

NO:

COUNCIL DATE:

REGULAR COUNCIL

TO: **Mayor & Council**

DATE: **November 14, 2019**

FROM: **General Manager, Finance**

FILE: **1880-20**

SUBJECT: **Quarterly Financial Report – Third Quarter - 2019**

RECOMMENDATION

The Finance Department recommends that Council receive this report for information.

INTENT

The purpose of this report is to provide Council with an update on the City's financial activity through the third quarter of 2019 and to compare this activity with the 2019 Financial Plan and the same period in 2018.

DISCUSSION

Based on the Five Year (2019-2023) Financial Plan which was adopted by Council on December 19, 2018, the following discussion provides a summary of the current economic environment including key economic factors globally, nationally and in our province, followed by an outline of Surrey's financial performance through the third quarter of 2019.

Economic Environment and Key Economic Factors

Global and United States Economic Outlook

The ongoing trade war between the United States ("US") and China continues to weigh down the global economy. Financial markets have experienced volatility as developments emerge from the bilateral negotiations. Investor confidence has suffered, and businesses are holding back on capital outlays given the uncertainties. The International Monetary Fund ("IMF") is estimating global Gross Domestic Product ("GDP") will be reduced by 0.8% next year due to the reciprocal tariffs between the US and China.

The US-China trade war and unclear path towards Brexit have dampened demand. Eurozone GDP fell to 0.2% in the second quarter with Italy and Germany possibly heading into recession. The European Central Bank ("ECB") announced that starting November, it will restart its bond buying program. The ECB has cut the deposit rate paid to commercial banks to encourage more lending and it will begin €20 billion monthly purchases of commercial bank bonds. Quantitative easing by the ECB has renewed concerns that the Eurozone may be drawn into a trade war with

the US. In the past, President Trump has accused the ECB of using its monetary policy to devalue its currency in order to support the European export sector.

The United Kingdom's ("UK") Conservative party elected Boris Johnson as the new Prime Minister ("PM") after Elizabeth May stepped down. The PM's negotiated deal with the European Union ("EU") failed to gain parliamentary support which forced a third Brexit Extension. European leaders granted an extension until January 31st, 2020 and cautioned the UK that this may be the last extension offered. The British Parliament has approved the election bill with a snap general election scheduled for December 12th this year. The future of Brexit will be dependent on which party forms the new government. The possible outcomes range from acceptance of the current negotiated deal by Parliament, renegotiation of the Brexit deal with the EU, a second Brexit referendum, cancellation of Brexit and a no-deal Brexit.

The US economy has advanced at a moderate rate with GDP projected to grow at 2.2% this year. The unemployment rate is at 3.7%, a historically low level. The Federal Reserve ("Fed") is expecting inflation to come in close to the 2% target rate.

The Fed cut its key interest rate by 25 basis points at each of its meetings in July, September and October of this year. The reasoning provided was that insurance is needed due to resurgent trade tensions and slowing global growth. The central bank did not yield to the President's call to lower its key rate to near or below zero percent. Strong consumer spending continues to fuel the economy. There are concerns that if new tariffs come into place, consumption will decrease as the prices of goods go up.

The US has put a pause on further escalation of Chinese tariffs, but tensions seem to be easing. The Trump administration is considering the possibility of delisting Chinese companies from US stock exchanges. Another possibility being considered is restricting US pension funds from investing in Chinese companies. It is not clear how the mechanism of delisting Chinese companies would work but the news is sending shockwaves through financial markets and leaving investors on edge. The forced delisting of companies for geopolitical reasons is very unusual. It remains to be seen whether further actions will be taken by the US or if the threat is just part of their negotiation tactics.

Canadian Overview

Canada's economy is showing resiliency with a strong second quarter. GDP grew by an annualized rate of 3.7%. The national unemployment rate came in at 5.7% in August and wages grew by 3.8% year-over-year. Inflation remains close to the central bank's target rate of 2%.

The biggest headwind facing Canada is the ongoing trade war between the US and China. A slow down in the US would drag down Canada's economy as the US is Canada's largest trading partner. The trade war is shrinking business investments which had shown signs of recovery last year. The central bank is expecting slower growth in the second half of the year as quarter two advances were driven by the recovery of export growth and stronger energy production.

The Bank of Canada ("BOC") kept interest rates on hold, opting to not follow suit behind other major central banks and their interest rate cuts. The BOC cited a strong domestic economy and concerns that lower interest rates will reignite a build-up of household debt. The US Central Bank's Fed Funds Rate range of 1.75% - 2.00% is essentially parallel to the BOC's rate of 1.75%. Further cuts by the Fed may force the BOC to follow course as investment will flow to markets with the highest yield. If BOC rates diverge too far from US interest rates, demand for Canadian

dollars will rise as investment surges in. This will put upward pressure on the Loonie and potentially harm exports.

British Columbia Economic Highlights

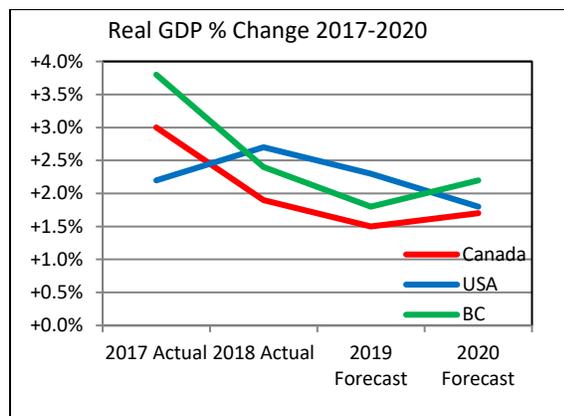
British Columbia's ("BC's") Finance Minister presented the first quarterly budget update and revised 2019 GDP growth projections down to 1.7% due to slowing global economic activity and reductions in retail sales and exports. The projected budget surplus for the year was revised down to \$179 million.

The BC forestry industry has been hit hard in recent months with dozens of mills curtailing or ceasing operations. Lumber supply has been limited due to wildfires and pine beetle infestation. The provincial government has introduced a \$69 million aid package to help the forestry sector. The province also wants the sector to produce more value-added lumber products rather than exporting raw materials alone.

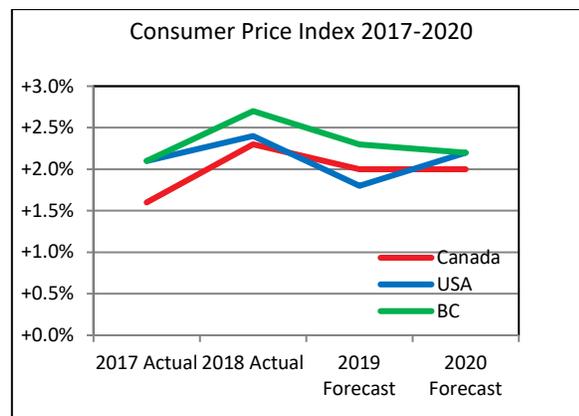
The housing market appears to be recovering from the downturn in the prior year according to the British Columbia Real Estate Association. The average price of all types of homes has increased 2.6% and the number of units sold increased by 4.9% in August compared to the same period last year. The government's various tax measures have tempered the housing market; however, demand can surge if the BOC starts to cut its key interest rate.

BC's economy will depend on major construction projects to fuel growth in the coming years as consumer spending is expected to be muted. Construction of the Kitimat Liquefied Natural Gas ("LNG") plant, twinning of the Trans Mountain Pipeline and the Patullo Bridge Replacement Project are expected to be major contributors to economic activity.

Gross Domestic Product (GDP) Growth Rate and Consumer Price Index (CPI)



Graph 1

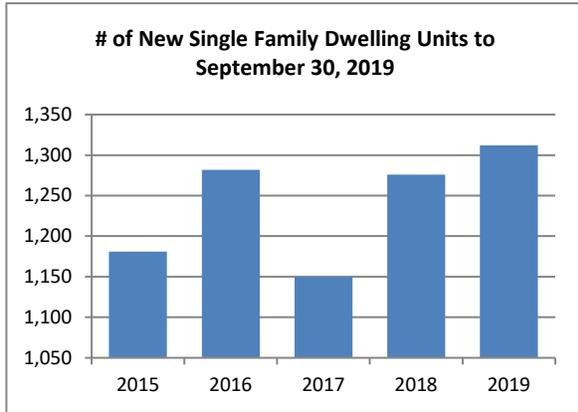


Graph 2

Surrey's Financial Performance

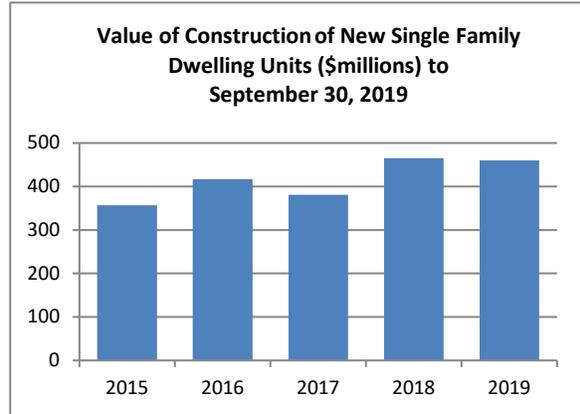
Overall, single-family residential sector in the City is indicative of stagnant or declining activity and a shift towards increased construction activity in multi-family residential projects and high rises. The industrial, commercial and institutional sectors are more indicative of a stabilized market.

The following graphs show data through the first nine months of 2019 compared to previous years.



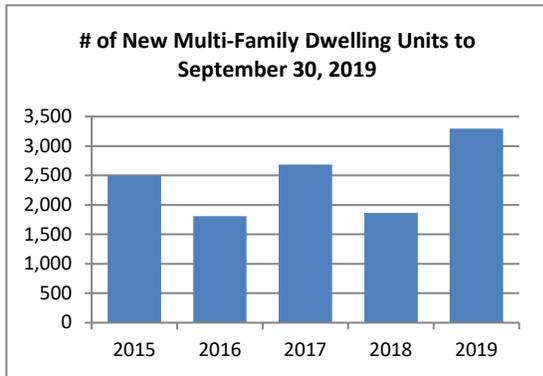
Graph 3

The increase in new Single-Family dwelling units can be attributed to more single-family homes being built with secondary suites, resulting in more dwelling units.



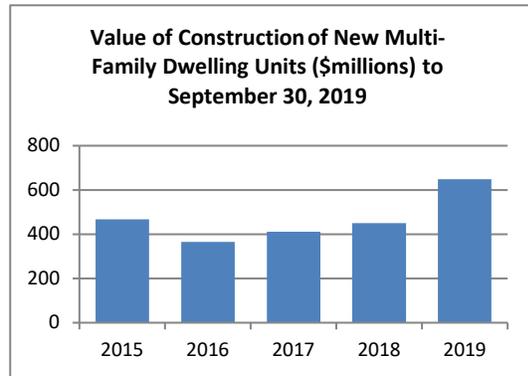
Graph 4

Due to a decline in Single-Family permits without secondary suites but an offsetting increase in such permits with secondary suites, the overall value of construction of New Single-Family dwelling units is similar to last year.



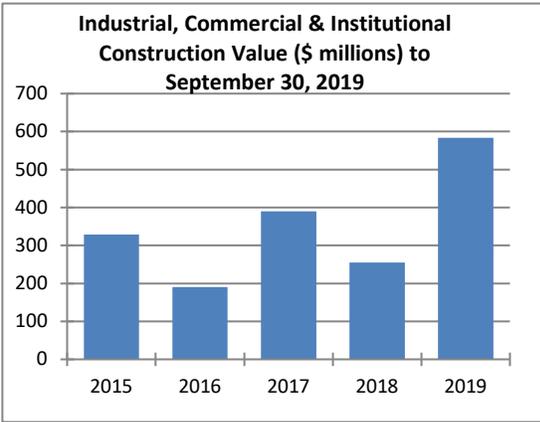
Graph 5

Due to an increase in several new townhouse and new high-rise apartment projects being given permits in this nine-month period, the total number of Multi-Family dwelling units being built in this period is significantly higher than the same period last year. Some of the significant high-rise apartments are being constructed in the City Centre area.



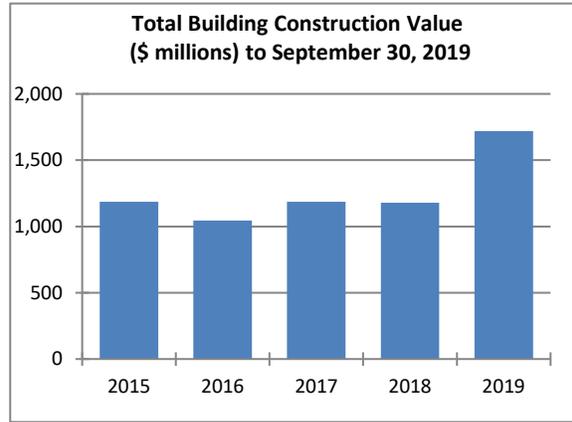
Graph 6

Consistent with the number of Multi-Family dwelling units being built in this period as compared to the same period last year, the value of construction in these building types has increased significantly when compared to the same period last year.



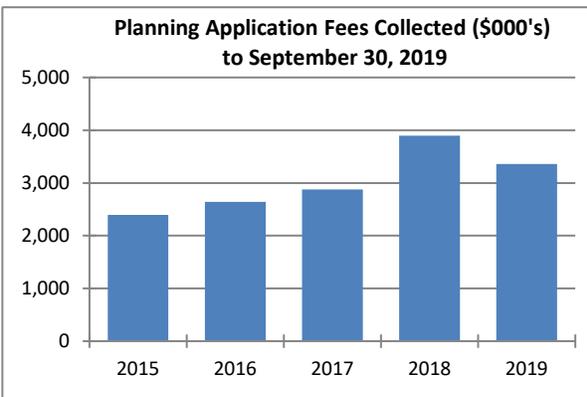
Graph 7

Construction value of Industrial, Commercial Institutional (“ICI”) permits during this period is significantly higher as compared to the same period in 2018. This is primarily due to several large office, retail and warehouse businesses; and several new secondary and elementary schools being issued their permits in this period.



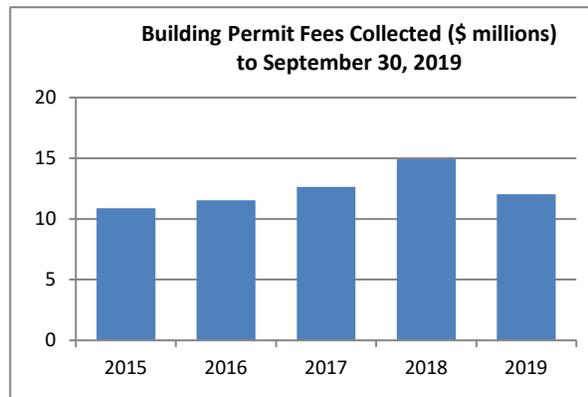
Graph 8

Overall, the value of total building construction in the City for the nine months of the year is significantly higher when compared to the same period last year, primarily due to several high value ICI permits issued in this period.



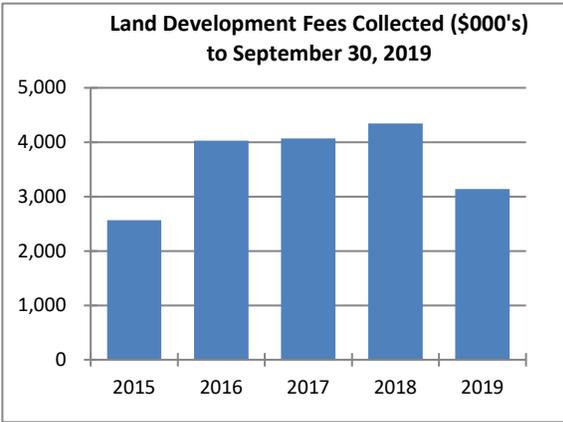
Graph 9

Planning application fees collected in the first nine months of the year are 14% lower than those collected in the same period last year. Continuing negative trends in the real estate market likely had a negative impact on new planning applications received by the City in this year.



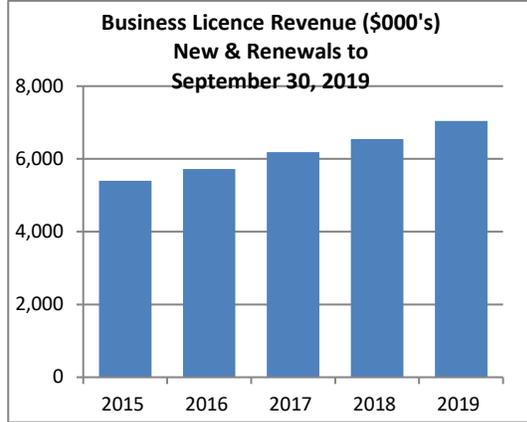
Graph 10

Building permit fees collected for the first nine months of this year are 19% lower than those collected in the same period last year. These fees are indicative of trend in Building Permits being applied with the City for new build projects.



Graph 11

Similar to a decline in Building Permit fees collected in this period, Engineering Land Development fees collected in the first nine months of the year are 28% lower than the same period in 2018.

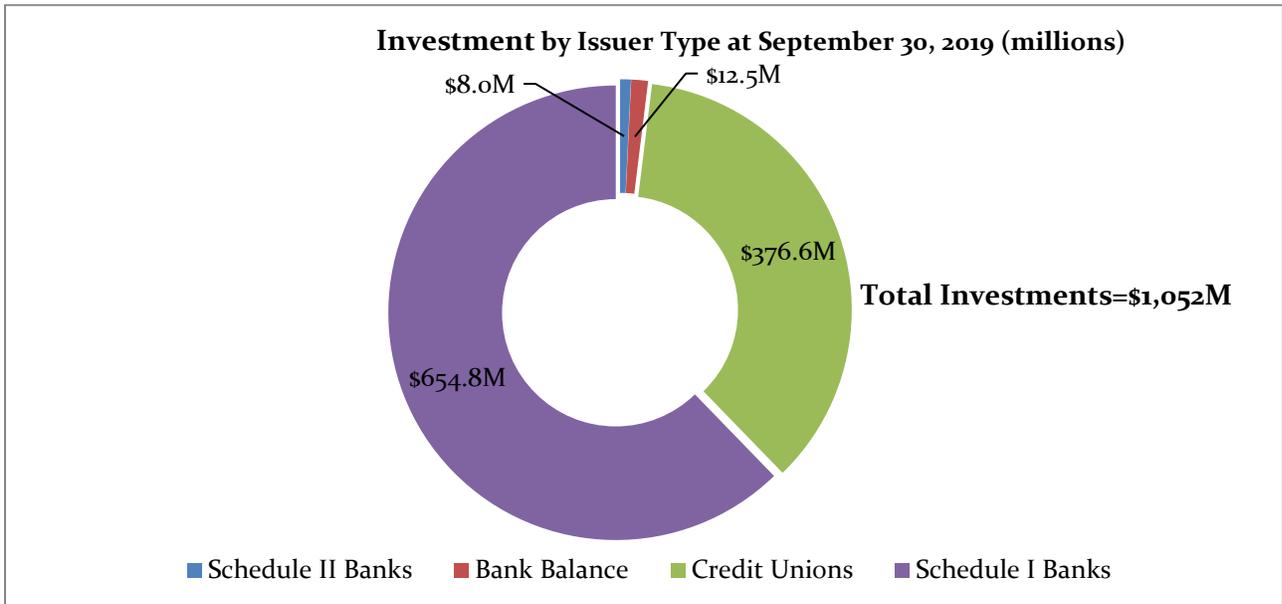


Graph 12

Business Licence Revenue has increased by 8% as compared to the same period last year due to an increase in new businesses obtaining business license in the City.

City Investment Portfolio

The City invests public funds in a prudent manner, providing investment return and long-term security while meeting daily cash flow needs. The investment portfolio is currently valued at \$1,052 million. This represents the amounts earmarked for commitments and working capital related to the City's Capital Program and Operating Expenditures. The graph below shows the City's Investment Portfolio by issuer type.

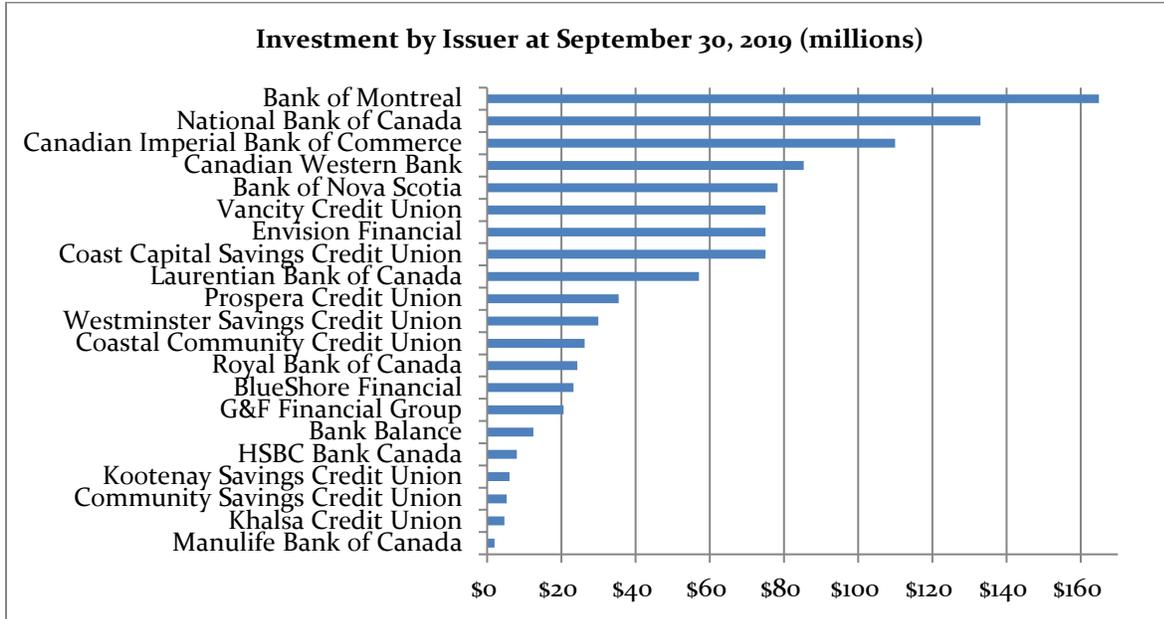


Graph 13

Investments within the portfolio are managed within the framework of the City's Investment Policy. Objectives of the Policy include:

Diversification

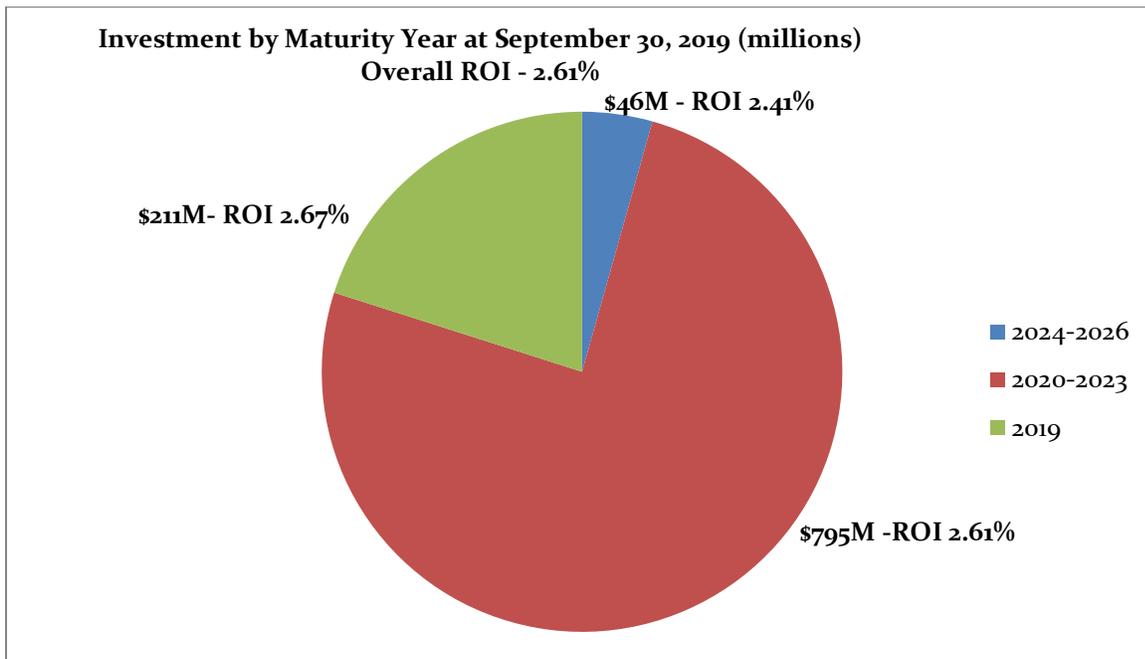
In order to reduce overall portfolio risk, the City diversifies its investment holdings across a range of security types and financial institutions. Graph 14 shows a listing of the City's portfolio by Financial Institution.



Graph 14

Liquidity

The City ensures that the investment portfolio remains sufficiently liquid in order to meet all reasonably anticipated operating and capital cash flow requirements. Maturities coincide with cash requirements, as much as reasonably possible. Graph 15 shows the portfolio by maturity terms.



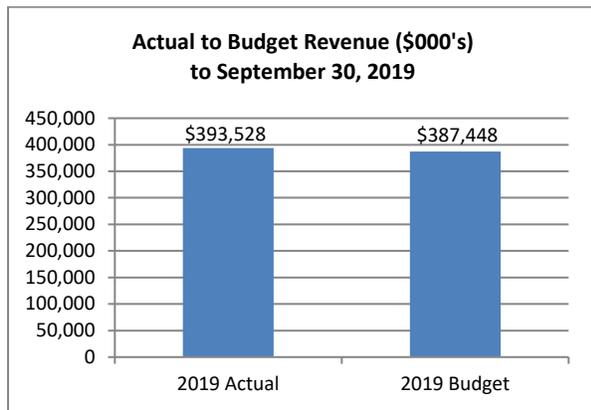
Graph 15

Return on Investment

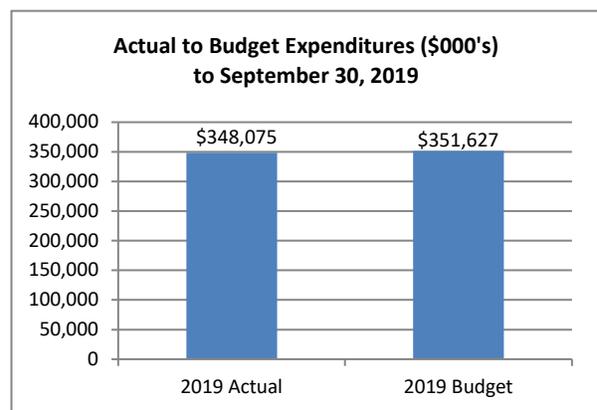
The City's investment portfolio is currently earning a combined rate of approximately 2.61% while maintaining investment security as outlined in the City's investment policy. Interest revenue is currently expected to meet budget by year end. The City strives to earn a reasonable rate of return on the investment portfolio throughout varying budgetary and economic cycles, taking into account investment risk constraints and liquidity needs.

Actual Revenues and Expenditures Relative to the 2019 Budget (Financial Plan)

The following graphs illustrate the variances between the actual and the budgeted operating revenues and expenditures respectively, excluding transfers to reserves, for the third quarter of 2019.



Graph 16



Graph 17

Appendix "I" documents the General Operating Fund's revenues and expenditures through the third quarter of 2019 at a more detailed level. Departments in conjunction with Finance Department are proactively monitoring their actual results on a monthly basis. The following section provides a high-level explanation on a Department-by-Department basis of year to date variances in relation to the 2019 Financial Plan; and as shown in Appendix "II".

Policing Transition has a favourable variance of \$390,000, primarily due to staff vacancies and the timing of expenditures; and is forecasted to have a favorable variance at year-end of \$310,000.

RCMP currently has a favourable variance of \$671,000, primarily due to higher than budgeted revenues and the timing of expenditures; and is forecasted to have a favorable variance at year-end of \$471,000.

Fire Services has a favourable variance of \$755,000, primarily due to revenues being higher than budgeted and the timing of expenditures; and is forecasted to have a small favorable variance at year-end of \$29,000.

Engineering Services Department has a favourable variance of \$1,300,000, primarily due to higher than budgeted revenues from Land Development fees; and is forecasted to have a favorable variance at year-end of \$898,000.

Parks, Recreation & Culture Department has a favourable variance of \$721,000, primarily due to the timing of various expenditures; and is forecasted to have a favorable variance at year-end of \$159,000.

Library Services has a favourable variance of \$337,000, primarily due to the timing of expenditures and staff vacancies; and is forecasted to meet budget at year-end.

Planning and Development Department which also includes Civic Facilities, has a favourable variance of \$2,161,000 due predominately to higher than budgeted revenues from various permit fees; and is forecasted to have a favorable variance at year-end of \$3,599,000.

Mayor and Council currently have a small favourable variance of \$83,000 due to the timing of expenditures and is forecasted to be on budget at year-end.

City Grants currently have a favourable variance of \$522,000 and is forecasted to be on budget at year-end.

City Manager's Department has a favourable variance of \$148,000, primarily due to the timing of expenditures; and is forecasted to have a favorable variance at year-end of \$50,000.

Investment & Intergovernmental Relations Department has a favourable variance of \$293,000, primarily due to the timing of expenditures; and is forecasted to have a favorable variance at year-end of \$125,000.

Finance Department has a favourable variance of \$425,000, primarily due to staff vacancies and timing of expenditures; and is forecasted to have a favorable variance at year-end of \$325,000.

Corporate Services Department has a favourable variance of \$466,000, primarily due to staff vacancies, timing of expenditures and revenues being higher than budgeted; and is forecasted to have a favorable variance at year-end of \$275,000.

SUSTAINABILITY CONSIDERATIONS

The 2019 Quarterly Financial Report supports the objectives of the City's Sustainability Charter 2.0. In particular, this report relates to Sustainability Charter 2.0 theme of Economic Prosperity and Livelihoods. Specifically, this report supports the following Strategic Objective ("SO"):

Corporate SO8: Work towards corporate financial sustainability, including financial reporting.

CONCLUSION

Overall, in relation to the 2019 adopted budget, there has been no material concerns noted through the third quarter of 2019.

Staff will continue to closely monitor all areas to ensure that any negative variances from the 2019-2023 adopted budget are recognized in a timely fashion and appropriate mitigating action is taken where possible.

Kam Grewal, CPA, CMA
General Manager, Finance

Appendix "I" 2019 Third Quarter Council Report, Executive Summary-Revenues & Expenditures
Appendix "II" 2019 Third Quarter Council Report, Departmental Detail

2019 3rd QUARTER COUNCIL REPORT
EXECUTIVE SUMMARY - REVENUES & EXPENDITURES
\$ 000's

	2019: 3rd Qtr YTD Actual	2019 YTD BUDGET	2019: 3rd Qtr YTD Variance	2019 ANNUAL FORECAST	2019 ANNUAL BUDGET	2019 Projected Variance
REVENUE SUMMARY						
Net Taxation	274,266	273,360	906	365,386	364,480	906
Secondary Suite Infrastructure Fee	14,989	14,500	489	19,822	19,333	489
Other Corporate Fees	2,267	2,072	195	3,195	3,000	195
Investment Interest	13,239	13,405	(166)	17,701	17,623	78
Contribution from SCDC	3,375	3,375	-	4,500	4,500	-
Provincial Casino Revenue Sharing	3,150	3,150	-	4,200	4,200	-
Carbon Tax Rebate	488	487		650	650	
Other Trsf from Government	1,144	1,144	-	1,525	1,525	-
Penalties & Interest on Taxes	3,343	3,244	100	3,740	3,640	100
Corporate Leases	5,526	5,555	(29)	7,542	7,571	(29)
Non-Tax Revenues	47,520	46,932	589	62,875	62,042	833
Program Revenues	71,741	67,157	4,585	93,307	87,805	5,502
TOTAL REVENUES	393,528	387,448	6,080	521,568	514,327	7,241
EXPENDITURE SUMMARY						
Program Expenditures, net of transfers	336,663	340,352	3,689	461,162	461,901	739
Council Priorities	195	195	-	260	260	-
Fiscal Services	556	423	(133)	697	564	(133)
Debt Interest & Principal	9,666	9,663	(3)	12,779	12,779	
Other	995	995	-	1,571	1,055	(515)
TOTAL EXPENDITURES	348,075	351,627	3,553	476,468	476,559	91
CORPORATE TRANSFER SUMMARY						
Transfer to /(from) Operating Sources	(2,157)	(1,134)	1,023	(2,360)	(1,512)	848
Transfer to /(from) Capital Sources	9,683	9,449	(234)	12,755	12,599	(156)
Transfer to /(from) Surplus	21,593	19,833	(1,760)	29,686	26,681	(3,005)
TOTAL TRANSFERS	29,119	28,148	(971)	40,081	37,768	(2,313)
Surplus (Deficit)	16,335	7,673	8,662	5,019	-	5,019
Trsf (To)From Unapprop Surplus	(16,335)	(7,673)	(8,662)	(5,019)	-	(5,019)
BALANCED BUDGET	-	-	-	-	-	-

PROJECTED SURPLUS (DEFICIT)

\$ 5,019

Appendix "II"

2019 3rd QUARTER COUNCIL REPORT DEPARTMENTAL DETAIL \$ 000's							
PROGRAM REVENUES	2018: 3rd Qtr YTD ACTUAL	2019: 3rd Qtr YTD ACTUAL	2019 YTD BUDGET	2019: 3rd Qtr YTD Variance	2019 Projected ACTUAL	2019 ANNUAL BUDGET	2019 Projected Variance
Policing Transitioning	6,211	6,452	6,101	351	8,486	8,135	351
RCMP Contract	-	-	-	-	-	-	-
Fire	1,823	2,448	2,033	415	2,521	2,095	426
Engineering Services	6,242	6,721	5,926	795	8,726	7,830	896
Parks, Recreation & Culture	27,668	27,498	27,008	490	34,262	35,046	(784)
Surrey Public Library	1,196	1,417	1,203	213	1,665	1,595	70
Planning & Development	18,745	18,954	16,724	2,230	26,545	22,298	4,247
Mayor & Council	-	-	-	-	-	-	-
City Grants	-	-	-	-	-	-	-
City Manager	-	2	2	-	2	2	-
Invest. & Intergovernmental Relations	-	20	-	20	20	-	20
Finance	964	931	1,072	(141)	1,288	1,429	(141)
Corporate Services	7,352	7,299	7,087	212	9,793	9,375	418
TOTAL PROGRAM REVENUES	70,200	71,741	67,157	4,585	93,307	87,805	5,502
PROGRAM EXPENDITURES NET OF TRANSFERS	2018: 3rd Qtr YTD ACTUAL	2019: 3rd Qtr YTD ACTUAL	2019 YTD BUDGET	2019: 3rd Qtr YTD Variance	2019 Projected ACTUAL	2019 ANNUAL BUDGET	2019 Projected Variance
Policing Transitioning	22,593	23,597	23,637	40	32,526	32,484	
RCMP Contract	99,768	103,449	104,120	671	138,356	138,827	471
Fire	45,867	47,699	48,039	340	67,713	67,316	(397)
Engineering Services	7,613	7,755	8,261	505	10,289	10,291	2
Parks, Recreation & Culture	70,179	72,611	72,842	231	98,892	99,835	943
Surrey Public Library	13,219	13,773	13,897	124	18,847	18,777	(70)
Planning & Development	22,282	23,527	23,459	(68)	32,633	31,985	(648)
Mayor & Council	1,141	1,131	1,214	83	1,737	1,737	
City Grants	938	1,067	1,590	522	1,758	1,758	()
City Manager	853	803	951	148	1,245	1,295	50
Invest. & Intergovernmental Relations	916	896	1,169	273	1,493	1,598	105
Finance	7,564	7,496	8,063	566	10,562	11,028	466
Corporate Services	31,741	32,858	33,112	254	45,113	44,970	(143)
TOTAL PROGRAM EXPENDITURES	324,674	336,663	340,352	3,689	461,162	461,901	780
NET PROGRAM	2018: 3rd Qtr YTD ACTUAL	2019: 3rd Qtr YTD ACTUAL	2019 YTD BUDGET	2019: 3rd Qtr YTD Variance	2019 Projected ACTUAL	2019 ANNUAL BUDGET	2019 Projected Variance
Policing Transitioning	16,382	17,145	17,536	390	24,040	24,349	310
RCMP Contract	99,768	103,449	104,120	671	138,356	138,827	471
Fire	44,043	45,251	46,006	755	65,192	65,221	29
Engineering Services	1,372	1,034	2,334	1,300	1,563	2,461	898
Parks, Recreation & Culture	42,510	45,113	45,834	721	64,629	64,789	159
Surrey Public Library	12,023	12,356	12,693	337	17,182	17,182	-
Planning & Development	3,537	4,573	6,735	2,161	6,088	9,687	3,599
Mayor & Council	1,141	1,131	1,214	83	1,737	1,737	
City Grants	938	1,067	1,590	522	1,758	1,758	()
City Manager	853	801	949	148	1,243	1,293	50
Invest. & Intergovernmental Relations	916	877	1,169	293	1,473	1,598	125
Finance	6,600	6,566	6,991	425	9,274	9,599	325
Corporate Services	24,389	25,559	26,025	466	35,320	35,595	275
NET PROGRAM TOTAL	254,474	264,922	273,195	8,273	367,855	374,096	6,241