DB/Cash Balance Investment Allocation Guidelines

Do you want to add more defined benefit (DB) plans to your block of business? The first step is educating yourself on these unique plans. Grow your practice with this helpful education and an easy investment solution to help you meet your investment objectives.

DB Investment Allocation

The investment allocation of a DB plan, whether a traditional pension plan or cash balance plan, should be set according to the liability and/or objective (e.g., crediting rate in the case of cash balance plans) and a function of the promised benefits. Risk should only be taken to fund the benefit, hence matching the objective with the appropriate risk level/asset allocation model is critical.

Traditional DB Factors

Funded status – The ratio of the plan's assets to liabilities (PBO). The PBO can typically be found in the plan's most recent actuarial report or provided on request by the plan's actuary.
Guideline *– The greater the funded status, the more conservative the plan's allocation should be to fixed income or "liability hedging assets." If the plan is funded well enough to pay current and future benefits, there is no reason or strong rationale to accept more risk around this benefit stream than necessary. A suggested weighting across equity/alternatives and fixed income is shown below:*

Traditional DB Factors (continued)

Return seeking assets – Generally equity-focused, but may include other asset classes to increase return and/or lower portfolio risk.

Liability hedging assets – Typically credit-focused, but may include other asset classes to increase return and/or lower portfolio risk.

Open (going concern) vs. closed/frozen plans – The glidepath for closed plans typically derisks at a higher rate as you close the funding gap. This is due to the closing date and known cash flows.

Time horizon – Frozen or closed plans need to be more conservative since the liabilities are finite and of a shorter duration than as compared to a going concern (existing perpetually).

***Guideline** – Frozen or closed plans should be positioned more conservatively, with fixed income assets closely approximating the duration of the liability.*

Balance sheet volatility – The plan liability is reflected on the company's balance sheet. An asset mix that is invested in long-duration fixed income (hedging) assets will track the liability to a greater extent, limiting the surplus/shortfall that will be experienced.

***Guideline** – a more conservative allocation, with the fixed income allocation closely approximating the duration of the plan's liabilities, will help reduce balance sheet volatility*

Cash Balance Plans

Crediting rate – This is the guaranteed rate credited to participants on an annual basis. This rate can help drive the allocation decision in addition to the costs to run the plan (i.e., if the plan's crediting rate is 5% and the costs/fees to run the plan are approximately 1%, then the target return for portfolio would be 6%)

***Guideline** – The crediting rate and/or expected rate of return will help drive the allocation policy. The higher the targeted rate of return, the more aggressive the asset allocation.*

Funded status – The ratio of the plan's assets to liabilities (PBO)

***Guideline** – The greater the funded status, the more conservative the plan's allocation should be to fixed income or "liability hedging assets"*

Traditional DB Investment Strategy

LDI Glidepath Guidelines (closed)

Funded Status (PBO)	Return Seeking	Liability Hedging	% weight / flexPATH portfolio	% Core Bond Fund (Lord Abbett)
>115	0	100	0	100
110-115	0-2.5	97.5-100	5 / flexPATH Index+ Conservative Retirement	95
105-110	0-5	95-100	10 / flexPATH Index+ Conservative Retirement	90
100-105	5-10	90-95	20 / flexPATH Index+ Conservative Retirement	80
95-100	10-20	80-90	35 / flexPATH Index+ Conservative Retirement	65
90-95	20-35	65-80	100 / flexPATH Index+ Conservative Retirement	0
85-90	35-50	50-65	100 / flexPATH Index+ Moderate Retirement	0
80-85	50-65	35-50	100 / flexPATH Index+ Aggressive Retirement	0
75-80	60-70	30-40	100 / flexPATH Index+ Conservative 2035	0
70-75	65-80	20-35	100 / flexPATH Index+ Aggressive 2025	0
65-70	70-80	20-30	100 / flexPATH Index+ Moderate 2035	0
<65	75-85	15-25	100 / flexPATH Index+ Moderate 2035	0

LDI Glidepath Guidelines (open)

Funded Status (PBO)	Return Seeking	Liability Hedging	% weight / flexPATH portfolio	% Core Bond Fund (Lord Abbett)
115-120	0-10	90-100	10 / flexPATH Index+ Conservative Retirement	90
110-115	5-15	85-95	20 / flexPATH Index+ Conservative Retirement	80
105-110	10-20	80-90	40 / flexPATH Index+ Conservative Retirement	60
100-105	15-25	75-85	65 / flexPATH Index+ Conservative Retirement	35
95-100	20-30	70-80	70 / flexPATH Index+ Conservative Retirement	30
90-95	25-35	65-75	100 / flexPATH Index+ Conservative Retirement	0
85-90	35-50	50-65	100 / flexPATH Index+ Moderate Retirement	0
80-85	50-65	35-50	100 / flexPATH Index+ Aggressive Retirement	0
75-80	60-75	30-40	100 / flexPATH Index+ Conservative 2035	0
70-75	65-80	20-35	100 / flexPATH Index+ Aggressive 2025	0
65-70	70-80	20-30	100 / flexPATH Index+ Moderate 2035	0
<65	75-85	15-25	100 / flexPATH Index+ Moderate 2045	0

If the plan is utilizing another custodian/recordkeeper, a long credit fund, if available, may be used for 50 percent of the core bond allocation to better match a longer duration liability.

RPAG CITs for an Optimal Portfolio

Using RPAG's capital market assumptions, the return targets below can be met with a corresponding RPAG CIT (or multiple where applicable). These return targets are assessed annually by the RPAG Investment Committee and are subject to change.

Additionally, flexPATH's custodian, Wilmington Trust, is offering RPAG members an exclusive discounted rate for custodial services!

Return Target	Fund
4-5%	flexPATH Index+ Moderate Retirement R1
5-6%	flexPATH Index+ Moderate 2025 R1
6-7%	flexPATH Index+ Moderate 2035 R1
7-8%	flexPATH Index+ Moderate 2045 R1

For more information on RPAG's exclusive CITs, please contact RPAG support at 877.360.2480 or support@rpag.com.