

**TO:** CHAIR AND MEMBERS  
FINANCIAL MANAGEMENT COMMITTEE

**DATE:** 2019 May 15

**FROM:** DIRECTOR FINANCE

**FILE:** 7500-01

**SUBJECT:** CITY INVESTMENTS - MUNICIPAL FINANCE AUTHORITY - NEW MORTGAGE FUND

**PURPOSE:** To provide an update on the new Municipal Finance Authority Mortgage Fund.

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**RECOMMENDATION:**

1. **THAT** the Financial Management Committee receive this report as information.

**REPORT****1.0 INTRODUCTION**

The Director Finance provided a memorandum dated 2019 March 15 to the Chair and Members of the Financial Management Committee to advise of the development of a new Municipal Finance Authority of British Columbia (MFABC) Mortgage Fund. The MFABC also currently has 3 pooled funds for BC municipalities to invest; the Money Market, Intermediary and Bond funds all managed by Phillips, Hager & North (PH&N). This report will provide an update and the next steps for the City of Burnaby to invest in the new MFABC Mortgage Fund.

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 expenditure; and subsection (a) allows for investments in “securities of the Municipal Finance Authority”. Council has assigned the responsibility for the management of the investment portfolio to the Director Finance (Bylaw No. 11553).

**2.0 POLICY SECTION**

The investment activities have a positive impact on the community through alignment with the City of Burnaby’s Corporate Strategic Plan by supporting the following goals and sub-goals:

- A Connected Community
  - Partnership –  
Work collaboratively with businesses, educational institutions, associations, other communities and governments

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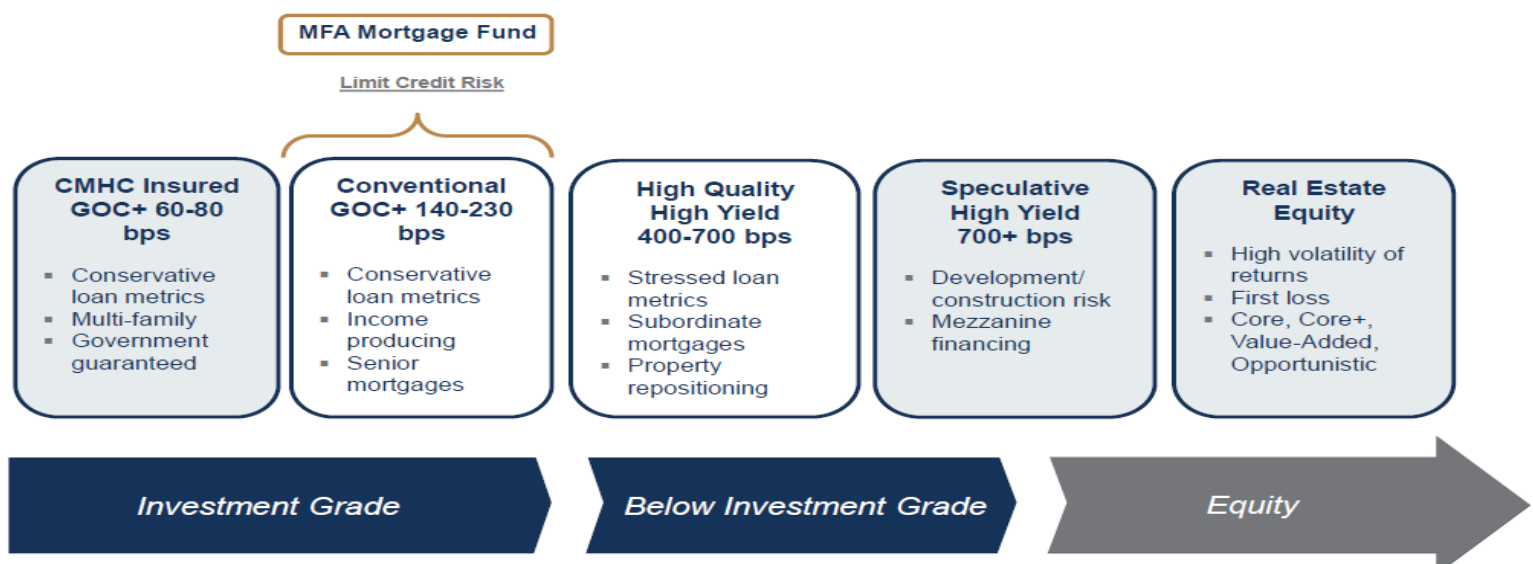
- A Dynamic Community
  - Economic opportunity –  
Foster an environment that attracts new and supports existing jobs, businesses and industries
- A Thriving Organization
  - Organizational culture –  
Ensure that our core values are reflected in our policies, programs and service delivery
  - Financial viability –  
Maintain a financially sustainable City for the provision, renewal and enhancement of City services, facilities and assets

### 3.0 BACKGROUND

The new MFABC Mortgage Fund will participate in the PH&N Mortgage Pension Trust which is an existing \$4 billion closed fund created in November 2001; however, PH&N has been providing clients with mortgage investment funds since 1974. Client mortgage investments were amalgamated into the Trust in 2001 to simplify operations, provide purchasing power and lower costs.

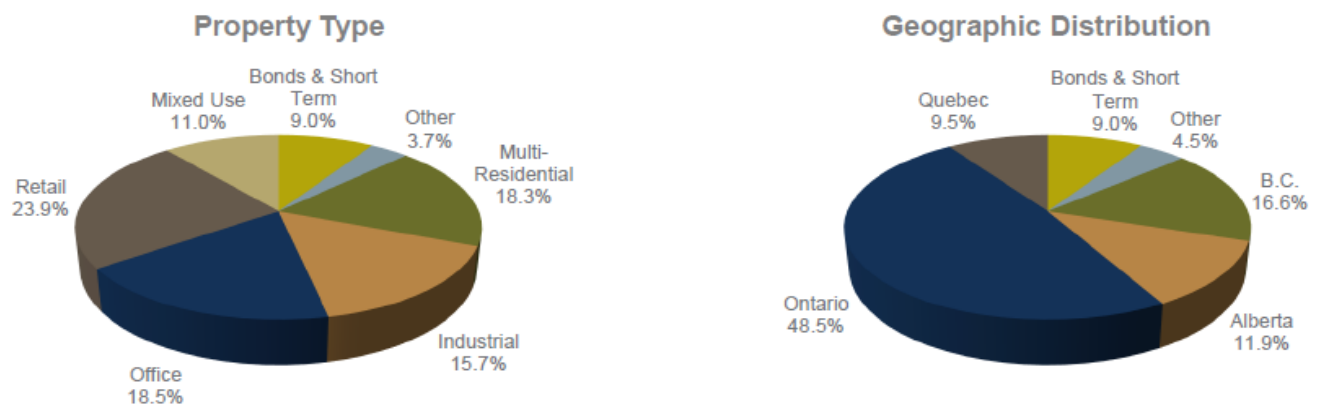
A consortium of lower mainland municipalities recently met to discuss and plan the finer details of the new MFABC Pooled Fund. There is much interest in this fund as this represents asset class diversification with higher yield potential than most municipalities can currently obtain in the markets or the other pooled funds. The PH&N Mortgage Pension Trust (MPT) focuses on conventional mortgages at a spread of 140-230 basis points above Government of Canada five year bonds. As shown in table 1 below, even within an asset class such as mortgages, there are varying degrees of investment products and associated risks. The MFABC Mortgage Fund will hold investment grade first mortgages only.

**Table 1: MFA Mortgage Fund investment focus (Source: MFABC/PH&N (April 2019))**



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The MPT currently maintains a 59% loan to value ratio on Canadian first mortgages on revenue producing properties; both commercial and residential. The mortgages are carefully selected to ensure stable net operating income with a high degree of debt servicing coverage. There has never been a default in the MPT. The graphs below provide details about the current asset distribution by property type and geographic distribution across Canada.



<sup>1</sup> Over equivalent term Canada issues

Yield is reported on a gross-of-fee basis, Series O, standard performance available in the appendix

\* Excludes interest only mortgages which represent 11.6% of the total mortgages

(Source: MFABC/PH&N (April 2019))

Furthermore, as a way of providing added liquidity to the portfolio, the investments into the fund will be invested 85% into the MPT and 15% into liquid short term bonds similar to the MFABC Bond Fund. Even though liquidity is being added to the fund for redemptions, municipalities will sign an authorization of deposit letter, confirming their understanding of the long term investment time frame. Funds required for cash flow or other liquidity needs should not be invested in this new fund.

Current legislation within the Community Charter restricts municipalities from investing in mortgage funds directly however allows MFABC to do so. Therefore municipalities can currently only capitalize on such an investment through MFABC. With all MFA Pooled funds, the investments are not guaranteed by the MFA or PH&N, who manages the investment funds. The pooled funds are investments in allowable products as stipulated under Section 16 of the Municipal Finance Authority of BC Act. The Act provides for a wider range of investment product types and guarantors than the Community Charter does for direct investing by a municipality.

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#### **4.0 INVESTMENT OPPORTUNITY**

Treasury Services within the Finance Department is currently reviewing the operational requirements (account entry, reconciliation, investment and income recognition) to prepare for an initial investment of \$25 million. Finance will set a cap of \$50 million which represents 2.94% of the City's \$1.7 billion portfolio. This allows the City the flexibility to slowly increase holdings as economic and market conditions continually change. Furthermore, Finance will update investment limits to reflect the holdings in the MFA pooled funds in both dollar amount and as a percentage of the total portfolio. It is expected the fund will launch in June/July 2019. However, new deposits are staged and deposited only when the new mortgages are funded. So transfer of money into the fund may not occur until October/November.

Investing in the new MFABC Mortgage Fund provides for asset class diversification for the City of Burnaby. Further diversification is prudent within our investment strategy and risk management of a municipal portfolio. The nature of the fund also provides the City with an increased yield opportunity for long term sustainability. Treasury's approach is to consider these funds a longer term commitment of 5-10 years and possibly longer. Several investors have been in the PH&N MPT since inception and holding real estate investment assets for even much longer for asset class diversification. The rate of return on this new fund in conjunction with economic cycles and interest rate movements will determine the time horizon on the investment in the funds for the City of Burnaby.

The current annualized yield on the PH&N MPT is 2.88% with a 5 year and 10 year historical return of 3.46% and 4.40% respectively. The fund has a target range yield between +140 to +230 basis points over the Canada 5 year bond which is currently yielding 1.54%; hence a targeted annual return between 2.94% and 3.84%. In 2018 the City's portfolio return was a respectable 3.16%; however, the City's yield and income will continue to be impacted since our longer term investments with yields earning between 4.00% - 7.00% are slowly maturing and interest rates are still near historical lows.

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## 5.0 CONCLUSION

The City will invest an initial \$25 million into the new MFABC Mortgage Fund to a maximum of \$50 million. While representing less than 3% of the City's current portfolio, the initial investment will allow the City the flexibility to increase our holdings when we are ready as this is a new fund and asset class and the City has no prior investments in MFABC pooled funds. These are funds that are not required for short term cash flow needs and can be invested for the longer term. When investing in such a product, a longer time horizon provides for a smoothing effect of the daily price and short term fluctuations of the fund as interest rates change and other variables impact the fund. Some of the existing funds and investors in the MPT have been invested since 2001 which attests to the steady and longer term growth intention of the fund.

It is recommended that the Financial Management Committee receive this report as information.



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DIRECTOR FINANCE

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Copied to: City Manager