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Milliman 2007 Pension Funding Study

April 11, 2007

Key Findings

- Significant Improvement in Funded Status
- Asset Gains Exceeded Expected Return
- Increase in Discount Rates
- Reduction in Shareholder Equity under New Accounting Rules
- Continued Increase in Pension Expense
- Decrease in Employer Contributions
- Asset Allocation Unchanged
- 2007 – Year for Reaction to New Rules

Milliman 2007 Pension Funding Study

- 100 U.S. companies
  - Largest public companies with DB Plans that file reports with the SEC
  - Companies with largest DB plan assets
  - Total pension assets of almost $1.3 trillion
- Analysis of Key Pension Data
  - Footnote Disclosures
  - Earnings Statement
  - Balance Sheet

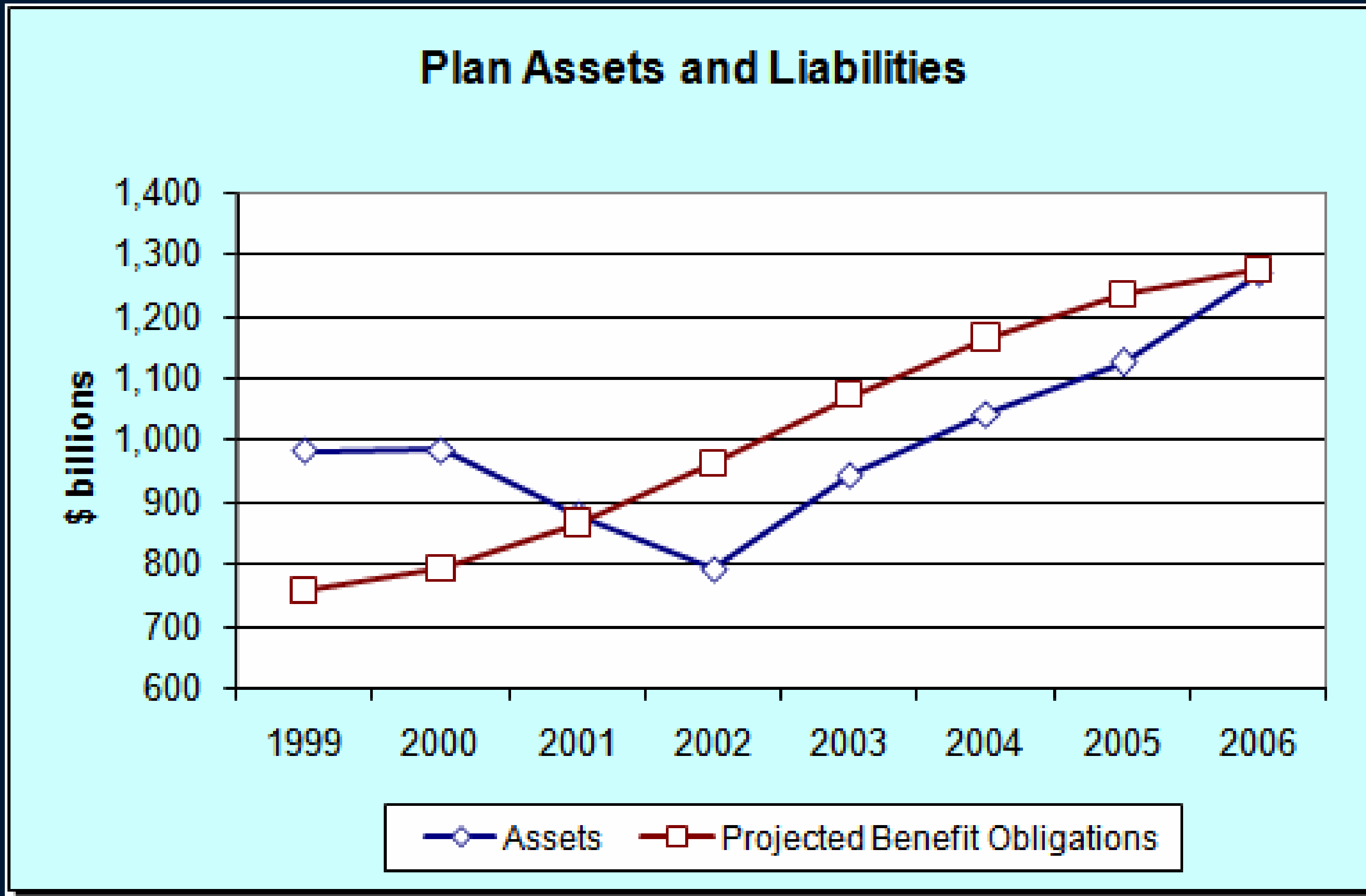
Milliman 2007 Pension Funding Study

- Companies Included
  - Significant DB assets and liabilities
  - Annual Reports released by 3/15/2007
  - Includes 12 companies with FYEs other than 12/31
- Companies Excluded
  - Private Companies
  - Mutual Insurance Companies
  - US subsidiaries of foreign parents
- Disclosure Information includes:
  - US Qualified pension plans
  - Non-qualified plans (mostly unfunded)
  - Foreign plans (often unfunded)

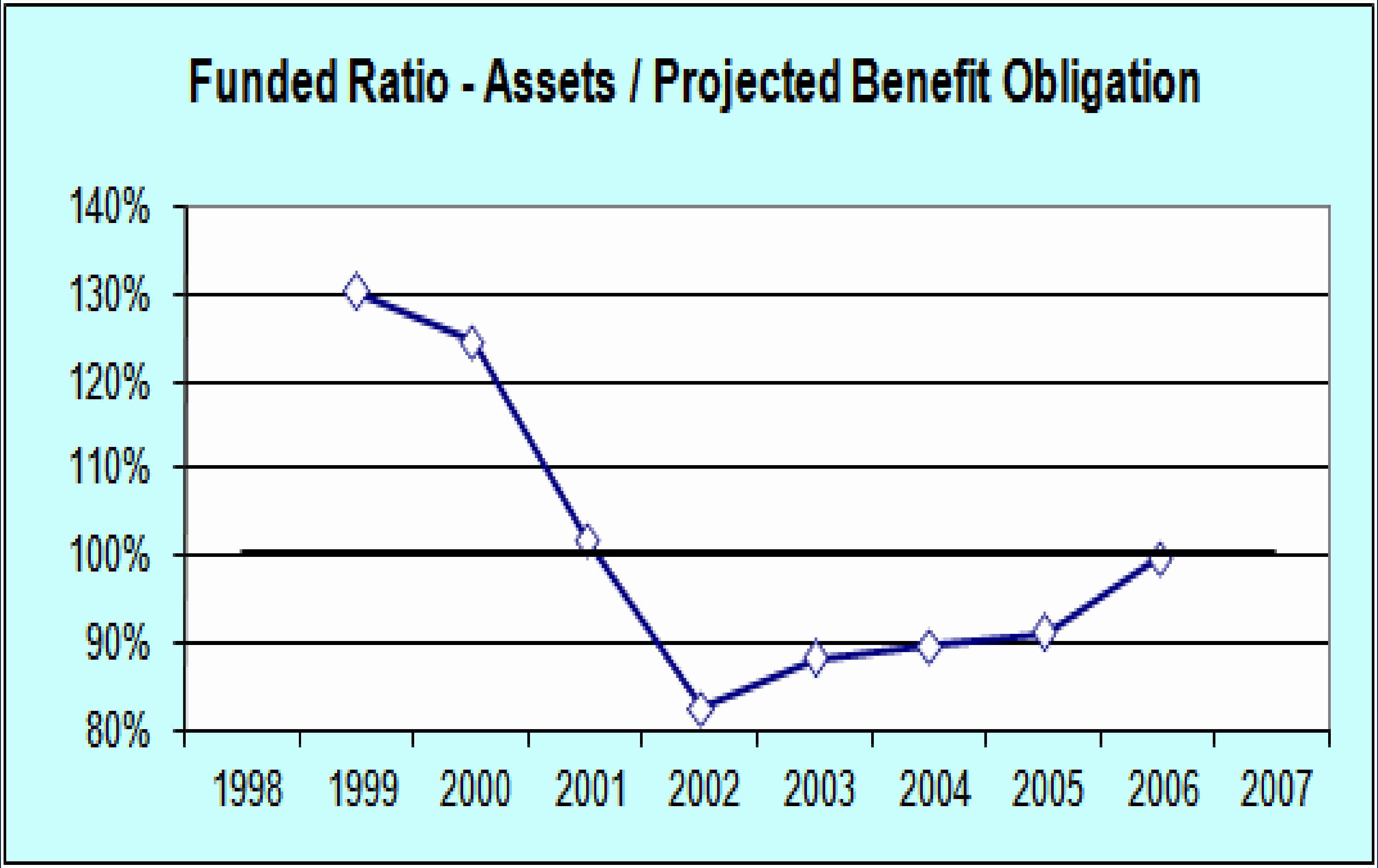
Funded Status Improvement

- PBO funded status improved significantly with asset gains joined by the effect of increased discount rates – Only $4.3b deficit at end of 2006, versus $106.9b deficit at end of 2005
- Aggregate pension funded status improved by $102.6b in 2006, after funded status improvements of $12.1b in 2005, $5.8b in 2004 and $43.4b in 2003
- Cumulative funded status gains of $164.0b for past 4 years still overshadowed by cumulative losses of $402.4b for preceding 3-year period
- Number of companies in surplus position at end of 2006 doubled from 20 to 40, but still far below 90 with surplus assets at end of 1999

Funded Status Improves
Assets Up, While Liability Growth Slows



Funded Status Increases Continue

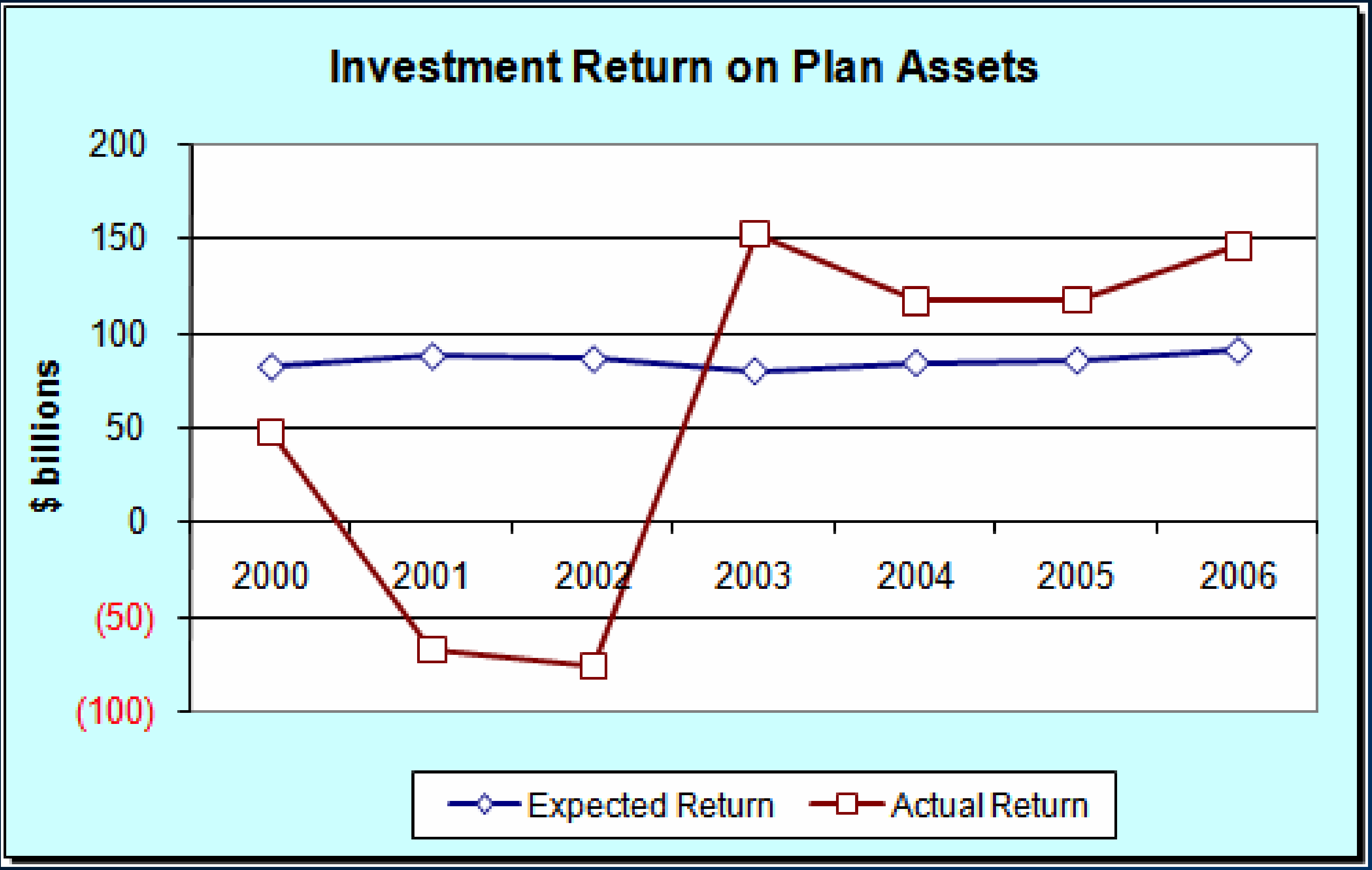


Continued Asset Gains

- Actual return on assets of 12.8% for 2006 exceeded expected return of 8.4% by $54.6b
  - Fourth consecutive year of gains (average annual return of 13.9% with cumulative surplus gains of $193b) after three consecutive years of losses (cumulative losses of $360b)
  - Actual returns for 2006 ranged from 4.3% to 18.1%
  - During past seven years, actual rate of return has been annual rate of about 5.9% vs. expected return of 8.8%.
  - Recent asset gains combined with discount rate increase to improve funded ratios and are expected to decrease pension expense for 2007

Actual Returns Exceed Expected in 2006

Fourth Consecutive Year of Surplus Asset Gains



New Balance Sheet Exposure

- New accounting standard requires full recognition of plan's funded status (PBO vs MV of Assets)
- Among 100 companies, 89 implemented
- For pensions and other postretirement benefits, post-tax decrease of $133b (5.7%) in shareholder equity
- Increase in shareholder equity for 6 companies

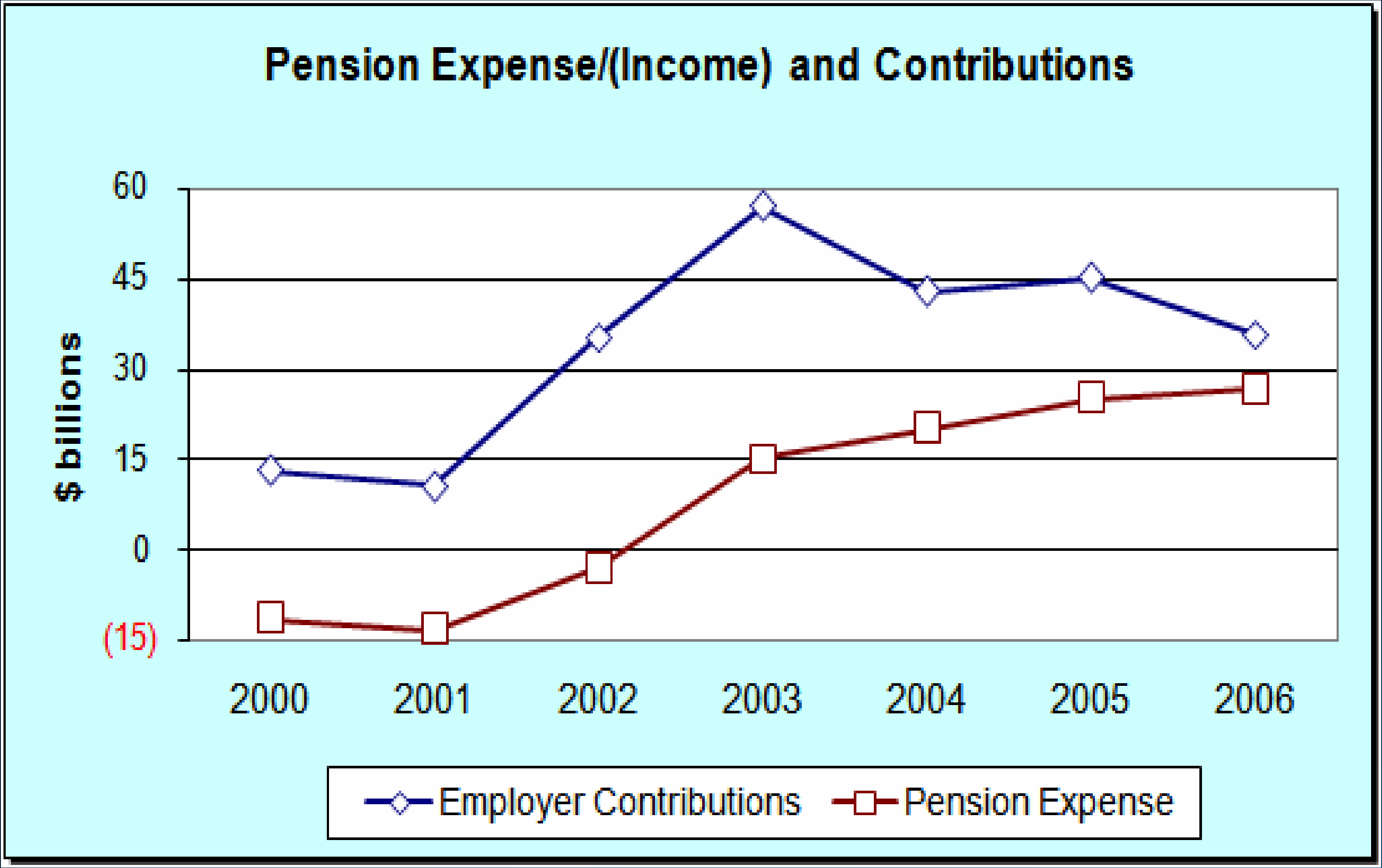
Peak for Pension Expense

- Aggregate pension expense of $26.4b for 2006, up from 2005 expense of $24.6b, vs. pension *income* of $14.3b in 2001
- Only 9 companies with pension income in 2006 compared to 61 in 2001
- Four years of strong asset gains, together with discount rate increase for 2006 likely to produce lower pension expense for 2007

Lower Employer Contributions

- Employer contributions decreased to $35.7b for 2006 from $44.9b for 2005
- Contributions continued to exceed expense, by a cumulative excess of $184b during the past seven years
- Pension Protection Act of 2006 is expected to significantly affect amount and volatility of future contributions
- Plan sponsors may continue to contribute at lower levels in 2007 in reaction to new accounting standards and new pension funding law

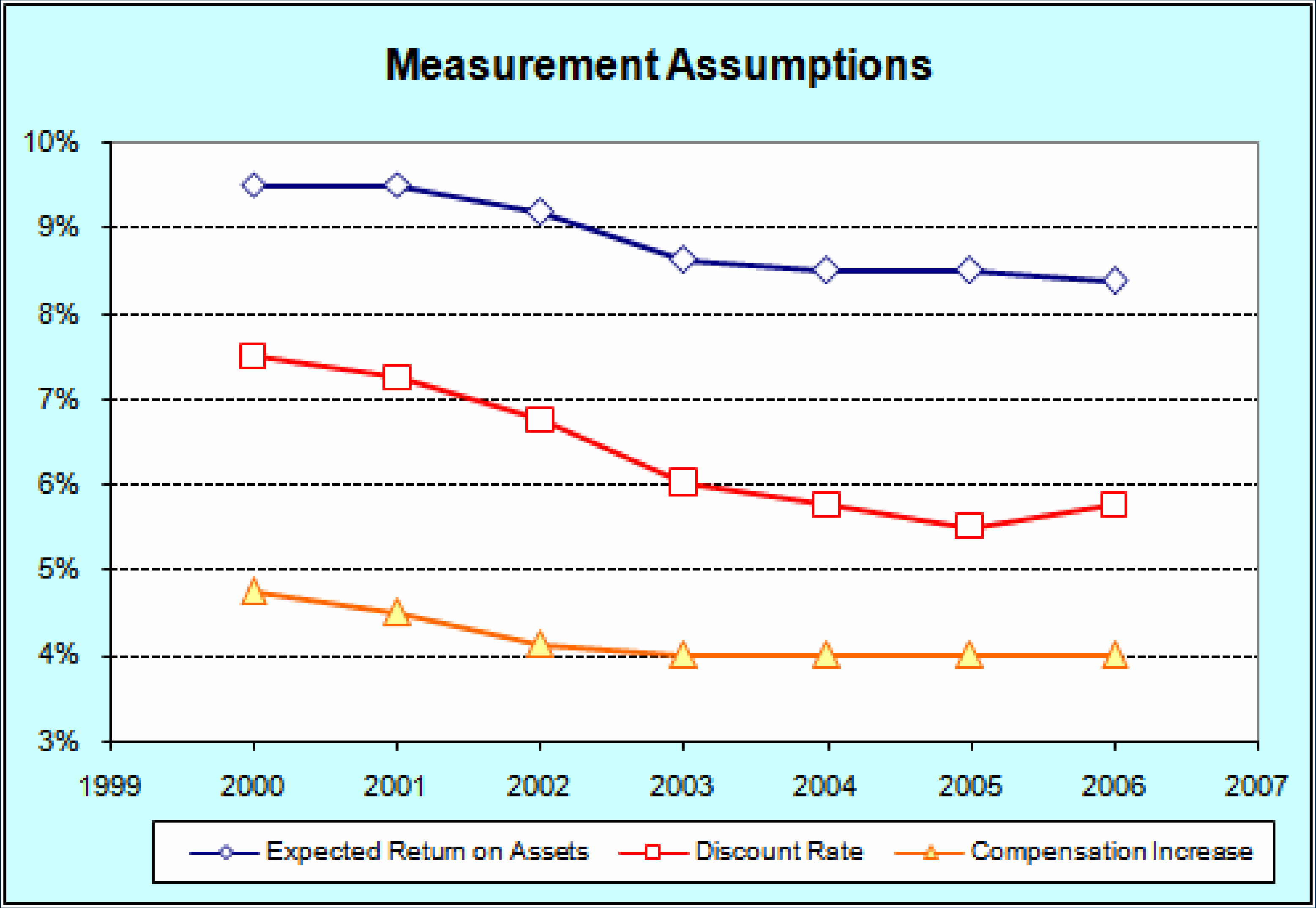
Pension Expense and Contributions



Higher Discount Rates
Lower Expected Return on Assets

- Median Discount Rate up to 5.75% for 2006, from 5.50% in 2005, after incremental declines from 7.50% in 2000
- Median expected rate of return on assets lowered to 8.4% from 8.5% in 2005
- 12 companies continue to use an expected return of at least 9.00%

Higher Discount Rates



Asset Allocation Stable

- Equity asset allocations at the end of 2006 ranged from 17.6% to 78.0% with a median of 63.8%, only up slightly from the median of 63.5% at the end of 2005
- Fixed income asset allocations for end of 2006 ranged from 1.0% to 72.6% with a median of 29.3%, only down slightly from the median of 29.8% at the end of 2005

Asset/Liability Mismatch

- Most pension plans still have a significant asset/liability mismatch
- Many companies have begun investigating risk management strategies to preserve the funded status and mitigate pension financial risks
- Many companies have also begun investigating creative investment strategies to increase returns

Shift to Liability-Driven Investing

- Liability-Driven Investing (LDI) seeks to reduce the level and volatility of pension financial risks while attempting to generate a return above the market-based growth rate of the liabilities
- Financially efficient portfolios have two components
  - Hedging interest rate risk of liabilities
  - Generating excess returns above the growth rate of the liabilities

Managing Pension Risk

- Set the investment benchmark equal to the market-based growth rate of the liabilities
- Improve funded status risk/return
  - Decrease market (beta) risk and increase active management (alpha) risk
  - Increase fixed income duration <u>and</u> allocation
  - Decrease equity allocation; increase alternative investment allocation
  - Usage of derivatives for beta exposure
  - Consideration of portable alpha and absolute return strategies

2007 – Reaction and Preparation

- New accounting and funding standards have increased volatility and make financial projections a necessary planning tool
- Increased use of LDI strategies to reduce volatility and help preserve funded status
- New wave of cash balance conversions after new law and court decisions
- Reversal of recent trend of plan freezes
- Increased appreciation of DB plans with changing demographics

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