Retirement News Highlights

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Cash rate scenario analysis drives asset allocation reset at Maryland

By Amanda White
top1000funds.com
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The asset allocation of the $63 billion Maryland State Retirement and Pension System is "better than a 60:40" protecting the fund on the downside. But now CIO Andrew Palmer is looking at the allocation in the context of cash rates persistently at 4 per cent, what that means for various asset classes and how the fund should be allocating accordingly.

The asset allocation of the $63 billion Maryland State Retirement and Pension System "is working" according to its chief investment officer Andrew Palmer with the fund producing a relatively good year of returns despite the market conditions.

The fund's asset allocation is "better than a 60:40" according to Palmer with the asset mix specifically protecting the fund on the downside.

The long-term strategic asset allocation is 34 per cent public equities, 21 per cent rate sensitive assets, 16 per cent private equity, 8 per cent credit/debt strategies, 15 per cent real assets, and 6 per cent absolute return, designed to produce greater protection during short-term market volatility.

In fiscal year 2022 the portfolio returned -2.97 per cent, net of fees, which was well below the 6.80 per cent assumed actuarial return rate but ahead of the plan's policy benchmark of -3.48 per cent.

"Returns relative to risks are very good. That's what we are aiming for. We can always get higher returns by taking more risk," says Palmer in an interview with Top1000funds.com.

"The high allocation to private markets has worked well over the past year, although with recovering public markets it's holding us back a bit this year."

The fund continues to tweak its allocations and is making some changes around the edges, including winding back allocations to emerging markets and bond protection over the next year or so.

Emerging markets has made up about 7.5 per cent of the total public equities allocation, and an asset allocation discussion in February specifically focused on China.

"When we made our move into emerging markets, China was a small part of that allocation now China is 40 per cent of EM equities," Palmer says, adding that after an evaluation of the return expectations the fund has decided to wind back emerging markets and a lot of that is due to the outlook for China.

“Among EM we think China will have a lower return expectation than the rest of emerging market and developed market stocks and we think we should have a premium for investing in China equities,” he says.

The adjustment over the next two years will rebalance towards US equities (6-10 per cent).

“We think returns are broadly higher respectively in public markets now, so we can move back to less risky stocks,” Palmer says.

BIGGEST RISKS IN THE PORTFOLIO

While Palmer is clear that any investment decisions are based on risk /return assessments and not politics, he is aware of the geopolitical risks to the portfolio.

“The biggest thing we should be advocating for is China and the US to figure out their differences,” he says. “Biden and McCarthy need to figure out the debt negotiations and then China and the US need to respect each others’ sovereignty and look at the bigger things they can work together on, such as climate change, and partner together to be more impactful. This will take a reset.”

As part of a recent risk assessment of the portfolio by a large investment bank, scenario analysis looked at the impact of an invasion of Taiwan by China and the possible US reaction to that.

“With a Ukraine-like reaction by the US we would see a fall in the portfolio of 8 per cent immediately,” Palmer says. “If we reduce our exposure to China from 10 to 5 per cent then we can reduce that to a 7.5 per cent loss. There is so much interconnectivity because of the impact on global growth and inflation, the interruption to global trade is orders of magnitude bigger than Russia.”

Scenario analysis of various risks is a contributor to asset allocation changes for the fund and Palmer also points to climate risk analysis as a driver of the decrease in the absolute returns portfolio and an increase in infrastructure and natural resources a few years ago.

In 2015 when Palmer joined the fund as CIO the absolute returns allocation was 16 per cent, now it’s down to 6 per cent.

“A couple of years ago we shifted the absolute returns portfolio from 8 to 6 per cent and moved it into natural resources and infrastructure. The return scheme is diversifying but not sensitive to inflation and we wanted to add inflation sensitivity,” he says, adding he is still worried about inflation.

“After the financial crisis the central banks were fighting against deflation and fiscal stimulus that ended up driving the inflationary impulse. We are going to have a similar problem on the other side, to get inflation back down. It will be hard for them to get it materially lower,” he says. “The Fed has done a fair amount and needs to let it work a little bit. They were late to this, they should have been tightening when the government was stimulating.”

Recognising that all asset class teams do things differently when it comes to climate risk, one of the key projects at the fund is to coordinate efforts across asset classes to drive more effective practice.

Using the Alladin risk system to evaluate risks and build functionality to identify, reduce, and hedge climate risks Maryland is also incorporating an engagement program by first identifying the most effective places to engage.

“The focus for the next year or so is to build that out,” Palmer says.

Looking forward from a top-down perspective, the team is assessing the performance of non-zero cash rates and what that means for the portfolio.

“We are trying to earn 6.8 per cent and if you can earn 4 per cent on cash what does it mean for other asset classes and what should our return hurdles be for those,” Palmer says. “If an infrastructure manager is earning 2 per cent over cash and the money is locked up why is that exciting for us?”

Palmer still sees a lot of value in the private world and a differentiation of investments that can’t be replicated in the public space. But he wants to make sure the tradeoff is clear.

“It really depends on how permanent this non zero cash rate of 3-4 per cent will be,” he says.

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Labor secretary nominee defends ESG rule in tense House testimony

By Brian Croce
Pensions & Investments
June 7, 2023

In a lengthy hearing on Wednesday that focused mainly on the labor market, child labor breaches and worker safety, Julie Su, acting secretary of labor, defended the department's new environmental, social and governance rule.

Rep. Rick Allen, R-Ga., pressed Ms. Su, President Joe Biden's nominee for labor secretary, on the rule, which took effect Jan. 30 and permits retirement plan fiduciaries to consider ESG factors when selecting investments and exercising shareholder rights.

"Our ESG rule did not require financial advisers to do anything in particular," Ms. Su said in testimony before the House Education and the Workforce Committee. "What it did was give them the flexibility."

Congressional Republicans, who as a whole oppose the rule, with help from a handful of Democrats, in the House and Senate on Feb. 28 and March 1, respectively, approved a joint resolution under the Congressional Review Act to nix the Labor Department rule, but Mr. Biden subsequently vetoed the resolution.

Mr. Allen introduced a bill last year with Rep. Andy Barr, R-Ky., similar in scope to a rule finalized late in the Trump administration that said retirement plan fiduciaries could not invest in "non-pecuniary" vehicles that sacrifice investment returns or take on additional risk. Mr. Allen said he's working on reintroducing the bill during this Congress.

Under the Biden administration, the Labor Department rescinded the Trump-era rule.

On Tuesday, Ali Khawar, principal deputy assistant secretary of the Labor Department's Employee Benefits Security Administration, said the rule is neutral and doesn't require consideration of ESG factors when making an investment decision.

But in January, Republican attorneys general from 25 states filed a lawsuit in U.S. District Court in Amarillo, Texas, arguing that the rule undermines key protections for retirement savers, oversteps the department's authority under the Employment Retirement Income Security Act and is arbitrary and capricious.

Separately, Mr. Allen asked Ms. Su about the department's efforts concerning fiduciary investment advice. The Labor Department is currently working on a rule-making initiative that could broaden who's considered a fiduciary under ERISA by amending the regulatory definition of the term fiduciary.

Though Ms. Su did not get into specifics, she said the department will listen to all stakeholders when crafting the rule.

Ms. Su's nomination for labor secretary, which advanced out of the Senate Health, Education, Labor and Pensions Committee in April in an 11-10 party-line vote, is in a precarious place. No Republicans supported her confirmation as deputy labor secretary in 2021, and none are expected to do so this time, which means the vote will be narrow. A vote in the full Senate has not yet been scheduled.

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Dude, Gen X is totally unprepared for retirement, survey finds

By Kerry Hannon·Senior Columnist
yahoo!finance
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For the so-called Slacker Generation, their retirement reality bites.

Just over half of Generation X — born between 1965 and 1980 — have little to nothing socked away for retirement, according to research by Prudential Financial of 2,000 pre-retiree Gen Xers conducted between March 31 to April 6, 2023. Thirty-five percent of the 65 million US Gen Xers have less than $10,000 saved, and 18% have no savings.

The results, echoed in two other recent surveys, reflect the burdens this generation faces and are a big wake-up call — especially for the oldest members who are about a decade from retirement age.

“Gen X is staring at one of the most complex landscapes for retirement readiness in decades,” Prudential Vice Chair Rob Falzon told Yahoo Finance. “Due to the decline in defined benefit pension plans, which often supported previous generations’ retirement, as well as uncertainty about the economy and long-term Social Security benefits.”

‘Gen Xers have less confidence in their financial future’

The Prudential research comes on the heels of the latest study from Allianz Life Insurance Company of North America published last week and Northwestern Mutual's 2023 Planning & Progress Study published in mid-May, both of which raised serious concerns about Gen X's future financial outlook.

It's a trifecta of gloomy news for Gen Xers.

In Allianz's report, 64% of Gen Xers worry they won't have enough saved for retirement, up from 55% in 2021. That's even higher than what the Prudential report clocked and also tops Northwestern Mutual's finding that 55% of Gen Xers say they won't be financially prepared for retirement when the time rolls around.

If that wasn't enough, nearly half believe they could outlive their savings, according to the Northwestern Mutual survey conducted among 2,740 U.S. adults between February 13 and March 2, 2023.

"A notable finding in our report was that Gen Xers have less confidence in their financial futures than other generations," Kelly LaVigne, vice president of Consumer Insights at Allianz Life, told Yahoo Finance.

Overall, only 55% of Gen Xers believe they are better off than previous generations at their age, versus 70% of boomers and 61% of millennials, Allianz found. And 69% of them said they are confident in their ability to financially support all the things they want to do going forward, down from 73% last year and lower than the 76% for millennials and 86% for boomers.

Allianz Life conducted the online survey of 1,000 adults who either had $150,000 or more in investable assets, or incomes of $50,000 a year if single and $75,000 a year if married in February and March of 2023.

Why is Gen X so behind on retirement saving?

While it could be easy to blame apathy or disengagement — characteristics that Gen Xers have often been saddled with by onlookers — there are several underlying economic issues making it harder for this cohort to save.

"The goal for retirement planning is to enjoy today without feeling like you're sacrificing tomorrow's dreams, but Gen X is clearly more anxious than other generations about what lies ahead," Christian Mitchell, chief customer officer at Northwestern Mutual, told Yahoo Finance.

"Many in this generation are simultaneously taking care of kids and aging parents. When so many people count on you, it's easy to deprioritize yourself," he said. "But as their retirement age gets closer, pressure for Gen X builds."

Adding to those responsibilities is higher consumer prices.

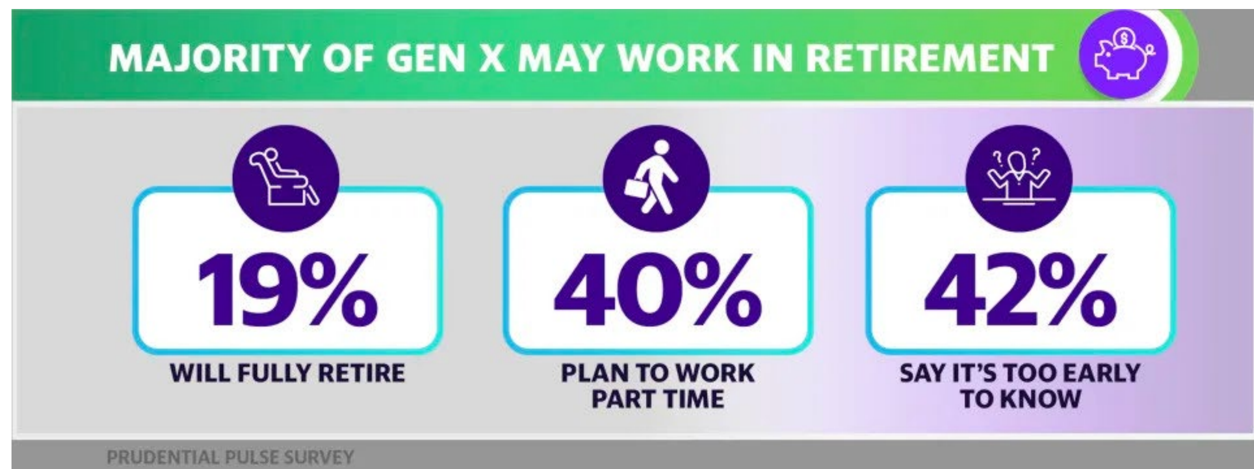
More than two-thirds of working Gen Xers are concerned about reaching their savings goals due to inflation, and nearly three-quarters say the current economic environment makes it hard to plan beyond day to day, according to the Prudential research.

In fact, 67% of those canvassed by Allianz say their income is not keeping up with the rising cost of living, up from 54% just last year.

What do Gen Xers expect in retirement?

Their solution: Almost half (47%) of all working Gen Xers expect to retire later than anticipated to make up for that, and another 2 in 5 plan to work part time after retirement, Prudential reported.

While the Prudential survey found that 58% expect to rely on Social Security as their primary source of retirement income, the Northwestern Mutual one found that just 45% were "very or somewhat confident" that Social Security will be there to support them when they need it.



That makes sense because the current projections are that, if no policy action is taken, the Social Security trust fund reserves will be depleted by 2033 when the oldest Gen Xers hit full retirement age. At that point, Social Security will be able to pay out only 77% of benefits.

Pensions are also a thing of the past. Only 20% of Gen Xers plan to use traditional pensions as a source of retirement income and a tiny 11% say they will mainly rely on a pension, Prudential reports.

"It's a new era we are entering into, where folks are dependent on their defined contributions plans for retirement and very few lucky folks — excluding government employees — have defined benefit plans which they can use in retirement," Tricia Rosen, a certified financial planner with Access Financial Planning in Andover, Mass., told Yahoo Finance.

And while in the past, home equity was often a kitty to fund retirement lifestyles, a slim 16% of Gen X plan to use their home value to support their retirement years.

No financial plan in place

Many Gen Xers also have their heads in the sand when it comes to even focusing on their future.

Although they know they are admittedly not financially in good shape for retirement, nearly half spend no time a week thinking about retirement, according to Prudential's survey, while two-thirds have no retirement strategy, a real sticking point, according to many financial advisors.

"Gen Xers have not taken the time to get a financial plan in place," Barbara Pietrangelo, a certified financial planner with Prudential in Ada, Michigan, told Yahoo Finance. "Those that have a plan tend to feel in a much better place."

But a quarter surveyed by Allianz say "retirement is too far away for me to start worrying about it now," while nearly half say they can't even think about saving for retirement right now and are just trying to take care of day-to-day expenses.

To be fair, it may not be that they are blithely tuning out. There are indications that Gen Xers are, in fact, concerned and they're increasingly cognizant that time is not on their side. Only a quarter of Gen Xers say they have plenty of time to save money for retirement later, down from 43% in 2021, the Allianz Life study found.

"They're starting to reach that critical window in preparing for retirement, which is usually about 10 years before leaving the workforce," Allianz's LaVigne said. "At that point, many people are at a life stage to really focus on retirement –their kids are grown, they are likely making more money, and have already made big purchases like a home. This is the time when many people can really start buckling down."

It can start by taking action and simply setting goals, then prioritizing those goals, and reviewing regularly, Pietrangelo added. Maxing out retirement plan contributions — including catch-up ones when they hit 50 — is also imperative.

The Prudential survey found that many Gen Xers are taking steps, with 56% saving 10% or more of their income, 40% upping retirement contributions, and 86% adjusting their lifestyle so they can save more.

"The bottom line is this: While time to plan is running out, there is still time to act," Mitchell said. "The data represents an opportunity for Gen X to mobilize and get organized."

Kerry Hannon is a Senior Reporter and Columnist at Yahoo Finance. She is a workplace futurist, a career and retirement strategist and the author of 14 books, including "In Control at 50+: How to Succeed in The New Work of Work" and "Never Too Old To Get Rich." Follow her on Twitter @kerryhannon.

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