
TO: MEMBERS OF THE INVESTMENT BOARD

SUBJECT: 2021 INVESTMENT MANAGEMENT ANNUAL REPORT

PREPARED BY AND KEY CONTACT: T. RAYAISSE, PORTFOLIO MANAGER, EXT. 4724
J. BAYLEY, INVESTMENT ANALYST, EXT. 4423

SUBMITTED BY: C. MILLAR, DIRECTOR OF FINANCE AND TREASURER, EXT. 5130

RECOMMENDED MOTION

1. That the Report to the Investment Board concerning the 2021 Investment Management Annual Report approved by the City's Investment Board on March 30, 2022, be received for information.
2. That the Environmental, Social and Governance (ESG) integration framework in Appendix "B" of the Report to the Investment Board dated March 30, 2022, be adopted.
3. That the following statement be added to the Investment Policy Statement under Section 4.1. Investment Principles:
 - a) Material ESG factors and traditional financial factors are identified and assessed to form an investment decision.

PURPOSE & BACKGROUND

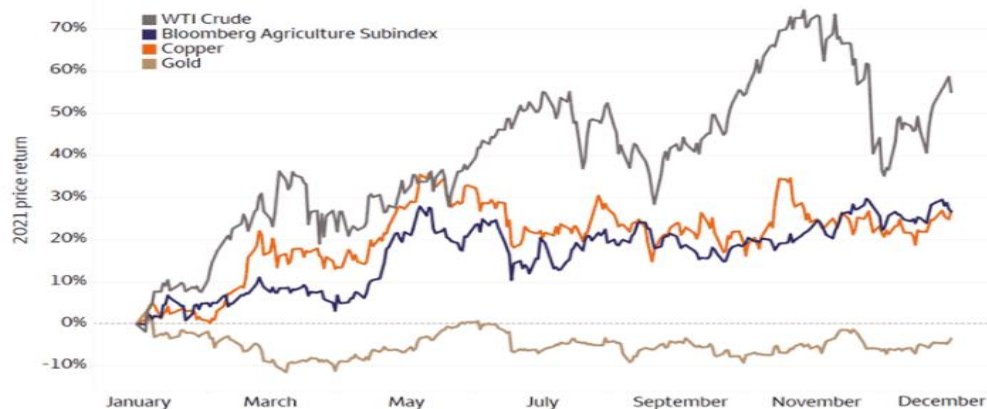
4. The purpose of this Report is to discuss the performance of the investment portfolio in 2021, as required by Ontario Regulation 43/18 (as amended) of the *Municipal Act, 2001*.
5. Ontario Regulation 43/18 (Eligible Investments and Related Financial Agreements) of the *Municipal Act, 2001* requires certain disclosures to Council as outlined in Appendix "A" including a statement from the Treasurer indicating if all investments are consistent with the City's Investment Policy and Investment Plan.
6. On June 3, 2019, City Council adopted By-law 2019-047 adopting the Prudent Investor Standard in accordance with section 418.1 of the *Municipal Act, 2001* and approved the establishment of an Investment Board. The Investment Board is responsible for control and management of the City's investments pursuant to the Prudent Investment Standard and the Investment Policy Statement adopted by City Council.
7. On January 13, 2020, City Council approved motion 20-G-001 appointing four citizen representatives to the Investment Board in accordance with the terms of reference as authorized. Membership is comprised of the City's Treasurer and the four citizen members. Members are appointed for a term to expire on November 14, 2022, unless otherwise provided by a resolution of City Council.
8. Following Council's adoption of motion 20-G-091 regarding the Investment Policy Statement on June 15, 2020 the Investment Board met on November 18, 2020 and adopted an Investment Plan to achieve the objectives set out in the Investment Policy. The Investment Plan deals with how money is to be invested and sets out the asset allocation ranges.
9. As per Ontario Regulation 43/18, the Investment Board should submit an annual report to the Finance and Corporate Services Committee about the performance of the City's investment portfolio.

10. On May 10, 2021, Council adopted motion 21-G-113 requesting that staff in the Finance Department and the Investment Board investigate the feasibility of adopting a Responsible Investment Screening Process for the City's Investment Portfolio using a structure of environmental, social and governance (ESG) factors and report back to the Finance and Corporate Services Committee in 2022.

ANALYSIS

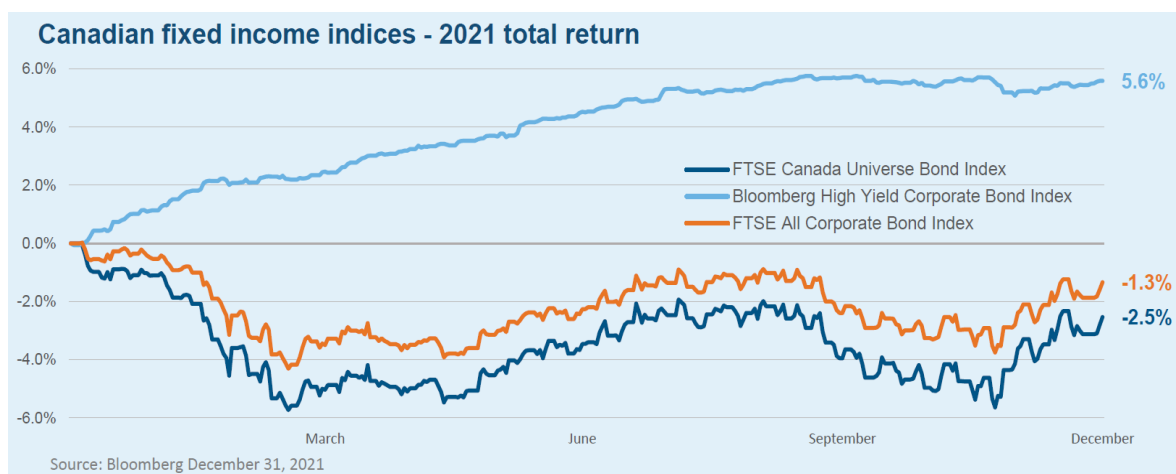
Market commentary:

11. Yet another unprecedented year for the financial markets. Global equity markets rallied to fresh new highs, driven by a low interest rate environment, robust corporate earnings growth as consumer spending surged as lockdown restrictions eased, and renewed optimism that the COVID-19 vaccine rollout would help return normalcy for businesses and consumers. Retail investors returned to the equity markets in part driven by the “meme’ stock frenzy and short-term day trading.
12. In the US the S&P 500 Index rose by 26.9%; Europe’s EURO STOXX 50 Index rose by 21%; the global MSCI World Index gained 20.1% on the year. Here in Canada, the S&P/TSX Composite Index rose by 21.7%. In summary 2021 was another very strong but volatile year for equity markets, led by broad sector advances in Energy, Real Estate, and Financials.
13. Increased consumer demand exacerbated global supply chain bottlenecks led prices of everything from automobiles, commodities, food and housing higher. Low housing supply, elevated pandemic savings and the anticipated “new normal” of hybrid-work drove housing prices to new record highs. The Canadian Real Estate Association (CREA) reported nearly 670,000 houses changed hands in 2021, eclipsing the previous records set in 2020 by about 20% and about 30% higher than the 10-year rolling average.
14. Annual Inflation in Canada was 3.4% for 2021, coming in much higher than the forecast 2.5% expectations made at the beginning of the year. There were significant differences in inflation geographically. The largest inflation increases were observed in Prince Edward Island (+5.1%) and Nova Scotia (+4.1) and the lowest were in the Yukon (2.2%) and Nunavut (+1.4%). Ontario saw prices increase by +3.5%.
15. In the commodity sector, West Texas Intermediate (WTI) Crude oil futures contracts, the North American benchmark for oil, traded in negative territory in 2020 due to a dramatic drop in demand caused by the COVID-19 pandemic. 2021 saw a significant snapback in WTI Crude prices surging almost 60% for the year. Meanwhile, food-based commodities such as Soybeans, Wheat, Corn, Coffee, and Sugar, gained almost 30% YoY as measured by the Bloomberg Agricultural Sub-index.



Source: Bloomberg.

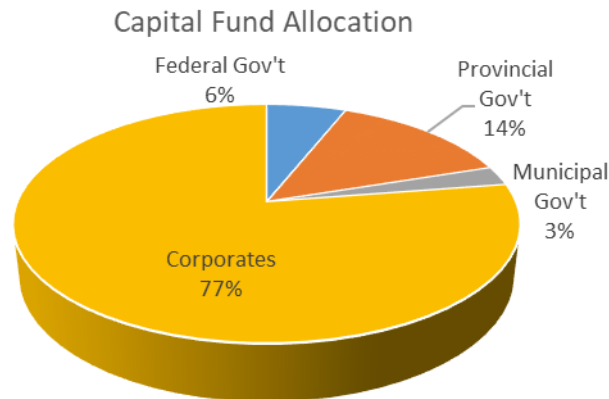
16. Inflation concerns created volatility in Canadian fixed income markets amid rising bond yields. The FTSE Canada Universe Bond Index declined by 2.5%. Most of the price decline occurred in the first quarter when the Government of Canada 10-year bond yield rose by 88 basis points (bps) on the back of renewed optimism for a reopening of the world economy driven by high vaccination rates. The overall rise in yields led to less volatile shorter duration bonds outperforming longer duration bonds. The FTSE Canada Long Term Overall Bond Index fell 4.5%, while the FTSE Canada Short Term Index declined by 0.9%.
17. High quality investment-grade corporate bonds performed better than government bonds as credit spreads tightened. High yield bonds were by far the best performer; the Bloomberg Canadian High Yield Corporate Bond Index produced a mid-single-digit return as showed in the graph below (source: Mackenzie Investments). Within the government sector, federal bonds outperformed provincial and municipal bonds.



Portfolio Commentary:

18. The portfolio is made up of three funds – the Operating Fund, the Capital Fund and the Growth Fund.
19. The portfolio achieved a FY 2021 total return of 1.61% or \$4.57 million on an average portfolio value of \$283.87 million. All three funds outperformed their respective benchmarks over the year, providing a better return than if the City chosen a purely passive approach.
20. However, due to the continued low interest rate environment and very low cash yields, investment returns were lower by 69 basis points compared to 2020.
21. The negative price performance from bonds detracted from portfolio returns. This was a result of the yield curve shifting higher and flattening in anticipation of aggressive monetary tightening in response to increasing inflation. The relatively small allocation of the portfolio to equities (1%) served to offset some of the downside. The portfolio continues to be transitioned to the adopted Prudent Investor strategy and at this point the 2021 performance does not fully represent the expected full impact of adding equities and expanding the fixed income positions.
22. The **Operating Fund** returned 1.05% or \$1.68 million on a weighted average balance of \$161 million. This represents 37% of the total portfolio return. Compared to the total return of the Canada 90 Day Treasury Bill Index which returned 0.20% in 2021, the money-market portfolio outperformed this benchmark by 85 basis points. As the portfolio shifts to the new policy portfolio the money-market weight is expected to diminish.

23. The **Capital Fund**, which consisted of fixed income instruments, mainly Government and Investment-Grade Corporate bonds (above BBB-rating), and a Promissory Note had a weighted average value of \$118 million and returned 2.24% or \$2.63 million. The Capital Fund contributed approximately 58% of the total portfolio return. The Capital fund outperformed the 1–10-year aggregate benchmark, which returned -4.1% by 634 basis points. The outperformance was driven largely by a higher allocation to corporate issues which outperformed Government bonds by ~120 basis points and the allocation to higher yielding GICs and the Promissory Note. Additionally, a higher average coupon for bonds in the portfolio 5.09% versus the benchmark 2.61% and a less volatile weighted duration of 5.6 versus the benchmark of 10.4 made the portfolio less sensitive to changes in interest rates.



24. The **Growth Fund**, which held \$5 million in Canadian and US equities at year-end and returned 39.24%. Albeit a small allocation of the total portfolio, equities contributed approximately 6% to total portfolio return compared to less than 1% in 2020. The equity portfolio consisted of 75% US Equities and 25% of Canadian Equities. The tactical overweight position to US equities, coupled with the strengthening of the US Dollar led to an unrealized currency gain for the equity portfolio when stated in Canadian dollars.

Environmental, Social and Governance (ESG) Integration framework

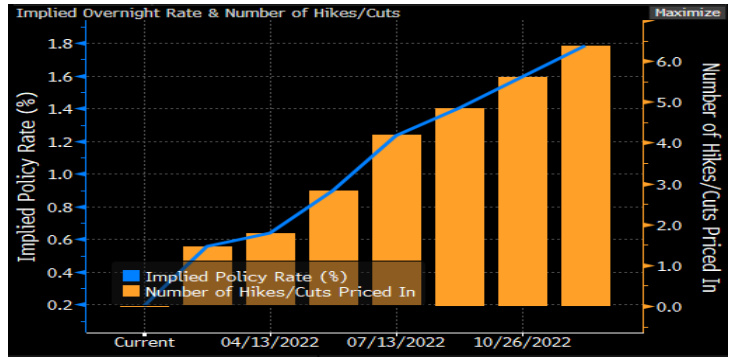
25. ESG integration is defined as “the explicit and systematic inclusion of ESG factors in investment analysis and investment decisions.” It is a holistic approach to investment analysis, where material factors—ESG factors and traditional financial factors—are identified and assessed to form an investment decision. ESG integration typically has three components:
- a) **Research:** material financial and ESG information are gathered from various sources and discussed with companies’ management teams.
 - b) **Security and portfolio analysis:** assessment of the impact of material financial and ESG factors on the corporate and investment performance of a company, sector, country, and/or portfolio.
 - c) **Investment decision:** The material traditional financial factors and ESG factors identified and assessed influence a decision to either buy/increase weighting, hold/maintain weighting, sell/decrease weighting, or do nothing/not invest.

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26. ESG integration does not mean that:
- a) Investment in certain sectors, countries, and companies is prohibited;
 - b) Portfolio returns are sacrificed to perform ESG integration techniques;
 - c) Immaterial ESG factors affect investment decisions and traditional financial factors are ignored; or
 - d) Major changes to investment process are necessary.
27. ESG integration and exclusionary screening are not the same. Exclusionary screening is implemented through a screening policy that reduces the investment universe. Typically, exclusionary screening is implemented before any investment analysis takes place. This is contrary to ESG integration, where financial information and ESG information are embedded in the security selection and portfolio construction process and all companies, sectors, and/or countries in the investment universe can be bought and sold.
28. A key component of ESG integration is lowering risk and/or enhancing returns. ESG integration techniques are applied to uncover hidden risks that might remain undiscovered without the analysis of ESG information and trends. ESG integration is a complement to current investment process and practices. The main addition to process is the sourcing and analysing of ESG information, which is necessary to understand the top ESG issues affecting a company, sector, or country.
29. The CFA Institute and Principles for Responsible Investment (PRI) developed a framework (See Appendix B) for ESG Integration which identifies various ESG integration techniques which could be used based on the particulars of each firm. As every firm is unique, the ESG integration techniques of one firm are not necessarily the right techniques for all firms. For instance, most ESG integration techniques suitable for the City's current investment process will be at the portfolio construction level.
30. For instance, based on the City's investment strategy and investment plan which entail investing in broad market sector securities, at the portfolio level, staff would:
- a) Monitor and review ESG and financial risk exposures across sectors, countries and currencies;
 - b) Assess the ESG profile of portfolios relative to the ESG profile of their respective benchmarks and when necessary, adjust the weightings of sectors, countries and/or currency to mitigate ESG risk exposures; and
 - c) Integrate ESG risk analysis in asset allocation decision to mitigate both short and long term ESG risks and enhance financial performance.
31. As mentioned in paragraph 27, a necessary ingredient to ESG integration is the availability of ESG information to assist in the assessment and decision-making process. The sourcing of this information would come at an additional cost. Much like the credit analysis and rating industry, more companies are specializing in ESG analysis and rating for companies, sectors and countries. This trend should improve the quality and availability of the data, the development of standards in reporting and most importantly promote good ESG practices globally.

32. We recommend adopting the CFA Institute and Principles for Responsible Investment (PRI) ESG Integration framework as the general framework for the City because of its holistic approach to ESG integration and the implementation flexibility it provides. As the investment management evolves more and more techniques could be easily integrated.

Looking Ahead

33. The latest read on inflation data in Canada suggests that inflation continues to accelerate to the upside and the market is pricing in more aggressive moves by the Bank of Canada to tame inflation. The chart on the right (right axis) indicates that the current expectations for Bank of Canada, likely hiking at 6 of the remaining 7 scheduled meetings for 2022, bringing the bank rate to a more neutral 2.0%. Analysts' consensus suggests that inflation is to return to around 3% by year end as monetary policy tightens. However, rising labour costs could be a longer-term issue for sustained inflation rates.



34. Against the backdrop of heightened geopolitical tension, the possibility of a resurgence of COVID 19 and potential default in the Chinese property markets (Evergrande), Central Banks must tread carefully as they embark on the path of interest rate “normalization”. Amid all the risks and uncertainties, a disciplined approach to investment management, paired with a focus on a long-term outcome are some of the best risk management tools.

APPENDIX "A"

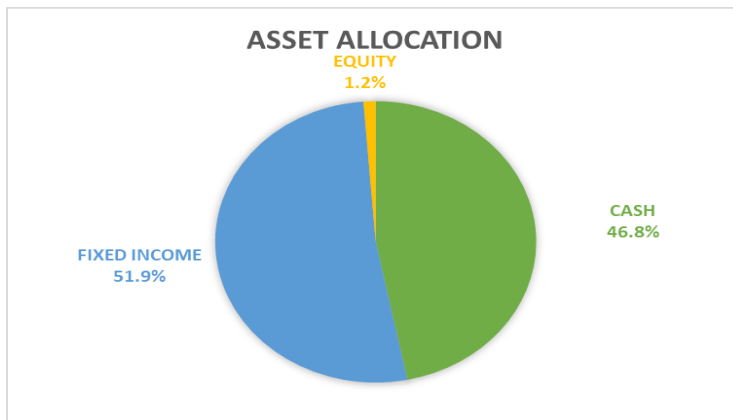
Regulatory Disclosures

i) Performance

The Corporation of the City of Barrie earned a total return of 1.61% in 2021, 69 basis points lower than 2020 driven by the ongoing low interest rate environment and the underperformance of bonds. This was largely driven by a significant upward shift in the yield curve and due to inflation concerns and the anticipated policy response by the Bank of Canada.

ii) Asset Allocation

The following table shows the overall asset allocation by portfolio compared to the policy portfolio. The portfolio is sufficiently diversified across securities with the top 20 holdings representing approximately 23% of the total portfolio.



Top Holdings			
Alectra 4.41% Promissory Note	20,000,000.00	6.24%	
Canada Housing Trust 2.55% Dec-2023	5,134,315.00	1.60%	
Newfoundland & Labrador Hydro 5.70% Jul-2033	3,923,238.00	1.22%	
Ontario Hydro 8.25% Jun-2026	3,842,724.00	1.20%	
Newfoundland & Labrador 8.45% Feb-2026	3,786,693.00	1.18%	
Prince Edward Island 6.10% Jul-2027	3,664,143.00	1.14%	
Nova Scotia 9.60% Jan-2022	3,019,062.00	0.94%	
British Columbia 9.50% Jun-2022	2,941,148.55	0.92%	
Reg of Waterloo 1.9% Apr-2029	2,912,709.05	0.91%	
Gov't of Canada 9.25% Jun-2022	2,590,265.00	0.81%	
NAV Canada 7.40% Jun-2027	2,531,862.00	0.79%	
Nova Gas Transmission 8.875% May-2026	2,489,378.00	0.78%	
Lloyds Banking Group 3.50% Feb-2025	2,109,954.00	0.66%	
Heathrow Funding 3.25% May-2025	2,060,076.00	0.64%	
West Edmonton Mall 4.309% Feb-2024	2,037,704.00	0.64%	
Wells Fargo 2.493% Feb-2027	2,014,458.00	0.63%	
Province of Saskatchewan	2,013,276.00	0.63%	
George Weston 6.69% Mar-2033	1,924,165.82	0.60%	
Enbridge 7.20% Jun-2032	1,915,735.19	0.60%	
Scotiabank 8.90% Jun-2025	1,468,492.80	0.46%	
% Top 20 Holdings	72,379,399.41	22.57%	

iii) Maturity Distribution

As at 31st December, the fixed income portfolio had a weighted average maturity of 5.6 years compared to 10.4 years of the respective fixed income benchmark. The fixed income portfolio is defensively positioned for a rising interest rate environment. Additionally, 47% of the portfolio is invested in cash equivalents with an average maturity of less than 90 days.

iv) Investment in Own Securities: None

v) Statement of Treasurer regarding Compliance with Investment Policy

I, Craig Millar, Treasurer of the City of Barrie, hereby state that in my opinion, all investments were made in accordance with the investment policies and goals adopted by the City.

vi) Statement of Treasurer regarding Quality of Investment

I, Craig Millar, Treasurer of the City of Barrie, state that none of the investments fell below its required standard during the period covered by this Report.

C. Millar, MBA, CPA, CGA
Director of Finance and Treasurer

APPENDIX "B"

ESG INTEGRATION FRAMEWORK



RESEARCH: THE INNER CIRCLE

Qualitative Analysis

- **Company questionnaires:** Questionnaires sent to companies to collect more ESG data and information where the company's level of public ESG disclosure is inadequate. These questionnaires are also used in parallel with regular company meetings, where investors and companies will meet to discuss the most material ESG issues.
- **Red-flag indicators:** Securities with high ESG risk are flagged in lists, research notes, dashboards, and databases.
- **Watch lists:** Securities with high ESG risk are added to a watch list for regular monitoring.
- **Internal ESG research:** Based on a variety of data sources, proprietary ESG research/views/scores are created for all securities in the portfolio and investment universe.
- **SWOT analysis:** ESG factors are included in the traditional SWOT (strengths, weaknesses, opportunities, and threats) analysis.
- **Materiality framework:** A materiality/sustainability framework is created that includes all the key ESG risks and opportunities for each sector/country. This framework is referred to when making investment decisions and is regularly updated.
- **ESG-integrated research note:** Research notes/credit notes consist of traditional financial information and analysis and ESG information and analysis.
- **Centralized research dashboard:** Traditional financial data and ESG data are kept on one platform (dashboard/database) so practitioners can analyze concurrently traditional financial factors and ESG factors.
- **ESG agenda at (committee) meetings:** Investment teams (and possibly ESG teams/specialists) have a dedicated ESG item on all agendas of investment team meetings. Committees meet to discuss ESG strategy, ESG performance of portfolios, and/or controversial securities.

Active Ownership

- **Voting:** This structured process captures all voting rights and applies a rigorous analysis to management and shareholder resolutions before casting votes. In addition to being used for voting, this process can be employed to submit resolutions on which other shareholders may vote.
- **Individual/collaborative engagement:** Engagement captures any interactions between the investor and current or potential investee companies on ESG issues and relevant strategies, with the goal of improving (or identifying the need to influence) ESG practices and/or improving ESG disclosure. It involves a structured process that includes dialogue and continuously monitoring companies. These interactions might be conducted individually or jointly with other investors.

SECURITY LEVEL: THE MIDDLE CIRCLE

Security Valuation—Equities

- **Forecasted financials:** Adjustments are made to forecasted financials (e.g., revenue, operating cost, asset book value, capital expenditure) for the expected impact of ESG factors.
- **Valuation-model variables:** Adjustments are made to valuation-model variables (e.g., discount rates, perpetuity growth, terminal value) for the expected impact of ESG factors.
- **Valuation multiples:** Adjustments are made to valuation multiples to calculate “ESG-integrated” valuation multiples. These multiples are then used to calculate the value of securities.
- **Forecasted financial ratios:** Forecasted financials and future cash flow estimates are adjusted for ESG analysis and the effect on financial ratios is assessed.
- **Security sensitivity/scenario analysis:** Adjustments are made to variables (sensitivity analysis) and different ESG scenarios (scenario analysis) are applied to valuation models to compare the difference between the base-case security valuation and the ESG-integrated security valuation.

Security Valuation—Fixed Income

- **Credit analysis**
 - **Internal credit assessments:** ESG analysis is used to adjust the internal credit assessments of issuers.
 - **Forecasted financials and ratios:** Forecasted financials and future cash flow estimates are adjusted for ESG analysis and the effect on financial ratios is assessed.
 - **Relative ranking:** ESG analysis impacts the ranking of an issuer relative to a chosen peer group.

- **Relative value analysis/spread analysis:** An issuer's ESG bond spreads and its relative value versus those of its sector peers are analyzed to find out if all risk factors are priced in.
- **Duration analysis:** The impact of ESG issues on bonds of an issuer with different durations/maturities is analyzed.
- **Security sensitivity/scenario analysis:** Adjustments to variables (sensitivity analysis) and different ESG scenarios (scenario analysis) are applied to valuation models to compare the difference between the base-case security valuation and the ESG-integrated security valuation.

PORTFOLIO LEVEL: THE OUTER CIRCLE

Risk Management

- **ESG and financial risk exposures and limits:** Companies, sectors, countries, and currency are regularly reviewed and monitored for changes in ESG risks and opportunities and for breaches of risk limits.
- **Value-at-risk analysis:** ESG analysis feeds into value-at-risk models.
- **Portfolio scenario analysis:** Different ESG scenarios are run to assess the impact of ESG factors on portfolio risk and return.

Portfolio Construction

- **ESG profile (versus benchmark):** The ESG profile of portfolios is examined for securities with high ESG risks and assessed relative to the ESG profile of a benchmark.
- **Portfolio weightings:** Adjustments are made to weightings of companies, sectors, countries, and/or currency in a portfolio to mitigate ESG risk exposures and avoid breaching ESG risk limits and other risk limits.
- **Portfolio scenario analysis:** Different ESG scenarios are run to assess the impact of ESG factors on portfolio risk and return.

Asset Allocation

- **Strategic asset allocation:** Strategic asset allocation (SAA) strategies factor in ESG objectives and analysis to progressively mitigate the ESG risks and enhance financial performance.
- **Tactical asset allocation:** Tactical asset allocation (TAA) strategies factor in ESG objectives and analysis to mitigate short-term ESG risks.
- **Portfolio scenario analysis:** Different ESG scenarios are run to assess the impact of ESG factors on SAA strategies and TAA strategies.