

GLOBAL BONDS: *EASIER SAID THAN DONE?*

WHY THE SLOW RESPONSE TO FPR?

- low yields, tight spreads
- misperception of low alpha and limited diversification
- liability management
- currency risks
- complex new instruments
- new investment policies
- implementation is intimidating!



IMPLEMENTATION

Global bond alpha or beta?

Permitted assets

Derivatives

Manager
selection

Mandate

GLOBAL BONDS – ALPHA OR BETA?

<i>Alpha</i>	<i>Beta</i>
"Core plus" vs. domestic benchmark	<ul style="list-style-type: none">• Global bond manager vs. global benchmark (currency can be a big source value)• Foreign "core plus" vs. foreign benchmark
"Alpha transport" of global or specialty managers vs. domestic benchmark or liabilities	Specialty managers vs. specialty benchmark e.g. high yield, emerging markets
Hedge funds	

PERMITTED ASSETS

“Maple” bonds

Foreign issuers in Canadian dollars

Global credit

Investment grade

High Yield

Emerging Markets

CDS

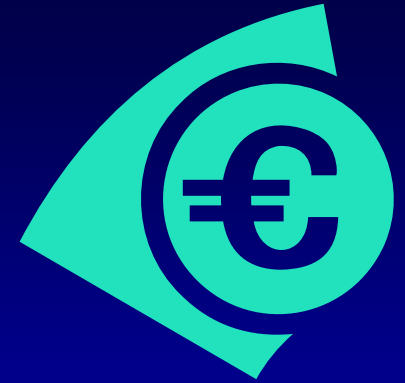
Structured Products

ABS/CDO

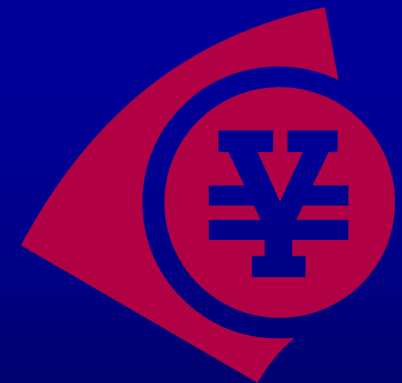
MBS

Real Return Bonds

Global government bonds



Derivatives



MAPLES – FOREIGN CREDIT RISK ONLY



Pay \$C price to buy the bond: \$C99.95

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Pay \$C price to buy the bond: \$C99.95

Earn Maple Bond Yield: Canada 5 yr + 57 bps

MAPLES – FOREIGN CREDIT RISK ONLY



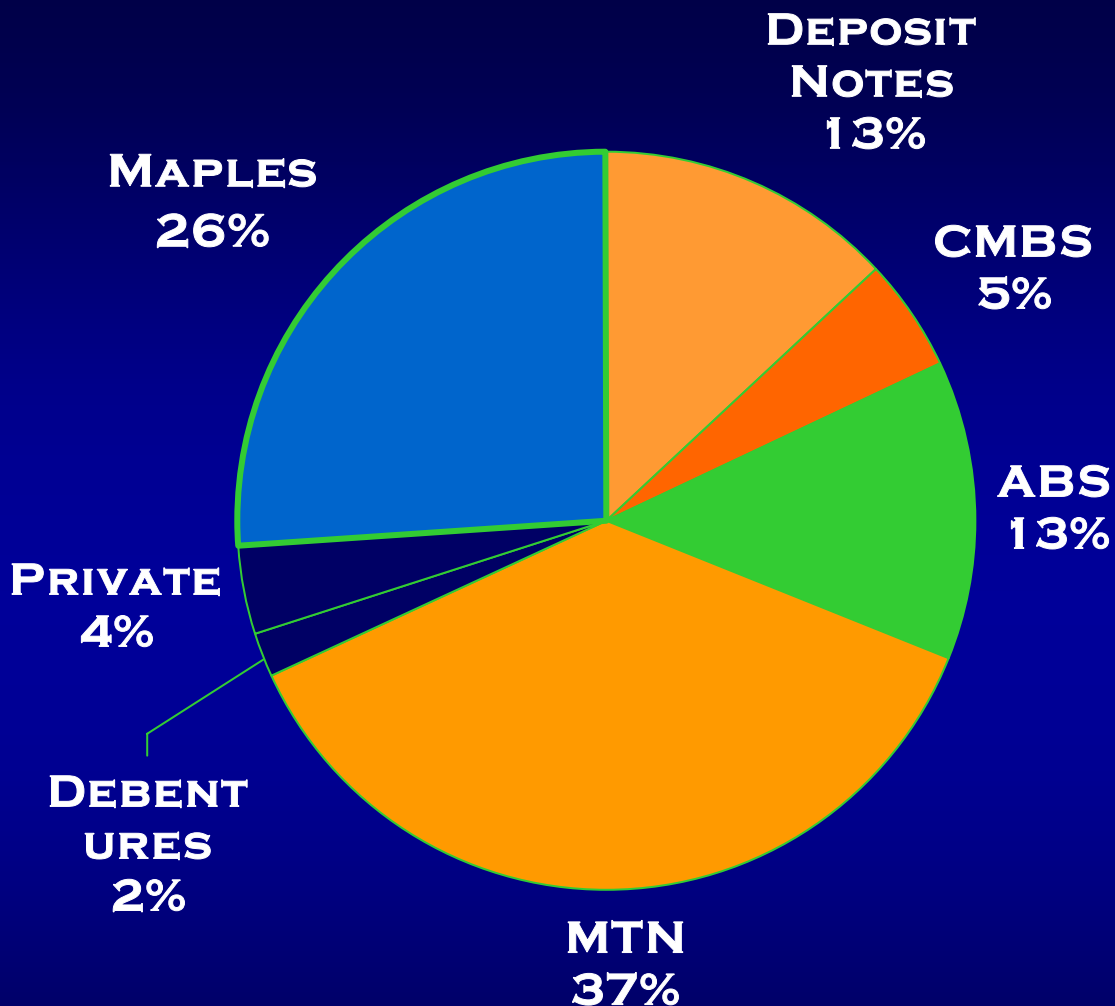
Pay \$C price to buy the bond: \$C99.95

Earn Maple Bond Yield: Canada 5 yr + 57 bps

Receive \$C par at maturity: \$C100

No currency or foreign interest rate risk.

MAPLES – HEAVY ISSUANCE THIS YEAR



So far in 2006

\$7.3 billion total

\$3 billion
corporate

26% of all non-govt
credit

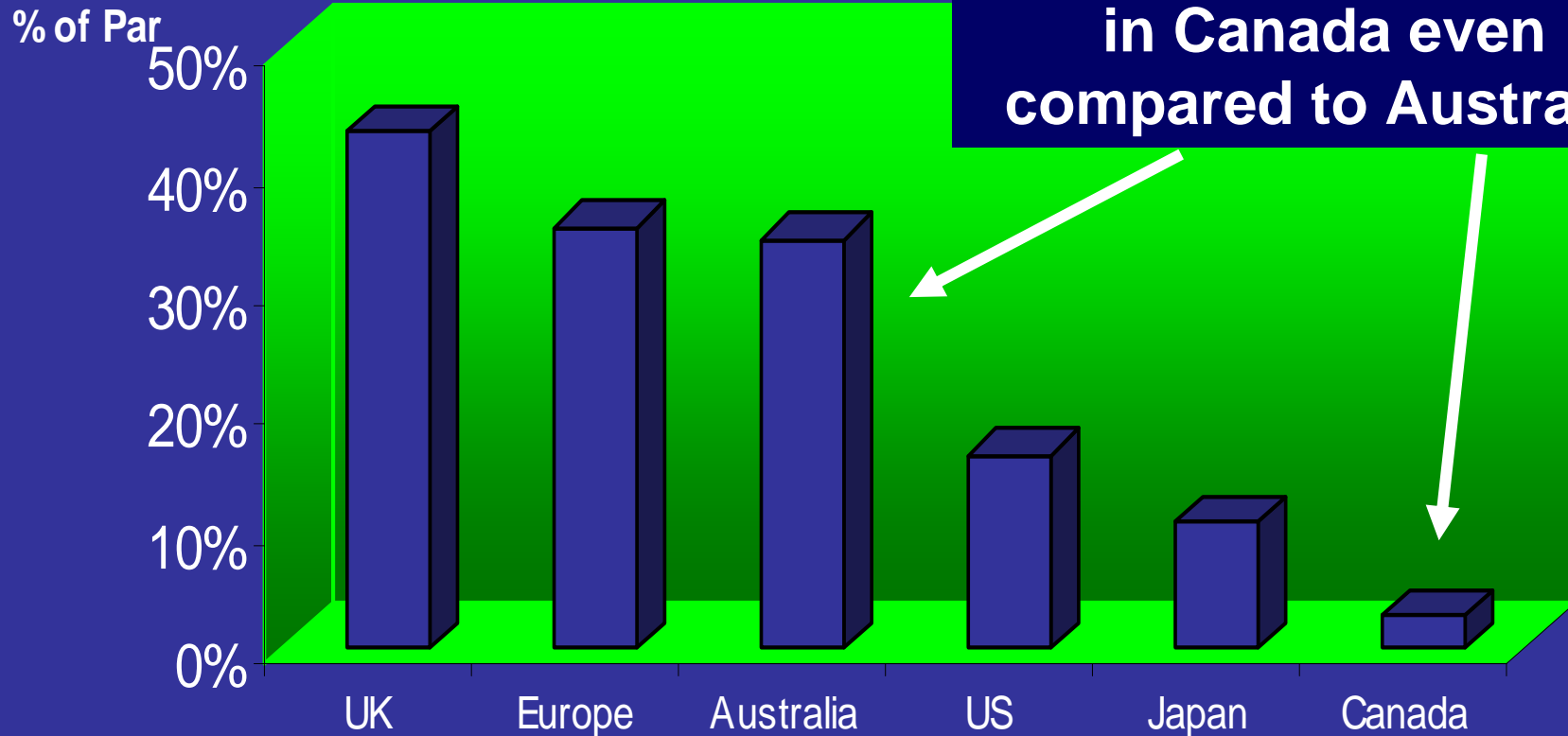
40% of corporate
bonds

Source: TD Securities. As of April 25, 2006



MAPLES – HERE TO STAY?

Still few foreign bonds
in Canada even
compared to Australia



Source: Merrill Lynch

MAPLES – MAINLY FINANCIALS SO FAR

SNCF

KOMMUNALBANKEN

**JP MORGAN
CHASE**

**BEAR
STEARNS**



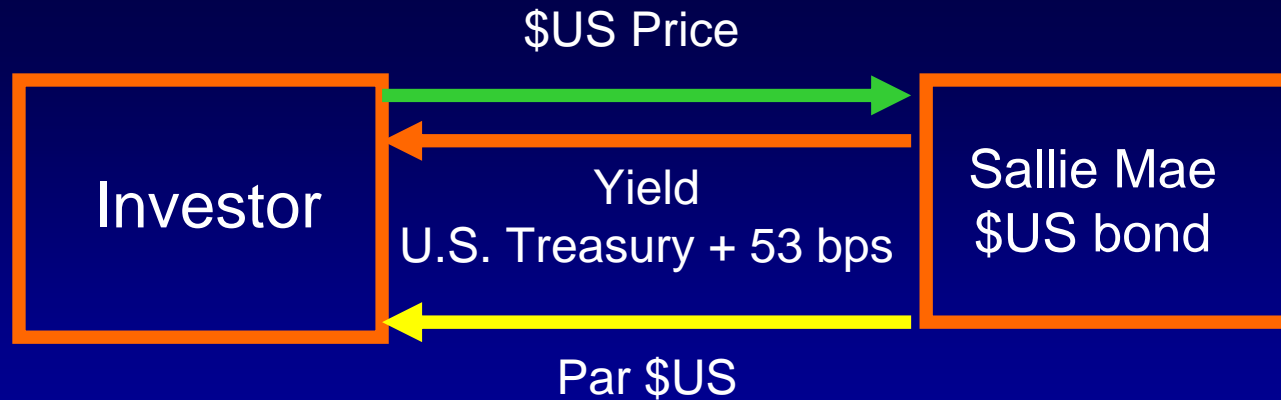
CITIGROUP

SALLIE MAE

RENTENBANK

**MORE DIVERSIFICATION IS NEEDED
SINCE 44% OF CANADIAN
CORPORATES ARE FINANCIALS**

FOREIGN BONDS – ADD CURRENCY AND FOREIGN INTEREST RATE RISKS



Pay \$US price to buy the bond: \$US 99.85

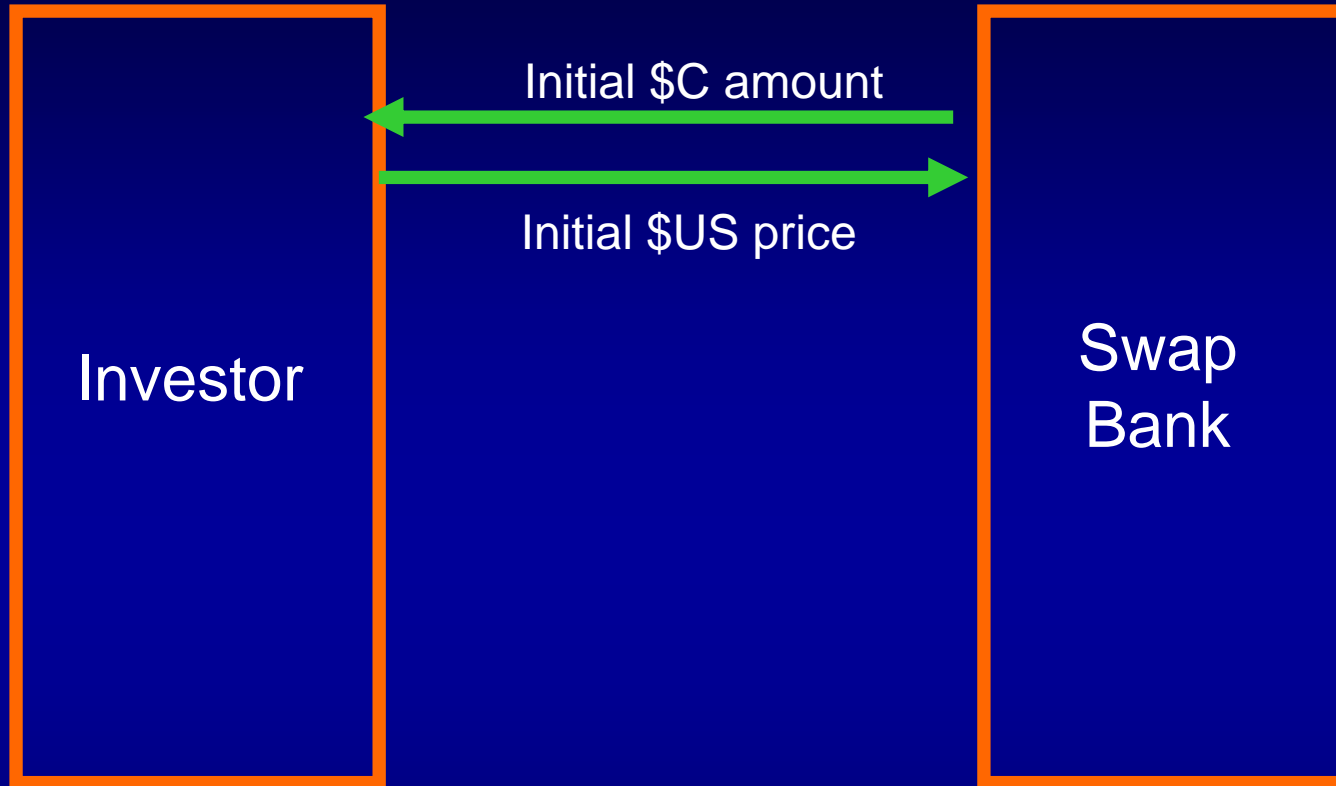
Earn Foreign Bond Yield: U.S. Treasury 5 yr + 53 bps

Receive \$US Par at maturity \$100

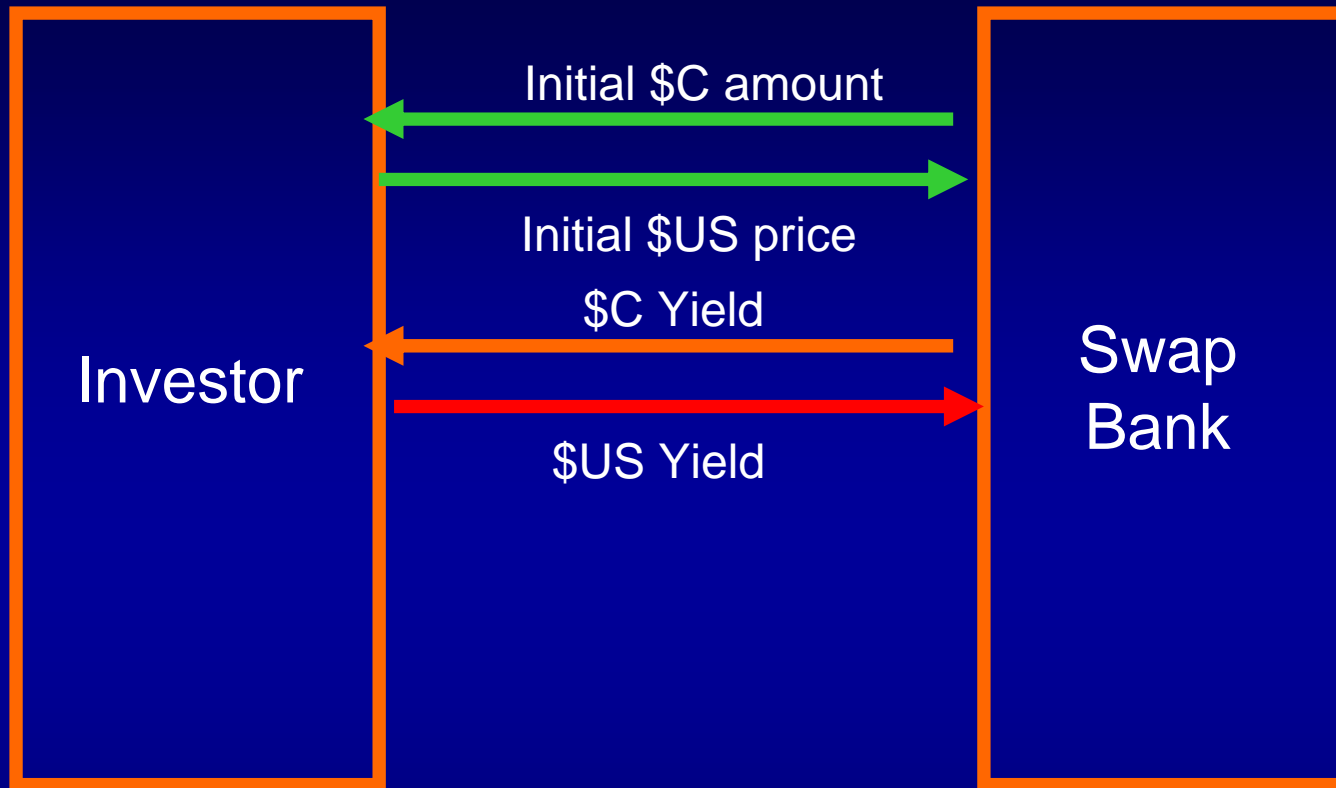
LIQUIDITY + DIVERSIFICATION

HEDGE THE UNWANTED RISKS!!

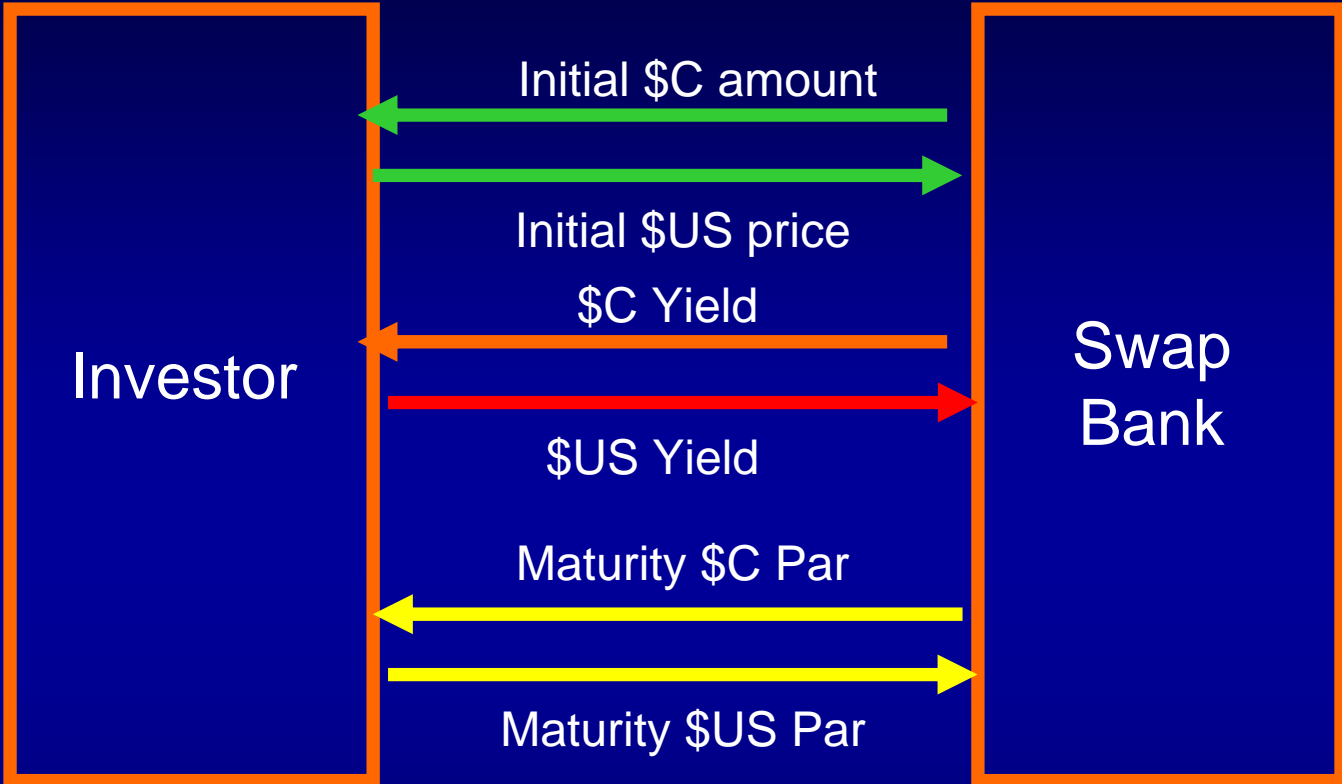
CROSS-CURRENCY ASSET SWAP



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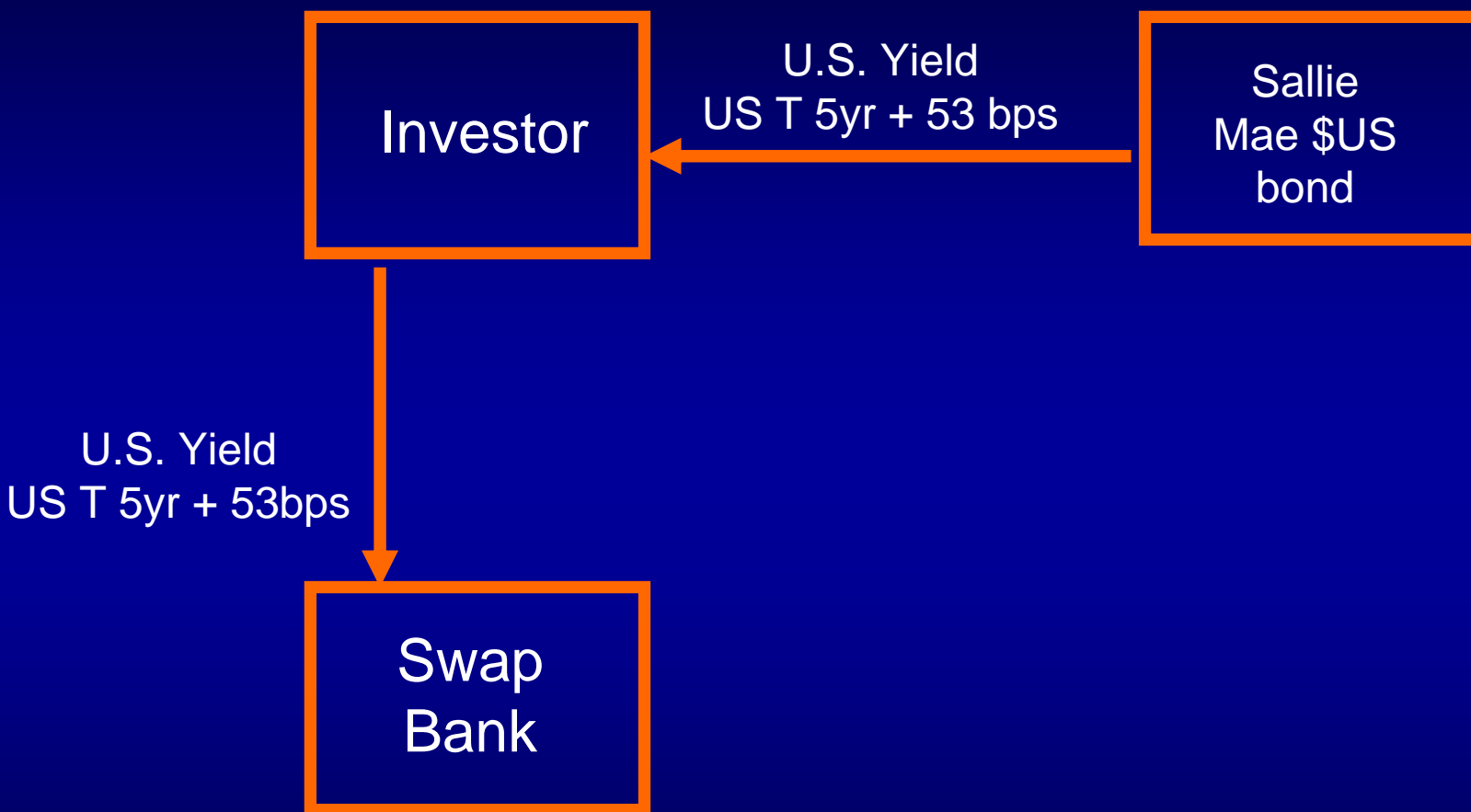
CROSS-CURRENCY ASSET SWAP



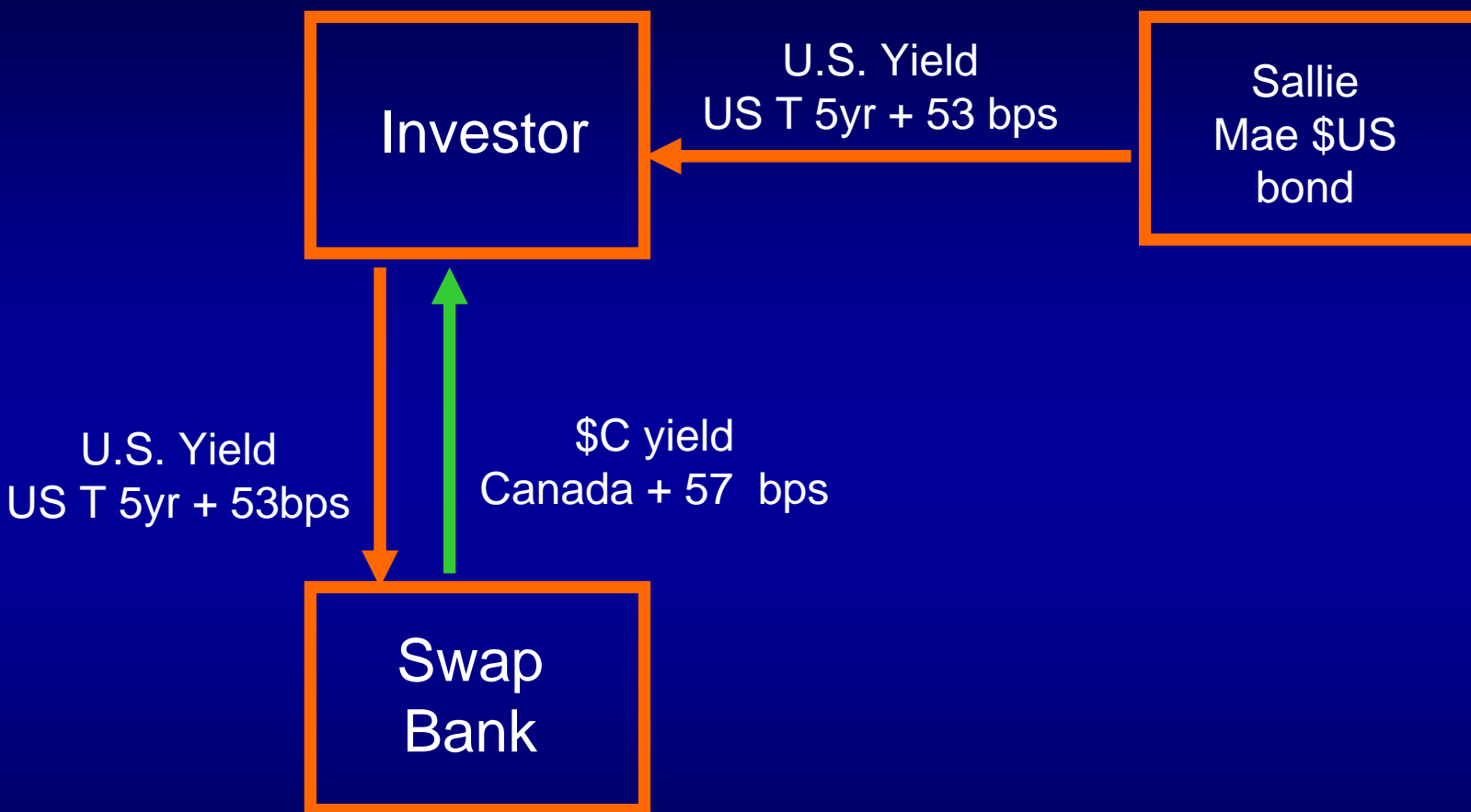
Same spot exchange rate at initiation and maturity



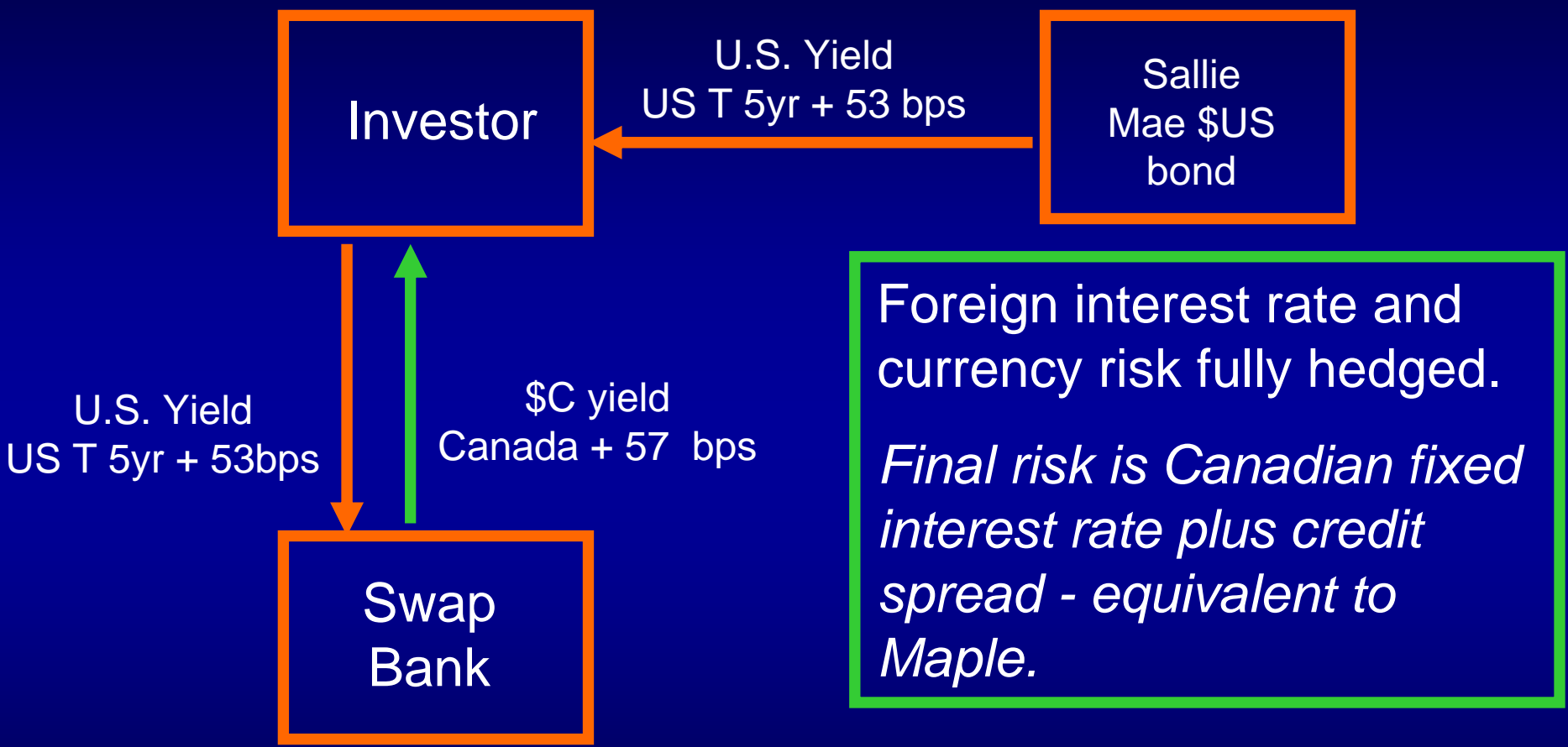
FOREIGN BOND + ASSET SWAP HEDGE



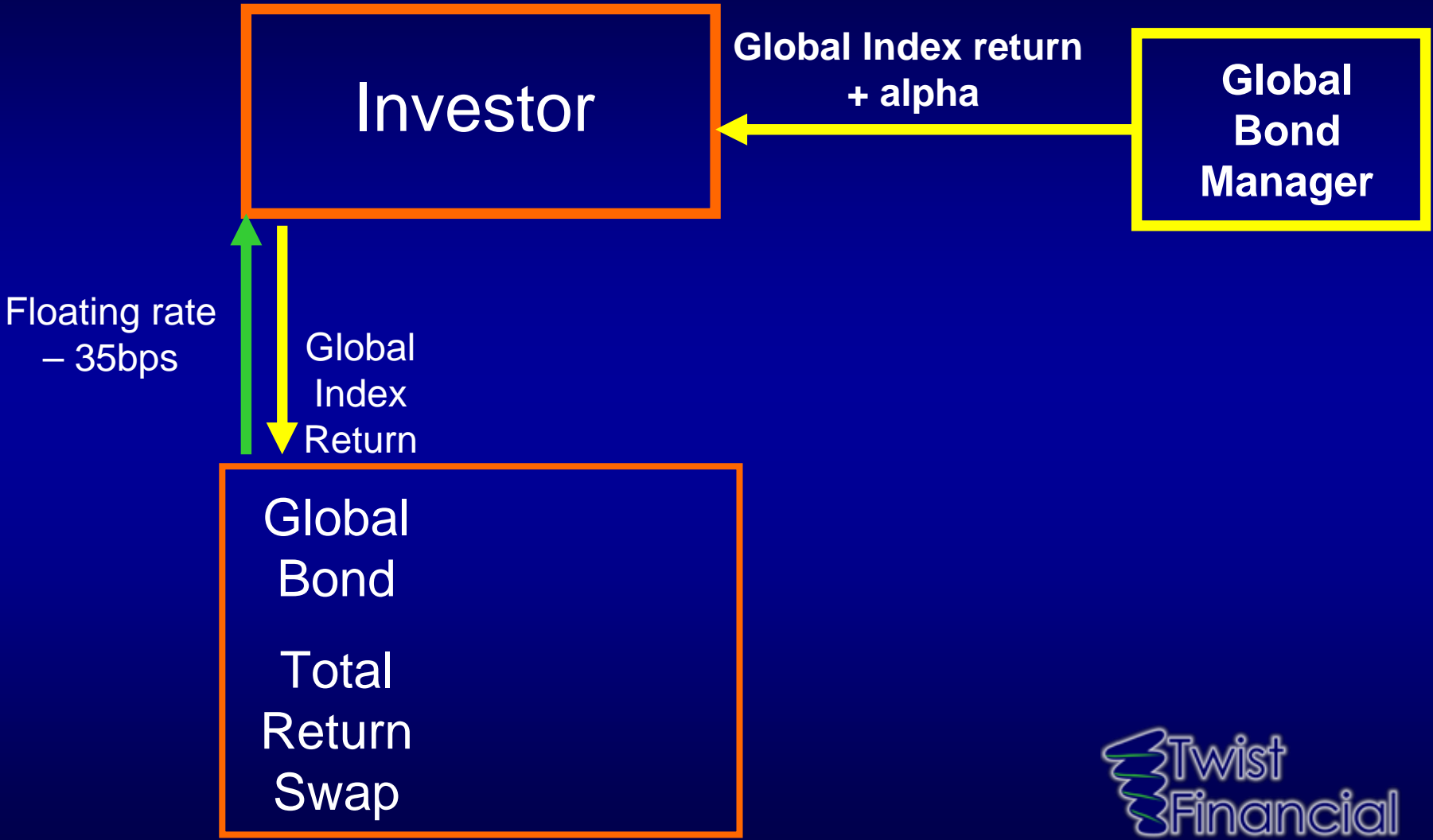
FOREIGN BOND + ASSET SWAP HEDGE



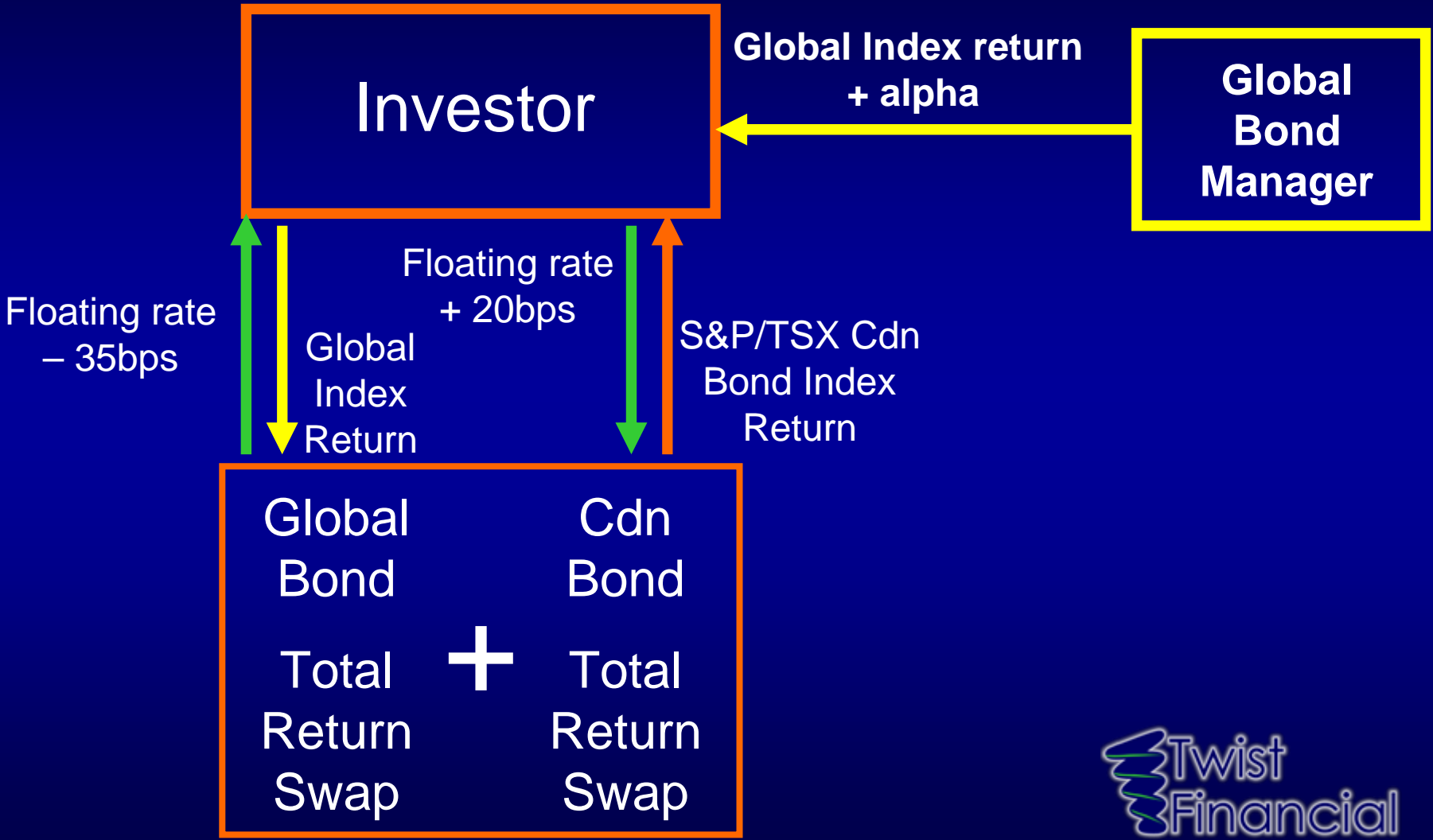
FOREIGN BOND + ASSET SWAP HEDGE



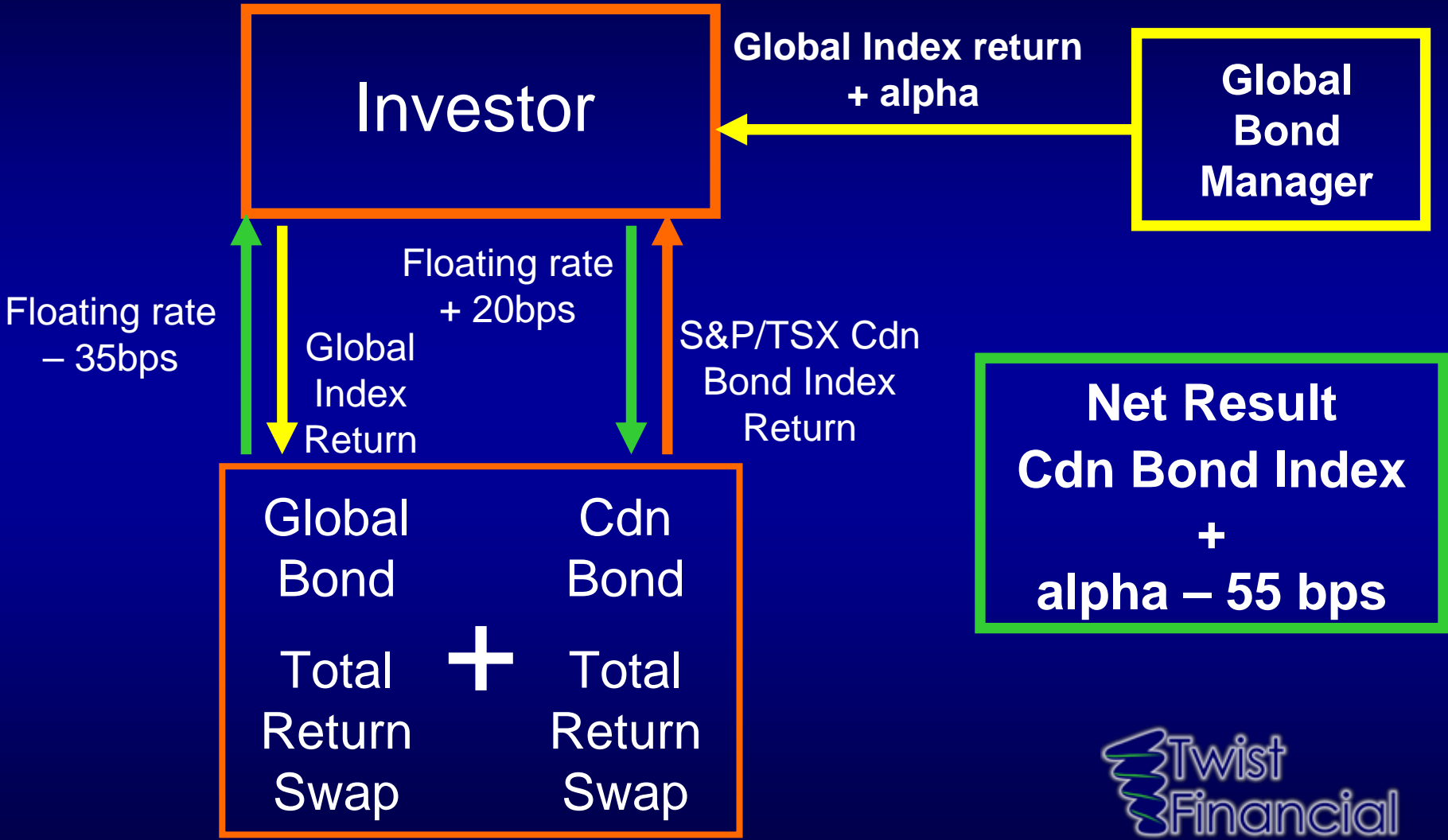
DERIVATIVES – ALPHA TRANSPORT



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DERIVATIVES - IMPLEMENTATION

- ISDA – standard documentation needed for swaps with all counterparties
- Dealers can have ISDA agreements with pooled funds - reduces documentation for individual pension plans
- Get advice on derivatives policy design

WILL PLANS GO GLOBAL?

- Alpha vs. Beta?
- Education will help
- For most plans, easy to start with adding global bonds for “alpha” vs. domestic benchmark
- Global or specialty mandates as beta or alpha transport come next
- Evaluate a variety of domestic and global managers

