



2025 **TARGET-DATE FUND** ROUNDTABLE

Over the last decade or so, **target-date funds** have established themselves as the default option for defined contribution pension plan sponsors. But with a complex blend of economic factors, market dynamics and regulatory changes contributing to an increasingly turbulent environment for plan members and institutions alike, TDF managers are actively reassessing their practices. We asked eight expert panellists to discuss some of the biggest trends in the TDF market.

MEET OUR EXPERT PANELLISTS:



**DEREK
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Multi-asset institutional
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**NICK
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**SERGIO
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**JON
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**STEPHANIE
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**NANCY
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**VARTKES
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partner, defined contribution
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What are the most important factors to consider when assembling a TDF glidepath?

PILOTTE: There are three main questions to ask when designing a glidepath. The first is: who are you designing it for? We want to understand the makeup of the participant base in a holistic way by looking at their savings rates, their risk tolerance and what other retirement income solutions and benefits they have outside of the plan.

Second, what problem are we trying to solve for participants? The major focus of the target-date solution is the risk of outliving your money in retirement, so it's about understanding how you balance the different risks that are part of that problem in a way that's appropriate to the participant base.

The last question that we would think about is: how do you meet the fiduciary's needs? It's not just the end user that you have to think about. For the plan sponsor that is actually selecting the program, you have to look at cost, performance expectations, transparency and any other support they need.

BEANE: There's no silver bullet in our view; it's really a mosaic of factors. The way we approach it is to put ourselves in the shoes of the end investor when setting allocations, choosing underlying funds and deciding on our rebalancing approach and risk management oversight.

At the end of the day, plan members are not aware of these inputs. What they care about is the output and whether their investment selection allows them to retire on time with the standard of living that they expected.

RUBENYAN: We look at each product as a point between two extremes: at one end, you have an asset mix that is designed to generate some level of replacement income; and, at the other, you have an asset mix designed to minimize the risk of depletion. There's obviously no glidepath that is designed absolutely for one or the other, so we work with clients to figure out the glidepath that best meets their objectives.

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— Beane

How do you think about the active versus passive debate when it comes to TDF allocations?

KNOWLES: I would start off by saying that there's no such thing as an index TDF. Every single TDF is an active strategy based on the investment manager's interpretation of Canadian investor demographics, savings rates, capital markets and diversification, in conjunction with other variables.

When we talk about implementation above and beyond the glidepath, that's when you get into the conversation of active versus passive and I think it comes down to the plan sponsor's cost sensitivity, their investment beliefs around market efficiency and how they view the kind of value that active management can generate in the long term.

PILOTTE: Another type of strategy that bears mentioning is a hybrid one that takes some of the best of indexing and the best of active, and brings that together in a more systematic way. A blend or hybrid approach can achieve many of the same benefits that indexing offers, while also accessing some active upside potential.

BEANE: We do employ a fully active approach. As we look at the markets, passive has had a huge tailwind over many years, given the low volatility, low rates, low inflation and low cost of capital that we have seen. Company and security selection hasn't mattered as much, given how top-heavy the markets have been, but a lot of our more recent conversations with clients have touched on what happens when the market dynamics change and those tailwinds aren't present anymore. That's when diversification and active management have historically benefited.

How do you approach the balancing act that's required to manage specific risks like longevity and inflation into the management of your TDFs?

KNOWLES: There are really two forms that this balancing can take in your investment process, the first of which would be through the quantitative techniques we use to evaluate our portfolios and assess the trade-offs associated with specific risks being borne by Canadians, depending on where they are in their life cycle. Then, at the portfolio construction level itself, there's various investments that we can utilize to try and — not necessarily hedge — but diversify some of those risks that individuals are faced with.

BEANE: From an investment management standpoint, it's important to start thinking about addressing longevity and inflation risks much earlier than the date of retirement – well before fixed income becomes the dominant part of the portfolio. Proactively incorporating these considerations into the glidepath design and prudently growing capital over time helps to ensure that the portfolios are ultimately better positioned to manage those types of risks over the long term.

DE RANGO: A lot of this comes down to the volume and quality of the data that is available to us. As we get a clearer picture of the data and how to utilize it, we can have more robust discussions around considerations such as longevity and inflation. Just as an example, people

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– De Rango

generally refer to 65 as the typical retirement date. But in an era when people are living longer and retiring later, I don't know if we should necessarily continue to view age 65 as a “magical” end point to decide if the glidepath should continue to evolve or not. This is the type of discussion that we can have more holistically once we get a better understanding of the data.

How is the current economic volatility impacting plan sponsors approach to TDFs when it comes to asset allocation? What advice can you offer them?

KNOWLES: In the conversations that we're having, plan sponsors are being somewhat stoic about this whole thing. They appear to be staying the course, which is exactly what you would want to see in the current market environment and in the context of a target-date strategy that's designed for very long-term outcomes.

To us, economic volatility appears to be a good catalyst to remind sponsors about why diversification really matters when we think about designing, implementing, monitoring and evolving a strategic investment mix. Over the last decade, U.S. assets have been driving investment portfolios higher and leading to strong absolute returns for pretty much every target-date strategy. But for many, that recent experience has crowded out the longer-term history, one where U.S. equities haven't always outperformed.

RUBENYAN: Sponsors don't select a TDF looking at the current economic environment; they are looking, 30 or 40 years out, for a product that will help them manage risk and provide the appropriate income replacement ratio for their plan members.

During our manager performance monitoring meetings, clients sometimes expect the worst especially during periods when the equity markets have been declining. Yet when they look at the actual returns, they see that the majority of their members are invested in TDFs, most of which have generated positive returns despite the current economic volatility.

PILOTTE: What we're hearing from plans sponsors and their advisors is that this idea of suitability is back on the table. Over the past decade they haven't been focused on the risk side of the equation and we've seen glidepaths – particularly in the U.S. – get more and more aggressive, thanks to the focus on return and growth.

Now with the uncertainty and turbulence, people are stepping back and looking at their participant profiles. There's more focus on that near-retirement demographic and what we can do to make sure that they stay on track, stay invested and don't get derailed by a market shock that could eat into the great accumulation that's happened up to this point.

BEANE: The other thing to remember is that, for younger members, volatility can be beneficial. Given they have decades to invest, market fluctuations offer opportunities to help them accumulate assets at lower prices.

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– Knowles

As a fund manager, how do you account for the varying investor profiles at individual plan sponsors when building asset allocation strategies?

MARIAMO: By default, TDFs are one-size-fits-most, and I think most managers are probably just thinking about solutions for the average Canadian. But that's something plan sponsors feel increasingly uncomfortable about.

As an industry, we focus a lot on age 65 because that's when the average Canadian retires. But when you look into the data, roughly 30 per cent of Canadians are fully retired

before age 64 and then another 30 per cent of people are still working past the age of 69.

Then during the accumulation phase, we're also seeing a lot of irregular work and savings patterns, whether it's because of the nature of the plan sponsor's operations or because of the global trend of younger generations looking for career mobility, which means they're changing employers more often, switching industries, pursuing further education and taking extended personal or professional breaks. These are things that need to be recognized and accounted for when we're thinking about the Canadians that we're designing our solution for.

KNOWLES: It can't be the average. It needs to be the wide spectrum that is truly representative of the Canadian population.

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— Mariamo

One of our approaches is to develop personas that cover a wide range of different investor attributes. Whether it's different savings habits, retirement ages, job categories or whatever the case may be, having a very diverse sample size helps you to evaluate the trade-offs across the entire life-cycle journey.

Target-date providers should be comfortable living in the left tail in terms of their understanding of various uncertain scenarios. It's important to have an intimate understanding of less desirable attributes that could lead to unfavourable retirement outcomes, for example: low savings rates, people losing their job before they plan to, career mobility.

DELISI: Completely agree, we need to target the widest group possible to ensure we're improving outcomes for the vast majority and not a singular average member that ultimately isn't representative of member populations. While we certainly are aware of Canadian demographic data and conduct survey work, we take a capital

markets approach to glidepath design that emphasizes thoughtful and deliberate risk management throughout the glidepath to drive positive outcomes for the largest group of members possible. This approach doesn't anchor on specific — often stale — demographic information, but instead is very applicable to the actual reality facing plan members, as well as changes in capital markets that impact member returns.

Given different manager strategies and varying glidepaths, benchmarking remains a challenge for the target-date industry. What is your approach?

DELISI: A holistic approach that puts retirement-ready outcomes at the forefront would really be the ideal state. It's something the industry has been trying to solve for some time; but, without the certainty and uniform application you get with a defined benefit plan, this kind of metric remains pretty elusive.

As we continue to work towards that ideal, we believe traditional performance metrics — both benchmark-relative and peer-relative — and understanding the embedded risk throughout various points of the different glidepaths remain powerful comparators for plan sponsors to consider when assessing fit for their plan membership.

BEANE: Rolling returns analysis is also important, because it provides a more comprehensive view of how a manager performs across a variety of market conditions as opposed to static trailing returns, which only measure performance over a very fixed window. Given the extended bull market of recent years, it's critical to evaluate performance across full-market cycles. Look at peak-to-peak and trough-to-trough periods to really understand how strategies hold up in both up and down markets.



SPONSORED CONTENT

DE RANGO: I remember early on in my career when I was set to present at a due diligence meeting for a DB plan client. At a time when broad markets were in decline, our strategy was in negative territory in an absolute sense; however, it was outperforming nicely on a relative basis. I was looking forward to what I thought would be a positive meeting because the strategy was outperforming its benchmark over the time period in question. I got stumped when I was questioned about how this relative outperformance helps meet the pension plan's liabilities, especially given that absolute performance was negative at the time. I realized that beating a benchmark does not always translate into good news. It was an important lesson for me. While relative outperformance is great, ultimately, a relevant benchmark needs to be indicative of the goal that we're striving for.

If the goal of TDFs is to maximize the chances that a plan member reaches his or her retirement objectives, then I might suggest that looking at benchmarks and/or peer-group performance on an ex-post basis might not necessarily be the best way to gauge suitability of any given target-date portfolio. Just because most of us are familiar with current benchmarking methods does not necessarily make them relevant. I think we have an opportunity to do a better job of benchmarking TDFs.

BEVILACQUA: When plan sponsors are comparing individual managers, everyone has a different way to construct those benchmarks and then, on top of that, how they stack up against peers.

It's important for plan sponsors to take a step back and understand what risk their TDF managers are trying to assess or what's the key risk they're trying to mitigate for at that point in the life cycle.

Another challenge for plan sponsors is that we're always tied to the Statement of Investment Policy, which is driven by numerical aspects. But I think we're doing a better job at

taking more of a qualitative approach in how we assess these glidepaths.

PILOTTE: The way the plan sponsor writes the investment policy statement for the default investment makes or breaks what they end up deciding to do, so they need to think more strategically about how they assess the target-date solution.

Unlike other funds in the lineup, it's not about beating the S&P 500 or the Russell 1000 index.

Those shorter-term metrics don't capture everything we're looking for in a TDF. We can have all the best benchmarks in the world, but if those investment policy statements are just a carbon copy of every other asset class in the lineup, it doesn't matter.

What is your strategy when it comes to engaging with investors and preventing complacency surrounding their TDF allocations?

MARIAMO: As an investment manager, we feel we have a role to play in engaging plan members with relevant and useful content. For example, we record videos and webcasts for plan members to better understand the TDF that they invest in.

Another thing we can do is to reframe what a TDF strategy is outside of just being the default fund and connecting it to a broader planning effort. You're investing in a TDF because you've decided to delegate investment decisions to a professional manager, but then there's still a journey that needs to be followed in terms of saving and planning for retirement to achieve their long-term objectives.

RUBENYAN: The sponsor and the record keeper play a bigger role. The plan sponsor can look, not just at the performance of a particular TDF, but also at what kind of retirement readiness outcome it is expected to generate and, more importantly, what percentage of their members are going to be ready to retire at a certain age. Then they can work with the record keeper to deploy educational material that takes a holistic look at all the key factors that need to be aligned, including encouraging increased contributions, selecting the appropriate target date fund and reducing withdrawals from the plan, et cetera, in order to ensure that participants meet their retirement objectives.

BEVILACQUA: The onus is definitely on the sponsor to build some of this education into a story that each participant along their journey has to think about. That could be through persona-based communication, which is something that has resonated with the market.

Changing the messaging around the benefits of TDFs and how they can be incorporated in more flexible plan designs are things that the market should also be thinking about. For example, we're focusing more on helping plan members around not only retirement savings, but short- and medium-term goals. The vintage might look different if a member has a short-term perspective on their tax-free savings account or non-registered assets that they might be investing in.

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— **Pilotte**

In your opinion, is it optimal to incorporate private alternative assets into TDFs? Can these assets help enhance risk-adjusted returns for plan members?

RUBENYAN: The data we have show that in 2019, 66 per cent of TDFs included an element of alternative assets. In 2024, that number has gone up to 83 per cent and the bulk of the increase can be attributed to direct investments in alternatives. Private alternative assets have the potential to enhance risk-adjusted returns and this is one of the main reasons they are being included at higher allocations.

KNOWLES: We need to distinguish what type of alternatives we're talking about here. A lot of times, people talk about alternatives in the conventional sense of real estate investment trusts or listed infrastructure, which we believe is part of the broad market exposure that you're getting when you invest in the S&P 500.

From an investment perspective, private alternatives are where we see the most bang for your buck, in terms of the ability to offer enhanced diversification against the public side of an investment portfolio, which remains the vast majority of target date portfolios.

I would encourage plan sponsors to test their investment managers' thinking if they're including alternatives. The benefit is you get smooth returns from having private alternatives, but in the context of a TDF with liquidity considerations, you need to go one, two, three steps deeper to really understand the risk that it introduces to the portfolio. Alternatives are generally advertised as a free lunch in terms of improving risk adjustment returns, but that's certainly not the case.

BEANE: Privates are often promoted for their lower correlation, higher return potential and ability to enhance risk adjusted returns, but there are studies out there suggesting that it may be overstated, especially over longer time horizons. Privates appear less volatile due to infrequent pricing. That smooths the return and understates the potential true risk, which has been referred to as "volatility laundering." When you adjust for those distortions, privates exhibit higher volatility, increased beta and correlation and diminished alpha, so there is a trade-off there.

Liquidity is something else you really have to think about, because locking up capital makes it difficult to rebalance. If you're allocating to privates in a volatile period, TDF managers might have to sell public assets for liquidity, which could increase the weight for private assets in the portfolio well beyond what the manager intended.

BEVILACQUA: When you're talking about increasing utilization, you have to take that a step further and look at where in the glidepath these alternatives are being allocated to. Risk-adjusted returns are important, but you need to understand what you may be giving up, possibly, on the younger side of things. That's an important part of the conversation when we're assessing how managers are incorporating alts into their portfolios.

PILOTTE: Some large mega plans have a lot of comfort with alternatives in their custom target-date solutions, because they've been using them in their DB plans for decades. But for the smaller plans or the retail audience, I think there's a big discussion on suitability that needs to be had.

Then there's the cost impact. This is such a fee-sensitive area for plans, and just embedding more cost into that default option is a tough one for many plan sponsors to accept.

KNOWLES: We've been maybe a little bit more negative on alternatives than I would have expected, so I'll try to offer a little bit of balance. Canada is the leader in this globally and we'll probably continue to be, given the success that we've had in the DB environment. Despite all of the risks that we've appropriately discussed, the smoothed investment return is what you actually experience in your investment account, and there is an undeniable benefit to that in the long term for creating value and accumulating wealth. Introducing alternatives into a TDF also allows members to scratch that itch in a professionally managed fund, rather than via an a la carte offering.

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GLOBAL LEADER IN
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– Knowles

What role does environmental, social and governance or sustainability considerations play in your TDFs?

RUBENYAN: Many regulatory bodies and standards, including CAPSA, recognize that ESG factors can be material to long-term investment performance. Incorporating ESG analysis can help identify risks and opportunities that might not be apparent through traditional financial metrics alone. The key is to identify and continue to discover those particular ESG metrics that are material to financial outcomes. For example, it could be understanding the level of female representation or the

level of diversity of decision-makers on boards, or it could be understanding the carbon intensity of your investments. There are a number of meaningful metrics to monitor that could have an impact on outcomes.

KNOWLES: I know that the conversation has been clouded more and more over the years, but all ESG really is, is an assessment of risks and opportunities that are out there in the marketplace, formalized under a particular name.

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ESG FACTORS CAN BE MATERIAL TO LONG-TERM PERFORMANCE, HELPING IDENTIFY RISKS AND OPPORTUNITIES TRADITIONAL METRICS MIGHT MISS.

– Rubenyan

There's no denying that in the long term, through a sustainable transition, there are going to be winners and losers, both at the regional level and the underlying security selection level. That manifests itself as risks and opportunities for us to try and capitalize on as target-date investors.

Through history, this has always been part of the research mosaic

that an active investment manager should be taking into consideration to capitalize on, or risks to avoid as target date investors.

What is the most effective way to communicate risk considerations with investors?

DE RANGO: I think it's important for the plan sponsor to understand the demographics of their employee base, because if you ask five people what risk means to them, you might get five different answers.

I think we can do a better job of educating plan members and it should involve collaboration between record keepers, plan sponsors, consultants and fund managers.

KNOWLES: Talking about risk is the fastest way to lose an audience, especially one that maybe doesn't want to be there and was only incentivized to attend by a pizza lunch. We have to reorient that conversation away from risk, towards opportunity and how can we achieve positive retirement outcomes. It's about appropriate expectation

setting, ensuring plan members understand it's not just about the investment performance of a target-date strategy, but also about all the things that can be done to improve your odds of a positive retirement experience.

BEVILACQUA: The aim here is to tie some of these messages together in a holistic way and make it more digestible for plan members when they're thinking about managing their portion of their DC journey, whether that's building some of these things into persona-based investments or figuring out how we incorporate some of these messages around investments, risk appetite or the purpose and benefits of TDFs into other decisions they're making.

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– Bevilacqua

Where does the TDF industry go from here?

BEVILACQUA: Hopefully we get to conversations and assessments of retirement readiness. I think committees are more comfortable looking at TDFs or even their DC plans holistically in terms of a retirement ratio or an income replacement ratio, rather than how does our plan stack up against peers. The main driver of all this has got to be whether it's meeting the needs for our employees.

DE RANGO: I look back to the days where DC plans were all about helping members build their own portfolios, which we eventually learned was fraught with problems: namely, lack of engagement.

When target risk portfolios came into the frame, we thought it was going to solve most engagement problems. Just when we thought we had it all figured out, TDFs came around.

We're in an exciting time in this industry of ours. We have an opportunity to take TDFs and evolve them into something that makes a whole lot more sense for the CAP marketplace.

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WE'RE IN AN EXCITING TIME IN THIS INDUSTRY – WE HAVE AN OPPORTUNITY TO EVOLVE TDFS INTO SOMETHING THAT MAKES MORE SENSE FOR THE CAP MARKETPLACE.

– De Rango

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