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HEADLINE: Low rates offset pension funds' equity gains

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Think the stock market's stellar performance this year means the end of the pension **funding** crisis that grabbed headlines last year?

Quite the opposite, it turns out. Corporate **pension plans** are actually getting weaker this year, analysts say, because the boost to pension assets from a rising stock market has not been able to outpace the effect of the concurrent drop of interest rates to historical lows.

Pension plans at Standard & Poor's 500 companies are expected to be underfunded by about $247 billion at the end of 2003, up from $225 billion at the end of last year, according to a recent Credit Suisse First Boston report.

Ratings agency Standard & Poor's estimates that pension underfunding at S&P 500 companies will widen to roughly $220 billion at the end of the year from $212 billion last year, said S&P analyst Howard Silverblatt.

S&P assumes 60 percent of pension assets are invested in stocks and the remaining 40 percent in fixed income assets. CSFB assumes a 65 percent equity and 35 percent fixed income mix of plan assets.

A **pension plan** is underfunded when its assets are not enough to cover its expected obligations to employees. Pension underfunding came into the spotlight last year when a prolonged bear market and falling interest rates shrank pension assets and boosted liabilities.

Several companies have diverted cash and stock to prop up their **pension plans,** while others have watched pension costs eat into earnings.

"It was a growing situation last year, it continues this year, and it should be a concern to all investors," said Silverblatt. "'How much money does my company have to put into pensions, where are they going to get the money, and what is it going to be taken out of?'"

While the bear market of the last three years was responsible for pension woes last year, low interest rates can be blamed for this year's. Interest rates are at 45-year lows after 13 rate cuts dating to early 2001.

When rates fall, the discount rate used to calculate the pension benefits a company must pay out in today's dollars also falls.

That, in turn, increases pension obligations.

Last year, the number of companies in the S&P 500 with underfunded plans rose to 334, the highest level in

10 years. That figure could rise to 340 this year, according to CSFB estimates.

Companies also face the threat of growing pension costs this year because of accounting rules designed to spread pension expense over several years.

That means the dismal performance of **pension plans** in the last three years will start showing up in profits this year.

As a result, pension costs for S&P 500 companies are expected to balloon to $19 billion from $4 billion last year, according to the CSFB report.

Congress plans to temporarily allow companies to value pension obligations with a discount rate tied to the yield on long-term, high-grade corporate bonds rather than a rate tied to the 30-year Treasury bond.

That would result in a higher discount rate, smaller pension obligations and reduced **funding** requirements.

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