City of Burnaby

Meeting 2017 February 06

COUNCIL REPORT

FINANCIAL MANAGEMENT COMMITTEE

HIS WORSHIP, THE MAYOR
AND COUNCILLORS

SUBJECT: CITY INVESTMENTS – 2016 YEAR END REPORT

RECOMMENDATION:

1. THAT this report be received for information purposes.

REPORT

The Financial Management Committee, at its meeting held on 2017 January 25, received and adopted the *attached* report providing a 2016 Investment Program update and presenting the 2017 Investment Program forecast.

Respectfully submitted,

Councillor D. Johnston
Chair

Councillor C. Jordan
Vice Chair

Councillor P. McDonell
Member

Copied to:	City Manager Director Finance

Meeting 2017 Jan 25

COMMITTEE REPORT

TO:	CHAIR AND MEMBERS FINANCIAL MANAGEMENT COMMITTEE	**DATE:**	2017 January 17
FROM:	DIRECTOR FINANCE	**FILE:**	7500-01

SUBJECT: **CITY INVESTMENTS – 2016 YEAR END REPORT**

PURPOSE: To provide a 2016 Investment Program update and to present the 2017 Investment Program forecast.

RECOMMENDATION:

1. **THAT** this report be received for information purposes.

REPORT

Part 6, Division 3, Section 183 of the Community Charter states that the City may invest or reinvest money that is not immediately required for expenditures. Council has assigned the responsibility for the management of the investment portfolio to the Director Finance (Bylaw No. 11553). This report highlights significant events that have occurred in the investment program during 2016 and the forecast for 2017.

The City's investments on 2016 December 31 totaled $1,100,947,412.54 (2015 – $923,955,890). This is represented by a single investment portfolio – City of Burnaby Investment Fund – and includes restricted funds such as Development Cost Charges and all other reserve funds. Schedule B lists the institutions the City invests in and the investment limits that have been placed on these institutions for 2017.

1.0 2016 SIGNIFICANT EVENTS

1.1 Investment Funds

A portion of the portfolio's investments is held in money market instruments until cash is required for expenditures. The City's Investment Fund is directly impacted by any movement in short-term interest rates during the year, particularly from July onward, when the investment fund significantly increases by over $1.4 billion upon receipt of tax revenue and then decreases to approximately $1.0 billion in May.

The Bank of Canada bank rate, which governs the level of short-term interest rates, opened the year at 0.75% and closed on 2016 December 31 at the same rate. The average yield for 90 day Bankers Acceptance's was 0.83%, one basis point lower than the average for 2015.

Despite the continuation of low annual yields throughout 2016 the City's investment strategy generated $44 million (3.62%) return on investments (2015 – $41.5 million at 3.91%). The impact of fluctuations in short-term interest rates on investment income is offset by a portion of fund surplus in longer term investment grade bonds with annual yields of 3.00% – 7.35%. These longer term investments have continued to provide income and yield stabilization for the portfolio year-over-year despite historical lows in money market and bond market yields. However, the percentage of the portfolio in these longer term investments has decreased as maturities have occurred.

In 2016, Canadian ten-year and thirty-year bond rates were volatile with yearly highs of 1.84% and 2.42% respectively and lows of 0.95% and 1.55% respectively. Both bonds saw lower average rates in 2016 with the ten-year bond average 1.25% (2015 – 1.52%) and the thirty-year bond average 1.92% (2015 – 2.19%).

An alternative investment option for British Columbia municipalities is to place funds with the Municipal Finance Authority of British Columbia (MFA-BC). The MFA-BC offers three investment fund alternatives and reports the returns annually, with the most recent information provided below for the period ending 2016 December 31, along with a corresponding yield for a comparable benchmark indices. All three funds offered by the MFA-BC include corporate debt. The Community Charter restricts the City from investing in corporate debt unless we invest directly into the MFA-BC's funds. The City's investments performed well in 2016 when broken down by term as a means of comparison to the Municipal Finance Authority (MFA) Pooled funds and noted indices benchmark returns as shown in Table 1.

Table 1 – Breakdown of Yield Comparisons

Fund Type	Fund/Benchmark	1 year return	City of Burnaby
Money Market	MFA Money Market Fund (for investments less than 1 year)	0.79%	1.47%
	MFA Custom Benchmark-FTSE TMX Canada 30-day T-Bill Index	0.32%	
Intermediate	MFA Intermediate Fund (for investments from 1 – 3 years)	1.13%	1.90%
	FTSE TMX Canada 365- Day Treasury Bill Index	0.23%	
Bond Fund	MFA Bond Fund* (for investments of more than 3 years)	1.43%	4.99%
	FTSE TMX Canada Short Term Overall Bond Index	0.81%	

* The MFA Bond Fund maximum term to maturity is seven years, the City of Burnaby's comparable includes all remaining portfolio investments with a term greater than three years.

Generally the portion of the Investment Fund that is not expected to be needed in the near future is invested in longer term investments with higher yields. Approximately $618 million is invested in long-term investments (one year and longer); the balance in shorter term investments that mature within one year.

Table 2 – Breakdown for Portfolio Maturities by Term at 2016 December 31

City of Burnaby Investment Fund	Face Value ($)	%	Cost Amount ($)	%
Maturities in 2017	515,869,053.00	35.06%	493,635,436.97	44.84%
Maturities 2018 to 2022	451,704,752.25	30.70%	336,322,896.71	30.55%
Maturities 2023 to 2027	256,914,574.00	17.46%	106,958,346.05	9.72%
Maturities 2028 +	246,771,465.00	16.77%	164,030,732.81	14.90%
Total	**1,471,259,844.25**		**1,100,947,412.54**	

1.2 Banking Relationships and Counterparties

The City of Burnaby's investment portfolio consists of debt issued by Canadian banks as identified in both Schedule A and Schedule B. Securities issued by the banks do not have an investment guarantee from the Canadian Federal Government. Retail depositors receive deposit insurance from the Canadian Deposit Insurance Corporation (CDIC) in the amount of $100,000 for investments with a term to maturity less than five years. The City of Burnaby is not considered a retail depositor and therefore, CDIC coverage does not apply. Treasury Operations monitors the counterparties that we invest as part of our ongoing risk mitigation strategy and investment procedures.

The City's investment banking relationships remained consistent during 2016 for long-term fixed income products. RBC Capital Markets, TD Securities, CIBC-Wood Gundy, Scotia Capital and Canaccord Genuity were the City's lead investment bankers. For short-term money market investments, the City invested with BC, Alberta and Saskatchewan Credit Unions who provided a premium over bank BA's and continue to receive investment guarantees by their respective insurance funds; the Credit Union Deposit Insurance Corporation in BC, the Credit Union Deposit Guarantee Corporation in Alberta and the Saskatchewan Credit Union Deposit Guarantee Corporation. While each is a legislated provincial government insurance corporation funded by the credit unions, in Alberta the Credit Union Act provides for the provincial guarantee of all Credit Union Deposit Guarantee Corporations obligations. The Province of British Columbia and the Province of Saskatchewan does not guarantee the liabilities of the respective provincial corporations.

The City's portfolio growth over the last decade means increased investment limits are required to remain well diversified. The City has made counterparty changes (identified in Schedule B) to provide increased product and investment diversification and to ensure the City's continued ability to deploy funds into the market with the flexibility that a large portfolio requires. Diversification is essential for managing investment risk and return.

The Province of British Columbia portfolio limit has been increased from $150 million to $160 million and the Province of Alberta limit has been increased from $140 million to $160 million. The remaining provincial limits have not been changed. For the five major Canadian, banks their limits have been increased from $150 million to $160 million each. National Bank has been increased by $20 million to $80 million.

Limits are unchanged for each individual credit union in BC; however the maximum limit for the BC credit union total has been increased by $10 million to $160 million. Alberta and Saskatchewan credit union limits have also increased by $10 million to $150 million and $60 million respectively. The Alberta and Saskatchewan credit union individual limits have increased by $5 million each.

2.0 OUTLOOK FOR 2017

At the end of 2016 the dichotomy between Canada and the US became greater as economic indicators for employment, growth, inflation and future central bank policy continues going in different directions. Globally, very accommodative interest rate policies remain in place. While Canada's output and economy has been slower in growth when compared to the US, Canada is still affected by commodity pricing and historically high household debt.

The challenges to maintain positive real returns on investments will become greater in 2017 and future years. Market volatility has increased due to many unknowns surrounding global security and leadership. This has meant varying degrees of market volatility, producing swings in price and yield.

A major concern for Canadian municipalities is the 2016 implementation of *Bill 15-C, Budget Implementation Act 2016, Division 5 – Bank Recapitalization Regime*. As a result of the 2007/2008 global recession and as a means of protecting tax payers from "bailing-out" Canadian financial institutions under extreme economic conditions, the legislation ensures risk is born by the debt holders of the banks. The intention is to have the banks issue long term investments into products that are convertible to common shares should a bank become non-viable. This will recapitalize the bank. However, the ramifications for the City of Burnaby under the *Community Charter* guidelines could mean a significant decrease in the bank investments we hold. Thus, shifting holdings to federal and provincial investments and short term GIC's that have lower yields and limited product access; the result being reduced yields and income for the City going forward.

Treasury staff is monitoring the activities around this legislation and await the impending Department of Finance Canada publication slated for mid-February that will provide specific and clear guidelines around the changes. From this we can determine the severity of the impact.

For the City of Burnaby, economic factors suggest that 2017 investments will continue to be affected by the extreme low interest rate environment. As longer term investments mature, reinvestment of large principal amounts at lower interest rates will result in lower annual portfolio yields and lower income. The City is projecting an annual yield of 3.00% for 2017 and $40.5 million in investment income. Of this investment income amount, $6 million is the current 2017 operating budget contribution (2016 – $6.5 million) with the remainder of funds distributed to reserve funds.

3.0 CONCLUSION

Diversification and a conservative investment strategy have provided the City with a 2016 return of $44 million at an annual yield of 3.62% on the City's Investment Fund. For 2017, Treasury Operations will continue to monitor money and fixed income markets for investment opportunities to provide liquidity, capital preservation and yield management.

Denise Jorgenson
DIRECTOR FINANCE

DJ:DS/mm

Attachments: *Schedule A – 2016 City of Burnaby Investments Update*
Schedule B – 2017 City of Burnaby Investment Limits

Copied to: City Manager

SCHEDULE A

2016 City of Burnaby Investments Update

Dominion Bond Rating Service (DBRS) is the leading Canadian institutional credit rating agency, the authority on the fiscal strength of financial and governmental bodies.

Schedule B provides an updated listing of each institution and the limits currently in place for the combined capital and operating investment portfolios. The investment portfolio contains a preferred mix by category of security and maintains a dollar limits for each investment issuer.

Table 1 provides a breakdown of the ratings used in Schedule B:

Tab1e 1 – DBRS Ratings

Term	Meaning
Schedule I Bank	Canadian-owned Bank
Schedule II Bank	Foreign-owned Bank
Senior Debt	A bond or other form of debt that takes priority over other debt securities sold by the issuer.
Subordinated Debt	A bond or other form of debt that ranks below senior debt but higher than other debt securities sold by the issuer.
Not Rated	Financial Institutions who do not require a rating agencies review of their financial position. This decision is typically associated with the type of debt the institution issues.
DBRS investment quality categories for short-term securities:	
R-1	High (investment grade) credit quality
R-2	Medium (average grade) credit quality
R-3	Low (speculative) credit quality
High	The relative standing within each rating classification, e.g. R-1 High is, by definition the highest credit quality available.
Middle	
Low	
DBRS investment quality categories for bonds and long-term debt are:	
AAA	Highest quality credit
AA	Superior credit
A	Upper mid grade credit

CITY OF BURNABY

SCHEDULE B

INVESTMENT LIMITS FOR 2017

SECURITIES CATEGORY	*Short-term Investments* DBRS Ratings	*Long-term Investments* DBRS Ratings	Investment Limits	Portfolio % Mix
Federal & Federal Guaranteed	R1 – High	AAA	No Limit	
TOTAL FEDERAL & FEDERAL GUARANTEED			No Limit	No Limit
Coast Capital Savings CU ($60M max)	Not Rated	Not Rated		
Gulf & Fraser Credit Union ($30M max) (dba G&F Financial)	Not Rated	Not Rated	$ 160,000,000	
North Shore Credit Union ($30M max) (aka BlueShore Financial)	Not Rated	Not Rated		
VanCity Savings CU ($60M max)	R1 – Low	Not Rated		
Westminster Savings CU ($30M max)	Not Rated	Not Rated		
TOTAL BRITISH COLUMBIA CREDIT UNIONS *			$ 160,000,000	25% Max.
Servus Credit Union ($75M max)	Not Rated	Not Rated	$ 150,000,000	
First Calgary Financial ($75M max)	Not Rated	Not Rated		
TOTAL ALBERTA CREDIT UNIONS **			$ 150,000,000	25% Max.
Conexus Credit Union ($30M max)	Not Rated	Not Rated	$ 60,000,000	
Affinity Credit Union ($30M max)	Not Rated	Not Rated		
TOTAL SASKATCHEWAN CREDIT UNIONS ***			$ 60,000,000	10% Max.
Alberta	R1 – High	AA High	$ 160,000,000	
British Columbia	R1 – High	AA High	$ 160,000,000	
Manitoba	R1 – Middle	A High	$ 70,000,000	
New Brunswick	R1 – Middle	A High	$ 70,000,000	
Nova Scotia	R1 – Middle	A High	$ 70,000,000	
Ontario	R1 – Middle	AA Low	$ 100,000,000	
Prince Edward Island	R1 – Low	A Low	$ 60,000,000	
Saskatchewan	R1 – High	AA	$ 100,000,000	
Quebec	R1 – Middle	A High	$ 90,000,000	
TOTAL PROVINCES			$ 880,000,000	60% Max.
Bank of Montreal	R1 – High	AA	$ 160,000,000	
CIBC	R1 – High	AA	$ 160,000,000	
Royal Bank	R1 – High	AA	$ 160,000,000	
ScotiaBank	R1 – High	AA	$ 160,000,000	
Toronto Dominion Bank (aka TD-Canada Trust)	R1 – High	AA	$ 160,000,000	
Canadian Western Bank	R1 – Low	A Low	$ 60,000,000	
Manulife Bank of Canada	R1 – Middle	A High	$ 60,000,000	
National Bank of Canada	R1 – Middle	AA Low	$ 80,000,000	
TOTAL SCHEDULE 'I' BANKS			$ 1,000,000,000	60% Max.
TOTAL SCHEDULE 'II' BANKS			$ 0	10% Max.

** British Columbia Credit Unions are CUDIC guaranteed*

*** Alberta Credit Unions are CUDGC guaranteed and ensured by the Province of Alberta*

**** Saskatchewan Credit Unions are CUDGC guaranteed*