Investor Risks

associated with PEPP Investment Funds

This table shows the investor risks associated with each PEPP investment fund. Each asset allocation fund has the investor risks identified. The Bond Fund and Money Market Fund are exposed principally to credit risk and interest rate risk as their holdings are limited to domestic fixed-income securities. The other risks come into play when there are investments other than bonds within the fund.

Credit Risk	A fixed income security, such as a bond, is a promise to pay interest and repay the principal on the maturity date. There is always some risk that the issuer will fail to honour that promise. This is called credit risk. Credit risk is lowest when issuers have a high credit rating from a credit rating agency. Conversely, credit risk is higher when issuers have a low credit rating. Issuers with lower credit ratings typically offer higher interest rates to make up for the higher credit risk. This leads to bonds with greater yields, but also greater volatility.
Currency Risk	When a fund invests in foreign denominated securities, the value of those securities is subject to increase or decrease based on changes in the exchange rate between the foreign currency and the Canadian dollar. This is called currency risk. Currency risk can be reduced by using a currency hedging strategy.
Derivative Risk	Derivatives can be useful financial instruments for hedging against losses, gaining exposure to financial markets and making indirect investments. These involve certain risks.
Equity Risk	Funds that invest in equities, such as common shares, are affected by the general economy and financial markets as well as by the success or failure of the issuer of the shares. When stock markets rise, the value of equity securities tend to rise also, and when stock markets fall, the value of equity securities tend to fall. The risk that any given equity security will rise or fall simply because of general market forces is called equity risk.
Foreign Investment Risk	Investments issued by foreign companies or governments can be riskier than those issued by Canadian companies or governments. Foreign countries can be affected by political, social, legal, or diplomatic developments that can have significant impacts on foreign investments. These risks that are unique to foreign investments are called foreign investment risk.
Index Risk	Some investment funds have a stated objective of following a given market index. Market conditions may allow a situation where one or more securities may comprise a significant portion of the index. Any fund that is intended to follow such an index may find high exposure to that same security or securities. This high concentration of investments in one or more securities reduces the diversification of the fund and may lead to greater volatility and reduced liquidity.
Interest Rate Risk	Investment funds that invest in fixed income securities, such as bonds are sensitive to changes in interest rates. In general, a rise in interest rates will lead to lower values for fixed income securities, and a decrease in interest rates will lead to higher values for fixed income securities. Securities with longer terms to maturity are generally more sensitive to changes in interest rates. This risk that a change in interest rates will affect the value of a security is called interest rate risk.

Liquidity Risk	Liquidity is a measure of how quickly an investment can be exchanged for cash as a fair market value. Investments with poor liquidity cannot be sold quickly or cannot be easily sold for the fair market value. Investments with lower liquidity generally see greater volatility in value. When an investment fund is unable to liquidate one or more investments quickly or at fair market value, the investment fund may lose value. This is called liquidity risk and is more common with real estate or securities issued by smaller companies.
Real Estate Sector Risk	Some investment funds concentrate their investments entirely in real estate holdings. As with any investment fund that focuses on a single market sector versus diversifying investments across various sectors, a real estate based fund will be less diversified and therefore subject to greater risk and volatility. Further, a real estate investment fund must continue to invest only in real estate, even during periods when the performance of this market sector is performing poorly. This dependence on the real estate sector, and the risks associated with it are called real estate sector risk.
Small Company Risk	The prices of smaller company issued shares tend to fluctuate more than those issued by large companies. This higher volatility can be the result of the smaller company having greater difficulty establishing good financing or markets for their products. Also, smaller companies generally issued fewer shares which can lead to some liquidity risk. This higher volatility and exposure to liquidity risk common among smaller companies is called small company risk.
Underlying Fund Risk	Some investment funds invest in other investment funds called underlying funds. If another party that holds units in that underlying fund redeems a substantial number of units of the underlying fund, the underlying fund may have to change its portfolio significantly to meet the liquidity requirements of the redemptions. This may have a negative impact on the value of the underlying fund, and therefore on the value of the investment funds that holds units in it. The risk that activities of some unit-holders of the underlying fund may have an impact on other unit-holders of the underlying fund is called underlying fund risk.

Risk	PEPP Steps*	Accelerated Growth	Growth	Balanced	Moderate	Conservative	Bond	Money Market
Credit	Very Low - Low	Very Low	Very Low	Very Low	Very Low	Low	Low	Very Low
Currency	Very Low - Moderate	Moderate	Low	Low	Low	Very Low	Very Low	None
Derivative	Very Low - Low	Low	Very Low	Very Low	Very Low	Very Low	None	None
Equity	Low - Moderate	Moderate	Moderate	Moderate	Moderate	Low	None	None
Foreign Investment	Very Low - Low	Low	Low	Low	Very Low	Very Low	Very Low	None
Index	Very Low - Low	Very Low	Very Low	Low	Low	Low	Moderate	None
Interest Rate	Very Low - Moderate	Very Low	Very Low	Low	Low	Moderate	Moderate	Very Low
Liquidity	Very Low	Very Low	Very Low	Very Low	Very Low	Very Low	None	None
Real Estate	Very Low	Very Low	Very Low	Very Low	Very Low	Very Low	None	None
Small Company	Very Low	Very Low	Very Low	Very Low	Very Low	Very Low	None	None
Underlying Fund	Very Low - Low	Very Low	Very Low	Very Low	Very Low	Very Low	Very Low	None

* PEPP Steps carries variable levels of risk because it is a lifecycle investment fund made up of 13 steps. Members enter the fund at the step that matches their age, and then are automatically moved into more conservative asset mixes as they progress through the age bands.