TAKING STOCK: THE IMPORTANCE OF DE-RISKING PENSION PLANS AND Q4 LIABILITY PERFORMANCE

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BLOG POST

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Even as markets settle back down, the rout in December underscores the continuing need for de-risking pension plans.

While the first eleven months of 2018 presented pension plans with a "goldilocks" scenario of increasing assets and funded status and decreasing pension liabilities, the market volatility in December upended much of the gains garnered earlier in the year. Pension plans invested in a traditional 60/40 split between equity and fixed income lost approximately 7.1% in funded status in the fourth quarter. However, NEPC clients implementing a liability-driven investing (LDI) strategy likely fared better during the same period, many holding fewer equities and more longer-dated Treasuries, which returned 4.2% for the three months ended December 31.

We recommend clients continue down their allocation glidepaths as adopted. The recent uptick in pension risk transfers, as employers took advantage of mortality assumption arbitrage opportunities and changes to the corporate tax rate, has led many to lower their plan size and move down their glidepath, while increasing interest-rate hedging in 2018.

After watching interest rates and plans' funded status climb throughout the year as pension liabilities fell by 7.21% in 2018, we saw rates fall back in December. At the same time, spreads widened, creating an almost flat return for discount rates and liabilities during the fourth quarter. Liabilities increased 0.3% since September, and the corresponding discount rate proxy moved from 4.17% on September 30 to 4.22% as of December 31, according to the FTSE Pension Liability Index.

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