



CITY OF HAMILTON
Corporate Services Department
Financial Planning & Policy Division

TO:	Chair and Members Audit, Finance and Administration Committee
COMMITTEE DATE:	May 12, 2014
SUBJECT/REPORT NO:	Treasurer's Investment Report 2013 Fiscal Year by Aon Hewitt (FCS14027) (City Wide)
WARD(S) AFFECTED:	City Wide
PREPARED BY:	Gerald T. Boychuk 905-546-4321
SUBMITTED BY:	Mike Zegarac General Manager of Finance and Corporate Services
SIGNATURE:	

RECOMMENDATION

That Report FCS14027 "Treasurer's Investment Report 2013 Fiscal Year by Aon Hewitt", as provided to Council, be forwarded to the Hamilton Future Fund Board of Governors for information.

EXECUTIVE SUMMARY

In accordance with the Municipal Act, 2001, the regulations thereunder, and the City's Statement of Investment Policies and Procedures (the "SIP&P"), the Treasurer of the City of Hamilton (the General Manager of Finance and Corporate Services) is presenting to Council the City of Hamilton - Reserve Funds Treasurer's Investment Report 2013 Fiscal Year (the "Treasurer's Report"), attached as Appendix "A" to Report FCS14027.

The Treasurer's Report is an investment report for the City's Reserve Fund and the Hamilton Future Fund (the "Funds") for fiscal year 2013, and is prepared by Aon Hewitt on behalf of the Treasurer.

All investments met the eligibility requirements as prescribed by Ontario Regulation 438/97 ("O. Reg. 438/97") and were made in accordance with the investment policies and goals adopted by the City (the City's SIP&P), with the exception of one type of investment detailed in Appendix I of the Treasurer's Report. This investment which

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represents 0.76% of the Funds was sold on April 14, 2014 to ensure alignment with O. Reg. 438/97.

Performance of the Investments for the Funds

The market rate of return for the twelve month period ending December 31, 2013 was - 0.73% for the Reserve Fund, and was -0.03% for the Hamilton Future Fund. Details were provided in Report FCS13063(a) and Report FCS13064(a) respectively. The Funds underperformed the benchmark rate of return of 0.42% due to an underweight position in short term bonds, which outperformed mid-term and long-term bonds as a result of the significant increase in interest rates in 2013.

Market rate of return is based on security market value, and includes net unrealized gains/losses, net realized gains/losses, and income; and is provided by RBC Investor & Treasury Services (RBC I&TS), the City's custodian.

The market rates of return for the Funds, given above, as well as those for each quarter in fiscal year 2013, were verified (allowing for a tracking error of +/- 0.1%) by Aon Hewitt, thereby providing an independent third party review of the Funds' investment performance.

On an average cost basis for fiscal year 2013, the Reserve Fund's annual rate of return was 1.9% and the Hamilton Future Fund's annual rate of return was 2.39%. The rate of return on a cost basis excludes net unrealized gain/losses but includes all income and net realized gains/losses and values the securities using original cost.

Investment in City of Hamilton Securities

During fiscal year 2013, the City was invested in its own long-term securities, which have a market value of \$16.1 million, or a proportion of 2.1% of the total market value of the Reserve Fund as at December 31, 2013. As at December 31, 2012, the proportion was 2.2%. The slight decline in proportion is due to market fluctuation. The City had no transactions in or disposals of its own long-term securities during fiscal year 2013. During fiscal year 2013, the City was not invested in its own short-term securities which is unchanged compared with the fiscal year 2012.

Other Information for Fiscal Year 2013

As detailed in Report FCS11006(c), on October 4, 2013, the City sold in the public bond market the entire holdings (par value \$75,664,883) of Master Asset Vehicle II Notes (MAV II Notes) in the Reserve Fund, which comprised 9.8% of the total market value of the Reserve Fund as at December 31, 2012. The proceeds from the sale were subsequently reinvested for the Reserve Fund in investments in accordance with the City's SIP&P.

Alternatives for Consideration – Not Applicable

FINANCIAL – STAFFING – LEGAL IMPLICATIONS (for recommendation(s) only)

Financial: None.

Staffing: None.

Legal: None.

HISTORICAL BACKGROUND (Chronology of events)

In accordance with O. Reg. 438/97 and the City of Hamilton's SIP&P, the Treasurer of the City of Hamilton shall prepare and present to Council each year an investment report on the management of the City's Funds during the prior fiscal year.

The investment report, prepared by Aon Hewitt on behalf of the Treasurer, is the Treasurer's Report and is attached as Appendix "A" to Report FCS14027.

As required by O. Reg. 438/97, the investment report contains at a minimum, the following information:

- a statement about the performance of the investments for the Funds;
- a description of the estimated proportion of the total investments of the City 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;
- a statement by the Treasurer as to whether or not, in his opinion, all investments are consistent with the investment policies and goals (the City's SIP&P) adopted by the City;
- 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;
- such other information that Council may require or that, in the opinion of the Treasurer, should be included; and
- a statement by the Treasurer as to whether any of the investments cited in O. Reg. 438/97 Section 8(2.1) fall below the standard prescribed by O. Reg. 438/97 during the period covered by the investment report (in this case fiscal year 2013).

POLICY IMPLICATIONS AND LEGISLATED REQUIREMENTS

In accordance with the Municipal Act, 2001 and the City's SIP&P, the Treasurer shall prepare and present to Council each year an investment report on the management of the City's Funds during the prior fiscal year.

RELEVANT CONSULTATION

Aon Hewitt prepared, on behalf of the Treasurer, the Treasurer's Report. Legal Services in the City Manager's Office has been consulted on the legislative and regulatory amendments affecting the City's SIP&P.

ANALYSIS AND RATIONALE FOR RECOMMENDATION

Fund Performance (pages 4 and 5 of the Treasurer's Report)

The market rate of return for the Reserve Fund and the Hamilton Future Fund is determined and provided by RBCI&TS. Aon Hewitt verified RBCI&TS' market rate of return for each quarter end in fiscal year 2013 and (annualized) longer periods. Aon Hewitt confirms their market rate of return matches that of RBCI&TS for the periods considered, allowing for a 0.10% tracking error. Table 1 presents a summary of these results, and also includes a comparison of the market rate of return with the benchmark rate of return for each period.

Table 1: Fund Performance (%) and Comparison with Benchmark

	Q1 2013 %	Q2 2013 %	Q3 2013 %	Q4 2013 %	1 Year %	3 Year %
Benchmark	0.6	-1.0	0.4	0.5	0.4	2.6
Reserve Fund						
RBC I&TS	0.9	-1.6	0.5	-0.5	-0.7	3.0
Aon Hewitt	0.9	-1.6	0.5	-0.5	-0.7	3.0
Difference	0.0	0.0	0.0	0.0	0.0	0.0
Hamilton Future Fund						
RBC I&TS	0.9	-1.5	0.2	0.5	0.0	2.1
Aon Hewitt	0.8	-1.5	0.2	0.5	-0.1	2.1
Difference	-0.1	0.0	0.0	0.0	-0.1	0.0
Reserve Fund Minus Benchmark	0.3	-0.6	0.1	-1.0	-1.1	0.4
Hamilton Future Fund (RBCI&TS)						
Minus Benchmark	0.3	-0.5	-0.2	0.0	-0.4	-0.5

For the one-year period ending December 31, 2013, the Reserve Fund and the Hamilton Future Fund underperformed the benchmark by 1.1% and 0.4% respectively. The underperformance is attributed to the Funds being underweight in short-term bonds, which outperformed mid-term and long-term bonds over fiscal year 2013. Interest rates during 2013 increased significantly; for example, the government of

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Canada bond with a term to maturity of ten years increased from 1.9% at the beginning of the year (2013) to 2.8% at the end of the year (2013).

The benchmark for the Funds is composed of 10% 91-day T-Bills, 62.5% DEX Short-Term All Government Bond Index, and 27.5% DEX All Government Bond Index.

Types of Securities (pages 6 to 8 of the Treasurer's Report)

The types of securities (and the entities who issue them) which municipalities are permitted to invest in are prescribed by legislation and regulations, including O. Reg. 438/97. Most of these securities and their issuers have been included by the City in its approved list of issuers given in Appendix A (Sector and Issuer Limitations) of the City's SIP&P. The list of issuers (the "list") given in the Treasurer's Report corresponds with this approved list.

Bank in Canada is one of the issuers on the list, and refers to a bank listed in Schedule I, II or III to the *Bank Act* (Canada). O. Reg. 438/97 permits municipalities to invest in deposit notes issued by such banks with no prescribed credit rating of the deposit note provided the term to maturity of the deposit note is less than two years on the day that the investment is made. On the other hand, if the term to maturity of the deposit note is greater than two years on the day the investment is made, O. Reg. 438/97 requires that credit rating assigned to the deposit note is at a minimum AA-. The Sector and Issuer Limitations in the City's SIP&P will be updated to reflect this requirement.

Portfolio Securities (pages 9 to 13 of the Treasurer's Report)

As at December 31, 2013, the total market value (including accrued interest) of the securities was **\$759,113,140.71** (which excludes the market value of the One Equity Portfolio, \$11,140,128) for the Reserve Fund and **\$51,760,197.97** for the Hamilton Future Fund.

The investments identified in Appendix I of the Treasurer's Report (attached as Appendix "A" to Report FCS14027), are (senior) deposit notes issued by Canadian Western Bank, a bank listed in Schedule I to the *Bank Act* (Canada), the terms of which provide that the principal and interest shall be fully repaid more than two years but less than or equal to five years after the day the investment was made. Four separate purchases (and no sales) of these deposit notes were made over the period between September 2012 and February 2014. This type of investment was formerly permitted under O. Reg. 438/97. While deposit notes may be purchased from a Schedule I bank listed in the *Bank Act* (Canada), currently under O. Reg. 438/97, a prescribed minimum credit rating is required for deposit notes with a term to maturity of greater than two years on the day of purchase. As this was not the case with the Canadian Western Bank deposit notes, these securities have recently been sold. Total gross proceeds of the sale were \$6,277,723.98, and the total original cost price was \$6,187,276.98, thereby giving net proceeds of \$90,447.00.

MAV II Notes

On October 4, 2013, the City sold in the public market the entire holdings of MAV II Notes (par value \$75,664,883), which comprised 9.8% of the total market value of the Reserve Fund as at December 31, 2012. The proceeds from the sale were subsequently reinvested in securities for the Reserve Fund in accordance with the City's SIP&P.

Investments in City of Hamilton Securities

During fiscal year 2013, the City was invested in its own long-term securities, which had a total market value of \$16.1 million, or a proportion of 2.1% of the total market value of the Reserve Fund as at December 31, 2013. As at December 31, 2012, the proportion was 2.2%. The slight decrease in proportion is attributed to market fluctuation. The City had no transactions in or disposals of its own long-term securities during fiscal year 2013. During fiscal year 2013, the City was not invested in its own short-term securities - unchanged compared with fiscal year 2012.

Investment in One Equity Portfolio

In addition to the securities listed, the City also invests in shares of the One Equity Portfolio for the Reserve Fund; the investment has a market value of \$11,140,128 and a book value of \$8,500,000 as at December 31, 2013.

Restrictions (from pages 14 and 15 of the Treasurer's Report)

Table 2, below, reproduced from the Treasurer report, shows that as at December 31, 2013, on a combined basis, the Funds were being managed in accordance with the minimum quality requirements, maximum quantity restrictions and all other imposed restrictions, with the exception of the one type of investment detailed in Appendix 1 of the Treasurer's Report.

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Table 2: Restrictions

Constraints	Policy Complied with Yes/No
The City shall not invest more than 25% of the portfolio in short-term debt issued or guaranteed by the City.	Yes
Total investment in "A" or equivalent rated debt on purchase must not exceed 35% of the market value of the City's bond portfolio	Yes
The City shall not invest in a security that is expressed or payable in any currency other than Canadian dollars	Yes
The City shall not invest in a security issued or guaranteed by a school board or similar entity unless: The money raised by issuing the security is to be used for school purposes	Yes
Permitted ranges	(%)
Federal issues	0-100
Provincial holdings in aggregate	0-100
Single province exposure	0-50
Individual non-federal/non provincial holdings*	0-10
Non-federal/non provincial holdings in aggregate	0-50
Municipal issues*	
- individual muni issue rated "AAA"	0-10
- individual muni issue rated "AA"	0-10
- individual muni issue rated "A"	0-5
Municipal holdings in aggregate	0-30
Short-term securities	0-50
Portfolio duration	1-6 Years

*Except for City of Hamilton issues which have an upper limit of 25%

Table 3, below, not included in the Treasurer's Report, shows as at December 31, 2013 the City's credit exposure (and maximum limit) for the Funds to the approved issuers (or sectors), given in Appendix A of the City's SIP&P.

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Table 3: Credit Exposure¹ (%) - As at December 31, 2013

<i>Issuer or Sector</i>	<i>Reserve Fund</i>	<i>Hamilton Future Fund²</i>	<i>Combined Funds</i>	<i>Maximum Limit %</i>
Cash (STIF)		0.7%	0.0%	
Canada				
Direct	1.3%	0.0%	1.3%	100%
Guarantee	1.6%	0.0%	1.5%	25%
Provinces				
Ontario	10.4%	24.4%	11.2%	50%
Other	34.9%	25.4%	34.8%	50%
Municipalities				
Hamilton	2.0%	0.0%	1.9%	25%
Other	17.1%	2.0%	16.1%	30%
Banks				
Schedule I	31.0%	47.5%	32.1%	50%
Asset Backed Securities	0.0%	0.0%	0.0%	25%
Corp. Bonds	0.0%	0.0%	0.0%	15%
Comm. Paper				
Corp. Paper and ABCP	0.6%	0.0%	0.6%	20%
One Equity Portfolio	1.1%	0.0%	1.1%	10%
Total	100.0%	100.0%	100.0%	

Notes to Table 3:

¹ Credit exposure refers to the par value of holdings in individual issuers or sectors as a percentage of the total par value of holdings in the fund.

² For the Hamilton Future Fund, credit exposure does not reflect the shares of the Hamilton Utilities Corporation, which are held in the Hamilton Future Fund custodial account with RBC I&TS.

Transactions (page 16 of the Treasurer's Report)

The total dollar amount of purchases and sales of securities in the Reserve Fund was approximately \$322.7 million, with total net purchases of \$4.5 million.

The total dollar amount of purchases and sales of securities in the Hamilton Future Fund was approximately \$239.0 million, with total net sales of \$13.4 million (including transactions of cash to and from the short-term custodial account).

Certificate by CIO (page 17 of the Treasurer's Report)

The CIO has certified on page 17 of the Treasurer's Report that the Funds were managed in compliance with the Municipal Act, 2001, and in accordance with the terms, conditions and guidelines stipulated in the City's SIP&P, with the exception of one type of investment identified in Appendix I of the Treasurer's Report (attached as Appendix "A" to Report FCS14027).

ALTERNATIVES FOR CONSIDERATION

Not Applicable.

ALIGNMENT TO THE 2012 – 2015 STRATEGIC PLAN

Strategic Priority #2

Valued & Sustainable Services

WE deliver high quality services that meet citizen needs and expectations, in a cost effective and responsible manner.

Strategic Objective

- 2.1 Implement processes to improve services, leverage technology and validate cost effectiveness and efficiencies across the Corporation.

APPENDICES AND SCHEDULES ATTACHED

Appendix "A" to Report FCS14027.