

The background features a large, stylized logo consisting of the letters 'P', 'S', and 'P' in a bold, sans-serif font. The letters are rendered in a dark blue color with a subtle gradient and are set against a textured, swirling blue background. The 'P's are positioned on the left and right, with the 'S' in the center, creating a symmetrical design.

The Public Sector Pension Investment Board

2002 ANNUAL REPORT

PSP INVESTMENTS

CORPORATE PROFILE

The Public Sector Pension Investment Board (PSP Investments) is a Crown corporation created to invest in capital markets the net contributions received after April 1, 2000 from the pension plans of the Federal Public Service, Canadian Forces and Royal Canadian Mounted Police. It operates at arm's length from the federal government. Its statutory objectives are to manage the funds entrusted to it in the best interests of the contributors and beneficiaries of the plans and to maximize investment returns without undue risk of loss.

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ANNUAL OBJECTIVES

The legislation governing PSP Investments requires the annual report to include its objectives for the fiscal year under review, indicating to what extent they were met, and to state its objectives for the new fiscal year. This information is summarized below.

FISCAL YEAR 2002 OBJECTIVES	STATUS*
• Develop operating policies and procedures	✓
• Initiate the hiring of internal investment expertise and external fund managers	✓
• Initiate active investment management programs that can add value above the returns of market indices	✓
• Recruit staff for administration, investment accounting, risk management and performance measurement functions	✓
* ✓ indicates objective was substantially or completely achieved	

OBJECTIVES FOR FISCAL YEAR 2003

- Continue implementation of active investment management in order to generate value added returns
- Implement an automated order management system for equity trading
- Upgrade performance measurement to a new system
- Implement an internal audit function

CHAIRPERSON'S REPORT



William R.C. Blundell, Chairperson

Oversight and governance related initiatives were a priority focus for the Board of Directors of the Public Sector Pension Investment Board during fiscal year 2002. The aim was to complete a policy framework that enables PSP Investments — as the organization is popularly known — to pursue its objectives in a determined yet highly disciplined manner, avoiding undue risk.

As PSP Investments enters its third year of operation, the underlying, long-term goal is to generate returns at least sufficient to cover pension liabilities, through a combination of superior investment performance, cost effectiveness and efficiency. This necessitates being decidedly bottom line oriented while ensuring that requisite risk management mechanisms are in place — and stringently enforced.

To that end, the Board of Directors has worked closely with senior management on the development and implementation of appropriate policies and practices for investment risk management. The numerous initiatives taken to date range from stipulations governing the proportion of assets that can be “actively” managed — i.e. not necessarily invested in a manner that replicates select market indices — to strict limits on the amount of money allocated to individual investment managers. More work remains to be done in this area as our investment activities continue to expand in scope and complexity. However, we are committed to taking whatever measures are necessary to make sure the money entrusted to PSP Investments by the pension plans’ sponsor and contributors is safe and properly accounted for.

In the area of fiduciary responsibility, the Board of Directors approved comprehensive Conflict of Interest Procedures for Directors during fiscal year 2002, as well as a revised Code of Conduct for officers and employees. The amended code incorporates more stringent reporting requirements that reflect the hiring of in-house portfolio managers and traders.

As PSP Investments continues to assemble its team of investment and support staff, the Board of Directors has also been engaged in the development of administration related policies.

Noteworthy in that regard, the Human Resources and Compensation Committee collaborated with senior management on the drafting and adoption of a Human Resources Policy. The policy is tailored to help instill a team based culture and — even more importantly — to ensure that the interests of employees (both administrative and investment personnel) are closely aligned with those of plan trustees and beneficiaries, by linking pay to performance.

ACKNOWLEDGEMENTS

In just two short years, we have succeeded in putting in place the solid foundations for an organization that is destined to develop into one of the country's largest and — I fully expect — best performing pension fund pools.

This would not have been possible without the contributions of the capable, committed and strong-willed group of men and women who sit with me on PSP Investments' Board of Directors. I am grateful to them for their wise counsel and support.

When the Board of Directors was formed at the beginning of fiscal year 2001, Directors were appointed to staggered terms; I am pleased to note that three members whose initial terms had expired — Bob Baldwin, Jean-Louis Bourbeau and Carl Otto — were re-appointed, effective April 1, 2002.

I would also like to take this opportunity to say thank you to Carl Haller, our former executive vice president, for his pivotal role in overseeing the transition of PSP Investments from start-up status — with a single employee, Carl — to an established organization with its own permanent management and staff.

Finally, on behalf of the entire Board of Directors, I would like to commend our President and Chief Executive Officer, Adel Sarwat, and his team for their excellent work over the course of the past year. Thanks in large part to Adel's leadership, PSP Investments is positioned to move to the next level as it implements active management of a substantial portion of the assets entrusted to its control.

PRIORITIES GOING FORWARD

As the new fiscal year continues to unfold, the Board of Directors remains committed to providing the oversight and guidance required by a dynamic and growing organization. Long-term priorities from our perspective include:

- Making certain that PSP Investments generates returns that enable the pension plans to meet — and, ideally, exceed — their actuarial liabilities;
- Providing for continuous enterprise-wide, risk management policies and procedures sufficiently comprehensive to cover all internal and external activities; and
- Ensuring “zero breaches” of the code and guidelines governing fiduciary responsibilities.



William R.C. Blundell
Chairperson

- *As PSP Investments enters its third year of operation, the underlying, long-term goal is to generate returns at least sufficient to cover pension liabilities through a combination of superior investment performance, cost effectiveness and efficiency.*
- *PSP Investments' Human Resources Policy is tailored to help instill a team based culture and — even more importantly — to ensure that the interests of employees... are closely aligned with those of plan trustees and beneficiaries, by linking pay to performance.*

PRESIDENT'S REPORT



*Adel Sarwat, President
and Chief Executive Officer*

I am pleased to report that the Public Sector Pension Investment Board (PSP Investments) produced an income of \$146.8 million and a rate of return of 2.73% for the fiscal year ended March 31, 2002, while achieving substantially all of the objectives we had established for that period. Consolidated net assets as of the fiscal 2002 year-end were \$5.6 billion at market value, compared with \$2.5 billion a year earlier. With key policies, procedures and administrative structures largely in place, we now are positioned to begin delivering the value-added returns that our investment policy was designed for.

Team building was high on the fiscal year 2002 agenda. And we made excellent progress in terms of assembling the nucleus of the lean, tightly-knit organization we wish to build — a small core of experienced professionals with proven capabilities in their respective fields who, together, will form a multi-disciplinary team with a global perspective. Key hires on the investment side included our first three internal portfolio managers, for U.S., European and Canadian equities, respectively. On the administrative side, Chief Financial Officer Danielle G. Morin joined us early in the fiscal year and we also recruited department heads in the areas of Finance and Control, Investment Administration, Performance Measurement and Information Technology.

CLEARLY DEFINED OBJECTIVES

Clearly defined objectives — which we regard as a prerequisite for success — have been established for all team members, investment and administrative staff, alike. The aim is to ensure that employees fully understand not only our corporate objectives, but also what we expect each individual to contribute in terms of achieving those objectives. As well, employees are better able to ascertain what career prospects await them in a results oriented environment that values commitment and initiative and rewards solid performance.

We also put in place the proper measures needed to accurately gauge employees' performance on an individual and collective basis. Of course, this is particularly crucial in terms of investment returns, which are used by our Board of Directors and other stakeholders to measure the overall success of PSP Investments.

I am confident that the innovative human resources and compensation policies developed by management and approved by the Board of Directors during fiscal year 2002 will help us attract and retain top-calibre talent, as we round out the organization.

ACTIVE MANAGEMENT — MAKING GOOD ON OUR COMMITMENT

We also made good on our commitment, outlined in last year's annual report, to commence implementation of “active” investment management during fiscal year 2002 as a means of maximizing returns.

Internal managers for U.S. and European equities were the first to be hired, and were given funds to manage, effective October 2001. In February 2002, two external managers for fixed income investments were appointed and given assets to manage. We also initiated active internal management of Canadian equities in the same month. This followed PSP Investments' request for a change in the regulations governing PSP Investments that had restricted our investments in Canadian equities to replicating a widely recognized Canadian stock market index. The change in these regulations was made in October 2001, clearing the way for the gradual transition to an active approach. Then, just prior to our fiscal year end, we selected additional external managers for U.S., EAFE (Europe, Australasia & Far East) and Canadian equities. They will be formally appointed and given funds to manage early in fiscal year 2003.

It is our intention to hire more internal managers during fiscal year 2003, along with the requisite support staff, as opportunities to recruit suitably qualified and experienced professionals present themselves. In addition to generating cost savings that contribute to over-all added value, in-house investment management provides better control over the risk/reward profile of the funds. However, external active managers will handle approximately 30% of the funds' total assets in fiscal year 2003.

In conjunction with our implementation of active investment management, PSP Investments has forged ahead with the introduction of comprehensive investment risk management policies and procedures. The first step in this direction entailed the imposition of strict controls on both the overall proportion of assets allocated to active management and the amounts entrusted to individual managers. The next step, to be taken during fiscal year 2003, entails the establishment of a full fledged Investment Risk Measurement function, backed by the appropriate systems.

Our Code of Conduct has been revised to incorporate more stringent reporting requirements to guard against the possibility of unethical and/or unauthorized behaviour.

- *Clearly defined objectives — which we regard as a prerequisite for success — have been established for all team members, investment and administrative staff, alike... We also put in place the proper measures needed to accurately gauge employees' performance on an individual and collective basis.*
- *We made good on our commitment, outlined in last year's annual report, to commence implementation of “active” investment management during fiscal year 2002 as a means of maximizing returns.*

ASSET MIX

Equities continue to account for 65% of PSP Investments' assets, in accordance with the long-term asset mix policy that was last revisited at the time of our mandated annual review in February 2002. I should point out, as well, that the asset mix policy was also reviewed in the wake of September 11th, 2001. We then decided to maintain the existing policy.

In November 2001, we were pleased to meet with the Advisory Committees of the three pension plans to review the previous annual report, explain our policies and update them on developments. Annual meetings with the Advisory Committees are part of the rigorous reporting requirements of PSP Investments.

- *Annual meetings with the Advisory Committees of the three pension plans are part of the rigorous reporting requirements of PSP Investments.*

READY TO MOVE FORWARD

The achievements of fiscal year 2002 have positioned us to move forward in pursuit of our overriding, long-term objective to deliver returns that will enable the pension plans to meet — or preferably exceed — their actuarial liabilities. To that end, we have launched active investment management, hired key managers and team leaders and selected or put in place systems and procedures in crucial areas. Moreover, we have accomplished this while maintaining stringent control over the cost side of the ledger.


CHALLENGES FOR FISCAL YEAR 2003

Foremost among the challenges that we have identified for fiscal year 2003 are: continuing the implementation of active investment management, in order to generate value-added returns; implementing an automated order management system for equity trading; upgrading performance measurement to a new system; and implementing an internal audit function.

ACKNOWLEDGEMENTS

In closing, I would like to thank PSP Investments' employees for their hard work and contributions to our success. They are the mainstays of our growing organization.

I would also like to express my gratitude to the Board of Directors for their support. And, finally, I wish to assure the plan sponsor, contributors and beneficiaries that I remain committed to leading PSP Investments in a manner that will enable us to maximize returns for their benefit.



Adel Sarwat

President and Chief Executive Officer

INVESTMENT POLICY AND STRATEGY

This section summarizes the statutory investment objectives of the Public Sector Pension Investment Board (PSP Investments) as well as the policy and strategy being utilized to achieve those targets. This past year saw the introduction of “active” investment management, designed to help generate value-added returns, and the implementation of procedures that ensure the expeditious investment of cash flow in a policy-neutral manner.

STATUTORY INVESTMENT OBJECTIVES

The mission of PSP Investments is straightforward:

- to manage funds in the best interests of contributors and beneficiaries of the underlying pension plans; and
- to maximize returns without undue risk of loss.

ASSET MIX POLICY AT MARKET VALUE (For fiscal year 2002)

	TARGET	RANGE	BENCHMARK
Canadian Equities	35%	30%-40%	TSE 300*
Foreign Equities	30%	25%-35%**	CUSTOMIZED***
Fixed Income	32%	27%-37%	SC Bond Universe
Cash Equivalents	3%	0%-10%	SC 91-day T-bill

* SPX/TSX starting May 1st, 2002.

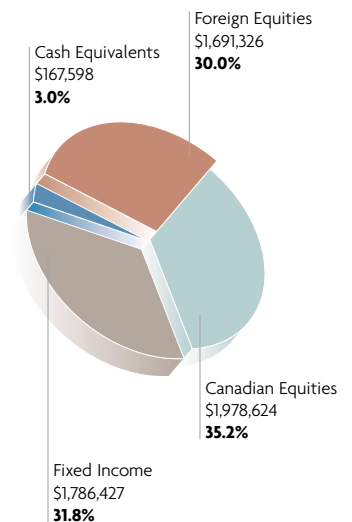
** Foreign equity exposure cannot exceed 30% at book value, but can be higher at market value.

*** S&P 500 and EAFE indices weighted according to market capitalization (rebalanced monthly). Emerging markets will be included in the benchmark when investments are made in those markets. (EAFE is the MSCI Europe, Australasia and Far East Index).

ASSET MIX POLICY

In June 2001, PSP Investments reached the 65% equities weighting that was targeted when the asset mix policy was reviewed in February 2001. This compares with a target of 61% at the end of March 2001 and a target of 55% at the outset of operations in April 2000. Current policy provides for the assets to continue being invested as follows: 35% in Canadian equities; 30% in Foreign equities (the maximum allowed pension funds under the *Income Tax Act*); 32% in Fixed-income vehicles; and 3% in Cash equivalents.

% ASSET CLASSES (As of March 31, 2002)





From left to right:

Lyne Crépin
Director,
Investment Administration

Adrien Diouf
Specialist, Investment Program

Jérôme Bichut
Senior Portfolio Manager,
European Equities

Lynne Carboneau
Senior Administrator

ACTIVE INVESTMENT MANAGEMENT IMPLEMENTED

PSP Investments subscribes to the view that an appropriate balance of increased equity exposure and active investment management is likely to prove most effective in terms of generating value-added returns. Accordingly, its strategy entails actively managing a portion of the assets.

During its first 18 months of operation, however, the organization utilized passive investment management, which entails replicating recognized market indices by purchasing shares — or other securities, as the case may be — in the same proportion they are represented in the relevant index. In the case of Canadian equities, PSP Investments, in fact, had no alternative. Federal regulations restricted investments in Canadian equities to replicating a widely recognized Canadian stock market index. When PSP Investments was ready to engage in active management, a change to this regulation was applied for and effected in October 2001.

With active management, investment professionals can increase or reduce exposure to certain securities based on the perceived risk/return profile. The aim is to outperform the relevant market indices and thereby enhance PSP Investments' ability to maximize returns over time, without undue risk of loss.

The implementation of active management got under way in the second half of fiscal year 2002, when internal managers for U.S. and European equities were hired and given assets to manage. As well, two external managers for fixed-income investments were appointed and given money to manage. Active internal management of Canadian equities began in February 2002 in the wake of the change in regulations mentioned above. External managers for U.S., EAFE (Europe, Australasia & Far East) and Canadian equities have been selected and will be allocated assets to manage early in fiscal year 2003.

From left to right:
Harry Young
 Senior Trader, Equities
Louise Lachance
 Administrative Assistant
Frédéric Lecoq
 Senior Portfolio Manager,
 Canadian Equities
Adel Sarwat
 President
 and Chief Executive Officer
Susan Da Sie
 Senior Portfolio Manager,
 US Equities



PSP Investments intends to recruit more internal managers over the course of the year, along with a limited number of specialized analysts, as suitably qualified people become available. In-house investment management results in cost savings that contribute to over-all value added, while providing better control over the risk/reward profile of the entire portfolio.

Although the use of derivatives is permitted by the Act, PSP Investments has not yet utilized them in either active or passive management.

INVESTMENT RISK MANAGEMENT

With the implementation of active investment management, PSP Investments has introduced a comprehensive two-step system of checks to limit the risks inherent in its investment activities.

The first step — already in place — entails strictly controlling both the overall percentage of assets allocated to active management and the amounts entrusted to individual managers. This allocation is done in a manner that also reflects the degree of risk associated with the individual managers' styles. The second step will see the establishment, during fiscal year 2003, of a formal, in-house Investment Risk Measurement function, backed by appropriate systems.

Policies to manage other credit, market and financial risks have been in place since PSP Investments began operating. For instance, the credit risk of bonds and cash-equivalent securities is managed by controlling the percentage held in lower rated securities, as measured by an external credit rating agency. Interest rate risks associated with fixed-income investing are managed through diversification strategies, as is the currency risk implicit in foreign equities.

CASH FLOW AND REBALANCING

Over the course of fiscal year 2002, PSP Investments received \$3 billion of new money to invest. This cash flow represented 120% of the total assets of \$2.5 billion at the beginning of the fiscal year 2002, April 1, 2001.

Cash flow is received several times a month in amounts ranging from relatively small sums to as much as \$200 million. Consequently, clear policies and procedures for investing cash flows are an important consideration in the implementation of the overall investment policy.

On receipt of cash flow:

- Money is immediately invested in all asset classes;
- Amounts are allocated to asset classes such that the resulting asset-class weights are not disturbed by the cash flow received in the course of a month. If cash flow is received at the end of a month, it is utilized in the monthly rebalancing of asset classes to conform with policy weights.

PSP Investments established these specific procedures for two reasons. Firstly, it does not want to be forced into making investment decisions based on the timing of cash flows. Secondly, it wishes to ensure that its rate of return measured against the Policy Benchmark reflects investment decisions and not the timing of cash flows.

Nevertheless, given that PSP Investments is still in the early years of operation — with cash flow that is relatively large vis-à-vis assets — there will still be a measurable (positive or negative) impact on performance stemming from the investment of new cash flow. Indeed, that is the main reason why the three pension plan accounts generated slightly different returns: their cash-flow patterns were different.

CHANGES IN ACCOUNTING STRUCTURE

The advent of active investment management in October 2001 necessitated a change in accounting procedures to ensure the equitable alignment of cash flow. Whereas each of the pension plans previously maintained separate accounts for each asset class, a pooled arrangement has now been established for each asset class. Essentially, each of the three plans holds “units” of those pooled assets in proportion to their overall share of assets. The switch in accounting structure also entailed creating a fourth, consolidated PSP Investments account that reflects the combined assets. Consequently, the annual report for fiscal year 2002 incorporates four sets of financial statements.

FISCAL YEAR 2002 RESULTS

The Public Sector Pension Investment Board (PSP Investments) completed its second year of operation on March 31, 2002. During that period, it received \$3.0 billion in net contributions from the Public Service, Canadian Forces and Royal Canadian Mounted Police pension plans. Cash inflows of varying amounts were received several times a month and invested as soon as possible in a policy-neutral manner. On a consolidated basis at the fiscal 2002 year-end, 35.2% of assets were invested in Canadian equities, 30.0% in foreign equities and 34.8% in Fixed-income securities. The market value of invested assets as of March 31, 2002 totalled, \$5.6 billion, compared with \$2.5 billion a year earlier.

MARKET PERFORMANCE

Fiscal year 2002 witnessed major gyrations in the markets. Canadian equity and Fixed-income markets ended the fiscal year with almost identical rates of return: 4.9% for the TSE 300 Composite Index and 5.1% for the Scotia Capital Bond Universe Index. Foreign markets fared less well, generating rates of return (in Canadian dollars) for fiscal year 2002 of 1.6% for the Standard and Poor's 500 Index of U.S. companies and (7.3)% for the Morgan Stanley Capital International EAFE Index, which encompasses about 1,200 companies in Europe, Australasia and the Far East. The EAFE returns reflected a large drop in the Japanese market.

Equity markets exhibited weakness during the summer of 2001, as evidence of an economic slowdown mounted. The decline accelerated with the September 11th, 2001 events. At its lowest, the TSE 300 was 17% below its level at the beginning of PSP Investments' fiscal year. Aggressive easing of monetary policy, anticipation of increased fiscal stimulus and a positive turn in the Afghan war contributed to a recovery in the markets to January 2002. The recovery was also helped by consumer spending — which, although it experienced slower growth, never turned negative — benefiting from lower U.S. income taxes and reduced energy prices. Fixed income markets moved in the opposite direction to equity markets. For example, the price of the *10-year government of Canada bond* gained almost 9% from trough to peak, only to give back most of that gain in the second half of the fiscal year.



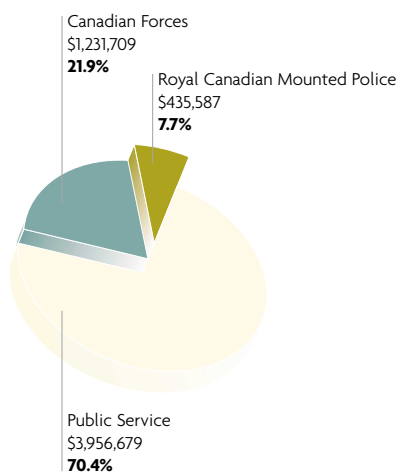
From left to right:
Éric Hamid
 Trader, Equities
Danielle G. Morin
 Chief Financial Officer
Nicole Goulet
 Administrative Assistant
Asif Haque
 Director, Performance Measurement
Claire Boucher
 Specialist, Investment Services

INVESTMENT RESULTS

In fiscal year 2002, the consolidated pension plan account produced an income of \$146.8 million. This compared with a loss of \$227 million in fiscal year 2001.

PLAN INVESTED ASSETS (As of March 31st, 2002)

% OF TOTAL ASSETS



RATES OF RETURN ON CONSOLIDATED PENSION PLAN ACCOUNT (For fiscal year 2002)

	PORTFOLIO RETURNS	BENCHMARK RETURNS	
Canadian Equities	4.7%	4.9%	TSE 300
Foreign Equities	(3.3)%	(2.6)%	S&P 500, EAFE*
Fixed Income	5.3%	5.1%	SC Bond Universe
Cash Equivalents	4.0%	3.7%	SC 91-day T-bill
Consolidated accounts	2.7%	2.8%	Policy Benchmark**

These are time-weighted rates of return, before fees and expenses, for the consolidation of the three pension plan accounts. They are calculated in accordance with the mandatory requirements set forth by AIMR*** and audited as such.

* In Canadian dollars, weighted by market capitalization.

** Based on weights in the investment policy. See page 7

*** Association for Investment Management and Research

RATES OF RETURN

The rate of return for the consolidated pension plan account in fiscal year 2002 was 2.7%, reflecting the market conditions noted above and resulting from a 4.7% rate of return for Canadian equities, a (3.3)% rate of return for Foreign equities, a 5.3% rate of return for Fixed-income, and a 4.0% rate of return for Cash equivalents.

This compares to a rate of return of 2.8% for PSP Investments' Policy Benchmark (see Benchmarks — Page 14) and a (4.1)% rate of return recorded by PSP Investments in fiscal year 2001.

Returns and benchmarks for each pension plan account are presented in Note 4 of their respective financial statements. The differences between the rates of return of the pension plan accounts are primarily due to different cash flow profiles. (See Cash Flows and Rebalancing — Page 10)

From left to right:
Dan Thanh Nguyen
 Director, Information Technology
Marie-Josée Côté
 Accountant
Ken Monds
 Director, Government/
 Plan Relations
Marie-Ange Bankamwabo
 Receptionist
Karolyne Vinet
 Director, Finance and Control



CHANGES IN NET ASSETS

The consolidated pension plan accounts began fiscal year 2002 with net assets of \$2.5 billion at market value. Consolidated net contributions during the fiscal year added \$3.0 billion. After factoring in the net income from operations, consolidated net assets as of the fiscal 2002 year-end were \$5.6 billion at market value.

EXPENSES

The cost of operating PSP Investments during fiscal year 2002 totalled \$7.3 million, compared to \$3.6 million in fiscal year 2001. The higher costs can be attributed mainly to the planned increase in the number of employees and related office expenses. Total expenses amounted to 0.18% of average assets — or 0.16% of average assets, when external investment management fees are excluded.

Looking ahead to fiscal year 2003, total expenses are expected to increase, reflecting the appointment of additional external managers and internal staff, as well as the amortization of investments in new computer systems. However, excluding external investment management fees, expenses expressed as a percentage of average assets should not vary significantly compared to those of fiscal year 2002.

PSP Investments' five-year plan takes into account the projected growth in assets and targets a lower ratio of expenses to average assets — again excluding external investment management fees — than is currently the case. The magnitude of external investment management fees will depend on the nature of the assets held and the speed at which the organization is able to continue assembling its internal team.

PERFORMANCE MEASUREMENT AND EVALUATION

Rigorous performance measurement is an essential tool for management to evaluate its internal and external investment managers. It is also the tool used by the Board of Directors and other stakeholders to evaluate the performance of PSP Investments.

The following principles are used to help ensure a precise measure of investment returns:

- Returns are time-weighted rates of return in Canadian dollars, calculated according to mandatory requirements set forth by the Association for Investment Management and Research (AIMR);
- Returns are measured at the portfolio, asset-class and total plan account levels for each of the three pension plan accounts and for total PSP Investments assets;
- Returns are calculated daily and geometrically compounded to calculate period returns;
- Returns are calculated on a gross basis (i.e. before external investment management fees and before all expenses); and
- Returns net of these items can also be calculated from data provided.

BENCHMARKS

- Each asset class — Canadian equities, foreign equities, Fixed-income and cash equivalents — has a benchmark defined in PSP Investments' Statement of Investment Policies, Standards and Procedures (SIP&P);
- The rate of return for each asset class is compared against the relevant asset-class benchmark rate of return;
- A Policy Benchmark has been created from the asset-class benchmarks and asset-class weights established in the SIP&P. These weights are rebalanced at the end of each month;
- The total fund return is compared to the Policy Benchmark return.

GOVERNANCE

Effective governance is essential in order to safeguard the capital entrusted to the Public Sector Pension Investment Board (PSP Investments) and to ensure that appropriate objectives are pursued and achieved in line with the fulfillment of its legislated mandate.

In this section of the annual report you will find pertinent information on the mandate itself, the role of the Board of Directors and key policies designed to guide the organization's activities and behaviour. New during the past fiscal year are Conflict of Interest Procedures, an amended Code of Conduct, formalized Proxy Voting Guidelines and a Policy on Social and Environmental Responsibility.

CONFLICT OF INTEREST PROCEDURES

In June 2001, the Board of Directors of PSP Investments formally approved Conflict of Interest Procedures for Directors, designating the Audit and Conflicts Committee to monitor their application.

The Board of Directors recognizes it is inevitable that conflicts of interest — or at least the appearance of such conflicts — will arise. The procedures are therefore intended to provide a workable process for identifying, minimizing and resolving potential conflicts of interest. They will help ensure that Directors have a full understanding and appreciation of PSP Investments' principles and values to assist them in determining appropriate business practices and behaviour.

The Conflict of Interest Procedures address such matters as the requirement for full disclosure; how and when a conflict may arise; deemed conflicts of interest; the duty to refrain from voting where a conflict exists; the use and disclosure of confidential information and the duty to report breaches.

The Conflict of Interest Procedures may be viewed in their entirety on PSP Investments' Web site: www.investpsp.ca

REVISED CODE OF CONDUCT

In accordance with its governing legislation, PSP Investments has a Code of Conduct for officers and employees. A revised version of the code, which incorporates more stringent reporting requirements that take into account the hiring of portfolio managers and securities traders, was approved by the Board of Directors in October 2001. As well as ensuring stringent compliance with the relevant statutory requirements, the code serves as a framework that provides officers and employees with a full understanding of the organization's corporate principles and values to assist them in determining appropriate business practices and behaviour.

- *Conflict of Interest Procedures for Directors address such matters as the requirement for full disclosure; how and when a conflict may arise; deemed conflicts of interest; the duty to refrain from voting where a conflict exists; the use and disclosure of confidential information and the duty to report breaches.*

Among other things, the code deals with honesty and integrity; compliance with the law; use of confidential information; reporting of personal investment transactions; receiving or giving of entertainment, gifts and favours from or to third parties; membership in and public representation of non-profit and professional associations; and personal use of PSP Investments' resources, assets and facilities. As well, PSP Investments maintains a restricted list of securities of which the organization has confidential knowledge. Officers and employees are prohibited from trading in securities on the restricted list.

The Board of Directors has mandated the Audit and Conflicts Committee to monitor the implementation and enforcement of the code.

The Code of Conduct may be viewed on PSP Investments' Web site: **www.investpsp.ca**

PROXY VOTING GUIDELINES

Proxy Voting Guidelines approved by the Board of Directors in February 2002 are designed to ensure that shares beneficially owned by PSP Investments will be voted in accordance with its investment policy and objectives.

The guidelines stipulate that PSP Investments will be particularly mindful of corporate governance principles when considering the merits of an issue and will exercise its voting rights with a view to maximizing the value of its shareholdings. The guidelines focus on four areas considered crucial in terms of their potential impact on performance:

- the independence, size and effectiveness of a company's board of directors;
- management and directors' compensation, including stock options and incentive compensation plans;
- takeover protection; and
- shareholder rights.

For instance, the guidelines favour boards that have a majority of unrelated directors as well as a separation of board and management roles.

The guidelines apply equally to securities managed internally and those held in portfolios managed for PSP Investments by external managers. Furthermore, the shares of all Canadian equity investments are voted internally, regardless of whether they are managed internally or externally. In the case of indexed funds, where PSP Investments is one of the owners of units in a pooled fund, it cannot legally impose a voting policy. However, the voting policies of external managers are reviewed to ensure consistency with PSP Investments' guidelines.

The Proxy Voting Guidelines may be viewed on PSP Investments' Web site: **www.investpsp.ca**

- *Proxy Voting Guidelines stipulate that PSP Investments will be particularly mindful of corporate governance principles when considering the merits of an issue and will exercise its voting rights with a view to maximizing the value of its shareholdings.*

POLICY ON SOCIAL AND ENVIRONMENTAL RESPONSIBILITY

During fiscal year 2002, the Board of Directors approved a Policy on Social and Environmental Responsibility pertaining to its investments. While recognizing that the primary responsibility of PSP Investments is to provide for the financial benefit of contributors to the plans and to support the fulfillment of the pension promise explicit in those plans, the policy states that “the environmental and social impact of the behaviour of corporations...may be one of a number of relevant factors that our investment professionals would wish to take into account in making investment decisions for the plans”.

The Policy on Social and Environmental Responsibility may be viewed on PSP Investments' Web site: www.investpsp.ca

LEGISLATED MANDATE

The legislated mandate of the Public Sector Pension Investment Board (PSP Investments) is:

- To manage funds received “in the best interests of the contributors and beneficiaries” of the three pension plans; and
- To invest “with a view to achieving a maximum rate of return without undue risk of loss, having regard to the funding, policies and requirements of the pension plans... and the ability of those plans to meet their financial obligations.”

The legislation states that PSP Investments shall not, directly or indirectly, carry on any business or activity or exercise any power inconsistent with these objectives.

RELATIONSHIP TO PENSION PLANS

Effective April 1, 2000, the federal government created three new pension funds — one each for the existing Public Service, Canadian Forces and Royal Canadian Mounted Police (RCMP) pension plans. These pension funds receive the employer and employee contributions in respect of each plan to provide for liabilities for service after April 1, 2000. The balances (that is, contributions after payment of benefits accrued since April 1, 2000 and after plan administration expenses) are transferred to separate accounts at PSP Investments, to be invested in financial markets.

The government is the sponsor and administrator of the plans. The President of the Treasury Board is responsible for the Public Service plan, the Minister of National Defence for the Canadian Forces plan, and the Solicitor General of Canada for the RCMP plan.

The President and CEO and the Chairperson meet once a year with the Advisory Committees of the three plans.

ACCOUNTABILITY AND REPORTING

PSP Investments' management is accountable to the Board of Directors. The Directors are accountable to Parliament through the President of the Treasury Board, who is responsible for PSP Investments' legislation and is required to table its annual report in Parliament. PSP Investments is required to provide quarterly financial statements and the annual report to the President of the Treasury Board, the Minister of National Defence and the Solicitor General of Canada. Annual meetings with the advisory committees of the three pension plans are also part of the rigorous reporting requirements.

SELECTION OF DIRECTORS

A Board of Directors comprised of 12 members, including the Chairperson, governs PSP Investments. The Governor in Council appoints all members on the recommendation of the President of the Treasury Board. Qualified candidates for directorship are selected and recommended to the President of the Treasury Board by an eight-member nominating committee that operates at arm's length from the government. PSP Investments' legislation disqualifies as Directors, members of the Senate, the House of Commons and provincial legislatures, federal government employees and those entitled to benefits from federal public sector pension plans. (A list of current Directors may be found on Page 50.)

DUTIES OF DIRECTORS

In order to ensure that legislated and regulatory objectives are fully met, the Board of Directors has defined its role to include, among other responsibilities, the following:

- Appointment of the President and Chief Executive Officer (CEO);
- Approval of a written Statement of Investment Policies, Standards and Procedures;
- Approval of strategies for achieving investment performance objectives;
- Adoption of appropriate policies for the proper conduct and management of PSP Investments, including a Code of Conduct, Conflict of Interest Procedures and risk management policy;
- Approval of human resources and compensation policies;
- Establishment of appropriate performance evaluation processes for the Board of Directors, the President and CEO and other members of senior management;
- Preparation and approval of quarterly and annual financial statements for each underlying pension fund and for PSP Investments.

BOARD COMMITTEES

The Board of Directors has established the following four committees to assist in the fulfillment of its obligations:

- Investment Committee;
- Audit and Conflicts Committee;
- Governance Committee; and
- Human Resources and Compensation Committee.

Recommendations of Board committees are subject to the approval of the full Board.

The Investment Committee consists of the full Board. The composition of the other committees is set out on page 50 of this report.

Further information relative to PSP Investments' committees may be viewed on PSP Investments' Website: www.investpsp.ca

DIRECTORS' COMPENSATION

Compensation for members of PSP Investments' Board of Directors is determined based on the median compensation received by directors of companies included in the Toronto Stock Exchange's TSE 300 Composite Index. It is reviewed every two to three years. Each Director receives a \$12,000 annual retainer. Chairs of committees are paid an additional \$3,000 retainer. A \$900 per-meeting fee is paid for each Board and Board committee meeting attended. However, only a single fee is paid when Board and Investment Committees meet jointly. (The Board met nine times during fiscal year 2002 and held 19 committee meetings.) The compensation paid to Directors during fiscal year 2002 is summarized in Note 5 (a) to the financial statements of PSP Investments.

ASSESSMENT OF BOARD PERFORMANCE

Regulations require that the Board of Directors set out in the annual report the procedures in place for the assessment of its own performance. A formal performance evaluation policy, adopted in accordance with those requirements, focuses on procedures designed to encourage frank and confidential discussions between the Chairperson and individual Directors, as well as between the Chairperson and the President and CEO of PSP Investments. To facilitate the assessment process, guidelines for evaluating the Board of Directors' performance are distributed once a year to every Director as well as to the President and CEO. The guidelines take the form of a questionnaire. Directors submit their completed questionnaires to the Chairperson, who utilizes the feedback during subsequent

one-on-one consultations with individual Directors and with the President and CEO. The discussions focus on concerns and opportunities for improvement, what is working properly or has improved since previous assessments. The outcome of these meetings is reviewed with the Governance Committee each January, following which a report summarizing the findings of the assessment process — complete with appropriate recommendations — is submitted to the full Board of Directors.



FINANCIAL STATEMENTS
AND NOTES TO THE FINANCIAL STATEMENTS

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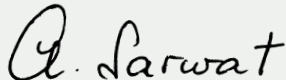
MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING

The financial statements of the Public Sector Pension Investment Board ("PSP Investments") have been prepared by management and approved by the Board of Directors. The financial statements have been prepared in accordance with Canadian generally accepted accounting principles. Management is responsible for the contents of the financial statements and the financial information contained in the annual report.

PSP Investments maintains records and systems of internal control and supporting procedures to provide reasonable assurance that PSP Investments' assets are safeguarded and controlled, and that transactions are in accordance with the *Public Sector Pension Investment Board Act*, the accompanying regulations, the by-laws, and the Statement of Investment Policies, Standards and Procedures.

The Audit and Conflicts Committee assists the Board of Directors in discharging its responsibility to approve the annual financial statements. The Committee meets regularly with both management and the external auditors to discuss the scope and findings of audits and other work that the external auditors may be requested to perform from time to time, to review financial information, and to discuss the adequacy of internal controls. The Committee reviews the annual financial statements and recommends them to the Board of Directors for approval.

PSP Investments' external auditors, Deloitte & Touche LLP, have conducted an independent examination of the financial statements in accordance with Canadian generally accepted auditing standards, performing such tests and other procedures as they consider necessary to express an opinion in their Auditors' Report. The external auditors have full and unrestricted access to management and the Audit and Conflicts Committee to discuss findings related to the integrity of PSP Investments' financial reporting and the adequacy of internal control systems.



Adel Sarwat
President and Chief Executive Officer
May 9, 2002



Danielle G. Morin
Chief Financial Officer
May 9, 2002

INVESTMENT CERTIFICATE

The Public Sector Pension Investment Board Act (the "Act") requires that a certificate be signed by a director on behalf of the Board of Directors, stating that the investments of the Public Sector Pension Investment Board ("PSP Investments") held during the year were in accordance with the Act and PSP Investments' investment policies, standards and procedures. Accordingly, the Investment Certificate follows:

"The investments of PSP Investments held during the year ended March 31, 2002, were in accordance with the Act and PSP Investments' Statement of Investment Policies, Standards and Procedures."



William R. C. Blundell
Chairperson
May 9, 2002

PUBLIC SERVICE PENSION PLAN ACCOUNT

Auditors' report

To the Board of Directors of
Public Sector Pension Investment Board – Public Service Pension Plan Account

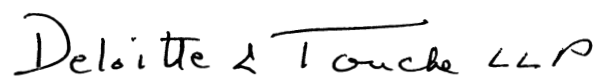
We have audited the Balance Sheet and the Statement of Investment Portfolio of the Public Sector Pension Investment Board – Public Service Pension Plan Account (the “Public Service Pension Plan Account”) as at March 31, 2002 and the Statements of Net Income/(Loss) and Accumulated Net Income/(Loss) from Operations and of Changes in Net Assets for the year then ended. These financial statements are the responsibility of the Public Sector Pension Investment Board's (“PSP Investments”) 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 Public Service Pension Plan Account and the investments held as at March 31, 2002 and the results of its operations and of changes in its net assets for the year then ended in accordance with Canadian generally accepted accounting principles.

Further, in our opinion, the transactions of the Public Service Pension Plan Account that have come to our notice during our audit of the financial statements have, in all significant respects, been in accordance with the *Public Sector Pension Investment Board Act* (the “Act”) and the by-laws.

Further, in our opinion, the record of investments kept by PSP Investments' management pursuant to paragraph 35 (1) (c) of the Act fairly presents, in all material respects, the information required by the Act.


Chartered Accountants

Montreal, Quebec
May 1, 2002

PUBLIC SERVICE PENSION PLAN ACCOUNT

Balance Sheet*As at March 31*

	2002 (\$000)	2001 (\$000)
ASSETS		
Investments – at fair value (Note 2)	3,956,679	1,789,506
Cash	19,036	106
Accrued income	15	26
Due from the Canadian Forces Pension Plan Account (Note 5)	516	270
Due from the Royal Canadian Mounted Police Pension Plan Account (Note 5)	182	95
	3,976,428	1,790,003
LIABILITIES		
Accounts payable and accrued liabilities	1,212	499
NET ASSETS	3,975,216	1,789,504
NET ASSETS REPRESENTED BY:		
Accumulated net income/(loss) from operations	(64,831)	(164,211)
Accumulated fund transfers	4,040,047	1,953,715
	3,975,216	1,789,504

On behalf of the Board of Directors:



Paul Cantor
Director and Chair of the Audit and Conflicts Committee

Statement of Changes in Net Assets*For the year ended March 31*

	2002 (\$000)	2001 (\$000)
NET ASSETS, BEGINNING OF YEAR	1,789,504	—
CHANGES IN NET ASSETS		
Fund transfers (Note 3)	2,086,332	1,953,715
Net income/(loss) from operations	99,380	(164,211)
NET ASSETS, END OF YEAR	3,975,216	1,789,504

PUBLIC SERVICE PENSION PLAN ACCOUNT

Statement of Net Income/(Loss) and Accumulated Net Income/(Loss) from Operations

For the year ended March 31

	2002 (\$000)	2001 (\$000)
INVESTMENT INCOME		
Interest and dividends	94,111	2,444
Net realized gains/(losses) (Note 2c)	(258,587)	(81)
Net unrealized gains/(losses)	268,988	(163,986)
	104,512	(161,623)
INVESTMENT AND ADMINISTRATIVE EXPENSES (Notes 5 and 6)		
Salaries and benefits	1,944	573
Operating expenses	1,610	758
External investment management fees	527	149
Professional and consulting fees	1,051	1,108
	5,132	2,588
NET INCOME/(LOSS) FROM OPERATIONS	99,380	(164,211)
ACCUMULATED NET INCOME/(LOSS) FROM OPERATIONS, BEGINNING OF THE YEAR	(164,211)	—
ACCUMULATED NET INCOME/(LOSS) FROM OPERATIONS, END OF THE YEAR	(64,831)	(164,211)

Statement of Investment Portfolio

As at March 31

Investments (Note 2)	2002*			2001**		
	Cost (\$000)	Fair Value (\$000)	% of Portfolio (At Fair Value)	Cost (\$000)	Fair Value (\$000)	% of Portfolio (At Fair Value)
CANADIAN EQUITIES						
PSP Canadian Equities Fund 131,307,615.207260 units	1,275,713	1,392,032	35.2	742,481	602,892	33.7
FOREIGN EQUITIES						
PSP Foreign Equities Fund 112,246,031.773966 units	1,142,418	1,189,917	30.0	538,615	483,148	27.0
FIXED INCOME						
PSP Fixed Income Fund 128,317,440.461707 units	1,315,631	1,256,819	31.8	656,109	687,179	38.4
CASH EQUIVALENTS						
PSP Cash Equivalents Fund 11,789,343.236263 units	117,915	117,911	3.0	16,287	16,287	0.9
	3,851,677	3,956,679	100.0%	1,953,492	1,789,506	100.0%

* As of October 2nd, 2001 the pooled fund investments held by the Public Service Pension Plan Account were transferred into PSP Funds.

** Investments were exclusively in pooled funds managed by State Street Global Advisors (SSgA).

PUBLIC SERVICE PENSION PLAN ACCOUNT

Notes to the Financial Statements*For the year ended March 31, 2002***ORGANIZATION**

The Public Sector Pension Investment Board ("PSP Investments") was formed pursuant to the *Public Sector Pension Investment Board Act* (the "Act") with a mandate to invest in financial markets the contributions to the Public Service, Canadian Forces and Royal Canadian Mounted Police pension plans. Prior to the implementation of the provisions of the Act, the balances of the plans were credited with a rate of interest based on long-term Government of Canada bonds.

The Public Service Pension Fund was established by amendments to the *Public Service Superannuation Act*, to receive contributions and make benefit payments in respect of member service after April 1, 2000. The excess of contributions over benefits is transferred, by the Public Service Pension Fund, to PSP Investments – Public Service Pension Plan Account for investment. PSP Investments maintains records of the Pension Fund's net contributions, as well as the allocation of its investments and the results of its operations to each of the Plan Accounts.

PSP Investments is responsible for managing amounts that are transferred to it in the best interests of the beneficiaries and contributors under the *Public Service Superannuation Act*. The amounts are to be invested with a view to achieving a maximum rate of return, without undue risk of loss, having regard to the funding, policies and requirements of the *Public Service Superannuation Act*.

1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES***Basis of presentation***

These financial statements present the financial position and operations of PSP Investments as they pertain to the investment of the excess funds transferred to it from the Public Service Pension Fund. Accordingly, they do not reflect all of the assets, or the details of the pension contributions, payments and liabilities of the Public Service Pension Fund. The statements have been prepared in accordance with Canadian generally accepted accounting principles and the requirements of the Act.

Valuation of investments

Investments consist of the unit interest in PSP Investments' assets (The PSP Funds) that are allocated to this Plan Account. Investments are recorded as of the trade date and are stated at fair value. Fair value is the amount of the consideration that would be agreed upon in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act. Fair value for investments in pooled funds is based on unit values, which reflect the quoted market prices of the underlying securities.

Income recognition

The investment income has been allocated by PSP Investments according to the number of units of PSP Funds held by the Public Service Pension Plan Account.

Investment income is recorded on the accrual basis and represents realized gains and losses on the disposal of investments, unrealized gains and losses on investments held at the end of the year, interest income and dividends. These income items include the related distributions from PSP Funds.

Translation of foreign currencies

Transactions in foreign currencies are recorded at the rates of exchange on the transaction date. Investments denominated in foreign currencies and held at the end of the year are translated at exchange rates in effect at the year end date. The resulting realized and unrealized gains and losses on foreign exchange are included in investment income.

Fund transfers

Amounts received from the Public Service Pension Fund are recorded on a cash basis.

Income Taxes

PSP Investments is exempt from Part I tax under paragraph 149 (1)(d) of the *Income Tax Act* (Canada).

Use of estimates

In preparing these financial statements, management must make certain estimates and assumptions which can affect the reported values of assets and liabilities, related income and expenses and note disclosures. Actual results may differ from estimates.

PUBLIC SERVICE PENSION PLAN ACCOUNT

Notes to the Financial Statements

For the year ended March 31, 2002

2 INVESTMENTS

The Statement of Investment Portfolio provides details of investments held as at March 31, 2002.

(a) Investment Policy

PSP Investments has established a Statement of Investment Policies, Standards and Procedures, (the "Investment Policy") which sets out the manner in which the assets shall be invested for the Public Service Pension Plan Account. Asset mix policy and benchmarks at March 31, 2002 were as follows:

Asset Class	Policy Mix	Benchmark
Canadian Equities	35.0%	TSE 300
Foreign Equities	30.0%	S&P 500, MSCI EAFE
Fixed Income	32.0%	SC Bond Universe
Cash Equivalents	3.0%	SC 91-day T-bill

Prior to October 25, 2001, the Regulations of the *Act* stipulated that the investments of PSP Investments in Canadian equities had to substantially replicate the composition of one or more widely recognized broad market indices. The Toronto Stock Exchange 300 Composite Index (TSE 300) had been selected as an appropriate market index for Canadian equities. On October 25, 2001, an amendment to the Regulations of the *Act* enabled PSP Investments to invest without replicating a widely recognized Canadian equity index.

(b) Foreign currency exposure

This Plan Account is exposed to currency risk through holdings of units in PSP Funds of non-Canadian equities where investment values will fluctuate due to changes in foreign exchange rates. The underlying foreign currency exposures by currency as at March 31 were as follows:

Currency	2002		2001	
	Fair Value (\$000)	% of Total	Fair Value (\$000)	% of Total
US dollars	683,437	57.4	240,754	49.8
Euro	190,156	16.0	99,577	20.6
British pound	125,913	10.6	52,427	10.9
Yen	103,686	8.7	58,013	12.0
Others	86,725	7.3	32,377	6.7
	1,189,917	100.0%	483,148	100.0%

In accordance with the Investment Policy, foreign currency exposures are not hedged.

(c) Transfer of SSgA Pooled Fund units to PSP Funds

On October 2nd 2001, PSP Investments created the PSP Funds and the units in SSgA pooled funds previously held in the name of this Plan Account were transferred to the PSP Funds. This deemed disposition caused previously unrealized losses to become realized in the Statement of Net Income/(Loss) and Accumulated Net Income/(Loss) from Operations for this Plan Account. This has no impact on the Plan Account, except for bringing the Investments cost values closer to their fair values.

3 FUND TRANSFERS

During the year, PSP Investments received \$ 2,086.3 million (2001- \$1,953.7 million) of transfers from the Public Service Pension Fund. The transfers result from net current employer and employee contributions to the Public Service Pension Plan.

PUBLIC SERVICE PENSION PLAN ACCOUNT

Notes to the Financial Statements

For the year ended March 31, 2002

4 INVESTMENT PERFORMANCE

Portfolio and benchmark returns for the year ended March 31 were as follows:

	2002		2001		
	Portfolio Returns	Benchmark Returns	Portfolio Returns	Benchmark Returns	
Canadian Equities	4.7%	4.9%	(11.8)%	(12.2)%	TSE 300
Foreign Equities	(3.3)%	(2.6)%	(13.2)%	(13.0)%	S&P 500 & MSCI EAFE
Fixed Income	5.3%	5.1%	8.3%	8.3%	SC Bond Universe
Cash Equivalents	4.0%	3.7%	—	—	SC 91-day T-Bill
Total return	2.7%	2.8%	(3.8)%	(4.0)%	

The Total Benchmark return aggregates the asset class benchmark returns according to the weights specified in the Investment Policy, as disclosed in Note 2(a).

Returns have been calculated in accordance with the mandatory requirements set forth by the Association for Investment Management and Research (AIMR). Returns are presented gross of investment and administrative expenses.

5 INVESTMENT AND ADMINISTRATIVE EXPENSES

The *Act* requires that the costs of operation of PSP Investments be charged to the three plans for which it provides investment services. Under section 4 (3) of the *Act*, the President of the Treasury Board shall determine to which Plan Account these costs will be charged, in consultation with the Minister of National Defence and the Solicitor General of Canada. An allocation policy has been developed which allocates the direct costs of investment activities, such as investment management and custodial fees, to each Plan Account, and allocates administrative costs, such as salaries and benefits, advisory services, directors' fees and other administration costs, based upon the asset value of each Plan Account.

Administrative costs have been allocated on a quarterly basis according to the policy, resulting in an allocation as follows:

	2002	2001
Public Service Pension Plan Account	70.6%	71.9%
Canadian Forces Pension Plan Account	21.7%	21.0%
Royal Canadian Mounted Police Pension Plan Account	7.7%	7.1%

The costs of operations are financed by the Public Service Pension Plan Account, which is reimbursed by the other Plan Accounts on a quarterly basis.

Further details of Investment and Administrative expenses are shown in the PSP Investments Financial Statements.

6 COMPARATIVE FIGURES

Certain comparative figures have been reclassified to conform with the current year presentation.

The Custody fees were previously included in External investment expenses. They were transferred to Operating expenses to allow better disclosure of the External Investment management fees.

CANADIAN FORCES PENSION PLAN ACCOUNT

Auditors' report

To the Board of Directors of
Public Sector Pension Investment Board – Canadian Forces Pension Plan Account

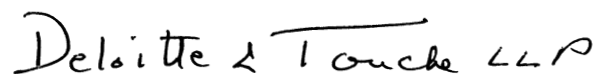
We have audited the Balance Sheet and the Statement of Investment Portfolio of the Public Sector Pension Investment Board – Canadian Forces Pension Plan Account (the “Canadian Forces Pension Plan Account”) as at March 31, 2002 and the Statements of Net Income/(Loss) and Accumulated Net Income/(Loss) from Operations and of Changes in Net Assets for the year then ended. These financial statements are the responsibility of the Public Sector Pension Investment Board's (“PSP Investments”) 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 Canadian Forces Pension Plan Account and the investments held as at March 31, 2002 and the results of its operations and of changes in its net assets for the year then ended in accordance with Canadian generally accepted accounting principles.

Further, in our opinion, the transactions of the Canadian Forces Pension Plan Account that have come to our notice during our audit of the financial statements have, in all significant respects, been in accordance with the *Public Sector Pension Investment Board Act* (the “Act”) and the by-laws.

Further, in our opinion, the record of investments kept by PSP Investments' management pursuant to paragraph 35 (1) (c) of the *Act* fairly presents, in all material respects, the information required by the *Act*.



Chartered Accountants

Montreal, Quebec
May 1, 2002

CANADIAN FORCES PENSION PLAN ACCOUNT

Balance Sheet

As at March 31

	2002 (\$000)	2001 (\$000)
ASSETS		
Investments – at fair value (Note 2)	1,231,709	532,690
Cash	5,009	43
Accrued income	2	5
	1,236,720	532,738
LIABILITIES		
Accounts payable and accrued liabilities	156	22
Due to Public Service Pension Plan Account (Note 5)	516	270
	672	292
NET ASSETS	1,236,048	532,446
NET ASSETS REPRESENTED BY:		
Accumulated net income/(loss) from operations	(19,041)	(48,631)
Accumulated fund transfers	1,255,089	581,077
	1,236,048	532,446

On behalf of the Board of Directors:



Paul Cantor
Director and Chair of the Audit and Conflicts Committee

Statement of Changes in Net Assets

For the year ended March 31

	2002 (\$000)	2001 (\$000)
NET ASSETS, BEGINNING OF YEAR	532,446	—
CHANGES IN NET ASSETS		
Fund transfers (Note 3)	674,012	581,077
Net income/(loss) from operations	29,590	(48,631)
NET ASSETS, END OF YEAR	1,236,048	532,446

CANADIAN FORCES PENSION PLAN ACCOUNT

Statement of Net Income/(Loss) and Accumulated Net Income/(Loss) from Operations

For the year ended March 31

	2002 (\$000)	2001 (\$000)
INVESTMENT INCOME		
Interest and dividends	30,047	678
Net realized gains/(losses) (Note 2c)	(79,064)	(17)
Net unrealized gains/(losses)	80,195	(48,530)
	31,178	(47,869)
INVESTMENT AND ADMINISTRATIVE EXPENSES (Notes 5 and 6)		
Salaries and benefits	600	167
Operating expenses	497	230
External investment management fees	166	42
Professional and consulting fees	325	323
	1,588	762
NET INCOME/(LOSS) FROM OPERATIONS	29,590	(48,631)
ACCUMULATED NET INCOME/(LOSS) FROM OPERATIONS, BEGINNING OF THE YEAR	(48,631)	—
ACCUMULATED NET INCOME/(LOSS) FROM OPERATIONS, END OF THE YEAR	(19,041)	(48,631)

Statement of Investment Portfolio

As at March 31

Investments (Note 2)	2002*			2001**		
	Cost (\$000)	Fair Value (\$000)	% of Portfolio (At Fair Value)	Cost (\$000)	Fair Value (\$000)	% of Portfolio (At Fair Value)
CANADIAN EQUITIES						
PSP Canadian Equities Fund 40,876,309.185290 units	396,886	433,342	35.2	221,110	180,831	33.9
FOREIGN EQUITIES						
PSP Foreign Equities Fund 34,941,663.738446 units	356,213	370,415	30.0	159,042	141,861	26.7
FIXED INCOME						
PSP Fixed Income Fund 39,944,989.127895 units	410,241	391,246	31.8	196,404	205,333	38.5
CASH EQUIVALENTS						
PSP Cash Equivalents Fund 3,670,000.853579 units	36,705	36,706	3.0	4,665	4,665	0.9
	1,200,045	1,231,709	100.0%	581,221	532,690	100.0%

* As of October 2nd, 2001 the pooled fund investments held by the Canadian Forces Pension Plan Account were transferred into PSP Funds.

** Investments were exclusively in pooled funds managed by State Street Global Advisors (SSgA).

CANADIAN FORCES PENSION PLAN ACCOUNT

Notes to the Financial Statements*For the year ended March 31, 2002***ORGANIZATION**

The Public Sector Pension Investment Board ("PSP Investments") was formed pursuant to the *Public Sector Pension Investment Board Act* (the "Act") with a mandate to invest in financial markets the contributions to the Public Service, Canadian Forces and Royal Canadian Mounted Police pension plans. Prior to the implementation of the provisions of the Act, the balances of the plans were credited with a rate of interest based on long-term Government of Canada bonds.

The Canadian Forces Pension Fund was established by amendments to the *Canadian Forces Superannuation Act*, to receive contributions and make benefit payments in respect of member service after April 1, 2000. The excess of contributions over benefits is transferred, by the Canadian Forces Pension Fund, to PSP Investments – Canadian Forces Pension Plan Account for investment. PSP Investments maintains records of the Pension Fund's net contributions, as well as the allocation of its investments and the results of its operations to each of the Plan Accounts.

PSP Investments is responsible for managing amounts that are transferred to it in the best interests of the beneficiaries and contributors under the *Canadian Forces Superannuation Act*. The amounts are to be invested with a view to achieving a maximum rate of return, without undue risk of loss, having regard to the funding, policies and requirements of the *Canadian Forces Superannuation Act*.

1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES***Basis of presentation***

These financial statements present the financial position and operations of PSP Investments as they pertain to the investment of the excess funds transferred to it from the Canadian Forces Pension Fund. Accordingly, they do not reflect all of the assets, or the details of the pension contributions, payments and liabilities of the Canadian Forces Pension Fund. The statements have been prepared in accordance with Canadian generally accepted accounting principles and the requirements of the Act.

Valuation of investments

Investments consist of the unit interest in PSP Investments' assets (The PSP Funds) that are allocated to this Plan Account. Investments are recorded as of the trade date and are stated at fair value. Fair value is the amount of the consideration that would be agreed upon in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act. Fair value for investments in pooled funds is based on unit values, which reflect the quoted market prices of the underlying securities.

Income recognition

The investment income has been allocated by PSP Investments according to the number of units of PSP Funds held by the Canadian Forces Pension Plan Account.

Investment income is recorded on the accrual basis and represents realized gains and losses on the disposal of investments, unrealized gains and losses on investments held at the end of the year, interest income and dividends. These income items include the related distributions from PSP Funds.

Translation of foreign currencies

Transactions in foreign currencies are recorded at the rates of exchange on the transaction date. Investments denominated in foreign currencies and held at the end of the year are translated at exchange rates in effect at the year end date. The resulting realized and unrealized gains and losses on foreign exchange are included in investment income.

Fund transfers

Amounts received from the Canadian Forces Pension Fund are recorded on a cash basis.

Income Taxes

PSP Investments is exempt from Part I tax under paragraph 149 (1) (d) of the *Income Tax Act* (Canada).

Use of estimates

In preparing these financial statements, management must make certain estimates and assumptions which can affect the reported values of assets and liabilities, related income and expenses and note disclosures. Actual results may differ from estimates.

CANADIAN FORCES PENSION PLAN ACCOUNT

Notes to the Financial Statements*For the year ended March 31, 2002***2 INVESTMENTS**

The Statement of Investment Portfolio provides details of investments held as at March 31, 2002.

(a) Investment Policy

PSP Investments has established a Statement of Investment Policies, Standards and Procedures, (the "Investment Policy") which sets out the manner in which the assets shall be invested for the Canadian Forces Pension Plan Account. Asset mix policy and benchmarks at March 31, 2002 were as follows:

Asset Class	Policy Mix	Benchmark
Canadian Equities	35.0%	TSE 300
Foreign Equities	30.0%	S&P 500, MSCI EAFE
Fixed Income	32.0%	SC Bond Universe
Cash Equivalents	3.0%	SC 91-day T-bill

Prior to October 25, 2001, the Regulations of the *Act* stipulated that the investments of PSP Investments in Canadian equities had to substantially replicate the composition of one or more widely recognized broad market indices. The Toronto Stock Exchange 300 Composite Index (TSE 300) had been selected as an appropriate market index for Canadian equities. On October 25, 2001, an amendment to the Regulations of the *Act* enabled PSP Investments to invest without replicating a widely recognized Canadian equity index.

(b) Foreign currency exposure

This Plan Account is exposed to currency risk through holdings of units in PSP Funds of non-Canadian equities where investment values will fluctuate due to changes in foreign exchange rates. The underlying foreign currency exposures by currency as at March 31 were as follows:

Currency	2002		2001	
	Fair Value (\$000)	% of Total	Fair Value (\$000)	% of Total
US dollars	212,751	57.4	71,294	50.3
Euro	59,195	16.0	27,499	19.4
British pound	39,196	10.6	15,249	10.7
Yen	32,277	8.7	16,941	11.9
Others	26,996	7.3	10,878	7.7
	370,415	100.0%	141,861	100.0%

In accordance with the Investment Policy, foreign currency exposures are not hedged.

(c) Transfer of SSgA Pooled Fund units to PSP Funds

On October 2nd 2001, PSP Investments created the PSP Funds and the units in SSgA pooled funds previously held in the name of this Plan Account were transferred to the PSP Funds. This deemed disposition caused previously unrealized losses to become realized in the Statement of Net Income/(Loss) and Accumulated Net Income/(Loss) from Operations for this Plan Account. This has no impact on the Plan Account, except for bringing the Investments cost values closer to their fair values.

3 FUND TRANSFERS

During the year, PSP Investments received \$674.0 million (2001- \$581.1 million) of transfers from the Canadian Forces Pension Fund. The transfers result from net current employer and employee contributions to the Canadian Forces Pension Plan.

CANADIAN FORCES PENSION PLAN ACCOUNT

Notes to the Financial Statements

For the year ended March 31, 2002

4 INVESTMENT PERFORMANCE

Portfolio and benchmark returns for the year ended March 31 were as follows:

	2002		2001		
	Portfolio Returns	Benchmark Returns	Portfolio Returns	Benchmark Returns	
Canadian Equities	4.7%	4.9%	(11.9)%	(12.2)%	TSE 300
Foreign Equities	(3.3)%	(2.6)%	(13.2)%	(13.0)%	S&P 500 & MSCI EAFE
Fixed Income	5.3%	5.1%	8.3%	8.3%	SC Bond Universe
Cash Equivalents	4.1%	3.7%	—	—	SC 91-day T-Bill
Total return	2.8%	2.8%	(4.2)%	(4.0)%	

The Total Benchmark return aggregates the asset class benchmark returns according to the weights specified in the Investment Policy, as disclosed in Note 2(a).

Returns have been calculated in accordance with the mandatory requirements set forth by the Association for Investment Management and Research (AIMR). Returns are presented gross of investment and administrative expenses.

5 INVESTMENT AND ADMINISTRATIVE EXPENSES

The *Act* requires that the costs of operation of PSP Investments be charged to the three plans for which it provides investment services. Under section 4 (3) of the *Act*, the President of the Treasury Board shall determine to which Plan Account these costs will be charged, in consultation with the Minister of National Defence and the Solicitor General of Canada. An allocation policy has been developed which allocates the direct costs of investment activities, such as investment management and custodial fees, to each Plan Account, and allocates administrative costs, such as salaries and benefits, advisory services, directors' fees and other administration costs, based upon the asset value of each Plan Account.

Administrative costs have been allocated on a quarterly basis according to the policy, resulting in an allocation as follows:

	2002	2001
Public Service Pension Plan Account	70.6%	71.9%
Canadian Forces Pension Plan Account	21.7%	21.0%
Royal Canadian Mounted Police Pension Plan Account	7.7%	7.1%

The costs of operations are financed by the Public Service Pension Plan Account, which is reimbursed by the other Plan Accounts on a quarterly basis.

Further details of Investment and Administrative expenses are shown in the PSP Investments Financial Statements.

6 COMPARATIVE FIGURES

Certain comparative figures have been reclassified to conform with the current year presentation.

The Custody fees were previously included in External investment expenses. They were transferred to Operating expenses to allow better disclosure of the External Investment management fees.

ROYAL CANADIAN MOUNTED POLICE PENSION PLAN ACCOUNT

Auditors' report

To the Board of Directors of
Public Sector Pension Investment Board – Royal Canadian Mounted Police Pension
Plan Account

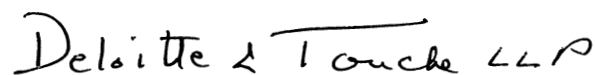
We have audited the Balance Sheet and the Statement of Investment Portfolio of the Public Sector Pension Investment Board – Royal Canadian Mounted Police Pension Plan Account (the “Royal Canadian Mounted Police Pension Plan Account”) as at March 31, 2002 and the Statements of Net Income/(Loss) and Accumulated Net Income/(Loss) from Operations and of Changes in Net Assets for the year then ended. These financial statements are the responsibility of the Public Sector Pension Investment Board's (“PSP Investments”) 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 Royal Canadian Mounted Police Pension Plan Account and the investments held as at March 31, 2002 and the results of its operations and of changes in its net assets for the year then ended in accordance with Canadian generally accepted accounting principles.

Further, in our opinion, the transactions of the Royal Canadian Mounted Police Pension Plan Account that have come to our notice during our audit of the financial statements, have, in all significant respects, been in accordance with the *Public Sector Pension Investment Board Act* (the “Act”) and the by-laws.

Further, in our opinion, the record of investments kept by PSP Investments' management pursuant to paragraph 35 (1) (c) of the *Act* fairly presents, in all material respects, the information required by the *Act*.



Chartered Accountants

Montreal, Quebec
May 1, 2002

ROYAL CANADIAN MOUNTED POLICE PENSION PLAN ACCOUNT

Balance Sheet*As at March 31*

	2002 (\$000)	2001 (\$000)
ASSETS		
Investments – at fair value (Note 2)	435,587	188,905
Cash	26	16
Accrued income	—	2
	435,613	188,923
LIABILITIES		
Accounts payable and accrued liabilities	56	10
Due to Public Service Pension Plan Account (Note 5)	182	95
	238	105
NET ASSETS	435,375	188,818
NET ASSETS REPRESENTED BY:		
Accumulated net income/(loss) from operations	(7,153)	(17,692)
Accumulated fund transfers	442,528	206,510
	435,375	188,818

On behalf of the Board of Directors:



Paul Cantor
Director and Chair of the Audit and Conflicts Committee

Statement of Changes in Net Assets*For the year ended March 31*

	2002 (\$000)	2001 (\$000)
NET ASSETS, BEGINNING OF YEAR	188,818	—
CHANGES IN NET ASSETS		
Fund transfers (Note 3)	236,018	206,510
Net income/(loss) from operations	10,539	(17,692)
NET ASSETS, END OF YEAR	435,375	188,818

ROYAL CANADIAN MOUNTED POLICE PENSION PLAN ACCOUNT

Statement of Net Income/(Loss) and Accumulated Net Income/(Loss) from Operations

For the year ended March 31

	2002 (\$000)	2001 (\$000)
INVESTMENT INCOME		
Interest and dividends	10,791	204
Net realized gains/(losses) (Note 2c)	(28,493)	(6)
Net unrealized gains/(losses)	28,807	(17,635)
	11,105	(17,437)
INVESTMENT AND ADMINISTRATIVE EXPENSES (Notes 5 and 6)		
Salaries and benefits	212	56
Operating expenses	181	85
External investment management fees	58	6
Professional and consulting fees	115	108
	566	255
NET INCOME/(LOSS) FROM OPERATIONS	10,539	(17,692)
ACCUMULATED NET INCOME/(LOSS) FROM OPERATIONS, BEGINNING OF THE YEAR	(17,692)	—
ACCUMULATED NET INCOME/(LOSS) FROM OPERATIONS, END OF THE YEAR	(7,153)	(17,692)

Statement of Investment Portfolio

As at March 31

Investments (Note 2)	2002*			2001**		
	Cost (\$000)	Fair Value (\$000)	% of Portfolio (At Fair Value)	Cost (\$000)	Fair Value (\$000)	% of Portfolio (At Fair Value)
CANADIAN EQUITIES						
PSP Canadian Equities Fund 14,455,756.369672 units	140,267	153,250	35.2	79,320	64,506	34.1
FOREIGN EQUITIES						
PSP Foreign Equities Fund 12,356,845.579382 units	126,052	130,994	30.0	56,693	50,729	26.9
FIXED INCOME						
PSP Fixed Income Fund 14,126,327.385281 units	145,114	138,362	31.8	70,527	73,670	39.0
CASH EQUIVALENTS						
PSP Cash Equivalents Fund 1,297,875.834010 units	12,982	12,981	3.0	—	—	—
	424,415	435,587	100.0%	206,540	188,905	100.0%

* As of October 2nd, 2001 the pooled fund investments held by the Royal Canadian Mounted Police Pension Plan Account were transferred into PSP Funds.

** Investments were exclusively in pooled funds managed by State Street Global Advisors (SSgA).

ROYAL CANADIAN MOUNTED POLICE PENSION PLAN ACCOUNT

Notes to the Financial Statements*For the year ended March 31, 2002***ORGANIZATION**

The Public Sector Pension Investment Board ("PSP Investments") was formed pursuant to the *Public Sector Pension Investment Board Act* (the "Act") with a mandate to invest in financial markets the contributions to the Public Service, Canadian Forces and Royal Canadian Mounted Police pension plans. Prior to the implementation of the provisions of the Act, the balances of the plans were credited with a rate of interest based on long-term Government of Canada bonds.

The Royal Canadian Mounted Police Pension Fund was established by amendments to the *Royal Canadian Mounted Police Superannuation Act*, to receive contributions and make benefit payments in respect of member service after April 1, 2000. The excess of contributions over benefits is transferred, by the Royal Canadian Mounted Police Pension Fund, to PSP Investments — Royal Canadian Mounted Police Pension Plan Account for investment. PSP Investments maintains records of the Pension Fund's net contributions, as well as the allocation of its investments and the results of its operations to each of the Plan Accounts.

PSP Investments is responsible for managing amounts that are transferred to it in the best interests of the beneficiaries and contributors under the *Royal Canadian Mounted Police Superannuation Act*. The amounts are to be invested with a view to achieving a maximum rate of return, without undue risk of loss, having regard to the funding, policies and requirements of the *Royal Canadian Mounted Police Superannuation Act*.

1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES***Basis of presentation***

These financial statements present the financial position and operations of PSP Investments as they pertain to the investment of the excess funds transferred to it from the Royal Canadian Mounted Police Pension Fund. Accordingly, they do not reflect all of the assets, or the details of the pension contributions, payments and liabilities of the Royal Canadian Mounted Police Pension Fund. The statements have been prepared in accordance with Canadian generally accepted accounting principles and the requirements of the Act.

Valuation of investments

Investments consist of the unit interest in PSP Investments' assets (The PSP Funds) that are allocated to this Plan Account. Investments are recorded as of the trade date and are stated at fair value. Fair value is the amount of the consideration that would be agreed upon in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act. Fair value for investments in pooled funds is based on unit values, which reflect the quoted market prices of the underlying securities.

Income recognition

The investment income has been allocated by PSP Investments according to the number of units of PSP Funds held by the Royal Canadian Mounted Police Pension Plan Account.

Investment income is recorded on the accrual basis and represents realized gains and losses on the disposal of investments, unrealized gains and losses on investments held at the end of the year, interest income and dividends. These income items include the related distributions from PSP Funds.

Translation of foreign currencies

Transactions in foreign currencies are recorded at the rates of exchange on the transaction date. Investments denominated in foreign currencies and held at the end of the year are translated at exchange rates in effect at the year end date. The resulting realized and unrealized gains and losses on foreign exchange are included in investment income.

Fund transfers

Amounts received from the Royal Canadian Mounted Police Pension Fund are recorded on a cash basis.

Income Taxes

PSP Investments is exempt from Part I tax under paragraph 149 (1) (d) of the *Income Tax Act* (Canada).

Use of estimates

In preparing these financial statements, management must make certain estimates and assumptions which can affect the reported values of assets and liabilities, related income and expenses and note disclosures. Actual results may differ from estimates.

ROYAL CANADIAN MOUNTED POLICE PENSION PLAN ACCOUNT

Notes to the Financial Statements

For the year ended March 31, 2002

2 INVESTMENTS

The Statement of Investment Portfolio provides details of investments held as at March 31, 2002.

(a) Investment Policy

PSP Investments has established a Statement of Investment Policies, Standards and Procedures, (the "Investment Policy") which sets out the manner in which the assets shall be invested for the Royal Canadian Mounted Police Pension Plan Account. Asset mix policy and benchmarks at March 31, 2002 were as follows:

Asset Class	Policy Mix	Benchmark
Canadian Equities	35.0%	TSE 300
Foreign Equities	30.0%	S&P 500, MSCI EAFE
Fixed Income	32.0%	SC Bond Universe
Cash Equivalents	3.0%	SC 91-day T-bill

Prior to October 25, 2001, the Regulations of the *Act* stipulated that the investments of PSP Investments in Canadian equities had to substantially replicate the composition of one or more widely recognized broad market indices. The Toronto Stock Exchange 300 Composite Index (TSE 300) had been selected as an appropriate market index for Canadian equities. On October 25, 2001, an amendment to the Regulations of the *Act* enabled PSP Investments to invest without replicating a widely recognized Canadian equity index.

(b) Foreign currency exposure

This Plan Account is exposed to currency risk through holdings of units in PSP Funds of non-Canadian equities where investment values will fluctuate due to changes in foreign exchange rates. The underlying foreign currency exposures by currency as at March 31 were as follows:

Currency	2002		2001	
	Fair Value (\$000)	% of Total	Fair Value (\$000)	% of Total
US dollars	75,238	57.4	25,336	49.9
Euro	20,934	16.0	10,432	20.6
British pound	13,861	10.6	5,482	10.8
Yen	11,414	8.7	6,092	12.0
Others	9,547	7.3	3,387	6.7
	130,994	100.0%	50,729	100.0%

In accordance with the Investment Policy, foreign currency exposures are not hedged.

(c) Transfer of SSgA Pooled Fund units to PSP Funds

On October 2nd 2001, PSP Investments created the PSP Funds and the units in SSgA pooled funds previously held in the name of this Plan Account were transferred to the PSP Funds. This deemed disposition caused previously unrealized losses to become realized in the Statement of Net Income/(Loss) and Accumulated Net Income/(Loss) from Operations for this Plan Account. This has no impact on the Plan Account, except for bringing the Investments cost values closer to their fair values.

3 FUND TRANSFERS

During the year, PSP Investments received \$236.0 million (2001- \$206.5 million) of transfers from the Royal Canadian Mounted Police Pension Fund. The transfers result from net current employer and employee contributions to the Royal Canadian Mounted Police Pension Plan.

ROYAL CANADIAN MOUNTED POLICE PENSION PLAN ACCOUNT

Notes to the Financial Statements

For the year ended March 31, 2002

4 INVESTMENT PERFORMANCE

Portfolio and benchmark returns for the year ended March 31 were as follows:

	2002		2001		
	Portfolio Returns	Benchmark Returns	Portfolio Returns	Benchmark Returns	
Canadian Equities	4.8%	4.9%	(14.5)%	(14.8)%	TSE 300
Foreign Equities	(3.3)%	(2.6)%	(13.6)%	(13.6)%	S&P 500 & MSCI EAFE
Fixed Income	5.3%	5.1%	8.5%	8.5%	SC Bond Universe
Cash Equivalents	4.0%	3.7%	—	—	SC 91-day T-Bill
Total return	2.7%	2.8%	(6.2)%	(5.1)%	

The Total Benchmark return aggregates the asset class benchmark returns according to the weights specified in the Investment Policy, as disclosed in Note 2(a).

Returns have been calculated in accordance with the mandatory requirements set forth by the Association for Investment Management and Research (AIMR). Returns are presented gross of investment and administrative expenses.

5 INVESTMENT AND ADMINISTRATIVE EXPENSES

The *Act* requires that the costs of operation of PSP Investments be charged to the three plans for which it provides investment services. Under section 4 (3) of the *Act*, the President of the Treasury Board shall determine to which Plan Account these costs will be charged, in consultation with the Minister of National Defence and the Solicitor General of Canada. An allocation policy has been developed which allocates the direct costs of investment activities, such as investment management and custodial fees, to each Plan Account, and allocates administrative costs, such as salaries and benefits, advisory services, directors' fees and other administration costs, based upon the asset value of each Plan Account.

Administrative costs have been allocated on a quarterly basis according to the policy, resulting in an allocation as follows:

	2002	2001
Public Service Pension Plan Account	70.6%	71.9%
Canadian Forces Pension Plan Account	21.7%	21.0%
Royal Canadian Mounted Police Pension Plan Account	7.7%	7.1%

The costs of operations are financed by the Public Service Pension Plan Account, which is reimbursed by the other Plan Accounts on a quarterly basis.

Further details of Investment and Administrative expenses are shown in the PSP Investments Financial Statements.

6 COMPARATIVE FIGURES

Certain comparative figures have been reclassified to conform with the current year presentation.

The Custody fees were previously included in External investment expenses. They were transferred to Operating expenses to allow better disclosure of the External Investment management fees.

PUBLIC SECTOR PENSION INVESTMENT BOARD

Auditors' report

To the Board of Directors of
Public Sector Pension Investment Board

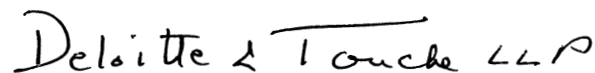
We have audited the Balance Sheet and the Statement of Investment Portfolio of the Public Sector Pension Investment Board ("PSP Investments") as at March 31, 2002 and the Statements of Net Income/(Loss) from Operations and of Changes in Net Assets for the year then ended. These financial statements are the responsibility of the PSP Investments 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 PSP Investments and the investments held as at March 31, 2002 and the results of its operations and of changes in its net assets for the year then ended in accordance with Canadian generally accepted accounting principles.

Further, in our opinion, the transactions of PSP Investments that have come to our notice during our audit of the financial statements, have, in all significant respects, been in accordance with the *Public Sector Pension Investment Board Act* (the "Act") and the by-laws.

Further, in our opinion, the record of investments kept by PSP Investments' management pursuant to paragraph 35 (1) (c) of the *Act* fairly presents, in all material respects, the information required by the *Act*.



Chartered Accountants

Montreal, Quebec
May 1, 2002

PUBLIC SECTOR PENSION INVESTMENT BOARD

Balance Sheet

As at March 31

	2002 (\$000)	2001 (\$000)
ASSETS		
Investments – at fair value (Note 2)	5,623,975	2,511,101
Cash	24,633	165
Accrued income	17	33
Other assets	247	—
	5,648,872	2,511,299
LIABILITIES		
Accounts payable and accrued liabilities	2,233	531
NET ASSETS	5,646,639	2,510,768
NET ASSETS REPRESENTED BY:		
Public Service Pension Plan Account	3,975,216	1,789,504
Canadian Forces Pension Plan Account	1,236,048	532,446
Royal Canadian Mounted Police Pension Plan Account	435,375	188,818
	5,646,639	2,510,768

On behalf of the Board of Directors:



Paul Cantor
Director and Chair of the Audit and Conflicts Committee

Statement of Changes in Net Assets

For the year ended March 31

	2002 (\$000)	2001 (\$000)
NET ASSETS, BEGINNING OF YEAR	2,510,768	—
CHANGES IN NET ASSETS		
Fund transfers (Note 3)	2,996,362	2,741,302
Net income/(loss) from operations	139,509	(230,534)
NET ASSETS, END OF YEAR	5,646,639	2,510,768

PUBLIC SECTOR PENSION INVESTMENT BOARD

Statement of Net Income/(Loss) from Operations

For the year ended March 31

	2002 (\$000)	2001 (\$000)
INVESTMENT INCOME		
Interest and dividends	125,190	3,327
Net realized gains/(losses) (Note 2c)	(412,404)	(105)
Net unrealized gains/(losses)	434,009	(230,151)
	146,795	(226,929)
INVESTMENT AND ADMINISTRATIVE EXPENSES (Note 5)		
Salaries and benefits	2,756	796
Operating expenses	2,288	1,073
External investment management fees	751	197
Professional and consulting fees	1,491	1,539
	7,286	3,605
NET INCOME/(LOSS) FROM OPERATIONS (Note 6)	139,509	(230,534)

Statement of Investment Portfolio

As at March 31

Investments (Note 2)	2002*			2001**		
	Cost	% of Portfolio Fair Value	(At Fair Value)	Cost	% of Portfolio Fair Value	(At Fair Value)
	(\$000)	(\$000)		(\$000)	(\$000)	
CANADIAN EQUITIES						
PSP Canadian Equities Fund						
Active management	221,627	224,310	4.0	—	—	—
Indexed management	1,601,915	1,754,314	31.2	1,042,911	848,229	33.8
	1,823,542	1,978,624	35.2	1,042,911	848,229	33.8
FOREIGN EQUITIES						
PSP Foreign Equities Fund						
Active management	354,428	365,527	6.5	—	—	—
Indexed management	1,264,202	1,325,799	23.5	754,349	675,738	26.9
	1,618,630	1,691,326	30.0	754,349	675,738	26.9
FIXED INCOME						
PSP Fixed Income Fund						
Active management	1,174,030	1,175,227	20.9	—	—	—
Indexed management	636,317	611,200	10.9	923,040	966,182	38.5
	1,810,347	1,786,427	31.8	923,040	966,182	38.5
CASH EQUIVALENTS						
PSP Cash Equivalents Fund	167,598	167,598	3.0	20,952	20,952	0.8
	5,420,117 ***	5,623,975 ***	100.0%	2,741,252	2,511,101	100.0%

* As of October 2nd, 2001 the pooled fund investments held by the three Pension Plan Accounts were transferred into pooled accounts held by PSP Investments (PSP Funds).

** Investments were exclusively in pooled funds managed by State Street Global Advisors (SSgA).

*** Include investment receivables of \$81,206 thousand (2001 - Nil) and investment payables of \$84,057 thousand (2001 - Nil) pertaining to pending trades for a net payable of \$2,851 thousand.

PUBLIC SECTOR PENSION INVESTMENT BOARD

Notes to the Financial Statements*For the year ended March 31, 2002***ORGANIZATION**

The Public Sector Pension Investment Board ("PSP Investments") was formed pursuant to the *Public Sector Pension Investment Board Act* (the "Act") with a mandate to invest in financial markets the contributions to the Public Service, Canadian Forces and Royal Canadian Mounted Police pension plans. Prior to the implementation of the provisions of the Act, the balances of the plans were credited with a rate of interest based on long-term Government of Canada bonds.

The Public Service, Canadian Forces and Royal Canadian Mounted Police Pension Funds were established by amendments to the *Public Service Superannuation Act*, the *Canadian Forces Superannuation Act* and the *Royal Canadian Mounted Police Superannuation Act* ("the *Superannuation Acts*"), to receive contributions and make benefit payments in respect of member service after April 1, 2000. The excess of contributions over benefits is transferred, by each Pension Fund, to their respective PSP Investments-Plan Account for investment.

PSP Investments is responsible for managing amounts that are transferred to it in the best interests of the beneficiaries and contributors under the *Superannuation Acts*. The amounts are to be invested with a view to achieving a maximum rate of return, without undue risk of loss, having regard to the funding, policies and requirements of the pension plans established under the *Superannuation Acts*.

PSP Investments commenced operations April 1, 2000, and has a fiscal year end of March 31.

For the first time a financial statement has been produced for PSP Investments which includes the interest of the three Plan Accounts, in addition to financial statements of each Plan Account.

1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES***Basis of presentation***

These financial statements present the financial position and operations of PSP Investments as they pertain to the investment of the excess funds transferred to it from the Public Service, Canadian Forces and Royal Canadian Mounted Police Pension Funds. Accordingly, they do not reflect all of the assets, or the details of the pension contributions, payments and liabilities of all three Pension Funds. The statements have been prepared in accordance with Canadian generally accepted accounting principles and the requirements of the Act.

Plan Accounts

PSP Investments maintains records of each Pension Funds' net contributions, as well as, the allocation of its investments and the results of its operations to each of the Plan Accounts.

Separate financial statements for each Plan Account have been published.

Valuation of investments

Investments are recorded as of the trade date and are stated at fair value. Fair value is the amount of the consideration that would be agreed upon in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act.

Market prices for securities and unit values for pooled funds are used to represent the fair value of investments. Unit values reflect the quoted market prices of the underlying securities.

Income recognition

Investment income is recorded on the accrual basis and represents realized gains and losses on the disposal of investments, unrealized gains and losses on investments held at the end of the year, interest income and dividends. These income items include the related distributions from pooled funds.

Translation of foreign currencies

Transactions in foreign currencies are recorded at the rates of exchange on the transaction date. Investments denominated in foreign currencies and held at the end of the year are translated at exchange rates in effect at the year end date. The resulting realized and unrealized gains and losses on foreign exchange are included in investment income.

Fund transfers

Amounts received from each Pension Fund are recorded on a cash basis in their respective Plan Account.

PUBLIC SECTOR PENSION INVESTMENT BOARD

Notes to the Financial Statements*For the year ended March 31, 2002***1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)***Income Taxes*

PSP Investments is exempt from Part I tax under paragraph 149 (1) (d) of the *Income Tax Act* (Canada).

Use of estimates

In preparing these financial statements, management must make certain estimates and assumptions which can affect the reported values of assets and liabilities, related income and expenses and note disclosures. Actual results may differ from estimates.

2 INVESTMENTS

The Statement of Investment Portfolio provides details of investments held as at March 31, 2002.

(a) Investment Policy

PSP Investments has established a Statement of Investment Policies, Standards and Procedures, (the "Investment Policy") which sets out the manner in which the assets shall be invested for the three Plan Accounts. Asset mix policy and benchmarks at March 31, 2002 were as follows:

Asset Class	Policy Mix	Benchmark
Canadian Equities	35.0%	TSE 300
Foreign Equities	30.0%	S&P 500, MSCI EAFE
Fixed Income	32.0%	SC Bond Universe
Cash Equivalents	3.0%	SC 91-day T-bill

Prior to October 25, 2001, the Regulations of the *Act* stipulated that the investments of PSP Investments in Canadian equities had to substantially replicate the composition of one or more widely recognized broad market indices. The Toronto Stock Exchange 300 Composite Index (TSE 300) had been selected as an appropriate market index for Canadian equities. On October 25, 2001, an amendment to the Regulations of the *Act* enabled PSP Investments to invest without replicating a widely recognized Canadian equity index.

(b) Foreign currency exposure

PSP Investments is exposed to currency risk through holdings of securities and units in pooled funds of non-Canadian equities where investment values will fluctuate due to changes in foreign exchange rates. The underlying foreign currency exposures by currency as at March 31 were as follows:

Currency	2002		2001	
	Fair Value (S000)	% of Total	Fair Value (S000)	% of Total
US dollars	971,426	57.4	337,383	49.9
Euro	270,284	16.0	137,509	20.4
British pound	178,971	10.6	73,158	10.8
Yen	147,377	8.7	81,046	12.0
Others	123,268	7.3	46,642	6.9
	1,691,326	100.0%	675,738	100.0%

In accordance with the Investment Policy, foreign currency exposures are not hedged.

(c) Transfer of SSgA Pooled Fund units to PSP Funds

On October 2nd 2001, PSP Investments created the PSP Funds and the units in SSgA pooled funds previously held in the name of the three Plan Accounts, were transferred to the PSP Funds. This deemed disposition caused previously unrealized losses to become realized in the Statement of Net Income/(Loss) from Operations for the three Plan Accounts. This has no impact on the Plan Accounts, except for bringing the Investments cost values closer to their fair values.

PUBLIC SECTOR PENSION INVESTMENT BOARD

Notes to the Financial Statements

For the year ended March 31, 2002

2 INVESTMENTS (continued)

(d) PSP Canadian Equities Fund - 10 largest holdings

	Company Name	Market Value (\$,000)	% of PSP Canadian Equities Fund
1	Royal Bank of Canada	97,395	4.9
2	Toronto-Dominion Bank	77,609	3.9
3	Scotia Bank	76,921	3.9
4	BCE Inc.	61,004	3.1
5	Nortel Networks Corporation	60,525	3.1
6	Manulife Financial Corporation	59,729	3.0
7	Alcan Inc.	55,901	2.8
8	Canadian Imperial Bank of Commerce	55,147	2.8
9	Bank of Montreal	53,421	2.7
10	Barrick Gold Corporation	47,035	2.4
Total 10 largest Holdings		644,687	32.6

Some of the holdings shown above are held through Indexed Pooled Fund participation.

(e) PSP Foreign Equities Fund - 10 largest holdings

	Company Name	Market Value (\$,000)	% of PSP Foreign Equities Fund
1	General Electric Company	36,966	2.2
2	Microsoft Corporation	31,617	1.9
3	Exxon Mobil Corporation	30,647	1.8
4	Pfizer Inc.	27,819	1.6
5	Citigroup Inc.	26,831	1.6
6	Wal Mart Stores Inc.	25,687	1.5
7	Intel Corporation	22,780	1.3
8	BP p.l.c.	21,591	1.3
9	American International Group Inc	20,472	1.2
10	Johnson & Johnson	20,406	1.2
Total 10 largest Holdings		264,816	15.6

Some of the holdings shown above are held through Indexed Pooled Fund participation.

(f) PSP Fixed Income Fund

The PSP Fixed Income Fund holds securities invested in Canada as follows:

	Market Value (\$,000)	% of PSP Fixed Income Fund
Government of Canada	707,031	39.6
Provincial	474,606	26.6
Municipal	10,109	0.6
Corporate	592,401	33.1
Cash	2,280	0.1
Total	1,786,427	100.0

Some of the holdings shown above are held through Indexed Pooled Fund participation.

PUBLIC SECTOR PENSION INVESTMENT BOARD

Notes to the Financial Statements*For the year ended March 31, 2002***3 FUND TRANSFERS**

During the year, PSP Investments received \$2,996.3 million (2001 \$2,741.3 million) of transfers from the three Pension Funds. The transfers result from net current employer and employee contributions to their respective Pension Plan.

The breakdown of the fund transfers is as follows:

	2002	2001
	(\$000,000)	(\$000,000)
Public Service Pension Fund	2,086.3	1,953.7
Canadian Forces Pension Fund	674.0	581.1
Royal Canadian Mounted Police Pension Fund	236.0	206.5
Total Fund Transfers	2,996.3	2,741.3

4 INVESTMENT PERFORMANCE

Portfolio and benchmark returns for the year ended March 31 were as follows:

	2002		2001		
	Portfolio Returns	Benchmark Returns	Portfolio Returns	Benchmark Returns	
Canadian Equities	4.7%	4.9%	(12.0)%	(12.2)%	TSE 300
Foreign Equities	(3.3)%	(2.6)%	(13.2)%	(13.0)%	S&P 500 & MSCI EAFE
Fixed Income	5.3%	5.1%	8.3%	8.3%	SC Bond Universe
Cash Equivalents	4.0%	3.7%	—	—	SC 91-day T-Bill
Total return	2.7%	2.8%	(4.1)%	(4.0)%	

The Total Benchmark return aggregates the asset class benchmark returns according to the weights specified in the Investment Policy, as disclosed in Note 2 (a).

Returns have been calculated in accordance with the mandatory requirements set forth by the Association for Investment Management and Research (AIMR). Returns are presented gross of investment and administrative expenses.

5 INVESTMENT AND ADMINISTRATIVE EXPENSES*(a) Operating expenses*

Operating expenses consisted of the following:

	2002	2001
	(\$,000)	(\$,000)
Office supplies and equipment	996	271
Remuneration earned by Directors	339	279
Occupancy costs	336	90
Communication expenses	248	276
Travel and accommodation for Directors' meetings	160	82
Custody and Fund Administration	116	35
Other operating expenses	93	40
Total	2,288	1,073

Total remuneration earned by Directors includes an annual retainer for each Director of \$12,000, an additional annual retainer of \$3,000 for each committee chair, and Board and committee meeting fees of \$900 per meeting. Separate fees are not paid for investment committee meetings when they are held as a committee of the whole during Board meetings.

PUBLIC SECTOR PENSION INVESTMENT BOARD

Notes to the Financial Statements

For the year ended March 31, 2002

5 INVESTMENT AND ADMINISTRATIVE EXPENSES (continued)

Directors of PSP Investments come from various regions of the country and accordingly they incur travel and accommodation expenses in attending meetings of the Board and committees.

(b) Salaries and benefits

Included in salaries and benefits is compensation earned by executive officers. The total compensation earned during the fiscal year by the executive officers was as follows:

Employee/Position	Year	Base Salary	Annual Bonus ⁴	Long Term Incentive Plan ⁴	Benefits ⁵
Adel Sarwat	2002	\$275,000	\$143,000	\$213,000	\$50,500
President and Chief Executive Officer	2001	138,900 ¹	70,000	—	—
Carl Haller	2002	81,000 ²	—	—	—
Executive Vice President	2001	256,000 ²	—	—	—
Danielle G. Morin	2002	181,400 ³	82,600	53,500	26,800
Chief Financial Officer	2001	—	—	—	—

¹ The President and Chief Executive Officer commenced employment on September 11, 2000, and in addition to the above, was awarded a signing bonus of \$210,000 in fiscal year 2001.

² The Executive Vice President commenced employment on February 28, 2000 with the mandate to coordinate the start-up phase. He left PSP Investments on August 31, 2001, and periodically provided consulting services for \$12,000 until December 31, 2001.

³ The Chief Financial Officer commenced employment on April 6, 2001, and in addition to the above, was awarded a signing bonus of \$30,000.

⁴ Bonus awards include short-term and long-term components and are based on the achievement of agreed objectives. PSP Investments has established a new program for the long-term bonus which will be in place starting fiscal year 2003. Consequently, long term bonus for the last 2 years has been paid to close the previous program.

⁵ Benefits include other miscellaneous non-cash remuneration. Included is the premium for long-term disability coverage which is now integrated in PSP Investments Group Insurance coverage. In addition to the above, the executive officers are covered by a contributory defined benefit pension plan which provides them with a pension benefit of 2% of the best 3 year average earnings for each year of service.

(c) Professional and consulting fees

Professional and consulting fees consisted of the following:

	2002	2001
	(\$,000)	(\$,000)
Consulting fees	758	859
Legal	381	462
Professional accounting and audit fees	352	218
Total	1,491	1,539

Consulting fees represent amounts paid for professional advice in connection with the development of business strategy and human resource policies, recruiting, and other professional advice and services.

PUBLIC SECTOR PENSION INVESTMENT BOARD

Notes to the Financial Statements*For the year ended March 31, 2002***6 ALLOCATION OF NET INCOME/LOSS FROM OPERATIONS**

The allocation of the net income/loss from operations of PSP Investments to each Plan Account is as follows:

(a) Investment Income

The investment income has been allocated according to the number of units of PSP Funds held by each Plan Account.

(b) Investment and Administrative Expenses

The *Act* requires that the costs of operation of PSP Investments be charged to the three plans for which it provides investment services. Under section 4(3) of the *Act*, the President of the Treasury Board shall determine to which Plan Account these costs will be charged in consultation with the Minister of National Defence and the Solicitor General of Canada. An allocation policy has been developed which allocates the direct costs of investment activities, such as investment management and custodial fees, to each Plan Account, and allocates administrative expenses, such as salaries and benefits, advisory services, directors' fees and other administration costs, based upon the asset value of each Plan Account.

Administrative costs have been allocated on a quarterly basis according to the policy, resulting in an allocation as follows:

	2002	2001
Public Service Pension Plan Account	70.6%	71.9%
Canadian Forces Pension Plan Account	21.7%	21.0%
Royal Canadian Mounted Police Pension Plan Account	7.7%	7.1%

The costs of administrative expenses are paid by PSP Investments by way of an advance from the Public Service Pension Plan Account, which is reimbursed by the other Plan Accounts on a quarterly basis.

CORPORATE DIRECTORY

Board of Directors and Investment Committee

WILLIAM R.C. BLUNDELL

Chairperson of the Board

Former chairman and CEO, GE Canada
Toronto, Ontario

BOB BALDWIN

National Director, Social and Economic Policy
 Canadian Labour Congress
Ottawa, Ontario

BARBARA BENDER, CA

Vice-President
 Spartan Systems Limited
Saint John, New Brunswick

JEAN-LOUIS BOURBEAU, FCIA

Former chair and former CEO
 William M. Mercer Limited
Montreal, Quebec

RICHARD BRADSHAW

Former President and CEO
 Phillips, Hager & North Investment
 Management Ltd.
Vancouver, British Columbia

PAUL CANTOR, LL.B., FICB

Managing Partner, Canada
 Russell, Reynolds Associates
Toronto, Ontario

PAUL G. HAGGIS

Executive Vice-President
 Business Development
 & Chief Credit Officer
 Manulife Financial
Toronto, Ontario

DONNA SOBLE KAUFMAN, LL.M.

Corporate Director
Toronto, Ontario

LYNN LOEWEN, CA

Vice-President Finance & Administration
 Air Canada Regional Inc.
Halifax, Nova Scotia

KEITH G. MARTELL, CA

Chairman of the Board
 First Nations Bank of Canada
Saskatoon, Saskatchewan

CARL H. OTTO, CFA

President and CEO
 IFPT Management Inc.
Montreal, Quebec

SUSAN SHERK

Senior Human Environment Consultant
 AMEC Plc
St. John's, Newfoundland

Audit and Conflicts Committee

PAUL CANTOR, Chair
 BARBARA BENDER
 JEAN-LOUIS BOURBEAU
 KEITH G. MARTELL

Governance Committee

DONNA SOBLE KAUFMAN, Chair
 LYNN LOEWEN
 CARL H. OTTO

Human Resources and Compensation Committee

PAUL G. HAGGIS, Chair
 BOB BALDWIN
 RICHARD BRADSHAW
 SUSAN SHERK

CORPORATE DIRECTORY

Management**ADEL SARWAT, CFA**

President and Chief Executive Officer
Montreal, Quebec

DANIELLE G. MORIN, FCIA

Chief Financial Officer
Montreal, Quebec

JÉRÔME BICHUT, CFA

Senior Portfolio Manager, European Equities
Montreal, Quebec

SUSAN DA SIE, CFA

Senior Portfolio Manager, US Equities
Montreal, Quebec

FRÉDÉRIC LECOQ, CFA

Senior Portfolio Manager, Canadian Equities
Montreal, Quebec

LYNE CRÉPIN

Director, Investment Administration
Montreal, Quebec

ASIF HAQUE, CFA

Director, Performance Measurement
Montreal, Quebec

KEN MONDS

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DAN THANH NGUYEN

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