

Index	Estimated Weights %	Total Return		
		QTD %	YTD %	Last 12 Months %
Ryan Labs Cash	5	0.04	0.05	0.29
Barclays Aggregate Index	30	2.06	2.37	7.47
S&P 500	60	-2.74	9.49	5.45
MSCI EAFE Int'l	5	-6.85	3.38	-13.46
Asset Allocation Model	100	-1.31	6.67	5.20
Ryan Labs Liability (PPA)	100	5.56	4.47	25.66
Assets – Liabilities (PPA)		-6.87	2.20	-20.46
Ryan Labs Liability (FAS158)	100	12.27	10.60	33.21
Assets – Liabilities (FAS 158)		-13.58	-3.93	-28.01
Ryan Labs Liability (TSY)	100	12.19	4.25	34.16
Assets – Liabilities (TSY)		-13.50	2.42	-28.96

In last month's A/L Watch, a brief overview of the pension related portions of SB 1813, the Moving Ahead for Progress in the 21st Century Act, was provided. Just after Independence Day, on July 6, 2012 President Obama signed this bill (added to the 6/30 A/L Watch for timeliness). The impact of Section 40312, Pension Funding Stabilization, is that funding relief is granted to plan sponsors through the stabilization of PPA interest rates via a floor and ceiling on the

"If the calendar year is:	The applica- ble min- imum per- centage is:	The applica- ble max- imum per- centage is:
2012	90%	110%
2013	85%	115%
2014	80%	120%
2015	75%	125%
After 2015	70%	130%."

current year's rate. The floor and ceiling are calculated using the 25 year average of PPA interest rates preceding the year at issue, per the table to the left.

For 2012, these changes are expected to increase PPA yields by 125 to 150 basis points, resulting in expected contribution reductions of 15 to 20% or more for 2012.

As Page 3 of A/L Watch shows, the strong asset returns of the RL Asset Allo-

cation Model for '09 and '10, coupled with the positive returns for '11 and the first half of 2012 have not added value to funding ratios. 2008 ended with a typical ERISA pension plan's funding ratio at 69.74%, while June 2012 ended with funding levels approximating 67.07%. Additionally, Q2 has not been kind to funding levels, whereby liabilities rallied by +5.56% while the RL Asset Allocation Model returned -1.31%. Volatility will not go away, hence the latest round of funding relief.

For risk management practitioners, the PPA has never been a rule that conforms to the reality of the market. By extrapolating the corporate yield curve further out in duration than corporate bonds exist in the marketplace, hedging all PPA funding volatility is not possible. There has been a constant disconnect between funding rules and economic reality, and now a bigger disconnect between the corporate bond market, funding rules and accounting (FAS 158) rules. As such, when implementing LDI strategies in a risk management framework, plan sponsors should be aware of this disconnect.

The Pension Funding Stabilization provision is certainly appreciated by plan sponsors. However, while the contribution calculation has changed, the underlying economics of needing to pay \$1 of assets to fund \$1 of liabilities have not. It would be beneficial to everyone if there was a strategy out there that provides returns based off of the 25 year average of corporate yields. However, there is not. Until plan sponsors are able to purchase such a product, a higher level of pension risk management can be achieved by understanding market reality and implementing strategies that do not ignore it.

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	0.99	1.83	1.85	1.78
5 Year Corporate	25	2.04	4.54	4.17	5.39
10 Year Corporate	25	3.04	7.69	4.30	10.60
30 Year Corporate	25	4.26	13.91	5.95	20.65
RL PPA Index ²	100	3.48	15.29	4.47	25.66

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	0.62	1.79	1.00	1.68
5 Year Corporate	25	1.47	4.69	3.05	6.66
10 Year Corporate	25	2.53	7.94	3.87	13.42
30 Year Corporate	25	3.86	14.35	6.20	22.58
RL FAS158 Index ²	100	3.02	16.03	15.12	36.13

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

Index	Weights	'00	'01	'02	'03	'04	'05	'06	'07	'08	'09	'10	'11	06/'12
Ryan Labs Cash	5%	6.57	5.01	1.92	1.19	1.27	3.17	4.89	5.22	3.01	0.51	0.35	0.39	0.05
Barclays Aggregate	30%	11.63	8.44	10.25	4.10	4.34	2.43	4.33	6.96	5.24	5.94	6.54	7.84	2.37
S&P 500	60%	-9.10	-11.89	-25.15	28.68	10.88	4.91	15.79	5.50	-37.01	26.45	15.06	2.12	9.49
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	8.14	-12.19	3.38
Asset Allocation Model	100%	-2.50	-5.42	-13.49	20.04	8.93	4.61	12.25	6.35	-24.49	19.43	11.87	3.26	6.67
RL PPA Liability		7.72	15.40	24.17	7.30	11.22	5.95	2.36	2.39	10.44	6.34	13.73	21.13	4.47
Return Difference		-10.22	-20.82	-37.66	12.74	-2.29	-1.34	9.89	3.96	-34.93	13.10	-1.86	-17.87	2.20
Funding Ratio (RL PPA)		144.98	118.83	82.78	92.61	90.70	89.55	98.20	102.00	69.74	78.33	77.05	65.68	67.07
Liabilities (TSY)	100%	23.91	3.91	16.73	1.57	9.96	10.08	0.85	10.81	42.48	-25.71	9.41	31.08	4.25
Return Difference		-26.41	-9.33	-30.22	18.47	-1.03	-5.47	11.40	-4.46	-66.97	45.14	2.46	-27.82	2.42
Funding Ratio (Economic)		96.23	87.60	64.92	76.72	76.00	72.23	80.39	77.16	40.89	65.74	67.22	52.95	54.18

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

We believe the information provided here is reliable, but do not warrant its accuracy or completeness. This material is not intended as an offer or solicitation for the purchase or sale of any financial instrument. The views and strategies described may not be suitable for all investors. This material

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