$20 billion club

Strong equity returns overcome sharp discount rate drops in 2020 to push average funded ratio to its highest level since 2013

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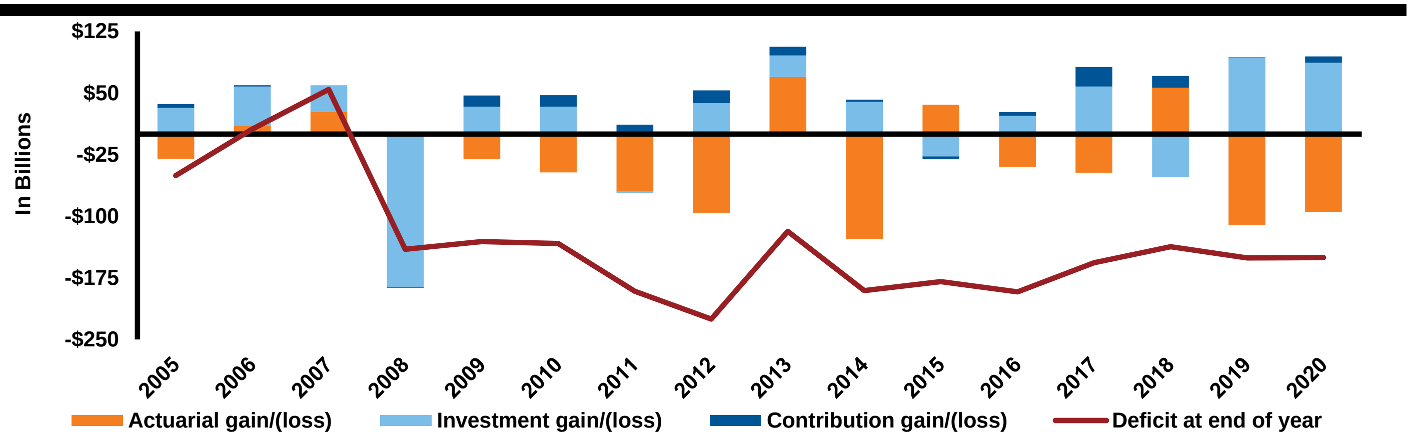
With the onset of the COVID-19 pandemic, 2020 was tumultuous year in the financial markets. Global equities fell by over 30%, the 10-year treasury rate dipped to 0.51%, and spreads expanded to their highest levels in years. DB plan sponsors are only required to disclose their funded position once per year, but for those tracking it daily or even monthly, it was a turbulent ride. In the end, like in 2019, equity markets soared and discount rates dropped. But unlike 2019, for these 19 U.S.-listed companies with the largest corporate DB pension liabilities, this led to *improved* average funded ratio, which is **now at its highest level since 2013**. Global equities returned 17% in 2020 while discount rates fell around 70 bps, leading to an improvement of average funded ratio in this group from 84.9% to 86.2%. The funding deficit in dollar terms decreased slightly from $151 billion to $150 billion.

We follow this select group of listed companies since they offer an up-to-date snapshot of the corporate pension industry, and they help set the stage for the future. Their approach to benefit, funding and investment strategy trailblazed much of what we are seeing in the broader industry. They tend to have the scale and resources to innovate and think creatively, setting trends that many other DB sponsors will eventually follow.

Exhibit 1 illustrates funded status experience for this group since 2005. The red line shows the dollar surplus or deficit, with the bars indicating the key change drivers in each year. You will notice parallel images of 2019 and 2020. Actuarial losses increased the deficit in both years, with investment gains offsetting this effect. This pattern is similar to 2017 and most other years since 2015.

Exhibit 1: Combined surplus/(deficit) of the $20 billion club, 2005-2020[1]



Keeping up its pattern for another year, these plan sponsors have not experienced a gain from both investment returns and actuarial gains (usually rising discount rates) since 2013, and only once since 2007.

Contributions ticked up in 2020 from long-term lows in 2019, with the help of a significant contribution of company stock by Boeing. The outlook for 2021 contributions, meanwhile, is quite low, with very few firms committing to any discretionary contributions.

Investment gains offset most of the actuarial losses, which were driven by a ~70bps decrease in discount rates.

The average increase in funded ratio among these sponsors was 1.2%. There was wide variation, however, as both Boeing, GE and Pfizer saw improvements of nearly 4% with the help of discretionary contributions. Meanwhile, UPS fell nearly 5%, in large part due to updated estimates on pension benefits due for the Central States Pension fund. Honeywell remained the only sponsor in the group with a global funded ratio above 100%.

Overall pension liabilities continued to climb due to lower discount rates and new benefit accruals, with combined liabilities for this group exceeding $1 trillion for the first time. Combined assets also rose to their highest levels, topping $900 billion.

Exhibit 2 shows how liabilities and assets performed during 2020.

Exhibit 2: 2020 global pension assets and liabilities development

LIABILITIES	(IN $BILLIONS)
Liability (Projected Benefit Obligation) at Start of Year	981.0
Accrual of new benefits (Service Cost)	11.9
Benefits paid	-53.5
Interest payable on liability (Interest Cost)	26.4
Impact of change in interest rates and in actuarial assumptions (Actuarial loss)	94.5
Miscellaneous other	-8.1
Liability (Projected Benefit Obligation) at End of Year	1,052.2

ASSETS	(IN $BILLIONS)
Assets (Fair Value) at Start of Year	830.2
Employer contributions	19.8
Benefits paid	-52.6
Investment return on plan assets	113.0
Miscellaneous other	-8.5
Assets (Fair Value) at End of Year	901.9

SURPLUS / (DEFICIT)	(IN $BILLIONS)
Excess (Shortfall) of assets below liabilities at Start of Year	-150.8
Excess of employer contributions over service cost	7.9
Actuarial gain (loss)	-94.5
Investment return less interest cost	86.6
Miscellaneous other	0.5
Excess (Shortfall) of assets below liabilities at End of Year	-150.3

Source: Corporate 10-K Filings, Russell Investments

2020 contributions get a boost after 2019 lows, but 2021 contributions could be the lowest in 15 years

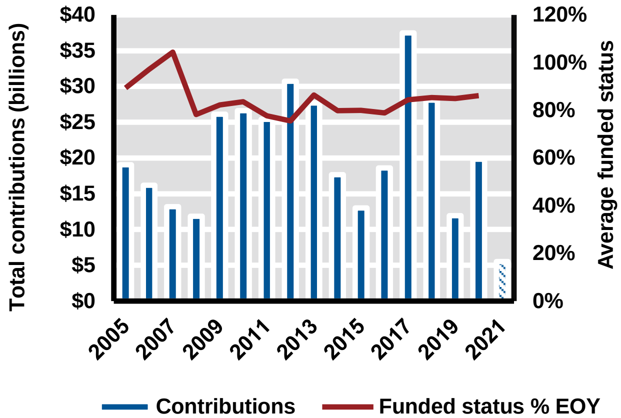
These sponsors tried to maximize tax deductions in advance of imminent tax changes in 2017 and 2018, contributing over $65 billion in those two years. While 2020 contributions were up to $19.8 billion from the $11.9 billion in 2019, 2021 contributions may be the lowest in over 15 years at $5-6 billion, as sponsors are hesitant to commit discretionary contributions with the future, uncertain state of the pandemic.

In addition, the prospect of corporate tax rates rising under the Biden administration may also be leading sponsors to wait for a larger tax deduction by contributing later.

Moreover, with pension funding stabilization still in place and perhaps being extended, few sponsors have significant required contributions in their U.S. plans.

Exhibit 3 shows the pattern for contributions since 2005, including an estimated value for 2021 as disclosed in financial reporting.[2]

Exhibit 3: Contributions 2005-2021



GE, GM and Lockheed Martin purchase annuities, Johnson & Johnson changes their benefits

GE continued with its journey to fund up and de-risk its plan. This time offloading $1.7 billion in retiree liability, after cashing out billions more in 2019.

GM disclosed that they purchased annuities for salaried retirees in Canada at a cost of $1.5 billion.

For the third year in a row, **Lockheed Martin** transferred liabilities out of the plan, again with a combination of buy-out/buy-in transactions totaling $2.2 billion, as they work to reduce the size of their U.S. pension plans.

Johnson & Johnson reduced their benefit obligations by $1.8 billion by changing the benefit formula (to "Retirement Value") for all non-union employees starting in 2026.

Membership of the $20 billion club

The $20 billion club consists of the following 19 corporations, generally included due to their global pension liabilities exceeding $20 billion:

1. 3M
2. AT&T
3. Boeing
4. Corteva
5. Dow Chemical
6. Exxon Mobil
7. FedEx
8. Ford Motor
9. General Electric
10. General Motors
11. Honeywell International
12. IBM
13. Johnson & Johnson
14. Lockheed Martin
15. Northrop Grumman
16. Pfizer
17. Raytheon Technologies
18. United Parcel Service
19. Verizon Communications

These are no longer the only U.S.-listed corporations with over $20 billion in liabilities. Merck, Exelon, Caterpillar, Citigroup, Delta Air Lines, Bank of America, PG&E and Chevron all now exceed $20 billion in global pension liabilities, with more added every year rates drop. Observations and comparisons are more straightforward when the group is consistent, however, so for now we have chosen to maintain a fairly steady group from year-to-year.

While future adjustments are possible, for the time being the only change we have made is the inclusion of Raytheon Technologies, the product of the Raytheon + United Technologies merger in 2020 (both predecessor firms have been part of this group since its inception).

[1] Source: Russell Investments, Corporate 10-k filings

[2] This is the sum of all the individual companies expected 2021 contributions.

Related reading

Owens, J (2020). “20 billion club: Liabilities and assets peaked in 2019 and funded status continues to stagnate”

Owens, J (2020). “$20 billion club: Assets and liabilities peak again while contributions plunge in another record-breaking year”, *Russell Investments Blog*, February 29, 2020

Owens, J (2019). “$20 billion club: Equity downturn in Q4 nearly overshadows higher discount rates and strong contributions in 2018”, *Russell Investments*

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Owens, J (2019). “Better late than never…GE pension risk in focus”, *Russell Investments Blog*, October 28, 2019

Field, A (2019). “$20 billion club strategy”, *Russell Investments*, March 2019

Owens, J. (2018). “Tax Reform has been signed – what could this mean for DB plan sponsors?”, *Russell Investments Blog*, January 3

Owens, J. (2018). “Record-breaking contributions and returns for $20 billion club”, *Russell Investments Blog*, February 28

Owens, J. (2018). “20 billion club posts record contributions in 2017 as funded status jumps”, *Russell Investments*

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