Canadian Pension Funds:
Investment Partners in the U.S. – Real Estate, Energy, Infrastructure & Beyond

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Summary

U.S. private and public sectors should look north of the border for investment partnerships, and take advantage of Canadian pension funds' bullish interest in investing in the United States. In 2013, the combined Top 100 Canadian pension funds' assets under management reached $900 billion for the first time. At the end of 2012, the assets of the Top 100 totaled $877.1 billion, up from $798.8 billion in 2011. Assets climbed by an overall average of nearly 10% in the last year, with only one plan reporting a decline in its assets, compared to 26 in 2011. The Top 100 Canadian pension funds are expected to break the $1 trillion mark in the next two years. Canada is a major player in the world of pension funds and investment, investing heavily in opportunities outside Canada in a myriad of asset classes. U.S. entities and companies would do well to consider partnering with these formidable players.

Key Players in Canada

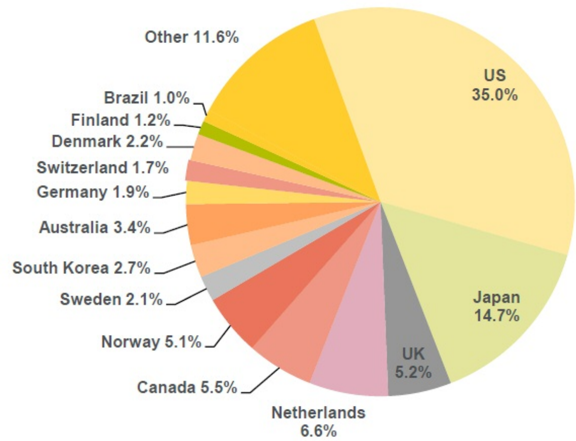
The Top 10 Canadian pension funds are (ranked by size of pension assets as of December 2013): The Canada Pension Plan Investment Board (CPPIB), The Caisse de depot et placement du Quebec (La Caisse), The Ontario Teachers' Pension Plan Board (OTPP), The British Columbia Investment Management Corporation (BcIMC), The Public Sector Pension Investment Board (PSP Investments), The Ontario Municipal Employees Retirement System (OMERS), The Healthcare of Ontario Pension Plan (HOOPP), The Alberta Investment Management Corp. (AIMCo), The Ontario Pension Board (OPB), and the Ontario Public Service Employees Union Pension Trust (OPTrust).

The Top 10 Canadian pension funds represent close to 35% of all Canadian retirement assets and 80% of public pension plan assets. Seven of the underlying pension plans are among the top one hundred plans worldwide, in which CPPIB and OTPP are 9th and 17th respectively in the world for the total assets managed. From 2003 to 2011, the Top 10 grew their pension assets under management from $350 billion to $714 billion. While about one-third of this growth ($125 billion) resulted from net inflows to the funds, two-thirds ($240 billion) was driven by investment returns. Together, they have more than $400 billion invested across various asset classes in Canada. They have participated in some of the largest deals in the world in recent years, including one of the largest electricity transmission and distribution companies in the U.S., seven United Kingdom airports including London Heathrow, three Chilean water utilities and one of the largest and most profitable insurance providers in South Korea. For example, CPPIB investments contain 8.5% of Canadian Stocks; 34.5% of foreign stocks; and 5.7% stocks in emerging countries for the 2014 fiscal year.

Canada’s Rank on the World Stage

Total value of fund assets
Split by fund domicile

Country	No. funds
US	124
UK	26
Canada	19
Japan	17
Australia	15
Netherlands	13
Germany	12
Switzerland	12
Denmark	8
Sweden	7
Finland	5
Brazil	3
South Korea	2
Norway	1
Other	36
Total	300



Note: ‘Other’ includes the following markets: Belgium, Chile, China, Colombia, France, India, Ireland, Kuwait, Luxembourg, Malaysia, Mexico, New Zealand, Peru, Philippines, Poland, Portugal, Russia, Singapore, South Africa, Spain, Taiwan and Thailand.

From: Towers Watson, P&I / TW 300 Analysis, Year End 2012, August 2013.

The New Canadian Pension Fund Investment Model

The Economist magazine referred to the Canada’s pension funds as “Maple Revolutionaries”.[1] Unlike any other pension fund, Canadians prefer to run their portfolios internally and invest directly. In other words, they invest more money into buy-outs, infrastructure and property than publicly traded stocks and bonds. They believe that direct investment will produce higher returns; they are in some ways like “depoliticized sovereign-wealth funds”.[2] OTTP has been using this approach since the 1990s. For the others, however, the economic crisis of 2008, the stock exchange markets instability and the limited credit offered by banks created a new wave of capital needs in many sectors. Canadian pension funds have thus shifted their portfolio and investment focus since 2007 to follow OTPP into direct investment.

The new Canadian model has many advantages. In the midst of the great recession of 2008, companies including pension funds looked to find a way to cut expenses. By focusing on direct investment, the Canadian model is cost saving because it eliminates the fees of intermediaries charging each transaction and each margin of profit on the stock and bond market. Moreover, the Canadian pension funds feel less pressure to chase the high returns, which enables them to pursue

[1] "Maple Revolutionaries: Canada's Pension Funds." *Economist (US)* 3 Mar. 2012. Web. 20 June 2014. <http://www.economist.com/node/21548970>.

[2] Maple Revolutionaries: Canada's Pension Funds." *Economist (US)* 3 Mar. 2012. Web. 20 June 2014. <http://www.economist.com/node/21548970>.

investments with less risk and leverage. Over the past ten years, OTPP had the highest total returns of the biggest 330 public and private pension in the world.

The Melbourne Mercer Global Pension Index, widely considered as the premier international ranking of retirement income systems, has found Canada's to be among the strongest in the world. The Index tracks more than forty indicators of system health in such areas as integrity, adequacy and sustainability. In 2012, Canada ranked sixth out of eighteen countries – ahead of the United Kingdom, the United States, Germany, France and Japan, among others.

Grade	Index Value	Countries	Description
A	>80	Denmark	A first class and robust retirement income system that delivers good benefits, is sustainable and has a high level of integrity.
B+	75–80	Netherlands Australia	A system that has a sound structure, with many good features, but has some areas for improvement that differentiates it from an A-grade system.
B	65–75	Switzerland Sweden Canada Singapore Chile UK	
C+	60–65	Nil	A system that has some good features, but also has major risks and/or shortcomings that should be addressed. Without these improvements, its efficacy and/or long-term sustainability can be questioned.
C	50–60	Germany USA Poland France Brazil Mexico	
D	35–50	China Japan Korea (South) India Indonesia	A system that has some desirable features, but also has major weaknesses and/or omissions that need to be addressed. Without these improvements, its efficacy and sustainability are in doubt.
E	<35	Nil	A poor system that may be in the early stages of development or a non-existent system.

We believe that none of the countries in this study has an E-grade system, which would be represented by an index value below 35. A score between 35 and 50, representing a D-grade system, indicates a system that has some sound features but there exist major omissions or weaknesses. A D-grade classification may also occur in the relatively early stages of the development of a particular country's retirement income system, such as in China, India, Indonesia and Korea.

From: Melbourne Mercer Global Pension Index, October 2013 – 5th Edition

Canadian Pension Fund Investments in the U.S. and Internationally

Investing in Canada is a priority; however Canadian pension funds have invested all around the world since 2007. Just CPPIB alone has 197 worldwide partnerships in 33 countries, resulting in 103 transactions for the 2014 fiscal year. Some of the major investments for the past three years in the United States and the rest of the world are listed below:

Investments in the United States

- CPPIB and PSP Investments acquired Kinetic Concepts, an American medical devices company based in San Antonio (TX), for $6.1 billion in 2011.

- CPPIB tripled its investment in 2011 in the internet phone service Skype in an $8.5 billion deal with Microsoft, taking home $933 million on an initial $300 investment.

- OMERS has $10billion invested in the United States, both public and private markets.
- In October 2011, OMERS became one of Canada's largest venture capital investors with OMERS Venture, a $180 million fund that will focus on North American technology, media, telecommunications, clean technology and life sciences.
- In November 2011, La Caisse announced an $850 million deal to buy ConocoPhillips' 16.55% stake in Colonial Pipeline Co, the largest refined petroleum products pipeline in the United States.
- CPPIB invested $2 billion, representing a 45% interest, in 10 regional malls, primarily in California, and two redevelopment sites (2012).
- CPPIB, with a partnership with Ares Management LLC, bought U.S. luxury retailer Neiman Marcus Group Ltd. and its 79 stores for $6 billion in September 2013.
- OTPP invested $500 million in Hudson's Bay Co.'s $2.9 billion purchase of Saks Fifth Avenue in New York City in July 2013.
- OTPP bought Impark, which leases or manages more than 2,000 parking locations, consisting of more than 400,000 parking spaces in more than 25 markets in Canada and in the U.S.
- La Caisse total assets geographic diversification is represented by 56.2% in Canada; 19.7% in the U.S. and 9.7% for the Euro zone. Recent major investments in the U.S. include:
  - ***January 2013:*** $500 million investment in a portfolio of 13 Invenergy wind farms in Canada (2) and in the United States (11);
  - ***April 2013:*** Investment in the $1.5 billion equity residential portfolio recently taken private by Goldman, Sachs & Co. and real estate manager Greystar Real Estate Partners;
  - ***June 2013:*** Acquisition of the 47-story Wells Fargo Center in Seattle for $390 million;
  - ***October 2013:*** Acquisition with an affiliate of Beacon Capital Partners of a 51% managing member interest in 1211 Avenue of the Americas in NYC valued at more than $850 million;
  - ***October 2013:*** $370 million investment in the 10 and 120 South Riverside Plaza office buildings in Chicago, IL.
  - ***November 2013:*** Joint venture MWest, backed by DivcoWest, Ivanhoé Cambridge and TPG Real Estate added 825,000 square feet to its Silicon Valley Portfolio;
  - ***June 2014:*** Opening of an office in Washington D.C. to expand its U.S. & global presence;
  - ***July 2014:*** Acquisition of a 24.7 % ownership stake in Invenergy based in Chicago;
  - ***August 2014:*** In a partnership with Veritas Investments Inc., it will acquire multiresidential properties in San Francisco.
- In July 2013, OMERS in partnership with a Japanese pension fund, acquired 50% stake for $2 billion in the Midland Cogeneration Venture in Midland, MI, a gas-fired thermal power plant.
- CPPIB bought the insurance business Wilton Re Holdings Limited (Wilton, CT) for $1.8 billion in March 2014.

Investments Around the World

- OTPP invested $541 million in two Chilean water utilities in 2011.
- Also in November 2011, AIMCo bought 50% stake in Chile's second-largest electricity distributor, Grupo Saesa, from Morgan Stanley Infrastructure Partners.
- CPPIB 50% stake in the Commonwealth Property Office Fund includes 21 office buildings in Australia, valued to $3.3 billion, acquired in 2013.
- 27.6% stake in Aliansce Shopping Center, one of Brazil's largest shopping mall developers.
- A 15% stake in ORPEA S.A., based in Paris, France, Europe' largest supplier of nursing care.
- Many real estate investment in the UK including: 23.15% stake in 6 airports (with London Heathrow), office buildings in London ($200 million), and shopping malls in Birmingham ($400 million).
- New CPPIB investments include real estate partnerships in India valued to $450 million for new residential projects in Mumbai.
- CPPIB 36.5% stake in the major transporter of natural gas in Peru, *Transportada de Gas del Peru*, valued to $807 million.
- Real estate partnerships in South Korea and China valued to $400 million.

Canada's Economic Environment

Canada's financial system has been described as strong and stable by many economists and specialists. Not only have the Canadian pension funds outperformed most international competitors, but the Canadian banks have also faired very well in spite of the economic crisis. The top 5 banks in Canada[3] have reported profits of $29.4 billion for the 2014 fiscal year, up a healthy 5% from last year despite the weak economy, slower consumer lending and other economic issues. Four of these banks are also in the Top 10 of the strongest banks in the world according to Bloomberg Market Magazine.[4] The stability of the financial structure in Canada is very solid, based on an important capital inflow, and it is projected to continue its growth for many years to come.

For More Information

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[3] The top 5 Canadian banks are: Royal Bank of Canada (RBC), Toronto-Dominion Bank (TD Canada Trust), Bank of Nova Scotia (Scotiabank), Bank of Montreal (BMO), and Canadian Imperial Bank of Commerce (CIBC).
[4] According to data compiled by Bloomberg Markets magazine; CIBC, Royal Bank, Scotiabank and TD were ranked 3rd, 4th, 7th and 8th, respectively, on the publication's annual ranking of the world's strongest and safest lenders as of May 2013.

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