEST. NEST is a government intervention in a private market. We sit alongside Legal & General, Standard Life Savings, and a variety of other players in the market. No employer has to use us, and any employer can use us. But we behave extremely well under UK trust law, and we do the very best job we can. So that's another approach. You can regulate markets, but if as a government you place a provider in a market that is tasked with transparently doing the best job it can, then there's a question about whether that is also an interesting and maybe effective way of creating good outcomes. Certainly our price, which is equivalent to 50 basis points, seemed to have a significant impact on the prevailing prices across the providers of workplace pensions.

Utkus: My next question is about the relationship between financial education and behavioural economics. Yoshino-san made a fairly forceful statement about the role of financial education and DC and retirement savings. As many of you know, there is a substantial body of research literature emerging around the world that most households in North America, Europe, and Asia can't respond to three basic financial literacy questions about compound interest, inflation, and diversification. It's very famous research on financial literacy. So we need to improve financial literacy in the schools. Yet, on the other hand, we just talked about the role of defaults in pension plans and said the better choice, at least with respect to retirement plans, is to default people into choices that they're not really educated about. They're informed about them, but not necessarily educated about them. So I'll pose this philosophical question. Which is it: education or behavioural economics? Are they at odds with one another or are they complementary?

Nomura: At the moment, in Japan, the financial literacy debate is a very big issue, as Professor Yoshino pointed out earlier. And, actually, DC plans are seen as a very important platform for providing investment education for working people. Investment education should not just be in schools anymore. It's important to have a good curriculum for students, but what about the people who already finished school? We have to think about them as well, and in DC plans, employers are required to make a good effort to provide financial or investment education to DC participants. So it's going to be a very good platform for providing basic financial and investment knowledge.

[In Japan,] DC plans are seen as a very important platform for providing investment education for working people.

—Akiko Nomura

Further, as part of our DC reforms, we are going to introduce something very similar to a default product. This means that we are aware of the global trend, and we are trying to import something that is not only good for Japan's DC system, but also for Japanese employers and employees. So we will have both: national literacy and a default product for DC plans.

Jones: So the evidence in the United Kingdom was very clear: most people in the United Kingdom think pensions are very dull, and they are scared of investing. They can see all those computers at Goldman Sachs and Morgan Stanley, and people know they are designed to take money off of them and they don't fancy their chances. So the attitude of the man on the street in the United Kingdom will be to say, 'It's your job to do this investing business. When I go into a garage to buy a Toyota or a Nissan, they don't sit me down and say, "Well, it's very important that you

learn how to design the engine and the braking system. After all, this has to be a safe car. It has to perform well. It's your job. You're the person driving the car. It's your job to design the car.'" It's ridiculous. It's Toyota's job or Nissan's job to design a car that's safe and the government's job to ensure, via regulation, that cars meet a minimum standard of safety. UK consumers take exactly the same view. They say, 'I'm a hairdresser. I work in a restaurant.' In one piece of video, we had a medical student waving *Gray's Anatomy*, which is a very big textbook of medical knowledge, saying, 'I've got enough to learn. I don't want to learn about your world of investments. It's boring. It's your job to do that for me, and I will be very cross if you do it badly. But don't expect me to do it. I don't even know what this word "diversification" means in this context, and I have no desire to learn.'

Utkus: So, Tim, I think that's right. However, one of the fundamental issues that's emerging in the United States is the recognition that while you can put the pension product, or the DC plan, on automatic, there are a wide range of financial choices in your life that are not automatable and that will ultimately affect your retirement security. I can't put you on autopilot with credit cards, bank loans, or personal savings. If you buy too big a house, you're going to be poor in retirement. If you spend too much on your children, maybe you'll be rich from your children, but there are a variety of financial choices that are not automatable.

It seems to me that while the consensus is that the pension system should be automatic, increasingly our smartphones are going to help people manage these other financial decisions. So I think these digital platforms and other kinds of robo-advice that Yoshino-san referred to have the potential to complement pensions.

Jones: I completely agree. My slightly comedic approach to this is really about the fiction that you can turn ordinary people into investment professionals capable of doing asset allocation. In the United Kingdom, there is no chance. But what do you do with this wealth? I mean, you're completely right. The family circumstance, the household circumstance is absolutely specific. Do you have a partner? Do you have outstanding debt at the point of retirement? How wealthy are you? How much risk can you take with this piece of wealth compared with other pieces of wealth you have in your household? We will not try to teach our plan participants to be investment managers, but we will over a period of decades—from their forties, when they start to get interested, through their fifties and sixties—say to them, 'Look, we're building up a substantial pool of wealth here. So let's talk about what is right for you, in your circumstances, so that we can get the best value out of this pool of wealth that we are building on your behalf.' So in that broader sense, if that's financial literacy, I completely agree.

Nomura: I agree. And also, yes, adding financial planning for your lifetime is an important element to the Japanese DC system.

Utkus: Yes, there seems to be a worldwide consensus on doing something in schools. In the United States, we have algebra and these type of math problems that say, 'One train leaves San Francisco at this speed. Another train leaves New York at this speed. Where will they meet in the middle of the United States?' There has been this discussion, however, that instead of doing math problems like those, we should do compound-interest and risk-return calculations. We have only a few minutes left, and I want to give each of you at least one

minute to highlight the issues surrounding postretirement.

Jones: So the legislative changes in the United Kingdom really opened up the debate about what to do with this wealth. You can take cash; you can have some form of a drawdown; you could buy a hard guaranteed product; or you could go into some pool with soft guarantees, with the intent to create a revenue stream but with no actual contractual guarantee to create a revenue stream. So we have these four things that you can do with your wealth, and right now we are in the middle of a very lively debate about these options. In addition to deciding what's right for you and your family's circumstances, we need to get people to engage with the pros and cons of each of the four options, and it's a long journey.

Nomura: Given that Japan's DC system is young—it started in 2001—there has not been significant debate about how to decumulate funds within the DC system. However, it might be changing, because many people have been accumulating a certain amount of funds within the DC system. Also, one important thing to remember about the Japanese retirement benefit system is that we are a lump-sum culture. Most people receive a lump sum of money when they retire, and I think this issue is going to gain more importance and attention in Japan.

Utkus: It is an important issue, and one that will conclude our panel. There's a lot to talk about when it comes to postretirement drawdown. For example, in America, Australia, Canada, the United Kingdom, and elsewhere, there's an active debate about the decumulation phase and how to successfully translate assets into income and at a low cost. 🌱

PANEL 2

Investment Diversification and Long-Term Savings: Default Funds and Beyond

PANELLISTS

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United States

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Managing Director, Japan Country Executive
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United Kingdom

JOHN REKENTHALER
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The success of DC systems depends on many factors, including participation rates, contribution rates, and investment strategies. In this session, panellists from Japan, the United Kingdom, and the United States discussed how behavioural economics has helped create new tools that have addressed some of the issues facing voluntary DC systems. Some of those tools include automatic enrolment and target date funds, and the panellists highlighted the differences in how automatic enrolment and target date funds could be structured by contrasting US and UK experiences. The session also examined Japan's growing need for a more robust DC system, with broader coverage, higher contribution rates, and access to more diversified investment options.

The following is an edited transcript of the discussion.

David W. Monroe: During this panel, we're going to discuss investment diversification and long-term savings, as well as the use of default funds. Each panellist will take a turn speaking and then we'll have a period for questions and answers.

Tim Jones: I'm going to briefly talk about NEST's default investment approach. First,

I would like to highlight a big cultural difference: NEST runs under trust law, which is very old. It goes back roughly to the 12th century, when people went off to fight in the Crusades. The knights that went off to fight in the Crusades were very wealthy people. They had significant assets—land, farm animals, staff—and somebody was appointed to act as a reasonable manager

of those assets while the knights were away fighting for years. So that's the root of English trust law.

So our job, managing other people's money under trust, is to do what a reasonable man or woman would do with that money. We're not required to guarantee that the principal amount invested is returned intact. We just have to do a reasonable job of managing those assets for those people, and that was a very important driver of our approach towards designing the default strategy for NEST. First we went out and asked our target market about investing. We defined our target market as people earning up to 35,000 pounds [US\$50,000]. These are not people who are remotely interested in or competent in investing. There is no history of these people having a stock portfolio. There is more of a history of that in the United States. The United Kingdom does not have that, apart from people buying into government privatisations as things were denationalised. That's the only stock this group traditionally holds.

So we asked our target market about investing, and this is what they said:

Look, you know, this is your job, okay? It's my money, but it's your job to act as the reasonable person to look after it. So don't expect me to be interested. I'll blame you if you get it wrong, but I'm not interested in it any more than I'm interested in designing the engine for the car I'm going to buy. It's the car manufacturer's job, not mine. I'm a consumer here. I do what I do, but I don't do anything else. But it is my money, and big ups and downs worry me. So I'd really like it to be kind of safe here, because I'm doing a safe thing. I'm saving for my later life. I'm not interested in playing the stock markets like those guys in the city. I don't like them, and I don't trust them. I'm trying to be safe here. So big ups and downs are going to trouble me. And of course I want it to be low-cost, but I want value for my money. I don't want it to be cheap and nasty; I want it to be cheap and great.

About the panellists

David W. Monroe is general counsel at Matthews International Capital Management, LLC. Before joining the firm in 2014, he served as senior managing director, chief legal officer, and cochair of the Global Risk Control Group for Nikko Asset Management Co., Ltd. in Tokyo. Earlier in his career, Monroe led the legal and compliance functions for several large asset management group companies in Japan.

Douglas L. Hymas is Japan country executive for BNY Mellon in Japan. Hymas has worked in Japan since 1991 and has been active in the American Chamber of Commerce in Japan. A California-licensed attorney, Hymas worked as a legal specialist with Lehman Brothers from 1995 and with Barclays Global Investors from 1998.

Tim Jones is CEO of the NEST Corporation. He has substantial experience in the financial sector, having previously held a variety of senior positions including non-executive director of Capital One Bank (Europe), chief executive of retail banking at NatWest Bank, and chief executive at Mondex, Purseus, and Simpay.

John Rekenhaller is vice president of research for Morningstar, Inc. He joined Morningstar in 1988 and has served in several capacities, including overseeing Morningstar's research methodologies and leading thought leadership initiatives such as the *Global Fund Investor Experience* report. He currently writes regular columns for morningstar.com and *Morningstar Advisor* magazine.

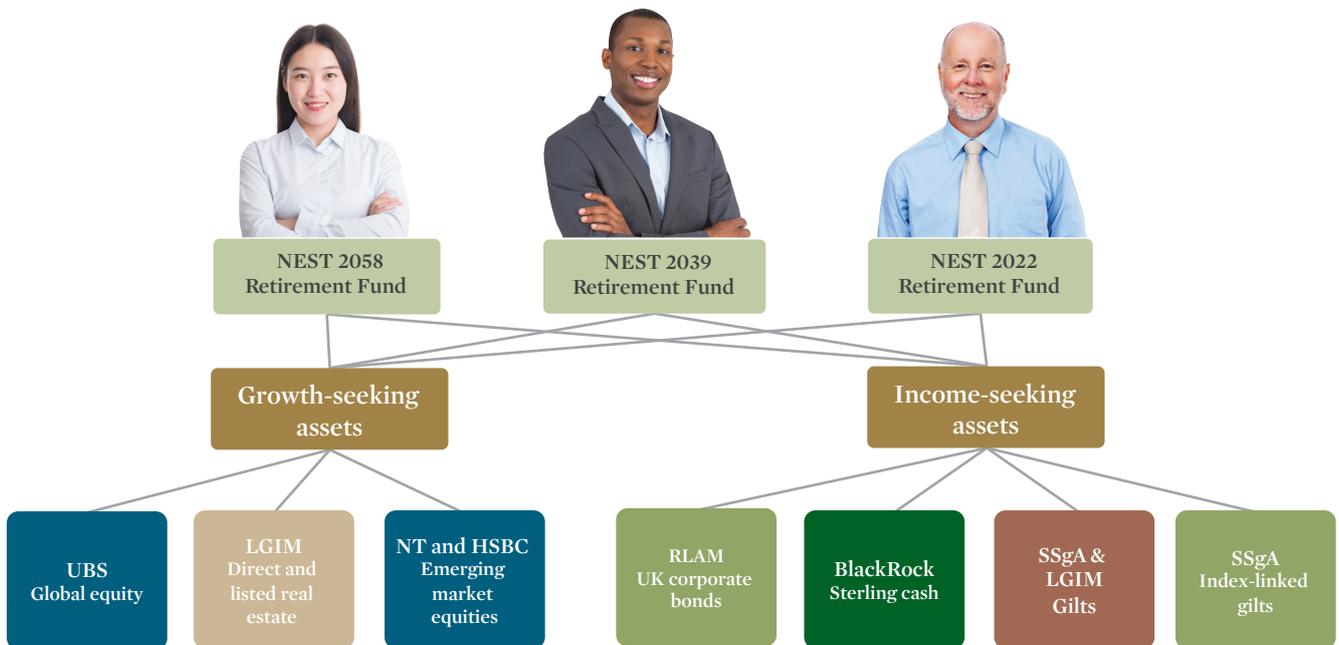
So that's what they asked for, and we knew that we would have volume. We are designed for about five million members, and we could do 10 million. But we are built, we think, for around five million members by 2018. So we then had to design a default option against that scale. We looked for a way of carefully managing these people's money, and we looked at target date funds as the best approach. We looked across the pond to North America, found target date funds, and said, 'Yes. That looks like the right approach.' However, we did not want mechanistic set-and-forget target date funds. We wanted dynamically managed target date funds, because we had seen the criticism that some US target date funds received during the 2008 financial crisis.

But because we had scale, and because we knew that our target market would understand that they get a state pension at a particular year, we felt it was just simple to say to them, 'When you join NEST, we put you

into a target date fund for the year you get the state pension. There's one target date fund for every single year, so we have about 50 of them. We know your date of birth, and thus, know your state pension eligibility age.' For young people joining today, that age will be 68, and we work out which year that is. So you get put into the 2065 target date fund—or whatever the right year is—and that simplicity resonates with our members.

How do we cook up our recipe of volatility and risk for these lovely people? We do it by having two composites [Figure 4.1]. We have a growth-seeking composite, and we have an income-seeking composite. To create the volatility recipe for each year, we take a different percentage of the growth composite and the income-seeking composite. To create these two composite funds, we have a set of mandates that sit underneath them. For the growth-seeking composite, the mandates are global equity, direct and listed real estate, and emerging market equities. For the income-seeking

FIGURE 4.1
NEST Retirement Date Funds: Unique, Single-Year Target Date Funds



Prepared by: Tim Jones, presentation at the 2015 Global Retirement Savings Summit (Tokyo, Japan)

composite, the mandates are UK corporate bonds, sterling cash, gilts, and index-linked gilts. We decided quite early on that because we were starting with no funds under management, there was no business case for NEST to run the money. So we decided that the only sensible thing to do was to buy asset management capability from the industry. We have the world's leading asset managers running our mandates, and we chose them by running a competition for each individual mandate. We specified the mandate in detail, and then we invited the asset management industry to bid.

Now, obviously, we engage with the industry. There's no point in us specifying something that nobody actually has anything close to. That would not be sensible. So as we are looking to add a new asset class, we engage with the industry and say, 'We think we want one of these. Would you be

interested in bidding for something that looks a bit like this?' This gives us a sense as to whether there will be a market of participants.

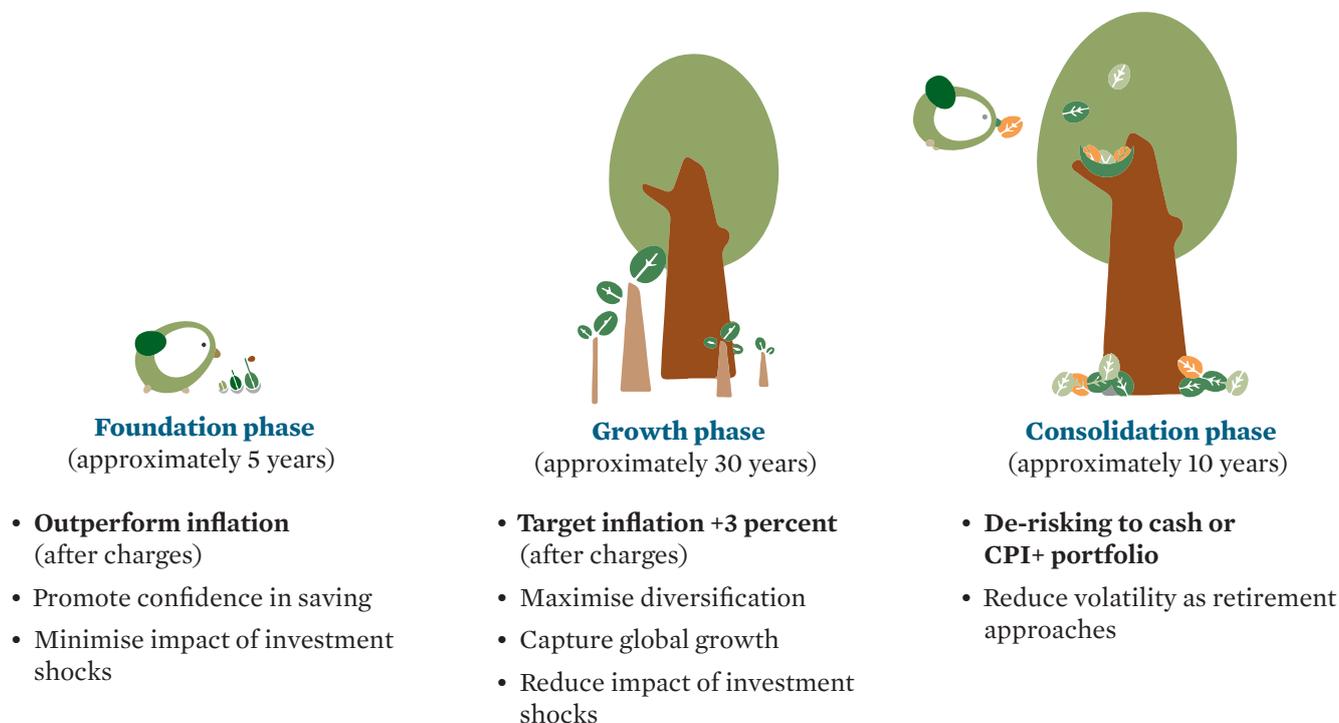
We are still very small—maybe two million members, but only 430 million pounds under management. So NEST, in terms of funds under management, is still tiny. We'd love to be invested in infrastructure, but we don't have the scale to do that yet. As we develop that scale, however, we can add mandates to our composites, which will make them richer, more sophisticated, and more complete.

The objective of our retirement date funds is to exceed inflation by a considerable margin, and we have three phases [Figure 4.2]. The first is our foundation phase, the second is our growth phase, and the third is our consolidation phase. The foundation phase is quite controversial, because we

FIGURE 4.2

Objective of NEST Retirement Date Funds

Achieve target investment returns well in excess of inflation after all charges over the long term



Prepared by: Tim Jones, presentation at the 2015 Global Retirement Savings Summit (Tokyo, Japan)

tell our target market at the beginning that we will expose them to less volatility and risk during the first phase than we will in the later phases. This came directly from research with our target market. We asked these young people, 'Do you fancy taking a bit of risk?' And they said, 'Oh, yeah, I'd love to take a bit of risk. Bring it on. I'm a risk kind of person.' Then we did qualitative panels where we introduced them to this concept over the course of two weeks. In the first week we said, 'There's 100 pounds in your fund.' Then we sent them a letter halfway through the next week, saying, 'I'm sorry, it's 90 pounds now. You know that risk you took? Well, I'm sorry, it was high risk, and you've lost some money.' Finally we brought them back for a second panel the following week, and they said, 'This is outrageous. Who's stolen my money? I want to get out of here. This is ridiculous. I know I said I'd take risk, but I didn't think it would go down.' So their expressed risk appetite was much higher than their actual risk tolerance.

Remember, our target market is in their twenties and they do not have that much money under management. So even if you were successful with your high-risk strategy, the total quantum of extra wealth you're building is very small. These are not professional football players or pop stars that have an inverted income experience in their life. They start at the bottom and some of them work their way up. So there's no real financial case for taking a lot of risk early on. It's more important that they get used to saving and that they stay in. That's the foundation phase. The growth phase is much more conventional. We're targeting the consumer price index [CPI] plus 3 percent after all charges in the context of a low-charge scheme.

The third phase, the consolidation phase, is all about getting ready to buy that annuity with three-quarters of your pot. It was great while that was the law, but we are right in the middle now of deciding how we change that third phase to recognise the

very different landscape that the removal of compulsory annuitisation has brought to the UK market. Later this year we will announce how NEST is going to evolve to take account of the new freedoms.

In addition to NEST Retirement Date Funds, we do have some additional choices, but we don't expect many people to take them. The reason we have them is mostly to do with behavioural economics. The behavioural scientists said, 'Look, if you don't give people any choice, they will say that's very bad. You're a very bad person. You're forcing me to go into this retirement date structure. I don't like it.' But if you give them a small number of choices, they can say, 'Well, I considered those other choices, but I thought I'd stay in the retirement date structure because it looked like a pretty good structure to me.' So having the choices there gives them permission to not make any and to stay in the default construction and be happy; 99.7 percent of the two million plus NEST members are in the default fund, and we are very happy with that.

The other choices are: the NEST Pre-Retirement Fund, the NEST Lower Growth Fund, the NEST Higher Risk Fund, the NEST Sharia Fund, and the NEST Ethical Fund. We've given two of those investment choices unattractive names: 'lower growth' and 'higher risk.' These names are unattractive on purpose, as the names are designed to make you *not* choose that option. The other two are more serious. For the Muslim community, we have a Sharia-compliant fund, and for people that wish to have an ethically screened fund, we have an ethical fund. The pre-retirement fund is a short run that will disappear in a few years. So that's it, we do not have 300 fund supermarket choices. That would have been completely the wrong thing to do.

So what members get from NEST is a very straightforward experience [Figure 4.3]. They can see the choices if they want to, and we will tell them what is going on in

great detail. We have fund fact sheets that set out *exactly* what we're doing with their money, but they don't have to read them. If they want to read them and find out, that's fine. But if they don't want to, that's fine, too. Our tonality is very welcoming. We're not trying to put people off learning about this. We're just not *requiring* them to learn about it.

And simplicity drives our product as much as possible. We have one price. We don't price the individual fund choices, even though they do cost us a different amount of money. Now 'under the hood' of the programme, we do have quite a lot of sophistication, but we don't want to or feel the need to talk to our members about the details. We do need to talk to the intermediaries, employee benefit consultants, independent financial advisers, and media commentators about those details though. If we didn't or if they couldn't review the details, they would say, 'Well, this is a pretty poor-quality product.' So there is an audience for that level of sophistication, but that audience is not our members.

John Rekenhaller: In my presentation, I'll tell you a little bit about target date funds, which are the main way in which default investments occur in 401(k) plans in the

United States. I'm going to talk more about the background, including how we got there.

Most target date funds tend to look pretty similar for investors that are a long ways away from retirement. So in general terms, from one US provider to the next, the 2050, 2055, and 2060 funds will look largely similar. A high percentage of the fund will mainly be invested in equities, mostly mainly US equities, because we certainly have a home bias in the United States. In fact, we often have trouble recognising that there are other countries outside of the United States. Then over time, the asset allocation to equities declines. Actually, the funds differ the most when they mature and reach their target date, because some providers become very conservative and basically invest the fund's assets in cash and short-term, fixed-income portfolios. Others believe in having a fairly significant portion invested in equities with the idea that the person will continue to own this fund for maybe another 20 or 30 years and needs inflation protection. So US target date funds don't differ that much at the beginning, but they do quite a bit at the end. And they're diversified. They do have some international securities and some things like Treasury inflation protected securities,

FIGURE 4.3

The NEST Experience

What members see...

- » Straightforward enrolment experience
- » NEST Retirement Date Funds
- » Focused NEST fund choices
- » Clear communications without being overwhelming
- » Same low charge across all funds

And 'under the hood'

- » Multi-phase investment approach, targeting different risk and return objectives
- » Dynamic and sophisticated risk management that's designed to succeed in different economic conditions
- » Unique delivery system that provides flexibility and efficiency
- » High levels of governance and clear alignment of interests

Prepared by: Tim Jones, presentation at the 2015 Global Retirement Savings Summit (Tokyo, Japan)

or TIPS, which adjust to inflation and so forth. But they're largely invested in basic US large cap stocks, Treasury bonds, and cash. That's mostly what they're made of.

So how did we get there? The 401(k) happened a little bit by accident. It was a voluntary savings programme. If employees wished to use the programme, they could, and if not, they did not need to participate. That was the structure. Education was regarded as the solution to get people to participate more. Tim told some stories, and we certainly can on our side of the Atlantic as well, about employers bringing in people and having sessions to educate participants about the principles of investments, risk return, and so forth. If you could get the participant to check a box and do something in that meeting, you got something done. If they left the meeting and had not checked a box, they probably were not going to come back and check a box and get invested. So it was, much as Tim said, that most people did not want to become investors, and they were not going to become investors based on a one-hour session.

There were a variety of reasons why the educational approach was problematic. It worked well with the older, wealthier employees who were inclined to invest anyway. It did not connect with younger or lower-income workers. As a result, many 401(k) plans had problems, the so-called issues with nondiscrimination provisions under the US tax code. The way the nondiscrimination provisions work is that if you offer a 401(k), you have to get a fairly broad level of participation in the plan. It couldn't just be the senior, highly compensated employees. And plans were having difficulty because the educational approach was not getting enough of the younger or lower-income workers involved.

A natural response would be an automated enrolment programme to move people into default funds. If you move people into investments automatically, you're probably

going to get higher participation than if you don't move them in automatically. In the late 1990s, there was a lot of research from major universities—Wharton, Harvard, Chicago—looking at 401(k) plans and making arguments for automated enrolment to improve participation rates.

So the academic community—although they were not the only ones—certainly had an effect on changing the discussion about how to get people to save.

This argument in the 1990s was really about trying to get retirement savings right for the masses. Since then, automatic enrolment has really grown. The percentage of 401(k) plans that had automatic enrolment in 2002 was 7 percent. By 2013, about half of the 401(k) plans offered automatic enrolment. Automatic enrolment is particularly popular with large plans.

The first default solution in the United States was cash. For a long time, employers viewed it as the 'legally' safest alternative. If an employer put an employee in some other product and the product lost money, the employer was concerned about potential litigation. So cash was seen as the least likely to cause employee concerns or complaints.

The academic community, again, was quite involved in this and criticised the notion of the cash solution. They said, 'Well, you're getting low expected returns, the lowest expected return of any asset out of cash.' Once defaulted, most employees tended to stay in that asset. They were slow to move from cash to other assets. The academics pointed out that the very inertia that keeps people in a plan once you default them keeps them from moving out of whatever investment that you first put them into. So maybe you should put them into something that's better and more suitable because they may not leave. Also, most employees tended not to increase their contribution rates or were slow to increase their contribution rates after being defaulted.

FIGURE 4.4

Target Date Funds

- » Legally protected by the Pension Protection Act of 2006
- » Easily understood by employees
- » Diversified portfolio addresses the problem of low returns; dynamic asset allocation addresses the problem of employee inertia
- » In 2013, of the Vanguard 401(k) plans that designated a default option, 91 percent used target date funds

Prepared by: John Rekenhalter, presentation at the 2015 Global Retirement Savings Summit (Tokyo, Japan)

The response to these arguments was target date funds [Figure 4.4]. Target date funds are legally permitted to be used as default investments by the Pension Protection Act of 2006 and the regulations that implemented the act. That was a significant act, because it said you could default people into riskier assets than cash. It's important to know, however, that target date funds are not the only kind of fund that are permitted by law. You can put people into a balanced fund, managed account, or into competing lifecycle funds, such as aggressive, conservative, or moderate.

Why did target date funds become the most popular? Well, if you think about it, they have an advantage. This comes down to product superiority from the investor's perspective. If you look at a balanced fund, there's one balanced fund for everybody in the plan. So that doesn't feel customised. Target date funds, however, are set up every five years, so it feels more targeted to you. Lifecycle funds—such as aggressive, conservative, or moderate—require the investor to make a decision. 'Am I aggressive, conservative, or moderate?' We want to put up the fewest barriers possible for investment, so when it comes to defaulting someone into a balanced fund, how do you decide? Do you just drop them into the moderate? Then everybody gets the same fund, just like a balanced fund. If you're giving them a choice, which sometimes happens when you're getting a lineup of funds, then you're forcing a choice on them.

And in a managed account, it's more of a custom and expensive option.

So with target date funds, you feel like you have the best of both worlds. You have something that feels more customised but it's the cost of a non-custom product. It's priced the same as other funds. And target date funds have run away with the field, as Vanguard data from 2013 show. Indeed, of the Vanguard 401(k) plans that designated a default option, 91 percent used target date funds.

It is important to note that target date funds do not solve the problem of low contribution rates. However, other innovations—such as automatic increases—are being adopted by employers, in combination with the use of automatic enrolment. Auto-increase means that an employee's contribution automatically increases, usually on an annual basis. For example, an employer could begin an employee with a 3 percent contribution, and can then adjust the contribution rate to 4 or 5 percent the next year, 6 or 7 percent the following year, and so forth. As with plan participation in general, an employee can always opt out, which is critical. An employee can opt out of participating in a plan, and an employee can opt out of a default fund and move to another fund. An employee can also opt out of the auto-increase. Yet most people, once you put them on a path, tend to stay there. And this is where we are right now in terms of the development of default funds.

In conclusion, from my perspective, the 401(k) plan has clearly changed over time. Plan costs have come down. The creation of default programmes, development of target date funds, and implementation of automatic enrolment and automatic savings are all improvements that have helped people using 401(k) plans achieve better results than they were 10, 15, or 20 years ago. But this is largely true with large company plans. The small company plans have not adopted these changes in the same way. The economics of serving small plans are more difficult, and they're generally not as strong for the employee as the large plans. So that's where we are right now in the United States.

Douglas L. Hyman: Good afternoon, everyone. It's a pleasure for me to be here. I work with BNY Mellon here in Japan, and I'm also the chairman of the Investment Management Committee of the American Chamber of Commerce in Japan. That latter role is probably more relevant since I have been involved in discussions with certain government entities and organisations about the development of pension programmes, including DC programmes.

First, I'd like to retrace some of the history of the DC system here in Japan. I was working for an investment management company back in 2001 when the DC system was first introduced. It was called Japan Version 401(k), and we were all excited about it. Our company was one of many that invested in a new entity that was supposed to take advantage of the 401(k) business, and we were all excited about the system. Unfortunately, at the last hour, contribution limits were cut, and I think that inhibited some of the developments and some of the impact of the 401(k) programme. Over time, those limits have been increased by small amounts, and that's helped. Yet we continue to advocate for higher contribution limits across the board for all DC programmes. That brings me to one of my fundamental points: we should

continue to advocate for a robust DC programme here in Japan.

Unfortunately, we always run up against the Tax Agency in Japan. It's a formidable barrier, and for today's discussion, I'd like to put the issue of contribution limits aside and talk about the structure and the history of the DC system outside of contribution limits.

First, I'd like to discuss Japan's pension structure [Figure 4.5]. Japan often describes itself as having a three-tiered pension structure. The base is the national pension, the basic pension. This is the national pension programme to which every Japanese citizen is expected to contribute and from which they should get something back at some point in the future. Because of the low birth rate and ageing society problems, there's a lot of distrust and fear surrounding this programme. Specifically, there are concerns that the younger generations won't benefit as much from it in the future. So that has put pressure on both the government and employers to improve the amount of benefits available in the other layers of the pension structure.

The second tier consists of several components that cover different groups of workers: the employee's pension insurance is for private-sector salaried workers and the mutual aid pension is for public servants. This second tier doesn't cover all citizens in Japan. So, to put this in context by types of workers, public servants are covered both under the first tier [the national pension programme] and the mutual aid pension programme that is part of the second tier. Then they also have access to a third layer, an 'occupational addition.'

For private-sector salaried workers, they're covered by the first tier [the national pension programme] and the second tier [the employee's pension insurance programme], which usually comes from mutual aid

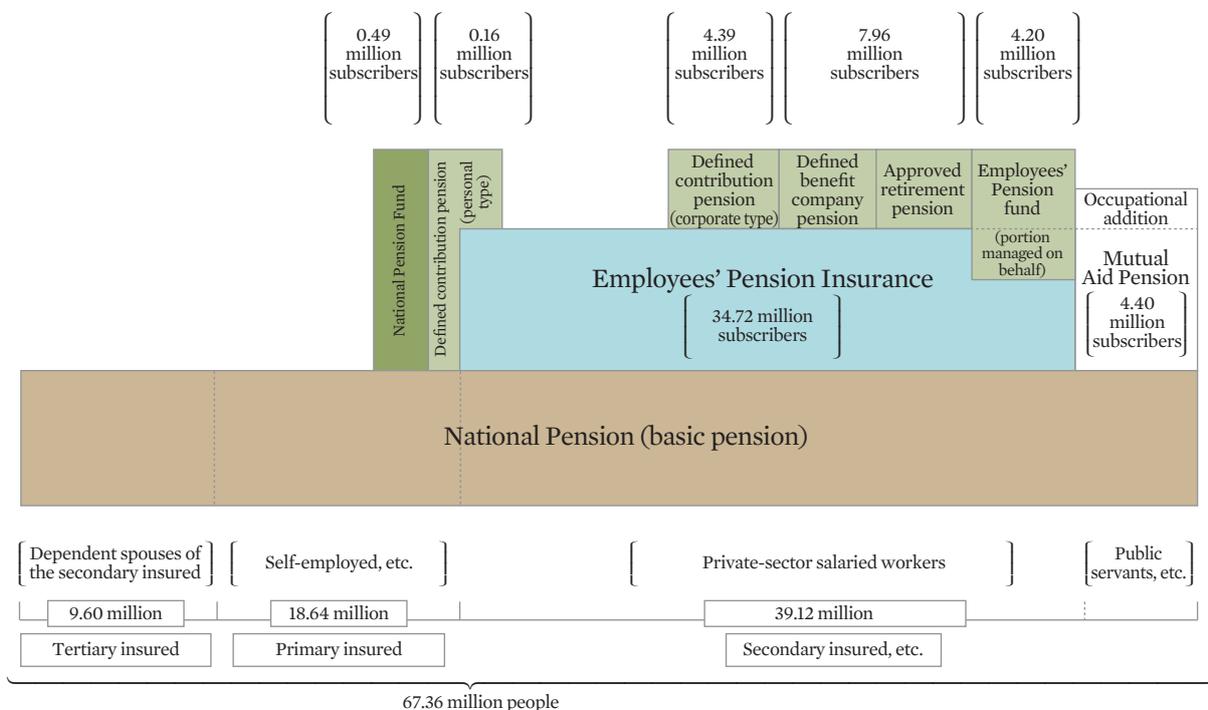
associations offering some type of pension programme. Then, on top of that, individual companies are allowed to offer employees certain tax preferred or tax benefited programmes, in the form of what we call a pension programme. That pension programme is the third tier, and the government introduced the DC system into this third tier in 2001. And it's a fairly small portion of the entire pension system. According to data from the Japanese Ministry of Health, Labour, and Welfare, 4.39 million subscribers are currently in DC pension corporate type plans. There are about 7.96 million in DB and approved retirement programmes, and 4.2 million in the Employees' Pension Fund, which is another type of pension programme that actually is being phased out. So, in this context, the number of employees covered by DC plans is quite small.

There's another slice of DC plans. It is in both the second and third tiers, and it's titled 'defined contribution pension—personal type.' Currently, it's quite small, with only about 0.16 million subscribers. The American Chamber of Commerce of Japan has been advocating for the expansion of this programme for some time, in the form of both increasing the contribution limits and expanding it to more subscribers. Our first recommendation was to expand it to government workers. It was our view that if government workers had a programme available to them, then that would become a standard for the rest of society. I'm pleased to say that in the latest round of reform proposals that are coming out, the government included our proposal and it also went further.

FIGURE 4.5

Structure of Japan's Pension System

Figures are as of the end of March 2013 unless otherwise noted



Source: MHLW (<http://www.mhlw.go.jp>) (translated from Japanese)

Prepared by: Doug Hymas, presentation at the 2015 Global Retirement Savings Summit (Tokyo, Japan)

Currently, dependent spouses of employees are only covered by the national pension programme. There is no other programme available to them. Under the current reform proposals, the government has proposed expanding the personal DC plan to cover those spouses. The expansion also will include the self-employed and those who work for companies that either do not offer DC plans or perhaps offer DC plans but not to the full extent. In other words, the goal is to expand the personal DC plan as much as possible to allow all Japanese people to have some sort of programme available to them if they would like. This proposal is enormous, and we think it will create a sea change in the way the DC system works in Japan. We think it will also increase the level of dialogue about how investing and Japan's pension programmes work. Indeed, it could be quite a catalyst for addressing the pension crisis.

Japan is at a point now where the risk of inaction—keeping investors in cash and deposits—has become greater than the risk of taking action and putting investors into riskier assets.

—Doug Hymas

Now, again, let's go back through history a little bit. In 2001, some of the motivations for introducing the DC programme came from companies that wanted to take pension liabilities off their books and put them on individuals. There was a bit of a selfish motivation there for companies, but it seemed to work well for everyone. So at least we got the DC programme introduced at that point. At the time, people recognised that the low birth rate combined with Japan's ageing society meant a change needed to take place in the pension system, and a DC system was one of the reform measures adopted to help that situation. Now, the 401(k) should have made a big dent in the problem, but there were several weaknesses in the version that was introduced.

I believe the DC programme was weakened because it became an alternative for companies offering DB plans. So the emphasis was more often on helping companies avoid their pension liabilities, and not really on improving the pension situation for employees. I think that's been recognised, and I think people are trying to rectify it now. Also, contribution limits were set so low that they were less than meaningful in denting the pension problem. Another weakness that we saw was that companies were given the responsibility to contribute to the DC programme. Now I say that's a weakness because in my experience in the United States, employees were responsible for designating how much money they would put in their DC accounts and it made them feel personally responsible for their investments. It helped increase the level of investor education in the United States, and I believe studies have shown that since the early 1980s, the level of investor education in the United States has exploded. A huge contributor to that development was the introduction of 401(k) programmes.

I think Japan hindered the development of investor education in Japan by having companies initially contribute to the programme. Another weakness was that it wasn't clear who had responsibility for product selection, and that problem still persists. I've had many discussions with Japanese asset management companies, foreign asset management companies, and employers about who bears the responsibility for choosing products. This lack of clarity often hindered companies' willingness to provide risky products or to encourage their employees to consider investing in riskier assets.

Now we are at a time where Japan's investment psychology must change [Figure 4.6]. Data from 2014 fund flows from the Bank of Japan show what will happen with the 868 trillion yen in personal assets that Japanese households are holding in cash and deposits under two scenarios. The data for

the first scenario show what will happen to that 868 trillion yen if the economy reaches the government's target of 2 percent inflation. The data for the second scenario show what will happen to that 868 trillion yen if deflation of 1 percent continues. If Japan reaches the 2 percent inflation rate, individual assets will drop significantly in value as inflation goes up. The data show that if we don't put households' money in riskier assets, then those households are going to lose money. However, if deflation continues, the assets will continue to increase. The message behind this data is that it has not been such a bad thing for households to have been invested in cash over the past 10 or 15 years because it has been during a deflationary period. But now the environment is changing. The government's and Bank of Japan's efforts to increase inflation is actually showing some effectiveness. Kuroda-san, the governor of the Bank of Japan, recently mentioned that he feels like he is halfway to the 2 percent

inflation target. It's pulled back a little bit, but he expects it's going to continue.

So the deflation scenario no longer applies, and we're now looking at the inflation scenario. If we're going to help Japanese workers, individuals, and pensioners prepare for retirement, we have to start focusing on riskier investments. Thus, Japan is at a point now where the risk of inaction—keeping investors in cash and deposits—has become greater than the risk of taking action and putting investors into riskier assets. The risk of inaction now is very real, and I think it should continue to drive the discussion about introducing riskier assets.

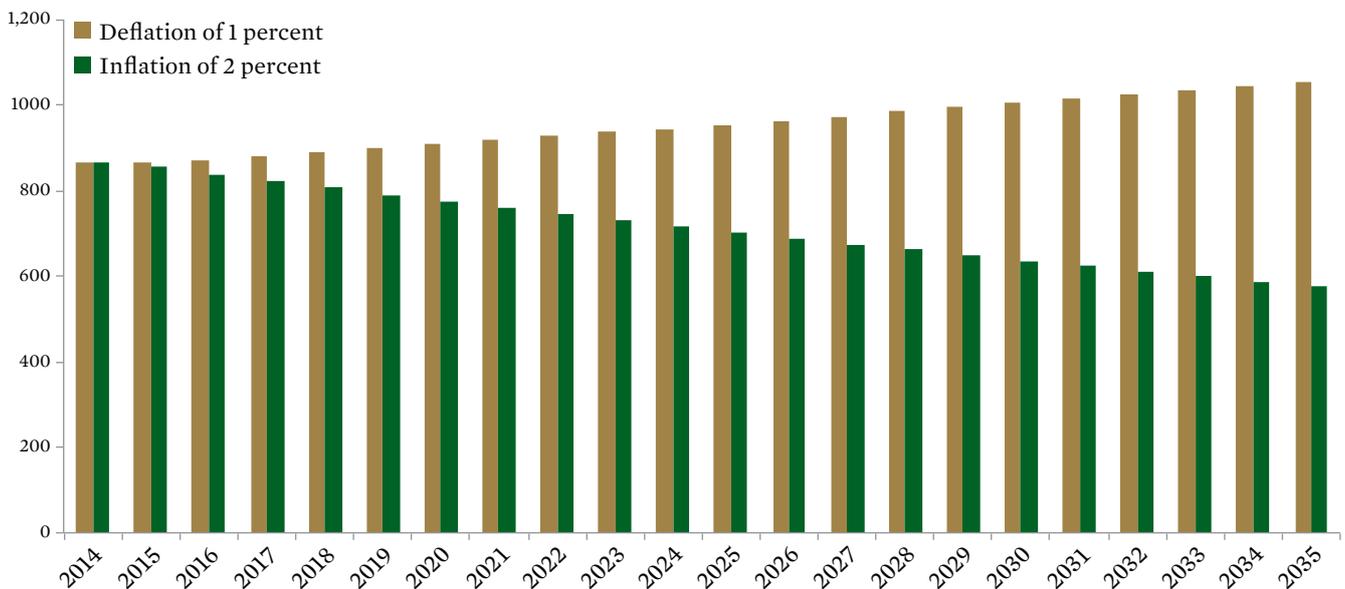
As in other markets, responsibility for long-term savings and investment is shifting away from the government and institutions and towards individuals. Institutions have been increasingly unable or unwilling to bear the risks of market downturns and inflation against their fixed payment

FIGURE 4.6

Why Japan's Investment Psychology Must Change

Real value of Japanese households' ¥868 trillion in cash and deposits

Trillions of yen



Source: ¥868 trillion from Bank of Japan's Flow of Funds for June 2014

Prepared by: Doug Hymas, presentation at the 2015 Global Retirement Savings Summit (Tokyo, Japan)

obligations. In most markets, investor education is expanding to help individuals take responsibility for their retirement savings. In Japan, however, individuals' knowledge about true long-term investment remains low. Despite efforts to convert individuals from savers to investors, the percentage of individual assets and deposits remains high while the percentage of investments stays low. Even participants in 401(k) plans are shielded from decisionmaking and protected from the exposure to investment risks and rewards, which keeps them from choosing to invest in riskier assets. In Japan, 60 percent of 401(k) assets remain in cash or guaranteed products. I believe the current rate is about 40 percent in cash and 20 percent in guaranteed products. So 60 percent of the assets are not growing in the way they are intended to under a 401(k) programme, and that's what needs to change given the inflationary environment that is coming into play.

We need better education in Japan—not only for investors, but also for both those who provide the plans and for employers so they can understand how they should be looking out for employees and pensioners.

—Doug Hymas

As an advocate for DC and 401(k) programmes and for introducing riskier assets, I'd like to share just a few recommendations for reform. The new individual DC programme that will be introduced hasn't been given a name yet, so I'd like to take the liberty of giving it the name that I think it should have: My-DC Account. So the following are my recommendations to those who can implement policies for the new individual DC programme.

First, we need to increase contribution limits. Second, we need structural improvements to enhance usability, which need to include better default options. We were asked by the FSA to give them our views on

default options, and we pointed to a legal change in the United States that specifically said that default options may include target date funds. The FSA was quite interested in that section of the law. Who knows, we might see that being introduced fairly soon, but I think that's the level of protection that we need to avoid the issue of responsibility for product decisions. In that context, I would also recommend eliminating the mandatory capital preservation option. I've spoken with many participants, including those involved in the DC system who say that having the capital preservation option as a mandatory requirement actually inhibits investors from choosing something else because they're so risk adverse. So we should consider eliminating that option or at least downplaying it.

My third recommendation is that we need better portability and continuity. The model that's being used to formulate the new policy for My-DC is women in the workplace, which dovetails nicely with the Womenomics Programme by the Abe Administration. The proposed reform is addressing the situation in which women work for a number of years, quit to bear children, and then come back to the workforce. Currently, most DC programmes don't allow women to maintain their DC programme after they quit a company. There's not enough portability. It may be legally allowed, but most of the programmes don't allow such continuity from a technical and practical perspective. Therefore, women have to cash out or somehow convert their savings to something else. Then when women go back to the workforce, there's no way to bring those savings back into the workforce. So the idea is to find a way to allow a typical woman to build her retirement assets while she's working, allow that money to grow tax-free and in a tax preferred environment while she's away from the workplace, and then come back into the workplace and

enjoy continuity. That's an important scenario. And let me just say, it's not just for women, it could be for men who are also taking time off to raise a child.

The last recommendation is that we need better education in Japan—not only for investors, but also for both those who provide the plans and for employers so they can understand how they should be looking out for employees and pensioners. That can only come through experience, dialogue, and by looking more closely at how things are done offshore. And I think we've seen some great examples here today.

Finally, we spoke mostly about DC plans today, but I'm also excited about the success of the Nippon Individual Savings Account [NISA] programme. NISA has also helped people focus on longer-term savings. As many of you may know, the NISA version is modeled after the United Kingdom's Individual Savings Account [ISA]. After ISAs were introduced, they were eventually made permanent. We believe that the Japan version should become permanent to encourage longer-term savings through NISA.

Monroe: Thank you, Doug. Now we have some questions from the audience, and I'll start with this one. 'It's very interesting to hear about the role of behavioural finance, and we heard about that in bits and pieces. Can you summarise the role that behavioural finance has played in your jurisdiction?'

Jones: Well, it really depends on the whole of the policy shift. In the United Kingdom, the view was that only changing the frame from 'do nothing and you're out' to 'do nothing and you're in' would significantly change coverage. But the decision to apply the law to all employers—the law that said an employer must provide a plan and enrol most workers in it—was actually

very important as well. It took a lot of political courage to drive coverage down to the small- and medium-enterprise sector, which has nothing to do with behavioural economics. I think excitement has arisen from behavioural economics, because it had such startling results. We had the same people with the same attitudes and the same level of wealth, and the different frame seemed to shift the dial from a 30 percent participation rate to a participation rate in the 90s.

It's surprising to me to hear that in the both the United States and United Kingdom, simply trying to educate people didn't automatically turn them into investors.

—Doug Hymas

Rekenthaler: I think the academic community had a large effect on changing the focus of the discussion in the 1990s. When asset managers used to talk about retirement savings, they tended to discuss who had the best widgets. And their focus was on higher net worth individuals—the senior people in the company—and how to attract and retain wealthy clients. Well, the academic community was looking at a very different kind of problem, which is how to address America's broad retirement solution. The academic community came in, and a lot of the asset managers looked at the research, took it, and ran with it. So the academics also affected how asset managers were thinking about the retirement savings challenge. It was, in my mind, a very healthy collaboration that ended up with two different viewpoints coming together. There are a lot of asset managers that now have think tanks and research that are moving into policy territory. Indeed, this kind of conference is an example of this trend.

Hymas: I think behavioural finance is sort of a new area in Japan, and I think

there's a lot of fertile ground for discussion here. Thinking over the 401(k) experience, we're only learning now how people respond. We've basically confirmed that they won't move towards risky investments on their own. I think Japan can learn a lot from behavioural finance, and I think the resources and the tools are here. I just think it needs to be employed and followed. I don't think it's worked its way into policy yet, and I think the UK and US models are great for us to follow.

Monroe: After hearing about the effect of implementing some of the conclusions of behavioural economics, are you surprised that Japan's approach of 'education, education' hasn't really resulted in the kind of investing hoped for?

Hymas: It's actually almost comforting to hear that the reason it hasn't taken off here may be the same as in the United States. It's surprising to me to hear that in the both the United States and United Kingdom, simply trying to educate people didn't automatically turn them into investors. The government here in Japan has made a valiant effort to try to encourage people to move from being savers to investors, and it just hasn't worked that well. The examples here suggest that there's nothing unique about that.

Rekenthaler: Education is a partial solution, but I just don't see how education is going to be the complete answer. That was the experience in the US marketplace.

Hymas: And that's good to learn so we can maybe skip over some of the steps and problems that the United States and United Kingdom experienced and get right to the solution.

Jones: We've recently done some research with NEST members, and even in a qualitative panel, when you take them through the investment process over 90 minutes, a number of them still prefer to be in a very low-risk product that will expose them to

inflation risk. Now, because of trust law, we can override that in the name of their best interests and put them into a riskier solution. But it's not because you talk to them in detail, and then they see the light and become diversified investors. When you talk to them in detail, they actually massively overplay downside risk against upside risk. They get worried, and they say, 'No, no, I'll just protect my capital.' I think the prognosis for taking people who have chosen not to join the investment industry and pretend that somehow they're going to turn into sophisticated investors through education certainly is not borne out by the United Kingdom.

Rekenthaler: It can be a little bit tricky territory because there can be a coercive element to new tools that result from behavioural economics. I use the word 'nudge,' which is a popular word, but it doesn't take too much further to go from nudge to push. And that's an issue as well.

Hymas: May I ask you both a question? From a Japanese perspective, I think there is a reluctance to push people too hard and too far, because we end up taking responsibility for that push. How has that been handled? Do companies and policymakers feel responsible if the investments don't go the way they expected? Are there claims and, if so, how are those handled?

Jones: In the United Kingdom, the investment responsibility lies with a scheme provider. An employer is simply responsible for selecting a 'qualifying scheme.' The worker looks to the scheme's performance, not to the employer. Working lives in the United Kingdom are becoming much more split up into a large number of smaller employments. It's not as if you've got a cradle-to-grave employment relationship anymore. Currently, the average number of employments is 11. People in their twenties may well have 15 or 20 employments by the time they reach 70 years old. So we feel that it makes much more sense to look to the plan provider as the person with responsibility,

because of those 20 employers, which ones are you going to look to if it didn't go well?

Rekenthaler: On the issue of liability, it's worth pointing out that the Pension Protection Act was passed in 2006, which permitted the adoption of target date funds as a default investment option. Then in 2008, we had an unpleasant market. In 2009, there was a lot of blame going around about the performance of target date funds during the crisis. So the debate was not about, 'Should we be defaulting people into risk, and is it wrong to default people and have these default programmes?' No, the debate was about whether target date funds were getting it wrong. Generally, that debate ended with the conclusion that for the most part, target date funds did okay, so the United States didn't put new rules in place to change what target date funds were doing. But that was the discussion. It was never a question about not putting people into them. Yet as we know, the United States has a long tradition of stocks going up, so people got more comfortable with the notion that they would go up again.

Monroe: It is also quite interesting that even in the United States, there was a reluctance to put people into the default product until 2006, when the Pension Protection Act created this safe harbour for employers to protect them from liability for selecting a default investment.

So a question for Doug is, given that Japan has had a different economic experience than the United States, wouldn't employers be very reluctant to set a default product that was investing in equities and riskier products without a safe harbour?

Hymas: I would actually go back to what Yoshino-sensei said earlier, that there are other asset classes out there besides equity. I believe a lot of inexperienced investors think that if they're investing, that means they're investing in Japanese stocks, which have gone down over the past 20 years. They've bounced back recently, but will

they continue to go up, or will they go down? That's a good question, and we're not sure. But that's only one asset class, only one option. The investment world has many asset classes, and there's so many that are much less risky than equities. A target date fund, for example, might have a slice of Japanese equities, but it should also have plenty of other asset classes.

It's not a good idea for an investor or employee to be in cash instead of being exposed to a diverse range of investment products. I think that's the level of education that we need—not necessarily learning or knowing about how each stock moves but teaching them that generally, over time, a properly managed diversified portfolio offers better returns than keeping money in cash.

NEST research has shown that the financial benefit of putting participants into higher volatility investments in the early stage of their career is very low.

—Tim Jones

Monroe: We have a question from the audience for Tim, and the question is, 'It seems that NEST's conservative approach for phase one must have a dramatic effect on the lifetime performance of the fund.' Tim, I'm sure NEST modeled that, and you've decided that this is the right approach. Please talk about it, because it is a very interesting approach.

Jones: The premise of the question is false, because the premise is that the conservative start has a dramatic effect. In our modeling, the effect was a maximum of 3 percent. Why was it so low? It's because these low-to-moderate earners at the beginning of their careers don't earn much. Therefore, there's not much money in their fund in their twenties. If you do 3 percent better, you're adding 3 percent to a small amount, which doesn't make much difference. We take people out of that conservative start in their late twenties. By the time

they're 31 or 32 years old, they're in the CPI plus 3 growth fund. I think there was a supplement to the question, which said, 'Will you revisit this start as the maturity and understanding of the UK markets develop?' In short, yes. Whether we'll change it is another matter, but we'll absolutely review it. It came from research with our members about the difference between their risk appetite and risk tolerance. Now, if that were to change, then we might change our approach to phase one. NEST research has shown that the financial benefit of putting participants into higher volatility investments in the early stage of their career is very low.

Monroe: Very interesting. Another topic that has come up quite a bit is choice and how much choice to give. Tim, again you've taken a very interesting approach. Could you talk about how you came up with limited choice?

Jones: Well, we went to Sweden and they said, 'We have 700 fund choices. Please don't do that.' We then consulted one of the greatest philosophers of the 20th century—that would be Bruce Springsteen—who famously said, '57 channels and nothing on.' Fifty-seven channels and nothing on is perhaps a reflection of the quality of American television, but it also goes to this issue of choice. What on earth are you going to do if you're confronted with 57 choices? You're just mesmerised. You haven't a clue whether that far eastern Asia opportunity fund is better than that emerging market smart beta fund. It's all gibberish to ordinary investors, so how do you translate that gibberish very easily?

So we again used behavioural economists to help us, and we've used them many times. It's not just in the automatic enrolment. The behavioural economists said:

You should provide a small number of fund choices—not because you want people to take them, but because you

want people to feel they had a choice, which they then choose not to exercise. Then they end up in the retirement default fund, which you make as high quality as possible so that you can do a fantastic job on their behalf.

Rekenthaler: Morningstar's experience in tracking how investors use funds—which ends up being how advisers use funds—is that if you give people more choice and more specialised funds, they find more ways of making mistakes. So I would echo what NEST is doing, to strongly push people towards the most broadly diversified portfolio you have, and then hope that they don't use the other funds. I think that would give investors the best experience over the long term.

Hymas: When I first came to Japan and went to a restaurant, I was intrigued by the menus. Everything is already set: the soup, the rice, the fish, everything. You have three choices, but each choice includes a menu of options within that choice. I think that's very natural for Japanese people, and I think that would be very comfortable for most Japanese people who are not that sophisticated with respect to investing. I think they would find that optimal.

Monroe: But there is a behavioural economics theory that says if you give people more than three choices on anything, they start to feel overwhelmed. Oftentimes, there's an enormous number of options in your Japanese 401(k). When you have people who are struggling to understand differences between asset classes, they must feel overwhelmed. So maybe part of the solution is less choice, less options.

Hymas: I think that's precisely the area where behavioural finance and behavioural economics can come into play here in Japan. They can use that as justification for trimming down the number of options and maybe refining what those options should be. 🌱

Programme

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Welcoming Remarks

Paul Schott Stevens

President and CEO
Investment Company Institute
United States

Keynote Speech: Long-Term Savings Reforms in Japan: Asset Allocation, Pensions, and Defined Contribution Arrangements

Naoyuki Yoshino

Dean, Asian Development Bank Institute
(ADB Institute)
Professor Emeritus, Keio University, Japan

PANEL 1

Role of Private Pensions in Retirement Savings—Countries' Case Studies

Stephen P. Utkus, Moderator

Principal, Vanguard Center for Retirement Research
The Vanguard Group
United States

Tim Jones

CEO
NEST Corporation
United Kingdom

Akiko Nomura

Senior Analyst, Research Department
Nomura Institute of Capital Markets Research
Japan

TEA/COFFEE BREAK

PANEL 2

Investment Diversification and Long-Term Savings—Default Funds and Beyond

David W. Monroe, Moderator

General Counsel
Matthews International Capital Management, LLC
United States

Douglas L. Hymas

Managing Director, Japan Country Executive
BNY Mellon
Japan

Tim Jones

CEO
NEST Corporation
United Kingdom

John Rekenhaller

Vice President, Research
Morningstar, Inc.
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CLOSING REMARKS

Dan Waters

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