TORONTO

REPORT FOR ACTION

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

Date: November 12, 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 third quarter of 2020, and

2. Investment Policy and Plan Compliance certificates and reports for the third 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 October 7, 2020, the Toronto Investment Board adopted a report called the Sinking Fund and Long Term Fund - Performance and Compliance Update for the Second Quarter of 2020
http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2020.IB9.2

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 as at September 30, 2020.

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
Sept. 30, 2020	$692.4***	$695.3***	$54.8	$71.3	$55.2	$1,569.0

*$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.
***Asset mix rebalancing: $145 million was transferred to Fiera LDI and $166 million was transferred to Addenda on September 8, 2020.

Table 2 - Historical Asset Mix of the Sinking Fund

Asset Class - Sectors	Policy Range	Policy Target	5/01/19 (%)	9/30/19 (%)	12/31/19 (%)	3/31/20 (%)	6/30/20 (%)	9/30/20 (%)
Segregated Sinking Fund Short Term Fund (Internal)	0%-100%	0.0%	23.2%	34.1%*	31.1%	29.5%	37.0%**	23.0%
Cash & Cash Equivalents (Investment Managers)	0%-5%	0.0%	0.0%	0.1%	0.1%	0.1%	0.1%	0.2%
Government of Canada & Guarantees	0%-100%	30.0%	0.0%	6.6%	8.0%	9.0%	7.9%	14.6%
Provincial (and Guarantees) & Municipal Bonds	0%-100%	30.0%	76.6%	44.2%	36.4%	35.7%	32.2%	38.5%

Asset Class - Sectors	Policy Range	Policy Target	5/01/19 (%)	9/30/19 (%)	12/31/19 (%)	3/31/20 (%)	6/30/20 (%)	9/30/20 (%)
Corporate Bonds	0%-60%	10.0%	0.2%	15.0%	16.9%	15.8%	14.3%	14.8%
Global Equity Pooled Funds	0%-30%	20.0%	N/A	N/A	7.5%	9.9%	8.5%	8.9%
Real Assets	0%-15%	10.0%	N/A	N/A	N/A	N/A	N/A	N/A
Total		100.0%	100.0%	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 September 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)	467.1	-	-	-	-	-	467.1 (23.0%)
Cash & Cash Equivalents (Investment Managers)	-	1.2	3.7	-	-	-	4.9 (0.2%)
Government of Canada & Guarantees	-	208.0	89.9	-	-	-	297.9 (14.6%)
Provincial (and Guarantees) & Municipal Bonds	-	369.5	415.1	-	-	-	784.6 (38.5%)
Corporate Bonds	-	113.7	186.6	-	-	-	300.3 (14.8%)
Global Equity Pooled Funds	-	-	-	54.8	71.3	55.2	181.3 (8.9%)
Total	467.1	692.4	695.3	54.8	71.3	55.2	2,036.1 (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 third quarter of 2020 was $2.0 billion in market value. This balance was comprised of 23% segregated short term fund, 68% bonds (of which, 15% 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. The fixed income allocation was topped up to the 70% level (approximately) as per the target asset mix indicated in the Investment Plan.

As demonstrated in Table 4, the fixed income portion of the Sinking Fund outperformed its market return benchmark by 20 basis points during the third quarter of 2020. The global equity portion of the Sinking Fund outperformed its market return benchmark by 100 basis points during the third quarter of 2020. The total externally managed Sinking Fund underperformed its market return benchmark by 30 basis points. Despite the fact that both asset classes outperformed their respective benchmarks, the overall invested asset underperformance was due to how the fund benchmark return was weighted. The benchmark for the total fund is calculated based on the weighted average return of the target asset mix, the plan is currently transitioning towards the target asset mix and is not fully allocated at the moment. The fourth and last global equity pooled fund manager is expected to be on board by the end of 2020. For performance breakdown by investment manager, please see table 5 and 6. Further details of performance for each investment manager has been prepared by the investment consultant (Aon) in Attachment 1 and 2.

Table 4 - Third Quarter 2020 - Sinking Fund Market Return (%)*

Sinking Fund - Q3, 2020	**Fixed Income**	**Global Equity Pooled Funds**	**Total Externally Managed Sinking Fund**
Portfolio Market Return (%)	0.0	7.0	0.9
Benchmark (%)	-0.2	6.0	1.2
Value Added (%)	0.2	1.0	-0.3

* From Aon Report - Performance Review and Investment (Q3 Performance)

Table 5 - Third Quarter 2020 - Market Return Performance of the Sinking Fund managed by Fiera LDI and Addenda

Fixed Income - Q3, 2020	Fiera LDI	Addenda
Total Fund Size (Market Value $millions)	$692.4	$695.3
Portfolio Average term (years)	16.5	14.9
Benchmark Average term (years)	13.0	13.3
Average credit quality	AA	AAL
Q3 Portfolio Return* (%)	-0.1%	0.1%
Q3 Benchmark Return* (%)	-0.1%	-0.2%
Q3 Value Added* (%)	0.0%	0.3%

* From Aon Report - Performance Review and Investment (Q3 Performance)

Table 6 - Third Quarter 2020 - Market Return Performance of the Sinking Fund managed by Pier 21, Oakmark and Fiera CCF*

Global Equities Pooled Funds - Q3, 2020	Pier 21	Oakmark	Fiera CCF
Total Fund Size (Market Value $millions)	$71.3	$54.8	$55.2
Portfolio Market Return (%)	7.7	5.4	7.9
Benchmark (%) (MSCI ACWI)	6.0	6.0	6.0
Value Added (%)	1.7	-0.6	1.9

* From Aon Report - Performance Review and Investment (Q3 Performance)

On a book return basis (excluding unrealized gain and losses), during the third quarter of 2020, the Sinking Fund earned $10.4 million yielding an annualized return of 2.6%. Trading activities generated $2.7 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 - Q3	$1,607.1	$10.4	2.6%
2020 - Q2*	$1,546.1	$8.0	2.1%
2020 - Q1*	$1,513.6	$8.8	2.3%
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%

*Due to accounting adjustment on bank interest earned, Q1 was previously reported at $8.9M Earned Income and rate of return of 2.4%. Q2 was previously reported at $8.3M Earned Income and rate of return of 2.2%

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
September 30, 2020	$1,349.3	$1,348.7	$107.9	$141.2	$122.6	$3,069.7

*$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 Range	Policy Target	5/1/19 (%)	9/30/19 (%)	12/31/19 (%)	3/31/20 (%)	6/30/20 (%)	9/30/20 (%)
Segregated Short Term Fund (Internal)*	0%-100%	0.0%	25.0%	29.7%	23.7%	20.4%	19.5%	19.3%
Cash & Cash Equivalents (Investment Managers)	0%-5%	0.0%	0.0%	0.4%	0.8%	0.6%	1.5%	0.8%
Government of Canada & Guarantees	0%-100%	30.0%	2.7%	8.4%	7.4%	10.1%	7.4%	8.9%
Provincial (and Guarantees) & Municipal Bonds	0%-100%	30.0%	63.8%	36.3%	35.6%	34.9%	36.3%	35.0%
Corporate Bonds	0%-60%	10.0%	8.5%	25.2%	25.8%	24.7%	26.1%	26.2%
Global Equity Pooled Funds	0%-30%	20.0%	N/A	N/A	6.7%	9.3%	9.2%	9.8%

Asset Class - Sectors	Policy Range	Policy Target	5/1/19 (%)	9/30/19 (%)	12/31/19 (%)	3/31/20 (%)	6/30/20 (%)	9/30/20 (%)
Real Assets	0%-15%	10.0%	N/A	N/A	N/A	N/A	N/A	N/A
Total		100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100%

*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 September 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)	735.9	-	-	-	-	-	735.9 (19.3%)
Cash & Cash Equivalents (Investment Managers)	-	27.0	2.9	-	-	-	29.9 (0.8%)
Government of Canada & Guarantees	-	158.4	181.7	-	-	-	340.1 (8.9%)
Provincial (and Guarantees) & Municipal Bonds	-	684.1	648.1	-	-	-	1,332.3 (35.0%)
Corporate Bonds	-	479.8	516.0	-	-	-	995.8 (26.2%)
Global Pooled Fund Equities	-	-	-	107.9	141.2	122.6	371.7 (9.8%)
Total	735.9	1,349.3	1,348.7	107.9	141.2	122.6	3,805.6 (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 September 30, 2020 was $3.6 billion (market value). This balance is comprised of 20% segregated short term fund and cash, 70% bonds (of which, 26% are Corporate bonds), and 9% equities.

As shown in Table 11 below, the fixed income portion of the LTF outperformed its benchmark (FTSE Canada Universe Bond Index) by 20 basis points during the third quarter of 2020. The global equity portion of the LTF outperformed the benchmark by 110 basis points during the third quarter of 2020. The total externally managed Long Term Fund has underperformed its market return benchmark by 10 basis points. Despite the fact that both asset classes outperformed their respective benchmarks, the overall invested asset underperformance was due to how the fund benchmark return was weighted. The benchmark for the total fund is calculated based on the weighted average return of the target asset mix, the plan is currently transitioning towards the target asset mix and is not fully allocated at the moment. The fourth and last global equity pooled fund manager is expected to be on board by the end of 2020. For performance breakdown by investment manager, please see Table 12 and 13. Further details of performance for each investment manager has been prepared by the investment consultant (Aon) in Attachment 1 and 2.

Table 11 - Third Quarter 2020 - Market Return (%) for the Long Term Fund*

Long Term Fund - Q3, 2020	**Fixed Income**	**Global Equities Pooled Funds**	**Total Externally Managed Long Term Fund**
Portfolio (%)	0.6	7.1	1.5
Benchmark (%)	0.4	6.0	1.6
Value Added (%)	0.2	1.1	-0.1

* From Aon Report - Performance Review and Investment (Q3 Performance)

Table 12 - Third 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	$1,128.4	$220.3	$1,216.4	$132.9
Average term (years)	11.1	11.0	8.0	11.2	7.2
Average credit quality	AA	AA	A	AA	AA
Sept 30, 2020 Investment Return (%)**	0.4%	0.6%	0.9%	0.6%	0.4%
Sept 30, 2020 Investment Return (%) - Value Added**	N/A	0.2%	N/A	0.2%	N/A

*FTSE Canada Universe Bond Index

** From Aon Report - Performance Review and Investment (Q3 Performance) and individual manager's reporting

Table 13 - Third Quarter 2020 - Market Return Performance of the Long-Term Fund managed by Pier 21, Oakmark and Fiera CCF*

Global Equities Pooled Funds - Q3, 2020	Pier 21	Oakmark	Fiera CCF
Total Fund Size (Market Value $millions)	$141.2	$107.9	$122.6
Sept 30, 2020 Investment Return (%)*	7.7	5.4	7.9
Sept 30, 2020 Benchmark (%) (MSCI ACWI)*	6.0	6.0	6.0
Sept 30, 2020 Value Added Investment Return (%)*	1.7	-0.6	1.9

* From Aon Report - Performance Review and Investment (Q3 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 $46.2 million in the Long Term Fund yielding an annualized return of 5.2% during the third quarter of 2020. The trading activities during this period generated $29.7 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 - Q3	$3,610.8	$46.2	5.2%
2020 - Q2*	$3,567.8	$40.6	4.6%
2020 - Q1*	$3,531.8	$32.8	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%

* Due to accounting adjustment on bank interest earned, Q2 was previously reported at $41.1M (4.7%) and Q1 were previously reported at $33.3M (3.8%)

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 15 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 to Q3 Earned	Remaining 2020 Requirement
$143.0	$119.6	$23.4

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 third quarter as of September 30, 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 - Toronto Investment Board - Discussion Guide Q3 2020 (Aon)
Attachment 2 - Performance Review and Investment (Aon) - September 30, 2020
Attachment 3 - Compliance Certificates and Reports (July 2020 - September 2020)
Attachment 4 - Flow of Funds - Sinking Funds