MARKHAM

Report to: General Committee | Report Date: Feb 3, 2014

SUBJECT: 2013 Investment Performance Review
PREPARED BY: Mark Visser, Senior Manager of Financial Strategy & Investments x.4260

RECOMMENDATION:

1) THAT the report dated February 3, 2014 entitled "2013 Investment Performance Review" be received;

2) AND THAT staff be authorized and directed to do all things necessary to give effect to this resolution.

EXECUTIVE SUMMARY:
Not applicable

FINANCIAL CONSIDERATIONS:
Not Applicable

PURPOSE:

Pursuant to Regulation 74/97 Section 8, the Municipal Act requires the Treasurer to "prepare and provide to the Council, each year or more frequently as specified by Council, an investment report".

The investment report shall contain,

(a) a statement about the performance of the portfolio of investments of the municipality during the period covered by the report;

(b) a description of the estimated portion of the total investments of a municipality 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 were made in accordance 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;

(e) such other information that the Council may require or that, in the opinion of the Treasurer, should be included.

BACKGROUND:

For the year ending December 31, 2013, the City of Markham's Income Earned on Investments was $10.464 million, compared to a budget of $10.350 million, representing a $0.114 million favourable variance.

The 2013 budget assumed an average general fund portfolio balance of $258.8 million to be invested at an average rate of return of 4.00%. The actual average portfolio balance was lower than budgeted levels, however, the average rate of return was higher than budgeted levels. The details of these two factors will be discussed below.

Interest Rate

Throughout 2013, the Bank of Canada Prime Rate was at 3.00%, with short-term money market rates in the 1.00-1.40% range. As well, bond rates continued to be at relatively low levels as investors sought out less risky investments. The City was able to take advantage of these low rates by selling some it its bond holdings and realizing Capital Gains.

In 2013, the City's investments had an average interest rate of 3.95%, 5 basis points lower than the forecast. However, through active bond trading, the City realized $0.964 million of Capital Gains, thereby increasing the actual rate of return to 4.35%; 35 points higher than the 4.00% forecasted rate. The difference in the rate of return accounts for a favourable variance of $0.844 million.

Portfolio Balance

The budgeted average portfolio balance for 2013 was $258.8 million. The actual average general fund portfolio balance (including cash balances) for 2013 was $240.5 million. The lower portfolio balance accounts for an unfavourable variance of $0.730 million.

Variance Summary

	Budget	Actual	Variance
Portfolio Balance	$258.8m	$240.5m	($15.3m)
Interest Rate	4.00%	4.35%	0.35%
Investment Income	$10.350m	$10.464m	**$0.114m**

Portfolio Balance Variance Impact	**($0.730m)**
Interest Rate Variance Impact	**$0.844m**

Portfolio Composition

All investments made in 2013 adhered to the City of Markham investment policy. At December 31, 2013, 56% of the City's portfolio was comprised of government issued securities and 44% of the portfolio was made up of instruments issued by Schedule A Banks. All of these levels are within the targets established in the City's Investment Policy. (Exhibit 1).

The December 31, 2013 investment portfolio was comprised of the following instruments: Bonds 79%; GICs 12%; T-Bills 9% (Exhibit 2).

At December 31, 2013, the City's portfolio balance for all funds was $333.6 million (including bank balances). DCA investments represented $91.2 million of this amount. The City's portfolio (all funds excluding DCA) of $242.4 million was broken down into the following investment terms (Exhibit 3):

	2013	2012
Under 1 month	6.8%	13.1%
1 month to 3 months	0.0%	4.5%
3 months to 1 year	9.5%	21.5%
Over 1 year	83.6%	60.8%
Weighted average investment term	2,389.9 days	1,980.5 days
Weighted average days to maturity	1,445.2 days	1,216.2 days

Since December 31, 2012, the weighted average days to maturity has increased from 1,216.2 days to 1,445.2 days. This reflects the strategy of the City selling some of its shorter duration bonds and reinvesting in longer duration bonds.

Money Market Performance

The City of Markham uses the 3-month T-bill rates to gauge the performance of investments in the money market. The average 3-month T-bill rate for 2013 was 0.97% (source: Bank of Canada). Non-DCA Fund money market investments held by the City of Markham in 2013 (including bank balances) had an average return of 1.28%. Therefore, the City's money market investments outperformed 3-month T-Bills by 31 basis points. See Exhibit 4 for all Money Market securities held by the City of Markham in 2013.

Bond Market Performance

The 2013 highlights of the bond portfolio are as follows:

- 15 bonds were purchased with a face value of $67.9 million
- 15 bonds matured with a face value of $55.0 million
- 5 bonds were sold with a combined face value of $14.5 million
- $964,000 of Capital Gains were realized

At December 31, 2013, the City held 73 bonds in the general fund portfolio. The amortized value of these bonds at year-end was $232.2 million. The market value of these bonds at December 31, 2013 was $238.2 million. This translates into $6.0 million of unrealized gains at year end.

For much of 2013, bond rates were once again at extremely low levels. This created a good selling opportunity, where Markham was able to sell 5 bonds (with a combined face value of $14.5 million) and earn $964,000 of capital gains. It was not until the end of 2013 that the bond rates began to rise. If the rates continue to increase in 2014, it will represent a good buying opportunity for Markham. See Appendix 5 for all 2013 bond transactions.

Reserve Funds and Other Interest
The following table outlines the interest earned on investments for all major City funds and reserves.

	Average Balance	Interest Earned	Average Rate
General Portfolio	$240,500,000	$10,464,000	4.35%
Reserve Funds	$126,700,000	$1,576,000	1.24%
Trust Funds	$2,300,000	$87,000	3.77%
Powerstream Promissory Note	$67,900,000	$3,787,000	5.58%
MEC/District Energy Loans	$16,800,000	$871,920	5.19%
Development Charge Reserves	$86,400,000	$1,023,000	1.18%

Because of the large swing in portfolio balances throughout the year (due to the timing of the collection and disbursement of taxes), there will always need to be a significant portion of the City's funds invested in the money market.

The City's Interest Allocation Policy (as approved by Council) stipulates that money market rates be allocated to the interest bearing reserves and bond interest be allocated to the general portfolio. The reasons for this are 1) over the long term, bond rates generally outperform money market rates, therefore the City is able to achieve higher rates of return in its general portfolio and thereby reducing the immediate need for tax increases; 2) bond market rates are more stable which allows for smoother budgeting; and 3) reserves and reserve funds can more easily absorb these money market rate fluctuations as the requirements for these funds are longer term in nature.

The average rate earned for the Development Charge Reserves is also low as the majority of investments need to be kept short term, as it is forecasted that the reserves will be depleted by 2015.

OPTIONS/ DISCUSSION:

Outlook
Although rates have been low for a sustained period of time, the City is still well positioned to weather the current environment. At the beginning of 2014, the City's amortized bond and long term accrual investments balance was approximately $232.2

million, with approximately 75% of that amount locked in until at least 2016 at comparatively attractive rates.

The Investment Income budget for 2014 is $10.35 million (unchanged from the 2013 budget). This is comprised of an estimated $250.0 million general portfolio balance invested at an average rate of 4.14%.

FINANCIAL TEMPLATE (Separate Attachment):
Not applicable

ENVIRONMENTAL CONSIDERATIONS:
Not applicable

ACCESSIBILITY CONSIDERATIONS:
Not applicable

ENGAGE 21ST CONSIDERATIONS:
Not applicable

BUSINESS UNITS CONSULTED AND AFFECTED:
[Insert text here]

RECOMMENDED BY:

28/01/2014

X Joel Lustig

Joel Lustig
Treasurer

28/01/2014

X Trinela Cane

Trinela Cane
Commissioner, Corporate Services

ATTACHMENTS:

Attachment 1:

- Exhibit 1 – Investment Portfolio by Issuer
- Exhibit 2 – Investment Portfolio by Instrument
- Exhibit 3 – Investment Terms
- Exhibit 4 – 2013 Money Market Investments
- Exhibit 5 – 2013 Bond Market Investments
- Exhibit 6 – 2013 DCA Fund Investments