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## Pension Plans Had a Great Year, But Retirees Likely Won't Benefit From It.

***One good investment year isn’t enough to fix struggling systems’ problems.***

Public pension plans are reporting double-digit investment returns, and some are even finishing with record highs this year.

The high earnings are due to a robust stock market and are welcome news after two straight years of below-average returns for most pension plans. But finance experts say the investment boost likely won’t translate into an equally impressive reduction in pension debt because of the increasing cost of pensions.

“Government contributions tend to be insufficient to reduce unfunded liabilities — even if the plans meet their target,” says Tom Aaron, vice president and senior analyst at Moody’s Investors Service.

Pension plans rely heavily on investment earnings because annual payments from current employees and governments aren’t enough to cover yearly payouts to retirees. As it stands, roughly 80 cents on every dollar paid out to retirees comes from investment income.

The average annual investment earnings target for pension plans is 7.4 percent. By Aaron’s calculations, pension plans would need investment returns of nearly 11 percent to prevent unfunded liabilities from growing.

Many plans are actually on track to beat that lofty figure this year, reporting returns between 10 and 14 percent, according to a Governing analysis. But it’s becoming much harder for pension plans to gain ground than to lose it.

For example in 2016, low investment earnings prompted the average funding ratio of pension plans — which refers to how much money is set aside to meet obligations to retirees — to slide down 5 points to 68 percent funded, according to Boston College’s Center for Retirement Research. Meanwhile, the positive returns this year have the center projecting an average funding increase of only 3 percentage points.

Aaron and the center attribute this difficulty to the fact that governments are not paying enough into pensions in the first place.

Obviously, a plan’s fiscal health can make it even more difficult to play catch-up.

That’s been the case in Chicago. Its municipal employees’ $4.3 billion pension fund last year had just 19 percent of the assets it needed to meet all its liabilities. It reported an impressive 12.4 percent investment gain, but those earnings weren’t nearly enough to make up for the pension payments going out of the fund. In the end, its asset level actually dropped by about $31 million, which means its funded status likely won’t improve.

It doesn’t help, Aaron says, that Chicago retirees nearly outnumber the active workers still paying into their pensions. “That’s the absolute worst time to be underfunded because you have this negative cash flow dynamic going on,” he says, “so that makes the plan even more susceptible to volatility.”

On the other hand, New York state’s pension fund, which is nearly 94 percent funded and earned an 11.4 percent return on investments, saw its total assets increase to a record high $192 billion — a boost of more than $13 billion over the prior year’s balance even after making payouts.

Many pension systems are seeking to remedy their funding issues by lowering their investment targets. In the short-term, that would increase a plan’s overall liability, which would make them appear worse off — even after a year of good returns.

But over time, that would increase governments’ annual pension payments, which is better for a system’s long-term fiscal health.

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BY LIZ FARMER | AUGUST 3, 2017