The AMBACHTSHEER Letter

Sustainable Pension Design • Effective Pension Management

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CAN THE *CPP INVESTMENTS* ORGANIZATION PASS THE 'LEGITIMACY' TEST?

*"**Legitimacy**: authenticity, validity ... ability to be defended by logic and justification"*

Oxford Dictionary

"0verstaffed, overpaid, and underperforming, the CPP investment fund is in need of a sharp course correction."

Andrew Coyne, The Globe & Mail
May 30, 2025

What is the *Canadian Pension Model*?

As the *CPP Investments* organization is the biggest of eight large Canadian pension funds with similar characteristics (*CDPQ*, *PSP*, *OTPP*, *OMERS*, *HOOPP*, *BCI*, *AIMCO* are the other seven), Andrew Coyne's cited opinion piece effectively questioned the legitimacy of an organization design that has globally become known as the *Canadian Pension Model*. Paraphrasing the Oxford Dictionary definition of 'legitimacy', is the *Model* really unauthentic, invalid, and unable to be defended by logic and justification, as Mr. Coyne suggests? That is the question this *Letter* addresses.

My 2021 *Journal of Portfolio Management* article titled "**The Canadian Pension Model: Past, Present, and Future**" set out the *Canadian Pension Model* story in considerable detail. Its origin came from Peter Drucker's 1976 book "The Unseen Revolution" where he foresaw that workers would end up owning the means of production not through violent revolution, but through their pension funds. This would eventually place pension organizations in the position of managing retirement savings in the best interests of current and future workers. To do this job well, Drucker argued that these organizations needed to convey legitimacy, be well governed, and use scale economies to create value at an affordable cost.

Through a series of fortuitous events set out in the article, *Ontario Teachers' Pension Plan* would become the globe's first Drucker Model pension organization in 1991. As *OTPP* began to produce measurable value -for-money, other Canadian pension organizations took note and began to move to the Drucker model as well. This included *CPP Investments*, which launched in 1999. Today, Canada's eight largest pension pools are often referred to as the 'Maple 8'.

Canadian Pension Model Investment Performance

The 2021 *JPM* article allocated considerable space to reporting the investment performance of the Maple 8. This raises an important question: what is the best benchmark against which to evaluate investment performance of these funds? Ideally, that benchmark should be investible, low cost, with risk exposure that represents the best-possible assessment of the risk tolerance of the pension plan's risk bearers. For example, a passively invested, well-diversified 60% equities/40% bonds mix might be a typical benchmark portfolio for assessing the investment performance of a pool of retirement savings.

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The article cited a detailed study by *CEM Benchmarking* comparing the average 2006-2015 investment performance of the 'Maple 8' versus the average performance of its global universe of 132 other funds for which it had 2006-2015 data. The 'Maple 8' outperformed their benchmarks by an average 0.6%/yr versus an average of 0.1%/yr for the other 132 funds. More importantly, only one of the eight Maple funds (i.e., 12.5% of the total) underperformed its benchmark, while 51 (39% of the total) of the other 132 funds did. The article also cited a 2020 study by Americans Lipshitz and Walter which compared the most recent average 10-year investment returns and funded status of the largest 10 Canadian funds versus those of the largest 25 U.S. funds. The 10 Canadian funds generated an average 9.0% return and were 100% funded versus its liabilities. Over the same period, the 25 U.S. funds generated an average 6.8% return and were 62% funded.

What About *CPP Investments*?

These empirical findings confirm the global perception of the financial strength and investment prowess of the *Canadian Pension Model*. But where does *CPP Investments* fit into this story? Is it an exception to the 'Maple 8' rule of superiority? Unfortunately, its just-released Annual Report does not make it easy to answer this question. In its discussion of identifying the most relevant benchmark against which to compare its actually achieved investment return, the Report goes on a hard-to-understand series of tangents.

For example, there is considerable discussion of Market Risk Targets, which were called Reference Portfolios in prior Annual Reports. As an example, one of a number of possible Market Risk Targets is an 85-15 stock/bond mix. However, the Report notes that such a strategy exposes *CPP* stakeholders to the potential of "severe losses", and that prudence suggests a relevant benchmark portfolio should embody greater diversification against such an outcome. This leads to the creation of a better diversified, but still passive Benchmark Portfolio.[i] The Report states *CPP Investments* generated a strong 10-year net value added of 1.4%/year against such an investible well-diversified passive Benchmark Portfolio.

Rather than stopping there, the Report also disclosed that since implementing active management in 2006 , *CPP Investments* generated a -0.2%/year net value added when measured against a combination of Market Risk Targets from fiscal 2007 to 2024 and the Benchmark Portfolio in fiscal 2025. It is difficult to understand how this is useful information if the Market Risk Targets are not deemed to be investable well-diversified reference portfolios for benchmarking purposes. Yet, it is this single misleading -0.2%/ year number that triggered the May 30 Coyne anti-*CPP Investments* tirade. The lesson for *CPP Investments* is that too much Annual Report information can be as bad as too little information. That is especially the case when that misleading 'too much' information overshadows *CPP Investments*' strong investment management performance over the course of the last 10 years when properly measured.

The Power of 'Ownership Investing'

In addition to this 'too much information' lesson, there is another topic *CPP Investments*, and other funds built on the Drucker 'legitimacy' foundation, should be addressing more forcefully. If pension funds are the custodians of accumulated workers' capital, they should act that way. That is, they should search for ways to raise the productivity of that capital for the benefit of its owners, and through them, for society at large. We have been calling this 'ownership investing' in previous *Letter*s.

Indeed, *CPP Investments* is already engaged in 'ownership investing'. Fifteen years ago, it founded the *Portfolio Value Creation Group*, which it explains this way: "*Portfolio Value Creation (PVC) works closely with deal teams, portfolio company management, and deal partners to create value within portfolio companies. Working across all sectors, geographies, and deal phases, PVC helps with diligence, enhances governance, monitors portfolio companies, drives operational change, and facilitates transfer of best practices across all areas of CPPIB's asset management and value-creating activities.*"

The *PVC* idea arose as part of *CPP Investments*' decision to invest *CPP* assets more actively. This meant playing an active role in assisting portfolio companies build better businesses. Since 2010, the *PVC Group* has grown considerably, numbering some 40 professionals today, spread across offices in Toronto, London, Hong Kong, Mumbai, San Francisco, and Sao Paulo.

What kind of skills/experience set is required to do this broad mandate justice? Here is a composite CV of the 14 senior members of the *PVC Group* roughly organized into six categories:

1. Accelerating sales growth, pricing optimization, sales and market execution, corporate strategy
2. Margin improvement and efficiency, cost structure optimization, operations productivity
3. Corporate governance, asset onboarding, carve-outs/post-merger integration, cyber security
4. Sustainable value creation and integration, decarbonization, physical risk resilience
5. Human capital management, organization design and effectiveness
6. Advanced data and analytics, AI-based innovation, digital transformation

The collective skills/experience package of *PVC*'s leadership group was built partially through direct, hands-on experience working in commercial organizations and investment asset management roles, and partially through the team's expertise in business transformation while working for major consulting organizations such as *Bain*, *Boston Consulting*, and *McKinsey*.

How does the *PVC Group* partner closely with Investment Teams and jointly engage with *CPP Investments* portfolio companies to protect and create long term value? When I posed this question to them last year, their response was:

Most of our engagements fall into one of three categories:

1. *Comprehensive strategy review and formulation*
2. *Operational transformation*
3. *Stand*-up of new businesses and carve-outs

Examples in each category are:

COMPREHENSIVE STRATEGY REVIEW AND FORMULATION

- *Situations can change after a portfolio investment has been made. For example, business models can shift, or new market opportunities can emerge. Such changes could warrant a strategic review of the investment.*
- *In such cases, PVC's approach is to focus on identifying how the investment's key value-drivers may be changing and engaging its senior management to adjust its strategic plan accordingly. These reviews typically involve leveraging subject experts in the sector and clearly understanding the geographical and cultural contexts.*
- *Two examples of this kind of intervention involved a U.S.-based mid-market private lender and a global digital infrastructure provider. In the former case, new profit pools were unlocked with the design and implementation of a new line of business. In the latter case, a priority-setting challenge was addressed through a PVC-led strategic review. The result was renewed clarity on which businesses to invest in further, which businesses to downplay, or even fully exit.*

OPERATIONAL TRANSFORMATIONS

- *We expect all our portfolio investment companies to have clear value-creation plans. Situations arise where such plans become stale and need to be updated. PVC can identify such situations and help boards and senior managements discover what is needed to drive transformation.*
- *This may involve sales force design, product or services pricing, and/or their cost-effective delivery (e.g., supply chain optimization, procurement, or operational effectiveness). PVC helps investment companies focus on actions that move the needle and ensure that the right resources are assigned to the work.*
- *For example, over the last five years, PVC has supported an infrastructure company management team in developing and implementing several efficiency programs. These programs have delivered US$70M /year in run-rate savings while maintaining high asset integrity. Three examples are restructuring a major third-party service contract, leveraging GenAI to create operational efficiencies, and building an incentives-supported 'lean' management culture.*

STAND-UP OF NEW BUSINESSES AND CARVE-OUTS

- *PVC runs a standard onboarding process for new investments. This sometimes leads to an opportunity to unlock a promising business unit from a larger company. Such a unit may have been neglected and suffered from underinvestment. In such a case, PVC may assist in building out organization functions in HR, Finance, Legal, IT, and recruiting the requisite leadership team. At the same time, it ensures that the new policies and procedures are fit for purpose, and consistent with organization standards.*
- *For example, CPP Investments bought a large financial services unit of a conglomerate, which it chose to set up as a stand-alone business. In this case, PVC negotiated a transition services agreement with the seller. This enabled the continuity of the business while setting up its new long-term operational framework. Interim executives were brought in to cover the key functional roles until permanent hires could be made. PVC ran an extensive process to select these key executive leaders, as well as board members for the new governance function.*

Rethinking the Focus of *CPP Investments* Annual Report

Canadian communications guru Marshall McLuhan once proclaimed that "*the medium is the message*". So, in the context of this *Letter*, if *CPP Investments*' message to its stakeholders is to convey 'legitimacy', then the 'ownership investing' strategies described above would be powerful mediums to convey that message. Andrew Coyne might even write a complimentary column about it.

Keith Ambachtsheer

Endnotes:

i. *For more on the benchmarking distortions caused by excessive passive management in global financial markets, see the just-released 2025 study "**Passive Aggressive: The Risks of Passive Investing Dominance**" by Chris Brightman and Campbell Harvey. The key message of the study is that large flows into passive strategies undermine diversification and increase systematic risk.*

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