S&P Dow Jones Indices

A Division of S&P Global

CONTRIBUTORS

Smita Chirputkar

Director Global Research & Design

Massi De Santis, PhD

Vice President Dimensional Fund Advisors

Christine Lubieniecki

Senior Associate Dimensional Fund Advisors

Philip Murphy, CFA

Vice President North American Equity Indices

Making STRIDEs in Evaluating the Performance of Retirement Solutions

EXECUTIVE SUMMARY

The S&P Shift to Retirement Income and Decumulation (STRIDE) Index Series incorporates an innovative risk management framework focused on providing increasing levels of clarity and stability around sustainable annual consumption in retirement. This paper tests S&P STRIDE's approach to consumption risk management and asset allocation over the period 2003 to 2016 for a hypothetical cohort of 2010 retirees by comparing the S&P STRIDE Glide Path 2010 Index Total Return to the average 2010 target date fund (TDF). Our main findings are as follows.

- The risk management approach employed by S&P STRIDE would have helped reduce uncertainty about retirement income through a period of variable interest rates, inflation, and market returns. In particular, we show how the risk management component of the S&P STRIDE Index can provide clarity and stability around affordable future consumption prior to and into retirement. The approach aims to help retirement plan participants seamlessly transition from accumulation to retirement.
- The risk management strategy can be used to reduce the impact of market, inflation, interest rate, and sequencing risks on retirement consumption.
- In contrast, we find that an industry average of traditional 2010 TDFs exhibited high variability in terms of retirement consumption over the period. Estimates of affordable consumption from such a strategy were highly sensitive to market risk, interest rates, and inflation. As a result, these strategies demonstrated large fluctuations in the level of expected retirement consumption over the period.

INTRODUCTION

Retirement can mean different things to different people. For some, retirement means a complete stop from working. For others, it means ending a professional career in pursuit of something new. Regardless of the definition, retirement normally marks the point when the primary source of income ends and savers begin to rely on their accumulated balances to

The S&P STRIDE Indices use an asset allocation framework designed to balance the opportunity to grow assets with the need to reduce the uncertainty of how much inretirement income a saver's balance can afford.

maintain their standard of living. Therefore, in the context of retirement, a primary goal is often to be able to sustain an inflation-adjusted stream of income, or a level of consumption associated with a standard of living, throughout retirement and to have relevant and meaningful information about what that level of sustainable consumption stream is before and throughout retirement.

The S&P STRIDE Indices use an asset allocation framework designed to balance the opportunity to grow assets with the need to reduce the uncertainty of how much in-retirement income a saver's balance can afford. The indices use a glide path that transitions from growth-seeking assets to assets that can support a more stable level of inflation-adjusted, in-retirement income. The indices are designed to be a benchmark for market participants saving to fund consumption in retirement.

In this paper, we use the S&P STRIDE Indices to benchmark traditional TDFs, which are investment vehicles used predominantly by people saving for retirement. In particular, we focus on target date strategies that have moved from accumulation to retirement in the past 10-15 years, so we can evaluate their performance in terms of retirement income. To do that, we show how STRIDE data can be used to translate account balance performance into information about how much in-retirement income or consumption the account balance can be expected to afford over time. Our analysis illustrates how a retirement solution that manages uncertainty about how much in-retirement income a saver's balance can afford might provide more robust risk management and greater clarity on progress toward retirement goals.

The S&P STRIDE Index Series is published under agreements between S&P Dow Jones Indices and Dimensional Fund Advisors. In development of the S&P STRIDE Index Series, S&P Dow Jones Indices used ideas from life cycle finance and an innovative risk management approach to funding consumption in retirement. S&P Dow Jones Indices thanks Robert Merton for his pioneering work in these fields, as well as Dimensional Fund Advisors for their contributions in the development of the S&P STRIDE Index Series.

A PRIMER ON THE S&P STRIDE INDEX SERIES

The S&P STRIDE Index Series combines a target date glide path with a risk management framework designed to reduce uncertainty about future retirement consumption. It contains multi-asset-class indices composed of three broad asset classes: global equities, global fixed income, and a portfolio of inflation-protected securities intended to match to the investment and consumption horizon of cohorts retiring in five-year intervals, or vintages. Each vintage is designed to cover a full life cycle, including working years from ages 25 to 65 and in-retirement years from ages 65 to 90. The glide path allocation is illustrated in Exhibit 1.

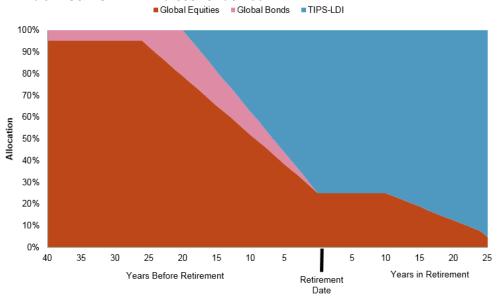


Exhibit 1: S&P STRIDE Indices' Glide Path

Source: S&P Dow Jones Indices LLC and Dimensional Fund Advisors. Chart is provided for illustrative purposes. TIPS-LDI: Treasury Inflation-Protected Securities, liability-driven investing.

We can divide the glide path into three phases to examine how the allocation shifts over time. The first phase goes from 40 to 20 years before retirement and focuses on diversified global stock and bond indices that are expected to grow over time. The second phase is a transition phase that goes from 20 years' pre-retirement to retirement. In this phase, the index weight is gradually shifted from growth assets to a risk management strategy designed to reduce uncertainty about the level of future retirement consumption the portfolio can afford. The final stage is the in-retirement or decumulation phase, where the main goal of the index is to mitigate uncertainty about the level of consumption that can theoretically be sustained from accumulated savings.

During the growth phase between 40 and 20 years before retirement, the S&P STRIDE glide path has a 95% allocation to equities. This is higher than the average allocation across TDFs weighted by assets. For example, as of December 2016, the average equity allocation ranged from 85% to 88% for TDFs dated 2040 to 2060.¹ At and throughout retirement, the equity exposure of the S&P STRIDE Indices is on the conservative end of the range of asset allocations across TDFs. While the S&P STRIDE Indices have a 25% equity allocation at retirement, the 2015 TDF average is 47% (ranging from 21% to 56% across funds) and the 2010 TDF average is 39% (ranging from 16% to 45%).²

The primary objective of the S&P STRIDE glide path near or in retirement is to manage uncertainty about the amount of retirement consumption that

We can divide the glide path into three phases to examine how the allocation shifts over time.

¹ Asset weighted average, using available target date funds from the Morningstar database as of December 2016.

² As of December 2016.

An allocation of 25% equities at retirement aims to constrain the potential losses in the event of poor stock market performance.

accumulated savings can afford. History has shown that during financial or other crises, both equity markets and the economy may suffer declines. An allocation of 25% to equities at retirement aims to constrain the potential losses in the event of poor stock market performance. This explains the more conservative equity exposure of the S&P STRIDE Indices at and throughout retirement and the high allocation to a risk management strategy designed to reduce uncertainty around the retirement consumption that the asset allocation can support. For the first 10 years after the target date, the target equity allocation remains at 25%. This remaining allocation to global stocks provides potential growth to possibly increase the consumption amount that can be afforded during the initial 25-year horizon. After 10 years in retirement, a portion of the consumption growth assets is "sold off" (removed from the Index portfolio) in an effort to provide additional retirement consumption. This is the rationale for a gradual decline in equity allocation 10 years after the target date.

S&P STRIDE'S RETIREMENT HORIZON AND RISK MANAGEMENT FRAMEWORK

S&P STRIDE's risk management strategy begins with defining both a retirement goal and its expected horizon. The goal is defined as annual inflation-protected income or consumption over a horizon of 25 years, starting at retirement. The 25-year horizon includes life expectancy at age 65 plus a buffer to account for uncertainty about life expectancy. Assuming participants retire at age 65, this covers the period between age 65 and age 90. The goal is indexed to a USD 1 annual inflation-adjusted consumption stream over the 25 years, as illustrated in Exhibit 2.

Exhibit 2: USD 1 Annual Inflation-Adjusted Consumption Stream

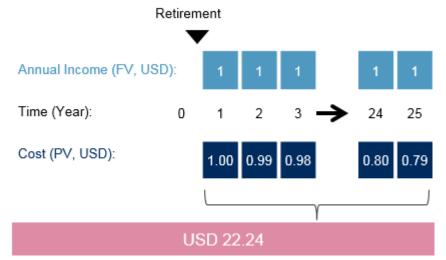


Source: S&P Dow Jones Indices LLC. Chart is provided for illustrative purposes.

The starting point for the consumption stream for each vintage is linked to the target date. For example, the 2025 index assumes that withdrawals will start in 2025 and end in 2049, the 2030 index assumes withdrawals will start in 2030 and end in 2054, and so on.

At any point in time, the consumption stream illustrated in Exhibit 2 can be viewed as a liability. This liability has a cost, which can be computed as the present value of the future expected cash flows. Because the liability is in inflation-adjusted terms, this cost can be estimated using real interest rates. For example, assuming a real interest rate of 1%, the cost of a 25-year USD 1 inflation-adjusted stream of income is USD 22.24, as illustrated in Exhibit 3.

Exhibit 3: The Cost of a Generalized Retirement Income Liability, "GRIL" Today's Cost of a 25-Year USD 1 Inflation-Adjusted Stream of Income



If interest rates go up, the cost of GRIL goes down, and vice versa.

Source: S&P Dow Jones Indices LLC and Dimensional Fund Advisors. Chart is provided for illustrative purposes. Assuming first year of income begins immediately. Present value calculation assumes a discount rate of 1%.

In the <u>S&P STRIDE Index Series Methodology</u>, this liability is referred to as the generalized retirement income liability (GRIL). S&P Dow Jones Indices computes a monthly present value, or cost, of GRIL for each retirement vintage using prevailing real interest rates. The liability decreases by USD 1 each year into retirement, so that after the first year, only 24 years of payments are expected, after the second year, only 23 payments are expected, and so on.

The cost of GRIL fluctuates with changes in inflation and interest rates. Much like the relationship between bond prices and interest rates, if interest rates go up, the cost of GRIL goes down, and vice versa. This implies that, for a given level of account balance, the amount that can be consumed is higher when interest rates are higher, and vice versa. Interest rates constitute a risk to the level of consumption that can be sustained from a level of savings. Inflation has a similar effect—the purchasing power of an account balance declines with inflation and increases with deflation.

The sensitivity of GRIL to real interest rates and inflation depends on the maturity of its cash flows. The longer the average maturity or, more technically, the duration of the cash flow, the higher the sensitivity.³ An investment that matches the sensitivity of GRIL to interest rates and inflation can reduce the uncertainty about how much consumption can be sustained with an investment. One can attempt to achieve this by computing the duration of the GRIL and constructing an inflation-protected

³ Duration is a measure of sensitivity of a cash flow stream (like a bond) to interest rates. It is a weighted average maturity across the cash flows, with weights given by the relative present value of each cash flow.

portfolio of government bonds with the same duration. This is an example of liability-driven investing (LDI). The S&P STRIDE Index Series constructs the LDI strategy for each target date by combining a set of Treasury Inflation-Protected Securities (TIPS) to match the duration of the appropriate GRIL.⁴

How does this investment strategy reduce uncertainty about future consumption? The sensitivity of the strategy to inflation and interest rate risks is the same as that of the GRIL. When interest rates go up, the value of the TIPS-LDI index allocation tends to decrease along with the value of GRIL. When interest rates go down, the converse is true, with the values of the TIPS-LDI index allocation and GRIL tending to increase. Similarly, the value of the TIPS-LDI index allocation tends to rise alongside GRIL when inflation is positive, and vice versa, thus protecting the future purchasing power represented by S&P STRIDE.

The sensitivity of the strategy to inflation and interest rate risks is the same as that of the GRIL.

USING THE S&P STRIDE TO EVALUATE THE PERFORMANCE OF TDFs

Given their design, the S&P STRIDE Indices can be used to analyze how an investment solution that balances the tradeoff between growth opportunities and income risk management has performed in various market, inflation, and interest rate environments. For the same reasons, and because providing income in retirement is one of the primary goals of participants in retirement accounts, the S&P STRIDE Indices can be used to evaluate the performance of traditional TDFs under the same scenarios.

As a proxy for traditional TDFs, we take the asset-weighted average returns of all Morningstar-categorized TDFs. Back-tested hypothetical returns for S&P STRIDE Indices are available from January 2003 to the present. The observed variability in market and interest rates over this period gives us a useful case study for the purpose of our analysis. We focus the analysis on the S&P STRIDE Glide Path 2010 Index. For this index, the 2003-2016 period covers the seven years leading up to retirement and the first seven years into retirement, a key transitional period from accumulation to early retirement.

The GRIL measure allows us to translate traditional performance (normally viewed in units of returns or account balance) into retirement income or consumption units, which is important because the performance that matters to retirees is in terms of affordable consumption in retirement. We will look at performance in consumption units after a review of performance in traditional, account balance terms.

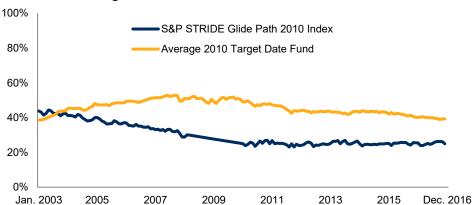
For more details about STRIDE design and methodology, see Gerard O'Reilly, Massi De Santis, Philip Brzenk, Aye Soe, Peter Tsui, "Introducing the S&P STRIDE Index Series," S&P Dow Jones Indices, 2016, and the S&P STRIDE Index Methodology, S&P Dow Jones Indices, 2016.

2010 Target Date Asset Allocation Comparison and Implications for Risk Management

The S&P STRIDE allocation to equities follows the glide path referenced in Exhibit 1. As seen in Exhibit 4, the 2010 equity allocation was 43% in January 2003 and reached 25% by December 2009. It then stayed close to that level throughout the remaining sample period. In January 2003, the equity allocation across the 2010 TDFs ranged from 17% to 63%. The asset-weighted average allocation was approximately 40%, similar to the S&P STRIDE Glide Path 2010 Index.⁵ Over the period studied, the sample of funds included in the asset-weighted average changed as additional fund families released 2010 TDFs. Not only did some of the new fund families have equity allocations above 50%, but some existing fund families increased their equity allocation during the period.⁶ This explains why the asset-weighted average for TDFs was 50% by December 2009, with allocations across fund families ranging from 15% to 64%.

The asset-weighted average allocation was approximately 40%, similar to the S&P STRIDE Glide Path 2010 Index.

Exhibit 4: Allocation to Equities – Back-tested S&P STRIDE Glide Path 2010 Index Versus Average 2010 TDF



Source: S&P STRIDE Glide Path 2010 Index data from S&P Dow Jones Indices LLC. Average 2010 TDF is the asset-weighted average across the TDF families included in the Morningstar universe. As of December 2016, the data included 57 TDF families. Past performance does not guarantee future results. Chart is provided for illustrative purposes. Data from January 2003 to December 2016 is backtested. Back-tested performance is not actual performance but is hypothetical Indices are not available for direct investment. Index performance does not reflect the expenses associated with the management of an actual portfolio. Please see the Performance Disclosures at the end of this document for more information regarding the inherent limitations associated with back-tested performance. For more information, see "S&P STRIDE Index Series Description and Disclosures" in the Appendix.

The S&P STRIDE Indices lower weight to equities reflects their focus on attempting to reduce uncertainty about retirement consumption. As discussed earlier, three main investment risks drive uncertainty around future consumption: market risk, interest rates, and inflation. For savers

⁵ Values for the TDF industry computed using data from Morningstar as of December 2016. If for a given month the equity allocation of a fund is not available, we use the closest previous and subsequent months with observed allocation for that fund and interpolate between the two

⁶ Some TDF families did increase allocation prior to retirement. For an analysis, see "Bait and Switch: Glide Path Instability," Ibbotson Morningstar, Sept. 12, 2011.

For savers that are close to retirement, the sequence in which they experience returns may also affect their ability to sustain a consistent level of consumption.

that are close to or are already drawing down from their portfolios, the sequence in which they experience returns may also affect their ability to sustain a consistent level of consumption. For example, a sequence of poor market performance early in retirement can increase the likelihood of running out of money early. Market risk is not the only cause of sequencing risk. Interest rates and inflation risks also matter. For example, an unexpected rise in inflation early in retirement increases the likelihood of running out of money early. A traditional allocation to stocks and bonds introduces sequencing risk because of market, interest rate, and inflation risks.

The glide path of the S&P STRIDE Indices is designed to reduce sequencing risk. The dedicated allocation to assets that hedge against the effects of inflation and interest rates on future consumption means that sequencing risk only enters through the exposure to growth assets.

Account Balance Performance

We start by measuring performance in terms of current theoretical account balance, or wealth units. This is a useful starting point, as it is how most traditional performance analysis is conducted, and it provides information about different retirement strategies in various market environments.

Exhibit 5 illustrates the cumulative growth of the S&P STRIDE Glide Path 2010 Index and the average 2010 TDF from 2003 to 2016 (net of fees). To help interpret results, Exhibit 5 also shows the performance of the <u>S&P 500®</u> over the same period, and we plot the 10-year interest rate as published by the U.S. Federal Reserve Board on a secondary axis.

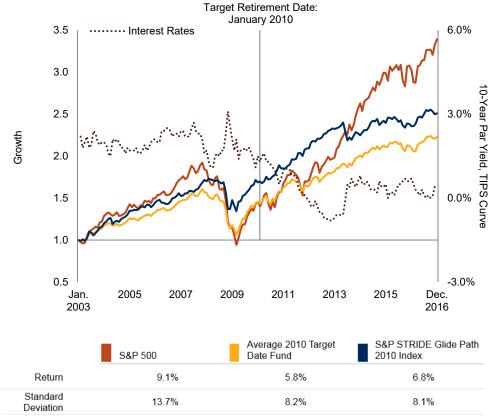


Exhibit 5: Growth of Wealth and Performance Statistics

Differences in asset allocation are the main drivers of performance in account balance units.

Source: S&P STRIDE Glide Path 2010 Index data from S&P Dow Jones Indices LLC. The average 2010 TDF is the asset-weighted average across the TDF families included in the Morningstar universe. As of December 2016, the data included 57 TDF families. Past performance does not guarantee future results. Chart and table are provided for illustrative purposes and reflect back-tested index data and hypothetical historical performance. Please see the Performance Disclosure at the end of the document for more information regarding the inherent limitations associated with back-tested performance. Indices are not available for direct investment. Index performance does not reflect the expenses associated with the management of an actual portfolio. For more information, see "S&P STRIDE Index Series Description and Disclosures" in the Appendix.

Differences in asset allocation are the main drivers of performance in units. First, a greater allocation to equities at the onset of the financial crisis caused a larger drop for the average 2010 TDF than for the S&P STRIDE Glide Path 2010 Index. The emphasis on the TIPS-LDI index allocation also benefited asset growth, given the decline in interest rates between 2009 and the first quarter of 2013. Exhibit 5 shows that the monthly volatility of the average 2010 TDF and the STRIDE Glide Path 2010 Index are similar over the period considered (8.2% versus 8.1%).

The STRIDE TIPS-LDI index allocation matches the duration of the 25-year theoretical cash flow starting at retirement. The duration of this "cash flow" varies with interest rates and with time to and through retirement. At the point of retirement (2010 in this case), it is expected to be around 10-12 years. This is a longer duration than the typical duration across TDFs, which averages about five years (see section titled "The LDI Risk Management Strategy in Practice" for a discussion).

Exhibit 6 focuses in on the performance of the three strategies during the peak-to-trough period for the S&P 500, October 2007 to February 2009, and the following recovery. Over a 16-month period ending February 2009, the S&P 500 fell 51% from its peak, and it took 36 months to return to the previous high.

Exhibit 6: Maximum Drawdown and Recovery of Account Balance



1. Represents maximum loss/drawdown for peak to trough of each index from January 2003-December 2016.

Source: S&P 500 and S&P STRIDE Glide Path 2010 Index data from S&P Dow Jones Indices LLC. The average 2010 TDF is the asset-weighted average across the TDF families included in the Morningstar universe. As of December 2016, the data included 57 TDF families. Data from Morningstar Past performance is no guarantee of future results. Chart is provided for illustrative purposes and reflects back-tested hypothetical historical performance. Please see the Performance Disclosure at the end of the document for more information regarding the inherent limitations associated with back-tested performance. Indices are not available for direct investment. Index performance does not reflect the expenses associated with the management of an actual portfolio. For more information, see "S&P STRIDE Index Series Description and Disclosures" in the Appendix.

It is important to note that over any given period, differences in allocations for one strategy could cause it to perform better than the others; for example, in rising equity markets, the S&P 500 would likely outperform the Average TDF and S&P STRIDE Glide Path 2010 Index. However, market downturns, changes in interest rates, and inflation levels cannot be predicted in advance. Exhibit 6 serves as a good reminder that retirement outcomes can be meaningfully affected by these types of events. The difference in performance between the average 2010 TDF and the S&P STRIDE Glide Path 2010 Index seen in Exhibit 6 may stem from a fundamental difference in risk management between the two strategies. To analyze the implications of these differences in terms of the theoretical amount of income retirees can provide for themselves in retirement, we need to evaluate performance in income terms.

Translating Account Balance Performance Into Income Units Using GRIL

For market participants planning for retirement consumption, the key performance questions can include: How much consumption can I expect my accumulated savings to sustain? What is the uncertainty or variability of that expectation? Evaluating performance in consumption units is important because there are additional factors beyond an account balance that affect retirement income. For example, if an account balance increases at a rate less than inflation, expected income is reduced. Similarly, a lower interest rate means one can sustain less income from the same account balance. Conversely, a lower account balance when interest

The difference in performance between the Average 2010 TDF and the S&P STRIDE Glide Path 2010 Index stems from a fundamental difference in risk management between the two strategies.

rates increase may mean the level of income that can be sustained from savings is unchanged or may be even higher.

We can convert wealth units into consumption units by using the cost, or present value, of GRIL, which is an estimate of the cost of USD 1 of inflation-adjusted income for 25 years commencing at the respective target date. Remember that because the GRIL uses real interest rates (i.e., market data on inflation-protected bonds with various maturities), it gives us information about what it would cost to build a bond portfolio that pays USD 1 each year in retirement, adjusted for inflation, assuming a retirement horizon of 25 years. By dividing an account balance by the appropriate cost of GRIL, participants can estimate the amount of income that savings could sustain over time.

By dividing an account balance by the appropriate cost of GRIL, participants can estimate the amount of income that savings could sustain over time. Let's look at an example that describes the concept. In December 2009, Jill decides to retire next month at age 65. She has accumulated USD 1,000,000 in savings and wants to determine the inflation-adjusted consumption that her account balance can sustain over the next 25 years. She can estimate this amount by dividing USD 1,000,000 by USD 20.01, which is the cost of 2010 GRIL at that time. Jill finds that USD 1,000,000 provides an estimated consumption level of USD 49,975 per year for 25 years on an inflation-adjusted basis (Exhibit 7).

Exhibit 7: From Account Balance to Retirement Income

Above equation expressed in terms of an income stream commencing immediately

Source: S&P Dow Jones Indices LLC and Dimensional Fund Advisors. Chart is provided for illustrative purposes.

This framework can be used for planning purposes at any point in time leading up to and during retirement, providing meaningful information about retirement readiness and allowing market participants to monitor their progress toward achieving their goals.

The cost of retirement consumption is driven by changes in real rates and inflation. Exhibit 8 shows how the cost of S&P 2010 GRIL changes over time, along with 10-year real interest rate (on the secondary axis).

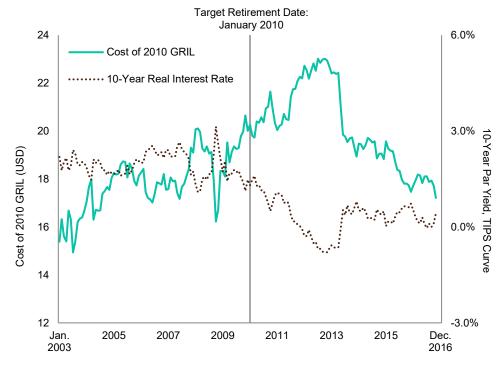


Exhibit 8: Cost of 2010 GRIL Value Over Time and 10-Year Real Rate

Source: S&P Dow Jones Indices LLC and U.S. Federal Reserve System. Data from January 2003 to December 2016. Chart is provided for illustrative purposes.

For Jill, this means that over time, the estimated retirement consumption level will vary, unless her account balance moves in tandem with the cost of retirement consumption. For example, the variability observed in Exhibit 8 shows that a constant account balance can be highly volatile in terms of estimated retirement consumption.

A constant account balance can be highly volatile in terms of estimated retirement consumption.

THE LDI RISK MANAGEMENT STRATEGY IN PRACTICE

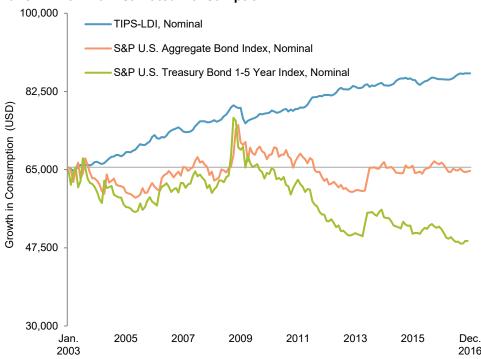
The uncertainty about the cost of consumption driven by interest rates and inflation can be hedged using the S&P STRIDE TIPS-LDI index allocation. The estimated consumption over time from this strategy can be calculated by simply dividing the performance of the LDI strategy in account balance units by the cost of GRIL every month (see Exhibit 9). Assuming an account balance of USD 1,000,000 at the beginning of the period (January 2003), initial affordable consumption starts at about USD 65,000. By December 2009, right before retirement, the amount of affordable consumption under the LDI strategy reaches about USD 78,000 in nominal terms (Exhibit 9). However, over these seven years, cumulative inflation was about 19%. This means that by December 2009, the amount of real affordable consumption for the LDI strategy was about USD 65,000 per year in January 2003 U.S. dollars, just like the initial consumption estimate

Stability in the inflationadjusted consumption estimates is a reflection of the risk management utilized by the S&P STRIDE Indices. (see Exhibit 9).⁷ In January 2010, we assume a withdrawal amount equal to the amount implied by GRIL each year—so USD 78,000 in the first year, which is equivalent to USD 65,000 in 2003 U.S. dollars.

Stability in the inflation-adjusted consumption estimates is a reflection of the risk management utilized by the S&P STRIDE Indices, effectively hedging for changes in interest rates and inflation. The light blue dashed line in Panel B illustrates the evolution of the estimated, inflation-adjusted consumption over time and its stability around the original USD 65,000 estimate in 2003 U.S. dollars (see Exhibit 9).

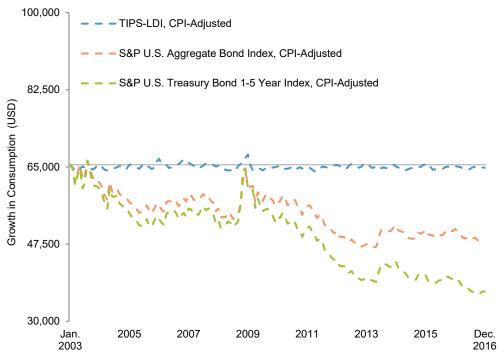
Exhibit 9: Evolution of Estimated Consumption, TIPS-LDI Versus Intermediate Bonds





Source: S&P Dow Jones Indices LLC and Dimensional Fund Advisors. Back-tested data from January 2003 to December 2016. Past performance is no guarantee of future results. Chart is provided for illustrative purposes and reflects back-tested and hypothetical historical performance. Please see the Performance Disclosure at the end of this document for more information regarding the inherent limitations associated with back-tested performance.

In other words, because of inflation, the USD 78,000 estimate in December 2009 can afford the same basket of goods and services as USD 65,000 in January 2003.



Panel B: CPI-Adjusted Estimated Consumption (2003 U.S. Dollars)

Source: S&P Dow Jones Indices LLC and Dimensional Fund Advisors. Back-tested data from January 2003 to December 2016. Past performance is no guarantee of future results. Chart is provided for illustrative purposes and reflects back-tested hypothetical historical performance. Please see the Performance Disclosure at the end of this document for more information regarding the inherent limitations associated with back-tested performance.

Panel C: Theoretical Estimated Consumption						
RISK MANAGEMENT STRATEGY	JANUARY 2003 (USD)	DECEMBER 2009 (USD)	MARCH 2013 (USD)			
TIPS-LDI, Nominal	64,180	77,728	83,408			
TIPS-LDI, CPI-Adjusted	64,893	65,109	64,817			
S&P U.S. Aggregate Bond Index Nominal	64,955	68,259	60,222			
S&P U.S. Aggregate Bond Index CPI-Adjusted	64,669	57,178	46,798			
S&P U.S. Treasury Bond 1-5 Year Index Nominal	64,871	64,282	50,365			
S&P U.S. Treasury Bond 1-5 Year Index CPI-Adjusted	64,585	53,846	39,139			

Source: S&P Dow Jones Indices LLC. Nominal represents the income estimate seen in nominal U.S. dollars over time; CPI-adjusted represents real purchasing power. Table is provided for illustrative purposes and reflects back-tested hypothetical historical performance. Indices are not available for direct investment. Index performance does not reflect the expenses associated with the management of an actual portfolio. Please see the Performance Disclosure at the end of this document for more information regarding the inherent limitations associated with back-tested performance.

commences, the liability considered by GRIL declines by USD 1 for each year into

Prior to the target retirement date (January 2010, in the case of Exhibit 9), the liability considered by GRIL is a 25-year stream of annual USD 1 inflation-adjusted income. Once retirement commences (again, January 2010 in Exhibit 9), the liability considered by GRIL declines by USD 1 for each year into retirement (e.g., 24 years in 2011, 23 years in 2012, etc.). Exhibit 9 assumes that at and throughout retirement, each month, Jill withdraws one-twelfth of the estimated consumption. For example, in

Once retirement

retirement.

January 2010, the estimated consumption is USD 78,000, so she "withdraws" USD 6,500 for the month, and her account is decreased by the same amount. Over time, the estimate under the LDI investment increases to keep up with inflation (light blue line in Panel A of Exhibit 9), and her theoretical purchasing power stays close to the initial estimate of USD 65,000 in January 2003 U.S. dollars (light blue dashed line in Panel B of Exhibit 9).

Let's compare the LDI performance with other fixed income strategies used in TDFs. A common strategy across TDFs is to achieve broad exposure to the bond market during accumulation and increase focus on shorter-term government and Treasury securities as the target date nears. For example, consider the S&P U.S. Aggregate Bond Index as representing the performance of a U.S. market-wide strategy and the S&P U.S. Treasury Bond 1-5 Year Index as representing the performance of short-to intermediate-term U.S. Treasuries. As seen in Exhibit 9, both of these indices have greater variability in inflation-adjusted consumption units than the S&P STRIDE's 2010 TIPS-LDI Allocation (TIPS-LDI Allocation). The annualized volatility is 7.1% and 8.7% for the two indices, respectively, versus 1.9% for the S&P STRIDE LDI. More importantly, at the end of 2009, estimated nominal consumption for the two indices was USD 68,259 and USD 64,282, respectively (USD 57,178 and USD 53,846 in January 2003 U.S. dollars). This means that real consumption declined from the January 2003 level by about 13% and 18%, respectively, for the S&P U.S. Aggregate Bond Index and the S&P U.S. Treasury Bond 1-5 Year Index.

Additionally, between October 2008 and March 2013, interest rates declined, causing the cost of GRIL to increase (see Exhibit 8). Over this period, returns of the S&P U.S. Aggregate Bond Index and the S&P U.S. Treasury Bond 1-5 Year Index did not keep pace, resulting in a decline in estimated consumption. Assuming the same withdrawals as under the LDI scenario, by March 2013 estimated nominal consumption for the two indices declined to USD 60,222 and USD 50,365, respectively (USD 46,798 and USD 39,139 in January 2003 U.S. dollars).8 Our analysis shows that fixed income investments not tied to the retirement liability or GRIL, like the S&P U.S. Aggregate Bond Index and S&P U.S. Treasury Bond 1-5 Year Index, can subject savers to interest rate and inflation risk, both of which also introduce sequencing risk in retirement.⁹ These results also have implications for our comparison of the S&P STRIDE Glide Path 2010 Index against the average 2010 TDF in consumption units, as traditional TDFs tend to allocate more assets to short-term fixed income as the target date approaches. Duration mismatches between TDFs' fixed

Fixed income investments not tied to the retirement liability or GRIL can subject savers to interest rate and inflation risk.

⁸ The discrepancy between the S&P U.S. Aggregate Bond Index and S&P U.S. Treasury Bond 1-5 Year Index for the period is due in part to the S&P U.S. Aggregate Bond Index's exposure to a positive credit premium in the period.

To learn more about using LDI in retirement planning, see Massi De Santis, "Retirement Planning: An Introduction to Liability-Driven Investing", Dimensional Fund Advisors, 2015.

income allocations and required future retirement income are common. Looking across TDFs, the average effective duration is five, with seemingly little variation approaching retirement.¹⁰

Having this risk management tool may help market participants to decide how much uncertainty in future consumption they are willing to take in order to increase expected future income. In contrast, by combining short- to intermediate-maturity bonds to a growth portfolio, market participants may reduce expected returns (relative to a growth portfolio) without a corresponding reduction in interest rate, inflation, sequencing risk, and ultimately in-retirement consumption risk. Thus, they could obtain a worse risk/return tradeoff relative to the LDI.

Systematically Reducing Income Risk

We saw above that the S&P STRIDE's 2010 TIPS-LDI Allocation is effective and may be superior to short-term fixed income at hedging inflation and interest rate risks, as well as including long-term income assets. From 2003 to 2016, a hypothetical portfolio fully invested in the S&P STRIDE 2010 TIPS-LDI allocation would have grown nominal income at approximately the growth rate of CPI, essentially resulting in an inflation-protected income stream for 2010 retirees.

The actual S&P STRIDE glide path transitions gradually from primarily growth assets to TIPS-LDI. It reaches a 75% allocation to TIPS-LDI at retirement. In order to demonstrate how income risk may be mitigated as this shift occurs, we now seek to illustrate the income-generating performance of several hypothetical static allocations of TIPS-LDI and global equities.

Having the right risk management allows market participants to decide how much uncertainty in future consumption they are willing to take in order to increase expected future income.

¹⁰ Source: Morningstar, based on effective duration on 2,364 share classes of TDFs in the Morningstar Direct Open End Fund Database, as of December 2016.

- 100% TIPS-LDI CPI-Adj. 117,500 75% TIPS-LDI/25% S&P Global BMI CPI-Adj. 50% TIPS-LDI/50% S&P Global BMI CPI-Adj. 100,000 25% TIPS-LDI/75% S&P Global BMI CPI-Adj. Growth in Consumption (USD) 82,500 65,000 47,500 2005 2007 2009 2011 2013 2015 Dec. Jan. 2003 2016

Exhibit 10: The Historical Trade-off Between Inflation-Adjusted Income Growth and Income Security With Varying Levels of Global Equities Exposure (in 2003 U.S. dollars)

Source: S&P Dow Jones Indices LLC and Dimensional Fund Advisors. Back-tested data from January 2003 to December 2016. Past performance is no guarantee of future results. Chart is provided for illustrative purposes and reflects back-tested hypothetical historical performance. Indices are not available for direct investment. Index performance does not reflect the expenses associated with the management of an actual portfolio. Please see the Performance Disclosure at the end of this document for more information regarding the inherent limitations associated with back-tested performance. Blended indices are hypothetical.

Exhibit 10 compares the previous example of a 100% TIPS-LDI allocation to various hypothetical, monthly rebalanced portfolios of TIPS-LDI and the S&P Global BMI Net Total Return Index. The S&P STRIDE glide path progresses from nearly all equity (95%) to 75% TIPS-LDI/25% global equities at the target date. Exhibit 10 depicts the trade-off between income growth and income security at varying levels of static equity exposure, thereby providing a means for grasping the potential impact of S&P STRIDE's glide path strategy on the mitigation of income risk through time. One can think of the S&P STRIDE glide path as shifting through the static profiles embodied in the exhibit, from greater income growth potential to enhanced income security, except that in the live index this transition is done on a continuous basis and more smoothly than would be implied by shifting across static allocations.

Several characteristics of the hypothetical static portfolios may further our understanding of the basic trade-off between income growth and income risk. In Exhibit 11, we see that the most aggressive portfolio (75% equities) would have theoretically generated 1.4 times the inflation-adjusted income of the 100% TIPS-LDI portfolio by December 2016. However, that income growth would have been accompanied by a significantly higher level of income uncertainty. The annualized standard deviation of hypothetical income afforded with the most aggressive portfolio is about 12.8%,

compared with 2.3% for the 100% TIPS-LDI allocation. In other words, to earn 40% more income, one would have had to accept well over five times

One can think of the S&P STRIDE glide path as shifting through the static profiles embodied in the exhibit, from greater income growth potential to enhanced income security.

the risk (as measured by standard deviation). On the other hand, a significant degree of hypothetical income growth was obtainable with a modest amount of equity exposure and a relatively mild increase in income uncertainty—as shown by the 75% TIPS-LDI/25% equities portfolio.

Exhibit 11: Income Growth Versus Income Volatility					
Based on CPI Adjusted Income Affordability (2003 U.S. dollars), 2003-2016	25% TIPS-LDI/ 75% S&P BMI	50% TIPS-LDI/ 50% S&P BMI	75% TIPS-LDI/ 25% S&P BMI	100% TIPS-LDI	
Multiple of 100% TIPS-LDI Income as of December 2016	1.4	1.3	1.2	NA	
Annualized Standard Deviation of Income (%)	12.8%	8.7%	4.7%	2.3%	
Multiple of Standard Deviation of 100% TIPS-LDI Income	5.4	3.7	2.0	NA	

Source: S&P Dow Jones Indices and Dimensional Fund Advisors. Back-tested data from 2003 to 2016. Past performance is no guarantee of future results. Table is provided for illustrative purposes and reflects back-tested hypothetical historical performance. Indices are not available for direct investment. Index performance does not reflect the expenses associated with the management of an actual portfolio. Please see the Performance Disclosure at the end of this document for more information regarding the inherent limitations associated with back-tested performance. Blended indices are hypothetical.

The 75% TIPS-LDI/25% equities portfolio is quite similar to S&P STRIDE's allocation at each index's target date.

We are now ready to compare the S&P STRIDE Glide Path 2010 Index against the average 2010 TDF in consumption units.

Evaluating Index Performance in Consumption Units

The S&P STRIDE Glide Path 2010 Index allocation in January 2003 starts with approximately 50% of the assets in the TIPS-LDI allocation. The remaining 50% is allocated to global equities (43%) and global nominal fixed income (7%). The TIPS-LDI allocation increases over time and reaches 75% in December 2009.

Let us return to Jill's example. She started in January 2003 with USD 1 million. Each month during the sample period, Jill can take her account balance and estimate her expected retirement consumption by dividing it by the cost of 2010 GRIL. We can repeat the same calculation assuming she invested her savings in the industry average of TDFs and the S&P 500. Exhibit 12 illustrates the level of estimated consumption in retirement for Jill under these alternatives.¹¹

We believe that the 75/25 mix is a reasonable allocation if one's goal is to gain income security while preserving a potential for income growth in retirement.

¹¹ Prior to the target retirement date (January 2010 in the case of Exhibit 12), the liability considered by GRIL is a 25-year stream of annual USD 1 inflation-adjusted income. Past retirement (again, January 2010 in Exhibit 12), the liability considered by GRIL declines by USD 1 for each year into retirement (e.g., 24 years in 2011, 23 years in 2012, etc.). This, combined with the fact that Exhibit 12 assumes no withdrawals are actually made from the account after 2010, means that the amount of affordable annual consumption after 2010 would naturally be expected to increase year–over-year into retirement.

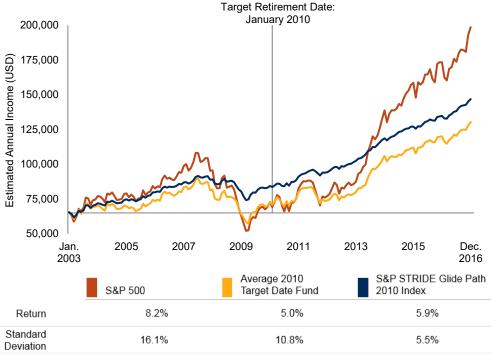


Exhibit 12: Growth of Estimated Retirement Income

The annualized volatility of monthly changes in the estimates under the average 2010 TDF is about twice the volatility of the S&P STRIDE Glide Path 2010 Index over the sample

considered.

Source: S&P 500 and S&P STRIDE Glide Path 2010 Index data from S&P Dow Jones Indices LLC. The average 2010 TDF is the asset-weighted average across the TDF families included in the Morningstar universe. As of December 2016, the data included 57 TDF families. Data from Morningstar. Past performance is no guarantee of future results. Chart is provided for illustrative purposes and reflects back-tested hypothetical historical performance. Please see the Performance Disclosure at the end of this document for more information regarding the inherent limitations associated with back-tested performance. Indices are not available for direct investment. Index performance does not reflect the expenses associated with the management of an actual portfolio. For more information, see "S&P STRIDE Index Series Description and Disclosures" in the Appendix.

Most noticeable from the Exhibit 12 is the difference in the variability of the consumption estimates between the strategies. The annualized volatility of monthly changes in the estimates under the average 2010 TDF is about twice the volatility of the S&P STRIDE Glide Path 2010 Index over the sample considered (10.8% versus 5.5%).

With the S&P STRIDE Glide Path 2010 Index, estimated consumption is USD 84,000 as of December 2009, which is higher than the USD 78,000 estimate achieved with the TIPS-LDI component only. The variability of consumption estimates is also higher than that of the LDI component only (5.5% versus 1.9%). The estimated consumption for the average 2010 TDF is USD 72,000 as of December 2009, with significantly more variability over the period (10.8%). What explains this difference?

Two years from retirement, the 2008-2009 financial crisis resulted in large changes to equity values and interest rates. Exhibit 13 shows growth of consumption over the October 2007-February 2009 period (the same peak-to-trough and recovery period we evaluated for the S&P 500 earlier).

Average 2010
S&P 500

S&P 500

S&P STRIDE Glide Path
2010 Index

21 months | 50 months | 21 months | 49 months | 20 months | 22 months | 22 months | 22 months | 25 months | 25 months | 25 months | 26 months | 2

Exhibit 13: Maximum Drawdown and Recovery of Estimated Retirement Income

 Represents maximum loss/drawdown for peak-to-trough of each index from January 2003-December 2016.

Source: S&P 500 and S&P STRIDE Glide Path 2010 Index data from S&P Dow Jones Indices LLC. The average 2010 TDF is the asset-weighted average across the TDF families included in the Morningstar universe. As of December 2016, the data included 57 TDF families. Data from Morningstar Indices are not available for direct investment. Performance does not reflect the expenses associated with the management of an actual portfolio. Past performance is no guarantee of future results. Chart is provided for illustrative purposes and reflects back-tested hypothetical historical performance. Please see the Performance Disclosure at the end of this document for more information regarding the inherent limitations associated with back-tested performance. Indices are not available for direct investment. Index performance does not reflect the expenses associated with the management of an actual portfolio. For more information, see "S&P STRIDE Index Series Description and Disclosures" in the Appendix.

The large drawdown we see for the average 2010 TDF is in large part a result of the higher equity allocation (28% versus 49%). Notice that the drawdown for the average 2010 TDF is greater in income units than it was in account balance units. This is because of the decline in interest rates that started in October 2008 (see Exhibit 8). In contrast, the drawdown for the S&P STRIDE Glide Path 2010 Index is lower in consumption units than in wealth units due to the appropriate risk management framework.

The difference in risk management strategies is much more visible after equity values began to recover in February 2009. Notice that while equity values rebounded, the cost of future consumption or GRIL increased due to a decline in interest rates that lasted until March 2013. This means that right after the financial crisis, savers in TDFs were hit by a decline in the purchasing power of their account balance in consumption units. As a result, the nominal consumption level did not reach the pre-crisis level until April 2013 (49 months), well into retirement for a 2010 retiree. This is an example of how interest rate changes and inflation can cause a loss in consumption and introduce sequencing risk.

In contrast, in October 2007, 67% of the S&P STRIDE Glide Path 2010 Index was allocated in the TIPS-LDI component. This limited the drawdown in both wealth and consumption units. In addition, the LDI allocation hedged the impact of declining interest rates during the equity rebound. For example, between March 2009 (when the rebound started) and December 2009 (right before retirement), the cost of 2010 GRIL increased by 10.6% and CPI by 1.7%. At the same time, the TIPS-LDI returned 14.0%, hedging the increase in the cost of consumption. By way of comparison, the S&P U.S. Aggregate Bond Index and S&P U.S. Treasury Bond 1-5 Year Index returned 5.9% and 1.3%, respectively, over the period, significantly lagging the increase in the cost of the liability. The

The large drawdown we see for the average 2010 TDF is in large part a result of the higher equity allocation.

benefits of the LDI strategy extend beyond risk management. This strategy is also important to help investors plan towards retirement and monitor their progress. Retirement investors are often shown estimates of projected future income. As Exhibits 9 and 12 illustrate, income projections can be sensitive to future market performance, inflation, and changes in interest rates, and there is no reliable way to say what those will be in the future. Without proper risk management, estimates are unlikely to be useful. For income estimates to be meaningful to investors planning for retirement, they need a solution that manages risks relevant to the outcome. If the goal is future consumption, the investment solution should manage consumption risk. This way, the uncertainty about future consumption can be reduced over time as participants approach retirement, providing some clarity about the estimate of in-retirement consumption their savings may support.

CONCLUSIONS

When evaluating the performance of an investment, it is important to measure performance relative to the goal. In planning for retirement, one goal typically is to be able to fund a desired standard of living for all the years in retirement. Given the dependencies of affordable consumption on interest rates and inflation, account balances may not provide a full picture of how much a retiree will be able to consume during her retirement life, so measuring performance by looking at the evolution of account balances is probably not enough. Instead, it may be beneficial to evaluate performance in consumption units that are consistent with the goal.

In this analysis, we evaluated the performance of an income-focused approach relative to traditional TDFs, a popular method of investing for retirement. When evaluated in wealth units, we observed differences in performance but found little information about the effectiveness of either approach to provide clarity or certainty around consumption in retirement.

When evaluated in a consumption unit framework, we saw meaningful differences between the two approaches. As a tool to help managing the relevant risks, the S&P STRIDE Glide Path 2010 Index can provide meaningful information about estimated levels of consumption in retirement, whereas the Average 2010 TDF showed large swings in expected retirement consumption. From a planning and monitoring perspective, highly variable estimates are not an effective investment solution for the goal.

Evaluating the effectiveness of retirement solutions in consumption terms also helps to understand the benefits of using an income-focused approach to meet retirement consumption goals. If participants have tools that provide meaningful information and an investment strategy that manages the relevant risks, they can be better informed about their retirement readiness and more empowered to make decisions that can improve retirement outcomes.

When evaluated in a consumption unit framework, we saw meaningful differences between the two approaches.

APPENDIX

S&P STRIDE Index Series Description and Disclosures

In response to the need for income-focused benchmarks within defined contribution plans, on Jan. 11, 2016, S&P Dow Jones Indices (S&P DJI) launched the S&P Shift to Retirement Income and Decumulation (STRIDE) Index Series.

The series features multi-asset class income-based indices tied to target retirement dates. Dimensional Fund Advisors worked collaboratively with S&P DJI to develop the glide path, inflation hedging, and duration hedging techniques used in these indices.

Index Series Description

The S&P Shift to Retirement Income and Decumulation (STRIDE) Index Series comprises 12 multiasset class indices, each corresponding to a particular target retirement date. The asset allocation for each index in the series is based on a predetermined life-cycle glide path. Each index is fully investable, with varying levels of exposure to equities, nominal fixed income securities, and inflationadjusted bonds.

The S&P STRIDE Index Series represents a strategy that builds a portfolio of assets to support a hedged stream of inflation-adjusted retirement income. The indices also provide a new framework for benchmarking TDFs that focus on delivering similar results. The indices are individually composed of asset class indices (an index of indices), and the index series includes target date years in five-year increments (vintages). Each index vintage covers a full life cycle of accumulation (during what are generally considered working years) and decumulation in retirement years. Beginning 20 years before each target date, the indices gradually re-allocate some of their weight from accumulation constituents to inflation-adjusted income constituents. This process is analogous to dollar cost averaging into income-producing assets. The income portion consists of a duration-hedged combination of Treasury Inflation Protection Securities (TIPS) indices. The duration of the combined TIPS indices is matched monthly to the duration of a hypothetical retirement income cash flow stream that begins at the target date and lasts for 25 years.

For More Information

General: http://spindices.com/index-family/multi-asset/sp-stride

Index Series Methodology: http://spindices.com/documents/methodologies/methodology-sp-stride-index-series.pdf

Example and more data: http://spindices.com/indices/multi-asset/sp-stride-glide-path-2005-index-total-return

The S&P STRIDE Indices is a product of S&P Dow Jones Indices LLC or its affiliates ("SPDJI"), and has been licensed for use by Dimensional Fund Advisors LP ("Dimensional"). Standard & Poor's® and S&P® are registered trademarks of Standard & Poor's Financial Services LLC ("S&P"); Dow Jones® is a registered trademark of Dow Jones Trademark Holdings LLC ("Dow Jones"); these trademarks have been licensed for use by SPDJI and sublicensed for certain purposes by Dimensional. Dimensional's Products, as defined by Dimensional from time to time, are not sponsored, endorsed, sold, or promoted

by SPDJI, S&P, Dow Jones, or their respective affiliates, and none of such parties make any representation regarding the advisability of investing in such products nor do they have any liability for any errors, omissions, or interruptions of the S&P STRIDE Indices.

Dimensional Fund Advisors LP receives compensation from S&P Dow Jones Indices in connection with licensing rights to the S&P STRIDE Indices.

PERFORMANCE DISCLOSURE

The S&P STRIDE Glide Path 2010 Index was launched on January 11, 2016. The S&P U.S. Aggregate Bond Index was launched on July 15, 2014. All information presented prior to an index's Launch Date is hypothetical (back-tested), not actual performance. The back-test calculations are based on the same methodology that was in effect on the index Launch Date. Complete index methodology details are available at www.spdji.com.

S&P Dow Jones Indices defines various dates to assist our clients in providing transparency. The First Value Date is the first day for which there is a calculated value (either live or back-tested) for a given index. The Base Date is the date at which the Index is set at a fixed value for calculation purposes. The Launch Date designates the date upon which the values of an index are first considered live: index values provided for any date or time period prior to the index's Launch Date are considered back-tested. S&P Dow Jones Indices defines the Launch Date as the date by which the values of an index are known to have been released to the public, for example via the company's public website or its datafeed to external parties. For Dow Jones-branded indices introduced prior to May 31, 2013, the Launch Date (which prior to May 31, 2013, was termed "Date of introduction") is set at a date upon which no further changes were permitted to be made to the index methodology, but that may have been prior to the Index's public release date.

Past performance of the Index is not an indication of future results. Prospective application of the methodology used to construct the Index may not result in performance commensurate with the back-test returns shown. The back-test period does not necessarily correspond to the entire available history of the Index. Please refer to the methodology paper for the Index, available at www.spdji.com for more details about the index, including the manner in which it is rebalanced, the timing of such rebalancing, criteria for additions and deletions, as well as all index calculations.

Another limitation of using back-tested information is that the back-tested calculation is generally prepared with the benefit of hindsight. Back-tested information reflects the application of the index methodology and selection of index constituents in hindsight. No hypothetical record can completely account for the impact of financial risk in actual trading. For example, there are numerous factors related to the equities, fixed income, or commodities markets in general which cannot be, and have not been accounted for in the preparation of the index information set forth, all of which can affect actual performance.

The Index returns shown do not represent the results of actual trading of investable assets/securities. S&P Dow Jones Indices LLC maintains the Index and calculates the Index levels and performance shown or discussed, but does not manage actual assets. Index returns do not reflect payment of any sales charges or fees an investor may pay to purchase the securities underlying the Index or investment funds that are intended to track the performance of the Index. The imposition of these fees and charges would cause actual and back-tested performance of the securities/fund to be lower than the Index performance shown. As a simple example, if an index returned 10% on a US \$100,000 investment for a 12-month period (or US \$10,000) and an actual asset-based fee of 1.5% was imposed at the end of the period on the investment plus accrued interest (or US \$1,650), the net return would be 8.35% (or US \$8,350) for the year. Over a three year period, an annual 1.5% fee taken at year end with an assumed 10% return per year would result in a cumulative gross return of 33.10%, a total fee of US \$5,375, and a cumulative net return of 27.2% (or US \$27,200).

GENERAL DISCLAIMER

Copyright © 2017 by S&P Dow Jones Indices LLC, a part of S&P Global. All rights reserved. Standard & Poor's ®, S&P 500 ® and S&P ® are registered trademarks of Standard & Poor's Financial Services LLC ("S&P"), a subsidiary of S&P Global. Dow Jones ® is a registered trademark of Dow Jones Trademark Holdings LLC ("Dow Jones"). Trademarks have been licensed to S&P Dow Jones Indices LLC. Redistribution, reproduction and/or photocopying in whole or in part are prohibited without written permission. This document does not constitute an offer of services in jurisdictions where S&P Dow Jones Indices LLC, Dow Jones, S&P or their respective affiliates (collectively "S&P Dow Jones Indices") do not have the necessary licenses. All information provided by S&P Dow Jones Indices is impersonal and not tailored to the needs of any person, entity or group of persons. S&P Dow Jones Indices receives compensation in connection with licensing its indices to third parties. Past performance of an index is not a guarantee of future results.

It is not possible to invest directly in an index. Exposure to an asset class represented by an index is available through investable instruments based on that index. S&P Dow Jones Indices does not sponsor, endorse, sell, promote or manage any investment fund or other investment vehicle that is offered by third parties and that seeks to provide an investment return based on the performance of any index. S&P Dow Jones Indices makes no assurance that investment products based on the index will accurately track index performance or provide positive investment returns. S&P Dow Jones Indices LLC is not an investment advisor, and S&P Dow Jones Indices makes no representation regarding the advisability of investing in any such investment fund or other investment vehicle. A decision to invest in any such investment fund or other investment vehicle should not be made in reliance on any of the statements set forth in this document. Prospective investors are advised to make an investment in any such fund or other vehicle only after carefully considering the risks associated with investing in such funds, as detailed in an offering memorandum or similar document that is prepared by or on behalf of the issuer of the investment fund or other vehicle. Inclusion of a security within an index is not a recommendation by S&P Dow Jones Indices to buy, sell, or hold such security, nor is it considered to be investment advice.

These materials have been prepared solely for informational purposes based upon information generally available to the public and from sources believed to be reliable. No content contained in these materials (including index data, ratings, credit-related analyses and data, research, valuations, model, software or other application or output therefrom) or any part thereof (Content) may be modified, reverse-engineered, reproduced or distributed in any form or by any means, or stored in a database or retrieval system, without the prior written permission of S&P Dow Jones Indices. The Content shall not be used for any unlawful or unauthorized purposes. S&P Dow Jones Indices and its third-party data providers and licensors (collectively "S&P Dow Jones Indices Parties") do not guarantee the accuracy, completeness, timeliness or availability of the Content. S&P Dow Jones Indices Parties are not responsible for any errors or omissions, regardless of the cause, for the results obtained from the use of the Content. THE CONTENT IS PROVIDED ON AN "AS IS" BASIS. S&P DOW JONES INDICES PARTIES DISCLAIM ANY AND ALL EXPRESS OR IMPLIED WARRANTIES, INCLUDING, BUT NOT LIMITED TO, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE, FREEDOM FROM BUGS, SOFTWARE ERRORS OR DEFECTS, THAT THE CONTENT'S FUNCTIONING WILL BE UNINTERRUPTED OR THAT THE CONTENT WILL OPERATE WITH ANY SOFTWARE OR HARDWARE CONFIGURATION. In no event shall S&P Dow Jones Indices Parties be liable to any party for any direct, incidental, exemplary, compensatory, punitive, special or consequential damages, costs, expenses, legal fees, or losses (including, without limitation, lost income or lost profits and opportunity costs) in connection with any use of the Content even if advised of the possibility of such damages.

S&P Dow Jones Indices keeps certain activities of its business units separate from each other in order to preserve the independence and objectivity of their respective activities. As a result, certain business units of S&P Dow Jones Indices may have information that is not available to other business units. S&P Dow Jones Indices has established policies and procedures to maintain the confidentiality of certain non-public information received in connection with each analytical process.

In addition, S&P Dow Jones Indices provides a wide range of services to, or relating to, many organizations, including issuers of securities, investment advisers, broker-dealers, investment banks, other financial institutions and financial intermediaries, and accordingly may receive fees or other economic benefits from those organizations, including organizations whose securities or services they may recommend, rate, include in model portfolios, evaluate or otherwise address.



RESEARCH

Planning and Investing for Retirement Consumption

September 2017

Massi De Santis, PhD Vice President RESEARCH For most people, a successful retirement begins with being able to maintain the standard of living they are accustomed to. This means the primary goal of their retirement savings is to help sustain their desired, inflation-adjusted expenses throughout retirement: a "consumption stream." Defining the goal as an in-retirement consumption stream is a key step in designing an appropriate investment solution.

Any asset allocation decision represents a tradeoff between the opportunity of future growth and reducing uncertainty about future outcomes. Accordingly, a solution to the retirement problem should provide the ability to grow assets in an effort to increase expected consumption in retirement while seeking to manage the uncertainty of retirement consumption. Clearly defining the risks for the goal can help identify investment instruments that help manage these risks effectively and lead to a better tradeoff for investors.

If the goal is a future consumption stream, the key uncertainty is how much consumption the accumulated savings can sustain. This uncertainty is driven by the uncertainty of future stock and bond returns, interest rates, and inflation. We call these market risk, interest rate risk, and inflation risk.

In this article we describe Dimensional's approach to managing the uncertainty of in-retirement consumption, considering the key risks that affect this uncertainty. After the appropriate risk management strategy for the goal is identified, the asset allocation question becomes how to balance the tradeoff between growth assets and risk management assets. This question can then be addressed using tools from modern life cycle finance research. Separate from market, interest rate, and inflation risks is longevity risk. We will describe one approach to managing this risk.

As discussed below, identifying the appropriate risk management strategy is not only a crucial element of the asset allocation question but also a key aspect of planning and monitoring progress towards the retirement goal. The risk management strategy allows communication in terms of units that matter for the goal (meaningful communication)—in this case a future consumption stream. Through meaningful communication, the risk management strategy enables savers to make important decisions. How much do I need to save? When can I retire? How much can I expect to withdraw from my retirement account every month? What is the uncertainty around these estimates?

While this article does not address the details of implementation, Dimensional has developed a set of solutions, including target date retirement income funds, that implement the life cycle approach we describe here. Retirement investors can use Dimensional's mutual fund solutions as a standalone solution or in combination with other solutions that help manage the uncertainty of future retirement income, including annuities.

RETIREMENT CONSUMPTION AND RISK MANAGEMENT

The first step to determine how to manage key risks is to define how long accumulated savings can be expected to support in-retirement consumption. Starting with life expectancy at the typical retirement age is usually a good place to begin. It also makes sense to include a buffer to account for uncertainty about life expectancy. Assuming an average life expectancy of 20 years plus a buffer of five years, the retirement goal can be thought of as \$1 of inflation-adjusted consumption over 25 years.

With this framework for the withdrawal period, we can think about a solution that manages the volatility of how much in-retirement consumption an investor's accumulated savings can support over that period. At any point in time, the goal illustrated in **Exhibit 1** has a cost, which can be computed as the present value of the future cash flows. This cost can be estimated using real interest rates. Real interest rates are used because we think of the consumption stream in inflation-adjusted terms.

The cost of the goal will fluctuate with changes in inflation and interest rates. For example, if interest rates go down (up), the cost of the goal goes up (down). Stated differently, this implies that for a given account balance, the amount that can be consumed is lower (higher) when interest rates are lower (higher). Interest rates constitute a risk to the level of consumption that can be sustained from a level of savings. Inflation has a similar effect. The purchasing power of an account balance declines with positive inflation and increases with negative inflation.

The sensitivity of the goal to real interest rates and inflation depends on the maturity of the cash flows. The longer the average maturity, or more technically the duration of the cash flow, the higher the sensitivity.\(^1\) An investment that matches the sensitivity of the goal to interest rates and inflation can reduce the uncertainty about how much consumption can be sustained with the investment. This can be achieved by computing the duration of the in-retirement consumption stream and constructing an inflation-protected portfolio of government bonds with the same duration. This is an example of liability-driven investing or "LDI."\(^2\)



For illustrative purposes only. Not guaranteed.

^{1.} Duration is a measure of the sensitivity of a cash flow stream (like a bond) to interest rates. It is a weighted average maturity across the cash flows, with weights given by the relative present value of each cash flow.

^{2.} A liability-driven investment (LDI) strategy is designed to focus on assets that match future liabilities. LDI strategies contain certain risks that prospective investors should evaluate and understand prior to making a decision to invest. These risks may include, but are not limited to, interest rate risk, counterparty risk, liquidity risk, and leverage risk.

How does this investment strategy reduce uncertainty about future consumption? Because the sensitivity of the investment to inflation and interest rate risks is the same as that of the goal, the value of the investment tends to increase (decline) when interest rates go down (up) or when inflation is positive (negative), thus protecting the future purchasing power of the portfolio.

A COMPLETE SOLUTION

The importance of the risk management framework goes beyond managing key risks like inflation and interest rates. The risk management strategy is a key element in balancing the tradeoff between growth opportunities and reducing the uncertainty of in-retirement consumption. It allows investors to control the level of exposure to market risk they desire in expectation of future growth over their working career and in retirement.

Modern life cycle research highlights the importance of considering (i) the entire life cycle of the investor and (ii) the sources of capital for the goal when making asset allocation decisions. The first element means considering the retirement consumption goal throughout the accumulation phase, not simply waiting until retirement to figure out how to sustain future consumption. The second point is important because different sources of capital can have different risks for the goal. Most people fund their consumption through a combination of accumulated savings (financial capital) and future savings (human capital). Early in an investor's career, most of the funding for retirement is expected to come from future savings, while financial capital is a small fraction of expected funding. At this stage, investing in a growth portfolio does not have a material effect on the overall risk of the total retirement funding because most of it will happen in the future. But as time goes by, the accumulated assets become a larger fraction of the funding and a more conservative allocation is needed for those assets.

The duration of the future consumption stream can be matched as early as around 20 years prior to retirement. Investors can devote a portion of their assets to risk management gradually over the 20 years, effectively saving toward "slices" of future consumption and reducing uncertainty about the level of retirement

consumption the savings can support. At retirement, the focus of the allocation is on providing clarity and confidence about how much consumption the savings can support, so the majority of the assets are invested in the LDI risk management strategy. Following this life cycle approach allows investors to seamlessly transition from their working life into retirement.

WITHDRAWAL RATES AND SEQUENCING RISK

The question about how much consumption a portfolio can generate over time is often asked in the context of a traditional portfolio of stocks and bonds in which the fixed income is used to reduce portfolio volatility rather than matched to the consumption goal. Given the portfolio, what is a withdrawal rate that the portfolio can sustain with a high likelihood?

Without the proper risk management, the estimated withdrawal rate is necessarily based on assumptions about future expected returns from that portfolio. This causes uncertainty, above and beyond the time series variability of returns, about how long money can last in retirement.

For investors drawing down from their portfolios, the sequence in which they experience returns may also matter to their ability to sustain consumption. For example, a sequence of bad market returns early in retirement increases the likelihood of running out of money early. Market risk is not the only cause of sequencing risk. Interest rates and inflation risks also matter. For example, an unexpected rise in inflation early in retirement increases the likelihood of running out of money early. A traditional allocation to stocks and bonds introduces sequencing risk because of market, interest rate, and inflation risks.

In contrast, the risk management strategy we described solves both of these problems. First, the LDI strategy does not need estimates of future returns to determine the level of income it can sustain. Market data on real interest rates at any point in time can be used. Because a retiree has the majority of their savings for the consumption goal invested in the consumption risk management strategy, the reliance on assumptions is greatly reduced. Second, because a large portion of the portfolio is invested in assets that hedge consumption risk, sequencing risk is also reduced.³

^{3.} With the LDI approach, sequencing risk only comes though growth assets, which in retirement are a small fraction of the portfolio.

IMPORTANCE OF RISK MANAGEMENT FOR PLANNING

Having the right risk management strategy is also important to help investors plan toward retirement and monitor their progress. Retirement investors are often shown estimates of projected future income. It is important to realize that income projections can be very sensitive to future changes in the market, inflation, and interest rates, and there is no reliable way to say what those will be in the future. Without the proper risk management strategy, the estimates are not very meaningful. For income estimates to be meaningful to an investor, so that he or she can use them to plan for retirement, investors need a solution that manages risks related to the projections. If the goal is future consumption, the investment solution should manage consumption risk. This way, the uncertainty about future consumption can be reduced over time as participants approach retirement, providing clarity and confidence about the estimate of in-retirement consumption their savings can support.

If participants have tools that provide the right information and manage the right risks, they can be empowered to solve their retirement problem. How much do I need to save? When can I retire? What is the monthly paycheck I can expect from my savings? Dimensional has developed a retirement income calculator to help retirement savers plan and budget for retirement consumption.

LONGEVITY RISK AND ANNUITIES

In defining the consumption goal, we used life expectancy plus a buffer to account for uncertainty about one's lifetime. This approach is helpful in that it provides a reasonable framework for investors who plan to draw down from their portfolios. The approach may require an adjustment to consumption should the investor realize he or she needs to withdraw for longer than planned. For investors concerned

with longevity risk, one risk management tool is annuities. For example, investors could plan for the 25-year horizon using available target date retirement income funds and devote a portion of their savings to deferred annuities that start paying 25 years into retirement. Additionally, annuities with income benefits can also be used as a tool to reduce the volatility of lifetime retirement income.

Dimensional's retirement solutions, annuities, and a combination of both can be used to provide more clarity and confidence about future retirement consumption, making their planned consumption stream less subject to market, interest rate, inflation, sequencing of returns, and longevity risks.

CONCLUSIONS

A good retirement solution should provide robust and well-diversified strategies that are expected to grow the value of a participants' savings so they can afford higher levels of consumption in the future, while managing uncertainty about the level of future retirement consumption the portfolio can support.

The asset allocation framework should balance the tradeoff between the growth objective and managing the risks associated with the uncertainty about the level of consumption. The right risk management strategies remove the need to rely heavily on assumptions about future returns, making information about future retirement consumption meaningful. These tools can empower investors to make informed decisions about their retirement future.

This information is provided for registered investment advisors and institutional investors and is not intended for public use. Dimensional Fund Advisors LP is an investment advisor registered with the Securities and Exchange Commission. Consider the investment objectives, risks and charges and expenses of the Dimensional funds carefully before investing. For this and other information about the Dimensional funds, please read the prospectus carefully before investing. Prospectuses are available by calling Dimensional Fund Advisors collect at (512) 306-7400 or at us.dimensional.com. Dimensional funds are distributed by DFA Securities LLC.

Insurance and annuity products are not offered through Dimensional.

Investments in target date funds are subject to the risks of their underlying funds, and asset allocations are subject to change over time in accordance with each fund's prospectus. An investment in or retirement income from a Target Date Portfolio is not guaranteed at any time, including on or after the target date. An investment in or retirement income from a Target Date Portfolio does not eliminate the need for investors to decide—before investing and periodically thereafter—whether the Portfolio fits their financial situation. For more information please refer to the prospectus. There is not quarantee strategies will be successful.

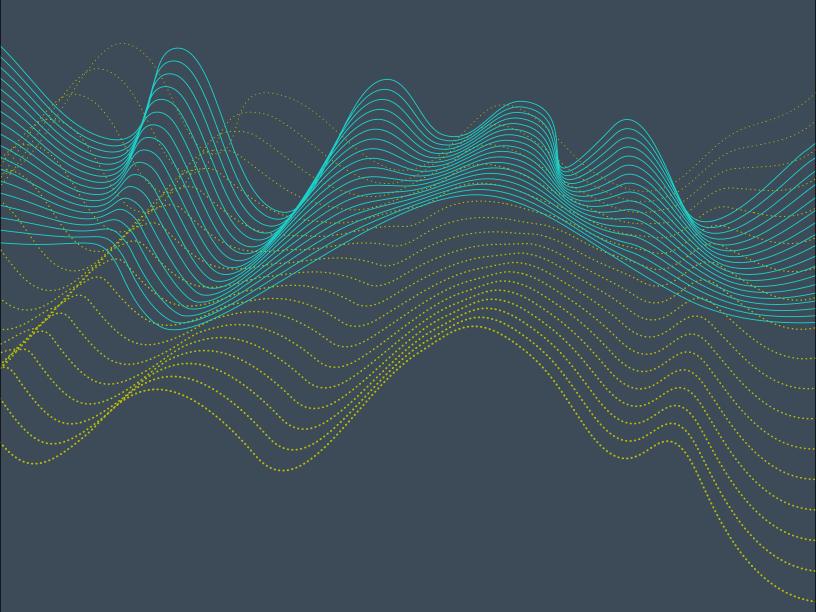
The information provided does not constitute investment advice, and it should not be relied on as such. It should not be considered a solicitation to buy or an offer to sell a security. It does not take into account any investor's particular investment objectives, strategies, tax status, or investment horizon. You should consult your tax and financial advisor. All material has been obtained from sources believed to be reliable. There is no representation or warranty as to the accuracy of the information, and neither Dimensional Fund advisors LP nor any of its affiliates shall have liability for the decisions based on such information.

dimensional.com





US MUTUAL FUND LANDSCAPE 2018



The U.S. mutual funds referred to in this publication are not registered as managed investment schemes with the Australian Securities and Investments Commission and as such these funds are not currently available to Australian investors.

This publication has been prepared by Dimensional Fund Advisors LP and is provided in Australia by DFA Australia Limited (AFS Licence No. 238093, ABN 46 065 937 671

Each year, Dimensional analyzes returns from a large sample of US-based mutual funds. Our objective is to document the power of market prices by assessing the performance of mutual fund managers.

This year's study updates results through 2017. The evidence shows that a majority of fund managers in the sample failed to deliver benchmark-beating* returns after costs.

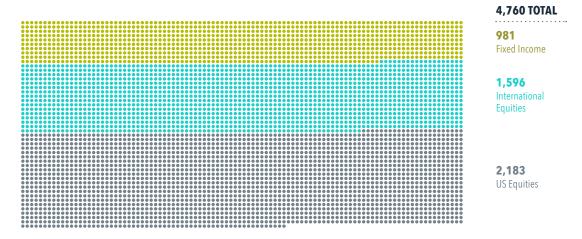
We believe that the results of this research provide a strong case for relying on market prices.

^{*}In the study results, "benchmark" refers to the Morningstar category index used to evaluate the performance of each respective mutual fund in the sample. See Data Appendix for additional information.

SURVEYING THE LANDSCAPE

US-Based Mutual Funds, 2017

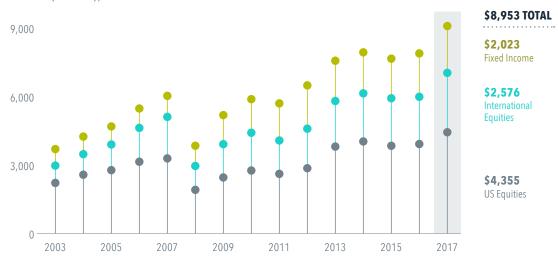
Number of equity and fixed income funds in the study



Number of US-domiciled funds in the sample as of December 31, 2017. International equities include non-US developed and emerging markets funds.

Assets under Management

In USD (billions), 2003–2017



Total value of assets in the sample over the past 15 years. Numbers may not sum due to rounding.

The global financial markets process millions of trades worth hundreds of billions of dollars each day. These trades reflect the viewpoints of buyers and sellers who are investing their capital. Using these trades as inputs, the market functions as a powerful information processing mechanism, aggregating vast amounts of dispersed information into prices and driving them toward fair value. Investors who attempt to outguess prices are pitting their knowledge against the collective wisdom of all market participants.

So, are investors better off relying on market prices or searching for mispriced securities?

Mutual fund industry performance offers one test of the market's pricing power. If markets do not effectively incorporate information into securities prices, then opportunities may arise for professional managers to identify pricing "mistakes" and convert them into higher returns. In this scenario, we might expect to see many mutual funds outperforming benchmarks. But the evidence suggests otherwise.

Across thousands of funds covering a broad range of manager philosophies, objectives, and styles, a majority of the funds evaluated did not outperform benchmarks after costs. These findings suggest that investors can rely on market prices.

Let's consider the details.

This study evaluates a sample of 4,760 US-based mutual funds through 2017. The funds collectively managed almost \$9 trillion in shareholder wealth.

DISAPPEARING FUNDS

Few Mutual Funds Have Survived and Outperformed

Performance periods ending December 31, 2017



The sample includes funds at the beginning of the 5-, 10-, and 15-year periods ending December 31, 2017. Survivors are funds that had returns for every month in the sample period. Winners are funds that survived and outperformed their respective Morningstar category index over the period.

The size of the mutual fund landscape masks the fact that many funds disappear each year, often due to poor investment performance.

Investors may be surprised by how many mutual funds become obsolete over time. About half of the equity and fixed income funds were no longer available after 15 years.

Including these non-surviving funds in the sample is an important part of assessing mutual fund manager performance. The evidence suggests that only a low percentage of funds in the original sample were "winners"—defined as those that both survived and outperformed benchmarks.

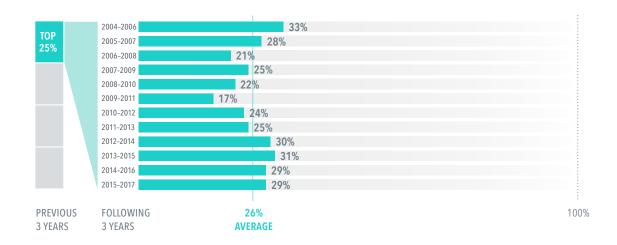
Both survival and outperformance rates tended to fall as the time horizon expands. For the 15-year period through 2017, only 14% of equity funds and 13% of fixed income funds survived and outperformed their benchmarks.

THE SEARCH FOR PERSISTENCE

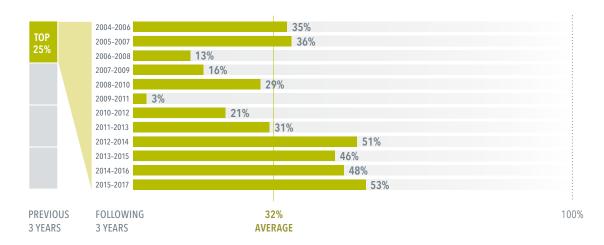
A Fund's Past Performance Is Not Enough to Predict Future Results

Percentage of funds that were top-quartile performers in consecutive three-year periods





FIXED INCOME FUNDS



At the end of each year, funds are sorted within their category based on their three-year total return. The tables show the percentage of funds in the top quartile (25%) of three-year performance that ranked in the top quartile of performance over the following three years. Example (upper chart): For 2017, only 29% of equity funds were ranked in the top quartile of performance in their category in both the previous period (2012–2014) and subsequent period (2015–2017).

Some investors may resort to using track records as a guide to selecting funds, reasoning that a manager's past success is likely to continue in the future.

Does this assumption pay off? The research offers evidence to the contrary.

The exhibit shows that among funds ranked in the top quartile (25%) based on previous three-year returns, a minority also ranked in the top quartile of returns over the following three-year period. This lack of persistence casts further doubt on the ability of managers to consistently gain an informational advantage on the market.

Some fund managers might be better than others, but track records alone may not provide enough insight to identify management skill. Stock and bond returns contain a lot of noise, and impressive track records may result from good luck. The assumption that strong past performance will continue often proves faulty, leaving many investors disappointed.

Most funds in the top quartile of past three-year returns did not repeat their top-quartile ranking over the following three years. Over the periods studied, top-quartile persistence of three-year performers averaged 26% for equity funds and 32% for fixed income funds.

THE IMPACT OF COSTS

High Costs Can Reduce Performance

Percentage of winners and losers based on expense ratios

EQUITY FUNDS



FIXED INCOME FUNDS



The sample includes funds at the beginning of the 5-, 10-, and 15-year periods ending December 31, 2017. Funds are sorted into quartiles within their category based on average expense ratio over the sample period. The chart shows the percentage of winner and loser funds by expense ratio quartile for each period. Winners are funds that survived and outperformed their respective Morningstar category index, and losers are funds that either did not survive or did not outperform their respective Morningstar category index.

If competition drives prices to fair value, then one might wonder why so many funds underperform. A major factor is high costs, which reduce an investor's net return and increase the hurdle for a fund to outperform.

All mutual funds incur costs. Some costs, such as expense ratios, are easily observed, while others, including trading costs, are more difficult to measure. The question is not whether investors must bear some costs, but whether the costs are reasonable and indicative of the value added by a fund manager's decisions.

Let's consider how one type of explicit cost—expense ratios—can impact fund performance. Our research shows that mutual funds with the highest expense ratios had the lowest rates of outperformance. Especially for longer horizons, the cost hurdle becomes too high for most funds to overcome.

High fees can contribute to underperformance because the higher a fund's costs, the higher its return must be to outperform its benchmark. Therefore, investors may be able to increase the odds of a successful investment experience by avoiding funds with high expense ratios. Funds with higher average expense ratios had lower rates of outperformance. For the 15-year period through 2017, 6% of the highest-cost equity funds and 9% of the highest-cost fixed income funds outperformed their benchmarks.

COSTLY TURNOVER

High Trading Costs Also Impact Returns

Percentage of winners and losers based on turnover





The sample includes equity funds at the beginning of the 5-, 10-, and 15-year periods ending December 31, 2017. Funds are sorted into quartiles within their category based on average turnover during the sample period. The chart shows the percentage of winner and loser funds by turnover quartile for each period. Winners are funds that survived and outperformed their respective Morningstar category index, and losers are funds that either did not survive or did not outperform their respective Morningstar category index.

Other activities can add substantially to a mutual fund's overall cost burden. Equity trading costs, such as brokerage fees, bid-ask spreads, and price impact, can be just as large as a fund's expense ratio. Trading costs are difficult to observe and measure. Nonetheless, they impact a fund's return—and the higher these costs, the higher the outperformance hurdle.

Among equity funds, portfolio turnover can offer a rough proxy for trading costs.² Turnover varies dramatically across equity funds, reflecting many different management styles. Managers who trade frequently in their attempts to add value typically incur greater turnover and higher trading costs.

Although turnover is just one way to approximate trading costs, the study indicates that funds with higher turnover are more likely to underperform their benchmarks. The reason is that excessive turnover creates higher trading costs, which can detract from returns.

For all periods examined, equity funds in the highest average turnover quartile had the lowest rates of outperformance. For the 15-year period through 2017, 9% of the highest-turnover funds outperformed.

^{1.} Bid-ask spread is the difference between the highest price a buyer is willing to pay for an asset and the lowest price for which a seller is willing to sell it.

^{2.} Fixed income funds are excluded from the analysis because turnover is not a good proxy for fixed income trading costs.

SUMMARY

The performance of US mutual funds illustrates the power of market prices. For the periods examined, the research shows that:

- Outperforming funds were in the minority.
- Strong track records failed to persist.
- High costs and excessive turnover may have contributed to underperformance.

The results of this study suggest that investors are best served by relying on market prices. Investment methods based on a manager's ability to outguess market prices have resulted in underperformance for the vast majority of mutual funds.

Despite the evidence, many investors continue searching for winning mutual funds and look to past performance as the main criterion for evaluating a manager's future potential. In their pursuit of returns, many investors surrender performance to high fees, high turnover, and other costs of owning the mutual funds.

We believe the underperformance of most US mutual funds highlights an important investment principle: The capital markets do a good job of pricing securities, which intensifies a fund's challenge to beat its benchmark and other market participants. When fund managers charge high fees and trade frequently, they must overcome high cost barriers as they try to outperform the market.

Choosing a long-term winner involves more than seeking out funds with a successful track record, as past performance offers no guarantee of a successful investment outcome in the future. Moreover, looking at past performance is only one way to evaluate a manager.

In the end, investors should consider other aspects of a mutual fund, such as underlying market philosophy, robustness in portfolio design, and attention to total costs, all of which are important to delivering a good investment experience and, ultimately, helping investors achieve their goals.

Data Appendix

US-domiciled open-end mutual fund data is from Morningstar and Center for Research in Security Prices (CRSP) from the University of Chicago.

Equity fund sample includes the Morningstar historical categories: Diversified Emerging Markets, Europe Stock, Foreign Large Blend, Foreign Large Growth, Foreign Large Value, Foreign Small/Mid Blend, Foreign Small/Mid Growth, Foreign Small/Mid Value, Japan Stock, Large Blend, Large Growth, Large Value, Mid-Cap Blend, Mid-Cap Growth, Mid-Cap Value, Miscellaneous Region, Pacific/Asia ex-Japan Stock, Small Blend, Small Growth, Small Value, and World Stock. For additional information regarding the Morningstar historical categories, please see "The Morningstar Category Classifications" at morningstardirect. morningstar.com/clientcomm/Morningstar_Categories_US_April_2016.pdf.

Fixed income fund sample includes the Morningstar historical categories: Corporate Bond, High Yield Bond, Inflation-Protected Bond, Intermediate Government, Intermediate-Term Bond, Muni California Intermediate, Muni California Long, Muni Massachusetts, Muni Minnesota, Muni National Intermediate, Muni National Long, Muni National Short, Muni New Jersey, Muni New York Intermediate, Muni New York Long, Muni Ohio, Muni Pennsylvania, Muni Single State Intermediate, Muni Single State Long, Muni Single State Short, Short Government, Short-Term Bond, Ultrashort Bond, and World Bond. For additional information regarding the Morningstar historical categories, please see "The Morningstar Category Classifications" at morningstardirect.morningstar.com/clientcomm/Morningstar_Categories_US_April_2016.pdf.

Index funds and fund-of-funds are excluded from the sample. Net assets for funds with multiple share classes or feeder funds are a sum of the individual share class total net assets. The return, expense ratio, and turnover for funds with multiple share classes are taken as the asset-weighted average of the individual share class observations. Fund share classes are aggregated at the strategy level using Morningstar FundID and CRSP portfolio number.

Each fund is evaluated relative to the Morningstar category index assigned to the fund's category at the start of the evaluation period. So, if, for example, a fund changes from Large Value to Large Growth during the evaluation period, then its return will still be compared to the Large Value category index. Surviving funds are those with return observations for every month of the sample period. Winner funds are those that survived and whose cumulative net return over the period exceeded that of their respective Morningstar category index. Loser funds are funds that did not survive the period or whose cumulative net return did not exceed their respective Morningstar category index.

Index data provided by Bloomberg Barclays, MSCI, Russell, FTSE, and S&P Dow Jones Indices. Bloomberg Barclays data provided by Bloomberg. MSCI data © MSCI 2018, all rights reserved. Frank Russell Company is the source and owner of the trademarks, service marks, and copyrights related to the Russell Indexes. FTSE fixed income indices © 2018 FTSE Fixed Income LLC, all rights reserved. S&P and Dow Jones data © 2018 S&P Dow Jones Indices LLC, a division of S&P Global.

Indices are not available for direct investment. Their performance does not reflect the expenses associated with management of an actual portfolio.

Dimensional Fund Advisors LP is an investment advisor registered with the Securities and Exchange Commission.

Mutual fund investment values will fluctuate, and shares, when redeemed, may be worth more or less than original cost. Diversification neither assures a profit nor guarantees against a loss in a declining market. There is no guarantee investment strategies will be successful. Past performance is no guarantee of future results.

AMERICAS
Austin, Charlotte, Santa Monica, Toronto, Vancouver

EUROPE London, Amsterdam, Berlin ASIA PACIFIC Sydney, Melbourne, Singapore, Hong Kong, Tokyo

dimensional.com

