# Contents

**Raoul Briet** Chairman, Supervisory Board
**Francis Mayer** Chairman, Executive Board

# Message

FROM THE CHAIRMEN OF THE SUPERVISORY AND EXECUTIVE BOARDS

With the due caution that is required of the long-term investor and having acquired sufficient hindsight, it is now possible to make an initial financial assessment of the investments made by the FRR in connection with the mission that was entrusted to it by public policymakers. The results so far are very positive. At the December 31, 2005 reporting date, the FRR's net asset value was 26.65 billion euros. The management result, which is total investment income net of expenses and unrealized capital gains on invested assets, was 2.79 billion euros on the same date. This means that the FRR's performance during the year ended was 12.4% net of expenses, which is 10 points higher than the risk-free rate of return on assets. Looking at the portion of its assets actually invested in marketable securities (i.e., stocks and bonds, excluding money market instruments), the total return was 19.1% last year. In eighteen months, since the Fund made its first investments in the summer of 2004, the FRR has achieved a global performance of 15.9%, and the return on invested assets is 29.2%.

The FRR was able to take full advantage of the excellent conditions that prevailed in the equity markets last year, particularly within the euro area, which is where most of this performance originated. While it is not repeatable, and the European as well as the global economic and financial environment that is shaping up in 2006 is not free of risks, this performance does provide a solid base of support on which the Fund can build subsequent investments in asset classes already represented in the portfolio. In particular, this applies to fixed-income instruments, for which a deliberately cautious stance was adopted in 2005 in light of excessive market prices.

Overall, three-fourths of the FRR's portfolio has been invested in eighteen months, without any operational difficulties. Naturally, this process will continue throughout 2006, financial market


trends permitting. In addition, the Fund will make its first foray into private equity investments, as soon as the RFP currently under way has been completed.

The end of 2005 was also marked by a triple consolidation:

– that of the role of the FRR in the vital and necessary system set up to begin preparing for the future financing needs of France's general old age pay-as-you-go insurance plan, as attested to by the fact that public policymakers have decided to give the Fund an additional sum of 3.1 billion euros to manage, owed by the electric and gas industries to the CNAV Old Age Fund *(Caisse nationale d'assurance vieillesse)*;

– that of the Fund's identity as a long-term investor, which strives to manage in accordance with collective values that serve and promote balanced economic, social and environmental development via, in particular, an active policy of voting proxies, which went into force in 2005; the launching of a major RFP aimed at selecting asset managers specialized in integrating the extra-financial criteria defined by the Fund into their investment processes; and the FRR's participation in French and international initiatives which promote socially-responsible investment principles and practices, such as that initiated by the UN;

– that of its newly adapted organization, which is achieving greater control over its costs by using best market practices as a benchmark.

Thanks to these developments, we are particularly confident in the ability of the FRR and its staff to continue to rise to the challenges inherent in the demanding mission that has been entrusted to them by public policymakers.

# Financial markets evolution

**Macro-economic environment: economic expansion continues in 2005 in spite of uncertainties**

In 2005, the recovery that began in the spring materialized in vigorous fashion in Asia, the United States and within the euro area, which this time around was able to take full advantage of the more buoyant global environment.

The business conditions that prevailed in 2005 provided proof in and of themselves of the exceptional ability of economies to resist sharply rising commodity prices, in particular oil prices, which rose substantially for the third year in a row. The good financial health of the developed world's businesses and banks, not to mention the positive monetary and financial conditions that prevailed throughout 2005 — including the stabilization of currency markets — undoubtedly made it easier for the world's economies to absorb higher production costs and the erosion in purchasing power caused by rising energy costs. The persistence of high oil prices in 2005 neither pushed the global economy into recession nor prevented a vigorous recovery from unfolding.

This backdrop enabled the central banks to gradually get over their fear of deflation and begin dealing more seriously with emerging inflation risks. While the pace of inflation, excluding energy prices, was particularly moderate in the various regions of the world, inflationary pressures nonetheless built up, justifying central bank decisions to pursue monetary tightening in the United States, to begin raising key rates in the euro area and, as was announced in Japan, to put an end in the fall to that country's heterodox monetary policy.

**The financial markets: an excellent harvest in 2005**

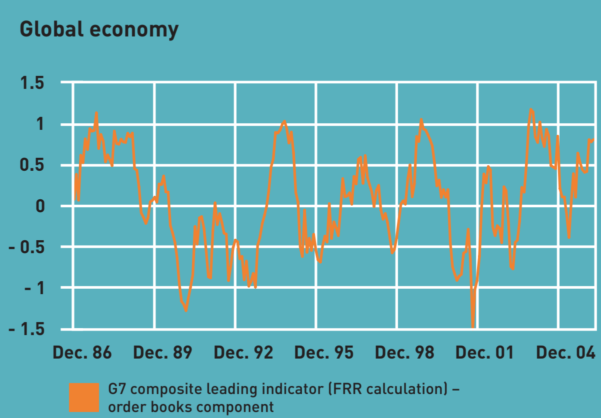
**Balance restored to currency market**

The return to stability of the currency market in 2005, including the dollar's 7%-10% reappreciation versus its principal partner currencies, helped to achieve more balanced global growth last year. Undoubtedly, the main beneficiary of this improved situation was the euro area. This more balanced exchange parity picture was mostly due to the clearly expressed desire on the part of G7 finance ministers and central bankers to cooperate in the effort to resolve the unbalanced financing of global growth. China also made steps toward greater cooperation in July 2005, when it took steps to make its exchange rate system more flexible.

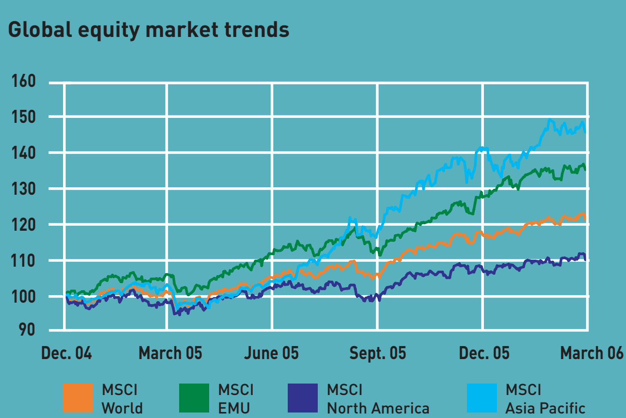
**Equity markets buoyed by attractive valuation levels**

The dollar's rise against the euro served as a catalyst to appreciation in the European equity markets, for which 2005 was again a very good year. On the year, the gain was more than 20% for the DJ Euro STOXX 50 index. In addition to support from the dollar, Europe's equity markets also got a boost from European corporations, whose healthy balance sheets and high profitability led to remarkable earnings growth.

**Economic expansion faced bumps in 2005**




**2005: a good year for the equity markets**



The prospects for a lasting rebound in domestic growth within the euro area were taken by investors as yet another sign of encouragement working in favor of European equities, further supported by the intensity with which Europe's corporations restructured in 2005, an effort that led to news of a number of merger and acquisitions in the pipeline.

Investors — most of them non-residents — flocked to Japanese equities, as the Japanese economy appeared to be on the verge of emerging from a long period of deflation and the Bank of Japan began sending out a steady stream of positive news flow. The undeniable return to economic growth and corporate profitability, against a backdrop of unprecedented restructuring in the Japanese banking system, provided more than enough support for the exceptional performance of the Japanese equity market, which gained more than 45% in 2005 (TOPIX index).

While the expansion of the American economy, which grew slightly faster than its long-term potential, continued throughout 2005, the US equity market trend was not nearly as spectacular as its European or Japanese counterparts, with the full-year gain reaching only 3.5% after having fluctuated within a particularly broad range.

**As short-term rates rose, long-term yields remained stubbornly low throughout 2005**

Although all of the factors that traditionally lead to higher yields were present as of the end of 2004, the yield on 10-year treasuries remained low (between 4.0% and 4.6%) in the United States and even fell in the Euro Area (from 3.7% at the beginning of the year to 3.3% at year-end).

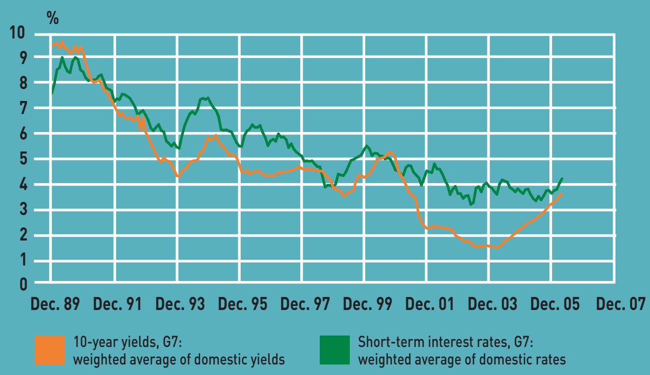
Long-term yields showed signs of weakness twice over the course of 2005. In June, US yields bottomed out at 3.9%, while their European counterparts fell to an annual low of 3.1%. Then, in September, US long-term yields again dropped, to 4.0%, while their European counterparts reached their lowest point of the year (3.0%).

In addition to the gradual dissipation of uncertainties about the sustainability of growth, the central banks began communicating their clear intention of normalizing monetary policy to avoid the risk of a resurgence of inflation. The combined effect of these two factors was enough to produce slightly higher long-term yields by the end of the year. However, in spite of this increase, long-term yields finished out the year 2005 at levels that were below their fundamental value, which was not the case for bonds with short or intermediate maturities. Yields on these instruments rose in line with central bank key rate hikes.

The correction that observers were expecting in the bond markets never materialized in 2005. On the contrary, these markets generally turned in honorable performances throughout the year, although they came nowhere near to competing with returns on display in the equity markets.

**Long-term yields remain low despite rise in short-term rates**

**G7 short- and long-term interest rates:**



# Portfolio activation

**The FRR's investment strategy: continue stepping up investment, differentially by asset class**

In the course of 2005, the FRR continued to step up its portfolio investments, in compliance with the principles that were laid down at the outset of this process:

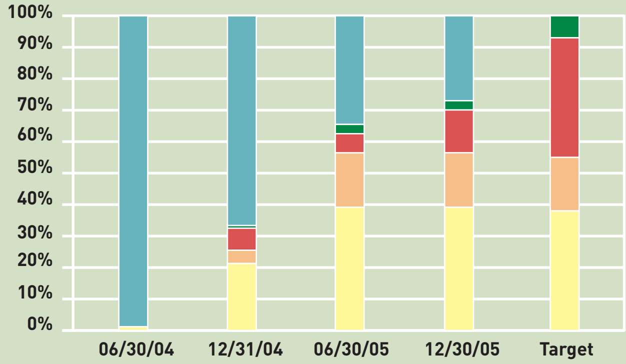
- insofar as possible, spread out and time the acquisition of the various types of securities comprising its initial portfolio to ensure sufficient diversification in terms of purchase prices;
- give preference to asset classes whose valuation, as measured by an analysis of fundamentals, appears relatively higher over a medium- to long-term horizon. Conversely, postpone or increase the intervals on investments in asset classes that are overpriced compared to their estimated equilibrium price;
- insofar as the two aforementioned principles permit, obtain sufficient diversification of the portfolio by investing in as broad a spectrum of asset classes as possible, in order to reduce the exposure of its total return to one or more shocks that are specific to a particular type of security.

After having given preference in 2004 to investments in European equities, and more particularly to mid-caps, the FRR pursued its strategy of stepping up the pace of its investments in 2005, completing its exposure to equities and also sequencing its investments in bond mandates.

All of the FRR's equity mandates, with the exception of standby mandates, which had not yet been activated by year-end 2004, were launched in early 2005. Consequently, the FRR's target equity allocation of 55% of total net assets was reached in the first six months of the year. This target was maintained when the electrical and natural gas industries entrusted a cash payment to the FRR for investment, through a wave of additional investments made in the spring of 2005. Positive market trends observed starting in the second quarter of 2005 brought exposure to the equity markets slightly higher than the medium-term target (56.4% of the FRR's NAV at June 30, 2005), a level that was maintained throughout the second half of the year. Conversely, the Fund remained very conservative with respect to investments in euro-bond mandates, as fixed-income products continued to show valuation levels deemed very high over a medium-term investment horizon. Against this backdrop, mandates awarded to euro and international bond specialists were only gradually and conservatively activated as market conditions permitted, rising from 9% to 16.6% over the course of the second half of the year.

In addition, in the interest of minimizing risk in the international component of the global portfolio, a policy of hedging against the currency risk was rolled out concomitant to the activation of the first non-euro mandates in the fall of 2004. The aim of this policy is to protect between 80 and 100% of the exposure to non-euro currencies by setting up appropriate hedges.

**Analysis of FRR's total assets**




| | 06/30/04 | 12/31/04 | 06/30/05 | 12/30/05 | Target |
|---|---|---|---|---|---|
| Cash and equivalent | 98.8% | 66.7% | 34.5% | 27.0% | 0.0% |
| Non-euro bonds | 0.0% | 0.8% | 2.9% | 2.9% | 7.0% |
| Euro bonds | 0.0% | 7.0% | 6.1% | 13.7% | 38.0% |
| Non-euro equities | 0.0% | 4.2% | 17.3% | 17.2% | 17.0% |
| Euro equities | 1.2% | 21.3% | 39.2% | 39.2% | 38.0% |

**Composition by macro-asset class at year-end 2005**

| | In € billions | In % |
|---|---|---|
| Euro bonds | 10.4 | 39.2% |
| Non-euro equities | 4.6 | 17.2% |
| Bonds | 4.4 | 16.6% |
| Money market (including currency hedges) | 7.2 | 27.0% |
| **TOTAL** | **26.6** | **100%** |

**The experience of working with a transition broker is a positive one for the FRR**

In the course of 2004, and concomitant to the asset manager selection process, the FRR launched an RFP to select a transition broker. Inspired by the experience of a number of large foreign pension reserve funds, this was the first decision of its kind in the French asset management market.

The FRR decided to use a transition broker in order to complete the entire series of transactions required to build its portfolios within tight timeframes, involving substantial volumes of cash and financial instruments, and under optimal conditions of confidentiality. In addition, the decision to use the services of a transition broker was based on a desire to reduce the global cost of implementation traditionally associated with the construction of a particularly large portfolio of financial instruments. It was also made to facilitate the settlement/delivery flow by simplifying the process of reconciling positions with the custodian and by reducing the number of settlement instructions. Finally, using a transition broker helps to achieve complete control over the transition through detailed and frequent reporting that allows the FRR to constantly monitor the exposure, trading process, costs and performances related to each one of its portfolios.

When the RFP process was completed in July 2004, Goldman Sachs was selected to serve as the FRR's transition broker. In the space of sixteen months — between September 2004 and December 2005 — transactions valued at more than 13 billion euros were negotiated. Of the total, 10 billion euros involved equities and 3 billion euros involved bonds.

By using the services of a transition broker, the FRR was able to:

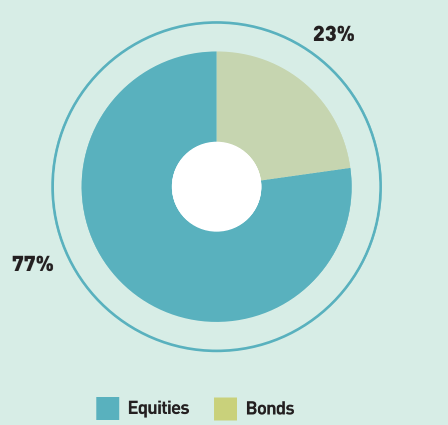
- complete substantial volumes of transactions in short periods of time (on average, three days for equity trades, for example);
- complete these transaction under stringent conditions of confidentiality, as the Fund's build-up was not the subject of market disclosures at any time;
- complete these transactions at lower cost than would have been possible without the intervention of this service provider;
- facilitate settlement and delivery as expected by centralizing transactions, aggregating transactions to limit the number of lines, and acquiring the capability to track settlement flows in real time;
- maintain complete control over transactions during the investment step-up phase by holding preparatory meetings with asset managers prior to transitions, coordinating the various parties involved in these transactions (managers, custodian, overlay manager) and performing pre-trade surveys and post-trade reporting.

# Portfolio composition

## at December 31, 2005

On December 31, 2005, after new mandates had been activated and additional funds made available for investment, the FRR's invested portfolio (excluding activity related to the overlay manager) was distributed as follows: 15 billion euros invested in European, US and Asian equities, and 4.4 billion euros invested in European and international bonds, both nominal and inflation-linked.

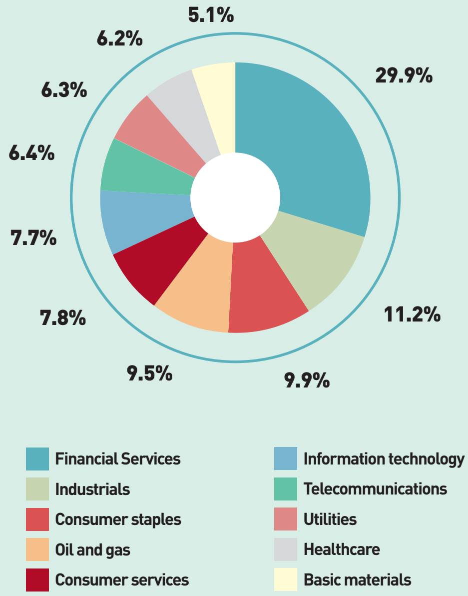
**Analysis of invested assets by class: equities/bonds**




On December 31, 2005, the fair market value of the FRR's equity portfolio was 15.024 billion euros. In geographic terms, and in descending order of importance, this portfolio was principally exposed to the French, US, German, Spanish, Italian and Dutch stock markets. The allocation to French equities, which largely exceeded the relative weight of French market capitalization (the FRR's allocation in French equities was 22%, whereas the market capitalization of the Paris Bourse is equal to 4% of total market capitalization worldwide) was primarily the result of deliberate overweighting to the euro area in the FRR's strategic allocation.

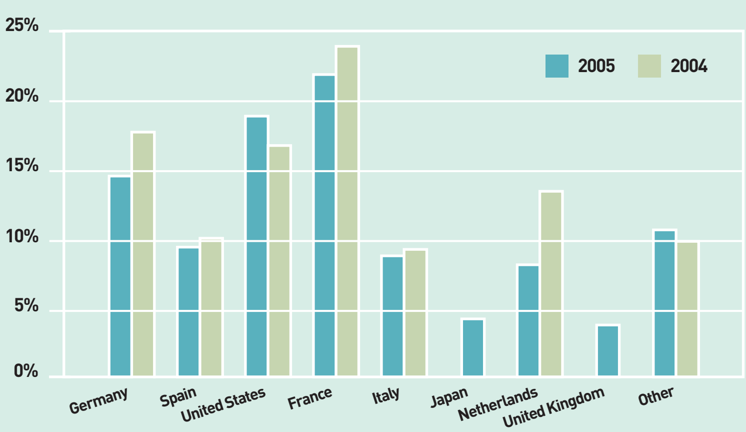
The change made to this allocation in 2005 reflects the decision to activate a number of different mandates throughout the year, in particular Pacific Rim equities (including Japan and excluding emerging countries) and

**Analysis of equity investments by sector**

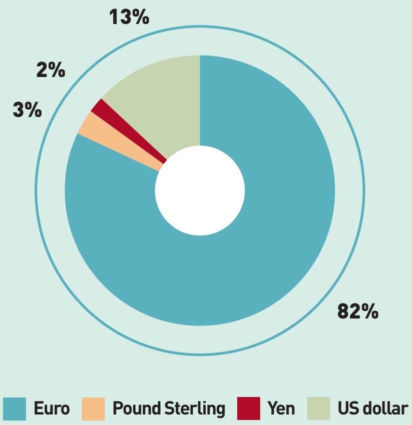



European equities (excluding euro area mandates), as attested to by the inclusion of both Japan and the United Kingdom in the 2005 asset allocation. Analyzed by sector, the portfolio was principally invested in financial

**Change in equity investments by country**




**Analysis of fixed income assets by currency**



services, industrials and consumer staples at the year-end reporting date in 2005. For the most part, it reproduces the composition of the benchmark indices — which serve to measure manager performance — for each mandate.

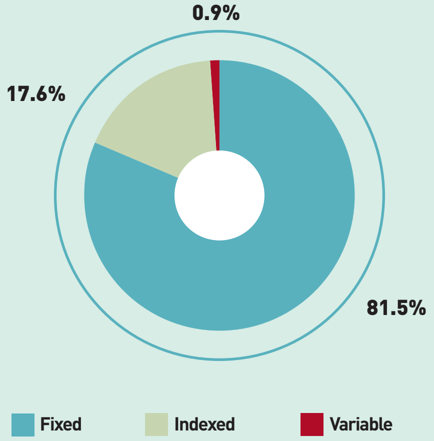
On December 31, 2005, the fair market value of the bond portfolio was 4.404 billion euros.

The bond portfolio was primarily invested in euro bonds, and its distribution in terms of currency was very close to the benchmark index for activated mandates.

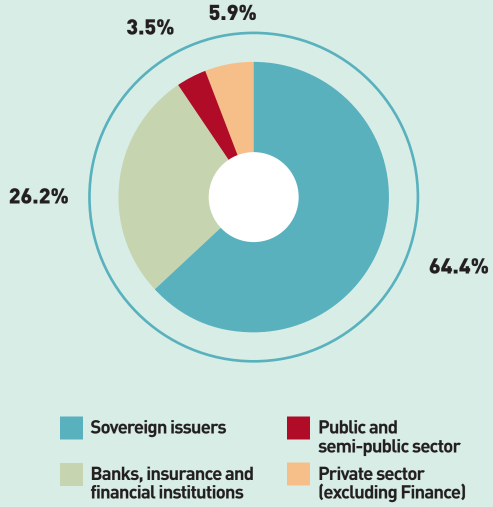
On December 31, 2005, just under 18% of the bond portfolio was invested in inflation linkers, while the remainder was almost exclusively invested in nominal, fixed-income bonds. The percentage invested in floating rate instruments — included in the investment universe of managers but not represented in their benchmark index — was marginal. A substantial proportion (25.5%) of the bonds in the portfolio on December 31, 2005 had maturities that exceeded fifteen years, reflecting the composition of the benchmark indices, which were constructed to ensure consistency with the extended duration of the FRR's liabilities.

Close to 65% of the bond portfolio was composed of sovereign issues. This percentage is significantly higher than the benchmark indices of the activated mandates.

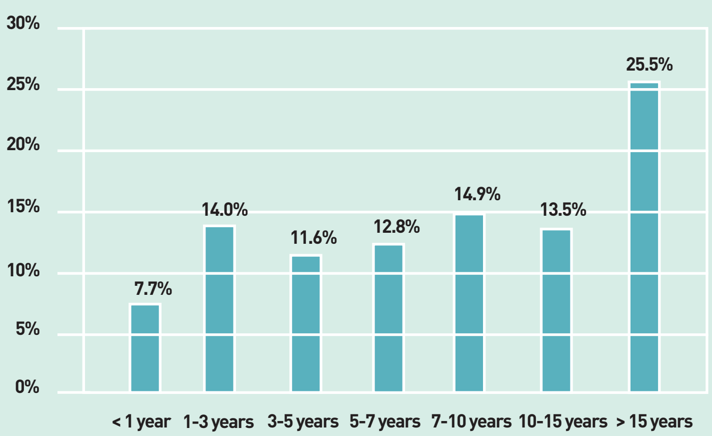
**Analysis of fixed-income products by benchmark**



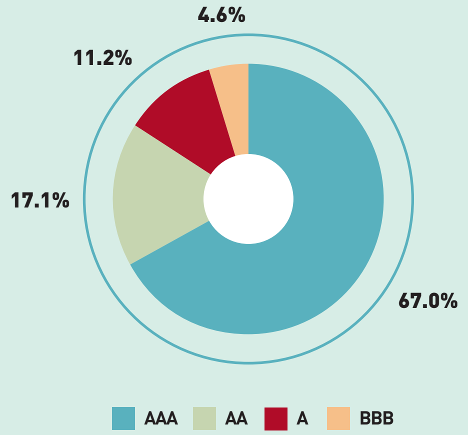

**Analysis of fixed-income products by type of issuer**




**Analysis of bond portfolio by maturities**




**Analysis of bonds by rating**



# Managing the tactical allocation and currency risk

Institutional investors may delegate three types of mandates to asset management firms: the management of equity funds, the management of bond funds and the management of what are known as diversified funds. For funds of this type, the allocation of invested assets between equities and bonds is managed, but for only some of the invested assets and independently of what may occur in one or the other compartment. Another approach involves entrusting management to specialists with expertise in specific asset classes, with assets allocated globally and transversally. The currency risk can also be managed at the global level, in transversal or "overlay" fashion. The FRR has opted to use this approach for its tactical allocation and currency risk management needs. The FRR has also decided to maintain responsibility for defining the tactical positions taken while totally delegating both the implementation of these decisions and the management of its currency risk.
After an RFP process was completed, the FRR selected State Street Global Advisors to handle both of these tasks as of 2005.

## The approaches selected by the FRR

### The need for tactical asset allocation

In the interval between two adjustments to the strategic allocation, decisions of a tactical nature pertaining to asset allocations are necessary for at least two reasons. First of all, significant market movements and anomalies frequently shift the actual percentage of various asset classes away from their initially determined strategic weighting. These changes in the asset balance place the portfolio at greater risk and are a source of under- or over-performance.
Secondly, it appear to be inefficient to maintain the portfolio's initially determined strategic asset allocation relative weightings during periods of obvious under- or over-valuation in the financial markets, during specific phases in the economic cycle, or if certain inflation scenarios materialize. Market valuation, economic cycle position and inflation cycle position are the three fundamental factors that underlie the FRR's tactical allocation philosophy.
In this way, tactical allocation can provide a source of additional value creation that is not correlated to the rest of the portfolio.

### Overlay management of the currency risk

The FRR defines the concept of transversal or "overlay" management as the process whereby the global currency exposure of its portfolio is managed separately from the underlying financial assets that have generated the exposures to various currencies, by a specialized manager with a dedicated risk budget.

## How the FRR's currency overlay management program works

### Advantages and workings of the tactical process: a pragmatic approach to rebalancing the portfolio's investments

The FRR's tactical program involves implementing its tactical allocation through the use of simple derivatives, futures contracts, which provide an opportunity for exposure to the financial markets without necessarily physically holding the underlying financial asset. The rationale behind this way of working is twofold: the FRR does not have good visibility over its inflows and hence cannot count on a steady supply of fresh resources to fund its allocations. At this time, the FRR cannot reallocate all or some portion of the physical assets it has entrusted for management under mandates for as long as these mandates remain in force.

The FRR's tactical horizon spans a period of from six to nine months, compared with many asset management firms, whose investment horizon is less than three months. Most of the time, decision-making involves a pragmatic rebalancing of the physical asset positions in the FRR's portfolio toward the target percentages of its strategic allocation. This means that the FRR may take no asset risk for a certain period of time. But in specific situations, it is also ready and willing to take an asset allocation risk — around periods of clear economic cycle reversal and when significant valuation gaps in the market have been confirmed, but after having adjusted for risk factors that include investment flows, investor positions and the short-term dynamics at work in the market.

Overall, this is a qualitative decision-making process based on quantitative tools. It requires the development of situational views and an analysis of market valuation models. The degree of latitude that the Supervisory Board of the FRR has granted to tactical allocation allows a maximum deviation from the assigned strategic equity weighting of plus or minus 6%.

**How the currency risk is hedged: a two-step process**

The first step consists of passively managing the currency risk as the FRR steps up its investment program. The hedge ratio is set at 90% for each currency, although it may be changed temporarily if the FRR detects a clear risk for any particular currency.

The second step generally involves a shift to active management of the currency risk: the ratio will shift actively within a range of 80-100%, based on market trends or expectation scenarios, and the responsibility for these shifts will be placed entirely on the manager. The FRR expects to integrate active currency risk management operationally in 2006.

Pragmatism, driven by the power of sophisticated quantitative tools and a unique partnership maintained through daily contact with managers, forms the foundation for the basic principles and decisions made in connection with these missions. This same spirit of pragmatism ensures a great deal of flexibility to act in accordance with market trends while also seeking to generate, over the long term, additional performance related to measured risk, calibrated through ongoing management adjustments.

To achieve this aim, the FRR maintains a close and unique relationship with the asset managers selected. The latter play an advisory role in all allocation decisions, execute the decisions made by the FRR by carrying out investments in the markets on its behalf and monitor transactions to ensure compliance with these decisions.

# Global performance and performance of financial strategies

**Performance of FRR assets in 2005**

**The Fund's asset structure is gradually being brought into alignment with the strategic target that was set by the Supervisory Board.**

The data in the table below is rounded off and expressed in absolute value terms:

| Assets in € bn | 06/30/04 | 12/31/04 | 06/30/05 | 12/30/05 |
|---|---|---|---|---|
| Cash | 16.6 | 12.8 | 8.1 | 7.2 |
| Non-euro bonds | 0.0 | 0.2 | 0.7 | 0.8 |
| Euro bonds | 0.0 | 1.3 | 1.4 | 3.6 |
| Non-euro equities | 0.0 | 0.8 | 4.0 | 4.6 |
| Euro equities | 0.2 | 4.1 | 9.2 | 10.4 |
| **TOTAL** | **16.8** | **19.2** | **23.4** | **26.6** |

The FRR's net asset value was 26.6 billion euros at year-end 2005. During the year, net assets grew by 7.4 billion euros, of which 4.6 billion was attributable to new inflows to the Fund.

**FRR's global performance**

In 2005, the FRR's global performance was a very satisfactory 12.6% return on invested assets, which is 10 percentage points above the risk-free rate of return. Net of all expenses, this global performance was 12.4%.

During the year, assets invested in marketable securities provided a net return of 19.1%. It should also be noted that, on average, these assets invested in marketable securities outperformed their benchmark indices.

Since the start of the management phase in late June of 2004, the FRR's global performance figure is 15.9% (15.65% net of all fees), and net performance of assets invested in marketable securities is 29.2%.

Performance was largely driven by returns on equity investments in general and euro area equities in particular. Generally speaking, as equity mandates were activated, a process that was completed in March of 2005, the portfolio took advantage of market appreciation. For the full year 2005, European equities accounted for nearly three-quarters of the FRR's performance, while its investment in this asset class represented 38% of the Fund's total assets.

Bonds made a more marginal contribution to performance, the FRR having made the tactical decision to defer the activation of bond portfolios in light of the historically low yields that prevailed throughout 2005.

Taken as a whole, the tactical allocation and currency

**Analysis of performance (gross of fees) per asset class and average weight of these asset classes during the year**

| | Contribution to performance | Average weight |
|---|---|---|
| TOTAL PERFORMANCE | 12.58% | |
| **Total equities** | **12.45%** | **50.4%** |
| European equities | 9.27% | 38.2% |
| of which euro area | 8.62% | 35.5% |
| of which excluding euro | 0.65% | 2.7% |
| North American equities | 2.05% | 9.4% |
| Pacific Rim equities | 1.13% | 2.7% |
| **Total bonds** | **0.88%** | **11.2%** |
| Euro bonds | 0.39% | 6.6% |
| Indexed bonds | 0.25% | 2.4% |
| International bonds | 0.24% | 2.2% |
| **Cash** | **0.87%** | **38.4%** |
| **Overlay and tactical management** | **–1.62%** | **0.5%** |

risk activity generated a counter-performance of -1.6%, attributable to currency hedging transactions. It should be noted that the aim of this activity is to globally neutralize the impact of currency fluctuations on the portfolio, and that the negative performance was offset by a positive exchange rate impact of a similar magnitude on the performance of mandates invested in [other] currencies.

### Global risk

This performance was achieved without generating excessive risk, as we can see by looking at two complementary indicators — the beta coefficient and the VaR (value at risk).

At the December 31, 2005 reporting date, the beta coefficient (which measures the correlation between changes in the benchmark and the value of the portfolio) was 1.1. This means that any variation of x% in the level of the benchmark leads to a 1.1x% variation in the value of the portfolio.

VaR measures the maximal risk of loss in the theoretical, hypothetical event that the portfolio is liquidated in one year, with a 95% probability of occurrence. At year-end 2005, this risk of loss was 18% of the value of the portfolio on this same date. The magnitude of this risk can be compared to the percentage of unrealized capital gains in the equity portfolio on this same date, which was around 15%.

### Financial strategy performance

On the December 31, 2005 reporting date, 23 asset management mandates had been activated, of which 18 equity mandates and 5 bond mandates. Four of them were being managed passively and 19 actively (this refers to bond mandates in particular).

The first investment portfolios were constituted in June 2004. On December 31, 2005, the duration over which management was implemented was still relatively short, within a range of two to eighteen months. Taken as a whole, the average duration of these mandates was around twelve months. Readers are advised to keep this in mind when assessing performance differentials versus the benchmark indices, which the FRR tracks on a regular basis. This indicator is not yet a salient one, and should not be used to draw hard and fast conclusions about the performance of the FRR's asset managers.

Since their start-up dates, the asset management strategies put in place have provided positive performances as measured in absolute terms. These aggregate performances are between 8.7% and 51.2%. The strategy that produced the highest return was that put in place within the euro area mid-cap equities lot (51%), illustrating the outperformance of mid-and small-cap stocks over large caps within this geographic region. As for euro area large-cap equity strategies, they provided a return that was also highly satisfactory (more than 33%). Similarly, Pacific Rim equities, excluding emerging countries, recorded the best performance outside the euro area (40%), consistent with the strong performance of the developed Asian nations in general and Japan in particular.

US equities and non-euro European equities (the latter mainly represented by the UK market) under-performed the aforementioned regions relatively speaking, although they provided historically high returns (23% for the US mid-caps strategy, and between 19 and 25% for US large-caps and non-euro European equities).

Finally, strategies based on bond investments got a boost from the drop in rates in the second half of 2004 and in 2005, both in the euro area and the rest of the world. These strategies provided returns of between 8.7% and 13.3%.

**Absolute performances of strategies, from start-up dates for each lot through December 31, 2005. (The start-up date for each lot is the date on which that lot's first mandate was activated).**

| | | Performance since start-up (%) |
|---|---|---|
| LOT 1 | Euro area equities, large-caps (passive management) | 33.4 |
| LOT 2 | Euro area equities, small- and mid-caps (active management) | 51.2 |
| LOT 3 | Euro area equities, large-caps (active management) | 34.4 |
| LOT 4 | US equities, large-caps passive management) | 17.6 |
| LOT 5 | US equities, mid-caps (active management) | 23.2 |
| LOT 6 | US equities, large-caps, value style (active management) | 18.9 |
| LOT 7 | US equities, large-caps, growth style (active management) | 25.4 |
| LOT 8 | Non-euro area equities (active management) | 20.4 |
| LOT 9 | Pacific Rim equities, excluding emerging countries (active management) | 40.4 |
| LOT 10 | Euro bonds, sovereign and corporate issuers (active management) | 13.3 |
| LOT 11 | International and inflation-linked bonds (active management) | 8.7 |
| LOT 12 | International and inflation-linked bonds (active management) | 9.5 |

# New requests for proposals (RFP)

**The FRR's private equity RFP**

On December 16, 2005, the FRR launched an RFP to select managers for a private equity program, the underlying principles of which had been previously approved by its Supervisory Board. The aim of this first program is to enhance the returns on Fund's global portfolio, which was constructed from a long-term perspective, and to reduce the portfolio's global risk through further diversification. Investment in private equity also makes a positive contribution to the economy by supporting business development.
Pursuant to these two objectives, the Supervisory and Executive Boards of the FRR have taken a pragmatic approach to this first private equity program, structured around four underlying principles:

**An ambitious initial investment program**

For this first program, the FRR has committed approximately 1.5 billion euros to private equity, which represents just under 6% of its current total invested assets. Taking into account the latency and timing effects involved in this type of investment, the program should result in a private equity portfolio of around 1 billion euros. Subsequent private equity programs will allow the FRR to either maintain or build on this initial investment.

The FRR has deliberately scaled this first allocation as a lump sum investment rather than as a percentage of its global allocation, in order to avoid the risk of standardizing and annualizing future allocations to this asset class.
The investment horizon for this program has been set at three to five years, with the phase of commitment to new private equity vehicles spread from 2006 to 2010, in order to diversify the harvesting timeframe of fund investments.

**An allocation deliberately tilted toward European markets**

Today, the private equity market is still tilted toward North America, the locus of two thirds of all investments in terms of volume. However, thanks to the growing maturity of the European markets, and in particular the French market, in terms of both depth (the number and quality of potential targets, transactions completed and intermediation) and the professional caliber and experience level of private equity investment professionals, European institutionals can overweight their local region during the portfolio construction phase. The FRR has opted for a strong tilt in favor of Europe, allocating between 60 and 65% of its program to investments in this

**LOT 1 Diversified private equity in European markets**

The size of this lot, which covers the geographic region known as Europe (i.e. the European Union, Switzerland and Norway), is at least 450 million euros. Its focus is both follow-on and later-stage equity investment opportunities in funds of all sizes with interests in mid-to large-sized European businesses. It also includes a venture capital allocation with a technological tilt.

**LOT 2 European market small and mid caps**

The size of this lot, which covers the European region known as Europe exclusively (i.e. the European Union, Switzerland and Norway), is set at 250 million euros. It has a clear focus on both follow-on and later-stage equity investment opportunities, primarily situated in one or more local markets, and in small-and mid-cap companies.

**LOT 3 Diversified North American private equity**

The size of this lot, which primarily covers the geographic region known as North America, is at least 450 million euros. Once again, its major focus is follow-on, later-stage and venture capital investments with a technological tilt.

**LOT 4 Diversified international portfolio of secondaries**

This lot, which is set at 150 million euros or more, covers both Europe and North America. By acquiring secondaries that are diversified in terms of both the number of lines and investment strategies, this lot is designed to offer the FRR the maturity and potential liquidity needed to step up the pace of investment in its first private equity program while reducing the global risk.

region. The North American component of the program will be limited to around 30%, leaving the remaining 5% free for allocation outside these two primary regions as opportunities arise.

### Investment via fund of funds managers

For this program, the FRR decided to delegate management, via fund of funds managers, and to break the allocation down into several discretionary management mandates. This approach addresses regulatory constraints which are binding on the FRR, and which prohibit the Fund from directly overseeing the private equity investment fund process. The FRR is allowed to access various types of expertise in selection and allocation, which ensures that the program will achieve adequate diversification in terms of management styles and, above all, better access to private equity funds. This approach also offers a second pooling effect on the level of the FRR's portfolio, which will considerably diminish the risk factor typically associated with this asset class.

### Broad diversification of portfolios

Given the duration of the program and the risk inherent in this type of investment, diversification of the portfolio allocation during the fund selection phase appears to be a critical success driver that can help to avoid an over-concentration of risk factors. The FRR has therefore designed its initial portfolio to provide ample diversification without running the risk of excessive dispersal of the various strategies to which exposure is desired. This diversification can be described in the following manner:

- four separate lots, primarily broken down by broad geographic regions and around one or two dominant strategies, will be used to select fund of funds managers that best meet the specific needs of the FRR.
- within each lot, and as a sideline to the central investment strategies that will constitute the heart of the portfolio, the managers selected will also have an opportunity to make use of optional strategies — to be capitalized on as opportunities arise and insofar as their own experience and expertise permit;
- diversification in terms of harvesting will be encouraged so that economic cycle impacts can be smoothed out, and will be reinforced by an allocation for secondary buyouts of private equity funds within a dedicated lot.

The manager selection process is consistent with the French government procurement code in general, and with the so-called competitive dialogue procedure in particular. It is a three-phase process that begins with an initial screening of applicants, followed by a dialogue between the government buyer and the short-listed applicants (during which the program's legal and technical aspects are discussed in detail) and ending with the awarding of mandates.
For the FRR, this program constitutes a first investment in private equity. It expects other allocations to follow, dedicated to either specific sectors or specific funding mechanisms.

# Implementing an SRI strategy

Two years after the FRR began operations, its SRI (socially responsible investment) strategy began to take shape. Today, this strategy has three basic underpinnings:

- an active policy of voting proxies at shareholder meetings in accordance with a set of published guidelines for the FRR's asset managers. An initial assessment of this policy was carried out in 2005;
- respect for universal principles, such as the UN's Global Compact. The asset managers with active European mandates, which, on December 31, 2005, accounted for more than 5 billion euros, have made a number of specific commitments in this regard to the FRR. The issue of expanding the scope of investment covered by these commitments has naturally been raised;
- the incorporation of environmental, social and governance criteria, which support sustainable development, into the portfolio management process and investment decisions. The FRR launched an SRI RFP in mid-2005, for an indicative amount of 600 million euros, whose stated aim was to select managers whose SRI philosophy is closest to its own and work with them over the long term on ways of taking ESG criteria into account in the stock-picking and portfolio management processes.

As part of this strategy, the FRR participated last year in the UN-sponsored PRI initiative aimed at promoting principles of responsible investment on the part of investors. In 2006, the FRR lent its support to yet other initiatives, such as the CDP (Carbon Disclosure Project) and academic research in the area of SRI.

### 2005 SRI RFP

In late June of 2005, after having consulted the principal players in SRI, the FRR launched an RFP designed to award several mandates to manage European equity portfolios in accordance with socially-responsible investment criteria, for an indicative amount of 600 million euros.
This RFP, which will be completed in the second quarter of 2006, is structured around the following principles:

### Commitments that managers of active equity mandates covering European large caps are asked to respect

**Research and analysis**

Subject to the availability of data, the FRR requests that asset management firms seek out and analyze relevant and reliable information on the social and environmental behavior and practices of companies being considered for investment (through analysis of published materials, contact with companies, internal research, special rating agencies, etc.). The aim of this analysis is twofold: first, to include this information in the stock-picking process (see next commitment) and second, to broaden and deepen knowledge of these companies, so that the most appropriate and useful extra-financial future performance indicators can be identified.

**Consideration of extra-financial criteria**

Using the results of this research and analysis, the FRR requests that asset management firms gradually incorporate extra-financial criteria into their stock-picking process (if they are not already doing so) and that, in doing so, they use generally accepted international guidelines. They may establish their own guidelines or benchmarks or – as a bare minimum – simply refer to the nine principles set out in the UN Global Compact. Management firms may choose to integrate these criteria into the management process more or less gradually, as long as they tend toward the establishment of a serious SRI management policy. Moreover, the mandate's stated risk tolerance level and management objectives must be respected throughout this gradual integration process.

**Transparency**

The FRR requests that management firms disclose how they have integrated extra-financial criteria into their management process and the impact of the SRI filters they have used on the portfolio (composition, performance, risk, etc.).

**Exchange with the FRR**

Managers who are awarded mandates by the FRR are expected to share the information they acquire on companies, and to disclose both how they implement their methods and their track record as managers, so that the FRR can eventually build its own benchmark and method.

1 • The FRR considers that equities managed using an SRI process do not constitute a new asset class per se. In other words, the FRR does not view SRI as a means of enhancing the efficiency of its portfolio and does not assign this type of investment an ex ante investment return objective or a volatility hypothesis that is significantly different from those underlying its other equity investments.

2 • The FRR expects that a specifically SRI investment process will include extra-financial considerations in its stock analysis process, on three primary levels:

**The first concerns the assets selected:**
The idea is to better apprehend the environmental, social or corporate governance threats and opportunities implicit in the business strategy and their impact on the FRR's long-term investment strategy. Indeed, while it is undeniable that these threats and opportunities exist, it remains difficult at this time to establish a relationship of direct and robust causality between these factors and long-term investment value creation. As the mixed findings of the research conducted to date show, it is too early to say whether SRI investments out- or under-perform conventional investments.

**The second is more economic in nature:**
The idea is to identify and, insofar as possible, to assess the impact of this strategy on other economic actors, in particular on the public domain that ultimately holds the purse strings of the FRR and other pension plans. In fact, it would be somewhat paradoxical if the FRR's own investment policy did not attempt to take corporate practices into account, especially those that could have a positive or negative impact on the public, which, in many cases, is forced to assume the financial consequences.

**The third is related to the nature of the FRR:**
The FRR was created to serve the general interest. It has a long-term investment horizon and will not make any payouts until 2020. Consequently, the Fund is in a position to be an innovative investor and promote best practices, acting in the furtherance of the objectives set for it by law and by its own Supervisory Board. Through this RFP, the FRR intends to make a methodological contribution to the development of SRI in Europe, and to support efforts in this direction by all relevant economic actors: asset management firms, businesses, rating agencies, etc.

3 • To guide potential managers in their analytic work, the FRR drew up its own responsible investment principles and submitted the list to them when the second phase of the RFP began in the fall of 2005. These principles were intended to serve as guidelines to managers of SRI mandates in their analysis, stock-picking and shareholder dialogue practices. They describe the FRR's expectations with respect to the companies that make up its portfolio of investments, in terms of their strategic decisions and management practices as well as in their relationships and dealings with stakeholders (suppliers, clients, employees, shareholders) and the environment in which they operate. These principles cover five major themes.

4 • Consequently, the approach is fundamentally multi-criteria. For this reason, the FRR has ruled out investment processes based on the notion of screening or excluding a priori certain economic sectors. The FRR prefers to encourage inclusive processes of the "Best in Class" type. Naturally, managers will be free to exclude stocks that, upon analysis, conflict with the Fund's SRI principles — independently of their market capitalization. This will ultimately depend on the degree of discretion left to managers, which will be indicated by the FRR during the second phase of the RFP process, so that it can select and eventually combine a sufficiently representative range of management processes.

5 • Consistent with this approach, and due to the still geographically disparate nature of extra-financial information available to managers, the FRR has decided at least initially to focus on the universe of pan-European equities (European Union, Member States of the European economic area and the Helvetic Confederation) covering mid and large caps.

### Signing the UN's Principles for Responsible Investment (PRI)

In early 2005, the General Secretary of the United Nations asked an international group of investors that included the FRR to develop a number of principles in the aim of promoting the integration of socially-

responsible investment practices into the financial management process. After six working sessions, and with the help of experts participating on behalf of the various stakeholders (businesses, NGOs, researchers, etc.), the Principles for Responsible Investment (PRI) emerged in the spring of 2006.
As stated today, the PRI reflect the shared values of the participating group of long-term investors with diversified portfolios, including insurers and reinsurers, pension reserve funds and other public institutionals, as well as private sector pension funds. These principles are fully compatible with the FRR's SRI strategy.

### Membership in the Carbon Disclosure Project

Supported by the UNEP (United Nations Environmental Programme), the CDP is one of the most important initiatives to emerge from the English-speaking world in the area of the environment and climatic change. Interested in promoting fuller disclosure of the environmental records and practices of businesses, as well as their level of energy use and their climatic impacts, the FRR joined the CDP for the first time in late 2005, just prior to the extension of the annual CDP questionnaire to the 120 largest listed companies in France, which make up the SBF index.

### Assessment of the proxy voting initiative of 2005

The FRR Supervisory Board discussed and agreed to a number of principles related to the voting of proxies. Accordingly, the right of the FRR as a shareholder to vote in general meetings is systematically exercised by each one of the Fund's managers, who in turn vote in accordance with the general guidelines set forth by the Fund; positions are taken in the name of the Fund on the basis of the Fund's interest alone; and these positions are taken in full independence.
These guidelines were made public after the Supervisory Board adopted them in January of 2005, and a month later, in February of 2005, they were sent out to the FRR's asset managers to enable them to actually vote proxies on behalf of the shareholder at the annual general meetings held in the spring of 2005.

### Participation in general meetings

At the end of the first season in which the guidelines were in force, and in respect of the lines held in investment portfolios, the FRR participated via its managers in 395 annual general meetings of the shareholders out of the 567 that were actually held, which amounts to 70% of the global portfolio. Conversely, managers voted on average over 54% of their portfolio. A number of significant disparities were observed from one manager to the next. Proxies were voted in the euro area, Europe and the United States, with a high proportion in French shareholder meetings. At meetings held during the 2005 season, some 7 569 resolutions were submitted to discussion and vote. They can be broken down as follows: 6 802 votes for (89.5%), 720 votes against (10%) and 47 abstentions (0.5%).

### Analysis of the votes

For the sake of illustration and based on reports provided by management firms and a survey of resolutions submitted by companies included in the CAC 40, a more qualitative analysis of how the FRR's managers voted indicates that the negative votes behalf of the FRR were motivated by inadequate disclosure on regulated agreements, the granting of clearly excessive directors' fees, members of the Board (on issues pertaining to their independence or the high number of positions and directorships held) as well as transactions involving equity and debt: shareholder base (buyback or buyout authorization during periods of takeovers or poison pill, waiver of preferential rights to subscribe to equity issues) and transactions to promote employee stock ownership (new equity issues reserved for employees with stock price discounted by more than 20%, stock grants with price discounts, free allotments of shares).
In their reporting to the FRR, asset managers indicated that they are developing a policy of approaching company management to explain the reasons for their negative voting. In the case of French companies, this takes place prior to the shareholders' meeting at which the vote will be cast; in the case of non-French companies, the negative vote is explained in a letter after the fact and sent to the company in question.
A global analysis of how its managers voted proxies indicates that all of them comply with the general guidelines provided by the FRR. Management firms also used their own analysis of the vote — and in some cases followed the recommendations of specialists in this area — by nature more detailed than the guidelines furnished by the FRR. This document is not a detailed proxy voting guide, and managers have a great deal of latitude to interpret the principles it sets forth, provided that they act in the interests of the FRR.

## Socially-responsible investment principles applicable to FRR awarded mandates for this approach to asset management

**First SRI principle: respect basic human and worker rights**

In support of this first principle, the FRR is particularly attentive to the following items:

- respect and promote international human rights law within the sphere of influence;
- practice zero tolerance of human rights violations;
- promote and ensure compliance with fundamental principles and rights at work:
  - freedom of association and recognition of the right to collective bargaining;
  - elimination of all forms of forced labor and human slavery;
  - elimination of child labor;
  - elimination of discrimination in employment and career.
- comply with all international covenants pertaining to the design, development, manufacture, storage, use, transfer and the destruction of chemical and bacteriological weapons and anti-personal land mines.

**Second SRI principle: develop employment by improving the quality of human resource management**

In support of this second principle, the FRR is particularly attentive to the following items:

- promote human resource management policy that favors disclosure, dialogue and the active participation of employees in their workplace and business;
- define and conduct of human resource management policy whose focus is long term and whose language is consistent with the organization's business development strategy. In particular, such policy favors negotiation and consultation with personnel representatives (both at the local and corporate level, where applicable), and actively promotes employment and the durable involvement of employees in the workplace and the business, particularly by providing:
  - continuing education opportunities for employees throughout their career;
  - tools and resources that help employees cope with economic change and, in particular, that foster the creation of new businesses and activities;
  - profit-sharing programs for employees.
- implement policies and procedures aimed at obtaining ongoing improvements in working conditions, in particular those that relate to worker health and safety, both physical and mental.

**Third SRI principle: assume responsibility for the environment**

In support of this third principle, the FRR is particularly attentive to the following items (the exact wording will depend on each company's business area or industry):

- factor the environment into the business strategy. In particular, apply the principle of precaution and work to prevent environmental pollution and biodiversity impairment;
- strive to develop the eco-efficiency of manufacturing processes as well as products, making efforts to promote and develop environmentally-friendly technologies and the use of renewable energy;
- takes steps to reduce $CO_2$ and other greenhouse gas emissions, as well as the volume and toxicity levels of waste products and water consumption;
- develop and enforce HEQ (high environmental quality) and energy standards for the company's own plant, property and equipment (production facilities, offices and real-estate assets);
- factor in the environmental impact of the means of transportation used by the company, both internally and externally;
- develop a policy of full disclosure on the health and safety impacts on employees, local residents and clients of manufacturing processes and products;
- assume financial liability for accidental pollution related to the company's business.

**Fourth SRI principle: respect the consumer and fair trade practices**

In support of this fourth principle, the FRR is particularly attentive to the following items:

- promote product safety and quality. Practice full disclosure with clients, as measured by the laws in force locally and best industry practice;
- refrain from behaviors that interfere with or prevent the market from functioning correctly, as well as from engaging in behaviors or practices that prevent the exercise of fair trade and competition;
- promote initiatives aimed at establishing cooperative relationships with suppliers, sub-contractors and co-contractors;
- make available the tools and systems needed to prevent attempted corruption, racketeering, money-laundering and other business crimes.

**Fifth SRI principle: promote good corporate governance:**

- corporate organization and draft resolutions submitted to the approval of shareholders should comply with the guidelines pertaining to voting proxies developed by the FRR.

# The FRR's internal reorganization and operating costs

### Legal framework of the FRR

The regulations that govern the FRR were amended and supplemented by French decree no. 2005-162 dated December 30, 2005. The key provisions are indicated below:

- The FRR is no longer required to submit its management agreements to the prior approval of its regulators.
- The role of the independent auditors has been further clarified: they no longer certify the itemized statement of the FRR's assets and related values, but rather the annual financial statements, and issue a statement of limited review on the Fund's half-year financial statements.
- An exception to the required minimum investment of 3% may be granted in the cases specified in article R-135-29 of the French Social Security Code, making it possible for the FRR to invest in new asset classes via investment mandates or ad hoc investment vehicles such as private equity and real estate.

In addition, the FRR may, subject to the terms and conditions set forth in a government order issued on November 3, 2005, on a temporary basis and to safeguard its assets, directly assume responsibility for the management of investments under one or several mandates, without engaging the services of an asset management firm.

The wording of all amended or updated legislation and regulations is available on the FRR's website.

### The FRR re-elects some Supervisory Board members

The FRR Supervisory Board re-elected some of its members. Mr. Raoul Briet was re-elected to his position as Chairman of the Board by government decree issued on December 6, 2005. The current make-up of the Supervisory Board is appended to this report.

### The FRR reorganizes its own teams

In the past three years, the FRR has been in the start-up phase of its ambitious project. Accordingly, the focus has been on laying down the solid foundations needed to successfully carry out the important public service mission that was entrusted to its care.

In 2005, the FRR felt it was time to assess the first three years and make adjustments as needed, after implementing its structure and tools and after stepping up its financial management activity following the international asset manager selection process via a series of initial RFPs.

After discussions with an outside consultant and the operational staff at the CDC *(Caisse des Dépôts et Consignations)*, the FRR made changes to its organizational structure intended to strengthen its financial planning capability, optimize its structures and work methods and streamline certain technical functions.

Consequently, the FRR's organization has been realigned around three central divisions — Finance, Corporate and Legal, and Risk Control — structured within seven internal departments in addition to the accounting agency.

On December 31, 2005, 30 employees were assigned to the FRR's three central divisions. Their functions are described below:

- **The Finance Department** is responsible for preparing the strategic asset allocation guidelines that the Executive Board submits to the Supervisory Board, for selecting the FRR's financial services providers and defining the terms of their engagement, and for producing the analyses that serve as foundations for the Executive Board's decisions in the area of tactical allocation and currency risk management. This division is also responsible for monitoring the execution of management mandates, in particular for compliance and in terms of manager performance.

- **The Financial Performance and Risk Control Department** is responsible for managing the FRR's global risk exposure (centralizing information related to risk detection, measurement and monitoring), the Fund's global performance attribution and the management of the organization's own operational risks.
- **The Corporate and Legal Department** is responsible for coordinating and managing the FRR's legal issues: implementation and monitoring of management mandates and agreements with the FRR's other service providers; provision of legal counsel on the process by which the FRR selects its service providers; development and execution of the Fund's proxy voting policy. This division is also in charge of budget and management control, and communications policy.

The roles of the various departments have also been redefined to ensure optimal coverage of the full range of the FRR's operational activities:

- **Investment Strategy and Risk Budgeting**
This department is responsible for functions dedicated to strategic allocation and the FRR's long-term risk management.
- **Tactical Allocation**
This department is in charge of managing tactical allocation and coordinating the FRR's exchange rate risk hedging policy.
- **Asset Manager Selection and SRI**
This department coordinates the process of selecting outside asset managers and is in charge of defining and implementing the FRR's SRI (socially-responsible investment) principles.
- **External Asset Management**
This department is responsible for monitoring the FRR's asset management mandates, and in particular for analyzing portfolio performance and ensuring that all mandated services are provided by managers.
- **Middle Office and Reporting**
This department carries out the FRR's middle office functions, which include financial administration, relationships with the FRR's custodian, depositary and asset valuation expert *(Caisse des Dépôts et Consignations)* and the coordination of the financial reporting process.
- **Legal**
This department is responsible for the legal coordination of the FRR's management mandates and service agreements, particularly in connection with the Fund's selection processes, and also monitors the proxy voting process.
- **Financial Performance and Risk Control**
This department is in charge of coordinating the management of the FRR's financial risks. It centralizes information related to identifying, measuring and monitoring these risks and ensures compliance with regulations in force.

In addition, **the accounting agency** is responsible for all of the FRR's accounting and bookkeeping functions, including the preparation of the interim and financial statements and reports that are submitted by the Executive Board to the Supervisory Board and the accounting committee.

### Budget items

The FRR's budget for 2005 was adopted by the Executive Board in November of 2004 and then approved by the Fund's regulators. The operating expenses used in 2005 came to a total of 60.4 million euros and were primarily attributable to the following three phenomena:

- throughout the year, portfolio investments were stepped up and the tactical allocation program, which is the direct responsibility of the Executive Board, was initiated;
- throughout the year, portfolio investments were stepped up and the tactical allocation program, which is the direct responsibility of the Executive Board, was initiated;
- the FRR continued to consolidate its organization, structures and tools over the course of last year.

The rise in these expenses is aligned with the beginning of operations for the FRR as mandates to manage its reserves were activated. It also largely reflects the full-year cost of managing portfolios that were invested after the start of 2004, coupled with the pursued initialization of new management mandates. This move toward full-operational status had an impact on expenses related to financial management (fees paid to managers and brokerage commissions on trades) as well as on operational costs directly related to the volumes under management (custodial and fund administration costs).
In 2005, the FRR made efforts to reduce its administrative management expenses other than those related to the operational management of its mandates (payroll, property management costs and operating expenses) and both pursued and refined the rollout and integration of management steering indicators for the Fund and for the performance of the administrative management of the CDC *(Caisse des Dépôts et Consignations)*.
Finally, all of these costs were benchmarked for measurement against the best practices in the market. The FRR's operating expenses for 2005 are itemized below, presented in accordance with the chart of accounts for social security organizations, which is used by the FRR for its own accounting:

| Operating expenses (in € millions) | 2004 | 2005 |
|---|---|---|
| Payroll expense | 4.482 | 5.267 |
| Financial management* | 4.824 | 37.171 |
| Custodial services/Fund administration | 4.673 | 13.285 |
| Information systems and technology (dedicated IS) | 1.083 | 1.267 |
| Consultants | 0.994 | 1.743 |
| Other general expenses | 1.646 | 1.711 |
| **TOTAL OPERATING EXPENSES** | **17.702** | **60.444** |

* Management and brokerage fees.

### Monitoring managers

Within the FRR, the External Asset Management Department is responsible for supervising asset management mandates. In addition to maintaining daily contact with managers, the supervision of mandates includes two more formal processes: quarterly internal reporting and management committee meetings.
Quarterly reports are prepared using data provided by the FRR's own accounting department and custodial services as well as by the individual asset managers. By analyzing data from both of these sources, the FRR is able to establish an independent vision that supplements the manager's, and that can be used as needed for the purpose of comparison. In particular, reporting is used to analyze management processes to ensure that they are consistent with the initial descriptions provided by managers in their proposals, absolute and relative performance, risk exposure levels (both ex ante and ex post tracking error), trades (rotation, brokering, best execution), quality of operations (reporting scope and timeframes, quality of settlement-deliveries), compliance incidents, proxy voting performance and SRI reporting. Taken together, these factors of analysis are used to measure the extent to which actual management style and process confirm to the initial bid submitted, and in so doing help to ensure the overall consistency of the FRR's portfolio of invested assets.
In addition, the FRR holds management committee meetings with its asset managers — annually for passive mandates and twice a year for active mandates. These meetings provide an opportunity to discuss issues related to implementing the asset management process. These issues are the same as those covered in the quarterly reports submitted. The External Asset Management Department also helps to prepare and lead meetings of the internal committees responsible for supervising the risk and performance aspects of mandates.
Finally, the FRR's Manager Selection Committee examines on a quarterly basis the performance of asset management mandates that have been awarded.

# Organization chart

**Supervisory Board**
**President:** Raoul Briet
**Vice-Presidents:** Jean-Louis Beffa
Jean-Christophe Le Duigou

**Manager selection Committee**
**President:** Antoine de Salins
Alain Hindié – Christopher Nowakowski
René Karsenti – Alain Robidel

**Executive Board**
**President:** Francis Mayer
Antoine de Salins – Philippe Most

**Public accountant**
Bruno Veccia

**Corporate & legal Division**
Maria Rucli

**Finance Division**
Jean-Louis Nakamura

**Risk management Division**
François Pelletier

**Legal Department**
Manager:
Bénédicte Paulze d'Ivoy

**Investment strategy & risk budgeting Department**
Manager:
Christophe Aubin

**Financial performance & risk control Department**
**Manager:** Pierre Leygue

**Communications Department**

**Tactical asset allocation Department**
**Manager:** Laurent Degioanni

**Budget & management control Department**

**Asset manager selection & SRI Department**
**Manager:** Nada Villermain-Lécolier

**External asset management Department**
**Manager:** Philippe Aurain

**Middle-office & reporting Department**
**Manager:** Isabelle Szendy

# Fund Governance

■ **SUPERVISORY BOARD**

**Chairman**
**Raoul Briet**

**Vice-Chairman**
**Jean-Louis Beffa**
Chairman and CEO, the Saint-Gobain Group

**Vice Chairman**
**Jean-Christophe Le Duigou**,
Representing the Confédération générale du travail (CGT)
*Alternate: Pierre-Yves Chanu*

Board members

**Members from the French *Assemblée nationale***
**Yves Bur**
*Alternate: Pierre Hellier*
**Marc Laffineur**
*Alternate: Jean-Yves Chamard*

**Members from the French *Sénat***
**Jean-Jacques Jegou**
*Alternate: Claude Domeizel*
**Dominique Leclerc**
*Alternate: Yves Freville*

Representatives of social security insureds appointed by nationally representative trade unions

**Confédération générale du travail – Force ouvrière (CGT-FO)**
**Jean-Jacques Poujade**
*Alternate: Bernard Devy*

**Confédération française démocratique du travail (CFDT)**
**Jean-Paul Le Bail**
*Alternate: Philippe Le Clezio*

**Confédération française des travailleurs chrétiens (CFTC)**
**Isabelle Sancerni**
*Alternate: Michel Moise-Mijon*

**Confédération française de l'encadrement – CGC**
**Solange Morgenstern**
*Alternate: Danièle Karniewicz*

Representatives of self-employed employers and workers

**Mouvement des entreprises de France**
**Jean-René Buisson**
*Alternate: Catherine Thibier*
**Véronique Cazals**
*Alternate: Agnès Lepinay*
**Alain Leclair**
*Alternate: André Renaudin*
*Association française de la gestion financière*

**Confédération générale des PME**
**Jean-François Veysset**
*Alternate: Georges Tissie*

**L'Union professionnelle artisanale**
**Dany Bourdeaux**
*Alternate: Berthe Duguey*

Representatives of the Minister in charge of Social Security, appointed by government order issued by the Minister in charge of Social Security
**Dominique Libault**
*Alternate: Stéphane Seiller*
**Jean-Louis Rey**
*Alternate: Franck Le Morvan*

Representing the Minister of the Economy, Finance and Industry, appointed by government order issued by the Minister of the Economy, Finance and Industry
**Xavier Musca**
*Alternate: Thierry Francq*

Representing the Minister in charge of the Budget, appointed by government order issued by the Minister in charge of the Budget
**Philippe Josse**
*Alternate: Henri Lamotte*

## EXECUTIVE BOARD

**Chairman**
**Francis Mayer**

**Other members**
**Antoine de Salins**
**Philippe Most**

## MANAGER SELECTION COMMITTEE

**Chairman**
**Antoine de Salins**

**Alain Hindié**
Consultant
**René Karsenti**
Chief financial officer, BEI
**Christopher Nowakowski**
Former international consultant
**Alain Robidel**
Managing partner, AC2F Consultants

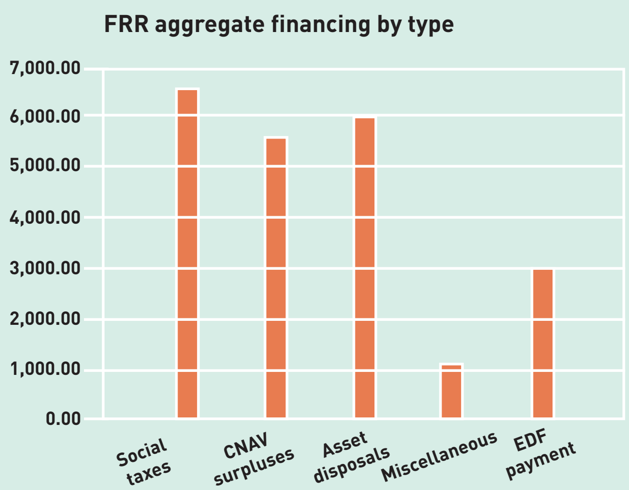
# The 2005 financial statements

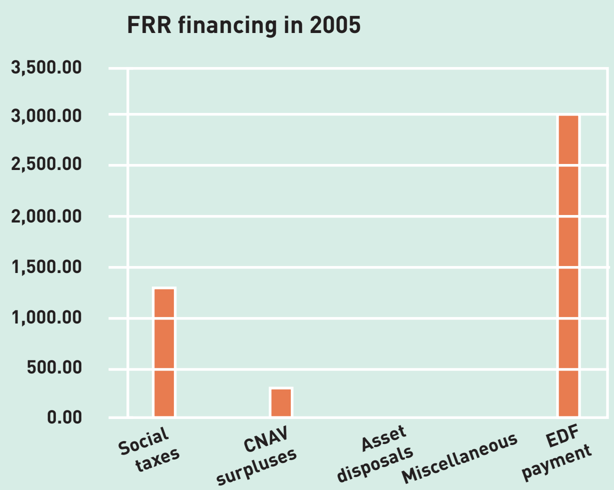
Due to the provision of external sources of funding and the results of financial management, the FRR's total financial assets increased substantially over the course of 2005. On December 31, 2005, the aggregate value of the Fund's marketable securities and cash on hand totaled 26.65 billion euros, compared with 19.17 billion euros previously.

### External sources of funding

The resources provided for under the act of July 19, 2001 reached 1.5 billion euros in 2005, bringing the total amount of endowments received by the FRR since inception to 19.4 billion euros. This sum makes up the bulk of the Fund's equity, which totaled 23.25 billion euros on December 31, 2005.

In addition, pursuant to a ministerial order dated January 31, 2005, the CNIEG *(Caisse nationale des industries électriques et gazières)* made an additional payment of 3.06 billion euros to the Fund, a one-off contribution intended for the CNAVTS Old Age Fund *(Caisse nationale d'assurance vieillesse des travailleurs salariés)* as of 2020. This contribution is carried on the FRR's balance sheet as a liability, adjusted to reflect the investment income it will generate as a result of the FRR's management, less all related management fees. On the December 31, 2005 reporting date, the total value of this sum was 3.32 billion euros.



### Results of financial management

According to the FRR's chart of accounts, which is set forth in a CNC (Conseil national de la comptabilité) opinion dated June 23, 2004, the accounting treatment of interest income and expense differs from that of capital gains and losses.

The FRR's trading portfolio is carried on the balance sheet at its fair market value. All of the differences between the price paid to acquire securities and their fair market value on the year-end accounting cut-off date are unrealized capital gains or losses, as the case may be, and are recorded under equity by the FRR, with the exception of the percentage of the return earned on the one-off contribution that is attributable to CNAVTS. On December 31, 2005, unrealized capital gains recorded under equity totaled 2.05 billion euros, versus 342.22 million euros on December 31, 2004. The total value of the trading portfolio on this same date was 19.54 billion euros.

Both interest expense and income are charged against or credited to the income statement, as the case may be. Taken together, income earned in marketable securities and capital gains or losses made on disposals totaled 785.62 million euros, versus 359.38 million euros in 2004.

### Operating expenses

Operating expenses totaled 64.44 million euros in 2005, compared with 17.70 million euros in 2004. The rise in expenses — which include fees paid to investment firms, brokerage fees paid on the sale of securities and routine operating expenses — was directly attributable to the increase in assets under management.

Total investment income less total operating expenses provides a result for 2005 of 725.83 million euros, which is included under the FRR's equity.

In accordance with article L. 135-12 of the French Social Security Code *(Code de la Sécurité sociale)*, the financial statements for 2005 were submitted to and certified by the independent auditors of the FRR.

**Financing per year**

# BALANCE SHEET
## December 31, 2005

| **ASSETS** (in euros) | **12/31/05** | **12/31/04** |
|---|---|---|
| LONG-TERM ASSETS | 1,690.28 | 2,673.15 |
| RECEIVABLES | 5,202,444,159.95 | 1,048,287,005.47 |
| Endowments allocated to the FRR receivable | 2,607,175.98 | 30,371,640.68 |
| Receivables from operations | 91,923.75 | 1,699.19 |
| Receivables on financial instruments | 24,220,303.70 | 5,057,972.56 |
| Receivables on forex transactions | 5,170,335,241.47 | 1,012,855,693.04 |
| Receivables on financial futures | 5,189,515.05 | |
| MARKETABLE SECURITIES | 19,540,213,460.85 | 6,370,829,564.52 |
| Equities | 14,859,006,789.73 | 4,886,124,166.53 |
| Bonds | 4,091,131,600.06 | 1,323,739,082.30 |
| Negotiable debt instruments | 590,075,071.06 | 160,966,315.69 |
| CASH | 7,118,883,247.53 | 12,799,668,450.81 |
| PREPAID EXPENSES | 2,837.46 | |
| **TOTAL ASSETS** | **31,861,545,396.07** | **20,218,787,693.95** |

| **LIABILITIES** (in euros) | **31/12/05** | **31/12/04** |
|---|---|---|
| EQUITY CAPITAL | 23,251,188,881.19 | 19,256,593,579.81 |
| Endowments | 19,421,244,676.10 | 17,891,910,401.15 |
| Reserves | 1,054,083,549.67 | 711,862,872.89 |
| Valuation variance | 2,050,027,247.78 | 310,599,628.99 |
| Net income for the year | 725,833,407.64 | 342,220,676.78 |
| PAYABLES | 8,609,324,617.66 | 961,136,997.51 |
| CNIEG non-recurring contribution | 3,321,990,853.24 | |
| Payables from operations | 41,099,012.90 | 13,925,893.91 |
| Payables on financial instruments | 43,710,784.28 | 1,193,985.40 |
| Payables on forex transactions | 5,198,506,062.35 | 946,017,118.20 |
| Payables on financial futures | 4,017,904.89 | |
| DEFERRED INCOME | 1,031,897.22 | 1,057,116.63 |
| **TOTAL LIABILITIES** | **31,861,545,396.07** | **20,218,787,693.95** |

# STATEMENT OF INCOME
## December 31, 2005

| EXPENSES (in euros) | 12/31/05 | 12/31/04 |
|---|---|---|
| Outside services | 59,816,767.20 | 17,114,966.34 |
| Taxes | 53,991.61 | 53,405.45 |
| Payroll expense | 572,789.55 | 532,720.48 |
| Amortization | 982.87 | 275.75 |
| OPERATING EXPENSES | 60,444,531.23 | 17,701,368.02 |
| Currency translation losses | 347,071,047.34 | 1,660,981.43 |
| Expenses on financial futures | 995,409.08 | |
| Expenses on the sale of securities | 129,594,549.80 | 13,889,255.00 |
| Other financial expenses | 25,629.79 | 154,670.61 |
| Interest expense on CNIEG | 84,343,161.10 | |
| FINANCIAL EXPENSES | 562,029,797.11 | 15,704,907.04 |
| NON-RECURRING EXPENSES | 216,427.53 | 0.00 |
| TOTAL EXPENSES | 622,690,755.87 | 33,406,275.06 |
| **NET INCOME FOR THE PERIOD** | **725,833,407.64** | **342,220,676.78** |
| **TOTAL** | **1,348,524,163.51** | **375,626,951.84** |

| INCOME (in euros) | 12/31/05 | 12/31/04 |
|---|---|---|
| Income from marketable securities | 355,455,955.68 | 40,038,043.16 |
| Currency translation gains | 121,025,204.14 | 1,730,752.36 |
| Income on financial futures | 5,765,636.43 | |
| Income on the sale of securities | 659,247,120.26 | 28,179,495.83 |
| Other financial income | 206,165,418.04 | 305,145,542.02 |
| FINANCIAL INCOME | 1,347,659,334.55 | 375,093,833.37 |
| NON-RECURRING INCOME | 864,828.96 | 533,118.47 |
| TOTAL INCOME | 1,348,524,163.51 | 375,626,951.84 |
| **TOTAL** | **1,348,524,163.51** | **375,626,951.84** |

# Notes to the financial statements for 2005

**1. Legislative and regulatory changes**

The Social Security Financing act for 2005 supplemented existing regulations governing the activity of the FRR. In particular, article L.135-12 modified the role ascribed to the Statutory Auditors. They are now responsible for certifying the annual financial statements and issuing a limited report after examining the Fund's interim financial statements, applicable as of the reporting period ended June 30, 2005.

The financial statements for the year ended December 31, 2005 are compared to the unaudited financial statements for the year ended December 31, 2004.

**2. Significant accounting policies and methods**

The financial statements of the FRR are drawn up based on the generally accepted accounting principles set out in the chart of accounts for Social Security organizations and in opinion no. 2003-07 of June 24, 2003 issued by the CNC *(Conseil national de la comptabilité)*.

The generally accepted accounting standards have been applied with the aim of ensuring that the financial statements reflect the conservatism principle and provide a true and fair view of the Fund's financial position, in accordance with the basic principles of going concern, consistent accounting policies and accrual accounting.

Transaction recording dates are the trading dates for those transactions in the portfolio. Transactions are recorded at cost (accrued coupon interest and fees excluded), and the PRMP rule *(prix de revient moyen pondéré* – weighted average cost price) is used for realized capital gains or losses.

Asset values are calculated on the basis of positions held on Friday evening or the last TARGET business day of the week, and the last TARGET business day of the month. The default price is the closing price on the issuer's benchmark market, case by case on the principal quotation market.

Because the FRR's accounts are stated in euros, positions of FRR mandates in foreign currencies are valued and accounted for on the basis of exchange values calculated using WM/Reuters closing spot rates (4:00 pm London time).

Forex futures are valued on the basis of both a straight-line amortization of the initial swap points for the transaction and by the valuation of the foreign currency position based on WM/Reuters closing spot rates (4:00 pm London time).

For unlisted securities, valuation is based on the acquisition price (or the redemption value for unlisted bonds close to maturity).

In the event that price quotes are not available on the day of valuation, assets are valued on the basis of the last known price or using a predefined procedure in the case of previously established prices.

For fixed-income instruments, accrued coupon interest on the transaction or at valuation are expressed with respect to the value date. This accounting policy is related to the fact that operations are accounted for as of the date of the trade.

Euro area government and corporate bonds are valued on the basis of ISMA prices.

Global bonds are valued on the basis of Merrill Lynch prices for the US, and of quoted prices for UK and Japanese bonds.

Inflation-index linked bonds are valued on the basis of closing prices, using the appropriate index rate, on the basis of quoted prices for the UK and on the basis of prices contributed by ISMA and Merrill Lynch for euro area and for US bonds, respectively.

BTF and BTAN French sovereign debt securities are valued on the basis of published Banque de France rates on the date of valuation. Values for negotiable debt instruments stated in a currency other than the euro that will mature in less than three months from the accounting cut-off date are established on a straight-line basis.

Futures contracts are valued closing settlement prices.

Unrealized gains and losses on financial instruments are accounted for as valuation variances. As such, they have no effect on the Fund's net earnings.

Realized gains and losses are credited to or charged against income.

The fees paid to management firms are based on a rate scale that assigns basis points to lots of assets under management. Certain mandates receive variable fees for outperforming their benchmark index by a given margin.

Balance sheet assets are amortized over three years.

The non-recurring, lump-sum contribution mentioned in article 19 of L. 2004-803 of August 9, 2004 and paid to the FRR by the CNIEG, pursuant to the April 20, 2005 decision by the *Haut Conseil interministériel de la comptabilité des organismes de Sécurité sociale,* is accounted for and carried as a liability in the FRR's financial statements.

**3. Financial statement presentation**

For reader convenience, certain classifications have been made with respect to these financial statements:

**Balance sheet:** The various line items are presented as net values and take into account amortization (for long-term fixed assets) and valuation variances (for financial assets and liabilities).

**Payable endowments allocated to the FRR** include the total endowments allocated to the FRR in 2005 and known at the accounting cut-off date, but not yet received on December 31, 2005.

**Payables and receivables on financial instruments** include securities transactions carried out by investment firms but for which settlement is pending (coupon interest due and payable or receivable, sales or purchases pending settlement).

**Payables and receivables on forex transactions** include pending transactions involving currencies, regardless of whether they are over-the-counter cash transactions or related to futures contracts.

**Payables and receivables on financial futures** include pending transactions related to futures (marge payable or receivable, security deposit).

**Marketable securities** fall under one of three categories: equities, bonds and negotiable debt instruments (NDI). They are recorded and carried at their fair market value, including accrued coupon interest for bonds and NDIs.

The line item **"cash and equivalent"** includes all of the FRR's cash accounts stated in euros or in other currencies (at their year-end exchange values) as well as accrued interest on these sight and term deposits.

**Equity includes :**

- endowments, which are the monies the Fund has received since the date of its inception in 1999,
- reserves, which correspond to the aggregate returns the Fund has generated since its inception,
- valuation variances, which represent the unrealized capital gains and losses recorded for all assets on the December 31, 2005 reporting date,
- net income for the year.

**The line item "CNIEG non-recurring contribution" includes :**

- the terms and conditions under which the CNIEG electricity and gas industry fund *(Caisse nationale des industries électriques et gazières)* is to pay the FRR the non-recurring, lump-sum contribution mentioned in article 19 of L. 2004-803 of August 9, 2004 were set by order of the Minister of Solidarity, Health and the Family on January 31, 2005. Pursuant to this order, the CNIEG was to pay the FRR the sum of 3,060,000,000 euros by June 30, 2005,
- interest paid to the FRR by the CNIEG pursuant to the order dated January 31, 2005,
- a proporationate share of the income for the period, net of management fees, which corresponds to interest earned by the FRR on the cash sum provided by the CNIEG,
- the share in the FRR's total unrealized capital gains or losses at December 31, 2005 represented by the aforementioned cash sum.

### 4. Change in the value of marketable securities in the portfolio

| | | | | 12/31/2004 |
|---|---|---|---|---|
| | Purchase price | Unrealized losses or gains | Accrued interest | Book price |
| Equities | 4,676,784,759.36 | 209,339,407.17 | | 4,886,124,166.53 |
| Bonds | 1,266,672,957.88 | 34,715,528.47 | 22,350,595.95 | 1,323,739,082.30 |
| Negotiable debt instruments | 160,353,793.23 | –210,630.47 | 823,152.93 | 160,966,315.69 |
| | **6,103,811,510.47** | **243,844,305.17** | **23,173,748.88** | **6,370,829,564.52** |

| | | | | 12 /31/2004 |
|---|---|---|---|---|
| | Purchase price | Unrealized losses or gains | Accrued interest | Book price |
| Equities | 12,687,579,110.16 | 2,171,427,679.57 | | 14,859,006,789.73 |
| Bonds | 3,951,809,281.20 | 75,723,400.77 | 63,598,918.09 | 4,091,131,600.06 |
| Negotiable debt instruments | 587,083,442.88 | –1,597,001.95 | 4,588,630.13 | 590,075,071.06 |
| | **17,226,471,834.24** | **2,245,554,078.39** | **68,187,548.22** | **19,540,213,460.85** |

| | | 12/31/2004 | 12/31/2005 | Change |
|---|---|---|---|---|
| Equities | | 4,886,124,166.53 | 14,859,006,789.73 | 9,972,882,623.20 |
| Bonds | | 1,323,739,082.30 | 4,091,131,600.06 | 2,767,392,517.76 |
| Negotiable debt instruments | | 160,966,315.69 | 590,075,071.06 | 429,108,755.37 |
| | **6,370,829,564.52** | **19,540,213,460.85** | **13,169,383,896.33** | |

### 5. Analysis of portfolio by remaining term to maturity

| | 12/31/2005 |
|---|---|
| 0-1 year | 14.25% |
| 1-3 years | 13.02% |
| 3-5 years | 10.80% |
| 5-7 years | 11.93% |
| 7-10 years | 13.79% |
| 10-15 years | 12.55% |
| → 15 years | 23.66% |
| | **100.00%** |

### 6. Analysis of portfolio by coupon type

| | 12/31/2005 |
|---|---|
| Fixed | 82.87% |
| Indexed | 16.33% |
| Floating or variable | 0.81% |
| | **100.00%** |

## 7. Analysis of portfolio by currency of listing

| Currency | Equities | Bonds | NDI* | Total |
|---|---|---|---|---|
| AUD | 152,933,262.67 | | | 152,933,262.67 |
| CHF | 168,261,850.98 | | | 168,261,850.98 |
| DKK | 5,216,487.79 | | | 5,216,487.79 |
| EUR | 10,360,196,720.60 | 3,318,915,495.06 | 566,891,451.89 | 14,246,003,667.55 |
| GBP | 551,304,888.25 | 132,389,068.77 | 3,185,262.70 | 686,879,219.72 |
| HKD | 57,248,852.46 | | | 57,248,852.46 |
| JPY | 665,785,978.99 | 79,423,717.20 | | 745,209,696.19 |
| NOK | 23,095,605.36 | | | 23,095,605.36 |
| NZD | 3,137,296.69 | | | 3,137,296.69 |
| SEK | 51,007,813.75 | | | 51,007,813.75 |
| SGD | 27,788,141.12 | | | 27,788,141.12 |
| USD | 2,793,029,891.07 | 560,403,319.03 | 18,966,459.25 | 3,372,399,669.35 |
| **TOTAL*** | **14,859,006,789.73** | **4,091,131,600.06** | **589,043,173.84** | **19,539,181,563.63** |

* Including prepaid interest: 1,031,897.22 euros

## 8. Itemized statement of securities at December 31, 2005

| | |
|---|---|
| Euro area equities | 10,360,196,720.60 |
| Non-euro area EU equities | 798,886,646.13 |
| US equities | 2,793,029,891.07 |
| Asian equities ex-Japan | 241,107,552.94 |
| Japanese equities | 665,785,978.99 |
| | **14,859,006,789.73** |
| Euro area bonds | 3,318,915,495.06 |
| Non-euro area EU bonds | 132,389,068.77 |
| US bonds | 560,403,319.03 |
| Japanese bonds | 79,423,717.20 |
| | **4,091,131,600.06** |
| Euro NDI | 566,891,451.89 |
| Non-euro area EU NDI | 3,185,262.70 |
| US NDI | 18,966,459.25 |
| | **589,043,173.84** |

## 9. Endowments receivable (earmarked for the FRR)

| | 12/31/2005 |
|---|---|
| CDC - prescribed consignments | 1,605,167.68 |
| UMTS royalties/license fees | 105,015.00 |
| ACOSS - employee savings | 896,993.30 |
| **TOTAL** | **2,607,175.98** |

### 10. Long-term liabilities and operating receivables and payables

| | 12/31/2005 | Due in more than one year | Due in less than one year |
|---|---|---|---|
| **Receivables** | | | |
| Advances to suppliers | 91,923.75 | | 91,923.75 |
| **TOTAL** | **91,923.75** | **0.00** | **91,923.75** |
| **Payables** | | | |
| Government and social security | 69,035.86 | | 69,035.86 |
| Other | 41,029,977.04 | | 41,029,977.04 |
| **TOTAL** | **41,099,012.90** | **0.00** | **41,099,012.90** |

### 11. Receivable on financial management

| | 12/31/2005 |
|---|---|
| **Related to financial instruments** | |
| Interest coupons due and immediately payable | 20,421,454.54 |
| Sales pending settlement | 3,798,849.16 |
| | **24,220,303.70** |
| **Related to forex transactions** | |
| Futures purchases | 151,903,881.39 |
| Forex forwards receivables | 5,008,691,578.60 |
| Forex spot receivables | 746,520.58 |
| Valuation variance | 168.46 |
| Discount/premium on term market | 8,993,092.44 |
| | **5,170,335,241.47** |
| **Related to financial futures** | |
| Security deposits | 5,125,565.05 |
| Margin receivable | 63,950.00 |
| | **5,189,515.05** |

### 12. Payable on financial management

| | 12/31/2005 |
|---|---|
| **Related to financial instruments** | |
| Securities purchased, settlement pending | 43,708,634.07 |
| Valuation variance on purchased securities | 2,150.21 |
| | **43,710,784.28** |
| **Related to forex transactions** | |
| Forward sales | 5,045,191,532.03 |
| Forex forwards | 151,091,244.90 |
| Forex spot payables | 34,381.04 |
| Premium | 2,188,904.38 |
| | **5,198,506,062.35** |
| **Related to financial futures** | |
| Margin to be settled | 4,017,904.89 |
| | **4,017,904.89** |

### 13. Change in equity

| | 12/31/2005 | 12/31/2004 | Evolution |
|---|---|---|---|
| Endowments | 19,421,244,676.10 | 17,891,910,401.15 | 1,529,334,274.95 |
| Reserves | 1,054,083,549.67 | 711,862,872.89 | 342,220,676.78 |
| Valuation variance | 2,050,027,247.78 | 310,599,628.99 | 1,739,427,618.79 |
| Net income for the year | 725,833,407.64 | 342,220,676.78 | 383,612,730.86 |
| | **23,251,188,881.19** | **19,256,593,579.81** | **3,994,595,301.38** |

### 14. CNIEG non-recurring contribution

On December 31, 2005, the non-recurring contribution of 3,060,000.00 euros paid to the FRR were supplemented by:
- interest paid by the CNIEG to the FRR, totaling 22,277,139.14 euros,
- a percentage of the FRR's investment income for the second half of 2005, net of management fees, totaling 62,066,021.91 euros,
- a percentage of the unrealized capital gains generated in the second half of 2005, i.e. 177,647,692.14 euros.

| | |
|---|---|
| FRR's total equity on June 30, 2005 | 20,357,474,105.28 |
| Endowments in third quarter 2005 | 232,858,284.84 |
| CNIEG payment | 3,082,001,492.19 |
| | **23,672,333,882.31** |

| **CNAV SHARE ON JUNE 30, 2005** | **13.02%** |
|---|---|
| **Endowments** | |
| 06/30/2005 | 18,129,016,811.65 |
| 09/30/2005 | 18,361,875,096.49 |
| | **232,858,284.84** |

### Analysis as of December 31, 2005

| | 06/30/2005 | 12/31/2005 | To be allocated |
|---|---|---|---|
| **OPERATING EXPENSES** | **24,904,145.28** | **60,444,531.23** | **35,540,385.95** |
| Investment income | 336,101,218.29 | 847,695,559.35 | 511,594,341.06 |
| Non-recurring income or expense | –16,294.34 | 648,401.43 | 664,695.77 |
| Global income | 311,180,778.67 | 787,899,429.55 | 476,718,650.88 |
| Valuation variance on securities | 993,257,396.94 | 2,245,554,078.39 | 1,252,296,681.45 |
| Valuation variance – foreign exchange | –130,131,671.65 | –19,828,479.95 | 110,303,191.70 |
| Valuation variance – derivatives | 67,240.00 | 1,949,341.48 | 1,882,101.48 |
| Valuation variance – global | 863,192,965.29 | 2,227,674,939.92 | 1,364,481,974.63 |
| Investment income less operating expenses | 476,718,650.88 | | |
| % share | 13.02% | | |
| CNAV share | 62,066,021.91 | | |
| Valuation variance | 1,364,481,974.63 | | |
| % share | 13.02% | | |
| CNAV share | 177,647,692.14 | | |

### 15. Cash and equivalent

| | |
|---|---|
| AUD | 5,104,459.85 |
| CHF | 1,939,702.62 |
| DKK | 2,423.96 |
| GBP | 13,575,126.31 |
| HKD | 232,052.82 |
| JPY | 18,744,475.14 |
| NOK | 1,522,374.73 |
| NZD | 11,524.63 |
| SEK | 845,361.79 |
| SGD | 38,201.37 |
| USD | 80,249,072.98 |
| **TOTAL ASSETS IN FOREIGN CURRENCIES** | **122,264,776.20** |

| | 12/31/2005 |
|---|---|
| Accrued interest on cash accounts | 54,656,024.37 |
| In foreign currencies | 122,264,776.20 |
| In euros | 6,941,962,446.96 |
| **TOTAL CASH** | **7,118,883,247.53** |

### 16. Operating expenses

| | 2005 |
|---|---|
| Administrative management CDC | 20,737,958.00 |
| Compensation paid to investment firms | 24,747,669.61 |
| Other outside services | 14,331,139.59 |
| of which brokerage fees | 12,423,387.65 |
| Taxes | 53,991.61 |
| Payroll expense | 572,789.55 |
| Amortization | 982.87 |
| **OPERATING EXPENSES** | **60,444,531.23** |

### 17. Off-balance sheet commitments

#### Indexed futures

Buyer position

| Buyer position | Currency | Amount | Commitment | Market Value |
|---|---|---|---|---|
| CAC 40 | EURO | 3,174 | 149,362,805.00 | 150,320,640.00 |
| DJ EURO STOCK | EURO | 3,879 | 137,270,550.00 | 139,178,520.00 |
| SP 500 | USD | 379 | 102,460,545.01 | 100,794,625.07 |
| TOPIX | JPY | 54 | 6,067,515.77 | 6,374,625.36 |
| FTSE | GBP | 96 | 7,907,242.94 | 7,846,543.44 |
| | | | **403,068,658.72** | **404,514,953.87** |

### Interest rate futures

Buy position

| Name | Currency | Amount | Commitment | Market value |
|---|---|---|---|---|
| EURO BUND | EURO | 285 | 34,599,520.00 | 34,724,400.00 |
| EURO BOBL | EURO | 212 | 23,941,540.00 | 23,936,920.00 |
| CBOT US | USD | 55 | 5,104,383.64 | 5,101,389.30 |
| | | | **63,645,443.64** | **63,762,709.30** |

Sell position

| Name | Currency | Amount | Commitment | Market value |
|---|---|---|---|---|
| EURO SCHATZ | EURO | -920 | –97,038,515.00 | – 96,862,200.00 |
| | | | **–97,038,515.00** | **–96,862,200.00** |

### Forex forward contracts

| Currency | Currency receivable | % | Currency payable | % |
|---|---|---|---|---|
| AUD | 156,940,477.82 | 3.13% | 19,086,493.83 | 12.63% |
| CHF | 162,539,028.09 | 3.25% | 0.00 | 0,00% |
| DKK | 10,808,817.90 | 0.22% | 4,813,952.25 | 3.19% |
| GBP | 659,408,080.28 | 13.17% | 29,426,982.55 | 19.48% |
| HKD | 61,707,602.98 | 1.23% | 10,271,701.15 | 6.80% |
| JPY | 699,833,701.08 | 13.97% | 4,997,128.25 | 3.31% |
| NOK | 25,012,203.66 | 0.50% | 2,272,348.14 | 1.50% |
| NZD | 3,002,068.75 | 0.06% | 154,132.01 | 0.10% |
| SEK | 48,106,584.49 | 0.96% | 7,487,494.39 | 4.96% |
| SGD | 25,086,791.01 | 0.50% | 860,890.01 | 0.57% |
| USD | 3,156,246,222.54 | 63.02% | 71,720,122.32 | 47.47 % |
| | **5,008,691,578.60** | **100.00 %** | **151,091,244.90** | **100.00%** |

### Other commitments

The financial terms and conditions regarding the use of the SPIRRIS software are currently being negotiated with the CDC *(Caisse des Dépôts et Consignations)*

## 18. Additional information

### Transaction on futures markets

| Securities pledged | Currency | Amount | Market value |
|---|---|---|---|
| BTF 02/09/2006 | EUR | 4,675,000 | 4,663,582.00 |
| BTF 03/09/2006 | EUR | 16,000,000 | 15,931,803.03 |
| GBR TREASURY BILL 02/06/06 | GBR | 200,000 | 289,794.79 |
| US TREASURY BILL 02/23/06 | US | 1,300,000 | 1,095,672.08 |

### Cash security deposits

| | |
|---|---|
| EUROS | 963,350.00 |
| JPY | 118,300.01 |
| USD | 4,043,915.04 |
| | **5,125,565.05** |

## 19. Prior period income

| | 2004 | 2005 |
|---|---|---|
| **NET INCOME FOR THE YEAR** | **342,220,676.78** | **725,833,407.64** |

# Statutory Auditors' report on the financial statements

## Year ended December 31, 2005

*This is a free translation into English of the statutory auditors' report issued in the French language and is provided solely for the convenience of English speaking readers. The statutory auditors' report includes information specifically required by French law in all audit reports, whether qualified or not, and this is presented below the opinion on the financial statements. This information includes an explanatory paragraph discussing the auditors' assessments of certain significant accounting and auditing matters. These assessments were considered for the purpose of issuing an audit opinion on the financial statements taken as a whole and not to provide separate assurance on individual account captions or on information taken outside of the financial statements.*

In compliance with the assignment entrusted to us by the Executive Board, we hereby report to you, for the year ended December 31, 2005, on:

- the audit of the accompanying financial statements of Fonds de Réserve pour les Retraites;
- the justification of our assessments;
- the specific verifications and information required by law.

These financial statements have been approved by the Board of Directors. Our role is to express an opinion on these financial statements based on our audit.

We hereby inform you that the financial statements for fiscal year 2004 were not audited. In accordance with article L. 135-12 of the French Social Security Code *(Code de la Sécurité sociale)*, our role was limited to an audit of the itemized statement of the Fund's assets at the December 31, 2004 reporting date.

**1 – Opinion on the financial statements**

We conducted our audit in accordance with professional standards applicable in France. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by the management, as well as evaluating the overall financial statements presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements give a true and fair view of the Fund's financial position and its assets and liabilities, as of December 31, 2005, and of the results of its operations for the year then ended in accordance with the accounting rules and principles applicable in France.

**2 – Justification of our assessments**

In accordance with the requirements of article L. 823-9 of the Commercial Code relating to the justification of our assessments, we bring to your attention the following matter:

As part of our assessment of the accounting principles used by the Fund and as described in the note "significant accounting policies", we verified the correct application of the valuation methods applied to the financial instruments in the portfolio.

The assessments were made in the context of our audit of the financial statements, taken as a whole, and therefore contributed to the formation of the opinion expressed in the first part of this report.

**3 – Specific verifications and information**

We have also performed the specific verifications required by law in accordance with professional standards applicable in France.

We have no matters to report regarding the fair presentation and the conformity with the financial statements of the information given in the management report of the Board of Directors, and in the documents addressed to the Executive Board with respect to the financial position and the financial statements.

Done in Paris and Paris-La Défense, on April 24, 2006

Constantin Associés

Françoise Constant

KPMG Audit
*Département de KPMG SA*

Isabelle Bousquié

# Asset management firms selected by the FRR (1)

at December 31, 2005

**LOT 1: Eurozone large caps, passive management**
Indicative mandate size: 1 billion euros for a period of three years
- Barclays Global Investors Limited
- Crédit Agricole Asset Management
- Vanguard Investments Europe SA

**LOT 2: Eurozone small and mid caps, active management**
Indicative mandate size: 200 million euros for a period of five years
- AXA Investment Managers Paris (AXA Rosenberg Investment Management Ltd)
- Crédit Agricole Asset Management
- HSBC Investments (France)*
- Société Générale Asset Management

**LOT 3: Eurozone large caps, active management**
Indicative mandate size: 620 million euros for a period of four years
- AXA Investment Managers Paris (AXA Rosenberg Investment Management Ltd)
- Capital International Limited
- Groupama Asset Management
- Lombard Odier Darier Hentsch

**LOT 4: US large caps, passive management**
Indicative mandate size: 640 million euros for a period of three years
- Barclays Global Investors Limited*
- Vanguard Investments Europe SA

**LOT 5: US mid caps, active management**
Indicative mandate size: 200 million euros for a period of five years
- Société Générale Asset Management (Trust Company of the West-TCW)

**LOT 6: US large caps, active value management style**
Indicative mandate size: 460 million euros for a period of four years
- DWS Investments
- Robeco Institutional Asset Management* (Boston Partners Asset Management LLC)

**LOT 7: US large caps, active growth management style**
Indicative mandate size: 460 million euros for a period of four years
- AGF Asset Management (RCM Capital Management LLC)
- Goldman Sachs Asset Management*

**LOT 8: Europe ex-eurozone large caps, active management**
Indicative mandate size: 240 million euros for a period of four years
- AXA Investment Managers Paris (AXA Rosenberg Investment Management Ltd)
- Schroders Investment Management Ltd
- Invesco Asset Management*

**LOT 9: Pacific rim large caps, including Japan and excluding emerging countries, active management**
Indicative mandate size: 240 million euros for a period of four years
- Capital International Limited
- Morgan Stanley Investment Management
- Nomura Asset Management UK Ltd*

**LOT 10: Eurozone bonds, sovereign and credit (investment grade), active management**
Indicative mandate size: 960 million euros for a period of four years
- AGF Asset Management
- AXA Investment Managers Paris
- BNP Paribas Asset Management SA
- IXIS Asset Management SA
- Crédit Agricole Asset Management*
- HSBC Investments (France)
- Robeco Institutional Asset Management

**LOT 11: International bonds pegged to inflation (2/3 euro and 1/3 international non-euro), active management**
Indicative mandate size: 480 million euros for a period of four years
- AXA Investment Managers Paris*
- F & C Management Ltd

**LOT 12: International bonds (non-euro denominated) government and corporate issuers (investment grade), active management style**
Indicative mandate size: 480 million euros for a period of four years
- Capital International Limited*
- IXIS Asset Management SA (Loomis, Sayles & Company, LP)
- Aberdeen Fund Management

(1) The name of the firm to which the contracting entity has eventually delegated financial management is indicated in parentheses when the names of this firm and of the contracting entity are different. Moreover, in accordance with regulations in force governing this RFP process, notification of the mandate awarded is binding on the FRR and will take place after the related contract has been finalized with the investment management firm whose proposal has been retained.

* Standby mandate: the FRR reserves the right to activate standby management mandates as needed, in particular with the aim of ensuring an adequate risk spread or in the event that one or more managers appointed for the same mandate is unavailable.

This annual report was produced on recyclable paper using clean printing processes.
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