THE 5 MYTHS OF PENSION RISK TRANSFER

There's lots of talk these days about managing pension risk. But what separates the myths from the math? We ran a series of simulations to find out.

1

THE MYTH

A LITTLE LDI MAKES A BIG DIFFERENCE FOR PENSION PLANS

THE MATH

Liability-driven investments can help plans de-risk – but without a significant reallocation to fixed income, sponsors still face substantial risk. Plus, LDI doesn't account for longer retirements, unless augmented with longevity insurance.

Our simulations revealed that increasing fixed income allocation from 30% to 45% still left more than ¾ of the initial pension liability risk.

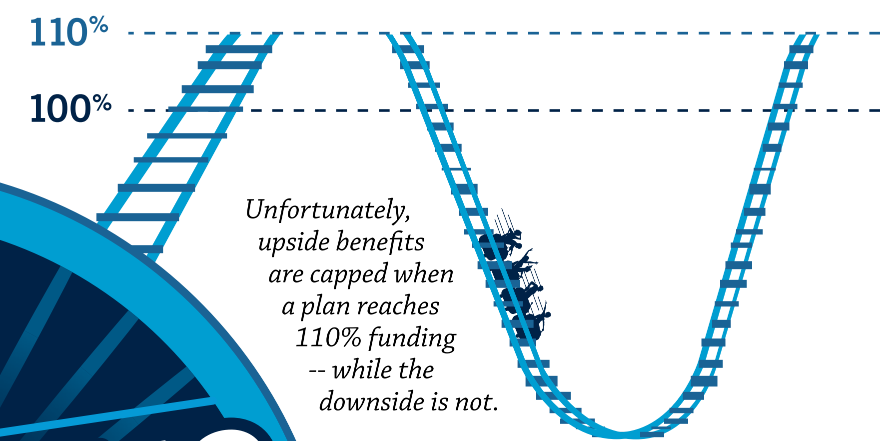
2

THE MYTH

IT'S SMART TO DELAY DE-RISKING WHEN INTEREST RATES ARE LOW

THE MATH

It's not uncommon for companies to misjudge the risk they are taking on when watching the market. Why? Specific, sustained market conditions must exist for plans to realize improved funded status.



Unfortunately, upside benefits are capped when a plan reaches 110% funding -- while the downside is not.

But every risk deserves the potential for reward. As funded status improves, companies should contemplate de-risking.

3

THE MYTH

PRT ONLY WORKS FOR FULLY FUNDED PLANS

THE MATH

For underfunded plans, it's true that pension buyouts could lower funded ratios. But there is a solution: a pension buy-in enables risk transfer without affecting the plan's funding ratio.

4

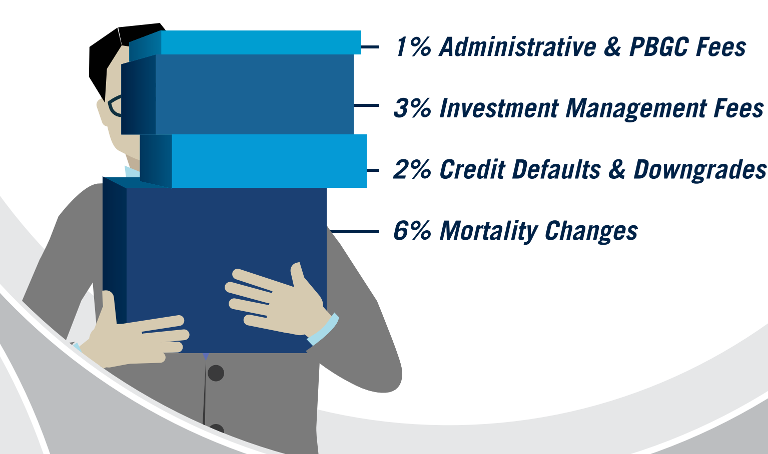
THE MYTH

THE PRICE IS NOT RIGHT FOR RISK TRANSFER

THE MATH

The premium over GAAP liability to transfer risk is lower than what the market perceives. Often over-looked when calculating risk transfer costs are expenses incurred by a company whether it de-risks or not.

The liability created by increasing longevity accounts for possibly the most significant percentage of premium over GAAP liability.



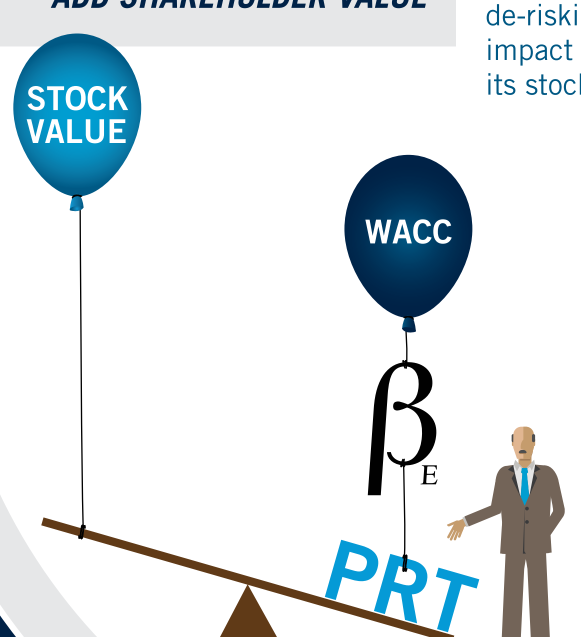
5

THE MYTH

PENSION RISK TRANSFER DOES NOT ADD SHAREHOLDER VALUE

THE MATH

Does PRT drive down a company's valuation? A close investigation reveals that de-risking could, in fact, positively impact a firm's valuation and, thus, its stock price.



PRT could lower equity beta and WACC, which may grow stock value and provide more financial flexibility for a company.

Data taken from *Reducing Pension Risk: The Five Myths Holding Back Plan Sponsors.*

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