INFLATION-SENSITIVE INVESTMENTS

DESCRIPTION

The Inflation-Sensitive Investments asset class consists of three portfolios: Real Estate, Infrastructure and Real Return Bonds. The investment income generated by these assets is generally inflation-linked so as to partially hedge the inflation risk associated with the liabilities of many Caisse clients.

The Real Estate and Infrastructure portfolios, which represent $33 billion of net assets, are actively managed based on an absolute-return approach. The Real Return Bonds portfolio, with $1 billion of net assets, is indexed.

MARKET CONTEXT

The economic recovery over the past four years in the United States, combined with falling interest rates, enabled this asset class to generate high returns. Moreover, strong demand from institutional investors for real estate and infrastructure assets continues to put constant upward pressure on prices. These less-liquid assets are popular because they offer an excellent risk-return profile and a high, stable current yield, while enabling managers to diversify risk within an overall portfolio.

In the case of real estate, the liquidity arising from the accommodative policies adopted by central banks reduced the risk premiums associated with certain markets. In addition, shopping centres and office buildings generated a sound current yield in Canada and the United States, mainly due to strong rental revenues.

With more pronounced volatility in the equity markets and low yields expected in the bond markets, investor appetite for infrastructure was stronger than ever. The objective of governments to reduce their budget deficits also substantially increased the number of infrastructure transactions carried out by private investors.

HIGHLIGHTS OF RESULTS

	At Dec. 31, 2014	4 years			1 year		
Specialized portfolio	Net assets ($ billions)	Net investment results ($ millions)	Return (%)	Index (%)	Net investment results ($ millions)	Return (%)	Index (%)
Real Estate	22.9	8,814	12.1	13.8	2,114	9.9	11.1
Infrastructure	10.1	3,344	13.8	17.9	1,149	13.2	21.5
Real Return Bonds	1.0	192	4.6	4.6	125	13.2	13.2
Inflation-Sensitive Investments	34.0	12,350	12.1	14.5	3,388	11.0	13.9

The Inflation-Sensitive Investments asset class recorded the highest absolute results for la Caisse over the past four years. During that period, it generated $12.4 billion of net investment results and an annualized return of 12.1%. The 2014 return for this asset class was 11%.

REAL ESTATE

Over four years, the Real Estate portfolio generated an annualized return of 12.1% and $8.8 billion of net investment results. For 2014, the portfolio had a 9.9% return. These returns exceed the long-term target.

During the period, the portfolio benefited from significant increases in the value of its shopping centres and office buildings in North America. In addition, these properties generated strong rental revenues as a result of their high occupancy rates.

The benchmark index returned 13.8% over four years mainly because it is not affected by the weak performance of the hotel sector.

In 2014, la Caisse’s real estate subsidiary Ivanhoé Cambridge continued the strategic repositioning of its portfolio, carrying out a record volume of transactions, with $5.1 billion in acquisitions and $8.6 billion in dispositions.

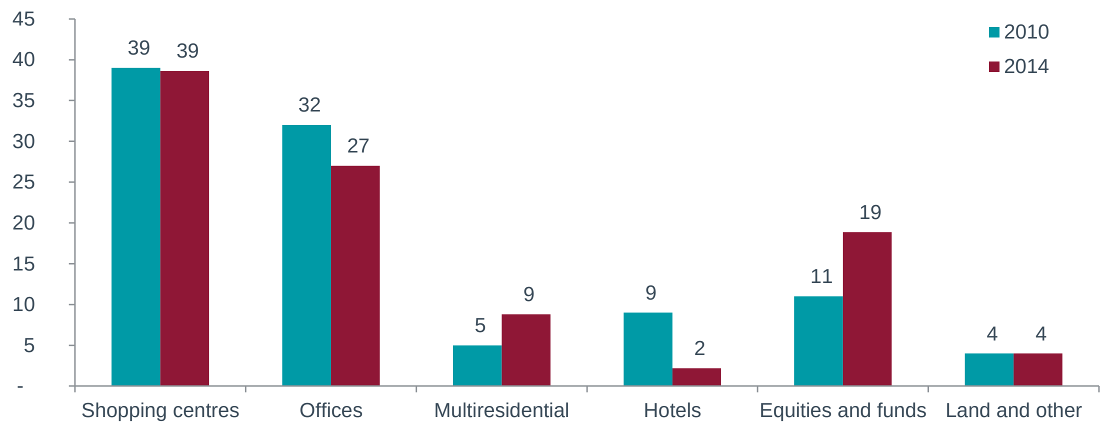
- In the United States, Ivanhoé Cambridge invested more than US$630 million in its office building platform, acquiring high-quality buildings in the heart of Manhattan, Seattle and Denver. In San Francisco, with its new partner Veritas, it acquired its first 580 multiresidential units in the heart of the city. With the objective of enlarging its footprint in the United States, Ivanhoé Cambridge recently announced, along with its partner Callahan Capital Properties, the acquisition of Three Bryant Park in Midtown Manhattan in New York City, for US$2.2 billion.

- In Europe, along with Blackstone, Ivanhoé Cambridge became the largest shareholder of Gecina, France’s third-largest publicly traded real estate company. In addition, five acquisitions in key markets doubled the value of the logistics and warehouse company P3 Logistic Parks, owned in partnership with TPG.

– In Québec, Ivanhoé Cambridge concluded a co-ownership agreement with Manulife to build, own and operate an office building at 900 de Maisonneuve Ouest, in downtown Montréal. In 2014, it also completed the historic restoration and renovation of the Fairmont Le Château Frontenac.

– In line with its strategy, Ivanhoé Cambridge divested itself of properties that no longer fit its quality profile or its target sectors and markets. As a result, it disposed of 21 hotels, including a portfolio of 18 hotels in Europe, as well as buildings in Munich and Frankfurt, markets where it does not intend to build critical mass. It also sold a portfolio of retail and office buildings in Canada for a total of $1.5 billion.

Sectoral breakdown of the Real Estate portfolio
(as a % of total assets)



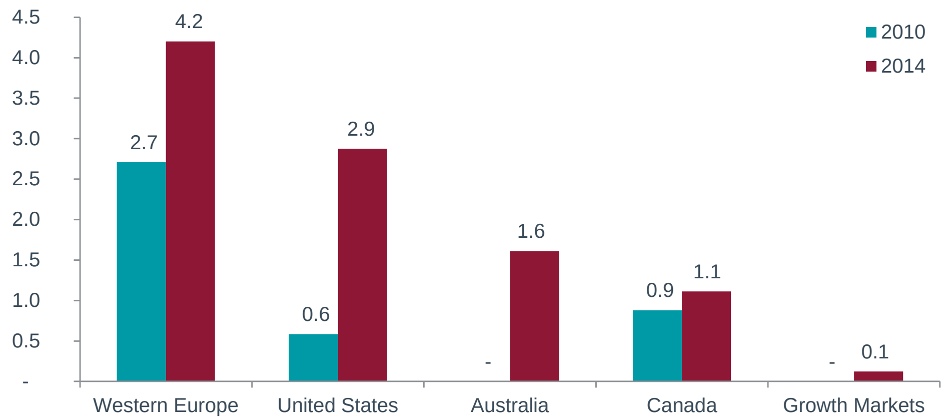
INFRASTRUCTURE

Over four years, the Infrastructure portfolio produced a 13.8% annualized return and generated $3.3 billion of net investment results. In 2014, the portfolio had a return of 13.2%. These returns exceed the long-term target.

The current yield, which reflects strong results by the operating companies in the portfolio, accounted for more than 60% of the portfolio's return during the period. The increase in the value of the assets in the portfolio, a result of their high quality as well as investor appetite for this asset class, accounted for close to 40% of the performance over four years.

Over the past four years, the size of the Infrastructure portfolio has more than doubled, growing from $4.3 billion in assets in 2010 to more than $10 billion at the end of 2014. This significant increase has allowed for greater diversification of the portfolio from both geographic and sectoral standpoints. As the following table shows, the portfolio's construction is geared to further deployment of capital in the United States and Australia, with less concentration in Europe. The portfolio is growing rapidly and is currently concentrated in about 10 major assets representing close to 90% of its value.

Geographic breakdown of the Infrastructure portfolio from 2010 to 2014
(total assets in billions of $)



Over four years, the benchmark index had a 17.9% return. The return on the 60 public securities that make up this liquid index was boosted significantly by the international equity markets' exceptional performance over the past four years. Of this return, only 25% was due to the current yield generated by companies. More than 75% of the return stemmed from the general rise in equity markets and capital gains associated with strong investor appetite for this asset class.

In 2014, the portfolio's managers carried out acquisitions totalling $1.3 billion. In the United States, la Caisse acquired a 30% interest in Indianapolis Power & Light Company, a retail electric service provider, and a 24.7% stake in Invenergy, a North American leader in wind power. At the start of the year, la Caisse acquired a 25% interest in London Array, the world's largest offshore wind farm, off the coast of the United Kingdom.

In the years to come, la Caisse will continue to make significant investments in infrastructure, particularly in Québec, the United States and in growth markets. This asset class is central to its investment strategy, especially in an environment of low interest rates and greater volatility in the equity markets.

Moreover, la Caisse recently announced that it would put in place a new business model to carry out major public infrastructure projects. The model will be implemented first in Québec and will enable la Caisse to further develop its expertise in project operations. This will give la Caisse a competitive advantage enabling it to increase its exposure to infrastructure elsewhere in the world.

REAL RETURN BONDS

This indexed portfolio generated an annualized return of 4.6% over four years. The 13.2% return for 2014 was due to lower real rates, which significantly increased the prices of long-term bonds.