

City of Regina 2022 Annual Investment Report

Contact: Irene Hryniw, Manager, Financial Analysis & Support

Prepared by: Irene Hryniw, Manager, Financial Analysis & Support



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Background

City Council and Administration have a fiduciary responsibility to the citizens of Regina to prudently manage the City's cash and investment assets. Municipalities generally take one of the following two approaches to investing funds: investing in fixed income only or investing following the prudent person principle. Municipalities that invest in fixed income only invest in bonds, commercial paper, government treasury bills and GIC's. Municipalities following the prudent person principle may invest in a broad range of investments, so long as they do so with care, skill, prudence, and diligence that a prudent person acting in that capacity would use.

Where provincial legislation does not restrict investments, a city's bylaw guides their investment strategy. Section 132 of *The Cities Act* states:

"132 (1) Subject to the regulations, a council shall, by bylaw, establish an investment policy setting out the types of investments in which the city is authorized to invest its available funds.

(2) A city may only invest its money in investments authorized by the municipality's investment Policy.

(3) The Lieutenant Governor in Council may make regulations respecting the required contents of a bylaw to be passed pursuant to this section."

City Council approved the City's Investment Policy (the Policy) on February 24, 2021 (Schedule C of *The Regina Administration Bylaw*) which follows the prudent person principle to investing. All definitions and directions included in the Policy are part and parcel of an Investment Protocol which has been established to provide guidelines and a framework for the investments of the City's funds. Within that framework, an Investment Committee was established with the foremost fiduciary responsibility to ensure compliance with the Policy requirements.

The Policy requires that, on or before June 30th of each year, an annual report be provided to City Council which includes the following:

1. The rate of return achieved in the prior period for each account, and the combined portfolio;
2. An analysis of accounts and total portfolio compared to relevant benchmarks; and
3. Any proposed changes to the Investment Policy.

Investment Committee Members

The Investment Committee has a fiduciary responsibility to ensure assets within the Investment Accounts are managed prudently, ensuring compliance with the Policy, regularly reviewing investment allocations of assets and monitoring investment performance.

The City's Investment Committee is comprised of the following staff:

- Executive Director, Financial Strategy & Sustainability (Chair)
- Director, Financial Services (Vice-Chair)
- Manager, Budget & Long-term Financial Planning
- Manager, Financial Analysis & Support
- Financial Business Partner

Investment Objectives

The overall Investment Policy objective is to incorporate industry best practices in order to ensure the preservation of capital and maintain liquidity in the portfolio. Each investment account seeks to achieve a combination of safety of principal, income maximization subject to constraints of the investment policy, and minimization of the use of temporary borrowing facility.

In managing investments, consideration is given to rate of return relative to the risk, liquidity of the investment, the duration of the investment portfolio and the prudent person principle of investment management.

The City of Regina collects different streams of revenue, which includes taxes and service fees, while delivering service to its citizens. There is considerable uncertainty regarding the amount and timing of revenues received, operating expenses incurred, and capital funds expended to deliver municipal services. As a result, the City holds cash in bank accounts for forecasted immediate needs, while setting aside significant reserves for future known and unknown expenses. The amount available for investment at any point in time varies based on revenues received and expenditures incurred, and subsequent cashflow forecasts.

To manage cash flow uncertainty, the investable assets are divided into three Investment Accounts:

- a Short-Term Account used for cash reserves expected to be spent within three years from the date the funds were received.
- a Mid-Term Account used for cash reserves expected to be spent in three to five years from the date the funds were received; and
- A Long-Term Account used for cash reserves expected to be spent in five or more years from the date the funds were received.

The City also maintains an operating bank account for immediate cash needs.

Capital Market Review

Throughout Canada, economic activity became more volatile towards the end of 2022 due to increased interest costs related to high inflation. In the beginning of 2022, the year began with the global markets facing the impact of the Covid-19 omicron variant. However, the variant posed less of a threat than its predecessors leading to the economy to reopen and markets to respond accordingly. However, just as the economy began to rebound, Russia invading Ukraine sending a shockwave through markets. A surge in energy prices due to economies reopening, tight labour markets and ongoing supply chain issues resulted in multi-decade inflationary highs. The central banks were caught behind the curve on inflation and measures began to be implemented throughout the later part of the year to try to curb consumer spending and reduce inflation.

Investment Policy Overview

The Municipal Best Practices Survey indicated that cities generally use an Investment Committee that is responsible for implementing the investment strategy approved by Council, selecting investment managers, selecting appropriate performance benchmarks and administrative procedures for investment managers, and annual reporting to Council.

The City's Investment Policy requires an annual report to Council on or before June 30 each year which includes the following:

- The rate of return achieved in the prior period for each account and combined portfolio;
- An analysis of the accounts and portfolio compared to relevant benchmarks; and
- Any proposed changes to the policy.

The City's current approach is in alignment with Municipal Best Practices, with a Council approved Investment Policy, an established Investment Committee, and the Annual Investment Report that is submitted to Council.

Investment Management

The Municipal Best Practices Survey identified that most cities use a combination of external professional investment managers with some investment activities managed by City staff. In 2021, City Council approved amendments to the City's Investment Policy which allowed the move from investing in fixed income only to investing in a broad range of investments within guidelines of the Investment Policy. In mid-2022, an investment manager (TD Asset Management) was secured and began the work of buying investments in accordance with the amended Investment Policy.

The City's 2022 Financial Statements include the Investment Income of interest earned and realized gain/loss as of December 31, 2022.

The realized gain/loss is the difference between the initial cost and the proceeds from the sale or redemption of a financial security. A gain occurs when the proceeds from the security sold are greater than the cost. A loss occurs when the proceeds are less than the cost. The City's approach is to include realized gains/losses within investment income while unrealized gains/losses are excluded.

The following chart provides the City's Investment Returns (%) over the last eight years:

Year	2022	2021	2020	2019	2018	2017	2016	2015
City Investment Returns (%)	2.37	0.59	1.13	4.42	0.65	1.75	3.87	4.67

The City's investment returns are calculated by dividing the total investment income earned by the total City's investment portfolio and cash balances during the year. Included in the investment income are realized gains and losses while unrealized gains and losses are excluded. Investment income in the City's consolidated financial statements only recognizes realized investment gains and losses. Total investment return is net of Investment Manager fees. When unrealized gains and losses are included in the investment return calculation, City invest returns rise to 3.13 per cent for 2022.

The interest rates at the beginning of 2022 were at record lows, with short-term interest rates at around 0.5 per cent. Interest rates started to slowly rise in April 2022, with the greatest increases in the July through December time period.

Investment Time Horizon

The City has three investment accounts: short, mid, and long-term, each focusing on the three objectives for the City’s investments to varying degrees. The long-term account has a larger focus on investment returns, while the mid and short-term accounts place greater emphasis on liquidity and preservation of principal.

Analysis of Investment Accounts Compared to Relevant Benchmarks

It is important to note that the City’s investment benchmarks were set pre COVID 19 and are intended to measure investment returns over a period of 3 - 5 years. As the Investment Manager only had the last four to six months of investment activity in 2022 to report on, it is difficult to make any assessment of investment return performance compared to benchmarks. This context is important as we compare our return on investment to the benchmarks.

Short-Term Investment Account

The City’s Financial Services Department uses cash flow forecasting to determine the amounts to be placed in each of the Investment Accounts. Funds forecasted to be required in the next three years are placed in the short-term account. The composition of the proposed short-term account is outlined in the table below. The short-term account is the most conservative account and is intended to protect the purchasing power of the City’s funds.

The Short-Term investment account will be used for cash reserves expected to be spent within 3 years from the date the funds were received.

The investment objectives of the Account are to:

- a. Preserve capital;
- b. Maintain 1 to 5 business day liquidity (for converting investments to cash);
- c. Achieve a long-term annualized nominal return that is equal to or greater than the Canadian inflation rate (as measured by the Consumer Price Index – Total);
- d. Avoid negative cumulative returns over any rolling four-year period; and
- e. Investments are to be within the minimum and maximum asset class guidelines as shown in Table 1.

The table below demonstrates the portfolio against the asset class benchmarks outlined in the Investment Policy.

Table 1: Short Term Investment Account (as of December 31, 2022)

Asset Class	Minimum (%)	Benchmark (%)	Maximum (%)	Portfolio Actual (%)
Short-Term Corporate Bonds	40.0	70.0	80.0	70.3
Short-Term Government Bonds	0.0	0.0	20.0	0
Money Market Funds	20	30	40.0	29.7
Guaranteed Investment Certificates	0.0	0.0	40.0	0
Total Account		100.0		100

- Short-Term Corporate Bonds: Short-term corporate bonds represented 70.3 per cent of the short-term investment accounts, which meets the benchmark.
- Money Market Funds: Money market funds represented 29.7 per cent, which also meets the benchmark.
- Short-Term Government Bonds and Guaranteed Investment Certificates: As at December 2022, there were no investments in short-term government bonds and guaranteed investment certificates which is within the minimum guideline of 0.0 per cent and meets the benchmark.

One of the investment objectives of the Short-Term Investment Account is to achieve a long-term annualized nominal return that is equal to or greater than the Canadian inflation rate (as measured by the Consumer Price Index). In 2022, the annual Consumer Price Index was 6.8 per cent. For the four to six months the Investment Manager managed funds within the short-term investment account, a return of 1.49 per cent was achieved (1.75 per cent when unrealized gains or losses are taken into consideration). If annualized, this level of return would equate to approximately 3.58 per cent (4.19 per cent if unrealized gains/losses are taken into consideration).

Mid-Term Investment Account

The mid-term investment account is funded with the City's funds not required for three to five years. The goal for these funds is to provide a greater return than the short-term account, while still preserving principal and providing liquidity if changes occur that require the City to access these funds sooner than the three-year to five-year time horizon.

The Mid-Term investment account will be used for cash reserves expected to be spent in 3 to 5 years from the date the funds were received.

The investment objectives of the Account are to:

- a. Preserve capital and liquidity.
- b. Achieve a minimum annualized nominal rate of return that is 1.8 percentage points over the Canadian Consumer Price Index. This 1.8 per cent return objective is consistent with the balanced objectives of capital preservation, liquidity, return enhancement and the overall investment risk level that the Mid-Term Account could assume. It normally will be assessed over annualized rolling five-year periods.
- c. Investments are to be within the minimum and maximum asset class guidelines as shown in Table 2.

Table 2 below demonstrates the portfolio against the asset class benchmarks outlined in the Investment Policy.

Table 2: Mid-Term Investment Account (as of December 31, 2022)

Asset Class	Minimum (%)	Benchmark (%)	Maximum (%)	Portfolio Actual (%)
Equities				
Canadian Equities	5.5	7.5	10.5	8.2
Global Equities	12.5	17.5	22.5	18.1
Total Equities	18	25	33	26.3
Alternative Investments				
Mortgages	7	10	13	8.5
Canadian Real Estate	2	5	8	1.7
Total Alternatives	9	15	21	10.2
Fixed Income				
Mid-Term Corporate Bonds	25	30	35	31.7
Mid-Term Government Bonds	15	20	25	20
Money Market Funds	7	10	13	11.8
Total Fixed Income	47	60	73	63.5
Total Account		100		100

- Equities: Canadian and global equities represented 26.3 per cent of mid-term investment accounts, which is above the benchmark, but within the minimum/maximum guideline.
- Alternatives: Mortgages and Canadian real estate alternatives represented 10.2 per cent of mid-term investments accounts, which is below the overall benchmark, but within the minimum/maximum guideline. The Canadian Real Estate asset class was 1.7 per cent of the actual portfolio, below the minimum guideline of 2.0 per cent. It was expected that during the initial phase of the Investment Manager converting cash into medium and long-term investments, that in the short term some of the minimum and maximum benchmarks would not be met as the investment manager gauged when best to enter (invest) into the various asset class markets. It is expected that all asset class investments will be within their minimum/maximum guidelines by the end of 2023.
- Fixed Income: Mid-term corporate bonds, mid-term government bonds, and money market funds represented 63.5 per cent of mid-term investments accounts, which is above the benchmark, but within the minimum/maximum guideline.

One of the investment objectives of the Mid-Term Investment Account is to achieve a minimum annualized nominal rate of return that is 1.8 percentage points over the Canadian CPI. This means an expected rate of return of 8.6 per cent in 2022. For the four to six months the Investment Manager managed funds within the medium-term investment account, a return of 2.43 per cent was achieved (4.47 per cent when unrealized gains/losses are taken into consideration). If annualized (for illustrative purposes only), this level of return would equate to approximately 5.82 per cent (10.72 per cent if unrealized gains/losses are taken into consideration). As mentioned earlier in the report, investment performance in the Mid-Term Investment Account should be measured over the long term (i.e., five years), with 4-6 months month performance of the fund in 2022 provided in this report as information.

Long-Term Investment Account

The long-term Investment Account is the most “return-seeking” component of the investment portfolio. Funds for expenditure in 5 years or more offer the City an opportunity to seek higher returns that can be used to fund operating and capital expenditures. The table below outlines the composition of the long-term account.

The Long-Term Investment Account will be used for cash reserves to be spent in five or more years from the date that the funds were received.

The investment objectives of the Account are to:

- a. Preserve capital and liquidity;
- b. Achieve a minimum annualized nominal rate of return that is 3.0 per cent percentage points over the Canadian Consumer Price Index. This 3.0 per cent return objective is consistent with balanced objectives of capital preservation, liquidity, return enhancement and the overall investment risk level that the Account could assume. It normally will be assessed over annualized rolling five-year periods; and
- c. Investments are to be within the minimum and maximum asset class guidelines as shown in Table 3.

Table 3 demonstrates the portfolio against the asset class benchmarks outlined in the Investment Policy.

Table 3: Long-Term Investment Account (as at December 31, 2022)

Asset Class	Minimum (%)	Benchmark (%)	Maximum (%)	Portfolio Actual (%)
Equities				
Canadian Equities	7.5	12.5	17.5	12.8
Global Equities	27.5	32.5	37.5	33.8
Total Equities	35.0	45.0	55.0	46.6
Alternative Investments				
Mortgages	7.0	10.0	13.0	8.5
Canadian Real Estate	7.0	10.0	13.0	2.1
Total Alternatives	14.0	20.0	26.0	10.6
Fixed Income				
Mid-Term Corporate Bonds	15.0	20.0	25.0	36.7
Mid-Term Government Bonds	10.0	15.0	20.0	0.0
Money Market Funds	0.0	0.0	10.0	6.1
Total Fixed Income	25	35	55	42.8
Total Account		100		100

- Equities: Canadian and global equities represented 46.6 per cent of long-term investment accounts, which is above the benchmark but within the minimum/maximum guideline.

- Alternatives: Mortgages and Canadian real estate alternatives represented 10.6 per cent of long-term investments accounts, which is lower than the overall benchmark and minimum guideline. The Canadian Real Estate asset class was 2.1 per cent of the actual portfolio, below the minimum guideline of 7.0 per cent. It was expected that during the initial phase of the Investment Manager converting cash into medium and long-term investments, that in the short term some of the minimum and maximum benchmarks would not be met as the investment manager gauged when best to enter (invest) into the various asset class markets. It is expected that all asset class investments will be within their minimum/maximum guidelines by the end of 2023.
- Fixed Income: Mid-term corporate bonds, mid-term government bonds, and money market funds represented 42.8 per cent of long-term investments accounts, which is above the overall benchmark, but within the minimum/maximum guideline. The Mid-Term Corporate Bonds and Mid-Term Government Bonds are outside their minimum/maximum guidelines. However, it was expected that during the initial phase of the Investment Manager converting cash into medium and long-term investments, that in the short term some of the minimum and maximum benchmarks would not be met as the investment manager gauged when best to enter (investment) into the various asset class markets. It is expected that all asset class investments will be within their minimum/maximum guidelines by the end of 2023.

One of the investment objectives of the Long-Term Investment Account is to achieve a minimum annualized nominal rate of return that is 3.0 percentage points over the Canadian CPI. This means an expected rate of return of 9.8 per cent in 2022. For the approximately four to six months the Investment Manager managed funds within the long-term investment account, a return of 2.65 per cent was achieved (5.09 per cent when unrealized gains/losses are taken into consideration). If annualized (for illustrative purposes only), this level of return would equate to approximately 6.36 per cent (12.22 per cent if unrealized gains/losses are taken into consideration). As mentioned earlier in the report, investment performance in the Long-Term Investment Account should be measured over the long term (i.e., five years), with four to six months performance of the fund in 2022 provided in this report as information.

The following provides a summary of the Investment Manager's observations with respect to 2022:

- Investors witnessed a strong rebound in total portfolio returns in 2022. High returns were accompanied with elevated volatility as markets oscillated between optimism of a soft landing and fears of systematic risk rooted in the collapse of several US regional banks. Swift intervention from policy makers calmed the mood in 2022 and helped global equities finish the year with mid-to-high single digit returns.
- Active returns in fixed income were positive as the portfolio ended 2022 with a higher duration than the benchmark.
- A focus on quality growth, at reasonable valuations, resulted in an underweight to the concentrated number of higher-multiple stocks that outperformed and drove index-level returns. An overweight to short-term investments as we queued up for real estate also dragged on performance as both equities and bonds had a strong year.
- Real assets and commercial mortgages lagged the returns from public markets during the fourth quarter, however, continue to provide strong diversification to the portfolio.

Asset mix positioning has moved towards neutral and had little impact on benchmark relative returns.

Source of Investments

The City of Regina invests funds that stem from the following sources:

- Reserves: operating, capital and self-sustaining
- Capital deposits: unspent allocated capital funds and government grants
- Funded Employee Benefit Obligations (EBO): medical, dental and life insurance
- General Operations and deferred revenues
- Other: trusts

The above funds are invested in a diversified portfolio of financial assets consisting of money market securities, short-term and long-term government and corporate bonds, private credit, commercial mortgages, global equities, and infrastructure investments. The allocation of source funds is executed in accordance with the investment objectives of the City.

Summary of Investments

As at December 31, 2022, the market value and cost value of the City's external investments is \$380.8 million and \$377.1 million respectively. Externally managed investment generated an investment income of \$7.1 million while internal investment generated a total of \$5.3 million, for a total 2022 Investment Income of \$12.4 million. A \$1 million increase from the previous year.

Externally Managed Investments (with Realized Gains/Losses)

Portfolio	Initial Investment	Cost at Year End	Investment Income (\$)	Investment Return (%)	Annualized Investment Return (%) ¹
Short-Term	220,000,000	223,281,573	3,281,573	1.49%	3.58%
Mid-Term	70,000,000	71,697,570	1,697,570	2.43%	5.82%
Long-Term	80,000,000	82,118,656	2,118,656	2.65%	6.36%
Total	370,000,000	377,097,798	7,097,798		

Externally Managed Investments (with Realized and Unrealized Gains/Losses)

Portfolio	Initial Investment	Market Value	Investment Income (\$)	Investment Return (%)	Annualized Investment Return (%)
Short-Term	220,000,000	223,843,849	3,843,849	1.75%	4.19%
Mid-Term	70,000,000	73,125,562	3,125,562	4.47%	10.72%
Long-Term	80,000,000	84,072,682	4,072,682	5.09%	12.22%
Total	370,000,000	381,042,092	11,042,093		

¹ Annualized investment return is shown for illustrative purposes only and represents actual investment return, annualized over a year.

Internally Managed Investments

	Investment Income (\$)
Internally Managed Investments (G.I.C)	586,430
Interest earned on Cash Balance	4,708,366
Total	5,294,796

Performance Measurement Benchmarks

The investment performance of all funds is reported to City Council on an annual basis. Investment benchmarks are used for comparison purposes to assess the actual performance of the Investment Manager versus the performance benchmarks established in the City’s Investment Policy. Investment managers are expected to generate higher returns than the benchmark measure over a period of time (3-5 years). The Investment Manager began working with the City’s investment portfolio at midyear and at the time when markets were volatile. As a result, actual results in this report compared to the performance benchmarks do not provide the long-term perspective required to evaluate the performance of the City’s investments against established benchmarks. However, the information in this report provides information on the City’s overall investment returns in 2022.

As the Investment Manager moved funds from cash to Medium and Long Term Investments, it was expected that the asset class minimum and maximums would not be immediately achieved by the Investment Manager. Within this context, the Investment Manager did a reasonable job maintaining the City’s investments between the minimum and maximum limits outlined in the *Investment Policy* and remaining relatively on the benchmark with portfolio mix within Investment Accounts. It is expected that in 2023, investments will be within the asset class minimum/maximum limits.

The *Investment Policy* outlines investment types the Investment Manager can invest in as highlighted below:

Short-Term Fixed Income Portfolio

The Manager will seek to achieve the Account’s investment objective by investing in a diversified portfolio of Canadian corporate fixed income securities, both directly and through investment in funds managed by the Manager, subject to the investment guidelines.

Mid-Term Fixed Income Portfolio

The Manager will seek to achieve the Accounts investment objective by investing in a diversified portfolio of Canadian and Global equities, fixed income securities, and alternative asset classes, through investments in funds managed by the Manager, subject to investment guidelines.

Long-Term Fixed Income Portfolio

The Manager will seek to achieve the Account’s investment objective by investing in a diversified portfolio of Canadian and Global equities, fixed income securities, and alternative asset classes and through investment in funds managed by the Manager, subject to the investment guidelines.

Investment Income

In 2022, The City of Regina's total externally managed portfolio generated \$7.1 million of investment income in the six months they managed the investment funds. Investment income is based on realized gains/losses, interest and dividends and excludes unrealized gains/losses. As of December 31, 2022, the unrealized gains were an additional \$3.9 million.

Short Term Liquidity

The Short-Term Liquidity portfolio is invested in a combination of corporate and bank paper, term deposits and short-term government and corporate bonds. All investments in short term liquidity portfolio mature in less than two years.

Cash Flow Management Strategy

Forecasting of short-term and long-term cash flows is a critical input in the investment management process. To meet the City's investment objectives, the cash flow forecast is utilized for liquidity management purposes and investment decision making. The cash management strategy is largely influenced by the interest rate environment.

Risk Management and Compliance

The City manages investment risk through a sound governance framework and a comprehensive investment policy. The policy defines investment objectives, appropriate diversification requirements, eligible asset classes and security instruments, investment strategies, and quality and quantity constraints.

When investing in the capital markets some risk is inevitable. This includes liquidity, market, credit and interest rate risk from inflations and rising interest rates. The City monitors advanced risk metrics at both a manager's and total portfolio level to ensure that the level of risk taken is in line with the City's meeting its investment objectives.

Expense Management

The City procured the services of an external investment manager and secured the services in 2022. The timing was fortunate in that the City avoided the principal risk that many Cities experienced in Q1 of 2022.

Conclusion

The City's current investment approach is in alignment with Municipal Best Practices, with a Council approved Investment Policy, an established Investment Committee, and an Annual Investment Report to Council.

In 2022, the City's Investment Income was \$12.4 million, which was an increase from 2021 of \$9.6 million. The increase was mainly due to better interest rates in 2022 as well as having externally managed investments. The externally managed investments earned (\$7.1 million), while GIC and bank interest contributed 42 per cent of the total interest earned (\$5.3 million). The City will continue to be prudent in its approach to financial investing in 2023.