O Canada!

Can the UK LGPS emulate Canada's 'Maple Eight'? Alex Janiaud finds out

Summary
• The UK government is considering a Canadian-style pension model to tap into Local Government Pension Scheme (LGPS) investment.
• Canada's eight large public sector pension schemes have a much higher allocation to private equity and infrastructure assets than their UK counterparts, although their respective allocations to domestic assets vary.
• UK pension trustees have a fiduciary responsibility to prioritise their members and not the fortunes of the UK economy.

Chancellor, Rachel Reeves, is the latest in a line of UK politicians seeking to channel UK pension money into domestic assets.

In September, the Treasury, the Department for Work and Pensions the and Ministry for Housing, Communities and Local Government issued a sweeping call for evidence that included questions on the potential for a more consolidated LGPS, with a view to boosting investment in UK listed and unlisted equities and infrastructure.

The government asked if there is "a case for establishing additional incentives or requirements" for Local Government Pension Scheme (LGPS) funds, as well as DC schemes, to

increase their portfolio allocations to UK assets and asset classes. The preceding Conservative government shared its hope of mobilising LGPS funds, publishing a consultation outcome in November 2023.

Labour's Pension Schemes Bill and pension review aspires to support this aim. And in August, Reeves said that she wanted LGPS funds to learn from the Canadian pension system, ahead of a meeting with representatives from 'Maple Eight', a group of large Canadian pension funds.

"The size of Canadian pension schemes means they can invest far more in productive assets like vital infrastructure than ours do," she says. "I want British schemes to learn lessons from the Canadian model and fire up the UK economy, which would deliver better returns for savers and unlock billions of pounds of investment."

Pension Protection Fund chief executive officer, Michelle Ostermann, tells *Pensions Age* that "it's understandable that the government's eye has been drawn to Canada as part of its pension review, given that it is now considered a global leader in the pensions space".

"The experience of Canada demonstrates how size and scale is critical to good outcomes for members," she continues. "The challenge the UK faces to achieve a similar scale is the fragmentation of the pensions market," she adds.

Canada is 'eating the UK's lunch'

Like the LGPS, the Maple Eight are large investors with globally diverse portfolios. Together managing more than £570 billion in assets, five out of the eight funds allocate over half of their assets towards private markets, according to Hymans Robertson.

Canadian schemes have followed a similar trajectory in their allocations to domestic equities, with allocation to Canadian public equities dropping from 80 per cent of their total equity investments in 1990 to just 10 per cent in 2020, according to Letko Brosseau.

There are significant differences in the extent to which these funds have domestic investment exposure, however. The Healthcare of Ontario Pension Plan has the greatest exposure to Canadian assets at 55 per cent of its portfolio, per Hymans Robertson, while the Canada Pension Plan Investment Board has Canadian exposure of just 12 per cent.

LGPS fund investment in UK equities is low. Just 6 per cent of LGPS fund assets were held in UK equities in 2023, compared with 45 per cent of LGPS assets held either in non-UK equities, according to the LGPS Board.

"As UK pensions have switched out of UK equities, they have helped feed a doom loop of lower demand, lower valuations, and a less dynamic market," a report by New Financial says.

Canadian public sector pension funds are lightyears ahead of the LGPS when it comes to private equity and infrastructure. Just 8 per cent of LGPS fund assets were invested in private equity and 7 per cent in infrastructure last year, while Canadian public sector pension funds hold 34 per cent of their assets in private equity and infrastructure in aggregate, according to the New Financial study – although just 7 per cent of the Maple Eight's infrastructure investment is in Canadian assets, according to Hymans Robertson.

"Canada's thirst for growth from private markets is leading to them eating the UK's lunch," Pension SuperHaven director, Henry Tapper, tells *Pensions Age.*

UK central government interference

Hymans Robertson head of LGPS client consulting, Robbie McInroy, observes that the UK and Canadian systems have similar levels of assets invested domestically and that both countries' governments are focused on encouraging more domestic investment.

The LGPS and Canadian funds both have a clear desire to tackle climate risk and carbon transition challenges, he adds. But there are differences between the way politicians in both countries interact with their public sector pension funds.

"A founding principle of the Canadian model is an aim to align interests and collaborate between the different stakeholders without political interference," McInroy says.

"The ongoing trend for *[the UK]* central government to involve itself in the LGPS investments and structure would make it hard to argue there is more independence from political interference than for the Canadian funds," he continues. McInroy also notes the Maple Eight funds' extensive use of internal investment management compared to the LGPS.

The previous UK government's 2023 consultation proposed requiring LGPS funds in England and Wales to invest up to 5 per cent of their assets in "levelling up the UK", and to update guidance to compel funds to consider meeting the government's ambition of a 10 per cent allocation to private equity in the LGPS.

It may take an even more robust approach from Labour to push LGPS funds to invest in domestic assets.

Pensions Management Institute director of policy and public affairs, Tim Middleton, tells *Pensions Age* that trustees will place the interests of their members above the government's desire for more domestic investment.

"Pension schemes won't invest more heavily in UK equities just because the government would like them to," he says. "There would have to be sound investment decisions for them to invest their stakeholding in the UK equity market."

"If that's going to happen then it's likely that the government will have to resort to either incentivisation, or even more ominously, some form of coercion." Middleton warns that this "will create real conflict between the pension system and the government".

UK pension funds also face a practical obstacle to investing in patient capital, Middleton observes.

"There is no proper exchange for that kind of asset, so it's very difficult for pension schemes to invest in that particular class of asset and divest at the same time as well," he says.

"Unless, and until there is a more efficient system – an exchange of some sort – there are going to be significant obstacles for all UK pension schemes to increase their holdings as the government wants."

Ostermann is, however, optimistic that the UK can learn from Canada.

"Over the past decade, Canadian DB pension plans have modernised to address shifts in life expectancy, employment patterns, and retirement age choices," she says. "This has been achieved through hybrid designs, for example by utilising shared-risk models or by incorporating target benefit provisions.

"I believe there is an opportunity for the UK to draw on the Canadian experience here as we evolve our thinking around consolidation, sophisticated investment management and governance."

Written by Alex Janiaud, a freelance journalist