STRS report for the STRS Board, March 2019.

Investment Returns

STRS investment returns followed fairly closely the assumed rate of return in CY 2018 until October, when it started falling behind. Losses in December caused the CY 2018 return to be 1.75%, a loss to the system of $6.3 B compared to what the assumed rate of return would have delivered.

STRS investments continue to do well, compared to other public funds. In CY 2018, STRS outperformed the benchmark by 0.29% and was in the 11^{th} percentile of Callen's Public Fund Sponsor Database. Someone on the Board asked if it would be worth studying the funds that did better than STRS; it's easy to think the goal is the highest return on investments, but minimizing the risk of a debilitating loss if things turn south is probably a more compelling goal. Compared to the 10^{th} percentile (from the top) of such funds, STRS had a return on investment of:

Last year	Last 3 years	Last 5 years	Last 7 years	Last 10 years
-0.21%	-0.01%	+0.48%	+0.28%	-0.02%

Financial Plans

There was discussion at the February STRS Board meeting on funding objectives. While some members continue to advocate for a return of COLAs, the Board's primary goal is "to safeguard members' benefits in the long term." **The Board is less concerned with reinstating COLAs than they are in avoiding a third major cut in benefits** (after the 2012 change affecting pensions of new retirees and the employee contribution rate, and the loss of COLAs for retirees in 2017). Intergenerational equity is also a goal, meaning how the pain is shared between active and retired teachers. Initially the previous cuts affected primarily active teachers, but as time goes by the loss of COLAs means that retirees will suffer the greater loss. Robin Rayfield of ORTA made a plea for the Board to agree on what goals needed to be achieved in order for COLAs to be resumed. This the Board was reluctant to do, noting how complex the accounting is; the Board has to balance the ratio of assets to liabilities, how soon this ratio is projected to reach 100%, and consultants' predictions of future investment returns. And when future finances do improve, the Board at that time may not simply reinstate the COLA as it was; they could declare one-time cash bonuses or COLAs for one or more years but not continuing thereafter. Chairman Robert Stein summarized the discussion by saying it's too complex for the Board to adopt guidelines for when current policies will change, plus there's no way for the current Board to commit future Boards to any particular course of action. In the meantime, any change in current policy is likely quite a few years away.

Hanging over financial planners are major sources of uncertainty:

International trade tensions,
Unresolved Brexit,
Protests against reforms in France (especially labor reforms),
Questions of fiscal sustainability in Italy, and
Elections and new governments in many countries (especially Britain).

STRS Data

In their fifth year of teaching, teachers who adopted the Defined Contribution (DC) or Combined Plan can convert their funds to the Defined Benefit (DB) plan, and last year 8% chose to do so, likely because they had decided to make teaching their career.

At the February Board meeting, Saperstein Associates reported on the latest annual phone surveys of active and retired teachers in STRS. Although how they handled some of their statistics was on the dubious side, the message was surprisingly clear that cuts in the pension formula and loss of COLAs have not greatly affected the opinion of STRS held by both actives and retirees. Retirees' overall impressions of STRS held steady, with 95% having a very favorable or somewhat favorable opinion. The percentage of retirees who felt that their pension benefits were an excellent or good value over the last three years were 84%, 86%, and 77% respectively; this question had the largest drop that might be attributed to the loss of COLAs. Retirees' perceptions of the STRS Board went up over the last year, from 71% very or somewhat favorable in 2017 to 76% in 2018. These trends, however, are likely within the sampling error.

Legislative News

Conflict between teacher and the legislature continues in Kentucky. The teachers called a "sickout" strike in response to a proposed change in how members are elected to the board that oversees the state teachers pension system. Presently 7 of the 11 board members are elected by members in the system, and the proposed changes would have 7 different groups each pick a member (e.g., Kentucky Retired Teachers Association, Kentucky Association of School Superintendents). The legislature is also considering allowing regional colleges and universities to leave the state's pension system and pay off their debt to the system over 25 years, and offer plans such as a 401(k) instead. Actuaries are worried this could make the pension system's financing even worse.

Illinois is considering various financing arrangements to cut the payments the state is scheduled to pay into the pension system, such as floating bonds (they are close to junk status as is) or extending the time to pay off the pension debt by seven years.

PERI is making noises about trying to raise the employer contribution rate for OPERS, which might affect what STRS does. So far I haven't heard STRS say much about this possibility, presumably believing it wouldn't have much chance of passing the legislature.