UNIVERSITY OF ALBERTA

INVESTMENT COMMITTEE REPORT TO THE BOARD OF GOVERNORS

For the Year Ended March 31, 2008

U N I V E R S I T Y O F A L B E R T A

INVESTMENT COMMITTEE REPORT TO THE BOARD OF GOVERNORS

For the Year Ended March 31, 2008

CONTENTS:

Highlights 1

Governance and Compliance 3

Endowment Funds 4

Investment Policy & Risk 4

Investment Performance 4

Spending Policy 7

Non- Endowed Funds 8

Going Forward 9

Appendix 1 – Investment Manager Structure 10

Appendix 2 – Investment Performance by Asset Class 12

Appendix 3 – Long-Term Value Added 17

	2008	2007
Non-Endowed Funds	Millions	
Short-term	$ 567	$ 268
Mid-term	63	91
Long-term	115	90
	745	449
Endowment Funds	734	751
	$ 1,479	$ 1,200

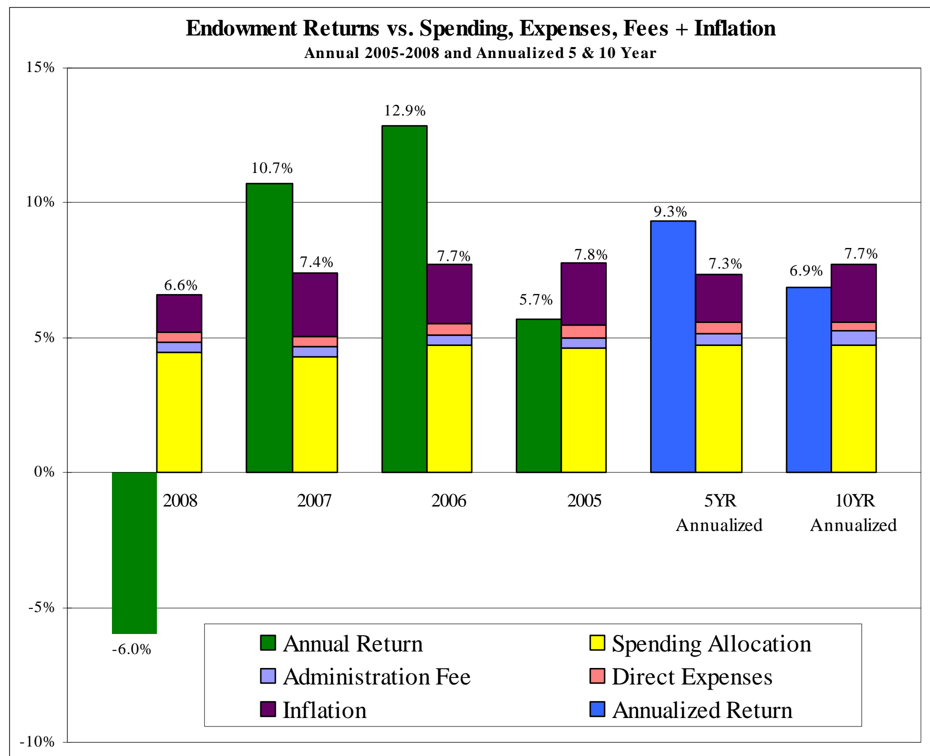
The investment assets of the University of Alberta that are under the governance of the Investment Committee had a total market value of $1,479 million (2007 - $1,200 million) as of March 31, 2008.

Endowment Funds - Highlights

The market value of the endowments decreased by $17 million to $734 million. New contributions to the endowments added $52 million to the value of endowments. However, this positive effect was more than offset by investment losses of $42 million, plus spending allocations and administrative expenses of $27 million. The new contributions include $34 million in new donations, $13 million in Province of Alberta matching grants and $5 million from the Province of Alberta's Access to the Future fund. The aggregate amount available for spending purposes during the year was $39 million.

The primary investment objective for the endowment fund is to earn a return which over time will cover defined expenditures for university programs, fees, expenses and the impact of inflation on the fund.

In order to meet this requirement an investment policy portfolio has been developed which carries a reasonable expectation of generating returns which will meet or exceed the objective and so maintain or grow the earning power of the fund in real terms over time. The policy portfolio is comprised of major asset classes (bonds, stocks, and alternate investments). On the basis of this policy portfolio, investment managers are retained to generate returns which match or exceed the returns provided by various market indices or benchmarks. Over time this objective has been met as the current value of the fund exceeds the inflation adjusted contributions by $72 million. The accompanying chart shows how the actual investment performance has fared relative to this primary objective.



The fund experienced a loss of 6.0% which fell significantly short of the 6.6% primary investment objective as well as having a significant impact on longer term results. This result reflects:

- a capital market environment in which equities, particularly foreign equities affected by the strength of the Canadian dollar, experienced significant losses (the Canadian S&P TSX returned 4% while the MSCI World Index fell by 13.5%);
- the investment policy which strongly favours equity and foreign equity in particular (foreign equity accounts for 55% of the policy benchmark) and
- very narrow leadership in equity market performance which created significant issues for investment managers particularly those with Canadian equity mandates.

In November of 2007 the Board approved a revised Investment Policy following a comprehensive asset-liability study. The Policy is designed to maximize long-term returns with an acceptable level of risk while maintaining the long-term real value of the endowments after spending and expenses. Management with the direction of the Investment Committee is in the process of implementing the new Investment Policy. Key features of the new Investment Policy include the following:

- The allocation to equities is being increased from 70% to 80% offset by a corresponding decrease in the fixed income allocation.
- Enhanced credit quality standards for the fixed income portion of the portfolio commensurate with the reduced allocation to this asset class and deterioration in credit conditions in the market as a whole.
- An increased allocation within the equity component to alternative investment strategies from 5% to 20%. Of this amount, 10% will be allocated to hedge funds, while 5% will be allocated to private equity and 5% to real estate.

Non-Endowed Funds - Highlights

The non-endowed funds have increased by $294 million to $745 million. The funds were invested in highly rated, liquid money market products ($567 million), bonds with a duration of less than 5 years ($63 million), the UEP ($80 million), as well as $35 million in shares of publicly traded spin-off companies. The majority of this increase in total non-endowed funds is attributable to research and capital funding. During the fiscal year ending March 31, 2008, the University received restricted research and capital funding that was not spent in its entirety by the end of the fiscal year. $31 million of the increase in non-endowed funds is attributable to the University's equity holdings in publicly traded spin-off companies.

In August of 2007 a liquidity crisis for third party asset backed commercial paper (ABCP) unfolded. This previously robust market collapsed due to investor concerns about the underlying exposure to US sub-prime mortgage assets in some 22 trusts with a value of $32 billion. At the time the University's exposure to the affected ABCP was $171 million. In addition to this, the University held $39 million in bank sponsored ABCP. All ABCP holdings at the time of acquisition were rated R-1 high by the Dominion Bond Rating Service as required by the University's Investment Policy.

The scope and complexity of this liquidity crisis required an orderly restructuring process involving the cooperation of all market participants. In late August 2007 the University began participating in the restructuring process. As events evolved, it was determined that a more active participation role was in the University's best interests. In late October 2007 the University became a member of the Pan-Canadian Investors Committee for Third-party Structured Asset-Backed Commercial Paper that was overseeing the restructuring process.

The restructuring process will result in the issuance of long-term floating rate notes that match the duration of the underlying assets. Although it is expected that an active market for the restructured notes will evolve over time, it is possible that the restructured notes will be held to maturity. Using a comprehensive, long-term cash flow forecast, management has concluded that the exposure to ABCP does not represent a liquidity issue for the University. All existing obligations and commitments will continue to be met.

The performance of the non-endowed funds was -2.8% versus a benchmark rate of return of 2.3%. The shortfall in performance relative to the benchmark reflects the impact of the ABCP holdings which were written down by $41 million representing 24% of the ABCP par value.

Governance and Compliance

The Board has delegated to the Investment Committee responsibility and authority to make decisions on behalf of the Board in the Committee's defined area of responsibility, except to the extent that such authority has been specifically limited by the Board in the Terms of Reference for the Committee. The Investment Committee meets regularly as part of its governance responsibility for oversight and implementation of the investment policy. The Investment Committee:

- Reviews and recommends to the Board investment objectives and policies for the Endowment and Non-Endowed funds.
- Approves investment manager mandates, appointments and terminations.
- Monitors compliance to the investment policy and investment manager mandates.
- Addresses and resolves any identified non-compliance matters.

Management provides the Investment Committee with quarterly reports on investment performance. The Investment Committee forwards to the Board an annual investment review. Management retains the services of independent external consultants that specialize in evaluating fund performance on a quarterly basis. Specialized consultants are retained from time to time to assist with governance matters, asset-liability studies and manager searches.

The Investment Committee monitors compliance with the approved investment policy, investment manager mandates and related legal aspects on a regular basis. The aforementioned restructured ABCP holdings will not be in compliance with the investment policy. Management has recommended that in order to maintain value, it is in the University's best interest to hold the restructured securities. In accordance with the authority delegated to the Investment Committee in this matter by the Board of Governors on September 25, 2007; the Investment Committee has approved three ABCP restructuring plans that seek to maintain value of the University's holdings. The Investment Committee has provided the Board of Governors with regular updates on the ABCP restructuring process. All other non-compliance issues have been immaterial and have not resulted in any losses. All have been resolved and there is nothing material to report.

Endowment Funds

Endowments consist of the Unitized Endowment Pool (UEP) and a small number of other endowed funds managed outside the UEP. Endowment investments are comprised of Canadian, U.S. and international equities, Canadian government and corporate bonds, mortgages, real estate, alternative investment funds and money market instruments.

Investment Policy & Risk

The primary investment policy objective for the endowment funds is to maintain the real capital value of the endowment while providing an appropriate level of spending. This requires returns which meet or exceed the all in spending policy rate plus inflation and fees over time within an acceptable level of risk.

The Investment Committee has implemented a number of strategies both to meet the UEP return objectives and to control risk:

- The asset mix policy has established allocations to fixed income products for income, and to equities and alternative assets for growth.
- The asset mix is regularly reviewed for appropriateness and to monitor the risk of the UEP not meeting its primary objective of earning the spending rate plus expense plus inflation (shortfall risk). A review was completed by the Investment Committee during the past fiscal year and approved by the Board of Governors on November 2, 2007 and the new asset mix will be implemented over a period of years.

UEP Asset Mix as at March 31, 2008

	2008 Policy Range Min.-Max. %	2007 Policy Range Min.-Max. %	2008 Actual Asset Mix %	2007 Actual Asset Mix %
Fixed Income				
Money Market Securities	-5 - 5	-5 - 10	5.6	5.0
Bonds, Debentures, Real Return Bonds	10 - 30	20 - 40	25.9	22.3
Total	15 - 25	20 - 40	31.4	27.3
Equity				
Canadian Equity	10 - 20	10 - 20	15.6	15.2
Foreign Equity	40 - 50	40 - 60	49.2	54.6
Alternative Assets	15 - 25	0 - 10	3.8	2.9
Total	75 - 85	60 - 80	68.6	72.7

- The allocation of equities across Canada, the United States of America and other international capital markets diversifies market specific risk.
- The allocation of funds among different fund managers diversifies manager style risk. Please refer to Appendix 1 for details.
- The allocation of funds between both active and passive investment strategies controls active management risk.
- The University has retained a number of managers who are defensive in nature to mitigate losses in a market downturn.
- An active currency manager has been retained to manage currency risk in the portfolio.

Investment Performance
Measuring Performance of Endowment Funds

The returns of individual asset classes in the Fund are measured against established market benchmarks.

With the introduction of the currency overlay program to the UEP, the MSCI World Index return is now calculated with a 50% hedge to the Canadian dollar. The total fund return is measured against the return of the asset mix policy benchmark. The difference between the endowment's return and the benchmark

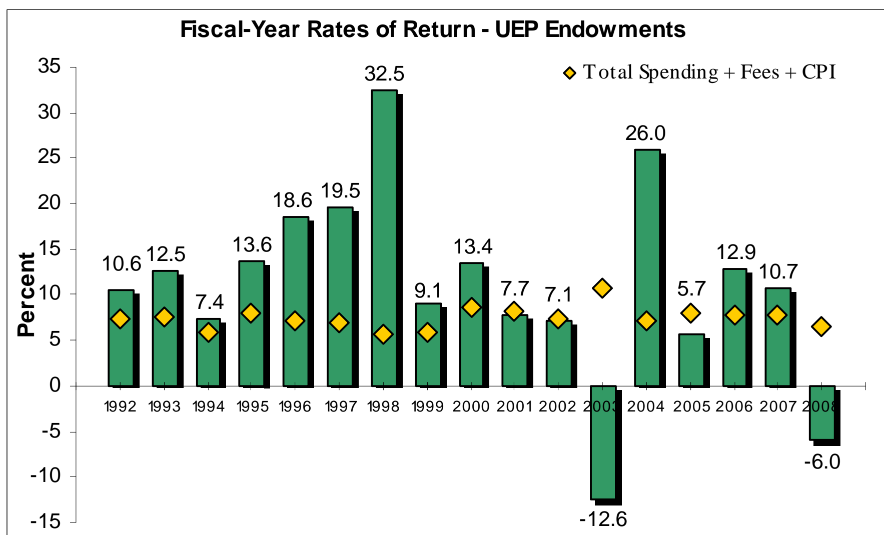
UEP Investment Policy Benchmark	Current	Target
DEX Universe Bond Index	20%	20%
DEX Real Return Bond Index	10%	0%
S&P/TSX Composite Index (Cap 10)	15%	15%
MSCI World Index 50% (Hedged to CAD)	55%	45%
Absolute Return (US 3 Month T-Bill + 6.0%)	0%	10%
Private Equity (Venture Economics Index)	0%	5%
Real Estate (IPD Index)	0%	5%
	100%	100%

return reflects the value added by strategic and investment policy allocation decisions together with active management by our investment managers. Please refer to Appendix 3 for details. The benchmark return for the endowment pool is calculated from the asset mix and the benchmark indices as outlined in the above table.

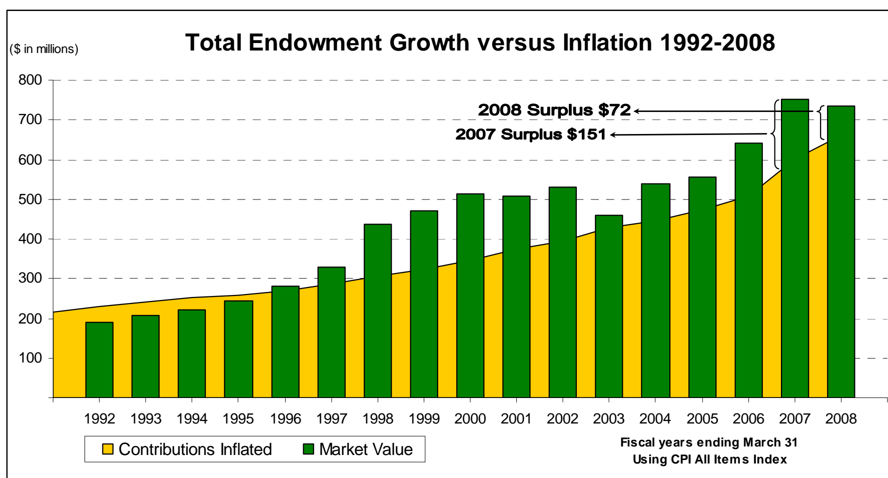
To assist the Investment Committee in its on-going assessment of the investment policy's effectiveness, the Committee monitors the performance of other similar, though not necessarily directly comparable, funds. It does so through participation in Mellon Analytical Solutions Canadian Master Trust Universe (CMTU), the Canadian Association of University Business Officers (CAUBO), and the U.S.A National Association of College and University Business Officers (NACUBO) endowment surveys.

Annual Endowment Fund Performance to March 31, 2008

The main objective of the endowment investment policy is the preservation of capital. This objective was not met in fiscal 2008 as the real value of the endowments decreased by 12.6%, comprised of the 6.0% loss plus all in expenditures of 5.2% and inflation of 1.4%.



As shown in the adjacent graph, the market value of the endowments continues to exceed the cumulative endowment contributions indexed for inflation by $72 million. This however represents a 52% decrease from the $151 million in 2007. A surplus is required to protect the real value of the endowment funds and enable a stable and predictable spending allocation in periods of poor investment performance.



There were three main factors behind the poor performance in the portfolio: Weak global equity markets, the continued appreciation of the Canadian dollar against the US dollar, and below benchmark performance by several of our active equity managers.

The US sub-prime mortgage crisis resulted in a contraction of credit and liquidity in the global financial sector. Central banks responded in a coordinated fashion by injecting liquidity on numerous occasions. The prospect of a US recession triggered by the housing sector coupled with the potential for commodity driven inflation led to fears of stagflation. Investors became concerned that a major slow down in the US economy would have a significant negative impact on the global economy. These concerns together with increased risk aversion resulted in losses for equities in most developed economies. The MSCI World Index posted a loss of 13.5% in Canadian dollar terms. The US and Europe, Australasia and Far East (EAFE) markets all posted double digit losses for the

year. Canada's equity market with its significant weighting in commodity based sectors was a notable exception with the S&P/TSX Composite posting a return of 4.0%. On the basis of the investment policy the UEP had a 49.2% allocation to foreign equities, higher than many Canadian endowment and pension funds. The overweight position in foreign equities hurt returns on both an absolute and relative basis.

The decision to partially hedge the portfolio to the Canadian dollar had a positive impact on the portfolio; adding 0.6% to overall performance this year. During the year the Canadian dollar appreciated by 11.5% and 11.4% against the US dollar and the Pound Sterling respectively, but depreciated by 4.6% and 5.2% against the Euro and Japanese Yen respectively. With a 55% target allocation to Non-Canadian securities, currency is a significant source of risk and volatility in the portfolio; and it is prudent to manage this risk. The active currency overlay managed by JP Morgan was not a source of added value in the fiscal year. The benchmark measured by a passive 50% hedge ratio gained 2.1% for fiscal 2008, while the actively managed currency overlay gained only 1.0% for the same period.

The majority of the University of Alberta's active, external managers, with the exception of Walter Scott & Partners, failed to add value to the portfolio in fiscal 2008. Overall the underperformance by active management in fiscal 2008 was 1.8%.

In the Mellon Analytical Services Canadian Master Trust Universe (CMTU), which is composed of Canadian institutional pensions, endowments, and foundations, the median fund lost 2.5%. Because of differing regulatory and operational constraints on these funds, their returns at any point in time are not strictly comparable to one another or to the U of A endowment fund. Nonetheless they do provide information on the relative performance of differing investment strategies. Within this universe the endowment's investment performance was ranked in the 97th percentile, while the benchmark return ranked in the 82nd percentile. This poor ranking is generally explained by the UEP's higher allocation to foreign equities relative to other Canadian endowment and pension funds and lower allocation to Fixed Income than most. Foreign equities posted significant losses in the fiscal year; while Canadian equities and Fixed Income recorded gains.

Annualized Return - UEP Endowments
Relative to Asset Class Benchmarks — **Year Ending March 31**

	1YR %	2YR %	3YR %	4YR %	5YR %	10YR %
Short Term Return	4.5	4.3	3.9	3.5	3.3	3.9
91-day Treasury Bill Return	*4.6*	*4.4*	*3.9*	*3.5*	*3.4*	*3.9*
Fixed Income (non-RRB)	5.5	5.4	5.1	5.0	6.1	6.1
DEX Universe Bond Index	*5.8*	*5.6*	*5.4*	*5.3*	*6.1*	*6.1*
Fixed Income (Real Return Bonds)	6.3	3.2	5.9	7.1	8.6	
DEX RRB Index	*6.4*	*3.2*	*6.0*	*7.1*	*8.7*	
Canadian Equity	-3.6	4.1	10.8	13.1	17.1	10.8
S&P/TSX Composite Index (Cap 10)	*4.0*	*7.7*	*14.2*	*14.1*	*18.5*	*9.9*
Foreign Equity Total	-14.7	-1.3	3.2	2.8	8.5	5.1
MSCI World Index	*-13.5*	*-0.4*	*4.3*	*3.8*	*8.4*	*1.7*
Non-North American Equity	-12.6	1.0	6.3	6.0	13.7	
MSCI EAFE Index	*-13.1*	*1.9*	*7.7*	*7.4*	*13.4*	
U.S. Equity	-17.7	-4.7	-1.0	-1.4	2.4	0.1
Standard and Poors 500 Index	*-15.6*	*-3.4*	*0.2*	*-0.3*	*3.6*	*0.2*
Absolute Return Strategies	*2.3*	*6.1*	*6.5*			
US T-Bills +6.0%	*10.9*	*11.0*	*10.5*			
Currency Overlay	1.0	*0.2*				
50% passively hedged benchmark	*2.1*	*0.4*				
Total Fund	-6.0	2.0	5.5	5.6	9.3	6.9
Benchmark Return	-4.2	2.6	6.3	6.1	9.7	5.7
CTU Median	-2.5	3.9	7.3	7.4	10.7	6.4
CPI Index	1.4	1.8	1.9	2.0	1.8	2.1

Annual Performance - UEP Endowments
Relative to Asset Class Benchmarks — **Years Ending March 31**

	2008 %	2007 %	2006 %	2005 %	2004 %
Short Term Return	4.5	4.1	3.0	2.3	2.7
91Day Treasury Bill	*4.6*	*4.2*	*2.8*	*2.2*	*3.0*
Fixed Income (non-RRB)	5.5	5.4	4.4	4.7	10.9
DEX Universe Bond Index	*5.8*	*5.5*	*4.9*	*5.0*	*10.8*
Fixed Income (Real Return Bonds)	6.3	0.1	11.7	10.7	15.0
DEX RRB Index	*6.4*	*0.0*	*11.8*	*10.7*	*15.3*
Canadian Equity	-3.6	12.3	25.5	20.5	34.3
S&P/TSX Composite Index (Cap 10)	*4.0*	*11.4*	*28.4*	*13.9*	*37.7*
Foreign Equity Total	-14.7	14.1	12.9	1.5	35.7
MSCI World Index	*-13.5*	*14.7*	*14.3*	*2.3*	*29.2*
Non-North American Equity	-12.6	16.7	17.9	4.9	52.3
MSCI EAFE Index	*-13.1*	*19.4*	*20.4*	*6.3*	*41.3*
U.S. Equity	-17.7	10.4	6.7	-2.4	18.6
Standard and Poors 500 Index	*-15.6*	*10.6*	*7.7*	*-1.8*	*20.7*
Absolute Return Strategies	2.3	10.1	7.2		
US T-Bills +6.0%	*10.9*	*11.1*	*8.5*		
Currency Overlay	1.0	-0.5			
50% passively hedged benchmark	*2.1*	*-1.3*			
Total Fund	-6.0	10.7	12.9	5.7	26.0
Benchmark Return	-4.2	9.9	14.2	5.5	25.2
CTU Median	-2.5	10.8	14.9	8.2	24.5
CPI Index	1.4	2.3	2.2	2.3	0.7

On a five-year basis the UEP returned 9.3% versus a CMTU median return of 10.7%. The relative underperformance of the UEP reflects the relative out-performance of Canadian equities versus foreign equities during the past five years in conjunction with the UEP's lower allocation to this market.

The University of Alberta participates in benchmark studies sponsored by the Canadian Association of University Business Officers (CAUBO) and the USA's National Association of College and University Business Officers (NACUBO). The most recent published data from these organizations is for the periods ending December 31, 2006 and June 30, 2007 respectively. The University of Alberta has had mixed performance versus the other 21 Canadian universities with assets greater than $100 million. The University's return of 13.0% for the one year ending December 31, 2006 ranks 17th of the 23 largest Universities in terms of assets under management in CAUBO survey, but the 10 year return of 10.6% is ranked second overall. Short-term results lagged due to the UEP's relatively lower allocation to Canadian equities.

The NACUBO survey results are similar. The University's returns lagged in the short-term as the 1 year return of 15.3% for the year ending June 30, 2007 ranked in the 4th quartile. However, over the long-term results are better as the University ranks in the second quartile for the 10yr period. The UEP 10yr return of 9.4% as of June 30, 2007 is ranked 127th overall of the 778 universities and colleges surveyed in the NACUBO study. NACUBO requests that Canadian Universities report their returns in Canadian dollar terms. The significant appreciation of the Canadian dollar makes direct comparisons problematic. The UEP returns expressed in US dollar terms ranked in the first quartile for all time periods surveyed, with a 1 year return of 20.5% ranking 77th and the 10 year return of 12.3% ranking 26th.

Spending Policy

For the year ending March 31, 2008, $33.0 million was made available from the Endowments to support program spending.

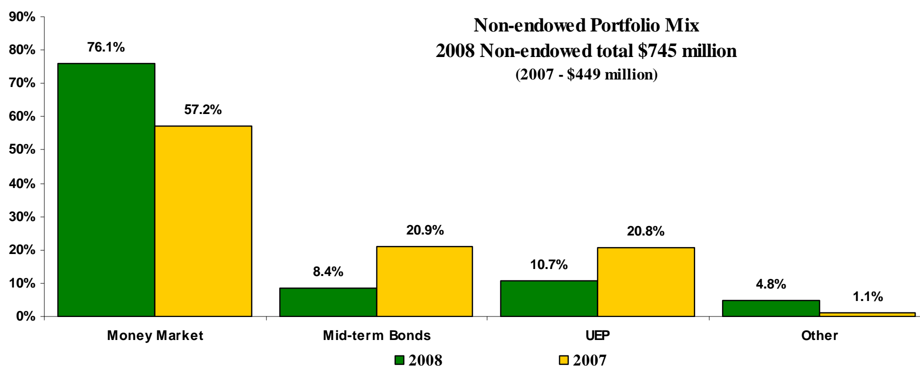
On April 1, 2004 the University implemented a Board of Governors approved long-term strategy to shift the endowment's spending model to a sustainable inflation indexed model with a spending rate maximum of 6.0% of market value and a spending rate minimum of 4.0% of market value. The move was required given that the effective rate of spending at the time exceeded the long-term real return expectation of 5.0%. Under this strategy, the shift is occurring gradually to limit the impact of spending allocation reductions on the programs being supported. The spending policy during the transition period will remain based on a 36-month average. The spending allocation is being gradually reduced from 5.0% to 4.25% over a 4-year period. The spending rate for fiscal 2008 was 4.65% and will be reduced to 4.45% for fiscal 2009. It had been forecast that this new spending policy would result in year-over-year declines in the spending allocation of approximately 3.0% in each of the years in the transition period. The 5-year annualized return of 9.3% for the period ending March 31, 2008 has had a favourable impact on the forecast year-over-year reductions. The spending allocation for the fiscal year ending March 31, 2008 remained unchanged from the previous year, while the spending allocation for fiscal 2009 will decline by 0.9%. Future investment returns will continue to impact the forecast reductions in the spending allocation for the fiscal year 2010.

Costs

The Administrative Fee totaled $3.1 million for fiscal 2008, representing 0.41% of average market value of the fund. The Administrative Fee supports indirect expenses incurred by central administration associated with the programs supported by the Endowments. Direct expenses were $3.2 million during the same period or 0.42% of the average market value of the fund. These expenses represent manager fees, custodial fees and other direct costs associated with the management of the endowment assets.

Non-Endowed Funds

The Non-endowed Investment Pool (NEIP) represents the University's operating, capital, and restricted funds, of which $567 million (2007 - $268 million) is held in money market instruments while the remaining $178 million (2007 - $181 million) is invested in bonds and equities.



The investment policy approved by the Board of Governors in June 2005 identified that only a portion of non-endowed funds are required for short-term cash flow management, with the remainder being available for medium to long-term investment strategies. The policy objective of the short and mid-term funds is to earn the highest return possible on investments that ensure the security of the invested capital. The majority of the short-term fixed income investments are managed by UBS Global Asset Management in their "Cash in Action" fund. It is expected that this fund will generate comparable returns but with a lower risk profile than could be achieved by the University. The fund is being used to meet the University's daily liquidity requirements, which has allowed the remainder of the short-term funds to be invested in longer-term high-quality treasury bills and bankers acceptances. The short and mid-term fixed income investments that are managed internally use a buy and hold to maturity strategy. Yield curve analysis, duration management, and credit quality are taken into account in the pre-trade fixed income analysis.

The non-endowed funds posted a loss of 2.8% for the year. Cash and cash equivalent money market funds comprised 76.1% or $567 million of the non-endowed funds at the end of the fiscal year. Of this amount $344 million is managed by UBS, which posted a return of 4.5% slightly underperforming the benchmark DEX 91 day T-Bill return of 4.6%. However in aggregate the short-term portion of the NEIP lost 2.3% as a result of a $41 million write down related to the University's $171 million asset backed commercial paper holdings (ABCP).

Asset Backed Commercial Paper (ABCP)

ABCP had been a component of the University's short-term investment program for over 5 years. The market for ABCP had functioned well without any settlement problems or credit downgrades. In August of 2007 a liquidity crisis for third party ABCP unfolded. This previously robust market collapsed due to investor concerns about the underlying exposure to US sub-prime mortgage assets in the affected 22 trusts with a total value of $32 billion. At the time the University's exposure to the affected ABCP was $171 million. This exposure represented approximately 20% of the total NEIP pool of $820 million. In addition to this the University held $39 million of bank sponsored ABCP in August of 2007. All ABCP holdings at the time of acquisition were rated R-1 high by the Dominion Bond Rating Service as required by the University's Investment Policy.

The scope and complexity of this liquidity crisis required an orderly restructuring process involving the cooperation of all market participants. In late August 2007 the University began participating in this process, by registering with the restructuring advisor and executing extraordinary note holder resolutions to effect a standstill period for the restructuring process. As events continued to evolve over the coming months, it was determined that a more active leadership role was in the University's best interests. In late October 2007 the University became a member of the Pan-Canadian Investors Committee for Third-party Structured Asset-Backed Commercial Paper that was overseeing the restructuring process. Since November of 2007 the University has participated extensively in the activities of this Committee. The restructuring process will result in the University holding floating rate notes with a long term to maturity which matches the underlying assets. The yield on these notes will be lower than the yield provided by other securities with comparable risk and duration characteristics.

The restructured ABCP notes will be held in the mid-term portion of the University's NEIP. Although it is expected that an active market for the restructured notes will evolve over time, it is possible that the restructured notes will be held to maturity. A comprehensive long-term cash flow forecast has been prepared and it was determined that the exposure to ABCP does not represent a liquidity issue for the University and all obligations and commitments will continue to be met.

Other Assets

Internally managed mid-term bonds with duration under 5 years comprise 8.4% or $63 million of the non-endowed funds; these bonds provided a return of 6.0%, which lagged slightly the benchmark DEX Short Term Bond index return of 6.4%.

At March 31, 2008 $80 million or 10.7% of the non-endowed funds was invested in the UEP, which lost 6.0% for the year.

Going Forward

Management with the direction of the Investment Committee will continue to implement the changes contemplated by the investment policy that was approved by the Board of Governors on November 2, 2007. This will include an assessment of the continued appropriateness of the current active Canadian equity mandates as well as manager searches in the following areas:

- An active Canadian fixed income mandate that can invest in global fixed income on an opportunistic basis for added value.
- An active core US Equity Manager that can invest across the market capitalization spectrum to enhance returns.
- Suitable investment opportunities in the alternatives asset class, including hedge fund of funds, private equity fund of funds as well as real estate.

The Investment Committee is also focusing on improved management of risk in the portfolio. The establishment of a risk budget for the UEP and its incorporation into the ongoing performance monitoring process will be investigated.

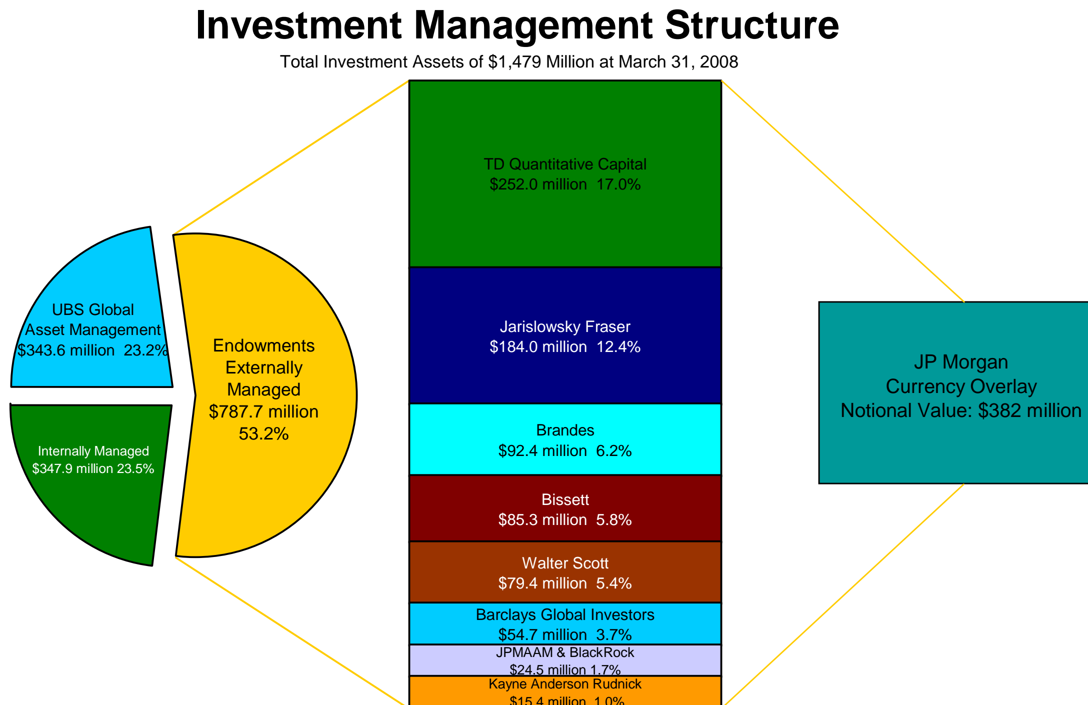
Board of Governors Investment Committee established October 1997.
Investment Committee Membership for the period June 2007 to June 2008:

Bob Kamp, Chair (external member)
Ken Bancroft (external member)
Fred Barth (external member)
Barbara Belch (external member)
Gordon Clanachan (Board member)
Jim Drinkwater, Vice-Chair (external member)
Lynne Duncan (external member)
Allister McPherson (external member)
Brian Heidecker (ex-officio)
Dr. Eric Newell (ex-officio)
Dr. Indira Samarasekera (ex-officio)

Prepared for Board Investment Committee
By Financial Services - Treasury

Appendix 1 - Investment Manager Structure

The University retains the services of ten external fund managers for the bond, equity and absolute return components of the endowment investment portfolio.



Barclays Global Investors has a Russell 1000 enhanced equity mandate. BGI uses a fundamental multi-factor quantitative model to provide returns in excess of the benchmark. This mandate is tightly risk-controlled as BGI strives to provide annual excess returns of 1-2% with an active risk of no more than 2.0%. BGI has been a fund manager for the University of Alberta since January 2007.

Bissett Investment Management has an active Canadian equity mandate. Bissett's approach is to identify companies that have good growth potential and are presently trading at reasonable prices. Bissett has been managing funds on behalf of the University since November 1998.

BlackRock Alternative Advisors (formerly Quellos Capital Management) has an absolute return strategy mandate. On October 1, 2007 BlackRock acquired the fund of funds business of Quellos Group, and merged it with BlackRock's existing fund of funds business. The University has invested in Q-BLK Strategic Partners II Ltd. which operates a hedge fund of funds product. Q-BLK Strategic Partners II invests in approximately 40 individual strategy funds run by managers outside of BlackRock. These different strategies seek to generate a return by capitalizing on market inefficiencies and include relative value, event driven, fundamental long/short, direct sourcing and directional trading strategies. BlackRock excludes certain strategies from their fund of funds, such as global macro and managed futures. As well, BlackRock seeks to identify and invest with new fund managers at an early stage to establish a long-term competitive advantage. This mandate was funded on January 1, 2005.

Brandes Investment Partners has an active international equity mandate that includes Europe, Australia, the Far East, and emerging markets. Brandes' style is that of a value manager, in which undervalued companies are identified and investments are made for future growth. Brandes has been a fund manager for the University since November 1998.

Jarislowsky Fraser Ltd. has an active, balanced mandate that includes bonds, Canadian equities and international equities. Jarislowsky Fraser's equity style can be described as a hybrid value/growth style that

focuses on a company's long-term fundamentals rather than on short-term events. Their fixed income style includes interest rate anticipation, yield curve management and sector rotation. Jarislowsky Fraser has been a fund manager for the University for more than 25 years.

JP Morgan Alternative Asset Management has an absolute return strategy mandate. The University of Alberta has invested in JPMAAM's Multi-Strategy Fund Ltd. which operates a hedge fund of funds product. The Multi-Strategy Fund invests in approximately 30 individual strategy funds run by managers outside of JPMAAM. These different strategies seek to capitalize on market inefficiencies which include relative value, opportunistic/macro, long/short equities, merger arbitrage/event driven, distressed securities and dedicated short selling strategies. JPMAAM selects well-established hedge fund managers with assets under management greater than $50 million. JP Morgan Alternative Asset Management's mandate was funded on January 1, 2005.

JP Morgan Asset Management has an active currency overlay mandate. JP Morgan uses both quantitative and qualitative measures to actively track seventeen different currency pairs. The manager uses a series of currency forward contracts to either increase or decrease the university's exposure to a certain currency, in the context of a strategic hedge ratio of 50% that is based on the UEP's actual exposure associated with its foreign equity holdings. The primary goal of the mandate is to manage the UEP's underlying currency risk exposure, with a secondary goal of return enhancement. The long-term objective for this mandate is to generate a 1.0% excess return over that of the strategic hedge ratio with a target tracking error of 2.0%. The mandate commenced on October 31, 2005.

Kayne Anderson Rudnick Investment Management LLC, has an active US small-mid cap equity mandate. Kayne Anderson Rudnick invests in high quality companies at a reasonable price, seeking to identify the next generation of blue chip companies through bottom up fundamental research focused on companies with an S&P rating of A- or better. Kayne Anderson Rudnick's mandate was funded on December 1, 2003.

TD Quantitative Capital has a passive U.S. equity S&P500 index mandate, a DEX Bond Universe index mandate, and a DEX Real Bond index mandate. In fiscal 2007 the University took a portion of the funds allocated to the Real Return bond mandate and invested it in the TD Emerald Short-term Income Fund. The University has been using the services of TD Quantitative Capital since 1996.

Walter Scott & Partners Limited has an active international equity mandate that includes Europe, Australia, and the Far East. Walter Scott seeks to invest in companies capable of sustaining an internal rate of return growth above 20% per annum. Walter Scott's mandate was funded on July 1, 2003.

UBS Global Asset Management has an active Canadian money market mandate. Utilizing their internal global credit team UBS seeks to add value by interest rate anticipation, sector allocation, yield curve management, and security selection. UBS was first funded on April 25, 2007.

Appendix 2 - Investment Performance by Asset Class

Balanced Manager Performance

Jarislowsky Fraser's loss for the year of 7.5% fell short of their benchmark loss of 4.8%. Since 2007 Jarislowsky Fraser has been tactically reducing their allocation to fixed income and reallocating funds to US and EAFE equities. This shift in asset allocation detracted from performance as both asset classes substantially underperformed Canadian fixed income. Performance within Canadian fixed income was also hurt by a higher than benchmark weight to corporate bonds, which underperformed government bonds. The loss on foreign equities was in line with the overall benchmark: outperformance in US equities was offset by underperformance in EAFE equities. In Canadian equities, Jarislowsky was below the benchmark return due to an underweight allocation to the two best performing sectors, materials and information technology, and an overweight allocation to consumer staples and discretionary sectors, both of which were among the poorest performers.

Individual Asset Class Performance
Fixed Income

Fixed income includes publicly traded Canadian bonds, a Canadian bond index pool, real return bonds and privately issued mortgages. Currently 55.8% of the fixed income allocation is in the TD Emerald Canadian Index bond fund. The TD Emerald Real Return Bond Fund accounts for another 24.5%. Jarislowsky Fraser manages 18.1% of the bond portfolio, while the remaining 1.6% was managed internally. The overall fixed income portfolio returned 5.6% versus the UEP Fixed Income benchmark of 6.0%.

Top 10 Canadian Fixed Income Holdings

Company	Market Value ($ millions)	% of CDN Bonds	% of Portfolio
Gov't of Canada RRB 4.00% 01-DEC-2031	11.81	4.7%	1.5%
Gov't of Canada RRB 4.25% 01-DEC-2026	10.80	4.3%	1.3%
Gov't of Canada RRB 4.25% 01-DEC-2021	10.67	4.2%	1.3%
Gov't of Canada RRB 3.00% 01-DEC-2036	9.32	3.7%	1.2%
Gov't of Canada 5.75% 01-JUN-2029	3.98	1.6%	0.5%
Gov't of Canada 4.00% 01-JUN-2017	3.93	1.6%	0.5%
Canada Housing Trust 4.55% 15-DEC-2012	3.56	1.4%	0.4%
Gov't of Canada 5.75% 01-JUN-2033	3.33	1.3%	0.4%
Gov't of Canada 8.00% 01-JUN-2023	3.06	1.2%	0.4%
Gov't of Canada 4.25% 01-DEC-2009	2.90	1.2%	0.4%

Bonds

Canadian bond rates of return for the endowments were 5.4% for the fiscal year. This return trailed the DEX Bond Universe return of 5.8% but exceed the RMCTU median of 5.2%. After raising interest rates once at the beginning of the fiscal year, the Bank of Canada, in response to the credit crisis, began to reduce the overnight rate from 4.50% to 3.50% as at March 31, 2008. The yield curve in both Canada and the US moved from flat or inverted at the beginning of the year to upwardly sloping at the end of the fiscal year.

Jarislowsky Fraser underperformed the benchmark with a return of 4.3%. Jarislowsky targets the corporate credit market to add value to the portfolio. The credit crisis resulted in a general widening of corporate spreads and led to a flight to quality government bonds which negatively impacted performance. The index return for corporate bonds of 2.8% fell well short of 7.7% return for Government of Canada bonds and 5.9% return for Provincial Government bonds. While Jarislowsky was able to add value through corporate bond selection with a return of 3.5% it was insufficient to make up for shortfall resulting from the over allocation to this sector of the bond market.

The TD Emerald Canadian Bond Index Fund is indexed to the DEX Bond Universe and essentially tracked the benchmark with a return of 5.8%.

Real Return Bonds

Real return bonds are bonds that pay a rate of return that is adjusted for inflation. Unlike regular (nominal) bonds, this feature ensures that purchasing power is maintained regardless of the future rate of inflation. The real return bond fund investment strategy is to invest in Canadian issued bonds that are selected and weighted mathematically to approximate the overall risk and return characteristics of the DEX Real Bond Index. The fund invests in federal and provincial real return bonds and debentures with a minimum A credit rating requirement for the purchase of individual securities. For the year ending March 31, 2008 the DEX Real Bond Index was returned 6.4%. The TD Asset Management Portfolio was slightly behind the index with a return of 6.3%. The real return bond yield decreased from 1.76% to 1.60% during the year which contributed towards absolute performance. Real return bonds began the fiscal year with a break even inflation rate of 2.44% and ended the year at 2.33%. Priced in, this accounts for the under performance of real return bonds to nominal long Government of Canada bonds, which returned 8.0%.

In September 2006, the committee decided to reduce the UEP's allocation to Real Return bonds. The high demand for these bonds by Canadian pension funds has created a supply/demand imbalance which has skewed returns for the asset class. This imbalance reduced the bonds inflation hedging attributes. Due to significant positive past performance and a concern about the ability of the bonds to provide ongoing inflation hedging, the Investment Committee reduced the allocation by one-third to 6.5% of the UEP. The allocation to real return bonds will be eliminated as the new investment policy is implemented.

Canadian Equity Component

The Canadian equity portfolio lost 3.6% for the period compared to gains of 4.0% for the Canadian equity benchmark S&P/TSX Composite Index, and 1.0% for the CMTU median. The Canadian market remains highly concentrated with 75.5% of the index composed of three sectors: Financials (29.2%), Energy (28.0%) and Materials (18.3%). The heavy concentration in commodity based sectors combined with continued strong global demand for commodities resulted in the Canadian market posting a modest return. Canada was one of the very few developed markets to record a gain for the year ending March 31, 2008. Returns within the Canadian market were extremely concentrated, with Research in Motion, Potash Corporation of Saskatchewan, Alcan and Encana accounting for most of the index return. This highly concentrated market made it difficult for active management strategies to outperform the benchmark index.

Top 10 Canadian Equity Holdings

Company	Market Value ($ millions)	% of CDN Equities	% of Portfolio
Manulife Financial Corporation	6.04	4.8%	0.8%
Royal Bank of Canada	5.59	4.5%	0.7%
EnCana Corporation	5.46	4.4%	0.7%
Bank of Nova Scotia	5.30	4.2%	0.7%
Canadian National Railway Co.	5.11	4.1%	0.6%
Toronto Dominion Bank	4.95	3.9%	0.6%
Power Financial Corporation	3.93	3.1%	0.5%
Talisman Energy Inc.	3.76	3.0%	0.5%
Thomson Reuters Co.	3.66	2.9%	0.5%
Suncor Energy Inc.	3.25	2.6%	0.4%

Jarislowsky Fraser's Canadian equity portfolio gained 0.5% but was below the benchmark. Successful stock selection in five of the nine sectors that the manager was invested in helped returns. But this was more than offset by underweight positions in the two best performing sectors, Materials and Information Technology and overweight positions in the Consumer Discretionary and Consumer Staples sectors, which were among the poorer performers.

For fiscal 2007, Bissett's loss of 5.6% significantly trailed the benchmark by 9.6%. Bissett's focus on non-cyclical stocks resulted in a significant underweight to the Materials sector. Increasing commodity prices resulted in significant share price appreciation for stocks in this sector. Bissett seeks to acquire growing companies at a reasonable price. Most stocks within this sector failed to meet Bissett's valuation criteria. The manager finished

the year with only a 1.4% allocation to Materials versus a 18.3% weighting in the Index. This, combined with poor stock selection in the sector significantly hurt relative performance. An underweight allocation to a strong performing Information Technology sector and an over allocation to the poor performing Consumer Staples and Financial sectors were also negatives.

Foreign Equity Component

The foreign equity component is comprised of U.S. equities and units in three Europe, Australasia, Far East, and emerging market (EAFE) funds. The endowment's foreign equity component posted a loss of 14.7% compared to the benchmark Morgan Stanley Capital International Composite World Index which lost 13.5% for the year. The endowments also failed to better the CMTU median loss of 13.7%. These returns can be further broken down into their US and Non-North American components.

Top 10 Foreign Equity Holdings

Company	Market Value ($Cdn millions)	% of Foreign Equities	% of Portfolio
Exxon Mobil	5.28	1.3%	0.7%
GlaxoSmithKline	4.98	1.3%	0.6%
Nestlé	4.23	1.1%	0.5%
Ericsson	3.87	1.0%	0.5%
General Electric	3.81	1.0%	0.5%
Procter & Gamble	3.74	0.9%	0.5%
Woodside Petroleum	3.41	0.9%	0.4%
Deutsche Telekom	3.35	0.8%	0.4%
Mitsubishi UFJ Financial Group	3.32	0.8%	0.4%
Essilor International	3.28	0.8%	0.4%

Jarislowsky Fraser's foreign equity portfolio had a loss of 14.0%, slightly lower than the MSCI World Index. The US equity component of the Jarislowsky Fraser foreign equity portfolio had a positive relative return with a loss of 14.1% compared to the S&P 500 loss of 15.6%. On the EAFE side, Jarislowsky Fraser underperformed, posting a loss of 13.9% against the MSCI EAFE benchmark loss of 13.1%. Jarislowsky Fraser concentrates on large-cap, non-cyclical stocks in their portfolios. All sectors in the US market, with the exception of Energy, posted losses for the year. The manager was well positioned to take advantage of the market turning towards more defensive stocks. Stock selection and an overweight allocation to the better performing Consumer Staples sector helped performance, while an underweight position in Materials detracted. Similar conditions prevailed in the EAFE market where the only sector to post a positive return was the Materials sector. Jarislowsky's performance in the EAFE market was negatively impacted by the fact that losses amongst the very large-cap names were generally higher than the overall index given their greater exposure to a potential US economic slowdown. Several stock specific issues also hurt performance.

The Non-North American (EAFE) equity mandate managed by Brandes Investment Partners had a loss of 17.8%, which trailed the MSCI EAFE Index loss of 13.1%. The value investing style employed by Brandes was out of favor during this past year. During the year the MSCI EAFE Value index lost 17.1% while the corresponding growth index lost only 9.0%. Brandes attributes their underperformance primarily to stock selection. Country and sector allocations are for the most part a function of their bottom up stock selection process. Country allocation and stock selection within countries impeded performance in all but the emerging market countries. From a sector perspective, their overweight allocation to Telecommunications helped returns but this was offset by an underweight allocation to the Materials sector. Poor stock selection in nine of the ten sectors in which the manager was invested in hurt returns especially in the Information Technology (3.3%) and Health Care (1.3%) sectors.

Walter Scott & Partners' EAFE mandate posted a loss of 7.4% for fiscal 2008, which bettered the MSCI EAFE by 5.7%. The growth style employed by Walter Scott was in favor this past year. The manager focuses on companies that they view to have the potential to grow in excess of 20% per year. Walter Scott believes that China offers the highest growth potential but that there are too many risks associated with direct investment in China. Therefore, the manager looks mainly to Asian companies that have significant business dealings in China.

Walter Scott has maintained an overweight position in Asian stocks, with the portfolio having a 37.5% allocation to Japan and 13.0% to Hong Kong as of March 31, 2008. Although Hong Kong was one of the very few developed markets, other than Canada, to post a positive return of 1.3% for the year, Japan was one of the weakest performing markets with a loss of 24.1%. Walter Scott's strong relative performance this year is primarily attributable to their stock selection process.

The Barclays Global Investors (BGI) Russell 1000 Alpha Tilts mandate lost 19.7%, which trailed the benchmark loss of 15.9% by 3.8%. BGI uses a tightly risk-controlled quantitative fundamental model, which is optimized daily, to take slight overweight and underweight positions in approximately 400 securities. The model is market neutral, meaning that the composition of the portfolio matches that of the Russell 1000 in terms of Beta exposure and sector and industry allocation. The target for this portfolio is to provide 1-2% added value over the index with no more than a 2% tracking error. The significant under performance for this mandate is entirely due to stock selection and the fact that BGI's value and quality quantitative signals simultaneously failed to add value. In the past 10 years such simultaneous failure has only happened in 14 months of which 7 were concentrated in the current fiscal year. During the first part of the year, the lack of risk aversion amongst investors contributed towards growth stocks (-11.7%) out performing value stocks (-20.0%). This differential was greater than during the 1999 technology bubble, but impacted a broader array of industries, and BGI's model was unable to react in a manner that would add value. The strategy was put under further pressure during the credit crisis, as technical selling pressures facing hedge funds drove the value of underweighted stocks up as short positions were being unwound, and put downward pressure on value of over-weighted stocks as they were sold to cover short positions.

The U.S small to mid-cap equity portfolio, managed by Kayne Anderson Rudnick, lost 26.1% for the fiscal year versus the benchmark Russell 2500 index loss of 21.1%. Kayne Anderson Rudnick invests in high quality companies at a reasonable price, seeking to identify the next generation of blue chip companies through bottom up fundamental research focused on companies with an S&P rating of A- or better. With the slow down in the US economy and widening credit spreads, investors began shifting towards higher quality stocks. This benefited the strategy in the first half of the fiscal year. The underperformance for the year is attributable to stock selection in the fourth quarter as company specific issues in the Financials, Materials and Energy sector weighed on performance.

The S&P 500 Index portfolio managed by TD Quantitative Capital lost 15.6% for fiscal 2008 matching the S&P 500 benchmark loss of 15.6%.

Alternative Asset Component

JPMAAM under-performed for the fiscal year with a return of 3.5% against a target US T-Bills + 6% return of 10.9%. Although the mandate fell short of its target return, it outperformed both the HFRI Fund of Funds Conservative index return of 1.5% and the HFRX Global Hedge Fund index which lost 0.2%. JPMAAM reported the largest positive contribution from relative value and dedicated short selling strategies. The only strategy to hurt absolute performance was merger arbitrage. Merger arbitrage was challenged as widening credit spreads place pressure on announced leveraged buy outs and resulted in a reduced opportunity set. JPMAAM believes going forward that relative value and credit strategies will offer the best opportunities. Specifically, they plan to focus on niche and volatility based relative value strategies as well as on credit managers that seek to extract value from distressed sub-prime mortgages and asset backed securities. They have a negative view on both the opportunistic macro and merger arbitrage space.

Blackrock under-performed their target return of 10.9% with a return of 1.1%. The mandate did however perform in line with the HRFI Fund of Funds Conservative index return of 1.5%. While all underlying strategies contributed towards absolute performance, the amounts were all small. Relative value strategies while contributing the most to returns came under pressure as the credit crisis resulted in margin calls for many hedge funds that forced an unwinding of trades in a falling market. This placed even more downward pressure on asset values. Blackrock believes that this market environment has created many profitable entry points for astute managers going forward. Event driven strategies disappointed as financing execution risk resulted in declining

merger and acquisition activity. Distressed credit strategies also came under pressure as credit spreads widened. Going forward, Blackrock sees good opportunities in the credit space and in direct sourcing as banks are unable to finance transactions while they repair their balance sheets. Hedged direction strategies disappointed given the fact that most managers have a net long bias and equity markets retreated significantly. Blackrock continues to focus on discovering new talent in the hedge fund space and believes that they will be able to continually access new value-adding strategies, especially if investment banks begin to scale back their proprietary trading operations.

Currency Overlay

The notional asset value of the JP Morgan active currency mandate is based on the UEP's actual exposure to foreign currency. With a 55% target allocation to non-Canadian securities, currency is a significant source of risk that must be managed. The overlay program finished the fiscal year with a notional value of $382 million. The strategic hedge ratio of 50% added 85 basis points to the UEP's benchmark performance as the Canadian dollar appreciated in value against several major currencies, including the US dollar, during fiscal 2008. The overlay account added 60 basis points to the fund's performance and gained 1.0% on the year against a benchmark return of 2.1%. This underperformance is primarily attributable to a long position in the US dollar when the Canadian dollar continued to appreciate against the US dollar. JP Morgan's model had signaled that the Canadian dollar was over-valued from a purchasing power perspective. The Canadian dollar did eventually pull back from its peak value against the US dollar. Value added on Japanese Yen, Swedish Krona and Australian Dollar positions were offset by losses on positions related to the Euro and the Pound Sterling.

Appendix 3 - Long-Term Value Added

The graph below depicts the UEP's return in excess of the benchmark return since inception. The benchmark has varied over time as changes have been made to the UEP's investment policy. This graph demonstrates that active management strategies have successfully added value over the longer term. Active management strategies failed to add value in fiscal 2008.

The yellow bars depict annual performance in relationship to the benchmark. The green line annualizes these amounts over a moving four-year period. The red line represents the cumulative value added since inception. The black diamond single point marks the ten-year annualized value added.