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**For Information**


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DATE: May 14, 2018

REPORT TITLE: **2017 TREASURY REPORT**

FROM: Stephen VanOfwegen, Commissioner of Finance and Chief Financial Officer

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**OBJECTIVE**

To provide the annual results of investment activity in accordance with the Region of Peel Investment Policy; and, to provide the annual results of energy commodity hedging performance in accordance with the Energy Commodity Procurement Policy.

**REPORT HIGHLIGHTS**

- All investment transactions during 2017 were in accordance with the Region of Peel's Investment Goals and Policies.
- All commodity price hedging agreements during 2017 were in accordance with the Energy Commodity Procurement Policy.
- The General Fund earned a yield of 2.5% (\$57.7 million) exceeding the benchmark based on Financial Times Stock Exchange (FTSE) Russell fixed income composite index yield by 1.0% (\$22.0 million).
- The \$57.7 million revenue was allocated primarily to Reserves (91%).
- The investment strategy continues to ensure safety of principal and sufficient liquidity to meet the Region of Peel's needs, while maximizing returns.

**DISCUSSION**
**1. Background**

In accordance with Ontario Regulation 438/97 (as amended) of the *Municipal Act, 2001*, and the Region of Peel's ("Region") Investment Goals and Policies, the Treasurer is required to report annually on the Region's investment portfolio, including the performance of the portfolio and its consistency with the Investment Goals and Policies set out by the Region.

Regional Council approved the adoption of the Energy Commodity Procurement Policy which outlines the framework and guidelines of the overarching strategy to manage and mitigate the risks associated with competitive energy markets.

In accordance with Ontario Regulation 653/05 (as amended) of the *Municipal Act, 2001*, and the Region's Energy Commodity Procurement Policy, the Treasurer is required to report annually on the Region's commodity hedging performance.

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### 2. Treasurer's Discretionary Authority

Policy F20-05 Investment Goals and Policies provides the Treasurer with discretionary authority to temporarily exceed investment limitations within the Region's Investment Goals and Policies. As reported in the 2016 Treasury Report, the Treasurer used this discretion in 2017 in addition to the following:

- Cash and investments in Government of Canada bonds fell slightly below the 15% minimum in January 2017 to 14.8%. This was resolved immediately the following month. Lower cash balances normally occur at this time of year as levy receipts are low between November and January.
- At the same time, cash and short term investments fell below the 20% minimum between January and July. With the increased portfolio size, the minimum short term holding requirements were higher than required to meet funding needs of the Region.

Revisions to the Investment Goals and Policies were approved by Council at the July 6, 2017 meeting. There were no further instances where the Treasurer exercised this discretionary authority after the approval of the policy changes.

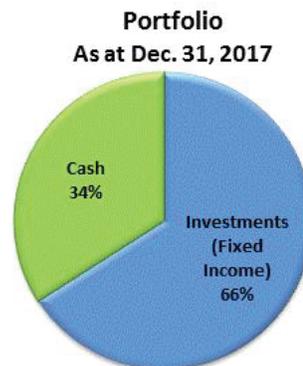
### 3. General Fund

The General Fund is comprised of cash and investments held for working capital, reserves and reserve funds, and other funds of the corporation. It does not include cash or portfolio balances of the Sinking Funds.

#### Investments

- As at December 31, 2017, the amortized book value of the portfolio was \$2,278,675,895, allocated between cash (\$776,566,360) and fixed income investments (\$1,502,109,536) as outlined in Chart A.
- Within the General Fund, the majority of funds are allocated to and/or restricted for specific spending purposes such as Wastewater \$349 million, Housing \$302 million, Water \$188 million, Working Funds \$187 million, Roads \$139 million, Peel Regional Police \$141 million, and Waste Management \$168 million.

**Chart A**



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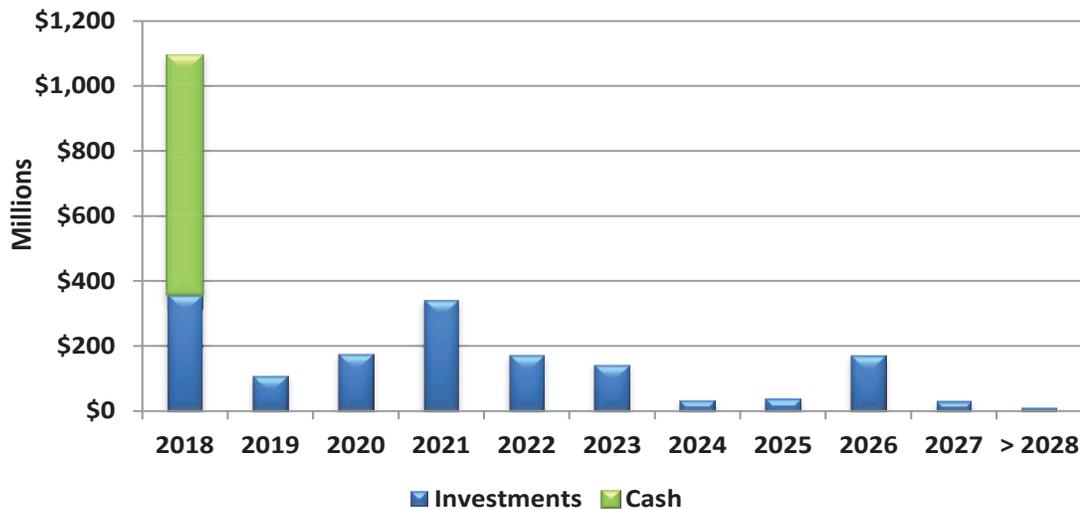
- While the allocation to cash is higher than it was historically, it is primarily due to the forecasted interest rate rise, advantageous deposit rates through the Region’s banking contract making the purchase of short-term investments (12-18 month maturities) less attractive, and the short-term need for cash to fund the development charge projects until debentures are issued.

**Portfolio Maturity**

- At year end, in addition to the readily available cash held by the Region, 16% of investments will be maturing in 2018 as shown in Chart B below.
- Bond maturities, for the most part, are aligned with the expected use of reserves and reserve funds.

**Chart B**

**Portfolio Maturities  
As at Dec 31, 2017**



*\*maturities are expressed using par value*

**Portfolio Distribution**

- Throughout the year, all of the Region’s assets were held in cash or in strong/extremely strong quality investment grade instruments shown in Chart C.
- Approximately 55% of the Region’s funds were invested in government bonds with the majority invested in provincial bonds, and 10% in bonds of Canadian banks as shown in Chart D.

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Chart C

**Credit Quality Distribution**  
As at Dec. 31, 2017

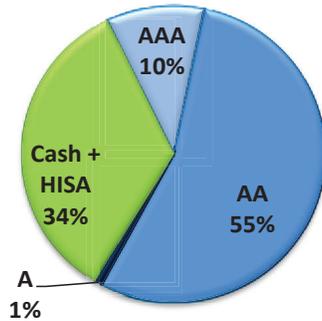
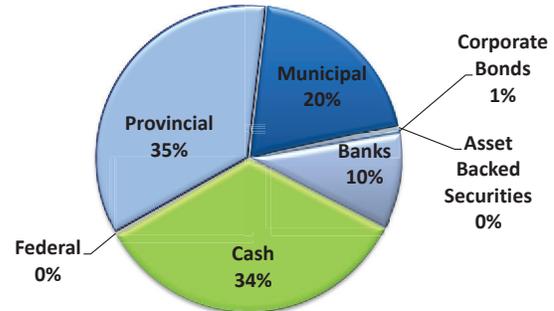


Chart D

**Sector Distribution**  
As at Dec. 31, 2017



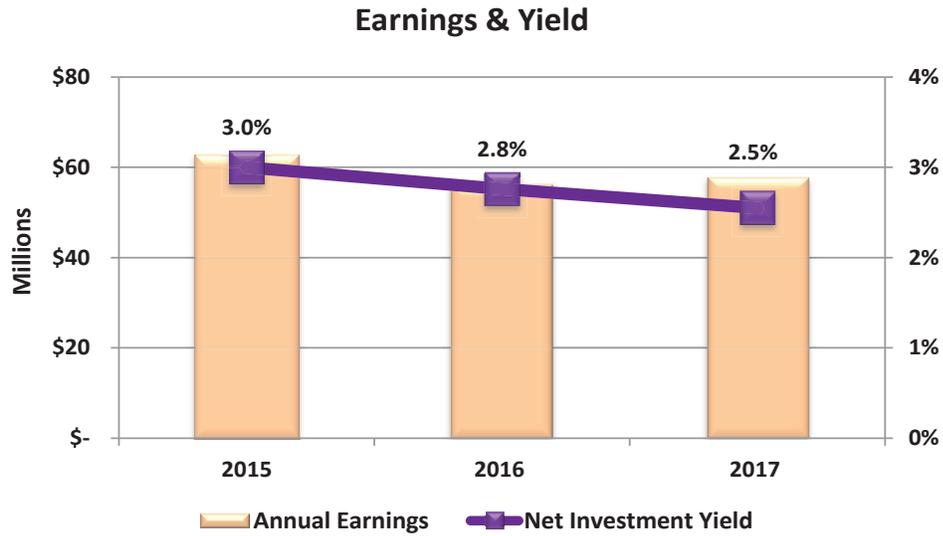
### Portfolio Costs

- The Treasury Division's management expense ratio (MER) was 3.0 basis points (0.030%) in 2017. The MER represents the operational cost relative to the size of the assets under management.
- In comparison, the ONE Fund charges a management fee of 19 basis points (0.19%) for the money market fund, 40 basis points (0.40%) for the bond fund and 45 basis points (0.45%) for the corporate bond fund.
- If the Region were to reinvest the General Fund into ONE Fund's portfolios, assuming a similar allocation, the additional cost is estimated to be 27.8 basis points (0.278%) or an additional annual budget outlay of \$5.9 million.

### Performance

- For the year ending December 31, 2017, the General Fund returned a yield of 2.5% (after MER). This represented annual earnings of \$57.7 million driven primarily from \$40.4 million of interest received/accrued and \$17.3 million of amortized investment premium and discounts.
- The gross fixed income investment yield is based on earned revenues (interest income, realized capital gains/losses, amortized premiums/discounts and securities lending income) as a percentage of the weighted average value net of expenses.

Chart E



- The Region measures its performance against a benchmark consisting of weighted composite returns sourced from the Financial Times Stock Exchange (FTSE) Russell Canadian market indices listed below in Table A.

Table A

**Benchmark - FTSE Russell**

Indices	Benchmark Allocation	Benchmark Yield
Money Market Index	21%	0.05%
Short Term Bond Index (1- 5 years)	51%	0.83%
Mid Term Bond Index (5 - 10 years)	27%	0.63%
Long Term Bond Index (10+ years)	1%	0.03%
	100%	1.54%

Table B

**Performance**

Indices	Benchmark Allocation
ROP Gross Investment Yield	2.54%
Benchmark Yield	1.54%
Value Add	1.00%

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- The Region exceeded the benchmark by 1.00% due to short term funds, cash held in bank and less than 1 year maturities. On average 24% of the General Fund was held in cash in 2017 earning an average deposit rate of 1.23%. This far exceeded the short term benchmark return, which consists of T-Bills and Corporate Paper returning 0.71%. Also, the General Fund's short term portfolio held investments with an average yield to maturity of 3.06% which exceed the benchmark. In addition, focus was placed on municipal issues which paid a higher rate in the 3 to 5 year maturity term.

#### 4. Caledon Debt Retirement Fund

The Caledon Debt Retirement Fund was established in 2003. Since that time, the Town of Caledon contributed \$29.0 million to this fund which together with earned interest, covered liability payments (principal and interest) of \$36.7 million.

On December 31, 2016, \$413,743 was remaining in the bank account. In 2017, Caledon's Debt Retirement Fund earned \$7,190 which equates to a yield of 2.5% (earnings rate). This compares to \$77,726 or 2.9% in 2016

These Debt Retirement Fund assets funded \$420,933 or 15.9% of the 2017 Series AD debenture issue liabilities resulting in the wind-up of the Debt Retirement Fund.

Caledon directly funded the \$2.2 million principal payment and \$42,705 interest that was due December 14, 2017. The outstanding debenture liability of \$5.3 million will be funded directly by Caledon until the debenture matures on December 14, 2019.

**Table C**

Date	Payment	DRF Fund	Town of Caledon	Total
Jun. 14, 2017	Interest	\$231,819	\$0	\$231,819
Dec. 14, 2017	Interest	\$189,114	\$42,705	\$231,819
Dec. 14, 2017	Principal	\$0	\$2,179,000	\$2,179,000
Totals		\$420,933	\$2,221,705	\$2,642,638

#### 5. Sinking Funds

The Sinking Fund is under the direction of the Sinking Fund Contribution and Debt Retirement Committee and is comprised of the Treasurers from the three area municipalities, as well as the Regional Treasurer and Director of Corporate Finance as Chair, or their delegates.

The objective of managing the Sinking Fund is to ensure that they are fully funded each year through earnings within the funds and any necessary contributions from participants.

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## Investments and Performance

- The investment returns were greater than the target return in all sinking funds in 2017, with the exception of Series EP, shown in Table D. Cash continues to earn the rate of return in the General Fund portfolio.

Table D

Series	Issue Date	Maturity Date	(\$ millions)					Actual Return	Target Return	Earnings Surplus/(Deficit)	
			Annual Provision Pymts	Total Provision Pymts	Holdings					Region of Peel	Town of Caledon
					Investments (Book Value)	Cash	Total				
DQ	Jun 29/10	Jun 29/40	\$8.9	\$62.5	\$67.6	\$1.0	\$68.6	4.1%	4.0%	\$227,191	\$2,472
EB	Oct 06/11	Dec 01/21	\$7.8	\$47.0	\$19.1	\$31.2	\$50.3	2.7%	2.5%	\$828,917	\$2,665
EC	Oct 30/12	Oct 30/42	\$6.8	\$34.2	\$32.8	\$2.8	\$35.6	4.5%	2.5%	\$1,836,602	n/a
EP	Jun 20/13	Jun 20/53	\$0.3	\$1.4	\$0.9	\$0.6	\$1.5	2.8%	4.0%	(\$14,401)	n/a
EQ	Aug 23/13	Dec 02/33	\$9.1	\$36.3	\$27.8	\$9.3	\$37.2	3.9%	3.3%	\$626,240	n/a
FX	Nov 02/16	Nov 02/26	\$13.7	\$13.7	\$13.7	\$0.1	\$13.7	2.6%	2.0%	\$14,128	n/a
<b>Totals</b>			\$46.7	\$195.0	\$161.9	\$44.9	\$206.8				

## 6. Compliance

- Ontario Regulation 438/97 requires that a municipality report on investments held in its own securities. Tables E and F contain details of holdings and transactions throughout 2017.

Table E

## Region of Peel Bonds - Holdings

Date	Par Value		% of Portfolio
	Portfolio <sup>(1)</sup>	RoP Bonds <sup>(2)</sup>	
Dec. 31/17	\$1,851,423,408	\$55,811,000	3.0%
Dec. 31/16	\$2,088,616,008	\$53,855,000	2.6%
Yr. over Yr. Change	(\$237,192,600)	1,956,000	

<sup>(1)</sup> Total of General Fund and the six Sinking Fund portfolios.

<sup>(2)</sup> RoP long term bonds held in portfolios.

- Due to 2017 purchases, relative holdings of the Region's debentures increased by 3.0%.
- During 2017, five purchase transactions, one in the General Fund, two in the Sinking Fund Series DQ and two in the Sinking Fund Series EC, occurred in the Region's debentures.

Table F

## Region of Peel Bonds – Transactions

Portfolio	Transaction	Date	Coupon	Par Value	Price		Yield
					Purchase	Sale	
GF	Purchase	Aug. 04/17	3.85%	\$542,000	106.305		3.473%
GF	Sale	Oct 30/17	3.85%	\$542,000		106.305	3.473%
GF	Maturity	Jun. 29/17	4.00%	\$665,000			4.031%
GF	Maturity	Dec. 14/17	6.65%	\$2,179,000			6.680%
GF	Maturity	Aug. 20/17	1.10%	\$4,000,000			1.032%
Series DQ	Purchase	Jul. 20/17	5.10%	\$5,000,000	128.707		3.305%
Series DQ	Purchase	Jul. 31/17	5.10%	\$2,300,000	126.904		3.400%
Series EB	None						
Series EC	Purchase	Aug. 04/17	3.85%	\$958,000	106.305		3.473%
Series EC	Purchase	Oct. 30/17	3.85%	\$542,000	106.305		3.473%
Series EP	None						
Series EQ	None						
Series FX	None						

- During 2017, the General Fund and each Sinking Fund portfolio was in compliance with all regulatory and policy requirements.

## 7. Debt

- As at the end of December, Region of Peel had outstanding debt totalling \$1.4 billion of net own-purpose debt, including \$173.7 million in Peel Housing Corporation's social housing mortgages.
- In 2017, the Region did not issue debt on its own behalf. However, in September \$38.9 million was issued for the City of Mississauga. As of December 31, 2017 the Region's issued and outstanding net own-purpose debt totaled \$1.4 billion, detailed as follows:

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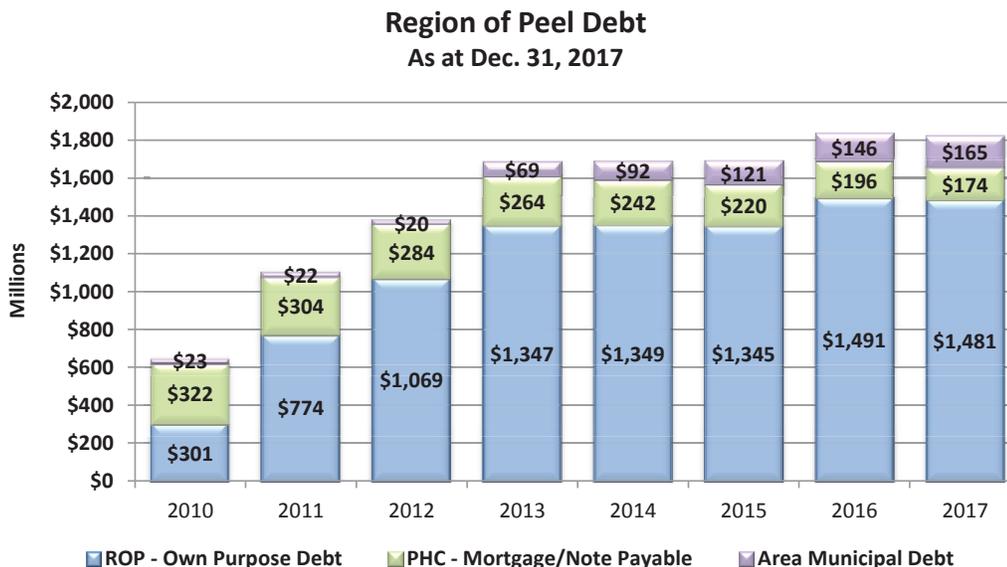
Table G

## Region of Peel Debt as at December 31, 2017

Date Issued	Issued for	Description	2017	2016
28-Sep-17	Mississauga	Series FY - GH	\$38,853,000	\$0
02-Nov-16	Region of Peel	Series FX	\$150,000,000	\$150,000,000
01-Jun-16	Caledon	Series FM - FW	\$2,790,000	\$3,100,000
01-Jun-16	Mississauga	Series FM - FW	\$33,500,000	\$37,584,000
20-Aug-15	Mississauga	Series FB - FL	\$32,000,000	\$36,000,000
10-Jun-14	Mississauga	Series ER - FA	\$24,142,000	\$27,963,000
23-Aug-13	Region of Peel	Series EQ	\$250,000,000	\$250,000,000
20-Jun-13	Region of Peel	Series EP	\$33,000,000	\$33,000,000
20-Jun-13	Mississauga	Series ED - EN	\$27,400,000	\$32,900,000
30-Oct-12	Region of Peel	Series EC	\$300,000,000	\$300,000,000
04-Nov-11	Region of Peel	FCM	\$2,962,290	\$3,143,988
06-Oct-11	Region of Peel	Series EB	\$199,358,912	\$199,358,912
06-Oct-11	Caledon - Series EB	Series EB	\$641,088	\$641,088
01-Feb-11	Region of Peel	CMHC	\$52,237,340	\$54,994,021
29-Jun-10	Region of Peel	Series DQ	\$499,567,304	\$499,567,183
29-Jun-10	Caledon	Series DQ	\$432,696	\$432,817
29-Jun-10	Region of Peel	Series DR - EA	\$3,000,000	\$4,000,000
09-Nov-01	Region of Peel	CMHC	\$0	\$33,333
14-Dec-99	Caledon	Series AD	\$4,793,000	\$6,972,000
<b>Gross Region of Peel Debentures</b>			<b>\$1,654,677,630</b>	<b>\$1,639,690,342</b>
Mortgages payable by Peel Housing Corporation			\$173,721,143	\$195,891,103
<b>Total Outstanding</b>			<b>\$1,828,398,773</b>	<b>\$1,835,581,445</b>
<b>Less:</b>	Region's sinking fund deposits		<b>-\$215,484,030</b>	<b>-\$161,972,602</b>
			\$1,612,914,743	\$1,673,608,843
<b>Less:</b>	Mississauga		<b>-\$155,895,000</b>	<b>-\$134,447,000</b>
	Caledon*		<b>-\$8,637,406</b>	<b>-\$11,136,261</b>
<b>Net Region own-purpose Debt</b>			<b>\$1,448,382,337</b>	<b>\$1,528,025,582</b>

\* Impact of Coleraine Road included.

Chart F



- In 2017, the Region did not issue external debt for its own purposes, resulting in an \$85.2 million decrease in net debt (debenture and mortgage principal and Sinking Fund provision payments).
- At year-end, the Region had internal borrowings of \$33.9 million to fund capital construction in social housing.
- The Development Charges Reserve Funds' balance at year end was a surplus of \$44.6 million. Over the course of 2017 the reserve fund balance decreased by \$69.5 million.

## 8. Energy Procurement Performance

The objectives of the Energy Commodity Procurement Policy are to establish commodity price hedging agreements that ensure regulatory compliance, provide financial flexibility and maximize procurement opportunities. In accordance with Ontario Regulation 653/05 (as amended) of the *Municipal Act, 2001*, and the Energy Commodity Procurement Policy, the Treasurer is required to annually apprise Council of the commodity hedging performance.

### Electricity

In September of 2014, the Region purchased a 10% hedge for electricity for calendar year 2017 to mitigate risks of rate volatility. No additional hedge volumes were procured after that because subsequent projections showed that 2017 market conditions would be relatively stable. The 10% hedge of approximately 43.8 million kWh was purchased at \$0.03375/kWh inclusive of transaction fees, or a total of approximately \$1.47million. The risk mitigated where the spot prices (Hourly Ontario Electricity Price or HOEP) exceeded the fixed hedge price totalled approximately \$136,000. The HOEP exceeded the fixed price only 15% of the time in 2017 (fairly stable market), which allowed the Region to take advantage of the low spot market prices.

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**Natural Gas**

The Region hedged 44% of its approximately 15.5 million m<sup>3</sup> of natural gas requirements for 2017. The hedge volume of 6.89 million m<sup>3</sup> was purchased from both the Region's gas supplier and the Housing Services Corporation at various delivery points at an average price of \$0.1597/m<sup>3</sup> inclusive of transaction fees, or a total of approximately \$1.1 million. The total risk mitigated from volatility in the natural gas market for the year was approximately \$251,000.

The fixed price hedge volumes for electricity and natural gas that were purchased for 2017 were consistent with the Region's policies and goals to address risks on commodity price volatility.

**9. Cash Management Strategy – Update**

On May 25, 2017, Audit and Risk Committee adopted a new Cash Management Strategy that was subsequently approved by Council on June 8, 2017. The strategy is aligned to the Region's risk tolerance and identifies opportunities to improve and enhance current Treasury practices with an expectation to generate additional investment returns and reduce borrowing costs.

The project outcomes identified to Audit and Risk Committee were as follows:

- Redefine the Treasury function's mandate
- Enhance the Treasury function's practices
- Increase the potential to generate greater financial returns

The Region retained Deloitte to assist with operationalizing the plan and staff is working with Deloitte to implement the plan. The current phase will address the organizational and process changes which are largely expected to be in place by year end 2018. Any changes to the current policies will be brought forward to Council early in the new term. The technology considerations for the Treasury implementation plan will be part of the broader Enterprise Resource Planning strategy.

**10. Prudent Investor Status – Update**

In May 2017, Bill 68 *Modernizing Ontario's Municipal Legislation Act* received Royal Assent in the legislature. The Bill made a number of changes to the *Municipal Act, 2001* including the extension of the Prudent Investor Standard (the "Standard") to qualifying municipalities (including the Region), which became enabled through the passing of O. Reg. 588/17.

Previously, municipal investment activities were solely regulated through O. Reg. 438/97: *Eligible Investments and Related Financial Agreements*, which restricts municipal investments to highly rated Canadian bonds, money market instruments and other similar debt instruments.

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The Standard, however, allows municipalities greater investment authority than what was previously prescribed under the *Municipal Act, 2001*. The *Trustee Act* stipulates the provisions for the Standard which can be generally viewed as a non-prescriptive, broad authority to invest as a 'prudent person' would. The *Trustee Act* outlines that a Prudent Investor must:

- view risk within the context of their total portfolio;
- make investments in view of the unique circumstances of the beneficiary;
- diversify portfolio investments across assets;
- make investments with a view toward the impact of inflation; and,
- consider total return of the investments.

Through the passing of the Regulation, municipalities now have the option to continue to invest through the prescribed list, or choose to expand their investment opportunities by participating in the Standard. By utilizing a Prudent framework, municipalities are able to generate potentially greater investment returns.

To best understand the implications of implementing a Prudent Investor framework in Peel, staff are working to evaluate options for implementation. Staff will also work with our municipal partners at the City of Toronto and other municipalities to assess best practices and lessons learned in the implementation of the Standard. Regional staff will also continue to collaborate with our local municipal partners to support the assessment of approaches to implementing the Standard in Peel.

Staff will seek to report back to Regional Council in the coming months with a more thorough analysis of changes to the regulation related to the Standard. The initial analysis will include an assessment of the risks and merits in undertaking the new investment model. Following this review, staff and Council will have the information necessary to inform the extent to our participation in the Standard.

### 11. Treasurer's Comments

It is the opinion of the Treasurer and Director of Corporate Finance that all transactions during 2017 were in compliance with the Region's Investment Goals and Policies and Ontario Regulation 438/97 in regards to investments, as well as the Region's Energy Commodity Procurement Policy and Ontario Regulation 653/05 in regards to commodity hedging, and that this report satisfies the Treasurer's legislative requirements per Ontario Regulations 438/97 and 653/05.

### FINANCIAL IMPLICATIONS

The revenue generated through investment activities in 2017 was allocated to reserves (91%), operations (6%) and some non-program Regional bank accounts (3%).

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CONCLUSION

The Region's Investment Goals and Policies provide the Region with an effective and efficient investment management operation which maximizes the rate of return on investment while ensuring safety of principal and liquidity.



Stephen VanOfwegen, Commissioner of Finance and Chief Financial Officer

Approved for Submission:



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D. Szwarc, Chief Administrative Officer

*For more information, please contact Julie Pittini, Director of Treasury Services, extension 7120, or at [julie.pittini@peelregion.ca](mailto:julie.pittini@peelregion.ca).*

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