Annual Report of the Southern Boundary Restoration and Enhancement Fund and the Northern Boundary and Transboundary Rivers Restoration and Enhancement Fund for the year 2003.

Introduction

In June of 1999, the United States and Canada reached a comprehensive new agreement (the "1999 Agreement") under the 1985 Pacific Salmon Treaty. Among other provisions, the 1999 Agreement established two bilateral funds: the Northern Boundary and Transboundary Rivers Restoration and Enhancement Fund (Northern Fund); and the Southern Boundary Restoration and Enhancement Fund (Southern Fund). The purpose of the two funds is to support activities in both countries that develop improved information for resource management, rehabilitate and restore marine and freshwater habitat, and enhance wild stock production through low technology techniques. Subject to Congressional appropriations, the United States agreed to capitalize the Northern and Southern funds in the amounts of $75 million U.S. and $65 million U.S. respectively, over a period of up to four years. The 1999 Agreement also established a Northern Fund Committee and a Southern Fund Committee, each comprised of three nationals from each country, to manage the funds.

Committee Members

<u>Northern Fund Committee</u>

Canada:

John Lubar, Co-Chair
Gord Zealand
Ron Fowler

United States:

Jim Balsiger, Co-Chair
Kevin Duffy (David Bedford)
Jev Shelton

<u>Southern Fund Committee</u>

Canada:

Ron Kadowaki, Co-Chair
Don Hall
Bill Otway

United States:

Rollie Rousseau, Co-Chair
Larry Rutter
Don Sampson (Olney Patt)

Executive Summary

- Northern and Southern Fund Committee members met jointly six times in all; twice in-person, three times via conference call and once via a combined in-person and conference call meeting.

- There was a recovery in equity markets in the latter part of a year that had started with negative first quarter returns.

- Total contributed capital (nominal) at year end was $CDN 209,796,000 or $US 140,065,000. Actual fund asset value at December 31st was $CDN 200,393,000 or $US 155,055,000. The discrepancy between the cumulative deficit of $CDN 9,403,000 and cumulative surplus of $US 14,989,000, is due to the relative currency valuations. (See Appendix).

- In June 2003, the last US cash installment of $CDN 55,439,871 or $US 39,740,000 was added to the Fund.

- The selection of a new global value manager, Brandes Investment Partners, was approved by the Joint Committee in March.

- On the U.S. section, David Bedford and Olney Patt were appointed to the Northern and Southern Fund Committees respectively, replacing Kevin Duffy and Don Sampson.

- The Fund Coordinator began a part-time secondment with the Pacific Salmon Foundation in Vancouver, B.C. in February, 2003.

Committee Meetings

The Northern and Southern Fund Committees have agreed that given the congruent nature of their agendas and their decision to combine the funds into a single master account for investment management purposes, and the efficiencies involved with respect to interaction with the fund managers, it was appropriate to meet together as a Joint Fund Committee at least until such time as the two committees begin to fund projects in their respective areas. Thus the Joint Fund Committee met in person on two occasions (June 2, 2003 and November 4-5, 2003) and by telephone conference call three times (March 14, 2003. May 5, 2003 and September 12, 2003), and once in a combined in-person and conference call arrangement (February 14, 2003). In addition, a four person Global Value Manager Search Sub-Committee met once in person (January 13, 2003) and once via conference call (March 6, 2003).

The Joint Committee's first meeting in 2003, a combination conference call and in person meeting, was held in Portland, Oregon on February 14th, 2003. Perry Teperson of Hewitt and Associates provided an assessment of a reply to a letter sent to the Funds' US equity managers MFS Investment Management (MFS) in December, 2002 regarding access to a pooled fund investment vehicle so as to reduce the high fees currently paid to MFS by the Fund. It was agreed to respond to MFS expressing dissatisfaction with their reply. A report was given on progress in the search for a Global Value Manager and the search sub-committee agreed to meet again for further discussion.

The second meeting of the year was held via conference call on March 14th, 2003. The Global Value Manager search sub-committee recommended that Brandes Investment Partners be chosen and a motion was passed confirming the selection. A draft letter to MFS was reviewed and changes suggested. Hewitt and Associates were instructed to prepare suggestions of alternate investment management firms.

A dollar cost averaging strategy was discussed as a possible strategy for the anticipated last US funded installment into the Fund.

The third meeting of the year was held via conference call on May 5th, 2003. The dollar cost averaging strategy was further debated with the general consensus being that a 6 month phase-in period with Brandes would be suitably conservative and risk averse given the prevailing market conditions. A motion to this effect was passed unanimously. Hewitt and Associates agreed to prepare a discussion document suggesting alternative investment management firms to MFS for consideration at the next meeting.

The fourth meeting of the year was an in person meeting held on June 2nd, 2003. There was a brief discussion on the operating budget. Hewitt and Associates presented their first quarter report, in which the Fund returned a disappointing –8.3% and some attention was paid to the influence on the Fund of the strong Canadian dollar. On the subject of MFS, Hewitts' recommendation was to not fire the firm because they were performing acceptably in a difficult market environment and an adequate period of time had not elapsed in order to afford a fair evaluation of the manager's performance. A majority of the Committee agreed with this analysis. A debate on active and passive Bond manager alternatives followed. The meeting closed with a review of a spreadsheet model forecasting potential funding scenarios under a variety of different financial assumptions.

At the fifth meeting held by telephone conference call on September 12th, 2003, Hewitt and Associates presented their second quarter report, noting that equities had rallied during the quarter and the bond portfolio had performed well. The pro's and con's of the MFS pooled fund option were debated. The active vs. passive bond issue debate was deferred to a later date. Some potential topics for discussion at the upcoming annual Fund Manager reviews in November were discussed.

The last meeting of the year was marked by the annual Fund investment manager performance report and interviews held at the PSC office on November 4th and 5th, 2003. The Committee was generally satisfied with the performance and report from Barclays Global Investors. The interview with Putnam Investments led to a very lengthy debate concerning the company's recent difficulties with U.S. mutual fund regulators. In particular, the Committees were very concerned about the discoveries of unethical trading activity by both clients and key staff of Putnam. Senior staff changes and uncertainty about the potential impacts on future returns that might result for existing and prospective investors created by Putnams' improprieties were also a significant concern. Since the situation with Putnam had only come to light just prior to the meeting and it appeared that steps were being taken by the company to rectify the situation, a decision was made to retain Putnam for the moment and to request additional information for consideration by the Committees in January. The committees were satisfied with the report and performance of Brandes Investment Partners. The interview with MFS also triggered vigorous debate, but this time concerning the company's performance, the outcome of which was a decision to retain the firm and re-evaluate in November 2004. In the meantime staff were instructed to initiate a transfer of assets from the MFS segregated account into an available pooled fund, to benefit from a saving in management fees.

It should be noted that due to the status of the Funds' investments, no discussion was held related to fund expenditures in support of restoration and enhancement activities.

Global Value Manager

A global value manager hiring sub-committee was struck on August 16th, 2002. On the committee representing the Southern Fund were Rollie Rousseau and Bill Otway and for the Northern Fund Jev Shelton and Ron Fowler. The hiring sub-committee held an in person meeting in Vancouver, BC on January 13th, 2003 (Larry Rutter substituting for Rollie Rousseau) at which four potential global value managers were interviewed.

The four firms interviewed were Morgan Stanley, Sprucegrove, Templeton and Brandes Investment Partners.

A conference call was held on March 6th, 2003 at which Brandes Investment Partners were chosen unanimously.

Investment Review

Equity markets at the beginning of 2003 had been falling for three consecutive years and with the threat of a war in Iraq looming, negative first quarter returns were recorded in all major asset classes held by the Fund.

With the worst fears for the consequences of war in Iraq not realized, the second quarter saw a modest recovery on the equity markets, but both Putnam and MFS performed poorly relative to benchmark.

Signs of economic recovery around the world lifted investor confidence and equities had a strong third quarter. Brandes Investment Partners did well, but Putnam and MFS performed weakly.

By the end of the year there was evidence of a global recovery beginning to build. As confidence returned, equity markets rose sharply. While the improvement in the fortunes of the global economy and the sharp turnaround in corporate profits have boosted the markets, they remain unsure whether the recovery can be sustained. Investors' main concern is that the world economy remains in much the same shape as it was before the slump and is still dependent on the US consumer. The US economy remains the engine of global growth. Consequently, the global economy remains vulnerable should the US economy stumble.

Total contributed capital (nominal) at year end was $CDN 209,796,000 or $US 140,065,000. Actual fund asset value at December 31st was $CDN 200,393,000 or $US 155,055,000. The apparent discrepancy of a cumulative deficit of $CDN 9,403,000 and a cumulative surplus of $US 14,989,000, results from the performance of the Canadian and U.S. currencies over the life of the Funds.

Contributed capital and asset value of the individual Funds as of December 31, 2003 stood as follows:

	Contributed Capital		**Asset Value**	
Northern:	$CDN 111,919,531	$US 75,000,300	$CDN 106,856,341	$US 82,712,227
Southern:	$CDN 98,164,491	$US 65,065,300	$CDN 93,536,381	$US 72,401,902

Committee Appointments

Olney Patt replaced Don Sampson on the Southern Boundary Restoration and Enhancement Fund Committee, U.S. section in November 2003. David Bedford replaced Kevin Duffy on the Northern Fund Committee, U.S. section at the same time.

Fund Coordinator

In view of the poor economic climate and given the very gradual recovery of the Fund and the resulting unlikelihood that the funds would be supporting projects for some time, it was agreed that as a cost saving measure and as an opportunity for professional development, Angus Mackay the Fund Coordinator would take an initial 6-month part-time secondment with the Pacific Salmon Foundation in Vancouver BC, starting in February 2003. This was subsequently extended for a further 6 months.