

Management Discussion and Analysis

FOR THE YEAR ENDED MAY 31, 2009

MANAGEMENT DISCUSSION AND ANALYSIS FOR THE YEAR ENDED MAY 31, 2009

This Management Discussion and Analysis (“MD&A”) is intended to help the reader to assess, through the eyes of management the Fund’s results and financial condition and the material changes therein during the financial year ended May 31, 2009. The annual MD&A complements and supplements the financial statements and contains financial highlights, but does not contain the complete annual financial statements of the Fund. To facilitate understanding of events and uncertainties, this MD&A should be read together with our financial statements and the notes thereto. Certain prior year financial data have been restated to be comparable with those of the current year. These restatements result in particular from the application of the *Regulation Respecting Development Capital Investment Fund Continuous Disclosure*.

This MD&A contains forward-looking statements about the Fund’s activities, results, and strategies that should be interpreted with caution. Because, by their nature, forward-looking statements involve assumptions, uncertainties and risks, it is possible that a number of factors may cause forecasts not to materialize. For example, legislative or regulatory changes, economic and business conditions and the level of competition are just a few of the major factors that could influence, sometimes significantly, the accuracy of the forward-looking statements in this report. This MD&A is dated June 19, 2009.

You can get a copy of the annual financial statements at your request, and at no cost, by calling us at 514-383-3663 or toll free at 1-800-567-3663, by writing to us at 8717 rue Berri, Montréal, Québec H2M 2T9 or by visiting our website at www.fondsftq.com or SEDAR at www.sedar.com.

You can also obtain a copy of the interim documents in this manner.

FINANCIAL HIGHLIGHTS

The following tables show selected key financial information about the Fund and are intended to help you understand the Fund’s financial performance for the past 5 years. This information is derived from the Fund’s audited annual financial statements. The Fund’s results are discussed under *Results of operations* on page 3.

Ratios and supplemental data

YEARS ENDED MAY 31

(in millions of dollars, except otherwise specified)	2009	2008	2007	2006	2005
Revenues	239	261	249	231	213
Net earnings (net loss)	(919)	(89)	475	366	271
Net assets	6,375	7,285	7,239	6,607	5,955
Class A shares outstanding (in thousands)	291,733	290,050	284,628	277,466	264,845
Total operating expense ratio* (%)	1.70	1.36	1.34	1.40	1.43
Portfolio turnover rate**:					
- Development capital investments (%)	6.71	12.22	18.35	15.15	17.60
- Other investments (%)	179.65	118.80	113.45	83.22	89.07
Trading expense ratio*** (%)	0.02	0.03	0.03	0.04	0.04
Number of shareholders (number)	570,889	575,394	574,794	573,086	568,383
Issues of shares	655	611	571	614	706
Redemptions of shares	647	476	402	329	256
Fair value of development capital investments****	4,598	3,959	3,736	3,333	2,899

* The total operating expense ratio is obtained by dividing operating expenses of the Fund (before tax on capital) for the year, as shown on its statement of operations, by the average net assets of the Fund. Without this change in calculation method resulting from the application of the *Regulation Respecting Development Capital Investment Fund Continuous Disclosure*, the ratio would have been 1.64% for the financial year ended May 31, 2009.

** The portfolio turnover rate reflects the number of changes made to the composition of the portfolio. There is not necessarily a relationship between a high turnover rate and the portfolio’s performance.

*** The trading expense ratio represents transaction costs expressed as a percentage of average net assets of the Fund.

**** These investments include funds committed but not disbursed as well as guarantees and suretyships.

Change in net assets per share

YEARS ENDED MAY 31

(in dollars)	2009	2008	2007	2006	2005
Net assets per share, beginning of year*	25.05	25.36	23.74	22.41	21.37
Change in accounting policy	—	—	(0.04)	—	—
Increase (decrease) from operations**:	(3.16)	(0.31)	1.68	1.35	1.07
<i>Interest and dividends</i>	0.82	0.90	0.87	0.85	0.84
<i>Operating and trading expenses</i>	(0.37)	(0.34)	(0.33)	(0.33)	(0.32)
<i>Income tax and tax on capital</i>	(0.05)	0.00	(0.07)	(0.03)	(0.08)
<i>Realized gains (losses)</i>	(1.31)	0.35	0.61	0.04	0.59
<i>Unrealized gains (losses)</i>	(2.25)	(1.22)	0.60	0.82	0.04
Variance from issues and redemptions of shares	(0.11)	0.00	(0.02)	(0.02)	(0.03)
Net assets per share at May 31 of year shown*	21.78	25.05	25.36	23.74	22.41

* The amount of net assets per share is based on the actual number of shares outstanding at the relevant time.

** The increase (decrease) from operations is based on the weighted-average number of shares outstanding over the financial year.

ECONOMIC CONDITIONS

The year 2008 was marked by an unprecedented global crisis as the economy was facing the worst recession since the 1930s. Many exceptional events occurred during the year, including the bankruptcy of large financial institutions such as Lehman Brothers and Washington Mutual. Massive government intervention likely prevented such bankruptcies from multiplying.

The American economy has been in a recession since the fourth quarter of 2007. While indebtedness and excessive consumption fuelled the economy since the beginning of the 1980s, the current situation is the opposite. Savings rates are up while consumption is down. The annualized GDP growth rate fell from -0.2% in the fourth quarter of 2007 to -6.3% in the fourth quarter of 2008. Consumer confidence is at its lowest level in more than forty years and some 6 million jobs were lost since the beginning of 2008, resulting in an unemployment rate of 9.4%. The Federal Reserve lowered its discount rate to an extraordinarily low 0.25% to keep mortgage rates at very low levels. Inflationary pressure at the beginning of the year has now been replaced by deflation. These are the reasons why the 10-year Treasury bond rates dropped to 2% before increasing to 3.75%.

Europe and Japan were also affected by the international crisis, particularly through exports to the U.S. The economic slowdown in industrialized countries had a smaller effect on the Chinese economy thanks to internal demand. Another consequence of the global recession was a significant decrease in demand for commodities. A steep drop in raw material prices was seen equally in energy products, grains and metals. To mitigate risks of a depression, monetary authorities across the world quickly and sharply lowered their discount rates.

The Canadian economy entered into a recession in the fourth quarter of 2008, one year after the U.S. Annualized GDP growth fell from -3.7% in the fourth quarter of 2008 to -5.4% in the first quarter of 2009. Goods and services exports and domestic demand dropped significantly. The year 2008 saw a decrease in exports and a return to budget deficits both at the provincial and federal levels. No province is safe from the current recession. Ontario is one of the most affected provinces because of its automotive industry. The Québec economy did better in 2008 than the overall Canadian economy, with growth in Québec GDP of 1.0% compared to overall Canadian GDP growth of 0.5%. Unemployment remains slightly higher in Québec (8.7%) compared to Canada as a whole (8.4%).

The global economic slowdown and the steep drop in raw material prices led to the depreciation of the value of the loonie against the U.S. dollar. The Canadian dollar moved from parity in May 2008 to US\$0.77 in March 2009 to climb back up to US\$0.92 as at May 31, 2009. The number of Canadian jobs lost since the employment peak in October 2008 amount to 362,000. Like elsewhere in the world, the inflation rate dropped to the bottom of the Bank of Canada's intervention band. Consequently, it was not slow to lower its overnight rate to 0.25% in April 2009. Rates for 10-year government bonds dropped from 3.7% in May 2008 to 2.6% at the beginning of 2009 before increasing to 3.4% in May 2009.

During the Fund's financial year ended May 31, 2009, the variable return of the stock markets can be attributed to the volatility of financial markets, the credit crisis and the economic recession. In this context, the majority of stock markets across the world recorded very negative returns, including the Canadian market (S&P/TSX composite) at -29.5% and the American market (S&P 500) at -34.4% (-28.0% in Canadian dollars). Lower interest rates nonetheless drove the Canadian bond market to a 5.5% performance during the twelve-month period ended May 31, 2009 despite the significant widening of credit spreads, particularly for corporate issuers.

These economic conditions form the background for our 2008-2009 activities. They had dire effects on the Fund's performance for this financial year, as well as on our partner companies and shareholders. However, the rally in the financial and stock markets between March and May 2009 meant the Fund ended its financial year on a good note, recording a positive return in the second half.

MANAGEMENT DISCUSSION OF FINANCIAL PERFORMANCE

RESULTS OF OPERATIONS

Overall results

The significant instability that resulted from the global financial crisis had a major impact on the performance of financial institutions worldwide. The Fund did not escape this crisis unscathed.

Therefore, a net loss of \$919 million was recorded for the last financial year, compared to a net loss of \$89 million for the prior year. With this result, the Fund generated a negative return of 12.6%, sharply down from the previous year's negative return of 1.2% and below the forecasts that were made last year. These forecasts neither anticipated a worldwide financial crisis of such magnitude nor the numerous effects it had on our financial assets, especially those that are publicly traded. However, put into perspective, the return of the Fund compared favourably with that of major stock indices¹ and Canadian balanced funds², which incurred higher losses for the same period.

It is worth noting that the loss for the year was entirely incurred during the first half of the year, which coincides exactly with the period of heavy turmoil experienced by the stock markets. During the last six months of the year, a positive return of 3.2% was recorded, fuelled by the stock market recovery and the resulting performance of our listed securities.

Investments and Other Investments sectors both significantly influenced the results for the year. The assets managed by the Investments sector are essentially mission-driven development capital investments in public and private partner companies in the form of shares, units or loans. This sector earned a negative gross return of 12.0% for the 2008-2009 financial year, down from the negative return of 4.7% generated last year. Despite this return and given the level of investments made by the Fund during the year, in keeping with its mission, the assets in this sector increased and represented \$3.0 billion or 47% of the Fund's assets under management as at May 31, 2009 (compared to 41% in the prior year). The Other Investments sector manages the remaining assets not invested in partner companies, which consist of bonds, money market securities, sector-based shares, funds of hedge funds, a portfolio of high-revenue securities³ and international infrastructure funds. For the year ended May 31, 2009, this sector generated a negative gross return of 10.4%, down from the positive return of 3.0% earned for the prior year. The assets of this sector represented \$3.4 billion or 53% of the Fund's assets under management as at May 31, 2009 (compared to 59% a year ago). The ratio of operating expenses to average net assets was 1.7% for the year ended May 31, 2009, up from last year's ratio. This increase is mainly attributable to the significant decrease in the net assets of the Fund in 2008-2009.

Fund return

YEARS ENDED MAY 31

	2009			2008		
	Assets under management at end of year* M\$	Weight %	Return %	Assets under management at end of year* M\$	Weight %	Return %
Development capital investments	3,022	47.0	(12.0)	2,950	40.8	(4.7)
Other investments**	3,408	53.0	(10.4)	4,289	59.2	3.0
	6,430	100.0	(10.8)	7,239	100.0	0.2
Operating and trading expenses			(1.7)			(1.4)
Income tax and tax on capital			(0.1)			0.0
Fund return (full year)			(12.6)			(1.2)
Fund return (1st half of the year)			(15.3)			0.2
Fund return (2nd half of the year)			3.2			(1.4)

* Assets under management at end of year refer to the fair value, at the end of the financial year, of the assets managed by the Investments and Other Investments sectors and used to generate revenues presented in the statement of operations of the Fund.

** Other investments represent the remaining assets not invested in our partner companies. Managed by the Other Investments sector, this portfolio consists of bonds, money market securities, sector-based shares, funds of hedge funds, a portfolio of high-revenue securities and international infrastructure funds.

1. For the same period (June 1, 2008 to May 31, 2009), the S&P/TSX composite generated a return of -29.5%, the BMO Québec-based small cap index, of -34.5%, the S&P 500, of -34.4%, the NASDAQ, of -29.7%, and the Russell 2000, of -33.0%.
2. For the same period (June 1, 2008 to May 31, 2009), the average return of Canadian balanced mutual funds was -16.6% (source: global neutral balanced funds, as compiled by globefund.com).
3. The portfolio of high-revenue securities is comprised of preferred shares, high-dividend shares and income trust units.

Sector results

The performance of the Investments sector is influenced by various factors, including the behaviour of the financial markets, the economic and business conditions in which our partner companies operate, and the active management of our investments. The negative gross return of 12.0% of the Investments sector for the most recently ended year is largely explained by the following:

- The poor performance of the stock markets during the past year, especially for smaller-cap companies, which had a significant impact on the results of the portfolio of listed securities of our Investments sector. Despite a stock market rebound since March 2009, this portfolio generated a negative return of 34.3% for the year, a lower performance than the negative return of 18.2% achieved last year, when the stock markets were already very unstable. It should be noted that this negative return was realized despite good sector diversification of the portfolio, as the poor performance of the stock markets was systemic;
- A negative return of 6.5% on our private securities and specialized funds. This performance followed the positive return of 1.0% recorded in the previous year. This decrease is mainly attributable to the combined impact on our partner companies of the economic recession experienced in the United States and Canada, the persistent effects of the increase in credit cost, the volatility of the Canadian dollar compared to the U.S. dollar and foreign competition.

The evolution of interest rates and the performance of the stock markets are the determining factors in analyzing the performance of the Other Investments sector. Accordingly, the results achieved by this sector are influenced by the behaviour of the financial markets and the conditions affecting the economic environment in which the Fund operates. The gross negative return of 10.4% of the Other Investments sector for the year ended May 31, 2009 is largely explained by the following:

- The poor performance of the stock markets during the past year, which had a significant impact on the results of the sector-based shares⁴ and other securities portfolios⁵. These portfolios generated a negative return of 27.6%. This performance followed the negative return of 0.3% recorded by these portfolios last year, in a stock market already affected by the beginning of the financial crisis both in Canada and internationally, and positive returns approximating 20.0% each year achieved, in a much more favourable economic environment, in the three previous years. It is, thus, important to specify that, despite the disappointing results for the year, the sector-based strategy implemented in June 2004 has nevertheless enabled us to earn an average annual return of 6.5% over a five-year period;
- A positive return of 2.0% on our fixed-income securities portfolio for the last year compared to a positive return of 4.2% for the previous year. The performance of the bond portfolio was negatively affected by the decline in value of bonds (provinces and corporate) due to the widening of credit spreads. This was partially offset by the impact of lower interest rates on securities issued by the Government of Canada, implying an increase in the fair value of the bonds held which, combined with the interest income generated by the portfolio, allowed us to earn a positive overall return on this asset class.

Return by asset class

YEARS ENDED MAY 31

	2009			2008		
	Assets under management at end of year M\$	Weight %	Return %	Assets under management at end of year M\$	Weight %	Return %
Development capital investments						
Private securities and specialized funds	2,480	38.6	(6.5)	2,200	30.4	1.0
Listed securities	542	8.4	(34.3)	750	10.4	(18.2)
Other investments						
Fixed-income securities	1,927	30.0	2.0	2,690	37.2	4.2
Sector-based shares and other securities	1,481	23.0	(27.6)	1,599	22.0	(0.3)
	6,430	100.0	(10.8)	7,239	100.0	0.2

4. The sectors are materials, energy, consumer staples, utilities and telecommunications.

5. Other securities include funds of hedge funds, the portfolio of high-revenue securities (comprised of preferred shares, high-dividend shares and income trust units) and, since 2008-2009, international infrastructure funds.

Analysis of cash flows, balance sheet, and off-balance sheet items

Cash flows

Cash flows from operating activities of the Fund totalled \$170 million in 2008-2009, up from the \$108 million recorded in 2007-2008. This increase is mostly explained by the change in accounts receivable and payable.

Cash flows from financing activities of the Fund totalled a negative amount of \$27 million for the 2008-2009 financial year, compared to an aggregate positive amount of \$143 million for the previous year. Overall, the balance of shares issued less shares redeemed was positive for the year, but lower than historical levels, which explains the decrease in corresponding cash flows. The increase in shares redeemed, which totalled \$645 million for the year on a cash basis, compared to \$481 million for the prior year, contributed to this decrease. This increase in shares redeemed essentially stemmed from the anticipated decrease in the share price on January 5, 2009. On the other hand, shares issued totalled \$655 million for the year on a cash basis, an increase over the corresponding total share issues of \$611 million reached a year ago.

Cash flows from investing activities of the Fund totalled a negative amount of \$133 million for 2008-2009, compared to an aggregate negative amount of \$254 million for the previous year. It should be noted that any investment or other investment disbursed by the Fund is a cash outflow giving rise to a negative cash flow. Since the amount of disbursed development capital investments for the 2008-2009 financial year has greatly exceeded the amount of proceeds from the disposal of direct investments (disinvestments) for the same period, a portion of the other investments portfolio has been sold during the year. The proceeds from these sales, combined mainly with the positive cash flows from operating activities, allowed the Fund to generate the cash flows needed to support the volume of disbursed development capital investments in partner companies.

The Fund also has lines of credit available for its working capital requirements. As at May 31, 2009, these lines of credit were unused.

Balance sheet and off-balance sheet items

Balance sheet development capital investments increased from \$3.3 billion as at May 31, 2008 to \$3.4 billion as at May 31, 2009. This increase essentially resulted from net disbursed investments during the year (disbursed investments less disinvestments), partially offset by the decline in the overall fair value of our investments recorded over the year.

With the Fund's record direct investments in partner companies of \$848 million (in addition to the \$542 million the Fund agreed to invest in connection with the last budget of the Government of Québec) for the year, an increase over the previous investment record of \$730 million achieved last year, the Investments sector once again outperformed its historic milestones and the goals set at the beginning of the year. In addition, amounts committed but not yet disbursed increased from \$625 million as at May 31, 2008 to \$1,209 million as at May 31, 2009. This increase is essentially attributable to the commitments resulting from the last budget of the Government of Québec that are not yet disbursed and therefore not yet recorded on the balance sheet.

Balance sheet other investments decreased by some \$1.0 billion over the past year to settle at \$3.2 billion as at May 31, 2009. This decrease is attributable to the decline in value of the portfolio resulting from the economic and financial crisis and to the increase in net investments made during the year (on a disbursed basis).

As a result of the decline in interest rates that continued during the 2008-2009 financial year, the bond hedge did not generate the expected results and was gradually reduced from \$2.0 billion as at May 31, 2008 to \$75 million as at May 31, 2009. In addition, other hedging strategies implemented during the year, with the objective of improving the risk/return profile of the investments and other investments portfolios, in particular with respect to the sector-based share portfolio, were also significantly reduced during the year in response to the course of stock markets. Derivatives are also used to protect the other investments portfolio against, in particular, exchange rate fluctuations when its assets are denominated in foreign currencies. The *Overall Financial Assets Management Policy* allows the use of derivatives only for capital protection purposes.

MISSION OF THE FUND, OBJECTIVES AND STRATEGIES

Mission and objectives

The Fund is a union-based development capital investment fund that was born out of the Québec Federation of Labour. Created in 1983 under the *Act to Establish the Fonds de solidarité des travailleurs du Québec (F.T.Q.)*, the Fund endeavours to collect the savings of Quebecers who want to participate in creating and maintaining jobs, in order to improve the situation of workers and stimulate the Québec economy. The Fund also helps raise awareness and encourage workers to save for retirement as well as represents an aid for economic training to workers in the companies the Fund invests in.

The Fund's mission is strongly supported by both levels of government since subscriptions to shares of the Fund qualify for RRSPs and give rise to a 15% tax credit at both the Québec and federal tax levels, for a total of 30%⁶.

Strategies

To implement its mission and to reach its objectives, the Fund deployed various strategies, both from a global management perspective and by sector. The Fund therefore implemented an *Overall Financial Assets Management Policy* under which it manages its financial assets in an integrated and comprehensive manner to produce a reasonable return for its shareholders while mitigating the volatility of the return from half-year to half-year. Accordingly, the assets in the other investments portfolio are distributed in a way that is complementary to the portfolio of investments made in partner companies in keeping with the Fund's mission. This strategy allows the Fund to obtain, overall, the desired risk/return balance.

Following a modification of its authorized target asset allocation in April 2008, the Fund added international infrastructure funds to its balance sheet valued at \$46 million as at May 31, 2009. No modification to the target asset allocation was authorized during the 2008-2009 financial year. However, the Fund may modify its targets depending on the circumstances and events that occur in the next few years. The considerable volatility of financial and stock markets during the last financial year resulted in significantly modifying the actual weight of its various asset classes, which led the Fund to rebalance its portfolio at different points during this financial year. These rebalancings were made to comply with the limits and guidelines of the *Overall Financial Assets Management Policy* regarding the target asset allocation. They were also a way to actively manage the portfolio within the limits set out by the policy to marginally improve its risk/return profile, taking into consideration the erratic actions of financial and stock markets.

The Shareholder Services sector

The Shareholder Services sector actions are focused on three strategic axes: developing systematic savings, mobilizing our LR (local representatives) network and developing the loyalty of our shareholders. To do so, the Shareholder Services sector principally relies on a network of nearly 2,100 LRs from QFL-affiliated unions (as well as unions the Fund has agreements with) who work as volunteers to promote the Fund in their workplace. These LRs explain the Fund's objectives and encourage workers to subscribe to Fund shares and thereby contribute to Québec's economic development while saving for retirement. Continuing education is provided, in collaboration with the *Fondation de la formation économique*, to the entire LR network to mobilize them around the Fund's mission and the development of systematic savings.

Several shareholder loyalty-building activities were carried out this year, either by personalized mailings, telephone contact or by our increased presence across Québec during the RRSP period. Our strategies are distinguished by their personalized approach. In the current economic conditions, and because the Fund demonstrated immense transparency to its shareholders, we saw an exceptional volume of share redemptions during this period. In fact, shareholders eligible for redemption for retirement were able to redeem their shares before the announcement of the share price last January. In addition, last July the *Purchase-by-Agreement Policy* was updated to simplify the redemption process for shareholders and to adapt to new social situations.

The *Fondation de la formation économique*, created in 1989, encourages economic training for workers so they can increase their influence on Québec's economic development. The education program continues to adapt to the needs of companies and their employees, particularly in today's economic conditions. The Fondation pursues its efforts to publicize the program to the Fund's partner companies to benefit the greatest number of workers possible.

The Investments sector

The Investments sector's strategies focus on realizing the Fund's mission regarding investing in companies impacting Québec's economy as well as strategic investments based on existing criteria. The Investments sector is made up of three main areas of intervention: i) aerospace, construction, services and transportation, ii) natural resources, industries and consumer goods and iii) new economy. Each of these areas is under the responsibility of a Senior Vice-President and includes several specialized sub-sectors. During summer 2008, the Fund grouped the information technology and telecommunications and life sciences sectors under the Senior Vice-President, New Economy.

6. Please see the prospectus for applicable limits and other terms.

This segmentation allows the development of a sector-based expertise valued by our current and future partner companies. Multidisciplinary teams also support our investment teams with their expertise: legal, tax, business valuation, market study, due diligence, labour relations and public market departments. A due diligence committee monitors the credit risk level to ensure it is acceptable and in line with the Fund’s mission. In addition, to deal with more difficult situations, the Senior Vice-President, Turnaround Management and Special Projects, together with the Vice-President, Legal Affairs, very closely monitors investments that entail greater credit risk.

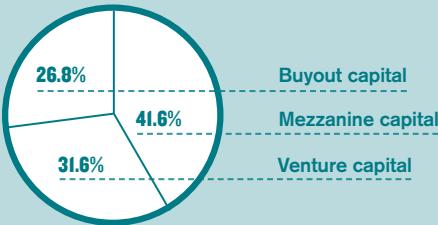
The last few years the Fund has supported the creation of specialized funds and the arrival in Québec of foreign funds by making significant investments in them. This strategy resulted in a considerable inflow of foreign and private capital which helped stimulate the Québec economy while allowing the Fund to better diversify its investments. For a few years now the Fund has increased the volume of its investment in unsecured debentures. This strategy has allowed the Fund to earn a current return on its investments through interest payments, which contributes to the stability of its return.

During the last financial year, the Fund created the position of Vice-President, Majority Interests, whose responsibilities include promoting investments in companies facing succession issues in terms of ownership. Therefore, and contrary to its usual practices, the Fund may, in certain specific situations, make an investment that results in the Fund temporarily becoming the controlling shareholder.

The Fund makes significant investments in each category of development capital as defined by Canada’s Venture Capital & Private Equity Association (CVCA). The CVCA proposes classifying private equity investments into three categories: buyout capital, venture capital and mezzanine capital.⁷ Applying this definition, the following graph presents the breakdown of our \$3.1 billion development capital investments portfolio, at cost.

Breakdown of development capital investments portfolio⁸ by category (at cost)

AS AT MAY 31, 2009



The Other Investments sector

In managing the balance of our assets not invested in partner companies (presented under Other investments in the financial statements), the Other Investments sector is governed by the *Overall Financial Assets Management Policy* which targets sound diversification of the Fund’s financial assets. A sufficient portion of financial assets must be invested so they can meet the Fund’s liquidity needs as well as produce current revenue to cover operating expenses.

All the portfolios in the Other Investments sector, except for the money market portfolio and part of the bond portfolio, are managed by external specialized managers. The two portfolios that are managed internally at the Fund by a team of professionals represented \$1.2 billion as at May 31, 2009 or more than 37% of the total amount of other investments.

Using derivative products provides active management of market risks the Fund is exposed to. When appropriate a risk management strategy is established by the Other Investments sector and authorized by the appropriate authorities to minimize the Fund’s exposure to volatility in interest rates, foreign exchange rates and stock market prices.

During the last year the Fund restructured its Other Investments sector by splitting the responsibilities between two separate Vice-Presidents: the Vice-President, Marketable Securities Portfolio Management and the Vice-President, Marketable Securities Portfolio Strategies and Québec Public Market. These changes are in response to the Fund’s desire to continue prioritizing the optimization of its risk/return ratio despite the increasing complexity of financial markets.

7. Based on the classification proposed by the CVCA, a buyout capital investment is made by purchasing shares of an established private or public company looking to grow organically or through acquisition. A venture capital investment is made by purchasing shares of a company that is generally unlisted and in the start-up or early development stage. Mezzanine capital consists of subordinated debt or preferred shares with or without a variable portion in equity warrants.
 8. On a fund disbursement basis, excluding investments in real estate funds and in listed securities acquired on the secondary market.

60% rule

The 60% rule set out in the Fund's Incorporation Act stipulates that the Fund's average unsecured investments in qualified business enterprises must represent at least 60% of its average net assets of the previous financial year. The remaining assets may be invested in other financial vehicles for asset diversification and sound management purposes. The calculation method for this rule is based on the value of the Fund's assets, which depends in part on interest rate fluctuations and on the performance of stock markets and the economy in general.

As at May 31, 2009, the value of average qualified investments amounted to \$4.4 billion, or 61.7% of the average net assets of the previous financial year (compared to 62.0% as at May 31, 2008). Since the minimum percentage prescribed was reached as at May 31, 2009, the amount of share issues will not be limited for the 2009-2010 financial year. Therefore, the Board of Directors of the Fund has set at an amount of \$700 million the value of shares to be issued giving rise to labour-sponsored fund tax credits for that financial year. As at May 31, 2009 the Fund was also in compliance with all other limits and rules set out in its Incorporation Act.

The Fund expects to comply with all the limits and rules set out in its Incorporation Act over the next several years.

RECENT DEVELOPMENTS

Accounting policies and IFRS changeover plan

During the last financial year, the Fund applied new accounting standards adopted by the Canadian Institute of Chartered Accountants ("CICA"). These standards, which are described in Note 3 to the financial statements, did not affect net loss and loss per share or net value per share as at May 31, 2009 and 2008. In addition, future changes in accounting standards and information concerning the International Financial Reporting Standards ("IFRS") conversion plan are discussed in Note 4 to the financial statements.

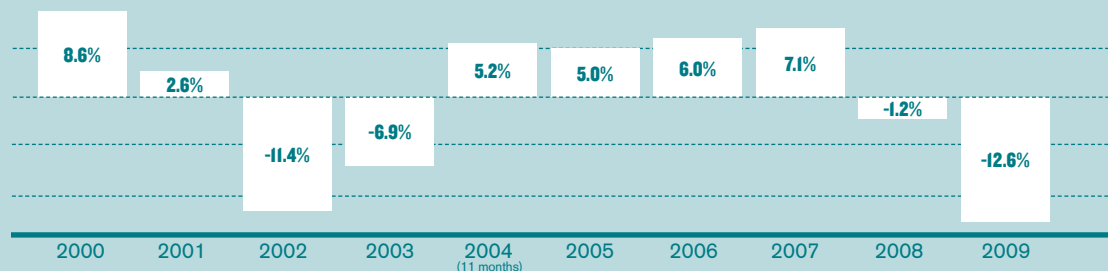
The Fund does not anticipate adopting new accounting policies that would significantly affect its net earnings for the next financial year or the value of its net assets as at May 31, 2010.

PAST PERFORMANCE

This section presents the past performance of the Fund. The past performance of the Fund does not necessarily indicate how it will perform in the future.

YEAR-BY-YEAR RETURNS OF THE FUND

The following chart shows the Fund's annual performance and illustrates how the Fund's performance has changed from year to year for the last ten financial years.



The annual performance of the Fund is calculated by dividing earnings (loss) per share for the financial year by the price per share at the beginning of the financial year. Such performance differs from the annual compound return to the shareholder because the annual performance of the Fund is calculated taking into account share issuances and redemptions made during the year, which have a dilutive or accretive effect on earnings (loss) per share, as the case may be. Such effect was 0.5% on the performance recorded for 2008-2009.

ANNUAL COMPOUND RETURNS TO THE SHAREHOLDER

At the current price of \$21.78, a shareholder who has invested at the beginning of each of the periods indicated below earns the following annual compound returns:

10 years	5 years	3 years	1 year
-0.4%	0.4%	-2.8%	-13.1%

The annual compound return to the shareholder is calculated by taking into account the annualized change in the price per share over the periods indicated. This return differs from the annual performance of the Fund since, as mentioned above, it does not take into account the dilutive or accretive effect of share issuances and redemptions made during the year.

Since the inception of the Fund, the annual compound return to the shareholder has been 3.2%.

ANNUAL COMPOUND RETURNS TO THE SHAREHOLDER (INCLUDING TAX CREDITS)

Including the Québec and federal labour-sponsored funds tax credits (each amounting to 15%), at the current price of \$21.78, a shareholder who has, for instance, invested an equal amount each year through payroll deduction earns an annual compound return of 9.3% and 6.1% for a 7-year and 10-year period, respectively. This return does not take into account the RRSP tax deductions.

SUMMARY OF INVESTMENT PORTFOLIO

As at May 31, 2009, the Fund's total assets comprised of the development capital investments and other investments portfolios, were broken down as follows:

Asset Classes	% of net assets
Development capital investments	
Private securities	24.7
Specialized funds	14.2
Listed securities	8.5
	47.4
Other investments	
Cash and money market	5.5
Bonds	24.7
Sector-based shares	15.2
Funds of hedge funds	3.6
Portfolio of high-revenue securities	3.8
International infrastructure funds	0.7
	53.5

As at May 31, 2009, the issuers of the top 25 positions held by the Fund, of which 17 are part of the development capital investments portfolio and 8 are part of the other investments portfolio, were as follows:

Issuers	% of net assets
Development capital investments (17 issuers)*	28.7
Other investments (8 issuers)**	15.7
	44.4

* The 17 issuers representing, as a group, 28.7% of the Fund's net assets are:

Addenda Capital inc.
Atrium Innovations inc.
Cogeco Câble inc.
Corporation Financière L'Excellence Ltée
Entreprises publiques québécoises à faible capitalisation⁹
Éthanol Greenfield inc.
Fonds immobilier du Fonds de solidarité FTQ inc.⁹
Gestion TFI, société en commandite
LJVH Holdings inc.
Metro inc.
Société de gestion d'actifs forestiers Solifor, société en commandite⁹
Société en commandite immobilière SOLIM⁹
Société en commandite immobilière SOLIM II⁹
SSQ, Life Insurance Company Inc.
Stella Jones Inc.
Transcontinental Inc.
Trencap s.e.c.

** The 8 issuers representing, as a group, 15.7% of the Fund's net assets are:

Financement Québec	4.6%
Government of Canada	3.2%
Hydro-Québec	2.6%
Province of Québec	1.2%
Laurentian Bank of Canada	1.1%
FRM Diversify II Fund SPC	1.1%
The Bank of Nova Scotia	1.0%
Q-BLK Strategic Partners, Inc.	0.9%

This summary of investment portfolio may change due to ongoing portfolio transactions of the Fund.

9. Despite their relatively important weight in the overall portfolio of the Fund, these issuers do not constitute a significant concentration risk given their large number of investees.

CONTRIBUTION TO QUÉBEC'S ECONOMIC DEVELOPMENT

Thanks to the savings collected from 571,000 shareholders, of whom nearly 253,000 subscribed in 2008-2009, more than ever the Fund continues playing an active role in the development and growth of Québec's companies. In particular, in the current economic environment that is less favourable to our Québec companies, our rhythm of investment increased over the last year to a total of \$848 million, in addition to the \$542 million that the Fund has agreed to invest in connection with the last budget of the Government of Québec, to support Québec entrepreneurs who have demonstrated resilience during this difficult time of tightened credit conditions. However, an economic recession might be a good time for them to review their internal processes, optimize their operations, redefine their markets and even seize favourable opportunities. Our teams are working closely with company executives because the coming months could also be tumultuous. As such, the Fund maintains its objective to continue investing with a long-term vision to help companies move through this period with confidence and to optimistically look forward to the days beyond the crisis.

Several structuring investments for the Québec economy were made over the year that contributed to creating, maintaining or saving quality jobs. In the financial services sector, \$30 million was invested in Montrusco Bolton Investments, which helped bring control of this large portfolio manager back to Québec, and an investment of \$100 million in Corporation Financière L'Excellence, a subsidiary of Industrial Alliance Insurance and Financial Services, helped the company continue to grow through acquisition. In the printing sector, Transcontinental received unsecured financing of \$100 million to support its growth despite the current economic environment.

In the distribution sector, for example, \$20 million allowed Groupe B.M.R. to acquire a regional chain and consolidate its market share against foreign renovation megacentres. We have renewed our business ties with Premier Tech, an agricultural products and industrial equipment manufacturer, after our initial assistance of more than 20 years was completed in 2007, through an investment of \$15 million to support the company's development and long-term stability. Also, to preserve ownership and management of timberland in the Bas-Saint-Laurent region, \$66 million allowed Solifor to buy the property titles from AbitibiBowater. In addition, \$6 million was invested in Groupe Solmax, a global manufacturer of geosynthetic membranes so it could consolidate its position in Québec and pursue its international strategy.

The Fund also maintained its commitment toward companies operating in the new economy. Investments amounting to \$125 million that were made include the following: \$31 million was invested in GFI Solutions Group, including \$20 million so it could acquire Bell Business Solutions, a subsidiary of Bell Canada that offers a wide range of enterprise resource planning (ERP) software; \$21 million in BDR Capital so it could support the growth of several companies in the telecommunications sector; and \$2 million in Fonds soutien Montréal parallèle, a fund that specializes in providing seed capital to information technology and telecommunications companies.

The Fund did not make any investments in 2008-2009 as part of its strategic investments program.¹⁰

Furthermore, to weather the recession that has been battering Québec for the last several months, on March 19, 2009 it was announced in the provincial budget that the Fund will join the Government of Québec and other partners in launching three new financing programs. This represents a great sign of the Government of Québec's confidence as it has been supporting the Fund's mission for more than 25 years and believes in the value of its contribution to the dynamism of Québec's economy. In this context, the Fund agreed to invest an amount totalling \$542 million, with \$500 million already committed during the 2008-2009 financial year.

The objectives of these three new specialized funds are presented below:

Creation of the *Élan d'entreprises* recovery fund

This new \$500 million fund is intended to fuel the development of medium and large private and public Québec companies grappling with liquidity problems that could delay their investment projects, and hence, their growth. This fund will be capitalized equally by the Fund and Société générale de financement du Québec (\$250 million each).

Creation of the *Terallys Capital* fund to finance new economy sector venture capital funds

The importance of recapitalizing Québec companies in the new economy, particularly those at the start-up stage, cannot be overstated. The Fund is therefore proud to pursue its commitment in this sector and inject \$250 million in the \$700 million of initial capital for the Terallys Capital fund, created jointly with the Caisse de dépôt et placement du Québec and Investissement Québec. This fund's objective is to raise an additional \$125 million from private institutional investors.

Creation of Québec seed capital funds

Over the years, with the support of its network of regional funds, SOLIDES (*Société locale d'investissement dans le développement de l'emploi*), and specialized funds, the Fund has made numerous investments in Québec start-ups. To continue supporting Québec ingenuity, the Fund will join other key economic players in Québec to set up three seed capital funds in which a total of \$125 million will be invested. The Fund's share in these new funds could reach \$42 million.

10. The 2003-2004 Québec budget granted the Fund the opportunity to make strategic investments in large Québec companies with assets of less than \$500 million or with a maximum net worth of \$200 million.

POLICY FOR INVESTMENTS OUTSIDE QUÉBEC¹¹

Investments made by the Fund over the years pursuant to the *Policy for Investments Outside Québec* have had significant economic spin-offs for Québec as required by the policy. This year, a total of \$76 million was invested in the various eligible categories pursuant to this policy.

The eligibility of investments made by the Fund in private funds outside Québec, pursuant to the 60% rule, is conditional to reinvestment in Québec companies of an amount at least equal to the amount these private funds received. These private funds should also bring to their partner companies a specific expertise and/or an international business network necessary for their development. In the last year, the Fund invested the equivalent of \$54 million in three private funds outside Québec and anticipates that each of these private funds, in addition to supporting the Fund's efforts in terms of Québec's economic development, will invest in Québec companies an amount at least equal to the sums received from the Fund.

An investment of \$4.1 million in a company impacting the Québec economy was qualified under the policy during the last year. Finally, the Fund invested the equivalent of \$18 million in three companies outside Québec that carry out large-scale projects in Québec.

THE FUND NETWORK

Since its inception in 1983, the Fund has built a solid investment network that provides entrepreneurs who follow their ambitions with patient capital based on their needs. A veritable business hub brimming with ideas, talent and knowledge, this network offers the Fund's partner companies the opportunity to share common concerns with other SMEs, learn from past experiences and forge new business ties. The Fund's Investment network revolves around four levels of investment:

- The Solidarity Fund QFL offers \$2 million and up for large companies.
- The 16 Regional Solidarity Funds QFL offer \$100,000 to \$2 million to meet the needs of businesses in every region of Québec. The Equity Loan and the Growth Loan are the two main products offered by the regional funds.
- The 87 SOLIDEs (*Sociétés locales d'investissement dans le développement de l'emploi*), created by the Fund and the *Fédération québécoise des municipalités*, offer \$5,000 to \$100,000 to small businesses.
- The specialized funds form an investment network in Québec and abroad that invests in assorted industries. The Fund's commitment to this network continued in 2008-2009, in particular through new funds created with the help of the Government of Québec, which has allowed the Fund to increase the breadth of its various networks and to facilitate Québec SMEs' access to capital in all their stages of development.

The following graph shows the breakdown of the Fund's investments based on its various network components:

Distribution of investments by network components (at cost)

AS AT MAY 31, 2009



11. Since 1998, the Fund has been authorized by the Québec Minister of Finance to invest outside Québec provided certain clearly defined conditions are met, notably with regards to economic spin-offs. The main groups of eligible investments are private funds outside Québec, companies impacting the Québec economy and large-scale investment projects (financing for expansion, modernization, productivity improvement).

OUTLOOK AND TRENDS

ECONOMIC AND FINANCIAL OUTLOOK

The immediate future is paved with uncertainty and the end of the two-year long global crisis does not seem near. Banks, consumers, businesses and governments are all concerned.

All the problems plaguing American banks are not yet solved because of the large amounts of “toxic” assets weighing down balance sheets and the conditions the American government imposes when it intervenes. Consumers are still uncertain; increasing unemployment encourages saving (which is rising) rather than spending while the massive loss of wealth is worrisome for those facing retirement.

The stock market collapse perfectly expresses the sentiments of American companies in particular and global companies in general. Future profits will be lower and hope for a sudden economic rebound is slim. With the pessimism exhibited by company executives, it should not be surprising to see the rationalizations of 2008 continue through the next year. None of this takes into account the uncertainty faced by large U.S. automakers and the collateral damage on the other sectors of the automobile industry.

If we look for an optimistic note, we would have to look at U.S. housing prices. Consumers will not receive credit to augment their spending as long as housing prices are not rising. Banks will not see the value of “toxic” assets they hold rise and credit will continue to be difficult to obtain.

Of course the Canadian market is linked to its southern neighbour; it is thus difficult to be optimistic for Canada for the next few quarters. Raw material prices are greatly linked to American demand and a rebound in China would help Canada weather this rough period. Many variables could influence our currency; adopting quantitative easing (money creation) would devalue the Canadian dollar while stabilizing raw material prices would sustain the loonie. A range between \$0.80 and \$0.95 is expected. Thankfully, Canadian banks are healthier than U.S. banks.

Short-term interest rates are close to zero and the long term interest rates must go lower to sustain the economy. The Bank of Canada should not have difficulties following an expansionist monetary policy based on very low interest rates during 2009. International inflation expectations are squarely anchored under the 2% level and recorded inflation remains very weak, leaving plenty of room for the central bank.

The Québec economy cannot, however, go it alone in 2009; its economic statistics will depend on those of Canada. Despite significant assistance from government spending (notably on infrastructure), the province will not escape what we hope is a brief recession. The most optimistic scenarios do not show a rebound before fall 2009.

TRENDS IN THE DEVELOPMENT CAPITAL INDUSTRY

After several years of uninterrupted growth, the Québec venture capital market experienced a sharp decline in activity (both in volume invested and the number of investments) in 2008. The decrease in activity, both in Québec and the rest of Canada, is largely due to the decreased presence of American and other foreign venture capital investors. If we add the buyout capital and mezzanine capital categories to venture capital, development capital activities as a whole slightly dipped in 2008 compared to 2007 and returned to 2006 levels for amounts invested and the number of transactions.

Despite lower investments, Québec still represents slightly more than one quarter of all venture capital investments made in Canada, specifically because of the strong activity of all the tax-advantaged funds in our province. Nearly one third of investments made in Québec are attributable to them, compared to less than one quarter for all tax-advantaged funds in Canada.

During the next year the Fund expects to continue being an important and essential player in the development capital industry in Québec. Nonetheless, experts generally agree that 2009 will likely be difficult. Given the difficulties most institutional investors have faced in the stock markets, we can expect it to be harder for investment funds to find new capital. Most of the funds' portfolios include companies that were affected by the crisis and that will need to be more actively supported in 2009, thereby limiting the capacity of these funds to invest in new companies. However, banks moving to tighten credit might cause entrepreneurs looking for financing to let other investors participate in their capital and thereby provide opportunities for funds that possess enough liquidity to invest in these companies.

THE SAVINGS MARKET AND RRSP

According to a number of finance experts, the savings market will continue to be tough next year. Investors' confidence was shaken; the words of the day for financial advisors remain caution and risk reduction. For investors who are more risk-tolerant, unsecured products will still be considered from among the range of retirement savings products.

During next year, the Fund RRSP should maintain its advantageous position among the choice of retirement savings products thanks to its tax credit and competitive return. According to the results of the SOM-RRSP study from May 2009 (a study on the retirement savings market), the average contribution to the Fund RRSP and the number of small investors choosing the Fund for portfolio diversification should continue to increase.

FUND OUTLOOK¹²

Based on the currently foreseeable economic and financial outlook, and taking into consideration our mission and investment strategies, we are targeting an annual return of 3% to 4%, on average, over the next years. This return does not take into account tax credits granted to shareholders upon purchasing shares of the Fund and is subject to significant half-year or annual volatility.

While the Fund is confident it will reach its return objective in the long term, the annual return depends on current economic conditions and the ups and downs of the stock and financial markets. Therefore, the Fund's return over the next year will be greatly influenced by stock market returns. The return for private securities is also linked to the general performance of the economy and may be lower than their historic average returns, particularly because of the lingering effects of the increase in credit cost and the economic recession, the volatility of the Canadian dollar compared to the U.S. dollar and the effects of foreign competition. The Fund is targeting a ratio of operating expense to average net assets comparable to the one achieved for the financial year ended May 31, 2009.

In the coming years, the Fund expects to continue using derivative products with respect to a portion of its bond portfolio to lessen the negative impact an increase in Canadian interest rates would have on its earnings. Given the protection such a strategy provides, we must therefore sacrifice a part of the earnings resulting from an increase in the value of our bond holdings should the rates of the bonds issued by the Canadian government decline. The level of hedging of the bond portfolio will vary based on the economic outlook. This strategy is necessary to meet shareholder expectations and to avoid, inasmuch as possible, a decline in the Fund share price. We also use other protective measures, such as occasionally using derivative products to reduce our exposure to foreign exchange risk or to reduce the impact of an anticipated fall in the value of certain sectors or specific securities on the stock markets. In such cases, we must also relinquish a part of the increase in the price of our investment if the corresponding currency or stock market price rallies.

With projected share issues higher than anticipated redemptions, the Fund's net assets should increase over the next year. On the other hand, the volume of investments made by the Fund will likely be lower than the record investments levels recorded in the last two financial years.

RISK MANAGEMENT

Sound risk management practices are vital to the success of the Fund. We manage our risk within a framework taking into account the nature of the Fund's activities and the risks we can reasonably assume in light of the desired risk/return ratio and shareholder expectations. To this end, we capitalize on a structured risk management process to determine, measure and control the significant risks with which the Fund must contend.

Notice to readers: The following two paragraphs and the sections on market risk, credit and counterparty risk and liquidity risk form an integral part of the financial statements on which an auditors' report was issued on June 19, 2009.

The Fund manages all its financial instruments in an integrated, comprehensive manner in accordance with the standards set out in the *Overall Financial Assets Management Policy* adopted by the Board of Directors. This policy covers both development capital investments and other investments. It sets goals, guidelines and limits allowing the management of the Fund to ensure that the target risk/return profile is met on an operational basis. It also specifies that derivative financial instruments must never be used for speculation purposes.

The principles of our risk management approach did not change materially during the financial year ended May 31, 2009. In the normal course of business, the Fund is exposed to different risks; the principal ones are presented below.

¹² The outlook presented in this MD&A reflects the Fund's expectations with respect to future events, based on information available to the Fund as at June 19, 2009, and presupposes certain risks, uncertainties and assumptions. Many factors, several of which are beyond our control, may cause the Fund's actual results, performance, or achievements to differ materially from explicit or implicit expected future results, performance, or achievements.

MARKET RISK

Market risk is inherent to the Fund's participation in financial markets and represents the risk of losses arising from fluctuations in interest rates, exchange rates and prices of listed financial instruments. More specifically, this risk varies with the financial markets' conditions and certain market parameters, such as volatility, that may lower the value of the Fund's financial assets and thus have a negative impact on the Fund's balance sheet and Statement of Operations. Consequently, and as was seen during the 2008-2009 financial year, difficult economic conditions could have a negative impact on the value of the Fund's shares.

The Fund's financial assets are especially sensitive to listed share prices and fluctuations in bond interest rates (Canada bond rates, credit spreads). Since most of its transactions are in Canadian dollars, the Fund's direct exposure to exchange risk is relatively low. However, common hedging mechanisms such as foreign currency forward contracts are generally used for other investments in a foreign currency.

The Fund manages market risk by allocating its financial assets across several classes. In addition, the Fund invests in various industries (government and government agencies, financial institutions, technology, manufacturing and primary, services and tourism, regional or local funds and real estate) and geographic areas, within the limits allowed by its Incorporation Act.

Sensitivity analyses and simulations are used to inform senior management of material levels of market risk exposure. The Fund may then use derivative financial instruments to reduce its market risk exposure and safeguard the value of its assets.

The value of unlisted financial instruments in the development capital investments portfolio is established using approved and accepted valuation techniques. These techniques are based on a set of assumptions that take into account market conditions such as exchange rates, economic growth, credit spreads, etc. as at the valuation date. Since the assumptions used are highly interrelated, a sensitivity analysis that isolates the impact of only one of these variables on the private securities portfolio is not considered to fairly represent the sensitivity of the results.

Sensitivity of the Fund's results to market risk, as at May 31

(in millions of dollars)	2009	2008
Change in bond interest rates*		
1% increase in bond interest rates	(99)	(60)
1% decrease in bond interest rates	99	60
Change in listed share prices**		
10% increase in listed share prices	172	192
10% decrease in listed share prices	(172)	(175)

* This analysis is performed on bonds held by the Fund presented under Other investments in the financial statements. In this analysis, the impact on results takes into account the use of derivative financial instruments in certain cases.

** This analysis is performed on listed shares held by the Fund presented under Development capital investments and Other investments in the financial statements. In this analysis, the impact on results takes into account the use of derivative financial instruments in certain cases.

CREDIT AND COUNTERPARTY RISK

The Fund's exposure to credit risk stems mainly from its investment activities in development capital associated with its mission. In that regard, the investments are generally unsecured. Its other investment activities entail less of this risk since the counterparties concerned are typically more financially solid (governments, banks, etc.).

Credit risk is the potential for loss due to the failure of a partner company (financial instruments presented under Development capital investments), issuer or counterparty (financial instruments presented under Other investments) to honour its contractual obligations or due to a degradation of its financial position. The Fund manages this risk and maintains a sound diversification of its assets through the *Overall Financial Assets Management Policy*. This policy therefore allows us to manage the concentration risk associated with exposure to an issuer or group of issuers with common characteristics (industries, credit ratings).

Exposure to credit and counterparty risk as at May 31

(fair value as a percentage of net assets)	2009	2008
Weight of the five largest investments (Development capital investments)	14.6	14.8
Weight of the five largest issuers or counterparties (Other investments)	12.6*	18.8*

* The share attributable to securities issued or guaranteed by the Governments of Québec and Canada represented 11.5% as at May 31, 2009 (May 31, 2008: 12.0%).

The summary of investment portfolio presented previously in this MD&A also discloses relevant information for assessing the credit and counterparty risk concentration level.

Targets by industries, in keeping with our internal structure, are approved each year for the development capital investments portfolio. These targets are set using risk budget management. Based on an optimal risk level defined for this portfolio as a whole, risk budget management allows us to more effectively monitor and control the portfolio profile and sector allocation by risk level. The risk/return balance of this portfolio is achieved through a sector-based risk budget allocation that takes into account the higher risk of our investments in certain sectors.

The status of investments is re-examined regularly to justify their classification in one of the following categories: compliant with internal criteria, under watch or in turnaround. To deal with the more difficult situations, an internal committee monitors very closely investments that entail greater credit risk.

Classification of the development capital investments portfolio at May 31

(fair value in millions of dollars)	2009	2008
Compliant with internal criteria	3,109	3,111
Under watch	213	187
In turnaround	31	9
	3,353	3,307

In the case of the other investments portfolio, issuer and counterparty ratings and exposure limits by borrower or counterparty enable a prudent diversification of our assets. These criteria are set based on the risks specific to each asset class and ensure that the Fund's results will not be materially affected in the event of a payment default. As at May 31, 2009 and 2008, the weighted average credit rating of bonds was A, which is in compliance with the requirements of the *Overall Financial Assets Management Policy*.

Fair value of bonds included in the other investments portfolio by Standard & Poor's ratings

(in millions of dollars)	2009	2008
AAA	294	272
AA	243	342
A	886	1,684
BBB	206	270
Other	9	13
	1,638	2,581

LIQUIDITY RISK

The Fund must make disbursements on a daily basis. Cash outflows occur when the Fund redeems Class A shares held by shareholders, disburses its investments in companies, remits amounts under management and pays operating expenses. The Fund must be able to obtain the cash required to meet its commitments. Liquidity risk is therefore related to the potential for loss due to the inability of the Fund to meet such commitments. In certain cases, securities acquired on the market by the Fund may be subject to resale restrictions, thus potentially reducing their liquidity.

The Incorporation Act of the Fund provides that part of the financial assets may be invested in marketable securities on organized markets, such as stock and bond markets, which offers the possibility to easily obtain cash. The Fund also has access to bank credit facilities for additional sources of liquidity.

As at May 31, 2009, the ratio of liquid financial assets¹³ as a percentage of assets under management was 51.2% (May 31, 2008: 56.1%), demonstrating management's opinion that the Fund has the required liquidity to fulfill all its obligations and commitments.

OPERATIONAL RISK

Inherent to all the Fund's activities, operational risk is the risk of sustaining losses as a result of the inadequacy or failure of certain processes or systems in place or due to human factors or external events. This risk also includes legal risk.

¹³ Liquid financial assets are comprised of fixed-income securities (cash, bonds and money market securities), listed shares of the other investments portfolio and certain listed shares of the development capital investments portfolio.

Effective policies, standards and procedures are implemented to manage this risk. Control principles and mechanisms are monitored and periodically revised as part of a continuous improvement process. The Fund's operational risk management and the effectiveness of its management framework are underpinned by the following guiding principles:

- Competent, well-trained staff;
- A culture of integrity;
- Segregation of incompatible duties;
- Adoption of a concept of independence inspired by the securities regulations applicable to public companies;
- Delegation of decision-making authority to Special Boards whose majority of members are independent;
- Adherence to a framework program of financial compliance adapted to the Fund's particular circumstances;
- Control of technology development and information security;
- A planning process for resumption of activities in the event of business interruption;
- Continuous monitoring of changes in applicable legislation, regulations and standards, including the Fund's compliance therewith; and
- Risk identification and assessment when new products or activities are introduced.

The Codes of Ethics and Conduct define, among other things, the rules of conduct to be followed by employees, officers and directors to avoid, for instance, conflict of interest situations. All employees or officers must, in the execution of their duties, put the interests of the Fund ahead of their own or those of third parties. They must also avoid placing themselves in a conflict of interest situation, either real, potential or apparent. The Codes of Ethics and Conduct prohibit, among others, certain personal trading deemed conflictual, including receiving certain gifts and using any advantage, information or interest related to the Fund that would be incompatible with the professional duties and responsibilities of an employee. In addition, the Codes forbid, among other things, the disclosure by directors and employees, for purposes other than the execution of their duties, of confidential information obtained through such execution.

Each year, all employees must complete a statement of interests held and a statement on the compliance of their conduct with the Code.

To diversify its financial assets management, the Fund also calls upon the services of specialized external managers and acquires interests in specialized funds. Where appropriate, the Fund purchases insurance that transfers certain components of operational risk to insurers.

OTHER RISKS

The Fund is also exposed to other risks such as strategic and reputation risks, which could result in negative financial consequences.

Strategic risk, which includes competitive risk and risk associated with regulatory changes, refers to the possibility of incurring losses as a result of ineffective strategies, lack of integrated business strategies or the inability to adapt the strategies to changes in the business environment. We manage this risk through a strategic and operational planning process that seeks input from all levels of the organization before being submitted to the Board of Directors for approval. The Management Committee then periodically monitors each sector's business plan. Any strategic decision or change to the Fund's orientations that could have a material impact is authorized beforehand by the appropriate authorities, based on the powers delegated to them.

Reputation risk is the risk that negative publicity, whether founded or unfounded, will or may cause losses, a decrease in liquidity or a decline in the customer base. The Fund controls and manages reputation risk through proper training, legal and financial due diligence for all its capital development investments, sound governance practices and the application of policies and procedures as well as through the formulation and implementation of the Codes of Ethics and Conduct. The Fund is a responsible corporate citizen that takes ethical, social and environmental aspects into consideration when making investment decisions. We have also adopted a voting rights policy with regards to public companies and a code of conduct for international business dealings. The Fund also ensures that any financial information released outside the organization is accurate and validated beforehand.

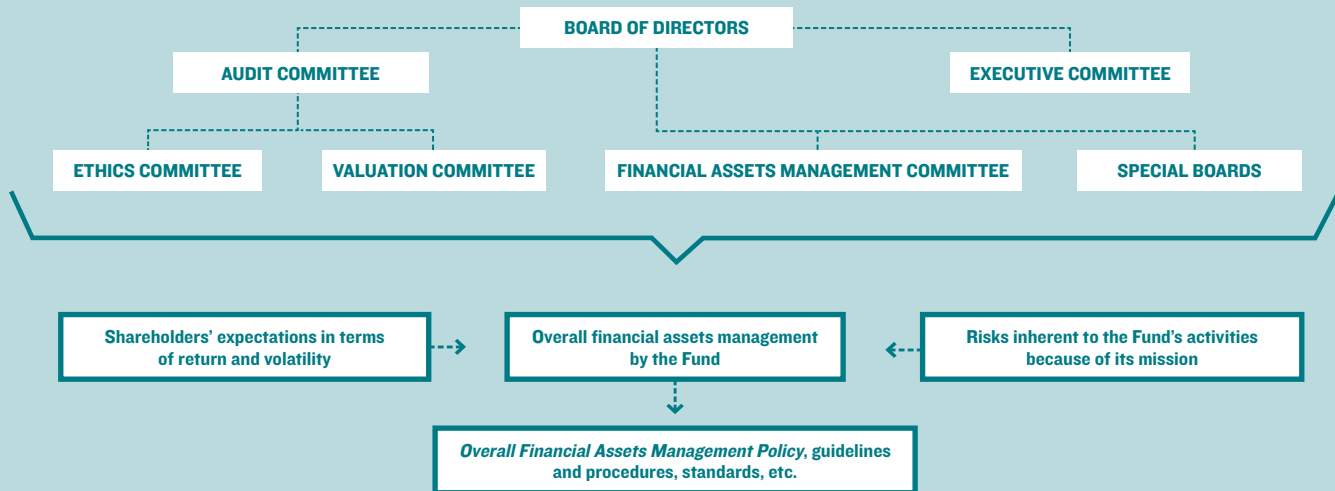
In 2008, the Fund implemented a *Disclosure Policy* concerning all financial and non-financial information issued and/or disclosed externally and the information that is communicated internally to a large number of employees. The main objectives of this policy are to provide a disclosure framework and standards, to ensure that information disclosed is rigorously prepared and validated, to make the Fund's employees aware of disclosure principles, and to specify the roles and responsibilities of the main participants in the disclosure process.

The application of this policy is monitored by a Disclosure Committee composed of members of management of the Fund. The main responsibilities of this Committee are to set disclosure guidelines, to implement and keep up to date the *Disclosure Policy* and ensure it is complied with, and to ensure that relevant and effective disclosure controls and procedures are in place. The Disclosure Committee reports its activities to the Management Committee.

GOVERNANCE

RISK GOVERNANCE

The Management Committee, comprised of the President and CEO and executives, is responsible for the global management of the Fund's operations. Because risk management is an essential part of overall financial assets management, the Fund has put in place a management framework to ensure that risk management and control strategies and resulting operational decisions take the established level of acceptable risk into account. This management framework is as follows:



Our risk governance structure comprises a series of policies approved by the Board of Directors. Policies, standards, guidelines, and procedures are regularly reassessed to ensure that we rely on only the best possible practices. It should be noted that the functions of Chairman of the Board and President and CEO are separate.

The *Overall Financial Assets Management Policy* is a key piece of this management framework. The policy sets out the target financial asset allocation allowing the Fund to fulfill its mission while meeting the desired risk/return ratio through sound diversification that helps mitigating the volatility of such return from half-year to half-year. This policy also provides objectives, guidelines, and limits within which our managers and professionals perform their duties and carry out their mandates. In fact, the *Overall Financial Assets Management Policy* is composed of several policies covering general principles, orientations, limits and guidelines applicable to the various asset classes, including a separate policy applicable to the Investments sector. The detailed guidelines and procedures covering the management of financial assets on an operational basis are presented separately to facilitate their application.

Board of Directors

The Board of Directors carries out specific duties, including:

- Ensuring the Fund's mission is followed at all times as noted in its Incorporation Act;
- Approving the main directions, policies and business strategies of the Fund;
- Approving investment recommendations for which it is responsible;
- Ensuring the Fund, in its role as an investor, behaves as a socially responsible company to the extent applicable; and
- Evaluating the Fund's performance on a regular basis.

Members of the Board of Directors are nominated or elected according to the rules set out in the Fund's Incorporation Act. In carrying out its mandate, the Board delegates part of its responsibilities to the following committees:

Executive Committee, Special Boards and Other Delegate Boards

In addition to the Board of Directors, Delegate Boards also oversee development capital investment decisions. Delegate Boards include the Executive Committee and the Special Boards created for the *Traditional, New Economy, Mining Portfolio and Turnaround and Majority Interests* sectors. Each development capital investment of \$5 million or more must be authorized by the Board of Directors, or the Executive Committee if the Board of Directors is unable to meet in a timely fashion. Regardless, each of these investments must be recommended by the Special Board overseeing the corresponding activities. All investments of less than \$5 million are under the authority of the corresponding Special Board. The Special Board for the *Traditional* sector was created in May 2009. Prior to this its mandate was performed by the Executive Committee. The four Special Boards are composed of a majority of independent members.

Audit Committee

The Audit Committee is comprised entirely of independent members and its mandate includes: recommending the audited financial statements and MD&A for approval by the Board of Directors; approving the principles for valuing development capital investments and receiving the Valuation Committee's report; enquiring about the effectiveness of internal controls implemented by management and the fact that they are not overridden; enquiring about the compliance and risk management process and providing feedback; and receiving the Ethics Committee report and overseeing the application of the Code of Ethics for Board members. The Committee also ensures the Fund complies with the statutes, regulations and agreements that govern its operations and that have a material financial impact. The Audit Committee reports on its activities to the Board of Directors and makes recommendations to it when necessary.

In addition, an Ethics Committee composed of members of management support the Audit Committee in monitoring the application of the Fund's Codes of Ethics and Conduct.

Financial Assets Management Committee

This committee is responsible for monitoring the implementation, compliance with and updating of the *Overall Financial Assets Management Policy*, including the investment policy and the policies applicable to the various asset classes of the Other Investments sector. Its primary mandate is to ensure that asset management is coordinated and linked. In this capacity, it recommends the financial vision and orientation for financial assets management to the Board of Directors. This committee also monitors performance, changes in the risk/return ratio and the Fund's compliance with all its policies regarding financial assets management, and ensures that the Fund has adequate and sufficient guidelines and procedures. The Financial Assets Management Committee reports twice yearly on its activities to the Board of Directors and makes recommendations to it when necessary.

Valuation Committee

The Fund created the Valuation Committee, which is composed of a majority of independent qualified valuers, in the second half of the 2008-2009 financial year, and mandated it to provide a reasonable assurance that the procedure used for valuing the development capital investments portfolio comply with the procedure set out in the *Regulation Respecting Development Capital Investment Fund Continuous Disclosure*. The Valuation Committee reports twice yearly on its review to the Audit Committee.

NEW REGULATION OF THE *AUTORITÉ DES MARCHÉS FINANCIERS*

In 2008, the *Autorité des marchés financiers* issued the *Regulation Respecting Development Capital Investment Fund Continuous Disclosure*. These new requirements have been applied to the Fund's financial statements and MD&A for the 2008-2009 financial year. Generally speaking, this Regulation requires the disclosure of additional items, essentially in the balance sheet, the Statement of Operations and the notes to the financial statements. In addition, the Fund must now disclose more information about its derivative financial instruments and issue a schedule of its other investments.

The Regulation also specifies the contents of the Management Discussion and Analysis and the Annual Information Form and clarifies the management framework that should govern the procedure for valuing development capital investments.

VALUATION FRAMEWORK

Development capital investments and other investments are recorded on the balance sheet at their fair value.¹⁴ However, the majority of the Fund's development capital investments are made in private companies or specialized funds for which a fair value must be established because the securities issued by these companies or funds are not traded on organized, public markets. Specialized valuers employed by the Fund determine the fair value of these investments. These valuers report to the Executive Vice-President, Finance and follow a structured process comprising several verification and validation steps to ensure the quality, uniformity and integrity of the work performed and of the resulting fair value.

The management framework that should govern the procedure for valuing development capital investments is set out in the *Regulation Respecting Development Investment Fund Continuous Disclosure*. In particular, the Regulation specifies the minimum qualifications required for specialized valuers employed by the Fund as well as the authority responsible for approving the valuation principles used. The Regulation also requires that all relevant information about the valuations (excluding publicly traded issuers valued using market prices) should be provided to an independent valuation committee. In addition, the President and Chief Executive Officer and the Chief Financial Officer must sign a certification confirming that valuation procedures set out in the Regulation were complied with and the aggregate fair value of the development capital investment portfolio. This certification was filed on SEDAR for the first time as at May 31, 2009.

¹⁴ Using fair value is a best practice recognized by venture capital firms and private equity funds. Fair value is defined as the amount of the consideration that would be agreed upon in an arms-length transaction between knowledgeable, willing partners who are under no compulsion to act.

FINANCIAL GOVERNANCE

The Fund continued its work over the last financial year to develop a financial compliance program commonly known as *Confor*. While not required to apply MI 52-109 issued by the Canadian Securities Administrators, the Fund has decided to base its work upon the principles stated in this rule, thereby demonstrating its willingness to respect best practices in financial governance. This framework applies to controls providing reasonable assurance that the financial information prepared and reported is reliable and that the financial statements are prepared in accordance with Canadian Generally Accepted Accounting Principles.

Management is responsible for designing and maintaining internal control over financial reporting and disclosure controls and procedures. It must also periodically evaluate their design and effectiveness.

During the year, the Fund completed its evaluation of the design of internal control over financial reporting and its evaluation of the design and effectiveness of disclosure controls and procedures. Certifications were signed by the President and Chief Executive Officer and the Chief Financial Officer as at May 31, 2008 and 2009 confirming their responsibility to that effect. These certifications are available on SEDAR. A mechanism for sub-certification by several Fund executives also supports the certifications.

During the 2009-2010 financial year the Fund will continue to deploy its evaluation process of effectiveness to all internal controls to be able to attest to their effectiveness in its May 31, 2010 MD&A. Management's conclusions on the design of internal control over financial reporting and the design and effectiveness of disclosure controls and procedures are presented below.

MANAGEMENT'S REPORT ON INTERNAL CONTROLS

Management is responsible for designing and maintaining internal control over financial reporting and disclosure controls and procedures. It must also periodically evaluate their design and effectiveness. The evaluation of control design was performed based on the COSO Framework (Committee of Sponsoring Organizations of the Treadway Commission), a recognized financial governance framework.

CONCLUSIONS ON THE DESIGN OF INTERNAL CONTROL OVER FINANCIAL REPORTING

As at May 31, 2009, management evaluated the design of internal control over financial reporting. Based on the work done, management can conclude that internal control over financial reporting is adequately designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements in accordance with Canadian Generally Accepted Accounting Principles. During the year ended May 31, 2009, there was no change in the Fund's internal control over financial reporting that has materially affected, or is reasonably likely to affect, the Fund's internal control over financial reporting.

CONCLUSIONS ON THE DESIGN AND EFFECTIVENESS OF DISCLOSURE CONTROLS AND PROCEDURES

As at May 31, 2009, management evaluated the design and effectiveness of disclosure controls and procedures. Based on the work done, management can conclude that disclosure controls and procedures are adequately designed and operate effectively to provide reasonable assurance that information disclosed is recorded, processed, summarized and presented within the time periods specified in the regulations and that it is communicated to management on a timely basis for decision-making purposes.