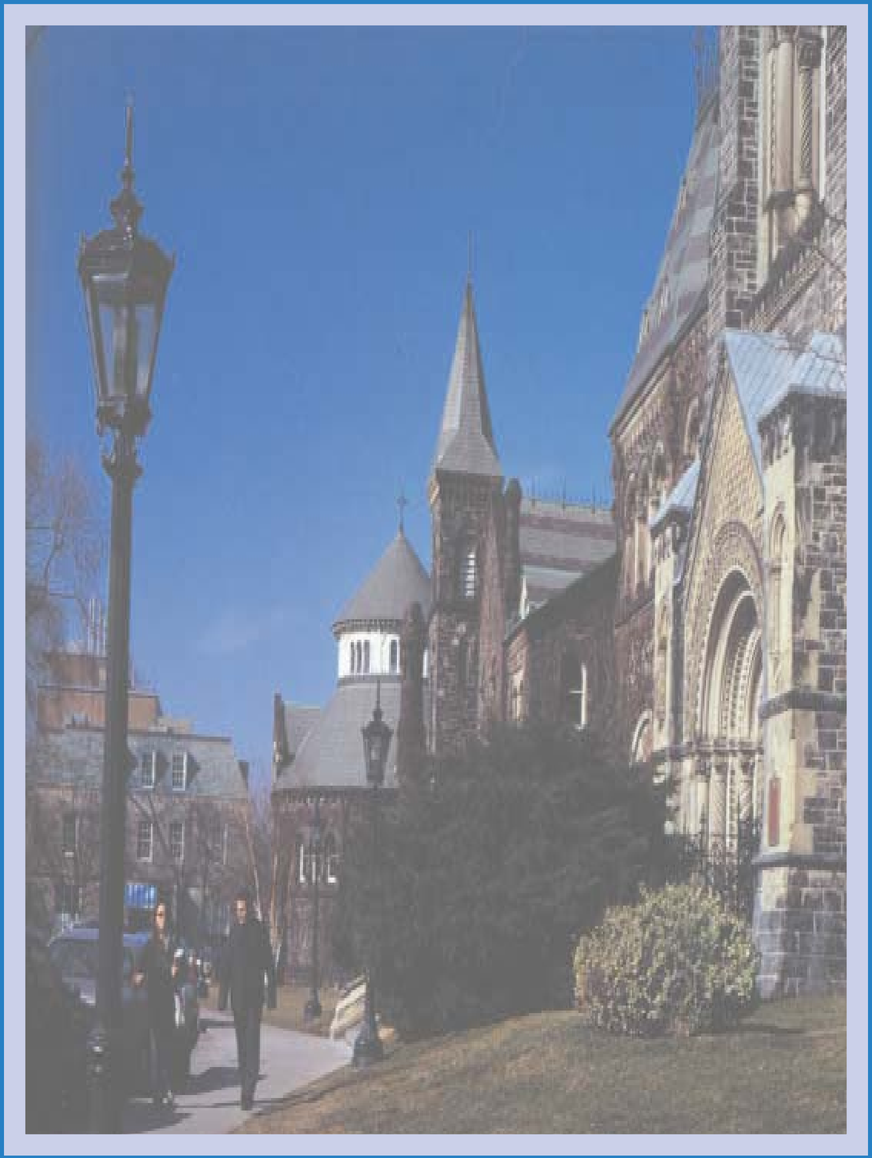
Annual Report 2001



University of Toronto Asset Management Corporation

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All returns mentioned in this report are in Canadian dollar terms, unless otherwise stated.

University of Toronto Asset Management Corporation

Annual Report 2001

Mission

The University of Toronto Asset Management Corporation strives to create added value by providing both current and future financial resources for the University and its pension funds that will contribute to globally recognized education and research.

We will strive to provide state of the art investment management with diligence, competence and the highest of professional conduct and continually seek out and formulate the best investment ideas into prudently managed portfolios that optimally balance risk and return.

Introduction and Brief History

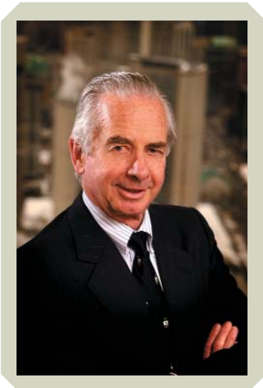
On May 1, 2000, the University of Toronto established the University of Toronto Asset Management Corporation (UTAM), a wholly-owned separately-incorporated investment subsidiary governed by an independent Board of Directors. The UTAM Board of Directors is responsible for the oversight and direction of the UTAM Corporation and reports on investments to the Business Board of the University of Toronto. Prior to the formation of UTAM, the University's investment function had been handled by its Treasury department as overseen by the President's Investment Committee.

Following its formation, during the second half of 2000, UTAM recruited and hired staff, established an office, reviewed and reset the Pension Master Trust and University Funds investment policy asset mixes and benchmarks, then implemented the revised policy mixes in December 2000. During 2001, UTAM added several employees, formed the compliance operation, enhanced the technology platform, and focused on implementing investment strategy while continuing to develop operational policies and investment processes.

Calendar year 2001 constituted the inaugural performance year for the funds, as measured to the new benchmarks, and the first full year of the asset management responsibilities being carried out by UTAM.

The audited financial statements for UTAM's operations for the year ended December 31, 2001 are presented at the end of this report. The assets managed by UTAM are held by the University of Toronto and are reported on separately and accordingly in the University's financial statements for fiscal years ending April 30 and in the University of Toronto Pension Plan and OISE Pension Plan financial statements for fiscal years ending June 30.

UTAM



I am pleased to present the second Annual Report of the University of Toronto Asset Management Corporation. This was our first full year of operation.

UTAM was established to manage the financial assets of the university. These consist of the Pension Plan, a Long Term Capital Appreciation Pool (primarily endowed assets) and the Expendable Funds Investment Pool representing the operating funds of the university. The purpose of UTAM is to preserve the purchasing power of these financial assets and to earn a return sufficient to permit the University to maintain its support for current and future generations of students and faculty as well as post-retirement benefits. It is to achieve these real return objectives over the appropriate time horizon that ranges from indefinite for LTCAP, to the average duration of 13 years for the pension liabilities, to the 2-3 year horizon of EFIP.

The table below shows that the real return target exceeded the long-term funds' performance in 2001.

Fund	Pension Fund	LTCAP
Assets ($ million)	$2,146	$1,196
Rate of Inflation	0.70%	0.70%
Required Real Rate of Return*	4.00%	5.00%
Required Nominal Rate of Return	4.70%	5.70%
Nominal Rate of Return Earned	-1.48%	-3.23%

* Does not include investment management fees.

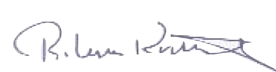
Bonds were the only asset class that added value on an inflation adjusted basis. Our funds are heavily weighted towards equity securities and, in Canada, the United States and Overseas, on average these were down in excess of 10%.

Notwithstanding the unfavourable real results, we still hold the belief that a mix of 20% to 30% bonds and 80% to 70% stocks will over sufficiently long periods provide returns in excess of our objectives. We also believe that diversification can increase return and reduce risk. Finally we believe that while markets are efficient, there are times and places of inefficiency that we can successfully exploit.

In the report of the President, you will see that during 2001 we made considerable progress at diversifying our portfolios and that we have moved a significant amount from passive to active management. We have also invested in smaller companies and pursued absolute return strategies and these are described more fully in his report. These initiatives mitigated the losses we would have incurred had we remained a passive investor in global equities.

Staff complement grew during 2001. At the beginning of the year, a fourth Managing Director came on board, completing the investment team and a Compliance Manager was added to oversee internal processes and to contribute to the due diligence carried out on external managers' operations. An Administrative Secretary was hired to help balance the load, bringing full-time staff up to twelve persons.

Equity markets rarely experience two negative years in a row. UTAM started up during one of these rare periods for the equity markets in the United States and Overseas. Nevertheless, much has been accomplished and a strong foundation has been built. This investment should yield higher real return as we go forward. The Board of Directors recognizes this and on their behalf I wish to express their thanks for the dedication and hard work of our staff.



Robert W. Korthals
Chairman

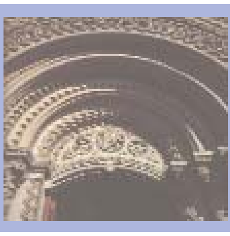
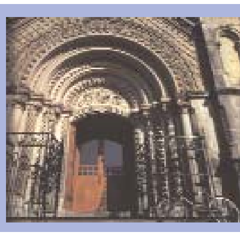
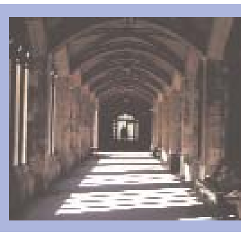
It is a pleasure to report on the first full year of operations since UTAM was established May 1, 2000. An enormous amount was accomplished in 2001 in the midst of a continually deteriorating economic and investment landscape, which culminated with the tragic events of September 11. Our accomplishments enabled us to mitigate capital loss as well as to take advantage of several attractive investment strategies, which we expect will add significant value going forward. While the pace of change was considerable, it was a necessity due to the rapid acceleration of the market downturn that began in the spring of 2000. A number of new mandates were added in both the North-American and International equity portfolios. Early in the year we launched an extensive effort to establish a strong compliance and risk management function. This enabled us to begin in-house investment management in the fourth quarter, a function that is likely to grow significantly in the next year.

There is evidence that leads one to the conclusion that diversification may play an increasingly significant role over the next few years. Given reasonable and rational forecasts of world GDP growth over the next several quarters, it is likely to be very difficult to generate an attractive real rate of return in 2002. Increasing correlations of world equity markets are making it harder to obtain diversification. At the same time, market volatility is significantly increasing the need for diversification. Historically, investment practitioners believed that investing in representative market indexes such as the S&P 500 provided adequate diversification. Over the past few years, it has become apparent that diversification solely through indexing does not provide adequate downside protection. As an obvious example, passively holding the full index weight in a stock like Nortel Networks that plunged more than 75% last year would not have served capital protection within the funds.

Clearly, we must adapt to these new conditions, though we must distinguish between temporary anomalies and secular change. One of the greatest challenges of management in any industry is to recognize the difference between fads and actual industry metamorphosis. The inability to distinguish between the two can bring about disastrous results. In hindsight, the belief in ongoing and sustained double and triple digit growth of "new economy" companies at the peak of NASDAQ was clearly a fad. Fads in the investment management industry can be dangerous in that they are not predicated on sound financial theory.

There is also a large risk in the inability to recognize fundamental industry changes. Investment manager performance over the past two decades led many institutional investors to the belief that active equity management is a zero-sum game and, given the difficulty in selecting active managers who can consistently outperform their benchmarks, institutions are better off with a passive or indexed strategy. However, market performance of the past 18 months has brought to light the lack of downside protection and risk management shortfalls of a purely passive management strategy.

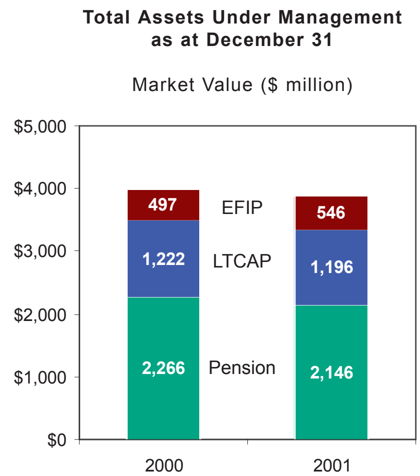
At UTAM, we recognize the need to use a wide array of strategies in order to optimize the risk and return profile of funds under management. We are seeing fundamental change in the investment

management industry, in that many conventional money managers are developing and managing what have traditionally been referred to as "alternative products". Long and short equity management, arbitrage strategies and other niche opportunities that were once considered cottage industries are rapidly becoming institutionalized as money managers recognize the difficulty in consistently generating attractive returns through conventional money management techniques. In looking at the dramatic changes in so many industries brought about by changes in technology and information management, it is not surprising to see these developments occurring in the investment management industry. At the same time, however, we recognize the need to use a wide range of tools in the portfolio management process. No single strategy, whether it is passive or active, conventional or alternative, can provide a total solution. We believe that relying too heavily on any one investment strategy or style can weaken the risk management process and lead to disappointing long-term results. An integral aspect of our risk management process is to maintain a balance across a range of strategies and continually monitor and evaluate the strategy mix.

Our significant diversification of funds under management over the past year has greatly intensified our need for focused risk management and oversight. We recognize that investment management is both an art and a science, which necessitates thorough qualitative and subjective analysis in addition to quantitative analysis. The cohesiveness of the UTAM team that has developed in our first full year of operations will continue to ensure our dedication and focus on this process.

Donald W. Lindsey
President and CEO



UTAM oversees the investment of the University of Toronto's three main asset pools. These three investment pools had an aggregate market value of $3.9 billion as at December 31, 2001, and their descriptions follow.

Pension Master Trust (Pension)

The Pension combines for investment purposes the assets of the University of Toronto Pension Plan and the University of Toronto OISE Pension Plan. The Pension fund had a market value of $2,146 million as at December 31, 2001 compared to $2,266 million as at December 31, 2000. The slight decline in market value was due to two factors: equity markets around the world declined in a very difficult investment environment and the Pension fund had net cash outflows as payments to beneficiaries were far larger than contributions.

Long-Term Capital Appreciation Pool (LTCAP)

LTCAP is composed primarily of endowed assets, including quasi-endowments which are unrestricted funds designated long-term by the University of Toronto. LTCAP had a market value of $1,196 million as at December 31, 2001 compared to $1,222 million one year earlier. The slight decrease in market value reflects declines in capital markets and incorporates the fund's cash inflows from contributed donations and outflows for university endowed spending.

Expendable Funds Investment Pool (EFIP)

EFIP consists of short and medium term operating funds of the University of Toronto. It includes government grants and student fees as well as ancillary operations revenue, capital funds, donations, research grants and trust funds. EFIP had a market value of $546 million as at December 31, 2001 compared to $497 million at the end of the previous year. The increase in market value was primarily due to positive cashflows from donations.

In addition to the three principal pools, total other investments of $213 million as at December 31, 2001 were managed by UTAM. These included capital held temporarily in reserve for University building projects and a series of specifically invested trust funds, consisting of endowed and expendable assets that are segregated for investment due to the conditions and constraints of each trust.

Asset mix refers to the policy weights in specific asset classes, such as U.S. equities and Canadian bonds, that the funds are normally expected to hold. The asset mix is described in terms of target weights in selected capital market indexes, such as the Russell 3000 Index and the Scotia Capital bond indexes, and this composite of indexes constitutes the performance benchmark for the assets under management. The benchmark expresses the target levels of investment rate of return and corresponding risk (volatility of returns) that a fund's assets may assume in order to meet that fund's liabilities. Most academic and investment industry studies have demonstrated that asset mix is the single largest determinant of fund performance. The asset mix decision is so critical to the success of an investment program, that prudent person rules require that it be stated in full clarity and transparency within the policies that govern the fiduciaries that oversee and invest institutional funds. The asset mix and corresponding performance benchmark are therefore the purest presentable expression of investment goals and responsibilities.

The bar charts in this section illustrate the December 31, 2001 year-end asset mix compared to the policy asset mix for each of the funds, Pension, LTCAP, and EFIP.

The three policy asset mixes that became effective on January 1, 2001 were established by UTAM in a concerted process with the University of Toronto that took place during calendar year 2000. The process of establishing appropriate asset mixes involved a rigorous review of each fund's obligations and stated objectives and took a ten-year forward-looking view in its assessment of the prospects for capital markets. The process resulted in the approval of major changes to the investment policies by the University's Business Board in November 2000. The conversion of the legacy Pension, LTCAP and EFIP portfolios to the newly-adopted benchmarks began in December 2000 and the target asset class weights were attained in early January 2001. Through 2001, a great deal of effort was devoted to developing the investment programs within the constituent asset classes and this is discussed in detail in this report.

The investment policies describe a unique asset mix for each of the three funds according to the individual fund's obligations, objectives and investment constraints (such as time horizon, liquidity needs, and regulatory issues.) A central feature of each fund's asset mix is its normal equity-to-fixed income ratio. Each policy also defines ranges, or policy bounds, within which the asset class weights are allowed to vary.

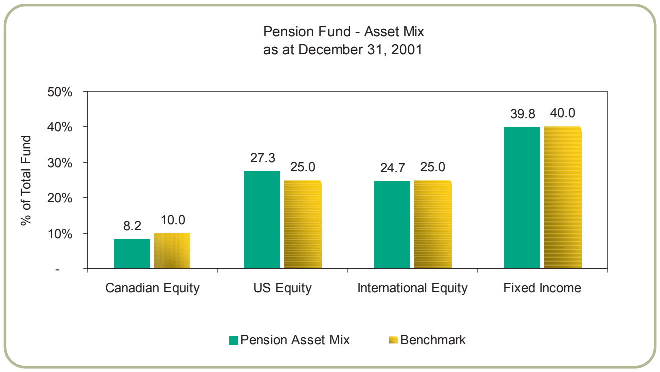
The policy equity-to-fixed income ratio represents the parameters for the amount of investment risk the fund assets may normally assume. Policies with higher equity targets are suitable for funds with higher return objectives and a correspondingly greater ability to assume investment risk, which is typically in line with the fund having a long investment horizon. Conversely, a higher fixed-income weight in the ratio signifies a lower rate of return target and a requirement to moderate investment risk (volatility of returns), usually in order to meet liquidity needs relating to the fund's particular obligations.

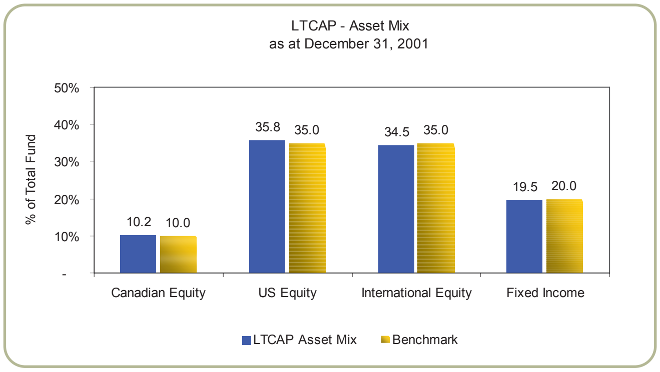
Each fund's actual and benchmark asset class weightings are illustrated in this section accompanied by summary descriptions of the chief determinants of its policy asset mix.

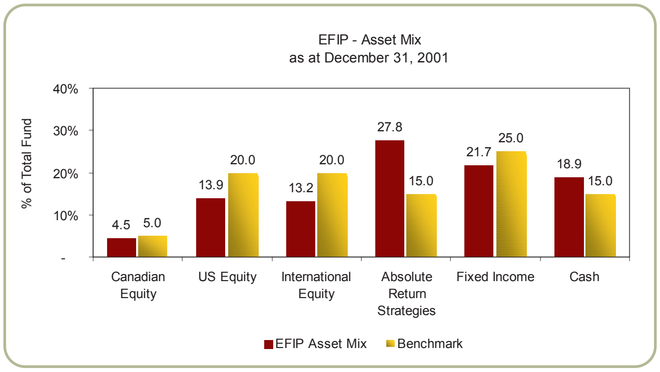
The policy asset mix for the Pension is 60% equities and 40% fixed income. The 60-40 mix is appropriate for the Pension fund's investment horizon, which is a function of the relative maturity of the University of Toronto Pension Plan participants' profile. The Pension fund's equity weighting is permitted to vary within a range of 50% to 70% of total fund. The policy weights for the Canadian, U.S. and international equity classes are described in the next section (page 9).

The LTCAP is a perpetual investment fund representing endowments and designated long-term assets. The LTCAP's policy asset mix is 80% equities and 20% fixed income, a mix that is suitable for endowment funds that are established to permanently support University academic and research activities through a stream of stable payouts. This heavy equity weighting, which is permitted to vary between 70% and 90% of the total fund, indicates willingness to accept a high degree of risk in order to meet the primary target for endowed spending of 5% of the market value over four-year rolling periods. A facet of endowment investing is the requirement that assets be exposed to sufficient investment risk in order to produce a return that will protect the endowment capital and provide for the endowed spending that is aligned with an ambitious real return target. The overriding objective of University endowment management is to provide purchasing power evenly to endowment beneficiaries both today and into the indefinite future. This requires coordination of the investment program with the spending formula so that present-day academic activities are not over-supplied with endowment funding at the expense of their successors in generations from now, nor vice versa. Endowment fiduciaries are responsible for achieving these dual and sometimes conflicting objectives of protecting the value of the endowment corpus while providing for a sustained and meaningful level of inflation-adjusted spending.

The EFIP pool is made up of University operating funds that normally are expended within one-month to three-years from receipt. Analysis of the University of Toronto's revenue-expense cycle has resulted in identification of a core of assets that are available for investment over a longer period. This core is deemed quasi-endowment and is exposed to greater investment risk with the objective of having those funds work to enhance the returns to University operations. EFIP may hold an equity exposure of up to 60% of the total fund while 25% of the fund is managed in low-volatility, short-duration strategies and 15% on average is held in cash to meet operational liquidity needs.







MANAGEMENT OF INVESTMENT RISK

The management of investments and their attendant multitude of risks is the primary focus of UTAM. Since risks may be defined within an endless universe of possibilities, to effectively deal with this plentitude the focus must fall upon a manageable and critical set. The greatest risk to a fund is the possibility that the asset mix and accompanying investment strategy will fail to meet the obligations of that fund. To deal with this risk, UTAM and its Board of Directors are committed to continually revisiting and developing our understanding of the needs and expectations for the University of Toronto's pension plan, endowment fund, and operating funds. The requirement to develop shared expectations and work on this matter together with the University's senior management is paramount.

The risks associated with assigning and overseeing the allocations among investment strategies, styles, and manager mandates are further myriad. A significant few of these ongoing concerns are described here.

As a manager of managers, UTAM is responsible for selecting and assigning mandates to investment professionals with demonstrated skills. The process that describes the work of allocating to and monitoring external managers is known as due diligence and is conducted by UTAM on an investment and operational compliance level. The risk that due diligence has not gone deep enough, or perhaps has relaxed over time resulting in the potential for a conflict of interest, is of supreme concern. UTAM takes very seriously its duties to protect the interests of the funds' beneficiaries, and that is best effected through nurturing an organizational culture of transparency and high professional standards. In turn, UTAM expects the external professionals that we choose to work with to uphold these same standards of practice. UTAM has adopted the Code of Ethics and Standards of Practice that are governed by the Association of Investment Management and Research (AIMR) and we are dedicated to these established standards.

Concentrations of exposures within any security, sector, style, or strategy, that deviate from that security, sector, style or strategy's normal weighting in the investable set have repeatedly in the past resulted in excessive volatility and disappointment. The act of pursuing in excess a tactic that appears to be winning, likely due to momentum, severely puts the assets at risk. Knowledge and responsiveness to this danger, sometimes in the face of criticism, will distinguish marginal policies from those that are successful in the long run. A key implication is that ensuring broad diversification of the assets is a primary duty, that exposures must be many and controlled in magnitude. A further implication is that investors must have the courage to sustain their philosophy during periods when out-of-favour exposures might be hurting performance.

Strategies that employ derivatives and long-short security positions tend to be more complex than traditional investments thus raising the requirement for sophisticated knowledge. UTAM's professionals therefore strive to grow investment knowledge as we realize that the performance prospects for certain complex investment strategies exceed those that may be available from more traditional strategies.

Geographic Diversification

UTAM's philosophy of broad geographic diversification has led to the adoption of policy asset mixes that reflect the capitalization-weighted distribution of world markets. The equity weightings in the Pension, LTCAP, and EFIP benchmarks reflect that the U.S. equity market is the single largest equity market worldwide representing approximately one half of the world's capitalization, international markets make up the other half, and Canadian markets constitute less than 3% of the total world capitalization.

A slight home market bias has been allowed to prevail in the Canadian equity weightings within the asset mixes. The reality of a limited opportunity set in Canadian equities led to the new benchmarks' moderated Canadian equity policy weight of 10% in both Pension and LTCAP, as prior to 2001, the Canadian equity benchmark weights had been 40% of each fund. The balance of the equity policy weights for each fund have been split equally between U.S. equities and international equities, mirroring the actual distribution of global market capitalization.

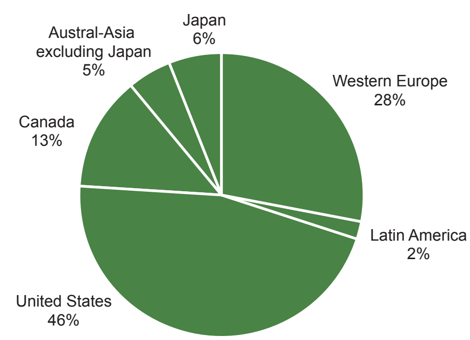
Therefore, as shown in the previous bar charts (page 7), the Pension equity policy weight of 60% is split into policy weights of 10% for Canadian equities, 25% for U.S. equities and 25% for international equities. The LTCAP equity policy weight of 80% is split into policy weights of 10% for Canadian equities, 35% for U.S. equities and 35% for international equities.

In the U.S., the Russell 3000 Index replaced the S&P 500 Index as the policy benchmark for U.S. equities due to its broader representation of the U.S. equity market. Introduction of the Russell 3000 Index redressed the large capitalization bias in the S&P 500 by including 2,500 mid- and small-capitalization equities in its composition. This benchmark index is a reasonable representation of the U.S. equity universe that is the selection territory for UTAM's U.S. equity managers.

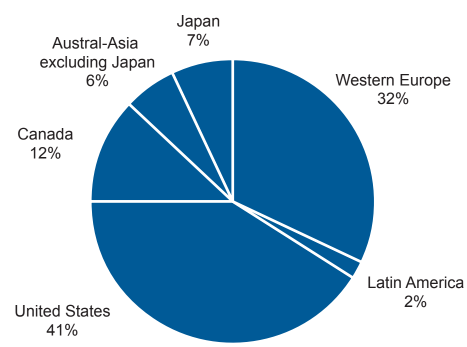
The international equity segments of the funds are generally invested in developed non-North-American capital markets, as represented by the Morgan Stanley Capital International Europe, Australasia, and Far East (MSCI EAFE) Index. The Canadian equity reference benchmark is the Toronto Stock Exchange (TSE) 300 Index.

Pension Fund Geographical Distribution of Equity as at December 31, 2001

Pension Fund Foreign Content: 27.40%



LTCAP Fund Geographical Distribution of Equity as at December 31, 2001



The pie charts depict the actual geographical distribution of the equity segments for Pension and LTCAP as of December 31, 2001.

Fixed Income

The fixed income segments of LTCAP and EFIP have been managed on an all-passive, all-Canadian basis for the last five years. At the beginning of 2001, the benchmark for Canadian fixed income was revised and tilted toward a longer duration, approximately 7.5 years, by establishing policy weights within the fixed income segments of 60% Scotia Capital Universe Bond Index and 40% Scotia Capital Long Term Bond Index. (Duration expressed in years is a measure of investment risk in fixed income portfolios.) The Universe-Long Bond combination is designed to produce a higher return and improved diversification benefits over the long term and in order to do this, an additional degree of risk relative to the Universe Bond Index is assumed. A key requirement of the fixed income segment is to provide for enhanced protection of pension and endowment funds during disinflationary periods when interest rates are falling and bond prices are rising. This roughly was characteristic of the recent environment and a further benefit was the reduction in correlations between fixed income and equity returns.

Pension Foreign Content

The deemed foreign content of the Pension fund was 27.4% at December 31, 2001, as measured on a book value basis, which provided a 2.6% cushion versus the 30% foreign content limit. At the end of 2000, the Pension's foreign content had been 20.5%. The 6.9% increase during 2001 reflected key factors: the federally regulated increase to 30% from 25% in permitted pension fund foreign content; the increased investment policy allocations to U.S. and international equities; and, a shift of assets from synthetic to active mandates.

The Federal Income Tax Act restricts pension funds to a maximum book value holding of 30% in non-Canadian assets; this constraint is in sharp contrast to the approximate 97% of non-Canadian assets represented by the world's investable markets.

The 20% gap between the Pension's policy asset mix of 50% and the foreign content restriction of 30% affects over $400 million of Pension investments, causing these assets to be exposed to a limited subset of foreign economic exposures. Generally, this differential exposure between the target foreign equities weighting and the allowable foreign content has been invested in synthetic and mostly-passive strategies that are deemed Canadian content due to their structure and use of derivatives. Synthetic strategies are legal, in compliance with the Income Tax Act, and supported by Revenue Canada, but they are not ideal.

Passive synthetic equity strategies generate index-like returns and expose the assets to levels of risk that correspond to the underlying equity indexes. Funds invested in synthetic strategies have generally foregone opportunities for pursuing a risk-adjusted reward. Increasingly in the present market environment, benefits are available from investing with superior active managers focused on security selection and controlled levels of risk. In sum, the foreign content limit effectively restricts the use of active management in the Pension fund, which puts a significant constraint upon UTAM's strategies for producing risk-adjusted return above that available from passive investing.

The foreign content regulation, though relaxed somewhat in recent years, has long contributed to frustration in the Canadian pension institutional market where UTAM shares the opinion that the limitation increases both the cost and the risks to investing Canadian pension assets. In contrast to the Pension fund, the University's endowment monetarily benefits from the ability to diversify freely within the bounds of investment policy into the U.S. and international markets.

Foreign Currency Exposure

The adoption of the new benchmarks at the outset of 2001 ushered in considerably greater non-Canadian exposure for the three main funds and a coincident greater exposure to foreign currencies and accompanying exchange rate volatility. For example, the Pension fund previously had a benchmark weight of 20% in foreign equity which was raised to 50%, effective January 1, 2001. The LTCAP's policy asset mix was revised from 30% foreign equity to 70% foreign equity also beginning in 2001. EFIP's benchmark, which formerly had a zero weighting in non-Canadian assets, was revised for 2001 to an allocation to foreign assets of up to 60% of the total fund. Approximately one-quarter of all assets under management, or $1.0 billion, moved from Canadian to foreign investments at the beginning of the year and, in all, over half of all assets overseen by UTAM are invested outside Canada.

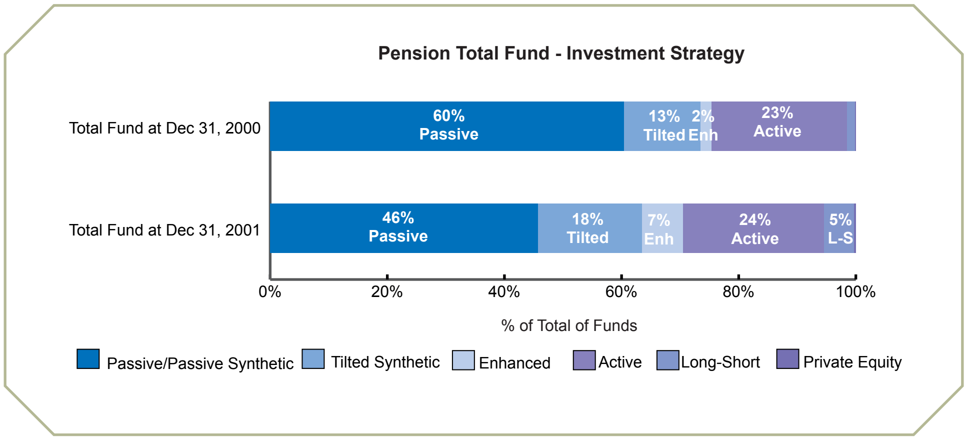
UTAM has instituted a currency risk management program in the form of a currency overlay that partially hedges the currency exposure of the non-Canadian dollar denominated assets. The purpose of the currency management program is to moderate returns volatility arising from the impact of exchange rate volatility without speculation as to the direction of currency movements. This program was run passively for most of 2001, then in October 2001 was converted to an active strategy overseen by an external currency specialist.

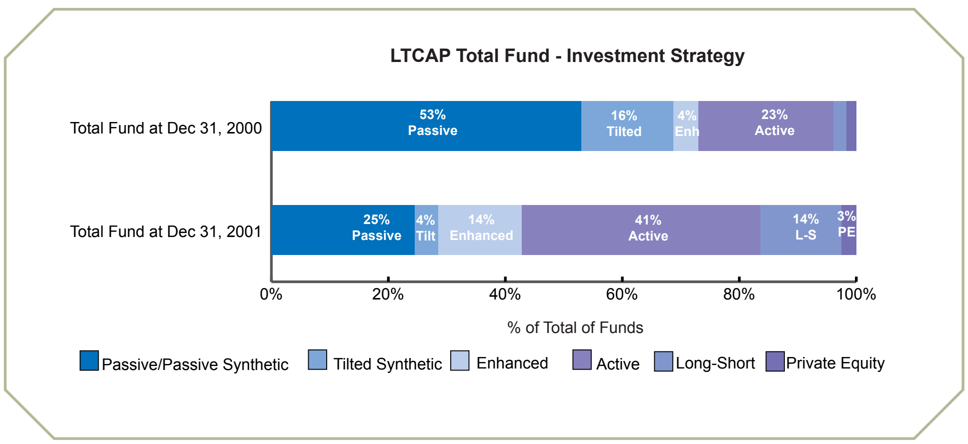
Manager Strategies and Styles

Within each asset class, UTAM combines strategies that broadly include passive, passive-synthetic, enhanced index, capitalization-tilted synthetic, and active management approaches to long-only investing in publicly-traded securities.

Passive management is the process of replicating a particular index such as the Scotia Capital Universe Bond Index or the Russell 3000 Index. Replication may be in full, through holding all the individual securities that comprise the index, or selective through stratified portfolio construction or sampling of securities to produce portfolios that closely parallel index characteristics. Alternatively, synthetic strategies may be used to produce the total return of an index through the use of other instruments; in these portfolios, the asset is recreated through holding positions in equity index futures contracts on a non-leveraged basis collateralized with high-quality, short-term debt instruments. Enhanced indexation is a hybrid of active and passive management whereby the portfolio managers will replicate the index usually with fewer securities than in the index and by slightly over-weighting and under-weighting individual equities for the purpose of adding incremental value. A tilted synthetic strategy overweights or underweights the various capitalization-sized segments of the market based on relative performance expectations. Active portfolio managers build portfolios of equities designed to outperform the broad equity markets.

Within the actively-managed segments, mandates are diversified by style. Manager styles represented in the equity segments, range across value and growth specializations, concentration by capitalization size, and differing philosophies for combining quantitative, qualitative and fundamental investment analysis in the portfolio management process. Investment style refers to the criteria investment managers use to select securities for a portfolio and a common style distinction is between value and growth. Value managers screen for equities that, for example, trade at a low multiple of price to earnings relative to the broad market with the expectation that these equities are undervalued relative to the broad market and will move up in price. Growth managers select equities with earnings growth rates that are higher than the broad markets. Consequently they tend to trade at a price to earnings multiple that is higher than the broad





market, but with the expectation that their higher growth will translate into equity price growth that outpaces the market. Low price-to-earnings equities dominated this past year's equity performance.

To this style-diversified mix, UTAM has introduced hedge funds and private equity partnerships. Hedge fund managers are hired to pursue long-short strategies that involve buying undervalued securities that are expected to increase in price and simultaneously borrowing and selling securities perceived to be overvalued that are expected to decline in price. The component of the portfolio that is sold short also acts as a hedge against broad market declines. Private equity partnerships invest in privately-held corporations in which fundamental changes are effected prior to a sale of the company or a public equity offering.

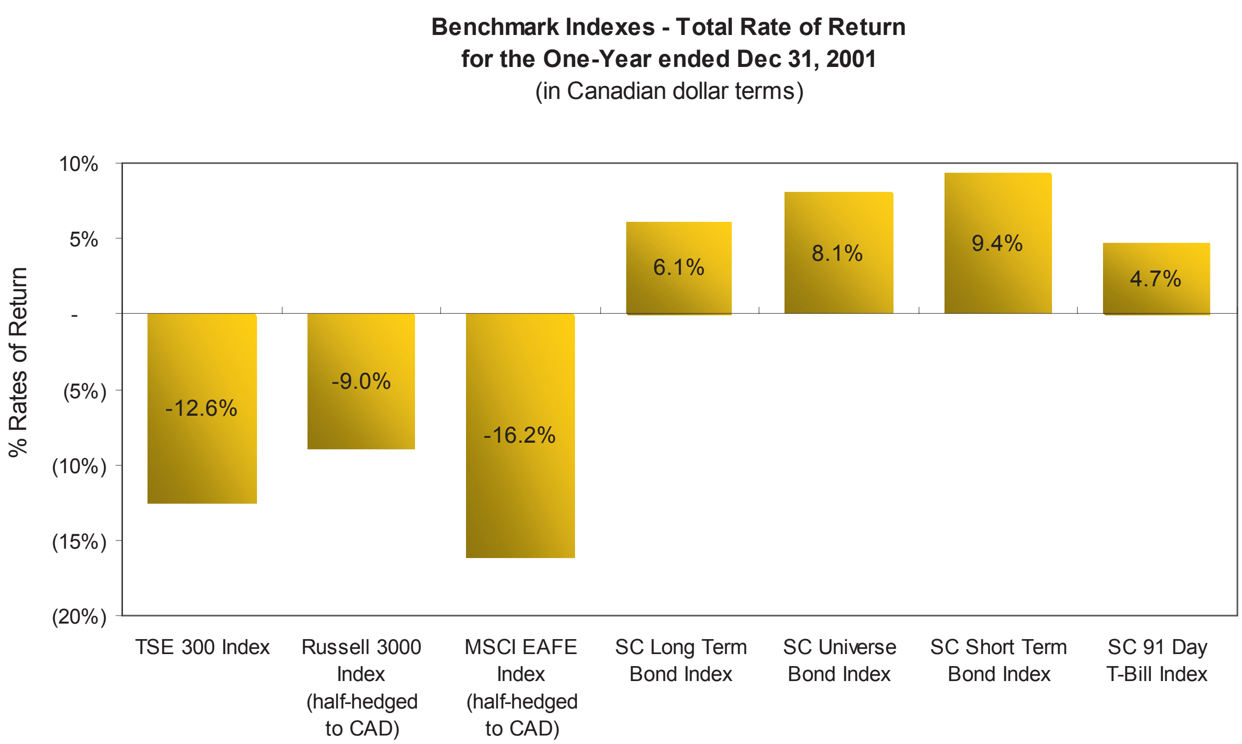
The above charts show the total fund strategy and style diversification at the beginning and end of 2001. Equity classes were reformed significantly throughout the year, while the fixed income components - 40% of Pension and 20% of LTCAP - began and ended the year 100% passively managed. The investment strategy profiles changed dramatically as seen in the illustration. The extent of this change constitutes formative work in developing and implementing UTAM's strategies within the funds, and it is unlikely that reallocation work to this degree will be seen in future periods.

The shift of a portion of assets from passive toward active and other diversifying strategies constituted the completion of work that began with the change in asset allocation in December 2000. When the new policy asset mixes were adopted, the best way to implement them efficiently at the outset of 2001 had been through employing passive-synthetic strategies. It was intended that the initial high level of passive exposure, especially in the U.S. and international equity segments, be a temporary measure that would be refined with the introduction of tilts toward active management as each of the equity class programs took shape. UTAM's overall strategy for the funds is to use a balanced and risk-controlled combination of the various strategies, including active, passive, synthetic, long-short, and private equity, in order to achieve efficient portfolios.

Calendar 2001 was characterized by large declines in interest rates, which contributed to a strong fixed income performance, and by badly negative returns throughout equity markets. The inversion in long-run relative performance of equities versus fixed income was severe as all equity classes yielded negative returns in contrast to the high-single digit rates of return produced by fixed income exposures. Over longer multi-period measurement horizons, rates of return produced by equities have exceeded those generated by fixed income and this relationship is expected to prevail over time. Although the short-term risks arising from the volatility of equity prices are well known, this understanding did not necessarily ease the disappointment in results felt by equity-biased investors who rode the ravages of recession and political and economic disaster during 2001. The battering aside, we maintain our beliefs that equities will outperform fixed income over the long run and steady investors will be rewarded for taking equity risk

The year 2001 was the second consecutive year in which fixed income outperformed the major world equity markets. In Canada, the return on the TSE 300 Index was -12.57% compared to 8.08% for the Scotia Capital Universe Bond Index. The return on U.S. equities as measured by the Russell 3000 Index was -5.90% unhedged (all returns are stated in Canadian dollar terms), and international equities, as measured by the MSCI EAFE Index, had a return of -16.38% unhedged in 2001.

We pursued several strategies that were successful

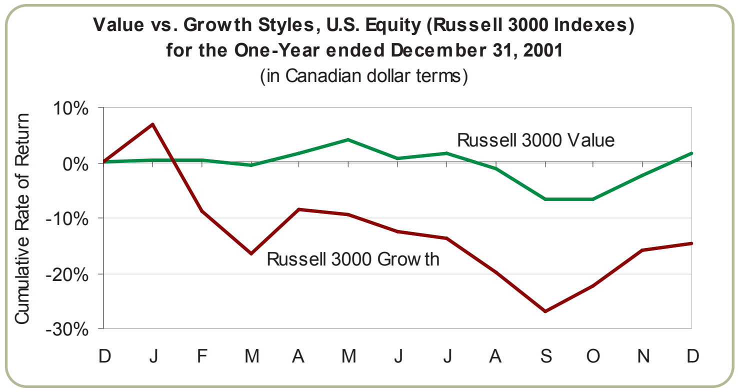


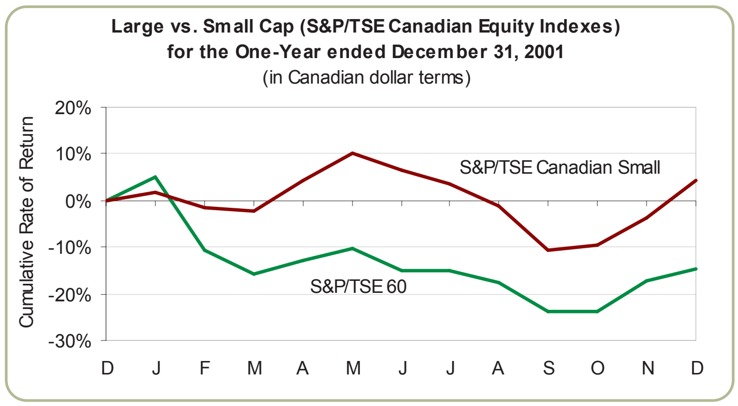
in outperforming various equity indexes. Many of the active equity managers performed well versus the indexes, though returns differed dramatically by investment style. The style divergence experienced by U.S. equities during 2001 is highlighted in a comparison of the one-year returns to the Russell 3000 Value Index and the Russell 3000 Growth Index of 1.66% and -14.59%.

This discrepancy demonstrates the importance of balancing funds by management style. In the late 1990's, the growth style had dominated value as capital flowed to technology, telecommunications and internet services equities with the expectation that earnings would grow at double-digit rates well into the future. The NASDAQ Index, which is heavily weighted with technology and telecommunications equities, declined 16% in 2001 after experiencing a 37% decline in 2000.

The value-growth dichotomy was not limited to the U.S.; similar results held across Canadian and international equity markets.

The other performance dichotomy was large-capitalization versus small-capitalization equities. Small-capitalization companies, those with a total market value of between U.S. $250 million and $1 billion, outperformed large-capitalization equities. The S&P TSE Canadian Small Cap Index returned 4.22% in 2001 relative to - 14.82% for the TSE 60, which represents 60 of the largest companies listed on the Toronto Stock Exchange. In the U.S. equity market, the Russell 1000 Index, a universe of large-capitalization equities, returned -6.97% compared to an 8.91% gain by the Russell 2000 Index, a universe of small-capitalization equities.





RETURN OBJECTIVES

The policy return objectives for the Pension and LTCAP are quantified and measurable on two levels. First, the funds target an expected annualized inflation-adjusted (real) rate of return objective over four-year periods. The real return target expresses the long-term requirement that matches the fund's obligations, thereby fulfilling the fund's purpose. For the Pension fund, this is stated as a four percent real return requirement, while the LTCAP fund has a more ambitious requirement of five percent on a real return basis.

The real return objectives have been established individually for the funds. The Pension Plan payout formula, when actuarially applied to the profile of participants and retirees, produces an expected dollar outflow that translates to a return requirement that is prescribed to the level of plan assets. The LTCAP's endowment payout formula has been established by the University; five percent of the four-year rolling average market value of the endowments is committed to spending on an annual basis. Further, the policies describe the requirement for capital preservation of the purchasing power of the endowment capital and the spending and capital protection rules together align with the target of five percent real return.

Second, on a market-relative basis, the funds aim to add value above the four-year annualized return of a weighted composite of market indexes that expresses the broad range of permissible investments and the general plan for achieving the fund's objectives. The composite benchmark indexes are shown and explained in the section on asset mix.

The policy four-year measurement period reflects the expectation that variability of returns will be experienced over shorter periods, when capital markets volatility and the propensity for the markets to favour certain investment styles may have a significant but temporary impact on relative returns. The extreme divergence between growth and value styles and dramatic reversal of favour observed over the last few years is an example of the style-sensitivity of capital markets. As the funds weather varying market environments through periods that approach four years, the degree of skill and discipline employed in the portfolio management process begins to emerge in the results. The longer-term measurement horizon establishes a disciplined approach to the investment process that indicates an intention to avoid frequent and reactionary shifts in asset allocation.

Four-Year Performance

The following table compares the Pension and LTCAP returns to the various benchmarks over the last four years and on a four-year annualized basis, as prescribed by the UTAM policies.

This table illustrates several trends. In 1998 and 1999, the performance of both funds fell significantly short of the returns to their total fund benchmarks. This has turned around following the transition year of 2000, with both funds significantly outperforming their index benchmarks in 2001. The changes brought about after the formation of UTAM contributed to these improvements in relative performance over the four-year cycle. The areas of four-year underperformance - the Pension versus its composite benchmark and the LTCAP versus its real return benchmark - show that work must be ongoing.

The real return objective was particularly difficult to meet in 2001 due to prevailing market conditions that caused large segments of marketable securities to fail to match the inflation rate. Even with the extraordinarily adverse market conditions of the last two years during which equity markets fell far short of inflation, the funds have still roughly approached their four-year rolling real rate of return targets. Over periods of longer than four years, not shown here, the funds have more than met the real return objectives.

In order to ensure that each fund under management provides the necessary financial resources for stakeholders, it is essential to take a long-term view. We are confident that our asset allocation policies are designed to achieve superior results. These asset mixes may not be optimal in every investment environment, particularly last year when fixed income outperformed equities. Going forward, however, we feel the funds are well-positioned to outperform the real return objectives.

	Annual Rates of Return				Four-Year Annualized
	2001	*2000*	*1999*	*1998*	*1998-2001*
Pension Master Trust Total Rate of Return	-1.48%	5.19%	12.9%	8.1%	6.0%
Policy Composite Index Benchmark *					
Composite Benchmark Objective	-4.66%	5.60%	15.0%	9.9%	6.2%
Value Added	3.18%	-0.41%	-2.1%	-1.8%	-0.2%
Policy Real Return Benchmark					
Inflation (CPI) + 4% Objective	4.70%	7.23%	6.6%	5.0%	5.9%
Value Added	-6.18%	-2.04%	6.3%	3.1%	0.2%
LTCAP Fund Total Rate of Return	-3.23%	5.10%	14.6%	9.7%	6.3%
Policy Composite Index Benchmark *					
Composite Benchmark Objective	-8.62%	3.70%	17.0%	12.0%	5.6%
Value Added	5.39%	1.40%	-2.4%	-2.3%	0.8%
Policy Real Return Benchmark					
Inflation (CPI) + 5% Objective	5.70%	8.23%	7.6%	6.0%	6.9%
Value Added	-8.93%	-3.13%	7.0%	3.7%	-0.5%

* The 2001 benchmark return is geometrically linked with pre-2001 benchmark returns and incorporates the change in target asset mix at beginning of 2001.

ONE-YEAR PERFORMANCE

This report largely focuses on one-year results for relative performance. Prior years' results are in fact not directly comparable to 2001. Two factors have created performance comparison discontinuity for the three funds: the introduction at the beginning of the year of significant amendments to the benchmark asset mixes and the extent of the diversification work that took place during the year. The funds' allocations have changed to such a degree that they bear limited resemblance to their former compositions. This is substantiated by the fact that close to two-thirds of the assets in the three funds have been reallocated among asset classes, investment styles and investment managers by UTAM since its formation in 2000. Major restructurings limit the relevancy of comparing the funds to their past selves in a continuous sense. However, historical information is critical to understanding a fund's record in meeting its obligations over time and the four-year record has been reviewed above.

The following table compares the Pension, LTCAP and EFIP returns to their respective composite benchmarks and component indexes for the 2001 performance year.

Performance Measurement
Fund Rates of Return (%) and Comparision to Benchmarks
for the One-Year ended December 31, 2001

	Fund Return	Benchmark Return	Difference
Pension Master Trust			
Canadian Equity	(9.77)	(12.57)	2.80
U.S. Equity	(3.84)	(8.97)	5.13
International Equity	(10.55)	(16.17)	5.62
Fixed Income	7.33	7.27	0.06
Total Fund vs Benchmark	**(1.48)**	**(4.66)**	**3.18**
LTCAP			
Canadian Equity	(2.43)	(12.57)	10.14
U.S. Equity	(4.07)	(8.97)	4.90
International Equity	(9.29)	(16.17)	6.88
Fixed Income	7.42	7.27	0.15
Total Fund vs Benchmark	**(3.23)**	**(8.62)**	**5.39**
EFIP			
Investment in LTCAP	(3.23)	(8.62)	5.39
Canadian Equity	(10.66)	(12.57)	1.91
U.S. Equity	(8.26)	(8.97)	0.71
International Equity	(16.13)	(16.17)	0.04
Absolute Return	12.18	7.22	4.96
Short Bonds	9.11	9.37	(0.26)
Cash Equivalents	5.10	4.72	0.38
Total Fund vs Benchmark	**0.09**	**(1.65)**	**1.74**

Indexes	
TSE 300 Index	(12.57%)
Russell 3000 Index (half-hedged)	(8.97%)
MSCI EAFE Index (half-hedged)	(16.17%)
SC Combined (60% Universe/40% LT Bond)	7.27%
SC Universe Bond Index	8.08%
SC Long Term Bond Index	6.06%
SC 91 Day T-Bill Index + 250 bp	7.22%
SC Short Term Bond Index	9.37%
SC 91 Day T-Bill Index	4.72%

All returns are stated in Canadian dollar terms.

2001 Performance - Real Return

The Pension and LTCAP fund real return objectives are set relative to the rate of inflation and this is an important measure of whether purchasing power has been maintained. The real return objective for LTCAP is a four-year annualized rate of return of inflation plus 5% and for the one-year ended December 31, 2001 this hurdle was 5.7%. The real return objective for the Pension fund is inflation plus 4%; this hurdle was 4.7% for the one-year ended December 31, 2001. Neither fund met its real return objective over the one-year period, in fact, they considerably underperformed due to the extreme negative returns from the equity classes.

Short-term periods when marketable securities underperform versus inflation are normal and over the longer term, marketable securities are most likely to deliver excess returns. This emphasizes the importance of maintaining and measuring the appropriate asset mix with a long-term perspective, particularly for funds with high objectives which may sustain considerable market volatility and occasional years of negative performance in order to achieve returns during favorable market environments that more than compensate for the years of shortfall.

2001 Performance - Relative Return

For the year ended December 31, 2001, the Pension, LTCAP and EFIP returned -1.48%, -3.23% and 0.09% respectively. The Pension Master Trust, LTCAP and EFIP funds outperformed their individual benchmarks, composites of major market indexes established for the outset of 2001, by 318, 539, and 174 basis points respectively.

The Pension fund's positive performance versus the benchmark was achieved across all asset classes. Approximately one-half of the Pension's 318 basis points of excess return over the benchmark was delivered by the international equities and the other half from the North-American Equities. Of the North-American value added, approximately 85% came from the U.S. equities and 15% from Canadian. Fixed income, which is managed passively and weighted between the long and universe segments of the Canadian fixed income market, produced a small value added through the year. Asset weighting during the period neither contributed nor detracted from performance, which reflected the intended outcome of UTAM's policy of rebalancing the funds back to benchmark weights on a regular basis.

The LTCAP's excess performance above the benchmark was similarly achieved across all asset classes. As with the Pension, approximately one-half of the 539 basis points of value added came from the international equity segment which significantly outperformed the MSCI EAFE Index. The balance of the excess return was generated by the North-American equities segment, approximately 70% from U.S. equities and 30% from the Canadian equities, which included a real estate component. Fixed income contributed a small portion of positive excess return. And, as in the Pension fund, the actions of rebalancing and managing the Pension's cash outflows did not have an impact on the fund's performance.

The EFIP's relative performance of 174 basis points over the benchmark return was achieved through both weighting and selection. Due to the large cyclical liquidity demands on this fund, the cash allocation drifts naturally between 5% and 40% of the total fund. This caused the assets in the fund that track medium- to long-term duration strategies to change dramatically in terms of proportion of the total fund, which was an expected behaviour for the EFIP assets. Hence, the excess return attributed to weighting was significant and for EFIP, rebalancing activities are dominated by the cyclical expansion and contraction of the total assets. Fortunately, value was added due to the underweighting of international equity - the lowest returning asset class in the EFIP mix - and the overweighting of short-term fixed income, which was the highest returning asset class during the year. The other source of significant excess return was the absolute return strategies component which outperformed its benchmark over the year despite a large underweight at the beginning of the year when the program was being instituted. By the end of the year, UTAM had overweighted the exposure to these strategies which served to enhance the total fund return. Approximately one-fifth of the EFIP assets, deemed to be quasi-endowment, are invested through the mechanism of the LTCAP; the latter's outperformance was also a positive factor in EFIP's relative return for the equity segment.

2001 Performance - Comparative Measurement

In addition to the composite benchmark and real return objectives, the Pension and LTCAP have a third objective of exceeding the median return of an appropriate investment fund universe comprised of funds with similar asset mix and return objectives.

A relevant comparative universe would be composed of funds with similar asset mixes to either the Pension fund or the LTCAP that would allow for comparison of skill versus peer groups that sought to attain similar objectives. The significant differences between the Pension and LTCAP asset mixes and objectives virtually preclude them from participating in the same comparative universe.

Canadian Trust Universe	Universe Median Rate of Return	Pension Fund Rate of Return and Percentile		LTCAP Rate of Return and Percentile	
Total Fund	-0.30%	-1.48%	(71)	-3.23%	(82)
Canadian Equity	-3.73%	-9.77%	(76)	-2.43%	(40)
US Equity	-5.94%	-3.84%	(41)	-4.07%	(41)
Non-North American Equity	-11.91%	-10.55%	(42)	-9.29%	(32)
Fixed Income	7.89%	7.33%	(70)	7.42%	(70)

Source: Russell/Mellon Analytical Services

The difficulties with peer universes have been well documented by the Association of Investment Management and Research (AIMR) and others; and typically include lack of transparency, survivorship bias, and sampling inconsistencies, so UTAM has sought to refer to universes that are carefully constructed by their proprietors.

The table above presents for comparison the universe median rates of returns supplied to UTAM by an external consulting firm. Percentile ranks as available for the Pension and LTCAP are shown in brackets; a first percentile rank refers to best in sample and the median return represents the 50th percentile.

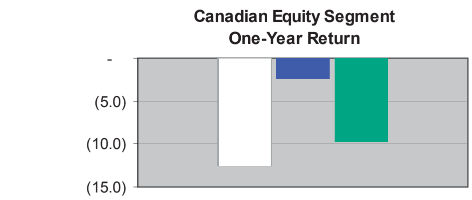
At December 31, 2001, the 70 funds that participated in the Canadian Trust Universe had significantly higher exposures to fixed income than the LTCAP and greater weightings in Canadian equity and cash versus both the LTCAP and Pension fund. Correspondingly, the universe participants' allocations to international and U.S. equities are much lower.

The participants' average total equity weighting was 56% - compared to Pension's 60% and LTCAP's 80% benchmark weights. The universe's foreign

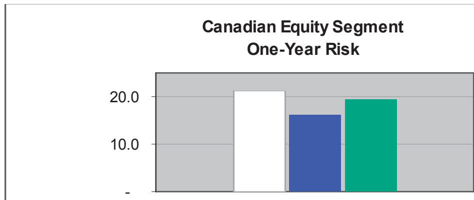
equity exposure is less than 20% of total assets which does not compare readily to the Pension's 50% foreign equity exposure and LTCAP's 70% weighting. While these asset mix deviations limit comparability of the Pension and LTCAP to the other funds, meaningful comparisons may still be made for individual asset classes, such as U.S. equity and Canadian bonds. The results in the table show that the Pension and LTCAP equity segments generally exceeded the median returns for asset classes. The exceptions were the Pension's Canadian equity segment and both Canadian fixed income segments. The passive and enhanced Canadian equity mandates hurt the Pension fund relative to the peer group's greater active content while the Canadian fixed income components underperformed the Bond Universe during the year 2001 due to their greater target exposure to long-term bonds.

Further comparison of results can be made to universes of U.S.-based endowments. These tend to have an asset mix that is similar to the LTCAP, with however no exposure to Canadian equities and fixed income. Russell/Mellon's universe of U.S. Foundations and Endowments produced a median return of -3.93% (in USD terms) compared to LTCAP's -3.23% (in CAD terms). Cambridge Associates, a group that specializes in analysis and reporting of U.S. university endowment results, reported a median performance of -3.00% (in USD terms).

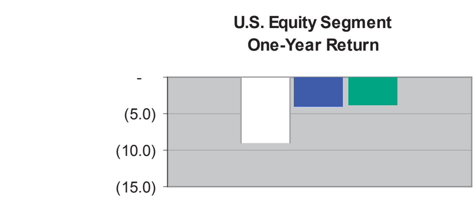
Insofar as a fund's return stated in its local currency terms is a measure of its record in meeting its obligations, and U.S. endowments have real-return objectives that are similar to University of Toronto's five percent, we have presented returns in USD terms without attempting to reconcile the currency differential strictly as an indication of what others have done.



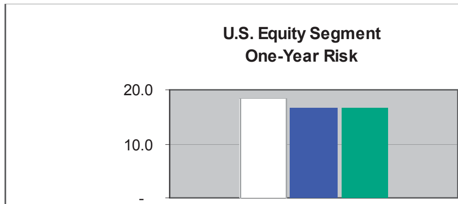
	Rate of Return (%)
TSE 300 Index	(12.57)
LTCAP - CE	(2.43)
Pension - CE	(9.77)



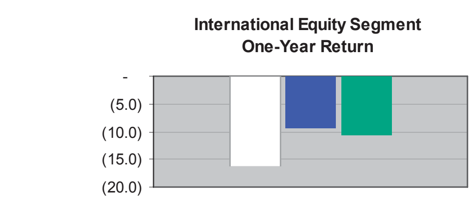
	Standard Deviation (%)
TSE 300 Index	21.30
LTCAP - CE	16.25
Pension - CE	19.50



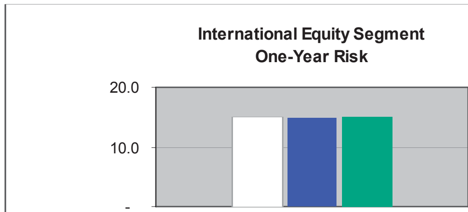
	Rate of Return (%)
Russell 3000 Index (Half-Hedged)	(8.97)
LTCAP - USE	(4.07)
Pension - USE	(3.84)



	Standard Deviation (%)
Russell 3000 Index (Half-Hedged)	18.47
LTCAP - USE	16.75
Pension - USE	16.72



	Rate of Return (%)
MSCI EAFE Index (Half-Hedged)	(16.17)
LTCAP - IE	(9.29)
Pension - IE	(10.55)



	Standard Deviation (%)
MSCI EAFE Index (Half-Hedged)	14.98
LTCAP - IE	14.86
Pension - IE	15.10

The one-year measures of return and risk for Pension and LTCAP's three equity segments - Canadian equity, U.S. equity, and international equity - are shown in the diagrams to the right. All equity components in the Pension and LTCAP exceeded the returns of their respective benchmarks on a cumulative basis, both in absolute and risk-adjusted terms. For each of the equity components, the risk as measured by standard deviation was approximately equal to or lower than the benchmark's risk.

These equity results, viewed in their relationship of risk to return, were highly positive and demonstrated the responsiveness of the equity programs to the intense diversification work that had been committed through the year.

The best overall segment performances, relative to the equity benchmark indexes, were generated by the international equity components of the Pension Master Trust and LTCAP, which exceeded the MSCI EAFE Index return by 562 and 688 basis points respectively. In LTCAP, the rate of return produced by the Canadian equity segment was greater than that of the TSE 300 Index by a remarkable 1014 basis points, due largely to the inclusion of real estate in the segment. While real estate tends to be a hybrid of equity and fixed income, for allocation purposes LTCAP's legacy exposures to two institutional real estate funds are grouped with Canadian equity. The Pension fund's Canadian equity segment, which was homogenously Canadian equity with no real estate exposure, had a performance that exceeded that of the index by 280 basis points. The U.S. segment returns for Pension and LTCAP, exceeded the Russell 3000 Index return by 513 and 490 basis points respectively.

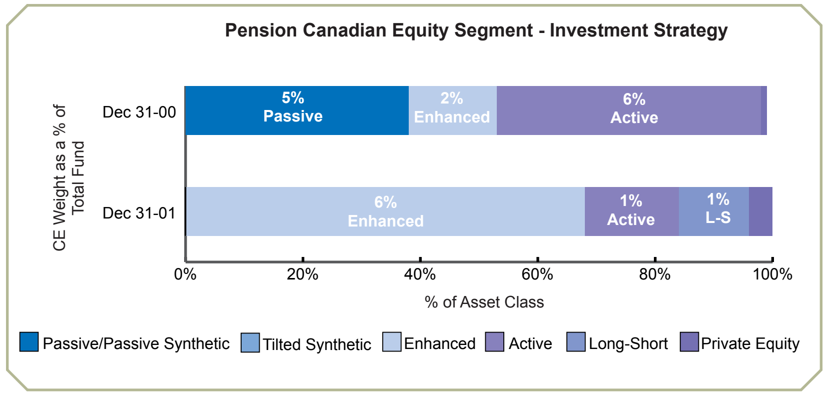
North-American Equities

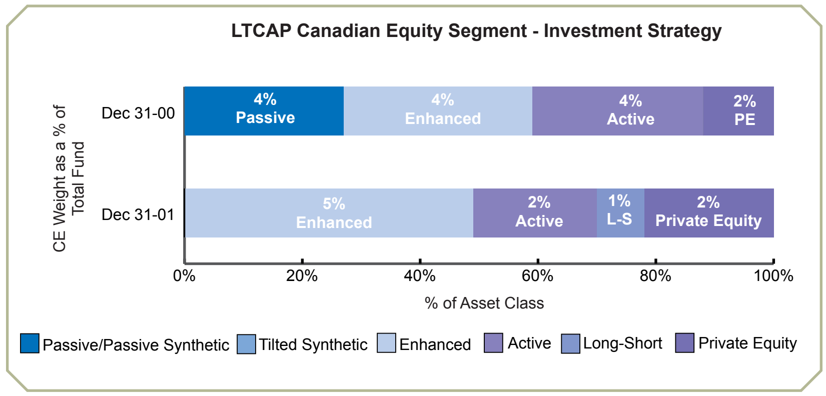
The asset mix target weights for North-American equity are 35% for the Pension fund (10% Canadian, 25% U.S.) and 45% for LTCAP (10% Canadian, 35% U.S.). In both Pension and LTCAP funds, the North-American conventional equity exposure is a mix of broad market, growth and value investment styles.

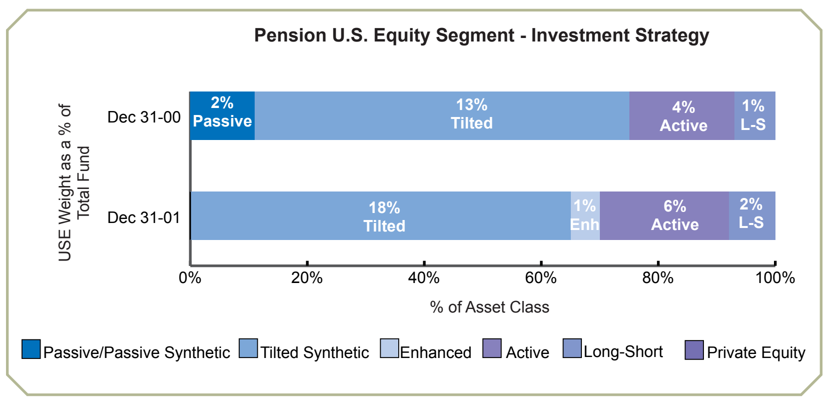
During 2001, significant proportions of the Canadian and U.S. equity segments were moved from passively-managed index funds to actively-managed mandates. To further diversify the funds and to add value, the equity exposures were broadened to include non-traditional investments such as long-short equity hedge funds. Several long-short managers that were added in 2001 to the Canadian and U.S. equity segments were responsible for a significant proportion of the outperformance in the North American components of both Pension and LTCAP funds.

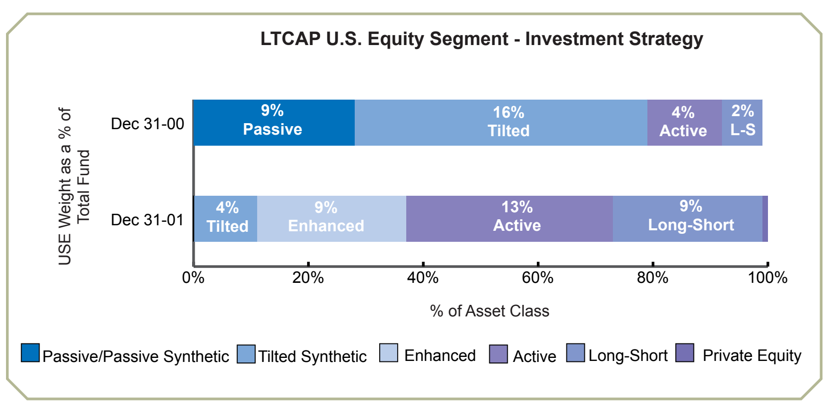
The bar charts show the strategy composition of the Canadian equity and U.S. equity segments for Pension and LTCAP at the beginning of the year and at the end of the year, illustrating the extent of the strategy diversification work that took place during 2001.

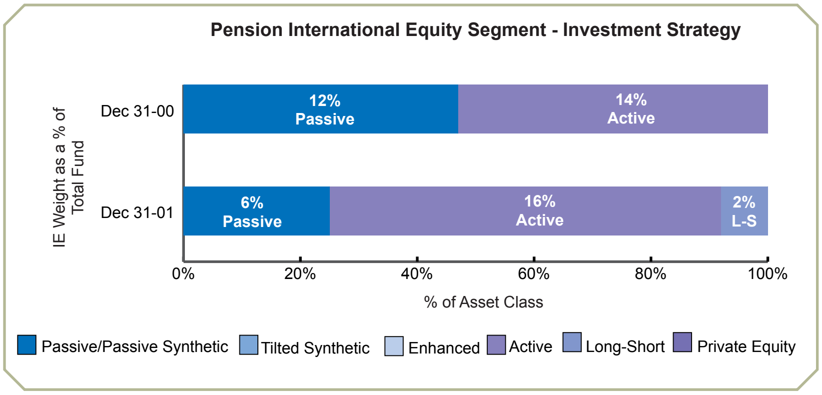
By year end, all Canadian equity exposure was either actively or semi-actively managed, and outperformed the TSE 300 total return index benchmark by 280 basis points in the Pension fund and

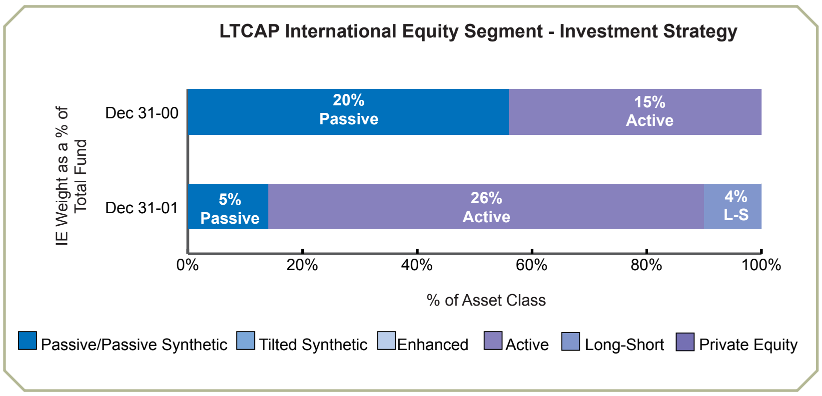












1014 basis points in the LTCAP fund.

On the U.S. side, approximately 60% of the U.S. equity exposure in the Pension fund is held in three synthetic equity portfolios, with UTAM tilting the portfolio mix among the three component capitalization sizes to add value. The same process is applied to the synthetic U.S. holdings in LTCAP to the extent of about 40% of the U.S. portfolio. The U.S. components of the funds also performed exceptionally well in 2001, exceeding the benchmark return by 513 basis points in Pension and 490 basis points in LTCAP.

Beginning in October 2001, an internally-managed portfolio was introduced to the LTCAP fund. The strategy employs futures contracts on three U.S. equity indexes in combination with U.S. denominated short-term backing assets to produce an enhanced synthetic capitalization-tilted portfolio. The internal enhanced U.S. equity mandate made up 6.9% of the LTCAP total fund as at December 31, 2001.

International Equities

The asset mix target weights for international equity are 25% for the Pension fund and 35% for LTCAP. The bar charts below depict the beginning and end of year compositions across strategies for the two funds. The year-end profiles for international equity within Pension and LTCAP are significantly different from each other due to the foreign content restriction on pension investments; the Pension necessarily holds a greater degree of passive-synthetic international equity. The charts demonstrate that a great deal of work was done to diversify the assets and raise the return prospects for both funds, and the results for 2001 were pleasing.

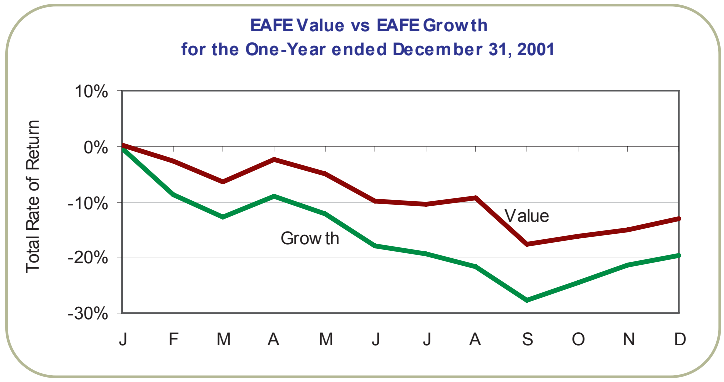
Though helpful in terms of liquidity and cost of trading, passive-synthetic international equity tends to constrain opportunities to add risk-adjusted value. The beginning of 2001 had been characterized by a large passive-synthetic exposure, a result of the asset mix conversion that had taken place on total fund bases for Pension and LTCAP. During 2001, much of the synthetic exposure was reallocated to active and long-short strategies.

International equity markets in 2001 were dominated by two trends, as illustrated in the following chart showing the cumulative returns of the EAFE Value and EAFE Growth indexes. First, international equity markets suffered from negative returns in a volatile and bearish environment. Second, value significantly outperformed growth during the first nine months of the year.

Both these trends reversed in the fourth quarter. Equity markets bounced, and growth overtook value, however, the fourth quarter reversal did not alter the dominant effects evident throughout the year.

Within this environment, UTAM's international equity program held up extremely well on a relative basis delivering unhedged returns of -10.1% in the pension fund and -9.1% in the LTCAP versus an overall MSCI EAFE benchmark return of -16.4%.

The primary reasons for the very good relative performance were the overweighting in the value discipline, the outperformance of several active managers, and the allocation to long-short managers that delivered positive returns in a year when international equities were down significantly.



Fixed income performed well during 2001, due to dramatic declines in interest rates. The contribution of positive absolute returns by this segment to total fund performance was important to mitigating the significantly negative returns that came from the equity investments. The present extreme low level of interest rates, however, requires that caution be associated with expectations for this asset class moving forward. As interest rates are unlikely to fall further from current low levels, and they may well rise, this would lead to lower fixed income returns in the future than were experienced during the long secular downtrend in interest rates that took place in the past years.

The asset mix policy weights for the fixed income segments are 40% for the Pension fund and 20% for LTCAP. The fixed income segments in both funds are managed with parallel strategies. At the beginning of 2001, the strategy had been revised to extend the duration of the portfolios; forty percent of each fund's fixed income was converted from broad market exposure to long-bond exposure. Both the universe bond and long-term bond exposures are run passively by an external manager.

During the year, periodic rebalancing was employed to maintain target weights in fixed income on a total fund basis. The weightings of universe and long term bonds within the fixed income components, versus the benchmark weights, were generally neutral throughout the year. The fixed income segments for Pension and LTCAP had returns of 7.33% and 7.42% respectively, exceeding the combined benchmark return of 7.27% by 6 basis points and 15 basis points respectively. The combined benchmark was composed of 60% Scotia Capital Universe Bond Index and 40% Scotia Capital Long Bond Index, which indexes returned respectively 8.08% and 6.06%. The relative concentration of Pension and LTCAP's exposures along the long end of the yield curve resulted in the funds' returns falling short of the broad universe during 2001.

Generally, the fixed income segments for LTCAP and Pension, while long-term in their market exposure, are an important source of liquidity for meeting fund obligations. The relative stability of fixed income - lower volatility of returns relative to equity - and the capacity of this segment to earn a steady stream of interest income contribute to its lead role in liquidity generation. Close work with the external fixed income portfolio manager caused the process of funding the regular payouts to the University for endowment spending and to retired pension beneficiaries to be efficient.

The fixed income components within EFIP are managed with short-term objectives. The exposure is split between short-term bonds and cash with the objective of meeting all University operational spending needs from cash while taking moderate risk through the short-term bond exposure. The short-term bonds served to moderate the risk in the EFIP total fund and were additionally a significant source of return. During 2001, the Scotia Capital Short Term Bond Index total rate of return was 9.37%, while the bond portfolio returned 9.11%; the difference was caused by the timing of a withdrawal whereas the underlying pooled fund in which EFIP held units slightly exceeded the benchmark return. EFIP cash had a return of 5.10% for the year, compared to 4.72% for the Scotia Capital 91-day Treasury Bill total return index, reflecting the U.S. cash that moved through the account and corresponding foreign exchange profits that were realized during the year. The short-term bonds and cash were largely in actively-managed investment pools run by an external portfolio manager.

As at December 31, 2001, absolute return strategies composed 27.8% of EFIP compared to a benchmark weight of 15%. During the second half of 2001, the overweight in absolute return strategies was intentionally built up corresponding with the decrease in weighting in the higher-risk segments of the EFIP fund, including Canadian equity, U.S. equity and international equity. The extreme volatility of the equity classes during 2001 in combination with their poor performance through the first three quarters substantiated UTAM's focus on tactically reducing the total fund risk in EFIP. The result was positive for EFIP as the absolute return component produced a total rate of return of 12.18% for the year, exceeding its benchmark of Canadian Treasury Bills plus 250 basis points by 496 basis points. The absolute return performance during 2001 was the highest among all the component asset classes comprising the EFIP benchmark.

Absolute return strategies seek to return a spread over the risk-free rate, typically 91-Day Treasury Bills plus 250 to 400 basis points, with low volatility. A classic absolute return strategy involves some form of arbitrage, or locking in the spread between a higher yielding security and a lower yielding security through offsetting long and short positions. Absolute return managers strive to generate positive returns regardless of the direction of the broad equity markets. Consequently, they tend to outperform broad equity indexes in down markets. However, since their offsetting long and short positions create a more conservative risk profile, they tend to underperform the broad equity indexes during periods when markets are trending upward.

The incremental expected returns in excess of those expected for bonds, along with the low volatility profile of absolute return strategies relative to equity and fixed income indexes, have made this new asset class an ideal exposure for EFIP given its relatively short investment horizon.

The private equity programs for Pension and LTCAP were launched during 2001. Private equity investments are made in the form of commitments to funds managed by professional management groups. Eight funds were selected to provide exposure to venture capital, buyouts, and the energy sector. The private equity strategies are diversified by geographic exposure, by industry, and by stage of development. The managers of the funds have been selected on the basis of their ability and the extent of their success in the past. The manager selection in this asset category tends to be the central determinant of future performance.

Approximately 10% of the capital committed to the eight funds has been called by the private equity managers. The balance of the committed funds will be invested over the next three to four years as the managers find appropriate investments.

In the initial commitment phase of the private equity program, there is typically no return on investment; results are expected to be harvested after three years or more of program development. The development of UTAM's private equity program is ongoing and it will take several years to reach full allocation.

The revised asset mix policies adopted at the beginning of 2001 increased the exposures in Pension, LTCAP and EFIP to U.S. and international equities and led to the transition of over $1.0 billion of the funds' assets out of Canadian markets, bound for foreign markets. At December 31, 2001, the foreign currency exposure across the three funds summed to $1.9 billion.

UTAM had examined the impact of currency exposure on asset returns in Canadian dollar terms and reached the conclusion that currencies typically contribute uncompensated risk to foreign investments in the form of excessive short-term volatility of returns. Therefore, as part of the asset mix revision, a currency risk management program was introduced for the purpose of moderating the returns volatility arising from changes in foreign exchange rates. The policy benchmark indexes for the U.S. equity and international equity segments are accordingly measured 50% hedged back to the Canadian dollar. The 50% hedge ratio supports a neutral stance in regard to whether the Canadian dollar may in the future appreciate or depreciate against a foreign currency.

Initially, a currency manager was hired to run a currency overlay mandate on a passive basis, whereby the benchmark weights in foreign assets were hedged 50% back to the Canadian dollar. Adjustments for changes in the value of assets under management were made monthly. The result was a reduction in volatility over the space of several months, however, a side effect of the process involved cash flow uncertainty associated with monthly marking to market.

In October 2001, after an extended process of due diligence before the Board of Directors, UTAM converted the currency overlay mandate to an active strategy and a currency specialist manager was hired to oversee the process. The active currency overlay manager may vary the actual currency hedge positions around the benchmark 50% hedge ratio in order to protect the funds further during periods of increased exchange rate volatility. As with the predecessor passive currency overlay program, the aim is not to speculate on currency direction but rather to control and dampen the returns volatility arising especially during episodes of extreme currency movements.

Currency overlay mandates have been established for each of the three funds, all with a benchmark 50% hedge ratio. The manager tracks the actual currency exposures in the underlying portfolios and separately overlays these with currency forward contracts that on a neutral basis hedge half the underlying exposures to U.S. dollar, the Euro, the British Pound and the Japanese Yen back to the Canadian dollar. The mandate uses only major liquid currencies in its strategy covering over 80% of the funds' foreign currency exposures.

During 2001, the Canadian dollar generally fell against major currencies. Versus the U.S. dollar, British Pound and the Euro, the Canadian dollar depreciated by 6.28%, 3.54%, and 0.79% respectively. Versus the Japanese Yen, the Canadian dollar appreciated by 7.39%. The half-hedged benchmarks for U.S. and international equities, the Russell 3000 Index and the MSCI EAFE Index, incorporate one-half of the changes in exchange rates for all constituent currencies. The performance impact of the hedging mandates is reported in aggregate with the U.S. equity, international equity, and absolute return strategy segments of the Pension, LTCAP and EFIP funds.

AUDITORS' REPORT

To the Board of Directors of
University of Toronto Asset Management Corporation

We have audited the balance sheet of the **University of Toronto Asset Management Corporation** as at December 31, 2001 and the statement of expenses and recoveries for the year then ended. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the company as at December 31, 2001 and the results of its operations for the year then ended in accordance with Canadian generally accepted accounting principles.

Toronto, Canada
February 1, 2002

Ernst & Young LLP
Chartered Accountants

As at December 31	2001	2000
	$	$
ASSETS		
Current		
Cash	15,478	169,010
Due from the University of Toronto *[note 3]*	39,160	-
Accounts Receivable	6,479	87,370
Deferred Compensation Plan *[note 4]*	7,307	-
Prepaid Rent	-	28,626
	68,424	285,006
LIABILITIES		
Current		
Accounts Payable	61,117	272,280
Deferred Compensation Plan Payable *[note 4]*	7,307	-
Due to the University of Toronto *[note 3]*	-	12,726
	68,424	285,006

See accompanying notes

On behalf of the Board:

Robert W. Korthals, Chairman

Year ended December 31	2001 $	Period from date of incorporation on Apr 25, 2000 to Dec 31, 2000 $
EXPENSES		
Salaries and Benefits	2,090,240	955,905
Occupancy	134,610	-
Consulting Fees	136,171	83,901
Startup Costs	112,769	451,496
Office Supplies and Services	68,456	12,916
Professional Development	10,201	9,780
Professional Fees	62,652	40,845
Telecommunications	167,557	34,839
Travel and Entertainment	69,775	23,257
Other	10,201	12,040
	2,862,632	1,624,979
RECOVERIES		
CURIE Management Income	30,067	10,540
Recovery from the University of Toronto *[note 3]*	2,832,565	1,614,439
	2,862,632	1,624,979
NET INCOME FOR THE PERIOD	-	-

See accompanying notes

DECEMBER 31, 2001

1. RELATIONSHIP WITH THE UNIVERSITY OF TORONTO

University of Toronto Asset Management Corporation ["UTAM"] is a corporation without share capital incorporated on April 25, 2000 by the Governing Council of the University of Toronto [the "Governing Council"] under the Corporations Act (Ontario).

The principal objectives of UTAM are to create added value by providing both current and future financial resources for the University of Toronto ["U of T"] and its pension funds that will contribute to globally recognized education and research.

2. SIGNIFICANT ACCOUNTING POLICIES

Basis of presentation

These financial statements present the financial position and operations of UTAM as a separate legal entity. The securities representing the investments of the funds of U of T are held on behalf of U of T in the names of such trustees or nominees as may be directed by UTAM, but not in the name of UTAM.

The financial statements have been prepared in accordance with Canadian generally accepted accounting principles.

3. RELATED PARTY TRANSACTIONS

In accordance with the Service Agreement dated May 1, 2000 between the Governing Council of U of T and UTAM, U of T will pay UTAM for its services an amount which will enable it to recover the appropriate costs of its operations. As at December 31, 2001, $39,160 is due from U of T [2000 - $12,726 due to U of T].

4. DEFERRED COMPENSATION PLAN

UTAM has entered into a Deferred Compensation Plan with certain of its employees. On approval of the Board after year-end, one half of the amount is payable immediately and included in the current year financial statements. The balance is deferred to be expensed over the vesting period which does not exceed three years. Funds for the deferred amount are used to acquire units in the Long Term Capital Appreciation Pool (“LTCAP”) investment fund of U of T.

The Deferred Compensation Plan represents units held at market value for vested compensation due to employees. In addition at December 31, funds of $71,212 (2000 - nil) are held on deposit in the LTCAP for unvested deferred compensation.

Any fluctuations in market value of the LTCAP units are at the risk of, or for the benefit of, the employee.

5. STATEMENT OF CASH FLOWS

A separate statement of cash flows has not been presented since, in the opinion of management, the information it would contain is readily apparent from the other financial statements.

ROBERT W. KORTHALS
CHAIRMAN OF THE BOARD

Mr. Korthals was President of the Toronto Dominion Bank from 1981 to 1995. He is a Commissioner of the Ontario Securities Commission. Mr. Korthals also serves as Chairman of the Ontario Teachers' Pension Plan Board, and as director of several other corporations including Cognos Inc., Co-Steel Inc., Rogers Communications Inc., and Suncor Energy Inc. Mr. Korthals holds a degree in Chemical Engineering from the University of Toronto and an MBA from the Harvard School of Business.

JALYNN H. BENNETT, *Chair of the Audit and Compliance Committee*
Jalynn H. Bennett & Associates Ltd, President

H. GARFIELD EMERSON, *Chair of the Compensation Committee*
Fasken Martineau DuMoulin, National Chair

ROBERT J. BIRGENEAU
University of Toronto, President

FELIX CHEE
University of Toronto, Vice-President Business Affairs and CFO

RUSSELL J. HISCOCK
C.N. Investments, Manager, Equity Investments

GORDON J. HOMER
Scotia Capital, Deputy Chairman

ERIC F. KIRZNER
Rotman School of Management, Director, Executive MBA Program

ANTHONY R. MELMAN
Onex Corporation, Vice-President

JAMES J. MOSSMAN
Blackstone Group, Senior Managing Director and CIO

ANDREA ROSEN
TD Bank Financial Group, Executive Vice President, Commercial Banking

JOSEPH L. ROTMAN
Roy-L Capital Corporation, Chairman and CEO

ROBERT G. WHITE
University of Toronto, Chief Financial Officer Emeritus

NEIL DOBBS, *Secretary*
University of Toronto, Deputy Secretary to the Governing Council

J. CHRISTOPHER BARRON
Honorary Member

WILLIAM R. WATERS
Honorary Member

MASTER CUSTODIAN

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State Street Financial Centre
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Toronto, Ontario M5K 1J7

Donald W. Lindsey, CFA, MBA
President and Chief Executive Officer

President and CEO of UTAM (University of Toronto Asset Management Corporation). He is also the Chief Investment Officer of the University of Toronto. Mr. Lindsey began his career with the University of Virginia Investment Management Company, where he served initially as Investment Analyst and proceeded to become Assistant Director of Investments, Senior Investment Officer and Director. He has taught in the McIntire School of Commerce at the University of Virginia. He holds the CFA designation, and has also taught CFA exam preparation and other courses in Croatia, Romania, Japan, South Africa, Switzerland, Italy and the United Kingdom. He is a member of the Pension Committee of the St. Michael's Hospital in Toronto; and a member of the Investment Sub-Committee of Trinity Health in Novi, Michigan. Mr. Lindsey holds a BA in Political Science from Virginia Tech and an MBA from James Madison University.

Michael C. Doran, CFA, MBA
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Laurie M. Lawson, CFA
Managing Director, Asset Allocation and Special Asset Classes

Philip E. Paroian, CFA, ASA
Managing Director, International Equity and Emerging Markets

Brian Stewart, CIM, MBA
Managing Director, Private Markets

Jeffrey Sutcliffe, CFA, FCSI
Director, Fixed Income

Julianna Varpalotai-Xavier, CA
Chief Operating Officer

Lisa Chung
Manager, Operations

Rabinder Grewal
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