

## NATCAN CANADIAN BOND FUND

**Management Approach** We are active managers who apply a quantitative approach based on macroeconomic analysis where the emphasis is placed on the management of a reward/risk equation. Our objective is to maintain an asymmetry of expected returns versus the underwritten risks. Our management approach is a three-step process. The first step consists in a strategic replication of the benchmark in order to reduce tracking errors and to control the portfolio's risk. We select specific securities in order to capture liquidity and complexity premiums accessible on the market without adding credit or duration risks. Finally, the third and last step focuses on performing tactical management deviations relative to the benchmark.

### MARKET OVERVIEW

The credit crisis unleashed just over a year ago increased in the third quarter of 2008, spreading to most stock markets and the global economy. In the past months, many financial institutions have disintegrated, including Lehman Brothers, Washington Mutual, Fannie Mae, Freddie Mac, AIG, Fortis, Merrill Lynch, and Wachovia. Fortunately, none of these were included in the portfolio.

Inevitably, all this uncertainty has had a negative effect on the corporate bonds market. The increasing risk of companies defaulting was reflected in the price of financial securities, pushing the bond market into negative territory, all of which, in spite of the collapse of stock markets. Market volatility reached a peak and returns are now expected to fluctuate significantly on a daily basis.

To illustrate the excessive level of market volatility, note the 0.21% increase in a single day for the 30-year Government of Canada Bond, climbing from 4.08% to 4.23% at the end of the quarter.

In this environment, the DEX Universe Bond Index fell 0.37%, bringing its annual cumulative return to +1.83%. This performance is much less than the annual cumulative return registered by its government component of almost +2.40%.

### PERFORMANCE REVIEW

For the third quarter, the portfolio registered a return inferior to its benchmark. This underperformance is essentially due to our investments in commercial mortgage-backed securities (CMBS), Supranational Agency bonds (Maple Bonds), and in Canadian banks. Although this focus on less liquid securities in the current environment subtracted points from portfolio performance, we believe the quality of these securities will prove beneficial in the long-term.

The portfolios' Canada-U.S. positioning and our corporate security selection enabled us to offset part of the decline.

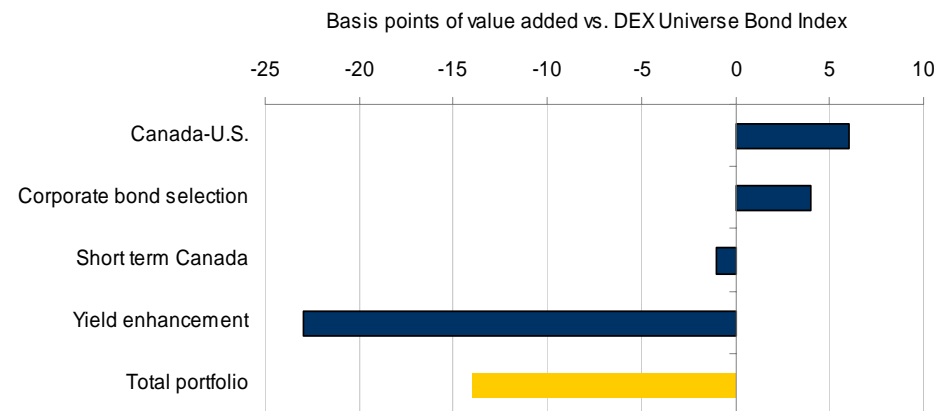
### PERFORMANCE

	3 months	YTD	1 year	4 years	10 years
Fund <sup>1</sup>	-0.51%	1.63%	4.55%	4.48%	5.69%
Index <sup>2</sup>	-0.37%	1.83%	4.62%	4.79%	5.73%
Added value	-0.14%	-0.20%	-0.07%	-0.31%	-0.04%

<sup>1</sup> - Everywhere in this bulletin, "Fund" refers to the Natcan Canadian Bond Fund.

<sup>2</sup> - Everywhere in this bulletin, "Index" refers to the DEX Universe Bond Index.

### PERFORMANCE ATTRIBUTION



# NATCAN CANADIAN BOND FUND

## OUTLOOK AND STRATEGY

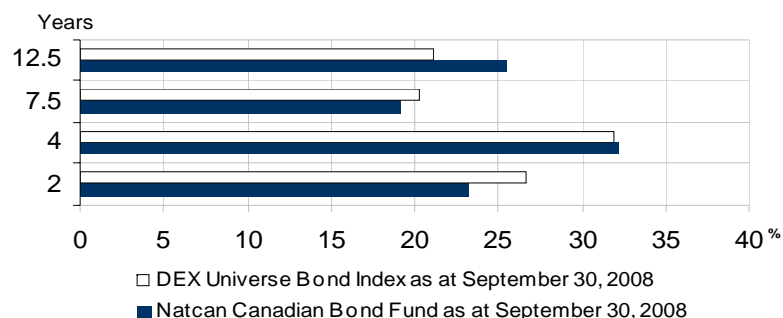
A prudent strategy is required, considering the growing probability of an economic recession. Interest rates, albeit low, have reached a more realistic level given the weak growth outlook and strong deflationary pressures. If the economic slowdown is to further escalate, we may be forced to increase the portfolio duration considerably. Additionally, if the measures recently implemented by central banks to stabilize markets are successful in their objective, we will seek to increase our exposure to the corporate sector.

Credit spreads are being supported by issuers' need for capital amid the current credit crunch. As such, we favour only the highest quality credit ratings. Spreads of government-backed securities also widened considerably. However, their credit ratings remain unscathed.

We are maintaining overweight positions in securities issued by agencies guaranteed by G7 countries and in Royal Bank, TD Bank, and Bank of Nova Scotia's senior debt. Indeed, though we remain confident in the solvency of Canadian banks in spite of the current market uncertainty, the unstable environment has convinced us to favour senior debt.

During the month, we moved to a more neutral position in U.S. bonds as we had accomplished our value added objective with respect to this position.

## DURATION DEVIATIONS (%)



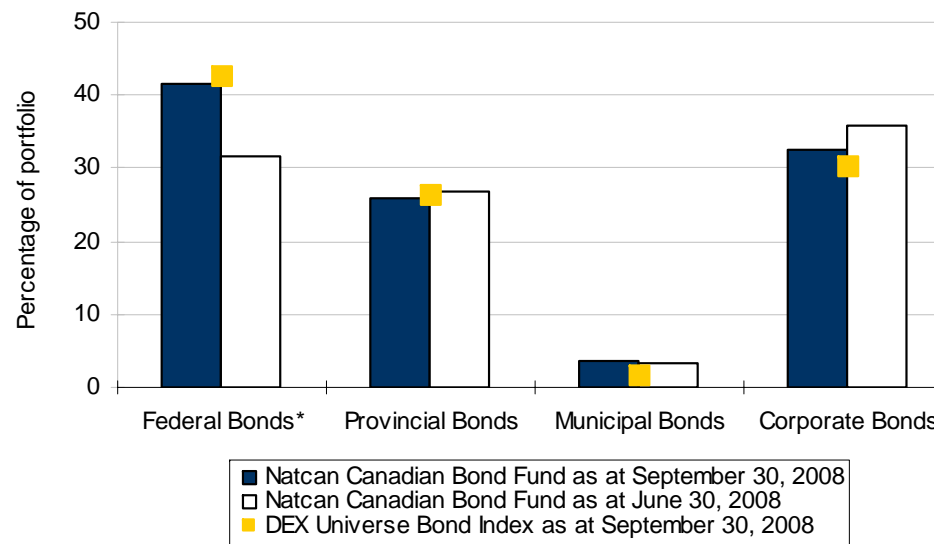
\* Duration points are interpolated between these four points. Shorter and longer bonds are placed in the 2 and 12.5 buckets respectively.

This publication is intended for your private information. The information and opinions herein are provided for informational purposes only, are subject to change based on market and other conditions. The views expressed should not be relied upon as the basis for your investment decisions. Past performance is not necessarily indicative of future performance. This document is not and should not be construed as a solicitation or offering of units of any fund or other security in any jurisdiction. No part of this publication may be reproduced in any manner without the prior written permission of Natcan Investment Management Inc. The Natcan Pooled Funds performance returns are calculated on a net of fees basis. All market index returns presented in this document were provided by Thomson Reuters and PC-Bond, a business unit of TSX Inc.

## ADJUSTED DURATION

	As at September 30, 2008	As at June 30, 2008
Fund	6.74 years	5.93 years
Index	6.16 years	6.41 year

## SECTOR ALLOCATION



\* Most Supranational Agency bonds issued in Canadian currency are considered under Federal bonds. A small percentage can also be found under Corporate bonds.

