

The Regional Municipality of York

Committee of the Whole
Finance and Administration
May 4, 2023

Report of the Commissioner of Finance

2022 Annual Investment Report

1. Recommendations

Council receive this report for information.

2. Summary

This report discusses the investment activities that were undertaken during 2022, as required by Ontario Regulation 438/97 (as amended) of the *Municipal Act, 2021* and the Region's *Investment Policy*.

Key Points:

- The General Fund earned \$110 million on an average investment of \$4.32 billion, representing a realized rate of return of 2.55%
- Total returns exceeded the FTSE/S&P Index and ONE Investment Program benchmarks by 3.41% and 0.60% respectively
- The Sinking Fund earned \$26 million on average investments of \$1.02 billion, representing a realized rate of return of 2.54%
- All investments made during the year met the requirements of the investment policies approved by Council and the Sinking Fund Committee

3. Background

The Treasury Office manages both the General Fund and the Sinking Fund investment portfolios on behalf of the Region. As at December 31, 2022, these portfolios had a combined maturity value of approximately \$6.27 billion.

The General Fund investments adhere to the Region's *Investment Policy*

The General Fund consists of investments held for the reserves and reserve funds, working capital and other funds of the corporation (Table 1). The maturity value of these investments at year end consisted of cash of \$680 million, fixed income securities of \$4.05 billion, and equity investments of \$145 million, for a total of \$4.88 billion.

Table 1
General Fund Portfolio Holdings
As at December 31, 2022
(\$millions)

Category	Total	% Total
Cash*	680	14%
Fixed Income	4,051	83%
Equity	145	3%
Total	4,876	100%

* Cash is in the form of bank deposits and high interest savings accounts

General Fund investments were made in accordance with the Region's *Investment Policy*, which has the following objectives:

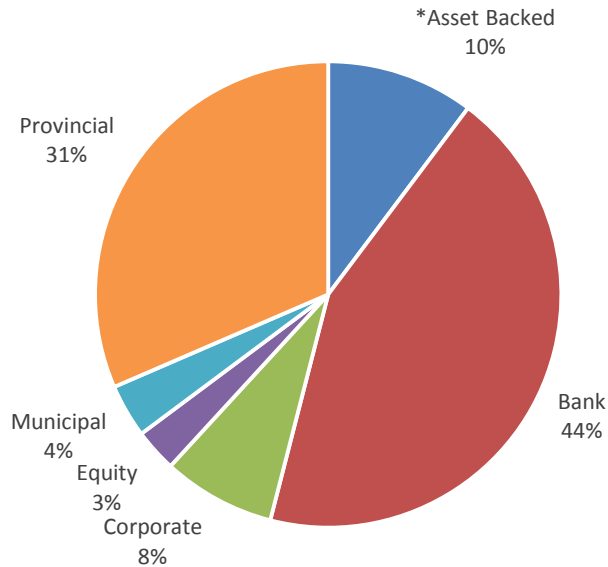
- Adherence to statutory requirements
- Preservation of capital
- Maintaining liquidity
- Earning a competitive rate of return

In addition, all investments met the eligibility requirements that are set out by Ontario Regulation 438/97 (as amended) of the *Municipal Act, 2001*, which specifies limits for each type of investment that can be held.

As shown on Table 1, on December 31, 2022, approximately 97% of the General Fund's portfolio consisted of fixed income or interest-producing investments. The remaining 3% were equity investments that are managed through the ONE Investment Program, a fund sponsored by the Association of Municipalities of Ontario (AMO) and the Municipal Finance Officers' Association of Ontario (MFOA). Figure 1 provides a breakdown of the investment held by sector categorization.

Attachment 1 provides the maturity distribution of the holdings. In 2022, the average term of the portfolio was 3.57 years, which was shorter the Region's benchmark term of 5 years.

Figure 1
General Fund Holdings by Sector Categorization
As at December 31, 2022



*Asset Backed Securities (ABS) are a type of financial investment that is collateralized by an underlying pool of high quality assets and are all AAA rated

Sinking Funds are used to repay the principal amount of debentures upon their maturity

Most of the debentures issued by York Region are required under the *Municipal Act* to have a Sinking Fund to repay the principal amount of the debenture at its maturity. In 2022, there were 11 of these “sinking fund” debentures outstanding that will mature between 2025 and 2043. The Sinking Fund portfolio is investments that are being held for this purpose and on December 31, 2022, they had a maturity value of \$1.392 billion (Table 2).

Table 2
York Region Sinking Fund Portfolio Holdings
As at December 31, 2022 (\$millions)

Category	Total	% Total
Cash*	23	2%
Fixed Income - Provincial	1,369	98%
Total	1,392	100%

* Cash is in the form of bank deposits and high interest savings accounts

During 2022, \$195 million was contributed into the Sinking Fund to meet the actuarial requirements needed for the retirement of those debentures. Investments within the Sinking Fund portfolio are segregated to align with the maturity of their respective sinking fund debenture.

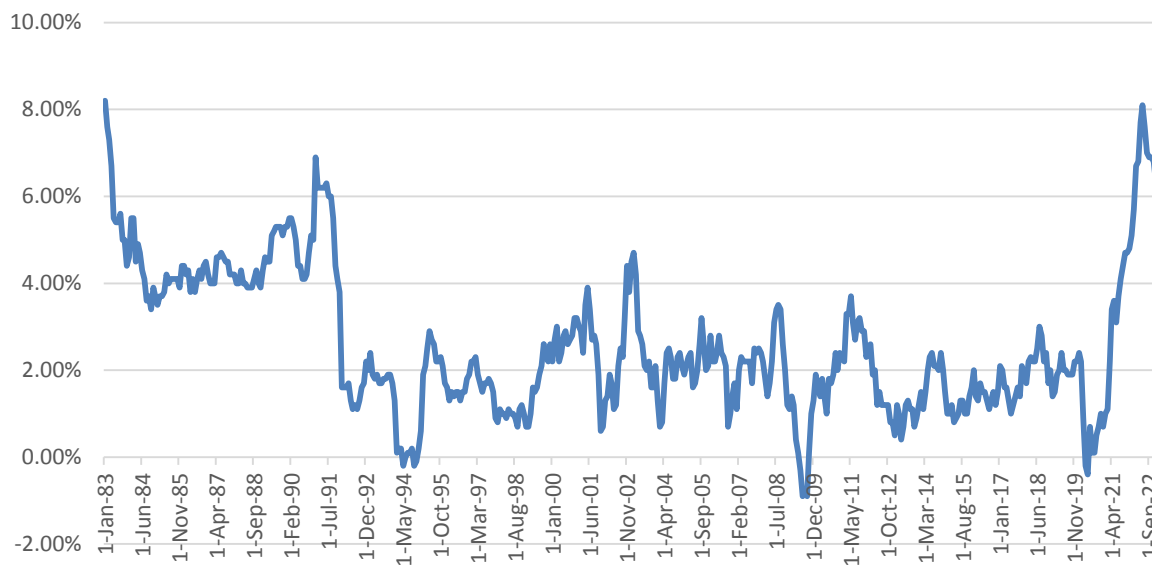
Sinking Fund investments in the portfolio are held in trust on behalf the participants of the debentures which during 2022 included the Town of Georgina, the Township of King and York Region. All investments were made according to a policy that was established by the Sinking Fund Committee¹, which is similar to the Region's own *Investment Policy*.

4. Analysis

Bond yields rose to the highest levels in 10 years due to higher inflation and geopolitical concerns

2022 proved challenging for fixed-income investors as bond yields rose to levels not seen in over ten years due to higher inflation and geopolitical concerns. The unprecedented levels of fiscal stimulus used to combat the hardship many faced due to COVID-19 closures combined with supply chain bottlenecks due to COVID-19 and the war in Ukraine led to higher levels of inflation (Figure 2) not seen in over forty years.

Figure 2
Consumer Price Index (CPI) Year-Over-Year Change
1983-2022



Central banks worldwide began to hike interest rates to curb consumer spending to combat inflation. Accordingly, the Bank of Canada started hiking rates at an unprecedented speed, and by year-end, the overnight rate finished the year 400 basis points higher at 4.25%

¹ The Sinking Fund Committee is comprised of York Region's Commissioner of Finance (Chair), the Director of Corporate Services and Treasurer for the Town of Georgina, the Deputy City Manager, Corporate Services, City Treasurer and Chief Financial Officer for the City of Vaughan, and the Director of Finance and Treasurer for the Township of King

(Figure 3). As a result, the government of Canada's ten and two-year bond yields increased by 304 and 171 basis points to finish the year at 4.05% and 3.30%, respectively (Figure 4).

Figure 3
Bank of Canada Overnight Lending Rate
2017-2022

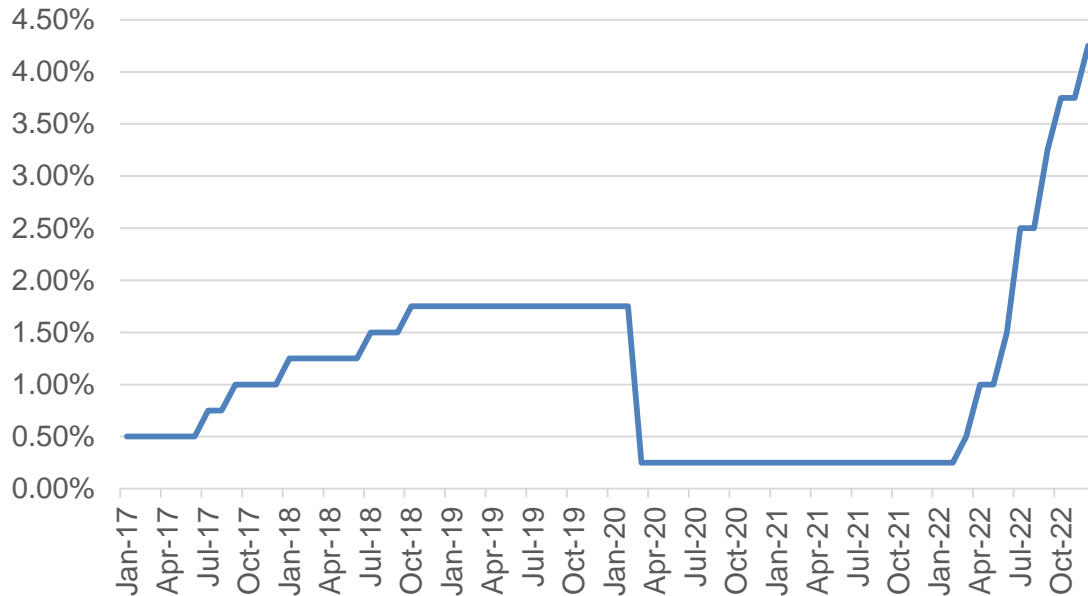


Figure 4
Government of Canada 2 and 10-Year Bond Yields
2022



Market risk associated with the General Fund portfolio was managed by having high quality liquid investments and restricting term exposure

97% of the General Fund investments in 2022 were held in highly liquid fixed income securities in the form of bank debt and deposits, money market securities and marketable bonds (government and corporate). High quality liquid securities hold on to their value better and are more easily traded in times of market stress which reduces the risk to an investment portfolio. Almost all of the Region's investments had a superior credit rating of at least AA-.

The market value of investments will also tend to rise or fall as interest rates fluctuate. If interest rates rise, the market value of the securities will decline and conversely, if interest rates fall, the market value will rise – the difference between the market value of a security at any point in time and the purchase price paid is referred to as an unrealized gain or loss. Gains or losses for the portfolio are only realized if and when the investments are sold. Also, the longer the average term of a portfolio, the greater the impact these fluctuations have on the value of the portfolio.

Therefore, an effective strategy that has been used by the Region to mitigate the impact of rising interest rates, is to restrict the term of the portfolio. Year over year, the term of the investment portfolio was relatively unchanged, from an average of 3.50 years in 2021 to 3.57 years in 2022.

The General Fund earned \$110 million for a realized rate of return of 2.55%

In 2022, the General Fund generated realized returns of \$110 million on an average portfolio balance of \$4.32 billion. This equates to a realized rate of return of 2.55%. Realized returns include actual interest income, dividend earnings and realized capital gains resulting from the sale of securities. These returns are referred to as “realized” as they represent all cash income realized and are credited to the reserves, reserve funds and other accounts.

Another method of calculating investment performance is referred to as mark-to-market returns (also known as total returns). Mark-to-market investment returns include the same components as realized returns, but also take into account any change in the market value of securities held from one period to the next.

This change in market value (due to the change in interest rates and stock market values) is not realized in the form of cash income, but rather is potential gain or loss if all the investments being held are liquidated on the date of the calculation, which for the purpose of this report, was December 31, 2022.

As noted above, mark-to-market adjustments include the period over period change in the market value of the securities held in the portfolio. Bond prices are inversely related to interest rates. As previously cited, when interest rates rise, bond prices decrease and conversely when interest rates fall, bond prices increase. As indicated in Figure 4 above, in 2022 interest rates rose throughout the year and as a result, bond values decreased which resulted in an unfavorable mark-to-market impact. After accounting for the impact of a decrease in market, value mark-to-market returns for 2022 totaled -2.63%.

Table 3
York Region General Fund Portfolio
Comparison of Realized and Mark-to-Market Returns 2018 – 2022
(millions)

Year	Average	Realized		Mark-to-Market	Mark to Market	
	Assets	Income	Return*	Adjustments	Income	Return*
2022	\$4,320.0	\$110	2.55%	(\$223.6)	(\$113.6)	(2.63%)
2021	\$3,837.7	\$99.8	2.60%	(\$54.0)	\$45.8	1.19%
2020	\$3,305.7	\$124.4	3.76%	\$53.5	\$177.9	5.38%
2019	\$3,003.9	\$104.2	3.47%	\$47.2	\$151.4	5.04%
2018	\$2,838.2	\$64.6	2.28%	(\$8.9)	\$55.7	1.96%

*These returns exclude program costs of approximately 2.5 basis points

**Market value (mark-to-market) adjustments reflect the gain or loss in value of securities over the prior year end valuation

After factoring in approximately \$850,000 for the cost to operate the investment program (staff, safekeeping, market monitoring services, transaction costs, etc.), the net return for the General Fund was 2.53%, a difference of 2.5 basis points. The 2.5 basis point cost compares favourably to the management fee charged by the ONE Investment Program, which equates to a weighted average cost of approximately 35 basis points.

Investment income earned during the year is allocated back to the source of the funds that have been invested. The sources are comprised of reserves, reserve funds as well as various deferred revenue accounts (e.g., development charges) that are held by the Region. In accordance with the *Investment Policy*, the anticipated length of time that funds are expected to remain in each of the reserves or deferred revenue accounts will determine whether those funds will receive the short, medium, or long-term interest rate that the Region earns on its investment portfolio.

The Sinking Fund earned \$26 million for a realized rate of return of 2.54%

In 2022, the Sinking Fund generated realized returns of \$26 million on a portfolio averaging \$1.02 billion. This equates to a realized rate of return of 2.54%. The returns were \$5 million higher than the \$21.2 million required to meet the Sinking Fund's actuarial requirement for 2022.

The actuarial requirements of the Sinking Funds for the year are based on predetermined expected rates of return (set at time of the debenture issue) for each Sinking Fund debenture. The expected rates of return range from 1.50% to 3.0% depending on the term characteristics (10-year, 20-year or 30-year) of the Sinking Fund and on market conditions at time of issuance. The Sinking Fund requirements are expected to accumulate to an amount

sufficient to pay the related debentures face value on maturity. The excess of revenue over these requirements for the year kept in the fund balance until the maturity of the debenture.

The General Fund portfolio performance is measured against two benchmarks

The investment performance of the General Fund Portfolio is compared to two different types of benchmarks: a managed fund benchmark and an index fund benchmark. Both benchmarks are considered fair references as they reflect the nature and scope of the mandate of the Region's investment program, as intended by the *Investment Policy*.

The managed fund benchmark is represented by the weighted composite returns of the ONE Investment Program's Money Market, Bond and Equity portfolios. Each of these funds is professionally managed by a different investment management firm selected and monitored by the ONE Investment Program.

The index fund benchmark the Region measures its performance against is provided by the Financial Times Stock Exchange (FTSE) Capital Markets Group, a predominant provider of exchange-related indices throughout the world.

For the equity portion of the portfolio, the Region compares against the S&P/TSX (Standard and Poor's/Toronto Stock Exchange) Composite Index, which is designed to measure the market activity of stocks listed on the Toronto Stock Exchange.

The Region's index-based benchmark, therefore, consists of the weighted composite returns of the FTSE Canadian Money Market, Short-Term Bond, Mid-Term Bond and Long-Term Bond indices and the S&P/TSX Composite Index. This benchmark reflects the returns earned on the passive investment of securities and can be easily tailored to reflect the changing nature of a portfolio over time. The FTSE/S&P Composite Index is used as the primary benchmark when assessing the Region's portfolio performance. The composite mark-to-market return of this benchmark in 2022 was -6.04%. York Region's portfolio return of -2.63% exceeded that benchmark by 3.41%.

The General Fund Portfolio has consistently outperformed its benchmarks

The 2022 results and comparisons for the last five years for both the ONE Investment Program and the FTSE/S&P Composite Index are summarized in Table 4 and as also depicted in Figure 5.

Table 4
Comparison of Mark-to-Market Returns
General Fund versus FTSE/S&P Composite Index and ONE Program

Year	York Region	FTSE TMX		ONE Program	
	Return	Return	Difference	Return	Difference
2022	(2.63%)	(6.04%)	3.41%	(3.23%)	0.60%
2021	1.19%	(0.79%)	1.98%	(0.26%)	1.45%
2020	5.38%	4.98%	0.40%	3.77%	1.61%
2019	5.04%	4.27%	0.77%	2.76%	2.28%
2018	1.96%	1.37%	0.59%	1.35%	0.61%
5 Year Average	2.19%	0.76%	1.43%	0.88%	1.31%

As Table 4 and Figure 5 indicate, the General Fund’s investment returns have consistently exceeded both the FTSE/S&P Composite Index and ONE Investment Program returns every year since 2018. In fact, York Region’s investment returns have exceeded those benchmarks every year since 2010, except once, in the case of the ONE Investment Program in 2013. York Region’s portfolio has generated excess returns (as captured in Figure 7) totaling \$420 million compared to the FTSE/S&P Index, and \$517 million compared to the ONE Investment Program since 2010. These returns have been achieved while consistently keeping both credit and term risk exposures at prudently low levels. The average credit rating of securities held in the portfolio is maintained at AA and the average term under four years.

Figure 5
General Fund Mark-to-Market Investment Returns
Compared to Benchmarks

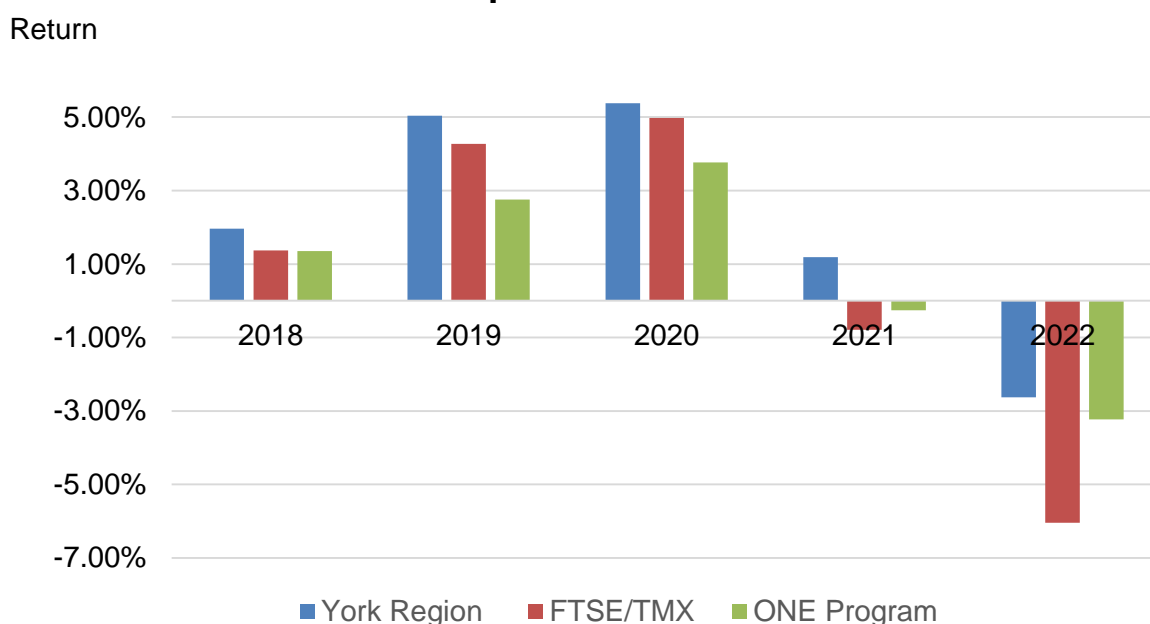
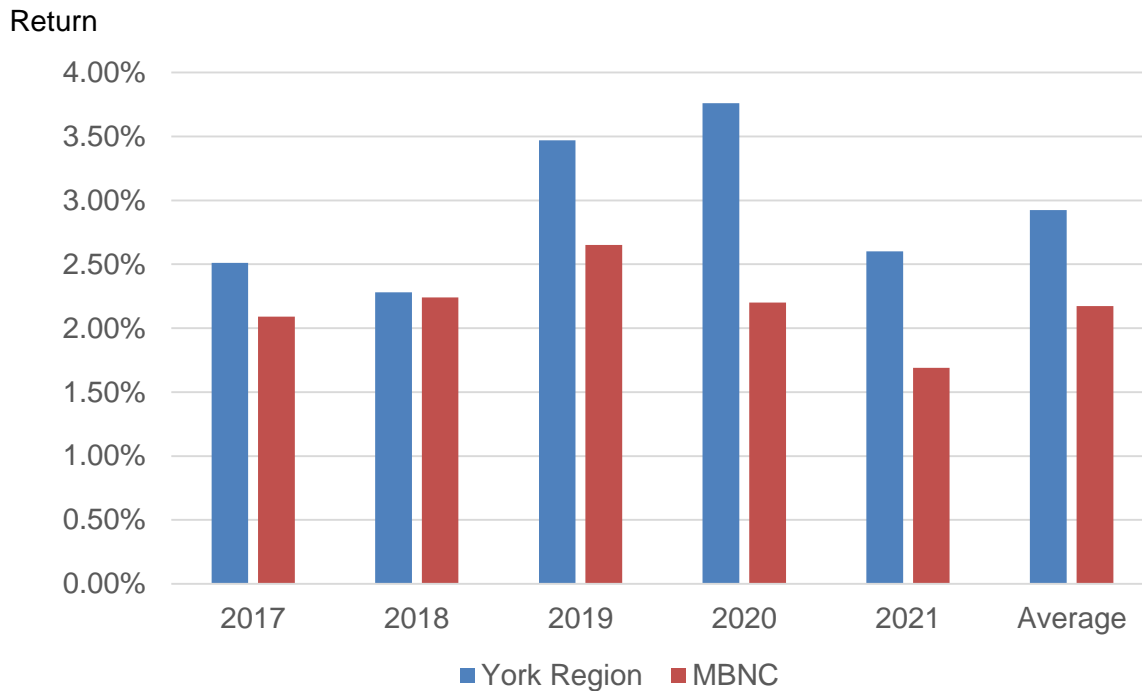


Figure 6 below compares the General Fund’s realized returns with those of the Municipal Benchmarking Network Canada (MBNC). The MBNC comparison is a good measurement of how York Region’s investment program has performed compared to municipal peers both within Ontario and across Canada. As depicted, York Region’s investment returns have exceeded these respective returns every year since 2017. It should be noted that 2022 comparisons are not provided as investment results for the MBNC municipalities are not available until June/July 2023.

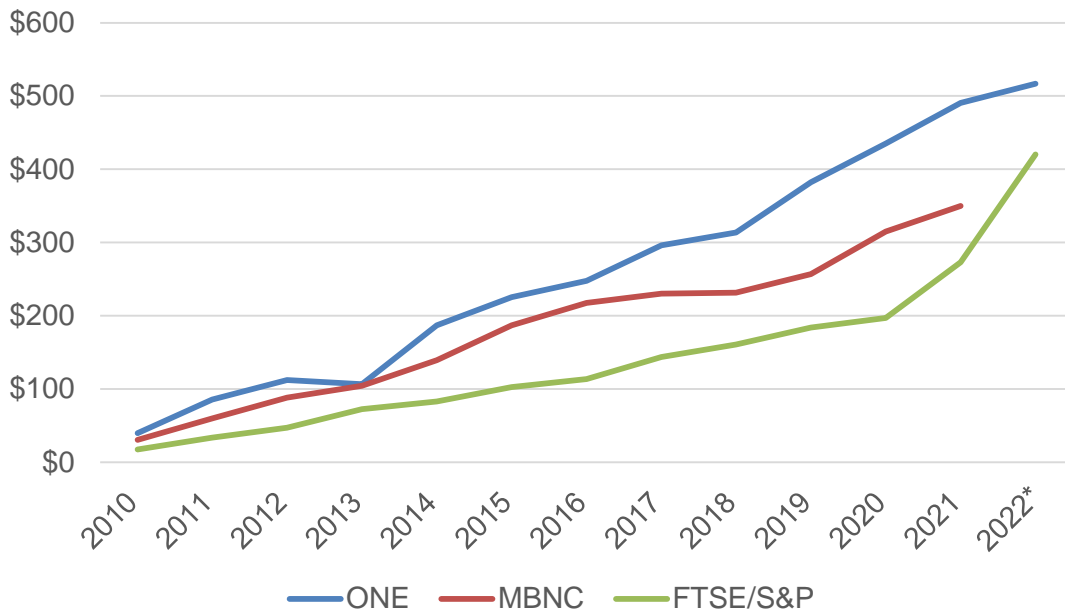
Figure 6
Comparison of General Fund Realized Investment Returns
with Municipal Peers



*MBNC 2022 data not available until June/July 2023

Figure 7 illustrates the amount of additional investment earnings York Region’s investment program has generated compared to its respective benchmarks and peer municipalities over the period from 2010 to 2022. As depicted, the General Fund earned \$420 million more compared to the FTSE/S&P, \$350 million more than the average return of the MBNC member municipalities and \$517 million more compared to the ONE Program.

Figure 7
Cumulative Surplus Over Benchmarks and Municipal Peers



*MBNC 2022 data not available until June/July 2023

Holdings of the Region's own debt did not change significantly during 2022

As of December 31, 2022, approximately 0.72% of the General Fund portfolio was invested in York Region's own securities, compared to 0.68% a year ago. These securities are treated in the same way as any other securities in the portfolio in that they are bought when returns are promising and sold when funds are needed, or other opportunities arise. Information regarding these transactions is presented in Appendix B as required by Ontario Regulation 438/97 (as amended) of the *Municipal Act, 2001*.

Market uncertainty will continue to influence the investment strategy for 2023

Continued market uncertainty will influence the Region's investment strategy during 2023. Actions of the Bank of Canada and the US Federal Reserve to manage inflation, supply issues and geopolitical concerns all represent challenges for global capital markets during 2023. Therefore, maintaining an investment portfolio profile that is both defensive and flexible is considered to be the prudent strategy.

With these factors in mind, our investment strategy will focus on opportunities as they may become available, such as extending the term of the portfolio beyond the current 3.57 years, if and as rates rise, and increasing equity holdings when share prices are low on market weakness for potential long term growth.

5. Financial

The General Fund generated realized investment returns of \$110 million for reserves and reserve funds during 2022

The Region generated realized investment returns of \$110 million on the General Fund in 2022. After costs, the total return was 3.41% higher than the FTSE/S&P Composite Index and 0.60% higher than the ONE Investment Program. These returns are contributed to and augment reserve and reserve fund balances over the longer term, reducing future levels of required contributions to these funds.

Realized investment returns on the Sinking Fund totaled \$26 million which will be used towards the retirement of outstanding debt

In 2022, the Sinking Fund generated realized returns of \$26 million on a fixed income portfolio averaging \$1.020 billion. This equates to a realized rate of return of 2.54%. The returns were \$5 million higher than the \$21 million required to meet the Sinking Fund actuarial requirement for 2022.

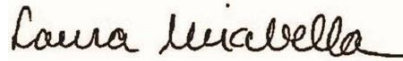
6. Local Impact

Returns generated from the General Fund portfolio have no direct impact on area municipalities. However, higher returns realized by the Sinking Fund portfolio help defray costs of borrowing for those municipalities participating in these Sinking Funds.

7. Conclusion

In 2022 the General Fund investment portfolio generated \$110 million, for a realized return of 2.55%. Total returns exceeded the FTSE/S&P and ONE Investment Program benchmarks by 3.41% and 0.60% respectively.

For more information on this report, please contact Edward Hankins, Director, Treasury Office and Deputy Treasurer at 1-877-464-9675 ext. 71644. Accessible formats or communication supports are available upon request.



Recommended by:

Laura Mirabella
Commissioner of Finance and Regional Treasurer



Approved for Submission:

Bruce Macgregor
Chief Administrative Officer

April 21, 2023

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Appendix A and B
Attachment 1 – General Fund Holdings

Regional Municipality of York
Maturity Distribution of General Fund Fixed Income Investments
General Fund
For Year Ended at December 31, 2022

Period	2022		2021		Difference
	Amount	%	Amount	%	%
Less than 1 year	1,698,621,446	36	1,911,014,930	46	(10)
From 1 year up to, but not including 5 years	1,791,199,520	38	1,225,336,661	30	8
From 5 years up to, but not including 10 years	592,456,149	13	403,710,993	10	3
From 10 years up to 30 years	649,351,000	14	582,050,002	14	(0)
Grand Total	4,731,628,115	100	4,122,112,586	100	

* excludes equities of \$145.2 million in 2022 and \$137.5 million in 2021

Regional Municipality of York
Investment Transactions - Region of York Securities
General Fund
For Year Ended at December 31, 2022

Transaction Date	Settlement Value	Issuer	Yield	Maturity Date	Security Type	Transaction Type
Dec 16, 2022	4,976,418	York Region	4.211%	Nov 18, 2041	Bond	Purchase
