

The Monthly Pension Review: September 2024



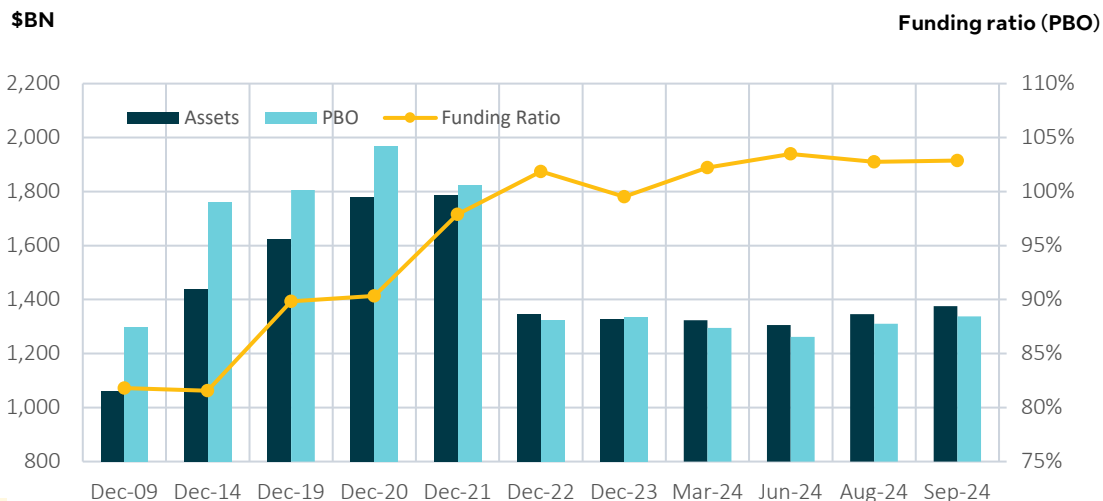
U.S. Federal Reserve finally cuts rates

September Market Summary

- **Funded status remained mostly stagnant in September** – Assets returned 2.2% while liabilities returned 2.1%.(1)
- **The S&P 500 Index returned 2.0% in September** – After experiencing some losses before the U.S. Federal Reserve cuts, the index had its fifth straight month of increases.
- **The Long Credit Index yield fell 17 basis points (bps) last month** – Treasury yields fell 29 bps prior to the Fed cutting rates, and then began to rise again after the rate cuts announcement.

Market Watch	Dec-22	Dec-23	Aug-24	Sep-24
Funded Status (1)	101.9%	99.5%	102.8%	102.9%
FTSE Discount Rate	4.95%	4.76%	4.91%	4.79%
Long Credit Yield	5.59%	5.22%	5.36%	5.19%
US 30Y TSY Yield	3.96%	4.03%	4.20%	4.12%
S&P 500	3,840	4,770	5,648	5,762

Milliman Pension Funding Index (September 2024)¹



Example of risk management during price volatility – excess of 30-year yield of Company A over 30-year Company B's yield²



A. Opportunity for managers to trim exposure to Company A (rated A-/A3 as of December 2018) as spreads began to tighten, while adding to positions in Company B (rated higher at A/A2) to maintain exposure to the same industry

B. Markets sell off; holding Company B over Company A would have enabled managers to remain up in quality

C. Post selloff, the short-term technicals again look attractive in Company A; opportunity for managers to start a new position in Company A, adding through new issuance at market wides and capturing the subsequent tightening in pricing relationship

LONG CREDIT SLEEVES CAN BE AN IMPORTANT PART OF PENSION PLAN PORTFOLIOS

- Long credit tends to correlate strongly with pension plan accounting liabilities, whose discount rates are typically based on high-quality corporate bond yields.
- The asset class can also provide a favorable hedge for the duration and cash flow profile of plans with long-dated liabilities.

There are a number of ways that managers can add value in the long credit space across a variety of market environments.

- A common misconception among investors is that a long-duration portfolio must mean a long-term holding period for the underlying assets.
- For longer-duration portfolios, price return tends to dominate income return. In long-duration portfolios, the benefits of additional yield in lower quality issues can be wiped out by small spread movements.
- Therefore, moving down in quality, or liquidity, to chase extra yield or spread in the long end of the curve is not always a winning strategy.
- Instead, managers tend to see more consistent success in outperforming long-duration benchmarks from exploiting pricing relationships between individual names, capitalizing on spread tightening and actively capturing those returns.
- This approach may lead to a higher information ratio through a portfolio that expresses many smaller active positions rather than a few large macro bets.

For clients like pension plans with an LDI focus, or those that utilize a multi-manager arrangement, this approach can provide a diversified source of alpha against both liabilities and other managers.

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, except for most recent month which is estimated based the return for representative pension plan asset allocation and prior month's liabilities adjusted for duration and change in discount rate. FTSE Discount Rate source: FTSE. Long credit, US 30Y TSY yield, S&P 500 Index value source: Bloomberg.

² Source: Bloomberg. Shown for illustrative purposes only. The securities identified and described do not represent all of the securities purchased, sold or recommended for client accounts. The reader should not assume that an investment in the securities identified was or will be profitable.

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Market chart indices:

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

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