



Legislative Assembly of Alberta

The 28th Legislature
Second Session

Standing Committee
on the
Alberta Heritage Savings Trust Fund

Thursday, June 19, 2014
1:02 p.m.

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**Legislative Assembly of Alberta
The 28th Legislature
Second Session**

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

Casey, Ron, Banff-Cochrane (PC), Chair
Jablonski, Mary Anne, Red Deer-North (PC), Deputy Chair

Amery, Moe, Calgary-East (PC)
Barnes, Drew, Cypress-Medicine Hat (W)
Dorward, David C., Edmonton-Gold Bar (PC)
Eggen, David, Edmonton-Calder (ND)
Khan, Stephen, St. Albert (PC)
Kubinec, Maureen, Barrhead-Morinville-Westlock (PC)*
Olesen, Cathy, Sherwood Park (PC)**
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* substitution for Stephen Khan
** substitution for David Dorward

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

Participants

Ministry of Treasury Board and Finance

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Aaron Brown, Director, Portfolio Management, Capital Markets

Rod Matheson, Assistant Deputy Minister, Treasury and Risk Management

Darcy Scott, Public Affairs Officer

Alberta Investment Management Corporation

Darren Baccus, Chief Client Relations and Legal Officer

Dale MacMaster, Executive Vice-president, Public Market Investments

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Thursday, June 19, 2014

[Mrs. Jablonski in the chair]

The Deputy Chair: Good afternoon, everyone. We're going to call the meeting to order. My name is Mary Anne Jablonski. I'm the MLA for Red Deer-North, and I'm going to be chairing this meeting this afternoon because our brave and courageous chairman couldn't be here today. But he is on the phone, so that's wonderful to hear.

I'm calling the meeting to order and asking the committee members in the room and on the phone and all other attendees around the table to introduce themselves for the record.

Mr. Amery: Thank you. Moe Amery, MLA for Calgary-East and member of this committee.

Mr. Eggen: Good afternoon. My name is David Eggen. I'm the MLA for Edmonton-Calder.

Mr. Scott: Hello. Darcy Scott, Treasury Board and Finance, communications branch.

Mr. Baccus: Darren Baccus, AIMCo.

Mr. MacMaster: Dale MacMaster, AIMCo.

Mr. Matheson: Good afternoon. Rod Matheson with Treasury Board and Finance.

Mr. Brown: Aaron Brown, Treasury Board and Finance.

Mr. Babineau: Rod Babineau, Treasury Board and Finance.

Mr. Sittler: Jeff Sittler with the Auditor General's office.

Mr. Saher: Merwan Saher, Auditor General.

Ms Sales: Tracey Sales, LAO communications.

Ms Dotimas: Jeanette Dotimas, LAO communications.

Mrs. Dacyshyn: Corinne Dacyshyn, committee clerk.

The Deputy Chair: And on the phone, please.

Ms Kubinec: Maureen Kubinec, standing in for MLA Stephen Khan.

Mr. Barnes: Drew Barnes, MLA, Cypress-Medicine Hat.

Mr. Casey: Ron Casey, Banff-Cochrane.

The Deputy Chair: It's good to hear from all of you. I'm glad that you're able to be here through technology.

The meeting materials were posted to the internal committee website last week.

A few housekeeping items to address before we turn to the business at hand. The first thing is that the microphone consoles are operated by the *Hansard* staff, so you don't have to press the buttons, I guess. Please keep cellphones, iPhones, and BlackBerrys off the table as these may interfere with the audiofeed. The audio of committee proceedings is streamed live on the Internet and recorded by *Hansard*. Audio access and meeting transcripts are obtained via the Legislative Assembly website.

The first item on the agenda is to approve the agenda. Do I have anyone to move that? Moved by Moe Amery that the agenda for the June 19, 2014, meeting of the Standing Committee on the

Alberta Heritage Savings Trust Fund be adopted as circulated. All in favour? On the phone? Okay. It sounds like that was unanimous. The motion is carried.

We're going to be looking at the Alberta heritage savings trust fund annual report 2013-2014. It's a draft. The draft of the 2013-2014 annual report was posted on the internal website last week, and a revision to the minister's transmittal letter was posted on Tuesday. Members are reminded that this draft report is confidential and that once approved by this committee, final copies will be printed by Alberta Treasury Board and Finance, and copies will be distributed to all members by the chair, thereby making the report public.

Could I ask Mr. Matheson, assistant deputy minister, to give us a review of the report, please?

Mr. Matheson: Certainly. Thank you, Madam Chair. Good afternoon to members of the committee. I am here today on behalf of Minister Horner, who sends his regrets. Before you is the 2013-14 annual report of the Alberta heritage savings trust fund. As the chair mentioned, pending the committee's approval, this report will be released to the public next week, after the report is released to your colleagues in the Legislature.

I'd like to just spend a minute and highlight a few areas of the report. As you can see from page 1, the heritage fund's value continued to climb in 2013-14. I would also note that last year the fund recorded the highest-ever investment income.

As required by legislation, \$193 million was retained in the fund for inflation-proofing, and the remaining balance of the income was transferred to the general revenue fund.

For the year the heritage fund finished flat against its policy benchmark from a performance point of view. However, it far surpassed the long-term target that the government has established for the heritage fund, which is inflation plus 4 and a half per cent. Looking out over a longer term horizon, the fund posted five- and 10-year returns of 12.7 per cent and 7.5 per cent annualized respectively. Over that same 10-year period Canadian inflation was 1.8 per cent, which makes the all-in target for the heritage fund for that 10-year period 6.3 per cent. As you can see, the fund has comfortably outpaced that measure. AIMCo delivered an average 1.2 per cent in added value over the past five years, which is also ahead of the target that they've established.

Referring to the charts on page 13, you can see how each investment class fared in the fiscal year as well as the fund's overall performance. Fixed income had a strong final quarter, which brought its total year return to 3.2 per cent, well ahead of the .8 per cent benchmark. The inflation-sensitive and alternative class had a double-digit performance as well. We've noted before, though, that there's measurement mismatch between assets that are valued over a long cycle and benchmarks that are marked to market daily.

The largest holdings in the portfolio are equities, and they returned 24.3 per cent for the year. The primary driver of the fund's investment return was the global equity portfolio, which earned 28.3 per cent and comprised a little over a third of the fund at year-end.

I just want to make an observation. At the last meeting of the committee committee member Eggen requested information on the value of the investments that were made in Alberta, and the Department of Treasury Board and Finance has provided that information to the committee separately. I just want to note that AIMCo has a mandate to seek the best returns regardless of geography. The majority of the world's investment opportunities reside outside of Alberta or even Canada, and it is important to

strike a balance to make sure that the fund is properly diversified and prudently invested for all Albertans.

I would also like to note the graph on the top of page 11 for committee members. At the May 2014 committee meeting committee member Dr. Sherman asked about the inflation-adjusted value of the fund. The graph that is on page 11 was introduced in the report three years ago at the request of a prior committee member. We update this information annually as changes quarterly would be insignificant.

1:10

It is clear that the per capita value of the fund has declined since its peak in 1987. Since the inception of the fund the population of Alberta has more than doubled. That combined with the period between 1987 and 2005, when the fund was not inflation-proofed, has caused the per capita value to decline. However, given the recent legislative changes which will see the heritage fund retain its income as well as receive potential further deposits from nonrenewable resource revenue, we expect the per capita value and the total value of the fund to rise in the future.

One last point. Looking forward, the department will again be reviewing the asset mix for the heritage fund in this coming year. This is something that should be done every five years or thereabouts. We look at long-term expected returns and balance that against the expected risks and how the markets interact.

Those are my opening comments. I'll invite Dale MacMaster to see if there is anything he'd like to supplement or add to my comments.

Mr. MacMaster: I'm here, by the way, on behalf of Leo de Bever, who sends his regrets.

I would just say that overall we are pleased with the results of the fund. Of course, that's no indication of future returns.

I would take any questions you might have.

The Deputy Chair: Thank you, Mr. MacMaster.

Are there any questions from the panel, from the members here?

Mr. Barnes: Excuse me, Madam Chair. I have a question, please.

The Deputy Chair: Sure. Go ahead, Drew.

Mr. Barnes: Okay. Thank you. Just on private equity the one-year return is quite a bit off the one-year benchmark, so I'd like to hear from some of the people involved as to why they think this is, exactly how the benchmark is set, and if it's a short-term thing where it would temporarily just be a valuation or if there are some uncertainties on our returns there, please. If somebody could talk about private equity, I would appreciate it.

The Deputy Chair: Drew, are you referring to a page number in the report as well?

Mr. Barnes: Yeah. I am, Madam Chair. It's page 13, asset class return versus benchmark. Right at the very, very bottom under equities are Canadian, global, and private. We have a one-year return of 9.6 per cent versus the benchmark of 26.7 per cent.

The Deputy Chair: Thanks very much, Drew.

Mr. MacMaster, did you want to take that question?

Mr. MacMaster: Sure. I can comment. When it comes to private equity, AIMCo really takes a long-term view of our investments there. For us that type of horizon is 10 years, perhaps 15 years. I would say that if you look at the five-year returns, it's not as

dramatic, and I think if you were to look at returns over a 10- or 15-year period, we would hope to have that a lot closer to the benchmark. The returns in the public equity market, as you probably well know, were very high, unusually high. Global equity market returns were 25 per cent plus. It makes it very difficult for assets that aren't marked on a regular basis, that are long-term in nature, to keep up. Our view, as I said, is long term. The investments we make today we expect to be benchmarks over the very long run.

The Deputy Chair: Drew, do you have any other questions?

Mr. Barnes: Yeah. Just as a follow-up, at \$1.3 billion we're some side of 7 or 8 per cent of our total Alberta fund here. The list of the top 10 holdings on page 15 looks like it's fairly well diversified, which is good to see, but I wonder about the process of investment. Who analyzes it? Who values it? You know, how do different firms have the option of getting in there? Could somebody please talk about the overall process of picking a private equity?

Then, actually, in regard to one of the earlier questions: how many of these would be Alberta based? Is that a requirement at all?

The Deputy Chair: Mr. MacMaster.

Mr. MacMaster: Sure. Being Alberta based is not a requirement. We are not geographic oriented. We're totally return oriented. Obviously, at times there are investments in our own backyard that we can analyze, that meet the criteria, but it's always based on a return criteria.

Our investment team is staffed with highly qualified professionals with years and years of investment experience, who have over the years tapped into a network of partners who direct them to deals for AIMCo to look at, evaluate, and potentially invest in. And there are numerous, numerous deals. Perhaps, you know, 80 to 90 per cent of those deals that we see are rejected before something actually meets all the criteria to make it into the portfolio. Yes, we do aim to have a diversified portfolio of positions in terms of the industry, the sector we're in, in addition to having a diversified set of strategies across the world in terms of both our public and private equities.

The Deputy Chair: Thank you.

Mr. Barnes: Just as a follow-up, is there an element of sort of angel investing, or do you look for more established opportunities, or is that part of the diversification, where you look down the gamut?

Mr. MacMaster: I would say that we invest based on receiving the highest risk-adjusted return that we can, and I would also say that the investments tend to be later stage than what someone might call angel investing. I would consider that term, at least, very early stage.

Mr. Barnes: Okay. Thank you.

The Deputy Chair: Thanks, Drew.

I want to welcome Dr. Raj Sherman, Edmonton-Meadowlark. Raj, you have a question?

Dr. Sherman: Thank you. Mr. MacMaster and the rest of the team, I want to thank you for doing the work you do. Jeez, I wish I was getting these rates of return. Equity markets have done well.

You've done a very good job of managing the fund, so I want to thank you on behalf of the Alberta Liberals.

One question I have: since the inception of the trust fund in 1976, using the historical data rates of return and compound interest, what would be the fair value of the fund today if no money was transferred out of the fund into general revenues?

Mr. Matheson: That would be a very challenging number to come up with. There would be a wide variety of assumptions one would have to make, so I certainly wouldn't want to hazard even a guess just off the top of my head. If we went back to 1976 and tried to look at returns and values since then, as I say, it would require a lot of assumptions. I wouldn't even know. I wouldn't want to hazard a guess.

Dr. Sherman: The main reason why I ask you this question is that if we actually didn't use the interest for general revenues, the government would have to be more fiscally prudent with the money that we do spend and look for other sources of revenue, perhaps progressive income tax, to pay the daily bills. It would be nice to see how much money we would actually have in the bank, and with the returns you're getting us, I'd love to know how much interest we're getting as well on top of what the value of the fund would be, because you generated pretty good returns for us. So if you can get back to us, I'd appreciate it.

Thank you.

Mr. Matheson: Just for clarity, what would you like us to try to provide?

Dr. Sherman: Assuming all the growth of the fund, the returns that you've had using compound rates of interest at the time, what would the total fund be worth today had we actually not spent any of the interest?

Mr. Matheson: I see. Okay.

Dr. Sherman: That would give us, you know, that it might be \$50 billion, it might be \$60 billion, or it might be \$40 billion. Well, we know it's going to be more than \$40 billion because you've taken \$36 billion out plus \$17 billion. It would be nice to know what that number would be.

If you can also project, you know, what our rate of return would be based on what your performance has been recently and how much interest we'd get off that as well.

Mr. Matheson: If I could just add that if we go back to the inception of the fund, when the heritage fund was created in 1976, it did not have a single mandate of maximizing investment returns. It was invested in a variety of divisions, some of which were designed to support the Alberta economy. I guess I'm just cautioning that if we go back historically, there might not even be a rate of return on the heritage fund back in its early days because it was not designed to earn a commercial or a financial rate of return. We will certainly try to come up with a number.

Dr. Sherman: We know that we've taken certain money out that we've put into general revenues, so put that back into the gross number for a ballpark figure of general rates of return at that time, plus or minus, you know, a percentage point here and there. I understand it can be difficult getting an exact figure, but if you can give us a ballpark range of what the value of the fund would be had we not spent any interest money and just had it compound. What would the performance that you have had over the last number of years be?

1:20

The Deputy Chair: It sounds like you're going to have to make a really good educated guess, Mr. Matheson.

Mr. Matheson: We will do our best.

The Deputy Chair: We also have questions from David Eggen. If you'd like, go ahead.

Mr. Eggen: Thank you, Chair. Thank you so much for your presentation and the annual report. It's comprehensive, and I think it reflects the success of the investments from last year and this year. It's quite good news.

I'm curious, though, about what I had asked last time in regard to the percentage of investment that the heritage trust fund has in Alberta investments. Thanks for the information, but I was quite surprised to see that only 9.4 per cent of the fund is invested in Alberta. I think a lot of Albertans would be surprised to see that, too. Most of that, really, is in real estate investments. I mean, we have to remind ourselves that this is not just a regular equity fund, but it's an extension of an investment in the province's future.

My first question is: has there ever been a mandated percentage of this fund that was meant to be invested in the province of Alberta? I know that we don't have that now, but were we ever under that sort of a rule in the past with the fund?

Mr. Matheson: I'll answer that. As I said earlier, if you go back to the original creation of the heritage fund and its original legislation, in fact by legislation in the heritage fund act there were a number of divisions of the heritage fund, one of which, in fact, was called the Alberta investment division, whose legislated mandate was to invest in Alberta and, largely, to support Alberta provincial corporations and organizations in the province. But all of that was changed in I believe it was 1993, when the heritage fund act was completely rewritten and the mandate for the fund was totally changed. It was turned into an endowment, with a pure mandate to seek long-term, maximum returns within acceptable risks, which is how it's operated today.

Mr. Eggen: Right. Okay. So from '93 there was no fixed number to invest in the province of Alberta. I mean, it's interesting that the change in mandate sort of coincides with the change in the growth of the fund, too, both per capita and in actual dollars and adjusted dollars. I'm just, you know, wondering if AIMCo is able to work with a mandate that requires a percentage of the heritage trust fund to be invested in Alberta equities. You could work with that contingency?

The Deputy Chair: Mr. MacMaster.

Mr. MacMaster: Certainly. We're an organization that is client-centric, so we take whatever guidance our clients give us in terms of the mandate, in terms of the broad asset mix and the risk that they'd like to take. Certainly, with our largest client, which is the heritage fund, if the decision was made to go down a path of investing equities or some other assets in Alberta, AIMCo would do its best to fulfill its mandate and provide that as a service to its client.

Mr. Eggen: Thanks. Certainly, you have to diversify. It's important to have a balance in the mix, both inside this economy and outside, both in Canada and even around the world, but like I said, I was just a bit surprised to see that we only have a 9.4 per cent investment in the province of Alberta directly through the heritage trust fund.

Thank you very much.

The Deputy Chair: Thank you, David.

I would like to welcome Cathy Olesen. Cathy is the MLA for Sherwood Park, and she's substituting for Mr. Dorward. Welcome.

Ms Olesen: Thank you, Madam Chair. My apologies for being late, but I was at a meeting that I couldn't leave.

The Deputy Chair: Understood.

Moe Amery, you have the next question.

Mr. Amery: Well, thank you, and thank you very much for being here. Help me understand this. Again on page 13, under the asset class return versus benchmark, when I look at the global, the one-year return is 28.3 per cent. Is that the return on the portion of the fund that's invested globally?

Mr. MacMaster: Invested in global equities. If you refer to the chart on page 13, there's an equity section which contains Canadian equities, global equities, and private equities. The 28.3 per cent, which is the one-year return, represents the return for global equities.

Mr. Amery: What portion of the fund is invested in global equities?

Mr. MacMaster: That, I believe, is in another table, on page 12. If you refer to the bottom part of that table, under equities, global developed equities are 34.4 per cent as of March 2014.

Mr. Amery: So we have a lot more of the fund invested globally than in the province, as Mr. Eggen was just saying. There's 9.4 per cent invested in the province?

Mr. MacMaster: Yes.

Mr. Amery: Now, with the turmoil that we're seeing around the world, mainly in Russia, Ukraine, and the Middle East, would that be a risky investment?

Mr. MacMaster: Well, let me say first of all that when it comes to the world of investing, there are always places in the world that are dangerous places. Certainly, you know, the Middle East is an active area right now. There's certainly considerable risk there. You referred to, I believe, Russia and Ukraine. That's heated up. There are some exposures to that part of the world through our emerging markets portfolio. It's relatively small. We use internal managers and external managers, that we hire for certain mandates, around the world. The emerging markets, in part, are managed externally by managers we know and trust.

Markets reacted to the news around Ukraine, with Russian stocks down 30 to 50 per cent, which actually presented a buying opportunity. Sometimes where there's risk and turmoil, it presents an opportunity, and that's the way we view the world. But it's important to understand that our portfolios are widely diversified, not only across the asset mix. What you see here is in part developed by our colleagues in Finance with a policy that makes sense for Albertans, then invested by AIMCo, and broadly diversified across asset mix and security type.

Mr. Amery: Thank you.

The Deputy Chair: Thank you, Moe.

Are there any more questions from the committee members? Any questions from those who are here via the telephone?

Seeing no more questions, the next thing that we would have to do is to approve the report. I'm asking if there's someone who would like to make the motion that

the Standing Committee on the Alberta Heritage Savings Trust Fund approve the 2013-2014 Alberta heritage savings trust fund annual report as circulated.

Mr. Eggen has made that motion. All in favour? On the phone? That was three ayes from the phones, so it looks like this is unanimously approved. It's carried.

1:30

The next item on the agenda has to do with the public meeting communications plan update. At the last heritage committee meeting I asked communications to look into how Albertans could submit questions to the committee via telephone during the public meeting. As you know, we can take questions from Twitter, and we can take questions from e-mail, but there are some people like me that are pretty old-fashioned and using the telephone would have been really handy. To this end, communications is recommending the installation of a temporary LAO phone line for accepting questions during the public meeting. These questions would be sent to the chair and the deputy chair in the same way that Twitter questions are sent. The cost is negligible and could be absorbed in the existing budget.

Now, if there are any questions, Jeanette can respond to those questions. Is anybody concerned about that? And we're okay on the phones, too, right? Okay. It sounds like it.

Seeing no one with any questions, we need a motion that the Standing Committee on the Alberta Heritage Savings Trust Fund approve the addition to the 2014 public meeting communications plan of a temporary telephone line for accepting questions during the public meeting, with the cost being absorbed by the existing communications budget.

Would anyone like to make that motion? MLA Cathy Olesen. Thank you. All in favour? Opposed? That's carried.

Moving to other business on the agenda, a follow-up item was provided by Treasury Board and Finance in response to Mr. Eggen's question at the last meeting. It has been mentioned, but, Mr. Eggen, I'm sure that you as well as other committee members received this item. Are there any questions on this memorandum that answers your question, Mr. Eggen?

Mr. Eggen: No. Once again, I thank the team that put this together. It's very interesting, I think. Perhaps we have to ask ourselves whether we should think about, you know, increasing the percentage of the heritage trust fund that's invested in Alberta.

The Deputy Chair: Okay. Thank you very much.

If there are no other items of business, we'll move to the date of the next meeting. The next meeting will be scheduled in September to review and receive the first-quarter report for 2014-2015 and to review the action plan for the public meeting.

Can I have a motion to adjourn the meeting? Moe Amery moved that the meeting be adjourned. All in favour? Thank you very much, everyone, for attending.

[The committee adjourned at 1:33 p.m.]

