IB9.2

REPORT FOR ACTION

Sinking Fund and Long Term Fund - Performance and Compliance Update for the Second Quarter of 2020

Date: September 21, 2020
To: Toronto Investment Board
From: Randy LeClair, Director, Capital Markets
Wards: All

SUMMARY

As required by the City's Investment Policy, the purpose of this report is to provide the Toronto Investment Board ("Board") with the following:

1. The performance of the Sinking Fund and Long Term Fund for the second quarter of 2020, and

2. Investment Policy and Plan Compliance certificates and reports for the second quarter of 2020.

RECOMMENDATIONS

The Director, Capital Markets recommends that:

1. Toronto Investment Board receive this report for information.

FINANCIAL IMPACT

There are no financial impacts on the City's operating or capital budgets as a result of this report.

DECISION HISTORY

At its meeting of July 28, 2020, City Council adopted the report City of Toronto Investment Report for the Year 2019 and the Three Month Period Ending March 31, 2020
http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2020.EX15.10

At its meeting of July 8, 2020, the Toronto Investment Board adopted a report called the Sinking Fund and Long Term Fund - Performance and Compliance Update for 2019 and First Quarter of 2020
http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2020.IB7.3

At its meeting of June 29, 2020, City Council adopted the report Investment Policy Update
http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2020.EX14.2

At its meeting of February 19, 2020, City Council adopted the 2020 Capital and Operating Budgets:
http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2020.EX13.2

At its meeting of June 28, 2018, City Council adopted the report City of Toronto Investment Policy for 2017 and the First Quarter of 2018 and Policy Update, which set the guidelines for investment of the Sinking Fund and Long Term Fund:
http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2018.EX35.16

In 2008, the City adopted a new Investment Earnings Policy that prioritizes the order of allocation of investment earnings:
https://www.toronto.ca/legdocs/mmis/2008/ex/bgrd/backgroundfile-10354.pdf

COMMENTS

Performance Overview and Cash Flows

Sinking Fund (SF)

Seventy percent of Sinking Fund was transferred in-kind to two fixed income investment managers on May 1, 2019. The two fixed income investment managers are Fiera Capital ("Fiera LDI") and Addenda Capital ("Addenda"). During the fourth quarter of 2019, approximately seven percent of the Sinking Fund was transferred (cash) to two global equity pooled fund managers. A third global equity pooled fund manager also started in February 2020 resulting in a total equities exposure of 10% at the fund level. The three global equity pooled fund managers are Oakmark Global Pooled Fund II ("Oakmark"), Pier 21 WorldWide Equity Pool ("Pier 21"), and Fiera Capital Common Contractual Fund ("Fiera CCF"). Table 1 shows the value of the Sinking Fund managed by these five investment managers.

Table 1 - Size of Sinking Fund managed by Fiera LDI, Addenda, Oakmark, Pier 21 and Fiera CCF (Market Value in $millions)

Date	Fiera LDI	Addenda	Oakmark	Pier 21	Fiera CCF	Total
May 1, 2019	$679.8	$679.9	-	-	-	$1,359.7
June 30, 2019	$697.4	$688.2	-	-	-	$1,385.6
Sept. 30, 2019**	$506.5	$494.0	-	-	-	$1,000.5
Dec. 31, 2019	$498.7	$489.4	$62.2*	$62.0*	-	$1,112.3
Mar. 31, 2020	$511.2	$479.8	$44.6	$58.0	$46.6*	$1,140.2
June 30, 2020	$549.5	$529.6	$52.0	$66.3	$51.2	$1,248.6

*$56 million was transferred to each of Oakmark and Pier21, and $54 million was transferred to Fiera CCF

**The decline in externally managed assets as at September 30, 2019 was attributable to funds being transferred to meet a debt maturity obligation of $400 million on December 2, 2019.

Table 2 - Historical Asset Mix of the Sinking Fund

Asset Class - Sectors	Policy Target Allocation	May 1, 2019 (%)	Sept. 30, 2019 (%)	Dec. 31, 2019 (%)	Mar. 31, 2020 (%)	June 30, 2020 (%)
Segregated Sinking Fund Short Term Fund (Internal)	0.0%	23.2%	34.1%*	31.1%	29.5%	37.0%**
Cash & Cash Equivalents (Investment Managers)	0.0%	0.0%	0.1%	0.1%	0.1%	0.1%
Government of Canada & Guarantees	30.0%	0.0%	6.6%	8.0%	9.0%	7.9%
Provincial, Provincial Guarantees, & Municipal Bonds	30.0%	76.6%	44.2%	36.4%	35.7%	32.2%
Corporate Bonds	10.0%	0.2 %	15.0%	16.9%	15.8%	14.3%
Global Equities Pooled Funds	20.0%	N/A	N/A	7.5%	9.9%	8.5%
Total	10.0%	100.0%	100.0%	100.0%	100.0%	100.0%

*The increase was due to preparation for debt repayment in December 2019.

**The increase was due to new money from sinking fund deposits. The asset mix has been rebalanced by distributing the new money to the investment managers in the beginning of September 2020.

Table 3 - Asset Mix held by Sinking Fund Investment Managers as at June 30, 2020 (Market Value $ millions)

Asset Mix - Sectors	Internal City of Toronto	Fiera LDI	Addenda	Oakmark	Pier 21	Fiera CCF	Total
Segregated Sinking Fund Short Term Fund (Internal)	732.0	-	-	-	-	-	732.0 (37.0%)
Cash & Cash Equivalents (Investment Managers)	-	0.4	1.1	-	-	-	1.5 (0.1%)
Government of Canada & Guarantees	-	146.5	9.4	-	-	-	155.9 (7.9%)
Provincial, Provincial Guarantees, & Municipal Bonds	-	310.6	328.1	-	-	-	638.7 (32.2%)
Corporate Bonds	-	92.0	191.0	-	-	-	283.0 (14.3%)
Global Equities Pooled Funds	-	-	-	52.0	66.3	51.2	169.5 (8.5%)
Total	732.0	549.5	529.6	52.0	66.3	51.2	1,980.6 (100.0%)

The Sinking Fund continued to have large cash holdings. The cash holdings are held in a segregated Short Term fund specifically for the Sinking Fund. The average weighted fund balance (including segregated cash) for the second quarter of 2020 was $1.5 billion in market value. This balance was comprised of 37% segregated short term fund, 54% bonds (of which, 14% are Corporate bonds), and 9% equities. Excess cash holdings (beyond money put aside for upcoming investments in equities and real assets) was used to rebalance the portfolio asset mix during the third quarter of 2020. Bonds allocation was topped up to about the 70% level as per the target asset mix indicated in the Investment Plan.

Table 4 - Second Quarter 2020 - Market Return Performance of the Sinking Fund managed by Fiera LDI and Addenda

Fixed Income - Q2, 2020	Fiera Benchmark	Fiera LDI	Addenda Benchmark	Addenda
Total Fund Size (Market Value $millions)	N/A	$549.5	N/A	$529.6
Average term (years)	13.1	16.2	13.2	15.4
Average credit quality	N/A	AA	N/A	AAL
June 30, 2020 - Investment Return (%)*	7.5%	7.5%	7.6%	10.6%
June 30, 2020 - Investment Return (%) - Value Added*	N/A	0.0%	N/A	3.0%

* From Aon Report - Performance Review and Investment (Q2 Performance)

Table 5 - Second Quarter 2020 - Market Return Performance of the Sinking Fund managed by Pier 21, Oakmark and Fiera CCF*

Global Equities Pooled Funds - Q2, 2020	Pier 21	Oakmark	Fiera CCF
Total Fund Size (Market Value $millions)	$66.3	$52.0	$51.2
Portfolio (%)	14.3	16.7	9.7
Benchmark (%) (MSCI ACWI)	14.6	14.6	14.6
Value Added (%)	-0.3	2.1	-4.9

* From Aon Report - Performance Review and Investment (Q2 Performance)

As demonstrated in Table 6, the fixed income portion of the Sinking Fund outperformed its market return benchmark by 140 basis points during the second quarter of 2020. The global equities portion of the Sinking Fund underperformed its market return benchmark by 100 basis points during the second quarter of 2020. The total externally managed Sinking Fund underperformed its market return benchmark by 120 basis points. Further details of performance for each investment manager has been prepared by the investment consultant (Aon) in Attachment 1 and 2.

Table 6 - Second Quarter 2020 - Sinking Fund Market Return (%)*

Sinking Fund - Q2, 2020	Fixed Income	Global Equities Pooled Funds	Total Externally Managed Sinking Fund
Portfolio (%)	9.0	13.6	9.5
Benchmark (%)	7.6	14.6	8.3
Value Added (%)	1.4	-1.0	1.2

* From Aon Report - Performance Review and Investment (Q2 Performance)

On a book return basis (excluding unrealized gain and losses), during the second quarter of 2020, the Sinking Fund earned $8.3 million yielding an annualized return of 2.2%. Trading activities generated $0.2 million in realized capital gains.

Table 7 - Sinking Fund Earned Income ($millions)

Year	Average Fund Balance (Book Value)	Earned Income	Earned Return on Capital (Annualized)
2020 - Q2	$1,546.1	$8.3	2.2%
2020 - Q1	$1,513.6	$8.9*	2.4%*
Dec. 31, 2019	$1,713.8	$83.1	4.9%
2019 - Q4	$1,687.1	$14.2	3.4%
2019 - Q3	$1,875.2	$16.7	3.6%
2019 - Q2	$1,755.2	$39.9	9.4%
2019 - Q1	$1,595.5	$12.3	3.1%

*Earnings reported in Q1 were revised (Previously reported at $8.6M at an Earned Return on Capital) rate of 2.3%)

Flow of Funds - Sinking Fund

The City of Toronto has no debt maturities in 2020. The City plans to issue a total of $1 billion sinking fund debentures in 2020 depending on market conditions. As at September 18, 2020, the City has issued $606 million debenture issues for 2020 with maturities in 2029 ($200 million), 2030 ($100 million) and 2040 ($306 million). Attachment 4 shows the flow of funds for the Sinking Funds for 2020.

Long Term Fund (LTF)

Seventy percent of Long Term Fund was transferred in-kind to two fixed income investment managers on May 1, 2019. The two fixed income investment managers are Connor, Clark & Lunn Investment Management ("CC&L") and Leith Wheeler Investment Counsel Ltd ("LW").

During the fourth quarter of 2019, approximately seven percent of the Long Term Fund was transferred (cash) to two global equity pooled fund managers. A third global equity pooled manager started in February 2020 resulting in a total equity exposure of over 9% at the fund level. The three global equity pooled fund managers are Oakmark Global Pooled Fund II ("Oakmark"), Pier 21 WorldWide Equity Pool ("Pier 21"), and Fiera Capital Common Contractual Fund ("Fiera CCF").

On November 1, 2019, an additional $336 million was transferred to CC&L and LW from the excess liquidity in Short Term Fund ($168 million to each manager).

Table 8 - Size of Long Term Fund managed by CC&L, LW, Oakmark, Pier 21 & Fiera Capital (Market Value in $millions)

Date	CC&L	LW	Oakmark	Pier 21	Fiera CCF	Total
May 1, 2019	$1,050.2	$1,053.8	-	-	-	$2,104.0
June 30, 2019	$1,070.7	$1,074.2	-	-	-	$2,144.9
Sept. 30, 2019	$1,082.8	$1,087.2	-	-	-	$2,170.0
Dec. 31, 2019*	$1,242.8	$1,248.3	$122.2*	$122.8*	-	$2,736.1
Mar. 31, 2020	$1,262.0	$1,262.0	$87.7	$114.8	$103.6*	$2,830.1
June 30, 2020	$1,338.8	$1,342.3	$102.3	$131.2	$113.7	$3,028.3

*$360 million cash was transferred to the management of Oakmark, Pier 21 and Fiera CCF ($120 million each)

Table 9 - Historical Asset Mix Long-Term Fund

Asset Class - Sectors	Policy Target Allocation	May 1 2019 (%)	Sept. 30 2019 (%)	Dec. 31 2019 (%)	Mar. 31 2020 (%)	June 30, 2020 (%)
Segregated Short Term Fund (Internal)*	0.0%	25.0%	29.7%	23.7%	20.4%	19.5%
Cash & Cash Equivalents (Investment Managers)	0.0%	0.0%	0.4%	0.8%	0.6%	1.5%
Government of Canada & Guarantees	30.0%	2.7%	8.4%	7.4%	10.1%	7.4%
Provincial, Provincial Guarantees & Municipal Bonds	30.0%	63.8%	36.3%	35.6%	34.9%	36.3%
Corporate Bonds	10.0%	8.5%	25.2%	25.8%	24.7%	26.1%
Global Equities Pooled Funds	20.0%	N/A	N/A	6.7%	9.3%	9.2%
Real Assets	10.0%	N/A	N/A	N/A	N/A	N/A
Total	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%

*Segregated Short Term Fund includes cash and short-term investments that will be allocated to investment managers of the Long Term Fund.

Table 10 - Asset Mix held by Long-Term Fund Investment Managers as at June 30, 2020 (Market Value $millions)

Asset Mix - Sectors	Internal City of Toronto	CC&L	Leith Wheeler	Oakmark	Pier 21	Fiera CCF	Total
Segregated Sinking Fund Short Term Fund (Internal)	734.3	-	-	-	-	-	734.3 (19.5%)
Cash & Cash Equivalents (Investment Managers)	-	53.8	2.1	-	-	-	55.9 (1.5%)
Government of Canada & Guarantees	-	114.0	163.5	-	-	-	277.5 (7.4%)

Asset Mix - Sectors	Internal City of Toronto	CC&L	Leith Wheeler	Oakmark	Pier 21	Fiera CCF	Total
Provincial, Provincial Guarantees, & Municipal Bonds	-	741.6	623.4	-	-	-	1,365.0 (36.3%)
Corporate Bonds	-	432.9	549.8	-	-	-	982.7 (26.1%)
Global Pooled Fund Equities	-	-	-	102.3	131.2	113.7	347.2 (9.2%)
Total	734.3	1,342.3	1,338.8	102.3	131.2	113.7	3,762.6 (100.0%)

The Long Term Fund continued to have large cash and short-term investment holdings in anticipation of the upcoming investments in global equities and real assets. The ending fund balance (including segregated cash) as at June 30, 2020 was $3.6 billion (market value). This balance is comprised of 21% segregated short term fund and cash, 70% bonds (of which, 26% are Corporate bonds), and 9% equities.

Table 11 - Second Quarter 2020 - Market Return Performance of the Long-Term Fund managed by CC&L and LW

	Benchmark* (for Active subfund)	LW - Active subfund	LW - Inactive subfund	CC&L Active subfund	CC&L - Inactive subfund
Total Fund Size (Market Value $millions)	N/A	$1,096.1	$242.7	$1,100.9	$241.4
Average term (years)	11.2	11.0	7.7	11.4	7.7
Average credit quality	AA	AA	A	AA	AA
June 30, 2020 Investment Return (%)**	5.9%	6.5%	3.9%	6.9%	6.8%
June 30, 2020 Investment Return (%) - Value Added**	N/A	0.6%	N/A	1.0%	N/A

*FTSE Canada Universe Bond Index

** From Aon Report - Performance Review and Investment (Q2 Performance)

Table 12 - Second Quarter 2020 - Market Return Performance of the Long-Term Fund managed by Pier 21, Oakmark and Fiera CCF*

Global Equities Pooled Funds - Q2, 2020	**Pier 21**	**Oakmark**	**Fiera CCF**
Total Fund Size (Market Value $millions)	$131.2	$102.3	$113.7
June 30, 2020 Investment Return (%)*	14.3	16.7	9.7
June 30, 2020 Benchmark (%) (MSCI ACWI)*	14.6	14.6	14.6
June 30, 2020 Value Added Investment Return (%)*	-0.3	2.1	-4.9

* From Aon Report - Performance Review and Investment (Q2 Performance)

As shown in Table 13 below, the fixed income portion of the LTF outperformed its benchmark (FTSE Canada Universe Bond Index) by 80 basis points during the second quarter of 2020. On the other hand, the global equity portion of the LTF underperformed the benchmark by 120 basis points during the second quarter of 2020. The total externally managed Long Term Fund has outperformed its market return benchmark by 40 basis points. Further details of performance for each investment manager has been prepared by the investment consultant (Aon) in Attachment 1 and 2.

Table 13 - Second Quarter 2020 - Market Return (%) for the Long Term Fund*

Long Term Fund - Q2, 2020	**Fixed Income**	**Global Equities Pooled Funds**	**Total Externally Managed Long Term Fund**
Portfolio (%)	6.7	13.4	7.5
Benchmark (%)	5.9	14.6	7.1
Value Added (%)	0.8	-1.2	0.4

* From Aon Report - Performance Review and Investment (Q2 Performance)

The fixed income portion of the Long Term Fund is under the management of CC&L and LW, of which each are separated into an Active sub-fund and an Inactive sub-fund. The Inactive portion is less than 20% of the total assets under management for each manager. The managers are only measured and compensated for the Active sub-funds. The Inactive sub-fund holds the inherited illiquid bonds (mostly municipal bonds). The manager will progressively incorporate the Inactive sub-fund into the Active sub-fund either through bond maturities or liquidation when market conditions are appropriate. The Inactive sub-funds are expected to be fully incorporated into the Active sub-funds by 2021.

On a book return basis, Investment managers earned $41.1 million in the Long Term Fund yielding an annualized return of 4.7% during the second quarter of 2020. The trading activities during this period generated $23.0 million in realized capital gains.

Table 14 - Long Term Fund Earned Income ($millions)

Year	Average Fund Balance (Book Value)	Earned Income	Earned Return on Capital (Annualized)
2020 - Q2	$3,567.8	$41.1	4.7%
2020 - Q1	$3,531.8	$33.3*	3.8%*
YTD - Dec. 31, 2019	$2,986.1	$187.9	6.3%
2019 - Q4	$3,246.5	$23.2	2.9%
2019 - Q3	$2,973.1	$38.2	5.2%
2019 - Q2	$2,889.3	$104.3	15.2%
2019 - Q1	$2,835.2	$22.2	3.2%

*Earnings reported in Q1 were revised (Previously reported at $31.0M with an Earned Return on Capital of 3.6%)

Earned Income Requirement Update

The amount of forecasted earned investment income from the LTF required by the operating budget for 2020 is estimated at $143.0 million (equivalent to approximately 3.8% rate of earned return net of Board expenses). The $143.0 million is projected to be allocated between the operating budget ($75.0 million) and the Reserve Funds ($68.0 million). Similar to previous years, allocations will be finalized in 2021 after actual results are tabulated and confirmed by the Accounting Services Division. Table 13 shows the remaining investment income to be allocated from the $143.0 million.

Table 15 - Remaining Investment Income to be allocated in 2020

Required Income for 2020	Q1 & Q2 Earned	Remaining 2020 Requirement
$143.0	$74.4	$68.6

Flow of Funds - Long Term Fund

As reported in December 2019, there was an excess liquidity of $500 million that was not required for the Short Term Fund. Subsequently, it was transferred to the Long Term Fund on November 1, 2019 for investment in the asset mix as outlined in the Board approved Investment Plan.

There was an additional $500 million of projected excess available for transfer from the Short Term Fund to the Long Term Fund planned for April 2020. However, due to the current COVID-19 situation, this amount is no longer considered as excess liquidity and, as a result, was not transferred to Long Term Fund. Staff will continue to re-assess the City's liquidity position and advise accordingly.

Investment Policy and Plan Compliance

Council has adopted the updated Investment Policy on June 29, 2020. All investments in the Sinking Fund and Long Term Fund are consistent with the Investment Policy and the Investment Plan for the second quarter of June of 2020 (Attachment 3).

CONTACT

Randy LeClair, Director, Capital Markets;
Tel: 416-397-4054; Email: Randy.Leclair@toronto.ca

Betsy Yeung, Manager, Investments;
Tel: 416-392-6302; Email: Betsy.Yeung@toronto.ca

SIGNATURE

Randy LeClair
Director, Capital Markets

ATTACHMENTS

Attachment 1 - Discussion Guide Q2 2020 (Aon)
Attachment 2 - Performance Review and Investment (Aon) for the period ending June 30, 2020
Attachment 3 - Compliance Certificates and Reports (April 2020 - June 2020)
Attachment 4 - Flow of Funds - Sinking Funds