

<b>TO:</b>	<b>CHAIR AND MEMBERS CORPORATE SERVICES COMMITTEE MEETING ON JUNE 2, 2015</b>
<b>FROM:</b>	<b>MARTIN HAYWARD MANAGING DIRECTOR, CORPORATE SERVICES AND CITY TREASURER, CHIEF FINANCIAL OFFICER</b>
<b>SUBJECT:</b>	<b>2014 INVESTMENT REPORT</b>

<b>RECOMMENDATION</b>
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That, on the recommendation of the Managing Director, Corporate Services and City Treasurer, Chief Financial Officer, the 2014 Investment Report **BE RECEIVED** for information.

<b>BACKGROUND</b>
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The City of London maintained a monthly average investment portfolio of \$617 million in 2014 (2013, \$549 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 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 2014 focused on building a balanced portfolio, with the goal to move the current portfolio closer towards the City's investment policy targets. Comparisons of the City's portfolio as at December 31, 2014 to the previous year and policy targets are shown below.

<b>Classification</b>	<b>Description</b>	<b>% of Portfolio (Dec 31, 2014)</b>	<b>% of Portfolio (Dec 31, 2013)</b>	<b>Target</b>
Cash & Short-Term	Maturing in less than 1 year	60%	72%	50%
Medium-term	Maturing in 1 – 5 years	24%	11%	25%
Long-term	Maturing in more than 5 years	16%	17%	25%

The City moved closer towards the targets by investing reserves and reserve fund cash that was available for the medium-term (1 – 5 years). A total of \$103 million was invested throughout 2014, including \$55 million in an externally managed medium-term portfolio with Scotia Institutional Asset Management and \$48 million managed internally through investment brokers.

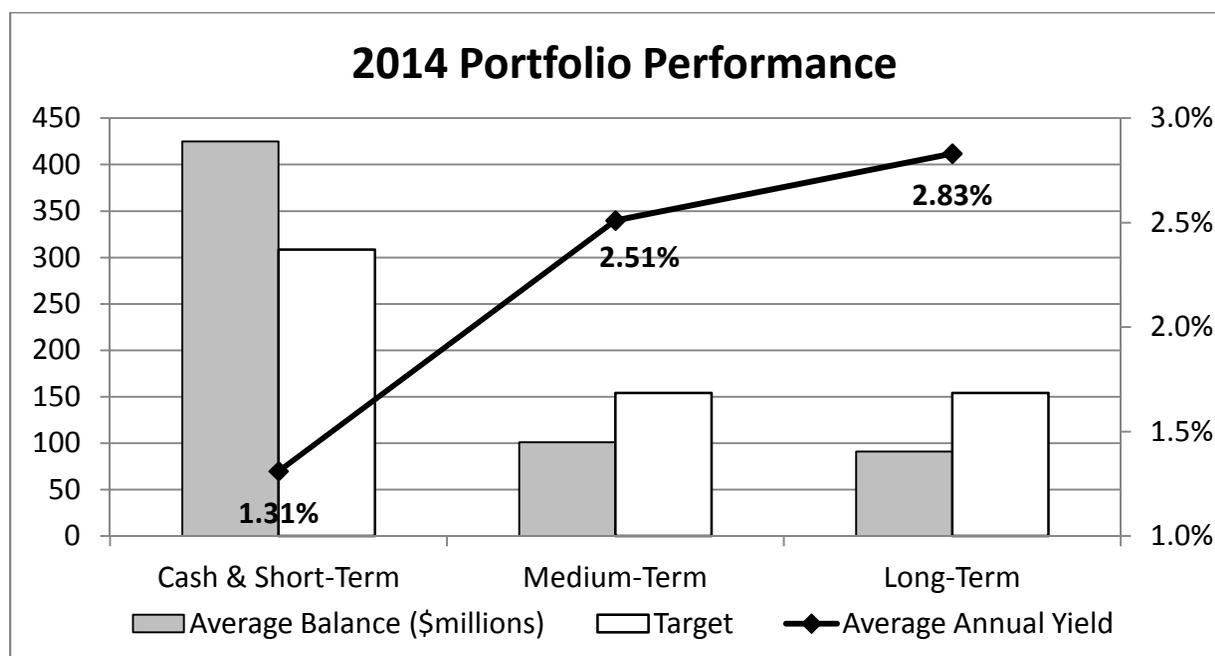
The City's externally managed portfolios are actively managed with Scotia Institutional Asset Management. The active management of these portfolios allows the City to benefit from the services provided by a sophisticated investment team, which includes frequent monitoring and trading, diversifying funds, and anticipating interest rate changes. It is anticipated that the higher returns offered by an actively managed portfolio will exceed the cost of administration. Income earned through externally managed portfolios is re-invested.

The City's internally managed portfolio utilizes the buy and hold strategy, buying investment products from investment brokers at varying maturity dates and withdrawing income earned. This strategy ensures a steady stream of cash flows will be available to match cash demands and minimizes interest rate risk by smoothing fluctuations in the market over time. In 2014, the City added four additional investment broker accounts as part of the City's strategy to diversify and ensure the most competitive investment yields are obtained.

The 2015 investment strategy will continue to focus on building a balanced portfolio, with the goal to move the current portfolio closer towards the City's investment policy targets.

**Performance of Portfolio Investments**

The chart below shows a breakdown of the average annual yield for 2014, as well as the investment portfolio balance in comparison to policy targets.



**Cash & Short-Term**

In 2014, the City had an average of \$425 million in cash earning interest at an average rate of 1.31%. This City's regular bank account earns interest at bank prime less 1.75% (1.25% for 2014). The City also has a premium interest rate savings account, earning between 0.10% and 0.25% above the City's regular bank account in 2014. Depending on seasonal cash flow needs, the City had between \$75 million and \$150 million in its premium interest rate savings account during 2014. A large proportion of cash is being held in the bank primarily due to yields on short-term investments (< 1 year) being lower than interest earned in the bank. For 2014, the Bank of Canada overnight target rate remained at 1.0%, while the average yield on 3-month Treasury Bills was 0.92%.

**Medium-Term**

In 2014, the City had an average of \$101 million in investments with a maturity of one to five years from original purchase date (\$49 million externally managed, \$52 million internally managed). The average yield on these investments for 2014 was 2.51% (net of fees).

The City's externally managed medium-term portfolio is compared to the FTSE TMX Canada Short-Term All Government Bond Index, which is similar in duration and composition to the City's portfolio. The FTSE TMX Canada benchmarks provide performance standards for Canadian fixed income investments and are one of the broadest and most widely used measures of performance of marketable government and corporate bonds outstanding in the Canadian market, noting that not all the bonds within the indices would meet the guidelines in terms of credit quality, liquidity, and term to maturity. The City's portfolio outperformed the benchmark by 0.07%. The positive variance relative to the index was primarily attributable to the higher yielding corporate bonds held within the portfolio relative to the all government bond index. The City's externally managed medium-term portfolio had an average yield 2.46% (net of fees) in 2014.

The internally managed investments had an average yield of 2.56%. The internally managed portfolio has laddered securities with purchases from 2011 to present. The yields in 2011 were higher than those in the latter part of 2013 when the externally managed portfolio was initiated. This contributes to the 0.10% net performance gain of the internally managed portfolio over the externally managed portfolio.

### Long-Term

In 2014, the City's long-term investment portfolio had an average balance of \$91 million. The City's long-term portfolio is externally managed with Scotia Institutional Asset Management, and had an average yield of 2.83% (net of fees) in 2014.

This portfolio is compared to the FTSE TMX Canada Short/Mid All Government Blend Bond Index, which is similar in duration and composition to the City's portfolio. The City's long-term portfolio underperformed against the benchmark by 0.90%.

The underperformance can be attributed to the duration positioning of the portfolio. The portfolio ended the year with duration of 4.2 years relative to the index of 4.6 years. The relatively shorter duration resulted from anticipation of an interest rate hike by the U.S. Federal Reserve followed by a similar rate hike by the Bank of Canada as the U.S. economy continues to expand and employment strengthens. However, looking ahead to 2015, the unexpected rate cut from the Bank of Canada in response to the negative effects that a weaker price of oil would have on our economy, at least in the short term benefited the portfolios that were longer in duration as bond yields fell. Scotia Institutional Asset Management expects that Canada will experience stronger exports from foreign demand, increased business confidence and investment, and employment growth. Thus given their economic view, the portfolio is positioned for improving growth and eventually higher rates.

### **Eligible Investments (Statement of Compliance)**

The Municipal Act, 2001 stipulates that a municipality may invest in securities prescribed under Ontario Regulation 438/97. A complete listing of the City's investments held as at December 31, 2014 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. On August 6, 2014 a City of London Debenture, \$250,000 par value, coupon rate 5.75%, matured. This security was purchased on March 4, 2002 and had a coupon rate of 5.75%. At the end of 2014, the City did not hold any of its own securities in comparison to 2013, in which the proportion was 0.2% of total investments (excludes cash).

### **Investment income**

The Municipal Act, 2001, S.O. 2001, c.25 subsection 418 (2) and (4) 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 fund 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 2014, the City earned a total income of \$10,675,430 (\$9,724,246 in 2013) from investments of which \$7,849,554 (\$7,153,877 in 2013) was earned from reserve fund investments and \$2,825,876 (\$2,570,369 in 2013) was earned from general fund investments.

### **Looking Ahead**

With the oil price shock in mind, the Bank of Canada lowered its Overnight Target Rate from 1.0% to 0.75% on January 21, 2015. As a result, the interest rate on the City’s regular bank account and premium interest rate account lowered by 0.15%, and there was a significant drop in benchmark bond yields (a 5-year Government of Canada benchmark bond yield dropped from 1.34% in December 2014 to 0.69% in January 2015). The Bank of Canada Overnight Target Rate is not forecasted to increase until the fourth quarter of 2016 (TD Economics April 8, 2015).

### **Acknowledgements**

This report was prepared jointly with Rick Lamon, Manager of Modelling, Forecasting & Systems Control.

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**APPENDIX A - City of London Investment Portfolio as at December 31, 2014**

Instrument	Cost	Coupon Rate	Maturity Date (DD-MM-YR)
<b>Cash Held in the Bank &amp; Short-Term Investments:</b>			
General Cash	\$ 115,431,285	1.31%	
Reserve Fund Cash	188,091,314	1.31%	
CIBC Deposit Note	5,000,000	2.00%	17-Feb-15
Royal Bank GIC	999,040	1.45%	17-Mar-15
Royal Bank GIC	699,968	3.65%	25-May-15
Bank of Nova Scotia GIC	100,070	2.00%	28-May-15
Bank of Monreal GIC	4,000,000	1.96%	07-Aug-15
Bank of Monreal GIC	16,000,000	1.91%	04-Sep-15
CIBC Term Deposit	4,000,000	1.81%	15-Oct-15
Toronto-Dominion Bank	1,991,000	3.37%	02-Nov-15
<b>Total Cash &amp; Short-Term Investments</b>	<b>\$ 336,312,677</b>		
<b>Medium-Term Investments:</b>			
Bank of Montreal Residual	\$ 8,771,700	2.72%	08-Jul-16
Bank of Monreal GIC	3,000,000	2.01%	08-Aug-16
Bank of Monreal GIC	12,000,000	2.10%	06-Sep-16
CIBC Term Deposit	6,000,000	2.09%	17-Oct-16
Bank of Nova Scotia GIC	3,984,000	2.01%	19-Dec-16
Royal Bank GIC	3,000,000	2.31%	08-Aug-17
Bank of Monreal GIC	2,000,000	2.26%	05-Sep-17
Bank of Montreal Residual	7,760,000	3.82%	26-Sep-17
CIBC Term Deposit	3,000,000	2.19%	15-Oct-17
Bank of Nova Scotia GIC	1,988,000	2.13%	18-Dec-18
<b>Scotia Institutional Asset Mgmt Portfolio (Medium-Term)</b>			
Cash	12,304	0.40%	
National Bank of Canada	1,016,844	3.15%	11-Feb-15
Royal Bank of Canada	2,033,618	3.18%	16-Mar-15
Canada Government T-Bill	2,108,463	0.90%	09-Apr-15
Bank of Montreal	3,509,005	1.89%	05-Oct-15
New Brunswick Province	2,616,388	4.30%	03-Dec-15
Ontario Province	2,090,129	4.40%	08-Mar-16
Canada Housing Trust	15,281,431	2.75%	15-Jun-16
Toronto-Dominion Bank	2,053,137	2.95%	02-Aug-16
CIBC	1,020,836	2.65%	08-Nov-16
Ontario Province	4,304,614	4.30%	08-Mar-17
Toronto-Dominion Bank	2,027,701	2.43%	15-Aug-17
Ontario Province	2,003,505	1.90%	08-Sep-17
Royal Bank of Canada	2,021,265	2.36%	21-Sep-17
Manitoba Province	2,207,570	4.70%	22-Sep-17
CIBC	2,008,941	2.35%	18-Oct-17
Quebec Province	2,187,253	4.50%	01-Dec-17
BC Province	5,090,348	2.25%	01-Mar-19
Province of Alberta	3,520,985	2.00%	01-Jun-19
Canada Housing Trust	24,085,065	1.95%	15-Jun-19
Total Scotia Portfolio (Medium-Term)	81,199,400		
<b>Total Medium-Term Investments</b>	<b>\$ 132,703,100</b>		

**APPENDIX A - City of London Investment Portfolio as at December 31, 2014 - Continued**

Instrument	Cost	Coupon Rate	Maturity Date (DD-MM-YR)
<b>Long-Term Investments <i>Note (A)</i>:</b>			
Scotia Institutional Asset Mgmt Portfolio (Long-Term)			
Cash	\$ 20,514	0.40%	
Canada Government T-Bill	1,539,102	0.90%	09-Apr-15
Bank of Montreal	2,014,382	1.89%	05-Oct-15
Ontario Province	2,495,170	4.40%	08-Mar-16
Bank of Montreal	996,761	5.10%	21-Apr-16
Canada Housing Trust	14,434,400	2.75%	15-Jun-16
Royal Bank of Canada	2,002,724	3.66%	25-Jan-17
CIBC Deposit Notes	2,090,109	3.95%	14-Jul-17
Ontario Province	5,026,147	1.90%	08-Sep-17
Ontario Province	4,047,994	4.20%	08-Mar-18
Toronto-Dominion Bank	2,981,541	2.17%	02-Apr-18
Royal Bank of Canada	2,570,606	2.82%	12-Jul-18
Quebec Province	2,044,576	4.50%	01-Dec-18
Province of Alberta	5,068,864	2.00%	01-Jun-19
Quebec Province	2,210,173	4.50%	01-Dec-19
BC Province	3,623,476	4.10%	18-Dec-19
New Brunswick Province	2,208,765	4.50%	02-Jun-20
Toronto-Dominion Bank	1,011,043	2.56%	24-Jun-20
Nova Scotia Province	2,230,491	4.10%	01-Jun-21
New Brunswick Province	2,070,747	3.35%	03-Dec-21
Canada Housing Trust	26,721,505	2.65%	15-Mar-22
Ontario Province	5,073,571	3.15%	02-Jun-22
<b>Total Long-Term Investments</b>	<b>\$ 92,482,663</b>		
<b>Total Investment Portfolio</b>	<b>\$ 561,498,440</b>		
<b>Note: <sup>(A)</sup> This portfolio is deemed long-term as the intention of administration is to invest these funds for a period of more than five years.</b>			
<b>Cash balances as per bank accounts as at December 31, 2014.</b>			
<b>Cash and investment balances, unaudited.</b>			