



GLOBAL MEGATRENDS

Today, and over the foreseeable future, a series of events – call them global megatrends – will have a profound impact on the world economy. Each issue of Point of View will share insight into these trends and how the institutional investment community is preparing to address them.

THE MOVE TOWARD DC PLANS

Defined contribution plans are gaining favor with employers around the globe. And why not? They're easier to implement than defined benefit plans, less costly to maintain and contain features that are popular with many employees. Between 1985 and 2004, the number of DC plans soared from 30,000 to more than 420,000.¹ Defined contribution assets accounted for a quarter of total pension assets worldwide in 2006, with growth estimated at about 1% per year.² Many pundits, and even some plan sponsors, however, are wondering if the pendulum has swung too far. After all, DC plans have some shortcomings, whereas DB plans have valuable features that provide a much-needed safety net for workers. Are there some options that include the best of both worlds? That's likely to be a subject of discussion and debate in many circles for years to come.

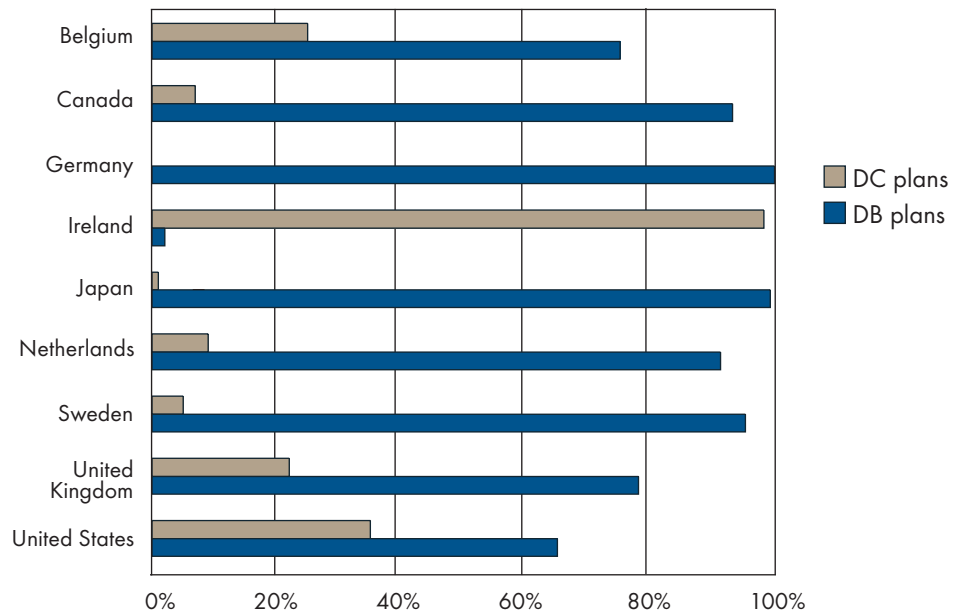
¹Source: Pension Benefit Guarantee Corporation

²Source: Pensions & Investments, February 6, 2006

Defined Benefit Versus Defined Contribution in Occupational Plans, 2004

The Global Picture

The retirement landscape worldwide is shifting as DC plans grow in popularity, according to the latest report from the Organisation for Economic Co-operation and Development. The number of occupational DC plans has been multiplying in countries such as the United States and Ireland. Meanwhile, in many other countries such as Canada, Japan, the Netherlands and Sweden, DB assets still represent more than 90% of total occupational pension assets.



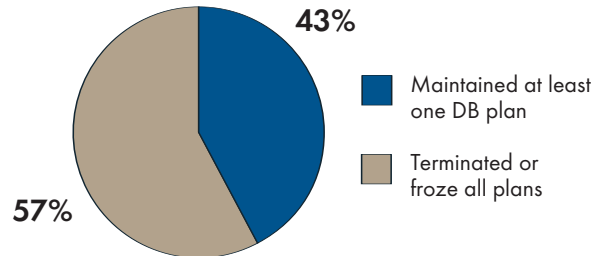
Source: Organisation for Economic Co-operation and Development, "Pension Markets in Focus," October 2006

The Pension Freeze

The number of 1,000 largest U.S. firms that have frozen or terminated DB plans nearly tripled to 113 in 2005, from 34 in 2001. But as the pension freeze breakdown chart (right) shows, of the 113 sponsors with frozen or terminated plans, 43% maintained at least one active DB plan.

FORTUNE list	Number of defined benefit plan sponsors	Number of plan sponsors with frozen or terminated plans
2005	627	113
2004	627	71
2003	633	45
2002	624	39
2001	638	34

Pension Freeze Breakdown



Source: Watson Wyatt Worldwide

The U.K. Snapshot

In the United Kingdom, funding and regulatory issues are prompting the growth of defined contributions plans.

Pension deficits remain volatile: The aggregate deficit for FTSE 100 DB plans in the U.K. reached a high of £54 billion in January 2006 and hit a low of £29 billion three months later. (The deficit was £46 billion as of September 2006, according to the *Financial Times*.)

Impact on corporate balance sheets: Under IAS19 (an international accounting standard for employee benefits), DB deficits are recorded on balance sheets as debt or liabilities.

Returns insufficient to plug hole: DB plans remained underfunded due to falling bond yields and updated mortality assumptions, despite strong investment returns in 2005.

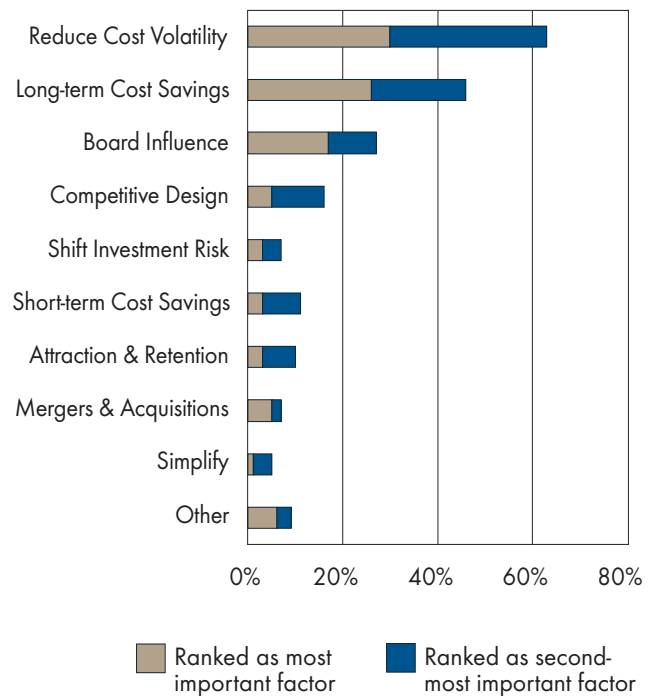
Buyouts present costs, opportunity: Under U.K. legislation, companies can eliminate obligations to their DB scheme through a “buyout” measure — or by paying insurance companies to assume the pension liabilities. (The idea is that companies can transfer liabilities from their books and onto insurance companies.) The total buyout cost across FTSE 100 companies is estimated to be about £500 billion and represents a net shortfall of more than £175 billion.

More pension scheme closures likely: Some observers believe the Pensions Act 2004 in the U.K. could hasten the demise of pension schemes, as companies are forced to pour more cash into the plans.

Source: Lane, Clark & Peacock, *Accounting for Pensions 2006*

The U.S. Perspective

According to a recent study, two-thirds of S&P 500 firms still offer DB plans, but the trend toward freezing or terminating plans continues to rise. In 2006, about two-thirds of plan sponsors cited cost volatility as one of the most important factors for changing their plan designs, and 30% of sponsors ranked it as the most important factor.



Source: Mercer Human Resource Consulting