REPORT FOR ACTION

City of Toronto Investment Report for the Year 2022

Date: May 23, 2023
To: Executive Committee
From: Chief Financial Officer and Treasurer
Wards: All

SUMMARY

The purpose of this report is to provide the following information:

1. Performance of the Funds for the year 2022
2. General Market Update and Benchmark Performance
3. City of Toronto Investment Policy and Procedures

The City's General Group of Funds ("General Fund") hold the working capital and amounts designated for the City's reserves and reserve funds. The General Fund is comprised of two pools of investments: (a) the Short Term Fund (liquidity funds managed internally), and (b) the Long Term Fund (funds not immediately required are managed by the Toronto Investment Board). The General Fund had a book return of 0.9 percent and generated $92 million for the full year 2022.

During the pandemic, the General Fund has held a larger position in the Short Term Fund to enhance the liquidity and to generally lower the overall risk (risk management). On average, the Short Term Fund, including the short-term investments of the Long Term Fund, was about 65% of the overall General Fund in 2022 compared to 48% from the pre-pandemic level in 2019. This higher weighting in the Short Term Fund provided significant protection, as well as increased returns as short-term rates moved higher.

The City's Sinking Fund portfolio, which holds the investment funds for future debt repayments, also had a return of 0.9% on the book return basis and generated $18 million for the 12 months ending December 31, 2022.

Since January 1, 2018, the City's long-term investments (Long Term Fund and Sinking Fund) have been managed by the Toronto Investment Board ("Board") under a Council adopted Investment Policy which is based on the prudent investor standard. The investment portfolios have been progressively phased in to make use of the broader range of investments that have become available. Although the overall portfolio risk has been reduced through asset mix diversification, the potential for volatility in total returns over the short-term investment horizon still exist while the risk-adjusted total returns over the long-term investment horizon are expected to be higher.

The Board manages four external fixed income managers and four external global equity managers engaged in managing the long-term investments. Both fixed income and equity investment classes are fully funded in accordance with the target asset mix in the Investment Policy with 70 percent allocated to fixed income and 20 percent to global equities. As at December 31, 2022, approximately 90 percent of both the Sinking Fund and the Long Term Fund were managed by external fund managers. The remaining 10 percent will be allocated to real assets, which is currently at the contract negotiation phase with the Board selected investment managers. Adding real assets to the current investment portfolios, which already compose of fixed income and global equity, will help to enhance the portfolios' risk-adjusted investment return and align with the Council-approved policy target asset mix. The Board continues to evaluate opportunities in the real asset category.

The Long Term Fund has an asset mix of both equity investments and fixed income investments. Due to the equity market downturn experienced in 2022 the total return results (which includes unrealized gains and losses) in both the Long Term Fund and the Sinking Fund were negatively impacted during 2022. In addition, due to global central banks implementing sharp increases to short-term interest rates it resulted in negative total returns for investors holding long-term assets like fixed income and global equities. It has been more than a decade since the world has experienced such a dramatic change in these rates and the inflation rates experienced globally. For example, the widely followed fixed income benchmark, called the FTSE Canada Universe Bond Index, had a 1-year return of -11.7 percent at December 31, 2022. A negative return for this bond index is extremely rare (it has only experienced a negative 1-year return in three years since 1983), as well as the magnitude of this decline has never been experienced in the last 40 years (largest decline previously was -4.31 in 1994).

It is a legislative requirement that the Investment Policy be reviewed annually. Staff have reviewed the Investment Policy and are not currently recommending any changes given that the policies have only been in place since 2018 and in that time we have experienced three years of volatility triggered by COVID-19 impacts. The City of Toronto Investment Policy can be reviewed in Attachment 1 of this report.

Although the prudent investor standard has only been in place for four years, and was carefully phased in, we have been monitoring whether this change was effective versus the previous prescribed list (prior to 2018). The report also provides a comparison of returns between the previously used prescribed list versus the currently used prudent investor standard. The review shows the current regulation has been beneficial to the Long Term Fund by approximately $200 million over the four years it has been in place.

For the year 2022, all funds managed are compliant with the Investment Policy. The City's auditor, KPMG LLP, will perform the Investment Policy audit during the second half of 2023.

The Board has hired a third-party data provider in order to monitor and report on the high-level Environmental, Social, and Governance (ESG) attributes of the City's investment portfolio. This investment fund-level ESG reporting process will complement the existing corporate-level ESG performance report. This service is relatively new and staff are working with the vendor to develop a report that will provide an overview of the City's portfolios from an ESG perspective. It is expected this new report will be included in the next investment performance report in approximately six months.

The Russian invasion of the Ukraine occurred in February 2022 and all contracts with external investment managers include clauses prohibiting investment in sanctioned companies and countries. These contracts also include clauses that focus on anti-terrorism and anti-money laundering policies and prohibit dealing with any sanctioned companies or countries in this regard.

Subsequent to December 31, 2022, with a moderation of inflation and other related economic data, it would seem many central banks, such as the Bank of Canada, have now paused any further short-term interest rate increases. Since it would appear the actions of central banks are near a terminal point, with the prospect of lower interest rates in the future, long-term assets have rebounded to provide significantly higher returns in the first three months of 2023 ending March 31, 2023.

Other related events happening in the first few months of 2023 show the impact of higher interest rates. More specifically, we have seen several regional bank failures in the U.S. In addition, troubles with Swiss bank Credit Suisse resulted in them being purchased by Union Bank of Switzerland (UBS) in a move negotiated by Swiss regulators. While the funds managed by the Board were largely insulated from these events, caution is being advised to external investment managers as other financial and corporate issues may emerge as we progress through 2023.

RECOMMENDATIONS

The Chief Financial Officer and Treasurer recommends that:

1. City Council receive this report for information.

FINANCIAL IMPACT

From an operating budget perspective, when recognizing only realized gains and losses within the General Fund earned $92.4 million and $27.5 million was allocated to reserve funds in accordance to the Council-approved interest allocation policy. The remaining ($57.3 million) was allocated to the operating plan after Toronto Investment Board expenses in 2022 ($7.6 million) were deducted.

When using only realized gains and losses the City's Sinking Funds portfolio earned $18.9 million for the year 2022. These earnings are retained within the Sinking Funds and must be used for the purpose of retiring debenture debt at maturity.

DECISION HISTORY

At its meetings held on June 15, 16, 2022 City Council received the report from the Chief Financial Officer and Treasurer for information. This report provided the performance and compliance for year 2021.
https://secure.toronto.ca/council/agenda-item.do?item=2022.EX33.6

At its meetings held on December 15, 16, 17, 2021 City Council received the report from the Chief Financial Officer and Treasurer for information. This report provided the performance and compliance for the six month period ending June 30, 2021.
http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2021.EX28.4#

At its meetings held on July 17, 2021, City Council received the report from the Chief Financial Officer and Treasurer for information. This report provided the performance and compliance for the year 2020.
http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2021.EX25.6

At its meetings held on June 29 and 30, 2020, City Council adopted the Investment Policy Update report with amendments.
http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2020.EX14.2

COMMENTS

General Market Update for 2022

While concerns over the global pandemic faded during 2022 and the world emerged from lockdowns, the driving force for markets was the high inflation created by low interest rates, surging demand, and supply chain disruptions. Inflation as measured by the Consumer Price Index (CPI) reached levels not seen in decades and was far above the 2 percent target level that many central banks deem as acceptable. As a result, central banks globally started to tighten credit conditions through the use of higher short-term interest rates to slow an economy down and correct the supply/demand imbalance.

In Canada, a number of key milestones drove the economy and market returns:

- Inflation (as measured by CPI) reached as high as 8.1 percent in June 2022, this was an increase of 5.1 percent on a year-over-year basis which was the largest 12-month jump since 1951. The CPI dropped to 6.3 percent by December 2022 however inflation is still above the 2 percent target used by the Bank of Canada;

- The Bank of Canada responded to this high inflation with a series of seven increases to the short-term overnight rate starting in March 2022. This rate started 2022 at 0.25 percent and finished the year 400 basis points higher at 4.25 percent. There has been an additional increase of 0.25 percent to this rate in early 2023. An increase of this magnitude has not been seen since before the financial crisis in 2008;

- Longer term interest rates followed suit and moved substantially higher. For example the yield on the 30-year Government of Canada bond increased the most in a single year since 1994. Higher interest rates means the value of bonds fall which resulted in the largest negative return on bonds in 40 years with the widely followed benchmark FTSE Canada Universe Bond Index down 11.7 percent;

- A phenomenon known as "the inverted yield curve" persisted for most of 2022. This happens when short-term interest rates are higher than long-term interest rates. The inverted yield curve is usually a precursor to the start of an economic recession. The last inverted yield curve happened over 10 years ago before the financial crisis in 2008;

- Higher interest rates also impacted Canada's housing market, with a drop in average home prices were down 12 percent in December 2022 which is the largest year-over-year decline in over 40 years of records.

Other global central banks, including the U.S. Federal Reserve, followed a similar course of action with similar results. In the U.S. most notably:

- The 10-year Treasury yield gapped higher by more than 250 basis points from March 2022 to late October 2022. That was the fastest rise in this yield in such a condensed timeframe since 1987.

- The gap in yield between 3-month T-bills and 10-year Treasuries topped 70 bps in December 2022 which is the deepest inversion since 1981.

Global equity markets also fell in 2022 in reaction to the rising interest rate environment and the potential for a general slowdown or recession in the economy. It is very rare to see equity market returns negative at the same time bond returns are negative and it has not happened in over 50 years (last occurrence was 1969). Some of the selected equity market returns for the year 2022 were (in Canadian dollars):

- S&P/TSX Composite Index down 5.8 percent
- S&P 500 Index down 12.2 percent
- MSCI All-Country World Index (ACWI) down 12.4 percent
- MSCI Emerging Markets Index down 14.3 percent

The Russian invasion of Ukraine in February 2022 was also a cause for concern for many financial market participants. Whether this conflict resulted in supply chain disruptions or concerns that it may escalate or spill-over to other countries remained an additional risk throughout 2022 and into 2023. As a side note, all contracts with external investment managers include clauses prohibiting investment in sanctioned companies and countries. These contracts also include clauses that focus on anti-terrorism and anti-money laundering policies and prohibiting dealing with any sanctioned companies or countries in this regard.

Subsequent Events - 2023

First, the impact of higher interest rates are now being seen with several regional bank failures in the U.S. In addition, troubles with Swiss bank Credit Suisse resulted in them being purchased by Union Bank of Switzerland (UBS). While the funds managed by the Board were largely insulated from these events, caution is being advised to external investment managers as other financial and corporate issues may emerge as we progress through 2023.

Secondly, a sharp rebound higher in many markets is developing as it would appear central banks have completed or nearing completion of the interest rate increases. For example, three month returns as at March 31, 2023, we have seen the major indices move significantly higher:

- FTSE Canada Universe Bond Index up 3.2 percent
- S&P/TSX Composite Index up 4.6 percent
- S&P 500 Index up 7.4 percent
- MSCI All-Country World Index (ACWI) up 7.2 percent
- MSCI Emerging Markets Index up 3.8 percent

As an example of the impact of public markets on investment returns in 2022, we have provided the results of several key pension funds that have reputable track records in Table 1 which demonstrates the need to review investment returns over longer periods. The results in the select pension funds show a sub-par performance for the single year (2022) as compared to their longer term (10-year) track records. Most of the performance "drag" in 2022 was attributable to public market investments. In fact, all the pension funds on Table 1 had losses in their "public market" investments to varying degrees. Where they were different was on the "private market" side which includes items like real assets, private credit, and private equity. The City of Toronto's investment plan is currently transitioning towards the target asset mix by adding real assets as the final step which is currently in contract negotiation stage with the real assets manager.

Table 1 - Pension Fund Comparable

	10-year Return	2022 Return
Healthcare of Ontario Pension Plan (HOOPP)	8.35%	-8.60%
Ontario Teachers' Pension Plan (OTPP)	8.50%	4.00%
Ontario Municipal Employees Retirement System (OMERS)	7.50%	4.20%
Canada Pension Plan Investment Board (CPPIB)	10.00%	1.90%*

*As at December 31, 2022, year-end is March 2023.

Background on City of Toronto Investment Funds

Working capital and the amounts designated for reserves and reserve funds are held for investment in the City's General Group of Funds ("General Fund"). The General Fund is comprised of two sub-funds known as the Short Term Fund and the Long Term Fund. Given the specific purpose of the Sinking Fund (debt retirement), it is managed separately from the General Fund but adheres to the same primary investment beliefs and objectives. Attachment 2 provides a short background on the City's investment funds.

In November 2015, the province amended Ontario Regulation 360/15 the investment regulations under the City of Toronto Act, 2006 which replaced the prescribed list of investments with what is known as the prudent investor standard. The prudent investor standard is not specific and is used in situations where there is a trustee that has a fiduciary responsibility over funds that should invest according to the beneficiaries' situation and to consider the risk and return profile of the overall portfolio. This change removed the previous limitations and allows the City to be responsible for its own investment decisions as a prudent investor. The change required the City to establish an independent local board that would have fiduciary duty over the City's funds that were not immediately required. This local board can hire agents (external investment managers) which would carry out the fiduciary duty of the board.

Although this new provincial regulation was announced in late 2015, the effective date for this new regulation was January 1, 2018. During this transition period the City created the Toronto Investment Board (the "Board") and appointed six independent members who have substantial knowledge and experience in the financial markets. In addition, City Council approved a new Investment Policy reflecting a target asset mix with 70 percent allocated to fixed income and 20 percent to global equities to diversify the investment risk. Prior to the creation of the Board, the City's investments were all managed internally by City staff and were limited to a prescribed list of eligible investments set by the province in the legislation. This prescribed list limited the City investments to primarily government bonds and some high quality bonds of financial institutions.

While the Board would be responsible for "funds not immediately required", internal staff continue to manage the Short Term Fund to meet City's liquidity needs while maximizing investment return in accordance to the regulation.

During 2018, the Board chose eight external investment managers to manage the fixed income (70%) and global equity (20%) allocations as outlined in their Investment Plan. The new investment policy and plan, in conjunction with the investment consultant and investment managers, are expected to result in improved investment returns over the longer-term while also reducing overall portfolio risk. A comparison of the results under the prudent investor standard versus a theoretical prescribed list appears later in this report (Table 2).

There was a transition period before reaching the long-term target asset mix and realizing optimal long-term returns. During this time the investment portfolio phased in a greater use of the broader range of investments that became available. Although the portfolio risk continued to be reduced, the potential for volatility in short-term returns would still exist.

In June 2018, Council approved the creation of the Investment Income Stabilization Reserve. This reserve was established for the purpose of stabilizing investment income contributions to the operating budget by minimizing in-year variances through receiving funds in years when investment income is in excess of the amount expected in the operating budget and withdrawing funds in years when investment income is below budget.

During 2019, invested assets in both the Long Term Fund and the Sinking Fund were managed by four external fixed income investment managers (70%) and two global equity pooled fund managers (7%). The third global equity pooled fund manager was added in February 2020 for both the Long Term Fund and the Sinking Fund. The fourth and final global equity pooled fund manager was added in December 2020 and January 2021 for the Long Term Fund and the Sinking Fund respectively. Both fixed income and equity asset classes are fully funded in accordance to the target asset mix in the Investment Policy. As at December 31, 2022, approximately 90 percent of both the Long Term Fund and the Sinking Fund were managed by external investment managers selected by the Board.

The four fixed income investment managers are Connor, Clark & Lunn Investment Management ("CC&L") and Leith Wheeler Investment Counsel Ltd ("LW") for the Long Term Fund, as well as Fiera Capital ("Fiera LDI") and Addenda Capital ("Addenda") for the Sinking Fund.

The four global equity pooled fund managers are Oakmark Global Pooled Fund II ("Oakmark"), Pier 21 WorldWide Equity Pool ("Pier 21"), Fiera Capital Common Contractual Fund ("Fiera CCF"), and Legal & General Investment Management ("LGIM") for both the Long Term Fund and the Sinking Fund.

The remaining cash holdings are for future investment in real assets and upcoming debt repayment. The Board has selected two real asset investment managers to date (currently under contract negotiation) and will continue to evaluate investment opportunities in real assets.

Prescribed List versus the Prudent Investor Standard - Comparison

Previous to 2018, the City of Toronto followed investment regulations which were known as a "prescribed list". In other words, the provincial regulations provided a list of acceptable investments that were primarily government bonds, and a few high quality financial (bank) bonds. This was changed in 2018 with the overhaul of this regulation that allowed for the "prudent investor standard" and the creation of the Board and the hiring of professional money managers.

With four completed years of the new regulations, staff have developed a simple comparison to compare the "prescribed list" to the "prudent investor standard" using the Long Term Fund to answer the question is the City of Toronto any further ahead given the changes in regulation. While the new investment managers were phased in over the past few years starting in 2019, and still more to be added, there was an interest to see if there was a difference at this relatively early stage. Results are shown below in Table 2.

Table 2 - Prescribed List versus the Prudent Investor Standard - Comparison

Year-End	Prescribed List Return[1] (%)	Prudent Investor Return[2] (%)	Difference[3] (%)
2019	6.42	6.20%	-0.20
2020	8.69	10.30%	1.61
2021	-2.97	2.00%	4.97
2022	-11.69	-11.20%	0.40
4-Year Return	**-1.04**	**6.12**	N/A
Compound Annual Growth Rate	**-0.26**	**1.50**	N/A

[1] FTSE Canada Universe Bond Index was used to replicate the Prescribed List

[2] Prudent Investor Return was the actual returns of the Long Term Fund

[3] Difference is the Prudent Investor Return minus the Prescribed List Return

The outperformance of the Prudent Investor Standard over four years is the equivalent of approximately $200 million in total dollar terms on the close to $3 billion initially invested under this new regulation for the Long Term Fund.

It would seem the Prudent Investor Standard is proving to be an effective tool for diversification of returns and improving the risk profile of the Long Term Fund. It is expected the gap in performance will continue to grow and compound over time and as the Investment Policy asset mix is fully implemented.

General Fund Total Return Performance for 2022

As shown in Table 3 below, the Short Term Fund (STF) has outperformed the benchmark by 90 basis points (0.9 percent), the Long Term Fund (LTF) has underperformed the benchmark by 170 basis points (1.7 percent), and together the General Fund has slightly outperformed the benchmark return by 10 basis points (0.1 percent) in the year 2022. From a longer investment horizon perspective, the General Fund has outperformed the market benchmark by 50 basis points (0.5 percent) on a 4-year annualized return basis.

Table 3 –Total Returns versus Market Benchmarks (%) for the General Fund[1] as at December 31, 2022

	1 year (Year-over-Year)			4 year (annualized)		
	Short Term Funds[2]	Long Term Fund	General Fund[3]	Short Term Funds[2]	Long Term Fund	General Fund[3]
Portfolio Return (%)	2.6%	-11.2%	-1.6%	1.7%	1.7%	1.7%
Benchmark Return (%)	1.7%	-9.5%	-1.7%	1.0%	1.6%	1.2%
Value Added (%)	0.9%	-1.7%	0.1%	0.7%	0.1%	0.5%

[1]Calculated from RBCIS Performance Analytics and Aon, Performance Review
[2]Including cash portion of the Long Term Fund
[3] Weighted by Market value of the Short Term and long Term funds

The prolonged period of unusually volatile market conditions during 2022 resulted in a very rare market abnormality of negative annual returns from both stocks and bonds. There have been only two other calendar years when both stocks and bonds had negative returns, which was in 1931 and 1969. The stock and bond markets are usually negatively correlated to each other which they tend to move in opposite directions and present good risk diversification in an investment portfolio. Subsequent to year-end 2022, this abnormality started to reverse itself in early 2023 and is expected to resume their long-term relationship.

As demonstrated in Table 4 below, the General Fund, which is composed of both the Short Term Fund and the Long Term Fund, had an average total fund balance of $10.6 billion during the year. When excluding unrealized gains and losses from the total return, the General Fund earned $92.4 million (0.9% annualized rate of return on capital) over the year 2022.

Table 4 - Investment Portfolio for the year 2022 ($millions)

Portfolio	Average Fund Balance	Book Income	Book Return on Capital
1. Long Term Fund	$3,682.0	-$85.5	-2.3%
2. Short Term Fund	$6.903.0	$177.9	2.6%
Total General Funds	$10,585.0	$92.4	0.9%

All the losses were realized in the fixed income portion of the Long Term Fund as shown in Table 5 below as a result of sharp interest rates increases in 2022.

However, book income (realized gain/losses) is not a complete picture of the performance as it leaves out an unrealized gains and losses. While total (market) return (1-year period) is still negative, it outperformed the market benchmark by 0.6%.

Table 5 - Book Income Attribution for Long Term Fund - 2022 ($millions)

Long Term Fund Earned Income by Asset Class as at December 31, 2022 ($ millions)	
Fixed Income	-99.7
Global Equities	5.3
Short Term Investments	8.9
Total Earned Income	**- 85.5**

As shown in Table 6 below, the total book income earned (excluding unrealized gains and losses) in 2022 was $37.5 million lower than the budgeted income contribution to the operating budget. It should be noted that performance measured by book value is for the accounting and budget purposes only while the total return (market value) reflects the current value of the portfolio. Historical allocation of gross investment earnings is shown in Attachment 5.

Table 6 - Actual and Budget Investment Earnings (Operating Budget) for 2022

Book Investment earnings ($ millions & Annualized Rate of Return)	**Actual**	**Budget**	**Over/Under Budget**
1. Long Term Fund	-$113.0	$67.9	-$180.8
2. Short Term Fund	$177.9	$34.6	$143.3
Total General Funds	**$64.9**	**$102.4**	**-$37.5**

[1]Includes income allocation to Reserve Fund, which was $1M higher than budgeted for the year 2022.

Investment earnings ($92.4 million) were allocated to eligible reserve funds ($27.5 million) and the Operating Budget ($57.3 million) after deducting investment expenses ($7.6 million) in accordance to the Council-approved interest allocation policy.

In addition, the City's Short Term Fund that mainly holds City's working capital is currently at a higher level to ensure sufficient liquidity during the pandemic at the cost of some investment returns. On average, the Short Term Fund, including the short-term investments of the long term fund, was about 65% of the overall General Fund in 2022 compared to 48% from the pre-pandemic level in 2019. We expect the short-term balance to return to pre-COVID levels once the pandemic is over and post-pandemic impact is assessed. As shown in Table 6 above, the higher balance in the Short Term

Fund in the rising interest rate environment provided much higher income than budgeted while allowing for protection and manage the Covid financial impacts.

Sinking Fund Total Return Performance in 2022

The City's Sinking Fund portfolio, which holds the investment funds for future debt repayments, had underperformed the weighted market benchmark by 1.1%, with a -1.8 percent annualized total return for the three year period ending December 31, 2022 as shown in Table 7. On a shorter term basis, the fund had a total return of -13.9 percent for the year 2022, underperforming the weighted market benchmark by 1.9 percent (also shown in Table 7).

The blended benchmark for the total sinking fund is calculated based on the weighted average return of the target asset mix including real assets, the plan is currently transitioning towards the target asset mix and is not fully allocated at this point. Excluding the cash set aside for the upcoming investment in real assets, the externally managed invested assets (long term fund portion of the sinking fund) actually outperformed the weighted market benchmark by 0.2%.

The prolonged period of unusually volatile market conditions during 2022 resulted in a very rare market abnormality of negative annual return from both stocks and bonds There have been only two other calendar years when both stocks and bonds had negative returns which were 1931 and 1969. The stock and bond markets are usually negatively correlated to each other and present good risk diversification in an investment portfolio.

The Board had selected and entered into agreements with two fixed income investment managers and four global equity pooled fund managers to invest the Sinking Fund. The investment managers use a customized benchmark index that more appropriately reflects the updated fixed income strategy (LDI - Liability Driven Investment) based on the required cash flows to fund future liabilities. The customized benchmark index does not have enough history for the 4-year measurement.

Liability Driven Investment (LDI) is very different than the active strategy used for the Long Term Fund. With the LDI strategy, an investment manager focuses on the debt repayment (liability) and match the asset purchases to those maturity dates. This is similar to how insurance companies and pension funds manage their risk.

Table 7 below shows the duration of the invested assets closely matches the duration of the liabilities in the Sinking Fund. Bond duration is measurement of interest rate risk. It is a way of measuring how much bond prices are likely to change if and when interest rates move. By matching the duration of the assets and liabilities, investment managers can substantially manage the interest rate risk in the portfolio. In effect, the external managers are working to "immunize" the portfolio to ensure the fund with have cash available when the obligation comes due.

In addition, the Sinking Fund receives regular contributions throughout the year in accordance with the regulations and by-laws when debt is issued. In a rising rate environment as in 2022, these cash contributions are invested at higher yields which is beneficial to the fund.

Table 7 - As at December 31, 2022 - Duration for the Sinking Fund[1]

(Years)	Fixed Income Duration
Portfolio Duration	12.2
Liability Duration	12.2

[1]From Aon Performance Review (Fixed Income)

Table 8 **- Total Return versus Market Benchmark (%) for the Sinking Fund as at December 31, 2022**

	1 year (Year-over-Year)			3 year (annualized)		
	Short Term Sinking Funds	Long Term Sinking Fund	Total[2] Sinking Fund	Short Term Sinking Funds	Long Term Sinking Fund	Total[2] Sinking Fund
Portfolio Return (%)	2.3%	-16.7%	-13.9%	1.7%	-2.4%	-1.8%
Benchmark Return (%)	1.7%	-14.4%	-12.0%	0.8%	-1.0%	-0.7%
Value Added (%)	0.6%	-2.3%	-1.9%	0.9%	-1.4%	-1.1%

[1]Calculated from RBCIS Performance Analytics and Aon, Performance Review
[2] Weighted by market value of the Short Term and Long Term Funds

When excluding the unrealized market gains and losses, the Sinking Fund portfolio earned 0.9% ($18.9 million) for the year 2022 on a book income basis as shown in Table 9 below. The asset mix attribution of the book income is listed on Table 10 below. These funds will be used to pay the City's long-term debt obligations at maturity and the shorter term performance volatility should not affect the longer term purpose of these funds. Sinking Fund contributions made in 2022 and in early 2023 will be invested in fixed income securities at higher yields than the assumed required rate of return of the fund.

Table 9 - Sinking Fund Book Return as at December 31, 2022

Portfolio	Average Weighted Capital Balance (Book Value)	Book Income	Book Return on Capital (Annualized)
Sinking Fund	$2,084.0	$18.9	0.9%

Table 10 - Book Income Attribution for Sinking Fund - 2022 ($millions)

Sinking Fund Earned Income by Asset Class as at December 31, 2022 ($ millions)	
Fixed Income	8.8
Global Equities	3.0
Short Term Investments	7.1
Total Earned Income	**18.9**

The investment portfolios have progressively phased into greater use of the broader range of investments that become available. Although the overall portfolio risk has been reduced through asset mix diversification, the potential for volatility in total return over the short-term investment horizon still exist while the risk-adjusted total return over the long-term investment horizon are expected to be higher and sufficient to meet the debt repayments.

There were no debt maturities in 2022. The next maturity will be in September 2023 for $300 million.

Record of Transactions in City of Toronto Debentures

To comply with Ontario Regulation 610/06 Financial Activities of the City of Toronto Act, 2006, the City maintains a record of each transaction in its own securities, including a statement of the date and the purchase or sale price of each security transaction. A listing of these transactions are found in Attachment 3.

Compliance with the Investment Policy Guidelines

All the City's funds were within the Asset Mix requirements set out in the Council-approved Investment Policy for the year 2022. The breakdown of each portfolio is shown in Attachment 4.

There were no exceptions to report for the year 2022.

The City's auditors, KPMG LLP, will perform the annual investment policy compliance audit procedures for 2022 during the second half of 2023.

The Investment Policy has been reviewed by staff and there is currently no recommended changes.

Reporting on Environmental, Social, and Governance (ESG) Performance

When reviewing the update to the Investment Policy in June 2020, City Council had requested the Chief Financial Officer and Treasurer, and the Toronto Investment Board to consider and incorporate internationally-recognized best practices for Environmental, Social and Governance.

The Toronto Investment Board has recently contracted a third-party data provider in order to monitor and report on the high-level Environmental, Social, and Governance (ESG) attributes of the City's investment portfolio. This investment fund-level ESG reporting process will complement the existing corporate-level ESG performance report.

A report to City Council will be included in the next semi-annual performance report expected in November/December 2023.

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SIGNATURE

Heather Taylor
Chief Financial Officer and Treasurer

ATTACHMENTS

Attachment 1 - City of Toronto Statement of Investment Policy and Procedures
Attachment 2 - Background on the Funds
Attachment 3 - Record of Transactions in City of Toronto Debentures
Attachment 4 - Breakdown of the Portfolios by Sectors and by Credit Ratings
Attachment 5 - Historical Allocation of Gross Investment Earnings