RESEARCH BRIEF

The State of Pensions 2024 | October Update

The Hidden Cost of Pension Debt Paralysis

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EQUABLE

The State of Pensions Remains Fragile in 2024.

The funded status of public retirement systems in the U.S. has continued improving as of September 30, 2024 — thanks both to strong financial market performance and record high contribution rates. However, there are similarly strong negative pressures on public plans that has blunted funded status improvement. Among those negative pressures are steadily growing benefit payments resulting in record high negative cash flow combined with over 1 in 5 public plans contributing less than the interest accumulating on their existing unfunded liabilities. The net result is a nearly 6 percentage point increase to the national average funded status that hovers at a fragile 81%.

To put this in context, consider that after investment returns of nearly 25% in 2021 the national average funded ratio had improved to 83.9%. If public plans had been able to steadily grow from there, then they would be approaching around 90% average funded ratios today. Instead, public plans then suffered sharp losses, strong gains again, and some flat performance as well. The fiscal fragility of those pension funds mas meant unfunded liabilities today are projected to be hundreds of billions higher than at the end of 2021. The unfortunate reality is that public plans are stuck in pension debt paralysis.

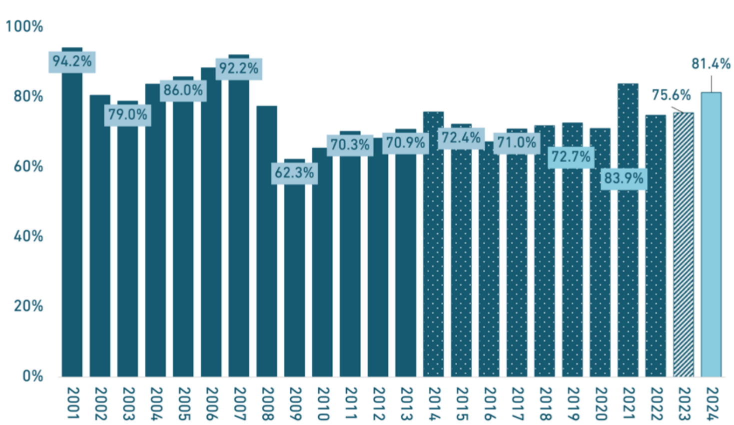
The good news is that there is a pathway out of this fragility for public plans. The bad news is that pathway requires contribution rates to rise even further than their record highs today — and/or for states to increase supplemental contributions into their funds at rates even greater than previous years.

State policymakers won't want to keep putting dollars toward paying down pension debt, but reliance solely on market performance isn't a realistic strategy. Over the past fiscal year public equity indices have reached all time-highs, fixed-income and real estate benchmark performance has been exceptional, and private capital returns have reported yields higher than public markets. The results are investment returns averaging over 9.5%—and if that's not enough to provide a breakthrough from pension debt paralysis, it is unreasonable to future returns on their own can restore funded status reliance. Additional pension contributions are simply an unavoidable necessity for the future.

The national funded ratio average is projected to increase from 75.6% in 2023 to 81.4% in 2024.

Investment returns in 2024 have been strong for plans with a June 30 fiscal year end, and even stronger for those ending in September. The average return among the 121 plans that have reported a complete fiscal year return as of June 30, is 9.8%. Our projected return for plans with September fiscal year ends is 14.4%. If financial markets continue growing this year, we expect the 2024 funded status to further improve by December.

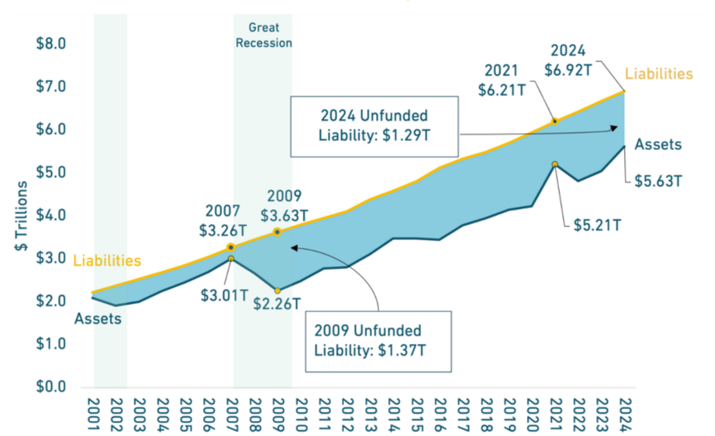
FUNDED RATIO AVERAGE
FOR STATE & LOCAL PENSION PLANS | 2001-2023 + 2024 Estimate



The total pension funding shortfall will decline to $1.29 trillion in 2024, down from $1.63 trillion in total unfunded liabilities in 2023.

Unfunded liabilities are down in 2024 from the previous year, but remain over $288 billion higher than at their recent low point of around $1 trillion at the end of 2021. The good news is that the total funding shortfall this year is lower than the $1.37 trillion in unfunded liabilities at the end of the financial crisis.

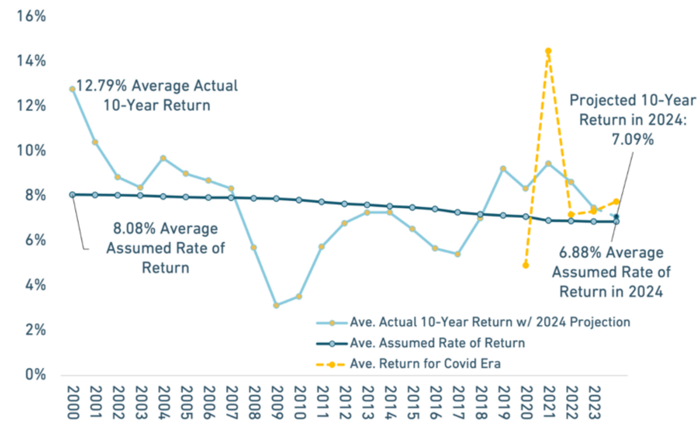
TOTAL UNFUNDED LIABILITIES
FOR STATE & LOCAL PENSION PLANS | 2001-2023 + 2024 Estimate



A 9.5% average investment return for the 2024 fiscal year has helped the funded status of public plans improve.

Preliminary 2024 investment returns (for data reported as of September 30) show a 9.5% return on average for state and local plans. Out of the 125 plans who have reported actual returns for fiscal year 2024, 120 of them beat their assumed return target (averaging 6.9% nationally).

INVESTMENT RETURN AVERAGES
COMPARED TO ASSUMED RATES OF RETURN | 2001-2024

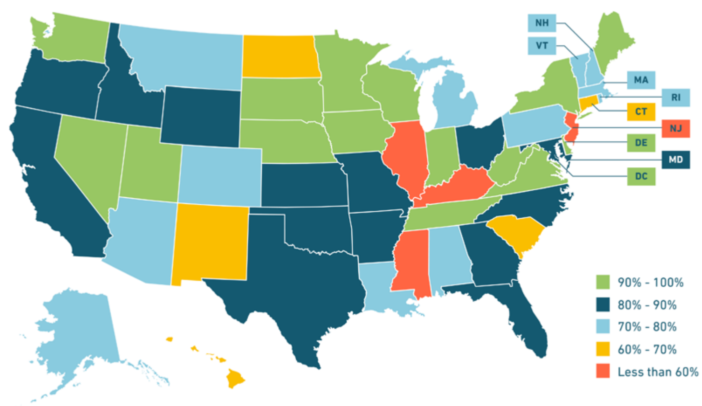


While average returns beat expectations this year, the rolling 10-year average return continued to decline. The 10-year average is just over 7%, slightly better than the current average assumed return. We anticipated this trend last year (see our 2023 October Update) after assessing the look back period. A similar analysis suggests that next year will see an improvement in the 10-year average if annual returns are above expectations.

A majority of U.S. state and municipal pension plans are distressed or fragile.

Within the states, funded ratios and unfunded liability levels continue to vary considerably from state to state. The vast majority of plans have a Fragile (90% to 60%) or Distressed (60% or less) funded status. There are 16 states where the average funded ratio is Resilient (90% or higher), while 31 states have a Fragile funded status and 4 states are Distressed.

2024 ESTIMATED FUNDED RATIOS BY STATE BASED ON ESTIMATED ASSETS FOR STATE & LOCAL PENSION PLANS



Note: *The funded status of a pension plan is not the only benchmark of fiscal health. It is also important consider the reasonableness of actuarial assumptions and funding policies, the size of contribution rates as share of state budgets, and cash flows (among other factors).*

How This Update Changes Our Findings for State and Local Pension Plans:

- The average 2024 estimated rate of return shifted from 7.4% to 9.5% after factoring in reported preliminary returns and updated private equity data for the second quarter of 2024.
- The average 2024 estimated funded ratio shifted from 80.6% to 81.4% based on updated return data.
- The total 2024 unfunded liability *estimate* shifted from $1.34 trillion to $1.29 trillion based on updated data.
- The average 2023 *actual* funded ratio shifted from 75.8% to 75.6% based on additional reported plan data.
- The total 2023 *actual* unfunded liability reported shifted from $1.61 trillion to $1.63 trillion based additional reported plan data.

To read more about State of Pensions visit Equable.org/StateofPensions2024

WHAT IS INCLUDED IN THIS UPDATE?

When we published State of Pensions in July 2024, there were still 42 state or local retirement systems that had not released data for the fiscal year ending 2023. These plans amounted to 12.0% of anticipated accrued liabilities for 2023. Further, our July report relied in part on estimated investment returns using benchmarks for the various reported asset classes that pension funds were using as of 2023.

Over the last three months several retirement systems have released new and updated data, including preliminary investment return reports. This October 2024 fact sheet uses those reports to includes the following:

- Updated 2023 actual financial data, including the addition of actuarial valuation report data from 27 retirement systems. There are still outstanding 2023 reports from nine plans across seven state systems (CalPERS, Massachusetts SERS, Massachusetts TRS, Michigan PSERS, Michigan Municipal, Nevada PERS, and Pennsylvania Municipal) and six municipal systems (Atlanta ERS, Atlanta Police, Atlanta Fire, Boston Employees, Boston Teachers, and Dallas PFRS).

- Updated 2024 estimates use preliminary investment returns from retirement systems, pension fund trusts, and state treasurer or comptroller offices. As of this update, 73 (29.8%) of the 245 retirement systems in the available data have reported preliminary returns for their full fiscal 2024 and those are used to estimate their 2024 assets. In addition, another 54 plans (22.0%) have reported a preliminary asset total as of the close of fiscal 2024. For the remaining retirement systems included, 44 plans (18.0%) have reported partial investment returns during the 2024 fiscal year, meaning our estimate combines partial year preliminary actual returns and benchmarks. Another 42 plans (17.1%) have reported preliminary assets through part of the 2024 fiscal year, meaning our estimate combines partial year preliminary assets with benchmark returns. The remaining 32 plans (13.1%) have not reported any investment performance or preliminary asset totals for fiscal 2024, meaning that their estimates are based entirely on market benchmarks and their respective asset allocations.

The Equable Public Retirement Research Database includes 253 retirement plans; however, data were insufficient to include eight of these plans in State of Pensions analysis because of delayed reporting.

ABOUT STATE OF PENSIONS

State of Pensions is Equable Institute's annual report on the status of statewide public pension systems, put into a historic context. Governments face a wide range of challenges in general – and some of the largest are growing, and often unpredictable, pension costs. State of Pensions analyzes trends in public pension funding, investments, contributions, cash flows, and benefits for 245 of the largest statewide and municipal retirement systems in all 50 states to illuminate the scale and effects of these challenges. Click here to access previous editions of State of Pensions, as well as additional data and resources.

ABOUT EQUABLE INSTITUTE

Equable Institute is a bipartisan nonprofit that works with public retirement system stakeholders to solve complex pension funding challenges with data-driven solutions.

ABOUT THE AUTHORS

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