Investment Policy Statement

Workers' Compensation Board – Alberta

Effective March 1, 2023

Workers' Compensation Board – Alberta

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Part 1: Overview

1.1. Statement of Purpose and Principles

The Investment Policy Statement ("the Statement") of the Workers' Compensation Board - Alberta ("WCB") describes the investment objectives and guidelines that govern the management of the investment portfolio of the Accident Fund.

The WCB claim benefit liabilities, return objectives and risk tolerance form the foundation on which the Statement is established.

The overall principle that guides management of WCB's investment portfolio is the "prudent person rule." It requires that decisions are to be made in a manner that a reasonable and prudent person, in a fiduciary relationship, would apply with respect to a portfolio of investments to avoid undue risk of loss and to obtain a reasonable return.

Investments shall be managed in accordance with the criteria and limitations outlined in this Statement and will abide by all relevant legislation.

1.2. The Accident Fund

The Accident Fund was established through the *Workers' Compensation Act* ("the Act") to support a sustainable workers' compensation system for the benefit of workers and employers. The Accident Fund consists of all assets, liabilities, and reserves of WCB. All money received by WCB is to be paid into the Accident Fund and all expenditures of WCB, including the costs of administering the Act, are to be paid from the Accident Fund.

The Act grants WCB authority to invest its funds in adherence with prudent investment standards, with the requirement to ensure sufficient assets are available in the Accident Fund for the payment of present and future compensation as estimated by WCB's actuary.

The Act requires WCB to engage Alberta Investment Management Corporation ("AIMCo") as the designated provider of investment management services.

Reference: *Workers' Compensation Act, RSA 2000, Sections 91, 92 and 92.1*

1.3. Governance

The WCB Board of Directors ("the Board") has overall responsibility for the investments of the Accident Fund. Strategic investment direction is set by the Board through approval of the Investment Policy Statement. The Statement is reviewed annually by the Finance Committee of the Board, with any amendments then recommended for approval by the Board.

The Finance Committee is responsible for overseeing the investment portfolio to ensure it is managed in accordance with the Statement. To satisfy this commitment the Finance Committee reviews regular updates and reporting on portfolio activities, results, risk, and overall performance of the investment manager.

The Finance Committee delegates more detailed oversight and monitoring responsibilities to WCB management. WCB management recommends Investment Policy Statement amendments and provides regular portfolio updates and reporting to the Finance Committee.

AIMCo, as the investment manager, is accountable for implementation of the Statement and day-to-day management of the investment portfolio in accordance with the Investment Management Agreement between AIMCo and WCB. AIMCo must also provide reporting that is sufficient for the Board to discharge their oversight responsibilities.

External investment consultants may be engaged by the Board to assist in the development of the Statement, evaluate investment results and manager performance and provide advice on other matters related to governance.

Part 2: Investment Beliefs

Investment beliefs inform strategic decision-making regarding the investment portfolio and provide guidance for its management. The Board's investment beliefs include:

(a) Asset mix can positively impact the relationship between assets and liabilities and reduce funding level volatility. The nature of liabilities should be considered during the asset allocation decision process.

(b) The long-term asset mix is the primary determinant of a portfolio's risk and return.

(c) Diversification of asset classes, implementation strategies, and securities can improve the risk and return characteristics of the portfolio.

(d) Understanding and managing risks are key to achieving sustainable long-term returns and volatility objectives.

(e) There is a relationship between risk and return, where in the absence of skill, higher returns require taking higher risk.

(f) Over the long term, equities are, on average, expected to outperform bonds to compensate investors for assuming higher risk.

(g) Foreign currency exposure should not add or detract value over long time periods. Over shorter time horizons, some foreign currency exposure can act as a diversifier, but large exposures can increase portfolio volatility.

(h) Market inefficiencies create opportunities to enhance returns and reduce risk, however the level of inefficiency can vary by asset class, region, market, and time period.

(i) Effective implementation strategies can improve the net return and/or lower the risk of the portfolio.

(j) Short-term market timing is an inefficient strategy for consistently increasing portfolio returns.

(k) Costs to implement an investment program should be effectively managed, transparent, and aligned with the overall investment objectives of the portfolio.

Part 3: Investment Objectives

The fundamental investment objective for the investment portfolio is to earn a rate of return net of investment expenses that equals or exceeds the actuarial required rate of return over the long term. This is the rate of return required to generate sufficient assets to meet WCB's liabilities and ultimately support a fully funded Accident Fund.

The actuarial required rate of return is the discount rate used to value the claim benefit liabilities on a funding basis. This rate of return makes provision for adverse deviation in the liability by setting the probability of earning the required rate at between 60% and 80%. The higher the probability used, the higher the provision for adverse deviation.

Over the short and medium term, an investment portfolio's return can deviate significantly from long-term expectations, both positively and negatively. While WCB is a long-term investor with liability cashflows that extend beyond 50 years, the short-term volatility of the investment portfolio has implications on the stability of premium rates and the ability to meet the Act's legislated requirement to remain fully funded. The investment portfolio must be managed at an acceptable level of risk to minimize the impact of investment return volatility on financial results.

Portfolio policy asset mix implementation that includes active management is expected to generate returns over the long term that are higher than passively investing in the policy benchmarks at a similar or lower level of volatility. The target for additional return from active management at the total portfolio level is set at 40 basis points (0.40%) per annum, net of fees and expenses measured over rolling annualized four-year periods.

Part 4: Long-Term Asset Mix

The long-term asset mix decision is the key strategic determinant to achieving the investment portfolio objectives. Through the asset allocation process, the balance between risk and return is evaluated to set a long-term policy asset mix with both an expected rate of return that exceeds the actuarial required rate and an expected volatility that reflects the Board's risk tolerance.

4.1. Factors in Determining the Policy Asset Mix

In setting the policy asset mix of the investment portfolio, WCB considers the following factors:

(a) achieving at a minimum, the actuarial rate of return that supports the long-term sustainability of the Accident Fund;

(b) the WCB Funding Policy including the target funding range, the goal to minimize premium rate volatility and the requirement to remain fully funded;

(c) the characteristics of WCB liabilities and their correlation with categories of investment assets;

(d) mitigating exposure to unexpected inflation;

(e) ensuring adequate liquidity is available to satisfy operational cash flow needs; and

(f) the risk tolerance of the Board.

The long-term risk and return characteristics of the policy asset classes and target asset mix are determined through an asset-liability study. The expected return of the policy target asset mix is calculated using a 50% probability.

The policy asset mix is reviewed through an asset-liability study every three to five years, or sooner if there are significant changes to capital market assumptions, WCB's financial condition, relevant legislation or any of the factors listed above.

4.2. Asset Classes

The investment portfolio will be invested in a diversified portfolio of the following asset classes:

Fixed Income

These investments generally provide capital preservation, a steady source of diversification and a hedge against interest rate risk.

Cash and Short Term	Generally refers to debt securities issued by governments, banks, and other corporate entities with a term to maturity of 1 year or less at the time of purchase. This asset class provides safety of principal while ensuring a high degree of liquidity to meet cash needs.
Bonds	Primarily composed of investment grade, publicly traded debt instruments issued by governments and corporations, as well as asset-backed securities. Investments in this asset class provide a stable income stream and a reliable source of liquidity.
Mortgages	Commonly refers to loans secured by commercial real estate assets such as mortgage loans and mortgage-backed securities. These investments are expected to provide a steady cash flow, diversification, and enhanced risk-adjusted returns within fixed income.
Private Debt	Generally includes privately negotiated loans to entities that are secured by the assets of the borrower. While illiquid in nature, these offer diversification and opportunity for return enhancement.

Equities

Equity investments provide exposure to global economic growth, generally providing higher rates of return in the long term than the other asset categories but with higher volatility.

Public Equity	Includes, but is not limited to, publicly traded equity securities, preferred shares, convertible preferred shares, and other forms of equity instruments. These can be listed or domiciled in Canadian, global, and emerging market countries.

Inflation Sensitive

These investments provide stable income, long-term value enhancements and/or mitigation of inflation risk due to their inflation pass-through attributes.

Real Return Bonds	Primarily includes bonds issued by federal, provincial, or corporate entities that provide a rate of return that is linked to an inflation index.
Real Estate	Generally refers to the direct or syndicated ownership of domestic or global commercial properties, as well as publicly traded real estate investment trusts (REITs). Largely illiquid, this includes investment in sectors such as office, industrial, retail, and multi-family residential.
Infrastructure	Includes but is not limited to direct, commingled or publicly traded equity ownership of real assets. These global investments are often regulated private assets with significant barriers to entry that provide an essential facility or service.

4.3. Investment Benchmarks

Policy benchmarks are assigned to each asset class that broadly represent the risk and return properties that WCB expects for investments within these categories. Generally, the selection of investment benchmarks reflects relevant representative market-based indices for each asset class, but where unavailable, industry accepted benchmarks have been assigned.

The policy benchmarks clarify the nature of the expected investments and degree of risk that should be pursued in the implementation of the policy asset mix and selection of investment strategies. These benchmarks are also used for the measurement and evaluation of investment performance.

4.4. Policy Asset Mix

The policy asset mix, including policy weights, target ranges and benchmarks for each asset class, is summarized in the following table:

Asset Class	Policy Weight	Target Range		Benchmark
		Min	Max	
FIXED INCOME				
Cash and Short Term	3	0	5	FTSE Canada 30-day T-Bill Index
Bonds	21	15	38	FTSE Canada Universe Bond Index
Mortgages	5	2	7	60% FTSE Canada Short-Term Overall Bond Index + 40% FTSE Canada Mid-Term Overall Bond Index + 50 bps
Private Debt	2	0	3	40% S&P/LSTA Leveraged Loan Index (Currency hedged to CAD) + 40% S&P European Leveraged Loan Index (Currency hedged to CAD) + 90 bps
Total Fixed Income	**31**	**20**	**50**	
EQUITY				
Canadian	10	5	15	S&P/TSX Capped Composite Index
Global	20	10	30	MSCI World ex Canada Index (Currency 50% hedged, U.S. Dollar 25% hedged to CAD)
Emerging Market	5	2	10	MSCI Emerging Markets Index (CAD)
Total Equity	**35**	**20**	**45**	
INFLATION SENSITIVE				
Real Return Bonds	5	2	10	FTSE Canada Real Return Bond Index
Canadian Real Estate	10	6	18	MSCI REALpac Canadian All Property Index – Large Institutional Subset
Foreign Real Estate	4	0	6	MSCI IPD Global Regional Property Index (CAD)
Infrastructure	15	10	20	50% FTSE Canada Real Return Federal Bond Index + 50% MSCI All Country World Index (Currency hedged to CAD)
Total Inflation Sensitive	**34**	**20**	**45**	
Total Portfolio	**100**			

The actual allocation when compared to asset mix targets, minimums and maximums are all based on market value and adjusted for the exposures created by derivative securities when used for management of the asset mix.

Part 5: Implementation

5.1. *Implementation of the Policy Asset Mix*

While the selection of the policy asset mix is of critical importance, effective implementation is also essential to achieving the objectives of the investment portfolio. Prudent diversification by asset class, geographic exposures, underlying return-risk factors, currencies and investment strategies is key to enhancing the long-term risk-adjusted return of the investment portfolio.

The investment portfolio will include active management where there are perceived opportunities to exploit market inefficiencies. A skilled investment manager can deliver a long-term return that is higher than the aggregate return of the passive benchmarks used to measure relative performance, while balancing the effect on short-term volatility.

AIMCo is responsible for investing the portfolio in compliance with the policy asset mix target range for each asset class, with the asset mix to be maintained in close relation to the policy weights. AIMCo is given latitude to tactically deviate from the asset mix targets to act upon opportunities, or to adjust the portfolio in response to changing market conditions, provided the portfolio continues to be managed in accordance with the permitted ranges in the Investment Policy Statement and the terms of the Investment Management Agreement. During periods of extreme market volatility, limited liquidity or lack of suitable private asset investments, an asset class may temporarily exceed the minimum or maximum of its allowable range. If this occurs, AIMCo is required to immediately notify WCB and provide a plan to rebalance back within the allowable range in a measured and reasonable manner as market liquidity allows.

5.2. *Risk Management*

The assumption of investment risk is necessary to meet the return objectives of the investment portfolio. The goal is not to eliminate risk but instead to manage it and to ensure that the level of risk taken is consistent with the investment objectives in the Statement. Ongoing assessment of economic, market, operational and other risks to the total portfolio is prudent to mitigate the impact of investment returns on WCB's funding level and the ability of the Accident Fund to service its liabilities.

The investment portfolio will be measured and monitored for:

(a) the risk of adverse funding level changes or becoming unfunded in relation to WCB liabilities;

(b) the active risk taken through implementation that varies from the policy asset mix;

(c) the volatility of its returns; and

(d) downside risks through stress and scenario testing.

WCB sets its tolerance for risk through the selection of the long-term policy asset mix, the benchmarks used for performance evaluation and any other risk metrics communicated to AIMCo.

Overall, risk management activities need to be executed to provide for a well-diversified portfolio in consideration of the objectives and constraints of the Statement.

5.3. Manager Evaluation

AIMCo's ability to implement the policy asset mix and achieve the active management target will be evaluated against policy benchmarks. The primary time frame for long-term performance evaluation is rolling annualized four-year periods. The rates of return for quarterly and annual periods will be reviewed and monitored for identification of performance concerns.

AIMCo will also be evaluated on the risk taken to achieve the portfolio returns. The volatility of the portfolio, estimated by the annualized standard deviation, will be evaluated versus that of the passive policy benchmark. Relative volatility will be evaluated on both annual and rolling annualized four-year time periods.

5.4. Eligible Investments

As the exclusive investment manager of WCB's investment portfolio, AIMCo products, primarily pooled funds, are the sole mechanism available to implement WCB's policy asset mix.

AIMCo products and their underlying securities must reflect the return and risk characteristics of their respective asset classes and demonstrate appropriate risk controls and constraints. This includes but is not limited to single name exposures, counterparty credit ratings and credit quality.

The selection of AIMCo products will be based on their contribution to the portfolio's risk and return, rather than in isolation. Products that WCB's portfolio may invest in are specified in the Investment Management Agreement.

5.5. Additional Investment Guidelines

Derivatives - may be used to achieve portfolio management objectives, including strategies to:

(a) replicate holding or selling any eligible investment, individually or in aggregate.

(b) protect the portfolio from any credit, currency, interest rate, equity market risk, or any other financial risk.

(c) manage asset class allocations and exposures in relation to overall asset mix targets.

Derivatives are to be used prudently within a portfolio context. Implementation can include overlay pools that apply the above strategies at an asset class or overall portfolio level. They may not be used to alter an asset class weight outside of its permitted range or violate any other constraint specified in the Statement.

Foreign currency exposure - provides portfolio diversification over the long term but foreign currency fluctuations can increase the short-term volatility of the fund. Currency hedging is used to reduce this short-term volatility and lessen the potential impact on funding level and employer premiums. Asset class target hedge ratios based on the market value of their foreign currency exposures are as follows:

Bonds, Mortgages and Private Debt: 100% hedged

Global Equity: 25% for U.S. dollars, 50% for other major currencies

Emerging Market Equity: unhedged

Developed Market Infrastructure: 100% hedged

Emerging Market Infrastructure: unhedged

The target hedge ratios vary by asset class based on the volatility of the asset class, the cost of hedging, the currency characteristics and the expected relationships between currencies and asset prices. The investment manager has the discretion to actively manage currency exposures if consistent with the investment objectives within the Investment Policy Statement.

Leverage - is permitted for the purpose of enhancing returns and managing risk. However, using borrowed capital to gain investment exposure can magnify the actual returns of the underlying securities both on the upside and the downside. Other forms of leverage can include derivatives and repurchase agreements. Leverage may be employed provided that robust risk policies and controls are established to monitor and mitigate the risks where it is used.

Liquidity - will be required for various reasons which include funding the payment of benefits and expenses, rebalancing the portfolio, meeting capital calls and other investment transactions. Ensuring adequate liquidity for these uses can be more complex with the inclusion of private market investments which are beneficial to the risk and return profile of the portfolio but cannot be readily purchased or sold. Liquidity risk within the portfolio will be monitored to ensure these funding needs can be met.

Securities lending - may be undertaken for the purpose of generating additional return. Program risks are to be closely monitored by the investment manager and loans are to be secured according to industry best practice.

Short selling - of individual securities, by way of borrowing securities, or otherwise, is permitted to increase the return and/or manage the risk in the portfolio. The investment manager will assess the impact of these strategies on risk and apply relevant limits to mitigate where prudent.

Valuation - of the investment portfolio is based on the fair value of the investment assets held as determined in accordance with International Financial Reporting Standards (IFRS). Estimates for investments not traded in an active market will be determined using generally accepted valuation methods including, but not limited to, independent expert appraisals, discounting future cash flows or comparison with pricing of similar assets. The investment manager must implement valuation policies and processes that reflect industry best practice including methodology, timeliness, and sourcing.

5.6. Responsible Investing

Responsible investment refers to the incorporation of environmental, social and governance (ESG) factors into the investment decision-making process. Investment strategies that manage risks and assess opportunities related to ESG are more likely to produce sustainable, long-term returns. WCB requires AIMCo to employ a responsible investment program that supports the achievement of the Investment Policy Statement investment objectives.

5.7. Proxy Voting

WCB expects that the corporations in which it invests should be guided by the principles of good corporate governance and management. An important stewardship responsibility of all shareholders is to exercise the right to vote on all issues put forward at shareholder meetings.

WCB delegates this responsibility to AIMCo, with the requirement that it apply a proxy voting policy that is consistent with increasing shareholder value. Implementation may include the use of third-party proxy voting service providers. AIMCo shall provide a report on proxy voting activity on at minimum an annual basis.

Part 6: Conflicts of Interest and Standards of Professional Conduct

All individuals with responsibilities pertaining to the investment portfolio, both internal and external to WCB, are required to comply with the codes of conduct and standards as set out by their employer, applicable professional associations, and relevant regulatory bodies. WCB requires that AIMCo adopt comprehensive code of conduct and conflict of interest policies that adhere to industry best practice. All decisions and transactions pertaining to the investment portfolio are to be made in the best interests of WCB.

Part 7: Constraints and Compliance

The constraints applicable to WCB's investment portfolio are determined by the policy asset mix and guidelines specified in the Investment Policy Statement, as well as those detailed in the AIMCo product descriptions eligible for investment.

AIMCo is required to implement robust risk management policies and internal controls, must comply with all applicable laws and regulations, and make decisions in alignment with the tax status of WCB.

AIMCo must formally confirm compliance with the constraints in the Statement, the terms of the Investment Management Agreement, and relevant product descriptions on at minimum a quarterly basis. Any identified breach must be communicated to WCB in a timely manner, including the nature of the breach and a prudent course of action to return the portfolio to compliance within a reasonable period of time.