

# Direction

A Quarterly Review of a Model MEPP's Funded Status

## Q1 2020 Pension Plan Experience

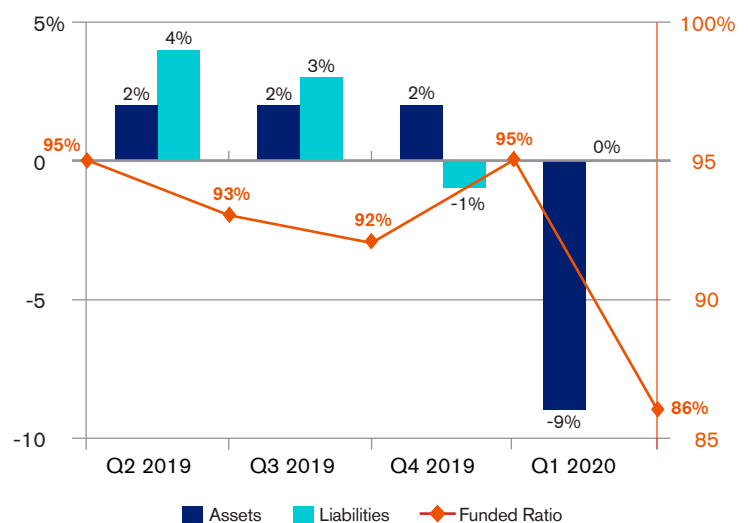
### Funded status of model MEPP falls in Q1 due to investment loss resulting from COVID-19

During the first quarter (Q1) of 2020, the funded status of Segal model multi-employer pension plan (MEPP) dropped from 95 percent to 86 percent, driven by the loss on assets influenced by the COVID-19 outbreak as illustrated by the line in Graph 1.

Graph 2 shows the movement in the benchmark discount rate over the past three years. The discount rate increased slightly by approximately five basis points in Q1 compared to Q4.

The benchmark discount rate varies based on the asset mix of a plan. The model plan's allocation is 55 percent equity and 45 percent bonds. A plan with a higher equity allocation would have had a higher benchmark discount rate and vice versa.

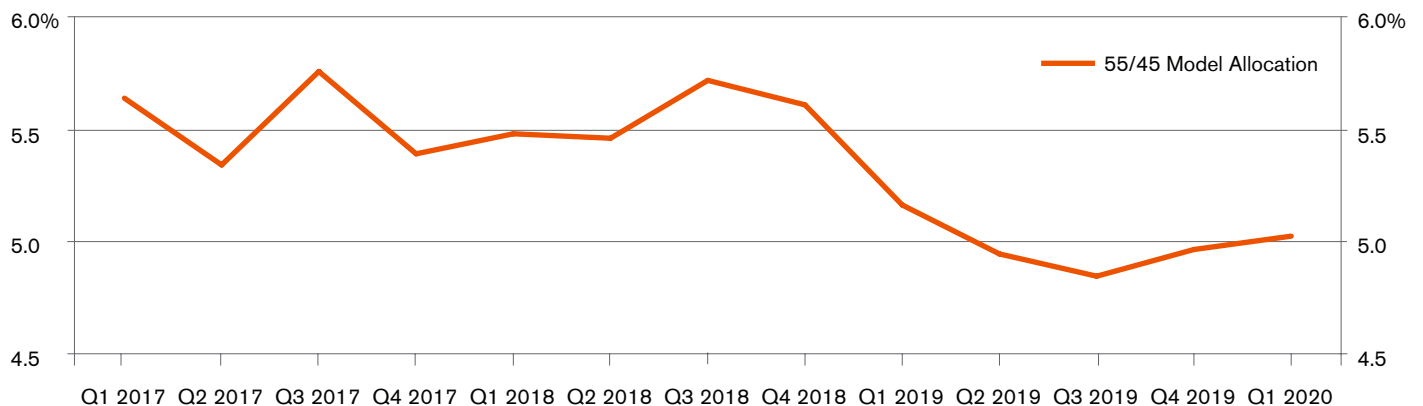
Graph 1: Change in Assets,<sup>1</sup> Liabilities and Funded Ratio<sup>2</sup>



<sup>1</sup> The model MEPP's portfolio has a simple, passively invested asset allocation of 25 percent to domestic equities, 15 percent to U.S. equities, 15 percent to international equities and 45 percent to Canadian bonds.  
<sup>2</sup> This is the ratio of a defined benefit (DB) plan's assets to accrued liabilities. The graph shows the funded ratio at the end of each quarter. The funded percentage for the model MEPP was set to 100 percent as of January 1, 2016.

Source: Segal, 2020

Graph 2: Benchmark Discount Rate<sup>1</sup>



<sup>1</sup> The benchmark discount rate as defined by the Target Benefit Regulations in Alberta and British Columbia. It is composed of long-term Government of Canada bonds and Canadian corporate bond yields.

Source: Segal, 2020

## Investment highlights

Graph 3 illustrates investment performance for the last three quarters of 2019 as well as Q1 of 2020.

During Q1, these were the key factors affecting investment performance:

- Spread of the COVID-19 pandemic that led to shutdown or reduction of most industrial production in developed countries
- High unemployment straining government spending, health of the financial system and people's daily life and personal wealth
- Start of the Saudi-Russian oil price war threatening countries, like Canada, that have high oil production costs, and the future of the U.S. shale oil and gas industry

Note that because MEPPs typically use asset smoothing, market fluctuations may not immediately alter a plan's financial position, but may do so over time.

## Employment level by industry

Year over year, there was a dramatic decline in hours worked in all industries, as shown in the table below.

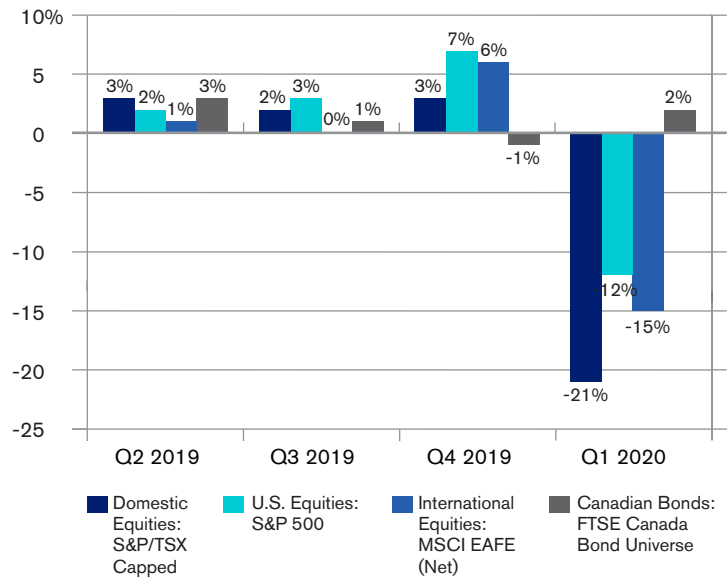
Change in the hours worked may alter the cost of a plan. A reduction in the hours worked will affect the plan's ability to cover fixed costs. This risk is magnified when a plan is dependent upon future contributions to pay down its unfunded benefit obligations.

### Percentage Change in Hours Worked, by Industry, Q1 2019–Q1 2020

|                              |        |
|------------------------------|--------|
| Construction                 | -10.7% |
| Manufacturing                | -7.4%  |
| Transportation & Warehousing | -13.0% |
| Utilities                    | -3.3%  |
| Wholesale & Retail Trade     | -12.8% |
| All Industries Combined      | -14.0% |

Source: Statistics Canada, CANSIM table 282-0092

## Graph 3: Investment Performance



Source: Investment Metrics, 2020

## Important: examine your own plan's experience and assumptions

*Direction* is designed to raise awareness of the risks MEPPs face. Trustees should examine changes in their own plan's assets, liabilities, funded ratio and employment level.\* [Segal](#) can help boards of trustees to project their MEPP's funded ratio through [asset-liability modeling \(ALM\)](#) and assist in [developing funding strategies](#) to achieve the desired funding targets.

\* Individual plan results will differ from this model for a host of reasons, including different funded positions, liability duration and contribution margin.

For details about how we can help trustees manage their plan through ALM, funding-strategy development and other services, or if you have questions about *Direction*, contact your Segal consultant or one of the following experts:

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