Prism

First Quarter 2023 Pension Plan Experience

Model Pension Plan's Funded Status Continues to Rise

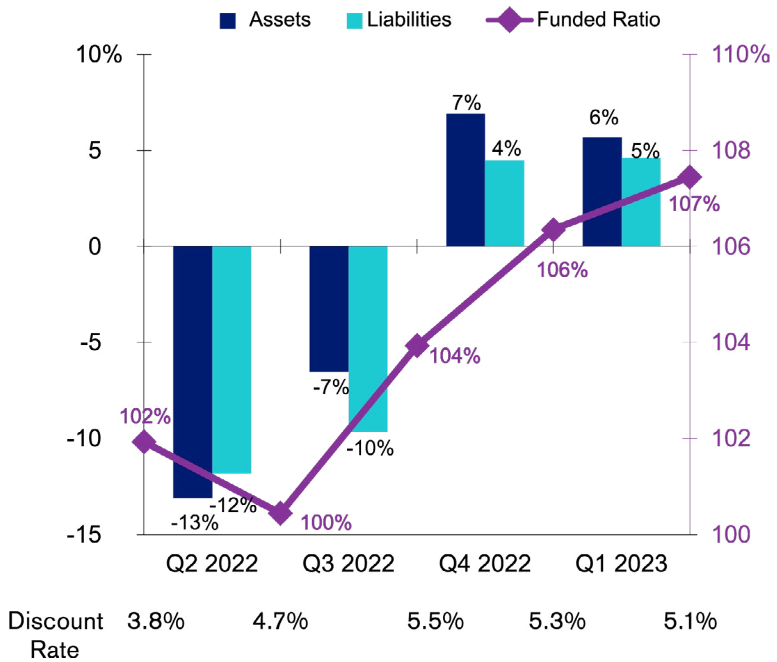
During the first quarter (Q1) of 2023, the funded status of the model pension plan examined in each issue of *Prism* rose by 1 percentage point, to 107 percent. (See Graph 1.) This increase in funded status is attributable to a 6 percent increase in assets, partially offset by a 5 percent increase in liabilities.

Changes in the yield curve

High-quality corporate bond yields decreased by 25 basis points during Q1 — the net result of a 10 basis-point increase in credit spreads and a 35 basis-point decrease in U.S. nominal Treasury yields (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.)

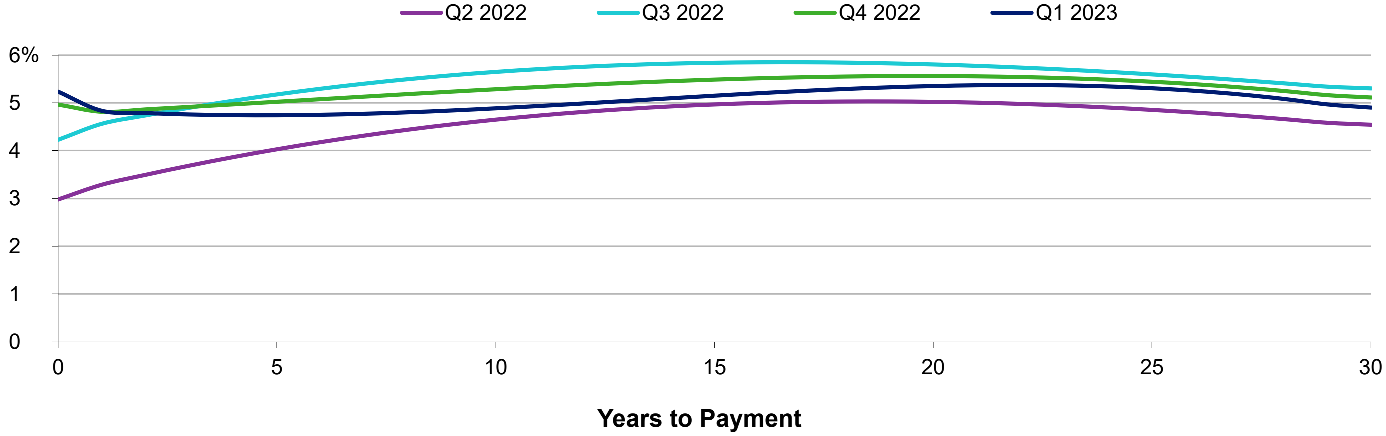
Graph 1: Change in Assets,[1] Liabilities and Funded Ratio[2]



[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 2022 (after publication of the Q1 2022 *Prism*), the funded percentage for the model DB plan was reset as of January 1, 2022 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*

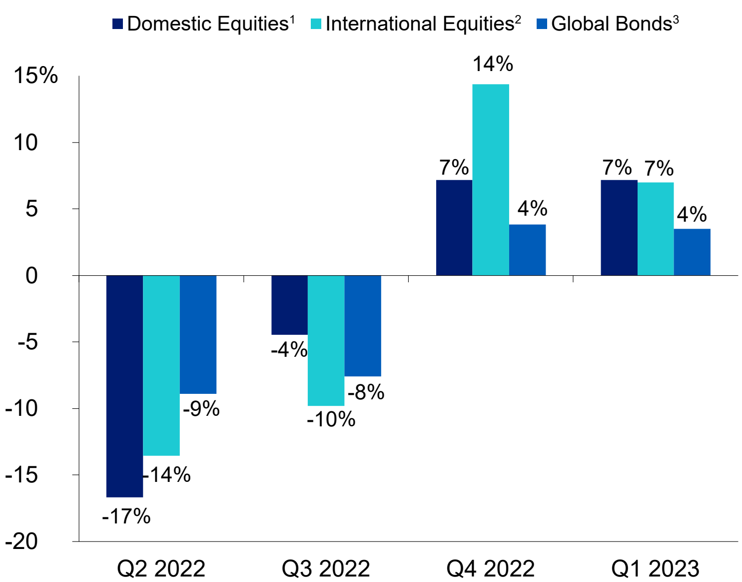
***Prism* examines the effect of changes in the assets and liabilities of a model private sector single-employer pension plan on its funded ratio over the four most recent quarters, viewing such changes through a marked-to-market lens. The primary focus is to understand the combined impact of asset movement 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 6 percent rise in asset value in Q1.

U.S. equity and fixed income both posted single-digit returns during Q1. U.S. equity markets were positive during a volatile quarter that was dominated by a regional bank crisis and investor expectations regarding whether Federal Reserve (the Fed) rate increases were ending. In response to still stubbornly high inflation and a red-hot jobs market that puts the unemployment rate at a near record-low level, the Fed continues to raise rates, but at a slower pace. Developed international and emerging market equities also posted positive single-digit returns during the quarter, with developed international stocks outperforming both U.S. and emerging market stocks. A modestly weakening U.S. dollar during the quarter provided a further tailwind for international markets. Domestically, growth stocks significantly outperformed value, and large-cap stocks modestly outperformed small caps.

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

Fixed income returns were positive in Q1 both domestically and internationally with interest rates moderating somewhat. International bonds were aided by U.S. dollar weakness. U.S. Treasury yields tightened across the yield curve providing single-digit bond returns for all investment-grade bond asset classes. In March 2023, the Federal Open Market Committee (FOMC) increased the target range for the federal funds rate (for a ninth consecutive meeting) 25 basis points to a target range of 4.75–5.00 percent. FOMC's guidance indicates that the Fed may be close to ending its hiking cycle, but only if inflation data continues to moderate. The yield on the 10-year Treasury note ended the quarter at 3.48 percent, down 40 basis points during Q1.

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.

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