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Fitch: US Public Pension Market Volatility Exposure Remains High

Fitch Ratings-New York-03 November 2025: Robust market valuations in recent years have supported funding progress for U.S. state and local defined benefit pension plans. However, public pensions remain underfunded and fundamentally exposed to market volatility. A market shock could increase the burden of state and local pension liabilities and drive contributions higher, says Fitch Ratings. Governments with weaker liability metrics and high carrying cost burdens could be most vulnerable to rating pressure.

Post-global financial crisis, plan sponsors took various policy actions such as reducing benefits to new employees, using more conservative actuarial assumptions and discount rates, and increasing contributions. This helped stabilize plans and support funding improvement. But other trends, including higher allocations to alternative investments and steady demographic weakening, could amplify the effects of a market shock.

According to the Public Plan Database, alternative investments outside of traditional equity, fixed income and cash were 34% of pension portfolios in fiscal 2024, double the fiscal 2008 level. Allocations to increasingly complex categories of alternatives can include leverage or variable rate strategies that expose investors, including pensions, to greater losses. Many of these alternatives have not yet been tested in a downturn. The illiquidity of many alternative investments could also force plans with tighter cash flows to sell marketable assets at a loss to meet benefit or other obligations, such as capital calls.

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