



Quarterly update on

Estimated Solvency Funded Status of Defined Benefit Pension Plans in Ontario

June 2024

Introduction

Each quarter, FSRA monitors the solvency funding position, and publishes the estimated solvency ratios of Ontario Defined Benefit (DB) pension plans that are subject to solvency funding. This is one of the supervisory tools FSRA utilizes to improve outcomes for pension plan beneficiaries and to proactively engage in a dialogue with plan sponsors where there may be a concern over the security of the pension benefits.

It should also be useful for plan fiduciaries who must adhere to a high standard of care in administering their pension plans and investing the plan assets. Having an effective governance framework in place with a good understanding of the key risks facing the plan, their impact and risk mitigation strategies are key to achieving the desired outcomes and enhancing the ability to withstand periodic stresses. For example, having due consideration to the plan's ability to absorb fluctuations in funding costs and the probability of delivering the promised benefits under a range of possible outcomes that may result from the funding and investment strategy are important elements of a plan administrator's duty as a fiduciary.

Projected Solvency Position as at June 30, 2024

The median projected solvency ratio has reached a new peak at the end of the second quarter of 2024, increasing by 1% from the previous quarter. The funded status remains strong, with 90% of plans still projected to be fully funded as of June 30, 2024.

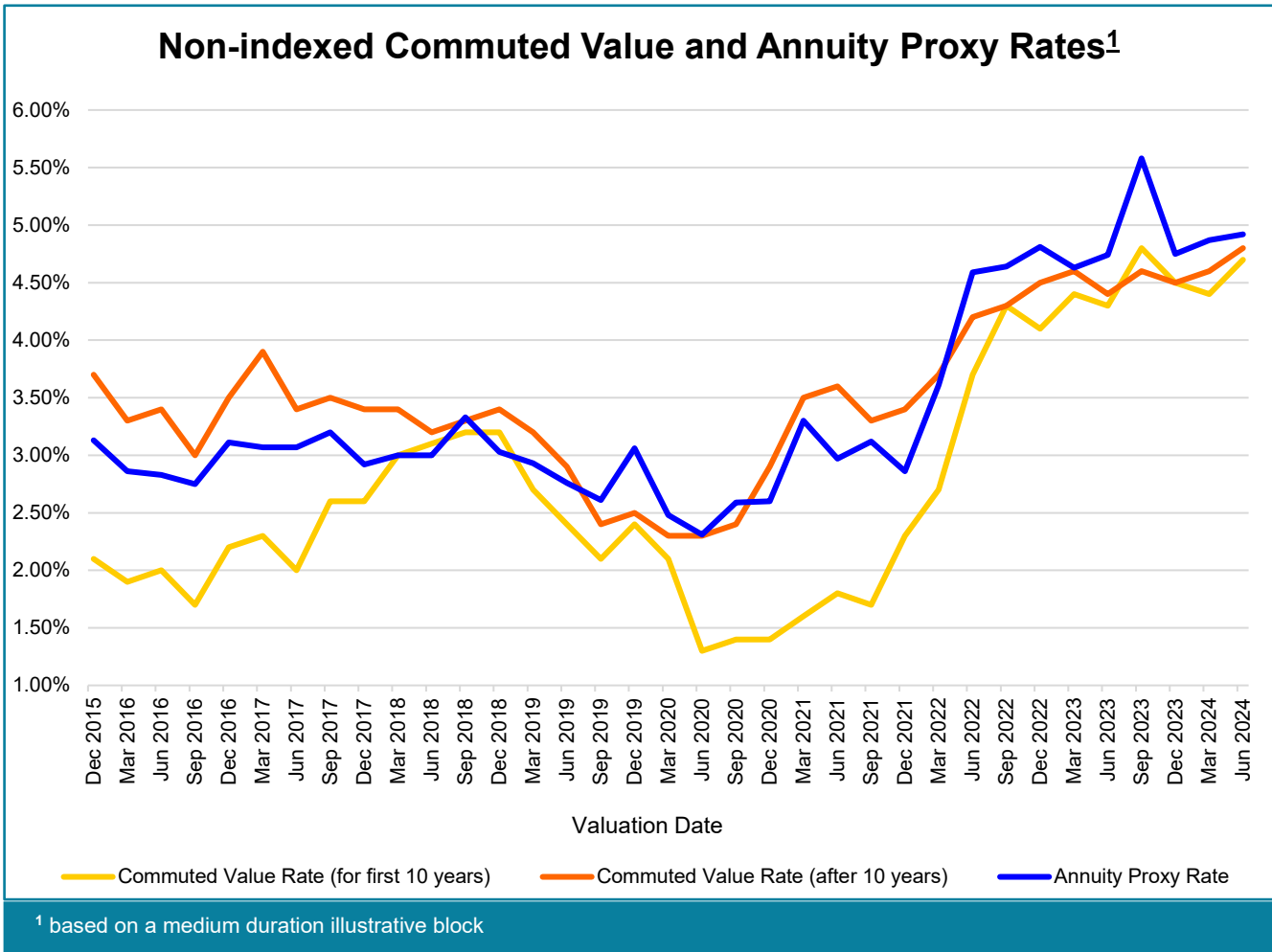
- The median projected solvency ratio was 123% as at June 30, 2024, a 1% increase from 122% as at March 31, 2024.
- The percentage of pension plans that were projected to be fully funded on a solvency basis maintained its level at 90% as at June 30, 2024, with 2% of plans falling below an 85% solvency ratio, also unchanged from last quarter.
- Pension funds eked out positive investment returns in Q2 2024, averaging a net return of 0.6%.
- Solvency discount rates increased since the last quarter resulting in a decrease in plan liabilities.

Over the past four years, pension plans have shown remarkable financial resilience despite facing significant market fluctuations. This steady performance has helped to enhance public confidence in the pension sector and the significant role they have in providing financial security and contributing to the economy. Although recent successes provide a solid foundation, the possibility of future interest rate cuts, unforeseen changes in the financial landscape, and new challenges are inevitable, putting pressure on the funded position of pension plans. Plan sponsors and administrators must continue to be proactive in understanding and assessing how future uncertainties might impact their pension plans. Strong governance and risk management practices are critical to effectively manage pension plans.

Projected Solvency Position as at June 30, 2024	Q2 2024	Q1 2024	Q4 2023
Median solvency ratio	123%	122%	119%
Percentage of plans with a solvency ratio greater than 100%	90%	90%	89%
Percentage of plans with a solvency ratio between 85% and 100%	8%	8%	9%
Percentage of plans with a solvency ratio below 85%	2%	2%	2%

The projected solvency position, in aggregate, improved since last quarter. The 1% increase in the estimated median solvency ratio since March 31, 2024 is attributable to:

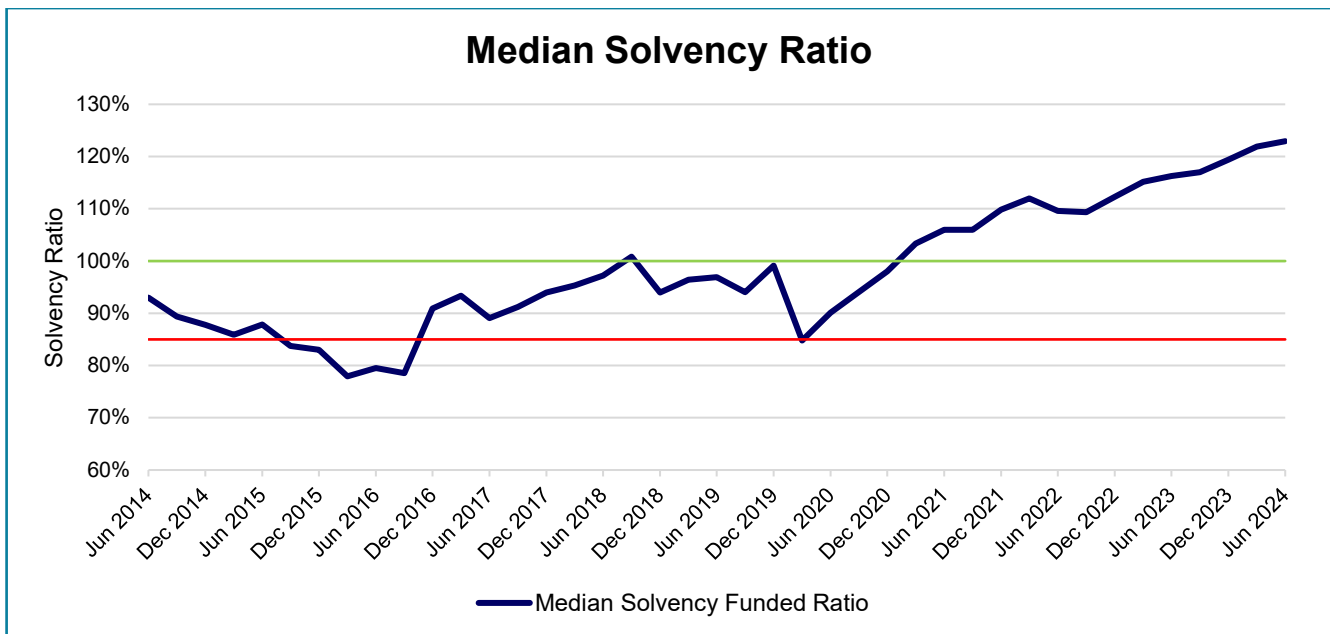
- Rise in solvency discount rates
 - The non-indexed commuted value discount rates, for the select and ultimate periods, increased by 30 bps and 20 bps, respectively and the non-indexed annuity purchase discount rate increased by 5 bps, resulting in a decrease in pension liabilities.
- Q2 2024 pension fund investment returns
 - The average second quarter 2024 gross and net, after expense, return estimates were 0.9% and 0.6%, respectively.

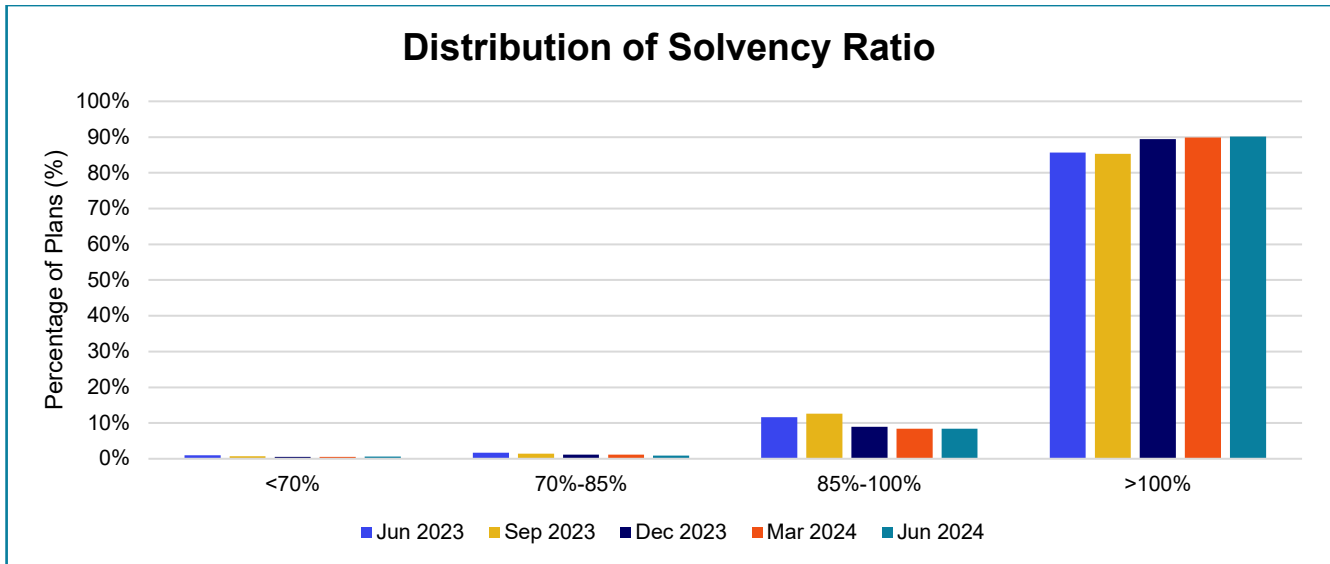


During Q2 2024, Canada had its first policy interest rate cut since March 2020, however economic data caused concerns over mild increases in both inflation and unemployment. Statistics Canada data shows Canadian GDP increased 1.1% from April 2023 through to April 2024. The Trans Mountain pipeline began operations, which is Canada’s first new pipeline in decades. The Bank of Canada (BoC) expected the start of commercial operations for the Trans Mountain pipeline to add one quarter of one percent of GDP growth to Canada in Q2. In real estate, the BoC has raised concerns that valuations are under pressure in the commercial real estate sector, particularly in areas where vacancies are high. Canadian CPI inflation ticked up to 2.9% in May, from 2.7% in April, and the BoC expects inflation to reach 2% in 2025. Canadian shelter costs are still a concern, with the shelter component of CPI increasing by 6.4% in May 2024. Unemployment rose to 6.4% in June, from 6.1% at the end of the last quarter, as labour productivity remains low.

While the Canadian yield curve remained inverted, Q2 2024 brought a modest 23 bps steepening of Canadian government bond benchmark yields, with the 2-year yield declining to 3.99% and the 10-year yield rising to 3.50%. The FTSE Canada Universe Bond index returned 0.9% for the quarter, while equity market returns in Canada were mildly negative with the S&P / TSX Composite Index returning -0.5%, underperforming US equity markets which returned 4.3%. Many equity investors have raised concerns that US equity returns and earnings growth expectations in Q2 2024 have been disproportionately driven by positive expectations for AI technology.

The Canadian policy interest rate was cut 0.25% by the BoC on June 5th to 4.75%, while the US Federal Reserve hasn't cut the US Federal Funds Target Range, with the range remaining at 5.25% to 5.50%. The Canadian dollar declined relative to the US dollar by about 1%, dropping to 0.7310 USD per Canadian dollar. Both the BoC and the US Federal Reserve proceeded with quantitative tightening and continued to reduce balance sheet holdings. At the end of Q2, the swaps market was pricing in one rate cut in both Canada and the US in the coming quarter.





Methodology and Assumptions

- The results reported in each plan's last filed actuarial valuation reports (assets and liabilities) were projected to June 30, 2024 based on these assumptions:
 - Sponsors would use all available funding excess and prior year credit balance for contribution holidays, subject to any statutory restrictions.
 - Sponsors would make normal cost contributions and special payments, if required, at the statutory minimum level.
 - Cash outflows were assumed to equal pension amounts payable to retired members as reported in the last filed valuation report. Plan administration costs were not directly reflected in cash outflows, but indirectly through net, after expense investment earnings.
 - Projected liabilities were calculated based on the Canadian Institute of Actuaries' (CIA) Standards of Practice for Pension Commuted Values and the CIA annuity purchase guidance applicable at the projection date.

2. Each plan's actual net rates of return are calculated based on its most recently filed Investment Information Summary (IIS) information. Where returns needed to be estimated, this was done using the IIS asset allocation in combination with market index returns, offset by a 25 basis point quarterly expense charge.

The following table summarizes the average IIS plan asset allocations by major asset class based on the most recent filed IIS:

Cash and Short-Term Investments	Canadian Equities	Foreign Equities	Fixed Income	Real Estate	Other
3.3%	18.3%	18.6%	52.3%	6.3%	1.2%

Market index returns on the major asset classes have been as follows:

	FTSE Canada 91-day T-Bill Index	S&P / TSX Total Return Index	MSCI World Total Net Return Index	FTSE Canada Universe Bond Index	FTSE Canada Long Term Bond Index	Cohen & Steers Global Realty Majors Index
Q2 2024	1.3%	-0.5%	3.8%	0.9%	0.2%	-0.9%
Q1 2024	1.2%	6.6%	11.7%	-1.2%	-3.6%	2.3%
Q4 2023	1.3%	8.1%	8.7%	8.3%	14.8%	14.3%
Q3 2023	1.2%	-2.2%	-1.4%	-3.9%	-9.5%	-3.9%