



Pension Risk Solutions for DB Pension Plans

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External Market Drivers

Then (1980's)

- Extended Bull Market & High Interest Rates
- Overfunded Pension Plans
- Corporate Consolidation/LBOs
- Impending Reversion Tax Change

Now

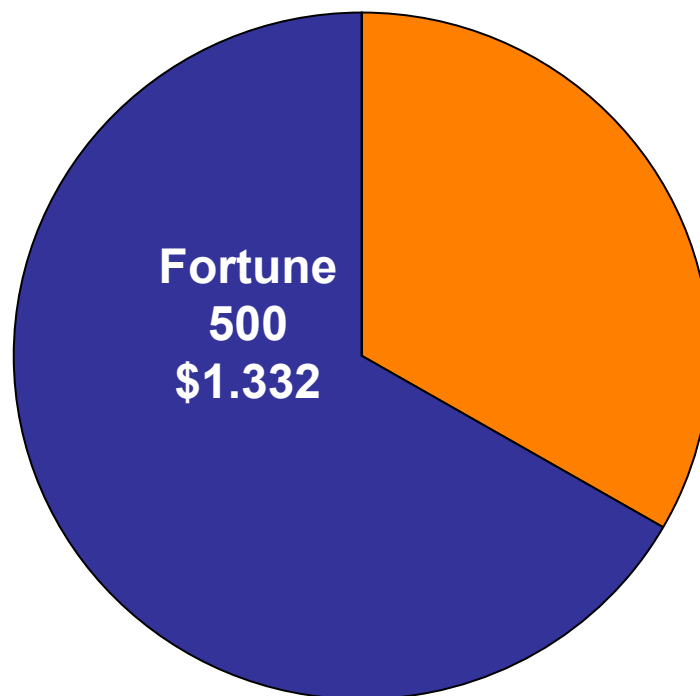
- Uncertain Equity Markets & Low Interest Rates
- Funding Status / Demographic Shift
- Challenging Economic Environment
- Proposed Accounting & Regulatory Changes

Current Business Perspective: Pensions Evolution

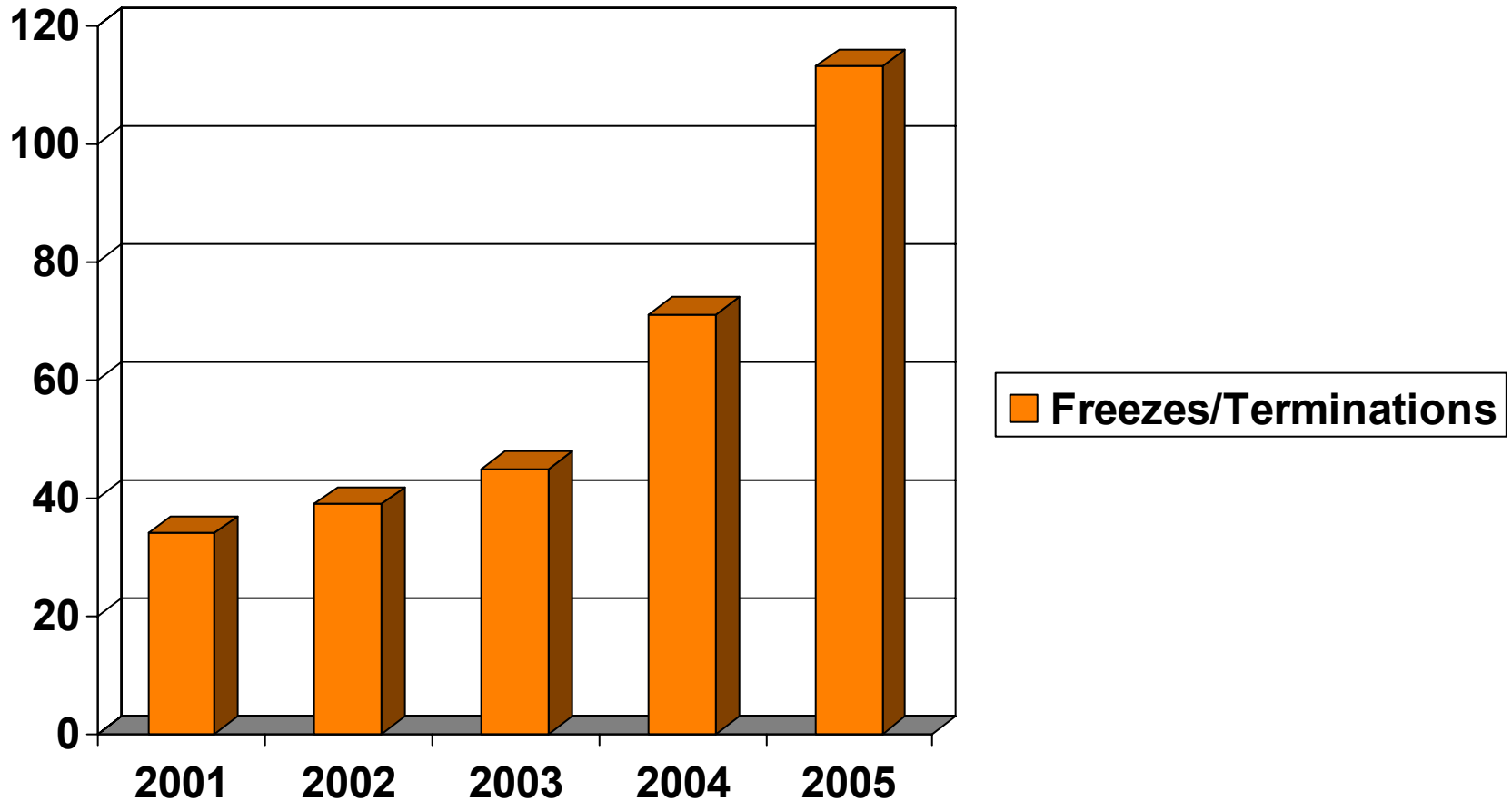
- The Evolution of Pension Plan Management
- Convergence of External Trends Today
- Cumulative Effect of Unintended Consequences

U.S. Defined Benefit Plan Assets

Fortune 500 company plan assets represent approximately 67% of the \$2 trillion market.



Prevalence of DB Pension Plan Freezes/Terminations Among FORTUNE 1000 Firms



Source: Watson Wyatt Worldwide

What Is Really Happening with DB Plan Sponsors?

- It's status quo for 77% of the companies surveyed
- 86% either have no plans to convert to cash balance or they do not yet know what they are going to do in this area
- 92% feel well/somewhat prepared for the new funding rules
- 63% feel the risks are manageable, plus 30% feel they are acceptable
- 89% of the companies surveyed have ongoing plans to manage
- 3% of US plan sponsors have some funds allocated to an LDI strategy

Freeze Expectations & Realities

- I thought it would reduce cost volatility.
- I thought it would reduce my short term costs.
- My Board made me do it.
- Everyone else was doing it.
- I thought it would shift investment risk.
- I thought it would be simpler.
- My employees don't understand the plan anyway.

Pension Protection Act

Beginning in 2008:

- 100% funded target for determining required funding
- Modified yield curve
- Significant changes regarding:
 - Determining contribution rates
 - Smoothing
 - Use of credit balances

Financial Accounting Standards Board

Old Rules:

- Funded status of a plan was shown in the footnotes of the financial statements
- Reported number often differed from pensions' actual funded status

New Rules:

- Companies must list net financial position of their pension plans on their balance sheet as an asset or liability
- Requires changes to be reported in the year that they occur

Plan Sponsor Investment Trade-Off

- Investment decision
 - Equities may make pensions “cheaper” but create asset liability mismatch
 - Duration matched fixed income investments make cash flows less volatile
- Impact on competitiveness
 - Potential long-term cost savings vs. short- and intermediate-term cash flow volatility
 - Largest contributions often due at the worst time

New World View for DB Plan Sponsors

- Some freezes, more status quo
- Thoughtful analysis and focus on new math
- Key retention element for selective industries
- Convergence of employee appreciation, plan management and new retirement patterns?

Defined Benefit Plans - More Decision Drivers

- Volatility of Earnings and Stock Price
- Cashflow Sensitivity
- Capital Focus
- Balance Sheet vs Income Statement
- Corporate Culture

Determining Correct Strategy

- “New Math” is the first key
- Every plan assessed in terms of how it stands relative to the PPA's new funding structure

A New Way to Manage Pension Plan Risk

Today

- Management strategies focus on assets

Tomorrow

- Liabilities get equal weight
- New framework for decision making
- Building blocks to create solutions
- Liability insights integrated with asset management

Benefits of Pension Liability Management

- Understanding plan liabilities provides foundation for effective decision making
- Elimination of key risks
- Reduced volatility and provides more certainty in expected costs
- Increased benefit security for participants
- Greater flexibility to focus on core businesses
- Enables inclusion of pension plan risk into company-wide risk management processes

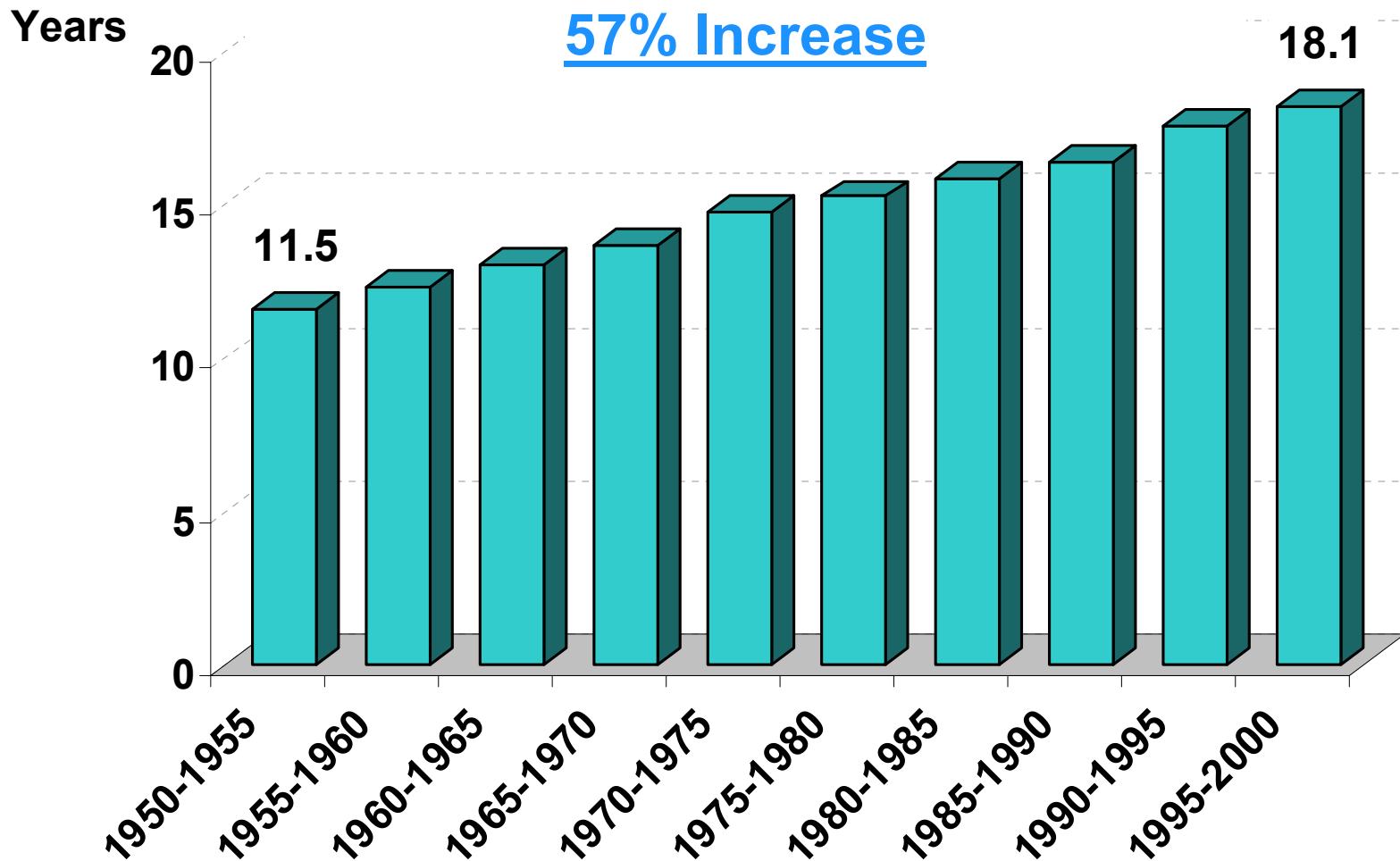
Integrating Liabilities into DB Management

- Managing plan volatility is a core focus
- Liabilities are deconstructed
- Liability profile plus volatility appetite drive decision making
- Liability focused solutions

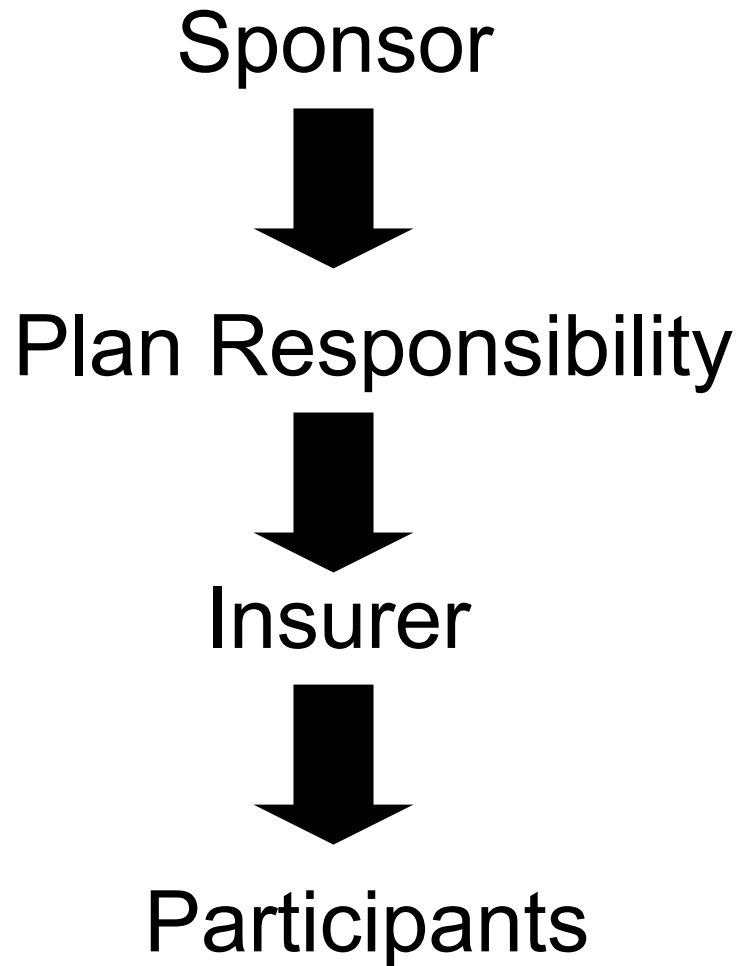
Risk Effects

- Mortality
- Expense
- Investment
- Market

Average Number of Years Spent in Retirement (Males)



Standard Termination Process



Global Fortune 100 Employer in the Technology Industry

PLAN CHARACTERISTICS

Mature DB Plan, Supplemental DB Plan, Fully Funded,
Recent DB Plan

Freeze

DRIVERS

Maintain earnings levels

Stabilize costs & align benefits with global competitors

Income statement sensitivities

Corporate culture

Limit / control future DB liability growth and size

U.S. Domestic Fortune 500® Financial Services Company

PLAN CHARACTERISTICS

Immature DB Plan, 15 Years Old, High Equity Allocation
Left Plan Underfunded

DRIVERS

Maintain stock price growth and access to capital

Balance sheet sensitivities

Corporate culture

Ensure future plan affordability and stability

Manage future volatility

Employee retention

Outlook: DB Challenges & Opportunities in the US

- Guarantees more important than ever
- New generation of DB products that manage financial effects
- Central role of effective long term asset-liability management
- Changing players, changing roles
- Active regulatory environment