The Monthly Pension Review: October 2023

Rates remain at cycle highs, providing an opportunity for plan de-risking

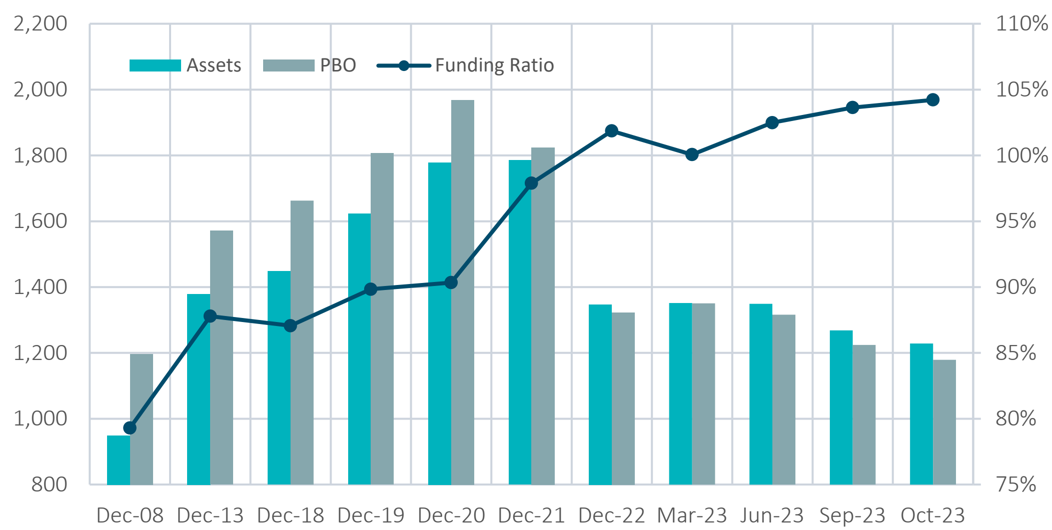
SLC Management

October Market Summary

- **Funded status increases by 0.6% through September** – Assets returned -2.7% while liabilities returned -3.1%.(1)
- **Equities continued to slump in October** – The S&P 500 Index returned -2.2% last month, as economic uncertainty and the rise in Treasury yields impacted sentiment.
- **The Long Credit Index yield rose by 39 basis points (bps) in October** – The yield increase was driven by rates, as the 30-year Treasury rose 39 bps last month.

Market Watch	Dec-21	Dec-22	Sep-23	Oct-23
Funded Status (1)	97.9%	101.9%	103.6%	104.2%
FTSE Discount Rate	2.63%	4.95%	5.61%	5.96%
Long Credit Yield (2)	3.10%	5.59%	6.13%	6.52%
US 30Y TSY Yield	1.90%	3.96%	4.70%	5.09%
S&P500	4,766	3,840	4,288	4,194

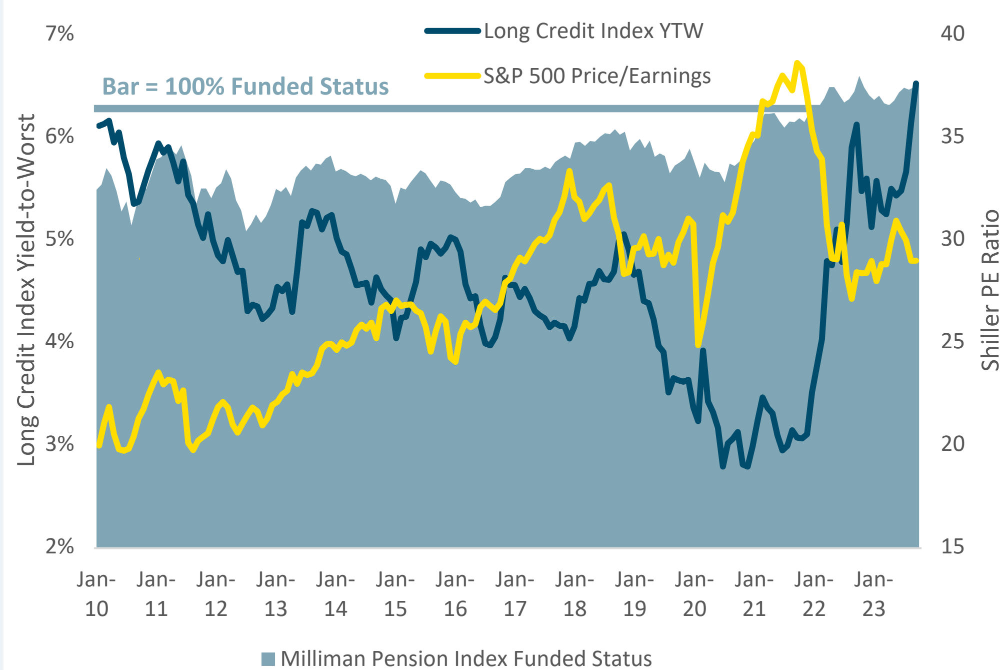
Milliman Pension Funding Index (October 2023)



BONDS VS. STOCKS: RELATIVE VALUE, IMPACT ON DE-RISKING

- In March of 2022, the U.S. Federal Reserve began hiking interest rates to counter high inflation. Short Treasury rates rose, which subsequently drove long rates up as well. As a result, the average funded status for the Milliman 100 Pension Funding Index rose above 100% for the first time since August 2008. The index's funded status has remained above 100% in 19 of the 20 months since March 2022, and closed October at a value of 104.2%, its highest reading since May 2008, indicating that DB pension plans are consistently in a position of surplus for the first time in over a decade.
- After a prolonged bull market run in the fixed income market following the Global Financial Crisis of 2007–2008, bonds experienced their worst year on record in 2022, with the Long Credit Index returning -25.3%, predominantly due to rising interest rates. As prices declined across the board, yields have risen to their highest levels in nearly 15 years, presenting an attractive opportunity for institutional investors to lock in high rates. The 30-year Treasury closed October at 5.09%, and the yield-to-worst on the Long Credit Index finished at 6.52%.
- Equities also had a down year in 2022 but have rallied so far in 2023. According to the Shiller PE Ratio, which is the price-to-earnings ratio of the S&P 500 Index based on average inflation-adjusted earnings from the previous 10 years, equity valuations are substantially higher than their long-term average. As of October month end, the Shiller PE sat at a value of 28.9, almost double the long-term average value of 17.1. Given near term expectations of economic headwinds, these elevated valuations may not be pricing in the full level of risk currently facing markets.
- Given elevated funded status ratios and the current relative value landscape of bonds and stocks (i.e., bond valuations appear cheap and equity valuations appear rich), we believe plan sponsors should strongly consider de-risking plans and locking in higher interest rates while they are here.

Long Credit Yield vs. S&P 500 Long-Term P/E



*Based on monthly performance of the S&P 500 Index. Data from Bloomberg.

(1) Data from reference Bloomberg Indices. Funded status is in reference to Pension Funding Index of the top 100 US corporate pension plans sourced from Milliman.

(2) Funded Status source: Milliman. FTSE Discount Rate source: FTSE. Long Credit Yield source: Bloomberg. US 30Y TSY Yield source: Bloomberg. AAA Non-Agency CMBS and A Corporate source: Bloomberg.

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Market chart indices:
- AAA Non-Agency CMBS and A Corporate source: Index data from Bloomberg.

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Disclosures

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(1) Funded Status for the current month is estimated and subject to change as final numbers are released. Data from reference Bloomberg Indices.
(2) The Long Credit yield corresponds to the Bloomberg Long Credit Index.