FSRA
Financial Services Regulatory Authority of Ontario

Ontario

www.fsrao.ca

Quarterly update on

Estimated Solvency Funded Status of Defined Benefit Pension Plans in Ontario

December 31, 2023

25 Sheppard Avenue West
Suite 100
Toronto ON
M2N 6S6
Telephone: 416-250-7250
Toll free: 1-800-668-0128

25, avenue Sheppard Ouest
Bureau 100
Toronto (Ontario)
M2N 6S6
Téléphone: 416 250-7250
Sans frais: 1 800 668-0128

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 December 31, 2023

Pension plans' health continued to improve steadily throughout the year, resulting in an all-time high at the end of 2023. The median projected solvency ratio has exceeded 100% for twelve consecutive quarter-ends starting from March 31, 2021. Nearly 90% of plans have a solvency funded ratio above 100% at December 31, 2023.

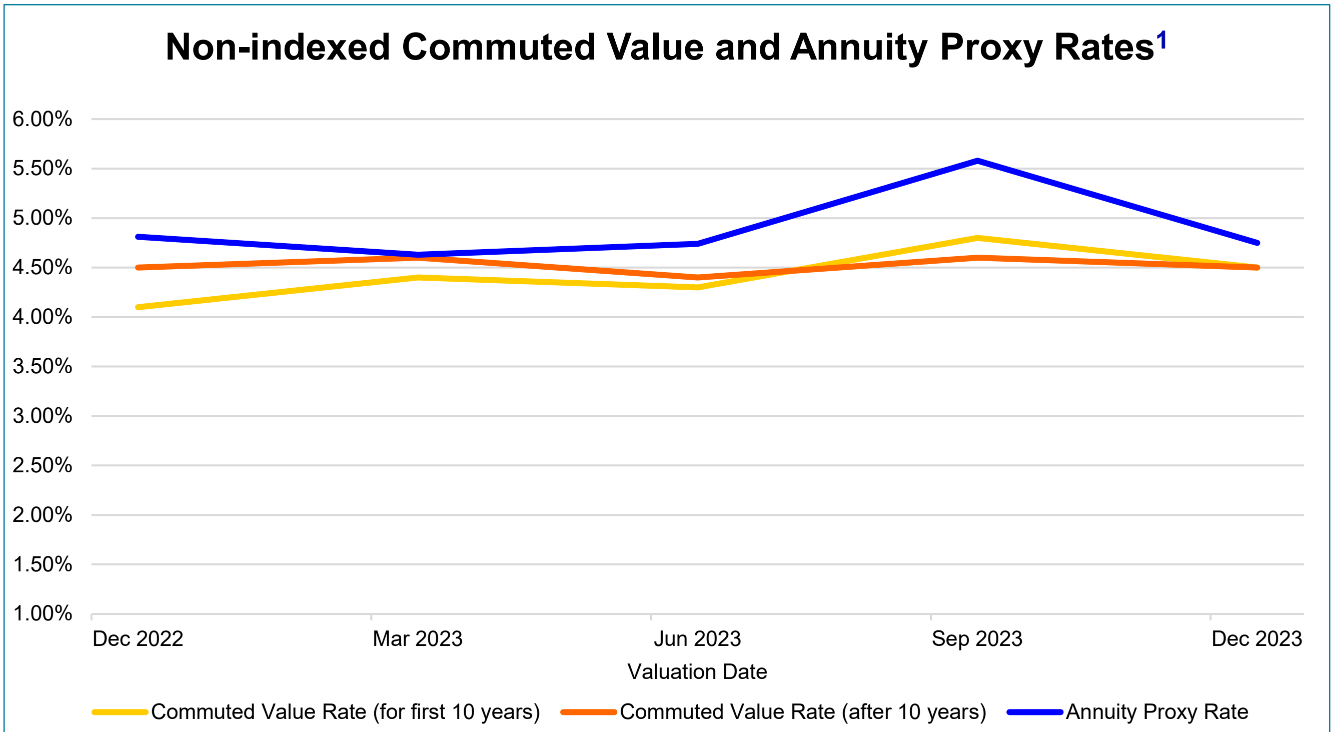
- The median projected solvency ratio was 119% as at December 31, 2023, a 2% increase from 117% as at September 30, 2023 (and a 7% increase from 112% at the end of 2022).
- The percentage of pension plans that were projected to be fully funded on a solvency basis as at December 31, 2023 was 89% compared to 85% as at September 30, 2023. The percentage of plans falling below an 85% solvency ratio was 2%, unchanged from last quarter.
- Investment returns in Q4 rebounded sharply from last quarter's negative returns, posting a positive average net return of 9.9%. For the year as a whole, pension plans achieved an average net return of 10.0%.
- Solvency discount rates decreased since the last quarter resulting in an increase in plan liabilities, partially offsetting the asset gains.

The financial resilience demonstrated by pension plans over the past three years in the face of significant market uncertainty is good news for all pension stakeholders. The ability to maintain sound funded ratios during this time enhances the confidence members have in their pension plans. This achievement, however, should be tempered with a continued commitment to constant vigilance and strong governance. It is important to recognize that the financial landscape is inherently dynamic, and while the recent successes provide a strong foundation, new challenges will inevitably arise. Plan sponsors and administrators should continue to remain proactive in understanding how these uncertainties may impact their pension plans. Achieving and maintaining financial resilience requires a steadfast dedication to risk management and strategic planning in order to adapt to emerging conditions and ensuring the long-term sustainability of pension plans.

Projected solvency position as at December 31, 2023	Q4 2023	Q3 2023	Q4 2022
Median solvency ratio	119%	117%	112%
Percentage of plans with a solvency ratio greater than 100%	89%	85%	81%
Percentage of plans with a solvency ratio between 85% and 100%	9%	13%	17%
Percentage of plans with a solvency ratio below 85%	2%	2%	2%

The projected solvency position, in aggregate, improved since last quarter. The 2% increase in the estimated median solvency ratio since September 30, 2023 is attributable to:

- Positive Q4 2023 pension fund investment returns
  - The average fourth quarter 2023 gross and net, after expense, return estimates were 10.1% and 9.9%, respectively.
- Decline in solvency discount rates
  - The non-indexed commuted value discount rates, for the select and ultimate periods decreased by 30 bps and 10 bps, respectively, and the non-indexed annuity purchase discount rate decreased by 83 bps, resulting in an increase in pension liabilities.

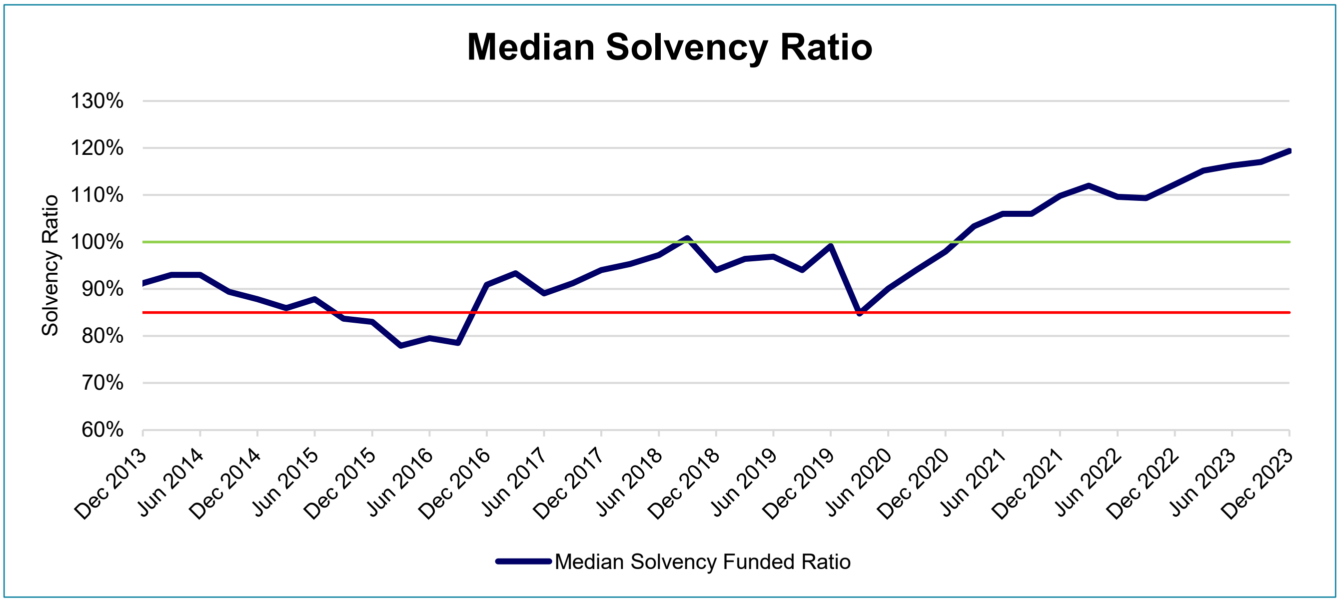


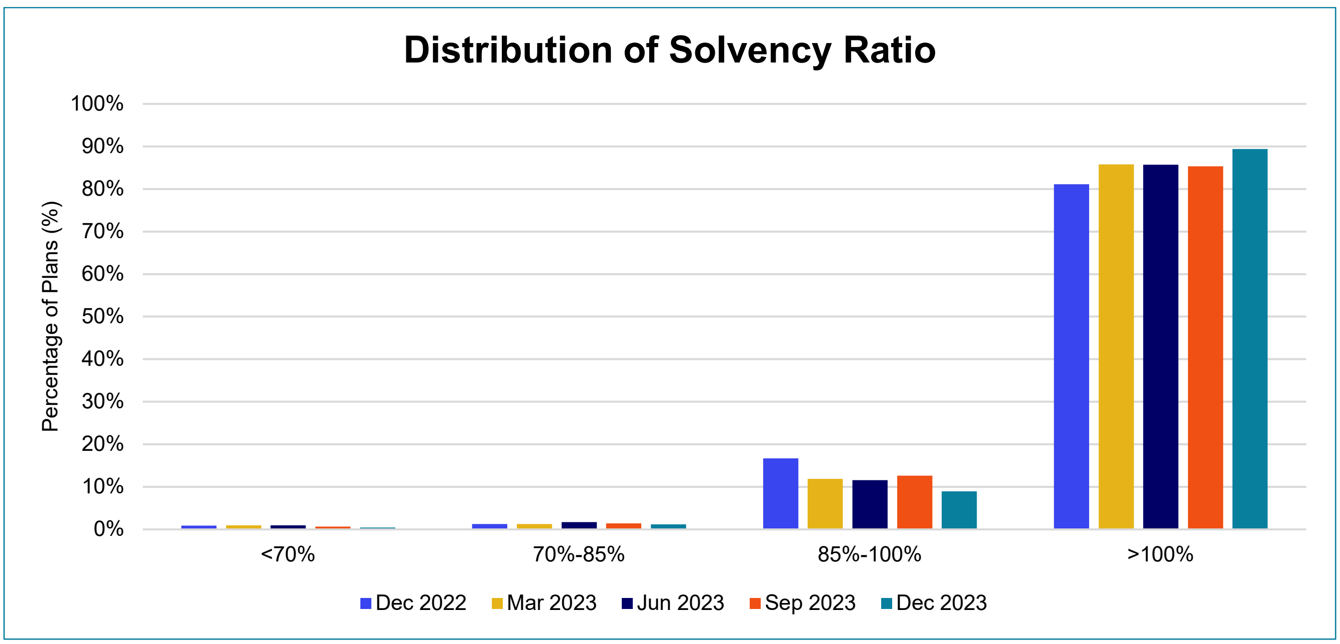
[1] based on a medium duration illustrative block

During the fourth quarter of 2023, bond yields decreased and steepened, equity markets increased substantially, while shelter costs and unemployment increased. Statistics Canada data indicates annual CPI inflation stood at 3.1% in both October and November, while core inflation was 2.7% and 2.8% in October and November, respectively. Core inflation omits the most volatile components of the CPI index, as defined by the Bank of Canada (BoC). The shelter component of CPI increased by more than the aggregate CPI index, increasing by 5.9% from November 2022 to November 2023. Unemployment increased from Q3, and stood at 5.8% in December, up from 5.5% in September. Canadian GDP, month-over-month, did not grow in October, but did increase year-over-year, with October 2023 GDP 0.9% higher than October 2022 GDP. The BoC revised their GDP forecasts for 2023 and 2024 downward in October, but their 2025 forecast upward, to 1.2%, 0.9%, and 2.5%, respectively, from 1.8%, 1.2%, and 2.4%, in their previous monetary policy report.

At the end of Q4, the Canadian government bond yield curve remained inverted, with the 10-year benchmark yield 78 basis points below the 2-year benchmark yield, compared to a spread of 84 basis points at the end of Q3. The yield curve shifted down from Q3 to Q4, with the 2-year benchmark yield having declined by 99 basis points to 3.88%, while the benchmark 10-year yield dropped 93 basis points to 3.10%, reducing the difference between the 2-year and 10-year yields. In Canadian markets, for Q4, the FTSE Canada Universe Bond index increased 8.3% and the S&P/TSX Composite equity index returned 8.1%. The Canadian dollar increased in value relative to the US dollar and stands at 0.7551 US dollars per Canadian dollar at quarter end.

Central banks held target rates steady in Q4. The BoC has held the policy rate at 5.00% since July and the US Federal Reserve has maintained the federal funds target range at 5.25% to 5.50%. Both the BoC and the US Federal Reserve proceeded with quantitative tightening and continued to reduce balance sheet holdings, decreasing their total assets from Q3 to Q4. As at the end of Q4, the overnight index swaps markets were pricing in no interest rate cuts for Canada during the next quarter, but two interest rate cuts in the US over the next quarter.


Median Solvency Ratio
130%
120%
110%
100%
90%
80%
70%
60%
Solvency Ratio
Dec 2013
Jun 2014
Dec 2014
Jun 2015
Dec 2015
Jun 2016
Dec 2016
Jun 2017
Dec 2017
Jun 2018
Dec 2018
Jun 2019
Dec 2019
Jun 2020
Dec 2020
Jun 2021
Dec 2021
Jun 2022
Dec 2022
Jun 2023
Dec 2023
Median Solvency Funded Ratio


Distribution of Solvency Ratio
100%
90%
80%
70%
60%
50%
40%
30%
20%
10%
0%
Percentage of Plans (%)
<70%
70%-85%
85%-100%
>100%
Dec 2022
Mar 2023
Jun 2023
Sep 2023
Dec 2023

Methodology and assumptions

1. The results reported in each plan's last filed actuarial valuation reports (assets and liabilities) were projected to December 31, 2023 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
3.5%	19.2%	19.7%	50.2%	6.3%	1.1%

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
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%
Q2 2023	1.0%	1.1%	4.5%	-0.7%	0.6%	-2.5%
Q1 2023	1.1%	4.6%	7.6%	3.2%	4.7%	-0.1%