

Impact of Market Volatility on Participant Exchange Behavior

Recent market events are drawing a lot of attention to how defined contribution participants are reacting. This report contains exchange data through November 2008, and although these findings are early, it will provide some insight on the initial actions that participants took, if any, as they weather the turbulent markets of 2008.

The Investment Company Institute (ICI) recently released a statement to the House Education and Labor committee on the impact that the current financial crisis is having on workers' retirement security. Their research¹ found that "plan investors do not overreact to market downturns or panic; they have demonstrated commitment to long-term savings, and that consistent 401(k) contributors have seen their accounts rebound after bear markets."

Key Insight

Recent Fidelity record kept data supports the ICI statement that the majority of DC participants² have, in fact, not overreacted to the current market downturn. Below are the key findings:

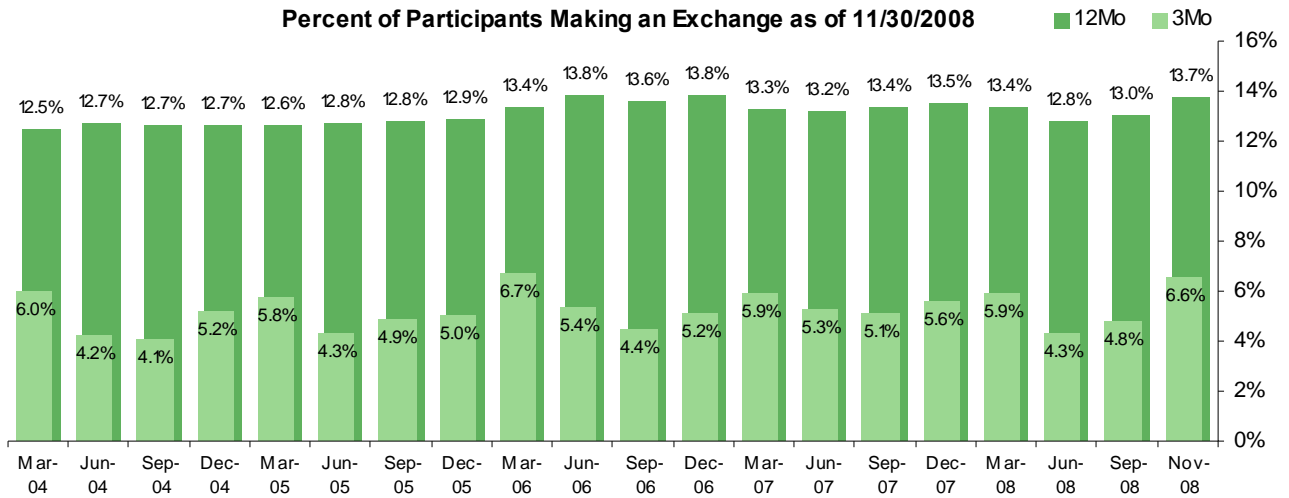
- ☑ From September 15, the day after Lehman Brothers filed for bankruptcy protection, through October 10, the net flow out of equities was significant. This migration peaked on October 10, and from that point through November 30, the shift out of equities was less dramatic.
- ☑ Of the participants on record as of September 30, 2.5% made an exchange during September, 4.0% made an exchange during October, and 1.8% made an exchange during November.
- ☑ Overall, only 6.6% of participants made an exchange in the three month period ending November 30.
- ☑ 98% of participants who contributed in Q2 2008 continued to contribute to their DC plan in Q3 2008 even though market conditions continued to be volatile.
- ☑ Only a handful of the 19,300 plans for which Fidelity provides recordkeeping services have suspended or terminated their employer contributions.

¹The Impact of The Financial Crisis on Workers' Retirement Security - Hearing Before the Education and Labor Committee States House of Representatives - October 21, 2008
http://www.ici.org/home/08_house_ret_security_stmt.html

²Participants equates to all accounts with greater than a \$0 balance. Active participants means actively employed (i.e. not terminated).

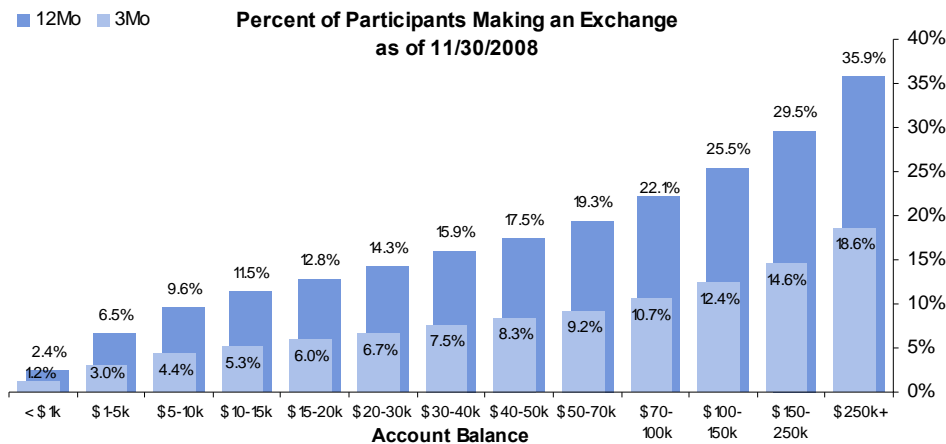
Exchanges

Although the number of participants making exchanges in November 2008 was higher than recent quarters, it still represents a relatively small number of Fidelity's record kept participant base. The likelihood of a participant to make an exchange is highly correlated with account balance (i.e. the higher the balance, the more at stake, and the greater the likely level of participant engagement).



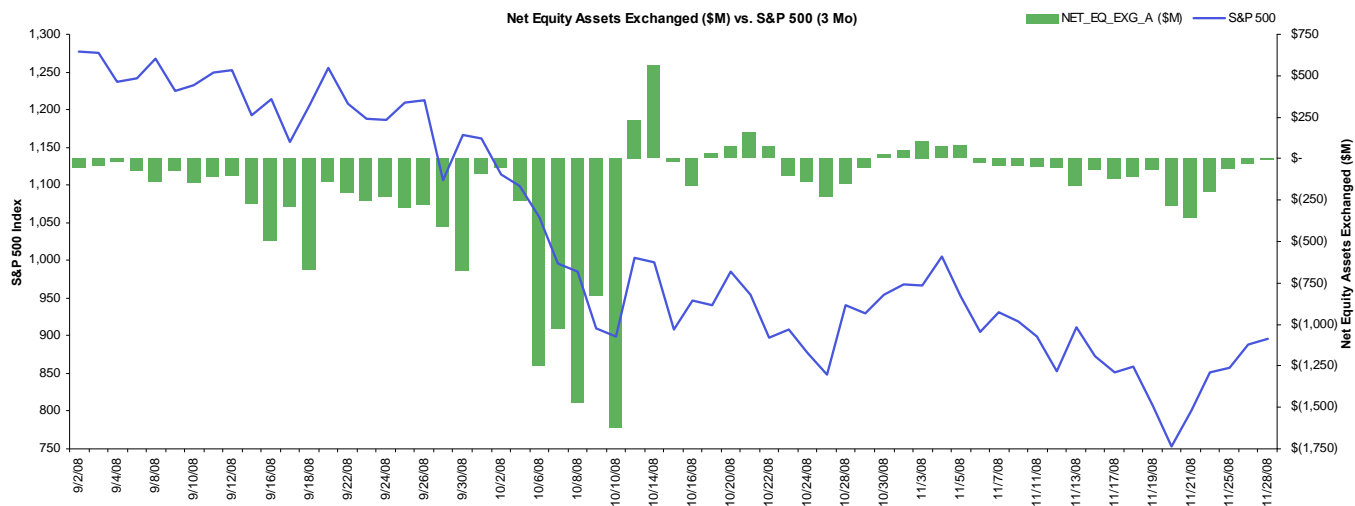
Did You Know?

- ☑ The chart above indicates that, overall, only 6.6% of participants made exchanges from September 2008 through November 2008—up from 4.8% in the 3 month period ending September 2008.
- ☑ Of the participants on record as of September 30, 2008, 2.5% made an exchange during September, 4.0% made an exchange during October, and 1.8% made an exchange during November. (Note that the market was open for 21, 23, and 18.5 days in September, October, and November respectively.)
- ☑ Although the percent of participants making exchanges increased over the past three months, the 3-month period with the highest exchange activity (11.0%) occurred in the first quarter of 2000 during the peak of the tech bubble.
- ☑ Between November 2007 and November 2008, 35.9% of participants with a balance greater than \$250k made an exchange, but only 6.5% of participants with a balance between \$1k and \$5k made an exchange, as shown in the chart below.



Net Equity Exchanges

The chart below highlights the net equity exchange activity from September 2008 through November 2008. The green bars depict the net money exchanged into or out of equities, which include domestic, international, and the equity portion of blended investment options (excluding company stock). The blue line represents the Standard & Poor's 500 (S&P 500) daily closing price.



What's happening?

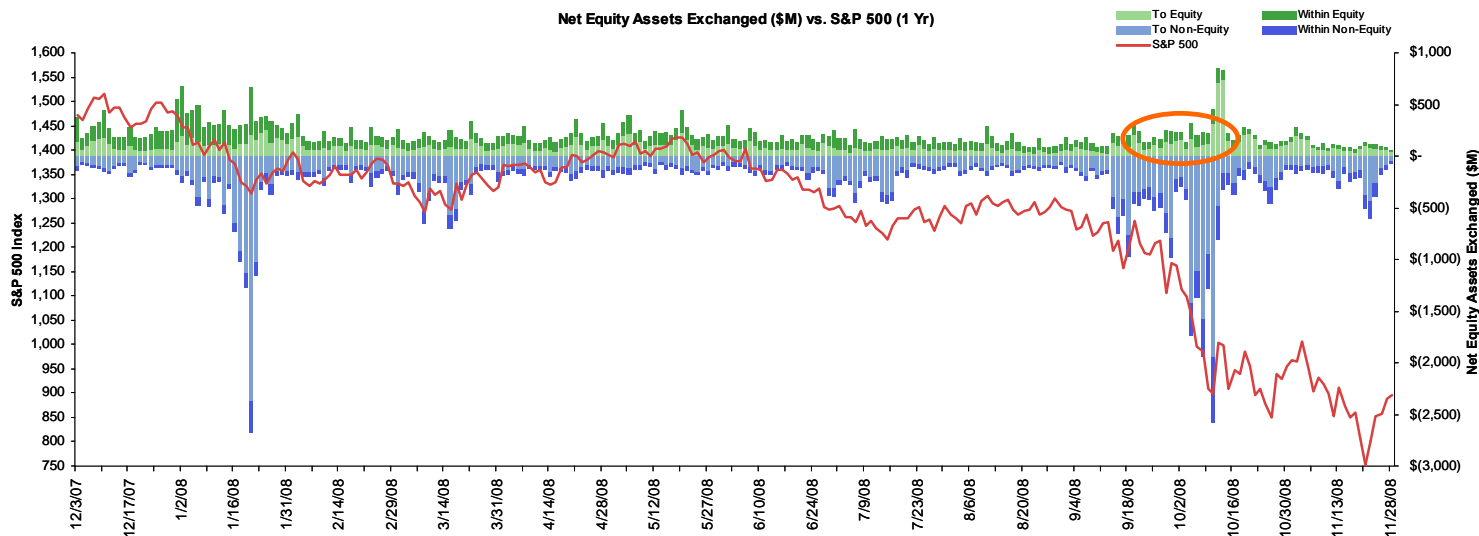
The data above highlights that the net exchange flow out of equities was significant between September 15, 2008, which was the day after Lehman Brothers filed for bankruptcy protection, and October 10, 2008.

- On October 9, the Dow Jones Industrial Average (DJIA) fell below 9,000 for the first time in five years, driven primarily by financial fears. The migration out of equities peaked the next day, and from that date through November 30, the shift out of equities was less dramatic. This suggests that some DC participants that made asset allocation changes may have decided to wait out the economic crisis.
- In the two days following October 10, some participants apparently felt that a bottom had been reached because net exchanges flowed from non-equities back into equities for the first time in almost three months.

Movement between Asset Classes

Underlying the general market-driven trends behind net exchanges into and out of equities, there is considerable movement taking place within and across asset classes. Looking at the chart below:

- ☑ The blue highlights that most of the exchange volume involving non-equities involves movement from equities to non-equities, rather than between non-equities.
- ☑ While the chart on page three depicts the overall net equity flows, the orange circle in the chart below highlights that even when the market dropped significantly in early and mid-October, there was still movement into equities.



Conclusion

Although this Building Futures snapshot contains early results from the current market downturn, our initial findings support the ICI testimony to the House Education and Labor committee that the majority of DC participants did not initially overreact to the current economic situation in terms of exchange volumes. Fidelity will continue to analyze the impact that the recent market volatility is having on DC participant behavior, and will provide you with more insight as the data becomes available.

As a plan sponsor, you may be wondering what steps you can take to help your employees manage through this difficult time. Below are some high-level recommendations that you may want to consider:

- ☑ **Reinforce for employees the importance of contributing to the plan.** For many employees their workplace savings plan is their primary savings vehicle, without it, many individuals would not have the discipline to automatically save a percentage of each pay check.
- ☑ **Continue to evaluate plan design strategies to create better outcomes.** For example, this might be a good time to consider prescriptive plan design options such as auto-enrollment or auto annual increase.
- ☑ **Review your fund line-up.** Evaluate your fund line-up to ensure that it offers key attributes such as broad market coverage, high diversification potential, sufficient choice, and a simple design.
- ☑ **Work with your service provider to help put employees on the path to financial wellness** by improving holistic employee guidance. Encourage all employees to have a financial plan. People have many financial needs, and many will require some help to balance those needs. It can be hard for individuals to focus on what to do 10, 20, and 30 years in the future - it's easier to focus on what to do next. Having a plan helps to lay the groundwork.

For plan sponsor use only.

Fidelity Investments recordkept data includes an analysis of over 19,300 corporate and tax exempt DC plans and over 14.5 million recordkept participants. Notes: All data in the Report exclude plans record kept for Fidelity Investments' own employees. This report excludes plans with 0 participants, Phantom Non Qual Plans, & TEM Pooled Plans). Participants must have >\$0 Real Assets.

Keep in mind that investing involves risk. The value of your investment will fluctuate over time and you may gain or lose money.

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