



Legislative Assembly of Alberta

The 28th Legislature
First Session

Standing Committee
on the
Alberta Heritage Savings Trust Fund

Annual Public Meeting, Edmonton

Wednesday, October 2, 2013
7 p.m.

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The 28th Legislature
First Session**

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

Khan, Stephen, St. Albert (PC), Chair
Jablonski, Mary Anne, Red Deer-North (PC), Deputy Chair

Anderson, Rob, Airdrie (W)
Casey, Ron, Banff-Cochrane (PC)
Dorward, David C., Edmonton-Gold Bar (PC)
Eggen, David, Edmonton-Calder (ND)
Kubinec, Maureen, Barrhead-Morinville-Westlock (PC)
Sandhu, Peter, Edmonton-Manning (Ind)
Sherman, Dr. Raj, Edmonton-Meadowlark (AL)

Ministry of Treasury Board and Finance Participants

Rod Babineau	Manager, Portfolio Analysis, Capital Markets
Lowell Epp	Executive Director, Capital Markets

Alberta Investment Management Corporation Participants

Darren Baccus	Associate General Legal Counsel
Leo de Bever	Chief Executive Officer and Chief Investment Officer

Office of the Auditor General Participant

Merwan Saher	Auditor General
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**Standing Committee on the
Alberta Heritage Savings Trust Fund**

Public Participants

Ken Allred
Beth Bell
Randy Duguay
Ken Korchinski
Ron Lupton
Aden Murphy

7 p.m.

Wednesday, October 2, 2013

[Mr. Khan in the chair]

The Chair: Good evening. Welcome to the 2013 annual public meeting on the Alberta heritage savings trust fund. I'm Stephen Khan, MLA for St. Albert and chair of the standing committee on the fund. The \$16.8 billion Alberta heritage savings trust fund is a large part of a better Alberta for tomorrow. We're pleased to be here with you today to discuss what's new in 2013 and how the fund will provide a brighter future for our province.

I'd like to begin the meeting by introducing the rest of the panel. Let's start with the members of the standing committee. On my right we have Mrs. Mary Anne Jablonski, MLA for Red Deer-North, deputy chair. To her right we have Ron Casey, MLA for Banff-Cochrane, and to my left, Mr. Rob Anderson, MLA for Airdrie; to his left, Dr. Raj Sherman, MLA for Edmonton-Meadowlark; Mr. David Dorward, MLA for Edmonton-Gold Bar; Mr. David Eggen, MLA for Edmonton-Calder; Ms. Maureen Kubinec, MLA for Barrhead-Morinville-Westlock; and last but not least, Mr. Peter Sandhu, MLA for Edmonton-Manning.

At this time I'd also like to acknowledge some of our colleagues from the Assembly in the audience. We have Jacquie Fenske, MLA for Fort Saskatchewan-Vegreville, and Danielle Smith, MLA for Highwood. Thank you for joining us today.

We are the Standing Committee on the Alberta Heritage Savings Trust Fund, an all-party committee of the Legislative Assembly. In a nutshell, we review and approve the performance of the fund and report back to Albertans and the Legislative Assembly.

The President of Treasury Board and Minister of Finance is ultimately responsible for the fund and its investments. The department looks after setting the fund's long-term strategy, developing the funds, investment policies, and monitoring the performance of its investments. Joining us on stage from Alberta Treasury Board and Finance are Lowell Epp, executive director, capital markets, and Rod Babineau, manager of portfolio analysis, capital markets.

The Alberta Investment Management Corporation, also known as AIMCo, is responsible for making and managing investments in stocks and bonds and other investment instruments within the fund's portfolio. Joining us from AIMCo are Dr. Leo de Bever, chief executive officer, and Darren Baccus, associate general legal counsel.

I'm happy to remind you that tonight's meeting is being broadcast live on Shaw TV and webcast on the Legislative Assembly website at www.assembly.ab.ca. I'd like to encourage all those watching from home to join the conversation and to contribute to our discussions during the live broadcast through the online chat or Twitter under the hash tag shown on the bottom of your television screen. Simply submit your questions, and we'll do our best to respond to as many of the questions as time will allow during the question-and-answer segment of the meeting, which will immediately follow our presentations.

Now, we have a panel made up of experts, and we have a panel here made up of politicians. We promise to keep our answers brief, a daunting task for some of us politicians, I know. This will hopefully allow us to address as many of your questions and comments as possible. Your input is very important to us, and I encourage you to participate.

Please note that this meeting is being recorded by *Alberta Hansard*, and transcripts from this meeting will be available online and can be found on the Assembly website.

By the end of our meeting our objective is to have walked you through the history, mission, long-term performance, and future of the Alberta heritage savings trust fund. Let's start by updating you on what's new. Some of you may remember that just last year this committee sought Albertans' input on the future of the fund. We asked for direction from public stakeholders through our Dollars and Sense consultations held by the Alberta government.

As a direct result of the government's consultation the Fiscal Management Act was debated in Assembly and passed in the spring of 2013. The Fiscal Management Act renews Alberta's fiscal framework and creates the requirement for an operational plan, a savings plan, and a capital plan. Under the new savings plan over the next few years contributions will increase until, ultimately, 100 per cent of the income is retained within the savings fund by 2016-2017. So some very exciting changes are on the horizon, changes that will ensure the fund is relevant for our children and our grandchildren.

With that, let's begin the presentation.

[A video was shown from 7:05 p.m. to 7:12 p.m.]

The Chair: That was a terrific summary of the Alberta heritage savings trust fund, and it's always wonderful to get a little bit of historical context.

Now I'd like to invite Lowell Epp, executive director of capital markets at Alberta Treasury Board and Finance, to walk us through a financial update of the fund.

Mr. Epp: Thank you, Mr. Chair, and thank you for allowing me to present this information. As was mentioned in the video, the investment objective of the fund is to maximize long-term investment returns. To do this, the Department of Finance and the Minister of Finance have set up an investment policy that seeks to achieve a prudent balance between expected returns and risk. It has a long-term focus, it is globally diversified, and we attempt to minimize the cost of investing. The fund's manager, AIMCo, manages over \$70 billion in funds, and this gives them a cost advantage. Managing costs is one of the most important ways to ensure higher returns.

The investment policy of the heritage fund, which you can find online at the heritage fund's website, sets out the policy asset mix for the fund, which guides the investment management of the fund. The policy portfolio is an expression of the long-term objectives in a practical, implementable form. The target allocation for the fund is to have 50 per cent invested in equities globally. This will be broadly diversified by country and by industry as well as by company. Thirty per cent is to be invested in inflation-sensitive and alternative investments such as real estate and infrastructure, and again that has both a domestic and global component. Twenty per cent is invested in interest-bearing securities, or what we like to call fixed income. The investment manager is given latitude to apply expertise with changing market conditions. If AIMCo feels that certain asset classes will perform better, they have the ability to overweight or underweight certain asset classes.

The current asset allocation as of March 31, 2013, the end of the last fiscal year, had 53 per cent in equities, 27 per cent in inflation-sensitive and alternative investments, and 20 per cent in fixed income. The amount in inflation-sensitive and alternative investments is slightly below target, largely because it's still in an implementation phase.

Starting April 1, 2011, the heritage fund changed its allocation, the target asset mix, from 20 per cent to 30 per cent in this asset class. AIMCo has been filling that asset class with investments,

but instead of filling it rapidly, they are filling it cautiously and trying to maximize returns rather than simply buying investments at any price.

In the 2012-13 fiscal year the fund earned net investment income of \$1.32 billion. This was based on gross income of \$1.46 billion and management fees of \$148 million. Of the \$1.32 billion in investment income, \$1.15 billion of this income was transferred to the general revenue fund. The remaining \$161 million was retained within the fund for inflation-proofing purposes, as is set out in the heritage fund act.

All of the fund's major asset classes had positive returns during the year, with equities being the largest component of the portfolio. They also have the largest component of income, earning \$908 million in gross income. Inflation-sensitive and alternative investments earned \$302 million, and fixed income earned a gross income of \$254 million.

Since its inception the heritage fund has contributed almost \$35 billion to government programs and expenditures. You can see on the graph that since about 1981-82 most of the fund's income has been transferred to general revenues. These general revenues have helped pay for expenditures or keep taxes low or build capital projects.

Historically the fund has performed quite well. You can see the investment returns on the graph. Over the last four years we have achieved an average return of 11.9 per cent following the financial crisis here of 2008-09, where the fund lost 18 per cent. Overall, over the last five years the fund has earned an average return of 5.2 per cent. Over 10 years it's an average compound return of 8.1 per cent.

One of the goals of the fund is to earn a long-term real return of 4 and a half per cent, or, in other words, to earn 4 and a half per cent over inflation. Over the last five years it has not achieved this goal. Inflation has averaged 1.8 per cent over that time while the return on the fund is 5.2 per cent, or a 3.4 per cent real return. If you look at the last four years, however, and omit the financial crisis year, it has performed well in excess of the 4 and a half per cent real return target.

In terms of individual asset class performance 2012-13 was an exceptional year. Overall, equities had a return of 13.3 per cent during the year, inflation-sensitive and alternative investments had an overall return of 10.9 per cent, and fixed income had a return of 7.5 per cent.

Among subasset classes, which are shown on the chart, the strongest performance was in global equities, with a 14.8 per cent return. Real estate also had a strong performance of 13 and a half per cent. But what is important to note is that all the major sub-asset classes had positive returns, which makes it an exceptional year.

The strong performance of the fund was due to a combination of good market returns and strong value-added performance by AIMCo. The fund's benchmark investment return, or the return before adding investment management expertise, was 10.1 per cent during the year. In other words, AIMCo through its expertise in management added 1.5 per cent in value during the year.

That concludes my remarks. Thank you.

7:20

The Chair: Thank you, Mr. Epp, for that informative presentation.

I'll now call upon Dr. Leo de Bever, chief executive officer of AIMCo, to provide a market update.

Dr. de Bever: Good evening. As Lowell pointed out, we manage these as part of a \$70 billion portfolio. I don't know whether you realize the power of economies of scale in our business, but if you

were to manage this fund as a separate entity, the cost of doing it would probably be double just because of lack of economies of scale. Furthermore, what we've done in the past five years at AIMCo is bring a lot more expertise to Alberta to do it here rather than farm it out to somebody else. The power of that is enormous as well because, to the extent that we can bring the expertise to do various tasks to Alberta, the cost of doing it is about a third or a quarter of what we would have to pay an external manager.

I entitled my presentation Great Economic Potential, Poor Execution, Mediocre Asset Returns. The first thing is a very optimistic idea; the second and third are not so much so. I want to put this in perspective. Lowell was saying that the target is CPI plus 4 and a quarter or whatever it is. I can't produce that out of thin cloth or old cloth. My team can only produce the return that the markets will give us on the asset mix that the department sets for us plus whatever we do by being a little bit more clever than the market. Last year that was a billion and a half. On \$17 billion, that's not an insignificant amount.

What I see going forward is great economic potential, but the frustration is that for a variety of reasons economies around the world don't seem to be able to execute on that potential very well simply because of the process by which we make decisions. As a result, I think returns going forward aren't likely to be anywhere near what they were in the '90s, which was extraordinary even in the last hundred years. When I look at that, I say: can we imagine a better future than what these numbers would indicate? Of course, by ourselves for \$70 billion we can't do that, but what we're trying to do at AIMCo is not try to solve the problems of the whole world but just to solve the problems of our little piece of it.

Now, the notion was that this fund is being invested globally. We have 8 per cent of our assets in Alberta. Some people think that's too much; some people think it's too little. The general idea on our asset mix is that we are global investors, and we're trying to diversify the risk away from the oil and gas exposure that the province has in its asset base.

Now, when we look at the global economy after 2008, it has recovered very, very slowly by historical standards. In North America we've done relatively well, meaning that compared to, say, Europe or Japan or a number of other jurisdictions our growth has done better, 2 to 3 per cent. Within that piece Alberta has done relatively well because of the strength until very recently in commodity prices.

I would like to put out there – it's not my main purpose in life to elaborate on this – that the Alberta advantage in the resource base we have is not automatic. There's a price component to it. If prices go lower, the advantage disappears. We can reverse that by making the economy more productive. There's a tendency – I'm Dutch by background, so I can say this – for resource economies to develop something called Dutch disease, meaning that you take your resources for granted, and as a result you don't get the benefit from them that you should be expected to get.

The other point that I'm trying to make in this presentation is that, going forward, bond returns are going to be very poor, and if I could afford to take a 10- or 20-year horizon, I'd rather be in stocks than in bonds.

The final, uplifting part, which is also part of the title, was that we see an unprecedented pace of innovation, and one of the challenges that our economy faces is dealing with the technological changes that result from that or from the changes in our economic structure that result from that.

On the next slide, when we look at global growth and look at it in more granular detail, the big thing that's happened in the last 10 years is right in the energy sector. The U.S. having a much bigger energy potential because of fracking, for instance, is making that

economy much more cost-competitive internationally than it used to be. But, again, I told you about some of the things that are holding back decision-making. The U.S. government right now has shut down because the democratic policy or decision-making process has not produced a reasonable outcome.

Canada is being hurt right now, after some years where we felt pretty good about ourselves, by weaker commodity prices. Again, in Europe you have this problem that we all are going to face. The demographics and the misguided promises that were probably made in the '50s and '60s on both the health care and the pension fronts are coming home to roost. It's very difficult to find a long-term fiscal balance without killing the economy in the short run.

Then we have China. Everybody talks about how China was such a rapidly growing economy. It's now slowing down. That happens all the time. It happened with Japan; it happened with Korea. But the Chinese now have a challenge. Their challenge is to move their economy away from just building all sorts of big megaprojects at the state level to a more granular investment policy in things that ordinary consumers in China want to buy. Of course, Japan is trying to recover from 20 years of very, very weak economic growth. The slowdown in the rest of the world has hurt a lot of the smaller emerging markets, which are now, from an economic point of view or an equity point of view, priced so low that they actually present good opportunities for us.

When you look at inflation across the world, it sort of shows the same pattern in very different economies. After relatively strong inflation up to 2008 or so, it dropped dramatically after the 2008 crisis and really is sitting at around 2 per cent, 1 per cent, depending on the economy that you're talking about. Inflation is not an immediate risk, but it may become a risk once all that money that central banks have put into the economy starts to work.

When you look across the world and you look at how growth has proceeded over the last 50 years, when you look at economic growth, it's basically driven by three components. One is the labour force growth, and you can see that the dark component in this slide is starting to taper down. In other words, the growth in the labour force globally is weaker than it was even 20 years ago.

Then the next piece that determines how much the economy grows in aggregate is how much capital you can add per person that's employed and how much productivity you can inject into the economy. Frankly, the weak spot, particularly in our economy and in the U.S. economy, has been that productivity component, and if there's anything that could improve the outlook for the economy as a whole, it would be a better use of new technology to drive productivity.

When you look at the next slide, on U.S. GDP, and where the increase in GDP is coming from – I picked the U.S. because the numbers are more readily available, but a similar pattern would apply to our economy – energy in itself, which of course in Alberta is very important, is going to be a big driver for economic growth in the U.S. and in Canada as well. Globalization, which sometimes is seen as a bit of a problem from the standpoint in particular of displacing employment, will actually in the next decade add considerably to economic growth.

The buzzword "big data" may not be familiar to you, but what it really refers to is that one part of technological change in our economy where we're getting better and better at looking at data in sort of a macro sense, in an economic sense, and making things like logistics, how we move things around in the economy, much more productive.

The last two columns are interesting, particularly when you look at what the yellow indicates. Going forward, those components are going to drive the economy more than they did in the past. One of the problems: infrastructure. We're not building

enough infrastructure. We should have been building infrastructure after 2008, while the economy was down, and as a result we don't have enough sewers, we don't have enough water systems, we don't have enough roads, we don't have enough energy plants. That's going to eventually catch up with us, and I think that at some point those things have to be built.

7:30

The final one, the talent column, is interesting. The successful economies are going to drive their economy on the skills of their people, and that's always been the case, but there are more and more people that are going to be able to apply their skills to more and more new technology.

That's the main thing on the next slide that I would like to bring out. This is really important. If there's one thing you remember from this presentation, it's this: never in human history have so many people with so much education had access to the store of human knowledge at such a low cost. Now, why is that important? When Newton was in his prime, he said that he stood on the shoulders of giants, and what he meant by that was that all that he did was essentially built on what people before him did. But because information is so much more accessible now and so many more people are looking at it, the range of new ideas is going to accelerate going forward, and it's going to mean that technological change is going to accelerate. There's no question in my mind about that.

The next slide is a slide that people often bring forward when they say: well, okay, that's interesting, but do we have the right structure in place to take advantage of that technology? One measure is the amount that venture capital represents in terms of GDP. What I'd like you to take away from this is: yeah, okay, this is one way – and there are certain economies, like Israel and the U.K., that are taking good advantage of this particular vehicle – but it's not the only way and not the prime way that innovation gets financed. For instance, Japan, according to this, is really a failure in the financing of new ventures with venture capital investments, but that's because the way they do it is more through an angel structure – families and friends – and that's true for Canada and the U.S. to a large extent as well.

The other thing you have to know – and people don't like to hear this – is that a lot of inventions that are now relevant started out with government support. In a province like Alberta that's not always a popular thing to say. For instance, Google started with a \$500,000 grant from the NSF about improving the library system in the United States, and fracking was a technology that came out of something funded by the U.S. government.

So in these early stages of innovation historically there has always been government involvement. In a country like Israel, which looks very impressive on this chart, a lot of it is defence driven. Even in the U.S. – in the U.S. there was a recent announcement that desalination was improving at a rapid rate thanks to an invention by Lockheed. Well, why would Lockheed be involved in desalination? Because they service aircraft carriers that don't want to haul around diesel to desalinate water.

Now, when you look at the macro themes that we're pursuing at AIMCo, they look suspiciously Alberta based, but it just so happens that the world is focused on things that matter to Alberta. First of all, I mean, everybody talks about energy in this province. Yes, energy is at the base of almost any technological innovation in the world or in history. The last big one was in 1900, when we went to electricity and gasoline and so on to drive certain economic processes. This is happening again.

There are all sorts of new alternatives and better ways of using energy, saving energy, that are driving our economy, but we have

other resources in this province. Food and forestry are a good example. Food is very closely related to the availability of water, so Alberta's ability to exploit food technology will depend to a large extent on its ability to control the water supply in the economy because you can think of wheat exports, for instance, as a substitute for water or water exports.

Thirdly, materials: we produce a lot of mining materials and metals in this province, and again they're feeding into the Asian growth, a need for those materials.

The last one, technology, we've added over the last couple of years because we realize that one of the issues in Alberta is that we probably have moved all the welders from Ontario to Alberta that we can, so now it's a matter of making the welders we have more productive, and for that you need new technology. The interesting thing about technology is that a few centuries ago, in the first Industrial Revolution, it was basically a matter of replacing muscle power. A lot of the changes that are happening now are replacing brainpower. When you go to the oil sands or you go to Grande Prairie and look at horizontal drilling, you see that technology is a huge component of how these things operate now compared to the way they were operating 10 years ago.

On the next slide I'm showing you why I'm not impressed with bonds or, to flip it around, why if Alberta wants to raise capital, it's probably not a bad time to do it. Interest rates, after rising from 1950 to 1980 to a peak of 18 or 19 per cent – I don't know whether you remember that in the early '80s you could still renew your mortgage at 21 per cent. Those times are long gone. We're now back to historically low interest rates. The problem with that from the standpoint of holding bonds is that going forward, there are only two scenarios in bonds: one is terrible, and the other one is really terrible. The terrible one is just low returns, like 2 per cent, 2 and a half per cent. The really terrible one is that interest rates go up, and the bonds you own are worth less because the new bonds that are out in the market earn a higher coupon, a higher rate of interest.

That's why on the next slide I show you why we feel that being in equities is probably a better place for us to manage the money in the heritage fund. This is showing the equity premium, meaning the incremental return over cash – but cash is right now earning next to nothing, right? – that you can get out of equity markets. Now, the problem with equities is that they're very volatile, as we saw in 2008. Again, if you're able to look through that volatility – and the heritage fund can because we don't need the money next year or five years or 10 years from now; we need it at some point in the distant future – when you can do that, you can pick up that equity premium pretty consistently.

I'd like to leave it there. I'm ready for your questions.

The Chair: Thank you so much, Dr. de Bever. Thank you to AIMCo. Thank you to the Alberta Treasury Board for all the work that you do, gentlemen.

Standing on the shoulders of giants, indeed. I think all of us in this room should feel blessed to be tackling the issues that we are today, dealing with a \$16.8 billion dollar fund, which is the envy of many, many jurisdictions around the world.

That concludes our formal presentations. Before I open the floor to questions, I'd like to remind our viewers at home to join our conversation and submit questions to the committee online by logging onto the Assembly website at www.assembly.ab.ca. For your convenience we will accept questions through the online chat as well as through Twitter. Again, your comments are important to us, and we will attempt to answer as many questions as we possibly can during this meeting.

I'll now open the floor to questions from the in-house audience. We have microphones on either side of the stage. When you come up to ask questions to be answered, please state your name for the record before you begin asking your questions.

While we have folks in the audience formulating their many questions, we do have a couple of questions online. I'll turn the floor over to our deputy chair, Mary Anne Jablonski. Mary Anne.

Mrs. Jablonski: Thank you, Chair. From Adam Knisely: "Do the committee members acknowledge that we would be in a better position to deal with disasters like the southern Alberta flood in June if we invested more in and withdrew less from the fund?"

The Chair: We have a couple of folks who'd like to speak to that issue. Mr. Eggen.

Mr. Eggen: Well, thank you. I think that is a question on many Albertans' minds. The essence and the reason that the Alberta heritage trust fund was created in the first place was because we were having so much more royalty coming into the economy. It's to capture those royalties and to have it as a rainy-day fund and to have it as well as a fund that we disburse for diversifying our economy. Because we're not collecting the resource royalties properly in this province anymore – the rates have gone down so radically – that's why the heritage trust fund is static. While we could have used that as a contingency fund during the emergency this summer, instead the heritage fund is static and flat.

The Chair: Rob Anderson would like to take a run at this question.

7:40

Mr. Anderson: Sure. I think it's a very good question from Adam. You know, one interesting fact is – and it goes to some of the policy changes that have recently taken place in the heritage fund, which are actually very positive. If we had just left the interest in the heritage fund, the annual interest earned in the heritage fund from 1986 till present, the heritage fund today would likely be worth somewhere in the neighbourhood of about \$150 billion. Assuming we're getting 7 per cent return on investment, which as we saw from the presentation would be a reasonable amount, that would be well over \$10 billion a year in investment income, which is more than what we receive in oil and gas returns on an annual basis. So we would have that money. Not only would we not be reliant on oil and gas revenues any more, we would be able to weather the storm when these emergencies come.

One of the positive things that I think we've seen over the last year or so is a recognition, a start of a recognition, that it was probably a mistake not to invest that, leave the interest in the fund alone over time. That's why some of the changes that have been made recently include by 2016, if I'm not mistaken, leaving the interest generated each year by the fund in the fund to grow and compound with interest so that hopefully 25 years from now we're not in the same position that we find ourselves in today.

The Chair: Mr. Anderson, of course, speaks to the Fiscal Management Act, which was legislation that was passed this past spring, debated in the House. As Mr. Anderson noted, starting in 2015, over the course of three years the government is committed to ensuring that there's a sliding scale on the rate of our revenues that we're going to be keeping up until at three years prorated we'll be keeping 100 per cent of that interest.

We've got a couple more speakers to this issue. Dr. Sherman would like to comment, take a crack at this one as well.

Dr. Sherman: Thank you, Mr. Chair. Adam, you have asked a very good question. When the trust fund was developed, the mission was to save nonrenewable resource revenue and then grow that revenue. The idea was to pay for government programs like health care and education through taxation dollars, not tie the education, health care, and social services to the price of a barrel of oil or the price of gas.

A couple of things that we need to do as provincial legislators – and this is beyond the purview of this committee – is to really address the revenue side of the equation. As every expert in the economic summit and the Conference Board of Canada said, we have a revenue problem. Alberta must look at taxation to pay for health care and education. Alberta total personal and corporate income tax alone only raises about \$14 billion, and that doesn't even pay for one year of health care, which is about \$17 billion.

Not only do we have to address paying for public programs through taxation, we also can't be picking up debt. Right now we're actually picking up debt to put some money away in the savings account, and these are issues that we have to look at beyond this committee.

I agree with the principles of the fund. It would be great to put a lot more money away, but we do have to address the revenue side of our equation as well.

The Chair: I think Dr. Sherman hit the nail on the head when he did say that a lot of those sentiments and concerns are beyond the purview of this committee. Just a reminder to everybody that our committee is a committee that reviews and approves and reports on the Alberta heritage savings trust fund. Although there are a lot of fascinating issues we're going to be talking about, we're going to try to stick to what's relevant for this committee and what this meeting is about.

Mr. Casey: I think that just speaking to the use of the fund for floods, the fund was never intended to be a rainy-day fund. It was never intended to be something you simply tapped into this year, next year, or next week because you had a crisis on your hands. You're meant to deal with crises and special circumstances in the day that those were occurring.

The heritage trust fund is about future generations. It's about when nonrenewable resource revenues are depleted or slow down to a point where the province really needs additional revenue. That's really what the fund is for. As we build it with the new fiscal management plan, those funds will be there for future generations. But this is a fund for future generations. This isn't a fund to be used as a piggy bank that you throw on the floor and smash every time you need a few extra cents to do something with. This is a fund for grandchildren, your great-grandchildren, and their children.

The Chair: Thank you, Mr. Casey. That is interesting. I believe even Peter Lougheed used the phrase "savings for a rainy day." Again, that "savings for a rainy day" is in the context of: back in 1976 I think they thought of when the oil and gas runs out. Where we are now, we know that it's more likely that the world will move on to some sort of alternative energy supply. As Mr. Casey has said, that rainy day scenario isn't a rainy day such as the – oh, that was a bad pun, wasn't it? – disaster that we had in southern Alberta.

We'll let Maureen Kubinec have the last word on this.

Ms Kubinec: Thank you. That was a good question, Adam.

I'd wanted to talk just briefly, though, about some of the things that go along with the Alberta heritage trust fund. There are other parts of it that a lot of people maybe aren't aware of, and those are the Foundation for Medical Research and the scholarship fund, which are important components of it. It's amazing how those have grown. In 1981 the Foundation for Medical Research started out with \$300 million in it. Eight hundred and fifty million dollars has been directed to scientific communities, and the forecast for that for this year is \$1.28 billion. That's an example of some of the other things that fall under the purview of AIMCo that they do such a good job managing.

The Chair: Thank you, MLA Kubinec.

We do see some people walking to the microphones. We'll take a question from the floor.

Mr. Duguay: Hi. My name is Randy Duguay. I'm from St. Albert. I really keyed in a bit on the discussion from Dr. Leo de Bever around the points of innovation and how governments can look at programs to stimulate productivity and new areas for the economy. When I think about the idea of the heritage fund, there has been this long-standing idea that it is there for the long term, thinking about our children's children. I wonder about using a portion for today's children and starting to think about how we redirect our economy and actually look at that investment, similar to the notes here from Maureen Kubinec. I really would like to see us starting to track more, not just on the health fund but also looking at other areas that we can be successful at, going beyond having a national energy strategy and also having a national innovation strategy. I'd like some comments on that.

The Chair: Thank you, again. I think a part of this public engagement process is also a little bit of an education piece. I'd just like to reiterate a couple of the points that Maureen made that I think are very pertinent to Mr. Duguay's question. In 1981 \$300 million was transferred from the heritage savings trust fund into the Alberta Heritage Foundation for Medical Research. This has been a terrific fund in terms of developing medical innovative research here in Alberta. The fact is that through some of the work through Treasury Board and AIMCo this fund, which started with that initial \$300 million investment, is now estimated to be worth almost \$1.28 billion. Of course, as Maureen mentioned, the Alberta heritage scholarship fund is for our high school children who are graduating from high school and high achieving. These are terrific opportunities that we have.

I think Mr. Anderson said it last year at this meeting. You know, we have special opportunities here in Alberta where we may be able to create more of these funds and offshoots. That's what these types of meetings are about. It's about engaging Albertans and seeking some input and direction as to what you want done with your savings fund.

Anybody else care to comment on that last question?

Dr. Sherman: Randy, you have a very good question. In fact, investing in any innovation and technology and research and development is absolutely essential. It is what has made Alberta a world energy leader. This is why one of the major issues for us as legislators is that education spending in Alberta since 2008 has essentially been flatlined despite population growth and inflation.

7:50

Recently we just had an about \$147 million cut at the university level, some of the biggest, most drastic cuts in decades. For our economy to improve, we actually need to invest in education

today, from K to 12 and postsecondaries, especially in the University of Alberta and the University of Calgary, because we have some world-leading cutting-edge research that the public must invest in. As Dr. de Bever just said, when the public actually invests dollars in research and postsecondary education, you don't know what kind of inventions are going to happen. So, absolutely, we support massive investment, and it would be great to see a fund dedicated to protecting sustainable, predictable funding for postsecondary education.

The Chair: Thank you, Dr. Sherman.

I believe David Dorward has perhaps the last comment on this question.

Mr. Dorward: Yeah. Just a brief comment. The President of the Treasury Board and the Minister of Finance, the hon. Doug Horner, is certainly aware of the discussion and welcomes conversation on this. Any time I've talked to him about that, he certainly welcomes that conversation and I believe has some plans to go out and ask those kinds of questions to Albertans and bring up the issue of what Albertans would like to have the fund invested in today that doesn't take away the nature of the fund itself, the capital, but maybe adds to the strength of it. I also wondered if Dr. de Bever had any comments on how the fund today does those kinds of things in the province now.

Dr. de Bever: Well, if you can deploy the capital in the fund in enterprises that are both productive and innovative, then you kill two birds with one stone, right? Doing that is easier said than done. Most people think that the lack of successful startups is a function only of money, but it isn't. It's a function of money and skills in managing a process or a business. Most innovators are terrible business people. Out of 10 companies that start up, eight die before they get to anything sizable. So I've been trying to figure out how we can do more of that, but it's not easy.

The federal government has been looking at the same issue, and throwing more money at it is not the most efficient way. You have to have a really well-thought-out process by which you look at which early startups have the highest potential of being successful, and then you fund it. If you do it successfully, then the heritage fund makes money on it. It's not taking money out of the heritage fund and then not getting anything back. The ideal thing is that you deploy the money, make a return on it, and the fund keeps growing. That is, frankly, a nut that we're trying to crack at AIMCo in our new strategic vision. Because of the emphasis on technology we think we should do more there, but doing it effectively is easier said than done. Everybody in the world is wrestling with this, and we are, too.

Mr. Dorward: Just to finish that off, I think that included in that discussion could be not the micro basis of exactly which group would get some funding to be able to do what they think they can do but also looking at the more global perspectives of, "How can Alberta establish itself so that we're ready for the kinds of innovation that could come in the next while? Are there structures that we could help to stimulate where entrepreneurs could come and do things?" so the more global, macro-based kind of discussions and issues.

Thank you, Mr. Chair.

The Chair: Thank you, Mr. Dorward. Before we move on to the next round of questions, I would regret it if I didn't mention also the access to the future fund, which is a spinoff, if you will, of the Alberta heritage savings trust fund, which is a fund that is directly allocated and administered by the Ministry of Enterprise and

Advanced Education for some of the types of initiatives that we've been talking about here.

We've got a little bit of a lineup on the floor. We'll call that a lineup. Before that we're going to go to an online question, please.

Mrs. Jablonski: Mr. Chair, the next question reminds me of a sign that I saw last year when I was at the Grand Canyon and we were at a Grand Canyon restaurant. The sign said: free beer tomorrow. So the Twitter question is on how we define tomorrow when we say saving for tomorrow.

The Chair: That is a fascinating question. We have a couple of folks who'd like to take a run at that. We'll start with David Dorward.

Mr. Dorward: Well, I've discussed this sitting at home on my couch with my wife, and I've read back to the days of the start of the fund. I just wanted to mention that we have all seen a catastrophic change in gas royalty revenues in the province of Alberta as the rest of the world has found gas, so we earn much less in Alberta from royalties from gas than we used to. So you might say that with respect to a rainy day in the area of the gas revenues certainly we have seen a big fall-off in that area.

I always go back to the day when the nonrenewable resource is gone or it's not there, and for me that is a long time. I've asked experts, and you get different answers from different people, but it is estimated to be a very, very long time. Personally, I feel that mankind will solve the nonrenewable resource dilemmas prior to us actually running out. I think it will be that long. When you look at what mankind's done in the last 60 or 70 or 80 years, there's been incredible movement, and that should continue to happen. For me, the heritage trust fund is there for the day when the rest of the nonrenewable resource goes away like we had a hint of in the sense of the gas going away.

The Chair: Thank you, Mr. Dorward.

Mr. Anderson: Another good question online. I don't think that tomorrow is defined as a date on the calendar when we're discussing this. I think tomorrow is defined as a goal, as a milestone, and that milestone I think Premier Lougheed pretty much summed up perfectly. It's the day when we can no longer rely on nonrenewable resources for our revenues or for a huge part of our revenues. For example, over the last few years we've taken in roughly anywhere in the area of about \$7 billion to \$8 billion per year in nonrenewable resource revenues.

For me and, I think, for a lot of Albertans, we need to be striving towards a heritage fund where the amount of the fund, the amount of interest generated off the fund each year, can one day replace that \$7 billion to \$8 billion to \$9 billion, whatever it is. I agree with Mr. Dorward. Oil is not going to be running out first. What's going to happen is that the need for oil is going to decrease. Therefore, the price will come down, and therefore our oil being as difficult to get out of the ground as it is, it'll become somewhat uneconomical for us to do so. That's the 20- or 30-year thing that might happen here.

If we spend the next 20 or 30 years making sure we put enough away – not necessarily all of it, because we want to invest some of it, obviously, in education and these endowment programs that we've talked about – that in 20, 30 years, when we don't have those revenues coming in anymore, we don't have to slash and gut our social programs, our health care, our education, we'll still be able to pay for those things and keep our children and our grandchildren here in Alberta instead of seeing them move somewhere else for better opportunities.

The Chair: Thank you, Mr. Anderson.

I believe that from our panel of experts here Dr. de Bever would like to take a crack at this one as well.

Dr. de Bever: Okay. There are two aspects of the question the way it was treated. One is: which tomorrow are we dealing with? I was trained as an economist, and I think that what I would like to do, given that the resource revenue base is so unstable, if we could get the endowment trust fund up to the point where you can run it like an endowment – I don't know how well you know how charities or, say, philanthropic endowments are run. They basically take a percentage of the capital every year, so you have a fairly stable outflow, and that will allow you to replace over time some revenue source that you no longer have. That would be more disciplined than, say, letting all the fluctuations in resource prices show up in a fiscal plan.

8:00

The issue around when tomorrow is – in other words, when is that time when we're running out of resources? – I would approach a little differently. I think there's probably a lot more energy in Alberta than we think there is, but if we cannot exploit it at prices that are consistent with the future that we're likely to face, then it isn't going to do us any good. That means that you have to have a much better technology to take it out.

I would agree that the danger of commodity prices falling is probably pretty high because if you look at a long-time series of commodity prices, despite the fact that they're nonrenewable, their real price has been dropping. There's only been one exception, and that is wood. Wood has held its real value for the last 130 years, but grain was selling for \$6 or \$7 a bushel in 1895. Resources, whether it's food resources or metals or energy, their long-term trend with the interruption of OPEC – and OPEC, too, and a few other things have been down. So as a province that has those resources, you have to get better and better at exploiting them to be able to get the revenue benefit that the heritage fund is banking on.

The Chair: Thank you very much, Dr. de Bever. Fascinating. Wood.

We've got David Eggen and then Dr. Sherman. They've promised to be very, very brief. We do have a question from the floor, and we've got a backlog of questions now online that we'd like to get to.

David Eggen, please.

Mr. Eggen: Sure. Just very, very briefly, this idea of tomorrow, I think, is very important for the heritage fund. We need to make the fund robust enough so that we can use it in a number of different ways in the future. So it's not just being saved for two generations hence, but once it has built enough equity, we can use it tomorrow, literally. We really do need to start putting that money into it tomorrow, literally. As Dr. de Bever mentioned, that commodity price that we're enjoying now for oil is not necessarily something we can count on in the future.

The Chair: Thank you, Mr. Eggen.
Dr. Sherman.

Dr. Sherman: Thank you, Mr. Chair. How do we define tomorrow? Tomorrow will be defined by what happens in the lives of our children today. Have we used our social licence to develop our resources in a responsible manner? Tomorrow will be defined by: do we have a strong economy and a strong society?

Thank you so much for that question.

The Chair: Thank you, Dr. Sherman.

We're going to return to the floor for a question from our audience. Do more folks have questions? If some of this conversation stimulates questions, please feel free to come to the mike.

Your name, sir?

Mr. Murphy: Aden Murphy. Question for the MLAs or the expert panel, whoever wants to address it. It kind of goes off of Dr. de Bever's comments on wood staying even. Part of the asset mix of the trust fund is timberlands. It's been the only thing, I think, that's underperforming your benchmarks. Is there any particular reason why it's still part of the fund? Are you expecting it to pick up in the future significantly?

The Chair: Thank you for that question. Dr. de Bever did say "wood," so it's an appropriate question for Dr. de Bever.

Dr. de Bever: All right. Our major investments in timberland were a long-term investment. It's actually located in Australia. We bought 1,500 square kilometres of forestland out of bankruptcy. We looked at this and said: man, it's going to take us five or 10 years to sort this out, but if we're buying it at such a low price, eventually we're going to make that return. This is the problem with the way people look at the returns on the heritage fund. You shouldn't be looking at it on a quarterly or an annual basis; you should be looking at it on five or 10 or 15 years.

I've said this before: we're long-term investors, but some of my critics are only long-term investors as long as it makes money in the short run, and that doesn't work for a long-term policy. You have to stick to course, you have to set the strategy, and you have to know why you're doing what you're doing. If you buy low, eventually you're going to make the return, but you're going to have to be patient in getting that return. It doesn't always happen tomorrow. In fact, that's probably the biggest problem we face. The world is becoming increasingly short term. People like me but running public companies are increasingly under pressure to show results tomorrow and the day after. A lot of processes that good companies have to run take a long time to come to fruition.

We have to be very patient with the returns on this fund. That's not an excuse for underperformance. It's just the reality of life that if you want superior returns, it's usually because somebody else doesn't have the patience to wait for them. But if you are, then it's a benefit to the fund.

The Chair: Thank you for that question.

As our audience thinks hard about some more questions to ask, I think we're going to go to an online question.

Mrs. Jablonski: We have a Twitter question from @noleftandright. To what extent can you compare or contrast the heritage savings trust fund to other jurisdictions like Norway and with what cautions on comparing?

The Chair: The Norway question. David Eggen will be first up to bat for that one.

Mr. Eggen: Well, there are some differences. Certainly, with Norway and other sovereign funds around the world, you know, with national governments we have to make some distinction. However, I think it's worthy to note that many other national and state or provincial jurisdictions were inspired by the Alberta heritage fund concept back in 1976. So while we steered away and did not put the money into those funds, others did to the point where there's a rating now from last year showing the top 20

sovereign funds around the world, and Alberta's does not even rate in any of those.

So it's not just Norway. There are more than 20 other sovereign funds around the world that put that money in properly and are realizing the investment opportunities from that. For example, the Norwegian funds or the Kazakhstan funds are so large that they just use the interest. They use it as a hedge and a deferment against the vagaries of their own internal economy.

We, I think, started something really good, and we failed to keep investing in it over these last 30 years. Now is the chance for us to start doing that again.

The Chair: I know for a fact that this is one of my colleague David Dorward's favourite subjects.

Mr. Dorward: Well, I agree with what you said there. You know, the Norway fund is there, and it'll help the people of Norway in the future to be sure, but there are a lot of differences. Norway is a sovereign nation, and Alberta is not. Alberta over the years has sent over funding to other provinces in what are called equalization payments, and Norway doesn't have those kinds of things. Norway also has a 70 per cent resource tax, and I'm not sure that that would be tolerable in our North American environment. Their sales tax is from 25 to 40 per cent, their GST, if you will; ours is 5 per cent. So they have other ways to fund things. Their income taxes and corporate taxes are very, very high. So that's just the decision that they've made, to have those higher taxes which fund their operating expenses, allowing them to be able to tuck away a lot of dollars into that great fund that they have available for the future.

The Chair: Thank you, David.

Dr. Sherman: A very good question. The whole intent of the fund here was to save nonrenewable resource revenue. The fund stood at \$12.6 billion in 1984, and today when you account for inflation, it really stands at about \$7 billion. So in the last quarter century of back-breaking work we really haven't put any money away. In fact, it's actually lost value because we've had a policy to really spend, to run public programs and spend every cent of nonrenewable resource revenue.

The real question we as a society have to make is: are you willing to pay a little bit more in taxes to actually pay for your public programs? If you look at Canada, the second lowest tax jurisdiction in this country is British Columbia, and they tax \$12 billion more than we do. Saskatchewan, the darling of conservative politics in the country, taxes \$14 billion more. Society has to decide. If they're willing to pay a little bit more, just a modest increase in taxes, and still be the most competitive jurisdiction in the country without going as high as Norway, we could actually start saving money in the fund and use taxation dollars to pay for regular public programs.

The Chair: I mean, we're talking about Norway, so inevitably, I guess, we have to talk about taxes, but I do want to remind folks of our purview here. When we're talking about taxes, it certainly sits outside of the policy-making decisions of this committee.

Coming back to Norway, I think one thing that we have to consider is that the Norwegian fund, which sits at around \$600 billion, is not just a savings vehicle, but it's also a pension fund. So if we're comparing apples to apples, if we build in the pension funds that AIMCo manages for us, we're talking more of a \$70 billion comparative. So I just wanted to throw that in.

I think David Dorward has one last supplemental before we move on.

8:10

Mr. Dorward: No. I hesitate because I really was going to say that my constituents of Gold Bar don't want the government dipping into their pockets for any more taxes. That's what they do in Norway, and that's just a different style and a different philosophy.

The Chair: Well, it's a certainly a different culture. I think we can all agree on that.

We have some folks on the floor that have questions. Before we get to you, we have a little bit of a backlog online. I'd like to get to one more online question, and then we'll return to the floor.

Mrs. Jablonski: Thank you. Another Twitter question from @whitebird12. Is it fair to say that investment gains of fund is what gets drawn down over years or is principal also drawn down?

The Chair: We'll go to our expert panel for that question.

Mr. Epp: At this point in time it's only the income and only that income that is in excess of inflation for the year that gets transferred out of the fund. The principal of the fund does not get touched.

The Chair: Thank you, Mr. Epp.

I believe Rob Anderson wants to give that one a go.

Mr. Anderson: Yeah. Mr. Epp, of course, is right. The principal has not been drawn down, but of course the value of the principal can decrease if the value of the investments in the fund decrease. We saw an example of this in 2008, I believe, with the world financial crisis, where the fund was – I couldn't give you the exact number – worth almost \$18 billion, \$17.6 billion or something like that. It, of course, lost a lot of value that year because everything lost a lot of value that year, all funds did. It lost a couple of billion dollars. In other words, the size of the principal or the value of the fund went down.

The next year, as we saw in the presentation, when the market went back up, the fund earned – I can't give an exact number off the top of my head – roughly \$2 billion, maybe a little less than that. Essentially, the market went back up as much as it had gone down, but instead of leaving that \$2 billion in the fund to replace what was lost, that money was taken out, and it was spent. So the value of the fund decreased.

Even though, of course, that's not technically taking the principal out, what's happened is that because we haven't always left the interest earned in the fund every year to grow, the value over time has decreased, which means that the heritage fund today, adjusted for population and inflation growth, is worth less than it was in 1976, when it was first established. It's a real tragedy, frankly, and I hope that going forward, with the new changes that have been made to the Fiscal Management Act and so forth, we won't repeat that same mistake again for our kids.

Mr. Casey: Well, I think that Mr. Anderson has already touched on it here. We can't do much about what occurred 10 years ago or five years ago or three years ago. I mean, we can talk about it, but tonight should be about what the future looks like for this fund. We can dwell all we want and wring our hands all we want about what should have been or could have been, but let's talk about where we're going with this.

The Fiscal Management Act puts us on the right track with this. We're going to see 30 per cent of the revenues put in place for 2015-16, 50 per cent by '16-17, and 100 per cent of the revenues by '17-18. These numbers are going to be huge at the end of the

day. I don't think anyone will argue that a savings plan for Alberta, a true savings plan built into our budget process, has been missing because it was a piece that was an add-on, and everyone agrees there.

What we have now with the way the budgeting is handled through the Fiscal Management Act is that before we balance our budget on operations, there are a couple of things that happen. Number one, our savings account is looked after, so that money is transferred into savings. It's taken out of revenue and put in savings. The next thing that happens is that we pay any debt servicing that is required. The revenue that's left over then is the operational budget that we have to build and to operate this government on.

So we're taking our savings and we're taking our debt servicing right off the top, and we're guaranteeing that we're balancing the budget on the operations on the revenue that's left over. This is a huge step forward, and it was actually a stroke of genius. If you talk about other places copying the heritage trust fund, I thoroughly believe you're going to see other provinces and other municipalities around the country and around the world copying the fiscal management plan because it really will build a future for Alberta.

The Chair: Thank you for that, Mr. Casey.

You know, in the course of preparation for this meeting I watched last year's meeting a couple of times, and I've also sat in on some of the consultation that our President of Treasury Board and Minister of Finance has done. Through the course of the public engagement last year and from virtually everybody that we talked to, including members of the panel, it was very important for everyone that we begin to renew and invest in that fund.

I think that for the first time in possibly 25 years we're going to be seeing a reinvestment in the fund, and as Mr. Casey very capably said, it's reinvesting the interest that we're making over a three-year period till a hundred per cent of that interest remains in our Alberta heritage savings trust fund and our nonrenewable resources, a sliding scale to make sure that in really good years we're reinvesting and putting a great deal of money back into our Alberta heritage savings trust fund so that we can grow it again. I think that's something we all agree on.

Dr. Sherman, just briefly before we can move on.

Dr. Sherman: Mr. Casey is right. We've got to look towards the future. I don't know if it's a stroke of genius or a sleight of hand, because while we're putting money in the bank account, we're actually taking out money on the credit card and on the line of credit, on the other side of the ledger. We're picking up money there to put it in the savings account. At the same time we're actually gutting the education system, which is really the future. As Dr. de Bever says, we have to invest in technological advancements, which is the education system of our children.

Alberta right now has the lowest high school graduation rate and the lowest postsecondary participation rate in the country, and for us to succeed as a province, we have to invest. We have to look at all of this in a balanced way, not just at how much money is in the trust fund. You've got to look at what your credit card balance is and at what's happening with the public services. These all go hand in hand. You can't save money until you run your household and you make sure you pay off your debt. Then and only then can you really start saving money.

The Chair: Thank you, Dr. Sherman. I'll also take this opportunity again just to let everybody know that our committee is the Standing Committee on the Alberta Heritage Savings Trust Fund.

We're talking about a lot of interesting and fascinating topics, but the focus for our standing committee and the focus of our expert panel is on the trust fund itself.

With that sentiment in mind, we'll carry on with a question from the floor.

Mr. Allred: Thank you, Mr. Chair. Ken Allred from the beautiful municipality of Crowsnest Pass and part of the Rocky Mountains. Firstly, I would like to commend the Legislature on passing the fiscal accountability act and for finally, after 30 years, getting the heritage fund back on track. I think that's commendable, and I was very pleased to hear that it's etched in legislation. I just hope that in the future you will move it up to the full 30 per cent of non-renewable resource revenues.

I was pleased that Mr. Casey earlier in the evening clarified the fact that the heritage fund was not primarily set up as a rainy-day fund. I would just like to have you clarify that the objectives of the heritage fund are still as they initially were set up, and that is that 50 per cent of the fund was set up as an endowment for future generations, 40 per cent was for economic diversification and quality-of-life improvements, and only 10 per cent was for a rainy-day fund. Could you please clarify if that is still the objective of the fund?

The Chair: Thank you very much for those questions. You know, I've got some historical notes here that sort of speak to that. On May 19, 1976, when royal assent was given to the Alberta Heritage Savings Trust Fund Act, the act actually outlined three objectives for the heritage fund. At that time, in '76, it was to save for the future, to strengthen or diversify the economy, and to improve the quality of life in Alberta.

Now, anybody else on the panel care to speak to that question?

8:20

Mr. Anderson: I'll speak really quickly to it. I first want to just recognize Mr. Allred for his service as an MLA for St. Albert. I remember sitting many nights in the Legislature hearing him talk very passionately about the need to restore or strengthen or get back to, I guess you could say, the mission of the heritage fund, and he should be commended for fighting for that for so long. It's good to see him here, and I'm also glad to see that he's moved to southern Alberta. That's always good to see.

I think that there has been a little bit of mission creep, a little bit of change in the mission of the heritage fund. Obviously, the sustainability fund – it's not the sustainability fund any more. It's called the contingency fund; it just got changed again. We like changing. You know how it goes. The contingency fund has kind of been separated out, and there's a whole different set of goals and milestones and criteria for how that's going to be built in the future. Then, of course, the endowment funds for quality of life, the education funds we talked about, Alberta Innovates: these things are much less than 40 per cent of the total value of the fund.

I think that there has been mission creep, but at the same time I think that, you know, that's natural. As we go and as society changes, especially now, when we're not seeing the end of oil but where there's kind of a light at the end of the tunnel, I think, where we're seeing as a province that, oh, my gosh, we might not have all this money forever, I think that putting a little bit more emphasis on the saving portion for the next decade or two decades – who knows how long? – is a really positive thing. I really do think the day will come when we cannot rely on this type of oil and gas revenue much longer.

The Chair: Thank you, Mr. Anderson, and thank you also for acknowledging my friend Mr. Allred. I didn't want to be too much of a hometown guy. It's great to see you here, and thank you for the question.

We have some more folks on the floor, but before we get there, we're going to go to a question online.

Mrs. Jablonski: Mr. Chair, we have a very anxious person from Twitter. It is AHSTFWatcher. "Noting that a significant return is seen in the investment in global equities, are considerations taken to make ethical investments and what controls are in place to ensure they match Alberta values?"

The Chair: That's an excellent question. I know that in reviewing some of the committee meetings in years past, this has been a topic hotly spoken to in our committee meetings.

Dr. Sherman, I think we'll throw this question at our expert panel, perhaps to Dr. de Bever.

Dr. de Bever: Okay. Socially responsible investing can be a minefield. It's 80 per cent common sense. I mean, why would you invest in anything that has poor labour practices, poor environmental practices, anything else that society in general doesn't agree with? Ultimately, it's going to hurt the business that you're investing in. There's a small component where it becomes a bit of a political game that you can agree or disagree with. Not all of us in this room would even agree on what principles of social investing should be, and you have to be careful.

Not too long ago I was on a video conference with a Dutch pension plan that wanted to blackball some companies that are investing in the oil sands because they were environmentally unfriendly. If we start picking on other people because they're in the mining business and mining generally is a dirty business – you know, you punch a hole in the ground, and usually it doesn't look too pretty, at least in the beginning – you have to be careful how you let socially responsible investing play out.

We spend a lot of time at AIMCo in doing it better. We're getting more and more involved in tracking things that shouldn't be happening. For instance, the textile factory collapse led us to say: "All right. How do you know that you're even investing in that kind of thing? It might be two or three layers deep in your investment structure." You have to be very careful how you handle it, that you don't apply Canadian standards to third-world countries.

I'll give you an example. When I was 14 years old, half of the class in high school disappeared out of class and went to work in the factories because even 50 years ago that was pretty common. We find that offensive now, but there are still economies in the world where people enter the labour force at a much younger age than we do and where there's a necessity for children to contribute to family income. Then it becomes a balancing act. How do you trade that off against, for instance, the need for education of that kind of population? We pay careful attention to this kind of thing, but it's not as easy as it looks because some of it is in the eye of the beholder. What is socially responsible, and at what point do you punish a company for having some little piece that you disagree with?

I'll give you an example. General Dynamics makes F-16s, I think. Norway put General Dynamics on the forbidden list. Now, isn't it a bit hypocritical when your air force flies F-16s but you put the company that produces them on the list of people you can't invest in? We come across examples like that all the time. Yes, we pay attention to it, but we also apply common sense when we do it.

The Chair: Thank you, Dr. de Bever.

We're going to go back to the floor for a question.

Mr. Eggen: No. I have a comment.

The Chair: I'm sorry. That's right. David, forgive me. David Eggen.

Mr. Eggen: Thanks. It's very important in a democratic society, when we're making investments using public money, that we debate ethical issues on a free and open basis. That debate has to be vigorous, but it can't be encumbered by our fear that perhaps it would compromise our economic situation or that it doesn't represent everyone's values at any one time. We are using a set of values that we use for ethical investment – right? – through AIMCo and the heritage trust fund. That doesn't preclude us from debating and bringing up new issues as they come up over time. Yes, child labour perhaps was something that was more pervasive in different times, but it's something that we have to debate and look at very critically and question as to whether we invest in that using our public money.

The same can be said about the oil sands. We debate those issues, and we put them out and deal with them. If we choose to try to put them away, then we end up having them come back to bite us, right? Debate on ethical investment is absolutely essential. It's not going to deter our economy or our investments. In fact, ultimately, it makes for a stronger investment in the long term.

The Chair: Thank you, Mr. Eggen.

We're going to now go to a question from the floor.

Ms Bell: Beth Bell from St. Albert. This is aimed at Dr. de Bever. Does AIMCo have a prohibition against investment in small- and mid-capital energy producers in Alberta, and if so, why?

Dr. de Bever: We don't. In fact, we invest in a number of small- and mid-cap companies. Our criterion is not to discriminate on the basis of size. It's whether the investment is likely to be producing as much return as we could get somewhere else. Again, I come back to: we don't have a prohibition on investing in energy or an inclination to do so. Part of our role is diversification, so unless the returns are compelling, energy is probably not the first place we would look because it doesn't diversify the stability of the fund.

To answer your question, no, we don't have a prohibition or a policy against investing in small or mid-sized companies.

The Chair: Thank you, Dr. de Bever.

We are going to go back to the chat lines.

8:30

Mrs. Jablonski: This also is a Twitter question, from @noleftandright. There is research suggesting the centre of economic activity sits in Asia, not the west. Does this factor in decisions?

Dr. de Bever: Well, you don't invest in the centre of gravity. You invest in jurisdictions where you expect to get your money back with a decent return. Frankly, I have trouble with places like India and China for that reason, because I don't feel that I can always trust the legal system. That's why certain jurisdictions that are emerging markets where you have solid legislation in place provide a better opportunity.

For instance, we have a lot of money in Chile. Now, why is that? Chile is not that big. Well, Chile decided it needed a lot of foreign capital to build their economy, and they were willing to

make it very attractive for that capital to come and stay. For instance, a lot of Canadian pension funds basically own half of all the toll roads in Chile. And I'm very happy there.

Going to Brazil is a different story. Argentina, you wouldn't get me there with anything because I can't trust the people there. I mean, if people start nationalizing your investments, why would you go there?

I look for jurisdictions everywhere where the opportunities are attractive from a return point of view and where people stick to the rules that they set out because both things are important in trying to make your heritage fund grow.

The Chair: Thank you very much, Dr. de Bever.

We have a couple of questions online, and we have a gentleman on the floor. Let's go to the question online, and then we'll come back to the floor.

Mrs. Jablonski: Another question from Twitter. Does this standing committee set goals or expectations on AIMCo percentage-wise?

Dr. de Bever: Yeah, you do. You set the asset mix.

Now, I have a friendly debate going with Finance over that. I think this fund is probably, given its long-term nature, not as aggressively invested as it could be, but that's a debating point. It depends on how much risk you're willing to allow on this fund. Here's the tradeoff. The more risk you let into the fund, the higher your long-term return is likely to be. The problem from a politician's point of view is that taking more risk also means that there are going to be years where you're taking a bigger tumble because that's what risk is. Risk is the possibility of losing a lot of money in a very extreme set of circumstances in return for having a higher long-term return. So that's the debate.

But the answer is yes. The Department of Finance and the minister give me marching orders in terms of how much to invest in stocks, how much in bonds, how much in infrastructure, how much in real estate, things like that.

The Chair: Thank you, Dr. de Bever. I mean, that's a terrific question in terms of speaking to the mandate of this standing committee. I could read the mandate, but I'll just summarize it by saying that our role as a standing committee is to review and approve, to report, and engage the public on the Alberta heritage savings trust fund.

I believe Dr. Sherman has a comment, and then we'll go to David Dorward to wrap up this question.

Dr. Sherman: Essentially this question is really: do we as a committee have an oversight role and a mandate and any responsibility? We actually did have that responsibility. Recently the legislation was changed, so we actually don't have any direct oversight. That oversight has been removed in a law that was passed recently. So essentially we get a report, and we make another report to talk about the report.

I had asked the chair here who said that that is correct. Our oversight function as a committee is no longer there over the Alberta heritage savings trust fund. So given that we can no longer review or approve the business plan of the heritage fund, we've all said – you know, we used to have the no-meet committees, and the question is: do we have a no-point committee now?

We're asking for the government to restore in legislation so that we legislators can actually have oversight and input into what Dr. de Bever does.

The Chair: Well, as you can probably guess, Dr. Sherman, I don't share that viewpoint. I think what transpired is that there are 87

MLAs that sit in the Assembly, and through the course of the spring all 87 MLAs had an opportunity to voice their opinions and their constituents' opinions on this very issue.

In terms of the value of this committee I think all we have to do is look back at last year and the engagement that this committee had and what we heard from our audience at this meeting, when we reported that folks wanted to see us grow the Alberta heritage savings trust fund, and a direct result of that is our fiscal management framework. So I certainly see value in this standing committee. I'm proud of the work that this committee does.

I'll let David Dorward have the last word on this question.

Mr. Dorward: Thank you, Mr. Chair. Yeah, all MLAs have input to the minister that's responsible for this area, our thoughts, and we certainly have the Assembly where we have the ability to ask questions of the minister or give statements to the minister on our thoughts relative to this and in our committee as well.

I would like to go back to the business plan of the government, 2013-16, which was released this spring. The pertinent paragraph says:

The President of Treasury Board and Minister of Finance, who is the hon. Doug Horner right now, is responsible for the management and investment of the Fund and is required to report on the performance of the Fund within 60 days of the end of each quarter and make public the annual report within 90 days of the end of the fiscal year. The President of Treasury Board and Minister of Finance prepares the business plan,

which I have a copy of in my hand here,

and presents it for approval to Treasury Board,

a committee that I sit on,

and the Standing Committee on the Alberta Heritage Savings Trust Fund.

So we see that and approve it, which is what it states here.

Thanks, Mr. Chair.

The Chair: Thank you, David Dorward.

Rob Anderson has asked to just make a brief comment about this specific question.

Mr. Anderson: It is true, as Dr. Sherman says, that we don't have that oversight role as strongly as we did before, and I do think that's not good. But I do think that this committee does serve a very, very important purpose, and it's not so much one of oversight but one of transparency and accountability. If you look at the mission statement, one of the things that we are supposed to do is report to the Legislative Assembly on whether the mission of the fund is being fulfilled.

This is the people's fund. I mean, this is one of the most unique things we have in Alberta. And I think it's very important to have an active committee which is constantly assessing, as the statement says, whether the mission of the fund is being fulfilled. If we don't do that, there's a chance that we get some serious deviation from what the fund was intended to be. If we keep it public, if we keep it out there, we keep having these meetings and raising the awareness, it allows us to get that feedback back to government and have that transparency and accountability in the system.

Although I'm a big fan of Dr. Sherman, I have to disagree with him on this. I do think that this committee does have a very important purpose.

The Chair: Thank you for those comments, Mr. Anderson. I think some of the important words that you said are that the Alberta heritage savings fund, that \$16.8 billion, is our money. It's not the government's money; it's the people of Alberta's money. With

that in mind, I do strongly believe, and I'll say it again: I'm proud of the work that this committee does.

With that said, we'll return to the floor for what could possibly be our last question of the night. There's an opportunity to get a question or two in online or if there are any last questions from the folks in the auditorium today. I do thank you all very much for coming and asking such engaging and intelligent questions.

Mr. Korchinski: Being the last person at the mike, does that mean that I can continue for some time?

The Chair: I did say at the onset that we were going to be brief in our answers, and I think we haven't lived up to that billing. So we'll pass you the floor, and you do have a little bit of time.

Mr. Korchinski: Okay. First of all, Ken Korchinski from St. Albert. I've actually got two or three points, and I'll raise them all at once. This is for our expert panel. First of all, could you tell us how you measure up against similar types of funds like pension funds or other funds of a similar nature. I'd like to hear that. You know, I commend you on your 11.6 per cent growth, but to me it doesn't mean much unless I know how you compare against your peers.

8:40

Secondly, in terms of risk management, a thing that's on a lot of our minds that we hear in the press is the circus that's going on in the United States, especially with regard to their debt, \$16 billion in debt.

Mr. Casey: Trillion.

Mr. Korchinski: Trillion; I'm sorry.

Anyway, they don't appear to have an answer to it. Now, when you look at your risk management or your strategy, how do you deal with that? How do you account for that? You know, the worst-case scenario, I suppose, is that the United States is going to do something very serious and go bankrupt or something. I don't know. I'm not an expert, but I worry about that.

Thirdly – I've got a three-part question – I can understand your investments when you have stocks and bonds. You get reports every month or every quarter, and you know exactly what their return is. But on your alternative investments like real estate, how do you evaluate them when you turn in a report of this nature?

Dr. de Bever: Actually, those are three very, very good questions. The first one: how do we measure up? There's a tendency to agree at the beginning of the year that the outcome should be measured against the objectives that you set, and at the end of the year everybody ranks everybody by net return anyway. The reason that that's important is that I get my marching orders from Finance in terms of the asset mix that I can invest in, right? Well, that asset mix has a certain innate return. What that asset mix really does, by the way, is it sets a risk boundary around what I can invest in. Based on that asset mix, I can figure out what's the worst that can happen to me once in 40 or once in 100 years, and that's how I control the risk in that program.

Now, if you look at how we've measured up, I think on a risk-adjusted basis we've done very well, but there are funds that had higher net returns. Let me give you an example. HOOPP, which is not an endowment but a pension plan in Ontario, had a 17 per cent return, but it did so with 100 per cent leverage. Our legislation essentially says I can't use any. Now, do I want to use 100 per cent leverage? No, I don't. But the point is that if you have different tools to play with, you can end up in certain years in

much better or worse positions. So if I take their 17 per cent and translate it back, it's comparable because if you take 17 per cent and you take the cost of the debt and you add it back in and you translate it to a unlevered portfolio, we actually look pretty good.

You have to measure each fund against the objectives that you set for it. You can't say, "Well, I only want you to take so much risk," and then somebody else takes more risk, makes a higher return, and you say: well, you didn't do as well as the other guy. It's very hard to compare funds, but on a risk-adjusted basis I would say that over the last five years we've done relatively well.

Now, your second question is a really interesting one, and that's really whether bonds are a safe asset or a risk-free asset. Government bonds are always taken to be a risk-free asset even though governments default on their debt more often than you realize. In my mind, bonds are not a risk-free asset, and your reference to the U.S. is a good one. There's probably more risk in U.S. bonds now than there was, say, 20 years ago, so that's an issue.

Bonds are not a very good asset for another reason. Whatever risk there is in bonds, the return on that risk is going to be lousy. I showed you that graph. If interest rates stay stable, the return is going to be low. If interest rates go up, the return is going to be negative. Now, what's good about that, right? So it's not just the risk; it's the return on that risk. My guess would be that the return on bond risk is going to be negative or lower than it is on stock risk, where it's likely to be positive.

Your third question is a really interesting one. One of the advantages that you have when you can invest money for the very long term is that you can commit it to things that don't get measured on a daily basis, like forests or real estate or private equity or whatever. The theory is that if you do that, you can over time get a higher risk-adjusted return because committing your money for a longer period of time should have a return in itself. In other words, the fact that you're tying your capital up for a longer period of time should give you a higher return.

Now, how do you value assets that have that characteristic? We have expert external valuers, and what they basically do is measure the cash flows on these things. Real estate is the easiest one. Real estate is pretty straightforward. You look at the rent rolls on, say, a shopping mall, and you say: "All right. How long is that likely to continue? What's the present value?" Then you discount it at some interest rate, and that gives you the value of the building. For forestland it's a little trickier, particularly the kind that we invested in, but there are ways of doing it.

Ultimately it's still a guess, but I would tell you that the measurement that the stock market gives to assets is not accurate either. Do you really believe that at the end of 2008 stocks and bonds were what the stock market and the bond market said? It reflected more the desperation of the last seller than any fundamental economic value. It's always a guessing game as to what something is really worth. In fact, if you tried to sell all your stock – for instance, if I took, say, Imperial Oil. If I try to sell it all in one day, I couldn't get for it what yesterday said that stock was worth. So, yeah, stock markets and bond markets measure value, but the accuracy of that value is not always any worse or better than what you have in the unlisted markets.

Mr. Korchinski: Thank you very much.

The Chair: Thank you, Dr. de Bever, for that very fulsome answer.

We have a couple more questions that have come in online. Deputy Chair.

Mrs. Jablonski: Thank you, Mr. Chair. This question is from Twitter, one entry but three questions, from @why_knot1. Has the

Alberta heritage savings trust fund rid itself of death funds? What bonuses were paid for last fiscal year? How much was charged to the Alberta heritage savings trust fund and on what basis?

Dr. de Bever: This is an emotionally loaded question. All I would give as an answer is that 20 U.S. states now have gone on record that the kind of vehicles we invest in are socially desirable. What they're referring to here is insurance policies that if you cashed them in with the insurance company when you need cash, don't get the full economic value. So the trade-off is holding onto your policy so your heirs can collect or cashing in the policy and dealing, for instance, with health issues or whatever while you're still alive. Those states have basically said that from their point of view and from a social point of view it's better to have that instrument.

And it's a useful arbitrage. Basically, it's no different from investing in annuities. You could think of annuities as death funds because if people die earlier than anticipated, you make money. It's no different from keeping a policy alive and cashing in when the person dies. It's just a risk assessment, and basically it became a very good instrument when the market got dislocated. In 2008 there were more people willing to cash in their instruments because they ran into trouble with some of their other investments, among other things, and there were fewer people buying because the banks were out of the esoteric asset game because of new regulatory requirements.

So, you know, I would like to get rid of the emotional label and focus on what the economics are and what the social function of the investment is.

Mrs. Jablonski: The next part of that same tweet by @why_knot1 was: what bonuses were paid for last fiscal year, and how much was charged to the Alberta heritage savings trust fund and on what basis?

8:50

Dr. de Bever: The basis is easiest. Roughly speaking, in the long run if we generate a dollar more than markets deliver to us, the management group that's responsible for that gets about 5 cents. If we had done that through an external manager, he would have typically gotten 20 cents. Again, it comes back to – you know, it used to be that no one paid any attention to a lot of money being paid to anonymous external managers, but there now is a lot of attention on people internally, that they can see because they're on our management payroll, that are getting paid actually a much smaller allowance for adding value to your heritage fund.

The Chair: Thank you, Dr. de Bever.

As we're getting close to the finish line here, we have a couple more questions we may be able to get to from our online engagement. Thanks to everybody online and the questions through Twitter. Very much appreciated. We may have one more question from the floor it looks like, and we'll give that certainly some priority. We'll go to online, and perhaps we'll be able to wrap up with a question from the floor.

Mrs. Jablonski: This is from Matt, and he says, "In referring to the Heritage Fund Mr. Khan said 'This fund is our money not the government's money' . . . but isn't all money spent/collected/saved/owed by the government 'our' money?"

The Chair: I think the short answer to that – and perhaps we can all agree – is yes. Yes, you're here. Absolutely.

Mrs. Jablonski: One more question?

The Chair: You know what? Let's go to that question, and then we'll go to the floor. That set the record for short questions.

Mrs. Jablonski: Okay. Another Twitter question from Marie Renaud: "If fund revenues will no longer be used to help pay our expenses, what are the plans to manage loss of revenue?" I think she's referring to our financial act.

Mr. Anderson: Well, this is a great question. There's a lot of truth to it. You know, the government is planning on investing more in the heritage fund, leaving the interest in there and so forth, but of course they've been spending the interest in previous years. So this is a change, and that means less revenue.

One of the issues that you're probably going to hear debated a lot now that we kind of have the direction of the heritage fund more sorted out than we did before is the issue of debt. By not using those revenues anymore, leaving them in the fund and so forth, along with the increased spending over the last decade in this province, we're in a position now where we're borrowing quite a lot of money every year, roughly \$4 billion every year, for certainly the next three years according to the government's budget document. Is that appropriate? Is that the right amount? Are we kind of, you know, robbing Peter to pay Paul? Is that what's going on with the saving strategy and the debt strategy?

You know, these are all questions we're going to have to debate as a province, and there are a lot of different answers for them. My view, of course, is that we should avoid debt and we should work on the expense side and try to find ways to save money so that we can both save money in the heritage fund and not go into any further debt than we already have been.

The Chair: We're running dangerously close to the finish line here. I do want to get to the last question from the floor.

David Dorward, really quickly if you can.

Mr. Dorward: Yeah. Fortunately, we have a Premier who along with Minister Horner toured the province in the fall of 2012 and heard from Albertans that they wanted us to look at our own expenses first, and that's exactly what the budget did when it came in this last spring. So I'm confident that the government is working towards that. I sit on results-based budgeting, one of the six committees, and we're doing those kinds of things in there right now. Good question.

The Chair: Yeah. You know, this really is an excellent question in the sense that, as my esteemed colleague Mr. Casey said, this is about looking forward. The fact of the matter is that over the course of the last 37 years we've directed almost a billion dollars a year from our fund into general revenue, which has helped pay for essential services, which has helped pay for infrastructure. You've heard this time and time again from our experts: it's about finding and striking the right balance. Moving forward, our implementation of the Fiscal Management Act begins in 2015-2016, so we have the opportunity of time to make sure we're doing this right.

Now, really quickly, I want to get in the last question from the floor before we wrap this up. Sir.

Mr. Lupton: Thank you. Ron Lupton, from Ma-Me-O Beach. Should we as Albertans be happy with the amount of royalties collected by the government from the oil companies? Is there any kind of a parallel that we can draw between these revenues and the profits taken by the oil companies that sell our product?

The Chair: Thank you for that question.

I'll remind you that we're very close to the end here, so if we can answer this quickly, please.

Mr. Eggen: Yeah. We've heard a lot about how we are restructuring the heritage trust fund. That's something we've been fighting hard to do, and I commend everyone for doing that. But it means very little if we don't have the money to put into that structure. Certainly, we have managed to do so in the past, 30-some years ago, but we haven't done that for the last 20 years, and we won't be able to do it for the next 20 years until we start collecting the royalties that are owed to us as the citizens of Alberta.

The Chair: Folks, I'll remind you that we can answer some of these questions for you and carry on with this discussion after the cameras close down, but unfortunately we've run out of time.

Before I close, I'd like to sincerely thank all of you for your participation tonight. I think I can speak on behalf of the entire committee when I say that we've enjoyed spending the evening with you and engaging in conversation about the Alberta heritage savings trust fund. I really want to thank everybody that was here tonight. This really is a big part of the mandate of our committee, the public engagement piece. I know it wasn't the most pleasant evening tonight, so those who made it out tonight really wanted to be here.

Mr. Anderson: Outside.

The Chair: Outside, yes. I should qualify that. Inside it's remarkably pleasant in the beautiful confines of the Oasis Centre.

Thank you so very much for being here. I want to thank our esteemed panel of experts as well. Gentlemen, you did an outstanding job tonight. I also definitely want to thank my colleagues who serve so very dedicatedly on this standing committee. As I said, I'm very proud of the work that all of my colleagues on the committee perform on behalf of all Albertans.

With that said, we are hosting a very light reception. Please don't feel that you have to run away. Most of my colleagues, I believe, are able to stick around and would love to speak with you and answer any more questions you have or to just have an opportunity to say hello and thank you for coming.

I'd also like to thank the very dedicated staff who made this all happen and worked very hard for a very long time to make this happen, so a round of applause for them as well, please.

Folks, I believe in showbiz they say: that's a wrap. So we'll see you in the lobby for the reception.

Thank you.

[The committee adjourned at 8:59 p.m.]

