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Macro Roundup Artcile

Headline: The Risks from State and Local Government Employee Pension Plans: A Stochastic Simulation Analysis

Article Link: https://www.aei.org/research-products/working-paper/the-risks-from-state-and-local-government-employee-pension-plans-a-stochastic-simulation-analysis/

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Tweet: Mark Warshawsky simulates the performance of government pensions based on the past ten-year history of bond and stock returns. At the 25th percentile of historical returns, few plans are fully funded, and many are below 50% funding. @AEIecon

Summary: Most state and local governments provide defined benefit (DB) pension retirement plans to their employees. A traditional measure of the funded status and hence the security of a pension plan is its funded ratio, that is, the ratio of assets to liability. Using a 2022 database of 187 large pension plans, basic plan features and conditions, actuarial relationships, simple economic projections, and varied bond and stock investment returns based on past ten-year historical periods in the US and the current asset allocation of the plans, I create a risk model. This risk assessment is denominated as the range of reasonably possible future actuarial funded ratios and amounts of indicated employer contributions across plans, when investment performance is poor but within historical experience. Several plans would be at or near insolvency, about 11 percent of plans would see very large drops in funded status, while employer contributions would, on average, double, and for about one in seven plans, triple. At the 25th percentile, shown in Exhibit 5, the modal projected funded ratio is around 75%, the liability-weighted mean is 72%, few plans are fully funded, and a substantial segment is below 50% funding, with a few showing severely worsening funded ratios.

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Primary Topic: Government Spending

Topics: Academic paper, Database, Fiscal Policy, Government Spending, Politics

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