V for Victory in Target Date Fund Glidepaths: The Crying Need for Change

Change is the law of life. And those who look only to the past or present are certain to miss the future. *-John F. Kennedy*

Target date funds (TDFs) have grown from almost nothing 10 years ago to more than $1.5 trillion today, yet no one has questioned the shape of glidepaths that decrease in equity exposure through time, ultimately leveling off at or near the target date. There is a better glidepath and it is V-shaped, a big departure from current practices.

A better glidepath for retirees

To see this better design, start with what is best for people in retirement as explained by Dr Wade Pfau and Michael Kitces' Reducing Retirement Risk with a Rising Equity Glide Path, In the conclusion to this very thoughtful and rigorous study, the author's state: ***the results reveal that rising glidepaths are even more effective, especially when they start off conservatively. The most favorable (i.e., least adverse) shortfall actually occurs with a glidepath that starts at only 10% in equities and rises to "only" 50% in equities.***

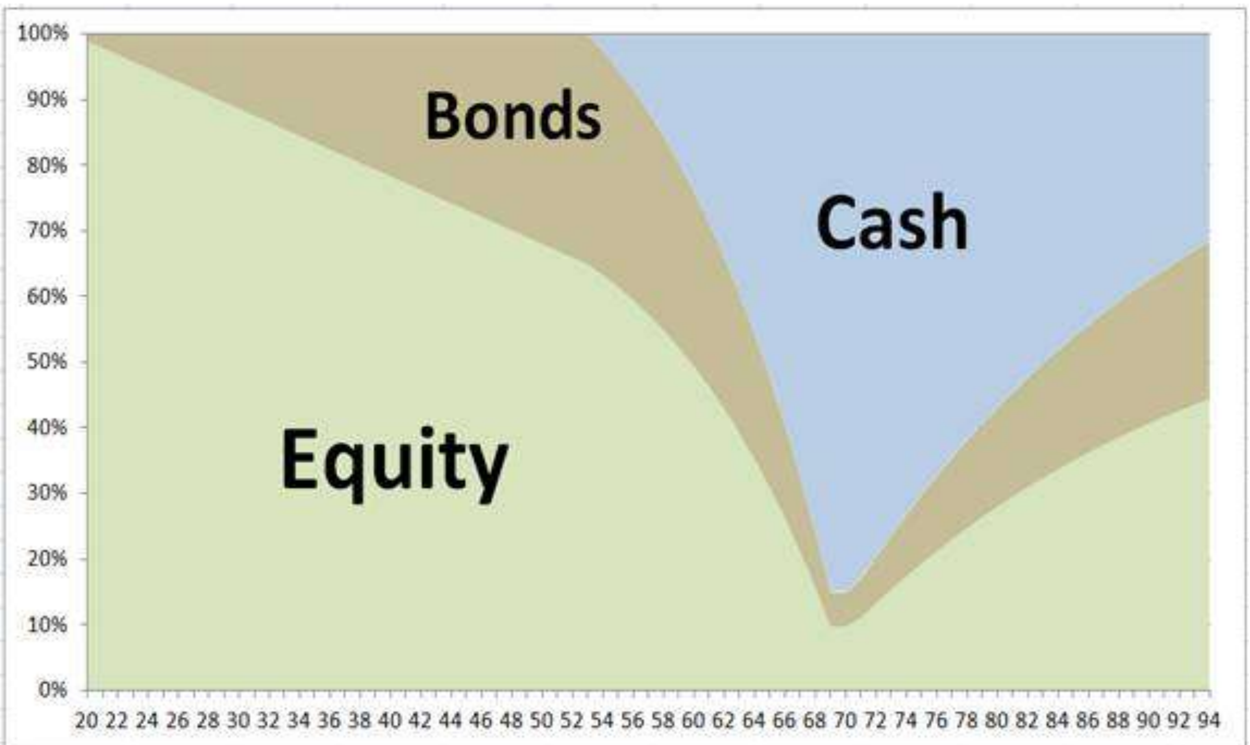
The better glide path for retirees is increasing in equity exposure rather than flat, and it starts at a very low 10% in equities. This low equity allocation is designed to protect against Sequence of Return Risk: losses in early years of retirement can be devastating because account balances are at their highest.

A better glidepath for working people

Working backwards from retirement, the glide path for working people should end at 10% in equities. This makes perfect sense because there is a Risk Zone spanning the 5 years before and after retirement during which lifestyles are at stake. So the shape for working people is the same as it has been from the beginning but the end point is much lower. The typical TDF currently ends at about 55% in equities. This needs to be reduced significantly.

The complete V-shaped glidepath

The better glidepath looks like this:



This glidepath defends against sequence of return risk by being very safe in the Risk Zone. It's also important that all asset classes are well diversified. Equities are global stocks plus real estate. Bonds are global bonds, and Cash is Treasury bills and short-intermediate TIPS (Treasury Inflation Protected Securities).

There is only one V-shaped glidepath currently in existence. It is the patented Safe Landing Glidepath® followed by the SMART Target Date Fund Index. Someone had to be first. The industry really should follow.