

Outline for Empire Club Speech, June 11th, 2009

Dr. Leo de Bever

AIMCo – The New Kid on the Investment Block

Ladies and gentlemen

Canada has more than its share of innovative funds that invest long-term savings with a single minded focus on the best long-term return on risk for the ultimate recipientsand I am proud to have been part of the Ontario Teachers story for almost 10 years.

I am really pleased that so many of you have come today to hear more on how we intend to give substance to the provincial government's dream to create another strong pension and endowment manager in Alberta.

The Alberta Economy

Before I get to AIMCo itself and how it intends to deploy Alberta savings in global opportunities, I want to talk a bit about the larger Alberta growth story,

- about the maturation of its educational and medical institutions,
- the opportunities for technologies that may solve some of Alberta's energy issues,
- the outlook for capital looking for attractive returns in energy.
- and very selfishly, I want to show what AIMCo and other Edmonton financial institutions represented here today have a lot to offer to people with the right skills.

Alberta has been a rapid growth story ever since it became a province in 1905. At that time it was home to only 4% of Canadians.

Since then, it has been a magnet for immigrants.

Until the 50s, that was still a function of opportunities in grain farming and ranching. But over the last 40 years population growth has been double the national average largely because of energy. Today, Alberta makes up 11% of Canada's population and produces 17% of national GDP.

The province has the youngest population in the country, and even in the current environment, 71% of the working age population has jobs, versus a national average of 61%.

The Edmonton-Calgary corridor is now home to 2.5 million people, one of the biggest urban concentrations in Canada. Perhaps not surprisingly, growing at twice the national rate has meant that public spending on social infrastructure has been running at twice the national average per capita.

That is one reason Alberta's recession has not been quite as bad as in the rest of the country.

A fast growing population base and a growing energy industry need greater financial sector capacity.

Employment Opportunities in Edmonton

We are looking for good people but we are not the only ones. Calgary serves as regional headquarters for Canada's big five banks and services the traditional oil and gas sector.

However, ATB Financial, the largest financial services provider in Alberta, is headquartered in Edmonton, as is Canadian Western Bank, the west's largest regional schedule 1 bank, along with the province's largest credit union, Servus.

I have been doing business in Alberta for 25 years. The changes over that period have been remarkable. Because of public and private investments, many the provincial institutions now have critical mass. The most obvious place where that has happened is in the universities and medical facilities.

I have spent a fair bit of time with both the University of Calgary and the University of Alberta and have been impressed with the quality of university programs and facilities, made possible in part, by Alberta's good economic fortune.

In an effort to broaden the pool of homegrown financial talent AIMCo has agreed to fund the Alberta Finance Institute in partnership with both universities. Reputations tend to lag reality, and it will take a while before the high caliber of academic staff and academic programs is recognized externally. But it is already starting to happen. The *Financial times of London* this year ranked the Alberta MBA program among the "Top 100" in the worldnumber 2 in Canada.

The same is true in other areas like medicine and other life sciences where the major constraint seems to be to attract or train people fast enoughto staff what are truly world scale facilities.

Alberta's Energy-based Economy

The recent financial and economic crisis obviously has not passed Alberta by. But the province has held up well within Canada just like Canada has not suffered as much as many other countries.

There have been job losses, cancellations of oil sands projects and the conventional oil and gas sector in Calgary is feeling very depressed. Lower oil and gas revenues imply that the provincial government will run a deficit for the next few years.

The one constant in economics is the human tendency to overreact to both good news and bad news.

Canadians and Albertans are far more depressed than we need to be. Yes we have lots of problems but our respective glasses are three quarters full. Canada's financial system is healthier than most and the financial stimulus pumped into the economy will eventually have its effect. We are better equipped than most countries to deal with our problems, particularly if we don't just sit around waiting for government to do it for us.

Today is likely to be the darkest moment before the dawn, not the prelude to a protracted bust.

The global economy may already be bottoming out, and at AIMCo we intend to take full advantage of the investment opportunities that this represents. When growth resumes, both the demand and price for energy should pick up. So there is a reasonable possibility that Alberta will grow again by 2010.

It may not be a rapid straight line recovery, but worrying about the shape of a recovery distracts you from what matters in the long run.

The key to long-term economic success will be the same it always is; finding productive people to deploy financial capital in the right technologies with well managed companies.

In the end, sustainable jobs and companies have to be efficient and productive. The challenge in a resource economy like Alberta is that there is not much interest in productivity when the market is good and not much capital to do so when product prices are weak.

Not enough investment is taking place in the downturn to put more productive capacity in place for the next upturn.

Alberta is a high cost producer in both the conventional energy sector and the oil sands. The conventional sector will need new tricks to get oil and gas out of old fields economically.

The oil sands reserves theoretically rival those of Saudi Arabia. But again, development costs are high.

95% of oil sands reserves are deep enough that they will have to be developed in situ and the existing technology is costly and immature in its use of water and energy

So more needs to be done to come up with better technological solutions. But, it's hard to imagine a scenario where we cannot find a rational way to develop Alberta's oil sands in a world short of oil.

What is AIMCo

Now, let's talk about AIMCo

I knew I was in trouble when I was introduced in Calgary late last year as "Leo de Bever, CEO of AIMCo, the best kept secret in Alberta".

In case I had missed the point, when AIMCo bought 20% of a company called Precision Drilling many people concluded the province was getting into the drilling business. The good news is that it gave us an opportunity to explain who we really were, and reasonable people understood.

The bad news is that the world has its share of very unreasonable people.

So who are we?

We manage about \$70 billion of Alberta's savings. I am told that makes us Canada's fifth largest investment fund manager.

We serve a number of public sector pension plans, endowments such as the Alberta Heritage Savings Trust Fund, as well as the government's short term stabilization fund.

These funds were previously administered from within the Department of Finance.

The Importance of Independence

A few years ago, the Alberta government reviewed the international evidence on best practice for investing these kinds of funds. It concluded that managing such assets through a separate entity structured like OTPP and CPP would mean better governance and that better governance would lead to better long-term results.

So AIMCo was set up on January 1, 2008 as a crown corporation run by an independent board.

With an impeccable sense of timing I came on board in August 2008, just as the bottom fell out of the market.

The decision to create AIMCo was a courageous one from a political perspective. It represents a very sharp break from the past. I am sure we will have our challenges in ensuring that everyone sticks with the program, but the Minister of Finance and the Premier have been very supportive.

My board and I believe that being separate from government is absolutely crucial to our success.

Precision Drilling provides one good reason; i.e. there should be no confusion about the independence of the decision making process. But there is a more fundamental reason related to objectives and measuring outcomes.

Pension and endowment investment policies specify that we invest about 60% of our assets in stocks.

So AIMCo and organizations like it deliberately seek short term equity market risk with an historical annual range of returns between -40% and +60%. We do it because over time all that annual volatility tends to produce an attractive average incremental long-term return on risk.

In that framework our job is to consistently exceed annual market returns because, over time, average market returns are expected to be attractive.

However, reaction to AIMCo's -16% return for 2008 and the treatment CPP recently received at the hands of the Commons Committee clearly show that politics and the court of public opinion don't like short term risks and short term losses. So they want our annual returns to be positive.

That leads to a fundamental contradiction.

The reason equity risk is rewarded in the long run is that annual stock returns are essentially unpredictable.

If managers could anticipate and sidestep negative annual market returns, their actions would change market pricing, and the reward for taking risk would cease to exist.

There is no evidence that this is the case. So that leaves us with two solutions;

- let the court of public opinion set a suboptimal investment policy, or
- accept that there needs to be a buffer between long-term investing and politics.

I suppose there is the additional possibility that the policies we are asked to implement are wrong and that risk has no return. The evidence on that score provides another curious aspect of all the current handwringing.

The period since 1982, the bottom of the last big bear market has delivered returns for pension funds far superior to anything we have seen over the last 100 years.

Without wanting to belittle last year's negative returns, that seems to suggest that our expectations may be higher than markets can deliver.

AIMCo's Philosophy

So what kind of manager will AIMCo be?

Expect us to have a single-minded focus on providing the best outcome for our investment partners. I am using "partner" instead of "client", because the relationship with the funds we manage is changing. AIMCo used to receive a very prescriptive set of investment instructions from its partner funds.

That is now morphing into a discussion on risk tolerance and how that translates into broad allocations to equities, bonds and real return assets.

After that it is up to AIMCo to find the best opportunities within these categories.

Once there is agreement on policy, how do you create an organization that finds the right investments and manages them effectively? It obviously all starts with the right people, not just on the investment side, but also in risk management and operations.

I inherited an organization that was very weak in systems and understaffed in operations. And the investment and operations side were not used to solving problems together.

We are upgrading our systems, processes and controls to best practice and people are solving problems at an amazing rate.

A lot of what we intend to do is just common sense.

We have abandoned strict asset class silos and are encouraging cooperation on opportunities that do not fit neatly in a traditional asset class.

The easiest return you can make for your partners is not spending it needlessly. That means doing the basics well, eliminating needless complexity and having the tools to spot errors early. Our industry has a need to strive for efficiency as much as any other.

I started with an organization that spent 75 percent of its budget on external management of 25% of its assets.

We will be very pragmatic about what we do ourselves and what we pay others to do. That has to be a pragmatic trade-off between benefits and costs, but a few examples may give you an idea where we are heading.

The existing private equity portfolio is highly concentrated in funds.

We now have an office in Toronto to get more efficient access to direct private equity deal flow. Expect more transactions like Precision Drilling or Viterra where we use our capital to help listed companies achieve objectives they could not achieve on their own.

Part of the reason I am here is that we want to make it clear that we are very open to working together with other pension and endowment funds and other institutional investors on large projects

Life in Edmonton

Edmonton as a location has not been an issue,

A recent study suggests there is a very wide gap between outsider perception of Edmonton and the far more positive views Edmontonians have about their city.

So we tend to spend a lot of time making sure people are aware of what the city has to offer.

Many of us with no ties to Alberta have moved for the unique opportunity

We're also attracting many talented Albertans, who previously moved away to centers like Toronto and New York. I started with 120 colleagues. We have replaced 30, hired about 80 people so far and are looking for another 50 over the next year or so. Our basic premise is that our people should be smart enough to work in any part of our organization.

If you know someone who's got what it takes to accept a brand new challenge in a fast-paced environment, send them our way.

So, we are a new player on the block, ready to implement best investment practices and improve upon them when we can. Over the coming months we'll be exploring investment opportunities with many of you in this room and others around the Globe.

Thank you for this opportunity to share my thoughts with you and I hope to see you in Edmonton in the near future.