



# Agenda Report

November 25, 2019

**TO:** Honorable Mayor and City Council  
**THROUGH:** Finance Committee  
**FROM:** Department of Finance  
**SUBJECT:** Quarterly Investment Report – Quarter Ending September 30, 2019

## **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 (CFO) 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 CFO 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*.

## **Quarterly Economic Review**

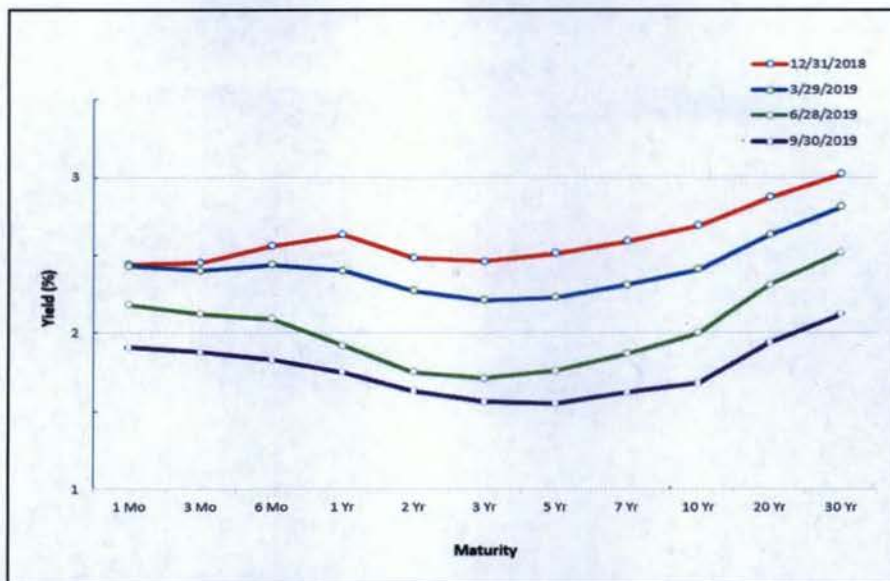
According to the advance estimate released by the Bureau of Economic Analysis of the U.S. Department of Commerce, the Gross Domestic Product (GDP) grew by 1.9% during the third quarter of 2019. In comparison, the real GDP growth for the first quarter of 2019 was 2.0%. Increases in personal consumption expenditures and government spending contributed to the growth in economic activity. This was partially offset by a drop in gross private domestic investment and by a deterioration of the net exports of goods and services.

September 2019 saw nonfarm payroll jobs expand by 180,000. With employment gains for July and August coming in at 166,000 and 219,000, respectively, the average monthly jobs created for 2019 thus far stands at about 169,000 per month. In contrast, 2018 saw nonfarm employment add an average of 214,000 jobs per month. The unemployment rate declined to 3.5% as of September 2019. The labor market continued to tighten as the average hourly earnings rose by 2.9% on an annualized basis in September.

The year-over-year Consumer Price Index (CPI) rose 1.7% in September 2019, which is now the tenth month in a row this figure has been at or below 2.0%. Meanwhile, the year-over-year Core CPI Index, which excludes food and energy components, rose 2.4% for the 12 months ending September 2019. Over the past year, the food index increased by 1.8% while the energy index contracted by 4.8%.

At its October 29-30 meeting, the Federal Open Market Committee (FOMC) decided to lower the target for the federal funds rate to a range of 1.50% - 1.75% in light of the implications of global developments for the economic outlook as well as muted inflation pressures. The interest rate cut is seen to support the sustained expansion of economic activity, strong labor market conditions, and inflation near the 2.0% objective.

Yields fell across all maturities for the third consecutive quarter (see chart in the following page). The yield on the 2-year Treasury note fell to 1.63% from 1.75% at the end of the previous quarter. Over the same period, the yield on the 5-year Treasury fell to 1.55% from 1.76%. This downward movement in yields again led to gains among all bond sectors. The broad-based Barclays U.S. Aggregate Bond Index posted a 2.27% gain for the third quarter of 2019 after returning 3.08% in the previous quarter. The best performing sector was Long Government and Investment Grade Credit. The Barclays Long U.S. Government Credit Index registered a 6.6% total return during the quarter and has thus far returned 20.9% for the nine-month period ending September 2019.



The growth in domestic equities in the first half of 2019 began to taper off during the third quarter of 2019. The broad-based S&P 500 composite posted a 1.19% gain during the third quarter of 2019 after posting a 3.79% gain during the prior period. The Dow Jones Industrial Average (DJIA) similarly posted a 1.19% gain after returning 2.59% in the prior quarter. The NASDAQ, which is dominated by Information Technology stocks, actually contracted by 0.09% during the quarter following a 3.58% gain in the prior quarter. The slowing growth of domestic equities in 2019 is graphically displayed in the chart below.





**Total Funds Under Management**

The following table represents total City funds under management based on their market values as of September 30, 2019.

	9/30/2019	6/30/2019	\$Change
Pooled Investment Portfolio	\$608,598,225	\$605,619,888	\$2,978,338
Capital Endowment	1,996,358	1,985,949	10,409
Stranded Investment Reserve Portfolio	63,794,231	66,228,804	(2,434,573)
Special Funds	21,617,650	21,705,766	(88,115)
Investments Held with Fiscal Agents	54,223,381	52,886,674	1,336,707
PARS Section 115 Trust	13,498,317	13,356,628	141,689
<b>Total Funds Under Management</b>	<b>\$763,728,162</b>	<b>\$761,783,707</b>	<b>\$1,944,454</b>

The Pooled Investment Portfolio value increased by a net \$2,978,338 due to the following transactions during the quarter:

Net Investment Earnings (Fair Market Value Change plus Interest Income)	\$3,554,132
Deposits and Credit Card Receipts	121,283,536
Property Tax Revenues	4,743,071
Sales Tax and Other State Apportionments	15,032,871
HUD Receipts Net of Payments and Loans	2,738,556
Payroll and Payroll-related Expenses	(76,405,464)
Vendor Payments and Accounts Payable Checks	(40,894,976)
Debt Service Payments Net of Reimbursements and Subsidies	(6,038,655)
Water and Power Payments Net of Receipts	(24,063,405)
Net Transfer from Other Funds	3,028,672
	<b>\$2,978,338</b>

The Capital Endowment Fund increased by a net \$10,409 representing the investment earnings for the period which includes the market value change of investments and the interest earned.

The Stranded Investment Reserve portfolio decreased by a net \$2,434,573 mainly due to a \$3,000,000 drawdown from the fund to partially fulfill the planned transfer of \$7,000,000 for the fiscal year from the Stranded Investment to the Energy Services Charge Reserve, meant to offset potential increases in power costs to customers. The difference is attributed to investment earnings for the quarter of \$565,427.

Special Funds decreased by a net \$88,115 due to a \$152,525 drawdown for Robinson Park construction expenses and a \$23,150 Annandale principal payment, partially offset by investment earnings for the quarter of \$87,560.

Investments held with fiscal agents increased by \$1,336,707 due to contributions of \$1,274,127 made to the Southern California Public Power Authority Stabilization Fund.

Other additions were a \$98,199 transitional increase for debt service payments made for various bond issues, and \$36,094 for the costs of issuance of the 2019A Electric Revenue Bonds; while this was partially offset by \$71,713 in market value losses net of investment earnings.

The PARS Section 115 Trust account increased by \$141,689. The change was comprised of market value change of investments and the interest earned totaling \$158,593, less \$16,904 in investment expenses.

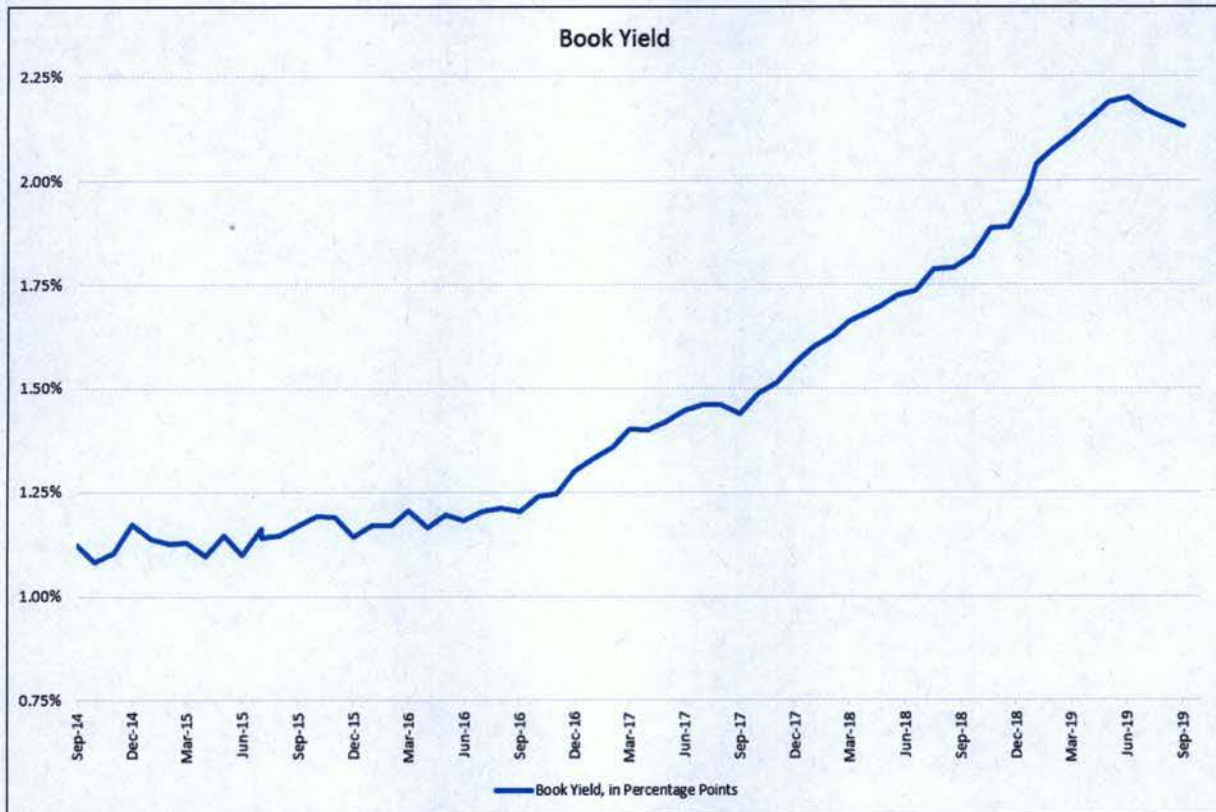
The City pools all internal funds to gain economies of scale and to simplify the investment function. There are over 100 funds in the Pooled Investment Portfolio. Because the September 2019 accounting records have not yet closed, staff estimates the General Fund's cash balance at approximately \$58 million at the end of September representing 10% of the September Pooled Portfolio value. The General Fund's cash balance fluctuates daily based on the timing of revenues receipts and payment of expenditures. Investments in the Capital Endowment Fund, the Stranded Investment Reserve Fund, the Special Funds, the PARS Section 115 Trust account, and funds held with fiscal agents are restricted funds or bond proceeds reserved in accordance with the City Charter, City ordinances, bond indentures, and Trust Agreements. The City targets an average duration of two years in managing the pooled portfolio based on the portfolio's risk and return evaluation and industry best practices as it pertains to public funds management. As of September 30, 2019, the portfolio's duration was 1.62 years.

Per government code requirements, attached are 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 September 30, 2019. On a monthly basis, the City Treasurer prices the pooled portfolio and all other funds and investments under management. The market values are obtained from Interactive Data Corporation (IDC) and from 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 2020 Investment Policy which was adopted by the City Council on July 22, 2019 and Section 53600 of the State Government Code. The City Treasurer currently maintains over \$50 million short-term liquid investments (1 to 90 day maturities) which represents approximately 1/12<sup>th</sup> of the City's total 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 a total return basis, the components of which include interest, amortization, and market value changes, the Pooled Portfolio posted a gain of 0.59% for the third quarter of 2019. This underperforms against the 0.70% return of the assigned benchmark, the Bank of America Merrill Lynch 1-3 Year US Corporate and Government Index, for the

same time period. Reflecting the rise in interest rates thru the end of 2018, The Pooled Portfolio's book yield was rising until June 2019. The graph below which represents the historic book yield of the Pooled Portfolio over the last five years shows that the said rise hit an inflection point in June 2019. The Pooled Portfolio's book yield began to drop in the succeeding months; this time reflecting the drop in interest rates in 2019 and the interest rates cut by the Fed.



**COUNCIL POLICY CONSIDERATION:**

This action supports the City Council's strategic planning goal to maintain fiscal responsibility and stability.



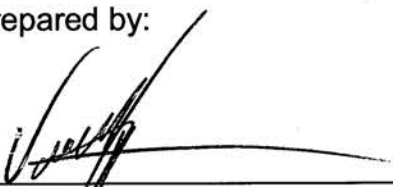
**FISCAL IMPACT:**

There is no fiscal impact as a result of this action nor will it have any indirect or support cost requirements. There is no anticipated impact to other operational programs or capital projects as a result of this action.

Respectfully submitted,

  
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MATTHEW E. HAWKESWORTH  
Department of Finance

Prepared by:

  
\_\_\_\_\_  
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Deputy Director of Finance/City Treasurer

Approved by:

  
\_\_\_\_\_  
Steve Mermell  
City Manager

Attachment: (1)

- 1) Attachment A – Quarterly Investment Report - Quarter Ending September 30, 2019