

Index	Estimated Weights %	Total Return		
		QTD %	YTD %	Last 12 Months %
Ryan Labs Cash	5	0.10	0.19	0.45
Lehman Aggregate	30	3.49	5.33	9.52
S&P 500	60	-11.43	-6.66	14.41
MSCI EAFE Int'l	5	-13.75	-12.94	6.37
Asset Allocation Model	100	-6.60	-2.98	12.16
Ryan Labs Liability (PPA)	100	8.79	10.45	22.82
Assets – Liabilities (PPA)		-15.39	-13.43	-10.66
Ryan Labs Liability (FAS158)	100	10.22	11.90	21.96
Assets – Liabilities (FAS 158)		-16.82	-14.88	-9.80
Ryan Labs Liability (TSY)	100	18.39	17.74	13.03
Assets – Liabilities (TSY)		-24.99	-20.72	-0.87

With credit continuing to rally, PPA liabilities gained another 4.01% in the month of June to finish with a YTD return of 10.45%. The 2nd Quarter proved to be painful for both assets declining and liabilities rallying. The Quarter closed with assets down –6.60%, and the difference between assets and liabilities for the quarter being –15.39%.

The average U.S. pension portfolio in America, estimated at 65% equities and 35% fixed income, has returned -2.98% YTD through June 30, 2010. The average pension asset portfolio returned 12.16% over the last 12 months. Over this same time period, liabilities have rallied 10.45% YTD, and the trailing 12 months have seen liabilities on a PPA basis rise by 22.82%. Funding on a YTD PPA basis ended June at 68.40%, down from the May YTD funding ratio of 72.95%.

On June 25, 2010, President Obama signed the Preservation of Access to Care for Medicare Beneficiaries and Pension Relief Act. This act provided accounting relief for ERISA plans that fall under the Pension Protection Act. Under the Relief Act, defined benefit plans will be allowed to stretch out amortization periods for investment losses for two of the years between 2008 and 2011, either over a period of up to 15 years or over a nine-year period, at the option of the plan sponsor. The prior version of the PPA required plans to amortize their investment losses over seven years. However, what this Act does not change is the economics behind pension liabilities.

Regardless of the discount mechanism (i.e., PPA yield curve, FAS 158 yield curve, GASB ROA, etc.), smoothing, or amortization, the underlying economics of a defined benefit plan are that when \$1 of benefits needs to be paid out, \$1 of assets must be used to pay it. With the PPA/FAS 158/GASB yield curve being uninvestable, there are no accounting or actuarial techniques that can or will amortize or smooth \$.68 (current estimated PPA funding ratio) into \$1 if there is a shortfall when a benefit must be paid.

From an economic perspective, it becomes important for CFO's and Finance Directors to understand that just because a liability is priced at a risk premium, the risk premium will not always be realized when it's time to pay out a benefit. This becomes a significant issue when looking to implement a risk management strategy based on a PPA/FAS 158/GASB pricing methodology. Simply stated, the PPA and FAS yield curves cannot be hedged due to the fact that there is no credit available beyond 15 years in duration, and the GASB ROA cannot be hedged as there are no guaranteed investments that can earn 7.5% to 8.5% per year. When implementing a risk management LDI strategy, it is important to take into account the economics, as we have yet to find an asset or a counterparty that will make up the difference of a mispriced pension liability.

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Ryan Labs Pension Protection Act Equal Weighted Index
(RL PPA Corp A to AAA Index)

	Estimated Weights%	YTW ¹ %	MDuration (Years)	YTD Returns %	Last 12 Month Returns %
2 Year Corporate	25	1.75	1.86	2.02	6.09
5 Year Corporate	25	3.35	4.43	5.05	12.11
10 Year Corporate	25	4.40	7.00	7.03	16.36
30 Year Corporate	25	5.41	13.02	10.07	19.41
RL PPA Index ²	100	4.13	16.98	10.45	22.82

Ryan Labs FAS 158 Pension Protection Expense Equal Weighted Index
(RL FAS 158 Corp AA to AAA Index)

	Estimated Weights%	YTW ¹ %	MDuration (Years)	YTD Returns %	Last 12 Month Returns %
2 Year Corporate	25	1.43	1.86	2.24	6.20
5 Year Corporate	25	2.90	4.31	5.55	11.62
10 Year Corporate	25	3.89	7.42	9.43	15.50
30 Year Corporate	25	5.51	13.06	10.34	21.97
RL FAS158 Index ²	100	3.82	16.85	11.90	21.96

1. *Effective Annualized Yield to Worst*
2. *Equal Weighted Index*

Index	Weights	'00	'01	'02	'03	'04	'05	'06	'07	'08	'09	06/'10
Ryan Labs Cash	5%	6.57	5.01	1.92	1.19	1.27	3.17	4.89	5.22	3.01	0.51	0.19
Lehman Aggregate	30%	11.63	8.44	10.25	4.10	4.34	2.43	4.33	6.96	5.24	5.94	5.33
S&P 500	60%	-9.10	-11.89	-25.15	28.68	10.88	4.91	15.79	5.50	-37.01	26.45	-6.66
MSCI EAFE Int'l	5%	-13.87	-21.11	-15.64	39.17	20.70	14.02	26.87	11.62	-43.06	32.45	-12.94
Asset Allocation Model	100%	-2.50	-5.42	-13.49	20.04	8.93	4.61	12.25	6.35	-24.49	19.43	-2.98
RL PPA Liability		11.79	14.39	27.91	6.59	10.06	4.77	1.18	2.32	3.97	19.21	10.45
Return Difference		-14.29	-19.81	-41.40	13.45	-1.13	0.17	11.07	4.03	-28.46	0.22	-13.43
Funding Ratio (RL PPA)		149.13	123.31	83.40	93.92	92.95	92.80	102.96	107.01	77.72	77.87	68.40
Liabilities (TSY)	100%	26.56	3.63	17.36	1.04	11.40	12.23	0.17	11.53	59.13	-34.30	17.74
Return Difference		-28.79	-9.04	-30.86	19.01	-2.47	-7.62	12.08	-5.17	-83.62	53.74	-20.72
Funding Ratio (Economic)		100.20	91.46	67.41	80.09	78.32	73.00	81.80	78.01	37.02	67.29	55.45

Notes: RL PPA liability curve is the spot curve of the replication of IRS PPA curve (US credit A to AAA).

RL Treasury liability curve is the proxy for economic liabilities.

Assumptions :Normal costs = annual contributions

No benefit enhancements

Assets portfolio rebalanced monthly

The material presented and calculated here is based on information considered reliable. Ryan Labs does not represent that it is accurate or complete.

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