

Is TIAA-CREF Safe?

The company's financial health seems to be distinct from the recent declines of your investments

By PROFESSOR PENNYWISE

"Since many professors have TIAA-CREF as the core of their retirement plan," writes a reader in response to Pennywise's depiction of the financial crisis (*The Chronicle*, December 19, 2008), "please do an in-depth report on its financial health and how solid its accounts are."

In analogous spirit, Laurie Fendrich, professor of fine arts at Hofstra University, posted a brilliant mock-populist rant on *The Chronicle's* Brainstorm blog under the title "Someone's Gotta Pay." Fendrich recounts an evening when, sipping a glass of merlot, she fantasized over who to sue for "the decline in value in my TIAA-CREF retirement portfolio." Eventually she settles on her campus TIAA-CREF rep for defrauding her "by giving me several pamphlets written in Aquitanian, and insisting on speaking only Aquitanian whenever we would meet — even though he knew full well I could barely speak a word of it."

Let me attempt, without recourse to Aquitanian, to shed light on the company's stability. Are our investments with TIAA-CREF safe? "Our" is the mot juste. Full disclosure: Most of Pennywise's vast and imposing financial empire is invested with TIAA-CREF. My wife and I both have retirement accounts with the firm, multiple ones in my case, and I own a TIAA-CREF life-insurance policy.

There are two dimensions to the question of whether TIAA-CREF is safe. The first is the stability of the company itself. The second is the risk and volatility of its specific products. It is important to differentiate between the two.

Let's start with the company. TIAA-CREF boasts a long track record, dating to 1918, when the Carnegie Foundation first created the Teachers Insurance and Annuity Association, supplemented in 1952 by the College Retirement Equities Fund. For 90 years, TIAA-CREF has provided financial services to college professors and staff members. That longevity is reassuring; it means that TIAA-CREF survived the Great Depression. (So too, of course, did General Motors, founded in 1908 and now hanging by a bailout thread.)

Congress eliminated TIAA-CREF's tax-exempt status in 1998¹, but the company still conceives of itself as nonprofit. It is run by a board, not private owners. Its profits are

¹ The Teachers Insurance and Annuity Association of America (TIAA), a stock life insurance company, is a wholly owned subsidiary of the TIAA Board of Overseers, a New York not-for-profit corporation. By the terms of its charter, TIAA exists to help meet the financial needs of the individuals and institutions it serves on the best terms practicable, all without profit to the corporation (TIAA) and its stockholder (the Board of Overseers). In practice, this means that profits are distributed to policyholders in the form of dividends over the lifetime of their association with TIAA, or remain available for purposes that the Trustees of TIAA determine can help uphold TIAA's mission. TIAA also does not have to manage the short-term earnings expectations that confront publicly held

either kept by the organization — used for technological upgrades, underwriting announcements on National Public Radio, or whatever — or distributed back to insurance policyholders and retirement-plan participants. This self-conception as "nonprofit" does not mean that TIAA-CREF does not aspire to make money. Quite the contrary. Its executives are well-compensated. However, unlike the investment banks that exploded in sequence over the past two years, TIAA-CREF is not traded on Wall Street. Because it has not gone public, it has had little earnings pressure of the kind that led much of American finance into unsustainable securitization practices, causing our present mess.

In fact, TIAA-CREF has a reputation for sound, sober judgment. In journalist Roger Lowenstein's book *Origins of the Crash* (2004), a post-mortem of the tech and telecom bubbles, he supplies a fascinating footnote on TIAA-CREF while telling the tale of the rise and fall of Enron. For those who have forgotten, Enron was a giant Texas-based energy company whose stock shares traded as high as \$90 in 2000 before revelations of its accounting skullduggery reduced it to ashes. One of the few analysts to call Enron's bluff was Kim Schnabel, a TIAA-CREF analyst. "Schnabel courageously recommended that TIAA-CREF's portfolio managers sell their Enron shares," writes Lowenstein. "TIAA-CREF was one of the few major fund organizations not to get burned."

The company ranks at 86 in the Fortune 500, making it a giant. The rest of the Fortune 500 list, however, demonstrates that bigness does not guarantee stability: GM is fourth, Citigroup eighth, AIG 13th, and so on. (The latest list was determined before the recent implosion.) Nevertheless, TIAA-CREF's revenues of \$27-billion and profits of \$1.4-billion make it one of the largest life-insurance firms in the country. TIAA-CREF has hundreds of billions of dollars in assets under management. It serves more than three million individual clients at more than 15,000 institutions in the academic, medical, cultural, and nonprofit fields — all loaded with high-income professionals in sectors that have held up relatively well in comparison to manufacturing or retail. The strength of this client base implies a steady revenue stream, a positive indicator for TIAA-CREF's permanence.

The four credit-ratings agencies² all give TIAA-CREF their highest possible ratings: A++ from A.M. Best, AAA from Fitch, Aaa from Moody's, and AAA from Standard & Poor's. That would seem conclusive, except for the troubling fact that Moody's gave Lehman Brothers an A only a month before it collapsed. All of the rating agencies awarded triple-A grades to the collateralized debt obligations now seen as toxic. The reliability of the agencies' research has come under fire because their revenue depends on the very companies they rate.

insurance companies. The College Retirement Equities Fund (CREF) is a New York not-for-profit corporation. CREF operates at cost (i.e., without profit), with investment returns passed through to participants and reflected in account asset values. CREF funds and accounts are managed by a subsidiary of TIAA. Since 1998, both TIAA and CREF have been subject to federal income taxation following a decision by Congress to end the organization's tax-exempt status under Section 501(c)(3) the Internal Revenue Code.

² Please note the discussion of ratings above does not apply to TIAA-CREF, but to TIAA, as an insurance company. These ratings do not apply to variable annuities, mutual funds, or any other product or service not fully backed by TIAA's/TIAA-CREF Life's claims-paying ability. A++, A.M. Best Company (as of 9/08); AAA, Fitch Ratings (as of 8/08); Aaa, Moody's Investors Service (as of 7/08); AAA, Standard & Poor's (as of 8/08) – the highest possible ratings from these independent analysts.

It is as if TIAA-CREF had been given straight A's by four well-known grade inflators. Does it follow that TIAA-CREF did not deserve the grades? Of course not. In fact, very few companies receive top marks from all four ratings firms.

Ultimately, the clearest indication of the stability of TIAA-CREF may be its absence from this year's headlines and news reports. Sixteen months into the massive shakeout that has reduced many corporations to beggary, TIAA-CREF has not requested a single penny from Washington.³ The company vows — and its financial statements would appear to confirm — that it had minimal exposure to the subprime loans that occasioned this crisis. All indications are that TIAA-CREF is far sounder than the average American financial provider today.

Given that TIAA-CREF seems sound, you might ask, why are my TIAA-CREF balances declining? That requires that you understand your holdings. If your TIAA-CREF assets are in a university-sponsored retirement plan, they are annuities. Any money you invested in TIAA Traditional Annuity⁴ has not, in fact, declined, since that account guarantees the principal — what you put in — and provides a return to boot.

Most TIAA-CREF contributors, however, probably put at least some contributions toward variable annuities. "Variable" means fluctuating. The value of those instruments moves up and down based upon the general markets for, say, stocks or real estate. If and when a recovery materializes, look for them to rise again.

Do not, in the meantime, conflate volatility with risk. Simply because your variable accounts' value has bounced downward in this severe downturn (volatility) does not mean the whole amount you have invested is in jeopardy (risk). You will only risk a loss if you lock in the decline by selling out now, while your accounts are low. Your declines at the moment are paper declines that may be offset by paper gains later — if you have patience.

As for Pennywise, I continue to put money into my university-sponsored TIAA-CREF retirement plan. I have confidence — not certainty, for we live in uncertain times — in the staying power of TIAA-CREF. In a future column, I will try to lay out your TIAA-CREF options in plain English, as opposed to Aquitanian. Feel free to send along any specific questions you'd like clarified. Until then, I recommend that you put on some Telemann, close your eyes, and keep sipping that merlot. I risk the conjecture that doing so may reduce the volatility of your mood.

³ Teachers Insurance and Annuity Association of America (TIAA) is participating in TALF, a Federal Reserve program which aims to get credit flowing to consumers and improve the economy. TIAA-CREF's two eligible money market funds (TIAA-CREF Funds Money Market Fund and the TIAA-CREF Life Money Market Fund) participate in the U.S. Treasury's Money Market Guarantee Program.

⁴ A guaranteed annuity backed by TIAA's claims-paying ability, TIAA Traditional guarantees your principal and a minimum interest rate (typically between 1 and 3%) plus it offers the opportunity for additional amounts in excess of the guaranteed rate. These additional amounts, when declared by the TIAA Board of Trustees, remain in effect for the "declaration year" that begins each March 1. TIAA has credited additional amounts of interest every year since 1948. Any guarantees under annuities issued by TIAA are subject to TIAA's claims-paying ability. Payments under CREF and the TIAA Real Estate Account are variable and will rise or fall based on investment performance.

Professor Pennywise is the pseudonym of a professor in the humanities at a major public university in the Midwest who is merely a frugal academic, not a financial professional. Questions may be sent to professorpennywise@yahoo.com. For an archive of his previous columns, see http://chronicle.com/jobs/news/archives/columns/academic_assets.

Please note all TIAA-CREF investment products are subject to market risk.

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