



City of Richmond

Report to Committee

To: Finance Committee

Date: January 11, 2017

From: Jerry Chong
Director, Finance

File: 03-0900-01/2017-Vol
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Re: 2016 Investment Report

Staff Recommendation

That the report titled 2016 Investment Report dated January 11, 2017 from the Director, Finance be received for information.

Jerry Chong
Director, Finance
(604-276-4064)

REPORT CONCURRENCE	
CONCURRENCE OF GENERAL MANAGER 	
REVIEWED BY STAFF REPORT / AGENDA REVIEW SUBCOMMITTEE	INITIALS: DW
APPROVED BY CAO 	

Staff Report

Origin

This report provides an overview of the City's investment position for fiscal year 2016.

This report supports Council's 2014-2018 Term Goal #7 Strong Financial Stewardship:

Maintain the City's strong financial position through effective budget processes, the efficient and effective use of financial resources, and the prudent leveraging of economic and financial opportunities to increase current and long-term financial sustainability.

- 7.1. Relevant and effective budget processes and policies.*
- 7.2. Well-informed and sustainable financial decision making.*
- 7.3. Transparent financial decisions that are appropriately communicated to the public.*
- 7.4. Strategic financial opportunities are optimized.*

Analysis

The City's investment book value was approximately \$980 million as of December 31, 2016. During the year, the investment portfolio earned approximately \$19 million which equates to an annual interest yield of approximately 2.0%.

The City's investment portfolio holds the City's working capital that is required to pay for ongoing operating expenditures and it is also comprised of unspent capital funds relating to the timing of project implementation, uncommitted reserves, deposits, development cost charges and other sources that will be expended in future years.

Permitted Investments

Under Section 183 of the *Community Charter*, a municipality may invest money and is not immediately required in one or more of the following:

- (a) securities of the Municipal Finance Authority;
- (b) pooled investment funds under section 16 of the Municipal Finance Authority Act;
- (c) securities of Canada or of a province;
- (d) securities guaranteed for principal and interest by Canada or by a province;
- (e) securities of a municipality, regional district or greater board;
- (f) investments guaranteed by a chartered bank;
- (g) deposits in a savings institution, or non-equity or membership shares of a credit union;
- (h) other investments specifically authorized under this or another Act.

Investment Objectives

In accordance with Investment Policy 3703, the City's primary investment objectives are:

1. Compliance with statutory requirements;
2. Preservation of capital;
3. Maintenance of adequate liquidity;
4. Taking into account the above constraints and requirements in maximizing rate of return.

2016 Investment Performance

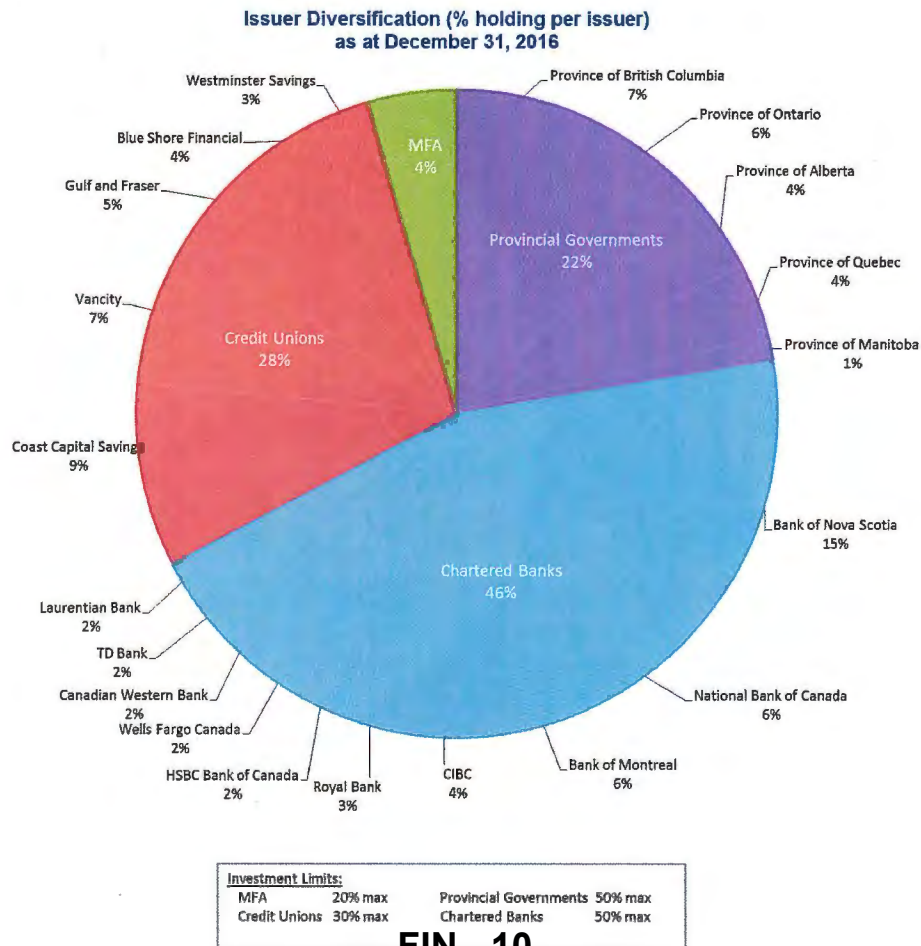
The City maintains an intermediate investment fund (short to medium term) and a fixed income fund (longer term) in its investment portfolio. The term to maturity of the investment funds matches the City’s working capital requirements and anticipated funding requirements from reserves. The weighted average yield of the City’s investments was 2.0% in 2016.

The City’s intermediate investment fund is mainly comprised of chartered banks and credit union term deposits and notes, with an average term of 2 years. This portfolio had a weighted average yield of 1.90%. During 2016, yield enhancement strategy was used for this fund and the City’s performance exceeded our benchmarks (comparable FTSE index and MFA’s Intermediate Fund), while meeting all investment objectives of capital preservation, high liquidity and low risk.

The City’s fixed income fund is comprised of bond products of permitted issuers such provincial governments, chartered banks and the MFA pooled investment funds that mature between 2 to 5 years. The weighted average yield of the portfolio for 2016 was 2.10%. The performance of this portfolio has surpassed the FTSE benchmark and is consistent with MFA’s bond fund’s return.

Investment Portfolio Overview

The City’s investment portfolio, through issuer diversification along with a balanced assessment of credit risks, complies with the City’s Investment Policy throughout the year. A breakdown of the investment portfolio holdings as at December 31, 2016 is illustrated in the chart below:

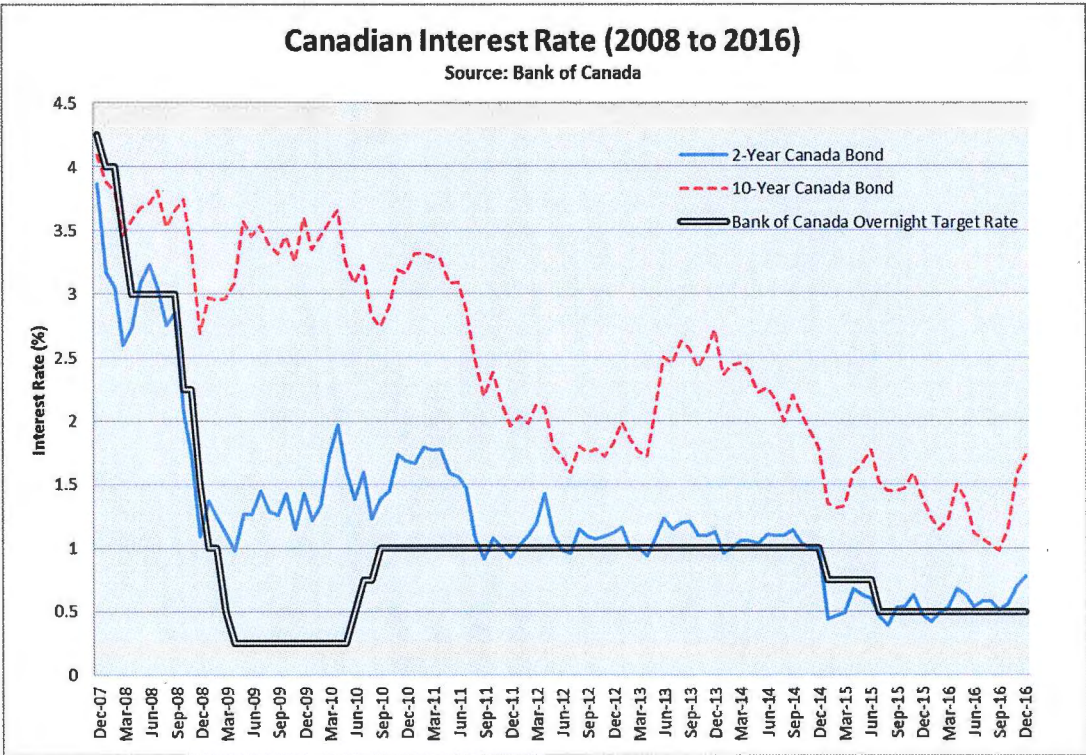


Looking Back at 2016 and Outlook for 2017

Certain economic events took place in 2016, which resulted in both economic and political uncertainties within and beyond the Canadian borders. Some of these events include:

- Concerns over the slowdown of growth of China;
- The plummeting oil prices and the weakening of the Canadian dollar;
- Lower than expected Canadian GDP;
- Weak export and decline in business investment causing slowdown of Canada’s overall productivity growth;
- The unexpected outcome of the June United Kingdom’s referendum to exit the European Union causing volatility to the global financial markets;
- The results of the US election adding another level of volatility and uncertainty to the financial markets and the Canadian economy; and
- The US Federal Reserve raising interest rate for the first time since 2008.

As shown in the graph below, the Canadian interest rates were operating at an all-time low throughout 2016. The Bank of Canada has continued to maintain its overnight interest rate unchanged at 0.50% throughout 2016. Recent statements from the Bank of Canada suggested that the possibility of further policy easing cannot be dismissed. It is continued to believe that the Bank of Canada will unlikely pull any trigger on monetary policy to increase interest rates until 2018.



City's Investment Strategy – 2017 and beyond

The City's investment portfolio will continue to be affected by the current interest rate environment. As investments that were purchased in the past gradually mature, the City will be reinvesting its funds at the prevailing market interest rate which is lower than our existing portfolio yield. Despite the interest rate challenge, the City will prudently assess its short-term and long-term cash flow requirements and will continue to reposition and rebalance its investment portfolio to achieve policy compliance and yield optimization.

Yield enhancement strategies will continue to play a key role in the City's investment portfolio. Conditions remain favourable to emphasize on short to medium term deposits instead of exposing the City's investment portfolio to the volatility and the low return of the fixed income/bond market. The short to medium term investment mandate will provide the required level of liquidity (for capital requirements) and maximize available yield in the current interest rate environment.

Forthcoming Legislation and Banking Industry Changes

There are two major changes in the banking industry that staff is continuing to monitor.

1. Bail-in Legislation

During the global financial crisis, some financial institutions were considered “too-big-to-fail” and were bailed-out by large scale government support. There was widespread concern about taxpayers funding the rescue of these institutions and that government intervention to prop up a failing company can foster moral hazard by incentivizing companies to take more risks and investors to act less diligently or cautiously.

In June 2016, the Government of Canada Parliament passed Bill C-15 which includes provisions to create a bank recapitalization regime (also known as bail-in legislation), where certain liabilities of a distressed financial institution are converted to equity.

The potential impact of this legislation to the City (and to all other BC municipal governments) could mean that bank investment that is current permitted under the *Community Charter* may no longer be considered principally guaranteed due to its convertible feature. As such, municipal governments may need to shift their investment holdings to only federal issues, provincial issues and short term deposits which offer lower yields and limited offerings, thereby resulting in reduced investment income and creating budget concerns.

City staff are monitoring the development of the legislation and is waiting the Department of Finance of Canada to release the related publication, which is scheduled to be available in February 2017. The City will continue to assess the impact of the legislation and will act accordingly to ensure investment activities will continue to comply with statutory requirements.

2. Federally Regulated Credit Unions

In 2012, the federal government established the new legal frameworks under the *Jobs and Economic Growth Act* which enabled credit unions to register nationally, opening branches across the country. Coast Capital Savings Credit Union became the first credit union in BC where its members voted in December 2016 in favour of moving ahead with the plans to transition to a Federal Credit Union. Subject to approval from various regulatory bodies, if approval is granted, it is anticipated that it will become a federal credit union in 2018.

Just like banks, any federal regulated credit unions will be regulated under the Office of the Superintendent of Financial Institutions (OSFI) and will be limited to \$100,000 deposit insurance through the Canada Deposit Insurance Corporation (CDIC) instead of the 100% unlimited deposit guarantee under the Credit Union Deposit Insurance Corporation (CUDIC), a statutory corporation backed and regulated by the Province of BC.

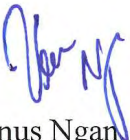
There is currently no change to the CUDIC deposit insurance for deposits held at Coast Capital until it completes the transition to the federal environment. It is anticipated that grandfathering provisions will be granted to any deposits held before the transition date until they mature. City staff will continue to monitor the changes and will act accordingly to ensure the City's Investment Policy will be updated to reflect the proposed changes when more information becomes available.

Financial Impact

None.

Conclusion

The City's investment activities for 2016 have been conducted in accordance with the City's Investment Policy. Staff will continue to administer the investment portfolio and the investment environment in a prudent manner to ensure that the City's investment objectives will continue to be met.



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