Legislative Assembly of Alberta

The 27th Legislature
Second Session

Standing Committee on the Alberta Heritage Savings Trust Fund

Monday, March 16, 2009
8:01 a.m.

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Standing Committee on the
Alberta Heritage Savings Trust Fund

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Douglas Stratton	Senior Vice-President, Fund Management Group

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8:01 a.m. Monday, March 16, 2009

[Mrs. Forsyth in the chair]

The Chair: If I may, I'd like to call the meeting to order. We're very appreciative of the minister and all of her staff being here. As someone who has been in her position before, I know how busy she is. So thank you, Madam Minister.

What I'm going to do first is ask the committee members and everyone around the table to introduce themselves for the record. I'm going to start, and we'll go this way. I'm Heather Forsyth, the chair and the MLA for Calgary-Fish Creek.

Mrs. Dacyshyn: Corinne Dacyshyn, committee clerk.

Mr. Denis: Jonathan Denis, MLA, Calgary-Egmont.

Dr. Massolin: Good morning. I'm Philip Massolin, and I'm the committee research co-ordinator, Legislative Assembly Office.

Mr. Dunn: Fred Dunn, Auditor General.

Mr. Saher: Merwan Saher, office of the Auditor General.

Mr. Brown: Aaron Brown, Finance and Enterprise.

Mr. Parihar: Jai Parihar, chief investment officer, AIMCo.

Mr. Bhatia: Robert Bhatia, Deputy Minister of Finance and Enterprise.

Ms Evans: Iris Evans, Minister of Finance and Enterprise.

Dr. de Bever: Leo de Bever, CEO, AIMCo.

Mr. Stratton: Doug Stratton, senior vice-president of AIMCo.

Ms Hay: Sandie Hay, Finance and Enterprise.

Mr. Pappas: Dave Pappas, Finance and Enterprise.

Ms Kuperis: Kari-ann Kuperis, Finance and Enterprise.

Mr. Kang: Good morning. Darshan Kang, MLA, Calgary-McCall.

Mr. Campbell: Robin Campbell, MLA, West Yellowhead.

Mr. Johnston: Good morning. Art Johnston, Calgary-Hays.

Mr. Elniski: Good morning. Doug Elniski, deputy chair, MLA for Edmonton-Calder.

The Chair: Thank you.

I just want to advise everyone at the table that Ms Notley has withdrawn from the committee as of March 12, and no replacement has been appointed by the Assembly.

We're going to move on to the approval of the agenda. Can I have a motion that the agenda for the March 16, 2009, meeting of the Standing Committee on the Alberta Heritage Savings Trust Fund be adopted as circulated? Robin. All in favour? Anyone opposed? Thanks.

If I could have someone move that the minutes of the December 1, 2008, meeting of the Standing Committee on the Alberta Heritage Savings Trust Fund be adopted as circulated. Jonathan. Okay. Good.

The Alberta heritage savings trust fund third-quarter update was distributed to all members on February 26, 2009. The Alberta Heritage Savings Trust Fund Act indicates that one of the functions of the committee is to receive, not approve, and review quarterly reports on the results of the operation of the heritage fund. The minister and her departmental officials are in attendance to assist with the review. Madam Minister.

Ms Evans: Well, thank you, Madam Chair. I'm so grateful that you're so businesslike and prompt. It's helping us with a very full day today, so I'm really grateful for that.

I'm also grateful at this juncture for the first time to present Leo de Bever, whom I think we were extremely fortunate to attract. That's no credit to myself but, rather, the absolutely excellent board, of which our deputy is currently a member and which has many notables from Alberta from the entrepreneurial sector who have really strived since the 1st of last year to ensure that AIMCo is world class and carries on a proud tradition of financial excellence in management.

There have been many changes that have come into place over the last couple of years in readiness for this from Finance and Enterprise officials. For this past year, interestingly enough – although I am reporting on the heritage fund, I just want to set the context – there have been plans made by the group to locate in different premises, away from the Terrace Building, and last summer staff were taken from being staff members of the Alberta government to the AIMCo management group, which is quite different. Many of them surrendered their previously held positions in the public service to become part of an organization which we hope will become those entrepreneurial investment managers that, as one of my predecessors, the Hon. Shirley McClellan, stated, will take us to a more entrepreneurial vision of how we do our investment management.

Rather than investment management internally in Finance and Enterprise under the dome, in a manner of speaking, and with government, we have an excellent board, who have selected Leo, who started in the third week of August last year. Challenges other than human resources challenges have related to our computer management systems, our human resources, our payroll. All the kinds of things that practically a new corporation would undertake have been undertaken during this period of time.

Still, when I reported on February 26 about the third-quarter results in the heritage fund and reported that the funds were down collectively some 15 per cent in the year overall, we matched that with Norway and the Norwegian fund, for example, at between 23 and 25 per cent. The Norwegian fund was down $60 billion in September and reported just recently at a $92 billion loss. So our losses in the heritage fund comparably have been extremely good. The management in both Finance and Enterprise and in AIMCo would caution against comparators with other funds because of different mixes of assets and so on. When we get to the business plan, you'll see that there is a new schedule that has been agreed to by both Finance and AIMCo for the management of the fund, but I am very satisfied that the management of the fund for this past year, in the most tumultuous economic climate we've seen in decades, has been both responsible and responsive.

The interesting thing I could tell you as an MLA and a minister is that while I get letters about many things and criticisms about many things, as you can well imagine, it's only in the House, in fact, from a member of Her Majesty's opposition that we've had any criticism of the heritage fund because most people recognize that in both our heritage fund and in our endowments there is both a long-term strategy and savings plan. But there are also funds that are managed in the endowments that enable them to be prepared for more rapid disposal should the need arise for capital projects, et cetera. I'm very satisfied with the management that we've had in this past year and present this to you for any questions that you might have relative to the fund management.

The Chair: Do we have any questions to the minister?

Seeing none, then I need someone to move that

> the Standing Committee on the Alberta Heritage Savings Trust Fund receive the 2008-09 third-quarter report on the Alberta heritage savings trust fund as presented.

Art. Thank you. All in favour? Opposed? It's carried.

The Chair: Moving on to number 5, the revised business plan was posted on the Internet website last Tuesday. The fund's business plan must be approved by the standing committee. So, Madam Minister, if you would.

Ms Evans: Thank you very much. One of the things that the Premier's office aspired to when I became Minister of Finance and Enterprise was to make sure that we followed through with the commitment made to establish AIMCo as an entrepreneurial organization and as such reviewed the asset mix. It was also reviewed with the department, initiating a formalized review, engaging a consultant to look at the asset mix of how we spend and save our money and so on and how we manage to maximize the return on investments. You could say that this business plan is geared to maximize the return on the investments within a tolerable risk that is both prudent and bears in mind the policies and, I guess you could call it, the traditions of excellence in the financial management of the heritage fund.

8:10

We have goals and performance objectives which will continually be reviewed over this next year – for example, in the quantifying of the risks, et cetera, that the fund might undertake – but in order to really give more flexibility to this, I would call it, very sophisticated board of management and to the management that they have retained, we have to find an asset mix that gives more latitude, where you can see greater opportunities for variance within the asset mix.

If you look at the table that's included, you will see that AIMCo has been moved away from a very strict adherence to a particular type of asset mix to more latitude. If I could draw your attention to page 3 under goal 1, asset allocation, which has been posted on the web and which both Finance and the AIMCo management have agreed to, it shows some minimums and maximums with more latitude than they've had previously. Now, the targets themselves – the amount of 20 per cent, for example, in the money market, 30 per cent inflation sensitive and alternatives, and 50 per cent in equities – are not remarkably different than what it was previously. You will see that within the structure of the heritage fund this is remarkably aligned to what previously has been available, but within the various asset classes, for example, if you could take Canadian equities, they can have from as few as zero investments to up to 15 per cent in that category to reflect Canadian equities.

This gives some opportunity for the board and specifically for the management to identify what the risks are, to make sure that there's adherence to the policy, but there is more flexibility for investments within that category. If you look at 1.2, AIMCo's responsibility is to "retain investment managers who employ active management strategies." In other words, don't necessarily allow the funds to just sit there and see if they behave themselves. Their job is to add value and above the benchmark portfolio; in other words, to exceed, to meet and beat the targets. If you even look at the way that that's incented within the AIMCo management themselves, if they can do well on the targets, then obviously they will materially benefit. If they don't do well on the targets, obviously they won't. So we have defined this asset allocation and present it today in the business plan for your perusal and for questions you might ask.

On the next page, relative to risks to achieving goals and performance measures, of course, it draws to your attention that diversifying doesn't necessarily eliminate the risk of loss. That's why you hire bright people and have a bright board in place. There are more specifics about that strategy, but overall the heritage fund will continue to be managed within the prudent fashion it has been in the past but with a management team that has been challenged to do even more.

If you look to the future, my ultimate hope with this fund would be that our great-great-grandchildren will have the benefit of this fund as an operating supplement if it's necessary. "If it's necessary" would be the words that I'd like you to remember. When we come out of this period of recession and restabilize our funding, hopefully we will no longer depend on the assets in the heritage fund for operating budgets because that in the past has been one way we could have saved more. You could argue today what those savings might have achieved in the financial climate we've had, but our ultimate goal with this fund is to grow this fund to give it some options and capacity to help with the future of forthcoming generations.

Actually, with that, perhaps, because I've spoken a bit about the asset mix and allocation, I'd invite Leo to make any observations about that and then Robert from the Finance department. Leo, if you'd like to add to that.

Dr. de Bever: Sure. Thanks, Minister. Madam Chairman, I think the minister has stated very well that what we hope to achieve with this revised asset mix is a bit more flexibility to take advantage of what is a rapidly developing investment climate with both opportunities and pitfalls showing up at a greater frequency and then the time frame over which this policy is set. On page 3: by having three very broad asset classes and giving us the flexibility to move within that, that gives us maximum opportunity to deliver the best return in the long run for all Albertans.

I know some of you have been discouraged by what has been happening over the last year or so, and so am I, but the only reason we make a very high expected return on this fund is that occasionally there are years like 2008, when the risk we're taking does not have a return and, in fact, has a loss, as we experienced.

I'd like to point out that compared to the fate that has befallen others, we've come off relatively easy. Some of that is skill; some of that is luck. Part of the luck was that the Canadian dollar went down, and as a result when you compare, say, a typical U.S. fund with the typical Canadian fund, the Canadian fund typically did better if it didn't hedge its exposure. So what I'm saying is that there are a lot of things that are hard to anticipate for a manager. In fact, if we could anticipate the way the markets would move, the return that we could garner on average from being in risky asset classes probably wouldn't be there.

My team is very much intent on making the most of this asset mix and making sure that over time you can be proud of having us there to, as the minister said, provide a savings pool that you can use once the revenue from energy may have subsided, and you may have to use this to supplement the structural reliance you have in energy revenues right now.

Ms Evans: And perhaps Robert.

Mr. Bhatia: Thank you. Just a couple of very brief comments. The analyses that we did in working toward this new asset allocation framework all confirmed that the overall approach that we've been taking with the heritage fund of a significant allocation to equity investments will over the long run produce the best investment results.

Secondly, as the minister and Leo were indicating, this framework allows AIMCo more flexibility to make tactical decisions but also, in particular, more flexibility to take advantage of the opportunities in the less conventional types of assets. With respect to infrastructure, real estate, timberlands, real return bonds, and hedge funds AIMCo now has substantial flexibility to move in and out of those types of investments because many of those investment types are quite opportunistic and depend on the particular market conditions at a point in time as to what opportunities are available. That was the thinking behind the new asset allocation framework.

The Chair: Thank you.

Questions to the minister? Doug, go ahead.

Mr. Elniski: Okay. Thank you. The first question I have. If I may, I'd like to skip forward to page 7, which talks about forecasted annual investment expenses. I note a line in here in subnote 1 that says that forecasted expenses do not include external management performance fees. Then you go on later into the first main bullet there to talk about private equity and how the fees are typically more expensive. How are fees determined, where are they reported, and what do we benchmark them against to know we're getting a good deal?

8:20

Ms Evans: Now, just before Leo responds to that, if I may, there's been, I think, a determined effort to look from retaining outside expertise and contractual services to building that capacity within the organization. But on how the fees are determined and how they undergo that, Leo, please.

Dr. de Bever: There is a conventional structure in private equity, as an example, because that's primarily what we're dealing with, where the base fees are 2 per cent and the performance fees are 20 per cent of the incremental return. That structure is under pressure because it is so demanding that only the top quartile managers net-net add value. One of the prime reasons we have increased our internal capacity to deliver the same kind of investment is because with an internal team you can reduce the fees that you have to pay externally. Not only that, but you can co-invest alongside a external manager, which reduces your average fees. The reporting for those fees is done on an annual basis. I don't know exactly on what page you would find it, but we would separately record the base fees and the performance fees.

Mr. Elniski: Thank you very much.

Mr. Denis: I was also wondering about page 7. It talks about "as a percentage of fair value." It goes up this year, .38 projected to rise, I guess, marginally percentagewise, but over this amount of money that is a fair amount of coin. I was wondering if you could comment on what the rationale was for this projected increase? I presume this is similar to a management earning ratio that you would see in a mutual fund.

Dr. de Bever: Well, if you were to compare it to a mutual fund, you would recognize that 48 basis points is not a very large number.

Mr. Denis: I didn't suggest otherwise.

Dr. de Bever: The number is slightly higher than I would expect it to be at this stage, but I'll explain very briefly why it is. This fund over the last seven years has seen an underinvestment in what is required to maintain the basic structure and to have it prudently supervised. What I mean by that are systems, operations, compliance, that sort of thing. That is part of the reason that the number went up, and that's a transitional change.

The second reason it went up is that when you try to replace external management with internal management, the cost of doing so is up front because you have to build the internal capacity before you are confident enough to let loose to not use external managers. That's the second component.

I would hope that between markets going up in the long run and us being successful in replacing external management with internal management and using our internal capacity to drive down the fees that we pay externally, this number would come down.

The Chair: Thank you.

Hugh.

Mr. MacDonald: Yes. Thank you, and good morning. I'm referencing page 2. Could you please tell me who these external managers are that have been hired? I know that in the WCB annual report on their investment of over $6 billion there was a list of the external managers hired.

Dr. de Bever: Well, somewhere in our reporting there must be a list, and if there isn't, I can provide you with one. In fact, I would say that we have too many external managers. We're overdiversified. That's one of the changes we're making. We have external managers both in the area of, say, international equities, hedge funds, and private equity. Now, the specific names: they would be the likes of KKR and Goldman Sachs and people like that.

The Chair: Is this your supplemental, Mr. MacDonald?

Mr. MacDonald: Yes. Management fees, I notice, over the years have certainly increased, whether it was prior to AIMCo or now that we have AIMCo involved in the heritage savings trust fund. How much is spent on external management investment fees?

Dr. de Bever: You may have heard me say this before: we spend nine times as much on a dollar that's externally managed compared to one that's internally managed. With that kind of ratio, the incentive to build up an internal team is very high because even if you pay them very handsomely, you can do much better if you get the results, and this is what it's all about. It's not just about cost; it's also about return. That's why we're going to be very careful in replacing external management with internal management: because you want to make sure you have the capacity to deliver the same return. Does that answer your question?

Mr. MacDonald: Yes. And I will get back on the list, Madam Chairman, please.

Ms DeLong: I'm hearing two opposite messages here: one, that you're supposedly going to be cutting your costs by going to internal management and another, that external management is more expensive. It seems to me that it's quite possible for you to manage this so that you essentially move resources in at a rate that keeps your costs level and, if you were just to decide that that's what you were going to do, that it's not a totally impossible thing to do.

Dr. de Bever: Well, let me explain why that's not happening. The small component that is very high cost is the one that's increasing in this fund. So the mix of assets we invest in is shifting to what is a more expensive way of managing money in terms of cost. The reason we're doing it is not to increase the cost but to get the incremental return. What you're finding is that an expensive asset class is becoming a bigger part of the overall asset mix and that to stem the growth in costs that are associated with that, we're moving more internally. It's the balance between the two that in the short run is not yet bringing down costs but should over time.

Ms DeLong: But what I see is that you're asking for $5 million. In terms of increasing costs, is it $5 million?

Dr. de Bever: Right. But that's not due to external managers. It's due to a number of factors, including what I talked about before. For instance, in response to some of the weaknesses found by the Auditor General and by myself as well, we're fixing some of those problems, and that costs money, too. I'll give you an example. We're spending $8 million in systems this year to replace IT systems that haven't been replaced for 20 or 25 years. It's that deferred maintenance that's contributing to the overall cost.

Ms Evans: If I might just add to that, Alana, in my opening remarks about the business plan or even about the heritage fund itself this morning I've alluded to the fact that along with the extraordinary financial climate the organization is planning a move outwards. They've also been working very actively with the Auditor General's office to pick up those pieces that have been found deficient in the organization itself.

I just want to challenge all of you – I really would – to go and look at what Finance has spent on itself and managing the province's funds and managing the functions of Finance over the last five to 10 years. You'll find that, like the prudent father, they save themselves for last and take the least, so there's a lot more being requested from people that are contributing elsewhere in the organization. That has resulted in our systems being at a lesser level than many other organizations'. Our government did make a policy decision even before my time in Health to put the resources in Health and in some of those other ministries because we thought that the net benefit, for example, to both Albertans and to our government of building an electronic health record would be better in the long run. But then as a result of that, if you weed through the comments that have been made by the Auditor General, you'll find yourself in Finance with systems that are outdated and without perhaps the proper financial controls and monitoring devices, et cetera, et cetera, et cetera. You go through that litany, and that's what is bearing the bulk of the cost that Leo and AIMCo are adding this year.

The Chair: Another supplemental?

Ms DeLong: Could I have another supplemental, Madam Chair?

The Chair: One more.

Ms DeLong: Thank you very much. It seems to me that – you're absolutely right – we do need to invest in proper computer systems for this very important part of government. But what I see is just an increase in costs here. It isn't a matter of: "Okay. We're going to get this done, put this one-time investment in and get it done, get ourselves up this level, and then be up at this level here." What I see is not what should be essentially a capital cost; what I see is just increased operating costs.

8:30

Dr. de Bever: Well, aside from these transitional items, being systems, what you're looking at is sort of putting the team in place that will eventually be able to take over from external management to some degree. What you're also seeing is an asset mix that's shifting to relatively high-cost assets: things like real estate, things like private equity, things like infrastructure. They're in order of magnitude more expensive to manage, but they are also expected to return many times more than the incremental cost. So one cannot just look at cost. You have to look at the composition of assets and what it costs to manage those assets. If the asset mix were constant, you would see what you would expect to see, which is a declining cost curve, but because we're at the same time shifting the asset mix in a direction of more labour-intensive and more expensive asset classes, the cost does not go down yet.

Ms DeLong: Okay. Thank you very much.

The Chair: Mr. MacDonald.

Mr. MacDonald: Yes. Thank you very much. To the minister of finance, please. The heritage fund is forecast to lose $2.4 billion. There's no transfer of funds to the general revenue fund or no income available for inflation-proofing. On page 6 under income and expenses and forecast annual income I'm curious: what's going to happen when the fund regains a yearly income? Is it going to be used to recoup or restore the losses that have occurred, or is that income then going to go back into general revenue?

Ms Evans: Madam Chairman, if I respond to that fully, we're really getting into an area where it's a postbudget conversation. When we table our budget on April 7, I think it will become clear how we're going to manage. Obviously, we have already signalled that we will be spending from that portion of savings that was external to the heritage fund, which existed in the capital and sustainability accounts. I could undertake a more articulate opportunity at that time, as a matter of fact, and even give a written response to this group so that you'll know.

Essentially speaking, if I could quote Jack Mintz, a recession is not the time to contemplate how you're managing your savings but how you're managing to stay afloat with your operational budget until such time as you come through to the other side. I think common sense would dictate that you would rebuild your emergency savings account, and then you would look to how you manage the future of the heritage fund. I know we'll have much more conversation about that in the future.

If you look at the forecast, they're matching at a lower level what we anticipate simply because even if you look at indicators like the International Monetary Fund and so on, you don't anticipate there will be a huge recoup on our losses.

I just want to ask you all a question. If you think today of how many refineries and plants and industrial-commercial enterprises have closed down in China in the last year, you might give me an answer of a thousand, but in actual fact it's 70,000 – 70,000 – closures in China in the last year. People who are waiting breathlessly for our economy to turn around should contemplate that when we put numbers together like this for a business plan, we're looking at what our possibilities are in the face of an economy that has been struck on all parts. That's why we're not being overly optimistic in this business plan.

When I get through the budget, hopefully, we'll be able to give you an explanation to Mr. MacDonald's question that will help to at least illuminate where we're going with that.

The Chair: Thank you, Madam Minister. One of the things that I'm proud of in the short time I've been on this committee is that you've always been very good about written answers when we've had a question, so we'll look forward to that through the clerk.

Jonathan.

Mr. Denis: Thank you, Madam Chair. To the minister or one of her deputies. I think you make a good argument about the benefits of internal versus external management, but I want to talk about accountability, obviously, to the owners of the fund, being the residents of Alberta. How are the internal managers kept accountable vis-à-vis the external managers?

Ms Evans: That's a very good question. I wish Leo was another deputy, but I don't actually have that much say over his performance; it's his board, really, that does. But he does report.

I think that probably Robert could talk about the internal versus external in the past relative to the accountability today. Did you want to just touch on that?

Mr. Bhatia: Maybe I'll start it, and then Leo probably should supplement. First of all, AIMCo is responsible for the overall management of the fund, of course, within the policy that you see before you today. Then AIMCo makes the decisions as to what extent they use internal resources or hire external managers. I know from past experience that there's an extensive framework of accountability for both internal management but also for external managers. Leo, maybe you should comment on exactly how external managers are held accountable.

Dr. de Bever: Well, for external managers it's a matter of evaluating their plan against how they execute, but ultimately it shows up in how they get compensated. There are two aspects to the way we look at external managers. Are they continuing to execute the plan that we signed up for? That's the external accountability.

The internal accountability is through my board, and the board has a very strong sense of being accountable to the whole population of Alberta. In fact, I can tell you that on a day-to-day basis it's a very challenging board in terms of making sure that we stay within the risk limits that we originally accounted for. They hold me extremely highly accountable for how I run the internal team and how that team makes decisions.

Ms Evans: Could I just add one thing? I had the opportunity to meet with the board at a supper meeting. They don't seem to have social suppers; they seem to have working suppers. Charles Baillie, who is the president and chairman of the AIMCo board, looks after the discussion with the other officers. They talk a lot about risk and risk management and accountability. There's reporting to the government. There's reporting to the board that happens on a regular basis.

Relative to this move away from external risk managers to internal management – and I was thinking about Alana's questions earlier – if you look at what Leo has defined, a new type of asset mix, and what we will be paying for that and you look at the projections of the cost and the expected rate of return, that graph is very interesting because it shows that even though there are more costs built in, there is an expectation of a greater rate of return.

The board through the work of Leo and the staff along with our own staff will be looking at how we quantify risks in the future with this change in management structure. But the accountability through to the board, the accountability through to the heritage fund committee will not change. If anything, I think that you will see us become even more assertive about our quarterly reporting and our transparency of how AIMCo manages and reports back through to you.

Mr. Denis: Just one supplemental, Madam Chair. Were the contracts with the external managers at the end of their life, or were they terminated early, and if they were terminated early, were there any termination fees associated with them?

Dr. de Bever: The contracts. We simply inherited both the assets and most of the staff and the contracts that AIM had in place before it became AIMCo. We are in fact winnowing down the range of managers we employ, but that had nothing to do with either their cost or the transition from AIM to AIMCo. This happens in the normal course of business. It's more a question of not hiring additional managers to manage incremental assets rather than terminating managers although some of that is involved as well.

8:40

The Chair: Mr. MacDonald.

Mr. MacDonald: Yes. Thank you. I would like to go back at this time to page 6, income and expenses. In 2010-11 and 2011-12 and as we look also at this fiscal year, you leave those forecasts blank. Again, am I to assume that there will be no transfer in the next two and a half years to the general revenue fund from the heritage savings trust fund, nor will there be any amounts retained for inflation-proofing of the fund?

Ms Evans: That'll be in the budget.

Mr. MacDonald: That'll be in the budget. You can't answer that today.

Ms Evans: No. Hugh, you wouldn't want me carted off to jail.

Mr. MacDonald: No. The thought never occurred to me.

Citizens certainly would be interested to know. I find it surprising that those lines are just left blank.

The Chair: If I may, those will be in the budget, and you will have the opportunity after the budget is tabled to ask all sorts of questions like that.

Mr. MacDonald: Interesting. Thank you. Can I get back on the list, Madam Chair, please?

The Chair: You can go ahead right now.

Mr. MacDonald: Okay. I had an additional question. It's on the asset allocation, page 3. Infrastructure is listed as 2.8 per cent of the actual asset mix. Could I have a list, please, through the clerk to all members, of the investments that we have in infrastructure projects?

Dr. de Bever: I'm sure I could provide you with that. Did you have any particular thing in mind?

Mr. MacDonald: Well, on page 4, the second paragraph from the bottom, private income investments such as infrastructure investments, bridge loans. I would just like to have a look at all of that, if you don't mind, please.

Dr. de Bever: No. I can give you a list. I can also tell you that, relatively speaking, those assets have done quite well. What hurt us last year is two things: equities and credit. Infrastructure and real estate, by comparison, have been relatively good performers.

The Chair: Leo, if you could provide that information through the clerk. Thank you.

Mr. MacDonald: I'm just curious if these are all or part of a 3P project.

Dr. de Bever: Some of them are 3Ps.

Mr. MacDonald: Thanks.

The Chair: Jonathan.

Mr. Denis: My question has been answered. Thank you.

The Chair: Are there any other questions from the floor? Seeing no other questions, I have one question, if I may, as the chair. That goes to page 2 under fund governance. In the second paragraph it says:

> When investing the assets of the Fund, the Alberta Heritage Savings Trust Fund Act requires the Minister to adhere to investment policies, standards and procedures that a reasonable and prudent person would apply in respect of a portfolio of investments to avoid undue risk of loss and obtain a reasonable return.

I'm assuming that same thing applies to you?

Dr. de Bever: We run the fund. The board runs the fund on a prudent-man principle, so it's delegated authority. That's the way the structure was envisioned, that the government through the minister delegates to an independent board to make decisions that are devoid of politics and are solely focused on prudent-man investment principles.

The Chair: If I may, prudent can mean a lot of things to a lot of people. How do you define prudent?

Dr. de Bever: Prudent, the way it has been interpreted, is that if it were your own money in some sense, would you consider this to be an unreasonable risk? The difference with managing money for someone else is that you have to take an extra duty of care. In other words, if you were Warren Buffet and you were playing with your own money, you could afford certain risks that you wouldn't take if you were managing money on behalf of other people. That's where the prudent-man principle comes in: you're extra careful in making sure that you satisfy your obligation to that external party.

The Chair: Thank you very much.

Mr. Kang: My question is about the loss in the heritage fund of 15 per cent, in what investments that loss occurred, and what is happening to those investments. Are we still leaving money in those investments, or are we moving the money out of those investments where the loss occurred? What is happening with those investments?

Ms Evans: Just to reiterate, Madam Chair, this is, I think, the question that Mr. Kang has posed: with the losses what was the asset mix in those losses particularly? What has happened to them? We've had quite a bit of conversation about that at other tables, but did you want to just give a high-level overview?

Dr. de Bever: Well, you can do two things in investing. You can stick money in a savings account, and you'll get a low return, but you'll not have any high risk of principal loss. Or you can go into equities or corporate bonds and take more risk, which on average will pay you a return but at times, that you cannot predict, will give you a loss. The year 2008 was a year where investing in corporate credit and in equities was not particularly beneficial. In fact, it incurred a large loss. Equity markets lost 40 to 50 per cent, depending on where you were invested. Credit relative to, say, government bonds lost in part because the banking system collapsed and caused certain corporations and banks to collapse along with it. To summarize, the 15 per cent loss in large part came from corporate credit, and it came from equities.

It's not something that happened because managers were imprudent or they did something they shouldn't have done. It's that the markets are very volatile. That very volatility in the long run creates a gain, a net excess return over what you would expect if you were to put your money in a savings account, but in particular years – and 2008 was sort of a 1 in 25- or 1 in 50-year event – you don't make money, and you lose money. That's the source of the loss. That's why in some sense it's very difficult to say, going forward, that you should make changes because of what happened in 2008. That's the very nature of a long-term investment policy; if you stick with it, in the long run it will pay off.

Mr. Kang: My supplemental is on the same question. What are the projections? You know, will there be a 10 per cent loss or a 5 per cent gain?

Dr. de Bever: In a market where equities move up or down 5 per cent a week, it is very hard to predict what is going to happen. We suspect that this year will be a tough year, but at some point either late this year or next year certain equity markets will start to turn around. We think that corporate interest rates, which have gone from unreasonably closely balanced with government rates to very different from government rates, very much higher – that differential will narrow, which will translate into a gain for us on our corporate credit holdings.

So where will things go, and where will the return come from? If I knew that with any accuracy, we would all be a lot richer. In general terms, over the next 10 years I would expect that equities will do substantially better than most fixed-income investments and that the average return will more than compensate us for the risk that we're taking in this asset mix.

Mr. Kang: I was just asking you to look in your crystal ball.

Dr. de Bever: Oh. You want to get some personal investment advice.

Mr. Kang: Thank you, sir. Thank you.

The Chair: Thank you.

Seeing no questions, I need someone to move that the Standing Committee on the Alberta Heritage Savings Trust Fund approve the business plan as circulated.

Mr. Elniski: So moved.

The Chair: All those in favour? Opposed? Carried.
Thank you, Madam Minister.

Ms Evans: Thank you very much.

8:50

The Chair: Thank you to your staff, also.
Has everyone had a chance to review the memo from the Minister of Finance and Enterprise regarding the number of hits on the heritage fund section of the Alberta Finance and Enterprise website? Does anybody have any questions?
Seeing none, we'll move on. A copy of the committee's 2009-10 budget was posted on the internal website for committee members. The status quo budget has been approved by the Special Standing Committee on Members' Services. Therefore, this document is provided for information only.
Other business. I just want to raise one additional item. At the committee's December meeting the minister offered to provide committee members with AIMCo's economic update. These have been regularly posted on the internal website. Do members wish to continue this process?

Mr. Elniski: Yes, please.

The Chair: Yes? All right.
Is there any other business that members would like to raise?
Seeing none, we'll move on. The next meeting will be held at the call of the chair for the purpose of deciding the location for this year's public meeting and approving the heritage fund's 2009 annual report. The annual report must be approved by the standing committee and distributed to all members by June 30, so I anticipate this meeting to be held in early June.
I'd like a motion to adjourn. Art. Thank you.
Thank you, everybody. Again, great job.

[The committee adjourned at 8:51 a.m.]

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