1969

QUÉBEC DEPOSIT AND INVESTMENT FUND

FOURTH ANNUAL REPORT

Bodies authorized by an act of the provincial legislature to deposit moneys with the Québec Deposit and Investment Fund

Québec Agricultural Marketing Board
Québec Crop Insurance Board
Québec Deposit Insurance Board
Québec Pension Board

Legal Deposit — 1st quarter 1970
Québec National Library

QUÉBEC DEPOSIT AND INVESTMENT FUND

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1969

Board of Directors

as at December 31, 1969

Claude Prieur, *Chairman*
General Manager,
Québec Deposit and Investment Fund

Robert De Coster, *Vice-Chairman*
President,
Québec Pension Board

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Economic Advisor to the Cabinet,
Government of Québec

Marcel Cazavan*
Deputy Minister of Finance,
Government of Québec

Raymond Lavoie
Associate General Manager,
Crédit Foncier Franco-Canadien

E.-A. Lemieux*
General Manager — Finance and Accounting
Hydro-Québec

Charles B. Neapole
President,
Montreal Stock Exchange and
Canadian Stock Exchange

Roland Parenteau
Director,
Ecole Nationale d'Administration,
Université du Québec

Marcel Pepin
National President,
Confederation of National Trade Unions

Maurice Turgeon*
Vice-President,
Québec Municipal Commission

**Associate member*

Management

Claude Prieur, *General Manager*

Investment Department

Bonds

Gérard H. Cloutier, *Manager*
Jean-Michel Paris, *Associate Manager*
Jean C. Lavoie, *Assistant Manager*
Jean Laflamme, *Assistant Manager*

Stocks

Pierre Arbour, *Manager*
Etienne de Kosko, C.F.A., *Associate Manager*

Real Estate and Mortgages

Patrick O. Wells, *Manager*

Treasury Department

Jean-Marie Côté, C.A., *Treasurer*

Secretariat

Gérard J. Blondeau, C.ADM., *Secretary*

Law Department

Paul Martel, LL.L., *Legal Counsel*

Québec Deposit and Investment Fund

CLAUDE PRIEUR
CHAIRMAN OF THE BOARD
AND GENERAL MANAGER

Québec City, March 4, 1970

The Honourable Mario Beaulieu,
Minister of Finance,
Government of Québec.

Dear Sir:

In accordance with the provisions of the charter of the Québec Deposit and Investment Fund, I am transmitting herewith our fourth annual report for the year ended December 31, 1969.

As required under Section 41 of the charter, this report comprises an outline of investment policy, a summary of our activities and statements of accounts duly verified by the Provincial Auditor, along with related statistical data.

Yours very truly,

Claude Prieur

Report of management

During the year ended 31st December 1969, the assets of the Québec Deposit and Investment Fund increased from $683,932,828 to $990,383,601 and the income for this fourth year of operation reached $55,825,222 compared with $35,306,683 for the preceding year.

1969 in retrospect

The year was characterized by marked weaknesses in both the bond market and the stock market. The bond market remained under the influence of the inflationary psychosis and the skepticism of the investor regarding the effectiveness of restrictive fiscal and monetary measures. The decline in the stock market was due to several factors, principally the probable repercussions on future company earnings of higher production costs, including labour, the slower rate of growth of productivity and the effect on companies of the anti-inflationary measures taken by governments.

Within the framework of a concerted strategy aimed at relieving pressure on prices and costs, the Canadian fiscal and monetary authorities applied throughout the year a series of restrictive measures that had the effect of slowing the rate of economic growth. These measures, however, did not produce all the expected results as quickly as anticipated, and the bond market continued to deteriorate.

During the first half of the year, there was a succession of increases in bank rate and prime rate which paralleled a similar trend in the United States. During the second half of the year, the chartered banks were subjected as of the 1st of June to the maintenance of higher secondary reserves. The monthly rate of increase in the money supply was reduced progressively from an average level of 13.8% during the first six months to 5.6% in December. Monetary restrictions thus acted initially on the level of interest rates and eventually more directly on the availability of credit.

In fiscal matters, the Federal Government proposed a policy of austerity.

In the spring budget, the Minister of Finance announced the extension of the 3% surtax on income and also proposed regional restrictive measures by deferring capital cost allowances on certain new construction in the provinces of Ontario, Alberta and British Columbia. Moreover, on the 13th of August, significant cuts were announced in Federal Government spending including a reduction in Civil Service establishment. Finally, at year end, the Federal Government forecast a greater budgetary surplus and indicated its willingness to consider other restrictive regional measures and the possibility of controls on consumer credit.

These fiscal and monetary measures, together with serious union conflicts, had a marked effect on economic activity. The most recent statistics available indicate a significant slowdown in the growth of the gross national product in real terms, of industrial production, of productivity and of corporate earnings. Moreover, foreign trade in 1969 did not play as dynamic a part as it did during the preceding year.

The concomitant presence of inflationary pressures and of a relatively high rate of unemployment in Canada is explained in part by regional factors. Indeed the accelerated growth of the last few years and the inflationary pressures proved to be more pronounced in certain regions. Québec has often been among those provinces suffering from such disparities. Although economic growth in real terms in Québec compares not unfavourably with the national average, the Province has felt rather severely the consequences of the stabilizing measures adopted in 1969 by the Federal Government.

Investment policy

At the beginning of 1969, an investment program of the order of $300 million was formulated in the light of the then existing economic outlook. Although market conditions during the year led to revision of this investment program, it was nevertheless possible to adhere, in the main, to original goals.

This year again, an appreciable part of the available funds was allocated to the acquisition of bonds issued or guaranteed by Québec. The role thus played by the Fund was particularly useful because of the critical state of the market from time to time during the year. The Fund understandably invests a larger proportion of its assets in this type of investment than do most private investment firms. This is the result of the interplay of many factors, some of which acquire a greater importance in prolonged periods of tight money. Particularly, it must be remembered that all the provinces of Canada other than Québec receive and use for their own purposes the full amount of the funds accumulated by the universal pension plan. In Québec, on the other hand, these monies are remitted to the Fund and only that part which is used to purchase Government bonds (and that, at current market rate) becomes available to the Government for its investment program. The Fund is also aware that today, the adequate financing of Government has become essential to the maintenance of a satisfactory level of economic activity in many sectors of private enterprise.

The net annual amount allocated by the Fund to the acquisition of bonds issued or guaranteed by Québec and of municipal and school bonds, has increased each year. Nonetheless, the allocation by the Fund of such relatively large amounts to investments in the public sector has not prevented it from making significantly large investments in the private sector. In fact, investments in the private sector represent from year to year an increasing percentage of the portfolio of the Fund; at year end, they accounted for more than one quarter of long-term investments and amounted, including commitments, to $272 million.

One of the fundamental goals of the investment policy of the Fund is to favor those investments likely to stimulate the economy. Although it is not the prime responsibility of the Fund to initiate alone projects related to economic development and in this way to supplant private initiative, the Fund is nonetheless able to foster and even render possible those projects which are deemed to be beneficial to the economy of the Province. This task might seem relatively simple at first glance but in addition to the economic and social advantages that a project may promise, it must also be financially viable. If it is true that the economy of Québec has a growing need for capital, it is equally true that Québec requires an ever increasing supply of competent managerial talent. In this context, the Fund considers its investments in the educational system of the Province to be of prime importance because the creation of a qualified manpower pool is as paramount for the economy as the need for natural and financial resources.

The economic and financial consequences of the acquisition of securities in the market may be more or less direct depending on whether these securities are purchased at the time of a new issue or in the secondary market. In the first instance, such acquisitions are a direct injection of new capital in a company while in the second they constitute, initially at least, merely the substitution of one bondholder or shareholder for another. The Fund is aware of this distinction and has concentrated its purchases in the new issue market. During the year, the scarcity of such new issues of acceptable quality has prevented the Fund from doing as much as it would have wished in this sector.

In the mortgage and real estate field, the Fund has continued to give preference to long-term financing of new construction. The concentration of these investments in new construction has created employment and has helped to relieve the housing shortage. It is to be noted that the Fund, like most North American lending institutions, is now actively seeking an equity participation in one form or another in the projects that it finances. Such a trend represents an equity awareness in a field traditionally oriented to fixed interest securities.

Investment operations

Bond portfolio — Faced with the economic outlook that prevailed during 1969, most major financial institutions, the traditional purchasers of bonds, turned more and more from the long-term bond market to the money market and the stock market. Furthermore, at certain times during the year, Canadian borrowers found it impossible to tap the U.S. or European bond markets because of recurring market dislocations.

From the beginning of the year, it became increasingly evident that the fiscal and monetary authorities were resolutely engaged in combatting inflationary pressures, in spite of the unpopularity of the austerity measures which were indicated. In this economic climate, the Fund increased progressively that portion of its assets held in fairly liquid form so that, if need be, it could lend assistance to the public borrowers of Québec.

The constant maintenance of a strong liquid position during the year permitted a high degree of flexibility in investment operations. Thus, without in any way interfering with its operations in the private sector, the Fund was able to negotiate directly, in May, a $50 million loan to the Province and, in September a $25 million loan to Hydro-Québec. In these transactions, recourse was had to what were then unusual terms and which, while scrupulously respecting market conditions, did not unsettle the retail market for other public borrowers. Short-term investments of the Fund amounted to $54 million at December 31st, after having reached much higher levels during the year.

The Fund subscribed during the year to 63.1% of the $225 million of bonds issued or guarantted by the Government of Québec on the Canadian market. Such investments now amount to $559,468,000. The average return on these securities is 7.44% in comparison with 7.08% last year. The Fund also purchased $8,088,000 of bonds issued by universities, CEGEPs and hospitals, such bonds being guaranteed by Government grants.

In the same period the Fund purchased $28,807,000 of municipal and school bonds, an increase of approximately 50% over the previous year. In this category, a wide regional coverage was attained. This part of the portfolio amounted at year end to $89,656,000 and the yield had increased from 7.47% to 8.00%.

In the market for corporate bonds, the Fund acquired investments totalling $9,167,500 of which $3,768,000 were negotiated privately; furthermore, the Fund had commitments amounting to $11.5 million at year end. This part of the portfolio increased therefore, from \$37,564,000 to \$46,731,500 and the yield at year end was 7.38% compared with 7.19% the previous year.

In the fourth year of operations, the nominal value of the bond portfolio increased from \$577,744,000 to \$767,006,500 and the yield from 7.07% to 7.46%.

Stock portfolio — During 1969 stock markets in both Canada and the United States followed a downward trend which brought the Dow Jones Index from 943.75 to 800.36, and the Montreal Stock Exchange Composite Index from 185.99 to 179.50. This constituted declines of 15.2% and 3.5% respectively. The somewhat better performance of the Canadian exchanges was due largely to the recovery which followed the publication in November of the White Paper on proposals for Tax Reform. The proposed tax reform, if adopted, would allow shareholders of a large number of Canadian companies to recover, through tax credits, a substantial portion of the amounts of taxes paid by these companies to the Canadian Government. On the other hand, public utility stocks did not share in the market recovery because of the failure of the White Paper to deal with the possible refunding to shareholders of taxes collected by the Federal Government and remitted to the provinces. The stock portfolio of the Fund containing, as it does, substantial holdings of utility stocks was adversely affected by this uncertainty.

The prospect of unsettled markets during the year prompted the Fund to reduce its stock purchases in the early part of the period. Later, when stock prices had moved lower, the Fund accelerated its purchases. These weaker markets, which appear to be continuing into 1970, may provide an excellent opportunity to step up investments in high grade stocks having attractive growth prospects.

The stock portfolio amounted to 15.8% of total assets at the close of the period. If this percentage were to be raised to the maximum allowed under the charter of the Fund, that is to 30% of total assets, the increase should be programmed over a period of time to take advantage of market opportunities. The stock portfolio increased from $99,200,000 to $156,600,000 during the year. This increase was distributed evenly among the various industry groups without any great change in their relationship to the total value of the portfolio. Thus, of the six main groups in the portfolio, utilities (24.3%), financial institutions (18.1%) and mines and metals (13.5%), retained the same order of relative importance while the others, — consumer goods (13.6%), oil and gas (10.8%) and heavy industries (12.0%), — showed slight variations by comparison with last year. At the close of the period the cumulative surplus of market value over book value amounted to $9.0 million or 11.2% of the average value of the portfolio. The indicated dividend return on these investments is forecast at 3.53% of their book value.

Real estate and mortgages — With the close of the year, the Fund completed its second year of activity in real estate and mortgages. During 1969, the Fund continued to favour new construction, particularly in the field of lower cost rental housing. A large part of these investments was made with the guarantee of the Central Mortgage and Housing Corporation. In the field of industrial and commercial real estate investment, the Fund encouraged the construction of new plants in Québec in cooperation with large and medium-sized corporations. The Fund sought to spread its real estate and mortgage investments throughout the economic regions of Québec. Investments of this type stretch from Chandler to Hull and from Sherbrooke to Val d'Or and Chicoutimi.

In 1969, the mortgage market, throughout Canada, was very difficult as a result of monetary restrictions and the lack of funds in the hands of the traditional lenders. This led to frequent use of new patterns of lending with an equity or a revenue participation where formerly simple mortgages would have been acceptable.

At the close of the period the real estate and mortgage portfolio amounted to $29.9 million showing a return of 9.10% and outstanding commitments will result in the disbursement of an additional $30 million during 1970. It should be noted that the earned rate of this portfolio does not take into account the variable element of participating transactions.

At 31st December 1969, the aggregate of the portfolios of the Fund amounted to $976,017,252 and was constituted as follows: Government bonds 62.1%, municipal and school bonds 8.5%, corporate bonds 4.7%, stocks 16.0%, real estate and mortgages 3.1% and short-term securities 5.6%.

New legislation

On 13th June 1969, legislation was enacted to amend the charter of the Fund to describe more precisely certain classes of investment and to raise the allowable maximum for others. The need for these changes had become apparent in the light of actual practice. The law also widened the field of activity of the Fund by allowing it to receive on deposit, with the approval of the Lieutenant-Governor in Council, sums of money derived from a supplemental pension plan to which contributions are made by a school corporation or a body which derives more than one half of its resources from the consolidated revenue fund.

These new powers were stated more specifically and broadened by an amendment to the charter of the Fund assented to on 23rd of December 1969. This amendment was contained in an Act respecting supplemental pension plans established by collective agreement decrees. This law, the primary purpose of which is to entrust to the Québec Pension Board the administration of these pension plans, also provides that the contributions made and any other sums collected, will be entrusted to the Fund. The law further states that the Board shall have the power to delegate its authority concerning the administration of the patrimony.

The Fund is required to hold these investments separate from its own and to manage them in accordance with the law governing supplemental pension plans. The general investment policy is to be determined by the administrator of these plans who shall establish the pattern of distribution among various classes of investments.

The year's results

The gross income of the Fund expressed in terms of a rate of return on the average amount on deposit during the year increased from 6.45% in 1968 to 6.73% in 1969. The almost continual decline in the bond market which made this improvement in yield possible also led, on the other hand, to the acceptance of book losses on most sales of bonds made in the course of the Fund's trading operations. While these bond trades are in reality profitable because the proceeds of sales are reinvested at higher yields, they did involve the taking of book losses of $1,864,299 during the year. These book losses when offset against the profit on sale of stocks bring the accumulated net profit from sale of securities to $5,953,536, the figure appearing in the balance sheet.

The net earned rate of the Fund rose from 6.34% in 1968 to 6.63% in 1969 and the operating costs dropped from 0.12% to 0.10%.

The Fund accepts, according to the needs of its depositors, both demand and notice deposits. The average amount of demand deposits was $28.7 million during 1969. On these deposits interest was paid in the amount of $2,101,208 at a rate which fluctuated between 6.36% and 7.90% through the year while the average was 7.32% by comparison with 6.39% the preceding year. Notice deposits averaged $800.4 million in 1969 and the net income of $52,876,238, an amount equivalent to a rate of 6.61% compared with 6.33% the preceding year, was credited to the depositors. The Fund has therefore paid interest on all deposits at an average rate of 6.63% compared with 6.34% the preceding year.

The Board of Directors

During the year Mr. Michel-F. Bélanger was appointed to the Board to replace Mr. Jacques Parizeau whose term of office had expired.

Early in 1970, the terms of office of Mr. Roland Parenteau and Mr. Marcel Pepin having expired, Mr. Hervé Belzile and Mr. Louis Laberge were appointed to the Board.

The Board expresses its thanks to Messrs. Parenteau, Parizeau and Pepin for their valuable contribution to the direction and administration of the Fund.

Staff

At the close of the year, the Fund had a staff of 57 employees. The Board of Directors acknowledges the effective contribution of the staff to the results achieved and wishes to express its sincere thanks. The increased responsibilities devolving on the Fund and the continuous growth of its assets make it imperative to expand the staff with additional experienced portfolio managers and financial analysts.

On behalf of the Board of Directors,

Claude Prieur

Chairman.

Quebec City, March 4, 1970.

FINANCIAL STATEMENTS

Québec Deposit and Investment Fund

BALANCE SHEET
As at December 31, 1969

ASSETS

	1969	1968
Portfolio (book value)		
Bonds	$735 250 469	*$549 970 455*
Preferred shares	6 004 185	*4 745 695*
Common shares	150 631 320	*94 494 600*
Mortgages	25 499 045	*2 695 341*
Real estate	4 411 761	*1 141 232*
Short-term investments	54 220 472	*20 542 389*
	$976 017 252	*$673 589 712*
CURRENT ASSETS		
Cash on hand and in bank	$ 52 271	*$ 77 096*
Accrued interest	14 086 011	*10 040 725*
Dividends receivable	7 575	*40 520*
Accounts receivable	1 220	—
	$ 14 147 077	*$ 10 158 341*
OTHER ASSETS		
Fixed assets (less depreciation)	$ 217 027	*$ 177 659*
Guarantee deposits and prepaid expenses	2 245	*7 116*
	$ 219 272	*$ 184 775*
	$990 383 601	*$683 932 828*

(Note) Book value: investments in bonds, mortgages and depreciable real estate are taken at amortized cost while investments in common and preferred shares and land are taken at cost.

On behalf of the Board of Directors
Claude Prieur Robert De Coster

LIABILITIES

	1969	1968
Current liabilities		
Accounts payable	$ 66 969	*$ 64 991*
Commitment guarantees	99 971	*81 844*
Accrued interest on demand deposits	410 516	*445 113*
Interest payable on notice deposits	15 785 490	*10 010 281*
	$ 16 362 946	*$ 10 602 229*
Demand deposits	$ 43 354 405	*$ 53 840 705*
Notice deposits		
Depositor's account	$924 712 714	*$618 081 184*
Profit on sale of investments	5 953 536	*1 408 710*
	$930 666 250	*$619 489 894*
	$990 383 601	*$683 932 828*

AUDITOR'S REPORT

In accordance with Section 43 of the Québec Deposit and Investment Fund's act, I have examined the balance sheet of the Fund as at December 31, 1969 and the related statement of income and expenditure for the year ended on that date. My examination included a general review of the accounting procedures and such tests of accounting records and other supporting evidence as I considered necessary.

In my opinion, the investments and the operations of the Fund were made in accordance with the act; the accompanying balance sheet and statement of income and expenditure present fairly the financial position of the Québec Deposit and Investment Fund as at December 31, 1969 and the results of its operations for the year ended on that date, in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Gustave-E. Tremblay, c.a.,
Provincial Auditor.

Québec City, March 3, 1970.

STATEMENT OF INCOME AND EXPENDITURE
for the year ended December 31, 1969

	1969	1968
Income		
Interest on bonds	$ 45 255 337	*$ 29 779 068*
Dividends	4 410 257	*2 501 021*
Interest on mortgages	1 270 749	*69 110*
Real estate revenue	180 842	*53 805*
Net interest on short-term investments	4 666 375	*2 903 679*
Sundry	41 662	—
	$ 55 825 222	*$ 35 306 683*
Expenditure		
Directors' fees and expenses	$ 6 941	*$ 7 090*
Salaries	536 857	*383 377*
Travelling expenses	30 760	*19 525*
Legal and professional fees	8 872	*5 501*
Rent	98 749	*72 426*
Bank charges	30 951	*51 890*
Office equipment rental	21 263	*19 603*
Electricity, telephone and insurance	24 051	*16 959*
Financial publications and services	11 138	*10 082*
Stationery and printing	19 879	*15 514*
Amortissements	34 820	*22 960*
Other expenses	23 495	*14 764*
	$ 847 776	*$ 639 691*
Net operating income	$ 54 977 446	*$ 34 666 992*
Less: Interest on demand deposits	$ 2 101 208	*$ 1 862 555*
Net income	$ 52 876 238	*$ 32 804 437*

Distribution of net operating income and amounts allocated during the year

	Interest on Demand Deposits	Interest on Notice Deposits	Total
Balance of interest payable for previous year	$ 445 113	$ 10 010 281	$ 10 455 394
Add: Net operating income for the year	2 101 208	52 876 238	54 977 446
	$ 2 546 321	$ 62 886 519	$ 65 432 840
Less: Interest paid during 1969	2 135 805	47 101 029	49 236 834
Balance of interest payable on January 1, 1970	$ 410 516	$ 15 785 490	$ 16 196 006

Deposit accounts — summary of transactions

	Demand Deposits	Notice Deposits	Total
Balance at beginning of year	$ 53 840 705	$618 081 184	$671 921 889
1969: Deposits	246 908 396	—	246 908 396
Transfers	(259 530 501)	259 530 501	—
Interest paid	2 135 805	47 101 029	49 236 834
Balance at end of year	$ 43 354 405	$924 712 714	$968 067 119

STATISTICAL INFORMATION

Yield on deposits

	Amount	Yield equivalence on average deposits*
Gross Income	$ 55 825 222	6.733%
Expenditures	847 776	0.102%
Net Operating Income	$ 54 977 446	6.631%

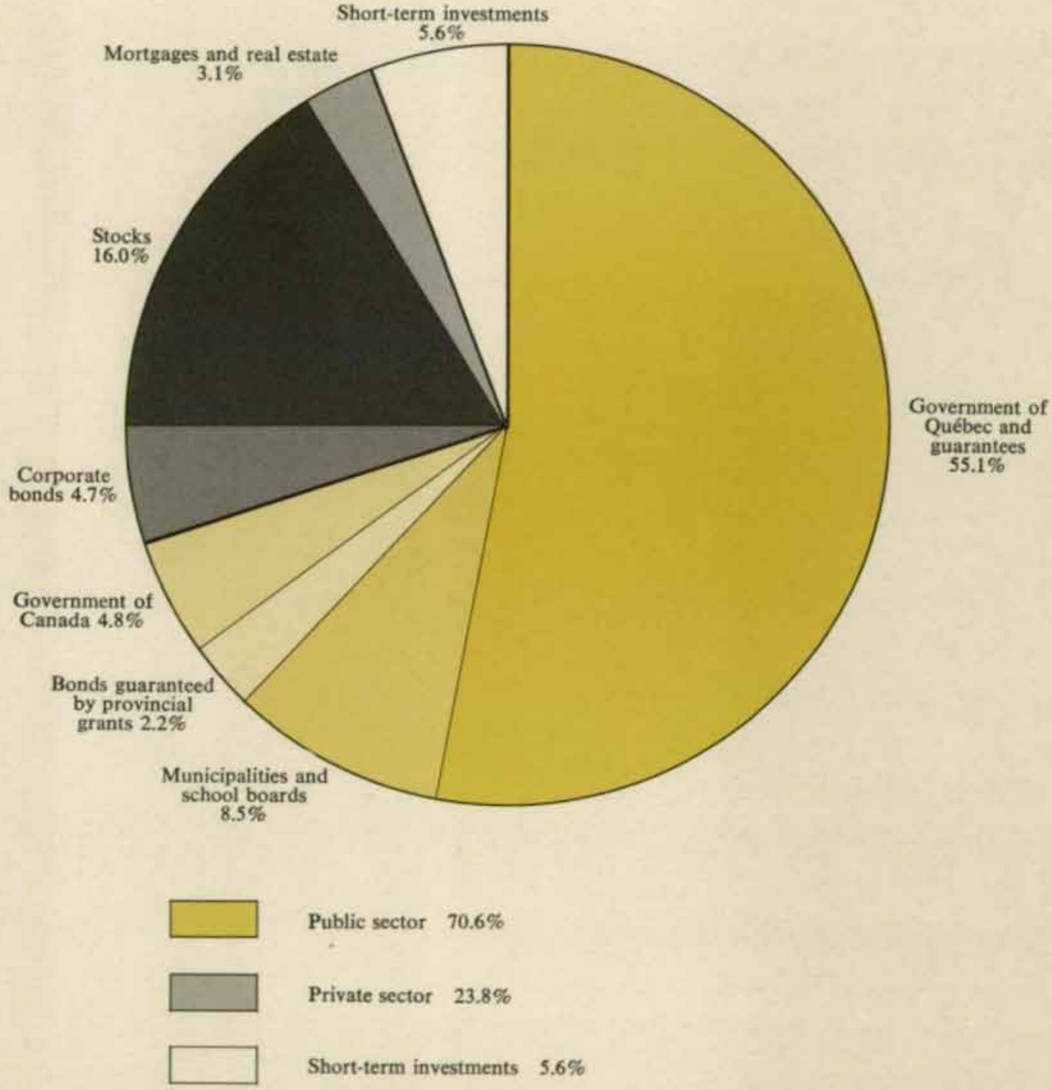
*Average deposits were $829 052 350.

Average interest rate paid on deposits

	Average Deposits	Interest paid or due	Average yield
Demand Deposits	$ 28 691 262	$ 2 101 208	7.323%
Term Deposits*	—	—	—
Notice Deposits	800 361 088	52 876 238	6.606%
Total	$829 052 350	$ 54 977 446	6.631%

*No Term Deposits received during the year

PORTFOLIO DISTRIBUTION
AS AT DECEMBER 31, 1969



Portfolio summary as at December 31, 1969

% Book Value		Nominal Value	Book Value
75.3%	Bonds		
	Government of Canada	$ 49 400 000	$ 46 738 980
	Government of Québec and Guarantees	559 468 000	538 404 402
	Guaranteed by Provincial Grants	21 751 000	20 947 888
	Municipal and School	89 656 000	83 611 344
	Corporate	46 731 500	45 547 855
		$767 006 500	$735 250 469
16.0%	Stock		
	Public Utilities		$ 38 028 934
	Banks and Financial		28 299 007
	Consumer Goods and Services		21 311 225
	Heavy and Secondary Industries		18 761 124
	Oil and Gas		16 984 990
	Mines and Metals		21 099 948
	Forest Products		7 417 247
	Science and Technology		4 733 030
			$156 635 505
2.6%	Mortgages		$ 25 499 045
0.5%	Real Estate		4 411 761
			$ 29 910 806
5.6%	Short-Term Investments		$ 54 220 472
100.0%	Total Portfolio		$976 017 252

1) Weighted average of yields as at December 31, 1969.

2) The deficiency of market under book value, in the amount of $125 406 880, does not take into account a net cumulative deficit of $1 864 299 on sale of bonds.

3) The excess of market value over book value, in the amount of $1 184 455, does not take into account a net cumulative profit of $7 817 835 on sale of such securities.

Percentage	Yield[1]	Market Value
6.4%	6.57%	$ 38 807 063
73.2%	7.44%	446 611 319
2.8%	7.93%	17 521 622
11.4%	8.00%	69 509 610
6.2%	7.38%	37 393 975
100.0%	7.46%	$609 843 589 [2]
24.3%	3.46%	$ 34 949 481
18.1%	5.06%	34 315 709
13.6%	2.51%	21 412 873
12.0%	3.76%	19 227 769
10.8%	1.49%	16 606 297
13.5%	4.30%	20 294 079
4.7%	4.40%	7 648 369
3.0%	1.80%	3 365 383
100.0%	3.53%	$157 819 960 [3]
85.3%	9.21%	$ 25 499 045
14.7%	8.43%	4 411 761
100.0%	9.10%	$ 29 910 806
		$ 54 220 472
		$851 794 827