

# TECHNOLOGY DEMOCRATIZES CUSTOMIZATION

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**Technology democratizes customization.** This is a notion that I have ruminated on for a long while, and I have begun to hear it from others of late. I am heartened because it resonates so deeply with Milestone Group's objectives, culture and strategy, as well my own. Hence, it is the point of embarkation for this article.

'Democratization' is defined by Oxford as "the action of making something accessible to everyone."

In our industry, technology democratizes customized investment solutions: it makes them accessible for everyone. There are many manifestations of customized investment solutions<sup>1</sup>, but I am focused on a particular one that builds on the concepts and structure of target date funds<sup>2</sup>, conceptually seizing the benefit associated with customization, while exploiting some of the design and structural concepts of target date funds for the sake of efficiency.

As is well known, a target date fund (TDF) is an investment structure that is implemented with an array of underlying investments that are deliberately selected to create a well-diversified portfolio. The weightings of those underlying investments are strategically determined and systematically adjusted over time to maintain an asset allocation that is appropriate in the context of that investor's expected retirement date, which serves as the determinant of the investor's risk profile. This progressive shift in the asset allocation is known as the 'glidepath.' Target date funds are deployed as a series, usually comprised of ten funds - or 'vintages' - offered in five-year increments, each designated by their respective target dates, and each using the same 'glidepath' but each at different points along the glidepath reflecting that vintage's number of years from its target date, the expected retirement date.

The key point for the purpose of this discussion is that each vintage is customized in response to the risk profile of a cohort of investors. But that customization reflects only one factor: the target date/retirement date. While that is indeed customization, it is a very limited/narrow expression of customization.

However, this limitation is not from a lack of imagination. Work has been done to design investment products that would substantially improve the 'fit' of solutions to the investors they serve. Product design has been done with consideration for additional factors such as whether the investor: 1) has other retirement savings/benefits, 2) owns their home, 3) has a spouse or partner with retirement or other savings; as well as 4) the impact of Social Security or other government retirement plans; and 5) the investor's 'need,' which is often expressed as 'expected spending' in retirement. Consideration of these factors has the capacity to substantially improve the 'fit' of the customized investment solution.



But this more specifically customized fit would result in more complex investment products. If a next generation product design were to begin with the current form of a target date fund series comprised of ten vintages, with each of those vintages further specified with five additional factors, each of which had five possible selections, that would render 25 cohorts<sup>3</sup> in place of each original vintage. Each cohort would have a glidepath that was customized to its particular risk/objectives profile, thus providing an investment strategy – and outcome – more finely tailored to that cohort's profile.

But, if each TDF vintage was replaced by 25 cohorts, the original series of ten vintages would be replaced by 250 cohorts. Therein lies the challenge.

If setting up and maintaining the asset allocation for 250 cohorts sounds ominous, it is if you are relying on 'traditional' investment technology and operations.

In fact, if you ask an operations executive about the feasibility of operating a TDF series with 250 cohorts, I am confident that executive would tell you: "It is absurd."

With 'traditional' investment technology and operations, servicing the current state of complexity is an extremely challenging process; it is fraught with operating risk and therefore significant financial risk. From an operations perspective, to move to an even more complex structure would be perilous. In many investment organizations, the current state for managing these complex investment structures principally relies on spreadsheets and manual operations and controls<sup>4</sup>. This obsolete 'state of the art' precludes product innovation and the delivery of customized solutions at scale.

**Paradoxically**, advanced technology that is purpose-built to efficiently and securely operate the complex investment structures such as I've described above is available and in production at massive scale now. The democratization of customized investment solutions, and the efficient and secure delivery of the improved outcomes they offer, is absolutely feasible now.

Isn't it incumbent upon those of us in positions to advance the state of this art, to do so?

***There is a better way. Let us show you.***



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<sup>1</sup> Including Institutional Managed Account Platforms, Robo Advisors and various smartphone 'Apps'.

<sup>2</sup> Custom Open Architecture Target Date Funds are a more extensive expression of this approach, but for this essay, Target Date Funds in general represent the essential concept.

<sup>3</sup> 5<sup>2</sup> (i.e. five squared)

<sup>4</sup> See Milestone Group's Asset Allocation Technology Survey 2020, <https://www.milestonegroup.com/whitepapers-resources/survey-findings-and-conclusions-asset-allocation-technology>