

TO:	CHAIR AND MEMBERS CORPORATE SERVICES COMMITTEE MEETING ON SEPTEMBER 24, 2013
FROM:	MARTIN HAYWARD MANAGING DIRECTOR, CORPORATE SERVICES AND CITY TREASURER, CHIEF FINANCIAL OFFICER
SUBJECT:	2012 INVESTMENT REPORT

RECOMMENDATION

That, on the recommendation of the Managing Director, Corporate Services and City Treasurer, Chief Financial Officer;

1. the 2012 Investment Report **BE RECEIVED** for information; and
2. the attached proposed by-law (Appendix “B”) **BE INTRODUCED** at the Municipal Council meeting on October 1, 2013 to repeal and replace the Municipal Council’s current Investment Policy 8(12), in order to reflect current best practices.

BACKGROUND

The City of London maintained a monthly average investment portfolio of approximately \$460 million in 2012 (2011, \$347 million), which includes investments in securities, prescribed under Ontario Regulation 438/97. As such, the City is required to provide an annual investment report to Council. The report, at a minimum, shall contain the following;

- a) a statement about the performance of the portfolio of investments during the period covered by the report;
- b) a description of the estimated proportion of the total investments that are invested in its own long-term and short-term securities to the total investment of the municipality and a description of the change, if any, in that estimated proportion since the previous year’s report;
- c) a statement by the Treasurer as to whether or not, in his opinion, all investments are consistent with the investment policies and goals adopted by the municipality;
- d) a record of the date of each transaction in or disposal of its own securities, including a statement of the purchase and sale price of each security; and
- e) such other information that Council may require or that, in the opinion of the Treasurer, should be included.

The following report meets the above requirements.

INVESTMENT REPORT

Investment Strategy

The City of London’s overall investment strategy is to invest public funds in a manner that prioritizes security and liquidity of principal over attaining higher investment returns.

The investment strategy in 2012, focused on investing reserve fund cash that was available for the next five to ten years and purchasing long-term investments (i.e. maturity dates greater than one year) with varying maturity dates.

In keeping with this strategy, the City invested \$13 million in guaranteed term deposits (GTD) earning between 1.81% and 2.19% with maturities ranging from 3 to 5 years and increasing its long-term asset management investment portfolio with Scotia Private Client Group by \$25 million.

The Scotia Private Client Group investment portfolio started with an initial investment of \$25 million in August 2005 and then an additional \$25 million was invested in September 2008 and August 2012, for a total investment of \$75 million. The City's strategy with this long-term investment portfolio is to continue to reinvest the interest earned each month. As of December 31, 2012, the City has earned interest of \$11,543,454 from inception of the portfolio, which is an accumulated return (net of fees) of approximately 24% over the past 7.5 years (per year average yield 3.2%, net of fees). For 2012, the net average annual yield was approximately 4.0%.

The 2013 investment strategy will continue to focus on investing reserve and reserve fund cash that is available for the next five to ten years and purchasing bonds at varying maturity dates, this strategy is referred to as the "ladder approach". The purpose of purchasing a number of bonds with staggered maturity dates rather than one bond with a single maturity date is to minimize interest rate risk, allowing the City to capitalize on favourable interest rate conditions and maintain greater liquidity. Higher yields are best obtained by taking advantage of the interest rate curve of the capital market which tends to yield higher rates of returns for longer term investments.

This investment strategy complies with the City's investment policy of preserving principal and liquidity. Long term bonds, when held to maturity, have limited risk to the principal invested and by varying the maturity dates of the long-term bonds the City will be able to maintain liquidity.

Eligible Investments (Statement of Compliance)

The Municipal Act, 2001 stipulates that a municipality can invest only in securities prescribed under Ontario Regulation 438/97. A complete listing of the City's investments held as at December 31, 2012 is attached in **APPENDIX A**. All investments meet the eligibility requirements as prescribed by Ontario Regulation 438/97 and were made in accordance with the investment policies and goals adopted by the City.

Investment in Own- Securities

Ontario Regulation 438/97 requires that the City report the estimated proportion of total investments that are invested in its own long-term and short-term securities to the total investments held by the municipality. At the end of 2012, the City held \$250,000 par value of its own securities, which was approximately 0.20% of total investments (excludes cash). The securities mature on August 6, 2014. No additional own-securities were purchased during the year and there was a decrease of 0.10% (2011, 0.30%) in the proportion of own securities to total investments from the previous year's report.

Performance of Portfolio Investments

In 2012, the City's average amount of funds available for investing from the General Fund (operating and capital), Reserve Funds and Reserves was \$460 million. Of this amount \$365 million was held in cash earning interest at bank prime less 1.75%, the average earned on cash held in the bank for 2012 was 1.28% (1.26% in 2011). The remaining amount, \$95 million, was held in investments, which earned an average of 3.78% (3.41% in 2011). The overall investment return for 2012 was 1.80% (1.76% in 2011).

	2012		2011		2010		2009	
	Average Monthly Balance	Average Annual Return	Average Monthly Balance	Average Annual Return	Average Monthly Balance	Average Annual Return	Average Monthly Balance	Average Annual Return
Cash Held In Bank	\$ 364.5	1.28%	\$ 260.7	1.26%	\$ 280.9	0.82%	\$ 275.6	0.75%
Investments								
Short term (<1 yr)	\$ -	-	\$ 7.6	1.32%	\$ 12.3	1.04%	\$ 11.3	3.84%
Long term	95.2	3.78%	78.5	3.61%	72.6	4.65%	82.8	5.72%
Total Investments	\$ 95.2	3.78%	\$ 86.1	3.41%	\$ 84.9	4.13%	\$ 94.1	5.49%
Total Invested	\$ 459.7 ^(A)	1.80%	\$ 346.8	1.76%	\$ 365.8	1.56%	\$ 369.7	1.94%

(Average monthly balance in millions)

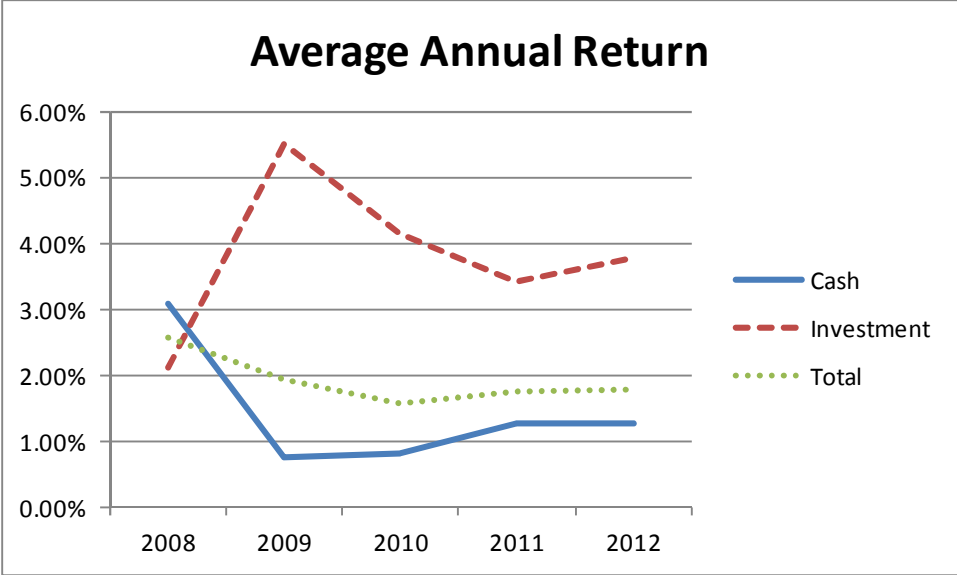
Note:

^(A) Actual ending cash and investment balance as at December 31, 2012 was \$466 million. The above table shows the monthly average balance for 2012.

The proportion of cash held in the bank has increased primarily due to yields on short-term investments (< 1 year) being lower than interest earned in the bank. In December 2009, the yield on 3 month Treasury Bills was 0.19%, with an average of 0.32% for the year and from 2010 to 2012 the average increased from 0.58% to 0.97%, lower than what the City was earning in the bank. With short-term rates being below what the City is earning in the bank, and forecasted to remain so through 2014, the City invested \$75 million in April 2013, to a premium interest rate investment account, earning 0.1% (10 bps) above the City’s regular bank account, while maintaining liquidity.

In 2012, the total average investment portfolio increased by \$113 million primarily from a debt issuance of \$72 million in September 2012. This issuance relieved the pressure of using the reserve funds to temporarily finance capital works in 2012. This will allow the City to invest in long-term investments earning higher yields in 2013.

For 2012, approximately 79% of the City’s total investments were in cash, which is consistent with 2007 to 2011, where cash and short-term investments ranged from 78% - 87% of the total investment portfolio. Since the City is highly invested in cash, the overall return from 2008 reflects the decline in bank interest rates and slow increase through to 2012. In 2011, the City “turned the curve” as the overall returns increased from its lowest point in 2010, and continued to increase in 2012. The increase is due to investing more of the portfolio in longer term instruments earning higher yields.



Investment income

The Municipal Act, 2001, S.O. 2001, c.25 subsection (2) states that *“any earnings derived from an investment shall be credited to the fund from which the money was invested and earnings from combined investments shall be credited to each separate fund in proportion to the amount invested from it”*. Therefore, interest and capital gains earned on Reserve Funds cash and investments are allocated to all reserve funds on a prorated basis and are used for the purpose for which the reserve fund was created. Investment income earned from the General Fund is allocated to general revenues, which contributes to offsetting the amount of taxes levied.

In 2012, the City earned a total of \$8,272,972 (\$6,385,518 in 2011) of income from investments of which \$6,391,630 (\$5,498,112 in 2011) was earned from Reserve Fund investments and \$1,881,342 (\$887,406 in 2011) was earned from General Fund investments.

Looking Ahead

As the economy continues to recover long-term yields are forecasted to move moderately higher in 2014 and the Bank of Canada Overnight Target Rate is forecasted to increase from the current 1.00% to 1.25% in the beginning of 2015 (CIBC World Markets Inc., Economic Insights - June 6, 2013). This outlook is based on information available to date and is subject to change relative to the economic climate. The City's debt issuance, which closed on September 3, 2013, will increase the City's operating cash flow allowing the City to be even more active in the investment markets.

Amendments to Investment Policy 8(12)

Substantive Content Changes

The attached investment policy (Schedule A) has been revised to provide clearer guidance on the City's investment strategy (section 5.0) with respect to diversification and performance of investments. Diversification has been updated to include guidance for investment terms, i.e. proportions for short, medium and long-term investments with respect to the total investment portfolio. Guidance on performance benchmarks has been added to the policy to aid in determining suitable yields for securities. This guidance will be beneficial in selecting and purchasing securities that fit with the investment objective of maximizing interest yield while minimizing the risk to capital.

Purchasing investments is a time sensitive transaction given that interest rates are subject to change until the investment broker receives trade instructions to settle a transaction. As such, the policy has been revised to allow the City Treasurer to explicitly delegate the authority to complete investment transactions. This will alleviate the issue of missing opportunities for purchasing investments with preferable yields.

Phrasing, Organization and Minor Revisions of Content Changes (Non-substantive Changes)

As part of the policy revisions, Administration has rephrased, reorganized or made minor revisions to some of the content of the policy. These changes are not substantive in nature however improve the readability, and flow of the policy. Listed below are the areas that have been rephrased, reorganized or have had minor revisions.

- 1.0 Policy Statement and Purpose
- 2.0 Scope
- 3.0 Standard of Care
- 4.0 Objectives
- 5.0 Investment Strategy
- 6.0 Reporting
- Glossary of Terms

Together, these revisions will help ensure the integrity of the investment management process while allowing the City to be in a better position to capitalize on investment opportunities.

As a result of the above-noted considerations, the attached (Appendix B) proposed by-law is being brought forward for the Municipal Council's consideration.

Acknowledgements

This report was prepared with support from Rick Lamon, Financial Planning & Policy.

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CONCURRED BY:	RECOMMENDED BY:
Larry Palarchio Director of Financial Planning & Policy	Martin Hayward Managing Director, Corporate Services and City Treasurer, Chief Financial Officer,

Appendix A
Appendix B

Cc. M.Turner, Deputy City Treasurer

APPENDIX A - Investment Portfolio Held by the City of London as at December 31, 2012

Instrument held	Purchase Price	Yield	Maturity Date (DD-MM-YR)
<u>Cash Held in Bank</u>			
General	\$ 103,135,999	1.25%	
Reserve Funds	238,979,650	1.25%	
Total Cash Held in Bank	\$ 342,115,649		
<u>Investments</u>			
Fixed Income (Internally Managed)			
City of London Serial Debenture	250,000	5.75%	06-Aug-14
Waterloo Security	499,000	4.70%	19-Nov-14
Canadian Imperial Bank Deposit Note	5,000,000	2.00%	17-Feb-15
Canadian Imperial Bank Guaranteed Term Deposit	4,000,000	1.81%	15-Oct-15
Toronto-Dominion Bank	1,991,000	3.37%	02-Nov-15
Bank of Montreal Residual	8,771,700	2.72%	08-Jul-16
Canadian Imperial Bank Guaranteed Term Deposit	6,000,000	2.09%	17-Oct-16
Bank of Montreal Residual	7,760,000	3.82%	26-Sep-17
Canadian Imperial Bank Guaranteed Term Deposit	3,000,000	2.19%	15-Oct-17
Total Internally Managed Fixed Income	\$ 37,271,700		
Fixed Income (Scotia Private Client Group)			
Capital Cash	\$ 809	1.25%	01-Jan-13
Canada Government T-Bill	263,609	0.95%	04-Jan-13
Canada Government T-Bill	6,513,846	0.92%	14-Feb-13
Canada Housing Trust	4,972,100	3.60%	15-Jun-13
Royal Bank of Canada Bond	1,031,000	5.45%	04-Nov-13
Canada Housing Trust	2,031,140	2.20%	15-Mar-14
Bank of Montreal Deposit Note	1,961,000	4.78%	30-Apr-14
Canada Housing Trust	3,991,830	2.75%	15-Dec-14
Royal Bank Deposit Note	2,474,750	4.71%	22-Dec-14
Canada Housing Trust	3,053,505	2.95%	15-Mar-15
Saskatchewan Province	2,990,386	4.25%	03-Dec-15
Ontario Province	3,969,200	4.40%	08-Mar-16
Bank of Montreal Bond	991,000	5.10%	21-Apr-16
New Brunswick Province	1,060,300	4.70%	21-Jul-16
Canada Housing Trust	2,025,980	1.85%	15-Dec-16
Royal Bank of Canada Bond	1,991,150	3.66%	25-Jan-17
Canadian Imperial Bank Deposit Note	1,521,905	3.95%	14-Jul-17
Ontario Province	3,985,200	1.90%	08-Sep-17
Manitoba Province	1,053,400	4.70%	22-Sep-17
Ontario Province	4,024,600	4.20%	08-Mar-18
Quebec Province	2,032,760	4.50%	01-Dec-18
Canada Housing Trust	5,789,934	4.10%	15-Dec-18
Alberta Province	2,034,530	4.00%	01-Dec-19
British Columbia Province	3,602,535	4.10%	18-Dec-19
British Columbia Province	3,466,185	3.70%	18-Dec-20
Scotia Private Short-Mid Government Bond Pool Note (A)	19,437,781	3.42%	15-Jun-14 to 15-Mar-22
Total Externally Managed Fixed Income	\$ 86,270,435		
Total Investments	\$ 123,542,135		
Total Investment Portfolio (General and Reserve Funds) Note (B)	\$ 465,657,784		
Note: ^(A) Contains Canada Housing Trust, Province of Quebec, Ontario, Nova Scotia and New Brunswick Bonds, weighted average yield 3.42%			
Note: ^(B) Monthly average balance of portfolio held for 2012 was \$459,638,124, average annual return 1.80%			