Pyramis Global Advisors
Investment Manager Review
December 9, 2009

EXECUTIVE SUMMARY

- On December 9, 2009 Martin Bélanger met with the following Pyramis Global Advisors professionals from 9:30 a.m. to 2:30 p.m. at their Smithfield, Rhode Island offices:
    - Rajan Burney, Vice President, Institutional Client Management
    - Adam Neal, Vice President, Institutional Sales
    - Michael Strong, Institutional Portfolio Manager
    - Chris Steward, Institutional Portfolio Manager
    - Brian Hoesly, Institutional Portfolio Manager
    - Cedric de la Chaise, Portfolio Manager, European Equities (by phone)
    - Eileen Dibb, Portfolio Manager, Japanese Equities
    - Peter Chiappinelli, Institutional Portfolio Manager
    - Mariana Egan, Portfolio Manager
- Ranked "Review" by Russell
- Pyramis is a solid organization with extensive resources
- Since our last review, there have been no changes in investment personnel directly involved with our portfolio
- The portfolio has underperformed its benchmark in 2009 mostly because value has outperformed growth
- The negative value added was caused by poor stock selection while regional allocation, especially in the Pacific Basin, has added value
- Since inception (on March 8, 2005), Pyramis has provided 1.39% of value added over the benchmark, annualized
- Year-to-date the European and Japanese portfolio managers have underperformed their benchmark, while the manager of Pacific Basin ex-Japan portfolio has significantly outperformed
- Their investment process has not materially changed in recent years and they have adequate risk controls in place
- Regarding environmental, social and governance issues, Fidelity looks very hard at company practices and they take into account any environmental, social and governance practices that would be detrimental to the company in the long run
- Cedric de la Chaise, the European portfolio manager, manages about $7 billion in assets; Fidelity believes that there's an additional $2 billion of extra capacity
- Fidelity doesn't have any compliance issues, all accounts are in compliance with the portfolio guidelines, they're not currently facing any major litigation, they have an adequate Code of Conduct and potential conflicts of interests have been disclosed

RECOMMENDATION

- Although Pyramis has not been able to add value in 2009, they have added 139 bps of value added since inception

- The regional portfolio managers have remained consistent to their style and the portfolio managers that we've met (Eileen Dibb for Japan and Cedric de la Chaise for Europe) have demonstrated good insights about their respective markets
- Pyramis has extensive resources from an investment research point of view and has the potential to generate value added in the future
- Despite the "Review" rating by Russell, I don't recommend making any changes to our relationship with Pyramis Global Advisors.

ORGANIZATION

- Pyramis Global Advisors is the institutional money management division of Fidelity Investments
- As of September 30, 2009 Pyramis Global Advisors had $7.9 billion in assets with Canadian clients and $148.5 billion worldwide
- Total assets managed by Fidelity Investments were $1.47 trillion as of September 30, 2009
- Western had $75.1 million in assets with Pyramis as of November, 2009
- Since the last review (in January 2009) Pyramis has had a net gain of 18 clients in Canada while it had a net loss of 116 clients worldwide
- Fidelity Investments is privately owned but key employees are eligible to a phantom share plan
- Sales people are paid a salary and earn a commission based on gross sales; they are also eligible for a long-term profit sharing plan that is linked to the financial health of the company
- Portfolio manager compensation is related to performance
    - Comparisons are made with the MSCI EAFE Index and a peer group universe
    - They measure performance over 1-year, 3-year and 5-year horizons
- Analysts performance is evaluated using quantitative metrics (~70%) and qualitative metrics (~30%)

INTERNATIONAL GROWTH MANDATE

Performance Analysis

As of October 31, 2009

	3-Month	**YTD**	**1-Year**	**3-Year**	**Since Inception (08/03/2005)**
Pyramis International Growth	7.88%	10.74%	11.96%	-4.70%	0.97%
MSCI EAFE	7.71%	11.13%	13.15%	-6.45%	-0.42%
Value Added	*0.17%*	*-0.39%*	*-1.19%*	*1.75%*	*1.39%*
Pyramis Europe	9.78%	11.43%	10.64%	-3.60%	1.21%
MSCI Europe	9.55%	13.47%	12.94%	-6.59%	-0.57%
Value Added	*0.23%*	*-2.04%*	*-2.30%*	*2.99%*	*1.78%*
Pyramis Japan	-1.20%	-7.46%	-0.94%	-13.76%	-4.68%
MSCI Japan	-0.78%	-7.04%	0.78%	-10.51%	-2.84%
Value Added	*0.42%*	*-0.42%*	*-1.72%*	*-3.25%*	*-1.84%*
Pyramis Pacific ex-Japan	*14.32%*	49.76%	49.55%	7.47%	11.25%
MSCI Pacific ex-Japan	14.26%	44.10%	46.27%	3.91%	6.28%
Value Added	*0.06%*	*5.66%*	*3.28%*	*3.56%*	*4.97%*

International Growth:

- The fund has 213 names:
  - 94 in Europe
  - 88 in Japan
  - 31 in Pacific ex-Japan
- The annual turnover as of September 30, 2009 was 75.33%
- The Institutional Portfolio Manager is Michael Strong
  - He’s responsible for regional allocation, complying with investment guidelines and cash management
- Stock selection is made by the regional portfolio managers:
  - Europe: Cedric de la Chaise (based in London, U.K.)
  - Japan: Eileen Dibb (based in Rhode Island)
  - Pacific: John Lo (based in Singapore)
- The Fund has outperformed its benchmark by 1.39% since inception
  - The European and Pacific regions have added value; Japan has detracted value
- For the first 10 months of 2009, the Fund’s return was 10.74% compared to 11.13% for the MSCI EAFE Index.

    - The Pacific Basin ex-Japan has added 566 bps, while Europe and Japan have detracted value
    - Value has outperformed growth so far in 2009
    - Regional allocation provided 0.54% of value added
    - Stock selection subtracted 1.69%; stock selection was negative in Europe (-1.53%) and Japan (-0.48%) but positive in the Pacific region (0.32%)
- The Fund uses the MSCI EAFE Index as a benchmark, not the MSCI EAFE Growth Index
    - Pyramis uses the traditional MSCI EAFE benchmark (renamed the MSCI EAFE Standard) which includes large cap and mid cap companies; there's also a new MSCI EAFE index (MSCI EAFE Investable Market Index) which also includes small cap stocks, in addition to mid cap and large cap stocks; there have been no changes to their strategy as a result of changes in the MSCI indices.
- The top contributors to the performance of the portfolio for the twelve-month period ending October 31, 2009 were:
    - Volkswagen AG, a German car manufacturer
    - Anheuser Busch InBev, a Belgian brewer
    - Tencent Holdings Ltd., a Chinese software manufacturer
- The top detractors were:
    - Unicredit SPA, an Italian bank
    - Fresenius SE, a provider of products and services for the healthcare industry
    - BNP Paribas, an French bank
- From a sector point of view, their overweight in Software & Services and in Insurance, as well as their underweight in Automobiles & Components have added the most value
- Their underweight in Banks, Capital Goods, as well as their overweight in Healthcare Equipment & Services have been detractors
- Normally they would expect that most of the return should be coming from stock selection (normally 75% to 85%); that has not been the case so far in 2009, regional allocation added about 0.54% while stock selection subtracted about 1.69% to performance
    - As of October 31, 2009 the portfolio was slightly overweight in the Pacific region and underweight in Europe and Japan

Europe:

- Cedric de la Chaise's investment philosophy involves looking for growth, quality and reasonable valuations
- Typical themes that he will try to exploit include cyclical recoveries
- Cedric de la Chaise manages $7 billion in European equities; Fidelity estimates that they have $2 billion of extra capacity
    - They determine capacity based on investment style, number of holdings and turnover
    - They focus on companies with $2 to $5 billion in market capitalization

- The European component accounted for 65.1% of the portfolio as of October 31, 2009, compared to 66.6% for the benchmark
- The portfolio had a 11.43% return for the first ten months of 2009, compared to 13.47% for the benchmark, for a negative value added of 2.04%
- Since inception the European component has had a positive value added (1.78%, annualized)
- The top contributors to the performance of the European portfolio in 2009 were:
    - Volkswagen AG, a German car manufacturer
    - Anheuser Busch InBev, a Belgian brewer
    - HSBC Holdings PLC, a U.K. bank
- The top detractors were:
    - Unicredit SPA, an Italian bank
    - Fresenius SE, a provider of products and services for the healthcare industry; the stock detracted value because it didn't go down as much during the fall; they have increased their position in the stock
    - BNP Paribas, an French bank
- From a sector point of view, their underweight in Automobiles & Components and Food Beverage & Tobacco, as well as their overweight in Insurance have added the most value
- Their underweight in Banks and Capital Goods, as well as their overweight in Diversified Financials have been detractors
    - Banks have detracted performance
    - Investing in ING Group was a mistake; they were forced to split the company; several constraints were imposed; they have kept the position because it still has value
    - Defensive stocks haven't done well in 2009; defensive stocks that didn't deliver were penalized even more
- Europe is an overleveraged market
- There is sovereign risk attached to peripheral European countries
- Core Europe is not as leveraged but is facing headwinds nevertheless
- Most companies have beaten their earnings expectations in 2009, although expectations were low
- European companies have restructured very aggressively as a result of the recession
- Unemployment is expected to increase in Europe in 2010
- Cedric mentioned that they misread the banks and industrials sectors
    - Pricing has resisted in the industrials sector
    - They have focused on high quality banks
- They have increased their underweight in industrials
- The European economy has stabilized and looks better; transfer payments have allowed consumers to maintain their consumption
- Valuations are decent and in line with historical averages
- Insurance companies have a low equity exposure, compared to historical averages
- Portfolio positioning:
    - Overweight in commercial and professional services, diversified financials, healthcare equipment and services (stable growth companies)

    - Serco Group plc (business services company) and Fresenius SE (healthcare equipment) are two overweight holdings
    - Underweight in capital goods and utilities
    - Banks discount the recovery the most, but the portfolio manager is cautious because of regulatory risk
    - Anheuser-Bush: invested in the company when they refinanced; they still own the stock but there’s less upside
    - No capacity reduction in the auto sector in Europe; they have a little position in BMW
    - They prefer to play the auto sector through Michelin
- Regarding the integration of environmental, social and governance factors, they have analysts reviewing them; they are aware of them and they will integrate them if they have a meaningful impact on the risk or the valuation of a company, but there are not too many businesses at risk.

Japan:

- The portfolio is managed by Eileen Dibb; she focuses on earnings growth
- From a valuation point of view, she looks at relative P/E ratios, although she switched to P/B ratios this year due to the lack of positive earnings for some companies
- She tries to incorporate the best ideas from analysts
- She monitors approximately 100-150 companies; they focus on about 35 stocks, the best growth stock over time; most of them will make it into the portfolio
- Eileen currently manages approximately $2 billion in Japanese equities
- The Japanese component accounted for 20.7% of the portfolio as of October 31, 2009, compared to 21.2% for the benchmark
- The portfolio had a -7.46% return for the first ten months of 2009, compared to -7.04% for the benchmark, for a value added of -0.42%
- Since inception the Japanese component has had a negative value added (-1.84%, annualized)
- The top contributors to the performance of the Japanese portfolio in 2009 were:
    - Sumitomo Electric Industries Ltd., a manufacturer of electric wires and cables
    - Kubota Corp., a manufacturer of machinery
    - Takeda Pharmaceutical, a global pharmaceutical company
- The top detractors were:
    - East Japan Railway Co., a passenger railway company
    - Tokio Marine Holdings Inc., property & casualty insurer and life insurer
    - Nomura Holdings Inc., a financial holding company; Nomura has raised capital twice, even though they didn’t need it
- From a sector point of view, their overweight in Pharmaceuticals, Biotech and Life Science, in Household & Personal Products and in Software & Services have added the most value
- Their underweight in Materials and Automobiles & Components, as well as their overweight in Telecommunication Services have been detractors
- We may have a big rally in Japan next year; earnings are rebounding but are not reflected in stock prices

- Some companies are raising capital, even though they don't need it
- Financial sector:
    - Banks have been a problem; some have raised capital even though they didn't need it
    - They have bought regional banks
    - They have bought some consumer oriented banks; they should benefit from the rebound in consumer spending
    - They believe that banks are undervalued
- Current portfolio positioning:
    - Their top active position is Shionogi & Co.; they own the Crestor franchise; Crestor is a drug that lowers cholesterol; they expect revenue growth of 10-15% and earnings growth of 20-25% in the near future; the stock is currently correcting
    - Industrials companies still haven't bounced back yet
- Amortization of goodwill is the most significant accounting difference between Japan and North America; they are currently looking at the conversion to the new International Financial Reporting Standards and their implications
- Regarding the integration of environmental, social and governance factors, they are active talking to management about it; they are not that many environmental issues in Japan as the country is at the forefront in this area; governance is a bigger issue
- ESG factors don't have a big impact on the portfolio, beside companies that Fidelity doesn't allow because of legal issues in the U.S. (e.g. on-line gaming companies)

Pacific Basin ex-Japan:

- Because of the small weight in the MSCI EAFE Index (currently 12.2% of the Index), the Pacific Basin ex-Japan component of the portfolio is managed more aggressively than the other two components, i.e. the number positions is smaller (about 20-30) and the active positions are larger
- The expected tracking error of the sub-portfolio is 8% to 10%
- The Pacific Basin ex-Japan component accounted for 14.2% of the portfolio as of October 31, 2009, compared to 12.2% for the benchmark
- The portfolio had a 49.76% return for the first ten months of 2009, compared to 44.10% for the benchmark, for a value added of 5.66%
- Since inception the Pacific Basin ex-Japan component has had a positive value added (4.97%, annualized)
- The top contributors to the performance of the Pacific Basin ex-Japan portfolio for the first ten months of 2009 are:
    - Tencent Holdings Ltd., a Chinese software manufacturer
    - Lion Nathan Ltd., an Australian producer of beer and wine products
    - Westfield Group (Stapled Unit), an Australian real estate company managing shopping centres
- The top detractors were:
    - Westpac Banking Group, an Australian bank
    - Telstra Corp. Ltd., an Australian telecommunications and media company
    - Raffles Education Corp. Ltd., a Singapore-based provider of private education

- From a sector point of view, their overweight in Software & Services and in Food Beverage & Tobacco, as well as their underweight in Utilities have added the most value; their overweight in retailing is based on the fact that Asian consumers are less leveraged
- Their underweight in Banks (they were underweight when the market rebounded), as well as their overweight in Consumer Services and Retailing have been detractors

Investment Personnel:

- Since our last review, there have been no changes to the personnel directly involved with the management of our portfolio
- We met for the first time with Eileen Dibb, the new portfolio manager of Japanese equities, and she has demonstrated a reasonably strong knowledge of the Japanese markets and the companies in her portfolio
- We met again with Cedric de la Chaise, the European equity manager. He has generated good performance since he has started managing our portfolio and he again appeared knowledgeable and insightful about the thematic impacting European equities and about the securities in our portfolio
- Michael Strong, Brian Hoesly and Chris Steward have remained in place as lead portfolio managers of the strategy
- The firm has 409 investment professionals worldwide, down from 439 when we held our last review; reductions occurred outside North America (mostly in London) during the fourth quarter of 2008 and reductions in 2009 occurred primarily in the Boston office; staff reductions were split almost evenly between Europe and North American, while the Japanese and Pacific ex-Japan regions have seen an increase in staff level
- The only portfolio manager that we haven't met so far is John Lo, who manages the Pacific ex-Japan region. We hope to meet with him at the next review. He has generated strong performance since the inception of our portfolio.
- The structure they have in place (Michael strong as lead portfolio manager who makes the regional decision and the regional portfolios managed by dedicated portfolio managers using the research produced by local analysts) seems to be working for them; with a large pool of analysts located all over the world, Fidelity has a strong position compared to its competitors

Investment Process:

- Process hasn't changed: bottom-up growth
- The strategy focuses on companies with above-average earnings growth combined with attractive relative valuations. Companies that possess fundamental strength in technology or business \ strategy that provide a competitive advantage are emphasized.
- Fidelity leverages its global research team to assess a company's competitive position.
- Buy criteria:
    - Attractive business model
    - Favorable secular trends
    - Positive earnings surprises

    - Reasonable valuations
- Sell criteria:
    - Deterioration in company fundamentals
    - Excessive price appreciation
- Environmental, Social and Governance Factors:
    - Regarding the integration of environmental, social and governance factors, Fidelity, and by extension Pyramis, believes that high standards of corporate social responsibility ("CSR") will generally make good business sense and have the potential to protect and enhance investment returns. Their investment process considers social, environmental and ethical issues into account when these have a material impact on either investment risk or return. They believe that social, environmental, and ethical best practices should be encouraged provided it enhances long term financial return.
    - They do not screen out companies from our investment universe purely on the grounds of poor social, environmental, or ethical performance but rather adopt a positive engagement approach whereby they discuss these issues with the management of the companies in which they invest on behalf of their clients. They use the information gathered during these meetings both to inform their investment decisions and to encourage company management to improve procedures and attitudes. They believe that this is one effective way to improve the attitude of business towards CSR.

Risk Controls:
- Risk controls are Michael Strong's responsibility
    - Regional weights: Benchmark weight +/- 5%
    - Country weights: Benchmark weight +/- 5%
    - Industry group weights: Benchmark weight +/- 5%
    - Security weights: Benchmark weight +/- 3%
    - Market capitalization: Benchmark weighted average +/- 15%
- The portfolio manager has access to a web-based application that tracks several metrics, such as beta and tracking error
- The macro economic environment is also taken into consideration
- They target the stock specific risk to account for about $66^{2/3}$% to 70% of total risk and the tracking error to be between 2% and 4%
- They monitor their exposure to growth and value and to dividend and momentum

Capacity:
- Russell raised some issues about capacity, more specifically that the assets managed by Cedric de la Chaise were too large for him to generate some value added
- Cedric de la Chaise manages $7 billion in European equities; Fidelity estimates that they have $2 billion of extra capacity
    - They determine capacity based on investment style, number of holdings and turnover
    - They focus on companies with $2 to $5 billion in market capitalization

Trading:

- Fidelity provided a visit of the trading floor
- There haven't been any issues with liquidity when doing monthly redemptions; they keep 1-2% of the portfolio invested in cash for redemption purposes

COMPLIANCE

- Pyramis is in compliance with the investment objective, investment guidelines and investment constraints of our mandate
- Due to its size, Fidelity faces litigation from time to time. All litigation has been disclosed in applicable regulatory filings and Fidelity doesn't expect any of the proceedings to have a negative material impact on its operations.
- There were no issues raised by regulators which would have a material effect on the relationship between Fidelity Canada and UWO
- Pyramis has an adequate Code of Ethics "Rules of Employee Investing" that employees have comply with
- To the best of its knowledge, Pyramis has disclosed any conflict of interest or potential conflict of interest involving Pyramis or key investment personnel

LIFECYCLE FUNDS

- During the last portion of the review, I met with Peter Chiappinelli, Senior Vice President, Asset Allocation Strategist and Mariana Egan, Vice President and Portfolio Manager, to discuss their ClearPath Institutional Lifecycle Funds.
- Pyramis (and Fidelity) is a leader in lifecycle funds with more than $100 billion in assets under management worldwide, including $1.7 billion in Canada
- The firm has dedicated resources and has conducted extensive research to come up with the optimal design for their lifecycle funds:
    - They integrate academic theory and real participant behaviours
    - They have three distinct phases: accumulation, retirement and post-retirement (10 years after retirement)
    - Each phase has its own specific objectives
    - The objectives in the accumulation phase are to provide: 1) an 80% replacement ratio, 2) a final dollar amount equivalent to 10 times the member final salary and 3) a 5% sustainable withdrawal rate
    - The replacement ratio is integrated with public pensions available in Canada
    - The optimal asset mix during the accumulation phase was obtained through stochastic simulation and by stress testing the equity return assumptions and by assuming various equity shocks throughout the accumulation phase
    - The optimal asset mix in retirement and in post-retirement was obtained by varying the withdrawal rate, by assuming a large equity shock at retirement and by assuming that the member would live to age 92
    - All these steps lead to a robust glidepath that maximize the member's retirement income

- Pyramis provides management of the lifecycle through four asset classes: Canadian equities, foreign equities, fixed income and alternatives (real estate, currency strategy)
- Unfortunately, Pyramis doesn't offer the possibility to customize their lifecycle funds by including other managers who could provide additional diversification and also passive investing
- In conclusion, Pyramis (and Fidelity) is the world leader in lifecycle funds. They have conducted extensive research to develop their glidepath and own substantial data on participant behaviour
- Although their lack of flexibility regarding customization is a downside, we should continue to tap their extensive knowledge of the market to come up with the best solutions for our members