Pension Finance Watch

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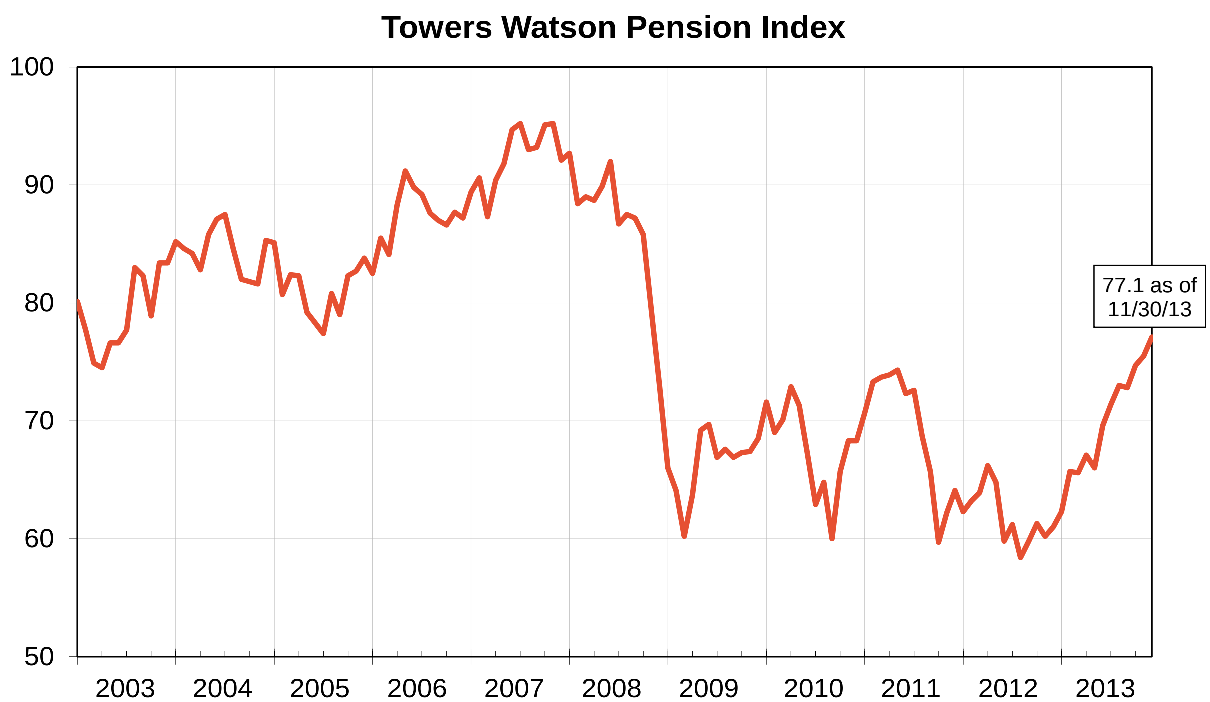
November index reaches five-year high

Capital markets were favorable on all fronts in November. Positive equity returns and an upward movement in interest rates resulted in a 2.1% increase in the Towers Watson Pension Index. The index value has now moved up almost 24% for the year, to 77.1 -- a level last seen in October 2008.



About this report

Pension Finance Watch is designed to support our clients in the ongoing financial management of their U.S. retirement plans. The report tracks the value of the Towers Watson Pension Index in a series that was initiated in 1990.

The Pension Index reflects the asset/liability performance of a hypothetical benchmark pension plan, and provides an indicator of capital market effects on pension plan financing. Individual plan results will vary based on such factors as portfolio composition, investment management strategy, liability characteristics and contribution policy.

If you have questions or comments about this report, please contact
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Investment returns

The equity portfolio returned 2.7% in November. Positive equity returns in nine of 11 months have driven the equity portfolio up over 28% for the year. Rising yields implied negative fixed income returns for the month, and both long bond indexes remain deep in negative territory for the year.

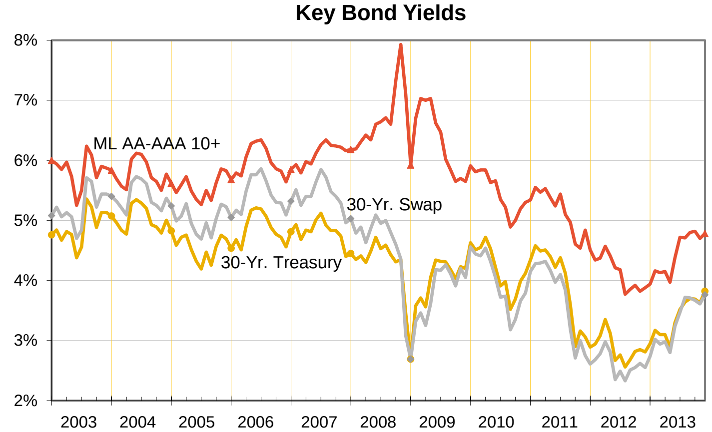
Asset Class Returns	*November 2013*	*YTD*	*Last 12 Months*
Stock Returns			
S&P 500 (Large Cap)	3.1%	29.1%	30.3%
Russell 2500 (U.S. Small/Mid-Cap)	2.7%	33.4%	36.9%
EAFE (International)	0.8%	21.0%	24.8%
Fixed Income Returns			
3-Month T-Bills	0.0%	0.1%	0.1%
Long Treasury Bonds	-2.5%	-10.9%	-12.7%
Barclays Capital Aggregate Bond Index	-0.4%	-1.5%	-1.6%
Long Corporate Bonds (AAA/AA)	-1.0%	-7.5%	-8.0%

Interest rates

Long corporate yields increased in November and are up over 80 basis points for the year. Long Treasury yields moved up even more, so that the credit spread (the incremental yield on long corporate vs. long government bonds) fell below 1.0%.

Bond Yields	*Nov. 2013*	*Dec. 2012*	*Nov. 2012*
U.S. Treasuries			
30-Year	3.82	2.95	2.81
10-Year	2.75	1.78	1.62
3-Month	0.06	0.05	0.08
30-Yr. Swap Rate	3.76	2.74	2.55
Corporate Bonds			
ML AA-AAA 10+	4.78	3.94	3.88
Citigroup HG Credit	4.72	3.83	3.77
Moody's Aa	4.62	3.75	3.62
Barclays Capital Agg.	2.33	1.74	1.69

Key Bond Yields



Effect on pension index

The Towers Watson Pension Index tracks the performance of a hypothetical pension plan invested in a 60% equity/40% fixed income portfolio. That portfolio recorded a 1.4% return for November. We track two alternative investment portfolios with different mixes of equity/fixed income. Monthly returns on the 20% and 60% fixed income portfolios were 2.0% and 0.8%.

We have also begun tracking a second version of the 60% fixed income portfolio that incorporates longer duration fixed-income investments – that portfolio returned 0.1% for the month. It trails the shorter duration portfolios over the trailing 9 and 12-month periods, with the performance shortfall obviously attributable to increases in long bond yields over these periods.

Pension liabilities as defined for U.S. accounting purposes are typically measured based on yields on high quality corporate bonds as of the measurement date. Using our RATE:Link methodology, which matches those corporate yields to projected cash flows, the benchmark discount rate was determined at 4.83% -- up 9 basis points for the month.

Similar to bond prices, values for pension obligations move in the opposite direction of interest rates. Our liability index (based on projected benefit obligations) declined 0.8% in November, reflecting the offsetting effects of interest accumulation and the increase in the discount rate.

The changes in asset and liability values caused the Towers Watson Pension Index to move up 2.1% to 77.1.

Pension Index Results

	November 2013	*YTD*	*Last 12 Months*
Benchmark Portfolio Returns			
20% Fixed Income	2.0%	22.0%	23.5%
40% Fixed Income (benchmark)	1.4%	15.8%	16.9%
60% Fixed Income	0.8%	9.9%	10.5%
60% Fixed Income (long duration version)	0.1%	5.1%	5.1%
Benchmark Plan Liability Results			
Discount Rate (at valuation date)*	4.83	3.96	3.83
Liability Growth Factor	-0.8%	-7.4%	-8.6%
Pension Index*	77.1	62.3	61.0
Percentage change	+2.1%	+23.8%	+26.4%

*Rates determined as of 11/30/2013, 12/31/2012 and 11/30/2012, respectively.

Definition of terms

Asset Class Returns

- Total return incorporates the combined effect of price changes and interest/dividend income; this may differ from index results which are based only on price changes.
- The Russell 2500 Index tracks companies ranked 501 to 3000 ordered by market value of equity; these are considered small and mid-capitalization stocks.
- EAFE refers to the Morgan Stanley Capital International Europe, Australasia, Far East Index of equity securities; total return is reported in U.S. dollars, which includes the effect of currency changes.
- 3-Month T-Bill returns are based on the Citigroup 3-Month Treasury Bill Index.
- Long Treasury Bond returns are based on the Barclays Capital Long Treasury Bond Index.
- Long Corporate Bond returns are based on the Citigroup High Grade Credit Index (as described above).

Bond Yields

- Treasury yields are constant maturity yields reported by the Federal Reserve.
- 30-year swap rate is that applicable for a fixed rate payer in return for receiving three month LIBOR, as reported by the Federal Reserve.
- ML 10+ AA-AAA 10+ Index includes issues with 10+ years to maturity and AA or AAA ratings from the Merrill Lynch U.S. Corporate Master Index.
- Citigroup High Grade Credit Index includes issues with 10+ years to maturity and a minimum rating of AA-/Aa3.
- Moody's Aa Corporate Bond Index is a component of Moody's Long Term Corporate Bond Indexes; included bonds have maturities of 20+ years.
- Barclays Capital Aggregate Bond Index covers the broad range of investment grade bonds, including government and corporate securities (minimum grade Baa) and mortgages.
- Note: bond yields are stated as yields to maturity, on a bond-equivalent basis (reflecting semi-annual coupons).

Benchmark Portfolio Returns

- The benchmark portfolio reflects a diversified asset allocation of 60% equity (40% large cap, 10% small/mid-cap, 10% international) and 40% fixed income (35% BC Agg., 5% T-bills). This generally aligns with the average portfolio for the 300 large companies included in Towers Watson's benchmarking database.
- Alternative portfolios with 20% and 60% fixed income allocations are constructed with similar asset class ratios within their equity and fixed income segments.
- The 60% fixed income-long duration portfolio includes a similarly constructed equity segment along with a fixed income segment consisting of 27.5% long corporate bonds, 27.5% long Treasury bonds and 5% T-bills.

Benchmark Discount Rate

- The discount rate is determined for our benchmark plan each month using a yield curve developed based on high-quality corporate bonds (10th-90th percentiles). This calculation uses our RATE:Link methodology to develop an appropriate discount rate based on the benchmark plan's projected cash flows. Higher or lower discount rates might be appropriate for other plans.*

Liability Growth Factor

- The benchmark plan is based on a traditional final-pay based formula and covers a relatively mature population. Roughly one-half of the plan's obligations are related to inactive participants. The liability growth factor reflects the percentage change in the plan's projected benefit obligation due to the accumulation of interest and changes in financial assumptions.*

Towers Watson Pension Index

- The index reflects the PBO funded ratio (market value of assets/projected benefit obligation) for a benchmark pension plan. The asset value changes from month to month based on the investment performance of the 60% equity portfolio, assumed contributions and benefit payments. Liability values increase with benefit accruals and interest cost, offset by benefit payments, and are adjusted to reflect changes in financial assumptions.
- Contributions are set equal to the level of service cost for the benchmark plan. This implies that contributions offset the effect of ongoing benefit accruals; thus, the Pension Index captures the impact of capital market results alone.

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* Discount rate and salary increase assumptions are adjusted to reflect changes in market interest rates; the sensitivity of the plan's liability measure to a percentage point change in interest rates is roughly 14%. Note that plans with different designs or demographics will see different results in terms of both the level of appropriate discount rate and the impact of changes in financial assumptions. For example, account-based designs generally entail reduced liability duration, and thus a lower discount rate and less sensitivity to interest rate changes.

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