FSRA
Financial Services Regulatory Authority of Ontario

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Autorité ontarienne de réglementation des services financiers

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Quarterly update on

Estimated Solvency Funded Status of Defined Benefit Pension Plans in Ontario

December 31, 2021

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, 2021

Pension plans' health continued to improve steadily, after their quick recovery to pre-pandemic levels a year ago. The median projected solvency ratio at the end of 2021 is 25% higher than at March 31, 2020 and 12% higher than the start of the year. The median solvency ratio is now at its highest level since monitoring began.

- The median projected solvency ratio was 110% as at December 31, 2021, increasing from 106% as at September 30, 2021 (and 98% at the end of 2020).

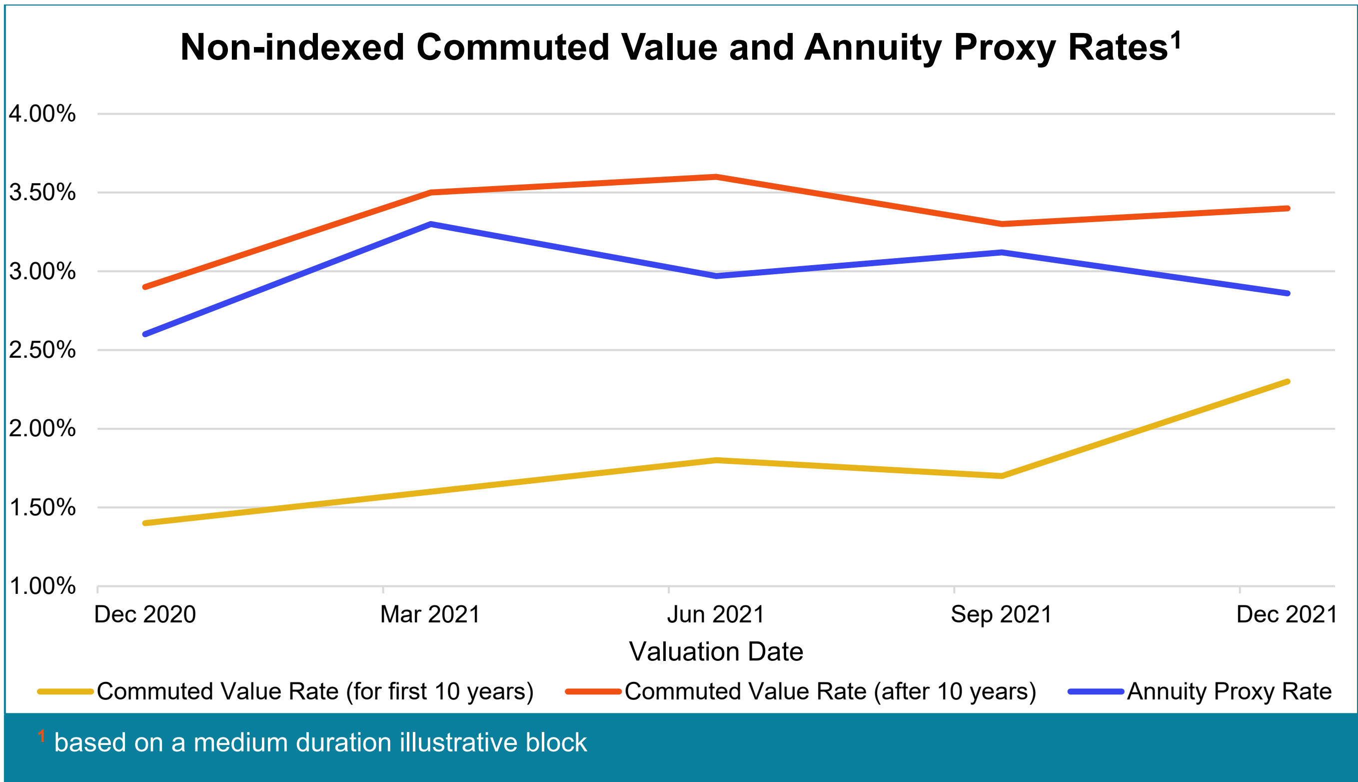
- The percentage of pension plans that were projected to be fully funded on a solvency basis at December 31, 2021 was 81%, while 2% were projected to have a solvency ratio below 85%.

The significant improvement in the health of pension plans over the last several quarters is good news for all pension stakeholders. However, it must be tempered with the understanding that constant vigilance and good governance are essential to managing and mitigating risks of a deterioration in the funded position. While the future is always uncertain, plan sponsors and administrators can and should understand how these uncertainties may affect their pension plan. This will enable them to have strategies and processes in place to adapt to emerging conditions.

Projected Solvency Position as at December 31, 2021	Q4 2021	Q3 2021	Q4 2020
Median solvency ratio	110%	106%	98%
Percentage of plans with a solvency ratio greater than 100%	81%	67%	45%
Percentage of plans with a solvency ratio between 85% and 100%	17%	30%	42%
Percentage of plans with a solvency ratio below 85%	2%	3%	13%

The projected solvency position, in aggregate, improved since last quarter. The 4% increase in the estimated median solvency ratio since September 30, 2021 is attributable to:

- Positive Q4 2021 pension fund investment returns
  - The average fourth quarter 2021 gross and net, after expense, return estimates were 5.2% and 4.9% respectively.
- Change in solvency discount rates
  - The non-indexed commuted value discount rate for selected period and ultimate period increased by 60 bps and 10 bps respectively whereas the non-indexed annuity purchase discount rate decreased by 26 bps. Overall, these offsetting changes had a negligible net impact on the liabilities.



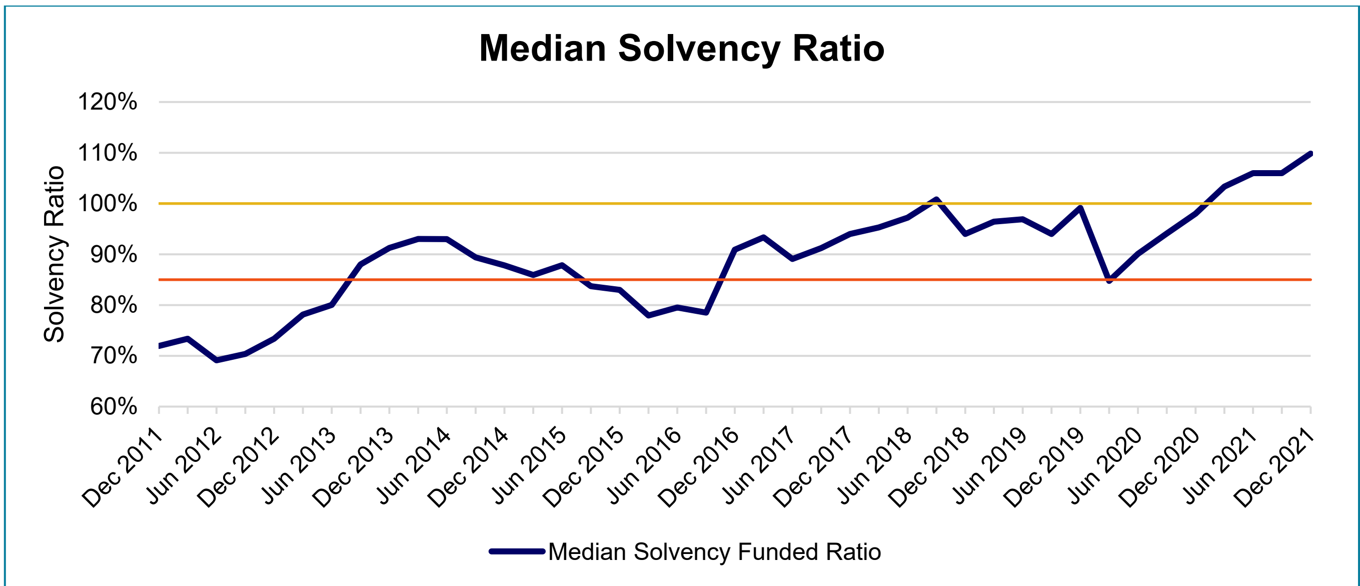
[1] based on a medium duration illustrative block

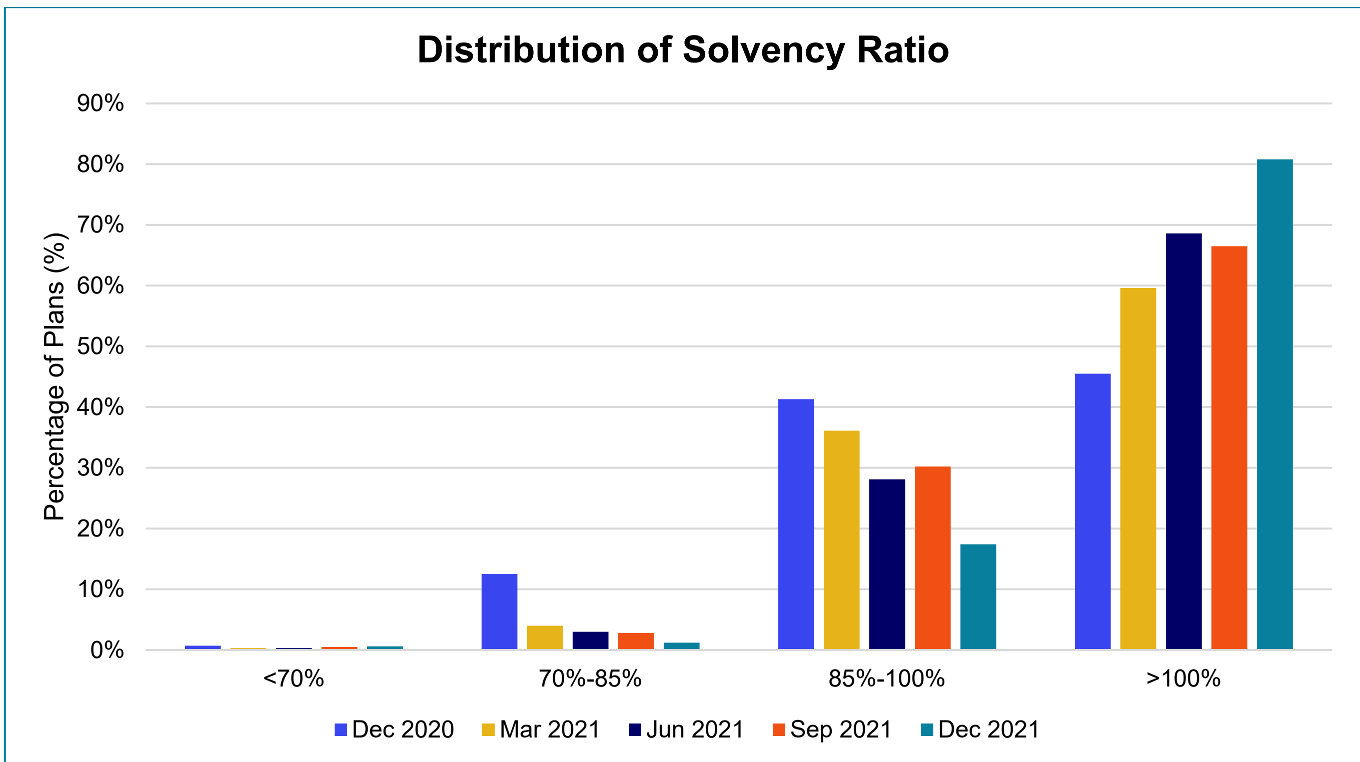
The fourth quarter saw the continuation of the COVID-19 pandemic and the beginning of the rapid spread of the Omicron variant, leading to the re-introduction at the end of the quarter and beginning of 2022 of numerous lockdown restrictions throughout the country. However, the economy had been continuing to improve with both the unemployment rate and GDP virtually back to pre-pandemic levels. Specifically, Statistics Canada data show the unemployment rate had improved to 5.9% in December from 6.9% in September and GDP had increased by 0.8% month-on-month in October. Inflation has remained above the Bank of Canada (BoC) target range of 1% to 3% for eight consecutive months, with annualized CPI inflation of 4.7% in November. Global supply chain disruptions continued and annualized goods inflation in November was 6.9% compared to that for services at 2.9%. The BoC expects inflation to ease back towards their 2% target in the second half of 2022.

The fourth quarter saw a flattening of the Government of Canada (GoC) benchmark bond yield curve with 10-year and long-term bond yields down modestly and 2-year and 3-year yields steeply higher. The quarter also saw positive returns in both Canadian fixed income and equities. The FTSE Canada Universe Bond index increased by 1.5%, while the S&P/TSX Composite index rose by 6.5%.

Against the backdrop of improving national economies and increased inflation, a number of central banks are reducing or ending their quantitative easing programs. Indeed, the Bank of England, has even raised their bank rate. In Canada, monetary policy remains accommodative with the BoC maintaining the overnight target rate at 0.25%. The BoC has ended its quantitative easing program but will reinvest the proceeds of maturing bonds to maintain its GoC bond holdings. In the US, the Federal Reserve maintained the federal funds rate target range at 0% to 0.25%. While continuing with asset purchases,

they lessened the pace of purchases in the fourth quarter and intend to wind down the program in March of 2022, subject to the outlook for the economy.





Methodology and assumptions

1. The results reported in each plan's last filed actuarial valuation reports (assets and liabilities) were projected to December 31, 2021 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	Canadian Equities	Foreign Equities	Fixed Income[2]	Real Estate	Other
2.0%	20.9%	21.4%	49.3%	5.3%	1.1%

[2] Assumed to be 50% FTSE TMX Universe Bonds and 50% FTSE TMX Long Term Bonds.

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

	S&P / TSX Total Return Index	MSCI World Total Net Return Index	FTSE TMX Universe Bond Index	FTSE TMX Long Bond Index	Cohen & Steers Global Realty Majors Index
Q4 2021	6.5%	7.5%	1.5%	4.8%	11.6%
Q3 2021	0.2%	2.3%	-0.5%	-1.6%	1.5%
Q2 2021	8.5%	6.2%	1.7%	3.7%	9.2%
Q1 2021	8.1%	3.5%	-5.0%	-10.7%	3.7%