



Halifax Regional Council
May 28, 2002

TO: Mayor Kelly and Members of Halifax Regional Council

SUBMITTED BY: *S. Dale MacLennan*
S. Dale MacLennan, CA, Director of Financial Services

DATE: May 21, 2002

SUBJECT: Investment Activities - Quarter Ending March 31, 2002

INFORMATION REPORT

ORIGIN

Quarterly report of investment performance and adherence to Investment Policy as required by Investment Policy adopted by Council.

BACKGROUND

The amended Investment Policy was adopted at the April 23, 2002 meeting of Regional Council. The Investment Policy has been forwarded to the Minister, Service Nova Scotia and Municipal Relations for approval as per the Municipal Government Act. The Investment Policy calls for quarterly reporting by the Treasurer to Regional Council and the Investment Policy Advisory Committee. A report has been submitted to the Investment Policy Advisory Committee

DISCUSSION

Staff have been investing by balancing the Objectives of the Investment Policy as well as the constraints of Section 100(1) of the Municipal Government Act which requires the following with respect to Municipal funds (that they be):

- “(a) deposited in an interest bearing account at a bank doing business in the Province;
- (b) invested pursuant to an investment policy adopted by the Council and approved by the Minister; or
- (c) invested in investments in which a trustee is permitted to invest pursuant to the Trustee Act.”

The Investment Policy requires a report to Council on investment performance and compliance with the Policy.

Economic and Investment Climate

Investment markets have been challenged with high profile bankruptcies such as Kmart and Enron as well as accounting and auditing concerns embodied in the Anderson situation. Credit rating downgrades outpaced upgrades by a 4 to 1 margin in Canada in 2001 as reported by the Dominion Bond Rating Service. The events of September 11 also demonstrated how vulnerable economies and investment markets can be in the short run. Central Bankers in Canada and the United States responded to weakening economies and the September 11 terrorist attacks by slashing interest rates to levels not seen in a generation.

Signs of growth are returning to the Canadian and United States economies after what has been termed a “Recessionette” due to the brevity and lack of severity. In Canada, year over year inflation as measured by the CPI increased to 1.5% in February from 1.3% and 0.7% respectively

in January and December. The Unemployment Rate fell 0.2% to 7.7% in March. The Quarter ending March 31 saw the largest gain in employment since 1987. Gross Domestic Product rose 0.6% in January over December.

Consumers have responded to lower interest rates by spending. This appears to be responsible for returning the North American economies to a growth path. However, whether business investment will pick up to perpetuate economic growth remains to be seen. There is no doubt that the reductions in interest rates since the beginning of 2001 have created a tremendous amount of liquidity. As indicated on the attached graph of Canadian Commercial Bank Prime Rates there is a lot of room for the Bank of Canada to raise rates should the economy continue to grow.

The United States Federal Reserve moved from an easing to a neutral bias at their March 19 meeting. The Bank of Canada lowered rates by 1/4% January 15, held rates steady at the March 5 meeting and raised rates by 1/4% at the April 16 meeting. The Bank believes a robust recovery is now underway in Canada although they also feel some risks remain. They are beginning the process of “reducing the substantial amount of stimulus in place in a timely and measured manner”.

The short term investment markets began pricing in a Bank of Canada rate increase with remarks by the Bank Governor around the middle of March. However, as the April 16 rate setting date approached the markets began to discount the possibility. It was reported on the morning of April 16 that a survey of 12 out of 18 Bloomberg economists believed that there would not be a rate increase. Notwithstanding, staff continued to invest believing that the rates offered by the market were fair compensation for the risk of future rate increases by the Bank of Canada.

In the short run it will be interesting to see if the move by the Bank of Canada ahead of the U.S. Federal Reserve will reduce the impact of economic developments in the U.S. on Canadian market interest rates. To the degree that this rate increase may have been motivated by concern over the level of the Canadian dollar adds an additional level of complexity over and above the publicly stated goal of beginning to reduce the level of monetary stimulus in the economy. Attempting to predict future actions by the Bank of Canada will be more difficult.

Investment Activities

In light of the above economic and financial market concerns the strategy emphasis has been on quality and liquidity as evidenced by the graphs attached. External investments were limited to Government of Canada instruments. This was in keeping with previous discussions with the Investment Policy Advisory Committee at the December meeting.

As the interest rate environment in the Quarter changed from declining to steady and rising, the investment strategy also changed from locking in returns as rates fell to placing investments that would offer a reasonable reward for the term of the investment given the anticipated pace of future interest rate increases. Maturities were kept to under one year. The quality and liquidity of these investments will provide a solid core around which portfolios can be built in the future as the economy improves and the Investment Policy is more fully implemented.

Addressing the specific Investment Policy Objectives, preservation of capital was the foremost consideration. Government of Canada instruments carry virtually no risk of default. Liquidity risk was minimal given the marketability of Government of Canada instruments and with the term of the investments under one year. Some interest rate risk was taken on with the term of the investments. This was felt to be reasonable given the prevailing views on the future of interest rates as well as the ability to earn a greater return over the interest bearing Royal Bank deposit account. Diversification of the investment portfolio was not actively pursued during the Quarter. The Enron and Anderson debacles will delay any movement into corporate instruments in the near term.

Investments with a term of beyond one year were not actively considered in the Quarter. This was partly due to the relatively low level of these rates compared to recent years and partly because reliable longer term forecasts of cash requirements are still under development.

Cash flow models were developed during the quarter which will facilitate the matching of specific investments to specific cash requirements. Emphasis was on the requirements of the Operating Fund. Investments made to date will be replaced by long term investments as cash requirements of the Reserve Funds are better known and as longer term rates improve. Refinement of these cash flow models will be ongoing.

The rate of return on the total Short Term Investment Portfolio at March 31 was 2.31% compared to the three month Government of Canada Treasury Bill yield of 2.21% . This includes the portion in the interest bearing Royal Bank account which provided a yield of 2.00% at March 31 as well as a weighted average rate of return 2.42% from the Government of Canada investments. A summary of these of investments is attached as Appendix A.

Outlook

In the upcoming quarter, the first of the new fiscal year, staff plan to expand the investment choices under active consideration to include Banker's Acceptances of R-1 Middle rated Schedule A Canadian banks as well as Canadian dollar instruments of other government issuers. Expanding investment choices will facilitate the matching of investment maturities to cash requirements. This

will be balanced against the prospect for future rate increases by the Bank of Canada as well as the very real risk that the economic recovery in North America could stall, particularly if short term rates are raised too soon or too quickly.

BUDGET IMPLICATIONS

N/A

FINANCIAL MANAGEMENT POLICIES / BUSINESS PLAN

This report complies with the Municipality's Multi-Year Financial Strategy, the approved Operating, Capital and Reserve budgets, policies and procedures regarding withdrawals from the utilization of Capital and Operating reserves, as well as any relevant legislation.

ALTERNATIVES

N/A

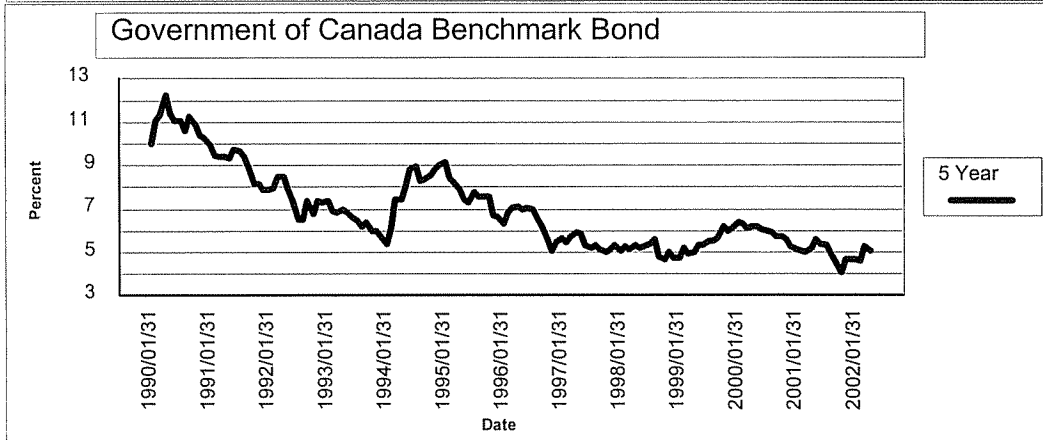
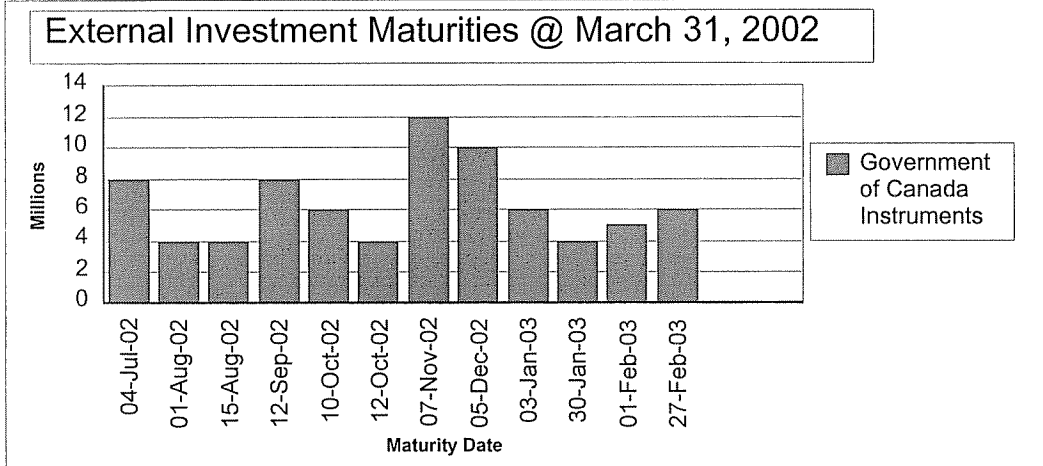
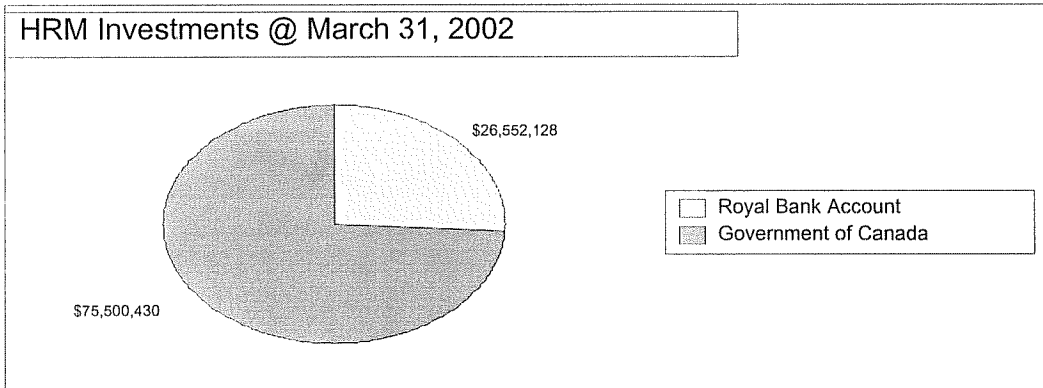
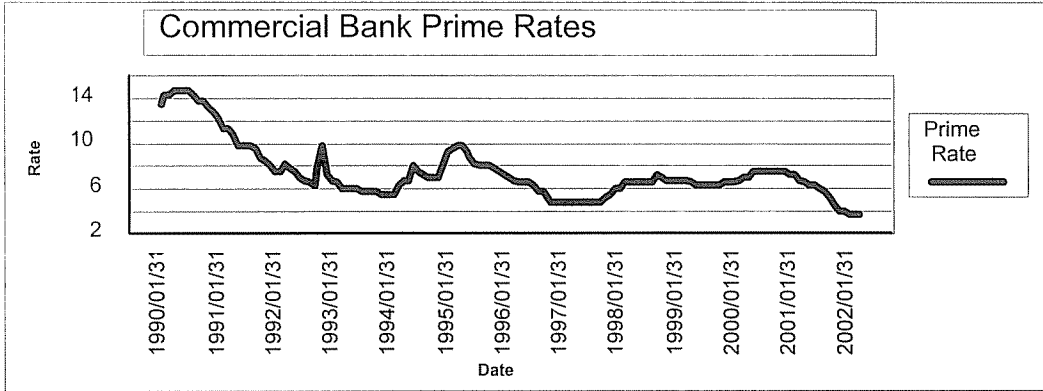
ATTACHMENTS

1. Graphs of Commercial Bank Prime Rates, HRM Investments at March 31, 2002 and Government of Canada 5 Year Bond Yields.
2. Appendix A Schedule of investments held at March 31, 2002.

Additional copies of this report, and information on its status, can be obtained by contacting the Office of the Municipal Clerk at 490-4210, or Fax 490-4208.

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Report Approved by: Reg Ridgley, CGA, Manager, Strategic Project Support



Halifax Regional Municipality

Appendix A

Summary of Investment @ March 31, 2002

<u>Date of Purchase</u>	<u>Issuer</u>	<u>Instrument</u>	<u>Price</u>	<u>Yield</u>	<u>Cost</u>	<u>Maturity Date</u>	<u>Maturity Amount</u>	<u>DBRS Rating</u>
12-Oct-01	Government of Cananda	Treasury Bills	97.178	2.92%	\$3,887,120	12-Oct-02	\$4,000,000	R-1 High
26-Oct-01	Government of Cananda	Treasury Bills	97.908	2.43%	\$3,916,320	12-Sep-02	\$4,000,000	R-1 High
16-Nov-01	Government of Cananda	Treasury Bills	97.601	2.52%	\$3,904,040	07-Nov-02	\$4,000,000	R-1 High
20-Nov-01	Government of Cananda	Treasury Bills	97.701	2.44%	\$3,908,040	07-Nov-02	\$4,000,000	R-1 High
22-Nov-01	Government of Cananda	Treasury Bills	97.595	2.57%	\$3,903,800	07-Nov-02	\$4,000,000	R-1 High
17-Dec-01	Government of Cananda	Treasury Bills	97.704	2.43%	\$4,885,200	05-Dec-02	\$5,000,000	R-1 High
18-Dec-01	Government of Cananda	Treasury Bills	97.793	2.34%	\$4,889,650	05-Dec-02	\$5,000,000	R-1 High
18-Jan-02	Government of Cananda	Bond Residual	97.624	2.35%	\$4,881,200	01-Feb-03	\$5,000,000	AAA
22-Jan-02	Government of Cananda	Treasury Bills	99.102	2.03%	\$3,964,080	04-Jul-02	\$4,000,000	R-1 High
22-Jan-02	Government of Cananda	Treasury Bills	97.479	2.16%	\$3,939,160	10-Oct-02	\$4,000,000	R-1 High
28-Jan-02	Government of Cananda	Treasury Bills	99.105	2.10%	\$3,964,200	04-Jul-02	\$4,000,000	R-1 High
11-Feb-02	Government of Cananda	Treasury Bills	99.007	2.14%	\$1,980,140	01-Aug-02	\$2,000,000	R-1 High
11-Feb-02	Government of Cananda	Treasury Bills	97.676	2.46%	\$1,953,520	30-Jan-03	\$2,000,000	R-1 High
13-Feb-02	Government of Cananda	Treasury Bills	98.996	2.19%	\$1,979,920	01-Aug-02	\$2,000,000	R-1 High
13-Feb-02	Government of Cananda	Treasury Bills	97.607	2.55%	\$1,952,140	30-Jan-03	\$2,000,000	R-1 High
14-Feb-02	Government of Cananda	Treasury Bills	97.836	2.50%	\$1,956,720	03-Jan-03	\$2,000,000	R-1 High
14-Feb-02	Government of Cananda	Treasury Bills	98.915	2.20%	\$1,978,300	15-Aug-02	\$2,000,000	R-1 High
21-Feb-02	Government of Cananda	Treasury Bills	97.915	2.46%	\$1,958,300	03-Jan-03	\$2,000,000	R-1 High
21-Feb-02	Government of Cananda	Treasury Bills	98.97	2.17%	\$1,979,400	15-Aug-02	\$2,000,000	R-1 High
26-Feb-02	Government of Cananda	Treasury Bills	98.596	2.30%	\$1,971,920	10-Oct-02	\$2,000,000	R-1 High
26-Feb-02	Government of Cananda	Treasury Bills	97.922	2.49%	\$1,958,440	03-Jan-03	\$2,000,000	R-1 High
26-Feb-02	Government of Cananda	Treasury Bills	97.461	2.62%	\$1,949,220	27-Feb-03	\$2,000,000	R-1 High
01-Mar-02	Government of Cananda	Treasury Bills	97.418	2.71%	\$1,948,360	27-Feb-03	\$2,000,000	R-1 High
07-Mar-02	Government of Cananda	Treasury Bills	98.779	2.40%	\$1,975,580	12-Sep-02	\$2,000,000	R-1 High
08-Mar-02	Government of Cananda	Treasury Bills	96.982	3.36%	\$1,939,640	27-Feb-03	\$2,000,000	R-1 High
26-Mar-02	Government of Cananda	Treasury Bills	98.801	2.62%	\$1,976,020	12-Sep-02	\$2,000,000	R-1 High
27-Mar-02	Government of Cananda	Treasury Bills						
Total Short Term Investments							\$77,000,000	
Interest Bearing Royal Bank Account							\$26,552,128	
Grand Total							\$103,552,128	