

Title: Wednesday, November 5, 2003 Heritage Savings Trust Fund Committee

Date: 03/11/05

Annual Public Meeting – Grande Prairie

[Mr. Hutton in the chair]

The Chair: Good evening, everyone. I'm Drew Hutton, the MLA for Edmonton-Glenora and the chair of the Alberta Heritage Savings Trust Fund Committee. I'm just going to ask the other members to please sit down, and then I'm going to turn it over to one of our hosts for the day, Mel Knight.

Mr. Knight: Well, good evening, ladies and gentlemen. I certainly want to welcome all the committee members to Grande Prairie. I think that we had a very good day today in and around the city of Grande Prairie and visited some of our industrial area and certainly educational facilities and recreational facilities. We got to Centre 2000 and had what I would say is a very productive day, both from the point of view of the committee and certainly to allow committee members to get a little more appreciation for the northwestern part of the province and Grande Prairie in particular.

I'm certainly very proud and pleased that we were able to have the committee come to Grande Prairie for the heritage trust fund's annual meeting. As a member of the all-party Standing Committee on the Alberta Heritage Savings Trust Fund I am pleased that the city was chosen to host the 2003 annual public meeting.

I would like to at this time take an opportunity to introduce the other committee members that are in attendance. On my left is Drew Hutton, the chair of the Heritage Savings Trust Fund Committee and MLA for Edmonton-Glenora; Bill Bonner, MLA for Edmonton-Glengarry; Debby Carlson, MLA for Edmonton-Ellerslie; Rob Lougheed, MLA for Clover Bar-Fort Saskatchewan; Richard Marz, MLA for Olds-Didsbury-Three Hills; and my longtime friend and next-door neighbour about 40 years ago, George VanderBurg, MLA for Whitecourt-Ste. Anne.

I'll turn it over to Mr. Hutton.

The Chair: Thank you very much, Mel. I'd like to introduce some other folks that have attended the meeting with us, but before I do that, I'd like to thank Mel and Gordon Graydon as well, two great MLAs representing the area.

I'd like to first introduce the previous MLA for this area. Where's Walter Paszkowski? Walter, give us a wave. Thanks for coming out, Walter. He represented the riding for a number of years, and it's good to see him out.

I'd like to introduce the Hon. Greg Melchin, Minister of Revenue; Doug Stratton, who is the director of fund management for Alberta Revenue; and Peter Orcheson, who is the senior manager of equities for Alberta Revenue. Also here representing the department – give a wave – is Tammy Forbes, information officer. At the back there Karen Sawchuk, committee clerk; Liz Sim, senior editor of *Alberta Hansard*; Michelle Grove from *Hansard*; and Melanie Schmahl, network analyst for information systems services.

Also, I was remiss in identifying my colleague of the day from Dunvegan. Hector Goudreau is here in the room too. Hector, good to see you out. Thanks for coming, buddy.

Is Gordon Graydon here? Where is Gordon? There he is. Thanks for today, Gordon.

I'd like to start our presentation and let you know that it will be in two parts. Members of the committee will review the history and mission, structure, and governance of the heritage fund. The Hon. Greg Melchin, Douglas Stratton, and Peter Orcheson will then

discuss the operation and performance of the fund. We will have a question and answer period following the presentation, and when you go to the mike – and I'll remind you of this later too – please announce your name when you're asking your questions.

I would like to now turn it over to my colleague Debby Carlson to begin the presentation.

Ms Carlson: Thank you, Mr. Chairman, and I would also like to thank everyone for attending this evening. The heritage fund was started in 1976 and has been a unique aspect of Alberta's financial situation. No other province has such a fund. From 1976 to 1983 the fund grew, with 30 percent of oil and gas revenue going into the fund. From 1982 to the present all income from the fund was transferred into general revenue to meet the financial priorities of the province. Further, spending on capital projects ended in 1995. The bulk of the fund's investments up to 1996 were in fixed-income instruments such as bonds and money market securities.

I'll let George VanderBurg continue.

7:10

Mr. VanderBurg: Thanks, Deb. Again, to Mel and Gordon and the community, thanks so much for your hospitality today. It was just great. Great to see some former local politicians that I've served with in the past here as well this evening.

To get on with the task at hand, an obvious question raised by the chart is why the fund has not grown since 1987. I think that's probably the question that I get most when I'm out in my constituency and talk about the trust fund. The value of capital projects is not included, and after 1987 nearly every dollar of income generated by the fund was taken out of the fund and used within the general revenue fund. Those dollars were used to support programs in various sectors, such as health, education, and infrastructure. The only exceptions were in 1997, '98, and 2000, when \$176 million, \$25 million, and \$230 million were retained for inflation-proofing.

The second last bar shows a drop in the book value of the fund in the fiscal year '02-03, representing a loss in that year. We'll be discussing recent income in later slides.

The income profile of the fund is discussed by Rob Lougheed in the next slide.

Mr. Lougheed: Thanks, George. The chart before you indicates that the heritage fund has made a substantial contribution to the province's revenue. From '77 to '86 the income grew dramatically. This reflected the growth in the fund and the fact that the interest rates were substantially higher during that period of time. Income from the fund has declined, which has reflected the fact that the fund has not grown and that there's been a decline in the interest rates as well. Interest rates peaked in about 1981 and then declined further to around this current time, where we're looking at 5.4 percent for 30-year government bonds.

Cumulative income transferred to the general revenue fund as of March 31 of this year, 2003, was \$21.9 billion and \$3.5 billion for capital projects, so that's a total of \$24.4 billion. The net loss in 2002-03 resulted in no cash transfers to the GRF that year. That was the first net loss for the heritage fund, and that loss was attributed to the equity investments and also the decline in those equity investments during that year.

I'll turn it over to Richard.

Mr. Marz: Thanks, Rob. The income that Rob talked about that was transferred over the years to the general revenue fund does not include the impact of the legacy investments, which continue to make social and economic contributions in the province. One

example of this is the Alberta Heritage Foundation for Medical Research endowment fund. This fund was started in 1980 with a \$300 million contribution by the heritage fund, and not only did this provide an immediate impact in terms of the advances in medical science but has also provided a competitive edge in the biotechnology industry.

By 1996 concerns were raised about the sustainability of investment income, and many people were wondering whether we should sell off the fund and just pay down the debt of the province, and if it was decided to keep the fund, how should the fund be managed in the future?

Bill Bonner will discuss how these issues were resolved.

Mr. Bonner: Thank you, Richard. To all of you that have attended the meeting tonight, thank you very much for your interest and your warm hospitality today. We certainly have enjoyed it and had a great day.

An important step in the resolution of those issues was a broad consultative process. In 1995 questionnaires were sent out to Albertans asking specifically whether Albertans thought the fund should be sold off or retained. Further, if the fund was retained, how should it be managed? As a result of that process it was decided to retain the fund but manage it on a new basis. The mission of the fund would be to focus on maximizing the financial return. This would allow the current and future generations of Albertans to gain the maximum benefit of the fund.

In addition, provisions are in place in legislation to allow the fund to grow. Given the province's strong fiscal position in 1999-2000, \$230 million of income was retained in the fund. This will basically offset the impact of inflation.

Finally, the new legislation and business plan for the fund calls for professional investment management. It was decided that policy investments would be sold and that the fund would be managed on the same basis as an institutional endowment fund. The issue facing the government in 1996 was: how do we get from an income-oriented fund to a fund that would give us an opportunity to maximize the potential financial return on the fund?

Mel Knight will now speak to the governance of the fund.

Mr. Knight: Thank you very much, Bill. At this point in time I have to diverge just a little bit and concede that my colleague George VanderBurg has probably still maintained his position as drawing out the most numbers of people to an annual meeting in recent times. In Whitecourt he had an excellent turnout. Richard is now saying no; he thinks it was him. So there's a little contest going on here. I just wanted to point that out. Again, thank you very much, Bill.

Certainly, one of the keys to the heritage trust fund is transparency, and every quarter an investment report is provided on the fund both in hard copy and on the heritage trust fund's web site. Copies are available at the back, and we would be happy to put anyone in attendance on a mailing list if you so require. In addition, an annual report is prepared and published within three months of the end of the province's fiscal year, which is March 31.

Another key is accountability. We have clearly defined benchmarks that we can use to measure the performance of the fund. In addition, we have adopted a well-defined standard of care in the management of investment, the prudent person rule, which is the basis for the investment management industry. We have instituted public meetings such as this one to discuss the fund and its performance. Finally, the fund's performance is reviewed quarterly by an all-party committee of the Legislature and by the new Endowment Fund Policy Committee.

I'll let the chair, Drew Hutton, continue this part of the

presentation.

The Chair: Thank you, Mel. The meeting is not over. You could go call a couple of friends and break George's record if you'd like.

The chart broadly sets out the governance structure of the plan. First, the government as elected representatives of Albertans is responsible for the broad fiscal objectives of the fund. It is at this level that the decision to create the fund was made and, more recently, to underscore the principle of an endowment for all Albertans.

The select standing committee is created under section 6 of the heritage fund act and currently includes two of nine members that are not in the governing party. The duties of this committee are (a) to review and approve the business plan, (b) to receive and review quarterly reports, (c) to approve the annual report, (d) to review after each fiscal year-end the performance and report to the Legislature as to whether the mission of the heritage fund has been fulfilled, and lastly, (e), to hold public meetings with Albertans on investment activities and results of the heritage trust fund. Today's meeting fulfills the final requirement.

The act also delegates the day-to-day running of the fund to the Minister of Revenue. The Minister of Revenue in this fiscal year created an Endowment Fund Policy Committee. The committee has responsibility for advising the minister and is comprised of three MLAs, including the minister, plus private-sector investment experts. Implementation of investment policy is charged to the investment management division of Alberta Revenue.

I will now call on the Hon. Greg Melchin, Douglas Stratton, and Peter Orcheson to discuss the operations of the fund.

7:20

Mr. Melchin: Thank you, Drew. I, too, would like to thank everybody here for taking the opportunity to come and visit with us this evening. Feel free at the end to ask questions of anyone here with regard to the heritage fund.

We're fortunate, really, in this province to have had this \$12 billion asset working for Albertans. Having produced over \$25 billion of income through its life, it has benefited us in tremendous ways. We felt it important that a number of years ago a select standing policy committee, an all-party committee, was created for oversight and provision of help and assistance in policy and direction of the fund to the department, first to the Minister of Revenue and, clearly, to the investment management division under the Department of Revenue.

We also felt this year that we wanted to strengthen some private-sector involvement in some policy advice, and as such we did create an endowment policy committee, as the chairman outlined. That committee is newly formed and put in place and is of great assistance already in providing expertise and advice with regard to investment policy. That will form the basis of business planning, which then eventually will come to the all-party standing committee to ratify and approve a business plan of the government.

We want to switch focus now a little bit to talk more about the investment management division: its structure, its investment policies, benchmarks, and how we manage this fund. You're going to see through this that the last couple of years – this year-end being reported on March 31, 2003, was the end of a very difficult year in the markets globally. The heritage fund did not escape without substantial declines in market values in the fund through that period of time.

I would say, though, that we do invest in the long term. We know that Albertans want this fund to be here for the future. That's why you can take a long-term investment perspective, why you can afford

and should have a diversified portfolio of equities and bonds and the like, and I'll have Doug and Peter complement that issue in more detail. Part of that, you could see, is that just as the markets have declined, in these first two quarters of this year the markets have substantially risen. So you've got to take a longer term perspective, be prepared to handle some volatility, acknowledging that over the long term we will do very well.

So we'll turn our focus now to some of the structure, benchmarks, and the like. Doug will start.

Thanks.

Mr. Stratton: Thank you, Minister. In terms of Alberta Revenue's investment philosophy that we bring to the management of the fund, we would characterize ourselves as being first and foremost risk aware. We pay close attention to where we have invested the fund relative to the investment policy approved in the business plan. Risk primarily is managed through diversification. We look at the fund to make sure that we do not ignore or have an excessive exposure to a particular asset class, equity index, investment style or stock or industry. This was an important consideration in the decision to have half our equity exposure in non-Canadian markets. Canada represents 3 percent of the world equity market and does not have exposure to many key growth sectors. By increasing our non-Canadian equity exposure, we have increased our overall diversification.

We also consider ourselves to be disciplined investors. We look for strategies that can generate value-added on a constant, repeatable basis. We look for opportunity to add value incrementally where it makes sense. In some markets, such as the U.S., it has been tough to beat the benchmark index, the S & P 500. Rather than risk underperforming in the market, we have indexed a significant portion of our U.S. exposure. We take a long-term view and do not try to anticipate every bump and blip in the market. We believe that cost matters. A clear, competitive advantage is that we can invest at a very low cost. Finally, we do not do everything in-house. About one-third of assets are managed outside of Alberta Revenue.

This chart illustrates conceptually the investment structure of the fund. From the perspective of investment management, the investment policy as described in the fund's annual business plan is our starting point. From this we set our actual implementation plan, which includes the actual asset mix and the method of accessing particular asset classes. Investment management uses a number of strategies to access investment performance. We use traditional managers that try to add value with stock selection. We add managers with different styles of investing, growth, value, et cetera. We use synthetic structures, such as equity swaps, and we use nondirectional hedge funds as well.

This pie chart illustrates the policy asset mix of the fund. This is the asset mix that is detailed in the 2004 business plan of the fund. The policy asset mix becomes the initial asset allocation policy. It is further refined by breaking the bond/equity split down into additional asset classes for further diversification, such as Canadian and foreign equity and also real estate. Ranges are established for each asset class. This ensures that the fund will maintain exposure to each major asset class and limits the discretion of the manager. If market action results in the breach of any of these limits, then discipline of rebalancing is imposed.

The fund has significant investments in equities, including foreign equities, U.S. and non North American. It is broadly diversified by country, industry sector, and company and a significant component that is managed externally. The fund also has an important allocation to real estate, and there are allocations as well to absolute return strategies and private equity.

There are other investment policies that we follow as well. We have policies with respect to the hiring of external managers, the types of strategies we will use. We have limits on the quality of securities and how much of specific types of securities we will hold. There are policies on how much discretion we will allow managers to have in terms of executing transactions. Finally, our mandates have clearly defined benchmarks on which to monitor and measure performance.

The fund is positioned for long-term growth, and this is reflected in an important equity allocation. In 2002-03 equities declined in value, and this caused a loss for the fund, the first loss in the fund's 27-year history. Equities are more volatile than other asset classes such as money market and fixed income. The commitment to equities will therefore produce potentially large swings in income of the fund in the short term.

The Endowment Fund Policy Committee must balance the short-term swings in income with the longer term higher growth of some more volatile asset classes. The loss in 2002-03 certainly illustrates the volatility of income. The following chart may help to illustrate the long-term potential of equity investing.

I will now turn the presentation over to Peter Orcheson, who will speak on the next slides.

Mr. Orcheson: Thanks very much, Doug. The slide you see here illustrates the relative return of equity investments versus bonds. The red line represents the S & P 500 index, and the blue line represents the U.S. government 30-year bond. The most striking point here I'd like to illustrate is that a hundred dollars invested in 1925 in the S & P 500 would net \$171,941 today for a nontaxable investor. The same investment in fixed income would net you only \$6,000.

Now, why is this? Without getting into a theoretical argument about equities over bonds, just imagine yourself. You know, there are probably many people in this room who have their own business or are thinking about starting their own business, and if you're going to take money out of the bank, a GIC or a T-bill, or if you're going to make an investment in an existing business, there's an opportunity cost there. Unless you think that the returns compensate you for what you're giving up on the fixed-income side or on the debt side, you're not going to make that investment.

Now, for larger companies, like in the S & P 500, this capital allocation and reallocation is going on all the time, so the average return on equity for the S & P 500 would be, you know, something in the order of 15 percent versus fixed income, currently probably about 5 percent. So over time equities will outperform.

That being said, you can go through some difficult periods, and we've gone through one recently. You can see from the chart that we've had the dip in the S & P 500 in the recent period. You'll also see some volatility in the earlier period, which is the Great Depression, and we can see some weakness certainly in the '70s as well. The reality is that what the market is willing to pay for earnings in terms of price earnings ratio can fluctuate quite a bit with the business cycle, and the return on the equity in the company can fluctuate a fair bit too. But as long as you feel that the economy is sound such that investment projects, you know, are profitable and as profitable as they have been since 1925, I still think the asset class offers a lot of merit.

7:30

Just getting on to performance, the bar chart here outlines the recent performance of the fund, and it's taken from the 2003-2004 first-quarter update. Note the negative 11 percent return in 2002-2003. It certainly was a difficult period, but you'll also note that in

the first three months of this fiscal year we've had a return of plus 7.1 percent and since the end of June the fund has continued to enjoy strong returns in the stock market and strong returns overall. Like many in the investment business, you know, we expect better returns going forward such that our four-year number of 1.7 percent will continue to look better.

Last, I'd like to highlight just a couple of points on the future of the fund. Firstly, the income volatility of the fund will become, you know, more apparent than it has been in the past because of the focus on more longer term investments such as equities. We're constantly looking at ways to mitigate this volatility, and we have taken such steps, certainly within the asset mix. On the second point, the increase in the future levels of income to the province are going to be, obviously, dependent on the size of the fund itself. This brings the question of spending income now versus retaining it in the fund to grow that income.

With that, I'd like to just turn the presentation back over to Drew Hutton.

The Chair: Well, thank you very much, Minister Melchin, Doug, and Peter, as well as my colleagues on the committee, for the presentation. This concludes the formal portion of our presentation, but I'd like to acknowledge Marie from Mel Knight's office. She really did the lion's share of the work, I know, on our tour today. Is Marie here, by the way? This is the problem: we're sitting blind. There. Would you give us a wave? Thank you very much, Marie. It's greatly appreciated. We did have a terrific day. Thank you for arranging the tours. I'd also like to thank my committee clerk, Karen Sawchuk. Karen, again, thank you very much for the work that you've done, as well as the *Hansard* group, who are recording the proceedings here this evening. We obviously couldn't do this without them.

Now, I turn this over to you. This is your opportunity to ask a question of us. You have an opportunity to ask a question. Don't feel shy at all. Please go up to the mike. Just identify yourself. We're more than happy to hear. As I always say, there are no dumb questions. Please feel free to ask anything about the fund. You've got the Minister of Revenue here. He's also prepared, I'm sure, to deviate from that at any time. Thanks.

Ms Feeney: Hi. My name is Betty Feeney. You mentioned the heritage fund for medical research. Can you indicate how this money is allocated, and are there any other endowments?

Mr. Melchin: Thank you, Betty. There are actually three endowment funds other than the heritage fund in existence today. One is the Alberta Heritage Foundation for Medical Research, that was mentioned previously. There's a fund that's half a billion dollars that was put in two or three years ago towards research for science and engineering purposes. There's also a scholarship fund. That's a fund a little over \$200 million that goes towards providing scholarships for postsecondary education.

Those three funds are all based and invested upon an ability to establish a spending level that would allow for some of the income to be retained in the fund to allow the fund itself to grow, be inflation-proofed, so that the real value of that fund would be retained over time. The rest of the income that would be earned above inflation, simply put, anyway, would be allowed to be spent and was put to other boards.

There is a board in place for medical research that has oversight for the spending of that income. They will put together researchers and projects and direction and policy to govern how medical research grants should be put out, and much of that is done through

the oversight of my colleague, Victor Doerksen, the Minister of Innovation and Science.

But there is a separate board governance for the authorization of the spending. The fund itself would only transfer a portion of its income to that other board to allocate for direct medical research purposes. You talk to the University of Alberta, certainly the universities throughout this province, and many people in the medical industry. It has led to many tremendous research projects being undertaken in this province, highly recognized and known as contributing substantially to medical research. That fund was initially \$300 million. It grew. It's over \$800 million, \$850 million approximately, so it's retained its value over time.

I don't know if there is more detail that you wanted on that, though.

Ms Feeney: I think that's it. Thank you.

Ms Wilson: My name is Carol Wilson. I think it was Debby who mentioned that there's no other fund like this. There is another fund like this. It's called the Alaska heritage fund. It was started at the same time as this one. The Alaska fund is worth \$65 billion, and we have a paltry \$12 billion. I'd like to know why our fund wasn't managed as well as the Alaska fund, and if they're going to do anything about that.

Mr. Melchin: Thank you, Carol. One thing I would like to say. You're right. There are more oil funds in the world. The Norwegians actually have a fund also. We met with a number of the officials from Norway with regard to their fund. Their fund actually is a federal fund being built up because they don't have a pension fund itself. Their fund is actually to provide pension obligations for those retiring in Norway, so it has quite a different purpose.

In Alaska – you're absolutely correct – oil moneys continue to be put into the Alaska fund, and it has grown to the number that you stated, around \$65 billion. I forget the exact number, but it's certainly growing.

In comparison, the heritage fund had a different mandate to begin with than the Alaska fund. When it was originally created, it had four different purposes. There are a number of ways to create and build economic activity in the province, and this fund started off with saying that it should support economic and social projects. There were a number of diversification loans made in the '80s with respect to the heritage fund. There's been quite a bit of investment in some forestry activities, for example. I would say that those loans were made for diversification purposes and not specifically just for an investment purpose.

The province, when Premier Klein came in, said that we would no longer be in the business of being in business and making direct loans to companies, which some of those loans were made to. So those purposes were changed. There were a number of those loans that were bad debts. The heritage fund has one loan left in it from those days. All the rest have been settled. That's the Prince Rupert grain terminal. There's about a \$93 million loan that's still on the books of the heritage fund for the Prince Rupert grain terminal. So there were a number of loans made for diversification. There were also about . . .

Ms Wilson: Excuse me. I'm not concerned about the loans. I want to know why some of the oil revenues that come into this province haven't been put back into this fund. That's why it was set up – wasn't it? – to begin with.

Mr. Melchin: Initially, 30 percent of all the oil and gas revenues were to go into the heritage fund. That's correct. In the early '80s, when the government at the time, still under, I think, Premier Lougheed, who created the fund – when this province saw oil and gas, the national energy program, and a number of things collapse, it changed from 30 percent to 15 percent because the revenue was needed for the government of the day to support health, education, infrastructure, roads and the like, all of the priorities of Albertans.

7:40

And 1986, thereabout, was once again another period of time in Alberta when oil prices, you know, fell off the market, really. Oil was down about \$10 or so. At that time, the government changed the policy so that no further oil and gas revenues would go to the heritage fund and the income would stay and go to general revenues. So those were decisions made back in the 1980s to change the mandate of the fund.

Now, what has happened is quite different. This government in the 1980s incurred a substantial amount of debt. The debt went up to about \$23 billion in the province, and the priority has been to pay off the debt before we start building new assets. I would say that's been the priority we've heard over and over again from Albertans: wanting the debt to be paid. Get rid of the risk and the obligation to outside parties and pay off those debts. That debt has now been reduced from just under \$23 billion down to about 4 and a half billion dollars. So we are now getting back into a position where debts are about eliminated and we can start reconsidering the purpose and growth, potentially, of the fund.

Ms Wilson: Also the royalties were lowered to the oil companies when this government came in, and the price of oil is what now? Thirty dollars a barrel? Do you think maybe you could raise the royalties and put some into this fund?

Mr. Melchin: Those are all policies that could be debated. I can't say that we can get into a debate here because that's not a heritage fund-specific policy to debate with respect to the royalty policy. I'd prefer to not, given the context of the purpose of the meeting, get into a discussion of the royalty. That would be the Energy minister in particular that would have to bring that forward.

The Chair: We've received \$24.4 billion from the fund by carving off the interest for the last number of years. I met with some of the Alaska representatives this past summer, and they may have the fund at the level they do right now, but they're in a pickle with regard to running deficits right now and are losing funds because they're distributing it to their residents. So in some ways you're comparing apples to oranges with regard to the mandate of the fund. We've benefited from the interest from the heritage trust fund so that we wouldn't be running any deficits and debt, whereas Alaska is now running deficits.

Mr. Melchin: I'd also say that a big difference initially about the Alaska fund versus the heritage fund is the heritage fund also put about \$3.5 billion into a variety of capital projects. There are a number of ways to build opportunity for the future. Some are to build financial assets, like what Alaska has done. Another is to build capital assets or infrastructure that paves the way and positions industry to having an opportunity to develop more of the resources and opportunities that we have in Alberta. If you look at the growth and what's happened in Alberta, you can see that many great economic factors have worked for us. By seeing that the right

infrastructure is in place and the right policy is in place, even in the oil and gas sector, that's allowed for billions of dollars to come into these industries and our growth as a province to be, really, one of the highest growths in all of North America.

Mr. Estlin: My name is Fred Estlin, and I recently served on an Alberta government task force. It was called Access to Capital. I have to kind of give a bit of history here – and Greg is grinning a bit there because he's heard this before – but it's all about private equity and what's happening in Alberta. Through this task force we found that Alberta venture capital represents 2.4 percent of the total venture capital invested in Canada, and we perceive ourselves to be strong entrepreneurs. We have 10 percent of the population and 14 percent of the GDP, but only 2.4 percent of the venture capital invested in Canada is invested in Alberta.

Part of what we found there was that in other jurisdictions within Canada and outside Canada there is considerable public money involved in investing in private equities. This comes back again to the Alberta government's very good policy of 1995 of not being in the business of being in business. But there are various ways that public money can be invested through private sources into private equity, which again over time has shown that well-managed private equity returns about 20 percent.

Coupled with this is that we are investing considerable public dollars in public research through our institutions, universities and colleges, and endowments for specific research. We found that way too much of this research is being removed from Alberta to be commercialized. So we're funding the research with public dollars and then not getting the benefit of the diversification to the Alberta economy because of lack of venture capital.

The question would be: has there been consideration to up the private equity percentage that the trust fund and potentially other public moneys in Alberta would then reinvest in the private sector that would help commercialize so much of the very good research that's coming out of our various public institutions?

Mr. Melchin: I'd just like to say this, Fred, with respect to that. I actually have the report that I think they referred to in front of me, and it does talk quite a bit about how do we commercialize some of the great research that we're doing in this province and how do we see that there's access to capital markets. I do concur that creating the right economic environment for attracting capital is critical to the future of this province.

Now, that said, there are a number of things that we are doing to help improve capital questions, specifically with regard to the heritage fund and not just the heritage fund but the other endowment funds too: the scholarship fund, the medical fund, and the ingenuity fund. We have committed to increasing private equities. What's happened is that in the past the heritage fund was all invested in fixed income, and the objective was: how do we maximize long-term returns? So we said that we ought to start transitioning towards a diversified portfolio, balanced both with equities and with bonds.

Now, in that transition there's been quite a bit of diversification into the public equities markets, and more recently, last year, we changed the policy to increase private equity participation up to 5 percent. We're not at that 5 percent yet; we're at 2 percent approximately at this stage. It's a lot harder to place private equity capital than public equities. There's a readily made wide liquid market for public equities. So we do have a number of the private equities. We ourselves won't be making the direct investments in choosing those companies, but we will invest in fund managers, some of which are in Alberta also so that some of that private equity

capital is actually being placed in Alberta under private equities as an objective.

We are going to continue to look at the opportunity. It's more sophisticated. You need the resources of research, expertise of manpower, and quite a bit more sophistication to handle and manage that asset class. So in some respects it's needing a little bit of transition time to both bring that expertise inside and with outside fund managers.

In addition, I would like to tell you some follow-up to this report that is happening. Recently I've been working with the Minister of Economic Development and the Minister of Innovation and Science, Mark Norris and Victor Doerksen, with respect to a couple of those key questions. One was research and development tax credits. Another one was access to capital markets, venture capital in particular.

7:50

We have engaged some work both from the University of Calgary and the University of Alberta, a couple of individuals to do some baseline research on what has been done in other jurisdictions and to get both a theoretical and practical database of information on those questions so that when we do start addressing capital, we've got the right baseline information to talk from. This is a short-term project. It's not going to be one that we'll be studying forever, so I will want to tell you that we are working actively on that topic. I don't have something to report to you today, and we do want to address how we can ensure that this an attractive place to invest.

I'll tell you from being in New York and talking to a number of our fund managers in New York that when you ask the question about Canada – and we've got to promote Alberta because we do have some different structures than the rest of Canada, and we've got to tell our Alberta advantage story – invariably they say: okay; tell me about Canada; what do you think about the opportunities of investing money in Canada? They say a lot of great things about Canada. They say a lot of things about some of our industries, such as forestry or oil and gas and such. So they look at some of the niche. It's a small market, everybody knows, in the world in comparison, certainly, to the United States. But invariably they'll say that with our tax structures in Canada our governments take too much money and that we get better returns leaving our money in the United States.

I'm not trying to tell you what that means other than that that's the perspective of the large institutional fund managers in New York. We have to be competitive with our U.S. neighbours to see that it is attractive to them to invest their money in Canada, that we can create more of the opportunity. So some of it is even a broad fiscal policy at which we have been doing substantially better than all the other provinces in the country. We've got to promote the Alberta advantage abroad. We've got to tell our story better, not just some of the niche markets but some of the very broad positive things that are happening in Alberta. So that will also be part of the approach in marketing ourselves to the investment community abroad.

Mr. VanderBurg: One of the things that I've done as a private member is brought together a paper that was predominantly driven by small- and medium-sized companies that were in the business of mining for diamonds and gold in Canada. We had looked at and we had talked about this venture capital. We'd also talked about very high-risk capital. How do they get that? How do they get it in other provinces? Why do we have an abundance of geologists and people with mining equipment working all over Canada except in Alberta?

So we drafted a paper. It took us about six months. Not 5 cents of government money in it, all private research. It came down to a

couple of things. One thing stood out that I brought to the Revenue minister and the Minister of Energy and to the Minister of Finance: all the other provinces had an opportunity for provincial tax credits through flow-through shares or super flow-through shares. So if you invested a dollar in the XYZ gold company, you would get in some provinces 15 cents on a provincial tax credit, and I think Quebec was as high as 43 cents. There are different ways to create investment capital. I think that through an opportunity of flow-through shares, which now the government of Canada has adopted – there's a federal flow-through share that's available. I think that maybe the province of Alberta could do that.

So I have a paper in front of these ministers that gives us some information on how we can think different. I think that's one of the things that the Premier has taught us. I won't call us rookies anymore, but those of us who came in 2001 think different. I do see some opportunities for creating, especially in those high-risk markets, a better environment for investment here in Alberta. So I'm awaiting a positive report back from these ministers.

Mr. Whittaker: Good evening. My name is Dale Whittaker, and I'm really glad to see the minister and our MLAs up here representing the heritage savings trust fund. I was looking at your stock portfolio. It looks like mine: buy high, sell low. Not all of it, but there are a number of them.

But, anyway, I guess I was thinking more of the money that we have to invest, and I was wondering why we're not able to put more into our own tar sands projects, to invest our money into them, where we get the return out of what we're doing in processing up there. It's maybe like the pipeline, the Northwest Territories pipeline that's going to happen. Why can't we own part of that? If we invest more into our Canadian businesses instead of investing into different equities. I look at some of them, you know, a lot of them overseas groups and different ones, and quite a few of them are down a lot from what I see they paid, which again looks like mine. I guess to invest more into Alberta industries.

The power situation. You know, why can't we put more of our money into it and have a better return out of it instead of integrating losses into the high-tech things and things of that nature?

Anyway, those are just my thoughts. Thanks.

The Chair: Thank you very much, Dale. I think the main thing is that our mandate is the prudent person rule right now, but I think the minister addressed some of this as did George with his little lobby there with regard to having a look at private investors and high-risk investments.

Mr. Henderson: Mr. Chairman, I'm Jim Henderson, president of Grande Prairie Regional College. I guess my comments may not be surprising from an educator, but I'm also a chartered accountant, and one of the things that I've often been critical of in our profession is the inadequacies of financial reporting in some ways. To give an example, in education I can probably make a great bottom line, make a great profit, if I just stop serving the learners. To me the bottom line has to be the number of learners that we have served in the industry, not how many dollars and cents we have on the bottom line.

There is ample evidence that investment in education, particularly postsecondary education, results in a better quality of life, healthier citizens, lower rates of incarceration, the types of things that I think should also be one of the bottom lines we're targeting with. While I applaud the fact that we've got scholarships coming through the heritage fund, I also recognize that here in Alberta, where we have so many opportunities, this past year we have had position layoffs,

program closures, suspensions, et cetera, across the province. It strikes me that for a province that's trying to invest in our future, we're missing out on an opportunity by, in fact, not being able to educate our learners as quickly as others have.

So I guess my question is: would the heritage fund consider investment in areas such as postsecondary education to make sure we can in fact take every opportunity from the Alberta advantage?

The Chair: Well, Jim, we had a caucus retreat this fall and then a cabinet retreat, and the number one issue was education, primary and postsecondary education. As far as investing in it, we have. I guess it just depends, as you said, on how you look at the bottom lines. I go back to the \$24.4 billion that we have received from the heritage trust fund. That has gone into general revenue, therefore can be seen to be going into education. We just had the Commission on Learning deliver to us on October 10, and the Minister of Learning has said that he will have a response within six to eight weeks. We've had discussions with regard to our universities and our postsecondary institutions, and it is the best investment we can make. I think I speak for all my colleagues when I say that, that it truly is the best investment we can be making. There's going to be a need out there as well.

Does anybody want to supplement that?

Mr. Melchin: Jim, nice outfit. He had a golf tournament here. Can you believe this? An indoor golf tournament. None of us got to participate today. We're all envious that they had a great indoor golf tournament here at Grande Prairie college. We'll be back for next year's, I guess, then.

8:00

To a fellow CA, Jim, I would like to say this. It is truly setting priorities. It is all about that. You know, it's all about allocating a priority of scarcity of resources. The health and education budgets of K to 12 and postsecondary comprise close to two-thirds of the provincial budget. Really, the heritage fund income is all going to general revenues to support the priorities; therefore, health and education. The question that sometimes people are complaining about with the heritage fund as an asset is: why aren't you retaining more of it inside the asset? But, clearly, what we've been doing is directing it towards high-priority programs and delivery that you've specifically mentioned now.

As to what more can you do, we'd be delighted to talk about that in a venue other than just the specific heritage fund committee, and that's part of the good challenges we have as a government: how do you see that we provide the best of opportunities for our children to get all the education they need? It's vital.

Mr. Bonner: Jim, last September I had the opportunity with a number of colleagues from the Legislature to tour the British Isles. One of our stops was in Ireland, who had provided free education from the '60s on. During our meetings with a Senator who had also been a Member of Parliament, I asked him what influence their education policies of the '60s had on their economic success of today. He indicated that if they had not had that investment in education at that time, they would not have been prepared with a highly educated workforce when their technological age started. So I along with many of my colleagues continue to feel that investment

in education is one of the best investments that we can make, and we certainly would like to see more investment into that area.

Thank you.

The Chair: Well, if there are no further questions, I'd like to say thank you to you all for taking the time to come out and hear about one of our greatest assets, the heritage trust fund. I'd also again like to thank the minister and his staff for coming out and providing their presentation. If you would like to see the transcript from this meeting, you can just log on to the Assembly web site. It's www.assembly.ab.ca.

With that, unless Mel wants to say a few words, we'll call this meeting adjourned. Do you want to say anything, Mel?

Mr. Knight: Well, just to wrap up, Drew. Thank you very much. Again, I certainly do appreciate your participation in the meeting. The questions that were brought forward, of course, are duly recorded, and we certainly will in deliberations in the committee and elsewhere take your questions to heart. You can be assured that there will be discussion around the questions that came forward.

Just to reiterate what Drew has said, we feel extremely proud of the heritage trust fund. It has been demonstrated over the years to be extremely useful to Albertans. Nearly \$25 billion has gone into programs and infrastructure, general revenue items that your government deals with on a yearly basis, and that \$25 billion has made a tremendous difference to the province of Alberta and to our ability to prepare ourselves over the years for what has been a tremendous amount of growth.

You don't have to go very far in and around Grande Prairie, the county and the municipalities that are around northwestern Alberta, to see the results of that growth, and certainly without the investment that was available from the heritage trust fund, I would have to tell you that we would have been in a much different situation today. Even things that we now almost consider, you know, a done thing – the twinning of highway 43 comes to mind as just a huge plus to northwestern Alberta. The movement of goods and services on the corridor has been extremely beneficial to us.

You have to think of this money as part of the overall pool of money that's allowed Alberta to be prepared, and certainly as we move ahead, we will continue to manage the fund in a way that will allow us to be prepared for future expansion, which we know is on the way.

So again I want to thank my colleagues. I think we enjoyed the day. I want to certainly thank the college here for their generous hospitality, and I do want to thank everybody that came out and participated.

Finally, hon. Minister Melchin, you have again done an excellent job and fielded the questions in a very professional manner, and we thank you for your participation.

Mr. Melchin: Thank you.

The Chair: Well, that will conclude the meeting, and there is coffee outside if you want to have a little more informal chat.

Thank you.

[The committee adjourned at 8:06 p.m.]

