Legislative Assembly of Alberta

The 29th Legislature
Fourth Session

Standing Committee
on the
Alberta Heritage Savings Trust Fund

Tuesday, September 25, 2018
1 p.m.

Transcript No. 29-4-3

Legislative Assembly of Alberta
The 29th Legislature
Fourth Session

Standing Committee on the
Alberta Heritage Savings Trust Fund

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

Cyr, Scott J., Bonnyville-Cold Lake (UCP)
Dang, Thomas, Edmonton-South West (NDP)
Ellis, Mike, Calgary-West (UCP)
Horne, Trevor A.R., Spruce Grove-St. Albert (NDP)
Kleinsteuber, Jamie, Calgary-Northern Hills (NDP)*
Loyola, Rod, Edmonton-Ellerslie (NDP)**
Luff, Robyn, Calgary-East (NDP)
McIver, Ric, Calgary-Hays (UCP)***
McPherson, Karen M., Calgary-Mackay-Nose Hill (AP)
Turner, Dr. A. Robert, Edmonton-Whitemud (NDP)

* substitution for Thomas Dang
** substitution for Bob Turner
*** substitution for Scott Cyr

Office of the Auditor General Participant

W. Doug Wylie	Auditor General

Support Staff

Robert H. Reynolds, QC	Clerk
Shannon Dean	Law Clerk and Director of House Services
Stephanie LeBlanc	Senior Parliamentary Counsel
Trafton Koenig	Parliamentary Counsel
Philip Massolin	Manager of Research and Committee Services
Sarah Amato	Research Officer
Nancy Robert	Research Officer
Corinne Dacyshyn	Committee Clerk
Jody Rempel	Committee Clerk
Aaron Roth	Committee Clerk
Karen Sawchuk	Committee Clerk
Rhonda Sorensen	Manager of Corporate Communications
Jeanette Dotimas	Communications Consultant
Tracey Sales	Communications Consultant
Janet Schwegel	Managing Editor of *Alberta Hansard*

Transcript produced by *Alberta Hansard*

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

Alberta Investment Management Corporation
Dale MacMaster, Chief Investment Officer
Mark Prefontaine, Chief Client and Stakeholder Relations Officer
Kevin Uebelein, Chief Executive Officer

1 p.m. Tuesday, September 25, 2018

[Mr. Coolahan in the chair]

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

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

Mr. Ellis: Mike Ellis, Calgary-West.

Mr. Prefontaine: Mark Prefontaine, Alberta Investment Management Corporation.

Mr. MacMaster: Dale MacMaster, AIMCo.

Mr. Uebelein: Kevin Uebelein, AIMCo.

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

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

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

Ms Luff: Robyn Luff, MLA for Calgary-East.

Mr. Kleinsteuber: Jamie Kleinsteuber, the MLA for Calgary-Northern Hills.

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. I'd like to ask those participating on the phone to introduce themselves. I'll start with Mr. McIver. Are you on the phone, Mr. McIver?

Okay. Mrs. Schreiner.

Mrs. Schreiner: Kim Schreiner, MLA for Red Deer-North.

The Chair: Great. Thank you.

If Mr. McIver comes back on, just let me know.

Okay. As per Standing Order 56(2.1) to (2.4) I would like to note the following substitutions for the record: Member Loyola was intended to substitute for Dr. Turner, Mr. McIver was intended to substitute for Mr. Cyr, and Mr. Kleinsteuber is substituting for Mr. Dang.

Before we turn to the business at hand, a few operational items. Please note that the microphones are operated by *Hansard* and that the committee proceedings are being live streamed on the Internet and broadcast on Alberta Assembly TV. Please set your cellphones and other devices to silent for the duration of this meeting.

The first item on the agenda is the approval of the agenda. Would a member like to move approval? Mr. Kleinsteuber moves that the agenda for the September 25, 2018, meeting of the Standing Committee on the Alberta Heritage Savings Trust Fund be adopted as circulated. All in favour? On the phone? Thank you. Any opposed? Hearing none, that is passed.

It sounds like you're there now, Mr. McIver. Would you mind introducing yourself?

Mr. McIver: Ric McIver, MLA, Calgary-Hays.

The Chair: Great. Thank you.

The next item is the approval of the minutes from June 20, 2018. Would a member like to move that the minutes for the June 20, 2018, meeting of the Standing Committee on the Alberta Heritage Savings Trust Fund be adopted as circulated? Ms Luff moves that the minutes for the June 20, 2018, meeting of the Standing Committee on the Alberta Heritage Savings Trust Fund be adopted as circulated. All in favour? On the phone? Okay. Any opposed? Hearing none, that is carried.

The next item will be around the trust fund's first-quarter report. The Alberta heritage savings trust fund's first-quarter report for 2018-2019 was released on August 29, 2018. 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 with AIMCo and Mr. Lowell Epp and Mr. Rod Babineau of Treasury Board and Finance here to assist us with our review.

With that, I will turn the floor over. Mr. Epp is going first? Okay. Thank you.

Mr. Epp: Thank you, Mr. Chair, and thank you, members of the committee. Minister Ceci is unable to attend today and sends his regrets. I am certainly pleased to be here on his behalf to provide a brief update on the Alberta heritage savings trust fund's first-quarter report. Once we've completed it, we are certainly willing to take questions and answer any questions you may have.

As for the heritage fund's quarterly report, I will spend a few minutes to provide some highlights from the report and then ask my colleagues from AIMCo to speak about the fund's results from their perspective and to provide some commentary on the financial markets.

As of June 30, 2018, the fund had a market value of $17.6 billion, a net income of $286 million for the first three months of the year. Investment expenses were $33 million for the quarter. The fund was invested at that time 43 per cent in equities, 37 per cent in inflation-sensitive assets, 19 per cent in fixed income, and 1 per cent in overlays.

When looking at the fund's investment performance, the focus of any evaluation should start with the long-term returns given that the legislated mandate of the fund is to maximize those returns over the long term. Over the past five years the fund has earned a return of 10.6 per cent. Over the past 10 years the fund has had a return of 7.9 per cent. The fund's objective, as we've discussed before, is to earn a return of 4 and a half per cent above the rate of inflation over the long run. The five-year return is 4.5 per cent above the target, and the 10-year return is 1.7 per cent above the target, so it is achieving its long-term investment objectives.

It is also important to measure performance against the market-based benchmark. Over the past five and 10 years the fund has outperformed its market-based benchmark by .8 per cent and .6 per cent respectively. The goal for the fund is to outperform this benchmark by 1 per cent over the long term. Over the recent past the fund's returns were slightly below this target.

Year-to-date results have been relatively good. During the first quarter of the current fiscal year the fund earned a return of 2 per cent. When looking at components of this return, equity investments earned 3.6 per cent, inflation-sensitive assets returned .8 per cent, and fixed-income investments earned .9 per cent.

Lastly, I would like to give a brief update on the Alberta growth mandate. Since the announcement of this mandate in 2015 AIMCo has made commitments to 31 separate investments, and these have a total of $386 million. All of these investments, of course, meet the heritage fund's legislated requirement to maximize long-term investment returns. As before, we will continue to provide the committee clerk with periodic reporting regarding investments made under this mandate as appropriate.

That concludes my remarks for today, Mr. Chair. Thank you.

The Chair: Thank you.

We'll move on to AIMCo.

Mr. Uebelein: I'll go first, then. So far this year we've experienced continued strong economic growth figures across most developed economies and corresponding strength in those equity markets. However, despite these positive signals, we're cautious regarding the ongoing health of the global bull market.

The reasons for our caution include the following. First, as Dale and I have continued to say before, economic expansion and bull markets do not and cannot last forever, and the current bull market is already now one of the all-time longest in history. Second, we've already seen a significant narrowing of the breadth of the market gains this year, meaning that while the market continues to perform well and is rising, it is being derived by a smaller and narrower number of companies. Finally, third, we do believe that continued upward pressure on interest rates and the threat of growing trade protectionism will have some dampening impact on the global economic growth and therefore also on asset prices. However, predicting when or measuring the degree of this impact is always difficult.

All in, these factors lead us to be cautious but, to be sure, not necessarily bearish. I would also add that should a worst case happen – and that is a severe market correction – we believe that the heritage fund portfolio and the portfolios of our other clients are in a position to safely withstand such an event and that Dale and his team are ready to take advantage of tactical opportunities on behalf of our clients.

With that, I'm going to pass the microphone to Dale.

Mr. MacMaster: Thank you. The heritage fund returned 2 per cent for the quarter. This was led by equities, which returned 3.6 per cent for the quarter. It represents 43 per cent of the portfolio. Canadian equities, which represent 9 per cent of the fund, had a strong quarter, led by energy stocks, returning 6.3 per cent for the quarter. We already talked a little bit about the longer term performance relative to benchmarks, and that's all great, with very good total absolute returns and relative returns as well. I would just emphasize that if you look at the five-year number, at 10.6 per cent, it really stands out how good the most recent past has been for investors.

1:10

Now, while we are pleased with the results, I'd like to echo Kevin's comments that the investing environment has become more challenging as we find ourselves in the late innings of the business cycle and a bull market that is now 10 years old. We see the North American economies at full employment, with unemployment rates the lowest they've been in decades. Consumer confidence is high, and the housing market has now fully recovered. Along with that robust economy come wage pressures that are starting to push inflation a little bit higher. As a result, central banks around the world, not only in North America, are starting to lift interest rates and remove the stimulus which has driven asset prices over the last 10 years. This is typical of the late-cycle dynamics. We've seen it before. We'll continue to take care in investing, as all investors should be doing.

After 10 years now in this bull market corporate earnings have likely peaked. Equity valuations are stretched. The corporate credit environment is also frothy, with corporate credit spreads being very tight. We haven't seen these levels since 2006, just before the credit crisis. The landscape for liquid assets is also challenging. We see stiff competition for assets in the infrastructure and real estate and private equity programs. Real estate has had an excellent run in the last 10 years, a great period of performance, but we see vacancy rates very low and cap rates also quite low on top of government bond rates. Again, another reason to be a little cautious here.

We expect the Federal Reserve to raise interest rates tomorrow, which would be the eighth increase in this cycle since 2015. We think Canada will likely follow in October. It's expected that with the withdrawal of monetary stimulus combined with the issues around trade, the global economy will also start to slow as we move through the rest of 2018 and into 2019 and '20, with a chance of a recession in the coming year or two.

Putting the combination of one of the longest bull markets together with the valuations, the interest rates starting to go up – of course, no one has a crystal ball – we think it's a time for investors to be extra cautious. We don't want to be overpaying for assets. Rather, keeping a little bit of cash on hand should markets fall out of bed would be the obvious for long-term investors ready to step in and do some buying on behalf of all Albertans.

My colleague just passed me a note here. I believe there was an outstanding question from the last meeting around an investment that we made that was confidential. We were under an NDA, which is a confidentiality agreement, so we could not make that name public, but now that's been lifted. The company was Trident Exploration, which is a private company based here in Alberta involved in gas exploration.

The Chair: Does that conclude your remarks?

Mr. MacMaster: It does. Thank you.

The Chair: Excellent. We will open the floor to questions.

First I would like to ask Member Loyola to introduce himself, please.

Loyola: Thank you very much, Mr. Chair. I'm Rod Loyola, MLA for Edmonton-Ellerslie.

The Chair: Great. Thank you.

Starting with Mr. Ellis, I'll keep a list.

Mr. Ellis: Thank you very much, Chair. Thank you, gentlemen, for being here and for an excellent presentation as usual. Mr. MacMaster, I just had a question. You had mentioned energy stock returns. I think you said that they were positive. Can you expand on that slightly? What type of energy stocks were you investing in that received such positive returns? Wind, solar, oil and gas, as an example?

Mr. MacMaster: Sure. Just to go back over my comments, Canadian equities enjoyed a single quarter of good returns, 6.3 per cent. Unfortunately, the first quarter wasn't so great, and the third quarter isn't shaping up as well. If you'll recall, during the second quarter oil prices started to move higher and Canadian energy stocks had a nice lift. Unfortunately, the differential for local crude versus, you know, global benchmarks has widened, and those equity stocks have rolled over. I was referring to the sector in general. I think that for the second calendar quarter, our first quarter, energy stocks as a group were up about 14 per cent.

It was the biggest increase of all the sectors within the Canadian market. But, as I said, there are numerous challenges there going forward with pipeline policies. You probably read about it in the paper every day.

Mr. Ellis: If I can just follow up, Chair. Are these investments in Alberta companies as it pertains to, of course, the Alberta mandate, or are these – I mean, obviously, you're wanting to get the best return for Albertans on their money. Are these positive returns coming from, you know, other energy companies that are outside of Alberta?

Mr. MacMaster: Well, both. You know, a large component of the subindex in energy is based in Alberta. Of course, this is a market-weighted benchmark, so the Suncors and CNQs of the world would carry the biggest weights and probably have the biggest impact on that index. I can't tell you which stocks drove that; I don't have that level of attribution. But the entire boat was lifted, for the most part, in that quarter.

Mr. Ellis: Thank you, sir.
Thank you, Chair.

The Chair: Thanks.
Mr. Loyola.

Loyola: Thank you very much, Mr. Chair and through you to the gentlemen at the table. I want to thank you very much for being here today and for the insights that you shared regarding your presentation.

On page 1 of the report it discusses the Alberta growth mandate, which was to invest up to 3 per cent of the fund directly into Alberta growth. What percentage of the fund has in fact been invested in Alberta growth since the mandate was announced as part of Budget 2015?

Mr. MacMaster: In total $386 million, and currently $154.6 million is outstanding. We made a number of investments. Some of them have been sold, you know, at a nice profit. TransAlta Renewables is one that comes to mind.

Loyola: Okay. As the Alberta economy continues to recover – I mean, exports are up, manufacturing is up, wages are up – what impact does Alberta's economic recovery have on investment opportunities through the Alberta growth mandate?

Mr. MacMaster: Well, you know, since this program started, we've continued to evaluate opportunities, and we'll continue to do so. I think in the early going, given the types of investments we've talked about before, you know, in 2014 the first big downturn in energy provided us an opportunity to step in and provide primarily debt- and warrant-type capital to companies that were being squeezed out a little bit. The front end of this was driving that.

I would say that now that things have recovered a little bit, there are other opportunities that may evolve for us around the move from traditional energy to renewables. Alberta's involvement, for instance, in converting coal to gas-fired electricity plants is very interesting to us, and there could be opportunities. We're reviewing some of those right now. Obviously, pipelines are top of mind. We'll continue to review these, but I think it's very promising for us. Of course, as I always say to this committee when I'm here, you know, the 3 per cent mandate wasn't the beginning of our investment in Alberta. In fact, today we have roughly $9 billion, I believe, across the portfolio invested in Alberta, and the heritage fund would be $1.7 billion-ish.

Mr. Uebelein: It's $8 billion and $1.5 billion.

Mr. MacMaster: Yeah. So significant investment in Alberta beyond the 3 per cent, and as I always say, it's because Alberta has been traditionally such a great place to invest.

Loyola: Okay. It has been a great place to invest, eh? Wonderful to know.

In this upcoming fiscal year, do you anticipate exiting other investments, and if so, what is the reason behind exiting other investments in the Alberta growth mandate?

Mr. MacMaster: Well, it really varies. In the case of TransAlta Renewables, you know, we got in at a very attractive price. The company quickly recovered to beyond full valuation, as far as we're concerned, and we exited the position. It's since, you know, fallen back down. So that was an opportunistic investment that worked for both parties. Sometimes it's just all about valuation. If we can get something that we think is inexpensive and then sell it when it appears to be very expensive, that's a good trade for us and for the portfolio. Another example was, I believe, with Savanna, where it was kind of a hostile takeover situation. We would have liked to remain in that position, but shareholders voted against that. Those are two examples.

1:20

Mr. Uebelein: There's a third example. As you probably already know, some of the structure transactions that we put into the growth capital mandate include a debt component or a debt with warrants component. As we see these companies either recover or just their cost of capital go down because of the overall economic recovery in Alberta and in the oil patch, then their ability to prepay our investment – in other words, reimburse us – and find a lower cost of capital to continue their growth trajectory sometimes happens.

An example of that was Calfrac Well Services, where we made a combination of investments in them, including a debt component that did have a prepayment option, so they voluntarily gave us our money back with a very handsome return, and they continue to be growing.

Loyola: Okay. Perfect.

Mr. Chair, through you to the gentlemen, thank you very much for answering my questions.

The Chair: Thank you.

I'm going to ask if anyone on the phone has a question. Mr. McIver, Mrs. Schreiner?

Mr. McIver: I do if you don't mind.

The Chair: Yeah. Go ahead, please.

Mr. McIver: Okay. Thank you. A couple of questions. In your answer to Mr. Loyola about the TransAlta Renewables you talked about how the investment went up and then you sold it and it went down again. I guess congratulations on that and on the overall results. Can you talk about the factors that maybe caused that to go up and then what caused it to go down?

Mr. MacMaster: That's a good question. You know, I sometimes really don't understand the whims of the market. It would be cheeky for me to say, you know, more buyers than sellers, but it's hard to say, right? All we can do is analyze an investment opportunity and try and come up with a value for it.

In the case of TransAlta Renewables, when we purchased it, I think it was around $9 a unit. To us it appeared, you know, fairly cheap, and then it went up to $16. Today I think it's $11. Who knows? It's the whims of the market. There have been some ups and downs in the last couple of years for the energy sector. I just talked about it being up 14 per cent in the first fiscal quarter, and then it rolled over again. The sentiment around the sector, you know, continues to evolve and change, and I think TransAlta Renewables, to a certain extent, gets caught up in that.

Mr. McIver: Was TransAlta a beneficiary of the provincial government's subsidies on the renewables that they are in?

Mr. MacMaster: I'm not sure.

Mr. McIver: Okay. All right. I'll look that up another time.

Now, the Alberta growth mandate, of course, as I think Mr. Loyola said, is 3 per cent of the heritage fund into Alberta growth. You did answer some of the questions that I had. Thank you, Mr. Loyola, for asking those. As a general question on the growth mandate: when you hit $500 million, is the mandate completed, or is it the Finance minister's direction to reach $500 million and stay steady at that much invested in Alberta?

Mr. Epp: The mandate would be, if and when that $500-odd million is reached or 3 per cent is reached, to maintain that percentage. So if an asset was sold out of the portfolio, there would be room to purchase another one. The intention is to have that 3 per cent always invested. So it's not . . .

Mr. McIver: If I heard correctly – and I was trying to listen carefully – we were at $386 million, and I think you said you divested a couple, that there's $154 million outstanding, so by that number it's not really tough math, I guess. There should be another roughly $346 million to be invested. If that's correct, when do you think we might get to the $500 million level? Any estimates or any ideas?

Mr. MacMaster: I can't answer for sure. I think that if one of these larger infrastructure-like assets became available, it could be one or two transactions. It's really hard to say. As I say, we are looking at a few things, so it might not be long, but I can't promise. You know, we have to stick to our discipline.

Mr. McIver: All right. Has the government given you a timeline on when they want you to get to the $500 million mark?

Mr. MacMaster: No. I've not received a timeline. You know, as I have always said, this is driven by our mandate to achieve the highest risk-adjusted returns, first and foremost.

Mr. Uebelein: Yeah. We have not had . . .

Mr. McIver: So let me ask you: if we didn't have the growth mandate per se, how much do you expect that you probably would have already invested in Alberta anyways without the growth mandate?

Mr. Uebelein: That's also a difficult one to calculate. What I can tell you is that we would have still been looking for strong investment opportunities in Alberta. However, our allocation to those types of investments would have been lower, and therefore the implication is that in any one of those investments we might have made smaller investments than we were able to do because of this allocation. I can also tell you that in response to the allocation, Dale and his team increased the resources available to look at transactions. All of those things lead us to believe that without that allocation either fewer or less large investments would have been made, but it's imponderable for us to do a what-if analysis on a scenario that never existed.

Mr. McIver: All right. Fair enough. So you would have invested some in Alberta businesses anyways. It's just that we can't really say for sure whether it would be more or less, but I think you just suggested it's probably a little more because you had put more resources into it and had more capital available for that. That's a fair answer.

Now, through the growth mandate, any idea of how many jobs have been generated for Albertans as a result of the investments to date?

Mr. MacMaster: I have no idea. No.

Mr. McIver: Okay. Have the delays in the Trans Mountain pipeline – and we're all aware of those – had any effect on AIMCo's ability to find positive investment opportunities in Alberta?

Mr. MacMaster: Sorry. Could you rephrase the question? I don't think I quite got it.

Mr. McIver: Well, I'm saying that the fact that Trans Mountain pipeline has been delayed for so long, has the investment climate, as illustrated by Trans Mountain, made it harder for you to find positive investment opportunities in Alberta?

Mr. MacMaster: I think that's been part of the mosaic that's affected the investment landscape more broadly in Alberta, in combination with the challenges around, you know, TransCanada PipeLines, Keystone pipeline, Energy East, Gateway. I mean, this isn't the first pipeline to have challenges, so there's obviously a growing frustration in the energy sector that's having an impact on companies operating here. I think that's impacting the amount of foreign capital that's investing in the energy sector in Alberta. So it's all of that. It's all of that.

Mr. Uebelein: I think anything that adds to the uncertainty of the price that can be discovered or can be derived for oil that comes from Alberta has a potential dampening effect on the investment climate, particularly from outside investment. So we could view this . . .

Mr. McIver: Okay. Thank you.

Mr. Uebelein: . . . as an opportunity.

Mr. McIver: I'm sorry. I apologize. Carry on. Please don't stop.

Mr. Uebelein: No, no. That's all I had to say.

Mr. McIver: Okay.

The Chair: Thanks, Mr. McIver. I'm going to move on, and then we'll come back to you.

Mr. McIver: Now, I'm just sitting in on the committee, but just looking through the quarterly report . . .

The Chair: Mr. McIver.

Mr. McIver: Yes.

The Chair: I'm just going to move on to other people. We can come back to you, okay?

Mr. McIver: All right. I'll be here. Thank you.

The Chair: Thank you.
Mr. Kleinsteuber.

Mr. Kleinsteuber: Thank you, Chair. Yeah. Earlier, Mr. Uebelein, I think you mentioned, sir, some comments about growing trade protectionism, and I think everybody's been following along with some of the signals that they may have seen from the United States administration. So I'm wondering if you expect the fund to be impacted in any way from the outcome of some of the ongoing NAFTA negotiations or how some of our investments might have been exposed in that way.

1:30

Mr. Uebelein: I'll say something, and then I'll really defer to Dale. You know, the short answer is that, of course, anything that could have an impact on global trade and global economic growth is going to have an impact on our investment portfolio and on investment portfolios of anybody. It's our job to make sure that our diversification is strong enough that it doesn't have a material negative impact, so we're watching this very closely. It's a negotiation, in the purest sense, with some characters that wear as a badge of pride their ability to negotiate cleverly. We'll see how that all falls out, but we don't see any individual exposures that we think are necessarily critically at risk. Certainly, we hope this all works out in a positive way so that global trade can continue to move in the right direction.

Mr. MacMaster: Yeah. I don't have much to add. I mean, I think trade is a global, broader issue that overhangs the market to a certain extent. The longer it goes on, you know, probably the more impact it has, but it has an impact on investor confidence. Its impact on global growth is probably 40 or 50 basis points. So if we're expecting 3.9 per cent in global growth next year, if everything was enacted according to the statements that have been made to date, you're probably looking at 40 or 50 basis points off that in trade protectionism effects. I think my issue is just more the broader implications and the issues around investor confidence with that kind of a backdrop. But, as Kevin says, I mean, a lot of this is bravado and negotiation. Hopefully, we'll get over it soon and get on with it.

Mr. Uebelein: One of the things that we think about a lot is not just this element on its own but how it adds a broader sense of uncertainty to this other issue that both of us have talked about, which is interest rates generally rising. So these central bank governors – Poloz is certainly one of them – who have models on exactly how to increase interest rates and what impact that might have on the economy have this wild card variable, which makes their ability to model and predict exactly how the economy will respond to interest rates. It adds another layer of uncertainty to what is already an imperfect science at best. That's sort of an interesting multiplier effect on this risk or issue.

Mr. Kleinsteuber: Right. Well, thanks for that.
I was wondering, too – and this question is open, really, for anybody – what impact to the fund the recently levied tariffs on Canadian steel and aluminum might have had with some of the investments, or have we been exposed in that way?

Mr. MacMaster: Probably, but it's not a huge impact, and I believe, if I'm not mistaken, that the government has stepped in to offset some of that. Again, you know, the market is viewing these as short-term bumps in the road. They'll appeal it to the necessary bodies, as they've done in the past, and win that case, and then they'll be compensated, and on we go. That's where we are.

Mr. Kleinsteuber: All right. Thanks a lot.

The Chair: Mr. Ellis, you have a question.

Mr. Ellis: Thank you very much. Gentlemen or, I guess, maybe Mr. MacMaster here, you've talked a lot over the last year, maybe two years about Calfrac, and then you brought up Calfrac again. I know that you're still invested in Calfrac. I think you've mentioned that. We had obviously done some looking into it. Calfrac, of course, appreciated the injection of money that you gave them. Sadly, they had taken that money and gone to some other jurisdictions outside of Alberta in which to conduct their business. I know you don't get into the idiosyncrasies of these companies and the day-to-day operations. However, are you aware of Calfrac kind of maybe changing a little bit of their direction and doing a bit more business and investing themselves in Alberta?

Mr. MacMaster: Yeah. I mean, I'm not exactly sure what Calfrac's plan is. I think it would really be beneficial if the energy sector more generally had more clarity on what the rules are, for instance around getting pipelines approved and getting more investment in the energy patch, which I think has been stifled. There are a number of smaller companies which have left the industry. There was actually an article in the paper the other day about that. I'm not sure, but it seems to me that on a value basis, Alberta looks, you know, really cheap compared to other jurisdictions, but foreign capital and even local capital are a little hesitant to step forward and make necessary investment while the rules of the game are still up in the air, I think.

Mr. Ellis: Thank you.
If I could have just one follow-up?

The Chair: Yeah.

Mr. Ellis: I've had the good fortune, I guess, to consult with several energy leaders within Calgary, and of course they've mentioned that many red tape issues and policies are somewhat stymying their ability to do business, specifically in Alberta. However, they did indicate to me that they had spent a lot of time and money and effort in, specifically, the Houston area. Do you have any investments, from your perspective as the Alberta heritage savings trust fund, in some of the energy markets within the Houston area?

Mr. MacMaster: Without having specifics in front of me, given that the Houston energy sector would be part of the S&P 500 and the U.S. equity market, by virtue of our holdings in U.S. equities we would be exposed there.

Mr. Ellis: All right. Thank you.
Thank you, Chair.

The Chair: Thank you.
Mr. Horne.

Mr. Horne: Yeah. Thank you, Chair. Thank you all for taking time to meet with us once again. I'm sure, really, that everybody in the room has very busy schedules, and it's greatly appreciated that you're taking this time once again.
Just a few questions, but I'll certainly defer to the chair if we need a few other MLAs in there. I'm wondering if the level of risk exposure that the fund is subjected to has changed substantially in the past year.

Mr. MacMaster: Again, I don't have the exact risk metrics in front of me, but it's my opinion that the active risk that we take has not changed much in the past year and, for that matter, probably not total risk other than any asset mix changes that we've implemented.

Mr. Horne: Okay. Now on page 12, note 4, entitled Investment Risk Management, there's reference made to the financial risks that the fund is exposed to. What do you view to be the greatest risk to the fund at this time, and what is being done to mitigate that risk?

Mr. MacMaster: Well, probably the greatest risk to the fund is across the asset mix that is chosen for the long-term objectives of the fund. You know, Lowell spoke about those objectives at the beginning of the meeting. If you want to achieve those types of returns, it means that you need to take risk, and you take the risk by investing in things like equities, real estate, infrastructure, and even fixed income and corporate credit and so on. You take that risk knowingly in order to achieve the return. Your greatest risk, really, is your asset mix. You know, from time to time we'll go through the business cycle and for the most part you'll have positive returns, but there'll be times when they're negative. But over the long run you should get to your objective. I think the numbers we showed you today are giving us some evidence that we're on the right path. Your asset mix is really where your most risk is, but, you know, you do that intentionally for the objective, and that's all good.

I hope that answers your question.

Mr. Horne: Yes. Thank you.

The Chair: Thank you.

Mr. McIver, would you like to continue?

Mr. McIver: Thank you, Chair. I'm grateful for the opportunity.

Now, a couple of things here. I was listening to the other comments. I think it was whoever spoke after Mr. Epp. I think it might have been Mr. Uebelein who made comments that we might be at the end of the bull market. He talked about a bunch of indicators that would say that, not the least of which – I think he talked about this as one of the longest bull markets ever. He also said that one of the indicators that it might be ending is that there would be wage pressures up. I just wanted to ask: what effect would the increased wage pressures have on the ability to invest and get a good return?

1:40

Mr. MacMaster: Sure. Maybe I'll answer that one. For many years, you're probably aware, the central banks after the credit crisis were mostly concerned with deflation. This is why we had unprecedented levels of stimulus and buying assets to try and encourage a little bit of inflation. Well, I think they've succeeded. Headline numbers for inflation in Canada and the U.S. are around 3 per cent, core inflation is around 2 per cent, and wages recently have been closer to 2.9 per cent. Hey, that's great. We've got inflation going. Central banks are thinking, though, that you don't want too much inflation, so they start to take their foot off the gas, right? So they're removing the stimulus and hoping to normalize rates, which is really a sign of health for the markets. If we can get to more normal levels of interest rates, it's probably best for everybody.

What challenges does that leave for investors? Well, for one thing, fixed income is challenged because rates are so low. You know, we saw rates below zero, in fact, in some jurisdictions. With rates normalizing and bond rates at very low levels, it's going to be hard to achieve the returns that we did in the last number of years. That's just a given. That's one area.

The bigger risk is that this is a guessing game for the central banks and inflation goes up too quickly. They're behind. They have to raise rates more quickly, and, lo and behold, the stock market falls out of bed and you have a bit of a debacle. That's always a risk when central banks are raising interest rates, but we, like them, are hopeful that they can negotiate this transition at the end of the cycle.

The challenges for us on things like equities are that they are valued, so we're being very cautious. As I mentioned in my statements, the liquid assets are also fully priced. It's a time to be cautious, and should we get some kind of fallout, given that we're long-term investors and we have the capital to invest and the liquidity, then we'll be able to step in and buy attractive assets at decent prices.

Mr. McIver: Okay. All right. No, I was just wondering. You had me thinking about what the effect might be of a 30 per cent increase in the minimum wage in that mix.

One of the other things, in going through the report, that I was looking for – and I know you'll see it on some investment prospectuses for mutual funds – is a top 10 holdings list, you know, with the name of the assets, the equities, bonds, and such that the fund holds. Is that something that we've ever contemplated adding onto the heritage savings trust fund reporting?

Mr. Epp: Well, we provide that information on an annual basis but not on a quarterly basis.

Mr. McIver: Okay. That'll explain why I didn't see it in the quarterly report. Thank you very much for your answer.

Chair, those are my questions. I thank you folks that answered the questions very much.

The Chair: Great. Thank you.

Ms Luff.

Ms Luff: Thank you, Mr. Chair, and thank you, guys, for being here. I guess you've talked a little bit about how the global investment landscape has been shifting, like, that we're maybe coming to the end of the bull market. Also, you mentioned that there was sort of a narrowing in the group of equities that was making money still. I'm just wondering if you could comment on how that shift in the global market is impacting the future and the health of the fund.

Mr. MacMaster: Sure. When we were referring to the breadth narrowing – I'll just give you an example. If you look at the S&P 500, which is a leading U.S. equities benchmark, technology stocks now make up 27 per cent of that. There are six stocks that make up 17 per cent. Those are, you know, the stocks that you've all heard about, the FANG stocks: Facebook, Amazon, Google, et cetera. That group is up about 20 per cent year to date, not to June but to date. The median sector is only up 1 and a half per cent, right? So you have, you know, technology stocks up 20 per cent. That gives you an idea.

Those six stocks represent $4 trillion of market value, which is two times the size of the entire Canadian market. You get a sense of how it's becoming more concentrated and being led by a narrower group of favourite stocks of investors and leaving the rest behind. These are pretty typical sorts of things you see at this part of the business cycle. For us, it means that we, you know, can't necessarily jump onboard with the enthusiastic speculators. We have to maintain our discipline and continue to look for assets that are attractively priced for the returns they're going to deliver. That might mean that over short periods of time we underperform the benchmark, but that's the discipline that comes with investing.

Ms Luff: Cool. Since you bring up tech stocks, obviously we have a growing tech sector here in Alberta. You know, Edmonton has done a great job in the last little while of attracting tech companies to Alberta. I guess: what does that overall landscape mean for opportunities to invest in smaller tech companies within Alberta or otherwise?

Mr. MacMaster: Well, certainly, as part of the 3 per cent mandate, if we can find, you know, technology stocks or any private equity situation that can meet our standards, we're more than willing and have been looking. We would probably have exposure through our small-cap fund if they are listed already.

Ms Luff: Cool. Thanks.

Looking forward, you know, the current breakdown of assets in the fund is 18.6 per cent in interest-bearing securities, 43.1 per cent in equities, 37.3 per cent in inflation-sensitive, strategic, tactical, and currency investments. You mentioned earlier that the asset mix is sort of where the most risk is. So is the long-term plan to keep that ratio of investments fairly consistent, or do you review it regularly and see about mixing it up, depending on what the market is doing?

Mr. MacMaster: I'll maybe ask Lowell to address the strategic asset mix.

Mr. Epp: The strategic asset mix is long term. The target is 50 per cent in equities, 30 per cent in inflation-sensitive and alternative investments, and 20 per cent in fixed income. AIMCo has the authority to vary from those weights in the short term. That's the long-term objective.

I don't know if you have any comments on the shorter term variations.

Mr. MacMaster: Yeah. I might just add, from a tactical standpoint, you know, how we move the portfolio over shorter periods of time, where we're staying very close to the target weights for a couple of reasons. Number one, we don't have a lot of conviction, as you've probably been gathering from our conversations, around equities yet. Fixed income doesn't really offer a lot of return either. So we're kind of sitting, biding our time, waiting for something to shake out, and hopefully, if that happens, we'd be ready to pounce and maybe overweight equities if we saw a 10 or 15 per cent correction, which wouldn't surprise anyone over the next year.

Ms Luff: Sure. I just have one more if that's okay, Mr. Chair. I mean, the last one, then, is just: you know, do you have any plans in the near future to enter into some of the higher risk investment fields, which seem to be exciting right now? I know there's a lot of movement around cannabis, for instance, coming into legalization in October. Just wondering if there's anything in those sorts of areas that you've been looking at.

Mr. MacMaster: Well, you know, you may recall my comments about bitcoin a year or two ago.

Ms Luff: I'm new to the committee, so I do not recall those.

Mr. MacMaster: Yeah. Okay. Well, you can go back and read the transcripts.

Mr. Uebelein: A cure for insomnia.

Mr. MacMaster: Yeah. I mean, these are areas, you know, that can attract speculation, right? I'm sure there'll be a real cannabis industry at some point here, but as you can tell by the price movement in these equities, it does attract that speculative element, just like bitcoin did. We see some wild price movements, and if you do look at some of the equities there, there are issues around valuation. All these companies really don't have any earnings yet, so it's all about anticipation of what could be. There's lots of risk around that, for sure.

Ms Luff: Thank you.

Mr. Uebelein: I wanted to come back to one of your previous questions, if I may, very briefly.

Ms Luff: Yeah.

Mr. Uebelein: You talked about Alberta's strength in technology. So frequently and, honestly, almost all the time that we spend sitting here is to talk about the investment portfolio of the heritage fund. That's why we're here. So we don't have an opportunity to talk about the point of intersection that we have on strategic issues. In other words, how do we make AIMCo a better investor over the long run? There's a point of intersection, frankly, with some of the strengths that we see in Alberta and specifically here in Edmonton on technology.

1:50

We're in very rich conversations and indeed negotiations right now with some of these smaller artificial intelligence or machine learning organizations, companies, if you will, here in Edmonton to try to find partnering ways where we can become better investors either at the point of investing decisions or, just as likely, in the back or middle office on how we operationalize a $110 billion asset management company, just doing it smarter, either using data metrics or machine learning.

We're excited about that. It doesn't mean that we're necessarily investing in those companies, but we're partnering with them, and that makes them more successful, and we think it's going to make us better investors in the long run.

Ms Luff: Yeah. Very interesting. Thank you for adding that. I appreciate it.

Thanks, Mr. Chair.

The Chair: Thank you.

I have no one on the list right now. Are there any further questions? Mr. Horne, go ahead.

Mr. Horne: Yeah. Thank you, Chair. I'm just reflecting back to 2017 as I was on the committee at that time, and I recall you mentioning that 2017 was a bit of a unique year, where returns were higher. I'm just curious: after the first quarter of this year would you say that the current rate of return for 2018 is, I suppose, a bit more typical or as expected?

Mr. MacMaster: I would say that it's a challenging environment, and we're seeing that. You know, for your first fiscal quarter, 2 per cent was reasonable, but I think that by the time we get to year-end, we're going to see more challenges. So my cautionary remarks in 2017, I think, are in a way coming true. Certainly, for active managers like ourselves it's very challenging. With the narrowness of the market, active managers are having a more difficult time adding value, and the value area is underperforming growth, you know, technology. So this presents a challenging environment for us.

Mr. Uebelein: Last year we had a trifecta. It was almost the lowest ever interest rates, very buoyant equity markets, and virtually no volatility in those equity markets. We already know that interest rates have continued to rise through that period, so this year we do not have the same interest rate environment. Volatility has ticked up a bit but is still relatively low. So we're not experiencing the same sort of trifecta of positive events this year.

Mr. Horne: Yeah. I think that is to be expected and is something I've been noting in the papers. Thank you.

The Chair: Mr. Ellis.

Mr. Ellis: Thanks. Just a question here in regard to your strategic, tactical, and currency investments. I see on March 31, 2018, 192 I'm assuming million, and then it went on June 30, 2018, down to $175 million. Maybe you can just elaborate a little bit. I'm assuming this is investment in currency, and please correct me if I'm wrong. Is there a tactical way in which you make the decisions in regard to investing the money in currency in different countries; i.e., you know, the euro or in the United States, as examples?

Mr. MacMaster: Sure. I mean, you know, when it comes to currency, we act for 32 clients, including the heritage fund, and we manage currency exposures at the top of the house, and we don't typically take a lot of risk in currency. It has not traditionally been a very good place to add value. The fund is exposed to currency in the global equity portfolio, for instance, but it's a diversified basket, and that's a choice made by the asset managers. Most places in the portfolio foreign currency is hedged, so in fixed income, infrastructure, private equity, real estate, except for the foreign side, it is hedged.

Mr. Ellis: Thanks for elaborating on that.
Thanks, Chair.

The Chair: Good. Thank you.
Anyone on the phone with a question?

Mr. McIver: Just one quick one if you don't mind, Chair.

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

Mr. McIver: Thank you very much. In looking at page 6, the statement of cash flows, I was trying to listen carefully here, and I think I heard a reference at some point about, you know, maybe being at a bigger cash position when we expect the market may not go on with a bull market forever. It could be that I'm overreacting, but in looking at the cash investment in the bottom line on that page in the chart, our cash deposits in the consolidated cash investment trust fund have gone down from $170 million to $97 million. Is that an anomaly, or would we expect in the future, with the cautions that you've given us in this meeting, to see that cash position go up over the next short term in anticipation of what may or may not happen in the future?

Mr. MacMaster: Right. Well, maybe I'll tackle the tactical question, if you will. We don't typically hold a lot of cash because that's a drag on performance. When I talk about moving the portfolio around, if we saw a correction in equity markets, what typically happens is that equity prices go down and bond prices actually rally. So it's a nice diversifier in the portfolio. We would sell bonds and then buy equities if we felt it was the appropriate time. The amount of cash you see on these financial statements isn't that relevant to us managing the portfolio.

Mr. McIver: Right. Okay. And that's why it's a good thing that you're managing it and I'm not. Thank you for that answer. I appreciate it very much.
Thank you, Chair.

The Chair: Great. Thank you.
Okay. I'll do a last call for questions and look around. Seeing none, with that said, thank you so much for your presentation.
Would a member like to move that the committee receive the report? Okay. Member Loyola. Member Loyola moved that

> the Standing Committee on the Alberta Heritage Savings Trust Fund receive the 2018-2019 first-quarter report on the Alberta heritage savings trust fund.

All in favour? On the phone? Any opposed? I see none.

> That is carried.

The next item on the agenda today is about the 2018 public meeting. We have an update. As you know, members, under the Alberta Heritage Savings Trust Fund Act this committee is required to hold a public meeting informing Albertans of the status of the fund. At its June 20, 2018, meeting the committee agreed to hold this year's public meeting on October 25, 2018, here at the Edmonton Federal Building from 7 p.m. to 9 p.m.
At this time I'd like to call on the committee clerk to give a brief overview of the status of preparations for this meeting. Mr. Roth.

Mr. Roth: Thank you, Mr. Chair. I won't get into the weeds with this. I'll just give you sort of a high-level update as per the committee's direction with regard to the comms plan and the various other pieces. Sort of going off last year's great response to the public meeting, I think it was the biggest public meeting that the committee had seen in a number of years. The galleries were full. The overflow area had a number of people. So sort of working off last year, while it worked well, we're just making sure that there are sufficient resources in terms of LASS staff and committee services staff, and it looks like things are under way for that. The communications pieces are being prepared. The machine has been cranked up as per the committee's direction. If you have any questions, I can certainly do my best to answer.

The Chair: Thank you.
Any questions for Mr. Roth. No? Anyone on the phone?
Okay. Hearing none and seeing none, we'll move on to other business. Are there any items of other business? On the phone, other business?
Okay. Hearing none, the date of the next meeting will in fact be the public meeting, and it will be on October 25 unless a meeting is called by the chair prior to that date.
At this time I would like to call for a motion to adjourn. Ms Luff. Moved by Ms Luff that this meeting be adjourned. All in favour? On the phone? Any opposed? Seeing none, that motion is carried.
Thank you.

[The committee adjourned at 1:59 p.m]

Published under the Authority of the Speaker
of the Legislative Assembly of Alberta