Speech to the

Ontario Teachers' Federation
Board of Governors

Annual Meeting

By:
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Chair
Ontario Teachers' Pension Plan Board
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Merci beaucoup, (Reno), et bonjour à toutes et à tous.

I am joined today by board member Rod Albert. Rod is our newest board member, having come on board on January 1. Rod is not new to Teachers' by any means, though. As many of you are no doubt aware, as President of the OTF at the time, Rod led the negotiations with the Ontario government in the establishment of the Ontario Teachers' Pension Plan as an independent organization in 1990. Rod will address you when I conclude my remarks. Jim Leech, our CEO, and Melissa Kennedy, our General Counsel and Senior Vice-President Corporate Affairs, are here as well, and will join me in taking your questions at the conclusion of Rod's and my remarks.

First, I must congratulate you, Reno, on your successful year in office. I know the market ups and downs and their effect on our fund, and the chronic funding shortfall situation, have been major concerns for you and your executive. I want to commend you on your calm and deliberate approach to the issues we face. Your understanding of the fact that there is no roadmap for any of us to follow in navigating these unprecedented times has been most appreciated.

And let me welcome you to your new position as president, Rian. You have assumed tremendous responsibility for one of our province's most precious resources: our teachers. . I know the pension plan is only one of your many concerns, but you will appreciate that we at the pension plan consider it your most important. I am sure you would not want us to feel any other way.

I am here today to talk to you about two things

1. First, the current economy, in the context of the outlook for your pension plan, and
2. Second, the considerable progress made this year by senior representatives of the OTF, the government and plan administration who comprised the

Sustainability Working Group. They have worked together to address the state of chronic pension shortfalls that our plan has been experiencing in recent years.

I will start with a look at the economy and market conditions.

It's now been three years since the demolition derby of asset backed commercial paper, subprime mortgages and the ensuing financial crisis began. You've heard that period referred to as a "Black Swan" – something that could not have been foreseen, because it had never been seen before. I still remember our Chief Investment Officer at the time, Bob Bertram, expressing his dismay as fixed income and equity markets, which aren't supposed to move in the same direction, did exactly that. Commercial paper had frozen and many investors were forced to sell other investments – driving their prices down - to meet their debt obligations. And so values of both asset classes fell in unison

It's now two years later, and while we may have crept out of the depths of the 2008-2009 recession, the good times certainly have not returned to either the markets or the economy.

Some call the US situation a "fragile economic recovery." Some call it "Japan Lite", likening it to Japan's "lost two decades" that began in the 90s … with five recessions since then causing the country to slip in and out of economic consciousness. A total of 8.5 million American jobs were lost in 2008-09. 4.5 million Americans remain unemployed today – roughly the equivalent to the population of the city of Los Angeles. And until Americans are working, their economy can't. Employment is the engine of the modern economy, fueling new home, car and major appliance purchases. Given Canada's dependency on the US economy, when they are ailing, so are we.
This year's market swings have been dizzying and unpredictable. As I started drafting my remarks for today, China also announced an economic slowdown. This drove the Dow Jones to its largest sell-off in more than a month.

Looking outside North America and across the Atlantic, the European contagion that began in earnest this year has also kept the brakes on any economic recovery there.

I am pleased to report that your pension fund did not have any exposure to European sovereign debt under whose weight Portugal, Ireland, Italy, Greece and Spain (with the inelegant acronym PIIGS) continue to reel; nor did we have any exposure to British Petroleum. You may have read that our public equities' team was able to purchase a significant position in Transocean, the oil rig company sometimes wrongly blamed for the BP gulf catastrophe. Their share price dropped at the time of the blowout; we purchased additional shares near the low, and I'm pleased to say those shares are already up 25%.

The Canadian economy is healthy by comparison to other countries', largely because it is resource-based. Never has it been a better time to be hewers of wood and drawers of water, not to mention miners and oilers. However, the fact remains that we live in a global economy, and so we are not immune to the effects of Japan Lite or the PIIGS.

As Neil Petroff, our Chief Investment Officer, warned in his remarks at our April annual meeting:

> "Because (the 2009) rebound was largely the result of stock market recovery and not true economic growth, we don't expect market returns to maintain this pace going forward."

Unfortunately, he was right.

With markets weak and interest rates even lower than last year, it will come as no surprise, I am sure, that we have not seen pension funding relief. The plan's most important liability risk is a decline in real interest rates. And while we thought that interest rates might have climbed with recovery, that has not happened; in fact Real

Return Bond yields have fallen by .11% to 1.42%. As a result our overall funding position has worsened.

As reported earlier this year, our 2010 shortfall was already projected to grow, with $12.7 billion in losses held back in the smoothing adjustment at the end of 2009, to be recognized over the next three years. The continuing fall in real interest rates exacerbates that problem.

With that backdrop, you can understand why the board and management of the pension plan are as encouraged as we are with the progress made by the Sustainability Working Group over the past several months.

Let me remind you of the genesis, mandate and composition of that working group.

It was created as part of the understanding reached at the time of the January 1, 2009 valuation filing. The parties agreed at that time to form a Sustainability Working Group to study the best means to keep the Teachers' pension plan secure and affordable well into the future. The tripartite group was composed of senior representatives from the OTF and the Ontario government, as well as plan management. All three groups had their advisors – actuaries and in the case of the OTF, their lawyer – at the table. It was facilitated by the esteemed Dr. Harry Arthurs, who chaired the recent Ontario Expert Commission on Pensions. Together, they considered all possible changes to the plan to safeguard its long-term viability and affordability.

Many members of plan staff expended literally thousands of hours of work to support the working group's efforts.

The result of their deliberations is contained in a report that will be presented to the membership in September. It will focus on two new processes:

- First, an independent review of the rate-of-return assumption used to estimate the value of plan liabilities. This transparent process is designed to allow the partners to put the issue behind them with confidence; and
- Second, a review of options, including possible changes to future contribution and benefit levels, if the filing valuation shows a funding shortfall in 2012.

The working group per se now has been dissolved and its membership reconstituted into the Partners' Consultative Committee – a group that meets every quarter - which will act on the findings and recommendations.

A separate communication and education group also was formed as part of the filing agreement. It developed and delivered a comprehensive collection of materials – speakers' kits, webcasts, fact sheets, newsletters and more -- to help the general membership understand the funding challenges facing the plan. If you haven't yet done so, I encourage you to visit the tripartite website, FundingYourPension.com, and review the materials housed there. There have been nearly 5,000 unique visitors to the site to-date. 95% of the visitors surveyed said the presentation helped them understand the pension plan's funding challenges, and 92% said they would recommend the site to others. This communications effort will continue through the next filing.

With interest rates as low as they are, markets as weak as they are, remnants of the 2008 loss still to be smoothed in, and maturing demographics, we expect our deficit will be significant on that date. It is pretty clear that it will be a deficit too large to be "tweaked" away with minor adjustments. Nor is there sufficient time for investment returns or interest rates to cure the problem. Changes will have to be made to ensure the plan's sustainability.

We are very pleased that the partners have gotten ahead of the game, by ensuring that there is a list of options, already researched and available for careful and thoughtful discussion in the months to come.

What will the solution be? It is of course too soon to tell. That will be up to the people at the table when the time comes. While I don't know what the ultimate decision will be, I do know this: it will be the best informed, most transparent decision made since we first found ourselves in a deficit position in 2003.

And now it is my pleasure to invite Rod Albert to present his update on behalf of his fellow board members.

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