

**VBA WINS US\$100 MILLION U.S. SMALL-CAP MANDATE WITH CANADA POST CORPORATION**
**U.S. SMALL-CAP DIVISION WINS MANDATE**

It is with great pride that VBA announces the most significant mandate win in its 19-year history. The Canada Post investment manager search for a U.S. Small-Cap mandate was very competitive, with VBA being the only Canadian-based U.S. Small-Cap Equity manager invited to the finals. The facts that we have maintained outstanding investment performance results and that we are a specialized small-cap investment manager were certainly major factors that led to this appointment.

**U.S. SMALL-CAP INVESTMENT PERFORMANCE**

It is again my pleasure to report on the continuing outstanding investment performance results of the U.S. Small-Cap Equity Management Division.

For the year-ended December 2009, VBA's U.S. Small-Cap Pension Fund Composite Ranks:

- 17<sup>th</sup> Percentile on the Nine-Year Basis,
- 16<sup>th</sup> Percentile on the Five-Year Basis,
- 4<sup>th</sup> Percentile on the Three-Year Basis, and
- 48<sup>th</sup> Percentile on the One-Year Basis.

The following table shows the investment performance results of the Van Berkomp and Associates Inc.'s ("VBA") U.S. Pension Fund Composite for the period ended December 31, 2009 compared with the Russell 2000 Small-Cap Index as well as the S&P 500 Index.

**VBA U.S. Pension Fund Composite Results**  
**Total Time Weighted Rates of Return**  
**Annualized for Periods Greater than One Year**  
**(To December 31, 2009)**  
**(in US dollars)**

	<b>3 Mos.</b>	<b>YTD</b>	<b>1 Yr.</b>	<b>2 Yrs.</b>	<b>4 Yrs.</b>	<b>5 Yrs.</b>	<b>7 Yrs.</b>	<b>8 Yrs.</b>	<b>9 Yrs.</b>	<b>Since</b>
	<b>(%)</b>	<b>(%)</b>	<b>(%)</b>	<b>(%)</b>	<b>(%)</b>	<b>(%)</b>	<b>(%)</b>	<b>(%)</b>	<b>(%)</b>	<b>06/30/00</b>
	<b>(%)</b>	<b>(%)</b>	<b>(%)</b>	<b>(%)</b>	<b>(%)</b>	<b>(%)</b>	<b>(%)</b>	<b>(%)</b>	<b>(%)</b>	<b>(%)</b>
VBA U.S. Pension Fund	4.25	35.30	35.30	-1.20	5.93	5.72	10.61	8.28	9.90	10.84
Russell 2000 Index	3.87	27.17	27.17	-8.24	-0.48	0.51	8.65	4.49	4.27	3.38
S&P 500 Index	6.04	26.46	26.46	-10.74	-0.67	0.42	5.52	1.60	0.00	-0.95
<b>Value Added</b> <b>(VBA U.S. Composite minus</b> <b>Russell 2000)</b>	<b>0.38</b>	<b>8.13</b>	<b>8.13</b>	<b>7.04</b>	<b>6.41</b>	<b>5.21</b>	<b>1.96</b>	<b>3.79</b>	<b>5.63</b>	<b>7.46</b>

NOTE: Van Berkomp and Associates Inc. [an entity registered with the Quebec, Nova Scotia, Ontario, Alberta, and British Columbia Securities Commissions as Portfolio Manager and with the Securities and Exchange Commission (United States) as Investment Advisor] has prepared and presented the report in compliance with the Global Investment Performance Standards ("GIPS") of the CFA Institute. The CFA Institute has not been involved with the preparation or review of this report. As at December 31, 2009, the VBA U.S. Pension Fund Composite ("VBA U.S. Pension Fund") totalled US\$301.77 million in small-cap assets, which represented 100% of the firm's U.S. assets under management and 34.0% of the firm's total assets under management. The VBA U.S. Pension Fund Composite includes eight major pension fund accounts. A complete list of the firm's composites and a description of each are available.

**COMPARATIVE INVESTMENT PERFORMANCE VERSUS THE RUSSELL INVESTMENT GROUP UNIVERSE OF U.S. SMALL-CAP MANAGERS**

I have enclosed the comparative investment performance results of the VBA U.S. Pension Fund Composite in the Russell Investment Group Universe of U.S. small-cap equity managers. Also enclosed is the risk/reward chart showing the VBA U.S. Pension Fund Composite versus the Russell Investment Group Universe of 177 U.S. Small-Cap portfolios as evaluated by BNY Mellon Asset Servicing.


**REVIEW AND OUTLOOK OF U.S. SMALL-CAP STOCKS**

Enclosed you will find the quarterly review and outlook for U.S. Small-Cap stocks for the fourth quarter 2009.

If you would like to learn more about VBA and our U.S. Small-Cap Equity Management Division, please visit us on our web site at [www.vbassociates.com](http://www.vbassociates.com) or call me at 1 888 VBA-5759, extension 223 or at (514) 985-5759, extension 223, or Mathieu Sirois at extension 237 or by e-mail at [contact@vbassociates.com](mailto:contact@vbassociates.com).

In the case of U.S. domiciled consultants and sponsors, please contact Richard A. Murphy or H. Alex Winters of North Bridge Capital, who represent VBA in the U.S. as our third party marketing organization. You may contact them by telephone at (617) 573-0011 or by email at [rich@northbridgecap.com](mailto:rich@northbridgecap.com) or [alex@northbridgecap.com](mailto:alex@northbridgecap.com)

Sincerely yours,

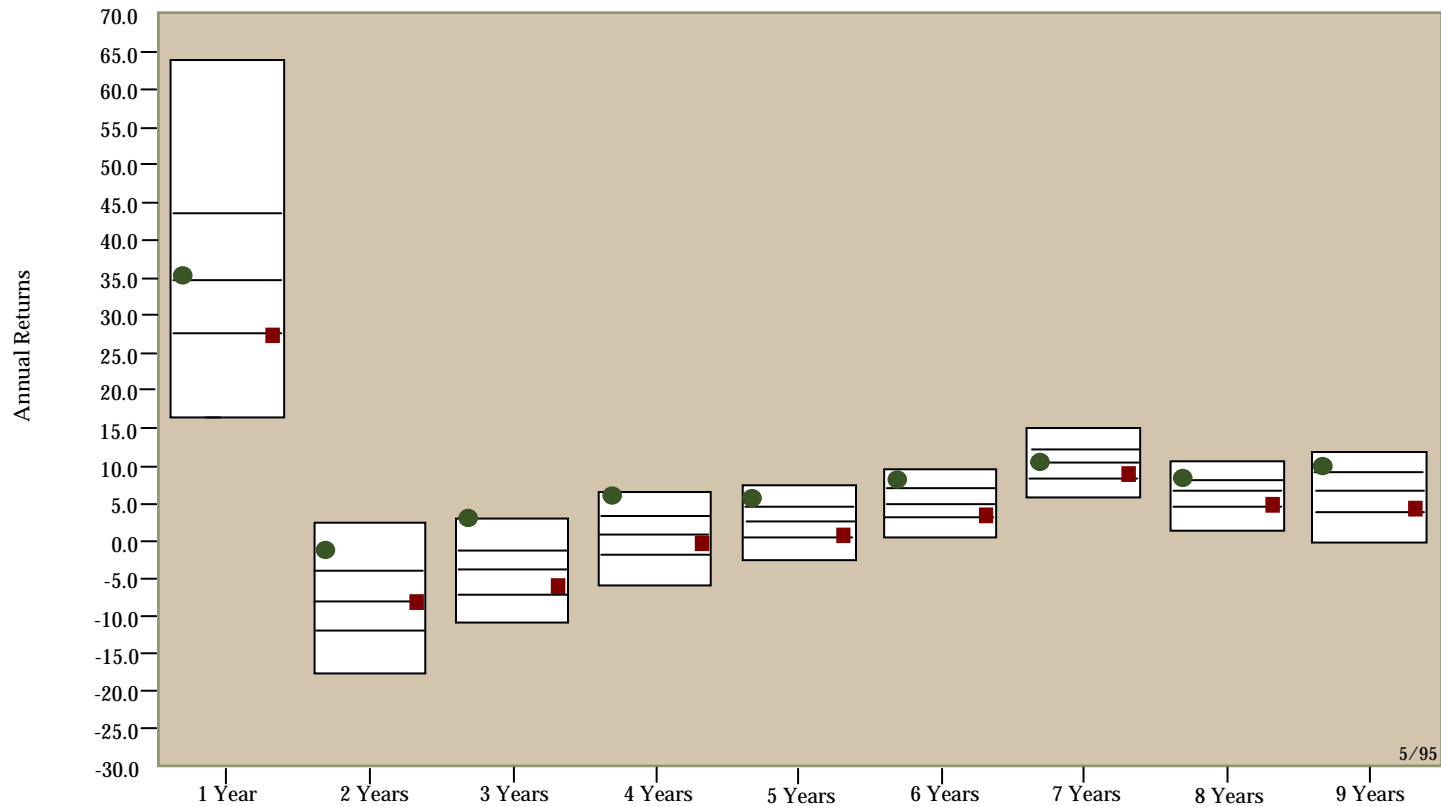


*J. Sebastian van Berkomp*  
President and Chief Executive Officer

# PERFORMANCE OF THE VBA U.S. PENSION FUND COMPOSITE VERSUS RUSSELL INVESTMENT GROUP



## Small-Cap Equity Universe Rates of Return for Periods Ending December 31, 2009



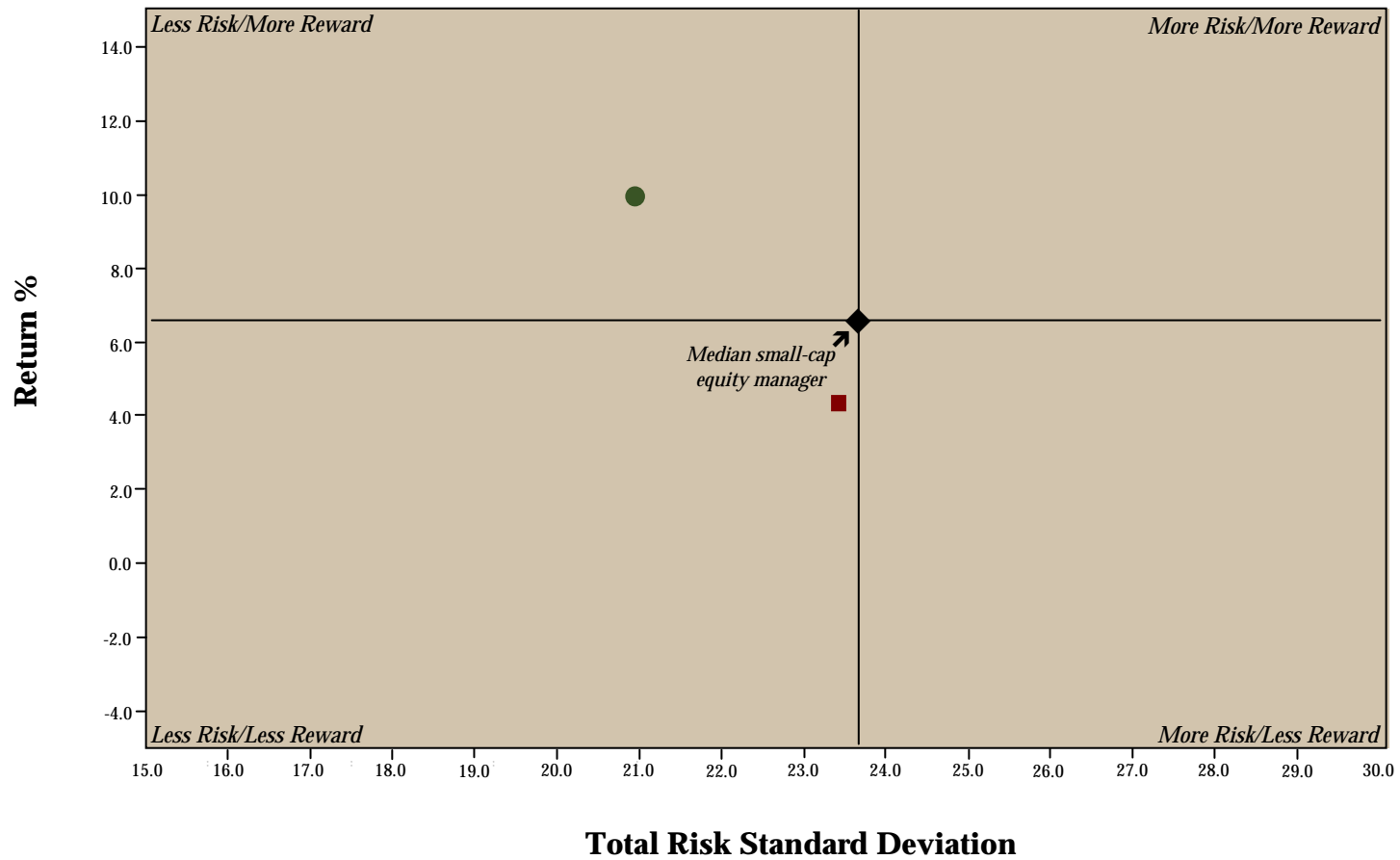
	Value	%Tile	Value	%Tile	Value	%Tile	Value	%Tile	Value	%Tile	Value	%Tile	Value	%Tile	Value	%Tile	Value	%Tile
5 <sup>th</sup> Percentile	63.9		2.3		2.8		6.3		7.2		9.4		15.1		10.6		11.6	
25 <sup>th</sup> Percentile	43.7		-3.9		-1.2		3.3		4.6		7.0		12.1		8.2		9.0	
Median Percentile	34.7		-8.0		-3.8		0.8		2.5		5.0		10.3		6.5		6.6	
75 <sup>th</sup> Percentile	27.3		-11.9		-6.9		-1.7		0.3		3.1		8.3		4.6		3.9	
95 <sup>th</sup> Percentile	16.6		-17.3		-11.0		-5.8		-2.6		0.4		6.0		1.5		-0.3	
# of Portfolios	383		367		310		310		278		250		227		192		177	
● VBA U.S. Pension Fund Comp	35.3	48	-1.2	14	3.1	4	5.9	7	5.7	16	8.2	13	10.6	47	8.3	24	9.9	17
■ Russell 2000 Index	27.2	76	-8.2	53	-6.1	70	-0.5	65	0.5	72	3.3	73	8.7	72	4.5	78	4.3	73

Universe Source: Russell Investment Group

# PERFORMANCE OF THE VBA U.S. SMALL-CAP PENSION FUND COMPOSITE VERSUS THE BNY MELLON UNIVERSE



## Small-Cap Equity Universe Risk / Reward 9.0 Years Ending December 31, 2009



- VBA
- Russell 2000

Universe Source: Russell Investment Group



## REVIEW AND OUTLOOK OF U.S. SMALL-CAP STOCKS

In this usually joyful Holiday Season for everybody, including investors, we are not surprised to witness the usual end-of-the-year rally unfolding largely as hoped for in such a strong year for the market. In fact, we are inclined to think that we have been in a Santa Claus rally for almost ten months now, as the dramatic stock market recovery experienced since the market lows of last March 2009 has been so seamless, steady and has gone largely uninterrupted. It is indeed fascinating to witness such high levels of optimism after the hardships that we all went through in last year's Holiday Season.

The final quarter of this year was merely a continuation of the same cheerful trends that have inspired this highly unusual year, although at a moderating pace. In fact, since March 2009, investors have been so accustomed to month-after-month rapid rises in the key U.S. benchmarks that this quarter's market performance, even though still very good by historical standards, felt somewhat lackluster. The drivers of the continuation of this impressive run by the stock market were essentially the same: corporate profits widely and broadly outpacing expectations yet again, and continued signs of economic recovery in most corners of the economy. It did not really matter to investors that effective cost-cutting by virtually all the corporations once again was the major culprit behind the outperformance in corporate earnings in the face of still quite lackluster revenue growth and tame demand from end-users. Nor did market participants give much consideration to the fact that the strong reading for the third quarter U.S. gross domestic product ("GDP") had much to do with one-time or non-recurring stimulants that stemmed largely from the government's tireless and countless initiatives to prop the economy, such as its efforts directed at the ailing auto and housing sectors. Also, a little talked about aspect behind the strength in the third quarter GDP number was the steep decline in the personal savings rate, such drawdown driving additional consumer expenditures in the short term, but being a worrisome sign in itself and not very helpful to restore long-term consumer financial health and discipline.

Even though the Russell 2000 put an exclamation point in December to this monster junk rally, with a stunning 8% rise, dramatically outperforming the S&P 500 for the month, this steep reversal in relative performance was not enough to prevent large-cap stocks from out-performing small-caps in this final quarter of the year. After having lagged badly in this huge market recovery since March 9, large-caps played catch-up in this last period. We believe investors' newfound appetite for large company stocks had all to do with their appealing relative valuation after several months of significant underperformance in this bull market and with corporate earnings that have held up much better throughout 2009 for large-caps versus their smaller counterparts. Also, with mixed signals on the strength of this economic recovery and some emerging concerns over the future direction of the markets, it felt as if investors found more comfort in redirecting some money towards safer and cheaper blue chip stocks.

For 2009 as a whole, small-cap stocks still managed to narrowly beat large-caps in what has been an entertaining, roller-coaster race between the two. One should not be surprised of such outperformance, as 2009 was clearly a successful and inspiring year for risk-taking. After having been buried alive in 2008, the "risk trade" came roaring back from the grave since last spring. As a general rule, the more risk you took as an investor in 2009, the more money you made. Hence, by far the most successful investments were made in low-quality, very small market capitalization U.S. stocks, in high-yield debt, in emerging markets, and in most commodities. In 2009, we witnessed a true, global junk rally across geographies and asset classes, very much reminiscent of what we last went through in 2003. In this past year, maximizing risk was the way to maximize reward for most investors.

The major difference for us is that unlike 2003, we managed to outperform both the Russell 2000 and the S&P 500 by a wide margin, for the full year as well as since the market bottom of March 9. In fact, the year that just came to an end proved to be our best ever for absolute returns and one of our most successful against major U.S. indices, a very unusual accomplishment for us in this type of market environment. Hence, in what was the largest intra-year rally in over 75 years (since the Great Depression era), our portfolio was up an astonishing 92% since the market low of March 9, widely exceeding the 84% total return of the Russell 2000, and the 67% return recorded by the S&P 500 over



that same period. While this bull market was truly spectacular and beyond most pundits' wildest expectations, to put it in perspective, it still leaves all the major U.S. indices about 26-30% below their peak reached in 2007. Nevertheless, the breadth of this rally was staggering, with about 10% of the S&P 500 stocks and 18% of the Russell 2000 stocks doubling in value in 2009.

Within the U.S. small-cap category, as we have said repeatedly all year, it is the most cyclical, lower quality and smaller names that performed the best by a wide margin in this multi-month rally. In this environment, we are especially pleased to have added about 800 basis points of value over the Russell 2000 in this very unfriendly market for us. The broad drivers of our outperformance in 2009 have been discussed in previous quarterly comments: careful stock picking, a discounted portfolio valuation versus all the major U.S. benchmarks, a fine balance between defensive stocks and more economically-sensitive names, numerous high-quality names that were added to the portfolio around the bottom of the market and which have greatly contributed to our performance this year. Our two best stocks for the year were *Tempur-Pedic International Inc.* and *Sotheby's*, two high-quality companies and great leaders in their respective market that also happened to be among our hardest-hit stocks in the previous year. However, those two companies demonstrated that they were great well-run businesses; hence, there was no permanent value destruction suffered by our clients and their stocks simply overreacted to the downside in 2008. With a strong business model and improved industry prospects, and as high-beta, economically-sensitive and early cycle stocks, those names rebounded very strongly in 2009 to become among investors' favorite names to own. Also, as we said last quarter, our performance was disproportionately enhanced by the new names that were added to the portfolio late last year and earlier this year; for this reason, nine of our best twenty stocks in the portfolio in 2009 were such new holdings.

More specifically, our performance in this final quarter benefited from two discrete events that we would like to discuss in greater detail: a private equity transaction and healthcare reform in the U.S. On the one hand, our returns were strongly enhanced in the December quarter by the announcement that one of our top ten holdings, *IMS Health Incorporated* ("IMS Health"), a dominant provider of data, information and analytics to the pharmaceutical industry, after having entertained discussions with several private equity firms in previous weeks, was being acquired for a steep premium by two such financial players. Hence, the stock was up about 37% in this most recent quarter, largely as a result of the acquisition premium being paid on this name. Interestingly, at \$5.2 billion in total, this was the largest private equity deal in the U.S. stock market since May 2008. Therefore, we were fortunate to have been one of the very few beneficiaries in 2009 of such financial transactions that were so plentiful before the market meltdown but that literally went away during the last credit crisis. As we have written in the past, our portfolio holdings, as a result of our focus on high-quality businesses that have sustainable competitive advantages, generate strong free cash flows and high returns on capital, with a strong balance sheet and that are trading at a discount to their intrinsic value, tend to be great acquisition candidates for financial players. *IMS Health*, which was added to our portfolio late in 2008, during some of the worst moments of the bear market, had all of the great financial and business attributes, but was trading at a significant discount to its intrinsic value as a result of a difficult industry environment and the deep recession impacting many of its markets. As the private equity market slowly came back to life late this year, the value in *IMS Health's* stock was recognized by some financial players.

Also, while several of our consumer names led the way in this most recent quarter, we had significant contribution as well from many of our healthcare names in this final month of the year, largely as a result of the significant progress made in the proposals to reform the healthcare system in the U.S. Early in 2009, you might recall, as we discussed, that our performance was negatively impacted by early proposals to reform the healthcare system, as the market was surprised by a reform proposal out of President Obama's administration that came very early during his first mandate, considering that it already had its hands full with the severe recession and the financial crisis. As a result of such talks, healthcare stocks, including ours, sold off in February and lagged the rally thereafter, hurting our relative performance at a time when we needed such defensive names to hold better than a free-falling market. Nevertheless, we quickly felt that this broad sell-off might be creating a great buying opportunity in the sector, as virtually all the stocks in the space became very cheap, regardless of their actual exposure to healthcare reform. Hence, we spent the next several weeks investigating the



matter, discussing the situation with several healthcare company executives, Wall Street analysts and other industry contacts. Since we have been doing research on healthcare names for a long time and have owned stocks in the sector (primarily service providers) for many years, we have developed a unique knowledge of that industry over time and established many contacts.

While different proposals to reform the current healthcare system in the U.S. indeed created significant reimbursement uncertainty for service providers dependent on the federal government, it became clear at one point, because of several political factors at stake, that only two or three different proposals would survive the long and grueling legislative process. Hence, at one point, we were in a position to quantify the impact of these two or three major proposals that took the lead in the race to reform healthcare for each investment candidate or holding that we were looking at, depending on the sub-sector that it was in and on its actual exposure to government reimbursement. Therefore, we were able to determine a worst-case scenario for earnings and hence for the stock of each company that we owned then or could own that had exposure to this healthcare reform. From that thorough analysis, we quickly realized that a few high-quality companies in this sector, with sound business models, a very successful long-term track record, with great financial attributes, and that could play a key role in the lawmakers' desire to contain healthcare costs and reduce the number of uninsured people were greatly under-valued by the market, even assuming a worst-case scenario for reimbursement cuts.

Not surprisingly, many generalist investors decided to shy away from the healthcare sector as a result of this significant uncertainty created by reform proposals, combined with the general lack of appeal of this sector relative to economically-sensitive, early cycle stocks that quickly garnered significant momentum in the early part of the year. As a result of this sector rotation away from healthcare, the industry, with the exception of some pockets of strength, badly lagged the market for a good part of the year. As contrarian investors, our appetite for the space only kept growing as we learned more about healthcare reform and its expected financial impact on companies that we were able to bake into our financial models. We therefore added to our existing positions in the sector and hence maintained our "overweight" position in healthcare at a time when most generalist funds were underweight. As more clarity emerged late in the year as to the outcome of reform, its timing and its impact on reimbursement for each sub-sector, such stocks had a very strong finish to the year, and we benefited strongly from such rebound in December. While we fully expect additional volatility driven by continued refinements to current reform proposals (meaning short periods of under- or outperformance), it looks as if taking a contrarian view on this issue of healthcare reform and loading up on the stocks of a few market leaders that will play an essential role in the healthcare system of tomorrow has and will pay off handsomely in the future.

It also helped that we maintained a large exposure to one of the few healthcare sub-sectors that might actually benefit from healthcare reform: acute-care hospitals. Since one of the stated goals of this reform is to greatly reduce the number of uninsured Americans, which have represented a major financial burden for hospitals, many market observers believe that the reform as currently proposed will be beneficial to acute-care hospital providers. We have long held a position in the stock of *Universal Health Services, Inc.* (UHS), a large acute-care hospital operator in the U.S., which happened to be the largest position in our portfolio for most of the year. Such potential benefit from reform drew a strong rally in UHS's stock and in its peers in 2009, with the stock up over 60% on the year and being one of the largest contributors to our strong performance. Despite the strong share price performance of UHS, the stock still trades around its historical-low valuation multiples and at a discount to its intrinsic value, making this position still highly appealing. Hence, we are not paying for any benefit related to healthcare reform, effectively giving us a free option on any such favorable outcome that could be captured in coming years.

As we look ahead to 2010, we remain puzzled and somewhat troubled by the overall bullishness of investors and market observers. While official investor surveys point to general cautiousness and unease, virtually nobody is forecasting a double-dip recession or a big pullback in the stock market, with the vast majority expecting continued economic improvements and stock market gains, which forces us to conclude that the consensus is still decidedly bullish or, at the very least, quite complacent. Also, the 2010 published estimates for corporate profits still point to a very bullish earnings growth scenario. We are somewhat reluctant to be this cheerful about corporate earnings for



2010 for a few reasons. First, while cost and revenue comparisons should be fairly easy at least for the first half of the year, and there is good operating leverage built in for many companies that have aggressively taken costs out of their business in 2009, we are of the opinion that most corporations, being so lean already, only have limited additional ability to take more costs out without disrupting current operations. Hence, we believe that earnings growth at U.S. companies at some point in 2010 will become much more dependent on revenue growth, which at this point remains elusive in most sectors.

Also, we remain fascinated by the great disconnect between a very cheerful Wall Street and the much more sober mood on Main Street and in Corporate America. Specifically, the behavior of corporate CEOs is still definitely cautious, with a focus on tight inventory levels, low capital expenditures, constrained advertising budgets, hiring freezes or selective layoffs, and tight management of balance sheets, as companies are hoarding cash or paying down debt instead of spending loosely on acquisitions or share buybacks.

Despite the unquestionable signs of economic recovery as it relates notably to housing, IT spending, manufacturing, consumer confidence and spending, we also have genuine worries about the U.S. economy in 2010, with major question marks lingering around such soft spots as the housing sector, commercial real estate, some industrial markets and the credit markets in general, especially when inevitably, the government starts pulling out its significant financial support, and as interest rates start rising at some point. Also, despite a much stronger-than-expected job report in November, the labor market remains weak by any standard, and the Americans remain underemployed to a large degree. The U.S. consumers, although still alive, remain constrained in their ability to spend. Last but not least, the great deleveraging phenomenon by consumers and financial players currently in motion will continue to slow down the economy in many ways in 2010 and beyond.

Such factors lead us to believe, for what it is worth, that this economic recovery will remain below average. With such an unexciting macro outlook, the current valuation of the major U.S. stock indices, near their historical average multiples, looks just about full to us. That leaves the market very much dependent on strong earnings growth to register more gains, an outcome we are not fully ready to bet on. We believe such uncertain backdrop for the economy and the stock market is setting the stage for much more discrimination in the performance of stocks in the coming year. With the “easy money” on most stocks having been made in 2009, we do not think that the market breadth will be nearly as convincing in 2010. We would therefore hope that the relative and absolute performance of stocks will be much more dependent on the fundamentals of each company, an environment that would obviously play right into our core strength.

Despite three consecutive years of significant outperformance, we fully believe that our portfolio remains strongly positioned against all major U.S. indices. It still trades at a discount to such benchmarks while exhibiting what we think is its best-ever level of quality. Therefore, we think the future of our VBA U.S. Small-Cap product is very bright and promising.