CITY WIDE
IMPLICATIONS

To: Chair & Members
Audit & Administration Committee

From: Joseph L. Rinaldo
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Date: March 13, 2007

Re: Hamilton Future Fund Annual Investment Report to December 31, 2006
(FCS06044(c)) City Wide

Council Direction:
Not Applicable

Information:

The City of Hamilton Future Fund portfolio has returned 4.74% (excluding realized and
unrealized profits) for the year ending December 31, 2006. Bond lending revenues of
$9,340 are included in the earnings rate. For the past 3 years, the average earning rate
on investments has been 4.58%. The overall return which is impacted by increasing or
decreasing asset prices was 3.80% for the 12 months ending December 31, 2006.
Over the past three years, this overall return has averaged 5.05%. The Future Fund
account has generated, on average over the past three years, approximately $5.3+
million in interest, realized capital gains and lending income annually. The duration of
the portfolio, as of December 31, 2006, was 4.55 years compared to approximately 4.7
years as of December 31, 2005. The total value of the portfolio was $103,448,239 as of
December 31, 2006.

The One Fund (offered by the Association of Municipalities of Ontario and the Municipal
Finance Officers’ Association) returns for the year ending December 31, 2006, was
3.62% for bonds, including unrealized gains and 3.83% for money markets. If our policy
had been used in these funds, (i.e., 90% bonds and 10% money market) the annual
return would have been 3.64%. This underperformed the Hamilton Future Fund
account performance by 16 basis points. This translates into excess revenue from
current management of the Hydro account of approximately $162,000 on an average
portfolio of $101 million.
Investment Return Indicators (for information purposes only)  
(Ending December 31, 2006)

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<tbody>
<tr>
<td>Policy Target</td>
<td>3.91%</td>
<td>3.48%</td>
<td>5.23%</td>
<td>4.88%</td>
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<tr>
<td>Hamilton Future Fund Portfolio</td>
<td>3.80%</td>
<td>5.21%</td>
<td>6.15%</td>
<td>8.18%</td>
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<tr>
<td>The One Fund – Bonds</td>
<td>2.62%</td>
<td>2.09%</td>
<td>4.93%</td>
<td>4.39%</td>
</tr>
<tr>
<td>The One Fund – Money Markets</td>
<td>3.83%</td>
<td>2.52%</td>
<td>2.20%</td>
<td>2.64%</td>
</tr>
<tr>
<td>Scotia Index – Short Governments</td>
<td>3.88%</td>
<td>2.23%</td>
<td>4.89%</td>
<td>4.60%</td>
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<tr>
<td>Scotia Index – Mid Governments</td>
<td>3.91%</td>
<td>5.43%</td>
<td>7.62%</td>
<td>6.17%</td>
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<tr>
<td>Lending Revenues</td>
<td>$9,340</td>
<td>$10,814</td>
<td>$7,063</td>
<td>$4,022</td>
</tr>
<tr>
<td>Earning Rate (Excluding Capital Gains)</td>
<td>4.74%</td>
<td>4.77%</td>
<td>4.23%</td>
<td>4.38%</td>
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Unrealized capital gains at December 31, 2006, totalled $2,559,781, resulting in a total portfolio value of $103,448,239. A capital gain of $151,000 has been realized through the past 12 months. The portfolio fluctuated through this period from a low of 64.04% bonds to a high of 84.69% bonds and is currently 64.04% bonds on a cost basis.

The chart referred to below illustrates the changes in Canadian interest rates over the past 24 months:

**CANADIAN INTEREST RATES**

<table>
<thead>
<tr>
<th>Maturity Term: Canada Benchmark</th>
<th>Interest Rate January 2, 2007</th>
<th>Interest Rate January 3, 2006</th>
<th>Interest Rate January 4, 2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>One Month (T-Bill)</td>
<td>4.12%</td>
<td>3.17%</td>
<td>2.35%</td>
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<tr>
<td>2 yr</td>
<td>3.98%</td>
<td>3.81%</td>
<td>3.02%</td>
</tr>
<tr>
<td>5 yr</td>
<td>3.97%</td>
<td>3.89%</td>
<td>3.69%</td>
</tr>
<tr>
<td>10 yr</td>
<td>4.07%</td>
<td>3.97%</td>
<td>4.30%</td>
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This chart shows that, over the past two years, the general level of interest rates in Canada has increased. Compared to January 2006 and January 2007, it appears that rates have not moved much but that hides most of the rate movements this year. For example, 5 year bond yields have varied from 3.75% to 4.56% before settling in at
3.97% and 10 year bond rates have varied from 3.87% to 4.66% before settling in at 4.07%. Two year bonds have varied from a yield of 3.71% to 4.45% over the past year before ending at 3.98%.

It does appear that the housing slowdown in the US has not spread to other sectors of the economy. Apart from this sector, the rest of the US economy is showing resilience with improvements in industrial production, employment and manufacturing activity. This steady GDP growth should help with the soft landing scenario envisioned by most economists. The Fed is expected to keep rates steady for the near future. The Bank of Canada acknowledges that the slowdown in the US housing sector and automobile sector has reduced economic growth in Canada. It is unlikely that the Bank of Canada will change the Bank Rate until well into the second half of 2007 and rates will move upwards or downwards, depending upon overall economic performance going forward.

While yields of money market instruments are higher than bond yields, the Hamilton Future Fund will continue to hold a large portion of funds in money market instruments. The portfolio will consider increasing duration when the yield curve steepens or expectations of a decrease in money market rates occurs.

Joseph L. Rinaldo
General Manager
Finance and Corporate Services