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| Item..... | 07 |
| Meeting..... | 2008 Feb. 18 |

COUNCIL REPORT

TO: CITY MANAGER **DATE:** 2008 February 15
FROM: DIRECTOR FINANCE File: 7500 01
SUBJECT: CITY INVESTMENTS – 2007 UPDATE
PURPOSE: To update Council on the City's current investment program

RECOMMENDATION:

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

REPORT

Periodically, the Director Finance makes a stewardship report to Council regarding the City's investment portfolio.

The Community Charter states that the City may invest or reinvest money that is not immediately required. Council has assigned the responsibility for the management of the investment portfolio to the Director Finance (Bylaw No. 11553). The City's cash and investments on hand at 2007 December 31 totalled \$491,620,864 (2006 - \$446,862,033). This is represented by a single investment portfolio – City of Burnaby General Investment Fund - and includes restricted funds such as Development Cost Charges and all reserve funds. Prior to 2007 Jan 02, the City's investments were broken down by Capital (2006 - \$345,610,149) and General Revenue (2006 - \$101,251,884) Funds.

This report highlights significant events that have occurred in the investment program during 2007 and the forecast for 2008. Attachment 1 lists the institutions the City invests with and the investment limits that have been placed on those institutions.

SIGNIFICANT EVENTS DURING 2007

Investment Funds:

The City's General Investment Fund is directly impacted by any movement in short-term interest rates during the year, particularly from July onward when the investment fund reaches a high of over \$620 million upon receipt of tax revenue and then decreases to approximately \$430 million

in May. A portion of the portfolio's investments is held in money market instruments until cash is required for expenditures.

The bank rate, which governs the level of short-term interest rates, opened the year at 4.50% and was raised to 4.75% on 2007 July 10. The Bank of Canada raised the rate only once in 2007, only to see the rate close at 4.50% on 2007 December 31. The average yield for 90 day Bankers Acceptance's was 4.57%, somewhat above 2006's average of 4.16%. In 2007, the General Investment Fund generated \$28.5 million (5.21%) return on investment. (2006 - \$24.59 million at 5.02%)

To help offset the impact of low short-term interest rates on investment income, the City holds a portion of fund surpluses in long-term, investment grade bonds. The majority of these longer term investments were purchased in years when market yields were materially higher than current market yields. Holdings range from annual yields of 5.50% - 7.25%. For 2007, ten (10) year and long-term (30) year bond rates remained consistently low, starting the year at 4.03% and 4.09% respectively in January. The highs were reached in June at 4.62% for the ten (10) year bond and 4.56% for the long-term (30) year bond. The ten (10) year bond average for 2007 was 4.28% and the long-term (30) year bond average was 4.32%.

Generally the portion of the General Investment Fund that is not expected to be drawn on in the near future is invested in longer term investments with higher yields. Approximately \$366 million is invested in long-term investments (one year and longer); the balance in shorter term investments that mature within one year.

Banking Relationships:

The City's investment banking relationships remained consistent during 2007. HSBC Bank Canada, RBC Capital Markets, and the Canadian Imperial Bank of Commerce were the City's lead investment bankers. The City continued its business relationships with B.C. credit unions placing short-term investments with Vancouver City Savings Credit Union and Coast Capital Savings. In 2007 December, the City re-established investments with Gulf & Fraser Credit Union and decreased our limit authorizations on existing credit unions to further diversify our B. C. credit unions holdings.

In addition, the City has maintained investments with Community Savings Credit Union, an Alberta based credit union that is ultimately guaranteed by the Government of Alberta. The 2008 investment limits for the Province of Alberta have been increased to \$80 million to reflect the superior rating and fiscal responsibility of the Province.

Other than Gulf & Fraser Credit Union, no additional banking relationships were established during 2007. The Investment Limits for 2008, Schedule A, is attached for review.

Outlook for 2008

Since August 2007, North American investment markets have been extremely volatile. US subprime debt issues have created an atmosphere of decreased credit access for corporations. There have been excessive losses and write-offs for both US and Canadian Financial Institutions and corporations. Evidenced by this weakness in the markets, the central banks have continued to decrease short term interest rates in an effort to provide economic stimulus and liquidity.

On 2008 January 22, the bank continued its current easing campaign by reducing rates an additional 25 basis points to 4.25%. The Banks ability to mitigate growth and inflation risks is driven by two major factors. First, the US Federal Reserve is easing very quickly. The US Fed Rate was decreased from 5.25% in August to 4.25% in 2007 December. In 2008, the rate has been decreased by 125 basis points in a span of 8 days - thus the current rate is now 3.00%. The second factor is the strength of the Canadian dollar to the US, which is mainly driven by a weak U. S. dollar and higher commodity prices.

Further rate cuts in Canada are expected in the first half of 2008 as economic dialogue includes concern of a US recession spill over into Canada. The Bank of Canada has reduced GDP projections for 2008 to 1.8 per cent but are currently projecting that the Canadian economy will expand by 2.8 per cent in 2009. In the Bank of Canada's Monetary Policy Report Update released 2008 January 22, the central bank expects the weaker US economy will put downward pressure on Canada's export growth. However, domestic demand is expected to remain strong – supported by income growth driven by high commodity prices.

Based on global activities, market imbalances have been unfolding quickly since August 2007. While there has been a slow and methodical approach to monetary activity by both the U.S. and Canadian central banks through the second half of 2007, current market rhetoric and actions have pointed to a more disorderly and rapid change to economic imbalances. For example, weaker than expected inflation in late 2007 and recent manufacturing layoffs implies that the Canadian economy is also slowing.

For the City of Burnaby, these economic factors suggest that both absolute return and investment yield should remain flat when compared to 2007 levels. While investment income earned on short term holdings will be affected by the decrease in money market interest rates, the City repositioned some holdings into three to five year terms before the yield curve began steepening. The current forecast for 2008 investment income is \$25 million. Of this amount, \$6.4 million is the current operating budget forecast (2006 - \$6.3 million) with the remainder of funds distributed to Reserve Funds.

Summary

Solid diversification and investment strategy development has allowed the City to increase its investment income, while maintaining strict controls and guidelines outlined under the Community Charter. With an annual yield of 5.21% in the General Investment Fund, the return on investment in 2007 was in excess of \$28.5 million.



Rick Earle
DIRECTOR FINANCE

Attach.

Attachment 1

The following 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, the 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.

| <u>Term</u> | <u>Meaning</u> |
|--|--|
| Schedule I Bank | Canadian-owned Bank |
| Schedule II 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 | 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

INVESTMENT LIMITS FOR 2008

| SECURITIES CATEGORY Federal & Federal Guaranteed | Short-term Investments R1 - High | DBRS Ratings | | Limits Per Counterparty No Limit | Portfolio Mix Total |
|---|-------------------------------------|---------------|---------------------------------------|--|------------------------|
| | | Senior AAA | Long-term Debt Subordinated N/A | | |
| TOTAL FEDERAL & FEDERAL GUARANTEED | R1 - High | AA High | N/A | No Limit | No Limit |
| British Columbia | R1 - High | AA High | N/A | 60,000,000 | |
| TOTAL PROVINCE OF BRITISH COLUMBIA | | | | 60,000,000 | 30% Max. |
| Alberta | R1 - High | AAA | N/A | 80,000,000 | |
| Alberta Capital Finance Authority * | Not Rated | Not Rated | Not Rated | | |
| Community Savings Credit Union ** | | | | | |
| TOTAL PROVINCE OF ALBERTA | | | | 80,000,000 | 30% Max. |
| Saskatchewan | R1 - Middle | AA Low | N/A | 40,000,000 | |
| Manitoba | R1 - Middle | A High | N/A | 40,000,000 | |
| Ontario | R1 - High | AA | N/A | 60,000,000 | |
| Quebec | R1 - Middle | A High | N/A | 45,000,000 | |
| TOTAL PROVINCES OTHER (Excluding B.C. and Alberta) | | | | 185,000,000 | 50% Max. |
| Bank of Montreal | R1 - High | AA | AA Low | 50,000,000 | |
| CIBC | R1 - High | AA Low | A High | 40,000,000 | |
| Royal Bank | R1 - High | AA | AA Low | 50,000,000 | |
| Scotiabank | R1 - High | AA | AA Low | 50,000,000 | |
| Toronto Dominion Bank (aka TD-Canada Trust) | R1 - High | AA | AA Low | 50,000,000 | |
| Manulife Bank of Canada | R1 - Middle | AA Low | Not Rated | 25,000,000 | |
| National Bank of Canada | R1 - Middle | AA Low | A High | 20,000,000 | |
| TOTAL SCHEDULE 'I' BANKS | | | | 285,000,000 | 50% Max. |
| HSBC Bank Canada | R1 - High | AA | AA Low | 50,000,000 | |
| BNP Paribas (Canada) | R1 - Middle | AA | Not Rated | 20,000,000 | |
| Citibank Canada | R1 - High | AA High | Not Rated | 20,000,000 | |
| TOTAL SCHEDULE 'II' BANKS | | | | 90,000,000 | 30% Max. |
| Coast Capital Savings Credit Union | Not Rated | Not Rated | Not Rated | 25,000,000 | |
| Gulf & Fraser Credit Union (dba G&F Financial) | Not Rated | Not Rated | Not Rated | 5,000,000 | |
| VanCity Savings Credit Union | R1 - Low | Not Rated | Not Rated | 35,000,000 | |
| TOTAL CREDIT UNIONS | | | | 60,000,000 | 30% Max. |

* Province of Alberta authority, agent of the Alberta crown.

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