The Monthly Pension Review: March 2023

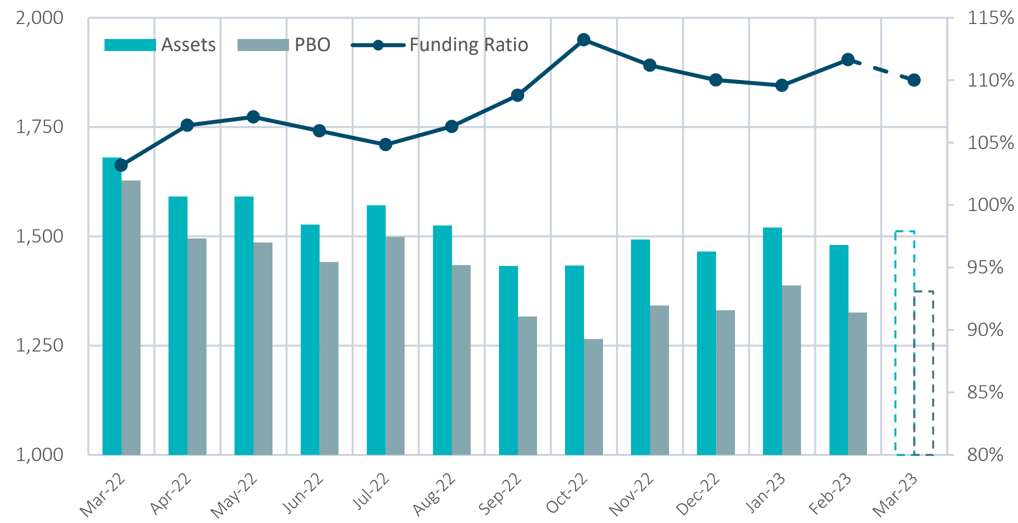
Funded status decreases as rates take a tumble

March Market Summary

- Funded status falls despite positive performance across fixed income and equities – Assets returned 2.2% while liabilities increased by 3.7%.(1)
- Equities rebounded amid the market volatility after a negative February – The S&P 500 Index returned 3.7% in March as the market rebounded once the dust settled from the bank turmoil.
- The Long Credit Index yield decreased by 29 basis points (bps) in March after rising 45 bps in February – Despite the fears of credit stress, long spreads remained relatively unchanged in March as Treasury rates caused the decline in yield.

Market Watch (2)	Dec-21	Dec-22	Feb-23	Mar-23
Funded Status	97.9%	110.0%	111.6%	110.0%
FTSE Discount Rate	2.63%	4.95%	5.02%	4.70%
Long Credit Yield	3.10%	5.59%	5.57%	5.28%
US 30Y TSY Yield	1.90%	3.96%	3.92%	3.65%
S&P 500	4,766	3,840	3,970	4,109

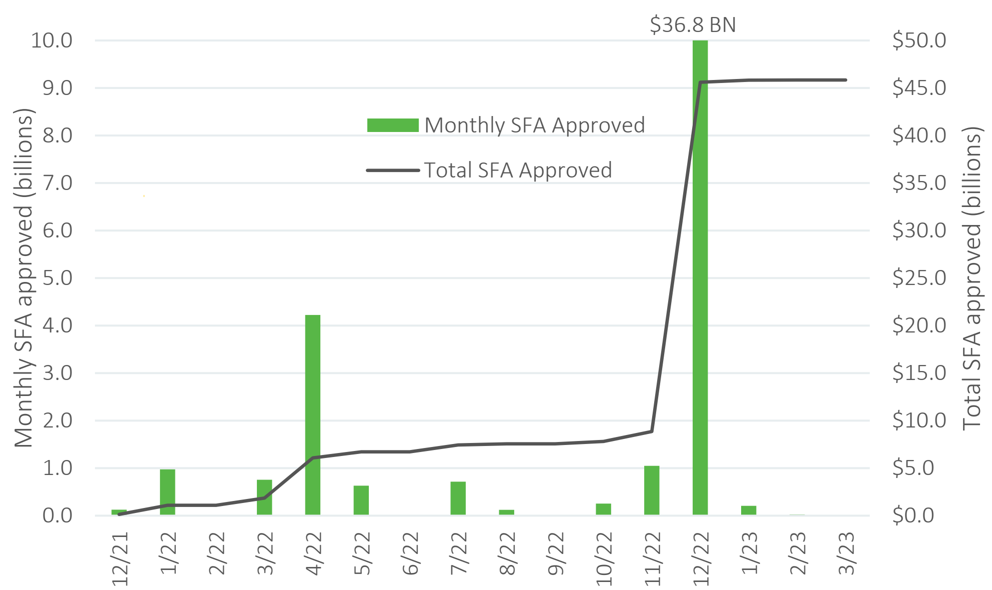
Milliman Pension Funding Index (March 2023 estimate)



SPOTLIGHT: ARPA'S IMPACT ON TAFT HARTLEY PLANS

- Cash-flow-focused mandates have traditionally been used by corporate pension plans and insurers looking to better hedge their liability payments. However, with the implementation of the American Rescue Plan Act of 2021 (ARPA), we are seeing historically underfunded multi-employer pension plans utilize the same tools to secure benefit payments for plan participants.
- These plans are estimated to receive $90+ billion as part of the Special Financial Assistance (SFA) Program component of ARPA, administered by the Pension Benefit Guaranty Corporation (PBGC). Initially, the PBGC was focused on defined priority groups, but as of 3/11/2023, all other financially troubled multiemployer plans could apply.
- As of 3/31/2023, the PBGC had approved over $45 billion in SFA assets with another $23 billion under review. As the priority group window to apply for SFA assets has ended, there are now over 100 additional plans on the waiting list to be reviewed for approval.
- Some elements of the investment strategy related to SFA assets are prescribed. This includes requiring a minimum of 67% of SFA assets to be invested in IG fixed income, as well as restrictions on the type of instruments permitted.
- Plan sponsors face the challenges of securing future payments while also generating excess returns that may extend the life of plan assets. At SLC Management, we work with our Taft Hartley clients to build compelling solutions, both cash-flow-focused and total-return-oriented, that strike the balance between these two objectives.

Total SFA assets approved over $45 billion, with $37 billion approved in December 2022 alone



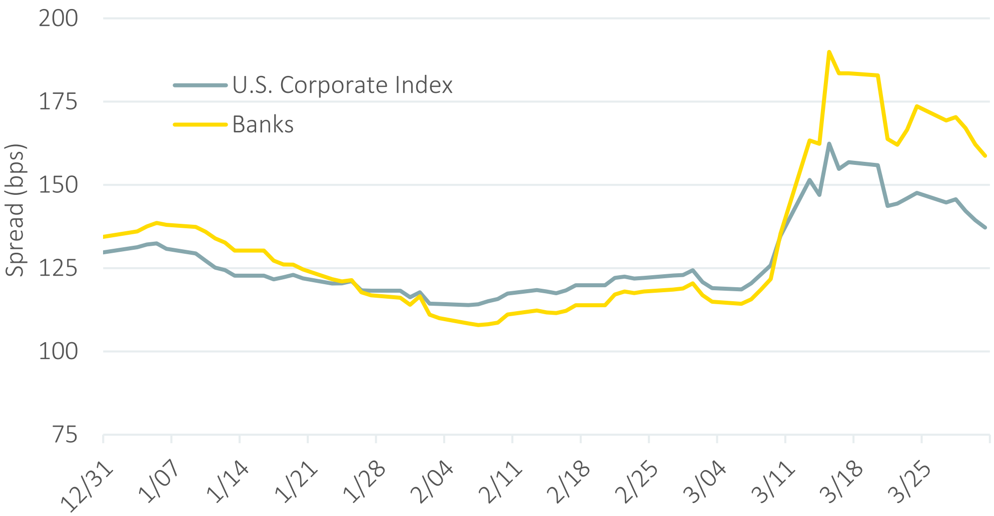
Source: Pension Benefit Guaranty Corporation.

(1) Funded Status for the current month is estimated and subject to change as final numbers are released. Data from reference Bloomberg Indices. Funded status is in reference to the top 100 US corporate pension plans sourced from Milliman.

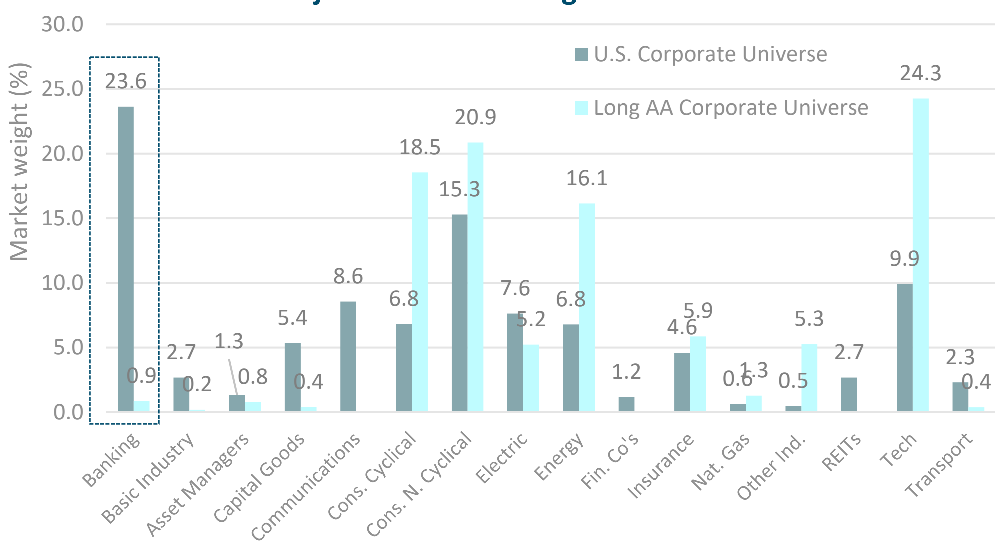
(2) Funded Status source: Milliman. FTSE Discount Rate source: FTSE. Long Credit Yield source: Bloomberg. US 30Y TSY Yield source: Bloomberg. S&P 500 source: Bloomberg. Long Corporate Index source: Bloomberg.

SLC-20230413-2842848

After trading inside the U.S. Corporate Credit index in February, banks now sit 22bps wide following the March turmoil



Banks make up ~24% of the overall corporate universe but just ~1% of the long AA universe



Market observations:

- After lagging the rest of the corporate credit market in 2022, financials swung from the best performing corporate sector in 2023 through to February to the worst performing sector through to March.
- Despite realizing a 2023 year-to-date spread tightening of 25 bps by February, the financials sector ended the quarter 25 bps wider than year end 2022, compared to a spread widening of only 8 bps for the overall corporate credit index.

SLC Management view:

- We began to trim our financials overweight within our long credit portfolios in January and February as we looked to take gains from the spread rally within banks amid lower issuance from global systemically important banks (G-SIBs).
- Our allocation fell from an overweight of almost 6% to start 2023 to around 2% by the end of Q1 with almost all the movement happening before the banking turmoil began the week of March 10.

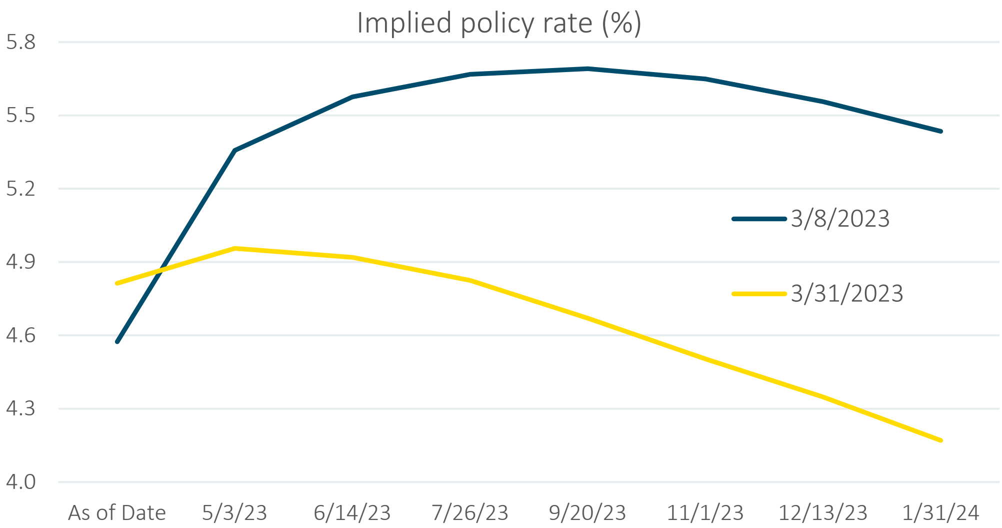
Implications for plan sponsors:

- For LDI investors, it is important to understand the credit mismatch between the discount rate used to value liabilities and the corporate credit portfolios often used to hedge those liabilities.
- While financial spreads blew out compared to the overall corporate universe, other sectors stayed relatively in line with the market. Banking makes up over 20% of the U.S. corporate universe but less than 1% of the long AA corporate universe. Due to this mismatch, portfolios used to hedge liabilities discounted on an AA curve may have experienced a spread mismatch during the first quarter of 2023.

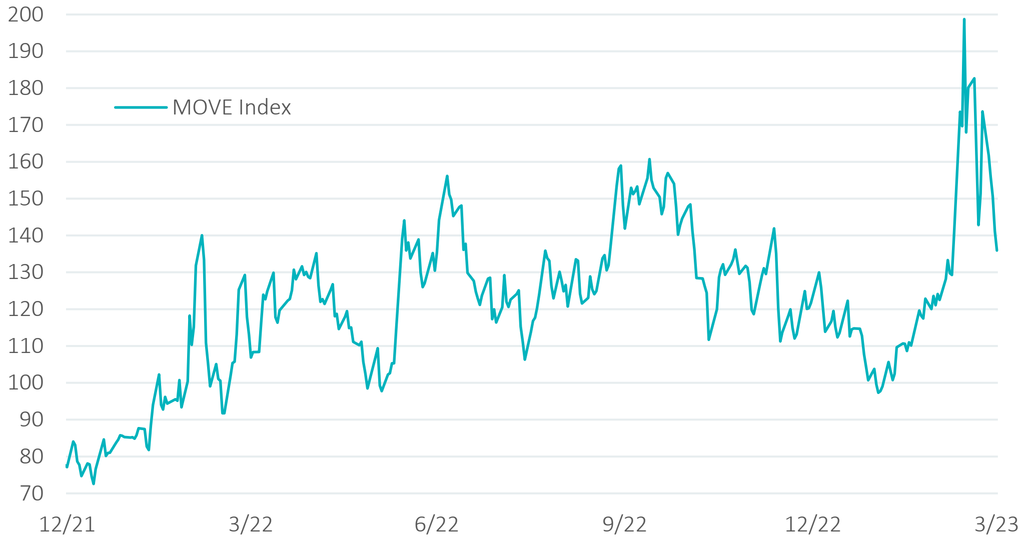
Source: Bloomberg.
A full list of data sources and indices can be found in the back of this presentation.

SLC-20230413-2842848

The market has swung from pricing in continued hikes to potential cuts



The bank turmoil in mid-March caused interest rate volatility to spike to levels not seen since 2008



Market observations:

- Regional bank turmoil in March drastically reduced market expectations for future tightening by the U.S. Federal Reserve. At current levels, the market effectively believes that the Fed could start cutting interest rates this year.
- As of March 8, the terminal, or peak, Fed funds rate implied by the bond market was 5.69%. But as of March month end, the rally in Treasuries had reduced the terminal rate to 4.96%, falling near the current effective policy rate of 4.83%.
- Interest rate volatility hit its highest level since 2008 as the MOVE index jumped from 124 at the end of February to a high of 199 on March 15. However, after only a few weeks at elevated levels, the index fell to 136 to close out the month of March.

SLC Management view:

- Under typical market conditions, a focus on overall duration and credit exposure can capture the vast majority of interest rate risk for a plan sponsor. However, front-end interest rates have seen a significant increase in volatility, and this could prove to be a driver of funded status volatility for plans that haven't effectively hedged their key rate exposures across the yield curve. We recommend that plan sponsors take a holistic look at their interest rate exposure and evaluate any significant mismatches in term structure.

Implications for plan sponsors:

- The 10-year Treasury yield finished the month at 3.48%, rising to a peak of 4.06% on March 2 before falling to a low of 3.38% on March 24, a 68-bp intramonth swing. The 2-year Treasury saw a swing that was almost double in size at 128 bps intramonth.
- Despite the significant drop in yields and elevated market volatility, the average funded status for corporate pension plans finished Q1 2023 unchanged at 110% as the year-to-date return of 7.5% in equities helped to offset the decline in liability discount rates.

Source: Bloomberg, Milliman.
A full list of data sources and indices can be found in the back of this presentation.

Disclosures

Nothing in this paper should (i) be construed to cause any of the operations under SLC Management to be an investment advice fiduciary under the U.S. Employee Retirement Income Security Act of 1974, as amended, the U.S. Internal Revenue Code of 1986, as amended, or similar law, (ii) be considered individualized investment advice to plan assets based on the particular needs of a plan or (iii) serve as a primary basis for investment decisions with respect to plan assets.

The information may present materials or statements which reflect expectations or forecasts of future events. Such forward-looking statements are speculative in nature and may be subject to risks, uncertainties and assumptions and actual results which could differ significantly from the statements. As such, do not place undue reliance upon such forward-looking statements. All opinions and commentary are subject to change without notice and are provided in good faith without legal responsibility.

Certain information contained herein has been obtained from published and non-published sources prepared by other parties, which in certain cases has not been updated through the date hereof. While such information is believed to be reliable for the purpose used herein, SLC does not assume any responsibility for the accuracy or completeness of such information and such information has not been independently verified by SLC.

Market chart indices:
- Special Financial Assistance program of American Rescue Plan Act asset source: PBGC
- U.S. Corporate index and bank spreads source: Bloomberg
- Market weight of sector in U.S. Corporate Universe and Long AA Corporate Universe source: Bloomberg
- Implied Policy Rate source: Bloomberg
- MOVE index level source: Bloomberg

SLC Management is the brand name for the institutional asset management business of Sun Life Financial Inc. (“Sun Life”) under which Sun Life Capital Management (U.S.) LLC in the United States, and Sun Life Capital Management (Canada) Inc. in Canada operate.

Sun Life Capital Management (Canada) Inc. is a Canadian registered portfolio manager, investment fund manager, exempt market dealer and, in Ontario, a commodity trading manager. Sun Life Capital Management (U.S.) LLC is registered with the U.S. Securities and Exchange Commission as an investment adviser and is also a Commodity Trading Advisor and Commodity Pool Operator registered with the Commodity Futures Trading Commission under the Commodity Exchange Act and Members of the National Futures Association. In the U.S., securities are offered by Sun Life Institutional Distributors (U.S.) LLC, an SEC registered broker-dealer and a member of the Financial Industry Regulatory Authority (“FINRA”).

BentallGreenOak, InfraRedCapital Partners (InfraRed) are also part of SLC Management and Crescent Capital Group LP (Crescent) are also part of SLC Management.

Bentall Green Oak is a global real estate investment management advisor and a provider of real estate services. In the U.S., real estate mandates are offered by BentallGreenOak (U.S.) Limited Partnership, who is registered with the SEC as an investment adviser. In Canada, real estate mandates are offered by BentallGreenOak (Canada) Limited Partnership, BGO Capital (Canada) Inc. or Sun Life Capital Management (Canada) Inc. BGO Capital (Canada) Inc. is a Canadian registered portfolio manager and exempt market dealer and is registered as an investment fund manager in British Columbia, Ontario and Quebec.

InfraRed Capital Partners is an international investment manager focused on infrastructure. Operating worldwide, InfraRed manages equity capital in multiple private and listed funds, primarily for institutional investors across the globe. InfraRed Capital Partners Ltd. is authorized and regulated in the U.K. by the Financial Conduct Authority.

Sun Life Capital Management (Canada) Inc. is a Canadian registered portfolio manager, investment fund manager, exempt market dealer and, in Ontario, a commodity trading manager, and is the manager of the SLC Management Private Fixed Income Plus Fund, SLC Management Long Term Private Fixed Income Plus Fund, SLC Management Short Term Private Fixed Income Fund and the SLC Management Canadian Commercial Mortgage Fund.

Crescent Capital Group LP is a global alternative credit investment manager registered with the U.S. Securities and Exchange Commission as an investment adviser. Crescent is a leading investor in mezzanine debt, middle market direct lending in the U.S. and Europe, high-yield bonds and broadly syndicated loans.

Disclosures

Your purpose is our purpose

For institutional use only. Investing involves risk including the risk of loss of principal. The information provided does not constitute investment advice and should not be relied on as such. It should not be considered a solicitation to buy or sell a security. It does not take into account the investor's particular investment objectives, strategies, tax status or investment horizon. You should consult with your tax and financial advisor. All material has been obtained from sources believed to be reliable. There is no representation of warranty as to the accuracy of the information and SLC Management shall have no liability for decisions based on such information. The whole or any part of this work may not be reproduced, copied or transmitted or any of its concepts disclosed to third parties without SLC Management's express written consent.

(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.