Legislative Assembly of Alberta

The 29th Legislature
Third Session

Standing Committee
on the
Alberta Heritage Savings Trust Fund

Tuesday, January 16, 2018
1:29 p.m.

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Alberta Heritage Savings Trust Fund

Coolahan, Craig, Calgary-Klein (NDP), Chair
Schreiner, Kim, Red Deer-North (NDP), Deputy Chair

Clark, Greg, Calgary-Elbow (AP)
Cyr, Scott J., Bonnyville-Cold Lake (UCP)
Dang, Thomas, Edmonton-South West (NDP)
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Standing Committee on the Alberta Heritage Savings Trust Fund

Participants

Ministry of Treasury Board and Finance
- Rod Babineau, Manager, Portfolio Analysis, Capital Markets
- Lowell Epp, Assistant Deputy Minister, Treasury and Risk Management
- Stephen J. Thompson, Executive Director, Capital Markets

Alberta Investment Management Corporation
- Dale MacMaster, Chief Investment Officer
- Mark Prefontaine, Senior Vice-president, Client Relations
- Kevin Uebelein, Chief Executive Officer

1:29 p.m. Tuesday, January 16, 2018

[Mr. Coolahan in the chair]

The Chair: Good afternoon, everyone. I'd like to call the meeting of the Alberta Heritage Savings Trust Fund to order.

My name is Craig Coolahan, and I'm the MLA for Calgary-Klein and the chair of this committee. I'd like to now ask everyone at the table to introduce themselves, starting on my right.

Mrs. Schreiner: Good afternoon, everyone. Kim Schreiner, MLA for Red Deer-North and vice-chair of the committee.

Mr. Hanson: Good afternoon. Dave Hanson, MLA, Lac La Biche-St. Paul-Two Hills, standing in for Scott Cyr.

Mr. Prefontaine: Good afternoon. Mark Prefontaine with AIMCo.

Mr. MacMaster: Dale MacMaster, AIMCo.

Mr. Uebelein: Kevin Uebelein, AIMCo.

Mr. Epp: Lowell Epp, Treasury Board and Finance.

Mr. Thompson: Stephen Thompson, Treasury Board and Finance.

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

Mr. Robe-From: Nelson Robe-From, Auditor General's office.

Mr. Dang: Thomas Dang, MLA for Edmonton-South West.

Mr. Horne: Trevor Horne, MLA for Spruce Grove-St. Albert.

Dr. Turner: Bob Turner, MLA, Edmonton-Whitemud.

Ms McKitrick: Bon après-midi. Annie McKitrick, MLA, Sherwood Park.

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

Ms Sorensen: Happy New Year. Rhonda Sorensen, manager of corporate communications with the Legislative Assembly Office.

Mr. Koenig: Good afternoon. I'm Trafton Koenig with the Parliamentary Counsel office.

Dr. Massolin: Good afternoon. Philip Massolin, manager of research and committee services.

Mr. Roth: Good afternoon. Aaron Roth, committee clerk.

The Chair: Thank you.

Can I get those on the phone to introduce themselves, please?

Mr. Clark: Good afternoon. Greg Clark, MLA, Calgary-Elbow.

The Chair: That's all we have on the phone.

For the record I'd like to note that under Standing Order 56(2.1) to (2.4) Mr. Hanson is the official substitute for Mr. Cyr.

Before we turn to the business at hand, a few operational items. The microphone consoles are operated by *Hansard*, so there's no need for the members to touch them. Please keep all cellphones on mute. Audio and video of the committee proceedings are streamed live on the Internet and recorded by *Hansard*, and audio and video access and meeting transcripts can be obtained via the Legislative Assembly website.

The first item on the agenda today is to approve the agenda. Would somebody like to approve the agenda? Mr. Dang. Mr. Dang moves that the agenda for the January 16, 2018, meeting of the Standing Committee on the Alberta Heritage Savings Trust Fund be adopted as circulated. All in favour? On the phone? I think Mr. Clark said aye, yes. Any opposed? That motion is carried.

The next item is the approval of the minutes from the September 20, 2017, meeting. Are there any errors or omissions to note? If not, would a member like to move that they be adopted as circulated? Ms McKitrick moves that the minutes for the September 20, 2017, meeting of the Standing Committee on the Alberta Heritage Savings Trust Fund be adopted as circulated. All in favour? On the phone?

Mr. Clark: I'll abstain. I wasn't on the committee at that time.

The Chair: You can't abstain, Mr. Clark.

Mr. Clark: Can I vote on minutes for a meeting I wasn't at?

The Chair: Yes, because now you are able to read the transcripts.

Mr. Clark: Fabulous. Then I will vote in favour.

The Chair: Thank you.

Any opposed? Seeing none, that motion is carried. Thank you.

Okay. The next item on the agenda is the second-quarter report. The Alberta heritage savings trust fund second-quarter report for 2017-2018 was released on November 28, 2017. Committee members were sent notification of its release, and the report was posted to the committee's internal website. The Alberta Heritage Savings Trust Fund Act mandates that one of the functions of the committee is to receive and review quarterly reports on the operation and results of the heritage fund. We are pleased to have Mr. Kevin Uebelein, Mr. Dale MacMaster, and Mr. Mark Prefontaine from AIMCo and Mr. Lowell Epp, Mr. Stephen Thompson, and Mr. Rod Babineau from Treasury Board and Finance to assist us with our review.

We'll turn the table over to AIMCo, and then we'll take questions from the committee after that. Gentlemen.

Mr. Epp: I think I will start.

The Chair: You'll start? That's fine. Thank you.

1:35

Mr. Epp: Thank you, Mr. Chair and members of the committee. Minister Ceci is unable to attend today and sends his regrets. I am pleased to speak on his behalf and on behalf of the department to discuss the heritage fund's second-quarter update. I'm not going to spend a lot of time on the report. You all have the report in front of you. I will spend a few minutes going through some highlights, and then my colleagues from AIMCo will speak to the fund's results and provide some of their perspective.

Of course, the legislated objective of the heritage fund is to maximize long-term investment returns for the fund within a prudent level of risk, and this is set out in the Alberta Heritage Savings Trust Fund Act. The fund continues to exceed long-term policy objectives with a five-year annualized rate of return of 10.9 per cent and a 10-year rate of return of 6.9 per cent as of the end of the most recent quarter. During the second quarter the heritage fund provided a return of 2.4 per cent over the first six months of the current fiscal year. Results so far this year have been driven primarily by the fund's equity investments, which have returned 3.2 per cent. Inflation-sensitive assets have returned 2.6 per cent for the first six months of the year, and fixed-income investments have actually had a negative return of .3 per cent for the first half of the fiscal year.

At the end of the second quarter the heritage fund had a fair value of $17.1 billion, which is net of $803 million of income payable to the general revenue fund. The heritage fund's portfolio was allocated in the following asset classes: 45.5 per cent in equities, 34.8 per cent in inflation-sensitive and alternative investments, and 18.6 per cent in fixed income, with 1.1 per cent in various overlays.

The heritage fund through the first six months has earned $926 million net of expenses of $66 million. You will note that an investment return of 2.4 per cent over the first six months does not equate to $926 million. Investment income is greater than investment return because gains from previous periods have been realized during the quarter.

Finally, I will provide a brief update on the Alberta growth mandate. In Budget 2015, as you know, the government announced that 3 per cent of the heritage fund would be allocated to directly invest in Alberta growth. Since the announcement in October 2015, 25 separate investments in 18 companies, for a total of $345 million, have been made. Two of these investments were divested since that time, and if you want more details, AIMCo can speak to those divestments. Of course, AIMCo manages the day-to-day investment decisions of the heritage fund independent from the government, and decisions about investments are made within that scope. Investments that fit into the Alberta growth mandate must also meet the heritage fund's legislated requirement to maximize long-term investment returns.

That concludes my remarks, Mr. Chair, and I would pass it back to you.

The Chair: Thank you, Mr. Epp.
We'll turn it over to AIMCo now.

Mr. MacMaster: Right. Thank you.

The Chair: Pardon me. Just one moment.
I'll ask Mr. Ellis: can you just introduce yourself for the record, please?

Mr. Ellis: Mike Ellis, MLA, Calgary-West. Thank you.

The Chair: Thank you.
Mr. Uebelein.

Mr. Uebelein: Yes. First, I want to thank Mr. Epp for batting leadoff for me. Chairman Coolahan, thank you for having us here. As you know, because the heritage fund has a March 31 fiscal year-end, the performance data that you have presented in front of you is for a six-month period ending September 30, 2017. As it happens, though, AIMCo and many of our clients operate on a calendar year-end. This being January – Happy New Year, by the way – we are just finishing up a review of our full calendar year 12-month results. I thought that a very few comments on my part on the overall performance of AIMCo might be of benefit and interest to this committee.

The total asset pool that AIMCo manages for Alberta continued to grow during 2017. In fact, we crossed a bit of a milestone during the year when our total assets under management went above $100 billion. At December 31 our total assets under management stood at just about $104 billion. This strong asset growth is a function of very good overall investment returns for the year. Those returns are a reflection of overall strong markets, to be sure, but it also reflects a very strong value-added performance by AIMCo, well above the aggregate benchmark. I want to remind you that our value-added methodology is always net of all of our costs, whether those are internal or external costs. In other words, we never claim to have beaten our benchmark until every dollar of our costs has first been accounted for.

Also, by focusing on our net investment returns after costs and not simply on minimizing costs, we're able to make some well-judged and needed investments in improving our capabilities. This includes adding to the breadth and depth of our investment capabilities and in bolstering our needed support functions, all of these in line with our clients' demands and needs. Without these judicious cost spends, our ability to sustain long-term performance, I believe, would be put at risk.

At this point I'd like to pass it over to Dale to talk more about the heritage fund's performance over the last six months.

Mr. MacMaster: Sure. Thanks, Kevin. For the quarter ending September 30, the return was 1.3 per cent for the quarter. AIMCo outperformed by 32 basis points and, as Lowell highlighted, for the fiscal year to date 2.37 per cent versus 2.29 for eight basis points. I always like to focus on the longer term, and if you focus on the table at the bottom of page 1 of the report, you can see the one-year, five-year, 10-year, and since-inception returns, which I would say, from an absolute return point of view, are pleasing. Also, AIMCo's value-add through those periods is also positive, so that's great.

Products adding value: fixed income, mortgages, private debt – all over the benchmarks – Canadian equities, global equities. Emerging markets was a big winner this past year. So, you know, a strong year. You're not seeing all the results, obviously, until the end of September, but we can tell you today that things seem to be stacking up very well for both absolute returns for our clients, including the heritage fund, and relative returns. We've had quite a bull market in assets for the last eight years, and we're very pleased to report those results.

I can leave it at that and take questions if you'd like.

The Chair: Sure. We'll open up the floor to questions.

Mr. Clark: Mr. Chair, I'd like to be on the list, please.

The Chair: I've got you, Mr. Clark.
We'll start with Mrs. Schreiner, Mr. Hanson, and then Mr. Clark.

Mrs. Schreiner: Thank you, Mr. Chair. Mr. Epp, in your remarks you mentioned that the legislated objective of the heritage fund is to maximize the long-term investment returns for the fund within a prudent level of risk. Could you tell us: how do you define what an acceptable level of risk is?

Mr. Epp: I thought you were going to give me an easy question.

The Chair: Happy New Year.

Mr. Epp: We look at a couple of metrics. The investment policy states what is known as a value-at-risk target, which we have listed, which states that in 19 out of 20 years we expect to lose less than a certain amount. I believe that amount is 10 per cent. That is one way we have defined an acceptable level of risk.

The other thing that we have done to take that risk into consideration or a prudent level of risk is that we've spread the assets around both globally and among a variety of different investment classes. We invest in fixed income, real estate, private infrastructure, private equity, global equities, global real estate. We are trying to diversify the risk as much as possible.

To define it in words is extremely difficult. We certainly benchmark against other funds and see what they're doing to make sure that the choices that we have made in terms of the investment policy are not wildly out of line and seem reasonable.

Mrs. Schreiner: Thank you, Mr. Epp.

The Chair: Okay. Thank you.
Mr. Hanson.

Mr. Hanson: Thank you, Chair. Just kind of a pertinent question because of what happened that was announced yesterday: is the heritage trust fund invested at all in Carillion, and will the collapse of Carillion have any effect on the trust fund, I guess?

Mr. MacMaster: We have no exposure to Carillion in Canada. In Canada, as I understand it, they're largely government services, road cleaning, hospital services. We have no exposure in Canada at all in our real estate portfolio. Where we might see some exposure would be probably in construction contracts, as I understand it. We're just checking with our folks in Europe. We don't believe we have any exposure to them in our European projects at all. We'll confirm that for you, though.

1:45

Mr. Hanson: Very good. Thank you.

The Chair: Thank you.
Mr. Clark.

Mr. Clark: Thank you. I have a couple of questions. I'll perhaps do one and let others ask questions and come back if there aren't any others.

I'm very curious about the Alberta growth mandate. You said here at the bottom of page 1 of the report that your mandate is to invest up to 3 per cent of the heritage fund in investments, and you've made 25 investments, totalling $345 million. Can you just confirm for me what percentage of that 3 per cent we're at? Does that $345 million represent the full 3 per cent?

Mr. Epp: The market value of the fund is $17.1 billion, so 3 per cent of $17 billion is roughly $510 million. We are probably around two-thirds of the mandate's fill.

Mr. Clark: I guess I'm just curious, given that that mandate has now been in place going on three years, what challenges present or why it is that we're approximately $170 million underinvested on the Alberta growth mandate.

Mr. MacMaster: Sure. I can answer that. I think the short answer is that we have pretty tough criteria to invest the heritage fund's money and all of our clients' money. It's a pretty high bar. We have to have a great return. It has to pass all of our due diligence tests, and it's challenging.

The one area where we've been pretty fruitful, I think, in finding good investments, as I've pointed out here before, is in the energy sector, which kind of coincided roughly with the time of this new policy, when the sector had a downturn and a lot of capital left that sector. So we made a number of investments there. We continue to search very thoroughly for investments, and we have a couple in the hopper now that I think will bring us much closer to that should they work out. I can't comment on those specifically today, but I'm very confident we'll get there.

I always like to remind the committee as well that we have, you know, roughly $8 billion, $9 billion invested across the portfolio, the $100 billion, in Alberta, and we continue to believe that it's an attractive place to deploy capital provided it meets our criteria.

The Chair: Thank you.
Mr. Horne.

Mr. Horne: Yeah. Thank you. I noticed that the fixed income was down .3 per cent for the first half of the fiscal year. In the second-quarter update it stated that the decrease is "largely due to rising interest rates over the first six months of the fiscal year." Now, as somebody keeping an eye on interest rates – it's definitely something I've been following personally – what impact do you expect the anticipated increase in interest rates by the Bank of Canada to have on those fixed-income investments moving forward?

Mr. MacMaster: Sure. I can answer that. I think it's important for the committee to understand that if we get an environment of, you know, rapidly rising interest rates – I'm not forecasting that – it would be impossible for us to immunize the portfolio against the impacts of that. So there could be periods where the fixed-income product has a negative return. Keep in mind, though, that we always invest with a positive yield. Through the full maturity of the investments you will get a positive return, but on a mark-to-market basis you can have periods where you have a negative return, and that's what happened in this period. I can tell you that, looking to the end of the year, bond markets rallied, and the longer dated pools, the universe pool, and the long bond pools had a positive return. That's just a general comment on fixed income.

Specifically, the Bank of Canada raised interest rates twice in the summer, catching the market off guard, on the back of some very strong economic numbers, and we continue to see some of those. We saw an employment report in Canada, with the creation of 78,000 jobs and the unemployment rate dropping to 5.7 per cent, a multidecade low. So I'd expect that tomorrow, when the Bank of Canada meets again, we'll see another increase in rates of 25 basis points, taking the bank rate to 1.25 per cent, and I would expect, through the course of 2018, that we'll probably see two more, in my estimate, as interest rates are normalized.

Of course, we've seen global growth continue to pick up. We've seen the labour markets continue to improve both in the U.S. and Canada and in Europe, and we're starting to see a global synchronized removal of excess stimulus in monetary policy and a gradual increase in interest rates. We don't think it's going to become unhinged. It'll be slow and meticulous. The good thing is that inflation, despite tight labour markets, is not showing any rapid, you know, increases. That could change, but for now it's been what we call a sort of Goldilocks economy, where we're getting good growth, relatively low inflation. That's ideal for assets, and that's why the markets have done so well.

Mr. Horne: Yeah. Good to hear. Certainly great to hear that both the local economy and also the international economy are really improving.

Tied to that, are you anticipating that returns on equities will improve as the economy improves?

Mr. MacMaster: Well, that's a great question. You know, equities have had a long bull run, and there are a number of challenges that we face in the equity portfolio. One of them is valuations. Price-earnings multiples are well above the mean. We do have monetary policy shifting. Traditionally that's been a hurdle for equity markets. We have a certain amount of complacency in the market, I would say, and even some speculation with things like bitcoin and the excitement around cannabis stocks and so on.

You know, if you look at the last seven or eight business cycles since World War II, when they've ended and stock markets corrected has been when interest rates start to rise. So we're kind of cautious on equities. We still think it's the better of those two assets, fixed income and equities. We think that equities will be more challenged, so we're staying there, but we would not be surprised to see a correction. It's well overdue. We would almost welcome it for an opportunity to buy good-quality stocks at discounted prices.

Mr. Horne: Thanks.

The Chair: Thank you.
Mr. Hanson.

Mr. Hanson: Thank you. Actually, I've got a couple of questions that are related, and they deal with page 1 of your report and page 1 of the Q1 report. I'm just looking at a couple of discrepancies here. The first one is that it says, "As of June 30 . . . the Alberta Growth Mandate has invested in 19 different companies totalling [$216] million." Then in this report it says that you've invested in 18 different companies with 25 investments. I'd just like some clarification on that, how we've gone from 19 companies down to 18 and 25 investments.

At the same time, the fair value of assets dropped from 17.2 to 17.1, but you're showing a 2.4 per cent rate of return in that same period. I'd just like to clarify what happened there.

Mr. Babineau: Sure. I could probably comment on the first one. That's probably just a classification mistake on the first one, where we classified investments as companies, so we probably went from 19 to 25. I'll double-check on that.

How we went from 17.2 to 17.1: that's the net asset value. We've had years previous where we've made gains, but we've not sold those investments. As we sell investments, we recognize that income, and that income is then transferred. When those investments are sold, it moves into a different bucket – it moves into the payable account to the GRF – and it thus reduces the net asset value. While right now our assets are probably a little higher than 17.1 because we still have some of those assets invested, at the end of the year we'll only have, based on this report, $17.1 billion in the account because we're paying out to the GRF.

Mr. Hanson: That's good. Thank you.

The Chair: Is that all?

Mr. Hanson: For now, yeah.

The Chair: Mr. Dang.

Mr. Dang: Thank you, Mr. Chair, and thank you, everyone, for coming today. Welcome back, I guess. I guess I have a couple of questions about the global views of investment and how you kind of see the long-term and short-term outlooks, specifically here in North America. There's an increased sense of protectionism in some of our immediately neighbouring jurisdictions, particularly the United States, as demonstrated through some of our NAFTA negotiations, that I'm sure most people are watching at home. I guess: how does this change our investment strategy, and is there more of a focus placed on the state level or anything when you're looking at opportunities for investment?

1:55

Mr. MacMaster: Sure. I'll tackle that one. Protectionism has been, you know, a theme for a couple of years now, of course, and we're reacting, like everybody else, to the daily news on NAFTA. It's definitely on the Bank of Canada's radar in terms of an uncertainty. I think the problem is that, you know, uncertainty keeps businesses from making investments and potentially delays capital investment. That's one concern.

I think that, longer term, these trade issues will sort themselves out, but there could be some bumps along the way. I think that what that means for investing is that while we see the U.S., you know, continue to grow and see some inflationary pressures, probably increase rates three or four times, we see the Bank of Canada lagging on that, probably because of the uncertainty around NAFTA. Also, another hurdle for us in Canada is really high debt levels right across the piece but primarily at the retail level, the individual level, the household level. We've heard a lot about debt to incomes, and we also see steps to slow down the housing market with various measures, and that also is on the Bank of Canada's radar screen.

The other implication could be, you know, for the Canadian dollar. If the U.S. continues to raise rates and Canada lags, we'll probably see some increased pressure on the Canadian dollar. Certainly, if there was some announcement on NAFTA, there would probably be a knee-jerk reaction like we saw a couple of weeks ago, when there were some stories circulating that Trump was about to rip up NAFTA and so on.

I think the thing we need to keep in mind with things like NAFTA is that in terms of trade we're quite balanced with the U.S. They need us as much as we need them, to a certain extent. It's very possible that this conversation ends up in Congress and not at the bargaining table, where there's a lot of vested interest in continuing to trade with Canada. But it is an uncertainty, and that has impacts on markets.

Mr. Dang: Well, thank you. Yeah, it's definitely something that I think most people are interested in watching.

I guess the other one that I have a question about is one of the other big trade deals, obviously, that we're involved in. How do negotiations around the TPP 11 sort of affect our markets and how the outlooks look?

Mr. MacMaster: Most of the strategists and economists we talk to really downplay that. I mean, while it's good, our key trading partner, really, is the U.S. It's just dwarfed by TPP. Maybe that changes in 10 years, but we really don't hear any economists revising, you know, their outlook based on that.

Mr. Dang: Thank you.

The Chair: I have Dr. Turner, Ms McKitrick, Mr. Clark on the phone and then Mr. Hanson.

Dr. Turner: Thank you. Thank you very much to AIMCo and Treasury Board for this very illuminating review. I'm sure all Albertans, actually, are relieved to hear that that fund that supports our pensions as well as the heritage trust fund is doing so well.

I want to ask some questions about the fixed-income investments. Just like my colleague to the left here but at the other end of the age spectrum, these sorts of investments are the things that I'm personally supposed to be involved in. I think that when we're talking about pension plans and other sorts of investments that the province does, the fixed-income portfolio is the vital one. I'm afraid that some people listening to this report might think: oh, we've lost .3 per cent on that. I guess I've got a few questions. One is: what percentage of the heritage trust fund portfolio is in this sort of investment? Can you reassure Albertans – and I know you can – that even though the capital, basically the price of these investments, has gone down, that doesn't have anything to do with the return and the stability of their pensions or of the investments in the trust fund?

Mr. Uebelein: Well, I think I'll take the first crack simply because I've been so quiet. First, I think you've in essence answered your own question to a large extent.

Dr. Turner: I'm not supposed to ask a question I don't know the answer to, right?

Mr. Uebelein: I'll remember that.

As you know, if you're holding a fixed-income security, that's paying a fixed income, and interest rates rise, then the value of that security, if you were to sell it, will go down. They always work in that direction.

About 18 per cent of the heritage fund portfolio is in debt or so-called fixed-income assets. But unless and until those securities are sold, those losses are purely theoretical. They're mark-to-market losses. This also underscores, in essence, one of the points that Mr. Epp made before, which is that there is a real difference between investment income and investment returns, and that difference is, in essence, what leads to what amount is taken out of the heritage fund for the general revenue account. It's only those realized gains that are taken out for the general revenue account.

If you hold these securities to maturity, you'll continue to receive a positive return equal to the fixed-income coupon, and those mark-to-market losses will slowly just dissipate to zero. Meanwhile, if interests rates are rising, with additional cash flow we can buy into those higher interest rates and buy a higher coupon.

Dr. Turner: What is the proportion of the fund that's in these investments?

Mr. MacMaster: Eighteen per cent.

Dr. Turner: Okay. That's good. Thanks.

Mr. MacMaster: If you turn to page 2 in your report, it has the whole asset mix there for you.

Dr. Turner: Okay. Just on the comment about the rising interest rates, one of the things that I've observed in my own investments is that preferred shares that have I think it's called a variable return actually are rising in value. They may be rising in value, too, because the underlying company that they're issued by is doing well. But I'm pretty sure you folks know all about those sorts of manipulations as well.

Can I turn to the inflation-proofing thing? Just in follow-up to the previous questions, one of the big changes that had happened that might affect inflation was the change, basically, in the Fed in the U.S. from Yellen to – now I've forgotten the fellow's name that took over.

Mr. MacMaster: Powell.

Dr. Turner: Powell. My reading of this was that this was not a big change in terms of fiscal philosophy, but I'd be pleased to hear what AIMCo thinks.

Mr. MacMaster: Yeah, I would agree. These changes at the Fed aren't something we need to be too concerned about. The one remarkable thing about Powell: I think he's the first Fed chief that's not an economist. I think that was probably the most significant. But you have to remember that it's the Federal Open Market Committee that decides and that these decisions are well thought out, and there's a lot of bench strength on that. I think they're best positioned to make the right decision when it comes to monetary policy.

Dr. Turner: There's $123 million in the fund for inflation-proofing. It was mentioned in the public meeting that this is a key feature of our fund. Just as with MLA Schreiner's question about how adequate return is adjusted, how do you determine how much you need to protect from inflation? Who decides the number for inflation-proofing?

Mr. Epp: The Minister of Finance is ultimately responsible for setting the investment policy for the fund. The asset allocation between fixed income, inflation-sensitive and alternative investments, and equities and then subclasses to those was decided through some detailed what we call asset mix studies, where we ran numerous simulations to see, in our estimate, what would happen under various scenarios with various portfolio configurations. So that's how that was determined.

Dr. Turner: Great. Thank you very much.

The Chair: Thank you.

Ms McKitrick.

Ms McKitrick: Thank you, Mr. Chair. I have a number of questions that I'm going to ask. I think that in previous meetings we had some really good discussion about AIMCo's responsible investing policies and some of the things that you were doing that were really cutting edge in the investment sector. I wanted to first of all ask you a question around the fact that world-wide there are more investment opportunities around renewable energies. I was wondering if that was something that AIMCo is considering in terms of its investment policy.

2:05

Mr. MacMaster: I'll speak to investing in the renewables.

Would you like to comment generally on ESG?

Mr. Uebelein: Sure. Do you want to go first?

Mr. MacMaster: Yeah. In terms of renewables we've got a number of investments in that space in wind and solar in the U.S. primarily, but we are looking at some opportunities very close to home, so we continue to explore that. The reality of that space, though, is that, you know, with the economics today they still need government subsidies and encouragement, so that's just something to keep in mind. Technology continues to drive improvements there, but they still require government subsidies. We are fully invested there, so I wanted to make sure that you're aware of that.

Mr. Uebelein: In terms of AIMCo's approach to so-called ESG – environmental, social, and governance – issues, first off we are really proud of the work that we're doing. It's forged not just on what AIMCo thinks is the right thing to do but from multiple iterative conversations with our clients. It's our pension clients and the folks here to my right who talk to us about what they would like to see us trying to accomplish. I would categorize our attitude towards this into sort of two buckets.

One is that there are things that we want to take a stand on and say that we will not invest in because we think that it's bad for society. That's a very short list that would include things like weapons of mass destruction, tobacco, and things where, from a societal standpoint, we've decided that, regardless of the investment returns that might be possible, we're not going to go there.

When you go beyond that, what we're looking for is to invest in companies and, more importantly, not just companies but the management teams that are running these companies, that seem to have their eye on these issues, on how they're evolving and how they impact, the long-term impact on our world. That's important to us because what we've found is that management teams that are thinking progressively about environmental issues, about social issues, and around governance issues – for instance, how many women are on the board? – tend to correlate with companies that outperform the median over very long periods of time.

Now, I want to be really careful. I'm not saying that one is driving the other, but the correlations are there through multiple studies that show that enlightened management teams – and maybe it's because they're doing other things really well, but teams that are thinking about these issues tend to have stocks that outperform over very long periods of time, five, 10 years. We are trying to drive smart decisions that are good for the world, but it's also a self-enlightened strategy, in all honesty. We're working with management teams to try to get them to think progressively about, for instance, how many women they have on the board. We have active conversations about to what extent we will use our influence with our investing companies to try to get them to think that way, and it's a constantly evolving process, frankly.

Mr. MacMaster: I can give you some specifics, too. Just so you know, I mean, our responsible investing protocols involve, certainly, our proxy voting but engagement with companies, advocacy as well, communication with our clients and stakeholders like we do here today. Just to give you some idea, the ESG group, the responsible investing group, reports to me, and we are integrating those protocols when we review investment. For instance, on private equity, last year the ESG team did due diligence on six private equity funds that we committed to totalling $635 million in AUM and to assets, co-investment assets, of $350 million. They actually have due diligence checklists that they meet with management on and discuss to make sure they're aligned with us.

On proxy voting, the main areas, as Kevin highlighted, are on, say, pay, women on boards, board independence, and ESG disclosure, so things like carbon footprinting. We voted on 610 shareholder proposals, a 29 per cent increase over last year, and 31,000 ballots. This is a big part of this team's activity and reviewing every single proxy on our equity holdings and voting on those in accordance with our protocols. It's a very important area in our firm, and we're even taking a next step in terms of integrating perhaps models using ESG factors to select investments. It's an exciting area. It's a growing area. It's a very important area for us.

Ms McKitrick: Thank you. I really appreciate it. As an MLA in this province it's nice to know that the team that's looking after the heritage trust fund and, you know, our leaders have those values. I think it's a really good-news story for us, so thank you.

I wanted to talk a little bit about the larger picture of investment climate in general. We kind of, I think, you know, have touched on it, but I think it's really important at the moment. I understand that across the country the economy is improving and that here in Alberta we've added 26,000 jobs and that the economic indicators are looking up. Retail sales are up, manufacturing is up, and restaurant sales are up. I was wondering what your overall outlook on the investment climate in this province is.

Mr. MacMaster: Well, that's a tough one. We tend to have a global viewpoint and more of a national one, but I would say that for Alberta it's encouraging to see the signs that we've seen recently. You alluded to the job report, where Alberta actually led the country in job creations. That's great to see after, you know, the correction we saw in 2014, which was quite painful for us here in the province. That's great to see.

You know, I think Alberta still faces challenges, though, and probably the biggest one is in the most important sector here, which is energy, and that's getting the product to tidewater, to new customers. The U.S. is becoming a leader in energy production, in oil and gas, and we just can't depend on that same customer. There are obviously issues around that. Everyone is well versed in the pipeline debate that's happening. In the last couple of years growth has been driven by east and west. B.C., Ontario, and Quebec have improved their fiscal situation and come along. I'm encouraged to see Alberta pick up, but there are challenges ahead.

Mr. Uebelein: Just to add to what Dale has said, when we talk to our contacts in Calgary, I mean, they're still feeling quite a bit of pain, but if you look a little deeper, it's a good-news, bad-news story. What do I mean by that? Oil companies through this crisis have taken very active steps to reshape themselves. They've increased their efficiency. They've lowered their costs to a point where they can make money at much lower costs, but they've shed a lot of jobs in doing that. They've changed their economic model, if you will, so many of those oil patch jobs that were around before this cycle won't come back the same way because they've fundamentally used this as an opportunity to drive efficiencies through, to embrace and adopt technologies that allow them to have a lower cost point. That's good news because these oil companies, that are critically important for the backbone of Calgary and Alberta as a whole, are now profitable, and they will start to slowly reinvest. But to think that all those jobs are going to rebound in the same way is naive. It just won't happen. That's just a reality. As we see Calgary and the rest of Alberta recover, it's going to be through diversification into other industries, and we'll see that. It'll be positive in the long run.

Ms McKitrick: My last set of questions touch a little bit there.

The Chair: Ms McKitrick, I'm just going to move on, and we'll come back to you.

Ms McKitrick: Okay. That's fine.

The Chair: Mr. Clark, coming back to you on the phone.

Mr. Clark: Yeah. Thank you very much. Just briefly I wanted to pick up again on the Alberta growth mandate. Do you report it anywhere or can you tell us what the rate of return has been on the funds, the $345 million invested in the Alberta growth mandate?

Mr. MacMaster: The short answer is no. One of the challenges is because the investments are across different pools. We have infrastructure. We have equities. We have fixed income. They're spread out. We haven't actually sliced it, you know, just based on that 3 per cent. In fact, we don't even look at it from a total Alberta point of view, which would include everything we've got invested in Alberta, the $9 billion I referred to earlier across our complete asset mix.

2:15

Mr. Uebelein: I'm afraid we don't have a crisp answer for that, but I would say that anecdotally those investments have performed very well for us.

Mr. MacMaster: Yes. Anecdotally, I can't put out numbers, but certainly both dispositions that we made – TransAlta Renewables was a sizable investment, was a 45 per cent, you know, IRR, a really terrific return. We did sell that because it became overvalued. We got it at quite a discount, around $9, and sold it at over $14, and it's continued to slide in price, so that looks like a very good sale despite the equity markets moving higher. That was a great outcome. That would have lifted the portfolio. Savanna as well wasn't an investment we wanted to sell, but it was a hostile takeover and the shareholders voted, and we ended up with, I think, a 30-plus per cent return there. I would say that the results of the portfolio, the 3 per cent, are quite good.

Mr. Clark: I'm curious, though. I'm going to press this a little bit both here and going forward because while I love a good anecdote, I like data much better. If we've got something that has been mandated by the government to you in terms of a particular amount of money, I just think it's noteworthy that only two-thirds of the money, of that 3 per cent, has been allocated. I think that's interesting. I appreciate that you've applied some rigour in terms of what you feel is a reasonable return.

I acknowledge that TransAlta and the Savanna transactions have come good, but of the other I believe 25 or so, I guess 23 or so, are there any, you know, outside losses? With high risk can come high return but also, of course, can come substantial loss. So where we've got higher risk elements in the portfolio, I do think it's important that we have some oversight, so I would ask that we going forward be provided with some actual data on how we're doing in these particular investments.

Mr. Uebelein: Absolutely. We'll take that back with us, and we will work on that so we have something better than purely anecdotal responses.

The Chair: Okay. Thank you. So you will endeavour to get a written response. Is that what you're saying, Mr. Uebelein?

Mr. Uebelein: Yes.

The Chair: Thank you.

Mr. Clark: Thank you very much.

The Chair: Mr. Hanson.

Mr. Hanson: Thank you. I'm going to chase that Alberta growth mandate again if you don't mind, Chair. The first two bullet points in the criteria for investing: number one is to create jobs in Alberta, and the second one is to build new infrastructure in Alberta. Could you give us an example of infrastructure that these companies that you've invested in have built, and, possibly, if there are any measurables, how many jobs have been created in Alberta? I know that some of the companies that have been invested in are definitely creating jobs but not necessarily in Alberta. So I was wondering if you would have some examples that you could talk about or some of the measurables that you use and if you could talk about, possibly, some of the new companies that you've invested in in the last year here in Alberta.

Mr. MacMaster: I don't have any jobs data, but I can tell you that our real estate development projects – I'm pretty confident that jobs were created there to build these structures – Manning Town Centre, StoneGate industrial building, West Village Towers, StoneGate Common: all of these involve real estate development which would have created jobs, we think. I don't know how many. Certainly, Calfrac, I think we mentioned here last time, you know, brought back a lot of their employees, and I'm not sure in which jurisdictions those were.

I can tell you a little bit about what we've done recently. One of the investments we made recently was in Bonnefield, which is an agricultural fund based on farmland. That was a recent investment partly based in Alberta as well as Saskatchewan and Manitoba. We've made a number of investments in the energy patch, which I've mentioned before: Western Energy Services, Ikkuma, Ember Resources, Whitecap, Journey. All these are variations of oil and gas companies, some in production, some in oil field services, where we've primarily done debt and equity transactions. So there'd be debt with warrants attached. Again, I can't give you jobs data, but those are some of the recent investments.

Mr. Uebelein: Yeah. A couple of high-level comments, and these will all be comments that in one way, shape, or form we have already talked about in previous standing committees. The first is that these criteria for the 3 per cent allocation to the heritage fund, the so-called growth mandate, are not in lieu of our risk-based return criteria. On every investment we make for the heritage fund or any of our other clients, our first and our primary criteria is: are we going to, in our judgment, get an adequate investment return for the units of risk that we're taking on those investments? So it is not an either/or. We don't look at these growth mandates and say: are we going to accomplish these other criteria at the risk of having a poor risk-adjusted investment return? It's both.

Secondly, the types of investments that AIMCo makes in companies like this are ones where we would not have in the ordinary course the leverage to say: how many jobs is this X-million-dollar investment in your company going to create? It is not as simple as that. It doesn't come down to either that level of leverage on our part or that level of sort of calculable rubric.

However, what we are, I would say, counting on and confident of is that when we invest in strong, Alberta-based companies that are hiring and hiring Albertans, when we make a capital investment in these companies, good things will happen, and it will be a better outcome than if we hadn't made these investments in Alberta companies. So this is one instance where if you ask us to come up with anything other than anecdotal, I'd probably say that I can't do it and I won't do it because it's just not possible, whereas with the investment returns we're going to come back and answer Mr. Clark with a greater level of specificity.

The Chair: Okay. Mr. Dang.

Mr. Dang: Thank you, Mr. Chair. I just had a quick, maybe kind of complicated question, just something I think Dale brought up earlier around cryptocurrencies and bitcoin, around those types of things as the market is developing around those. I understand that they're going to be traded on open markets sooner rather than later in the United States and around the world. What sort of, I guess, almost speculation do you have about that and potential exposure that you might be interested in taking, or where do you think that it's going to go in terms of affecting markets we are actually invested in? We've seen rather large companies in the last month or two basically tack blockchain on the back of their name and see significant rises in the market, right? So, I guess, what are your general thoughts around that?

Mr. MacMaster: Well, I guess my general thoughts are, you know, that this is kind of a classic example of late-stage bull market excess speculation, whether that's the dot-com that we've seen before or I think it's touching on the cannabis stocks as well a little bit. I think that's what you're seeing. I can't ever see us investing in such a thing because we have no way to value these things, right? There's a lack of information. Whatever is behind these is behind closed doors. It's really a speculation. It's not going to stop people from perhaps throwing money at it, but I think there's a need, too, to separate the idea of bitcoin and cryptocurrencies with the blockchain technology, which I think has some value. I'm not a technology expert, but everyone that I talk to about it seems to think there's real value in blockchain technology. But the cryptocurrency is a classic example of something we would not do, and they're not currencies by the definition. I think you've seen a number of central banks come out and say that they don't qualify for the criteria of what a currency is.

2:25

Mr. Dang: Yeah. For sure. Thank you. I mean, definitely, we've seen some of values of these basically go parabolic, right?

Mr. MacMaster: Right. And that's what you need, right? To get people involved and to believe, you need prices to go up. And you can see that in every speculative bubble that we've seen for the last thousand years.

Mr. Dang: Thank you.

The Chair: Ms McKitrick.

Ms McKitrick: Thank you, Mr. Chair. I was going to ask you a question about the Alberta growth mandate's investments in oil and gas, but I think you've kind of covered that. I think one of you made a remark about the need for diversification in the province, so I was wondering about your investment in agricultural companies in Alberta and the room or the possibilities around more investment in the agricultural sector here.

Mr. MacMaster: Yes. That's a good question. We'd love to do that. It's challenging for a number of reasons. The agriculture investment is a strategy within the timber pool, which is itself quite small, but we have found, you know, a way to dip our toe there. It's through a fund investment because, as you can appreciate, agriculture tends to be the type of asset that's widely held and not easy to accumulate, so we made a relatively modest investment there. We'd love to do more, but it has its own challenges.

Ms McKitrick: And the investment you made is part of the Alberta growth mandate, the 3 per cent in Alberta companies?

Mr. MacMaster: Yes.

Ms McKitrick: Okay. We all appreciate it. Thank you.

The Chair: Thank you.
I have no other people on the question list.

Mr. Ellis: Chair, I have a question if you don't mind.

The Chair: Sure. Go ahead, Mr. Ellis.

Mr. Ellis: Okay. I just want to follow up in regard to the growth mandate, that everybody seems to be talking about over the last series of questions. I guess to AIMCo: have you received any feedback from the Finance minister or from anybody, you know, since it came out in 2015, as to how they believe things are going? Are they happy with the pace? I mean, I certainly appreciate that you guys are being very responsible and prudent. You also have the mandate to ensure that you're getting the best possible return for Albertans on their money. I'm just curious as to what, if any, other feedback you received on the work that you've been doing.
Thank you.

Mr. Uebelein: I would say that the kind of dialogue that we have with the minister's office is not dissimilar to the conversations that we're having here at this standing committee. They're eager to know what we're doing. They're respectful of the different roles that are played; in other words, that it's government's place to set asset allocations and that it's AIMCo's role to then pick those investments. So while they're eager to know what we're doing and to probe on that, they're also very careful not to cross that line. It's very similar to these conversations, I would say.
Would you add anything to that?

Mr. MacMaster: No. I think that covers it.

Mr. Uebelein: I mean, I think they wish that we invested more. We wish we could invest more, but we're doing the best that we can. We don't want to make investments that short-run look good and then lose everyone capital. It's as simple as that.

Mr. Ellis: Thank you, gentlemen.

The Chair: Great. Any final questions?
Okay. Seeing none, would a member like to move that the committee receive the second-quarter report? Mr. Horne. It's moved by Mr. Horne that

> the Standing Committee on the Alberta Heritage Savings Trust Fund receive the 2017-2018 second-quarter report on the Alberta heritage savings trust fund.

All in favour? On the phones? Any opposed? That motion is carried.
The next item on the agenda is the public meeting follow-up. As you know, hon. members, the committee held a public meeting on October 26, 2017, to provide information and answer questions from Albertans on the activities and state of the Alberta heritage savings trust fund. The attendance for this year's public meeting was significantly higher than in previous years, with 38 public members in the committee room and in the overflow rooms here at the Federal building. There were 38 questions posed by Albertans during the meeting: 19 via e-mail, two via Facebook, two via Twitter, and 15 in person. The public meeting was broadcast on Shaw TV in markets outside of Edmonton and Calgary, and it was streamed online through the Assembly website, which had 35 viewers.
I would now like to call upon the committee clerk to provide a brief overview of the costs associated with this public meeting, and then we'll have questions after that.

Mr. Roth: Thanks, Mr. Chair. I had sent to members of the committee via the internal website the breakdown of the various costs associated with the public meeting. Overall, it was a little bit higher than in previous years, but based on the communications plan that was approved for the public meeting, it definitely was within the scope of that. As the chair mentioned, this year not only did the room here fill, but the overflow room had about a dozen people in it as well, and it seemed to work well in terms of bringing people back and forth between the two rooms in terms of asking questions.
That's all I have, Mr. Chair.

The Chair: Thank you.
I'll open the floor to any comments or questions on the public meeting. Well, it just went that smoothly, I guess. There you go. Good.
We'll move on to item 6 on the agenda today, the draft annual report of the committee. One of the functions of this committee, as mandated in section 6(4)(c) of the Alberta Heritage Savings Trust Fund Act, is to "report to the Legislature as to whether the mission of the Heritage Fund is being fulfilled." The last such report was made to the Legislative Assembly on March 14, 2017, which covered the activities of the committee from December 2015 to December 2016. Since that time the committee has met several times and performed several of its functions as outlined in the act. Past practice has been for the committee clerk to prepare a draft report for the committee's consideration and that the committee's

report be made to the Assembly in the spring session of the Legislature.

Now, do any members have any comments or questions regarding the process of this or the activities in the Assembly?

Seeing none, we'll move on to other business. Is there any other business arising? On the phone?

Ms McKitrick: I'm sorry. I missed the opportunity when we were talking about the public meeting. I feel that the success of the public meeting was really due to the preparation of the staff and the way that they managed the questions and everything. I would like to give a vote of thanks to the staff for all their work in making sure that the public meeting fulfilled the mandate of this committee, which is to inform all Albertans about the work of the heritage trust fund.

The Chair: Well, thank you, Ms McKitrick. I will take this opportunity, too, to thank all the staff for the amazing job they did on the preparation for that meeting. Thank you very much.

If there's no other business, then the date of the next meeting will be sent out to the committee.

I would like to call for a motion to adjourn. Dr. Turner moves that this meeting on the Alberta heritage savings trust fund be adjourned. All in favour? On the phone? Any opposed? That motion is carried. The meeting is adjourned.

Thank you.

[The committee adjourned at 2:34 p.m.]

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