



Asset Liability Management: *What You Should Know*

**A Buck Consultants Webcast
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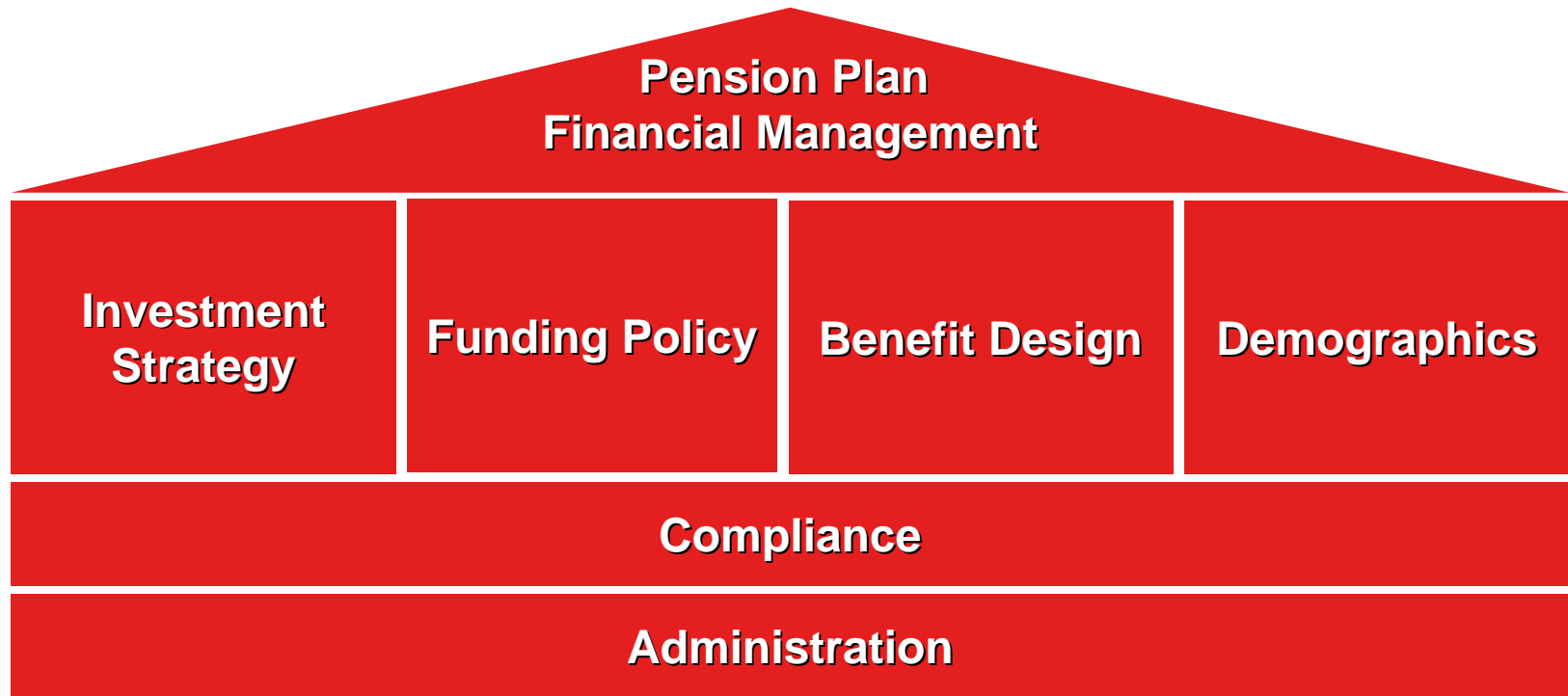
- Asset Liability Management (ALM) Overview
- Ongoing ALM Process
- Case Studies
- Conclusions
- Who to Contact
- Questions & Answers

Asset Liability Management

- Pension financial management requires understanding pension financial drivers
- Pension risk is managed relative to pension liabilities
- Asset liability management facilitates understanding the key drivers of pension risk
- Asset liability modeling is a valuable tool for understanding pension risk

Asset Liability Management

Effective pension financial management involves using Asset Liability Management (ALM) to establish a risk budget and then to understand, monitor, and manage the key drivers of pension plan costs on an ongoing basis to stay within the budget. It is particularly valuable in responding to the effects of an economic downturn.



Asset Liability Management

Investment Strategy

- Long-term strategic asset Allocation
- Shorter-term tactical asset Allocation
- Dynamic rebalancing
- New investment strategies / products

Funding Policy

- Impact of PPA
- Cash management and organizational liquidity
- Contribution timing
- Avoiding benefit restrictions
- Managing PBGC variable premiums

Benefit Design

- Ongoing, closed and frozen plans
- Benefit formula - timing and amount of benefit accruals
- Liquidity needs

Demographics

- New hire impact
- Exodus timing
- Corporate transactions



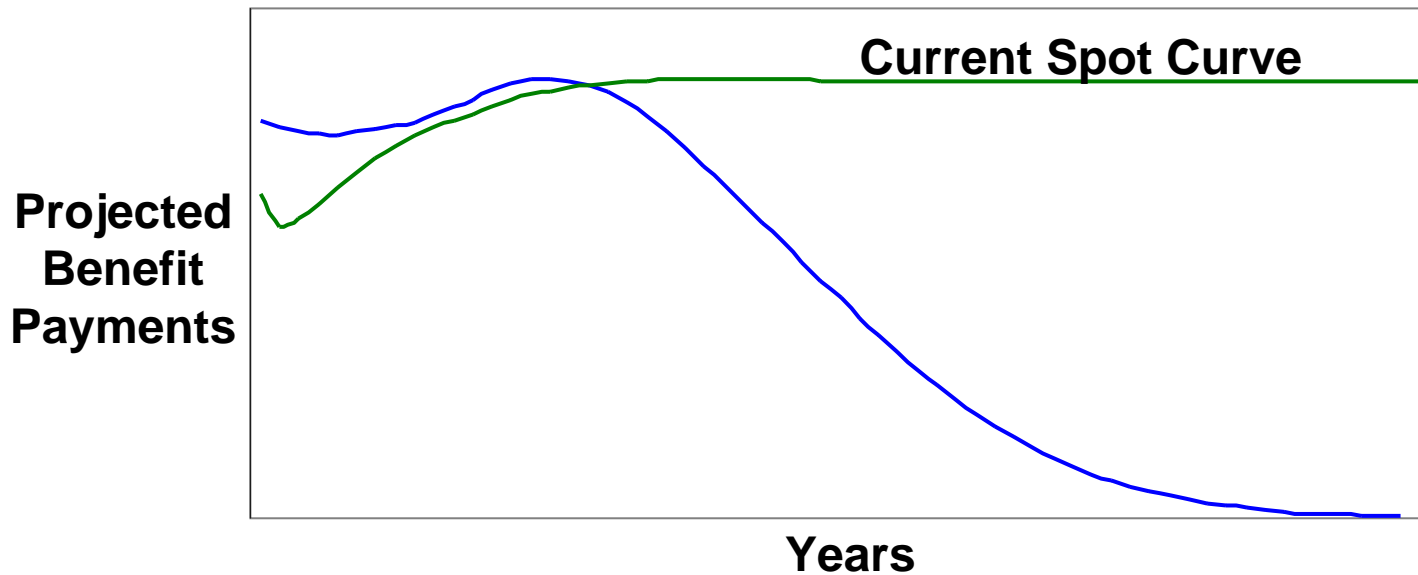
Ongoing ALM Process

Ongoing ALM Process

- Risk assessment/budgeting
- Risk allocation
- Developing a dynamic plan
- Implementation

Risk Budgeting

Risk Budget Is Built Around the Liability Benchmark

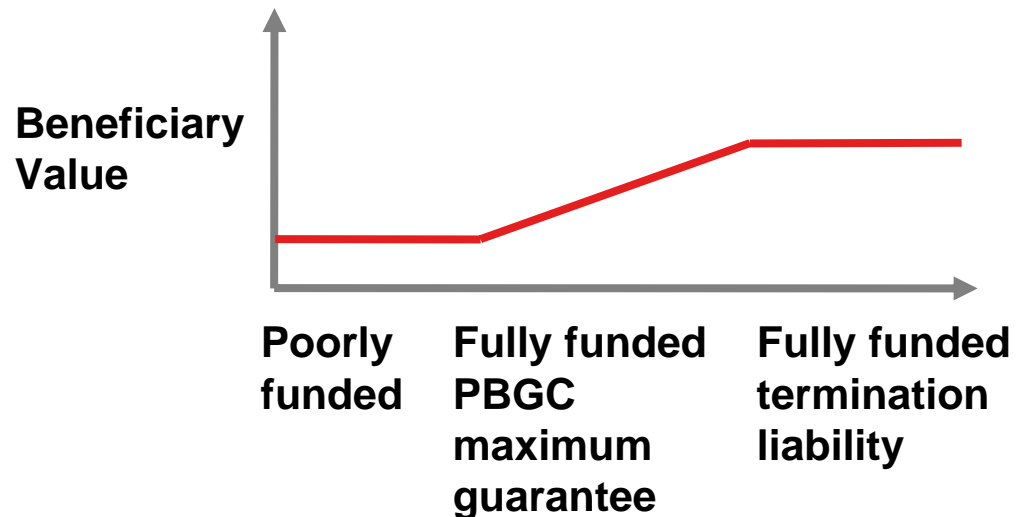


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Risk Budgeting – Fiduciary Considerations

Identifying the Best Interests of Participants

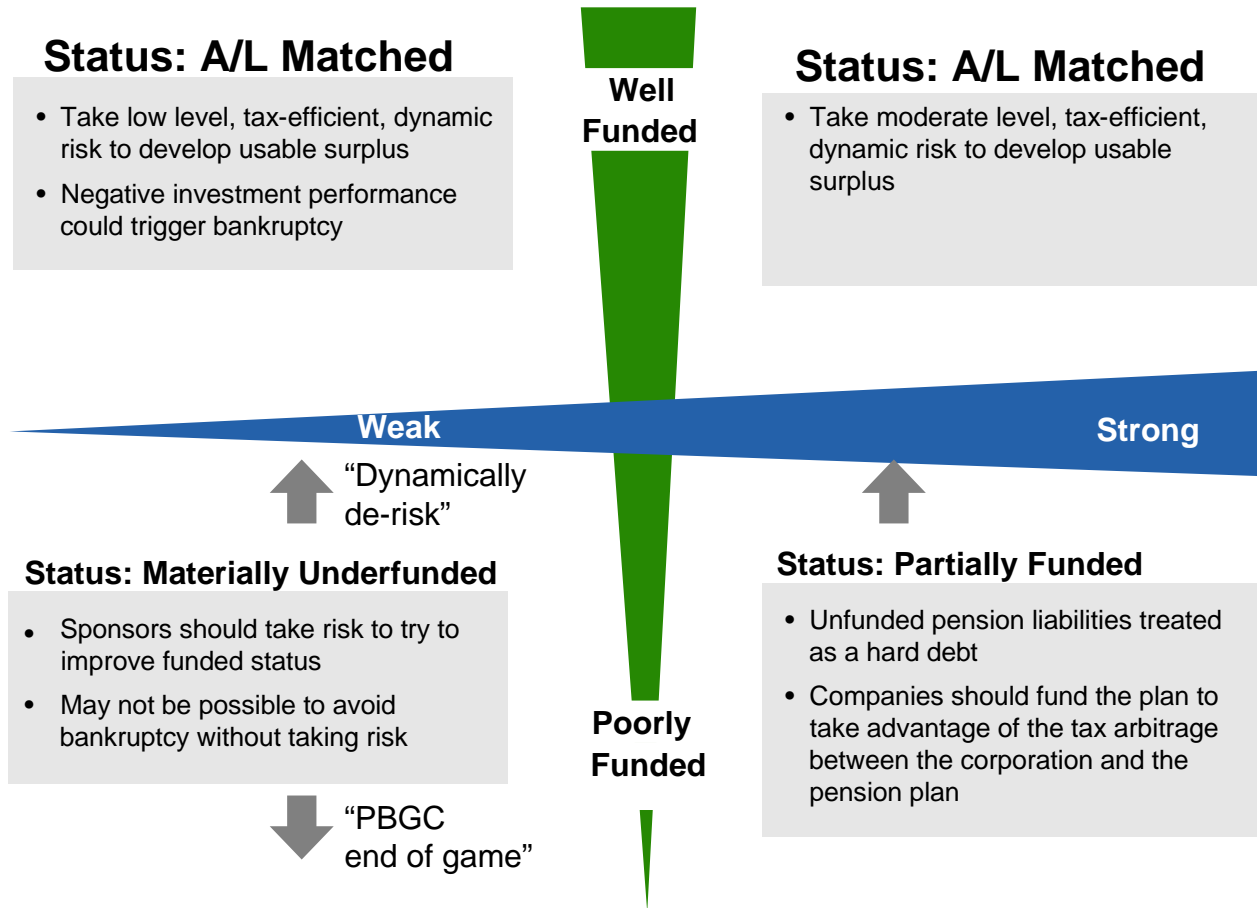
Beneficiaries can lose “value” if the plan sponsor claims bankruptcy and the plan is underfunded



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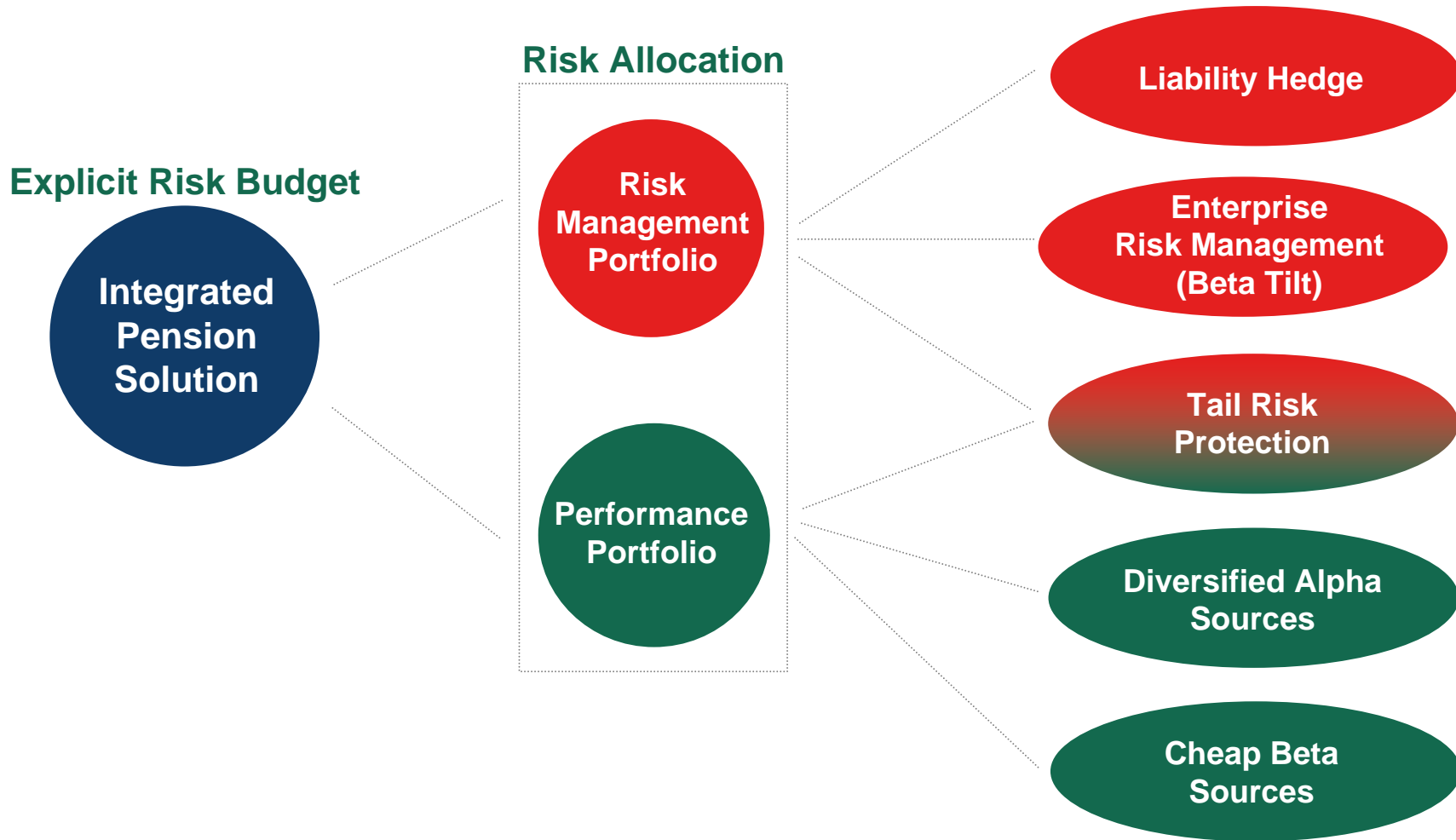
Risk Budgeting – Shareholder Considerations

Participant and Shareholder Interests Are Well Aligned

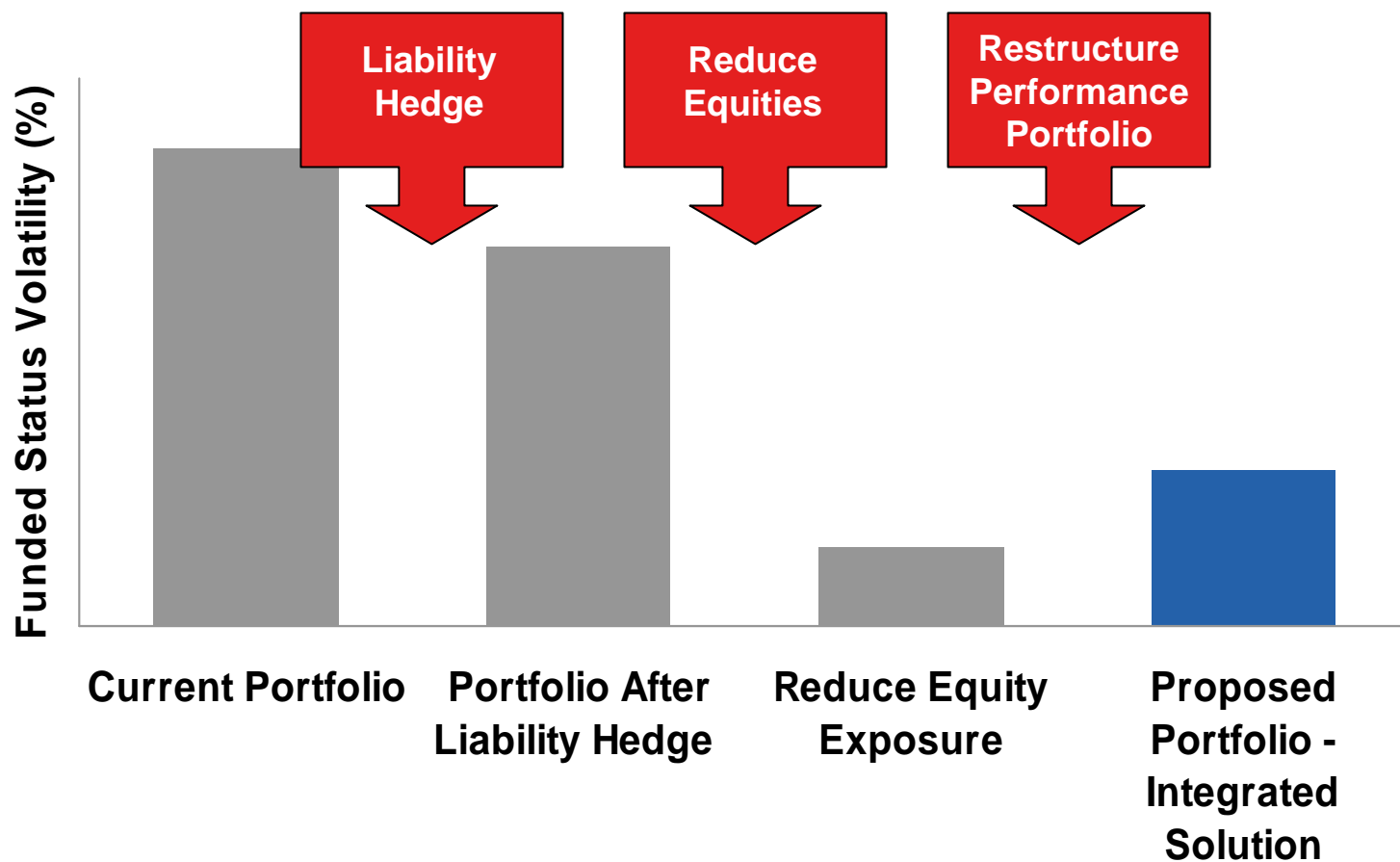


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Risk Allocation



Allocate Risk Efficiently

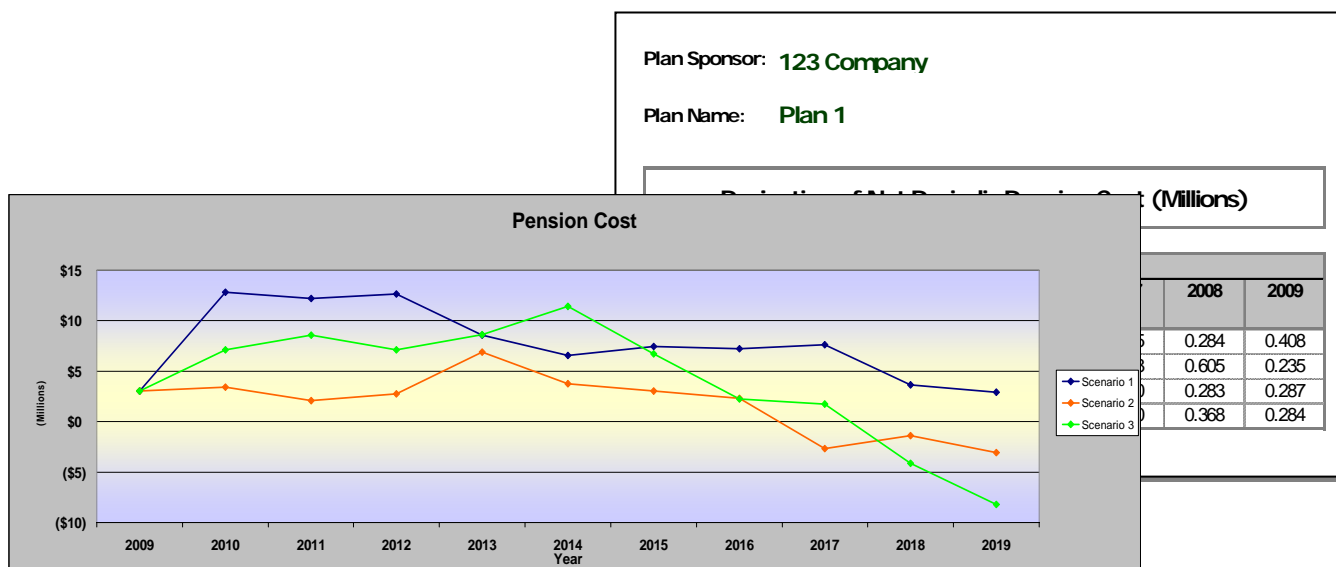




Developing a Dynamic ALM Plan

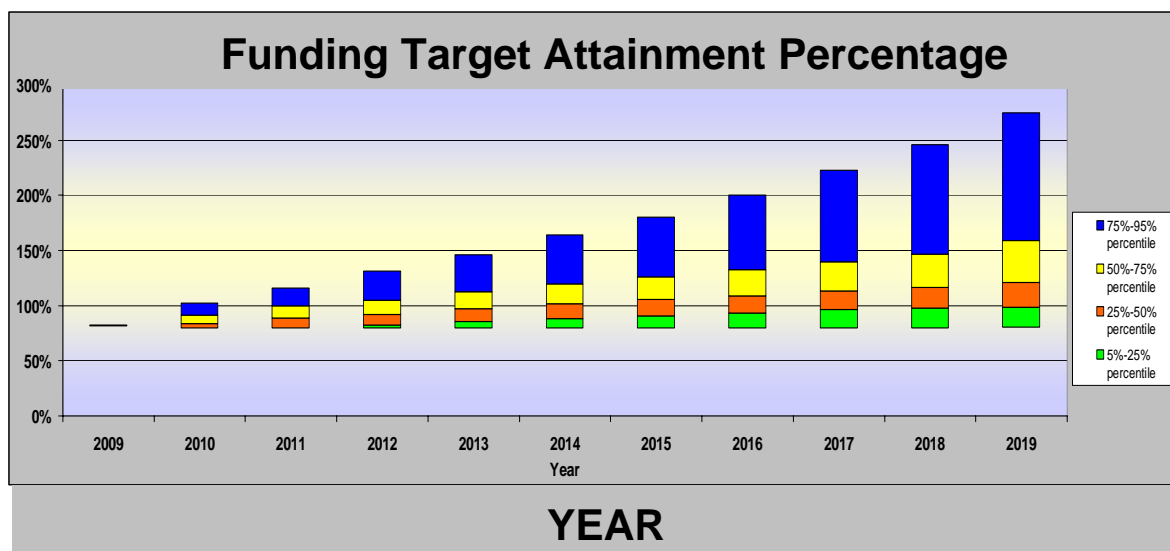
A Useful Tool: Asset Liability Modeling

- Scenario-based (deterministic) valuation projections
 - Evaluate the outcome created by specific economic and capital market environments
 - Identify the economic and capital market conditions that create a specific outcome



A Useful Tool: Asset Liability Modeling

- Monte Carlo (stochastic) valuation projections
 - Understand the likelihood of specific outcomes
 - Identify the range of specific outcomes
 - Observe how likelihoods/ranges are affected by different pension cost drivers

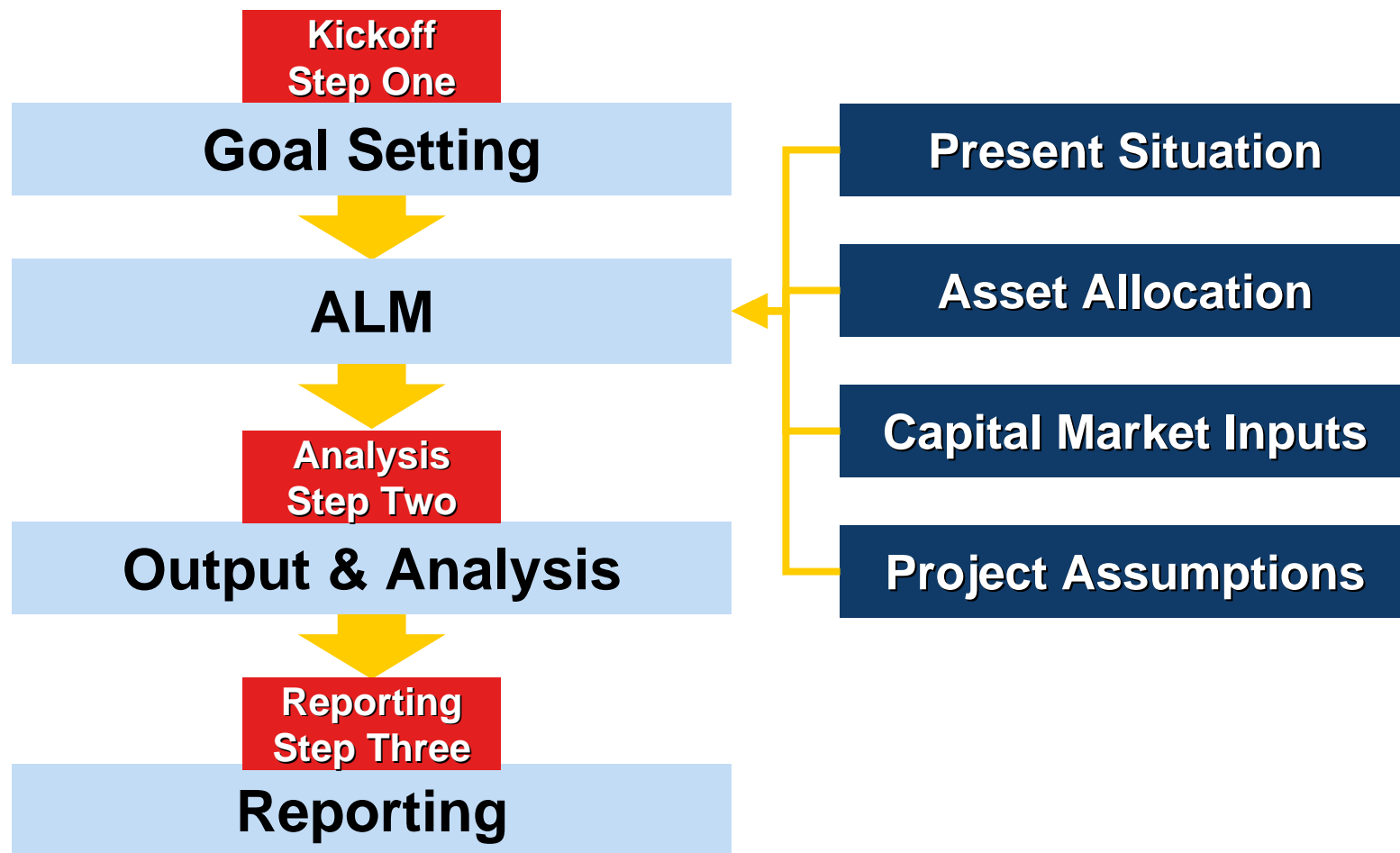


A Useful Tool: Asset Liability Modeling

- Common financial metrics
 - Cash funding requirements
 - PPA funded levels
 - Credit balances
 - Liquidity
 - Financial statement impact
 - PBGC variable premiums

A Useful Tool: Asset Liability Modeling

- Asset Liability Modeling Approach



Implementation

Ongoing Asset Liability Management

Dynamic Financial Management

- Developing the ultimate goal and dynamic glide path
- Implementation
 - Periodic monitoring of funded positions and risk and portfolio adjustments
 - Portfolio adjustments in response to hitting predefined triggers
 - Ongoing monitoring of asset class characteristics and manager performance drives adjustments to the allocation of active management fees
 - Periodic asset liability modeling updates

Ongoing Asset Liability Management

Dynamic Financial Management – Glide Paths

Illustrative Glide Path: 100% Portfolio



Current Situation

- Funded status volatility = 10.0%
- Asset allocation:
 - 35% fixed income
 - 55% equities
 - 10% alternatives
- Low liability interest rate hedge

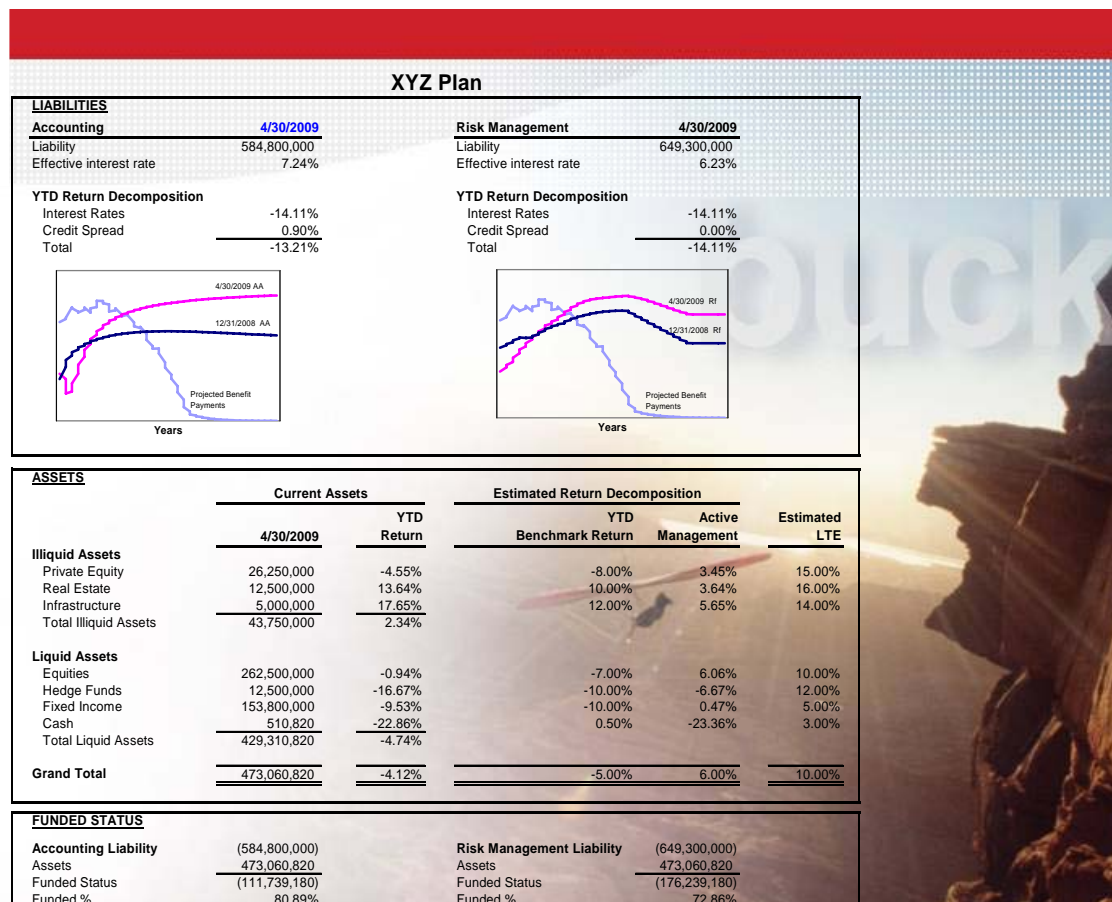
Ultimate Goal

- Funded status volatility = 2-4%
- Asset allocation:
 - Significant cash and long-duration treasuries
 - Low equity exposure
 - Spend risk budget on alternatives
- Liability interest rate hedge

- Improve Liability Tracking Error by at least x% per annum
- Reduce equity exposure by y% per annum
 - If the market declines, no rebalance is completed
 - If the market improves, rebalance assets and reduce equity exposure by additional y% per annum
- Degree of hedging – recommend interest rate triggers as well as time triggers

Ongoing Asset Liability Management

Dynamic Financial Management Dashboard



Case Studies

Asset Liability Management

Case Study Synopsis

- Evaluation of current and alternative investment strategies
 - Improve risk/return through alternative assets (e.g., hedge funds)
 - Longer-term portfolio de-risking through increased fixed income exposure
 - Evaluating the merits of a cash based liability interest rate hedge versus an overlay strategy
- Funding policy analysis
 - Compare the post-PPA minimum required contribution to Funding Target Attainment (FTAP) maintenance policies

Asset Liability Management

Case Study Synopsis

- Plan design – evaluate the impact of investment and funding strategies as part of plan redesign
 - Change in liability growth pattern and liquidity needs when plan changed to a cash balance plan from a final average pay plan
 - Change in emerging liabilities when a plan is closed to new entrants or frozen
- Demographic analysis
 - Evaluate the impact of alternative HRs

Conclusions

- Pension financial management requires understanding pension financial drivers
- Pension risk is managed relative to pension liabilities
- Asset liability management facilitates understanding the key drivers of pension risk
- Asset liability modeling is a valuable tool for understanding pension risk

Who to Contact

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Questions & Answers

Thank You

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