In Conversation with John Crocker

Kevin Smith

Across the globe, the past year's financial crisis has severely undercut the financial solvency of many pension plans in nearly every sector. The Hospitals of Ontario Pension Plan (HOOPP) is one of Canada's largest and most respected pension plans for healthcare workers. According to the most recent figures, HOOPP serves 155,000 active members, 79,000 pensioners and 321 participating employers (www.hoopp.com/about/glance).

John Crocker became president and chief executive officer (CEO) of HOOPP in 2001. He is responsible for HOOPP's overall leadership and management. John is a member and former director of the Toronto Society of Financial Analysts, a member of the CFA Institute and a member of the Pension Investment Association of Canada. On March 18, 2009, Kevin Smith, the president and CEO of St. Joseph's Healthcare Hamilton, interviewed John Crocker to discover how HOOPP is weathering the storm and protecting its members' futures.

HQ: Everyone around the world is concerned about the current economic state. What does the average HOOPP member need to know about the crisis? And how secure are our pensions?

JC: This is the worst economic crisis since the Great Depression. It has been fed by global real estate excesses driven by very low interest rates and too much leverage. The world is now dealing with the unwinding of that situation. Are HOOPP pensions secure? The answer is yes. On April 1, 2009, pensioners will receive an increase of three quarters of last year's inflation rate. That means their pensions will go up by about a 0.87% cost of living adjustment (COLA). As well, the price in benefits will remain stable through the end of 2010.

HQ: Would you give policy makers and government leaders low, medium or high marks for how they have responded to the crisis?

JC: The policy response from the central bankers and governments has been very vigorous – I give them high marks. There is some controversy, and people are worried about looming inflation and debased balance sheets; however, since at least Labour Day 2008, no major banks have, I believe, collapsed. The media and the public demand instant action. But policy decisions often take months – or even quarters – to have an impact. People need to be a little more patient and let time work.

Are HOOPP pensions secure? The answer is yes.

HQ: Some people are worried that if the crisis intensifies, there could be a greater negative effect on HOOPP funds and, possibly, a direct impact on members. Are there any

seminal events or issues that would make you reconsider how well HOOPP can meet its obligations?

JC: When you look at the failures to date, in most cases they arose from governance shortcomings. Managers and boards were either asleep at the switch or abdicated their responsibilities. One of HOOPP's strengths is that our board is monitoring events and regularly modelling scenarios – not just for today or tomorrow, but for one, three, five and 10 years from now. And we are basing these models on investments, actuarial assumptions and other important factors to determine what must be done. HOOPP's board will be keeping its long-range headlights switched on and will not abdicate its responsibilities. It will make decisions that are right for the long term.

Our board members understand their fiduciary duties in terms of what is in the best interests of the quarter of a million people who depend on HOOPP.

HOOPP also has the advantage of being cash-flow positive in the pension fund itself. While we take in roughly $1.5–$1.6 billion every year, we pay out around $1–1.1 billion. That leaves an annual surplus of between $300 and $500 million, which helps to build the fund. HOOPP will be cash-flow positive for at least the next 10 years. Unlike some other major pension funds that are cash-flow negative to the tune of a billion or two, we have a lot more flexibility. As well, our membership is growing. I don't have the final numbers, but I believe we gained between 6,000 and 7,000 members this year.

HQ: Historically, HOOPP has achieved well beyond its benchmarks. In the current situation, benchmarks are likely to be lower, but are they also harder to achieve?

JC: One of the reasons we have had relative success this year is that we're starting to institute a liability-driven approach to our investments, and that means we will change our benchmarks over time. Most other people in the sector, whether they administer mutual funds or pension funds, have asset-class benchmarks. They ask themselves, "Did we beat the Toronto Stock Exchange?" or, "Did we beat the Standard & Poor's 500?" But those kinds of comparisons are irrelevant. I have to pay $80 million a month in pensions, and that number is growing – that's the reality I'm truly concerned about.

Another important consideration is that HOOPP is a "price taker." Therefore, if all the markets are down dramatically, it is unrealistic to expect us to be up. But, while it is obviously going to be a tough year for the economy, we believe that the huge policy response by central governments, central banks and others will have an effect. As we get to the latter part of 2009, things ought to begin to get a little better. In fact, with so many excellent investment opportunities out there, we see some exciting future potential.

HQ: You mentioned next year's 0.87% COLA. Is it reasonable for pensioners to assume that similar adjustments are likely in the following years?

JC: HOOPP was one of the pioneers to go from *guaranteed* COLA to ad hoc COLA. That new approach gives us tremendous flexibility for dealing with the kind of storm we're in now. While the board is strongly committed to ad hoc COLA, we are obviously affected by financial markets and returns. We made a policy decision that permitted ad hoc 75% of the consumer price index (CPI) to be realized by members every year that returns permit it; if the money isn't there to do it, then obviously the board won't. But I can assure you that there's strong sentiment around the board table to continue with our commitment.

HQ: Other than outstanding management, why has HOOPP has done so well?

JC: Our success starts with the board because it sets the tone for the organization. Our joint governance model works because it allows a rounded view of issues. No matter what their backgrounds are, our board members understand their fiduciary duties in terms of what is in the best interests of the quarter of a million people who depend on HOOPP. Members are committed to attracting and retaining good people and to creating the right compensation approaches, and other means, to ensure we can do the job for members.

HQ: You have also put in place structures aimed at long-term growth.

JC: One of the differences I find at HOOPP is that we don't talk about quarterly results at all. In other positions I've held, I would go to client meetings and they would have the *Globe and Mail* out and, depending on the topical news of the day, they would say, "Did you own mining stocks or oil stocks or gold stocks, or this or that?" But that kind of thinking is totally irrelevant. The board and the staff keep their eyes on long-term results while planning for various scenarios and eventualities.

HQ: Are you doing anything special that other boards – such as hospital or investment boards – should be learning? How have you crafted such a successful and long-term oriented board?

JC: Unlike corporate or not-for-profit organizations where you can influence and even control who gets on the boards, at HOOPP the five "settlers" have the right to appoint anybody they want: the Ontario Hospital Association (OHA) appoints half the trustees (i.e., eight) and the four unions each appoint two.

That being said, we have spent a lot of time working with the settlers to explain the amount of work involved: usually about 200–300 hours a year. And we also emphasize that we're running a sophisticated financial institution here and that board members will be dealing with a host of issues, including investments, human resources and technology. Whether it's the OHA or the unions, they all have concerns about where healthcare is going, and it is in their best interests for HOOPP to be a success. In fact, HOOPP is a keystone for all these organizations. We're all in this together, and the settlers need to ensure that they have people on the board who support the initiatives we undertake. In turn, we are able to support the settlers.

Everyone at HOOOP is a member of the plan – we all have a personal stake in HOOPP's money.

HQ: Some people have expressed concern about HOOPP's ability to fund pensions for an increasingly aging population. Do you worry that the demographic shift will put HOOPP at risk?

JC: Ten years ago, the average age of an active HOOPP member was around 43 or 44. One might expect the average age now to be a little higher; however, that is not the case. At other major Ontario-based funds and pension providers, the average age has been rising. And that's problematic because as your active base becomes smaller your financial flexibility also decreases.

HQ: That's very good news, and I think it will alleviate quite a bit of anxiety for some of our more nervous members.

JC: Yes, I agree. In addition, part of our strategy is to be more aggressive in explaining the benefits of HOOPP membership for organizations that are recruiting workers. Whether it's individual hospitals, the healthcare sector as a whole, HealthForceOntario or other government initiatives, we want to spread the word that when you're trying to recruit people from the United States, Europe or other provinces, HOOPP membership ought to be a key selling feature.

This is part of HOOPP's transformation into an "influencing" organization. Unlike in past years, we now actively spread the HOOPP story to government and other stakeholders. Hospitals and OHA are concerned about the sector's future and a whole host of related issues. The unions are equally anxious about their futures in this era of deficits, economic slowdown, technology changes and cost pressures. We're looking to work with all those parties and the government to see whether we can help and also influence policy in the pensions area.

HQ: Do you have any advice for individual investors about the kinds of markers to which they should be attuned?

JC: Two big problems confront all investors: financial/banking system problems and real estate problems. With real estate, individuals can pay attention to statistics such as foreclosure rates and housing starts. In terms of the stock market, they can monitor how financial stocks are doing relative to the market as a whole. Through much of the past six months or so, when stocks in general were down, financial stocks were down even more. What we need to watch for is something like the market going up 2% and financial stocks rising 2.5%. If we see that foreclosure rates have dropped, housing starts have begun to improve and bank stocks have risen, those indicators will likely tell us that the worst of the storm has passed.

HQ: Do you have any advice for hospital foundations on how to weather this storm?

JC: Focus on income. Focusing on growth is fine in a strong, booming market. Whether it's bonds or common shares with good solid dividends, that's what foundations should focus on now and into the future.

HQ: When the world starts recovering from the economic meltdown, finding the best people is going to be a challenge. How will you ensure that HOOPP succeeds?

JC: Our board has focused on succession planning, training and leadership development. It's an old story: if you pay peanuts, you get monkeys. We need to ensure we're competitive in the financial services arena and that we offer a great working environment. We expect people to work hard, but we're not going to work people 24 hours a day. And we have the luxury of being able to take a long-term view: we don't shoot people because they had a bad week or bad month. As well, everyone at HOOOP is a member of the plan. We all have a personal stake in HOOPP's money, and our people take a proprietary interest in doing the right thing for the membership. HQ