Lakehead UNIVERSITY

Fall/Winter 2015

RETIREMENT PLAN REVIEW

Investment Volatility—What Drives It?

We all have a similar objective when it comes to investing: we want our money to grow. However, regular, continuous, rapid asset growth without periods of market unpredictability is unrealistic – this thought only exists in a fantasy world. Taking investment risk with its associated volatility is the only realistic way to increase assets over time.

Volatility refers to the degree of unpredictable change over time. To an investor, this generally alludes to the potential range of returns around an expected, or average, return over a long period of time. Volatility measures the above expected return and the below expected return. It is typical that higher long-term expected returns are associated with higher volatility – this supports the premise that investors should be compensated for the potential risk of underperforming the average expected return.

All investments have the potential to be volatile and many share the same factors for risk of volatility. An example of common volatility is the currency effect. Within the past year, the Canadian dollar has decreased in value relative to the US dollar which has enhanced US based investment returns. The US equity benchmark has increased 18 per cent over the past year – 90 per cent of this market increase is due to Canada's weakening dollar. In the past quarter the US benchmark (S&P 500) broke even – without the further deterioration of the dollar (or if you purchased the US Market in US dollars) the return would be closer to minus six per cent. To a lesser extent, investing in international equity has also generated returns that have been enhanced due to a weakening dollar. When the Canadian dollar appreciates, or gets stronger in comparison to another currency, it detracts from the absolute return of that fund.

Investment volatility also stems from a variety of global factors that drive investor sentiment and business profitability expectations. There has been concern over slowing global growth, high consumer debt and country debt levels. Conversely, improving US employment numbers and strong corporate balance sheets bode well for investment sentiment.

Almost all periods of history have had positive and negative factors during market sentiment. At times, these factors have been accountable for extreme market volatility. It is important to keep in mind to expect volatility even when it is unexpected. Make sure to focus on long-term objectives and remember that on many occasions, investing even when others had doubts, has subsequently yielded stronger investment results.

NEWSLETTERS ON-LINE!

Lakehead University Plan Members have access to the Proteus website where you can view current and past newsletters, Proteus' performance updates, investment manager presentations and other pension plan related documents.

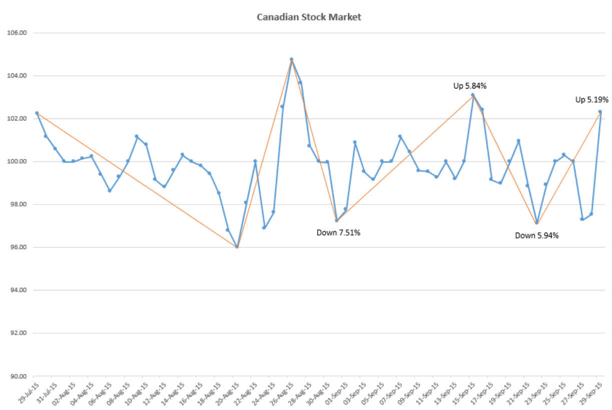
The website is secure.proteusperformance.com/member User ID: **Lakehead** Password: **learning**

PROTEUS
INVESTMENT & GOVERNANCE SPECIALISTS

Ready to Retire?

Q: What caused the recent volatility of the stock markets? *As a reminder, stocks plunged by 7.51 per cent in August and then shot back 5.84 per cent in September.*

A: At the most fundamental level, supply and demand in the market determines stock prices. Theoretically, earnings are what affect investors' valuation of a company, but ultimately it is the expectations about the company's future earnings growth that affects the demand for a stock. A positive outlook pushes the price up, while a negative one has investors selling their stake in the company, thus sending its price down.



Along with research, speculations and emotions are factored in when it comes to forming an opinion of stock valuation—contributing to stock price volatility. This volatility peaks during uncertain economic times and periods of irrational exuberance.

Stocks are not subject to well-defined parameters that help contain bond price volatility. The pattern of a stock price can be quite unpredictable at times. Quality companies (i.e. leaders, large and stable businesses) tend to exhibit reduced volatility, as they earn the trust of investors over their ability to maintain and grow their earnings stream.

Determining whether a stock is mispriced or not is a complex task. Sometimes even the professionals are wrong – for better or for worse.

Market Review

Canadian equities suffered a loss of 7.9% over the quarter. This was largely due to concerns about the global economy. Of particular importance to Canada were concerns over the Chinese economy and how that would affect demand for Canadian commodities. This led to a sharp decline in commodity prices, which meant large declines in the energy and materials sectors, where Canada's economy is highly concentrated.

World markets were down 2.6% at the end of the quarter. China played a large role in the erratic behaviour of global markets. The Chinese stock market fell dramatically (22.7%), this was followed by a devaluation of the yuan by China's central bank. The MSCI EAFE Index fell 3.5% over the quarter, while the S&P 500 Index gained 0.5%. A fall in commodity prices, a widening of credit spreads, and a drop in trading volume caused a multi-year high in market volatility. The MSCI Emerging Markets Index fell 11.8%. *Returns are all in Canadian dollars.*

The Bank of Canada lowered its overnight rate from 0.75% to 0.50% in early July, in response to Canada's diminished growth prospects. Interest rate volatility increased throughout the quarter as the Federal Reserve's possible rate hike approached. The Federal Reserve left its key lending rate unchanged at its September meeting. The FTSE TMX Canada Universe Bond Index posted a 0.15% gain during the quarter. Corporate bonds underperformed as spreads in the corporate sector reached their highest levels in three years.

Investment Structure

Lakehead University Main Pension Plan

Lakehead Pension Total Portfolio — The pension plan investment structure is comprised of a number of underlying investment funds managed by various investment management firms (see below). The goal of the investment mix is to provide long term capital growth and capital preservation. The Portfolio is currently invested in Canadian large-cap and mid-cap equities, Canadian bonds, American large-cap and small cap equities and International large-cap and small-cap equities.

Lakehead University Short Term Account

Short Term Account — The Short Term Account is comprised of one underlying investment fund managed by Jarislowsky Fraser (JF). The underlying fund is a money market fund. Money market funds invest in short term interest bearing (or discount) securities of governments, corporation and other short term borrowers with a time horizon generally under one-year. The rate of return for the fund should be consistent with short term Canadian interest rates.

Underlying Investment Managers

Main Pension Plan

Balanced Funds

Jarislowsky Fraser Total Portfolio — Invests in the pooled JF Canadian equity and bond funds. The target allocation is a 50-50 split between the two funds. The JF Canadian equity fund emphasizes buying long-term growth at a reasonable price. The JF Bond fund is managed based on safety of principal, conservative duration management, and optimization of yield.

Letko Brosseau Total Portfolio — Invests in the Letko Brosseau RSP Balanced and RSP Equity funds. Equity portfolios typically consist of 80 to 120 companies diversified by sector, geography, and individual security. The process is driven by security selection. In fixed income the emphasis is on high quality bonds that meet the objectives of stability and income. Turnover on fixed income is approximately 10% per year.

Canadian Equity Fund

CGOV Canadian Equity — Attempts to buy companies at a sufficient discount to their intrinsic values. The companies are diversified across a minimum of globally recognized industry sectors with the mandate limited to 25 companies. The fund is not expected to exhibit index-like characteristics.

American Equity Fund

Dimensional US Equity Small Cap Value — Invests primarily in securities of small-cap U.S. companies.

Global Equity Fund

State Street Global Advisors (SSgA) — A portfolio of primarily large capitalization global equity stocks that is intended to match the return on the MSCI World Index.

International Equity Fund

Dimensional International Small Cap Value — Invests primarily in securities of small-cap international (non-U.S.) companies.

Fixed Income Fund

Addenda Bond Fund — Invests in a diversified portfolio of bonds and provides investors with interest income and safety of principal along with opportunities for moderate capital growth.

Lakehead's Investment Structure and Managers

Investment Strategy

Capital Markets are unpredictable over short time periods, making attempts to shift between asset classes and 'time the market' difficult for even professional investors. Because of short-term volatility, a well diversified portfolio and a long time horizon generally offer the best protection from fluctuating markets.

A long term investor typically does not focus on poor performance in any given year. Instead, they review their strategy and consider whether the investment still fits with their long term objectives. If you are a long way from retirement, a mix of stocks and bonds may be prudent. If you are close to retirement, a more conservative investment approach may be appropriate as there is less time to recover investment losses. If you are unsure of the best strategy for you, you should seek independent professional advice before making your investment decisions.

Performance Summary

Period Ending September 30, 2015

	1 year	3 year	4 year	10 year
Lakehead Pension Total Portfolio	3.0	11.2	11.0	6.1
Benchmark	*3.5*	*9.1*	*9.2*	*5.7*
Lakehead Short Term Account*	1.1	1.2	1.2	n/a
Benchmark	*0.8*	*0.9*	*0.9*	*n/a*

Returns are shown before fees unless indicated. Past performance of a fund is not necessarily indicative of future performance.

**Performance shown is for the underlying pooled fund.*

Plan Governance

Plan Governance is handled by the Pension Board and Pension Advisory Committee.

The Professional Plan is administered by the Pension Board which is advisory to the Board of Governors. The Pension Board consists of the following members:

- Two Members of the Faculty (Bargaining Units #1 and #2);
- One Pensioner;
- One Member of Non-Faculty Staff; and
- Two persons chosen by the Board of Governors.

The Employee Plans is administered by the Pension Advisory Committee, which is advisory to the Board of Governors of the University. The Committee consists of:

- Two members appointed by the Board of Governors;
- One member of each bargaining unit;
- One member of non-union staff; and
- One member of non-union Technical staff.