Voya Target Retirement Funds

The Target Date Choice to Help Keep Retirement Goals on Track

Strategy overview

These portfolios are only offered as an investment option within variable products and retirement programs.

Key takeaways

- Stocks and bonds declined in tandem during the third quarter. Year to date, stocks have generally delivered solid returns, but the sharp, steady rise in interest rates has U.S. bonds poised to deliver their third consecutive year of negative returns.
- In the months ahead, we expect U.S. economic growth to slow, and inflation to continue decelerating. This environment should benefit bonds. Despite the anticipated slowdown, U.S. macro fundamental factors still look better than most of the developed world, and we favor U.S. assets as a result.
- The Funds posted negative absolute and relative returns for the period.

Market review

Stocks and bonds declined in tandem during the third quarter, reminiscent of 2022 when both asset classes sold off significantly. Large cap stocks outperformed smaller United States and international developed equities, but slightly lagged emerging markets (EM). Within the S&P 500, the energy sector performed best as oil prices surged higher. Communications was the only other sector to deliver gains and has posted the best performance of the year. Other sectors declined with utilities, real estate and consumer staples leading the way lower. Europe was the primary drag on international equities, as investors priced in the prospect of additional central bank rate increases. India posted gains in the period and China's stock market, the worst performing major country this year, stabilized and helped EM hold up better than other asset classes.

Rising rates continue to weigh on bonds. As a consequence of the jump in rates, long-duration U.S. Treasuries were the worst performing major asset class in the quarter and are on pace to deliver negative returns for the third consecutive calendar year, which has not occurred since 1928. Core U.S. and international developed market bonds were down a similar amount while EM debt fell, but to a lesser degree. Yet, high yield (HY) delivered positive returns due to relatively short duration, higher starting yields and spreads that were little changed.

Outlook

Not only has the U.S. avoided a widely anticipated recession amid a historically aggressive increase in interest rates, but the economy has been running well above potential growth. The economy proved to be less interest rate sensitive and more resilient than expected. Consumers and corporations locked in rates near historic lows. So, there has been limited diffusion through the lending channel, which is how monetary policy influences economic activity. We think this is set to change as higher rates seep into the system. There have also been non-monetary offsets that are likely to fade, most notably supportive government spending. The Inflation Reduction Act's open-ended 25% tax credit on semi-conductor manufacturing sparked a boom in construction that is unlikely to be repeated or maintained.

All eyes remain on inflation. Core Personal Consumption Expenditures, a key U.S. Federal Reserve gauge of consumer prices, was up 3.9% year over year in August, continuing its deceleration from last year's 5.6% cycle highs. Most of the drop has come from the supply side, but we believe tighter monetary policy and lessening fiscal support will weigh on the demand side in the period ahead. While housing costs remain elevated with home affordability now below record lows previously set in 2006, a sharp reduction in rents, which has a lagged effect on most price indexes, signals a further inflation dip. Oil prices have climbed, mainly from Saudi-Russian strategies to curtail supply, pushing headline inflation up. Igniting of the Israel-Hamas conflict has the potential for significant further Middle East supply disruption. Nonetheless, the rise is not yet alarming, as it has not translated into higher gas prices given a big compression in refining margins and is manageable relative to disposable income growth, which has been strong. More importantly for inflation is employment.

The labor market is cooling but not breaking. With the unemployment rate at 3.8%, labor markets have been strong, but job openings and quits have been trending down since March, suggesting a softening in the employment picture. While wages are declining, they are growing above inflation and are historically high. This suggests only modest weakening in consumer buying power, but we think there is more to come. Recent labor union activities have garnered attention, but they represent only about 10% of the workforce.[1] It typically takes 18–24 months after the beginning of a Fed tightening cycle for joblessness to increase. We just moved into this range.

U.S. assets remain attractive. Despite some headwinds, the U.S. continues to offer a robust macroeconomic picture compared to other developed nations, chiefly Europe. While we maintain a neutral stance on equities, we believe U.S. large cap stocks are best positioned to grind higher due to their more durable earnings streams than companies of other sizes or regions. We think earnings for S&P 500 companies have troughed and are set to enter a new phase of growth. However, earnings estimates are aggressive given what we believe will be slower economic growth in the next few quarters and we believe margins will somewhat revert alongside tighter financial conditions. This keeps us neutral overall with a more defensive tilt.

Small caps are cheap but vulnerable. The main concerns surrounding small caps are their exposure to rising rates given a higher proportion of debt needing to be rolled over in the short term and weaker interest coverage ratios compared to that of their large cap peers. Small cap revenues have historically had nearly two times the beta to nominal gross domestic product (GDP) compared to large caps, so any slowing in growth will likely impact this cohort more. However, the beta to service sectors — where most of the future incremental slowdown is likely to occur — appears lower than the headline GDP. Small caps tend to outperform during periods of expanding manufacturing activity; until we gain confidence that it has bottomed, we remain neutral.

We are cautious on Europe. European stocks ended last year and started this year with a bang, but we think they got ahead of themselves as they are further behind the curve in their inflation fight, continue to contend with issues of the eurozone structure — one monetary policy for the zone and different fiscal policies at the country level exemplified by Italy and France recently announcing generous new spending bills while the European Central Bank (ECB) struggles to withdraw stimulus. Europe's slowing macro momentum — illustrated by services and manufacturing Purchasing Managers' Index (PMI) indicating contracting activity — should take a bite out of corporate profits.

China continues to disappoint. There was little if any reopening burst of activity and economic growth is slowing with retail sales, industrial production and fixed investment all coming in less than expected. Exports have plunged, due in part to U.S. companies' efforts to re-shore or move off-shored manufacturing elsewhere. Furthermore, China's real estate sector, their main growth engine, is in freefall with multiple large property developers teetering on the edge of default. China continues to make progress on the technological front (e.g., semi-conductor chips, electric vehicles, aerospace, etc.), valuations are at a deep cross-sectional discount, and the government has signaled they may intervene with a stabilization fund to buy stocks, but the outlook is thorny. Although other EM countries have better near-term prospects, it is difficult to be bullish on EM equities overall when China is dragging.

U.S. dollar (USD) should hold strong but be less of a headwind to emerging markets. Technical factors suggest the modest retreat could continue in the near-term, but the USD likely maintains an edge over a broad basket of currencies thanks to relative growth and real rate differentials. Recent geopolitical shocks and subsequent flights to the USD validate its safe-haven status in times of heightened stress and uncertainty.

Bonds look increasingly attractive. The rapid rise in bond yields and the Fed's commitment to reducing growth below trend should drive yields lower as the economy weakens. With real 10-year yields pushing towards 2.5% and investment grade (IG) corporate bonds yielding more than the earnings yield on large U.S. stocks, fixed income investments have become more appealing. Furthermore, there are few signs of stress among large corporate issuers with most treasurers front-loading financing activities when rates were low.

Diversification is not dead. Through the third quarter, stocks and bonds have declined in tandem, reminiscent of 2022 when both asset classes sold off significantly. While this environment is causing some investors to question the merits of a balanced portfolio, we believe bonds will help diversify stock allocations as we return to more normal rate and inflation environments.

Positioning

At the beginning of the period, Funds held a neutral equity — fixed income split on the front- and back-ends, and relative to their strategic allocation benchmarks, modest tactical equity underweights and fixed income overweights in the belly. On average across the Funds, sub-asset class allocations were overweight to U.S. large cap equities and duration, and underweight in international developed equites, EM equities and HY.

Toward the end of August, portfolio managers (PMs) added to U.S. TIPs by reducing short term bonds in the near-dated vintages. The backup in real yields presented an opportunity to close TIPS underweights and assume a more neutral position.

Portfolios continue to favor U.S. assets and maintain modestly defensive posture overall with a preference for U.S. large cap equities and core IG fixed income.

Performance

The Voya Target Retirement Fund's primary performance objective is to outperform its strategic allocation composite benchmark over the long-term through tactical asset allocation, i.e., deviating from the composite benchmark over the short and medium-term and active manager selection. The benchmark return is the weighted average return of indices that represent asset classes included in the strategic allocation benchmark. Index returns are gross of all fees. The Funds are generally rebalanced monthly and the strategic asset allocations are updated annually to reflect changes to our capital market assumptions. In the second quarter of 2023, Funds' relative performance trailed their strategic allocation benchmarks. Tactical asset allocation and manager selection detracted.

Tactical asset allocation had a negative impact on performance during the period. Funds' overweights to U.S. large cap and underweights in international developed equites were the main contributors. While the performance difference between the two asset classes was small during the quarter, YTD the gap is significant. Larger U.S. companies continue to perform better than other regions and sizes due to their more durable earnings streams coming from their superior ability to passthrough higher prices to customers and cut costs. Europe struggled during the period. Declining activity, lingering inflation and the realization that the ECB probably likely needs to hike rates further weighed on stocks. The biggest headwind during the period came from the Funds' moderately long duration postures. Better-than-expected economic growth, concerns over widening fiscal deficits and an anticipation of further U.S. government debt issuance contributed to a sizable rise in interest rates and lower prices for longer maturity bonds.

Underlying managers were a headwind during the period. Strategies that contributed most to excess returns in the quarter were Voya Intermediate Bond, iShares Core S&P Mid-Cap ETF and Vanguard Long-Term Treasury ETF. The biggest detractors in the quarter were Voya Multi-Manager International Equity and Vanguard FTSE Developed Markets ETF.

[1] Source: BLS; Union Members - 2022 (bls.gov).

Principal Risks: There is no guarantee that any investment option will achieve its stated objective. Principal value fluctuates and there is no guarantee of value at any time, including the target date. The target date is the approximate date when investors plan to start withdrawing their money. When their target date is achieved they may have more or less than the original amount invested. For each target-date portfolio, until the day prior to its target date, the Trust will seek to provide total return consistent with an asset allocation targeted at retirement in approximately each Trust's designated target year. On the target date, the Trust's investment objective will be to seek to provide a combination of total return and stability of principal consistent with an asset allocation targeted to retirement.

Stocks are more volatile than bonds, and trusts with a higher concentration of stocks are more likely to experience greater fluctuations in value than portfolios with a higher concentration in bonds. Foreign stocks and small and midcap stocks may be more volatile than large cap stocks. Investing in bonds also entails credit risk and interest rate risk. Generally, investors with longer timeframes can consider assuming more risk in their investment portfolios. The Voya Target Solution Trusts are actively managed and the asset allocation adjusted over time. The trusts may merge with or change to other trusts over time. Refer to the prospectus for more information about the specific risks of investing in the various assets classes included in the Voya Target Solution Trusts.

As with any portfolio, you could lose money on your investment in the Voya Target Solution Trust. Although asset allocation seeks to optimize returns given various levels of risk tolerance, you still may lose money and experience volatility. Market and asset class performance may differ in the future from historical performance and the assumptions used to form the asset allocations for the Voya Target Solution Trust. There is risk that you could achieve better returns in an underlying portfolio or other portfolios representing a single asset class than in the Voya Target Solution Trust.

Important factors to consider when planning for retirement include your expected expenses, sources of income and available assets. Before investing in the Voya Target Solution Trust, weigh your objectives, time horizon and risk tolerance. The Voya Target Solutions Trust invests in many underlying portfolios, which are exposed to the risks of different areas of the market. The higher a portfolio's allocation to stocks the greater the portfolio's overall risk. Diversification cannot assure a profit or protect against loss in a declining market.

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The Fund discussed may be available to you as part of your employer sponsored retirement plan. There may be additional plan level fees resulting in personal performance to vary from stated performance. Please call your benefits office for more information.

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