Prism

Third Quarter 2021 Pension Plan Experience

Pension Plan Funded Status Drops Slightly as Assets Dip

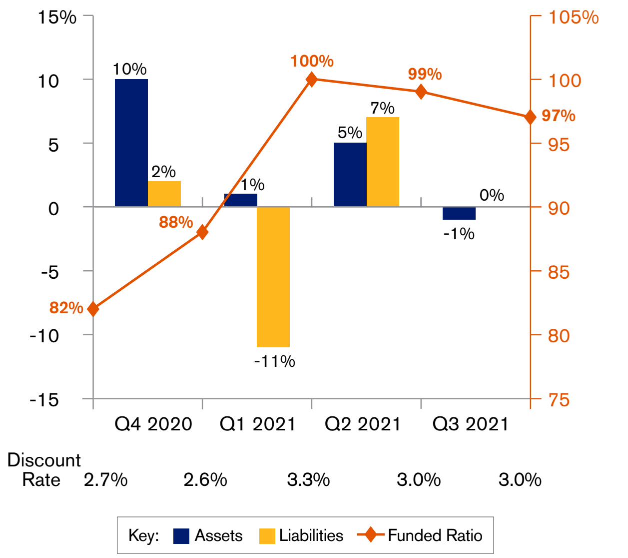
During the third quarter of 2021 (Q3), the funded status of the model pension plan examined in each issue of *Prism* dropped by 2 percentage points, to 97 percent. (See Graph 1.) This decrease in funded status is primarily attributable to a 1 percent decrease in assets.

Changes in the yield curve

High-quality corporate bond yields rose slightly during Q3 — the net result of a 5 basis-point increase in U.S. nominal Treasury yields and credit spreads that were mostly flat (see "Aspects of investment performance" on the next page for more details). This is illustrated in Graph 2 by the above-median curves.

Plans' liabilities are measured with the yield curve, determined by reference to high-quality corporate bond yields. Changes in the shape of the yield curve may have varying impact on plans' liabilities based on their maturity. (For background on yield curves, [read our primer].)

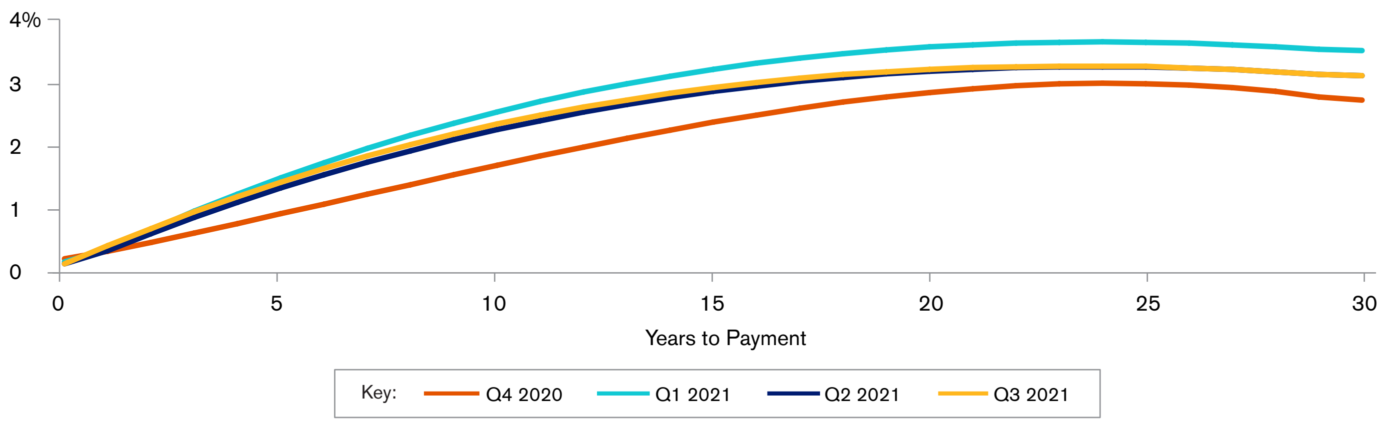
Graph 1: Change in Assets,[1] Liabilities and Funded Ratio[2]



[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. In May 2021, the funded percentage for the model DB plan was reset as of January 1, 2021, to reflect the average actual funded percentage of large pension plans.

Graph 2: 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.

About *Prism*

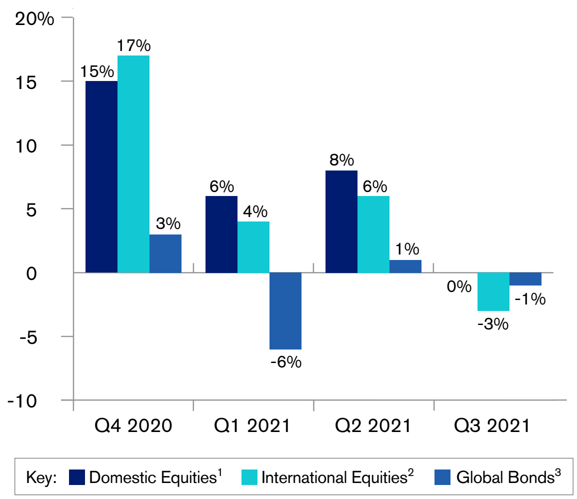
Prism examines the effect of changes in the assets and liabilities of a model private sector single-employer pension plan on its funded ratio over the four most recent quarters, viewing such changes through a marked-to-market lens. The primary focus is to understand the combined impact of asset movement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

Aspects of investment performance

This section discusses aspects of investment performance illustrated in Graph 3 that contributed to the model plan's 1 percent loss in asset value in Q3.

During Q3, financial markets ended up about where they started, after September losses offset gains earlier in the quarter. The percentage of fully vaccinated adults continued to climb, increasing by about 10 percentage points during the quarter, but COVID-related cases, hospitalizations and deaths all increased materially during the quarter providing some headwinds to financial market performance.

Graph 3: 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

Stock market performance was somewhat negative both domestically and internationally, with U.S. equities slightly outperforming developed international equities. Emerging market equities were the worst performer this quarter with Chinese stocks in particular performing poorly as a result of the default fears facing a large real estate developer.

Fixed income returns were relatively flat domestically during the quarter as yields barely moved, and slightly negative internationally — due partially to a strengthening U.S. dollar.

U.S. Treasury yields ended the quarter slightly higher than where they began, while investment-grade credit spreads stayed flat. As a result, U.S. government and investment-grade bond returns were all nearly flat for the quarter, regardless of maturity. In September 2021, the Federal Open Market Committee (FOMC) decided to maintain the target range for the federal funds rate at 0 to 0.25 percent. The FOMC further signaled that the target range could increase sooner than previously expected due to mounting concern over the persistency of inflation. The yield on the 10-year Treasury note ended the quarter at 1.52 percent, up 7 basis points from where it began.

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 Segal 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
- **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

* Individual plan results will differ from this model for a host of reasons, including different funded positions, liability duration and contribution patterns.

For more information about how ALM can help you manage your plan, contact your Segal Marco Advisors investment consultant or your Segal retirement consultant — or get in touch with us via our websites: segalmarco.com and segalco.com.

To receive future issues of *Prism* and other publications of interest to employers as soon as they are available online, join our email list.

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