

PRC Symposium

Saving and Retirement in an Uncertain Financial Environment

Discussant:

Nikolai Roussanov (Wharton)



Two Papers...

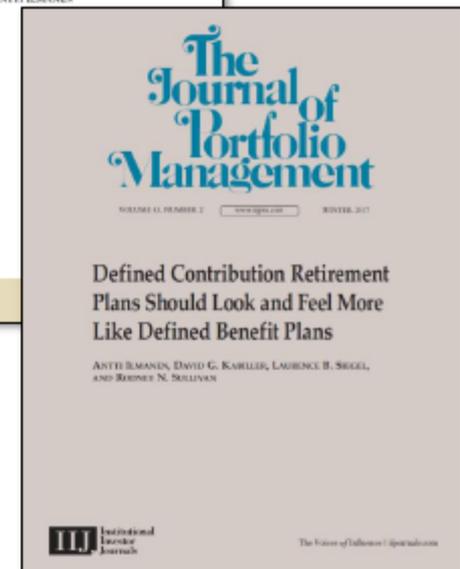
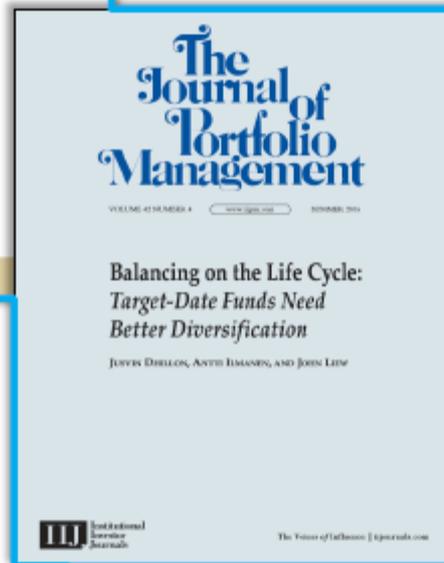
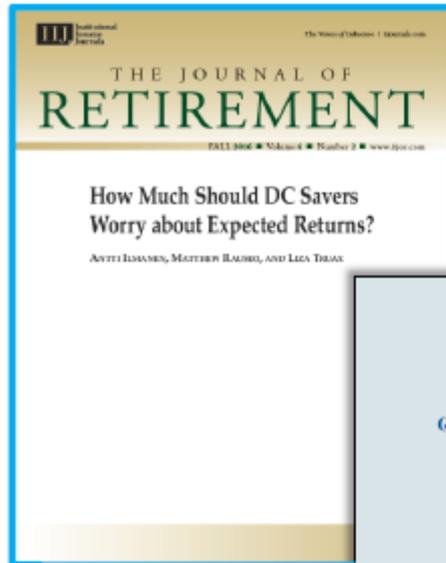
- How Persistent Low Expected Returns Alter Optimal Life Cycle Saving, Investment, and Retirement Behavior

Vanya Horneff, Raimond Maurer, and Olivia S. Mitchell

- Smarter Saving and Investing in a Lower Expected Return World

Antti Ilmanen

... or is it Five?



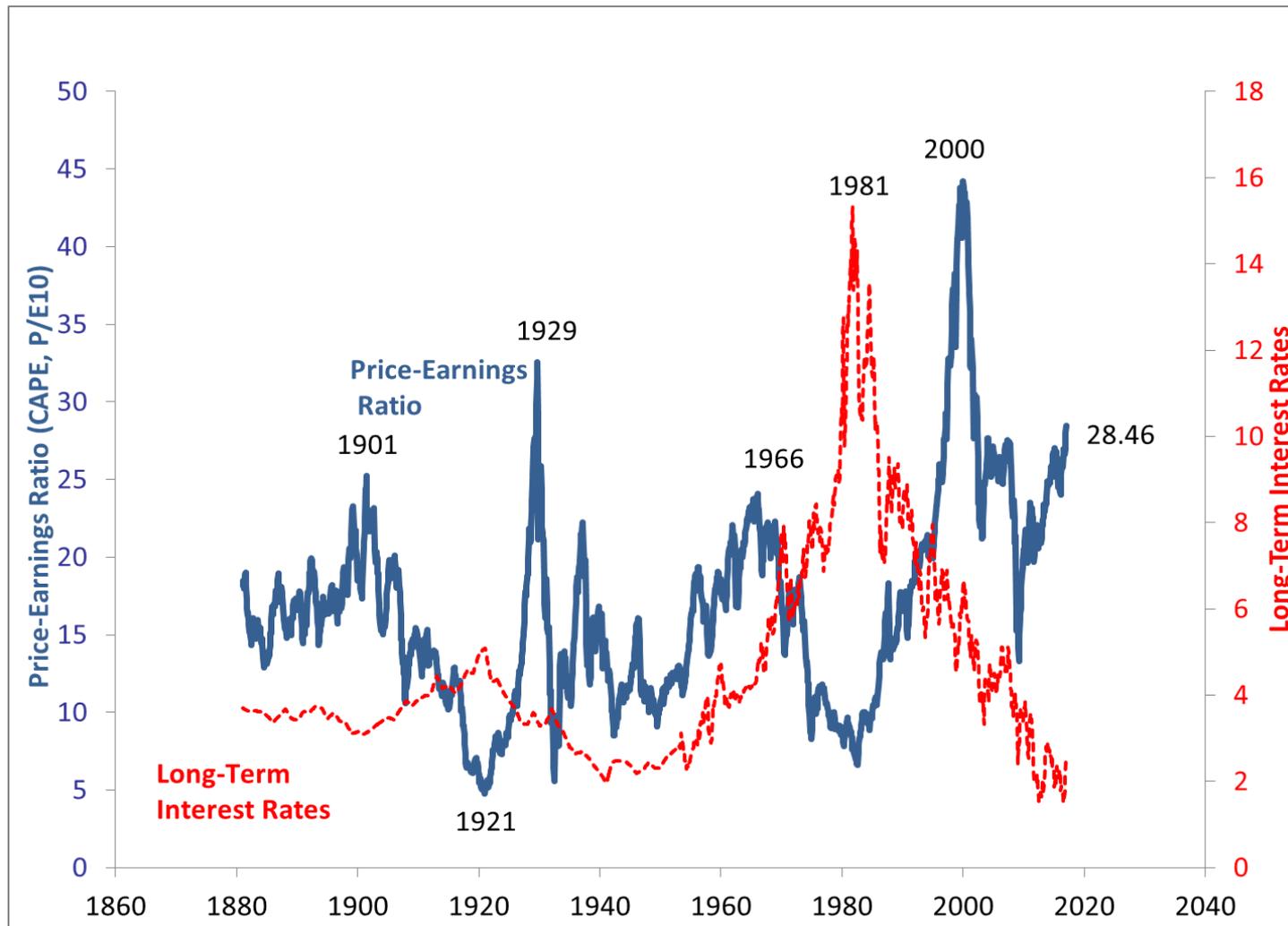
Horneff, Maurer, and Mitchell – main takeaways

- Detailed life-cycle portfolio model incorporating TDFs inside 401k plans (as well as stocks and bonds), income growth, tax
- “Counterfactual” analysis of reduction in risk-free interest rate
- Lower rates imply claiming retirement at older age
- Lower rates imply smaller retirement “nest eggs”
- Tax-advantaged accounts less beneficial

Some comments...

- Do people save more when rates are lower? (or less?)
income vs. substitution effects
- Does income grow at the same level when rates are lower?
macroeconomic perspective – “secular stagnation”?
- What about expected returns on stocks?

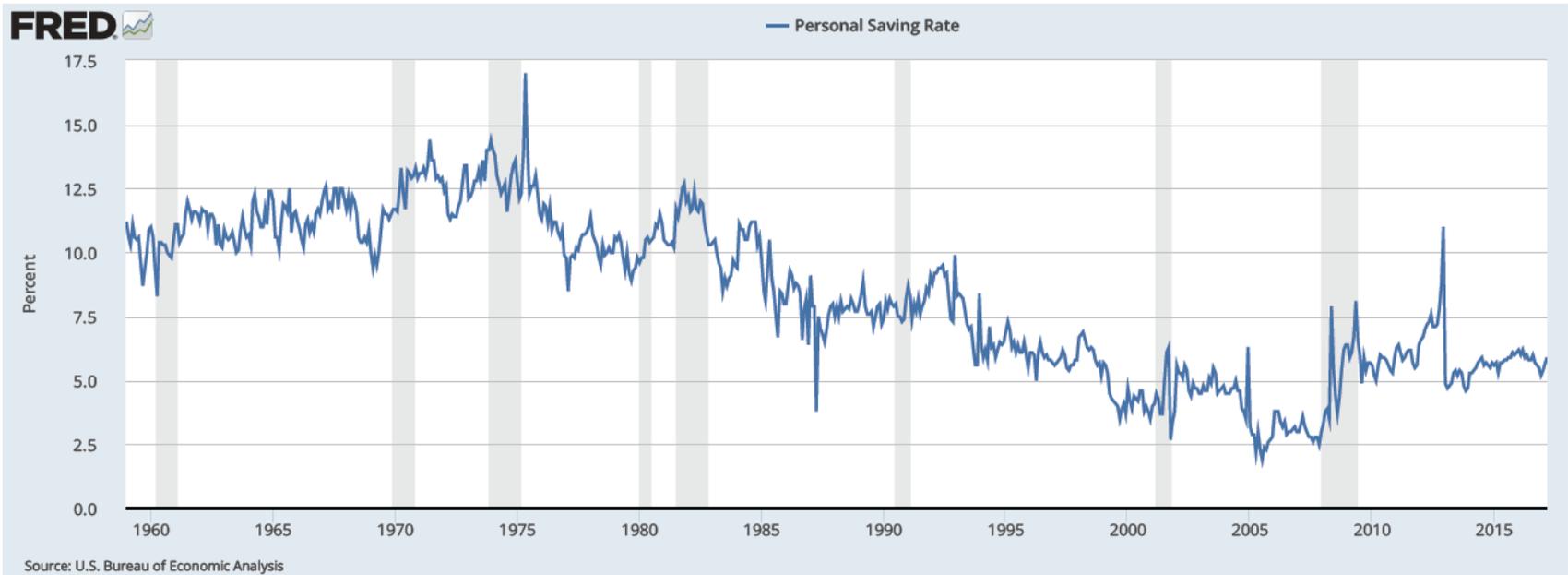
Shiller's Cyclically-Adjusted Price/Earnings (CAPE)



Ilmanen's (four papers) take-aways

- Lower expected returns require dramatically higher saving rates!
- Need to go beyond 60/40 or TDF allocation!
- Risk-parity, factor investing, alternatives/trend following
- Diversification is (nearly) free lunch, but ARPs are not!

Higher saving rates aren't likely (soon)



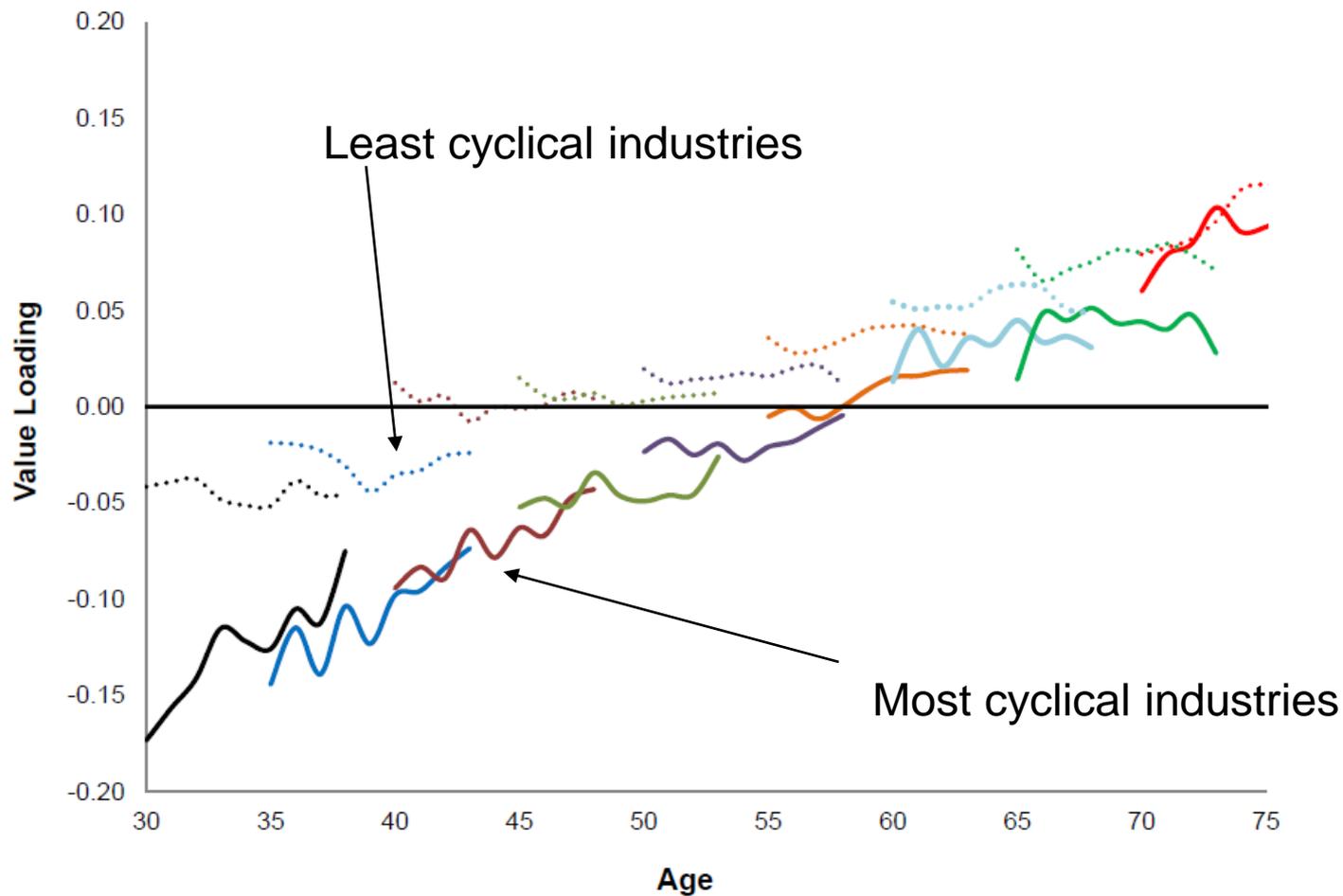
How attractive is factor investing?

- Depends on the pre-existing risk exposures of investors
- Why are these factor risk premia there in the first place?
- Are they purely behavioral/mispricing or risk-based?

For example, what if value is a compensation for

- ... own company/business risk
- ... long-run income/consumption risk
- ... skill obsolescence/technological displacement risk

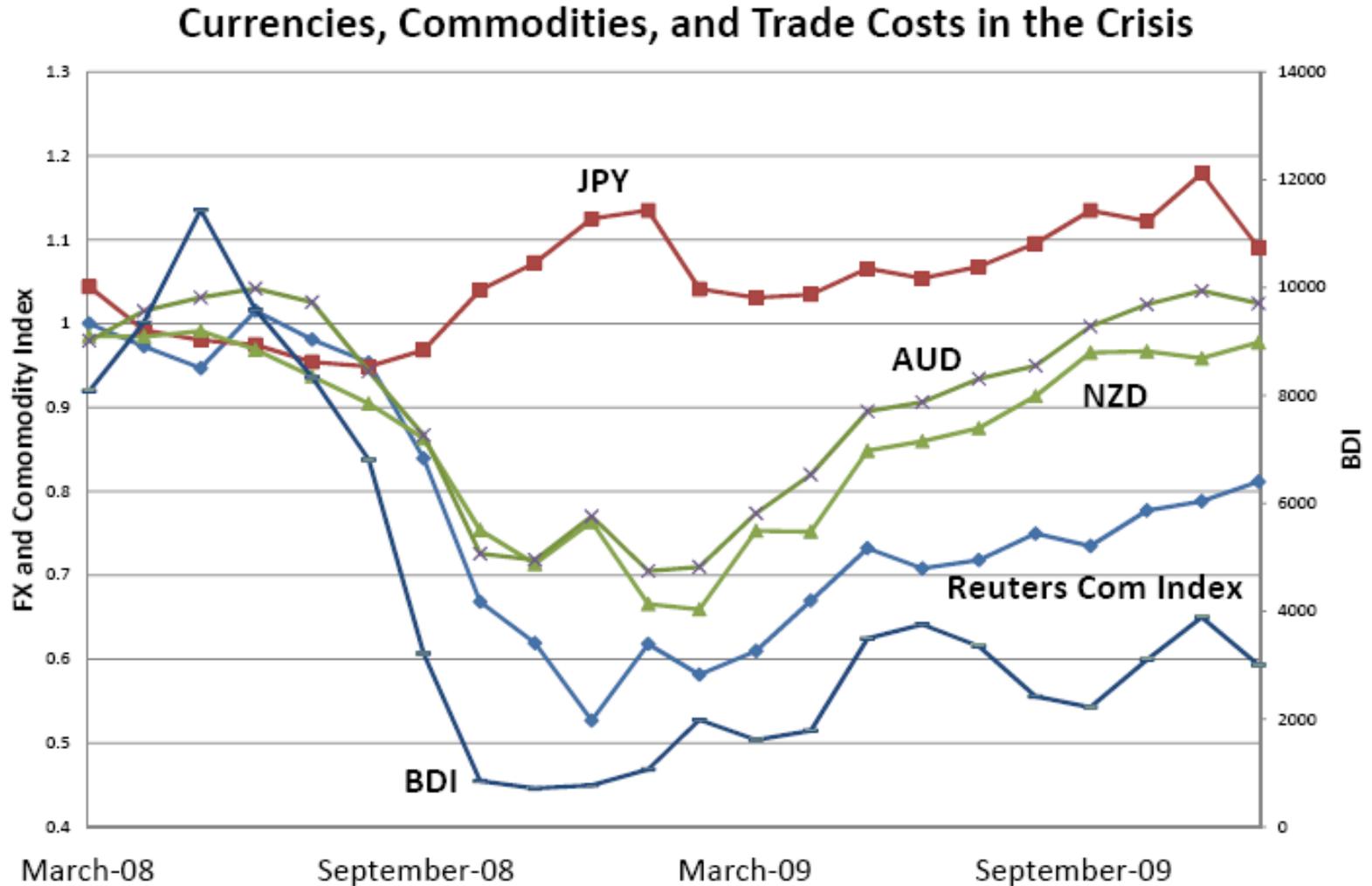
Value “Ladder” in Portfolios of Swedish Workers



Risks of other Alternatives/Factors?

- Momentum (timing is everything)
- Carry (across asset classes)
- Defensive (low volatility, high quality)
- Commodities (long-only vs. ARP)
- Illiquid assets (PE, real estate, etc.)

FX Carry and Commodities Exposed to Global Cycle

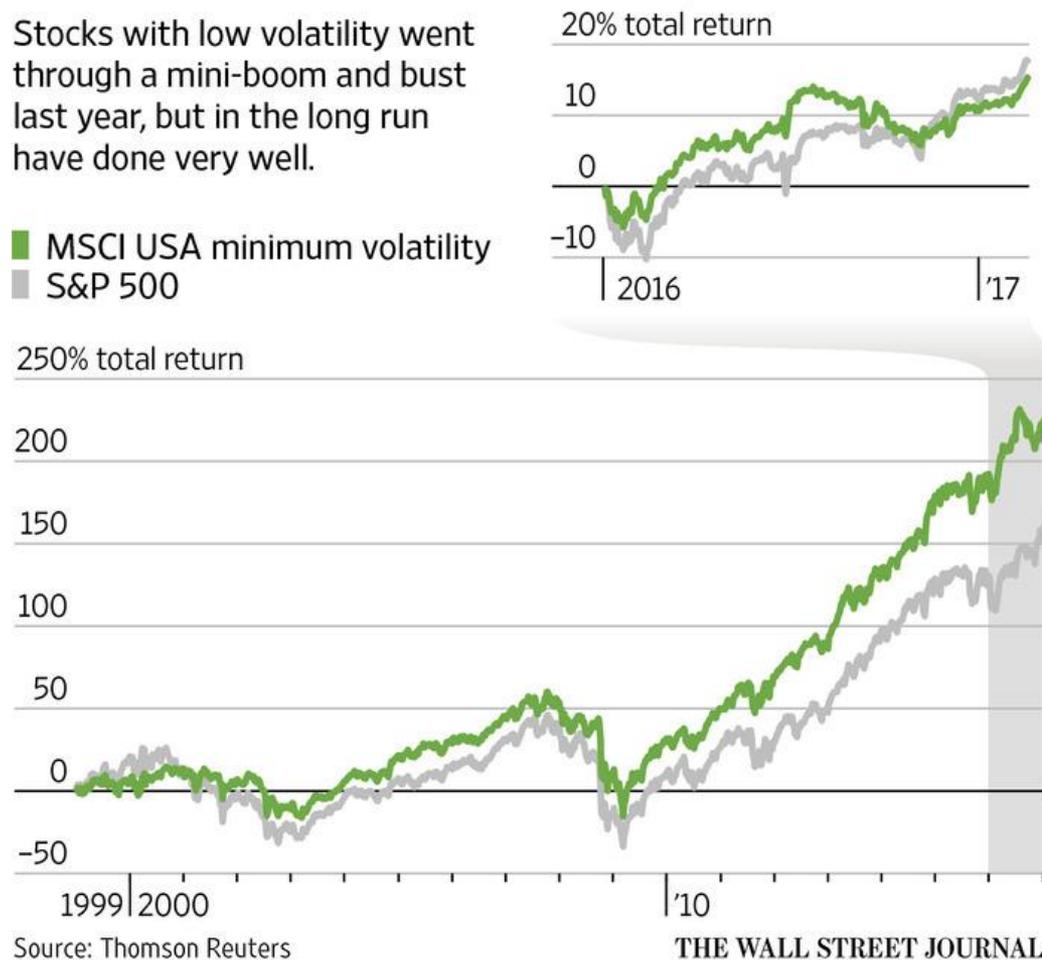


How Defensive?

Low Volatility Proves Volatile

Stocks with low volatility went through a mini-boom and bust last year, but in the long run have done very well.

■ MSCI USA minimum volatility
■ S&P 500



Summary

- Factor investing has its role ...
- ... but no silver bullet
- Retirement investors will need to save more ...
- ... and work longer