

# 2020 INVESTMENT COMMITTEE ANNUAL REPORT

Edmonton



# BALANCED. RESPONSIBLE. DIVERSE.

The City of Edmonton has rigorous policies and procedures in place to maximize investment returns at a prudent level of overall risk.

These policies and procedures guide the City's Investment Committee in managing and building upon the City's financial assets to help sustain Edmontonians' quality of life.

Over the past 10 years, these accomplishments have contributed over \$800 million of investment earnings and dividends to the City's budget. If this amount had been related to taxation, property taxes would have increased by 6.4% over that time to make up the difference.

Successful management of the City's investment portfolio — which comprises six funds — is one of the key factors in maintaining Edmonton's financial sustainability.

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# 2020 OVERVIEW

## Edmonton's investments showed resiliency.

### THE YEAR OF VOLATILITY

In March 2020, the World Health Organization declared COVID-19 a global pandemic. The impact resulted in the sharpest drop in global GDP since World War II. Volatility reached extreme levels on the news of this shock, which led to equity markets falling by more than 30% from their highs reached earlier in the year.

In response, governments and central banks announced historic levels of fiscal and monetary stimulus to counter what would otherwise have been a global depression. This, along with the rapid advancement of a number of successful vaccines, calmed investors and, in a stunning reversal, financial markets ended the year in positive territory.

U.S. equities were one of the strongest performers as they returned 18.4% for the year and ended 2020 at an all-time high.

Closer to home, Canadian equities followed a similar pattern, but finished the year up only 5.6%. The Canadian dollar rose 2% versus the U.S. dollar, ending the year at a three-year high, despite the price of oil falling by 21% in 2020.

Global equities increased a respectable 13.8%, while returns were slightly higher when converted back into Canadian dollars.

The Bank of Canada lowered interest rates significantly during the year in response to the pandemic which led Canadian fixed income securities (bonds) to post a surprising 8.7% return for 2020. This followed a 6.9% return achieved in the prior year.

### THE CITY'S INVESTMENTS OUTPERFORMED

All of the City's investment funds matched or outperformed their benchmarks in 2020.

Performance ranged from 0.9% (Money Market Fund) to 11.6% (Ed Tel Endowment Fund), depending on each fund's asset mix.

On a four-year basis, investment returns have remained strong and, from a relative perspective, all the City's funds continued to exceed their policy benchmarks. Over a longer-term, ten-year basis, returns have been even better with all of the funds maintaining their outperformance versus their benchmarks.

Finally, the City's largest fund, the Ed Tel Endowment Fund, paid \$40 million in dividends to the City in 2020 and ended the year at its highest market value since inception.

### KEY PROJECTS

Following the approval by City Council of a revised Investment Policy to include a new real estate asset class to further diversify the investment funds, work began on **implementing the new strategy**. The following work was achieved in 2020:

- the manager search for the new investment strategy was completed,
- as part of the above work, a review of the City's equity structure was undertaken to ensure that once funds were transitioned to real estate, the new structure would continue to provide diversification across markets and investment styles as well as maintain a sufficient level of liquidity going forward, and
- the investment management agreement for the real estate mandate was developed and finalized.

This work will continue in 2021 (See What's Ahead).

The **City's Investment Committee Terms of Reference** was updated to reflect the new Investment Policy C212E recently approved by City Council. The Risk Management Section was also updated to align with that of the Investment Policy.

As part of an ongoing commitment to innovation and improvement, **internal fixed income management** processes are being refined. Further to this, work began to enhance the security selection process, and will continue throughout 2021.



## WHAT'S AHEAD?

Financial markets continued their positive tone as they entered 2021. The prospects of economies renormalizing as well as the extraordinary stimulus that central banks and governments continue to provide are the driving influences in moving markets higher. Looking ahead, these will be important factors in determining future capital market returns.

As many markets are at or close to all-time highs and valuations rise, active management, prudent diversification and keeping to established investment principles will be even more important in managing the volatile investment environment going forward.

In the upcoming year, the Investment Committee will oversee the following key projects:

### **Implementing the recommendation of the asset allocation reviews.**

Now that implementation to the new real estate strategy has begun, the following work will occur in 2021:

- creating a new trust structure at the City's custodian to include the real estate portfolio, and
- transitioning the assets to the new structure

### **Major Cities Investment Regulation.**

The Major Cities Investment Regulation, which outlines the permitted investments for the cities of Edmonton, Calgary and Medicine Hat, was up for renewal in early 2021. However, the regulation was subsequently extended to expire in June 2022. As a result, work will be undertaken with the Government of Alberta to review the regulation and to ensure it continues to meet the City's ongoing investment requirements.

### **Appointment of a new Investment Committee member.**

As per the Terms of Reference, external members can serve only two consecutive three-year terms on the Investment Committee. One new committee member is able to be appointed to the Investment Committee. This ensures continued good governance of the City's financial assets.

### **Implementation of the unlisted infrastructure strategy.**

As part of a multi-year project, the City continues to transition assets to the unlisted infrastructure strategy as suitable investment opportunities arise.

## CAPITAL MARKET PERFORMANCE

The rate of return for each City asset class is compared with the published total return of its corresponding broad-market index. These indices, weighted by the Policy Asset Mix, are used to calculate the performance benchmark for each fund.

The City uses the following indices as points of reference by which the investment performance of each fund is evaluated:

**Cash:** FTSE Canada 91 Day Treasury Bill Index (91 Day T-Bills)

**Short-Term Bonds:** FTSE Canada Short Term Bond Index (FTSE Short-Term)

**Bonds:** FTSE Canada Universe Bond Index (FTSE Universe)

**Canadian Equity:** S&P/TSX Capped 10% Index (TSX)

**Global Equity:** Morgan Stanley Capital International Inc. World Index excluding Canada (MSCI World ex-Canada)

**Emerging Market Equity:** Morgan Stanley Capital International Inc. Emerging Markets Index (MSCI EM)

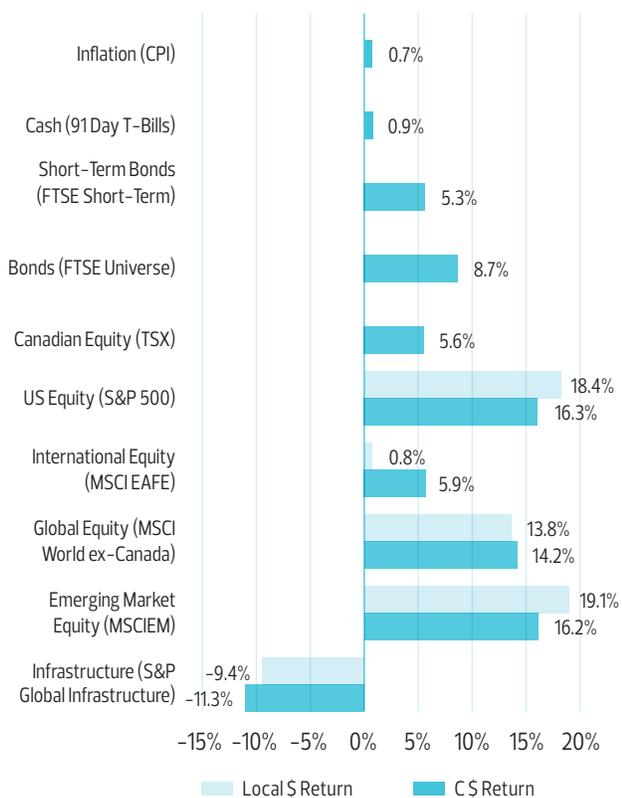
### **Infrastructure:**

Unlisted – Consumer Price Index (CPI) + 4.5%

Listed – Standard & Poor's Global Infrastructure Index (S&P Global Infrastructure)

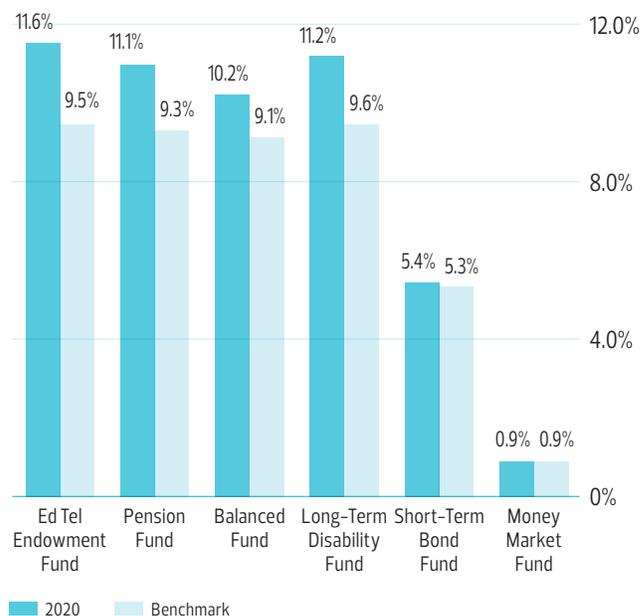
Investment performance returns are presented before management fees are deducted according to industry standards.

### 2020 Capital Market Returns

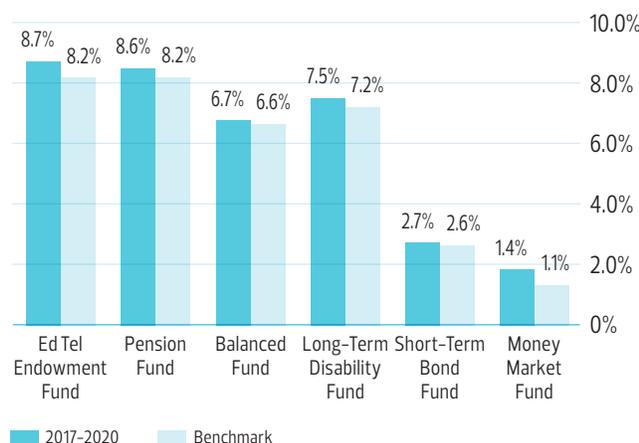


Local \$ Return represents returns expressed in the associated foreign currencies. CS Return reflects the return converted to Canadian dollars.

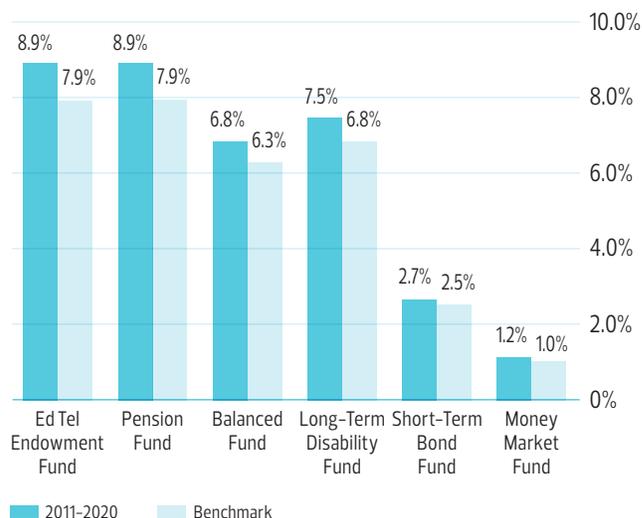
### 2020 Performance vs. Benchmark



### Four-Year Performance vs. Benchmark (2017-2020)



### Ten-Year Performance vs. Benchmark (2011-2020)



# PORTFOLIO PERFORMANCE

## INVESTMENT FUNDS

Ed Tel Endowment Fund | Pension Fund | Long-Term Disability Fund

## RESERVES AND WORKING CAPITAL FUNDS

Money Market Fund | Short-Term Bond Fund | Balanced Fund

Investments within the reserves and working capital funds represent financial holdings of the Corporation held for a specific purpose within the City's budget. The investment earnings from these funds are transferred to the City's capital budget on an annual basis.

## ED TEL ENDOWMENT FUND

### Fund Management

Multiple Investment Managers

### Market Value

\$914 million (Dec. 31, 2020)

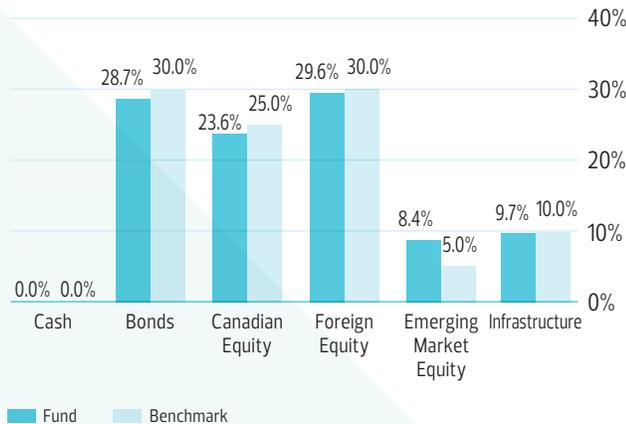
### Performance (rate of return)

Over one year (2020)	+11.6%
Over four years (2017-2020, per annum)	+8.7%
Over ten years (2011-2020, per annum)	+8.9%

### Performance against Policy Benchmark

Over one year (2020)	+2.1%
Over four years (2017-2020, per annum)	+0.5%
Over ten years (2011-2020, per annum)	+1.0%

### Ed Tel Endowment Fund Asset Mix vs. Policy Mix

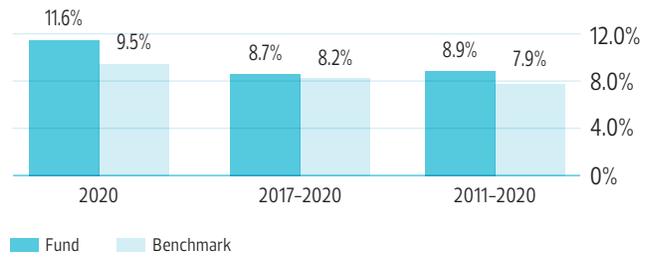


## DESCRIPTION

The objective of an endowment fund is to provide a source of income in perpetuity while ensuring the real purchasing power of the fund is maintained. The Ed Tel Endowment Fund was created in 1995 to hold the financial assets generated by the sale of Edmonton Telephones to TELUS Corporation. It is considered a financial legacy for future generations that delivers a stable, sustainable and growing dividend for the City.

The Ed Tel Endowment Fund paid a dividend of \$40 million in 2020 and ended the year at its highest market value since the fund was established. The total dividend to be paid in 2021 is set at \$41 million.

### Ed Tel Endowment Fund Performance vs. Benchmark



### Ed Tel Endowment Fund Annual Dividend Payments



**SINCE 1995, THE ED TEL ENDOWMENT FUND HAS EARNED A COMPOUND ANNUAL RATE OF RETURN OF 8.4% VERSUS THE BENCHMARK RETURN OF 7.5%, GROWN ITS PRINCIPAL FROM \$465 MILLION TO \$914 MILLION AND PAID \$874 MILLION IN DIVIDENDS TO THE CITY.**

#### **ED TEL ENDOWMENT FUND BYLAW – KEY SUCCESS FEATURES**

**Inflation Indexing:** To ensure real purchasing power is not eroded, the City maintains the “Inflation Adjusted Principal” of the fund.

**Spending Rate:** The fund’s investment policy sets the portion of the fund paid out annually as dividends.

**Smoothing Mechanism:** This dividend calculation formula minimizes the effects of volatile investment returns and provides for a more stable and predictable annual dividend from the fund.



## PENSION FUND

### Fund Management

Multiple Investment Managers

### Market Value

\$299 million (Dec. 31, 2020)

### Performance (rate of return)

Over one year (2020) +11.1%  
 Over four years (2017-2020, per annum) +8.6%  
 Over ten years (2011-2020, per annum) +8.9%

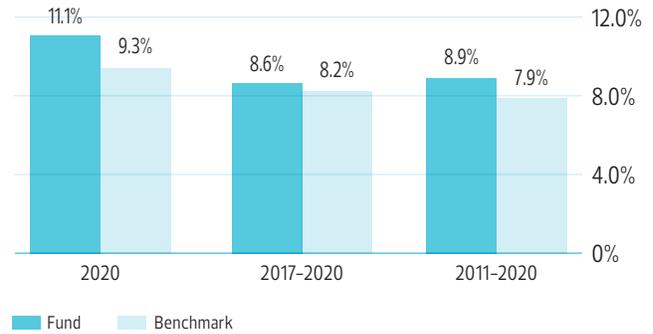
### Performance against Policy Benchmark

Over one year (2020) +1.8%  
 Over four years (2017-2020, per annum) +0.4%  
 Over ten years (2011-2020, per annum) +1.0%

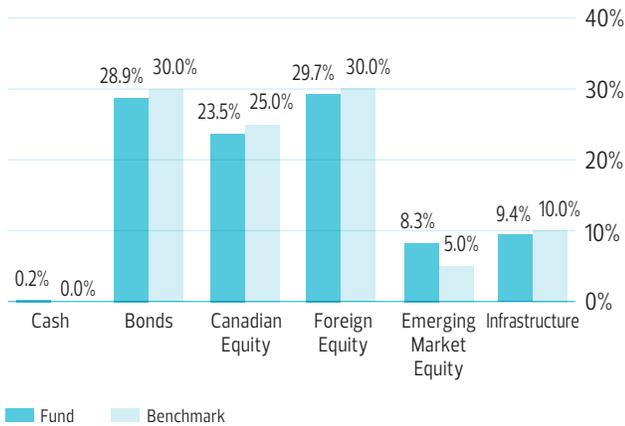
### Description

The Pension Fund consists of the Firefighters' Supplementary Pension Plan, the Fire Chief and Deputy Fire Chiefs' Supplementary Pension Plan and one closed pension plan with a small number of beneficiaries.

Pension Fund Performance vs. Benchmark



Pension Fund Asset Mix vs. Policy Mix



## LONG-TERM DISABILITY FUND

### Fund Management

Multiple Investment Managers

### Market Value

\$162 million (Dec. 31, 2020)

### Performance (rate of return)

Over one year (2020)	+11.2%
Over four years (2017–2020, per annum)	+7.5%
Over ten years (2011–2020, per annum)	+7.5%

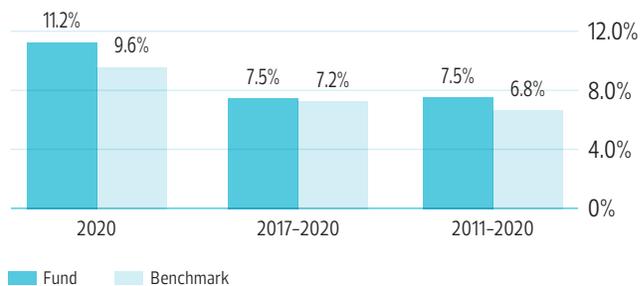
### Performance against Policy Benchmark

Over one year (2020)	+1.6%
Over four years (2017–2020, per annum)	+0.3%
Over ten years (2011–2020, per annum)	+0.7%

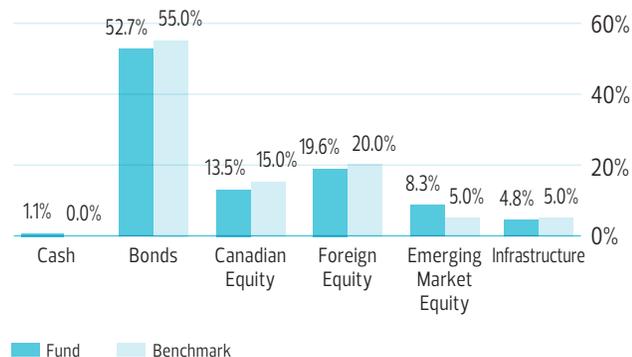
### Description

The Long-Term Disability (LTD) Fund holds investments for six City of Edmonton long-term disability plans.

LTD Fund Performance vs. Benchmark



LTD Fund Asset Mix vs. Policy Mix



## MONEY MARKET FUND

### Fund Management

City of Edmonton Investment Management (internal)

### Market Value

\$523 million (Dec. 31, 2020)

The City's revenue streams are cyclical; the fund value peaks each July at approximately \$1 billion.

### Performance (rate of return)

Over one year (2020)	+0.9%
Over four years (2017-2020, per annum)	+1.4%
Over ten years (2011-2020, per annum)	+1.2%

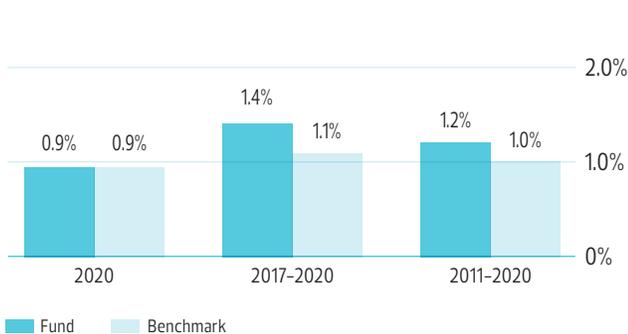
### Performance against Policy Benchmark

Over one year (2020)	+0.0%
Over four years (2017-2020, per annum)	+0.3%
Over ten years (2011-2020, per annum)	+0.2%

### Description

The Money Market Fund absorbs the excess or shortfall in the daily operating requirements of the City. The fund ensures that sufficient cash and liquid assets are available to cover the City's short-term obligations. As such, the fund is solely invested in money market securities with a time horizon of one year or less, depending on the City's forecast of commitments.

Money Market Fund Performance vs. Benchmark



## SHORT-TERM BOND FUND

### Fund Management

City of Edmonton Investment Management (internal)

### Market Value

\$345 million (Dec. 31, 2020)

### Performance (rate of return)

Over one year (2020)	+5.4%
Over four years (2017-2020, per annum)	+2.7%
Over ten years (2011-2020, per annum)	+2.7%

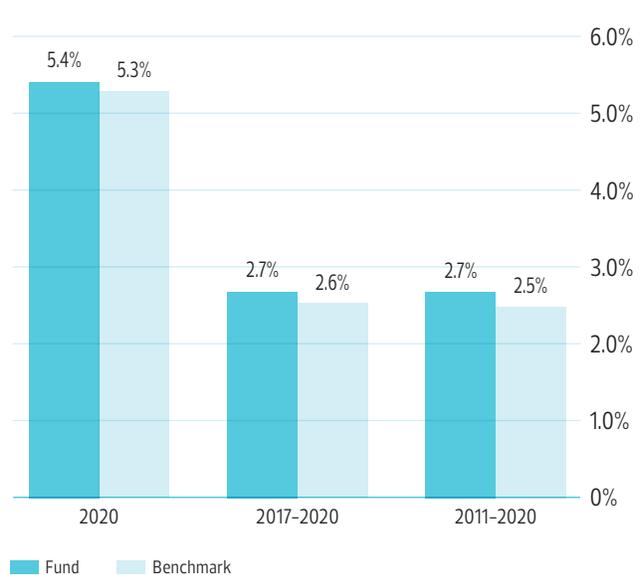
### Performance against Policy Benchmark

Over one year (2020)	+0.1%
Over four years (2017-2020, per annum)	+0.1%
Over ten years (2011-2020, per annum)	+0.2%

### Description

The Short-Term Bond Fund provides an investment vehicle for working capital that is not currently needed to fund City operations but will be needed in less than five years. Therefore, the fund holds fixed income securities with an investment horizon of less than five years.

Short-Term Bond Fund Performance vs. Benchmark



## BALANCED FUND

### Fund Management

Multiple Investment Managers

### Market Value

\$840 million (Dec. 31, 2020)

### Performance (rate of return)

Over one year (2020)	+10.2%
Over four years (2017-2020, per annum)	+6.7%
Over ten years (2011-2020, per annum)	+6.8%

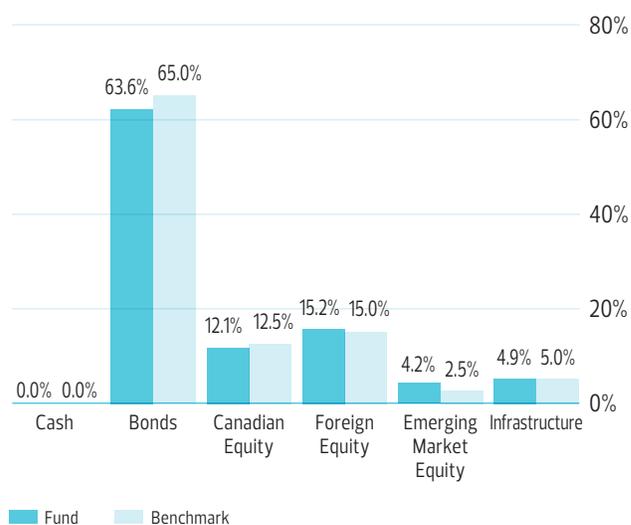
### Performance against Policy Benchmark

Over one year (2020)	+1.1%
Over four years (2017-2020, per annum)	+0.1%
Over ten years (2011-2020, per annum)	+0.5%

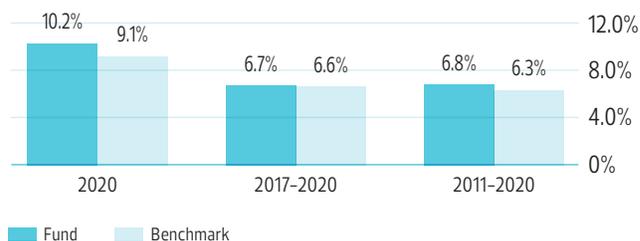
### Description

The Balanced Fund has a time horizon of greater than five years and is a long-term investment vehicle for operating and capital reserve funds, deferred revenue accounts and other similar funds. Because it has a longer-term investment horizon, it has a risk tolerance that permits owning some equities. The fund is reported, and performance is benchmarked against the mid-points of its policy asset mix ranges.

Balanced Fund Asset Mix vs. Policy Mix



Balanced Fund Performance vs. Benchmark



# INVESTMENT PHILOSOPHY

## A prudent approach to investing municipal assets

The investment program plays an important role in Edmonton's Financial Sustainability Plan, which addresses Edmonton's financial sustainability and the development of a long-range financial plan. Strong accountability and oversight matched with diversified expertise have allowed the program to provide considerable added value to the City of Edmonton over time.

Empirical evidence suggests the most important determinant of investment returns and risk is asset mix. As a result, the City establishes an asset allocation policy for each of its investment funds that is consistent with the specific objectives, risk profile and investment time horizon of each fund.

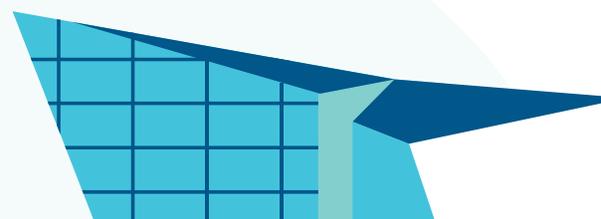
Within the various asset classes, diversification is further enhanced through the split between internal and external investment managers, which results in a multi-asset, multi-manager investment framework.

Expanding the depth of employed strategies and broadening the scope of investment opportunities have been key drivers of the program's successful evolution over time. Different investment styles offer additional risk control, reduce the possibility of investment losses and ensure that fund objectives are met. Comparative advantages, such as liquidity, the ability to invest long term and a cost-effective investment program, allow the City the opportunity to generate a significant

incremental return over time. As an example, the City typically falls within the positive value-added and low-cost category in an annual survey of institutional investment managers around the world.

The guiding principles used to determine the broad investment structure and strategy for the City's various funds are called investment beliefs. One of the main beliefs is that over the long term, equities will outperform bonds to compensate for their higher risk. Although equity returns are expected to be greater than bonds over the long run, they are also more volatile. For this reason, equity investments are only suited for investment portfolios with longer-term (for example, more than five years) investment horizons. Accordingly, only the Ed Tel Endowment Fund and the Pension Fund have significant equity allocations (each has 60% equity). Conversely, the investment funds with a lower tolerance for risk and shorter time horizons (for example, working capital funds) are not invested in equities and therefore are sheltered from the higher volatility of equity markets.

Finally, as part of an annual review process, a formal risk assessment of the City's investment program ensures risk mitigation strategies and controls are in place and consistent with industry best practices.



## INVESTMENT BELIEFS

1. The investment return on the funds is a function of capital market returns, asset allocation, manager structure and individual managers.
2. There is a relationship between risk and return – higher returns generally require taking higher risk.
3. In the long term, equities will outperform bonds to compensate for their higher risk.
4. The long-term asset mix is the most important component of a portfolio's risk and return.
5. Active management can add value but comes with added costs and effort, which must be assessed along with the passive alternative, whenever changes are made.
6. Alternative strategies/asset classes may be appropriate and will be evaluated based on their liquidity, the management time needed to monitor the investment and the level of transparency.
7. Market timing at the policy level is an inefficient strategy for consistently increasing returns.
8. Diversification of asset classes, implementation strategies and security selection can improve the risk and return characteristics of the funds.
9. Asset mix rebalancing generally adds value relative to buy and hold strategies.
10. Effective manager structure can improve the net returns and lower the risk of the funds.

## INFRASTRUCTURE INVESTMENTS

Infrastructure is defined as large-scale projects that provide essential services to society. Examples include toll roads, airports and utilities, and may involve developing, operating and/or maintaining the asset.

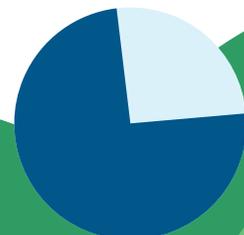
The infrastructure asset class is a global market. Investments can be made either through unlisted (private) or listed (publicly-traded) strategies. Possible opportunities for investors are expected to continue expanding significantly in the coming years.

## ASSET ALLOCATION

The mix of asset classes in a fund is called the asset mix. For example, a fund could have an asset mix of 30% bonds, 25% Canadian equity, 30% global equity, 5% emerging market equity and 10% infrastructure.

The asset mix reflects the investor's underlying goals and objectives for the fund in terms of risk and reward.

The Policy Asset Mix is the long-term target asset mix of the fund, as stated in the Investment Policy. This allocation is structured to allow the fund to meet its stated investment objectives over time. Over shorter time periods, the returns may fall short or exceed the investment objectives.



# GOVERNANCE

Established by the City Manager, the Investment Committee governs the investment of the City's financial assets and provides proper oversight of the City's investment efforts. Committee members bring investment and business expertise. Continual monitoring of the City's investment program and implementing changes as necessary ensures the funds are well-positioned and appropriately invested to meet their objectives. This approach also assures Edmontonians that the City's policies and procedures maximize investment returns at a prudent level of overall risk.

## 2020 INVESTMENT COMMITTEE MEMBERS

**Mary Persson** *Chairperson*

Deputy City Manager and Chief Financial Officer  
City of Edmonton

**Stacey Padbury** *Secretary*

Deputy City Treasurer and  
Branch Manager, Financial Services  
City of Edmonton

**Greg Holubowich**

President  
Edmonton Fire Fighters' Union

**Filip Ksiazkiewicz**

Senior Portfolio Manager  
TELUS Investment Management

**Savvas Pallaris**

Executive Vice-President,  
Commercial Mortgages and Life Investments  
Addenda Capital

**Blake Walker**

Former Manager Treasury and Deputy City Treasurer  
City of Calgary

## KEY RESPONSIBILITIES OF THE INVESTMENT COMMITTEE

- Review and recommend changes to the Investment Policy and Terms of Reference.
- Review investment strategies, capital market assumptions and manager structure.
- Monitor all reported investment activities for compliance with City policy and statutory requirements.
- Meet with external investment managers, performance measurement advisors and external auditors.
- Monitor investment performance versus established performance benchmarks.
- Assist the Chief Financial Officer in preparing an annual report on investment performance for recommendation to the City Manager and City Council.

## KEY RESPONSIBILITIES OF CITY COUNCIL

City Council, as senior governing fiduciaries, receives reports and recommendations from the City Manager and approves the Investment Policy, which establishes the following:

- investment objectives and beliefs,
- permitted investment categories and asset allocation,
- performance benchmarks and implementation strategies,
- proxy voting guidelines and
- monitoring, controls and reporting requirements.

## COMPLIANCE

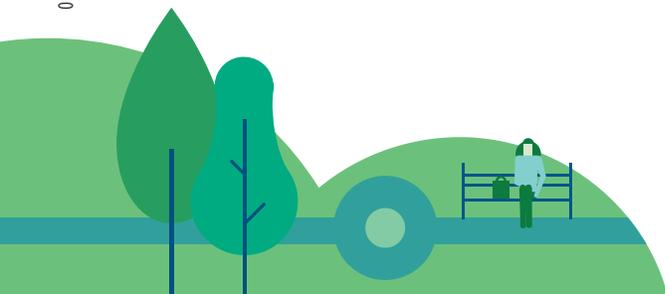
As at December 31, 2020, the investment funds were in compliance with the City of Edmonton Investment Policy and all statutory requirements.

## PROXY VOTING

The City's Investment Policy contains a commitment for the City of Edmonton to support social and ethical business practices through proxy voting — the shareholder resolution process.

A proxy voting agent is retained to vote the City's ballots for the companies in which the City owns shares. The voting service adheres to the City's guidelines through careful analysis of each voting issue.

During 2020, the City of Edmonton exercised its shareholder rights and voted its proxies in accordance with the Investment Policy. In addition, the Investment Committee is currently reviewing environmental, social and governance (ESG) practices.



# MANAGEMENT STRATEGIES

The City's investment structure combines active and passive management strategies.

**Active strategies** are in place when the potential to exceed the return of the established benchmark by actively selecting securities is believed to be high:

- Active managers try to exceed performance benchmarks by investing in a subset of securities expected to outperform the broader benchmark index – basing the selection of securities on a specific theory or investment style.

**Passive strategies** are used in markets where active management generally has not outperformed the benchmark over time:

- Passive managers fully replicate a broad market index such as the TSX or S&P 500 (by buying securities in the same proportion) – ensuring returns are virtually the same as the published index returns. As a result, passive managers minimize the risk of underperformance and have little opportunity for outperformance, but their fees and expenses are significantly lower than those for active management.

## INTERNAL FUND MANAGEMENT

The fee savings from managing a portion of the City's financial assets in-house are approximately \$1.5 million a year. This approach has resulted in more than \$15 million in savings over the last 10 years.

## INVESTMENT MANAGERS

The Ed Tel Endowment Fund, Pension Fund, Long-Term Disability Fund and Balanced Fund all share the same investment managers.

### Canadian Equity

QV Investors  
TD Asset Management (passive)  
Triasima Portfolio Management

### Canadian Fixed Income

City of Edmonton Investment Management (internal)

### Global Fixed Income

Ninety One

### Global Equity

Arrowstreet Capital  
Copper Rock Capital Partners

### Emerging Market Equity

Arrowstreet Capital

### US Equity

TD Asset Management (passive)

### International Equity

Fidelity Institutional Asset Management

### Infrastructure

Northleaf Capital Partners (unlisted)  
RARE Infrastructure (listed)



