Caisse de dépôt et placement du Québec

ANNUAL REPORT 2008

A PDF version of the Annual Report 2008 – Additional Information is provided on a compact disc at the end of this document.

The "General notes" at the end of this document provide information that facilitates an understanding of the texts, tables and figures that follow.
The Annual Report 2008 and the Annual Report 2008 – Additional Information are available on line at www.lacaisse.com and on a compact disc at the end of this document.

PROFILE

The Caisse de dépôt et placement du Québec is one of the largest institutional fund managers in Canada. The Caisse was created in 1965 by an Act of the National Assembly of Québec to manage the funds contributed to the province's newly created universal pension plan, the Régime de rentes du Québec. In the decades that followed, many other public organizations also became depositors, increasing the pool of capital that the Caisse represents.

OUR MISSION

"The mission of the Fund is to receive moneys on deposit as provided by law and manage them with a view to achieving optimal return on capital within the framework of depositors' investment policies while at the same time contributing to Québec's economic development."

Act respecting the Caisse de dépôt et placement du Québec, section 4.1

OUR DEPOSITORS

The Caisse's 25 depositors as at December 31, 2008, were mainly Québec public and private pension and insurance plans. Depositors' net assets totalled $120.1 billion at year-end, with the seven main depositors accounting for 96% of assets.

OUR OPERATIONS

The Caisse invests its depositors' funds in various asset classes, including fixed income, equities, hedge funds, commodity financial instruments, private equity, infrastructure, real estate and real estate debt. The Caisse invests in Québec, in Canada and on international markets.

This geographic diversification allows it to take advantage of investment opportunities that arise in all regions of the world. Investments outside Canada represented 42% of depositors' total assets as at December 31, 2008. In addition to its depositors' funds, the Caisse administers or manages assets for clients, mainly in the real estate sector.

OUR PEOPLE

The Caisse had 813 employees as at December 31, 2008. The real estate units Cadim, Ivanhoe Cambridge, SITQ and Otera Capital employed a total of 1,957 people.

To work at the Caisse is to come in contact each day with highly qualified professionals in various areas, recruited in Québec and elsewhere in the world. The Caisse is justifiably proud of its experienced professionals and up-and-coming generation of talent.

Almost 50% of the Caisse's employees have more than 15 years of experience in their area of expertise. Their overall level of education is also exemplary. For example, 83% of employees have a university degree, and 41% have a postgraduate degree.

Many employees belong to a recognized professional order of accountants, actuaries, engineers, lawyers or notaries. Moreover, in 2008, a total of 113 employees held the designation of Chartered Financial Analyst (CFA) and 17 held that of Financial Risk Manager (FRM). The Caisse endorses the principles of employment equity and aims for a level of diversity that is representative of the various groups that make up our society.

MANAGEMENT PRINCIPLES

The Caisse's approach to human resources is based on three principles: meritocracy, transparency and collaboration. This approach ensures employees are committed to achieving the Caisse's objectives, for it recognizes performance and fosters transparent communication in a collaborative environment.

/ MERITOCRACY
Encourage employees to achieve an outstanding level of success by recognizing performance and rewarding those who excel.

/ TRANSPARENCY
Promote clear, open communication between team leaders on various hierarchical levels and their employees to establish specific objectives and expectations.

/ COLLABORATION
Promote engagement and commitment so that employees work together to achieve objectives.

OUR VALUES

The officers and employees of the Caisse share and act on four fundamental values in the day-to-day performance of their duties. These values shape the organization's identity and are the basis for its business policies and depositor-service approach.

/ EXCELLENCE
The determination to excel and the commitment to aim constantly for outstanding success in a given field of expertise. This value is based on development of employees' competencies and recognition of their performance as well as the use of best practices for each area.

/ ETHICS
Endorsement by all employees of high standards and criteria in their behaviour and business practices and of rules of conduct for relations with colleagues, suppliers and partners.

/ BOLDNESS
Leadership and a flair for innovation in all areas of activity. It is also the determination to take calculated risks in order to act on promising business and investment opportunities and to achieve objectives, as well as the ability to learn from one's mistakes.

/ TRANSPARENCY
Clear communication with employees, depositors, the public and other stakeholders as well as accurate, regular reporting on practices, objectives and results.

OUR INVESTMENT PHILOSOPHY

The Caisse strives to achieve its target returns in accordance with the depositors' investment policies and the resulting risk budgets. This active management of depositors' holdings is based on the following investment philosophy:

/ ACTIVE MANAGEMENT
Exploit opportunities in all financial markets by adapting strategies to economic, political and social issues.

/ FUNDAMENTAL AND OPPORTUNISTIC APPROACH
Emphasize the intrinsic value of companies as well as their potential earnings and value creation over the medium and long terms. Take advantage of investment opportunities as circumstances arise.

/ OPEN MANAGEMENT
Use external management or partnerships to complement in-house expertise, especially for certain distant markets.

/ INTERNAL RESEARCH AND INVESTMENT PROCESS
Invest on the basis of internal research and rigorous analysis.

/ RISK MANAGEMENT
Optimize risk level and allocation, using a range of financial products, various management styles and investment diversification based on company size, sector and geographic location.

/ ACCOUNTABILITY OF MANAGERS
Ensure portfolio managers are fully accountable for their results.

MAIN FINANCIAL DATA

A DISAPPOINTING RETURN IN 2008

TABLE 1
RETURNS[1]
(for periods ended December 31)

	CAISSE OVERALL RETURN (Weighted average return earned for Caisse's depositors)	NET INVESTMENT RESULTS	VALUE ADDED (Overall return less the return on market indexes)		QUARTILE RANKING IN RELATION TO LARGE CANADIAN PENSION FUNDS (RBC Dexia Investor Services – Plans Over $1 Billion Universe)	INDIVIDUAL RETURNS FOR THE MAIN DEPOSITORS
2008	**(25.0)%**	**$ (39.8) B**	**(6.6)%**	**$ (10.5) B**	**Fourth**	**(26.9)% – (17.0)%**
2007	**5.6 %**	**$ 7.9 B**	**(0.6)%**	**$ (1.2) B**	**First**	**5.1% – 6.6%**
2006	**14.6 %**	**$ 17.8 B**	**1.9 %**	**$ 2.0 B**	**First**	**12.5% – 16.3%**
2005	**14.7 %**	**$ 15.2 B**	**1.8 %**	**$ 1.5 B**	**First**	**13.4% – 17.9%**
2004	**12.2 %**	**$ 10.8 B**	**1.0 %**	**$ 0.6 B**	**First**	**11.3% – 14.6%**

AVERAGE ANNUAL RETURNS
(for the period ended December 31, 2008)

	CAISSE OVERALL RETURN	VALUE ADDED	QUARTILE RANKING	INDIVIDUAL RETURNS FOR THE MAIN DEPOSITORS
2006-2008 (3 years)	**(3.2)%**	**(2.4)%**	**Fourth**	**(3.9)% – (0.5)%**
2004-2008 (5 years)	**3.1 %**	**(1.0)%**	**Third**	**2.4 % – 4.9 %**

1 Figures in dollars are net of operating expenses.

MAIN FINANCIAL DATA

FIGURE 2

COMPOSITION OF TOTAL ASSETS UNDER MANAGEMENT

(as at December 31, 2008)

DEPOSITORS

Depositors' net assets **$120.1 B** + Liabilities (primarily assets financed by borrowing) **$66.8 B**

DEPOSITORS' TOTAL ASSETS

$186.9 B

+

CLIENTS

Assets under management **$17.3 B** + Assets under administration **$16.2 B**

ASSETS UNDER MANAGEMENT AND ASSETS UNDER ADMINISTRATION

$33.5 B

=

TOTAL ASSETS UNDER MANAGEMENT

$220.4 B

FIGURE 3

CHANGES IN ASSETS

(for periods ended December 31 – in billions of dollars)

- Depositors' net assets
- Depositors' total assets
- Total assets under management

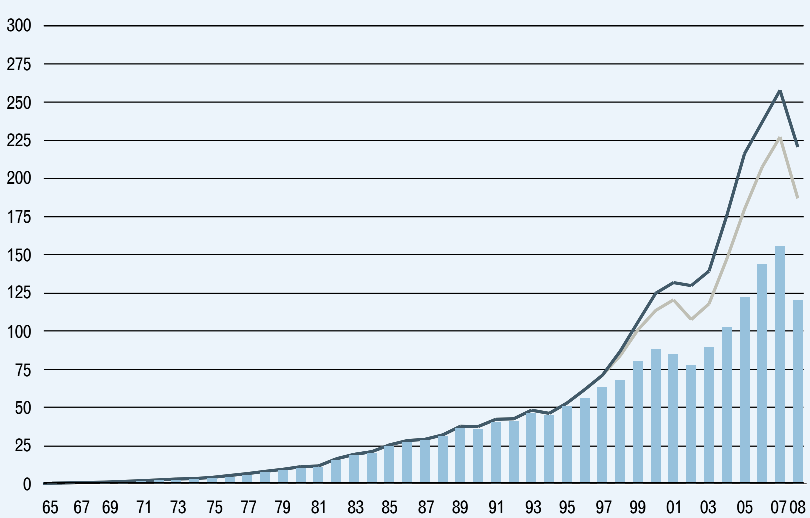


FIGURE 4

CHANGES IN ASSETS

(for periods ended December 31 – in billions of dollars)

- Depositors' net assets
- Depositors' total assets
- Total assets under management

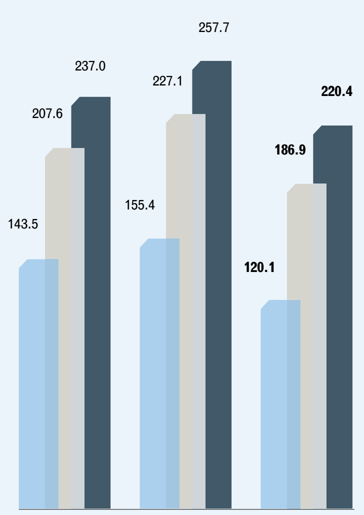


TABLE 5

RESULTS AND CHANGES IN TOTAL ASSETS UNDER MANAGEMENT

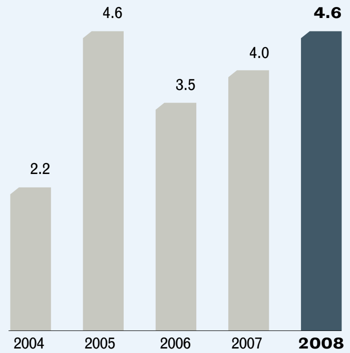
(for periods ended December 31 – in millions of dollars)

	2008	2007
Net investment results		
Investment income	**6,161**	6,531
Less:		
Operating expenses	**263**	261
External management fees	**51**	69
Net investment income	**5,847**	6,201
Gains (losses) on the sale of investments	**(23,228)**	9,427
Total realized income (losses)	**(17,381)**	15,628
Unrealized decrease in value of investments and liabilities related to investments	**(19,034)**	(5,860)
Unrealized decrease in value of investments in third-party and bank-sponsored ABCP, net of back interest	**(3,401)**	(1,897)
Total unrealized decrease in value	**(22,435)**	(7,757)
Net investment results	**(39,816)**	7,871
Excess depositors' deposits over withdrawals	**4,554**	4,000
Increase (decrease) in net assets	**(35,262)**	11,871
Depositors' net assets	**120,088**	155,350
Liabilities (primarily assets financed by borrowing)	**66,787**	71,799
Depositors' total assets	**186,875**	227,149
Assets under management	**17,364**	16,498
Assets under administration	**16,185**	14,098
Assets under management and assets under administration	**33,549**	30,596
Total assets under management	**220,424**	257,745

FIGURE 6

DEPOSITORS' SURPLUS DEPOSITS OVER WITHDRAWALS

(for periods ended December 31 – in billions of dollars)



MAIN FINANCIAL DATA

TABLE 7

NET ASSETS, RETURNS AND VALUE ADDED

(for periods ended December 31)

	2008				3 years 2006-2008			5 years 2004-2008		
Asset class	Net assets $ billion	%	Return $ million	Value added[1] (b.p.)	%	Return $ million	Value added[1] (b.p.)	%	Return $ million	Value added[1] (b.p.)
Fixed Income and Currencies	**52.2**	**4.4**	**2,231**	**(145)**	4.1	5,563	(41)	5.2	10,434	(21)
Equity Markets	**26.4**	**(36.7)**	**(21,257)**	**(89)**	(6.9)	(9,313)	24	1.3	1,899	(2)
Hedge Funds	**5.3**	**(21.3)**	**(1,487)**	**(42)**	(4.3)	(788)	32	1.0	(290)	264
Private Equity	**14.0**	**(36.0)**	**(7,968)**	**281**	(3.9)	(2,941)	535	5.5	572	648
Real Estate	**25.4**	**(16.1)**	**(4,910)**	**(1,352)**	4.1	1,874	(576)	11.9	7,628	(117)
Asset Allocation and other[2]	**0.3**	**–**	**(2,013)**	**–**	–	(1,671)	–	–	(1,784)	–
Expense for third-party and bank-sponsored ABCP	**(5.8)**	**–**	**(3,969)**	**–**	–	(5,866)	–	–	(5,866)	–
	120.1[3]	**(25.0)**	**(39,816)**[3]	**(658)**	(3.2)	(14,221)	(238)	3.1	11,754	(100)

1 In relation to benchmark indexes.

2 The results of these operations include those of Rebalancing Decisions and are presented net of expenses.

3 The net assets and the return in dollars are those presented in the combined financial statements audited by the Auditor General of Québec. For more information, see note 11 to table 1 of the section "Financial statistics and review" in Annual Report 2008 – Additional Information.

TABLE 8

DETAILED BREAKDOWN OF DEPOSITORS' NET ASSETS BY ASSET CLASS

(percentage of fair value as at December 31)

	2008	2007
Fixed income		
Short Term Investments	**3.7**	1.5
Real Return Bonds	**0.5**	0.6
Bonds	**37.4**	25.4
Long Term Bonds	**2.6**	2.0
	44.2	29.5
Equity markets		
Canadian Equity	**10.9**	12.9
U.S. Equity	**1.9**	4.4
Foreign Equity	**3.4**	6.4
Emerging Markets Equity	**2.6**	3.2
Québec International	**3.6**	9.4
	22.4	36.3
Other investments		
Investments and Infrastructures	**3.6**	4.1
Private Equity	**8.3**	7.3
Real Estate Debt	**9.6**	7.4
Real Estate	**12.0**	11.3
Hedge Funds	**3.3**	3.4
Commodities	**1.1**	1.6
	37.9	35.1
Asset Allocation and other	**0.4**	0.3
Third-party and bank-sponsored ABCP[1]	**(4.9)**	(1.2)
Total	**100.0**	100.0

1 To track third-party and bank-sponsored ABCP more effectively, the Caisse has separated its reporting on it from that on management of its specialized portfolios.

TABLE 9

THE CAISSE'S 25 DEPOSITORS AND THE BODIES THAT ADMINISTER THEM

(fair value as at December 31 – in millions of dollars)

	First deposit	Depositors' net assets 2008 $	2008 %	2007 $	2007 %
PENSION PLANS					
Régie des rentes du Québec					
Fonds du Régime de rentes du Québec	1966	**26,227**	**21.9**	34,761	22.4
Commission de la construction du Québec					
Supplemental Pension Plan for Employees of the Québec Construction Industry	1970	**9,864**	**8.2**	11,774	7.6
Commission administrative des régimes de retraite et d'assurances					
Government and Public Employees Retirement Plan	1973	**33,794**	**28.2**	46,063	29.7
Pension Plan for Management	1973	**6,029**	**5.0**	7,701	5.0
Individual Plans	1977	**202**	**0.2**	274	0.2
Pension Plan for Elected Municipal Officials	1989	**128**	**0.1**	173	0.1
Régime de retraite pour certains employés de la Commission scolaire de la Capitale	2006	**39**	**–**	49	–
Régime de rentes pour le personnel non enseignant de la Commission des écoles catholiques de Montréal	2007	**241**	**0.2**	304	0.2
Régime de retraite des membres de la Sûreté du Québec	2007	**35**	**–**	21	–
Régime complémentaire de rentes des techniciens ambulanciers/ paramédics et des services préhospitaliers d'urgence	1990	**208**	**0.2**	254	0.2
Ministère des Finances, Gouvernement du Québec					
Fonds d'amortissement des régimes de retraite	1994	**26,101**	**21.7**	31,962	20.6
Régime de retraite de l'Université du Québec	2004	**167**	**0.1**	212	0.1
Régime de retraite du personnel des CPE et des garderies privées conventionnées du Québec	2005	**47**	**–**	53	–
Régime complémentaire de retraite des employés syndiqués de la Commission de la construction du Québec	2006	**19**	**–**	15	–
Régime de retraite des employés de la Ville de Laval	2007	**33**	**–**	27	–
INSURANCE PLANS					
Régie des marchés agricoles et alimentaires du Québec					
Fonds d'assurance-garantie	1967	**6**	**–**	6	–
La Financière agricole du Québec	1968	**196**	**0.2**	241	0.2
Autorité des marchés financiers	1969	**446**	**0.4**	437	0.3
Commission de la santé et de la sécurité du travail					
Health and Work Safety Fund	1973	**7,849**	**6.5**	10,987	7.1
Société de l'assurance automobile du Québec					
Fonds d'assurance automobile du Québec	1978	**5,772**	**4.8**	8,283	5.3
Fédération des producteurs de bovins du Québec	1989	**3**	**–**	3	–
Régime de rentes de survivants	1997	**327**	**0.3**	462	0.3
Conseil de gestion de l'assurance parentale					
Parental Insurance Fund	2005	**2**	**–**	200	0.1
OTHER DEPOSITORS					
Office de la protection du consommateur	1992	**34**	**–**	27	–
Société des alcools du Québec	1994	**83**	**0.1**	53	–
Ministère des Finances, Gouvernement du Québec					
Fonds des générations	2007	**1,297**	**1.1**	1,008	0.6
Fonds de la réserve budgétaire du gouvernement du Québec	2008	**337**	**0.3**	–	–
Fonds des congés de maladie accumulés	2008	**602**	**0.5**	–	–
Total		**120,088**	**100.0**	155,350	100.0

MESSAGE FROM THE CHAIRMAN

A YEAR OF COUNTLESS CHALLENGES

A FINANCIAL CRISIS WITHOUT PRECEDENT

For the Caisse and many other institutional investors, 2008 will no doubt go down in history as a year of countless challenges.

The combination of several factors means the Caisse has recorded results that are well below expectations. Like the organization's other stakeholders, the Board of Directors can only express its disappointment with the returns obtained in 2008. Still, my colleagues on the Board and I can testify to the efforts made by the senior management team and all employees to contend with the worst financial crisis to have hit our economy since the Caisse was created.

It will take several years to analyze fully the impacts of the crisis, which, we hope, peaked in the fourth quarter of 2008. Never had we seen such a cataclysm sweep over almost all the world's asset classes, sectors of activity and markets at the same time. With such a widespread debacle, diversification no longer held up. But diversification was an integral part of the Caisse's approach and had enabled it to prosper for many years.

ABCP: FOCUSING ON THE SOLUTION

In this unusual market context, the negotiations to restructure asset-backed commercial paper (ABCP) continued. After acknowledging that we had placed too much confidence in this type of investment as regards its liquidity, we applied ourselves to working out a solution. Caisse senior management demonstrated a keen sense of leadership to ensure a solution was put in place. Had it not been for their diligence and tenacity, the impact of the ABCP investments could have been much greater. With the restructuring plan applied under the Montréal Accord, the Caisse will be able to recover a good portion of the amounts invested.

The ABCP episode prompted the Board of Directors and senior management to take measures to prevent similar situations from occurring. In other words, the lessons learned have resulted in concrete action.

SENIOR MANAGEMENT CHANGES

These measures and the steps taken toward the end of 2008 to minimize the effects of the crisis took place in a context of change within the Caisse's senior management ranks. Despite the climate of uncertainty caused by the transition period, the senior management team remained fully functional. They continued their activities with the usual dedication, in line with clearly defined priorities and guidelines. They therefore moved to preserve capital, to contain risks and to maintain liquidity at a prudent level – as the President and Chief Executive Officer explains in his message. The Board of Directors obtained assurance that all matters would receive due attention and appropriate treatment. I should like to take this opportunity to point out the exceptional work done by Fernand Perreault, who took over as President and Chief Executive Officer. In the circumstances, the task was not an easy one, but he quickly rallied the troops to take up the challenge. Thanks are also due to Richard Guay for the work he accomplished and his commitment to the Caisse. Moreover, I am grateful to Henri-Paul Rousseau for his major contribution to the development of the organization. He demonstrated tremendous leadership and dedication during his six years at the Caisse.

DEBATE OVER THE CAISSE

With all these events, the Caisse has constantly been a subject of debate in recent months. Given the institution's importance and role in Québec's financial sector, it is entirely legitimate to want information on it. Still, it is vital to keep things in perspective and to understand that the Caisse's priority is to continue its mission by playing its role as an investor to benefit its depositors. This is especially true in the context of a financial crisis, when the managers must draw on all their energy to adjust to the new market reality while continuing to play an active role in Québec.

We should not forget that formal reporting mechanisms have been established and for several years have been followed to the letter to ensure timely communication of the required information to all parties concerned. The Board of Directors can bear me out. Moreover, I should add that very few of the world's institutional investors publish such an exhaustive annual report and provide such a detailed website on their operations.

GOVERNANCE CHALLENGES

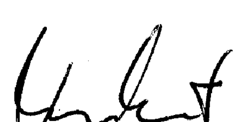
Overseeing the Caisse's reporting is an integral part of the Board's mandate, and we devote all the requisite attention to it. The activity reports of the Board and its committees, at the end of the Annual Report, give an idea of the scope of the governance work done in 2008. Owing to the context, our schedule was unusually full. The Board and the committees held many special meetings to monitor the various matters effectively and to support Caisse senior management in the application of solutions to the financial crisis.

In particular, we are closely monitoring the review of the Caisse's operational model, undertaken in the last quarter. Once this exercise is complete, the Board and the Executive Committee will have the necessary information to resume planning for the three years to come. In this way, it will be possible to develop a 2010-2012 strategic plan adapted to the new market context.

AN ORGANIZATION WORTHY OF OUR SUPPORT

This is the last Annual Report I shall sign as Chairman. Most certainly it would have been preferable to end my mandate on a note that was more positive for the Caisse. It is an institution worthy of the support of all, so that it can continue its mission effectively. Beyond the difficulties of recent months, I retain from my experience that the Caisse has the strength and the skills to deal with adversity and to quickly re-establish its position as one of the top-ranked fund managers.

In conclusion, I should like to express my deep gratitude to everyone I have worked side by side with during my four years as Chairman. We have developed tremendous team spirit, which has strengthened my conviction that the Caisse has everything it needs to play its role fully. I offer all employees, senior management, the Board of Directors and Robert Tessier, the new Chairman, my best wishes for success.



/ **PIERRE BRUNET**
Chairman

March 5, 2009

MESSAGE FROM THE PRESIDENT AND CHIEF EXECUTIVE OFFICER

A MAJOR FINANCIAL CRISIS

The financial crisis that characterized 2008 had a considerable impact on the results of institutional fund managers; in fact, most recorded the worst returns in their history. The Caisse de dépôt et placement du Québec was no exception, ending the year with an overall return of -25.0%. This figure corresponds to the weighted average return for the Caisse's 25 depositors, whose net assets fell from $155.4 billion to $120.1 billion between January 1 and December 31, 2008.

These results are extremely disappointing, especially as they fall considerably short of the -18.5% return on the benchmark portfolio and the -18.4% median return recorded by large Canadian pension funds. The Caisse therefore did not add value in relation to the portfolios' benchmark indexes and, after four years of first-quartile returns, placed in the last quartile of its comparison universe.[1]

Given these results, I believe it is important to understand fully the factors that gave rise to this situation and to draw lessons for the years to come.

THREE MONTHS THAT CHANGED THE WORLD

The subprime mortgage debacle in the United States played an important role in setting off a chain reaction that led, in the fall of 2008, to the worst financial crisis since the 1930s. The bankruptcy of the investment bank Lehman Brothers, on September 15, was another catalyst; it caused investors to lose confidence in the markets, for they doubted the U.S. government's will to backstop financial institutions in difficulty.

The sudden increase in risk aversion caused credit spreads to widen to an extraordinary degree. This phenomenon began in 2007 but worsened in 2008, causing the market value of most assets to plummet. As market volatility soared, financial institutions responded swiftly by cutting off credit to preserve their liquidity.

Overnight, the normal mechanisms on certain markets known for their liquidity were completely disrupted. The currency market was especially affected. For example, in October the Canadian dollar experienced the sharpest drop in its history.

1 Source: RBC Dexia Investor Services – Plans Over $1 Billion Universe.

IMPACT OF THE CRISIS ON THE CAISSE'S RETURN

Confronted with these unprecedented events and a climate of increasing uncertainty, the Caisse moved quickly to adjust its strategy and the composition of its portfolio. To preserve depositors' capital, it maintained its liquidity at a prudent level and reduced its equity exposure. The weight of fixed-income securities in the overall portfolio rose from 30% to 44% and that of equities fell from 36% to 22%, to reduce the portfolio's absolute risk.

A SUDDEN, ACROSS-THE-BOARD DROP IN INVESTMENT VALUES

These changes had a positive impact on the return as at December 31, 2008. Even so, the Caisse's diversified portfolio was hit hard by the dislocation of the markets and the sudden, across-the-board drop in the value of all asset classes in the fall.

The net investment results for 2008 amount to -$39.8 billion. Unrealized decreases in value, or paper losses, represent 56.3% ($22.4 billion) of that amount. This high proportion is due partly to the accounting standards that the Caisse must abide by; they require that investments be valued as if they were available for sale as at December 31, even in a context of high volatility. These standards also apply to private equity and real estate, even though they are usually held for several years.

The picture would be quite different had we been able to value these investments as a function of how long we plan to hold them. We would have been able to take into account their economic value rather than a value reflecting the extreme volatility of the markets. It should be noted that the Caisse's portfolios of non-traditional investments hold quality assets. Moreover, the investment income from these assets was up in 2008 and should continue to rise in 2009.

UNPRECEDENTED WEAKNESS OF THE CANADIAN DOLLAR

The sharp decrease in the value of the Canadian dollar in October pushed up the value of our foreign investments by $11.3 billion once they were converted into Canadian currency. The cost of the Caisse's currency hedging was $8.9 billion, however. This is a record amount, most of which is due to 100% hedging of foreign private equity and real estate investments.

The cost of foreign exchange hedging in 2008 has to be put into perspective. For the 10-year period that includes 2008, the effect of the hedging is slightly positive. The Caisse adopted its currency hedging policy about 15 years ago, and studies show that the effect of such hedging is neutral over the long term, provided that it remains consistent.

ASSET-BACKED COMMERCIAL PAPER

The additional $4.0-billion expense for asset-backed commercial paper (ABCP) is another consequence of the deteriorating market conditions in the fall of 2008. I should like to point out, however, that in this respect the year ended on a positive note, with the conclusion of an agreement that provides for the conversion of the ABCP into notes with an average maturity of seven years. With the application of this agreement, the Caisse is quite hopeful that a large portion of its provision for ABCP will be reversed in the years to come.

In hindsight, we placed too much confidence in these short-term securities, which had the highest rating and were therefore considered as safe as other money market products, such as treasury bills. It is true that the Caisse's ABCP was diversified in terms of issuers; but no overall limits were placed on this type of financial instrument, which has evolved over the years.

For a detailed analysis of the return on the Caisse's overall portfolio and specialized porfolios, please see the sections of the Annual Report that discuss these matters.

MESSAGE FROM THE PRESIDENT AND CHIEF EXECUTIVE OFFICER

MANAGING OUR RISKS MORE EFFECTIVELY

The Caisse has always made a special effort to identify, to measure and to control the risks associated with all its operations, especially active management of investments. It has therefore considerably stepped up its risk management activities in the past five years.

In 2007, in the wake of the ABCP crisis, it put in place new oversight and management measures, including the requirement of two rating sources for a financial instrument to be considered rated, a moratorium on new financial instruments and the introduction of centralized risk monitoring.

The ABPC episode and the financial crisis of 2008 have accelerated the application of an ambitious three-year plan to upgrade the Caisse's practices. The plan covers such matters as risk management in extreme scenarios, a more stringent approval process for new investment operations, and risk measurement and methodology.

REVIEWING THE CAISSE'S OPERATIONAL MODEL

More broadly, like all other large fund managers, the Caisse is confronted with the radical changes that are reshaping the financial environment.

In November 2008, Caisse senior management started a series of projects to review the organization's practices and operational model. In addition to risk management, which is central to our concerns, this work will cover such key aspects as management of the ABCP portfolio, currency hedging, liquidity management, leverage and target returns. From the organizational standpoint, the Caisse plans to bring together certain highly qualified employees who are scattered throughout the organization, a situation that is a secondary effect of the strong growth of recent years.

In 2009, the senior managers will apply the recommendations that emerge from this work. These gradual changes, along with the 2010-2012 strategic planning exercise, will be made in consultation with the depositors.

In terms of investments, we plan to rebalance the overall portfolio as a function of our assessment of the various markets. We should like to reiterate our utmost confidence in the value of our assets; moreover, we believe the Caisse's portfolio is well positioned to weather the continuing financial crisis.

Lastly, in a context in which access to credit is tight, the Caisse will continue to support solid Québec companies, in concert with the other players active in the market. To that end, the Private Equity group has set up a $1.5-billion program that will be deployed in the months to come.

RISING TO THE CHALLENGE

At the end of the most difficult year in its history, the Caisse is still one of the most solid financial institutions in Québec and Canada. It is still part of a small circle of fund managers that have the size and expertise to take part in the most promising opportunities on the international financial markets.

Over more than four decades, the Caisse has had mainly positive years. By staying focused on the depositors' long-term objectives, it has obtained an 8.3% average annual return since inception.

I personally have always been very proud to work for the Caisse, an outstanding organization that I have watched grow and prosper for almost 30 years, especially since I have had the honour of serving as President and Chief Executive Officer, surrounded by highly competent people in all our fields of activity.

I am convinced that, by drawing on its strengths, the Caisse can rise to the challenge of the financial crisis and continue to carry out its mission successfully, for the benefit of its depositors and, by extension, Québec as a whole.

In conclusion, I should like to thank the representatives of the 25 depositors for their patience and understanding, as well as for their confidence in the Caisse. Thanks are also due to the members of the Board of Directors for their support and dedication in all circumstances, particularly Pierre Brunet for his outstanding work as Chairman. I am also grateful to my colleagues on the Executive Committee and to all Caisse employees for their commitment and professionalism during a momentous year. Lastly, I should like to welcome Michael Sabia, my successor as President and Chief Executive Officer.

/ **FERNAND PERREAULT**
President and Chief Executive Officer

March 12, 2009

EXECUTIVE COMMITTEE

(as at Decembre 31, 2008)

From left:

FERNAND PERREAULT
Executive Vice-President Real Estate
Acting President and Chief Executive Officer from November 13, 2008 to January 7, 2009
President and Chief Executive Officer from January 8 to March 12, 2009

SUZANNE MASSON
Executive Vice-President Corporate Affairs and Secretary

MICHEL MALO
Executive Vice-President Hedge Funds

RICHARD GUAY
Chief Investment Officer until May 30, 2008
Acting President and Chief Executive Officer from May 30 to September 4, 2008
President and Chief Executive Officer from September 5, 2008 to January 7, 2009
Strategic Adviser from January 8, 2009

CHRISTIAN PESTRE
Executive Vice-President and Chief Strategist

NORMAND PROVOST
Executive Vice-President Private Equity

FRANÇOIS GRENIER
Executive Vice-President Equity Markets

SUSAN KUDZMAN
Executive Vice-President Depositors and Risk

GHISLAIN PARENT
Executive Vice-President Finance and Operations

V.P. PHAM
Executive Vice-President Information Technology until January 9, 2009

ROBERT W. DESNOYERS
Executive Vice-President Human Resources and Organizational Development

PHILIPPE ITHURBIDE
Executive Vice-President Fixed Income and Currencies

DEPOSITORS

TABLE 10
THE SEVEN MAIN DEPOSITORS

DEPOSITOR	TYPE OF PLAN	DESCRIPTION
Government and Public Employees Retirement Plan (RREGOP)	Pension plan	RREGOP consists primarily of contributions by employees who work in Québec's health and social services sector, education system and public sector. The plan is administered by the Commission administrative des régimes de retraite et d'assurances (CARRA).
Fonds du Régime de rentes du Québec	Pension plan	The fund contributes to Quebecers' income security, notably by providing for payment of a retirement pension. This mandatory plan is administered by the Régie des rentes du Québec (RRQ), and the contributions to the fund are made by employers and employees.
Fonds d'amortissement des régimes de retraite (FARR)	Pension plan	FARR provides for payment of retirement benefits that are the responsibility of the government, according to the provisions of the retirement plans for the public and parapublic sectors. The fund is financed by the Québec government and administered by the Ministère des Finances.
Supplemental Pension Plan for Employees of the Québec Construction Industry	Pension plan	The plan is administered by the Commission de la construction du Québec (CCQ). The contributions to the plan are paid by construction industry employers and workers.
Health and Work Safety Fund	Insurance plan	The fund mainly compensates workers who have work-related accidents and contributes to their rehabilitation. The fund is administered by the Commission de la santé et de la sécurité du travail (CSST) and financed by contributions from Québec employers.
Fonds d'assurance automobile du Québec	Insurance plan	The fund compensates victims of vehicular accidents and promotes traffic safety. It is financed mainly by fees collected by the Société de l'assurance automobile du Québec (SAAQ) for driver's licences and vehicle registration.
Pension Plan for Management (RRPE)	Pension plan	The RRPE consists of contributions by management employees in the public and parapublic sectors. The plan is administered by CARRA.

The Caisse serves its depositors, most of which are public and private Québec pension and insurance plans. Many of the Caisse's depositors are social security plans that provide retirement pensions or insurance benefits, such as the CSST and the SAAQ. Through these plans, a large majority of Quebecers are affected by the Caisse's operations.

The Caisse's undertaking to the depositors is to invest and manage their funds in such a way as to obtain a return consistent with their objectives and risk tolerance.

The Caisse had 25 depositors as at December 31, 2008. The Caisse's seven main depositors represent more than 96% of depositors' net assets. Twenty of the 25 depositors are obliged by law to have the Caisse invest the funds they collect from their contributors.

The other depositors are not obliged by law to deal with the Caisse but derive certain advantages from doing so, including access to various asset classes, which allow for greater diversification, at reasonable cost. Moreover, a large asset base allows considerable economies of scale in terms of transaction costs, research, computer systems, administrative support and skills development.

THE CAISSE'S RESPONSIBILITIES TOWARD A DEPOSITOR

The Caisse is responsible for managing the depositor's assets according to the investment policy established by the depositor. To that end, it provides fund management services, advisory services and periodic reporting. The Caisse has signed service agreements with most of its depositors.

FUND MANAGEMENT

/ It invests the moneys it receives with a view to an optimal return, in accordance with each depositor's investment policy.

/ It carries out research to determine attractive investment opportunities on various markets.

/ It designs and offers investment products to meet depositors' requirements.

ADVISORY SERVICES

/ It offers advisory services for the development and review of each depositor's investment policy, taking into account its target returns and risk tolerance.

/ It prepares economic and financial analyses and provides risk and return forecasts based on the index for each asset class.

/ It does allocation simulations involving various asset classes to optimize each depositor's benchmark portfolio.

/ It offers depositors information and training sessions on investment and the Caisse's operations.

REPORTING

/ It holds several meetings with each depositor during the year.

/ It submits regular reports on its financial position, its returns and their source, the value added in relation to the benchmark index and the risk assumed.

/ It issues certificates of compliance attesting that it has respected the investment policies.

A DEPOSITOR'S RESPONSIBILITIES TOWARD THE CAISSE

Each depositor is responsible for respecting the financial undertakings it makes to its participants. It is also responsible for establishing its investment policy, in co-operation with the experts at the Caisse.

In addition to its obligations to the Caisse, the depositor manages all relations with its participants. It is responsible for collecting their contributions and paying out their pension or insurance benefits. It also makes actuarial studies to determine the amount required to meet its financial obligations over the long term.

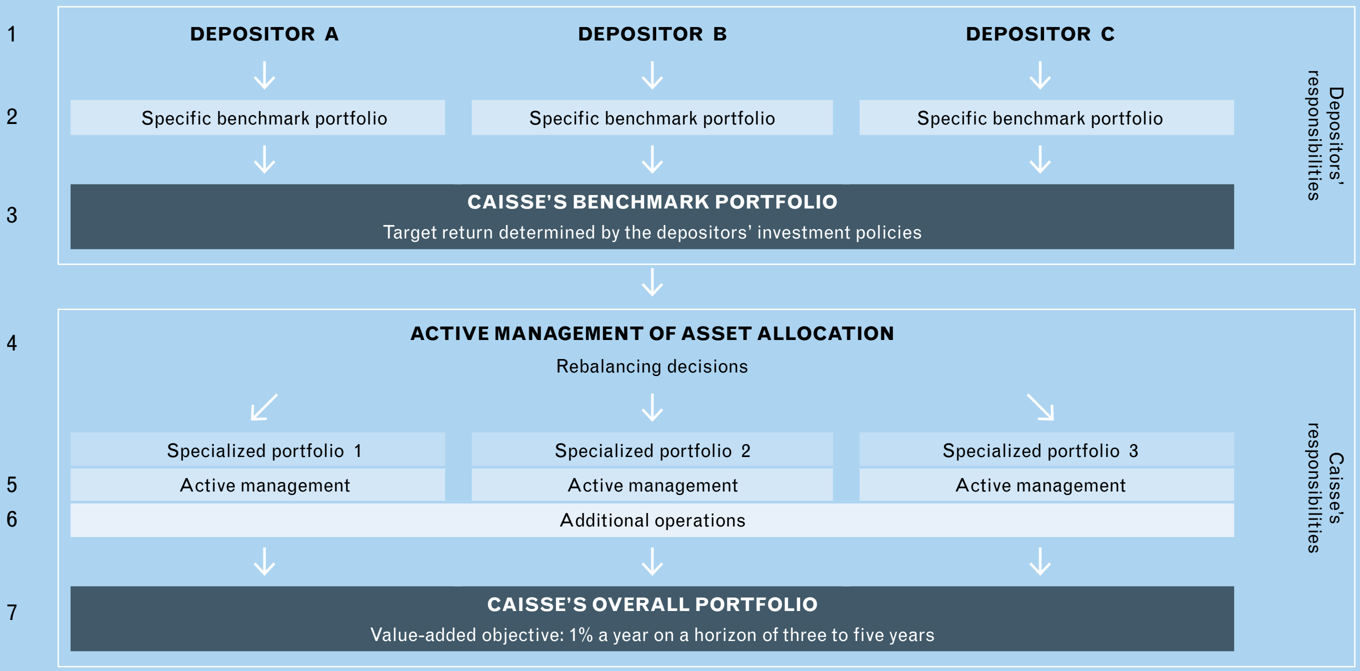
TARGET RETURNS

In co-operation with the depositors, the Caisse develops investment policies that enable them to achieve their long-term objectives. Each depositor's target return depends on its obligations to its participants. The weighted average target return of the depositors' benchmark portfolios is the target of the Caisse's benchmark portfolio. In 2008, this long-term target corresponded to a 7% average annual return.

It is important to bear in mind that returns are uncertain. According to estimates, the Caisse's return may be negative one year out of five and greater than 8% four years out of ten. In this context, close co-operation and constant dialogue between the depositors and the Caisse are crucial.

With active management of asset allocation and 18 specialized portfolios, the Caisse aims to outperform the benchmark indexes for all its portfolios by 1%.

FIGURE 11
PROCESS USED TO MANAGE DEPOSITORS' HOLDINGS



PROCESS USED TO MANAGE DEPOSITORS' HOLDINGS

THE DEPOSITORS

1 The Caisse manages the funds of 25 depositors, most of them pension and insurance plans, with a view to earning an optimal return.

2 Each depositor can invest its funds in 18 specialized portfolios that are similar to mutual funds, each holding financial products of the same type, such as stocks or bonds. The selected asset allocation becomes the depositor's specific benchmark portfolio, which sets out minimum and maximum weightings for each specialized portfolio. For example, a depositor may decide that the Canadian Equity portfolio will represent 10% to 20% of its benchmark portfolio, with a target of 15%.

3 The depositors each have a different target return because of the differences in their individual benchmark portfolios. The Caisse's benchmark portfolio is the weighted result of the depositors' benchmark portfolios.

THE CAISSE

4 The Caisse makes rebalancing decisions based on short- and medium-term economic forecasts and changes on the financial markets. These decisions are adjustments to the weightings of the specialized portfolios so as to enhance the return on the overall portfolio, within the upper and lower limits of the Caisse's benchmark portfolio. For example, the Caisse may decide to reduce the weighting of the equity portfolios and to increase that of the fixed-income portfolios.

5 The Caisse actively manages its 18 specialized portfolios. The managers of each portfolio conduct their investment operations with the objective of outperforming their benchmark index. For example, a Canadian equity manager will select securities with a view to outperforming the S&P/TSX Index.

6 Each investment group performs additional investment or financing operations intended to enhance the return on the specialized portfolios they are responsible for. For example, the Fixed Income and Currencies group borrows money at a low rate from financial institutions in return for the temporary transfer of liquid bonds provided as collateral.

7 The Caisse's overall portfolio presents the depositors' net asset allocation among the specialized portfolios at a given date, taking into account market fluctuations and active management of asset allocation. The Caisse's overall return corresponds to the weighted average return on the depositors' funds invested in the 18 specialized portfolios. Generally speaking, the Caisse aims to outperform the return on its benchmark portfolio by 1%.

RETURNS AND FINANCIAL POSITION

FINANCIAL CERTIFICATION[1]

FINANCIAL CERTIFICATE OF THE PRESIDENT AND CHIEF EXECUTIVE OFFICER

I, Fernand Perreault, President and Chief Executive Officer of the Caisse de dépôt et placement du Québec, certify that:

1/ I have reviewed the combined financial statements, the schedules (tables of returns), the press release announcing the annual results and the Annual Report (hereafter referred to as the "Annual Filings") of the Caisse de dépôt et placement du Québec (the "Caisse") for the year ended December 31, 2008.

2/ To the best of my knowledge, the Annual Filings do not contain any untrue statement of a material fact or omit to state a material fact that is required to be stated or necessary to make a statement that is not misleading in light of the circumstances in which it was made, with respect to the fiscal year covered by the Annual Filings.

3/ To the best of my knowledge, the combined financial statements and the other financial information included in the Annual Filings fairly present in all material respects the financial position of the Caisse as at the closing dates of the fiscal years presented in the Annual Filings, as well as the results of its operations for those years.

4/ The Executive Vice-President, Finance and Operations, and I are responsible for establishing and maintaining disclosure controls and procedures and internal control in respect of financial information for the Caisse, and we have:

a) Designed such disclosure controls and procedures, or caused them to be designed under our supervision, to provide reasonable assurance that material information relating to the Caisse, including its subsidiaries, is made known to us by others within those entities, particularly during the period in which the Annual Filings are prepared;

b) Designed such internal control over financial reporting, or caused it to be designed under our supervision, to provide reasonable assurance that the financial information is reliable and that the combined financial statements have been prepared, with a view to publication of the financial information, in accordance with generally accepted accounting principles in Canada; and

c) Evaluated the effectiveness of the disclosure controls and procedures as at the end of the fiscal year covered by the Annual Filings and ensured that the Caisse presents in the Annual Report 2008 our conclusions in accordance with our self-assessment.

5/ I have ensured that the Caisse presents in the Annual Report 2008 any material changes in internal control over financial reporting during the fiscal year ended December 31, 2008, that have had or it is reasonable to think may have a material effect on internal control over financial reporting.

/ **FERNAND PERREAULT**
President and Chief Executive Officer until March 12, 2009

March 27, 2009

1 Pursuant to the Caisse's financial certification policy, the President and Chief Executive Officer and the Executive Vice-President, Finance and Operations, sign a public financial certificate each year.

The two signing authorities responsible for the public financial certificates rely on internal financial certificates signed by various officers of the Caisse and its subsidiaries as well as work carried out under the financial certification program.

FINANCIAL CERTIFICATE OF THE EXECUTIVE VICE-PRESIDENT, FINANCE AND OPERATIONS

I, Ghislain Parent, Executive Vice-President, Finance and Operations, of the Caisse de dépôt et placement du Québec, certify that:

1/ I have reviewed the combined financial statements, the schedules (tables of returns), the press release announcing the annual results and the Annual Report (hereafter referred to as the "Annual Filings") of the Caisse de dépôt et placement du Québec (the "Caisse") for the year ended December 31, 2008.

2/ To the best of my knowledge, the Annual Filings do not contain any untrue statement of a material fact or omit to state a material fact that is required to be stated or necessary to make a statement that is not misleading in light of the circumstances in which it was made, with respect to the fiscal year covered by the Annual Filings.

3/ To the best of my knowledge, the combined financial statements and the other financial information included in the Annual Filings fairly present in all material respects the financial position of the Caisse as at the closing dates of the fiscal years presented in the Annual Filings, as well as the results of its operations for those years.

4/ The President and Chief Executive Officer and I are responsible for establishing and maintaining disclosure controls and procedures and internal control in respect of financial information for the Caisse, and we have:

a) Designed such disclosure controls and procedures, or caused them to be designed under our supervision, to provide reasonable assurance that material information relating to the Caisse, including its subsidiaries, is made known to us by others within those entities, particularly during the period in which the Annual Filings are prepared;

b) Designed such internal control over financial reporting, or caused it to be designed under our supervision, to provide reasonable assurance that the financial information is reliable and that the combined financial statements have been prepared, with a view to publication of the financial information, in accordance with generally accepted accounting principles in Canada; and

c) Evaluated the effectiveness of the disclosure controls and procedures as at the end of the fiscal year covered by the Annual Filings and ensured that the Caisse presents in the Annual Report 2008 our conclusions in accordance with our self-assessment.

5/ I have ensured that the Caisse presents in the Annual Report 2008 any material changes in internal control over financial reporting during the fiscal year ended December 31, 2008, that have had or it is reasonable to think may have a material effect on internal control over financial reporting.

/ **GHISLAIN PARENT**, FCA
Executive Vice-President, Finance and Operations

March 27, 2009

CONCLUSIONS ABOUT THE DESIGN OF INTERNAL CONTROL OVER FINANCIAL REPORTING

In 2008, the Disclosure Committee oversaw work that involved mainly improving and updating existing documentation as well as evaluating the design of internal control over financial reporting. The purpose of this evaluation of the design of internal control, which covers the Caisse's main financial processes, is to ensure that the Caisse's reporting objectives are reached.

The evaluation of the design of internal control over financial reporting was carried out with the framework usually adopted by North American companies, namely that of the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The work carried out enabled the Disclosure Committee to conclude that internal control over financial reporting is designed to provide reasonable assurance that the financial information presented is reliable and that the combined financial statements of the Caisse were prepared in accordance with generally accepted accounting principles in Canada.

Caisse management also carried out work that enabled it to determine that for the year ended December 31, 2008, the institution made no changes to internal control over financial reporting that could have had a material negative effect.

In the year to come, Caisse management will decide on the effectiveness of internal control over financial reporting. In that regard, the Canadian Securities Administrators selected December 15, 2008, as the effective date of the obligation to disclose the results of this last phase. This date excluded the large Canadian banks from this obligation for 2008 because their fiscal year ends on October 31. The Caisse has decided to follow the same schedule as such institutions and has deferred disclosure of the results of its evaluation of internal control effectiveness until 2009.

CONCLUSIONS ABOUT THE EFFECTIVENESS OF THE DISCLOSURE CONTROLS AND PROCEDURES

In accordance with the Caisse's financial certification policy, the design and effectiveness of the disclosure controls and procedures pertaining to the Annual Filings, namely the combined financial statements, the schedules (tables of returns), the press release announcing the annual results and the Annual Report, must be evaluated.

In addition to work involving internal control over financial reporting, the Disclosure Committee supervised work to update existing documentation and work concerning evaluation of the design and effectiveness of the disclosure controls and procedures.

As at December 31, 2008, this evaluation confirms that the disclosure controls and procedures are adequate and effective, and provide reasonable assurance that all relevant information is gathered and submitted in a timely fashion to senior management, in particular to the President and Chief Executive Officer and to the Executive Vice-President, Finance and Operations, so that the appropriate decisions concerning disclosure can be made.

The Board of Directors also approved the 2008 Annual Filings before their public disclosure.

MARKET CONTEXT 2008

HIGHLIGHTS

Financial crisis: The financial turmoil that began in the United States spread to the rest of the world. Tension on the financial markets in the wake of the Lehman Brothers bankruptcy caused credit spreads to widen to an extraordinary degree and most asset classes to go into freefall. The crisis was the worst since the 1930s, fuelling concerns that the international financial system was on the verge of collapse.

Economy: In the first half of the year, the still-resilient emerging market economies sustained global growth. The price of crude oil spiralled upward until mid-July, amid resurgent worries about inflation. As the financial crisis deepened in the fall, however, the worldwide economy tipped into a severe recession. In response, central banks cut their key rates to unusually low levels.

Liquid markets: Volatility and risk aversion soared. Stock market indexes recorded their steepest declines since the 1930s. Money markets came under extreme stress, and yields on government securities fell to new lows.

Private equity: The deal flow dried up in all segments of the market. The earnings of private equity companies declined as the liquidity and credit crisis intensified, recession encompassed the world and the stock market selloff pushed down investment valuations.

Real estate: Investors shunned commercial real estate. Widening credit spreads weighed heavily on portfolios of properties. Tight credit and the difficult economic outlook drove property values down and capitalization rates up.

ECONOMIC AND FINANCIAL CONTEXT

THE WORST FINANCIAL CRISIS SINCE THE 1930s BATTERS THE MARKETS

The financial crisis was preceded by strong credit growth and robust global economic activity. The rapid expansion of many export-driven economies, including China and the oil exporters, generated tremendous excess liquidity around the world. These funds tended to flow into U.S. government bonds. Starting in 2000, borrowing costs fell to unusually low levels; inflation was tame, and the Federal Reserve adopted a highly accommodative monetary policy. This environment increased the demand for credit.

Using financial engineering, institutions offered loans they did not keep on their balance sheets. Securitization enabled them to pool debt, such as mortgages, credit card balances and car loans, and to sell it to investors in the form of complex structured products. The dissociation between the originator of the financial product and the ultimate bearer of the risk reduced the market's transparency; investors therefore counted on rating agencies to establish the appropriate return for such securities. In this way, lenders transferred credit risk to third parties attracted by superior returns. This phenomenon increased the supply of credit.

In short, financial innovation and abundant liquidity, coupled with low interest rates, weak volatility and an incentive to risk taking, encouraged a consumer-spending and -debt binge, driving up financial leverage and demand for assets. The prices of several asset classes rose to unsustainable levels. A case in point is the residential real estate sector in United States, where the proliferation of subprime loans caused house prices to soar. For these financial products to be viable, property values had to keep rising. The downturn in residential real estate, which began in 2006, pushed up default and foreclosure rates. As mortgage-backed securities lost value, financial institutions took substantial write-downs, and the risk of debt securities was swiftly repriced. Investors lost confidence in the credit markets, and structured products became illiquid.

MARKET CONTEXT 2008

The subprime meltdown triggered the crisis. But the U.S. residential mortgage market was only one example of over-reliance on credit in all its forms. This phenomenon was characterized by:

/ Lax underwriting standards;

/ Complex, opaque instruments that proved to be fragile in a time of stress;

/ Failure by investors and rating agencies to analyze and to monitor risk; and

/ Abnormally low risk premiums.

When the credit bubble burst, the financial and economic impact jolted the entire world. Financial institutions saw their capital plummet. The tally for losses and writedowns caused by problems on the credit markets was already approaching US$1 trillion globally at the end of 2008. Bank balance sheets were burdened with complex securities and illiquid assets of uncertain value. Rising credit risk combined with strong risk aversion caused credit spreads to widen dramatically (figure 12). To get their balance sheets back in order, financial institutions tightened credit. Since the banks could not be sure about the stability of other institutions, the interbank market came to a standstill.

THE CRISIS INTENSIFIES IN THE FALL OF 2008

The deteriorating balance sheets of the large banks increased systemic risk. In the United States, the monetary and political authorities orchestrated many operations to reduce the risk that the financial system would collapse. The Federal Reserve took a barrage of unusual measures to inject liquidity into financial institutions. In March, it recapitalized the investment bank Bear Stearns, which was on the verge of failure before it was taken over by J.P. Morgan. In September, the government effectively nationalized Fannie Mae, Freddie Mac and the insurer American International Group. But it stayed on the sidelines when the investment bank Lehman Brothers went bankrupt on September 15.

The markets' reaction to this decision was devastating: selling of assets accelerated, especially by overleveraged investors, most asset classes went into freefall, market volatility spiked and interest rates on government securities fell to historic lows. Overnight, on many financial markets regarded as highly liquid, the normal mechanisms broke down. It became exceedingly difficult and costly to carry out transactions. On the foreign exchange market, for instance, transactions dried up for currencies other than the U.S. dollar, the euro and the yen.

The currency market also saw unprecedented volatility. The rush into U.S. dollars caused the other currencies to depreciate suddenly, with the exception of the yen, which rose quickly when investors trying to reduce risk purchased large quantities of yen to close out positions financed by borrowing on the Japanese market. In one month, from September 26 to October 27, the Canadian dollar fell 20% against the greenback, recording a loss three times greater than its previous largest monthly variation of -5.7% in November 1976.

Aggressive action not seen since the 1930s managed to stem the carnage in the last two months of the year. Central banks slashed their key rates and poured vast amounts of money into the banking system. In an unprecedented co-ordinated effort, the central banks in the United States, the euro zone, the United Kingdom, Canada, Sweden and Switzerland lowered their key rates on October 8; on the same day, the People's Bank of China followed suit.

In the United States, the Federal Reserve began lending to banks by purchasing their commercial paper and intervening directly in the credit markets. Governments went to great lengths to support their banking systems: they purchased assets, guaranteed loans, increased deposit insurance, guaranteed bank debt, recapitalized banks and even went so far as to nationalize banks.

THE WORLD TIPS INTO A DEEP RECESSION

All these measures failed to prevent the financial crisis from undermining global growth, which was relatively strong until the second half of the year, mainly because of the vitality of emerging markets. The price of oil climbed to US$147 a barrel in mid-July. In response to the inflationary spike caused by soaring commodity prices, central banks took a break for several months from the monetary easing they had begun with the onset of the financial crisis.

The already slowing economies of the industrialized countries succumbed in the fall when the financial crisis intensified. The contraction of bank credit in all countries curtailed consumer spending and business investment. Interbank lending dried up, disrupting international business transactions and contributing to a steep drop in exports in the fourth quarter. The financial crisis tipped the global economy into a severe recession, which in turn exacerbated the crisis, since the rapid deterioration of economic conditions rendered the balance sheets of financial institutions even more fragile. The governments of many countries announced vigorous initiatives to stimulate their economies and financial sectors; even so, the global economy will be prone to substantial risk for several years.

UNITED STATES

Economic activity was sustained in the first half, as a result of more than US$100 billion of fiscal stimulus provided by the U.S. government at the start of the year, as well as rising exports driven by worldwide growth and the weak greenback. In July, inflation clocked in at 5.6%, its highest level since 1991, sparking debate at the Federal Reserve over the need to increase the key rate to avoid a price spiral. The collapse of residential real estate, however, ultimately decimated the U.S. financial sector. The economic and financial conditions, which had been fragile since the start of the year, deteriorated swiftly.

The disappearance of three million jobs in 2008, plummeting equity markets and falling house prices caused household net worth to drop by 20%, prompting consumers to pull back on their spending in favour of a savings cushion. Rather than fears of inflation, concerns about deflation began to haunt the financial markets. In this context, the Federal Reserve cut its key rate to near zero, and the National Bureau of Economic Research announced that the recession had begun in December 2007.

CANADA

Despite strong domestic demand, Canada's growth was lacklustre at the start of the year, mainly because of the country's beleaguered auto sector and slumping exports. Until the fall, job growth was vigorous, however, and the activity rate climbed to a record 68%. Growth of domestic demand finally began to taper off in the second half of the year as the global economy slowed, and Canada entered a recession in the fourth quarter. With the decline in terms of trade, real income growth and confidence, households and businesses alike became cautious about their spending. The strong demand that had driven residential construction since 2002 began to falter, although not to the same extent as in the United States.

Even so, certain factors eased the blows taken by the Canadian economy. The record decline of the loonie against the greenback partially offset the impact of slowing worldwide demand and lower commodity prices (figure 13). Moreover, the money market responded favourably to the Bank of Canada's vigorous efforts to provide liquidity to the financial system. Credit conditions deteriorated during the year, but were better than in the other G7 countries; as a result, the Bank of Canada's monetary policy was more effective than that of the other central banks. The overnight financing rate decreased by 275 b.p. in 2008 and ended the year at 1.5%.

EUROPE

The euro zone's economic growth was sustained in the first half, and the inflation rate reached 4.1% at mid-year, significantly exceeding the 2% target set by the European Central Bank (ECB). In response, the ECB raised its key rate by 25 b.p. in July, believing that the risk of inflation outweighed the risk of a downturn. But many European financial institutions required public assistance in the second half of the year – proof that the financial crisis had also taken hold in Europe. A significant deterioration of the labour market, a sudden drop in the rate of inflation and the onset of a recession in the euro zone caused the ECB to reverse course in the last quarter, when it dropped its key rate by 175 b.p., taking it down to 2.5%.

The United Kingdom also slid into a recession during the year, under the impact of a substantial pullback by house prices, falling consumer spending and a wobbly banking system. As inflationary risks abated, the Bank of England slashed its key rate by 350 b.p. to 2%, its lowest level since 1951. The governments of several European countries, including Germany and the United Kingdom, proposed economic stimulus plans.

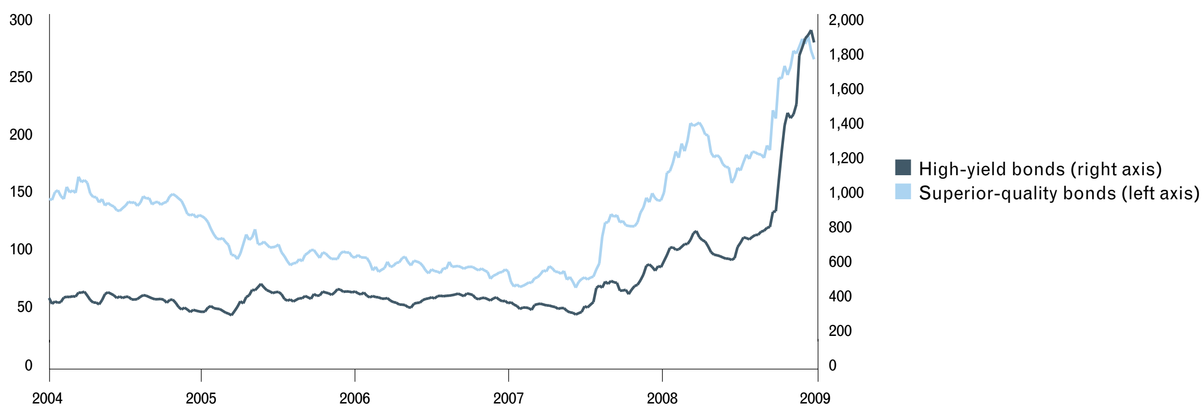
ASIA

Japan's exports were hammered by the global recession and the strong yen, which helped push the country into a deep recession. In a mainly symbolic move, the Bank of Japan lowered its key rate for the first time in seven years, taking it from 0.5% to 0.1%. The government provided a stimulus plan worth more than US$50 billion, but failed to prevent economic activity from collapsing in the fourth quarter, with the manufacturing sector hit hardest.

The People's Bank of China lowered interest rates by 189 b.p. during the year and also reduced the rate of mandatory bank reserves. The Chinese government also announced a US$580-billion stimulus plan for 2009 and 2010. These forceful moves show just how concerned the Chinese authorities are about their rapidly contracting economy. For the first time in five years, growth fell below 10%. Even though China had a record trade surplus in 2008, toward year-end its exports posted their first monthly decline in almost seven years as a result of the recession in the G7 countries. China ended the year with a 2.4% rate of inflation, substantially below the 8.7% recorded in the first quarter.

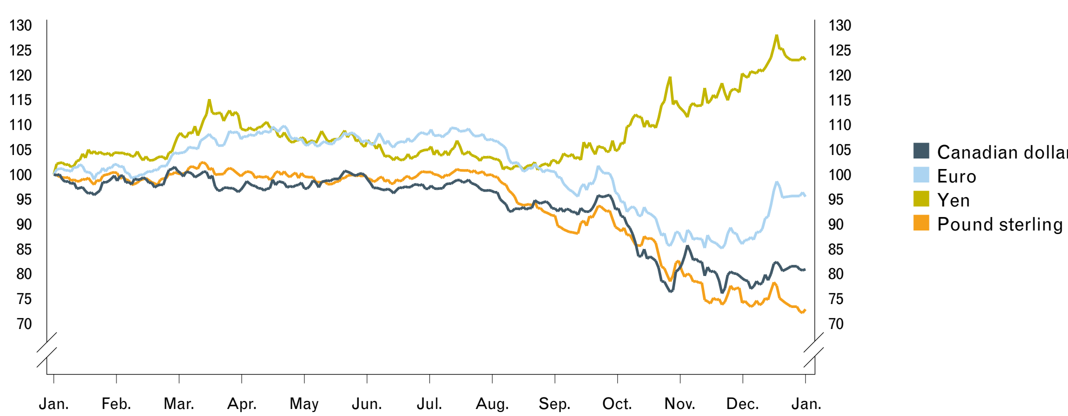
MARKET CONTEXT 2008

FIGURE 12
RISK PREMIUM
(U.S., b.p.)



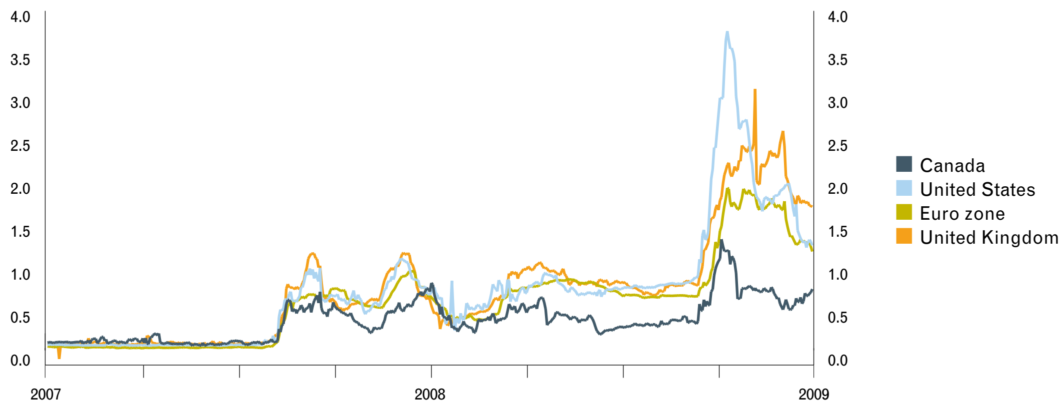
Source: Bloomberg

FIGURE 13
VALUE OF THE CANADIAN DOLLAR, THE EURO, THE YEN AND THE POUND STERLING AGAINST THE U.S. DOLLAR
(January 1, 2008 = 100)



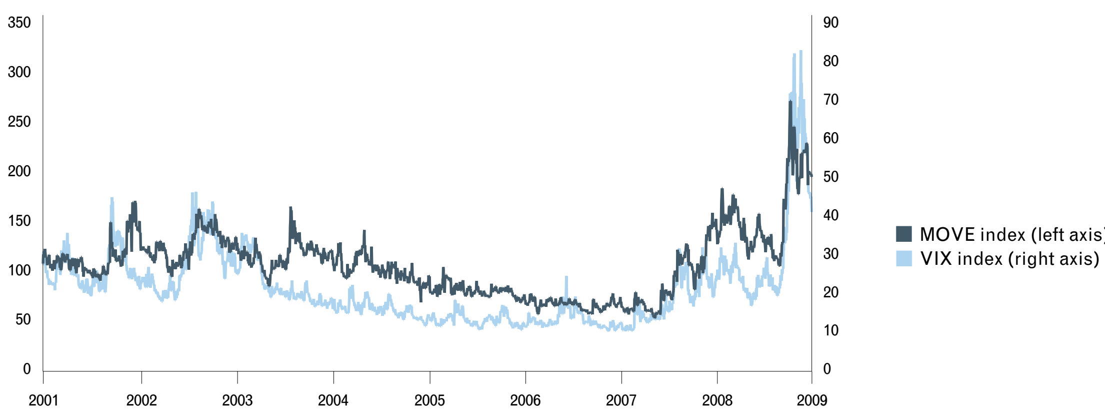
Source: Bank of Canada

FIGURE 14
SPREAD BETWEEN THREE-MONTH INTERBANK RATES AND THREE-MONTH OVERNIGHT INDEX SWAPS
(in percentage)



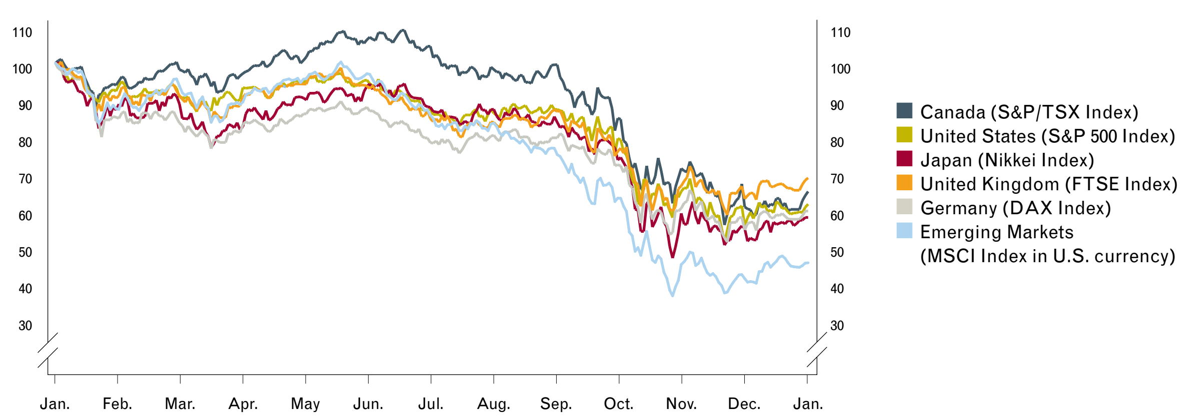
Source: Bloomberg

FIGURE 15
U.S. STOCK MARKET (VIX) AND BOND MARKET (MOVE) VOLATILITY INDEXES



Source: Bloomberg

FIGURE 16
EQUITY MARKETS IN 2008
(January 1, 2008 = 100)



Source: Datastream

MARKET CONTEXT 2008

BOND MARKETS

As the financial crisis intensified in the fall, the bond markets were roiled by:

/ An explosion of volatility;

/ Unprecedented widening of credit spreads;

/ Steeper yield curves;

/ The fallout from deleveraging; and

/ The development of deflationary expectations.

Tensions on the money markets increased in 2008. As the financial crisis deepened, interbank credit spreads exploded to more than 350 b.p. in the United States and more than 125 b.p. in Canada (figure 14). Liquidity is a precious commodity for banks, and they began to hoard capital rather than lend to one another. This situation brought interbank lending to a standstill and aggravated the contraction of international commercial credit. The many lending facilities put in place by the central banks finally succeeded in easing these tensions somewhat.

Amid extreme market volatility and rising risk aversion, investors flocked to treasury bills several times (figure 15). The return on three-month T-bills fell to 0.50% in mid-March, just before Bear Stearns' rescue, and it was almost zero when Lehman Brothers went bankrupt. In the last weeks of 2008, on expectations of a key rate approaching zero and strong demand for government securities, the rate of return fell to an extremely low level. In an unprecedented development, it even became negative for a brief period.

In the fall, investors turned to the safe haven of government bonds in anticipation of deflationary pressures, a deepening of the recession and quick monetary easing. Federal Reserve Chairman Ben Bernanke floated the idea of purchasing long bonds to keep long-term rates very low and to reduce the risk of deflation. Bond rates promptly fell to new lows, and bond portfolios therefore made strong gains. The Federal Reserve's vigorous monetary policy and the appeal of U.S. government securities in a time of crisis enabled them to post better returns than their Canadian counterparts. The yield curve steepened in the United States and Canada.

Lastly, as the crisis deepened, credit spreads on corporate bonds rose to record levels. In the case of top-quality debt, such spreads had not been seen since 1932. Credit spreads continue to be very high in relation to the default rate.

STOCK MARKETS

The stock markets fell at the start of the year as the banks struggled (figure 16). The S&P 500 Index was down about 20% from its October 2007 peak. The rescue of Bear Stearns reassured investors for several months about the monetary authorities' will to backstop the financial system. As the indicators improved in the second half in United States, mainly because of the tax stimulus plan and strong global growth, some investors were encouraged to forge ahead in the belief that the worst was over.

Continued economic growth in emerging markets and rising commodity prices seemed to lend credence to the decoupling theory that rapid growth in China and India was based on independent structural strength that largely immunized them from a downturn in the United States. In this context, the energy sector, which partially offset the weak financial sector, continued to generate strong enthusiasm in the first half. The Canadian stock market was in positive territory at mid-year on the appeal of energy securities.

A swift reversal occurred in mid-July. Moreover, continuing credit deterioration, especially in mortgages, forced financial institutions to record new writedowns. The unforeseeable repercussions of the Lehman Brothers bankruptcy in September caused investors to fear the worst. As volatility and risk aversion soared, the equity markets plunged. Massive selling by investors added to the downward pressure. As a result of forceful government action, the equity markets recovered at year-end but remained extremely volatile.

In short, the stock markets had one of their worst years ever in 2008, driving returns in the United States to the lowest level since 1937. All the main indexes shed more than 30%, and the MSCI Emerging Markets Index plunged almost 55%. None of the main sectors offered a safe haven from falling values, although consumer staples and health care held up better than the others. For the second year in a row, financials had the worst return.

HEDGE FUNDS

As the value of risky securities fell, many hedge fund managers engaged in forced liquidation to reduce their leverage. Nevertheless, in the first seven months of the year, this investment sector generally succeeded in fulfilling its role of preserving capital in a down market. Still, the explosion of systemic risk and the disruption of normally liquid markets put many strategies to the test.

Arbitrage strategies, including those based on anomalies in the relative values of fixed-income securities, incurred losses as a result of the swift breakdown of certain traditional correlations between securities. Other strategies performed better in falling markets, such as global macro strategies that properly identified the year's trends. The hedge fund sector will inevitably undergo profound change; many funds could disappear, while others will have to adapt to more stringent regulation.

COMMODITIES

Managers of commodity portfolios were confronted with a highly volatile environment in 2008. Many investors were convinced that growth in emerging markets would sustain high prices despite the slowdown in the industrialized economies, so they used commodities to diversify their portfolio risk. Combined with these fundamental factors, exuberance and speculation fuelled a stratospheric increase in commodity prices, followed by a vicious correction. The price of crude oil plummeted from $147 a barrel to $44 in less than six months.

In the financial sector, managers using directional strategies did not fare well all year, unless they correctly anticipated the timing of the market's reversal, while relative-value strategies recorded losses in the second half, with the strong increase in the correlation between most of asset classes. The diversification strategy based on commodities did not bear fruit in the second half of 2008, but this asset class will remain attractive over the long term to investors seeking a hedge against a possible resumption of inflation.

PRIVATE EQUITY

The deal flow fell sharply in all segments of the private equity market in 2008. Three phenomena caused these results in relation to the previous year:

/ The accentuation of the liquidity and credit crisis;

/ The onset of a global recession; and

/ The steep decline on the equity markets, which caused the fair value of investments to fall sharply because of new accounting rules.

The liquidity and credit crisis hit hard once again during the year. Market disruption deprived managers of abundant, affordable leverage. The unprecedented scarcity of credit, the collapse of U.S. investment banks and the debacle on the equity markets curtailed leveraged buyouts. This sudden reversal slowed the rate at which private investment firms deployed their capital. They also had to contend with the impacts of the global recession, which jeopardized deals concluded at the top of the market and severely depressed portfolio-company valuations.

Institutional investors' interest in infrastructure, which combines a stable income flow with financial obligations spread over a long period, kept the value of such investments fairly high in the first half. Transactions came to an end, however, as liquidity dried up and borrowing costs became prohibitive.

FIGURE 17

PRIVATE EQUITY CYCLE

EXPANSION Buyer's market	SLOWDOWN Seller's market	CONTRACTION Seller's market	RECOVERY Buyer's market

Expansion: buyer's market	**Slowdown: seller's market**	**Contraction: seller's market**	**Recovery: buyer's market**
/ Priority on companies with constant cash flow / Priority on defensive instruments / Limited, opportunistic acquisitions	/ Selective approach to acquisitions/sales / Active management of holdings / Reinvestment in promising holdings	/ Cautious resumption of acquisitions / Priority on equity investments / Stakes in funds on secondary market	/ Massive equity acquisitions
■ Infrastructure, mezzanine debt ■ Leveraged buyouts, restructuring, development capital	■ Restructuring, mezzanine debt ■ Infrastructure ■ Development capital, leveraged buyouts	■ Restructuring ■ Mezzanine debt, development capital ■ Infrastructure, leveraged buyouts	■ Leveraged buyouts, accumulation, development capital, infrastructure ■ Mezzanine debt, restructuring

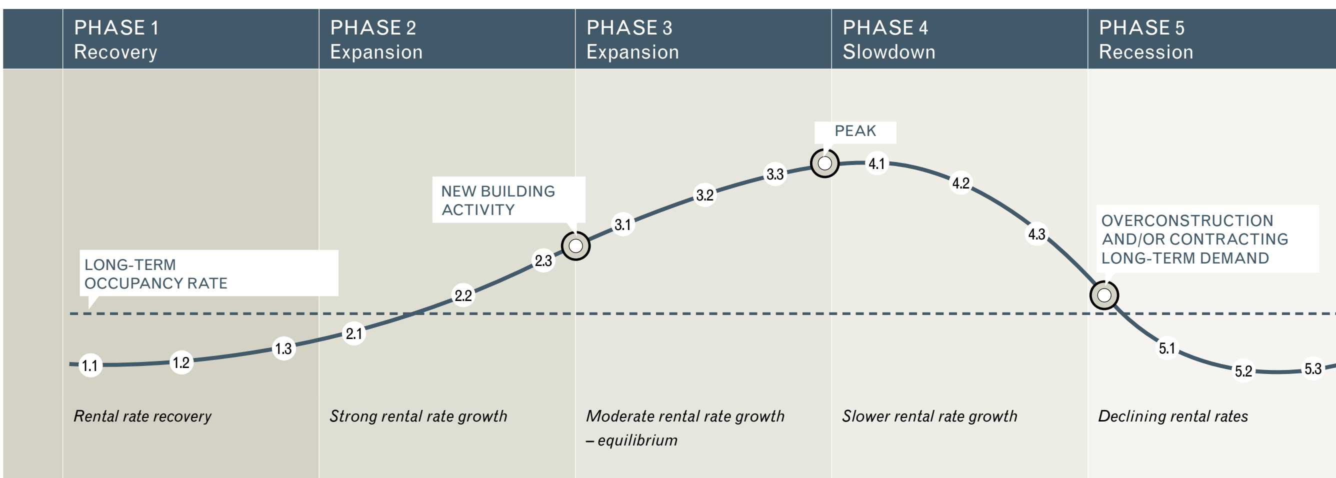
MARKET CONTEXT 2008

The turbulence on the credit markets had less severe repercussions in the venture capital sector, where leverage is less prevalent. Still, the plummeting equity markets considerably reduced exit opportunities. The steep downturn in the number of initial public offerings and purchases by strategic investors has extended holding periods and put downward pressure on returns.

The deteriorating business environment has increased the risk aversion of providers of capital and restricted sources of traditional financing, making private equity funding for development capital more competitive. This segment of the market could prove promising a little later in the private equity cycle. It offered very few opportunities in 2008 because of the gloomy economic outlook. The global recession will also create opportunities in distressed loans and corporate restructuring, since it will drive earnings down and default rates up (figure 17).

Lastly, the stock market selloff had a direct impact on the results of private equity funds in 2008. Managers must comply with accounting rules specifying that private equity valuations reflect the market value of comparable publicly traded companies.

FIGURE 18
POSITIONING OF CERTAIN REGIONS WITHIN THE GLOBAL COMMERCIAL REAL ESTATE CYCLE AT THE END OF 2008



	PHASE 1 Recovery	PHASE 2 Expansion	PHASE 3 Expansion	PHASE 4 Slowdown	PHASE 5 Recession
EMERGING MARKETS		**2.2** / Retail (India) **2.3** / Industrial (Brazil)	**3.1** / Retail (Mexico) / Multiresidential (Brazil, India) **3.2** / Office (Mexico, Brazil) / Retail (Brazil) / Hotel (India) **3.3** / Hotel (China) / Industrial (Mexico) / Multiresidential (China)	**4.1** / Office (India) / Retail (China[1], Russia) / Industrial (China) **4.2** / Office (China[1], Russia)	
DEVELOPED MARKETS			**3.1** / Office (Québec) **3.3** / Multiresidential (Canada) / Office (Western Canada, Ontario) / Retail (Germany, Japan)	**4.1** / Office (Central Europe, Japan) / Retail (Canada, Central Europe, France) / Hotel (Canada, euro zone, United Kingdom) **4.2** / Hotel (United States) / Industrial (Canada) / Multiresidential (United States) **4.3** / Office (United States, euro zone) / Industrial (United States warehouse)	**5.1** / Office (United Kingdom) / Retail (United States, United Kingdom, Spain)

1 Mainly the Shanghai market.

REAL ESTATE SECTOR

The credit crisis that began in 2007 continued throughout 2008 in the commercial real estate sector. As it intensified in the fall, investors pulled back. The markets saw a significant decrease in transactions and less use of leverage. These two factors helped push down the market value of properties. The deepening recession fuelled expectations that commercial real estate fundamentals would deteriorate and therefore pushed market values down. As a result, capitalization rates were generally up for the first time in several years.

In certain markets, particularly Canada and the market for quality buildings, the fundamentals generally held up well, and portfolios continued to produce solid current income. More broadly, rental and occupancy rates for office buildings and shopping centres began to weaken in 2008 as consumer spending and employment declined. Canada was largely unscathed by this trend in 2008. Its real estate sector remained relatively strong.

The situation was quite different in markets affected by a dropoff in consumer spending or the downturn in the financial sector, such as the United States, the United Kingdom and Spain. Real estate markets in emerging countries were also shaken by the crisis, but have less exposure to liquidity problems and seem poised for a more rapid recovery. Their long-term outlook is attractive as a result of their growth potential (figure 18).

The financial crisis hammered publicly traded real estate securities, investment funds and mortgage-backed securities. The current income from these portfolios dipped slightly in 2008, and default rates increased only a little. Even so, the value of these investments fell sharply as transaction volume collapsed and credit spreads widened tremendously, as a direct result of the general repricing of risk.

QUÉBEC'S MARKET CONTEXT

Québec's economic growth exceeded Ontario's in 2008 thanks to a solid performance by the aeronautics sector relative to the automotive sector. Moreover, with an economy that is more diversified than that of the other Canadian provinces, Québec has been able to absorb economic shocks better. Still, Québec has also been hit by the worldwide financial crisis and the recession in the United States, which is by far its main export market.

After a rather positive start, the province's economy entered a recession in the last quarter. It finished the year with a 7.3% jobless rate, up from 6.8% at the start of the year. The Québec government's infrastructure plan continues to bolster the construction industry, however, and is cushioning the slowdown in the residential real estate sector, where housing starts have slipped somewhat. Contrary to the decreases observed in Western Canada, the price of new houses in Québec increased by an average of 5% in relation to 2007.

The IQ120 stock market index, consisting of 120 of the largest companies with operations in Québec, was down 37% in 2008, a decline that slightly exceeded the loss on the TSX Index. It should be noted that financial institutions, which are affected by the global crisis, represent almost a third of the index. Québec companies had to cope with tighter and more costly credit, which had a negative impact on their earnings.

The crisis also had significant repercussions on the provincial bond markets, including Québec's. The rate spread between 10-year Québec government bonds and their Government of Canada counterparts averaged almost 100 b.p. in 2008, more than double the spreads of the past five years. Moreover, the spread exceeded 190 b.p. at year-end.

In response to the global financial crisis and the depressed stock markets, privately owned foreign venture capital funds proceeded cautiously. Québec's venture capital industry reflected the North American trend, with a sharp decrease in the amounts invested in 2008.

As a result of strong market fundamentals in Montréal and Québec City, the province's commercial real estate sector was surprisingly solid in 2008 in the case of office buildings and shopping centres. Strong demand for space and buoyant retail sales kept vacancy rates below the long-term average. The market conditions seemed on the verge of softening at year-end, however, as signs of weakness appeared, and investment fell sharply.

ANALYSIS OF OVERALL PERFORMANCE

The Caisse obtained an overall return of -25.0% in 2008. In comparison, the return on the benchmark portfolio was -18.5%, and the median return for large Canadian pension funds was -18.4%. The net investment results are -$39.8 billion.

HIGHLIGHTS

/ The weighted average return on depositors' funds for the year ended December 31, 2008, was -25.0%.

/ The return generated by the managers underperformed the benchmark indexes by 658 b.p. (6.58%). This subtracted value includes a $4.0-billion additional expense for ABCP.

/ The Caisse ranked in the fourth quartile of large Canadian pension funds, whose median return was -18.4%. The -6.6% difference is due mainly to the impact of currency hedging and ABCP investments.

/ The net investment results are -$39.8 billion, of which 56.3% are unrealized decreases in value. Taking into account net deposits totalling $4.6 billion, depositors' net assets decreased from $155.4 billion to $120.1 billion in 2008.

/ In response to the financial crisis, the Caisse changed its asset allocation significantly, increasing the weighting of fixed income from 29.5% to 44.2% and decreasing equities from 36.3% to 22.4%.

/ The absolute risk of the overall portfolio increased considerably because of the high level of market volatility. The portfolio's active risk also increased substantially, partially because of market volatility but also because of asset allocation changes and ABCP.

CAISSE'S OVERALL RETURN AND DEPOSITORS' INDIVIDUAL RETURNS

OVERALL RETURN

The -25.0% overall return corresponds to the weighted average return on depositors' funds invested in the Caisse's 18 specialized portfolios, to which are added treasury operations, the additional expense for ABCP and certain costs.

The global financial crisis that occurred in the fall caused almost all asset classes to drop sharply. For 2008 as a whole, the debacle on the equity markets alone accounts for two-thirds of the -18.5% return on the benchmark portfolio.

Moreover, active management of the overall portfolio and the specialized portfolios, including the additional expense for ABCP, subtracted 658 b.p. (6.58%).

For the three- and five-year periods ended December 31, 2008, the Caisse's returns are -3.2% and 3.1%, respectively.

DEPOSITORS' INDIVIDUAL RETURNS

The depositors can invest in 18 specialized portfolios offered by the Caisse. They determine the proportion of their funds that they want to invest in each portfolio as a function of their target returns and in this way establish their benchmark portfolios.

Certain depositors seek stable returns and preservation of capital. They therefore concentrate their investments in fixed income. The main depositors, however, have a long-term investment horizon and target returns that exceed fixed-income returns. They therefore diversify their portfolios by also investing in publicly traded equities and other asset classes with the potential for high returns, such as private equity, real estate and hedge funds.

At year-end, because of the differences in the composition of the depositors' portfolios, each obtains a different return. The individual returns of the seven main depositors, which represent more than 96% of net assets, ranged from -26.9% to -17.0% in 2008.

RETURN IN RELATION TO THE BENCHMARK INDEXES

The managers' return underperformed the Caisse's benchmark index by 658 b.p. (6.58%) as at December 31, 2008. The value subtracted for the three- and five-year periods ended December 31, 2008, is 238 b.p. (2.38%) and 100 b.p. (1.00%), respectively.

The unfavourable difference between the -25.0% return and the -18.5% return on the benchmark portfolio is due to three main factors. The first is the additional expense of $4.0 billion for ABCP, which is the equivalent of -2.5%.

The second is the difference between the return on the Real Estate portfolio and its benchmark index. As a result of the size of the portfolio, this difference represents -$3.7 billion, or -2.1%. Over five years however, the portfolio has a return of 17.0% and ranks in the first quartile of large Canadian pension funds.

The third factor relates to the Asset Allocation portfolio and the rebalancing decisions, whose contribution totals -$2.0 billion, or -1.1%. A portion of the portfolio's operations was exposed to various risk factors (credit, liquidity and inflation) whose values all fell simultaneously during the financial crisis in the fourth quarter. The portfolio's operations have been suspended and are under review.

Only a few portfolios outperformed their benchmark indexes in 2008, notably Private Equity (8.72%) and Canadian Equity (0.65%).

The main portfolios that underperformed their benchmark indexes are Real Estate (-18.51%), Investments and Infrastructures (-8.07%), unhedged and hedged U.S. Equity (-6.78% and -6.20%) and Real Estate Debt (-4.60%).

Table 19 shows net assets under management, returns and value added for each of the Caisse's asset classes. Lastly, table 20 presents the differences between the Caisse's returns and the indexes for the 18 specialized portfolios.

TABLE 19

NET ASSETS, RETURNS AND VALUE ADDED

(for periods ended December 31)

							3 years			5 years
				2008			2006-2008			2004-2008
Asset class	**Net assets**		**Return**	**Value added[1]**		Return	Value added[1]		Return	Value added[1]
	$B	**%**	**$M**	**(b.p.)**	%	$M	(b.p.)	%	$M	(b.p.)
Fixed Income and Currencies	**52.2**	**4.4**	**2,231**	**(145)**	4.1	5,563	(41)	5.2	10,434	(21)
Equity Markets	**26.4**	**(36.7)**	**(21,257)**	**(89)**	(6.9)	(9,313)	24	1.3	1,899	(2)
Hedge Funds	**5.3**	**(21.3)**	**(1,487)**	**(42)**	(4.3)	(788)	32	1.0	(290)	264
Private Equity	**14.0**	**(36.0)**	**(7,968)**	**281**	(3.9)	(2,941)	535	5.5	572	648
Real Estate	**25.4**	**(16.1)**	**(4,910)**	**(1,352)**	4.1	1,874	(576)	11.9	7,628	(117)
Asset Allocation and other[2]	**0.3**	**–**	**(2,013)**	**–**	–	(1,671)	–	–	(1,784)	–
Expense for third-party and bank-sponsored ABCP	**(5.8)**	**–**	**(3,969)**	**–**	–	(5,866)	–	–	(5,866)	–
	120.1[3]	**(25.0)**	**(39,816)[3]**	**(658)**	(3.2)	(14,221)	(238)	3.1	11,754	(100)

1 In relation to benchmark indexes.

2 The results of these operations include those of Rebalancing Decisions and are presented net of expenses.

3 The net assets and the return in dollars are those presented in the combined financial statements audited by the Auditor General of Québec. For more information, see note 11 to table 1 of the section "Financial statistics and review" in Annual Report 2008 – Additional Information.

ANALYSIS OF OVERALL PERFORMANCE

TABLE 20

RETURNS ON THE SPECIALIZED PORTFOLIOS IN RELATION TO MARKET INDEXES OR RECOGNIZED INDEXES

(for periods ended December 31, 2008 – percentage unless otherwise indicated)

				1 year			5 years
Specialized portfolio	2008 Index	Return %	Index %	Spread b.p.	Return %	Index %	Spread b.p.
Fixed income and currencies							
Short Term Investments	*DEX 91-Day Canadian T-Bill*	3.7	3.3	35	3.6	3.3	29
Real Return Bonds	*DEX Real Return Bond*	(2.2)	0.4	(260)	5.5	6.1	(53)
Bonds	*DEX Universe Bond*	4.8	6.4	(159)	5.3	5.5	(21)
Long Term Bonds	*DEX Long Term Government Bond*	4.6	6.2	(151)	–	–	–
		4.4	**5.9**	**(145)**	**5.2**	**5.4**	**(21)**
Equity markets							
Canadian Equity	*S&P/TSX capped*	(32.4)	(33.0)	65	5.3	4.2	116
U.S. Equity (hedged)	*S&P 500 hedged*	(45.2)	(39.0)	(620)	(5.9)	(3.3)	(254)
U.S. Equity (unhedged)	*S&P 500 unhedged*	(28.0)	(21.2)	(678)	(5.3)	(3.1)	(226)
Foreign Equity (hedged)	*MSCI – EAFE hedged*	(42.6)	(41.8)	(79)	0.3	0.7	(37)
Foreign Equity (unhedged)	*MSCI – EAFE unhedged*	(29.8)	(29.2)	(61)	0.5	0.7	(27)
Emerging Markets Equity	*MSCI – EM unhedged*	(45.0)	(41.6)	(337)	5.0	6.7	(168)
Québec International	*Québec International*	(41.2)	(40.4)	(82)	0.0	0.2	(19)
		(36.7)	**(35.8)**	**(89)**	**1.3**	**1.3**	**(2)**
Hedge funds							
Hedge Funds	*CS/Tremont Hedge Fund Index modified*	(20.9)	(20.8)	(7)	1.1	(1.2)	229
Commodities	*Commodity Financial Instruments*	(25.4)	(23.2)	(216)	–	–	–
		(21.3)	**(20.9)**	**(42)**	**1.0**	**(1.6)**	**264**
Private equity							
Investments and Infrastructures	*Investments and Infrastructures*	(44.7)	(36.6)	(807)	(2.1)	1.4	(350)
Private Equity	*Private Equity*	(31.4)	(40.1)	872	10.6	(3.0)	1,354
		(36.0)	**(38.9)**	**281**	**5.5**	**(1.0)**	**648**
Real estate							
Real Estate Debt	*Real Estate Debt*	(7.6)	(3.0)	(460)	4.3	3.8	49
Real Estate	*Aon – Real Estate*	(21.9)	(3.4)	(1,851)	17.0	19.0	(195)
		(16.1)	**(2.6)**	**(1,352)**	**11.9**	**13.0**	**(117)**
Asset Allocation and other[1]		$(2,013) M	–	–	$(1,784) M	–	–
Weighted average return on depositors' funds before third-party and bank-sponsored ABCP[2]		(22.3)	(18.5)	(380)	4.1	4.1	1
Third-party and bank-sponsored ABCP[3]		(2.5)	–	(255)	(0.9)	–	(94)
Weighted average return on depositors' funds[2]		**(25.0)**	**(18.5)**	**(658)**	**3.1**	**4.1**	**(100)**

1 The return is that of the activity, net of expenses, including Rebalancing Decisions, and is given in dollars. The results are combined for the five-year period.

2 Exclusion of third-party and bank-sponsored ABCP increases the capital base and lessens the impact of the negative results on the return.

3 Impact of third-party and bank-sponsored ABCP on the weighted average return on depositors' funds.

COMPARISON OF THE OVERALL RETURN WITH CANADIAN PEERS

The Caisse compares its financial results with those of its peers, even though there are significant differences between the composition of its benchmark portfolio and theirs. To that end, it uses studies that rank a sample of institutional fund managers on the basis of the returns obtained by each, such as the study by RBC Dexia Investor Services on Canadian pension funds of more than $1 billion.

According to this study, after four years of first-quartile returns, the Caisse ranked in the fourth quartile in 2008. Its -25.0% return is far lower than the -18.4% median return on large pension funds. This -6.6% difference is due mainly to two factors that set the Caisse apart from its peers: foreign exchange hedging and the additional expense for ABCP.

The average annual return over three years is -3.2% and ranks in the fourth quartile. Over five years, it is 3.1% and is in the third quartile. Table 21 shows the Caisse's overall return and ranking in relation to large Canadian pension funds.

TABLE 21

OVERALL RETURN

(as at December 31, 2008)

Period	Annual return	Quartile ranking in relation to large Canadian pension funds
1 year	(25.0) %	Fourth
3 years	(3.2) %	Fourth
5 years	3.1 %	Third

Source: RBC Dexia Investor Services – Plans Over $1 Billion Universe.

IMPACT OF CURRENCY HEDGING

Currency hedging is not a speculative activity but a means of mitigating risk that has been in place for about 15 years with the depositors' consent. It enables the managers to concentrate on their investment duties without having to be concerned about the impact of currency fluctuations on the value of their investments. Private equity, real estate and hedge funds are 100% hedged, while U.S. equities and foreign equities are partially hedged.

After generating favourable results in 2007, when the Canadian dollar was rising, currency hedging was especially costly in 2008 because of the Canadian dollar's sharp decline against the major currencies. It lost 20% against the U.S. dollar, 16% against the euro and 35% against the yen.

Its decline caused the value of the Caisse's foreign investments to rise by $11.3 billion. The foreign exchange hedging policy, designed to smooth out currency fluctuations, reduced this value by $8.9 billion. Ultimately, the weakness of the Canadian dollar therefore increased the value of the hedged investments by only $2.3 billion (see table 22).

The level of the Caisse's currency hedging costs is due to a proportion of foreign private equity and real estate investments that is far higher than that of its peers, as well as to its more extensive currency hedging policy. Such a policy should be considered over the long term, during which its impact on returns is neutral. In fact, its impact over 10 years is only slightly positive. For more information, see the section "Analysis of combined financial statements."

TABLE 22

COST OF FOREIGN EXCHANGE RISK HEDGING IN 2008

(in millions of dollars)

	Net increase in the value of investments denominated in foreign currencies (before hedging)	Cost of foreign exchange risk hedging	Breakdown of foreign exchange risk hedging cost	Net increase in the value of investments denominated in foreign currencies (after hedging)
Equity Markets	2,578	(804)	9.0%	1,774
Private Equity	3,490	(3,453)	38.6%	37
Real Estate	3,462	(3,551)	39.8%	(89)
Fixed Income and Currencies, Hedge Funds and Asset Allocation	1,755	(1,129)	12.6%	626
Total	**11,285**	**(8,937)**	**100.0%**	**2,348**

ANALYSIS OF OVERALL PERFORMANCE

IMPACT OF ABCP

In 2008, the Caisse recorded an additional expense of $4.0 billion for ABCP, which decreased its overall return by 2.5%. This additional amount includes an unrealized loss of $3.8 billion and a realized loss of $171 million, excluding back interest and interest received. (For more information, see note 4b of the combined financial statements.)

A cumulative provision of $5.6 billion was recorded for ABCP as at December 31, 2008. This provision represents 43.8% of the total cost of $12.8 billion. Given the low rate of actual loss in the ABCP structures at year-end 2008 and the levels from which losses may be recorded, the Caisse believes that a large portion of this cumulative provision will be reversed in the years to come.

The ABCP restructuring agreement was concluded on December 24, 2008, and closed in January 2009. The ABCP investments have become long-term notes that have an average maturity of seven years and generate interest income on a quarterly basis.

On January 21, 2009, the Caisse received $389 million of interest accumulated from August 15, 2007, to August 31, 2008.

CHANGES IN NET ASSETS

Depositors' net assets totalled $120.1 billion as at December 31, 2008, versus $155.4 billion a year earlier. This $35.3-billion decrease includes net investment results totalling -$39.8 billion and $4.6 billion of net deposits by the depositors.

The net investment results for 2008 include $29.2 billion of losses related to the composition of the benchmark portfolio, $6.2 billion of losses related to active management and an additional expense of $4.0 billion for ABCP. Operating expenses and external management fees subtracted another $0.4 billion.

Table 23 shows the changes in depositors' net assets from January 1, 2004, to December 31, 2008. It gives net investment results and net contributions by depositors.

Over the past five years, depositors' net assets have risen from $89.4 billion as at December 31, 2003, to $120.1 billion as at December 31, 2008. About 60% of this increase is due to net deposits ($18.9 billion), with the remainder attributable to net investment results ($11.9 billion).

NET INVESTMENT RESULTS AND FAIR VALUES

Unrealized losses in value amounted to $22.4 billion, or 56.3% of net investment results, in 2008. Net investment income, including interest, dividends and rent, totalled $5.8 billion. Realized losses on investments sold during the year came to $23.2 billion.

The substantial unrealized decreases in value are due to the swift, across-the-board decline in investment values during the financial crisis in the fall. Moreover, under the accounting rules in effect, investments that are not publicly traded decreased significantly in value, a decline that is more indicative of the prevailing market conditions than their intrinsic value and cash flow. For more details, see the inset on fair-value valuation at the end of this section.

TABLE 23

ANALYSIS OF CHANGES IN DEPOSITORS' NET ASSETS

(for the period 2004-2008 – in billions of dollars)

	2004	2005	2006	2007	2008	2004-2008
Net assets at beginning	89.4	102.4	122.2	143.5	**155.4**	**89.4**
Income generated by the composition of the overall benchmark portfolio (depositors' investment policies)	10.2	13.7	15.8	9.1	**(29.3)**	**19.4**
Value added by active management	0.8	1.7	2.3	1.0	**(6.2)**	**(0.3)**
Additional charge on third-party and bank-sponsored ABCP[1]	–	–	–	(1.9)	**(4.0)**[4]	**(5.9)**
Operating expenses[2]	(0.2)	(0.2)	(0.2)	(0.3)	**(0.3)**	**(1.2)**
External management fees[2]	–	–	(0.1)	(0.1)	**(0.1)**	**(0.3)**
Net investment results[3]	10.8	15.2	17.8	7.9	**(39.8)**	**11.9**
Depositors' net contributions	2.2	4.6	3.5	4.0	**4.6**	**18.9**
Net assets at end	**102.4**	**122.2**	**143.5**	**155.4**	**120.1**	**120.1**

1 To track its investments in third-party and bank-sponsored ABCP more effectively, the Caisse has decided to separate its reporting on this matter.

2 External management fees have been presented separately since January 1, 2007. The amounts for 2006 have been restated for comparison purposes.

3 Net investment results include income from depositors' demand deposits and term deposits.

4 For more information, consult note 4b of the combined financial statements.

ACTION IN RESPONSE TO THE FINANCIAL CRISIS

As a precautionary measure, the Caisse changed its asset allocation significantly in the fall of 2008 in response to the financial crisis.

As a result of these decisions, the composition of the overall portfolio diverged considerably from that of the benchmark portfolio as at December 31, 2008, and some of the specialized portfolios no longer respected their limits.

Table 24 shows these changes and the composition of the Caisse's benchmark portfolio at December 31, 2008, as well as the allocation of the overall portfolio at year-end 2007 and 2008.

COMPOSITION OF THE OVERALL PORTFOLIO

In response to the financial crisis and the plummeting Canadian dollar, the Caisse took unusual measures in the fall of 2008. The objective was to preserve depositors' capital and to maintain a prudent level of liquidity in a climate of uncertainty.

The Caisse changed its asset allocation significantly as a function of a possible intensification of the crisis – an outcome that did indeed occur. Exposure to the equity markets was reduced in favour of fixed income, so as to contain absolute risk and to maintain a prudent level of liquidity. To do so, the Caisse sold equities and other investments, closed out futures contracts and reduced its currency hedging.

TABLE 24

CHANGES IN THE COMPOSITION OF THE BENCHMARK PORTFOLIO AND THE OVERALL PORTFOLIO

(percentage of depositors' net assets)

	Benchmark portfolio as at December 31, 2008			Caisse's overall porfolio as at December 31, 2008	Caisse's overall porfolio as at December 31, 2007
	Lower limit %	Benchmark portfolio %	Upper limit %	%	%
Fixed income					
Short Term Investments	**0.1**	**1.1**	**9.1**	3.7	1.5
Real Return Bonds	**0.1**	**0.6**	**2.9**	0.5	0.6
Bonds	**21.2**	**26.9**	**36.2**	37.4	25.4
Long Term Bonds	**1.9**	**2.5**	**4.5**	2.6	2.0
Subtotal		**31.1**		**44.2**	**29.5**
Equity markets					
Canadian Equity	**6.9**	**12.2**	**17.8**	10.9	12.9
U.S. Equity	**0.2**	**3.4**	**11.3**	1.9	4.4
Foreign Equity	**1.0**	**5.5**	**12.8**	3.4	6.4
Emerging Markets Equity	**0.3**	**3.2**	**6.1**	2.6	3.2
Québec International	**6.3**	**10.2**	**15.0**	3.6	9.4
Subtotal		**34.5**		**22.4**	**36.3**
Other investments					
Investments and Infrastructures	**3.0**	**5.5**	**8.8**	3.6	4.1
Private Equity	**5.1**	**8.0**	**10.7**	8.3	7.3
Real Estate Debt	**2.5**	**6.5**	**10.0**	9.6	7.4
Real Estate	**6.0**	**9.8**	**14.3**	12.0	11.3
Hedge Funds	**0.4**	**3.0**	**5.2**	3.3	3.4
Commodities	**0.0**	**1.6**	**3.3**	1.1	1.6
Subtotal		**34.4**		**37.9**	**35.1**
Asset allocation and other	**0.0**	**0.0**	**1.0**	0.4	0.3
Third-party and bank-sponsored ABCP[1]				(4.9)	(1.2)
Total		**100.0**		**100.0**	**100.0**

1 To track third-party and bank-sponsored ABCP more effectively, the Caisse has separated its reporting on it from that on management of its specialized portfolios.

N.B.: The benchmark portfolio and its upper and lower limits are the result of the weighted average of the depositors' benchmark portfolios.

ANALYSIS OF OVERALL PERFORMANCE

The futures contracts and currency hedging placed pressure on the Caisse's liquid assets, but at no time in the fall did the Caisse run short of, or come close to running short of, liquid assets.

In fact, the Caisse manages its liquidity actively and carefully so that it can meet its obligations at all times, at the lowest possible cost. Liquidity comes from various sources, including investment income, depositors' net contributions, short-term securities, bond lending and the borrowing program, and are monitored on a daily basis. The Caisse's liquid assets of this kind totalled $21.5 billion, or 18% of depositors' net assets, as at December 31, 2008.

In short, the asset allocation changes increased the weighting of fixed income from 29.5% to 44.2% and that of equities from 36.3% to 22.4%. The upper and lower limits set for some specialized portfolios were exceeded in the case of several depositors, who were informed accordingly.

The overall portfolio will be rebalanced gradually in the months to come, as a function of the economic and financial context.

COMPOSITION OF THE BENCHMARK PORTFOLIO

The composition of the benchmark portfolio changed very little during the year. The portfolios of non-traditional assets in the other-investments category represented 34.4% of the benchmark portfolio at the end of 2008, up 0.7% from the year-earlier figure. The weighting of the equity portfolios increased 0.2%, while that of the fixed-income portfolios decreased 0.9%.

CHANGES IN THE MARKET RISK OF THE OVERALL PORTFOLIO

There is a strong link between overall return and risk, which is of two types:

/ Absolute risk is due to portfolio and investment volatility caused by market behaviour; and

/ Active risk is the possibility that the Caisse will obtain a return that differs from the return on its benchmark portfolio in managing its overall portfolio actively.

Figure 25 shows the changes in the components of the Caisse's risk.

For more details, see the discussion of integrated risk management in the section "Management framework."

ABSOLUTE RISK

During the year, the absolute risk of the overall portfolio and the absolute risk of the index of the Caisse's benchmark portfolio increased by 558 b.p. and 472 b.p., to 1,283 b.p. and 1,047 b.p., respectively. These increases are due essentially to greater volatility on the financial markets, particularly the equity, private equity, real estate and ABCP markets. Excluding ABCP, the absolute risk of the overall portfolio increased by 375 b.p. to 1,067 b.p.

ABCP and the Canadian Equity, Private Equity and Real Estate portfolios were the main contributors to the absolute risk of the overall portfolio as at December 31, 2008.

ACTIVE RISK

The active risk of most of the specialized portfolios increased significantly in 2008, owing to the increase in market volatility. In response to this situation, on a recommendation by Caisse senior management, the Board of Directors increased the active risk limit excluding ABCP to 250 b.p. Moreover, in the fourth quarter, the Board also eliminated the active risk limit including ABCP.

In October and November, the Caisse significantly changed its asset allocation and its currency hedging rate. The purpose of these decisions was to reduce the portfolio's absolute risk, but they also increased its active risk, since in this way the Caisse deviated from its benchmark portfolio.

The active risk of the overall portfolio ended the year at 444 b.p., for an increase of 249 b.p. If ABCP is excluded, active risk was 193 b.p., an increase of 38 b.p. ABCP and the Private Equity, Investments and Infrastructures, and Real Estate portfolios were the main contributors to the absolute risk of the overall portfolio as at December 31, 2008.

COMPARISON WITH PEERS

According to the study by RBC Dexia Investor Services, the average overall return of 3.1% over five years (2004-2008) ranks the Caisse in the third quartile of large Canadian pension funds. The study also indicates that this return was obtained with a level of realized risk comparable to that of the RBC Dexia sample (figure 26).

FIGURE 25

CAISSE'S OVERALL MARKET RISK (INCLUDING ABCP)

(Changes in risks from January to December 2008 – in basis points)

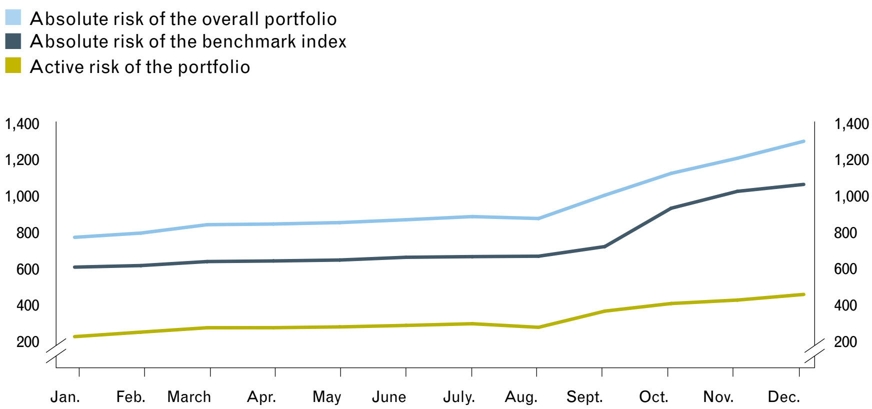
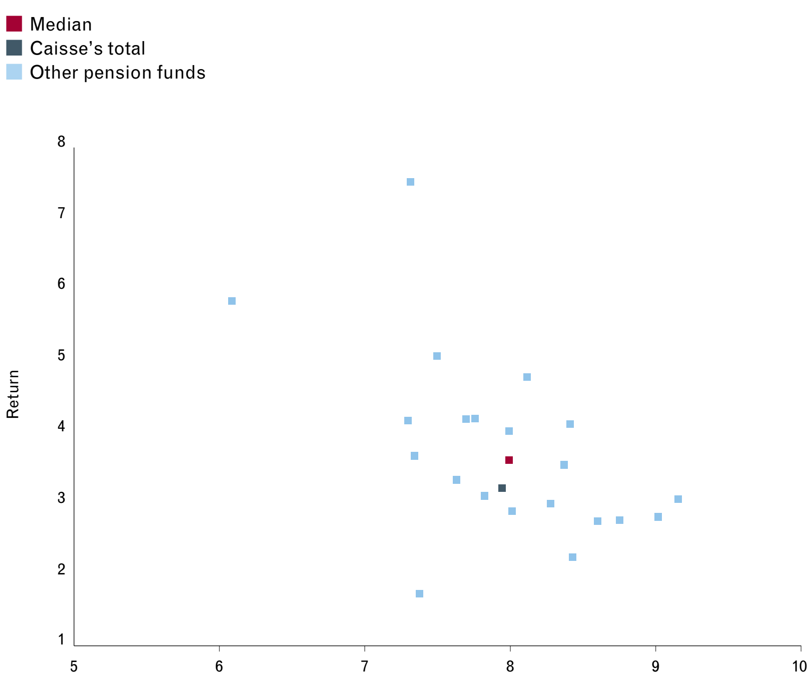


FIGURE 26

COMPARISON OF THE CAISSE WITH ITS PEERS: RELATIONSHIP BETWEEN HISTORIC RISK (FIVE YEARS) AND REALIZED RISK

(as at December 31, 2008 – in percentage)



Source: RBC Dexia Investor Services – Plans Over $1 Billion Universe.

ANALYSIS OF OVERALL PERFORMANCE

FAIR-VALUE VALUATION OF INVESTMENTS

Investment valuation is a process whereby a value is assigned to each investment held by the Caisse for the preparation of its financial statements. Valuation of investments at their fair value is performed periodically according to policies and procedures specific to each type of investment. These procedures comply with the standards and practices of Canadian and international organizations, and involve the use of closing prices on stock markets and independent valuation by professionals and experts. The Auditor General of Québec reviews all major investment valuations as part of his audit of the year-end financial statements.

ACCOUNTING PROVISIONS

According to accounting guideline no. 18 of the Canadian Institute of Chartered Accountants (CICA), the Caisse must establish the fair value of its investments on the assumption that they are available for sale as at the date of the preparation of the financial statements. This accounting guideline is to a great extent based on international changes in recent years to accounting standards on establishment of fair value. The purpose of the standards is to define a conceptual framework that can be used by all standards requiring fair-value valuation.

In normal circumstances, the fair-value, or mark-to-market, rule poses no problems because all financial markets are active, and investment values can be based on actual transactions involving comparable assets in various markets. When the markets are disrupted, however, namely when there are no purchases or sales, fair value has to be established on a mark-to-model basis whose parameters, including financing and illiquidity premiums, are subject to a high degree of subjectivity from one organization to another or from one valuation professional to another. The higher these premiums, the lower the fair value of the investments.

CURRENT DEBATE OVER FAIR VALUE

According to the accounting rules in effect in Canada, the Caisse is an investment company. As such, the Caisse, unlike other financial institutions, is not able to record its investments on a held-to-maturity basis. Its investments have therefore been valued as if they were available for sale as at the valuation date, namely December 31, 2008, when the markets were disrupted.

Fair-value valuation usually reflects potential profits and is an appropriate approach. The current crisis, however, has raised concerns regarding the use of the fair-value accounting rule, namely whether it still constitutes the best estimate of the value of financial assets and liabilities or whether, during a crisis, its use creates serious distortions.

At certain times, notably during a financial crisis, when liquidity is scarce and pricing information limited, this accounting rule causes discrepancies between the fair values established by various organizations for similar investments. The discrepancies indicate that the conceptual framework of the accounting standards for establishment of fair value gradually loses its relevance when the markets are inactive and volatile.

IMPACT ON THE CAISSE'S INVESTMENTS

The Caisse believes that these standards provide a coherent framework, but that they have to be applied with discernment. These restrictive standards do not take into account the fact that, in line with the long investment horizon adopted by its main depositors, the Caisse has the means and the intention to hold certain investments until their optimal value is reached.

At the end of 2008, inactivity on many financial markets, combined with abnormally high financing costs, made it necessary to use valuation models and parameters. The resulting unrealized decreases in value reflect the extreme volatility of the financial markets at that time.

Accordingly, the fair value established as at December 31, 2008, for investments on inactive markets, such as real estate, private equity, infrastructure, commercial debt and commercial mortgages, is more indicative of the extreme volatility on all the financial markets than the economic value of the investments held. In 2008, the Investments and Infrastructures, Private Equity, Real Estate Debt and Real Estate portfolios returned -44.7%, -31.4%, -7.6% and -21.9%, even though the investments in these portfolios continued to generate satisfactory income similar to the 2007 levels. Comparable income is expected in 2009.

ESTABLISHMENT OF FAIR VALUE AT THE CAISSE

Liquid investments

The fair value of liquid investments is established by means of valuation methods used in capital markets, such as discounting of future cash flows at the current interest rate, closing prices on major stock exchanges and data provided by securities brokers or other recognized specialist organizations.

On a quarterly basis, some of the portfolios and, on a semi-annual basis, all portfolios of unlisted liquid products are subject to valuation by independent professionals. These products, which include mainly bonds and over-the-counter derivatives, are evaluated with respect to the valuation models and data used.

Private equity

The fair value of private equity investments is established semi-annually as at June 30 and December 31, unless important circumstances entail a writedown of the value of an investment at another point in the year. The valuation is based on a valuation policy adopted by the Caisse's Board of Directors. The policy is based on the industry's best practices. It provides that the valuation of a private equity investment is first determined by the managers responsible for the investments concerned. It is then approved by the senior managers of the Private Equity group. Investments for which the fair value is higher than a pre-established materiality threshold must be submitted to an independent valuation committee or an independent external valuation professional.

Given the specialized nature of private equity investments, several valuation committees are used. These committees, which report to the Caisse's Audit Committee, are composed of independent valuation professionals. The Auditor General of Québec attends their meetings. The process is supplemented internally by periodic individual valuations as events occur.

Real estate

The fair value of real estate investments is established semi-annually as at June 30 and December 31, unless important circumstances entail a writedown of the value of an investment at another point in the year. Valuation of the investments in the Real Estate portfolio is based on a valuation policy adopted by the Caisse's Board of Directors. The policy is based on the industry's best practices.

For the Real Estate portfolio, external chartered appraisers certify the fair value of real estate assets. For other real estate investments, fair value is usually determined by external managers and, for debt associated with real estate investments, by internal managers. Moreover, the real estate units' external auditors perform work involving compilation of fair values when the audited financial statements are produced. Finally, in auditing the Caisse's books and accounts, the Auditor General of Québec relies on the work of external auditors and reviews all valuation reports.

In the case of the Real Estate Debt portfolio, the fair value of mortgage loans and securities is established according to the discounted value of future contractual cash flows at the market interest rate. This is the rate that can be obtained for loans or securities with similar conditions and maturity dates. In positions where cash flow spread cannot be estimated reasonably or reliably, the fair value corresponds either to the fair value of any asset given as collateral for the security, after deduction of foreseeable realization costs and any amount legally owed to the borrowers, or to the relevant market price for the security. For these investments, the Caisse relies on a valuation done by independent professionals or the externally audited financial statements of a subsidiary.

ABCP

In its original form, ABCP was a money market instrument with short-term maturities. Before the organized market for this type of financial instrument became frozen in August 2007, it provided daily quotations used to determine value. Since the real maturities of ABCP were often 90 days or less, its value fluctuated very little between the time of purchase, repricing of the instrument and its redemption by a trust.

In its restructured form, ABCP is a financial instrument with maturities that average seven years. Even so, there is no organized market for this type of instrument. Since no daily quotations are available, Canadian accounting standards require that ABCP be valued according to a discounting technique based on a financial model whose assumptions and probabilities reflect uncertainties regarding the amounts, the return and maturity of the cash flows, the illiquidity risk, the nature and credit risk of the underlying debt and financial assets, and credit spreads reflecting market conditions as at December 31, 2008.

The assumptions, based on information available as at December 31, 2008, use observable market data, such as interest rates, quality and credit price, as much as possible. They also take into account the particularities of the plan and are based partially on assumptions that are not backed by prices or rates observed on the market.

The fair value of each ABCP security has been establish from an estimate of the present value of cash flows according to various default and credit-loss scenarios covering all the underlying assets, the real maturities of the securities and the expected interest rates, and takes into account subordination of the restructured notes, where required. Once adjusted to take into account the impact of the credit risk of the underlying assets, the expected cash flows on the ABCP investments are discounted at a rate corresponding to a AAA credit rating, plus a financing and illiquidity premium.

Note 4b of the combined financial statements provides detailed information on the establishment of the fair value of the ABCP as well as the assumptions used.

ANALYSIS OF OVERALL PERFORMANCE

INTERNATIONAL OPERATIONS

In addition to investing in Québec and Canada, the Caisse has also been active on global markets since its inception. This approach goes hand in hand with its mission to seek an optimal return for depositors while minimizing risk. In line with the trend to global markets, the Caisse is active on five continents in a variety of asset classes.

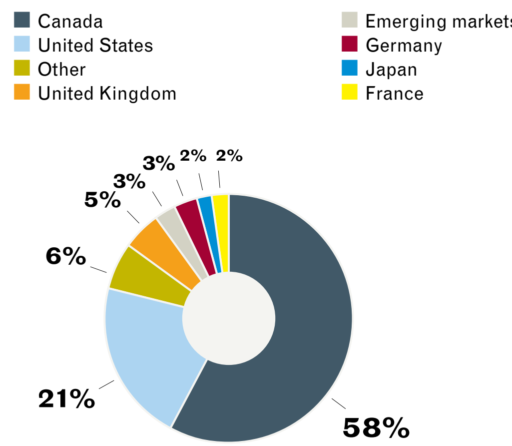
The proportion of depositors' total assets invested outside Canada was stable at 42% in 2008. This proportion should continue to change in the years to come as investment opportunities arise, especially in emerging markets, whose growth rates exceeded those of the industrialized countries. At present, most of the Caisse's foreign investments are made in industrialized countries. The United States represents 21% of total assets, up 3% from 2007, while the developed economies of Europe and Asia account for 18%. The United States, the United Kingdom, Germany, Japan and France each account for more than $4 billion of investment and thus represent the Caisse's main foreign markets (figure 27).

Investments in emerging markets amounted to $5.7 billion, all asset classes combined, or 3% of depositors' total assets. Holdings in the BRIC countries – Brazil, Russia, India and China – represented $2.8 billion, or 49% of emerging market investments, a 10% increase from 2007. The Caisse also had more than $1 billion in South Korea (figure 28). About 60% of the emerging market investments are in equities and about 40% in real estate.

FIGURE 27

GEOGRAPHIC BREAKDOWN OF DEPOSITORS' TOTAL ASSETS

(as at December 31, 2008 – in percentage)

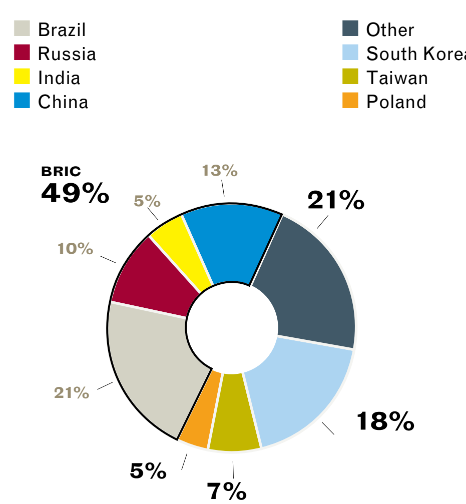


N.B.: As presented in the combined financial statements.

FIGURE 28

GEOGRAPHIC BREAKDOWN OF DEPOSITORS' TOTAL ASSETS IN EMERGING MARKETS

(as at December 31, 2008 – in percentage)



ASSET ALLOCATION

INVESTMENT PHILOSOPHY

ASSET ALLOCATION COMPRISES TWO COMPONENTS: REBALANCING DECISIONS AND MANAGEMENT OF THE ASSET ALLOCATION PORTFOLIO.

Rebalancing decisions involve short-term asset allocation operations that change the weighting of the specialized portfolios in relation to the benchmark portfolio within the limits set by the depositors' investment policies. These decisions entail overweighting or underweighting asset classes to enhance the Caisse's overall return.

The objective of the specialized Asset Allocation portfolio is to add value in relation to the Caisse's overall portfolio with a wide range of strategies designed to take advantage of opportunities on all the financial markets.

TABLE 29

MANAGEMENT OF ASSET ALLOCATION OPERATIONS

(as at December 31, 2008)

	Rebalancing decisions	
Management type	Active internal	The Caisse can adjust the weighting of the specialized portfolios within limits specified in the depositors' investment policies. These changes in weighting are limited, however, by market liquidity. For example, decisions regarding the Private Equity and Real Estate portfolios cannot be made at any time or without an impact on the value of these investments. The weighting of these portfolios therefore inevitably deviates from the target. The rebalancing decisions are based on the group's monthly analyses of the global macroeconomic environment and forecast returns on the various asset classes over the short and medium terms. These decisions are also a way of responding rapidly to economic and financial conditions.
Management approach	Discretionary	
Main analytical approach	Fundamental	
Investment horizon	0 to 18 months	
Main management styles and investment strategies	Opportunistic to enhance the Caisse's overall return	

Specialized portfolio	Asset Allocation				
Management mandate	Active management by Chief Strategist	Active management by Chief Investment Officer	Global tactical asset allocation		Research[1]
Management type	Active internal and partnership	Active internal	Active internal	Active external[2]	Active internal
Management approach	Discretionary	Discretionary	Discretionary and systematic	Discretionary and systematic	Discretionary and systematic
Main analytical approach	Fundamental	Fundamental	Top-down Econometric modelling and optimization	Top-down Relative evaluation of financial markets and risk premiums Econometric modelling and optimization	Fundamental and technical
Investment horizon	0 to 18 months	12 months to 10 years	0 to 18 months	0 to 18 months	0 to 18 months
Main management styles and investment strategies	Long-short Directional	Opportunistic to enhance the Caisse's overall return	Tactical directional (asset classes) Global macro		Long-short Directional

1 The Research team is also involved in managing the Québec International portfolio in co-operation with the Equity Markets group and the Fixed Income and Currencies group. The portfolio's returns are presented in the Equity Markets section.

2 Gradual disposition of the investments managed externally for the Tactical Asset Allocation mandate began in 2007, continued in 2008 and will be completed in the first half of 2009.

ASSET ALLOCATION

Confronted with the swift and simultaneous decline of most markets in the fourth quarter of 2008, the Caisse adapted its rebalancing decisions to reduce the absolute risk of the overall portfolio and to maintain a prudent level of liquidity. The systematic and discretionary strategies put in place by the managers of the Asset Allocation portfolio were tested by these extreme conditions. The managers moved more quickly to reduce the proportion of external mandates and closed out many positions managed in house. The losses generated by the asset allocation operations in 2008, including the Rebalancing Decisions component, totalled $2.0 billion, with three-quarters occurring in the fourth quarter.

HIGHLIGHTS

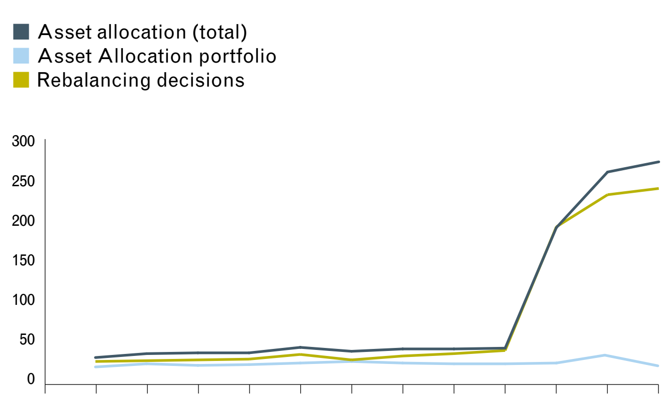
- / Over all, the Rebalancing Decisions component as well as active management of the four mandates of the Asset Allocation portfolio subtracted value in 2008. Only the decisions to rebalance the liquid portfolios, as well as those to reduce absolute risk in the fall, generated gains.
- / After a positive first half, the operations of all the mandates of the Asset Allocation portfolio began to subtract value in the third quarter. The losses rose sharply in the fourth quarter. The operations of the Chief Strategist were hit especially hard by market dislocation and an increase in volatility.
- / In the fourth quarter, various actions were taken for the Asset Allocation portfolio: termination of almost all external mandates and a major reduction of internal management operations. These activities are now under review. The Caisse also made rebalancing decisions to reduce the weighting of its equity investments and currency hedging for the specialized portfolios. These decisions were slightly profitable.
- / The Caisse plans to rebalance the overall portfolio in 2009 as a function of developments on the various markets. As for the Asset Allocation portfolio, its operations are under review.

OVERALL RETURN AND ANALYSIS OF ASSET ALLOCATION OPERATIONS

Asset allocation operations subtracted 107 b.p. (1.07%) from the Caisse's overall return in 2008, or the equivalent of $2.0 billion. The unprecedented financial crisis at the end of 2008, the simultaneous selloff on most markets, the sharp increase in volatility and the pronounced illiquidity of the markets had a tremendous impact on the asset allocation operations.

Figure 30 shows the active risk of the Asset Allocation portfolio and the rebalancing decisions. Reducing exposure to equity markets and increasing the weighting of fixed income in the fourth quarter resulted in a significant deviation from the depositors' benchmark portfolio. As a result, the active risk of the Rebalancing Decisions component increased significantly. The reduced foreign exchange hedging also increased the total active risk.

FIGURE 30
ACTIVE RISK – ASSET ALLOCATION
(for 2008 – in basis points)



N.B.: The active risk of the Asset Allocation portfolio excludes the effect of the decrease in currency hedging, whereas the total active risk includes it.

REBALANCING DECISIONS

Rebalancing decisions recorded a loss of $231 million in 2008. The decisions made during the year for the liquid portfolios and those made in the fourth quarter to preserve depositors' capital and to maintain a prudent level of liquidity generated gains. But the positioning of the less liquid portfolios gave rise to steep losses that completely cancelled out the gains.

Although overweighting the less liquid portfolios had often been profitable, the negative returns on these portfolios in 2008 reversed that situation. More specifically, the involuntary overweighting of the Real Estate and Real Estate Debt portfolios because of their inherent illiquidity is the main reason for the loss recorded in 2008. Tactical underweighting of the Emerging Markets Equity and Québec International portfolios in favour of the Bonds and Short Term Investments portfolios was profitable, however.

In addition, in response to the crisis, the Caisse quickly made decisions to reduce absolute risk and to maintain a prudent level of liquidity. For example, rebalancing decisions led to underweighting of the Equity Markets portfolios and the Commodities portfolio in favour of the Fixed Income and Currencies portfolios. The Caisse also reduced currency hedging of investments in international markets. At the same time, it reduced the potential margin calls it could have faced on currency forwards, in the expectation that the equity markets and the Canadian dollar would fall even further. This decision yielded positive results.

SPECIALIZED ASSET ALLOCATION PORTFOLIO

The specialized Asset Allocation portfolio lost $1.7 billion in 2008, subtracting 101 b.p. (1.01%) from the Caisse's overall return. The portfolio's operations generated positive returns in the first half of the year, but the managers were not able to protect their gains in the second half. The relative-value and volatility positions were hit especially hard by the extreme market conditions.

This loss is due to a great extent to various strategies based on a reduction in volatility over the long term on the stock and bond markets. When the crisis broke out in the fall, the opposite occurred, however, and volatility rose to extreme levels.

The interest-rate-arbitrage strategies and the fixed-income relative-value positions generated extremely negative returns. Moreover, strategies based on the spread between swaps and long-term bonds did not generate the expected return. The exit strategy put in place at year-end was hindered by illiquidity and pronounced market volatility.

Generally speaking, the systematic management strategies subtracted value. Positions based on the volatility of equity indexes generated a negative return as a result of the widespread market decline in 2008. These positions were closed out quickly at the start of the crisis, which limited losses. The operations of the Asset Allocation portfolio were scaled back substantially at the end of the year and are under review.

FIXED INCOME AND CURRENCIES

INVESTMENT PHILOSOPHY

THE INVESTMENT PHILOSOPHY OF THE FIXED INCOME AND CURRENCIES GROUP IS TO CREATE VALUE IN A RECURRING MANNER ACCORDING TO THE FOLLOWING PRINCIPLES:

/ Exploitation of opportunities on all fixed-income and currency markets;

/ Diversification and selection of management styles and investment strategies;

/ Diversification of the source of value added; and

/ Control over potential losses with rigorous management of market positions.

TABLE 31

SPECIALIZED PORTFOLIO MANAGEMENT BY THE FIXED INCOME AND CURRENCIES GROUP

(as at December 31, 2008)

Specialized portfolio	Short Term Investments	Real Return Bonds[1]	Bonds[1, 2]	Long Term Bonds[1]
Management type	Quasi-index	Strategic and tactical, internal and external		
Management approach	Discretionary	Discretionary and systematic		
Main analytical approach	Top-down and bottom-up Fundamental and quantitative	Top-down and bottom-up Fundamental and quantitative		
Investment horizon	0 to 18 months	0 to 18 months		
Main management styles and investment strategies	Replicate the return on the index as faithfully as possible	Directional, systematic and relative-value strategies involving interest rates, credit, volatility and currencies		

1 The Fixed Income and Currencies group uses a mechanism to share value added so that the various bond portfolios can benefit from the same investment ideas and expertise to generate value added. This approach makes it possible to allocate the value added of the Bonds portfolio to the other specialized portfolios forming the shared perimeter, namely Long Term Bonds, Real Return Bonds and Québec International (underlying bonds). The Short Term Investments portfolio is excluded from the perimeter.

2 Management of the Québec International portfolio is shared by the Equity Markets group and Fixed Income and Currencies group as well as the Research team (Asset Allocation portfolio), according to their expertise. The portfolio's returns are presented in the Equity Markets section.

The Fixed Income and Currencies group manages four specialized portfolios, contributes to the management of Québec International and plays three other roles:

/ Offers currency-hedging and advisory services to Caisse managers who invest in the international arena;

/ Co-ordinates and manages the Caisse's liquidity as a result of its comprehensive view; and

/ Contributes to the financing of the Caisse's less liquid portfolios, such as those of the Private Equity and Real Estate groups, notably to reduce their use of outside financing.

FIXED INCOME AND CURRENCIES

The managers in the Fixed Income and Currencies group had to cope with dysfunctional markets in the fourth quarter of 2008. The measures taken to help keep the Caisse's liquidity at a prudent level involved changes to the portfolios. These changes caused certain portfolio mandates to become imbalanced in relation to their indexes and therefore led to losses. The interest rate strategies, however, contributed very positively to the return, although the credit market strategies were unproductive. The portfolios have an overall return of 4.4% for 2008 and underperformed the benchmark index by 145 b.p. (1.45%).

HIGHLIGHTS

/ After three profitable quarters, during which the managers did well using opportunistic strategies, the Fixed Income and Currencies group saw its return plummet, as liquidity on the currency, interest rate and credit markets suddenly dried up. Even though the bond strategies continued to generate very positive results, the selection of corporate securities and the investments made in partnership with the Private Equity group subtracted value.

/ In October, the team responsible for the Caisse's foreign exchange hedging and the Currencies mandate had to cope with a market that at times was frozen. Certain positions that normally could have been closed out or hedged in a few hours had to be unwound gradually over several days, or even several weeks in some cases. The active management strategies therefore gave rise to losses.

/ The Fixed Income and Currencies group also closed out positions in the fourth quarter to help keep the Caisse's liquidity at a prudent level. These moves caused an imbalance in certain mandates in relation to their indexes, particularly the credit mandate. The positions sold were related mainly to the relative illiquidity of the various market segments.

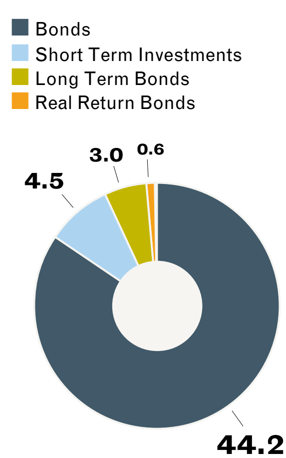
/ In 2009, the group will closely monitor the impacts of the crisis on interest rates and credit conditions. The low rates on government bonds and the lack of yield curve movement are indicative of limited investment opportunities if this situation persists in 2009. Moreover, an increase in default rates could adversely affect the credit market. The managers will therefore select securities prudently. Lastly, the managers are closely watching the greenback, since the United States is the epicentre of the financial crisis.

OVERALL RETURN AND SPECIALIZED PORTFOLIO ANALYSIS

The overall return on the portfolios is 4.4% in 2008, or 145 b.p. (1.45%) less than the benchmark index. Over five years, the return is 5.2%, or 21 b.p. (0.21%) less than the index. Table 33 gives the returns on the portfolios for one year, three years and five years. The Short Term Investments portfolio added value, while the Real Return Bonds, Bonds and Long Term Bonds portfolios underperformed their indexes.

The net assets in the portfolios totalled $52.2 billion as at December 31, 2008 (figure 32) versus $45.9 billion at the end of the previous period.

FIGURE 32
DEPOSITORS' NET ASSETS BY SPECIALIZED PORTFOLIO
(as at December 31, 2008 – in billions of dollars)



FIXED INCOME AND CURRENCIES

TABLE 33

SPECIALIZED PORTFOLIO RETURNS – FIXED INCOME AND CURRENCIES

(for periods ended December 31, 2008)

	1 year			3 years				5 years			
	Return %	Index[1] %	**Spread b.p.**	Return %	Index[1] %	**Spread b.p.**	Information ratio	Return %	Index[1] %	**Spread b.p.**	Information ratio
Short Term Investments	3.7	3.3	**35**	4.2	3.9	**30**	2.2	3.6	3.3	**29**	2.0
Real Return Bonds	(2.2)	0.4	**(260)**	(1.2)	(0.3)	**(93)**	(0.8)	5.5	6.1	**(53)**	(0.5)
Bonds	4.8	6.4	**(159)**	4.2	4.7	**(46)**	(0.4)	5.3	5.5	**(21)**	(0.3)
Long Term Bonds	4.6	6.2	**(151)**	4.3	4.8	**(49)**	(0.4)	–	–	**–**	–

1 The description of the indexes is given in the "General notes."

Until September, the group generated excellent returns. The economic scenario forecast by the group proved to be correct:

- A widespread decrease in short-term rates;
- A steepening of the interest rate curves;
- Further risk aversion; and
- Considerably wider credit spreads.

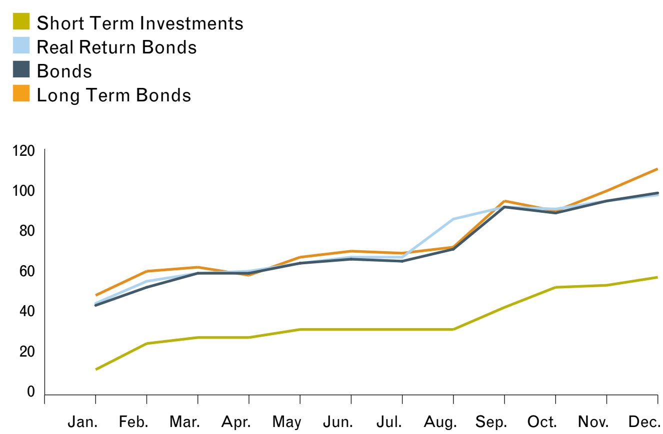
The group's strategies created value in the first three quarters. But in the last months of 2008 the expected economic crisis turned into a financial and liquidity crisis without precedent. This environment had an impact on the return earned by some of the group's mandates, especially the credit mandate. Moreover, the managers had to deal with difficulties stemming from the pronounced illiquidity of the markets. Over all, this situation cancelled out the gains made by the portfolios.

Figure 34 shows the active risk of the Fixed Income and Currencies group. The active risk of the Real Return Bonds and Long Term Bonds portfolios converges toward that of the Bonds portfolio because of the mechanism that shares the value added and risk between the portfolios. The active risk of all the specialized portfolios was up, mainly because of the increased volatility on the credit markets.

FIGURE 34

ACTIVE RISK – FIXED INCOME AND CURRENCIES

(for 2008 – in basis points)



SPECIALIZED SHORT TERM INVESTMENTS PORTFOLIO

The Short Term Investments portfolio returned 3.7% in 2008, or 35 b.p. (0.35%) more than its benchmark index. Over five years, the portfolio's return is 3.6%, or 29 b.p. (0.29%) more than its benchmark.

The Short Term Investments portfolio is managed prudently, and its structure was reviewed in 2008 to ensure simplified management. On a quarterly basis, the Bonds portfolio issues a three-month note in favour of the Short Term Investments portfolio. The note's rate is based on the Canadian treasury bill rate plus one-half of the spread between the T-bill rate and the repo rate. The portfolio benefitted in 2008 from the considerable spread between T-bill rates and repo rates, especially in March and during the financial crisis, and therefore was able to outperform the index.

SPECIALIZED REAL RETURN BONDS, BONDS AND LONG TERM BONDS PORTFOLIOS

All three portfolios underperformed their benchmark indexes in 2008. The Real Return Bonds portfolio subtracted 260 b.p. (2.60%) in relation to its index, with a return of -2.2%. The Bonds portfolio returned 4.8%, or 159 b.p. (1.59%) less than its index. As for the Long Term Bonds portfolio, it underperformed its index by 151 b.p. (1.51%) with a return of 4.6%.

Active management by the Fixed Income and Currencies group is centralized in the Bonds portfolio. The value added by this activity is then allocated among the Bonds, Real Return Bonds and Long Term Bonds portfolios.

The managers created value with judicious positions based on the yield curve. For example, the strategy combining swaps and spreads between Canadian and provincial bonds was profitable, even in the fourth quarter. An overweight position in short-term Canadian bonds against an underweight position in long bonds was also profitable.

In addition, the managers took advantage of the steepening yield curve with long positions in U.S. medium-term bonds against short positions in U.S. long-term bonds. Moreover, managers took advantage of the rate spreads between Canada and the United States and the relative value between provincial bonds. Still, the long position in U.S. real-return bonds gave rise to losses in the fall when inflationary expectations yielded to a deflationary outlook. The group also recorded losses on Canadian real return bonds, especially Québec notes, because of rising provincial rates.

The strategies used for corporate bonds and credit subtracted value. The managers were expecting credit spreads to widen in the context of a recession, which usually causes financial sector securities to outperform. But the persistent U.S. subprime residential mortgage crisis, combined with the global liquidity crisis, created substantial financing difficulties for U.S. and international financial institutions. At that point, financial sector securities began sustaining heavy losses that far exceeded the losses on other corporate notes. Security selection in the financial sector also had a negative impact on the portfolios' return. Moreover, the disposition of assets in the fourth quarter caused an imbalance in the allocation of this mandate and therefore increased the losses in relation to the index.

CREDIT SPREADS

The yield on bonds that are not issued by the government of the country involves a risk premium. This premium, expressed in basis points over and above the yield on government bonds, is a credit spread. In Canada, the yield spreads between corporate bonds and Canada bonds with the same maturity are credit spreads, as are the yield spreads between provincial bonds and Canada bonds.

During the crisis, investors turned massively to safe securities, pushing down interest rates on government bonds, such as Canada bonds. Since bond prices move inversely to interest rates, the value of federal bonds increased. The financial crisis also caused credit spreads for provincial and corporate bonds to widen considerably. Provincial bonds therefore underperformed federal bonds, while many corporate bonds recorded negative returns.

The credit mandate's partnerships with the Private Equity group detracted considerably from the return earned by the portfolios in 2008. The liquidity crisis and widening credit spreads pushed down the value of corporate loans, infrastructure loans, restructuring funds and distressed loans. Moreover, corporate loans and infrastructure loans posted an additional loss because of a significant devaluation at year-end, as a result of fair-value accounting rules.

For more details on fair-value accounting, consult the section "Analysis of overall performance."

FIXED INCOME AND CURRENCIES

Table 35 gives the group's investments by credit rating, including partnership securities.

TABLE 35

INVESTMENTS OF THE FIXED INCOME AND CURRENCIES GROUP BY CREDIT RATING

(as at December 31, 2008)

Credit rating	$M	%
AAA	27,436	43.4
AA	5,663	9.0
A	14,534	23.0
BBB	2,212	3.5
BB	559	0.9
B	22	–
CCC	27	–
CC	–	–
C	80	0.1
D	5	–
Non-rated[1]	12,730	20.1
Total	**63,267**	**100.0**

1 The financing provided by the Fixed Income and Currencies group to the Caisse's other portfolios, notably the Investments and Infrastructures, Private Equity and Real Estate portfolios, is not rated by the credit rating agencies. "Non-rated" refers essentially to these debt securities.

The operations of the Currencies team made a positive contribution to the portfolios' return in the first half of 2008. Positions in the Australian dollar against the Canadian dollar, as well as long positions in the yen in the first quarter and short positions in the yen in the second quarter, were especially profitable. The carry strategy[1] between emerging market currencies (Brazilian real, South African rand and Turkish lire) and the U.S. dollar also added value in the first half.

Starting in August, rapidly deteriorating global growth forecasts and falling commodity prices, which dragged down many currencies, including the Canadian dollar, caused the currency strategies to underperform. Moreover, the team was hit especially hard by the lack of liquidity on the currency markets in September, October and November. The managers were not able to close out certain positions quickly, an atypical situation for the foreign exchange market, deemed to be the most liquid market. The losses come from positions on the Asian currencies (South Korea, Indonesia, Malaysia, China and Thailand) and positions on the Scandinavian currencies against the pound sterling, and on the euro against the yen. Moreover, the carry strategy caused losses because of the appreciation of the U.S. dollar.

Table 36 lists the top 10 issuers in the specialized Bonds portfolio in alphabetical order.

TABLE 36

TOP 10 BOND ISSUERS

(as at December 31, 2008)

Bank Nederlandse Gemeenten NV
Canada Housing Trust
Financement Québec
Government of Canada
Government of Ontario
Government of Québec
Hydro-Québec
Kreditanstalt fuer Wiederaufbau
Merrill Lynch Mortgage Loans Inc.
Sydney Airport Finance Co. Pty. Ltd.

1 A carry strategy involves selling the currency of one country where interest rates are low and buying the currency of another country where interest rates are higher to take advantage of the interest rate differential.

EQUITY MARKETS

INVESTMENT PHILOSOPHY

TO ACHIEVE ITS VALUE-ADDED OBJECTIVES IN RELATION TO THE BENCHMARK INDEXES, THE GROUP USES:

- An analytical approach based on the intrinsic value of companies and their earnings outlook over the medium and long terms; and
- Optimization of the risk-return ratio, which favours construction of coherent, focused portfolios with the potential for excellent returns, in accordance with the limitations specified in the investment policies.

TABLE 37

SPECIALIZED PORTFOLIO MANAGEMENT BY THE EQUITY MARKETS GROUP

(as at December 31, 2008)

Market	Canadian	International			
Specialized portfolio	Canadian Equity	U.S. Equity (hedged and unhedged)	Foreign Equity (hedged and unhedged)	Emerging Markets Equity	Québec International[1]
Management type	Active internal	Active internal Index	Active internal and external Index	Active internal and external Index	Active internal and external Index
Management approach	Discretionary	Discretionary	Discretionary and systematic (external)	Discretionary and systematic (external)	Discretionary and systematic
Main analytical approach	Fundamental Bottom-up	Fundamental Bottom-up	Fundamental Bottom-up	Fundamental Bottom-up and top-down	Fundamental Bottom-up and top-down
Investment horizon	0 to 3 years				
Main management styles and investment strategies	Core Long Long-short	Long-short	Core Long Long-short	Core Long	Long-short (equity) Directional (bonds)

1 The Equity Markets group, the Fixed Income and Currencies group, and the Research team (Asset Allocation portfolio) share the management of the Québec International portfolio according to their expertise. The return on the portfolio is given in the Equity Markets section.

EQUITY MARKETS

The swift reversal on all the world's markets toward year-end and unprecedented volatility caused the returns on the specialized Equity Markets portfolios to fall sharply. This decline cancelled out all gains made in the first half of the year in sectors such as resources and energy, which until then were solid performers. The managers who were able to benefit from the proximity of their markets and leading-edge research were able to maintain portfolio equilibrium to outperform the benchmark indexes. In particular, this was the case of the Canadian Equity team in Montréal and the team at the New York office. The portfolios have an overall return of -36.7% for 2008 and underperformed the benchmark index by 89 b.p. (0.89%).

HIGHLIGHTS

/ The specialized Canadian Equity portfolio outperformed its benchmark index in 2008. The managers continued their strategy of more selective security selection on a long-term investment horizon.

/ Senior management of the Equity Markets group changed the management approach to the international equity portfolios managed in house at the Montréal office. These portfolios are now managed on an index basis rather than actively.

/ The group ended all the external management mandates of the U.S. Equity portfolio and scaled back those of the Foreign Equity portfolio.

/ As for the New York office, the long-short strategy put in place in 2006 has paid off. In 2008, it again outperformed the benchmark index.

/ In 2008, the Caisse obtained the status of Qualified Foreign Institutional Investor from the Chinese authorities. Starting in 2009, it will be able to invest up to US$200 million (in Chinese currency) in A-shares on the Shanghai and Shenzhen markets.

/ Under the policy on socially responsible investment, the managers incorporate non-financial criteria into their decisions. In 2008, working with the analysts, they contacted senior managers at Canadian companies more than 40 times to discuss governance, social responsibility and the environment. They also carried out direct engagement with mining companies on environmental matters. For the third year in a row, in co-operation with other institutional investors, the Caisse encouraged the Canadian companies in its portfolio to take part in the Carbon Disclosure Project.

/ In 2008, the Equity Markets group continued to tighten its operational model. In 2009, it will concentrate on active risk in niches where the group has comparative advantages, such as security selection by sector for Canadian equities, the long-short approach for U.S. equities (New York office), external management of foreign equities, index management and the multistrategy approach.

/ The sharp drop in financial stocks and the explosion of market volatility subtracted value in 2008, but as the intensity of the economic slowdown abates in 2009, volatility should drop, with a favourable impact on portfolio values.

OVERALL RETURN AND SPECIALIZED PORTFOLIO ANALYSIS

The Equity Markets portfolios earned an overall return of -36.7% in 2008, underperforming the benchmark index by 89 b.p. (0.89%). Over five years, the return is 1.3%, or 2 b.p. (0.02%) less than the benchmark. Table 39 shows the average annual return for each of the specialized portfolios for periods of one year, three years and five years.

Depositors' net assets in the specialized portfolios totalled $26.4 billion (figure 38) as at December 31, 2008, versus $56.3 billion a year earlier.

FIGURE 38
DEPOSITORS' NET ASSETS BY SPECIALIZED PORTFOLIO
(as at December 31, 2008 – in billions of dollars)

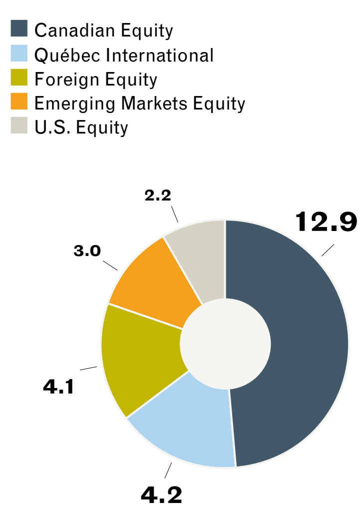


TABLE 39

SPECIALIZED PORTFOLIO RETURNS – EQUITY MARKETS

(for periods ended December 31, 2008)

	1 year			3 years				5 years			
	Return %	Index[1] %	**Spread b.p.**	Return %	Index[1] %	**Spread b.p.**	Information ratio	Return %	Index[1] %	**Spread b.p.**	Information ratio
Canadian Equity	(32.4)	(33.0)	**65**	(2.4)	(4.8)	**239**	1.2	5.3	4.2	**116**	0.6
U.S. Equity (hedged)	(45.2)	(39.0)	**(620)**	(14.1)	(10.1)	**(395)**	(1.1)	(5.9)	(3.3)	**(254)**	(0.9)
Foreign Equity (hedged)	(42.6)	(41.8)	**(79)**	(10.7)	(10.6)	**(11)**	(0.1)	0.3	0.7	**(37)**	(0.3)
Emerging Markets Equity	(45.0)	(41.6)	**(337)**	(5.1)	(3.1)	**(196)**	(0.8)	5.0	6.7	**(168)**	(0.9)
Québec International	(41.2)	(40.4)	**(82)**	(10.4)	(10.0)	**(40)**	(0.4)	0.0	0.2	**(19)**	(0.2)

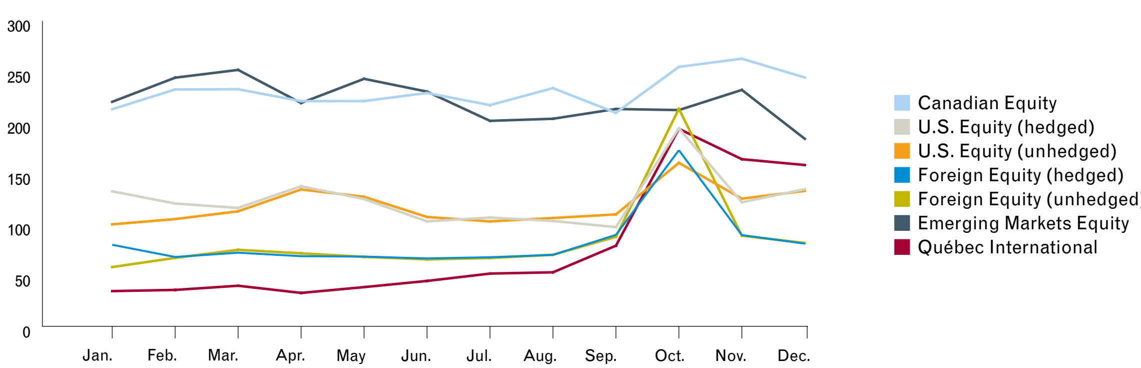
1 The description of the indexes is given in the "General notes."

Figure 40 shows the active risk of the Equity Markets portfolios. The strong market volatility had no major impact on the active risk of the specialized equity portfolios. In October, however, for asset allocation purposes and to help keep the Caisse's liquidity at a prudent level and to reduce absolute risk, the managers sold U.S. and foreign equities. As a result, the active risk of the portfolios concerned spiked during that month.

FIGURE 40

ACTIVE RISK – EQUITY MARKETS

(for 2008 – in basis points)



EQUITY MARKETS

SPECIALIZED CANADIAN EQUITY PORTFOLIO

The Canadian Equity portfolio's return for 2008 was -32.4%, or 65 b.p. (0.65%) more than the benchmark index. Over five years, the portfolio returned 5.3%, outperforming its benchmark by 116 b.p. (1.16%).

Once again, added value is due to a strategy based on security selection on a long-term horizon. The managers maintained a balanced portfolio of quality companies. In addition, by emphasizing long-term investment, the team maintained a low portfolio turnover rate, which reduced transaction costs.

During the year, the sectors that made the largest contribution to value added were energy, information technology and industrials. Companies in the financial and consumer sectors subtracted value substantially, however, as did absolute-return strategies.

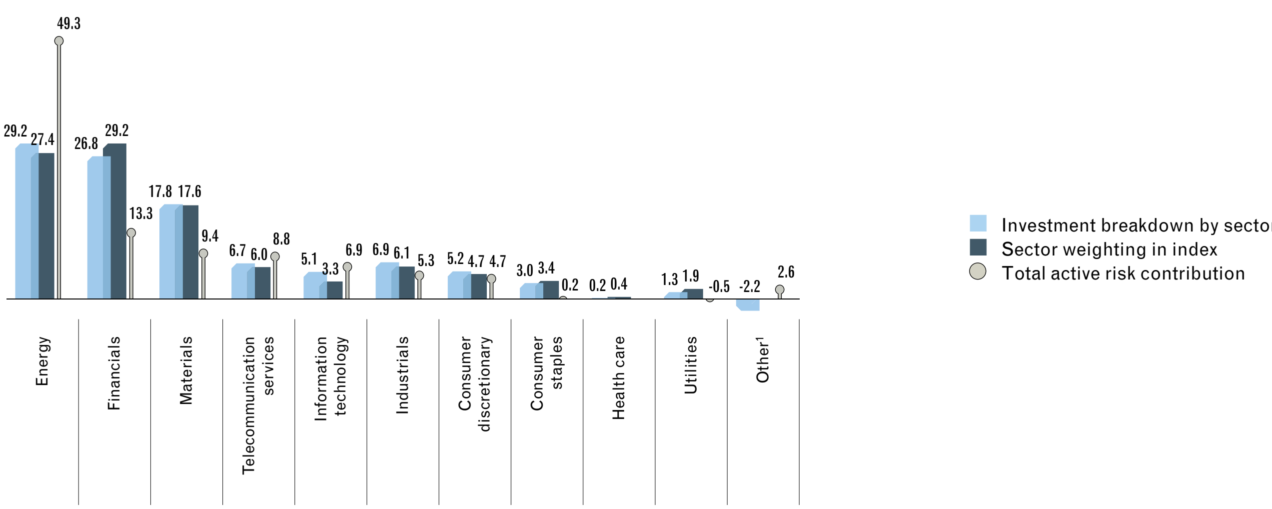
Figure 41 shows the weighting of each sector in the portfolio and its contribution to active risk. Security selection in the energy sector made the largest contribution to active risk.

Table 42 gives the portfolio's top 10 positions at year-end 2008 in alphabetical order.

TABLE 42
TOP 10 POSITIONS – CANADIAN EQUITY
(as at December 31, 2008)

Canadian Imperial Bank of Commerce
Canadian Natural Resources Limited
EnCana Corporation
Gold Corp.
Goldcorp Inc.
Manulife Financial Corp.
Rogers Communications Inc.
Royal Bank of Canada
Toronto-Dominion Bank
TransCanada Corp.

FIGURE 41
SECTOR BREAKDOWN OF ACTIVE RISK – CANADIAN EQUITY
(as at December 31, 2008 – in percentage)



1 Cash and cash equivalents, currency contracts, unallocated derivatives and generalist funds.

SPECIALIZED U.S. EQUITY PORTFOLIOS

The U.S. equity portfolios (hedged and unhedged) underperformed their benchmark index in 2008. The hedged U.S. Equity portfolio returned -45.2% in 2008, underperforming its benchmark index by 620 b.p. (6.20%).

The return on the unhedged portfolio is -28.0%, or 678 b.p. (6.78%) less than the index. The difference between the total returns on the hedged and unhedged portfolios is due to the Canadian dollar's sharp drop against its U.S. counterpart in the fall.

The underperformance in relation to the index is due mainly to the portfolio's decline in the fourth quarter. As for absolute-return operations, the extreme volatility in the fourth quarter caused substantial losses that offset all the gains made in the first half of the year. Moreover, as a result of unsatisfactory results over an extended period, the group terminated all the external management mandates.

Internally, for the second year in a row the managers at the New York office outperformed the index with a judicious long-short strategy. For most of the year, the long positions were the main contributors to the gains recorded, especially in the information technology, consumer staples and consumer discretionary sectors, as well as in financials.

Figure 43 shows the weighting of each sector in the portfolio and its contribution to active risk. The energy, information technology and consumer discretionary sectors contributed the most.

The hedged portfolio's average return over five years is -5.9%, or 254 b.p. (2.54%) less than its index. During that period, absolute-return strategies accounted for most of the value subtracted from the portfolio, primarily because of the scope of the losses recorded in the fourth quarter of 2008.

Table 44 presents the portfolio's top 10 positions in alphabetical order.

TABLE 44

TOP 10 POSITIONS – U.S. EQUITY

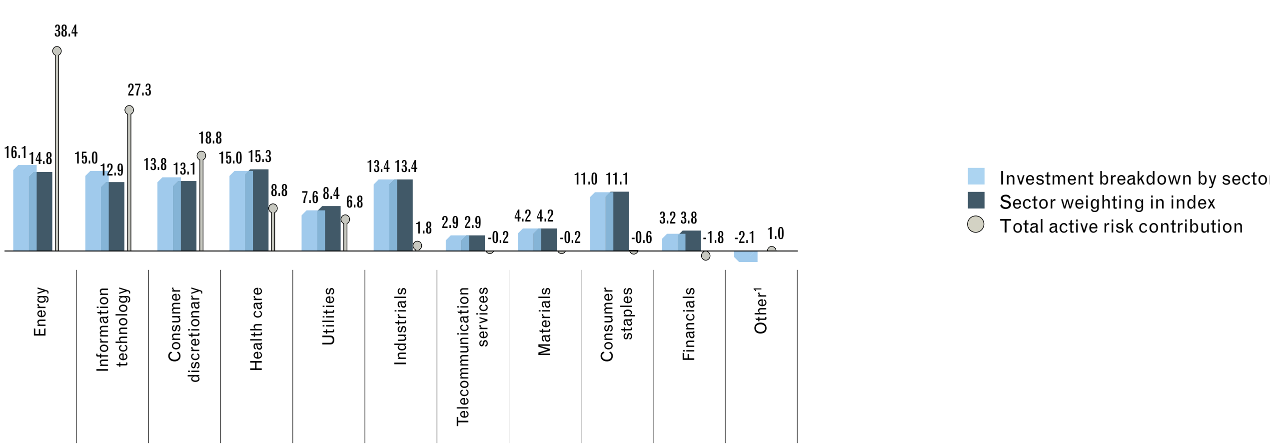
(as at December 31, 2008)

AT&T Inc.
Chevron
Exxon Mobil Corp.
General Electric Co.
Johnson & Johnson
JPMorgan Chase & Co.
Microsoft Corp.
Pfizer Inc.
Procter & Gamble Co.
Wal-Mart Stores

FIGURE 43

SECTOR BREAKDOWN OF ACTIVE RISK – U.S. EQUITY

(as at December 31, 2008 – in percentage)



1 Cash and cash equivalents, currency contracts, unallocated derivatives and generalist funds.

N.B.: Figures 41 and 43 give the sector breakdown of active risk. The contribution to active risk includes several parameters, such as the sector weighting of the portfolio and in relation to the benchmark index, the risk specific to each sector and the diversification effect. The level of contribution to active risk may, therefore, be different from the portfolio's sector exposure. A negative contribution indicates that the positions reduce the portfolio's risk as a result of the diversification effect.

EQUITY MARKETS

SPECIALIZED FOREIGN EQUITY PORTFOLIOS

The Foreign Equity portfolios (hedged and unhedged) underperformed their benchmark index. The hedged Foreign Equity portfolio returned -42.6%, or 79 b.p. (0.79%) less than its index.

The unhedged Foreign Equity portfolio returned -29.8%, or 61 b.p. (0.61%) less than the benchmark index. The difference between the total return on this portfolio and that of the hedged portfolio is due to the Canadian dollar's weakness against the euro and the yen.

For the year as a whole, the internal management team underperformed the benchmark by only a few basis points. The strategies used for the U.K. market subtracted value, with most losses coming in the financial sector. In the last quarter, the group transferred the U.K. portion of the portfolio to index management.

The external managers made a positive overall contribution in relation to the benchmark index. Certain external mandates underweighted financials and materials and significantly outperformed their index. Moreover, the absolute-return operations, which are limited to borrowing and lending of the securities in the portfolio, were profitable.

Figure 45 shows the geographic breakdown of the investments and the contribution to the active risk assumed by the portfolio managers. The contribution to active risk by geographic market is due mainly to underweighting Australia and Japan.

The hedged portfolio's average annual return over five years is 0.3%, or 37 b.p. (0.37%) less than its index. During that period, active external management outperformed the indexes, while active internal management fell short.

Table 46 presents the portfolio's top 10 positions in alphabetical order.

TABLE 46

TOP 10 POSITIONS – FOREIGN EQUITY

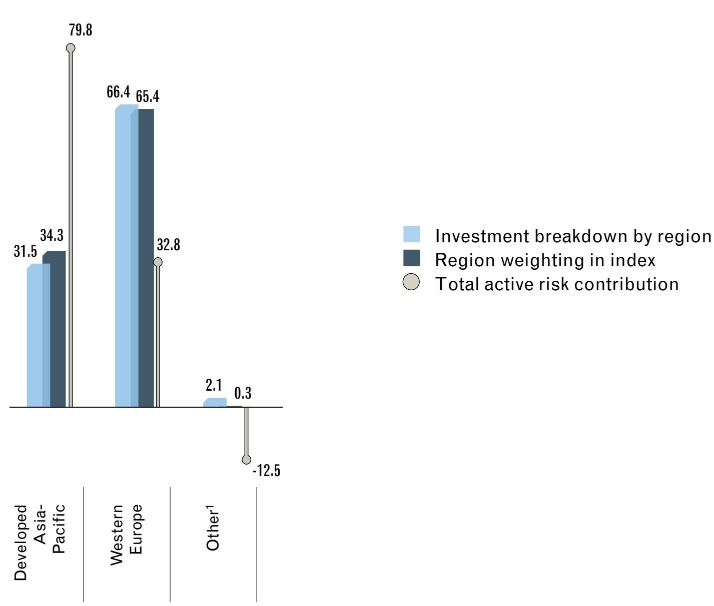
(as at December 31, 2008)

BP PLC
ENI SpA
HSBC Holdings PLC
Nestlé SA
Novartis AG
Roche Holding AG
Royal Dutch Shell PLC
Telefonica SA
Toyota Motor Corp.
Vodafone Group PLC

FIGURE 45

GEOGRAPHIC BREAKDOWN OF ACTIVE RISK – FOREIGN EQUITY

(as at December 31, 2008 – in percentage)



1 Offshore, cash and cash equivalents, currency contracts, unallocated derivatives and generalist funds.

SPECIALIZED EMERGING MARKETS PORTFOLIO

The Emerging Markets Equity portfolio returned -45.0% in 2008, underperforming its benchmark index by 337 b.p. (3.37%).

This underperformance is due mainly to the results obtained by in-house active management. Moreover, the losses were amplified by currency depreciation in the countries making up the index. As for the external management mandates, the results fell slightly short of the index owing to the significant drop in the return in the fourth quarter. As for absolute-return strategies, securities lending and borrowing was profitable all year and added value to the portfolio.

With respect to internal active management, from January to November security selection for India, South Africa, Taiwan and Brazil was the activity that subtracted the most value. Thereafter, in light of these disappointing results, the group's managers began reducing the portfolio's active risk.

The external managers continued their active management mandates. Their returns differed considerably, however. Three had negative returns while one obtained twice its value-added objective. Security selection for Mexico, China and Indonesia was the least profitable in 2008.

Figure 47 shows the geographic breakdown of the investments and the contribution to active risk. The contribution to active risk by geographic market is due mainly to security selection in Asia and Latin America.

Over five years, the portfolio has an average annual return of 5.0%, underperforming the benchmark index by 168 b.p. (1.68%). For that period, both internal and external active management made a negative contribution in relation to the benchmark index.

Table 48 shows the portfolio's top 10 positions in alphabetical order.

TABLE 48

TOP 10 POSITIONS – EMERGING MARKETS EQUITY

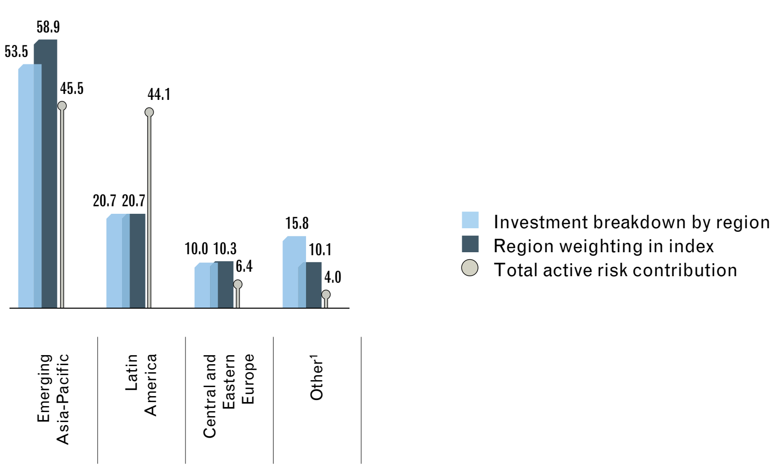
(as at December 31, 2008)

America Movil SAB de CV
China Life Insurance Co. Ltd.
China Mobile Ltd.
Companhia Vale do Rio Doce CVRD
Gazprom OAO
Industrial & Commercial Bank of China
PetroChina Co. Ltd.
Petroleo Brasileiro SA
Samsung Electronics Co. Ltd.
Taiwan Semiconductor Manufacturing Co. Ltd.

FIGURE 47

GEOGRAPHIC BREAKDOWN OF ACTIVE RISK – EMERGING MARKETS EQUITY

(as at December 31, 2008 – in percentage)



1 Developed Asia-Pacific, Africa, offshore, cash and cash equivalents, currency contracts, unallocated derivatives and generalist funds.

N.B.: Figures 45 and 47 give the geographic allocation of active risk. The contribution to active risk includes several parameters, such as the regional weighting in the portfolio and in relation to the benchmark index, the risk specific to each region and the diversification effect. The level of contribution to active risk may, therefore, be different from the portfolio's geographic exposure.

EQUITY MARKETS

SPECIALIZED QUÉBEC INTERNATIONAL PORTFOLIO

The Québec International portfolio returned -41.2% in 2008, underperforming its benchmark index by 82 b.p. (0.82%). For the nine-month period ended September 30, 2008, the managers' return outperformed the index, but the gains were completely cancelled out by the portfolio's substantial decline in the fourth quarter.

The Equity Markets group, the Fixed Income and Currencies group and the Research team (Asset Allocation portfolio) actively manage the portfolio according to their fields of expertise. The strategies adopted by the Equity Markets group increased the portfolio's value in 2008. The Fixed Income and Currencies group and the Research team recorded substantial losses, however, mainly because of country and security selection.

Over five years, the portfolio has an average annual return of 0.0%, or 19 b.p. (0.19%) less than the index. During that period, however, it outperformed the index in 2004, 2005 and 2007.

QUÉBEC INTERNATIONAL

The specialized Québec International portfolio has a hybrid structure. It consists of bonds denominated in Canadian dollars, which implicitly protects it against currency risk, as well as a basket of futures contracts based on world stock markets. The futures contracts produce a stock-index return in exchange for a return on short-term investments. The portfolio's objective is to increase the exposure of the Caisse's overall portfolio to foreign equity markets with a view to greater diversification and superior returns.

HEDGE FUNDS

INVESTMENT PHILOSOPHY

THE INVESTMENT PHILOSOPHY OF THE HEDGE FUNDS GROUP IS TO:

/ Identify and invest in the best sources of value added in the hedge fund and commodities industry;

/ Analyze fundamental factors likely to affect returns and identify market inefficiencies;

/ Use quantitative methods to identify investment opportunities;

/ Perform rigorous risk management in the design of each strategy and transaction; and

/ Optimize the portfolio's structure by emphasizing external funds that respect the principles of transparency, alignment of interests and governance.

TABLE 49

SPECIALIZED PORTFOLIO MANAGEMENT BY THE HEDGE FUNDS GROUP

(as at December 31, 2008)

Specialized portfolio	Hedge Funds				Commodities
Management mandate	Discretionary Global Macro	Equity Global Macro	Hedge Funds of Funds[1]	Strategic Opportunities (hedge funds alternative beta)	Management of commodity futures Management of underlying currencies and real-return bonds
Management type	Active internal	Active internal	Active external	Active internal and partnership	Active internal and external Index internal and external
Management approach	Discretionary and systematic	Discretionary	Discretionary	Quantitative and systematic	Discretionary
Main analytical approach	Top-down Relative evaluation of financial markets and risk premiums	Macroeconomic Top-down Relative evaluation of sectors and regions	Fundamental Top-down (selection of strategies) and bottom-up (selection of managers)	Top-down and bottom-up	Fundamental and technical
Investment horizon	0 to 3 years				0 to 18 months
Main management styles and investment strategies	Global macro Long-short	Global macro Long-short	Arbitrage Event-driven Global macro Long-short	Directional Relative value	Long-short Directional Relative value

1 The group undertook an operational restructuring of the Hedge Funds of Funds mandate in 2008 to simplify its management. When the restructuring is complete in the first half of 2009, the mandate will go by the name of External Hedge Funds.

HEDGE FUNDS

The Hedge Funds group continues to reposition its operations to capitalize on the managers' experience in evaluating, selecting and monitoring the best investment strategies and external funds. Even so, the group was not able to avoid the negative outcome of the credit and liquidity crisis that hit the global markets. Moreover, falling commodity prices in the second half of the year had an adverse impact on the positions in the Commodities portfolio. The portfolios have an overall return of -21.3% for 2008 and underperformed the benchmark index by 42 b.p. (0.42%).

HIGHLIGHTS

/ The extreme volatility of the markets combined with illiquidity on the bond and foreign exchange markets in the fall of 2008 obliged the Hedge Funds group to reduce the portfolios' absolute risk so as to preserve capital. Moreover, greater correlation between the world's financial markets curtailed investment opportunities toward year-end, thereby reducing active risk-taking.

/ As in 2007, the group reduced the number of external funds and slightly increased the weighting of highly specialized funds. It also established stricter selection criteria as a function of investment strategies, management fees and asset liquidity. The group continued its initiatives to improve the transparency of the external funds and to gradually bring their management policies into line with the interests of the Caisse and its depositors.

/ The group began an operational restructuring of the funds of funds in the fourth quarter to improve investment, monitoring and reporting procedures. This measure will be completed in the first half of 2009 and will reduce operating costs.

/ The operations of the Hedge Funds portfolio's Equity Global Macro mandate began early in July. The managers of this mandate aim to profit from macroeconomic trends and imbalances between sectors and regions using equity-related securities.

/ The managers of the Commodities portfolio put in place a new operating platform to improve risk measurement and monitoring.

/ The managers of the Hedge Funds portfolio expect an increase in default rates and a return to less correlation between the world's financial markets by the end of 2009. The hedge fund industry will most likely undergo profound change in 2009. The team that selects and monitors the external funds will therefore continue to be cautious. As for the Commodities portfolio, the managers are gradually positioning themselves for an eventual increase in the demand for commodities in a context of supply constraints. In the meantime, they are partial to relative-value positions in metals and agricultural products.

OVERALL RETURN AND SPECIALIZED PORTFOLIO ANALYSIS

The portfolios had an overall return of -21.3% in 2008, underperforming the benchmark index by 42 b.p. (0.42%). Table 50 gives the returns for periods of one year, three years and five years.

The Depositors' net assets in the Hedge Funds and Commodities portfolios totalled $5.3 billion as at December 31, 2008 (figure 51), versus $7.7 billion at the end of 2007.

FIGURE 51

DEPOSITORS' NET ASSETS BY SPECIALIZED PORTFOLIO

(as at December 31, 2008 – in billions of dollars)

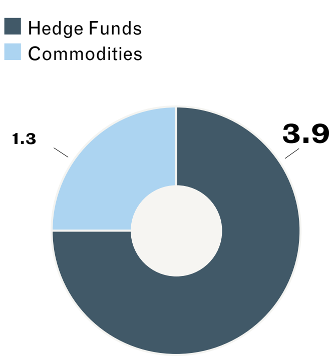


TABLE 50

SPECIALIZED PORTFOLIO RETURNS – HEDGE FUNDS

(for periods ended December 31, 2008)

	1 year			3 years				5 years			
	Return %	Index[1] %	**Spread b.p.**	Return %	Index[1] %	**Spread b.p.**	Information ratio	Return %	Index[1] %	**Spread b.p.**	Information ratio
Hedge Funds	(20.9)	(20.8)	**(7)**	(2.6)	(3.4)	**84**	0.1	1.1	(1.2)	**229**	0.6
Commodities	(25.4)	(23.2)	**(216)**	(8.5)	(7.6)	**(87)**	(0.2)	–	–	**–**	–

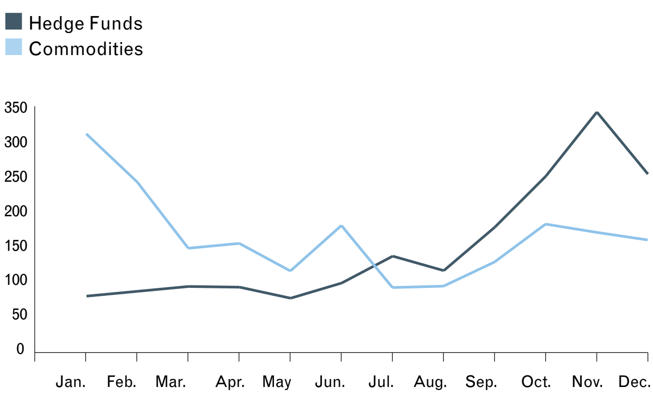
1 The description of the indexes is given in the "General notes."

Figure 52 shows the active risk of the Hedge Funds group. The active risk of the Hedge Funds portfolio increased considerably in the fall along with the market volatility. The risk decreased somewhat toward year-end, however, when various positions were closed. The active risk of the Commodities portfolio fell in the first quarter because of the decision to close out certain positions so as to take profits. In the second half, active risk fluctuated along with variations in the prices of the commodities underlying the index's components.

FIGURE 52

ACTIVE RISK – HEDGE FUNDS

(for 2008 – in basis points)



SPECIALIZED HEDGE FUNDS PORTFOLIO

The Hedge Funds portfolio had a return of -20.9% in 2008, or 7 b.p. (0.07%) less than its benchmark index. Over five years, the portfolio has an average return of 1.1%, outperforming its benchmark index by 229 b.p. (2.29%).

In-house active management gave rise to losses. For the Discretionary Global Macro mandate, the managers' strategies called for devaluation of the euro, convergence of short-term global interest rates and lower inflation in the United Kingdom. In the first half, however, the opposite scenario occurred. In the second half, tumbling energy prices and lower valuations for companies in that sector put downward pressure on returns. The managers closed out many of these positions in September, when the crisis took hold, so as to reduce the mandate's risk.

The operations of the Equity Global Macro mandate began in July with a defensive positioning aligned with the deteriorating global economic and financial situation. Nevertheless, the scope of certain market events caused losses. The short positions in the financial sector suffered when the U.S. government adopted a plan to bail out struggling financial institutions. The managers reacted quickly; they closed out these positions and reduced the mandate's risk by one-half. In October, short positions in the European automobile sector recorded losses because of the sharp rebound of one security. Still, the managers did well with strategies based on plummeting energy prices, declining demand in emerging markets and resilience in the health care sector.

In 2008, to improve the diversification of the Strategic Opportunities mandate (hedge funds alternative beta), the managers adopted new investment approaches based on the industry's best quantitative and systematic strategies. In addition, a balance between trend-driven strategies and strategies based on long positions reduced the losses incurred by long-short equity strategies. Market-neutral strategies produced mixed results. The positions were reduced considerably in the fourth quarter in response to extreme market conditions.

The selection of external funds and their allocation by style and strategy generated positive results in 2008. The managers reduced the amounts invested in funds specializing in long-short equity strategies and increased their investments in funds that focus on distressed debt. Moreover, their decision to overweight funds that take advantage of market trends produced gains in relation to the benchmark index.

The external funds were not able to avoid the markets' sharp decline, however. But they did manage to limit losses and to outperform the benchmark index. Funds that specialize in global macro strategies and directional positions based on market trends stood out. Fixed-income-arbitrage funds, which use leverage to enhance their returns, suffered the most, owing to deleveraging in the market.

HEDGE FUNDS

Table 53 gives the portfolio's top 10 hedge fund management companies in alphabetical order.

TABLE 53
TOP 10 MANAGEMENT COMPANIES – HEDGE FUNDS
(as at December 31, 2008)

AQR Capital Management LLC
Brevan Howard Capital Management LP
Crestline Management LP
D.E. Shaw & Co. LP
Diversified Global Asset Management Corporation
HBK Investments LP
Och-Ziff Capital Management Group
Pacific Alternative Asset Management Company
Paulson Advantage
Spinnaker Capital Ltd.

SPECIALIZED COMMODITIES PORTFOLIO

The Commodities portfolio made gains in the first half of the year in relation to the index. But market volatility and plummeting prices in the second half completely offset these gains. The portfolio returned -25.4% in 2008, underperforming the benchmark index by 216 b.p. (2.16%).

Over three years, the portfolio has an average annual return of -8.5% and underperformed the index by 87 b.p. (0.87%). Active management in metals and energy and the cost of replicating the index are the reasons for this result.

Management of the Commodities portfolio is divided into two main activities: index management and active management. Index management uses commodity derivatives to replicate the return on the benchmark index. The return on these operations fell slightly short of the benchmark. The difference is due to the cost of rolling over the futures contracts required to replicate the index.

Active management uses derivatives to manage sector weightings (energy, industrial metals, precious metals, livestock, grains and agricultural commodities) and commodity weightings. In the first half of 2008, the Commodities portfolio managers took advantage of rising energy prices. Strategies based on rising forward prices for natural gas and increasingly volatile crude oil prices were profitable. The strategy based on overvaluation of the price of agricultural products also paid off. The short positions in copper and gold generated losses, however.

In the third and especially the fourth quarters, commodity prices collapsed amid expectations of a global recession and falling demand. As a result, all sectors lost ground and ended the year in negative territory, with the exception of gold, which rose slightly on safe-haven buying. The managers' strategies for industrial and precious metals subtracted value as a result of strong volatility. But they recorded some gains with their positions in crude oil, natural gas and agricultural products.

PRIVATE EQUITY

INVESTMENT PHILOSOPHY

PRIVATE EQUITY INVESTMENT REQUIRES THOROUGH COVERAGE OF TARGET MARKETS AND COMPANIES. THE GROUP'S INVESTMENT PHILOSOPHY IS THEREFORE BASED ON:

/ Investment allocation by category, taking into account the market cycle;

/ Direct investments in markets close at hand, partnerships for distant markets and an opportunistic approach geared to market conditions;

/ Selection of the best corporate management teams and investment funds to maximize long-term returns;

/ Risk management based on analysis and rigorous monitoring of investments, including exit strategies; and

/ Investment diversification by industrial sector, geographic area, financial product and business maturity.

TABLE 54

SPECIALIZED PORTFOLIO MANAGEMENT BY THE PRIVATE EQUITY GROUP

(as at December 31, 2008)

Specialized portfolio		**Investments and Infrastructures**			**Private Equity**			
Investment categories		Development capital	Debt	Infrastructures	Leveraged buyouts	Venture capital	Mezzanine debt	Restructuring
Management type		Active						
Management by geographic region	Québec	Direct	Direct	Direct	Indirect or partnership	Indirect	Direct	Indirect
	Canada ex Québec	Direct or partnership	Direct or syndication	Direct or partnership	Indirect or partnership	Indirect	Direct or partnership	Indirect
	United-States / Europe	Direct or partnership	Partnership or syndication	Direct or partnership	Indirect or partnership	Indirect	Direct or partnership	Indirect
	Emerging markets	–	–	Indirect and market watch	Indirect	–	–	–
Main investment vehicles		Equity securities	Senior debt	Equity securities	Funds and equity securities	Funds	Funds and debt securities	Funds
Management approach		Discretionary						
Main analytical approach		Fundamental bottom-up						
Investment horizon		3 to 7 years						
Main management styles and investment strategies		Long Participation						

PRIVATE EQUITY

The Private Equity group continued to adjust its action plan in 2008 to reflect the market's accelerated move into the contraction phase of the cycle. This shift affected all types of private equity. Leveraged buyouts are the category that saw the most pronounced slowdown as a result of the credit crisis. Distressed loans and restructuring funds offered the most appealing business opportunities, however. The value of the investments authorized during the year is less than half that of 2007. The group continued to be very selective about its investments, focusing on those categories that offer the most promising returns at this phase of the cycle. At the same time, it carefully managed existing holdings. The portfolios have an overall return of -36.0% for 2008 and underperformed the benchmark index by 281 b.p. (2.81%).

TABLE 55

OVERALL INVESTMENTS AUTHORIZED IN 2008

Investment category	Number	$M
Debt	5	1,226
Infrastructures	4	596
Venture capital	8	172
Leveraged buyouts and mezzanine debt	15	924
Development capital and accumulation	13	552
Restructuring	1	370
Total	**46**	**3,840**
Management type		
Direct transactions	29	2,063
Funds	17	1,777
Total	**46**	**3,840**

HIGHLIGHTS

/ The investments authorized in 2008 totalled $3.84 billion, versus $8.97 billion a year earlier and $18.6 billion at the peak in 2006. Direct transactions came to $2.1 billion and investments in funds, $1.8 billion (table 55).

/ As for the transactions authorized in 2008, reinvestments in portfolio companies and funds accounted for more than half of the total. Discounted interests in senior-debt portfolios also figured prominently, with more than a quarter of the amounts authorized. Table 56 shows a sampling of the investments given the green light in 2008.

/ Leveraged buyouts, restructuring funds and distressed loans account for three-quarters of the amounts disbursed in 2008, mainly as a result of approvals given in previous years.

/ To help maintain the Caisse's liquidity at a prudent level and to reduce its absolute risk, the group sold listed securities. These dispositions totalled about $1.0 billion during the year.

/ The Caisse and the Business Development Bank of Canada celebrated five years of partnership in the AlterInvest Fund in 2008. The fund supports small and medium-sized enterprises (SMEs) in Canada, regardless of their development stage. Since 2003, it has invested $453 million in 371 SMEs, with more than $200 million of the disbursements going to Québec.

/ In 2009, the Private Equity group will apply the strategy developed and approved at the end of the year. It will continue to manage its holdings carefully, paying special attention to portfolio companies in need of financial support to ensure they are poised to take advantage of the coming recovery. At the same time, the managers will apply their development-capital expertise close to home, namely in Québec, since this category generally offers the best potential for long-term returns in the context of a recession.

OVERALL RETURN AND SPECIALIZED PORTFOLIO ANALYSIS

The overall return on the portfolios for 2008 is -36.0%, or 281 b.p. (2.81%) more than the benchmark index. As a result of the credit crunch and the global economic crisis, private equity retrenched and the deal flow dried up. Moreover, the inactive market, combined with strong volatility, considerably reduced the value of the companies in the portfolio, since their valuations are established as if they were available for sale as at December 31, regardless of how long they will actually be held. Thus, even though many companies have a sound financial position, increased their earnings in 2008 and are poised to take advantage of an upturn, their valuations are down substantially.

It should be noted that lower return is due mainly to an unrealized decrease in value. As the private equity sector recovers, the valuations of the portfolio companies should improve.

Table 57 gives the details of the average returns on the group's portfolios for periods of one year, three years and five years. Before the onset of the credit crisis in August 2007, the group took advantage of favourable market conditions. For the past five years, the Private Equity group's return is 5.5%, with 648 b.p. (6.48%) of value added in relation to the benchmark index, notably because of the excellent results with leveraged buyouts in 2004, 2005 and 2006.

TABLE 56
EXAMPLES OF INVESTMENTS AUTHORIZED IN 2008

Targeted firm	Head office	Sector	Partners	Project
Empire Maintenance Industries Inc.	Montréal	Commercial and industrial cleaning company	BMO Capital Corporation and Bank of Montreal	Partial buyout of a shareholder
Gestions Varekai Inc. (Les Fermes Sunchef)	Montréal	Chicken processing	None	Increase in production capacity
Rad Technologies Inc.	Thetford Mines	Snowblowers and tractor attachments for various markets	None	Recapitalization
Solisco Printers Inc.	Scott	Commercial printing and graphic production	None	Expansion project and shareholder buyout
Pixman Nomadic Media Inc.	Montréal	Tactical and mobile marketing	FIER Boréal 02 FIER Ville-Marie s.e.c. Fonds d'investissement Actions-croissance PME inc.	Expansion project
Cycle Capital Fund I, LP	Montréal	Fund that invests in the cleantech and renewable energy sectors	Cascades Inc. Centrale des syndicats du Québec (CSQ) Brookfield Renewable Power Inc. Fonds d'action québécois pour le développement durable (FAQDD) Solidarity Fund QFL Fondaction CSN Investissement Québec	Creation of a venture capital fund
TPG Partners VI, LP	United States	Generalist investment fund that focuses on large investments	TPG GenPar VI, LP	Leveraged-buyout fund
Clarus Lifesciences II, LP	United States	Investment fund that specializes in biotechnology companies	Clarus Ventures, LLC	Venture capital fund

TABLE 57
SPECIALIZED PORTFOLIO RETURNS – PRIVATE EQUITY
(for periods ended December 31, 2008)

	1 year			3 years				5 years			
	Return %	Index[1] %	**Spread b.p.**	Return %	Index[1] %	**Spread b.p.**	Information ratio	Return %	Index[1] %	**Spread b.p.**	Information ratio
Investments and Infrastructures	(44.7)	(36.6)	**(807)**	(12.0)	(7.0)	**(492)**	–	(2.1)	1.4	**(350)**	–
Private Equity	(31.4)	(40.1)	**872**	1.3	(10.9)	**1,226**	–	10.6	(3.0)	**1,354**	–

1 The description of the indexes is given in the "General notes."

PRIVATE EQUITY

TABLE 58

TOTAL ASSETS UNDER MANAGEMENT – PRIVATE EQUITY

(fair value as at December 31, 2008 – in billions of dollars)

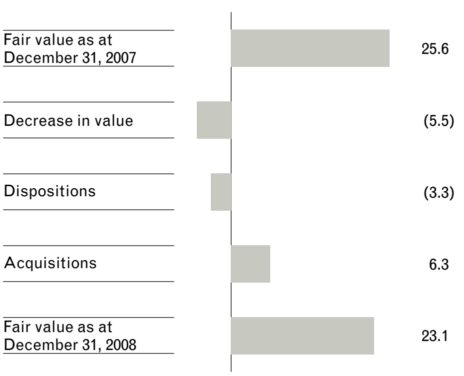
	Depositors' net assets	Depositors' total assets[1]	Assets under management or under administration	Total assets under management	
Investments and Infrastructures	4.3	11.8	0.8	12.6	50.2%
Private Equity	9.7	12.5	–	12.5	49.8%
Total	**14.0**	**24.3**	**0.8**	**25.1**	**100.0%**

1 Including assets related to the internal partnership with the Fixed Income and Currencies group.

FIGURE 59

VALUE OF THE PRIVATE EQUITY GROUP'S INVESTMENTS

(in billions of dollars)



N.B.: Non-consolidated and before derivative financial instruments.

FIGURE 60

ABSOLUTE RISK – PRIVATE EQUITY

(for 2008 – in basis points)

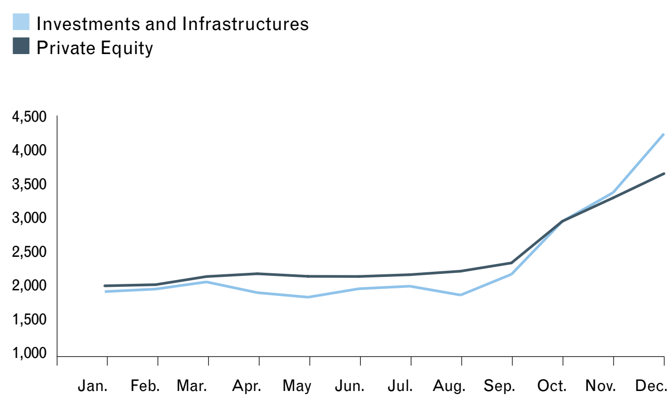


FIGURE 61

CATEGORY BREAKDOWN – INVESTMENTS AND INFRASTRUCTURES

(percentage of fair value as at December 31, 2008)

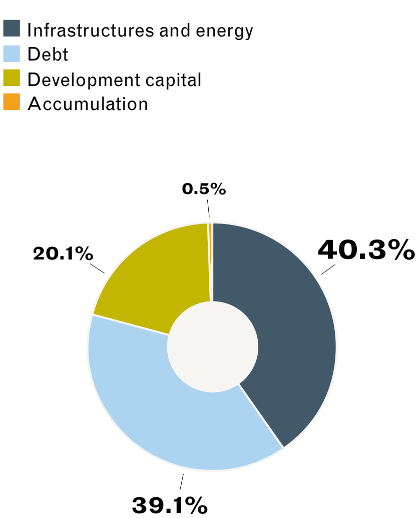
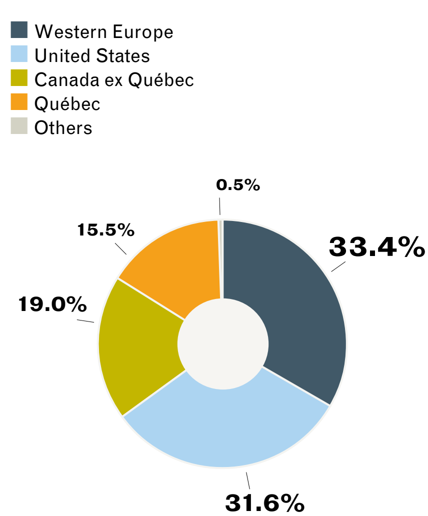


FIGURE 62

GEOGRAPHIC BREAKDOWN[1] – INVESTMENTS AND INFRASTRUCTURES

(percentage of fair value as at December 31, 2008)



1 Based on region of activity.

As at December 31, 2008, depositors' net assets in the Investments and Infrastructures portfolio and the Private Equity portfolio totalled $14.0 billion (table 58), down $3.8 billion from 2007.

Depositors' total assets amounted to $24.3 billion and property under management or administration, $0.8 billion. The group's total assets under management amounted to $25.1 billion at year-end.

As shown by figure 59, the fair value of the group's investments was $23.1 billion as at December 31, 2008, down $2.5 billion from the previous year. The decline is due to the combined effect of $6.3 billion of acquisitions, $3.3 billion of dispositions and a $5.5 billion decrease in the value of investments.

Figure 60 shows absolute risk for the Private Equity group. During the year, the absolute risk of the Investments and Infrastructures portfolio and the Private Equity portfolio rose in tandem with the volatility on the global stock markets, taking into account the portfolios' leverage.

SPECIALIZED INVESTMENTS AND INFRASTRUCTURES PORTFOLIO

The Investments and Infrastructures portfolio returned -44.7% in 2008, or 807 b.p. (8.07%) less than its benchmark index. This decline is due mainly to a decrease in the value of the loans because of their having been valued as if they were available for sale as at December 31, 2008 (see "Fair-value valuation of investments" in the section "Analysis of overall return"). Over five years, the average return is -2.1%, or 350 b.p. (3.50%) less than the index. During that period, development capital generated gains while infrastructure subtracted value.

All investment categories contributed to the portfolio's drop in value in 2008. In the case of development capital, the financial services sector recorded the largest losses, followed by the consumer discretionary and materials sectors. In infrastructure, almost all the losses occurred in industrials and energy.

During the year, the managers continued to dispose of listed securities, with sales totalling $1 billion.

As at December 31, 2008, the Investments and Infrastructures portfolio comprised investments in 189 companies and funds. Figures 61 and 62 show the portfolio's breakdown by category and region. The weight of investments in senior debt continued to rise, reaching 39.1% of the portfolio versus 35.4% in 2007. From the geographic standpoint, Canada, the United States and Western Europe have almost equivalent weightings, at 34.5%, 31.6% and 33.4%, respectively. Figure 65 shows the investment breakdown by sector; the industrial sector continues to dominate, followed by energy and utilities.

Lastly, table 63 gives the top 10 investments in the Investments and Infrastructures portfolio in alphabetical order, and table 64, the portfolio's top 10 investments in Québec, also in alphabetical order.

TABLE 63

TOP 10 HOLDINGS – INVESTMENTS AND INFRASTRUCTURES

(as at December 31, 2008)

ACH Limited Partnership
Compagnie Financière Edmond de Rothschild Banque
Enbridge Energy Partners LP
FGP Topco Limited (BAA)
HCA Inc.
Hochtief Airport Capital GmbH
Interconnector UK Ltd.
Kebexa Participations SAS
Noverco Inc. (Gaz Métro)
PNC Financial Services Group Inc.

TABLE 64

TOP 10 QUÉBEC HOLDINGS – INVESTMENTS AND INFRASTRUCTURES

(as at December 31, 2008)

ACH Limited Partnership
AlterInvest Fund II Limited Partnership
AlterInvest Fund Limited Partnership
Cirque du Soleil
Dépan-Escompte Couche-Tard Inc.
Gesca Ltd.
Hewitt Equipment Ltd.
Noverco Inc. (Gaz Métro)
TransForce Inc.
Yellow Pages Income Fund

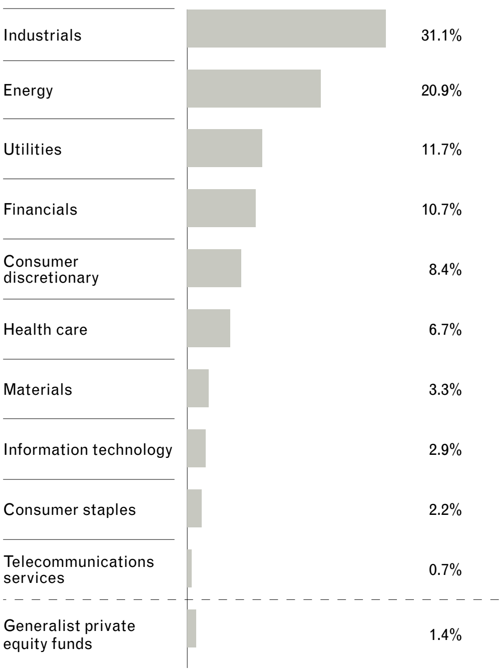
SPECIALIZED PRIVATE EQUITY PORTFOLIO

The Private Equity portfolio returned -31.4% in 2008, outperforming its benchmark index by 872 b.p. (8.72%). Over five years, the average return is positive at 10.6%, for 1,354 b.p. (13.54%) of value added in relation to the index. The gains recorded during that period are due mainly to leveraged buyouts.

After several years of exuberance, the leveraged-buyout market slowed considerably in 2007 as a result of the liquidity crisis and then almost ground to a halt. During the year, the managers concentrated more on distressed loans and restructuring funds.

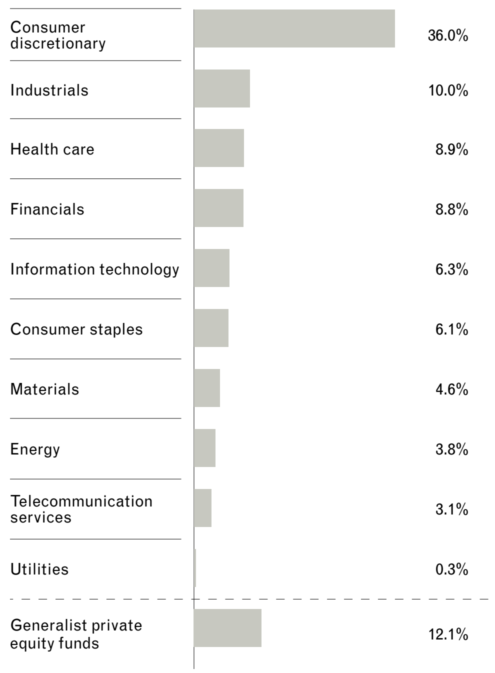
PRIVATE EQUITY

FIGURE 65
SECTOR BREAKDOWN – INVESTMENTS AND INFRASTRUCTURES
(percentage of fair value as at December 31, 2008)



Note: Investments held by generalist private equity funds have been broken down by sector, where possible.

FIGURE 66
SECTOR BREAKDOWN – PRIVATE EQUITY
(percentage of fair value as at December 31, 2008)



Note: Investments held by generalist private equity funds have been broken down by sector, where possible.

FIGURE 67
CATEGORY BREAKDOWN – PRIVATE EQUITY
(percentage of fair value as at December 31, 2008)

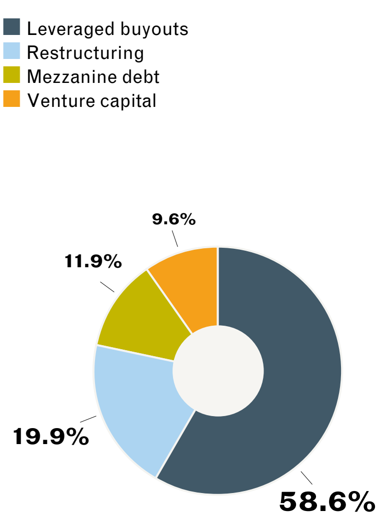
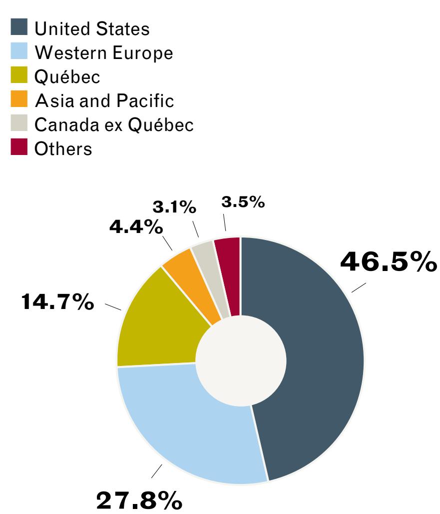


FIGURE 68
GEOGRAPHIC BREAKDOWN[1] – PRIVATE EQUITY
(percentage of fair value as at December 31, 2008)



1 Based on region of activity.

All investment categories were down during the year. Most of the portfolio's loss of value stems from leveraged buyouts. This decline is due mainly to the consumer discretionary, information technology and industrials sectors as well as the generalist funds. Mezzanine debt produced the best results.

The Private Equity portfolio held investments in 332 companies and funds as at December 31, 2008. As figure 67 shows, leveraged buyouts still account for most of the investments, with a weight of 58.6%. In terms of geographic breakdown, investments in foreign companies and funds dominate, with more than 80% of the total (figure 68). The consumer discretionary sector continues to represent the highest investment value (figure 66).

Tables 69 and 70 give the Private Equity portfolio's top 10 investments and top 10 investments in Québec, respectively, in alphabetical order.

TABLE 69

TOP 10 HOLDINGS – PRIVATE EQUITY

(as at December 31, 2008)

Avenue-CDP Global Opportunities Fund LP
Cerberus Institutional Partners LP (Series Four)
CVI Global Value Fund LP
European Directories SA
ILM Investments LP
OCM Opportunities Fund VII (Cayman) Ltd.
OCM Opportunities Fund VIIb LP
Park Square Capital Partners LP
PRA International
Quebecor Media Inc.

TABLE 70

TOP 10 QUÉBEC HOLDINGS – PRIVATE EQUITY

(as at December 31, 2008)

Camoplast Inc.
Capimont Technologies Limited Partnership
Cari-All Group Inc.
GeminX Biotechnologies Inc.
J.A. Bombardier (J.A.B.) Inc.
Novacap II Limited Partnership
Propulsion Ventures III S.E.C. Fund
Quebecor Media Inc.
T2C2 / Bio 2000 Limited Partnership
ViroChem Pharma Inc.

REAL ESTATE

INVESTMENT PHILOSOPHY

TO ACHIEVE ITS TARGET RETURNS, THE REAL ESTATE GROUP FAVOURS:

- Active management to create value with asset turnover and arbitrage between markets, holding vehicles and products according to the position in the real estate cycle;
- Partnership strategies to secure expertise on local markets, act on opportunities more effectively and reduce risk;
- Rigorous management of leverage and concentration risks for optimal profitability; and
- Expansion of its operations in emerging markets with a long-term horizon.

TABLE 71

SPECIALIZED PORTFOLIO MANAGEMENT BY THE REAL ESTATE GROUP

(as at December 31, 2008)

Specialized portfolio	Real Estate		Real Estate Debt
Investment categories	Investment Asset and portfolio management, financial engineering Development and construction Building operation Advisory services		Real estate financing Origination, underwriting, closing and servicing of real estate loans Securitization and issuance of real estate financing products Investment
Management type	Active internal and partnership		Active internal and partnership
Management approach	Discretionary		Discretionary
Main management styles and investment strategies	Conventional and prestige investments	Opportunistic investments	Underwriting of real estate financing Purchase of securities
Main analytical approach	Top-down and bottom-up	Top-down and bottom-up	Top-down and bottom-up
Investment horizon	More than 5 years	Less than 3 years	1 to 10 years

REAL ESTATE

During the year, the Real Estate group was hindered by the credit crunch, the economic slowdown and rising capitalization rates. The market value of its investments fell considerably, but the decline was partly offset by cash flow from operations totalling a record $1.5 billion. The group therefore had a positive year from the operating standpoint, as a result of its high-quality properties and loans. After a moderately active start to the year, the real estate market went into the doldrums. Transaction volume declined significantly to $9.8 billion. The portfolios have an overall return of -16.1% for 2008 and underperformed the benchmark index by 1,352 b.p. (13.52%).

HIGHLIGHTS

SPECIALIZED REAL ESTATE DEBT PORTFOLIO

/ Transaction volume totalled $3.2 billion in 2008, or about one-third of the level reached the previous year.

/ The managers concluded major transactions on various markets, including:

- A $140-million term loan with the Homburg real estate fund for the refinancing of Place Alexis Nihon in Montréal; and
- A $142-million term loan to Delcon Development Group for the construction of an Edmonton shopping centre.

/ The Real Estate group created Otera Capital to bring together management of all its commercial real estate financing operations under one roof. The new subsidiary offers underwriting, credit and asset management services in Canada and elsewhere.

SPECIALIZED REAL ESTATE PORTFOLIO

/ In a difficult economic environment, transaction volume was down by almost 40%, going from $10.8 billion in 2007 to $6.6 billion in 2008.

/ Most of the acquisitions took place at the start of the year as a result of commitments made in 2007. For example, the group made substantial investments in the Lone Star funds. Development projects in France, Germany and Spain were also completed.

/ Taking advantage of favourable conditions in the first half, the Real Estate group carried out dispositions totalling almost $2 billion, mainly office buildings in Montréal, Toronto, Western Canada and New York, as well as three hotels in Canada.

/ The Real Estate group continued its strategy of expanding in emerging markets, with several partnership acquisitions in Brazil, Russia, India and Mexico. The group also established a presence in India and stepped up its activities in China.

The difficult economic context will continue to put downward pressure on valuations in 2009. Caution will be the watchword, and the managers will focus on existing investments, aiming to control operating costs and to maintain occupancy rates. Attractive arbitrage opportunities should arise, especially in listed real estate securities, but the group will have limited leeway because the real estate sector has an overweight position in the Caisse's overall portfolio. To remedy this situation, the group will consider ways to free capital and to diversify its sources of funds. Lastly, the group will continue its long-term strategy of expanding its operations in emerging markets.

REAL ESTATE

TWO SPECIALIZED PORTFOLIOS: REAL ESTATE AND REAL ESTATE DEBT

The Real Estate group invests in equity and financing products in the office and business park, retail, hotel and residential sectors in the Americas, Europe and Asia. The group co-ordinates the operations of its Cadim division and its subsidiaries, Ivanhoe Cambridge, Otera Capital and SITQ, whose holdings are divided into two specialized portfolios: Real Estate and Real Estate Debt.

DIVISION AND MAIN SUBSIDIARIES

CADIM is involved in real estate investment management in Canada, the United States, Europe and Asia. Its investments include opportunistic products that are usually held for less than three years, as well as hotels and multiresidential buildings. It had $18.2 billion of total assets under management as at December 31, 2008. Cadim is a division of the Caisse.

IVANHOE CAMBRIDGE owns, manages, develops and invests in shopping centres in urban areas of Canada, the United States, Brazil, Europe and Asia. It owns about 80 shopping centres outright or in partnership, for total leasable area of more than 4.6 million square metres. Ivanhoe Cambridge had $17.9 billion of total assets under management at year-end. The Caisse has a 93.7% stake in Ivanhoe Cambridge, with the remainder held by four Canadian pension funds.

OTERA CAPITAL is active in commercial real estate financing in Canada, the United States and Europe. Its financing services include underwriting, active management, syndication and securitization, and it offers a wide range of products extending from conventional mortgage loans to structured products. Otera Capital is a subsidiary of the Caisse, which has a 99.2% stake. It had $25.8 billion of assets under management.

SITQ develops, invests in and manages office buildings and business parks owned outright or in partnership. Its portfolio consists of more than 120 properties in large urban centres of Canada, the United States, France, the United Kingdom and Germany, for more than 3.6 million square metres of leasable area. It had $15.8 billion of total assets under management as at December 31, 2008. The Caisse owns 91.6% of SITQ, with the remainder held by five Canadian pension funds.

OTHER SUBSIDIARIES AND AFFILIATES

CANADA

AXIMA SERVICES specializes in technical management of office buildings. Its operations take in more than 2.3 million square metres in Québec. The interest in this company was sold in February 2009.

MAESTRO is a real estate asset manager that specializes in residences for seniors and students. It has $1.2 billion of assets under management.

MCAP manages real estate debt in four main sectors: residential and commercial mortgages, construction loans and equipment leasing. It has $2.4 billion of assets under management or administration. MCAP transferred a portion of its assets under management or administration to Otera Capital in 2008, namely commercial and construction loans with a value of $8 billion.

PRESIMA manages an international portfolio of publicly traded real estate securities. It has $0.5 billion of assets under management.

UNITED STATES

CWCAPITAL manages real estate debt in all sectors of the industry. It has $11.1 billion of assets under management or administration.

THE PRAEDIUM GROUP is a real estate asset manager that specializes in mid-sized unproductive and undervalued assets. It has $3.7 billion of assets under management.

EUROPE

SIMON IVANHOE is a shopping centre developer, owner and manager with $1.2 billion of assets under management or administration.

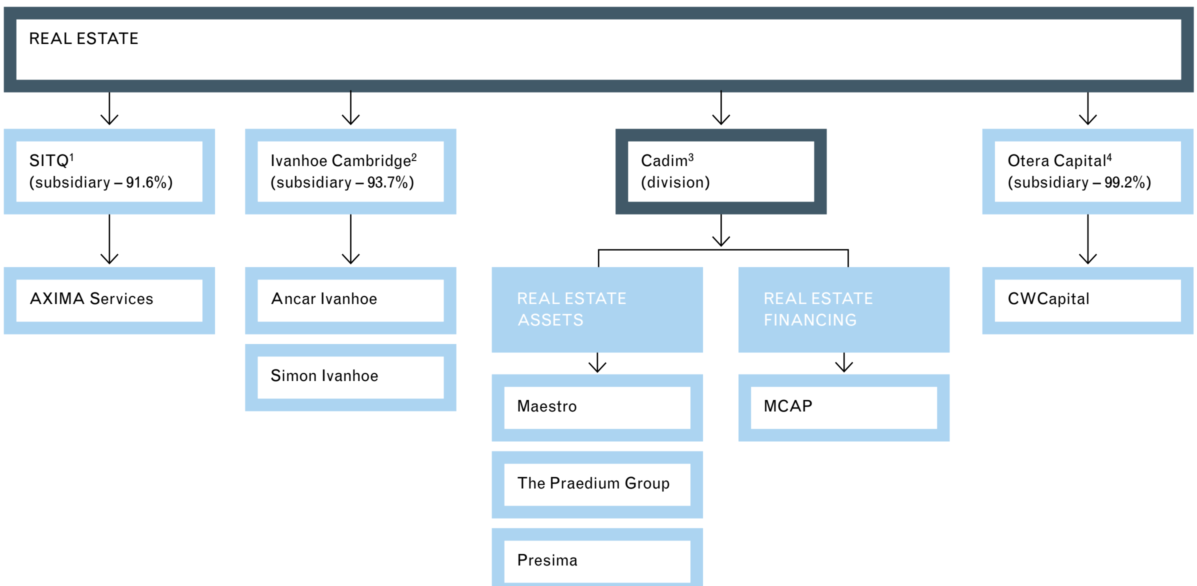
BRAZIL

ANCAR IVANHOE is a shopping centre developer, owner and manager with $1.2 billion of assets under management or administration.

FIGURE 72

ORGANIZATION CHART – REAL ESTATE

(as at December 31, 2008)



1 Paul D. Campbell
President and Chief Executive Officer
SITQ

2 René Tremblay
President and Chief Executive Officer
Ivanhoe Cambridge

3 Richard Dansereau
President and Chief Operating Officer
Cadim

4 Jean Lamothe
President and Chief Executive Officer
Otera Capital

REAL ESTATE

OVERALL RETURN AND SPECIALIZED PORTFOLIO ANALYSIS

The portfolios earned an overall return of -16.1% in 2008, or 1,352 b.p. (13.52%) less than the benchmark index. After a moderately active start to the year, the commercial real estate market went into the doldrums. The credit crunch and the economic slowdown curtailed transactions, and investment volumes fell considerably in all regions of the world. The widespread increase in capitalization rates reduced the valuations of the Caisse's properties in all its markets.

It should be noted that the Caisse's real estate assets continue to enjoy substantial cash flow from operations, owing to the high quality of the properties and loans. Most of the Caisse's properties are class-A buildings that tend to attract quality tenants. The occupation rate is at a historically high level of about 95%, and rents held steady throughout 2008. In the same vein, loans were provided for certain quality buildings. Even so, cash flow from operations was not enough to offset the lower fair values. These decreases in value are unrealized losses, however, and the valuations should recover in the years to come.

The details of the portfolios' returns for one year, three years and five years are given in table 74.

The Real Estate group had $25.4 billion of depositors' net assets under management as at December 31, 2008, with $11.3 billion in the Real Estate Debt portfolio and $14.1 billion in the Real Estate portfolio. Table 75 gives the breakdown of the Real Estate group's total assets under management.

The Real Estate group's transaction volume decreased significantly during the year, falling to $9.8 billion, with $3.4 billion of acquisitions and investments, $1.3 billion of leasehold improvements, construction and renovation projects, $1.9 billion of sales and $3.2 billion of real estate financing transactions.

Figure 73 shows the absolute risk for the Real Estate group. Both portfolios were affected by the increase in market volatility, especially in the fourth quarter. The significant use of leverage accentuated this effect in the Real Estate portfolio. As for the Real Estate Debt portfolio, the revaluation of high-yield debt securities reduced the absolute risk toward year-end.

FIGURE 73

ABSOLUTE RISK – REAL ESTATE

(for 2008 – in basis points)

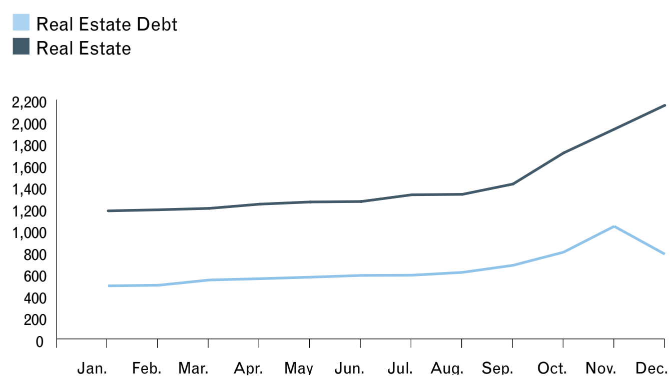


TABLE 74

SPECIALIZED PORTFOLIO RETURNS – REAL ESTATE

(for periods ended December 31, 2008)

	1 year			3 years				5 years			
	Return %	Index[1] %	**Spread b.p.**	Return %	Index[1] %	**Spread b.p.**	Information ratio	Return %	Index[1] %	**Spread b.p.**	Information ratio
Real Estate Debt	(7.6)	(3.0)	**(460)**	(0.2)	1.8	**(205)**	(0.6)	4.3	3.8	**49**	0.2
Real Estate	(21.9)	(3.4)	**(1,851)**	7.0	15.1	**(813)**	–	17.0	19.0	**(195)**	–

1 The description of the indexes is given in the "General notes."

AON – REAL ESTATE INDEX

The benchmark for the Real Estate portfolio is the Aon – Real Estate Index. The index consists of the IDP Canada Annual Property Index (70%) and, for the United States, the hedged NCREIF Property Index (30%), to which 40% leverage is applied. The real estate in the index has to be appraised once a year, but it is not necessary to do so as at December 31 or to use independent chartered appraisers.

The Real Estate portfolio, however, has a geographic composition and a range of products that are very different from the index, as well as a greater degree of leverage. Moreover, all the properties in the portfolio are valued by external independent chartered appraisers as at December 31, 2008.

SPECIALIZED REAL ESTATE DEBT PORTFOLIO

The Real Estate Debt portfolio returned -7.6% in 2008, underperforming its benchmark index by 460 b.p. (4.60%). Over five years, the portfolio has an appreciable average annual return of 4.3% and exceeds the index by 49 b.p. (0.49%).

Generally speaking, the portfolio's level of activity was moderate in 2008. Transaction volume fell as the managers adjusted their investment criteria to the new market conditions, especially in the United States. Interest income and principal repayment remained solid, owing to the quality of the loan portfolio. First-mortgage loans fared better than subordinated loans. Delinquency, default and loss rates were slightly up, in line with forecasts.

TABLE 75

TOTAL ASSETS UNDER MANAGEMENT – REAL ESTATE

(fair value as at December 31, 2008 – in billions of dollars)

	Depositors' net assets	Depositors' total assets	Assets under management or under administration	Total assets under management	
Otera Capital	11.3	13.6	12.2	25.8	33.2%
Real Estate Debt portfolio	**11.3**	**13.6**	**12.2**	**25.8**	**33.2%**
SITQ		11.6	4.2	15.8	20.3%
Ivanhoe Cambridge		12.9	5.0	17.9	23.0%
Cadim		7.0	11.2	18.2	23.5%
Real Estate portfolio	**14.1**	**31.5**	**20.4**	**51.9**	**66.8%**
Total	**25.4**	**45.1**	**32.6**	**77.7**	**100.0%**

REAL ESTATE

The substantial devaluations recorded during the year limited the portfolio's growth, however. Widening credit spreads caused the fair value of loans to drop, especially in the case of structured products.

Depositors' net assets in the portfolio amounted to $11.3 billion as at December 31, 2008, a decrease of $0.2 billion from the previous year.

The loans provided during the year ranged from $24,000 to $141 million, and transactions totalled $3.2 billion. Figures 78 and 79 show the portfolio's sector and geographic breakdowns at year-end.

Tables 76 and 77 give the portfolio's top 10 loans and top 10 Québec loans, respectively, in alphabetical order.

TABLE 76

TOP 10 LOANS – REAL ESTATE DEBT

(as at December 31, 2008)

299 Burrard Management Ltd. (Westbank and Peterson Group)
BRE / Hospitality Europe Holding BV
Legacy Hotels REIT
Maui Beach Resort LP
PCV ST MEZZ 10 LP
SCG/CLP Holdings LP, SCG Hotel CLP LP
Star GT Acquisition SAS
The Pointe at Balboa LP
Tour de la Bourse SPE inc.
TRZ Mezz 4 LLC, TRZ CN Mezz 4A LP (Trizec Properties)

TABLE 77

TOP 10 QUÉBEC LOANS – REAL ESTATE DEBT

(as at December 31, 2008)

1200 McGill College Inc.
9170-4767 Québec inc.
CDM de Montréal-1 inc.
Fiducie Darion
Fonds Immobilier Homburg
FPI Cominar (1)
FPI Cominar (2)
Montez (Victoriaville) inc., Montez Retail Fund Inc. and Société immobilière Sym inc.
Place du Royaume inc.
Tour de la Bourse SPE inc.

FIGURE 78

SECTOR BREAKDOWN – REAL ESTATE DEBT

(in percentage of fair value as at December 31, 2008)

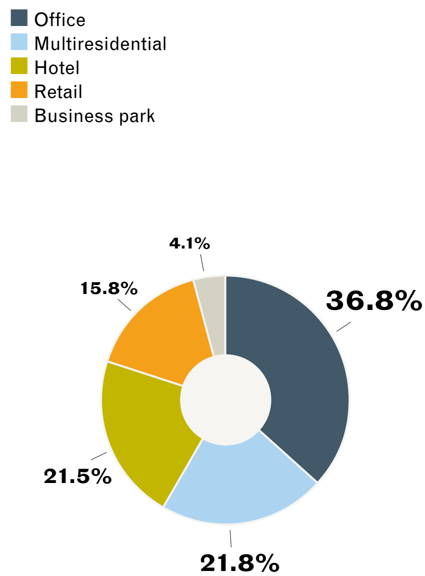
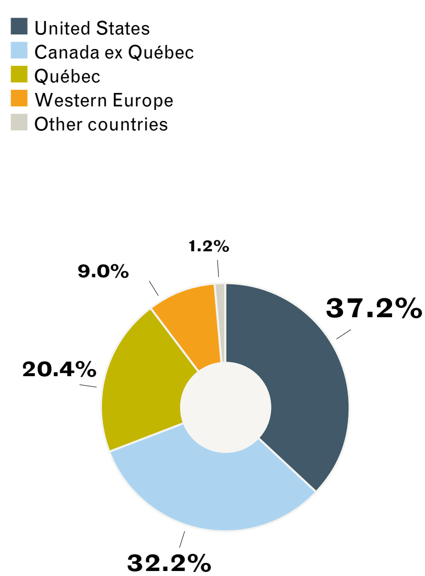


FIGURE 79

GEOGRAPHIC BREAKDOWN – REAL ESTATE DEBT

(in percentage of fair value as at December 31, 2008)



SPECIALIZED REAL ESTATE PORTFOLIO

The Real Estate portfolio in 2008 returned -21.9%, underperforming the benchmark index by 1,851 b.p. (18.51%). Over five years, the average annual return is 17.0%, or 195 b.p. (1.95%) less than the benchmark.

During the year, tight credit conditions curtailed commercial real estate transactions, and investment volumes fell considerably around the world. The widespread increases in capitalization rates for all types of property in all regions hit the portfolio hard, and the three real estate units saw the fair value of their investments decrease significantly. The decreases in value are unrealized losses, however.

Cadim also saw the fair value of its investments in the hotel sector fall substantially. Moreover, its investments in publicly traded real estate securities and the Lone Star funds produced poor returns.

Investments in shopping centres also suffered as a result of rising capitalization rates. Ivanhoe Cambridge recorded substantial decreases in value, especially in the United Kingdom and Spain.

The situation is essentially the same for office buildings. SITQ's properties in Washington, Paris and London were especially affected.

The portfolio's cash flow from operations exceeded that of the previous year, however, owing to the quality of the properties and the tenants on all markets. Occupancy rates stayed high and rents held steady, especially for office buildings and shopping centres.

As at December 31, 2008, depositors' net assets in the portfolio totalled $14.1 billion, down $3.5 billion from the previous year.

In the shopping centre sector, Ivanhoe Cambridge's transactions totalled $1.8 billion in 2008, with $1.1 billion of acquisitions and $0.7 billion of leasehold improvements, construction and renovation projects.

In the office building and business park sector, acquisitions totalled $0.3 billion, with $1.2 billion of sales and $0.3 billion of leasehold improvements, construction and renovation projects, bringing SITQ's total transactions to $1.8 billion.

Lastly, in opportunistic products, hotels and multiresidential buildings, Cadim's transactions totalled $3.0 billion, including $2.0 billion of acquisitions, $0.7 billion of sales and $0.3 billion of leasehold improvements, construction and renovation projects.

Figures 80 and 81 give the sector and geographic breakdowns at year-end. The proportion of investments in Canada decreased in favour of the United States and emerging markets in 2008.

FIGURE 80

SECTOR BREAKDOWN – REAL ESTATE

(in percentage of fair value as at December 31, 2008)

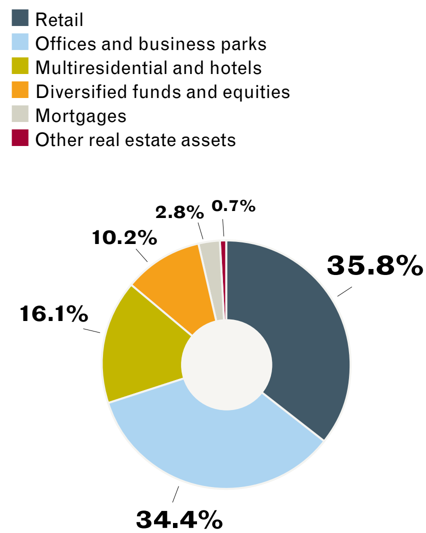
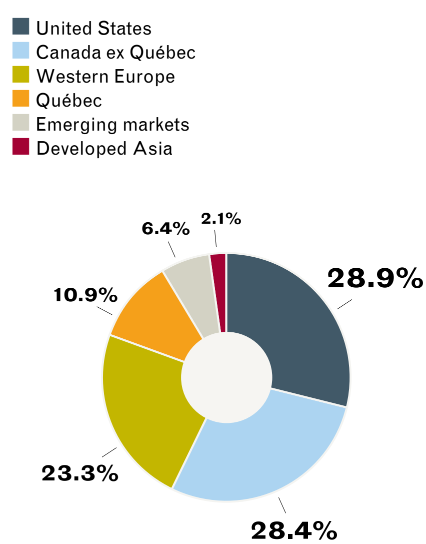


FIGURE 81

GEOGRAPHIC BREAKDOWN – REAL ESTATE

(in percentage of fair value as at December 31, 2008)



REAL ESTATE

Table 82 gives the portfolio's top 10 investments in the world in alphabetical order. The Real Estate group is also very active on markets close to home and owns many prestigious buildings in Québec. Table 83 gives the portfolio's top 10 investments in Québec in alphabetical order.

TABLE 82

TOP 10 INVESTMENTS – REAL ESTATE

(as at December 31, 2008)

Investment	Subsidiary or division	Leasable area (in thousands of m^2)	Ownership (%)
11-13 Theresienhöhe, Munich, Germany	SITQ	58.7	100.0
388-390 Greenwich Street, New York, United States	SITQ	244.8	49.4
1515 Broadway, New York, United States	SITQ	150.5	45.0
Lone Star (Asia, Europe and North America funds)	Cadim	–	–
Madrid Xanadú, Madrid, Spain	Ivanhoe Cambridge	93.5	100.0
Metropolis at Metrotown, Burnaby, British Columbia	Ivanhoe Cambridge	223.1	100.0
Newport Corporate Center, Seattle, United States	SITQ	83.1	100.0
St. Enoch Shopping Centre, Glasgow, United Kingdom	Ivanhoe Cambridge	71.0	100.0
Tour T1, Paris, France	SITQ	61.5	100.0
Vaughan Mills, Vaughan, Ontario	Ivanhoe Cambridge	104.0	100.0

TABLE 83

TOP 10 QUÉBEC INVESTMENTS – REAL ESTATE

(as at December 31, 2008)

Investment	Subsidiary or division	Leasable area (in thousands of m^2)	Ownership (%)
1000 De La Gauchetière Ouest, Montréal	SITQ	85.2	100.0
Centre CDP Capital, Montréal	SITQ	52.9	100.0
Fairview Pointe-Claire, Montréal	Ivanhoe Cambridge	91.1	50.0
Galeries d'Anjou, Montréal	Ivanhoe Cambridge	111.4	50.0
Laurier Québec, Québec City	Ivanhoe Cambridge	54.5	50.0
Les Rivières, Trois-Rivières	Ivanhoe Cambridge	51.7	85.0
Montréal Eaton Centre, Montréal	Ivanhoe Cambridge	26.9	100.0
Place Ville Marie, Montréal	SITQ	239.2	50.0
Rockland, Montréal	Ivanhoe Cambridge	61.0	100.0
World Trade Centre Montréal, Montréal	SITQ	52.6	100.0

ANALYSIS OF COMBINED FINANCIAL STATEMENTS

The financial statements of the Caisse de dépôt et placement du Québec are combined, which means they include the accounts of the Caisse's subsidiaries, the General Fund, the Individual Funds and the specialized portfolios. Depositors' holdings presented in the combined statement of net assets reflect the combination of the net account value of each Caisse depositor.

The combined financial statements are prepared according to generally accepted accounting principles in Canada, as provided for by the *Act respecting the Caisse de dépôt et placement du Québec*.

As required by law, the Auditor General of Québec audited the Caisse's books in 2008, and his report accompanies the combined financial statements. Over all, the Auditor General reports on 53 financial statements, namely the Caisse's combined statements and those of the General Fund, the depositors' 33 individual funds and the 18 specialized portfolios. He has issued unqualified opinions for all the financial statements.

CHANGEOVER TO INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS)

Canada's Accounting Standards Board (AcSB) confirmed on February 13, 2008, that publicly accountable enterprises would be obliged to apply the International Financial Reporting Standards (IFRS) in place of generally accepted accounting principles (GAAP), starting on January 1, 2011. The AcSB also ruled that the enterprises will have to provide comparative information according to the IFRS one year before the changeover.

The Caisse intends to adopt the IFRS for the preparation and presentation of its combined financial statements and other financial statements as necessary. It plans to report according to the rules in effect as of January 1, 2011. To that end, the Caisse began to put in place an IFRS adoption program in July 2008. This structured program involves various Caisse teams, the use of outside advisers, employee training and disclosure of the results and the impacts of the work to the interested parties.

The Caisse's transition to the IFRS standards will take place in three stages: detailed diagnostics, detailed planning and implementation.

STAGE 1: DETAILED DIAGNOSTICS

This stage, completed in the fall of 2008, involved a comparative analysis of GAAP and the IFRS standards to determine the main choices available to the Caisse. For the time being, the main differences identified concern recording of financial instruments, account consolidation and preparation of financial statements.

STAGE 2: DETAILED PLANNING

The information derived from the diagnostics was used to structure and to document a detailed plan that will serve as the framework for a harmonious changeover to the new standards. This stage identified the main challenges and issues, as well as each team's responsibilities.

STAGE 3: IMPLEMENTATION

This stage involves mobilizing, co-ordinating and overseeing the various teams to ensure implementation according to expectations and deadlines. The changes will affect accounting, business and internal control procedures as well as financial and management reports. Implementation has already begun and will continue over the next two years.

The IFRS standards transition program is taking place according to the established plan.

ADOPTION OF NEW ACCOUNTING STANDARDS IN 2008

On January 1, 2008, the Caisse adopted the provisions of Section 3862, "Financial Instruments – Disclosures," and Section 3863, "Financial Instruments – Presentation." These sections replace Section 3861, "Financial Instruments – Disclosure and Presentation." They change the presentation requirements for notes to financial statements, placing greater emphasis on information to be provided on the nature and scope of the risks associated with financial instruments and the way the entity manages these risks.

ANALYSIS OF COMBINED FINANCIAL STATEMENTS

FAIR VALUE OF INVESTMENTS

According to the provisions of accounting guideline no. 18 of the Canadian Institute of Chartered Accountants (CICA), the Caisse must establish the fair value of its investments as at the date of the preparation of the financial statements on the assumption that they are available for sale. This restrictive standard does not take into account the fact that, given the long investment horizon of its main depositors, the Caisse has investments that it has the means and the intention to hold until their optimal value is reached.

In normal circumstances, this fair-value, or mark-to-market, rule does not pose any problems, since all financial markets are active, and investment values can be based on actual transactions involving comparable assets on various markets. When the markets are disrupted, however, and no purchases or sales are taking place, fair value has to be established on a mark-to-model basis whose parameters, particularly financing and illiquidity premiums, involve a high degree of subjectivity from one organization to another or one valuation professional to another. As at December 31, 2008, inactivity on various financial markets, including real estate debt, private equity, infrastructure, corporate bonds and real estate, combined with abnormally high financing costs, obliged investors to use valuation models and parameters that gave rise to unrealized decreases in value reflecting the extreme volatility of the financial markets as at that date.

The financial crisis of 2008 prompted Canadian and international authorities to adopt measures to resolve the financial information problems created by the extreme volatility on the financial markets. These new standards were approved by AcSB in November 2008 and include reclassification of financial assets, including a changeover from the categories "held for trading purposes" or "available for sale" to the category "held to maturity." Unlike Canadian financial institutions, investment companies, including the Caisse, may not avail themselves of these new provisions. On October 22, 2008, the Caisse wrote to the AcSB to propose that special measures, similar to those that other Canadian financial institutions are allowed to use, be adopted for investment companies. The AcSB did not accede to the Caisse's request.

In establishing the fair value of its investments, the Caisse uses quoted market prices, independent evaluators who are highly regarded in their markets or evaluation committees consisting of independent experts. In addition, the external auditors of the real estate entities (for real estate investments) and the Auditor General of Québec (for all the Caisse's investments) review the valuation work done by the Caisse, the independent valuation professionals and the valuation committees. The valuation methods used for the Caisse's investments are described in detail in the section "Analysis of overall return."

NET ASSETS AND DEPOSITORS' TOTAL ASSETS

The net assets of the Caisse's depositors totalled $120.1 billion as at December 31, 2008, a decrease of $35.3 billion in relation to 2007. This decline is due to net investment results of -$39.8 billion and depositors' net contributions totalling $4.6 billion. In 2007, the increase was $11.9 billion, with $7.9 billion due to net investment results and $4.0 billion to depositors' net contributions.

Depositors' total assets amounted to $186.9 billion in 2008 compared with $227.1 billion in 2007, a decrease of $40.2 billion. Total assets include $66.8 billion of liabilities in 2008 versus $71.7 billion in 2007. The liabilities, which include securities lending, short selling of securities, mortgage loans and the financing programs of the subsidiary CDP Financial, essentially finance the purchase of investments.

NET INVESTMENT RESULTS

Net investment results for 2008 had an unfavourable effect of $39.8 billion compared with a favourable effect of $7.9 billion in 2007 (figure 84). The net effect of -$39.8 billion in 2008 is due to four sources:

/ Investment income totalling $5.8 billion (mainly interest income, dividends, fees and rents), net of operating expenses and external management fees;

/ The net impact of gains or losses on the sale of investments totalling -$23.2 billion;

/ The net impact of increases or decreases in the fair value of the investments and liabilities related to the investments that the Caisse held as at December 31, 2008, totalling -$19.0 billion; and

/ The impact of third-party and bank-sponsored ABCP, net of back interest, totalling -$3.4 billion.

Investment income totalled $6.2 billion in 2008, versus $6.5 billion in 2007. If operating expenses and external management fees are excluded, net income totalled $5.8 billion in 2008 and $6.2 billion in 2007. Investment income came from fixed-income securities ($3.7 billion in 2008 and $3.7 billion in 2007) and variable-income securities ($2.5 billion in 2008 versus $2.8 billion in 2007). The differences between 2008 and 2007 are due mainly to the lower average investment volume and lower interest rates.

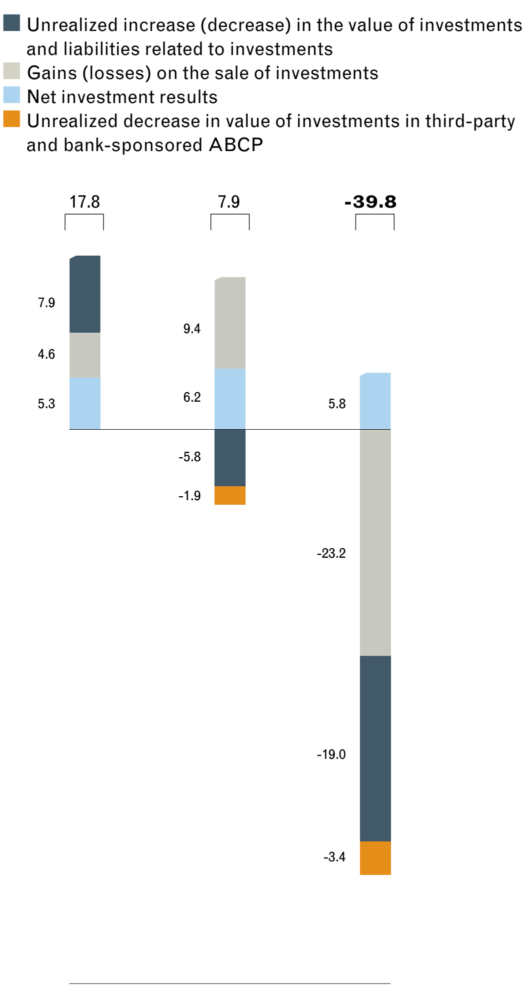
Net losses on the sale of investments totalled $23.2 billion in 2008, or a loss of $23.3 billion for variable-income securities, a gain of $0.2 billion for fixed-income securities and transaction costs totalling $0.1 billion. Net gains totalled $9.4 billion in 2007, or $9.1 billion for variable-income securities and $0.3 billion for fixed-income securities. For more information, see note 6d of the combined financial statements.

The net unrealized decrease in the value of investments totalled $22.4 billion in 2008, including a $3.4-billion unrealized decrease in the value of third-party and bank-sponsored ABCP, net of back interest. The unrealized decrease in the value of investments (excluding third-party and bank-sponsored ABCP) was $19.0 billion in 2008, namely a decrease of $14.2 billion for variable-income securities and $4.8 billion for fixed-income securities, including liabilities related to investments. In 2007, the net unrealized decrease in the value of investments was $5.8 billion, including $4.0 billion for variable-income securities and $1.8 billion for fixed-income securities, including liabilities related to investments.

FIGURE 84

CHANGES IN NET INVESTMENT RESULTS

(for periods ended December 31 – in billions of dollars)



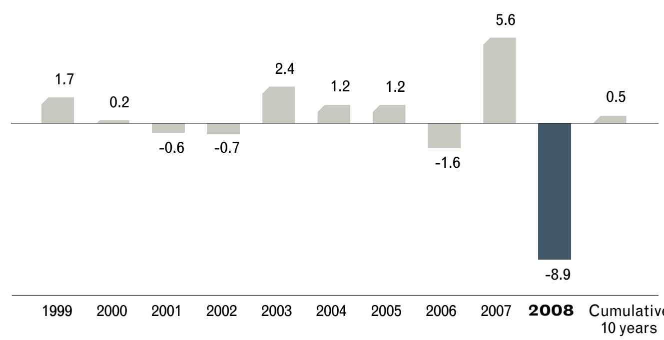
IMPACT OF FOREIGN EXCHANGE HEDGING

In 2008, the hedging policy made a negative contribution of $8.9 billion to the net investment results, whereas in 2007 it made a positive contribution of $5.6 billion. Over 10 years, the Caisse's hedging policy has given rise to a cumulative net gain of $0.5 billion (figure 85).

FIGURE 85

IMPACT OF CURRENCY HEDGING OVER 10 YEARS

(in billions of dollars)



ANALYSIS OF OPERATING EXPENSES AND EXTERNAL MANAGEMENT FEES

The Caisse's operating expenses represent all costs incurred to manage and administer the portfolio, with the exception of external management fees. Operating expenses are presented in a separate item of the combined statement of income and changes in net assets. Expenses related to management of the Real Estate portfolio and the Real Estate Debt portfolio are included in operating expenses. Operating expenses related to management and administration of real estate assets and mortgages are deducted from real estate investment income and mortgage income, respectively.

Operating expenses totalled $263 million in 2008, or substantially the same level as in 2007, when they amounted to $261 million.

External management fees represent amounts paid to external financial institutions, mainly institutional fund managers specializing in international equities, to manage, on behalf of the Caisse, funds belonging to the Caisse. External management fees are presented in a separate item of the combined statement of income and changes in net assets.

External management fees totalled $51 million in 2008 versus $69 million in 2007. The decrease is due mainly to a decline in the value of assets.

OPERATIONAL EFFICIENCY

The Caisse periodically reviews its procedures to maintain strict control over its operating expenses. Its objective is to keep operating expenses at a level that, taking into account the composition of its investments, is comparable to that of institutional fund managers of the same size with similar operations. For many years, the Caisse has taken part in exercises to benchmark its costs per asset class. Generally speaking, these costs compare favourably with those of its peers.

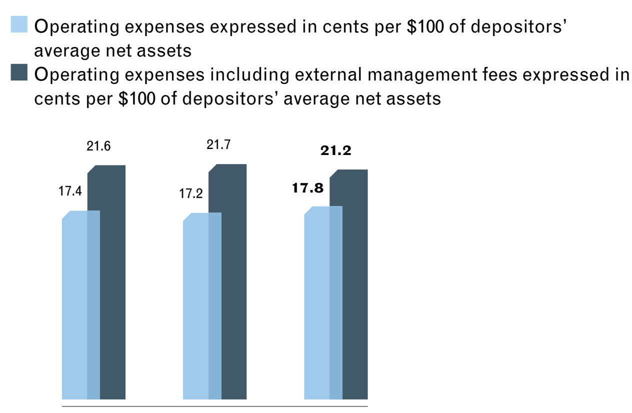
It is common practice for fund managers to express operating expenses in basis points, or the cost in cents to manage $100 of average net assets. Figure 86 shows operating expenses expressed in cents per $100 of depositors' average net assets for 2006, 2007 and 2008. Expressed in this way, the Caisse's operating expenses rose from 17.4 cents in 2006 to 17.8 cents in 2008. This difference is due mainly to the combined effect of the decrease in depositors' average net assets, careful management and tightening of expenses, especially in the fourth quarter of the year.

Together, operating expenses and external management fees, expressed in cents per $100 of depositors' average net assets, fell from 21.6 cents in 2006 to 21.2 cents in 2008.

FIGURE 86

OPERATING EXPENSES AND EXTERNAL MANAGEMENT FEES[1] EXPRESSED IN CENTS PER $100 OF DEPOSITORS' AVERAGE NET ASSETS

(for periods ended December 31)



1 Including external management fees that were previously deducted from investment income. The figures for 2006 have been restated.

Still, this measure is not ideally suited to the Caisse because it manages $186.9 billion of total assets and also manages and administers portfolios of properties totalling $33.5 billion for clients. Thus to monitor operating expenses related to its overall operations, the Caisse expresses its operating expenses as a function of average total assets under management.

Figure 87 shows operating expenses expressed in cents per $100 of average total assets under management for 2006, 2007 and 2008. Expressed in this way, the Caisse's operating expenses increased from 10.0 cents in 2006 to 10.3 cents in 2008. This difference is due mainly to the impact of the decrease in depositors' average net assets in 2008.

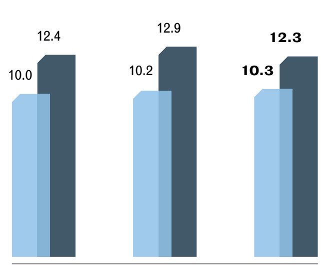
Operating expenses and external management fees expressed in cents per $100 of average total assets under management decreased from 12.4 in 2006 to 12.3 in 2008.

FIGURE 87

OPERATING EXPENSES AND EXTERNAL MANAGEMENT FEES[1] EXPRESSED IN CENTS PER $100 OF AVERAGE TOTAL ASSETS UNDER MANAGEMENT

(for periods ended December 31)

- Operating expenses expressed in cents per $100 of average total assets under management
- Operating expenses including external management fees expressed in cents per $100 of average total assets under management



1 Including external management fees that were previously deducted from investment income. The figures for 2006 have been restated.

CDP FINANCIAL

CDP Financial, a wholly owned subsidiary of the Caisse, began its operations on June 9, 2003, with an initial offering of $3.0 billion of commercial paper.

Its main activity is to carry out borrowing programs on institutional markets in Canada and Europe so as to optimize the financing costs of the Caisse and the companies it controls.

CDP Financial's liabilities, namely the amount of notes outstanding, increased by $3.4 billion during the year, going from $3.3 billion at year-end 2007 to $6.7 billion as at December 31, 2008. Outstanding short-term borrowing totalled $6.4 billion at year-end, while term loans totalled $0.3 billion.

MULTICURRENCY PROGRAM

CDP Financial set up a short-term multicurrency borrowing program on the European market in 2007 to diversify the Caisse's sources of funds and to carry out offerings in several currencies. Offerings totalling almost $1 billion were carried out under this program in 2008.

SHORT-TERM BORROWING

Outstanding short-term borrowing amounted to $6.4 billion as at December 31, 2008, versus $2.0 billion a year earlier. The average maturity in 2008 was 89 days. Annual transaction volume was $16.7 billion, and the average amount outstanding was $3.0 billion. Figure 88 shows that 58.3% of the offerings were purchased in Québec, 35.7% in the other provinces of Canada and 6.0% in Europe.

MEDIUM-TERM BORROWING

CDP Financial did not issue any medium-term notes in 2008. Maturing notes totalling $1.0 billion were reimbursed, leaving $0.3 billion outstanding as at December 31, 2008.

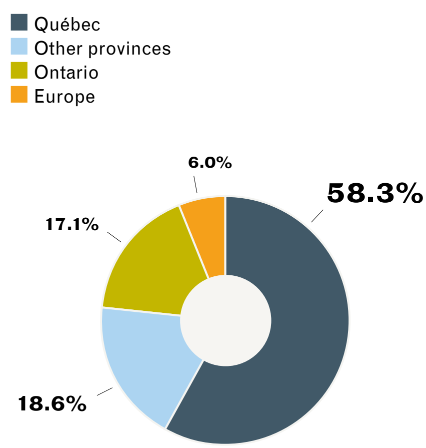
LETTERS OF GUARANTEE

During the year, the subsidiary co-ordinated offerings of letters of guarantee, which provide interim support for certain investment operations. Outstanding letters of guarantee amounted to $87.8 million as at December 31, 2008.

FIGURE 88

GEOGRAPHIC BREAKDOWN OF COMMERCIAL PAPER SALES

(as at December 31, 2008)



CREDIT RATINGS

Dominion Bond Rating Services (DBRS), Moody's Investors Services (Moody's) and Standard & Poor's (S&P) maintained their credit ratings for the Caisse and its subsidiary CDP Financial in 2008, as shown in table 89. These credit ratings are the highest issued by the rating agencies.

TABLE 89

CREDIT RATINGS

	Short-term	Long-term
DBRS[1]	R-1 (high)	AAA
Moody's[2]	Prime-1 (Aaa)	Aaa
S&P[3]	A-1 + A-1 (high)	AAA

1 On February 25, 2009, DBRS published an update that confirmed the Caisse's current credit ratings.

2 On March 6, 2009, Moody's confirmed the short- and long-term credit ratings of CDP Financial and maintained a "stable" outlook.

3 On February 26, 2009, S&P placed the Caisse's AAA long-term issuer credit rating on "credit watch negative" for three months. At the time of printing, no decision had been made.

COMBINED FINANCIAL STATEMENTS

MANAGEMENT'S RESPONSIBILITY FOR COMBINED FINANCIAL REPORTING

Preparation and presentation of the combined financial statements of the Caisse de dépôt et placement du Québec (the "Caisse") are the responsibility of management. The combined financial statements were prepared in accordance with generally accepted accounting principles (GAAP) in Canada. We ensure that the financial data in the Annual Report are consistent with those in the combined financial statements.

The combined financial statements include amounts based on management's best estimates and judgment, with due regard for their relative importance. Moreover, in the preparation of the financial data, management has made decisions regarding the information to be presented, has made estimates and has made assumptions that affect the information presented. Future results may differ considerably from our current estimates, because of changes in the financial markets or other events that may have an impact on the fair value of the investments established as at December 31, 2008.

In our responsibility for the reliability of financial information, we use a sophisticated internal control mechanism applied systematically on all levels of the organization. This mechanism consists of organizational and operational controls, financial information disclosure controls and procedures, and internal control over financial information. The Caisse's internal control mechanism is based, among other things, on a clear definition of responsibilities, effective allocation of duties, delegation of powers, competent resources, appropriate procedures, information systems, tools and practices, relevant and reliable information whose adequacy enables all employees to fulfill their responsibilities, control, compliance and integrated risk management measures that are proportional to the issues specific to each process and designed to reduce risks likely to affect achievement of the Caisse's objects, and oversight of compliance with an extensive body of internal policies.

This control mechanism makes it possible to ensure that appropriate internal controls are in place as regards operations, assets and records. Moreover, the Caisse's internal audit group reviews the internal controls on a regular basis. These controls and audits are designed to provide reasonable assurance regarding the reliability of the accounting records used to prepare the combined financial statements and to ensure that assets are not used or disposed of in any unauthorized manner, that liabilities are recorded, and that we meet all the legal requirements to which the Caisse is subject, including the *Act respecting the Caisse de dépôt et placement du Québec.*

Each year, we certify that the design of the internal control regarding financial information is sufficient and that the design and functioning of the financial information disclosure controls and procedures are effective. We report any significant irregularity to the Audit Committee of the Board of Directors of the Caisse, as necessary.

The Auditor General of Québec has audited the combined financial statements of the Caisse, and his report covers the nature and scope of the audit and expresses his opinion. The Auditor General has unrestricted access to the Audit Committee to discuss any matter relating to his audit.

The Board of Directors and its committees supervise the manner in which management fulfills its responsibility for the establishment and presentation of financial information, maintenance of appropriate internal controls, compliance with the requirements of laws and regulations, management of and control over the main risks and evaluation of major transactions. Moreover, it approves the combined financial statements and the Annual Report.

The Board of Directors has approved the combined financial statements as at December 31, 2008. It is assisted in its responsibilities by the Audit Committee, of which all members are outside directors. This Committee meets with management and the Auditor General, examines the combined financial statements and recommends their approval to the Board of Directors.

/ **FERNAND PERREAULT**
President and Chief Executive Officer

/ **GHISLAIN PARENT,** FCA
Executive Vice-President, Finance and Operations

Montréal, February 18, 2009

AUDITOR'S REPORT

To the National Assembly

I have audited the combined statement of net assets of the Funds of the Caisse de dépôt et placement du Québec as at December 31, 2008, along with the combined statement of income and changes in net assets for the year then ended. These financial statements are the responsibility of the Caisse's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with generally accepted auditing standards in Canada. These standards require that I plan and perform an audit in such a way as to obtain reasonable assurance that the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall presentation of the financial statements.

In my opinion, these combined financial statements present fairly, in all material respects, the financial position of these Funds as at December 31, 2008, as well as the results of their operations and the changes in their net assets for the year then ended, in accordance with generally accepted accounting principles in Canada. As required by the *Auditor General Act* (R.S.Q., chapter V-5.01), I report that in my opinion these principles have been applied on a consistent basis with that of the preceding year.

/ **RENAUD LACHANCE,** CA auditor
Auditor General of Québec

Québec City, February 18, 2009

COMBINED STATEMENT OF NET ASSETS

As at December 31, 2008

(in millions of dollars)	2008	2007
Assets		
Investments at fair value *(notes 4a and b)*	**182,493**	222,797
Advances to depositors	**754**	372
Investment income, accrued and receivable	**1,394**	1,209
Transactions being settled	**1,241**	1,567
Other assets	**993**	1,204
	186,875	227,149
Liabilities		
Liabilities related to investments *(note 4c)*	**62,612**	66,100
Transactions being settled	**849**	2,087
Other liabilities	**1,511**	1,561
Non-controlling interests *(note 4d)*	**1,815**	2,051
	66,787	71,799
Depositors' holdings *(note 5)*	**120,088**	155,350

Derivative financial instruments *(note 9)*

Commitments and contingencies *(note 11)*

The accompanying notes are an integral part of the combined financial statements.

For the Board of Directors,

/ **FERNAND PERREAULT**

/ **CLAUDE GARCIA**

COMBINED STATEMENT OF INCOME AND CHANGES IN NET ASSETS

for the year ended December 31, 2008

(in millions of dollars)	2008	2007
Investment income *(note 6a)*	**6,161**	6,531
Less:		
Operating expenses *(note 7)*	**263**	261
External management fees	**51**	69
Net investment income	**5,847**	6,201
Gains (losses) on the sale of investments *(note 6d)*	**(23,228)**	9,427
Total realized income (losses)	**(17,381)**	15,628
Unrealized decrease in value of investments and liabilities related to investments *(note 6e)*	**(19,034)**	(5,860)
Unrealized decrease in value of investments in third-party and bank-sponsored ABCP, net of back interest *(note 4b)*	**(3,401)**	(1,897)
Total unrealized decrease in value	**(22,435)**	(7,757)
Net investment results	**(39,816)**	7,871
Excess depositors' deposits over withdrawals	**4,554**	4,000
Increase (decrease) in combined net assets	**(35,262)**	11,871
Combined net assets, beginning of year	**155,350**	143,479
Combined net assets, end of year	**120,088**	155,350

The accompanying notes are an integral part of the combined financial statements.

COMBINED FUNDS NOTES TO FINANCIAL STATEMENTS

(as at December 31, 2008)

1.
CONSTITUTION AND OPERATIONS

The Caisse de dépôt et placement du Québec, a legal person established in the public interest within the meaning of the *Civil Code*, is governed by the *Act respecting the Caisse de dépôt et placement du Québec* (R.S.Q., chapter C-2). It receives funds, the deposit of which is provided under the Act. Pursuant to both the federal and provincial income tax acts, the Caisse is not subject to income taxes.

GENERAL FUND (CONSOLIDATED STATEMENTS)

The General Fund comprises all treasury operations (management of demand and term deposits, and corporate financing) as well as results from net investments related to third-party and bank-sponsored asset-backed commercial paper ("third-party and bank-sponsored ABCP") held in the specialized Bonds portfolio (760).

INDIVIDUAL FUNDS

The individual funds are comprised of diversified investments, and each fund has only one depositor that exclusively makes participation deposits therein. The individual funds are for the use of the following depositors:

Fund 300: Fonds du Régime de rentes du Québec administered by the Régie des rentes du Québec;

Fund 301: Government and Public Employees Retirement Plan administered by the Commission administrative des régimes de retraite et d'assurances;

Fund 302: Pension Plan for Management administered by the Commission administrative des régimes de retraite et d'assurances;

Fund 303: Individual plans administered by the Commission administrative des régimes de retraite et d'assurances;

Fund 305: Pension Plan for Elected Municipal Officers administered by the Commission administrative des régimes de retraite et d'assurances;

Fund 306: Régime complémentaire de rentes des techniciens ambulanciers/paramédics et des services préhospitaliers d'urgence administered by the Aon Conseil;

Fund 307: Fonds d'assurance automobile du Québec administered by the Société de l'assurance automobile du Québec;

Fund 311: Supplemental Pension Plan for employees of the Québec construction industry – general account – administered by the Commission de la construction du Québec;

Fund 312: Supplemental Pension Plan for employees of the Québec construction industry – retirees account – administered by the Commission de la construction du Québec;

Fund 313: Supplemental Pension Plan for employees of the Québec construction industry – supplementary account – administered by the Commission de la construction du Québec;

Fund 314: Fonds d'assurance-dépôts administered by the Autorité des marchés financiers;

Fund 315: Fonds d'assurance-prêts agricoles et forestiers administered by La Financière agricole du Québec;

Fund 316: Fonds d'amortissement du régime de retraite – RREGOP administered by the ministère des Finances, Government of Québec;

Fund 317: Fonds d'amortissement du régime de retraite – RRPE administered by the ministère des Finances, Government of Québec;

Fund 318: Fonds d'amortissement des autres régimes de retraite administered by the ministère des Finances, Government of Québec;

Fund 326: Fonds d'assurance-récolte administered by La Financière agricole du Québec;

Fund 327: Fédération des producteurs de bovins du Québec;

Fund 328: Régime de rentes de survivants administered by the Conseil du trésor, Government of Québec;

Fund 329: Fonds d'assurance-garantie administered by the Régie des marchés agricoles et alimentaires du Québec;

Fund 330: Fonds de la santé et de la sécurité du travail administered by the Commission de la santé et de la sécurité du travail;

Fund 332: Fonds des cautionnements des agents de voyages – cautionnements individuels administered by the Office de la protection du consommateur;

Fund 333: Fonds d'indemnisation des clients des agents de voyages administered by the Office de la protection du consommateur;

Fund 341: Fonds pour l'éducation et la saine gouvernance – Fonds de trésorerie administered by the Autorité des marchés financiers;

Fund 342: Régime de retraite de l'Université du Québec administered by the Comité de retraite du Régime de retraite de l'Université du Québec;

Fund 343: Fonds d'assurance parentale administered by the Conseil de gestion de l'assurance parentale;

Fund 347: Régime de retraite du personnel des CPE et des garderies privées conventionnées du Québec administered by the Aon Conseil;

Fund 348: Régime complémentaire de retraite des employés syndiqués de la Commission de la construction du Québec administered by the Comité de retraite du Régime complémentaire de retraite des employés syndiqués de la CCQ;

Fund 351: Fonds des générations administered by the ministère des Finances, Government of Québec;

Fund 353: Régime de retraite des membres de la Sûreté du Québec – caisse participants administered by the Commission administrative des régimes de retraite et d'assurances;

Fund 361: Régime de rentes pour le personnel non enseignant de la Commission des écoles catholiques de Montréal administered by the Commission administrative des régimes de retraite et d'assurances;

Fund 362: Régime de retraite pour certains employés de la Commission scolaire de la Capitale administered by the Commission administrative des régimes de retraite et d'assurances;

Fund 363: Régime de retraite des employés de la Ville de Laval administered by the Comité du Régime de retraite des employés de la Ville de Laval;

Fund 368: Fonds pour l'éducation et la saine gouvernance – Fonds capitalisé administered by the Autorité des marchés financiers (created July 1, 2008).

SPECIALIZED PORTFOLIOS

The specialized portfolios are pooled funds for participation deposits of the various funds. The specialized portfolios are the following:

- Short Term Investments (740)
- Real Return Bonds (762)
- Bonds (760)
- Long Term Bonds (764)
- Canadian Equity (720)
- U.S. Equity – hedged (731)
- U.S. Equity – unhedged (734)
- Foreign Equity – hedged (730)
- Foreign Equity – unhedged (733)
- Emerging Markets Equity (732)
- Québec International (761)
- Investments and Infrastructures (781) (consolidated statements)
- Private Equity (780) (consolidated statements)
- Real Estate Debt (750) (consolidated statements)
- Real Estate (710) (consolidated statements)
- Commodity Financial Instruments (763)
- Hedge Funds (770) (consolidated statements)
- Asset Allocation (771)

2.
ACCOUNTING POLICIES

The preparation of the combined financial statements of the Caisse in accordance with generally accepted accounting principles in Canada requires that management make estimates and assumptions, which have an impact on the accounting of assets and liabilities, the presentation of contingent assets and liabilities at the date of the financial statements and the accounting of revenues and expenses during the financial year covered by the financial statements. Actual results may differ from such estimates.

A statement of cash flows is not presented as it would provide no further useful information for the comprehension of cash flows during the year.

A / COMBINED FINANCIAL STATEMENTS

The combined financial statements comprise the accounts of the Caisse's subsidiaries, along with those of the General Fund, the individual funds, and the specialized portfolios. The accounts of each fund and each portfolio are presented in financial statements audited by the Auditor General of Québec.

B / INVESTMENTS AND JOINT OPERATIONS

Investments and related assets and liabilities are accounted for at fair value, which is the estimated exchange value that would be agreed upon in an arm's-length transaction between competent, willing parties in conditions of full competition, established at the year-end.

Transaction costs which are directly attributable to the acquisition and sale of investments are included in income and applied against gains and losses on the sale of investments. Transaction costs include commissions and stock exchange fees.

FIXED-INCOME SECURITIES

Fixed-income securities comprise short-term investments, bonds, third-party and bank-sponsored ABCP and mortgages. Acquisitions and sales of fixed-income securities are recorded at the transaction date, except for mortgages which are recorded at the settlement date.

i / Valuation method

The fair value of fixed-income securities other than mortgages is determined based on the market price when such a value is available. When a market price is not available, the fair value of the securities is determined based on valuation methods used in capital markets, such as the annualization of future cash flows at the current interest rate, or on similar transactions on an arm's-length basis. These valuations are supported by assumptions which consider market data such as interest rate yield curves and the risk premium related to the issuer's creditworthiness. In some cases, the data used in the assumptions do not rely on observable market factors as described earlier. Market data are adjusted to reflect uncertainty and to ensure securities are recorded at fair value. According to its estimates, management is of the opinion that the use of possible alternative assumptions to determine the fair value of these securities, with the exception of third-party and bank-sponsored ABCP, would not result in significantly different fair values. The valuation method for third-party and bank-sponsored ABCP, as well as the variations in fair value attributable to possible alternative assumptions for these securities, is discussed in note 4b.

The fair value of mortgages is determined based on the annualization of future contractual cash flows at the market interest rate. This rate is the rate that could be provided on loans or securities with similar conditions and maturities based on valuations made by management. Where the spreading of cash flows cannot be estimated in a reasonably reliable fashion, the fair value corresponds either to the fair value of any collateral on the security, after deducting expected costs of realization and any amount legally due to borrowers, or at the observable market price for the security.

The fair value of most fixed-income securities is reviewed biannually by valuation committee, comprised of independent experts or by an independent valuation firm.

ACCOUNTING POLICIES (cont.)

ii / Investment income and gains and losses on the sale of investments

Investment income from fixed-income securities includes amortization of the premium and the discount, which makes it possible to maintain a constant real return until maturity. Income from mortgages is reduced by operating expenses and financial costs of CMBS and is recorded under Investment Income – Fixed-income securities.

Gains and losses on the sale of investments represent the difference between the unamortized cost and the net realizable fair value on the sale of investments. The unamortized cost represents the acquisition cost adjusted to reflect the amortization of the premium or discount.

VARIABLE-INCOME SECURITIES

Variable-income securities comprise equities and convertible securities as well as real estate holdings. Acquisitions and sales of equities and convertible securities are recorded at the transaction date, while acquisitions and sales of real estate are recorded at the settlement date.

i / Valuation method

The fair value of equities and convertible securities traded on a stock exchange is determined based on prices on major stock exchanges as well as those provided by recognized financial institutions. For unlisted equities and convertible securities, valuations are made using commonly used valuation methods such as the earnings multiples of comparable listed companies, the annualization of cash flows, or based on similar transactions made on an arm's-length basis. The most commonly used earnings multiples are the EBITA multiple, the p/e multiple and the price/book ratio. The valuations of unlisted equities and convertible securities are reviewed biannually by valuation committee, comprised of independent experts or by an independent valuation firm.

The fair value of private investment funds presented under Equities and convertible securities, is determined based on the fair value provided by the general partner, using commonly used valuation methods.

The fair value of real estate holdings is determined and certified annually by recognized independent chartered appraisers. The valuation techniques used rely principally on three recognized methodologies: the capitalization of earnings, the annualization of cash flows at market rate and the comparison to recent similar market transactions. The amount established is supported by reasonable assumptions and is subsequently adjusted to reflect other assets and liabilities that have an impact on fair value.

ii / Investment income and gains and losses on the sale of investments

Dividend income is recognized on the ex-dividend date. Income from real estate holdings is reduced by operating expenses related to real estate holdings, operation expenses and loan financial expenses, and is recorded under the item Investment income – Variable-income securities.

Gains and losses on the sale of investments represent the difference between the cost and the net realizable value on the sale of investments. The cost of investments is the acquisition cost, except for the acquisition cost of investments in joint ventures, which are accounted for using the equity method.

DERIVATIVE FINANCIAL INSTRUMENTS

Pursuant to its investment management, the Caisse conducts transactions involving various derivative financial instruments to manage the risks associated with exchange rate, interest rate, and market fluctuations.

Derivative financial instruments whose fair value is favourable are recorded under the item Investments, whereas those whose fair value is unfavourable are recorded under Liabilities related to investments.

ACCOUNTING POLICIES (cont.)

i / Valuation method

Derivative financial instruments are recorded at their fair value at year-end. These values are established using prices on the major stock exchanges as well as those provided by recognized financial institutions. For unlisted instruments, fair value is determined based on similar transactions made on an arm's-length basis or using recognized and commonly used models. Models used include the annualization of future cash flows at current return and the Black & Scholes model. These models require the use of assumptions regarding the amount and maturity of future cash flows and current return. Assumptions are prepared based on market data such as interest rate yield curves, premiums related to credit risk, foreign exchange rates as well as volatility and correlation of equity and commodity prices and interest rate. In the case of derivative financial instruments that are new, complex or with a long-term maturity, it can be necessary to use assumptions that are based on non-market data such as a projection of interest rate curves and data on volatility. Such data are subsequently adjusted to reflect uncertainty and to ensure securities are recorded at fair value. Based on its estimates, management believes using alternative assumptions to evaluate such derivative financial instruments at fair value would not result in significantly different fair values.

The fair value estimates of most derivative financial instruments are reviewed biannually by independent valuation firm.

ii / Investment income and gains and losses on the sale of investments

Investment income from derivative financial instruments is included in income from fixed-income and variable-income securities, whereas gains and losses from derivative financial instruments are included in gains (losses) on the sale of investments on the basis of the underlying investments.

SECURITIES ACQUIRED UNDER REVERSE REPURCHASE AGREEMENTS

The Caisse conducts security-borrowing operations involving short-term investments and bonds to cover short sales or to generate additional income from security-borrowing operations. These security-borrowing operations are recorded under Securities acquired under reverse repurchase agreements. Interest earned on reverse repurchase agreements is recorded as interest income under the item Investment income – Fixed-income securities.

SECURITIES SOLD UNDER REPURCHASE AGREEMENTS

The Caisse conducts security-lending operations involving short-term investments and bonds to generate cash flow liquidity or to generate additional income from security-lending operations. These security-lending operations are recorded under Securities sold under repurchase agreements. Interest paid on repurchase agreements is applied against Investment income – Fixed-income securities.

SHORT SELLING OF SECURITIES

Short selling of securities represents the commitment by the Caisse to purchase securities from third parties to cover its positions. Interest expenses related to commitments involving short selling of short-term investments and bonds are recorded under Investment income – Fixed-income securities, whereas costs related to commitments involving short selling of equities are recorded under Investment income – Variable-income securities.

Gains and losses on commitments related to short selling of short-term investments and bonds are recorded in Gains (losses) on the sale of investments – Fixed-income securities, whereas those related to short selling of equities are recorded in Gains (losses) on the sale investments – Variable-income securities.

C / ADMINISTERED PROPERTY AND PROPERTY UNDER MANAGEMENT

The Caisse and its subsidiaries administer and manage property entrusted to them by clients and on their behalf. This property is not included in the "Combined statement of net assets" of the Caisse. The Caisse and its subsidiaries receive fees in return for such portfolio management services and administrative services, which include the administration of real estate properties and management of securitized loans.

ACCOUNTING POLICIES (cont.)

D / FOREIGN CURRENCY TRANSLATION

The fair value of investments and any other assets and liabilities denominated in foreign currencies is translated into Canadian dollars at the rate of exchange prevailing at the year-end.

The cost of investments in equities and that of real estate holdings from integrated foreign operations and the unamortized costs of investments in bonds, mortgages, and short-term investments are translated at the rate of exchange prevailing on the acquisition date. The cost of investments from self-sustaining foreign operations is translated at the rate prevailing at the year-end.

Income is translated at the rate of exchange prevailing on the transaction date, with the exception of income from the specialized real estate portfolio, which is translated at the average rate for the year.

E / LOAN SECURITIZATION

The Caisse periodically securitizes loans and mortgages by selling such loans and mortgages to a collaterized security entity, which subsequently issues securities to investors. Such transactions are recorded as sales where the Caisse is deemed to have relinquished control over such assets and to have received compensation other than the beneficial rights attached to the assets disposed of, in accordance with Accounting Guideline AcG-12 “Transfers of receivables” in the Canadian Institute of Chartered Accountants (“CICA”) Handbook. At the time of securitization, no beneficial right attached to the securitized loans is retained. Any gains and losses deriving from such transactions are recorded under Gains (losses) on the sale of investments – Mortgages and Bonds.

Companies under common control usually continue to manage loans after disposition. Since management fees are established on the basis of the market for such services, no assets or liabilities under management are recorded at the date of disposition.

F / OPERATING EXPENSES

Operating expenses represent all expenses related to portfolio management and administration, with the exception of those related to external management. Operating expenses are presented under a specific item in the “Combined statement of income and changes in net assets.” Expenses related to the management of the specialized real estate and real estate debt portfolios are included in operating expenses. Operating expenses related to the management and administration of real estate holdings and mortgages are deducted from real estate holdings investment income and mortgages investment income respectively.

G / EXTERNAL MANAGEMENT FEES

External management fees represent amounts paid to external financial institutions, principally institutional fund managers active on international stock markets, for the management of Caisse funds on behalf of the Caisse. External management fees are presented under a specific item in the “Combined statement of income and changes in net assets.”

3.
ADOPTION OF SECTION 3862 FINANCIAL INSTRUMENTS – DISCLOSURE AND SECTION 3863 FINANCIAL INSTRUMENTS – PRESENTATION

On January 1, 2008 the Caisse adopted the provisions in Section 3862 *Financial Instruments – Disclosure* and Section 3863 *Financial Instruments – Presentation.* Sections 3862 and 3863 replace Section 3861 *Financial Instruments – Disclosure and Presentation*. These sections amend the requirements regarding the presentation of the notes to financial statements, and emphasize the importance of the information to be disclosed concerning the nature and size of risks related to financial instruments as well as the method used by the entity to manage such risks.

4.
INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS

A / INVESTMENTS

(in millions of dollars)		2008		2007
	Fair value	**Cost**	Fair value	Cost
Fixed-income securities				
Short-term investments				
Canadian	**5,826**	**5,910**	9,889	9,894
Foreign	**3,580**	**4,522**	4,865	4,898
	9,406	**10,432**	14,754	14,792
Bonds				
Issued or guaranteed by:				
Canadian government	**16,552**	**15,211**	23,586	22,966
Province of Québec	**9,265**	**8,517**	8,592	7,831
Other Canadian provinces	**3,047**	**2,969**	2,304	2,236
Municipalities and other Canadian bodies	**1,611**	**1,597**	1,728	1,724
Canadian government corporations	**11,091**	**10,201**	13,311	12,619
U.S. government	**823**	**740**	205	208
Other foreign governments	**1,812**	**1,594**	1,759	1,814
Mortgage securities				
Canadian	**272**	**276**	284	276
Foreign	**711**	**2,438**	2,022	2,601
Canadian corporations	**12,592**	**13,623**	15,947	16,260
Foreign corporations	**2,911**	**4,076**	4,695	5,315
Inflation-indexed securities				
Canadian	**587**	**604**	934	895
Foreign	**1,973**	**1,611**	3,381	3,664
Hedge funds	**439**	**460**	2,132	2,323
	63,686	**63,917**	80,880	80,732
Third-party and bank-sponsored ABCP *(note 4b)*	**7,186**	**12,787**	10,740	12,607
Mortgages				
Canadian	**6,451**	**6,431**	5,979	5,939
Foreign	**5,342**	**5,738**	4,481	4,574
	11,793	**12,169**	10,460	10,513
Total fixed-income securities	**92,071**	**99,305**	116,834	118,644
Variable-income securities				
Equities and convertible securities				
Canadian	**12,523**	**16,055**	17,172	14,938
U.S.	**10,968**	**14,604**	18,208	20,127
Foreign and emerging markets	**17,714**	**21,180**	26,926	24,357
Hedge funds	**4,688**	**4,933**	4,848	5,051
	45,893	**56,772**	67,154	64,473
Real estate holdings				
Canadian	**11,884**	**8,987**	13,184	9,117
Foreign	**11,032**	**10,450**	9,256	8,610
	22,916	**19,437**	22,440	17,727
Total variable-income securities	**68,809**	**76,209**	89,594	82,200

INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS (cont.)

(in millions of dollars)		2008		2007
	Fair value	**Cost**	Fair value	Cost
Amounts receivable with respect to investments				
Securities acquired under reverse repurchase agreements				
Canadian	**2,900**	**2,901**	2,457	2,127
Foreign	**2,780**	**2,730**	4,986	5,110
Amount pertaining to derivative instruments				
Canadian	**2,465**	**26**	532	39
Foreign	**13,468**	**1,681**	8,394	1,921
	21,613	**7,338**	16,369	9,197
Total investments	**182,493**	**182,852**	222,797	210,041

The fair value of investments includes Canadian and foreign private equities for which no market price is available. The fair value of such securities details as follows:

(in millions of dollars)	2008	2007
Canadian securities		
Short-term investments	**1,184**	1,234
Bonds	**1,122**	1,244
Third-party and bank-sponsored ABCP	**7,186**	10,740
Equities and convertible securities	**3,786**	4,789
	13,278	18,007
Foreign securities		
Short-term investments	**2,764**	3,030
Bonds	**690**	769
Equities and convertible securities	**18,072**	16,593
	21,526	20,392
	34,804	38,399

Investments – Real estate holdings includes investments in joint ventures reported on an equity basis. These investments at fair value details as follows:

(in millions of dollars)	2008	2007
Investments in joint ventures	**9,097**	8,401
Real estate holdings	**15,889**	14,356
Short-term investments	**15**	29
Investment income, accrued and receivable	**10**	6
Other assets	**678**	586
	16,592	14,977
Loans and notes payable	**74**	106
Mortgage loans payable	**6,284**	5,367
Other liabilities	**1,026**	1,053
Non-controlling interests	**111**	50
	7,495	6,576

INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS (cont.)

B / THIRD-PARTY AND BANK-SPONSORED ABCP

As at December 31, 2008, the Caisse held investments in Canadian asset-backed commercial paper ("ABCP") that has been restructured. These investments are divided into three types:

/ "Third-party ABCP" that has been restructured under the restructuring agreement of the Pan-Canadian Investors Committee;

/ "Other third-party ABCP" that has been restructured (White Knight Trust) or whose restructuring has failed (Devonshire Trust); and

/ "Bank-sponsored ABCP" that had to be restructured in 2008 as the securities matured (Apex Trust, Great North Trust and Superior Trust).

DESCRIPTION OF ABCP

ABCP is short-term debt supported by a range of financial instruments. The assets, such as mortgage or consumer loans, or exposure to risk, such as credit default swaps, are acquired by a conduit by means of various types of transaction, including the purchase of financial assets and derivatives. ABCP is generally issued for a term of 30, 60 or 90 days, discounted or interest-baring.

The financial instruments serving as assets for a conduit that issued ABCP generally have maturities that are longer than the maturity of the ABCP issued. The conduit therefore must typically have liquidity backstop facilities with a financial institution that it can avail itself of, on certain conditions, in the event that it is not able to issue new ABCP securities in order to redeem those that mature or to meet the need for additional liquid assets.

Until the summer of 2007, narrowing credit spreads were conducive to the creation of leveraged super-senior ("LSS") structures. These structures give investors exposure supported by a super-senior tranche of a group of reference assets. Generally speaking, the exposure corresponds to many times the amount invested by investors in a given conduit and posted as collateral by the conduit for the beneficiary of the credit protection. For example, an investment of $10 million may be supported 10 times by means of a credit linkage to a super-senior tranche with a notional amount of $100 million. The combination of assets posted as collateral and a credit default swap, such as an LSS, is generally referred to as synthetic assets.

A super-senior tranche has an attachment point, namely the threshold of losses that the group of reference assets must reach before payment obligations are triggered. In general, this threshold significantly exceeds the level of loss consistent with a note rated R-1 (high) or AAA. Thus the level of loss to which the super-senior tranche is exposed is generally lower than that historically experienced for this rating level. When the level of loss increases or when there are indicators showing that it could rise (triggers for additional collateral calls), the purchasers of protection against credit default may require additional collateral over and above the amounts initially invested. The structures did not have mechanisms to obtain liquid assets so as to meet the additional collateral calls.

If additional collateral cannot be provided, the LSS is unwound to the benefit of the purchaser of protection against credit default. This unwinding entails a loss for the investors in the ABCP, even if the real loss of the group of reference assets has not reached the attachment point on the super-senior tranche.

The subprime mortgage crisis in the United States caused disruption on the international markets, which resulted in a liquidity crisis on the Canadian third-party ABCP market in mid-August 2007. Since August 13, 2007, the Caisse has not been able to have redeemed amounts due under third-party ABCP. When acquired by the Caisse, the ABCP was rated R-1 (high) by the rating agency DBRS Limited ("DBRS"), namely the highest rating issued by DBRS for asset-backed commercial paper.

On August 13, 2007, the liquidity providers did not make available the amounts committed pursuant to their undertakings, since they did not believe that the necessary conditions had been met. The investors and the banks that had purchased credit default protection therefore agreed to a standstill period and began discussions within the framework of the Montréal Proposal and the Pan-Canadian Investors Committee for ABCP.

INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS (cont.)

TIMELINE OF THE RESTRUCTURING EFFORTS

Third-party ABCP

The efforts to restructure third-party ABCP, which began on August 13, 2007, and in which the Caisse has taken part actively, resulted in the conclusion of an agreement on December 24, 2008, which then required approval by the decision-making authorities of the institutions concerned as well as orders-in-council. The agreement was subsequently confirmed in its proposed form and gave rise to an exchange of securities on January 21, 2009.

The timeline of the key events leading to the restructuring is as follows:

On August 15, 2007, a group of investors and financial institutions, including the Caisse, proposed an agreement, the Montréal Proposal, designed to re – establish a climate of trust and to implement an effective resolution strategy that would include matching of the maturities of the underlying assets and replacement notes. Under the agreement, the investors and the financial institutions undertook not to put the conduits in default in order to avoid an unwinding of the credit protection and a forced sale of the debt and the underlying financial assets (the "standstill period").

On September 6, 2007, a Pan-Canadian Investors Committee consisting of participants in the Montréal Proposal was formed to oversee the restructuring process.

On November 6, 2007, DBRS issued a public information document providing additional information on the composition of each conduit. DBRS confirmed at that time that 97% of the debt and the underlying financial assets was of the highest quality and retained a AAA (high) rating, and that 2% was rated AA or AA (low).

On December 23, 2007, the Pan-Canadian Investors Committee approved an agreement in principle (the "restructuring proposal") for all the trusts covered by the Montréal Proposal, with the exception of Skeena Capital Trust (already restructured) and Devonshire Trust. The main objectives of the restructuring proposal announced on that date were to replace the third-party ABCP with new securities having maturities similar to those of the debt and the underlying financial assets, to combine certain series of third-party ABCP that are supported in whole or in part by synthetic assets, to alleviate the obligations of margin calls on LSS, to put in place margin funding facilities and to foster a secondary market so as to generate liquid assets for the holders of third-party ABCP.

On March 17, 2008, the Ontario Superior Court of Justice granted a motion by the Committee under the *Companies' Creditors Arrangement Act* ("CCAA") intended to establish a procedure to secure approval by the noteholders of a formal restructuring plan (the "plan").

On April 25, 2008, 96% of the noteholders in terms of number and value voted in favour of the plan.

On June 5, 2008, the plan was ratified by the Ontario Superior Court of Justice. The ruling was then appealed by a group of ABCP noteholders who wished to contest the plan's implementation.

On August 18, 2008, the Court of Appeal for Ontario upheld the decision of the Ontario Superior Court of Justice.

On September 19, 2008, the Supreme Court of Canada rejected the application for leave to appeal filed by the group of noteholders.

INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS (cont.)

On December 24, 2008, the Pan-Canadian Investors Committee and the banks that had purchased protection concluded a final restructuring agreement that was confirmed in January 2009 once the required approvals and orders-in-council were obtained. The key aspects of the final agreement are as follows:

/ Creation of three new structures in the form of trusts called “master asset vehicles” (“MAV 1,” “MAV 2” and “MAV 3”).

/ MAV 1 and MAV 2 will consist of the transactions of the ABCP conduits constituted solely of synthetic assets or of hybrid assets, namely a combination of synthetic and traditional assets. They will also include the high-risk assets associated with these transactions.

/ The main difference between MAV 1 and MAV 2 is that the margin funding facility is self-funded for the participants in MAV 1, whereas it is provided by third-party lenders in the case of MAV 2. As a result of this distinction, the interest paid to the holders of notes issued by MAV 2 is less than that paid to the holders of notes issued by MAV 1.

/ Establishment of margin funding facilities in support of MAV 1 and MAV 2 to finance possible collateral calls on the underlying LSS.

/ MAV 3 will consist of transactions of the ABCP conduits constituted exclusively of high-risk assets and traditional assets.

/ Establishment of an initial 18-month standstill period during which no additional collateral calls may be effected on the LSS.

/ Widening of certain “spread-loss triggers,” thereby deferring the possible triggering of additional collateral calls.

/ The Government of Canada, the governments of Québec, Alberta and Ontario, and the Caisse are taking part in the final agreement by establishing an additional senior margin funding facility.

On January 21, 2009, DBRS issued a final rating report for the Class A-1 and A-2 notes issued by MAV 1 and MAV 2 and confirmed the preliminary ratings issued on December 29, 2008, namely A.

Other third-party ABCP
On October 16, 2007, the Pan-Canadian Investors Committee announced the successful restructuring of the first of the 22 conduits affected by the Montréal Proposal, namely Skeena Capital Trust (restructured under the name of White Knight Trust).

On December 20, 2007, the Caisse received replacement securities and liquid assets on completion of the restructuring of this investment. Initially rated AAA by DBRS, the notes of White Knight Trust were successively downgraded to AA (low) in November 2008 and A (low) in January 2009.

Since December 23, 2007, many restructuring proposals have been reviewed with the bank that purchased protection against credit default by Devonshire Trust. These numerous attempts all proved unproductive. As a result of this failure, the bank began legal proceedings on January 13, 2009, to recover the collateral posted by the trust, and the Caisse therefore took a provision for the loss of its entire investment, resulting in a decrease in value of $337 million for fiscal 2008 ($48 million in 2007).

Bank-sponsored ABCP
The Caisse holds ABCP issued by trusts sponsored by financial institutions, including Sitka Trust (since restructured under the name of Apex Trust), Great North Trust and Superior Trust. As a result of market turbulence, these trusts received substantial collateral calls from purchasers of credit protection. The trusts were therefore restructured in 2008.

The replacement securities for Apex Trust, Superior Trust and Great North Trust received by the Caisse are not rated by an external agency.

INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS (cont.)

BALANCE AS AT DECEMBER 31

As at December 31, 2008 and 2007, the investments in third-party and bank-sponsored ABCP consist of the following elements:

(in millions of dollars)			December 31, 2008
	Fair value	Cumulative unrealized decrease in value	Cost
Third-party ABCP restructured under the agreement of the Pan-Canadian Investors Committee			
Synthetic and hybrid assets[1]	6,017	(3,725)	9,742
Traditional assets[2]	623	(115)	738
High-risk assets	–	(890)	890
	6,640	(4,730)	11,370
Other			
Third-party ABCP not restructured	–	(385)	385
Third-party ABCP restructured	198	(92)	290
Bank – sponsored ABCP restructured	348	(394)	742
	7,186	(5,601)[3]	12,787
Restructuring costs		(86)	
Cumulative unrealized decrease in value as at December 31, 2008		(5,687)	
Writeoff of assets[4]		(171)	
Losses on the sale of investments and cumulative unrealized decrease in value as at December 31, 2008		(5,858)	
Accrued interest receivable[5]		389	
		(5,469)	

(in millions of dollars)			December 31, 2007
	Fair value	Cumulative unrealized decrease in value	Cost
Third-party ABCP restructured under the agreement of the Pan-Canadian Investors Committee			
Synthetic and hybrid assets	8,635	(1,216)	9,851
Traditional assets	1,196	(103)	1,299
High-risk assets	313	(469)	782
	10,144	(1,788)	11,932
Other			
Third-party ABCP not restructured	337	(48)	385
Third-party ABCP restructured	259	(31)	290
	10,740	(1,867)[3]	12,607
Restructuring costs		(30)	
Cumulative unrealized decrease in value as at December 31, 2007		(1,897)	

1 The investments reflect the commitment made by the Caisse in 2008 to acquire MAV 2 notes at a discount at the time of the restructuring. The notional amount and the agreed-on purchase price for the notes are $170 million and $119 million respectively.

2 Not including an amount of $550 million representing the Caisse's share of repayment of underlying assets redeemed by the conduits as of December 31, 2008.

3 Includes the fair value of the commitments described in the following item.

4 During fiscal 2008, the restructuring of certain ABCP securities entailed writeoffs and similar adjustments of about $171 million.

5 Received on January 21, 2009.

INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS (cont.)

PRESENTATION IN COMBINED INCOME AND CHANGES IN NET ASSETS

(in millions of dollars)

Cumulative unrealized decrease in value as at December 31, 2008	**(5,687)**
Cumulative unrealized decrease in value as at December 31, 2007	**(1,897)**
	(3,790)
Accrued interest receivable	**389**
Unrealized decrease in value of investments in third-party and bank-sponsored ABCP, net of back interest	**(3,401)**

COMMITMENTS ASSOCIATED WITH THIRD-PARTY AND BANK-SPONSORED ABCP

The following table summarizes the commitments associated with the restructuring of third-party and bank-sponsored ABCP and the estimate of its fair value, which is included in the valuation of ABCP provided in the preceding item:

(in millions of dollars)	**December 31, 2008**	
	Ultimate maturity	**Commitments**
Agreement of the Pan-Canadian Investors Committee		
MAV 1 MFF – basic	**July 2017**	**5,767**
MAV 1 MFF – additional interest	**July 2017**	**400**
MAV 1 and MAV 2 SFF	**July 2017**	**300**
Subtotal		**6,467**
Restructured bank-sponsored ABCP	**December 2016**	**323**
Total		**6,790**

(in millions of dollars)	December 31, 2007	
	Ultimate maturity	Commitments
Preliminary agreement of the Pan-Canadian Investors Committee		
MAV 1 MFF – basic	July 2017	5,153

The fair value of the commitments is estimated to be a negative amount of $634 million ($383 million in 2007).

INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS (cont.)

Margin funding facility ("MFF")
In addition to the assets already provided as collateral to the purchaser of credit default protection, the final agreement of the Pan-Canadian Investors Committee provides that MAV 1 and MAV 2 must have an MFF to cover any collateral calls on the LSS. The Caisse has decided to self-fund its share of the MFF, which explains its interest in MAV 1.

The Caisse's share of this credit commitment amounts to $5,767 million, has the same rank as that of the other participants and matures in July 2017 or at an earlier date if all the LSS transactions are settled beforehand. This amount represents the commitment of $5,153 million that was negotiated under the preliminary agreement in December 2007, to which has been added an amount of $614 million under the terms of the final agreement of December 24, 2008. The Caisse will receive no fee in respect of this credit commitment. The advances that could be made under this MFF will bear interest at a rate based on the bankers' acceptance rate or the prime rate. All amounts advanced under the MFF will take precedence over the amounts payable on the notes issued by MAV 1. In the event that the Caisse defaults on its obligations to provide funds under its share of the MFF, the MAV 1 notes held by the Caisse could be exchanged for subordinated notes. The Caisse will have to maintain a credit rating equivalent to AA (high) with at least two of the four rating agencies, DBRS, S&P, Fitch and Moody's, failing which it will have to provide collateral or another type of credit support to MAV 1 or fulfill its commitments through another entity with a sufficiently high credit rating.

Under a separate agreement, the Caisse has agreed to take an interest of $400 million in the MFF commitments of a MAV 1 participant in exchange for a commitment fee of 1.2% per annum, namely the same rate as the third-party institutions that have underwritten the equivalent MAV 2 MFF. This interest will end automatically at the end of the MAV 1 MFF. This facility is at the same level as the Caisse's interest in the MFF, which means that these facilities would be called simultaneously in the event of a collateral call.

Senior funding facility ("SFF")
In the event that the MAV 1 MFF and the equivalent MAV 2 facility prove insufficient to meet the collateral calls of the vehicle in question, an SFF has been put in place with the participation of the governments of Canada, Québec, Alberta and Ontario and the Caisse for MAV 1 ($1.8 billion) and MAV 2 ($1.7 billion) to provide access to additional liquid assets. The Caisse's share of these credit commitments is $154 million for MAV 1 and $146 million for MAV 2. The Caisse will receive a commitment fee of 1.19% per annum until December 2016 in respect of this credit commitment. These commitments expire in July 2010, unless an amount has been drawn down and remains unpaid at that date, in which case all the liquid assets available for repayment in MAV 1 or MAV 2, as the case may be, will be used to pay the interest and principal of the SFFs before the relevant MFF and the notes issued by the vehicle in question. The advances that may be made under this facility will bear interest at a rate based on the bankers' acceptance rate or the prime rate.

Commitments associated with bank-sponsored ABCP
The bank-sponsored ABCP securities restructured in 2008 include two securities that represent interests in trusts that have indirect interests in LSS. To protect its interest in the underlying assets, the Caisse has agreed thus far to take part in collateral calls totalling $323 million, which have not yet had to be disbursed. In the event of additional collateral calls by the trusts, the Caisse will be able to decide at that time whether to take part. If it does not take part, the underlying positions will be liquidated, and the Caisse's investments will in all likelihood be lost. The securities and the related commitments mature at the latest in December 2016.

ESTABLISHMENT OF FAIR VALUE

Given that there is no active market for the third-party and bank-sponsored ABCP in which the Caisse holds investments, it has established, in accordance with CICA guidelines, fair values for the various ABCP securities, using a valuation technique based on a financial model whose assumptions and probabilities reflect uncertainties regarding the amounts, the return and maturity of the cash flows, the illiquidity risk, the nature and credit risk of the debt and the underlying financial assets, and credit spreads reflecting market conditions as at December 31, 2008. The assumptions, based on information available as at December 31, 2008, use observable market data, such as interest rates and credit quality and price, as much as possible. They also take into account specific aspects of the plan and are based partially on assumptions not supported by prices or rates observed on the market. As already stated, pursuant to the final restructuring plan, the third-party ABCP securities will be converted into new securities with maturities corresponding to those of the underlying assets. The new securities will bear interest at rates that will ultimately reflect the cash flow available within the vehicles, including the cost inherent in the funding facilities included in the restructuring plan.

INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS (cont.)

The fair value of each third-party and bank-sponsored ABCP security has been established from an estimate of the present value of cash flows according to various default and credit loss scenarios on all the underlying assets, the real maturities of the securities and the expected interest rates, and takes into account subordination of the restructured notes, where required. Once adjusted to take into account the impact of the credit risk of the underlying assets, the expected cash flows on the third-party and bank-sponsored ABCP investments are discounted at a rate corresponding to a AAA credit rating, plus a financing and illiquidity premium. The main assumptions considered in the model, excluding the high-risk assets, are as follows:

Fair value of third-party and bank-sponsored ABCP – Main assumptions

	December 31, 2008	December 31, 2007
Success rate of the restructuring plan	**100%**	90%
Weighted average interest rate of the notes to be received in the restructuring[1]		
A-1, A-2 and B	**BA [2] + 0.30%**	BA [2] + 0.30%
Default rate and credit loss	**S&P 1981-2007 table Default rated adjusted as a function of a downgrade Level of loss with a 70% default rate**	S&P 1981-2006 table Default rated adjusted as a function of a downgrade Level of loss with a 60% default rate
Financing and illiquidity premiums	**4.50%**	1.03%
Cost of margin funding facilities	**The financial impact of the facilities has been calculated on the basis of an annual commitment fee of 1.6%**	The financial impact of the facilities has been calculated on the basis of an annual commitment fee of 1.2%
Planned maturity of the new notes	**December 2016 for the MAV 1 and 2 notes**	As a function of the LSS maturities
Credit rating of the new notes[1]	**A for the series A-1 and A-2 notes The series B and C notes are not rated**	AAA for most of the LSS

1 Final data for 2008.

2 Three-month bankers' acceptance rate.

Given the nature of the underlying assets and their significant deterioration in the current economic context, the decrease in value applicable to the high-risk assets has been established at 100% of the notional amount of these securities as at December 31, 2008 (60% in 2007).

The assumptions regarding cash flows vary for each of the new variable-rate and long-term notes that will be issued, since they will have different credit ratings and risks.

The maturities vary according to the type of note because of the nature and the expected maturities of the underlying assets.

The Caisse has taken into account the probability that the historic cumulative default rates corresponding to the discount period will be more severe in the years to come. For the synthetic and hybrid assets, the estimated default rates apply to all the underlying assets.

INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS (cont.)

As already stated, the Caisse has provided funding facilities totalling $6,467 million to MAV 1, MAV 2 and a MAV 1 participant under the final restructuring plan. The Caisse will receive an annual commitment fee of 1.19% on the SFF totalling $300 million and 1.2% on the additional interest of $400 million in the MFF and will receive no commitment fee for the basic interest of $5,767 million of the MFF. The Caisse has estimated the financing premium normally required to be 1.6% in respect of the three facilities. In accordance with generally accepted accounting principles in Canada, the commitments to provide additional margin constitute lending commitments that must be recorded initially at their fair value. There is no active market from which the Caisse could derive the fair value of these commitments. Accordingly, the Caisse has established the fair value by applying a valuation technique that takes into account the fair value of substantially similar commitments and an analysis of discounted cash flows. The Caisse has included the financial impact of it in the valuation described previously. In the model used to determine the fair value of the ABCP, the Caisse has considered the fact that the triggers of collateral calls are based on spread-loss triggers linked more directly to the real behaviour of the reference portfolio of underlying assets, unlike certain mark-to-market triggers that reflect the price of credit more than the intrinsic credit quality of the same assets.

For the year ended December 31, 2007, the Caisse has not recorded interest income in respect of the third-party ABCP that it held from August 13, 2007. As at December 31, 2008, the cash flows considered in the model used to determine fair value include about $389 million of interest paid in January 2009 in respect of unpaid interest to August 31, 2008. Moreover, assumptions have also been made regarding the Caisse's share of the restructuring costs incurred to date as a member of the Pan-Canadian Investors Committee, less what will ultimately be recovered from the other participants in MAV 1 and MAV 2. The Caisse estimates that its cumulative net share of the restructuring costs could be $86 million, and that amount has been taken into account in the calculation of fair value.

Effect of the results on valuation

Given the foregoing, the Caisse as recorded against its portfolio of ABCP securities in difficulty a total decrease in value of $3,401 million and an asset writeoff of $171 million in its combined statement of income and changes in net assets for the year ended December 31, 2008, bringing its writeoffs and cumulative fair-value adjustments to $5,469 million. The decrease in fair value during the year ended December 31, 2008, is due mainly to downgrading of the notes to be received, wider credit spreads and deterioration of the credit market, resulting in lower estimates of the cash flow that will ultimately be received. The decreases in value observed for the high-risk assets and the securities of Devonshire Trust, as well as the commitments and the other particularities of the restructuring plan available at the valuation date, also contributed to this decrease.

The estimated fair value of the ABCP investments as at December 31, 2008, is not likely to be indicative of their definitive value or future fair value. Although management believes that its valuation technique is appropriate in the circumstances, changes to the main assumptions, including those used to determine the discount rates, the credit spreads, the expected returns, the credit risk of the underlying assets and the value of the various commitments and collateral, could have a material impact on the fair value of the new notes and the other ABCP securities in the years to come. Accordingly, resolution of these uncertainties could mean that the definitive value of the investments in subsequent periods differs considerably from management's current best estimates.

The most important assumptions regarding the model used by the Caisse to determine fair value are based on the financial impact of collateral calls, the default risk of the underlying assets, the loss rate in the event of default and the discount rates. The possible effect on the valuation technique of the variation in these assumptions and probabilities would change the estimated fair value of the ABCP investments as at December 31, 2008, as follows:

- An increase of 100 basis points in the financing premium in respect of the margin funding facilities would decrease the fair value by about $395 million;
- An increase of 100 basis points in the estimated discount rate would decrease the fair value by about $465 million; and
- A decrease in the expected credit rating of one notch would affect the anticipated default rates and would decrease the fair value by about $381 million.

The Caisse holds or has access to the funds required to meet all its financial, operational and regulatory obligations, and does not expect the illiquidity related to the ABCP to have a significant adverse impact on its financial health, credit rating or capital ratios.

INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS (cont.)

SUBSEQUENT EVENTS

In January 2009, the Caisse received the following assets after the completion of the third-party ABCP restructuring under the Pan-Canadian Investors Committee's agreement:

(in millions of dollars)	Notional amount	Fair value[2]	% of notes held
Liquid assets[1]	939	939	n.a.
MAV 1			
Class A-1	4,708	3,504	62%
Class A-2	3,951	2,913	62%
Class B	674	89	62%
Class C	289	–	62%
Tracking notes for high-risk assets	814	–	64%
MAV 2			
Class A-1	120	83	2%
Class A-2	38	27	1%
Class B	7	1	1%
Class C	5	–	2%
MAV 3			
Tracking notes for traditional assets	738	623	21%
Tracking notes for high-risk assets	76	–	14%

1 Represents repayment of principal of about $550 million on traditional assets and payment of $389 million of interest.

2 As a function of fair values established as at December 31, 2008. The Caisse is of the opinion that the fair value as at January 21, 2009, is much the same as that established as at December 31, 2008.

A subordination sequence is built into in the notes: the C notes are subordinate to the B notes, the B notes are subordinate to the A-2 notes, and the A-2 notes to the A-1 notes. This waterfall structure is designed to ensure that the subordinate tranches absorb the first losses so as to immunize the superior tranches. As a result of the waterfall structure, the C and B notes absorb the greatest decreases in value. In December 2008, DBRS issued an A rating for the A-1 and A-2 notes, but did not provide a credit rating for the B and C notes.

The MAV 3 securities received are tracking notes supported by assets that can be divided into three main groups:

/ Traditional assets in the amount of $496 million, consisting of good-quality commercial mortgage securities for which DBRS issued ratings ranging from A to AAA in January 2009;

/ Traditional assets in the amount of $242 million, consisting of interests in U.S. residential mortgage loans, which have been downgraded but are not considered high-risk; and

/ High-risk assets representing subprime U.S. residential mortgage loans in the amount of $76 million.

The various restructured notes bear interest at the following rates:

	Classes A-1, A-2 et B
MAV 1	BA + 0.30%
MAV 2	BA – 0.50%

The interest on the B notes is cumulative and is payable only when the principal and interest on the A-1 and A-2 notes have been paid in full.

All the tracking notes bear interest at a rate that will be adjusted as a function of the return on the underlying assets.

At the time of the preparation of these financial statements, there was still no active market for the various restructured notes. Moreover, the ability to transfer the MAV 1 notes is subject to considerable constraints.

The Caisse's ultimate ability to recover its investments in the replacement securities depends on the credit quality of the underlying assets.

INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS (cont.)

The assets underlying the restructured notes can be summarized as follows:

Underlying assets	MAV 1	MAV 2	Other conduits[1]
	%	%	%
LSS	74.6	75.9	75.0
Collateralized debt obligations	12.2	13.5	–
Commercial mortgage loans	7.6	6.5	25.0
Canadian non-prime residential mortgage loans	3.1	2.4	–
Other assets	2.5	1.7	–

1 The other conduits represent third-party ABCP not covered by the agreement and restructured bank-sponsored ABCP.

C / LIABILITIES RELATED TO INVESTMENTS

(in millions of dollars)		2008		2007
	Fair value	Cost	Fair value	Cost
Securities sold under repurchase agreements				
Canadian	19,161	19,120	30,084	29,786
Foreign	4,596	4,576	6,554	6,647
Commercial paper payable				
Canadian	5,415	5,407	1,990	1,990
Foreign	956	927	46	48
Short selling of securities				
Canadian	4,444	4,856	8,843	8,208
Foreign	3,344	3,304	7,716	7,498
Mortgage loans payable				
Canadian	935	932	277	269
Foreign	2,688	2,859	1,253	1,280
Other loans payable				
Canadian	672	691	1,564	1,553
Foreign	1,605	1,684	557	561
Amount pertaining to derivative instruments				
Canadian	1,277	37	291	20
Foreign	17,519	1,590	6,925	1,709
	62,612	45,983	66,100	59,569

D / NON-CONTROLLING INTERESTS

(in millions of dollars)		2008		2007
	Fair value	Cost	Fair value	Cost
Canadian	1,264	1,246	1,408	1,135
Foreign	551	769	643	671
	1,815	2,015	2,051	1,806

5.
DEPOSITORS' HOLDINGS

Demand and term deposits bear interest, and constitute indebtedness on the part of the Caisse toward the depositors.

During the year, the Caisse paid $39 million ($4 million in 2007) of interest on demand and term deposits.

Participation deposits are expressed in units, and each unit gives its holder a proportionate share in the net equity and the net income of a particular fund. At the end of each monthly period for the General Fund and the individual funds, the net investment income and the gains and losses on the sale of investments are distributed to participation deposit holders. At the beginning of the following period, the amounts distributed are paid out to (recovered from) the depositors' demand deposit accounts.

During the year, the Caisse paid $219 million ($10,921 million in 2007) in net income to participation deposit holders.

(in millions of dollars)	**2008**	2007
Caisse's indebtedness toward depositors		
Demand deposits	**2,038**	143
Term deposits	**98**	66
Interest on demand and term deposits	**2**	1
Net income to be paid out to participation deposit holders	**980**	317
	3,118	527
Participation deposit holders' holdings		
Participation deposits		
Balance, begginning of year	**131,560**	115,947
Units issued	**10,140**	16,882
Units cancelled	**(7,685)**	(1,269)
Balance, end of year	**134,015**	131,560
Gains (losses) not allocated on the sale of investments	**(257)**	17,283
Unrealized increase (decrease) in value of investments and other related assets and liabilities	**(16,788)**	5,980
	116,970	154,823
Depositor's holdings	**120,088**	155,350

6.

INVESTMENT INCOME, GAINS (LOSSES) ON THE SALE OF INVESTMENTS, AND UNREALIZED INCREASE (DECREASE) IN VALUE OF INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS

A / INVESTMENT INCOME

(in millions of dollars)	**2008**	2007
Fixed-income securities		
Short-term investments	**426**	685
Bonds	**2,841**	2,701
Mortgages *(note 6b)*	**457**	305
	3,724	3,691
Variable-income securities		
Equities and convertible securities	**1,639**	2,068
Real estate holdings *(note 6c)*	**830**	784
	2,469	2,852
Other income	**41**	61
Non-controlling interests	**(73)**	(73)
	6,161	6,531

Investment income – Fixed-income securities were reduced by $773 million ($1,221 million in 2007) in net expenses related to securities sold (acquired) under repurchase (reverse repurchase) agreements.

B / NET INCOME FROM MORTGAGES

(in millions of dollars)	**2008**	2007
Income from mortgages	**507**	424
Less:		
Expenses related to real estate debt subsidiaries		
Operation expenses	**31**	50
Financial costs of CMBS	**19**	69
	50	119
	457	305

INVESTMENT INCOME, GAINS (LOSSES) ON THE SALE OF INVESTMENTS, AND UNREALIZED INCREASE (DECREASE) IN VALUE OF INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS (cont.)

C / NET INCOME FROM REAL ESTATE HOLDINGS

(in millions of dollars)	2008	2007
Income from real estate holdings	**2,963**	2,482
Less:		
Expenses related to real estate subsidiaries		
Operating expenses related to real estate holdings	**1,556**	1,335
Operation expenses	**88**	99
Loan financial expenses	**499**	285
	2,143	1,719
Other income	**10**	21
	830	784

D / GAINS (LOSSES) ON THE SALE OF INVESTMENTS

(in millions of dollars)	2008	2007
Fixed-income securities		
Short-term investments	**96**	49
Bonds	**185**	306
Mortgages	**(43)**	23
	238	378
Variable-income securities		
Equities and convertible securities	**(22,828)**	8,789
Real estate holdings	**(507)**	458
	(23,335)	9,247
Non-controlling interests	**(9)**	(48)
	(23,106)	9,577
Less:		
Transactions costs of investments	**122**	150
	(23,228)	9,427

Gains (losses) on the sale of investments in bonds include $171 million of losses on the writeoff of assets related to third-party and bank-sponsored ABCP.

In addition, losses in the amount of $23,228 million (gains of $9,427 million in 2007) on the sale of investments recorded in the "Combined statement of income and changes in net assets" include $5,572 million in foreign exchange losses ($1,096 million in foreign exchange gains in 2007).

INVESTMENT INCOME, GAINS (LOSSES) ON THE SALE OF INVESTMENTS, AND UNREALIZED INCREASE (DECREASE) IN VALUE OF INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS (cont.)

E / UNREALIZED INCREASE (DECREASE) IN VALUE OF INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS

(in millions of dollars)	2008	2007
Fixed-income securities		
Short-term investments	**1,689**	217
Bonds	**4,496**	(1,291)
Mortgages	**(325)**	(124)
Securities acquired under reverse repurchase agreements	**(164)**	155
	5,696	(1,043)
Variable-income securities		
Equities and convertible securities	**(13,733)**	(3,144)
Real estate holdings	**(1,344)**	1,105
	(15,077)	(2,039)
Total investments	**(9,381)**	(3,082)
Less:		
Liabilities related to investments		
Securities sold under repurchase agreements	**(144)**	177
Commercial paper payable	**39**	(1)
Short selling of securities	**(1,225)**	(566)
Mortgage loans payable	**(149)**	(35)
Other loans payable	**(105)**	(23)
Derivative financial instruments	**11,682**	3,162
Non-controlling interests	**(445)**	64
	9,653	2,778
	(19,034)	(5,860)

The unrealized decrease in value in the amount of $19,034 million ($5,860 million in 2007) recorded in the "Combined statement of income and changes in net assets" includes an unrealized increase in value of $7,920 million related to foreign exchange (unrealized decrease in value of $3,633 million related to foreign exchange in 2007).

7. OPERATING EXPENSES

(in millions of dollars)	2008	2007
Salaries and employee benefits	**129**	140
Professional services	**52**	45
Data services and subscriptions	**18**	15
Premises and equipment	**17**	17
Depreciation of fixed assets	**19**	15
Other	**15**	15
	250	247
Safekeeping of securities	**13**	14
	263	261

8. IDENTIFICATION AND MANAGEMENT OF RISKS RELATED TO INVESTMENT OPERATIONS

The Caisse implemented a number of policies, guidelines and procedures to oversee operations. Investment policies oversee the range of activities performed at the portfolio managers level. For each specialized portfolio, the investment policy describes the philosophy, management type, investment universe, benchmark index, added value target and risk supervision, which includes concentration limits. Managers are aware of and must abide by the limits on their investment operations.

At the Caisse, risk management is based on an integrated risk management policy adopted by the Board of Directors. This policy, which is revised on a regular basis, is intended to promote a risk management culture and ensure appropriate risk management practices to help the Caisse better achieve its mission with depositors. More specifically, the risk management policy defines the governance and management of risk within the Caisse and establishes the level of risk that is acceptable in order to avoid excessive loss. In addition, this level of risk is related to the targeted value added to net assets, and promotes the efficient allocation of risk.

The governance of risk management is supported by three levels of control:

Level 1 – portfolio managers are primarily responsible for managing the risks related to their daily operations;

Level 2 – the Depositors and Risks committees (DRC and DRC – Transactions) and the Management committee; and

Level 3 – the Board of Directors and its Risk Management Committee, and Internal Audit.

The risk management policy includes reporting mechanisms for each of these levels. The policy also includes a framework for outsourcing management of investments, management of operational risks and management of derivative financial instruments.

To ensure the objectivity and rigour required to manage risks adequately, teams that are independent of portfolio managers are responsible for defining and monitoring the integrated risk management policy as well as the investment policies applying to the specialized portfolios.

The integrated risk management policy defines financial risks as follows:

A/ Market risk

B/ Credit and concentration risk

C/ Counterparty risk

D/ Financing liquidity risk

IDENTIFICATION AND MANAGEMENT OF RISKS RELATED TO INVESTMENT OPERATIONS (cont.)

A / MARKET RISK

Market risk represents the risk of financial loss deriving from changes in the value of financial instruments. The value of a financial instrument is impacted by changes in certain market variables such as interest rates, exchange rates, share and commodity prices, as well as their volatility. The risk derives from the volatility in the price of a financial instrument, which itself results from the volatility of such market variables.

The Caisse manages all market risks according to an integrated and comprehensive approach whereby major factors contributing to risk, such as industries, countries and issuers, are taken into account in analyzing market risk.

The Caisse can use derivative financial instruments traded either on exchanges or directly with banks and securities dealers, as part of the management of market risks deriving from its operations.

Market risk at the Caisse is measured using the method known as Value at Risk (VaR), which is based on the statistical measurement of the volatility of the market value of each position and its correlations. VaR is a statistical technique used to determine the worst loss expected during a given period based on a predetermined level of confidence. The Caisse uses a level of confidence of 84% in its calculations. The Caisse determines the VaR for each instrument included in all the specialized portfolios and aggregates the information for the overall portfolio.

The Caisse uses the historical simulation approach to estimating the VaR. A horizon of 800 days of observation of risk factors such as variations in exchange rates, interest rates and financial asset prices, is used to evaluate the volatility of returns and the correlation between various asset returns. The historical simulation approach is based essentially on the assumption that the future will be similar to the past. This approach requires that the series of historical data on all the risk factors used to estimate the returns on the instruments be available. In the absence of historical data, alternative methods are used.

The Caisse calculates two types of risk, the absolute risk and the active risk. The absolute risk, or absolute VaR, of the Caisse benchmark portfolio (target portfolio of depositors as a whole), is the result of the risk (volatility) of the benchmark indexes of the asset classes in the portfolio. For example, should depositors as a whole elect to increase the weight of equities in their benchmark portfolios, such risk would increase automatically due to the higher level of volatility of this asset class. Consequently, the expected absolute return would also increase. The absolute risk of the overall portfolio (comprised of the actual investments) equates the risk (volatility) of positions included in the overall portfolio. The absolute risk of the overall portfolio and that of the benchmark portfolio are calculated using the same method but they relate to different portfolios, the overall portfolio actually invested by the Caisse and the benchmark portfolio targeted by depositors.

The active risk, or VaR related to active management, represents the possibility that the Caisse record a return different from that of its benchmark portfolio as a result of its active management of the overall portfolio. The higher the active risk, the more the expected return from the overall portfolio will differ from the benchmark portfolio return.

The absolute risk of the Caisse's benchmark portfolio, the absolute risk of the overall portfolio and the active risk are measured on a regular basis.

The tables below show the overall portfolio's absolute risk and active risk for each specialized portfolio. The VaR relates to the large majority of assets held by the Caisse. The estimated market risk of instruments not included in the VaR related to the active management is measured on a quarterly basis by the Risk Management Committee of the Board of Directors.

IDENTIFICATION AND MANAGEMENT OF RISKS RELATED TO INVESTMENT OPERATIONS (CONT.)

ABSOLUTE RISK OF THE OVERALL PORTFOLIO

(in basis points)			2008
Specialized portfolios	**December 31, 2008**	**High**	**Low**
Short Term Investments (740)	43	44	3
Real Return Bonds (762)	849	849	602
Bonds (760)	363	363	331
Long Term Bonds (764)	734	734	643
Canadian Equity (720)	2,620	2,620	1,445
U.S. Equity – hedged (731)	2,535	2,535	1,383
U.S. Equity – unhedged (734)	2,540	2,540	1,546
Foreign Equity – hedged (730)	2,109	2,109	1,245
Foreign Equity – unhedged (733)	1,853	1,853	1,315
Emerging Markets Equity (732)	2,519	2,519	1,723
Québec International (761)	2,063	2,063	1,101
Investments and Infrastructures (781)	4,180	4,180	1,805
Private Equity (780)	3,601	3,601	1,970
Real Estate Debt (750)	780	1,036	488
Real Estate (710)	2,149	2,149	1,178
Commodity Financial Instruments (763)	1,792	1,882	1,666
Hedge Funds (770)	784	863	455
Asset Allocation (771)	66	66	12
Absolute risk of the overall portfolio	1,283	1,283	757

ACTIVE RISK OF THE OVERALL PORTFOLIO

(in basis points)			2008
Specialized portfolios	**December 31, 2008**	**High**	**Low**
Short Term Investments (740)	56	56	10
Real Return Bonds (762)	97	97	43
Bonds (760)	98	98	42
Long Term Bonds (764)	110	110	47
Canadian Equity (720)	245	263	210
U.S. Equity – hedged (731)	135	195	98
U.S. Equity – unhedged (734)	133	161	100
Foreign Equity – hedged (730)	81	173	67
Foreign Equity – unhedged (733)	82	214	59
Emerging Markets Equity (732)	184	252	184
Québec International (761)	159	194	33
Investments and Infrastructures (781)	2,607	2,607	1,066
Private Equity (780)	1,800	1,800	1,068
Real Estate Debt (750)	539	811	290
Real Estate (710)	390	390	209
Commodity Financial Instruments (763)	153	307	84
Hedge Funds (770)	249	339	69
Asset Allocation (771)	274	274	24
Active risk of the overall portfolio	444	444	213

IDENTIFICATION AND MANAGEMENT OF RISKS RELATED TO INVESTMENT OPERATIONS (cont.)

EXCHANGE RISK

The exchange risk represents the risk that the fair value or future cash flows of a financial instrument fluctuate due to variations in foreign currency prices. This risk is integrated in the overall measurement of VaR.

Also, as part of its exchange risk management, the Caisse uses instruments negotiated with banks; maturities generally range from one to twelve months for forward contracts and options, and from one to two years for foreign currency swaps. Upon maturity, new derivative financial instruments are negotiated in order to maintain effective long-term management of foreign exchange risks associated with investments and liabilities related to investments in foreign currencies.

The table below shows a summary of the allocation in foreign currency denominated net investments and amounts related to derivative products.

December 31, 2008
(in millions of dollars)

		Currency[1]					
	Canadian dollar	US dollar	Euro	GBP	Other	Subtotal	Total
Investments							
Fixed-income securities	73,839	11,964	1,952	1,555	2,761	18,232	92,071
Equities and convertible securities	12,055	18,077	5,912	3,346	6,503	33,838	45,893
Real estate holdings	11,884	4,245	5,341	762	684	11,032	22,916
Amounts receivable with respect to investments							
Securities acquired under reverse repurchase agreements	2,900	1,916	–	54	810	2,780	5,680
Amount pertaining to derivative instruments	2,465	11,037	1,365	607	459	13,468	15,933
	103,143	47,239	14,570	6,324	11,217	79,350	182,493
Liabilities related to investments							
Conventional debt	30,657	6,350	2,674	1,283	2,852	13,159	43,816
Amount pertaining to derivative instruments	1,277	14,146	2,298	524	551	17,519	18,796
	31,934	20,496	4,972	1,807	3,403	30,678	62,612
Subtotal	71,209	26,743	9,598	4,517	7,814	48,672	119,881
Non-controlling interests	1,264	170	42	339	–	551	1,815
Net investments	69,945	26,573	9,556	4,178	7,814	48,121	118,066

1 Investments are presented under the currency they are denominated in and are translated into Canadian dollars.

IDENTIFICATION AND MANAGEMENT OF RISKS RELATED TO INVESTMENT OPERATIONS (cont.)

December 31, 2007
(in millions of dollars)

		Currency[1]					
	Canadian dollar	US dollar	Euro	GBP	Other	Subtotal	Total
Investments							
Fixed-income securities	93,031	16,223	2,549	2,028	3,003	23,803	116,834
Equities and convertible securities	14,833	25,664	8,225	8,105	10,327	52,321	67,154
Real estate holdings	13,184	3,406	4,543	1,132	175	9,256	22,440
Amounts receivable with respect to investments							
Securities acquired under reverse repurchase agreements	2,462	2,235	925	447	1,374	4,981	7,443
Amount pertaining to derivative instruments	536	7,338	658	193	201	8,390	8,926
	124,046	54,866	16,900	11,905	15,080	98,751	222,797
Liabilities related to investments							
Conventional debt	42,830	8,740	2,480	1,349	3,485	16,054	58,884
Amount pertaining to derivative instruments	291	5,996	638	105	186	6,925	7,216
	43,121	14,736	3,118	1,454	3,671	22,979	66,100
Subtotal	80,925	40,130	13,782	10,451	11,409	75,772	156,697
Non-controlling interests	1,408	107	63	473	–	643	2,051
Net investments	79,517	40,023	13,719	9,978	11,409	75,129	154,646

1 Investments are presented under the currency they are denominated in and are translated into Canadian dollars.

The translation of the fair value of foreign currency investments into Canadian dollars results in a market impact of +$11,285 million (-$8,161 million in 2007). The impact of exchange rate hedging operations related to a portion of such investments is – $8,937 million (+$5,624 million in 2007). The net impact on net investment income is +$2,348 million (-$2,537 million in 2007).

INTEREST RATE RISK

The interest rate risk is the risk that the fair value or future cash flows of a financial instrument fluctuate due to changes in market interest rates. All of the interest bearing assets and liabilities as well as their effective rates are shown later in a table presenting the exposure to liquidity risk. This risk is integrated in the overall measurement of VaR.

PRICE RISK

Price risk is the risk that fair value or future cash flows fluctuate due to changes in market prices (other than changes deriving from the interest rate and foreign exchange risk), whether such changes derive from characteristics of the instrument itself or its issuer, or from elements affecting all similar financial instruments negotiated on the market. This risk is integrated in the overall measurement of VaR.

IDENTIFICATION AND MANAGEMENT OF RISKS RELATED TO INVESTMENT OPERATIONS (cont.)

B / CREDIT AND CONCENTRATION RISK

Credit risk is the possibility of a loss of market value in the event that a borrower, endorser, guarantor or counterparty does not honour its obligation to repay a loan or to fulfill any other financial commitment, or sees its financial situation deteriorate.

The analysis of concentration risk measures the fair value of a group of financial products (fixed-income and variable-income securities) related to a single issuer or a group of issuers[1] with similar characteristics (geographical area, industry, credit rating).

The concentration limit by group of issuers was set at 3% of the Caisse's total assets, with the exception of securities issued by the Government of Canada, the Government of Québec or another Canadian province or territory, as well as by their departments and agencies, which are not subject to concentration limits[2] . Sovereign issuers with a credit rating of AAA are also excluded from this limit on concentration.

As at December 31, 2008, the concentration by credit rating of the Caisse's group of issuers was as follows:

	Value in % of investments [3]
Credit rating:[4]	
AAA – AA	23.5%
A	15.3%
BBB	5.6%
BB or lower	2.5%
No credit rating:	
/ Real estate assets	20.1%
/ Third-party and bank-sponsored ABCP[5]	4.7%
/ Private equity	7.1%
/ Private equity funds and hedge funds	9.0%
/ Mortgages and mortgage securities	7.1%
/ Other	5.1%
Total	100.0%

1 A group of issuers represents a number of issuers under the control of a parent company.

2 The exposure to an issuer deriving from positions in derivative financial instruments is not accounted for in the concentration risk analysis.

3 The percentage of investments represents net positions by group of issuers.

4 Credit ratings are obtained from major credit rating agencies and are aggregated according to an algorithm developed in house. For purposes of this concentration, the only ratings used are long-term credit ratings from major credit rating agencies.

5 As state in note 4b, the new MAV 1 and MAV 2 notes resulting from the restructuring of third-party and bank-sponsored ABCP will be rated A.

The analysis of credit risk includes measuring the probability of default and the rate of recovery on debt securities held by the Caisse, as well as monitoring the changes in the credit ratings of issuers and groups of issuers whose securities are held in the Caisse portfolios.

In 2008, the major credit rating agencies increased the long-term credit rating of 115 groups of issuers held in the Caisse portfolios, while 223 groups of issuers were awarded lower ratings.

In the table above, groups of issuers for which no credit rating is available were categorized. For most of these groups, the absence of a credit rating is explained by the private quality of the investments, the absence of any debt, the restructuring of investments or a combination of these elements.

In the case of mortgages not awarded a credit rating, the analysis of credit risk is based in part on the loan-to-value ratio. In this ratio, the amount of the loan is divided by the market value of any asset received as collateral at the subscription date or the date funds were awarded, or at any other moment during the term of the loan.

IDENTIFICATION AND MANAGEMENT OF RISKS RELATED TO INVESTMENT OPERATIONS (cont.)

The table below shows the breakdown of mortgages by stratum of the loan-to-value ratio:

Loan-to-value ratio	Value in % of mortgages
0 to 55%	**11.6%**
55 to 65%	**26.8%**
65 to 75%	**45.0%**
75 to 85%	**16.4%**
More than 85%	**0.2%**

It is important to note that the Caisse manages all loans and obligations, including mortgages and private corporate bonds, following the same approach as for any financial asset in the bonds portfolio, which means in terms of total return rather than based on the various factors that can affect fair value such as the credit risk.

C / COUNTERPARTY RISK

Counterparty risk represents the credit risk from current and potential exposure related to transactions involving over-the-counter derivative financial instruments.

Transactions involving derivative financial instruments are negotiated with financial institutions whose credit rating is established by a recognized credit rating agency and whose operational limits are specified by management. In addition, the Caisse signs agreements making it possible to benefit from the offsetting effect of amounts at risk and the exchange of collaterals in order to limit its net exposure to this credit risk.

Risk is measured by counterparty, according to the agreement in effect, on the basis of which it is possible to calculate the net exposure resulting from over-the-counter derivative financial instruments and collaterals exchanged.

As at December 31, 2008, the Caisse's net exposure to counterparty risk totalled $496 million and involved 68 active counterparties.

D / FINANCING LIQUIDITY RISK

The financing liquidity risk corresponds to the possibility that the Caisse may not always be able to fulfill its commitments without having to obtain funds at abnormally high prices or sell assets.

Compliance with established rules is monitored on a monthly basis, and the liquidity status is determined daily. The Caisse uses various scenario simulations to estimate the potential impact on cash. Cash managers evaluate the liquidity of markets on which the Caisse obtains financing for its operations. They also ensure the Caisse is active on various financial markets and maintains relationships with credit rating agencies that rate the Caisse as well as capital providers.

IDENTIFICATION AND MANAGEMENT OF RISKS RELATED TO INVESTMENT OPERATIONS (cont.)

The table below presents a summary of maturities at par value of investments and liabilities related to investments.

(in millions of dollars)	2008					2007	
	Less than 2 years	2 to 5 years	More than 5 years	Total	Effective interest rate	Total par value	Effective interest rate
Fixed-income securities							
Short-term investments							
Canadian	6,125	68	–	6,193	2.5%	9,913	4.8%
Foreign	4,423	12	–	4,435	4.5%	4,810	6.9%
	10,548	80	–	10,628	3.3%	14,723	5.5%
Bonds							
Securities issued or guaranteed by:							
Canadian government	1,295	5,152	7,640	14,087	2.9%	21,376	4.2%
Province of Québec	257	697	7,037	7,991	4.7%	7,088	4.9%
Other Canadian provinces	–	63	2,841	2,904	4.6%	2,173	4.7%
Municipalities and other Canadian bodies	369	450	843	1,662	4.8%	1,772	5.1%
Canadian government corporations	90	5,408	3,883	9,381	4.0%	11,855	4.6%
U.S. government	–	–	886	886	3.7%	198	4.3%
Other foreign governments	180	–	1,504	1,684	3.6%	1,720	2.9%
Mortgage securities							
Canadian	6	234	57	297	12.3%	307	12.2%
Foreign	2,357	356	3,608	6,321	11.6%	3,053	11.1%
Canadian corporations	3,443	1,995	7,921	13,359	4.5%	16,386	5.3%
Foreign corporations	1,800	649	1,934	4,383	5.5%	5,153	6.7%
Inflation-indexed securities							
Canadian	–	17	392	409	2.1%	630	2.1%
Foreign	98	282	1,684	2,064	1.3%	3,178	1.8%
	9,895	15,303	40,230	65,428	4.7%	74,889	4.9%
Third-party and bank-sponsored ABCP	–	–	12,787	12,787	–	12,607	–
Mortgages							
Canadian	2,987	1,670	1,780	6,437	6.0%	5,946	7.0%
Foreign	4,185	998	555	5,738	6.0%	4,574	7.8%
	7,172	2,668	2,335	12,175	6.0%	10,520	7.3%
	27,615	18,051	55,352	101,018	4.8%	112,739	5.3%
Amounts receivable with respect to investments							
Securities acquired under reverse repurchase agreements							
Canadian	2,901	–	–	2,901	1.6%	2,525	4.4%
Foreign	2,780	–	–	2,780	0.2%	4,603	3.0%
	5,681	–	–	5,681	0.9%	7,128	3.5%
Liabilities related to investments							
Securities sold under repurchase agreements	23,636	–	–	23,636	2.1%	36,573	4.1%
Commercial paper payable	6,388	–	–	6,388	2.3%	2,050	4.8%
Short selling of securities	–	324	2,144	2,468	2.8%	8,678	3.5%
Mortgage loans payable	1,052	2,396	343	3,791	5.6%	1,549	6.8%
Other loans payable	2,227	255	–	2,482	2.5%	2,128	4.5%
	33,303	2,975	2,487	38,765	2.6%	50,978	4.2%

9.
DERIVATIVE FINANCIAL INSTRUMENTS

Derivative financial instruments are financial contracts whose value fluctuates on the basis of the underlying asset, and which do not require holding or delivering the underlying asset itself. This underlying value may be of a financial nature (interest rate, foreign currency, stock market security or index) or a commodity (precious metal, foodstuff or oil).

The notional amount of a derivative financial instrument represents the value of the notional principal to which a rate or a price applies to determine the exchange of future cash flows, and does not reflect the credit risk pertaining to the instrument.

The Caisse uses derivative financial instruments that include the following:

> Forward contracts and futures contracts are undertakings that enable the purchase or sale of an underlying value, the quantity and price of which are determined in the contract, which includes a predetermined delivery date. A forward contract involves customized conditions negotiated directly between the parties on the over-the-counter market. A futures contract has terms and conditions determined by an organized market.
>
> A swap is a transaction whereby two parties agree to exchange financial returns on predetermined conditions that include a notional amount and a term.
>
> An option is a contract negotiated by mutual agreement or traded on an organized market that gives the purchaser the right, but not the obligation, to buy or sell a given amount of an underlying security, index or commodity, at a strike price stipulated in advance, either at a determined date or at any time before a specified maturity date.

Foreign exchange risk arises from investments and liabilities related to investments denominated in foreign currencies, as well as from related derivative financial instruments.

Derivative instruments that are traded on exchanges or with banks and securities dealers are used to manage the interest rate and market risks of the total investment portfolio, as well as to generate income from transactions, which is included in investment income from fixed-income and variable-income securities.

DERIVATIVE FINANCIAL INSTRUMENTS (cont.)

A / SUMMARY OF DERIVATIVE FINANCIAL INSTRUMENTS

(in millions of dollars)				2008	2007
		Fair value			
	Notional amount	Assets	Liabilities	Net amount	Net amount
Foreign exchange risk management					
Foreign currency swaps					
Purchases	2,296	8	159	(151)	302
Sales	1,221	5	277	(272)	(10)
Forward contracts	21,727	552	1,957	(1,405)	769
Over-the-counter foreign currency options					
Purchases	636	17	–	17	5
Sales	465	–	9	(9)	–
	26,345	582	2,402	(1,820)	1,066
Interest rate and market risk management					
Interest rate and foreign currency swaps	153,225	5,857	5,876	(19)	(117)
Equity swaps	39,766	1,291	1,798	(507)	196
Credit risk swaps	19,618	1,038	1,076	(38)	18
Commodity swaps	16,677	2,300	1,881	419	43
Forward contracts	76,266	1,854	2,885	(1,031)	(39)
Futures contracts	38,613	–	–	–	–
Over-the-counter options					
Purchases	57,516	2,644	–	2,644	1,892
Sales	55,041	–	2,680	(2,680)	(1,414)
Exchange-traded options					
Purchases	11,641	326	–	326	242
Sales	12,699	–	198	(198)	(234)
Warrants	128	41	–	41	57
	481,190	15,351	16,394	(1,043)	644
Total derivative financial instrument contracts	507,535	15,933	18,796	(2,863)	1,710

DERIVATIVE FINANCIAL INSTRUMENTS (cont.)

B / SUMMARY OF DERIVATIVE FINANCIAL INSTRUMENT MATURITIES

(in millions of dollars)				2008	2007
	Notional amount – Maturity				
	Less than 2 years	2 to 5 years	More than 5 years	Total	Notional amount
Foreign exchange risk management					
Foreign currency swaps					
Purchases	881	1,415	–	2,296	1,804
Sales	93	579	549	1,221	1,742
Forward contracts	21,610	9	108	21,727	45,758
Over-the-counter foreign currency options					
Purchases	421	203	12	636	171
Sales	421	44	–	465	–
	23,426	2,250	669	26,345	49,475
Interest rate and market risk management					
Interest rate and foreign currency swaps	24,271	46,954	82,000	153,225	225,677
Equity swaps	26,636	267	12,863	39,766	57,553
Credit risk swaps	5,394	12,776	1,448	19,618	20,124
Commodity swaps	14,551	2,126	–	16,677	25,729
Forward contracts	70,955	5,311	–	76,266	44,007
Futures contracts	16,512	17,784	4,317	38,613	48,223
Over-the-counter options					
Purchases	34,462	11,794	11,260	57,516	66,286
Sales	29,430	14,530	11,081	55,041	60,896
Exchange-traded options					
Purchases	11,231	410	–	11,641	46,280
Sales	12,181	518	–	12,699	31,087
Warrants	56	48	24	128	210
	245,679	112,518	122,993	481,190	626,072
Total derivative financial instrument contracts	269,105	114,768	123,662	507,535	675,547

10.
SECURIZATIONS

During the year, no securitization operations were performed by Caisse subsidiaries ($2,273 million in 2007).

In the course of Caisse securitization operations, CMBS and notes payable acquired by the Caisse over the last few years from a collateralized security entity are recorded in the "Combined statement of net assets" under Mortgages securities. As at December 31, 2008, these securities amounted to $648 million ($1,699 million in 2007). Securitization operations have allowed companies under common control to generate management fees representing $21 million during the year ($4 million in 2007). No losses are expected owing to the nature and quality of such loans.

11.
COMMITMENTS AND CONTINGENCIES

Given the nature of its operations, the Caisse has a number of commitments.

Commitments to buy investments mean the Caisse is committed to buying investments that will be settled in the coming financial years, in accordance with the terms and conditions in each agreement.

For the Caisse, collaterals and loan guarantees consist in securing future income deriving from the sale of investments and transactions on derivatives as well as the reimbursement of loans made by investee companies to financial institutions and corporations. Collaterals related to the reimbursement of loans have no specific maturity date, except in some cases, where terms vary between one to nine years.

(in millions of dollars)	**2008**	2007
Commitments to buy investments	**16,277**	20,940
Collaterals and loan guarantees (maximum amount)	**802**	803
Third-party and bank-sponsored ABCP[1]	**6,790**	5,153
	23,869	26,896

1 For the description of the commitments related to third-party and bank-sponsored ABCP, refer to note 4b.

12.
COLLATERALS

In the normal course of business, the Caisse conducts transactions involving the lending and the borrowing of securities and on derivative products, in exchange for collaterals or assets, with various counterparties with which clearing agreements have been concluded to limit credit risk. In such transactions, the Caisse received assets as collateral. As at December 31, 2008, the Caisse had pledged and received as collateral assets for amounts of $36,959 million and $7,070 million ($51,656 million and $11,330 million in 2007) respectively. The amount of assets pledged as collateral includes assets with a value of $2,281 million ($723 million in 2007), which were pledged with depositaries to participate in clearing and payment systems.

13.
SUBSEQUENT EVENTS

In January of 2009, the Caisse received assets on completion of the restructuration of third-party ABCP under the agreement of the Pan-Canadian Investors Committee. The details of the assets received are given in note 4b under the heading "Subsequent events".

14.
COMPARATIVE FIGURES

Certain figures from the 2007 financial statements have been reclassified to conform to the presentation adopted in 2008.

SUPPLEMENTARY INFORMATION

SUMMARY FINANCIAL STATEMENTS FOR THE SPECIALIZED PORTFOLIOS

(in millions of dollars)	SHORT TERM INVESTMENTS (740)		REAL RETURN BONDS (762)		BONDS (760)		LONG TERM BONDS (764)		CANADIAN EQUITY (720)	
Consolidated net assets as at December, 31	**2008**	2007	**2008**	2007	**2008**	2007	**2008**	2007	**2008**	2007
Assets										
Investments at fair value										
Real estate holdings	–	–	–	–	–	–	–	–	–	–
Equities and convertible securities	–	–	–	–	–	–	–	–	**10,386.4**	12,949.3
Bonds	–	–	**579.4**	871.0	**65,233.9**	71,430.7	**3,075.2**	3,174.7	–	–
Mortgages	–	–	–	–	–	–	–	–	–	–
Mortgages securities	–	–	–	–	–	–	–	–	–	–
Short-term investments	**4,531.3**	762.1	–	–	**16,198.3**	18,074.2	–	–	**6,494.4**	11,329.0
Securities acquired under reverse repurchase agreements	–	767.3	–	–	**7,126.2**	15,148.7	–	17.8	–	–
Real estate held for resale	–	–	–	–	–	–	–	–	–	–
Third-party and bank-sponsored ABCP	–	–	–	–	**7,186.2**	10,739.4	–	–	–	–
Derivative financial instruments related to third-party and bank-sponsored ABCP	–	–	–	–	**5,601.1**	1,867.1	–	–	–	–
Demand deposits in the General Fund	–	1,610.6	–	61.3	–	–	**1,406.8**	1,237.2	–	363.2
	4,531.3	3,140.0	**579.4**	932.3	**101,345.7**	117,260.1	**4,482.0**	4,429.7	**16,880.8**	24,641.5
Other assets	–	6.4	**5.4**	2.4	**2,263.8**	2,727.8	**32.8**	36.0	**76.8**	34.2
	4,531.3	3,146.4	**584.8**	934.7	**103,609.5**	119,987.9	**4,514.8**	4,465.7	**16,957.6**	24,675.7
Liabilities										
Advances from the General Fund	**62.7**	–	**18.4**	–	**1,785.8**	10,670.9	–	–	**270.9**	–
Securities sold under repurchase agreements	–	779.1	–	72.7	**20,615.1**	33,110.3	**1,448.2**	1,266.9	–	–
Notes payable	–	–	–	–	**21,299.0**	19,323.6	–	–	–	–
Temporary funding attributable to foreign currency fluctuations	–	–	–	–	–	–	–	–	–	–
Loans payable	–	–	–	–	–	–	–	–	–	–
Mortgage loans payable	–	–	–	–	–	–	–	–	–	–
Commercial mortgage-backed securities	–	–	–	–	–	–	–	–	–	–
Participating debenture	–	–	–	–	–	–	–	–	–	–
Short selling of securities	–	–	–	–	**5,866.5**	15,073.2	–	21.9	**3,271.4**	3,677.2
Derivative financial instruments	–	1.9	–	–	**9,221.1**	1,776.5	–	–	**524.3**	216.4
Other liabilities	**6.6**	5.4	**4.8**	–	**510.8**	822.0	**38.5**	13.3	**64.2**	850.7
Non-controlling interests	–	–	–	–	–	–	–	–	–	–
	69.3	786.4	**23.2**	72.7	**59,298.3**	80,776.5	**1,486.7**	1,302.1	**4,130.8**	4,744.3
Net holdings of funds	**4,462.0**	2,360.0	**561.6**	862.0	**44,311.2**	39,211.4	**3,028.1**	3,163.6	**12,826.8**	19,931.4
Statement of consolidated income for the year ended December, 31										
Income										
Investment income										
Real estate holdings	–	–	–	–	–	–	–	–	–	–
Equities and convertible securities	–	–	–	–	–	–	–	–	**468.0**	434.3
Bonds	–	–	**31.4**	39.7	**923.7**	1,476.8	**137.2**	134.3	–	–
Mortgages	–	–	–	–	–	–	–	–	–	–
Mortgage securities	–	–	–	–	–	–	–	–	–	–
Short-term investments	**65.1**	440.6	–	–	**584.8**	640.1	–	–	**316.7**	520.6
Demand deposits in (advances from) the General Fund	**(2.8)**	158.9	**(0.6)**	(0.5)	**55.1**	(112.1)	**1.1**	3.9	**(15.1)**	(23.7)
	62.3	599.5	**30.8**	39.2	**1,563.6**	2,004.8	**138.3**	138.2	**769.6**	931.2
Other income	–	–	–	–	–	–	–	–	**6.3**	–
	62.3	599.5	**30.8**	39.2	**1,563.6**	2,004.8	**138.3**	138.2	**775.9**	931.2
Operating expenses	**0.2**	1.0	**0.6**	0.8	**35.9**	37.6	**2.3**	2.4	**32.8**	35.7
External management fees	–	–	–	–	–	–	–	–	–	–
Income before the following items	**62.1**	598.5	**30.2**	38.4	**1,527.7**	1,967.2	**136.0**	135.8	**743.1**	895.5
Interest on loans and notes payable	–	461.0	–	–	**290.9**	56.4	–	–	–	0.6
Non-controlling interests	–	–	–	–	–	–	–	–	–	–
Net investment income (loss)	**62.1**	137.5	**30.2**	38.4	**1,236.8**	1,910.8	**136.0**	135.8	**743.1**	894.9
Changes in consolidated net assets for the year ended December, 31										
Net investment results										
Net investment income (loss)	**62.1**	137.5	**30.2**	38.4	**1,236.8**	1,910.8	**136.0**	135.8	**743.1**	894.9
Gains (losses) on sale of investments	**23.3**	(28.3)	**31.2**	11.3	**1,173.6**	394.8	**45.4**	(22.7)	**(3,961.2)**	2,056.4
Unrealized increase (decrease) in value of investments and liabilities related to investments	**(6.1)**	16.9	**(51.4)**	(39.8)	**(405.2)**	(938.0)	**(44.3)**	28.2	**(3,039.3)**	(539.6)
Net investment results	**79.3**	126.1	**10.0**	9.9	**2,005.2**	1,367.6	**137.1**	141.3	**(6,257.4)**	2,411.7
Participation units issued (cancelled)	**2,084.8**	(317.6)	**(280.2)**	(169.7)	**4,331.4**	4,010.2	**(136.6)**	(23.1)	**(104.1)**	(398.9)
Net investment loss (net income) recovered from (allocated to) participation unit holders	**(62.1)**	(137.5)	**(30.2)**	(38.4)	**(1,236.8)**	(1,910.8)	**(136.0)**	(135.8)	**(743.1)**	(894.9)
Increase (decrease) in consolidated net assets	**2,102.0**	(329.0)	**(300.4)**	(198.2)	**5,099.8**	3,467.0	**(135.5)**	(17.6)	**(7,104.6)**	1,117.9
Consolidated net assets, beginning of year	**2,360.0**	2,689.0	**862.0**	1,060.2	**39,211.4**	35,744.4	**3,163.6**	3,181.2	**19,931.4**	18,813.5
Consolidated net assets, end of year	**4,462.0**	2,360.0	**561.6**	862.0	**44,311.2**	39,211.4	**3,028.1**	3,163.6	**12,826.8**	19,931.4
Investments and liabilities at cost as at December, 31										
Assets										
Investments										
Real estate holdings	–	–	–	–	–	–	–	–	–	–
Equities and convertible securities	–	–	–	–	–	–	–	–	**11,468.5**	10,134.5
Bonds	–	–	**598.0**	838.2	**59,022.8**	69,942.1	**3,035.0**	3,090.1	–	–
Mortgages	–	–	–	–	–	–	–	–	–	–
Mortgages securities	–	–	–	–	–	–	–	–	–	–
Short-term investments	**4,530.4**	759.3	–	–	**13,852.3**	17,798.9	–	–	**6,410.7**	11,319.2
Securities acquired under reverse repurchase agreements	–	773.2	–	–	**7,116.5**	15,078.1	–	18.0	–	–
Real estate held for resale	–	–	–	–	–	–	–	–	–	–
Third-party and bank-sponsored ABCP	–	–	–	–	**12,787.3**	12,606.5	–	–	–	–
Demand deposits in the General Fund	–	1,610.6	–	61.3	–	–	**1,406.8**	1,237.2	–	363.2
	4,530.4	3,143.1	**598.0**	899.5	**92,778.9**	115,425.6	**4,441.8**	4,345.3	**17,879.2**	21,816.9
Liabilities										
Securities sold under repurchase agreements	–	790.7	–	72.7	**20,572.9**	33,063.3	**1,448.3**	1,267.1	–	–
Notes payable	–	–	–	–	**21,277.5**	19,322.2	–	–	–	–
Temporary funding attributable to foreign currency fluctuations	–	–	–	–	–	–	–	–	–	–
Loans payable	–	–	–	–	–	–	–	–	–	–
Mortgage loans payable	–	–	–	–	–	–	–	–	–	–
Commercial mortgage-backed securities	–	–	–	–	–	–	–	–	–	–
Participating debenture	–	–	–	–	–	–	–	–	–	–
Short selling of securities	–	–	–	–	**5,689.8**	15,084.3	–	22.0	**3,760.2**	3,079.9
Derivative financial instruments	–	0.2	–	–	**1,000.4**	490.1	–	–	**12.2**	6.6
Non-controlling interests	–	–	–	–	–	–	–	–	–	–

U.S. EQUITY HEDGED (731)		U.S. EQUITY UNHEDGED (734)		FOREIGN EQUITY HEDGED (730)		FOREIGN EQUITY UNHEDGED (733)		EMERGING MARKETS EQUITY (732)		QUÉBEC INTERNATIONAL (761)		INVESTMENTS AND INFRASTRUCTURES (781)		PRIVATE EQUITY (780)	
2008	2007	2008	2007	2008	2007	2008	2007	2008	2007	2008	2007	2008	2007	2008	2007
–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
1,250.3	7,131.5	–	–	4,164.7	11,207.8	–	–	2,999.6	4,806.8	218.9	1,625.6	6,671.7	8,875.4	11,766.8	11,995.1
–	–	–	–	–	–	–	–	–	–	4,975.9	12,106.8	1,529.7	1,630.3	285.1	384.0
–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
2,206.3	1,413.5	1,896.7	4,245.2	0.4	17.5	3,468.5	6,549.8	–	172.5	1,548.7	3,658.1	3,545.4	3,910.8	401.9	358.1
–	–	–	–	–	–	–	–	–	–	148.9	477.5	–	–	–	–
–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
650.3	1,403.0	–	–	–	159.5	149.3	–	29.5	45.8	–	8,965.2	–	–	–	–
4,106.9	9,948.0	1,896.7	4,245.2	4,165.1	11,384.8	3,617.8	6,549.8	3,029.1	5,025.1	6,892.4	26,833.2	11,746.8	14,416.5	12,453.8	12,737.2
48.5	44.4	5.0	20.1	45.1	25.2	3.0	6.7	8.0	7.1	71.0	164.5	60.8	87.8	19.6	36.3
4,155.4	9,992.4	1,901.7	4,265.3	4,210.2	11,410.0	3,620.8	6,556.5	3,037.1	5,032.2	6,963.4	26,997.7	11,807.6	14,504.3	12,473.4	12,773.5
–	–	28.2	37.7	145.3	–	–	148.2	–	–	468.4	–	654.9	401.1	111.3	766.7
–	–	–	–	–	–	–	–	–	–	1,404.8	9,969.6	–	–	–	–
1,881.1	4,481.8	–	–	3,436.5	6,940.1	–	–	–	–	297.3	924.8	5,563.8	6,730.9	797.3	474.2
–	–	–	–	–	–	–	–	–	–	–	–	–	–	1,400.0	–
–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
1,294.0	2,490.3	–	–	61.4	115.4	–	–	–	–	233.1	1,058.6	–	–	119.5	145.7
610.1	201.1	–	24.9	41.6	108.4	42.4	112.6	5.2	6.6	90.5	13.8	544.6	36.1	308.7	40.0
23.9	297.9	2.8	14.9	13.6	634.1	1.5	–	20.5	23.4	249.4	475.0	47.1	31.2	19.4	14.9
–	–	–	–	–	–	–	–	–	–	–	–	723.9	896.2	–	–
3,809.1	7,471.1	31.0	77.5	3,698.4	7,798.0	43.9	260.8	25.7	30.0	2,743.5	12,441.8	7,534.3	8,095.5	2,756.2	1,441.5
346.3	2,521.3	1,870.7	4,187.8	511.8	3,612.0	3,576.9	6,295.7	3,011.4	5,002.2	4,219.9	14,555.9	4,273.3	6,408.8	9,717.2	11,332.0
–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
104.1	227.1	–	–	456.9	712.9	–	–	125.7	87.2	17.2	16.9	309.2	298.6	133.3	218.0
–	–	–	–	–	–	–	–	–	–	459.6	476.7	92.1	88.7	44.0	38.9
–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
109.7	29.7	154.2	173.5	4.5	2.2	286.3	436.7	4.4	5.9	112.0	131.1	229.7	275.4	47.8	52.4
(3.5)	7.7	0.1	0.2	0.8	(13.9)	(0.7)	0.6	4.4	2.0	(22.3)	22.6	(15.7)	(10.1)	(9.5)	(2.9)
210.3	264.5	154.3	173.7	462.2	701.2	285.6	437.3	134.5	95.1	566.5	647.3	615.3	652.6	215.6	306.4
–	–	–	–	–	–	–	–	–	–	–	–	18.6	27.6	2.6	23.0
210.3	264.5	154.3	173.7	462.2	701.2	285.6	437.3	134.5	95.1	566.5	647.3	633.9	680.2	218.2	329.4
6.6	7.2	19.7	18.2	7.4	8.9	13.4	16.3	15.6	12.3	20.0	11.9	35.8	34.3	23.6	26.8
0.9	3.5	3.8	9.5	7.3	6.7	12.7	12.3	10.6	15.4	8.7	3.5	–	–	4.0	7.6
202.8	253.8	130.8	146.0	447.5	685.6	259.5	408.7	108.3	67.4	537.8	631.9	598.1	645.9	190.6	295.0
158.0	182.0	–	–	305.7	467.8	–	–	–	–	32.8	41.1	300.3	354.2	3.9	4.6
–	–	–	–	–	–	–	–	–	–	–	–	27.1	25.9	–	–
44.8	71.8	130.8	146.0	141.8	217.8	259.5	408.7	108.3	67.4	505.0	590.8	270.7	265.8	186.7	290.4
44.8	71.8	130.8	146.0	141.8	217.8	259.5	408.7	108.3	67.4	505.0	590.8	270.7	265.8	186.7	290.4
(1,057.1)	1,207.3	(1,357.8)	(609.2)	(156.8)	1,133.3	(2,315.2)	(416.5)	(403.0)	601.9	(7,779.4)	105.1	(143.3)	1,673.8	(1,472.2)	1,338.8
478.9	(1,347.0)	108.9	(185.8)	(1,556.8)	(1,258.7)	91.0	(341.4)	(2,131.0)	32.8	(111.2)	(60.3)	(3,685.0)	(1,096.1)	(3,124.8)	(114.2)
(533.4)	(67.9)	(1,118.1)	(649.0)	(1,571.8)	92.4	(1,964.7)	(349.2)	(2,425.7)	702.1	(7,385.6)	635.6	(3,557.6)	843.5	(4,410.3)	1,515.0
(1,596.8)	891.2	(1,068.2)	(542.7)	(1,386.6)	576.1	(494.6)	855.1	543.2	74.7	(2,445.4)	1,442.5	1,692.8	(2,813.2)	2,982.2	1,971.7
(44.8)	(71.8)	(130.8)	(146.0)	(141.8)	(217.8)	(259.5)	(408.7)	(108.3)	(67.4)	(505.0)	(590.8)	(270.7)	(265.8)	(186.7)	(290.4)
(2,175.0)	751.5	(2,317.1)	(1,337.7)	(3,100.2)	450.7	(2,718.8)	97.2	(1,990.8)	709.4	(10,336.0)	1,487.3	(2,135.5)	(2,235.5)	(1,614.8)	3,196.3
2,521.3	1,769.8	4,187.8	5,525.5	3,612.0	3,161.3	6,295.7	6,198.5	5,002.2	4,292.8	14,555.9	13,068.6	6,408.8	8,644.3	11,332.0	8,135.7
346.3	2,521.3	1,870.7	4,187.8	511.8	3,612.0	3,576.9	6,295.7	3,011.4	5,002.2	4,219.9	14,555.9	4,273.3	6,408.8	9,717.2	11,332.0
–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
1,225.8	7,317.5	–	–	5,153.3	10,677.3	–	–	4,096.9	3,768.6	247.1	1,645.2	9,087.4	8,449.6	16,447.2	13,883.0
–	–	–	–	–	–	–	–	–	–	4,803.3	11,952.0	1,732.4	1,687.4	563.6	556.9
–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
2,222.6	1,447.0	1,862.5	4,294.9	–	17.4	3,392.8	6,495.0	–	175.6	1,556.6	3,660.4	4,515.2	3,908.6	412.2	357.6
–	–	–	–	–	–	–	–	–	–	148.9	480.2	–	–	–	–
–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
650.3	1,403.0	–	–	–	159.5	149.3	–	29.5	45.8	–	8,965.2	–	–	–	–
4,098.7	10,167.5	1,862.5	4,294.9	5,153.3	10,854.2	3,542.1	6,495.0	4,126.4	3,990.0	6,755.9	26,703.0	15,335.0	14,045.6	17,423.0	14,797.5
–	–	–	–	–	–	–	–	–	–	1,404.9	9,972.8	–	–	–	–
1,862.5	4,534.9	–	–	3,392.8	6,995.2	–	–	–	–	297.4	946.8	6,091.5	6,698.0	857.9	508.8
–	–	–	–	–	–	–	–	–	–	–	–	–	–	1,400.0	–
–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
1,605.1	2,062.5	–	–	59.1	119.1	–	–	–	–	250.9	1,092.3	–	–	84.1	83.4
34.9	41.9	–	–	–	0.1	–	–	–	–	3.6	3.6	3.9	4.2	–	–
–	–	–	–	–	–	–	–	–	–	–	–	989.8	939.8	–	–

SUPPLEMENTARY INFORMATION

SUMMARY FINANCIAL STATEMENTS FOR THE SPECIALIZED PORTFOLIOS (cont.)

(in millions of dollars)	REAL ESTATE DEBT (750)		REAL ESTATE (710)		COMMODITY FINANCIAL INSTRUMENTS (763)		HEDGE FUNDS (770)		ASSET ALLOCATION (771)	
Consolidated net assets as at December, 31	**2008**	2007	**2008**	2007	**2008**	2007	**2008**	2007	**2008**	2007
Assets										
Investments at fair value										
Real estate holdings	**–**	–	**23,050.7**	22,687.2	**–**	–	**–**	–	**–**	–
Equities and convertible securities	**–**	–	**5,015.8**	4,817.3	**3,069.5**	2,366.8	**4,606.0**	5,200.7	**1,075.9**	2,169.7
Bonds	**–**	–	**–**	–	**891.3**	2,005.5	**264.6**	653.6	**4,097.4**	5,081.5
Mortgages	**10,814.0**	9,364.7	**1,143.2**	1,257.3	**–**	–	**–**	–	**–**	–
Mortgages securities	**1,322.8**	2,621.6	**99.7**	99.4	**–**	–	**–**	–	**–**	–
Short-term investments	**42.1**	15.5	**1,581.4**	306.6	**222.8**	501.1	**170.2**	183.0	**1,129.7**	603.1
Securities acquired under reverse repurchase agreements	**–**	–	**–**	–	**–**	–	**–**	523.1	**864.1**	2,471.0
Real estate held for resale	**58.5**	50.3	**–**	–	**–**	–	**–**	–	**–**	–
Third-party and bank-sponsored ABCP	**–**	–	**–**	–	**–**	–	**–**	–	**–**	–
Derivative financial instruments related to third-party and bank-sponsored ABCP	**–**	–	**–**	–	**–**	–	**–**	–	**–**	–
Demand deposits in the General Fund	**528.2**	2.3	**–**	–	**–**	–	**–**	130.6	**609.2**	–
	12,765.6	12,054.4	**30,890.8**	29,167.8	**4,183.6**	4,873.4	**5,040.8**	6,691.0	**7,776.3**	10,325.3
Other assets	**894.1**	117.4	**587.1**	830.6	**289.8**	195.6	**18.3**	66.3	**108.8**	303.5
	13,659.7	12,171.8	**31,477.9**	29,998.4	**4,473.4**	5,069.0	**5,059.1**	6,757.3	**7,885.1**	10,628.8
Liabilities										
Advances from the General Fund	**–**	–	**525.2**	930.4	**443.4**	298.8	**607.6**	–	**–**	447.9
Securities sold under repurchase agreements	**–**	–	**–**	–	**–**	–	**–**	567.9	**3,319.2**	2,827.7
Notes payable	**–**	–	**200.0**	199.9	**–**	–	**–**	–	**367.9**	1,279.3
Temporary funding attributable to foreign currency fluctuations	**–**	–	**–**	–	**–**	–	**–**	–	**–**	–
Loans payable	**583.5**	–	**8,790.9**	7,118.6	**–**	–	**–**	–	**–**	–
Mortgage loans payable	**–**	–	**3,770.7**	1,683.3	**–**	–	**–**	–	**–**	–
Commercial mortgage-backed securities	**311.2**	349.2	**–**	–	**–**	–	**–**	–	**–**	–
Participating debenture	**93.3**	–	**–**	–	**–**	–	**–**	–	**–**	–
Short selling of securities	**–**	–	**–**	122.0	**–**	–	**181.3**	650.9	**668.9**	2,963.0
Derivative financial instruments	**1,118.3**	217.4	**2,022.2**	205.6	**2,554.6**	2,105.2	**270.3**	39.2	**3,161.1**	2,351.6
Other liabilities	**603.8**	136.7	**1,182.6**	1,121.6	**127.1**	141.5	**12.0**	9.8	**275.5**	45.1
Non-controlling interests	**38.3**	–	**1,052.5**	1,154.7	**–**	–	**51.7**	308.0	**–**	–
	2,748.4	703.3	**17,544.1**	12,536.1	**3,125.1**	2,545.5	**1,122.9**	1,575.8	**7,792.6**	9,914.6
Net holdings of funds	**10,911.3**	11,468.5	**13,933.8**	17,462.3	**1,348.3**	2,523.5	**3,936.2**	5,181.5	**92.5**	714.2
Statement of consolidated income for the year ended December, 31										
Income										
Investment income										
Real estate holdings	**–**	–	**506.1**	473.1	**–**	–	**–**	–	**–**	–
Equities and convertible securities	**–**	–	**25.6**	74.6	**(0.1)**	0.4	**(2.0)**	(2.3)	**0.2**	0.3
Bonds	**–**	–	**–**	2.4	**–**	(4.8)	**(2.0)**	2.9	**35.4**	8.9
Mortgages	**1,724.8**	757.1	**83.9**	51.8	**–**	–	**–**	–	**–**	–
Mortgage securities	**–**	–	**7.4**	8.9	**–**	–	**–**	–	**–**	–
Short-term investments	**0.5**	0.2	**100.1**	54.3	**9.8**	21.9	**0.5**	2.8	**–**	–
Demand deposits in (advances from) the General Fund	**10.3**	9.4	**(8.2)**	(24.7)	**(6.2)**	22.9	**(0.3)**	16.0	**(19.0)**	(57.0)
	1,735.6	766.7	**714.9**	640.4	**3.5**	40.4	**(3.8)**	19.4	**16.6**	(47.8)
Other income	**13.2**	9.6	**–**	–	**–**	–	**–**	–	**–**	–
	1,748.8	776.3	**714.9**	640.4	**3.5**	40.4	**(3.8)**	19.4	**16.6**	(47.8)
Operating expenses	**7.5**	8.4	**11.2**	9.4	**4.8**	5.9	**19.8**	18.3	**16.2**	14.7
External management fees	**3.1**	6.0	**–**	–	**–**	–	**–**	–	**0.2**	4.6
Income before the following items	**1,738.2**	761.9	**703.7**	631.0	**(1.3)**	34.5	**(23.6)**	1.1	**0.2**	(67.1)
Interest on loans and notes payable	**–**	–	**–**	–	**–**	–	**–**	0.6	**39.1**	53.2
Non-controlling interests	**–**	–	**45.7**	47.4	**–**	–	**–**	–	**–**	–
Net investment income (loss)	**1,738.2**	761.9	**658.0**	583.6	**(1.3)**	34.5	**(23.6)**	0.5	**(38.9)**	(120.3)
Changes in consolidated net assets for the year ended December, 31										
Net investment results	**1,738.2**	761.9	**658.0**	583.6	**(1.3)**	34.5	**(23.6)**	0.5	**(38.9)**	(120.3)
Net investment income (loss)	**(476.2)**	(197.0)	**(1,352.2)**	1,159.7	**(968.3)**	(231.4)	**(1,176.2)**	911.0	**(1,187.4)**	158.2
Gains (losses) on sale of investments										
Unrealized increase (decrease) in value of investments and liabilities related to investments	**(2,199.2)**	(457.5)	**(3,278.4)**	1,158.4	**575.0**	153.6	**107.6**	(492.7)	**(506.6)**	(167.5)
Net investment results	**(937.2)**	107.4	**(3,972.6)**	2,901.7	**(394.6)**	(43.3)	**(1,092.2)**	418.8	**(1,732.9)**	(129.6)
Participation units issued (cancelled)	**2,118.2**	3,048.5	**1,102.1**	1,298.4	**(781.9)**	288.6	**(176.7)**	541.7	**1,072.3**	335.2
Net investment loss (net income) recovered from (allocated to) participation unit holders	**(1,738.2)**	(761.9)	**(658.0)**	(583.6)	**1.3**	(34.5)	**23.6**	(0.5)	**38.9**	120.3
Increase (decrease) in consolidated net assets	**(557.2)**	2,394.0	**(3,528.5)**	3,616.5	**(1,175.2)**	210.8	**(1,245.3)**	960.0	**(621.7)**	325.9
Consolidated net assets, beginning of year	**11,468.5**	9,074.5	**17,462.3**	13,845.8	**2,523.5**	2,312.7	**5,181.5**	4,221.5	**714.2**	388.3
Consolidated net assets, end of year	**10,911.3**	11,468.5	**13,933.8**	17,462.3	**1,348.3**	2,523.5	**3,936.2**	5,181.5	**92.5**	714.2
Investments and liabilities at cost as at December, 31										
Assets										
Investments										
Real estate holdings	**–**	–	**19,206.6**	17,498.6	**–**	–	**–**	–	**–**	–
Equities and convertible securities	**–**	–	**4,239.2**	3,437.1	**716.8**	725.3	**4,839.3**	5,426.5	**240.2**	703.5
Bonds	**–**	–	**–**	–	**891.3**	2,005.5	**26.2**	670.4	**2,987.7**	5,184.4
Mortgages	**11,116.7**	9,386.3	**1,193.1**	1,272.2	**–**	–	**–**	–	**–**	–
Mortgages securities	**2,592.1**	2,774.1	**122.3**	102.7	**–**	–	**–**	–	**–**	–
Short-term investments	**42.1**	15.5	**1,581.4**	306.6	**222.8**	501.2	**156.0**	172.6	**534.5**	574.5
Securities acquired under reverse repurchase agreements	**–**	–	**–**	–	**–**	–	**–**	545.3	**824.9**	2,538.1
Real estate held for resale	**69.7**	68.3	**–**	–	**–**	–	**–**	–	**–**	–
Third-party and bank-sponsored ABCP	**–**	–	**–**	–	**–**	–	**–**	–	**–**	–
Demand deposits in the General Fund	**528.2**	2.3	**–**	–	**–**	–	**–**	130.6	**609.2**	–
	14,348.8	12,246.5	**26,342.6**	22,617.2	**1,830.9**	3,232.0	**5,021.5**	6,945.4	**5,196.5**	9,000.5
Liabilities										
Securities sold under repurchase agreements	**–**	–	**–**	–	**–**	–	**–**	553.4	**3,299.7**	2,909.2
Notes payable	**–**	–	**200.0**	200.0	**–**	–	**–**	–	**284.9**	1,269.7
Temporary funding attributable to foreign currency fluctuations	**–**	–	**–**	–	**–**	–	**–**	–	**–**	–
Loans payable	**598.9**	–	**8,979.8**	7,145.7	**–**	–	**–**	–	**–**	–
Mortgage loans payable	**–**	–	**3,932.3**	1,694.8	**–**	–	**–**	–	**–**	–
Commercial mortgage-backed securities	**305.4**	339.0	**–**	–	**–**	–	**–**	–	**–**	–
Participating debenture	**100.0**	–	**–**	–	**–**	–	**–**	–	**–**	–
Short selling of securities	**–**	–	**–**	137.4	**–**	–	**194.5**	657.5	**445.1**	3,021.5
Derivative financial instruments	**92.4**	26.0	**47.9**	27.3	**860.6**	547.5	**0.6**	5.2	**243.0**	738.4
Non-controlling interests	**38.3**	–	**987.4**	866.1	**–**	–	**55.7**	263.5	**–**	–

CONTRIBUTION TO ECONOMIC DEVELOPMENT

CONTRIBUTION TO ECONOMIC DEVELOPMENT

The Caisse's main contributions to Québec's economic development are the long-term returns it earns for its depositors, its investments in the province, the economic benefits of its operations and its commitment to the community.

In making private equity investments in Québec, the Caisse often uses a partnership approach that complements the role played by the province's financial institutions. This strategy creates synergistic expertise for Québec's companies, which constitutes an advantage for the economy.

HIGHLIGHTS

/ The Caisse is one of the largest investors in Québec, with $33.4 billion of total assets as at December 31, 2008; the private sector accounts for $17.3 billion of that amount.

/ Total assets in Québec represent 30.7% of its Canadian assets, a proportion that significantly exceeds the province's economic weight in the country.

/ The Caisse directly and indirectly finances almost 500 Québec companies and has equity and debt interests in more than 600 Québec buildings.

/ In 2008, the Caisse made 137 new investments in Québec for a total of $777 million.

/ In a context in which credit is more costly and less accessible, the Caisse allocated $1.5 billion late in 2008 to meet the needs of Québec companies.

/ The Caisse works with many public and private actors in Québec and shares its financial expertise and resources to benefit Québec companies.

/ In 2008, the Caisse created Otera Capital, a commercial real estate financing subsidiary with its head office in Montréal. Creation of the subsidiary involved moving the senior management team from Toronto to Montréal.

/ In 2008, in partnership with Kevric Real Estate Corporation, the Caisse created a $300-million real estate fund to acquire and to develop property in three markets, including Montréal.

/ The AlterInvest Fund, a partnership between the Caisse and the Business Development Bank of Canada, marked its fifth anniversary in 2008. This agreement has provided more than $200 million of financing to 161 small businesses in Québec.

LONG-TERM RETURNS AND INVESTMENT IN QUÉBEC

One of the Caisse's main contributions to Québec's economic development is the long-term return that it earns for its 25 Québec depositors. The 8.3% average annual return that the Caisse has generated for its depositors since it was created in 1965 has enabled them to keep their plans in good financial health.

The Caisse is one of the largest investors in Québec, with assets totalling $33.4 billion as at December 31, 2008, namely $3.8 billion invested by the Private Equity group, $1.6 billion by the Equity Markets group, $21.7 billion by the Fixed Income and Currencies group and $6.3 billion by the Real Estate group (table 90).

TABLE 90

CAISSE'S TOTAL ASSETS IN QUÉBEC

(as at December 31 – in billions of dollars)

	2008	2007
Private Equity	3.8	6.0
Equity Markets	1.6	2.4
Fixed Income and Currencies	21.7	23.6[1]
Real Estate	6.3	6.9
Total	**33.4**	**39.0**[1]
Private sector	17.3	23.3[1, 2]
Public sector	16.1	15.7[2]

1 The amounts have been restated, mainly with the addition of $1.0 billion to securities of private companies to take into account amounts receivable on short-term assets with a counterparty in Québec.

2 The amounts have been restated, mainly to take into account reallocation of $1.3 billion from the private sector to the public sector.

METHODOLOGY

To determine whether an asset is classified as a Québec investment, the Caisse uses the location of the head office of the company or of the issuer of the security or, in the case of real estate, the geographic location of the property.

This classification, generally used in the fund management industry, involves certain biases. Some companies are included, even though most of their operations are outside Québec. Similarly, companies with extensive operations in Québec are excluded if their head office is outside the province.

The Caisse therefore has a strong presence in Québec. Its assets in the province represent 30.7% of its Canadian assets, a proportion that significantly exceeds Québec's economic weight in the country (table 91). As for the Caisse's investments in Canada, they represent 58.1% of its total assets.

The Caisse's total assets in Québec's private sector amounted to $17.3 billion as at December 31, 2008. It had direct and indirect holdings in almost 500 companies as well as debt and equity investments in more than 600 properties.

Table 92 shows the Caisse's presence in the sectors of Québec's economy. The Caisse is active in all sectors, but is partial to real estate, financials, consumer staples and discretionary, industrials and utilities.

In 2008, the Caisse made 137 new investments in Québec totalling $777 million, with 39.6% in real estate, 32.3% in equities and 28.1% in private equity (table 93).

TABLE 91

CAISSE'S TOTAL ASSETS

(as at December 31 – in billions of dollars)

	2008	2007
In Québec	**33.4**	39.0
In Canada	**108.7**	131.4
Total[1]	**186.9**	227.1
(as a proportion)		
Québec/Canada	**30.7%**	29.7%
Canada/total	**58.1%**	57.8%

1 Caisse's total assets in Canada and other countries.

TABLE 92

SECTOR BREAKDOWN OF PRIVATE-SECTOR ASSETS IN QUÉBEC

(as at December 31, 2008)

Sector	Number of businesses	Number of buildings	Fair value $M	%
Energy	11		65	0.4
Materials	104		297	1.7
Industrials	67		1,009	5.8
Consumer staples and discretionary	114		2,624	15.2
Health care	64		83	0.5
Financials	30		5,454	31.5
Real estate	2	620	6,307	36.4
Information technology	74		333	1.9
Telecommunication services	10		408	2.4
Utilities	10		733	4.2
Other	6		6	0.0
Total	**492**	**620**	**17,320**	**100.0**

TABLE 93

NEW INVESTMENTS IN QUÉBEC IN 2008

(in millions of dollars)

Asset class	Number of investments	$M	%
Private Equity	80	218	28.1
Equity Markets	14	251	32.3
Real Estate	43	308	39.6
Total	**137**	**777**	**100.0**

CONTRIBUTION TO ECONOMIC DEVELOPMENT

PRIVATE EQUITY

For more than 25 years, the Private Equity group has been supporting Québec companies in all phases of the business cycle. It meets the needs Québec companies, regardless of their development stage, with a wide range of customized solutions and partnerships.

In Québec, the Caisse has the advantage of proximity. Throughout its history, the institution has used its knowledge of the local market to complement the financing provided by other institutions, especially in difficult periods.

More than ever, the Caisse is therefore working in partnership with the province's other suppliers of funds. When the economy is growing, capital is more readily available, and financing from the Caisse is naturally less in demand. At the bottom of the cycle or during tight credit conditions, the Caisse is called on to play a role that complements the usual sources of financing.

The total assets of the Private Equity group invested in Québec directly or in partnership totalled $3.8 billion as at December 31, 2008, with $157 million in venture capital, $80 million in small businesses, $224 million in medium-sized businesses and $3.336 billion in large businesses (table 94). In addition, the group had undisbursed commitments totalling $1.0 billion, to be paid out on conditions negotiated with its partners. Assets and commitments totalled almost $4.8 billion. Most of the variation in relation to 2007 is due to the lower fair value of companies as a result of the financial crisis. This one-time valuation in no way affects the group's philosophy, which is to invest for the long term.

As shown by table 95, the Private Equity portfolio in Québec comprises 423 companies in 10 sectors of activity. The consumer sectors, utilities and industrials account for most of the investments.

During the year, the group made 80 direct and indirect investments totalling $218 million, with new investments accounting for more than one-half.

The Private Equity group will maintain a prudent and thorough approach to investment selection, and will continue to monitor companies closely and to sustain them in co-operation with Québec's other leading public-sector and financial actors.

Late in 2008, the Caisse allocated $1.5 billion to finance Québec companies with a promising outlook. Whether they want to make an acquisition, to modernize their facilities or to meet a temporary liquidity need, the Caisse has the funds to assist them in a timely fashion.

TABLE 95

SECTOR BREAKDOWN OF THE PRIVATE EQUITY GROUP'S ASSETS IN QUÉBEC

(as at December 31, 2008)

Sector	Number of businesses	Fair value $M
Energy	9	10
Materials	98	283
Industrials	57	491
Consumer staples and discretionary	98	1,988
Health care	60	76
Financials	11	85
Information technology	68	84
Telecommunication services	6	41
Utilities	10	733
Other	6	6
Total	**423**	**3,797**

TABLE 94

PRIVATE EQUITY GROUP'S ASSETS AND COMMITMENTS IN QUÉBEC

(as at December 31 – in millions of dollars)

			2008			2007
	Assets	**Undisbursed commitments**	**Assets and commitments**	Assets	Undisbursed commitments	Assets and commitments
Venture capital	**157**	**491**	**648**	200	538	738
Small business	**80**	**89**	**169**	65	68	133
Medium-sized business	**224**	**197**	**421**	247	108	355
Large business	**3,336**	**246**	**3,582**	5,522	551	6,073
Total	**3,797**	**1,023**	**4,820**	6,034	1,265	7,299

Venture capital

The venture capital investment strategy continues to be based on partnership and has four components:

/ Invest in private funds that are well positioned in venture capital in Québec;

/ Coinvest with local funds to finance growth projects;

/ Attract foreign venture capital; and

/ Facilitate harmonization of business practices in the province.

The purpose of this approach is to create more diverse sources of capital, to generate a leverage effect, to increase the amounts available to Québec companies and to take advantage of the expertise of dynamic fund managers.

At year-end, the Caisse was a partner in 10 Québec funds and three funds from outside the province with an office in Québec (table 96). The funds had a total of $1.2 billion, and the Caisse's commitments totalled $231 million. By partnering with external capital, the Caisse makes a contribution that has more impact for Québec companies than a direct investment would.

The Caisse's total assets in this segment, held directly or through funds, amounted to $157 million in 105 companies at year-end.

Small business

In the small business segment, namely companies with financing needs of less than $2 million, the Caisse adopted a partnership investment strategy in 2003 with the Business Development Bank of Canada (BDC). Together, they set up the AlterInvest Fund for small businesses.

The fund's main focus is subordinated loans. In five years, the AlterInvest Fund has invested $453 million across Canada, including more than $200 million in 161 of Québec's small businesses. It has enabled many businesses to make their growth projects a reality.

The Caisse's indirect investments in small businesses totalled $80 million in 137 companies as at December 31, 2008. Its undisbursed commitments amounted to $89 million.

The fund fosters consolidation and expansion in most sectors of activity. With an average investment of $1.2 million, each company receives financial support based on the specific needs of its projects, regardless of development stage.

The Caisse has optimized its small business financing through BDC's extensive network of almost 800 employees at 23 offices in Québec.

TABLE 96

MAIN NICHES OF PARTNER FUNDS BY COMPANY DEVELOPMENT STAGE

<table>
<tr><th>Partner funds manager</th><th>Startup</th><th>Growth</th><th>Sustainability and ownership transfer</th></tr>
<tr><td>iNovia Capital</td><td>Generalist</td><td></td><td></td></tr>
<tr><td>GoCapital</td><td>Generalist</td><td></td><td></td></tr>
<tr><td>Cycle Capital</td><td>Renewable technology</td><td></td><td></td></tr>
<tr><td>ID Capital</td><td>Generalist</td><td></td><td></td></tr>
<tr><td>Capital St-Laurent</td><td>Generalist</td><td></td><td></td></tr>
<tr><td>Brightspark Ventures</td><td>Information technology</td><td></td><td></td></tr>
<tr><td>CTI Sciences de la vie</td><td colspan="2">Life sciences</td><td></td></tr>
<tr><td>AgeChem</td><td colspan="2">Life sciences</td><td></td></tr>
<tr><td>Rho Canada Ventures</td><td colspan="2">Information technology</td><td></td></tr>
<tr><td>Emerald Technology Ventures</td><td colspan="2">Renewable technology</td><td></td></tr>
<tr><td>Placements Propulsion</td><td colspan="2">Information technology</td><td></td></tr>
<tr><td>JLA Ventures</td><td colspan="3">Information technology</td></tr>
<tr><td>Novacap</td><td></td><td colspan="2">Information technology</td></tr>
</table>

CONTRIBUTION TO ECONOMIC DEVELOPMENT

Medium-sized business
Québec's medium-sized businesses operate in a very demanding environment. To ensure their sustainability, they must adapt their business models, invest in research and development, penetrate new markets and often insert themselves into global supply chains.

In this context, the Caisse has set up a team that specializes in medium-sized Québec companies with financing needs ranging from $2 million to $25 million. Its personalized solutions include equity investments, term financing, subordinated loans, mezzanine loans and debentures.

The Caisse strives to partner with solid management teams focused on the sustainability and growth of their companies with niche products and realistic business plans. It also enables Québec's medium-sized businesses to take advantage of a network of corporate directors and partners, as well as expertise and synergy developed over the years.

The Caisse also invests through funds, including the Québec Manufacturing Fund (Industrial Capital) and Novacap. The first fund aims to improve the productivity of Québec manufacturers. As for Novacap, it is a growth and leveraged-buyout fund that invests in companies that are leaders in traditional and technology sectors. Novacap helps them accelerate their operations significantly by focusing on internal growth, acquisitions and strategic alliances.

The Caisse's total assets in the medium-sized business segment amounted to $224 million in 55 companies as at December 31, 2008. It holds investments in many Québec companies, including Ezeflow, Laboratoire Médical Biron, Omega Laboratories and Solotech. The Caisse's undisbursed commitments totalled $197 million.

Large business
Since early in the 1980s, Québec's large businesses have been able to count on a team of private equity professionals for assistance with their projects. Many of its senior members, with an average of more than 20 years in the group, have gone through all the phases of an economic cycle, gaining experience that contributes to their understanding of the current context.

For financing needs of more than $25 million, the Caisse intends to take the initiative by working with various public and private actors in Québec to provide additional sources of optimized financing and to increase its economic benefits.

The financing solutions fall into two main categories:

/ Equity stakes of up to 30%, in the form of common or preferred shares; and

/ Loans, in the form of term financing, subordinated loans, mezzanine loans and debentures.

The Caisse continues to play a leading role in financing large Québec businesses. Its extensive knowledge of this market, as well as its size, enables it to assist them with their growth strategies for domestic and foreign markets alike.

The Caisse has a network of high-calibre partners that it intends to continue to support. The expertise it has acquired over the years in this way benefits all the companies it does business with.

The Caisse's total assets in the large business segment amounted to $3.3 billion in 126 companies as at December 31, 2008. It holds considerable stakes in such companies as ACH Limited Partnership, Bombardier Recreational Products (J.A. Bombardier (J.A.B) Inc.), Camoplast, Cascades, Cirque du Soleil, Dépan-Escompte Couche-Tard, Garda World Security Corporation, Gesca Ltd., Héroux-Devtek, Hewitt Equipment Ltd., Noverco (Gaz Métro), Quebecor Media, TransForce Inc. and Yellow Pages Income Fund. The Caisse's undisbursed commitments totalled $246 million.

EQUITY MARKETS

When selecting investments, the managers in the Equity Markets group usually focus on the intrinsic value of businesses and their development outlook over the medium and long terms. It is in the interests of the Caisse and its depositors that priority be placed on those companies that have the best development outlook and the best performance, in terms of the calibre of their senior management and board of directors, as well as their operations.

In this way, the Caisse strives to align its interests with those of its portfolio companies over the long term. By investing in this way, it gains a better understanding of Québec's businesses and builds trust-based relationships with them.

The Caisse has one of the largest portfolios of publicly traded Québec equities. In addition to the stakes in companies held by the Private Equity group ($352 million as at December 31, 2008), the Equity Market group held $1.6 billion of investments in 41 Québec companies at year-end.

During the year, the Caisse increased its holdings in 14 companies, for a total of $251 million, including BCE, Cogeco Cable, Yellow Pages Income Fund, Gildan Activewear, RONA and Transat AT. It also has large stakes in Canadian National Railway, SNC-Lavalin Group, CGI Group, Quebecor and Saputo.

The equity market decline contributed significantly to the drop in the value of the Québec stock portfolio in 2008.

FIXED INCOME AND CURRENCIES

The financing needs of the public sector have been decreasing in recent years, causing the relative importance of government securities in the Caisse's portfolio to decline. Even so, the Caisse continues to be one of the main purchasers of Québec public-sector bonds, and its holdings of government securities even increased slightly in 2008.

The Fixed Income and Currencies group holds mainly securities issued by the Québec government, Hydro-Québec, Financement Québec, Corporation d'hébergement du Québec, municipalities, and educational and health care institutions.

As shown by table 97, the group had $21.7 billion of assets in Québec as at December 31, 2008, including $16.1 billion in public-sector securities and $5.6 billion in corporate securities.

TABLE 97

FIXED INCOME AND CURRENCIES GROUP'S QUÉBEC ASSETS

(as at December 31 – in billions of dollars)

	2008	2007
Québec public sector:		
Québec government	**9.3**	8.6
Hydro-Québec	**3.9**	4.3
Other state-owned entreprises	**1.5**	1.3[1]
Municipalities and paragovernmental corporations	**1.4**	1.5
Subtotal	**16.1**	15.7[1]
Corporate securities	**5.6**	7.9[1, 2]
Total	**21.7**	23.6[2]

1 The amounts have been restated, mainly to take into account reallocation of $1.3 billion from the private sector to the public sector.

2 The amounts have been restated, mainly with the addition of $1.0 billion to securities of private companies to take into account amounts receivable on short-term assets with a counterparty in Québec.

The group held securities of 28 Québec companies, including Laurentian Bank of Canada, National Bank of Canada, BCE, BMO Capital Trust, Caisse centrale Desjardins, Cogeco Cable, SNC-Lavalin Group, Télébec and YPG Holdings.

REAL ESTATE

The Caisse Real Estate group has one of the largest portfolios of properties in Québec. It operates through its Cadim division and its subsidiaries, Ivanhoe Cambridge, Otera Capital and SITQ. The group specializes in property investment, development and management. It invests in equity and debt, with emphasis on office buildings and business parks, shopping centres, hotels and multiresidential buildings.

The search for high-quality buildings that are well positioned in their markets is the hallmark of the Caisse Real Estate group's operations. It seeks strategically located, highly stable assets that can adapt to fluctuations in the economic cycle.

Moreover, to maintain the quality and value of its Québec holdings, the group invested almost $70 million in 2008, including $63 million in projects to renovate, enlarge and update its portfolio of properties. During the year, the Caisse and its real estate entities benefited from an occupancy rate that peaked at 95%. This achievement is due to sound management by teams determined to preserve the value of their properties and the confidence of their tenants.

In 2008, the group announced that it would combine its real estate debt financing operations into a new subsidiary, Otera Capital, to consolidate its position as a world-class lender. Otera Capital is based in Montréal and specializes in commercial real estate financing, including underwriting, servicing, active management and syndication, with several products, including conventional mortgage loans. It has a loan-origination and underwriting team that focuses exclusively on Québec. When this subsidiary was created, the senior management team moved from Toronto to Montréal.

The Real Estate group's total assets in Québec amounted to $6.3 billion as at December 31, 2008, as shown by table 98. The group held debt and equity investments in more than 600 buildings in the province.

The Real Estate group's total acquisitions in 2008 amounted to $308 million and took the form of five direct investments ($16.5 million) and loans for 38 buildings ($291 million).

TABLE 98

REAL ESTATE GROUP'S ASSETS AND COMMITMENTS IN QUÉBEC

(as at December 31 – in millions of dollars)

			2008			2007
	Assets	Undisbursed commitments	Assets and commitments	Assets	Undisbursed commitments	Assets and commitments
Office buildings	**2,340**	**72**	**2,412**	2,736	147	2,883
Shopping centres	**2,876**	**42**	**2,918**	2,911	118	3,029
Hotels	**349**	**85**	**434**	460	77	537
Other	**741**	**201**	**942**	801	171	972
Total	**6,305**	**400**	**6,705**	6,908	513	7,421

CONTRIBUTION TO ECONOMIC DEVELOPMENT

The group will continue investing massively in Québec's real estate sector. For example, in partnership with Kevric Real Estate Corporation, the Caisse was involved in the creation of a $300-million real estate fund in 2008. The fund will acquire and develop properties in three markets, including Montréal.

Moreover, undisbursed commitments totalled $400 million as at December 31, 2008, including $208 million in the form of loans and $191 million of investments made directly or through funds.

Office buildings
The Caisse's equity and debt holdings in 100 office buildings in Québec totalled $2.3 billion as at December 31, 2008. The total leasable area of the buildings owned or managed by the Real Estate group was almost 600,000 square metres. During the year, the group provided almost $20 million of loans for four buildings.

The most important buildings owned by the group are in downtown Montréal: 1000 De La Gauchetière, 1500 University, the Caisse's business office, the Montréal World Trade Centre, the Sun Life Building and Place Ville Marie. In Québec City, the Real Estate group owns the Édifice Mérici, the Édifice Price and the Édifice de la Haute-Ville.

SITQ, the Real Estate group subsidiary that specializes in the office sector, invested tens of millions of dollars to renovate its buildings. Examples include:

/ Various renovations at Place Ville Marie, in Montréal, at a cost of almost $50 million;

/ A $2.9-million investment for renovations at 1000 De La Gauchetière, in Montréal. The project began in 2008 and will be completed in 2009; and

/ Major work at 1500 University and Complexe Les Ailes.

Shopping centres
The Caisse's equity and debt holdings in almost 200 Québec shopping centres totalled $2.9 billion as at December 31, 2008. The leasable area of the buildings owned or managed by the Real Estate group was 2.2 million square metres. Loans totalling $153 million were provided for 15 buildings during the year.

The group's most important retail properties are in Montréal: the Eaton Centre, Fairview Pointe-Claire, Rockland, Les Galeries d'Anjou and Place Montréal-Trust. Other assets include Centropolis in Laval, the Mail Champlain on Montréal's South Shore, Les Rivières shopping centre in Trois-Rivières, Place du Royaume in Saguenay and Laurier Québec and Place Ste-Foy in Québec City.

Ivanhoe Cambridge, the real estate subsidiary that specializes in shopping centres, invested tens of millions of dollars to reposition and to renovate various properties. During the year, it carried out the following projects:

/ Renovations at Place Ste-Foy, which will continue in 2009 and represent a $39-million investment. The project involves enlargement of the outlet operated by Simons (4,088 square metres), a well-known Québec retailer that has decided to make it the chain's flagship store, as well as construction of an underground parking garage and an increase in leasable area;

/ Completion of the $39-million project to redevelop Place Vertu shopping centre, in Montréal, begun in 2007. This project will reposition the mall with the addition of new retailers, some of them Québec companies, and the construction of a new food court; and

/ Development of Centropolis in Laval and redevelopment of Rockland in Montréal at a cost of almost $9 million during the year.

Hotels
The Caisse's debt and equity holdings in the hotel sector totalled $349 million in seven buildings as at December 31, 2008. During the year, $61 million of loans was provided to three companies in this sector.

Through its Cadim division, the Caisse owns superior-quality hotels, including two gems associated with the history of the province: the Fairmont Queen Elizabeth, in Montréal, and the Fairmont Le Château Frontenac, in Québec City.

Other assets
The Real Estate group's assets in the industrial and multiresidential sectors, as well as its other assets, totalled $741 million in 323 buildings, including 236 in the industrial sector and 73 in the residential sector, as at December 31, 2008. The Real Estate group made 21 new investments totalling $74 million in these sectors, including five direct investments amounting to $17 million. It also provided $57 million of loans for 16 buildings.

At year-end 2008 in the multiresidential sector, Cadim had a $170-million equity stake in the Maestro I, II, III, IV and V Residence Funds, of which more than $80 million has already been invested and almost $90 million is committed for future investments. Maestro, 55% owned by Cadim, specializes in acquisition and development of seniors residences in Canada. Maestro's 22 residences in Québec totalled $588 million as at December 31, 2008. At year-end, Maestro had more than $300 million of equity available for investment opportunities across the country through its Maestro IV and V Residence Funds.

ECONOMIC BENEFITS AND COMMUNITY SUPPORT

The operations of the Caisse and its real estate entities generate substantial economic and other benefits for Québec. They are among the main employers in the province's financial sector. The Caisse and its real estate entities, as well as their employees, pay substantial taxes and contributions to the various levels of government. A total of $154 million was paid out in 2008. Of that amount, the employer contribution was $80 million, while the employee portion was $74 million.

Moreover, they foster an exchange of knowledge and the development of skills while maintaining business relationships with a large number of suppliers of goods and services. The Caisse and its entities also place a great deal of importance on their corporate responsibility, particularly issues involving governance and the social and environmental aspects of investment. Lastly, they take part in many other activities that contribute to Québec's economic development.

The Caisse and its real estate entities have partened with many foreign companies, enabling Québec to showcase its know-how and expertise. To ensure sound management of its foreign investments, the Caisse has teams in various countries, with an emphasis on Europe and Asia. These teams maintain business relations with local partners and promote Québec's expertise. The knowledge and experience of the Caisse's high-calibre managers are also very much in evidence at major international conferences. Moreover, the Caisse's operations have enabled many of the province's businesses, such as legal, accounting and other specialized firms, to extend their reach beyond Québec.

DYNAMIC QUÉBEC EMPLOYERS

The Caisse and its real estate entities rely on employees with high-level skills and expertise. As shown by table 99, the Caisse employs 805 people in Québec, while the real estate entities account for 993, for a total of 1,798 employees.

The Caisse's operations require various types of specialized expertise. It therefore hires people with a high level of skill that often includes advanced education. At year-end, 83% of the Caisse's Québec employees had a university degree and 41% a master's degree or a doctorate. Moreover, 113 employees hold the designation of Chartered Financial Analyst (CFA), 58 others are in the process of obtaining it and 88 employees have a professional accounting designation (CA, CGA or CMA). In addition, 17 employees hold the Financial Risk Manager (FRM) designation.

The high-quality working environment offered to employees has been designed as a function of their needs. Employees have leading-edge technology and access to a wide range of specialized information. The Caisse also offers various services, including a daycare centre, a fitness centre and activities to enhance well-being. Moreover, it offers competitive compensation in line with reference markets.

For the fifth year in a row, Ivanhoe Cambridge was named one of Canada's 50 best employers. In an annual survey conducted by Hewitt Associates in conjunction with *Report on Business* magazine published by the *Globe and Mail*, it ranked 16th in 2009. It also ranked second among Québec companies.

The Caisse and its real estate entities are creating a new talent pool by hiring fresh graduates each year and offering university students internships and fellowships. In 2008, the Caisse and its Cadim division hired 35 students and trainees.

TABLE 99

NUMBER OF EMPLOYEES OF THE CAISSE AND THE REAL ESTATE ENTITIES IN QUÉBEC

(as at December 31)

	2008	2007
Caisse employees	**805**	763
Real estate unit employees[1]	**993**	887
Total	**1,798**	**1,650**

1 The real estate entities are Cadim, Ivanhoe Cambridge, Otera Capital and SITQ.

CONTRIBUTION TO ECONOMIC DEVELOPMENT

The Caisse encourages its employees to take specialized training and co-ordinates many conferences given by experts. During the year, in addition to external training, the Caisse provided internal training to 1,348 participants, for a total of 8,467 hours. Since it was founded, the Caisse has been involved in the development of a critical mass of finance professionals in Québec.

Research and innovation are also extremely important to the Caisse and its real estate entities. In a rapidly changing market, it is essential to develop new methods and to acquire new expertise by means that include:

- Co-operation with Québec universities on the publication of articles in specialized international journals, to extend the Caisse's sphere of influence while emphasizing local expertise; and
- Research contracts awarded to Québec universities and finance professionals.

Relations with Québec suppliers
The Caisse and its real estate entities maintain business relations with many Québec suppliers of goods and services. In 2008, their operating expenses in Québec totalled almost $615 million, including almost $380 million for real estate operating expenses.

These operating expenses also create several hundred jobs in the province, in security, technical services, physical-asset management, maintenance and other services related to real estate. For example, the subsidiary SITQ employs 425 such people in Québec.

The Caisse uses professional services in many areas and retains firms of auditors, consultants, lawyers and various other specialists and external resources.

Expenditure on information technology and professional services amounted to $22 million and $27 million, respectively, while rents totalled $37 million. Custodial fees for securities came to $13 million, external management fees to $10 million and brokerage commissions to $5 million.

In addition to taking advantage of the skills of many Québec suppliers, the Caisse makes a point of referring them to its business partners. In this way, it helps its business partners maintain and develop their expertise and contributes to their expansion in Québec and the international arena.

SHARING NETWORKS AND ENHANCING KNOWLEDGE

The Caisse has a large network of national and international partners that benefits the Québec companies it does business with. As a result of various initiatives, it enables Québec companies to expand outside the province and sometimes even to establish foreign operations. In the real estate sector, it provided $65 million of loans to six Québec companies in 2008 for real estate projects in Calgary, Kingston, Toronto and Victoria, most of them in the seniors-residence niche.

Moreover, the Caisse is proud of its seasoned teams and ensures that their knowledge receives due recognition.

- It fosters the publication of research papers, and organizes and contributes financially to various seminars and conferences.
- It assists university students by supporting many fellowship programs, several university chairs and various educational activities at Québec universities.
- In the fall of 2008, the Caisse and the Montréal Exchange helped create a trading room at the UQAM School of Management. By contributing $390,000, the Caisse aims to facilitate finance training in Québec by ensuring students can acquire hands-on experience.
- In co-operation with the Société de Relations d'Affaires at HEC Montréal, for the four years it has organized a stock market simulation for university students at its Montréal office.
- It encourages excellence in business reporting with fellowships, as well as the Caisse de dépôt et placement du Québec/Merrill Lynch Economic and Financial Journalism Awards.
- It has supported the activities of the Quartier international de Montréal since its creation in 1999. This non-profit organization is dedicated to creating a prestigious world-class district in Montréal. The organization and the project have already received many honours and awards, particularly for redevelopment of McGill Street.

The Caisse made a significant contribution to the celebration of Québec City's 400th anniversary in 2008.

- It helped finance construction of the Quai des Cageux on the Promenade Samuel-De Champlain, a large outdoor recreational area with various services, including rental space and restaurants.
- The Caisse also sponsored various activities held by the Faculty of Business Administration at Université Laval: an exhibit on the history of the Caisse, an address by the institution's President and Chief Executive Officer, a Génies en herbes (reach-for-the-top) competition and a stock market simulation.
- It organized a symposium on aging and health as part of the Entretiens Jacques-Cartier conference.
- The Caisse published *Anchored and Soaring*, a book on its head office in Québec City and business office in Montréal. The purpose of the book is to familiarize the Caisse's distinguished visitors with the institution.

The Caisse and its real estate subsidiary SITQ organized a series of events, including seven free noon-hour concerts in the Jardins de l'Hôtel-de-Ville.

SITQ also commemorated the 400th anniversary of the founding of Québec City with a unique energy-efficient lighting system that showcases the Édifice Price.

A RESPONSIBLE BUSINESS

The Caisse endorses the principal of reporting on its corporate responsibilities to all stakeholders. It believes that a fund manager and investor of its size must pay the utmost attention to such vital matters as corporate governance and the social and environmental aspects of investment.

Socially Responsible Investment
The Caisse abides by the principles of socially responsible investment (SRI). For instance:

/ It systematically exercises its voting rights in the publicly traded Québec companies in its portfolio;

/ As a participant in the Carbon Disclosure Project, it encouraged Québec companies to disclose information about their greenhouse gas emissions;

/ It presented its SRI approach to other investors and Québec pension plans as well as to its depositors;

/ It opened a dialogue and began working with Québec investors on various aspects of SRI;

/ It did a review of the companies in the Québec 30 Index from the standpoint of socially responsible investment; and

/ It took part in international SRI organizations. In this way, the Caisse has presented itself as a responsible business aware of the impact of its operations, and has also enhanced Québec's stature in the world.

For more information on SRI, consult the section "Management framework."

The Caisse is developing a procedure for systematic inclusion of environmental, social and governance factors for the private equity sector. This initiative will affect its analysis of investments in Québec companies.

In corporate governance, the Caisse is an active partner in the Collège des administrateurs de sociétés, of which it became a founding member in 2005. The college's mission is to develop governance rules and to improve knowledge and application of them at Québec companies by offering high-quality training to the members of their boards of directors. The college had 81 graduates in 2008, for a total of 173 since its creation.

Sustainable development
The Caisse and its real estate entities put in place the resources and mechanisms needed to manage their buildings and to carry out their projects with a view to sustainable development. They ensure their employees, suppliers, customers and partners are aware of these principles.

The work of the managerial teams at Ivanhoe Cambridge and SITQ has been recognized with numerous awards, including the Office Building of the Year award and environmental certifications from the Building Owners and Managers Association (BOMA) of Canada.

In 2008, BOMA awarded its BOMA BESt (Building Environmental Standards) certification to various office buildings and shopping centres in Québec, including the Caisse's business office in Montréal, Place Ville Marie, the World Trade Centre Montréal, 1000 De La Gauchetière, the Édifice Price, the Édifice Mérici, the Édifice de la Haute-Ville, Centre Rivière-du-Loup, Les Galeries de Hull, Galeries Rive Nord, the Mail Champlain, Place Ste-Foy and Place Montréal Trust.

A new green procurement policy took effect in 2008 at the Caisse's business office in Montréal. SITQ adopted the policy, which covers office supplies, maintenance products and construction materials, as well as their recycling or reuse. All these products must now contain recycled material and have little or no content that is harmful to health or the environment. SITQ's green committee also recommended that the policy be extended to all its other office buildings in Québec.

CONTRIBUTION TO ECONOMIC DEVELOPMENT

Other contributions to society

The Caisse is noted for its active commitment to the community. It supports many initiatives in education, health care, culture and the arts. In 2008, the Caisse provided financial support totalling almost $1.9 million to many of Québec's philanthropic initiatives and organizations. The Caisse provided support for many events held by about 50 local organizations. Its employees took part in more than 80 events, and encouraged various causes and organizations.

The Caisse has held an annual golf tournament since 2001 and donates all proceeds to the province's charitable organizations. In 2008, the Caisse raised a record $205,000, which was divided among five Québec organizations: Tel-jeunes, the Fondation Père Sablon, On the Tip of the Toes Foundation, Entraide Grands Brûlés and Logis Rose-Virginie.

In 2008, as in the previous year, the donations made by the employees of the Caisse and its real estate entities to Centraide/United Way's Québec campaign, combined with the institutional donations, exceeded $1 million. According to Centraide/United Way's most recent statistics, the Caisse's fund-raising effort is one of the 10 most generous in Québec.

In addition to providing financial support for cultural and artistic organizations and events, the Caisse supports Québec's culture through its art collection. Over the years, it has acquired works by Québec artists known for their talent and influence in the artistic world. Its collection consists of more than 100 museum-quality pieces created from 1965, the year the Caisse was founded, to the present day.

MANAGEMENT FRAMEWORK

MANAGEMENT FRAMEWORK

The Caisse's management framework consists of all policies, directives and procedures used for planning, organization, execution, control, evaluation, reporting and disclosure. The management framework also confirms the importance of optimizing operations, whether to fulfill the Caisse's mission or to ensure optimal use of the resources placed at its disposal by depositors.

The management framework covers all the Caisse's operations and applies to both the investment groups and the general services units. Implementing it is a collective endeavour that requires the involvement of all officers and employees, according to their roles and responsibilities. It ensures that the various teams maintain effective communication to ensure integrated management of the Caisse's various components.

HIGHLIGHTS

The Caisse continued to strengthen its management and control procedures in 2008.

/ The Caisse continued its efforts in risk management oversight and further improvement of its practices. As a result of the ABCP episode in 2007, it took an initial series of initiatives regarding the requirement of two credit rating sources for a financial instrument to be considered rated, a moratorium on any new financial instruments and implementation of centralized monitoring. It then began a review leading to the adoption of a three-year plan to raise risk management oversight, measurement and analysis to the level of the industry's best practices. Implementation of the plan accelerated in the fall of 2008.

/ The Caisse tightened the criteria for acceptance of new counterparties for transaction purposes. As a result of this tightening, certain legal agreements were amended and others were not concluded because they did not meet the new criteria.

/ The Caisse improved the speed of the controls it uses to monitor financial positions with its counterparties and thus ensured tighter management of collateral.

/ A new salary-structure model was established according to employee career paths, to become more competitive and to be better equipped to recruit the best candidates and to retain personnel. Moreover, a hiring freeze was imposed in response to the new economic context.

/ Projects to replace aging technology platforms and to improve information-security controls progressed satisfactorily.

/ The Caisse established detailed profiles to oversee, prevent and detect fraud. The profiles are use to evaluate inherent and residual fraud risk and to equip management and employees to manage this risk more effectively.

/ Progress on the financial certification process continued, in particular with respect to evaluation of internal control over financial reporting.

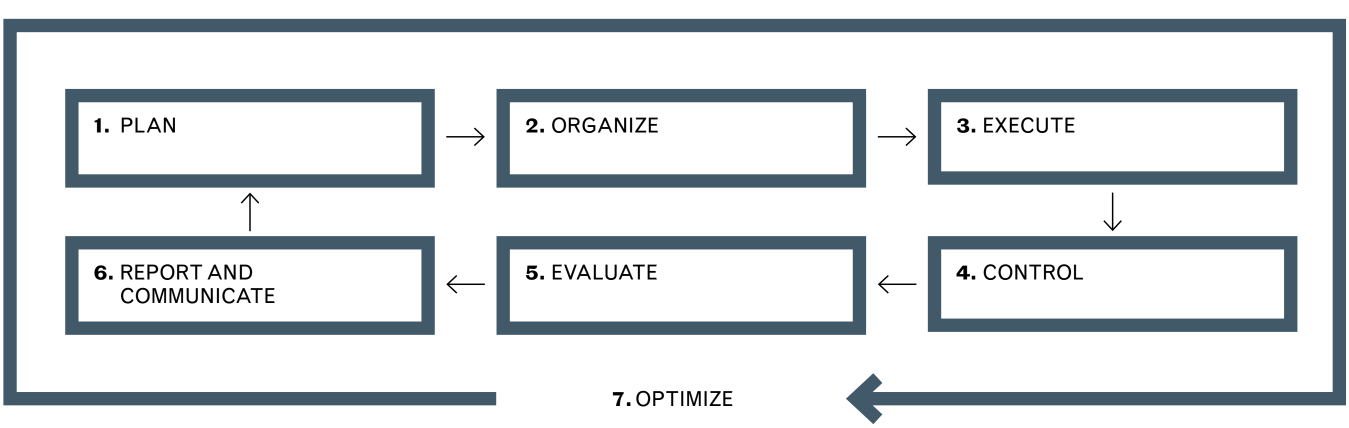
/ The Caisse has put in place sector compliance manuals and a compliance program for the Fixed Income and Currencies group. It also introduced a procedure to monitor trading operations.

/ The Caisse implemented a compliance program for the management mandates and co-ordinated a program to ensure compliance with the new regulation on short selling adopted by the regulatory authorities. It also introduced an automated process to monitor compliance with the regulation and the investment policies.

The current market context as well as changes to senior management led to deferral of work on the strategic three-year plan. The work will resume later in 2009. The Board of Directors approved this approach.

Figure 100 shows the main components of the management framework.

FIGURE 100
THE CAISSE'S MANAGEMENT FRAMEWORK



1. PLAN

Every three years, the Caisse prepares a strategic plan that establishes its main orientations, sets its objectives and defines the actions to be taken to achieve them. In agreement with the Board of Directors, the Caisse deferred development of the next strategic plan to 2009.

On the basis of this three-year strategic plan, each year the Caisse's senior managers prepare business plans, establish a book of business and information technology projects, and prepare the corresponding personnel, operating and capital budgets. Each business unit is responsible for the relevant portion of the annual business plan, and the employees are responsible for achieving the objectives set out in the plan. Individual objectives are established jointly by employees and team leaders, and then approved by the next two hierarchical levels.

The Board of Directors approves the three-year strategic plan, the annual business plans, the project book and the budgets, and monitors their implementation.

In addition, twice a year the President and Chief Executive Officer meets with all employees of the Caisse, as well as the expanded Executive Committee, which includes the main officers. Lastly, he meets with the main officers of the investment groups and the general services units on a regular basis to discuss their business objectives, projects and budgets.

2. ORGANIZE

The organizational structure and the regulation on internal management[1] define the roles and responsibilities of each member of the organization, from the Board of Directors to the employees, in the conduct of the Caisse's operations. At the same time, the Caisse's mission, ambition, investment philosophy and values serve to channel their efforts toward a common objective.

THE BOARD OF DIRECTORS AND INTERNAL AUDIT

The business operations of the Caisse are overseen by the Board of Directors, which consists of a maximum of 15 members, including the Chairman and the President and Chief Executive Officer. The Board of Directors has four committees: the Human Resources Committee; the Audit Committee; the Governance and Ethics Committee; and the Risk Management Committee (see the section "Board of Directors and Board committees").

The Board of Directors and its committees ensure that the Caisse's operations comply with the provisions of the Act respecting the Caisse and its regulations, and that the institution takes the measures required to achieve the objectives set out in its mission.

Internal Audit reports directly to the Chairman of the Audit Committee of the Board of Directors. From the administrative standpoint, it reports to the President and Chief Executive Officer.

SENIOR MANAGEMENT

The President and Chief Executive Officer is responsible for management of the Caisse in accordance with its regulations and policies. The senior managers have created various committees to assist them with their work and have assigned to them oversight and management of the institution's operations.

EXECUTIVE COMMITTEE

The Executive Committee has a mandate to advise the President and Chief Executive Officer regarding major decisions concerning the overall management of the organization. The Committee therefore oversees and monitors the institution's operations.

The section "Executive Committee" of the Annual Report presents the members of the Executive Committee.

The committees described below are under the jurisdiction of the Executive Committee, to which they report periodically.

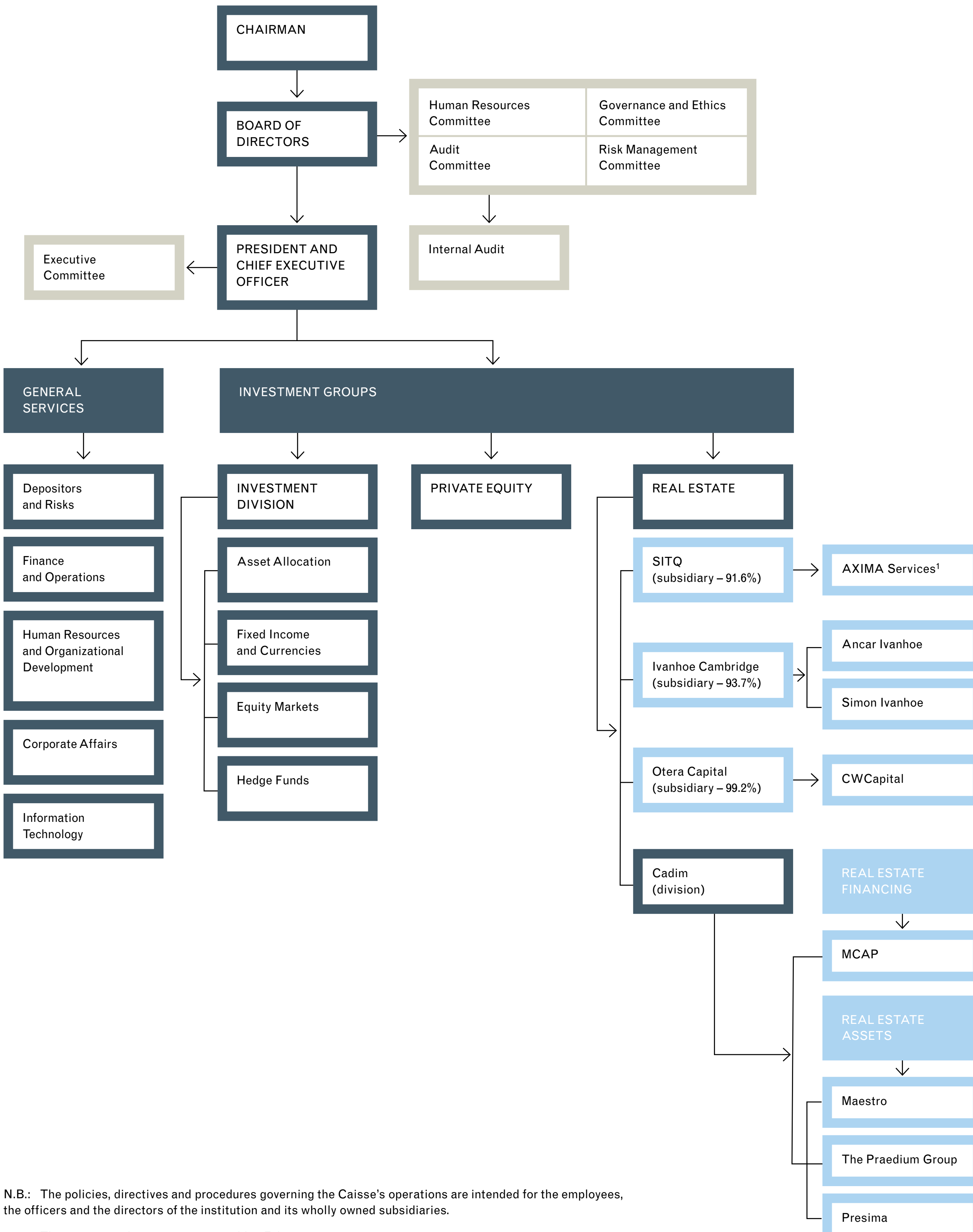
1 The regulation on internal management is available on line at www.lacaisse.com.

MANAGEMENT FRAMEWORK

FIGURE 101

ORGANIZATIONAL STRUCTURE

(as at December 31, 2008)



N.B.: The policies, directives and procedures governing the Caisse's operations are intended for the employees, the officers and the directors of the institution and its wholly owned subsidiaries.

1 The interest in this company was sold in February 2009.

Depositors and Risks Committee
The Depositors and Risks Committee (DRC) has a mandate to oversee and implement policies and systems designed to maintain an acceptable level of risk for the Caisse's operations. The DRC's responsibilities include interpreting depositors' investment policies, particularly in terms of market, liquidity and credit risk. It monitors and controls risks and reports regularly to the Risk Management Committee of the Board of Directors. The DRC also examines measures to be taken to manage risks adequately. It approves risk guidelines and limits to maintain the best possible balance between assumed risk and expected return.

Depending on the size of transactions and the level of authorization required, a specific committee, the DRC-Transactions, evaluates investment proposals submitted to it. As the case may be, the DRC-Transactions then approves the transaction or makes recommendations to the Chief Investment Officer, the President and Chief Executive Officer or the Risk Management Committee as well as to the Board.

Investment Division Committee
The Investment Division Committee has a mandate to review and approve the Caisse's main investment orientations, in addition to promoting collaboration between the investment groups.

The main responsibilities of the Investment Division Committee are to:

/ Approve, for each specialized portfolio, the investment philosophy, the long-term risk and return forecasts, and the significant changes to external management mandates;

/ Co-ordinate the sharing of information on market trends, best practices and definition of financial research programs, as well as monitor these programs and the related internal partnerships; and

/ Advise the Chief Investment Officer on asset allocation and investment strategies for each of the Caisse's 18 specialized portfolios.

Information Technology and Capital Budget Committee
The Information Technology and Capital Budget Committee has a mandate to maintain a technology platform adapted to the Caisse's operations, to approve major technology management policies and to ensure that projects are in keeping with the Caisse's strategic orientations.

The Committee also approves the annual plan for information technology projects and the related capital budget and submits them for approval to the Executive Committee. It also regularly monitors progress on various computer-related projects.

Disclosure Committee
The Disclosure Committee has a mandate to ensure compliance with the financial certification policy.[1] Its responsibilities include:

/ Reviewing the list of signing authorities for internal financial certificates and the texts of the financial certificates as well as making recommendations to the President and Chief Executive Officer;

/ Reviewing all the internal financial certificates, including conclusions and supporting documents;

/ Recommending changes to the financial reporting process or internal controls after reviewing the internal financial certificates;

/ Evaluating the design and effectiveness of the disclosure controls and procedures; and

/ Evaluating the design of the internal control for financial information and, beginning next year, its effectiveness.

INVESTMENT GROUPS AND GENERAL SERVICES GROUPS

The Investment Division, the Real Estate group, the Private Equity group and the five general services teams report directly to the President and Chief Executive Officer.

The Investment Division includes the investment groups active on liquid markets, namely Fixed Income and Currencies, Equity Markets and Hedge Funds, as well as asset allocation operations, including the Chief Strategist's activities. The Real Estate group has co-ordinated its main subsidiaries, namely Ivanhoe Cambridge, SITQ and, since January 1, 2009, Otera Capital, as well as its Cadim division. The Real Estate group's network includes other subsidiaries and affiliates.

The Caisse's investment groups work in co-operation with the five general services teams: Depositors and Risks; Finance and Operations; Human Resources and Organizational Development; Corporate Affairs; and Information Technology.

1 The financial certification policy is available on line at www.lacaisse.com.

3. EXECUTE

The Caisse has adopted various policies, directives and procedures governing its operations, for the employees, the officers or the directors of the institution and its wholly owned subsidiaries, as the case may be. These policies define the field of action of the employees and the business units in the exercise of their functions, including their relations with depositors, partners and other stakeholders. Some are broad and concern all employees, such as the human resources policy, whereas others cover specific activities or processes.

For example, the investment policies oversee the work of the portfolio managers. For each specialized portfolio, the investment policy defines the philosophy, management style, investment universe, benchmark index, value-added objective and risk oversight, including concentration limits. The policies result in directives and procedures specific to each management mandate. The managers therefore know the limits applicable to their investment operations and are obliged to respect them.

Finally, certain policies define the working environment of the Caisse's employees. They concern such matters as harassment at the workplace and application of the language policy.

4. CONTROL

The control functions are both centralized and decentralized; they may cover the Caisse as a whole or a specific process used by a business unit. Each control is designed to ensure that the policies, directives and procedures governing the Caisse's operations are applied and respected.

INTERNAL CONTROL[1]

The Caisse's internal control mechanism is applied systematically on all levels of the organization. It consists of an effective set of activities and measures, including validation, authorization, audit, data reconciliation, oversight, operational performance review and separation of duties.

To ensure its processes function in a coherent fashion, the Caisse has adopted an internal control policy that serves as an overall framework. Moreover, various aspects of internal control are covered by specific policies and other documents, such as the integrated risk management policy, the compliance policy, the disclosure policy, the financial certification policy, the plan for optimal resource use and the codes of ethics and professional conduct.

The Caisse's internal control mechanism provides a range of control functions on various levels, namely:

/ Control measures incorporated into activities, business processes and computer systems, and applied by those immediately responsible for them;

/ Control functions independent of the processes used for investment and transaction settlement and accounting processes;

/ Oversight functions, including the committees of the Board of Directors and those of senior management, as well as internal audit and compliance; and

/ External audit functions performed by the Auditor General of Québec and accounting firms, as well as monitoring by the credit rating agencies.

The internal control policy requires that senior management do overall self-assessments each year of the effectiveness of the general control environment and the fraud prevention and detection framework. In addition to these self-assessments, Internal Audit must assess the design and implementation of the processes and controls related to the general and information technology control environment.

1 The internal control policy is available on line at www.lacaisse.com.

FINANCIAL GOVERNANCE[1]

The Caisse has put in place a stringent financial governance policy to ensure the integrity of its financial processes and the reliability of the financial information that it prepares and communicates. The financial certification policy oversees and formalizes financial reporting by the Caisse and its subsidiaries. It is based on the principles of Multilateral Instrument 52-109 of the Canadian Securities Administrators, to which the Caisse is not subject. Application of the financial certification policy will be complete with the assessment of the effectiveness of internal control over financial reporting starting in 2009.

Under this policy, the Caisse must ensure that the financial information that it discloses faithfully reflects its financial position in all material respects and that this information is complete, actual, based on fair value and presented according to appropriate accounting standards. The policy also provides that the President and Chief Executive Officer and the Executive Vice-President, Finance and Operations, sign a public financial certificate each year. The certificates of both officers are at the beginning of the section "Returns and financial position" of the Annual Report. Both signatories rely on detailed work describing internal control over financial information as well as internal financial certificates signed by several officers of the Caisse and the subsidiaries.

The conclusions of the Disclosure Committee concerning the design of internal control over financial reporting and the effectiveness of the disclosure controls and procedures are given at the beginning of the section "Returns and financial position."

COMPLIANCE[2]

The purpose of the compliance policy is to ensure compliance with the laws, regulations, policies and directives applicable to the Caisse's operations, at all levels and in all functions. Compliance activities take several forms, such as documentation, dissemination and co-ordination of policies and directives, monitoring and implementation of compliance programs, and training of officers and employees.

The policy provides, for example, that the persons responsible for compliance provide the Board of Directors, the Risk Management Committee and the Executive Committee with the assurance that the compliance programs are applied. They must also provide the Audit Committee with the assurance that the mechanisms used to monitor compliance are sufficient and effective.

Moreover, compliance with the depositors' investment policies and the investment policies of the specialized portfolios constitutes an important part of the compliance programs applied on a half-yearly basis. Certificates of compliance with the policies are sent to senior management, the Board of Directors and the depositors.

In addition, the Board members, the officers and all employees of the Caisse must abide by a code of ethics and professional conduct. The code emphasizes the importance of ethical behaviour and professional conduct appropriate to business practices, respect for individuals and groups, and compliance with the laws, policies and regulations applicable to the Caisse.

Each year, all employees are obliged to reconfirm that they endorse the Code of Ethics and Professional Conduct. They must also report any situation where it is reasonable to believe that the Code has been infringed.

To avoid any conflict of interest, employees are subject to measures such as preauthorization of their personal transactions. As for the officers, they must place their portfolios in a blind trust or use an investment vehicle that does not give them a say in the selection of investments for their personal portfolios.

The codes of ethics and professional conduct are given in the Annual Report 2008 – Additional Information.

INTEGRATED RISK MANAGEMENT

Risk management goes hand in hand with the investment and portfolio management processes. In an increasingly demanding financial environment, where fund managers must take risks to achieve their target returns, robust risk management has become vital.

The relationship between risk and return is an integral part of the Caisse's operations. Moreover, the Caisse has always taken special care to identify, measure and oversee the risks related to its operations, especially active management of its investments. To that end, the Caisse has considerably stepped up its risk management activities in the past five years.

INTEGRATED RISK MANAGEMENT POLICY

In 2003, the Caisse developed a comprehensive, centralized approach to risk management oversight. To that end, it adopted an integrated risk management policy (IRMP) to ensure integrated risk management and better decision making within the Caisse's investment groups and general services teams.

The policy, which is revised regularly, is conducive to a risk management culture based on rigorous practices and helps the Caisse carry out its mission for the depositors. More specifically, it defines risk management governance at the Caisse, sets the level of risk deemed acceptable to prevent excessive losses, aligns this level of risk with value-added objectives and, lastly, promotes effective allocation of risk.

1 The financial certification policy is available on line at www.lacaisse.com.

2 The compliance policy and the codes of ethics and professional conduct are available on line at www.lacaisse.com.

MANAGEMENT FRAMEWORK

The IRMP is the cornerstone of risk oversight and covers all facets of risk management. It provides reporting mechanisms for each of these levels and it defines and describes such matters as:

/ The main principles: the risk model and the independence of the support teams in integrated risk management;

/ The organizational structure, the normative framework, governance and sharing of responsibilities;

/ The risk budgets;

/ The limits on transaction authorization and management outsourcing as well as limits on concentration by issuer;

/ The framework for outsourcing of management and use of derivative financial instruments; and

/ The management of various types of risk.

Levels of control
Risk management is ultimately the responsibility of the Board of Directors, but it is delegated to the managers on all levels so as to integrate it into the decisions they make each day. It applies to all Caisse employees and mandataries in the performance of their duties. Governance of risk management is based on three levels of control:

Level 1 – The portfolio managers, who are primarily responsible for managing the risks related to their daily operations;

Level 2 – The Depositors and Risks Committees (DRC and DRC-Transactions), with assistance from the Risk Management team, the Executive Committee and the compliance unit; and

Level 3 – The Board of Directors and its Risk Management and Audit Committees, as well as Internal Audit.

To ensure the required objectivity and rigour, teams that are independent of the portfolio managers are responsible for defining and monitoring the integrated risk management policy as well as the investment policies applying to the specialized portfolios.

Investment policies and risk budgets
The investment policies oversee the work of the portfolio managers. For each specialized portfolio, the investment policy defines the philosophy, management type, investment universe, benchmark index, value-added target and risk oversight, which includes concentration limits and risk limits.

A risk limit, or risk budget, is determined for each level of control. It takes into account the value-added objectives for each portfolio and is based on a target information ratio. For the Caisse's overall portfolio, the risk limit reflects the diversification effect of all the specialized portfolios.

THE CAISSE'S RISK MODEL

To manage risks properly, it is essential to be able to identify them and understand all their facets so that they can be evaluated. The risk model is therefore the basis of risk management at the Caisse. It establishes a common language, so that the various stakeholders can communicate effectively regarding risk management.

The risk model is also conducive to rigorous and exhaustive analysis of each risk. Ultimately, this process contributes to investment strategies that generate stable, optimal returns that meet depositors' expectations.

According to this model, the risks inherent in the Caisse's operations are divided into three broad categories: business risks, financial risks and operational risks. These categories are then subdivided to clearly distinguish each possible risk. Each risk requires a specific management approach that is often quite different from those used for the other risks.

FIGURE 102
THE CAISSE'S RISK MODEL

Business risks

Strategic risk

The Caisse is exposed to strategic risk when an event related to its practices or relations, or those of its subsidiaries or employees, does not comply with its mission, culture and fundamental values. Strategic risk is also related to the inadequacy of business strategies or deficiencies in the implementation of the organization's strategic orientations. Finally, the Caisse will be exposed to a strategic risk if its resources are not allocated as a function of established priorities.

The Caisse manages this risk with a structured strategic planning process that involves all units of the organization. Strategic orientations are proposed by the Executive Committee, approved by the Board of Directors and communicated to all employees. Annual business plans are then established. The members of the Board of Directors and of the Executive Committee receive a monthly summary of the Caisse's operations. Moreover, the President and Chief Executive Officer monitors the business plans of all units on a regular basis.

Reputation risk

Reputation risk is the possibility that an event related to the business practices or relations of the Caisse, its subsidiaries or its employees will adversely affect the Caisse's image or cause the public to lose confidence in the institution. This risk could detract from the organization's ability to achieve its objectives.

All directors, members of management and employees are responsible for carrying out their activities in such a way as to minimize reputation risk.

The Caisse manages and controls this risk by means of codes of ethics and professional conduct for directors, officers and employees, training programs, effective internal management and governance practices and various policies and procedures. It also ensures that the information it provides internally and externally is truthful and has been checked. It strives to ensure the public and the media gain a better understanding of its operations. The Caisse also rigorously monitors communications concerning it and responds by taking public positions as required.

Financial risks

Market risk

Market risk represents the risk of financial loss resulting from fluctuations in the price of financial instruments. The value of a financial instrument may be affected by changes in certain market parameters, such as interest rates, foreign exchange rates, share prices and commodity prices as well as their volatility. The risk results from the volatility of the price of a financial instrument, which itself arises from the volatility of such market variables.

The Caisse manages all market risks in an integrated, comprehensive fashion, so that the main factors contributing to risk, such as industry, country and issuer, are taken into account in the analysis of market risk.

The Caisse may use derivative financial instruments that are traded on exchanges or directly with banks and securities dealers to manage the market risks to which it is exposed.

Market risk at the Caisse is measured according to a statistical technique known as value at risk (VaR). This technique, used by most investment firms and financial institutions, covers almost all the assets held by the Caisse. The Caisse determines the VaR for each instrument in its specialized portfolios and aggregates the information for the overall portfolio.

The Caisse uses the historical simulation method to estimate VaR. It uses 800 days of observation of risk factors, such as changes in foreign exchange rates, interest rates and financial asset prices, to estimate the volatility of returns and the correlation between asset returns. The Caisse uses an 84% confidence level in its calculation.

VALUE AT RISK (VaR)

Value at risk (VaR) is based on the statistical measurement of the volatility of the market value of a position and its correlations. VaR uses historical data to estimate the loss expected during a given period according to a predetermined confidence level. For example, a publicly traded share with a price of $100 and a standard deviation of 1% has a daily VaR of $1.00 with an 84% confidence level. Thus there is a probability of 16% that the value of the share will lose more than $1.00 in one day.

One of the advantages of VaR is that it makes it possible to include the risk of a wide range of investments in only one measure, therefore providing an overall risk measurement for a portfolio and even for a set of portfolios.

The historical simulation method is based primarily on the assumption that the future will be similar to the past. This method requires a series of historical data for all the risk factors required to estimate the returns on instruments. In the absence of such historical data, particularly for less liquid products, such as private equity and real estate, substitute securities and various mathematical models have to be used to evaluate VaR.

In addition, VaR measures risk during normal market conditions. It does not estimate the loss that positions may incur during extreme market fluctuations, such as those that occurred in the fall of 2008. A realized loss may also differ significantly from VaR when the historically observed interrelationship between risk factors is disrupted. Lastly, VaR is not a single measure that can be used alone. Complementary methods are required to assess risk properly.

MANAGEMENT FRAMEWORK

Two types of risk are estimated, namely the absolute VaR of the Caisse's benchmark portfolio and the Caisse's overall portfolio, and the VaR of active management.

For more details on the estimate of absolute risk and the active risk of the overall portfolio for each of the Caisse's specialized portfolios, consult the section "Combined financial statements," particularly note 8, "Identification and management of risks related to investment activities," and the section "Analysis of overall performance."

For more details on the active risk of the specialized portfolios, consult the section "Analysis of specialized portfolio returns by investment group."

In addition, because VaR is not designed as a single risk management tool, the Caisse uses complementary limits and measures. For example, the investment policies define concentration limits (geographic, sector, instrument type, issuer, etc.). Loss limits are also defined for each management mandate. The Caisse also uses stress tests to evaluate the losses of a specialized portfolio and of the Caisse's overall portfolio in unusual circumstances. To do so, it uses historical events, such as the 1987 stock market crash and the 1991 Persian Gulf War, or simulations of fluctuations in risk factors, such as equity prices, foreign exchange rates, interest rates and commodity prices.

STRESS TEST

The stress test is a risk measurement that complements VaR and makes it possible to estimate the impact of unusual circumstances on returns. These circumstances have a low probability of occurring but are likely to give rise to substantial losses. Using extreme historical scenarios, such as the 1987 stock market crash, and hypothetical scenarios, the stress test measures a position's loss of value as a result of a variation in one or more often interrelated risk factors, such as equity prices, interest rates, credit spreads, foreign exchange rates, commodity prices and market volatility.

Like VaR, the stress test includes the risk of many positions in a single overall measurement that makes it possible to analyze losses for a portfolio and for a set of portfolios, according to the extreme scenarios retained.

Credit, concentration and counterparty risk

Credit risk

Credit risk is the possibility of a loss of market value in the event that a borrower, an endorser, a guarantor or a counterparty does not honour its obligation to repay a loan or to fulfill any other financial obligation, or sees its financial situation deteriorate.

The analysis of credit risk includes measurement of the probability of default and the recovery rate on debt securities held by the Caisse, as well as monitoring of credit-quality changes for the issuers and the groups of issuers[1] held in the Caisse's portfolios. In 2008, the main rating agencies raised the long-term credit ratings of 115 groups of issuers whose securities are held by the Caisse and lowered the ratings of 223 others.

Certain groups of issuers do not have a credit rating determined by the main rating agencies because of investment confidentiality, absence of debt, investment restructuring or a combination of these factors. In the case of mortgage loans that have no credit rating, the analysis of credit risk is done partially on the basis of the loan-value ratio. According to this ratio, the amount lent is divided by the fair value of the collateral securing the loan at the date of underwriting or provision of funds or at any other time during the term.

In managing credit risk, the Caisse frequently monitors changes in the ratings issued by agencies and does a comparison with internal credit ratings, when they are available.

Concentration risk

The analysis of concentration risk measures the fair value of all financial products (fixed-income and variable-income securities) related to a single issuer or a group of issuers with common characteristics (region, sector and credit rating).

The concentration limit for a group of issuers is set at 3% of the Caisse's total assets, with the exception of securities issued by the governments of Canada, Québec or another Canadian province or territory, as well as their departments and agencies, which are not subject to a concentration limit.[2] Sovereign issuers with a AAA credit rating are also excluded from this concentration limit. Concentration limits are also established for more-specific issuer characteristics.

For more details on concentration by credit rating for the Caisse's groups of issuers and the breakdown of mortgage financing by loan-value ratio, consult the section "Combined financial statements," particularly note 8, "Identification and management of risks related to investment activities."

1 A group of issuers is a set of issuers controlled by a parent company.

2 Exposure to an issuer arising from positions in derivatives is not taken into account in the analysis of concentration risk.

ABSOLUTE RISK AND ACTIVE RISK

Any investment decision involves an element of risk, including the risk of a financial gain or loss arising from a fluctuation in the value of the financial instruments held in a portfolio.

The absolute risk of the benchmark portfolio and that of the overall portfolio are calculated according to the same method, but cover different portfolios, namely the benchmark portfolio targeted by the depositors and the overall portfolio actually invested by the Caisse.

The absolute risk of the Caisse's benchmark portfolio is the result of the risk (volatility) of the benchmark indexes of the assets that make up the portfolio. For example, if the depositors generally decide to increase the proportion of bonds relative to the proportion of publicly traded equities in their benchmark portfolios, the risk will automatically be reduced, given the lesser volatility of bonds. At the same time, the expected long-term absolute return will also decrease.

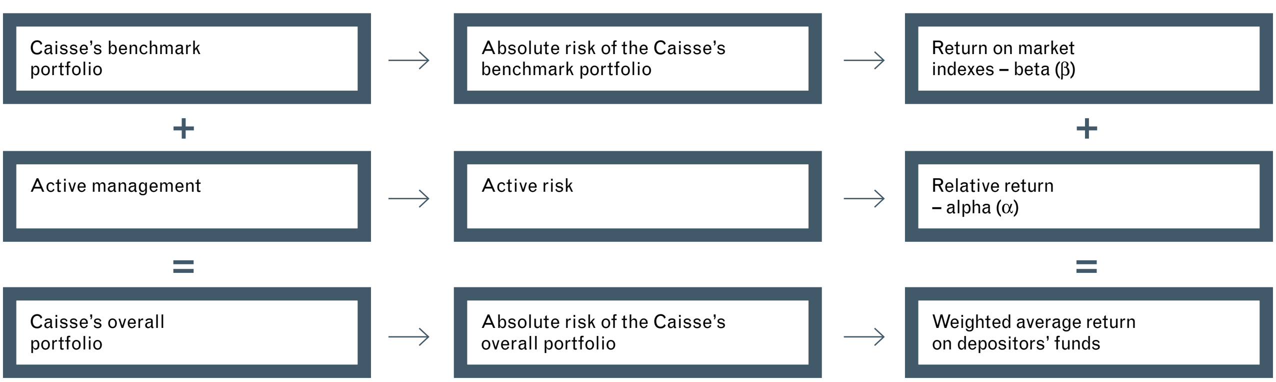
The absolute risk of the overall portfolio is the result of the risk (volatility) of the positions that make up the Caisse's overall portfolio.

Active risk represents the possibility that the Caisse will obtain a return that is different from that of its benchmark portfolio by managing its overall portfolio actively. The greater the active risk, the more the absolute return expected on the overall portfolio will differ from the return on the benchmark portfolio.

The absolute risk of the Caisse's benchmark portfolio and the active risk and the absolute risk of the overall portfolio are measured regularly and are subject to various limits.

Figure 103 shows the components of the Caisse's risk and return.

FIGURE 103
COMPONENTS OF THE CAISSE'S RISK AND RETURN



MANAGEMENT FRAMEWORK

Counterparty risk
Counterparty risk corresponds to the credit risk from current or potential exposure related to the Caisse's operations involving over-the-counter derivative financial instruments.

Transactions involving derivatives are carried out with institutions whose credit rating is established by recognized rating agencies and whose operational limits are set by senior management. Moreover, the Caisse enters into legal agreements based on the standards of the International Swaps and Derivatives Association[1] to benefit from the offsetting effect of the amounts at risk and the exchange of collateral. In this way, it limits its net exposure to this credit risk.

This risk is measured by counterparty, according to the legal agreement in effect, on the basis of which it is possible to calculate net exposure resulting from a set of over-the-counter derivative financial instruments and the collateral exchanged.

For more details on the Caisse's net exposure to counterparty risk, consult the section "Combined financial statements," particularly note 8, "Identification and management of risks related to investment activities."

Financing-liquidity risk
Financing-liquidity risk is the possibility that the Caisse may not always be able to fulfill the undertakings regarding its financial liabilities without having to obtain funds at abnormally high prices or that it may be obliged to sell assets. It also corresponds to the risk that it may not be possible to sell investments rapidly or to invest without having a significant adverse impact on the price of the investment in question.

Compliance with established rules is monitored on a monthly basis, and liquidity status is monitored on a daily basis. The Caisse simulates various scenarios to estimate the potential impact of different events on its liquidity situation. The managers responsible for liquidity management assess the liquidity of the markets on which the Caisse's financing operations are based. They ensure the Caisse is present on the various financial markets and maintain relationships with the agencies that rate the Caisse as well as its lenders.

For more details on the summary of investment maturities at face value and liabilities related to investments, consult the section "Combined financial statements," particularly note 8, "Identification and management of risks related to investment activities."

For more details on the Caisse's financing operations, consult the section "CDP Financial."

Operational risks
Operational risk corresponds to the possibility of direct or indirect financial loss arising from the deficiency of operations.

Operational risks are managed and estimated through self-assessment of risks, a listing of incidents, the use of indicators and maintenance of rigorous processes. The Caisse continues to introduce methods to evaluate and manage these risks.

Human resources management risk
The risk related to human resources management includes such elements as recruiting (recruiting competent, honest and motivated personnel), training (maintaining and developing employee competencies) and evaluating performance and compensation (ensuring fair, equitable and competitive compensation).

Process management risk
The risk related to management of the Caisse's processes applies to processes for input, settlement and tracking of transactions, and errors that may arise in the execution of the processes in place. In addition to internal causes specific to the Caisse, this risk may arise from the poor quality of services rendered by its subcontractors, external suppliers and business partners.

System management risk
The Caisse is exposed to a risk in the event of deficiency of its information technology infrastructures or computer systems. This deficiency may result from a breakdown or other malfunction that may cause delays or an interruption in operations that is not caused by a disaster.

Theft and fraud risk
This is the risk of losses arising from intentional acts to defraud, to embezzle funds or to appropriate the assets of the Caisse or its depositors.

Disaster risk
The risk of disaster represents the risk of losses arising from interruption of business as a result of a natural or other disaster.

Compliance risk
Compliance risk corresponds to the risk of losses as a result of a deficiency that is unintentional or due to negligence, to policies and directives, and to professional and ethical standards and practices specific to the Caisse's operations. It occurs in the event that the Caisse fails to fulfill its duties.

1 The ISDA promotes sound risk management practices and issues legal opinions on netting and collateral arrangements.

Legal risk

Legal risk is related to the rights and obligations associated with the Caisse's operations and the legislative framework in which they are carried out. Important aspects of legal risk are related to compliance with the laws and regulations governing the Caisse and its management teams. They also depend on the assurance that the agreements concluded by the Caisse properly reflect the planned operations and contain the appropriate provisions. Legal risk also refers to the risk of lawsuits that may affect the Caisse.

COMPARISON WITH BEST PRACTICES

To ensure constant improvement, the Caisse regularly revises its integrated risk management policy and related practices, which were developed and implemented more than five years ago.

The economic and financial conditions of recent years were conducive to the emergence of increasingly complex products that were correspondingly opaque. In that context and as a result of the ABCP episode in 2007, the Caisse took initiatives such as the requirement of two credit rating sources for a financial instrument to be considered rated, a moratorium on any new financial instruments and implementation of centralized monitoring.

It then began to review its risk management practices and to benchmark them against those of its peers and the financial sector. It retained the services of an external firm to perform a general, independent review of all the Caisse's risk management practices.

The consulting firm evaluated various factors divided into two groups: design of risk management practices and their effectiveness. The main conclusions of the study show that the Caisse's conception of risk management generally corresponds to the practices in effect but that the effectiveness of its application is slightly lower.

THREE-YEAR PLAN TO IMPROVE RISK MANAGEMENT

The Caisse has adopted a three-year plan to raise its risk oversight and assessment methods to the level of the industry's best practices. As a result of the events of the fall of 2008, the Caisse has accelerated this plan.

The plan will enable the Caisse to manage the risks assumed in active management of its various portfolios more effectively. This ambitious plan is based on five components:

/ Strengthening the risk management culture;

/ Development of risk management practices for unforeseeable events;

/ Implementation of an approval process for new operations;

/ Refinement of risk measurement and methodology; and

/ Optimization of the resources required to make the plan a success.

TABLE 104

REVIEW OF THE CAISSE'S RISK MANAGEMENT PRACTICES

	Design of risk management			Effectiveness of the application of risk management practices		
	Practice to be improved	Similar to industry practices	Best industry practices	Practice to be improved	Similar to industry practices	Best industry practices
Policies			X		X	
Governance and levels of control		X			X	
Risk model		X			X	
Culture		X		X		
Approval of new products			X		X	
Market risk measurement						
Methodology		X			X	
VaR estimation frequency	X			X		
Stress tests	X			X		
Measurement of credit, liquidity and operational risk		X			X	

MANAGEMENT FRAMEWORK

TABLE 105
THREE-YEAR RISK MANAGEMENT PLAN

Three-year plan	Main actions
Strengthen the risk management culture	/ Create five specialist positions, reporting to the Risk Management team, to support the investment groups / Revise the mandate and composition of the risk committees / Develop information and training sessions / Put in place a structured, uniform process to deal with abnormal situations
Establish risk management practices to deal with the unforeseeable	/ Strength stress tests to identify the risk associated with extreme scenarios / Review the notional limits for derivative financial instruments and the nominal limits / Revise all investment policies / Perform backtests to compare actual return with estimated risk / Improve oversight of the risk associated with geographic concentration, especially for emerging markets / Centralize monitoring of markets to detect any event that may affect risk measurement / Identify rising and substantial risk concentrations
Optimize the approval process for new operations	/ Review oversight of derivatives use / Improve the current approval process, taking into account strategic consequences, a cost-benefit analysis, and financial and operational risks
Refine risk measurement and methodology	/ Incorporate all risk products and factors into the software used to measure market risk and increase measurement frequency / Complete implementation of internal credit and counterparty ratings / Develop credit and counterparty VaR / Define concentration risk indicators / Develop additional liquidity risk scenarios / Review operational risk indicators / Complete centralized collection of operational incidents
Put in place the necessary resources	/ Hire and integrate new resources / Strengthen data management and information systems used for risk management

5. EVALUATE

The evaluation function checks whether risks are managed adequately to achieve objectives. This function can be exercised in a centralized or decentralized manner, internally and externally.

INTERNAL AUDIT

Internal Audit's mission is to provide objective assurance and consultation services to increase the effectiveness of the Caisse's operations. It helps to achieve the Caisse's objectives by using a systematic and methodical approach to assess the processes and systems used for risk management, control and corporate governance. It also helps improve them by making proposals to increase their effectiveness.

The scope of the work done by Internal Audit must make it possible to determine whether the processes, systems and controls, as they have been developed and implemented, are sufficient and are applied in such a way as to ensure that:

/ Risks are defined, evaluated and managed adequately;

/ Financial and operational information is authorized, reliable and available in a timely fashion;

/ Directives, policies, laws, regulations and statutory requirements are respected;

/ Human, informational, material and financial resources are acquired economically, used efficiently and protected adequately; and

/ Business programs, plans and objectives are carried out effectively, in accordance with the Caisse's mission.

Internal Audit reports functionally to the Audit Committee. From the administrative standpoint, it reports to the President and Chief Executive Officer. The organizational structure is designed to ensure Internal Audit has the independence required to perform its role effectively.

EXTERNAL AUDIT

External oversight is provided by various authorities. The Auditor General of Québec audits the Caisse's financial statements each year and takes part in various investment valuation processes during the year. Independent accounting specialists periodically assess the fair value of unlisted liquid investments, private equity and real estate. Independent auditors assess the Caisse's compliance with the GIPS® performance standards in establishing and presenting its returns. Lastly, three rating agencies evaluate the Caisse's credit profile and ability to discharge its financial undertakings.

6. REPORT AND COMMUNICATE[1]

The Caisse is bound to each depositor by a service agreement that defines the responsibilities of each party and specifies the conditions and frequency for the Caisse's reporting on its work. The agreements provide for monthly investment reports and individual meetings every six months. The depositors are also invited to seminars and events organized specifically for them so that they can assess the various economic and financial factors affecting their portfolios.

In its communications, the Caisse strives to achieve a balance between its desire for transparency and its obligation to protect depositors' interests, while complying with the law and its undertakings toward third parties. To that end, the Caisse has adopted an information disclosure policy for its external communications. The policy defines the way the Caisse processes and discloses information to the media and the public, mainly through its press releases, press conferences and Annual Report.

The Caisse is obliged to disclose information to comply with certain laws governing it, including its constituting statute, the Access Act and securities legislation. Although it is not subject to the disclosure requirements and recommendations applicable to publicly traded companies, it strives to comply with the best disclosure practices of its industry.

The many types of information disclosed include:

/ Insider-trading transactions in accordance with the disclosure requirements of securities legislation;

/ Material facts, such as decisions affecting the institution as a whole or a major investment;

/ The exercise of its voting rights; and

/ Its audited combined annual financial statements, the tables of returns presented in Annual Report 2008 – Additional Information and the press release announcing its annual results.

Internally, the Caisse ensures that the Board of Directors and the Executive Committee, as well as their committees, receive complete information in a timely fashion and that feedback mechanisms permit effective discussion. The Caisse also takes care to communicate effectively with its employees through open, sustained and transparent communication. For instance, it aims to inform its employees adequately of its business objectives, strategies and projects as well as news concerning it. The Caisse also ensures that news disseminated externally is announced beforehand to its employees. In this way, it promotes cohesion and a sense of belonging within the institution. Lastly, it encourages transparent discussions within and between its teams, and promotes person-to-person interaction through various communication channels.

1 The information disclosure policy is available on line at www.lacaisse.com.

7. OPTIMIZE[1]

The Caisse ensures that the funds entrusted to it by depositors are managed with due regard for economy, efficiency and effectiveness. Economy involves acquiring resources of the required quality, at a reasonable cost and in a timely fashion. Efficiency involves ensuring that resources are sufficient for the business requirements and are used appropriately. Effectiveness is measured by the degree to which an organization achieves its business objectives.

To achieve optimal use of resources, the Caisse ensures that:

/ Its strategic orientations, business plans, management practices used for administration, operations and control, and systems and tools are established or designed so that their implementation generally allows the organization to achieve the results it seeks, which is referred to as "effectiveness"; and

/ It acquires and manages the resources needed to achieve results with due regard for "economy" and "efficiency."

The Caisse's resources, processes, systems, tools and controls are designed to form a coherent whole in order to meet depositors' expectations. To reach that objective, the Caisse optimizes its resources so as to:

/ Achieve depositors' target returns;

/ Develop management practices that correspond to the best practices used by institutional fund managers; and

/ Make proper use of the funds placed at its disposal to manage its operations.

The Caisse ensures optimal use of resources with a three-year plan that proposes permanent activities and projects to improve management of investment and operational resources. Investment resources include depositors' holdings and the risk budget, while operational resources include human, material, financial, technological and informational resources.

The plan is based on the following principles, in accordance with the applicable legislation:

/ Operational resources are acquired and managed by means of mechanisms that provide sufficient resources to successfully carry out the main activities and to prudently manage costs and changes in them;

/ Investment resources are managed actively by means of sufficient operational resources to successfully carry out activities with a substantial impact on returns;

/ The effectiveness of resources is assessed comprehensively by a comparison of the results obtained with industry standards, namely benchmark indexes;

/ The Caisse's structures, activities and methods are subject to a continual improvement process; and

/ The work of Internal Audit helps strengthen the management practices used for administration, operations and control, as well as the Caisse's systems and tools.

EXERCISE OF VOTING RIGHTS AND RESPONSIBLE INVESTMENT[2]

The Caisse exercises its voting rights systematically according to the guidelines defined in its policy on the exercise of voting rights. Analyzing resolutions and taking a position on them involve considerable work, since it is a shareholder in more than 4,000 Canadian and foreign companies.

Resolutions from company management concern mainly governance, such as the election of directors and compensation. Most of the resolutions submitted by shareholders also concerned governance, but a large number are related to environmental and social issues.

The Caisse processed 4,152 proxy voting files involving Canadian and foreign companies during the year. The files involved analyzing and voting on a total of 38,199 proposals.

The Caisse expects its portfolio companies to respect principles of good governance, fundamental rights and freedoms, workers' rights and the local communities where they operate. It has therefore adopted a policy on socially responsible investment, which advocates an approach based on dialogue with companies.

In addition to examining the financial position of companies, the managers therefore include environmental, social and governance criteria in the analysis preceding their investment decisions. They also take advantage of discussions with these companies to inform them of the Caisse's concerns regarding corporate responsibility. The Caisse may occasionally submit proposals to shareholder meetings if the social record of a portfolio company is not satisfactory. Ultimately, the Caisse may sell the investment if the dialogue does not produce the expected results.

The Caisse is also involved in international efforts to ensure socially responsible investment. In 2006, it became one of the first signatories to the Principles of Responsible Investment of the United Nations. It has also endorsed the Carbon Disclosure Project, which enables investors to determine the impact of companies' operations on climate change.

1 A document on the Caisse's approach to optimal use of resources is available on line at www.lacaisse.com.

2 The policy on the exercise of voting rights, the details of the Caisse's voting and the policy on socially responsible investment are available on line at www.lacaisse.com.

BOARD OF DIRECTORS AND BOARD COMMITTEES

BOARD OF DIRECTORS

(as at December 31, 2008)

/ FERNAND PERREAULT
/ OUMA SANANIKONE
/ A. MICHEL LAVIGNE
/ CHRISTIANE BERGEVIN
/ JOCELYNE DAGENAIS
/ CLAUDE GARCIA
/ CLAUDETTE CARBONNEAU

/ ANDRÉ TRUDEAU
/ ALBAN D'AMOURS
/ LOUISE CHARETTE
/ STEVEN M. CUMMINGS
/ YVAN ALLAIRE
/ PIERRE BRUNET
/ HENRI MASSÉ (absent)

CHANGES TO THE BOARD OF DIRECTORS IN 2008

/ Two directors, Jocelyne Dagenais and André Trudeau, joined the Board at the start of 2008.

/ One of the directors, Sylvie Dillard, left the Caisse's Board during the year.

/ Henri Massé also resigned as a director early in 2009.

/ Since the President and Chief Executive Officer is an ex-officio member, the changes to Caisse senior management in 2008 also affected the composition of the Board of Directors.

BOARD OF DIRECTORS

PIERRE BRUNET

Chairman of the Board

Chairman of the Human Resources Committee

Member: Governance and Ethics Committee

Board member since April 27, 2005

Pierre Brunet was President and Chief Executive Officer of National Bank Financial for many years. He has also served as Chairman of the Board of Governors of the Montréal Exchange, the Montréal Board of Trade, the Investment Dealers Association, the Canadian Institute of Chartered Accountants and the Montréal Symphony Orchestra. He is currently Chairman of Montréal International and a director of METRO Inc. Mr. Brunet's many honours include the title of Fellow of the Ordre des comptables agréés du Québec, the Career A+ award from the IDA , the Order of Merit from the Université de Montréal and Officer of the Order of Canada.

FERNAND PERREAULT

President and Chief Executive Officer
Caisse de dépôt et placement du Québec

Board member since January 7, 2009

Before his appointment, Fernand Perreault was Executive Vice-President, Real Estate, of the Caisse and Chairman of the boards of directors of the group's main companies, namely Cadim, Ivanhoe Cambridge, Otera Capital and SITQ. Mr. Perreault was previously President and Chief Executive Officer of SITQ from 1987 to 1995.

Mr. Perreault has a law degree from the University of Ottawa and before joining the Caisse was Vice-President, Mortgage Insurance, at Canada Housing and Mortgage Corporation (CMHC).

YVAN ALLAIRE

Chairman
Institute for Governance of Private and Public Organizations (HEC-Concordia)

Chairman of the Governance and Ethics Committee

Member: Risk Management Committee

Board member since April 27, 2005

Yvan Allaire holds a doctorate in management science from the Massachusetts Institute of Technology and is a Fellow of the Royal Society of Canada, as well as Professor Emeritus of Strategy at the Université du Québec à Montréal. He is Chairman of the Institute for Governance of Private and Public Organizations (HEC-Concordia). Mr. Allaire is a member of the Conseil des relations internationales de Montréal (CORIM) and the National Committee (Canada) of the Aga Khan Foundation.

CHRISTIANE BERGEVIN

Senior Vice-President and General Manager
Corporate Projects
SNC-Lavalin Group Inc.

Member: Audit Committee

Board member since August 28, 2007

Christiane Bergevin is a graduate of McGill University and the Wharton School of Business. She has held various senior management positions, notably in international finance, with SNC-Lavalin Group subsidiaries since 1990. She was President of SNC-Lavalin Capital from 2001 to 2008, and was appointed Senior Vice-President and General Manager of the SNC-Lavalin Group in 2009. She is recognized in Canada and internationally for her financing leadership, and has been involved in many acquisitions and arranged numerous major financings, particularly in energy and infrastructure. Ms. Bergevin is a director of the Business Development Bank of Canada and the Chair of its Pension Funds Investment Committee. She is also a director of Cordiant Inc. and a former director of the Financial Women's Association of Québec and numerous philanthropic organizations.

CLAUDETTE CARBONNEAU

President
Confédération des syndicats nationaux

Member: Audit Committee

Board member since September 25, 2002

Claudette Carbonneau holds a bachelor's degree in political science and is the first woman to serve as President of the Confédération des syndicats nationaux (CSN), a position she has held since 2002. She is also Chair of Fondaction and Vice-President of the General Council of the International Trade Union Confederation and First Substitute of the Canadian delegation to the ITUC General Council. Ms. Carbonneau is also a member of the Québec government's Advisory Council on Labour and Manpower.

LOUISE CHARETTE

Corporate Director

Member: Risk Management Committee

Board member since April 27, 2005

Louise Charette holds a master's degree in business administration and a doctorate in mathematics. From 1981 to 2007, she held various management positions at the Commission de la construction du Québec, including Assistant Director General, Administration and Finance. In addition to her duties as Assistant Director General, she also headed the CCQ's Investment Committee. Ms. Charette has worked for a number of organizations. She was a founding member of the Regroupement des femmes cadres du Québec in 1984 and served as Vice-Chair of the Société d'habitation du Québec from 1998 to 2002.

STEVEN M. CUMMINGS, CM

President and Chief Executive Officer
Maxwell Cummings & Sons Holdings Ltd.

Member: Human Resources Committee

Board member since October 1, 2003

Steven M. Cummings is President and Chief Executive Officer of Maxwell Cummings & Sons Holdings Ltd. Active in community affairs, Mr. Cummings is a past President of Federation CJA and has served as President of the Jewish General Hospital Centre Board and its Foundation Board. He is also Founding Chair of the Montreal Holocaust Memorial Centre and Founding Co-Chair of ProMontreal. He is currently Co-Chair of the Canadian Council for Israel and Jewish Advocacy. Mr. Cummings is also a Member of the Order of Canada.

ALBAN D'AMOURS

Former President and Chief Executive Officer
Desjardins Group

Chairman of the Risk Management Committee

Board member since August 24, 2000

Alban D'Amours completed doctoral studies, specializing in monetary theory, public finance and econometrics. After teaching for several years, he held a number of positions in Québec's public service, including Deputy Minister of Revenue and Associate Deputy Minister of Energy. He joined the Confédération des caisses populaires et d'économie Desjardins du Québec in 1988 and has held several management positions since then. Mr. D'Amours was elected President of the Desjardins Group in 2000 and was re-elected in 2004.

JOCELYNE DAGENAIS

President
President and Chief Executive Officer
Commission administrative des régimes de retraite et d'assurances

Board member since January 1, 2008

Jocelyne Dagenais has been President and Chief Executive Officer of the Commission administrative des régimes de retraite et d'assurances (CARRA) since December 3, 2007. She has worked for the Québec public sector since 1977. Ms. Dagenais has held various positions, including Deputy Minister and Assistant Deputy Minister, with various departments. She has also been a member of many boards of directors, including those of Services Québec, the Centre des services partagés, the Régie de l'assurance maladie du Québec and Canada Health Infoway.

CLAUDE GARCIA

Corporate Director

Chairman of the Audit Committee

Guest member: Risk Management Committee

Board member since April 27, 2005

Claude Garcia has completed the course requirements for a doctorate from the London School of Economics and Political Science and is a Fellow of the Canadian Institute of Actuaries and the Society of Actuaries. In 1983, he joined Standard Life Insurance, where he held several senior management positions. In 1993, he was named President of the company's Canadian operations and served in that capacity until the end of 2004. Mr. Garcia has been actively involved with a number of organizations and currently sits on the boards of Cogeco, Cogeco Cable, The Excellence Life Insurance Company, Goodfellow, BTB Real Estate Investment Trust and the Institut de recherches cliniques de Montréal. He is also Chairman of the Agence des Partenariats public-privé du Québec.

A. MICHEL LAVIGNE

Corporate Director

Member: Audit Committee

Board member since April 27, 2005

A. Michel Lavigne was President and Chief Executive Officer of Raymond Chabot Grant Thornton until May 2005. He was also Chairman of Grant Thornton Canada and a director of Grant Thornton International. His directorships include Quebecor Media, TVA, Primary Energy Recycling and Nstein Technologies. Mr. Lavigne has received many distinctions; most notably, he is a Fellow of the Ordre des comptables agréés du Québec.

HENRI MASSÉ

Fédération des travailleurs et travailleuses du Québec

Member: Risk Management Committee

Board member since January 27, 1999

Henri Massé headed the Fédération des travailleurs et travailleuses du Québec (FTQ) as Secretary General and then as President from 1993 to 2007. He was also Chairman of the Board and Chairman of the Executive Committee of the Solidarity Fund QFL, and a member of the Board of Directors of the Commission de la santé et de la sécurité du travail. Mr. Massé has also served on various committees of the Conseil consultatif du travail et de la main-d'oeuvre, as well as the Executive Committee of the International Confederation of Free Trade Unions.

OUMA SANANIKONE

Corporate Director

Member: Governance and Ethics Committee

Board member since August 28, 2007

Ouma Sananikone is a corporate director with extensive experience on the European and Asian financial markets. She has worked for 25 years in banking, financial services and investment management. She is Chairman of Smarte Carte International and a non-executive director of Icon Systems, Air-Serve and Moto Hospitality Services. Ms. Sananikone has been a board member of numerous public and private companies, as well as charitable organizations, in Australia and elsewhere. Her special areas of interest are governance, ethics, community and leadership.

ANDRÉ TRUDEAU

President and General Manager
Régie des rentes du Québec

Board member since January 1, 2008

André Trudeau has been President and General Manager of the Régie des rentes du Québec since September 24, 2007. He has almost 30 years of experience with the Québec government, holding the positions of President and General Manager, Deputy Minister and Associate General Secretary at about 10 departments and agencies. He is a respected authority in regional planning and development, environment, municipal affairs and transportation. He has also assumed senior responsibilities in health care and social services, manpower training and income security. Mr. Trudeau's versatility and management skills have been the hallmarks of his career and in 2005 earned him the Prix Hommage awarded by the Institut d'administration publique du Québec.

BOARD OF DIRECTORS' REPORT

TABLE 106

DIRECTOR ATTENDANCE AT MEETINGS IN 2008

Director	Board of Directors		Audit Committee		Risk Management Committee		Human Resources Committee		Governance and Ethics Committee
	11 reg.	16 spec.	6 reg.[1]	3 spec.	10 reg.[1]	1 spec.	6 reg.[2]	5 spec.	6 reg.[2]
Yvan Allaire	10	13	–	–	9	1	–	–	6
Christiane Bergevin	9	13/14	6	3	–	–	–	–	–
Pierre Brunet	11	14	–	–	–	–	6	5	4
Claudette Carbonneau	7	12	3	1	–	–	–	–	–
Louise Charette	11	15	–	–	10	1	–	–	–
Steven M. Cummings	10	12	–	–	–	–	6	4	–
Jocelyne Dagenais	11	14	–	–	–	–	–	–	–
Alban D'Amours	8	13	–	–	10	1	–	–	–
Sylvie Dillard	5/7	3/5	–	–	–	–	3/3	4/4	–
Claude Garcia	11	16	6	3	10	1	–	–	–
Richard Guay	4/4	7/7	–	–	–	–	–	–	–
A. Michel Lavigne	11	11	6	3	–	–	–	–	–
Henri Massé	9	12	–	–	10	1	–	–	–
Fernand Perreault	2/2	4/4	–	–	–	–	–	–	–
Henri-Paul Rousseau	5/5	3/3	–	–	6/6	–	–	–	–
Ouma Sananikone	10	10	–	–	–	–	–	–	6
André Trudeau	11	15	–	–	–	–	–	–	–

1 The Audit Committee and the Risk Management Committee held a joint meeting.

2 The Human Resources Committee and the Governance and Ethics Committee held two joint meetings.

TABLE 107

INDEPENDENT BOARD MEMBER REMUNERATION AS DEFINED BY ORDER

Member	Annual remuneration	Remuneration as Committee Chairman	Attendance fees	Total remuneration
Yvan Allaire	$16,564.50	$5,176.50	$24,810.00	$46,551.00
Christiane Bergevin	$16,564.50	–	$18,600.00	$35,164.50
Claudette Carbonneau[1]	$16,564.50	–	$12,795.00	$29,359.50
Louise Charette	$16,564.50	–	$22,500.00	$39,064.50
Steven M. Cummings	$16,564.50	–	$18,622.50	$35,187.00
Alban D'Amours	$16,564.50	$5,176.50	$19,402.50	$41,143.50
Claude Garcia	$16,564.50	$5,176.50	$28,305.00	$50,046.00
A. Michel Lavigne	$16,564.50	–	$18,997.50	$35,562.00
Henri Massé[1]	$16,564.50	–	$19,777.50	$36,342.00
Ouma Sananikone	$16,564.50	–	$16,297.50	$32,862.00

1 The remuneration of these directors is not paid directly to them, in accordance with instructions they have given the Caisse.

BOARD MANDATE

The mandate of the Board of Directors is to ensure that the Caisse is managed in compliance with the provisions of its constituting statute and regulations. It must ensure that the institution takes the necessary steps to attain the objectives stated in its mission, namely to earn an optimal return on depositors' capital in accordance with their investment policies, while contributing to the economic development of Québec.

The Board adopts regulations and approves the Caisse's main guidelines and policies with respect to investment operations, socially responsible investment, risk management oversight and delegation of authority. Any matter that calls for special attention, particularly in light of its intrinsic importance or impact on the Caisse's portfolio or asset allocation, is discussed by the Board.

The Board reviews and approves the Caisse's strategic plan. It approves the institution's annual business plan, and reviews management's evaluations of the economic and financial environment throughout the year. It reviews and approves the Caisse's budgets as well as the annual financial statements and the Annual Report. The Board is required to assess the integrity of internal controls, disclosure controls and information systems, and to approve a financial disclosure policy.

The Board approves human resources policies, pay standards, pay scales and other employment conditions for Caisse officers and employees. It also determines pay standards, pay scales and other employment conditions for the President and Chief Executive Officer, according to parameters established by the government after consultation with the Board. On the recommendation of the President and Chief Executive Officer, the Board appoints the members of senior management.

Working with the Governance and Ethics Committee, the Board develops and oversees implementation of the Caisse's rules, procedures and polices on corporate governance. It approves the codes of ethics and conduct that apply to Caisse Board members and to officers and employees of the Caisse and its subsidiaries. As required by law, the Board of Directors has formed an Audit Committee, a Human Resources Committee, a Governance and Ethics Committee, and a Risk Management Committee.

COMPOSITION OF THE BOARD

The Caisse's Board of Directors consists of 13 members, out of the maximum of 15 allowed. One member, Sylvie Dillard, resigned as a director of the Caisse during the year. A second member, Henri Massé, stepped down as a director early in 2009.

Two members, Jocelyne Dagenais and André Trudeau, joined the Board at the start of 2008.

The Board consists of its Chairman, the President and Chief Executive Officer, depositors' representatives and independent members. The Act respecting the Caisse specifies that at least two-thirds of the Board members, including the Chairman, be independent. Since the President and Chief Executive Officer is an ex-officio member, the changes to the Caisse's senior management in 2008 also affected the composition of the Board of Directors.

DIRECTOR ATTENDANCE AT BOARD AND COMMITTEE MEETINGS

Regular meetings of the Board and its committees are scheduled several months in advance. Special meetings are convened on short notice, as required. The Board has decided that, under certain circumstances, a director's repeated absence from three consecutive regular meetings may constitute a vacancy. This rule does not apply to special meetings.

The members of the Board justify their absences from a meeting of a committee or the Board to the Secretariat of the Caisse.

In 2008, directors were not able to attend certain meeting of the committees or the Board for reasons that include identification of conflicts of interest, a change in the regular meeting schedule requested by the Caisse and health reasons.

INDEPENDENT BOARD MEMBER REMUNERATION

The remuneration of the Caisse's directors is determined by an order-in-council of the Québec government. The order-in-council establishes the following remuneration for directors of the Caisse, with the exception of the Chairman of the Board and the President and Chief Executive Officer, including a 2% increase as at April 1, 2007:

/ Annual remuneration for all independent directors, as defined by the order-in-council: $16,320;

/ Annual remuneration for a committee chairman: $5,100;

/ Attendance fee for each Board or committee meeting: $765; and

/ Attendance fee for each special or brief Board or committee meeting held by conference call: $382.50.

This remuneration was increased by 2% on April 1, 2008. Only directors whose status is independent, as defined by the order-in-council, are entitled to remuneration.

The Board members are also entitled to reimbursement of their travel and living expenses, when applicable.

The total remuneration of the Caisse's directors amounted to $381,282, which can be broken down as shown in table 107.

REMUNERATION OF THE CHAIRMAN OF THE BOARD

The remuneration of the Chairman of the Board is set by the Québec government at $125,000 a year. The Chairman of the Board is also entitled to reimbursement of entertainment expenses related to the duties of the position, to an annual ceiling of $15,000.

BOARD OF DIRECTORS' REPORT

BOARD ACTIVITY REPORT

COMPLIANCE WITH THE ACT RESPECTING THE CAISSE

Throughout the year, the Board ensured that the Caisse's operations complied with the Act and the relevant regulations.

STRATEGIC PLANNING AND BUSINESS PLANS

Each of the Caisse's business units and real estate subsidiaries presented its 2008 business plan to the Board, including objectives, challenges and related risks. The Board adopted the Caisse's business plan, asset allocation program and technology project book for the year. The Board also regularly received senior management's reports on the Caisse's business as well as changes in market conditions.

In June 2008, the Board members took part in the Journées Claude-Prieur, an annual information and discussion forum that brings together all Caisse stakeholders for a strategic look at subjects of concern to the business community. The theme, "New Business Realities," addressed the economic context in the first half of the year, namely the bank credit crisis. The theme of the event was also directly related to preparations for the 2009-2011 strategic planning exercise.

The onset of the global financial crisis in the fall of 2008 and its unusual nature made it necessary to rethink the assumption that the 2009-2011 strategic plan would build on the previous plan, on which planning work already undertaken was based. The Board therefore decided to defer the strategic planning exercise to 2009 to allow Caisse senior management to develop a plan adapted to the new market reality caused by the crisis.

In anticipation of an economic slowdown in Québec in 2009, the Board approved $1.5 billion to be used to support Québec companies during this difficult period, in tandem with the existing financing network. Because the Caisse is aware of the market's inefficiencies and illiquidity, it has decided to play a leading role in co-ordinating its activities with those of its financial partners to meet the financing needs of Québec companies and entrepreneurs. The Board regularly monitors the use of the approved amount.

As part of the reorganization of the Real Estate group, the Board approved the creation of a new subsidiary, Otera Capital. This new organization ensures sound geographic and sector allocation and dynamic asset management for the Real Estate Debt portfolio. The creation of the subsidiary will enable the group to pursue its growth and to act on market opportunities more easily.

Lastly, the Board approved the short-term renewal of the technology outsourcing contract, which is important to the organization's development. The agreement is scheduled to be reviewed in 2009 as part of the strategic planning process.

Despite the turbulence of 2008, the Board was able to oversee the Caisse's operations effectively and to take part constructively in its development. It supported senior management to help the Caisse deal with one of the most serious financial crises ever.

FINANCIAL RESULTS, INTERNAL CONTROL AND MANAGEMENT SYSTEM

The Board received reports analyzing the returns of the Caisse's various business units. It also approved the press release announcing the Caisse's results.

After each Audit Committee meeting, the Board received the Committee's report on its activities, including monitoring of the quarterly financial statements, budgetary monitoring of operating expenses and monitoring of internal audit work. On the Audit Committee's recommendation, the Board approved the Caisse's annual financial statements and budget. It also approved the Annual Report. Through the Audit Committee, the Board also ensured the integrity of all the controls applied to the various data used to establish the financial statements and the notes to the financial statements.

Through the reports of the Audit Committee, the Board monitored the plan for optimal use of resources. In co-operation with the Audit Committee and the Risk Management Committee, the Board reviewed the integrity of internal controls and management systems.

In addition, with the assistance of the Audit Committee, the Board oversaw the application of the policies on financial certification and information disclosure. In line with industry best practices, these policies ensure that the information disclosed by the Caisse is transparent and accurate.

In accordance with these policies, the President and Chief Executive Officer and the Executive Vice-President, Finance and Operations, certify publicly that the disclosure controls and procedures are sufficient and effective, and that the internal controls for financial information are sufficient. The signed certificates can be found in the "Financial certification" section of the Annual Report.

In addition, on the recommendation of the Audit Committee, the Board authorized senior management to issue only one complete certificate, including the evaluation of the effectiveness of internal control for financial information, starting in 2009, as is done in the Canadian banking sector.

Through reports from the Audit Committee, the Board was able to assess the impact on the Caisse of Canada's adoption of international financial information standards starting in 2011. The Board ensured that a plan for implementation of these standards was in progress.

After each Audit Committee meeting, the Board received an oral and written report on its activities. In this way, the Board ensured that the Audit Committee performed its functions adequately.

RISK MANAGEMENT

With assistance from the Risk Management Committee, the Board has identified the main risks to which the Caisse is exposed and ensured oversight of them. In this respect, the Board received an oral and written report on the Committee's activities after each of its meetings.

On the Committee's recommendation, the Board approved the value-added objectives and risk budgets for 2008. A risk limit for contracts or instruments of a financial nature was also approved in line with the overall risk limit defined for the Caisse's overall portfolio. This limit was monitored on a regular basis during the year.

Through the Committee, the Board monitored the integrated risk management policy. It reviewed deviations in respect of the investment policies and authorized them as it saw fit on the Committee's recommendation. The Board also authorized a change to the Caisse's overall active risk limit and considered a presentation from senior management on oversight of active risk and various proposals to improve such oversight.

Every quarter, after the review by the Risk Management Committee, the Board received a report on financial-risk and operational-risk monitoring from the Executive Vice-Presidency responsible for risk management.

Early in 2008, a major fraud affecting the French group Société générale came to light. In response to the events that occurred at that group, Caisse senior management reviewed the organization's internal operational controls. It submitted a report to the Board stating the effectiveness of the Caisse's practices for the areas of risk identified and the improvements undertaken.

The Board approved the main guidelines in the 2008 business plan for the Alpha Global fund of hedge funds, as proposed by senior management. It also endorsed the proposed action plan for an optimal hedge fund management structure.

The Board revised the delegations of authority applicable to certain Caisse operations.

The Board studied investment proposals by the Real Estate and Private Equity groups requiring its authorization and approved them as it saw fit. In each case, the Board considered an analysis of the risks associated with the investment and its impact on the risk level and concentration for the portfolio concerned. The Board did separate and regular monitoring of major investments with a substantial impact on the risk level and concentration of the specialized portfolios. The Board also ensured that a report on investments requiring authorization by Caisse senior management was submitted to the Risk Management Committee.

Caisse Senior management, in agreement with the Board, gave a consulting firm a mandate to review the Caisse's risk management practices and conduct benchmarking of the best practices in this area. The report confirmed the soundness of many of the Caisse's practices and pointed out that certain others were delayed. Through its Risk Management Committee, the Board ensured that measures were taken or continued in an expedited fashion to give effect to the report's recommendations.

Global financial crisis

The Board was quickly informed by senior management of the impact on the Caisse of the global financial crisis that broke out in the fall of 2008. Measures were approved to keep the Caisse's liquid assets at a prudent level and to enable the institution to maintain a sound financial position.

To strengthen the Caisse's organizational structure and risk management procedures, the Board supported senior management's proposal to review not only risk management practices but also the operational model in terms of the impacts of the global financial crisis. The Board therefore asked each group to review its methods in light of the deteriorating market liquidity and the long-term effects of the crisis. The review will lead to an informed and exhaustive strategic planning exercise in 2009 for the Board of Directors.

ABCP

At each regular Board meeting and the six special meetings on this matter, senior management informed the Board of the progress of the negotiations to restructure asset-backed commercial paper (ABCP). When the pace of the negotiations intensified in the fall, the Board created an advisory committee to assist senior management with its review of various aspects of this matter.

For example, the committee reviewed and discussed with Caisse senior management the proposed structure to convert the ABCP into longer-term securities, the negotiations in progress, including those within the Pan-Canadian Investors Committee, and possible strategies for overall management of this matter. On the recommendation of senior management, the Board approved the signature of all the agreements and documents necessary to restructure the ABCP under the Montréal Accord.

On the recommendation of the Audit Committee and the Risk Management Committee, the Board approved the methods for allocating the decrease in the value of the ABCP to the funds. At the end 2008 and the start of 2009, through its Audit Committee, the Board was informed of the downward revision in the value of the ABCP in the combined annual financial statements.

Lastly, the Board discussed with the Risk Management Committee, the Executive Vice-President responsible for risk management and the Chief Risk Officer certain matters pertaining to ABCP.

BOARD OF DIRECTORS' REPORT

PERSONNEL MANAGEMENT AND SENIOR MANAGEMENT SUPERVISION

The Board approved the annual objectives of the Caisse's President and Chief Executive Officer. In addition, at its meetings, senior executives regularly made presentations on their area of activity.

With assistance from the Human Resources Committee, the Board reviewed the performance of the President and Chief Executive Officer for 2007 on the basis of the objectives set at the start of the year. It also reviewed his evaluation of the performance of the senior officers. On a recommendation from the Human Resources Committee, the Board approved the salary conditions for Caisse employees and senior management for 2008 and the bonuses for 2007. With the Committee's assistance, the Board also reviewed the remuneration of the President and Chief Executive Officer in accordance with the parameters set by the Québec government. Lastly, on the recommendation of the Audit Committee, the Board approved the 2008 salary conditions and the 2007 bonus for the Vice-President, Internal Audit.

Throughout the year, the Board received reports from the Committee on the progress of various projects under the program to optimize talent management. On the Committee's recommendation, it approved an update of the human resources management plan to put in place a new system to manage positions and salaries, as well as the updated frame of reference for separation pay. The Board also approved the updated salary scales for 2009, the 2009 human resources budget and the harmonization of the employees' three separate group insurance plans into one plan.

After each meeting of the Human Resources Committee, the Board received an oral and written report summarizing the members' discussions and presenting the Committee's recommendations.

Position of President and Chief Executive Officer
With Henri-Paul Rousseau's resignation as President and Chief Executive Officer, the Board created a special selection committee. The committee was given a mandate to identify a candidate for the position of President and Chief Executive Officer of the Caisse. The Board authorized the special committee to retain the services of an external consulting firm to identify, analyze and recruit candidates.

On the recommendation of the Human Resources Committee, the Board revised and approved the expertise and experience profile for the appointment of the President and Chief Executive Officer.

With the approval of the Québec government, the Board appointed Richard Guay to assume interim management of the Caisse.

The Board received the special selection committee's progress reports. On the committee's recommendation, the Board, with the approval of the Québec government and on the basis of the expertise and experience profile, appointed Richard Guay as President and Chief Executive Officer. In co-operation with the Human Resources Committee, the Board established his remuneration and other employment conditions, according to the parameters set by the government.

Pursuant to the Act respecting the Caisse, when Mr. Guay had to take a leave of absence, the Board appointed Fernand Perreault, Executive Vice-President, Real Estate, to assume management of the organization. He was then appointed President and Chief Executive Officer for a period of six months, with the government's approval.

CORPORATE GOVERNANCE

The Board received an oral and written report describing all the activities of the Governance and Ethics Committee after each of its meetings.

The Board revised and readopted the codes of ethics and professional conduct for directors and employees, as submitted by the Governance and Ethics Committee.

The Board received a detailed report on the Caisse's exercise of its voting rights for those companies in which it exercised such rights. It also received a report on the application of the policy on socially responsible investment for 2007 and 2008.

On the recommendation of the Governance and Ethics Committee, the Board revised and approved, as recommended by the Committee, the composition of the Board's committees as well as the chairmanship of each committee. It also approved additions to the orientation and training program for new directors as well as a clarification to the resolution specifying circumstances in which a director's repeated absence from Board meetings constitutes a vacancy.

The Board received from the Governance and Ethics Committee a report on the declarations of director interests, pursuant to the provisions of the Code of Ethics and Professional Conduct for Directors. On the Committee's recommendation, it approved a procedure to manage conflicts that may arise from directors' appointments to other boards of directors.

The Board received a report from the Committee on the findings of the evaluation of the functioning of the Board of Directors. Proposed improvements to the Board's functioning and opportunities for ongoing training of the directors were also reviewed.

During regular Board meetings, presentations are made to the directors on various aspects of the Caisse's operations. In the past year, these presentations concerned such matters as private equity in Québec, the benchmark indexes for the investment policies of the specialized portfolios, hedge fund management, agreements under the auspices of the International Swaps and Derivatives Association, an update on the Real Estate Debt portfolio, and information technology as a tool for the Caisse's business units. Moreover, as a result of an initiative by the Governance and Ethics Committee, the directors attended a training session on market risk oversight.

During each of these activities, key members of Caisse senior management were available to explain the various subjects, and sufficient time was allowed for a full and complete discussion.

REPORT OF THE AUDIT COMMITTEE

COMMITTEE MANDATE

Under the terms of its mandate, the Audit Committee ensures that the Caisse's financial statements accurately reflect its financial position. To that end, it reviews the financial statements in co-operation with the Auditor General of Québec and recommends them to the Board of Directors for approval.

The Audit Committee ensures that sufficient and effective internal control mechanisms are in place. It also ensures that a risk management process for the Caisse's operations and a plan for optimal use of resources are put in place. It also follows up on the plan.

The Committee reviews any activity that may adversely affect the sound financial position of the Caisse. It is obliged to inform the Board of Directors, in writing, of any management operation or practice that is unsound or that does not comply with the laws, regulations or policies that govern the operations of the Caisse.

Furthermore, the Committee appoints the Vice-President, Internal Audit, and approves the audit plan. It receives internal audit reports on such matters as the application of internal control mechanisms, the risk management process and a plan for optimal use of resources. The Committee also ensures that the organizational structure gives the Internal Audit team the requisite independence in respect of Caisse senior management so that it can carry out its role effectively.

COMPOSITION OF THE COMMITTEE

The Audit Committee consisted of four independent members as at December 31, 2008.

Chairman:	Claude Garcia
Members:	Christiane Bergevin Claudette Carbonneau A. Michel Lavigne In addition, the Chairman of the Board of Directors regularly attends the meetings of the Audit Committee.

The Chairman of the Audit Committee and its members do not sit on any other committee of the Caisse's Board of Directors. The Chairman of the Committee is a guest member at the meetings of the Risk Management Committee.

ACCOUNTING OR FINANCIAL EXPERTISE

All the members of the Audit Committee have the required experience and knowledge to understand the Committee's mandate and to properly fulfill their role.

In their education and careers, they have acquired the abilities and skills to read and understand the Caisse's financial statements. Moreover, the Audit Committee includes members with financial or accounting expertise.

REPORT OF THE AUDIT COMMITTEE

REPORT OF THE AUDIT COMMITTEE ON THE PERFORMANCE OF ITS MANDATE AND THE PLAN FOR OPTIMAL USE OF RESOURCES

The Audit Committee met nine times in 2008. To perform its mandate, the Committee carried out the tasks described below.

FINANCIAL INFORMATION

/ The Committee reviewed the quarterly financial statements and budgetary monitoring of operating expenses.

/ As it does each year, the Committee oversaw an independent valuation of the fair value of the over-the-counter liquid investments, private equity and real estate in which the Caisse invested. In light of the unusual market conditions that developed in 2008, the Committee also oversaw an independent review of data pertaining to the valuations of 10 private equity investments as well as an additional external valuation of three investments; the Committee received a report on the valuation process.

/ The members of the Committee discussed with the Auditor General his audit plan for the Caisse's financial statements.

/ The Committee reviewed the combined annual financial statements with the Auditor General; the members also reviewed such matters as the procedure for preparation of the financial statements, the valuation of over-the-counter liquid investments, illiquid investments and ABCP being restructured, and external audit of returns. The Committee recommended that the Board of Directors approve the combined financial statements.

/ The Committee received the report to senior management issued by the Auditor General after his annual audit.

/ As they do each year, the Committee members met with the Auditor General twice in the absence of members of senior management to discuss various aspects of his mandate and related matters.

/ The Committee reviewed the report on the financial certification process that enables the President and Chief Executive Officer and the Executive Vice-President, Finance and Operations, to certify publicly that the disclosure controls and procedures are sufficient and effective, and that the internal control over financial reporting is sufficient.

/ The Committee reviewed the recommendations of the Canadian Securities Administrators regarding the evaluation of the effectiveness of internal control over financial reporting. It recommended that the Board issue a full certificate starting in 2009, as is done in the Canadian banking sector.

/ The Committee reviewed the summaries of the activities of the Audit Committees of the Caisse's real estate subsidiaries.

/ The Committee considered the impact, on the Caisse and its subsidiaries, of the introduction of joint auditing of the books and accounts of state-owned enterprises. It discussed this matter with the Auditor General and recommended preparatory work to the Board.

/ The Committee analyzed the impact on the Caisse's 2008 financial statements and Annual Report of the adoption of Sections 3862 and 3863 of the *CICA Handbook*.

/ The Committee reviewed the material impacts for the Caisse and its subsidiaries of the adoption by Canada of international accounting standards starting in 2011 and endorsed a project to implement these standards; the Committee members attended a special information session devoted exclusively to IFRS standards.

ABCP

After a discussion with the Auditor General on the method used to allocate the ABCP expense, the Committee recommended that the Board approve it. The Committee received quarterly reports on the fair value of the ABCP. At the end of 2008 and the start of 2009, the Committee reviewed the methodology and parameters used to establish the fair value of the ABCP as at December 31, 2008.

In addition, Committee members were regularly informed of the status of the negotiations on the restructuring of third-party ABCP during the meetings of the Board of Directors.

INTERNAL AUDIT

/ The Committee reviewed the 2008 business plan of the Internal Audit Vice-Presidency, as well as the audit universe and the overall risk assessment of the operations of each Executive Vice-Presidency for the year.

/ The Committee reviewed and adopted the internal audit plan for 2008 and occasionally gave the Vice-President, Internal Audit, specific mandates.

/ The members of the Committee reviewed the links between the internal audit functions at the Caisse and those of its real estate units; they endorsed implementation, starting in 2009, of an internal audit function for all the real estate units, centralized within the Caisse Real Estate group.

/ The Committee reviewed Internal Audit's quarterly reports on such matters as internal control mechanisms, components of the risk management process and optimal use of resources according to the plan in effect.

/ The Committee reviewed Internal Audit's report on the evaluation of the procedures and controls related to the general control environment and evaluation of the general information technology controls.

/ The Committee ensured that Caisse senior management gave effect to the recommendations made by Internal Audit. For example, they discussed with an Executive Vice-President the action plans that he intended to put in place to give effect to the recommendations made by Internal Audit during the previous audit cycle; the Committee ensured that the appropriate action plans were put in place.

- The Committee evaluated performance of the Vice-President, Internal Audit, and recommended the terms of his remuneration to the Board.
- The members of the Committee reviewed the Internal Audit report on various components of fraud risk and endorsed Internal Audit's campaign to make the Caisse's employees aware of fraud risks.
- The Committee ensured the Internal Audit team can act independently of Caisse management.
- The members of the Committee met regularly with the Internal Audit Vice-Presidency after their meetings in the absence of members of management.

INTERNAL CONTROLS AND THE PLAN FOR OPTIMAL USE OF RESOURCES

- The members of the Committee discussed management's overall self-assessment of the effectiveness of the general control environment and oversight of fraud prevention and detection.
- The members of the Committee reviewed the report on the monitoring and measurement activities carried out during the year under the financial and non-financial compliance programs.
- The Committee reviewed the activities carried out in 2007 in respect of the plan for optimal use of resources in 2007-2008 and reviewed the action plan 2008 in respect of the plan; the Committee also monitored the plan during the year.
- Each quarter, the Committee reviewed the reports on compliance with the investment limits specified in the Act respecting the Caisse. The Committee also conducted regular monitoring of the investments made pursuant to the last paragraph of section 37.1 of the Act respecting the Caisse.

RISK MANAGEMENT

The Risk Management Committee was given responsibility for implementation of a risk management process. To that end, the Audit Committee took the following initiatives:

- The Committee received copies of the minutes of the meetings of the Risk Management Committee, as well as the annual reporting document on integrated risk management.
- The Committee also received a copy of the certificates of compliance with the depositors' investment policies and the investment policies of the Caisse's specialized portfolios.
- The Chairman of the Audit Committee sat, as a guest member, on the Risk Management Committee.
- The Audit Committee and the Risk Management Committee held a joint meeting during which the committee members discussed reports by senior management on such matters as internal control, compliance and risk management.
- At the meetings of the Board of Directors, the members of the Audit Committee received the report provided by the Chairman of the Risk Management Committee after each meeting of that Committee.

After each of its meetings, the Committee provided an oral and written report to the Board of Directors on its activities.

In the exercise of their functions, the Board of Directors and its committees may retain the services of external experts. The Audit Committee did not use such services in 2008. It nevertheless supported senior management in its decision to retain a consulting firm to do an independent review of data pertaining to private equity valuation.

This report has been approved by the members of the Audit Committee.

REPORT OF THE HUMAN RESOURCES COMMITTEE

COMMITTEE MANDATE

The mandate of the Human Resources Committee is to review guidelines and strategies for human resources management. The Committee reviews human resources policies, submits them to the Board for approval and ensures they are implemented.

The Committee develops the expertise and experience profile for the appointment of the President and Chief Executive Officer and submits it to the Board for approval. Using this profile, the Committee reviews potential candidates, as necessary, recommends the appointment of the President and Chief Executive Officer to the Board and evaluates his performance.

On the recommendation of the President and Chief Executive Officer, the Committee reviews the appointment and remuneration of the Caisse's senior officers, and submits this information to the Board for approval. The Committee also reviews the responsibilities of the members of senior management and ensures that succession-planning mechanisms are in place. It reviews the performance evaluation for senior officers, which is done by the President and Chief Executive Officer.

With respect to remuneration, the Committee receives information each year concerning the Caisse's reference market. It reviews and submits to the Board a recommendation to establish the remuneration and other employment conditions of the President and Chief Executive Officer, within the parameters determined by the government after consultation with the Board. The Committee also reviews and submits to the Board the appropriate recommendations to establish the remuneration and other employment conditions of the Caisse's other officers and employees.

Finally, in co-operation with the Governance and Ethics Committee, the Committee develops expertise and experience profiles for the appointment of independent Board members and submits the profiles to the Board for approval.

COMPOSITION OF THE COMMITTEE

The Human Resources Committee consisted of two independent members as at December 31, 2008.

Chairman:	Pierre Brunet
Member:	Steven M. Cummings

Sylvie Dillard resigned as a member of the Board of Directors of the Caisse in 2008 and therefore as a member of the Human Resources Committee. Starting in November 2008, the Chairman of the Human Resources Committee asked the members of the Governance and Ethics Committee to hold joint meetings until the vacant positions on the Board were filled. Early in 2009, the Board therefore decided to appoint the members of the Human Resources Committee to the Governance and Ethics Committee, and vice-versa.

HUMAN RESOURCES COMMITTEE ACTIVITY REPORT

The Human Resources Committee met 11 times in 2008. In performing its mandate, the Committee carried out the activities described below. The Committee members have approved this report.

/ The Committee reviewed the salary conditions of the Caisse's employees for 2008 and submitted them to the Board of Directors for approval. It carried out the same procedure to determine employee bonuses for the previous year.

/ The Committee evaluated the performance of the President and Chief Executive Officer for 2007. It also reviewed the evaluations of the members of senior management, which were done by the President and Chief Executive Officer. On the basis of its review, the Committee recommended that the Board approve the 2008 salary increases, the 2007 bonuses and the other employment conditions for each member of senior management.

/ The Committee recommended to the Board, for approval, the 2008 remuneration, the 2007 bonus and the other employment conditions of the President and Chief Executive Officer, according to the parameters determined by the government.

/ The Committee reviewed the 2008 annual objectives of the President and Chief Executive Officer and submitted them to the Board of Directors for approval.

- During the year, the Committee regularly received reports on implementation and development of various projects under the talent management optimization program. It also monitored implementation of the overall program.
- The members discussed a succession management program for the President and Chief Executive Officer and the members of the Executive Committee.
- The Committee revised the expertise and experience profile for the independent members of the Board of Directors.
- The Committee reviewed the expertise and experience profile for the President and Chief Executive Officer and submitted it to the Board for approval.
- The Committee submitted to the Board of Directors for approval the remuneration and other employment conditions of the new President and Chief Executive Officer according to the parameters determined by the government.
- The Committee reviewed and approved or, as the case may be, recommended that the Board approve, the hiring and the salary conditions for employees holding the position of Vice-President or a higher position; it also confirmed that certain employees were eligible for the long-term incentive plan.
- The Committee reviewed and recommended to the Board an updated version of the human resources management policy to introduce a new system to manage jobs and salaries; the Committee also proposed an updated version of the frame of reference for severance pay.
- The Committee submitted to the Board for approval an updated version of the salary scales for the 2009 salary reviews as well as the 2009 human resources budget.
- The Committee analyzed the Caisse's ability to retain its best employees and to attract new resources.
- The Committee reviewed and submitted to the Board for approval a new group insurance plan to combine the Caisse's three separate plans into one.

After each of its meetings, the Committee reported on its activities to the Board of Directors, orally and in writing.

In the exercise of their functions, the Board of Directors and its committees may employ the services of external experts. The Caisse used the services of a professional firm for the recruitment of a new President and Chief Executive Officer.

REPORT OF THE HUMAN RESOURCES COMMITTEE ON OFFICER REMUNERATION

The Caisse is a financial institution whose performance depends essentially on the talent of its employees. Its officers are responsible for putting in place and carrying out business plans in line with the Caisse's mission, which is "to receive moneys on deposit as provided by law and manage them with a view to achieving optimal return on capital within the framework of depositors' investment policies while at the same time contributing to Québec's economic development."

The Caisse must rely on highly competent employees, whom it recruits on markets with occupations similar to its own. To attract such people, it must adopt a remuneration policy aligned with that of its reference market. Such a policy is vital if the Caisse is to attract, to retain and to motivate employees whose talent will enable it to achieve its business objectives in an environment where competition for talent is intense.

Long perceived as Québec's investment school, the Caisse has often lost talented employees recruited by other Canadian and foreign investment firms that can offer more advantageous compensation conditions than those in effect at the Caisse. To contain this trend, the Caisse has had to define programs enabling it to offer total remuneration that is competitive in its reference market, while respecting the remuneration parameters included in its *Regulation respecting internal management*.

According to these parameters, the remuneration and other employment conditions of the President and Chief Executive Officer must fall between the median and the 75th centile of the reference market, depending on whether the Caisse's performance is average or superior. The reference market is that of large Canadian pension funds.

The parameters also specify that the maximum level of total remuneration for investment positions must fall within the upper decile (90th centile) of the reference market. The total remuneration for other positions must be at the third quartile (75th centile) of the reference market.

REPORT OF THE HUMAN RESOURCES COMMITTEE

In light of these parameters, the Caisse's approach is generally, apart from certain exceptional cases, to offer remuneration near the median of the reference market when the Caisse's performance is average, and 75th-centile remuneration when its performance is superior.

The reference market for investment positions is defined as the Canadian institutional investment market and includes a representative sample of institutions, insurance companies, trust companies, pension funds, investment advisers, brokerage firms and fund managers or managers in similar industries. Reference may be made to the North American market for positions related to international investment. The reference market for non-investment positions is Québec, and includes the public sector.

To ensure that its remuneration programs are competitive and respect the parameters of the *Regulation respecting internal management*, the Caisse asks recognized firms to advise it on the analysis of its remuneration programs. An analysis is done regularly for many positions in a data bank covering the reference market. The results are used to compare the total remuneration offered at the Caisse for each matching position. The latest market analysis, completed early in 2009, shows that the total remuneration offered to the Caisse's officers in 2008 is within the parameters of the *Regulation respecting internal management* and the policy followed by the Caisse.

Under the *Act respecting the Caisse de dépôt et placement du Québec*, the Caisse must disclose the remuneration of the President and Chief Executive Officer and that of the five most highly remunerated officers reporting directly to him. The same disclosure is also required for wholly owned subsidiaries. CDP U.S. Inc. is a wholly owned subsidiary of the Caisse, and its President and Chief Executive Officer and officers are the same as those of the Caisse.

OFFICERS' TOTAL REMUNERATION

Total remuneration is comprised of all aspects of an officer's remuneration and includes base salary, annual bonus, long-term incentive plan, benefits programs, pension plans and other remuneration.

Base salary
An officer's base salary is aligned with the reference market. It is determined on the basis of the level of responsibility related to the position as well as the officer's experience, expertise and performance.

Variable remuneration
The variable-remuneration programs in effect at the Caisse, described hereunder, are based on Canadian practices in this area. The annual bonus program and the long-term incentive program represent a large portion of officers' total remuneration. To align officers' interests with depositors' expectations, the Caisse gives considerable weight to officers' long-term variable remuneration.

Annual bonus program
At the start of each fiscal year, the Board of Directors sets the annual objectives of the President and Chief Executive Officer. The Board also approves the annual objectives of the other officers, on the recommendation of the President and Chief Executive Officer. These objectives cover such matters as budgets, business plans and value-added performance objectives for each specialized portfolio in relation to predetermined thresholds. At the end of the year, as a function of the results obtained, the Board approves the annual bonus for each officer of the Caisse.

The amount of the bonus depends on the degree to which the President and Chief Executive Officer achieves the annual objectives and the Caisse's performance. In the case of the other officers, the amount of the bonus depends on the performance of the Caisse, the performance of the investment groups, the positioning of the Caisse in relation to its peers and the individual performance of each officer.

The performance is based on achievement of value-added objectives over and above predetermined thresholds, aligned with depositors' expectations. The Caisse's performance and that of the specialized portfolios is measured over a moving three-year period (five years for the Private Equity and Real Estate portfolios) to evaluate the results on a medium-term horizon.

No annual bonuses were paid in 2008 as a result of the Caisse's performance.

Long-term incentive plan
The long-term incentive plan (LTIP) represents a large portion of officers' remuneration and aligns their total remuneration with the Caisse's long-term value-added objectives. The performance is based on achievement of value-added objectives over and above a benchmark index, aligned with depositors' expectations. The Caisse's performance is measured on a moving five-year period so as to evaluate the results on a horizon that corresponds to a long-term investment philosophy.

In the case of the Executive Vice-President, Real Estate, the performance used is that of the Real Estate group, as a result of his many years of service with the group's subsidiaries before he joined Caisse senior management.

Under the LTIP, each officer receives an annual grant corresponding to a percentage of his base salary. A reserve is thereby created and it varies according to the Caisse's performance during a moving five-year period. The right to payment under the LTIP is vested gradually and, on certain conditions, starting from the end of the third year of the first cycle. The officer may receive, on vesting and depending on the Caisse's performance, a basic payment corresponding to a percentage of the reserve accumulated as at December 31 of each year. The distribution percentage ranges from 0% to 40% of the reserve and is based on the Caisse's performance throughout the cycle measured. The Board of Directors may decide to increase the distribution percentage to recognize long-term performance and thus grant an additional payment under the LTIP. In this case, it ensures that the officer's overall remuneration remains within the parameters specified in the *Regulation respecting internal management*.

The officers eligible for the long-term incentive plan in effect before the current plan was introduced in 2004 were given, in addition to the regular annual grant, an additional grant to take into account their waiver of the benefits they had been given under the previous plan. This additional grant has been included with the regular annual grants and is treated in the same way as the regular grants.

No bonuses were paid under the long-term incentive plan in 2008 as a result of the Caisse's performance.

Other compensation
Other compensation refers to perquisites (a car and the related operating expenses, parking, health care and professional consulting fees), the Caisse's contribution to the group insurance plan in effect for management and any other amount paid to an officer under a special agreement.

Pension plans
The Caisse's pension plan for officers has two separate components, namely the Basic Plan and the Supplemental Pension Plan for Designated Officers (SPPDO). The benefits under the supplemental plans vary according to the annual pension ceilings imposed on the basic plan by the Canada Revenue Agency.

Under the two plans, as President and Chief Executive Officer, Henri-Paul Rousseau is entitled to receive, at the normal retirement age, a total annual pension equal to $35,000 plus an amount corresponding to the number of years or fraction of a year of his membership in the pension plans multiplied by 8% of his eligible earnings. The maximum pension payable under the two plans may not exceed 60% of his eligible earnings.

Under the two plans, as President and Chief Executive Officer, Richard Guay is entitled to receive, at the normal retirement age, a total annual pension equal to an amount corresponding to the number of years or fraction of a year of his membership in the plans multiplied by 2% of his eligible earnings for each year or fraction of a year of membership before September 5, 2008, and by 4% for his eligible earnings for each year or fraction of a year of subsequent membership.

The provisions of the SPPDO in respect of Suzanne Masson differ from those of the other officers to take into account the fact that her basic pension plan is the Retirement Plan for Senior Officials (RPSO).

Under the two plans, the other officers are entitled to receive, at the normal retirement age, a total annual pension corresponding to 2% of their eligible earnings for each year or fraction of a year of membership, according to the annual ceilings imposed on the basic plan by the Canada Revenue Agency for each year when they were not members of the SPPDO.

The Board of Directors has abolished the Supplemental Pension Plan for Employees (SPPE), and no benefits will be payable under this plan.

REPORT OF THE HUMAN RESOURCES COMMITTEE

TABLE 108

SUMMARY OF OFFICERS' REMUNERATION FOR 2006, 2007 AND 2008

Name and position	Year	Salary ($)	Remuneration under an incentive plan that is not equity-based ($)		Value of pension plan ($)	Other remuneration[7] ($)	Total remuneration ($)
			Annual incentive plan	Long-term incentive plan			
Henri-Paul Rousseau	2008	339,904	–	–	358,200	405,673[2]	1,103,777
President and Chief	2007	490,000	125,000	1,131,950	579,600	40,000	2,366,550
Executive Officer[1]	2006	473,800	142,140	1,213,850	563,400	40,000	2,433,190
Richard Guay	2008	407,692	–	–	282,500	33,077	723,269
President and Chief	2007	375,000	450,000	187,950	173,800	30,000	1,216,750
Executive Officer[1, 3, 4]	2006	310,500	581,750	159,720	151,000	28,750	1,231,720
Fernand Perreault	2008	430,000	–	–	414,700	30,000	874,700
Executive Vice-President,	2007	395,000	650,000	496,820	73,700	30,000	1,645,520
Real Estate[5, 6]	2006	385,000	685,300	538,620	73,000	30,000	1,711,920
Normand Provost	2008	325,000	–	–	108,200	25,000	458,200
Executive Vice-President,	2007	315,000	475,000	208,640	112,300	25,000	1,135,940
Private Equity	2006	300,000	525,000	197,250	123,300	25,000	1,170,550
Ghislain Parent	2008	310,000	–	–	81,400	25,000	416,400
Executive Vice-President,	2007	272,000	320,000	90,690	92,100	25,000	799,790
Finance and Operations	2006	265,000	210,000	81,450	92,300	25,000	673,750
Suzanne Masson	2008	270,000	–	–	47,700	25,000	342,700
Executive Vice-President, Corporate Affairs,	2007	257,500	204,500	59,920	49,600	25,000	596,520
and Secretary	2006	252,500	200,000	40,500	58,100	25,000	576,100
Susan Kudzman	2008	270,000	–	–	70,500	25,000	365,500
Executive Vice-President,	2007	247,200	150,000	32,040	80,300	25,000	534,540
Depositors and Risks	2006	240,000	185,000	–	79,000	23,750	527,750

1 After the departure of Henri-Paul Rousseau, Richard Guay was appointed President and Chief Executive Officer on September 5, 2008.

2 Includes a separation allowance of $378,750 representing nine months of salary.

3 The value of Mr. Guay's pension plan for 2008 takes into account the reduction of his annual salary of $425,000 as President and Chief Executive Officer to $325,000 as Strategic Adviser to the President and Chief Executive Officer. This value also includes the pension plan enhancement provided to Mr. Guay when he was appointed President and Chief Executive Officer and maintained in his contract as Strategic Adviser to the President and Chief Executive Officer. The enhancement consists of a pension credit increased to 4% for each year of service, from September 5, 2008.

4 After his resignation, Mr. Guay was appointed Strategic Adviser to the President and Chief Executive Officer, from January 8, 2009.

5 Fernand Perreault held the position of Acting President and Chief Executive Officer from November 13, 2008, to January 7, 2009. He was appointed President and Chief Executive Officer from January 8, 2009, for six months.

6 The increase in the value of Mr. Perreault's pension plan in 2008 is due mainly to his continued membership in the Supplemental Pension Plan after the age of 65 and the increase in his pension by the amount of $20,000 a year.

7 Includes the amount of perquisites and separation allowances.

TABLE 109

SUMMARY OF OFFICERS' PENSIONS

Name and position	Years of credited service[1]	Annual benefits payable ($)		Benefits payable at start of year[2] ($)	Variation attributable to compensation elements[2] ($)	Variation attributable to non-compensation elements[2] ($)	Benefits payable at year-end[2] ($)
		At year-end	At age 65				
Henri-Paul Rousseau President and Chief Executive Officer	6.0	267,700	267,700	3,377,900	358,200	(451,000)	3,285,100
Richard Guay President and Chief Executive Officer	22.0	141,000	290,900	1,339,200	282,500	(767,800)	853,900
Fernand Perreault Executive Vice-President, Real Estate	21.2	196,500	196,500	1,587,300	414,700	(375,800)	1,626,200
Normand Provost Executive Vice-President, Private Equity	28.6	151,900	228,300	893,800	108,200	(436,300)	565,700
Ghislain Parent Executive Vice-President, Finance and Operations	6.1	34,200	159,500	425,800	81,400	(216,800)	290,400
Suzanne Masson Executive Vice-President, Corporate Affairs, and Secretary	28.3	141,200	170,900	455,100	47,700	(255,300)	247,500
Susan Kudzman Executive Vice-President, Depositors and Risks	3.3	15,200	116,500	175,900	70,500	(120,500)	125,900

1 Number of years of credited service in the basic plan. The number of years of credited service in a supplemental plan is equal to or less than the number of years in the basic plan.

2 The obligations do not include those of the basic plan, because a contribution is paid to CARRA, which assumes the obligation thereof. The contribution was about $12,300 in 2008.

REPORT OF THE HUMAN RESOURCES COMMITTEE

TABLE 110

SUMMARY OF OFFICERS' SEPARATION ALLOWANCES

Name and position	Precipitating event	Cash payment ($)	Other benefits ($)	Total ($)
Henri-Paul Rousseau President and Chief Executive Officer	End of employment	378,750[1]	–	378,750
Richard Guay President and Chief Executive Officer	End of employment	425,000[2]	–	425,000
Fernand Perreault Executive Vice-President, Real Estate[3]	Involuntary departure	438,578	1,000	439,578
Normand Provost Executive Vice-President, Private Equity[3]	Involuntary departure	386,314	1,000	387,314
Ghislain Parent Executive Vice-President, Finance and Operations[4]	Involuntary departure	614,000	1,000	615,000
Suzanne Masson Executive Vice-President, Corporate Affairs, and Secretary[4]	Involuntary departure	538,000	1,000	539,000
Susan Kudzman Executive Vice-President, Depositors and Risks[4]	Involuntary departure	538,000	1,000	539,000

1 Separation allowance representing nine months of salary.

2 Richard Guay's separation allowance of $425,000 was provided in his working conditions as President and Chief Executive Officer. As a result of his appointment as Strategic Adviser, Mr. Guay may receive a separation allowance corresponding to one month of total remuneration for each year of service, in the event of dismissal without just or sufficient cause or non-renewal of his contract.

3 Fernand Perreault and Normand Provost have no specific conditions related to their end of employment. Their separation allowance has therefore been calculated on the basis of the Caisse's separation allowance program, which provides one month of base salary for each year of service to a maximum of 15 months, taking into account service and age.

4 The employment contracts of these officers provide for a separation allowance in the event of dismissal without just or sufficient cause in an amount equal to their annual remuneration.

Analysis of the reference market for officers

The analysis of the reference market for the position of President and Chief Executive Officer is based on a comparison group of eight large Canadian pension funds. The analysis of the reference market for the other officers is based on a comparison group of about 60 businesses that are part of the reference markets referred to in the Caisse's *Regulation respecting internal management*.

The Caisse's *Regulation respecting internal management* requires that data reflecting the portrait of the reference market be compiled by means of a survey done by a recognized firm, and that they be administered and analyzed according to a methodology and rules generally recognized in this field.

To establish the comparison of the remuneration for each officer with that of the reference market, Towers Perrin uses a recognized and reliable analytical method that ensures all the components of this remuneration are considered on a comparable basis.

Table 111 compares the potential direct remuneration of each officer for 2008 with that observed in the reference market for a superior performance. It presents, on a comparable basis, the total remuneration paid at the 75th centile of the reference market and the total remuneration payable at the Caisse under the various remuneration programs in effect.

TABLE 111

COMPARISON OF EACH OFFICER'S POTENTIAL TOTAL REMUNERATION FOR 2008 WITH THAT OBSERVED IN THE REFERENCE MARKET FOR A SUPERIOR PERFORMANCE

Position	Reference market at 75th centile ($)	Caisse policy for a superior performance ($)	Ratio
	(A)	(B)	(B)/(A)
President and Chief Executive Officer[1]	3,240,000	1,995,000	0.62
Executive Vice-President, Real Estate[2]	2,266,000	1,755,000	0.77
Executive Vice-President, Private Equity[2]	1,753,000	1,329,000	0.76
Executive Vice-President, Finance and Operations[2]	1,078,000	897,000	0.83
Executive Vice-President, Corporate Affairs, and Secretary[2]	1,042,000	784,000	0.75
Executive Vice-President, Depositors and Risks[2]	1,127,000	784,000	0.70

1 Towers Perrin, Study of the Remuneration of the President and Chief Executive Officer, Caisse de dépôt et placement du Québec, 2009.

2 Towers Perrin, Study of the Remuneration of the Executive Committee, Caisse de dépôt et placement du Québec, 2009.

REPORT OF THE GOVERNANCE AND ETHICS COMMITTEE

COMMITTEE MANDATE

The Governance and Ethics Committee assists the Board of Directors with the development and implementation of principles and practices that are conducive to a sound governance culture at the Caisse. To that end, the Committee establishes rules, structures and procedures to ensure the Board of Directors acts independently from management.

The Committee must propose an orientation program for new directors and an ongoing training program. In this way, it ensures that the directors have the knowledge they require to contribute actively to the work of the Board and its committees. It makes recommendations to the Board regarding the composition and mandates of the Board's committees, as well as the composition and mandates of other committees that can facilitate the proper functioning of the Caisse. The Committee also proposes a procedure for evaluating the performance of the directors and the Board as a whole.

Together with the Human Resources Committee, the Governance and Ethics Committee submits to the Board the expertise and experience profile for the selection of independent members. It also proposes such candidates to the Québec government on the basis of the criteria established by law.

Finally, the Committee reviews regulations, codes and policies respecting the following matters and recommends them to the Board:

/ The ethics and professional conduct of the directors, officers and employees of the Caisse, including control measures pertaining to the personal use of information received with respect to Caisse operations, and instances in which officers of the Caisse are obliged to declare their interests;

/ Socially responsible investment; and

/ The governance principles that the Caisse intends to promote to the companies in which it exercises voting rights.

COMPOSITION OF THE COMMITTEE

The Governance and Ethics Committee consisted of three independent members as at December 31, 2008.

Chairman:	Yvan Allaire
Members:	Pierre Brunet Ouma Sananikone

Starting with the meeting of November 2008, the Chairman of the Human Resources Committee asked the members of the Governance and Ethics Committee to hold joint meetings, until the vacant positions on the Board were filled. Early in 2009, the Board therefore decided to appoint the members of the Governance and Ethics Committee to the Human Resources Committee, and vice-versa.

ACTIVITY REPORT OF THE GOVERNANCE AND ETHICS COMMITTEE

The Committee met six times in 2008. To fulfill its mandate, the Committee focused mainly on the governance matters described below.

RULES OF ETHICS AND PROFESSIONAL CONDUCT

/ The Committee revised the codes of ethics and professional conduct for directors, officers and employees of the Caisse, and submitted the codes to the Board of Directors for approval.

/ The Committee received a report on the application of the code of ethics and professional conduct for officers and employees.

/ On behalf of the Board of Directors, the Committee reviewed the directors' declarations of interest pursuant to the provisions of their code of ethics and professional conduct; it also forwarded the declarations to the competent authorities, as stipulated in the Act respecting the Caisse.

GOVERNANCE PRINCIPLES FOR THE EXERCISE OF VOTING RIGHTS

/ The Committee received a report on the exercise of the Caisse's voting rights for those companies in which it exercised such rights and discussed the principles governing such exercise in respect of various types of transactions carried out by the Caisse.

/ The Committee discussed the application of the policy on socially responsible investment in 2007 and 2008. More specifically, it discussed the Caisse's position on certain matters and recommended the position to the Board.

COMPOSITION OF THE COMMITTEES AND THE BOARD

/ The Committee reviewed the expertise and experience profile for independent Board members.

/ As part of the process to identify candidates for the position of director, the Committee considered the composition of the Board of Directors, the duration of the directors' mandates and the complementary competencies and expertise desired.

/ The Committee revised the composition of the Board's committees and the chairmanship of each committee, and submitted its recommendations to the Board of Directors.

FUNCTIONING OF THE COMMITTEES AND THE BOARD

/ The Committee supervised the performance evaluation of the Board, its Chairman and its committees. The Committee reported the results of this process to the Board of Directors. Using the results of these evaluations, the Committee determined the improvements required to the Board's functioning, as well as opportunities for ongoing training of the directors.

/ The Committee ensured that the directors carried out a self-evaluation, co-ordinated by the Chairman of the Board.

/ The Committee proposed additions to the orientation and training program for new directors.

/ The Committee reviewed the procedure for appointing members of the boards of directors of private companies in which the Caisse invests.

/ The Committee proposed a procedure to manage potential conflicts that may arise from the directors' appointment to other boards of directors.

/ The Committee proposed to the Board a clarification of the resolution setting forth the conditions in which a director's repeated absence from Board meetings constitutes a vacancy.

/ The Chairman of the Committee reported to the Board of Directors on the Committee's work after each of its meetings, orally and in writing.

/ The Committee proposed discussion sessions over the course of the year in the absence of senior management and ensured that the time allocated for these matters allowed for a full and complete discussion by the directors.

/ The Committee ensured that key members of Caisse senior management or external consultants were available to address the various subjects on the agenda of the Board's meetings, and that the time allocated for these matters allowed for a full and complete discussion.

/ The Committee ensured that the Board had all the relevant information and the time necessary to analyze the issues that the Caisse faces.

In the exercise of their functions, the Board of Directors and its committees may retain the services of external experts. The Governance and Ethics Committee did not use such services in 2008.

The Committee members have approved this report.

REPORT OF THE RISK MANAGEMENT COMMITTEE

The Board of Directors created the Risk Management Committee to assist the Audit Committee with its responsibility to put in place a risk management process.

COMMITTEE MANDATE

By establishing guidelines and policies for risk management and recommending them to the Board of Directors, the Committee seeks to maintain an appropriate level of business, financial and operational risks. In carrying out its mandate, the Committee ensures that risks are clearly identified, and that a process is in place to manage them.

The Committee also reviews and submits to the Board for approval, under the integrated risk management policy, any investment matter and any deviation from the investment policies.

In addition, it ensures that the Caisse fulfills its obligations to its depositors. To that end, it monitors compliance with the investment policy of each specialized portfolio and with each depositor's investment policy, and makes any necessary recommendations to the Board.

The Committee has various mechanisms to provide the Audit Committee with assurance regarding the implementation of a risk management process. These mechanisms are described below.

COMPOSITION OF THE COMMITTEE

The Risk Management Committee consisted of four members as at December 31, 2008.

Chairman:	Alban D'Amours
Members:	Yvan Allaire Louise Charette Henri Massé
Guest member:	Claude Garcia, Chairman of the Audit Committee The Chairman of the Board also regularly attends the Committee's meetings.

ACTIVITY REPORT OF THE RISK MANAGEMENT COMMITTEE

The Risk Management Committee held 11 meetings during the year. Its main achievements for 2008 are described below.

RESPONSIBILITIES FOR ESTABLISHMENT OF RISK MANAGEMENT GUIDELINES AND POLICIES

/ The Committee reviewed compliance with the investment policies of the Caisse's specialized portfolios and, as applicable, submitted any deviations to the Board of Directors for approval.

/ The Committee recommended to the Board of Directors a risk limit for contracts or instruments of a financial nature in accordance with the requirements of the *Regulation respecting the determination of instruments or contracts of a financial nature and the framework for their use*; it regularly received reports on compliance with this limit.

/ The Committee reviewed and recommended to the Board of Directors the value-added objectives and the risk budgets for 2008.

/ The Committee reviewed and recommended to the Board of Directors for approval a deviation to the Caisse's overall active risk limit. It also reviewed monitoring of active risk and various proposals for improving it.

/ The Committee reviewed the report on the Caisse's integrated risk management, which presents the structures put in place at the Caisse to monitor risk. The Committee also received reports on compliance and internal control.

/ The Committee analyzed the quarterly reports and the annual report on monitoring of changes in the Caisse's financial risks.

/ The Committee received a quarterly report on the operational risks related to management of processes and systems, legal affairs and human resources.

/ The Committee received a report on the risk management and monitoring directives put in place by Caisse senior management.

/ The Committee reviewed and recommended to the Board for approval the redefinition of the offering limits for the short- and medium-term financing programs of CDP Financial Inc.

/ The Committee reviewed the process that is used to manage and monitor the portfolio managers' mandates.

/ The Committee reviewed certain matters pertaining to ABCP.

/ At the end of 2007, the Committee reviewed the mandate given to an external consulting firm to revise the Caisse's risk management practices and to benchmark the best practices in this area. The Committee held a private meeting during the year with representatives of the firm. The Committee then received and discussed with them their report on the adequacy of several of the Caisse's practices and the delays affecting certain others.

/ The Committee discussed with the Executive Vice-President responsible for risk management, the Chief Risk Officer and the President and Chief Executive Officer the measures taken to give effect to the revision of risk management practices. It developed a five-part work plan, which includes: 1) enhancement of the risk management culture; 2) management of unforeseeable risk; 3) approval process for new operations; 4) resources required for the plan; and 5) various elements to strengthen risk measurement and methodologies.

/ The Committee also discussed with the Executive Vice-President responsible for risk management and the Chief Risk Officer adaptation of the process used to manage substantial risks in the new market conditions resulting from the global financial crisis that broke out in the fall of 2008.

INVESTMENT FILES

/ The Committee reviewed 15 investment files under the authority of the Board of Directors and, as it saw fit, submitted them to the Board for approval. For each file, in addition to the analysis submitted by the unit proposing the transaction, the Committee reviewed the analysis of the project's risks, particularly its impact on the degree and concentration of risk for the specialized portfolio and the Caisse's overall portfolio. The Committee also reviewed the investment's compliance with the risk management policies and directives.

/ The Committee also discussed the analysis of the risk-return ratio for each investment file submitted to it.

/ The Committee received the monitoring report on investment files that do not require Board approval and were authorized by Caisse senior management.

/ The Committee reviewed the risks associated with certain new products and received a report on the Caisse's exposure to certain sectors of activity.

/ The Committee received monitoring reports on investment files analyzed by the managers of the Private Equity and Real Estate groups.

/ The Committee regularly monitored certain major investments with a significant impact on the risk level and concentration of the specialized portfolios and the Caisse's overall portfolio.

REPORT OF THE RISK MANAGEMENT COMMITTEE

DEPOSITORS

/ The Committee reviewed the certificates of compliance with the depositors' investment policies and the investment policies of the specialized portfolios; it also discussed the depositors' expectations with respect to the establishment and monitoring of the policies.

/ The Committee discussed the establishment of benchmark indexes for the investment policies of the specialized portfolios.

/ The Committee revised the method for allocating the decrease in ABCP value to the funds and recommended that the Board approve it.

/ Through the Executive Vice-President responsible for relations with the depositors, the Committee ensured that they were satisfied with the Caisse's reporting.

After each of its meetings, the Committee reported orally and in writing to the Board of Directors on its activities.

It also submitted copies of its minutes to the Audit Committee and the Board of Directors. The Audit Committee and the Risk Management Committee held a joint meeting during which their members discussed senior management's reports on such matters as internal control, compliance and risk management.

In the exercise of their functions, the Board of Directors and its committees may retain the services of external experts. The Risk Management Committee did not use such services in 2008. It nevertheless supported senior management in its decision to retain a consulting firm for a review of the Caisse's risk management practices as well as benchmarking of best practices in this area.

This report has been approved by the Committee members.

GENERAL NOTES

1 / The Caisse's operations comply with the requirements of the *Act respecting the Caisse de dépôt et placement du Québec*[1] and with investment industry practices. Its financial statements are prepared in accordance with generally accepted accounting principles in Canada. Each year, the Auditor General of Québec conducts the financial audit.

2 / The Annual Report 2008 – Additional Information is an integral part of the Annual Report 2008 and presents the Schedules (tables of returns) as at December 31, 2008, relating to the composites of the Caisse depositors' accounts. The Schedules and calculations have been audited as at December 31, 2008, by Deloitte & Touche LLP for compliance with the Global Investment Performance Standards (GIPS®).

3 / The returns on the specialized portfolios represent the time-weighted rate of return.

4 / The benchmark indexes for the asset classes are the weighted average of the benchmark indexes of the specialized portfolios.

5 / Unless otherwise stated, returns are presented before operating expenses and external management fees. They include the return on cash and cash equivalents, and they take into account a foreign exchange hedging position. The return spreads related to the operating expenses of each specialized portfolio are presented in the Schedules of the Annual Report 2008 – Additional Information.

6 / Certain returns are expressed in basis points (b.p.). One hundred basis points equal 1.0% and one basis point equals 0.01%.

7 / Unless otherwise stated, all figures are given in Canadian dollars. The letters M and B used with dollar amounts designate millions and billions, respectively.

8 / Totals (figures or percentages) may vary because of rounding of figures.

9 / Many of the financial terms used in this Annual Report are defined in the glossary on the website at www.lacaisse.com.

10 / Unless otherwise stated, all data in the tables and figures are from studies made by the Caisse.

11 / The tables listing the top 10 investments present, in alphabetical order, the main cash positions based partially on information shown in tables 9, 10, 11 and 12 of the Annual Report 2008 – Additional Information, net of short selling.

1 The *Act respecting the Caisse de dépôt et placement du Québec* is available on line at www.lacaisse.com.

GENERAL NOTES

TABLE 112

CHANGES IN SPECIALIZED PORTFOLIO INDEXES OVER FIVE YEARS

(as at December 31, 2008)

Specialized portfolio	1 year	3 years	5 years
Short Term Investments (created July 1, 1998)	DEX 91-Day Canadian T-Bill		
Real Return Bonds (created January 1, 2004)	DEX Real Return Bond		
Bonds (created October 1, 1996)	DEX Universe Bond		
Long Term Bonds (created April 1, 2005)	DEX Long Term Government Bond		Portfolio not yet created
Canadian Equity (created July 1, 1995)	S&P/TSX capped		
U.S. Equity (created April 1, 1994)	S&P 500 hedged		
Foreign Equity (created April 1, 1989)	MSCI – EAFE hedged		
Emerging Markets Equity (created January 1, 1995)	MSCI – EM unhedged		
Québec International (created July 1, 1999)	Index consists of 80% DEX Provincial Québec Subindex contracts and 20% DEX 91-Day Canadian T-Bill, plus a basket of equity futures		
Hedge Funds (created April 1, 2003)	CS/Tremont Hedge Fund Index (modified) since July 1, 2007, SC 91-Day Canadian T-Bill from January 1, 2006, to June 30, 2007, S&P Hedge Fund Index previously		
Commodities (created August 1, 2004)	Index based 80% on the Barclays U.S. Government Inflation-Linked Bond 1-10 Year Total Return Index and 20% on the Merrill Lynch 3-month U.S. Treasury Bill, plus the unhedged Dow Jones-AIG Commodity Excess Return Index		Portfolio not yet created
Investments and Infrastructures (created July 1, 2003)	Index consists of 50% S&P/TSX capped, 25% S&P 500 hedged and 25% MSCI – EAFE hedged since October 1, 2006, S&P/TSX adjusted previously		
Private Equity (created July 1, 2003)	Index consists of 60% S&P 500 hedged and 40% MSCI – EAFE hedged since October 1, 2006, S&P 600 adjusted previously		
Real Estate Debt (created April 1, 1995)	Index consists of 90% DEX Universe Bond Index and 10% Lehman Brothers CMBS B hedged since October 1, 2005, SCU previously		
Real Estate (created October 1, 1985)	Aon – Real Estate		

Portfolio not yet created.

PORTFOLIO MANAGERS' VALUE-ADDED OBJECTIVES

The results of the Caisse's portfolio managers are evaluated on the basis of benchmark indexes specific to each management mandate. The managers are expected to build portfolios whose composition differs from that of the benchmarks so as to outperform the indexes over periods of three and five years.

In addition to existing market indexes, which are used for portfolios of liquid investments, the Caisse constructs composite indexes that are better suited to non-traditional investments. Indexes of this kind have been created for the following specialized portfolios: Québec International, Hedge Funds, Commodities, Investments and Infrastructures, Private Equity and Real Estate Debt.

/ The Annual Report 2008 and the Annual Report 2008 – Additional Information are available on the website at www.lacaisse.com.

/ Information: 514 842-3261, info@lacaisse.com

/ *Ce rapport annuel est aussi accessible en français en ligne sur www.lacaisse.com.*

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