Workshop

February 18, 2015

ITEM NAME: Workshop – Funding Risk and Risk Mitigation Strategy

PROGRAM: Actuarial, Investment, and Financial Offices

ITEM TYPE: Information

EXECUTIVE SUMMARY

This workshop will provide an overview of the funding risks faced in the funding of the Public Employees Retirement System, how these risks are changing, and introduce several concepts that can be applied to mitigate the risks outlined. In addition, the workshop will engage the board in a discussion of these risk mitigation concepts and seek guidance from the board regarding the strategy.

STRATEGIC PLAN

This agenda item supports Strategic Plan Goal A – to improve the long-term pension and health benefit sustainability. It specifically addresses the objective to fund the system through an integrated view of pension assets and liabilities.

BACKGROUND

At the November 2014 Finance and Administration Committee meeting staff presented the board with the third annual report on Funding Levels and Risk. As detailed in the report, public pension plans at CalPERS have been maturing. This maturation combined with expected investment volatility will produce substantial contribution volatility. In addition, there remains a significant probability that plans will suffer a large decrease to their funded status. These current risk levels have provided the impetus to educate and address how employers and other stakeholders can manage and mitigate risk through a series of presentations and workshops.

As part of the November presentation, staff promised to bring to the board further analysis on options to mitigate the risks outlined in the report.

ANALYSIS

Reducing the risk in the funding of the system will be difficult because it will involve tradeoffs between short and long-term considerations. In an attempt to balance these tradeoffs, this workshop will present several risk mitigation concepts that can be used individually or in combination. The strategy under consideration includes the following concepts:

- Optional additional contributions – encouraging employers to pay down their unfunded liability more quickly

- De-risking – lower the expected investment volatility either systematically, following a "glide path", or flexibly by lowering the discount rate and expected investment volatility following a great investment return, or the combination of the two for a blended glide path
- Asset allocation choice – provide employers with the ability to choose from one or two additional asset allocations

During the workshop, this strategy will be discussed in further detail including how these concepts could be implemented and their pros and cons. Following that, the board will take part in a discussion with an expert panel to explore the issues and consider next steps.

BUDGET AND FISCAL IMPACTS
Not applicable.

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