

# Agenda Report

September 26, 2011

**TO:** Honorable Mayor and City Council

**THROUGH:** Finance Committee

**FROM:** Department of Finance

**SUBJECT:** Quarterly Investment Report  
Quarter ending June 30, 2011

**RECOMMENDATION:**

This report is for information purposes 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:**

After a disappointing Gross Domestic Product (GDP) growth rate of 0.4% during the first quarter of 2011, the economy grew at a below-average rate of 1.3% during the second quarter. Economic statistics released during the second quarter reflect a continued slowdown in economic activity, raising concerns and increasing fear of the possibility of another global recession. Several factors contributed to this anemic economic growth including the tsunami in Japan, the sovereign debt crisis mainly in Greece, the rise of food and energy prices, the approaching of the deadline for the U.S. debt ceiling, and the continuing housing crisis. Despite the increasingly gloomy assessments of the economy, there were recent activities that produced some positive data indicating that the various sectors are responding differently to the current economic crisis.

Inflation on the other hand has been rising steadily over the last eight months. The Year-over-Year headline inflation measured at a quarter-end rate of 3.6%, and core inflation, which excludes the volatile food and energy items, increasing to a rate of 1.6%. The Fed announced that this rise in inflation is only temporary and should subside in the near future. The Fed's target range for core inflation remains between 1% and 2%.

The Labor market remained very weak during the second quarter. As of June 30, 2011, the unemployment rate measured at 9.2%, indicating a 0.4% increase from March's rate of 8.8%. Even though the economy did add an average of 105,000 non-farm jobs during the quarter, the rate was far less than the average of 250,000 jobs required to gradually reduce the unemployment rate. While most of the hiring was in the private sector, job reductions were heavily concentrated in the public sector.

Housing continues to remain a drag on the economy. The massive number of foreclosures and the number of mortgages currently in or about to default have put severe pressure on housing prices. Existing home sales experienced a decrease during the second quarter, and, with consensus among most economists, the housing market will not improve until the labor market improves.

U.S. Treasury yields declined across the yield curve during the second quarter. On June 30<sup>th</sup>, the two-year Treasury yield dropped 46% to yield at 0.45%, and is currently at a rate of 0.20%. During the end of the second quarter, the yield on the ten-year Treasury dropped to a rate of 3.16% and is currently at a rate of 2.17%. The Fed met twice during the quarter and maintained the Fed Funds rate close to 0%. More recently, the Fed

announced that it will maintain a short-term rate between 0% and 0.25% over the next two years. This was historically the first time that the Fed indicated its target rate for a definite period of time.

The recent enactment of the United States' debt ceiling agreement raised concerns and uncertainty over the economic ramifications on the nation. On August 2, 2011, lawmakers agreed to raise the nation's \$14.3 trillion debt ceiling and place a 10-year \$2.4 trillion spending reductions. Cuts in U.S. government spending may contribute to the deceleration of economic activity and continue to threaten long-standing recovery efforts. Despite concerns over a slowing economy and Europe's expanding sovereign debt crisis, the decision did, however, increase demand for Treasuries. While the U.S. economy remains in a fragile state, concerns were raised about the United States' ability to maintain its AAA credit rating. Amidst the difficulties of concluding debt ceiling and spending cut negotiations, however, Standard & Poors' controversial downgrade of the United States' credit rating raised insecurity among investors and employers.

**TOTAL FUNDS UNDER MANAGEMENT:**

The following represents the total City funds under management based on their market values as of June 30, 2011.

	<b>03/31/2011</b>	<b>06/30/2011</b>	<b>\$ Change</b>
Pooled Investment Portfolio	288,019,271	306,851,206	18,831,935
Capital Endowment	6,521,983	3,576,487	(2,945,496)
Stranded Investment Reserve Portfolio	62,972,456	63,826,066	853,610
Special Funds	55,072,555	40,645,535	(14,427,020)
Investments Held with Fiscal Agents	195,714,490	176,602,624	(19,111,866)
<b>Total Funds Under Management</b>	<b>608,300,755</b>	<b>591,501,918</b>	<b>(16,798,837)</b>

The Pooled Investment Portfolio increased by a net \$18 million due mainly to the receipt of property taxes in the amount of \$26.7 million and sales tax revenues in the amount of \$5.3 million, less the debt service payments made in the amount of \$14 million.

The Capital Endowment Fund was decreased by \$2.95 million as a result of a \$3 million drawdown from the fund made to cover budgeted project-related expenses. The Stranded Investment Portfolio increased by \$853,610 due to investment earnings on the Fund.

The Special Funds decreased by \$14.43 million due to 1) \$4.3 million in drawdowns from the 2010 Water Bond proceeds to cover capital expenditures made to the water system; 2) \$8 million reimbursement made by PCDC to the General Fund to cover transfers of SB481 revenues and administrative and project-related costs; and, 3) \$2.23 million SERAF payment was made to the County of Los Angeles.

The value of the investments held with fiscal agents dropped by \$19.11 million as a result of drawdowns on the Rose Bowl bond proceeds in the amount of \$12 million and a debt service payment made on the 1999 Pension Obligation Bonds in the amount of \$8.13 million.

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 June 30, 2011, the General Fund has \$37.4 million invested in the Pooled Investment Portfolio, which represents 12.18 percent of the Pooled 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 June 30, 2011. 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 at least \$45 million short-term liquid investments (1 to 90 day maturities) which represent 1/12<sup>th</sup> 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.

The book yield on the City's Pooled Portfolio continued to gradually decline in the last two years as short-term rates remained between 0.00 percent and 0.25 percent. All maturing investments were reinvested at lower yielding securities as compared to their original rate. The effective yield on the Pooled Portfolio accounts for realized trading gains and losses. The fiscal year-end effective yield was 1.72 percent, compared to the State Treasurer's Local Agency Investment Fund (LAIF) return of 0.48 percent and the average yield on the two-year U.S. Treasury of 0.55 percent for the same period.

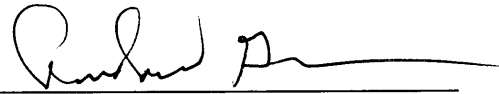
**COUNCIL POLICY CONSIDERATION**

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

**FISCAL IMPACT:**

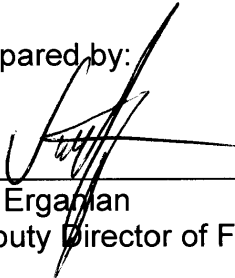
This item is for information only. There is no fiscal impact.

Respectfully submitted,



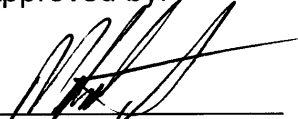
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ANDREW GREEN  
Director of Finance

Prepared by:



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Vic Erganian  
Deputy Director of Finance/City Treasurer

Approved by:



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MICHAEL J. BECK  
City Manager

Attachments:

Attachment A – Quarterly Investment Report (Quarter Ending 06/30/2011)