

Agenda Report

TO: City Council
Attn: Finance Committee

FROM: City Manager

DATE: November 19, 2001

RE: Quarterly Investment Report – Quarter ending 09/30/01

RECOMMENDATION:

This item is for information purposes only.

BACKGROUND:

Government Code Section 53646 (b)(1) requires the Treasurer or Chief Fiscal Officer of a local agency to render a quarterly report to the legislative body of the local agency containing detailed information on all securities, investments, and moneys of the local agency, a statement of compliance of the portfolio with the statement of investment policy, and a statement of the local agency's ability to meet its pool's expenditure requirements for the next six months. By requiring these reports to be made, this bill imposes a state-mandated local program. The bill requires the Treasurer or Chief Fiscal Officer to report whatever additional information or data may be required by the legislative body of the local agency.

In addition to the report required by Section 16480.7, Section 16481.2 was added to the Government Code requiring the Treasurer to submit a quarterly report to the legislative body/oversight committee within 30 days following the end of the quarter containing the following:

- 1) The type of investment, name of the issuer, date of maturity, par and dollar amount invested in each security, investment, and money within the treasury.
- 2) The weighted average maturity of the investments within the treasury.
- 3) Any funds, investments, or programs, including loans, that are under the management of contracted parties.

4) The market value as of the date of the report, and the source of this valuation for any security within the treasury.

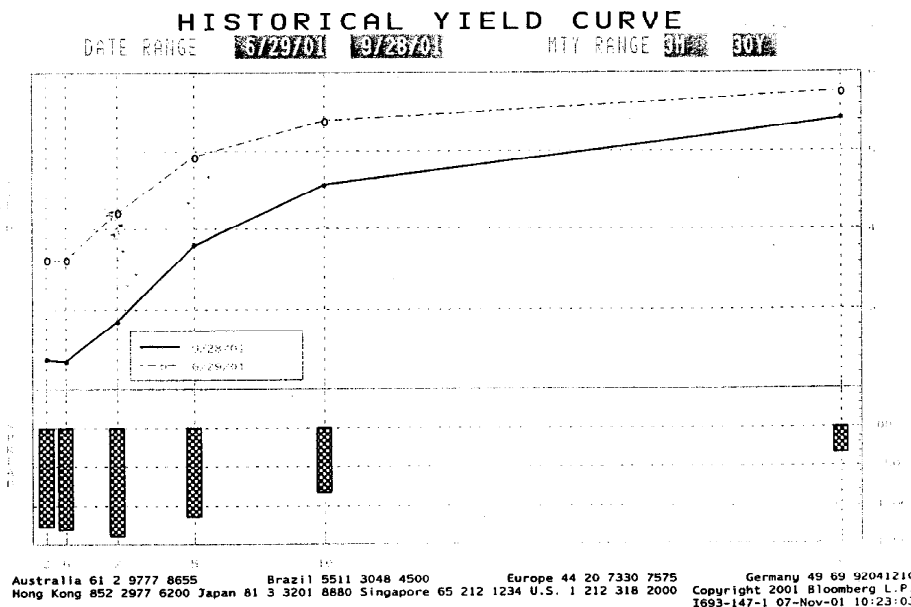
5) A description of the compliance with the statement of investment policy.

ECONOMIC SUMMARY:

The third quarter of 2001 saw a continued slowdown in the economy that went into shock after the terrorist attacks of September 11th, just when parts of the economy began to show some signs of recovery. The 3rd quarter GDP declined by 1% as compared to a positive 0.3% growth rate in the previous quarter. This negative GDP growth rate was anticipated by the market as the economy had come to a halt for a week after the terrorist attacks. Unemployment in September rose to 4.9% and Non-farm payroll fell by 113,000 jobs versus an expected decline of 45,000 jobs, and Consumer spending which accounts two-thirds of the economy declined 1.8%. By the end of the third quarter investors were just beginning to grasp the full effect of the events of September 11th on the economy, but it was clear that the economy had suffered a major setback and the recovery had been pushed further out on the horizon.

The FOMC met on August 21st and cut the Fed Funds rate by 0.25% to 3.5%. The FOMC also announced an inter-meeting 0.50% rate cut on September 17th after the terrorist attacks in an attempt to provide the financial markets with ample liquidity as well as boost the U.S. economy that had already shown many signs of weakness. On October 2nd, the FOMC met again and lowered the Fed Funds rate by an additional 0.50% to 2.5%. The Federal Reserve has cut its target for the overnight bank rate nine times this year by a total of 4% dropping it from 6.5% in September 2000 to 2.5% on October 2, 2001.

Treasuries rallied over the course of the third quarter, pushing yields lower along the curve. The largest shift in the curve occurred on the short end, where the two-year Treasury yield decreased from 4.16% to 2.85%, the lowest level since inception in 1973. Approximately half of the shift in the two-year Treasury yield occurred in the three week period following September 11th event when the two-year yield dropped by 0.67%. While there was a large shift in the short end of the curve, the long end of the curve was limited.



GASB - Mark to Market Accounting for Municipalities

On March 13, 1996, the Government Accounting Standards Board issued a proposal to change the accounting and financial reporting practices on investment securities for most public sector entities. This was finalized into GASB Statement No. 31 in March 1997. The provisions of GASB No. 31 were effective for financial statements beginning July 1, 1997. Statement No. 31 requires mark to market accounting for all investments except for investments with maturities of 1 year or less at the time of purchase. In essence, public entities will disclose all market value changes for securities, both positive and negative, in their financial statements. GASB 31 contains no exceptions for securities that management has the intent and ability to hold to maturity. This is radically different from the current accounting guidelines for public entities and unlike the standards (FASB 115) applicable to "for-profit institutions". Under FASB 115, those securities designated as "held to maturity" can be reported at amortized cost.

This change in investment accounting for public entities will have a significant impact on the overall financial operation of a public entity. The mark-to-market valuation of unrealized gains and losses in an investment portfolio can result in significant swings in an entity's operating statement and/or its unreserved fund balance. The City of Pasadena has already implemented GASB 31 accounting in fiscal year 1998.

Total Funds under management as of 09/30/01 (market values):

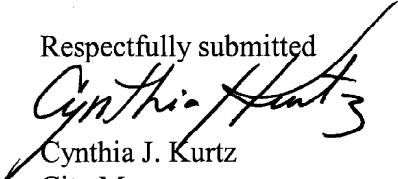
Pooled Investment Portfolio	165,430,871
Capital Endowment Portfolio	11,055,617
Stranded Investment Reserve Portfolio	160,820,576
Special Funds	24,291,184
Investments held with Fiscal Agents	<u>41,208,533</u>
Total Funds under management	<u>402,806,781</u>

Per the Government Code requirements, attached are the reports by each fund, indicating the type of investments, date of maturity, par and dollar amount invested in each security, investment and moneys within the treasury along with the market values as of September 30, 2001. The City Treasurer prices the pooled portfolio and all other funds and investments under management on a monthly basis. The market values are obtained from Interactive Data Corporation (IDC) and Bloomberg Financial System. IDC is an independent third party whose sole service is to provide market prices for all types of securities.

The types of securities held in the portfolio and their percentage allocation to the total are in compliance with the City's 2001-02 Investment Policy, which was adopted by the City Council on October 22, 2001 and Section 53600 of the State Government Code. The City Treasurer currently maintains an average of \$25 million short term liquid investments (one to 90 day

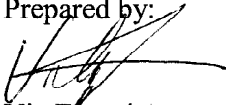
maturities). This balance, along with anticipated cash flows into the City's account, represent a strong liquidity position to meet budgeted expenditures for the next six months.

Respectfully submitted




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City Manager

Prepared by:



Vic Erganian
City Treasurer

Approved by:



Jay M. Goldstone
Director of Finance