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Date: April 11, 2007
To: Governing Council Business Board Members
From: George Luste, President, University of Toronto Faculty Association (UTFA)
Re: **April 11, 2007 Business Board Agenda Item #4, regarding
University of Toronto Asset Management Corp (UTAM) 2006 Annual Report**

My 5-minute time limit requires I be very brief. Regrettably this restricts what and how I present.

Background: UTFA members are the major stakeholder group in the UofT Registered and SRA pension plans. About 65% of the liabilities or almost \$2 billion in pension assets pertain to faculty and librarians. We are the major stakeholder in the pension plan, yet we have no meaningful governance role.

Question: Did UTAM add investment value to the \$2.87 billion UofT pension fund in 2006?

Answer: In 2006 UTAM's returns were less than a similar passive index fund.

Therefore: "No, I do not see how UTAM added real investment value".

If in 2006 UTAM had realized the passive index return of 13.5% instead of the actual 12.1%, the \$2.87 billion pension plan would today have an additional \$40 million¹ in assets.

Further details:

(i) UTAM Annual Report 2006² and the "balanced fund" equivalence

(a) Page 13 "The Pension and LTCAP portfolios can be viewed as essentially "balanced funds", which would traditionally have about 60% allocation to Equities and 40% to Fixed Income. The resulting 3:2 ratio (i.e. 60:40) is roughly approximated in the overall policy asset mix for these portfolios.

(b) Page 16. 12.1% is the net return for the UofT Pension fund

(ii) Passive returns for equity and bond indexes (in Canadian dollars)

The attached table from Libra Investment Management provides a year by year summary of various indexes and their real (not nominal) returns. It also shows the annual inflation number.

(iii) 2006 passive index return for a balanced fund (w/ 60% equities + 40% bonds).

Assume the 60% Equity portion is divided equally between Canadian (via TSX Composite), U.S. (via S&P 500) and International (via MSCI EAFE). The resulting 2006 returns are:

3.08%	TSX real return 15.4% x 0.2
2.84%	S&P 500 real return 14.2% x 0.2
5.02%	MSCI EAFE real return 25.1% x 0.2
0.96%	All Can Bonds real return 2.4% x 0.4
1.60%	Inflation in 2006 (converting real return to nominal return)

13.50% is the sum total nominal return for the above passive index balanced fund

¹ Or about \$37 million if one assumes 10 basis points as the passive index management cost.

² Draft copy of UTAM's 2006 Annual Report (in pdf format) is on the web at <http://www.utoronto.ca/govcncl/bac/details/bb/2006-07/bba20070411-4-item.pdf>

Index (Passive) Annual Real Return Table

Real (not nominal) annual pretax returns in Canadian dollars													
Year	Annual Canadian Inflation	Short 3 month T-bills	Long Canadian Bonds	Long Canadian Bonds	All Canadian Bonds	Real Return Bonds	TSX Composite	S&P 500	Wilshire 5000	MSCI EAFE	MSCI Emerging Markets	Gold Bullion	Year
1970	1.3%	5.4%		14.7%			-4.8%	-3.7%		-17.1%		-1.4%	1970
1971	5.0%	-1.1%		9.3%			2.9%	7.9%		23.8%		9.6%	1971
1972	5.1%	-1.5%		2.8%			21.2%	12.4%		30.0%		38.9%	1972
1973	9.4%	-3.8%		-6.7%			-8.3%	-22.0%		-21.5%		52.7%	1973
1974	12.3%	-3.9%		-15.1%			-34.1%	-34.8%		-31.0%		52.7%	1974
1975	9.5%	-1.8%		-1.3%			8.3%	28.6%	29.8%	28.5%		-28.5%	1975
1976	5.8%	3.3%		16.8%			4.9%	16.2%	18.7%	-2.7%		-10.1%	1976
1977	9.5%	-1.5%		-0.3%			1.1%	-8.0%	-3.5%	18.3%		21.5%	1977
1978	8.4%	0.1%		-4.0%			19.7%	6.6%	9.2%	34.3%		37.0%	1978
1979	9.8%	1.9%		-11.4%			31.9%	6.4%	12.7%	-4.7%		103.2%	1979
1980	11.1%	2.1%	-1.8%	-8.1%	-4.1%		17.1%	21.9%	23.0%	14.5%		6.0%	1980
1981	12.2%	6.4%	-3.4%	-12.7%	-7.1%		-20.0%	-15.8%	-14.8%	-12.4%		-40.3%	1981
1982	9.2%	5.8%	17.9%	33.6%	23.9%		-3.4%	15.3%	12.6%	-5.9%		9.1%	1982
1983	4.6%	5.1%	9.9%	4.8%	6.6%		29.5%	18.6%	19.5%	20.6%		-19.0%	1983
1984	3.7%	7.7%	8.8%	12.7%	10.6%		-5.9%	8.8%	5.6%	10.5%		-17.2%	1984
1985	4.4%	5.5%	10.2%	21.4%	16.1%		19.8%	33.5%	34.4%	58.9%		7.1%	1985
1986	4.2%	5.1%	6.9%	12.5%	10.1%		4.6%	12.5%	10.0%	61.1%		15.0%	1986
1987	4.2%	4.2%	2.7%	-2.3%	-0.1%		1.7%	-4.9%	-7.5%	12.9%		10.5%	1987
1988	4.0%	5.4%	4.2%	7.0%	5.6%		6.8%	2.9%	4.0%	13.4%	23.9%	-25.2%	1988
1989	5.2%	7.0%	5.0%	9.4%	7.2%		15.3%	21.5%	19.2%	2.2%	52.2%	-10.4%	1989
1990	5.0%	8.3%	5.3%	-0.6%	2.4%		-18.8%	-7.5%	-10.4%	-26.7%	-14.6%	-5.9%	1990
1991	3.8%	5.8%	13.6%	20.7%	17.7%		7.9%	25.2%	28.8%	7.9%	53.4%	-13.7%	1991
1992	2.1%	4.5%	6.3%	9.2%	7.6%	1.8%	-3.5%	15.9%	17.4%	-5.1%	20.0%	1.5%	1992
1993	1.7%	3.7%	11.4%	20.1%	16.2%	16.8%	30.3%	12.6%	13.8%	35.9%	78.8%	20.3%	1993
1994	0.2%	5.1%	-1.2%	-7.5%	-4.5%	-13.9%	-0.4%	7.3%	5.8%	14.4%	-1.9%	3.6%	1994
1995	1.8%	5.4%	13.5%	24.2%	18.6%	14.7%	12.6%	31.6%	30.5%	6.7%	-9.4%	-3.4%	1995
1996	2.2%	2.6%	8.4%	11.7%	9.8%	9.3%	25.6%	20.9%	19.2%	4.6%	4.3%	-6.2%	1996
1997	0.7%	2.3%	4.1%	17.6%	8.8%	3.9%	14.1%	38.2%	36.0%	5.7%	-8.4%	-18.6%	1997
1998	1.0%	3.7%	5.6%	11.7%	8.1%	4.9%	-2.6%	36.4%	31.0%	27.7%	-20.8%	5.2%	1998
1999	2.6%	2.2%	-0.3%	-8.3%	-3.6%	5.3%	28.4%	11.1%	13.4%	16.8%	52.7%	-7.5%	1999
2000	3.2%	2.2%	4.9%	9.4%	6.8%	13.0%	4.0%	-8.5%	-10.3%	-13.4%	-30.2%	-4.8%	2000
2001	0.7%	3.7%	8.6%	5.3%	7.3%	-0.1%	-13.2%	-7.0%	-6.1%	-16.9%	3.0%	6.3%	2001
2002	3.9%	-1.3%	2.3%	6.9%	4.7%	11.0%	-15.7%	-25.7%	-24.5%	-19.6%	-10.4%	19.7%	2002
2003	2.0%	0.9%	3.1%	6.9%	4.6%	11.0%	24.2%	3.7%	6.1%	12.1%	25.9%	-3.4%	2003
2004	2.1%	0.2%	2.9%	8.0%	4.9%	15.1%	12.1%	0.7%	2.3%	9.6%	14.4%	-5.0%	2004
2005	2.2%	0.5%	0.2%	11.4%	4.2%	12.8%	21.5%	-0.6%	0.7%	8.0%	27.4%	11.5%	2005
2006	1.6%	2.3%	2.3%	2.4%	2.4%	-4.5%	15.4%	14.2%	14.2%	25.1%	30.7%	21.5%	2006
Average	4.7%	2.8%	5.6%	6.3%	6.8%	6.7%	6.8%	7.9%	10.7%	8.8%	15.3%	6.3%	Average
St Dev	3.6%	3.1%	5.1%	11.5%	7.4%	8.4%	16.1%	17.7%	15.1%	21.3%	29.3%	26.8%	St Dev

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Table - A

Sources for Table -A

The enclosed worksheets show the annual total returns (income plus price changes) for a representative array of investable asset classes, per well-accepted indexes. One worksheet shows nominal returns by year, the other real returns (net of inflation). All returns are in terms of Canadian dollars. Foreign asset class returns are adjusted for year-end to year-end foreign exchange fluctuations to put them in Canadian dollar terms.

Data for these series was obtained or derived from public websites wherever possible. Data whose source is listed as the Globe & Mail or Financial Post were obtained or derived from public library stacks or microfilm.

Exchange rates 1970 Globe & Mail
1971-1992 [Prof. Werner Antweiler, UBC](#)
1993-date [Bank of Canada](#)

Inflation 1970-1988 Statistics Canada, Table 326-0001
1989-date [BC Government Statistics](#)

3 month T-bills 1970-date [Libra Investment Management Inc.](#)

Short Canadian bonds (SCM Short) 1980-1992 Financial Post
1993-2002 Globe & Mail
2003-date [Scotia Capital](#)

Long Canadian bonds (SCM Long) 1970-1992 Digitized from <http://www.globefund.com>
1993-2002 Globe & Mail
2003-date [Scotia Capital](#)

All Canadian bonds (SCM Universe) 1980-1992 Financial Post
1993-2002 Globe & Mail
2003-date [Scotia Capital](#)

Real return bonds 1992-2002 Derived from pension plan reports by Libra
2003-date [Scotia Capital](#)

S&P/TSX Composite 1970-date [Canadian Institute of Actuaries](#)

S&P 500 1970-2002 [Economagic.com](#)
2003-date [Standard & Poors](#)

Wilshire 5000 1975-date [Wilshire Associates](#)

MSCI EAFE 1970-date [MSCI](#)

MSCI Emerging Markets 1988-date [MSCI](#)

Gold bullion 1970-date [Kitco](#)

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Date: March 27, 2006
To: Governing Council Business Board Members
From: George Luste, UTFA President

**Re: University of Toronto Asset Management Corporation (UTAM)
2005 Annual Report – some comments**

My 5-minute time limit requires I be very brief.

Background: (i) given the proposed 5% budget cut across academic divisions for 2006-07 and (ii) given the Administration's claim during the recent negotiations with UTFA of a pension plan deficit as the reason why current pensions should **not** be fully indexed to inflation (2.2% in 2005), --- both the investment performance and the management costs of UTAM are important issues for UTFA members.

Pension Plan Expenses: UTAM expenses are a significant component of the increased total cost of administering the UofT Pension Plan. Prior to 1998 (before UTAM) the annual pension plan costs were under \$3 million. Today they are in excess of \$14 million. The attached Exhibit-A shows the dramatic increase over time in the total pension plan expenses. (In 2004-05 the total average annual cost was \$1,030 for each of the 13,934 plan members,- active, retired, terminated, suspended, exempt, etc.)

Passive Index Returns vs UTAM Returns: Investment expenses are a performance drag and can reduce returns. Passive investing (as opposed to active investing) has minimal cost. Exhibit-B illustrates how the returns from a simple passive allocation outperform active UTAM returns from 2003 to 2005.

Comments on the UTAM 2005 Annual Report:

(i) **Management Expenses and Investment Fees:** There is minimal information on expenses and fees in the UTAM report. Costs do matter. There are now two to three layers of active management costs. What are the costs for each layer ? How do they differ between the Pension and LTCAP accounts? How do they breakdown by asset class in the UTAM Exhibit 6 table?

(ii) **Cumulative Value Added:** On page 10 of the UTAM report it states: "*UTAM has generated cumulative value added of approximately \$615 million above the target for Pension and LTCAP combined*". I do not believe this increase in asset value should be attributed to UTAM (as the attached Exhibit B and C illustrate). Markets have been generous during the past three years.

(iii) **Risk:** The UTAM Report fails to explain or discuss this important topic adequately. Risk comes in many shapes and sizes. It is not always easy to quantify. The standard deviation numbers (or volatility) in Exhibit 8 (page 17) of the UTAM report do not seem to fully reconcile with the corresponding standard deviation numbers derived at the bottom of the attached Exhibit C.