

## Pension Plan Funded Status Drops Slightly Due to Liability Increases Outpacing Asset Increases in Q1 2014

During the first quarter of 2014 (Q1 2014), the funded status of the model pension plan examined in each issue of *Prism* decreased by 3 percentage points: from 95 percent to 92 percent. This decrease was driven by an asset return of 2 percent and a liability increase of 5 percent. See Graph 1.

### About Prism

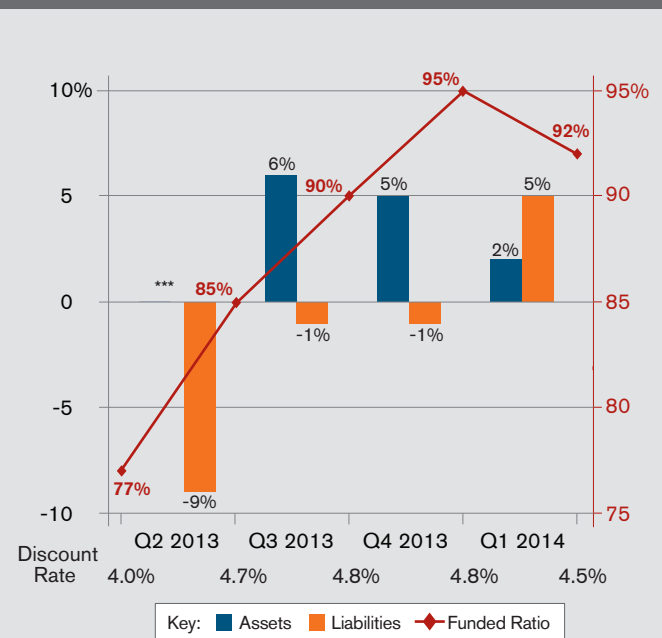
*Prism* examines the effect of changes in the assets and liabilities of a model pension plan on its funded ratio over the four most recent quarters, viewing such changes through a marked-to-market lens. The primary focus is to understand the combined impact of asset movement and interest rate shifts on perhaps the most important financial metric to plan sponsors: the plan's funded status.

## Aspects of Investment Performance

Following a stumble out of the gate in January, global equities recovered in February and March, finishing the quarter in positive territory. As shown in Graph 2, domestic equities modestly outperformed international equities. Large caps beat small caps and value stocks beat their growth counterparts. In a reversal of recent fortune, emerging markets equities outpaced developed market equities.

In the fixed-income world, global bonds, as measured by the Citigroup World Government Bond Index (WGBI), posted a 2.66 percent gain for the quarter (see Graph 2) following a 1.09 percent drawdown in Q4. Virtually all global fixed-income sectors posted positive performance, as interest rates fell during the quarter.

Graph 1: Change in Assets,\* Liabilities and Funded Ratio\*\*

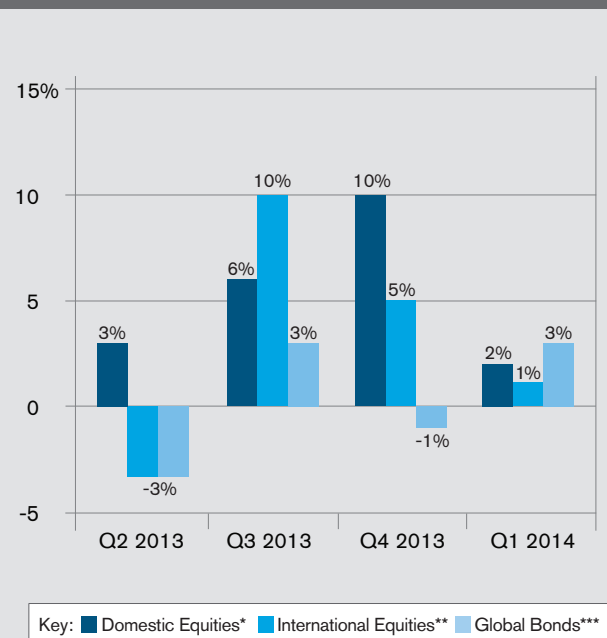


\* The model plan's portfolio has a simple, passively invested asset allocation of 45 percent to domestic equities, 15 percent to international equities and 40 percent to global bonds.

\*\* This is the ratio of a defined benefit (DB) plan's assets to accrued liabilities. The funded ratio data in the graph is the ratio at a point in time at the beginning or end of the quarter. The funded percentage for the model DB plan was reset as of January 1, 2014 to reflect the average actual funded percentage of large pension plans.

\*\*\* In Q2 2013, assets decreased 0.4 percent.

Graph 2: Investment Performance



\* Russell 3000

\*\* Morgan Stanley Capital International All Country World Index Ex-U.S. (MSCI ACWI Ex-U.S.)

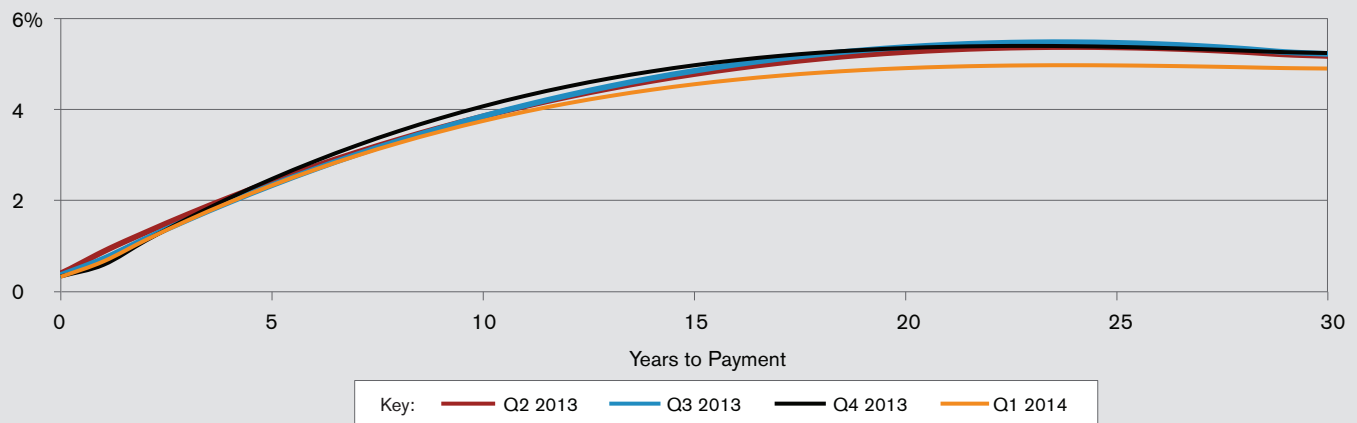
\*\*\* Citigroup World Government Bond Index (WGBI) Unhedged, which includes U.S. and international bonds

## Changes in the Yield Curve

High-quality corporate yields decreased about 30 basis points during Q1 2014. Treasury rates also decreased by similar amounts, reflecting immaterial changes in credit spreads. The overall shape of the yield curve remained similar to the previous quarter: an upward sloping yield curve which peaks at about 25 years, and then levels off, as illustrated by the above-median curves shown in Graph 3.\*

The decrease in the yield-curve level during Q1 2014 resulted in a decrease in the effective interest rate and, consequently, increased the model pension plan's liability by about 5 percent. As in previous quarters, the shape of the yield curve will have different effects for plans with different maturities. (For background on yield curves, see the following web page: <http://www.sibson.com/publications/presentations/2014PrismYCprimer.pdf>)

Graph 3: Changes in the Yield Curve\*



\* This curve reflects the average yield, at each duration, for corporate bonds rated AA that have yields above the median for that duration.

## Important: Examine Your Own DB Plan's Experience

Plan sponsors should examine changes in their own DB plans' assets, liabilities and funded ratios both from the vantage point of accounting and funding metrics. Individual plan results will differ from this model for a host of reasons, including different funded positions, liability duration and contribution patterns.



*Segal Rogerscasey and Sibson Consulting can help employers to project their DB plans' funded ratios through asset-liability modeling (ALM). For more information about ALM, contact your Segal Rogerscasey investment consultant or your Sibson retirement consultant.*

\* As a reminder, 10 basis points (bps) equals 0.1 percent.

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