



**Municipal Finance
Authority of BC**



**City of Victoria
COTW Presentation**
March 2019

Peter Urbanc, CEO

About the MFA



- Formed in 1970 through the *Municipal Finance Authority of British Columbia Act*
- Primary function: providing infrastructure financing for BC's local governments
 - Mandate includes offering short-term financing alternatives and Pooled Investment Funds
- Ensures access to stable low-cost financing and expanded/best-in-class investment choices for BC's local governments
 - Long term debt ratings of AAA/Aaa/AAA by S&P/Moody's/Fitch
 - 6 pooled funds, more in development

Governance



British Columbia – Local Government

- 28 Regional Governments made up of municipalities, cities, towns & villages

Board of Directors

- 39 Members appointed by local government
- Responsible for reviewing loans, electing trustees

10 Trustees

- Trustees responsible for overseeing operations and management
- Authorize debt issuance

MFA Employees

- Manage loans, debt and investments
 - Balance sheet of \$9.2bn
- Complement of 15 professionals

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MFA Financed Projects



Core Area Wastewater Treatment Project Victoria, BC

Total project cost \$775mm

Expected Completion Fall 2020



Summit at Quadra Village Senior Long-Term Care Home Victoria, BC

Total project cost \$86mm

Expected Completion February 2020



North Island Hospital Projects Campbell River & Courtney, BC

Total project cost \$606mm

Completed September 2017



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MFA 2020 Strategic Focuses



- **Stakeholder Engagement**
 - Increase connectivity with and communication to our stakeholders to deliver on sector needs and add value
- **Resiliency & Capacity**
 - Implement new processes and technology, and increasing our Team to enhance our ability to serve our Stakeholders and respond to external events
- **Implement Additional Risk Management Processes**
 - Update key policies and processes and implement comprehensive risk management practices
- **Technology Support & Security**
 - Transform our technology systems and practices to mitigate emerging areas of risk and create enhanced services for internal and external Stakeholders
- **Program Development & Improvement**
 - Ensure our products remain the best options for our Clients
 - Launch new Pooled Mortgage Investment Fund
 - Complete assessment of investment offerings in conjunction with Pooled Fund Advisory Comm.
 - Research a Prudent Investor “Balanced Fund” and a Fossil Fuel Free Bond Fund to meet Client demand

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Select Investment Topics:

Diversification
SRI Investing
Fossil Fuel Free Funds
Prudent Investor

Local Government Investment Universe



Eligible investments for BC's local governments (the "investment universe") are outlined in section 183 of the *Community Charter*:

- Securities of the Municipal Finance Authority;
- Pooled investment funds under section 16 of the *Municipal Finance Authority Act*;
- Securities of Canada or of a province;
- Securities guaranteed for principal and interest by Canada or a province;
- Securities of a municipality, regional district or greater board;
- Investments guaranteed by a chartered bank;
- Deposits in a savings institution, or non-equity or membership shares of a credit union;
- Other investments specifically authorized under this or another Act.



Diversification is key: strive to own all of the eligible investment categories listed above in order to reduce your portfolio's concentration risk

Investment Policy



A good investment policy provides guidance on portfolio construction and ongoing management. It helps maintain focus and is a critical tool in keeping the local government investment professional focused on the objectives. Councils or Boards approve the policy – **and then let staff manage the portfolio!**

Components

- | | |
|---|-----------------------------------|
| 1. Policy | 10. Collateralization |
| 2. Scope | 11. Safekeeping & Custody |
| 3. Prudence | 12. Diversification |
| 4. Objective | 13. Maximum Limits and Maturities |
| 5. Delegation of Authority | 14. Internal Controls |
| 6. Ethics & Conflicts of Interest | 15. Performance Standards |
| 7. Auth. Financial Dealers and Institutions | 16. Reporting |
| 8. Auth. & Suitable Investments | 17. Investment Policy Adoption |
| 9. Investment Pools | 18. Glossary |

Objectives and Principles

Primary objectives are, in order of priority:

1. **Preservation of Capital**
Accomplished through placing funds with creditworthy institutions and diversification
2. **Liquidity**
Maintain sufficient liquidity to meet all operating and capital requirements
3. **Return on Investment**
Achieve the greatest return, taking into account risk constraints and liquidity needs (maximize risk-adjusted returns)



Be mindful of conflicts of interest when asking for advice in creating or altering your investment policies

Socially Responsible Investing – Some Terminology



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Socially Responsible Investing

Socially responsible investing, also known as sustainable, responsible, "green" or ethical investing, is any investment strategy which seeks to consider both financial return and social/environmental good to bring about social change

ESG Factors

ESG investing entails researching and factoring in environmental, social, and governance issues, in addition to the usual financials, when evaluating potential stocks for your portfolio

Impact Investing

Investing in projects or organizations that meet a set of criteria that may include meeting specific social or environmental outcomes. Most often, does not involve screening out companies or sectors

Fossil Fuel Free (FFF) Investing

Implies the outright exclusion of companies involved in extracting, processing and transporting oil, gas and coal from a mandated investment universe. Definitions of FFF may vary.

UN PRI

Signatories of the United Nations' Principles for Responsible Investment are proponents of responsible investing best practices. Signatories follow 6 key principles and incorporate those into their processes.

Example of ESG factors: the UN's Sustainable Development Goals

The UN's Sustainable Development Goals are gaining prominence as a common norms-based investment strategy



SUSTAINABLE DEVELOPMENT GOALS
17 GOALS TO TRANSFORM OUR WORLD



Source(s): <https://www.un.org/sustainabledevelopment/blog/2015/12/sustainable-development-goals-kick-off-with-start-of-new-year/>

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The Wild Wild West: Many Reporting & Disclosure Standards are Being Developed



Excerpt from KPMG's 2019 Presentation: 'What are Common Trends in Sustainability Disclosure?'

Reporting landscape: initiatives driving ESG reporting



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Socially Responsible & Fossil Fuel Free Investing



- Several BC local governments have expressed interest in Socially Responsible Investing (SRI) via pooled funds offered by MFA
- SRI comprises a host of investment methodologies or strategies which aim to satisfy desired positive social outcome(s) in addition to realizing a return on investment. These outcomes are often measured under the lens of Environmental Social and Governance (ESG) factors.
- The SRI landscape is highly fragmented and complex. The investment industry, and a burgeoning consulting/research support subindustry, has not effectively promoted standardization of terminology or measurement.
- Our Clients' diverse needs and philosophies regarding the appropriate approach to SRI investing have made it impractical and expensive, for the time being, to develop broad-based SRI investment products
- Excluding Fossil Fuel related entities (i.e. FFF investing) is a common approach that many local governments want to employ (for instance, those local governments who have declared climate emergencies)
- MFA currently offers two Pooled High Interest Savings Accounts which provide an option for those interested in divestment or Fossil Fuel Free investment
- Given relative standardization of the definition of FFF, and asset-manager experience in developing cost-effective ways to screen-out FFF-related companies, MFA will likely be offering a Fossil Fuel Free Bond Fund in the near future
- As standardization improves and demand for certain strategies grow, MFA will continue to research new avenues for other SRI investment opportunities for BC's local governments, including Impact Investing options which are gaining traction in the industry

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Limited SRI Investment Opportunities for BC's Municipalities



- Direct investments into government bonds – safest investments one can make but many local governments do not have the tools to manage efficiently
- Direct investments into Green Bonds issued by Federal Agencies, or Provincial or Municipal governments – are typically long-dated (often not suitable), have a low yield and not enough names yet to create diversified portfolios
- SRI-linked Principal Protected Notes (PPN) issued by Canadian banks – can local governments value them?
- Impact GICs offered by some credit unions – many already consider Credit Union GIC as socially responsible product – so it is unclear what benefits an Impact GIC provides to justify the additional costs
- **Some local governments' investment needs dwarf availability of good SRI opportunities**

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4 of MFA's 7 Pooled Funds may be Considered Socially Responsible



	✓✓ 2 Pooled High Interest Savings Accounts	Money Market Fund	Intermediate Fund	Short Term (ST) Bond Fund	✓ Fossil Fuel Free ST Bond Fund (available soon?)	✓ Mortgage Fund
Key Features	<p>Provides Clients with alternatives to hold soon to be needed funds in a high-interest account offered by Schedule-1 Chartered Banks.</p> <ul style="list-style-type: none"> • Offered through CIBC & National Bank • CIDC Deposit Protection up to \$100K • Interest paid monthly • Yield net of all fees 	<p>Serves a similar purpose as the PHISA accounts, however provides diversification versus holding funds with a single entity.</p> <ul style="list-style-type: none"> • Provides a high-quality yield advantage • Currently fully invested in corporate money markets -attractive risk-adjusted incremental yield over similar-term gov't securities 	<p>The Intermediate Fund provides Clients with a diversified medium-term investment alternative. The Fund seeks a yield advantage through exposure to high-quality corporate credit.</p> <ul style="list-style-type: none"> • Approximate 30% gov't credit, 70% corporate credit asset mix 	<p>Designed for local government reserves not needed for 2 – 5 years. This diversified product is slightly more defensive as it has a longer duration profile.</p> <ul style="list-style-type: none"> • Approximate Asset Mix: 45% gov't credit, 45% corporate credit, 8% mortgage-backed securities, 2% cash 	<p>Designed for local government reserves not needed for 2 – 5 years. This diversified product is slightly more defensive as it has a longer duration profile.</p> <ul style="list-style-type: none"> • Approximate Asset Mix: very similar to Bond Fund 	<p>Provides an alternative to the Bond Fund for reserves not needed in the immediate future. Seeks a yield advantage by investing in high-quality 1st mortgages on Canadian income producing commercial properties</p>
Investment Time Horizon	N/A	0 – 9 months	9 – 24 months	24 months – 5 years	24 months – 5 years	3 years +
Current Yield (%)	2.32 – 2.46%	1.96%	1.99%	2.05%	2.05% (TBD)	3.05%

Investment Time Horizon Increases →

Exact composition of Funds subject to change in accordance with MFA's Pooled Investment Funds Investment Policies, Objectives, and Guidelines agreement with PH&N.
 Current Yield as of December 31 2019 and represents the 1 year yield. Mortgage Fund yield is an estimate only.

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Fossil Fuel Free Short Term Bond Fund Overview



- Expected Launch: March 23, 2020
- Provides a credible, well-diversified active investment solution for clients who choose to divest from fossil fuel related investments
 - Uses the same PH&N investment team and process with a proven track-record
 - Will use 3rd party screening services provided by Sustainalytics and Fossil Free Indexes
 - The Sustainalytics screen will exclude companies directly involved in the extracting, processing or transporting of coal, oil or natural gas
 - The Carbon Underground 200, maintained by Fossil Free Indexes, identifies the top 100 coal and the top 100 oil and gas publicly-traded reserve holders globally, ranked by the potential carbon emissions content of their reported reserves
- Benchmark:
 - FTSE Canada Short Term Overall Bond Index

Key Investment Guidelines:

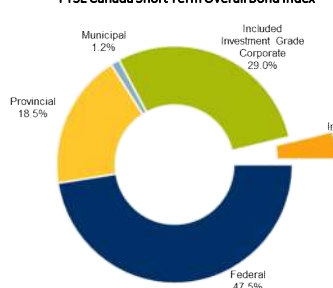
<u>Sector Concentration:</u>	<u>Max</u>	<u>Credit Quality:</u>	<u>Max</u>
Government securities	100%	A- and above	100%
Corporate	70%	BBB- to BBB+	25%
Non-Canadian dollar exposure	20%	Below BBB-	0%
Non-Canadian securities	30%	<u>Interest Rate Guidelines</u>	
Maples	10%	Benchmark +/- 1 year duration	
Illiquid assets	10%	Average term to maturity between 2 and 4 years	
RRB and TIPS	10%	Max 7 years and 3 months for any individual security	

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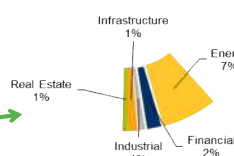
Fossil Fuel Companies Represent less than 4% of the Existing MFA Short Term Bond Fund



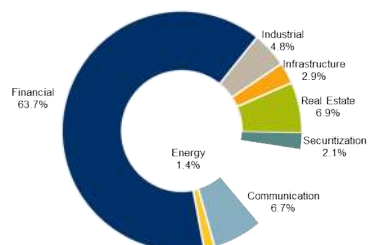
FTSE Canada Short Term Overall Bond Index



Sector breakdown of excluded investment grade corporate bonds (% of overall investment grade corporate)



Sector breakdown of remaining investment grade corporate bonds (% of overall investment grade corporate)



Investable Universe* Characteristics

Modified Duration (FTSE STBF Index)	2.72 yrs
Fossil Fuel Free Modified Duration**	2.71 yrs
Difference	-0.01 yrs
Yield to maturity (FTSE STBF Index)	2.01%
Fossil Fuel Free yield to maturity**	1.99%
Incremental	-0.02%

*Investable universe refers to FTSE Canada Short Term Overall Bond Index
 ** Assumes increase in market value of included holdings proportionate to % of universe before exclusion
 All data as of December 31, 2019
 Source: FTSE Global Debt Capital Markets Inc., RBC GAM (BondLab)

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Prudent Investor Rules: Expanding Investment Alternatives



- Alberta & Ontario have adopted a prudent investor regime for local governments
- Those rules expand the assets that a local government can invest in to include any investment that is deemed “prudent.” For example, it may be “prudent” to invest long term reserves (reserves not needed for 10 years or more) in securities (for example equities) which have higher volatility but higher expected returns
- To manage these more complex portfolios, Ontario has adopted an independent board model. Alberta has limited use of “prudent” portfolios to its largest municipalities
- September 2019: Burnaby’s resolution B128 calling for expanded investment opportunities under Prudent Investment Rules was endorsed at the UBCM Convention
- The Ministry responded on Feb19, 2020: “Local governments are responsible for public money for provisions of core services and upkeep of critical infrastructure. [...] As the Province’s primary objective regarding local government investments is to ensure protection of capital through low-risk instruments, the Ministry is not currently prepared to expand allowable investment provisions.”
- The Ministry’s will not offer prudent powers **to individual local governments** at this time. However, MFA has prudent investor powers itself and therefore the ability to offer any pooled investment options it deems appropriate for its clients. MFA believes a prudent investment approach may make sense if a local government earmarks a portion of its reserves as long-term in nature – for example, 10 years or longer
- In fact, most investment professionals would argue that it would be imprudent not to invest reserves that are ‘long-term’ in a broad global asset portfolio with a higher expected investment return than a fixed income portfolio
- There is a very wide range of reserve pool sizes and investment expertise across BC’s local governments, so a thoughtful approach is critical. History has taught us that the temptation of earning higher returns without understanding the critical need to segregate funds for the long term can lead to bad outcomes
- MFA will be studying the feasibility of appropriate options with Burnaby and other local governments in 2020

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CELEBRATING

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