Sibson Consulting

Segal Rogerscasey

Prism

A QUARTERLY REVIEW OF FUNDED STATUS

Strategic HR Consulting | Investment Solutions | Third Quarter 2014 Pension Plan Experience

Pension Plan Funded Status Decreases Slightly Due to Decline in Assets in Q3 2014

During the third quarter of 2014 (Q3 2014), the funded status of the model pension plan examined in each issue of *Prism* decreased by 2 percentage points: from 93 percent to 91 percent. This decrease was driven by a negative asset return of 2 percent and liabilities that remained flat. See Graph 1.

About *Prism*

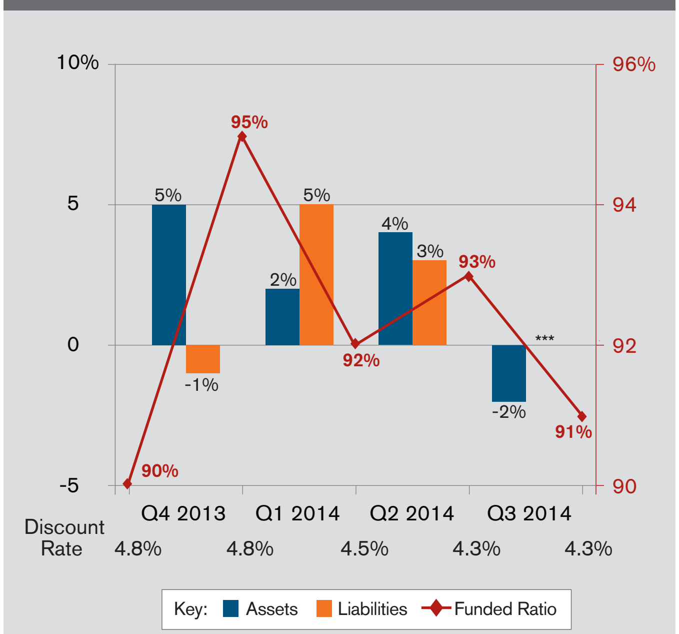
Prism examines the effect of changes in the assets and liabilities of a model pension plan on its funded ratio over the four most recent quarters, viewing such changes through a marked-to-market lens. The primary focus is to understand the combined impact of asset movement and interest rate shifts on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

Aspects of Investment Performance

Following solid gains in the first half of the year, global equities took a breather in Q3. As shown in Graph 2, domestic equities were roughly flat but still managed to outpace non-U.S. stocks, which fell 5 percent. Within the U.S., large caps significantly outperformed small caps while growth stocks edged out value stocks. Outside of the U.S., emerging market stocks outpaced their developed-market counterparts.

On the fixed-income side, global bonds, as measured by the Citigroup World Government Bond Index (WGBI), also had a drawdown, posting a 4 percent loss. The strength in the dollar was the primary reason for the poor performance of the index.

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

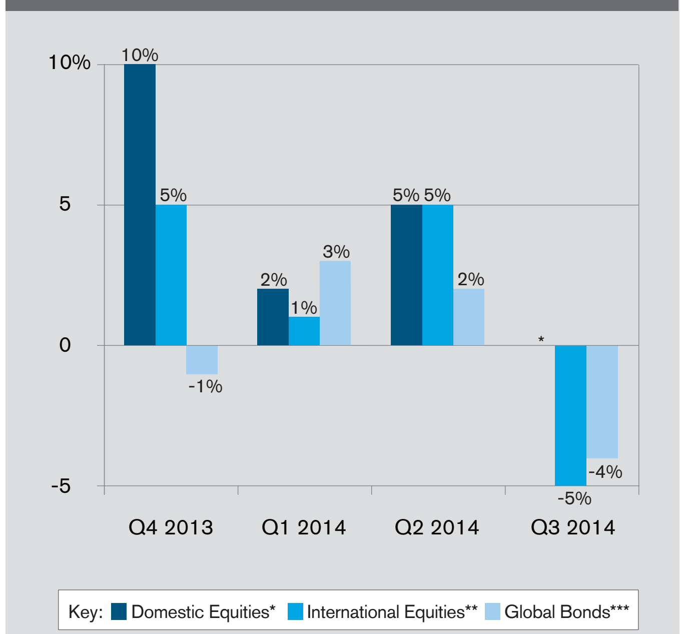


* The model plan's portfolio has a simple, passively invested asset allocation of 45 percent to domestic equities, 15 percent to international equities and 40 percent to global bonds.

** 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 Q3 2014, liabilities decreased 0.5 percent.

Graph 2: Investment Performance



* Russell 3000 (In Q3 2014, the return for domestic equities was 0.01 percent.)

** 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

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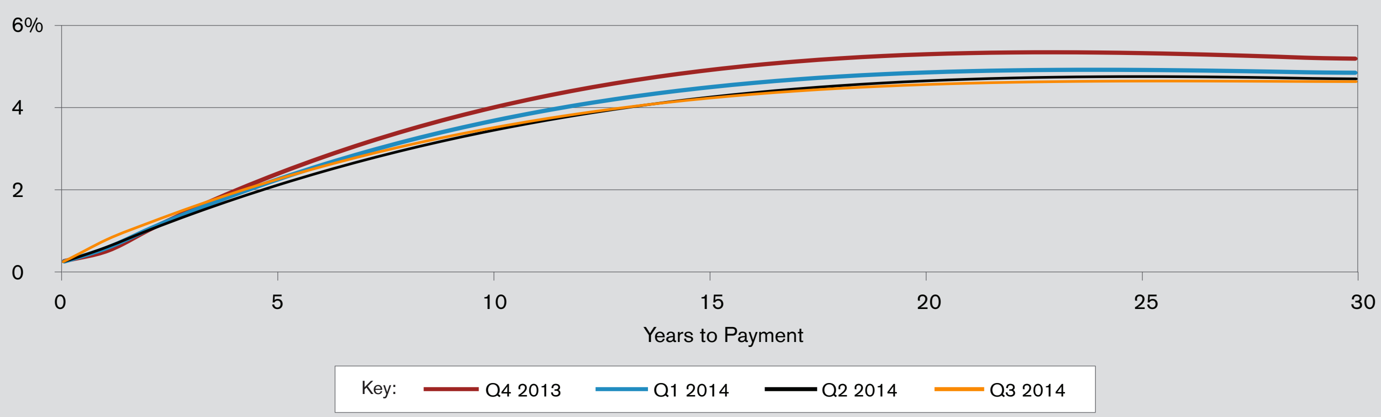
Changes in the Yield Curve

High-quality corporate yields decreased slightly during Q3 2014. This decrease was comprised of a general decrease in Treasury rates of about 10 basis points* and a minor increase in credit spreads. The overall shape of the yield curve remained similar to the previous quarter: an upward-sloping yield curve that peaks at about 25 years and then levels off, as illustrated by the above-median curves shown in Graph 3.

The minor decrease in the yield-curve level during Q3 2014 had little impact on the effective interest rate; consequently, the model pension plan's liability was virtually unchanged. Any change in the shape of the yield curve could have different impact on liabilities for plans with different maturities. (For background on yield curves, see the following webpage: 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 from the vantage point of both 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.

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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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