Caisse de dépôt et placement du Québec

PRESS RELEASE

EMBARGO – UNTIL THE BEGINNING OF THE PRESS CONFERENCE

THE CAISSE DE DÉPÔT ET PLACEMENT DU QUÉBEC ANNOUNCES A $7.2 BILLION INCREASE IN NET ASSETS AND A 4.0% RETURN IN 2011

Net assets reached $159.0 billion, a $38.9 billion increase since December 2008

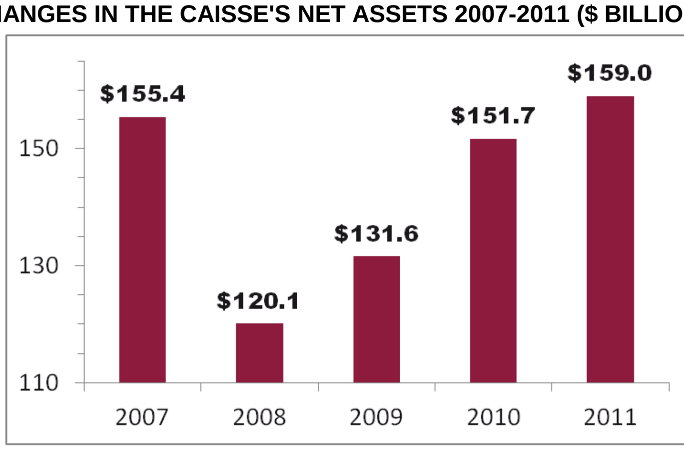
Montréal, February 23, 2012 – The Caisse de dépôt et placement du Québec announced that its weighted average return on depositor funds was 4.0% for the year ended December 31, 2011. The Caisse's net assets stood at $159.0 billion at the end of 2011, compared to $151.7 billion as at December 31, 2010. This growth is due to net investment results of $5.7 billion, plus $1.5 billion in net deposits.

“The Caisse delivered a solid performance in 2011—a year of many challenges in the markets,” said Michael Sabia, the Caisse's President and Chief Executive Officer.

The year 2011 was impacted by the European sovereign debt crisis which, combined with fears of a slowdown in emerging markets, heavily affected markets. Under these excessively volatile market conditions, the Caisse acted quickly by reducing its exposure to equity between the end of June and the end of September and by maintaining a high level of cash. It was also able to capitalize on its investments in Fixed Income, Private Equity, Real Estate and Infrastructure and generate a positive return for its depositors.

"Since 2009, we have worked on improving our ability to face turbulent markets. We have simplified our investment strategies, reduced our leverage and developed new tools, thereby enhancing our efficiency and agility. In 2011, these efforts served us well. Despite difficult conditions, we were able to adjust our asset allocation to protect our depositors' capital and notably grow our assets. After three years of hard work, the Caisse's net assets now stand at $159.0 billion, $3.6 billion above the level reached prior to the 2008 crisis," said Michael Sabia, the Caisse's President and Chief Executive Officer.

CHANGES IN THE CAISSE'S NET ASSETS 2007-2011 ($ BILLIONS)



Since December 2008, depositors' net assets grew by $38.9 billion. This growth is attributable to net investment results of $35.2 billion, plus net deposits of $3.6 billion. For 2009, 2010 and 2011, the Caisse’s annualized return was 9.1%.

SUMMARY OF RESULTS SINCE 2008

	Return		Operating Expenses and External Management Fees		Leverage (percentage of total assets)
	$ billions	%	$ millions	bp	%
2008	**(39.8)**	**(25.0)**	**314**	**21.2**	**36**
3 years					
2009	**11.8**	**10.0**	**271**	**22.0**	**23**
2010	**17.7**	**13.6**	**269**	**19.4**	**17**
2011	**5.7**	**4.0**	**278**	**18.0**	**17**
Total	**35.2**	**9.1** [1]	**273** [2]	**19.8** [2]	**n.a.**

[1] Annualized return
[2] Average

"We still have substantial ground to cover, however our performance over the last three years shows that the changes we have implemented are bearing fruit with respect to returns, operational efficiency and risk reduction," commented Mr. Sabia.

2011 ACHIEVEMENTS

During 2011, the Caisse finalized the implementation of the five priorities of its strategic plan and completed an in-depth review of its investment strategies, particularly concerning equity markets and its investments in emerging markets. "We also made significant progress in each of the three components of our contribution to Québec's economic development, namely, investing in promising Québec companies, providing support to companies intent on expanding internationally, and developing entrepreneurship," added Mr. Sabia.

Strong Growth of the Caisse's Assets in Québec

The Caisse's assets in Québec grew by more than $4.5 billion in 2011, now exceeding $41 billion. During the year, we invested in approximately 100 different projects, which include, in particular:

- $400 million in the consortium which began construction of the new CHUM, a major project for the future of cutting-edge medicine;
- $800 million in many successful companies, including Cascades, GENIVAR, Industrial Alliance and Kruger;
- $160 million in the acquisition of Montréal's Rockhill complex and close to $50 million in a dozen real estate projects, including the renovations of Mail Champlain and Château Frontenac;
- $60 million to benefit 58 SMEs located in all regions of Québec, through the Fonds Capital croissance PME, a partnership between the Caisse and Desjardins Group.

Furthermore, the Morningstar National Bank Québec Index, focused exclusively on Québec companies, has been integrated in the Canadian Equity portfolio's benchmark index to better reflect Québec's economic weight. Accordingly, the weighting of Québec securities in the Canadian Equity portfolio grew from 17% at the end of 2010 to approximately 21% at the end of 2011, an increase of close to $600 million.

Finally, the Caisse continued working to forge closer connections with the business community throughout Québec. It also worked closely with Québec universities active in developing financial expertise.

Other Achievements

The Caisse made major investments in other sectors, thereby strengthening its international presence. It also continued to improve both its risk management and in-house expertise, which resulted in a number of achievements. In particular, the Caisse:

- Completed new investments during the year totaling $1.6 billion in the Infrastructure portfolio, including two major projects in the oil and gas sector, namely €360 million in Fluxys, in Belgium, and US$850 million in Colonial Pipeline, the largest pipeline network in the United States, serving 260 terminals in 13 eastern and southern states;
- Increased the number of commitments to emerging markets following the granting of management mandates in equity markets in Brazil, China and India and adopted a plan to invest upwards of $700 million in Brazilian real estate. These investments are made in collaboration with local partners and are in step with the Caisse's long-term strategy;
- Consolidated and reorganized its real estate subsidiaries, and implemented a new strategy focused on operational expertise and on holdings located in countries where the Caisse has a strategic advantage;
- Improved its ability to research and analyze economic and financial trends. The recruitment of international-calibre experts has enabled the Caisse to better understand the macroeconomic and financial climate, the global economic outlook and its potential consequences on the Caisse's holdings;
- Maintained a high level of liquidity, exceeding $45 billion at the end of 2011, allowing the Caisse to meet all its potential obligations, even in the event of a significant market correction. The Caisse uses different extreme scenarios to measure the adequacy of the liquidity it holds. These risk management tools have been developed over the last three years.

MORE DETAILED RESULTS

"The past year was a real roller coaster ride, and market conditions considerably deteriorated in the second half of the year," said Roland Lescure, the Caisse's Executive Vice-President and Chief Investment Officer. "Through our efforts and the tools we developed over the last three years, we were able to act quickly by reducing our exposure to equity markets in the third quarter amidst declining markets, and by subsequently rebuilding our position as systemic risks decreased," he added.

The Caisse’s return was 4.0%, slightly below its benchmark portfolio of 4.2%. Thirteen of the 17 specialized portfolios posted positive results. As such, the four Fixed Income portfolios generated $5.7 billion (10.4% return) while Inflation-Sensitive Investments, which include Real Return Bonds (18.4% return), Infrastructure (23.3% return) and Real Estate (11.0% return), generated $3.1 billion. The Private Equity portfolio (7.1% return) generated $1.1 billion. This return is considerably higher than that posted by Equity Market portfolios (-7.2% return) and limited reductions in value in the Equity category to $3.3 billion.

Asset Class	Net Assets at Dec. 31, 2011 $ billions	Weight %	Net Investment Results $ billions	Return %	Index %
Fixed Income	58.8	37	5.7	10.4	9.5
Inflation-Sensitive Investments	25.2	16	3.1	13.9	15.3
Equity	72.8	46	(3.3)	(4.2)	(3.4)
Total[1]	159.0	100	5.7	4.0	4.2

[1] The total includes hedge fund, ABTN, asset allocation, overlay strategy and cash activities.

Fixed Income

The substantial decline in interest rates allowed the four portfolios in this sector to achieve strong gains with a return of 10.4%, outperforming its benchmark index by 0.9%.

In terms of net investment results, the Bonds portfolio ($4.0 billion) and Real Estate Debt ($1.0 billion) greatly contributed to the growth of depositors' assets. The initiative to refocus our Real Estate Debt activities, announced in the summer of 2009, was completed earlier than expected while generating returns of 17.1% in 2010 and 15.0% in 2011.

Inflation-Sensitive Investments

The three portfolios in this sector posted an excellent return of 13.9% in 2011.

The Real Return Bonds portfolio benefited from the appeal of Canadian bonds and from the lower expectations of real return to generate an 18.4% return.

The Infrastructure portfolio's 23.3% return stems from the robust operational performance of portfolio companies, and from the decline in long-term interest rates. Specifically, the return is in large part due to the performance of energy and airport service assets. This return is substantially above its benchmark index of 12.7%.

The Real Estate portfolio generated $1.8 billion in net investment results (11.0% return) due to a very strong performance in the shopping centre and office building sectors, especially in Canada and the United States. After two years of strong returns, managers have taken advantage of the strength of the Canadian market to sell certain assets and have accumulated cash to be able to reposition the portfolio in 2012.

The Real Estate portfolio return is below its respective benchmark index: 11.0% compared to 15.6%. The high level of cash in the Real Estate portfolio (close to $4 billion at the end of 2011) accounts for approximately half of this difference. The other half is due to the weak return of hotels, funds and other equity held by the portfolio—all non-strategic assets—compared to shopping centre, office building and multi-residential sectors that the Caisse expects to promote in the future.

Equity

After performing strongly for two years, Global Equity markets were unable to sustain the momentum without new monetary and fiscal stimulations by governments. Beginning in the summer, the European sovereign debt crisis, combined with fears of a slowdown in emerging markets and the precarious budgetary situation in the United States eroded investor confidence. Indexes plummeted on the majority of the major stock markets, particularly in the third quarter.

Throughout the year, Equity portfolios posted a negative absolute return of 4.2%, 0.8% below the benchmark index.

The Canadian Equity portfolio generated a -10.6% return, which is well below that of U.S. Equity (4.6% return) and confirms the strong correlation between Canadian Equity markets and Emerging Markets Equity portfolios (-16.4% return). It also falls short of its benchmark index which stood at -8.2%. Certain long-term portfolio positions, linked to the urbanization of emerging markets and the high demand for raw materials, underperformed in 2011. However, these positions have been successful over the long term and should persist accordingly into the future. Furthermore, the portfolio's insufficient exposure to high-dividend companies, which held up very well in 2011, accounts for much for the decline in value.

Now more than ever, the globalized world in which companies operate requires investors to deeply understand their strengths and overcome their weaknesses. The Caisse has initiated an in-depth review of the positioning of the Canadian Equity portfolio to ensure that it is well aligned with the new market conditions.

The Private Equity portfolio generated a 7.1% return. This performance is significantly above public market benchmark indexes and is due primarily to buyout activities. This portfolio continues to perform very well over time with annual returns of 10.8% in 2009 and 26.7% in 2010.

Value Added

Each year, the Caisse compares its performance with that of its benchmark portfolio. Since the reorganization of the Caisse's activities in the summer of 2009, the value added represents slightly more than $6.4 billion.

VALUE ADDED SINCE THE PORTFOLIO RESTRUCTURING IN JULY 2009

Asset Class	Annualized Return %	Index %	Added Value $ billions
Fixed Income	9.3	7.6	2.2
Inflation-Sensitive Investments	15.8	10.6	2.3
Equity	10.6	9.2	1.8
Total[1]	11.2	9.1	6.4

[1] The total includes hedge fund, ABTN, asset allocation, overlay strategy, commodity and cash activities.

FINANCIAL FOUNDATIONS

During 2011, the Caisse's financial position remained solid with overall portfolio liquidity totaling over $45 billion and leverage (liabilities over total assets) remaining stable at 17%.

Credit rating agencies reaffirmed the Caisse's investment grade credit rating with a stable outlook, namely AAA (DBRS), AAA (S&P) and Aaa (Moody's).

OPERATING EXPENSES

In 2011, the Caisse continued to improve its efficiency, paying close attention to its operating expenses. As such, total operating expenses, including external management fees, stood at $278 million in 2011. The ratio of operating expenses to total assets therefore decreased from 19.4 basis points (bp) in 2010 to 18.0 bp in 2011, a level that places the Caisse among best-in-class fund managers.

CONCLUSION

"Once again, in 2011, the Caisse posted solid results. We are now able to focus on the future; a future certainly ripe with challenges, but also business opportunities. Although we approach the global economy's high level of risk prudently, we are very well positioned to seize very attractive investment opportunities created by this climate of uncertainty and by the growth of emerging markets. For the first time in a long time at the Caisse, we have the financial flexibility to take advantage of such opportunities, both here in Québec and elsewhere in the world. This is essentially what we can expect in the years to come," concluded Mr. Sabia.

ABOUT THE CAISSE DE DÉPÔT ET PLACEMENT DU QUÉBEC

The Caisse de dépôt et placement du Québec is a financial institution that manages the funds primarily for public and private pension and insurance plans. As at December 31, 2011, it held $159 billion in net assets. As one of Canada's leading institutional fund managers, the Caisse invests in major financial markets, private equity and real estate. For more information: www.lacaisse.com.

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Returns

(for the year ended December 31, 2011)

Specialized Portfolios [1]	Net Assets at Dec. 31, 2011 ($ millions)[2]	Net Investment Results ($ millions)[2]	Return %	Index %	Variance ($ millions)
Fixed Income					
Short Term Investments	6,762	47	1.1	1.0	3
Bonds	41,600	3,981	10.1	9.8	103
Long Term Bonds	3,758	628	18.6	18.6	(2)
Real Estate Debt	6,680	1,014	15.0	9.5	369
Subtotal	**58,800**	**5,670**	**10.4**	**9.5**	**473**
Inflation-Sensitive Investments					
Real Return Bonds	1,288	203	18.4	18.3	0
Infrastructure	5,751	1,043	23.3	12.7	446
Real Estate	18,205	1,835	11.0	15.6	(728)
Subtotal	**25,244**	**3,081**	**13.9**	**15.3**	**(282)**
Equity					
Canadian Equity	18,564	(2,133)	(10.6)	(8.2)	(497)
Global Equity	10,855	(683)	(5.7)	(5.1)	(57)
Québec International	4,547	87	1.6	1.9	(24)
U.S. Equity	8,120	319	4.6	4.6	(1)
EAFE Equity	9,102	(962)	(9.6)	(10.0)	37
Emerging Markets Equity	5,886	(1,040)	(16.4)	(16.4)	0
Equity Markets Subtotal	**57,074**	**(4,412)**	**(7.2)**	**(6.3)**	**(541)**
Private Equity	15,746	1,113	7.1	7.4	(78)
Subtotal	**72,820**	**(3,299)**	**(4.2)**	**(3.4)**	**(619)**
Hedge Fund	3,270	4	0.5	(0.5)	29
Asset Allocation	1,221	121	n.a.	n.a.	n.a.
ABTN [3]	(2,520)	93	n.a.	n.a.	n.a.
Total [4]	**158,965**	**5,746**	**4.0**	**4.2**	**(366) [5]**

[1] The following are index-managed portfolios: Short Term Investments, Long Term Bonds, Real Return Bonds, U.S. Equity, European, Australasia & Far East (EAFE) Equity and Emerging Markets Equity.

[2] Net assets and net investment results are net of operating expenses.

[3] The ABTN portfolio financing exceeds the fair market value of its investments and mainly accounts for the negative net assets.

[4] The total includes overlay strategies and cash activities.

[5] ABTN activities, asset allocation, overlay strategies and cash activities of specific funds contribute to the total variance.

OVERALL PORTFOLIO MANAGEMENT

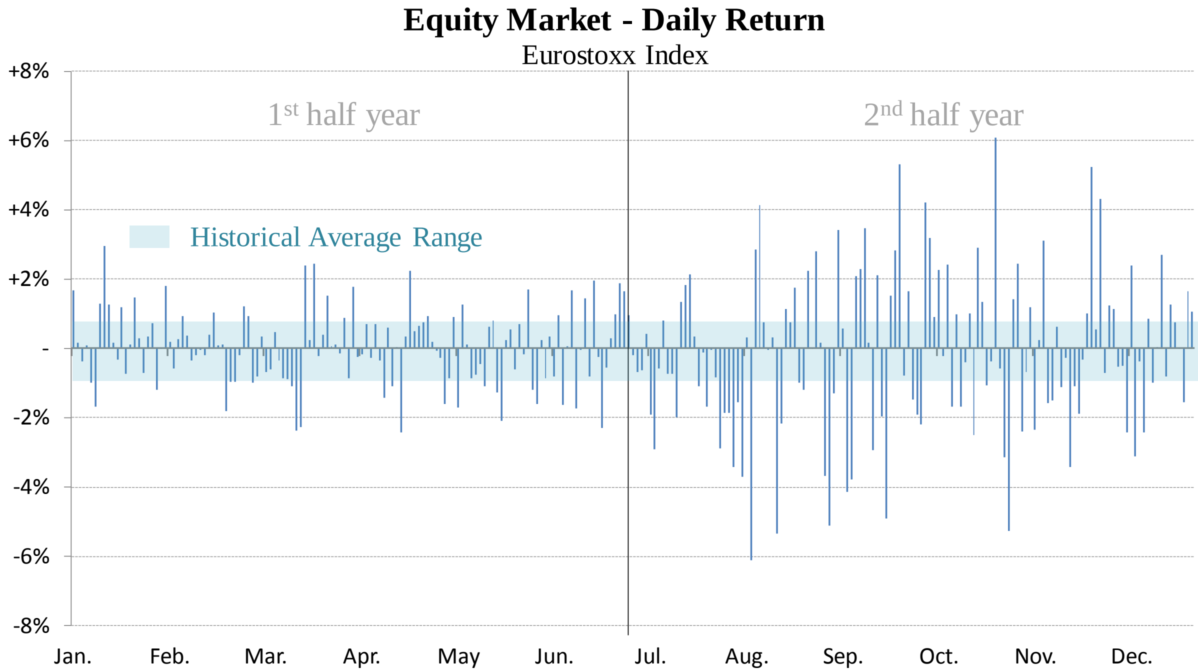
SUMMARY FOR THE YEAR

In a year marked by the European economic crisis and global uncertainty, there was a sharp rise in market volatility, essentially in the latter half of the year. In this context, overall portfolio management began to include protecting assets against a major decrease in equity markets. Due to efforts made and the tools developed in the past three years, hedging positions were managed in a flexible manner to take changing risk into account. As a result, the volatility for Caisse portfolio returns was significantly reduced.

MARKET CONDITIONS

The year started off with the Arab spring and the Tsunami in Japan. However, although these were major events, they ultimately had only a marginal impact on equity markets. Buoyed by a good outlook for growth and continuing expansionist monetary policies, in addition to major increases in profits recorded by publicly listed companies, western equity markets saw growth of approximately 1% to 3% in the first half of the year. Most importantly, this growth was achieved in an environment marked by little volatility, showing that investors were starting to regain their confidence in the markets.

There was a completely different story in the second half of the year. The downgrade of the U.S. credit rating and, especially, a deepening crisis in Europe had an impact on equity markets around the world. In the third quarter, markets tumbled by between -7% (U.S.) and -16% (Europe and emerging countries). Canadian markets declined by 12%. In addition to these equity market declines, there was a substantial increase in volatility which also remained in the fourth quarter. This illustrates the extent of the systemic risk at the height of the European economic crisis.



PORTFOLIO MANAGEMENT

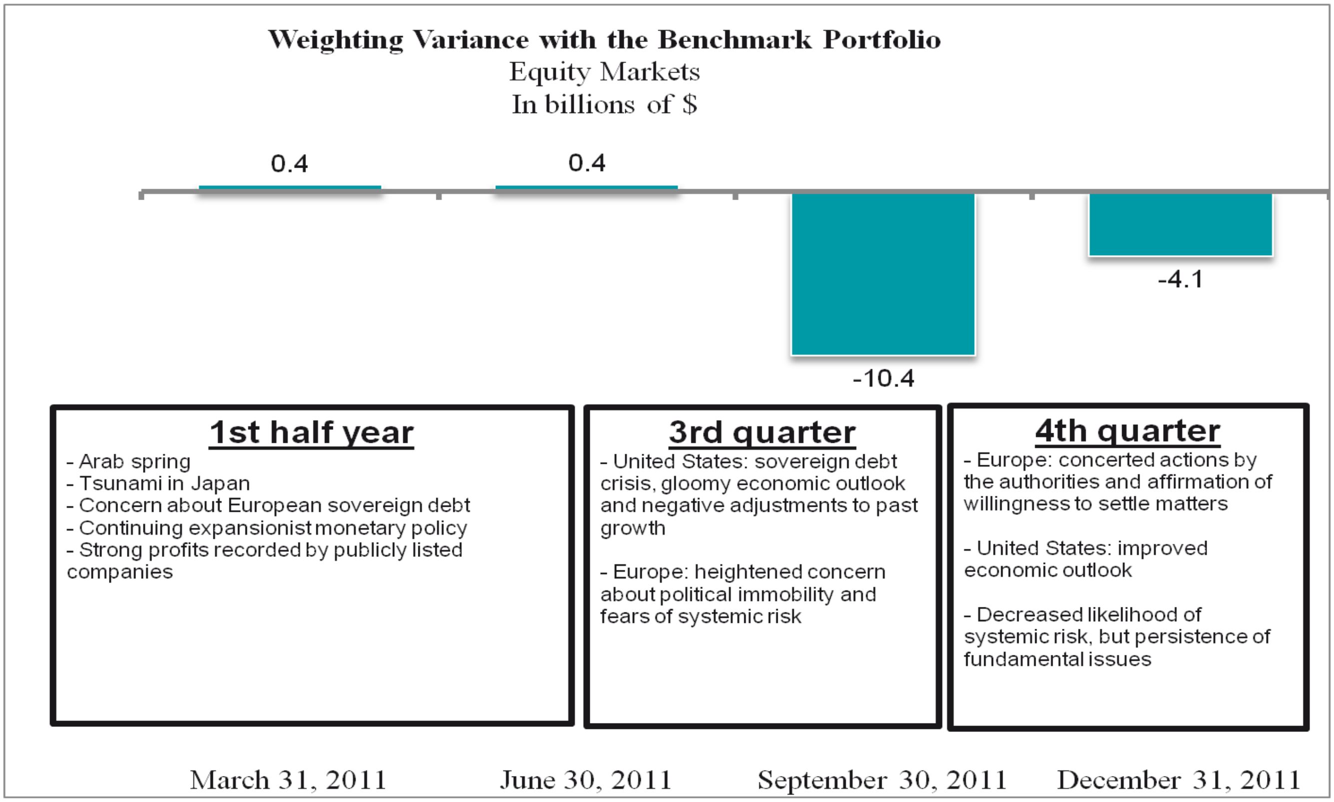
During the first six months, and considering the improvement in the market environment, the asset allocation for the overall portfolio remained close to the benchmark. Equity market exposure therefore remained around 37%.

During the summer, the deteriorating economic outlook in the U.S., the downgrade of the U.S. credit rating, and Europe's inability to find a credible solution to the crisis in Greece led the Caisse to put in place defensive measures to protect the overall portfolio. In September, there was the risk that the crisis in Greece would spread to the rest of Europe, affecting the banking sector as well as peripheral countries. Due to the threat of a systemic crisis, the Caisse further reduced its equity market exposure, which stood at 30% in September.

The European Summit held in October made it possible to officially recognize the need to recapitalize European banks and to recognize major losses on Greek debt. This systemic risk then gradually diminished with changes of government in Greece and Italy, followed by the arrival on the scene of the European Central Bank in December. In this context, hedging positions were significantly reduced without being completely cancelled.

In addition to these equity market hedging positions, the Caisse ensured prudent cash management throughout the year. Cash varied between $5 billion and $9 billion during the second half of the year.

The following chart presents changes in Caisse equity market exposure:



FIXED INCOME

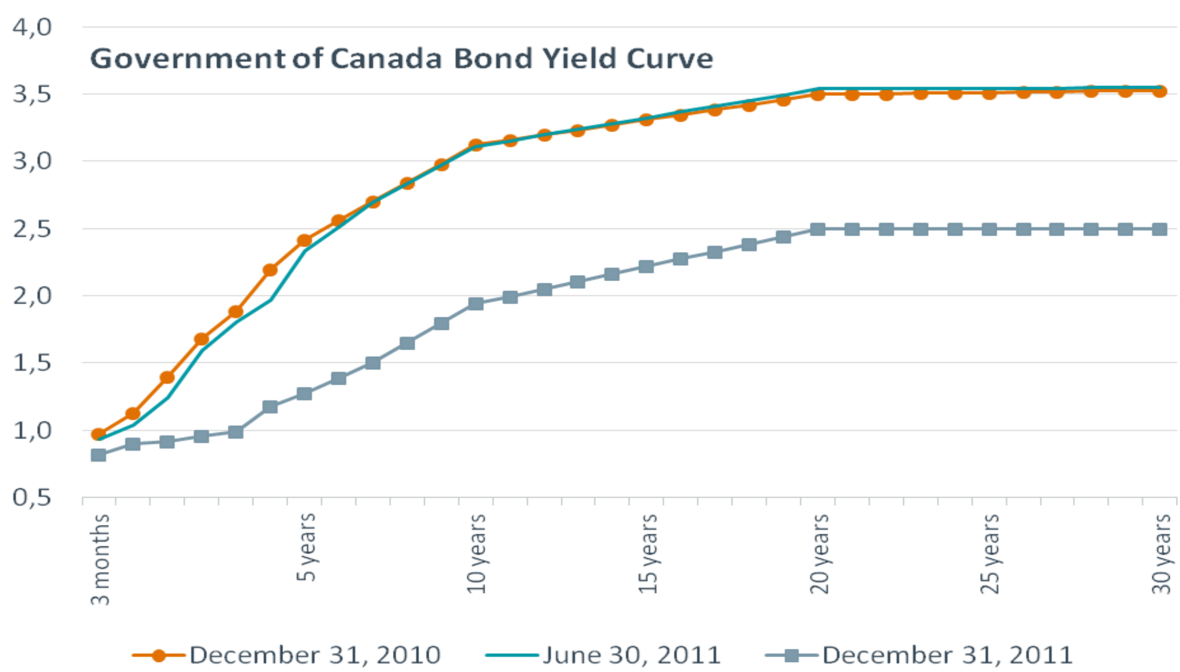
DESCRIPTION

The Fixed Income category consists of four portfolios: Short Term Investments, Bonds, Long Term Bonds and Real Estate Debt. It reduces the level of overall portfolio risk and matches the assets and liabilities of depositors.

The Bond and Real Estate Debt portfolios, with net assets totaling $48.3 billion, are actively managed, while the Short Term Investments and Long Term Bond portfolios, with net assets totaling $10.5 billion, are index-managed.

MARKET CONDITIONS

In 2011, the Canadian bond market had another year of good returns on government and corporate securities. This was largely due to the sharp decrease in the Government of Canada bond yield curve in 2011, primarily during the second half of the year (see graph). The decrease was driven by the precarious political and economic situation in the rest of the world, combined with Canada's reputedly more favourable fiscal position, as reflected in the Government of Canada's continued AAA credit rating. The Bank of Canada had to revise its economic scenario downwards and postpone monetary tightening.



The global bond markets also had a good year despite modest economic growth and the end of a wave of monetary easing in the United States. The solvency of mainly peripheral eurozone countries (Greece, Spain, Ireland, Italy and Portugal) was a focus of concern from August onwards. The market reacted adversely to a risk of contagion following a possible Greek default, and more specifically, its repercussions on the European banking system. Although stabilization measures (debt buybacks on the secondary markets and bank recapitalizations) were implemented, the expected economic slowdown depressed long-term rates on the major markets. Yields on 10-year government bonds in Canada and the U.S. ended the year at historical lows of less than 2%.

Changes in Government of Canada 10-Year Bond Yields

Source: Bank of Canada
Since 1982: Yield on Government of Canada 10-year benchmark bonds
Before 1982: Average yield on Government of Canada marketable bonds with maturities of over 10 years

The Canadian commercial real estate debt market also responded well to this environment with very positive performance in 2011. With mortgage credit spreads remaining fairly stable, the significant decrease in Canadian interest rates translated into higher returns over the year.

HIGHLIGHTS

Specialized Portfolio Performance

For the year ended December 31, 2011

	$ billions	Weight[1] %	Net Investment Results $ millions	Return %	Index %
Short Term Investments	6.8	4.3	47	1.1	1.0
Bonds	41.6	26.2	3,981	10.1	9.8
Long Term Bonds	3.8	2.4	628	18.6	18.6
Real Estate Debt	6.7	4.2	1,014	15.0	9.5
Total	**58.8**	**37.0**	**5,670**	**10.4**	**9.5**

[1] Compared to the Caisse's net assets

The overall return on the Fixed Income category was 10.4 %, 0.9% above the benchmark index. The portfolios in this category responded positively to a generalized decline in interest rates following on previous rate decreases in 2009 and 2010.

SHORT TERM INVESTMENTS

- The portfolio returned 1.1%, outperforming its benchmark index by 0.1%. This performance reflects an environment of very low short-term rates.

BONDS

- The largest share of assets held at the Caisse is invested in this portfolio: 26.2% or $41.6 billion as at December 31, 2011.
- The portfolio returned 10.1%, generating $4.0 billion in net investment results. The return was 0.3% above its benchmark index.
- The decline in medium- and long-term rates over the year drove up portfolio returns. Two thirds of the total return are value increases resulting from this decline.

LONG TERM BONDS

- The return on the portfolio was identical to the benchmark index at 18.6%.
- Almost 80% of the return was generated by value increases from lower long-term interest rates on government securities in the portfolio, which fell from 4% to 3%, a 1% decrease. This had an especially positive impact on the performance of this long-horizon portfolio.

REAL ESTATE DEBT

- This portfolio returned 15.0%, or $1.0 billion in net investment results, outperforming its benchmark index by 5.4%.
- Lower mortgage rates in Canada largely explain this strong performance in 2011.
- The last foreign assets were sold as part of the portfolio refocusing strategy. This took place in favourable conditions, which also helped deliver higher returns on these assets.

INFLATION-SENSITIVE INVESTMENTS

DESCRIPTION

The Inflation-Sensitive Investments category consists of three portfolios: Real Return Bonds, Infrastructure and Real Estate. These portfolios provide exposure to markets, including inflation-indexed, income-generating investments. This can partly hedge against the inflation risk associated with the liabilities of many Caisse depositors.

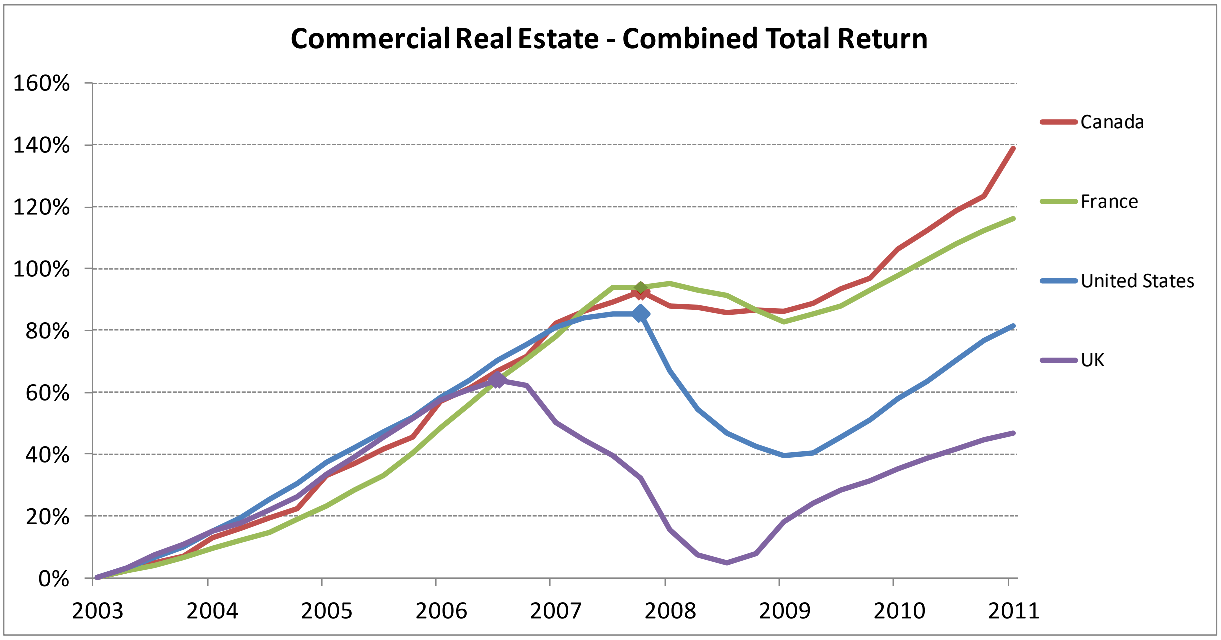
The Infrastructure and Real Estate portfolios, which have $24.0 billion in net assets, are actively managed. The Real Return Bonds portfolio, which has $1.3 billion in net assets, is index managed.

MARKET CONDITIONS

In an environment characterized by low interest rates and particularly volatile equity markets, less liquid assets, such as infrastructures and real estate, have become increasingly popular on account of the high, stable current income they provide and a generally low risk profile. Despite credit market volatility and the economic slowdown, projects and assets with excellent fundamentals maintained their ability to obtain financing at low rates, which has fared well for them and enabled them to post high returns.

In the infrastructure sector, the rebound in activity in 2010 continued into 2011, with a sharp rise in investments in this asset class. In the third quarter, 137 infrastructure funds, targeting an amount of $96 billion, were included on a global scale.

This phenomenon was also seen in real estate. On the one hand, in Canada, investment in commercial real estate assets maintained its solid performance as observed in 2010. On the other hand, for certain market sectors in the United States and Europe, commercial real estate investment fully offset the losses suffered during the 2008 financial crisis. In Europe, real estate asset sales by banks and governments resulted in an increased offer of assets on the market and, consequently, a certain price stabilization towards the end of the year.



Source : IPD (Investment Property Databank); NCREIF (National Council of Real Estate Investment Fiduciaries); in CAD hedged for currency risk

HIGHLIGHTS

Returns on Specialized Portfolios
For the year ended December 31, 2011

	$ billions	Weight[1] %	Net Investment Results $ millions	Return %	Index %
Real Return Bonds	1.3	0.8	203	18.4	18.3
Infrastructure	5.8	3.6	1,043	23.3	12.7
Real Estate	18.2	11.5	1,835	11.0	15.6
Total	**25.2**	**15.9**	**3,081**	**13.9**	**15.3**

[1] Compared to the Caisse's net assets

The overall return of the Inflation-Sensitive Investments category was 13.9%, 1.4% below the benchmark index, generating $3.1 billion in net investment results.

REAL RETURN BONDS

- The Real Return Bonds portfolio obtained an 18.4% return.
- Of this performance, 2.9% is the result of inflation over the period.
- The majority of the return is due to the decline in real interest rates over the year. They decreased from 1.1% to 0.26%, a 0.84% decline. The effect on the return of such decreases in rates is particularly positive for this portfolio given its long term.
- This year's excellent performance is in addition to the particularly high return of the last two years. In 2009 and 2010, the return was 17.1% and 11.1%, respectively.

INFRASTRUCTURE

- This specialized portfolio generated a return of 23.3%, $1.0 billion in net investment results. The return is 10.6% above its benchmark index.
- This return, which is higher than the expected long-term return, stems from the sound operational performance of portfolio companies and from the decline in long-term interest rates. In particular, the return substantially owes to the performance of energy and airport service assets, including Trencap and BAA (*British Airports Authority*).
- This year's excellent performance builds on the particularly high return from the last two years. In 2009 and 2010, the return on this type of asset was 33.6% and 25.4%, respectively.

REAL ESTATE

- The return on this portfolio stood at 11.0% in 2011, $1.8 billion in net investment results. The return was 4.7% below its benchmark index.
- This return is primarily attributable to increases in value of retail shopping centres and office buildings in Canada and the United States.
- The underperformance of the portfolio against its index is mainly due to the dilutive effect of cash and to the low return of funds and equity held by the portfolio relative to that of shopping centre, office, and industrial and residential building sectors that make up the benchmark index.
- This year's high return builds on the high return of 13.4% posted in 2010. In 2009, the portfolio had plummeted 12.7% in the aftermath of the 2008 financial crisis.

EQUITY

DESCRIPTION

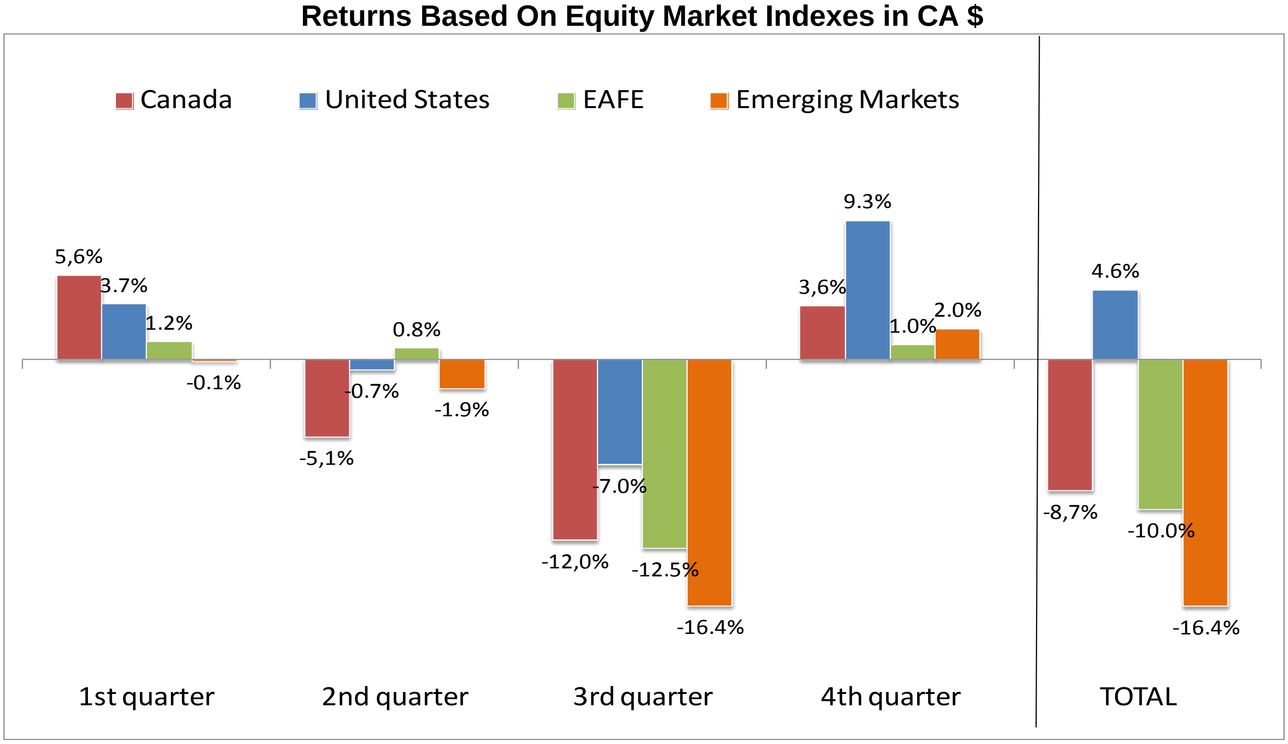
The Equity category consists of seven portfolios: Canadian Equity, Global Equity, Québec International, U.S. Equity, EAFE (Europe, Australasia, Far East) Equity, Emerging Markets Equity and Private Equity.

The Canadian Equity, Global Equity, Québec International and Private Equity portfolios, which have $49.7 billion in net assets, are actively managed. The U.S. Equity, EAFE Equity and Emerging Markets Equity portfolios, which have $23.1 billion in net assets, are index managed.

MARKET CONDITIONS

After a rather promising start to the year, most equity market indexes recorded heavy losses in the third quarter. These losses were especially related to the uncertainty caused by the European sovereign debt problems, the political debate in the U.S. regarding the raising of the debt ceiling, followed by the downgrade of sovereign debt from AAA to AA+, and the threat of an economic slowdown in emerging countries.

Returns Based On Equity Market Indexes in CA $



In total, and in spite of average earnings increases recorded by publicly listed companies, most of the major equity market indexes declined in 2011. The Canadian market (S&P TSX) is down 8.7%, the MSCI EAFE declined by 10.0% while the MSCI EM (emerging markets) is down 16.4%. Among the EAFE markets, European markets were particularly hard hit, with declines of close to 15%. The S&P 500 is the only major equity market index to end the year in positive territory (4.6%).

European markets were especially hard hit by the euro crisis, which created some very serious concerns regarding the health of eurozone banks. Emerging and Canadian markets saw declines as a result of uncertainty regarding global economic growth. The U.S. market resisted these pressures due to its more defensive sector mix and year-end U.S. economic news that reassured investors.

HIGHLIGHTS

Specialized Portfolio Returns
Year ended December 31, 2011

	$ billions	Weight[1] %	Net Investment Results $ millions	Return %	Index %
Equity					
Canadian Equity	18.6	11.7	(2,133)	(10.6)	(8.2)
Global Equity	10.9	6.8	(683)	(5.7)	(5.1)
Québec International	4.5	2.9	87	1.6	1.9
U.S. Equity	8.1	5.1	319	4.6	4.6
EAFE Equity	9.1	5.7	(962)	(9.6)	(10.0)
Emerging Markets Equity	5.9	3.7	(1,040)	(16.4)	(16.4)
Subtotal – Equity Markets	**57.1**	**35.9**	**(4,412)**	**(7.2**	**(6.3)**
Private Equity	15.7	9.9	1,113	7.1	7.4
Total	**72.8**	**45.8**	**(3,299)**	**(4.2)**	**(3.4)**

[1] Compared to the Caisse's net assets

The overall return for the Equity category is therefore -4.2%, which is 0.8% less than the benchmark index.

CANADIAN EQUITY

- The Canadian Equity portfolio generated a return of -10.6%, for net investment results of -$2.1 billion. This return is 2.4% below the benchmark index.
- This return is well below the 4.6% return for U.S. equity and confirms that Canadian equity markets are closely tied to emerging markets (return of -16.4%). The sector mix for the Canadian equity market represents a heavy exposure to the financial (29%) and materials (21%) sectors. Fear of a financial crisis and concerns regarding global economic growth, in particular in emerging economies, had an especially hard impact on the returns of companies in these sectors, which also explains the negative return posted by the Canadian market.
- The portfolio return is nonetheless below that of the index, mainly as a result of:
  - Certain long-term portfolio positions relating to urbanization in emerging countries and strong demand for basic materials underperformed in 2011. However, these positions paid off well in the long term and should continue to do so in the future.
  - The portfolio's under-exposure to companies paying high dividends, which resisted pressures very well in 2011 due to the major drop in interest rates.
- In early 2011, the Morningstar National Bank Québec Index, reserved exclusively for Québec companies, was incorporated into the Canadian Equity portfolio benchmark index in order to better represent the reality of the Québec economy in this portfolio. The value of investments in Québec grew by $589 million during the year and has increased by $1.2 billion since the end of 2009. Québec securities account for 21% of the Canadian portfolio at year end, up 4.2% in the past 12 months.

GLOBAL EQUITY

- The Global Equity portfolio generated a return of -5.7%, which is 0.6% below the benchmark index.
- The variance with this index is mainly attributable to positions in the healthcare, industrial products and natural resources sectors.
- In 2011, the management team completed the implementation of its new external management strategy, targeting specialized managers in countries such as China, India or Brazil, or exposure to specific economic sectors.

QUÉBEC INTERNATIONAL

- The Québec International portfolio generated a return of 1.6 %, which is close to the benchmark index.
- This return is better than the return for the Global Equity portfolio, mainly due to the high rate of return for the portfolio's bond component. The absence of emerging countries in the portfolio was also a favourable factor in 2011.

U.S. EQUITY, EAFE EQUITY AND EMERGING MARKETS EQUITY

- These portfolios, which are index managed, generated returns of between -16.4% and 4.6% during the year, which is in line with their benchmark index.
- Equity markets in emerging countries, Japan and the euro zone had an especially difficult year, with returns of between -12.2% and -16.4%.

PRIVATE EQUITY

- The Private Equity portfolio posted a return of 7.1%, which exceeds the return for equity market indexes but is 0.3% less than the return for the portfolio benchmark index.
- A total of 80% of the portfolio's performance is attributable to leveraged buyout financing activities and, especially, investments in funds.
- There were two phases in the Private Equity market in 2011. The first six months were marked by a high level of activity characterized by many refinancings, mergers and acquisitions and initial public offerings.
- There was a complete turnaround of the situation in the latter half of the year.
    - The financing market had completely dried up.
    - There was a considerable slowdown in activity for mergers and acquisitions and initial public offerings.
    - However, the market conditions favoured development capital transactions since companies sought solid partners to realize and ensure their future growth.
- Holding companies were very active on financial markets, carrying out refinancings while making the most of low rates and reviewing their loan maturities. The management team also took advantage of favourable market conditions to re-position the funds portfolio due to transactions on the secondary market, generating net inflows in excess of $1 billion. These two factors contributed to improving the portfolio quality and therefore reducing risk.
- New portfolio investments totaled $2.5 billion: $1.3 billion in direct investments, including $649 million in Québec and $1.2 billion in funds.

VALUATION OF INVESTMENTS

The Caisse performs a comprehensive fair value assessment of its illiquid real estate, infrastructure and private equity investments. In accordance with current Canadian accounting rules, it must value them at the price it would obtain if they were sold on the market under normal competitive conditions.

Independent external firms — external appraisers and valuation committees made up of experts in the field — evaluate all major investments. In addition, as part of their audit of the Caisse's financial statements, the co-auditors of the Caisse, the Auditor General of Québec and Ernst & Young, review the fair value of investments.

REAL ESTATE

- External chartered appraisers certify the fair value of real estate assets.
- 99% of real estate is reviewed in this way.

INFRASTRUCTURE AND PRIVATE EQUITY

- Investments with a fair value exceeding a predefined materiality threshold are subject to independent valuation committee or external appraiser review.
- 92% of the fair value of portfolio investments is reviewed in this way. .