RETIREMENT PLAN REVIEW
PCA RETIREMENT & BENEFITS, INC.
2nd Quarter 2016

THE BUILDING BLOCKS OF INVESTMENT PERFORMANCE

Our goal for every Core and Target Retirement Fund in the PCA Retirement Plan is for gross of fees returns to exceed the corresponding benchmark returns.

Over the almost forty years of my experience managing assets for individuals and institutions, I feel like I have almost seen it all. But I know this is not true. For instance, our collective experience during the 'Great Recession,' beginning in 2007, reveals that none of us has seen it all. I suppose I need to correct the statement above and simply conclude with, "I have seen a lot!"

One life and professional 'experience' I have agonized over has been periods when investment results under my watch have been below average. Sadly, one of those periods recently occurred in the PCA Retirement Plan. After experiencing generally good performance in 2012 and 2013, the last two calendar years have clocked returns below our expectations. When this happens, the experience is disheartening for everyone, especially if the gross return for the period is negative. Our goal for every Core and Target Retirement Fund in the PCA Retirement Plan is for gross of fees returns to ***exceed*** the corresponding benchmark returns. Participants in the PCA Retirement Plan can easily access information regarding net of fees fund performance relative to corresponding benchmarks at the following fund fact sheet links: pcarbi.org/core-funds and pcarbi.org/target-funds. In addition to this information, I have also started writing a quarterly summary of PCA Target Funds investment performance. We call this report the Quarterly Performance Review. You will find this document at the following link: pcarbi.org/wp-content/uploads/2014/08/TF-Qtr-Performance-Review-Q1-2016-update.pdf.

Achieving good investment performance over the long-term has been a topic of considerable research. On one hand, it would seem that fixing the problem of under-performance should be as simple as firing the under-performing culprit, i.e. investment manager.

—Continued on page 3

BREXIT: A Summary View

The recent news of Great Britain's popular vote to exit (aka, Brexit) the European Union (EU) came as a shock to the world on June 24th. Because it was expected that the "Remain" voters would prevail, market volatility was greater than expected and investors were generally confused about what impact this news would have on financial markets around the world. On the day the story broke, the S&P 500 closed down 3.6%. As this news has slowly been digested here in the United States, markets have rebounded. The S&P 500 was up just over 1.7% per day on June 28th and 29th.

Despite what appears to be an orderly recovery after this international shock, this news is a serious matter, especially for Britain. The idea of leaving the EU was sold to the British public largely on the backs of immigration controversy and presumed savings if the country separated itself from the EU. It is important to remember that the concept of the EU, since its inception, has been somewhat controversial since its construct has largely been based on trade economics rather than a political or monetary (agreement on central

—Continued on page 3

Building Blocks - *Continued from page 1*

I wish it was actually that easy. Achieving good investment performance is a ***process*** that looks more like building a winning college football team. Such an effort requires a supportive administration with a strong budget, talented coaches, motivated and hardworking athletes, proper facilities, great support programs like weight training, and a significant fan base. While we are not trying to build a winning football team here at PCA Retirement & Benefits, Inc. (RBI); we do believe this illustrates well the confluence of factors that result in performance success over the long term. Detailed below are some of those factors.

Oversight Team - The most critical component of a successful investment management program is found in the quality of the personnel providing oversight. At RBI we have a very clear and consistently applied philosophy regarding oversight. We believe that the individuals charged with making decisions for

Achieving good investment performance is a process that looks more like building a winning college football team.

the PCA Retirement Plan must have professional experience in the management of investment products. I have highlighted the expertise of RBI's Investment Committee in one of our 2015 publications. (pcarbi.org/wp-content/uploads/2014/ 09/ RPR2ndQtrWeb15.pdf) The individuals featured in this article are experts in the field of investment management and have a collectively long history in many types of market environments.

Competitive Fees - Asset management fees are charged against the returns that investors earn on retirement portfolios. RBI has a significant responsibility to regularly monitor and evaluate fees charged against the PCA Retirement Plan. One of the key measurements we use is the yearly overall expense ratio of the plan. This past year (2015) the expense ratio was 0.93%. This expense has been falling since 2010 (i.e. near the bottom of the Great Recession) when the expense ratio was 1.15%. One method we use to keep fees low is the incorporation of passive fund products in certain asset classes where the opportunities for performance have proven to be historically modest. This strategy puts us in the category of what the investment industry calls a hybrid retirement plan. Hybrid plans are those where part of the assets are managed in a passive investment strategy with the balance managed in an active investment strategy. (Passive investing is a strategy where the manger simply replicates the securities in the benchmark, and active investing is a strategy where the manager chooses securities based on a specific valuation methodology.) We believe this dual approach reduces fees while also placing the plan in a position to benefit from our active investment manager's performance.

Proprietary Target Retirement Funds - The PCA Target Retirement Funds have been created very specifically with PCA families in mind. First, they offer our participants the ability to coordinate an individual's normal retirement date with a fund that is specifically constructed for the investor. Each fund is diversified in a specific manner to address both issues of risk and return. This means that as a person ages, his or her PCA Target Retirement Fund is proactively managed in an attempt to reduce market volatility as retirement approaches. The Investment Committee has also acted proactively to reduce the participant's exposure to long term bonds, especially in funds managed for individuals getting closer to their retirement dates. Another excellent feature of the target retirement funds is that the majority of the assets are morally screened. We exclude investments in companies involved in abortion, alcohol, gambling, tobacco, pornography, certain lifestyle issues, bioethics, and human rights violations.

Performance Evaluations - The assets of the PCA Retirement Plan are managed daily by nineteen investment management firms located throughout the United States and in Edinburgh, Scotland. Performance evaluations are conducted quarterly by our investment consultant, Callan Associates, Inc., and these reports are then evaluated by the RBI Investment Committee and the staff. Each of our investment management firms is evaluated based on its performance relative to a benchmark and a universe of investment management peers. The RBI Investment Committee and our investment consultants at Callan work together to determine which managers we would like to appear before the committee, in person, to provide deeper insights into their performance results. The analysis reports from our consultant and interviews with investment managers are very important inputs into our decision to either retain or dismiss one of our investment managers.

Periods of under-performance, even in well managed retirement plans, are not unusual. History tells us that these periods will come and go. That said, it is always critical that RBI, as the

Continued on page 4

Annuities: *Are sales incentives stacked against the investor?*

One issue in the Annuity Market, as experts see it, is in the incentives the industry creates to sell certain annuity products.

Sales of annuities is big business. Last year, $237 billion dollars' worth of annuities were sold to U.S. investors.[1] The appeal of these types of investment products varies, but many investors are attracted to the guaranteed income payments provided by certain annuities. Years of investing in the financial markets have taken a toll on the emotional health of some investors. These individuals tend to be averse to risk and are attracted to the dependable income offered through some annuities. However, most investors find it difficult to evaluate their annuity options. Annuities are complex financial vehicles. The governing document of an annuity is typically long and filled with legalese and undecipherable industry jargon, making it difficult to evaluate and challenging to compare. Investors interested in annuities find themselves in a precarious situation. They are at the mercy of a salesperson to find an optimal annuity for them and their family. The nagging question many investors wrestle with is whether their agent is looking out for their best interest.

It would be wrong to paint all annuity salespeople with a broad brush. I am confident there are respectable annuity agents, and I do not claim to know the motivations of their hearts. These agents are simply selling an investment product and that product is neither inherently good nor bad. The insurance industry creates low-cost, high-quality annuities, high-cost, low-quality annuities and everything in between. The problem, as experts see it, is in the incentives the industry creates to sell certain annuity products. The annuity market, these days, is replete with annuities that provide high profit margins to insurance companies. These products tend to be annuities that are difficult to evaluate and are loaded with fees and expenses. Insurance companies expend significant money to market these products and highly incentivize (i.e. lavish vacations, expensive outings, and extravagant perks) their agents to sell certain lower quality, higher cost annuities. Are there well-constructed, low-cost annuities to be found? Yes, but these products are harder to find and they are not frequently sold. High-quality, low-cost annuities typically provide modest commissions since their profit margins are lower. These well-constructed annuities are harder to find because there is little or no advertising budget to market these products and the commissions associated to them do little to incentivize sales.

What we are left with is a high incentive to sell the inferior product. This is a conflict of interest created by insurance companies. Despite this conflict some investors believe the ethics of their annuity agent will protect them. These investors are of the impression that their financial advisors are legally obliged to act in their best interest. The sad truth is that it was perfectly legal for certain advisors (depending on their licensing and/ or

Continued on page 4

INVESTMENT PERFORMANCE: Average Annual Return Through 6/30/16

CORE FUNDS

	2ND QTR 16	1 YR.	3 YR.	5 YR.	10 YR.
PCA Large Cap Growth	-0.22%	0.07%	11.24%	9.82%	6.50%
PCA Large Cap Value	3.41%	-1.12%	9.26%	10.11%	N/A
S & P 500 Stock Index	2.31%	3.44%	11.11%	11.53%	6.82%
PCA Mid Cap Growth	2.79%	-1.27%	9.58%	10.32%	8.33%
PCA Mid Cap Value	3.95%	-0.28%	8.86%	10.30%	6.61%
PCA Small Cap	2.86%	-1.67%	5.54%	N/A	N/A
International Stock	0.23%	-7.03%	0.39%	-0.45%	0.65%
PCA Diversified Bond	2.27%	5.50%	3.81%	3.54%	4.60%
Conservative Bond	0.95%	0.76%	0.96%	1.02%	2.23%
Money Market	-0.04%	0.28%	-0.36%	-0.40%	0.66%

TARGET FUNDS

	2ND QTR 16	1 YR.	3 YR.	5 YR.
PCA TR2060	-1.85%	-3.16%	N/A	N/A
PCA TR2055	1.86%	-3.12%	5.77%	6.01%
PCA TR2050	1.86%	-3.12%	5.77%	6.01%
PCA TR2045	1.86%	-3.36%	5.57%	5.86%
PCA TR2040	1.99%	-3.35%	5.38%	5.68%
PCA TR2035	2.04%	-3.34%	5.06%	5.40%
PCA TR2030	2.01%	-3.16%	4.74%	5.08%
PCA TR2025	1.92%	-2.81%	4.29%	4.71%
PCA TR2020	1.77%	-1.77%	3.97%	4.39%
PCA TR2015	1.63%	-0.88%	3.70%	4.10%
PCA TR2010	1.56%	0.37%	3.50%	3.83%
PCA Harvester	1.48%	1.43%	3.23%	3.48%

Note: *Investment returns shown are net of investment manager, custodial and administrative fees. The above returns are unaudited.*

Annuities - Continued from page 3

credentialing) to direct individuals to annuities that provided them with the highest commission, perk, and/or giveaway, even if it was not an ideal investment for their client. A recent study by Financial Engines confirmed this mind-set. According to the study, 46% of Americans incorrectly believe their advisers were "legally required to put the best interests of their clients first when it comes to retirement."[2]

Investors evaluating annuities are at a significant disadvantage thanks to the legal and industry marketplace. Lower standards regarding investment advice and conflicts of interest have hamstrung even the best efforts to find dependable retirement income.

How can a novice investor avoid these traps?

Do it yourself – It is helpful to start the process by determining your end goal. Just what are you trying to accomplish through the purchase of an annuity? Focus on two things: what you want the annuity to guarantee and when you want the guarantee to start. Knowing this information will help you block the clutter in the sales pitch and marketing. Those working with a multi-carrier agent should compare annuities from multiple carriers with similar provisions. However, if your agent only works with a single carrier, contact others agents and compare provisions against the others. Finally, when comparing policies, make sure to compare the 'specimen policy.' This is a copy of the governing contract with all the important guarantees.

Do it for me – Find an impartial, fee-only, financial advisor who has in-depth experience in analyzing annuity contracts. This advisor will help you identify an optimal annuity for you, but should not sell it to you.

New Fiduciary Rule – Navigating the annuity market is about to get easier. On April 6, 2016 the U.S. Department of Labor introduced a new standard called the 'fiduciary rule.' Although compliance with the new rule is not mandated until April 10, 2017. Our next edition of the RPR will shed some light on this recent change and will elaborate on the benefits the 'fiduciary standard' offers to investors.

— Mark Melendez, *Client Services Manager*

1 LIMRA Secure Retirement Institute, U.S. Individual Annuities Survey
2 In Whose Best Interest? What Americans know and what they want when it comes to retirement investment advice. Financial Engines March 2016

Building Blocks - Continued from page 2

plan's fiduciary, engage in a comprehensive review of all management processes to make certain we maintain the fundamental strengths needed to foster good performance.

We believe the oversight processes presently employed by the PCA Retirement Plan represent the industry's best practices. However, even a fundamental strength can detract from performance relative to other similar plans. For instance, we believe that diversification is an essential element of good management. However, over the past two years diversified investments in non-U.S. investments, or inflation sensitive real assets, have detracted from performance. Does this mean that such diversification is a bad idea? We think not. We know from extensive modeling done by our investment consultant that diversification pays off over the long term. The challenge of long term investing is that it takes patience. One has to endure occasional years of painful under performance in order to reap the longer term rewards that comprehensive diversification delivers.

We would love to respond to any questions you may have regarding returns specific to individual retirement plan accounts. Please feel free to contact us at (800) 786-8765 to speak to one of our financial advisors. — Gary Campbell, *President*

BREXIT: - Continued from page 1

banking policy) identity. This lack of a common identity is why nationalism has become such a significant underlying issue among a number of EU nations.

While the news of Great Britain leaving the EU will contribute to a meaningful reduction in economic growth for this island nation, we believe its impact on U.S. growth will be quite modest. Britain is a great friend of the U.S. and could be counted on to represent the interests of the United States within the EU political power structure. That will unfortunately be lost.

A recent report from Moody's Analytics rightly points out that "recessions are always preceded by big declines in stock prices as investors sniff out weakening sales and profits at big publically traded companies." This does not necessarily mean that a recession is on the horizon since investors are a "fickle bunch and will sell for lots of reasons that may or may not be linked to what is going on in the broader economy." In this case, Moody's goes on to point out that none of the normal recession signals are indicating an impending recession. The bottom line is the U.S. economy still looks quite healthy despite the recent Brexit events. — Gary Campbell, *President*

Retirement **PLAN REVIEW** is a quarterly publication of *PCA Retirement & Benefits, Inc.*

1700 North Brown Road, Suite 106, Lawrenceville, GA 30043 • 678.825.1260 • 800.789.8765
Fax: 678.825.1261 • email: rbi@pcanet.org • Visit our web site: www.pcarbi.org •