Bellwether CONSULTING

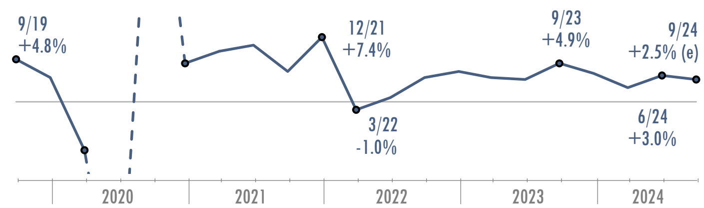
Your Quarterly Update on the Financial Markets
September 30, 2024

MARKET Recap

The US Economy: "Beginning Our Descent"

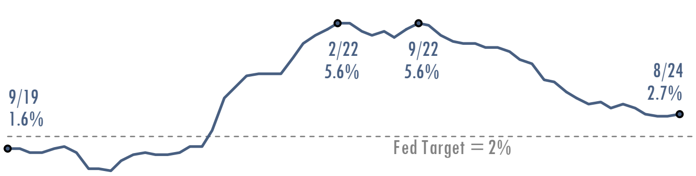
Economic growth accelerated modestly in the second quarter, buoyed by resilient consumer spending. Private inventories and nonresidential fixed investment also contributed positively, while imports increased. The Atlanta Fed's forecast for Q3 GDP is 2.5%, again driven by strong consumer spending. This estimate was revised down from 3.1% following the release of ISM's September Report on Business for manufacturing, which indicated some slowing in inventory spending.

Annualized Real GDP Growth

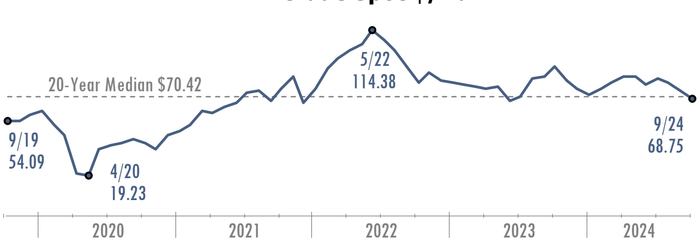


Relatively confident that inflation remains under control and labor conditions are reasonable, the Fed began its long-awaited easing program with a 50 basis point cut on September 18th. They also released an updated Summary of Economic Projections (the "dot plot") reflecting an accelerated pace of rate cuts compared to their June projections. The odd point was the "long term" expectation for the Fed Funds rate, which moved up from 2.8% to 2.9% despite the steeper descent angle for the next 2-3 years. While they expect to arrive early, where we're heading has not fundamentally changed; if anything, it reflects concern that, for the long term, inflation remains a threat.

Core Price Inflation (PCE Index)



WTI Crude Spot $/Bbl

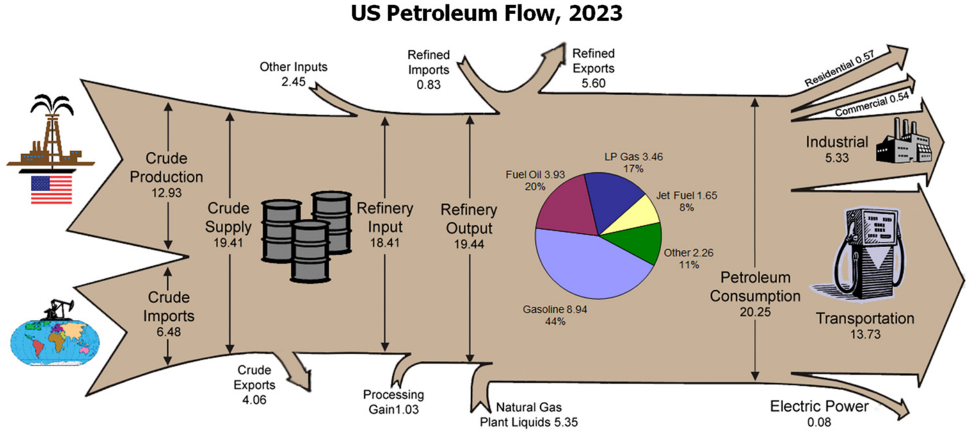


If short-term cyclical conditions are so benign, why be concerned about long-term inflation? In our view, four macro forces have driven inflation trends over the past century: geopolitics, demographics, government financing, and technological advancement. While the latter will continue to put downward pressure on prices, demographics and government financing have flipped from deflationary to inflationary, as we've discussed in several recent issues.

As for geopolitics, we believe war is inflationary, especially when served hot. Historically, short-term war inflation has been driven by commodity supply shocks, usually related to oil. Although filtered out of the "core" PCE and CPI measures of inflation, oil prices have a significant delayed impact, as petroleum affects manufactured goods directly and through the supply chain. It's remarkable that prices were not even more volatile in the first week of October following Iran's missile attack on Israel; one would have predicted a huge spike on that news two decades ago. One reason is that the US now sources 2/3 of its crude internally, a relationship that has flipped since 2020. If you combine crude oil and refined products, the US is now a net exporter of oil. Further, conflict operations to date have focused on missiles and drones, which are fuel-efficient compared to fighter jets and tanks.

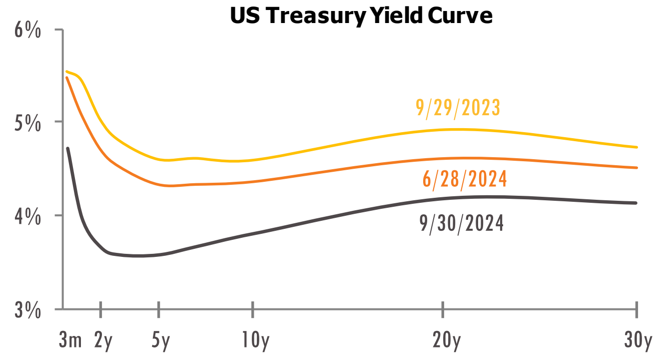
Throw-away weapons may be efficient, but they are not cheap. Long-term war inflation is vectored into the economy not just through commodity prices, but through deficit spending and rising government debt levels. Combined with high social spending and low taxes, that sets the stage for slow growth and inflation.

US Petroleum Flow, 2023



Million Barrels per Day Source: US Energy Information Administration

The US Bond Market



US Treasury yields and credit spreads declined gradually during the first two weeks of the quarter as financial markets began to price in a near-certain September Fed rate cut. The July 31st Federal Open Market Committee ("FOMC") meeting made clear that a 50 basis point cut was on the table. Market volatility soared for a few days as market participants digested the news, agitated that a suddenly flat-footed Fed may be behind the ball in propping up a faltering economy. US Treasury rates sped their decline while steepening enough that the 2-year through 20-year region finally looks normal. Meanwhile, credit spreads widened sharply. The spreads on below-investment-grade paper moved enough to overcome the decline in US Treasury yields.

By mid-August, Fed funds futures had swung back to favoring a 25-basis-point cut over a 50-basis-point cut at odds of 3:1. Risk appetites returned in coincidence. Yet, when the 50 basis point cut did come, it was calmly accepted by the market – even welcomed. Credit spreads ended the third quarter once again near historical lows as the market readily absorbed a new wave of corporate bond issuance. The landing gears are in position.

US Bond Index Returns	
Bloomberg Idx	**3Q24**
Aggregate	5.20%
Short Gov't	2.13%
Interm. Gov't	3.95%
Long Gov't	7.81%
TIPS	4.12%
Municipal	2.71%
Interm. Credit	4.58%
Long Credit	8.10%
High Yield	5.28%
(CS) Lev. Loan	2.08%
MBS	5.53%

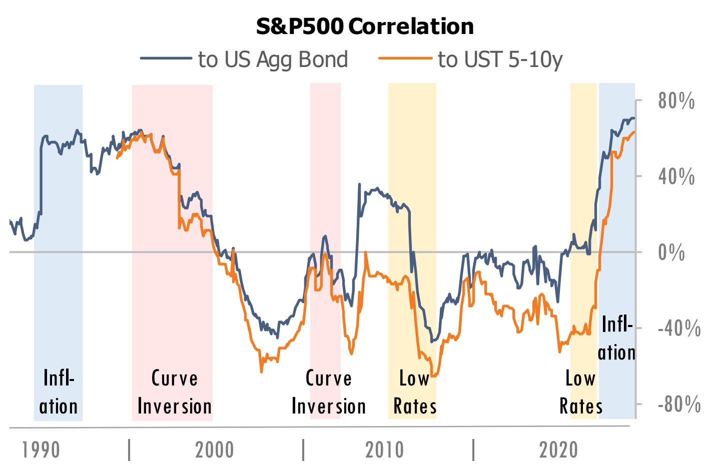
Long duration credit led US fixed income sectors as rates declined and lower credit quality outperformed modestly. However, the US Aggregate bond index was not too far behind and all US bond sectors posted healthy returns for the quarter. Securitized debt performed relatively well, despite delinquency rates inching higher.

Large outflows from fixed income mutual funds in 2022, followed by tepid inflows in 2023, were noted in our 3Q 2023 Market Recap. Outflows resumed in the following quarter but reversed at the start of 2024. As rates increased in the first and second quarters, this might have enticed investors to continue piling into fixed income funds. However, interest in the asset class waned even as yields became more attractive. More surprisingly, fixed income mutual funds and ETFs, together, picked up approximately $55 billion of inflows in the last several weeks of this quarter. In contrast, equity funds redeemed $11 billion net to investors over the same period.

It has been a long time since bond investors have enjoyed both a positively-sloped yield curve and attractive yields. After the 2008 Global Financial Crisis, the 10-year US Treasury yield remained below 3.5% for most of the following 14 years. For the past 2 years, the market has been in a new rate regime.

Obviously, higher yields correlate with higher pursuant fixed income returns. But if the yield curve continues to revert back to historically normal (i.e., positively-sloped yields at a healthy distance from the zero line), investors may gain much more. In such a regime, bonds can begin to compete with equities on return, typically with less volatility, and bonds more reliably serve as ballast when stock shares suffer.

A strong positive correlation between stocks and bonds has plagued investors for the past 3 years and soured many to balanced funds and even target-date funds. While a normal yield curve and higher yields should help, inflation is a related and significant factor driving this correlation. If inflation remains subdued, the benefits of equity and fixed income diversification should return. As the interest rate landscape evolves, bonds are well-positioned to play a more prominent role in achieving investment objectives, balancing the pursuit of returns with the management of risk. High-yielding money market funds and runaway equity returns have presented blustery headwinds for the good ol' US Aggregate Bond portfolio. Yet, if inflation remains under control, expect this old mainstay to recoup some of its deserved popularity.



The US Stock Market

Despite an early August meltdown, the US stock market turned in a strong quarter. The rout, which began in Asia, snowballed into the US in response to reported hiring slowdowns and the highest unemployment rate in almost three years (which is still low by historical standards). Amid fears that the Fed may have overshot a soft landing, some saw the sell-off as a predictable pullback from tech, especially AI, which has been on a tear since 2023. After a long-awaited rate cut in September, the Dow Jones Industrial Average and the S&P 500 ended Q3 with record closing highs – their 33rd and 43rd this year, respectively. The Nasdaq Composite posted its fourth consecutive quarterly gain.

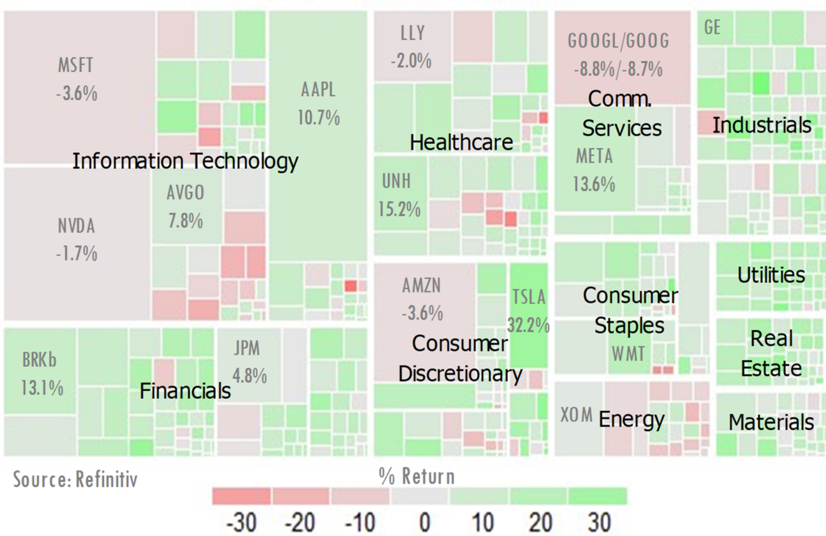
US Stock Indices - Total Returns			
Largecaps	**3Q24**	**Midcaps**	**3Q24**
S&P 500	5.89%	S&P Midcap 400	6.94%
Russell 1000	6.08%	Russell Midcap	9.21%
Growth	3.19%	Growth	6.54%
Value	9.43%	Value	10.08%
Broad Markets		**Smallcaps**	
S&P 1500	6.04%	S&P Smallcap 600	10.13%
Russell 3000	6.23%	Russell 2000	9.27%
Growth	3.42%	Growth	8.41%
Value	9.47%	Value	10.15%

S&P 500 Sector Components - Total Returns			
Sector	**3Q24**	**Sector**	**3Q24**
Utilities	19.37%	Consumer Discr	7.80%
Real Estate	17.17%	Health Care	6.07%
Industrials	11.55%	Comm Services	1.68%
Financials	10.66%	Info Tech	1.61%
Materials	9.70%	Energy	-2.32%
Consumer Stpls	8.96%		

The lead growth stocks had been enjoying for the last three quarters came to a halt with the Russell 3000 Value Index outperforming its growth counterpart by 6% for the quarter. However, most of this lead was built up in July. August saw value's outperformance narrow, and it reversed completely in September. Growth stocks benefit more from a falling rate environment since the present value of future earnings (a.k.a. the "growth" they are seeking) increases.

Small caps outpaced their large- and mid-cap peers. After a stellar July, they again bested larger firms in September, recording their longest streak of daily gains since March of 2021. Encouraged by the September rate cut, expectations of a healthy, Fed-supported business cycle created a positive environment for stocks, in general, and small-caps in particular.

3Q 2024 Returns in S&P 500 Companies

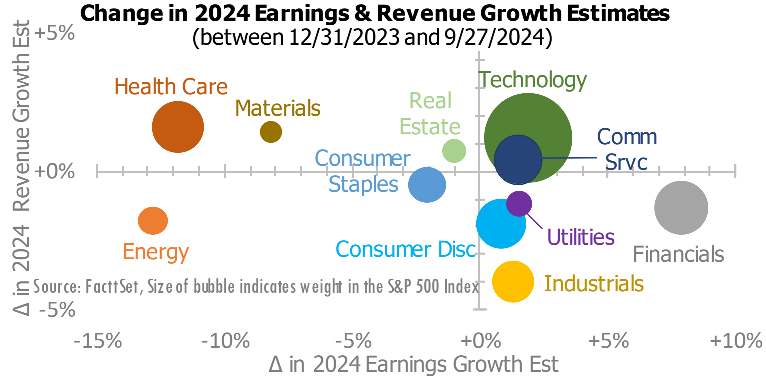


Performance dispersion across market sectors continued, up from over 10% in Q2 to over 20% in Q3. Returns in the Magnificent 7 diverged. Double-digit gains in Apple, Meta, and Tesla and strong performance in previously-lagging sectors like financials and industrials was enough to overcome the drag from the four remaining giants, which pulled their sectors to the bottom of the table. After benefitting from strong AI stories in previous quarters, NVIDIA, Microsoft, Amazon and Alphabet had not fully recovered from the August meltdown by the close of the quarter.

Utilities continued their climb, becoming the top-performing sector in large caps. We've noted that firms in the sector have been advancing on power requirements of the data centers critical to AI. However, the expectation and then realization of a September rate cut enhanced the already positive environment. Real estate, another rate-sensitive sector, was also a strong performer throughout Q3. The energy sector was the worst performer on falling oil prices driven by expectations of production increases in December and continued demand uncertainty, particularly out of China.

With the S&P 500 Index returning 26% in 2023 and 22% YTD, speculation on how much longer (and further) the bull market can continue has crept into market discourse. While the specter of the dot-com bubble looms, many point to a marked difference today. Companies driving the run are more profitable, and estimates of 2024 earnings and/or revenue growth have increased over the course of the year for most sectors [FactSet]. But with investor response to economic data only getting more dramatic, it remains to be seen whether we're one jobs report away from a true correction.

Change in 2024 Earnings & Revenue Growth Estimates
(between 12/31/2023 and 9/27/2024)



International Markets

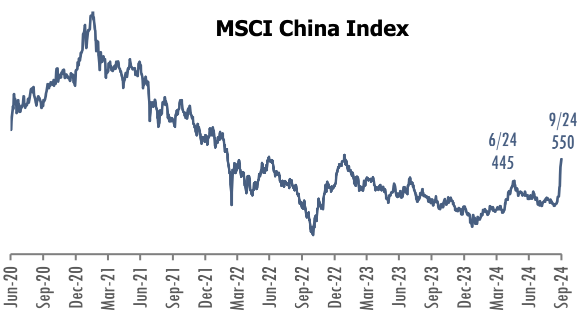
Global markets generated positive returns as inflation continued to drop and many global central banks began to lower interest rates and provide economic stimulus. According to the IMF, global growth is expected to remain stable with 3.2% GDP growth in 2024 and 3.3% in 2025. However, there has been some divergence between advanced economies and emerging and developing economies in terms of central bank moves.

Unhedged Foreign Markets Indices - Total Returns			
Stocks	**3Q24**	**Bonds**	**3Q24**
MSCI ACWI ex-US	8.06%	Global Aggregate	6.98%
EAFE (Developed)	7.26%	Pan-Euro	8.11%
Emerging Markets	8.72%	Asian-Pacific	9.48%
Europe	6.58%	Eurodollar	3.85%
Japan	5.72%	Other Currencies	3.06%
China	23.49%		
Latin America	3.75%		

Asia

In less than a week, the MSCI China Index advanced 21.6%, and closed 23.5% higher for the quarter. This after the People's Bank of China announced a slate of economic stimuli: cutting its benchmark interest rate, lowering required cash reserves for banks, cutting the interest rate on existing mortgages, and lowering downpayments for second homes. The central bank also indicated that further easing is in the pipeline, with another reduction in bank reserve requirements expected. To lift the country's ailing stock market, it announced 500 billion yuan in loans to funds, brokers, and insurers to buy Chinese stocks, with another 300 billion yuan to finance share buybacks by listed companies.

These measures positively impacted both China's and global equity markets, boosting shares of European luxury goods makers, lifting commodity prices, and fueling gains in US-listed stocks of Chinese companies such as Alibaba. Yields on Chinese government bonds climbed as investors rushed to buy stocks instead. The yuan rallied against the dollar, falling to 7.01 per dollar and putting the currency on pace for its strongest settle since May 2023. Still, the MSCI China Index is down 41.3% since its peak in February 2021, highlighting how the summer's economic dataweakened investor confidence.



China reported Q2 GDP growth of 4.7%, increasing doubt that Beijing's targeted 5% growth for 2024 can be achieved. The economy slowed further in August. Retail sales rose just 2.1%, slowing from a 2.7% YoY increase in July. Industrial production rose 4.5%, down from 5.1% in July. Manufacturing activity declined for a fourth straight month as well, suggesting contraction. Home prices fell 5.7%, the steepest decline in 9 years. The only bright spot was a record-setting surge in exports, which rose 8.7%. Sales of electric vehicles, batteries, and household appliances are now fueling China's economic growth.

While the cause of China's problems remains a property meltdown that is crimping consumer spending, the most urgent challenge is deflation which makes debts harder to pay and delays consumer spending in anticipation of better future prices. Consumer prices rose 0.6%. But when food and energy were excluded, the rise was just 0.3%, the lowest core inflation in more than three years. Producer prices have been declining for almost two years. While the broad range of economic support was well received by the markets, it may not be enough to turn around China's low-growth environment marked by falling prices and its serious real estate crisis. Instead, Beijing may need to get a firmer grip on the real estate downturn and take robust steps to boost consumption to spark a durable revival in the economy.

The Bank of Japan ended its negative interest rate regime in March. But in a move that surprised markets, it raised its short-term policy rate to 0.25% at the end of July noting steady progress towards consistently achieving 2% inflation. Global markets reacted negatively, having become sensitive to any signs of a change in monetary policy outlook and growth momentum. They dropped along with the Nikkei, which lost over 12%, its largest single-day point drop.

Japanese markets were also hard-hit by the unwinding of leveraged positions and carry trades causing losses and volatility to spread throughout global markets. The carry trade involves borrowing in a low-interest-rate currency to make investments in a higher-rate currency. Japan's ultra-low interest rates have made the yen the favored funding currency in recent years, but the BOJ's surprise rate hike meant it was no longer a cheap source of funding. Investors faced margin calls as the yen appreciated, forcing them to sell assets to buy yen to cover their positions, pushing the currency even higher.

Despite the significant volatility in August, Japan's moderate economic recovery continued in Q3. The BoJ's index of large manufacturers' sentiment closed the quarter at 13, holding steady at a 2-year high for the second straight quarter and in-line with market forecasts. With business sentiment stable, expectations remain for further interest rate hikes by the central bank. However, Japanese companies remain cautious about the outlook with service-sector firms projecting that economic conditions will deteriorate slightly over the final quarter.

Americas

Canadian equities made sizable gains, with the S&P/TSX Composite returning 5.7%, on strength in financials and technology. The Bank of Canada's recent rate cuts alleviated recession fears, boosting financial stocks and improving the outlook for REITs as borrowing costs decreased. However, the energy and materials sectors struggled under falling commodity prices. Aggressive monetary policy weakened the Canadian dollar, affecting foreign investment interest.

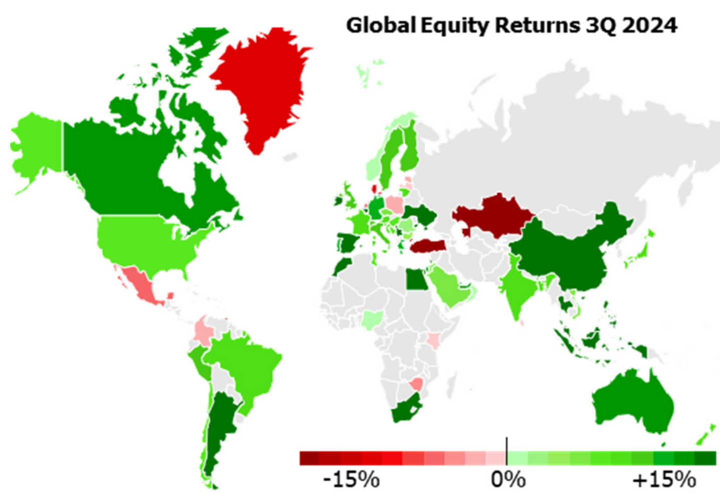
The investment landscape in Latin America was mixed, with Brazil's agricultural strengths countered by currency risks and Mexico's growth potential tempered by political and inflationary pressures. Argentina's investment market showed signs of stabilization and ongoing risks. After years of fiscal deficits, the Milei government initiated a stabilization program in December 2023. By mid-2024, the public sector recorded a fiscal surplus for six consecutive months, marking a significant turnaround. Inflation decreased sharply, dropping to just over 4% per month by August, down from 21% in January.

In Brazil, the stock market exceeded expectations, driven by strong agricultural exports. Despite this growth, the Brazilian real depreciated 13% year-to-date against the US dollar, leading to heightened inflationary pressures. The central bank's decision to raise rates by 25 basis points in September indicates ongoing concerns regarding inflation and fiscal stability. The underestimation of expenses in the 2025 budget raised red flags for investors. For pension plans, the real's depreciation poses risks that could erode investment returns and heighten the overall risk profile of Brazilian equities.

Political uncertainties over Mexico's June 2024 elections spurred market volatility. The peso weakened after the central bank's surprise rate cut to 10.50%. Currency depreciation may negatively affect investment values for pension funds, particularly if inflation remains a concern. Nonetheless, the peso's carry advantage against the US dollar offers some degree of stability. Ongoing judicial reforms and the evolving political landscape further complicate the investment outlook, raising concerns about the sustainability of Mexico's investment-grade status.

Europe

The Eurozone economy grew in Q2, despite unexpected drag from Germany, where manufacturing remained an anchor. GDP grew by 0.2% even as Germany's economy contracted about -0.1%. It was the second consecutive quarter of expansion after more than a year of lackluster growth due to the energy price shock. Expectations are that the recovery in the Eurozone will be faster in some southern economies versus core economies like Germany and France.



Inflation fell to 1.8% in September, coming in below the ECB's 2% target for the first time in more than 3 years as declining energy prices provided relief to consumers. Falling inflation along with a slow growth outlook has fueled speculation that the ECB will cut rates faster, perhaps as early as its next meeting in mid-October after cutting rates 25 basis points to 3.5% in September. The bank is in a tough spot, it must make sure that it has inflation under control which argues for waiting longer to lower rates versus concerns over anemic growth which argues for faster cuts. Economists expect inflation to tick up slightly before the end of 2024 as services inflation remains sticky. Bank President Christine Lagarde has said that the ECB is not committing to a future rate cut schedule, but will take a prudent approach based on economic data.

Despite economic struggles, Germany's Dax 40 Index finished up 6% for the quarter. With low economic growth, rising business bankruptcies, and industrial production 10% below pre-pandemic levels, expectations would typically be for a faltering equity market. However, Germany's equity market has risen this year due to a handful of technology companies. While German automakers have seen their stock prices drop 30% - 70%, technology-focused companies such as SAP and cloud computing firm Northern Data have benefited from the AI boom, rising 44% and 234% for the year, respectively.

European government bonds rallied after inflation in the eurozone fell. Bonds in Western Europe gained, pushing yields lower. As the quarter closed, Germany's 10-year yield fell to 2.03%, putting it near its lowest level since January. Equivalent yields on French and Italian debt dropped more than 10bps to close the quarter at 2.9% and 3.5%, respectively.

Focus On: Recordkeeper Monitoring

In 1965, NASA was racing to put a man on the moon. The space agency was full-steam-ahead on Project Apollo; but behind the scenes, its relationship with contractor North American Aviation (NAA) was stumbling. NAA was responsible for constructing the command and service modules for the Apollo spacecraft. And while the initial partnership had been smooth, by the mid-60s, cracks started to appear, figuratively and literally. Component failures, faulty welding, miscommunications, and production delays began to threaten NASA's ambitious timeline.

Rather than terminate the relationship, NASA took a different approach. NASA implemented daily briefings and mandated more detailed reporting and immediate communication of any emerging issues. By increasing the frequency of these check-ins and improving the clarity of expectations, NASA created an environment of real-time accountability. This structure allowed them to catch problems early and resolve them before they could derail the mission.

Additionally, NASA assigned more of its engineers to work directly with NAA's teams, creating a closer alignment between the two organizations. This level of hands-on collaboration, combined with contractual adjustments, fundamentally shifted how NAA approached the project. Renegotiating the contract for greater oversight, transparency, and communication was key to salvaging the relationship and ensuring the success of the Apollo missions.

Retirement plan sponsors may lack the motivation of one-upping Sputnik, but their mission is no less important and no less susceptible to vendor missteps. Properly managing vendor relationships starts with a prudent vendor selection process, which many plan sponsors are keen to follow. However, it is wishful thinking to believe a set-and-forget approach to vendor management will be successful, no matter how much the vendors assure it will be. Plan sponsors often devote significant time and resources to a formal request-for-proposal ("RFP") process, which can include analyzing thousands of pages of response material, conducting countless calls, and traveling for site visits. Yet, once in place, vendor monitoring can be less robust and less involved. The last thing anyone wants to do after conducting a vendor RFP is repeat the whole process anytime soon. However, as NASA showed, the point of monitoring a vendor isn't just to know when to replace them.

SLAs

Managing retirement plan vendors effectively requires more than setting up Service Level Agreements (SLAs) and passively monitoring performance, but it's a sensible place to begin. SLAs outline precise performance metrics, problem-resolution timelines, reporting standards, and establish a formal framework that vendors must adhere to. These agreements are crucial for maintaining service quality, managing expectations, and ensuring regulatory compliance.

A 401(k) recordkeeper serves as a prime example here as they are the most prominent and data-centric vendor for most plan sponsors; though, SLAs can be applied to any vendor. An effectively crafted recordkeeper SLA covers critical aspects such as data accuracy, transaction processing speeds, system availability, and response times for participant inquiries. For example, you might require that the vendor maintain a 99% accuracy rate in transaction processing and respond to participant queries within 24 hours. It should also detail remedial actions and potential penalties for missed targets to dissuade lax vendor service and compensate for lapses.

The challenge lies in crafting SLAs that are both strict and reasonable. They must be feasible yet enforce high standards. Weak SLAs often become either checkbox formalities or, worse, an assumed cost of doing business for vendors. SLAs are a starting point, not a solution. Plan sponsors have a duty to follow-up with prudent oversight and advocacy for the best interests of their participants.

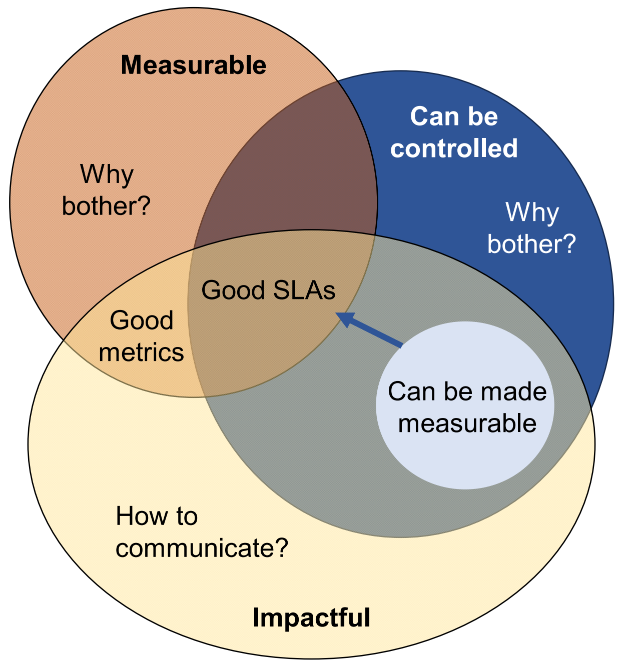
Common Recordkeeping SLA Standards

Overall fees at risk	
Max (incident, quarter, year)	1% / 3.75% / 15%
Transactions (20%) :	
Accuracy	99.5%
Call Center (20%) :	
Response Time	80% calls <=20 sec
Call Abandonments	<= 3%
Case Resolution	95% < 5 days 98% < 10 days 99% < 15 days
Participant Satisfaction	85-90%
First Call Resolution	90%
Callback Timeliness	Same day
Service Center Availability	99.5%
Service Center Outage Duration	Critical issues resolved within a 2-hour window
Interactive Voice Response System Availability	99%
Compliance Timeliness (45%) :	
1099Rs	Before Jan. 31 of, excl. corrected 1099Rs
Participant Correspondence	Within regulation-prescribed timeline
Posting Client Data	100% on time. Error correction < 1 day
Financial Transaction Timeliness	99% same day
Payment Timeliness	99% < 2 days
Systems (5%) :	
Website Down Time	98%, excl. scheduled maintenance
Website Responsiveness	95% of ppt-requested web pages < 6 sec

Measuring and Monitoring

Using SLAs, plan sponsors can define precise metrics such as transaction accuracy, response times for participant inquiries, system uptime, and compliance with regulatory standards. These quantifiable metrics are essential for continuously assessing and improving vendor performance. As the saying goes, "What gets measured gets managed." Except, that often misattributed quote originates from a 1956 paper by V.F. Ridgeway titled "Dysfunctional Consequences of Performance Measurements." It would be more apt to complete the quote with "…even when it's pointless to measure and manage it, and even if it harms the purpose of the organisation to do so" [Medium]. One solution is to measure what matters.

John Doerr's concept of Objectives and Key Results ("OKRs") in *Measure What Matters* tackles a similar challenge inherent in running a business. Relevant objective criteria are needed by which performance can be continuously assessed and improved. According to Doerr, "OKRs are a cooperative social contract to establish priorities and define how progress will be measured." In this way, SLAs can be properly appreciated as more than just a system to punish vendors for their mistakes and specify punitive damages. Vendors will do what you pay them to do. Early on, a structured evaluation process helps vendors align their operations with their clients' needs; later on, it helps vendors deliver on client expectations.



Plan sponsors need their SLAs and monitoring efforts to reflect what matters, which boils down to cost and satisfaction. Cost is easy to measure, satisfaction less so. Yet, without that objective in clear sight, a plan sponsor may unintentionally push their vendor to do things cheaper (good), faster (good), and worse (not good). Whatever is impactful, measurable, and can be controlled by the vendor can make a good SLA. Though, being measurable is the least important of these qualities. If it can't be measured but it is impactful, then the plan sponsor should make it measurable (e.g., survey participants about their experience and satisfaction) or find another way to communicate the criteria to the vendor (e.g., ask for qualitative updates on the topic). Items that are beyond the vendor's control won't serve as suitable SLAs, but they can still serve as good metrics, especially if they can be influenced by the plan sponsor's actions.

Regular audits and performance reviews are essential tools in this monitoring process. They allow plan sponsors to verify ongoing compliance with SLAs and identify areas needing improvement. Audits can reveal systemic issues that might not be visible through routine interactions, and performance reviews foster an ongoing dialogue between vendors and plan sponsors. This feedback loop is crucial for refining service delivery strategies and making necessary adjustments to SLAs in response to emerging trends, technological advancements, or new regulatory requirements.

Best practices for monitoring include:

- **Clear & Measurable:** Use specific performance stats aligned with regulatory requirements and fiduciary duties.
- **Audits and Reviews:** Conduct periodic internal and third-party evaluations to verify compliance.
- **Consequences for Non-Compliance:** Implement specific penalties for missed metrics and enforce them.
- **Communication:** Foster open dialogue with vendors to correct deficiencies and keep SLAs relevant.
- **Documentation:** Keep detailed records of all monitoring to demonstrate compliance with fiduciary duties.
- **Staying Informed:** Continuously update SLAs and monitoring to reflect current laws and best practices.

Trends

Your vendors don't operate in static, isolated industries; they are subject to, or possibly driving, important industry trends: fee compression, consolidation, technological innovation, and regulatory changes. Monitoring and SLAs must adapt with these trends or risk becoming antiquated and incomplete. For example, mobile apps have become the primary 401(k) access point for many participants.

A mass movement away from revenue sharing and bundled proprietary investments dealt a severe blow to profit margins. The greater transparency in pricing structures has helped avoid overpaying in participant fees, but it has arguably pushed plan sponsors to focus too much on fees versus service features and quality. In some cases, recordkeepers have balanced lower headline fees with increases to ancillary costs, such as distribution fees, and a greater emphasis on cross-selling additional financial products. However, overall fee compression continues.

Recordkeeping has long been a concentrated market where the top 10 players held most of the plan assets. However, there was room downstream for mid-sized and niche players. Over the past 20 years, two-thirds of vendors have disappeared and the industry has become increasingly top-heavy. Nearly half of the 20 largest recordkeepers in 2014 have since been acquired (MassMutual, Wells Fargo, Prudential, etc.).

Trends and Implications for SLAs and Metrics

Fee Compression	Risk of declining quality due to loss of resources and/or staff as well as over-standardization of services
Consolidation	Reduces competition and adds risk of resource diversion to disruptive integration activities and cross-selling
Technology	Risk of excessive focus on flashy or trendy capabilities which may not be that impactful to participants or to quality of services
Regulation	Requires work and talent so communications are not needlessly detailed and legalistic in tone, serving regulator instead of end-user

Vendors are doing more than scaling up; they are investing in productive and efficient operations to keep pace. Some firms remain committed to high-touchpoint boutique service models as fewer competitors are equipped to provide that. However, vendors are also trying to find fat to trim – and one person's gristle is another's bacon. SLAs need to be crafted to cover new technologies, operational strategies like offshoring, the implications of industry consolidation, and the nuances of evolving fee structures. Robust, relevant SLAs and monitoring mitigate erosion in service standards.

Advocating

Advocating for participants is a core fiduciary responsibility under ERISA; plan sponsors must ensure that vendors deliver suitable and competitive services that align with participants' best interests. Crafting SLAs that encompass components crucial for participant satisfaction, such as clear communication, transparent fees, and prompt resolutions goes a long way to accomplishing this. For instance, SLAs should require that any changes in fee structures or investment options are communicated clearly and promptly. In this way, careful oversight helps protect participants' investments by getting them accurate and timely information, essential for making informed decisions about their retirement savings.

Plan sponsors can solicit feedback from participants to understand their experiences and identify service gaps. Pairing that feedback with vendor service metrics will produce a full and current view of the vendor relationship. While datapoints from service reports indicate performance levels, direct feedback from participants provides deeper insights into potential issues.

Effective advocacy means more than just monitoring operations; it involves engaging with both the service providers and the participants. By regularly soliciting participant feedback and holding vendors accountable for their performance, plan sponsors can ensure that service providers rectify mistakes and adhere to agreed standards. This proactive engagement not only enhances participant satisfaction but also ensures the smooth and efficient operation of the retirement plan, fostering a reliable environment for managing retirement assets.

Leveraging Monitoring in Your Next RFP

Most RFPs are tools to identify the largest and cheapest vendor, and rarely do a good job of identifying the best vendor. To assemble the right questions for a meaningful RFP, start with your SLAs (assuming they are good). If you're asking about other things, maybe your criteria aren't so good. Past experience with vendors is a treasure trove of valuable data. If your current vendor has struggled with response times or offshored service quality, make sure those issues are front and center in your next round of negotiations. Don't settle for generic promises—demand specifics on how future vendors will avoid these pitfalls. When negotiating new contracts, insist on specific guarantees tied to penalties for poor performance.

Diligent management and monitoring of SLAs with retirement plan vendors are fundamental for plan sponsors who wish to ensure that services are delivered efficiently and in alignment with participants' best interests. The experience gained should serve as a resource for future planning, especially during the RFP or contract negotiation phases. If recurring issues were noted, future RFPs can specify enhanced standards to address this.

Understanding the nuances of past vendor performance and participant feedback can guide plan sponsors in negotiating more effectively. They will be better equipped to discuss specific pain points and leverage these discussions to secure more favorable terms or comprehensive service commitments from the next vendor. This informed approach ensures that new contracts are strategic enhancements that address previously identified gaps and opportunities.

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