REPORT FOR ACTION

Authority to Issue a Debenture

Date: June 18, 2020
To: Debenture Committee
From: Chief Financial Officer and Treasurer
Wards: All

SUMMARY

This report requests that the Debenture Committee approve the issuance of a 10-year sinking fund debenture in the amount of $100 million and enact the necessary borrowing by-law to give effect to this debenture issuance. The debenture was syndicated and sold in the domestic and global capital markets on June 16, 2020 and will be delivered to investors on June 30, 2020.

Details of the projects that are financed from the proceeds of this debenture are contained in Attachment A of this report.

RECOMMENDATIONS

The Chief Financial Officer and Treasurer recommends that:

1. The Debenture Committee approve the provision of long-term financing of the capital projects listed in Attachment A through the issuance of a 10-year sinking fund social debenture in the amount of $100 million in accordance with the terms and conditions set out in the purchase letter provided by the lead manager, BMO Capital Markets, and entered into by the Mayor and the Chief Financial Officer and Treasurer dated June 16, 2020 (the "Purchase Letter"), and as further described in this report.

2. Authority be granted for the introduction of the necessary Bill to the Debenture Committee to authorize the issuance of debentures.

3. The Debenture Committee authorize the appropriate City of Toronto officials to take the necessary actions to give effect thereto.

FINANCIAL IMPACT

The 2020 debt charge associated with this debenture issue is $1.5 million and is included in the City's 2020 Operating Budget in the Non-Program Corporate and Capital Financing account.

The annual debt charge, which includes sinking fund deposit and interest payments, is $10.5 million from 2021 to 2029, and $10.4 million in 2030.

DECISION HISTORY

Chapter 30, Debentures and other Borrowing of the City of Toronto Municipal Code, authorizes the Mayor (or the Deputy Mayor or the Budget Chair) and the Chief Financial Officer and Treasurer ("CFO") to enter into agreements in 2020 for the issue and sale of debentures to an aggregate amount not exceeding $1.0 billion to provide long-term financing for capital works. The terms of any such agreement to issue debentures must be reported by the CFO to the Debenture Committee for approval.
https://www.toronto.ca/legdocs/mmis/2019/ex/bgrd/backgroundfile-123459.pdf

The Chief Financial officer and Treasurer reported to the Debenture Committee about the City's new social debenture program at its meeting on May 13, 2020. The report indicated that the program responds to changes in global investor demand and aligns with the City's Corporate Strategic Plan Priorities, and may result in slightly lower borrowing costs.
http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2020.DB5.1

COMMENTS

Syndicate:

Acting in accordance with the aforementioned authorities and the unanimous advice of the City's debt syndicate's lead manager, BMO Capital Markets, and the joint-lead managers CIBC World Markets Inc., National Bank Financial Inc., and RBC Dominion Securities, the syndicate's offer to purchase the City's first social debentures, as contained in the Purchase Letter, was accepted on behalf of the City by the Mayor and the Chief Financial Officer and Treasurer.

Transaction:

The City issued a $100 million sinking fund social debenture on June 16, 2020. The debenture has a coupon interest rate of 1.60% and a maturity date of December 2, 2030. The debenture was priced to yield 1.602% to investors with an effective cost to the City of 1.665% (when dealer commissions are included). Delivery of the debenture and receipt of the proceeds will occur on June 30, 2020. This debenture has been sold and classified as a "social debenture" and the first Canadian public sector social debenture issued. The Social Debenture Program is established to align with the City's vision and strategic priorities to promote positive social outcomes.

Term:

This debenture has a 10-year term to maturity to align with the useful asset life of the underlying capital projects.

Use of Proceeds:

The City of Toronto's social debentures share the same financial and legal characteristics as other City's general obligation debentures issued in the past. They are backed by the credit and taxing power of the City. The main difference is a limitation on the use of proceeds. Under the Social Debenture Program, net proceeds from debentures are used to fund Council approved capital projects that align with the City of Toronto Social Debenture framework.

This debenture is within approved authority for borrowing in 2020. The proceeds will finance previously approved capital expenditures for the George Street Revitalization project and 1000 New Shelter Beds project from the Shelter, Support and Housing Administration, as detailed in Attachment A to this report.

Timing:

Market tone has continued to improve since City's last issuance on May 1st. Equity markets are focusing on optimism around re-opening economies and easing lockdown restrictions. The S&P/TSX equity index has recovered most of its 2020 losses and moving back towards the level seen at the end of February. The bond market continues to be favorable for the City to issue debentures.

The underlying 10-year Government of Canada interest rate was extremely attractive hovering around all-time lows. However, interest rates for bonds with longer maturities (e.g. 10-, 20-, 30-years) are expected to move slightly higher when the uncertainties surrounding COVID-19 impacts start to settle. According to Bloomberg's survey, the 10-year Government of Canada interest rate is forecasted to increase about 13 basis points by the fourth quarter of 2020.

Provincial and municipal credit spreads have significantly improved to near historic tight levels. Despite the slightly wider credit spreads from the all-time low levels, the near record low underlying Government of Canada bond yields are providing borrowers with very attractive funding costs. In addition, investors have large cash holdings due to sizable June bond interest payments in Canada.

In addition to taking advantage of favourable capital market conditions, the City also timed this issue ahead of other competing municipal supply. The transaction received very strong indications of interest and became over-subscribed shortly after City's Investors Update Conference Call on the afternoon of June 15th. To make use of this momentum, the City officially launched the transaction and priced the debenture on the morning of the June 16th.

Cost:

The City's all-in borrowing cost was at an interest rate of 1.665%. This represents the lowest borrowing cost that the City of Toronto has been able to achieve for a 10-year term. The Toronto spread over Government of Canada benchmark was 104 basis points (the Toronto spread over Province of Ontario benchmark was 22 basis points) which was slightly less than the City's typical conventional issue. The savings to the City of 1 basis point on $100 million debentures issued, in present value terms, are approximately $96K. This favourable financing is attributable to positive market conditions, investor confidence in Toronto, and investor relations work in recent years, as well as the growing demand for social debentures.

The 2020 debt charge associated with this debenture issue is $1.5 million**.** The annual debt charge, which includes sinking fund deposit and interest payments, is $10.5 million from 2021 to 2029, and $10.4M in 2030. The annual debt charges are included in the approved 2020 budget and future forecasts.

The total annual debt charges of all outstanding debentures that are supported by the City's property tax levy are within 15% of such tax levy as required by the City's policy. Also, the structure and pricing of this transaction achieved the lowest cost of funds available relative to other potential structures, markets, and currencies as permitted by the City of Toronto Act, 2006.

Distribution:

This issue achieved exceptional reception (4 times oversubscribed), with a wide placement distribution of debentures to 36 institutional accounts located across Canada, the United States, and Europe.

Other:

Council authority has been delegated to the Mayor and the CFO and Treasurer to issue an annual amount not to exceed $1.0 billion in new debt during each of the years 2019, 2020, 2021, and 2022. The planned 2020 borrowing program is $1 billion. The $200 million debenture issuance in May and this $100 million debt issuance in June leaves up to $700 million of debt issuance room remaining for the balance of this year.

CONTACT

Randy LeClair, Director, Capital Markets
Phone: 416-397-4054; E-mail: Randy.LeClair@toronto.ca

Betsy Yeung, Manager, Capital Markets
Phone: 416-392-6302; E-mail: Betsy.Yeung@toronto.ca

SIGNATURE

Heather Taylor
Chief Financial Officer and Treasurer

ATTACHMENT

Attachment 1 – Debenture Issue Summary - Project List