

REGULAR COUNCIL

TO: **Mayor & Council**

DATE: **October 12, 2023**

FROM: **General Manager, Finance**

FILE: **1880-20**

SUBJECT: **Quarterly Financial Report - Third Quarter – 2023**

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 for the first three quarters of 2023 and to compare this activity relative to the 2023 Financial Plan.

DISCUSSION

The following discussion provides a summary of the current economic environment including key economic factors globally, nationally, provincially, and within the City, followed by an outline of Surrey's financial performance through the first three quarters of 2023, in comparison to the Five-Year (2023-2027) Financial Plan which was adopted by Council on April 17, 2023.

Economic Environment and Key Economic Factors

International Overview

Central banks worldwide have put conditional pauses on interest rate increases. Some central banks have increased their rates after a period of pause due to persistently "sticky" inflation. In September, 10 central banks, which oversee the most heavily traded global currencies, held monetary policy meetings. Three of these central banks increased their key interest rates by a cumulative 0.75%. The Federal Reserve ("Fed"), Bank of England, along with central banks in Australia, Canada, and Japan, opted for no changes in their benchmark interest rates. Due to inflation coming down slower than anticipated, central banks are warning consumers and businesses to expect higher interest rates for a longer period of time.

The International Monetary Fund ("IMF") revised its economic forecast in July. Global economic growth is now forecasted at 3.00%, an upward revision of 0.2% from April's estimate. The IMF now expects to see the United States' ("US") economy advancing by 1.80%, China growing by 5.20%, and an expansion of 1.70% and 0.90% for Canada and the Eurozone, respectively. For 2023, the IMF is

forecasting global inflation to come in at 6.80% and then trend downwards to reach 5.20% in 2024. The Fund is urging central banks to communicate clearly on their inflation outlooks and monetary policies. The IMF warns that expectations of inflation are perpetuating higher inflation.

Israel declared that it was at war in response to a series of recent attacks by Hamas, the Palestinian group that governs Gaza. This latest conflict in the Middle East presents the potential to upend a fragile global economy that is still finding its path forward through the lingering effects of the COVID-19 pandemic and ongoing impacts of Russia's war in Ukraine. Oil markets are already considered apprehensive, and analysts will be watching this latest conflict closely as any spread in hostilities throughout the region could cause a spike in energy prices. Additional increases in oil prices would pressure the world's central banks to further push up interest rates, which would only complicate the ongoing battle against inflation.

United States Overview

The US Federal Reserve opted to keep the range for its benchmark interest rate at 5.25% to 5.50% in September, the highest in some 22 years, following a 0.25% hike in July. The Fed is projecting inflation to fall to 3.30% by the end of this year, drop further to 2.50% next year, and then reach its targeted goal of 2.00% by 2026. The core inflation rate, which excludes volatile food and energy prices, is expected to fall to 3.70% by the end of 2023.

The US central bank signalled that another rate hike is possible this year depending on whether inflation decelerates as much as expected. The Fed further forecasted an interest rate cut of 0.50% next year due to an economic slow down and declining inflation rate. US unemployment remains low, coming in at 3.80% in September with 336,000 jobs added, surpassing economists' estimates. Strong employment growth indicates that the US economy remains resilient despite rising interest rates.

The Fed is forecasting US Gross Domestic Product ("GDP") to grow by 2.10% this year and 1.50% next year. The unemployment rate is forecasted to peak at 4.10% next year. Based on the Fed's outlook, elevated interest rates are expected to remain for some time still as the central bank is not forecasting its first interest rate cut until the second half of 2024. The US dollar index has risen 6.90% since the middle of July. The US economy's recent strong performance has prevented a decline in the dollar, and if the economic environment remains supportive, the currency is expected to strengthen further.

Canadian Overview

The Bank of Canada ("BOC") kept its key interest rate at 5.00% in September after increases of 0.25% at both its June and July meetings. The central bank noted that the economy has shown weaker growth, however, BOC stands ready to raise its benchmark interest rate again should inflationary pressures persist. The higher interest rates have weighed down on economic growth. Canada's GDP in July was unchanged from the prior month's result. According to Statistics Canada's preliminary estimates, August GDP grew by a modest 0.1%.

Canada's inflation rate increased to 4.00% in August, up from July's rate of 3.30%. Inflation in grocery prices rose by 6.90%, outpacing headline inflation. The central bank is voicing concerns that inflation remains "sticky" and warns that firms are increasing prices at a faster and more frequent rate than prior to the pandemic. This trend continues to be persistent domestically and

internationally. The BOC warns higher labour costs, along with financing costs, are also contributing to the need for businesses to raise their prices.

In September, Canada's unemployment rate remained at 5.50%, for the third month in a row, with 64,000 jobs added. Average hourly wages in September increased by 5.00% from the prior year. Economists caution that strong job numbers in September are mainly driven by increases in seasonal and part-time employment growth.

British Columbia Overview

British Columbia ("BC") is experiencing an extremely destructive wildfire season this year. With approximately 28,500 square kilometers burned so far, the Province has more than doubled the previous record for area burned during a single wildfire season. The provincial government has spent more than \$1.0 billion on fire fighting efforts.

The government is forecasting a budget deficit of \$6.7 billion this year due to lower natural gas royalties and increased wildfire costs. Despite the large, forecasted deficit, the government is not planning to reduce services, implement new fees or cut taxes to balance the budget.

The high cost of living is expected to pose headwinds for BC's economy. The provincial government is projecting the economy to grow by 1.20% this year with growth forecasted at 0.80% in 2024. The government noted that uncertainty surrounding higher interest rates, weaker global demand and inflationary pressures are expected to slow economic growth.

The BC unemployment rate came in at 5.40% in September, up 0.20% from the prior month, with 25,700 jobs added. The construction sector had the largest growth in jobs while the food services and accommodation sectors had the most job losses. BC's annual inflation increased to 3.80% in August, up from July's rate of 3.00%, with higher gasoline and food prices as key contributors to the growth in the provincial Consumer Price Index ("CPI").

The BC government announced that allowable rent increases for the next year will be capped at 3.50%, which it feels balances the need to protect renters and help landlords who are facing increased costs. As inflation slowly returns to normal levels, the government intends to tie allowable rent increases to the CPI in future years.

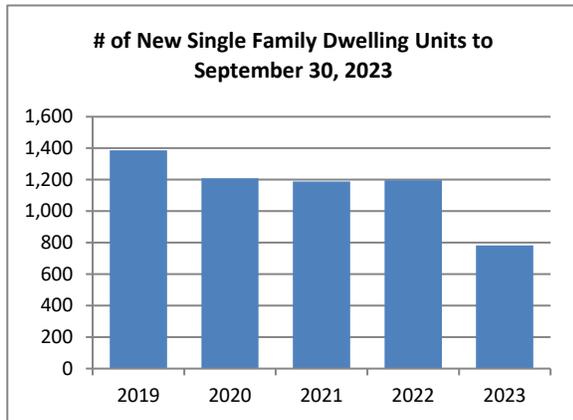
City of Surrey Overview

In the residential development category, the City has seen a decrease in construction of new single-family dwelling units, whereas multi-family development activity, especially low-rise apartments, has remained strong in this nine-month period as compared to the same period in 2022. In the non-residential development category, as compared to last year, the City has seen a decrease in the number of permits in the Industrial, Commercial & Institutional ("ICI") development segment.

Overall, rising interest rates and the resulting increase in financing costs have had a cooling effect on real estate construction in the region. This has resulted in a moderate slowdown in overall development permit activity in the City.

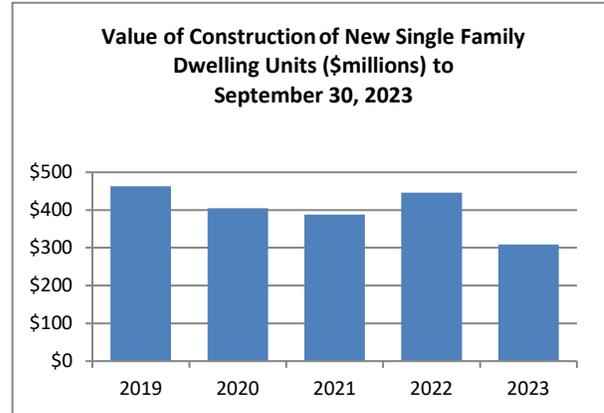
City of Surrey's Key Performance Indicators

The following graphs show data for the first nine months of 2023 compared to previous years.



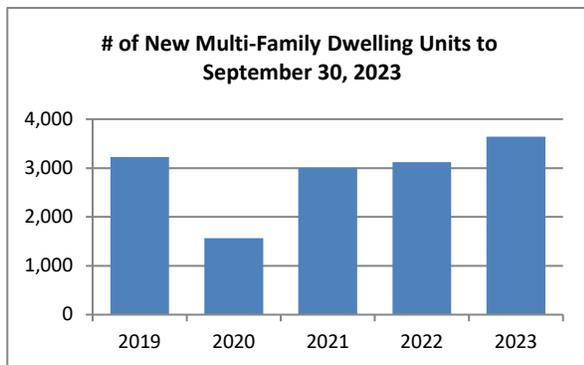
Graph 1

Due to a continued shift in residential development activity from single-family to multi-family, new single family dwelling units have declined by 35% in this nine-month period, as compared to the same period in 2022.



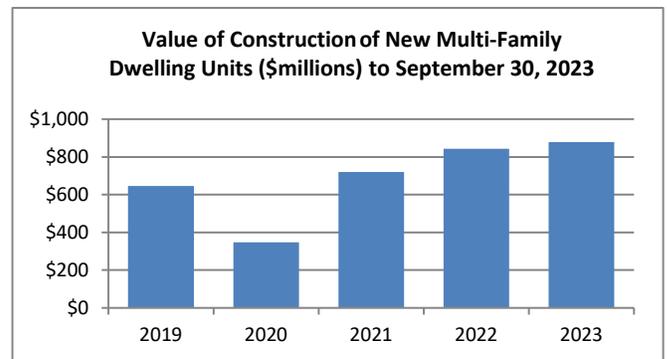
Graph 2

Due to a decline in the number of permits issued for new single-family dwelling units in this nine-month period as compared to the same period last year, the value of construction of these units has correspondingly decreased by 31% when compared to the same period last year.



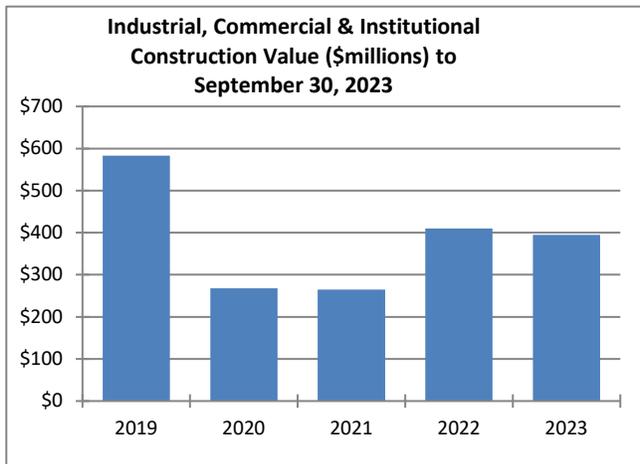
Graph 3

As discussed above, there has been an overall increase in development activity in multi-family residential projects. This nine-month period has seen an increase in permits for multi-family dwelling units of 17%.



Graph 4

Consistent with an increase in the number of permits issued for new multi-family dwelling units in this nine-month period as compared to the same period last year, the value of construction for these units has increased by 4% when compared to the same period last year.



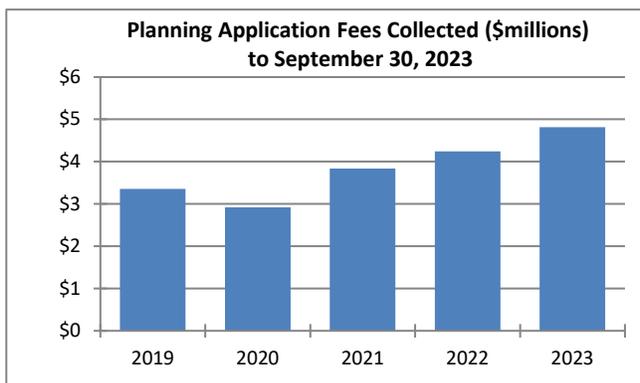
Graph 5

Construction value of ICI permits for the first nine months of 2023 is lower by 4% as compared to the same period in 2022.



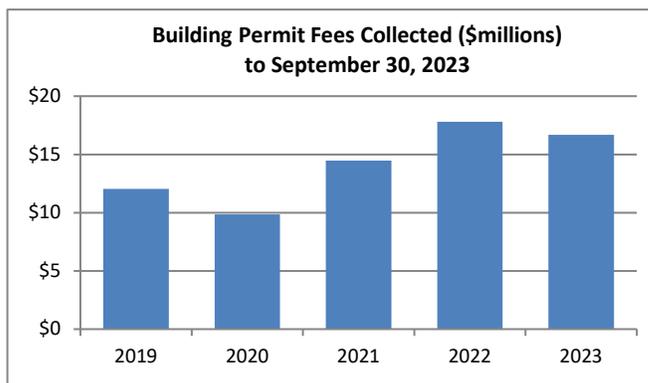
Graph 6

Due to a moderate slowdown in overall development permit activity in the City, year-to-date building construction values associated with multi and single-family residential projects, along with ICI projects, has declined by 7% as compared to the same period last year.



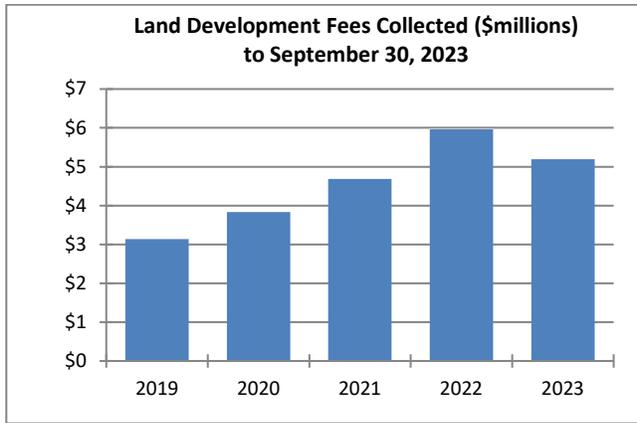
Graph 7

Despite a moderate slowdown in overall development permit activity, the City continues to see an increase in demand for future development projects in the City, resulting in planning application fees collected in the first nine months of the year being 14% higher than those collected in the same period last year.



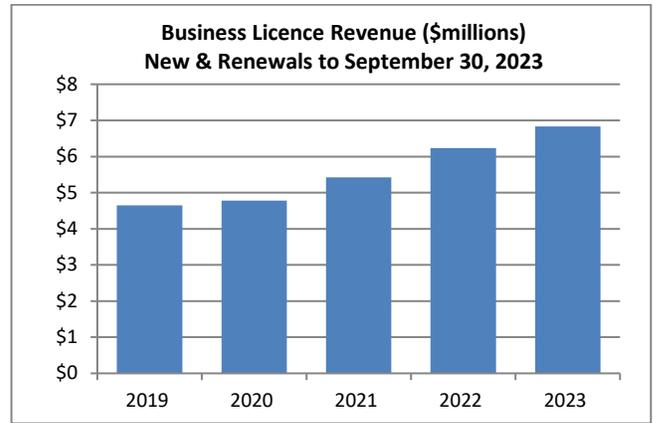
Graph 8

Since the total building construction value in the City year-to-date has decreased by 7% as compared to the same period last year (as reflected in Graph 6), building permit fees collected in this nine-month period have decreased by 6% as compared to the same period last year.



Graph 9

Land Development fees collected during the first nine months of 2023 are lower by 13% as compared to the same period in 2022. Overall, this pace of fee collection is consistent with the average land development fees collected in the first nine months of the four preceding years.

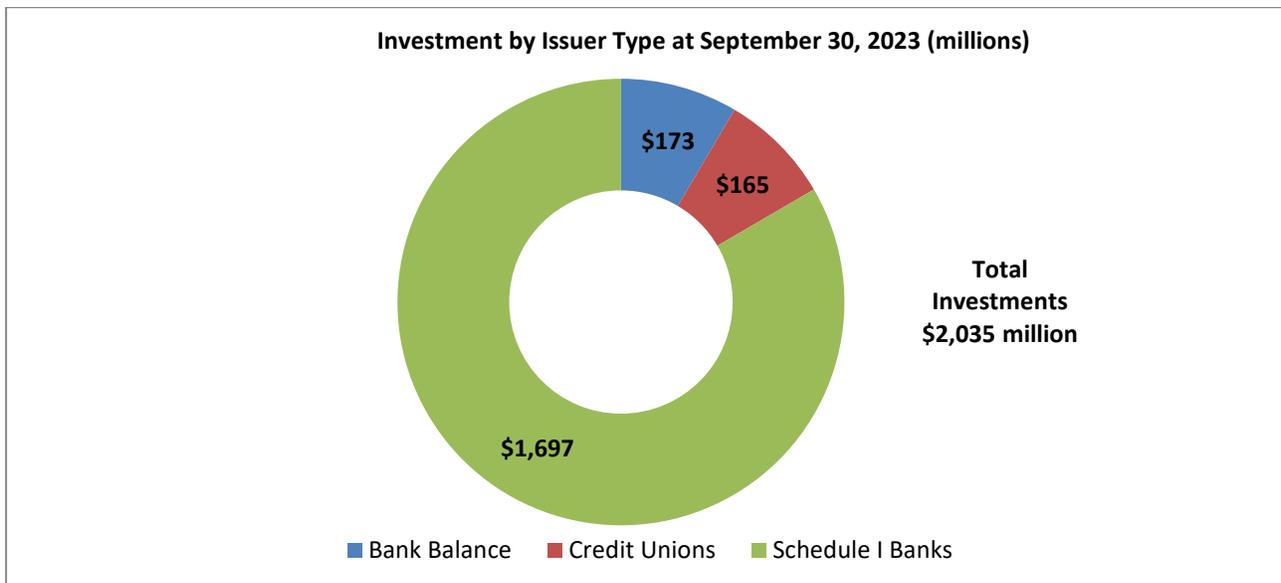


Graph 10

Consistent with increases over the last few years, business licence revenue in the first nine months of 2023 increased by 10% as compared to the same period last year. This increase aligns with a 11% increase in the number of businesses paying for business licences in Surrey in this nine-month period as compared to 2022.

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 \$2,035 million. Most of these funds have either been committed to specific capital projects or are funds that have been invested until they are needed to pay current operating expenses. Graph 11 shows the City’s Investment Portfolio by issuer type.



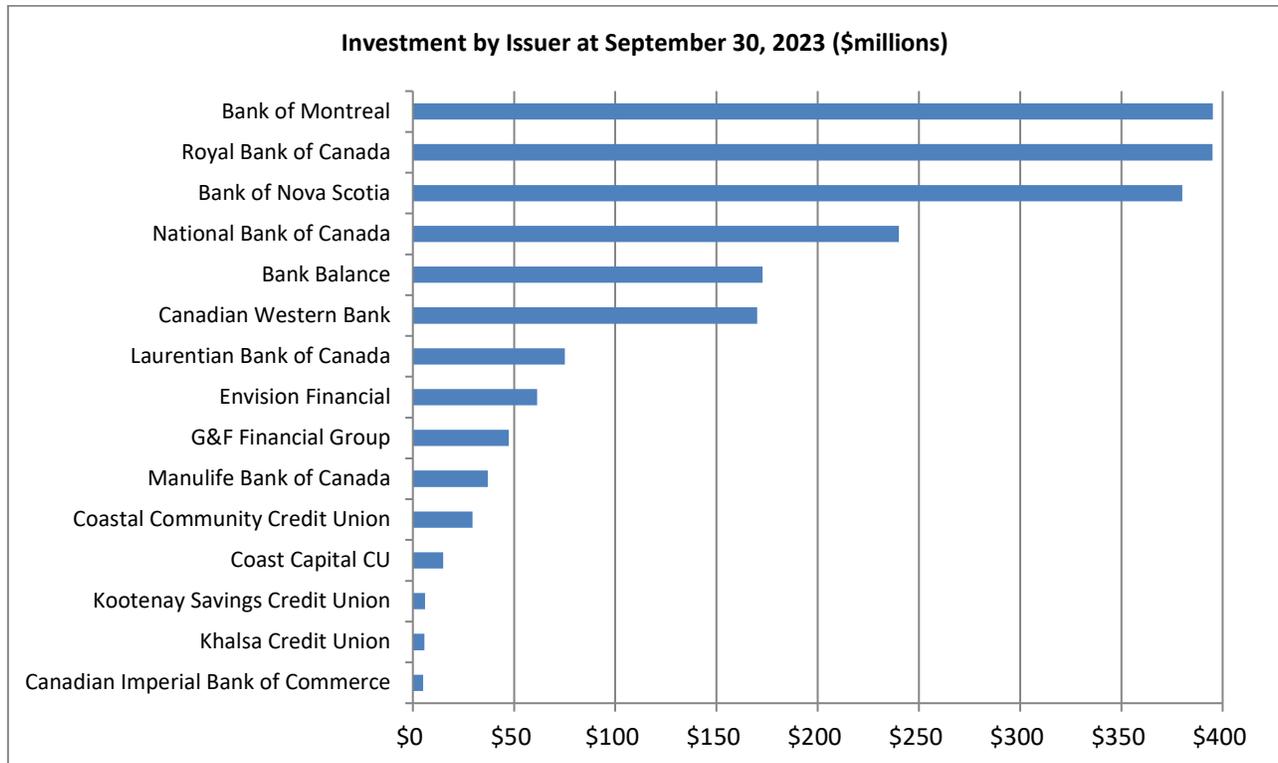
Graph 11

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

Objectives of the Policy include:

Diversification

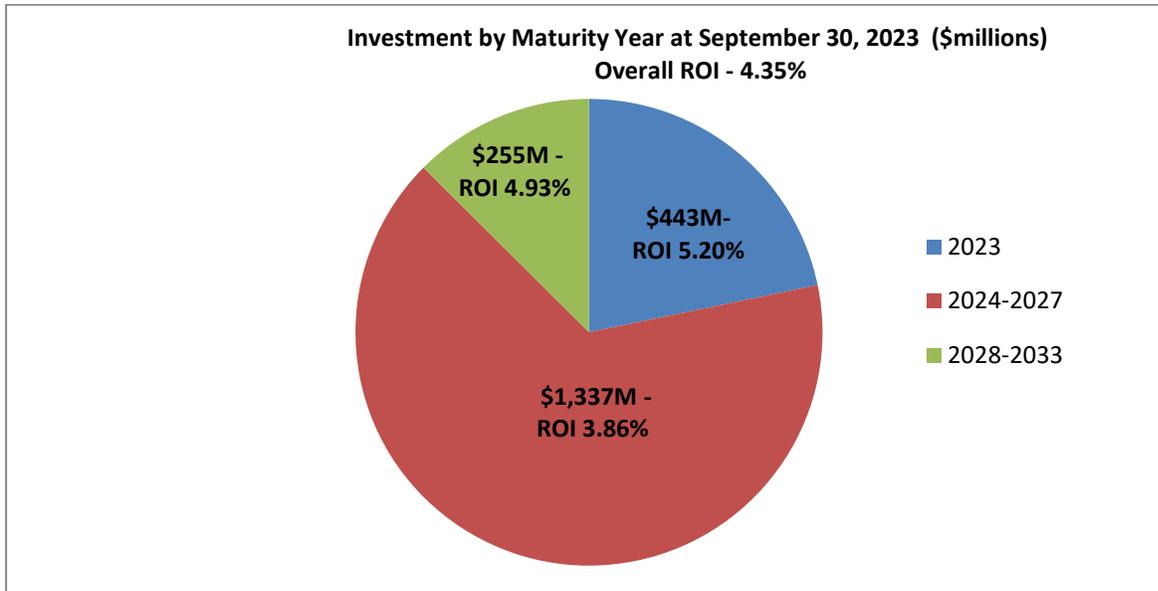
In order to reduce overall portfolio risk, the City diversifies its investment holdings across a range of security types and financial institutions. Graph 12 shows a listing of the City's portfolio by Financial Institution.



Graph 12

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. The investment portfolio is managed through the laddering of investment maturities to account for the timing of cashflow demands. The City's forecasted cash balances are currently in a healthy position with efforts ongoing to remain prepared as new information is incorporated into the cashflow forecast. In the event the City's cash flow requirements change drastically, we are well positioned to add liquidity as necessary. Graph 13 shows the portfolio by maturity terms.



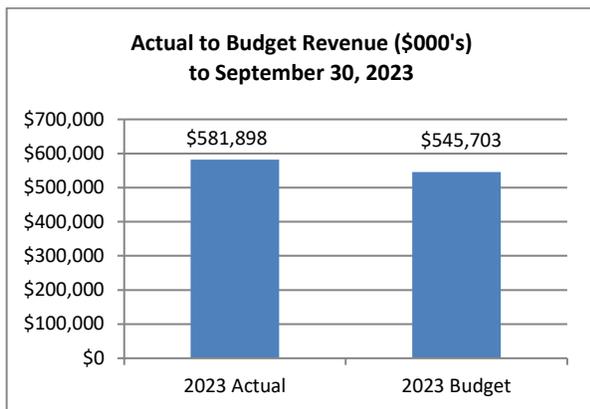
Graph 13

Return on Investment

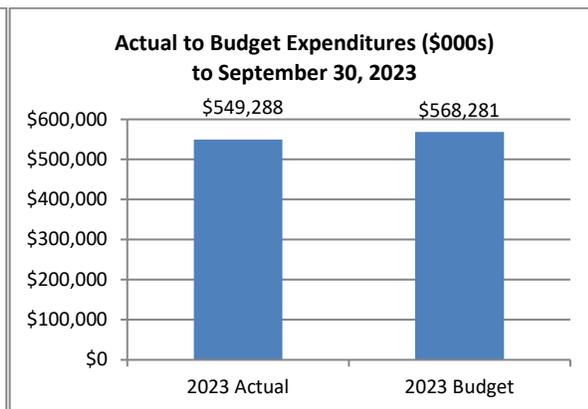
During the nine-month period ending September 30, 2023, the City’s investment portfolio earned a combined rate of approximately 4.35% (during the nine-month period ending September 30, 2022 – 2.18%) while maintaining investment security as outlined in the City’s investment policy. The City strives to 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 Budget (Financial Plan)

The following graphs illustrate the variances between the actual and the budgeted operating revenues and expenditures respectively, excluding transfers, for the first three quarters of 2023.



Graph 14



Graph 15

Appendix “I” documents the General Operating Fund’s revenues and expenditures at the end of the third quarter of 2023 at a more detailed level. Departments are proactively monitoring their actual results on a monthly basis. The following section provides an explanation on a Department-by-Department basis of year-to-date variances in relation to the 2023 budget and as shown in Appendix “II”.

Policing Services

In July 2023, the BC Minister of Public Safety and Solicitor General directed that the transition to the Surrey Police Service (“SPS”) continue. The Minister also appointed a strategic implementation advisor to aid all parties on the transition to the SPS. The Province has recommitted to providing the City with at least \$150 million to help offset the additional costs associated with the transition to the SPS, however, to date no funding from the Province has been received. The City is currently working with all parties to determine next steps and details as there are a number of unresolved issues related to the Minister’s decision.

In relation to the third quarter adopted budget for Policing Services, the following is the variance for each of the three components:

- **City Police Support Service** currently has a favourable variance of \$1.77 million primarily due to revenue from security clearance fees being higher than the budget and timing of expenditures. In addition, an amount of \$83.0 million at the end of the third quarter has been earmarked for future policing transition costs, this would be inclusive of fiscal 2023 and all future years.
- **Surrey Police Service** (“SPS”) has an unfavourable variance relative to budget of \$2.48 million at the end of this third quarter. The SPS 2023 budget was based on salaries and operating costs for SPS staffing and operations only until such time that the RCMP was the sole policing services provider for the City.
- **RCMP Contract** currently has a favourable variance of \$19.68 million due predominately to the fact that the RCMP was budgeted for a funded strength of 759, excluding integrated teams, but is currently staffed at lower than the budgeted strength.

It is imperative to highlight that there are still numerous and significant uncertainties regarding the financial requirements the City will need to expend on a go forward basis to finalize the policing transition. Staff will proactively monitor and incorporate new information as it becomes available and provide Council with updates as deemed necessary.

Fire Department currently has a favourable variance of \$3.29 million primarily resulting from the timing of the hiring of an approved 20 additional positions in 2023 and the timing difference associated with dispatch revenues.

Engineering Services-General Operating currently has a favourable variance of \$1.62 million, primarily due to higher-than-expected land development revenues, staff vacancies and the timing of expenditures.

Parks, Recreation & Culture (“PRC”) Department currently has a favourable variance of \$1.95 million. This is primarily due to vacancies, higher than expected facility rental revenues and unbudgeted grants received from another level of government. Timing of expenditures is also a contributing factor for the variance.

Surrey Public Library currently has a favourable variance of \$55,000, due to timing of operating costs and savings from vacancies.

Planning & Development Department which also includes Civic Facilities, currently has a favourable variance of \$4.11 million. Since Planning & Development revenues are recognized up to a two-year period, permit, inspection, and application-based revenues in this year are favourable due, in part to, better-than-expected permit and planning application fees collected in 2021/2022 that are, in part, being recognized as revenue in 2023.

Mayor and Council has a favourable variance of \$0.11 million, resulting from timing of expenditures and savings in operating costs.

City Grants have a favourable variance of \$0.18 million, resulting from timing differences.

City Manager's Department has a small favorable variance of \$15,000.

Community Services Department has a favourable variance of \$1.09 million primarily due to timing of operating costs and savings from vacancies.

Investment & Intergovernmental Relations Department has a small favorable variance of \$13,000.

Finance Department currently has a favourable variance of \$1.40 million, primarily due to the timing of expenditures and savings from vacancies.

Corporate Services Department has a favourable variance of \$1.28 million due to better-than-expected business license revenues, timing of expenditures and savings from vacancies.

CONCLUSION

As presented in this report, the City's financial performance relative to the adopted General Operating Budget for the third quarter of 2023 is relatively strong. City departments continue to proactively manage their respective budgets to ensure the financial position of the City for the remainder of the year remains strong and the City collectively meets budget at year end.

Kam Grewal, CPA, CMA
General Manager, Finance

Appendix "I": 2023 Third Quarter Council Report, Executive Summary - Revenues & Expenditures
Appendix "II": 2023 Third Quarter Council Report, Departmental Detail

Appendix "I"

2023 3rd QUARTER COUNCIL REPORT EXECUTIVE SUMMARY - REVENUES & EXPENDITURES

\$ 000's

REVENUE SUMMARY	2023: 3rd Qtr YTD Actual	2023 YTD BUDGET	2023: 3rd Qtr YTD Variance	2023 ANNUAL FORECAST	2023 ANNUAL BUDGET	2023 Projected Variance
Net Taxation	385,408	381,679	3,729	513,458	507,917	5,541
Secondary Suite Infrastructure Fee	24,551	20,656	3,895	28,431	24,931	3,500
Other Corporate Fees	3,077	3,300	(223)	4,575	4,400	175
Investment Interest	53,133	40,806	12,327	69,880	57,336	12,544
Provincial Casino Revenue Sharing	2,481	2,481	-	3,308	3,308	-
Carbon Tax Rebate	1,175	1,175	-	1,175	1,175	-
Other Trsf from Government	876	876	-	18,176	18,176	-
Penalties & Interest on Taxes	5,301	4,813	489	5,350	5,275	75
Corporate Leases	8,056	8,288	(231)	13,145	13,145	-
Non-Tax Revenues	98,650	82,394	16,256	144,040	127,746	16,294
Program Revenues	97,840	81,629	16,211	117,348	98,025	19,323
TOTAL REVENUES	581,898	545,703	36,196	774,845	733,688	41,157
EXPENDITURE SUMMARY	2023: 3rd Qtr YTD Actual	2023 YTD BUDGET	2023: 3rd Qtr YTD Variance	2023 ANNUAL FORECAST	2023 ANNUAL BUDGET	2023 Projected Variance
Program Expenditures, net of transfers	520,457	538,331	17,874	682,681	682,153	(528)
Council Priorities	106	195	89	260	260	-
Fiscal Services	(164)	125	289	(122)	167	289
Debt Interest & Principal	27,651	27,651	-	31,243	31,243	-
Other	1,238	1,979	741	19,822	23,063	3,241
TOTAL EXPENDITURES	549,288	568,281	18,992	733,885	736,886	3,001
CORPORATE TRANSFER SUMMARY	2023: 3rd Qtr YTD Actual	2023 YTD BUDGET	2023: 3rd Qtr YTD Variance	2023 ANNUAL FORECAST	2023 ANNUAL BUDGET	2023 Projected Variance
Transfer to /(from) Operating Sources	(13,594)	(13,594)	-	(18,074)	(18,074)	-
Transfer to /(from) Capital Sources	(13,616)	(15,435)	(1,819)	(13,616)	(15,435)	(1,819)
Transfer to /(from) Reserve Sources	11,318	11,247	(71)	15,067	14,996	(71)
Transfer to /(from) Surplus	9,181	11,342	2,161	13,464	15,315	1,851
TOTAL TRANSFERS	(6,710)	(6,439)	271	(3,159)	(3,198)	(39)
Surplus (Deficit)	39,320	(16,139)	55,459	44,120	-	44,120
Trsf (To)From Unapprop Surplus	(39,320)	16,139	(55,459)	(44,120)	-	(44,120)
BALANCED BUDGET	-	-	-	-	-	-
ANTICIPATED SURPLUS (DEFICIT) AT YEAR END						\$ 44,120

Appendix "II"

**2023 3rd QUARTER COUNCIL REPORT
DEPARTMENTAL DETAIL
\$ 000's**

	2023: 3rd Qtr YTD ACTUAL	2023 YTD BUDGET	2023: 3rd Qtr YTD Variance	2023 Projected ACTUAL	2023 ANNUAL BUDGET	2023 Projected Variance
PROGRAM REVENUES						
City Police Support Service	7,255	6,561	693	8,682	8,082	600
Surrey Police Service	-	-	-	-	-	-
RCMP Contract	-	-	-	-	-	-
Fire	5,040	4,236	804	4,414	3,991	423
Engineering Services	9,698	8,290	1,408	10,591	8,946	1,645
Parks, Recreation & Culture	27,322	26,300	1,021	35,624	35,211	413
Surrey Public Library	1,198	1,044	153	1,509	1,386	123
Planning & Development	30,268	25,695	4,573	34,911	28,258	6,653
Mayor & Council	-	-	-	-	-	-
City Grants	-	-	-	-	-	-
City Manager	-	-	-	-	-	-
Community Services	6,844	-	6,844	8,727	-	8,727
Invest. & Intergovernmental Relations	-	-	-	-	-	-
Finance	1,149	1,093	56	1,497	1,462	35
Corporate Services	9,067	8,410	657	11,393	10,689	704
TOTAL PROGRAM REVENUES	97,840	81,629	16,211	117,348	98,025	19,323

	2023: 3rd Qtr YTD ACTUAL	2023 YTD BUDGET	2023: 3rd Qtr YTD Variance	2023 Projected ACTUAL	2023 ANNUAL BUDGET	2023 Projected Variance
PROGRAM EXPENDITURES NET OF TRANSFERS						
City Police Support Service	107,795	108,868	1,073	123,186	124,071	885
Surrey Police Service	50,825	48,350	(2,475)	72,169	48,751	(23,418)
RCMP Contract	102,031	121,711	19,680	138,041	165,225	27,184
Fire	56,339	58,820	2,481	78,275	79,467	1,192
Engineering Services	10,855	11,062	207	13,898	13,968	70
Parks, Recreation & Culture	82,276	83,208	932	109,141	110,651	1,510
Surrey Public Library	17,244	17,147	(98)	22,815	22,692	(123)
Planning & Development	28,187	27,723	(465)	36,934	36,389	(545)
Mayor & Council	1,507	1,617	110	1,962	2,123	161
City Grants	701	884	184	1,179	1,179	-
City Manager	1,291	1,306	15	1,703	1,712	9
Community Services	8,720	2,965	(5,755)	12,048	3,921	(8,127)
Invest. & Intergovernmental Relations	1,551	1,564	13	1,972	2,050	78
Finance	10,281	11,629	1,347	14,859	15,443	584
Corporate Services	40,853	41,478	625	54,500	54,511	11
TOTAL PROGRAM EXPENDITURES	520,457	538,331	17,874	682,681	682,153	(528)

	2023: 3rd Qtr YTD ACTUAL	2023 YTD BUDGET	2023: 3rd Qtr YTD Variance	2023 Projected ACTUAL	2023 ANNUAL BUDGET	2023 Projected Variance
NET PROGRAM						
City Police Support Service	100,540	102,307	1,766	114,504	115,989	1,485
Surrey Police Service	50,825	48,350	(2,475)	72,169	48,751	(23,418)
RCMP Contract	102,031	121,711	19,680	138,041	165,225	27,184
Fire	51,299	54,584	3,285	73,861	75,476	1,615
Engineering Services	1,157	2,772	1,615	3,307	5,022	1,715
Parks, Recreation & Culture	54,954	56,908	1,954	73,517	75,440	1,923
Surrey Public Library	16,047	16,102	55	21,306	21,306	-
Planning & Development	(2,081)	2,028	4,109	2,023	8,131	6,108
Mayor & Council	1,507	1,617	110	1,962	2,123	161
City Grants	701	884	184	1,179	1,179	-
City Manager	1,291	1,306	15	1,703	1,712	9
Community Services	1,876	2,965	1,089	3,321	3,921	600
Invest. & Intergovernmental Relations	1,551	1,564	13	1,972	2,050	78
Finance	9,133	10,536	1,403	13,362	13,981	619
Corporate Services	31,785	33,068	1,283	43,107	43,822	715
NET PROGRAM TOTAL	422,617	456,701	34,085	565,334	584,128	18,794