

ALBERTA HERITAGE SAVINGS TRUST FUND

Financial Statements

YEAR ENDED MARCH 31, 2003

Auditor's Report	98
Balance Sheet	99
Statement of Operations	99
Statement of Changes in Financial Position	100
Notes to the Financial Statements	101
Schedules to the Financial Statements	
A Schedule of Investments in Fixed Income Securities	112
B Schedule of Investments in Canadian Equities	113
C Schedule of Investments in United States Equities	114
D Schedule of Investments in Non-North American Equities	115
E Schedule of Investment Returns	116

AUDITOR'S REPORT



To the Minister of Revenue

I have audited the balance sheet of the Alberta Heritage Savings Trust Fund as at March 31, 2003 and the statements of operations and changes in financial position for the year then ended. These financial statements are the responsibility of the Fund's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with Canadian generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In my opinion, these financial statements present fairly, in all material respects, the financial position of the Fund as at March 31, 2003 and the results of its operations and the changes in its financial position for the year then ended in accordance with Canadian generally accepted accounting principles.

[original signed]

Edmonton, Alberta
May 22, 2003

FCA
Auditor General

ALBERTA HERITAGE SAVINGS TRUST FUND

BALANCE SHEET

March 31, 2003 (thousands)

	2003	2002
Assets		
Portfolio investments (Note 3)	\$ 11,346,295	\$ 12,501,716
Accrued investment income	16,145	20,617
Receivable from sale of investments	-	16,163
Administration expense receivable	2	7
	<u>\$ 11,362,442</u>	<u>\$ 12,538,503</u>
Liabilities and Fund Equity		
Liabilities		
Liabilities for investment purchases	\$ -	\$ 269,287
Due to the General Revenue Fund	-	12,897
	-	<u>282,184</u>
Fund equity (Note 6)	11,362,442	12,256,319
	<u>\$ 11,362,442</u>	<u>\$ 12,538,503</u>

STATEMENT OF OPERATIONS

March 31, 2003 (thousands)

	Budget	2003 Actual	2002 Actual
Net income (loss) (Note 7)	\$ 590,500	\$ (893,877)	\$ 205,772
Transfers to the General Revenue Fund (Note 6)	590,500	-	205,772
Net change in fund equity (Note 6)	<u>\$ -</u>	(893,877)	-
Fund equity at beginning of year		12,256,319	12,256,319
Fund equity at end of year		<u>\$ 11,362,442</u>	<u>\$ 12,256,319</u>

The accompanying notes and schedules are part of these financial statements.

ALBERTA HERITAGE SAVINGS TRUST FUND

STATEMENT OF CHANGES IN FINANCIAL POSITION

Year Ended March 31, 2003 (*thousands*)

	2003	2002
Operating transactions		
Net income (loss)	\$ (893,877)	\$ 205,772
Non-cash items included in net income	58,636	(56,841)
	(835,241)	148,931
Decrease in accounts receivable	20,640	82,423
Increase (decrease) in accounts payable	(269,287)	124,272
Cash provided by (applied to) operating transactions	(1,083,888)	355,626
Investing transactions		
Proceeds from disposals, repayments and redemptions of investments	5,524,009	12,881,740
Purchase of investments	(4,228,530)	(13,338,370)
Cash provided by (applied to) investing transactions	1,295,479	(456,630)
Transfers		
Transfers to the General Revenue Fund	-	(205,772)
Increase (decrease) in amounts due to the General Revenue Fund	(12,897)	94,721
Cash applied to transfers	(12,897)	(111,051)
Increase (decrease) in cash	198,694	(212,055)
Cash at beginning of year	51,820	263,875
Cash at end of year	\$ 250,514	\$ 51,820
Consisting of Deposits in the Consolidated Cash Investment Trust Fund (Note 3)	\$ 250,514	\$ 51,820

The accompanying notes and schedules are part of these financial statements.

ALBERTA HERITAGE SAVINGS TRUST FUND

NOTES TO THE FINANCIAL STATEMENTS

March 31, 2003

NOTE 1 AUTHORITY AND MISSION

The Alberta Heritage Savings Trust Fund operates under the authority of the *Alberta Heritage Savings Trust Fund Act* (the Act), Chapter A-23, Revised Statutes of Alberta 2000, as amended.

The preamble to the Act describes the mission of the Fund as follows:

“To provide prudent stewardship of the savings from Alberta’s non-renewable resources by providing the greatest financial returns on those savings for current and future generations of Albertans.”

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND REPORTING PRACTICES

These financial statements are prepared in accordance with generally accepted accounting principles.

The accounting policies of significance to the Fund are as follows:

a) Portfolio investments

Fixed-income securities, mortgages, equities, real estate investments and absolute return strategy investments held directly by the Fund or by pooled investment funds are recorded at cost. Cost includes the amount of applicable amortization of discount or premium using the straight-line method over the life of the investments.

Investments in loans are recorded at cost less any and allowance for credit loss. Where there is no longer reasonable assurance of timely collection of the full amount of principal and interest of a loan, a specific provision for credit loss is made and the carrying amount of the loan is reduced to its estimated realizable amount.

Investments are recorded as of the trade date.

The cost of disposals is determined on the average cost basis.

Where there has been a loss in value of an investment in fixed-income securities, mortgages, equities, real estate and absolute return strategies that is other than a temporary decline, the investment is written down to recognize the loss. The written down value is deemed to be the new cost.

b) Investment Income

Investment income is recorded on the accrual basis where there is reasonable assurance as to its measurement and collectability. When a loan becomes impaired, recognition of interest income in accordance with the terms of the original loan agreement ceases. Any subsequent payments received on an impaired loan are applied to reduce the loan's book value.

Gains and losses arising as a result of disposals of investments are included in the determination of investment income. Income and expense from derivative contracts are included in investment income.

ALBERTA HERITAGE SAVINGS TRUST FUND

NOTE 2 (continued)**c) Foreign Currency**

Foreign currency transactions are translated into Canadian dollars using average rates of exchange, except for hedged foreign currency transactions which are translated at rates of exchange established by the terms of the forward exchange contracts. Exchange differences on unhedged transactions are included in the determination of investment income.

d) Investment Valuation

Fair value is the amount of consideration agreed upon in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act. Fair values of investments held either directly by the Fund or by pooled investment funds are determined as follows:

- (i) Public fixed-income securities and equities are valued at the period-end closing sale price, or the average of the latest bid and ask prices quoted by an independent securities valuation company.
- (ii) Mortgages, provincial corporation debentures and private fixed-income securities are valued based on the net present value of future cash flows. These cash flows are discounted using appropriate interest rate premiums over similar Government of Canada benchmark bonds trading in the market.
- (iii) The fair value of private equities is estimated by management.
- (iv) Real estate investments are reported at their most recent appraised value, net of any liabilities against the real property. Real estate properties are appraised annually by qualified external real estate appraisers.
- (v) The fair value of Absolute Return Strategy Pool investments are estimated by external managers.
- (vi) The fair value of loans is estimated by management based on the present value of discounted cash flows.
- (vii) The fair value of deposits, receivables, accrued interest and payables are estimated to approximate their book values.
- (viii) The fair value of investments and any other assets and liabilities denominated in a foreign currency are translated at the year-end exchange rate.

e) Valuation of Derivative Contracts

Derivative contracts include equity and bond index swaps, interest rate swaps, forward foreign exchange contracts, equity index futures contracts and cross-currency interest rate swaps. As disclosed in Note 4, the value of derivative contracts is included in the fair value of pooled investment funds. The estimated amount receivable or payable from derivative contracts at the reporting date is determined by the following methods:

- (i) Equity and bond index swaps are valued based on changes in the appropriate market based index net of accrued floating rate interest.
- (ii) Interest rate swaps and cross-currency interest rate swaps are valued based on discounted cash flows using current market yields. The fair value of cross-currency interest rate swaps was not available in prior years. Consequently, no amount is provided for comparative purposes.
- (iii) Forward foreign exchange contracts and equity index futures contracts are based on quoted market prices.

ALBERTA HERITAGE SAVINGS TRUST FUND

NOTE 3 PORTFOLIO INVESTMENTS*(thousands)*

	2003			2002		
	Cost	Fair Value	%	Cost	Fair Value	%
Fixed income securities (Schedule A)						
Deposit in the Consolidated Cash Investment Trust Fund (a)	\$ 250,514	\$ 250,514	2.3	\$ 51,820	\$ 51,820	0.4
Canadian Dollar Public Bond Pool (b)	3,012,610	2,996,258	27.1	3,372,717	3,291,655	26.0
Bonds, notes & short-term paper, directly held (c)	24,515	25,470	0.2	1,440,792	1,445,674	11.4
Private Mortgage Pool (d)	432,916	429,077	3.9	404,966	389,516	3.1
Provincial corporation debentures, directly held (e)	100,037	158,018	1.4	104,622	165,178	1.3
Loans, directly held (f)	97,359	97,359	0.9	97,359	97,359	0.8
	3,917,951	3,956,696	35.8	5,472,276	5,441,202	43.0
Canadian equities (Schedule B)						
Public equities:						
Domestic Passive Equity Pooled Fund (g)	907,115	1,050,459	9.5	886,167	1,097,763	8.7
External Managers Canadian Large Cap Equity Pool (h)	672,938	638,043	5.8	380,554	406,097	3.2
Canadian Pooled Equity Fund (i)	647,209	596,641	5.4	931,972	945,662	7.5
External Managers Canadian Small Cap Equity Pool (j)	72,655	80,751	0.7	67,471	88,027	0.7
Public equities, directly held	-	-	-	1,526	2,716	-
	2,299,917	2,365,894	21.4	2,267,690	2,540,265	20.1
Private Equity Pools (k)	93,047	83,160	0.7	86,069	83,047	0.6
	2,392,964	2,449,054	22.1	2,353,759	2,623,312	20.7
United States equities (Schedule C)						
Public equities:						
External Managers US Large Cap Equity Pool (l)	894,835	753,677	6.8	891,430	879,969	6.9
External Manager US Passive Equity Pool (m)	505,192	462,155	4.2	1,104,863	994,944	7.9
S&P 500 Index Fund (n)	443,426	429,631	3.9	-	-	-
External Manager US Small/Mid Cap Equity Pool (o)	111,304	106,645	0.9	102,321	122,653	1.0
United States Pooled Equity Fund	255	105	-	803	640	-
	1,955,012	1,752,213	15.8	2,099,417	1,998,206	15.8
Private Equity Pool (k)	7,155	6,839	0.1	-	-	-
	1,962,167	1,759,052	15.9	2,099,417	1,998,206	15.8
Non-North American equities (Schedule D)						
Public equities:						
External Managers EAFE Core Equity Pool (p)	1,054,819	876,238	7.9	1,013,353	994,087	7.8
External Managers EAFE Plus Equity Pool (p)	518,725	437,568	3.9	488,475	499,732	4.0
External Manager EAFE Passive Equity Pool (q)	411,772	427,300	3.9	505,888	507,434	4.0
EAFE Structured Equity Pool	-	-	-	803	818	-
	1,985,316	1,741,106	15.7	2,008,519	2,002,071	15.8
Real estate						
Private Real Estate Pool (r)	804,855	869,948	7.9	567,745	594,463	4.7
Absolute Return Strategies						
Absolute Return Strategy Pool (s)	283,042	282,967	2.6	-	-	-
Total equities, real estate and absolute return strategies	7,428,344	7,102,127	64.2	7,029,440	7,218,052	57.0
Total investments (t)	\$ 11,346,295	\$ 11,058,823	100.0	\$ 12,501,716	\$ 12,659,254	100.0

ALBERTA HERITAGE SAVINGS TRUST FUND

NOTE 3 (continued)

The majority of the Fund's investments are held in pooled investment funds established and administered by Alberta Revenue. Pooled investment funds have a market based unit value that is used to allocate income to participants and to value purchases and sales of pool units. As at March 31, 2003, the Fund's percentage ownership, at market, in pooled investment funds is as follows:

	% Ownership	
	2003	2002
Internally Managed Investment Pools		
Canadian Dollar Public Bond Pool	38.1	36.9
Canadian Pooled Equity Fund	55.0	47.0
Domestic Passive Equity Pooled Fund	47.7	41.3
EAFE Structured Equity Pool	-	0.2
Foreign Private Equity Pool (02)	43.8	-
Private Equity Pool	13.6	13.6
Private Equity Pool (98)	100.0	100.0
Private Equity Pool (02)	62.1	-
Private Mortgage Pool	42.8	43.2
Private Real Estate Pool	42.8	36.3
S&P 500 Index Fund	87.2	-
United States Pooled Equity Fund	18.0	18.0
Externally Managed Investment Pools		
Absolute Return Strategy Pool	88.2	-
Canadian Large Cap Equity Pool	25.5	18.8
Canadian Small Cap Equity Pool	18.6	18.7
EAFE Core Equity Pool	35.6	36.2
EAFE Passive Equity Pool	74.0	56.6
EAFE Plus Equity Pool	37.1	35.4
US Large Cap Equity Pool	41.6	37.0
US Passive Equity Pool	73.3	68.9
US Small/Mid Cap Equity Pool	26.9	30.2

- a) The Consolidated Cash Investment Trust Fund is managed with the objective of providing competitive interest income to depositors while maintaining appropriate security and liquidity of depositors' capital. The portfolio is comprised of high-quality short-term and mid-term fixed-income securities with a maximum term-to-maturity of three years. As at March 31, 2003, securities held by the Fund have an average effective market yield of 3.23% per annum (2002: 2.57% per annum).
- b) The Canadian Dollar Public Bond Pool is managed with the objective of providing above average returns compared to the total return of the Scotia Capital Universe Bond Index over a four-year period while maintaining adequate security and liquidity of participants' capital. The excess return is achieved through management of portfolio duration and sector rotation. The portfolio is comprised of high quality Canadian fixed-income instruments and debt related derivatives. As at March 31, 2003, securities held by the Pool have an average effective market yield of 5.41% per annum (2002: 5.80% per annum) and the following term structure based on principal amount: under 1 year: 2% (2002: 7%); 1 to 5 years: 37% (2002: 34%); 5 to 10 years: 31% (2002: 31%); 10 to 20 years: 11% (2002: 10%); over 20 years: 19% (2002: 18%).

ALBERTA HERITAGE SAVINGS TRUST FUND

NOTE 3 (continued)

- c) As at March 31, 2003, fixed-income securities held directly by the Fund have an average effective market yield of 4.36% per annum (2002: 4.02% per annum). As at March 31, 2003, fixed-income securities have the following term structure based on principal amount: under 1 year: Nil% (2002: 91%); 1 to 5 years: 100% (2002: 9%).
- d) The Private Mortgage Pool is managed with the objective of providing investment returns higher than attainable from the Scotia Capital Universe Bond Index over a four-year period or longer. The portfolio is comprised primarily of high quality commercial mortgage loans (94.6%) and provincial bond residuals (5.4%). To limit investment risk, mortgage loans are restricted to first mortgage loans, diversified by property usage and geographic location, and include a small portion of NHA insured loans. As at March 31, 2003, securities held by the Pool have an average effective market yield of 6.43% per annum (2002: 7.01% per annum) and the following term structure based on principal amount: under 1 year: 5% (2002: 10%); 1 to 5 years: 31% (2002: 21%); 5 to 10 years: 20% (2002: 23%); 10 to 20 years: 24% (2002: 26%); and over 20 years: 20% (2002: 20%).
- e) As at March 31, 2003, Provincial corporation debentures have an average effective market yield of 7.83% per annum (2002: 8.35% per annum) and the following term structure based on principal amounts: 5 to 10 years: 100%.
- f) Investment in loans are recorded at cost. The fair value of loans is estimated by management based on the present value of discounted cash flows. As at March 31, 2003, investment in loans, at cost, include the Ridley Grain loan amounting to \$91,245,000 (2002: \$91,245,000) and the Vencap loan amounting to \$6,114,000 (2001: \$6,114,000).
- Under the terms of the loan to Ridley Grain, 11% Participating First Mortgage Bonds due July 31, 2015, interest is compounded semi-annually and payable annually to the extent of available cash flow and any shortfall is to be deferred and capitalized. The principal of \$91,245,000 and deferred interest is repayable on or before July 31, 2015. Deferred interest at March 31, 2003 amounted to \$76,189,320 (2002: \$60,049,081). Grain throughput volumes are the main determinant of profitability of the grain terminal and the value of the loan to the Fund. Due to the uncertainty of forecasting the grain throughput volumes, income from the participating bonds is recognized when it is measurable and collectable.
 - The principal amount of the Vencap loan, amounting to \$52,588,000, is due July 2046 and bears no interest. Amortization ceased being recorded on the loan from December 31, 2000 onward.
- g) The Domestic Passive Equity Pooled Fund is managed on a passive approach with the objective of providing investment returns comparable to the S&P/TSX Index. A portion of the portfolio is comprised of both publicly traded Canadian equities and structured investments replicating the S&P/TSX 100 Index and the S&P/TSX 60 Index. The other portion of the portfolio fully replicates the S&P/TSX. The Pool's investment in units of the Floating Rate Note Pool (FRNP) are used as the underlying securities to support the index swaps of the pool. FRNP is managed with the objective of generating floating rate income needed for the swap obligations in respect of structured investments in foreign equities, domestic equities and domestic bonds. Through the use of interest rate swaps, FRNP provides investment opportunities in high quality floating-rate instruments with remaining term-to-maturity of ten years or less.

ALBERTA HERITAGE SAVINGS TRUST FUND

NOTE 3 (continued)

- h)** The Canadian Large Cap Equity Pool consists of multiple portfolios of publicly traded Canadian equities. Each portfolio is actively managed by an external manager with expertise in the Canadian large cap equity market. The performance objective is to provide returns higher than the total return of the S&P/TSX Index over a four-year period. Return volatility is reduced through multiple manager investment style and market capitalization focus.
- i)** The Canadian Pooled Equity Fund is managed with the objective of providing competitive returns comparable to the total return of the S&P/TSX Index while maintaining maximum preservation of participants' capital. The portfolio is comprised of publicly traded equities in Canadian corporations. Risk is reduced by prudent security selection and sector rotation.
- j)** The Canadian Small Cap Equity Pool consists of multiple portfolios of publicly traded Canadian equities with market capitalization of .15% of the S&P/TSX Index total market capitalization at time of purchase. Each portfolio is actively managed by an external manager with expertise in the Canadian small cap equity market. The performance objective is to provide returns higher than the total return of the S&P/TSX Index over a four-year period and returns higher than the Nesbitt Burns Small Cap Index over shorter time periods. Return volatility is reduced through multiple manager investment style and small capitalization focus.
- k)** Private Equity Pools are managed with the objective of providing investment returns higher than the Consumer Price Index (CPI) plus 8.0%. The Private Equity Portfolio consists of the Private Equity Pool, PEP98, PEP02 and the Foreign Private Equity Pool 2002. Private equity investments are held in institutionally sponsored private equity pools. Risk is reduced by avoiding direct investments in private companies and by limiting holdings in any single pool.
- l)** The US Large Cap Equity Pool consists of multiple portfolios of publicly traded United States equities. Each portfolio is actively managed by an external manager with expertise in the US large cap equity market. The performance objective is to provide returns higher than the total return of the Standard & Poor's (S&P) 500 index over a four-year period. Return volatility is reduced through multiple manager investment style and large capitalization focus.
- m)** Publicly traded US equities held in the externally managed US Passive Equity Pool replicate the Standard & Poor's (S&P) 500 index. The performance objective is to provide returns comparable to the total return of the S&P 500 index over a four-year period.
- n)** Publicly traded US equities held in the S&P 500 Index Fund replicate the Standard & Poor's (S&P) 500 index. The performance objective is to provide returns comparable to the total return of the S&P 500 index over a four-year period. The Pool's investment in units of the Floating Rate Note Pool (FRNP) are used as the underlying securities to support the index swaps of the pool (see Note 3g).

ALBERTA HERITAGE SAVINGS TRUST FUND

NOTE 3 (continued)

- o)** The US Small/Mid Cap Equity Pool consists of one portfolio of publicly traded United States equities. The portfolio is actively managed by an external manager with expertise in the small cap and mid cap US equity market. The performance objective is to provide returns higher than the total return of the Russell 2500 index over a four-year period.
- p)** The Europe, Australasia and Far East (EAFE) Core and Plus Equity Pools consist of multiple portfolios of publicly traded non-North American equities. EAFE Core portfolios are actively managed by external managers with European and Pacific Basin mandates. EAFE core managers have constraints on foreign currency management and deviations from the MSCI EAFE index asset mix by country. The EAFE Plus portfolios are actively managed by external managers with less constraints on country allocation, stock selection, currency management and investments in emerging markets. The performance objective is to provide returns higher than the total return of the Morgan Stanley Capital International (MSCI) EAFE index over a four-year period.
- q)** The externally managed EAFE Passive Equity Pool consists of one portfolio of non-North American publicly traded equities that replicate the MSCI EAFE index. The performance objective is to provide returns comparable to the total return of the MSCI EAFE index over a four-year period.
- r)** The Private Real Estate Pool is managed with the objective of providing investment returns higher than the Consumer Price Index plus 5%. Real estate is held through intermediary companies which have issued to the Pool, common shares and participating debentures secured by a charge on real estate. Risk is reduced by investing in properties that provide diversification by geographic location, by property type and by tenancy. As real estate returns are positively correlated to inflation and negatively correlated to returns from fixed income securities and equities, the Pool provides diversification from the securities market with opportunities for high return.
- s)** The Absolute Return Strategy Pool is managed with the objective of providing investment returns higher than the Consumer Price Index (CPI) plus 6%. The Pool uses external managers who employ various investment strategies. These strategies are expected to produce absolute positive investment returns with lower volatility.
- t)** Where there has been a loss in value of an investment that is other than a temporary decline, the cost of the investment is written down to recognize the loss (see Note 2 (a)). Where the fair value remains less than cost, after recording a writedown, it is management's best judgement that the decline in value is caused by short term market trends and are temporary in nature.

ALBERTA HERITAGE SAVINGS TRUST FUND

NOTE 4 DERIVATIVE CONTRACTS

Derivative contracts are financial contracts, the value of which is derived from the value of underlying assets, indices, interest rates or currency rates. The Fund uses derivative contracts held indirectly through pooled investment funds to enhance return, manage exposure to interest rate risk and foreign currency risk and for asset mix management purposes. The notional value of a derivative contract represents the amount to which a rate or price is applied in order to calculate the exchange of cash flows.

- (i) A swap is a contractual agreement between two counter-parties to exchange a series of cash flows based on a notional amount. An equity or bond index swap involves the exchange of a floating interest rate cash flow for one based on the performance of a market index. For interest rate swaps, parties generally exchange fixed and floating rate interest cash flows based on a notional amount. Cross-currency interest rate swaps are contractual obligations in which the principal amounts of Canadian fixed-income securities denominated in foreign currency are exchanged for Canadian currency amounts both initially and at maturity. Over the term of the cross-currency swap, counter-parties exchange fixed to fixed and fixed to floating interest rate cash flows in the swapped currencies. There are underlying securities supporting all swaps. Leveraging is not allowed.
- (ii) Forward foreign exchange contracts are contractual agreements to exchange specified currencies at an agreed upon exchange rate and on an agreed settlement date in the future.
- (iii) An equities index futures contract is an agreement to receive or pay cash based on changes in the level of the specified stock index.

The following is a summary of the Fund's proportionate share of the notional amount and fair value of derivative contracts held by pooled funds at March 31, 2003.

(thousands)

	Maturity			Notional Amount	2003		2002	
	Under 1 Year	1 to 3 Years	Over 3 Years		Fair Value (a)	Notional Amount	Fair Value (a)	
Equity index swap contracts	91%	9%	-	\$ 575,028	\$ (13,298)	\$ 510,859	\$ 7,733	
Bond index swap contracts	100%	-	-	52,107	(173)	55,553	(491)	
Forward foreign exchange contracts	100%	-	-	616,346	21,069	260,664	182	
Interest rate swap contracts	33%	64%	3%	404,230	(13,765)	230,634	(8,479)	
Equity index futures contracts	100%	-	-	13,754	421	-	-	
Cross-currency interest rate swaps	21%	16%	63%	275,384	(52,399)	380,982	(b)	
				\$1,936,849	\$ (58,145)	\$1,438,692	\$ (1,055)	

(a) The method of determining the fair value of derivative contracts is described in note 2 (e).

(b) Comparative figures at March 31, 2002 are not provided as the fair value of cross-currency swaps was not available in prior years.

ALBERTA HERITAGE SAVINGS TRUST FUND

NOTE 5 INVESTMENT RISK MANAGEMENT

Income and financial returns of the Fund are exposed to credit risk and price risk. Credit risk relates to the possibility that a loss may occur from the failure of another party to perform according to the terms of a contract. Price risk is comprised of currency risk, interest rate risk and market risk. Currency risk relates to the possibility that the investments will change in value due to future fluctuations in foreign exchange rates. Interest rate risk relates to the possibility that the investments will change in value due to future fluctuations in market interest rates. Market risk relates to the possibility that the investments will change in value due to future fluctuations in market prices.

The Standing Committee on the Alberta Heritage Savings Trust Fund reviews and approves the business plan of the Fund. In order to earn an optimal financial return at an acceptable level of risk, the 2002-2003 business plan proposes the following asset mix policy for the Endowment Portfolio.

Fixed income securities	25% to 45%
Equities	75% to 55%

Risk is reduced through asset class diversification, diversification within each asset class, quality and duration constraints on fixed-income instruments, and restrictions on amounts exposed to countries designated as emerging markets. Controls are in place respecting the use of derivatives (see Note 4). Forward foreign exchange contracts may be used to manage currency exposure in connection with securities purchased in foreign currency (see Note 4).

ALBERTA HERITAGE SAVINGS TRUST FUND

NOTE 6 FUND EQUITY

Section 8 (2) of the *Alberta Heritage Savings Trust Fund Act (the Act)* states that the net income of the Heritage Fund less any amount retained in the Fund to maintain its value shall be transferred to the General Revenue Fund annually in a manner determined by the Minister of Revenue.

Section 11(5) of the Act states that for fiscal years subsequent to 1999 and until the accumulated debt is eliminated in accordance with the *Fiscal Responsibility Act*, the Minister of Revenue is not required to retain any income in the Heritage Fund to maintain its value, but may retain such amounts as the Minister of Revenue considers advisable.

NOTE 7 NET INCOME (LOSS)

(thousands)

	2003	2002
Deposit and fixed-income securities	\$ 286,427	\$ 444,884
Canadian equities	(240,581)	(54,112)
United States equities	(591,448)	(8,065)
Non-North American equities	(390,325)	(213,481)
Real estate	39,265	38,001
Absolute Return Strategies	4,563	-
Investment income (loss)	(892,099)	207,227
Direct administrative expenses (Note 8)	(1,778)	(1,455)
Net income (loss)	\$ (893,877)	\$ 205,772

Investment income (loss) is comprised of interest, dividends, amortization of discount and premiums, swap income, security lending income and realized gains and losses, net of write-downs, on investments. The Fund's share of income (loss) earned from externally and internally managed investment pools is net of administrative expenses incurred by the pools (see Note 8).

The investment loss for the year ended March 31, 2003 includes writedowns totalling \$668,553,000 (March 31, 2002: \$269,283,000).

ALBERTA HERITAGE SAVINGS TRUST FUND

NOTE 8 ADMINISTRATIVE EXPENSES

Administrative expense includes investment management, cash management, safekeeping costs and other expenses charged on a cost-recovery basis directly from Alberta Revenue. The Fund's total administrative expense for the period, including amounts deducted directly from investment income of pooled funds is as follows:

(thousands)

	2003	2002
Direct fund expenses, (Note 7)	\$ 1,778	\$ 1,455
Externally managed investment pools	11,436	8,291
Internally managed investment pools	2,733	1,722
Total	\$ 15,947	\$ 11,468
Percent of net assets at fair value	0.144%	0.092%

NOTE 9 COMPARATIVE FIGURES

Certain 2002 figures have been reclassified to conform to 2003 presentation.

NOTE 10 APPROVAL OF FINANCIAL STATEMENTS

These financial statements were approved by the Deputy Minister of Revenue.

ALBERTA HERITAGE SAVINGS TRUST FUND

SCHEDULES TO THE FINANCIAL STATEMENTS

SCHEDULE OF INVESTMENTS IN FIXED INCOME SECURITIES

Schedule A

March 31, 2003 (thousands)

	Fund's share 2003		Fund's share 2002	
	Cost	Fair Value	Cost	Fair Value
Deposits and short-term securities	\$ 258,716	\$ 258,716	\$ 90,252	\$ 90,252
Fixed Income Securities (a)				
Corporate, public and private	2,134,498	2,115,369	3,161,066	3,116,173
Government of Canada, direct and guaranteed	639,630	640,529	1,181,806	1,157,039
Provincial, direct and guaranteed:				
Alberta	6,786	7,370	9,861	10,271
Other provinces	584,015	581,516	744,038	722,116
Municipal	62,260	63,169	49,249	48,791
Provincial corporation debentures	100,037	158,018	104,622	165,178
Loans	97,359	97,359	97,359	97,359
	3,624,585	3,663,330	5,348,001	5,316,927
Receivable from sale of investments and accrued investment income	41,239	41,239	78,837	78,837
Accounts payable and accrued liabilities	(6,589)	(6,589)	(44,814)	(44,814)
	34,650	34,650	34,023	34,023
	\$ 3,917,951	\$ 3,956,696	\$ 5,472,276	\$ 5,441,202

(a) Fixed income securities held as at March 31, 2003 have an average effective market yield of 5.68% per annum (2002: 5.41% per annum) and the following term structure based on principal amount:

	2003 %	2002 %
under 1 year	2	31
1 to 5 years	36	26
5 to 10 years	31	21
10 to 20 years	13	9
over 20 years	18	13
	100	100

ALBERTA HERITAGE SAVINGS TRUST FUND

SCHEDULE OF INVESTMENTS IN CANADIAN EQUITIES

Schedule B

March 31, 2003 (thousands)

	Fund's share 2003		Fund's share 2002	
	Cost	Fair Value	Cost	Fair Value
Deposits and short-term securities	\$ 23,056	\$ 23,056	\$ 34,647	\$ 34,647
Public equities (a)(b)				
Financial	717,653	759,882	643,536	746,185
Energy	297,762	368,554	233,727	328,373
Materials	363,479	359,403	341,579	368,738
Industrials	174,582	172,681	222,834	243,199
Consumer discretionary	193,152	171,206	210,139	207,260
Information technology	151,830	122,174	218,158	209,338
Telecommunication services	126,947	120,503	91,633	92,381
Consumer staples	88,729	101,180	78,482	98,663
Utilities	76,729	83,199	57,570	69,157
Health Care	86,322	80,995	96,768	100,588
	2,277,185	2,339,777	2,194,426	2,463,882
Passive index	16,456	16,680	30,234	32,015
	2,293,641	2,356,457	2,224,660	2,495,897
Private equities	88,295	81,569	81,175	79,491
Receivable from sale of investments and accrued investment income	6,579	6,579	21,319	21,319
Accounts payable and accrued liabilities	(18,607)	(18,607)	(8,042)	(8,042)
	(12,028)	(12,028)	13,277	13,277
	\$ 2,392,964	\$ 2,449,054	\$ 2,353,759	\$ 2,623,312

- (a) The Fund's effective net investment in Canadian public equities includes the fair value of deposits and floating rate notes, totalling \$550,918,000 (2002: \$510,081,000) which are used as underlying securities to support the notional amount of Canadian equity index swap contracts and equity index futures contracts.
- (b) The industrial classifications are those used by the S&P/TSX Index.

ALBERTA HERITAGE SAVINGS TRUST FUND

SCHEDULE OF INVESTMENTS IN UNITED STATES EQUITIES

Schedule C

March 31, 2003 (thousands)

	Fund's share 2003		Fund's share 2002	
	Cost	Fair Value	Cost	Fair Value
Deposits and short-term securities	\$ 23,198	\$ 23,198	\$ 13,110	\$ 13,110
Public equities (a) (b)				
Financial	386,731	338,718	368,148	357,170
Consumer discretionary	326,894	291,626	290,523	274,590
Health Care	270,831	257,348	256,430	248,791
Information technology	262,253	235,478	354,595	319,543
Industrials	218,911	191,605	226,164	223,369
Consumer staples	179,069	161,325	197,674	193,818
Energy	128,498	111,492	145,227	140,838
Telecommunication services	54,907	49,260	87,524	72,109
Materials	57,080	48,294	70,355	69,309
Utilities	45,953	43,141	79,384	75,298
	1,931,127	1,728,287	2,076,024	1,974,835
Passive index	132	174	313	291
	1,931,259	1,728,461	2,076,337	1,975,126
Private Equities	6,811	6,494	-	-
Receivable from sale of investments and accrued investment income	4,254	4,254	18,938	18,938
Accounts payable and accrued liabilities	(3,355)	(3,355)	(8,968)	(8,968)
	899	899	9,970	9,970
	\$ 1,962,167	\$ 1,759,052	\$ 2,099,417	\$ 1,998,206

(a) The Fund's effective net investment in US public equities includes the fair value of deposits and floating rate notes, totalling \$37,864,000 (2002: \$Nil) which are used as underlying securities to support the notional amount of US equity index swap contracts and equity index futures contracts.

(b) The industrial classifications are those used by the Standard & Poor's indices.

ALBERTA HERITAGE SAVINGS TRUST FUND

SCHEDULE OF INVESTMENTS IN NON-NORTH AMERICAN EQUITIES

Schedule D

March 31, 2003 (thousands)

	Fund's share 2003		Fund's share 2002	
	Cost	Fair Value	Cost	Fair Value
Deposits and short-term securities	\$ 64,941	\$ 64,941	\$ 31,001	\$ 31,001
Public equities (a)				
United Kingdom	538,441	462,446	491,588	494,816
Japan	320,114	273,788	386,408	340,718
France	179,921	153,954	218,911	220,626
Switzerland	150,805	131,937	156,183	159,836
Netherlands	127,664	105,851	156,839	158,483
Australia	87,877	90,362	72,150	80,516
Germany	101,305	82,318	133,246	130,791
Italy	85,869	76,510	63,398	66,291
Hong Kong	56,369	50,019	51,803	55,963
Spain	52,331	46,591	55,380	52,077
Finland	34,540	29,649	33,728	37,807
Sweden	28,607	28,528	27,574	33,577
Other	169,376	157,056	132,306	141,565
	1,933,219	1,689,009	1,979,514	1,973,066
Receivable from sale of investments and accrued investment income	13,595	13,595	33,857	33,857
Accounts payable and accrued liabilities	(26,439)	(26,439)	(35,853)	(35,853)
	(12,844)	(12,844)	(1,996)	(1,996)
	\$ 1,985,316	\$ 1,741,106	\$ 2,008,519	\$ 2,002,071

- (a) The Fund's effective net investment in Non-North American public equities includes the fair value of deposits and floating rate notes, totalling \$Nil (2002: \$779,000) which are used as underlying securities to support the notional amount of Non-North American equity index swap contracts and equity index futures contracts.

ALBERTA HERITAGE SAVINGS TRUST FUND

SCHEDULE OF INVESTMENT RETURNS

Schedule E

Year Ended March 31, 2003

The Fund uses the time-weighted rate of return based on market values to measure performance. The measure involves the calculation of the return realized by the Fund over a specified period and is a measure of the total return received from an investment dollar initially invested. Total return includes cash distributions (interest and dividend payments) and capital gains or losses (realized and unrealized).

The time-weighted rate of return measures the compounded rate of growth of the initial investment over the specified period. It is designed to eliminate the effect that the size and timing of cash flows have on the internal rate of return. The investment industry uses time-weighted rates of return calculated using market values when comparing the returns of funds with other funds or indices.

Investment returns for the Fund are as follows:

	2003	One Year Return			4 Year Compound Annualized Return
		2002	2001	2000	
Time-weighted rates of return					
Short-term fixed income	3.0	3.8	5.7	5.3	4.5
Scotia Capital 91-day T-Bill Index	2.7	3.7	5.7	4.7	4.2
Long-term fixed income	9.5	5.9	9.5	1.7	6.6
Scotia Capital Universe Bond Index	9.2	5.1	8.7	1.3	6.0
Canadian equities	(16.6)	4.2	(16.0)	37.8	0.1
S&P/TSX	(17.6)	4.9	(18.6)	45.5	0.6
United States equities	(30.6)	1.4	(14.4)	13.1	(9.2)
S&P 500 Index	(30.7)	1.6	(15.1)	13.2	(9.3)
Non-North American equities	(29.1)	(5.8)	(22.6)	37.3	(8.2)
MSCI EAFE Index	(29.3)	(7.3)	(19.6)	20.1	(10.8)
Private equities (1)	(3.3)	n/a	n/a	n/a	n/a
Consumer Price Index plus 8% (1)	5.7	n/a	n/a	n/a	n/a
Real estate	9.8	7.3	9.7	5.8	8.1
Consumer Price Index plus 5% (2)	9.6	9.9	11.9	9.9	10.3
Absolute Return Strategies	1.6	n/a	n/a	n/a	n/a
Consumer Price Index plus 6% (1)	4.7	n/a	n/a	n/a	n/a
Endowment portfolio	(11.3)	3.3	(6.1)	18.0	0.4
Policy Benchmark	(11.7)	3.4	(6.2)	15.9	(0.2)
Transition portfolio (3)	0.5	5.3	8.2	3.0	n/a
Overall Return	(11.0)	4.2	(0.1)	9.0	0.3

- 1) Actual and benchmark returns are for six months.
- 2) Effective April 1, 2002, the benchmark changed from the Russell Canadian Property Index (RCPI) to CPI plus 5%. Therefore, the benchmark for four years is a combination of RCPI and CPI plus 5%.
- 3) The Transition Portfolio was wound up in the first half of the year. The actual return of 0.5% is for six months.