UNIVERSITY OF ALBERTA

INVESTMENT COMMITTEE REPORT TO THE BOARD OF GOVERNORS

For the Year Ended March 31, 2005

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

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The investment assets of the University of Alberta that are under the governance of the Investment Committee had a total market value of $964 million (2004 - $885 million) as of March 31, 2005. Of this amount, $586 million (2004 - $568 million) relates to endowments, while the remaining $378 million (2004 - $317 million) relates to non-endowed funds.

Endowment Funds - Key Points

- The market value of the endowments increased by $18 million to $586 million. The increase was comprised of investment earnings of $31 million and new donations of $18 million, less spending allocations and administrative expenses of $31 million.
- The Unitized Endowment Pool (UEP) investment portfolio had a return of 5.7% for the year ending March 31, 2005. This return compares favorably to the benchmark return of 5.5% but represents a much lower return than the gain of 26.0% in the prior year. Higher commodity prices, while favorable for the Canadian equity market, had a negative impact on most foreign markets. The appreciation of the Canadian Dollar further reduced returns from foreign equities.
- The excess of endowment market values over contributions indexed for inflation was $112 million, compared with an excess of $124 million the previous year. Despite this decline, the excess remains strongly positive. The Investment Committee concluded, during its 2003 spending policy review, that an "all in" spending rate of 4.75% was best aligned with the portfolio's expected long-term rate of return after inflation. This expected rate of return is in line with the endowments' actual seven-year annualized rate of return after inflation of 5.2%.
- The Investment Committee will continue to focus on a balanced approach to grow the endowments through portfolio diversification of the asset mix and fund management with an emphasis on equities. This is outlined in the investment policy approved by the Board of Governors in June 2004. The portfolio structure of the UEP continued to add value of 0.2% in 2004-05. For the ten years ended March 31, 2005, the UEP has returned 11.9% annualized; this represents a long-term annualized added value of 1.7% over the benchmark return of 10.2%.
- The Investment Committee continues to implement the portfolio structure contained in the Investment Policy.
  - Two "absolute return strategy" managers were funded with $10 million each in January 2005 to further diversify the endowment portfolio. Both Quellos Capital Management and JP Morgan Alternative Asset Management (JPMAAM) manage hedge fund of fund products, which invest with multiple managers across a broad range of strategies. The objective for "absolute return strategy" managers is to reduce the overall volatility of the fund, while generating returns that are commensurate with the return objectives for the UEP.
  - The reduced long-term return expectations and the higher allocation to foreign equities have highlighted the fact that the endowments' foreign currency exposure is a risk that needs to be actively managed. The Investment Committee is currently searching for an active currency overlay manager to hedge the UEP against an appreciating Canadian Dollar, while still participating in the gains associated with a depreciating Canadian Dollar.
  - In response to the reduced long-term return expectations from traditional investments, the Investment Committee plans to fund other alternative investment strategies such as Private Equity to enhance returns.

Non-Endowed Funds - Key Points

The non-endowed funds have increased by $61 million to $378 million, and returned 3.2% for the year versus the benchmark return of 3.5%. The funds were mainly invested in high quality, liquid money market products ($200 million, with a return of 2.3%), bonds with a duration of less than five years ($76 million, with a return of 2.5%), and the UEP ($90 million, with a return of 5.7%).

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 endowment investment performance. The Investment Committee forwards to the Board an annual investment review. The Investment Committee 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 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. All 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

The endowment investment policy objective 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 spending policy rate plus inflation over time within an acceptable level of risk.

Portfolio diversification is used to help ensure that the endowment investment objectives are met. Diversification is achieved through the following strategies:

- The asset mix policy has established allocations to fixed income products for income, and to equities and alternative assets for growth.
- The allocation within equities between Canada, the United States of America and other international capital markets diversifies market specific risk.
- The allocation of funds amongst different fund managers diversifies manager style risk. Please refer to Appendix 1 for details.
- The allocation of funds between both active and passive investment approaches controls active management risk.

UEP Endowment Asset Mix as at March 31, 2005

	Policy Range Min.-Max. %	2005 Actual Asset Mix	2004 Actual Asset Mix
Fixed Income			
Money Market Securities	-5 - 10	2.1%	1.5%
Bonds, Debentures, Real Return Bonds	20 - 40	28.1%	30.3%
Total	20 - 40	30.2%	31.8%
Equity			
Canadian Equity	10 - 20	15.3%	14.8%
Foreign Equity	40 - 60	51.4%	53.2%
Alternative Assets	0 - 10	3.1%	0.2%
Total	60 - 80	69.8%	68.2%

Investment Performance
Measuring Performance of Endowment Funds

The returns of individual asset classes in the Fund are measured against established market benchmarks, such as the Scotia Capital (SC) Universe Bond Index, the Scotia Capital Real Return Bond (SC RRB) Index, the S&P/TSX Composite Index capped at 10% for any one security, and the Morgan Stanley Capital International World Index. The total fund return is measured against the benchmark asset mix policy return. The difference between the endowment's return and the benchmark 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 adjacent table.

UEP Investment Policy Benchmark

	2005	**2004**
91-Day Treasury Bill Return	0%	0%
Scotia Capital Universe Bond Index	20%	20%
Scotia Capital Real Return Bond Index	10%	10%
S&P/TSX Composite Index (Cap 10)	15%	15%
MSCI World Index	55%	55%
	100%	100%

The performance is also measured against that of other funds through participation in the Russell/Mellon Analytical Services Canadian Trust Universe (RMCTU), the Canadian Association of University Business Officers (CAUBO), and the National Association of College and University Business Officers (NACUBO) endowment surveys. The Investment Committee uses these universes as reference points to monitor whether or not the University's endowment investments have achieved competitive rates of return.

Annual Endowment Fund Performance to March 31, 2005

The University's endowment investments returned 5.7% for the year ending March 31, 2005. This compares favorably with the benchmark return of 5.5%. Two themes dominated fiscal 2005: escalating commodity prices, in particular oil, and the appreciation of the Canadian Dollar against most major currencies.

High oil prices had mixed effect on the Canadian economy and the University's endowment funds. The Canadian Energy sector posted an extremely strong return (43.6% annual return as of March 31, 2005). Many of the active managers in the UEP took advantage of this by overweighting the Energy Sector. However, transportation and manufacturing companies were hurt by the high cost of fuel.

The U.S. Dollar continued to depreciate against the Canadian Dollar, falling 7.7% for the year ending March 31, 2005. The Canadian Dollar appreciation put pressure on most sectors of the economy as Canadian exports became relatively less competitive.

The fund's Canadian equity managers contributed a positive 87 basis points to overall performance against the benchmark. Underperformance by active managers with Canadian fixed income and foreign equity mandates detracted 12 and 48 basis points respectively. Cash positions during the year detracted 7 basis points. This resulted in a slight out performance against the overall benchmark of 20 basis points (0.2%). Please refer to Appendix 2 for a detailed discussion of performance by asset class.

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

	2005 %	2004 %	2003 %	2002 %	2001 %
Short Term (Avg. Yield 00-02)	2.3	2.7	2.7	3.7	5.7
91Day Treasury Bill (Avg. Yield 00-02)	2.2	3.0	2.7	3.1	5.4
Fixed Income (non-RRB)	4.7	10.9	9.2	4.9	9.7
SC Universe Bond Index	5.0	10.8	9.2	5.1	8.7
Fixed Income (Real Return Bonds)	10.7	15.0			
SC RRB Index	10.7	15.3			
Canadian Equity	20.5	34.3	-15.6	13.9	3.1
S&P/TSX Composite Index (Cap 10)	13.9	37.7	-17.6	5.2	-8.9
Foreign Equity Total	1.5	35.7	-30.7	3.0	9.7
MSCI World Index	2.3	29.2	-29.8	-3.1	-18.3
Non-North American Equity	4.9	52.3	-30.9	2.6	6.8
MSCI EAFE Index	6.3	41.3	-29.0	-7.3	-19.6
U.S. Equity	-2.4	18.6	-30.7	4.0	15.6
Standard and Poors 500 Index	-1.8	20.7	-30.6	1.4	-14.8
Total Fund	5.7	26.0	-12.6	7.1	7.7
Benchmark Return	5.5	25.2	-12.7	2.6	-4.8
CTU Median	8.2	24.5	-10.6	5.4	-1.0
CPI Index	2.3	0.7	4.3	1.8	2.5

In the Russell/Mellon Analytical Services Canadian Trust Universe (RMCTU), composed of Canadian institutional pensions, endowments, and foundations, the median fund returned 8.2%. The Canadian dollar appreciation affected the University's portfolio more severely than it did the RMCTU median. This is because the RMCTU is heavily influenced by pension plans, many of which have higher allocations to Canadian equities and fixed income, and lower foreign equity exposure than does the UEP. To illustrate this point, the asset mix of the median RMCTU fund as of March 31, 2005 was 57.6% equities and 42.4% fixed income and cash. This asset mix is substantially more conservative than the UEP's target allocation of 70.0% to equities and 30.0% to fixed income. As well, the median RMCTU portfolio had a foreign equity allocation of less than 30.0% while the UEP's foreign equity exposure was 51%.

The endowments' 5.7% return placed it in a fourth quartile ranking in the RMCTU. This is largely attributable to our relatively heavier weighting to the global equity asset class which performed poorly this year. It should also be noted that the RMCTU quartile breaks for the year ending March 31, 2005 were fairly compressed with only 1.8% separating the first and fourth quartile breaks. In previous years the performance dispersion between the top and bottom quartiles was approximately 4.0%. On a five-year basis the endowment returned 6.1% versus an RMCTU median return of 4.7%. On this five-year basis the endowment's performance is within RMCTU's top 25% of all funds surveyed.

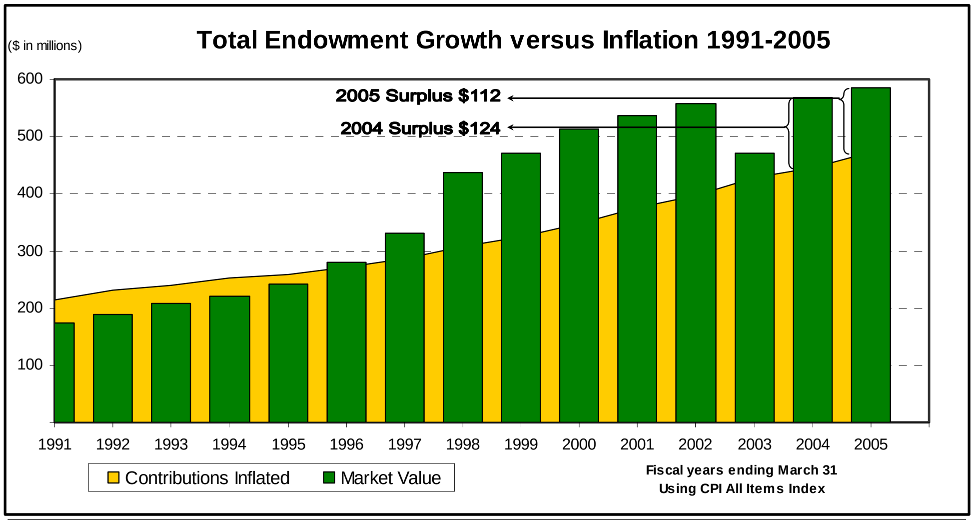
The University of Alberta participates in benchmark studies sponsored by CAUBO and NACUBO. The most recent published data from these organizations is for the periods ending December 31, 2003 and June 30, 2004 respectively. The University's return of 12.0% for the one year ending December 31, 2003 ranks in the second quartile of the CAUBO survey, the annualized ten year return of 11.8% positions the endowment in the first quartile and is ranked 2nd overall of the 73 Canadian Universities surveyed. The University's returns rank in the first quartile of all periods surveyed in the NACUBO study. The UEP ranked 30th overall of 747 U.S. universities for its ten year annualized return of 12.9% as of June 30, 2004.

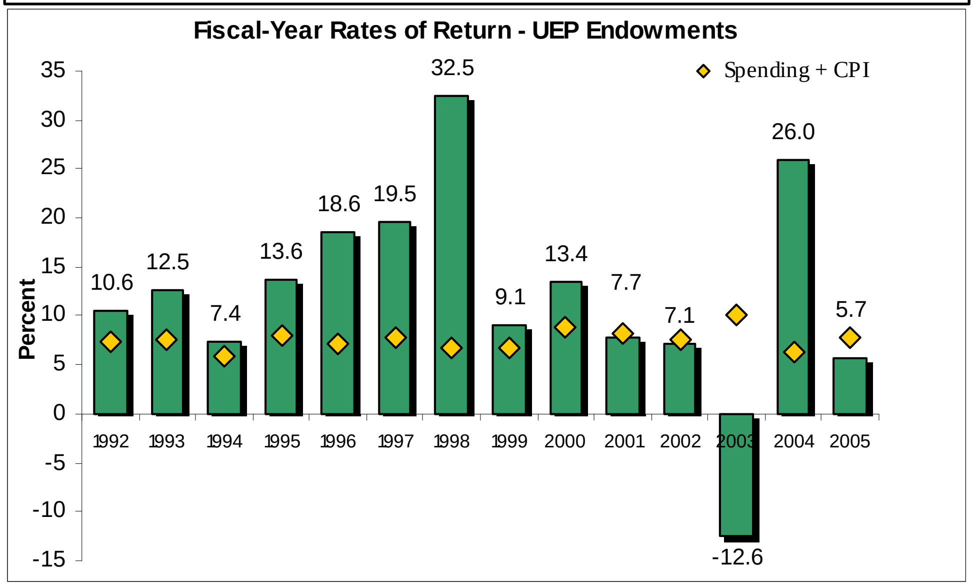
Annualized Return - UEP Endowments
Relative to Asset Class Benchmarks
Year Ending March 31

	1YR %	2YR %	3YR %	4YR %	5YR %
Short Term Yield	2.3	2.5	2.5	2.8	3.4
91-day Treasury Bill Yield	2.2	2.6	2.6	2.9	3.5
Fixed Income (non-RRB)	4.7	7.7	8.2	7.4	7.8
SC Universe Bond Index	5.0	7.9	8.3	7.5	7.7
Fixed Income (Real Return Bonds)	10.7	12.8			
SC RRB Index	10.7	13.0			
Canadian Equity	20.5	27.2	10.9	11.7	9.9
S&P/TSX Composite Index (Cap 10)	13.9	25.2	8.9	8.0	4.4
Foreign Equity Total	1.5	17.4	-1.5	-0.4	1.5
MSCI World Index	2.3	14.9	-2.5	-2.5	-6.0
Non-North American Equity	4.9	26.4	3.3	3.2	3.9
MSCI EAFE Index	6.3	22.6	2.2	-0.2	-4.4
U.S. Equity	-2.4	7.6	-7.1	-4.4	-0.7
Standard and Poors 500 Index	-1.8	8.9	-6.3	-4.4	-6.7
Total Fund	5.7	15.4	5.2	5.7	6.1
Benchmark Return	5.5	14.9	4.8	4.3	2.4
CTU Median	8.2	16.0	6.4	6.1	4.7
CPI Index	2.3	1.5	2.4	2.3	2.3

The main objective of the endowment investment policy is the long-term preservation of capital. This objective was not achieved this past year as the inflation adjusted return was 3.4%. The real value of the endowments decreased by 2.1%; comprising the 5.7% return less the 5.0% spending allocation, less the 0.50% administrative fee and less inflation of 2.3%. The five-year annualized inflation adjusted real rate of return was 3.8% and reinforces the continued relevance of the spending policy changes that were implemented this year.

As shown in the adjacent graph, the market value of the endowments currently exceeds the cumulative endowment contributions indexed for inflation by $112 million. This represents a decline of $12 million from 2004, but stands $80 million above the low point at the end of 2003. The current year's position is consistent with the Board's policy objective of providing stable funding in real terms over time to current and future generations while seeking growth in the real value of the fund.





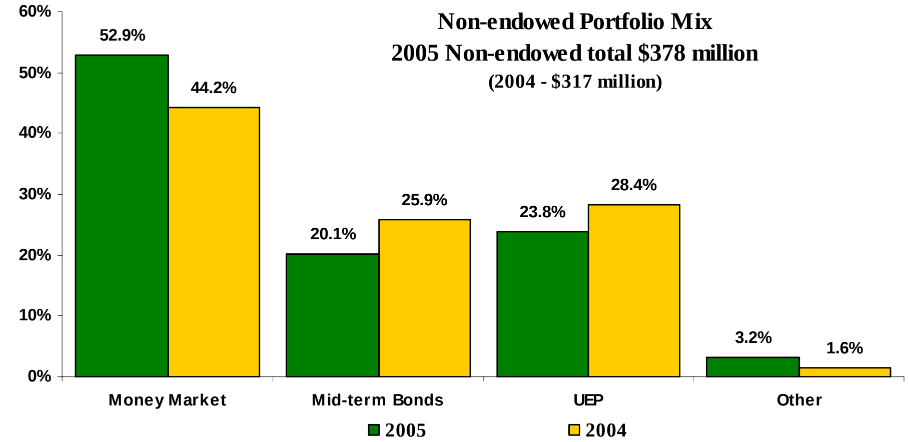
Spending Policy

On April 1, 2004 the University implemented a Board of Governors approved long-term strategy to shift the endowment's spending model to an inflation indexed model subject to a 6.0% maximum and a 4.0% minimum of market value. The move was required given that the current effective rate of spending significantly exceeds the long-term real return expectation. Under this strategy, the shift will occur 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 the 36-month averaging rule. This past fiscal year, the administrative fee was reduced from 0.75% to 0.50%. The spending allocation will be gradually reduced from 5.0% to 4.25% over a 4-year period commencing in the fiscal year ending March 31, 2007. 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 next 6 years. The extremely strong return of 26.0% for the fiscal year ending March 31, 2004 has had a positive impact on the forecast year over year declines which are now estimated to range between 1.1% and 3.0%. Future investment returns will continue to impact these forecast reductions in the spending allocation.

Non-Endowed Funds

The Non-endowed Investment Pool (NEIP) represents the University's operating, capital, and restricted funds, of which $200 million (2004 - $140 million) is held in money market instruments while the remaining $178 million (2004 - $177 million) is invested in bonds and equities.

The investment policy approved by the Board of Governors in June 2004 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 short and mid-term fixed income investments are currently managed internally, using 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 return on the non-endowed funds was 3.2% for the year. Cash and cash equivalent money market funds comprised 52.9% or $200 million of the non-endowed funds at the end of the fiscal year. These funds provided a return of 2.3%, which exceeded the benchmark Scotia Capital 91 day T-Bill return of 2.2%.

Internally managed mid-term bonds with duration under 5 years comprise 20.1% or $76 million of the non-endowed funds; these bonds provided a return of 2.5%, which was slightly lower than that of the benchmark Scotia Capital Short Term Bond Index at 2.9%.

At March 31, 2005 $90 million or 23.8% of the non-endowed funds was invested in the UEP, which returned 5.7% for the year.

Going Forward

Management under the direction of the Investment Committee is currently searching for an active currency overlay manager. The UEP has a significant exposure to foreign currency; primarily the US Dollar, Euro, Japanese Yen and the Pound Sterling. At present this exposure is not managed. An active currency manager would seek to hedge the UEP against an appreciating Canadian Dollar, while still participating in the gains associated with a depreciating Canadian Dollar. The primary focus for this mandate will be currency risk management and downside protection, with a secondary objective of return enhancement. It is expected that this mandate will commence in 2005-06.

Management will also begin work on identifying suitable private equity fund of funds managers. The primary objective from this asset class will be to enhance the returns of the endowment assets by identifying general partners with a demonstrated long-term ability to generate superior returns. Given the very long-term nature of such investments, the due diligence component of the search process will be of primary importance.

Management is currently searching for a manager for the short-term money market investments. Money market investing has been managed internally for over 20 years and management has generally been able to add value over the benchmark through corporate commercial paper products which offer a yield superior to T-Bills. From a return perspective, the past two years have basically equaled or underperformed the Scotia 91-day T-bill index. As well, commercial paper inventory has declined by 10% over the past five years taking $10 billion out of the market. The reduction in inventory, coupled with an increase in demand, has resulted in narrower yield spreads without a corresponding reduction of risk profiles. Therefore money market participants are seeing lower returns without lower risk. Although the University's return matched the 91-day T-bill rate of return, the University's portfolio is exclusively corporate paper and therefore has more risk than the index. Retaining a money market manager would allow the University to enhance returns by taking advantage of longer term (greater than 90 days) money market investments, lower risk through access to higher credit-rated products, while maintaining the necessary liquidity of the portfolio to meet operating needs.

Board of Governors Investment Committee established October 1997.
Investment Committee Membership for the period July 1, 2004 to June 30, 2005:

Bob Kamp, Chair (external member)
Ken Bancroft (external member)
Fred Barth (external member)
Barbara Belch (external member)
Jim Drinkwater (external member since June 1, 2005)
Lynne Duncan (external member)
J.D. Hole (board member)
Allister McPherson (external member)
Gerard Protti (board member)

Jim Edwards (ex-officio)
Dr. Rod Fraser (ex-officio)
Dr. Eric Newell (ex-officio)

Prepared for Board Investment Committee
By Financial Services - Treasury

Appendix 1 - Investment Manager Structure

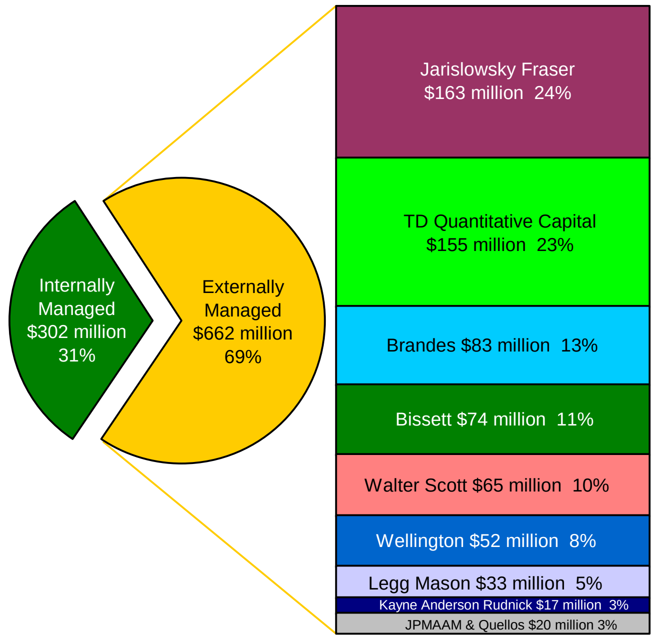
The University retains the services of ten external fund managers for the bond, equity and absolute return components of the endowment investment portfolio.

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.

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.

Investment Management Structure

Total Investment Assets of $964 Million at March 31, 2005



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 20 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 over 40 individual strategy funds run by managers outside of JPMAAM. These different strategies seek to capitalize on market inefficiencies: they 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. JPMAAM's mandate was funded on January 1, 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 and seeks to identify the next generation of blue chip companies through bottom up fundamental research of companies with an S&P rating of A- or better. Kayne Anderson Rudnick's mandate was funded on December 1, 2003.

Legg Mason Canada Inc. has an active Canadian bond mandate. Legg Mason is a duration specialist that seeks to add value through holding a different maturity profile from that of its benchmark index. Legg Mason has been managing funds on behalf of the University since November 1998.

Quellos Capital Management has an absolute return strategy mandate. The University has invested in Quellos Strategic Partners II Ltd., which operates a hedge fund of funds product. Quellos Strategic Partners II invests in over 50 individual strategy funds run by managers outside of Quellos. These different strategies seek to generate a return by capitalizing on market inefficiencies and include relative value, event driven and hedged directional strategies. Quellos excludes certain strategies from their fund of funds, such as commodity trading and global macro. As well, Quellos seeks to identify and invest with new fund managers at an early stage to establish a long-term competitive advantage. Quellos Capital Management's mandate was funded on January 1, 2005.

TD Quantitative Capital has a passive U.S. equity S&P500 Index mandate, a Scotia Capital Universe Bond Index mandate, and a Scotia Capital Real Return Bond Index mandate. 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 of above 20% per annum. Walter Scott's mandate was funded on July 1, 2003.

Wellington Management Company LLP has an active core United States equity mandate for large corporations. Wellington's style uses a balanced process that takes both top down and bottom up analysis into account in sector weighting and security selection. Both growth and value considerations are taken into account in the buy and sell discipline. Wellington has been managing funds on behalf of the University since July 2001.

Appendix 2 - Investment Performance by Asset Class

Balanced Manager Performance

Jarislowsky Fraser's total return for the year of 6.6% exceeded their benchmark return of 5.3%. During the year Jarislowsky Fraser's Canadian equity portfolio was well positioned, benefiting from stock selection in the materials sector and from an overweight position in two of the top three performing sectors, namely energy and consumer staples. Jarislowsky Fraser's overall return was tempered somewhat by slight underperformance in the Global Equity asset class which returned 2.2%.

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. 17% of the bond portfolio is in the Legg Mason Active Bond Fund. The UEP invests in two TD Quantitative Capital fixed income funds; the TD Emerald Canadian Index bond fund (21% of the holdings) and the TD Emerald Real Return Bond Fund (34% of the holdings). Jarislowsky Fraser managed another 24% of the bond portfolio, while the remaining 4% was managed internally. The overall fixed income portfolio returned 6.7% which trailed the fixed income benchmark return of 6.9%. However, the University's return exceeded the RMCTU fixed income median return of 5.7%.

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	18.51	10.0%	2.8%
Gov't of Canada RRB 4.25% 01-DEC-2026	17.36	9.4%	2.6%
Gov't of Canada RRB 4.25% 01-DEC-2021	17.23	9.3%	2.6%
Gov't of Canada RRB 3.00% 01-DEC-2036	6.87	3.7%	1.0%
Gov't of Canada 5.25% 01-JUN-2013	4.67	2.5%	0.7%
Gov't of Canada 5.50% 01-JUN-2010	4.64	2.5%	0.7%
Canada Housing Trust 4.75% 15-MAR-2007	4.56	2.5%	0.7%
Cda Housing Trust 4.100% 15-DEC-2008	4.20	2.3%	0.6%
Gov't of Canada 8.00% 01-JUN-2023	4.15	2.2%	0.6%
Prov. of Ontario 6.50% 08-MAR-2029	4.10	2.2%	0.6%

Bonds

Canadian bond rates of return for the endowments were 4.7% for the fiscal year. This return trails both the SC Bond Universe Index return of 5.0% and the RMCTU median of 5.0%. Rate hikes of the magnitude that were anticipated in the beginning of 2004 did not materialize: the Bank of Canada remained relatively passive in its monetary policy and concerned about the economic impact of an appreciating Canadian Dollar. The Bank of Canada initially reduced the overnight target rate from 2.25% to 2.0% in April 2004. The Bank of Canada then reversed direction, increasing the rate in both September and October 2004, which brought the rate to 2.5%. Measured rate hikes by the U.S. Federal Reserve from 1.0% to 2.75% coupled with a slight rise in long-term U.S. treasury yields in the beginning of 2005, further limited the demand for Canadian bonds. However, the bond market environment remains favorable for investors going forward due to stable inflation and interest rates. Short-term yields increased, while long-term yields decreased, resulting in a flattening of the yield curve. Scotia Capital long-term bonds returned 8.9% while Scotia Capital short-term bonds returned only 2.9%.

Legg Mason's return for the year was 4.0%, trailing the SC Bond Universe Index return of 5.0% by 100 basis points. Legg Mason maintained a very defensive stance throughout the past fiscal year expecting rising Canadian bond yields. The anticipated rise did not occur; therefore Legg Mason's short duration strategy underperformed the benchmark.

Jarislowsky Fraser matched the benchmark return of 5.0%. As with Legg Mason, Jarislowsky Fraser also adopted a shorter duration strategy during fiscal 2005 which detracted from performance. This was offset by a positive contribution from corporate bond selection. The manager further noted that spread compression in the Canadian corporate bond market has limited their long-term bond purchasing opportunities.

The TD Emerald Canadian Bond Fund is indexed to the SC Bond Universe Index and provided a benchmark return of 5.0%.

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 SC RRB 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, 2005 the real return bonds returned 10.7%, matching the SC RRB Index. The index is long in duration, which accounts for a substantial portion of its strong performance this past year. Demand for real return bonds continues to exceed supply resulting in further yield compression, which also contributed to this year's strong return.

Canadian Equity Component

The Canadian equity portfolio returned 20.5% for the period compared to a return of 13.9% for the Canadian equity benchmark S&P/TSX Composite Index and 16.4% for the RMCTU median. The relative out-performance of the benchmark can be attributed to stock selection and sector allocation by both active managers.

Top 10 Canadian Equity Holdings

Company	Market Value ($ millions)	% of CDN Equities	% of Portfolio
Bank of Nova Scotia	5.51	4.9%	0.8%
Royal Bank of Canada	5.44	4.8%	0.8%
Manulife Financial Corp.	4.92	4.3%	0.7%
Power Financial Corp.	3.85	3.4%	0.6%
Nexen Inc.	3.82	3.4%	0.6%
Canadian National Railway Co.	3.35	3.0%	0.5%
Encana Corp.	2.80	2.5%	0.4%
Petro-Canada	2.64	2.3%	0.4%
Loblaw Companies	2.64	2.3%	0.4%
Transcontinental Inc.	2.53	2.2%	0.4%

Jarislowsky Fraser was overweight in both the energy and consumer staples sectors which had returns of 43.6% and 16.6% respectively for the year. Jarislowsky Fraser also benefited from underweighting health care which had a sector return of -25.5%. Jarislowsky Fraser performed strongly on the stock selection side, outperforming in seven of the eight sectors in which they were invested. As a whole, Jarislowsky Fraser's Canadian Equity portfolio returned 26.6%, exceeding the benchmark of 13.9%.

For fiscal 2005, Bissett returned 17.5%, adding 360 basis points of value over the benchmark. Stock selection contributed to Bissett's overall success as they outperformed in six of eight sectors in which they were invested. As a result of their bottom up fundamental stock selection process Bissett also performed well by being overweight in the consumer staple and financial sectors, and underweight in the poorer performing materials sector.

Given the Canadian economy's dependence on the U.S., our fund managers' outlook for the Canadian equity market is heavily influenced by the U.S. economy. Prospects for growth in the U.S. remain moderate with Gross Domestic Product growth forecast to be around 3.0%. The already substantial U.S. current account deficit could continue to grow which may put further strain on the U.S. dollar. Growth is being driven by consumer borrowing and spending which could raise inflationary concerns and result in further monetary tightening by the Federal Reserve to slow economic growth and control inflation.

GDP growth forecasts for Canada fall closer to the 2.0% mark. While high oil prices have fuelled strong returns in the Canadian Equity markets, the appreciation of the Canadian dollar has hampered exports to the U.S.

Foreign Equity Component

The foreign equity component is comprised of U.S. equities and three Europe, Australasia, Far East, and emerging market (EAFE) funds. The endowment's foreign equity component posted a return of 1.5%, lower than the 2.3% return of the benchmark Morgan Stanley Capital International Composite World Index. The endowments also trailed the RMCTU median of 2.5%. These returns can be further broken down into their US and Non-North American components. The poor absolute performance can be mainly attributed to the rapid appreciation of the Canadian Dollar in fiscal 2005 which greatly impeded returns from U.S. dollar denominated investments.

Top 10 Foreign Equity Holdings

Company	Market Value $Cdn millions	% of Foreign Equities	% of Portfolio
Nestle Switzerland	5.75	1.6%	0.9%
General Electric Co. US	4.95	1.4%	0.7%
Microsoft Corp. US	4.58	1.3%	0.7%
Exxon Mobil Corp. US	4.36	1.2%	0.6%
Unilever UK/Netherlands	3.50	1.0%	0.5%
Altria Group Inc. US	3.44	1.0%	0.5%
Pfizer Inc. US	3.17	0.9%	0.5%
Citigroup Inc. US	3.09	0.9%	0.5%
Johnson & Johnson US	3.03	0.9%	0.5%
Millea Holdings Inc. Japan	2.91	0.8%	0.4%

Jarislowsky Fraser’s foreign equity portfolio had a return of 2.2%, which slightly underperformed the benchmark return of 2.3%. Jarislowsky Fraser’s U.S. return was -0.4% which compares favorably to the S&P 500 return of -1.8%. The value added was a result of good stock selection in various sectors and an underweight position in the worst performing sector, Information Technology. This was, however, offset to certain degree by sector allocation. Jarislowsky Fraser was overweight in 3 of the 4 worst performing sectors; Consumer Staples, Health Care and Financial Services, and underweight in 3 of the 4 best performing sectors; Utilities, Industrials and Materials. In absolute terms, performance was significantly impacted by the 7.7% depreciation of the US Dollar against the Canadian Dollar.

Jarislowsky Fraser’s EAFE equity return of 5.7% fell short of the MSCI EAFE benchmark of 6.3%. The shortfall can be attributed to sector allocation where Jarislowsky Fraser was overweight in three of the five sectors which underperformed the MSCI EAFE as a whole: Consumer Staples, Health Care and Consumer Discretionary. However, performance did benefit from country allocation as Jarislowsky Fraser was significantly underweight in Japan, which was the second worst performing market in the MSCI EAFE Index.

The EAFE equity managed by Brandes Investment Partners had a return of 7.5%, which added 120 basis points of value over the MSCI EAFE Index return of 6.3%. Brandes attributes this out performance to stock selection. Specifically, stock holdings in both the Financials and Diversified Telecom sectors performed strongly. As well, stock selection in the United Kingdom added value over the index.

Walter Scott & Partners’ EAFE mandate posted a return of 1.0% for fiscal 2005. This return lagged the benchmark return of 6.3%. The underperformance can be primarily attributed to the country allocation that has resulted from their “bottom up” security selection process. The Walter Scott portfolio is strongly overweight in Japan (41.4% as of March 31, 2005 versus approximately 22.0% for the MSCI EAFE): Japan was the second weakest performer in the MSCI EAFE with a return of -9.5%. Although Japanese equity markets remained virtually flat for the year (in local currency), the Canadian Dollar strengthened by 10% against the Japanese Yen. Correspondingly, the portfolio is underweight in Europe, especially France, Germany, Netherlands, Italy and the United Kingdom, all of which outperformed the MSCI EAFE as a whole. The overweight position in Japan detracted approximately 2.0% from performance, while the underweight position in Europe detracted approximately 3.0%. Given Walter Scott’s growth style, it is also important to note that MSCI EAFE Value index returned 10.2%, while the MSCI EAFE Growth index returned only 2.2% for the year. Walter Scott believes that economic and structural issues will continue to challenge European economies while the best growth opportunities remain in Asia.

The U.S. equity portfolio, managed by Wellington Management, posted a loss of 3.9%. Wellington underperformed both the S&P 500 benchmark of -1.8% and the RMCTU median of -1.1%. The U.S. Equity market continued to favor mid and small cap stocks for most of the 2004 calendar year. Wellington focuses on large cap equities with 90% of the portfolio invested in names with market capitalizations of greater than $6 billion. Wellington's research indicates the U.S. market has experienced a period of small cap out performance, the length of which is unprecedented. Wellington also believes that going forward, higher interest rates, a renewed focus on dividends, a synchronized global economic recovery combined with a weaker U.S. Dollar will favor high quality large multi-national corporations. Returns for the first calendar quarter of 2005 bear out this theory as the large cap Russell 1000 index outperformed the small cap Russell 2000 index -1.0% to -4.4%. This trend reversal has also been reflected in Wellington's performance for the four months ending April 30, 2005 with a return of 2.0% compared against the S&P 500 return of 0.5%.

The U.S small to mid-cap equity portfolio, managed by Kayne Anderson Rudnick, lost 3.0% for the fiscal year versus its benchmark of -0.4%. 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 attributes the underperformance to historically low yields and credit spreads in the U.S. market. This allows weak companies to continue to operate through debt financing. With the low credit spreads, investors are not willing to pay a premium for quality, which has suppressed high quality stock returns. Kayne Anderson expects relative out performance for their strategy when credit spreads widen to historical norms.

The S&P 500 Index portfolio managed by TD Quantitative Capital lost 1.9% for fiscal 2005 versus its S&P 500 benchmark return of -1.8%. The differential can be attributed to low cash returns from temporarily un-invested dividend receipts to the segregated fund.

Alternative Asset Component

Both the JP Morgan Alternative Asset Management (JPMAAM) and Quellos Capital Management hedge fund of funds products were funded as of January 1, 2005. Therefore only fourth quarter returns are available. Given the absolute return objective for these two funds, both are fully hedged back to the Canadian Dollar to remove any potential currency impact.

Both companies failed to meet their benchmark return of 2.1% (US T-Bill +6%). Quellos returned 0.9% for the quarter while JPMAAM returned 1.0%. Relative value strategies and in particular convertible bond arbitrage had a difficult quarter as credit spreads began to widen accompanied by a convertible bond sell off in an environment of poor liquidity. Hedged directional strategies and equity long/short managers also came under pressure given the generally weak equity markets during the quarter ending March 31, 2005. Global macro managers were challenged by the strengthening US Dollar in the quarter after a long and pronounced decline in 2004.

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. In general this graph demonstrates that active management strategies have successfully added value.

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.