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"A Summary of CRR Research on Public Pension Investments"

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Distinguished Members of the Commission,

Thank you for allowing me to speak today about the recent research completed by me and my colleagues at the Center for Retirement Research at Boston College (CRR). It is my sincere hope that the research will further inform the pension discourse in the Commonwealth.

My presentation today will summarize the results of two recent CRR briefs focused on public pension investment performance broadly. Assessments of Pennsylvania State Employees Retirement System (SERS) or Public School Employees Retirement System (PSERS) will be limited to high-level comparisons of SERS and PSERS to a broad universe of public pension plans. For those interested in making comparisons that are more detailed, the CRR has released a beta version of its Public Pension Investment Comparison Tool (http://crr.bc.edu/special-projects/public-plans-investment-comparison-tool-beta/). Currently, the tool allows users to compare a single plan's asset allocation and performance (for the total portfolio and individual asset classes) to a broad universe of plans or a selected sub-group of plans.

Below are links to the two briefs that I will be discussing today, with bullets of the key takeaways. Broadly, the briefs assessed plan performance in two ways – by comparing the long-term returns across plans and by comparing the long-term returns of plans to their own benchmarks. Both approaches found that alternative investments have had a meaningful, and mostly negative, impact on performance.

What Explains Differences in Public Pension Returns Since 2001?
(http://crr.bc.edu/briefs/what-explains-differences-in-public-pension-returns-since-2001/)

- Average investment returns for state and local pension plans varied over 2001-2016 from 6.3 percent for the top quartile to 4.6 percent for the bottom.
- The observed variation in returns accounts for much of the difference in today's funded levels.
- The analysis found that asset allocation – in equities, fixed income, and alternatives – was broadly similar across plans, while asset class returns showed more variation.
- Therefore, asset class returns – not allocation – turned out to be the primary reason for the disparities in overall returns.
- However, allocation played some role for the worst performing plans: in the wake of the 2008-2009 financial, they made a dramatic shift out of equities and into alternatives – specifically, hedge funds and commodities – during a period when these asset classes underperformed others.

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How Do Fees Affect Plans' Ability to Beat Their Benchmarks?
(http://crr.bc.edu/briefs/how-do-fees-affect-plans-ability-to-beat-their-benchmarks/)

- One way that public pension plans assess their investment performance is to compare returns by asset class to selected benchmarks.
- Plans pay fees to external asset managers with the expectation that they will exceed the benchmarks.
- As these fees have come under greater scrutiny, the question is whether higher fees help plans outperform their benchmarks.
- The analysis, using new data for 2011-2016, found that plans that paid higher fees experienced worse performance relative to their benchmarks.
- This finding held across all major asset classes, but was particularly pronounced for alternative assets, such as private equity and hedge funds.

The research briefs described above rely on data from the Public Plans Database (PPD) (http://publicplansdata.org/). The PPD is a comprehensive database containing data from 2001 to 2017 on the actuarial funded levels, pension fund cash flows, investments, and membership of 180 major state and local pension plans – making up over 95 percent of all state and local pension assets and members. Importantly for members of this commission, the PPD contains detailed data – sourced mostly from plan CAFRs – on asset allocation, target allocation, returns by asset class, and benchmark returns for each asset class. I hope that Commission members will consider the PPD a resource as they continue their deliberations.