

To: ONE Joint Investment Board
From: Keith Taylor, Chief Investment Officer, ONE Investment
Date: July 14, 2021
Re: City of Kenora – Annual Investment Plan Review
Report: ONE JIB-003-21

1. RECOMMENDATIONS

It is recommended that the Board:

1. Approve the City of Kenora's Investment Plan (Attachment 1).

2. SUMMARY

The City of Kenora's annual Investment Policy Statement review resulted in changes intended to closely align it with the ONE JIB Outcomes Framework. The City has \$41.8 million available to invest, \$23.5 million of which is part of the Citizens' Prosperity Trust Fund – a perpetual Fund intended to provide a recurring income stream while preserving the principal. Kenora's General Account and the projected reserve balances have a high degree of timing uncertainty due to impending decisions related to their infrastructure financing strategy (i.e., grant availability and debt options). The City will be executing a series of transactions that will result in a small net contribution to MNRI of approximately \$156,000 this year plus some income from pledged securities. Their updated Municipal Client Questionnaire shows that new MNRI will be mapped to the existing Outcomes in the plan and that no other changes are required to the Outcome mapping.

The average annual expected return in the proposed Investment Plan is 3.9%, which is 0.2% lower than the June 2020 Investment Plan. The difference is primarily attributable to lower return assumptions on the fixed income Pooled Funds that ONE JIB approved in February 2021.

3. BACKGROUND

Kenora's Annual Investment Policy Statement review resulted in changes that more closely align it with the ONE JIB Outcomes Framework

Kenora completed its Annual Investment Policy Statement review on April 20, 2021. Council is required to review and, if necessary, update the Policy annually as per Ontario Regulation 438/97 (the Regulation). Council amended its Investment Policy Statement so that it more closely aligns with the ONE JIB Outcomes Framework. The objectives, risk tolerance and investment horizons now mirror those in the Framework.

Kenora's investment objective is long-term growth and returns in excess of inflation

The Regulation requires municipalities to consider the following matters under the prudent investor regime:

- Preservation of capital
- Adequate liquidity that takes into account the needs of financial obligations and reasonably anticipated budgetary requirements
- Diversification by asset class, market, sector, issuer, credit quality and term to maturity
- Income and capital appreciation
- Macro risks, such as inflation, economic growth and interest rates.

Kenora's Investment Policy Statement verifies that the City has taken these considerations into account in setting its investment objectives. The City's overall investment objective is moderate growth at moderate levels of risk. The Citizens' Prosperity Trust Fund is perpetual in nature and the City is primarily concerned about preservation of capital and the ability to generate returns that can be used as revenue in the municipal budget. The General Account can assume a higher risk profile, which may achieve higher returns that are expected to exceed inflation.

Kenora's risk tolerance and investment horizon are defined by category and purpose of reserve and reserve fund, and they are aligned with the ONE JIB Outcome Framework

ONE JIB uses an Outcomes Framework to translate municipal needs and goals into investment allocations.

Table 1 below shows details of the ONE JIB approved Outcomes Framework, which classifies investments into four Outcome categories: Cash, Stable Return, Contingency, and Target Date Outcomes. The Outcomes are in alignment with Kenora's investment objectives, risk profile and time frames. Kenora's Investment Plan assigns investment allocations based on the Outcome mapping in Table 1.

Table 1: ONE JIB Outcomes Framework

Outcome Category	Outcome Strategy	Objective	Risk Tolerance, Liquidity	Investment Horizon
Cash	Cash	Preservation of capital	Low risk; high liquidity	< 3 years
Stable Return	Stable Return	Income generation: To generate returns to fund recurring needs	Moderate risk with emphasis on growth and stable returns, regular liquidity	> 5 years (Perpetual)
Contingency	Contingency	Contributions for unexpected and infrequent events	Higher risk, emphasis on longer-term capital growth with some liquidity	> 5 years (Perpetual)
	Asset mgt reserves	Contributions to generate returns to fund asset management reserves	Higher risk, emphasis on longer-term capital growth; low liquidity	> 10 years (Perpetual)
Target Date	Target Date 3-5 yrs	Preservation of capital	Low risk; high liquidity	3 - 5 years
	Target Date 5-10 yrs	Contributions toward capital projects, mitigate inflation impacts and meet target funding requirements	Moderate risk, liquid	5 - 10 years
	Target Date 10+ yrs	Contributions toward capital projects, mitigate inflation impacts and meet target funding requirements	Higher risk, emphasis on long term inflation-adjusted growth	> 10 years

Kenora's total MNRI is \$46.8 million, of which ONE JIB controls and manages \$41.8 million

Kenora has approximately \$41.8 million available for the ONE JIB to invest, excluding \$5.0 million in pledged or in-kind securities. This amount represents the approximate market value of current investments with ONE JIB plus a net contribution of approximately \$156,000. The City will be making a series of transactions that will see a contribution to the Citizens' Prosperity Trust Fund, a transfer from the Citizens' Prosperity Trust Fund to its General Account, and a withdrawal from its General Account.

As noted in last year's Investment Plan, the City groups its MNRI into two high-level categories: (1) General Account and (2) the Citizens' Prosperity Trust Fund. The Citizens' Prosperity Trust Fund is a legacy fund that was established with the proceeds from the sale of a telecom utility. The City targets 3% annual income to be generated by the Citizens' Prosperity Trust Fund. The City will often self-finance capital projects (i.e., borrow from its own reserves), paying itself annual interest of 3%. The portion of the Citizens' Prosperity Trust Fund classified as MNRI for ONE JIB is just a portion of the total value of the legacy fund. As the City repays its internal borrowing, that money may be reclassified as MNRI. Kenora is making a debt repayment this year and \$1.56 million will be added to the Citizens' Prosperity Trust Fund. The City will also be reallocating just over \$1.4 million from its Citizens' Prosperity Trust Fund to its General Account. Finally, Kenora will be withdrawing approximately \$1.4 million from its General Account for a planned water treatment project. Table 2 summarizes these transactions.

The City also has approximately \$5.0 million in pledged securities held by ONE Investment's Custodian. The income generated from those securities is to be added to the Stable Return Outcome along with the other Citizens' Prosperity Trust Fund funds.

Table 2: Summary of Anticipated MNRI Transactions

MNRI Summary & Transactions 2021			
Based on Market Value of Investments	CPTF	General	Total
Market Value May 31, 2021	23,372,533.55	18,197,945.28	41,570,478.83
<i>Planned Transactions by Kenora</i>			
Misallocation: on original transfer	(1,440,374.54)	1,440,374.54	-
income to Dec/20	(34,455.29)	34,455.29	-
income to Mar/21	(10,689.57)	10,689.57	-
2020 debt payments	1,556,326.93		1,556,326.93
Release of WTP reserve fund to operations		(1,400,038.69)	(1,400,038.69)
Residual Cash - In Kind bond Portfolio	73,616.81		
Sub Total - In ONE Pooled Funds	23,516,957.89	18,283,425.99	41,800,383.88

The City's MNRI is divided between the Citizens' Prosperity Trust Fund and its General Account, the latter of which can be further subdivided into contingency reserves and target date reserves

Kenora's MNRI can be divided into two major categories: (1) General Account and (2) the Citizens' Prosperity Trust Fund. The General Account can be categorized into the following types:

1. Capital reserves, which are used to fund capital infrastructure.
2. Stabilization reserves, which are a type of contingency reserve that is used to smooth out somewhat predictable annual volatility (e.g., winter maintenance costs, municipal election costs).
3. Contingency reserves, which are intended to manage potential cost shocks (e.g., emergency management, legal expenses).

The Citizens' Prosperity Trust Fund is a perpetual trust or legacy fund that is intended to provide an annual income of approximately 3% of its principal.

Table 3 below, adapted from the Municipal Client Questionnaire, shows the breakdown in dollar values by reserve type, category, and investment horizon. The stabilization reserves and contingency reserves mostly have expected investment horizons greater than five years, with a 3-year horizon for \$1.0 million of the contingency reserves. The capital reserve MNRI has more distinct timeframes with approximately \$3.0 million required in the 3-to-5-year range and \$6.0 million in the 5-to-10-year range. The City has noted that the capital reserve estimates use conservative assumptions due to uncertainty around availability of government grants and the infrastructure financing strategy. The Citizens' Prosperity Trust Fund figure noted in the table below includes \$5.0 million in pledged securities held by ONE Investment's custodian.

Table 3: MNRI by Type, Category and Time Horizon, from MCQ section 4.2 (rounded to \$ thousands)

				Investment Horizon of MNRI			
Reserve Type	Category	Comments	MNRI Amount	24 months to 3 years	3-5 years	5-10 years	10+ years
General Account							
Capital Reserves	Target Date	Volatile balances	9,283	-	3,042	6,042	200
Stabilization Reserves	Contingency Reserves	Stable balances	5,000	-	-	2,500	2,500
Contingency Reserves	Contingency Reserves	Modest growth expected	4,000	1,000	-	3,000	-
General Account Total			18,283				
Citizen's Prosperity Trust Fund (Citizens' Prosperity Trust Fund)							
Perpetual Trust	Citizens' Prosperity Trust Fund	Income generation	28,538				28,538
TOTAL MNRI			46,821				

Potential changes to Kenora's infrastructure financing strategy leave a high degree of uncertainty with respect to future contributions and withdrawals

As noted in a previous section, Kenora often relies on the Citizens' Prosperity Trust Fund to self-finance projects at a rate of 3%. However, the current low interest rate environment has the City considering debt options available through Infrastructure Ontario. If the City ultimately decides in favour of using external debt, the exact details will have an impact on the City's capital reserve forecasts. Additionally, the City is considering the cost/benefit of borrowing at a low rate to repay their internal loans. If the City chooses this option, much of that debt could be classified as MNRI and allocated to the portion of the Citizens' Prosperity Trust Fund under the control of ONE JIB. Additionally, one of the City's near-term projects (the majority of its 3-to-5-year allocation), a significant harbourfront redevelopment, is contingent on sizable contributions from senior levels of government that have not yet been secured. As a result of these two factors, the City has opted to provide further clarification on expected movements of MNRI after infrastructure financing decisions are made later this year.

Kenora has indicated separate risk tolerances in its Municipal Client Questionnaire for its General Account and the Citizens' Prosperity Trust Fund

Kenora has indicated that preservation of capital is a priority for the Citizens' Prosperity Trust Fund portion of its MNRI and is willing to accept lower returns as a result. The City is

comfortable with a conservative approach that has only a very small chance of capital loss over a 5-year period. Its tolerance for a single year loss is in the range of less than 5%. In speaking with the Treasurer, it was clarified that the tolerance for a single year loss applies to their initial capital investment, meaning that the City could accept greater risk with growth in the Citizens' Prosperity Trust Fund.

The City has a different risk profile for the General Fund, where the objective is moderate growth without excessive risk to capital and a moderate chance of capital loss over a 5-year period. The City would be comfortable with a single year decline in the 5-10% range.

4. ANALYSIS

The ONE JIB Outcomes Framework was used to allocate MNRI in a manner consistent with Kenora's Investment Policy Statement

Using the ONE JIB Outcome Framework, the Chief Investment Officer developed a proposed investment plan for ONE JIB's review and approval. The allocations in the proposed plan reflect the objectives, investment horizon and risk tolerance of the City. The characteristics of the City's reserves or other balances were considered when building the Investment Plan.

The proposed mapping of MNRI to Outcomes and resulting asset allocation are consistent with the time horizon and level of certainty in the City's cash flow forecasts

The City has considerable uncertainty about the timing of its capital reserve cash flows, largely due to upcoming strategic decisions with respect to debt financing. The potential harbourfront redevelopment project requires a target date allocation in the 3-to-5-year range. The City's stabilization and contingency MNRI are allocated to the Contingency Outcome. The capital reserves allocated to a horizon greater than 5 years have a higher degree of uncertainty than typical target date funds. The upcoming decisions with respect to debt financing could potentially push those target date funds to a later time period. As a result, the MNRI is taking on characteristics that are much more like contingency reserves – a time horizon greater than 5 years with a considerable degree of uncertainty. Instead of pushing these funds to a later target date, the funds have been mapped to the Contingency Outcome as the risk level is more aligned with the characteristics of the money.

The entirety of the Citizens' Prosperity Trust Fund is allocated to the Stable Return Outcome, as the Outcome was designed specifically for these types of reserves. Consistent with the information provided by the City, the MNRI is divided between the Stable Return Outcome (56.3%), the Contingency Outcome (36.1%) and the Target Date 3-to-5 years Outcome (7.6%). Using the ONE JIB Outcomes Framework, asset allocations (Table 4 below) and fund allocations (Table 5 below) are determined. The allocations show no significant changes from last year's Investment Plan.

Table 4: Proposed Asset Allocation

Outcome	Total Invested (\$ millions)	Portfolio Weight (%)	HISA (%)	Fixed Income (%)	Equities (%)	Total (%)
Stable Return	23.5	56.3	10	60	30	100
Contingency	15.1	36.1	-	40	60	100
Target Date 3-5 Years	3.2	7.6	20	70	10	100
Total	\$ 41.8	100.0				

Table 5: Proposed Pooled Fund Allocations by Outcome (\$ millions)

Outcome	ONE HISA	ONE Canadian Equity Fund	ONE Global Equity Fund	ONE Canadian Govt Bond Fund	ONE Canadian Corporate Bond Fund	ONE Global Bond Fund	Total
Stable Return	2.4	2.1	4.9	2.1	2.1	9.9	23.5
Contingency	-	2.7	6.3	0.9	0.9	4.2	15.1
Target Date 3-5 Years	0.6	0.1	0.2	0.3	0.3	1.6	3.2
Total \$	\$ 3.0	\$ 4.9	\$ 11.5	\$ 3.4	\$ 3.4	\$ 15.7	\$ 41.8

Table 6 provides the same information in percentage, showing how the fund holdings are held within each of the Outcomes.

Table 6: Fund Allocations as a Percentage of Total by Outcome

Outcome	ONE HISA	ONE Canadian Equity Fund	ONE Global Equity Fund	ONE Canadian Govt Bond Fund	ONE Canadian Corporate Bond Fund	ONE Global Bond Fund	Total
Stable Return	5.6%	5.1%	11.8%	5.1%	5.1%	23.6%	56.3%
Contingency	0.0%	6.5%	15.2%	2.2%	2.2%	10.1%	36.1%
Target Date 3-5 Years	1.5%	0.2%	0.5%	0.8%	0.8%	3.7%	7.6%
Total	7.2%	11.8%	27.5%	8.0%	8.0%	37.5%	100.0%

There are no proposed changes to the mapping of MNRI to Outcomes in comparison to the June 2020 Investment Plan

None of the changes in Kenora's Investment Policy Statement or its Municipal Client Questionnaire require changes to the City's Outcome mapping. The net change in MNRI discussed above accounts for the overall difference in MNRI and the slight changes to the Target Date 3-5 year and the Stable Return Outcomes when comparing to the May 31, 2021 mapping. The difference between the 2020 Plan mapping and the proposed plan mapping is primarily due to changes in market value at the Outcome level. The details are noted in Table 7 below.

Table 7: Percentage of MNRI by Outcome (2020 Plan vs. Current vs. Proposed)

Outcome	2020 Plan Weight	31-May-21 Weight	Proposed Plan Weight
Stable Return	57.0%	56.2%	56.3%
Contingency	35.2%	36.3%	36.1%
Target Date 3-5 Years	7.8%	7.5%	7.6%
Overall	100.0%	100.0%	100.0%

When compared to the June 2020 Plan most of the changes to the proposed plan can be explained by market value changes

After mapping MNRI to Outcomes, the Framework suggests the portfolio-level Pooled Fund allocations in tables 8a (in dollars) and 8b (percentage). Comparable numbers are provided for the initial June 2020 Plan allocations and actual allocations as of May 31, 2021. The difference between the 2020 Plan figures and the Proposed Plan figures in both tables can be explained by market value change and the contribution of new MNRI. The May Actual figures provide a reference point that incorporates market value change and transactions since the 2020 Plan.

Table 8a: Portfolio-level Allocations between ONE JIB Pooled Funds

Fund	2020 Plan \$ millions	Actual (May) \$ millions	Proposed Plan \$ millions
ONE HISA	\$ 2.8	\$ 2.8	\$ 3.0
ONE Canadian Equity Fund	4.5	5.6	4.9
ONE Global Equity Fund	10.4	11.7	11.5
ONE Canadian Government Bond Fund	3.1	3.2	3.4
ONE Canadian Corporate Bond Fund	3.1	3.1	3.4
ONE Global Bond Fund	14.4	15.1	15.7
Total \$	\$ 38.3	\$ 41.6	\$ 41.8

Table 9b: Portfolio-level Allocation Weights between ONE JIB Pooled Funds

Fund	2020 Plan Weight	Actual (May) Weight	Proposed Plan Weight
ONE HISA	7.3%	6.8%	7.2%
ONE Canadian Equity Fund	11.7%	13.6%	11.8%
ONE Global Equity Fund	27.3%	28.2%	27.5%
ONE Canadian Government Bond Fund	8.1%	7.6%	8.0%
ONE Canadian Corporate Bond Fund	8.1%	7.5%	8.0%
ONE Global Bond Fund	37.6%	36.3%	37.5%
Total \$	100.0%	100.0%	100.0%

Average expected returns on the proposed Investment Plan are 0.2% lower than the June 2020 Investment plan due to revised return assumptions

The average return expectation (i.e., Annual 10-yr Compound Return Assumptions) detailed in the plan is 3.9%. This is 0.2% lower than the return expectation in the June 2020 Investment

Plan. As the Outcome mappings and target weights will remain the largely same, the change is primarily attributable to the revised return assumptions established at the February 17, 2021 ONE JIB meeting, which lowered the return assumptions on some of the fixed income Pooled Funds. The overall equity allocation has risen by 0.3% between plans. The standard deviation of the proposed Investment Plan is unchanged vs the 2020 Investment Plan, implying that the level of investment risk has not changed. The expected risk and return details of the Investment Plan are summarized in table 9 below. Standard deviation remains unchanged from the previous plan.

Table 10: Risk and Return Comparison to Last Year's Plan

Plan version	Average Expected Returns	Standard Deviation
July 2021 Proposed Investment Plan	3.9%	4.9%
June 2020 Investment Plan	4.1%	4.9%
Difference	-0.2%	+0.0%

5. CONCLUSION

Kenora's Council completed its annual Investment Policy Statement review and updated the policy to align more closely with the ONE JIB Outcomes Framework. The proposed Investment Plan is consistent with the City's Investment Policy Statement. The proposed asset mix and investment allocations reflect the City's investment objectives and risk preferences expressed in its Investment Policy Statement and Municipal Client Questionnaire. As a result, the Investment Plan is appropriate for the City's objectives, risk tolerance, time horizons and available MNRI.

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