

PENSION MANAGEMENT RESEARCH PANEL

Quick Poll: The Top 10 Priorities for Pension Plan Sponsors in 2010

In January 2010, the **Pension Management Research Panel** conducted a Quick Poll asking executives to identify their organization's top ten pension priorities for the year. The poll was completed by 54 executives overseeing pensions ranging from US \$250 million to US \$10 billion in assets. None of the poll respondents were from institutional clients of SEI. The poll asked respondents to identify priorities for the year and then to rank them as a "marginal," "high" or "extremely high" priorities. The results were tabulated using a weighted system giving one point for a marginal priority, two for high and three for extremely high. The ranking of priorities is listed below.

On which priorities will executives at pension plan sponsors be spending their time this year?

1. Controlling funded status volatility

Recent industry reports suggest that a significant gain in assets during 2009 helped pension funding levels improve by 8 to 10 percent, finishing the year on average at around 78 percent funded¹. This follows 2008 in which plans saw an average decrease in funded status of 21 percent². The ongoing volatility in the capital markets and interest rates continues to result in funded status volatility, and plan sponsors will continue to be challenged in controlling this critical component of pension financial management. This concern is reflected in the poll results as a total of 91 percent of all respondents identified it as a priority. A third (33 percent) of all respondents said this was an "extremely high" priority, by far the highest percentage to do so for any priority in the poll.

2. Improving plan's funded status

While controlling the volatility of funded status is the highest priority, improving the plan's funding level follows close behind. As asset levels rose last year, discount rates decreased resulting in an increase in liabilities, thus offsetting some of those gains. The result was that despite strong equity markets for much of 2009, the improvement in funded status of many plans was not completely correlated and plan sponsors are still trying to make up the deficits. Almost all of those polled (90 percent) identified developing a strategy for improving the funded status as a priority in 2010, with more than two thirds (71 percent) saying it was at least a "high" priority.

3. Providing senior management or Board with a long-term pension strategy

As underfunded pension plans continue to impact overall corporate finances, companies are experiencing increased scrutiny from analysts, investors, creditors and other users of financial statements. In response, senior management and Boards are demanding that those overseeing pensions develop a comprehensive long-term strategy that can be effectively communicated to these key audiences. More than 90 percent said this was a priority and more than half (60 percent) of poll participants said it was at least a "high" priority in 2010.

4. Effectively managing duration moving forward

Duration is the measure of price sensitivity for a change in yield for both assets and liabilities. A mismatch between the duration of the plan's assets with the duration of the plan's liabilities can result in a significant swing in the plan's funded status. Effectively managing duration can protect the plan's funded status as assets and liabilities move in correlation to one another. This is a complex process and most (84 percent) identified this as a priority in 2010.

¹ Towers Watson – "Strong Market Returns Boost Funding Levels of Fortune 1000 DB Plans for 2009" (January, 2010)

² Standard & Poor's – "Funding Levels Fall, Credit Pressures" (June 2009)

5. Conducting an asset-liability study

Asset-liability studies can help plan sponsors by providing funding and investment strategies that help mitigate overall risk around the plan's funded status. The complicated actuarial connection that links assets and liabilities can be the most challenging aspect in overseeing a defined benefit plan, so asset-liability studies are conducted to provide insight around managing asset volatility towards the appropriate liabilities. Three quarters (75 percent) said this was a priority in 2010 and nearly half (48 percent) said this was a "high" priority in 2010.

6. Implementing a Liability-Driven Investing (LDI) approach using long-duration bonds

Historically, some of the popular tools used in LDI portfolios have been increased allocation of fixed income, use of long-duration bonds, and use of interest-rate swaps. Long-duration bond strategies continue to be viable options in the current market environment because bond and liability values are similarly sensitive to interest rates and move in tandem. Nearly two thirds of those polled (64 percent) said that implementing LDI using long duration bonds was a priority versus only 34 percent that said implementing LDI with interest rate swaps was a priority.

7. Stress-testing the portfolio to gauge its ability to withstand extreme macroeconomic environments

According to industry research conducted in December 2009, nearly three quarters (73 percent) of pension plans did not run stress tests at that time³. One reason for the lack of stress testing is that plan sponsors do not always have access to the necessary simulation tools to conduct a stress test. As part of an overall focus on risk management, plan sponsors are now looking for investment management providers capable of providing valuable portfolio construction advice based on stress testing. More than three quarters (78 percent) of poll respondents said stress-testing the portfolio was a priority in 2010.

8. Evaluating a different approach for investment management

The ongoing investment volatility of the past 18 months has changed what organizations are looking for in their investment management process. Today, they seek increased transparency, a goals-based approach to portfolio construction and investments managed in conjunction with liabilities. Pension-related focus is shifting towards limiting the plan's impact on corporate finance, risk management and long-term strategies, which is causing nearly two thirds (65 percent) of poll respondents to evaluate a different approach for investment management.

9. Changing funding policies and timelines

As pension plan sponsors continue to implement the new funding rules in the Pension Protection Act (PPA), the risks continue to become more difficult to manage. Plan sponsors need to be more strategic in developing their funding policies and timelines to address these risks, as making only minimum contributions can have a potentially drastic impact. More than two thirds (68 percent) said this was a priority in 2010.

10. Defining fiduciary responsibilities for trustees and investment consultants

As funding and accounting rule changes have increased external scrutiny of pensions, plan sponsors are becoming increasingly sensitive towards investment consultant conflicts, such as when they are paid as consultants and also paid by the funds they recommend. In response, plan sponsors are questioning to what extent consultants are actually plan fiduciaries compared to the plan's trustees. Fiduciary status is based on the functions performed for the plan, not just the person's title or role. Nearly half (48 percent) of the poll participants are focused on defining these functions and finding an accountable partner willing to execute them.

If you have any questions or comments about the results of this poll, please feel free to contact us via email at SEIRESEARCH@SEIC.COM or by phone at 1-866-680-8027.

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³ MSCI Barra – "The Future of Market Risk Management" (December 2009)