Quarterly Pensions Investments Review

Expected Investment Performance - Q3 2023

Introduction

The Quarterly Pensions Investments Review is a comparison in expected risk and return investment.

Key Findings

- Comparing pension funds and regions: North American and UK plans show relatively high expected returns and volatility, compared to mainland Europe.
- Comparing quarter on quarter: expected returns have increased overall, at similar levels of volatility.

If you're interested in learning how your pension fund is performing relative to others, please contact us for more information.

Expected Investment Performance – Risk and Return Results

The charts below show the expected investment return vs. the expected investment risk - from the top 30 largest pension funds per region.

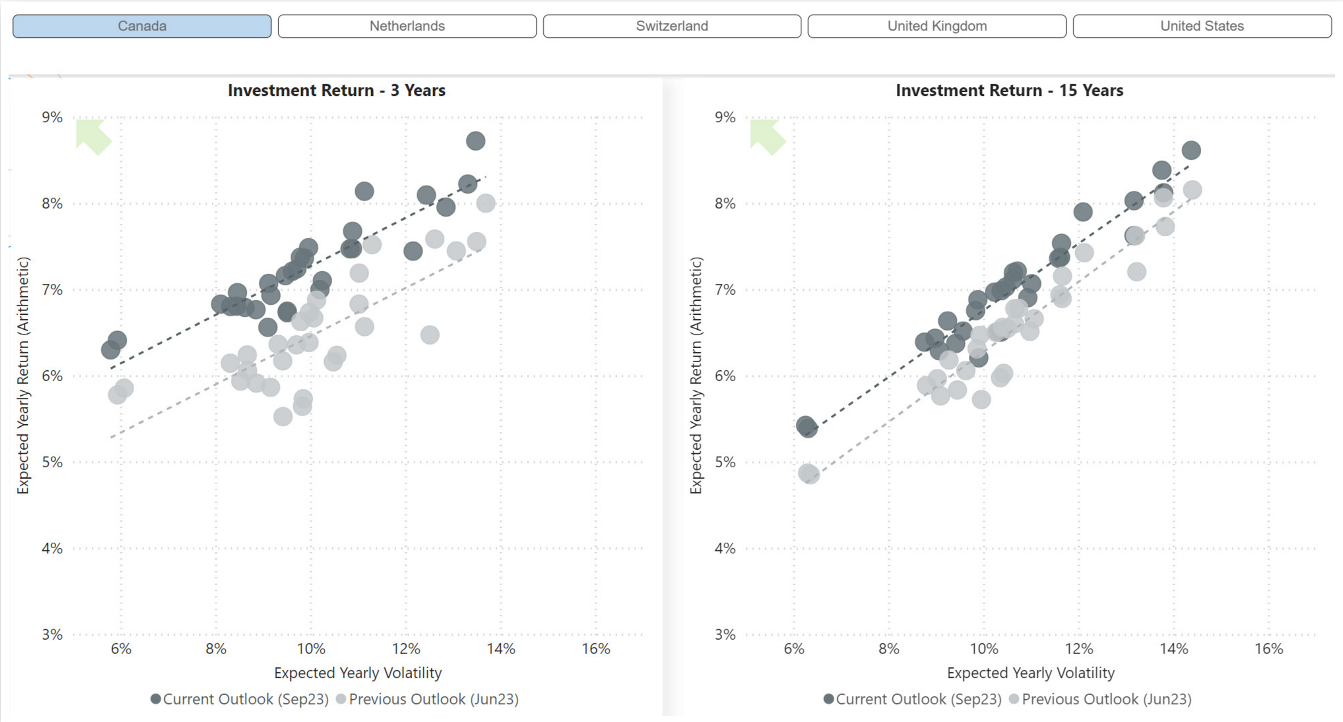
Comparing pension funds and regions

Looking at general trends, the difference in expected returns between regions is stark. This is true for both horizons, but it seems even more pronounced in the short-term. North American and UK plans show relatively high expected returns, while Swiss pension plans target a lower return, in line with their relatively low discount rates. In addition to different asset class allocations, the difference in return is also driven by home biases in combination with generally lower expected returns for mainland Europe.

It's interesting to note that differences in expected risks between countries are much smaller. The UK, especially, seems very efficient. While the risk/return trade-off for Swiss – and to a lesser extent – Dutch pension plans seems unfavorable compared to their counterparts, this is only half of the story. Our analysis focuses only on investment risk and does not assess the match with liabilities. An ALM study would uncover risks in terms of funding ratio and contribution volatility and VaR.

Next quarter we will dive into these differences in more detail.

Comparing quarter on quarter



Comparing the outlook for the end of September versus the end of June, we see a large uptick in expected returns for all regions – especially on the three-year horizon (with the exception of the UK). This is driven by a reversal in equity momentum and higher interest rates.

During the third quarter, capital markets adjusted to "higher for longer" interest rates. Long rates increased by roughly 75bps in the US and 50bps in Germany, causing high duration government bonds to severely underperform. Most developed market equities declined in the face of tightening financial conditions and the surge in oil prices, registering their first negative quarter of 2023. Emerging market equities also declined amid concerns of Chinese economic activity and renewed stress in property markets. The exceptions were the energy-heavy UK equity index which benefited from higher oil prices and Japanese equities supported by yen weakness boosting exports.

June's negative equity momentum expectation largely materialized, following disappointing equity returns in Q3. Consequently, the September momentum outlook significantly improved by about 5% compared to end-of-June, reflecting realized equity losses and declining headline inflation. Equity momentum is expected to be relatively flat over the next twelve months, balancing above-trend interest rates and upward pressure from short-term equity reversal effects. The momentum outlook remains clouded by elevated volatility and downside risk due to tight financial conditions and elevated geopolitical tensions.

Where the improved equity momentum outlook has a profound impact on the shorter-term expected returns, the "higher for longer" interest rates help boost expected returns in the long run as fixed income delivers higher carry.

Subscibe to receive the next quarterly update

Methodology and assumptions

This analysis is based on publicly available data, such as investment policy statements and annual reports, from the top 30 largest pension funds in Canada, the Netherlands, Switzerland, the UK, and the US.

The projections are made with GLASS Ortec Finance's GLASS, a forward-looking Asset-Liability Management platform for institutional investors. Plan modeling is based on strategic asset allocations, mapped to public and private benchmarks, and rebalanced annually. For simplicity, active hedging strategies and derivatives are not included in the Quarterly Pension Review.

Returns shown are gross of management fees and expressed in the local currency of the relevant country.

The projections in this analysis are driven by the Ortec Finance Economic Scenario Generator.

Ortec Finance is a leading global provider of technology and solutions for risk and return management, enabling you to manage your investment decisions.

More information?

If you have any questions regarding this information please get in touch with Elwin Molenbroek or Drazen Pesjak via the contact details below.

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