Prism

6-Point Jump in Model Pension Plan's Funded Status

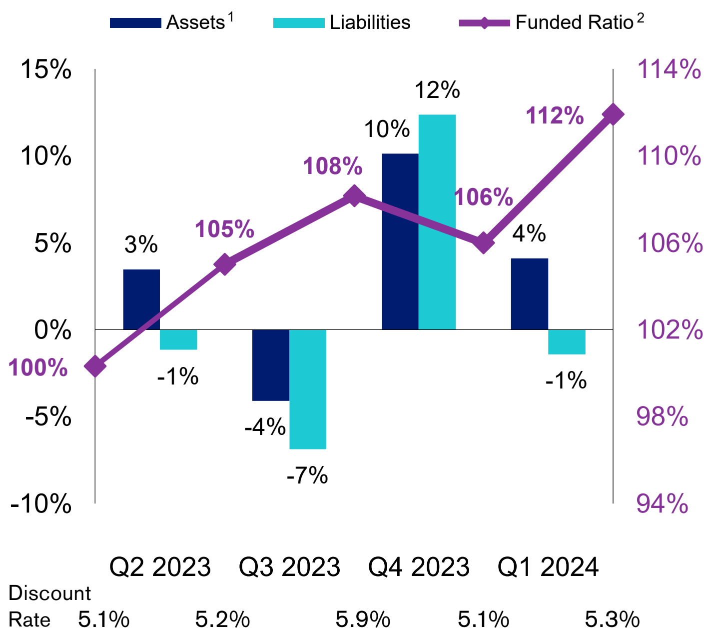
During the first quarter (Q1) of 2024, the funded status of the model pension plan examined in each issue of *Prism* rose by 6 percentage points, to 112 percent. (See Graph 1.) This increase in funded status is attributable to a 4 percent increase in assets and a 1 percent decrease in liabilities.

Changes in the yield curve

High-quality corporate bond yields increased by 20 basis points during Q1 — the net result of a 10 basis-point decrease in credit spreads and a 30 basis-point increase 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.)

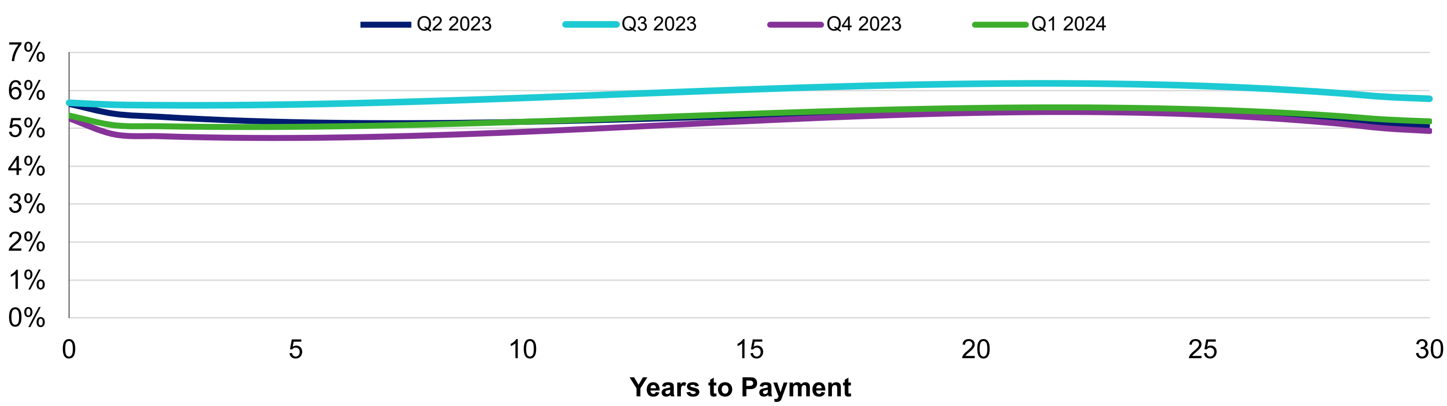
Graph 1: Change in Assets, Liabilities and Funded Ratio



[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 2023 (after publication of the Q1 2023 *Prism*), the funded percentage for the model DB plan was reset as of January 1, 2023 to reflect the average actual funded percentage of large pension plans.

Graph 2: Changes in the Yield Curve*



* 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*

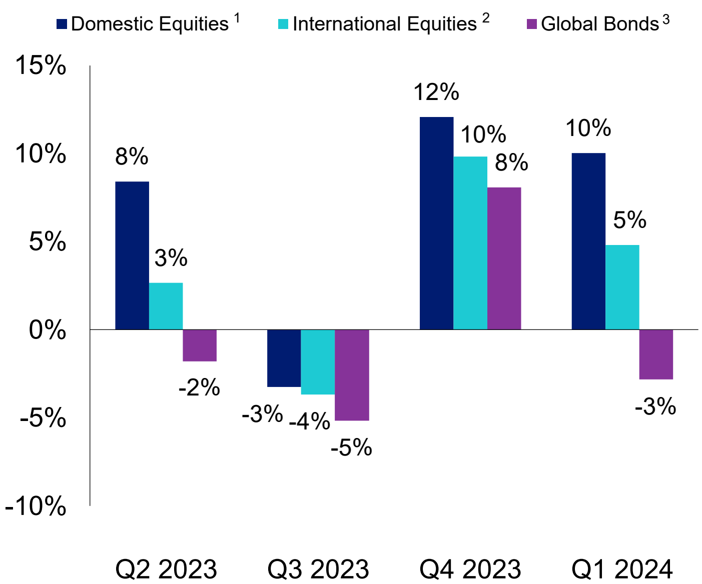
Prism examines the effect of changes in the assets and liabilities of a model private sector single-employer pension plan on its funded ratio over the four most recent quarters, viewing such changes through a marked-to-market lens. The primary focus is to understand the combined impact of asset movement 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 4 percent increase in asset value in Q1.

Both domestic and international equities had positive returns in Q1 — with domestic equities outperforming both developed international and emerging market equities. Emerging market equities were the laggard again this quarter, underperforming both U.S. and developed international stocks, although emerging markets also posted positive returns. A strong U.S. dollar hurt the performance of international stocks somewhat. Year-over-year inflation data during the quarter indicate that the anticipated reduction in inflation hasn't happened, which suggests any rate cuts this year may come later than expected. Nevertheless, U.S. unemployment remains low, corporate profits remain strong and market sentiment indicates a resilient consumer, all supporting strong market performance. Domestically, growth stocks outperformed value and large-cap stocks 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 slightly negative domestically and in developed international markets, with interest rates ticking slightly higher during the quarter. Emerging market debt posted slightly positive returns during Q1. U.S. Aggregate Bonds returned -1 percent during Q1, and the Global Aggregate Index posted a -2 percent return. The Federal Open Market Committee held the target range for the federal funds rate at 5.25 to 5.50 percent for a fifth consecutive meeting. This is the highest level in more than 20 years. Any hopes that rate cuts would come early in the calendar year were dashed when inflation readings remained stubbornly high. The yield on the 10-year Treasury note ended Q1 up 32 basis points from the end of the fourth quarter, at 4.20 percent.

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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