State Board of Administration

FRS Pension Plan Performance Review

Actuarial Assumptions Estimating Conference

October 23, 2019
Introduction

The Legislature, SBA Trustees, Division of Retirement, and SBA staff, have a history of supporting three critical requirements for pension funding sustainability:

- Reasonable benefits
- Prudent investments
- Responsible funding policy

Which resulted in 11-years of actuarial surpluses from 1998 thru 2008 and employers saving a cumulative $6.6B through reduced contributions.
Contributions and Funded Status

- 11-years of actuarial surpluses from 1998 thru 2008 and employers saving a cumulative $6.6B through reduced contributions.
- $3B in actuarially required contribution rates were not funded due to budgetary constraints from 2010 to 2013. Missed an opportunity to gain an estimated $5.8B in asset value as of June 30, 2019.
The “Global Financial Crisis” that began in 2007 led to marked to market asset value declines, creating an unfunded liability.

The FRS Pension Plan’s funded status continues to decline, currently at 83.9% (July 1, 2018), down from 84.3% (July 1, 2017).
FRS Pension Plan Changes in Market Value and Performance From March 9, 2009 Market Low to August 31, 2019 (10.5 Years)

Since the Great Financial Crisis low point, the FRS Pension Plan returned 10.91%, had an investment gain of $141.4B and paid out $63.8B in net benefit payments.
Growth in Pension Liability Continues to Outpace Growth in Asset Values

- Actuarial liabilities have continued to outpace asset growth and now stands at $185.95B as of July 1, 2018.
- Even with a post financial crisis return of 11.5% (from March 2009 to June 2018), the growth in pension liabilities still outpaced the growth in asset values.
From a $8.7B surplus (7/1/2008) to a $29.8B deficit (7/1/2018), the actuarial rate of return was 7.7% and assets returned 5.8% (11-yrs, from FY 2008 to 2018)

The funding deficit has continued to increase and stands at $29.8B as of July 1, 2018
Projected Median Unfunded Actuarial Liability Will Nearly Double Over the Next 15 Years

Overstating future investment returns will suppress current contributions in the short-term at the expense of ballooning future debt and weakening long-term funding.

*Source Aon Hewitt, using projected MV of assets*
Projected Median Funded Ratio is Expected to Decline Over the Next 15 Years

Source: Aon Hewitt, using projected MV of assets
• Relative to historical actuarial return assumptions, the Pension Plan’s performance is mixed.
A Significant Number of Public Pension Plans Have Lowered Their Actuarial Return Assumptions Since Fiscal Year 2010

- It is the consensus view among actuaries and investment consulting firms that forward-looking returns are expected to be substantially lower than in the past.
- SBA is expecting a 6.6% forward looking (30-yr) asset return assumption
Florida’s Contribution Rates Continue to Be Significantly Lower Than Other States

When employees started contributing 3%, employers’ composite contribution rate was lowered by more than 3%

Source: NASRA (National Association of State Retirement Administrators)
Since the Default Change Went into Effect, A Dramatic Shift in New Participant Elections

A significantly lower number of new hires going into the Pension Plan will accelerate the FRS Pension Plan’s maturity and net cash outflows
Increasing cash outflows adds additional complexity in managing the FRS Pension Plan’s assets.

A maturing plan with increasing cash flows needs will necessitate an asset allocation change to less risky and more liquid assets, thereby, lowering future return expectations.
The SBA has experienced significant growth since the depth of the “Great Financial Crisis”

Despite the significant growth in assets and strong performance, pension liabilities continue to outpace the growth in asset values

Funded status is expected to decline and the unfunded actuarial liability is expected to double over the next 15 years

SBA is projecting a long-term return assumption of 6.6%

Overstating future investment returns will suppress current contributions at the expense of ballooning future debt and weakening long-term funding

Actuarial Assumption Conference should continue to decrease the expected return assumption consistent with independent forward-looking return expectations, which are significantly lower than historical expectations
Florida’s employer and employee contribution rates are significantly lower than other states

A dramatic change in new hire DB/DC election rates, accelerating DB plan maturity and net cash outflows will eventually necessitate a less risky and more liquid asset allocation, thereby, lowering future return expectations

Intergenerational transfer of pension costs to future taxpayers