



## Pension Update Conference Call Thursday, September 25, 2014

### **PARTICIPANTS**

#### **Corporate Participants**

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**Shep Dunlap** – Vice President, Investor Relations  
**Gino Bonanotte** – Executive Vice President and Chief Financial Officer  
**Rob O’Keef** – Corporate Vice President and Treasurer

#### **Other Participants**

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**Keith Housum** – Analyst, Northcoast Research Partners, LLC  
**Tavis C. McCourt** – Analyst, Raymond James & Associates, Inc.  
**Kulbinder Garcha** – Analyst, Credit Suisse Securities, LLC  
**Ashwin Kesireddy** – Associate Analyst, JPMorgan Securities LLC

### **MANAGEMENT DISCUSSION SECTION**

**Operator:** Good morning and thank you for holding. Welcome to the Motorola Solutions Conference Call. Today’s call is being recorded. If you have any objections, please disconnect at this time. The presentation is currently posted on the Motorola Solutions Investor Relations website. In addition, a replay of this call will be available approximately three hours after the conclusion of this call over the internet. The website address is [www.motorolasolutions.com/investor](http://www.motorolasolutions.com/investor). At this time, all participants have been placed in a listen-only mode and a line will be open for your questions following the presentation. I would now like to introduce Mr. Shep Dunlap, Vice President of Investor Relations. Mr. Dunlap, you may begin your conference.

#### **Shep Dunlap, Vice President, Investor Relations**

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Thank you. Good morning and thank you for joining us today as we discuss changes to our U.S. pension plan. With me today are Gino Bonanotte, Executive Vice President and CFO; and Rob O’Keef, Corporate Vice President and Treasurer. Today, we will only be discussing material and answering questions related to our pension plans and transaction announced today. As a reminder, we will provide our full earnings results on November 4<sup>th</sup> and I would ask that you hold questions on the quarter until that time.

Next, I’d like to remind you that all statements made during this call that relate to future results and events are forward-looking statements that are based on our current expectations. Actual results and events could differ materially from those projected and the forward-looking statements because of a number of risks and uncertainties which are discussed in our annual and quarterly SEC filings and in the cautionary statement contained in our press release and on our website. We see no obligation to update our forward-looking statements. With that, I’d like to turn it over to Gino.

#### **Gino Bonanotte, Executive Vice President and Chief Financial Officer**

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Thank you, Shep, and thank you to all of you who are joining us on short notice today. This is a pivotal time at MSI as we continue to take a number of actions aimed at addressing our legacy operation and call structure. We’re working to reduce complexity in a number of ways, improving sales and R&D efficiency, real estate footprint, and IT complexity as well as back office functions.

With respect to the balance sheet, the major area of legacy burden is our pension obligation. Today's announcement represents aggressive action to address one of the company's largest legacy issues - it's outsized global pension liabilities. The actions we're announcing today will reduce our U.S. pension liability by \$4.2 billion or approximately 50% while retaining existing benefits for all of our plan participants. It will significantly reduce volatility and improve visibility to cash flow by mitigating the risk of large unexpected cash calls to fund legacy pension obligations.

Finally, inclusive of the incremental funding which Rob will detail later in the call, we'll eliminate required contributions over the next five to six years while ensuring the plan remains on solid footing. We're taking this action now for several reasons. First and foremost, our global pension liabilities are too large relative to the scale of the business. Secondly, timing and market conditions are favorable now in terms of historically low interest rates and an attractive market for annuities from insurance companies. Finally, I'm very pleased we were able to diffuse the liabilities below PBO value and well below economic valuation. This is an unprecedented outcome for this type of transaction.

Now, I'd like to turn the call over to Rob to take you through the key details of today's announcement and the action surrounding our U.S. pension plan.

#### **Rob O'Keef, Corporate Vice President and Treasurer**

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Thanks, Gino. I'd like to tee this up with just a brief overview of what we're doing here. There are three key components to the actions we're taking. First, we're planning to fund \$1.1 billion of cash into the U.S. plans this calendar year. That's an incremental \$800 million above the \$300 million or so minimum that we've talked about all year long. This incremental funding will ensure the plan remains on solid footing and coupled with the other actions we're going to discuss will eliminate required contributions, as Gino said, over the next five to six years bringing up cash for more productive uses.

The second component is lump sums. We'll be offering up to a \$1 billion of cash lump sum payments to our terminated vested participants, targeting a reduction in that portion of the plan liability of \$1.1 billion. We'll spend more time with you on that in a minute. Third, we've entered into an agreement with Prudential Insurance Company of America to purchase annuity contracts for the retiree population to reduce our liability by an additional \$3.1 billion. Again, we'll take you through all this in more detail in a minute. These are just the headlines.

Benefits will not change for participants as a result of these actions. Benefits will remain secure. Both payment options and/or the form of payment will change. From a company perspective, the net result is that our U.S. pension liability will be reduced by about \$4.2 billion which reduce earnings and cash flow volatility and significantly reduce the balance sheet. This is a rare case where all the constituents win and we'll talk more about that, too. These transactions are good for the company. They're good for the retirees. They're good for the term-vested and active participants.

The retirees maintain a secure benefit backed by a highly rated and regulated insurance company. The term-vested participants receive a new option, an option to receive lump sum or annuity payments. All participants that remain in the plan will benefit from a well-funded, smaller, and more manageable plan. The company, by reducing our U.S. liability by \$4.2 billion - as Gino mentioned about 50% - will benefit from significantly reduced earnings and cash flow volatility and improved financial flexibility. All this achieved with positive economics.

Next slide, I'm talking about U.S. pension actions taken. This slide provides some context. These are actions we're taking. These are really the next steps in the de-risking path we've been marching down.

We've already taken a number of important steps to manage our exposure. As a first step in containing the growth of the obligation, the U.S. pension plan was closed to new participants in 2005 and benefits were frozen for existing participants in 2009. That's a critical first step. The company has also committed a significant amount of capital over the years to fund this obligation. Looking back 10 years, we've contributed approximately \$3 billion into the U.S. pension plan.

Unfortunately, similar to many plans, a considerable sum was lost in the market collapse of 2008 and 2009, and we recognize this happens from time to time. I think the peak losses were 40% in those years and it has taken some time for the plan to recover, but the plan has recovered. We've also taken actions similar to other plan sponsors to better match plan assets with the liabilities and employ a liability-driven investing technology to further manage the risk within the plan. Now with today's actions, we're taking the next steps in de-risking the plan. These are the most aggressive and significant reductions in the gross liabilities.

Slide five provides an overview of the scale of the issue we're dealing with here. This looks at the global plans and the U.S. plans. At the end of 2013, the company's total global pension liabilities measured by GAAP PBO was about \$9.3 billion covering 95,000 participants with a global funded status of 82%, a deficit of \$1.6 billion. The U.S. plan which is going to be our focus today is about 80% of the global pension footprint. It covers 80,000 participants and at year-end, carried a PBO of about \$7.3 billion which was funded at 83% with a deficit of \$1.2 billion. Notably, the U.S. plan is in a significantly better funded position than it was a year prior in 2012. When the funded status was 65%, the deficit was about \$2.9 billion. Again, this is the type of volatility we're looking to mitigate with these actions.

The liabilities you see on this chart represent the legacy of a company that once had six major businesses, \$45 billion in revenue, and 150,000 employees. We are not that company anymore. Simply put, it's not prudent for a pure-play company with \$6 billion of revenue and about 15,000 employees to carry a \$9 billion to \$10 billion of global pension liability, servicing 95,000 participants. We do have strong confidence, and we'll talk more about that, that the new MSI is well-positioned to continue to generate robust earnings and free cash flow. However, it's not prudent to expose this smaller balance sheet to outsized risk and volatility that a pension liability of this scale can create. It doesn't make sense.

Flipping to slide six of our posted presentation, there's a lot of numbers here. I'm going to walk you through the pension maze for a few minutes, just to make it perfectly clear what's happening here. Focusing on the U.S. pension obligation which is where the action is, this chart walks from year-end 2013 status at the top of the table, down to an estimate of pro forma status following the transactions we're talking about today. That's the last line of the table.

Starting from the top of the table, we displayed the year-end 2013 funded status that you just saw. Since that time, interest rates have moved down - and again, we can take you through that - the liabilities, accrued interest as it always does, and actuarial estimates such as mortality have moved around as they always do, which has increased our liability by about \$1.1 billion to \$8.4 billion which is where it stands today. That's the U.S. liability. Additionally, the year-to-date returns in our asset portfolio, net of benefit payments is about \$300 million, increasing plan assets by that amount which you see in the second line as well.

Lastly, in order to provide you with a clean pro forma status prior to the risk transfer actions we want to focus on, in the third line we're adding this year's minimum required contributions of \$300 million which we would've contributed to the plan in any case, in the absence of these transactions. In the middle of table, you see the pro forma pre-transaction status. It's a PBO of about \$8.4 billion with \$6.7 billion of assets. This should be viewed as our best estimate of the liability valuation and overall plan status just

prior to the risk transfer actions we're discussing today so we can focus you on precisely on what's happening today.

Focusing now in the impact of the transaction, summarized in the bottom half of the table, as part of the de-risking, the company will voluntarily contribute an incremental \$800 million of cash into the plan. Recall that in August, we borrowed \$1.4 billion of debt, taking funding risk off the table, the majority of which was earmarked for this purpose.

Finally, when the transactions close in December, and now I'm pointing you to the second-to-last line on the table, the plan will transfer liabilities with a combined PBO of about \$4.2 billion, along with about \$4.1 billion in assets. Specifically, upon closing – again, we'll go into this in more detail in the Q&A – but the plan will issue up to \$1 billion of cash payments to the term vested participants who elect to receive lump sum payments, reducing plan assets by a billion and reducing the PBO by about \$1.1 billion if fully subscribed.

Upon closing the annuitization with Prudential based on current market conditions and other estimates, the plan will transfer about \$3.1 billion of assets to Prudential in payment for Prudential's group annuity contract covering the 30,000 retirees with a PBO liability of about \$3.1 billion. You should note these estimates are going to move around based on many different assumptions including interest rates, mortality estimates, and other estimates. But based on our current estimates, we're settling the retiree obligation with Prudential approximately at par, which is unprecedented. And while I caution you, it's very difficult to compare these types of transactions and trades with other deals in the market - the GMs, the Verizons, the other jumbos. This is the third largest trade so those are natural places to look. Those trades did involve premiums in the 10% range and we're settling at par.

Coming back to the last line in the table here, all else equal, we would expect to reduce the U.S. liability by about \$4.2 billion or about 50% all while maintaining a funded status of about 80%. Importantly, all the way to the right of this table, we're talking about participants. Well, it's very difficult to estimate which lump sum eligible people are going to actually elect to take the lump sum. We do estimate these transactions will reduce our participant population by 40,000 to 50,000, down to a range of 30,000 to 40,000. More to come on that as we get smarter about who's taking the lump sum.

In the next slide, there are several important drivers for undertaking this transaction now. First, we're going to be a smaller company with the divestiture of Enterprise and the legacy pension liabilities have become significantly outsized relative to the scale of the remaining business. As we've said, we need to put this business on the right capital structure footing now and eliminate undue risk and volatility. Second, as a result of favorable capital market conditions, we were able to opportunistically borrow long-term capital at a very attractive rate to support the plan funding, which we did in August. Third, the market for annuities – and we'll talk more about that – is very strong right now for a lot of reasons, allowing us to deliver a favorable economic result and the fees to liabilities below PBO value and well below economic valuation. Again, these actions significantly reduce volatility and cash flow, mitigating the risk of large, unexpected cash calls to fund the plan that could disrupt our business. This position is the balance sheet to better support the new MSI and importantly, these actions improve stability for all plan participants.

Lastly, just one final note on this. Our core business is mission-critical communications. It's not managing retirement assets and liabilities. Prudential's core business is managing retirement assets and liabilities. That's where these activities belong. Our employees, our customers, our shareholders, they don't want earnings in cash flow to be whipsawed by changes in interest rates and stock prices. They don't want our ability to invest in our business to be compromised by this type of volatility. That's what you're exposed to when you run an outsized pension fund.

Prudential is fully equipped to manage these risks. That's what they get paid for. Essentially, in the way we look at this, Gino and I, what we've done here is divest a large non-core business that exposes our core business to significant risk and we've done it at a very, very economically favorable cost. Now, I'll turn it back over to Gino.

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**Gino Bonanotte, Executive Vice President and Chief Financial Officer**

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Thank you, Rob. This is a significant transaction and I'm exceedingly pleased with the outcome. I want to thank Rob, Akash Raj, our assistant treasurer; our entire Treasury team; our advisers; and our partner for the substantial work that went into executing this in really an unprecedented timeframe. It's a very important step in our efforts to simplify the company and reduce risk. These transactions enable us to minimize the risk of future cash funding requirements as we've talked about while improving the stability of the plan for all pension participants. It does so while preserving a strong funding status.

Lastly, these transactions will provide greater flexibility to move to a more efficient capital structure that supports the needs of the firm in our goal of running an appropriately leveraged balance sheet. I'll now turn the call over the Shep.

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**Shep Dunlap, Vice President, Investor Relations**

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Thanks, Gino and Rob. Let's open it up for questions now. As a reminder, please limit yourself to one question and one follow-up. Operator, can you get us started?

**QUESTION AND ANSWER SECTION**

**Operator:** Certainly. The floor is now open for questions. At this time, if you have a question or comment, please press the \* then 1 on your touchtone phone. If at any point your question is answered, you may remove yourself from the queue by pressing the # key. We do ask that while you pose your question, please pick up your handset to provide optimal sound quality. Our first question is coming from Keith Housum with Northcoast Research. Your line is open.

**<Q - Keith Housum – Northcoast Research Partners, LLC>:** Thanks, guys. I appreciate the opportunity to ask questions, and congratulations on the move. I've got to ask a question for Gino. Is there any EPS impact from this transaction?

**<A - Gino Bonanotte, Motorola Solutions, Inc.>:** No. Thanks, Keith. Thanks for the question and I'm glad you brought it up. This was not a cost-reduction exercise. It was about reducing volatility around pension obligation and improving cash flow visibility. It does not impact 2015 - in and of itself, this transaction will not impact 2015 pension expense. Obviously, as we've talked about, it certainly will impact the minimum funding requirement but does not necessarily impact expense in 2015.

**<Q - Keith Housum, Northcoast Research Partners, LLC.>:** All right, I appreciate it. A follow-up question for you. You've taken off a good chunk of liability here but why not do more? You used to have 30,000 to 40,000 retirees out there with a benefit of coming to them.

**<A - Gino Bonanotte, Motorola Solutions, Inc.>**: Yes. That's a great question. First, certainly, we don't want to risk being overfunded. This transaction reduces the size of the MSI pension liability to a level we think is manageable for us on the balance sheet, and the marginal benefit of doing more wasn't worthwhile. Rob, I don't know if there's anything you want to add.

**<A - Rob O'Keef, Motorola Solutions, Inc.>**: I think that's right, so that's one cornerstone principle. The other is really the credit rating and our cornerstone principle with our capital structure – and we can talk more about this – is maintaining an investment-grade credit rating for our customers, these long-term contracts. On and on, there are a whole lot of reasons why we need that. Doing more would've probably required putting more capital into the plan, borrowing more money to do that, and we spend a lot of time with the agencies, believe me, over the last six months in detailed discussions assessing their comfort level with how far we could push the envelope, and we pushed it as far as we can. We're comfortable we hold the rating based on these transactions. Doing more would've stressed the rating. At the right time though, looking forward, there's going to be a time and a place where we can take another bite. By the way, lagging into these transactions makes some sense, too. We're not in the business of making big chunky capital markets bets, so we're going to have plenty of opportunity with our cash flow as this business grows to do more over time.

**<Q - Keith Housum, Northcoast Research Partners, LLC.>**: Great. Thanks. I appreciate it.

**Operator**: Again, as a reminder, it is \* and 1 to ask a question today. Our next question is coming from Tavis McCourt with Raymond James. Your line is open.

**<Q - Tavis McCourt, Raymond James & Associates, Inc.>**: Hey, guys. Just wanted to confirm a couple of things. So the near-term cash out flow is \$2.1 billion – the \$1.1 billion contributed plus the \$1 billion for lump sum payment? Is that correct?

**<A - Rob O'Keef, Motorola Solutions, Inc.>**: I'd say that differently. \$1.1 billion comes from the corporate into the plan so off the company's balance sheet into the plan. We borrowed a \$1.4 billion; \$1 billion of that will go into the plan. So that is effectively self-funded and trading one liability for another, so we're not reducing corporate cash in that effect. We're just trading leverage for leverage. Number one, it's \$1 billion of company cash that has been borrowed going into the plan. The \$1 billion of the lump sums will come out of the plan, so the plan balance sheet will reduce by a billion of cash and about \$1.1 billion of liability with respect to the lump sums.

**<Q - Tavis McCourt, Raymond James & Associates, Inc.>**: Okay, got you. So just to be clear, there's no earmark of the cash coming in from the Enterprise sale for any of these activities?

**<A - Rob O'Keef, Motorola Solutions, Inc.>**: No, Tavis. There isn't.

**<Q - Tavis McCourt, Raymond James & Associates, Inc.>**: Okay, great. Thanks a lot.

**Operator**: Our next question is coming from Kulbinder Garcha with Credit Suisse. Your line is now open.

**<Q - Kulbinder Garcha, Credit Suisse Securities, LLC>**: Thanks for the question. I'm trying to just understand on a go-forward basis once this is completed what this means for MSI's balance sheet and cash flow. With your \$300 million contributions you would've made this year come down fairly markedly and by what amount? I'm not sure if you've mentioned that, but what's the go-forward level of contribution you may need to make? Then also previously, I was treating this net deficit that you have with the pension as effectively a form of debt. To the degree that it's going to be smaller going forward, does that free up your balance sheet for other things you want to do with that cash?

**<A - Gino Bonanotte, Motorola Solutions, Inc.>**: Sure. The first part of the question was the cash impact and we talked about right now our view is for five to six years, there would be no minimum funding requirement for the pension plan for the next five to six years. So that's the impact on cash.

**<A - Rob O'Keef, Motorola Solutions, Inc.>**: When you rewind, historically, we're in this \$200 million to \$250 million; this year, it was \$300 million a year minimum contribution range. That goes to zero for the next five to six years, so that does free up cash flow for other more productive uses, number one.

Number two, in terms of the plan that remains, it's actually interesting that it's a nuance but we've divested the retiree plan which is the shortest duration portion of the liability. We're left with the younger people with a much longer duration and the company is left with, if you will, a much longer timeframe to resolve that issue.

In addition to no minimum of cash contributions required for five to six years, assuming markets hold up, we have a longer timeframe with a longer duration to make those payments. The benefit payments coming out of the plan, you can see this in our K. It used to be \$300 million to \$350 million a year. With the retirees coming up, that number goes down to \$70 million to \$80 million a year, so the plan is going to have many years where it's going to rehabilitate itself, if you will, from within and we're going to have a much longer timeframe to build this plan up. So it works on that level, too. It's a nuance but it's a really important nuance to understanding the economics of what we've done here.

**<Q - Kulbinder Garcha, Credit Suisse Securities, LLC>**: And so I guess the question for Gino then. With this audit flexibility, what do you do with it on a go-forward basis, given that MSI will be generating more cash, it sounds like? What do you do with that?

**<A - Gino Bonanotte, Motorola Solutions, Inc.>**: So Kulbinder, this is Gino. We've talked about the fact that we'd have obviously a better visibility to cash, lower volatility to cash, and the ability to use that cash for other purposes. We haven't updated our use of capital yet and we will do that post Enterprise transaction but for the time being, you should expect nothing different in our model from the use of cash perspective.

**<A - Rob O'Keef, Motorola Solutions, Inc.>**: I think I'll just add. We've talked about the evolution of our balance sheet and this is just a key step in enabling us to get there in a way that we've talked about.

**<A - Gino Bonanotte, Motorola Solutions, Inc.>**: Does that answer your question, Kulbinder?

**<Q - Kulbinder Garcha, Credit Suisse Securities, LLC>**: Yes. Thank you, very clear.

**<A - Gino Bonanotte, Motorola Solutions, Inc.>**: Thank you.

**Operator**: Our next question comes from Ashwin Kesireddy with JP Morgan. Your line is open.

**<Q - Ashwin Kesireddy, JP Morgan Securities, LLC>**: Yes, hi. Thanks for taking my question. This Ashwin on behalf of Rod. I was wondering if you could give us more color on this, one of the comments you made on you're left with younger people now with much longer duration. Is there any way for us to think about the split between Government and the Enterprise businesses here when it comes to the duration of employees here?

**<A - Rob O'Keef, Motorola Solutions, Inc.>**: Not really. The split of Enterprise is having no material impact on our plan at all. Really, that hasn't factored in. Not many people are leaving the plan. So no material impact from the Enterprise split.

**Operator**: I will turn the floor back over to Mr. Shep Dunlap, Vice President of Investor Relations, for any additional or closing remarks today.

**<A – Shep Dunlap, Motorola Solutions, Inc.>**: Thanks. No, I think that's it. I appreciate everybody joining us today on short notice and we'll be back to you soon. Thanks.

**Operator**: Ladies and gentlemen, this does conclude today's teleconference. A replay of this call will be available over the internet in approximately three hours. The website address is [www.motorolasolutions.com/investor](http://www.motorolasolutions.com/investor). We thank you for your participation and ask that you please disconnect your lines at this time. Have a wonderful day.