



GE's unfunded pension liability spikes in 2011

Posted: February 24, 5:49 PM

General Electric Co. said in a 10-K filed Friday that its principal pension plans had an unfunded liability of \$18.4 billion as of Dec. 31, more than double the \$7.1 billion reported a year earlier.

The above headline just crossed my desk, it is the lead for an article in Pensions & Investments, a trade publication that tracks trends, events, and goings-on in the pension world. One thing that has captured my interest lately is the effect of Fed actions – in the form of rock bottom interest rates up and down the yield curve – on the funding status of private pensions. As the Fed lowers long term interest rates through the purchase of bonds, it drives up the cost of pension funding because private pensions must use a lower discount rate to calculate their current contribution. This is where GE's release enters the story.

GE reported that of the \$8.5 billion in higher pension liability, roughly \$6.8 billion was due to a change in the discount rate used to determine current funding status. GE plans on contributing \$1 billion to its fund this year, which would leave the fund at least \$17.4 billion under-funded, all things being equal. Of course, the "all things being equal" statement would also require GE to earn the 8% rate of return that it assumes on its assets.

As the US economy continues to under-perform GDP growth targets and US housing remains depressed, it is clear that the Federal Reserve intends to hold interest rates as low as possible for years to come. This will only drive private pensions further down in their funding status, which will eventually have to be made up through corporate contributions. Where do the contributions come from? Current earnings. With year-over-year comparisons getting more difficult, a drag on earnings due to higher pension funding would not be welcome.

Sincerely,

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