

Pension Insights Newsletter

Fourth Quarter 2024

Corporate Pension Perspectives

Funding Levels

- Corporate pension funded status increased in Q4 2024 by 2.1%. Bonds experienced negative returns as interest rates increased due to fears of continued elevated inflation in 2025 on the backdrop of the presidential election in November. Discount rates therefore also increased, causing liabilities to decrease. Global equities exhibited underperformance overall. Markets in Europe struggled with weak industrial data while Emerging Markets faced headwinds from a strong U.S. dollar. US equities were up modestly thanks to the Mag 7 tech giants. The net result was an increase in funded status over the quarter for the 60/40 portfolio.

Actuarial & Regulatory Updates

- Estimated \$14B pension risk transfer activity during Q3 2024**
 - 35% increase from the third quarter of 2023, driven largely by single \$6B transaction with Prudential
 - Follows \$26B of activity during first half of 2024, a 15% increase from the same period during 2023
- On December 4, 2024, the Department of Labor filed an amicus brief in support of claims by retirees that their joint and survivor annuities need to be no less than the actuarial equivalent of their single life annuities on a reasonable basis**
 - Retirees argued that their joint and survivor annuity calculations violated ERISA's actuarial equivalence requirement by using outdated mortality assumptions. While the DOL did not agree or disagree with the retiree claims, they disagreed with the basis on which the court dismissed the retirees' initial claims
- Social Security Fairness Act signed into law by President Biden**
 - Repeals the Windfall Elimination Provision (WEP) and Government Pension Offset (GPO) provisions that prevented employees with a public pension from receiving full benefits under Social Security
 - Will increase Social Security payments to approximately 2.5 million retirees, including a lump sum for 2024 benefits

Funding Perspective

116.1%

funded status of proxy 60/40 plan

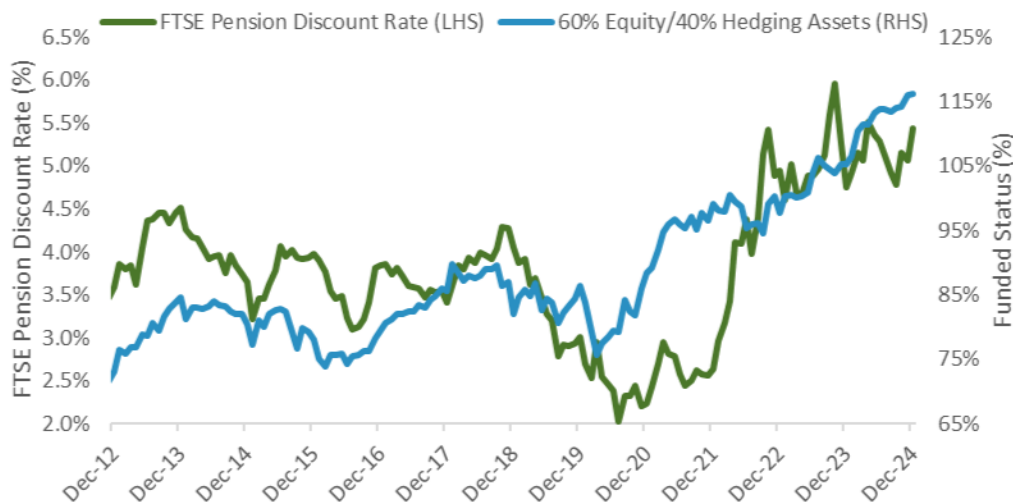
2.1%

change in funded status
for the quarter

5.44%

average discount rate
(up 0.65% in Q4)

FUNDED STATUS AND DISCOUNT RATES



Source: Fidelity Institutional Asset Management, Bloomberg, FTSE, as of 12/31/24.

For illustrative purposes only.



Market Commentary

- With the exception of domestic equities, Q4 saw declines in most asset classes as the global economic expansion took a breather. The weak returns were primarily driven by inflationary worries, investor concerns about mixed economic signals, and increasing geopolitical risks.
- On December 18th, the Fed cut rates 25 bps to a target range of 4.25%-4.5%. They discussed slowing the pace of future cuts as unemployment had undershot and inflation had overshot their forecasts. As a result, all major asset classes posted negative returns in December, with the exception of leveraged loans and commodities.
- Concerns over inflation and the anticipation for a more hawkish Federal Reserve drove the broad sell-off in fixed income during the quarter. Notably, the 10-year Treasury yield increased by 78 bps to 4.57%, which was the largest quarterly increase since 2022; longer duration bonds suffered as a result. Spreads tightened marginally over the quarter, but could not overcome the impact of rising Treasury yields.
- 2024 was a challenging year for fixed income, with the best performer, the Bloomberg U.S. Aggregate Index, returning a modest 1.3% for the year. This index, including a mix of bonds with various maturities, benefited from Fed rate cuts at the short end. The long end of the yield curve, driven more by supply of and demand for these assets, rose during the year. This resulted in negative returns for longer dated corporate and treasury bonds during 2024.
- On the flipside, US large cap equities returned 2.6% in Q4, ending 2024 +24%, largely driven by advancements in AI and resilient economic expansion. Among the "Mag 7", Nvidia, Tesla and Meta were significant contributors to this rally. Small Caps (+11.5% in 2024) continue to lag their larger peers.
- International markets lagged the U.S., especially in Q4 as the dollar strengthened, making exports from Europe and Asia less competitive. International Developed markets fell 8.1% for the quarter while Emerging market equities declined 7.9%. With the U.S. election results behind us, sovereigns are bracing for potential U.S. tariffs and their resulting impact to trade balances.

Market Moves: Interest Rates

Discount rates increased during the quarter, resulting in lower liability values.

	12/31/2024	9/30/2024	Change
Discount Rates			
FTSE Pension Discount*	5.44%	4.79%	0.65%
BBG Long Corporate	5.80%	5.18%	0.62%
BBG Long Treasury	4.86%	4.17%	0.69%
BBG Long Gov/Credit	5.34%	4.69%	0.65%
BBG Aggregate Bond Index	4.91%	4.23%	0.68%

Market Moves: Returns

International Stocks, bonds and liabilities all decreased during the fourth quarter. Ending on a positive note in Q4, domestic equities considerably outpaced other asset classes.

	4Q24	1-Year	3-Year
Equity Returns			
Russell 3000 (US Stocks)	2.6%	23.8%	8.0%
ACWI ex-U.S. (Non-US Stocks)	-7.6%	5.5%	0.8%
Bond Returns			
BBG Long Corporate	-6.2%	-1.9%	-6.8%
BBG Long Treasury	-8.6%	-6.4%	-12.0%
BBG Long Gov/Credit	-7.4%	-4.2%	-9.2%
BBG Aggregate Bond Index	-3.1%	1.3%	-2.4%
Liability Returns			
Proxy Liability*	-5.6%	-2.3%	-6.2%

Index performance shown does not reflect the deduction of advisory fees, transaction charges and other expenses, which if charged would reduce performance. All indices are unmanaged. Investing directly in an index is not possible. **Past performance is no guarantee of future results.**

Source: Fidelity Institutional Asset Management, Bloomberg, FTSE, as of 12/31/2024.

* Discount rate and proxy liability return based on FTSE Pension Liability Short Index (approximately 11-year duration). 3-Year return is annualized. For illustrative purposes only.

Real-World Considerations

Improved Pension Funded Status

The combined effect of equity markets racing to all-time highs and interest rates continuing to march higher during 2024 was the continued improvement of corporate defined benefit (DB) pension plan funded statuses. The rise in interest rates over the last few years combined with recent equity market performance has plan sponsors in a position not seen since before the financial crisis of 2008 – with a funding *surplus* to manage and protect, rather than a funding *deficit* and the associated required contributions. This paradigm shift from underfunded to overfunded DB plans has led to the emergence of several strategic trends for pension plans. Further, the continued improvement of the PBGC's funded position could lead to lower premiums charged by the government agency in the future and thus lower the cost of sponsoring a DB pension plan.

Emerging Trends Given New State of Pension Surpluses

As the funded status of pension plans has continued to improve, several strategic trends have emerged:

1. Shifting asset allocations away from equities and into high quality corporate bonds to lock in funded status improvement. Form 5500 data from 2018 to 2023 indicates that the average allocation to liability matching fixed income for the largest 100 corporate DB pension plans has increased 7% from 35% to 42%. By shifting out of equities and into fixed-income assets that match the profile of the pension liability, plan sponsors have been able to significantly reduce both equity and interest rate risk of their pension plans.
2. Record-breaking risk transfer activity. Persistent high Pension Benefit Guaranty Corporation (PBGC) premiums have significantly increased the administrative cost of sponsoring a DB pension plan. As a result, plan sponsors have increasingly turned to insurance companies to transfer portions of pension liability and reduce annual premium payments.
3. Some plan sponsors now find themselves in the enviable position of being significantly *overfunded*. Rather than look to de-risk or transfer the liability, a subset of these sponsors are finding creative ways to utilize their pension surplus in order to achieve certain HR objectives. One example is temporarily reducing or eliminating contributions to their 401(k) plan and replacing with a cash balance benefit in their DB plan with relatively equal value. Other examples include transferring excess assets to a retiree medical or life insurance plan (a "Section 420 transfer"), using excess assets to offer an early retirement window, and paying bonuses or other ancillary benefits through the DB plan.

What Does the Future Hold for DB Pension Plans?

- According to their 2024 annual report, the PBGC Single-Employer program's funding surplus grew from \$45 billion at the end of fiscal-year 2023 to \$54 billion at the end of fiscal year 2024. PBGC premiums present a significant cost to sponsors of DB plans, as seen through the rapid increase in pension de-risking activity referenced above. While Congress has ultimate control over the level of premium rates, the improved PBGC funded position could present an opportunity for legislators to lower premium rates in the future, and thus the cost of DB plan sponsorship. Such a decrease in premium rates could slow the trend of risk transfer activity, as plan sponsors would be less likely to pay premiums charged by insurers for taking on their pension risk and instead opt to manage pension risk through adjustments to their asset allocation.
- Research from a study published by the National Institute on Retirement Security entitled "Still a Better Bang of the Buck" found that DB pensions are more cost efficient at providing retirement income to retirees than defined contribution plans, delivering the same retirement income with 48% lower cost. This efficiency was determined to be the result of pooled longevity risk, the ability to maintain an "optimal" investment portfolio relative to an aging individual investor, and professional asset management. If the administration cost of sponsoring a DB plan is reduced through lower PBGC premiums, then plan sponsors could take a closer look at implementing defined benefit plans. Creative designs can be utilized that avoid balance sheet volatility while allowing participants to benefit from long-term market performance, such as market-based cash balance and variable annuity plans.

Additional Information:

Learn more about [Fidelity's Pension Solutions](#)

For Administration and Actuarial information visit: [Fidelity's Defined Benefit Solutions website](#)

For Investment Management information visit: [Fidelity's Institutional website](#)

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DEFINITIONS AND IMPORTANT INFORMATION

S&P 500 Index is a market capitalization-weighted index of 500 common stocks chosen for market size, liquidity, and industry group representation to represent US equity performance. **The FTSE Pension Liability Index** represents the single discount rate that would produce the same present value as calculated by discounting a standardized set of liabilities for a frozen pension plan using the FTSE Pension Discount Curve. **Bloomberg (BBG) US Long Treasury Index** is a market value-weighted index of investment-grade fixed-rate public obligations of the US Treasury with maturities of ten years or more. **Bloomberg (BBG) US Long Government/Credit Bond Index** is a market value-weighted index designed to measure the performance of fixed-rate, dollar-denominated, investment-grade debt securities with maturities of 10 years or more. **Russell 3000 Index** is a market capitalization-weighted index designed to measure the performance of the 3,000 largest companies in the US equity market.

MSCI ACWI (All Country World Index) ex USA Index is a market capitalization-weighted index that is designed to measure the investable equity market performance for global investors of large and mid cap stocks in developed and emerging markets, excluding the United States. Index returns are adjusted for tax withholding rates applicable to U.S. based mutual funds organized as Massachusetts business trusts (NR). **Bloomberg (BBG) US Aggregate Bond Index** is a broad-based flagship benchmark that measures the investment grade, US dollar-denominated, fixed-rate taxable bond market. The index includes Treasuries, government-related and corporate securities, mortgage-back securities (agency fixed-rate pass-throughs), asset-backed securities and collateralized mortgage-backed securities (agency and non-agency). **Bloomberg (BBG) US Corporate Bond Index** is an unmanaged market value-weighted index of investment-grade corporate fixed-rate debt issues with maturities of one year or more.

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