The Monthly Pension Review: September 2023

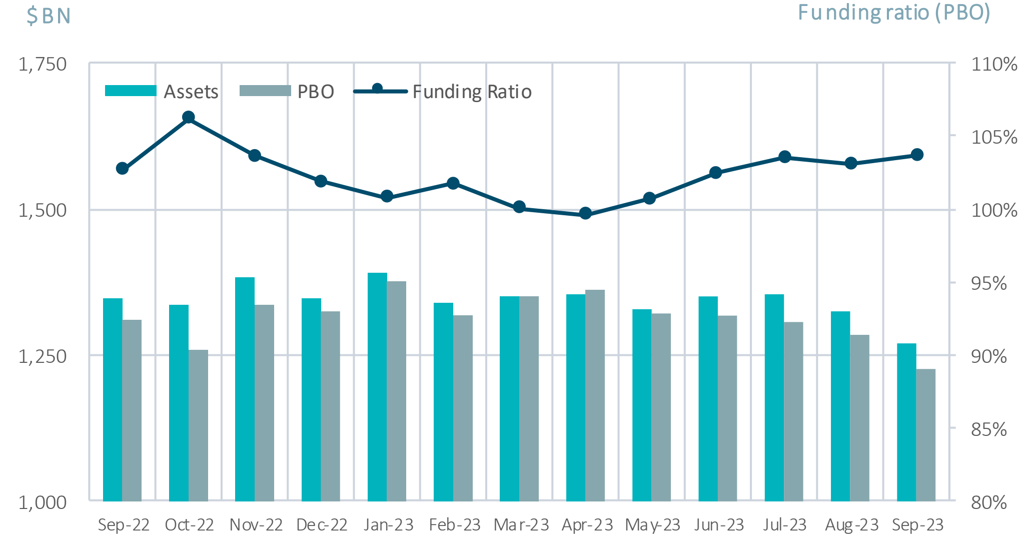
Intermediate & long Treasury yields continue to rise as investors anticipate high base rates for longer

September Market Summary

- **Funded status increases by 0.5% through September** – Assets returned -3.7% while liabilities returned -4.1%.[1]
- **Equities continued to slump in September** – The S&P 500 Index returned -4.8% last month, as economic uncertainty and the rise in Treasury yields impacted sentiment.
- **The Long Credit Index yield rose by 48 basis points (bps) in August** – The yield increase was primarily rates driven as the 30-year Treasury rose 49 bps last month.

Market Watch	Dec-21	Dec-22	Aug-23	Sep-23
Funded Status [1]	97.9%	101.9%	103.1%	103.6%
FTSE Discount Rate	2.63%	4.95%	5.13%	5.61%
Long Credit Yield [2]	3.10%	5.59%	5.65%	6.13%
US 30Y TSY Yield	1.90%	3.96%	4.21%	4.70%
S&P500	4,766	3,840	4,508	4,288

Milliman Pension Funding Index (September 2023)



IMPLICATIONS OF HIGHER YIELDS ON PLAN SPONSORS

- Following the U.S. Federal Reserve's most aggressive rate hiking cycle on record, U.S. Treasury yields have risen to levels unseen since the Great Financial Crisis of 2007–2008. The 10-year Treasury closed September at 4.57%, while the 30-year closed at 4.70%. Both rates have continued to rise even further during the early days of October. Year to date, the 10-year has risen 70 bps and the 30-year has risen 100 bps.
- While the front end of the yield curve is anchored to the federal funds rate and more directly tied to monetary policy, the long end is determined by expectations of the economy, particularly inflation. Early in the year, there was a disconnect between Fed rhetoric, which was focused on "higher rates for longer," and bond market sentiment. In other words, markets were anticipating capitulation on the part of the Fed. As U.S. economic reports continue to come in hot, inflation remains elevated and the Fed remains entrenched in "higher for longer," intermediate and long Treasury rates have spiked.
- Market technicals – the supply and demand dynamics of the Treasury market – also present headwinds for Treasuries. Less buying from China, and higher rates in other developed economies presenting investment alternatives have hurt demand. On top of this, supply is elevated to fund the budget deficit, and political uncertainty has likely increased the borrowing cost as well. Lower demand and increased supply translate to higher yields.
- The long-term fundamental picture in the economy likely points to lower rates in the future. As inflation continues to inch downward and more economic pain is felt, the Fed is likely to cut rates at some point. As such, investors are presented with the opportunity to lock in higher bond yields while they are here. For plan sponsors, this means de-risking the portfolio and opportunistically allocating to fixed income while yields are elevated. Despite relatively tight corporate credit spreads, the all-in yield on the long credit index closed September at 6.13%, and currently sits at its highest level since 2009.

U.S. 30-year Treasury Yield has reached its highest level in over 10 years

*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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(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.

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