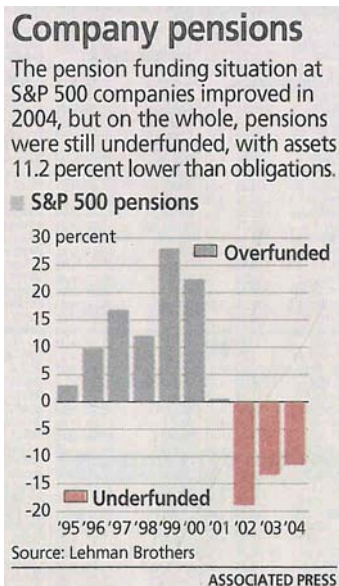


# Unfunded Liabilities & Unlearned Lessons

May 23, 2005

The action of United Airlines, to pass along to you and us the unfunded liabilities of their defined benefit plan, came as no surprise. What was a surprise was the ease with which the judge in their bankruptcy case dictated the transfer. As we are sure you know, this obligation becomes ours through a government agency that came into being in 1974. The chart below is Lehman Brothers estimate of the unfunded liabilities of those companies that comprise the S&P 500. If one were to include all public companies with defined benefit plans, the total unfunded is \$450 billion. UAL has now gone again to their employees for wage and benefit deductions. But for us it's too late, we are stuck with managements over promising to their employees for low these many years.



On another matter, there was a rumbling that some of the thousands of hedge funds (\$ 1 trillion) were in trouble. There was also a report that the hedge funds had a poor year in 2004 and are following it up with another this year. We mention this in that hedge funds have become the darlings of the pension fund consultants as common stocks and bonds have not worked well for the past 5 years. The idea is, we guess, that one cannot find asset classes which will deliver positive returns, there fore buying long and selling short at the same time is the way to Nirvana for such accounts. There is a huge lesson to be learned here – but we are not sure anyone is paying attention. The critical question is when will they do so? There is just so much we taxpayers can take. Do you realize that most pension funds assume a rate of return of 8%? Where do they get this rate? From their consultants of course. However, in our opinion, as so stated in our piece “A contrarian view” published in 2002 we projected a drought of income for the foreseeable future. Unfunded liabilities are destined to increase unless the various corporations increase dramatically their cash contributions. The Nobel Prize winners in economics from academia and the pension consulting industry from the nations leading MBA schools have sold us down the drain!