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SOLUTIONS FOR A LIFETIME

TIAA-CREF was created in 1918 to solve one pressing problem: people in higher education had great difficulty retiring because they did not have a secure source of income after they stopped working. Over the subsequent 90 years as TIAA-CREF expanded its ability to serve the broad financial needs of those whose work serve the greater good, retirement security remained central to the company's mission. This week's Market Monitor focuses on:

- Why lifetime retirement income was central to TIAA-CREF's mission;
- How the corporate 401(k) model challenged the TIAA-CREF lifetime retirement income model; and
- How TIAA-CREF is reaffirming its commitment to lifetime income.

The goal of any retirement system should be to ensure that a retiree's income will be adequate *and continue throughout his or her remaining life*. From the beginning, TIAA-CREF's defined contribution system was created and managed to ensure lifetime retirement income through individually owned accounts. TIAA, with its fixed-income and alternative investments, was not only designed to provide a contractual guaranteed minimum rate of return on contributions and accumulated assets, it also supported a variety of annuities, many of which guarantee lifetime income to retirees. Simply, participants who purchase such an annuity with savings they accumulate during their working years will receive income for as long as they live.*

* Annuity products supported by TIAA are only available to plan participants, and liquidity restrictions apply.



CREF was created to deal with another specific retirement income challenge. Following WW II, the ravages of inflation took a terrible toll on retirees whose income was based on savings that had been invested in low interest bonds during the Depression. CREF's equity investments allowed retirees (and those who were still employed) to take more risk, but also to have a better chance of receiving retirement income that would beat inflation over the long run. The CREF Stock Account was the first variable annuity, which combined equity investments with the option of income for life.

For many decades, until the late 1980s, TIAA-CREF was the dominant defined contribution model. It stacked up well against the major alternative — public and private defined benefit plans. Both defined benefit plans and TIAA-CREF's defined contribution plans placed central importance on guaranteed lifetime retirement income (in the case of the defined benefit plan, income was based on years of service and employment income).

However, in the latter part of the 20th century, the growing popularity of the 401(k) model began to challenge not only the defined benefit model, but also TIAA-CREF's version of the defined contribution model, including the importance of income guarantees.

The 401(k) defined contribution model was originally developed to supplement the corporate defined benefit plan. The 401(k) shared with TIAA-CREF an emphasis on individually owned contributions and accumulations and individually directed investment options. But the 401(k) model also offered two fundamentally new features. One was an enormous expansion of choice. Individuals could choose whether and when to enroll, how much to contribute, which of a large lineup of mutual funds to invest in, and how to take retirement income, including the option of a lump sum. The second feature was the opportunity to accumulate wealth. The 401(k) model placed supreme importance on creating and owning wealth rather than ensuring an income stream.

What most 401(k) plans didn't offer was the choice of guaranteed lifetime income. Instead, individuals could choose to use their pension wealth almost any way they wish. They could purchase an immediate annuity on the open market or, more likely, manage their own withdrawals over the entire period of their retirement.

The rise of the 401(k) model raised significant challenges for TIAA-CREF as its participants began to demand 401(k)-like choices for themselves. Beginning in the late 1980s TIAA-CREF began to create new investment options, expanding the available choices from two in 1987 (TIAA and CREF Stock) to over 45 accounts and mutual funds today. In 1990, it also eliminated the annuitization requirement so that retirees could, depending upon institutional plan rules, choose among annuity income, various forms of account withdrawals, or even lump-sum withdrawals. In certain respects, in its communications with participants, TIAA-CREF also began to place somewhat less emphasis on guaranteed income and more emphasis on 401(k)-like accumulating wealth.

The result is that today many TIAA-CREF plans have come to look more like corporate 401(k)s. Now, many participants experience the benefits of greater choice as well as more of the responsibilities, costs, and risks. For example, today fewer participants choose guaranteed lifetime income, in favor of managing their own withdrawals. With that choice, they also face the risk of running out of money, a risk that would be eliminated by a lifetime annuity.

Recently, as the baby boomers began to retire 401(k) providers and sponsors have begun to discover retirement income. Fund companies have begun to create retirement income funds and recommend withdrawal rates. Some sponsors are beginning to ally themselves with annuity providers. And public discussions of retirement are beginning to include consideration of income and longevity.

Fortunately, TIAA-CREF is uniquely positioned for this renewed emphasis on retirement income in place of the 401(k) model's emphasis on wealth accumulation. TIAA-CREF pays out over \$6 billion to 300,000 retirees, each year. Our organization has been providing guaranteed retirement income for 90 years and is the world's most experienced variable annuity provider. It has a deep understanding of longevity risk and long-term investing. Perhaps most important, TIAA-CREF has, for most of its existence, made ensuring lifetime retirement income the center of its financial services mission.

TIAA-CREF is in the process of reaffirming its commitment and mission to ensuring retirement income. It has recently introduced a retirement income fund designed to dovetail with its lifecycle funds. It continues to offer a full range of guaranteed and variable annuities and is actively engaged in designing new low-cost, easy-to-understand, retirement income options. These efforts serve to renew TIAA-CREF's position as the national leader in providing lifetime retirement income to those in higher education, medical services, and other nonprofit organizations.

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TIAA-CREF is a national financial services organization and the leading provider of retirement services in the academic, research, medical and cultural fields with over \$400 billion in combined assets under management. Further information can be found at www.tiaa-cref.org.

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