Sibson Consulting | Segal Marco Advisors

Prism

A QUARTERLY REVIEW OF FUNDED STATUS

Strategic HR Consulting | Investment Solutions | First Quarter 2019 Pension Plan Experience

Pension Plan Funded Status Increases Due to Positive Equity Returns in Q1 2019

During the first quarter of 2019 (Q1), the funded status of the model pension plan examined in each issue of *Prism* rose by 2 percentage points, to 89 percent. (See Graph 1.) This is a result of a 9 percent asset gain and a 6 percent increase in liabilities, as shown in Graph 3 on the next page.

About *Prism*

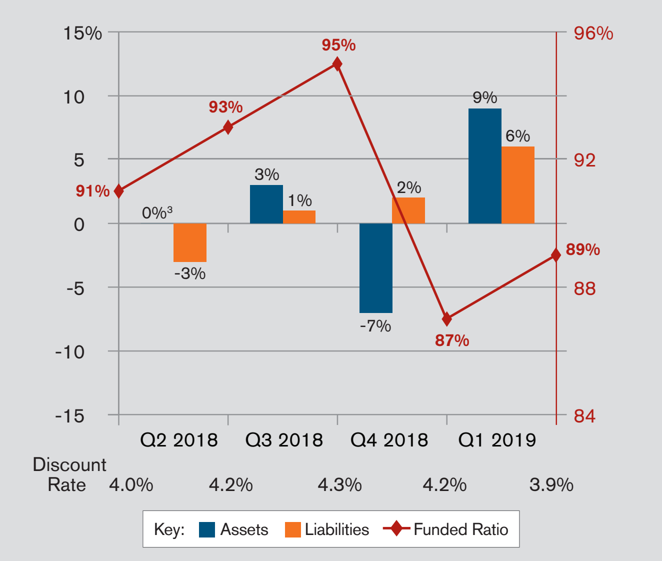
Prism examines the effect of changes in the assets and liabilities of a model pension plan on its funded ratio over the four most recent quarters, viewing such changes through a marked-to-market lens. The primary focus is to understand the combined impact of asset movement and interest rate shifts on perhaps the most important financial metric to plan sponsors: the plan's funded status.

Aspects of Investment Performance

These aspects of investment performance contributed to the model plan's 9 percent gain in asset value in Q1:

- Equities rebounded strongly during Q1 following the very poor returns during Q4 of last year, as shown in Graph 2. Global stocks had double-digit returns during the quarter for the first time in seven years. Although both developed international stocks and emerging market stocks were up substantially for the quarter (with the former edging out the latter), they finished behind U.S. stocks, which returned 14 percent. That was the best quarter for U.S. stocks since 2009. Among U.S. stocks, small cap just barely outperformed large cap for the quarter while growth topped value for the 8th time in the last nine quarters.
- Fixed-income returns were positive both domestically and internationally. The Federal Reserve Board's Federal Open Market Committee declined to increase the Federal Funds Rate at both of their first quarter meetings, maintaining the target range at 2.25 to 2.50 percent. The 10-year U.S. Treasury yield fell substantially during March and ended the quarter at 2.4 percent.

Graph 1: Change in Assets,[1] Liabilities and Funded Ratio[2]

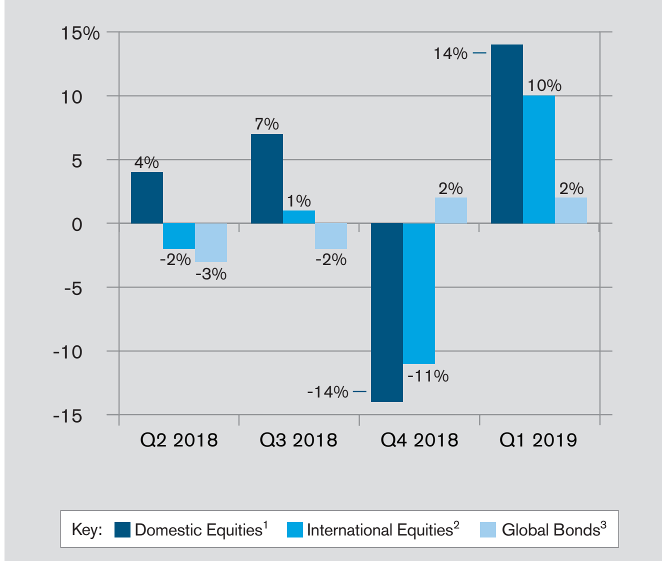


[1] The model plan's portfolio has a simple, passively invested asset allocation of 45 percent to domestic equities, 15 percent to international equities and 40 percent to global bonds.

[2] This is the ratio of a defined benefit (DB) plan's assets to accrued liabilities. The funded ratio data in the graph is the ratio on the last day of each quarter. The funded percentage for the model DB plan was reset as of January 1, 2018, to reflect the average actual funded percentage of large pension plans.

[3] In Q2 2018, assets increased 0.05 percent.

Graph 2: Investment Performance



[1] Russell 3000

[2] Morgan Stanley Capital International All Country World Index Ex-U.S. (MSCI ACWI Ex-U.S.)

[3] Citigroup World Government Bond Index (WGBI) Unhedged, which includes U.S. and international bonds

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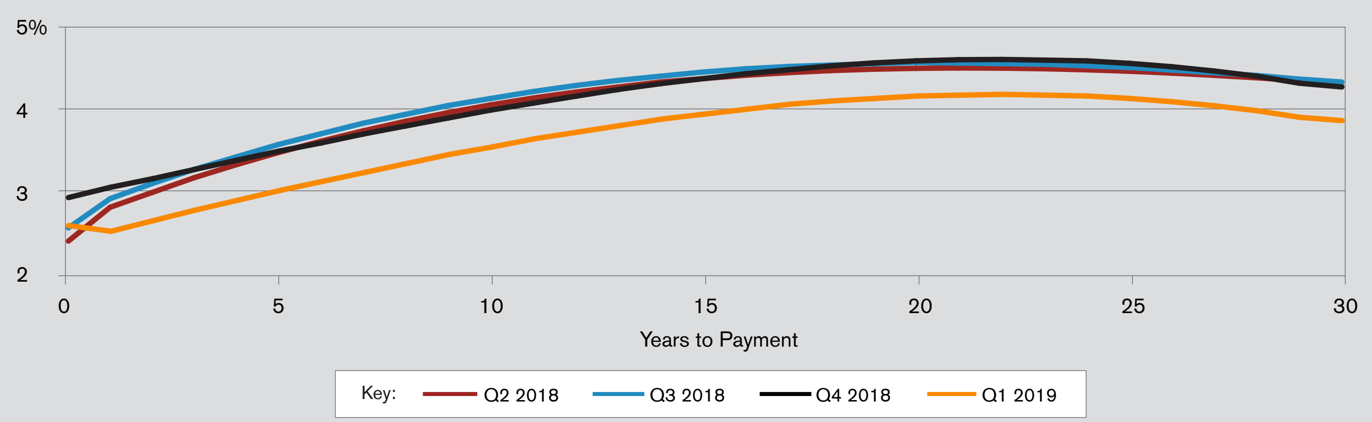
Changes in the Yield Curve

High-quality corporate yields fell during Q1, declining by 35 basis points* — the net result of a 25 basis-point decrease in U.S. nominal Treasury yields and a 10 basis-point decrease in credit spreads. During the quarter, yields decreased sharply, resulting in one of the flatter curves in recent memory, as illustrated by the above-median curves shown in Graph 3. The decline in yield-curve level resulted in a 6 percent increase in the model pension plan's liability.

Any change in the shape of the yield curve could have a dissimilar impact on liabilities for plans with different maturities. (For background on yield curves, read our online primer.)

Graph 3: Changes in the Yield Curve[1]



[1] This curve reflects the average yield, at each duration, for corporate bonds rated AA that have yields above the median for that duration.

Important: Examine Your Own DB Plan's Experience

Plan sponsors should examine changes in their own DB plans' assets, liabilities and funded ratios from the vantage point of both accounting and funding metrics.** Segal Marco Advisors and Sibson Consulting can help employers project their DB plans' funded ratios through:

- **Deterministic Modeling**, which projects results under a specific set of assumptions but does not offer insight into the likelihood of these outcomes; and
- **Stochastic Asset-Liability Modeling (ALM)**, which offers a more complete view of the range of a plan's possible future statuses and can act as an early warning sign of potential challenges through a long-term time horizon.

* As a reminder, 10 basis points (bps) equals 0.1 percent.
** Individual plan results will differ from this model for a host of reasons, including different funded positions, liability duration and contribution patterns.

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For more information about how ALM can help you manage your plan, contact your Segal Marco Advisors investment consultant or your Sibson retirement consultant.

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