

**Investment Consulting
William M. Mercer Limited**

2002 Fearless Forecast

Forecasts by 81 Canadian and
International Investment Managers



**The Economy and Capital Markets
Issues and Trends**

OPENING NOTE

We are pleased to present the results of our 2002 Fearless Forecast, which presents the views of institutional investment managers on the economy and capital markets. For this eleventh edition of the Fearless Forecast, we have received a record 81 responses from both Canadian and Foreign managers. We would like to extend our gratitude to the 81 fearless managers listed on the inside page before the back cover for taking the time to respond to our questionnaire.

HIGHLIGHTS OF 2002 RESULTS

A large proportion of money managers (74%) believe that the most important issues for 2002 in terms of the capital markets are corporate earnings and US interest rates. We did not ask any specific questions about corporate earnings, but we did ask about US interest rate levels. The average response was that the US Fed Funds rate would rise by 75 basis points over the year, ending at 2.5%, and that mid and long term US interest rates would also rise from current levels. In contrast, managers believe that Canadian interest rates will fall in the mid and long end of the curve, and they expect inflation to stay around the 2% level for the next 24 months.

Managers are not expecting these modest increases in US interest rates to have a negative impact on equity markets for the next year as they are forecasting, on average, double digit returns for the TSE300, the S&P500 and MSCI EAFE. Managers are expecting that the IFCI Emerging Composite (an emerging market index) will provide the best return for 2002.

On the currency side of the equation managers are expecting both the Canadian dollar and the Euro to strengthen significantly against the US dollar, with the loonie expected to go to 65 cents by year end and the Euro to be at 95 cents.

Perhaps the most interesting result from the survey is the relationship between managers' expectations for bond returns versus stock returns. For the Canadian market, managers are expecting the TSE300 Total Return Index (TRI) to beat the Scotia Capital Universe TRI by 3.5% over the next five years. Assuming a positively sloped yield curve (as we have now), this probably translates to a 3.0% equity risk premium over long Canada bonds. While this number is lower than the historical average, and lower than expectations we have seen in recent Fearless Forecasts, it is higher than the 0% that some analysts believe reasonable to expect. Our own research has produced an expected equity risk premium in the neighbourhood of 2.0% to 2.5%. The equity risk premium debate continues.

We wish you all the best for 2002.

SUMMARY OF RESULTS FROM 2001 FEARLESS FORECAST

Forecast Actual

The Canadian Economy

Bank of Canada Rate	5.5%	2.5%	Dec 31/2001
Annual Inflation Rate (CPI)	2.5%	0.6%	Nov 30/2001
Canadian Exchange Rate (\$U.S./\$CDN)	0.68	0.63	Dec 31/2001
Unemployment Rate	7.0%	8.0%	Dec 31/2001
Real GDP Growth Rate	3.4%	1.7%	Estimated Annualized

Investment Benchmarks

TSE 300 Total Return	12.0%	-12.6%	Dec 31/2001
S&P 500 Total Return (\$CDN)	10.0%	-6.5%	Dec 31/2001
MSCI EAFE Total Return (\$CDN)	12.0%	-16.3%	Dec 31/2001
MSCI World Total Return (\$CDN)	11.0%	-11.4%	Dec 31/2001
IFCI Emerging Composite Total Return (\$CDN)	10.0%	8.1%	Dec 31/2001
SC Universe Bond Total Return	7.0%	8.1%	Dec 31/2001
SC 91 Day T-Bills Total Return	5.3%	4.7%	Dec 31/2001

Top Performing Canadian Sectors

(Ranking out of 14 sectors in the TSE 300)

Financial Services	1st	11th
Industrial Products	2nd	14th
Oil & Gas	3rd	9th

Actual Top 3 Sectors

1. Transportation & Env.
2. Conglomerates
3. Merchandising

Top Canadian Equity Investment Styles

(Ranking out of 4 major equity investment styles)

Large Cap Growth	1st	4th
Large Cap Value	2nd	2nd
Small Cap Value	3rd	1st
Small Cap Growth	4th	3rd

Top Performing Countries within the MSCI World Index

(Ranking out of 22 countries within the MSCI World Index)

U.K.	1st	9th
Germany	2nd	17th
Canada	3rd	12th
U.S.	3rd	8th
Japan	5th	21st

Actual Top Performing Countries

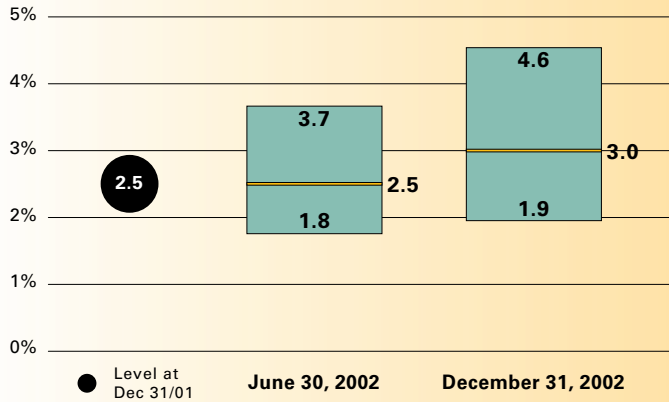
within the MSCI World Index

1. New Zealand
2. Austria
3. Australia
4. Ireland
5. Belgium

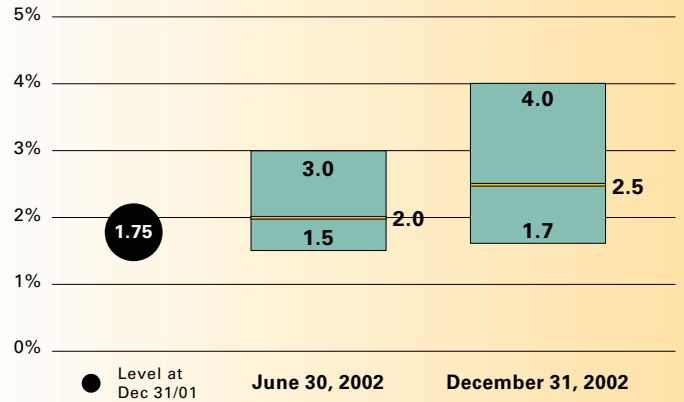
THE ECONOMY – 2002

Charts indicate the 95th percentile, median and 5th percentile forecasts.

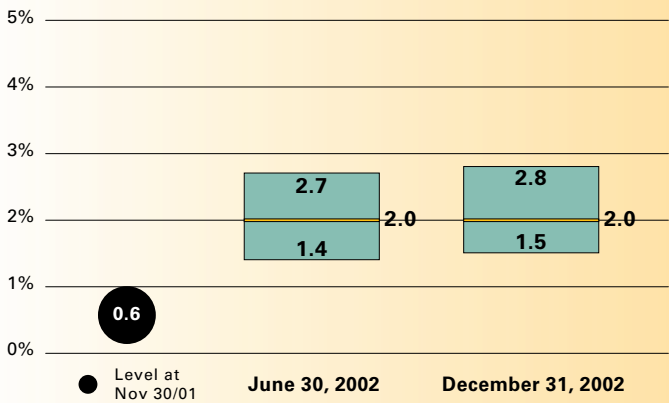
Bank of Canada Rate



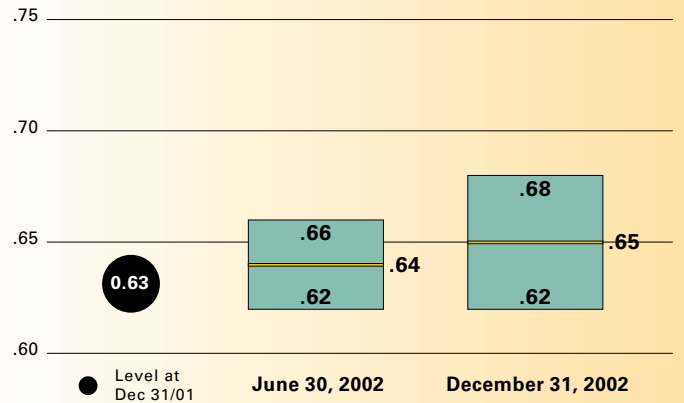
Federal Fund Rate (U.S.)



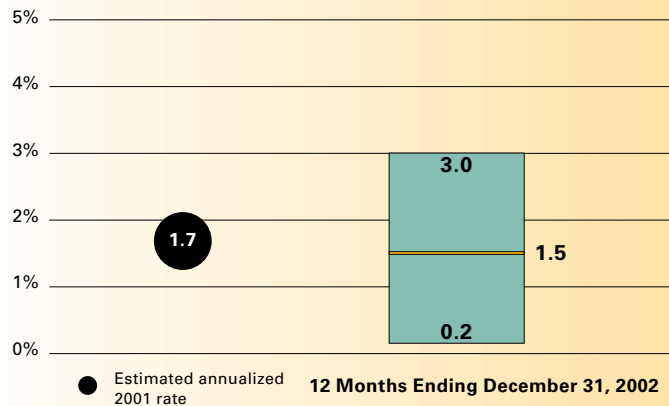
Annual Inflation Rate (CPI)



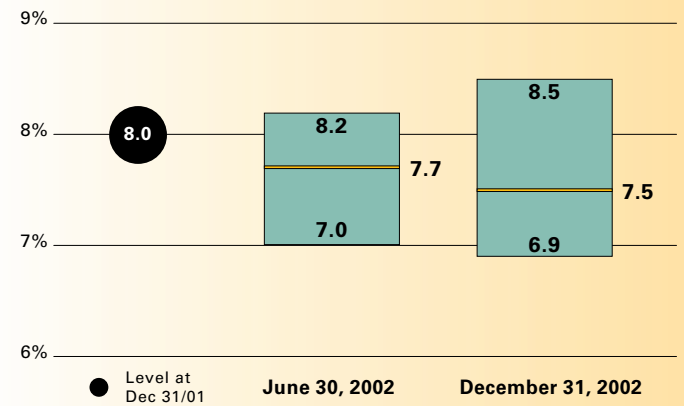
Canadian Exchange Rate (\$U.S./CDN)



Real GDP Growth Rate

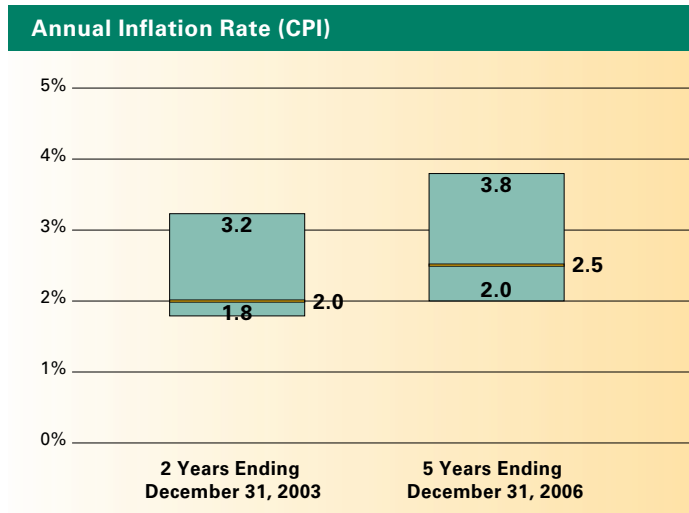


Unemployment Rate



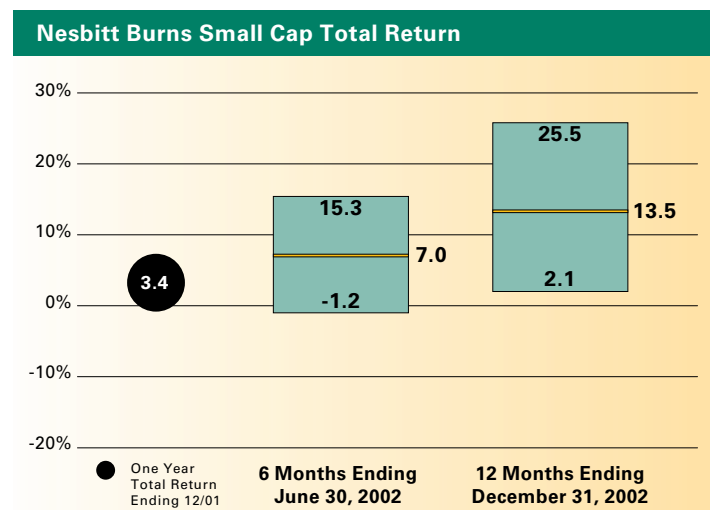
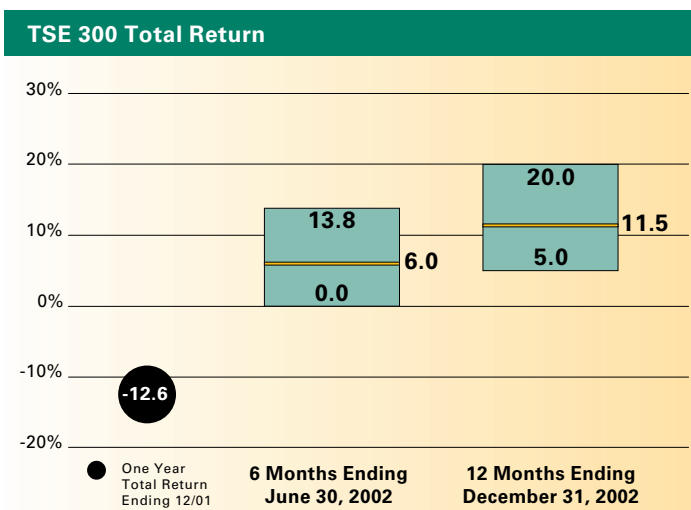
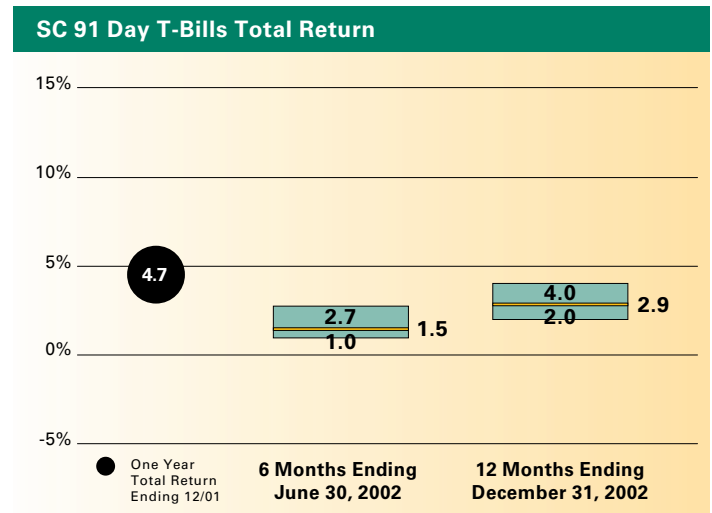
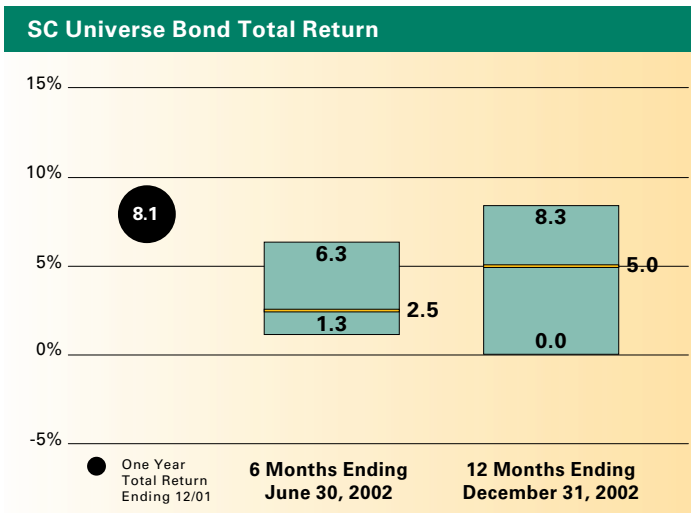
THE ECONOMY – LONG TERM

Charts indicate the 95th percentile, median and 5th percentile forecasts.



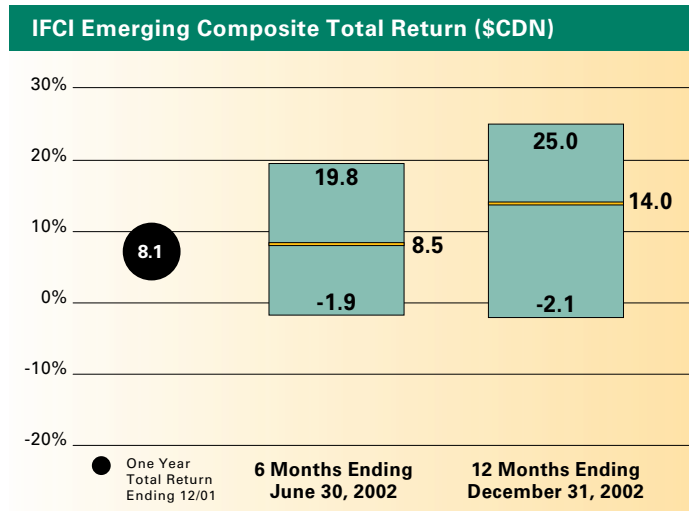
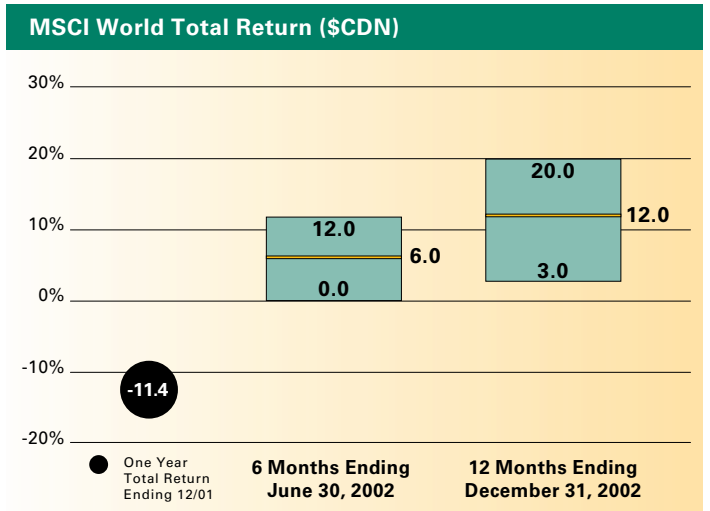
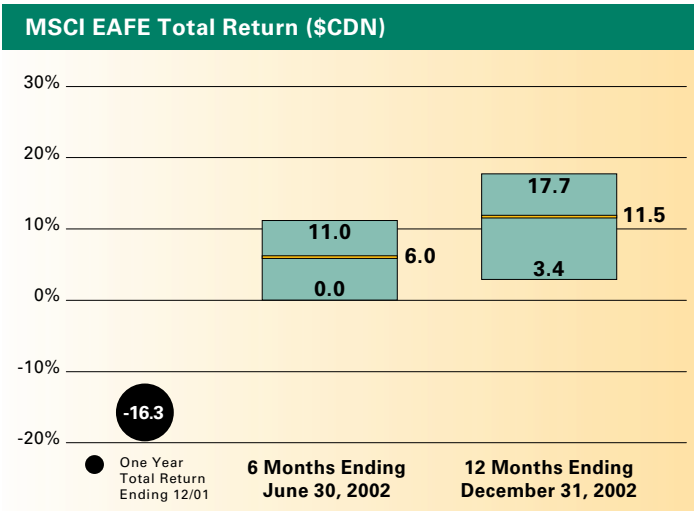
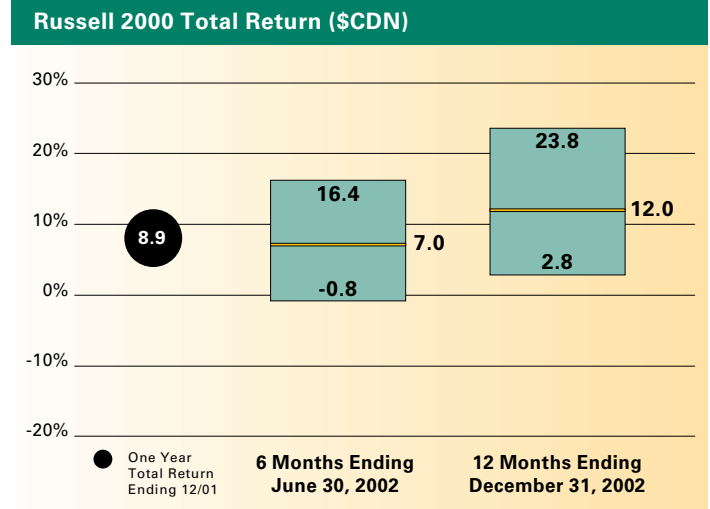
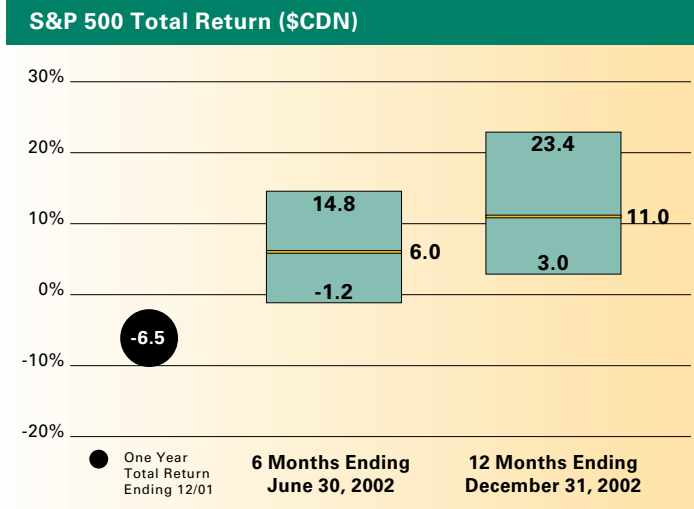
INVESTMENT BENCHMARKS – 2002

Charts indicate the 95th percentile, median and 5th percentile forecasts.



INVESTMENT BENCHMARKS – 2002

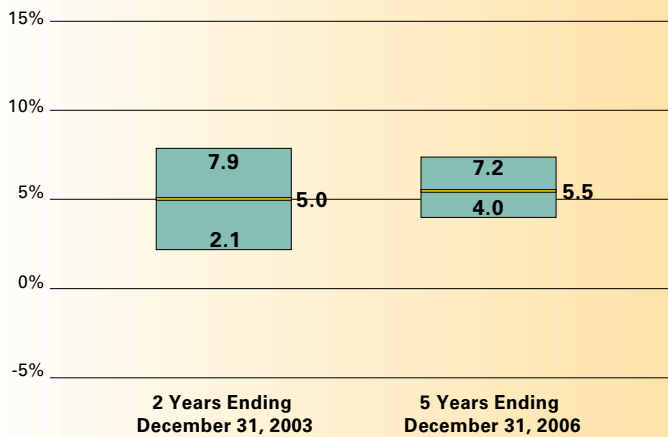
Charts indicate the 95th percentile, median and 5th percentile forecasts.



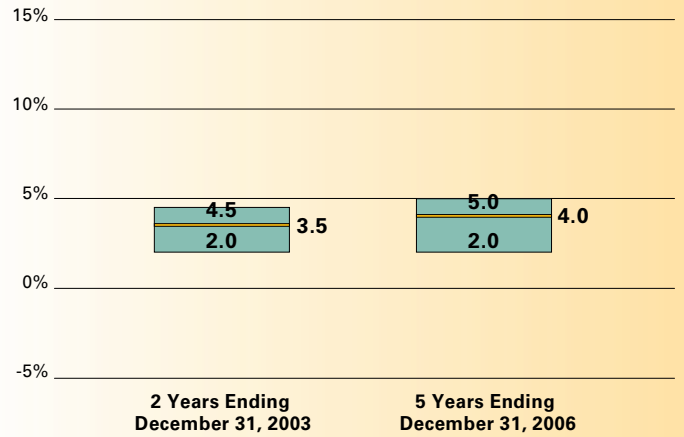
INVESTMENT BENCHMARKS – LONG TERM

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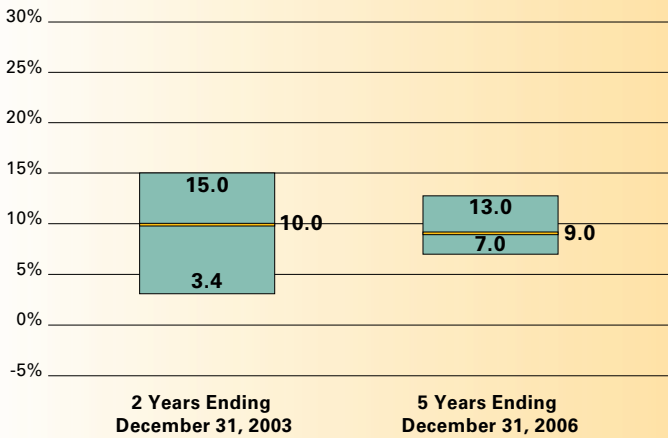
SC Universe Bond Total Return



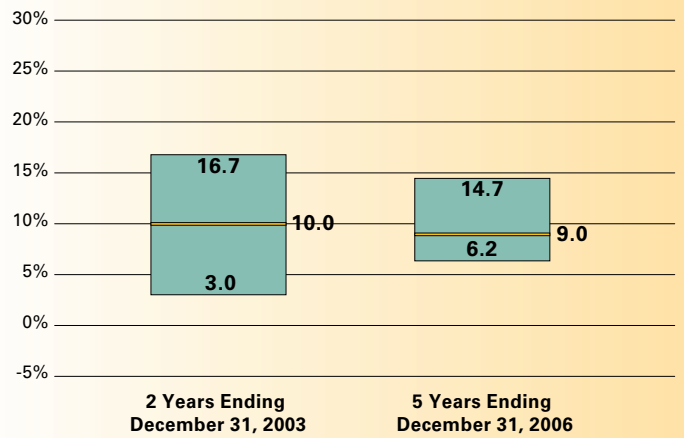
SC 91 Day T-Bills Total Return



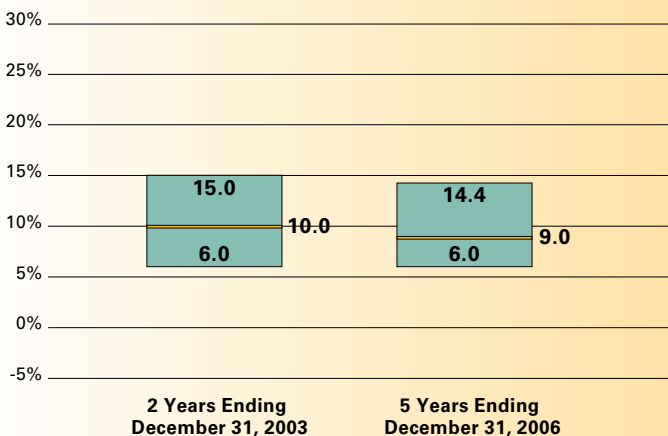
TSE 300 Total Return



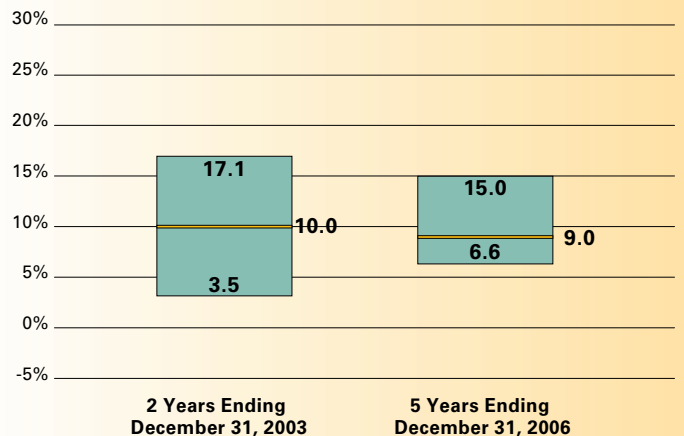
S&P 500 Total Return (\$CDN)



MSCI EAFE Total Return (\$CDN)



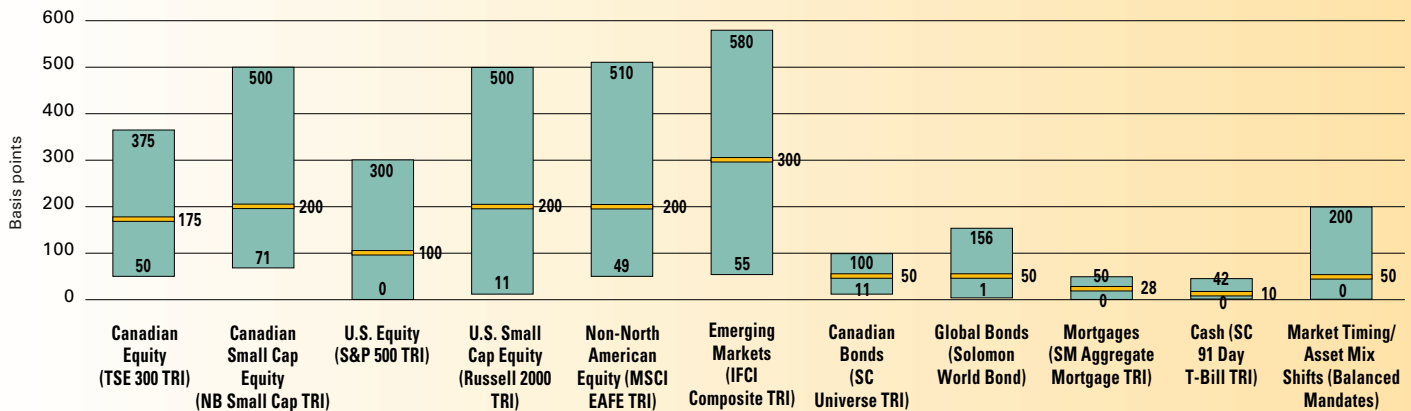
MSCI World Total Return (\$CDN)



INVESTMENT BENCHMARKS – LONG TERM

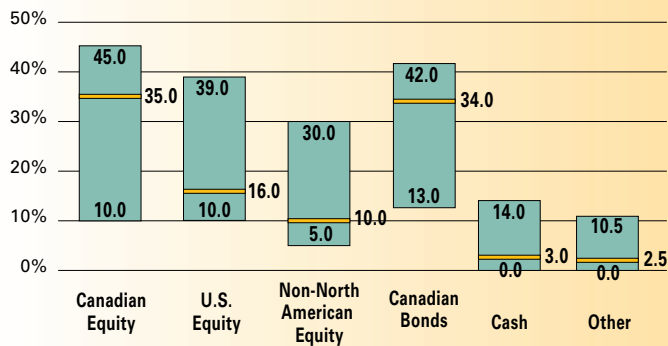
Charts indicate the 95th percentile, median and 5th percentile forecasts.

Managers estimate the value added (before fees) on an annual basis for each of the following asset classes over their respective benchmark for a market cycle:

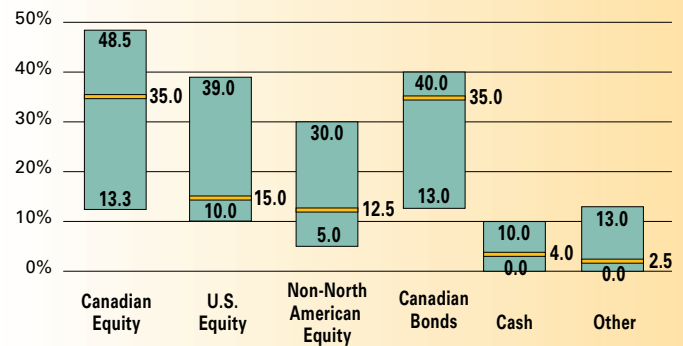


CANADIAN PENSION FUND INVESTMENTS

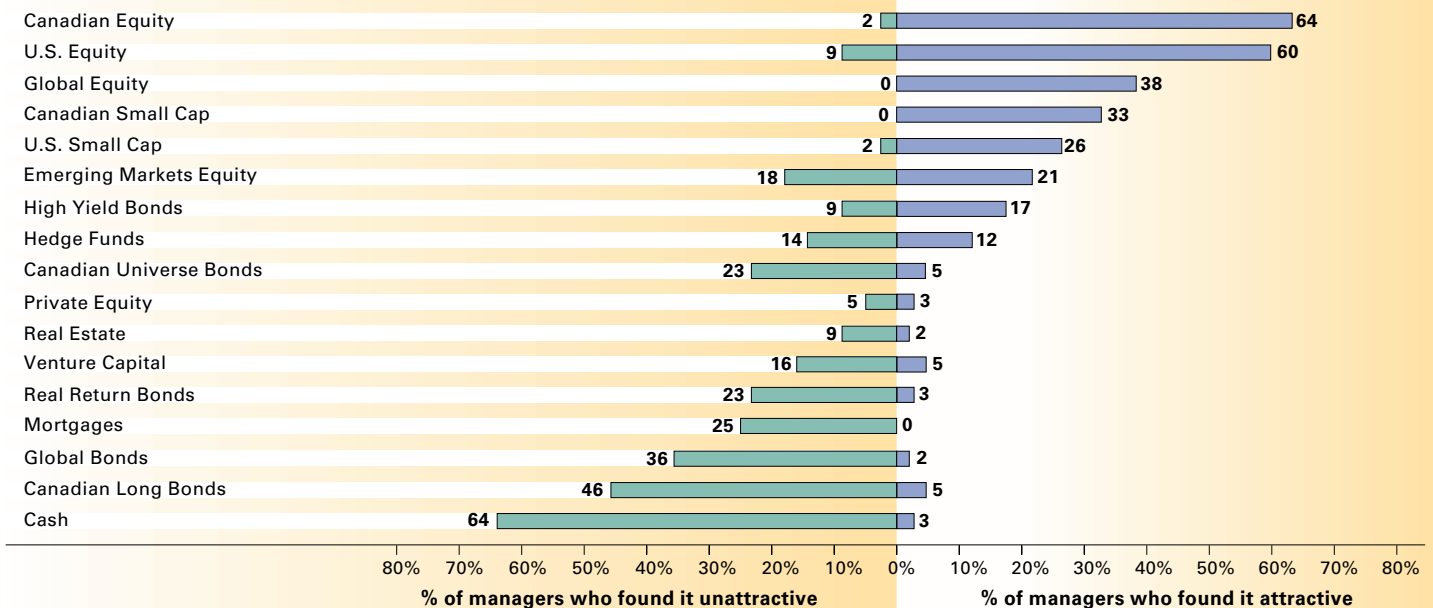
Managers recommend the following asset mix for a balanced pension fund as at June 30, 2002:



Managers recommend the following asset mix for a balanced pension fund as at December 31, 2002:

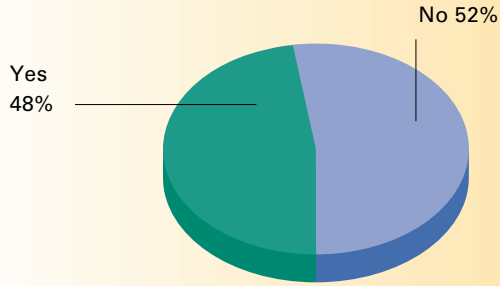


Managers rank the following as the most attractive (top 3) and least attractive (bottom 3) asset classes in 2002:

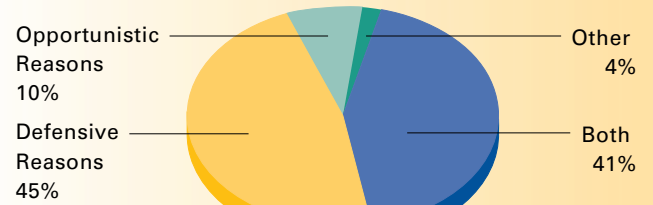


CANADIAN PENSION FUND INVESTMENTS

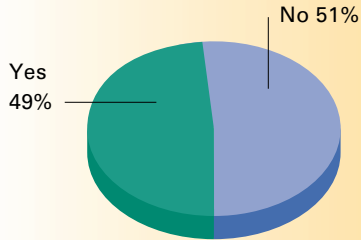
Investment managers were asked if they employ currency hedging strategies:



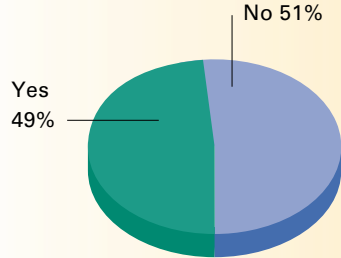
Why hedge currency?



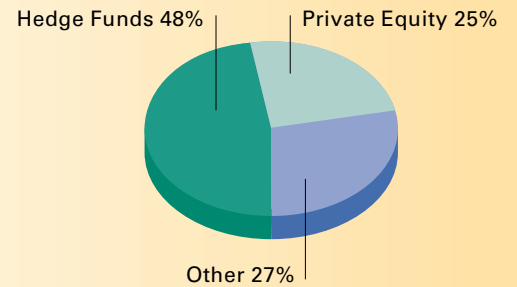
Investment managers were asked if they believe ethical mandates will increase in 2002:



% of managers currently offering alternative investments:

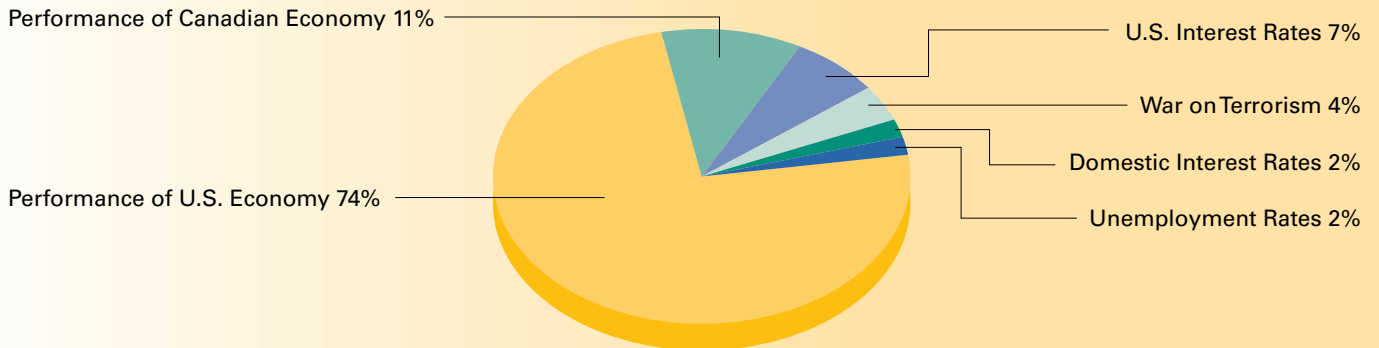


If yes, what type?



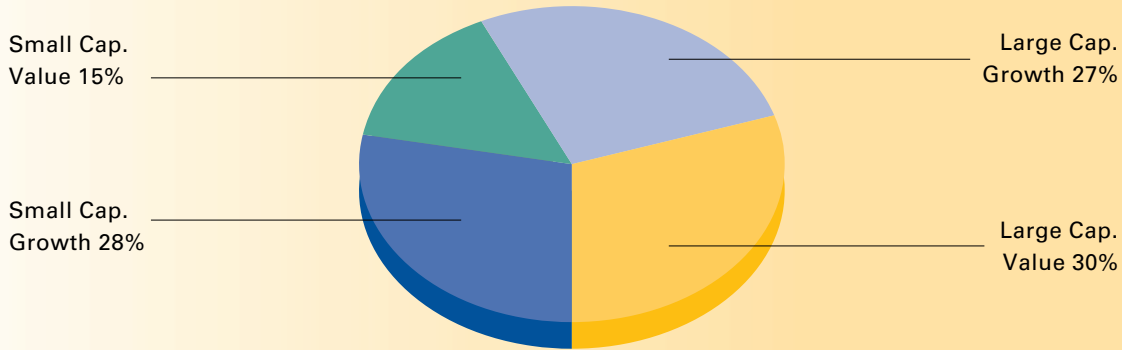
CANADIAN CAPITAL MARKETS

Managers rank the following as the top issues affecting Canadian markets in 2002:

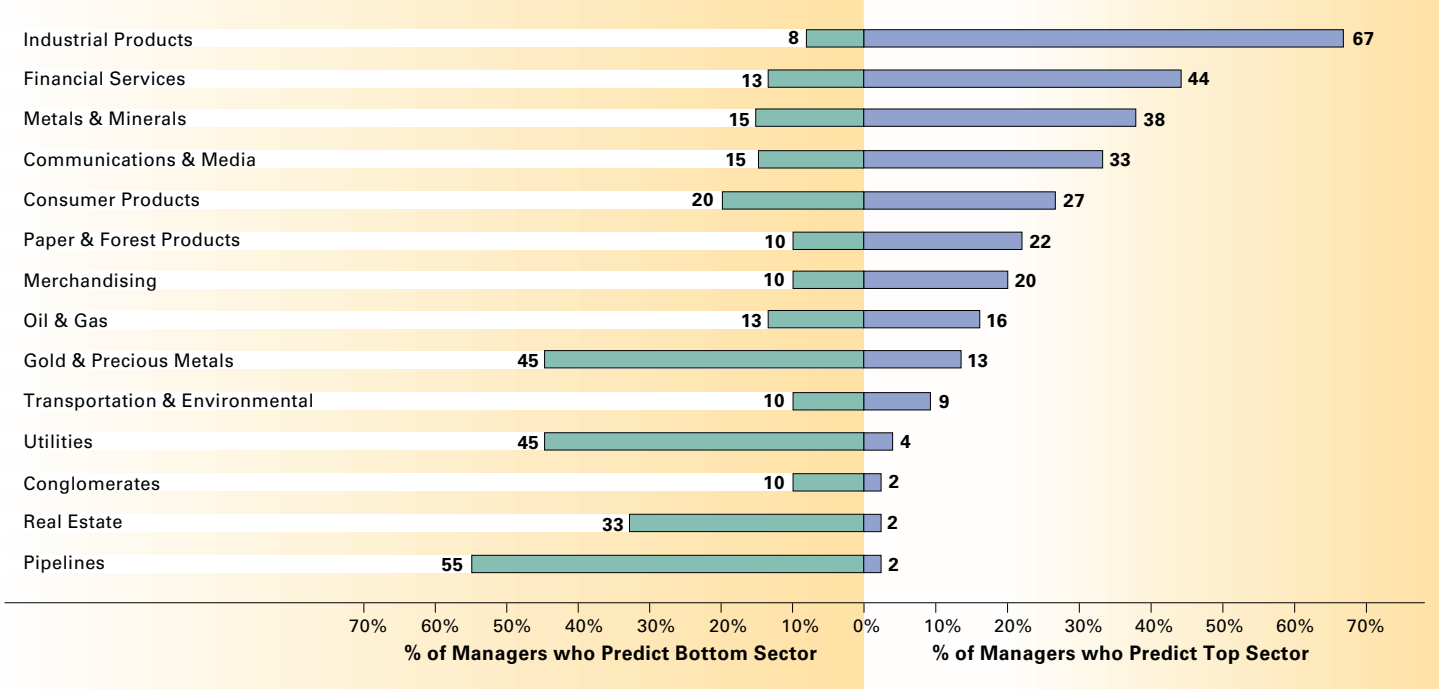


CANADIAN CAPITAL MARKETS

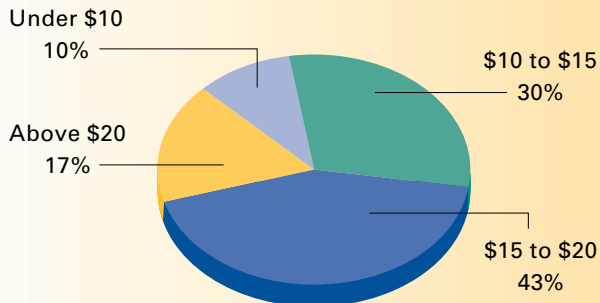
Best Canadian equity investment style for 2002:



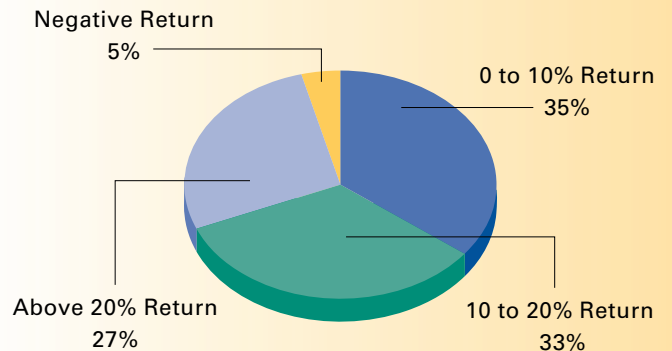
Managers expect the following to be the best performing (top 3) and worst performing (bottom 3) equity sectors of the TSE 300 Index in 2002:



Managers were asked to predict the price of Nortel at the end of 2002:

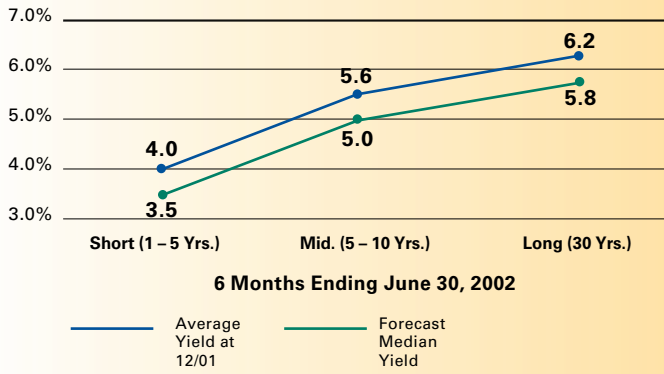


Managers' outlook on the technology sector for 2002:

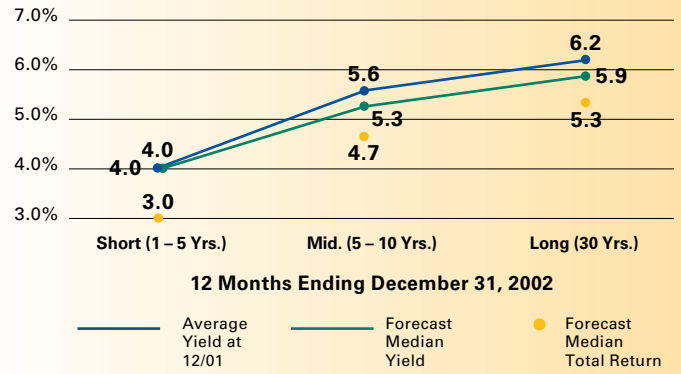


CANADIAN CAPITAL MARKETS

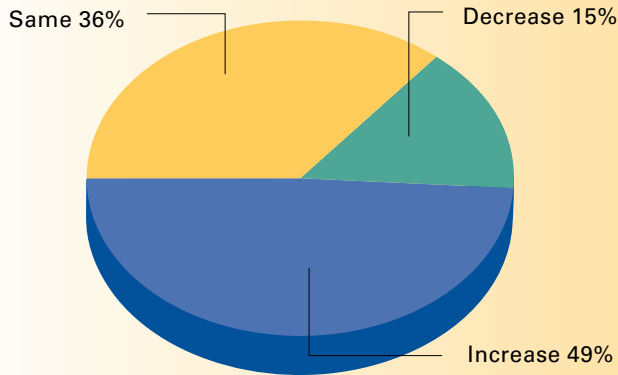
Government of Canada Bonds



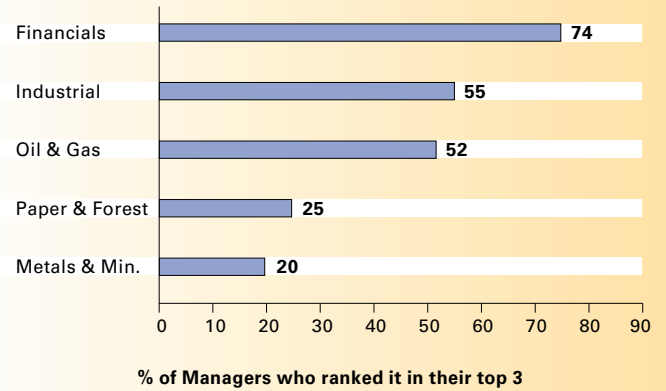
Government of Canada Bonds



Managers were asked if merger/acquisition activity in Canada would increase, decrease or stay the same in 2002:



Managers were asked to rank the top 3 Canadian sectors/industries that would experience the most consolidation in 2002:



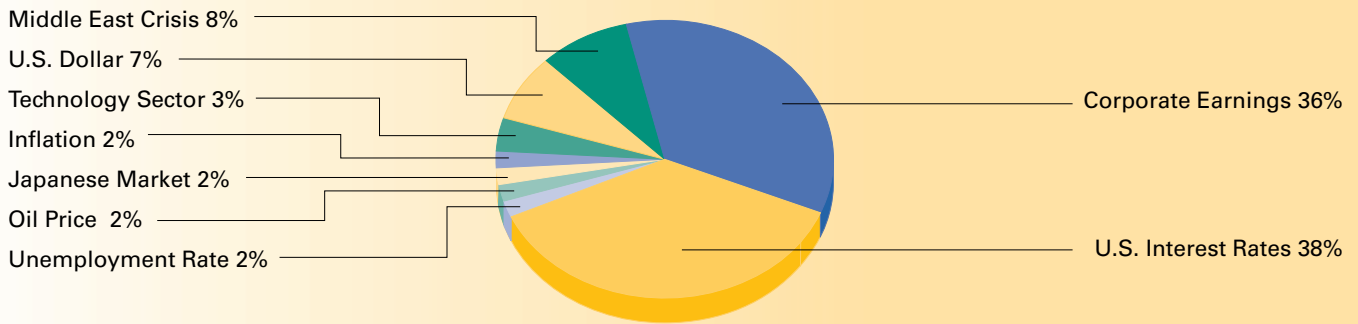
Managers ranked the 5 best performing Canadian stocks for 2002:

- > Nortel
- > Bombardier
- > Talisman
- > Biovail
- > Magna

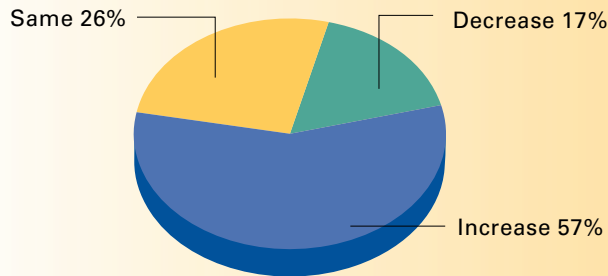
Based on the number of times Managers chose each stock in their top 5

GLOBAL CAPITAL MARKETS

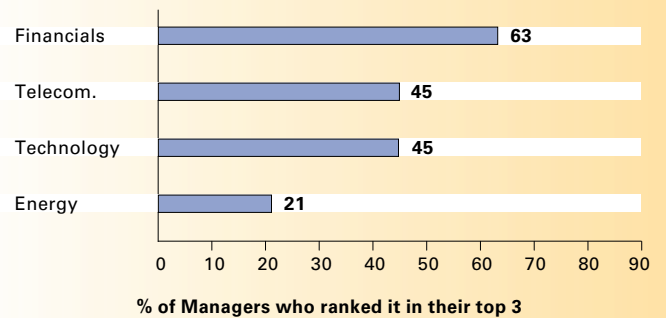
Managers were asked to rank the following as the top issues affecting global markets for 2002:



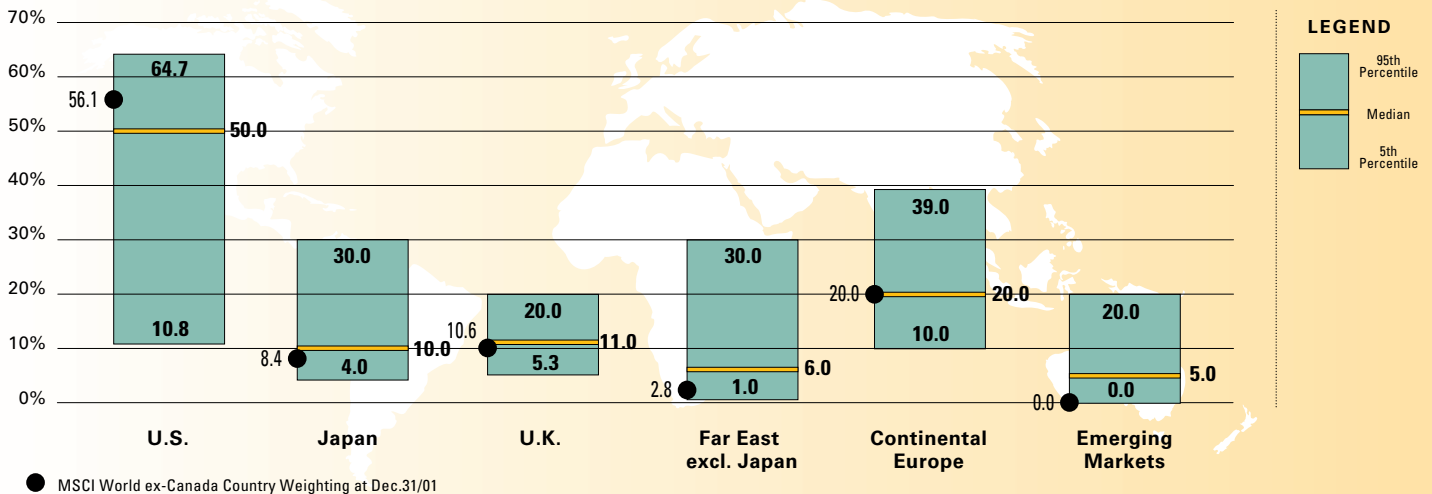
Managers were asked if merger/acquisition activity globally would increase, decrease or stay the same in 2002:



Managers were asked to rank the top 3 global sectors/industries that would experience the most consolidation in 2002:



Managers predict the following to be the best country/region allocation for a global equity portfolio in 2002:



Managers were asked to choose the top 5 performing equity markets in 2002:

- U.S.(21)
- Canada(16)
- U.K.(16)
- Japan(13)
- Hong Kong(12)

() indicates the number of times mentioned by managers

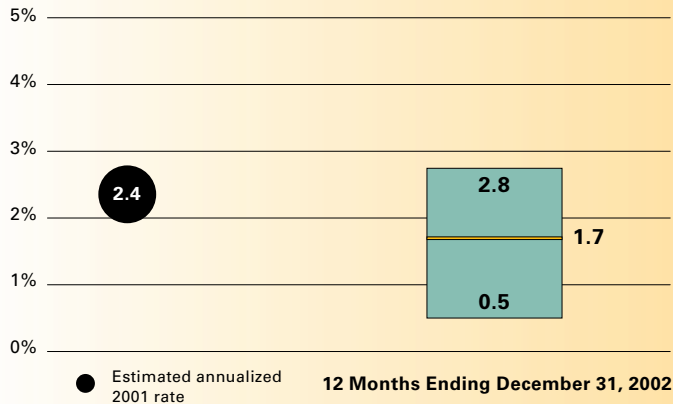
Managers were asked to choose the top 5 performing sectors in 2002:

- Information Technology(24)
- Financial Services(18)
- Health Care(16)
- Telecommunication Services(14)
- Industrial(12)

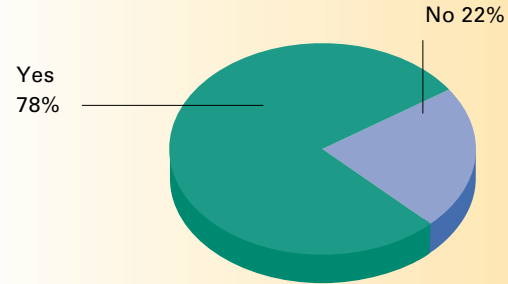
() indicates the number of times mentioned by managers

GLOBAL CAPITAL MARKETS

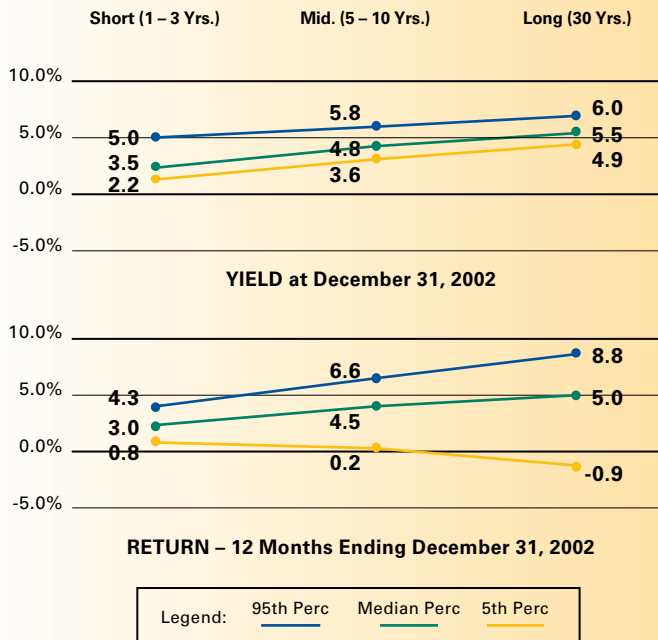
Managers were asked to predict the real global GDP growth rate in 2002:



Investment managers were asked if they thought the emerging markets would be attractive over the next 3 years:



United States Treasury Bonds

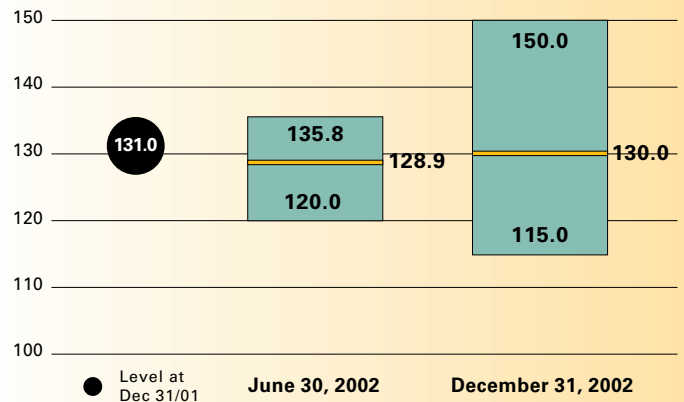


Investment managers were asked to list their top 3 global equity stock picks for 2002:

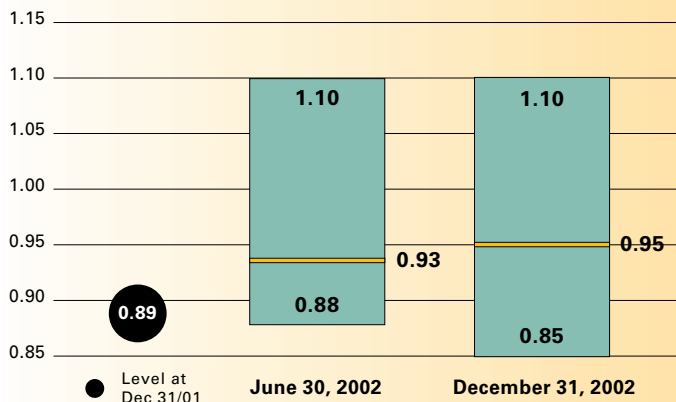
- > **Nokia**
- > **Microsoft, Vodafone**
- > **General Electric**

Based on the number of times Managers chose each stock in their top 3

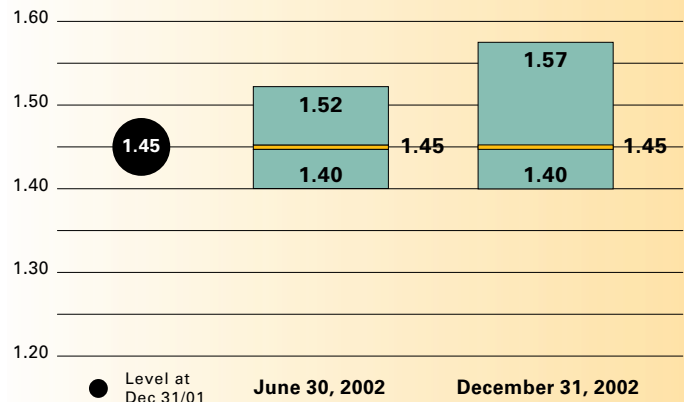
Yen/\$U.S. Exchange Rate



\$U.S./Euro Exchange Rate



\$U.S./Pound Sterling Exchange Rate



2002 FEARLESS FORECAST RESPONDENTS

Listed below are the 81 investment managers who have contributed their forecasts to this survey.

Aberdeen Murray Johnstone
Addenda Capital Inc.
Aeltus Investment Management, Inc.
AIG Global Investment Corp. (Canada)
AIM Funds Management Inc.
Altamira Investment Services Inc.
American Express Asset Management Group Inc.
AMI Partners Inc.
Aurion Capital Management Inc.
Baillie Gifford Overseas Limited
Baker Gilmore & Associates Inc.
Barclays Global Investors Canada Ltd.
Bernstein Investment Research & Management
Beutel, Goodman & Company Ltd.
Bissett Investment Management
BLC - Edmond de Rothschild Asset Management Inc.
BonaVista Asset Management Ltd.
Brandywine Asset Management, LLC
Brinson Canada Co.
Capital Guardian Trust Company
Centerfire Capital Management Inc.
Clarica Asset Management
Connor, Clark & Lunn Arrowstreet Capital Ltd.
Connor, Clark & Lunn Investment Management Ltd.
Co-operators Investment Counselling Ltd.
Deutsche Asset Management
Dresdner RCM Global Investors
Edinburgh Fund Managers PLC
Elantis Inc.
Elliott & Page Limited
Fiduciary Trust Company International
Foyston, Gordon, & Payne Inc.
Franklin Templeton Institutional
Goldman Sachs Asset Management
Grantham, Mayo, Van Otterloo & Co. LLC
Greystone Managed Investments Inc.
Guardian Capital Inc.
Hillsdale Investment Management Inc.
Invesco, Inc.
J. Zechner Associates Inc.
J.R. Senecal & Associates Investment Counsel Inc.
Jarislowsky Fraser Limited
Jones Heward Investment Counsel Inc.
JPMorgan Fleming Asset Management
KBSH Capital Management Inc.
Laketon Investment Management Ltd.
Leith Wheeler Investment Counsel Ltd.
Lincluden Management Limited
Lombard Odier International Portfolio Management Ltd.
London Life Investment Management Ltd.
Lotsoff Capital Management
Magna Vista Investment Management
Marvin & Palmer Associates Inc
McLean Budden Limited
Mellon Capital Management Corporation
MFS Institutional Advisors, Inc.
Middlefield Group
Montrusco Bolton Inc.
Morrison Williams Investment Management Ltd.
Mulvihill Capital Management Inc.
Newton Capital Management Limited
Oechsle International Advisors, LLC
Oppenheimer Capital
Optimum Asset Management Inc.
PanAgora Asset Management, Inc.
PCJ Investment Counsel Ltd.
Perigee Investment Counsel Inc.
Philippe Investment Management, Inc.
Pictet International Management Ltd.
QVGD Investors Inc.
Sceptre Investment Counsel Ltd.
Scheer, Rowlett & Associates
Standard Life Investments Inc.
State Street Global Advisors
Sun Life Quantitative Management Inc.
Synergy Asset Management Inc.
TAL Global Asset Management Inc.
TD Quantitative Capital
Turner Investment Partners, Inc.
Walter Scott & Partners Limited
YMG Capital Management Inc.

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The Investment Consulting Practice of William M. Mercer Limited provides comprehensive investment services to pension plans, foundations, endowments and other institutional investors. We are dedicated to partnering with clients in providing quality investment consulting and financial risk management services employing leading edge research and innovative tools.

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- Fund Governance
- Optimal Asset Allocation
- Asset/Liability Modelling and Risk Analysis
- Applied Immunisation Strategies
- Designing Investment Manager Structure
- Investment Manager Search and Selection
- Investment Manager Monitoring and Evaluation

- Transaction Cost Analysis
- Defined Contribution Services
- Recordkeeper Searches
- Design of Investment Option Packages
- Investment Planning Assistance
- Group Annuity Purchases
- Master Trustee/Custodian Selection
- Special Projects

For further information on the investment consulting services listed above, please call one of our offices:

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For information on the services of William M. Mercer Limited, please contact:

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Calgary 403 269 4945	London 519 672 9310	Toronto 416 868 2000	Montréal 514 285 1802	Halifax 902 429 7050	