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Published February 20th, 2019

Public pension plan investment performance continues to lag the financial markets

By Nick Marnell

The portfolios of the organizations that manage the pension plans for Lamorinda public agencies have failed for years to deliver investment returns that match those of a mainstream domestic equity index, putting pressure on the public agencies to make up the investment shortfall out of their local operating budgets.

The Contra Costa County Employees' Retirement Association manages and administers the pension plans for 16 public agencies including the Moraga-Orinda Fire District, the Contra Costa County Fire Protection District and Contra Costa County itself. According to association documents, the CCCERA portfolio market value as of Sept. 30 was $8.8 billion.

Through the third quarter of 2018 the S&P 500, an index that measures domestic equity performance, had risen 10.2 percent, while CCCERA investments rose 2.6 percent. The CCCERA investment performance has lagged the S&P 500 not only for those nine months but for all but two years of this decade, and those were the two years that the index grew only 2 percent.

"It's prudence," said Contra Costa County Supervisor Candace Andersen, a CCCERA board member since 2015. "If the market crashed, everyone's investment would tank."

When the market crashed in 2008, investments did tank - including those in the CCCERA portfolio. The market plunged 37 percent in 2008, and CCCERA investments fell 27 percent.

Gail Strohl, CCCERA chief executive officer, explained that CCCERA's portfolio adheres to the strategic objective of making benefit payments to its members, both those being paid today and those that will be paid far into the future. CCCERA addresses its near-term needs - $430 million in benefits paid in 2017 - by maintaining a portfolio of short-term assets, and provides growth to fund future benefit payments by maintaining a portfolio of long-term assets. "The CCCERA board has adopted this approach as it is likely to result in a smoother return profile over time," Strohl said.

The long-term return may be smoother, but it still lags the market. The S&P 500 rose 12 percent over the past 10 years, while CCCERA investment performance rose 7.8 percent.

The CCCERA investment results surpass those of the largest pension fund in the country - the California Public Employees' Retirement System, which manages the pension plan for the town of Moraga. According to its 2018 Comprehensive Annual Financial Report, CalPERS reports assets with a market value of $345 billion, and the agency has achieved a 10-year return of 5.6 percent, less than half the return of the S&P 500. "CalPERS sets our asset allocation to be mindful of returns and risk, so we can pay pensions for generations," said Megan White, investment operations information officer.

Results reported by the California State Teachers' Retirement System include $224 billion in assets as of June 30, delivering an annual return of 9 percent against the S&P 500 return of 14 percent.

"Overall, the plan assets have not been managed as carefully as they should be," said Jack Weir, president of the Contra Costa Taxpayers Association, a taxpayer advocacy group. "But neither agency has any real interest in fully funding these plans because the plans are guaranteed by the taxpayers."

The S&P 500 measures equity performance and that inherently makes it a risky benchmark, but time has confirmed its long-term stability. According to historical records, the average annualized total return for the S&P 500 over the past 90 years was 9.8 percent. Investing in riskier assets is not unheard of in pension plans, as the Police Officers' Retirement System of Fairfax County, Virginia, has committed to an investment in blockchain technology - bitcoin.

An annual return closer to 9.8 percent on pension plan assets would ease the pressure on local public agencies, which must cough up the difference when their pension plan managers fail to achieve investment goals. CCTA officer Jim Pezzaglia warned that cutbacks to local services will ensue as public agencies struggle to afford these higher payments required to fund their retirement plans. Bruce Burns, superintendent of the Moraga School District, said recently that pension contributions have almost doubled in the last five years, and will continue to grow for the near future. He noted that there is no funding stream to support the increase in pension costs.

"People gloss over this because they can't understand it," Pezzaglia said. "It's a subject that we have to resolve."

Reach the reporter at: nick@lamorindaweekly.com

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