

## TIAA-CREF: Not for Everyone

**Shirley M. Mueller**

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At one time I was an associate professor at Indiana University. While an academic, I was enrolled in a retirement option the school offered, Teachers Insurance Annuity Association-College Retirement Equities Fund, or TIAA-CREF. It was and is considered a low cost plan that provides financial services for those in the academic, medical, cultural, and research fields. In fact, they use their client base as an important part of their promotional marketing material, "serving those who serve others." Lately, however, I've been wrestling with how well I'm been served. My conclusion: not well enough.

TIAA (the bond portion of TIAA CREF) was founded by Andrew Carnegie in 1918. Initially it offered annuities and pensions for university professors. As institutions of higher learning initiated pension programs, they began using TIAA. After World War II, however, inflation required that the company also invest in stocks. Therefore in 1952, it formed the stock portion of the company, CREF. Since then the business has grown enormously because of the increase in employees at nonprofits, state government and educational institutions.

Further, the employers of these employees have funded their pension, unlike so many in the private sector. This means that TIAA-CREF now runs the retirement fund of millions of people and is the one of the nations' largest asset management companies. In that position, it has questioned corporate governance and executive compensation on a number of occasions in an effort to protect its participants. Now, however, the company seems to be taking a different turn, one that suggests it is less interested in serving its clients than itself. This is why.

Though TIAA CREF is low cost compared to many options, its charges are more than others in the low cost category. For example, the CREF money market expense ratio is 0.47, almost one-half of a percent. Compare this to Vanguard's Money Market Reserves (VMMXX) with an expense ratio of 0.28%. The return of each reflects the financial outlay from the client to the fund. TIAA-CREF's yield as of 9/22/09 was .01%. Vanguard was 21 times that at 0.21%, as of the same date.

This relationship of higher expense and lower returns doesn't stop at money markets. It permeates stock funds as well. Several studies have shown that there is a direct inverse correlation between expense and return.

### **Lower Expense Ratio Mutual Funds Outperform**

<b>Expense Ratio (%)*</b>	<b>Average Annual Pre-Tax Return (%)</b>
< 0.65 (low expense)	12.7 (more return)
1.07	11.1
1.60 (high expense)	10.0 (less return)

*Source: Stefan Sharkansy, "Risk Without Reward," July 2002, PersonalFunds.com; \*Data for larger capitalization US mutual funds*

Since TIAA-CREF stock funds are generally higher in expense than other low cost options (just like the money fund), studies like the above have important implications to the TIAA-CREF client. In general, a lower expense ratio means higher returns. For example, if an investor puts \$10,000.00 in a mutual fund that has an expense ratio of 1.5% and the return is 10%, he has \$281,000 in 40 years. However, if the expense ratio is 0.2%, the investor has \$421,000 at the end of the same time frame. This difference of \$140,000 is what the higher expense mutual fund puts into its pocket instead of the

investor.

The customers of TIAA-CREF, teachers and others in the caring industries, are by and large investors who think more about their jobs than their money. This means they are passive and the expense or performance of TIAA-CREF is not something they critically analyze.

There are others, however, who not only understand that “you can make money while you sleep,” but also want to make it work maximally for them. For these individuals, a re-examination of TIAA-CREF expense and performance compared to other low cost options could lead to an advantageous switch, one that has the potential to enhance their returns, even when they aren’t working.