

Report to Council



Date: March 20, 2023
To: Council
From: City Manager
Subject: Investment of Kelowna Funds 2022
Department: Financial Services

Recommendation:

THAT Council receives, for information, the Investment of Kelowna Funds for 2022 Report from the Director of Financial Services as presented on March 20, 2023 in alignment with Council's strong financial management priority.

Purpose:

To provide Council with information summarizing the City of Kelowna's 2022 investment portfolio and an overview of the performance of the portfolio as a whole.

Background:

Economic Overview

The 2022 economic environment consisted of generationally high inflation, and historic interest rate hikes. The Consumer Price Index (CPI) for Canada increased from 4.8% at the end of 2021 to a high of 8.1% in June 2022 and settling at 6.3 % at the end of December 2022. The increase in the inflation was caused by several factors which include:

- continued supply chain challenges
- continued monetary policy tightening
- geo-political conflict in Eastern Europe

The Bank of Canada increased the interest rate seven times over 2022. The interest rate went from 0.25% in January 2022 to 4.25% in December 2022. The Bank of Canada expects CPI to be close to 3% in mid-2023 with expectations of decreasing to 2% by the end of 2023. The Bank of Canada's long term CPI target remains at 2% and in order to achieve this the Bank of Canada is not ruling out further interest rate hikes in 2023.

Investment of Kelowna Funds

The Investment Policy contemplates a balance of investment return and risk mitigation. The City of Kelowna's investments have a market value of \$792.1 million as of Dec. 31, 2022. The funds are used toward the City's operating and capital programs and help offset taxation impact to residents. The portfolio is segregated into short term funds (29% or \$225.9 million) and long term funds (71% or \$544.2 million).

The City of Kelowna continues to utilize a laddered 10-year bond strategy and balanced approach for investment holdings and duration. The laddered strategy ensures that the bonds mature at a smooth and predictable rate and that investment income and maturing investments provide ongoing liquidity. This balanced approach results in the City having sufficient levels of income and funding available to meet the municipality's annual requirements.

Portfolio Performance

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 as at December 31, 2022. 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 2022, the City of Kelowna's 2.49% average rate of return was greater than performance indicators in each of these benchmarks except for the CPI Index Average.

Benchmark	Rate	City of Kelowna Average Rate
CPI Index Average	6.30%	2.49%
FTSE TMX Canada 91-Day T-Bill	1.80%	
Median Money Market Return	1.87%	
MFA Bond Fund	-3.43%	
MFA Money Market Fund	1.93%	

The City of Kelowna's portfolio was able to outperform these benchmarks by maintaining a large portion of the portfolio in high liquid instruments. This allowed the City to take advantage of the increases in interest rates by not locking in funds at low rates for long durations.

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.

In 2022, the City reinvested dividends in the amount of \$4.5 million. As of Dec. 31, 2022, the Fortis investment had a book value of \$76.7 million and a market value of \$115.3 million, which is a 7.8% decrease from Dec 31, 2021.

The Legacy Fund is to be an investment fund that benefits the citizens of Kelowna in perpetuity. There is a project team working on a proposed strategy for these Legacy Funds, with plans to seek Council endorsement later this year in order to support the 2024 budget and beyond.

The Year Ahead

2023 investment objectives include continued monitoring of interest rate fluctuations and the timing of investment maturities with the future cash flow requirements of the City. There is an inverse yield curve on GIC rates over the next 5 years which is an indicator that the Canadian Financial Institutions believe we are nearing the top of the Bank of Canada interest rate hikes and foresee a decrease in the Bank of Canada interest rate in the next few years. The City's Treasury department has started to extend the duration of its investment maturities to take advantage of the current interest rates. It will be a key focus of the Treasury department to balance the duration of the investment maturities with the major Capital requirements of the City.

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

Submitted by: James Lawson CA, CPA, Financial Analyst, Financial Planning

Approved for inclusion:



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