South Dakota Retirement System

SDRS Update for Executive Board of Legislative Research Council

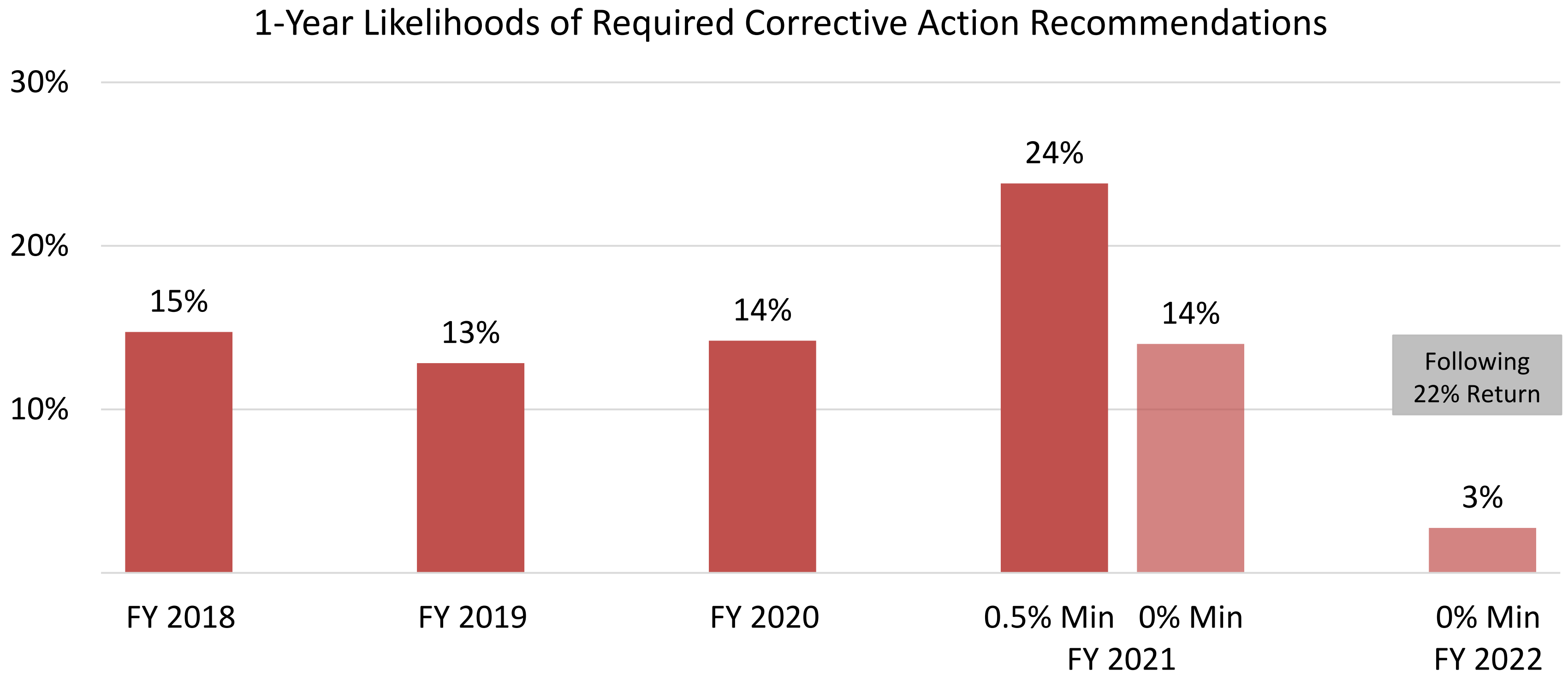
August 31, 2021

June 30, 2021 Projected Funding Results

- SDRS goal is to pay a COLA equal to inflation and to afford the full COLA range (0% to 3.5%):
  - Requires a Baseline Fair Value Funded Ratio (FVFR) of 100% or more
  - Projected baseline FVFR with the full COLA range is 106% at June 30, 2021
  - As a result, full COLA range will likely be affordable
- Fair value of assets support the full COLA range:
  - July 2022 COLA is inflation between 0% and 3.5%
  - CPI-W increase will likely exceed 3.5%
  - **July 2022 COLA will likely be 3.5%,** the highest in SDRS history
- Financial statements of SDRS and employers will reflect **approximately 106% funded status**
- The 2021 SDRS valuation will likely be the 26th of the last 31 with a FVFR of 100% or greater

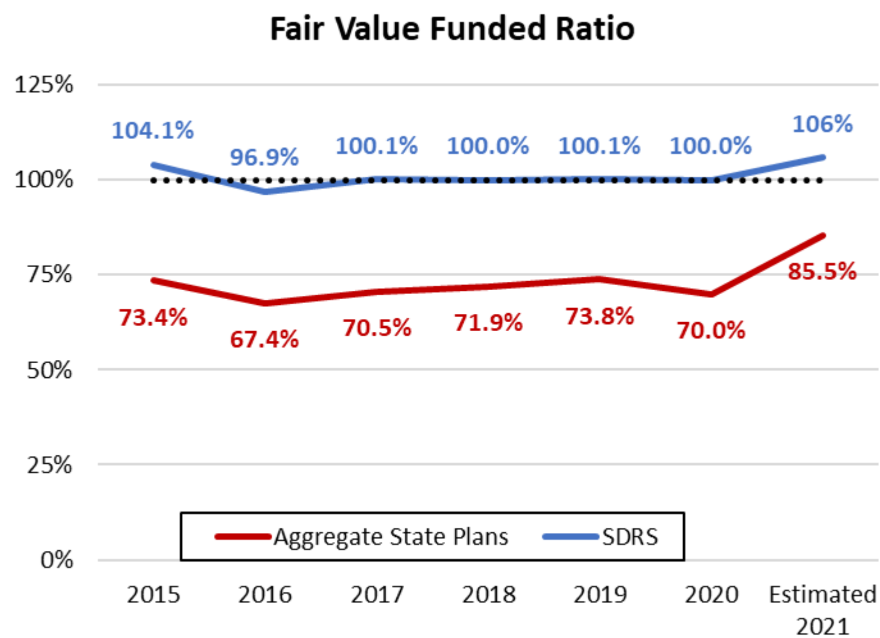
Corrective Action Risk Assessment

Lowering minimum COLA to 0% and favorable investment experience in FY 2021 **reversed recent trend** of increased likelihood of required corrective action recommendations

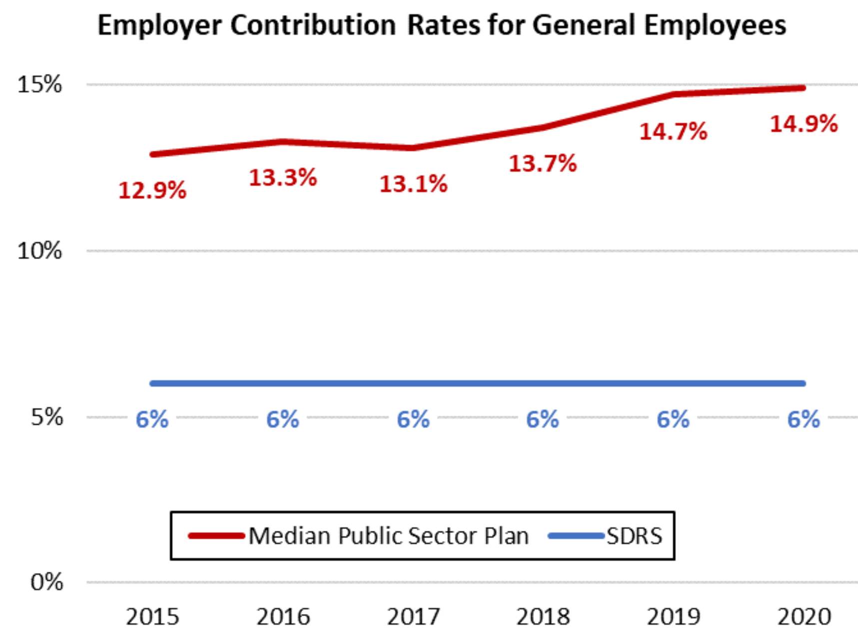


Before consideration of liability gains/losses. Likelihoods based on SDIC **current** asset allocation investment portfolio statistics (FY 2022: mean = 5.30%, standard deviation = 12.3%).

SDRS Funded Status and Contribution Rates Compared to Other State Plans



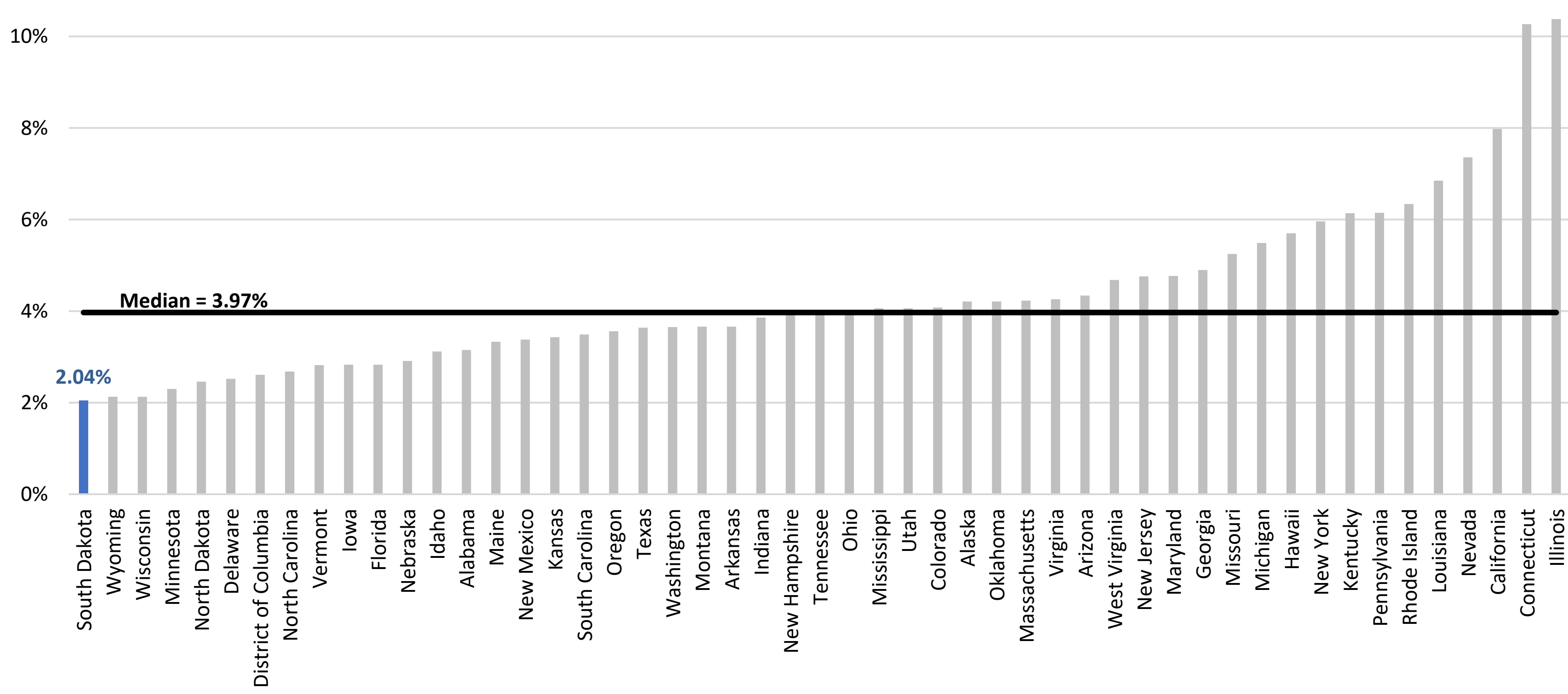
The median investment return assumed by statewide plans has dropped to 7.00%. SDRS assumes 6.5% investment return.



State plan funded ratios are from 2021 Wilshire Consulting Report on State Retirement Systems: Funding Levels and Asset Allocation. Estimated 2021 state plan figure is from 2021 Wilshire estimate released July 21, 2021. Employer contribution rates from NASRA Public Fund Survey, November 2020.

Government Spending on Pensions Comparisons

Government Contributions to Pensions as a Percent of All Direct Government Spending, FY 2018



Data from NASRA Issue Brief: State and Local Government Spending on Public Employee Retirement Systems.

2020 Contingency Planning

- Beginning in December 2019 and throughout 2020, SDRS Board and staff developed emergency plan to withstand more severe economic conditions
  - Benefit improvement policies, history, and issues identified and discussed
  - Numerous potential corrective actions and benefit improvements identified and discussed
  - Committee sought out rating agency perspectives as well as broader guidance on the implications of unfunded liabilities
- Resulting plan finalized at December 2020 Board of Trustees' meeting, including two important initiatives:
  - 2021 Legislation reduced COLA minimum to 0%
  - In extraordinary conditions, Board recommendations may consider permitting small, short-term unfunded liability affordable within fixed, statutory contributions after COLA reduced to 0%
- **Contingency plan provides framework for steps to consider in extreme financial downturn**

Demographic Trends

- The baby boom generation (born from 1946 to 1964) has a significant impact on SDRS demographics:
  - Boomers now 37% of membership
  - 65% of boomers now retired
  - SDRS now has over three retirees for every four active members
- The number of retirements is at an all time high:
  - FY 2021 retirements were at an all time high, approximately 10% more than the prior highest FY 2019
  - The median Class A retirement age had increased to 64.4 in FY 2020, FY 2021 TBD
  - Fewer members are retiring at earlier ages
- Negative cash flow (benefits paid in excess of contributions) is expected and stable
- **All SDRS employers will need to replace a significant portion of employees in upcoming years**

Summary

- SDRS is managed within the resources provided by **fixed contributions**
- SDRS will likely pay a **2022 COLA of 3.5%,** the highest in our history and the estimated funded status as of June 30, 2021 is **106%**, meeting both the retiree inflation protection and funding goals
- Under most economic conditions, SDRS variable benefits will result in full funding, but a severe or prolonged downturn could require Corrective Action recommendations
- SDRS Board contingency planning led to two initiatives that would enhance SDRS sustainability
- Long-term investment performance and commitment to managing liabilities result in a **projected funded status of 106%** – significantly better than most state retirement systems (estimated 85.5% in aggregate)
- Members continue to retire later; however, all employers will need to replace a significant portion of employees in upcoming years