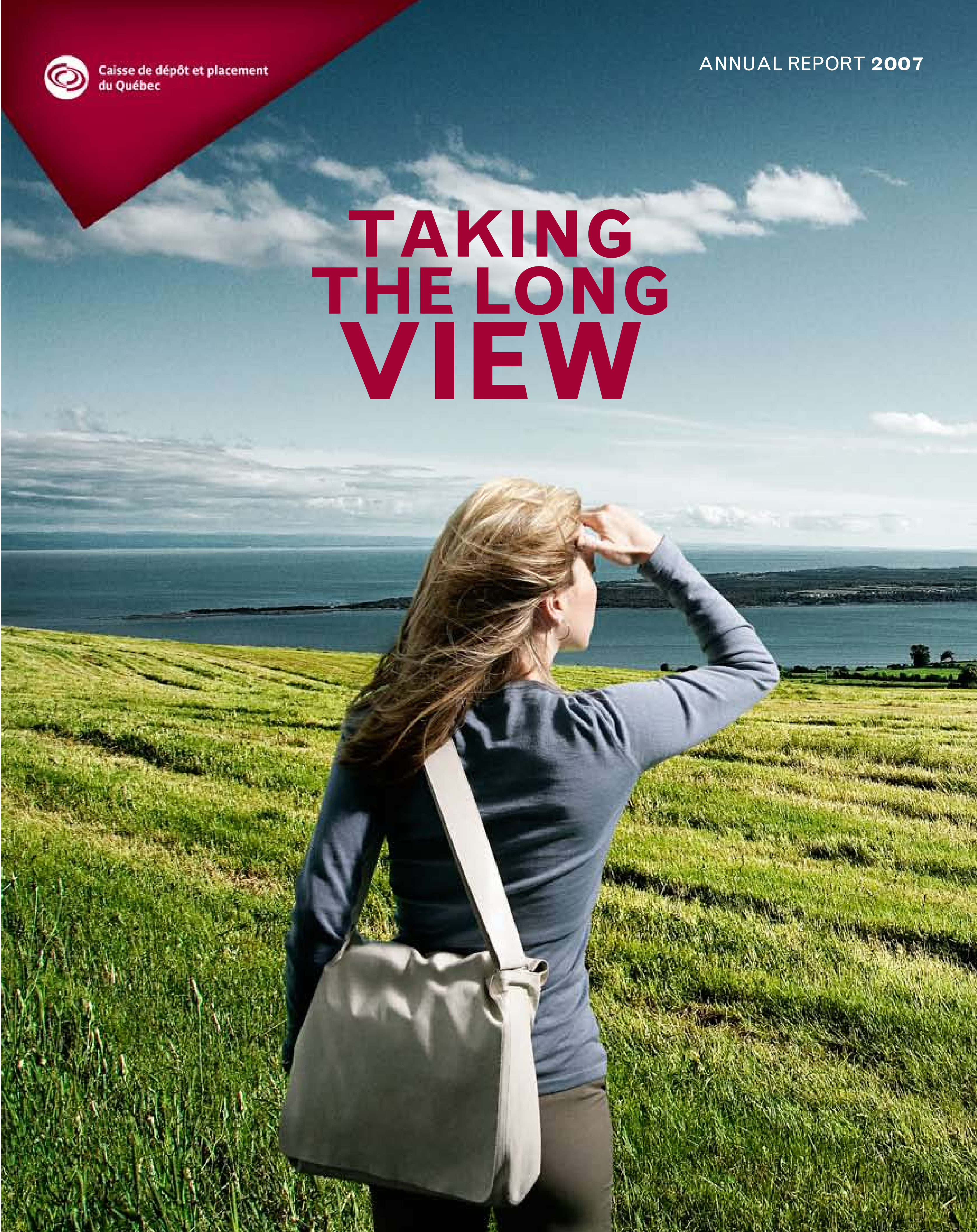
Caisse de dépôt et placement du Québec

ANNUAL REPORT **2007**

TAKING THE LONG VIEW



FOR ALL OF US

MISSION

"The mission of the Fund is to receive moneys on deposit as provided by law and manage them with a view to achieving optimal return on capital within the framework of depositors' investment policies while at the same time contributing to Québec's economic development."

Act respecting the Caisse de dépôt et placement du Québec, section 4.1

VALUES

The officers and employees of the Caisse share the values that guide the institution: excellence, ethics, boldness and transparency.

CAISSE STAKEHOLDERS

QUÉBEC GOVERNMENT

The Caisse is an agent of the government, which appoints its President and the members of its Board of Directors and approves the appointment, by the Board, of the President and Chief Executive Officer.

DEPOSITORS

The depositors are mainly Québec public- and private-sector pension and insurance plans whose funds are managed by the Caisse. Their common objective is to earn a superior return on the moneys provided by their contributors with a view to meeting future needs, such as payment of pension benefits or accident compensation.

PARTICIPANTS

The participants are individuals eligible for the depositors' group pension and insurance plans. Most Quebecers are members of one of the plans and are therefore affected by the returns earned by the Caisse.

COMPANIES

The Caisse has a portfolio of investments in more than 3,000 publicly traded companies and in many privately owned businesses.

CLIENTS

In addition to depositors' funds, the Caisse administers or manages property for clients, mainly in the real estate sector.

EMPLOYEES

The Caisse had 772 employees as at December 31, 2007. The real estate units Cadim, Ivanhoe Cambridge and SITQ employed a total of 1,772 people.

PARTNERS

The Caisse forms investment partnerships to share expertise and risk. It also maintains relations with various financial and business stakeholders for reasons that include maintaining a dialogue on the major issues facing the investment industry.

SUPPLIERS

The Caisse deals with various suppliers of goods and services, including fund managers, information technology specialists, legal advisers and auditors.

The "General notes" at the end of this document provide information that facilitates an understanding of the texts, tables and figures that follow.

A PDF version of the Annual Report 2007 and the Additional Information is provided on a compact disc at the beginning of this document.

MESSAGES

RETURNS AND FINANCIAL POSITION

ECONOMIC DEVELOPMENT

MANAGEMENT FRAMEWORK

OPERATIONAL LEVERS

BOARD OF DIRECTORS AND BOARD COMMITTEES

ADDITIONAL INFORMATION (PDF version on CD attached)

TAKING THE LONG VIEW MEANS SELECTING THE RIGHT TOOLS

/ **PIERRE BRUNET**
Chairman

MESSAGE FROM THE CHAIRMAN

IN THE FOLLOWING INTERVIEW, PIERRE BRUNET TALKS ABOUT THE ROLE PLAYED BY THE BOARD OF DIRECTORS IN 2007 AND THE SPIRIT OF CO-OPERATION BETWEEN THE BOARD AND SENIOR MANAGEMENT

The Caisse's results for 2007 once again testify to its professionalism and effectiveness. They also reflect a more difficult market context that called for solid governance. Throughout the year, the Board of Directors therefore played a key role by ensuring the Caisse was managed in accordance with the provisions of its Act and regulations.

Q1.
HOW DOES THE BOARD OF DIRECTORS SUM UP 2007?

First, we can say that 2007 was a year filled with challenges, for Caisse senior management as well as the Board of Directors. We saw a complete shift in the market context in a brief period. A combination of several factors, from the rapid appreciation of the Canadian dollar to the global credit crisis, prompted us to rethink our analysis of the market outlook to ensure an accurate assessment of the potential returns and their related risks.

The situation called for exceptional adaptability, so that we could maintain our progress toward long-term growth. In the eyes of the Board of Directors, the Caisse was able to demonstrate that it could rapidly change gears and rise to highly complex challenges.

Q2.
IN LIGHT OF THIS SITUATION, HOW DID THE BOARD OF DIRECTORS GO ABOUT FULFILLING ITS MANDATE?

The governance of the Caisse was central to the work of the Board of Directors in 2005 and 2006, when we took the measures required to put in place an adequate framework. So the members of the Board started 2007 with the right tools at hand.

For example, we could count on access to complete, relevant information to assist Caisse senior management with decision making. The ability of the Board members to ask the right questions at the right time proved to be an important asset, if only by shedding new light on the various matters we had to consider, such as optimal use of resources, risk management and business continuity. In fact, this attribute is conducive to constructive discussions between the Board and senior management and ensures sound decision making.

In addition, the program for integration and training of directors, two components of the process to improve governance, definitely contributed to the spirit of co-operation between the Board and senior management. These measures are part of our constant effort to broaden the Board's range of competencies, so that all investment-related matters can be discussed effectively.

In other words, the Board had an unusually demanding year. In addition to day-to-day business, such as monitoring the strategic plan and adopting the business plan and the budgets, we discussed a number of matters that required special attention. In addition to the 11 regularly scheduled Board meetings, we held 12 special meetings, not including the regular and special meetings of the Board's various committees. For an idea of the scope of this work, see the section "Board of Directors and Board committees."

MESSAGE FROM THE CHAIRMAN

Q3. LET'S TAKE THE EXAMPLE OF THIRD-PARTY ABCP. WHAT ROLE DID THE BOARD OF DIRECTORS PLAY IN THE DEVELOPMENT OF A SOLUTION?

The climate of trust and close co-operation between Caisse senior management and the Board of Directors contributed significantly to our ability to deal with this complex matter. As soon as the third-party asset-backed commercial paper (ABCP) crisis began, senior management notified the Board members. We had a detailed portrait of the situation at all times, to the extent that information was available. Sustained discussions enabled us to get a good grasp of the proposed solutions and the decisions that had to be made. From the onset of the crisis until year-end, this matter was on the agenda of each regular Board meeting. We also held five special meetings to deal exclusively with it.

In this way, the Board was able to assist senior management with its efforts to conclude the Montréal Accord. This assistance continued during the negotiations by the Pan-Canadian Investors Committee to reach an agreement to convert the third-party ABCP into securities with longer-term maturities. At the same time, after the market for these securities seized up, we reviewed and discussed mechanisms that would enable the Caisse to re-establish an appropriate level of liquid assets. Two Board committees also played an active role: the Risk Management Committee made recommendations on the appropriate methods for monitoring the ABCP, and the Audit Committee validated the approach used for the accounting treatment of it for the preparation of the financial statements.

I'd like to take this opportunity to point out the Caisse's leadership in this matter. Senior management relied on the solid expertise of its teams to begin developing solutions immediately. Their prompt action undoubtedly helped avoid a disorderly liquidation of the ABCP, with very serious consequences. Today, the entire market is benefiting from the initiative taken by the Caisse.

Q4. ULTIMATELY, HOW WOULD THE BOARD OF DIRECTORS QUALIFY THE RESULTS OBTAINED FOR THE YEAR?

My colleagues on the Board of Directors and I are very satisfied with the return obtained by the Caisse in 2007. By ranking in the first decile of its reference market, the Caisse has demonstrated that the depositors, and by extension their participants, can count on a competent organization that is completely dedicated to their interests.

All personnel at the Caisse deserve our utmost gratitude for the effort expended and the work accomplished. In particular, I'd like to congratulate the President and Chief Executive Officer, Henri-Paul Rousseau, and his senior management team. Under their direction, the Caisse has made remarkable progress. In five years, net assets under management have doubled from $77.7 billion to $155.4 billion. This is a remarkable performance and, above all, an important contribution to the sustainability of the depositors' plans.

Q5.
WHAT IS THE OUTLOOK FOR 2008, AND HOW DOES THE BOARD OF DIRECTORS INTEND TO PURSUE ITS MANDATE?

The market context will continue to be difficult in the short term. Its considerable volatility requires unprecedented vigilance and diligence. At the same time, given the intense competition, the increasing complexity of financial instruments and the greater emphasis on foreign markets as sources of returns, the investment business is becoming more demanding. It is imperative that each decision be the outcome of a process that is rigorous, precise and effective.

The Board of Directors therefore intends to continue improving the institution's governance. The arrival of new directors will complete our range of skills. This knowledge, combined with the tools at our disposal, will form the foundation enabling us to fulfill our responsibilities to Caisse senior management.

The matters that will require special attention in 2008 include preparation of the Strategic Plan 2009-2011. Once again, we shall do our utmost to see that issues that are crucial for the Caisse are taken into account fully. Knowing how to select the right tools is what enables us take the long view and to stay focused on our long-term growth objectives.

/ **PIERRE BRUNET**
Chairman

NEW MEMBERS OF THE BOARD OF DIRECTORS

Three directors stepped down in 2007 after contributing effectively to the work of the Board and its committees. They are Pierre Prémont, Duc Vu and John T. Wall. I'd like to express to each of them my deep gratitude for their diligence, professionalism and dedication throughout their mandates.

During the year, the Québec government appointed four new directors, bringing the number of Board members to 15, the maximum allowed by the Act respecting the Caisse.

Christiane Bergevin and Ouma Sananikone accepted the three-year mandate offered to them and joined the Board in the fall of 2007, bringing with them solid experience in vital areas of expertise.

In addition, Jocelyne Dagenais and André Trudeau were appointed in December 2007 and took part in their first Board meeting early in 2008. As President and Chief Executive Officer of the Commission administrative des régimes de retraite et d'assurances (CARRA) and President and General Manager of the Régie des rentes du Québec, respectively, they were named to the Board as representatives of the Caisse's depositors. Without a doubt, their extensive knowledge of issues related to management of pension funds and insurance plans will be extremely useful in our deliberations and decision making.

TAKING THE LONG VIEW MEANS FOCUSING ON THE FUTURE

/ **HENRI-PAUL ROUSSEAU**
President and Chief Executive Officer

MESSAGE FROM THE PRESIDENT AND CHIEF EXECUTIVE OFFICER

IN THE FOLLOWING INTERVIEW, HENRI-PAUL ROUSSEAU REVIEWS THE RESULTS FOR 2007, PRESENTS THE CAISSE'S PRIORITIES FOR 2008 AND EXPLAINS HOW HE SEES THE YEARS TO COME

Q1.

THE CAISSE RECORDED AN OVERALL RETURN OF 5.6% IN 2007, INCLUDING A $1.9-BILLION PROVISION FOR ITS INVESTMENTS IN THIRD-PARTY ABCP. LOOKING BACK ON THE YEAR, HOW WOULD YOU ASSESS THIS RESULT?

I believe the Caisse had a positive year, despite the challenges it had to cope with in the second half, such as the volatile equity markets, the global credit crunch and the liquidity crisis on Canada's third-party asset-backed commercial paper (ABCP) market.

We owe a good portion of our return to the diversification of the Caisse's overall portfolio, especially the high weighting of non-traditional assets, such as private equity and real estate. With the Canadian dollar surging against the hard currencies, our foreign exchange hedging was also vital. Lastly, our managers generated a return that outperformed the index of the Caisse's benchmark portfolio.

I'm also very satisfied with the overall 5.6% return because it places us in the first decile of large Canadian pension fund managers. After all, it means the Caisse did better than 90% of its peers.

Q2.

THE CAISSE HAS RECORDED A PROVISION FOR ITS INVESTMENT IN THIRD-PARTY ABCP. DOES THE PROVISION MEAN IT EXPECTS TO LOSE UP TO $1.9 BILLION?

First, I'd like to make it clear that, in our opinion, the $1.9-billion provision doesn't represent a total, irrevocable loss. Rather, it's a prudent estimate of losses that could materialize on completion of the third-party ABCP restructuring plan established by the Pan-Canadian Investors Committee, to which the Caisse belongs. Under this plan, all outstanding third-party ABCP will be exchanged for longer-term notes whose maturities correspond to the underlying assets of the securities concerned.

Most of the Caisse's provision, namely $1.4 billion, involves third-party ABCP whose underlying assets are of excellent quality. The second component of the provision, however, covers that portion of the ABCP investments exposed to U.S. subprime mortgages. This provision has been established at $469 million.

I'd like to add that the difficulties with third-party ABCP have tested the Caisse's ability to manage a major financial crisis. And we passed the test, if we consider the speed with which the teams mobilized and the scope of the work they accomplished in dealing with this matter, while ensuring the normal course of our operations. I'd like to offer my sincere thanks to the Caisse's employees for their solidarity and loyalty.

From the outset, we were able to count on the understanding and patience of the Caisse's 25 depositors. I'd also like to thank them for their trust in us. And I'm grateful to the members of the Board of Directors for their support throughout this trying period.

MESSAGE FROM THE PRESIDENT AND CHIEF EXECUTIVE OFFICER

Q3.
THE CAISSE'S PERFORMANCE IS EXCELLENT IN RELATION TO ITS PEERS, BUT DOES IT MEET THE DEPOSITORS' EXPECTATIONS?

To answer that question, we shouldn't look at 2007, or any other year, in isolation, because we have a long-term objective of 7%. Instead, we should evaluate what I like to call our batting average.

From 2003 to 2006, the Caisse's overall return was high, at 15.2%, 12.2%, 14.7% and 14.6%, respectively. If we add the 5.6% return for 2007, we get an average annual return of 12.4% for this five-year period. Moreover, depositors' net assets doubled, going from $77.7 billion at the end of 2002 to $155.4 billion as at December 31, 2007. About 81% of that growth is due to our returns.

We're satisfied with this performance, which reflects the close co-operation between the Caisse and its depositors – co-operation that has enabled us to meet and even exceed their expectations since 2003.

Q4.
WHAT ARE THE REASONS FOR THESE EXCELLENT RETURNS?

The Caisse's overall return is due to the depositors' investment policies, the behaviour of the financial markets and active management of our 18 specialized portfolios. But I believe the decision to refocus the Caisse on its role as a fund manager serving its depositors has also been a key success factor for us. It was formalized with legislative amendments that clarify the Caisse's mission and update its governance. In making this shift, we've strengthened our relationship of trust with the depositors and raised the organization's level of performance.

In brief, looking back on these five years, I'm very proud of what the people at the Caisse have accomplished in all our areas of activity. Still, I'm well aware that the returns we obtained during that period are exceptional, in the strict sense of the word. As I've said many times in recent years, such returns are not sustainable over the long term. Sooner or later, less favourable years will bring us back to our long-term objective of 7%.

Q5.
COULD SOME PEOPLE CONCLUDE THE CAISSE HAS TAKEN ON EXCESSIVE RISK IN SEEKING THESE HIGH RETURNS?

That's not the case. The Caisse has always been very careful about managing the funds entrusted to it. Moreover, it works in close co-operation with the depositors to construct portfolios that are diversified enough to meet their expectations, while respecting their risk tolerance.

To obtain a 7% average return over the long term, we can't restrict ourselves to fixed-income securities, such as bonds, which generate a return of only 4% or so. We have to invest in asset classes that are more profitable, but also riskier, such as publicly traded equities, private equity and real estate. The tremendous size of our portfolio also leads us to invest in all global markets. By diversifying in more ways than one, we can effectively manage the risks we assume, for example by limiting the risk related to one type of investment or one region of the world.

According to a study by RBC Dexia Investor Services, it appears that the Caisse earned its returns from 2005 to 2007 with a realized risk lower than that of its peers.

Q6.

WHAT ABOUT THE CAISSE'S OPERATIONAL EFFICIENCY? HOW DOES IT COMPARE WITH ITS PEERS'?

The Caisse's operating expenses in 2007 were 21.7 cents per $100 of average net assets, including external management fees. This level is comparable to that of 2006 and lower than it was in 2005 (22.6 cents). Moreover, it is similar to that of its Canadian peers of comparable size. The total number of employees was stable in 2007, at 772 in comparison with 783 in 2006, excluding the real estate units (Cadim, Ivanhoe Cambridge and SITQ). This level is lower than it was in 2002, when the Caisse had 814 employees.

Moreover, the Caisse has a strong performance when we look at its operating expenses in relation to its investment results, in other words its return in dollars. Over the past five years, these expenses have averaged two cents for each dollar of return that the Caisse generated for its depositors.

Q7.

YOU SAY YOU'RE SATISFIED WITH THE RETURNS THE CAISSE HAS EARNED IN THE PAST FIVE YEARS. ARE YOU JUST AS PLEASED WITH ITS CONTRIBUTION TO QUÉBEC'S ECONOMIC DEVELOPMENT?

I believe the Caisse continues to make a remarkable contribution to Québec's economic development. It does so above all with the returns it earns for its 25 depositors. In this way, the Caisse enhances the sustainability of the pension funds and insurance plans that make up the majority of the depositors and thus contributes to Quebecers' collective wealth.

The Caisse has always been a very active investor in Québec, and the province is still very much a priority for it. Far from being negligible, our total assets here amounted to $37.8 billion at year-end.

The Caisse partners with many companies, providing private equity, including venture capital, to a large number of companies. It's also one of the main investors in publicly traded equities, fixed income and real estate. And it forms investment partnerships for major transactions, such as the acquisition of Noverco (Gaz Métro) and Bombardier Recreational Products.

As a result of its proximity to the Québec market, the Caisse has an undeniable advantage over its peers when assessing the investment opportunities that arise here. For that reason, it has invested $13.2 billion more than the amount established according to the indexes underlying the investment policies. Its decision to use financial leverage enables it to invest a greater overall amount.

I'd like to add that the Caisse's contribution to the economic development of Québec goes beyond the returns it earns for the depositors and its local investments. The Caisse also generates substantial economic benefits with its operations. In fact, its contribution to economic development is such an important matter that it is discussed fully in its own section of this Annual Report.

MESSAGE FROM THE PRESIDENT AND CHIEF EXECUTIVE OFFICER

Q8.
HOW DO YOU RECONCILE THE NEED TO INVEST IN QUÉBEC WITH THE NEED TO INVEST ABROAD?

The Caisse fulfills its mission not only by making profitable investments here, but also by investing in other countries to earn millions of dollars that it brings back to Québec.

With its considerable assets under management, it must diversify its sources of return and limit the risks of its portfolio, including geographic risk. We need only consider that Canada represents less than 3% of the world's stock market capitalization to realize the importance of investing elsewhere.

The proportion of depositors' total assets invested outside Canada rose to 42% in 2007 and will continue to climb as investment opportunities arise, especially in emerging markets whose growth rates exceed those of Canada and the other industrialized countries. At the same time, the Caisse will continue to identify and to act on business opportunities in Québec, the market it knows best.

Q9.
THE PURPOSE OF THE STRATEGIC PLAN 2006-2008 IS TO MAKE THE CAISSE A BENCHMARK ORGANIZATION. HOW WOULD YOU SUM UP WHAT YOU HAVE DONE TO ACHIEVE THIS AMBITION, AND WHAT ARE YOUR PLANS IN THIS AREA FOR 2008?

In 2007, we made further progress on our four priorities: our investment returns, contribution to Québec's economic development, management framework and operational levers. With respect to our returns, we achieved several of the objectives underlying the creation of the Investment Division, such as co-ordination of asset allocation operations, including research, development of active currency management, formation of internal partnerships and deployment of new investment strategies.

As I've already pointed out, we continued to increase our investments in Québec. We also undertook to report on the Caisse's contribution to the province's economic development, an initiative that will continue in the years to come.

At the same time, we kept improving our management and control structures. The Caisse now has an up-to-date, complete management framework designed to provide the flexibility and agility it needs to fulfill its mission.

Lastly, considerable effort was made to strengthen our operational levers, particularly management of talent and improvements to the operational chain – all the processes that ensure rapid, accurate processing of transactions on the various markets. The operations teams were brought together in the same unit to enhance co-ordination and efficiency. As a result, information technology projects related to investment and operations took priority.

We've planned our action for 2008 in a spirit of continuity. Our priorities include reaching an agreement on third-party ABCP restructuring, as well as optimizing the operational chain, risk management and talent management. We'll also intensify our efforts to communicate with all Caisse stakeholders and continue to reposition our international operations. At the same time, we'll start planning for the period from 2009 to 2011. The objective of our new strategic plan is to build on the Caisse's achievements by drawing on our strengths to fulfill our ambition.

Q10.

HOW DO YOU SEE THE CAISSE, AS WELL AS THE ECONOMY AND THE FINANCIAL MARKETS, PERFORMING IN THE NEAR FUTURE?

First, we should bear in mind that the global environment changed radically in 2007. The liquidity crisis started in August and spread to all the players in the international financial system. It put an end to a long period of growth characterized by historically low interest rates, moderate investment risk premiums and almost non-existent volatility. During this prosperous period, liquidity was abundant and borrowing conditions were favourable, and we witnessed the creation of a spate of increasingly complex, and often increasingly opaque, financial instruments. Then, in mere weeks, liquidity dried up and credit spreads, namely the risk premium for the cost of borrowing, increased sharply.

The financial industry is reeling from this shock and will take some time to recover. So I see 2008 as a transitional year in which financial players will seek a new balance, as well as greater transparency and simplicity. In all likelihood, we'll also see considerable changes affecting credit rating agencies, regulatory frameworks and accounting standards, and the success of these changes will require the utmost co-operation by all industry players.

In the meantime, despite the slowing of the North American economy, the global economy could continue to grow, mainly because of the sustained development of Asia's economic engines. As market globalization proceeds, competition between large investors will only intensify. Moreover, the aging of the population and its impact on the job market and pension fund balance sheets will still be one of the major challenges confronting the Caisse and its depositors.

In this context, we'll closely monitor the U.S. economic downturn and try to take advantage of the investment opportunities it creates. And, since the emerging economies are expected to keep growing rapidly, the Caisse intends to redeploy its investment operations, first in real estate, by setting up local operations in the immense and rapidly growing markets of India and China.

Regardless of the market conditions over the short term, the Caisse will continue to take the long view with its investments, focusing on the future, in line with its depositors' target returns. The theme of our annual report, "Taking the long view for all of us," reflects the spirit of our efforts to position ourselves for the future by investing at home and abroad. We believe this approach holds the promise of sustained returns for the Caisse's depositors and collective wealth for Quebecers.

/ **HENRI-PAUL ROUSSEAU**
President and Chief Executive Officer

EXECUTIVE COMMITTEE

From left:

GHISLAIN PARENT
Executive Vice-President Finance and Operations

SUZANNE MASSON
Executive Vice-President Corporate Affairs and Secretary

CHRISTIAN PESTRE
Executive Vice-President and Chief Strategist

FRANÇOIS GRENIER
Executive Vice-President Equity Markets

FERNAND PERREAULT
Executive Vice-President Real Estate

HENRI-PAUL ROUSSEAU
President and Chief Executive Officer

AMBITION

THE CAISSE STRIVES TO BECOME A BENCHMARK ORGANIZATION AMONG INSTITUTIONAL FUND MANAGERS

NORMAND PROVOST
Executive Vice-President Private Equity

SUSAN KUDZMAN
Executive Vice-President Depositors and Risk

ROBERT W. DESNOYERS
Executive Vice-President Human Resources and Organizational Development

PHILIPPE ITHURBIDE
Executive Vice-President Fixed Income and Currencies

MICHEL MALO
Executive Vice-President Hedge Funds

V.P. PHAM
Executive Vice-President Information Technology

RICHARD GUAY
Chief Investment Officer

FOLLOW-UP ON THE STRATEGIC PLAN 2006-2008

TEAMWORK, RISK MANAGEMENT AND COHERENT EFFORT WERE VITAL IN 2007, NOT ONLY IN A TIME OF CRISIS BUT ALSO IN THE NORMAL COURSE OF BUSINESS. PROGRESS WAS MADE WITH EACH STRATEGIC PRIORITY.

PRIORITIES

RETURN

GENERATE A RETURN THAT MEETS DEPOSITORS' LONG-TERM EXPECTATIONS BY OPTIMIZING INVESTMENT STRATEGIES

See "Returns and financial position"

ECONOMIC DEVELOPMENT

CONTRIBUTE TO QUÉBEC'S ECONOMIC DEVELOPMENT

See "Economic development"

IN 2008, THE CAISSE WILL COMPLETE ITS ORGANIZATIONAL PRIORITIES, INCLUDING THOSE INVOLVING THE OPERATIONAL CHAIN, RISK MANAGEMENT, TALENT MANAGEMENT, AN AGREEMENT ON THIRD-PARTY ABCP, ITS INTERNATIONAL POSITIONING AND COMMUNICATION WITH STAKEHOLDERS. THE YEAR WILL ALSO MARK THE END OF THE STRATEGIC PLAN 2006-2008 AND THE DEVELOPMENT OF A NEW THREE-YEAR PLAN. THE STRATEGIC PLAN 2009-2011 WILL BUILD ON THE CAISSE'S ACHIEVEMENTS BY DRAWING ON ITS STRENGTHS TO ACHIEVE ITS AMBITION.

ACHIEVEMENTS 2007

/ A five-year return of 12.4%, ranking in the first 5% of the comparison universe, namely Canadian pension funds of more than $1 billion.

/ Returns of 5.6% in 2007 and 11.5% over three years, with both ranking in the first decile of large Canadian pension funds.

/ Ranking of the Caisse's investment policies in the first quartile of Canadian pension funds managing more than $1 billion.

/ Significant contribution to added value by the Private Equity, Hedge Funds, Canadian Equity, and Investments and Infrastructures portfolios.

/ Reorganization of the Fixed Income and Currencies group.

/ Concentration of the operations of the Hedge Funds portfolio in a smaller number of external funds for greater transparency.

/ Increase in the assets managed by the Private Equity group, in agreement with the depositors.

/ Presence of the Real Estate group in the four main emerging markets (Brazil, Russia, India and China).

/ Increase in the Private Equity group's total assets in Québec to $6.0 billion with investments in several funds that specialize in all phases of business development.

/ Investments in small businesses, mainly through the AlterInvest Fund, financed equally by the Caisse and the Business Development Bank of Canada.

/ Acquisition of the Château Frontenac in Québec City and the Queen Elizabeth in Montréal, in partnership with Westmont Hospitality Group.

/ Substantial increase in corporate bonds, especially notes issued by financial companies.

/ More than 90% of the Caisse's employees took part in the Centraide/United Way campaign. Donations made by the employees of the Caisse and its real estate units, combined with the matching institutional donations, exceeded $1 million in 2007.

OUTLOOK 2008

/ Capitalize on the reorganization of the Volatility and International Bond teams as well as the creation of the Currencies team in the Fixed Income and Currencies group.

/ Continue to gradually increase internal management of the Foreign Equity portfolio.

/ Place special emphasis on management of the existing portfolios of the Private Equity group, proximity development capital and investment in restructuring funds and distressed loans.

/ Increase real estate investments in emerging markets.

/ Create a real estate debt subsidiary.

/ Continue the venture capital strategy with emphasis on forthcoming fund raising from existing partners.

/ Deploy the capital in the Québec Manufacturing Fund to companies with high potential.

/ Continue to support Québec companies seeking financing.

/ Maintain the partnership with the Collège des administrateurs.

/ Assess and enhance the contribution made by the Caisse to Québec's economic development.

/ Take part in celebrations marking the 400th anniversary of the founding of Québec City.

/ Organize the annual Entretiens Jacques Cartier to be held in Québec City and the meeting of the Group of Montréal.

FOLLOW-UP ON THE STRATEGIC PLAN 2006-2008

PRIORITIES

MANAGEMENT FRAMEWORK

IMPLEMENT A MANAGEMENT FRAMEWORK BASED ON THE CHARACTERISTICS OF A BENCHMARK ORGANIZATION AND LEGAL REQUIREMENTS, PARTICULARLY IN INTERNAL CONTROL, RISK MANAGEMENT AND RESOURCE OPTIMIZATION

See “Management framework”

OPERATIONAL LEVERS

STRENGTHEN THE CAISSE'S OPERATIONAL LEVERS TO OPTIMIZE ITS RESOURCES

See “Operational levers”

ACHIEVEMENTS 2007	OUTLOOK 2008
/ Changes to the organizational structure to make the Caisse more efficient, particularly the operational chain. / Overhaul of the Information Technology Committee. / Revision of delegation of authority. / Continuation of the financial certification project. / Introduction of twice-yearly reporting on self-assessment of optimal resource use. / Update of the policy on socially responsible investment.	/ Develop the Strategic Plan 2009-2011. / Finish implementing the financial certification policy. / Refine the approach to responsible investment on international markets.
HUMAN RESOURCES EXCELLENCE	
/ Start of the program to optimize talent management, with application of the project's first governance rules and a review of the roles of the various teams in the Human Resources and Organizational Development Executive Vice-Presidency. / Introduction of a change-management process for the deployment of 14 priority projects.	/ Complete the projects started in 2007. / Achieve the human resources objectives of each Executive Vice-Presidency, according to the priorities established in its 2008 business plan. / Continue the program to optimize talent management.
RIGOROUS AND DYNAMIC RISK MANAGEMENT	
/ Assessment of the risks of 98 potential investment projects totalling $32 billion. / Identification of key indicators of the Caisse's operational risks. / First stages of optimization of the Caisse's overall risk allocation.	/ Establish a plan to improve risk management on the basis of best practices adopted by the industry. / Further improve the analytical platform and market risk information systems.
LEADING-EDGE RESEARCH	
/ A prestigious international prize awarded by a recognized academic journal. / Revision of the investment policies for most of the Caisse's depositors.	/ Continue research on optimal asset allocation and benchmark indexes.
LEADING-EDGE TECHNOLOGY AND OPERATIONAL EFFICIENCY	
/ Improvements to the operational chain and portfolio management tools.	/ Continue projects involving the operational chain. / Put in place a portfolio management system for the Private Equity group.

TAKING THE LONG VIEW MEANS INVESTING OURSELVES FOR OUR DEPOSITORS

/ **LOUIS-PHILIPPE THIBODEAU**
Senior Portfolio Manager
Telecommunications, Canadian Equities
Equity Markets

RETURNS AND FINANCIAL POSITION

FINANCIAL CERTIFICATION

Pursuant to the Caisse's financial certification policy, the President and Chief Executive Officer and the Executive Vice-President, Finance and Operations, sign a public financial certificate each year.

The two signing authorities responsible for the public financial certificates rely on internal financial certificates signed by various officers of the Caisse and its subsidiaries as well as work carried out under the financial certification program.

I, **Henri-Paul Rousseau, President and Chief Executive Officer** of the Caisse de dépôt et placement du Québec, certify that:

1/ I have reviewed the combined financial statements, the schedules (tables of returns), the press release announcing the annual results and the Annual Report (hereafter referred to as the "Annual Filings") of the Caisse de dépôt et placement du Québec (the "Caisse") for the year ended December 31, 2007.

2/ To the best of my knowledge, the Annual Filings do not contain any untrue statement of a material fact or omit to state a material fact that is required to be stated or necessary to make a statement that is not misleading in light of the circumstances in which it was made, with respect to the fiscal year covered by the Annual Filings.

3/ To the best of my knowledge, the combined financial statements and the other financial information included in the Annual Filings fairly present in all material respects the financial position of the Caisse as at the closing dates of the fiscal years presented in the Annual Filings, as well as the results of its operations for those years.

4/ The Executive Vice-President, Finance and Operations, and I are responsible for establishing and maintaining disclosure controls and procedures and internal control in respect of financial information for the Caisse, and we have:

a) Designed such disclosure controls and procedures, or caused them to be designed under our supervision, to provide reasonable assurance that material information relating to the Caisse, including its subsidiaries, is made known to us by others within those entities, particularly during the period in which the Annual Filings are prepared;

b) Designed such internal control over financial reporting, or caused it to be designed under our supervision, to provide reasonable assurance that the financial information is reliable and that the combined financial statements have been prepared, with a view to publication of the financial information, in accordance with generally accepted accounting principles in Canada;

c) Evaluated the effectiveness of the disclosure controls and procedures as at the end of the fiscal year covered by the Annual Filings and ensured that the Caisse presents in the Annual Report 2007 our conclusions in accordance with our self-assessment.

5/ I have ensured that the Caisse presents in the Annual Report 2007 any material changes in internal control over financial reporting during the fiscal year ended December 31, 2007, that have had or it is reasonable to think may have a material effect on internal control over financial reporting.

President and Chief Executive Officer
/ **HENRI-PAUL ROUSSEAU**

March 28, 2008

I, **Ghislain Parent, Executive Vice-President, Finance and Operations,** of the Caisse de dépôt et placement du Québec, certify that:

1/ I have reviewed the combined financial statements, the schedules (tables of returns), the press release announcing the annual results and the Annual Report (hereafter referred to as the "Annual Filings") of the Caisse de dépôt et placement du Québec (the "Caisse") for the year ended December 31, 2007.

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c) Evaluated the effectiveness of the disclosure controls and procedures as at the end of the fiscal year covered by the Annual Filings and ensured that the Caisse presents in the Annual Report 2007 our conclusions in accordance with our self-assessment.

5/ I have ensured that the Caisse presents in the Annual Report 2007 any material changes in internal control over financial reporting during the fiscal year ended December 31, 2007, that have had or it is reasonable to think may have a material effect on internal control over financial reporting.

Executive Vice-President, Finance and Operations
/ **GHISLAIN PARENT**, CA

March 28, 2008

CONCLUSIONS ABOUT THE DESIGN OF INTERNAL CONTROL OVER FINANCIAL REPORTING

During fiscal 2007, the Disclosure Committee oversaw work that involved mainly completing the documentation for certain controls, updating existing documentation and evaluating the design of internal control over financial reporting for the Caisse's main financial processes.

The evaluation of the design of internal control over financial reporting was carried out with the framework usually adopted by North American companies, namely that of the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The work carried out enabled the Disclosure Committee to conclude that internal control over financial reporting is designed to provide reasonable assurance that the financial information presented is reliable and that the combined financial statements of the Caisse were prepared in accordance with generally accepted accounting principles in Canada.

Caisse management also carried out work that enabled it to determine that during the year ended December 31, 2007, no changes were made in internal control over financial reporting that would have had a material negative effect.

In the year to come, work will continue to ensure the last phase of implementation, namely evaluation of the effectiveness of internal control over financial reporting. In that regard, the Canadian Securities Administrators (CSA) announced in November 2007 that it would defer the effective date of the obligation to disclose the results of this last phase, initially for financial years ending on or after June 30, 2008. The new effective date should be announced in 2008. The Caisse will deploy its process for evaluation of the effectiveness of its controls in 2008 so as to be prepared to publicly certify their effectiveness when required to do so and will continue to stress the importance of this last phase within the organization.

CONCLUSIONS ABOUT THE EFFECTIVENESS OF THE DISCLOSURE CONTROLS AND PROCEDURES

In accordance with the Caisse's financial certification policy, the effectiveness of the disclosure controls and procedures pertains to the Annual Filings, namely the combined financial statements, the schedules (tables of returns), the press release announcing the annual results and the Annual Report.

In addition to work involving internal control over financial reporting, the Disclosure Committee supervised work to update existing documentation and work concerning evaluation of the design and effectiveness of the disclosure controls and procedures.

As at December 31, 2007, this evaluation confirms that the disclosure controls and procedures are effective and provide reasonable assurance that all relevant information is gathered and submitted in a timely fashion to senior management, in particular to the President and Chief Executive Officer and to the Executive Vice-President, Finance and Operations, so that the appropriate decisions concerning disclosure can be made.

The Board of Directors also approved the 2007 Annual Filings before their public disclosure.

ASSET-BACKED COMMERCIAL PAPER

The asset-backed commercial paper (ABCP) crisis had an impact on the Caisse's operations and return in 2007. The unfolding of this unusual event and its impact on the Caisse are discussed in several sections of the Annual Report.

WHAT IS ASSET-BACKED COMMERCIAL PAPER?

Asset-backed commercial paper is a sophisticated variant of the commercial paper issued by businesses and institutions. It consists of short-term debt that institutional investors, as well as certain companies, purchase to earn a return on their liquid assets. ABCP differs from other types of commercial paper in that it is issued by trusts structured by large banks or by trusts structured by independent brokers, in which case it is called "third-party ABCP." Another characteristic of ABCP is that it is guaranteed by a portfolio of underlying assets, essentially debt.
The ABCP has been divided into three categories according to the underlying assets:

- Traditional ABCP, whose underlying assets are mortgages, credit card receivables, auto loans, etc.;
- Synthetic and hybrid ABCP, whose underlying assets include derivatives, mainly credit default swaps, and which usually involve leverage; and
- High-risk ABCP, whose underlying assets are U.S. subprime residential mortgages.

THE ABCP CRISIS

The collapse of the U.S. subprime residential mortgage market had a spillover effect in Canada in that it undermined investor confidence in all ABCP and its underlying debt, although the exposure to this type of loan was very limited. This crisis of confidence caused demand for ABCP to dry up. The mainly foreign banks that should have stepped in to maintain the liquidity of the third-party ABCP market instead invoked a clause of Canadian regulation to avoid honouring their commitments.

For more details, see the section "Market context 2007."

RESTRUCTURING PLAN

The objective of the memorandum of agreement announced by the Pan-Canadian Investors Committee is to enable a very large number of investors to recover most of their investments on maturity. It makes it possible to avoid a forced liquidation that would have entailed substantial losses for all holders of third-party ABCP and seriously disrupted Canada's financial markets. The agreement covers 20 trusts totalling $33 billion.

MANAGEMENT OF LIQUID ASSETS

The Caisse used third-party ABCP in the management of its liquid assets. It manages substantial amounts of liquid assets primarily to be able to act rapidly when promising investment opportunities arise, especially in private equity and real estate. The assets are also used to meet depositors' short-term requirements.

The considerable holdings of third-party ABCP are due to the net increase in funds to be invested from certain specialized portfolios, the intention to create value added with surplus liquid assets and Canada's relative scarcity of short-term debt securities.

VALUATION OF THE CAISSE'S INVESTMENTS IN THIRD-PARTY ABCP BEING RESTRUCTURED

As at December 31, 2007, the Caisse held $12.6 billion of third-party ABCP being restructured with a fair value estimated at $10.7 billion. The difference of $1.9 billion, or 15%, represents an unrealized decrease in value that had an adverse impact on the financial results for 2007. The estimate of fair value was established according to the guidelines of the Canadian Institute of Chartered Accountants (CICA).

For more details, see the "Analysis of combined financial statements," including the section on the "Investment valuation process," and note 4B, "Investments and liabilities related to investments."

IMPACT OF THE UNREALIZED DECREASE IN VALUE ON RETURNS

The $1.9-billion unrealized decrease in value lowered the Caisse's overall return for 2007 by 1.3%, taking it from 6.9% to 5.6%. This unrealized decrease in value is due to the liquidity crisis that began on Canada's ABCP market in August 2007.

For more details, see the "Summary of the Caisse's overall performance."

MARKET CONTEXT 2007

HIGHLIGHTS

/ **Liquidity crisis:** A liquidity crisis, caused mainly by the subprime mortgage debacle in the United States, began in August 2007. This crisis disrupted the global financial markets, leading to a general repricing of risk and tighter credit conditions.

/ **Economy:** The global economic expansion remained vigorous until the third quarter. As a result of the residential real estate crisis, the U.S. economy slowed significantly in the fourth quarter. The credit crunch and the increased risk of a recession prompted the U.S. Federal Reserve to begin a cycle of cuts to its key rate in September. As for emerging markets, they continued to grow at a rapid pace, pushing up food and energy prices. The rapidly rising price of oil helped propel the Canadian dollar above parity with the U.S. dollar in the fourth quarter. The loonie's new strength, combined with slowing demand in the United States, was detrimental to the manufacturing sector in Ontario and Québec.

/ **Liquid markets:** The onset of the liquidity crisis in August 2007 roiled the financial markets. On the bond markets, credit spreads widened, the spreads between short- and long-term interest rates widened and volatility returned. The stock markets experienced two corrections, in August and November, but were generally up at year-end.

/ **Private equity:** The leveraged-buyout market continued to be frothy in the first half of the year; after only six months, the total transaction value exceeded the previous annual record, set in 2006. Dysfunction on the structured-credit market swiftly curtailed this activity in August 2007. The credit crunch in the second half had not yet put a damper on institutional investors' enthusiasm for infrastructure, considered much less volatile.

/ **Real estate:** The liquidity crisis caused commercial real estate investment to slow. During the year, the fundamentals underpinning the office building and shopping centre markets remained generally sound, especially rents and property values, but tighter lending standards and the repricing of risk had a significant impact on the value of real estate debt securities.

GLOBAL MARKETS HIT BY A LIQUIDITY CRISIS

THE SLUMPING U.S. RESIDENTIAL MARKET ROILS THE FINANCIAL MARKETS

As in previous years, the economic and financial environment in the first half of 2007 was characterized by strong global economic growth, moderate interest rates, tame inflation, abundant capital, low volatility and strong correlation between the markets around the world. In this context, assets continued to appreciate, and the related risk premiums contracted further.

For several years, this environment was conducive to credit supply and demand alike. Lenders provided loans on increasingly favourable conditions. Securitization was used to spread the risks to third parties attracted by superior returns. Original debt securities, such as mortgages, credit-card balances and car loans, were pooled, packaged and sold to investors in the form of more complex structured financial products. The return on these products – including asset-backed commercial paper (ABCP) issued to finance the purchase of debt securities or debt-backed structured products – depended on the credit ratings assigned by the rating agencies. Certain vehicles that received the agencies' top rating were in fact exposed to very risky debt that could contaminate the financial structure of their products.

During the year, the excesses of the residential real estate markets in the United States brought to light the fragility of the market for structured-credit instruments. In 2005 and 2006, for example, more than 20% of the new mortgages issued in the United States were subprime. Through securitization, this high-risk mortgage debt made its way, along with other debt, throughout the global financial system, within hedge funds or structured investment vehicles that were often complex and opaque, so that it was difficult to quickly identify the ultimate holders of the risks and the losses associated with subprime mortgages.

In 2007, the slumping U.S. residential real estate market pushed up default rates and foreclosures for houses financed by subprime mortgages, causing writedowns of the securities backed by such debt. In June, the rating agencies began to downgrade securities backed by U.S. subprime mortgages. The sudden downgrades led the same month to the collapse of two Bear Stearns hedge funds. This development pointed up the increasing illiquidity of securities supported by debt and structured products, regardless of whether they were backed by subprime mortgages. These products were so opaque that it was hard to determine whether they had subprime exposure. Investors' growing aversion to risk therefore had a widespread contagion effect on all structured products. Investors began to fear that other funds and investment vehicles would have to write down their holdings in a depressed market and take heavy losses, prompting other investors using leverage to sell massive quantities of structured securities to meet margin calls. Liquidity on the secondary market for these securities quickly dried up in the summer.

THE LIQUIDITY CRISIS ERUPTS IN AUGUST 2007

On August 9, BNP Paribas announced it had frozen three of its funds, saying it could no longer value them accurately because of the illiquid market for structured products. The announcement was one of the triggers of a global liquidity crisis, leading to a general repricing of risk by the financial markets. Investor confidence in the credit markets evaporated, and the market for structured products seized up almost overnight, forcing several central banks to inject large amounts of liquidity to re-establish overnight financial operations.

Activity on the secondary markets for leveraged-buyout loans suddenly ended, forcing banks to keep such loans on their balance sheets. As well, demand for ABCP dried up in a few days, regardless of whether the paper was exposed to assets posing a real credit problem. Maturing ABCP had difficulty finding buyers. To reimburse investors, issuers of ABCP turned to the institutions that had given them liquidity guarantees, since the current income from their long-term debt securities could not cover their short-term liquidity needs. The banks that had provided these liquidity facilities had to transfer a portion of the unsold ABCP onto their balance sheets, as investors were extremely reluctant to purchase it, even when higher returns were offered.

In Canada, in the overwhelming majority of cases, the ABCP was backed by quality debt securities. The market therefore experienced above all a general liquidity crisis, as opposed to a crisis related directly to the poor quality of subprime mortgages. In the case of ABCP issued by trusts structured by the banks, the market continued to function, since the banks honoured their liquidity guarantees with support from the Bank of Canada. The situation was different for ABCP issued by trusts structured by independent brokers. They had liquidity guarantees provided mainly by foreign banks. When Coventree, the largest of the independent brokers, announced on August 13 that it could not roll over its maturing commercial paper, the guarantor banks refused to provide the requested liquidity. They said that the conditions obliging them to assist trusts in difficulty, namely a general market disruption, were not present. The main players in the third-party ABCP market quickly agreed to a standstill agreement, called the Montréal Accord, with the objective of reviewing the events that triggered the crisis, limiting future investment and converting the matured ABCP into long-term notes with maturities matching those of the underlying assets.

A SHOCK THAT WILL HAVE A PROFOUND IMPACT ON THE FINANCIAL SYSTEM

The liquidity crisis had a considerable impact on banks around the world. Their balance sheets rapidly deteriorated, especially in the United States, but also to various degrees elsewhere in the world. Banks became reluctant to lend to one another, which prompted central banks to infuse large amounts of liquidity into the banking system to ease tensions on the money markets. The banks also decreased their loan volume and tightened their lending standards. Next, they announced significant losses related to subprime mortgages, which drove the stock markets down further in the fall. Finally, they began recapitalizing, partially with infusions from investment funds in Asia and oil-exporting countries.

MARKET CONTEXT 2007

The financial crisis showed clearly that widespread use of products that lack transparency, are poorly understood by investors and are structured by non-bank intermediaries subject to inadequate regulation poses risks for the long-term stability of the financial system. It also revealed the need to review the models used to assess the risks associated with sophisticated financial instruments, especially those of the rating agencies. The crisis also highlighted, more than ever before, the need for international co-ordination by monetary and government authorities to ensure stable, efficient financial markets. Lastly, the crisis could mark the start of a greater presence by investment funds in Asia and oil-exporting countries as shareholders of Western companies, given the very large amounts of capital at their disposal.

ECONOMIC SLOWDOWN IN THE INDUSTRIALIZED COUNTRIES AND RAPID ECONOMIC EXPANSION IN EMERGING MARKETS

GLOBAL EXPANSION CONTINUES

The global economy saw vigorous expansion until the third quarter. The slowdown began in the fourth quarter in the industrialized countries, especially in the United States. As for emerging markets, their growth was just as rapid as in 2006, pushing up the price of many commodities, including oil, which peaked at close to $100 a barrel, as well as grains and oilseeds. Global inflation came under upward pressure, mainly because of rising energy and food prices. Gold, regarded as a safe haven, benefited from the financial turmoil and the weak U.S. dollar.

NORTH AMERICA

The effects of the bursting of the real estate bubble, which began in 2006, are still being felt in the United States. Further contraction of residential investment was the main damper on economic growth once again in 2007. Although housing starts plummeted, the imbalance on the real estate market remained pronounced: foreclosures are rising, inventories of unsold houses are climbing and lending conditions are getting tighter. As a result, housing prices were down nationally; falling property values helped undermine consumer confidence and, no doubt, curtail consumer spending. As a result of the slowdown, the weak dollar and strong global demand, net exports contributed significantly to growth in the second and third quarters, reducing the U.S. current account deficit.
The financial turmoil that began in the third quarter, the significant downturn expected in the fourth quarter and concerns that the credit crunch would plunge the country into a recession in 2008 prompted the Federal Reserve to begin cutting interest rates quickly in September, despite ongoing inflationary pressures fuelled above all by rising energy prices. The Fed lowered its key rate from 5.25% to 4.25% in three months.

In Canada, a strong job market, characterized by one of the lowest unemployment rates of the past 33 years, and business investment contributed to strong domestic demand. Still, the high-flying Canadian dollar, combined with the sluggish U.S. economy, pushed net exports down in the second half of the year and slowed the country's economic growth. The loonie soared more than 17% against the greenback, which also pushed down consumer prices (figure 1). Tighter credit conditions and the risk of a recession south of the border caused the Bank of Canada to abandon its policy of monetary tightening; it opted to lower its key rate by a quarter of a percentage point at its December meeting.

Canada's economic growth was again uneven. Québec and Ontario, the provinces where the manufacturing sector is concentrated, saw their economies expand more slowly than those of the provinces endowed with natural resources.
The soaring loonie and slowing demand in the United States combined to push down Québec's exports, slashing the province's economic growth rate and causing new losses of manufacturing jobs, especially in the forestry sector. The share of manufacturing jobs in total employment is therefore decreasing, as it is in all industrialized countries. It fell below 15% in 2007, a proportion similar to the level in Ontario but higher than that of the other provinces and the United States. Still, outstanding employment growth in the other sectors led to net creation of 100,000 jobs in Québec during the year, so that the unemployment rate fell to 6.9%, its lowest level since 1974.

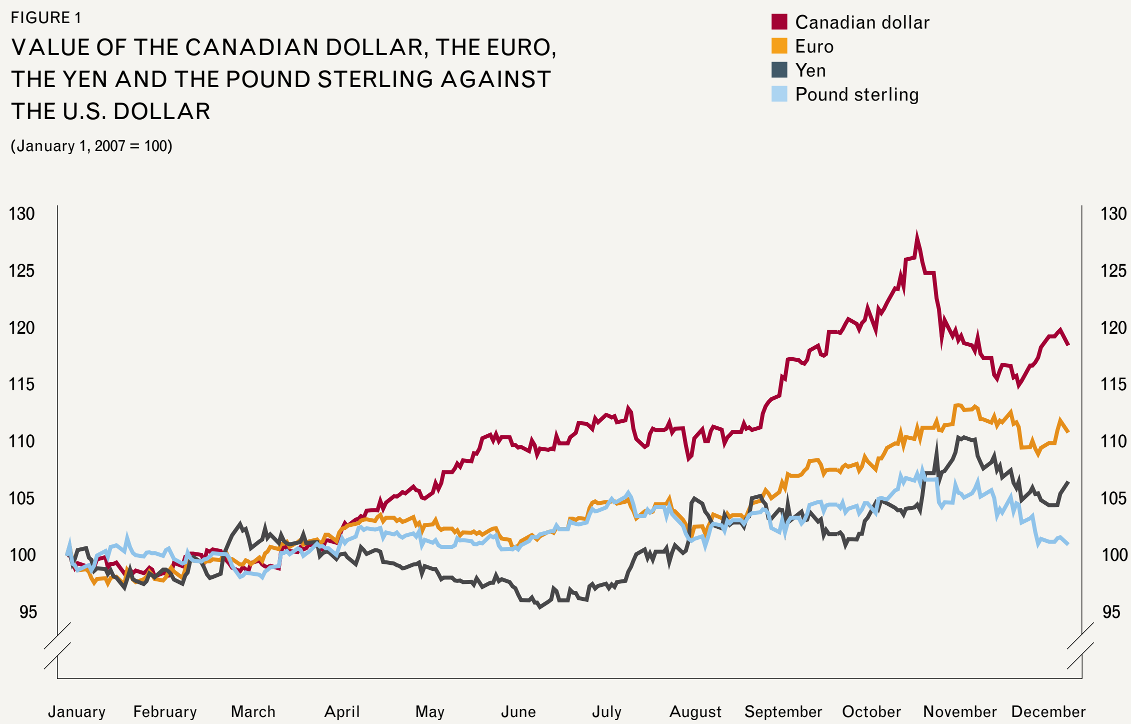
EUROPE

The European Central Bank (ECB) continued to apply a policy designed to contain the potentially inflationary impacts of strong consumer spending growth in the euro zone. It raised its key rate early in the year and stood pat thereafter, despite the financial crisis. Whereas the Fed responded to the crisis mainly by lowering its rates, the ECB preferred to inject massive amounts of liquidity into the banking system.
Although the euro was up more than 10% against the greenback in 2007, external trade continued to make a significant contribution to growth, especially in the third quarter. The Bank of

FIGURE 1

VALUE OF THE CANADIAN DOLLAR, THE EURO, THE YEN AND THE POUND STERLING AGAINST THE U.S. DOLLAR

(January 1, 2007 = 100)



Sources: Caisse de dépôt et placement du Québec, Bank of Canada

England responded to the financial crisis by reversing its monetary policy at the end of the year. It had raised its key rate by 0.75% in the first three quarters to contain overheating caused by solid domestic demand. But the slumping real estate sector and the easing of inflationary pressures in the fourth quarter gave it enough leeway to ease in December. The gains recorded up to that point by the pound sterling against the U.S. dollar were therefore almost completely wiped out toward the end of the year.

ASIA

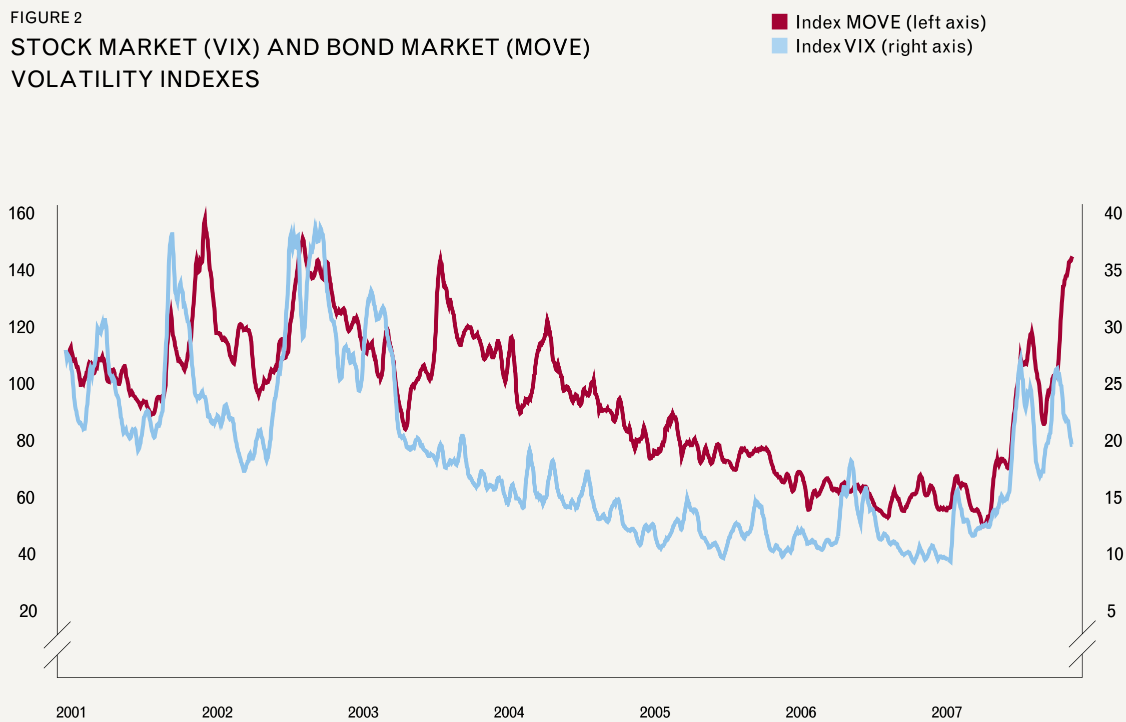
Japan's manufacturing sector was quite robust, especially in the second half of the year. The country saw growth but is still grappling with an inflation rate that is essentially zero, which prompted the central bank to keep its key rate unchanged at 0.50%. The yen was up more than 6% against the U.S. dollar, starting in August. Its relative strength is due partly to the narrower interest rate spread between the two countries, but the financial turmoil of the last five months was also a factor. It considerably reduced investors' appetite for risk, which decreased the carry trade – the practice of borrowing at a low rate, in Japan for example, and then investing the funds in securities that are denominated in another currency and offer a higher return. The carry trade tends to push down the yen, while unwinding such positions has the opposite effect.

In China, despite all the measures taken to cool the red-hot economy, such as repeated interest rate hikes and increases in financial institutions' obligatory reserve coefficients, growth exceeded 10% for the fifth straight year. Surging food prices pushed inflation up during the year. The price increases for other consumer goods were modest, but the authorities responded just the same by introducing administrative measures to limit price hikes. The renminbi was up more than 6% against the greenback.

MARKET CONTEXT 2007

FIGURE 2

STOCK MARKET (VIX) AND BOND MARKET (MOVE) VOLATILITY INDEXES



Sources: Caisse de dépôt et placement du Québec, Bloomberg

TURBULENCE IN LIQUID MARKETS

BOND MARKETS

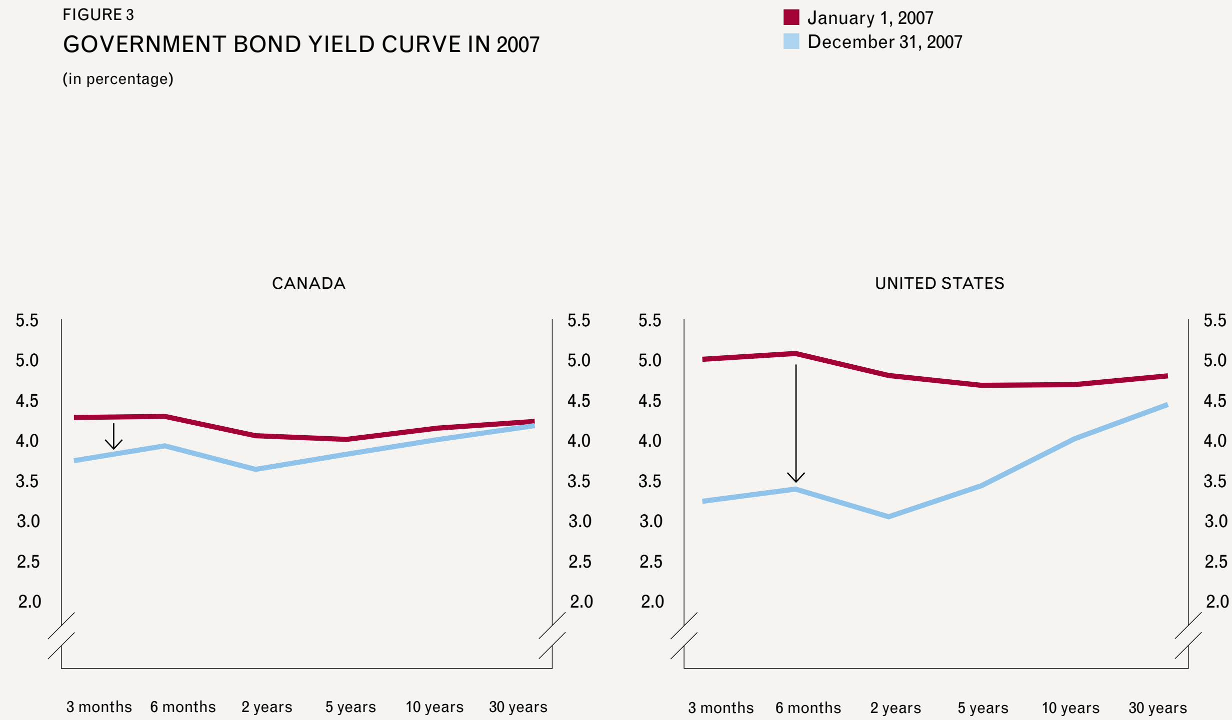
The liquidity crisis also roiled the bond markets in August 2007. From that point, the bond markets saw renewed volatility, less market correlation, much wider credit spreads and steeper yield curves (figure 2).

The money market, which until then had been very stable, was thrown into turmoil in August, when the liquidity for structured products dried up. Investors shunned commercial paper in favour of safe securities, such as U.S. treasury bills. The amount of outstanding commercial paper, including ABCP, fell by several hundred billion dollars. Banks that had provided liquidity facilities to issuers took onto their balance sheets a large portion of this paper, some of it contaminated by subprime mortgages. Liquidity became precious for the banks, which were reluctant to lend to one another. The spreads between LIBOR interbank rates and treasury bills widened considerably, especially in August and November.

FIGURE 3

GOVERNMENT BOND YIELD CURVE IN 2007

(in percentage)



Sources: Caisse de dépôt et placement du Québec, Bloomberg

After a continual, synchronized rise in rates during the first half of the year, government bonds also served as a safe haven for investors in the last five months. During that period, bond portfolios made gains in Europe and North America, although the returns were lower in the euro zone because of the ECB's more restrictive monetary policy. The more vigorous monetary policy of the Federal Reserve and the appeal of U.S. government securities in a time of crisis enabled U.S. bond portfolios to outperform Canadian bond portfolios. The drop in long-term rates was accompanied by an even more pronounced drop in short-term rates. The yield curve once again became positive in North America. The steepening was less pronounced in Canada than it was in the United States, the epicentre of the economic and financial shockwaves (figure 3).

In Canada, the financial crisis caused a widening of the spreads between bonds issued by Québec and the other provinces and those of the federal government. Similarly, the rush into safe bonds caused corporate bonds to suffer. Credit spreads, namely the difference between the yield on these bonds and that of government bonds, widened for the first time in several years, reaching levels not seen since 2001, a recession year.

STOCK MARKETS

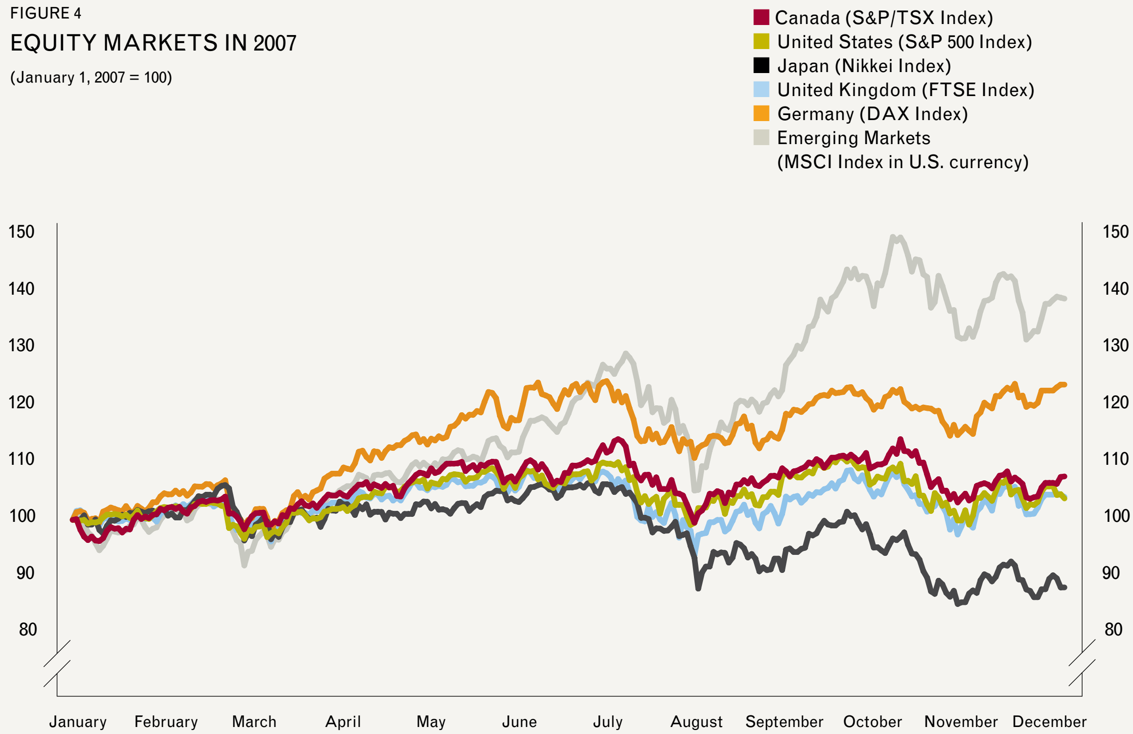
Amid strong global growth and low volatility, the stock markets made substantial, synchronized gains in the first half of the year. The Canadian market was driven partially by mergers and acquisitions. The markets were then shaken by the financial turmoil. The indexes became extremely volatile and experienced two sharp corrections, the first in August and the second in November.

MARKET CONTEXT 2007

FIGURE 4

EQUITY MARKETS IN 2007

(January 1, 2007 = 100)



Sources: Caisse de dépôt et placement du Québec, Bloomberg

In August, in the midst of the subprime crisis, investors had to cope with a sudden repricing of risk and a resumption of market volatility (figure 2). They turned massively to the safest securities, especially treasury bills, but also longer-term bonds, causing the stock markets of the main industrialized countries to plummet. The Federal Reserve's rate cut in September and the announcement of unexpectedly positive economic news enabled the markets to rally to new heights in October. As the banks began reporting unexpectedly high losses related to the subprime crisis, investors began a further repricing of risk that caused prices to fall sharply again in November. In this context of uncertainty and fear of a recession in the United States, the gains recorded in December after the second correction were modest and did not offset the losses incurred in November. The financial services sector was hit especially hard. It had benefited tremendously from the growth of structured finance, a sector that is virtually at a standstill today.

Generally speaking, the equity markets in the industrialized countries recorded gains in 2007, with the notable exception of Japan, which fell more than 10%. The Canadian markets, which were less affected by the difficulties in the financial sector, made more substantial gains than the U.S. markets. Canada's indexes benefited from a strong performance by the energy and materials sectors. In emerging markets, the stock markets posted very high annual returns, despite the financial turmoil of the second half of the year (figure 4). These markets, at first strongly correlated with those of the industrialized nations, took off in mid-August after a severe correction. The strength of emerging stock markets was reassuring to the proponents of the "decoupling" thesis, who hold that rapid growth in China and India is being driven by increasingly independent structural forces that give them considerable immunity against a slowdown in the United States.

REVERSAL OF THE PRIVATE EQUITY CYCLE

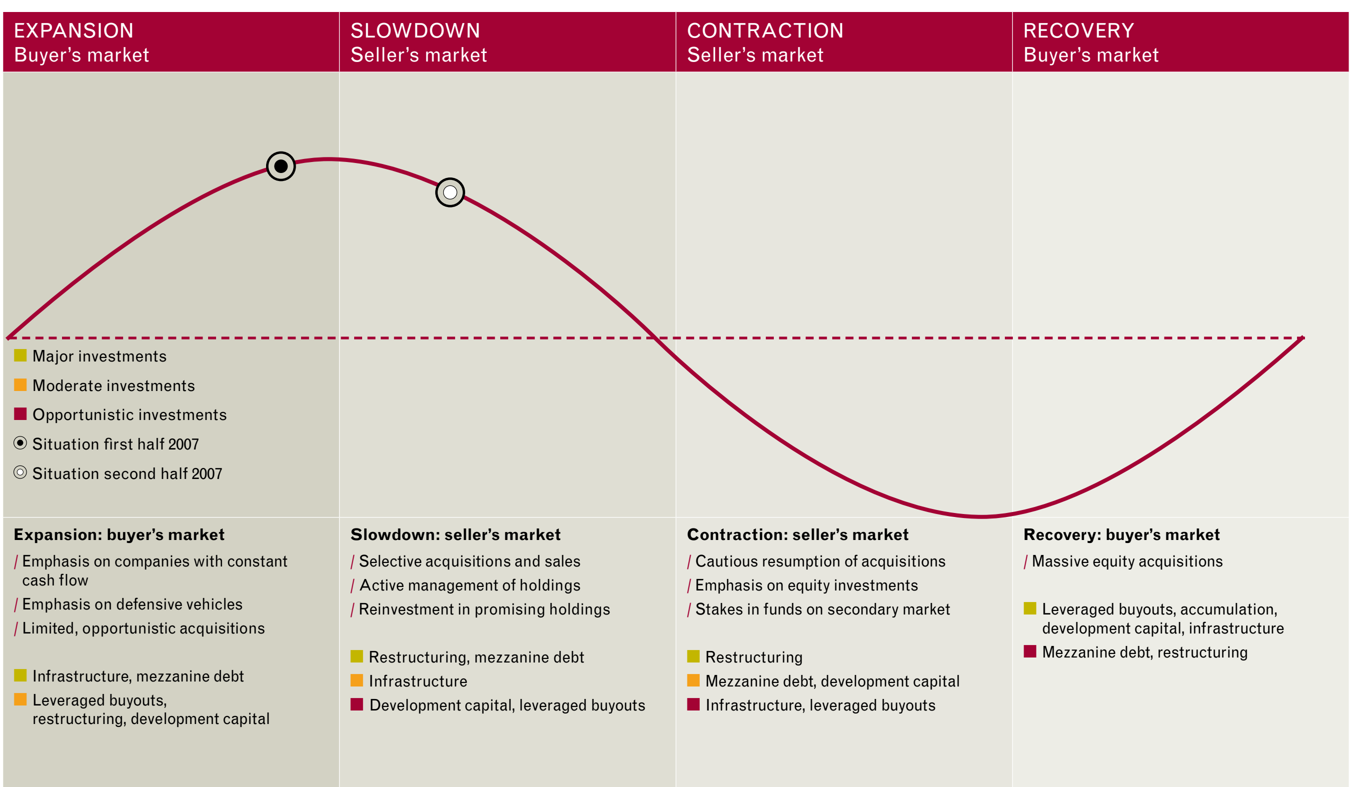
Abundant capital and institutional investors' enthusiasm for non-traditional investments, in an environment of low volatility and moderate interest rates, have caused inflows into leveraged-buyout funds to rise considerably since 2003. This trend continued into 2007. After only six months, the total value of these transactions exceeded the previous annual record, set in 2006. The onset of the liquidity crisis in August abruptly ended this enthusiasm. The higher cost of debt and rising risk premiums limited the credit available to finance leveraged acquisitions. Structured finance, which is vital for transactions in this market segment, slowed significantly in the second half. As a result, $150 billion of debt still had not found takers at year-end, and the market for new leveraged deals was essentially at a standstill.

Money continued to flow into venture capital funds. Moreover, the credit crunch in the second half had not yet dampened institutional investors' enthusiasm for infrastructure, whose characteristics are conducive to a matching of stable future income with financial obligations spread over a long period. Competition between the many institutional investors, which often are not affected by liquidity constraints, kept prices high in this segment of the market.

The onset of the liquidity crisis in August 2007 therefore caused a reversal of the private equity cycle, as shown by figure 5. This reversal was conducive to inflows into distressed-debt and restructuring funds, and prompted investors to be more selective in the case of infrastructure and development capital.

FIGURE 5

PRIVATE EQUITY CYCLE



MARKET CONTEXT 2007

REAL ESTATE SECTOR

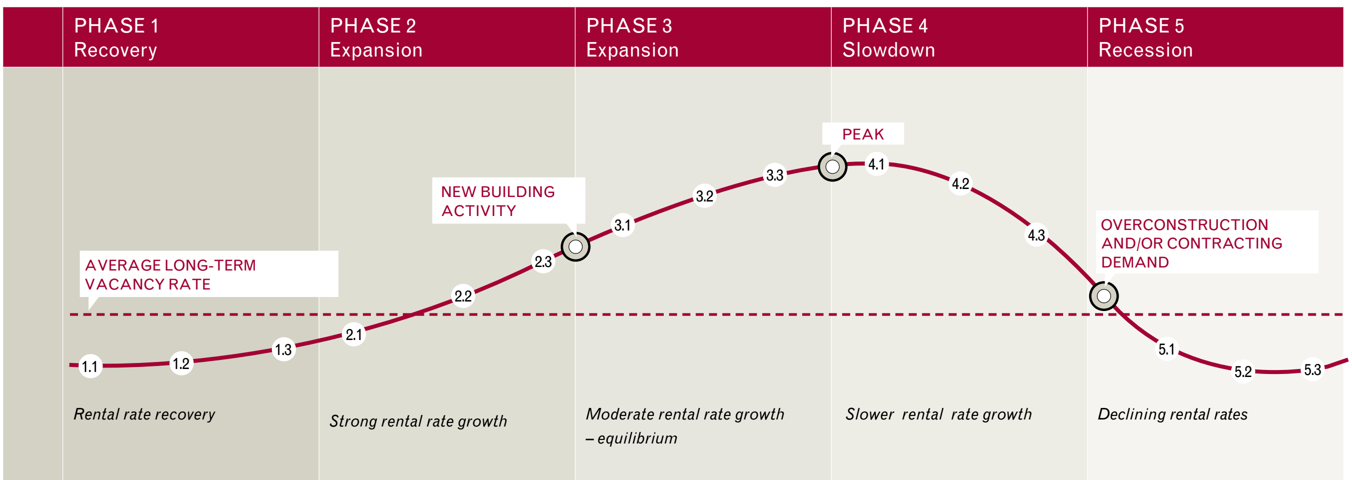
The year saw a reversal on the U.S. residential real estate market, which was shaken by the subprime crisis and in turn had a profound impact on the U.S. economy and the international financial system. The crisis of confidence and tighter lending conditions accelerated the transition from an abundance of capital to a liquidity crisis affecting real estate investment. This situation comes after several boom years characterized by low financing costs over a historically long period and a significant increase in prices as a result of the institutional and global nature of this investment sector.

In contrast to other reversals of the real estate cycle, this time the fundamentals underpinning leasing operations and construction of rental properties remained generally sound in the office building and shopping centre sectors. Rents continued to rise, with the exception of a few real estate markets and products, and vacancy rates were down. Moreover, certain markets, such as Western Canada, saw strong growth, whereas others, such as China and India, looked increasingly attractive. Lastly, despite the subprime crisis, the funds available for real estate remain abundant. As a result, although property values declined amid the credit crunch in the second half, capitalization rates were down only slightly for the year as a whole. The same cannot be said for real estate debt securities, however. They were hit by a general repricing of risk and widening credit spreads, even though non-residential real estate posted delinquency rates below historic levels.

Figure 6 shows the positioning, in the real estate cycle, of the real estate sectors in several regions of the world at the end of 2007. The markets advanced rapidly in 2007 and, in certain cases, are in a declining phase as a result of the overall increase in construction activity and softening demand at year-end, particularly in the shopping centre sector in the United States and the United Kingdom. Most of the emerging real estate markets, especially those of the BRIC countries (Brazil, Russia, India and China), entered an expansion or growth phase, which is expected to be sustained. Some of their submarkets (cities) may see corrections over the short and medium terms, however.

FIGURE 6

POSITIONING OF CERTAIN REGIONS WITHIN THE GLOBAL COMMERCIAL REAL ESTATE CYCLE AT THE END OF 2007



	PHASE 1 Recovery	PHASE 2 Expansion	PHASE 3 Expansion	PHASE 4 Slowdown	PHASE 5 Recession
DEVELOPED MARKETS		**2.1** / Office (United States suburbs, Germany, Québec) / Commercial (Germany) / Industrial (United States warehouse) **2.2** / Multiresidential (United States) **2.3** / Office (Ontario) / Commercial (Japan)	**3.1** / Office (Japan) / Hotel (Canada) **3.2** / Office (United States, Western Canada, continental Europe ex Germany) / Commercial (Canada, France) / Hotel (continental Europe, United Kingdom) **3.3** / Commercial (Spain) / Hotel (United States) / Industrial (Canada) / Multiresidential (Canada)	**4.2** / Office (United Kingdom) / Commercial (United States) **4.3** / Commercial (United Kingdom)	
EMERGING MARKETS	**1.3** / Office (Argentina) / Commercial (India) / Industrial (Brazil)	**2.1** / Office (Mexico, Brazil) **2.2** / Commercial (Brazil) **2.3** / Office (Central Europe) / Commercial (Mexico) / Industrial (Mexico, China) / Multiresidential (Brazil, India)	**3.1** / Office (India) / Hotel (India) **3.2** / Commercial (China,[1] Central Europe, Russia) **3.3** / Office (China,[1] Russia) / Hotel (China) / Multiresidential (China)		

1 Mainly the Shanghai market.

SUMMARY OF THE CAISSE'S OVERALL PERFORMANCE

THE CAISSE OBTAINED AN OVERALL RETURN OF 5.6% IN 2007, ADDING $7.9 BILLION TO DEPOSITORS' NET ASSETS

This return includes a provision of $1.9 billion for investments in third-party asset-backed commercial paper (ABCP) being restructured. Even so, it ranks in the first decile of the comparison universe of large Canadian pension funds. For the three- and five-year periods ended December 31, 2007, the Caisse also stands out, with returns of 11.5% and 12.4% respectively.

SUMMARY OF THE CAISSE'S OVERALL PERFORMANCE

INVESTMENT-POLICY ADVISORY SERVICES

The Caisse offers the depositors investment-policy advisory services that include proposing a benchmark portfolio consisting of various asset classes.

INVESTMENT POLICIES

The investment policy is the document that describes the depositor's situation and requirements, target returns, risk tolerance, benchmark portfolio and investment horizon.

BENCHMARK PORTFOLIOS

The Caisse works closely with its depositors mainly through macroeconomic analyses as well as risk, return and correlation forecasts for the specialized portfolios.

On the basis of each depositor's target returns and risk tolerance, the experts at the Caisse propose various asset allocation scenarios to establish the optimal risk-return ratio.

The scenario that is selected by the depositor becomes its target asset allocation, or benchmark portfolio. It specifies the upper and lower limits for each asset class to control active management of asset allocation by the Caisse's managers. The composition of the benchmark portfolio is then monitored on a regular basis and reviewed on the basis of the risk and return forecasts prepared by the Caisse's specialists.

CAISSE'S BENCHMARK PORTFOLIO

The Caisse's benchmark portfolio is the weighted combination of the depositors' benchmark portfolios.

HIGHLIGHTS

- With a 5.6% overall return, the Caisse ranks in the first decile of large Canadian pension fund managers.
- The overall return includes a $1.9-billion unrealized decrease in value (provision) as a result of the liquidity crisis that occurred on Canada's third-party asset-backed commercial paper (ABCP) market.
- The individual returns for the Caisse's seven main depositors range from 5.1% to 6.6%.
- The value added of the Caisse's portfolio managers is 72 b.p. (0.72%) before the provision for the ABCP investments. After the provision, the value subtracted is 57 b.p. (0.57%).
- Net investment results of $7.9 billion and net deposits of $4.0 billion increased depositors' net assets from $143.5 billion as at December 31, 2006, to $155.4 billion as at December 31, 2007.

COMPOSITION OF THE BENCHMARK PORTFOLIO AND CHANGES IN THE OVERALL PORTFOLIO

Table 7 shows the composition of the Caisse's benchmark portfolio as at December 31, 2007, as well as the effective allocation of the overall portfolio at year-end 2006 and 2007.

COMPOSITION OF THE BENCHMARK PORTFOLIO

The gradual increase in the weighting of the portfolios of non-traditional assets in the Caisse's benchmark portfolio began in 2004 and continued in 2007. These portfolios, categorized as "other investments," represented 33.7% of the benchmark portfolio as at December 31, 2007, for an increase of 4.8% during the year. Conversely, the weighting of the portfolios holding fixed income and publicly traded equities decreased by 2.8% and 2.0%, respectively.

COMPOSITION OF THE OVERALL PORTFOLIO

The difference between the composition of the overall portfolio and the benchmark portfolio as at December 31, 2007, is due to asset allocation and investment decisions made by the Caisse's managers. At that date, the weighting of the portfolios holding publicly traded equities and non-traditional assets was higher in the overall portfolio than it was in the benchmark portfolio.

The weighting of the specialized Private Equity, Real Estate Debt and Real Estate portfolios increased considerably in 2007, which explains the growth of non-traditional assets (other investments) from 32.6% to 35.1% in the overall portfolio.

TABLE 7

CHANGES IN THE COMPOSITION OF THE BENCHMARK PORTFOLIO

Specialized portfolio	Benchmark portfolio as at December 31, 2007			Caisse's overall porfolio as at December 31, 2007	Caisse's overall porfolio as at December 31, 2006
	Lower limit %	Benchmark portfolio %	Upper limit %	%	%
Fixed Income and Currencies					
Short Term Investments	0.2	1.4	9.1	1.5	1.9
Real Return Bonds	0.2	0.8	2.3	0.6	0.7
Bonds	21.7	27.4	34.4	25.4	25.2
Long Term Bonds	1.7	2.4	3.6	2.0	2.2
Subtotal		**32.0**		**29.5**	**30.0**
Equity Markets					
Canadian Equity	7.6	12.2	17.8	12.9	13.2
U.S. Equity	0.2	3.7	7.5	4.4	5.1
Foreign Equity	1.0	5.8	8.2	6.4	6.6
Emerging Markets Equity	0.3	3.1	5.0	3.2	3.0
Québec International	6.7	9.5	12.9	9.4	9.2
Subtotal		**34.3**		**36.3**	**37.1**
Other investments					
Investments and Infrastructures	3.0	5.4	8.8	4.1	6.1
Private Equity	5.1	7.9	10.6	7.3	5.7
Real Estate Debt	2.4	6.5	10.4	7.4	6.3
Real Estate	5.8	9.1	12.5	11.3	9.9
Hedge Funds	0.4	2.9	5.1	3.4	3.0
Commodities	0.0	1.9	3.4	1.6	1.6
Subtotal		**33.7**		**35.1**	**32.6**
Asset allocation and other	0.0	0.0	1.0	0.3	0.3
ABCP	–	–	–	(1.2)[1]	–
Total		**100.0**		**100.0**	**100.0**

1 To track its investments in third-party ABCP more effectively, the Caisse has decided to separate its reporting on this matter from that on management of the specialized portfolios.

N.B.: The benchmark portfolio and its lower and upper limits are the result of the weighted average of the depositors' benchmark portfolios.

SUMMARY OF THE CAISSE'S OVERALL PERFORMANCE

MARKET RISK

ABSOLUTE RISK AND ACTIVE RISK

The absolute risk of the benchmark portfolio and that of the overall portfolio are calculated according to the same method but cover different portfolios, namely the depositors' benchmark portfolio and the overall portfolio actually invested by the Caisse.

The absolute risk of the Caisse's benchmark portfolio depends on the risk (volatility) of the benchmark indexes for the asset classes in the portfolio. For example, if the depositors generally decided to increase the proportion of publicly traded equities in their benchmark portfolios, this risk would automatically increase, given the volatility of this asset class. The expected absolute return would also increase.

The absolute risk of the overall portfolio is the result of the risk (volatility) of the positions that make up the Caisse's overall portfolio.

Active risk represents the possibility that the Caisse, in managing its overall portfolio actively, will earn a return that differs from the return on its benchmark portfolio. The higher the active risk, the more the expected absolute return on the overall portfolio will differ from the return on the benchmark portfolio.

The absolute risk of the Caisse's benchmark portfolio and the active and absolute risk of the overall portfolio are measured regularly.

Figure 8 shows the components of the Caisse's risk and return.

FIGURE 8
COMPONENTS OF THE CAISSE'S RISK AND RETURN

Caisse's benchmark portfolio	→	Absolute risk of the Caisse's benchmark portfolio	→	Return on market indexes Beta (β)
+				+
Active management	→	Active risk	→	Relative return Alpha (α)
=				=
Caisse's overall portfolio	→	Absolute risk of the Caisse's overall portfolio	→	Weighted average return on depositors' funds

CHANGES IN THE MARKET RISK OF THE OVERALL PORTFOLIO

There is a strong link between the overall return and market risk, which is of two types:

- The risk associated with the component investments (absolute risk); and
- The risk associated with active management of the investments by the Caisse (active risk).

Figure 9 shows the changes in the components of the Caisse's risk.

ABSOLUTE RISK

During the year, the absolute risk of the overall portfolio and the absolute risk of the index of the Caisse's benchmark portfolio increased by 67 b.p. and 63 b.p., to 692 b.p. and 575 b.p., respectively. These increases are due essentially to greater volatility on the financial markets.

Including the third-party ABCP being restructured, the absolute risk of the overall portfolio increased by 33 b.p. to 725 b.p.

The Canadian Equity, Private Equity and Real Estate portfolios represented the largest portion of the absolute risk of the overall portfolio as at December 31, 2007.

ACTIVE RISK

In co-operation with the Board of Directors, Caisse senior management increased the overall value-added objective during the year from 90 to 100 b.p. and also increased the active risk limit of the overall portfolio from 180 to 200 b.p. (figure 31).

The active risk of the overall portfolio ended the year at 155 b.p. If the third-party ABCP being restructured is included, it rises to 195 b.p., an increase of 40 b.p. A special active risk limit of 50 b.p., applicable only to third-party ABCP, was approved by the Board of Directors.

The Private Equity, Investments and Infrastructures, and Real Estate portfolios represented the largest portion of the absolute risk of the overall portfolio as at December 31, 2007.

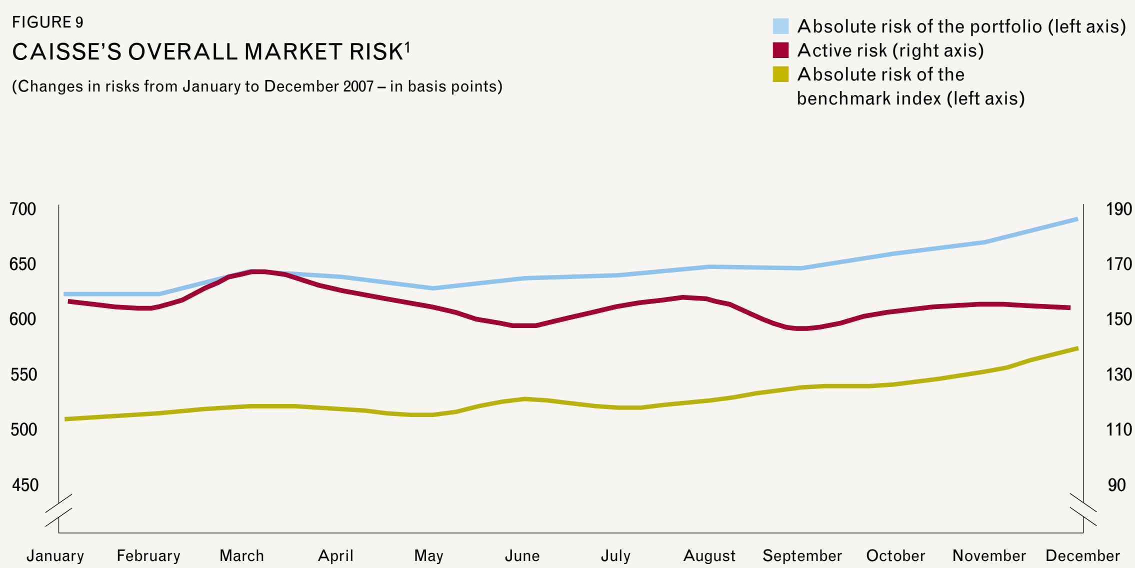
COMPARISON WITH PEERS

According to the study by RBC Dexia Investor Services, the average overall return of 11.5% over three years (2005-2007) ranks the Caisse in the first decile of large Canadian pension funds. The study also indicates that this return was obtained with a level of risk lower than that of its peers (figure 10).

FIGURE 9

CAISSE'S OVERALL MARKET RISK[1]

(Changes in risks from January to December 2007 – in basis points)



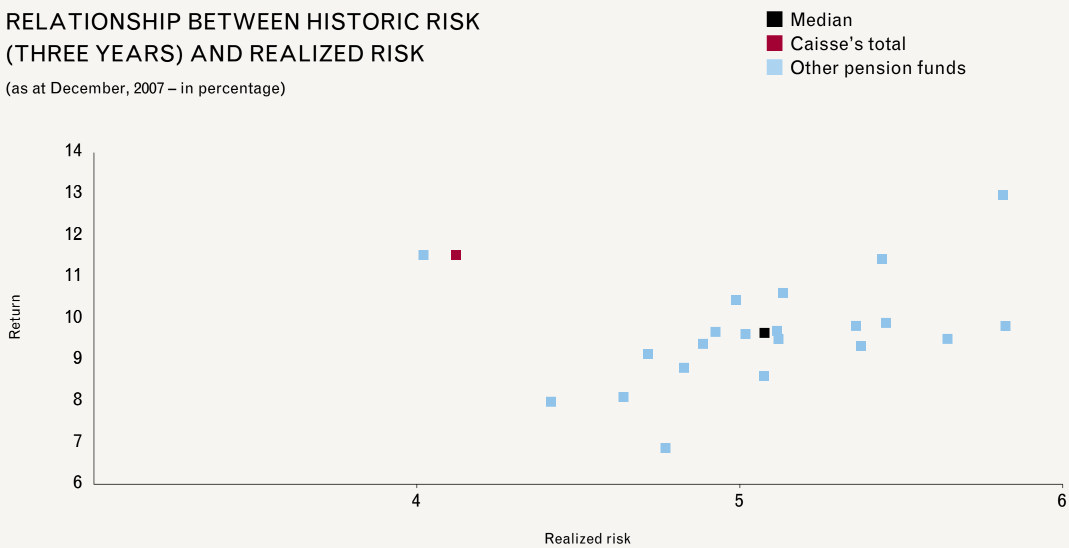
1 Without risk associated with third-party ABCP.

SUMMARY OF THE CAISSE'S OVERALL PERFORMANCE

FIGURE 10

COMPARISON OF THE CAISSE WITH ITS PEERS: RELATIONSHIP BETWEEN HISTORIC RISK (THREE YEARS) AND REALIZED RISK

(as at December, 2007 – in percentage)



Source: RBC Dexia Investor Services – Funds of $1 billion or more.

FIGURE 11

DEPOSITORS' NET ASSETS – 2002 TO 2007

(as at December 31 – in billions of dollars)

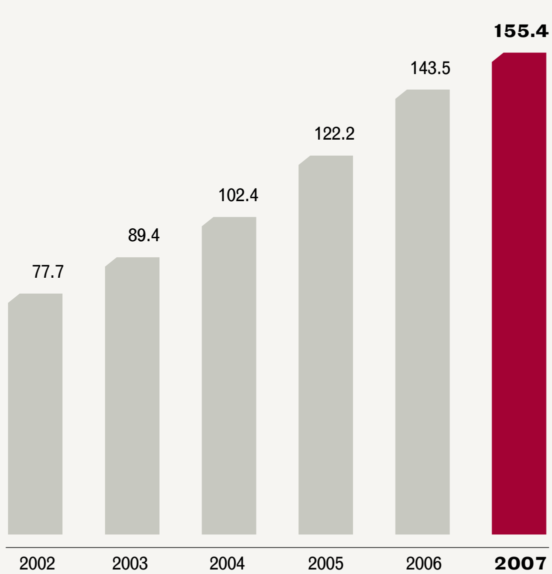
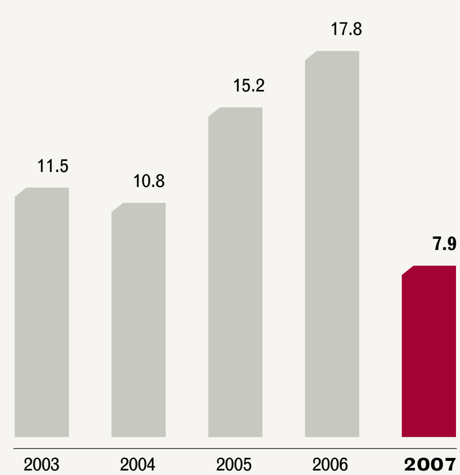


FIGURE 12

NET INVESTMENT RESULTS – 2003 TO 2007

(for periods ended December 31 – in billions of dollars)



CHANGES IN NET ASSETS

Depositors' net assets totalled $155.4 billion as at December 31, 2007, versus $143.5 billion in 2006, an increase of $11.9 billion. Of that amount, $7.9 billion is net investment results and $4.0 billion is net deposits by the depositors.

Over the past five years, depositors' net assets have doubled, going from $77.7 billion as at December 31, 2002, to $155.4 billion as at December 31, 2007 (figure 11). Investment operations account for 81.3% ($63.1 billion) of the increase, and net deposits 18.7% ($14.5 billion). The net investment results for this period are shown in figure 12.

Table 13 shows the changes in depositors' net assets from January 1, 2003, to December 31, 2007. It shows the three main sources of the changes, namely depositors' net contributions, the return related to the composition of the overall benchmark portfolio and the return resulting from active management. It also shows the operating expenses for that period.

The sections that follow analyze the depositors' net contributions as well as the overall return and its main sources. Operating expenses are analyzed in the section "Analysis of operating expenses and external management fees."

DEPOSITORS' NET CONTRIBUTIONS

The deposits made by the Caisse's depositors considerably exceeded their withdrawals during the five years ended December 31, 2007, resulting in net contributions totalling $14.5 billion.

TABLE 13

ANALYSIS OF CHANGES IN DEPOSITORS' NET ASSETS

(for the period 2003 to 2007 – in billions of dollars)

	2003	2004	2005	2006	**2007**	**2003-2007**
Net assets at beginning	77.7	89.4	102.4	122.2	**143.5**	**77.7**
Depositors' net contribution	0.2	2.2	4.6	3.5	**4.0**	**14.5**
Income generated by the composition of the overall benchmark portfolio (depositors' investment policies)	11.6	10.2	13.7	15.8	**9.1**	**60.5**
Value added by active management	0.1	0.8	1.7	2.3	**1.0**	**5.9**
Unrealized decrease in value of investments in third-party ABCP being restructured[1]					**(1.9)**	**(1.9)**
Subtotal	11.9	13.2	20.0	21.6	**12.3**	**79.0**
Operating expenses[2]	(0.2)	(0.2)	(0.2)	(0.2)	**(0.3)**	**(1.1)**
External management fees[2]				(0.1)	**(0.1)**	**(0.2)**
Subtotal	11.7	13.0	19.8	21.3	**11.9**	**77.7**
Net assets at the end	89.4	102.4	122.2	143.5	**155.4**	**155.4**

1 To track its investments in third-party ABCP more effectively, the Caisse has decided to separate its reporting on this matter.
2 External management fees have been presented separately since January 1, 2007. The amounts for 2006 have been restated for comparison purposes.

SUMMARY OF THE CAISSE'S OVERALL PERFORMANCE

OVERALL RETURN

The Caisse's overall return corresponds to the weighted average return on the depositors' funds invested in the 18 specialized portfolios, to which are added treasury operations, decreases in value and certain expenses. This return is 5.6% in 2007, for net investment results of $7.9 billion. The main factors that affected the return are:

- **The depositors' investment policies, particularly:**
  - The considerable weight of non-traditional investments in the overall benchmark portfolio, primarily in the Private Equity, Investments and Infrastructures, Real Estate and Hedge Funds portfolios.
- **The behaviour of the markets, including:**
  - A strong performance by the stock markets in Canada and emerging markets, offset by weak returns on the U.S. and foreign equity markets;
  - The global credit crisis, which caused credit risk premiums to widen suddenly; and
  - The liquidity crisis on Canada's third-party ABCP market.
- **Active management of the overall portfolio and the specialized portfolios:**
  - The foreign exchange hedging policy, which contributed an estimated $3.5 billion; and
  - The overall added value of 72 b.p. (0.72%) produced by the portfolio managers, which amounted to slightly more than $1 billion before the provision for third-party ABCP investments.
- **The weight of each depositor in the overall portfolio.**

For the three- and five-year periods ended December 31, 2007, the Caisse has returns of 11.5% and 12.4% respectively.

Table 14 shows the Caisse's overall return and ranking in relation to large Canadian pension funds.

TABLE 14
OVERALL RETURN
(as at December 31, 2007)

Period	Annual Return	Rank[1]
2007	5.6%	First decile
3 years	11.5%	First decile
5 years	12.4%	First 5 percentiles

1 RBC Dexia Investor Services – Funds of $1 billion or more.

DEPOSITORS' INDIVIDUAL RETURNS

The depositors can invest in the 18 specialized portfolios offered by the Caisse. They determine the proportion of their funds that they want to invest in each portfolio as a function of their target returns and in this way establish their benchmark portfolio.

Certain depositors seek stable returns and preservation of capital. They therefore concentrate their investments in fixed income. The main depositors, however, have a long-term investment horizon and target returns that exceed the returns on fixed income. They therefore diversify their portfolios by also investing in publicly traded equities and other asset classes with the potential for high returns, such as private equity, real estate and hedge funds.

At year-end, because of the differences in the composition of the depositors' portfolios, each obtains a different return. In 2007, the individual returns of the seven main depositors, which represent more than 97% of net assets, ranged from 5.1% to 6.6%.

COMPARISON WITH PEERS

The Caisse believes it is useful to compare its financial results with those of its peers, even though there are significant differences between the composition of its benchmark portfolio and theirs. To that end, it uses studies that rank a sample of institutional fund managers on the basis of the returns obtained by each, such as the study by RBC Dexia Investor Services on Canadian pension funds of more than $1 billion.

According to this study, the Caisse's overall return for 2007 ranks in the first decile of large Canadian pension funds. This is also the case for its average return from 2005 to 2007, which is 11.5%. For the period from 2003 to 2007, the Caisse ranks in the first five centiles of large Canadian pension funds with a 12.4% average return.

ANALYSIS OF THE SOURCES OF THE RETURN ON THE OVERALL PORTFOLIO

RETURN RESULTING FROM THE COMPOSITION OF THE CAISSE'S BENCHMARK PORTFOLIO

The Caisse's overall return is due to a great extent to the composition of its benchmark portfolio, which is the weighted combination of the depositors' benchmark portfolios. In 2007, income related to the composition of the Caisse's benchmark portfolio totalled $9.1 billion versus $15.8 billion in 2006 (table 13).

Estimate of the value added of the benchmark portfolio

The Caisse also compares the return on its portfolio to the return that it would have obtained if the asset allocation of its portfolio had been identical to that of its peers, adjusted for depositors' risk. The value added arising from this allocation, which differs from its peers', is estimated at 179 b.p., or almost $2.6 billion, before the provision for third-party ABCP. This amount is 149 b.p. more than the objective of 30 b.p.

IMPACT OF THE FOREIGN EXCHANGE HEDGING POLICY

In recent years, as part of its strategy to diversify the overall portfolio, the Caisse has gradually increased the weighting of non-traditional assets, especially foreign holdings of private equity and real estate. In agreement with the depositors, it has decided to assume exposure only to the risks and returns for these two asset classes by hedging 100% against the risks related to currency volatility.

Moreover, the Investment Division decided in 2007 to modify the depositors' currency hedging ratio for the U.S. Equity, Foreign Equity and Québec International portfolios. The ratio went from 60.6% as at December 31, 2006, to 66.4% as at December 31, 2007, for an increase of 5.8%. The purpose of this tactical change was to offset the effect of the sustained increase in the Canadian dollar against strong currencies.

The impact of these decisions on the overall return is estimated at $3.5 billion. In 2007, the Canadian dollar rose 17.9% against the U.S. dollar. Against the pound sterling, the yen and the euro, it was up 15.9%, 10.5% and 6.3%, respectively.

IMPACT OF THE UNREALIZED DECREASE IN THE VALUE OF THIRD-PARTY ABCP INVESTMENTS

The Caisse has recorded a $1.9-billion unrealized decrease in value of third-party ABCP that it held as at December 31, 2007. This provision, which represents 15% of the initial $12.6 billion investment,[1] is due to the liquidity crisis that occurred in Canada on the third-party ABCP market. The provision was established according to the guidelines of the Canadian Institute of Chartered Accountants and decreases the overall return by 1.3%, lowering it from 6.9% to 5.6%.

The provision has two main components. The first is a precautionary provision of $1.4 billion related to the synthetic and hybrid assets and the traditional assets held by the Caisse. The second component is a $469-million provision related to U.S. subprime residential mortgages. The Caisse's ABCP investments exposed to these assets total $782 million before the provision.

For more details on the provision for investments in third-party ABCP, please consult note 4B of the combined financial statements.

Reporting on third-party ABCP investments

To monitor these investments more effectively, the Caisse has decided to separate its reporting on them from the reporting on management of its specialized portfolios, considering:

- The unusual nature of the liquidity crisis that froze Canada's third-party ABCP market;
- The fact that these investments were included in centralized management of the liquid assets generated and used by several specialized portfolios.

1 The initial value of $13.2 billion announced by the Caisse in November 2007 has been adjusted to take into account the successful restructuring of Skeena Trust, completed on December 20, 2007.

SUMMARY OF THE CAISSE'S OVERALL PERFORMANCE

THE CAISSE'S TARGET RETURNS AND VALUE-ADDED OBJECTIVES

Most of the depositors are pension funds and insurance plans with a long-term investment horizon. In line with their target returns, the Caisse estimates that they require an overall return of about 7% on a 10-year horizon. A return of this kind can be obtained only with a diversified benchmark portfolio.

The Caisse's peers also have diversified benchmark portfolios. The Caisse's objective, however, is to exceed by 0.3% the expected return (6.7%) on its peers' asset allocation (adjusted for depositors' risks), without assuming any additional risk.

Moreover, the Caisse strives to exceed by 1%* the return on its overall benchmark portfolio, with active management of the specialized portfolios in which the depositors invest.

* In 2007, the Caisse's value-added objective increased from 90 b.p. (0.90%) to 100 b.p. (1.00%).

TABLE 15
THE CAISSE'S TARGET RETURNS AND VALUE-ADDED OBJECTIVE

Forecast asset allocation by peers, adjusted for depositors' risk	6.7%
Depositors' investment policies	+ 0.3%
Caisse's forecast benchmark portfolio	7.0%
Active management	+ 1.0%
Caisse's forecast overall portfolio	8.0%

VALUE ADDED BY ACTIVE MANAGEMENT OF THE SPECIALIZED PORTFOLIOS

The value added by the Caisse's portfolio managers as at December 31, 2007, exceeded the 6.2% return on the overall benchmark portfolio by 72 b.p. (0.72%). After the provision, the value subtracted is 57 b.p. (0.57%). The value added, after the provision, for the three- and five-year periods ended December 31, 2007, is in line with the depositors' objectives, at 99 b.p. (0.99%) and 82 b.p. (0.82%), respectively.

The main specialized portfolios that contributed to value added in relation to the benchmark indexes in 2007 are Private Equity (12.40%), Hedge Funds (4.12%), Canadian Equity (2.81%) and Investments and Infrastructures (1.97%).

The main specialized portfolios that underperformed their benchmark indexes are primarily the hedged and unhedged U.S. Equity portfolios (3.11% and 2.75%), the Real Estate portfolio (4.09%), although its absolute return was high at 20.3%, and the Real Estate Debt portfolio (2.58%).

Table 16 shows the net assets under management, the return and the value added for each of the Caisse's investment groups. Table 18 gives the differences between the returns and the indexes for the Caisse's 18 specialized portfolios. It also shows the differences between the returns and the return thresholds, as applicable. Figure 17 illustrates the contribution of each specialized portfolio to absolute risk and absolute return.

The detailed analysis of the returns for the investment groups and the specialized portfolios under their responsibility are given in the pages that follow.

TABLE 16

NET ASSETS, RETURNS AND VALUE ADDED

(for periods ended December 31)

		2007			2005-2007		
Investment group	**Net assets**	**Return**		**Value added**[1]	Return		Value added[1]
		%	**$ million**	**(b.p.)**	%	**$ million**	(b.p.)
Fixed Income and Currencies	**45.8**	**3.9**	**1,645**	**9**	4.8	5,895	9
Equity Markets	**56.3**	**5.6**	**2,776**	**66**	14.3	18,550	53
Hedge Funds	**7.7**	**5.5**	**375**	**94**	7.4	1,167	220
Private Equity	**17.8**	**13.6**	**2,359**	**852**	19.3	6,968	951
Real Estate	**29.1**	**12.0**	**3,009**	**(343)**	19.4	10,300	134
Asset Allocation and other	**0.4**	**–**	**(35)**[2]	**–**	–	343	–
Unrealized decrease in the value of third-party ABCP being restructured	**(1.9)**	**–**	**(1,897)**	**–**	–	(1,897)	–
Total	**155.4**[3]	**5.6**	**7,869**	**(57)**	11.5	40,790	99

1 In relation to benchmark indexes.
2 The results of these operations include cash asset allocation and are presented net of expenses. Expenses related to management of liquid assets relative to the reclassification of third-party ABCP as an illiquid investment have been subtracted from the contribution of $266.8 million made by the asset allocation operations.
3 The net assets are those presented in the combined financial statements audited by the Auditor General of Québec.

PORTFOLIO MANAGERS' TARGET RETURNS

The results of the Caisse's portfolio managers are evaluated in comparison with benchmark indexes or return thresholds.

VALUE-ADDED OBJECTIVES AND BENCHMARK INDEXES

Most of the Caisse's portfolio managers have value-added objectives in relation to the benchmark indexes relevant to their area of specialization. They construct portfolios whose composition differs from that of their benchmarks so as to outperform them over periods of three and five years.

In addition to the existing market indexes, which are used for the portfolios of liquid investments, the Caisse creates composite indexes that correspond more closely to non-traditional investment operations. This is the case of the indexes for the following portfolios: Québec International, Hedge Funds, Commodities, Investments and Infrastructures, Private Equity and Real Estate Debt. In this way, the return on the Caisse's overall portfolio and the benchmark portfolio can be compared to index management.

ABSOLUTE RETURN OBJECTIVES AND RETURN THRESHOLDS

The objective for the managers of the Investments and Infrastructures, Private Equity, Real Estate and Hedge Funds portfolios is to exceed a return threshold each year. This is a level of absolute return predetermined by the Caisse, taking into account the fact that these portfolios are more risky and less liquid than the equity portfolios. The returns expected of these managers are considerably higher than those of the equity indexes over a long period. The return thresholds must reflect this risk premium in relation to the indexes.

For example, the return threshold for the Private Equity portfolio was set at 12.0% and consisted of the sum of three data:

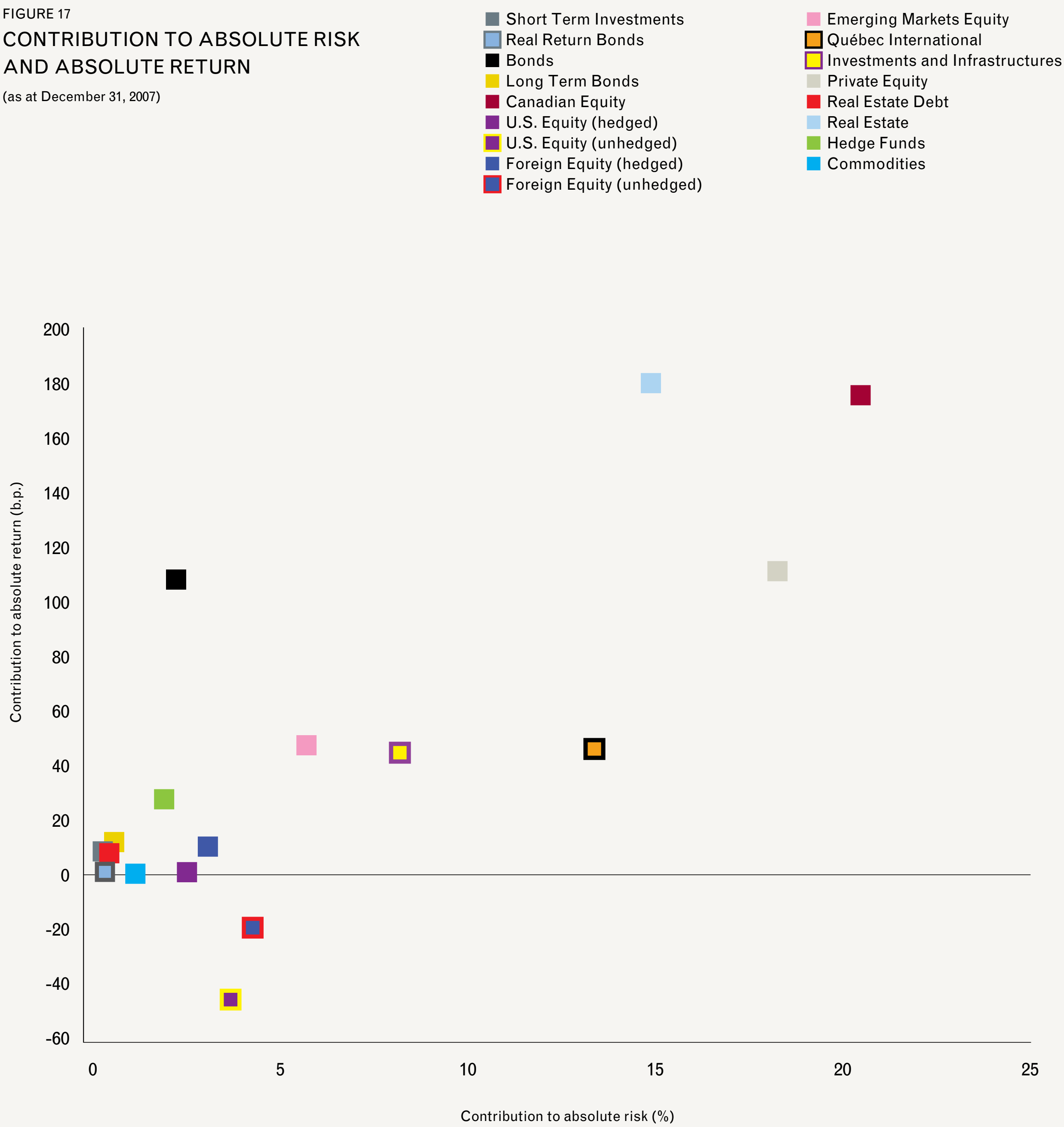
- The expected return on long-term government bonds: 4.3%;
- The equity risk premium: 2.7%; and
- The additional risk premium related to private equity: 5.0%.

The managers of this portfolio therefore have a mandate to construct a portfolio whose return exceeds the 12.0% threshold.

FIGURE 17

CONTRIBUTION TO ABSOLUTE RISK AND ABSOLUTE RETURN

(as at December 31, 2007)



SUMMARY OF THE CAISSE'S OVERALL PERFORMANCE

TABLE 18

RETURNS EARNED BY THE INVESTMENT GROUPS IN RELATION TO INDEXES AND RETURN THRESHOLDS

(for the period ended December 31, 2007 – percentage unless otherwise indicated)

Investment group Specialized portfolio	Index[1]	Threshold	Return[2]	Index	Spread	Index or treshold	Spread/ index or threshold
					b.p.		b.p.
Fixed Income and Currencies							
Short Term Investments	*DEX 91-Day Canadian T-Bill*		4.6	4.4	12	4.4	12
Real Return Bonds	*DEX Real Return Bond*		1.5	1.6	(8)	1.6	(8)
Bonds	*DEX Universe Bond*		3.8	3.7	7	3.7	7
Long Term Bonds	*DEX Long Term Government Bond*		4.7	4.4	27	4.4	27
			3.9	**3.8**	**9**	**3.8**	**9**
Equity Markets							
Canadian Equity	*S&P/TSX capped*		12.6	9.8	281	9.8	281
U.S. Equity (hedged)	*S&P 500 hedged*		0.7	3.8	(311)	3.8	(311)
U.S. Equity (unhedged)	*S&P 500 unhedged*		(13.3)	(10.5)	(275)	(10.5)	(275)
Foreign Equity (hedged)	*MSCI – EAFE hedged*		4.3	3.7	58	3.7	58
Foreign Equity (unhedged)	*MSCI – EAFE unhedged*		(5.1)	(5.7)	63	(5.7)	63
Emerging Markets Equity	*MSCI – EM*		17.0	18.2	(120)	18.2	(120)
Québec International	*Québec International*		4.8	4.6	15	4.6	15
			5.6	**5.0**	**66**	**5.0**	**66**
Hedge Funds							
Hedge Funds	*CS/Tremont Hedge Fund Index modified*	*DEX 91-Day Canadian T-Bill*	9.5	5.4	412	4.4	505
Commodities	*Commodity Financial Instruments*		(0.5)	3.8	(427)	3.8	(427)
			5.5	**4.6**	**94**	**4.0**	**152**
Private Equity							
Investments and Infrastructures	*Investments and Infrastructures*	*9%*	8.8	6.8	197	9.0	(22)
Private Equity	*Private Equity*	*12%*	16.2	3.8	1,240	12.0	418
			13.6	**5.1**	**852**	**10.7**	**297**
Real Estate							
Real Estate Debt	*Real Estate Debt*		0.9	3.5	(258)	3.5	(258)
Real Estate	*Aon – Real Estate*	*8%*	20.3	24.4	(409)	8.0	1 229
			12.0	**15.5**	**(343)**	**6.1**	**588**
Asset Allocation and other (in millions of dollars)[3]			(35)	n.a.	n.a.	n.a.	n.a.
Caisse's overall return – before unrealized decrease in the value of third-party ABCP being restructured (weighted average return on depositors' funds)			6.9	6.2	72	5.5	138
Unrealized decrease in the value of third-party ABCP being restructured ($ million)			(1,897)	n.a.	n.a.	n.a.	n.a.
Caisse's overall return (weighted average return on depositors' funds)			5.6	6.2	(57)	5.5	8

1 The description of the indexes is given in the "General Notes."
2 Returns are presented before operating expenses.
3 The results of these operations include cash asset allocation and are presented net of expenses. Expenses related to management of liquid assets relative to the reclassification of third-party ABCP as an illiquid investment have been subtracted from the contribution of $266.8 million made by the asset allocation operations.

N.B.: The returns on the specialized portfolios for periods of one year to 10 years, as well as the detailed description of the indexes and the thresholds, are presented in the "Additional Information – Annual Report 2007."

Spread versus index
Spread versus threshold

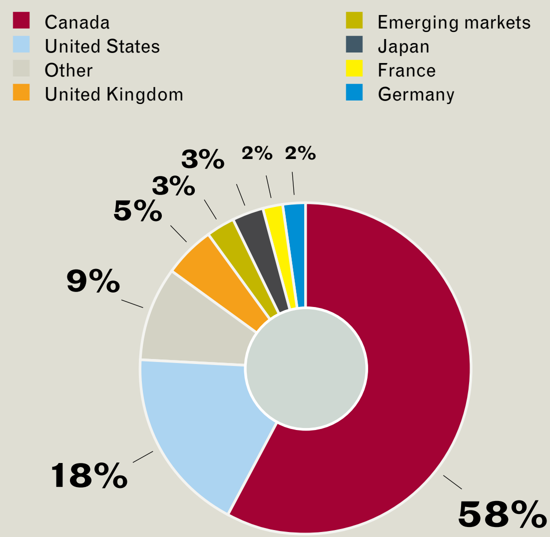
INTERNATIONAL ACTIVITIES

The Caisse has invested on the international markets since it was created, to reduce concentration risk and to enhance its investment returns. This international ambition goes hand in hand with its proximity investments and is part of the Caisse's mission to seek an optimal return for depositors while minimizing risk. The Caisse continues to be very active in Québec and Canada, where it can take advantage of knowledge and experience gained on the local market. In recent years its geographic diversification has accelerated, however, along with the trend to global markets, so that the Caisse is now active on five continents in a variety of asset classes.

The proportion of depositors' total assets invested outside Canada increased to 42%. This proportion will continue to change as investment opportunities arise, especially in emerging markets whose growth rates exceed those of Canada and the other industrialized countries. At present, most of the Caisse's foreign investments are made in industrialized countries. The United States represents 18% of total assets, while the developed economies of Europe and Asia account for 21%. The Caisse's main foreign markets are the United States, the United Kingdom, Japan, France and Germany, with each accounting for more than $2 billion of investments (figure 19).

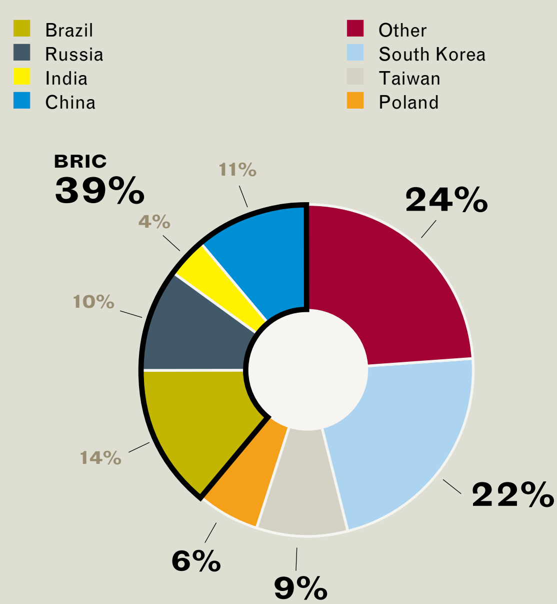
Investments in emerging markets top $6.7 billion, all asset classes combined, or 3% of depositors' total assets. Holdings in the BRIC countries – Brazil, Russia, India and China – were up sharply in 2007 to $2.7 billion, or 39% of all emerging markets investments. Elsewhere, the Caisse has $1.5 billion invested in South Korea and $600 million in Taiwan (figure 20). About 75% of the emerging market investments are in equities and 20% are in real estate.

FIGURE 19
GEOGRAPHIC BREAKDOWN OF DEPOSITORS' TOTAL ASSETS
(in percentage – as at December 31, 2007)



N.B.: As presented as in the combined financial statements.

FIGURE 20
GEOGRAPHIC BREAKDOWN OF DEPOSITORS' TOTAL ASSETS IN EMERGING MARKETS
(in percentage – as at December 31, 2007)



INVESTMENT PHILOSOPHY

The Caisse strives to achieve its target returns in accordance with the depositors' investment policies and the resulting risk budgets. This active management of depositors' holdings is based on the following investment philosophy:

ACTIVE MANAGEMENT

Exploit opportunities in all financial markets by adapting strategies to economic, political and social issues.

FUNDAMENTAL AND OPPORTUNISTIC APPROACH

Emphasize the intrinsic value of companies as well as their potential earnings and value creation over the medium and long terms. Take advantage of investment opportunities as circumstances permit.

OPEN MANAGEMENT

Use external management or partnerships to complement in-house expertise, especially for certain distant markets.

INTERNAL RESEARCH AND INVESTMENT PROCESS

Invest on the basis of internal research and rigorous analysis.

RISK MANAGEMENT

Optimize risk level and allocation, using a range of financial products, various management styles and investment diversification based on company size, sector and geographic location.

ACCOUNTABILITY OF MANAGERS

Ensure portfolio managers are fully accountable for their results.

INVESTMENT DIVISION

THE INVESTMENT DIVISION PROVIDES A CLEAR VISION OF THE CAISSE'S OVERALL PORTFOLIO AND OPTIMIZES ITS RISK AND RETURN

■ ■ ■ For slightly more than a year, it has been the umbrella for the groups that invest in liquid markets, namely Fixed Income and Currencies, Equity Markets and Hedge Funds, as well as for asset allocation operations. The Investment Division also co-ordinates all the Caisse's specialized portfolios and allocates active risk among the managers.

INVESTMENT DIVISION

Q

WHAT CONCLUSIONS CAN WE DRAW ABOUT THE INVESTMENT DIVISION AFTER A FULL YEAR OF OPERATIONS ?

A

THE CREATION OF THE INVESTMENT DIVISION ALLOWS BETTER CO-ORDINATION OF INVESTMENT OPERATIONS AND ENABLES THE INVESTMENT GROUPS TO WORK TOGETHER MORE EFFECTIVELY

This spirit of co-operation is especially apparent when large transactions are carried out. Arrangements for the financing of such investments can be organized between the various investment groups with assistance from the Investment Division. The Private Equity group and the Fixed Income and Currencies group are partners in major initiatives, including corporate debt, infrastructure loans, restructuring funds and distressed loans. Moreover the Chief Investment Officer has a broad view of the Caisse's portfolios and, as necessary, can reduce the asset allocation of one specialized portfolio to meet the financing needs of another. For example, he may decide to reduce the asset allocation of the Equity Markets group to increase that of the Real Estate portfolio.

This greater co-ordination manifests itself in various ways. Optimizing the use of risk is one of the most notable achievements of the Investment Division, in line with the new performance management approach. Managers assume risk to outperform their benchmark indexes. This risk is limited, however, and that is why the Investment Division strives to allocate it effectively. The risk budget is now allocated on the basis of merit and according to potential returns.

Co-ordination was also apparent during the liquidity crisis in August, when all the groups demonstrated solidarity in an unusual situation. The Investment Division ensured the coherence of the various decisions, so that the Caisse's level of liquidity was re-established in a very short time.

Lastly, the asset allocation operations are designed to enhance the Caisse's overall return. After a full year of operations, the Investment Division is recording significant gains with cash asset allocation, in addition to positioning the Asset Allocation portfolio for the future by placing special emphasis on proprietary research.

ASSET ALLOCATION

THE MANAGERS IN THE INVESTMENT DIVISION FOCUS ON THEIR KEY COMPETENCIES, ESPECIALLY RISK ALLOCATION, ACTIVE MANAGEMENT OF THEIR PORTFOLIO AND RESEARCH

■ ■ ■ Portfolio optimization, combined with research, plays a preponderant role in asset allocation operations. The Research team contributed to portfolio management by assuming a specific management mandate. Moreover, the Chief Investment Officer relies on advice from the asset allocation managers and the investment groups when he makes cash decisions to obtain the ideal allocation for the Caisse's overall portfolio. Together, these activities contributed $266.8 million to the overall return.

ASSET ALLOCATION

INVESTMENT PHILOSOPHY

THE PURPOSE OF ASSET ALLOCATION OPERATIONS IS TO ENHANCE THE CAISSE'S OVERALL RETURN. THE FOLLOWING MECHANISMS ARE USED:

- Overweighting or underweighting cash asset classes;
- Adding sources of value to those of all the Caisse's specialized portfolios;
- Using managers with different styles, both internally and externally.

TABLE 21

MANAGEMENT OF ASSET ALLOCATION OPERATIONS

(as at December 31, 2007)

Specialized portfolio	**Assest Allocation**					
Management mandate	Active management by Chief Strategist	Active management by Chief Investment Officer	Global tactical asset allocation		Reseach[1]	Cash asset allocation
Management type	Active internal and parternship	Active internal	Active internal	Active external	Active internal	Active internal
Management approach	Discretionary	Discretionary	Systematic	Discretionary and systematic	Discretionary and systematic	Discretionary
Main analytical approach	Fundamental	Fundamental and technical	Top-down Econometric modelling and optimization	Top-down Relative evaluation of financial markets and risk premiums Econometric modelling and optimization	Bottom-up	Fundamental and technical
Investment horizon	0 to18 months	12 months to 10 years	0 to18 months	0 to18 months	0 to18 months	0 to18 months
Main management styles and investment strategies	Long-short Directional	Opportunistic to enhance the Caisse's overall return	Global Macro Long-short		Long-short	Opportunistic to enhance the Caisse's overall return

1 In 2007, the Research team was involved in managing the Québec International portfolio in co-operation with the Equity Markets group and the Fixed Income and Currencies group. The portfolio's returns are included in those of the Equity Markets group.

HIGHLIGHTS

- The team responsible for the Tactical Asset Allocation mandate significantly increased the portion of its assets managed internally. Initially, this team mainly used external managers, to quickly acquire leading-edge knowledge and generate a return from the outset of its operations. Today, it has acquired a solid foundation that enables it to assume responsibility for a larger portfolio and to reduce the assets managed externally. This gradual increase in internal management will continue in 2008.
- In addition to research, advisory and training activities, the Research and Investment Policy Advice team also began active management based on quantitative analysis.
- To enhance the Caisse's overall return, the Chief Investment Officer acts on broad convictions, as well as on managers' ideas that do not correspond to the risk-return profile of the Caisse's other specialized portfolios. The Chief Investment Officer has considerable leeway regarding the type, size and maturity of the financial products he invests in.

CASH DECISIONS

The Investment Division periodically carries out asset allocation operations called "cash decisions." These are short-term tactical decisions that change the weighting of a specialized portfolio in relation to the benchmark portfolio. Acting on his convictions, the Chief Investment Officer can change the weightings of the specialized portfolios within the limits set in co-operation with the depositors. Overweighting the better-performing sectors enhances returns. Cash decisions are based on monthly in-house analyses of the global macroeconomic environment and the returns expected from the various asset classes over the short and medium terms.

OVERALL RETURN AND ANALYSIS OF ASSET ALLOCATION OPERATIONS

Asset allocation involves two complementary activities: the specialized Asset Allocation portfolio and cash decisions.

The asset allocation operations contributed $266.8 million to the Caisse's overall return in 2007.

Expenses related to management of liquid assets relative to the reclassification of ABCP as an illiquid investment have, however, been subtracted from the positive contribution made by these operations. Thus the activity "Asset allocation and other" represents a negative net contribution of $35 million (see table 18 of "Summary of the Caisse's overall performance").

SPECIALIZED ASSET ALLOCATION PORTFOLIO

The internal managers of the Tactical Asset Allocation mandate had a positive return, as a result of their long equity positions at the start of the year, which enabled them to take advantage of the market's considerable volatility. In the first half, the managers demonstrated discipline in their execution of strategies based on econometric models. They had to adapt these strategies, however, in response to the liquidity crisis in August. Lastly, the return earned by the external Asset Allocation managers, net of financing, was negative. Three funds that took positions based on the value of the yen and equity market returns detracted from the overall return.

CASH DECISIONS

As a result of cash asset allocation decisions, the portfolios of the Fixed Income and Currencies group were underweighted in favour of the Real Estate and Equity Markets portfolios. These decisions were profitable, particularly in light of the 20.3% return on the Real Estate portfolio.

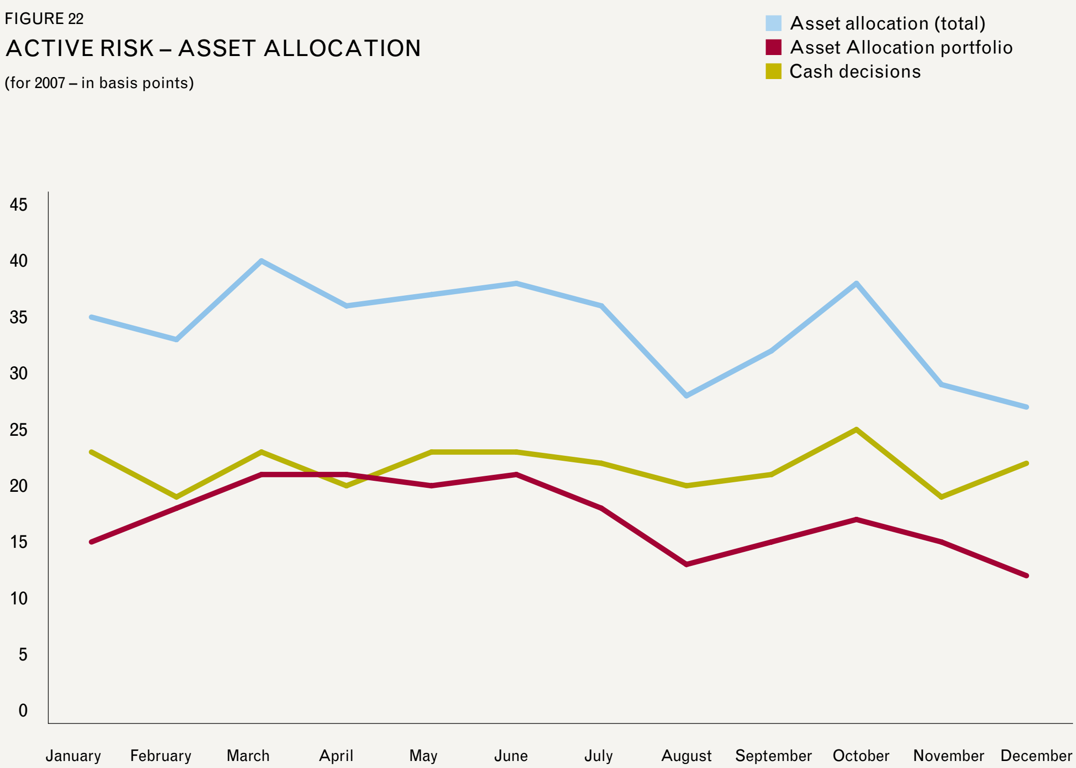
ASSET ALLOCATION

Figure 22 shows the active risk for asset allocation operations, which include the Asset Allocation portfolio and cash decisions. The active risk of cash decisions was fairly stable, as the portfolio's active risk declined. In the second half, the managers reduced the scope of their operations because of market volatility.

FIGURE 22

ACTIVE RISK – ASSET ALLOCATION

(for 2007 – in basis points)



FIXED INCOME AND CURRENCIES

THE FIXED INCOME AND CURRENCIES GROUP EQUIPPED ITSELF WITH A MORE ROBUST STRUCTURE IN 2007 TO ACT ON INVESTMENT OPPORTUNITIES

■ ■ ■ It earned a return of 3.9%, adding 9 b.p. (0.09%) of value in relation to the benchmark index, with the newly integrated Currencies team making a notable contribution to the group's return. The managers created value in a difficult environment.

Q

AFTER YEARS OF LIMITED INVESTMENT OPPORTUNITIES, ARE THE MARKET CONDITIONS AGAIN OFFERING SOURCES OF VALUE ADDED ?

A

YES, THE CONDITIONS ARE LOOKING MORE FAVOURABLE

The past decade has been very difficult for bond managers, especially the past five years.

For managers to create value added, the markets have to offer trends, volatility, spreads between corporate and government bonds, carrying costs,[1] weak correlation between bond asset classes[2] and a dispersal of returns on the classes. Obviously, it's difficult, if not impossible, to have all these factors at once and to take adequate positions at all times. In recent years, however, the Caisse and its peers have had to cope with a scarcity of investment opportunities. Moreover, the market's complacent attitude toward risk also contributed to the disappointing returns on the bond markets.

The bond management group's business plan and organizational structure were therefore reviewed. This multifaceted review involved integration of a team specializing in currencies, reorganization of the teams investing in the international bond markets, creation of a team specializing in volatility and mergers of teams to foster synergy and information sharing.

Beyond these changes, the second half of 2007 can probably be seen as a turning point for the markets: risk premiums increased, volatility reappeared, yield curves steepened significantly and correlation decreased, creating an attractive investment outlook. The search for additional sources of value added – through currencies, international bonds, volatility and systematic quantitative management – was therefore profitable. If this environment continues in 2008, the managers of the bond and currency portfolios should be able to take advantage of attractive investment opportunities.

1 The carrying cost is the difference between the interest expense of financing a security and its yield.
2 The bond asset classes are government bonds, corporate bonds and international bonds, which include emerging markets.

FIXED INCOME AND CURRENCIES

INVESTMENT PHILOSOPHY

THE INVESTMENT PHILOSOPHY OF THE FIXED INCOME AND CURRENCIES GROUP IS TO CREATE VALUE IN A RECURRING MANNER ACCORDING TO THE FOLLOWING PRINCIPLES:

- Exploitation of opportunities on all fixed-income and currency markets;
- Diversification and selection of management styles and investment strategies;
- Diversification of value added;
- Control over potential losses with rigorous management of market positions.

TABLE 23

SPECIALIZED PORTFOLIO MANAGEMENT BY THE FIXED INCOME AND CURRENCIES GROUP

(as at December 31, 2007)

<table>
<tr><th>Specialized portfolio</th><th>Short Term Investments</th><th>Real Return Bonds[1]</th><th>Bonds[1, 2]</th><th>Long Term Bonds[1]</th></tr>
<tr><td>Management type</td><td>Quasi-index</td><td colspan="3">Strategic and tactical, internal and external</td></tr>
<tr><td>Management approach</td><td>Discretionary</td><td colspan="3">Discretionary ans systematic</td></tr>
<tr><td>Main analytical approach</td><td>Top-down and bottom-up
Fundamental and quantitative</td><td colspan="3">Top-down and bottom-up
Fundamental and quantitative</td></tr>
<tr><td>Investment horizon</td><td>0 to 18 months</td><td colspan="3">0 to 18 months</td></tr>
<tr><td>Main management styles and investment strategies</td><td>Replicate the return on the index as faithfully as possible</td><td colspan="3">Directional, systematic and relative-value strategies involving interest rates, credit, volatility and currencies</td></tr>
</table>

1 The Fixed Income and Currencies group uses a mechanism to share value added so that the various bond portfolios can benefit from the same investment ideas and expertise to generate value added. This approach makes it possible to allocate the value added of the Bonds portfolio to the other specialized portfolios forming the shared perimeter, namely Long Term Bonds, Real Return Bonds and Québec International (underlying bonds). The Short Term Investments portfolio is excluded from the perimeter.

2 In 2007, management of the Québec International portfolio was shared by the Equity Markets group, the Fixed Income and Currencies group and the Investment Division, according to their expertise. The portfolio's returns are included in those of the Equity Markets group.

HIGHLIGHTS

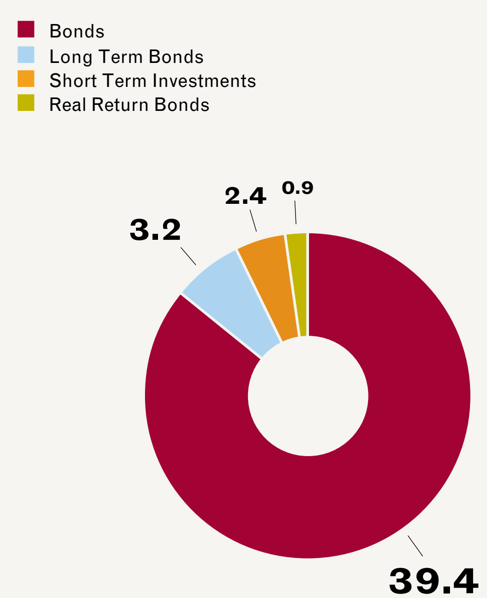
- In 2007, the group created a team that specializes in currencies. The Currencies team was profitable from its first months of operations. It manages a mandate actively and offers currency-hedging and advisory services to Caisse managers who invest in international markets.
- The financing operations were brought together within the Fixed Income and Currencies group, including the operations of CDP Financial. This structure gives concrete expression to the financing role it plays for the Caisse's other groups. In this way, the group can offer financing to the less liquid portfolios, such as those of the Real Estate and Private Equity groups, and reduce their dependency on banks. Moreover, the group can effectively co-ordinate the Caisse's liquid assets with this comprehensive approach.
- The internal partnership with the Private Equity group continued in 2007. In this way, $3.0 billion was allocated to corporate debt, infrastructure loans, restructuring funds and distressed loans. This partnership creates value added for the group and makes it possible to share expertise and market analysis.
- The Fixed Income and Currencies group was reorganized so that it can act more effectively on market opportunities, while providing effective management. In particular, this is the case of the Bond Absolute Return and International teams, which merged to become the International Bonds team. The team has a mandate to ensure greater diversification within the group and to invest in all international bond markets, including emerging markets.
- A management team focusing on interest rate and currency volatility was created to enhance returns and diversify the sources of them. These managers work in close co-operation with the Currencies and International Bonds teams.

OVERALL RETURN AND SPECIALIZED PORTFOLIO ANALYSIS

Although the assets in the bond portfolios were up in 2007, they decreased as a proportion of the Caisse's overall portfolio, in favour of non-traditional asset classes, including the Private Equity group's portfolios and Real Estate Debt. The net assets in the portfolios of the Fixed Income and Currencies group totalled $45.9 billion as at December 31, 2007 (figure 24), versus $42.9 billion at the end of the previous period.

To track its investments in third-party ABCP more effectively, the Caisse has decided to separate its reporting on this matter from that on management of the specialized portfolios (see "Summary of the Caisse's overall performance"). The return earned at the start of the year includes the return on the ABCP that was removed from the affected portfolios in the second half of the year.

FIGURE 24
DEPOSITORS' NET ASSETS BY SPECIALIZED PORTFOLIO
(in billions of dollars - as at December 31, 2007)



FIXED INCOME AND CURRENCIES

TABLE 25

RETURNS – FIXED INCOME AND CURRENCIES

(for periods ended December 31, 2007)

	1 year			3 years				5 years[2]			
	Return %	Index[1] %	**Spread b.p.**	Return %	Index[1] %	**Spread b.p.**	Information ratio	Return %	Index[1] %	**Spread b.p.**	Information ratio
Short Term Investments	4.6	4.4	**12**	4.0	3.7	**30**	2.3	3.5	3.2	**27**	1.4
Real Return Bonds	1.5	1.6	**(8)**	4.3	4.4	**(10)**	(0.2)	n.a.	n.a.	**n.a.**	n.a.
Bonds	3.8	3.7	**7**	4.8	4.7	**7**	0.4	5.8	5.6	**17**	0.7
Long Term Bonds	4.7	4.4	**27**	n.a.	n.a.	**n.a.**	n.a.	n.a.	n.a.	**n.a.**	n.a.

1 The description of the indexes is given in the "General notes."

2 Before July 1, 2003, private equity investments were recorded partially in the Bonds portfolio. Returns before that date have been recalculated, and the portion attributable to private equity has been excluded.

The group generated a 3.9% return in 2007, for 9 b.p. (0.09%) of value added. Table 25 gives the returns for the group's portfolios. The Short Term Investments, Bonds and Long Term Bonds portfolios generated value added, whereas the Real Return Bonds portfolio slightly underperformed its index.

Figure 26 shows the active risk by the Fixed Income and Currencies group. In May 2007, the active risk of the Real Return Bonds portfolio and the Long Term Bonds portfolio converge toward that of the Bonds portfolio because of the introduction of the value-added sharing mechanism. The Fixed Income and Currencies group uses a mechanism to share value added so that the various bond portfolios can benefit from the same value-added investment ideas and expertise. In this way, the value added of the Bonds portfolio is allocated to the other specialized portfolios in the shared perimeter, namely Long Term Bonds, Real Return Bonds and Québec International, which has an underlay of bonds. The Short Term Investments portfolio is excluded from the perimeter since it presents a rather low degree of active risk.

FIGURE 26

ACTIVE RISK – FIXED INCOME AND CURRENCIES

(for 2007 – in basis points)

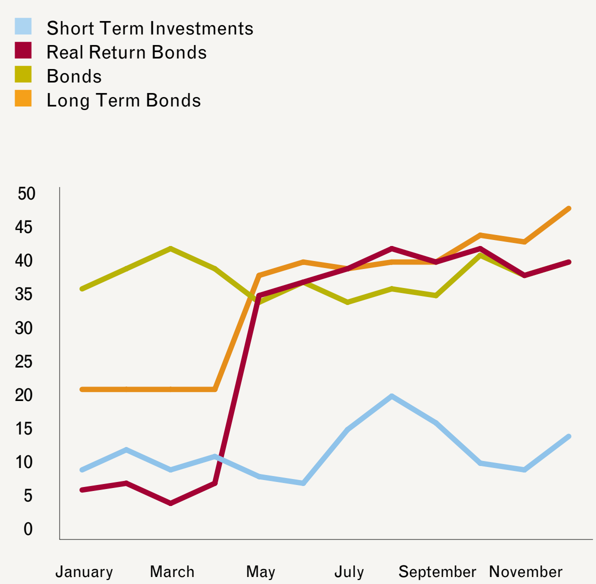


TABLE 27

INVESTMENTS OF THE FIXED INCOME AND CURRENCIES GROUP BY CREDIT RATING

(as at December 31, 2007)

Credit rating	$ million	%
AAA	22,510	42.7
AA	6,721	12.8
A	7,281	13.8
BBB	2,043	3.9
BB	386	0.7
B	183	0.4
CCC	174	0.3
Non-rated	13,387	25.4
Total	**52,685**	**100.0**

N.B.: "Non-rated" denotes financing provided by the Fixed Income and Currencies group to the Caisse's other portfolios, such as Investments and Infrastructures, Private Equity and Real Estate.

SPECIALIZED SHORT TERM INVESTMENTS PORTFOLIO

The Short Term Investments portfolio outperformed its index in 2007 by 12 b.p. (0.12%) with a 4.6% return. The portfolio has been managed on a quasi-index basis since August 31, 2007.

The portfolio's three-year return is 4.0%, versus 3.7% for the benchmark index.

SPECIALIZED REAL RETURN BONDS, BONDS AND LONG TERM BONDS PORTFOLIOS

Since May 2007, active management by the Fixed Income and Currencies group has been centralized in the Bonds portfolio. The value added as a result of these operations is then allocated proportionally to the Bonds, Real Return Bonds and Long Term Bonds portfolios. This allocation contributes in an identical fashion to the value added of each portfolio. A combined analysis of the returns will therefore be given for the three portfolios. Moreover, the Long Term Bonds and Real Return Bonds portfolios manage their own capital, which explains the differences in value added between the portfolios. The Bonds and Long Term Bonds portfolios outperformed their indexes by 7 b.p. (0.07%) and 27 b.p. (0.27%), respectively. The Real Return Bonds portfolio underperformed its benchmark index by 8 b.p. (0.08%).

In relation to its peers, the value added in 2007 places the Fixed Income and Currencies group very close to the first quartile. The strategies used for currencies, volatility, and Canadian and provincial bonds generated very attractive returns.

The operations of the Currencies team were especially profitable, mainly because of positions taken in the Canadian dollar and against the U.S. dollar, toward the end of the year. During the summer, two positions were especially profitable, namely those involving the Australian dollar against the New Zealand dollar and long positions involving the yen. Long positions in the Indian rupee and the Brazilian real, as well as other emerging currencies, created value in the first half of the year. Long volatility strategies were also profitable, especially in the second half, especially those involving the yen, the New Zealand dollar and Eurodollar contracts.

FIXED INCOME AND CURRENCIES

The managers generated value added by taking positions based on a steepening of the yield curve, especially in the United States and Canada. With the liquidity crisis, short-term rates fell more than long-term rates, especially on the U.S. curve. The managers also took positions based on the spreads between the Canadian and U.S. markets to enhance value added with nominal bonds as well as real-return bonds. Strategies combining swaps and spreads between provincial and Canadian bonds were especially profitable in the second half. The partnership with the Private Equity group also generated positive results.

The strategies employed for corporate bonds and credit subtracted value, however, since they were affected significantly by the liquidity crisis in the summer, but also by falling financial values toward the end of the year.

Table 28 shows the top 10 issuers in the specialized Bonds portfolio.

TABLE 28

TOP 10 BOND ISSUERS

(as at December 31, 2007)

Airport Development and Investment Ltd.
Canada Housing Trust
Canada Mortgage and Housing Corporation
Government of Canada
Kreditanstalt für Wiederaufbau
Merrill Lynch Mortgage Loans Inc.
Province of Ontario
Province of Québec
RBC Capital Trust
Sydney Airport Finance Co. Pty Ltd.

EQUITY MARKETS

THE EQUITY MARKETS GROUP EARNED AN OVERALL RETURN OF 5.6% TO OUTPERFORM ITS BENCHMARK INDEX BY 66 B.P. (0.66%). THIS RETURN CONTRIBUTED $2.8 BILLION TO DEPOSITORS' NET ASSETS

■ ■ ■ The managers generated this value added with astute security selection.

Q

WHAT STRATEGIES DO THE EQUITY MARKETS MANAGERS ADOPT TO STAND OUT IN THE VARIOUS MARKETS ?

A

THE EQUITY MARKETS GROUP TRIES TO EXPLOIT ITS COMPARATIVE ADVANTAGES ON VARIOUS MARKETS AND TO MAKE THE MOST OF ITS TALENTED MANAGERS

In Québec and elsewhere in Canada, the managers benefit from the proximity of the market. The size of the Caisse's assets is an extra advantage in the Canadian market. In these conditions, the managers are partial to a bottom-up approach, with value added coming mainly from security selection within sectors.

In comparison, the international markets are enormous. These markets are divided up according to the managers' talents and expertise in various niches or regions. The internal managers use long-short strategies to generate value added. The external managers use a core strategy, with geographic and sector allocation similar to that of the index. Their value added is due to security selection. Moreover, index management is used for a portion of the international portfolios to obtain a return similar to that of the benchmark indexes.

Lastly, the emerging markets managers have to primarily take positions in countries related to their benchmark index. Their approach is based on the risk outlook for the various countries and, to a lesser extent, on security selection. Still, stock picking by sector is becoming an increasingly important component of the strategy used by the emerging markets managers.

EQUITY MARKETS

INVESTMENT PHILOSOPHY

TO ACHIEVE ITS VALUE-ADDED OBJECTIVES IN RELATION TO THE BENCHMARK INDEXES, THE GROUP USES:

- An analytical approach based on the intrinsic value of companies and their earnings outlook over the medium and long terms; and
- Optimization of the risk-return ratio, which favours construction of coherent, focused portfolios with the potential for excellent returns, in accordance with the limitations specified in the investment policies.

TABLE 29

SPECIALIZED PORTFOLIO MANAGEMENT BY THE EQUITY MARKETS GROUP

(as at December 31, 2007)

Market	**Canadian**	**International**			
Specialized portfolio	Canadian Equity	U.S. Equity (hedged and unhedged)	Foreign Equity (hedged and unhedged)	Emerging Markets Equity	Québec International[1]
Management type	Active internal	Active internal and external Index	Active internal and external Index	Active internal and external	Active internal and external Index
Management approach	Discretionary	Discretionary and systematic (external)	Discretionary and systematic (external)	Discretionary and systematic (external)	Discretionary and systematic
Main analytical approach	Fundamental Bottom-up	Fundamental Bottom-up	Fundamental Bottom-up	Fundamental Bottom-up and Top-down	Fundamental Bottom-up and Top-down
Investment horizon	0 to 3 years				
Main management styles and investment strategies	Core Long Long-short	Core Long Long-short	Core Long Long-short	Core Long	Long-short (equity) Directional (bonds)

1 In 2007, management of the Québec International portfolio was shared by the Equity Markets group, the Fixed Income and Currencies group and the Investment Division, according to their expertise. The portfolio's returns are included in those of the Equity Markets group.

HIGHLIGHTS

- The specialized Canadian Equity portfolio earned an excellent return. During the year, certain mandates were consolidated to streamline its structure and improve active-risk allocation, while maintaining its sector diversification. Moreover, the managers are now focusing on a more restricted selection of securities with a longer investment horizon.
- After their first full year of operations, the managers at the New York office generated value added that exceeded expectations.
- The long-short strategy used for international markets recorded positive results. A gradual increase in internal management of the U.S. Equity and Foreign Equity portfolios began during the year and will continue in 2008.
- The size of the Emerging Markets portfolio increased, and the portion that is managed in house was up substantially.
- The managers in the group now monitor the social responsibility of the companies they invest in. The positions in the Canadian equity portfolio are evaluated according to a rating assigned by a specialized firm. This practice will be extended to the U.S. market in 2008.
- The group continued to improve its risk control and trading tools in 2007.

OVERAL RETURN AND SPECIALIZED PORTFOLIO ANALYSIS

The Equity Markets group earned an overall return of 5.6% in 2007, outperforming its benchmark index by 66 b.p. (0.66%). Table 30 shows the returns on the group's portfolios. Depositors' net assets in these portfolios totalled $56.3 billion (figure 31) as at December 31, 2007, versus $53.0 billion at the end of 2006. This year, the return was generated mainly by the Canadian Equity and Emerging Markets portfolios.

FIGURE 31
DEPOSITORS' NET ASSETS BY SPECIALIZED PORTFOLIO
(as at December 31, 2007 – in billions of dollars)

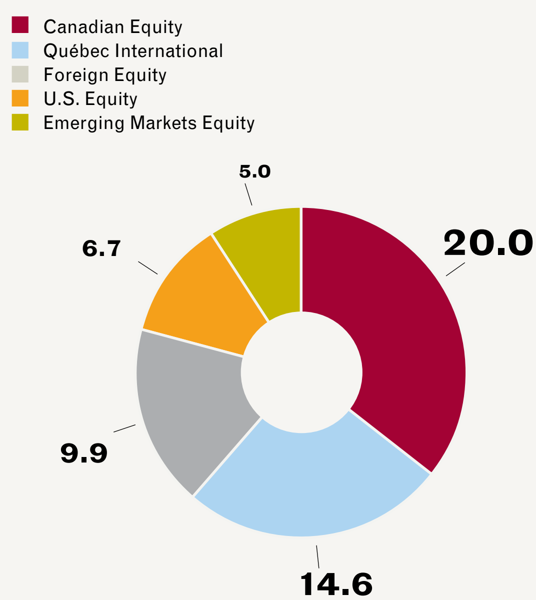


TABLE 30
RETURN ON EQUITY MARKETS
(for periods ended December 31, 2007)

	1 year			3 years				5 years[2]			
	Return %	Index[1] %	**Spread b.p.**	Return %	Index[1] %	**Spread b.p.**	Information ratio	Return %	Index[1] %	**Spread b.p.**	Information ratio
Canadian Equity	12.6	9.8	**281**	18.5	16.9	**154**	0.9	19.6	18.3	**127**	0.9
U.S. Equity (hedged)	0.7	3.8	**(311)**	6.8	7.4	**(59)**	(0.5)	11.4	12.5	**(111)**	(1.0)
Foreign Equity (hedged)	4.3	3.7	**58**	16.6	16.3	**30**	0.5	16.1	16.6	**(55)**	(0.7)
Emerging Markets Equity	17.0	18.2	**(120)**	26.6	26.7	**(14)**	(0.1)	24.4	24.7	**(36)**	(0.2)
Québec International	4.8	4.6	**15**	13.5	13.4	**10**	0.3	17.4	17.3	**3**	0.1

1 The description of the indexes is given in the "General notes."
2 Before July 1, 2003, private equity investments were recorded partially in the Equity Markets portfolios, with the exception of Québec International. Returns before that date have been recalculated, and the portion attributable to private equity has been excluded.

EQUITY MARKETS

SPECIALIZED CANADIAN EQUITY PORTFOLIO

The Canadian Equity portfolio's return for 2007 was 12.6%, or 281 b.p. (2.81%) more than the return on its index.

Once again, this result is due to the team's security selection and absolute return strategies. In the first half of the year, the portfolio benefited from mergers and acquisitions. The most profitable securities are associated with the materials, information technology, energy and telecom sectors. The securities in the consumer discretionary and financial sectors subtracted value, however. The absolute return operations were profitable.

Figure 33 shows the sector weighting of the portfolio and the sector contribution to active risk. The main active risks are related to the energy and materials sectors and are due to security selection.

Over three years, the portfolio has an average annual return of 18.5%, or 154 b.p. (1.54%) more than the return on its index. The managers' selections took advantage of growth in China and other emerging markets, especially in the energy and materials sectors.

Table 32 gives the portfolio's top 10 positions.

TABLE 32

TOP 10 POSITIONS – CANADIAN EQUITIES

(as at December 31, 2007)

Barrick Gold Corp.
Canadian Imperial Bank of Commerce
Canadian Natural Resources Limited
EnCana Corporation
Manulife Financial Corp.
Potash Corp. of Saskatchewan
Research In Motion Ltd.
Rogers Communications Inc.
Talisman Energy Inc.
Toronto-Dominion Bank

SPECIALIZED U.S. EQUITY PORTFOLIOS

After two years of value added, the U.S. Equity portfolios (hedged and unhedged) underperformed the benchmark index in 2007. The hedged U.S. Equity portfolio returned 0.7% in 2007, or 311 b.p. (3.11%) less than the index.

The unhedged U.S. Equity portfolio had a negative return of 13.3%, or 275 b.p. (2.75%) less than its benchmark index. The return on the hedged portfolio exceeds that of the unhedged portfolio because of the Canadian dollar's strength against the U.S. dollar.

Internally, the long-short strategies used by the New York and Montréal offices and the small-and-mid-cap niche created value. The absolute return strategies were unproductive, however.

As for the external managers, they posted negative returns. In this regard, a large portion of the year's results are due to the second half. More specifically, security selection in financials and energy, as well as underweighting energy and overweighting consumer discretionary, subtracted value. Moreover, managers using a quantitative approach sustained losses during the pronounced turbulence in August.

Figure 34 shows the portfolio's investment breakdown by sector and the sector contribution to active risk. The main active risks assumed are related to the energy and information technology sectors.

Over three years, the hedged portfolio has a return of 6.8%, or 59 b.p. (0.59%) less than the index.

Table 35 presents the portfolio's top 10 positions.

TABLE 35

TOP 10 POSITIONS – U.S. EQUITIES

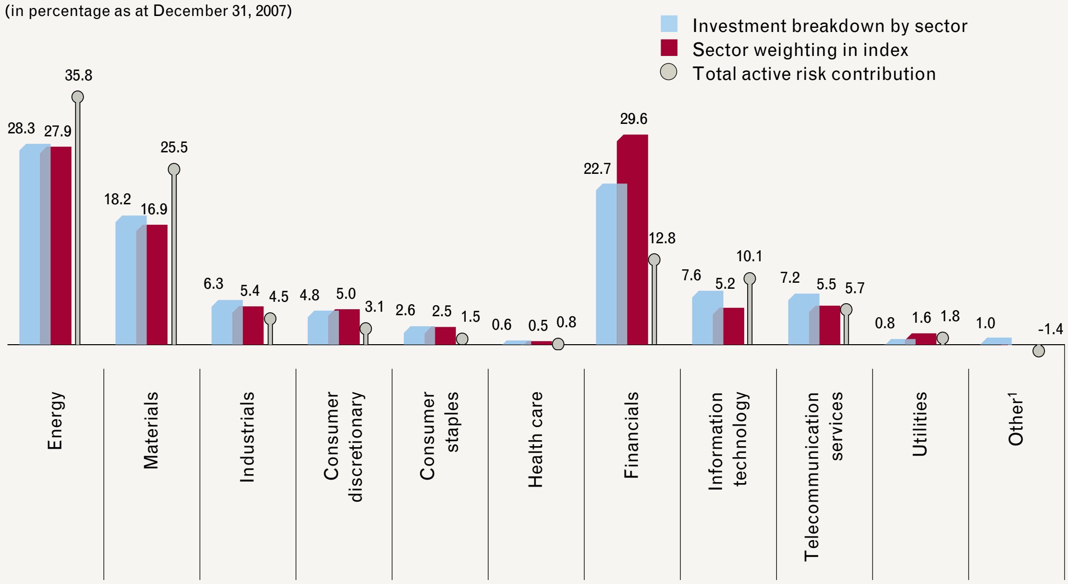
(as at December 31, 2007)

AT&T Inc.
Bank of America Corp.
Citi Group, Inc.
Exxon Mobil Corp.
General Electric Co.
Google Inc.
JPMorgan Chase & Co.
Microsoft Corp.
Pfizer Inc.
Procter & Gamble Co.

FIGURE 33

SECTOR BREAKDOWN OF ACTIVE RISK – CANADIAN EQUITIES

(in percentage as at December 31, 2007)

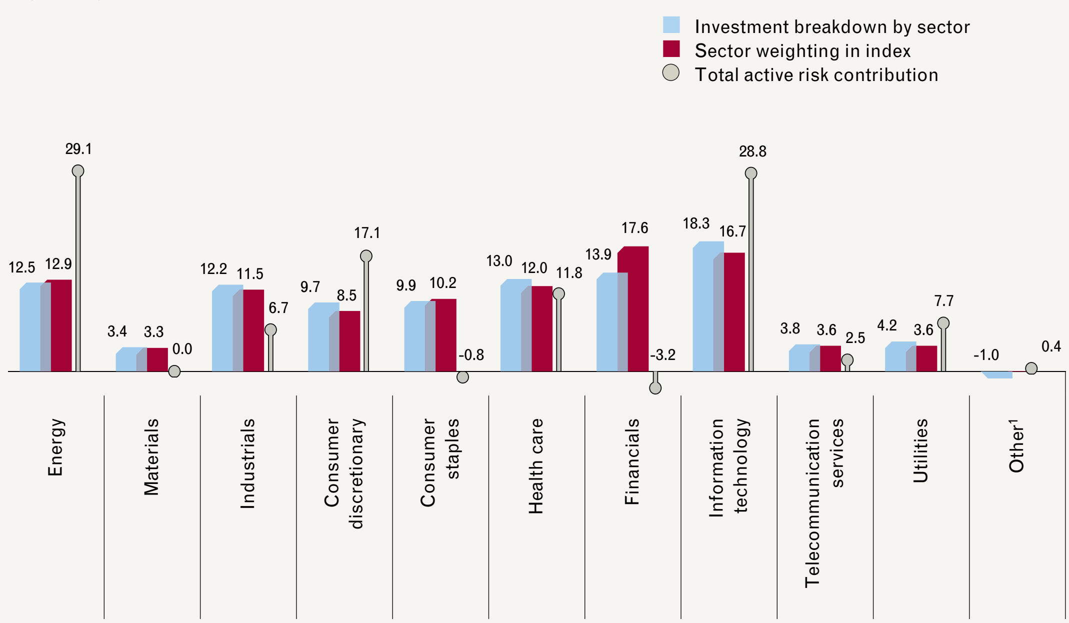


1 Cash and cash equivalents, currency contracts, unallocated derivatives and generalist funds.

FIGURE 34

SECTOR BREAKDOWN OF ACTIVE RISK – U.S. EQUITIES

(in percentage as at December 31, 2007)



1 Cash and cash equivalents, currency contracts, unallocated derivatives and generalist funds.

N.B.: Figures 33 and 34 give the sector allocation of active risk. The contribution to active risk includes several parameters, such as the sector weighting in the portfolio and in relation to the benchmark index, the risk specific to each sector and the diversification effect. The level of contribution to active risk may, therefore, be different from the portfolio's sector exposure. A negative contribution indicates that the positions reduce the portfolio risk as a result of the diversification effect.

EQUITY MARKETS

SPECIALIZED FOREIGN EQUITY PORTFOLIOS

The Foreign Equity portfolios (hedged and unhedged) outperformed their benchmark index for the second straight year. The hedged Foreign Equity portfolio returned 4.3%, or 58 b.p. (0.58%) more than its benchmark index.

The unhedged Foreign Equity portfolio had a negative return of 5.1%, or 63 b.p. (0.63%) more than its benchmark index. The difference between the return on this portfolio and the hedged portfolio is due mainly to the Canadian dollar's strength against the euro and the pound sterling.

The internal managers generated value with long-short strategies and absolute return operations. The strategies used for the United Kingdom and continental Europe detracted from the return in the second half of the year, however. The strategies used to select financial sector securities were counterproductive, mainly in the United Kingdom, which was affected by the liquidity crisis.

Externally, careful security selection and inclusion of several Central and Eastern European non-index securities were profitable. Conversely, the mandates specific to Europe and the Asian markets subtracted value.

Figure 37 shows the geographic breakdown of the investments and the contribution to the active risk assumed by the portfolio managers. The contribution to active risk by geographic market comes essentially from security selection on the European continent.

The hedged portfolio's three-year return is 16.6%, or 30 b.p. (0.30%) more than its index.

Table 36 presents the portfolio's top 10 positions.

TABLE 36

TOP 10 POSITIONS – FOREIGN EQUITIES

(as at December 31, 2007)

BHP Billiton PLC
BP PLC
Nestlé SA
Nokia OYJ
Rio Tinto PLC
Roche Holding AG
Royal Dutch Shell PLC
Total SA
Toyota Motor Corp.
Vodafone Group PLC

SPECIALIZED EMERGING MARKETS EQUITY PORTFOLIO

The Emerging Markets Equity portfolio returned 17.0% in 2007, underperforming its benchmark index by 120 b.p. (1.20%). A good portion of the difference between the return on the index and that of internal and external management is due to the results in the second half.

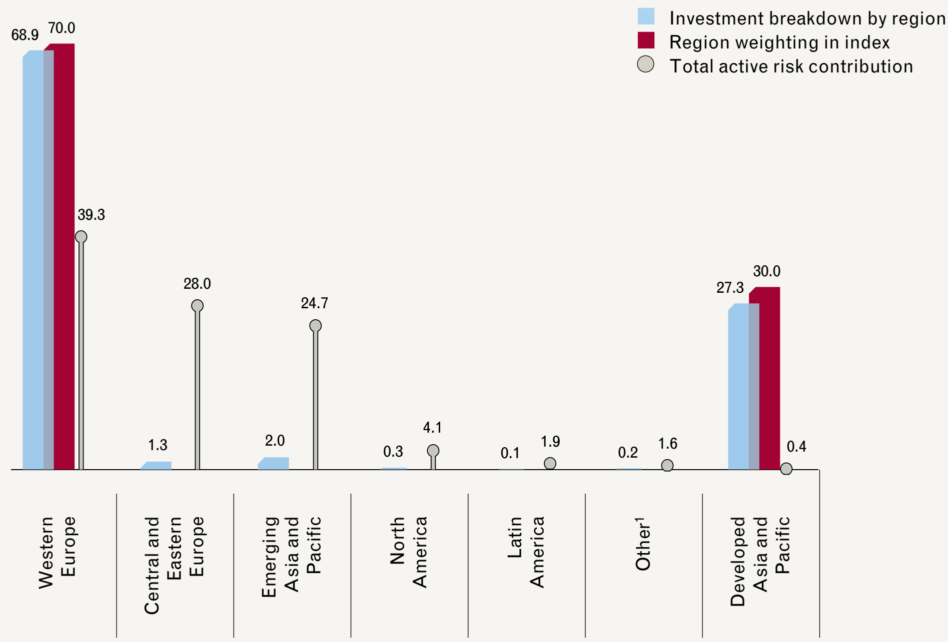
The internal managers are now responsible for a larger share of the portfolio. They underperformed the index. Their security selections for Brazil were not profitable. Brazilian companies in the energy and industrial sectors were affected by rising energy costs. The outlook for these companies remains attractive, however, as they are in sound financial shape. The relative return for internal management continues to be positive over three years.

Figure 38 shows the geographic breakdown of the investments and the contribution to the active risk assumed by the portfolio managers. The contribution to active risk by geographic market is due essentially to security selection in Asia and Latin America.

FIGURE 37

GEOGRAPHIC BREAKDOWN OF ACTIVE RISK – FOREIGN EQUITIES

(in percentage as at December 31, 2007)

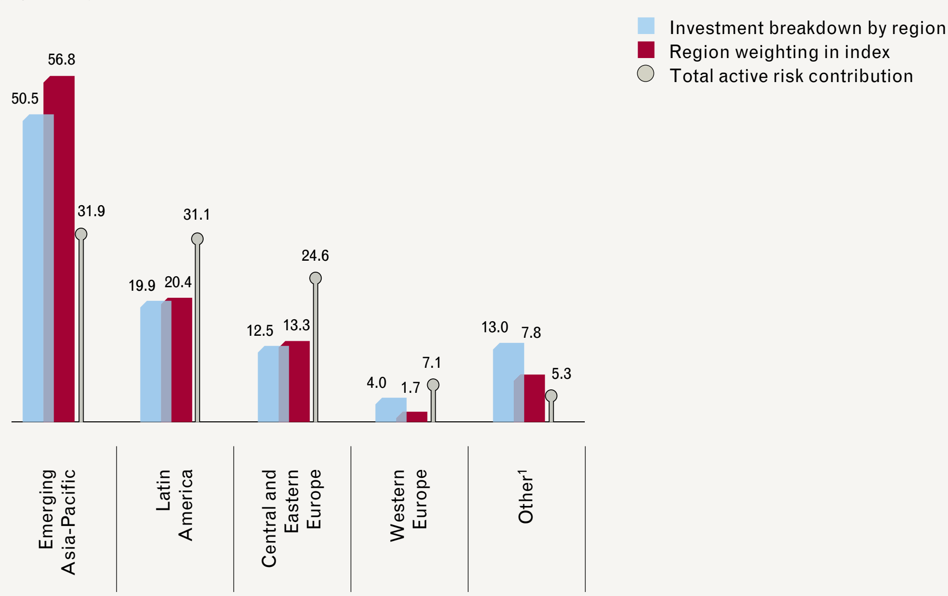


1 Offshore, cash and cash equivalents, currency contracts, unallocated derivatives and generalist funds.

FIGURE 38

GEOGRAPHIC BREAKDOWN OF ACTIVE RISK – EMERGING MARKETS EQUITIES

(in percentage as at December 31, 2007)



1 Developed Asia-Pacific, Africa, offshore, cash and cash equivalents, currency contracts, unallocated derivatives and generalist funds.

N.B.: Figures 37 and 38 give the geographic allocation of active risk. The contribution to active risk includes several parameters, such as the regional weighting in the portfolio and in relation to the benchmark index, the risk specific to each region and the diversification effect. The level of contribution to active risk may, therefore, be different from the portfolio's regional exposure.

EQUITY MARKETS

The external managers decided to underweight India and China, deeming these markets to be overvalued. The substantial returns on these two markets are the reason for the difference between the index and the return earned by the external managers.

Over three years, the portfolio returned 26.6%, underperforming the benchmark index by 14 b.p. (0.14%). During this period, the assets in the portfolio increased from $1 billion to $5 billion. As a rule, the managers have avoided overheated markets by overweighting value securities and underweighting the materials sector. They retreated too quickly from emerging markets they considered vulnerable to a U.S. recession and therefore lost out on opportunities for gains.

Table 39 presents the portfolio's top 10 positions.

TABLE 39
TOP 10 POSITIONS – EMERGING MARKETS EQUITIES
(as at December 31, 2007)

America Movil SAB de CV
China Mobile Ltd.
China Petroleum & Chemical Corp.
Companhia Vale do Rio Doce
Gazprom OAO
Lukoil
POSCO
Petroleo Brasileiro SA
Samsung Electronics Co. Ltd.
Sberbank

SPECIALIZED QUÉBEC INTERNATIONAL PORTFOLIO

The Québec International portfolio returned 4.8% in 2007, outperforming its benchmark index by 15 b.p. (0.15%). Over three years, the portfolio has returned 13.5%, for 10 b.p. (0.10%) of value added.

The benchmark index of the specialized Québec International portfolio was revised during the year. The new index is designed to enhance the return while modifying the portfolio's composition. The benchmark index is now weighted according to the gross domestic product of the countries in the basket of futures contracts. Previously, the index was weighted according to the stock market capitalization of these countries.

The Equity Markets group, the Fixed Income and Currencies group and the Investment Division's Research team are now involved in active management of the portfolio according to their fields of expertise. The strategies adopted by the Equity Markets group were very profitable, as were those of the Fixed Income and Currencies group. Those adopted by the Research team subtracted value, however, as a result of country selection and the systematic long-short strategy.

Over one year, the portfolio outperformed the MSCI World Index by 0.8%.

QUÉBEC INTERNATIONAL

The specialized Québec International portfolio has a hybrid structure. It consists of bonds denominated in Canadian dollars, which implicitly protects it against currency risk, as well as a basket of futures contracts based on world stock markets. The futures contracts produce a stock-index return in exchange for a return on short-term investments. The portfolio's objective is to increase the exposure of the Caisse's overall portfolio to foreign equity markets with a view to greater diversification and superior returns.

HEDGE FUNDS

THE HEDGE FUNDS GROUP EARNED A 5.5% RETURN TO OUTPERFORM ITS BENCHMARK INDEX BY 94 P.B. (0.94%) IN AN ENVIRONMENT MARKED BY STRONG VOLATILITY

■ ■ ■ The operations of the Hedge Funds portfolio have been concentrated in a smaller number of external funds to ensure greater transparency. Moreover, the level of risk of the Commodities portfolio was reduced substantially.

HEDGE FUNDS

Q

THE HEDGE FUND INDUSTRY IS OFTEN CRITICIZED FOR ITS LACK OF TRANSPARENCY AND THE RESULTING POTENTIAL RISK. WHAT IS THE HEDGE FUNDS GROUP DOING IN RESPONSE TO THESE CONCERNS ?

A

THE BUSINESS MODEL OF THE HEDGE FUNDS PORTFOLIO WAS REVISED IN 2007 TO DECREASE RISK AND TO INCREASE TRANSPARENCY

To reduce risk, the number of hedge funds was decreased, but the level of diversification was kept high. The funds were selected from the best in the industry, with emphasis on greater transparency. With fewer funds, the managers of this portfolio can monitor the funds under their responsibility more closely. Moreover, the weighting of highly specialized funds, whether by niche or geographic region, was increased.

In addition, the transparency of the hedge funds was increased. The segregated funds were included in an independent platform that will provide information to the portfolio managers. A third party will be given a mandate in 2008 to collate information from the external funds and then provide risk measurement for the non-segregated funds.

HEDGE FUNDS

INVESTMENT PHILOSOPHY

THE INVESTMENT PHILOSOPHY OF THE HEDGE FUNDS GROUP IS TO:

- Identify market inefficiencies with continual analysis of fundamental factors likely to affect returns;
- Use quantitative methods to identify investment opportunities;
- Perform rigorous risk management in the design of each strategy and transaction; and
- Obtain leading-edge external expertise to construct a portfolio that is less subject to market fluctuations.

TABLE 40

SPECIALIZED PORTFOLIO MANAGEMENT BY THE HEDGE FUNDS GROUP

(as at December 31, 2007)

Specialized portfolio	**Hedge Funds**			**Commodities**
Management mandate	Global Macro Discretionary	Hedge Funds of Funds	Strategic Opportunities	Management of commodity forwards Management of underlying currencies and real return bonds
Management type	Active internal	Active external	Active internal and partnership	Active internal and external Index internal and external
Management approach	Discretionary and systematic	Discretionary	Quantitative and systematic	Discretionary
Main analytical approach	Top-down Relative evaluation of financial markets and risk premiums	Fundamental Top-down (selection of strategies) and bottom-up (selection of managers)	Top-down and bottom-up	Fundamental and technical
Investment horizon		0 to 3 years		0 to 18 months
Main management styles and investment strategies	Global macro Long-short	Arbitrage Event-driven Global macro	Directional Relative-value	Long-short Directional

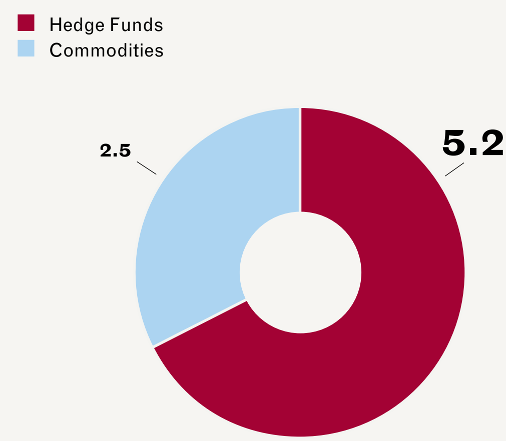
HIGHLIGHTS

- The business model of the external management team was revised in 2007. The number of funds was reduced, even though the size of the portfolio rose from $4.2 billion to $5.2 billion.
- The transparency of the segregated funds was increased when some of them were included in an independent platform. In addition, a third party will be given a mandate in 2008 to collate information from the external funds and then provide risk measurement for the non-segregated funds.
- A team was put in place within the Strategic Opportunities management mandate to apply the quantitative strategies of the best hedge funds.
- In the second half of the year, the active risk of the specialized Commodities portfolio was reduced substantially.

FIGURE 41

DEPOSITORS' NET ASSETS BY SPECIALIZED PORTFOLIO

(in billions of dollars – as at December 31, 2007)



OVERALL RETURN AND SPECIALIZED PORTFOLIO ANALYSIS

The depositors' net assets in the Hedge Funds and Commodities portfolios totalled $7.7 billion as at December 31, 2007 (figure 41), versus $6.5 billion at the end of 2006. The Hedge Funds group recorded a return of 5.5% in 2007, contributing $375 million and 94 p.b. (0.94%) of value added in relation to the benchmark index. Table 42 gives the returns on the group's portfolios.

SPECIALIZED HEDGE FUNDS PORTFOLIO

The Hedge Funds portfolio returned 9.5% in 2007, or 412 p.b. (4.12%) more than its benchmark index. A large proportion of the value added comes from the index used for the first six months of the year.

Internally, the managers foresaw the increase in asset risk resulting from the credit crunch. They took short positions in banks and certain indexes, which both fell during the crisis. The portfolio also made gains on the bond market and, as a result of short positions, on the equity markets. The development of in-house operations generated positive results. The market-neutral strategy incurred losses, however.

The external managers believed the risk posed by financial assets was underestimated for hedge fund operations. They therefore took positions in anticipation of a declining market. This strategy proved profitable. External management took advantage of the generally higher risk premiums.

TABLE 42

RETURN ON HEDGE FUNDS

(for periods ended December 31, 2007)

	1 year			3 years			
	Return %	Index[1] %	**Spread b.p.**	Return %	Index[1] %	**Spread b.p.**	Information ratio
Hedge Funds	9.5	5.4	**412**	8.4	5.1	**329**	1.0
Commodities	(0.5)	3.8	**(427)**	6.3	6.3	**(6)**	0.0

1 The description of the indexes is given in the "General notes."

HEDGE FUNDS

The Hedge Funds group is now positioning itself for continued credit deterioration in 2008, in the context of a difficult economic environment. The distressed-debt sector could be a promising area.

The portfolio has a three-year return of 8.4%, or 329 p.b. (3.29%) more than its benchmark index.

Table 43 gives the portfolio's top 10 hedge fund management companies.

TABLE 43

TOP 10 MANAGEMENT COMPANIES – HEDGE FUNDS

(as at December 31, 2007)

Crestline Management LP
D.E. Shaw & Co. LP
Diversified Global Asset Management Corp.
Ellington Management Group LLC
Endeavour Capital Management LLC
Farallon Capital Management LLP
HBK Investments LP
Harbert Management Corp.
Highbridge Capital Management LLC
Och-Ziff Capital Management Group

Figure 44 shows the absolute risk of the Hedge Funds portfolio. The significant decrease at mid-year is due to a considerable extent to the revision of the benchmark index.

SPECIALIZED COMMODITIES PORTFOLIO

The specialized Commodities portfolio recorded a negative return of 0.5% in 2007, or 427 p.b. (4.27%) less than its benchmark index, which advanced 3.8%. Assets under management totalled $2.5 billion as at December 31, 2007, versus $2.3 billion in 2006.

The portfolio was affected significantly by rising prices in the energy sector, especially the price of oil. Moreover, the extreme volatility of metals prices, including copper and aluminum, also contributed to these results. The portfolio's strategy was based on anticipation of lower spot prices as opposed to futures prices. This strategy proved to be particularly unfavourable.

In the second half of the year, the active risk allocated to the Commodities portfolio was radically reduced, for three reasons. First, the portfolio was already recording losses in the first half because of rising energy prices and volatile metals prices. At mid-year, several members left the team. Moreover, volatility increased sharply in late August. To minimize the portfolio's losses, the Caisse decided to suspend active management for all practical purposes.

Over three years, the portfolio has a return similar to that of the index.

Figure 45 shows the active risk of the Commodities portfolio. The portfolio's active risk fluctuated a great deal during the year. The significant decrease in risk toward year-end is due to the decision to limit the losses.

FIGURE 44

ABSOLUTE RISK – HEDGE FUNDS

(for 2007 – in basis points)

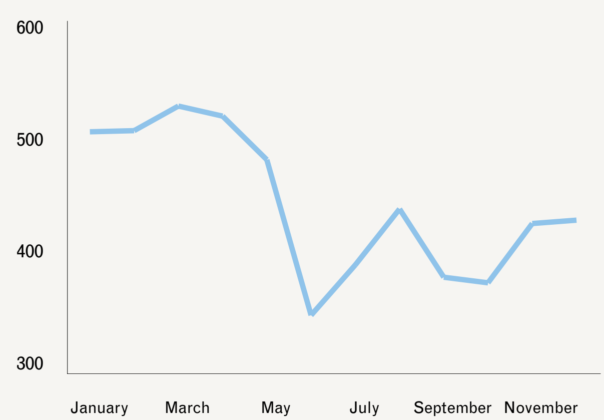
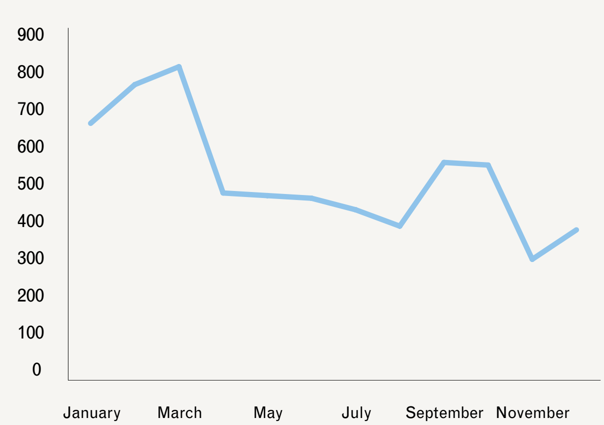


FIGURE 45

ACTIVE RISK – COMMODITIES

(for 2007 – in basis points)



PRIVATE EQUITY

A SUITABLY DEFENSIVE STRATEGY

The Private Equity group fared well despite the difficult market conditions of 2007. After a very busy first half, the liquidity crisis caused a pronounced slowdown on the leveraged-buyout market. A highly selective approach to investments and a shift to restructuring and distressed-loan funds proved to be wise strategies in these circumstances. Taking this tack, the Private Equity group generated a return of 13.6% and contributed $2.4 billion to depositors' net assets.

Q

HOW HAS THE PRIVATE EQUITY GROUP POSITIONED ITSELF TO COPE WITH THE REVERSAL OF THE CYCLE THAT BEGAN IN 2007 ?

A

IN 2006, THE PRIVATE EQUITY GROUP ADOPTED A STRATEGY TO DIVERSIFY RISK IN THE EVENT OF A SLOWDOWN AND BECAME EVEN MORE SELECTIVE ABOUT ITS INVESTMENTS

The group scaled back leveraged buyout and infrastructure investments, it ramped up investments in restructuring and distressed-loan funds and it sold a large portion of its listed securities. This strategy positioned both portfolios for the reversal of the cycle, which came at mid-year. The Private Equity group will maintain this strategy in 2008 and continue to take a disciplined and opportunistic approach to investment.

In recent years, an abundance of capital has led to an unprecedented easing of credit conditions, with low interest rates accompanied by extremely flexible conditions. Buyout funds took advantage of this situation to optimize their leverage and increase their deal flow. The credit crisis that began in August put an end to the exuberance. Overnight, the market for big leveraged buyouts ground to a halt, apart from the transactions already in progress.

The tougher credit conditions considerably reduced the competitive edge of investors who specialize in financial packages based on leverage. The new market conditions are conducive to a return of strategic investors, namely business operators who are experts in their industry and well placed to identify opportunities. The Private Equity group had already adjusted its partnership approach accordingly before the onset of the crisis in August.

PRIVATE EQUITY

INVESTMENT PHILOSOPHY

PRIVATE EQUITY INVESTMENT REQUIRES THOROUGH COVERAGE OF TARGET MARKETS AND COMPANIES. THE GROUP'S INVESTMENT PHILOSOPHY THEREFORE FEATURES:

- Direct investments in markets close at hand, partnerships for distant markets and an opportunistic approach, depending on market conditions;
- Selection of the best corporate management teams and investment funds to maximize long-term returns on capital;
- Risk management based on analysis and rigorous monitoring of investments, including exit strategies; and
- Investment diversification by industrial sector, geographic area, financial product and business maturity.

TABLE 46

SPECIALIZED PORTFOLIO MANAGEMENT BY THE PRIVATE EQUITY GROUP

(as at December 31, 2007)

Specialized portfolio		**Investments and Infrastructures**				**Private Equity**			
Investment categories		Development capital	Debt	Infrastructures	Accumulation	Venture capital	Leveraged buyouts	Mezzanine debt	Restructuring
Management type		Active							
Management by geographic region	Québec	Direct	Direct	Direct	Direct	Indirect or partnership	Indirect or partnership	Direct	Indirect
	Canada ex Québec	Direct or partnership	Direct or syndication	Direct or partnership	Direct	Indirect or partnership	Indirect or partnership	Direct or partnership	Indirect
	United States, Europe	Direct or partnership	Partnership or syndication	Direct or partnership	Direct	Indirect or partnership	Indirect or partnership	Direct or partnership	Indirect
	Emerging markets	–	–	Indirect and market watch	–	–	Indirect	–	–
Main investment vehicles		Equity securities	Senior debt	Equity securities	Publicly traded equity securities	Funds	Funds and equity securities	Funds and debt securities	Funds
Management approach		Discretionary							
Main analytical approach		Fundamental bottom-up							
Investment horizon		3 to 7 years							
Main management styles and investment strategies		Long Participation							

HIGHLIGHTS

- The weighting of the Private Equity portfolio in the benchmark portfolio went from 6.3% to 7.9% and that of the Investments and Infrastructures portfolio, from 4.4% to 5.4%. The Caisse made these changes after consulting the depositors.
- After setting a record in 2006, the volume of authorized investments reverted to a more normal level in 2007. The group was very selective about its transactions, which totalled $9.0 billion. Direct transactions amounted to $5.9 billion, while investment funds received $3.1 billion (table 47).
- Among the year's most important deals, the Private Equity group invested US$250 million in Enbridge Energy Partners, a U.S. company that transports oil and gas. More than 100 other transactions were also authorized in 2007, in diverse areas such as food distribution (U.S. Foodservice) and port services (GCT Global Container Terminals). Table 48 summarizes some of the investments authorized during the year.
- The managers sold $1.9 billion of listed securities held by the Investments and Infrastructures portfolio, generating a large reserve to be deployed at the bottom of the cycle.
- The internal partnership with the Fixed Income and Currencies group led to disbursement of $1.6 billion to restructuring and distressed-loan funds and the sharing of extremely valuable expertise and market analysis during the credit crisis.
- In Québec, the Caisse continued its venture capital strategy based on partnership. Its partner funds have already invested $100 million in about 40 Canadian companies and have attracted an additional $200 million from the external investors who took part in these deals.
- The strategy of supporting Québec companies saw a major shift during the year when an operational approach was added with the startup of the Québec Manufacturing Fund (Industrial Capital) and the appointment of an experienced operator to head the Medium-sized Businesses team. The strategy adopted by the Private Equity group for Québec is described in detail in the section "Contribution to Québec's economic development" of this Annual Report.
- The Private Equity group will continue to be very selective and opportunistic with all its investments in 2008. The managers will concentrate on the existing portfolios and opportunities that arise as a result of these investments. The group will be partial to a proximity approach to development capital in order to take advantage of its local market expertise and existing partnerships. It will also continue to invest in restructuring and distressed-loan funds.

TABLE 47

OVERALL INVESTMENTS AUTHORIZED IN 2007

Investment category	Number	$ million
Debt	33	3,021
Infrastructures	6	1,228
Venture capital	15	400
Leveraged buyouts and mezzanine debt	50	2,795
Development capital and accumulation	15	411
Restructuring	8	1,115
Total	**127**	**8,970**
Management type		
Direct transactions	78	5,898
Funds	49	3,072
Total	**127**	**8,970**

PRIVATE EQUITY

TABLE 48
A SAMPLING OF INVESTMENTS AUTHORIZED IN 2007

Targeted firm	Geographic region	Sector	Partners	Project
iNovia Investment Fund II LP Inc.	Québec	Diversified investment fund specializing in startups	BDC Capital Inc. Consensus Business Group Solidarity Fund QFL FIER Partenaires	Venture capital fund
Atrium Innovations Inc.	Québec	Health, nutrition and specialty chemicals	Banking syndicate led by National Bank Financial and RBC Capital Markets	Increase in credit facilities to finance expansion by acquisition
Remstar Media Partners	Québec	Distribution of film and television products	Solidarity Fund QFL Remstar Corporation	Creation of a new company to acquire and exploit distribution rights of mainly Canadian films
GCT Global Container Terminals Inc.	Canada ex Québec	Port services	Ontario Teachers' Pension Plan	Acquisition of four marine container terminals from Orient Overseas (International) Limited in New York City, New Jersey and Vancouver
Sun Capital Partners V	United States	Investment fund focused on restructuring of distressed small and mid-sized businesses in North America, Europe and Japan	Sun Capital Partners Inc.	Creation of a new private equity fund to capitalize on restructuring opportunities
Enbridge Energy Partners LP	United States	Oil and gas transportation	Enbridge Inc.	Investment increase to finance expansion projects
U.S. Foodservice	United States	Food distribution	Clayton Dubilier & Rice	Equity financing for a leveraged buyout
Laureate Education Inc.	United States	Network of private universities	Kohlberg Kravis Roberts Citigroup	Equity financing for a privatization
Financière Ermewa SA	Europe	Railway car and container rental	SNCF Participations West LB HVB Capital Partners AG Compagnie de Gestion et de Participation SA Assurances générales de France (AGF) Investors in Private Equity SA	Share acquisition
Interconnector (UK) Limited	Europe	Gas transmission	E.ON Ruhrgas UK Exploration & Production Limited Distrigaz SA OAO Gazprom ConocoPhillips (UK) Limited Eni International BV	Share acquisition

OVERALL RETURN AND SPECIALIZED PORTFOLIO ANALYSIS

The Private Equity group was able to advance steadily, despite the liquidity crisis that began in August. The group's overall return was 13.6% in 2007, or 297 b.p. (2.97%) more than its return threshold and 852 b.p. (8.52%) more than its benchmark index. Table 49 gives the details of the returns earned by the group's portfolios over one year and three years. With the substantial international exposure of both portfolios (64% for the Investments and Infrastructures portfolio and 75% for the Private Equity portfolio), the decision to hedge foreign-exchange risk fully was very profitable in 2007.

Over the past three years, all the investment categories were buoyed by extremely favourable credit conditions, and the group was well placed to take advantage of them. Leveraged buyouts generated exceptional returns, as shown by the three-year return on the Private Equity portfolio. The Investments and Infrastructures portfolio also took advantage of this boom, but to a lesser extent because it was created more recently.

As at December 31, 2007, depositors' net assets in the Investments and Infrastructures portfolio and the Private Equity portfolio totalled $17.8 billion, an increase of $1.0 billion from 2006 (table 50). Depositors' total assets amounted to $27.3 billion, and property under management or administration, to $0.8 billion. The group's total assets under management amounted to $28.1 billion at year-end.

TABLE 49

RETURN ON PRIVATE EQUITY

(for periods ended December 31, 2007)

	1 year			3 years		
	Return %	Index[1] %	**Spread b.p.**	Return %	Index[1] %	**Spread b.p.**
Investments and Infrastructures	8.8	6.8	**197**	11.5	14.6	**(304)**
Private Equity	16.2	3.8	**1,240**	25.3	5.9	**1,943**

1 The description of the indexes is given in the "General notes."

TABLE 50

TOTAL ASSETS UNDER MANAGEMENT BY THE PRIVATE EQUITY GROUP

(fair value as at December 31, 2007 – in billions of dollars)

	Depositors' net assets	Depositors' total assets[1]	Assets under management or under administration	Total assets under management	
Investments and Infrastructures	6.4	14.5	0.8	15.3	54.4%
Private Equity	11.3	12.8	–	12.8	45.6%
Total	**17.8**	**27.3**	**0.8**	**28.1**	**100.0%**

1 Including assets related to the internal partnership with the Fixed Income and Currencies group.

PRIVATE EQUITY

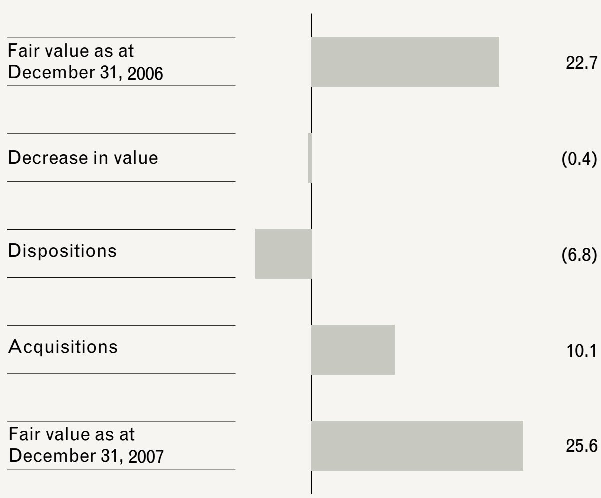
As shown by figure 51, the fair value of the group's investments was $25.6 billion as at December 31, 2007, for a year-over-year increase of $2.9 billion. This increase is due to the combined effect of $10.1 billion of acquisitions, $6.8 billion of dispositions and a $0.4-billion decrease in the value of investments. Taking advantage of the strong market in the first half, the managers carried out significant dispositions representing twice the amount of 2006, which enabled them to take profits and create a substantial reserve that they can deploy at the bottom of the cycle.

Figure 52 presents the absolute risk for the Private Equity group. In 2007, the absolute risk of the Investments and Infrastructures portfolio was up because of the greater concentration of investments in certain categories and the increased use of leverage. The absolute risk of the Private Equity portfolio was relatively stable, however.

FIGURE 51

VALUE OF THE PRIVATE EQUITY GROUP'S INVESTMENTS

(in billions of dollars)

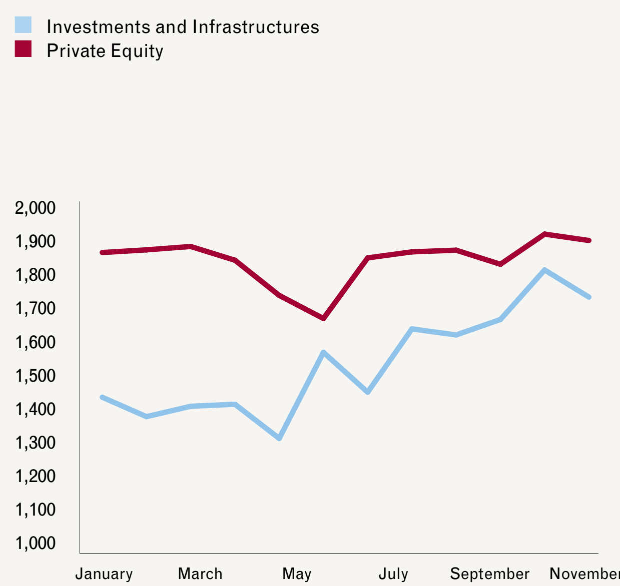


N. B.: Non-consolidated, before leverage and financial instruments.

FIGURE 52

ABSOLUTE RISK – PRIVATE EQUITY

(for 2007 – in basis points)



SPECIALIZED INVESTMENTS AND INFRASTRUCTURES PORTFOLIO

The Investments and Infrastructures portfolio returned 8.8% in 2007, or 22 b.p. (0.22%) less than its 9.0% return threshold. This return, however, exceeds the 6.8% return on the benchmark index by 197 b.p. (1.97%). The three-year return is 11.5%, or 251 b.p. (2.51%) more than the return threshold, but 304 b.p. (3.04%) less than the benchmark index.

More than half of the year's return is due to development capital. In this category, investments in the financial sector, with an emphasis on insurance companies, account for three-quarters of the gains, and investments in the industrials sector also fared well. Investments in the materials sector recorded a negative return, however.

The gains on infrastructure investments come mainly from the industrials and materials sectors.

Lastly, the managers also took advantage of the excellent market conditions at the start of the year to sell $1.9 billion of listed securities.

The fair value of the Investments and Infrastructures portfolio was divided among 206 companies and funds as at December 31, 2007. Figures 55 and 56 show the portfolio's breakdown by investment category and region. Investments in debt were up sharply to 35.4% of the portfolio, a level approaching that of infrastructure investments. From the geographic standpoint, the holdings are divided almost equally among Canada, Europe and the United States. Figure 57 shows the portfolio's sector breakdown, with industrials dominating, followed by energy and utilities.

Lastly, table 53 gives the top 10 holdings in the Investments and Infrastructures portfolio, and table 54, the portfolio's top five holdings in Québec.

TABLE 53

TOP 10 HOLDINGS – INVESTMENTS AND INFRASTRUCTURES

(as at December 31, 2007)

ACH Limited Partnership
Domtar Corp.
Enbridge Energy Partners LP
FGP Topco Limited (BAA)
HCA Inc.
Hochtief Airport Capital GmbH
Interconnector (UK) Limited
Kebexa Participation SAS
Noverco Inc. (Gaz Métro)
Yellow Pages Income Fund

TABLE 54

TOP FIVE QUÉBEC HOLDINGS – INVESTMENTS AND INFRASTRUCTURES

(as at December 31, 2007)

ACH Limited Partnership
Domtar Corp.
Noverco Inc. (Gaz Métro)
Power Financial Corp.
Yellow Pages Income Fund

PRIVATE EQUITY

FIGURE 55

CATEGORY BREAKDOWN – INVESTMENTS AND INFRASTRUCTURES

(percentage of fair value as at December 31, 2007)

- Infrastructures
- Debt
- Development capital
- Accumulation

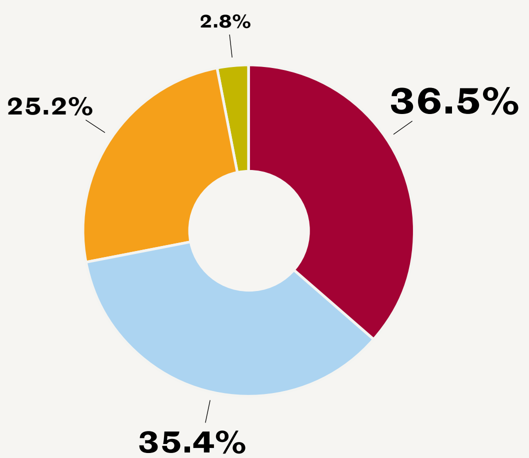
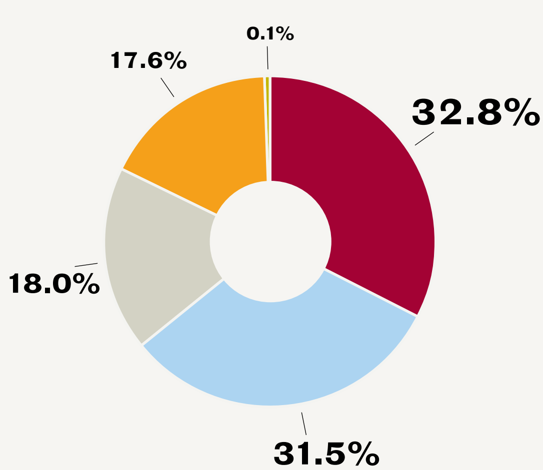


FIGURE 56

GEOGRAPHIC BREAKDOWN[1] – INVESTMENTS AND INFRASTRUCTURES

(percentage of fair value as at December 31, 2007)

- Europe
- United States
- Canada ex Québec
- Québec
- Asia and Pacific

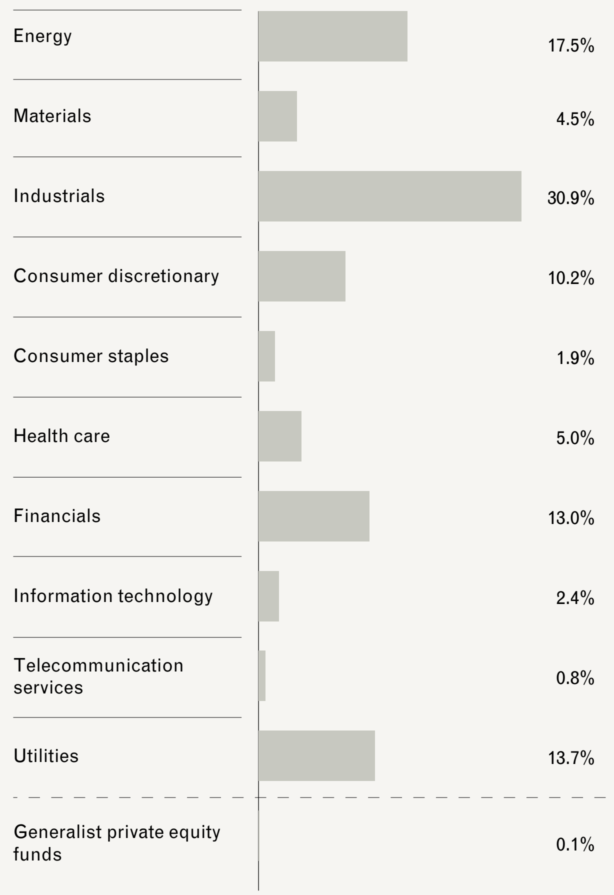


1 Based on region of activity

FIGURE 57

SECTOR BREAKDOWN – INVESTMENTS AND INFRASTRUCTURES

(percentage of fair value as at December 31, 2007)



N.B.: Investments held by generalist private equity funds have been broken down by sector, where possible.

SPECIALIZED PRIVATE EQUITY PORTFOLIO

In 2007, the Private Equity portfolio returned 16.2%, essentially because of leveraged buyouts. The portfolio exceeded its 12.0% return threshold by 418 b.p. (4.18%). It also generated 1,240 b.p. (12.40%) of value added in relation to its benchmark index. Over three years, the return is 25.3%, or 1,329 b.p. (13.29%) more than its return threshold and 1,943 b.p. (19.43%) more than its benchmark index.

After several years of exuberance, the leveraged-buyout market all but ground to a halt as a result of the liquidity crisis. The return for 2007 is therefore much closer to the expected long-term return and is very satisfactory in the circumstances. During the year, the managers concluded fewer buyout transactions but significantly increased their investments in restructuring and distressed-loan funds.

Almost all of the portfolio's return for 2007 was again due to leveraged buyouts. Investments in the consumer discretionary sector did particularly well. More specifically, the investment in Quebecor Media Inc. was by far the most profitable in the portfolio. Investments in industrials recorded a negative return, however.

The fair value of the investments in the Private Equity portfolio was divided among 349 companies and funds, as at December 31, 2007. As shown by figures 60, 61 and 62, leveraged buyouts represented 70.6% of the portfolio under management. Three-quarters of the investments were made outside Canada. The portfolio includes companies involved in many sectors of the economy, but mainly consumer discretionary. Table 58 presents the Private Equity portfolio's top 10 holdings. Table 59 gives the portfolio's five largest holdings in Québec.

TABLE 58

TOP 10 HOLDINGS – PRIVATE EQUITY

(as at December 31, 2007)

Avenue-CDP Global Opportunities Fund LP
Blackstone Firestone Principal Trans. Partners (Cayman) LP
CVI Global Value Fund LP
Cerberus Institutional Partners LP (Series Four)
European Directories SA
Grupo Corporativo ONO SA
ILM Investments LP
Park Square Capital Partners LP
Quebecor Media Inc.
Ray Investment SARL

TABLE 59

TOP FIVE QUÉBEC HOLDINGS – PRIVATE EQUITY

(as at December 31, 2007)

Camoplast Inc.
Fonds MinQuest I SEC
Fonds Télécom Média SEC
J.A. Bombardier (J.A.B.) Inc.
Quebecor Media Inc.

PRIVATE EQUITY

FIGURE 60

CATEGORY BREAKDOWN – PRIVATE EQUITY

(percentage of fair value – as at December 31, 2007)

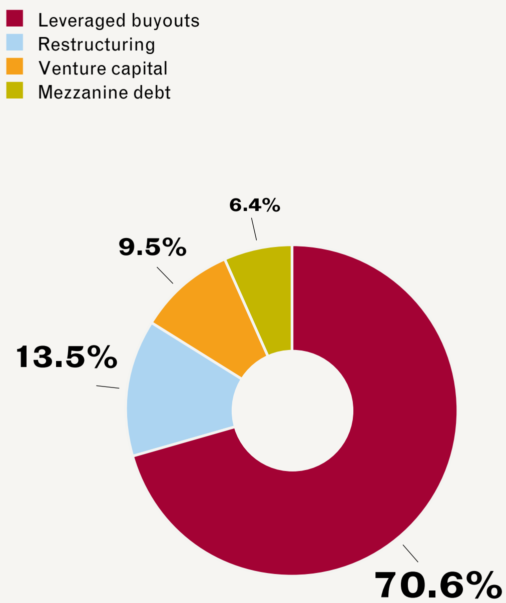
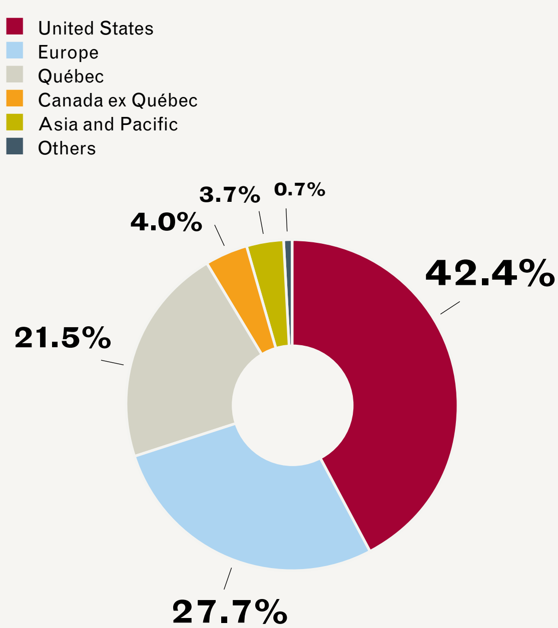


FIGURE 61

GEOGRAPHIC BREAKDOWN[1] – PRIVATE EQUITY

(percentage of fair value as at December 31, 2007)

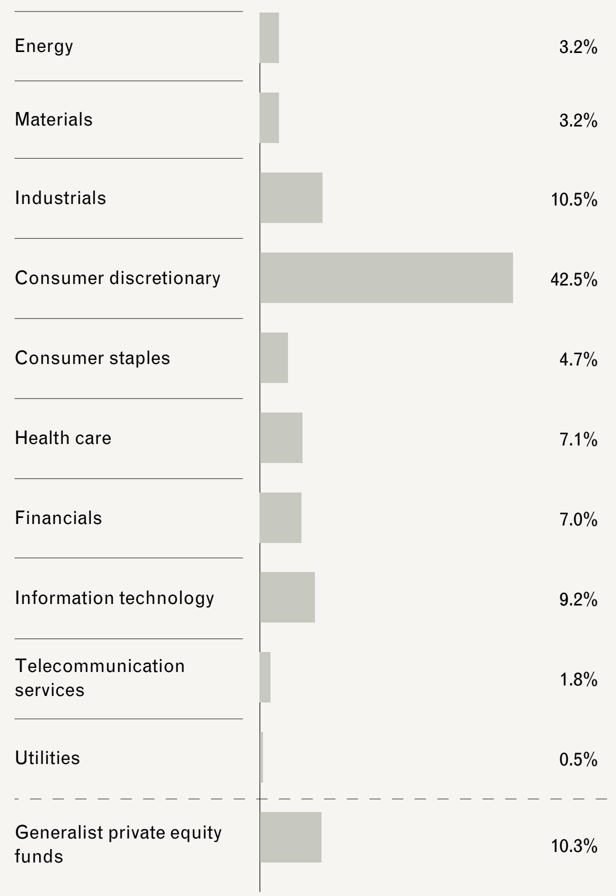


1 Based on region of activity.

FIGURE 62

SECTOR BREAKDOWN – PRIVATE EQUITY

(percentage of fair value as at December 31, 2007)



N.B.: Investments held by generalist private equity funds have been broken down by sector, where possible.

REAL ESTATE

MAJOR INCURSION INTO EMERGING MARKETS

The Real Estate group increased its commitments to emerging markets, with activity that includes its first partnerships in Russia and India. To manage this rapid international expansion, the group began a review of its international positioning and organizational structure, which will result in considerable changes in the years to come. The Real Estate group earned an overall return of 12.0% in 2007. Its transaction volume rose to a record $20.9 billion.

Q

EMERGING MARKETS
HAVE ASSUMED A
GREAT DEAL OF
IMPORTANCE
IN THE REAL ESTATE GROUP'S
STRATEGY IN RECENT YEARS.
WHAT ARE THE
OBJECTIVES
IN THESE COUNTRIES
?

A

THE GROUP'S THRUST IN THESE COUNTRIES IS TO ESTABLISH ITSELF IN PROMISING NEW MARKETS, WHILE DIVERSIFYING ITS ASSETS

The growth rates of the real estate sector in emerging markets are significantly higher than in the industrialized countries, and this trend should continue for several years.

The objective is to increase the proportion of its properties in emerging markets to about 20% over the next few years. The group was very active in these countries in 2007, with prospecting activities that led to new partnership agreements as well as major acquisitions and divestitures.

The group's strategy is based on two approaches. In China and India, for example, the markets are deep enough and the growth is sustained enough to justify a long-term presence. Teams from Ivanhoe Cambridge and Cadim have already been set up in Shanghai to carry out business development, and the same approach is planned for India. The goal is to acquire in-depth knowledge of these markets and form partnerships for the long term.

In other emerging markets where the conditions and outlook call for caution, the group is taking a more opportunistic approach based on shorter-term investments.

With impetus from the Real Estate group, the Caisse has begun a major review of the international component of its operations. The group's operations were central to this review, given the degree of advancement of the strategy and the needs specific to real estate investment. More than 30 managers from the Caisse and its subsidiaries have been interviewed, and about 30 institutions, primarily large institutional fund managers, have been surveyed about their practices. As a result of this study, considerable changes will be made to the group's organizational structure starting in 2008.

REAL ESTATE

INVESTMENT PHILOSOPHY

TO ACHIEVE ITS TARGET RETURNS, THE REAL ESTATE GROUP FAVOURS:

- Active management to create value with asset turnover and arbitrage between markets, holding vehicles and products according to the position in the real estate cycle;
- Partnership strategies to secure expertise on local markets, act on opportunities more effectively and reduce risk; and
- Rigorous management of leverage and concentration risks for optimal profitability.

TABLE 63

SPECIALIZED PORTFOLIO MANAGEMENT BY THE REAL ESTATE GROUP

(as at December 31, 2007)

Specialized portfolio	**Real Estate**		**Real Estate Debt**
Investment categories	Investment Asset and portfolio management, financial engineering Development and construction Building operation Advisory services		Real estate financing Origination, underwriting, closing and servicing of real estate loans Securitization and issuance of real estate financing products Investment
Management type	Active internal and partnership		Active internal and partnership
Management approach	Discretionary		Discretionary
Main management styles and investment strategies	Conventional and prestige investments	Opportunistic investments	Underwriting of real estate financing Purchase of securities
Main analytical approach	Top-down and bottom-up	Top-down and bottom-up	Bottom-up
Investment horizon	More than 5 years	Less than 3 years	1 to 10 years

HIGHLIGHTS

SPECIALIZED REAL ESTATE DEBT PORTFOLIO

- The Real Estate Debt portfolio grew by more than 26.4%, going from $9.1 billion to $11.5 billion, despite the unusually difficult investment climate caused by the credit squeeze.
- The managers carried out several major financings in various sectors, including:
  - A $305-million loan to Intrawest for a residential project in Hawaii;
  - A $165-million financing for the development of a parcel of land by Walton Development in Calgary;
  - A $121-million mortgage loan to Primaris REIT for Place d'Orléans shopping centre in Orleans, Ontario; and
  - An $85-million loan to Groupe Germain to build a mixed project (hotel, office, residential) in Calgary.
- In the United States, Cadim was involved in financing packages for the acquisition and privatization of Equity Office Properties by Blackstone Group ($400 million) and of Trizec Properties by Brookfield Properties and Blackstone Group ($375 million).
- Cadim carried out the largest resecuritization operation in its history, a $3.4-billion offering of commercial real estate collateralized debt obligations on the U.S. market. This offering enabled it to position the portfolio in anticipation of improved liquidity in this market. It was carried out in mid-November and had little impact on the 2007 return.
- A new organizational structure will be put in place in 2008 with the creation of a subsidiary that will focus exclusively on real estate debt.

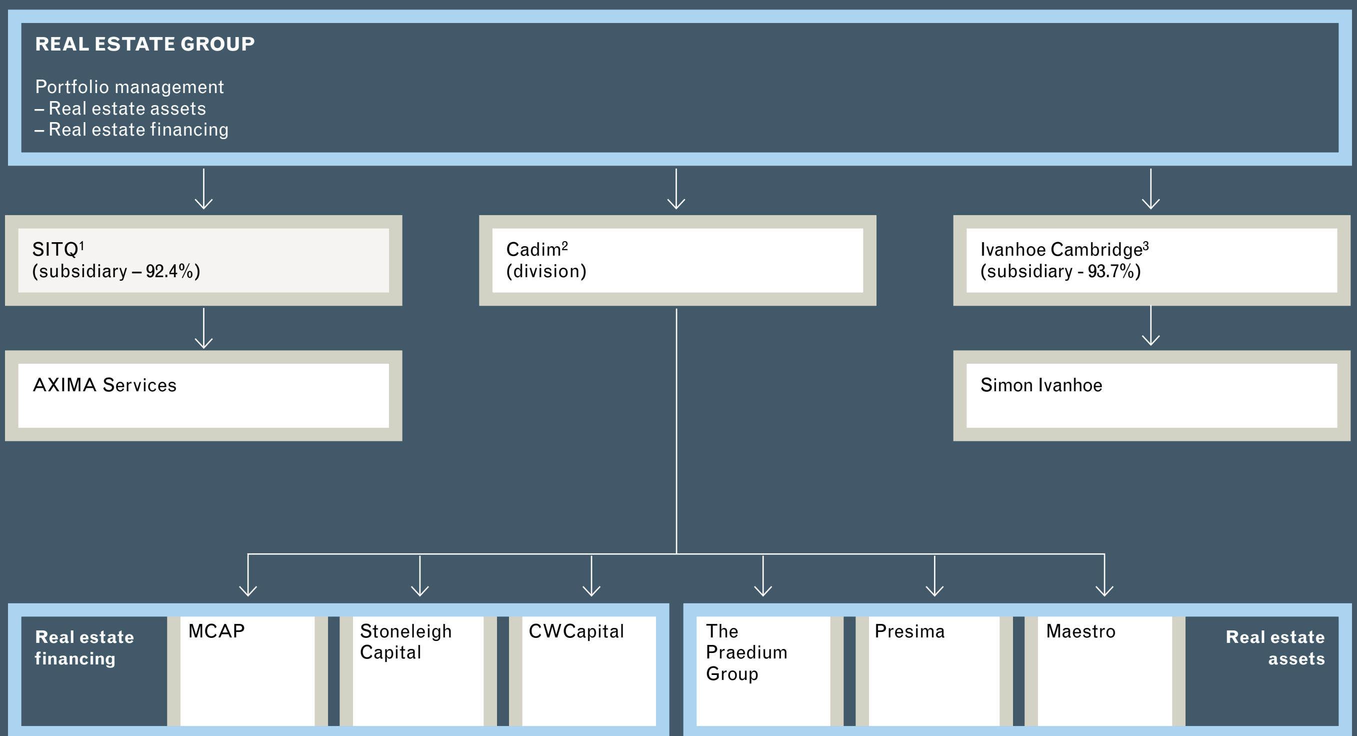
SPECIALIZED REAL ESTATE PORTFOLIO

- In line with its strategy, the Real Estate group entered and accentuated its presence in the four main emerging markets:
  - Ivanhoe Cambridge took its first steps in Russia with an investment in a Moscow shopping centre in partnership with Europolis, an Austrian real estate manager. SITQ did likewise through the Marbleton Property Fund.
  - The first commitments in India were made by Cadim under two partnership agreements, the one with Pacifica for eight development projects, and the other, with Vornado Realty Trust and The Chatterjee Group, involving a $600-million real estate fund.
  - SITQ made its first investment in China by taking a stake in the residential developer Canada China Property Investment.
  - Lastly, Ivanhoe Cambridge stepped up its presence in Brazil with a partnership acquisition of two new shopping centres, becoming the third-largest owner of shopping centres in Brazil.
- The Real Estate group authorized $1.8 billion of new commitments to development projects, particularly in Calgary, Germany and France. For example, SITQ acquired almost all of the French company Lucia, which owned the residual interest in Tour T1 and Immeuble B, two development projects in La Défense, near Paris.
- SITQ also acquired substantial interests in 1745 Broadway and Citi Towers, two prestigious properties in New York.
- Cadim was the main investor in a consortium that acquired Legacy Real Estate Investment Trust and took it private. With this transaction, Cadim became the owner of 14 prestigious hotels in Canada and the United States – including the Château Frontenac in Québec City and the Queen Elizabeth in Montréal – with a $1.8-billion stake owned jointly with Westmont Hospitality Group.
- René Tremblay, President and Chief Executive Officer of Ivanhoe Cambridge, became Chairman of the International Council of Shopping Centers, with a one-year mandate. He now heads the largest shopping centre industry association in the world, with 70,000 members in more than 80 countries.
- In 2008, the managers are aiming to double their commitments to emerging markets and to continue diversifying the portfolio with other promising products and markets. They are considering development projects, publicly traded companies, and products and markets affected by the credit crunch.

REAL ESTATE

FIGURE 64

ORGANIZATION CHART OF REAL ESTATE GROUP



1 Paul D. Campbell, President and Chief Executive Officer, SITQ
2 Richard Dansereau, President and Chief Operating Officer, Cadim
3 René Tremblay, President and Chief Executive Officer, Ivanhoe Cambridge

TWO SPECIALIZED PORTFOLIOS: REAL ESTATE AND REAL ESTATE DEBT

The Real Estate group invests in equity and financing products in the office and business park, retail, hotel and residential sectors in the Americas, Europe and Asia. The group co-ordinates the operations of its subsidiaries Ivanhoe Cambridge and SITQ, as well as its Cadim division, whose holdings are divided into two specialized portfolios: Real Estate Debt and Real Estate.

DIVISION AND MAIN SUBSIDIARIES

CADIM is involved in merchant banking and real estate investment management in Canada, the United States, Europe and Asia. Its investments include opportunistic products that are usually held for less than three years, as well as hotels and multiresidential buildings. Cadim also manages a large debt portfolio in addition to offering advisory and structured-finance services. It had $40.3 billion of total assets under management as at December 31, 2007. Cadim is a division of the Caisse de dépôt et placement du Québec.

IVANHOE CAMBRIDGE owns, manages, develops and invests in shopping centres in urban areas of Canada, the United States, Brazil, Europe and Asia. It owns about 70 shopping centres outright or in partnership, for total leasable area of more than 4.1 million square metres. Ivanhoe Cambridge had $16.3 billion of total assets under management as at December 31, 2007. The Caisse has a 93.7% stake in Ivanhoe Cambridge, with the remainder held by four Canadian pension funds.

SITQ develops, invests in and manages office buildings and business parks owned outright or in partnership. Its portfolio consists of more than 120 properties in large urban centres of Canada, the United States, France, the United Kingdom and Germany, for more than 4.0 million square metres of leasable area. It had $15.1 billion of total assets under management as at December 31, 2007. The Caisse owns 92.4% of SITQ. Five other shareholders are Canadian pension funds.

OTHER SUBSIDIARIES AND AFFILIATES

CANADA

AXIMA SERVICES specializes in technical management of office buildings. Its operations take in more than 2.3 million square metres in Québec.

MAESTRO is a real estate asset manager that specializes in residences for seniors and students. It has $1.0 billion of assets under management.

MCAP manages real estate debt assets in four main sectors: residential and commercial mortgages, construction loans and equipment financing. It has $10.2 billion of assets under management or administration.

PRESIMA manages an international portfolio of publicly traded real estate securities. It has $1.7 billion of assets under management.

UNITED STATES

CWCAPITAL manages real estate debt assets in all sectors of the industry. It has $12.0 billion of assets under management or administration.

THE PRAEDIUM GROUP is a real estate asset manager that specializes in mid-sized unproductive and undervalued assets. It has $3.8 billion of assets under management.

EUROPE

SIMON IVANHOE is a shopping centre developer, owner and manager with $1.8 billion of assets under management or administration.

STONELEIGH CAPITAL is a manager that specializes in real estate financing products with $1.1 billion of assets under management or administration.

REAL ESTATE

OVERALL RETURN AND SPECIALIZED PORTFOLIO ANALYSIS

In the past three years, the Real Estate group has put in place a diversification strategy, particularly to avoid excessive concentration in cities and sectors vulnerable to the ups and downs of the financial markets. To reduce this risk, the group focused on certain niches, especially emerging markets, rapidly growing markets (Western Canada), underexploited areas (shopping centres in Germany), development projects, hotels and distressed loans. This strategy has enabled the group to record results that are generally positive.

The Real Estate group earned an overall return of 12.0% in 2007, or 343 b.p. (3.43%) less than the benchmark index. The details of the returns earned by the group's portfolios over one year, three years and five years are given in table 65. Over the past five years, the Real Estate group has an outstanding return of 18.9% and ranks in the first quartile of pension funds that invest in real estate. This type of return is unlikely to be maintained over many years, however, and should revert to a level closer to the long-term expectations.

FIGURE 67

ACTIVE RISK – REAL ESTATE

(for 2007 – in basis points)

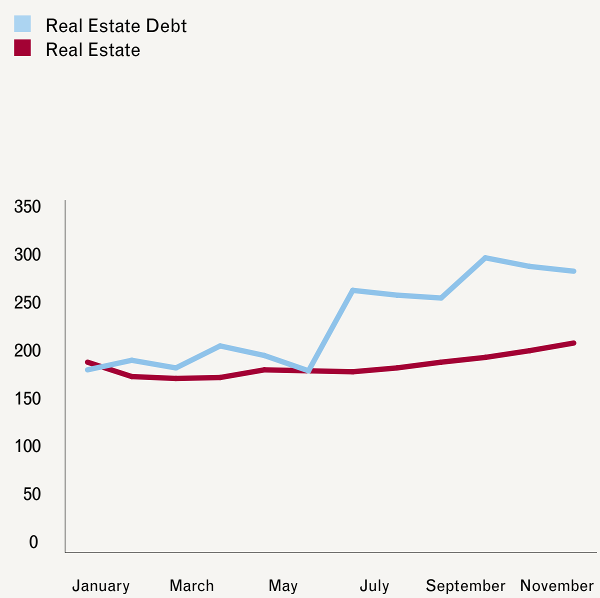


TABLE 65

RETURN ON REAL ESTATE

(for periods ended December 31, 2007)

	1 year			3 years				5 years			
	Return %	Index[1] %	**Spread b.p.**	Return %	Index[1] %	**Spread b.p.**	Information ratio	Return %	Index[1] %	**Spread b.p.**	Information ratio
Real Estate Debt	0.9	3.5	**(258)**	6.0	5.1	**99**	0.4	7.9	5.8	**211**	1.0
Real Estate	20.3	24.4	**(409)**	29.6	27.4	**213**	n.a.	26.6	22.2	**433**	n.a.

1 The description of the indexes is given in the "General notes."

TABLE 66

REAL ESTATE GROUP'S TOTAL ASSETS UNDER MANAGEMENT

(fair value as at December 31, 2007 – in billions of dollars)

	Depositors' net assets	Depositors' total assets	Assets under management or under administration	Total assets under management	
Real Estate Debt portfolio	**11.5**	**12.2**	**–**	**12.2**[1]	**17.0%**
SITQ		11.2	3.9	15.1	21.1%
Ivanhoe Cambridge		12.1	4.2	16.3	22.7%
Cadim		6.7	21.4	28.1[1]	39.2%
Real Estate portfolio	**17.6**	**30.0**	**29.5**	**59.5**	**83.0%**
Total	**29.1**	**42.2**	**29.5**	**71.7**	**100.0%**

1 The assets in the Real Estate Debt portfolio are managed by Cadim affiliates. As at December 31, 2007, Cadim's total assets under management amounted to $40.3 billion.

The Real Estate group managed $29.1 billion of depositors' net assets as at December 31, 2007, with $11.5 billion in the Real Estate Debt portfolio and $17.6 billion in the Real Estate portfolio. During the year, the managers of the Real Estate Debt portfolio made investments that increased depositors' net assets by more than 26.4%, or $2.4 billion, in relation to 2006. As for the Real Estate portfolio, depositors' net assets rose by $3.5 billion, for growth of 24.8%. Table 66 gives the breakdown of the Real Estate group's total assets under management.

The group's transaction volume in 2007 totalled a record $20.9 billion, with $7.0 billion of acquisitions and investments, $1.0 billion of leasehold improvements, construction and renovation projects, $2.8 billion of sales and $10.1 billion of real estate financing transactions.

Figure 67 gives the active risk for the Real Estate group. The active risk of the Real Estate Debt portfolio increased substantially at mid-year, primarily because of the liquidity crisis and its impact on subordinated debt securities.

SPECIALIZED REAL ESTATE DEBT PORTFOLIO

Depositors' net assets in the Real Estate Debt portfolio amounted to $11.5 billion as at December 31, 2007, an increase of $2.4 billion over the previous year.

The loans provided during the year ranged from $0.3 million to $422 million, and transactions totalled $10.1 billion. Figures 69 and 70 show the portfolio's sector and geographic breakdowns at year-end.

Tables 68 and 71 give the portfolio's top 10 loans and top five Québec loans, respectively.

TABLE 68

TOP 10 LOANS – REAL ESTATE DEBT

(as at December 31, 2007)

BRE / Hospitality Europe Holding BV
Buckingham Securities II - B
Buckingham Securities II - C
Legacy Hotels Real Estate Investment Trust
Menkes Consilium and AI
R-Roof Holdings II LLC
Star GT Acquisition SAS (Starwood Capital Group)
Starwood Capital Group LLC
TRZ Mezz 4 LLC, TRZ CN Mezz 4A LP (Trizec Properties)
Tour de la Bourse SPE Inc.

FIGURE 69

SECTOR BREAKDOWN – REAL ESTATE DEBT

(percentage of fair value – as at December 31, 2007)

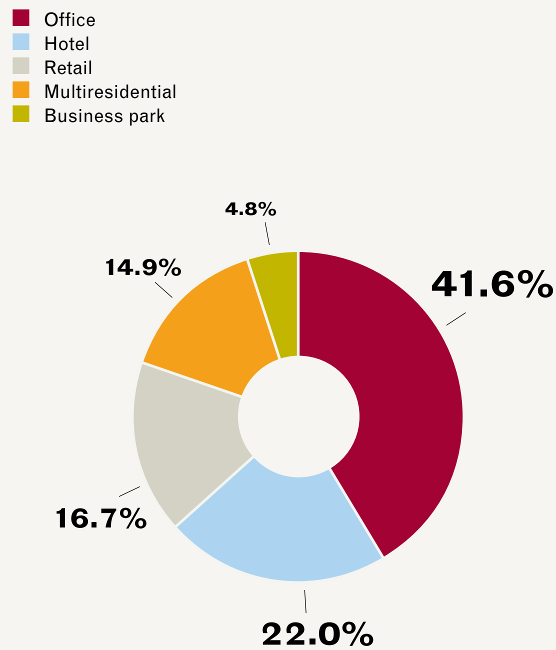
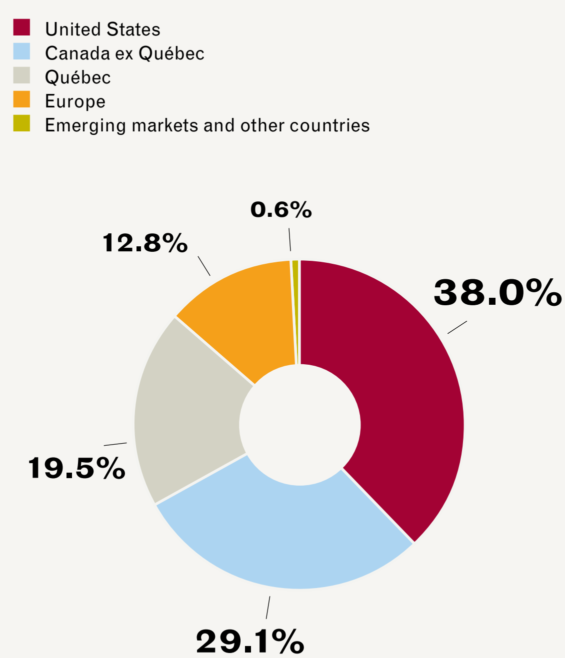


FIGURE 70

GEOGRAPHIC BREAKDOWN – REAL ESTATE DEBT

(percentage of fair value – as at December 31, 2007)



REAL ESTATE

TABLE 71

TOP FIVE QUÉBEC LOANS – REAL ESTATE DEBT

(as at December 31, 2007)

1200 McGill College Inc.
Borealis Real Estate Investment Trust
CDM de Montréal - 1 Inc. (Cité du multimédia)
Fonds de placement immobilier Cominar
Tour de la Bourse SPE Inc.

The Real Estate Debt portfolio returned 0.9% in 2007, underperforming its benchmark index by 258 b.p. (2.58%). Over five years, the portfolio has a solid return of 7.9% and outperformed the index by 211 b.p. (2.11%).

Generally speaking, loans provided relatively high current income. The portfolio contains exclusively commercial mortgages and therefore was not affected directly by the subprime mortgage crisis in the United States. In fact, the delinquency, default and loss rates remained low all year long.

The liquidity crisis in the United States increased credit spreads substantially, however, causing the portfolio's market value to decline. The subordinated debt assets in the portfolio, in particular, saw a significant devaluation on the listed markets in the United States.

SPECIALIZED REAL ESTATE PORTFOLIO

Depositors' net assets totalled $17.6 billion as at December 31, 2007.

In the shopping centre sector, Ivanhoe Cambridge's transactions totalled $1.4 billion in 2007, including $0.4 billion of acquisitions, $0.4 billion of sales and $0.6 billion of leasehold improvements, construction and renovation projects.

In the office building and business park sector, acquisitions totalled $2.5 billion, with $1.0 billion of sales and $0.3 billion of leasehold improvements, construction and renovation projects bringing SITQ's total transactions to $3.8 billion.

Lastly, in opportunistic products, hotels and multiresidential buildings, Cadim's transactions totalled $5.6 billion, including $4.1 billion of acquisitions, $1.4 billion of sales and $0.1 billion of leasehold improvements, construction and renovation projects.

Figures 72 and 73 give the sector and geographic breakdowns at year-end.

FIGURE 72

SECTOR BREAKDOWN – REAL ESTATE

(percentage of fair value – as at December 31, 2007)

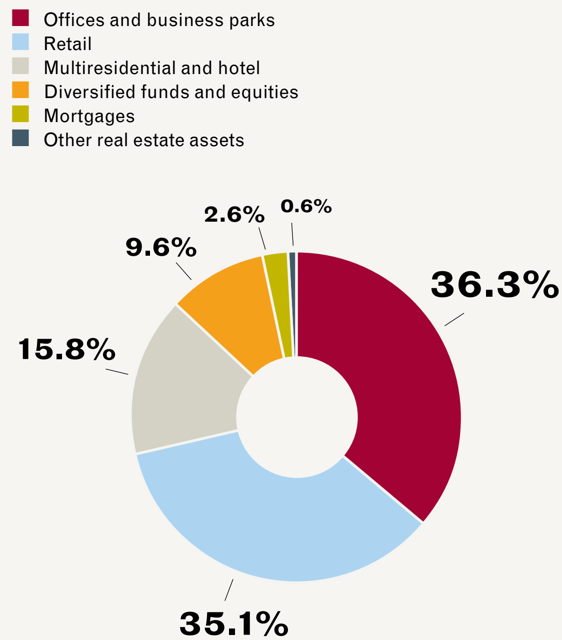


FIGURE 73

GEOGRAPHIC BREAKDOWN – REAL ESTATE

(percentage of fair value – as at December 31, 2007)

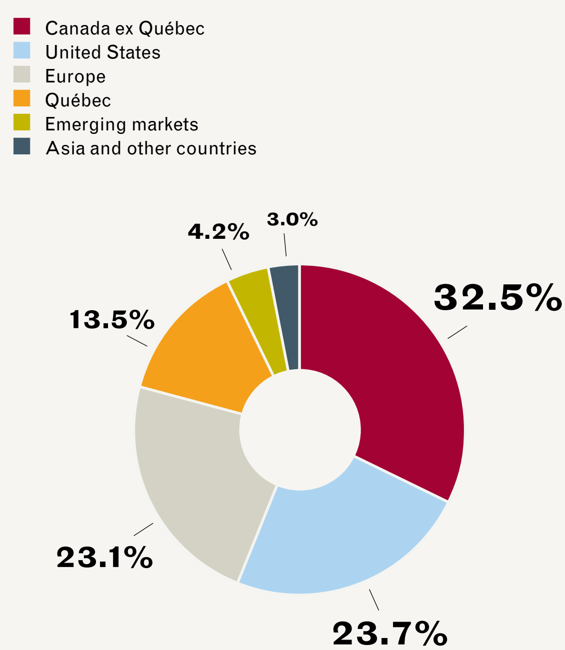


Table 74 gives the portfolio's top 10 investments in the world. The Real Estate group is also very active on markets close to home and continues to increase its holdings of prestigious buildings in Québec. Table 75 gives the portfolio's top five investments in Québec.

The Real Estate portfolio returned 20.3% in 2007, underperforming the index by 409 b.p. (4.09%). In relation to the 8.0% return threshold, the value added amounts to 1,229 b.p. (12.29%), however. The return over longer periods gives a better idea of the Real Estate portfolio managers' performance. For example, the 26.6% five-year return exceeds the index by 433 b.p. (4.33%).

After the enthusiasm of recent years, the real estate investment market slowed in the second half of 2007 amid tighter lending conditions. The market's fundamentals remained favourable, however, as rents were generally up and vacancy rates down, especially for office buildings and shopping centres. Real estate internal rates of return generally decreased during the year for the properties in the portfolio.

Investments in office buildings generated the best returns. SITQ recorded capital gains in all its markets, as a result of lower internal rates of return, falling vacancy rates and rising rents. The excellent results for properties in Boston, Vancouver and Paris are especially notable.

In the case of shopping centres, Ivanhoe Cambridge recorded capital gains because of lower internal rates of return and improved valuations for almost all its buildings. Shopping centres in Brazil saw exceptional increases in value, and properties in Western Canada made substantial contributions.

Finally, Cadim obtained its best results with opportunistic products, especially the Lone Star funds and its increasing investments in the hotel sector. Investments in residential rental properties generated satisfactory returns, while investments in publicly traded real estate companies declined.

TABLE 74

TOP 10 INVESTMENTS – REAL ESTATE

(as at December 31, 2007)

Investment	Subsidiary or division	Leasable area (m^2)	Ownership (%)
11-13 Theresienhöhe, Munich, Germany	SITQ	58,658	100.0
151 Buckingham Palace Road, London, United Kingdom	SITQ	18,020	100.0
388-390 Greenwich Street, New York, United States	SITQ	244,769	49.4
1515 Broadway, New York, United States	SITQ	150,485	45.0
Lone Star (Asia-Europe funds)	Cadim	–	–
Madrid Xanadú, Madrid, Spain	Ivanhoe Cambridge	93,508	100.0
Metropolis at Metrotown, Burnaby, British Columbia	Ivanhoe Cambridge	223,264	100.0
St. Enoch Shopping Centre, Glasgow, United Kingdom	Ivanhoe Cambridge	70,917	100.0
Tour T1, Paris, France	SITQ	67,123	95.6
Vaughan Mills, Vaughan, Ontario	Ivanhoe Cambridge	103,379	100.0

TABLE 75

TOP FIVE QUÉBEC INVESTMENTS – REAL ESTATE

(as at December 31, 2007)

Investment	Subsidiary or division	Leasable area (m^2)	Ownership (%)
1000 de La Gauchetière Ouest, Montréal	SITQ	85,307	100.0
Centre CDP Capital, Montréal	SITQ	52,922	100.0
Eaton Centre, Montréal	Ivanhoe Cambridge	26,923	100.0
Place Ville Marie, Montréal	SITQ	239,256	50.0
Rockland Centre, Montréal	Ivanhoe Cambridge	61,023	100.0

ANALYSIS OF COMBINED FINANCIAL STATEMENTS

The financial statements of the Caisse de dépôt et placement du Québec are combined, which means they include the accounts of the Caisse's subsidiaries, the General Fund, the Individual Funds and the specialized portfolios. Depositors' holdings presented in the Combined Statement of Net Assets reflect the combination of the net account value of each Caisse depositor.

The combined financial statements are prepared according to generally accepted accounting principles in Canada, as provided for by the *Act respecting the Caisse de dépôt et placement du Québec.*

As required by law, the Auditor General of Québec audited the Caisse's books in 2007, and his report accompanies the combined financial statements. Over all, the Auditor General reports on 54 financial statements, namely the Caisse's combined statements and those of the General Fund, the depositors' 34 individual funds and the 18 specialized portfolios. He has issued unqualified opinions for all the financial statements.

FUTURE OF ACCOUNTING STANDARDS IN CANADA

In 2006, the Accounting Standards Board of the Canadian Institute of Chartered Accountants (CICA) developed a strategic plan in which it calls for the adoption of International Financial Reporting Standards (IFRS) in Canada in three years, or starting in 2011. As a result of this decision, the Caisse did a comparative analysis in 2006 to identify the main differences between generally accepted accounting principles (GAAP) in Canada and the IFRS. In 2008, the Caisse will update this analysis as a function of changes in the IFRS to develop the required implementation plan. Personnel training on the new standards will continue during their implementation.

ADOPTION OF NEW ACCOUNTING STANDARDS IN 2007

The Caisse has adopted the provisions of Section 3855 of the CICA Handbook, "Financial Instruments – Recognition and Measurement," which took effect on January 1, 2007. Only the provisions regarding recognition, purchase or sale with standard delivery time and measurement of fair value apply to the Caisse's investments, given that the Caisse is defined as an "investment company" under Accounting Guideline No. 18. The impact of the application of these provisions involves mainly measurement of the fair value of investments traded on active markets (equities and derivatives).

The adoption of Section 3855 also affected the accounting treatment of transaction costs directly attributable to the acquisition of investments. Previously, transaction costs were capitalized in investment costs. When the investment was sold before year-end, the transaction costs were moved to gains/losses on the sale of investments in the statement of income. When the investment was still on the books at year-end, the obligation to record the investment at fair value meant that the transaction costs also moved to the statement of income through unrealized increases/decreases in the value of investments. With the new standard, transaction costs related directly to the acquisition of investments must be recorded directly in gains/losses on the sale of investments. For fiscal 2007, transaction costs were $150 million versus $120 million in 2006.

There has been no restatement of the comparative combined financial statements as a result of the adoption of Section 3855. Still, there has been a restatement of certain opening balances of depositors' holdings as a result of the capitalization of transaction costs in investment costs as at January 1, 2007.

Moreover, the Caisse has adopted the provisions of Section 3861 of the CICA Handbook, "Financial Instruments – Disclosure and Presentation," which took effect on January 1, 2007. The main impact of these provisions is the obligation to include a description of management's objectives and policy for financial risk management. The information provided concerning financial risks enable users of the financial statements to evaluate the scope of the risks related to the Caisse's financial instruments. It is therefore important that the Caisse provide precise explanations of its objectives and policy for financial risk management. The adoption of Section 3861 has given rise to the addition of note 8 to the combined financial statements, "Identification and management of risks related to financial instruments."

On January 1, 2007, the Caisse adopted the amendments proposed by the CICA to the accounting guidelines "Consolidation of Variable Interest Entities" (Ac-G15) and "Investment Companies" (AcG-18). Pursuant to these new provisions, an investment company that is the main beneficiary of a variable-interest entity (VIE) that is itself an investment company may no longer consolidate the VIE, except in the case of specific circumstances defined in AcG-18.

This amendment was adopted retroactively, and the combined financial statements have been restated. The restatement involved a decrease in assets and liabilities in the amount of $344 million but had no impact on the combined statement of income and changes in net assets or depositors' holdings as at December 31, 2006.

ANALYSIS OF COMBINED FINANCIAL STATEMENTS

ADOPTION OF NEW ACCOUNTING STANDARDS FOR 2008

In 2007, the CICA published Section 3862, "Financial Instruments – Disclosures," and Section 3863, "Financial Instruments – Presentation," which replace Section 3861, "Financial Instruments – Disclosure and Presentation." In Section 3862, greater emphasis is placed on information to be provided on the risks associated with recorded and off-balance-sheet financial instruments and the way these risks are managed. The presentation requirements were not modified, however, and Section 3863 carries forward unchanged the presentation requirements for financial instruments in Section 3861. The Caisse will apply these new sections starting with the year ended December 31, 2008.

TOTAL ASSETS UNDER MANAGEMENT

The net assets belonging to the Caisse's various depositors total $155.4 billion as at December 31, 2007, an increase of $11.9 billion in relation to 2006. This increase is due to $7.9 billion of net investment results and $4.0 billion of depositors' net contributions. In 2006, the increase was $21.3 billion, with $17.8 billion due to net investment results and $3.5 billion to depositors' net contributions.

If assets financed primarily by borrowing (liabilities contracted mainly to optimize depositors' returns) totalling $71.7 billion in 2007, versus $64.0 billion in 2006, are added, depositors' total assets rise to $227.1 billion in 2007 compared with $207.6 billion in 2006, an increase of $19.5 billion.

FAIR VALUE OF INVESTMENTS

Investments are recorded in the financial statements at fair value. In the case of liquid investments, or almost 74% of the total, the Caisse uses quoted market prices or methods recognized by organized financial markets to determine fair value. In the case of private equity and real estate, or about 21% of its investments, fair value is determined according to a valuation process that corresponds to good practices used by these industries. This valuation process is reviewed annually as a function of the changing standards and practices of Canadian and international organizations. With respect to investments in third-party asset-backed commercial paper (ABCP) being restructured, which correspond to 5% of the Caisse's investments, the valuation method is described in the paragraphs that follow.

THIRD-PARTY ASSET-BACKED COMMERCIAL PAPER BEING RESTRUCTURED

As at December 31, 2007, the Caisse held investments in the Canadian ABCP market. ABCP is a short-term financing instrument issued by trusts, also referred to as "conduits," generally for maturities ranging from one to three months. The third-party ABCP being restructured is backed by various assets, such as mortgage or consumer debt and financial assets. The subprime mortgage crisis in the United States caused disruption on the international markets, which resulted in a liquidity crisis on the Canadian ABCP market in mid-August 2007. Since August 13, 2007, the Caisse has not been able to redeem, on maturity, the third-party ABCP being restructured that it holds. At the time of its acquisition by the Caisse, the third-party ABCP being restructured was rated "R-1 (high)" by the rating agency DBRS Limited (DBRS), namely the highest rating assigned by DBRS for asset-backed commercial paper.

Considerable progress has been made toward restructuring the third-party ABCP since mid-August, 2007, and a restructuring proposal was made public by the Pan-Canadian Investors Committee on December 23, 2007.

INVESTMENT VALUATION PROCESS

LIQUID INVESTMENTS

The fair value of investments is established by means of valuation methods used in capital markets, such as discounting of future cash flows at the current interest rate, closing prices on major stock exchanges and data provided by securities brokers or other recognized specialist organizations.

On a quarterly basis, some of the portfolios and, at year-end, all portfolios of unlisted liquid products are subject to valuation by independent professionals. These products, which include mainly bonds and over-the-counter derivatives, are evaluated with respect to the valuation models and data used.

PRIVATE EQUITY

The fair value of private equity investments is established semi-annually as at June 30 and December 31, unless important circumstances entail a writedown of the value of an investment at another point in the year. The valuation is based on a valuation policy adopted by the Caisse's Board of Directors. The policy is based on the industry's best practices.

The policy provides that the valuation of a private equity investment is first determined by the managers responsible for the investments concerned. It is then approved by the senior managers of the Private Equity group.

Investments for which the fair value is higher than a pre-established materiality threshold must be submitted to an independent valuation committee. Given the specialized nature of private equity investments, several valuation committees are used. These committees, which report to the Caisse's Audit Committee, are composed of independent valuation professionals. The Auditor General of Québec attends all the meetings of the independent valuation committees. The annual valuation process is supplemented internally by periodic individual valuations and as events occur.

REAL ESTATE

The fair value of real estate investments is established on an annual basis as at December 31, unless important circumstances entail a writedown of the value of an investment at another point in the year. Valuation of the investments in the Real Estate portfolio is based on a valuation policy adopted by the Caisse's Board of Directors. The policy is based on the industry's best practices.

For the Real Estate portfolio, external chartered appraisers certify the fair value of real estate assets. For other real estate investments, fair value is usually determined by external managers and, for debt associated with real estate investments, by internal managers. Moreover, the real estate subsidiaries' external auditors perform work involving compilation of fair values when the audited financial statements are produced. Finally, in auditing the Caisse's books and accounts, the Auditor General of Québec relies on the work of external auditors and reviews all valuation reports.

In the case of the Real Estate Debt portfolio, the fair value of mortgage loans and securities is established according to the discounted value of future contractual cash flows at the market interest rate. This is the rate that can be obtained for loans or securities with similar conditions and maturity dates. In positions where cash flow spread cannot be estimated reasonably or reliably, the fair value corresponds either to the fair value of any asset given as collateral for the security, after deduction of foreseeable realization costs and any amount legally owed to the borrowers, or to the relevant market price for the security. The year-end valuation of the Real Estate Debt portfolio was reviewed by independent valuation professionals.

ANALYSIS OF COMBINED FINANCIAL STATEMENTS

VALUATION OF THIRD-PARTY ABCP BEING RESTRUCTURED

Given that there is no active market for the third-party ABCP being restructured, the Caisse established, in accordance with the guidelines of the Canadian Institute of Chartered Accountants (CICA), the fair values of its holdings of various types of ABCP. To do so, it used a valuation technique based on a financial model whose assumptions and probabilities reflect uncertainties related to the amounts and the maturities of the cash flow, the credit risk of the underlying debt and financial assets and the return. The assumptions, based on the information available as at December 31, 2007, use as much as possible observable market data, such as interest rates and credit quality. The Caisse estimated the fair value of each series of third-party ABCP being restructured by calculating the present value of the projected cash flows according to various default and loss scenarios, the maturities of the securities as well as a relevant discount rate increased by a premium to reflect the current illiquidity of the third-party ABCP being restructured.

The Caisse took into account the probability that the historic cumulative default rates, corresponding to the discount period, would be more severe in the next few years. The scenario corresponding to the success of the restructuring proposal takes into account an estimated default rate that makes it possible to establish an amount of "unproductive" assets with adverse impacts on the forecast cash flow. For the synthetic and hybrid assets, the estimated default rates apply to all the underlying assets. For the traditional assets and the synthetic assets that are excluded from the restructuring proposal, the Caisse applied a method similar to that used for the assets that are included, applying a multiplier to increase the level of the losses, given the uncertainty surrounding their restructuring. In the event that the restructuring proposal was not retained, the Caisse established scenarios based on an orderly liquidation or a forced liquidation of the synthetic and hybrid assets and the traditional assets. Moreover, the fair value of the high-risk assets has been reduced by 60%.

Management is of the opinion that the valuation technique used as at December 31, 2007, makes it possible to establish a reasonable estimate of the fair value of the third-party ABCP being restructured. Nevertheless, this estimate was established as a function of the information available as at December 31, 2007, the Caisse's assessment of the state of the financial markets and a weighted approach using a set of assumptions and probabilities, including that of the success of the restructuring proposal. Accordingly, the fair values established may vary significantly in subsequent periods. The most critical assumption regarding the valuation technique is based on the restructuring proposal's probability of success. Attributing greater weight to a liquidation scenario in the valuation technique would significantly decrease the estimated fair values. Conversely, acceptance of the restructuring proposal and a return to normal market conditions would increase the estimated fair values. The Caisse believes it is unlikely that the restructuring proposal will fail, given the stages already completed and its benefits for all stakeholders. The possible effect on the valuation technique of a 10% variation in the other assumptions and probabilities would not significantly change the estimate of the fair values as at December 31, 2007.

The Caisse recorded, against its portfolio of third-party ABCP being restructured, a total unrealized decrease in value of $1,897 million (including $30 million for restructuring costs) in its combined statement of income and changes in net assets for the year ended December 31, 2007. No interest receivable was recorded at year-end in respect of these securities.

TABLE 76

BREAKDOWN OF THIRD-PARTY ABCP BEING RESTRUCTURED IN ACCORDANCE WITH THE PAN-CANADIAN INVESTORS COMMITTEE'S PROPOSED CLASSIFICATION

(as at December 31, 2007 – in millions of dollars)

		Unrealized decrease in value and other		
	Par value	$	%	Fair value estimated
Synthetic and hybrid assets	10,526	(1,295)	(12)	9,231
Traditional assets	1,299	(103)	(8)	1,196
High-risk assets	782	(469)	(60)	313
Subtotal	12,607	(1,867)	(15)	10,740
Retructuring costs		(30)	–	
Total		**(1,897)**	**(15)**	

NET INVESTMENT RESULTS

Net investment results for 2007 totalled $7.9 billion compared with $17.8 billion in 2006 (table 77). This performance is due to four sources:

- Investment income (mainly interest income, dividends, fees and rents) net of operating expenses and external management fees ($6.2 billion);
- Net gains from the sale of investments (gains or losses realized on the sale of investments) ($9.4 billion);
- Net unrealized decreases in the value of investments and liabilities related to investments (appreciation or depreciation relative to changes in the fair value of the investments that the Caisse held as at December 31, 2007) ($5.8 billion); and
- Unrealized decrease in the value of third-party ABCP being restructured ($1.9 billion).

Investment income totalled $6.5 billion in 2007, versus $5.5 billion in 2006. If operating expenses and external management fees are excluded, this net income totalled $6.2 billion in 2007 and $5.3 billion in 2006. Investment income came from fixed-income securities ($3.7 billion in 2007 versus $3.3 billion in 2006) and variable-income securities ($2.8 billion in 2007 versus $2.2 billion in 2006). The differences between 2006 and 2007 are mainly due to the upward variation in average investment volume.

Net gains from the sale of investments totalled $9.4 billion in 2007, or $9.0 billion for variable-income securities and $0.4 billion for fixed-income securities. Net gains totalled $4.6 billion in 2006, or $4.8 billion for variable-income securities less $0.2 billion for fixed-income securities.

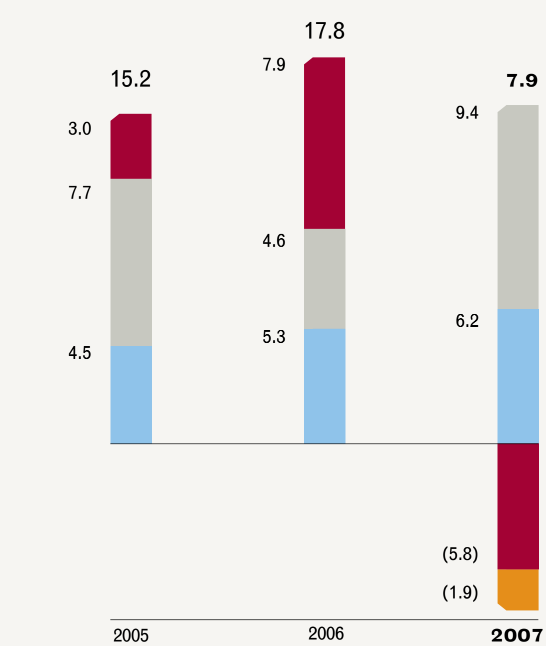
The net unrealized decrease in the value of investments was $7.7 billion in 2007, including a decrease of $1.9 billion in the value of third-party ABCP being restructured. The unrealized decrease in the value of investments (excluding third-party ABCP being restructured) was $5.8 billion in 2007, namely a decrease of $4.0 billion for variable-income securities and $1.8 billion for fixed-income securities, including liabilities related to investments. In 2006, the net unrealized increase in the value of investments was $7.9 billion, including $7.4 billion for variable-income securities and $0.5 billion for fixed-income securities, including liabilities related to investments.

FIGURE 77

CHANGES IN NET INVESTMENT RESULTS

(for periods ended December 31 – in billions of dollars)

- Unrealized increase (decrease) in the value of investments
- Net gains from the sale of investments
- Net investment results
- Unrealized decrease in the value of investments in third-party ABCP being restructured and other



ANALYSIS OF OPERATING EXPENSES AND EXTERNAL MANAGEMENT FEES

The Caisse's operating expenses represent all costs incurred to manage and administer the portfolio with the exception of external management fees. Operating expenses are presented in a separate item of the "Combined statement of income and changes in net assets." Expenses related to management of the Real Estate portfolio and the Real Estate Debt portfolio are included in operating expenses. Operating expenses related to management and administration of real estate assets and mortgages are deducted from real estate investment income and mortgage income, respectively.

Operating expenses totalled $261 million in 2007, up $34 million from the operating expenses in 2006. The increase is due mainly to growth in total assets under management in recent years.

External management fees represent amounts paid to external financial institutions, mainly institutional fund managers specializing in international equities, to manage funds belonging to the Caisse. External management fees are presented in a separate item of the "Combined statement of income and changes in net assets."

External management fees totalled $69 million in 2007 versus $54 million in 2006. The increase is due mainly to growth in the value of assets under management.

OPERATIONAL EFFICIENCY

The Caisse periodically reviews its procedures to maintain strict control over its operating expenses. Its objective is to keep operating expenses at a level that, taking into account the composition of its investments, is comparable to that of institutional fund managers of the same size with similar operations. For many years, the Caisse has taken part in exercises to benchmark its costs per asset class. Generally speaking, these costs compare favourably with those of its peers.

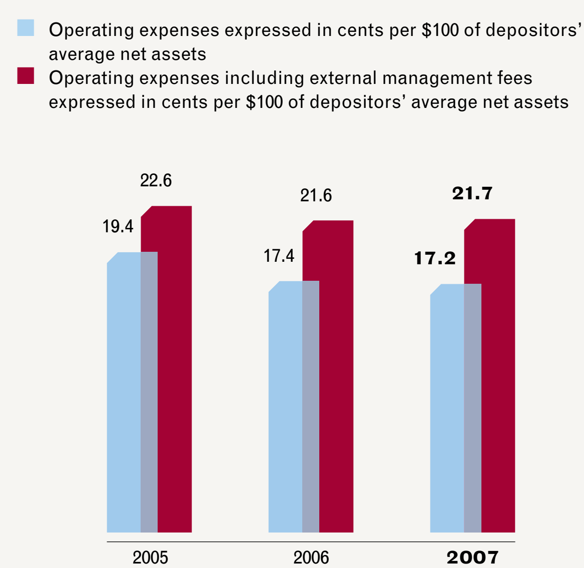
It is common practice for fund managers to express operating expenses in basis points, or the cost in cents to manage $100 of average net assets. Figure 78 shows operating expenses expressed in cents per $100 of depositors' average net assets for 2005, 2006 and 2007. Expressed in this way, the Caisse's operating expenses fell from 19.4 cents in 2005 to 17.2 cents in 2007. This favourable difference reflects the combined effect of the increase in depositors' average net assets and careful management of operating expenses.

Together, operating expenses and external management fees, expressed in cents per $100 of depositors' average net assets, fell from 22.6 cents in 2005 to 21.7 cents in 2007.

FIGURE 78

OPERATING EXPENSES AND EXTERNAL MANAGEMENT FEES[1] EXPRESSED IN CENTS PER $100 OF DEPOSITORS' AVERAGE NET ASSETS

(for periods ended December 31)



1 Including external management fees that were previously deducted from investment income. The figures for 2005 and 2006 have been restated.

Still, this measure is not ideally suited to the Caisse because the institution differs from other managers in that it assumes the cost of active management of investments financed by borrowing totalling $71.7 billion as well as management and administration, for clients, of portfolios of properties totalling $30.6 billion. Thus to monitor operating expenses related to its overall operations, the Caisse expresses its operating expenses as a function of average total assets under management.

Figure 79 shows operating expenses expressed in cents per $100 of average total assets under management for 2005, 2006 and 2007. Expressed in this way, the Caisse's operating expenses fell from 10.9 cents in 2005 to 10.2 cents in 2007. This favourable difference is due to the combined effect of the increase in average total assets under management and careful management of operating expenses.

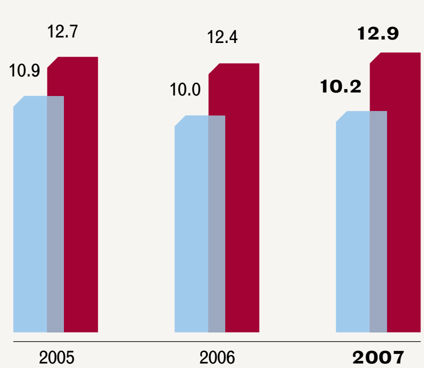
Operating expenses and external management fees expressed in cents per $100 of average total assets under management increased from 12.7 in 2005 to 12.9 in 2007.

FIGURE 79

OPERATING EXPENSES AND EXTERNAL MANAGEMENT FEES[1] EXPRESSED IN CENTS PER $100 OF AVERAGE TOTAL ASSETS UNDER MANAGEMENT

(for periods ended December 31)

- Operating expenses expressed in cents per $100 of average total assets under management
- Operating expenses including external management fees expressed in cents per $100 of average total assets under management



1 Including external management fees that were previously deducted from investment income. The figures for 2005 and 2006 have been restated.

CDP FINANCIAL

CDP Financial, a wholly owned subsidiary of the Caisse, began its operations on June 9, 2003, with an initial offering of $3 billion of commercial paper.

Its main activity is to design borrowing programs for institutional financial markets in Canada and Europe so as to finance certain investment operations carried out by the Caisse. CDP Financial strives to borrow at the lowest cost to enable the portfolio managers to optimize their return on leveraged investment operations, namely those not financed by funds invested by depositors.

CDP Financial's liabilities, namely the amount of the notes outstanding, decreased by $2.3 billion in 2007, going from $5.6 billion to $3.3 billion. Outstanding short-term borrowings totalled $2.0 billion as at December 31, 2007, while term loans totalled $1.3 billion.

SHORT-TERM BORROWING

In 2007, to complement the Canadian commercial paper program, CDP Financial set up a short-term multicurrency borrowing program on the European market, from an office in London. The purpose of the new program is to ensure diverse sources of funds for the Caisse and to carry out offerings in several recognized currencies. Offerings totalling $0.3 billion were carried out under the new program in 2007.

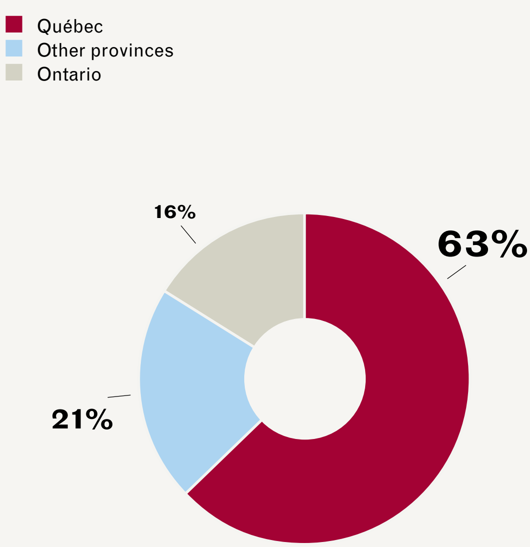
CDP FINANCIAL

Outstanding short-term borrowing amounted to $2.0 billion as at December 31, 2007, versus $4.1 billion at December 31, 2006. Annual transaction volume was $37.2 billion, with a turnover rate of 7.3 times the average amount outstanding and an average maturity of 48 days. As shown in figure 80, 63% of the offerings were purchased in Québec and 37% in Ontario and the other provinces.

FIGURE 80

GEOGRAPHIC BREAKDOWN OF COMMERCIAL PAPER SALES

(as at December 31, 2007)



MEDIUM-TERM BORROWING

CDP Financial did not issue any medium-term notes in 2007. Maturing notes totalling $0.2 billion were reimbursed, leaving $1.3 billion outstanding as at December 31, 2007.

LETTERS OF GUARANTEE

During the year, the subsidiary co-ordinated offerings of letters of guarantee, which provide interim support for certain investment operations. As at December 31, 2007, outstanding letters of guarantee amounted to $0.2 billion.

CREDIT RATINGS

Dominion Bond Rating Services (DBRS), Moody's Investors Services (Moody's) and Standard & Poor's (S&P) maintained their credit ratings for CDP Financial in 2007. These credit ratings are the highest issued by the rating agencies. Table 81 gives CDP Financial's credit ratings.

TABLE 81

CDP FINANCIAL'S CREDIT RATINGS

	Short-term	Long-term
DBRS	R-1 (high)	AAA
Moody's	Prime-1 (Aaa)	Aaa
S&P	A-1 +	AAA
	A-1 (high)	

FINANCIAL LEVERAGE

The Caisse's portfolio managers use borrowing, or financial leverage, to optimize the returns on their portfolios. This technique enables them to benefit from the difference between the return earned and the cost of borrowing. It is used especially for investments that receive regular cash flow, such as real estate and infrastructure.

COMBINED FINANCIAL STATEMENTS

COMBINED FINANCIAL STATEMENTS MANAGEMENT'S RESPONSIBILITY FOR COMBINED FINANCIAL REPORTING

Preparation and presentation of the combined financial statements of the Caisse de dépôt et placement du Québec (the "Caisse") are the responsibility of management. The combined financial statements were prepared in accordance with generally accepted accounting principles (GAAP) in Canada. We ensure that the financial data in the Annual Report are consistent with those in the combined financial statements.

The combined financial statements include amounts based on management's best estimates and judgment, with due regard for their relative importance. Moreover, in the preparation of the financial data, management has made decisions regarding the information to be presented, has made estimates and has made assumptions that affect the information presented. Future results may differ considerably from our current estimates, because of changes in the financial markets or other events that may have an impact on the fair value of the investments established as at December 31, 2007.

In our responsibility for the reliability of financial information, we use a sophisticated internal control mechanism applied systematically on all levels of the organization. This mechanism consists of organizational and operational controls, financial information disclosure controls and procedures, and internal control over financial information. The Caisse's internal control mechanism is based, among other things, on a clear definition of responsibilities, effective allocation of duties, delegation of powers, competent resources, appropriate procedures, information systems, tools and practices, relevant and reliable information whose adequacy enables all employees to fulfill their responsibilities, control, compliance and integrated risk management measures that are proportional to the issues specific to each process and designed to reduce risks likely to affect achievement of the Caisse's objects, and oversight of compliance with an extensive body of internal policies.

This control mechanism makes it possible to ensure that appropriate internal controls are in place as regards operations, assets and records. Moreover, the Caisse's internal audit group reviews the internal controls on a regular basis. These controls and audits are designed to provide reasonable assurance regarding the reliability of the accounting records used to prepare the combined financial statements and to ensure that assets are not used or disposed of in any unauthorized manner, that liabilities are recorded and that we meet all the legal requirements to which the Caisse is subject, including the *Act respecting the Caisse de dépôt et placement du Québec.*

Each year, we certify that the design of the internal control regarding financial information is sufficient and that the design and functioning of the financial information disclosure controls and procedures are effective. We report any significant irregularity to the Audit Committee of the Board of Directors of the Caisse, as necessary.

The Auditor General of Québec has audited the combined financial statements of the Caisse, and his report covers the nature and scope of the audit and expresses his opinion. The Auditor General has unrestricted access to the Audit Committee to discuss any matter relating to his audit.

The Board of Directors and its committees supervise the manner in which management fulfills its responsibility for the establishment and presentation of financial information, maintenance of appropriate internal controls, compliance with the requirements of laws and regulations, management of and control over the main risks and evaluation of major transactions. Moreover, it approves the combined financial statements and the Annual Report.

The Board of Directors has approved the combined financial statements as at December 31, 2007. It is assisted in its responsibilities by the Audit Committee, of which all members are outside directors. This Committee meets with management and the Auditor General, examines the combined financial statements and recommends their approval to the Board of Directors.

President and Chief Executive Officer
/ **Henri–Paul Rousseau**

Executive Vice-President, Finance and Operations
/ **Ghislain Parent**, FCA

Montréal, February 15, 2008

AUDITOR'S REPORT

To the National Assembly

I have audited the combined statement of net assets of the Funds of the Caisse de dépôt et placement du Québec as at December 31, 2007, along with the combined statement of income and changes in net assets for the year then ended. These financial statements are the responsibility of the Caisse's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with generally accepted auditing standards in Canada. These standards require that I plan and perform an audit in such a way as to obtain reasonable assurance that the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall presentation of the financial statements.

In my opinion, these combined financial statements present fairly, in all material respects, the financial position of these Funds as at December 31, 2007, as well as the results of their operations and the changes in their net assets for the year then ended, in accordance with generally accepted accounting principles in Canada. As required by the *Auditor General Act* (R.S.Q., chapter V-5.01), I report that in my opinion, with the exception of the changes in accounting principles presented in Note 3, these principles have been applied on a consistent basis with that of the preceding year.

Auditor General of Québec
/ **Renaud Lachance**, CA

Québec City, February 15, 2008

COMBINED STATEMENT OF NET ASSETS

(as at December 31, 2007)

(in millions of dollars)	2007	2006
Assets		
Investments at fair value *(notes 4a and b)*	**222,797**	203,491
Advances to depositors	**372**	1,024
Investment income, accrued and receivable	**1,209**	1,097
Transactions being settled	**1,567**	1,277
Other assets	**1,204**	625
	227,149	207,514
Liabilities		
Liabilities related to investments *(note 4c)*	**66,100**	60,644
Transactions being settled	**2,087**	514
Other liabilities	**1,561**	1,509
Non-controlling interests *(note 4d)*	**2,051**	1,368
	71,799	64,035
Depositors' holdings *(note 5)*	**155,350**	143,479

Derivative financial instruments *(note 9)*

Commitments and contingencies *(note 11)*

The accompanying notes are an integral part of the combined financial statements.

For the Board of Directors,

/ **Henri–Paul Rousseau**

/ **Claude Garcia**

COMBINED STATEMENT OF INCOME AND CHANGES IN NET ASSETS

(for the year ended December 31, 2007)

(in millions of dollars)	2007	2006
Investment income *(note 6a)*	**6,531**	5,522
Less:		
Operating expenses *(note 7)*	**261**	227
External management fees	**69**	54
Net investment income	**6,201**	5,241
Gains (losses) on the sale of investments *(note 6d)*	**9,427**	4,607
Total realized income	**15,628**	9,848
Unrealized increase (decrease) in the value of investments and liabilities related to investments *(note 6e)*	**(5,860)**	7,920
Unrealized decrease in the value of investments in third-party ABCP being restructured and other *(note 4b)*	**(1,897)**	–
Total unrealized increase (decrease) in value	**(7,757)**	7,920
Net investment results	**7,871**	17,768
Excess depositors' deposits over withdrawals	**4,000**	3,552
Increase in combined net assets	**11,871**	21,320
Combined net assets, beginning of year	**143,479**	122,159
Combined net assets, end of year	**155,350**	143,479

The accompanying notes are an integral part of the combined financial statements.

COMBINED FUNDS
NOTES TO FINANCIAL STATEMENTS

(as at December 31, 2007)

1.
CONSTITUTION AND OPERATIONS

The Caisse de dépôt et placement du Québec, a legal person established in the public interest within the meaning of the *Civil Code*, is governed by the *Act respecting the Caisse de dépôt et placement du Québec* (R.S.Q., chapter C-2). It receives funds, the deposit of which is provided under the Act. Pursuant to both the federal and provincial income tax acts, the Caisse is not subject to income taxes.

GENERAL FUND (consolidated statements)
The General Fund comprises all treasury operations (management of demand and term deposits, and corporate financing) as well as results from net investments related to third-party asset-backed commercial paper being restructured ("third-party ABCP being restructured") held in the specialized Bonds portfolio (760).

INDIVIDUAL FUNDS
The individual funds are comprised of diversified investments, and each fund has only one depositor that exclusively makes participation deposits therein. The individual funds are for the use of the following depositors:

Fund 300: Fonds du Régime de rentes du Québec administered by the Régie des rentes du Québec;

Fund 301: Government and Public Employees Retirement Plan administered by the Commission administrative des régimes de retraite et d'assurances;

Fund 302: Pension Plan for Management administered by the Commission administrative des régimes de retraite et d'assurances;

Fund 303: Individual plans administered by the Commission administrative des régimes de retraite et d'assurances;

Fund 305: Pension Plan for Elected Municipal Officers administered by the Commission administrative des régimes de retraite et d'assurances;

Fund 306: Régime complémentaire de rentes des techniciens ambulanciers œuvrant au Québec;

Fund 307: Fonds d'assurance automobile du Québec administered by the Société de l'assurance automobile du Québec;

Fund 311: Supplemental Pension Plan for employees of the Québec construction industry – general account – administered by the Commission de la construction du Québec;

Fund 312: Supplemental Pension Plan for employees of the Québec construction industry – retirees account – administered by the Commission de la construction du Québec;

Fund 313: Supplemental Pension Plan for employees of the Québec construction industry – supplementary account – administered by the Commission de la construction du Québec;

Fund 314: Fonds d'assurance-dépôts administered by the Autorité des marchés financiers;

Fund 315: Fonds d'assurance-prêts agricoles et forestiers administered by La Financière agricole du Québec;

Fund 316: Fonds d'amortissement du régime de retraite – RREGOP administered by the ministère des Finances, Government of Québec;

Fund 317: Fonds d'amortissement du régime de retraite – RRPE administered by the ministère des Finances, Government of Québec;

Fund 318: Fonds d'amortissement des autres régimes de retraite administered by the ministère des Finances, Government of Québec;

Fund 326: Fonds d'assurance-récolte administered by La Financière agricole du Québec;

Fund 327: Fédération des producteurs de bovins du Québec;

Fund 328: Régime de rentes de survivants administered by the Conseil du trésor, Government of Québec;

Fund 329: Fonds d'assurance-garantie administered by the Régie des marchés agricoles et alimentaires du Québec;

Fund 330: Fonds de la santé et de la sécurité du travail administered by the Commission de la santé et de la sécurité du travail;

Fund 332: Fonds des cautionnements des agents de voyages – cautionnements individuels administered by the Office de la protection du consommateur;

Fund 333: Fonds d'indemnisation des clients des agents de voyages administered by the Office de la protection du consommateur;

Fund 341: Fonds réservé administered by the Autorité des marchés financiers;

CONSTITUTION AND OPERATIONS (cont.)

Fund 342: Régime de retraite de l'Université du Québec administered by the Comité de retraite du Régime de retraite de l'Université du Québec;

Fund 343: Fonds d'assurance parentale administered by the Conseil de gestion de l'assurance parentale;

Fund 346: Fonds d'assurance parentale – Réserve administered by the Conseil de gestion de l'assurance parentale (closed November 1, 2007);

Fund 347: Régime de retraite du personnel des CPE et des garderies privées conventionnées du Québec administered by the Groupe-conseil Aon;

Fund 348: Régime complémentaire de retraite des employés syndiqués de la Commission de la construction du Québec administered by the Comité de retraite du Régime complémentaire de retraite des employés syndiqués de la CCQ;

Fund 351: Fonds des générations administered by the ministère des Finances, Government of Québec (created February 1, 2007);

Fund 353: Régime de retraite des membres de la Sûreté du Québec – caisse participants administered by the Commission administrative des régimes de retraite et d'assurances (created April 1, 2007);

Fund 361: Régime de rentes pour le personnel non enseignant de la Commission des écoles catholiques de Montréal administered by the Commission administrative des régimes de retraite et d'assurances (created January 1, 2007);

Fund 362: Régime de retraite pour certains employés de la Commission scolaire de la Capitale administered by the Commission administrative des régimes de retraite et d'assurances (created January 1, 2007);

Fund 363: Régime de retraite des employés de la Ville de Laval administered by the Comité du Régime de retraite des employés de la Ville de Laval (created July 1, 2007);

Fund 364: CCQ – Valeurs à court terme administered by the Commission de la construction du Québec (created July 1, 2007 and closed November 1, 2007)

SPECIALIZED PORTFOLIOS

The specialized portfolios are pooled funds for participation deposits of the various funds. The specialized portfolios are the following:

/ Short Term Investments (740)
/ Real Return Bonds (762)
/ Bonds (760)
/ Long Term Bonds (764)
/ Canadian Equity (720)
/ U.S. Equity – hedged (731)
/ U.S. Equity – unhedged (734)
/ Foreign Equity – hedged (730)
/ Foreign Equity – unhedged (733)
/ Emerging Markets Equity (732)
/ Québec International (761)
/ Investments and Infrastructures (781) (consolidated statements)
/ Private Equity (780) (consolidated statements)
/ Real Estate Debt (750) (consolidated statements)
/ Real Estate (710) (consolidated statements)
/ Commodity Financial Instruments (763)
/ Hedge Funds (770) (consolidated statements)
/ Asset Allocation (771)

2. ACCOUNTING POLICIES

The preparation of the combined financial statements of the Caisse in accordance with generally accepted accounting principles in Canada requires that management make estimates and assumptions, which have an impact on the accounting of assets and liabilities, the presentation of contingent assets and liabilities at the date of the financial statements and the accounting of revenues and expenses during the financial year covered by the financial statements. Actual results may differ from such estimates.

A statement of cash flows is not presented as it would provide no further useful information for the comprehension of cash flows during the year.

A / COMBINED FINANCIAL STATEMENTS

The combined financial statements comprise the accounts of the Caisse's subsidiaries, along with those of the General Fund, the individual funds and the specialized portfolios. The accounts of each fund and each portfolio are presented in financial statements audited by the Auditor General of Québec.

B / INVESTMENTS AND JOINT OPERATIONS

Investments and related assets and liabilities are accounted for at fair value, which is the estimated exchange value that would be agreed upon in an arm's-length transaction between competent, willing parties in conditions of full competition, established at year-end.

Transaction costs which are directly attributable to the acquisition and sale of investments are included in income and applied against gains and losses on the sale of investments. Transaction costs include commissions and stock exchange fees.

Fixed-income securities

Fixed-income securities comprise short-term investments, bonds, third-party ABCP being restructured and mortgages. Acquisitions and sales of fixed-income securities are recorded at the transaction date.

i / *Valuation method*

The fair value of fixed-income securities is determined by means of valuation methods used in capital markets, such as the annualization of future cash flows at the current interest rate and the prices of the major stock exchanges as well as those provided by recognized financial institutions. In addition, certain valuations are conducted by means of valuation methods commonly used, based on market data or on similar transactions on an arm's length basis. The valuation method used for third-party ABCP being restructured is presented in note 4b).

ii / *Investment income and gains and losses on the sale of investments*

Investment income from fixed-income securities includes amortization of the premium and the discount, which makes it possible to maintain a constant real return until maturity. Income from mortgages is reduced by operating expenses, financial costs of CMBS and write-off of deferred charges and is recorded under Investment Income – Fixed-income securities.

Gains and losses on the sale of investments represent the difference between the unamortized cost and the net realizable fair value on the sale of investments. The unamortized cost represents the acquisition cost adjusted to reflect the amortization of the premium or discount.

ACCOUNTING POLICIES (cont.)

Variable-income securities

Variable-income securities comprise equities and convertible securities as well as real estate holdings. Acquisitions and sales of equities and convertible securities are recorded at the transaction date, while acquisitions and sales of real estate are recorded at settlement date.

i | *Valuation method*

The fair value of equities traded on a stock exchange is determined based on prices on major stock exchanges as well as those provided by recognized financial institutions. For unlisted shares and real estate, certain valuations are made by independent valuators while others are made using commonly used valuation methods based on market data or similar transactions made on an arm's-length basis. The valuations of equities and convertible securities that are not publicly traded are reviewed biannually by an independent valuation committee while those of real estate are reviewed by independent valuators.

ii | *Investment income and gains and losses on the sale of investments*

Dividend income is recognized on the ex-dividend date. Income from real estate holdings is reduced by operating expenses related to real estate holdings, operation expenses and loan financial expenses, and is recorded under the item Investment income – Variable-income securities.

Gains and losses on the sale of investments represent the difference between the cost and the net realizable value on the sale of investments. The cost of investments is the acquisition cost, except for the acquisition cost of investments in joint ventures, which are accounted for using the equity method.

Derivative financial instruments

Pursuant to its investment management, the Caisse conducts transactions involving various derivative financial instruments to manage the risks associated with exchange rate, interest rate and market fluctuations.

Derivative financial instruments whose fair value is favourable are recorded under the item Investments, whereas those whose fair value is unfavourable are recorded under Liabilities related to investments.

i | *Valuation method*

Derivative financial instruments are recorded at their fair value at year-end. These values are established from prices on the major stock exchanges as well as those provided by recognized financial institutions. In the case of unlisted instruments, certain valuations are made on the basis of similar arm's-length transactions, or according to recognized, commonly used models, based on market data.

ii | *Investment income and gains and losses on the sale of investments*

Investment income from derivative financial instruments is included in income from fixed-income and variable-income securities, whereas gains and losses from derivative financial instruments are included in gains (losses) on the sale of investments on the basis of the underlying investments.

ACCOUNTING POLICIES (cont.)

Securities acquired under reverse repurchase agreements
The Caisse conducts security-borrowing operations involving short-term investments and bonds to cover short sales or to generate additional income from security-borrowing operations. These security-borrowing operations are recorded under Securities acquired under reverse repurchase agreements. Interest earned on reverse repurchase agreements is recorded as interest income under the item Investment income – Fixed-income securities.

Securities sold under repurchase agreements
The Caisse conducts security-lending operations involving short-term investments and bonds to generate cash flow liquidity or to generate additional income from security-lending operations. These security-lending operations are recorded under Securities sold under repurchase agreements. Interest paid on repurchase agreements is applied against Investment income – Fixed-income securities.

Short selling of securities
Short selling of securities represents the commitment by the Caisse to purchase securities from third parties to cover such positions. Interest related to commitments involving short selling of short-term investments and bonds are recorded under Investment income – Fixed-income securities, whereas costs related to commitments involving short selling of equities are recorded under Investment income – Variable-income securities.

Gains and losses on commitments related to short selling of short-term investments and bonds are recorded in Gains and losses on the sale of investments – Fixed-income securities, whereas those related to short selling of equities are recorded in Gains and losses on the sale investments – Variable-income securities.

C / ADMINISTERED PROPERTY AND PROPERTY UNDER MANAGEMENT

The Caisse and its subsidiaries administer and manage property entrusted to them by clients and on their behalf. This property is not included in the combined statement of net assets of the Caisse. The Caisse and its subsidiaries receive fees in return for such portfolio management services and administrative services, which include the administration of real estate properties and management of securitized loans.

D / FOREIGN CURRENCY TRANSLATION

The fair value of investments and any other assets and liabilities denominated in foreign currencies is translated into Canadian dollars at the rate of exchange prevailing at year-end.

The cost of investments in equities and that of real estate holdings from integrated foreign operations and the unamortized costs of investments in bonds, mortgages and short-term investments are translated at the rate of exchange prevailing on the acquisition date. The cost of investments from self-sustaining foreign operations is translated at the rate prevailing at year-end.

Income is translated at the rate of exchange prevailing on the transaction date, with the exception of income from the specialized real estate portfolio, which is translated at the average rate for the year.

ACCOUNTING POLICIES (cont.)

E / LOAN SECURITIZATION

The Caisse periodically securitizes loans and mortgages by selling such loans and mortgages to a collaterized security entity, which subsequently issues securities to investors. Such transactions are recorded as sales where the Caisse is deemed to have relinquished control over such assets and to have received compensation other than the beneficial rights attached to the assets disposed of, in accordance with Accounting Guideline AcG-12 "Transfers of receivables" in the Canadian Institute of Chartered Accountants ("CICA") Handbook. At time of securitization, no beneficial right attached to the securitized loans is retained. Any gains and losses deriving from such transactions are recorded under Gains (losses) on sale of investments – Mortgages and Bonds.

Companies under common control usually continue to manage loans after disposition. Since management fees are established on the basis of the market for such services, no assets or liabilities under management are recorded at the date of disposition.

F / OPERATING EXPENSES

Operating expenses represent all expenses related to portfolio management and administration, with the exception of those related to external management. Operating expenses are presented under a specific item in the "Combined statement of income and changes in net assets." Expenses related to the management of the specialized real estate and real estate debt portfolios are included in operating expenses. Operating expenses related to the management and administration of real estate holdings and mortgages are deducted from real estate holdings investment income and mortgages investment income respectively.

G / EXTERNAL MANAGEMENT FEES

External management fees represent amounts paid to external financial institutions, principally institutional fund managers active on international stock markets, for the management of Caisse funds on behalf of the Caisse. External management fees are presented under a specific item in the "Combined statement of income and changes in net assets."

3. CHANGES IN ACCOUNTING POLICIES

A / ADOPTION OF SECTION 3855, "FINANCIAL INSTRUMENTS – RECOGNITION AND MEASUREMENT"

i / *Description*

As of January 1, 2007, the Caisse adopted Section 3855 "Financial Instruments – Recognition and Measurement" in the CICA Handbook. As the Caisse qualifies as an investment company according to the Accounting Guideline No. 18 "Investment companies," the only provisions in Section 3855 applying to Caisse investments are those concerning the accounting, regular-way purchase or sale and measurement at fair value. The major change deriving from these new provisions involves determining the fair value of investments traded on active markets (equities and derivatives). The adoption of these new standards has had no significant impact on the combined financial statements.

This new standard also has an impact on the accounting of transaction costs related directly to the acquisition of investments. Previously such costs were capitalized in the cost of investments and must now be applied directly to income in the year such costs were incurred. Transaction costs include commissions and stock exchange fees. For the year ended December 31, 2007, transaction costs of $150 million were recorded in income under "Transaction costs of investments." As at December 31, 2006, such costs amounted to $120 million.

ii / *Opening balance adjustments*

The comparative combined financial statements were not adjusted. Certain opening balances in the depositors' holdings were adjusted, however, to reflect the transaction costs capitalized in the cost of investments as at Januray 1, 2007. These adjustments are as follows:

(in millions of dollars)	Balance as at January 1, 2007, before adjustments	Adjustments	Balance as at January 1, 2007, after adjustments
Caisse's indebtedness toward depositors	1,545		1,545
Participation deposit holders' holdings	115,947		115,947
Gains not allocated on the sale of investments	12,414	(120)	12,294
Unrealized increase (decrease) in value of investments and other related assets and liabilities	13,573	120	13,693
Depositors' holdings	**143,479**	**–**	**143,479**

B / ADOPTION OF SECTION 3861, "FINANCIAL INSTRUMENTS – DISCLOSURE AND PRESENTATION"

The CICA issued section 3861, "Financial Instruments – Disclosure and Presentation," which establishes standards for the presentation of financial instruments and non-financial derivatives, and specifies which information is to be given regarding such instruments. The application of these new standards has had no other significant impact than the addition of a new note: Note 8 – Identification and management of risks related to financial instruments.

CHANGES IN ACCOUNTING POLICIES (cont.)

C / CONSOLIDATION OF VARIABLE INTEREST ENTITIES

On January 1, 2007, the Caisse adopted the CICA changes to accounting guidelines AcG-15 "Consolidation of variable interest entities" and AcG-18 "Investment companies." According to these new dispositions an investment company that is the primary beneficiary of a variable-interest entity (VIE), which itself is an investment company, is no longer required to consolidate such VIE except in specific circumstances as specified in AcG-18.

This change was applied retroactively and the comparative financial statements were restated to reflect the impact of such new standards. The restatement has had no impact on the statement of income and changes in net assets or depositors' holdings as at December 31, 2006, but it has resulted in a change in the following items:

NET ASSETS

(in millions of dollars)	Decrease
Assets	
Investments at fair value	(328)
Investment income, accrued and receivable	(1)
Other assets	(15)
	(344)
Liabilities	
Liabilities related to investments	(213)
Other liabilities	(25)
Non-controlling interests	(106)
	(344)

D / SECTION 3862, "FINANCIAL INSTRUMENTS – DISCLOSURE," AND SECTION 3863, "FINANCIAL INSTRUMENTS – PRESENTATION"

The CICA issued Section 3862, "Financial Instruments – Disclosure," and Section 3863, "Financial Instruments – Presentation," which now replace Section 3861, "Financial Instruments – Disclosure and Presentation" and represent a revision and enhancement of the disclosure requirements of Section 3861. Presentation requirements are unchanged, however. As required by the transitional provisions, the Caisse will apply these sections as of the fiscal year ending December 31, 2008.

4.
INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS

A / INVESTMENTS

(in millions of dollars)	2007 Fair value	2007 Cost	2006 Fair value	2006 Cost
Fixed-income securities				
Short-term investments				
Canadian	**9,889**	**9,894**	28,945	28,947
Foreign	**4,865**	**4,898**	4,107	4,058
	14,754	**14,792**	33,052	33,005
Bonds				
Issued or guaranteed by:				
Canadian government	**23,586**	**22,966**	18,213	17,794
Province of Québec	**8,592**	**7,831**	9,309	8,388
Other Canadian provinces	**2,304**	**2,236**	4,002	3,907
Municipalities and other Canadian bodies	**1,728**	**1,724**	1,535	1,505
Canadian government corporations	**13,311**	**12,619**	10,681	9,932
U.S. government	**205**	**208**	1,180	1,148
Other foreign governments	**1,759**	**1,814**	950	916
Mortgage securities				
Canadian	**284**	**276**	342	323
Foreign	**2,022**	**2,601**	3,292	3,305
Canadian corporations	**15,947**	**16,260**	14,583	14,447
Foreign corporations	**4,695**	**5,315**	3,076	3,068
Inflation-indexed securities				
Canadian	**934**	**895**	1,054	978
Foreign	**3,381**	**3,664**	3,328	3,380
Hedge funds	**2,132**	**2,323**	2,428	2,327
	80,880	**80,732**	73,973	71,418
Third-party ABCP being restructured *(note 4b)*	**10,740**	**12,607**	–	–
Mortgages				
Canadian	**5,979**	**5,939**	4,877	4,779
Foreign	**4,481**	**4,574**	2,036	2,057
	10,460	**10,513**	6,913	6,836
Total fixed-income securities	**116,834**	**118,644**	113,938	111,259
Variable-income securities				
Equities and convertible securities				
Canadian	**17,179**	**14,943**	17,586	14,602
U.S.	**18,211**	**20,130**	15,897	15,569
Foreign and emerging markets	**26,822**	**24,278**	24,359	19,024
Hedge funds	**4,848**	**5,051**	4,477	4,267
	67,060	**64,402**	62,319	53,462
Real estate holdings[1]				
Canadian	**13,413**	**9,330**	11,181	8,156
Foreign	**9,027**	**8,397**	7,440	6,656
	22,440	**17,727**	18,621	14,812
Total variable-income securities	**89,500**	**82,129**	80,940	68,274
Amounts receivable with respect to investments				
Securities acquired under reverse repurchase agreements				
Canadian	**2,457**	**2,127**	1,332	1,332
Foreign	**4,986**	**5,110**	3,914	3,870
Amount pertaining to derivative instruments				
Canadian	**525**	**34**	423	17
Foreign	**8,495**	**1,997**	2,944	1,169
	16,463	**9,268**	8,613	6,388
Total investments	**222,797**	**210,041**	203,491	185,921

INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS (cont.)

A / INVESTMENTS (cont.)

[1] Investments – Real estate holdings includes investments in joint ventures now reported on an equity basis. These investments at fair value were as follows:

(in millions of dollars)	2007	2006
Investments in joint ventures	**8,401**	5,957
Real estate holdings	**14,356**	8,656
Short-term investments	**29**	6
Investment income, accrued and receivable	**6**	7
Other assets	**586**	236
	14,977	8,905
Loans and notes payable	**106**	–
Mortgage loans payable	**5,367**	2,448
Other liabilities	**1,053**	485
Non-controlling interests	**50**	15
	6,576	2,948

B / THIRD-PARTY ABCP BEING RESTRUCTURED

As at December 31, 2007, the Caisse holds investments in the Canadian market for commercial paper backed by assets that are not sponsored by banks and are being restructured (“third-party ABCP being restructured”). ABCP is a short-term financing instrument issued by trusts, also referred to as “conduits,” generally for maturities ranging from one to three months. The third-party ABCP being restructured is backed by various assets, such as mortgage debt or consumer and financial assets. The subprime mortgage crisis in the United States caused disruption on the international markets, which resulted in a liquidity crisis on the Canadian ABCP market in mid-August 2007. Since August 13, 2007, the Caisse has not been able to redeem, on maturity, the third-party ABCP that it holds. At the time of its acquisition by the Caisse, the third-party ABCP was rated “R-1 (High)” by the rating agency DBRS Limited (“DBRS”), namely the highest rating assigned by DBRS for asset-backed commercial paper.

Considerable progress has been made in order to restructure the third-party ABCP since August 13, 2007. On August 15, 2007, a group of investors and financial institutions, including the Caisse, proposed an agreement, the “Montréal Accord,” designed to re-establish the climate of trust and to identify an effective resolution strategy. Under this agreement, the investors and the financial institutions undertook not to place the conduits in default in order to avoid a forced sale of the underlying debt and financial assets (the “standstill”).

On September 6, 2007, a pan-Canadian committee, consisting of participants in the Montréal Accord, was formed to oversee the restructuring process. The Caisse is actively involved in the committee. On October 16, 2007, the committee chairman announced the successful restructuring of the first of the 22 conduits covered by the Montréal Accord, namely Skeena Capital Trust. On December 20, 2007, the Caisse received securities and cash totalling $754 million on completion of the restructuring of its $764.2 million of investments in Skeena Capital Trust.

On November 6, 2007, DBRS issued a public information document providing precise information on the composition of each conduit. DBRS confirmed that 97% of the underlying debt and financial assets was of “strong” quality and maintained its AAA rating and that 2% was rated AA or AA (low). DBRS has since changed the rating of one of the conduits to “R-4 (Under Review with Developing Implications).”

On December 23, 2007, the Pan-Canadian Investors Committee approved a proposed restructuring agreement, the “restructuring proposal,” for all the other trusts covered by the Montréal Accord, with the exception of Devonshire Trust. In all likelihood, definitive approval for the restructuring proposal will be given by the end of March 2008.

INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS (cont.)

On February 4, 2008, the Pan-Canadian Investors Committee reported on its new progress in implementing the restructuring proposal announced on December 23, 2007. The Committee expects that complete information on the restructuring and the approval process will be available at the end of February, and the objective is still to complete the restructuring by March 31, 2008. The standstill has been extended until February 22, 2008, and the extension also applies to Devonshire Trust, which was not part of the restructuring proposal announced in December 2007. The Committee has also reached an agreement in principle with several Canadian banks for their participation as lenders in a margin-call facility. Lastly, the Committee has selected BlackRock as the administrator and manager of the proposed restructuring vehicles. The restructuring has been approved in principle by the Pan-Canadian Investors Committee, certain merchant-bank asset suppliers and the promoters of each of the trusts.

The main objectives of the restructuring proposal announced on December 23, 2007, are to replace the third-party ABCP with new securities that have maturities similar to those of the underlying debt and financial assets, to pool certain series of third-party ABCP that are backed in whole or in part by synthetic assets, to mitigate the margin-call obligations of the existing conduits, to put in place margin facilities and to support the liquidity needs of holders of third-party ABCP as necessary. The restructuring proposal includes:

- A comprehensive and contemporaneous restructuring with separate solutions for:
  - Third-party ABCP backed by synthetic assets or a combination of synthetic and traditional securitized assets (“synthetic and hybrid assets”);
  - Third-party ABCP backed exclusively by traditional securitized assets (“traditional assets”);
  - Third-party ABCP backed by certain high-risk assets in the United States (“high-risk assets”);
- The restructuring of substantially all triggers so that they become more remote and transparent spread-loss triggers; and
- Investment-grade ratings for the restructured notes, which are expected by the investors committee and its advisers to be AAA for the synthetic assets and AAA and AA for the traditional assets.

As part of the restructuring, it is expected that the synthetic and hybrid assets will be divided into two restructuring vehicles, namely two limited partnerships that will issue variable-rate notes in exchange for existing third-party ABCP. Moreover, the parties have agreed that the participants in the two limited partnerships will put in place margin facilities in addition to those existing already. As a member of the first limited partnership, the Caisse would provide a margin facility of $5,267 million. The Caisse included in its valuation technique, described below, an estimate of the financial impact of a margin facility in respect of its third-party ABCP, in accordance with the restructuring proposal.

Given that there is no active market for the third-party ABCP being restructured, the Caisse established, in accordance with CICA guidelines, the fair values of its holdings of various types of third-party ABCP according to a valuation technique based on a financial model whose assumptions and probabilities reflect uncertainties related to the amounts and the maturities of the cash flow, the credit risk of the underlying debt and financial assets and the return. The assumptions, based on the information available as at December 31, 2007, use as much as possible observable market data, such as interest rates and credit quality. By establishing the fair values of the securities, the Caisse is attributing a strong probability of success to the restructuring proposal and a low probability to the scenario involving orderly or forced liquidation.

The Caisse estimated the fair value of each series of third-party ABCP being restructured by calculating the present value of the projected cash flows according to various default and loss scenarios, the real maturities of the securities as well as a relevant discount rate increased by a premium to reflect the current illiquidity of the third-party ABCP being restructured.

INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS (cont.)

The Caisse took into account the probability that the historic cumulative default rates, corresponding to the discount period, would be more severe in the next few years. The scenario corresponding to the success of the restructuring proposal takes into account an estimated default rate that makes it possible to establish an amount of "unproductive" assets with adverse impacts on the forecast cash flow. For the synthetic and hybrid assets, the estimated default rates apply to all the underlying assets. For the traditional assets and the synthetic assets that are excluded from the restructuring proposal, the Caisse applied a method similar to that used for the assets that are included, applying a multiplier to increase the level of the losses, given the uncertainty surrounding their restructuring. In the event that the restructuring proposal was not retained, the Caisse established scenarios based on an orderly liquidation or a forced liquidation of the synthetic and hybrid assets and the traditional assets. Moreover, the fair value of the high-risk assets has been reduced by 60%.

Given the foregoing, the Caisse recorded, against its portfolio of third-party ABCP being restructured, a total unrealized decrease in value of $1,897 million (including $30 million for restructuring costs) in its combined statement of income and changes in net assets for the year ended December 31, 2007. No interest receivable was recorded at year-end in respect of these securities.

As at December 31, 2007, the Caisse held third-party ABCP being restructured whose cost totalled $12,607 million ($10,740 million at fair value).

(in millions of dollars)	Fair value	Unrealized decrease in value	Cost
Synthetic and hybrid assets[1]	**9,231**	**1,295**	**10,526**
Traditional assets[2]	**1,196**	**103**	**1,299**
High-risk assets[3]	**313**	**469**	**782**
Restructuring costs	**–**	**30**	**–**
Total	**10,740**	**1,897**	**12,607**

1 Investments in the following trusts and series (the percentage indicates the proportion of the series attributable to synthetic and hybrid assets): Apollo series A (100%), Apsley series A (62.5%), Aria series A (89.4%) and E (100%), Aurora series A (100%), E (76.8%) and F (94.4%), Comet series A (100%), Devonshire (100%), Encore series A (100%) and E (100%), MMAI-I series A (100%), Opus series A (100%) and E (100%), Planet series A (55.5%), E (78.7%) and F (100%), Rocket series A (86.8%) and E (100%), SAT series A (100%) and E (100%), Silverstone series A (100%), SIT III series A (100%) and E (100%), Symphony series A (100%) and E (100%), Whitehall series A (100%), White Knight (100%).

2 Investments in the following trusts and series (the percentage indicates the proportion of the series attributable to traditional assets): Apollo series E (100%), Comet series E (87.1%) and F (100%), Gemini series A (100%), E (100%) and F (100%), Newshore series A (100%), Slate series A-1 (100%) and E-1 (100%).

3 Investments in the following trusts and series (the percentage indicates the proportion of the series attributable to high-risk assets): Apsley series A, (37.5%), Aria series A (10.6%), Aurora series E (23.2%) and F (5.6%), Comet series E (12.9%), Planet series A (44.5%) and E (21.3%), Rocket series A (13.2%), Ironstone series E (100%).

Management is of the opinion that the recorded estimate of the fair values is reasonable and is the most appropriate as at December 31, 2007. Nevertheless, the fair values are established as a function of the information available as at December 31, 2007, the Caisse's assessment of the state of the financial markets and a weighted approach using a set of assumptions and probabilities, including that of the success of the restructuring proposal. Accordingly, the fair values presented may vary significantly in subsequent periods. The most critical assumption regarding the valuation technique is based on the restructuring proposal's probability of success. Attributing greater weight to a liquidation scenario in the valuation technique would significantly increase the estimated unrealized decrease in value. Conversely, acceptance of the restructuring proposal and a return to normal market conditions would increase the estimated fair value. The Caisse believes it is unlikely that the proposal will fail, given its benefits for all stakeholders. The possible effect on the valuation technique of a 10% variation in the other assumptions and probabilities would not significantly change the estimate of the fair values as at December 31, 2007.

INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS (cont.)

C / LIABILITIES RELATED TO INVESTMENTS

(in millions of dollars)	2007		2006	
	Fair value	**Cost**	Fair value	Cost
Securities sold under repurchase agreements				
Canadian	**30,084**	**29,786**	26,944	26,951
Foreign	**6,554**	**6,647**	3,650	3,615
Commercial paper payable				
Canadian	**1,990**	**1,990**	4,111	4,112
Foreign	**46**	**48**	–	–
Medium-term notes	**917**	**916**	1,091	1,090
Loans payable				
Canadian	**345**	**346**	160	159
Foreign	**557**	**561**	361	359
Canadian commercial mortgage-backed securities				
Canadian	**302**	**291**	333	311
Foreign	**–**	**–**	847	843
Short selling of securities				
Canadian	**8,843**	**8,208**	13,392	12,245
Foreign	**7,716**	**7,498**	5,116	4,844
Mortgage loans payable				
Canadian	**277**	**269**	466	446
Foreign	**1,253**	**1,280**	954	958
Amount pertaining to derivative instruments				
Canadian	**291**	**20**	192	39
Foreign	**6,925**	**1,709**	3,027	856
	66,100	**59,569**	60,644	56,828

D / NON-CONTROLLING INTERESTS

(in millions of dollars)	2007		2006	
	Fair value	**Cost**	Fair value	Cost
Canadian	**1,408**	**1,135**	1,209	1,021
Foreign	**643**	**671**	159	166
	2,051	**1,806**	1,368	1,187

INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS (cont.)

E / SUMMARY CURRENCY BREAKDOWN - FAIR VALUE OF INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS

(in millions of dollars)							2007
	Currency[1]						
	Canadian dollar	U.S. dollar	Euro	GBP	Other	Subtotal	Total
Investments							
Fixed-income securities	93,244	15,937	2,622	2,028	3,003	23,590	116,834
Equities and convertible securities	17,186	25,040	8,240	6,215	10,379	49,874	67,060
Real estate holdings	13,413	3,176	4,544	1,132	175	9,027	22,440
Amounts receivable with respect to investments							
Securities acquired under reverse repurchase agreements	2,457	2,240	925	447	1,374	4,986	7,443
Amount pertaining to derivative instruments	525	7,457	644	193	201	8,495	9,020
	126,825	53,850	16,975	10,015	15,132	95,972	222,797
Liabilities related to investments							
Conventional debt	42,758	8,809	2,480	1,349	3,488	16,126	58,884
Amount pertaining to derivative instruments	291	5,996	638	105	186	6,925	7,216
	43,049	14,805	3,118	1,454	3,674	23,051	66,100
Non-controlling interests	1,408	107	63	473	–	643	2,051
Net investments	82,368	38,938	13,794	8,088	11,458	72,278	154,646

(in millions of dollars)							2006
	Currency[1]						
	Canadian dollar	U.S. dollar	Euro	GBP	Other	Subtotal	Total
Investments							
Fixed-income securities	93,466	15,084	1,485	1,989	1,914	20,472	113,938
Equities and convertible securities	17,598	22,281	7,141	6,341	8,958	44,721	62,319
Real estate holdings	11,181	2,452	3,666	1,218	104	7,440	18,621
Amounts receivable with respect to investments							
Securities acquired under reverse repurchase agreements	1,332	2,255	219	573	867	3,914	5,246
Amount pertaining to derivative instruments	423	2,174	459	168	143	2,944	3,367
	124,000	44,246	12,970	10,289	11,986	79,491	203,491
Liabilities related to investments							
Conventional debt	46,497	6,794	935	1,498	1,701	10,928	57,425
Amount pertaining to derivative instruments	192	2,282	498	164	83	3,027	3,219
	46,689	9,076	1,433	1,662	1,784	13,955	60,644
Non-controlling interests	1,209	124	35	–	–	159	1,368
Net investments	76,102	35,046	11,502	8,627	10,202	65,377	141,479

1 Investments are presented under the currency they are denominated in and are translated into Canadian dollars.

INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS (cont.)

F / SUMMARY OF MATURITIES OF INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS AT PAR VALUE

(in millions of dollars)					2007		2006
	Less than 2 years	2 to 5 years	More than 5 years	Total	Effective interest rate	Total par value	Effective interest rate
Fixed-income securities							
Short-term investments							
Canadian	9,881	32	–	9,913	4.8%	29,144	4.5%
Foreign	4,756	–	54	4,810	6.9%	4,115	6.8%
	14,637	32	54	14,723	5.5%	33,259	4.8%
Bonds							
Securities issued or guaranteed by:							
Canadian government	2,491	5,618	13,267	21,376	4.2%	16,361	4.1%
Province of Québec	306	1,674	5,108	7,088	4.9%	7,340	4.8%
Other Canadian provinces	5	65	2,103	2,173	4.7%	3,605	4.6%
Municipalities and other Canadian bodies	390	427	955	1,772	5.1%	1,493	5.2%
Canadian government corporations	2,169	6,264	3,422	11,855	4.6%	9,426	4.6%
U.S. government	–	2	196	198	4.3%	1,180	4.7%
Other foreign governments	144	–	1,576	1,720	2.9%	950	3.9%
Mortgage securities							
Canadian	5	89	213	307	12.2%	267	13.0%
Foreign	–	108	2,945	3,053	11.1%	5,412	11.3%
Canadian corporations	4,037	2,931	9,418	16,386	5.3%	14,295	5.0%
Foreign corporations	1,963	517	2,673	5,153	6.7%	3,067	6.3%
Inflation-indexed securities							
Canadian	–	–	630	630	2.1%	658	2.3%
Foreign	95	682	2,401	3,178	1.8%	3,151	1.9%
	11,605	18,377	44,907	74,889	4.9%	67,205	5.1%
Third-party ABCP being restructured	–	–	12,607	12,607	–	–	–
Mortgages							
Canadian	2,227	1,753	1,966	5,946	7.0%	4,779	6.8%
Foreign	3,616	838	120	4,574	7.8%	2,057	7.9%
	5,843	2,591	2,086	10,520	7.3%	6,836	7.2%
	32,085	21,000	59,654	112,739	5.3%	107,300	5.1%
Amounts receivable with respect to investments							
Securities acquired under reverse repurchase agreements							
Canadian	2,525	–	–	2,525	4.4%	1,332	4.2%
Foreign	4,603	–	–	4,603	3.0%	3,949	3.9%
	7,128	–	–	7,128	3.5%	5,281	4.0%
Liabilities related to investments							
Securities sold under repurchase agreements	36,573	–	–	36,573	4.1%	30,826	4.2%
Commercial paper payable	2,050	–	–	2,050	4.8%	4,143	4.3%
Medium-term notes	917	–	–	917	4.3%	1,092	4.2%
Loans payable	902	–	–	902	3.9%	521	4.4%
Canadian commercial mortgage-backed securities	8	301	–	309	6.9%	1,095	13.3%
Short selling of securities	1,088	831	6,759	8,678	3.5%	11,099	5.3%
Mortgage loans payable	483	495	571	1,549	6.8%	1,599	6.7%
	42,021	1,627	7,330	50,978	4.2%	50,375	4.7%

INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS (cont.)

The fair value of investments includes Canadian and foreign private companies' securities for which no market price is available. The fair value of such securities details as follows:

(in millions of dollars)	**2007**	2006
Canadian securities		
Short-term investments	**1,234**	1,303
Bonds	**1,244**	814
Third-party ABCP being restructured	**10,740**	–
Equities and convertible securities	**4,789**	4,154
	18,007	6,271
Foreign securities		
Short-term investments	**3,030**	2,248
Bonds	**769**	751
Equities and convertible securities	**16,593**	13,800
	20,392	16,799
	38,399	23,070

5.
DEPOSITORS' HOLDINGS

Demand and term deposits bear interest, and constitute indebtedness on the part of the Caisse toward the depositors.

During the year, the Caisse paid $4 million ($6 million in 2006) of interest on demand and term deposits.

Participation deposits are expressed in units, and each unit gives its holder a proportionate share in the net equity and the net income of a particular fund. At the end of each monthly period for the General Fund and the individual funds, the net investment income and the gains and losses on the sale of investments are distributed to participation deposit holders. At the beginning of the following period, the amounts distributed are paid out to (recovered from) the depositors' demand deposit accounts.

During the year, the Caisse paid $10,921 million ($8,724 million in 2006) in net income to participation deposit holders.

(in millions of dollars)	**2007**	2006
Caisse's indebtedness toward depositors		
Demand deposits	**143**	739
Term deposits	**66**	24
Interest on demand and term deposits	**1**	–
Net income to be paid out to participation deposit holders	**317**	782
	527	1,545
Participation deposit holders' holdings		
Participation deposits		
Balance, beginning of year	**115,947**	104,162
Units issued	**16,882**	12,119
Units cancelled	**(1,269)**	(334)
Balance, end of year	**131,560**	115,947
Gains not allocated on the sale of investments	**17,283**	12,414
Unrealized increase (decrease) in value of investments and other related assets and liabilities	**5,980**	13,573
	154,823	141,934
Depositors' holdings	**155,350**	143,479

6. INVESTMENT INCOME, GAINS (LOSSES) ON THE SALE OF INVESTMENTS, AND UNREALIZED INCREASE (DECREASE) IN VALUE OF INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS

A / INVESTMENT INCOME

(in millions of dollars)	**2007**	2006
Fixed-income securities		
Short-term investments	**685**	489
Bonds	**2,701**	2,589
Mortgages *(note 6b)*	**305**	206
	3,691	3,284
Variable-income securities		
Equities and convertible securities	**2,068**	1,544
Real estate holdings *(note 6c)*	**784**	713
	2,852	2,257
Other income	**61**	57
Non-controlling interests	**(73)**	(76)
	6,531	5,522

Investment income – Fixed-income securities were reduced by $1,221 million ($1,003 million in 2006) in net expenses related to securities sold (acquired) under repurchase (reverse repurchase) agreements.

B / NET INCOME FROM MORTGAGES

(in millions of dollars)	**2007**	2006
Income from mortgages	**424**	332
Less:		
Expenses related to real estate debt subsidiaries		
Operation expenses	**50**	36
Financial costs of CMBS	**69**	79
Write-off of deferred charges	**–**	11
	119	126
	305	206

C / NET INCOME FROM REAL ESTATE HOLDINGS

(in millions of dollars)	**2007**	2006
Income from real estate holdings	**2,482**	1,965
Less:		
Expenses related to real estate subsidiaries		
Operating expenses related to real estate holdings	**1,335**	952
Operation expenses	**99**	83
Loan financial expenses	**285**	238
	1,719	1,273
Other income	**21**	21
	784	713

INVESTMENT INCOME, GAINS (LOSSES) ON THE SALE OF INVESTMENTS, AND UNREALIZED INCREASE (DECREASE) IN VALUE OF INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS (cont.)

D / GAINS (LOSSES) ON THE SALE OF INVESTMENTS

(in millions of dollars)	2007	2006
Fixed-income securities		
Short-term investments	**49**	31
Bonds	**306**	(195)
Mortgages	**23**	(2)
	378	(166)
Variable-income securities		
Equities and convertible securities	**8,789**	4,837
Real estate holdings	**458**	(45)
	9,247	4,792
Non-controlling interests	**(48)**	(19)
	9,577	4,607
Transaction costs of investments	**150**	–
	9,427	4,607

In addition, gains in the amount of $9,427 million ($4,607 million in 2006) on the sale of investments recorded in changes in net assets were increased by foreign exchange gains of $1,826 million (decreased by foreign exchange losses of $3,383 million in 2006).

E / UNREALIZED INCREASE (DECREASE) IN VALUE OF INVESTMENTS AND LIABILITIES RELATED TO INVESTMENTS

(in millions of dollars)	2007	2006
Fixed-income securities		
Short-term investments	**217**	187
Bonds	**(1,291)**	328
Mortgages	**(124)**	(23)
Securities acquired under reverse repurchase agreements	**155**	80
	(1,043)	572
Variable-income securities		
Equities and convertible securities	**(3,144)**	7,482
Real estate holdings	**1,105**	2,218
	(2,039)	9,700
Total investments	**(3,082)**	10,272
Less:		
Liabilities related to investments		
Securities sold under repurchase agreements	**177**	72
Commercial paper payable	**(1)**	(1)
Medium-term notes	**–**	(8)
Loans payable	**(8)**	–
Commercial mortgage-backed securities	**(15)**	(3)
Short selling of securities	**(566)**	751
Mortgage loans payable	**(35)**	(18)
Derivative financial instruments	**3,162**	1,507
Non-controlling interests	**64**	52
	2,778	2,352
	(5,860)	7,920

7.
OPERATING EXPENSES

(in millions of dollars)	2007	2006
Salaries and employee benefits	**140**	116
Professional services	**45**	42
Data services and subscriptions	**15**	14
Premises and equipment	**17**	16
Depreciation of fixed assets	**15**	12
Other	**15**	16
	247	216
Safekeeping of securities	**14**	11
	261	227

8.
IDENTIFICATION AND MANAGEMENT OF RISKS RELATED TO FINANCIAL INSTRUMENTS

At the Caisse, risk management is based on an integrated risk management policy adopted by the Board of Directors. This policy, which is revised on a regular basis, is intended to promote a risk management culture and ensure appropriate risk management practices to help the Caisse better achieve its mission with depositors. More specifically, the risk management policy defines the governance and management of risk within the Caisse and establishes the level of risk that is acceptable in order to avoid excessive loss. In addition, this level of risk is related to the targeted value added to net assets, and promotes the efficient allocation of risk.

The governance of risk management is supported by three levels of control:

Level 1 / Portfolio managers who are primarily responsible for managing the risks related to their daily operations;

Level 2 / The Depositors and Risks Committee (DRC) and DRC-Transactions;

Level 3 / The Board of Directors and its Risk Management Committee.

The risk management policy includes reporting mechanisms for each of these levels. The policy also includes a framework for outsourcing management of investments, management of operational risks and management of derivative financial instruments.

To ensure the objectivity and rigour required to manage risks adequately, teams that are independent of portfolio managers are responsible for defining and monitoring the integrated risk management policy as well as the investment policies applying to the specialized portfolios.

IDENTIFICATION AND MANAGEMENT OF RISKS RELATED TO FINANCIAL INSTRUMENTS (cont.)

The policy also includes a procedure for the recommendation of investments for all investment groups. This process is organized based on responsibility levels as follows:

- The manager
- The investment committee of the investment group or the Board of Directors of a real estate subsidiary or unit
- DRC-Transactions
- The President and Chief Executive Officer
- The Board of Directors' Risk Management Committee
- The Board of Directors

The Caisse's integrated risk management policy focuses on the following major issues:

- Investment policies
- Market risk
- Absolute risk and active risk
- Credit and concentration risk
- Counterparty risk
- Financing liquidity risk

INVESTMENT POLICIES

The various investment policies define the limits for the specialized portfolios.

These policies specify the philosophy and management style, structure, investment universe, performance thresholds in terms of value added or absolute return, criteria applying to allocation and currency risk hedging. Finally, the policies establish the limits for concentration of investments by type of investment, issuer and currency.

MARKET RISK

Market risk represents the risk of financial loss deriving from changes in the value of financial instruments. The value of a financial instrument depends on the value of market risk variables such as interest rates, exchange rates, share prices and commodity prices as well as their volatility. The risk derives from the volatility in the price of a financial instrument, which itself results from the volatility of such market variables.

Market risk is measured according to the method known as the Value at Risk (VaR), based on the statistical measurement of the volatility of the market value of each position and its correlations.

The Caisse manages all market risks according to an integrated and comprehensive approach whereby major factors contributing to risk, such as industries, countries and issuers, are taken into account in analyzing market risk.

The Caisse can use derivative financial instruments traded either on exchanges or directly with banks and securities dealers, as part of the management of market risks deriving from its operations.

IDENTIFICATION AND MANAGEMENT OF RISKS RELATED TO FINANCIAL INSTRUMENTS (cont.)

ABSOLUTE RISK AND ACTIVE RISK

As at December 31, 2007, the absolute risk and active risk of the Caisse were 725 b.p. and 195 b.p. respectively. The absolute risk and the active risk are defined as follows:

> The absolute risk of the Caisse's benchmark portfolio (target portfolio of depositors as a whole) is the result of the risk (volatility) of the benchmark indexes of the asset classes included in the portfolio. For example, if the depositors decided to increase the weight of equities in their benchmark portfolios, such risk would automatically increase owing to the higher level of volatility of this asset class. Consequently, the expected absolute return would also increase. The absolute risk of the overall portfolio (comprised the actual investments) is the result of the risk (volatility) of the positions included in the Caisse's overall portfolio. The absolute risk of the overall portfolio and that of the benchmark portfolio are calculated according the same method, but they include different portfolios, such as the overall portfolio actually invested by the Caisse and the benchmark portfolio targeted by depositors.
>
> The active risk represents the possibility that the Caisse's active management of its overall portfolio may produce a return that is different from that posted by its benchmark portfolio. The higher the active risk, the more the expected absolute return on the overall portfolio will differ from the return on the benchmark portfolio.
>
> The absolute risk of the Caisse's benchmark portfolio, the absolute risk of the overall portfolio and the active risk are measured on a regular basis.

CREDIT AND CONCENTRATION RISK

Credit risk is the possibility of a loss of market value in the event that a borrower, endorser, guarantor or counterparty does not honour its obligation to repay a loan or to fulfill any other financial commitment, or sees its financial situation deteriorate.

The analysis of concentration risk measures the fair value of a group of financial products (fixed-income and variable-income securities) related to a single issuer or a group of issuers[1] with similar characteristics (geographic area, industry, credit rating). The concentration limit by group of issuers has been set at 3% of the Caisse's total assets, with the exception of securities issued by the Government of Canada, the Government of Québec or another Canadian province or territory, as well as by their departments and agencies, which are not subject to concentration limits.[2] Sovereign issuers with a credit rating of AAA are also excluded from this limit on concentration.

As at December 31, 2007, the concentration by credit rating of the Caisse's group of issuers was as follows:

Credit rating[3]	AAA-AA	A	BBB	BB or lower	No rating	Total
Total investments[4]	27.6%	13.3%	4.8%	4.0%	50.3%	100%

The analysis of credit risk includes measuring the probability of default and the rate of recovery on debt securities held by the Caisse, as well as monitoring the changes in the credit ratings of issuers and groups of issuers whose securities are held in the Caisse portfolios.

During 2007, a total of 204 groups of issuers held in the Caisse's specialized portfolios benefited from an improved long-term credit rating awarded by credit rating agencies, while 140 groups of issuers were awarded lower ratings.

COUNTERPARTY RISK

Counterparty risk represents the credit risk from current and potential exposure related to transactions involving over-the-counter derivative financial instruments.

Transactions involving derivative financial instruments are negotiated with financial institutions whose credit rating is established by a recognized credit rating agency and whose operational limits are specified by management. In addition, the Caisse signs agreements making it possible to benefit from the offsetting effect of amounts at risk and the exchange of collateral to limit its net exposure to this credit risk.

1 A group of issuers represents a number of issuers under the control of a parent company.
2 The exposure to an issuer deriving from positions in derivative financial instruments is not accounted for in the concentration risk analysis.
3 The various credit ratings are obtained from major public credit rating agencies and are aggregated according to an algorithm developed in house.
4 The percentage of investments represents net positions by group of issuers.

IDENTIFICATION AND MANAGEMENT OF RISKS RELATED TO FINANCIAL INSTRUMENTS (cont.)

Risk is measured by counterparty, according to the agreement in effect, on the basis of which it is possible to calculate the net exposure resulting from over-the-counter derivative financial instruments and collateral exchanged.

As at December 31, 2007, the Caisse's net exposure to counterparty risk totalled $1,037 million and involved 75 active counterparties.

FINANCING LIQUIDITY RISK

For a financial institution such as the Caisse, financing liquidity risk corresponds to the possibility that the Caisse may not always be able to fulfill its commitments without having to obtain funds at abnormally high prices or sell assets.

Compliance with established rules is monitored on a monthly basis, and the liquidity status is determined daily. The Caisse uses various scenario simulations to estimate the potential impact on cash. Cash managers evaluate the liquidity of markets on which the Caisse obtains financing for its operations. They also ensure the Caisse is active on various financial markets and maintains relationships with the credit rating agencies that rate the Caisse as well as capital providers.

9.
DERIVATIVE FINANCIAL INSTRUMENTS

Derivative financial instruments are financial contracts whose value fluctuates as a function of the underlying asset, and which do not require holding or delivering the underlying asset itself. This underlying value may be of a financial nature (interest rate, foreign currency, stock market security or index) or a commodity (precious metal, foodstuff or oil).

The notional amount of a derivative financial instrument represents the value of the notional principal to which a rate or a price applies to determine the exchange of future cash flows, and does not reflect the credit risk pertaining to the instrument.

The Caisse uses derivative financial instruments that include the following:

> Forward contracts and futures contracts are undertakings that enable the purchase or sale of an underlying value, the quantity and price of which are determined in the contract, which includes a predetermined delivery date. A forward contract involves customized conditions negotiated directly between the parties on the over-the-counter market. A futures contract has terms and conditions determined by an organized market.
>
> A swap is a transaction whereby two parties agree to exchange financial returns on predetermined conditions that include a notional amount and a term.
>
> An option is a contract negotiated by mutual agreement or traded on an organized market that gives the purchaser the right, but not the obligation, to buy or sell a given amount of an underlying security, index or commodity, at a strike price stipulated in advance, either at a determined date or at any time before a specified maturity date.

Foreign exchange risk arises from investments and liabilities related to investments denominated in foreign currencies, as well as from related derivative financial instruments. To manage exchange risk, the Caisse uses instruments negotiated with banks; maturities generally range from one to 12 months in the case of forward contracts and options, and from one to two years for foreign currency swaps. Upon maturity, new derivative financial instruments are negotiated to maintain effective long-term management of foreign exchange risks associated with investments and liabilities related to investments in foreign currencies.

Derivative instruments that are traded on exchanges or with banks and securities dealers are used to manage the interest rate and market risks of the total investment portfolio, as well as to generate income from transactions, which is included in investment income from fixed-income and variable-income securities.

IDENTIFICATION AND MANAGEMENT OF RISKS RELATED TO FINANCIAL INSTRUMENTS (cont.)

A / SUMMARY OF DERIVATIVE FINANCIAL INSTRUMENTS

(in millions of dollars)	2007				2006
		Fair value			
	Notional amount	**Assets**	**Liabilities**	**Net amount**	Net amount
Foreign exchange risk management					
Foreign currency swaps					
Purchases	**1,804**	**302**	**–**	**302**	–
Sales	**1,742**	**11**	**21**	**(10)**	(23)
Forward contracts	**45,758**	**916**	**233**	**683**	(600)
Over-the-counter foreign currency options					
Purchases	**171**	**5**	**–**	**5**	–
	49,475	**1,234**	**254**	**980**	(623)
Interest rate and market risk management					
Interest rate and foreign currency swaps	**225,677**	**1,564**	**1,681**	**(117)**	86
Equity swaps	**57,553**	**685**	**489**	**196**	116
Credit risk swaps	**20,124**	**221**	**203**	**18**	(26)
Futures contracts	**48,223**	**–**	**–**	**–**	–
Forward contracts	**69,736**	**3,030**	**2,940**	**90**	62
Exchange-traded options					
Purchases	**46,280**	**242**	**–**	**242**	241
Sales	**31,087**	**–**	**234**	**(234)**	(227)
Over-the-counter options					
Purchases	**66,286**	**1,892**	**–**	**1,892**	997
Sales	**60,896**	**–**	**1,414**	**(1,414)**	(648)
Warrants	**284**	**152**	**1**	**151**	170
	626,146	**7,786**	**6,962**	**824**	771
Total derivative financial instrument contracts	**675,621**	**9,020**	**7,216**	**1,804**	148

IDENTIFICATION AND MANAGEMENT OF RISKS RELATED TO FINANCIAL INSTRUMENTS (cont.)

B / SUMMARY OF DERIVATIVE FINANCIAL INSTRUMENT MATURITIES

(in millions of dollars)				2007	2006
	Notional amount - Maturity				
	Less than 2 years	2 to 5 years	More than 5 years	Total	Notional amount
Foreign exchange risk management					
Foreign currency swaps					
Purchases	8	1,796	–	1,804	–
Sales	763	155	824	1,742	2,249
Forward contracts	45,606	44	108	45,758	40,189
Over-the-counter foreign currency options					
Purchases	–	171	–	171	–
	46,377	2,166	932	49,475	42,438
Interest rate and market risk management					
Interest rate and foreign currency swaps	57,575	63,257	104,845	225,677	110,309
Equity swaps	47,872	2,601	7,080	57,553	57,110
Credit risk swaps	2,003	16,873	1,248	20,124	8,784
Futures contracts	30,930	14,781	2,512	48,223	59,862
Forward contracts	65,844	3,875	17	69,736	54,652
Exchange-traded options					
Purchases	46,048	232	–	46,280	159,382
Sales	30,873	214	–	31,087	136,765
Over-the-counter options					
Purchases	36,604	18,543	11,139	66,286	57,649
Sales	29,952	22,013	8,931	60,896	36,849
Warrants	160	114	10	284	290
	347,861	142,503	135,782	626,146	681,652
Total derivative financial instruments contracts	394,238	144,669	136,714	675,621	724,090

Notional amounts for 2006 have changed from the information reported in the combined financial statements as at December 31, 2006. This change applies mainly to futures contracts derivatives. The change affected notional amounts only and had no impact on the fair value of assets and liabilities related to such instruments. This change had no impact on the statement of income and changes in net assets as at December 31, 2006.

10.
SECURITIZATIONS

During the year, a wholly owned subsidiary of the Caisse securitized financial assets in the amount of $2,273 million (nil in 2006) through the issuance of commercial mortgage-backed securities. The wholly-owned subsidiary received a net income of $731 million as well as all non-offered classes included in the issue ("A-2" to "K") for a fair value of $1,542 million. Net losses of $26 million (nil in 2006) on the sale were reported in Gains (losses) on the sale of investments – Bonds. Expenses related to the transaction were assumed by the collateralized security entity.

In the course of Caisse securitization operations, commercial mortgage-backed securities and notes payable acquired by the Caisse over the last few years from a collateralized security entity are recorded in the combined statement of net assets under Mortgages securities. As at December 31, 2007, these securities amounted to $1,699 million ($294 million in 2006). Securitization operations have allowed companies under common control to generate management fees representing $4 million in 2007 ($2 million in 2006). No losses are expected owing to the nature and quality of such loans.

11.
COMMITMENTS AND CONTINGENCIES

Given the nature of its operations, the Caisse has a number of commitments.

Commitments to buy investments mean the Caisse is committed to buying investments that will be settled in the coming financial years, in accordance with the terms and conditions in each agreement.

For the Caisse, collaterals and loan guarantees consist in securing future income deriving from the sale of investments and transactions on derivatives as well as the reimbursement of loans made by investee companies to financial institutions and corporations. Collaterals related to the reimbursement of loans have no specific maturity date, except in some cases, where terms vary between one and 10 years.

(in millions of dollars)	**2007**	2006
Commitments to buy investments	**20,822**	20,741
Collaterals and loan guarantees (maximum amount)	**953**	567
	21,775	21,308

12.
COLLATERALS

In the normal course of business, the Caisse conducts transactions involving the lending and borrowing of securities in exchange for collaterals or assets, with various counterparties, with which clearing agreements have been signed to limit credit risk. In its securities lending operations, the Caisse received assets as collateral. As at December 31, 2007, the Caisse had pledged and received as collateral securities and other assets for amounts of $51,656 million ($39,460 million in 2006) and $11,330 million ($8,318 million in 2006), respectively. The amount of the assets pledged as collateral consists of assets with a value of $723 million ($764 million in 2006), which were pledged with depositaries to participate in clearing and payment systems.

13.
COMPARATIVE FIGURES

Certain figures from the 2006 financial statements have been reclassified to conform to the presentation adopted in 2007.

SUPPLEMENTARY INFORMATION

SUMMARY FINANCIAL STATEMENTS FOR THE SPECIALIZED PORTFOLIOS

(in millions of dollars)	SHORT TERM INVESTMENTS (740)		REAL RETURN BONDS (762)		BONDS (760)		LONG TERM BONDS (764)		CANADIAN EQUITY (720)	
CONSOLIDATED NET ASSETS AS AT DECEMBER 31	**2007**	2006	**2007**	2006	**2007**	2006	**2007**	2006	**2007**	2006
ASSETS										
Investments at fair value										
Bonds	–	–	871.0	1,053.9	73,297.8	52,994.3	3,174.7	3,001.8	–	–
Equities and convertible securities	–	–	–	–	–	–	–	–	12,949.3	12,369.1
Mortgages	–	–	–	–	–	–	–	–	–	–
Mortgage securities	–	–	–	–	–	–	–	–	–	–
Real estate holdings	–	–	–	–	–	–	–	–	–	–
Short-term investments	762.1	27,493.9	–	–	18,074.2	5,820.4	–	–	11,329.0	11,606.3
Securities acquired under reverse repurchase agreements	767.3	21,002.5	–	–	15,148.7	11,044.9	17.8	27.5	–	–
Third-party ABCP being restructured	–	–	–	–	10,739.4	–	–	–	–	–
Demand deposits in the General Fund	1,610.6	–	61.3	310.1	–	5,775.0	1,237.2	1,251.2	363.2	151.9
	3,140.0	48,496.4	932.3	1,364.0	117,260.1	75,634.6	4,429.7	4,280.5	24,641.5	24,127.3
Other assets	6.4	732.5	2.4	24.9	2,727.8	1,349.3	36.0	235.2	34.2	72.4
	3,146.4	49,228.9	934.7	1,388.9	119,987.9	76,983.9	4,465.7	4,515.7	24,675.7	24,199.7
LIABILITIES										
Advances from the General Fund	–	7,176.4	–	–	10,670.9	–	–	–	–	–
Securities sold under repurchase agreements	779.1	24,423.1	72.7	328.6	33,110.3	26,556.8	1,266.9	1,279.2	–	–
Short selling of securities	–	16.1	–	–	15,073.2	13,372.1	21.9	41.7	3,677.2	4,785.1
Loans and notes payable	–	14,787.7	–	–	19,323.6	–	–	–	–	25.6
Mortgage loans payable	–	–	–	–	–	–	–	–	–	–
Commercial mortgage-backed securities	–	–	–	–	–	–	–	–	–	–
Derivative financial instruments	1.9	8.2	–	–	1,776.5	659.3	–	–	216.4	48.3
Other liabilities	5.4	128.4	–	0.1	822.0	651.3	13.3	13.6	850.7	527.2
Non-controlling interests	–	–	–	–	–	–	–	–	–	–
	786.4	46,539.9	72.7	328.7	80,776.5	41,239.5	1,302.1	1,334.5	4,744.3	5,386.2
NET HOLDINGS OF FUNDS	2,360.0	2,689.0	862.0	1,060.2	39,211.4	35,744.4	3,163.6	3,181.2	19,931.4	18,813.5

STATEMENT OF CONSOLIDATED INCOME FOR THE YEAR ENDED DECEMBER 31										
INCOME										
Investment income										
Bonds	–	–	39.7	32.4	1,476.8	1,527.8	134.3	130.6	–	–
Equities and convertible securities	–	–	–	–	–	–	–	–	434.3	463.6
Mortgages	–	–	–	–	–	–	–	–	–	–
Mortgage securities	–	–	–	–	–	–	–	–	–	–
Short-term investments	440.6	392.7	–	–	640.1	178.9	–	–	520.6	388.4
Real estate holdings	–	–	–	–	–	–	–	–	–	–
Demand deposits in (advances from) the General Fund	158.9	197.2	(0.5)	–	(112.1)	(26.8)	3.9	2.6	(23.7)	(34.2)
	599.5	589.9	39.2	32.4	2,004.8	1,679.9	138.2	133.2	931.2	817.8
Other income	–	–	–	–	–	3.8	–	–	–	2.3
	599.5	589.9	39.2	32.4	2,004.8	1,683.7	138.2	133.2	931.2	820.1
Operating expenses	1.0	2.8	0.8	0.6	37.6	27.4	2.4	1.1	35.7	33.5
External management fees	–	–	–	–	–	0.1	–	–	–	0.4
INCOME BEFORE THE FOLLOWING ITEMS	598.5	587.1	38.4	31.8	1,967.2	1,656.2	135.8	132.1	895.5	786.2
Interest on notes payable	461.0	425.0	–	–	56.4	2.3	–	–	0.6	0.6
Non-controlling interest	–	–	–	–	–	0.1	–	–	–	–
NET INVESTMENT INCOME (LOSS)	137.5	162.1	38.4	31.8	1,910.8	1,653.8	135.8	132.1	894.9	785.6

CHANGES IN CONSOLIDATED NET ASSETS FOR THE YEAR ENDED DECEMBER 31										
NET INVESTMENT RESULTS										
Net investment income (loss)	137.5	162.1	38.4	31.8	1,910.8	1,653.8	135.8	132.1	894.9	785.6
Gains (losses) on sale of investments	(28.3)	(8.5)	11.3	21.5	394.8	430.2	(22.7)	(8.0)	2,056.4	2,671.1
Unrealized increase (decrease) in value of investments and liabilities related to investments	16.9	(1.7)	(39.8)	(91.4)	(938.0)	(645.1)	28.2	9.7	(539.6)	138.1
Net investment results	126.1	151.9	9.9	(38.1)	1,367.6	1,438.9	141.3	133.8	2,411.7	3,594.8
Participation units issued (cancelled)	(317.6)	(1,340.3)	(169.7)	(120.5)	4,010.2	(129.2)	(23.1)	1,249.1	(398.9)	(1,395.8)
Net investment loss (net income) recovered from (allocated to) participation unit holders	(137.5)	(162.1)	(38.4)	(31.8)	(1,910.8)	(1,653.9)	(135.8)	(132.1)	(894.9)	(786.0)
INCREASE (DECREASE) IN CONSOLIDATED NET ASSETS	(329.0)	(1,350.5)	(198.2)	(190.4)	3,467.0	(344.2)	(17.6)	1,250.8	1,117.9	1,413.0
CONSOLIDATED NET ASSETS, BEGINNING OF YEAR	2,689.0	4,039.5	1,060.2	1,250.6	35,744.4	36,088.6	3,181.2	1,930.4	18,813.5	17,400.5
CONSOLIDATED NET ASSETS, END OF YEAR	2,360.0	2,689.0	862.0	1,060.2	39,211.4	35,744.4	3,163.6	3,181.2	19,931.4	18,813.5

INVESTMENTS AND LIABILITIES AT COST AS AT DECEMBER 31										
ASSETS										
Investments										
Bonds	–	–	838.2	981.4	69,942.1	51,182.4	3,090.1	2,946.1	–	–
Equities and convertible securities	–	–	–	–	–	–	–	–	10,134.5	8,648.5
Mortgages	–	–	–	–	–	–	–	–	–	–
Mortgage securities	–	–	–	–	–	–	–	–	–	–
Real estate holdings	–	–	–	–	–	–	–	–	–	–
Short-term investments	759.3	27,499.0	–	–	17,798.9	5,722.7	–	–	11,319.2	11,599.7
Securities acquired under reverse repurchase agreements	773.2	20,984.4	–	–	15,078.1	11,029.8	18.0	27.5	–	–
Third-party ABCP being restructured	–	–	–	–	12,606.5	–	–	–	–	–
Demand deposits in the General Fund	1,610.6	–	61.3	310.1	–	5,775.0	1,237.2	1,251.2	363.2	151.9
	3,143.1	48,483.4	899.5	1,291.5	115,425.6	73,709.9	4,345.3	4,224.8	21,816.9	20,400.1
LIABILITIES										
Securities sold under repurchase agreements	790.7	24,405.2	72.7	328.7	33,063.3	26,545.4	1,267.1	1,279.5	–	–
Short selling of securities	–	16.1	–	–	15,084.3	13,372.2	22.0	42.1	3,079.9	3,631.2
Loans and notes payable	–	14,787.7	–	–	19,322.2	–	–	–	–	25.4
Mortgage loans payable	–	–	–	–	–	–	–	–	–	–
Commercial mortgage-backed securities	–	–	–	–	–	–	–	–	–	–
Derivative financial instruments	0.2	3.1	–	–	490.1	194.6	–	–	6.7	13.1
Non-controlling interests	–	–	–	–	–	–	–	–	–	–

U.S. EQUITY HEDGED (731) 2007	U.S. EQUITY HEDGED (731) 2006	U.S. EQUITY UNHEDGED (734) 2007	U.S. EQUITY UNHEDGED (734) 2006	FOREIGN EQUITY HEDGED (730) 2007	FOREIGN EQUITY HEDGED (730) 2006	FOREIGN EQUITY UNHEDGED (733) 2007	FOREIGN EQUITY UNHEDGED (733) 2006	EMERGING MARKETS EQUITY (732) 2007	EMERGING MARKETS EQUITY (732) 2006	QUÉBEC INTERNATIONAL (761) 2007	QUÉBEC INTERNATIONAL (761) 2006	INVESTMENTS AND INFRASTRUCTURES (781) 2007	INVESTMENTS AND INFRASTRUCTURES (781) 2006	PRIVATE EQUITY (780) 2007	PRIVATE EQUITY (780) 2006
–	–	–	–	–	–	–	–	–	–	**12,106.8**	10,756.4	**1,630.3**	960.5	**384.0**	605.6
7,131.5	7,603.7	–	–	**11,207.8**	10,065.1	–	–	**4,806.8**	4,187.5	**1,625.6**	1,302.5	**8,875.4**	9,732.3	**11,995.1**	8,362.7
–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
1,413.5	26.7	**4,245.2**	5,459.0	**17.5**	5.1	**6,549.8**	6,195.5	**172.5**	66.6	**3,658.1**	2,641.8	**3,910.8**	3,242.9	**358.1**	310.6
–	–	–	–	–	–	–	–	–	–	**477.5**	925.7	–	–	–	–
–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
1,403.0	–	–	64.1	**159.5**	–	–	26.6	**45.8**	–	**8,965.2**	5,002.1	–	–	–	–
9,948.0	7,630.4	**4,245.2**	5,523.1	**11,384.8**	10,070.2	**6,549.8**	6,222.1	**5,025.1**	4,254.1	**26,833.2**	20,628.5	**14,416.5**	13,935.7	**12,737.2**	9,278.9
44.4	565.5	**20.1**	7.9	**25.2**	162.7	**6.7**	4.6	**7.1**	56.6	**164.5**	152.8	**87.8**	57.9	**36.3**	27.8
9,992.4	8,195.9	**4,265.3**	5,531.0	**11,410.0**	10,232.9	**6,556.5**	6,226.7	**5,032.2**	4,310.7	**26,997.7**	20,781.3	**14,504.3**	13,993.6	**12,773.5**	9,306.7
–	159.1	**37.7**	–	–	731.1	**148.2**	–	–	8.8	–	–	**401.1**	856.8	**766.7**	912.8
–	–	–	–	–	–	–	–	–	–	**9,969.6**	6,249.7	–	–	–	–
2,490.3	695.6	–	–	**115.4**	82.4	–	–	–	–	**1,058.6**	854.1	–	40.6	**145.7**	81.4
4,481.8	5,422.6	–	–	**6,940.1**	6,149.9	–	–	–	–	**924.8**	–	**6,730.9**	3,853.7	**474.2**	89.2
–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
201.1	113.3	**24.9**	–	**108.4**	93.0	**112.6**	26.2	**6.6**	0.3	**13.8**	49.4	**36.1**	116.3	**40.0**	70.2
297.9	35.5	**14.9**	5.5	**634.1**	15.2	–	2.0	**23.4**	8.8	**475.0**	559.5	**31.2**	54.5	**14.9**	17.4
–	–	–	–	–	–	–	–	–	–	–	–	**896.2**	427.4	–	–
7,471.1	6,426.1	**77.5**	5.5	**7,798.0**	7,071.6	**260.8**	28.2	**30.0**	17.9	**12,441.8**	7,712.7	**8,095.5**	5,349.3	**1,441.5**	1,171.0
2,521.3	1,769.8	**4,187.8**	5,525.5	**3,612.0**	3,161.3	**6,295.7**	6,198.5	**5,002.2**	4,292.8	**14,555.9**	13,068.6	**6,408.8**	8,644.3	**11,332.0**	8,135.7
–	–	–	–	–	–	–	–	–	–	**476.7**	426.4	**88.7**	55.4	**38.9**	28.3
227.1	150.6	–	–	**712.9**	374.2	–	–	**87.2**	60.4	**16.9**	12.5	**298.6**	187.0	**218.0**	169.6
–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
29.7	0.6	**173.5**	105.5	**2.2**	0.2	**436.7**	227.2	**5.9**	2.1	**131.1**	101.2	**275.4**	111.9	**52.4**	34.4
–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
7.7	(8.2)	**0.2**	0.2	**(13.9)**	(24.5)	**0.6**	0.2	**2.0**	1.5	**22.6**	(25.0)	**(10.1)**	(19.4)	**(2.9)**	(3.1)
264.5	143.0	**173.7**	105.7	**701.2**	349.9	**437.3**	227.4	**95.1**	64.0	**647.3**	515.1	**652.6**	334.9	**306.4**	229.2
–	–	–	–	–	–	–	–	–	–	–	–	**27.6**	25.3	**23.0**	14.6
264.5	143.0	**173.7**	105.7	**701.2**	349.9	**437.3**	227.4	**95.1**	64.0	**647.3**	515.1	**680.2**	360.2	**329.4**	243.8
7.2	6.1	**18.2**	17.5	**8.9**	8.3	**16.3**	16.9	**12.3**	8.7	**11.9**	4.3	**34.3**	30.9	**26.8**	24.3
3.5	3.0	**9.5**	8.6	**6.7**	4.9	**12.3**	10.0	**15.4**	7.8	**3.5**	3.3	–	–	**7.6**	10.3
253.8	133.9	**146.0**	79.6	**685.6**	336.7	**408.7**	200.5	**67.4**	47.5	**631.9**	507.5	**645.9**	329.3	**295.0**	209.2
182.0	105.7	–	–	**467.8**	238.8	–	–	–	–	**41.1**	–	**354.2**	110.5	**4.6**	2.2
–	–	–	–	–	–	–	–	–	–	–	–	**25.9**	23.2	–	(0.1)
71.8	28.2	**146.0**	79.6	**217.8**	97.9	**408.7**	200.5	**67.4**	47.5	**590.8**	507.5	**265.8**	195.6	**290.4**	207.1
71.8	28.2	**146.0**	79.6	**217.8**	97.9	**408.7**	200.5	**67.4**	47.5	**590.8**	507.5	**265.8**	195.6	**290.4**	207.1
1,207.3	(545.6)	**(609.2)**	538.1	**1,133.3**	(692.1)	**(416.5)**	1,054.0	**601.9**	163.7	**105.1**	1,472.9	**1,673.8**	(265.8)	**1,338.8**	(61.6)
(1,347.0)	761.5	**(185.8)**	115.6	**(1,258.7)**	1,067.0	**(341.4)**	69.7	**32.8**	702.1	**(60.3)**	(95.4)	**(1,096.1)**	910.1	**(114.2)**	1,682.5
(67.9)	244.1	**(649.0)**	733.3	**92.4**	472.8	**(349.2)**	1,324.2	**702.1**	913.3	**635.6**	1,885.0	**843.5**	839.9	**1,515.0**	1,828.0
891.2	(117.5)	**(542.7)**	(319.3)	**576.1**	324.4	**855.1**	(723.9)	**74.7**	2,146.7	**1,442.5**	856.8	**(2,813.2)**	3,315.7	**1,971.7**	372.6
(71.8)	(29.2)	**(146.0)**	(82.4)	**(217.8)**	(99.7)	**(408.7)**	(204.2)	**(67.4)**	(47.7)	**(590.8)**	(508.0)	**(265.8)**	(195.6)	**(290.4)**	(210.1)
751.5	97.4	**(1,337.7)**	331.6	**450.7**	697.5	**97.2**	396.1	**709.4**	3,012.3	**1,487.3**	2,233.8	**(2,235.5)**	3,960.0	**3,196.3**	1,990.5
1,769.8	1,672.4	**5,525.5**	5,193.9	**3,161.3**	2,463.8	**6,198.5**	5,802.4	**4,292.8**	1,280.5	**13,068.6**	10,834.8	**8,644.3**	4,684.3	**8,135.7**	6,145.2
2,521.3	1,769.8	**4,187.8**	5,525.5	**3,612.0**	3,161.3	**6,295.7**	6,198.5	**5,002.2**	4,292.8	**14,555.9**	13,068.6	**6,408.8**	8,644.3	**11,332.0**	8,135.7
–	–	–	–	–	–	–	–	–	–	**11,952.0**	10,637.7	**1,687.4**	981.3	**556.9**	637.5
7,317.5	6,834.4	–	–	**10,677.3**	7,973.5	–	–	**3,768.6**	3,203.7	**1,645.2**	1,164.5	**8,449.6**	8,195.3	**13,883.0**	10,281.9
–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
1,447.0	25.4	**4,294.9**	5,347.8	**17.4**	5.1	**6,495.0**	5,885.7	**175.6**	65.7	**3,660.4**	2,641.8	**3,908.6**	3,217.8	**357.6**	295.4
–	–	–	–	–	–	–	–	–	–	**480.2**	908.1	–	–	–	–
–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
1,403.0	–	–	64.1	**159.5**	–	–	26.6	**45.8**	–	**8,965.2**	5,002.1	–	–	–	–
10,167.5	6,859.8	**4,294.9**	5,411.9	**10,854.2**	7,978.6	**6,495.0**	5,912.3	**3,990.0**	3,269.4	**26,703.0**	20,354.2	**14,045.6**	12,394.4	**14,797.5**	11,214.8
–	–	–	–	–	–	–	–	–	–	**9,972.8**	6,251.1	–	–	–	–
2,062.5	638.3	–	–	**119.1**	71.7	–	–	–	–	**1,092.3**	844.4	–	21.4	**83.4**	54.4
4,534.9	5,352.9	–	–	**6,995.2**	5,885.6	–	–	–	–	**946.8**	–	**6,698.0**	3,853.3	**508.8**	89.3
–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–
41.9	50.5	–	–	**0.1**	0.1	–	–	–	–	**3.6**	17.9	**4.2**	4.4	–	–
–	–	–	–	–	–	–	–	–	–	–	–	**939.8**	449.5	–	–

SUPPLEMENTARY INFORMATION

SUMMARY FINANCIAL STATEMENTS FOR THE SPECIALIZED PORTFOLIOS

(in millions of dollars)	REAL ESTATE DEBT (750)		REAL ESTATE (710)		COMMODITY FINANCIAL INSTRUMENTS (763)		HEDGE FUNDS (770)		ASSET ALLOCATION (771)	
CONSOLIDATED NET ASSETS AS AT DECEMBER 31	**2007**	2006	**2007**	2006	**2007**	2006	**2007**	2006	**2007**	2006
ASSETS										
Investments at fair value										
Bonds	**–**	–	**–**	32.0	**2,005.5**	1,983.4	**653.6**	1,656.3	**5,081.5**	2,784.5
Equities and convertible securities	**–**	–	**4,817.3**	4,445.9	**2,366.8**	939.6	**5,200.7**	4,698.1	**2,169.7**	866.4
Mortgages	**9,364.7**	6,700.4	**1,257.3**	375.9	**–**	–	**–**	–	**–**	–
Mortgage securities	**2,621.6**	3,579.1	**99.4**	125.1	**–**	–	**–**	–	**–**	–
Real estate holdings	**50.3**	1.1	**22,687.2**	18,697.9	**–**	–	**–**	–	**–**	–
Short-term investments	**15.5**	–	**306.6**	82.0	**501.1**	500.0	**183.0**	752.2	**603.1**	20.5
Securities acquired under reverse repurchase agreements	**–**	–	**–**	–	**–**	–	**523.1**	1,595.3	**2,471.0**	904.7
Third-party ABCP being restructured	**–**	–	**–**	–	**–**	–	**–**	–	**–**	–
Demand deposits in the General Fund	**2.3**	35.8	**–**	–	**–**	2.1	**130.6**	–	**–**	–
	12,054.4	10,316.4	**29,167.8**	23,758.8	**4,873.4**	3,425.1	**6,691.0**	8,701.9	**10,325.3**	4,576.1
Other assets	**117.4**	295.5	**830.6**	414.1	**195.6**	113.1	**66.3**	44.0	**303.5**	16.5
	12,171.8	10,611.9	**29,998.4**	24,172.9	**5,069.0**	3,538.2	**6,757.3**	8,745.9	**10,628.8**	4,592.6
LIABILITIES										
Advances from the General Fund	**–**	–	**930.4**	500.5	**298.8**	–	**–**	501.3	**447.9**	1,993.1
Securities sold under repurchase agreements	**–**	–	**–**	–	**–**	–	**567.9**	1,102.2	**2,827.7**	895.2
Short selling of securities	**–**	–	**122.0**	55.4	**–**	–	**650.9**	1,596.6	**2,963.0**	1,216.8
Loans and notes payable	**–**	–	**7,318.5**	5,695.5	**–**	–	**–**	64.2	**1,279.3**	–
Mortgage loans payable	**–**	–	**1,683.3**	1,582.3	**–**	–	**–**	–	**–**	–
Commercial mortgage-backed securities	**349.2**	1,236.0	**–**	–	**–**	–	**–**	–	**–**	–
Derivative financial instruments	**217.4**	220.4	**205.6**	390.4	**2,105.2**	893.1	**39.2**	699.4	**2,351.6**	85.1
Other liabilities	**136.7**	81.0	**1,121.6**	1,163.1	**141.5**	332.4	**9.8**	17.8	**45.1**	14.1
Non-controlling interests	**–**	–	**1,154.7**	939.9	**–**	–	**308.0**	542.9	**–**	–
	703.3	1,537.4	**12,536.1**	10,327.1	**2,545.5**	1,225.5	**1,575.8**	4,524.4	**9,914.6**	4,204.3
NET HOLDINGS OF FUNDS	**11,468.5**	9,074.5	**17,462.3**	13,845.8	**2,523.5**	2,312.7	**5,181.5**	4,221.5	**714.2**	388.3
STATEMENT OF CONSOLIDATED INCOME FOR THE YEAR ENDED DECEMBER 31										
INCOME										
Investment income										
Bonds	**–**	–	**2.4**	1.4	**(4.8)**	54.9	**2.9**	(0.4)	**8.9**	25.0
Equities and convertible securities	**–**	–	**74.6**	114.5	**0.4**	–	**(2.3)**	2.4	**0.3**	9.1
Mortgages	**757.1**	485.4	**51.8**	38.3	**–**	–	**–**	–	**–**	–
Mortgage securities	**–**	–	**8.9**	8.8	**–**	–	**–**	–	**–**	–
Short-term investments	**0.2**	–	**54.3**	31.0	**21.9**	20.2	**2.8**	2.7	**–**	8.4
Real estate holdings	**–**	–	**473.1**	500.2	**–**	–	**–**	–	**–**	–
Demand deposits in (advances from) the General Fund	**9.4**	7.6	**(24.7)**	(6.5)	**22.9**	(3.4)	**16.0**	(11.5)	**(57.0)**	(82.9)
	766.7	493.0	**640.4**	687.7	**40.4**	71.7	**19.4**	(6.8)	**(47.8)**	(40.4)
Other income	**9.6**	13.3	**–**	–	**–**	–	**–**	–	**–**	–
	776.3	506.3	**640.4**	687.7	**40.4**	71.7	**19.4**	(6.8)	**(47.8)**	(40.4)
Operating expenses	**8.4**	6.4	**9.4**	8.4	**5.9**	6.0	**18.3**	24.4	**14.7**	10.0
External management fees	**6.0**	5.7	**–**	–	**–**	–	**–**	–	**4.6**	–
INCOME BEFORE THE FOLLOWING ITEMS	**761.9**	494.2	**631.0**	679.3	**34.5**	65.7	**1.1**	(31.2)	**(67.1)**	(50.4)
Interest on notes payable	**–**	–	**–**	–	**–**	–	**0.6**	1.4	**53.2**	30.2
Non-controlling interest	**–**	3.3	**47.4**	49.9	**–**	–	**–**	–	**–**	–
NET INVESTMENT INCOME (LOSS)	**761.9**	490.9	**583.6**	629.4	**34.5**	65.7	**0.5**	(32.6)	**(120.3)**	(80.6)
CHANGES IN CONSOLIDATED NET ASSETS FOR THE YEAR ENDED DECEMBER 31										
NET INVESTMENT RESULTS										
Net investment income (loss)	**761.9**	490.9	**583.6**	629.4	**34.5**	65.7	**0.5**	(32.6)	**(120.3)**	(80.6)
Gains (losses) on sale of investments	**(197.0)**	(33.4)	**1,159.7**	420.9	**(231.4)**	15.2	**911.0**	(268.8)	**158.2**	198.2
Unrealized increase (decrease) in value of investments and liabilities related to investments	**(457.5)**	33.4	**1,158.4**	2,233.7	**153.6**	(0.4)	**(492.7)**	543.8	**(167.5)**	14.6
Net investment results	**107.4**	490.9	**2,901.7**	3,284.0	**(43.3)**	80.5	**418.8**	242.4	**(129.6)**	132.2
Participation units issued (cancelled)	**3,048.5**	2,759.7	**1,298.4**	527.8	**288.6**	736.7	**541.7**	37.2	**335.2**	13.8
Net investment loss (net income) recovered from (allocated to) participation unit holders	**(761.9)**	(490.9)	**(583.6)**	(629.4)	**(34.5)**	(65.7)	**(0.5)**	32.6	**120.3**	80.6
INCREASE (DECREASE) IN CONSOLIDATED NET ASSETS	**2,394.0**	2,759.7	**3,616.5**	3,182.4	**210.8**	751.5	**960.0**	312.2	**325.9**	226.6
CONSOLIDATED NET ASSETS, BEGINNING OF YEAR	**9,074.5**	6,314.8	**13,845.8**	10,663.4	**2,312.7**	1,561.2	**4,221.5**	3,909.3	**388.3**	161.7
CONSOLIDATED NET ASSETS, END OF YEAR	**11,468.5**	9,074.5	**17,462.3**	13,845.8	**2,523.5**	2,312.7	**5,181.5**	4,221.5	**714.2**	388.3
INVESTMENTS AND LIABILITIES AT COST AS AT DECEMBER 31										
ASSETS										
Investments										
Bonds	**–**	–	**–**	32.0	**2,005.5**	2,051.8	**670.4**	1,512.0	**5,184.4**	2,664.3
Equities and convertible securities	**–**	–	**3,437.1**	2,903.0	**725.3**	198.1	**5,426.5**	4,484.8	**703.5**	803.7
Mortgages	**9,386.4**	6,596.8	**1,272.2**	388.6	**–**	–	**–**	–	**–**	–
Mortgage securities	**2,774.1**	3,473.7	**102.7**	122.6	**–**	–	**–**	–	**–**	–
Real estate holdings	**68.3**	3.5	**17,498.6**	14,651.2	**–**	–	**–**	–	**–**	–
Short-term investments	**15.5**	–	**306.6**	82.0	**501.2**	500.0	**172.6**	683.3	**574.5**	–
Securities acquired under reverse repurchase agreements	**–**	–	**–**	–	**–**	–	**545.3**	1,578.1	**2,538.1**	896.5
Third-party ABCP being restructured	**–**	–	**–**	–	**–**	–	**–**	–	**–**	–
Demand deposits in the General Fund	**2.3**	35.8	**–**	–	**–**	2.1	**130.6**	–	**–**	–
	12,246.6	10,109.8	**22,617.2**	18,179.4	**3,232.0**	2,752.0	**6,945.4**	8,258.2	**9,000.5**	4,364.5
LIABILITIES										
Securities sold under repurchase agreements	**–**	–	**–**	–	**–**	–	**553.4**	1,088.8	**2,909.2**	889.8
Short selling of securities	**–**	–	**137.4**	52.1	**–**	–	**657.5**	1,573.6	**3,021.5**	1,100.8
Loans and notes payable	**–**	–	**7,345.7**	5,692.4	**–**	–	**–**	64.2	**1,269.7**	–
Mortgage loans payable	**–**	–	**1,694.9**	1,554.5	**–**	–	**–**	–	**–**	–
Commercial mortgage-backed securities	**339.0**	1,210.6	**–**	–	**–**	–	**–**	–	**–**	–
Derivative financial instruments	**26.0**	103.0	**27.3**	4.3	**547.5**	150.1	**5.2**	485.6	**738.4**	0.3
Non-controlling interests	**–**	–	**866.1**	737.7	**–**	–	**263.5**	500.4	**–**	–

TAKING THE LONG VIEW MEANS HAVING A SUSTAINABLE POSITIVE IMPACT HERE

/ **FRANÇOIS LIBOTTE**
Senior Director
Investments – Medium-sized Businesses
Private Equity

ECONOMIC DEVELOPMENT

Q

HOW DOES THE CAISSE CONTRIBUTE TO QUÉBEC'S ECONOMIC DEVELOPMENT ?

A

THE CAISSE FULFILLS THIS DUTY IN WAYS THAT INCLUDE:

1. CREATING COLLECTIVE WEALTH FOR QUEBECERS

The Caisse is a creator of wealth. It contributes to Québec's collective wealth and economic growth with the investment income it earns for its depositors. That is its main contribution to economic development.

2. INVESTING IN QUÉBEC'S ECONOMY

The Caisse is one of the largest investors in Québec. It plays a major role in business and government financing as well as in real estate. With its proximity to the Québec market, the Caisse is well placed to assess the investment opportunities it offers.

3. GENERATING SIGNIFICANT ECONOMIC BENEFITS WITH ITS OPERATIONS

The Caisse relies on the talent and dedication of its employees, encourages skills development, maintains relationships with a large number of suppliers of goods and services, and invests in the well-being of the community.

HIGHLIGHTS

- Since 2002, the Caisse has generated net investment results totalling $63.1 billion, earning $7.9 billion of that amount in 2007. Depositors' net assets have doubled, going from $77.7 billion to $155.4 billion.
- The Caisse is one of the largest investors in Québec, with $37.8 billion of total assets as at December 31, 2007.
- The Caisse's investments in Québec represent a substantial portion of its portfolio. As a result of its active management, it has invested $13.2 billion more in Québec than the amount established according to the indexes underlying the investment policies.
- The Private Equity group has invested in about 100 Québec companies, directly or through funds. Its venture capital strategy is generating significant results.
- The Fixed Income and Currencies group has substantially increased its holdings of corporate bonds, particularly those of financial institutions.
- The Real Estate group considerably increased its presence in the hotel market in 2007 with the acquisition of the Château Frontenac, in Québec City, and the Queen Elizabeth, in Montréal, in partnership with Westmont Hospitality Group.
- The operating expenses of the Caisse and its real estate subsidiaries in Québec total almost $600 million.
- More than 90% of the Caisse's employees took part in the Centraide/United Way campaign. Donations made by the employees of the Caisse and its real estate units, combined with the matching institutional donations, exceeded $1 million in 2007.

METHODOLOGY

To determine whether an asset is classified as a Québec investment, the Caisse uses the location of the head office of the company or the issuer of the security or, in the case of real estate, the geographic location of the property.

This classification, generally used in the fund management industry, involves certain biases. Some companies are included, although most of their operations are outside Québec. Similarly, companies with extensive operations in Québec are excluded if their head office is outside the province.

A KEY ROLE IN QUÉBEC'S ECONOMIC DEVELOPMENT

The Caisse's main contribution to Québec's economic development is by far the return it earns for its depositors. In this way, the Caisse contributes to the sustainability of the pension funds and insurance plans that form the majority of its depositors, and thus to Quebecers' collective wealth.

The Caisse obtains this return partially in Québec, its local market, where its experience and expertise are greatest.

The Caisse is very active in Québec's economy. It had $37.8 billion of assets in the province at year-end, including private equity, publicly traded equities, fixed income (including Québec's public sector) and real estate.

As a result of its active management, it has invested $13.2 billion more in Québec than the amount established according to the indexes underlying the investment policies. This favourable bias toward Québec investments is due primarily to two factors. First, its proximity to the Québec market gives the Caisse an undeniable advantage over its peers when it comes to evaluating the investment opportunities on this market. Second, the use of financial leverage enables it to invest a greater overall amount.

The Caisse's assets in Québec companies increased by 9.8% a year from 2002 to 2006, whereas Québec's economic growth averaged 4%. These assets totalled $23.4 billion as at December 31, 2007, up 12.5% from the previous year.

The total assets invested in Québec companies by the Caisse since 2002 have continued to increase substantially but have decreased in proportion to its net assets for the simple reason that its size doubled during that period.

1. THE CAISSE, A CREATOR OF WEALTH

In co-operation with its depositors, the Caisse contributes to Quebecers' collective wealth by earning investment income for the pension and insurance plans they belong to.

The Caisse plays a foremost role by offering its depositors varied investment options that include real estate and private equity, by ensuring they adopt effective investment policies with a sound risk-return profile and by delivering excellent returns over the medium and long terms.

Investment income is redeployed to generate additional income for the depositors and to enhance the ability to invest in Québec.

The returns obtained by the Caisse therefore affect Québec's economic development, since they have an impact on the financial strength of the pension and insurance plans that form the majority of the depositors.

Over the long term, an increase in the Caisse's return not only facilitates matching of the depositors' resources and financial obligations, but also gives them some leeway in their decisions about the level of contributions and benefits.

Since 2002, the Caisse has generated $63.1 billion of net investment results, earning $7.9 billion of that amount in 2007. Depositors' net assets have doubled, rising from $77.7 billion to $155.4 billion.

With a 5.6% return in 2007, the Caisse ranks in the first decile of its industry. Even better, it is in the first five centiles of the pension funds that have performed best over the past five years. If the Caisse had obtained only a third-quartile performance during that period, today its depositors would have $20 billion less of net assets.

Québec, especially the Caisse's Québec depositors, are reaping the benefits of this performance. The strong results recorded by the Caisse over the past five years have enabled it not only to earn the target returns specified in the depositors' investment policies, but also to exceed them and in this way contribute doubly to the plans' sustainability.

To be able to generate such income for its Québec depositors, the Caisse invests in the international arena but is also one of the largest investors in Québec.

2. THE CAISSE, ONE OF THE LARGEST INVESTORS IN QUÉBEC

The Caisse invests a portion of its depositors' total assets in Québec. With $37.8 billion of total assets as at December 31, 2007, the Caisse is one of the largest investors in the province. It invests mainly in private equity ($6.0 billion), publicly traded equities ($2.4 billion), fixed income ($22.4 billion) and real estate ($6.9 billion).

TABLE 82

THE CAISSE'S TOTAL ASSETS IN QUÉBEC

(as at December 31, 2007 – in billions of dollars)

Private Equity	6.0
Equity Markets	2.4
Fixed Income and Currencies	22.4
Real estate	6.9
Total	**37.8**

PRIVATE EQUITY

The Private Equity group invests in proximity markets and offers companies various financing options, to increase the capital available to sectors where it is insufficient and to identify investment opportunities with partners. It also monitors the global markets for Québec companies.

The group's assets in Québec totalled $6.0 billion as at December 31, 2007, with $200 million in venture capital, $65 million in small businesses, $247 million in medium-sized businesses and $5,522 million in large businesses. The Caisse also had $1.3 billion of undisbursed commitments, namely amounts to be paid out on conditions negotiated with partners. Assets and commitments therefore totalled $7.3 billion.

TABLE 83

THE PRIVATE EQUITY GROUP'S ASSETS AND COMMITMENTS IN QUÉBEC

(as at December 31, 2007 – in millions of dollars)

	Assets	Undisbursed commitments	Assets and commitments
Venture capital	200	538	738
Small business	65	68	133
Medium-sized business	247	108	355
Large business	5,522	551	6,073
Total	**6,034**	**1,265**	**7,299**

The assets comprise $971 million of corporate debt, $3,719 million of equity in privately held companies and $1,344 million of equity in publicly traded companies.

2. THE CAISSE, ONE OF THE LARGEST INVESTORS IN QUÉBEC

VENTURE CAPITAL

Instead of investing directly in technology companies and competing with other investment firms, the Caisse invests in partnership through local and foreign venture capital funds that are active in Québec. In recent years, the Caisse has set the objective of contributing to the development of Québec's venture capital industry by restructuring it according to a new approach. It has therefore adopted a four-fold strategy based on partnership. The Caisse has undertaken to:

- Invest in Québec funds that are well positioned in venture capital;
- Coinvest with funds to finance growth projects;
- Invest in funds that specialize in startups; and
- Attract foreign venture capital.

The purpose of this approach is to create more diverse sources of capital, to generate a leverage effect and to increase the amounts available to Québec companies. In this way, the Caisse and Québec entrepreneurs can benefit from the expertise of dynamic fund managers, while helping build a stronger and more competitive venture capital industry for the province.

Moreover, the Caisse organizes networking days for investment funds and local experts and entrepreneurs. It introduces companies seeking financing or information to investors. It also helps organize specialized seminars to disseminate the industry's best practices.

As a result of this new strategy, at year-end the Caisse was a partner of eight Québec venture capital funds and four funds that are from outside Québec but have an establishment in the province (table 84). These funds had $1.2 billion as at December 31, 2007, of which $242 million was committed by the Caisse. As a result of partnering with external capital, the Caisse's contribution has five times more impact than a direct investment would. This financing, usually in the form of equity, is available at each stage of the development of technology companies.

In addition, the Caisse has encouraged two major U.S. funds to set up shop in Montréal: ProQuest Investments and Vantage Point Venture Partners.

In only a few years the Caisse's strategy has generated significant results:

- From 2003 to 2006, Québec received more than half (55%) of the venture capital disbursements made in Canada;
- As a proportion of total funds raised, the contributions by private funds have increased 10-fold since 2003;
- The growth of foreign capital invested in Québec is two and a half times faster than the rate for the rest of Canada.

The Caisse's assets in the venture capital segment totalled $200 million as at December 31, 2007, and were invested in 46 Québec companies. Most of the investments are due to the new strategy of partnering with the private sector and were made in the past 18 months. The GoCapital and iNovia Capital funds specialize in startups, a niche for which no fund had been created since 2001. The Caisse authorized a $15-million investment in iNovia II in 2007.

The Caisse's commitments to the venture capital segment, including amounts committed with partners but not disbursed, totalled $738 million at year-end.

TABLE 84

MAIN NICHES OF PARTNER FUNDS BY COMPANY DEVELOPMENT STAGE

<table>
<tr><th>Partner funds under the new strategy</th><th>Startup</th><th>Growth</th><th>Sustainability and ownership transfer</th></tr>
<tr><td>iNovia Capital</td><td>Generalist</td><td></td><td></td></tr>
<tr><td>GoCapital</td><td>Generalist</td><td></td><td></td></tr>
<tr><td>ID Capital</td><td>Generalist</td><td></td><td></td></tr>
<tr><td>Garage Technology Ventures Canada</td><td>Generalist</td><td></td><td></td></tr>
<tr><td>Brightspark Ventures</td><td>Information technology</td><td></td><td></td></tr>
<tr><td>CTI Life Sciences</td><td colspan="2">Life sciences</td><td></td></tr>
<tr><td>AgeChem</td><td colspan="2">Life sciences</td><td></td></tr>
<tr><td>Rho Canada Ventures</td><td colspan="2">Information technology</td><td></td></tr>
<tr><td>Emerald Technology Ventures</td><td colspan="2">Generalist</td><td></td></tr>
<tr><td>Propulsion Ventures</td><td colspan="2">Information technology</td><td></td></tr>
<tr><td>JLA Ventures</td><td colspan="3">Information technology</td></tr>
<tr><td>Novacap</td><td></td><td colspan="2">Information technology</td></tr>
</table>

SMALL BUSINESS

Providing financing to small businesses involves many small transactions on a market that is well served by tax-advantaged funds, regional and local funds, banks and the Desjardins Group. Large amounts of capital are available. In this context, rather than operating its own network in competition with the other players, the Caisse has opted for a strategic partnership.

The Caisse invests in small businesses mainly through the AlterInvest Fund, which is financed equally by the Caisse and the Business Development Bank of Canada (BDC) and managed by a BDC team with subordinated-loan expertise. The products are available throughout Québec at about 30 branches.

The investments generally take the form of an unsecured loan, which is similar to an equity stake, but without the constraints that an investment in share capital involves (shareholders' agreement, board of directors, etc.). This tool is therefore very flexible and well suited to the financing needs of Québec's small businesses. The loans range from $250,000 to $2 million.

From 2003 to 2006, the AlterInvest Fund invested an average of $1 million in almost 300 Canadian companies. In December 2006, the Caisse announced it would renew its partnership with BDC and create a new $330-million fund to provide financing for Canadian SMEs over the next three years.

The assets of the AlterInvest Fund totalled $131 million in Québec as at December 31, 2007, with half ($65 million) financed by the Caisse. During the fund's latest fiscal year, 45 Québec companies borrowed $55 million.

The Caisse's commitments to the small business segment, including amounts committed with partners but not disbursed, totalled $133 million at year-end.

2. THE CAISSE, ONE OF THE LARGEST INVESTORS IN QUÉBEC

MEDIUM-SIZED BUSINESS

Québec's medium-sized businesses operate in an extremely demanding environment. To ensure their prosperity and sustainability, they must adapt their business models, stay ahead of producers in emerging markets and step up their research and development. Québec companies also have to sell their products in the international arena, penetrate new markets, insert themselves into global supply chains and take advantage of the strong Canadian dollar to purchase foreign equipment.

In this context, the Caisse has set up a team that specializes in Québec's medium-sized companies, offering financing and other assistance tailored to their needs. It strives to partner with strong management teams focused on the sustainability and growth of their businesses with niche products and a realistic growth plan.

When investing directly, the Caisse provides financial and operational assistance to medium-sized companies looking for $2 million to $25 million of financing. It also enables Québec's mid-sized businesses to take advantage of the network of corporate directors and contacts as well as the expertise and synergy it has developed over the years.

The Caisse also invests through funds, including the Québec Manufacturing Fund (Industrial Capital) and Novacap. The first fund aims to improve the operating efficiency and productivity of Québec manufacturers. Novacap is a growth and leveraged-buyout fund that invests in companies that are leaders in their markets. Novacap helps them accelerate their operations significantly by focusing on internal growth, acquisitions and strategic alliances.

With many business leaders planning to retire in the years to come, the Caisse has developed a financial product called Accès Relève to assist them in planning and carrying out ownership transfers. In this way, the Caisse contributes to the sustainability of Québec's companies.

The Caisse added an operational component in 2007 with the startup of the Québec Manufacturing Fund and the appointment of an experienced business executive to lead its team.

The Caisse's assets in the medium-sized business segment totalled $247 million, invested in 45 companies, as at December 31, 2007. The Manufacturing Fund authorized its first two investments during the year: $12 million in Triton Electronik Inc., a Montréal-based electronic contract design and manufacturing service provider; and more than $8 million in Fraco Products Ltd., a company that manufactures vertical-elevation work platforms used mainly in the construction industry.

The Caisse's commitments to the medium-sized business segment, including amounts committed with partners but not disbursed, totalled $355 million at year-end.

LARGE BUSINESS

Québec's large businesses can usually obtain financing on the Canadian and international markets on flexible, advantageous conditions. But when the market conditions become uncertain, investment risks and interest rates increase, and capital becomes scarce and costly.

In the development capital market, the Caisse is one of the few large financial institutions that meet the needs of Québec's large businesses by offering long-term capital.

Moreover, because of its size, when investment opportunities arise, the Caisse can undertake large, complex transactions, and form partnerships with other investors.

The Caisse makes investments of $25 million or more in large businesses.

The first half of 2007, until the start of the liquidity crisis in August, featured an exuberant mood and an abundance of capital. In the second half, however, capital dried up as a result of the global crisis. Access to capital became more difficult, constraining and costly. Since then, Québec businesses have submitted many projects to the Caisse. This is expected to be the case again in 2008.

The Caisse's assets in the large-business segment totalled $5.5 billion as at December 31, 2007, and were invested in 54 companies. The Caisse has substantial stakes in companies that include Bombardier Recreational Products (J.A. Bombardier Inc.), the Montréal Exchange, Cascades, Camoplast, Cirque du Soleil, Alimentation Couche-Tard, Domtar, Garda World, Industrial Alliance, Quebecor Media, SSQ Vie and Noverco (Gaz Métro).

The Caisse authorized investments totalling $735 million in 2007. For example, it approved an increase in the credit facilities of Atrium Innovations to finance acquisition projects. It also invested in Garda World, a Québec company that doubled in size to become a global security leader.

The Caisse's commitments to the large business segment, including amounts committed with partners but not disbursed, totalled $6.1 billion at year-end.

EQUITY MARKETS

When selecting investments, the managers in the Equity Markets group usually focus on the intrinsic value of businesses and their development outlook over the medium and long terms. It is in the interests of the Caisse and its depositors that priority be placed on those companies that have the best development outlook and the best performance, in terms of the calibre of their senior management, board of directors and managers, as well as their operations. The Caisse also acts in a more opportunistic manner by selling shares when they are expensive and buying when they are undervalued.

The Caisse generally strives to align its interests with those of the businesses over the long term. By investing in this way, it obtains a better understanding of Québec's companies and builds trust-based relationships with them. These relationships, which are extremely important for the businesses, permit balanced share ownership that is conducive to genuinely strategic choices and mitigate the constraints created by the need to generate short-term returns. Moreover, as a long-term shareholder, the Caisse can more effectively assess the impact of takeover attempts on such companies.

The Caisse has one of the largest portfolios of Québec equities. In addition to the stakes in publicly traded companies held by the Private Equity group ($1.3 billion), the Equity Markets group held $2.4 billion of shares in 51 companies as at December 31, 2007, including substantial stakes in Alimentation Couche-Tard, BCE, Canadian National Railway, Cogeco Cable, CGI Group, SNC-Lavalin Group, Gildan Activewear, METRO, Power Corporation of Canada, Quebecor, RONA and Saputo.

2.
THE CAISSE, ONE OF THE LARGEST INVESTORS IN QUÉBEC

FIXED INCOME AND CURRENCIES

The financing needs of the public sector have decreased in recent years, mainly because of lower government deficits. Moreover, as a result of market efficiency, borrowers can obtain financing at a relatively low cost. Although the Caisse has reduced the relative size of the government securities in its portfolio, it continues to be one of the main holders of bonds issued by Québec's public sector.

The Fixed Income and Currencies group holds mainly securities issued by the Québec government, Hydro-Québec, municipalities, educational institutions and health care institutions. It also invests in corporate bonds, co-ordinates the Caisse's liquid assets and provides financing to the Caisse's other groups.

The Fixed Income and Currencies group had $22.4 billion of assets in Québec as at December 31, 2007, including $14.4 billion in public-sector securities and $8.1 billion in corporate bonds.

TABLE 85

THE FIXED INCOME AND CURRENCIES GROUP'S ASSETS IN QUÉBEC

(as at December 31, 2007 – in billions of dollars)

Québec public sector:	
Québec government	8.6
Hydro-Québec	4.3
Municipalities and paragovernmental corporations	1.5
Subtotal	**14.4**
Corporate securities	**8.1**
Total	**22.4**

The group substantially increased its holdings of corporate bonds in 2007, especially those of financial corporations. Québec public-sector assets decreased slightly.

At year-end, the Caisse held securities in companies that include YPG Holdings (Yellow Pages Income Fund), BCE, National Bank of Canada and Caisse Centrale Desjardins.

REAL ESTATE

The Caisse carries out merchant banking and property management operations for Québec's real estate sector. It specializes in building ownership, development and management.

Through its Cadim division and its subsidiaries SITQ and Ivanhoe Cambridge, the Caisse makes equity and debt investments in Québec's office building, business park, retail, hotel and multiresidential sectors.

In selecting a real estate investment, the Caisse generally looks for an outstanding property with a dominant market position. It also seeks a strategic location, a high degree of stability and the ability to withstand fluctuations in the economic cycle. Moreover, the Caisse's initiatives are always based on a desire to enhance the immediate environment, to respect heritage considerations and to ensure energy efficiency. Its managers' work has received numerous awards.

In becoming one of the 10 largest managers of real estate assets in the world, the Caisse has developed unique expertise in Québec, as have its partners and suppliers of services. Its real estate financing know-how is an additional asset for the local financial community. Moreover, the Caisse enables Québec to take advantage of its international partner network, which has attracted considerable foreign investment to the province.

Québec's real estate market was quite active in 2007. Assets sold fairly quickly amid intense competition. Buildings fetched rather high prices on an efficient sellers' market. Even at year-end, the liquidity crisis and its impact on financing costs did not bring prices down. The year saw very few new construction projects that require financing.

The Caisse's equity and debt real estate assets in Québec totalled $6.9 billion at year-end. Commitments, including $513 million committed but not disbursed as at December 31, 2007, totalled $7.4 billion. The Caisse therefore has the largest real estate portfolio in the province.

TABLE 86

THE REAL ESTATE GROUP'S ASSETS AND COMMITMENTS IN QUÉBEC

(as at December 31, 2007 – in millions of dollars)

	Assets	Undisbursed commitments	Assets and commitments
Office buildings	2,736	147	2,883
Retail properties	2,911	118	3,029
Hotels	460	77	537
Other	801	171	972
Total	**6,908**	**513**	**7,421**

The Caisse authorized $1.2 billion of investments in 2007 through its real estate units, primarily for acquisitions, development projects, fixed assets and loans.

OFFICE BUILDINGS

The Caisse's equity and debt real estate investments in more than 150 office buildings totalled $2.7 billion as at December 31, 2007. The most important are in downtown Montréal, including Place Ville Marie, the Centre CDP Capital, 1000 de la Gauchetière, the Montréal World Trade Centre, the Tour de la Bourse, 1200, 1981 and 2001 McGill College, the Centre du Multimédia de Montréal and the Sun Life Building. In Québec City, it owns Place Hauteville, the Édifice Mérici and the Édifice Price.

During the year, 12 real estate debt investments totalling $248 million were authorized.

RETAIL PROPERTIES

The Caisse's equity and debt real estate assets in the retail sector totalled $2.9 billion and included almost 250 retail properties. The most important are in Montréal: the Eaton Centre, Rockland Centre, Fairview Pointe Claire, Les Galeries d'Anjou and Place Montréal-Trust. Other assets include Centropolis in Laval, the Mail Champlain on Montréal's South Shore, Les Rivières shopping centre in Trois-Rivières, Place du Royaume in Saguenay and Place Ste-Foy and Place Laurier in Québec City.

Ivanhoe Cambridge was very active on the Québec market in 2007 with projects that included:

- A $28-million project to enlarge Centropolis in Laval;
- Acquisition of the 37.5% stake that it did not already hold in La Place Vertu and the launch of a $38-million redevelopment project to reposition the mall in its market. In all, $43 million has been invested in the acquisition and the redevelopment project;
- Continuation of the project, begun in 2005, to redevelop Rockland Centre, with completion scheduled for 2008. Investments totalled $5 million in 2007 and will reach $45 million on completion;
- Investment of $35 million during the year in other Québec shopping centres.

During the year, 19 real estate debt investments were authorized, for a total of $193 million.

HOTELS

With the acquisition by its Cadim division of a large stake in Legacy Hotels Real Estate Investment Trust in 2007, the Caisse has considerably increased its presence in the hotel market. Legacy owns Québec hotels synonymous with luxury and comfort, including two jewels associated with the history of the province: the Château Frontenac, in Québec City, and the Queen Elizabeth, in Montréal.

The Caisse's assets in the hotel sector totalled $460 million as at December 31, 2007.

OTHER ASSETS

The Real Estate group's assets in the industrial and multiresidential sectors, as well as its other assets, totalled almost $801 million as at December 31, 2007. This amount includes almost $100 million of equity in the funds managed by Maestro, a company in which Cadim has a 55% interest. Maestro's assets in Québec totalled $563 million at year-end and were concentrated in the seniors-residence sector.

Moreover, the Real Estate group assisted Québec companies with their business development outside the province. With four Québec interest groups, it approved loans totalling $247 million for investments outside Québec. For example, these efforts will enable Groupe Germain to build a hotel in Calgary.

3. THE CAISSE GENERATES SUBSTANTIAL ECONOMIC BENEFITS

The operations of the Caisse and its real estate units generate substantial economic benefits for Québec. Their stature in the international arena benefits Québec as a whole. They pay salaries and maintain relationships with a large number of suppliers of goods and services. They foster skills development in many ways. Lastly, they take part in many other activities that contribute to Québec's economic development.

THE OPERATING EXPENSES OF THE CAISSE AND ITS REAL ESTATE UNITS TOTAL $600 MILLION

The Caisse and its real estate units carry out their mission as a result of the efforts and talent of 1,650 employees in Québec.

TABLE 87

NUMBER OF EMPLOYEES OF THE CAISSE AND ITS REAL ESTATE UNITS

(as at December 31, 2007)

Caisse	Real estate units[1]	Total
763	887	**1,650**

1 The real estate units include Cadim, SITQ and Ivanhoe Cambridge.

The Caisse and its real estate units maintain business relations with many Québec suppliers of goods and services. The operating expenses of the Caisse and its real estate units, in Québec, totalled $405 million in 2007, including $231 million of real estate operating expenses, $30 million of rents and more than $40 million of information technology and professional services contracts.

These operating expenses enable several hundred other employees to work in technical services, security, asset management, maintenance and other services related to real estate.

The Caisse also enables its suppliers to maintain and develop specialized expertise and contributes to their expansion in Québec. In 2007, it paid $3.4 million of commissions on equity and derivatives transactions to 14 brokers doing business in Québec. The Caisse also paid $9.9 million of portfolio management fees to seven companies doing business in Québec.

DEVELOPMENT OF COMPETENCIES

The Caisse places the utmost importance on the expertise and training of it teams. As at December 31, 2007, 82% of its employees (including Cadim) have a university degree, and 40% have a master's degree or a doctorate. In addition, 130 employees have the chartered financial analyst (CFA) designation, 37 others are in the process of obtaining it and 90 employees have an accounting designation (CA, CGA and CMA).

During the year, the Caisse offered training and development activities to all employees who wanted to acquire new skills and to enhance their expertise. These activities covered various subjects, including team management, finance, work organization and communication. They were offered to 1,487 participants, for a total of 6,831 training hours.

In addition, the Caisse fosters an exchange of knowledge, particularly on the economy and finance:

- It publishes research papers, and organizes and contributes financially to various seminars and conferences;
- It assists university students by supporting many fellowship programs, several university chairs and various educational activities at Québec universities; and
- It encourages excellence in business and financial reporting with fellowships, as well as the Caisse de dépôt et placement du Québec/Merrill Lynch Economic and Financial Journalism Awards of Excellence.

It is also an active partner in the Collège des administrateurs de sociétés, of which it became a founding member in 2005. The purpose of the college is to develop governance rules and to improve knowledge and application of them at Québec companies by offering high-calibre training to corporate directors.

The training provided by the college has increased considerably. No fewer than 90 instructors, from foremost professional firms, transmit the knowledge and experience they have acquired as corporate directors. More than 250 directors are involved in the various training programs, and 128 directors have a certified corporate director (CCD) university degree. Five professional orders have partnered with the college to provide continuing education to their members. The college also sets up projects on governance in financial services.

Lastly, the Caisse is one of the founding members of the Group of Montréal, an international group of pension and reserve funds that encourages information sharing on the industry's best practices. The Caisse organized the group's first two meetings, held in Montréal, and co-ordinated visits by managers from various countries. In the same spirit, the Caisse welcomed nine foreign delegations for discussions on its areas of expertise and practices.

OTHER CONTRIBUTIONS TO THE WELL-BEING OF THE COMMUNITY

CORPORATE RESPONSIBILITY

The Caisse endorses the principle of accountability to all parties concerned regarding its corporate responsibilities. It believes that a fund manager and investor of its size must pay the utmost attention to the vital issues of governance and the social and environmental aspects of investment. In this spirit, the Caisse published a brochure on corporate responsibility along with its 2007 financial results.

Under its policy on socially responsible investment, the Caisse exercises its voting rights on the basis of general and specific principles (see "Management framework").

CENTRE INTERNATIONAL SUR LA PROSPÉRITÉ DES ENTREPRISES DU QUÉBEC

The Caisse demonstrated leadership in 2007 with the creation of the Centre international sur la prospérité des entreprises du Québec (CIPEQ), whose mission is to provide close, active support to officers of Québec's medium-sized businesses that want to accelerate their growth by taking advantage of global markets.

CIPEQ's activities will be concentrated in five main areas of expertise specific to development of international operations: strategies for entering new markets; procurement strategies; mergers, acquisitions and alliances; organization and business models; and talent and human resources. In this way, the Caisse:

- Strives to help management teams gain a better understanding of the challenges they must rise to;
- Fosters discussion and networking between managers from different regions, cultures and industries; and
- Helps advance various business models adapted to the complexity of today's world.

QUARTIER INTERNATIONAL DE MONTRÉAL

Since the Quartier international de Montréal (QIM) was created in 1999, the Caisse has supported the activities of this non-profit organization dedicated to creating a prestigious, world-class district in Montréal. The project and the organization have already received numerous awards and distinctions, in particular for the redevelopment of McGill Street. The organization is now working on the creation of an entertainment district known as the Quartier des spectacles.

During the year, the Caisse again organized seven lunchtime concerts at Place Jean-Paul-Riopelle and Square Victoria. The concerts are held in co-operation with property owners in the district. They reflect the Caisse's commitment to its immediate environment.

MONTRÉAL EXCHANGE

During the year, the Caisse also considered the project to merge the Montréal Exchange with the Toronto Stock Exchange. It deemed the proposal attractive, but expressed a desire for a public hearing to examine such matters as the financial and strategic aspects of the transaction, as well as the applicable governance rules. The Caisse subsequently endorsed the project, while urging the Autorité des marchés financiers to obtain certain commitments from the new TMX Group. It also supports the efforts of the Montréal Exchange to develop the Montréal Climate Exchange.

OTHER INITIATIVES

The Caisse supports various other educational, cultural and philanthropic initiatives.

For example, the Caisse encourages social involvement on the part of its employees. The most significant manifestation of this commitment is undoubtedly their participation in the Centraide/United Way fund-raising campaign. In 2006, this support was recognized with the highest distinction given to donors: the *Solidaires* award. The donations made by the employees of the Caisse and its real estate units, combined with the matching institutional donations, exceeded $1 million in 2007. More than 90% of the Caisse's employees took part in the campaign.

TAKING THE LONG VIEW MEANS MANAGING WITH FORESIGHT

/ **JOANNE ALDERSEBAES**
Senior Director
Financial Governance and Special Projects
Finance and Operations

MANAGEMENT FRAMEWORK

Q

WHAT IS THE CAISSE'S MANAGEMENT FRAMEWORK ?

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THE MANAGEMENT FRAMEWORK IS THE SYSTEM USED BY THE CAISSE TO DEFINE ITS MAJOR MANAGEMENT ACTIVITIES AND THEIR COMPONENTS

Institutions that are successful over the long term operate in an orderly fashion with a view to the medium and long terms. Their management activities are well defined, complementary, non-repetitive and understood by employees. They are conducive to identification of the institution's priorities and achievement of its objectives.

A well-structured management framework ensures that essential management activities and their components are in place and that they are revised periodically as a function of best practices. It also clarifies the roles and responsibilities of each member of the organization. The management framework is dynamic and changes constantly as new needs and requirements arise.

The Caisse's management framework consists of all policies, directives and procedures used for planning, execution, control, evaluation, reporting and disclosure. The management framework also affirms the importance of optimizing operations, whether to fulfill the Caisse's mission or to ensure optimal use of the resources placed at its disposal by depositors.

The management framework covers all the Caisse's operations and applies to both the investment groups and the general services units. Implementing it is a collective endeavour that requires the involvement of all officers and employees, according to their roles and responsibilities. Above all, it ensures that the various teams maintain effective communication to ensure integrated management of the Caisse's various components.

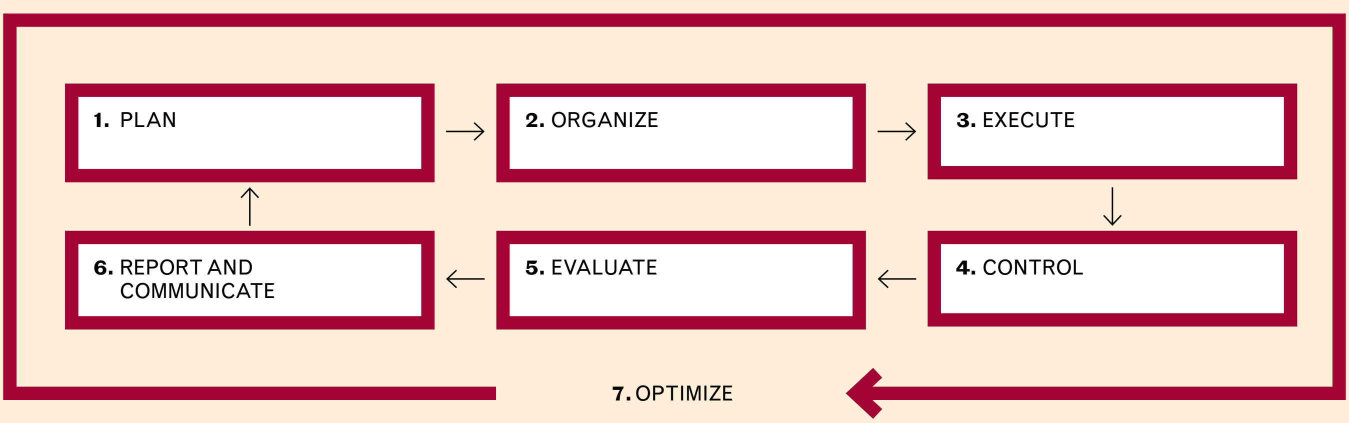
HIGHLIGHTS

The Caisse continued to strengthen its management and control structures in 2007.

- The delegations of authority were reviewed.
- Twice-yearly reporting on the self-assessment of optimal resource use was introduced by the Audit Committee of the Board.
- The policy on the exercise of voting rights for publicly traded companies was revised and brought up to date.
- The investment policies of several portfolios were revised.
- New directives were issued for the execution of transactions to specify the roles and responsibilities of the various business units and to set operational limits.
- A number of directives and practices affecting human resources and organizational development were introduced, revised or amended.
- A process was introduced to oversee internal transactions, including transactions by specialized portfolios, transactions between specialized portfolios and financial leverage used by the subsidiary CDP Financial.
- The Investment Division adopted a directive on target returns and risk limits for portfolio managers.
- The Caisse adopted compliance manuals for the Equity Markets and Private Equity groups, implemented an automated compliance process for the Fixed Income and Currencies group and updated an institutional manual of policies and directives.
- The Caisse took part in more than 100 meetings with its depositors with a view to transparent communication, regular reporting and knowledge transfer.
- The Caisse has made major organizational changes to optimize its operational chain. The activities of the analytical platforms, quantitative investment information support and investment administration were thus combined within the Finance and Operations Executive Vice-Presidency.

In 2008, the Caisse will begin developing its Strategic Plan 2009-2011 by organizing various consultations and discussions involving its officers, Board members and depositors.

FIGURE 88
THE CAISSE'S MANAGEMENT FRAMEWORK



1.

PLAN

Every three years, the Caisse establishes a strategic plan that defines its main orientations, sets its objectives and defines the action to be taken to achieve them.

On the basis of this three-year strategic plan, each year the Caisse's senior managers prepare business plans, establish a book of business and information technology projects, and prepare the corresponding personnel, operating and capital budgets. Each business unit is responsible for the relevant portion of the annual business plan, and the employees are responsible for the objectives set out in the plan. Individual objectives are established jointly by employees and team leaders, and then approved by the next two hierarchical levels.

The Board of Directors approves and regularly monitors the three-year strategic plan, the annual business plans, the project book and the budgets.

In addition, twice a year the President and Chief Executive Officer meets with all employees of the Caisse, as well as the members of the expanded Executive Committee, which includes the main officers. During these meetings, he provides an update on the Caisse's business objectives. Lastly, he meets with the main officers of the investment groups and the general services units on a regular basis to discuss business objectives, projects and budgets.

2.

ORGANIZE

The organizational structure and the regulation on internal management define the roles and responsibilities of each member of the organization, from the Board of Directors to the employees, in the conduct of the Caisse's operations. At the same time, the Caisse's mission, investment philosophy and values serve to channel their efforts toward a common objective.

INTERNAL MANAGEMENT*

The business operations of the Caisse are overseen by the Board of Directors, which consists of a maximum of 15 members, including the Chairman and the President and Chief Executive Officer. The Board of Directors has four committees: the Human Resources Committee; the Audit Committee; the Governance and Ethics Committee; and the Risk Management Committee (see the section "Board of Directors and Board committees").

The Board of Directors and its committees ensure that the Caisse's management complies with the provisions of the Act respecting the Caisse and its regulations, and that the institution adopts the measures required to achieve the objectives set out in its mission.

The President and Chief Executive Officer is responsible for management of the Caisse. The Investment Division, the Real Estate group, the Private Equity group and the five general services teams report directly to the President and Chief Executive Officer.

The Investment Division includes the investment groups active on liquid markets, namely Fixed Income and Currencies, Equity Markets and Hedge Funds, as well as asset allocation operations, including the activities of the Chief Strategist. The Caisse's investment groups work in co-operation with five general services teams: Depositors and Risks; Finance and Operations; Human Resources and Organizational Development; Corporate Affairs; and Information Technology.

Internal Audit reports directly to the Chairman of the Audit Committee of the Board of Directors. From the administrative standpoint it reports to the President and Chief Executive Officer.

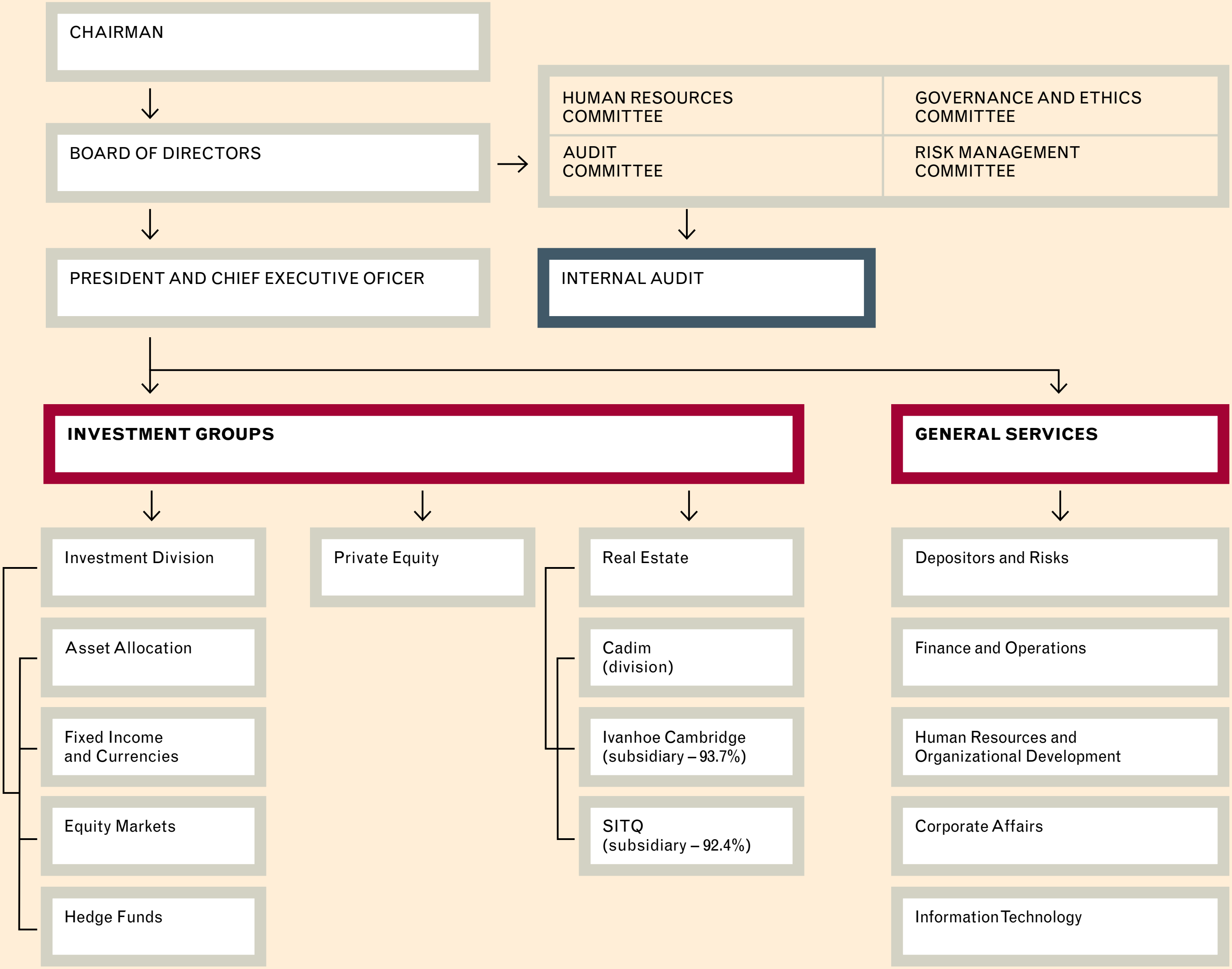
The senior managers have created various committees to assist them with their work and have assigned to them oversight and management of the institution's operations.

* The regulation on internal management is available on the Caisse's website.

FIGURE 89

ORGANIZATIONAL STRUCTURE

(as at December 31, 2007)



Executive Committee
The Executive Committee has a mandate to advise the President and Chief Executive Officer regarding major decisions concerning the overall management of the organization. The Committee therefore oversees and monitors the institution's operations.

The section "Executive Committee" of the Annual Report presents the members of the Executive Committee.

The committees described below are under the jurisdiction of the Executive Committee, to which they report periodically.

Depositors and Risks Committee
The Depositor and Risks Committee (DRC) has a mandate to oversee and implement policies and systems designed to maintain an acceptable level of risk for the Caisse's operations. The DRC's responsibilities include interpreting depositors' investment policies, particularly in terms of market, liquidity and credit risk. It monitors and controls risks and reports regularly to the Executive Committee and the Board's Risk Management Committee. The DRC also examines measures to be taken to manage risks adequately. It approves risk guidelines and limits to maintain the best possible balance between assumed risk and expected return.

Depending on the size of transactions and the level of authorization required, a specific committee, the DRC-Transactions, approves investment proposals submitted to it, mainly by the Private Equity and Real Estate groups. As the case may be, the DRC-Transactions then approves the transaction or makes recommendations to the Chief Investment Officer, the President and Chief Executive Officer or the Risk Management Committee as well as to the Board.

Investment Division Committee
The Investment Division Committee has a mandate to review and approve the Caisse's main investment orientations, in addition to promoting collaboration between the investment groups.

The main responsibilities of the Investment Division Committee are to:

- Approve, for each specialized portfolio, the investment philosophy, long-term risk and return forecasts and significant changes to external management mandates;
- Co-ordinate the sharing of information on market trends, best practices and definition of financial research programs, as well as monitor these programs and the related internal partnerships;
- Advise the Chief Investment Officer on asset allocation and investment strategies for each of the Caisse's 18 specialized portfolios.

Information Technology and Capital Budget Committee
The Information Technology and Capital Budget Committee has a mandate to maintain a technology platform adapted to the Caisse's operations, to approve major technology management policies and to ensure that projects are in keeping with the Caisse's strategic orientations.

The Committee also approves the annual plan for information technology projects and the related capital budget and submits them for approval to the Executive Committee. It also regularly monitors progress on various computer-related projects.

Disclosure Committee
The Disclosure Committee has a mandate to ensure compliance with the financial certification policy. Its responsibilities include:

- Reviewing the list of signing authorities for internal financial certificates and the texts of the financial certificates as well as making recommendations to the President and Chief Executive Officer;
- Reviewing all the internal financial certificates, including the conclusions and supporting documents;
- Recommending changes to the financial reporting process or internal controls after reviewing the internal financial certificates;
- Evaluating the design and effectiveness of the disclosure controls and procedures; and
- Evaluating the design of the internal control for financial information.

3.

EXECUTE

The Caisse has adopted various policies, directives and procedures to oversee the operations of its investment groups and general services teams. These policies define the field of action of the employees and the business units in the exercise of their functions, including their relations with depositors, partners and other stakeholders. Some are broad and concern all employees, such as the human resources policy, while others cover specific activities or processes.

For example, the investment policies oversee the work of the portfolio managers. For each specialized portfolio, the investment policy defines the philosophy, management style, investment universe, benchmark index, value-added objective and risk oversight, including concentration limits. The policies result in directives and procedures specific to each management mandate. The managers know the limits applicable to their investment operations and are obliged to respect them.

Finally, certain policies define the working environment of the Caisse's employees. They concern such matters as harassment at the workplace and application of the *Charter of the French Language*.

4.

CONTROL*

The control functions are both centralized and decentralized; they may cover the Caisse as a whole or a specific process used by a business unit. Each control is designed to ensure that the policies, directives and procedures governing the Caisse's operations are applied and respected.

INTERNAL CONTROL

The Caisse's internal control mechanism is applied systematically on all levels of the organization. It consists of an effective set of activities and measures, including validation, authorization, audit, data reconciliation, oversight, operational performance review and separation of duties.

To ensure its processes function in a coherent fashion, the Caisse has adopted an internal control policy that serves as a broad framework. Moreover, various aspects of internal control are covered by specific policies and other documents, such as the integrated risk management policy, the compliance policy, the disclosure policy, the financial certification policy, the plan for optimal resource use and the codes of ethics and professional conduct.

The Caisse's internal control mechanism provides several control functions on various levels, namely:

- Control measures incorporated into activities, business processes and computer systems, and applied by those immediately responsible for them;
- Control functions independent of the processes used for investment and transaction origination, settlement and accounting processes;
- Oversight functions, including the committees of the Board of Directors and those of senior management, as well as internal audit and compliance; and
- External audit functions performed by the Auditor General of Québec and accounting firms, as well as monitoring by the credit rating agencies.

The internal control policy requires that senior management do overall self-assessments each year of the effectiveness of the general control environment and the fraud prevention and detection framework. In addition to these self-assessments, it also provides that Internal Audit assess the design and implementation of the processes and controls related to the general and information technology control environment.

* The internal control policy is available on the Caisse's website.

FINANCIAL GOVERNANCE*

The Caisse has put in place a stringent financial certification policy to ensure the integrity of its financial processes and the reliability of the financial information that it prepares and communicates. The financial certification policy oversees and formalizes financial reporting by the Caisse and its subsidiaries. It is based on the principles of Multilateral Instrument 52-109 of the Canadian Securities Administrators, to which the Caisse is not subject. Implementation of the financial certification policy is in progress and should continue until the end of 2008.

Under this policy, the Caisse must ensure that the financial information that it discloses faithfully reflects its financial position in all material respects and that this information is complete, actual, based on fair value and presented according to appropriate accounting standards. The policy also provides that the President and Chief Executive Officer and the Executive Vice-President, Finance and Operations, sign a public financial certificate each year. The certificates of both officers are at the beginning of the section "Returns and financial position" of the Annual Report. Both signatories of the public certificates rely on internal financial certificates signed by several officers of the Caisse and the subsidiaries, as well as the work done under the financial certification program.

The conclusions of the Disclosure Committee concerning the design of internal control over financial reporting and the effectiveness of the disclosure controls and procedures are given at the beginning of the section "Returns and financial position."

* The financial certification policy is available on the Caisse's website.

COMPLIANCE**

The purpose of the compliance policy is to ensure compliance with the laws, regulations, policies and directives applicable to the Caisse's operations, at all levels and in all functions. Compliance activities take several forms, such as documentation, dissemination and co-ordination of policies and directives, monitoring and implementation of compliance programs, and training of officers and employees.

The policy provides, for example, that the persons responsible for compliance provide the Board of Directors, the Risk Management Committee and the Executive Committee with the assurance that the compliance programs are applied. They must also provide the Audit Committee with the assurance that the mechanisms used to monitor compliance are sufficient and effective.

Moreover, compliance with the depositors' investment policies and the investment policies of the specialized portfolios constitutes an important part of the compliance programs applied on a half-yearly basis. Certificates of compliance with the policies are sent to senior management, the Board of Directors and the depositors.

In addition, the Board members, the officers and all employees of the Caisse must abide by a code of ethics and professional conduct. The code emphasizes the importance of ethical behaviour and professional conduct appropriate to business practices, respect for individuals and groups, and compliance with the laws, policies and regulations applicable to the Caisse.

Each year, all employees are obliged to reconfirm that they endorse the Code of Ethics and Professional Conduct. They must also report any situation where it is reasonable to believe that the Code has been infringed.

To avoid any conflict of interest, employees are subject, for example, to preauthorization of their personal transactions. As for officers, they must place their portfolios in a blind trust.

The codes of ethics and professional conduct are given in the "Additional Information – Annual Report 2007."

** The compliance policy and the codes of ethics and professional conduct are available on the Caisse's website.

INTEGRATED RISK MANAGEMENT

To fulfill its mission as a fund manager, the Caisse must oversee and manage the risks related to its operations, especially active management of investments. To that end, it has adopted an oversight model to ensure integrated risk management and better decision-making within the Caisse's investment groups and general services teams.

Governance of risk management is based on three levels of control:

- The managers in the investment groups and general services;
- The Depositors and Risks Committees (DRC and DRC-Transactions) and the Executive Committee, assisted by independent teams of managers;
- The Board's Risk Management Committee and the Board of Directors;
- Internal Audit is also considered a third level of control by the Caisse.

The integrated risk management policy is the cornerstone of risk oversight and covers all facets of risk management. It applies to all Caisse employees and to its mandataries in the exercise of their functions. Generally speaking, the policy is conducive to implementation of a risk management culture based on rigorous practices and helps the Caisse fulfill its fundamental mission for its depositors. More specifically it is designed to:

- Prevent excessive losses on the specialized portfolios;
- Provide directives on the level of risk that the Caisse is prepared to assume in carrying out its mission pursuant to the investment policies of its depositors;
- Align target returns with risk limits; and
- Promote effective allocation of risk limits to the various investment groups and clearly establish risk management responsibilities.

The integrated risk management policy defines and describes:

- The main principles: the risk model and the independence of the support teams in integrated risk management;
- The organizational structure, the normative framework, governance and sharing of responsibilities;
- The risk budgets;
- The limits on transaction authorization and management outsourcing, the application of limits on transaction authorization and limits on concentration by issuer;
- The framework for outsourcing of management and use of derivative financial instruments; and
- The management of various types of risk.

THE CAISSE'S RISK MODEL

FIGURE 90

To manage risks properly, it is essential to be able to identify them and understand all their facets so that they can be evaluated and ranked in order of priority. The risk model is therefore the basis of risk management at the Caisse. It establishes a common language, so that the various stakeholders can communicate effectively regarding risk management.

The risk model is also conducive to rigorous and exhaustive analysis of each risk. Ultimately, this process contributes to investment strategies that generate stable, optimal returns that meet depositors' expectations.

According to this model, the risks inherent in the Caisse's operations are divided into three broad categories: business risks, financial risks and operational risks. These categories are then subdivided to clearly distinguish each possible risk. Each risk requires a specific management approach that is often quite different from those used for the other risks.

OVERSIGHT AND MEASUREMENT OF THE RISKS RELATED TO THE CAISSE'S OPERATIONS

Although each risk is distinctive, the Depositors and Risks Committee (DRC) aims to integrate them into a single analytical process. To ensure that oversight and practice of the Caisse's integrated risk management comply with the investment industry's best practices, the risk management policies are revised regularly with a view to their continual improvement. The DRC and the portfolio managers are assisted by internal and external experts whose role is to improve the risk evaluation methods.

BUSINESS RISKS

Strategic risk

The Caisse is exposed to strategic risk when an event related to its practices or relations, or those of its subsidiaries or employees, does not comply with its mission, culture and fundamental values. Strategic risk is also related to the inadequacy of business strategies or deficiencies in the implementation of the organization's strategic orientations. Finally, the Caisse will be exposed to a strategic risk if its resources are not allocated as a function of established priorities.

The Caisse manages this risk with a structured strategic-planning process that involves all units of the organization. Strategic orientations are proposed by the Executive Committee, approved by the Board of Directors and communicated to all employees. The members of the Board of Directors and of the Executive Committee receive a monthly summary of the Caisse's operations. Moreover, the President and Chief Executive Officer monitors the business plans on a regular basis.

Reputation risk

Reputation risk is the possibility that an event related to the business practices or relations of the Caisse, its subsidiaries or its employees will adversely affect the Caisse's image or cause the public to lose confidence in the institution. This risk could detract from the organization's ability to achieve its objectives.

All directors, members of management and employees are responsible for carrying out their activities in such a way as to minimize reputation risk.

The Caisse manages and controls this risk by means of codes of ethics and professional conduct for directors, officers and employees, training programs, effective internal management and governance practices and various policies and procedures. It also ensures that the information it provides internally and externally is truthful and has been checked. It strives to ensure the public and the media gain a better understanding of its operations. The Caisse also rigorously monitors communications concerning it and responds by taking public positions as required.

FINANCIAL RISKS

Market risk

Market risk represents the risk of financial loss resulting from fluctuations in the price of financial instruments. The value of a financial instrument may be affected by variations in certain market parameters, such as interest rates, foreign exchange rates, share prices and commodity prices as well as their volatility. The risk of a loss of value corresponds to absolute risk. In the context of active management, active risk, in other words the possibility that managers' returns will be different from those of their benchmark indexes, is added to absolute risk.

The market risk to which the specialized portfolios are exposed is assessed regularly. It is measured according to the value at risk (VaR) method, which is based on a statistical evaluation of the volatility of individual market positions and their correlation.

Credit, concentration and counterparty risk

Credit risk is the possibility of a loss of market value in the event that a borrower, an endorser, a guarantor or a counterparty does not honour its obligation to repay a loan or to fulfill any other financial obligation, or sees its financial situation deteriorate. Counterparty risk corresponds to the credit risk from current or potential exposure related to operations involving over-the-counter derivative financial instruments.

The Caisse constantly monitors matters that are sensitive to credit risk, using four types of analysis:

- Analysis of concentration risk measures the fair value of all financial products related to a single issuer or a group of issuers with common characteristics (regions, sectors, credit categories);
- Analysis of credit risk measures the probability of default and the recovery rate on debt products held by the Caisse, taking into account the credit quality of each security;
- Analysis of counterparty risk measures the current credit exposure of the Caisse's counterparties for over-the-counter derivatives, taking into account agreements making it possible to benefit from the offsetting effect of amounts at risk and the exchange of collateral;
- Analysis of delivery risk measures default risk and liquidity risk in the settlement of transactions. This risk arises mainly from currency contracts.

Liquidity risk
Liquidity risk is the possibility that the Caisse may not always be able to fulfill its undertakings without having to obtain funds at abnormally high prices or that it may be obliged to sell assets. It also corresponds to the risk that it may not be possible to sell investments rapidly or to invest without having a significant adverse impact on the price of the investment in question.

Compliance with established rules is monitored on a monthly basis, and the liquidity status is submitted to the DRC on a daily basis. The Caisse evaluates the impact of unfavourable financial market scenarios on the liquidity situation.

OPERATIONAL RISKS

Operational risk corresponds to the possibility of direct or indirect financial loss arising from the deficiency of operations.

Human resources management risk
The risk related to human resources management includes such elements as recruiting (recruiting competent, honest and motivated personnel), training (maintaining and developing employee competencies) and evaluating performance and compensation (ensuring fair, equitable and competitive compensation).

Process management risk
The risk related to management of the Caisse's processes applies to processes for input, settlement and tracking of transactions, and errors that may arise in the execution of the processes in place. In addition to internal causes specific to the Caisse, this risk may arise from the poor quality of services rendered by its subcontractors, external suppliers and business partners.

System management risk
The Caisse is exposed to a risk in the event of deficiency of its information technology infrastructures or computer systems. This deficiency may result from a breakdown or other malfunction that may cause delays or an interruption in operations that is not caused by a disaster.

Theft and fraud risk
This is the risk of losses arising from intentional acts to defraud, to embezzle funds or to appropriate the assets of the Caisse or its depositors.

Disaster risk
The risk of disaster represents the risk of losses arising from interruption of business as a result of a natural or other disaster.

Compliance risk
Compliance risk corresponds to the risk of losses as a result of a deficiency that is unintentional or due to negligence, to policies and directives, and to professional and ethical standards and practices specific to the Caisse's operations. It occurs in the event that the Caisse fails to fulfill its duties.

Legal risk
Legal risk is related to the rights and obligations associated with the Caisse's operations and the legislative framework in which they are carried out. Important aspects of legal risk are related to compliance with the laws and regulations governing the Caisse and its management teams, as well as assurance that the agreements concluded by the institution properly reflect the planned operations and contain the appropriate provisions. Legal risk also refers to the risk of lawsuits that may affect the Caisse.

Operational risks are managed and measured through self-assessment of risks, a listing of incidents, the use of indicators and maintenance of rigorous processes. The Caisse continues to introduce methods to evaluate and manage these risks.

5.

EVALUATE

The evaluation function checks whether risks are managed adequately to achieve objectives. This function can be exercised in a centralized or decentralized manner, internally and externally.

INTERNAL AUDIT

Internal Audit's mission is to provide objective assurance and consultation services to increase the effectiveness of the Caisse's operations. It helps to achieve the Caisse's objectives by using a systematic and methodical approach to assess the processes and systems used for risk management, control and corporate governance. It also helps improve them by making proposals to increase their effectiveness.

The scope of the work done by Internal Audit must make it possible to determine whether the processes, systems and controls, as they have been developed and implemented, are sufficient and are applied in such a way as to ensure that:

- Risks are defined, evaluated and managed adequately;
- Financial and operational information is authorized, reliable and available in a timely fashion;
- Directives, policies, laws, regulations and statutory requirements are respected;
- Human, informational, material and financial resources are acquired economically, used efficiently and protected adequately; and
- Business programs, plans and objectives are carried out effectively, in accordance with the Caisse's mission.

Internal Audit reports functionally to the Audit Committee of the Board of Directors. From the administrative standpoint, it reports to the President and Chief Executive Officer. The organizational structure is designed to ensure Internal Audit has the independence required to play its role effectively.

EXTERNAL AUDIT

External oversight is effected by various authorities. The Auditor General of Québec audits the Caisse's financial statements each year and takes part in various investment valuation processes during the year. Independent accounting specialists periodically assess the fair value of unlisted liquid investments, private equity and real estate. Independent auditors assess the Caisse's compliance with performance standards (GIPS®) in establishing and presenting its returns. Lastly, three rating agencies evaluate the Caisse's credit profile and ability to discharge its financial undertakings.

6.

REPORT AND COMMUNICATE *

The Caisse is bound to its depositors by service agreements that define the responsibilities of each party and specify the conditions and frequency for the Caisse's reporting on its work. The agreements provide for monthly investment reports and individual meetings every six months. The depositors are also invited to seminars and events organized specifically for them so that they can assess the various economic and financial factors affecting their portfolios.

In its communications, the Caisse strives to achieve a balance between its desire for transparency and its obligation to protect depositors' interests, while complying with the law and its contractual undertakings toward third parties. To that end, the Caisse has adopted an information disclosure policy for its external communications. The policy defines the way the Caisse processes and discloses information to the media and the public, mainly through its press releases, press conferences and Annual Report.

The Caisse is obliged to disclose information to comply with certain laws governing it, including its constituting statute, the Access Act and securities legislation. Although it is not subject to the disclosure requirements and recommendations applicable to publicly traded companies, it strives to comply with the best disclosure practices of its industry.

The many types of information disclosed include:

- Insider trading transactions in accordance with the disclosure requirements of securities legislation;
- Material facts, such as decisions affecting the institution as a whole or a major investment;
- The exercise of its voting rights; and
- Its audited combined annual financial statements, the tables of returns presented in "Additional Information – Annual Report 2007" and the press release announcing its results.

Internally, the Caisse ensures that the Board of Directors and the Executive Committee, as well as their respective committees, receive complete information in a timely fashion and that feedback mechanisms permit effective discussion. The Caisse also takes care to communicate effectively with its employees through open, sustained and transparent communication. For instance, it aims to inform its employees adequately of its business objectives, strategies and projects as well as news concerning it. The Caisse also ensures that news disseminated externally is announced beforehand to its employees. In this way, it promotes cohesion and a sense of belonging within the institution. Lastly, it encourages transparent discussions within and between its teams, and promotes person-to-person interaction through various communication channels.

* The information disclosure policy is available on the Caisse's website.

7.

OPTIMIZE*

The Caisse ensures that the funds entrusted to it by depositors are managed with due regard for economy, efficiency and effectiveness. Economy involves acquiring resources of the required quality, at a reasonable cost and in a timely fashion. Efficiency involves ensuring that resources are sufficient for the business requirements and are used appropriately. Effectiveness is measured by the degree to which an organization achieves its business objectives.

To achieve optimal use of resources, the Caisse ensures that:

/ Its strategic orientations, business plans, management practices used for administration, operations and control, and systems and tools are established or designed so that their implementation generally allows the organization to achieve the results it seeks, which is referred to as "effectiveness"; and

/ It acquires and manages the resources needed to achieve results with due regard for "economy" and "efficiency."

The Caisse's resources, processes, systems, tools and controls are designed to form a coherent whole in order to meet depositors' expectations. To reach that objective, the Caisse optimizes its resources in order to:

/ Achieve depositors' target returns;

/ Develop management practices that correspond to the best practices used by institutional fund managers; and

/ Make proper use of the funds placed at its disposal to manage its operations.

The Caisse ensures optimal use of resources with a three-year plan that proposes permanent activities and projects to improve management of investment and operational resources. Investment resources include depositors' holdings and the risk budget, while operational resources include human, material, financial, technological and informational resources.

The plan is based on the following principles:

/ Operational resources are acquired and managed by means of mechanisms that provide sufficient resources to successfully carry out the main activities and to prudently manage costs and changes in them;

/ Investment resources are managed actively by means of sufficient operational resources to successfully carry out activities with a substantial impact on returns;

/ The effectiveness of resources is assessed comprehensively by a comparison of the results obtained with industry standards, namely benchmark indexes;

/ The Caisse's structures, activities and methods are subject to a continual improvement process;

/ The work of Internal Audit helps strengthen the management practices used for administration, operations and control, as well as the Caisse's systems and tools.

* A document on the Caisse's approach to optimal use of resources is available on its website.

EXERCISE OF VOTING RIGHTS AND RESPONSIBLE INVESTMENT*

The Caisse exercises its voting rights systematically according to the guidelines defined in its policy on the exercise of voting rights. Analyzing resolutions and taking a position on them involve considerable work, since it is a shareholder in more than 3,000 Canadian and foreign companies.

Resolutions from company management concern mainly governance, such as the election of directors and compensation. Most of the resolutions submitted by shareholders also concerned governance but a large number are related to environmental and social issues.

The Caisse processed 3,657 proxy voting files involving Canadian and foreign companies during the year. The files involved analyzing and voting on a total of 28,603 proposals.

The Caisse expects its portfolio companies to respect principles of good governance, fundamental rights and freedoms, workers' rights and the local communities where they operate. It has therefore adopted a policy on socially responsible investment, which advocates an approach based on dialogue with companies.

In addition to examining the financial position of companies, the managers therefore include environmental, social and governance criteria in the analysis preceding their investment decisions. They also take advantage of discussions with these companies to inform them of the Caisse's concerns regarding corporate responsibility. The Caisse occasionally submits proposals to shareholder meetings if the social record of a portfolio company is not satisfactory. Ultimately, the Caisse may sell the investment if the dialogue does not produce the expected results.

The Caisse is also involved in international efforts to ensure socially responsible investment. In 2006, it became one of the first signatories to the Principles of Responsible Investment of the United Nations. It has also endorsed the Carbon Disclosure Project, which enables investors to determine the impact of companies' operations on climate change.

* The policy on the exercise of voting rights, the details of the Caisse's voting and the policy on socially responsible investment are available on the Caisse's website.

TAKING THE LONG VIEW MEANS INVESTING IN OUR EMPLOYEES' POTENTIAL

/ **EKATERINA BARZYKINA**
Director
Market Risk Management
Depositors and Risks

OPERATIONAL LEVERS

Q

HOW DOES THE CAISSE EVALUATE ITS RISK MANAGEMENT ?

A

THE CAISSE'S GOVERNANCE AND RISK MANAGEMENT PRACTICES ARE VERY SOUND

Assuming and managing risk is an integral part of investing. The two activities go hand in hand. Any investment decision involves an element of risk that has to be measured and monitored to ensure the risk is in line with the expected return.

The Caisse has developed a rigorous, integrated model for risk management. It allows for more effective decisions in its investment operations as well as its other areas of activity. The Caisse's approach is based on the accountability of each level where risk is monitored and investments are authorized.

Moreover, the Caisse is always on the lookout for the best risk management practices. It has therefore begun to benchmark the risk management practices used by its peers and the financial industry.

LEVER:

HUMAN RESOURCES EXCELLENCE

The utmost importance of human resources excellence becomes apparent in the increasingly complex and competitive environment of the financial sector. Since the Caisse's performance is based above all on the expertise of its employees, it is striving to become a benchmark employer that can attract, retain and motivate employees who will enable it to generate the returns expected by its depositors.

This ambition involves major challenges, owing to the scarcity of qualified professionals and their considerable mobility. In response to this situation, during the year the Caisse adopted a new approach to talent management that is based on the simultaneous commitment of all officers and employees concerned. This change of direction has enabled the Caisse to revise its employee-management model and to rethink its offer of services, notably by introducing a new approach based on three management principles – meritocracy, transparency and collaboration – as well as new policies and tools.

After focusing mainly on optimizing performance management and direct compensation in 2007, the Caisse will continue in this vein in 2008 by optimizing governance, staffing and skills development. In the years to come, the Caisse will have to rise to other challenges, such as manpower retention and diversity, knowledge transfer from one generation to the next and the increasing specialization of its industry.

The Caisse, excluding Cadim, had 772 employees as at December 31, 2007. The real estate units, Cadim, Ivanhoe Cambridge and SITQ, employed a total of 1,772 people.

HIGHLIGHTS 2007

/ Startup of the program to optimize talent management, including adoption of the project's first governance rules and a review of the roles of the various teams in the Human Resources and Organizational Development Executive Vice-Presidency.

/ Development of role profiles for all positions, including criteria for positions having a specific nature or status.

/ Development of competency profiles for team leaders and startup of the senior management succession plan.

/ Creation of a report to facilitate budgetary management of salaries, as well as a new human resources dashboard for each Executive Vice-Presidency.

/ Introduction of a new change-management process to underpin deployment of 14 priority human resources projects.

/ Development of a work plan to meet the requirements of the Act respecting equal access to employment.

/ A total of 234 positions filled, 55 of them internally, and organization of 204 employee training sessions.

/ Creation of Employee Services for one-stop management of personnel requests.

/ Creation of a business continuity plan in the event of a pandemic.

OUTLOOK 2008

/ Finalize implementation of projects developed in 2007:

- Complete the last stages of the new procedure to evaluate employee performance and the new variable-remuneration program;
- Determine the specific competencies for each position, in line with the new role profiles;
- Put in place a new salary structure based on the new role profiles as well as pay-equity rules;
- Complete the senior management succession plan.

/ Achieve the human resources objectives specific to each Executive Vice-Presidency, according to the priorities established by each in its 2008 business plan.

/ Continue the program to optimize talent management:

- Define the Caisse's talent-management philosophy and develop an umbrella policy for deployment of the new approach to talent management;
- Do a complete career-path review by revising the staffing and skills-development policies;
- Develop initiatives to ensure better employee retention;
- Analyze the deployment needs of a new human resources portal;
- Improve the human resources dashboard.

A STIMULATING WORK ENVIRONMENT

To work at the Caisse is to come in contact each day with highly qualified professionals in various areas, recruited in Québec and elsewhere in the world. The Caisse is justifiably proud of its experienced professionals and up-and-coming generation of talent.

Almost 50% of the Caisse's employees have more than 15 years of experience in their area of expertise. Their overall level of qualification is also exemplary. For example, 82% of employees have a university degree. Moreover, 37% have a master's degree and 3% have a doctorate.

Many employees hold a designation awarded by a recognized organization. In 2007, a total of 125 employees held the designation of Chartered Financial Analyst (CFA) and 11 held that of Financial Risk Manager (FRM). Moreover, the investment professionals are backed by multidisciplinary teams whose members have various types of expertise, with many belonging to professional bodies (accountants, actuaries, engineers, lawyers, notaries and so on).

The Caisse believes it is essential to ensure a new generation of talent for its various business units and therefore provides financial support to employees who continue their professional training. The Caisse invested almost 2.6% of its payroll in employee training in 2007. Moreover, each year it hires new graduates and offers training internships and fellowships to university students. As a result, more than 15% of the Caisse's employees are under the age of 30.

The Caisse endorses the principles of employment equity and aims for a level of diversity that is representative of the various groups that make up our society.

The Caisse's business office in Montréal provides a first-rate working environment. Employees have a variety of leading-edge technological tools and access to a broad range of specialized information. The Caisse also offers its employees various services, including a day-care centre, a fitness centre and activities designed to enhance their well-being. Lastly, the Caisse offers competitive compensation aligned with its reference markets.

MANAGEMENT PRINCIPLES

The Caisse's approach to human resources is based on three principles: meritocracy, transparency and collaboration. This approach ensures engagement and recognition of each employee's efforts by aligning individual objectives, team objectives and organizational objectives.

MERITOCRACY

Encourage employees to achieve an outstanding level of success by recognizing performance and rewarding those who excel.

TRANSPARENCY

Promote clear, open communication between team leaders on various hierarchical levels and their employees to establish specific objectives and expectations.

COLLABORATION

Promote employee engagement and commitment to achieve objectives.

LEVER:

RIGOROUS AND DYNAMIC RISK MANAGEMENT

In recent years, the Caisse has invested a great deal in its risk control and optimization teams as well as in systems and tools to measure overall risk more accurately. It has also ensured robust governance with various policies, directives and procedures (see "Management framework"). The integrated risk management policy is conducive to a rigorous risk management culture and stringent practices for all the Caisse's operations. Lastly, the Caisse has ensured that all stakeholders are aware of risk management concepts.

The risk management group had a challenging year, given the very volatile nature of the markets. It had to cope with the liquidity crisis while maintaining the normal course of its operations. The Caisse is determined to constantly improve this function to achieve its integrated risk management objective. In 2008, the Caisse will continue to draw on the industry's best practices by emphasizing processes and methods, with the objective of becoming a benchmark institution. On the initiative of the Depositors and Risks Executive Vice-Presidency, a mandate was given to a consulting firm to survey current risk management practices, identify best practices and carry out benchmarking vis-à-vis the Caisse's peers. The findings will be used to improve risk management practices and to prepare the Strategic Plan 2009-2011.

HIGHLIGHTS 2007

- First stages of implementation of tools to optimize the Caisse's overall risk allocation.
- Risk analysis for 98 investment projects totalling $32 billion, mainly for the Private Equity and Real Estate groups.
- Organization of a training seminar on certain risk management and market risk concepts for all Caisse employees, the Board of Directors and certain depositors.
- Implementation of a new methodology to estimate liquidity risk.
- Identification of key indicators of the Caisse's operational risks.
- Review of the analysis of new financial products, namely investment vehicles used for the first time by a manager but authorized by the portfolio's investment policy, to determine operational risks.
- Upgrading of the system used to estimate market risk in order to perform sophisticated simulations.
- Self-assessment of operational risks applicable to certain transversal processes, in particular the operational application chain.

OUTLOOK 2008

- Continue to implement a process to optimize the Caisse's overall portfolio.
- Establish a plan to improve risk management, according to recommendations made by a consulting firm and based on the best practices used by the Caisse's peers.
- Finish identifying key operational risk indicators.
- Continue to implement the market risk methodology for real estate assets.
- Continue to improve the analytical platform and the information systems used to manage market risk.
- Improve risk management monitoring capability.

LEVER:
LEADING-EDGE RESEARCH

Research is a vital performance lever for active management of depositors' holdings. Within each investment group, creation of value added is based essentially on proprietary research, complemented by targeted external research.

For several years, the Caisse has been using proprietary research to set itself apart from other institutional fund managers. In 2006, it laid the foundations of a dynamic research unit by combining its multidisciplinary research teams within the Investment Division.

Once again this year, as a result of recommendations made by these teams, the Caisse's investment policies ranked in the first quartile of the industry. Moreover, the investment groups also do their part, since they include experienced market analysts. For example, the excellence of their fundamental analysis is shown by the results for the specialized Canadian Equity portfolio. In 2008, the Caisse will consolidate its research capabilities, with a view to innovation and excellence.

HIGHLIGHTS 2007

/ Revision of the investment policies of most of the Caisse's depositors.

/ Optimization analysis of the suitable weight for the Private Equity group in the Caisse's portfolio, which resulted in an increase in the assets under management by the group.

/ Changes to the benchmark indexes of the specialized Québec International and Hedge Funds portfolios.

/ Revision of the methods used for long-term risk and return forecasts for the specialized portfolios.

/ Publication of six articles in scientific and professional journals.[1]

/ A prestigious Bernstein Fabozzi/Jacobs Levy Award for the Research and Investment Policy Advice team for the article "The Relative Importance of Asset Allocation and Security Selection," published in the *Journal of Portfolio Management*; and the Swisscanto Award for the same team for the article "Relative Importance of Hedge Fund Characteristics," published in *Financial Markets and Portfolio Management*.

/ Various types of economic research on major structural trends.

OUTLOOK 2008

/ Continue to offer to depositors quality advisory services based on innovative proprietary research and to recommend first-quartile benchmark portfolios.

/ Continue research on such subjects as selection of benchmark indexes, use of leverage and optimal allocation of the active-risk budget.

/ Enhance research capability, especially for asset allocation analysis.

/ Research and develop innovative investment strategies (systematic quantitative strategies, award of mandates) to enhance asset allocation returns.

/ Develop investment strategies to capitalize on research on economic conditions.

/ Perform strategic monitoring of emerging markets to capitalize on the best investment opportunities.

1 /Plante, Jean-François, and Mathieu Roberge. "The Passive Approach to Commodity Investing," *Journal of Financial Planning*, vol. 20, no. 5, May 2007, p. 66-75.
/Carpentier, Cécile, Jean-François L'Her and Jean-Marc Suret. "Does Securities Regulation Constrain Small Business Finance? An Empirical Analysis," *Small Business Economics: An International Journal*.
/Desrosiers, Stéphanie, Jean-François L'Her and Jean-François Plante. "Importance of Style Diversification for Equity Country Selection," *Journal of Asset Management*, vol. 8, no. 3, September 2007, p. 188-199.
/Hamza, Olfa, Jean-François L'Her and Mathieu Roberge. "Active Currency Hedging Strategies for Global Equity Portfolios," *Journal of Investing*, vol. 16, no. 4, winter 2007, p. 146-166.
/Carpentier, Cécile, Jean-François L'Her and Jean-Marc Suret. "Competition and Survival of Stock Exchanges: Lessons from Canada," *Review of Pacific Basin Financial Markets and Policies*, vol. 11, no. 2, 2008.
/Kooli, Maher, and Jean-François L'Her. "Dividends vs. Share Repurchases Evidence from Canada: 1985-2003." *Financial Review*.

LEVER:

LEADING-EDGE TECHNOLOGY AND OPERATIONAL EFFICIENCY

In technology and operational efficiency, 2007 was a year of continuity for the Caisse, which pursued implementation of its three-year information technology plan. Several major initiatives were deployed during the year to give the managers the increasingly powerful technological levers required to manage their portfolios. About 20 brokerage firms around the world are now linked electronically to the trading desks for execution and confirmation of buy and sell orders. Similarly, various transaction-settlement processes were reviewed, optimized and automated to make them more effective and efficient. Mechanisms are also in place to ensure Canadian stock and bond transactions meet the standards established by the financial authorities. In business continuity, the Caisse now has solid, operational IT recovery plans that allow for gradual resumption of critical operations systems within 24 hours. In 2008, the Caisse will continue to put in place its plan to further strengthen the operational chain and to deploy new tools for managers.

HIGHLIGHTS 2007

- Deployment of tools to manage and simulate returns on the Private Equity group's portfolios.
- Implementation of tools to optimize the portfolios of the Real Estate group.
- Deployment to 20 brokerage firms on international markets of a connectivity system to process orders.
- Implementation of a confirmation module for over-the-counter derivatives.
- Implementation of a system to allow external managers to engage in short selling.
- Implementation of issuer and common-share management systems according to market standards.
- Optimization of administrative procedures for derivatives and reconciliation with brokers and custodians.
- Automation of reconciliations with clearing brokers.
- Implementation of a proxy-management system to post the Caisse's voting record on its website.
- Ongoing deployment and improvement of the Caisse's portal content.
- Implementation of several major components to modernize the overall IT infrastructure and to strengthen information security access mechanisms.
- Successful testing of the IT disaster recovery plan and synchronization with the business continuity site.

OUTLOOK 2008

- Continue to optimize the operational chain through:
  - Integration of technology platforms within the portfolio management system for cash products;
  - Overhaul of the system used to monitor the portfolios of external managers;
  - Upgrade of systems for order and market risk management.
- Implement leading-edge systems and tools that are adapted and efficient, such as:
  - The system to manage the portfolios of the Private Equity group;
  - The system to monitor compliance with the investment policies of the Fixed Income and Currencies portfolios;
  - A tool to monitor and optimize the Real Estate portfolio;
  - Overhaul of the depositors' extranet;
  - The Human Resources portal and the Caisse's website.
- Continue to reposition the IT operations infrastructure through:
  - Completion of migration to consolidate and virtualize servers;
  - Migration of applications infrastructure services to a new technology;
  - Strengthening of information security access mechanisms.

BOARD OF DIRECTORS AND BOARD COMMITTEES

BOARD OF DIRECTORS

/ HENRI MASSÉ
/ CLAUDETTE CARBONNEAU
/ LOUISE CHARETTE
/ SYLVIE DILLARD
/ A. MICHEL LAVIGNE
/ ALBAN D'AMOURS
/ CHRISTIANE BERGEVIN
/ PIERRE BRUNET
/ HENRI-PAUL ROUSSEAU
/ OUMA SANANIKONE
/ CLAUDE GARCIA
/ STEVEN M. CUMMINGS
/ YVAN ALLAIRE

BOARD OF DIRECTORS

/ PIERRE BRUNET

Chairman of the Board

Chairman of the Human Resources Committee

Member: Governance and Ethics Committee

Board member since April 27, 2005

Pierre Brunet was President and Chief Executive Officer of National Bank Financial for many years. He has also served as Chairman of the Board of Governors of the Montréal Exchange, the Montréal Board of Trade, the Investment Dealers Association, the Canadian Institute of Chartered Accountants and the Montréal Symphony Orchestra. He is currently Chairman of Montréal International and a director of METRO Inc. Mr. Brunet's many honours include the title of Fellow of the Ordre des comptables agréés du Québec, the Career A+ award from the IDA, the Order of Merit from the Université de Montréal and Officer of the Order of Canada.

/ HENRI-PAUL ROUSSEAU

President and Chief Executive Officer
Caisse de dépôt et placement du Québec

Member: Risk Management Committee

Board member since September 1, 2002

Henri-Paul Rousseau holds a Ph.D. in economics and was a university professor for 15 years before holding various senior management positions in the financial sector. He has also served as an economic adviser to the governments of Canada and Québec on various issues. His many honours include the T.M. Brown Thesis Prize for the best doctoral dissertation in economics at the University of Western Ontario and four honourary doctorates: Concordia University (Laws); Université Lumière, Lyon 2; Université Laval (Business Administration); and Université de Sherbrooke. Mr. Rousseau is a member of the Academy of Great Montrealers and is actively involved in the community.

/ YVAN ALLAIRE

Chairman
Institute for Governance of Private and Public Organizations (HEC-Concordia)

Chairman of the Governance and Ethics Committee

Member: Risk Management Committee

Board member since April 27, 2005

Yvan Allaire holds a doctorate in management science from the Massachusetts Institute of Technology and is a Fellow of the Royal Society of Canada, as well as Professor Emeritus of Strategy at the Université du Québec à Montréal. He is Chairman of the Institute for Governance of Private and Public Organizations (HEC-Concordia). Mr. Allaire is a member of the Conseil des relations internationales de Montréal (CORIM) and the National Committee (Canada) of the Aga Khan Foundation.

/ CHRISTIANE BERGEVIN

President
SNC-Lavalin Capital

Member: Audit Committee

Board member since August 28, 2007

Christiane Bergevin is a graduate of McGill University and the Wharton School of Business. She has been President of SNC-Lavalin Capital since 2001 and is recognized for her leadership in domestic and international financing. In the past 20 years, she has arranged numerous major financings in Canada and elsewhere for projects, acquisitions and partnerships. Ms. Bergevin is a director of the Business Development Bank of Canada and the Chair of its Pension Funds Investment Committee. She is also a director of Cordiant Inc. and has been a member of many boards of directors, committees and advisory groups, notably as a founding member of the Financial Women's Association of Québec, and various national bodies and industry panels.

/ CLAUDETTE CARBONNEAU

President
Confédération des syndicats nationaux

Member: Audit Committee

Board member since September 25, 2002

Claudette Carbonneau holds a master's degree in political science and is the first woman to serve as President of the Confédération des syndicats nationaux (CSN), a position she has held since 2002. She is also Chair of Fondaction and Vice-President of the General Council of the International Trade Union Confederation and First Substitute of the Canadian delegation. Ms. Carbonneau is also a member of the Québec government's Advisory Council on Labour and Manpower.

/ LOUISE CHARETTE

Corporate Director

Member: Risk Management Committee

Board member since April 27, 2005

Louise Charette holds a master's degree in business administration and a doctorate in mathematics. From 1981 to 2007, she held various management positions at the Commission de la construction du Québec, including Assistant Director General, Administration and Finance. In addition to her duties as Assistant Director General, she also headed the CCQ's Investment Committee. Ms. Charette has worked for a number of organizations. She was a founding member of the Regroupement des femmes cadres du Québec in 1984 and served as Vice-Chair of the Société d'habitation du Québec from 1998 to 2002.

/ STEVEN M. CUMMINGS CM

President and Chief Executive Officer
Maxwell Cummings & Sons Holdings Ltd.

Member: Human Resources Committee

Board member since October 1, 2003

Steven M. Cummings is President and Chief Executive Officer of Maxwell Cummings & Sons Holdings Ltd. Active in community affairs, Mr. Cummings is a past President of Federation CJA and has served as President of the Jewish General Hospital Centre Board and its Foundation Board. He is also Founding Chair of the Montreal Holocaust Memorial Centre, and Founding Co-Chair of ProMontreal. He is currently Co-Chair of the Canadian Council for Israel and Jewish Advocacy and a director of VIA Rail Canada Inc. Mr. Cummings is also a Member of the Order of Canada.

/ ALBAN D'AMOURS

President and Chief Executive Officer
Desjardins Group

Chairman of the
Risk Management Committee

Board member since August 24, 2000

Alban D'Amours completed doctoral studies, specializing in monetary theory, public finance and econometrics. After teaching for several years, he held a number of positions in Québec's public service, including Deputy Minister of Revenue and Associate Deputy Minister of Energy. He joined the Confédération des caisses Desjardins du Québec in 1988, and has held several management positions since then. Mr. D'Amours was elected President of the Desjardins Group in 2000 and was re-elected in 2004.

/ SYLVIE DILLARD

Director, Special Projects

Ministère du Développement économique, de l'Innovation et de l'Exportation

Member: Human Resources Committee

Board member since September 25, 2002

Sylvie Dillard holds a master's degree in economics and has held a number of management and research positions in Québec's public service, including Assistant Deputy Minister of Planning and Evaluation at the Ministère de la Santé et des Services sociaux. In 1998, she was named President and Director General of the Fonds pour la formation de chercheurs et l'aide à la recherche, and from 2001 to 2007 she was President and Chief Executive Officer of the Fonds québécois de la recherche sur la nature et les technologies.

/ CLAUDE GARCIA

Corporate Director

Chairman of the Audit Committee

Guest member: Risk Management Committee

Board member since April 27, 2005

Claude Garcia has completed the course requirements for a doctorate from the London School of Economics and Political Science and is a Fellow of the Canadian Institute of Actuaries and the Society of Actuaries. In 1983, he joined Standard Life Insurance, where he held several senior management positions. In 1993, he was named President of the company's Canadian operations and served in that capacity until the end of 2004. Mr. Garcia has been actively involved with a number of organizations and currently sits on the boards of Cogeco, Cogeco Cable, Goodfellow, BTB Real Estate Investment Trust and the Institut de recherches cliniques de Montréal. He is also Chairman of the Agence des Partenariats public-privé du Québec.

/ A. MICHEL LAVIGNE

Corporate Director

Member: Audit Committee

Board member since April 27, 2005

A. Michel Lavigne was President and Chief Executive Officer of Raymond Chabot Grant Thornton until May 2005. He was also Chairman of Grant Thornton Canada and a director of Grant Thornton International. His directorships include Quebecor Media, TVA, Primary Energy Recycling and Nstein Technologies. Mr. Lavigne has received many distinctions; most notably, he is a Fellow of the Ordre des comptables agréés du Québec.

/ HENRI MASSÉ

Fédération des travailleurs et travailleuses du Québec

Member: Risk Management Committee

Board member since January 27, 1999

Henri Massé headed the Fédération des travailleurs et travailleuses du Québec (FTQ) as Secretary General and then as President from 1993 to 2007. He was also Chairman of the Board and Chairman of the Executive Committee of the Solidarity Fund QFL, and a member of the Board of Directors of the Commission de la santé et de la sécurité du travail. Mr. Massé has also served on various committees of the Conseil consultatif du travail et de la main-d'oeuvre, as well as the Executive Committee of the International Confederation of Free Trade Unions.

/ OUMA SANANIKONE

Corporate Director

Member: Governance and Ethics Committee

Board member since August 28, 2007

Ouma Sananikone is a corporate director with extensive experience on the European and Asian financial markets. She has worked for 25 years in banking, financial services and investment management. She is Chairman of Smarte Carte International and a non-executive director of Icon Systems, Air-Serve and Moto Hospitality Services. Ms. Sananikone has been a board member of numerous public and private companies, as well as charitable organizations, in Australia and elsewhere. Her special areas of interest are governance, ethics, community and leadership.

BOARD OF DIRECTORS' REPORT

BOARD MANDATE

The mandate of the Board of Directors is to ensure that the Caisse is managed in compliance with the provisions of its constituting statute and regulations. It must ensure that the institution takes the necessary steps to attain the objectives stated in its mission, namely to earn an optimal return on depositors' capital while contributing to the economic development of Québec.

The Board adopts regulations and approves the Caisse's main guidelines and policies with respect to investment operations, socially responsible investment, risk management oversight and delegation of authority. Any investment proposal or matter that calls for special attention, particularly in light of its intrinsic importance or impact on the Caisse's portfolio or asset allocation, is discussed by the Board.

The Board reviews and approves the Caisse's strategic plan. It approves the institution's annual business plan, and reviews management's evaluations of the economic and financial environment throughout the year. It reviews and approves the Caisse's budgets and annual financial statements. The Board is required to assess the integrity of internal controls, disclosure controls and information systems, and to approve a financial disclosure policy. The Board also approves the Caisse's Annual Report.

The Board approves human resources policies, pay standards, pay scales and other employment conditions for Caisse officers and employees. It also determines pay standards, pay scales and other employment conditions for the President and Chief Executive Officer, according to parameters established by the government after consulting the Board. On the recommendation of the President and Chief Executive Officer, the Board appoints the members of senior management.

Working with the Governance and Ethics Committee, the Board develops and oversees implementation of the Caisse's rules, procedures and polices on corporate governance. It approves the codes of ethics and conduct that apply to Caisse Board members and to officers and employees of the Caisse and its subsidiaries. As required by law, the Board of Directors has formed an Audit Committee, a Human Resources Committee, a Governance and Ethics Committee, and a Risk Management Committee.

TABLE 91

DIRECTOR ATTENDANCE AT MEETINGS IN 2007

Director	Board of Directors		Audit Committee	Risk Management Committee		Human Resources Committee	Governance and Ethics Committee
	11 reg.	12 spec.	5 reg.	11 reg.	5 spec.	11 reg.	8 reg.
Yvan Allaire	9	9	–	9	4	–	8
Christiane Bergevin	3/4	4/4	1/1	–	–	–	–
Pierre Brunet	11	12	–	–	–	11	8
Claudette Carbonneau	6	8	2	–	–	–	–
Louise Charette	11	12	–	11	5	–	–
Steven Cummings	9	9	–	–	–	10	–
Alban D'Amours	8	7	–	9	5	–	–
Sylvie Dillard	11	8	–	–	–	11	–
Claude Garcia	11	10/10	5	4/4	0/0	–	–
A. Michel Lavigne	11	8/10	5	–	–	–	–
Henri Massé	10	9	–	8	5	–	–
Pierre Prémont	8/8	7/8	4/4	–	–	–	–
Henri-Paul Rousseau	11	12	–	11	4	–	–
Ouma Sananikone	3/4	3/4	–	–	–	–	2/3
Duc Vu	4/4	3/3	1/2	–	–	–	–
John T. Wall	3/4	1/3	–	–	–	4/4	3/3

COMPOSITION OF THE BOARD

The Caisse's Board of Directors consists of 15 members, which is the maximum allowed. Three members, John T. Wall, Duc Vu and Pierre Prémont, resigned as directors of the Caisse in 2007.

Two new members, Christiane Bergevin and Ouma Sananikone, joined the Board in 2007. The Québec government has also appointed two other directors, Jocelyne Dagenais and André Trudeau, who are scheduled to join the Board early in 2008.

The Board consists of its Chairman, the President and Chief Executive Officer, depositors' representatives and independent members. The Act respecting the Caisse specifies that at least two-thirds of the Board members, including the Chairman, be independent.

DIRECTOR ATTENDANCE AT BOARD AND COMMITTEE MEETINGS

Regular meetings of the Board and its committees are scheduled several months in advance. Special meetings are convened on short notice, as required. The Board has decided that, under certain circumstances, a director's repeated absence from three consecutive regular meetings may constitute a vacancy. This rule does not apply to special meetings.

The members of the Board justify their absences from a meeting of a committee or the Board to the Secretariat of the Caisse. In 2007, directors were not able to attend certain meeting of the committees or the Board for reasons that include identification of conflicts of interest, a change in the regular meeting schedule requested by the Caisse and health reasons.

INDEPENDENT BOARD MEMBER REMUNERATION

The remuneration of the Caisse's directors is determined by Order-in-Council 610-2006 of the Québec government. The Order-in-Council establishes the following remuneration for directors of the Caisse, excluding the Chairman of the Board and the President and Chief Executive Officer:

/ Annual remuneration for all independent directors, as defined by the Order-in-Council: $16,000;

/ Annual remuneration for a committee chairman: $5,000;

/ Attendance fee for each Board or committee meeting: $750;

/ Attendance fee for each special or brief Board or committee meeting held by conference call: $375.

This remuneration was increased by 2% on April 1, 2007. Only directors whose status is independent, as defined by the Order-in-Council, are entitled to remuneration.

The Board members are also entitled to reimbursement of their travel and living expenses, when applicable.

The total remuneration of the Caisse's directors amounted to $328,432, which can be broken down as shown in table 92.

TABLE 92

INDEPENDENT BOARD MEMBER REMUNERATION AS DEFINED BY ORDER-IN-COUNCIL 610-2006

Director	Annual remuneration	Remuneration as Committee Chairman	Attendance fees	Total remuneration ***
Yvan Allaire	$16,240	$5,075	$24,750	$46,065
Christiane Bergevin	$ 6,800	–	$ 4,590	$11,390
Claudette Carbonneau*	$16,240	–	$ 9,105	$25,345
Louise Charette	$16,240	–	$23,220	$39,460
Steven Cummings	$16,240	–	$16,733	$32,973
Alban D'Amours	$16,240	$5,075	$17,528	$38,843
Claude Garcia	$16,240	$5,075	$19,035	$40,350
A. Michel Lavigne	$16,240	–	$15,210	$31,450
Henri Massé*	$16,240	–	$19,043	$35,283
Ouma Sananikone	$ 6,800	–	$ 4,973	$11,773
John T. Wall**	$ 8,000	–	$ 7,500	$15,500

* The remuneration for these directors is not paid directly to them, in accordance with instructions they have given the Caisse.
** John T. Wall waived the fee to which he was entitled for services rendered to the Caisse as a director pursuant to Order-in-Council 610-2006.
*** The remuneration and the attendance fees were increased by 2% on April 1, 2007.

BOARD OF DIRECTORS' REPORT

REMUNERATION OF THE CHAIRMAN OF THE BOARD

The remuneration of the Chairman of the Board is not covered by Order-in-Council 610-2006. It has been set separately by the Québec government at $125,000 a year. The Chairman of the Board is also entitled to reimbursement of entertainment expenses related to the duties of the position, to an annual ceiling of $15,000.

BOARD ACTIVITY REPORT

COMPLIANCE WITH THE ACT RESPECTING THE CAISSE

Throughout the year, the Board ensured that the Caisse's operations complied with the Act and the relevant regulations. It received from an independent firm an audit report on the plan for implementation of the Act respecting the Caisse. In this way, the Board obtained assurance that the tasks and actions proposed for the implementation of each section of the Act respecting the Caisse are adequate and sufficient, and that each section of the Act is covered by the implementation plan.

STRATEGIC PLANNING AND BUSINESS PLANS

Each of the Caisse's business units and real estate subsidiaries presented its business plan to the Board, including objectives, challenges and related risks. The Board adopted the Caisse's business plan, asset allocation program and book of technology projects for the year.

The Board also received regular reports from senior management on the Caisse's business operations and market conditions and trends. At mid-year and year-end, assessments of the Caisse's operations and an analysis of the economic and business outlook were presented to the Board.

The Board members took part in the Journées Claude-Prieur, an annual information and discussion forum that brings together all Caisse stakeholders for a strategic look at subjects of concern to the business community. The theme for 2007, "Global Issues and the Caisse," was particularly relevant for the Board members; they see to the strategic orientations of the Caisse, which manages an increasingly diversified portfolio invested with a view to the long term in Québec and elsewhere.

More specifically, during the year the Board also considered the Caisse's contribution to Québec's economic development. Presentations were made to the Board on the Caisse's private equity investments in Québec, including its venture capital operations, and their impact on economic development. The Board was also informed of the launch of the Centre international sur la prospérité des entreprises du Québec.

To address the increasing complexity of the global real estate market and its constant evolution, the Board reviewed and approved a proposal to reorganize the Real Estate group. The reorganization will allow the group to pursue its growth and to act on market opportunities more easily.

Lastly, the Board received from senior management a report on the information requirements of the Caisse's stakeholders. It supported management in the establishment of an action plan that meets the various needs.

These activities gave the Board a detailed and comprehensive view of the organization's projects and objectives. As a result, the Board was able to oversee the Caisse's operations effectively and to take part constructively in its development. During the year, the Board also monitored the Strategic Plan 2006-2008 and assessed the progress made with its implementation.

FINANCIAL RESULTS, INTERNAL CONTROL AND MANAGEMENT SYSTEM

The Board received reports analyzing the returns of the Caisse's various business units. It also approved the press release announcing the Caisse's results.

After each Audit Committee meeting, the Board received the Committee's report on its activities, including monitoring of the quarterly financial statements, budgetary monitoring of operating expenses and monitoring of internal audit work. On the Audit Committee's recommendation, the Board approved the Caisse's annual financial statements and budget. The Board also approved the Annual Report.

Also on the recommendation of the Audit Committee, the Board adopted the principle of a new presentation of operating expenses and external management fees in the combined financial statements. Through the Audit Committee, the Board also ensured the integrity of all the controls applied to the various data used to establish the financial statements and the notes to the financial statements.

On the recommendation of the Audit Committee, the Board adopted a plan for optimal use of resources. In co-operation with the Audit Committee and the Risk Management Committee, the Board reviewed the integrity of internal controls and management systems.

In addition, with the assistance of the Audit Committee, the Board oversaw the application of the policies on financial certification and information disclosure. In line with industry best practices, these policies ensure that the information disclosed by the Caisse is transparent and accurate.

The program allows the President and Chief Executive Officer and the Executive Vice-President, Finance and Operations, to certify publicly that the disclosure controls and procedures are sufficient and effective, and that the internal controls for financial information are sufficient. The signed certificates can be found in the "Financial certification" section of the Annual Report.

The Board, on the recommendation of the Audit Committee, adopted a resolution on preparation for joint auditing of its books and accounts, as provided by the Québec government for state-owned enterprises.

After each Audit Committee meeting, the Board received an oral and written report on its activities. In this way, the Board ensured that the Audit Committee performed its functions adequately.

RISK MANAGEMENT

With assistance from the Risk Management Committee, the Board has identified the main risks to which the Caisse is exposed, and ensured effective oversight of them. In this respect, the Board received an oral and written report on the Committee's activities after each of its meetings.

On the Committee's recommendation, the Board approved the active risk objectives and limits and the absolute risk limits for the year. A new method of measuring potential liquidity and a risk limit for contracts or instruments of a financial nature were also approved. The Board also ensured the limits were respected.

Through the Committee, the Board monitored the integrated risk management policy. It approved changes to the investment policies of the specialized portfolios, on the Committee's recommendation. It also reviewed overruns and deviations in respect of the investment policies and authorized them as it saw fit.

Every quarter, after the review by the Risk Management Committee, the Board received a report on financial risk monitoring from the Executive Vice-Presidency responsible for risk management.

The Board supported the review of the business model used in the hedge funds unit, as proposed by senior management. It endorsed the proposed action plan to achieve a structure deemed optimal for hedge funds management.

The Board revised the delegations of authority applicable to all the Caisse's operations.

The Board studied investment proposals requiring its authorization and approved them as it saw fit. In each case, the Board considered an analysis of the risks associated with the investment and its impact on the risk level and concentration for the portfolio concerned. The Board did separate and regular monitoring of major investments with a substantial impact on the risk level and concentration of the specialized portfolios. The Board also ensured that a report on investments requiring authorization by Caisse senior management was submitted to the Risk Management Committee.

Senior management, in agreement with the Board, decided to give a consulting firm a mandate to review the Caisse's risk management practices and conduct benchmarking of the best practices in this area.

On the Committee's recommendation, the Board adopted a structure to monitor risks related to the repositioning of a real estate asset.

BOARD OF DIRECTORS' REPORT

Reorganization of the Caisse's management structure
To strengthen the structure and processes for operations management and to ensure better operational control, the Board, on the recommendation of senior management, approved a reorganization of the Caisse's management structure. All operations involving investment administration, accounting and production of financial statements were combined under the same Executive Vice-President. Emphasis was placed on computerization of the entire operational chain. Lastly, the institutional reporting and strategic planning functions were placed in the same Executive Vice-Presidency.

Asset-backed commercial paper
Within hours of the start of the crisis involving third-party asset-backed commercial paper (ABCP), the Board was informed by Caisse senior management of the events disrupting the market. Thereafter, at each regular Board meeting and the five special meetings held on this matter, senior management informed the Board of the action being taken to stem the crisis and then to resolve the problem facing the industry and the market. The Board supported senior management in its efforts to bring about the Montréal Accord, its negotiations within the Pan-Canadian Investors Committee to convert the third-party ABCP into longer-term securities and its overall management of the matter.

More specifically, the Board reviewed and discussed with senior management the measures taken to re-establish an appropriate level of liquid assets after the third-party ABCP froze up and to cope with any deterioration of market liquidity. On the recommendation of the Risk Management Committee, the Board also adopted a method for administrative treatment of third-party ABCP in respect of the specialized portfolios and their investment policies to allow specific monitoring of third-party ABCP as long as required. At the end of 2007, through its Audit Committee, the Board was informed of the proposed approach for the accounting treatment of third-party ABCP in the annual combined financial statements.

PERSONNEL MANAGEMENT AND SENIOR MANAGEMENT SUPERVISION

The Board approved the annual objectives of the Caisse's President and Chief Executive Officer. In addition, at its meetings, senior executives regularly made presentations on their area of activity.

With assistance from the Human Resources Committee, the Board reviewed the performance of the President and Chief Executive Officer on the basis of the objectives set at the start of the year. It also reviewed his evaluation of the performance of the senior officers. On a recommendation from the Human Resources Committee, the Board approved the salary conditions for Caisse employees and senior management for 2007 and the bonuses for 2006. With the Committee's assistance, the Board also reviewed the remuneration of the President and Chief Executive Officer in accordance with the parameters set by the Québec government for the remuneration and other working conditions for Henri-Paul Rousseau.

To fulfill the Caisse's objective of achieving recognition as a benchmark organization, a presentation was made to the Board on a new approach to management of human capital, and it adopted a program to optimize talent management. The program aims for strategic management of employees as front-line contributors to the fulfillment of the Caisse's business objectives. Under this program, the Board paid special attention to performance management in 2007. On the recommendation of the Human Resources Committee, it adopted changes to the long-term incentive plan. Having familiarized itself with an organizational survey of employees conducted in 2006, the Board ensured that senior management followed up on the comments received.

On the Committee's recommendation, the Board also changed the group-insurance premium sharing for employees in the technical support and professional groups and revised the perquisites plan.

With assistance from the Human Resources Committee, the Board adopted a business continuity plan in the event of an influenza pandemic. The plan takes into consideration the World Health Organization guidelines regarding the various stages of a pandemic. It specifies how the Caisse would operate if a crisis significantly reduced the number of employees able to work.

After each meeting of the Human Resources Committee, the Board received an oral and written report summarizing the members' discussions and presenting the Committee's recommendations.

CORPORATE GOVERNANCE

The Board received an oral and written report on the activities of the Governance and Ethics Committee after each of its meetings.

The Board revised and readopted the codes of ethics and professional conduct for directors and employees, as submitted by the Governance and Ethics Committee.

The Board revised and readopted the policy on the principles governing the exercise of voting rights in publicly traded companies. It received a detailed report on the Caisse's exercise of its voting rights for those companies in which it exercised such rights. It also received a report on the application of the policy on socially responsible investment for 2006 and 2007.

On the recommendation of the Governance and Ethics Committee, the Board recommended to the Québec government candidates for the position of director of the Caisse. It also revised and approved, as recommended by the Committee, the composition of the Board's Committees as well as the chairmanship of each Committee.

The Board received from the Governance and Ethics Committee a report on the declarations of director interests, pursuant to the provisions of the Code of Ethics and Professional Conduct for Directors.

The Board received a report from the Committee on the findings of the evaluation of the functioning of the Board of Directors. It also received the report of the Chairman of the Board on the evaluation of the directors. Presentations were made on proposed improvements to the Board's functioning and opportunities for ongoing training of the directors.

During regular Board meetings, presentations are made to the directors on various aspects of the Caisse's operations. In the past year, these presentations concerned such matters as private equity and its impact on Québec, leveraged buyouts, venture capital in Québec, the benchmark indexes for the investment policies of the specialized portfolios, hedge fund management, property development in emerging markets, governance of the Real Estate group and the impact of the U.S. subprime mortgage crisis on the real economy. Moreover, on the initiative of the Governance and Ethics Committee, the directors attended a training session on market risk oversight.

During each of these activities, key members of Caisse senior management were available to explain the various subjects, and sufficient time was allowed for a full and complete discussion.

REPORT OF THE AUDIT COMMITTEE

COMMITTEE MANDATE

Under the terms of its mandate, the Audit Committee ensures that the Caisse's financial statements accurately reflect its financial position. To that end, it reviews the financial statements in co-operation with the Auditor General of Québec and recommends them to the Board of Directors for approval.

The Audit Committee ensures that sufficient and effective internal control mechanisms are in place. It also ensures that a risk management process for the Caisse's operations and a plan for optimal use of resources are put in place. It also follows up on the plan.

The Committee reviews any activity that may adversely affect the sound financial position of the Caisse. It is obliged to inform the Board of Directors, in writing, of any management operation or practice that is unsound or that does not comply with the laws, regulations or policies that govern the operations of the Caisse.

Furthermore, the Committee appoints the Vice-President, Internal Audit, and approves the audit plan. It receives internal audit reports on such matters as the application of internal control mechanisms, a risk management process and a plan for optimal use of resources. The Committee also ensures that the organizational structure provides the Internal Audit team with the requisite independence in respect of Caisse senior management so that it can carry out its role effectively.

COMPOSITION OF THE COMMITTEE

The Audit Committee consists of four independent members:

Chairman: CLAUDE GARCIA
Members: CHRISTIANE BERGEVIN, A. MICHEL LAVIGNE and CLAUDETTE CARBONNEAU

In addition, the Chairman of the Board of Directors regularly attends the meetings of the Audit Committee.

The Chairman of the Audit Committee and its members do not sit on any other committee of the Caisse's Board of Directors. The Chairman of the Committee is a guest member at the meetings of the Risk Management Committee.

ACCOUNTING OR FINANCIAL EXPERTISE

All the members of the Audit Committee have the required experience and knowledge to understand the Committee's mandate and to properly fulfill their role.

In their education and careers, they have acquired the abilities and skills to read and understand the Caisse's financial statements. Moreover, the Audit Committee includes members with financial or accounting expertise.

REPORT OF THE AUDIT COMMITTEE ON THE PERFORMANCE OF ITS MANDATE AND THE PLAN FOR OPTIMAL USE OF RESOURCES

The Audit Committee met five times in 2007. Its main achievements are listed below.

RESPONSIBILITIES PERTAINING TO FINANCIAL INFORMATION

- The Committee reviewed the quarterly financial statements and budgetary monitoring of operating expenses.
- The Committee oversaw an independent valuation of the fair value of the Caisse's over-the-counter, private equity and real estate investments. The Committee received a report on the valuation process.
- The Committee reviewed the report on the financial certification process that enables the President and Chief Executive Officer and the Executive Vice-President, Finance and Operations, to certify publicly that the disclosure controls and procedures are sufficient and effective, and that the internal control over financial reporting is sufficient.
- The members of the Committee discussed with the Auditor General his audit plan for the Caisse's financial statements.
- The members discussed with the Auditor General and the Vice-President, Internal Audit, an inaccuracy in the notes to the 2006 combined financial statements involving the face value of derivative financial instruments. This inaccuracy is not significant because face value is not used to determine the fair value of assets and liabilities, or to establish returns and to measure market risk. The Committee nevertheless reviewed all the controls applied to the various data used to establish the combined financial statements and the related notes.
- The Committee reviewed the combined annual financial statements with the Auditor General and recommended them to the Board of Directors for approval. It also received the report to senior management issued by the Auditor General after his annual audit and discussed it with him.
- The members of the Committee met with the Auditor General twice in the absence of members of management.
- The Committee ensured that the industry's best practices were applied in respect of the criteria that determine the inclusion of property for the calculation of property under management.
- To ensure transparency, the Committee reviewed and recommended to the Board a new presentation of operating expenses and external management fees in the combined financial statements.
- The Committee considered the impact, on the Caisse and its subsidiaries, of the introduction of joint auditing of the books and accounts of state-owned enterprises, and recommended preparatory work to the Board.
- The Committee analyzed the impact on the Caisse's 2007 financial statements of the adoption of Sections 3855 and 3861 of the *CICA Handbook*, as well as the adoption of changes to certain accounting guidelines. the Committee also considered the future impact of the adoption of Sections 3862 and 3863 of the *CICA Handbook* and the application of international accounting standards.

Asset-backed commercial paper

At the end of 2007, a presentation was made to the Committee on the preliminary approach for year-end accounting treatment of third-party ABCP. In addition, early in 2008, the Committee held a special meeting exclusively on the determination of the fair value of the ABCP as at December 31, 2007.

REPORT OF THE AUDIT COMMITTEE

RESPONSIBILITIES PERTAINING TO INTERNAL AUDIT

/ The Committee reviewed the 2007 business plan of the Internal Audit Vice-Presidency, as well as the audit universe and the overall risk assessment for the year.

/ The Committee reviewed and adopted the internal audit plan for 2007, as well as a change to the annual audit cycle.

/ The members of the Committee discussed with the Vice-President, Internal Audit, the methodology used to audit resource optimization.

/ The members of the Committee considered the risk methodology and analysis used by the Internal Audit Vice-Presidency to establish the fraud risk profile for the Caisse; they also received a progress report on the establishment of this profile from the Vice-President, Internal Audit.

/ The Committee reviewed the terms of the agreement to extend the outsourcing contract covering a portion of Internal Audit's duties.

/ The Committee reviewed Internal Audit's quarterly activity reports.

/ The Committee ensured the Internal Audit team can act independently of Caisse management.

/ The members of the Committee met regularly with the Internal Audit Vice-Presidency after their meetings in the absence of members of management.

RESPONSIBILITIES PERTAINING TO INTERNAL CONTROLS AND THE PLAN FOR OPTIMAL USE OF RESOURCES

/ The members of the Committee discussed management's overall self-assessment of the effectiveness of the general control environment and oversight of fraud prevention and detection.

/ The members of the Committee reviewed the report on the monitoring and measurement activities carried out during the year under the financial and non-financial compliance programs.

/ The Committee reviewed and recommended that the Board of Directors approve a plan for optimal use of resources in 2007-2008; the Committee also monitored the plan.

/ Each quarter, the Committee reviewed the reports on compliance with the investment limits specified in the Act respecting the Caisse. The Committee also conducted regular monitoring of the investments made pursuant to the last paragraph of section 37.1 of the Act respecting the Caisse.

RESPONSIBILITIES PERTAINING TO RISK MANAGEMENT

The Audit Committee ensured, through the Risk Management Committee, implementation of a risk management process. To that end, it took the following initiatives:

/ The Committee received copies of the minutes of the meetings of the Risk Management Committee, as well as the annual reporting document on integrated risk management.

/ The Committee also received a copy of the certificates of compliance with the depositors' investment policies and the investment policies of the Caisse's specialized portfolios.

/ The Chairman of the Audit Committee sits, as a guest member, on the Risk Management Committee.

/ At the meetings of the Board of Directors, the members of the Audit Committee received the report provided by the Chairman of the Risk Management Committee after each meeting of that Committee.

Through the Risk Management Committee, the Audit Committee also ensured that the Caisse's risk management practices were revised and the best practices were benchmarked. A consulting firm was retained for that purpose.

The Committee and the Board were informed of the onset of the third-party ABCP crisis within hours. Prompt action by the Caisse enabled it to re-establish an appropriate level of liquid assets and to maintain a sound financial position. No other activity likely to affect the Caisse's sound financial position was brought to the Committee's attention by the Internal Auditor or by an officer in 2007.

After each of its meetings, the Committee provided an oral and written report to the Board of Directors on its activities.

In the exercise of their functions, the Board of Directors and its committees may retain the services of external experts. The Audit Committee did not use such services in 2007.

REPORT OF THE HUMAN RESOURCES COMMITTEE

COMMITTEE MANDATE

The mandate of the Human Resources Committee is to review guidelines and strategies for human resources management. The Committee reviews human resources policies, submits them to the Board for approval and ensures they are implemented.

The Committee develops the expertise and experience profile for the appointment of the President and Chief Executive Officer and submits it to the Board for approval. Using this profile, the Committee reviews potential candidates, as necessary, recommends the appointment of the President and Chief Executive Officer to the Board and evaluates his performance.

On the recommendation of the President and Chief Executive Officer, the Committee reviews the appointment and remuneration of the Caisse's senior officers, and submits this information to the Board for approval. The Committee also reviews the responsibilities of the members of senior management and ensures that succession-planning mechanisms are in place. It reviews the performance evaluation for senior officers, which is done by the President and Chief Executive Officer.

With respect to remuneration, the Committee receives information each year concerning remuneration on the Caisse's reference market. It reviews and submits to the Board a recommendation to establish the remuneration and other employment conditions of the President and Chief Executive Officer, within the parameters determined by the government after consultation with the Board. The Committee also reviews and submits to the Board the appropriate recommendations to establish the remuneration and other employment conditions of the other officers and employees of the Caisse.

Finally, in co-operation with the Governance and Ethics Committee, the Committee develops expertise and experience profiles for the appointment of independent Board members and submits the profiles to the Board for approval.

COMPOSITION OF THE COMMITTEE

The Human Resources Committee consists of three independent members:

Chairman: PIERRE BRUNET
Members: STEVEN M. CUMMINGS and SYLVIE DILLARD

John T. Wall resigned as a member of the Board of Directors of the Caisse in 2007 and therefore as a member of the Human Resources Committee. He was replaced by Sylvie Dillard.

REPORT OF THE HUMAN RESOURCES COMMITTEE

HUMAN RESOURCES COMMITTEE ACTIVITY REPORT

The Human Resources Committee met 11 times in 2007. In performing its mandate, the Committee carried out the following activities:

- The Committee reviewed the 2007 annual objectives of the President and Chief Executive Officer and submitted them to the Board of Directors for approval;
- The Committee reviewed the salary conditions of the Caisse's employees for 2007 and submitted them to the Board of Directors for approval. It carried out the same procedure to determine employee bonuses for the previous year;
- The Committee evaluated the performance of the President and Chief Executive Officer. It also reviewed the evaluations of the members of senior management, which were done by the President and Chief Executive Officer. On the basis of its review, the Committee recommended that the Board approve the 2007 salary increases, 2006 bonuses and other employment conditions for each member of senior management;
- The Committee recommended to the Board, for approval, the 2007 remuneration, 2006 bonuses and other employment conditions of the President and Chief Executive Officer, according to the parameters determined by the government;
- The Committee reviewed and recommended to the Board changes in 2007 to the perquisites program as well as to the sharing of group insurance premiums for employees in the technical support and professional groups;
- The Committee reviewed a new human resources management program and submitted it to the Board for approval. The program, which is designed to ensure strategic management of employees as significant contributors to achievement of the organization's objectives, included a redefinition of roles and responsibilities for team leaders and the Human Resources and Organizational Development Executive Vice-Presidency. The program has been divided into various projects. During the year, the Committee regularly received reports on implementation and development of the projects and the overall program;
- The members discussed a succession management program for the President and Chief Executive Officer and the members of the Executive Committee;
- The Committee reviewed and recommended to the Board a revised organizational structure to combine operations involving investment administration, accounting and production of the financial statements under the same Executive Vice-President. In addition, special emphasis was placed on computerization of the entire operational chain. Moreover, the institutional reporting and strategic planning functions were placed in the same Executive Vice-Presidency;
- The Committee reviewed and approved or, as the case may be, recommended that the Board approve, the hiring and the salary conditions for employees holding the position of Vice-President or a higher position;
- The members of the Committee reviewed and recommended to the Board a business continuity plan in the event of an influenza pandemic. The plan sets out how the organization would function if a large number of employees were absent because of illness;
- The Committee discussed the three-year human resources and organizational development plan, in terms of the new human resources management program and the Caisse's overall strategic planning exercise.

After each of its meetings, the Committee reported on its activities to the Board of Directors, orally and in writing.

In the exercise of their functions, the Board of Directors and its committees may employ the services of external experts. The Human Resources Committee did not use such services in 2007. In reviewing one file, it met with an external consultant hired by Caisse senior management.

REPORT OF THE HUMAN RESOURCES COMMITTEE ON THE REMUNERATION OF THE PRESIDENT AND CHIEF EXECUTIVE OFFICER AND THE FIVE MOST HIGHLY REMUNERATED OFFICERS REPORTING DIRECTLY TO HIM

The Caisse is a financial institution whose performance depends essentially on the talent of its employees. Its officers are responsible for putting in place and carrying out business plans in line with the Caisse's mission, which is "to receive moneys on deposit as provided by law and manage them with a view to achieving optimal return on capital within the framework of depositors' investment policies while at the same time contributing to Québec's economic development.»

The Caisse must rely on highly competent employees, whom it recruits on markets for occupations similar to its own. To attract such people, it must adopt a remuneration policy aligned with that of its reference market. This is the only way it can hope to attract, retain and motivate employees whose talent will enable it to achieve its business objectives in an environment where competition for talent is intense.

Long perceived as Québec's investment school, the Caisse has often lost talented employees recruited by other Canadian and foreign investment firms that can offer more advantageous compensation conditions than those in effect at the Caisse. To contain this trend, the Caisse has had to define programs enabling it to offer total remuneration that is competitive in its reference market, while respecting the remuneration parameters included in its Regulation respecting internal management.

Total remuneration is comprised of all aspects of an officer's remuneration and includes base salary, annual bonus, long-term incentive plan, benefits programs, pension plans and other remuneration.

The reference market for investment positions is defined as the Canadian institutional investment market and includes a representative sample of institutions, insurance companies, trust companies, pension funds, investment advisers, brokerage firms and fund managers or managers in similar industries. Reference may be made to the North American market for positions related to international investment. The reference market for non-investment positions is Québec, and includes the public sector.

The parameters incorporated into the Regulation respecting internal management specify that the maximum level of total remuneration for investment positions must fall within the upper decile (90th centile) of the reference market. It should be noted that these maximums are in fact rarely reached. The total remuneration for other positions must be at the third quartile (75th centile) of the reference market.

Although the Regulation respecting internal management enables the Caisse to go beyond those limits, its approach is generally, apart from certain exceptional cases, to offer remuneration near the median of the reference market when the Caisse's performance is average, and 75th-centile remuneration when its performance is superior.

To ensure that its remuneration programs are competitive and respect the parameters of the Regulation respecting internal management, the Caisse asks recognized firms to advise it on the analysis of its remuneration programs. An analysis is done regularly for many strategic positions in a data bank covering the reference market. The results are used to compare the direct remuneration offered at the Caisse for each matching position. The latest market analysis, completed early in 2008, shows that the direct remuneration offered to the Caisse's President and Chief Executive Officer and to the officers is within the parameters of the Regulation respecting internal management and the policy followed by the Caisse.

Under the *Act respecting the Caisse de dépôt et placement du Québec,* the Caisse must disclose the remuneration of the President and Chief Executive Officer and that of the five most highly remunerated officers reporting directly to him. The same disclosure is also required for wholly owned subsidiaries. CDP U.S. Inc. is a wholly owned subsidiary of the Caisse, and its President and Chief Executive Officer and officers are the same as those of the Caisse.

REMUNERATION OF THE PRESIDENT AND CHIEF EXECUTIVE OFFICER

In May 2006, after the amendments to the *Act respecting the Caisse de dépôt et placement du Québec* came into effect, the government established parameters, by order-in-council, to enable the Caisse's Board of Directors to determine the remuneration and the other employment conditions of the President and Chief Executive Officer. According to these parameters, the remuneration and the other employment conditions of the President and Chief Executive Officer must be between the median and the 75th centile of the reference market, depending on whether the Caisse's performance is average or superior. The reference market is defined as that of large Canadian pension funds. These parameters have been incorporated into the Caisse's Regulation respecting internal management.

Base salary

The base salary of the President and Chief Executive Officer was reviewed in 2007 by the Board of Directors to reflect market conditions, taking into account the experience, expertise and performance of the President and Chief Executive Officer.

Variable remuneration

The variable-remuneration programs of the President and Chief Executive Officer are based on the same rules as those of the Caisse's other officers. These programs represent a large portion of the total remuneration of the President and Chief Executive Officer and link his remuneration to achievement of performance objectives. These are the annual bonus program and the long-term incentive plan. To align the interests of the President and Chief Executive Officer with depositors' expectations, the Caisse gives considerable weight to long-term variable remuneration.

REPORT OF THE HUMAN RESOURCES COMMITTEE

Annual bonus program

At the start of each fiscal year, the Board of Directors sets the annual objectives of the President and Chief Executive Officer. At year-end, as a function of the results obtained, it approves his annual bonus.

The amount of the bonus depends on the degree to which the President and Chief Executive Officer achieves the annual objectives and the Caisse's performance. The bonus may reach a maximum of 30% of his base salary, as provided by Order-in-Council 607-2002.

The performance is based on achievement of value-added objectives over and above predetermined thresholds. The Caisse's performance is measured over a moving three-year period to evaluate the results on a medium-term horizon.

Long-term incentive plan (LTIP)

The long-term incentive plan (LTIP) represents the largest portion of the variable remuneration of the President and Chief Executive Officer and aligns his overall remuneration with the Caisse's long-term value-added objectives. The performance is based on achievement of value-added objectives over and above a benchmark index. The Caisse's performance is measured over a moving five-year period to evaluate the results on a horizon corresponding to a long-term investment philosophy.

Under the LTIP, each year the President and Chief Executive Officer receives a grant corresponding to a percentage of his base salary. A reserve is thereby created and it varies according to the Caisse's performance during a moving five-year period. The right to payment under the LTIP is vested gradually and on certain conditions, starting from the end of the third year of the first cycle.

The President and Chief Executive Officer may receive, on vesting and depending on the Caisse's performance, a basic payment corresponding to a percentage of the reserve accumulated as at December 31 of each year. The distribution percentage ranges from 0% to 40% of the reserve and is based on the Caisse's performance throughout the cycle measured. The Board of Directors may decide to increase the distribution percentage to recognize long-term performance and thus grant an additional payment under the LTIP. In this case, it ensures that the overall remuneration of the President and Chief Executive Officer remains within the parameters specified in the Regulation respecting internal management.

When the current long-term incentive plan was introduced in 2004, like the other officers who were members of the long-term incentive plan put in place just before the current program took effect, the President and Chief Executive Officer was given, in addition to the regular annual grant, a grant to take into account his waiver of the benefits he had been given under the long-term incentive plan in effect when he was hired in 2002. This additional grant has been included with the regular annual grants and is treated in the same way as the regular grants.

TABLE 93

PAYMENTS IN 2007 UNDER THE LONG-TERM INCENTIVE PLAN

Name and position	Payments
Henri-Paul Rousseau President and Chief Executive Officer	$1,131,950[1]

1 The President and Chief Executive Officer received a basic payment of $507,950 and an additional payment of $624,000 in 2007.

Other compensation

Other compensation refers to perquisites (a car and the related operating expenses, parking, health care and professional consulting fees), the Caisse's contribution to the group insurance plan in effect for management and any other amount paid to an officer under a special agreement.

Pension plans

The pension program for the President and Chief Executive Officer has two separate components, namely the Basic Plan and the Supplemental Pension Plan for Designated Officers (SPPDO).

Under these two plans, the President and Chief Executive Officer is entitled to receive, from the normal retirement age, a total annual pension equal to $35,000 plus an amount corresponding to his number of years or fraction of a year of membership in the pension plans multiplied by 8% of his eligible earnings, defined as being the average of the base salaries for the three years of membership during which his salary was highest. The maximum pension payable under the two plans may not exceed 60% of eligible earnings.

The value of the obligation in respect of benefits under the SPPDO is $3,377,900 as at December 31, 2007.

TABLE 94

EXAMPLES OF THE AMOUNT OF ANNUAL PENSION PAYABLE, ON RETIREMENT, BEFORE ANY REDUCTION, FOR YEARS OF MEMBERSHIP IN THE SUPPLEMENTAL PENSION PLAN OF THE PRESIDENT AND CHIEF EXECUTIVE OFFICER

	Years of membership					
Eligible earnings	5 years	6 years	7 years	8 years	9 years	10 years
$450,000	$215,000	$251,000	$270,000	$270,000	$270,000	$270,000
$475,000	$225,000	$263,000	$285,000	$285,000	$285,000	$285,000
$500,000	$235,000	$275,000	$300,000	$300,000	$300,000	$300,000
$525,000	$245,000	$287,000	$315,000	$315,000	$315,000	$315,000
$550,000	$255,000	$299,000	$330,000	$330,000	$330,000	$330,000

SUMMARY OF THE DIRECT REMUNERATION OF THE PRESIDENT AND CHIEF EXECUTIVE OFFICER AND THE AMOUNTS RECEIVED BY HIM FOR 2005, 2006 AND 2007

The President and Chief Executive Officer's total direct remuneration normally differs from the total amounts he receives for a given year (see table 95). To determine the value of his direct remuneration, the present value of the annual grant added to the LTIP reserve is usually entered in the column "Long-term incentive plan" rather than basic payments related to a possible distribution under the plan, since these basic payments come from grants awarded in previous years and disclosed in the year in which they are awarded. Moreover, a payment made in a given year may be higher or lower than the value of a grant, or even nil, depending on the Caisse's performance during a given cycle or whether the right to a payment is not yet vested or only partially vested.

Thus using the present value of the grant for the year under the LTIP rather than the payment received under previous grants, one takes into account what is actually granted as direct remuneration during a year. On this basis, the total value of direct remuneration is equal to $1,550,713. The difference between the amounts received in 2007 and the value of direct remuneration for 2007 corresponds to the difference between the value of the 2007 annual grant under the LTIP, namely $260,590, and the basic payment of $507,950 received in 2007 relative to previous grants. There was no payment under the LTIP in 2005, whereas the value attributed to the reserve was $245,575.

The value of the direct remuneration of the President and Chief Executive Officer for 2005 is higher than the total of the amounts he received for 2005, because the value of the annual grant is taken into account in the calculation of his direct remuneration, even though he was not yet entitled to a basic distribution in 2005. The total of the amounts he received in 2006 and 2007 is higher than the value of his direct remuneration, since the basic payment under the LTIP, as a result of previous grants, is greater than the value of a basic grant and takes into account the Caisse's superior performance during the cycle measured.

The methodology used to establish the direct remuneration of the President and Chief Executive Officer respects the rules generally recognized in this area and makes it possible to establish a comparison of the direct remuneration of the President and Chief Executive Officer with that of the reference market on a comparable basis.

REPORT OF THE HUMAN RESOURCES COMMITTEE

TABLE 95

SUMMARY OF THE DIRECT REMUNERATION OF THE PRESIDENT AND CHIEF EXECUTIVE OFFICER AND THE AMOUNTS HE RECEIVED FOR 2005, 2006 AND 2007

Henri-Paul Rousseau

President and Chief Executive Officer

2007	Base salary	Annual bonus program	Lont-term incentive plan[1]	Additional distribution under the long-term incentive plan[2]	Other compensation[3]	Total
Value of direct remuneration	$490,000	$125,000	$260,590	$624,000	$51,123	$1,550,713
Amounts received	$490,000	$125,000	$507,950	$624,000	$51,123	$1,798,073
2006						
Value of direct remuneration	$473,800	$142,140	$253,000	$728,310	$50,564	$1,647,814
Amounts received	$473,800	$142,140	$485,540	$728,310	$50,564	$1,880,354
2005						
Value of direct remuneration	$460,000	$138,000	$245,575	–	$50,159	$ 893,734
Amounts received	$460,000	$138,000	–	–	$50,159	$ 648,159

1 The annual grant included in the President and Chief Executive Officer's reserve under the LTIP and used to calculate the "Value of his direct remuneration" is equal to 55% of his base salary as at December 31 of the previous year. Under the rules of the LTIP, the President and Chief Executive Officer is entitled in 2007 to a basic payment of $507,950. This amount comes from the basic distribution percentage provided in the LTIP, which is determined on the basis of the Caisse's performance since the program took effect. This amount is entered in the column "Long-term incentive plan" in "Amounts received."

2 As provided under the LTIP, to recognize the Caisse's superior performance from 2004 to 2007, the Board of Directors has approved for 2007 an increase in the basic distribution percentage for the President and Chief Executive Officer, giving him an additional payment of $624,000. This additional payment must be added to the value of the direct remuneration of the President and Chief Executive Officer for the year in which it is provided.

3 Includes the amount of perquisites as well as the portion of group insurance premiums paid by the Caisse.

ANALYSIS OF THE REFERENCE MARKET FOR THE POSITION OF PRESIDENT AND CHIEF EXECUTIVE OFFICER

Comparison of the direct remuneration policy for the position of President and Chief Executive Officer in 2007 with the reference market for a superior performance

The analysis of the reference market for the position of President and Chief Executive Officer is based on a comparison group of eight large Canadian pension funds. The Caisse's Regulation respecting internal management requires that data reflecting the portrait of the reference market be compiled by means of a survey done by a recognized firm, and that they be administered and analyzed according to a methodology and rules generally recognized in this field. To establish the comparison of the President and Chief Executive Officer's remuneration with that of the reference market, Towers Perrin uses a recognized and reliable analytical method that ensures all the components of this remuneration are considered on a comparable basis.

Table 96 compares the President and Chief Executive Officer's potential direct remuneration for 2007 with that observed in the reference market for a superior performance. It presents, on a comparable basis, the direct remuneration paid at the 75th centile of the reference market and the direct remuneration payable at the Caisse under the various remuneration programs in effect, including the maximum additional payment that the Board of Directors may decide to make under the long-term incentive plan.

TABLEAU 96

COMPARISON OF THE CAISSE'S DIRECT REMUNERATION POLICY FOR THE POSITION OF PRESIDENT AND CHIEF EXECUTIVE OFFICER IN 2007 WITH THE REFERENCE MARKET FOR A SUPERIOR PERFORMANCE

Position	Reference market at 75th centile	Caisse policy for a superior performance	Ratio
	(A)	(B)	(B) / (A)
President and Chief Executive Officer	$2,070,000	$2,070,000	1.00

Source: Towers Perrin, Study of the President and Chief Executive Officer, Caisse de dépôt et placement du Québec, 2008.

OFFICERS' REMUNERATION

Officers' remuneration consists of the following components: base salary, annual bonus program, long-term incentive plan, other compensation and pension plans.

Base salary
An officer's base salary falls within a salary structure aligned with the reference market. It is determined on the basis of the level of responsibility related to the position as well as the officer's experience, expertise and performance.

Variable remuneration
The variable-remuneration programs in effect at the Caisse, described hereunder, are based on Canadian practices in this area. They represent a large portion of officers' total remuneration and link their remuneration to achievement of performance and value-added objectives by the various investment groups and to those of the Caisse generally. These are the annual bonus program and the long-term incentive plan. To align officers' interests with depositors' expectations, the Caisse gives considerable weight to officers' variable remuneration.

Annual bonus program
At the beginning of each year, the Board of Directors approves budgets, business plans and value-added performance objectives for each specialized portfolio in relation to predetermined thresholds and market indexes. At the end of the year, as a function of the results obtained, it approves the annual bonus for each Caisse officer reporting to the President and Chief Executive Officer.

The amount of the bonus depends on the performance of the Caisse, the performance of the investment groups, the positioning of the Caisse in relation to its peers and the individual performance of each officer.

The performance is based on achievement of value-added objectives over and above predetermined thresholds aligned with depositors' expectations. The performance of the specialized portfolios and that of the Caisse are measured over a moving three-year period (five years for the Private Equity and Real Estate portfolios) to evaluate the results on a medium-term horizon.

Long-term incentive plan (LTIP)
The long-term incentive plan (LTIP) represents a large portion of officers' remuneration and aligns their total remuneration with the Caisse's long-term value-added objectives. The performance is based on achievement of value-added objectives over and above a benchmark index, aligned with depositors' expectations. The Caisse's performance is measured on a moving five-year period so as to evaluate the results on a horizon that corresponds to a long-term investment philosophy. In the case of the Executive Vice-President, Real Estate, the performance used is that of the Real Estate group, as a result of his many years of service with the group's subsidiaries before he joined Caisse senior management.

Under the LTIP, each officer receives an annual grant corresponding to a percentage of his base salary. A reserve is thereby created and it varies according to the Caisse's performance during a moving five-year period. The right to payment under the LTIP is vested gradually and, on certain conditions, starting from the end of the third year of the first cycle. The officer may receive, on vesting and depending on the Caisse's performance, a basic payment corresponding to a percentage of the reserve accumulated as at December 31 of each year. The distribution percentage ranges from 0% to 40% of the reserve and is based on the Caisse's performance throughout the cycle measured. The Board of Directors may decide to increase the distribution percentage to recognize long-term performance and thus grant an additional payment under the LTIP. In this case, it ensures that the officer's overall remuneration remains within the parameters specified in the Regulation respecting internal management.

REPORT OF THE HUMAN RESOURCES COMMITTEE

When the current long-term incentive plan was introduced in 2004, the officers hired before January 1, 2004, were given, in addition to the regular annual grant, a additional grant to take into account their waiver of the benefits they had been given under the long-term incentive plan in effect when they were hired. This additional grant has been included with the regular annual grants and is treated in the same way as the regular grants.

TABLE 97

PAYMENTS IN 2007 UNDER THE LONG-TERM INCENTIVE PLAN

Name and position	Payments
Fernand Perreault Executive Vice-President, Real Estate	$496,820
Richard Guay Chief Investment Officer	$187,950
Normand Provost Executive Vice-President, Private Equity	$208,640
Ghislain Parent Executive Vice-President, Finance and Operations	$90,690
Suzanne Masson Executive Vice-President, Corporate Affairs and Secretary	$59,920

Other compensation

Other compensation refers to perquisites (a car and the related operating expenses, parking, health care and professional consulting fees), the Caisse's contribution to the group insurance plan in effect for management and any other amount paid to an officer under a special agreement.

Pension plans

The Caisse's pension plan for officers has three separate components, namely the Basic Plan, the Supplemental Pension Plan for Designated Officers (SPPDO) and the Supplemental Pension Plan for Employees (SPPE). The benefits under the supplemental plans vary according to the annual pension ceilings imposed by the Canada Revenue Agency. The vesting of certain benefits is based on the Caisse's performance.

Mr. Perreault is a member of SITQ's basic pension plan. The total benefits are essentially the same as those in effect at the Caisse.

The provisions of the SPPDO in respect of Ms. Masson differ from those of the other officers to take into account the fact that her basic pension plan is the Retirement Plan for Senior Officials (RPSO).

The value of the obligation under the SPPDO and the SPPE is $ 4,127,900 as at December 31, 2007.

TABLE 98

EXAMPLES OF THE MINIMUM ANNUAL AMOUNT OF PENSION PAYABLE, AT NORMAL RETIREMENT AGE, FOR AN OFFICER'S YEARS OF MEMBERSHIP IN THE SUPPLEMENTAL PENSION PLANS

	Years of membership				
Eligible earnings	10 years	15 years	20 years	25 years	30 years
$200,000	$40,000	$ 60,000	$ 80,000	$100,000	$120,000
$250,000	$50,000	$ 75,000	$100,000	$125,000	$150,000
$300,000	$60,000	$ 90,000	$120,000	$150,000	$180,000
$350,000	$70,000	$105,000	$140,000	$175,000	$210,000
$400,000	$80,000	$120,000	$160,000	$200,000	$240,000

Note: These pension amounts may vary depending on the Caisse's performance during the years in which the officer is a member of the Supplemental Pension Plan for Designated Officers and the Supplemental Pension Plan for Employees.

SUMMARY OF THE DIRECT REMUNERATION AND AMOUNTS RECEIVED BY THE FIVE MOST HIGHLY REMUNERATED OFFICERS REPORTING DIRECTLY TO THE PRESIDENT AND CHIEF EXECUTIVE OFFICER FOR 2005, 2006 AND 2007

The total direct remuneration of each of the aforementioned officers normally differs from the total amounts received for a given year (see table 99). To determine the value of direct remuneration, the present value of the annual grant added to the LTIP reserve is usually entered in the column "Long-term incentive plan" rather than basic payments related to a possible distribution under the plan, since these basic payments come from grants awarded in previous years and disclosed in the year in which they are awarded. Moreover, a payment made in a given year may be higher or lower than the value of a grant, or even nil, depending on the Caisse's performance during a given cycle or whether the right to a payment is not yet vested or only partially vested.

Thus using the present value of the grant for the year under the LTIP rather than the payment received under previous grants, one takes into account what is actually granted as direct remuneration during a year.

Accordingly, the value of the direct remuneration of each aforementioned officer for 2005 is higher than the total of the amounts received for 2005 since the value of the annual grant is taken into account in the calculation of direct remuneration, even though there was no payment in 2005 under the LTIP. The total of the amounts received in 2006 and 2007 is in certain cases higher than the value of the direct remuneration, since the basic payment under the LTIP, as a result of previous grants, is greater than the value of a basic grant and takes into account the Caisse's superior performance during the cycle measured. In other cases, the total of the amounts received is lower than the total direct remuneration, since certain officers' right to a distribution was only partially vested in 2006 and 2007.

The methodology used to establish the direct remuneration of the aforementioned officers respects the rules generally recognized in this area and makes it possible to establish a comparison of the direct remuneration of the officers with that of the reference market on a comparable basis.

TABLE 99

SUMMARY OF THE DIRECT REMUNERATION OF THE FIVE MOST HIGHLY REMUNERATED OFFICERS REPORTING DIRECTLY TO THE PRESIDENT AND CHIEF EXECUTIVE OFFICER AND THE AMOUNT THEY RECEIVED FOR 2005, 2006 AND 2007

	Base salary	Annual bonus program	Long-term incentive plan[1]	Other compensation[2]	Total
Fernand Perreault					
Executive Vice-President, Real Estate					
2007					
Value of direct remuneration	$395,000	$650,000	$144,375	$ 33,700	$1,223,075
Amounts received	$395,000	$650,000	$496,820	$33,700	$1,575,520
2006					
Value of direct remuneration	$385,000	$685,300	$139,050	$33,877	$1,243,227
Amounts received	$385,000	$685,300	$538,620	$33,877	$1,642,797
2005					
Value of direct remuneration	$370,800	$660,024	$135,000	$33,810	$1,199,634
Amounts received	$370,800	$660,024	–	$33,810	$1,064,634

REPORT OF THE HUMAN RESOURCES COMMITTEE

TABLE 99 (CONTINUED)

	Base salary	Annual bonus program	Long-term incentive plan[1]	Other compensation[2]	Total
Richard Guay Chief Investment Officer[3]					
2007					
Value of direct remuneration	$375,000	$450,000	$146,250	$38,981	$1,010,231
Amounts received	$375,000	$450,000	$187,950	$38,981	$1,051,931
2006					
Value of direct remuneration	$310,500	$581,750	$ 93,750	$36,666	$1,022,666
Amounts received	$310,500	$581,750	$159,720	$36,666	$1,088,636
2005					
Value of direct remuneration	$250,000	$320,000	$ 84,375	$31,882	$ 686,257
Amounts received	$250,000	$320,000	–	$31,882	$ 601,882
Normand Provost Executive Vice-President, Private Equity					
2007					
Value of direct remuneration	$315,000	$475,000	$112,500	$32,903	$ 935,403
Amounts received	$315,000	$475,000	$208,640	$32,903	$1,031,543
2006					
Value of direct remuneration	$300,000	$525,000	$108,750	$32,794	$ 966,544
Amounts received	$300,000	$525,000	$197,250	$32,794	$1,055,044
2005					
Value of direct remuneration	$290,000	$510,000	$103,125	$32,698	$ 935,823
Amounts received	$290,000	$510,000	–	$32,698	$ 832,698
Ghislain Parent Executive Vice-President, Finance and Operations					
2007					
Value of direct remuneration	$272,000	$320,000	$ 99,375	$30,012	$ 721,387
Amounts received	$272,000	$320,000	$ 90,690	$30,012	$ 712,702
2006					
Value of direct remuneration	$265,000	$210,000	$ 93,750	$30,094	$ 598,844
Amounts received	$265,000	$210,000	$ 81,450	$30,094	$ 586,544
2005					
Value of direct remuneration	$250,000	$196,000	$ 84,375	$29,682	$ 560,057
Amounts received	$250,000	$196,000	–	$29,682	$ 475,682
Suzanne Masson Executive Vice-President, Corporate Affairs and Secretary					
2007					
Value of direct remuneration	$257,500	$204,500	$ 94,688	$31,069	$ 587,757
Amounts received	$257,500	$204,500	$ 59,920	$31,069	$ 552,989
2006					
Value of direct remuneration	$252,500	$200,000	$ 91,875	$31,153	$ 575,528
Amounts received	$252,500	$200,000	$ 40,500	$31,153	$ 524,153
2005					
Value of direct remuneration	$234,131	$190,120	$ 80,625	$30,788	$ 535,664
Amounts received	$234,131	$190,120	–	$30,788	$ 455,039

1 Represents the annual grant added to the officer's reserve under the LTIP. For the Chief Investment Officer, the basic grant for 2007 is equal to 45% of base salary as at December 31, 2006, and 37.5% of base salary as at December 31 of the preceding year for 2005 and 2006. For the other officers, this grant is equal to 37.5% of the officer's base salary as at December 31 of the preceding year. Any future payment under the LTIP, whether a basic payment or any additional payment, will be determined on the basis of the variation in the reserve according to the Caisse's performance during the cycle measured.

2 Includes the amount of perquisites as well as the portion of group insurance premiums paid by the Caisse.

3 Richard Guay was promoted to Chief Investment Officer as of March 31, 2006.

COMPARISON OF THE CAISSE'S 2007 DIRECT REMUNERATION POLICY FOR THE POSITIONS HELD BY THE OFFICERS WITH THE REFERENCE MARKET FOR A SUPERIOR PERFORMANCE

Analysis of the reference market for senior management positions

The analysis of the reference market for senior management positions is based on a comparative group of about 60 companies that are part of the reference market specified in the Caisse's Regulation respecting internal management.

The Caisse's Regulation respecting internal management specifies that the data reflecting the reference-market profile be compiled by means of a survey, conducted by a recognized firm, and that they be administered and analyzed according to a methodology and rules generally recognized in this field.

Table 100 compares each officer's potential direct remuneration based on the Caisse policy for 2007 with that observed in the reference market for a superior performance. It presents, on a comparable basis, the direct remuneration paid at the 75th centile of the reference market and the direct remuneration payable at the Caisse under the various remuneration programs in effect for a superior performance.

TABLE 100

COMPARISON OF EACH OFFICER'S POTENTIAL DIRECT REMUNERATION BASED ON THE CAISSE POLICY FOR 2007 WITH THAT OBSERVED IN THE REFERENCE MARKET FOR A SUPERIOR PERFORMANCE

	Direct remuneration for 2007		
Positions	Reference market at 75th centile	Caisse policy for a superior performance	Ratio
	(A)	(B)	(B) / (A)
Executive Vice-President, Real Estate	$1,976,000	$1,432,000	0.72
Chief Investment Officer	$2,488,000	$1,418,000	0.57
Executive Vice-President, Private Equity	$1,600,000	$1,143,000	0.71
Executive Vice-President, Finance and Operations	$ 879,000	$ 719,000	0.82
Executive Vice-President, Corporate Affairs and Secretary	$ 862,000	$ 683,000	0.79

Source: Towers Perrin, Study of Direct Remuneration, Caisse de dépôt et placement du Québec, 2008.

REPORT OF THE GOVERNANCE AND ETHICS COMMITTEE

COMMITTEE MANDATE

The Governance and Ethics Committee assists the Board of Directors with the development and implementation of principles and practices that are conducive to a sound governance culture at the Caisse. To that end, the Committee establishes rules, structures and procedures to ensure the Board of Directors acts independently from management.

The Committee must propose an orientation program for new directors and an ongoing training program. In this way, it ensures that the directors have the knowledge they require to contribute positively to the work of the Board and its committees. The Committee makes recommendations to the Board regarding the composition and mandates of the Board's committees, as well as the composition and mandates of other committees that can facilitate the proper functioning of the Caisse. The Committee also proposes a procedure for evaluating the performance of the directors and the Board as a whole.

Together with the Human Resources Committee, the Governance and Ethics Committee submits to the Board the expertise and experience profile for the selection of independent members. It also proposes such candidates to the Québec government on the basis of the criteria established by law.

Finally, the Committee reviews regulations, codes and policies respecting the following matters and recommends them to the Board:

- The ethics and professional conduct of the directors, officers and employees of the Caisse, including control measures pertaining to the personal use of information received with respect to Caisse operations, and instances in which officers of the Caisse are obliged to declare their interests;
- Socially responsible investment;
- The governance principles that the Caisse intends to promote to the companies in which it exercises voting rights.

COMPOSITION OF THE COMMITTEE

The Governance and Ethics Committee consists of three independent members.

Chairman: YVAN ALLAIRE
Members: PIERRE BRUNET and OUMA SANANIKONE

In 2007, John T. Wall resigned as a member of the Board of Directors of the Caisse and in so doing as a member of the Governance and Ethics Committee. He was replaced by Ouma Sananikone.

REPORT OF THE GOVERNANCE AND ETHICS COMMITTEE

The Committee met eight times in 2007. To fulfill its mandate, the Committee focused mainly on the governance matters described below to enable the Caisse to meet the highest corporate governance standards.

RULES OF ETHICS AND PROFESSIONAL CONDUCT

/ The Committee revised the codes of ethics and professional conduct for directors, officers and employees of the Caisse, and submitted the codes to the Board of Directors for approval.

/ On behalf of the Board of Directors, the Committee received and reviewed the directors' declarations of interest pursuant to the Code of Ethics and Professional Conduct for Directors and forwarded the declarations to the competent authorities, as stipulated in the Act respecting the Caisse.

/ The Committee revised the list of transactions subject to the preauthorization process for directors' personal transactions and compared the process with the practices of its peers.

GOVERNANCE PRINCIPLES FOR THE EXERCISE OF VOTING RIGHTS

/ The Committee received a report on the exercise of the Caisse's voting rights for those companies in which it exercised such rights and discussed the principles governing such exercise in respect of various types of transaction carried out by the Caisse.

/ The Committee discussed the application of the policy on socially responsible investment in 2006 and 2007.

COMPOSITION OF THE COMMITTEES AND THE BOARD

/ The Committee reviewed the expertise and experience profile for independent Board members.

/ As part of the process to identify candidates for the position of director, the Committee considered the composition of the Board of Directors, the duration of the directors' mandates and the complementary competencies and expertise desired.

/ The Chairman of the Committee and the Chairman of the Board reviewed and selected candidates for appointment to the Board; the Committee recommended the candidates to the Board of Directors, which recommended them to the Québec government.

/ The Committee revised the composition of the Board's committees and the chairmanship of each committee, and submitted its recommendations to the Board of Directors.

FUNCTIONING OF THE COMMITTEES AND THE BOARD

/ The Committee supervised the performance evaluation of the Board, its Chairman and its committees. The Committee reported the results of this process to the Board of Directors. In addition, the Chairman of the Committee met with the Chairman of the Board to discuss the comments and suggestions made in the evaluation forms. Using the results of these evaluations, the Committee determined the improvements required to the Board's functioning, as well as opportunities for ongoing training of the directors.

/ The Committee proposed an orientation program for new directors and training program for directors.

/ The Committee received a report on the self-evaluation of the members of the Board conducted by the Chairman of the Board.

/ The Committee reviewed the manual for directors.

/ The Chairman of the Committee reported to the Board of Directors on the Committee's work after each of its meetings, orally and in writing.

/ The Committee proposed discussion sessions over the course of the year in the absence of senior management and ensured that the time allocated for these matters allowed for a full and complete discussion by the directors.

/ The Committee ensured that key members of Caisse senior management or external consultants were available to address the various subjects on the agenda of the Board's meetings, and that the time allocated for these matters allowed for a full and complete discussion.

/ The Committee ensured that the Board had all the relevant information and the time necessary to analyze the issues that the Caisse faces.

In the exercise of their functions, the Board of Directors and its committees may retain the services of external experts. To identify candidates for the position of director of the Caisse, the Governance and Ethics Committee used the services of a professional firm. In accordance with the terms of its mandate, the Committee advised the Chairman of the Board and the President and Chief Executive Officer in advance of the use of the services of an external expert, the mandate awarded and the estimated budget.

REPORT OF THE RISK MANAGEMENT COMMITTEE

The Board of Directors created the Risk Management Committee to assist the Audit Committee with its responsibility to put in place a risk management process.

COMMITTEE MANDATE

By establishing guidelines and policies for risk management, the Committee seeks to maintain an appropriate level of business, financial and operational risks. In carrying out its mandate, the Committee ensures that risks are clearly identified, and that a process is in place to manage them.

The Committee also reviews and submits to the Board for approval any transaction, investment or investment matter and any deviation from policies under the authority of the Board of Directors, notably with respect to their impact on the Caisse's overall portfolio or asset allocation.

In addition, it ensures that the Caisse fulfills its obligations to its depositors. To that end, it monitors compliance with the investment policy of each specialized portfolio and with each depositor's investment policy.

The Committee has implemented various mechanisms to provide the Audit Committee with assurance regarding the implementation of a risk management process.

COMPOSITION OF THE COMMITTEE

The Risk Management Committee consists of five members.

Chairman: ALBAN D'AMOURS
Members: HENRI MASSÉ, LOUISE CHARETTE, HENRI-PAUL ROUSSEAU and YVAN ALLAIRE
Guest member: CLAUDE GARCIA

Claude Garcia, the Chairman of the Audit Committee, attends the Committee's meetings as a guest member. The Chairman of the Board also regularly attends the Committee's meetings.

ACTIVITY REPORT OF THE RISK MANAGEMENT COMMITTEE

The Risk Management Committee held 11 regular meetings during the year, as well as five special meetings. Its main achievements for 2007 are described below.

RESPONSIBILITIES FOR ESTABLISHMENT OF RISK MANAGEMENT GUIDELINES AND POLICIES

- The Committee reviewed the investment policies of the Caisse's specialized portfolios and, as applicable, submitted changes to the Board of Directors for approval, notably to revise certain limits.
- The Committee reviewed overruns or deviations in respect of the investment policies and, as necessary, submitted them to the Board of Directors for approval.
- The Committee recommended to the Board of Directors a risk limit for contracts or instruments of a financial nature in accordance with the requirements of the *Regulation respecting the determination of instruments or contracts of a financial nature and the framework for their use*; it regularly received reports on compliance with this limit.
- The Committee reviewed and submitted to the Board for approval a new method to measure liquidity risk.
- The Committee reviewed and recommended to the Board of Directors a change in the Caisse's overall value-added objective, as well as the active risk limit.
- The Committee reviewed the report on the Caisse's integrated risk management, presenting the structures put in place at the Caisse to monitor risk; the Committee also received reports on compliance and internal control.
- The Committee analyzed the quarterly reports and the annual report on monitoring of changes in the Caisse's financial risks.
- The Committee received a report on the legal risk management process.
- At each meeting, the Committee members conferred with the Executive Vice-President responsible for risk management and the Chief Risk Officer to ensure the Caisse has a sufficient and effective process to manage significant risks.
- The Committee supported senior management as regards a revision of the Caisse's risk management practices as well as benchmarking of best practices in this area; a consulting firm was retained for that purpose.
- The Committee received a report on the directives put in place by Caisse senior management for risk oversight and management.

Asset-backed commercial paper

The Risk Management Committee considered specific matters related to third-party ABCP. In this regard, the Committee:

- Held a special meeting on third-party ABCP immediately after the onset of the events of August 2007 to define the situation with Caisse senior management;
- Reviewed and discussed with senior management the measures taken to re-establish an appropriate level of liquid assets after the third-party ABCP market seized up and to cope with any deterioration of liquidity in the market;
- Reviewed and recommended to the Board an administrative method for the treatment of third-party ABCP in respect of the specialized portfolios and their investment policies, to allow for specific monitoring of third-party ABCP as long as required.

RESPONSIBILITIES FOR INVESTMENT FILES

- The Committee reviewed 25 investment files under the authority of the Board of Directors and, as it saw fit, submitted them to the Board for approval. For each file, in addition to the analysis submitted by the unit proposing the transaction, the Committee reviewed the analysis of the project's risks, particularly its impact on the degree and concentration of risk for the specialized portfolio and the Caisse's overall portfolio.
- The Committee also discussed the analysis of the risk-return ratio for each investment file submitted to it.
- The Committee received the monitoring report on investment files that do not require Board approval and were authorized by Caisse senior management.
- The Committee reviewed and recommended to the Board a structure to monitor the risks related to repositioning of a real estate asset.
- The Committee reviewed the risks associated with investment in a new sector of activity.
- The Committee received monitoring reports on investment files analyzed by the managers of the Private Equity and Real Estate groups.
- The Committee regularly monitored certain major investments with a significant impact on the risk level and concentration of the specialized portfolios and the Caisse's overall portfolio.

RESPONSIBILITIES TOWARD DEPOSITORS

- The Committee reviewed the certificates of compliance with the depositors' investment policies and the investment policies of the specialized portfolios; it also discussed the depositors' expectations with respect to the establishment and monitoring of these policies.
- The Committee discussed the establishment of benchmark indexes for the investment policies of the specialized portfolios.
- Through the Executive Vice-President responsible for relations with the depositors, the Committee ensured that they were satisfied with the Caisse's reporting throughout the year and, more specifically in the second half of 2007, with its monitoring of the ABCP situation.

After each of its meetings, the Committee reported orally and in writing to the Board of Directors on its activities. It also submitted copies of its minutes to the Audit Committee and the Board of Directors.

In the exercise of their functions, the Board of Directors and its committees may retain the services of external experts. The Risk Management Committee did not use such services in 2007. It nevertheless supported senior management in its decision to retain a consulting firm for a review of the Caisse's risk management practices as well as benchmarking of best practices in this area.

GLOSSARY

ABSOLUTE RETURN

Return as measured by accounting records for any set of investments, including a depositor's portfolio or the Caisse's overall portfolio.

ABSOLUTE RISK

Expression of a portfolio's market volatility. This risk is used to measure, on the basis of the securities in the portfolio, the magnitude of a potential return deficit in comparison with the portfolio's expected return.

ACCUMULATION INVESTMENT

Investment that involves accumulating shares of a publicly traded company over the long term to acquire a strategic position so as to take advantage of value-enhancement opportunities.

ACTIVE MANAGEMENT

Portfolio management that differs from the benchmark index as a function of the manager's opinion regarding the market's future behaviour. The manager selects certain securities or sectors to create value added.

ACTIVE RISK

Volatility of value added, generally measured on the basis of the portfolio manager's current positions and the volatility and correlations of the return associated with these positions.

ACTUARIAL LIABILITIES

Total financial obligations that a pension or insurance plan must meet, given the nature of the plan and its commitments to participants.

ANALYTICAL APPROACH

Data-analysis method that is carried out in advance of an investment decision and takes into account quantitative and qualitative factors.

ANALYTICAL PLATFORM

Computer tools and infrastructure that enable managers to analyze current or potential investments quickly and easily.

ARBITRAGE

Transactions carried out to profit from a real or apparent imbalance between two securities or two baskets of securities. Arbitrage involves the purchase of a security or a basket of securities that appears to be undervalued and the sale of another that appears overvalued. Depending on the products available, transactions may be conducted in cash or on the futures market.

ASSET ALLOCATION (TOTAL)

Percentage of each asset class in a portfolio. It may refer to the portfolio's targeted or real asset allocation. The Caisse's total asset allocation results from the sum of the weighted asset allocation of each depositor.

ASSETS UNDER ADMINISTRATION

Assets for which the Caisse's subsidiaries and affiliates provide administrative services on behalf of the clients that own them. The companies that administer the assets are not involved in investment or disinvestment decisions and receive payment in the form of fees.

ASSETS UNDER MANAGEMENT

Assets that are owned by partner companies or clients and managed by a subsidiary or an affiliate of the Caisse. The units that manage the assets are involved in investment and disinvestment decisions and receive fees as payment for services rendered.

AUTHORIZED INVESTMENT

Investment whose parameters (financial vehicle, financing terms, cost, expected returns, etc.) have been examined and accepted by the competent authority.

BENCHMARK INDEX

Index used to measure the effect of all investors' decisions. It reflects the general market trend and allows comparison with the Caisse's portfolio management result for each specialized portfolio or management mandate. The market index may vary depending on the investment horizon and mandate. It can be a stock market index for an entire portfolio or a subindex that corresponds to a chosen investment universe for a management mandate.

BENCHMARKING

Ongoing process that a company uses to compare and evaluate itself against companies that have adopted exemplary business practices, in order to obtain information confirming its business practices or to adopt measures to improve them.

BOTTOM-UP ANALYSIS

Analytical process that examines specific elements before considering general elements. For example, a company is analyzed before the impact of sector concentration, national concentration and foreign currency exposure are examined. Top-down analysis functions in the opposite direction.

CAISSE'S OVERALL PORTFOLIO

Combination of the depositors' individual portfolios in proportion to the weight of each portfolio managed by the Caisse, whose overall return is the weighted average return on depositors' funds.

CAPITALIZATION RATE

Standardized and annualized net income of a property at a specific date, divided by the estimated value or selling price. This rate can be used to compare real estate property values.

CASH OPERATIONS

Operations allowing for the immediate purchase or sale of assets at a defined price according to market conditions.

CLIENT

Company to which the Caisse or one of its subsidiaries provides portfolio management or property administration services in consideration of fees.

COMMERCIAL MORTGAGE-BACKED SECURITIES (CMBS)

Securities issued in tranches, for which credit ratings are provided by a recognized rating agency. Each tranche has a different credit rating depending on the guarantee associated with it. The guarantee is based on a group of mortgages granted to borrowers and on the guarantee provided by the issuer of the security.

COMMERCIAL PAPER

Debt security issued by a corporation with a maturity usually shorter than or equal to one year. Commercial paper is to corporations as treasury bills are to governments.

COMMERCIAL REAL ESTATE COLLATERALIZED DEBT OBLIGATIONS (CRE CDOs)

Commercial real estate collateralized debt obligations (CRE CDOs) are securities issued on quoted markets and guaranteed by a range of commercial real estate financial assets. The securities are divided into tranches with various maturities, and the issuer uses the proceeds of the underlying financial assets to reimburse the ultimate investors. The cash flow from the underlying assets is used to guarantee the various tranches.

COMMODITIES

Products that trade in the form of futures contracts on specialized exchanges. Examples are crude oil, gold, wheat and coffee.

GLOSSARY

COMPLIANCE CERTIFICATE

Document certifying compliance with the laws, regulations and policies governing the operations of the Caisse.

COMPOSITE

Predetermined set of securities that have shared investment objectives or strategies. A composite may be based on one or more of the following criteria: currency, country, company size, product type, etc.

CONVENTIONAL INVESTMENT (REAL ESTATE)

High-quality real estate occupying a dominant position in its market. This type of real estate asset presents an attractive financial picture over the long term (five to 10 years) owing to its high level of stability and potential to weather a downturn in the real estate cycle. This type of property also has the following characteristics: a strategic location, a stable cash flow and a high current return similar to the return on fixed-income investments such as bonds and quality tenants.

CORE STRATEGY

Strategy whereby the geographic and sector allocation of investments resembles that of the benchmark index and the value added comes from security selection.

CORRELATION

Statistic that measures the variation in the return on one financial asset in relation to another. The correlation coefficient measures the degree of dependence between two variables to determine, for example, whether the returns on a mutual fund fluctuate as a function of the market or other categories of funds. Selection of funds with a low degree of correlation ensures effective portfolio diversification.

CREDIT DEFAULT SWAP

Credit swap in which the buyer makes periodic interest payments calculated on the basis of a fixed rate for the term of the contract, or any other equivalent amount, and the seller agrees to make a payment only upon the occurrence of a specified credit event.

CREDIT SPREAD

Difference in yields to maturity associated with issuers other than the government of the country concerned. In this sense, the spread between corporate bonds and Government of Canada bonds is a form of credit spread, as is the difference in yields to maturity between Ontario bonds and Government of Canada bonds, Québec bonds and Government of Canada bonds, etc.

DEPOSITOR

Public- or private-sector pension or insurance plan whose funds are managed by the Caisse.

DEPOSITOR'S BENCHMARK PORTFOLIO

Portfolio whose net asset allocation among the Caisse's specialized portfolios is agreed on with the depositor and corresponds to its needs and risk tolerance.

DEPOSITOR'S INVESTMENT POLICY

Framework that defines the management of funds entrusted to the Caisse by a depositor and includes a description of the particular plan and its characteristics, the benchmark portfolio, the market indexes, the value-added expectations and other technical aspects, such as frequency of meetings and reporting requirements.

DEPOSITORS' NET ASSETS OR DEPOSITORS' HOLDINGS

Fair market value of depositors' assets managed by the Caisse.

DEPOSITORS' TOTAL ASSETS

Depositors' net assets plus assets financed by borrowing as well as transactions being settled, other liabilities and non-controlling interests.

DERIVATIVES, DERIVATIVE PRODUCTS

Contracts, commitments or agreements for the sale or purchase of assets or the exchange of returns at a future date. These financial instruments are called derivatives because their value depends on an underlying asset.

There are three types of derivative products: futures and forward contracts, options and swaps.

DEVELOPMENT CAPITAL

Investment in a privately or publicly held company that wants to expand through internal growth or through an acquisition. Also includes a partial or total buyback of shares from a major shareholder allowing for a transfer of ownership.

DIRECTIONAL STRATEGY

Portfolio strategy based on the manager's ability to predict the direction of the price of a security or a group of securities.

DISCRETIONARY APPROACH

Management approach that analyzes various parameters of the market and uses quantitative models to develop a measure of certainty regarding what appears to be a market imbalance. The transaction is carried out only if the manager believes the expected return compensates for the risk associated with the transaction.

DURATION

Average maturity of cash flows (coupon or face value). The maturity of each cash flow is weighted by its present value. This duration is also known as Macaulay Duration.

EQUITY INTEREST

Private investment made with the intention of holding it over the long term. This type of investment usually takes the form of capital stock in a company, and often gives the investor some degree of influence on the direction of the company through a board seat or specified management rights. In the context of the specialized Investments and Infrastructures portfolio, equity interest refers to a portion of the capital stock of a listed company.

EVENT-DRIVEN STRATEGY

Portfolio management strategy designed to take advantage of an event that may take place on the market. For example, buying shares of a company after determining they have fallen too much in response to a lawsuit brought against the company.

EXPECTED RETURN

Benchmark return to which is added the target value added, in accordance with the depositor's investment policy.

EXTERNAL MANAGEMENT

Portfolio management performed by managers who are not employees of the Caisse, but who have been given a management mandate in consideration of fees.

FAIR VALUE

Value of an investment that reflects all fluctuations resulting from market behaviour or from any event that makes it possible to consider appreciation or depreciation. The expression "market value" is often used.

FOREIGN EXCHANGE OR CURRENCY RISK HEDGING

Financial operation whereby an investment is protected from fluctuations in the exchange rate between the currency in which the investment was made and the investor's original currency.

FUND OF HEDGE FUNDS

Fund whose component securities are hedge funds. This approach generally ensures diversification of styles, philosophies, risks, etc.

FUNDAMENTAL ANALYSIS

Analysis based on the intrinsic value of a company and its more or less long-term outlook. It evaluates the company's qualitative and quantitative elements to determine whether, at the current share price, it appears undervalued, overvalued or fully valued. This method is based solely on calculation of ratios, returns and other quantitative data.

GLOBAL MACRO

Investment operations based on an analysis of macroeconomic and political factors. The fund manager invests on the basis of the expected direction a market will take or the returns expected from one market compared with another. The manager can trade on interest rates, shares, currencies and commodities.

HEDGE FUND

Fund managed actively and dynamically with flexible, sophisticated strategies to produce high absolute returns. The strategies include leverage, derivatives, and long and short positions.

INDEPENDENT MEMBER

Under the *Act respecting the Caisse de dépôt et placement du Québec*, a member of the Board of Directors who has not had any ties with Caisse management, the government or the depositors for at least three years.

INDEXED MANAGEMENT

Management that obtains the same return as the benchmark index by an essentially identical matching of the portfolio.

INDIVIDUAL FUND

Fund attributed to a single depositor. An individual fund buys units from the Caisse's various specialized portfolios.

INFORMATION RATIO

Difference between the return earned by a portfolio manager and the return on the benchmark index, divided by active risk. Used to evaluate a manager's ability to produce value added on a constant basis. By industry standards, an information ratio greater than 0.5 for a given period is considered excellent.

INFRASTRUCTURE

Investment in a company created to manage a specific project, such as a highway or an airport. It is characterized by less risk than other private equity investments owing to the stable and predictable nature of the long-term revenues.

INVESTMENT HORIZON

Foreseeable period, accepted by the investor, that an investment may require before returning a profit. For example, the Private Equity group has an investment horizon of three to seven years.

INVESTMENT POLICY (SPECIALIZED PORTFOLIO)

Framework that defines the rationale for a specialized portfolio or management mandate, and includes management philosophy, portfolio structure, investment universe, market index, target returns and value-added objectives, as well as risk elements and their limits.

JOINT INVESTMENT

Investment made jointly with several investors who share the risk and return. The Caisse may partner with one or more investors or financial institutions to make an investment. At the Caisse, this term is also used for an investment made jointly with a fund. In this case, the Caisse is a passive investor.

LEVERAGE

Use of borrowed funds to finance an investment. The classic example is the purchase of a property on which there is a mortgage. Derivatives and commodities also use a leverage effect.

LEVERAGED BUYOUT

High-yield investment in a company that wants to acquire a majority position in a third company that is usually well established and profitable. With no capital provided, the acquisition is financed by an issue of high-yield bonds.

LIABILITIES

Primarily undertakings related to investments, such as mortgage loans, securities sold under repurchase agreements and securities sold short.

LIQUID INVESTMENT

Financial asset or security that can be easily turned into cash through a sale.

LONG-SHORT STRATEGY

Absolute return operation based on the opportunity for portfolio managers to buy or sell a security short on the basis of their opinion regarding the direction of its price. See also Long position and Short position.

LONG POSITION

Overweighting of a security, a sector or an asset class in comparison with the portfolio's benchmark index. See also Long-short strategy.

MANAGEMENT MANDATE

Smallest measurable group of securities managed by a portfolio manager.

GLOSSARY

MEZZANINE DEBT

Expression used in the context of private equity and real estate.

A hybrid financial vehicle whose return consists of a fixed portion of either cash or additional bonds and a variable portion consisting of warrants of a company. There is generally no repayment of capital during the term of the loan.

Financing that bridges the gap between traditional financing and equity capital.

There are many types of mezzanine loans based on the risks and barriers to investment. The two main types are called high-yield mezzanine and low-yield mezzanine. The first resembles equity while the second is closer to traditional real estate financing.

OPPORTUNISTIC APPROACH

Investment method intended to take advantage of opportunities on the market to earn a profit. The opportunities may be the result of events or circumstances related to a rising or falling market or to market inefficiency.

OPPORTUNISTIC STRATEGY (REAL ESTATE)

Investment method used for a real estate asset with attractive short- and medium-term growth potential, and with the prospect of a sale in the medium term. Investments can take the form of debt or equity. Given the generally low current return, the return expected from this type of investment derives largely from the expected increase in the value of the real estate asset.

OUTSTANDING

Publicly issued and sold.

OVERALL BENCHMARK PORTFOLIO

Weighted sum of the depositors' benchmark portfolios.

OVERWEIGHTING

Proportion greater than the benchmark weighting.

PARTNERSHIP

Co-operation agreement between two or more investors that provides for pooling of their expertise and sharing of the risk inherent in joint investments.

PRIVATE EQUITY

Investment made in a company on a private basis. Such transactions do not involve the usual mechanisms of the organized market.

PROPRIETARY RESEARCH

Exclusive research conducted by Caisse employees as opposed to research purchased from an external supplier.

PROVISION

Estimated amount by which the balance of an asset that has declined in value is reduced and which is recognized in a counterparty account of the asset in question.

QUARTILE

Ranking of the performance of investment managers. After the results of the managers in a sample have been ranked in descending order, they are divided into four equal groups. The first quartile corresponds to the best results in the sample, and the fourth quartile corresponds to the poorest results. The median is the mid-point of the sample and separates the top two quartiles from the bottom two.

REAL RETURN

Return obtained over and above inflation. If an investment generates 6% per annum (nominal return) and inflation is 2%, then the real return is 4%. This return is used particularly in actuarial studies.

REAL ESTATE INTERNAL RATE OF RETURN

Rate of return based on the present value of the expected cash flow of a property, including its final fair value.

RELATIVE RETURN

See Value added.

RISK PREMIUM

Additional return required in comparison with the return obtained on an investment considered risk free, such as Government of Canada treasury bills or bonds.

S&P/TSX CAPPED INDEX

Index consisting of the same securities as the S&P/TSX Index, with one additional restriction: no security can represent more than 10% of the market capitalization of the index.

SECURITIZATION

Operation whereby a company converts assets or debt securities (mortgage loans, for example) by combining and structuring them in the form of a new security, which it then offers to investors. In this way it can increase its return, increase its liquid assets, revenues, etc.

SENIOR DEBT

Security that entitles the holder to be reimbursed ahead of other holders of securities from the same issuer. The debt may take the form of a bond, loan, etc., and may be associated with specific collateral such as a building or machinery.

SHORT POSITION

Underweighting of a security, a sector or an asset class in comparison with the portfolio's benchmark index. See also Long-short strategy.

SPECIALIZED PORTFOLIO

Group of securities with a common set of characteristics (currency, product type, market behaviour, etc.). Specialized portfolios are similar to mutual funds.

STRUCTURED FINANCING (REAL ESTATE)

Process that involves grouping debt assets, dividing them into tranches according to the associated risk level and then selling the tranches to investors. On completion of the operation, the risk depends solely on the assets and is no longer related to the quality of the original underwriter.

SUBORDINATED DEBT

Debt security that ranks below another debt claim and entitles the holder to be reimbursed after other debt holders. See also Senior debt.

SUBSIDIARIES AND AFFILIATES

Operational management company that specializes in one or more niche markets and is part of the Real Estate group's network. Its mandate primarily involves asset management and real estate investment (investments in equity ownership or financing products) on behalf of the Caisse, its main real estate subsidiaries and third-party investors. The Caisse or one of its main real estate subsidiaries normally holds a minimum 50% interest, which entitles it to appoint representatives to the company's board of directors and to exercise control, under a unanimous shareholder agreement.

SYNDICATION

Operation whereby a group of financial institutions carry out an investment or provide financing.

SYSTEMATIC APPROACH

Approach based on mathematical models incorporating several variables that portfolio managers define according to their degree of reliability and relevance. The managers follow a set of decision-making rules and try not to be influenced by their current opinion.

TAKE A COMPANY PRIVATE

Action of purchasing the securities of a listed company and withdrawing them from an official market so that they can no longer be publicly traded.

TECHNICAL ANALYSIS

Analysis based on charts that map out the past behaviour of the market in an attempt to project its future behaviour. Technical analysis is used primarily to identify inflection points for a market or a company, to determine whether a recent trend is likely to continue in the longer term and to determine other trend indicators.

TIME-WEIGHTED RATE OF RETURN

Return based on the initial fair value for the period, the contributions weighted by the time of contribution and the final fair value. The return alone is considered without regard to the decision as to when to call sums of money or to entrust sums to be managed.

TOP-DOWN ANALYSIS

Analytical process that examines general elements before considering specific elements. For example, this approach considers foreign currency exposure, national concentration and sector concentration before analyzing the outlook for a company. Bottom-up analysis functions in the opposite direction.

TOTAL ASSETS

See Depositors' total assets.

TOTAL ASSET ALLOCATION

See Asset allocation.

TOTAL ASSETS UNDER MANAGEMENT

All assets managed by the Caisse, namely all depositors' assets as well as assets under management and assets under administration on behalf of clients.

UNDERLYING ASSET

Security or product to which another security, usually a derivative, is linked. For example, the barrel of oil is the product that underlies oil futures contracts. Similarly, the price of an ounce of gold affects the price of gold futures contracts.

UNDERWEIGHTING

Proportion lower than the benchmark weighting.

UNREALIZED DECREASE IN VALUE

See Unrealized increase (decrease) in value.

UNREALIZED INCREASE (DECREASE) IN VALUE

Increase (decrease) in the fair value of a security in relation to its acquisition cost. The increase or decrease in value is "materialized" when it is recognized in the accounting books at the time of sale. If it is not yet recognized, it is said to be unrealized.

VALUE ADDED

Difference between the absolute return on a portfolio and that of the benchmark index.

VALUE AT RISK (VaR)

Method of measuring the risk that could be incurred as a result of exposure to a financial risk in normal market conditions during a given period within a determined confidence interval.

VENTURE CAPITAL

Investments in start-ups or early-stage firms that are usually unlisted. The expected high return makes this type of investment attractive. The investment is usually made in stages, with additional financing provided only if the company achieves agreed-on objectives.

VOLATILITY

Variability of the fair value of a market or security subject to rapid price changes. Volatility is said to be high when prices or rates vary widely over a short period.

YIELD CURVE

Relationship among the yields of bonds of the same quality but different maturities, put into graphic form. A yield curve applies to a single market. For example, the Canada bond yield curve is different from the Québec bond yield curve. A curve is snapshot valid at a given time and changes along with the market.

TABLES AND FIGURES

GENERAL NOTES

1 / The Caisse's operations comply with the requirements of the *Act respecting the Caisse de dépôt et placement du Québec*[1] and with investment industry practices. Its financial statements are prepared in accordance with generally accepted accounting principles in Canada. Each year, the Auditor General of Québec, to the extent that he deems it appropriate, conducts the financial audit and ensures that the Caisse's operations comply with laws, regulations, policies and guidelines, and with the systems and procedures set up to control and protect its assets.

2 / The "Annual Report 2007 – Additional Information" is an integral part of the Annual Report 2007 and presents the Schedules (tables of returns) as at December 31, 2007, relating to the composites of the Caisse depositors' accounts. The Schedules and calculations have been audited as at December 31, 2007, by Deloitte & Touche LLP for compliance with the Global Investment Performance Standards (GIPS®).

3 / The returns on the specialized portfolios represent the time-weighted rate of return.

4 / The benchmark index for the investment groups is the weighted average of the benchmark indexes of the specialized portfolios they manage.

5 / Unless otherwise indicated, returns are presented before operating expenses and external management fees. They include the return on cash and cash equivalents and they take into account a foreign exchange hedging position. The return spreads related to the operating expenses of each specialized portfolio are presented in the Schedules of the "Annual Report 2007 – Additional Information."

6 / Certain returns are expressed in basis points (b.p.). One hundred basis points equal 1.0% and one basis point equals 0.01%.

7 / Unless otherwise indicated, all figures are given in Canadian dollars. The letters M and B used with dollar amounts designate millions and billions, respectively.

8 / Totals may vary because of rounding of figures.

9 / Many of the financial terms used in this Annual Report are defined in the "Glossary" section.

10 / Unless otherwise indicated, all data in the tables and figures are from studies made by the Caisse.

11 / The tables listing the top five or 10 investments present, in alphabetical order, cash positions based on information shown in tables 9, 10, 11 and 12 of the "Annual Report 2007 – Additional Information," net of short selling.

1 The *Act respecting the Caisse de dépôt et placement du Québec* is available on the Caisse's website.

CHANGES IN SPECIALIZED PORTFOLIO INDEXES OVER FIVE YEARS

Specialized portfolio	1 year	3 years	5 years
Short Term Investments (created July 1, 1998)	DEX 91-Day Canadian T-Bill		
Real Return Bonds (created January 1, 2004)	DEX Real Return Bond		
Bonds (created October 1, 1996)	DEX Universe Bond		
Long Term Bonds (created April 1, 2005)	DEX Long Term Government Bond		
Canadian Equity (created July 1, 19955)	S&P/TSX capped		
U.S. Equity (created April 1, 1994)	S&P 500 hedged		
Foreign Equity (created April 1, 1989)	MSCI – EAFE hedged		
Emerging Markets Equity (created January 1, 1995)	MSCI – EM		
Québec International (created July 1, 1999)	Index consists of 80% DEX Provincial Québec Subindex contracts and 20% DEX 91-Day Canadian T-Bill, plus a basket of equity futures		
Hedge Funds (created April 1, 2003)	CS/Tremont Hedge Fund Index (modified) since July 1, 2007, SC 91-Day Canadian T-Bill from January 1, 2006, to June 30, 2007, S&P Hedge Fund Index previously		
Commodities (created August 1, 2004)	Index based 80% on the Barclays U.S. Government Inflation-Linked Bond 1-10 Year Total Return Index and 20% on the Merrill Lynch 3-month U.S. Treasury Bill, plus the unhedged Dow Jones-AIG Commodity Excess Return Index		
Investments and Infrastructures (created July 1, 2003)	Index consists of 50% S&P/TSX capped, 25% S&P 500 hedged and 25% MSCI EAFE hedged since October 1, 2006, S&P/TSX adjusted previously		
Private Equity (created July 1, 2003)	Index consists of 60% S&P 500 hedged and 40% MSCI EAFE hedged since October 1, 2006, S&P 600 adjusted previously		
Real Estate Debt (created April 1, 1995)	Index consists of 90% DEX Universe Bond Index and 10% Lehman Brothers CMBS B hedged since October 1, 2005, SCU previously		
Real Estate (created October 1, 1985)	Aon – Real Estate		

Portfolio not yet created

The *Annual Report 2007* and the *Annual Report 2007 – Additional Information* are available on the website: www.lacaisse.com.

Information: 514 842-3261, info@lacaisse.com

Ce rapport annuel est aussi accessible en français sur le site Internet de la Caisse.

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