Item	**11**
Manager's Report No.	**08**
Council Meeting	**00/03/13**

TO: CITY MANAGER 2000 March 07

FROM: DIRECTOR FINANCE File: I56-1-2

SUBJECT: CITY INVESTMENTS - 1999 UPDATE

PURPOSE: To update Council on the City's current investment program.

RECOMMENDATION:

1. THAT this report be received for information purposes.

REPORT

BACKGROUND

Periodically, the Director Finance makes a stewardship report to Council regarding the City's investment portfolio. The report highlights any significant events that have occurred in the investment program, lists the institutions the City invests with, and states the investment limits that have been placed on those institutions.

The Municipal Act states that Council has the authority to invest the municipality's reserve (capital) funds and that the Municipal Treasurer has the authority to invest the revenue (operating) funds.

Due to the volume of transactions involved in the placement of investments, Council has assigned the responsibility for the management of the investment portfolio to the Director Finance.

Attached is an updated schedule summarizing the institutions and limits currently in place for the combined capital and operating investment portfolios (Schedule A). While maintaining dollar limits for each investment issuer, our desired overall investment portfolio contains a preferred mix by category of security.

Schedule A references a number of terms with which the reader may not be familiar. A brief definition of the terms follows:

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

Term	Meaning
Schedule A Bank	Canadian-owned Bank
Schedule B Bank	Foreign-owned Bank
BDN	Bank Deposit Note (issued by all major banks)

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 Middle Low	The relative standing within each rating classification, e.g. R-1 High is, by definition the highest credit quality available.

DBRS investment quality categories for bonds and long-term debt are:

AAA	Highest quality credit
AA	Superior credit
A	Upper mid grade credit

Credit Unions of British Columbia

The Credit Unions of British Columbia are not currently rated by any of the Canadian institutional credit rating agencies. Credit Unions are regulated by the British Columbia Ministry of Finance and are under the Superintendent of Financial Institutions. The Superintendent monitors performance monthly and examines each credit union annually.

Credit Unions are required to meet regulatory, statutory capital and liquidity requirements, under the Financial Institutions Act of British Columbia and the Credit Union Incorporation Act of British Columbia.

The Province maintains, under the Credit Union Incorporation Act and in addition to the regulatory system, two credit union deposit insurance funds, of approximately $50 million and $78 million respectively, that are structured to support the liquidity of British Columbia credit unions. This infrastructure exists at the Provincial level to avoid concerns over default by individual credit unions in British Columbia.

Prior to placing any funds on deposit with a B. C. credit union the City obtains, from the Financial Institutions Commission, a certified copy of the business authorization and compliance record signed by the Superintendent of Financial Institutions Commission. A review and analysis of the audited financial statements of the credit union then determines the level of investment. The maximum term of an investment with any B. C. credit union does not exceed 180 days. The maximum amount of the portfolio invested with B. C. credit unions at any one time does not exceed 30% of the total investment portfolio.

SIGNIFICANT EVENTS DURING 1999

During 1999 short-term interest rates continued to decline as the prime interest rate, which governs the general level of short-term rates, moved from its 1998 high of 7.50% to a two year low of 6.25% in 1999. The average yield for 90 day Treasury Bills for 1999 was 4.68% (for 1998 4.72%). Overall short-term interest rates in Canada declined during 1999.

Long-term interest rates which had reached all-time historic lows in 1998 of 5.15%, started an upward movement in June 1999 and continued to move upward for the balance of 1999 closing the year at 1999 December 31 at 6.33%.

The General Revenue Fund is directly impacted by any movement in short-term interest rates during the year, particularly in July when the investment fund mushrooms from $50 million to $190 million upon receipt of tax revenue and then decreases again to approximately $67 million at year end.

In order to offset the impact of declining short-term interest rates on investment income in 1999, the General Revenue Fund invested a portion of its surplus funds in longer term, higher yield government bonds. In 1999 the General Revenue Fund generated $4.9 million in investment income (1998 $5.1 million), a 4% decrease over 1998.

During 1999 a portion of the Capital Fund reserves were invested in longer term high yield government bonds to realize higher income and safeguard the City's Capital Reserves income from the negative impact of declining short-term rates. The Capital Fund which represented $172 million at 1999 December 31 ($165 million 1998), generated income of $10.9 million ($9.8 million 1998), an 11.2% increase over 1998.

The average annual yield was 6.17% for the Capital Fund and 6.26% for the General Revenue Fund.

Throughout the year, the City continued to expand its investment dealer network, the most noteworthy being the formation of business relationships with Vancouver City Savings Credit Union. VanCity does not have a credit rating from DBRS, however they fall under the umbrella coverage of the B. C. Credit Union Act. In addition the long-term debt of VanCity, has the AAA rating from Standard & Poors credit rating agency of New York. The City's investments with VanCity are generally short-term deposits, one week to 30 days.

The core investment banking relationships remained consistent with 1998. RBC Dominion Securities (the Royal Bank) and the Toronto-Dominion Bank Treasury Group remained the City's lead investment bankers for 1999. The Toronto-Dominion Bank Treasury Group continued to be the most proactive investment dealer in both the money markets and bond markets.

The City purchased and installed "Treasury Manager Software" a Window's based treasury management system and a product of Selkirk Financial Technologies of Vancouver. This system is currently rated as North America's leading treasury and investment management system. In 1999 the City finalized installation and converted manual systems which greatly enhanced controls, recording and reporting of investment transactions.

In 1999 the City improved its ability to access and research financial markets, communicate with investment bankers and obtain competitive bids on-line through the use of the Internet, creating an environment of real-time information.

Finally, in 1999 the City purchased $94.9 million in forward contracts at pre-determined rates for the year 2000. The General Revenue Fund purchased $57.4 million, to be invested from the tax levy. The Capital Fund purchased $37.5 million, to be invested from the annual internal debt repayment and other surplus cash.

These contracts act to safeguard investment income and tax revenues from the negative impact of possible declining interest rates in 2000. By establishing a guaranteed rate of return, they also assist in forecasting the investment income for the coming year. The average term of these investments is six months to 12 months and the average yield is 6.02% for the General Revenue Fund and 6.41% for the Capital Fund.

OUTLOOK FOR 2000

Current economic forecasts for interest rates are at best uncertain. The Federal Reserve Board in the United States which controls the level of interest rates in North America is committed to raise rates in order to control inflation and cool what they consider to be an overheated expansion in the North American stock markets. The money markets have priced two interest rate hikes into the current rate structure in anticipation of the Federal Reserve Board's actions. The stock markets continue to increase in value due to the Internet/E-Com-merce/Telecommunications Sectors.

The interest rate yield curve reflects the uncertainty in the money market. Generally rates increase as the term increases. At the date of this report the curve is as follows:

90 day Treasury Bills	5.35%
One-year Treasury Bills	5.88%
Five year Government Bonds	6.25%
10 year Government Bonds	6.10%
30 year Government Bonds	5.82%

In 2000 the City will continue to invest in both the money and bond Markets for both the Capital and General Revenue Funds taking positions along the yield curve that will generate the highest yields, while maintaining liquidity and safety at all times. When an investment is placed or an investment strategy is entered into it must satisfy the criteria that it can be held until maturity. If these investments are in a capital gain position they may be sold prior to maturity.

Generally the portions of the Capital and General Revenue Funds that are not scheduled to be drawn on in the near future are invested in longer term investments with higher yields.

In the Capital Fund approximately $75 million is invested in long-term investments (5 to 17 years); the average yield on these investments is approximately 6.75%. The balance of the Capital Fund (approximately $100 million) is invested in shorter term investments that mature within 30 days to 24 months. Within the General Revenue Fund approximately $25 million is invested in long-term higher yield investments (5 to 17 years); the average yield on these investments is 6.25%. The balance of the General Revenue Fund investments have maturities of less than one year.

The City is currently reviewing the purchase of Government of Canada guaranteed short-term bonds that are equity linked notes. These notes have a term of approximately five years, a zero coupon and a yield determined by certain North America equity indexes such as the TSE 300, Dow or S & P 500. The notes may contain a basket of blue chip and other stocks. These notes trade at discounts from their initial issue price and once purchased can be sold in the bond markets at anytime. If held to maturity they yield approximately 2%, with investment fully guaranteed by the Government of Canada. The advantage to the City is that investment yields may be enhanced through the sale of the notes when market conditions are favourable. Research indicates that annual returns of 15% to 20% may be attainable. Investment in these bonds will not exceed $10 million.

The current forecasts for year 2000 investment incomes are favourable, with earnings in the Capital Fund estimated at $11.2 million ($10.9 million 1999) and $5.2 million ($4.9 million 1999) in the General Revenue Fund.

Staff will continue to research and develop investment strategies that allow the City to increase its investment income, while maintaining strict controls and guidelines outlined under the Municipal Act to safeguard the City's capital and ensure liquidity of the portfolio.

R. Maddalena

Rick Earle
DIRECTOR FINANCE

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Attach.

INVESTMENT LIMITS FOR 2000 ***Schedule A***

Securities Category	*Short-term INVESTMENTS* DBRS Ratings	*Long-term INVESTMENTS* DBRS Ratings	Investment Limit	Portfolio % Mix
FEDERAL & Fed. Guaranteed	R 1 - HIGH	AA HIGH	No Limit	No Limit
TOTAL FEDERAL & Fed. Guaranteed			**No Limit**	**No Limit**
BRITISH COLUMBIA	R 1 - MIDDLE	AA	$60,000,000	
TOTAL PROV. BC			**$60,000,000**	**30% Max.**
Alberta	R 1 - MIDDLE	AA HIGH	$40,000,000	
Manitoba	R 1 - LOW	A	$40,000,000	
Ontario	R 1 - MIDDLE	A HIGH	$40,000,000	
Quebec	R 1 - LOW	A LOW	$45,000,000	
TOTAL PROV. (EXCL. BC)			**$165,000,000**	**40% Max.**
Bank of Montreal	R 1 - MIDDLE	AA LOW	$40,000,000	
CIBC	R 1 - MIDDLE	AA LOW	$40,000,000	
Royal Bank	R 1 - MIDDLE	AA LOW	$40,000,000	
ScotiaBank	R 1 - MIDDLE	AA LOW	$40,000,000	
Toronto Dominion	R 1 - MIDDLE	AA LOW	$40,000,000	
National Bank of Canada	R 1 - LOW	A	$10,000,000	
TOTAL SCHED. 'A' BANKS			**$210,000,000**	**50% Max.**
ABN Amro Bank Canada	R 1 - HIGH	AA	$40,000,000	
Banque Nationale de Paris	R 1 - MIDDLE	AA LOW	$10,000,000	
Credit Suisse First Boston Canada	R 1 - MIDDLE	AA	$20,000,000	
Deutche Bank (Canada)	R 1 - HIGH	AA HIGH	$40,000,000	
HSBC Bank Canada	R 1 - MIDDLE	A HIGH	$40,000,000	
J. P. Morgan Bank Canada	R 1 - MIDDLE	AA	$20,000,000	
Citibank Canada	R 1 - MIDDLE	NOT RATED	$10,000,000	
Chase Manhatten Bank of Canada	R 1 - MIDDLE	AA	$10,000,000	
UBS Bank of Canada (Switzerland)	R 1 - HIGH	AA HIGH	$20,000,000	
TOTAL SCHED. 'B' BANKS			**$210,000,000**	**30% Max.**
VanCity Savings & Credit Union	NOT RATED	NOT RATED	$50,000,000	
Surrey Metro Savings Credit Union	NOT RATED	NOT RATED	$5,000,000	
Gulf & Fraser Credit Union	NOT RATED	NOT RATED	$5,000,000	
TOTAL BC CREDIT UNIONS / NON RATED INVESTMENTS			**$60,000,000**	**30% Max.**