

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15

Q: Reference: Page 46, Lines 1-2

Please provide documentation from Mercer for the 3.2% U.S. ERP cited.

A: A copy of the requested documentation is attached.

Bill Cannon

1
2
3
4
5
6

From: Stapleford, Rob [Rob.Stapleford@mercer.com]
Sent: June 15, 2007 8:18 AM
To: Bill Forbes; cannonw@queensu.ca
Cc: Assaf, Sofia; den Heyer, Martin
Subject: RE: A Favour
Attachments: Understanding_the_Equity_Risk_Premiums_%2825_07_2002%29.pdf

Hi Bill and Bill,
Hope all is well with you.

Attached please find a copy of a paper co-authored by Martin den Heyer in 2002 on the Equity Risk Premium. I hope that you find this to be helpful background information.

Mercer must make assumptions about the ERP for a number of applications including asset mix analysis using asset/liability modeling tools, setting the discount rates for pension funding and return on assets for pension accounting work. The Retirement and Investment practices have developed a tool that is updated monthly to reflect current economic parameters that we use for these purposes. The ERP is one of the assumptions that this tool utilizes. We develop normal, conservative and optimistic assumptions that provide consultants with a range of assumed expected returns to respond to client perspectives on this assumptions. Most of the time we focus on the Normal ERP which would represent Mercer's reasonable expectation of the ERP.

The following comments summarize the current (April 30, 2007) assumed ERP and range of assumptions at Dec 31 for each of 2003, 2004, 2005 and 2006 plus the April 2007 assumption for each assumed ERP. As you can see, the current assumption is near the low end of the range for the ERP in part, recognizing the strong performance of equity markets in recent years. The ERP is defined as the excess expected return of the equity markets over the expected yield on long term Government of Canada bonds. We use the same ERP assumptions for Canadian, US and International markets.

- Normal: 3.2% at April 30, 2007 and range of 3.0-3.8%
- Conservative: 2.5% at April 30, 2007 and range of 2.4-3.1%
- Optimistic: 4.0% at April 30, 2007 and range of 3.7-4.5%

I hope this information meets your needs. If you have any questions, please let us know.

Rob