

Canadian Markets' Performance

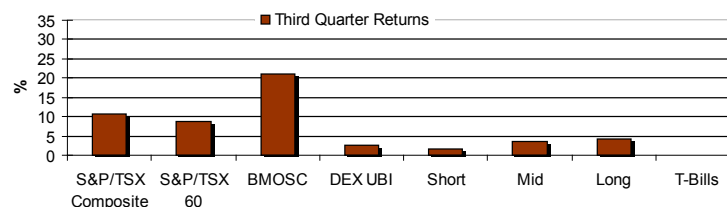
The Canadian equity market, as measured by the S&P/TSX Composite, had another strong quarter, returning (10.6%). The sectors with the highest returns were Health Care (22.2%), Financials (16.1%), and Materials (12.4%). Value stocks (13.6%) outperformed growth stocks (3.2%). Unemployment remains a concern at 8.4%. However, the Index of Consumer Confidence published by the Conference Board of Canada shows that consumer confidence has risen from 68.8 in February to 90.9 in September for a 22.1 point gain over the past seven months.

Information Technology (-8.1%) was the worst performing sector. IT's largest contributor by capitalization, Research In Motion, did not meet analyst estimates and had a quarterly price return of -12.5%. Financials, such as Bank of Montreal (20.1%), continued to post positive results as lending facilities improve with government stimulus. The Materials sector was led by gold. It closed the quarter at \$1,007.70/ounce and returned 8.7% over the period. Many consider gold a good hedge against inflation. As such, the recent run-up can be partly attributed to worries that monetary policy stimulus by governments will eventually lead to an increase in inflation. Consumer Staples (-2.7%) also lagged as risk aversion dissipated.

3RD QUARTER 2009

Small cap stocks, as measured by the BMO Small Cap Index, outperformed large cap stocks for the third consecutive quarter, returning 21.1%. Small cap growth stocks (22.2%) slightly outperformed small cap value stocks (20.5%) this quarter.

The Canadian bond market, as measured by the DEX Universe Bond Index returned 2.7%. The Corporate bond sector returned 4.5%, whereas safer Federal bonds returned 1.2%. By bond quality, high yield, A-rated and BBB-rated corporate bonds had the highest returns, 9.4%, 5.2% and 5.2%, respectively. Yields across short (1-5 years), mid (6-10 years) and long-term (greater than 10 years) maturities all moved downwards, ending the quarter at 2.19%, 3.68% and 4.66%, respectively. By maturity, long-term bonds (4.3%) were the top performer, while short-term bonds (1.6%) had the lowest return. As the yield curve has shifted toward a normal upward slope, investors have been willing to take on more maturity risk at the long end of the curve to earn a risk premium above shorter maturities.



Notable Dates

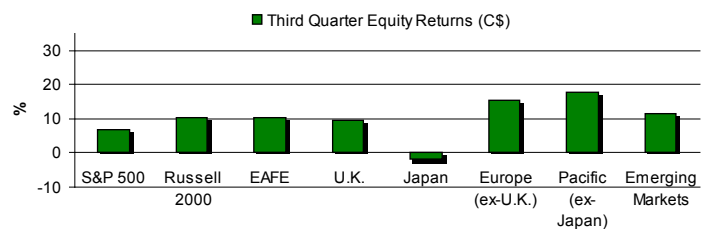
- Jul 21 Bank of Canada keeps overnight rate at 0.25%.
- Jul 30 "Cash for Clunkers" program in the U.S. is met with a lot of enthusiasm.
- Aug 24 President Barack Obama announces nomination of Ben Bernanke as Federal Reserve Chairman for second term.
- Aug 28 Statistics Canada reports Canadian current account deficit of \$11.2 billion. It is the first trade deficit since 1976.
- Sep 3 Job gains reported in Canada for the first time in four months.
- Sep 10 Japan's core machinery orders hit an all-time low, signaling weak capital spending and a slower recovery.
- Sep 10 Bank of Canada keeps overnight rate at 0.25%.
- Sep 17 Japan's policy board agrees to keep unsecured overnight call loan rate at 0.1%.

Global Markets' Performance

The global equity markets outpaced the Canadian markets. Similar to last quarter, emerging markets and small cap equities had the highest returns. Both have high betas (measure of risk compared to the broad market) and, as a consequence, have rallied more.

On a local currency basis, the S&P 500 returned 15.6%. The return drops to 6.8% on a Canadian dollar basis, as the C\$ appreciated against the U.S. dollar over the quarter. According to the Conference Board in the U.S., the Consumer Confidence Index increased to 53.1 from its June level of 49.3 (1985=100). As companies continued to take cost-cutting measures by reducing payrolls and as consumers cut back on spending, the U.S. has seen its unemployment rate increase to 9.8% from the June level of 9.5%. Eight of ten sectors had positive returns during the quarter. Financials (15.7%) continued as the leading sector, as analyst ratings were raised for the investment bank Goldman Sachs (25.0%). Industrials (12.0%) and Materials (11.8%) also had strong returns. Investors turned toward sectors that historically participate more from cyclical upswings. Defensive sectors continued to lag. The two negative contributors were Utilities and Telecom, returning -3.0% and -3.9%, respectively.

The MSCI EAFE returned 14.8% in local currency terms, decreasing to 10.4% in Canadian dollars, as more than half the currencies within the index depreciated versus the Canadian dollar. Once again, all ten sectors had positive returns, with Financials (18.1%) and Materials (10.4%) performing the best. Japan (-1.6%) was the worst performing region, while the Pacific ex-Japan region (17.7%) was the best. Emerging markets (11.7%) outpaced developed markets, led by the Latin America region (14.6%). Australia (23.0%) was the top performing country within the developed world. Hungary (31.3%) was the top performer within the emerging markets.



Dynamic Investment Policy—The New LDI

In the past decade, plan sponsors have experienced a wild ride in plan funding levels. With two major global equity market declines in 2000/01 and 2008, few defined benefit plans are currently in a surplus position. In fact, the aggregate funding declines of 2008 were likely the worst ever for pension plans in North America. Given the popularity and the wide acceptance of liability-driven investing concepts, why weren't more plans protected?

The answer is threefold. First, plan sponsors already employing LDI strategies generally matched only a portion of their assets with their liabilities. Second, plan sponsors tend to review their assets relative to their liabilities periodically, typically between three and five years. Thirdly, some sponsors who identified LDI as an attractive pension risk management strategy were left on the sidelines as they waited for the 'right time' to move to an LDI approach.

Armed with the knowledge of the challenges plan sponsors face when implementing LDI strategies and an understanding of the shortcomings of a traditional LDI approach, Hewitt has developed the Dynamic Investment Policy ('Dynamic IP') approach.

The key premise of the Dynamic IP is to develop a well-defined LDI asset allocation strategy based on two broad asset categories (risky assets and liability matching assets) that varies as plan funded ratios change.

A Dynamic IP is composed of two parts: a flight path and a rebalancing policy. The flight path is a series of target asset allocations for various levels of funding. The rebalancing policy includes rebalancing bands for risky and matching assets for points along the flight path. As with all investment strategies that employ rebalancing, Dynamic IPs exhibit buy

low/sell high characteristics, which leads to lower volatility and a more sensible allocation of plan assets from a risk management perspective.



Certain key steps are required in the development and implementation of a successful Dynamic IP approach:

Define Plan Goals and Objectives

Examples of this may include reaching a specific funded ratio, limiting pension expense or contributions to a certain level, and/or exiting the pension business entirely. The more specific the goals, the easier it is to design a Dynamic IP.

Define End State

Once the objectives are determined, one can then define a final target portfolio—the appropriate asset allocation for the portfolio once the target funded ratio level is reached. This involves an analysis of two forms of risk: minimum required return and maximum surplus risk. Minimum required return is an often overlooked measure of long-term risk (return shortfall), whereas maximum surplus risk is the more common, short-term measure (maximum loss threshold). A Dynamic IP strikes a balance between these two risks.

For example, the end state might be to have a 110% funded portfolio with 90% matching assets, and 10% return seeking assets to meet the minimum required return.

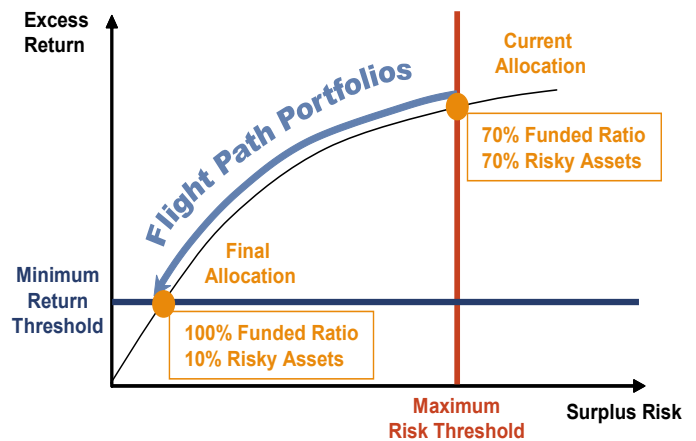
Develop a Flight Path

Define the investment and contribution strategy that will transition from the current position to the desired end state.

Leaving risk in the portfolio relative to the desired end state may reduce the time required to reach the end state and allow the sponsor to contribute less to the plan in the long run, but with greater volatility.

Rebalancing and Implementation Strategy

Select the asset classes and manager(s) to use in each of the liability-matching and risky asset components of the asset mix. Determine the rebalancing ranges and document the new investment and funding strategies.



Ongoing Monitoring

Ensure a process is in place to provide up-to-date information on the funded status so that trigger points in the investment and funding strategies can be implemented in a timely fashion.

Hewitt suggests monitoring the impact of capital market movements on the Dynamic IP on a monthly basis, though quarterly is also sufficient. However, we also believe that monitoring should occur when contributions are made and when significant disbursements are paid.

Advantages of the Dynamic IP over Traditional IP Approach

- Defined strategy for all plan assets
- Links investment strategy with current funded levels
- Success of strategy monitored continuously
- Facilitates a gradual de-risking of the portfolio, while avoiding 'timing' the market

Conclusions

Dynamic IPs provide a practical solution for achieving long term goals by systematically implementing an LDI strategy as funded status improves.

About Hewitt Associates

Hewitt Associates (NYSE: HEW) provides leading organizations around the world with expert human resources consulting and outsourcing solutions to help them anticipate and solve their most complex benefits, talent, and related financial challenges. Hewitt works with companies to design, implement, communicate, and administer a wide range of human resources, retirement, investment management, health care, compensation, and talent management strategies. With a history of exceptional client service since 1940, Hewitt has offices in more than 30 countries, including Canadian offices in Calgary, Montreal, Regina, Toronto and Vancouver, and employs approximately 23,000 associates who are helping make the world a better place to work.

Hewitt's investment consulting practice in Canada has focused solely on institutional consulting since 1973. We provide comprehensive consulting services to institutional clients including pension funds, endowment funds, charitable organizations and religious orders.

For more information, please visit www.hewitt.com/canada or contact Paul Malizia at 416-227-5737.