Caisse de dépôt et placement du Québec

Equities

HIGHLIGHTS

EQUITIES	5 years	2019
$167.1 B Net assets as at December 31, 2019	10.7% Annualized return	15.3% Return
	$68.4 B Investment results	$22.2 B Investment results

2 portfolios

Equity Markets

Benefit

The risk-adjusted return is higher than that of markets as a result of an absolute-return approach

Private Equity

Benefit

Expected long-term performance above that of equity markets

The **Equities** class accounted for nearly 50% of CDPQ's overall portfolio as at December 31, 2019 and includes two portfolios:

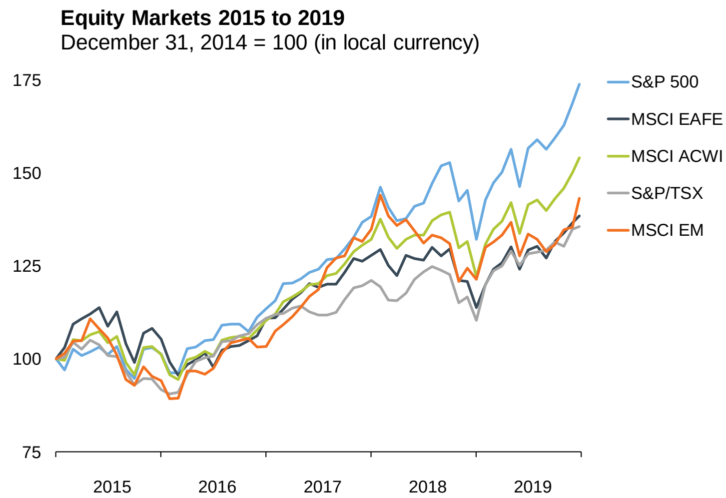
- **Equity Markets:** Actively managed, this portfolio invests in a wide range of corporate securities based on their fundamental value. It aims for sustained performance over the long term through its seven management mandates:
  - Global Quality
  - Canada
  - Growth Markets
  - Alternative Beta
  - Global Value
  - Relationship Investing
  - Strategic
- **Private Equity:** This portfolio includes securities of public and private companies in which CDPQ takes privately negotiated stakes, thereby becoming a long-term partner. A portion of the portfolio's assets are also managed through strategic partnerships with fund managers.

Market conditions

Equity Markets

Taking the post-March 2009 financial crisis low as its starting point, the current bull market is the longest in history, having lasted the entire decade. From 2015 to 2019, the main global stock indexes posted positive returns.

In 2019, the majority of indexes recorded some of their best annual returns of the economic cycle – an increase that follows the 2018 year-end correction. A variety of factors explain this: softening monetary policy around the world, labour resilience and mitigation of trade risks related to Brexit and tensions between the United States and China.



Among the major stock indexes, the S&P 500 posted its best return in five years, with an annualized gain of 11.7% (in local currency, all returns being presented in local currency on this page), especially due to the information technology (IT) and consumer discretionary sectors. The index obtained a 31.5% return in 2019, in a year marked by three phases.

The first was characterized by a change in tone by the U.S. Federal Reserve (the Fed) following the stock market correction at the end of 2018. The announcement that it was softening its monetary policy set off a market recovery that lasted until May. The second saw trade tensions between the United States and China heat up. The index was volatile in this phase, with no clear direction in its movements. Then, during the third phase at the end of the year, the rising probability of a Chinese-American agreement and stabilization of several economic indicators drove the S&P 500 to a record high.

The MSCI EAFE (Europe, Australasia, Far East) recorded an annual average return of 6.7% over five years and a 21.7% return in 2019. The improvement of certain economic data in Germany at the very end of the year, combined with monetary support from the European Central Bank, allowed European shares to deliver an annual performance of 23.8%, the most robust of the decade.

The Canadian S&P/TSX produced a 6.3% average annual return over five years. Its 22.9% return in 2019 is largely driven by an improvement in the natural resources sector. However, despite more moderate economic growth, the resilience of the labour market, rising core inflation and significant household debt prompted the Bank of Canada to hold its key rate steady during the year, while other banks lowered theirs.

Lastly, the MSCI EM growth markets index recorded an annual average gain of 7.5% over five years and of 18.0% in 2019. Cooling trade tensions with China and optimism on Brazilian economic policy were a big help to the index, while Indian stocks recorded performance that was positive but below the index due to slowing domestic growth.

Private Equity

Over the last five years, private equity markets generated high returns. This growth continued in 2019, but was below that of equity markets. Low lending rates and the vitality of the main global economies, combined with strong demand for this asset class, stimulated company valuations, which were up sharply from levels five years ago. Capital available for investment reached a new summit, having almost doubled since 2015, and remains concentrated in North America and Europe.

Equity Markets portfolio returns

In recent years, CDPQ has gradually moved from index-based to absolute-return management for its Equity Markets portfolios. This approach, which focuses on selecting assets based on their fundamental qualities, has delivered strong results. Over five years, the portfolio generated investment results of $48.7 billion and an annualized return of 10.0% over five years. It outperformed its benchmark by 1.2%, the equivalent of $5.2 billion in value added.

In 2019, while markets were booming, the portfolio posted a 17.2% return, lower than its index but well aligned with CDPQ's strategy. The strategy is based on constructing a portfolio that is resilient in the long term, in order to lessen sensitivity to market downswings, which also partially limits its exposure to market upswings. As for the impact of exchange rate fluctuations, it differs from one year to the next, but is favourable over five years.

GLOBAL QUALITY MANDATE

A pillar of CDPQ's absolute-return management strategy, this mandate invests in the securities of quality companies exposed to global growth that are traded on the major global stock exchanges. It targets companies with high and stable profits, solid economic foundations and cautious use of leverage. Since its creation in 2013, the mandate has obtained a risk-adjusted return greater than the market.

	5 years		2019	
$42.8 B Net assets as at December 31, 2019	11.7% Annualized return	9.4% Benchmark	18.2% Return	17.3% Benchmark

$19.9 B
5-year investment results

$6.8 B
2019 investment results

Five-year return

The mandate generated an annualized return of 11.7%, 2.3% higher than its benchmark index, which was 9.4%. This difference represents $3.7 billion in value added, which is largely the result of security selection. This is by far the primary contributor to the total value added created by all mandates. Over five years, the mandate generated investment results of close to $20 billion, driven by the excellent performance of the securities of companies based in the United States. Most sectors posted a high return over the period, particularly health care, consumer staples and IT. Since its creation, the mandate has shown resilience in different market conditions, outperforming the market while incurring lower risk.

2019 return

For one year, Global Quality generated investment results of $6.8 billion, the largest contribution among the mandates, with a return of 18.2%. This is largely explained by the selection of quality securities, particularly of U.S. IT companies. Both internal and external management activities contributed to the return. The former benefited from a favourable geographic allocation and the exceptional performance of companies in the health care and IT sectors. The latter benefited from a favourable selection of securities and significant exposure to the United States and to the IT sector.

CANADA MANDATE

This mandate invests in securities of publicly-listed Canadian corporations, with an emphasis on constructing a quality, concentrated portfolio that reflects distinctive aspects of the Canadian asset universe. It targets companies that, in addition to having exposure to growth, possess fundamental qualities and competitive advantages that will persist in the long term. Shares in Québec companies represent around 35.5% of the mandate's composition, compared to 16.1% for the S&P/TSX index.

	5 years		2019	
$22.3 B Net assets as at December 31, 2019	7.3% Annualized return	6.5% Benchmark	20.5% Return	23.1% Benchmark

$8.2 B
5-year investment results

Five-year return

The mandate generated an annualized return of 7.3%, and investment results of $8.2 billion. It outperformed its benchmark index by 0.8% and generated $891 million of value added. The strategy based on the robustness of the U.S. economy was good, both over five years and one year. Canadian companies active in the United States made strong contributions to the performance. This is seen with CGI, Alimentation Couche-Tard and CN, stocks representing the mandate's quality approach. Except for energy, which slumped during the period, all sectors made a positive contribution. Finance stands out due to its weighting and the excellent return of companies such as TD, RBC, Intact, Scotiabank, Industrial Alliance and Manulife. Note that for five years, this mandate has demonstrated resilience during the main market downturns. Risk-adjusted measures of the return were also favourable due to a return that outperformed the benchmark index and a lower risk profile.

$4.1 B
2019 investment results

2019 return

At 20.5%, this mandate posted the best one-year return in the Equity Markets portfolio. It stems mainly from finance and IT securities, but also from energy, which rebounded during the year. All these sectors recorded gains of over 25%. One of the reasons that finance stands out is the large position held in the insurance segment. Its excellent performance and strong weighting in the mandate make this sector the main contributor for the year. Among the factors explaining the difference with the benchmark index is SNC-Lavalin's downslide in 2019.

GROWTH MARKETS MANDATE

This mandate invests in growth market securities. It counts on the strong potential of these economies to produce long-term returns greater than those of stocks in developed markets. It has three components: one that involves absolute-return management carried out by seasoned external managers who share CDPQ's long-term investment approach and who have deep knowledge of these markets; an alternative beta component, where management is based on fundamental measures and not traditional indexes that use market capitalization; and an index-based component.

	5 years		2019	
$20.2 B Net assets as at December 31, 2019	9.2% Annualized return	7.3% Benchmark	17.2% Return	14.3% Benchmark

$7.3 B
5-year investment results

Five-year return

The mandate benefited from strong stock market performance in the major growth markets over the period: China, Taiwan, South Korea, Brazil and India. All sectors, with the exception of communications, posted gains. IT and finance contributed most to the return, which was 9.2% on an annualized basis, compared to 7.3% for the benchmark index. This difference represents $1.5 billion in value added, most of which stems from the external management component, especially managers in China. This demonstrates the merits of the active management strategy that increasingly focuses on partnering with specialized local investment firms. Before 2013, management was essentially index-based. The other components also obtained good returns over the period. Since 2015, the mandate has generated investment results of $7.3 billion.

$3.0 B
2019 investment results

2019 return

The mandate's performance was stimulated by positions in Taiwan, Brazil, and especially, China. The Chinese stock market alone generated half the return, with a good part stemming from stocks managed by local partners. They clearly benefited from the strength of this market, as well as from the careful selection of stocks, which made the difference. The mandate's external management activities were very profitable, both over five years and one year. All sectors made a positive contribution to the return, especially IT, finance and consumer discretionary.

ALTERNATIVE BETA MANDATE

This mandate invests in securities in developed markets, excluding Canada. The strategy involves weighting securities based on various fundamental measures, such as sales, cash flows and dividends, rather than on their market capitalization.

$14.9 B Net assets as at December 31, 2019	5 years	2019	
	This portfolio was created in 2016.	17.3% Return	21.2% Benchmark

$2.5 B
2019 investment results

Return since its creation

Since its creation four years ago, the mandate has delivered investment results of $6.0 billion.

2019 return

The mandate recorded a return of 17.3% in 2019, the majority of which is due to stocks of U.S. companies that were buoyed by that market's vitality. In terms of sectors, the positions in IT contributed most to performance, followed by industrials, health care and consumer staples. A different geographic allocation than the benchmark index's and less exposure to large-cap stocks limited the return. For the year, the portfolio generated investment results of $2.5 billion.

GLOBAL VALUE MANDATE

This mandate targets stocks whose prices seem low based on various measures of fundamental value. They involve stocks that seem undervalued, but with intrinsic value that shows potential of normalizing in the long term. The mandate is managed both internally and externally.

$10.1 B Net assets as at December 31, 2019	5 years	2019	
	This portfolio was created in 2017.	12.1% Return	20.2% Benchmark

$1.0 B
2019 investment results

Return since its creation

Since 2017, the mandate has generated investment results of $1.2 billion.

2019 return

The management process, which is focused on selecting value-style securities, results in a concentrated portfolio, with the positions delivering wide-ranging returns. Therefore, it is the stocks, more than geographical or sectoral factors, that determine performance. In 2019, the strong appreciation of certain stocks helped the mandate deliver a 12.1% return. Stock market conditions in recent years that were beneficial to large U.S. companies, particularly those in IT, to the detriment of value-style stocks, nonetheless had a negative impact when compared to the benchmark index.

Private Equity portfolio returns

This portfolio primarily includes direct investments and stakes in investment funds. Assets are allocated across various sectors and regions, in Canada, the U.S. and Europe, as well as in growth markets. More than a quarter of assets were invested in Québec as at December 31, 2019.

Private Equity is central to CDPQ's strategy of seeking to build long-term partnerships with companies in Québec and around the world, as well as supporting growth and operational excellence. The investment approach is focused on quality business relationships and value creation over time. Over the past several years, the composition of the Private Equity portfolio has changed considerably, as the share of funds has decreased while direct interests in companies have increased, and today represent more than three quarters of the activities.

	5 years		2019	
$50.2 B Net assets as at December 31, 2019	12.5% Annualized return	8.7% Benchmark	10.5% Return	11.8% Benchmark

$19.8 B
5-year investment results

Five-year return

The decision to increase the proportion of direct investments was good for the portfolio, both over five years and one year. Since 2015, the portfolio has generated an annualized return of 12.5% It outperformed its benchmark index by 3.7%, creating $4.8 billion of value added. Over five years, direct investments have turned in a strong performance. They were stimulated by the quality of the portfolio assets, with the main contributors being companies such as CGI, WSP Global and Chewy, a subsidiary of PetSmart. Despite underperforming direct investments, the funds posted a respectable return over the period and contributed strongly to the results. They have also provided CDPQ with attractive direct co-investment opportunities.

Overall, the portfolio obtained investment results of close to $20 billion over five years, thus reaching $50 billion in net assets as at December 31, 2019. The Private Equity teams completed many transactions in Québec and around the world. Close to $44 billion was deployed, with nearly $34 billion in materializations.

$4.5 B
2019 investment results

2019 return

The portfolio's return was 10.5% in 2019, mainly due to the performance of direct investments. This was driven by public securities, as well as the success of the Lightspeed and Chewy (PetSmart) IPOs. Also of note is the contribution from the materialization of the positions in MyEyeDr. and in certain funds. Investment funds provided a lower, but appreciable, return for the year.

In 2019, CDPQ deployed $10.5 billion in Québec and abroad, with major transactions in leading companies, including:

- Nuvei: Significant investment in this Québec company – a global supplier of payment technology – to finance an acquisition in the United Kingdom, establishing its market value at USD 2 billion.
- Cirque du Soleil: USD 120 million in financing, alongside Fonds de solidarité FTQ, to allow this Québec group, a world leader in the entertainment industry, to acquire U.S.-based The Works Entertainment.
- Healthscope: Investment of over AUD 300 million to acquire this leading Australian health care provider as part of a co-investment agreement with Brookfield Business Partners and its institutional partners.
- Hilco Global: A 27.3% stake in the U.S.-based financial services company and long-term partnership agreement targeting annual joint investments of around USD 150 million in distressed assets and other special situations.
- Sanfer: A USD 500 million investment in this independent pharmaceutical company – one of the main players in Mexico – to support its strategic growth in Latin America.
- Allied Universal: A major investment alongside partners in this North American leader in security valued at over USD 7 billion.

Investment results table for Equity Markets portfolios

As at December 31, 2019		5 years			2019		
Specialized portfolio and mandate	Net assets	Investment results	Return	Benchmark	Investment results	Return	Benchmark
	$M	$M	%	%	$M	%	%
Equity Markets	**116,937**	**48,663**	**10.0**	**8.8**	**17,686**	**17.2**	**18.0**
Global Quality mandate	42,828	19,921	11.7	9.4	6,819	18.2	17.3
Canada mandate	22,284	8,193	7.3	6.5	4,084	20.5	23.1
Growth Markets mandate	20,233	7,309	9.2	7.3	2,999	17.2	14.3
Alternative Beta mandate	14,929	5,987	N/A	N/A	2,528	17.3	21.2
Global Quality mandate	10,083	1,173	N/A	N/A	959	12.1	20.2
Other	6,580	6,080	N/A	N/A	297	N/A	N/A
Private Equity	**50,180**	**19,763**	**12.5**	**8.7**	**4,483**	**10.5**	**11.8**
Equities	**167,117**	**68,426**	**10.7**	**8.9**	**22,169**	**15.3**	**16.3**