PERSPECTIVES

# The Right Tools for the Job: Managing Pension Risk for Multiemployer Plans

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At the end of 2025, multiemployer plans in the aggregate found themselves in a desirable position. According to Milliman's multiemployer pension funding study for year-end 2025, aggregate funded status for defined benefit plans climbed past the fully funded mark to 103%, an improvement of over 50 percentage points from the trough measured in 2009! The consulting firm's annual study also revealed that 69% of plans are at least 100% funded, with 90% at least 80% funded.[1]

This, of course, is excellent news for plan participants, but many Trustees may be wondering and asking their advisors, "What now?"

Milliman noted that Trustee stewardship, strong asset returns, and the Special Financial Assistance Program—available to a subset of plans that qualified—aided in achieving this funded status milestone.[2] However, the investment strategies that helped plans reach this milestone may not be what keeps them there in the future. As we have seen in the past, funded status can deteriorate quickly. For example, during the Great Financial Crisis, aggregate funded status dropped by approximately 30% from the end of

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[1] Milliman's Multiemployer Pension Funding Study: Year-end 2025.
[2] Milliman.

2007 to the trough in 2009, according to Milliman.[3] Now may be the time to assess the asset allocation and tools to utilize moving forward.

Employing high-quality fixed income securities in an allocation is a helpful start. However, not all these instruments are created equal in the context of maintaining funded status and meeting benefit payments and other expenses into the future. Ultimately, tailoring these bonds to appropriate time horizons allows plans to limit the inherent pricing and reinvestment risk that otherwise comes with investing in fixed income against such obligations.

At the highest level, a defined benefit pension plan effectively is a mechanism by which plan sponsors promise to pay benefits to participants over a certain time horizon. A fixed income security or a bond is also a promise by a borrower to provide a stream of payments to a lender over a set time horizon by way of coupon and maturity payments. In other words, bonds behave much like pension liabilities, which is why these securities are used in strategies to manage risk. Given the inherent nature of a pension, multiemployer plans can use certain fixed income strategies and principles that align with the liability to manage that risk. These strategies are fitting tools that Trustees can put to work in managing a pension plan.

For example, short duration fixed income is quite predictable in terms of the cash flows delivered, but only over an accordingly short time horizon. Over a longer time horizon, reinvestment risk can be significant because the investor doesn't know the level of yields in the future when it's time to reinvest proceeds from maturing bonds. The potential to reinvest at lower yields than before introduces risk. Despite how fixed income or even cash allocations may appear in capital market assumptions that aren't measured with the liability in mind, the risk can be high when measured appropriately.

In a previous paper, we described several strategies or tools that Trustees can employ to better align assets and benefit payments and that are liability-aware. Cash flow matching is one expression of liability-aware investing that constructs a fixed income portfolio designed to match expected benefit payments and expenses. Put another way, the portfolio is comprised of high-quality bonds that generate plan cash inflows (coupons and maturity payments) to match those plan cash outflows (benefits and plan expenses). These portfolios are therefore unique to each plan's expected benefit payment profile, and their primary objective is predictability in meeting plan obligations. Matching asset cash flows to benefit payments promised to participants decreases instability in a plan's funded status and reduces the need to sell investments to fund benefit payments. This can be especially true for maturing plans or plans with a large majority of plan participants in retirement. For example, a cash flow matched portfolio can provide funds for participants already receiving benefits. This allows assets outside this strategy an opportunity to grow for active participants who continue to accrue more each year. Although cash flow matching strategies may provide lower return opportunities compared to other approaches, higher yielding strategies—equities, alternatives, non-investment grade bonds—may reduce the certainty that the priced-in returns are delivered in accordance with the targeted payouts.

None of these statements are intended to suggest that liability-aware strategies leave no room for taking risk. Rather, the idea is that risk should be taken in the intended places—i.e., where an investor is expected to be compensated for taking that risk. By better aligning plan assets to plan benefit payments, economic and contribution risk can be reduced while still maintaining a growth allocation.

In a liability-aware framework, plan assets are only one side of the equation. Another tool or principle that can be used by Trustees is to view future plan obligations in a way that lends itself to risk management strategies. This can be achieved by utilizing a market-aware or market-consistent discount rate to value future benefit payments. This could mean valuing future obligations using an expected rate of return on assets (EROA), regularly updated based on the latest long-term forecasts, or potentially going a step further and discounting based on prevailing market rates (i.e., investment-grade bond yields). The benefit

[3] Milliman.

of this approach is that it provides a more suitable way to consider the plan's assets in the context of the current value of obligations. For example, the magnitude of changes in a plan's liability value is very much a function of the time horizon. Characteristics of the plan liability and changes in its current value can be captured with a more market-aware discounting measure. This then reveals how well-matched the investments are along the time-horizon dimension. With a more static or stable discount rate, capturing the aforementioned changes in the liability present value isn't as readily observable.

Trustees have many tools at their disposal when deciding how to allocate plan assets. With most plans at or above the fully funded mark, Trustees and their advisors are now well positioned to evaluate strategies that preserve funded status. Strategies that align the design of the bond portfolio with the characteristics of the obligation are a recognized means of reducing plan risk and maintaining funded status, and are, quite literally, the right tools for the job.

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