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JOURNAL REPORTS: FUNDS & ETFS

CITs, the Not-Exactly Mutual Funds, Are on Pace to Hit $3 Trillion

Collective investment trusts are increasingly offered in 401(k) plans eager to lower costs

By Bailey McCann

Collective investment trusts, the increasingly popular retirement-plan investments that seem like mutual funds but aren't, are ballooning.

Data from financial-services company ALPS shows that assets in collective investment trusts, or CITs, could surpass the $3 trillion mark by the end of 2018, up from $1.9 trillion at the end of 2015.

Much of this is thanks to 401(k) plan sponsors adding CITs to the menus of investment choices that they offer their plan participants. The 2018 Defined Contribution Trends Survey from investment consultant Callan shows that such use of trusts in 401(k)s has jumped 48% since 2011, while the use of mutual funds has decreased.

Lower costs

When CITs are added to retirement plans, plan participants have new ways to expand their nest eggs. The trusts are sponsored by banks and trust companies, and so are primarily overseen by banking regulators. Thus, even though the trusts tend to mirror mutual funds in the types of assets and strategies they use, they have lower management and distribution costs because they aren't subject to Securities and Exchange Commission rules.

CITs are increasingly available through financial advisers as well. John Alshefski, senior vice president and managing director of Investment manager services at money manager SEI, says he's hearing from more advisers that are interested in offering their strategies in a collective trust.

"CITs have always been an option for the retirement market, but once a manager sees that they can offer a CIT cost-effectively, it's a no-brainer," he says. Many advisers are offering their investment strategies as a mutual fund and a CIT to give plan sponsors more options.

Historically, CITs have been used as a way of making active management available to investors at a lower cost. But Charlie Morrison, head of asset management at Fidelity Investments, says his company has taken steps to offer CITs with a wider range of investments.

"Some of the larger plan providers we work with said they were interested in building out their passive solutions, so we have helped with that," he says. "The bulk of our CIT offerings have been the result of client demand." Coupled with the growth of ETFs, plan sponsors can now put together a traditional 60/40 stock/bond portfolio in a CIT, shaving another percentage point or two off retirement-plan expenses.

The biggest retirement plans have always been able to offer participants the ability to customize their accounts, largely because of their size. But money-management firms are more willing to offer customization to smaller plans as overall costs to manage them have come down.

Todd Lacey, head of the retirement group at Stadion Money Management in Watkinsville, Ga., says that using a CIT structure, Stadion can create customized accounts for small and midsize plans using all low-cost products in a CIT wrapper. His company's StoryLine retirement product, for example, has five CITs made up of ETFs. Based on the risk profile of a given plan, Stadion can create customized retirement offerings by using the five CITs.

Innovation opportunity

"We've been operating on this one-size-fits-all model with 401(k)s and target-dates where we aren't looking at factors like when people start participating," Mr. Lacey says. "There's a recognition in the industry that this isn't great," he adds, and "there is an opportunity with CITs to jump-start some of that innovation."

One drawback of CITs, meanwhile, has been their lack of a trading symbol, making it difficult for 401(k) participants to track how the trusts are performing and compare them with other investments. Some companies that offer CITs, though, now offer mutual funds with identical asset mixes and strategies as the CITs they offer. So, CIT investors can use the mutual fund as a proxy for the CIT performance, because both are using the same strategy.

CIT providers understand that the market expects daily information, says Shelby George, senior vice president of advisory services at investment firm Manning & Napier.

"What we've seen with [CITs] is a lot of innovation behind the scenes in terms of improving the timeliness of reporting, getting more performance information out there, in addition to expanding the strategies that are available in a CIT," she says. Ms. George adds that she wouldn't be surprised to see a third party step in and start offering CIT research and ratings, similar to what Morningstar does for mutual funds.

Fiduciary standard

The growth of CITs in recent years also may be getting help from the pressure on retirement plans and financial professionals giving retirement advice to act as fiduciaries—a legal requirement to act in the client's interest. That responsibility adds to costs, advisers say. CITs, by contrast, because they are overseen by banking regulators, are already held to a fiduciary standard, and the cost and fees are already built in.

Francisco Negron, head of client services at T. Rowe Price, which maintains some of the largest CITs, sees the size of the retirement industry as a tailwind for CITs.

As retirement-plan assets grow, he says, "sponsors are more focused on cost and standards than ever."

Ms. McCann is a writer in New York.

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