

## NATCAN CORPORATE BOND FUND

**Management Approach** Based on rigorous risk management, our approach focuses on capital preservation. Our experts share a global market perspective, and favour a disciplined investment process rooted in the belief that security and industry selection plays a central role in portfolio performance. The portfolio is actively managed without duration deviations. Our management process begins with the duplication of the index through vigorous security selection. We then proceed to an in-depth analysis of relative values with the help of derivatives in order to increase the yield of the portfolio while avoiding additional credit risk. We then analyse economic, fundamental, and technical factors to try to predict Canada and U.S. credit spreads over a 6-month horizon. Finally, we initiate different tactical deviations, and conclude with the management, in real time, of these deviations by evaluating the risk and expected return of the portfolio.

### MARKET OVERVIEW

After experiencing extreme volatility during the first quarter of 2008, the credit market stabilized after the bailout of Bear Stearns by the Federal Reserve and JPMorgan, and central banks' additional liquidity measures, which have helped greatly reduce the systemic risk. However, spreads widened toward the end of June due to renewed concerns of inflation and significant supply of products by financial institutions. The spreads of the DEX Corporate Mid Term Index widened by 2 basis points to end the quarter at +198. The latest round of new issuance has required concessions to secondary trading levels of 10-20 basis points in order to induce buyers.

The DEX Corporate Mid Term Index returned -0.57% during the second quarter compared to -0.89% for the DEX Federal Bond Mid Term Index. The AAA/AA Bond Index outperformed during the quarter, returning 0.06% compared to -1.13% and -0.73 for the A and BBB Bond indices respectively.

### PERFORMANCE REVIEW

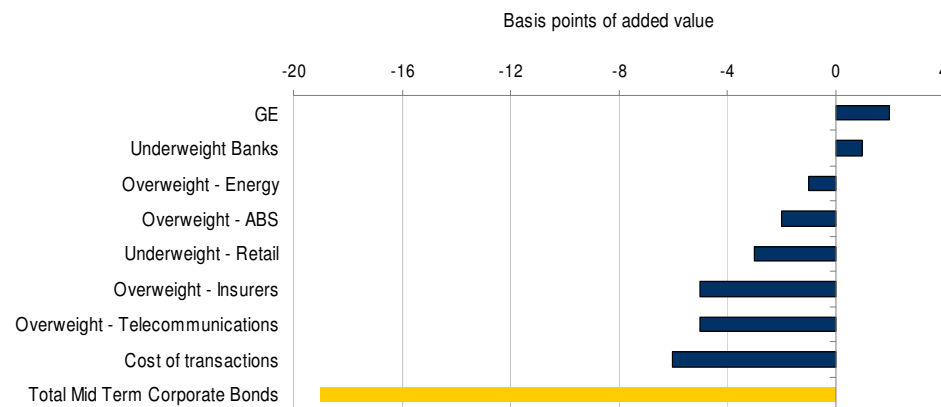
The portfolio lost 19 basis points during the second quarter of 2008. The portfolio's position in General Electric as well as its underweight in banks were the only two positive factors. The main negative contributors stemmed from transaction costs and overweights in insurance and telecommunications.

### PERFORMANCE

|                    | 3 months | YTD    | 1 year | 4 years | Since inception (1999-11) |
|--------------------|----------|--------|--------|---------|---------------------------|
| Fund <sup>1</sup>  | -0.75%   | 1.81%  | 4.03%  | 5.00%   | 7.13%                     |
| Index <sup>2</sup> | -0.57%   | 1.82%  | 4.13%  | 5.11%   | 7.02%                     |
| Added value        | -0.18%   | -0.01% | -0.10% | -0.11%  | 0.11%                     |

1 - Everywhere in this bulletin, "Fund" refers to the Natcan Corporate Bond Fund.  
2 - Everywhere in this bulletin, "Index" refers to the DEX Mid Term Corporate Bond Index.

### PERFORMANCE ATTRIBUTION VS THE INDEX



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## OUTLOOK AND STRATEGY

The cash/government bond portion of the portfolio has remained constant over the period (4.5%). Despite the significant widening of spreads since the beginning of the year, we believe the current economic uncertainties along with new issuances at significant concession levels will continue to influence credit spreads in the coming months. The weight of government bonds in the portfolio will remain above 3% given the ongoing uncertainty in the market.

We will continue to participate in new issuance at favourable pricing relative to secondary trading levels. Financial spreads (including ABS) are attractive on an historical basis. As such, we are looking to move to an overweight in that area over the coming quarters.

We are uncomfortable with BMO and CIBC's exposure to the U.S. sub-prime mortgage crisis, and prefer to wait for signs of improvement before reducing the underweight in banks. Moreover, the risk/return ratio of hybrid securities is becoming increasingly attractive relative to bank notes.

## TECHNICAL CHARACTERISTICS

| Characteristics               | Fund  |
|-------------------------------|-------|
| Number of issuers             | 55    |
| Yield to maturity             | 5.65% |
| Average spread (basis points) | 202   |
| Average credit rating         | 5.99  |

## MAIN DEVIATIONS

| Overweight                      | Natcan Weight | Index Weight | Weight Deviation | Natcan Duration | Index Duration | Dollar / Duration |
|---------------------------------|---------------|--------------|------------------|-----------------|----------------|-------------------|
| Government of Canada            | 3.93%         | 0.00%        | 3.93%            | 4.901           | 0.000          | -0.19             |
| Enmax Corporation               | 1.85%         | 0.50%        | 1.34%            | 7.377           | 7.377          | -0.10             |
| Industrial Alliance & Financial | 1.61%         | 0.49%        | 1.12%            | 4.786           | 4.875          | -0.05             |
| Manulife Financial              | 3.64%         | 2.61%        | 1.02%            | 7.201           | 6.682          | -0.09             |
| Credit Agricole SA              | 0.99%         | 0.00%        | 0.99%            | 6.112           | 0.000          | -0.06             |
| Alliance Pipeline               | 1.39%         | 0.41%        | 0.98%            | 4.746           | 3.287          | -0.05             |
| Bell Alliant                    | 2.36%         | 1.41%        | 0.95%            | 5.589           | 5.642          | -0.05             |
| Cooperators                     | 0.90%         | 0.00%        | 0.90%            | 3.536           | 0.000          | -0.03             |
| TD Bank                         | 9.83%         | 9.04%        | 0.78%            | 6.501           | 6.511          | -0.05             |
| Suncor                          | 1.91%         | 1.17%        | 0.74%            | 7.399           | 7.399          | -0.06             |

| Underweight        | Natcan Weight | Index Weight | Weight Deviation | Natcan Duration | Index Duration | Dollar / Duration |
|--------------------|---------------|--------------|------------------|-----------------|----------------|-------------------|
| BNS                | 1.72%         | 2.29%        | -0.57%           | 4.576           | 4.600          | 0.027             |
| BCIMC Realty Corp. | 0.00%         | 0.59%        | -0.59%           | 0.000           | 6.360          | 0.038             |
| EnCana             | 0.63%         | 1.29%        | -0.66%           | 7.095           | 7.095          | 0.047             |
| CIBC Bank          | 2.60%         | 3.36%        | -0.76%           | 6.220           | 5.769          | 0.032             |
| Fortis Inc.        | 0.70%         | 1.53%        | -0.83%           | 5.132           | 5.470          | 0.048             |
| Hydro One          | 0.89%         | 1.79%        | -0.91%           | 6.305           | 6.867          | 0.067             |
| Wells Fargo        | 0.82%         | 2.15%        | -1.33%           | 5.926           | 5.619          | 0.072             |
| Molson/Coors       | 0.00%         | 1.41%        | -1.41%           | 0.000           | 5.880          | 0.083             |
| Bank of Montreal   | 9.40%         | 12.02%       | -2.62%           | 6.582           | 6.447          | 0.156             |
| National Bank      | 0.00%         | 3.18%        | -3.18%           | 0.000           | 5.774          | 0.184             |

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