CAPITAL MARKET & INVESTMENT ACTIVITIES DURING 2012 AND THE OUTLOOK FOR 2013

Capital Market Activity

During 2012, the City issued in the public capital market $600 million of the $900 million that was approved for the year, consisting of $300 million 30-year debentures and $300 million 10-year debentures.

For 2013, a debt issuance of $900 million was again approved by Council but due to the new non-debt funding strategy, only $600 million in debt is likely to be issued.

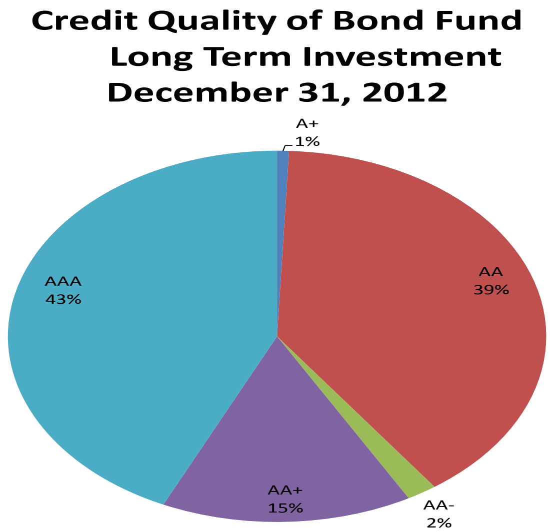
Increasing the term-to-maturity of the City debt issuance to match the economic life of the City's infrastructure assets and providing liquidity to investors through larger bond issues are very important features of the City's 2013 debt issuance program which has been structured to issue debt with 10 and 30 year terms as well as the ability to reopen bond issues, depending upon capital market conditions.

The City continues to monitor the domestic and international capital markets as well as evaluating alternative financing vehicles to identify opportunities to achieve the lowest cost of capital funds during 2013.

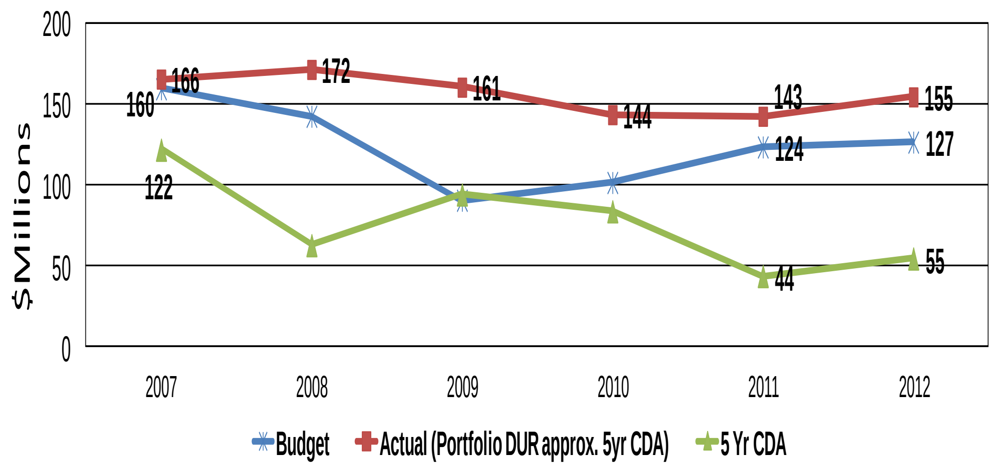
Investment Activity

The City owns and manages the General Group of Funds and the Sinking Fund, each having specific goals and objectives. The General Group of Funds is composed of two individual portfolios (the Bond and Money Market Funds) that are managed interactively. The Bond Fund is positioned towards funding the City's future reserve and reserve fund requirements and therefore takes a longer view of the market. The Money Market portfolio is primarily focused on ensuring that adequate liquidity is maintained to meet the immediate cash flow requirements of the City's daily operations. The Sinking Fund is for the use of retiring the City's debt as it becomes due and payable. The City also manages other smaller funds where the assets are not owned by the City (e.g. Trust Funds).

The City's bond portfolio continues to exhibit high credit quality and liquidity, especially during these extended periods of economic turbulence and market turmoil. The City does not hold any bonds with less than an "A" credit rating (see pie chart below).



In 2012, investment earnings on the City's General Group of Funds totalled $155 million. While Interest rates plummeted to historic lows in 2012, the City was still able to achieve investment earnings that exceeded budget (see chart below).



A 3.75% annual rate of return on capital was achieved in 2012 for the General Group of Funds (see table below)

Fund Type	Average Capital	Income	Return on Capital
Bond Fund	2,293,351,256	133,398,758	5.82%
Money Market Fund	1,835,309,813	21,674,741	1.18%
General Group of Funds	4,128,661,069	155,073,499	3.75%

Events in the Eurozone were again the major risk aversion event that influenced markets in Canada, the U.S., and globally in 2012. Yields from Bank of Canada bonds have remained unusually low due to safe-haven demand resulting from the situation in the Eurozone and from aggressive US Federal Reserve intervention. Looking forward into 2013, the global economy should continue to struggle through a transition period with risks continuing to feed from the Eurozone, fiscal austerity in the US and a slowing Chinese economic growth.

While core inflation remains well contained, the Bank of Canada is unlikely to raise the overnight interest rate until Q4/13 if not even later in 2014. Interest Rates (excl overnight rates) are expected to remain low but slowly increase over 2013 with the yield curve staying flat, in anticipation of economic recovery and Bank of Canada rate action. Bond yields are expected to remain low and could take at least a couple years before rising gradually to the more neutral 3.5% level in the 10-year yields (which were currently around 1.85% in the beginning of 2013). While maintaining safety of principle and sufficient liquidity, the City's investment strategy for 2013 is to add duration to its neutral position (extend term to enhance yield and to align with reserve fund balance forecasts) gradually if and as yields move higher.