Milliman analysis: Rising rates reduce pension deficit by $34 billion

Discount rate remains below 4% but still drives improvement in August after four consecutive months of declines

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Pension liabilities of the 100 largest corporate defined benefit pension plans fell by $23 billion in August while their corresponding assets improved by $11 billion, bringing the Milliman 100 PFI funded status deficit to $498 billion and a 72.4% funded ratio. Despite the modest improvement, the August 31 funded ratio remains well below its December 31, 2011, value of 78.7%.

HIGHLIGHTS

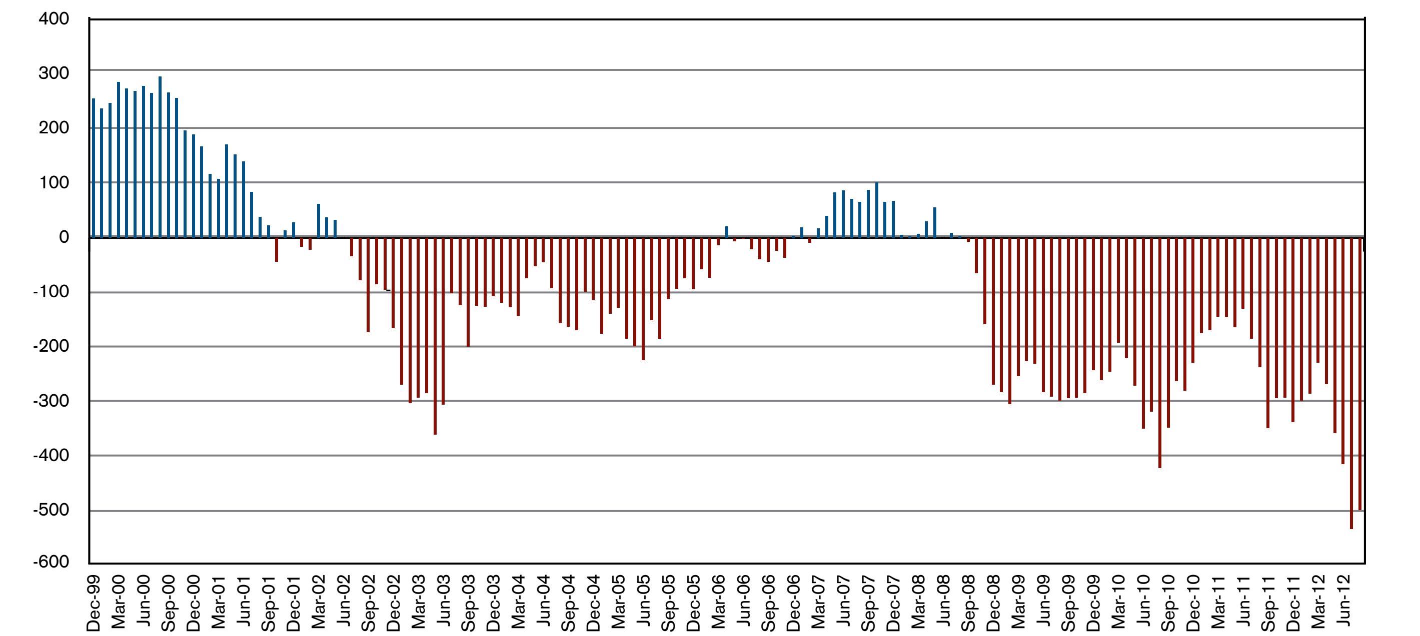
	$ BILLION			
	MV	PBO	FUNDED STATUS	FUNDED PERCENTAGE
JUL 2012	1,298	1,831	(533)	70.9%
AUG 2012	1,309	1,808	(498)	72.4%
MONTHLY CHANGE	+11	(23)	+35	+1.5%
YTD CHANGE	+63	+224	(161)	-6.3%

NOTE: NUMBERS MAY NOT ADD UP PRECISELY DUE TO ROUNDING

August's funded status improvement was primarily due to an increase in corporate bond interest rates, the benchmarks used to value pension liabilities. August's discount rate increase comes after four consecutive months of interest rate declines. In 2012, the discount rate has declined every month other than August and March. As of August 31, the funded ratio climbed to 72.4%, up from 70.9% at the end of July.

The projected benefit obligation (PBO), or pension liabilities, decreased by $23 billion during August, lowering the Milliman 100 PFI value to $1.808 trillion from $1.831 trillion at the end of July 2012. The change resulted from a meager increase of seven basis points in the monthly discount rate to 3.99% for August, from 3.92% for July.

FIGURE 1: MILLIMAN 100 PENSION FUNDING INDEX PENSION SURPLUS/DEFICIT



The Milliman 100 PFI asset value increased by $11 billion during August, raising the Milliman 100 PFI value to $1.309 trillion from $1.298 trillion at the end of July. The increase was due to investment gains of 1.02% for the month. By comparison, the Milliman 2012 Pension Funding Study published in March 2012 reported that the median expected investment return during 2011 was 0.63% (7.80% annualized).

Over the last 12 months (September 2011 – August 2012), the cumulative asset return has been 6.38% while the Milliman 100 PFI funded status has deteriorated by $262 billion. During this time the funded ratio of the Milliman 100 companies dropped to 72.4% from 83.8%. The increase in the pension deficit has been primarily due to the 12-month decline in discount rates to 3.99% from 4.96%.

2012-2013 PROJECTIONS

If the Milliman 100 PFI companies were to achieve an 7.8% median asset return (as per the 2012 pension funding study) expected for their pension plan portfolios and the current discount rate of 3.99% were to be maintained during years 2012 through 2013, we forecast the funded status of the surveyed plans would increase. This would result in a projected pension deficit of $479 billion (funded ratio of 73.6%) by the end of 2012 and a projected pension deficit of $403 billion (funded ratio of 78.0%) by the end of 2013. For purposes of this forecast, we have assumed 2012 aggregate contributions of $67 billion and 2013 aggregate contributions of $81 billion.

Please note that the contribution assumptions have not been adjusted to reflect the potential impact of the Moving Ahead for Progress in the 21st Century Act (MAP-21), which includes pension funding stabilization provisions. While several plan sponsors have announced reduced contributions, we feel that a majority of the Milliman 100 companies will continue to prudently fund the pension deficits in their respective plans and presumably continue with their existing pension de-risking funding strategies rather than lower their contribution level to satisfy minimum standards.

Under an optimistic forecast with rising interest rates (reaching 4.19% by the end of 2012 and 4.79% by the end of 2013) and asset gains (11.8% annual returns), the funded ratio would climb to 77% by the end of 2012 and 95% by the end of 2013. Under a pessimistic forecast with similar interest rate and asset movements (3.79% discount rate at the end of 2012 and 3.19% by the end of 2013 and 3.8% annual returns), the funded ratio would decline to 70% by the end of 2012 and 63% by the end of 2013.

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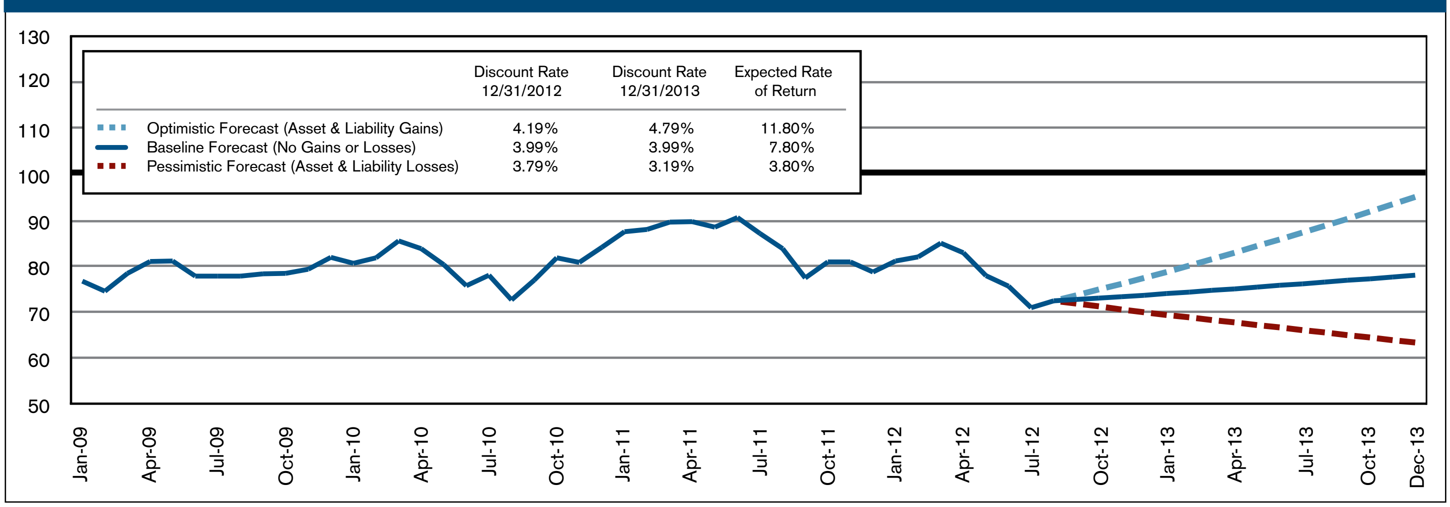
FIGURE 2: MILLIMAN 100 PENSION FUNDING INDEX – PENSION FUNDED RATIO



MILLIMAN 100 PENSION FUNDING INDEX – AUGUST 2012 (ALL DOLLAR AMOUNTS IN MILLIONS)						
END OF MONTH	YEAR	MARKET VALUE OF ASSETS	PROJECTED BENEFIT OBLIGATION (PBO)	FUNDED STATUS	CHANGE IN FUNDED STATUS	FUNDED RATIO
AUGUST	2011	1,222,908	1,459,129	(236,221)	N/A	83.8%
SEPTEMBER	2011	1,192,824	1,540,649	(347,825)	(111,604)	77.4%
OCTOBER	2011	1,241,510	1,534,408	(292,898)	54,928	80.9%
NOVEMBER	2011	1,235,787	1,527,813	(292,026)	872	80.9%
DECEMBER	2011	1,246,235	1,583,613	(337,378)	(45,352)	78.7%
JANUARY	2012	1,274,884	1,572,630	(297,746)	39,632	81.1%
FEBRUARY	2012	1,294,521	1,579,548	(285,027)	12,719	82.0%
MARCH	2012	1,297,681	1,526,122	(228,441)	56,586	85.0%
APRIL	2012	1,293,677	1,561,169	(267,492)	(39,051)	82.9%
MAY	2012	1,263,186	1,620,957	(357,771)	(90,279)	77.9%
JUNE	2012	1,283,728	1,697,711	(413,983)	(56,212)	75.6%
JULY	2012	1,298,087	1,830,942	(532,855)	(118,872)	70.9%
AUGUST	2012	1,309,312	1,807,731	(498,419)	34,436	72.4%

PENSION ASSET AND LIABILTY RETURNS (ALL DOLLAR AMOUNTS IN MILLIONS)						
		ASSET RETURNS			LIABILITY RETURNS	
END OF MONTH	YEAR	MONTHLY	YEAR-TO-DATE	DISCOUNT RATE	MONTHLY	YEAR-TO-DATE
AUGUST	2011	-2.24%	1.12%	4.96%	2.52%	8.93%
SEPTEMBER	2011	-2.47%	-1.38%	4.54%	6.44%	15.94%
OCTOBER	2011	4.07%	2.64%	4.53%	0.40%	16.41%
NOVEMBER	2011	-0.47%	2.15%	4.53%	0.38%	16.85%
DECEMBER	2011	3.00%	5.22%	4.67%*	-1.80%	14.74%
JANUARY	2012	2.46%	2.46%	4.71%	-0.37%	-0.37%
FEBRUARY	2012	1.70%	4.20%	4.69%	0.76%	0.39%
MARCH	2012	0.40%	4.62%	4.88%	-3.05%	-2.67%
APRIL	2012	-0.15%	4.46%	4.76%	2.63%	-0.11%
MAY	2012	-2.20%	2.16%	4.56%	4.14%	4.03%
JUNE	2012	1.79%	3.98%	4.32%	5.03%	9.26%
JULY	2012	1.28%	5.31%	3.92%	8.11%	18.12%
AUGUST	2012	1.02%	6.38%	3.99%	-1.01%	16.93%

* Reflects a change in our discount rate methodology in moving from the Citigroup Pension Liability Index to the Citigroup Above Median Pension Liability Index.

ABOUT THE MILLIMAN 100 MONTHLY PENSION FUNDING INDEX

For the past 12 years, Milliman has conducted an annual study of the 100 largest defined benefit pension plans sponsored by U.S. public companies. The Milliman 100 Pension Funding Index projects the funded status for pension plans included in our study, reflecting the impact of market returns and interest rate changes on pension funded status, utilizing the actual reported asset values, liabilities, and asset allocations of the companies' pension plans.

The results of the Milliman 100 Pension Funding Index were based on the actual pension plan accounting information disclosed in the footnotes to the companies' annual reports for the 2011 fiscal year and for previous fiscal years. This pension plan accounting disclosure information was summarized as part of the Milliman 2012 Pension Funding Study, which was published on March 29, 2012. In addition to providing the financial information on the funded status of U.S. qualified pension plans, the footnotes may also include figures for the companies' nonqualified and foreign plans, both of which are often unfunded or subject to different funding standards than those for U.S. qualified pension plans. They do not represent the funded status of the companies' U.S. qualified pension plans under ERISA.

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