Legislative Assembly of Alberta

The 27th Legislature
Fourth Session

# Standing Committee on the Alberta Heritage Savings Trust Fund

Wednesday, June 22, 2011
9 a.m.

Transcript No. 27-4-2

**Legislative Assembly of Alberta**
**The 27th Legislature**
**Fourth Session**

**Standing Committee on the**
**Alberta Heritage Savings Trust Fund**

Tarchuk, Janis, Banff-Cochrane (PC), Chair
Elniski, Doug, Edmonton-Calder (PC), Deputy Chair

DeLong, Alana, Calgary-Bow (PC)
Forsyth, Heather, Calgary-Fish Creek (W)
Groeneveld, George, Highwood (PC)
Johnston, Art, Calgary-Hays (PC)
MacDonald, Hugh, Edmonton-Gold Bar (AL)
Quest, Dave, Strathcona (PC)
Taft, Dr. Kevin, Edmonton-Riverview (AL)

**Department of Finance and Enterprise Participants**

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| Nick Kaczmarek | Public Affairs Officer |
| Rod Matheson | Assistant Deputy Minister, Treasury and Risk Management |

**Alberta Investment Management Corporation Participants**

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| Leo de Bever | Chief Executive Officer and Chief Investment Officer |
| Pine Pienaar | Senior Vice-president, Client Relations |

**Auditor General's Office Participant**

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**9 a.m.** **Wednesday, June 22, 2011**

[Ms Tarchuk in the chair]

**The Chair:** Good morning, everyone. I'd like to call this meeting to order and welcome everyone.

I wonder if we could just go around the table and have all of the committee members, the representatives from Finance and Enterprise, the office of the Auditor General, and AIMCo introduce themselves for the record. Maybe we'll start with you, Doug.

**Mr. Elniski:** Yes. Good morning. Doug Elniski, MLA, Edmonton-Calder.

**Mr. Johnston:** Art Johnston, Calgary-Hays.

**Mr. Groeneveld:** George Groeneveld, Highwood.

**Mr. Pienaar:** Pine Pienaar, AIMCo.

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

**Mr. Matheson:** Rod Matheson with Alberta Finance and Enterprise.

**Mr. Babineau:** Rod Babineau, Alberta Finance and Enterprise.

**Mr. Brown:** Aaron Brown, Finance and Enterprise.

**Ms LaFave:** Betty LaFave, office of the Auditor General.

**Mr. Kaczmarek:** Nick Kaczmarek, Alberta Finance and Enterprise.

**Ms Sales:** Tracey Sales, Legislative Assembly Office, communications.

**Mr. MacDonald:** Hugh MacDonald, Edmonton-Gold Bar. Good morning.

**Mrs. Dacyshyn:** Corinne Dacyshyn, committee clerk.

**The Chair:** Thank you.

Heather, you're on the phone?

**Mrs. Forsyth:** Yes. Hi, everybody. Heather Forsyth, Calgary-Fish Creek.

**The Chair:** Thank you very much.

Both Dr. Taft and Alana DeLong have sent their regrets that they're unable to attend this morning's meeting.

You all have a copy of the agenda, and I wonder if someone could move the agenda for Wednesday, June 22.

**Mrs. Forsyth:** I'll move that.

**The Chair:** Thank you very much, Heather.

All those in favour? Any objections? That motion is carried.

You have the minutes of our last meeting, so I wonder if someone could move that the minutes from March 22, 2011, be approved. Art. All those in favour? Any objections? Not seeing any, that motion is carried.

The draft 2010-11 annual report was posted on the internal website last week. I'd like to just remind members that the draft copy is confidential and that once it's approved by the committee, final copies will be printed and distributed to our colleagues. In order to meet the requirements of the Alberta Heritage Savings Trust Fund Act, the annual report must be approved by the standing committee and distributed to all MLAs by June 30.

At this point I'd like to turn the floor over to Rod Matheson, assistant deputy minister, to review the report.

**Mr. Matheson:** Thank you, Madam Chair. Good morning to you and the members of the committee. The minister sends his regrets on being unable to attend today. I'm pleased to be here this morning to provide the committee with an overview of how the heritage fund performed over the fourth quarter and, more importantly, over the year as a whole for 2010-11. It was largely a good-news story for fiscal 2011; however, there is still a lot to be cautious about going forward.

The fund earned just over $1 billion for the 2010-11 fiscal year. Of this, $360 million was retained in the fund for inflation-proofing and the remainder was transferred to the general revenue fund in accordance with the heritage fund act. Actual income for the fund exceeded the budgeted income by $104 million. The fund ended the fiscal year with a fair value of $15.2 billion, up from $14.4 billion at year-end 2010, and the fund had a one-year return of 10.4 per cent.

Returns for the heritage fund were strong across the board. Canadian equities led the way with a 19.9 per cent return, while real estate was also a strong performer at 13.4 per cent for the year. The lowest performer was fixed income at 6.9 per cent; however, that's still a good return for that asset class, and you would expect fixed income to have a lower performance in a strong market. AIMCo met its value-added target of 1 per cent, with the strongest value-added areas being global equities and real estate.

Looking at different time periods tells an interesting story about the heritage fund. The past two years have been very good as the fund had a two-year annualized return of 14 per cent, which far exceeds our long-term capital market expectations. However, looking over a longer horizon, the five- and 10-year returns are 3.5 per cent and 5.3 per cent, respectively. This shows how a bad year such as 2008 can negatively impact a fund for years to follow.

Looking ahead there continues to be a lot of uncertainty in the market. The debt situation in some European countries such as Greece and Ireland continues to raise concerns. There are even some commentators speculating about a possible credit-rating downgrade for the U.S. This demonstrates the full effect of the credit crisis, and the resulting stimulus measures have yet to be seen. A period of increased inflation is a real possibility given the amount of economic stimulus that has been pumped into global markets. While the fund has had consecutive double-digit returns, it would be wise not to expect that going forward. As such, the heritage fund remains a globally diversified portfolio that is focused on long-term returns that will meet or exceed the policy target of CPI plus 4 and a half per cent.

I'd like to just talk for a minute about the annual report itself which the committee is considering because we've restructured it somewhat. This year we've tried to better tell the story of the heritage fund so that it's more accessible for Albertans. We've enhanced the graphics as well as added sections up front on areas such as governance, investment strategy, and risk. As well, we've condensed and improved the first page highlights so that someone who wants to only read one page can really get all of the critical information in a concise manner, but the further into the report that Albertans read, the better they should be able to understand how the fund is invested, who is responsible, and how it performed. We certainly hope the committee finds the new format more accessible, and we welcome any feedback.

With that, I'll end my comments, and we welcome your questions.

**The Chair:** Okay. Any questions?

**Mrs. Forsyth:** I have a couple, but I don't need to go first.

**The Chair:** That's okay, Heather. Go ahead.

**Mrs. Forsyth:** Thanks, Rod, for your information. I'd like to ask you a couple of questions, three if I can, or I'll just go back on the speakers list. In your comments you talked about it being largely a good-news story, but you provided some cautionary notes on that. Can you explain that?

**Mr. Matheson:** The cautionary notes were really just meant forward looking – and certainly Leo may want to supplement this – that while the outlook is generally positive, it was just meant to say that, you know, there are some shadows on the horizon that we have to be cautious of. It's not entirely a rosy outlook.

I don't know, Leo, if you want to add anything?

**Dr. de Bever:** Well, as you said, the returns that we saw in the last two years certainly aren't normal. They're above average, just like 2008 was way below average. Because the attempt to solve the last crisis has involved the injection of a lot of liquidity, which has boosted equity markets, I'm a little nervous that it's too much of a good thing and at some point it's going to catch up with us. We're probably halfway through a normal five-year equity cycle, but if I had to make a bet – and it's always hard to make bets on short-term returns on equity markets in particular – I wouldn't think that 10 per cent for the next couple of years is going to be normal.

So far this year – and I'm talking calendar year; I don't have the fiscal year numbers – we only have a nominal return of 2 per cent for six months. So that shows you how volatile markets are, and that's pretty typical for a fund with a structure of our size.

The other thing I would caution is that the bond market, as Rod was saying, has had a tremendous return, even last year. It has had a tremendous return for 30 years because of generally declining interest rates. That can't continue, so at some point bond returns are going to be very disappointing. We just don't know when.

**Mrs. Forsyth:** May I do a couple of follow-ups, Madam Chair?

**The Chair:** Yeah. Go ahead, Heather.

**Mrs. Forsyth:** Okay. I wanted to ask – we're hearing a lot of terrible stories, I guess is the only word I can think of, with what's happening in Greece. Are there any effects to us on that?

**Dr. de Bever:** First of all, you should understand that Greece is a country with 18 million people, so it's relatively small in the European scene, but the discussion of Greece has had an enormous psychological impact on a number of other markets.

One of the things it has done is it has reduced the currency, the euro, in Europe, and that has made it more competitive relative to other jurisdictions, including North America. So that has been a benefit particularly to northern Europe, and it would compete with eastern Canada.

The strong demand for resources world-wide has helped Alberta so far. There seems to be a bit of a slowdown in economic growth in China that may affect that negatively, but overall I think western Canada, in particular, has been very well positioned in the current environment.

Yes, the headlines are scary. Yes, the debt levels in Greece are not sustainable. Yes, as Rod was saying, the debt levels in the United States are pretty scary. At some point we may see repercussions for that in terms of higher interest rates, particularly for the U.S. but eventually for Canada as well, which would impact our economy because, obviously, a higher cost of credit would make it harder to keep the economy going. In fact, the biggest issue from an economic standpoint is the absence of a really strong investment boom or a recovery of investment because it is ultimately the thing that's going to take over from what started out as a crisis generated by excess consumption, and so far that hasn't happened.

***9:10***

**Mrs. Forsyth:** I'll go back on the speakers list, Madam Chair. I don't want to tie up the whole committee.

**The Chair:** Okay. Thanks, Heather.

Before I move on to Hugh, I just want to note for the record that Member Dave Quest has joined the meeting. Good morning, Dave.

Hugh.

**Mr. MacDonald:** Yes. Thank you, Madam Chair, and good morning, everyone, again.

Mr. Matheson, when I look at the amount of money that is to be transferred to the general revenue fund of $720 million and we see an amount retained for inflation-proofing of $360 million – in my view, it is about time we started to inflation-proof the fund – when I compare this number to the third-quarter fiscal update, which indicates that it was anticipated that the heritage savings trust fund would provide $817 million to the general revenue fund, is that $817 million number in the third-quarter update net of what is anticipated to be used for inflation-proofing?

**Mr. Matheson:** Yes. That would have been comparable to the $720 million. That would have been after inflation-proofing.

**Mr. MacDonald:** So am I correct in assuming that we are almost a hundred million dollars less than what was anticipated in the third-quarter update in revenue submitted to the general revenue fund?

**Mr. Matheson:** Well, it would have been a combination of the investment income – the actual investment income would have been lower than what we would have been forecasting at third quarter because we would have had the whole fourth quarter of what happened in the capital markets that, you know, we would have had to take into account. Plus, inflation ended up being higher than the forecast we were using, so the net amount of the GRF would have been affected by both of those.

**Mr. MacDonald:** So Mr. Snelgrove will have $97 million less than anticipated at the end of the third quarter, correct?

**Mr. Matheson:** That would be correct, yes. Well, no – sorry – not in terms of what was transferred to the GRF because the full amount of the investment income is what is captured in the province's financial statements, in the income statement. What we're talking about is the net amount of cash that's transferred to the general revenue fund. So in this case for 2011 the entire investment income of $1,080,000,000 will be captured in the government's final year-end results for 2010-11.

**Mr. MacDonald:** Okay.

**Mr. Matheson:** It's just the cash that will be transferred to the GRF is less because of the amount that's retained in the fund for inflation-proofing.

**The Chair:** Okay. Doug.

**Mr. Elniski:** Thank you very much. Good morning, gentlemen, and thank you very much for the new format to the report. I like it quite a lot.

Leo, if I could get you to just expand a little bit on the market commentary, particularly the thoughts that the U.S. recovery is proceeding firmly, and then the concern you have with potential for policy mistakes by other governments. I'm just curious as to, first of all: where are you on the firm recovery in the U.S.? The second thing is: what, alternatively, does it look like when you talk about policy mistakes by other forms of government?

**Dr. de Bever:** Well, the market commentary came from Finance.

**Mr. Elniski:** Oh, okay. I'm sorry. The way it was written, I thought it was yours.

**Dr. de Bever:** No. But I think there's a serious question there. Growth is not enough in North America to make a dent in unemployment. Now, Alberta doesn't have a serious unemployment problem – in fact, we'll probably have a skill shortage before too long – but the rest of North America does have relatively elevated unemployment, 8 or 9 per cent. To make a dent in that, you have to grow for a sustained period at about 4 per cent a year. Growth for the next year is probably going to be half of that, so that is a serious issue. The attempt to solve that problem and to goose up the economy with liquidity is, in my mind, a questionable long-term strategy, and there are a lot more people now of that view than there were six or 12 months ago.

You may have heard of QE2, quantitative easing, and now there's some discussion of whether we need a third chapter on that, QE3. Basically, the reason I don't think it will work in the long run: it involves the government buying long-term debt when its issuance of long-term debt is enormous because of deficits. So it seems like a shell game when you look at it. Something real has to happen in the economy to get us out of this, and that real thing has to be, in my mind, a reconfiguration of final demand from consumption to investment. That has a secondary effect of building more capacity that allows the economy to grow going forward. Now, in terms of investments I think Alberta is probably contributing its share, but we're a very small part of the North American economy.

That's the fundamental weakness that we see right now, that corporations are sort of watching slow growth and saying: well, I'm not going to put my dollar down until I am reasonably assured that this economy is going to take off. It's a catch-22. Unless investment takes place, the economy is not going to take off, and they're not going to invest until the economy does.

Policy mistakes would be to continue to inject so much liquidity that the eventual resolution of this will involve a lot more pain in the form of debt and inflation than it should.

**Mr. Elniski:** Thank you.

**The Chair:** Heather.

**Mrs. Forsyth:** Thanks. I'd like to ask a question about your investments in the Asian market. Are you investing in the Asian market?

**Dr. de Bever:** We have an exposure to emerging markets, which includes Asia. It's a relatively inefficient market, which in the long haul should have a very attractive return, on the notion that rapid growth creates equity opportunities. In the short run that doesn't always follow.

We've been very cautious on emerging markets, and that has been justified by the latest pullback in that market. In other words, what tends to happen in growing markets is that people get carried away with the idea of growth rather than the reality that it makes money for investors. Those markets tend to be a lot more volatile because they are a lot more subject to sentiment than some of the more mature markets.

**Mrs. Forsyth:** So at this point you're really not looking at investing in the Asian market?

**Dr. de Bever:** No. We do have a base exposure. The way it works is that Finance gives us a target policy that includes global equities, and global equities includes emerging markets. So we do have a base exposure that reflects the weight of emerging markets in total global equity markets, and then we make the decision as to whether to maintain that target weight or to make it lower or higher. So right now we're a bit cautious.

**Mrs. Forsyth:** Sorry. I'm just flipping. I think it's page 17. Maybe you can explain the top five infrastructure holdings. I'm not sure if I understand what that is. You've got some in the U.S., Australia/U.K., the U.S., Spain, and the U.K. Can you maybe explain to me what that is exactly?

**Dr. de Bever:** Well, infrastructure holdings are designed to have sensitivity to inflation and a return that is sort of between stocks and bonds. Our pension funds in particular like it because it is one step up from the true asset that matches their liabilities, which is inflation-indexed bonds. Puget Sound is a regulated utility, so it has the characteristics of real return because it's regulated and its revenues tend to go up with inflation. That's the attraction there.

Let me see what else is in there. I mean, obviously there are some energy projects in there. Pipelines have the same characteristic. As long as you keep the pipeline operating, as long as traffic is going through the pipeline, you generate revenues, and it tends to be fairly stable from a real return point of view. Thames Water is a water utility in the U.K. A lot of the water sector in the U.K. is privatized, and it, for instance, is right now putting new water systems and sewer systems under the city of London. Again, the regulated rate of return on those kinds of assets is somewhere between stocks and bonds.

*9:20*

**Mrs. Forsyth:** Okay. Thanks, Madam Chair.

**The Chair:** Thanks, Heather.
Hugh.

**Mr. MacDonald:** Yes. Thank you very much. Mr. Matheson, I would like on behalf of my colleague Dr. Taft from Edmonton-Riverview to thank you for the information that you provided as a result of his request from the March 22 meeting this year. Your calculations on the valuations of the heritage fund based on fair market value certainly are interesting. It's quite sobering to look at this, to realize how much value over the years has been lost in the heritage savings trust fund. For instance, in 1980-81 the inflation adjusted per capita fair market value for each and every Albertan would have been $2,371, and in 2009-10 that has shrunk to less than a thousand dollars inflation adjusted per capita.

The hon. Member for Edmonton-Calder was talking about policy mistakes being made. Well, my first question to you would be: how much money would have been added or could have been added or should have been added to the heritage savings trust fund over the years just so that it could maintain its value if you factored in inflation adjustments? What are we looking at here?

**Mr. Matheson:** Well, we don't have that figure at our disposal here. If you'd like, we could do that calculation and bring it back. Through the chair we could provide that information if we make sure we understand the question so that we can get back to you.

**Mr. MacDonald:** Yes. What amount would we have to have currently? For instance, if over the years we had adjusted our heritage savings trust fund for inflation, what would be the amount that would be for us today? I find it incredible. People don't realize that the heritage fund in book value has shrunk so much. Even if you look at the book value in millions of dollars today at $13.8 billion for 2009-10, if you adjust that value for inflation, it's less than $4 billion. Citizens of this province, you know, know they have rainy-day fund, but I don't think they realize just how little money there has been set aside over the years.

**Mr. Matheson:** We will be happy to do that calculation. Like we've done in the past, we will send the answer back through the chair.

**The Chair:** Thank you.
Doug.

**Mr. Elniski:** Thank you. I just have an infrastructure question as well with regard to the Autopista in Chile. That's quite a significant road investment. I know that they were looking for I think it was $250 million for the construction cost for that particular road. What are we into it for, and what did the return on that particular investment look like it was going to be?

**Dr. de Bever:** Well, the way the seller reported that transaction is obviously to make it look like a very good transaction from their point of view. But that was $250 million a long, long, long time ago. If you put a normal return on it, you get the kind of number that we paid for it.

There's another factor that they don't mention, that one-third of the uplift came from currency realignment. In other words, Chile is an emerging economy. It's doing a lot better than it did when this road first was constructed. So in current dollars it's worth a lot more simply because of the currency.

The story of Autopista, though, is an interesting one as to why the heck we did go to Latin America to find these kinds of assets. We like to go to economies that have such a need for social infrastructure that they're very good to investors supplying the capital. So our return going forward should be, as I indicated before, somewhere between stocks and bonds, maybe a bit higher. That would be somewhere in the real 4, real 5 CPI adjusted rate of return. It might be better.

To show you how important that road is to Chile – as you know, Chile is a country that has a lot of earthquake risk – the contract specifies that if there ever were to be an earthquake that damaged this road, the government would compensate us for 80 per cent of the construction cost, or the rebuilding cost. The other 20 per cent is provided for by normal insurance that we already have. We look for these kinds of assets in countries that are very respectful of property rights and investor rights because ultimately that's what you want us to do, to bring as secure a rate of return for the heritage fund as we can find. So it's part of our inflation sensitive allocation, and that's where it belongs.

That one and the timberlands transaction are probably indicative of where we are going to go with AIMCo over the years now that we have the capacity to do these things ourselves. Don't underestimate what that means. I'll give you an example. The avoided transaction costs on that timberlands transaction was 7 per cent of the face value of the transaction. That simply means that having the expertise onboard to evaluate these investments ourselves rather than having to pay for it through intermediaries has that kind of an impact. That one, actually, in the long run might surprise us much more on the upside.

This is all by way of saying that when we get our marching orders as to what kind of assets to buy, we're very cognizant of that, and I think that over the last three years we've built the capacity to have the net return on these assets be a lot higher than it used to be when we farmed these kinds of mandates out to external managers.

**Mr. Elniski:** Good. Thank you very much.

**The Chair:** Hugh.

**Mr. MacDonald:** Yes. I have a number of questions. Thank you, Madam Chair. The first one is to Dr. de Bever. Is AIMCo currently involved in any discussions on providing a financial package or a loan package to the proposed arena in downtown Edmonton?

**Dr. de Bever:** I'm not a great fan of arenas as an investment object. That's my bias as an economist. I took a course once where they went through all the horror stories of arenas.

You know, at some point if the city wants to build an arena because of civic pride or whatever or because it reaches an agreement with Daryl Katz, that's their business. We are only associated with that whole downtown renovation project to the extent that there are pieces that make economic sense. There are a couple of buildings that might be built around that whole redevelopment that do make sense from an economic standpoint. That's my mandate. I'm not a nation builder or a city builder. You gave me marching orders to take the money in the heritage fund and make it grow, and that's what I'm doing. So we're not involved in that.

**Mr. MacDonald:** Okay. Thank you.

Mr. Matheson, I would like to express my gratitude to you for the information you provided prior to this meeting on the principles for responsible investment. I note that, first off, for the Norwegian government pension fund, their heritage fund, which is worth well over $500 billion at the moment, they certainly have guidelines for responsible investment. We are a partner in the United Nations agreement to provide an ethical investment guideline if you can call it that.

My first question would be to you. How many investments do we have in the Alberta heritage savings trust fund that for reasons of, for instance, ethical exclusion – I'm sorry about this, but the investments that the Norwegians would consider unethical: do you have any idea what value there would be in those amounts here in our heritage savings trust fund?

***9:30***

**Mr. Matheson:** Again, I would be happy to get back with specifics. I can tell you that we've looked at that from time to time in the past, and I'll say that it's very small, but that's not an adequate answer. I'm happy to get back to you. We'll look at that. It'll require a specific comparison, for example at year end, to what is on the Norwegian exclusion list, I guess, and we'll look to see if any of those are in the heritage fund and what the value would be.

**Mr. MacDonald:** If it's a very small amount, I can't understand why we wouldn't get rid of those investments. The Norwegians are talking about corporations, for instance, that produce cluster munitions, nuclear arms, tobacco products, and corporations that have severe environmental issues or problems in some of their facilities. If it's a small amount, I can't understand why we wouldn't abide by the United Nations or any other principles for responsible investment and simply get rid of these investments.

**Dr. de Bever:** Mr. MacDonald, you're making the assumption that the Norwegians are the sole and only judge of what is ethical investing.

**Mr. MacDonald:** No, I'm not. The United Nations has a clear directive on this as well, and this country is a signatory to that. I'm not making any assumption whatsoever about the Norwegians, but I do admire their investment strategies, and I do admire the fact that they have with their oil and gas production saved considerably more than we have in our heritage savings trust fund.

**Dr. de Bever:** Well, let me address the only issue that pertains to me. I mean, what policy was in Norway and what it is here: that's not for me to decide.

We don't have any cluster bombs, but you have to understand that by Norwegian standards or some very strict ethical investment standards most of the mining industry in Canada would be off limits to a strict ethical investor because of the damage it does when you dig a hole in the ground. So you have to be really careful because I was in Norway not too long ago to discuss this exact issue, and even they have trouble sometimes defining what they should exclude and where they should work with companies to do whatever needs to be done in a more responsible manner.

I mean, you can't be holier-than-thou. If you want iron ore, you're going to have to dig a hole in the ground and find it. If that does environmental damage, you have to trade off that damage against, you know, the fact that society needs the resources at issue.

I would tell you that 80 per cent of ethical investing is just plain common sense. In other words, if you have a company that is environmentally or ethically challenged, it just doesn't make a good business risk. So in a lot of cases you avoid those companies for that reason, for strict economic reasons, not because you have very, very extreme views on ethical investing. We are a signatory to the UN PRI. We take it seriously, but there is always a shade of grey.

I'll give you an example. I was discussing Monsanto with Norway. Initially they put Monsanto on the restricted list because Monsanto was employing child labour in a testing facility in India until they realized that young children in a country like India are a natural part of the economy. So this trade-off ultimately became that they provided educational facilities that would allow children used part-time in these facilities to get the education that would get them out of the bind they're in.

There is no black and white. There's a lot of grey, and when we look at specific investments, we're quite aware of that. It's always a thin line between: can you work with companies to mend their ways, or do you put them on an exclusion list?

**The Chair:** George and then Dave.

**Mr. Groeneveld:** Thank you, Madam Chairman. I'm going to start out with a comment I have on some of the line of questioning and what my colleague across the way here mentioned. I'm going to go back to the dollar figures we would have needed to come up with to inflation-proof.

I question the relevance of that question. That's something in the past, and why would you need that number? It would strictly have to be for a political reason of some kind, to beat someone over the head with. I just think we should be moving forward, where we're at from today. I really have no problem with your last question if you indeed have that concern. I think it was well answered.

When you come up with a 10.4 per cent rate of return, I think most of us probably rush to our investment person and say: what the heck have you been doing in this world when this can happen? This is great. You probably set yourself up because it's probably not sustainable, and I think you've pointed that out very well. Since I've been here, I think we've made a lot of changes. Since we've had this chairman, we've made a lot of changes. I think we've been moving forward, and I'm pretty proud of how we've done that. So I wouldn't be criticizing an awful lot where it's been moving from there forward.

I guess my question would be that at the end of the day here you've shrunk the Canadian investment portfolio somewhat when it seems to be that the safest place to be right now is within our own country. I see that a lot of the private ones are now pulling back in U.S. investment, and I think you've probably explained pretty well your concerns out there. Would you feel it's safer to stay back into the Canadian investments at this particular time, or are we then shoving too many eggs into one basket?

**Dr. de Bever:** We had a discussion with Finance over this issue, and I think there are some good arguments on either side. The argument for having a lower allocation to Canadian equities is that Canadian equities are basically finance, resources, and technology, right? Alberta has a big exposure to the resource part of that. As a matter of diversification you can make the case that we should be underweight in Canadian equities because the province already is exposed through the rest of its balance sheet to the resource part.

The alternative argument is the one you make, that right now there are worse markets to be in than Canada. I think the agreement that we ultimately reached recognizes both sides of that argument. So we have a higher allocation to Canadian equities than a theoretically pure number would be. I think it's quite justifiable to keep it that way because as I've said on a number of occasions, Canada and western Canada in particular are very well positioned to take advantage of the demand for food, energy, and materials that Asia will require to keep growing the way it has been.

**Mr. Groeneveld:** Good. Thank you.

**The Chair:** Okay. Dave and then Heather.

**Mr. Quest:** Thank you, Chair. I'd also like to make a comment, too, because there have been a number of comparisons made this morning, and Norway has come up a couple of times. Just a reminder: Norway has a 20 per cent sales tax, a 1 per cent asset tax, and some of the highest corporate and personal income taxes in the world, and it's a federal system, so I don't think it's really realistic to make comparisons. Looking at the rate of return, we've seen it over 10 per cent. You guys have done a phenomenal job, so thank you for that.

My question. Looking at how other economies impact ours – Greece, Ireland, Iceland, and of course the U.S. – you made mention earlier about what that debt will do, the inflationary pressures and so on. I'm just wondering how you see that impacting our fund going forward a year ahead, two years ahead. What do you think might happen with inflation, and what is that going to mean to us?

**Dr. de Bever:** All right. I think the longer we keep pushing liquidity into the economy in an attempt to make it grow, the bigger that wave of debt is going to be and the more severe the inflationary pressure will be. If you look one or two years out, it's quite possible that the party will continue to some degree. I have this horrible feeling that, say, if I look five years out, the debt market in particular will fall on hard times, and that initially will probably hit equities as well. If you took a 10-year view, I'm not sure whether I would want to be in debt rather than in equities. I think maybe on balance, being in equities, which traditionally are a higher risk asset, wouldn't be a better place to be. So, yes, there are repercussions.

***9:40***

It's amazing how hard it is to predict the timing of all of this. Just go back to 2008. How many of us really had an inkling that things were going to get as bad as they did? The numbers were there in front of us. We just felt that somehow we were going to muddle through, and that's always the expectation. We talked about Greece. That's the expectation, you know? Greece will somehow muddle through. The U.S. will somehow muddle through.

There's a book, if you want to read a history of the debt market, called *This Time Is Different*, and it basically describes that sooner or later these things come to a crescendo, and there's a day of reckoning and a reset. When that day will come I can't tell you. If I knew that, I could make you an enormous amount of money. Unfortunately, my degree of foresight is not that great. But at some point, I think, debt markets are going to run into trouble, and we are carefully watching that to make sure we get damaged as little as we can.

**Mr. Quest:** Thank you.

**The Chair:** Heather.

**Mrs. Forsyth:** Thanks, Madam Chair. I have a couple of questions, if I may. The first one. You talked about the – I have to flip back to my notes – real estate equities and how strong they are. I'm going to page 16, and you talk about a small portion in foreign real estate of about 7 per cent. Where would that be?

**Dr. de Bever:** Well, let me explain to you the challenge on real estate. Canadian pension plans are, from a structural point of view and how they operate, quite a bit ahead of the curve compared to some of their international counterparts. As a result of that, Canadian pension plans own most of the good real estate in Canada, and we've had to scramble. Remember last year? We still found a portfolio that somebody else had to sell in industrial real estate. But the pickings are getting slimmer, so we are starting to dip our toe into European and U.S. real estate, and in both cases we're looking at opportunities that came out of the misfortune of people who got damaged in 2008 and some of the new regulatory requirements that are causing real estate to be less of an attractive asset than it used to be.

But we're very, very cautious. We're making sure we're doing this with partners who know the local markets, but it's at this stage a fairly small part of what we do. We have some in Germany, some in the U.K., and we have some opportunities in the eastern United States.

**Mrs. Forsyth:** I'm writing. Sorry. Yeah. It's an interesting time when you look at some of the things that you've got invested. If you're looking at the retail market – Yorkdale shopping centre, Square One, and Scarborough – all three are in Ontario, and then you've made some notes under the Yorkdale shopping centre about it being one of the premier spaces. So those are three that you have in Canada that weren't part of the Canadian pension plan?

**Dr. de Bever:** Well, they're large, but for instance on Monday we opened up Eighth Avenue Place in Calgary, which was a project that a number of people said should never have been built, and it's turned out to be a really successful project because we built it during the darkest hour for Calgary as an option on the future, and it turns out it came on the market at exactly the right time. There's now some discussion of building the second tower on that project because the demand for office space is so strong in Calgary.

We don't discount the Canadian market, but it tends to be more in the nature of add-ons to stuff we already have of high quality, and our portfolio is probably one of the most high-quality portfolios that you can put together. The problem is that our clients have a big appetite for real estate, and we don't know where to find it. There's not as much around that is of the kind of quality we already have.

**Mrs. Forsyth:** Okay. Thanks.
May I go on, madam?

**The Chair:** Sure.

**Mrs. Forsyth:** Okay. Thanks.
I want to talk to you just briefly on your page 18, the top 10 global equity pool holdings. The fifth one down is Apple. I'm wondering, with all of the – I guess controversy would be one word – comments, what's happening with Research In Motion: have we got any money invested in that?

**Dr. de Bever:** Well, Research In Motion is a big part of the Canadian market, so we do. But you have to understand that just because it's in the newspaper and everybody talks about it, there are hundreds of things that we don't talk about that are equally risky that move the fund around. I just did a back-of-the envelope calculation. On the worst day in the week or the best day in the week the heritage fund either goes up or down in value by $200 million. That's not as a result of the things you read about in the newspaper; it's because we have so many holdings that all have their stories, both good and bad. RIM right now is the flavour of the day. It's an example of a company that became very prosperous with an idea and has trouble catching the next one.

Apple not too long ago was in the same vein. It made its name in the early age of the personal computer and just in the last few years has come up with a suite of products that has hit the spot. So that 1 and a half per cent: I would venture to guess that two or three years ago that was probably half a per cent. It's the value increase in Apple that has produced that.

Look at some of the others. Precision Drilling is probably the biggest story in AIMCo to date. We invested in that company at $3. It's now worth, I think, $17 the last time I looked.

There are some other ones on the list that are more problematic, and that's what we're in business for. If management were that easy and you could make money just by buying some stock, it would not be so hard. The stories of these companies – and there are probably half a dozen stories just on that list – are very complex, and it's very hard to predict how they play out. In some cases we can influence it, and in other cases we can't.

**Mrs. Forsyth:** When you comment about others on that list that are more problematic, would that be the ALL, América Latina, and JPMorgan?

**Dr. de Bever:** No. The biggest issue we have right now is around TNT. It's a Dutch company. Because of the slowdown in Europe its business has not grown as fast, and because of some weaknesses in management that we are working on, it has not done quite everything it could to move the company forward.

**Mrs. Forsyth:** Thank you.
Thanks, Madam Chair.

**The Chair:** Thanks.
Hugh.

**Mr. MacDonald:** Yes. Thank you. Certainly, it seems to be a sensitive matter with government members here whenever we look at the loss in value through inflation over the years of the heritage savings trust fund, but that's not my question at this point.

**Mr. Elniski:** We had to get it in anyway.

**Mr. MacDonald:** You bet. Yeah. Other people did. This is a democracy.

In 2005 the United Nations secretary-general invited a group of the world's largest institutional investors to join a process in developing the principles for responsible investment. As of April of this year over 850 investment institutions have signed on to this agreement, with assets under management of close to $25 trillion U.S., and last year the Alberta Investment Management Corporation signed on to this deal.

Now, I've had an opportunity to look, and in schedule D of the detailed list of investments we see that – I hope I'm pronouncing it correctly – Hanwha Chemical corporation, which is a producer of cluster munitions, has a fair value investment of over $900,000. We own 74,000-plus shares of that company. In the same schedule, schedule D, there is another outfit, EADS N.V., description as an industrial. We have a fair value holding in that of $1.1 million, or 55,000 shares. We have also, I believe in the same schedule, BAE Systems and BAE Systems PLC. We have close to $5 million of value in these two companies. They produce nuclear arms as well.

Then we have the British American Tobacco company with $844,000, or 24,000 shares. Then we have, also in schedule D, Imperial Tobacco, with 5 and a half million dollars worth of value, or 153,000-plus shares.

These are outfits that have been for ethical reasons rejected by Norway. It's a small amount here. We've signed on to this deal. Why are we holding these shares at this time?

***9:50***

**Dr. de Bever:** I would venture to guess that all of them are index holdings. One of them is Airbus. I mean, come on. You know, people would think that Airbus is a reasonably responsible company. But the other ones: I would agree with you. If any of them are active, I would be very surprised. They're probably part of an index somewhere. We've had an agreement with the province in the case, for instance, of tobacco. It's very expensive to exclude tobacco from an index holding, but we will not hold any active positions, in other words deliberate positions, other than getting cheap exposure to a market. I will verify that that is indeed the case, but I am 99 per cent sure that that is the case.

**Mr. MacDonald:** Thank you.

**The Chair:** Heather, did you have any more questions?

**Mrs. Forsyth:** No. Thanks, Madam Chair.

**The Chair:** Okay. Anyone else?
Hugh, anything else?

**Mr. MacDonald:** Not at this time, no.

**The Chair:** Thank you very much.
I wonder if someone could move that

> the Standing Committee on the Alberta Heritage Savings Trust Fund approve the 2010-11 annual report as circulated.

George. All those in favour? Any objections? That's noted. The motion is carried.

Okay. We just want to spend a few minutes talking about our public meeting coming up this fall. Just so you know, the deputy chair and I did meet with Corinne to talk about some options in the fall. We have heard that venue availability is actually quite challenging, so we narrowed it down as far as looking at the week of October 17, between Monday and Thursday of that week.

Maybe at this time, Tracey, if you could just give us an update on where you're at with looking at different options and what your proposal is.

**Ms Sales:** Thank you, Madam Chair. As far as the venue options, we have a few that we're looking further into, and as soon as we do have a venue that is going to satisfy all of our needs, including the broadcast needs, we will definitely let the committee know.

Right now, though, I'm going to walk you through the communications plan for the public meeting. We're recommending that we promote the public meeting locally. We're going to do this through, one, advertising through the local newspapers. In order to maximize frequency, I'm recommending that we run multiply in the *Edmonton Journal*, *Sun*, and *Examiner*. Two, I'm talking about promoting the meeting through the meeting site itself, if applicable, as well as the local constituency offices. We did try this last year in Lethbridge. We provided the constituency offices in Lethbridge with promotional materials to have in the constituency offices prior to the meeting. I think that this could be very effective in Edmonton considering the number of constituency offices that we have at our disposal.

We're also talking about updating the statistics card. We've been doing this for a few years now. It's a low-cost promotional item that just gives general information on the fund as well as inviting people to the meeting.

We're also talking about extending the reach province-wide. The number one recommendation is to again broadcast through Shaw on TV. Last year in Calgary alone we reached around 6,000 viewers, so it was a very successful broadcast. We're recommending that again this year.

We're also talking about trying to encourage public involvement with the meeting through an online chat option. Last year we broadcast the meeting live on our website through a live webcast. This year we're talking about coupling that with a chat option so that the public can actually submit questions that the committee can deal with during the public meeting.

We're also talking about advertising province-wide. We're going to try and cast a very wide net here, maximize reach, so we're looking at television advertising. The television advertising is actually coupled with the broadcasts, so Shaw will promote the meeting on TV for no additional cost. We're talking about online advertising, and we're talking about province-wide newspaper advertising as well to supplement the TV and the online advertising. We're also looking at distributing news releases as necessary and, of course, posting the information to the applicable websites.

Following the meeting we will measure the results and report back to the committee on the successful strategies, what we can do better next time, that sort of thing. We're looking at $43,600 for this plan as recommended, which is well within the budget of $65,000.

**The Chair:** Any questions for Tracey?

**Mrs. Forsyth:** I do, madam.

**The Chair:** Go ahead, Heather.

**Mrs. Forsyth:** Thanks, Tracey. I appreciate the work that you've done. I'm one of those frustrated people that continually are disappointed with the low turnout that we get at these meetings. I know all the hard work that you put into making sure that Albertans are well aware of this meeting. Have you considered looking at doing like a live town hall concept, which seems to be becoming quite successful?

**Ms Sales:** This would be very similar, of course, because it will be broadcast live, and it will also be webcast live.

**Mrs. Forsyth:** So does that mean that someone that is watching can call in with a question?

**Ms Sales:** We actually decided to go with the online chat option instead of the phone-in option. Some factors we considered were cost as well as when we were looking at a TV broadcast, including the audio element, we were worried about degradation of sound and that sort of thing coming across in the TV broadcast. It's a little more difficult to moderate the phone while we're doing a live TV broadcast, so we actually decided on the online option because it will be easier to manage.

**Mrs. Forsyth:** When you talk about managing, maybe you can explain what you mean. Are you concerned that someone will call in and happen to just come out with some – I don't know how to say this.

**Ms Sales:** No. That's okay. When I'm talking about managing, I'm talking about: with the online option we can have a laptop set up; we can have a moderator who reads the questions into a microphone. The question would then be read in for *Hansard*, to facilitate their purposes, and then the committee could answer the question. If we have people calling in, we could have multiple callers asking the exact same question, which, when you think about it, when you're watching the broadcast from home would get very tedious to viewers. Do you know what I'm saying?

**Mrs. Forsyth:** Yes.

**Ms Sales:** So it's not so much controlling as far as we're worried about what people are going to ask; it's more to do with ensuring that we have a good TV broadcast because we have to think about how all the pieces work together.

**Mrs. Forsyth:** Okay. Thanks.

**The Chair:** Corinne wants to add to that.

**Mrs. Dacyshyn:** The other issue that was considered regarding the phone-in was that we would have had to advertise ahead of time and get people to register their phone numbers. We felt that that would be costly as well as maybe not as effective as the committee would have liked if that's the right way to say that.

**The Chair:** Any other questions, Heather?

**Mrs. Forsyth:** No. Thanks, Janis.

**The Chair:** Other committee members? No.

Do we need a motion to approve the communication plan as presented? Then, obviously, we'll get back when we've narrowed down some date options. Okay. Dave will make that motion. All those in favour? Any opposed? That motion is carried.

Thank you, Tracey.

Okay. You all have a copy of the memo from Alberta Finance and Enterprise regarding the number of website hits. Does anybody have any questions about that?

Seeing none, we also have with our packages today the two follow-up items, that actually Hugh had referred to, from the Department of Finance and Enterprise arising from the March meeting. So I guess I would just ask if there are any questions about those.

Any other business that someone would like to raise? Okay.

We will hold the next meeting probably – well, it will be at the call of the chair but likely around mid-September to review the first quarterly report and then make the final arrangements for the public meeting.

Could someone move that we adjourn? George?

**Mr. Groeneveld:** I can do that.

**The Chair:** All those in favour? That motion is carried. Thank you very much.

[The committee adjourned at 10 a.m.]

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