

RETIREMENT

Want to Make Your 401(k) More Like a Pension? Do This.

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An income annuity will send you a monthly check for the rest of your life, much like a pension.

ILLUSTRATION BY LYNNE CARTY/BARRON'S STAFF; DREAMSTIME (2)

Over the past 40 years, 401(k)s have supplanted pensions. Now some asset managers are trying to make these retirement savings plans act more like pensions.

From 1980 through 2022, the proportion of private industry workers participating in [defined benefit](#)  pension plans fell to 15% from 38%,


according to the [Bureau of Labor Statistics](#) . Workers have been told instead to contribute to 401(k) plans to have a secure retirement, and most people with access to one do contribute.

The bigger challenge is what to do with these assets once they retire. Pensions gave retirees predictability—a guaranteed income stream that made it easy to understand how much they could spend. Social Security benefits provide lifetime income, but they represent just [30% of income](#)  for people 65 and over.

With longer life expectancies and unpredictable market returns, a lot of baby boomers are “feeling insecure about retirement,” says Jason Fichtner, head of the Retirement Income Institute. “They’re looking at these market cycles and asking, can I really afford to retire? How do I make sure it lasts through retirement, which could be 30 years?”

Some asset managers and retirement plan sponsors are trying to answer that question by including an option for guaranteed lifetime income in defined-contribution plans.

“We’re trying to replace that pension income,” Fichtner says.

Demographics make the issue especially salient now. The U.S. population 65 and over grew nearly five times faster than the total population did between 1920 and 2020. Americans’ confidence that they will be able to live comfortably through [retirement has declined](#) , while the [median value of retirement accounts](#)  for people 55 to 64 was just \$185,000 as of 2022.

Guaranteed Income in Your 401(k)

One catalyst for the push for lifetime income is the 2019 Secure Act,

which made it easier for employer 401(k) and other plans to offer guaranteed income options provided by life insurance companies.

“The recent shift in market environment has only exacerbated that trend,” says Brendan Curran, head of defined contribution for the Americas at [State Street](#) Global Advisors. The company will begin offering its IncomeWise product, an index-based target-date fund with the option for participants to convert their savings into lifetime income, in 2025.

State Street declined to say what the payout rate would be for the coming product. But you can get a rough idea of pricing by going on a site like [immediateannuities.com](#), which sells income annuities to the general public. Say you’re a 65-year-old single woman with \$100,000 in your 401(k)). You can buy an annuity from an insurer with a top credit rating that will pay you more than \$600 a month for the rest of your life.

Fidelity is rolling out an existing lifetime income product more broadly in 2024, which allows employees to convert a portion of their 401(k) savings into guaranteed income for life by purchasing an annuity. [BlackRock](#)’s LifePath Paycheck is a target-date fund that gives participants a similar option. So far, 14 large plan sponsors are in the process of implementing the strategy in their 401(k) plans, says a BlackRock spokesperson.

TIAA, which manages money for nonprofit institutions and their employees, has been offering an annuity option inside 403(b) plans for years. In August Nuveen, an asset manager owned by TIAA, launched a similar product for 401(k)s—a fixed income annuity embedded within a target-date fund, called Nuveen Lifecycle Income

Series.

“We are seeing incredible demand and growth for target date offerings that embed a fixed-income annuity,” says Brendan McCarthy, head of retirement investing at Nuveen.


Higher Annuity Payouts

Some strategists foresee a period of higher-for-longer interest rates as the Federal Reserve continues its fight against inflation, along with lower overall market returns. A traditional 60-40 portfolio may not return as much over the next 10 years as it did in the decade that ended in 2021, says Chris Nikolich, head of glide path strategies in US Multi-Asset Solutions at AllianceBernstein, which offers clients a target-date fund with an annuity option.

“Certain annuities...on top of a balanced portfolio can effectively meet the needs of a wide number of individuals,” Nikolich says. “It gives a guarantee of income in retirement that’s so important, but doesn’t require you to surrender your assets or give up growth potential.”

In addition, higher interest rates have boosted payout rates on annuities since payouts are largely based on interest rates and life expectancy. “Within the fixed deferred annuity market, we are seeing payout rates 80% higher from two years ago,” says Curran of State Street.

Just Don’t Call Them Annuities

[Annuity sales](#) have [risen](#)  in the past year, but hey still have a bad reputation. Many consumers think of them as overly complex investments with high fees and low liquidity. The annuities being offered through retirement plans are simpler to understand and have

lower fees, says Fichtner.

“If you ask someone, would you like to have a paycheck for life, the answer is yes. Would you like to make sure you don’t outlive your savings? Yes. Would you buy an annuity? They say no,” Fichtner says.

However, Fichtner’s research found that nearly twice as many participants prefer a retirement plan that offers a mix of investments and lifetime income to one that uses only investments or only a pension to provide income in retirement.

He wrote: “Workers value knowing how much they can safely spend more than any other characteristic of a retirement savings plan.”

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