

Report to Council



Date: March 21, 2022
To: Council
From: City Manager
Subject: Investment of Kelowna funds for 2021
Department: Financial Planning

Recommendation:

THAT Council receives, for information, the Investment of Kelowna Funds for 2021 Report from the Corporate Financial Planning Manager as presented on March 21, 2022 in alignment with Council's strong financial management priority.

Purpose:

To provide Council with an economic environment update, as well as information summarizing the City of Kelowna's 2021 investment portfolio and an overview of the performance of the portfolio as a whole.

Background:

Economic Review

During 2021, the COVID-19 pandemic continued to create many challenges for the local, provincial and national economies. In addition, British Columbia experienced significant wildfires and flooding, which combined with the pandemic impacts resulted in unprecedented supply chain challenges.

The Consumer Price Index (CPI) for Canada increased from 0.7% in 2020 to 4.8% in 2021. The Bank of Canada expects CPI to be close to 5% for the first half of 2022 with expectations of it decreasing to 3% by the end of 2022. The Bank of Canada's long term CPI target remains at 2%.

The Canadian CPI measures increases in the cost of living that is experienced by consumers, and includes major components such as accommodation, food and energy. While the CPI is the most widely reported measurement of inflation in Canada, it does not necessarily reflect the basket of goods that are purchased by a local government. Other measures that are tracked by Statistics Canada include residential and non-residential construction costs. Nationally, these measures increased by 21.7% and 11.2% respectively in 2021.

In late February of 2022, Russian armed forces invaded Ukraine. The economic impacts from this invasion have been significant and are expected to further increase inflation and reduce economic growth. Prices for energy, metals and agricultural products have increased significantly and are expected to rise further if geopolitical tensions continue.

For the entirety of 2021, the Bank of Canada kept the overnight interest rate at 0.25%. In March of 2022, the overnight rate was increased for the first time since the start of the pandemic to 0.5%. The overnight interest rate is expected to continue to increase during 2022 in 0.25% increments.

The interest rates that the City of Kelowna receives on its investments are primarily determined by the national and international economic climates.

Investment of Kelowna Funds

Under the BC Community Charter, local governments are restricted in the investments that they may choose. The City of Kelowna’s Investment policy is aligned to the Community Charter. Historically, this has meant that the City has invested the majority of its funds in provincial and corporate bonds, as well as guaranteed investments from banks and credit unions. Since the start of the COVID-19 pandemic in early 2020, both short-term and long-term interest rates have been at historically low levels.

The City of Kelowna continues to utilize a laddered strategy and balanced approach for investment holdings and duration. The laddered strategy has meant that investments mature at a smooth and predictable rate. However, as we have been in an extremely low interest rate environment for approximately two years, the returns on our overall portfolio have decreased relative to prior years. This is a due to older investments with higher rates of return having matured, and been replaced with newer investments with lower rates of return.

For the purposes of illustration, the following tables provides interest rates that were offered to the City of Kelowna at various points in the last two years:

Offered Investment Rates During 2020 and 2021

Bank Guaranteed Investment Certificates

	June 2021	October 2020
1 year	0.63	0.62
2 year	0.83	0.83
3 year	1.04	0.93
4 year	1.25	1.04
5 year	1.61	1.14

Provincial Bonds

	June 2021
1 year	0.40
5 year	1.06
10 year	1.79

Portfolio Performance

The City of Kelowna portfolio has a fund value of \$623.1 million as of Dec. 31, 2021. The investment returns from these funds are used toward the City's operating and capital programs and help fund programs and renew assets. The portfolio is diversified into: 36% (\$223.3 million) short term investments, 63% (\$393.6 million) long term investments and 1% (\$6.2 million) internally financed projects.

The City of Kelowna Investment Policy includes five market indicators as benchmarks to determine the investment portfolio's performance. The benchmarks are compared to the City's average rate of return earned on the entire investment portfolio. These benchmarks are the CPI Index Average, the FTSE TMX Canada 91-Day T-Bill, the median money market return, the MFA Bond Fund and the MFA Money Market Fund. In 2021, the City of Kelowna's 1.67% average rate of return was greater than performance indicators in each of these benchmarks with the exception of the CPI Index Average.

Policy Compliance

Council Investments Policy 316 mandates certain requirements for diversification of funds, as well as constraints for the maximum amounts that can be invested with any single government or corporation. During 2021, the investments portfolio complied with all policy mandates and constraints.

Legacy Fund

The Legacy Fund consists of City owned Fortis Inc. corporate shares purchased with the proceeds of the sale of the City's electrical utility, along with the proceeds received from the termination of the City's natural gas lease-in lease-out agreement with FortisBC Energy Inc in 2018. In 2013 the City of Kelowna purchased Fortis Inc. shares in the amount of \$55.0 million from the sale of the City's Electric Utility.

As of Dec. 31, 2021, the Fortis investment had a book value of \$72.2 million and a market value of \$125.1 million, for a return on investment since inception of 73%. Consistent with prior years the City reinvested all dividends received, in the amount of \$4.2 million.

The Year Ahead

2022 investment objectives include continued monitoring of the economic climate in order to safeguard and accurately position financial assets, along with continuing to diversify the assets to maintain the security of funds.

In late 2021, Council approved changes to the investment policy that will allow investments in a new fund offered through MFABC called the Diversified Multi-Asset Class Fund.

In conclusion, the Financial Planning team is evaluating our financial reserves and investment strategy to determine the City's optimal portfolio.

Internal Circulation:

Communications Consultant

Legal/Statutory Procedural Requirements:

The Financial Officer will provide Council with an annual report on the performance of the Investment of City of Kelowna Funds portfolio in the first quarter of the following year.

Existing Policy:

Council Policy Number 316

Considerations not applicable to this report:

Legal/Statutory Authority:

Financial/Budgetary Considerations:

External Agency/Public Comments:

Communications Comments:

Submitted by:

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Approved for inclusion:



cc: Genelle Davidson CPA CMA, Divisional Director Financial Services

Attachments:

Appendix A. Presentation to Council