Agenda Report

March 14, 2011

TO: Honorable Mayor and City Council

THROUGH: Finance Committee

FROM: Department of Finance

SUBJECT: **QUARTERLY INVESTMENT REPORT QUARTER ENDING DECEMBER 31, 2010**

RECOMMENDATION:

This report is for information only.

BACKGROUND:

Government Code Section 53646 (2)(b)(1) states that in the case of a local agency, the Treasurer or Chief Fiscal Officer may render a quarterly report to the legislative body of the local agency containing detailed information on; 1) all securities, investments, and moneys of the local agency; 2) a statement of compliance of the portfolio with the statement of investment policy; and 3) a statement of the local agency's ability to meet its pool's expenditure requirements for the next six months. By making these reports optional, this bill does not impose a state-mandated local program but encourages local agencies to continue to report. The bill also states that the Treasurer or Chief Fiscal Officer may report whatever additional information or data may be required by the legislative body of the local agency.

The quarterly report shall include 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 Commerce Department reported Gross Domestic Product (GDP) growth rate at 3.2% in the fourth quarter of 2010 making it the 6th consecutive quarterly GDP growth period. Even though GDP growth continued in a positive direction, it remained subpar compared to most recoveries on the historic record. The National Bureau of Economic Research announced in September 2010 that the Great Recession had ended in June 2009. This only meant that the economy stopped getting worse and the slow recovery had begun. Job growth was positive during the quarter. The economy added 385,000 new non-farm jobs, but the growth was not enough to make a real difference in the unemployment rate which remained at 9.4% as of December 31, 2010. Since the beginning of the economic recovery, the labor market added 1.1 million jobs, but this pales compared to the 8.4 million jobs lost during the recession. Corporations remained cautious throughout 2010 about adding workers due uncertainties about the national and global economy, tax laws and healthcare reform and the monetary policy. Chairman Bernanke commenting about the economy recently said that he did not expect employment to get back to normal for several years. Despite this mediocre economic growth, corporations managed to report healthy earnings gains and experienced a strong rebound in profits. Going forward, there seems to be a good momentum for economic growth with less deflationary risk. The average forecast for 2011 GDP growth rate is 3.3% rate with an expectation of no increase in Fed Funds rate in the near future. There are however several risks such as rising oil prices, stubborn high unemployment, and foreign political and debt crisis that could offset the expected growth outcome for 2011. It is expected that the Fed will maintain its accommodative stance for the foreseeable future given the weak labor market, but there are more questions about when the accommodative policy will be reigned in, given the increasing visibility of some inflation in producer prices and food and energy.

The overall U.S. stock market, as measured by the S&P 500 Index, ended the year on a strong note and returned 10.76% during the fourth quarter, and the technology market as measured by the NASDAQ Index returned 12%. Both short and long term interest rates increased during the fourth quarter as a result of increased optimism about the economic growth in 2011 resulting in a drop in value of fixed income securities. The overall U.S. bond market as measured by the Barclays Aggregate Bond Index returned -1.30% during the fourth quarter of 2010.

Total Funds Under Management as of 12/31/2010 (Market Values):

Pooled Investment Portfolio	286,117,797
Capital Endowment	6,513,894
Stranded Investment Reserve Portfolio	62,840,985
Special Funds	53,515,441
Investments Held With Fiscal Agents	218,895,557
Total Funds Under Management	627,883,674

The City pools all internal funds to get the economies of scale and simplify the investment function. There are over 100 funds in the Pooled Investment Portfolio. As of December 31, 2010, the General Fund had $30.9 million invested in the Pooled Investment Portfolio representing 10.81% of the Portfolio value. Investments in the Capital Endowment Fund, the Stranded Investment Reserve Fund, the Special Funds and funds held with fiscal agents are restricted funds or bond proceeds reserved in accordance to the City Charter, ordinances and the bond indentures.

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, as well as investment and moneys within the treasury with market values as of December 31, 2010. 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 Fiscal Year 2011 Investment Policy, which was adopted by the City Council on September 27, 2010 and Section 53600 of the State Government Code. The City Treasurer currently maintains an average of over $45 million short-term liquid investments (1 to 90 day maturities) which represent 1/12th of the City's aggregate annual operating budget. This balance, along with anticipated cash flows into the City's account, represents a strong liquidity position to meet budgeted expenditures for the next six months.

On December 31, 2010 the market value of the total investments under management increased by $186 million as compared to the previous quarter end due to the receipt of $153 million bond proceeds from the issuance of the Rose Bowl Bonds, the receipt of $28 million bond proceeds from the issuance of the 2010 Water Revenue Bonds, and the receipt of net property taxes in December. The book yield on the City's Pooled Portfolio continued to gradually decline in the last several quarters as short term rates remained 0%-0.25% rate and all maturing investments were reinvested at lower yielding securities as compared to their original rate. The quarter end effective yield on the

Pooled Portfolio, which accounts for realized trading gains and losses, was 1.79% compared to the State Treasurer's Local Agency Investment Fund ("LAIF") return of 0.49% and the average yield on the two year U.S. Treasury of 0.50%. for the same period.

COUNCIL POLICY CONSIDERATION:

This action supports the City Council Strategic Goal to maintain fiscal responsibility and stability.

FISCAL IMPACT:

This item is for information only. There is no fiscal impact

Respectfully submitted,

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Attachments:

Attachment A – Quarterly Investment Report (12/31/2010)