



Agenda Report

June 10, 2019

TO: Honorable Mayor and City Council
FROM: Department of Finance
SUBJECT: Quarterly Investment Report – Quarter Ending March 31, 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 3.2% during the first quarter of 2019. In comparison, the real GDP growth for the fourth quarter of 2018 was 2.2%. Increases in personal consumption expenditures, gross private domestic investment, net exports of goods and services, and government spending all contributed to the growth in economic activity.

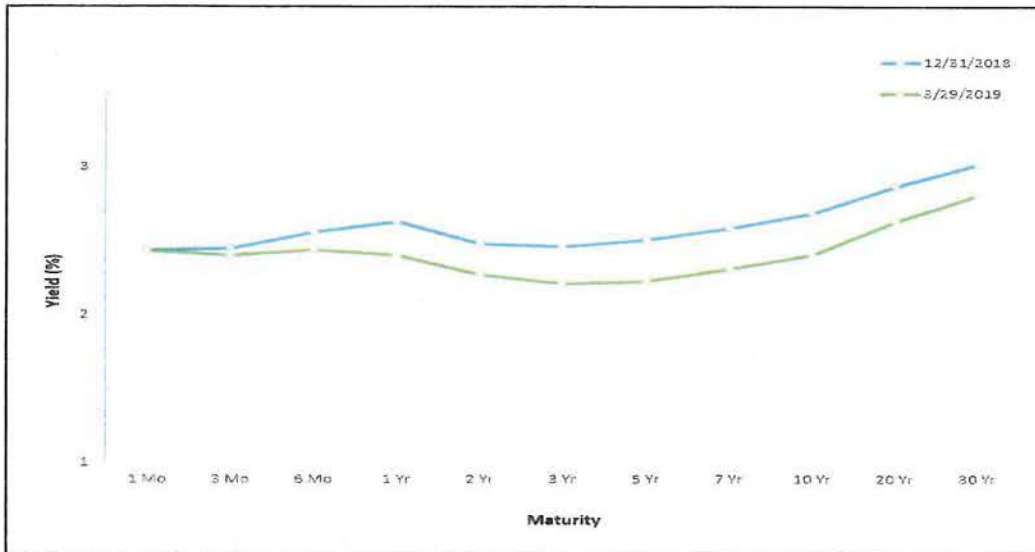
March 2019 saw nonfarm payroll jobs expand by 189,000. With employment gains for January and February coming in at 312,000 and 56,000, respectively, the average monthly jobs created for 2019 thus far stands at about 186,000 per month. In contrast, 2018 saw nonfarm employment add an average of 214,000 jobs per month. The unemployment rate stood at 3.8% as of March 2019, unchanged from the prior month. The labor market continues to tighten as the average hourly earnings rose by 3.2% on an annualized basis in March.

The year-over-year Consumer Price Index (CPI) rose 1.9% in March 2019, which is now the fourth month in a row this figure has been below 2.0%. The Bureau of Labor Statistics noted that the beginning of this four-month streak was the first time the 12-month change has been under 2.0% since August 2017. Meanwhile, the year-over-year Core CPI Index, which excludes food and energy components, rose 2.0% for the 12 months ending March 2019. Over the past year, the food index increased by 2.1% while the energy index actually contracted by 0.4%.

At its March 19-20 meeting, the Federal Open Market Committee (FOMC) decided to maintain the target range for the federal funds rate at 2.25% to 2.50%, noting the labor market's continued strength but that growth of economic activity has slowed. The FOMC also pointed out that while core inflation remains near 2.0%, overall inflation has declined largely as a result of lower energy prices. The FOMC's March 2019 Summary of Economic Projections had notable changes to the December 2018 projections. Real GDP growth for the upcoming year 2019 was revised downwards from 2.3% to 2.1%. The unemployment rate for the upcoming year 2019 was revised upwards from 3.5% to 3.7%. The federal funds rate, previously targeted to be in the range of 2.75% to 3.00% by the end of 2019 is now forecasted to be between 2.25% to 2.50%; the FOMC is thus seen to keep the rate at the current range through the end of 2019. At its April 30-May 1 meeting, the FOMC again left the target range for the federal funds rate unchanged but also reiterated that it will be patient as it determines future adjustments to the federal funds rate in light of global economic and financial developments and muted inflation pressures.

Yields fell across all maturities (see chart in the following page). The yield on the 2-year Treasury note fell to 2.27% from 2.48% at the end of the previous quarter. Over the same period, the yield on the 5-year Treasury fell to 2.23% from 2.51%. This downward movement in yields led to gains among all bond sectors. The broad-based Barclays

U.S. Aggregate Bond Index posted a 2.94% gain for the first quarter of 2019. The High Yield and Emerging Markets Debt sectors were the quarter's best performing with 7.4% and 6.6% total returns, respectively (Fidelity Investments).



Domestic equities rebounded during the first quarter of 2019, after suffering substantial losses during the fourth quarter of 2018. The broad-based S&P 500 composite posted a 13.07% gain during the first quarter of 2019 after posting a -13.97% total loss during the prior period. The Dow Jones Industrial Average (DJIA) similarly recovered with an 11.15% gain after losing -11.83% in the prior quarter. The NASDAQ, which is dominated by Information Technology stocks, followed a similar arc with a 16.49% gain during the quarter following a -17.54% loss in the prior quarter. The recovery of equities in the first quarter of 2019 is graphically displayed in the chart below. The S&P 500 and the DJIA indices both peaked around the end of the third quarter of 2018, both suffered relative dips at the end of the said year, and both are ending the first quarter of 2019 headed towards returning to their respective peaks reached in 2018.



Total Funds Under Management

The following table represents total City funds under management based on their market values as of March 31, 2019.

	3/31/2019	12/31/2018	\$Change
Pooled Investment Portfolio	\$586,346,085	\$579,859,453	\$6,486,631
Capital Endowment	1,971,226	1,969,227	1,999
Stranded Investment Reserve Portfolio	72,067,332	70,977,823	1,089,509
Special Funds	25,993,551	26,033,931	(40,379)
Investments Held with Fiscal Agents	50,067,550	50,135,165	(67,615)
PARS Section 115 Trust	12,970,624	12,281,477	689,146
Total Funds Under Management	\$749,416,367	\$741,257,076	\$8,159,291

The Pooled Investment Portfolio value increased by a net \$6,486,631 due to the following transactions during the quarter:

Net Investment Earnings (Fair Market Value Change plus Interest Income)	\$5,630,917
Deposits and Credit Card Receipts	104,770,785
Property Tax Revenues	24,099,800
Sales Tax and Other State Apportionments	12,292,555
HUD Receipts Net of Payments and Loans	676,291
Payroll and Payroll-related Expenses	(73,753,952)
Vendor Payments and Accounts Payable Checks	(33,742,282)
Debt Service Payments Net of Reimbursements and Subsidies	(12,783,854)
Water and Power Payments Net of Receipts	(19,679,811)
Net Transfer to Other Funds	(1,023,818)
	\$6,486,631

The Capital Endowment Fund increased by a net \$1,999 representing the investment earnings for the period of \$14,499 which includes the market value change of investments and the interest earned less a \$12,500 withdrawal to cover accumulated cost allocation expenses under the Charter Capital Fund.

The Stranded Investment Reserve portfolio increased by a net \$1,089,509 representing the investment earnings for the period which includes the market value change of investments and the interest earned.

Special Funds decreased by \$40,379 due to \$302,807 Robinson Park construction expenses partially offset by investment earnings for the quarter of \$262,428.

Investments held with fiscal agents decreased by \$67,615 as a result of \$671,506 in withdrawals made from the Stabilization Fund to pay for Water and Power invoices partially offset by a \$349,571 transitional increase for debt service payments made for

various bond issues, \$279,320 in investment earnings, and a \$25,000 withdrawal to cover cost of issuance costs for the 2018AB Rose Bowl Refunding bonds.

The PARS Section 115 Trust account increased by \$689,146. The change was comprised of market value change of investments and the interest earned totaling \$705,191, less \$16,044 in investment expenses.

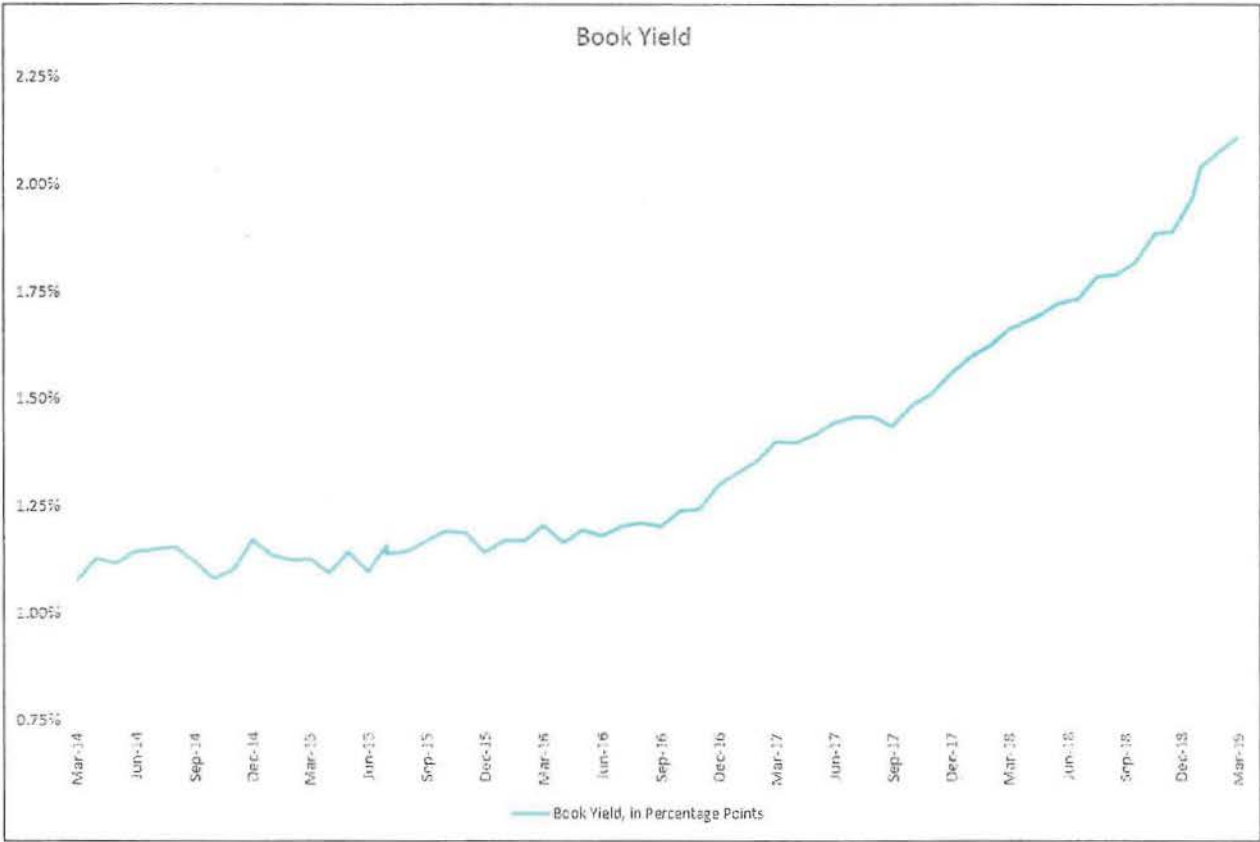
The City pools all internal funds to gain economies of scale and to simplify the investment function. There are over 100 funds in the Pooled Investment Portfolio. Because the March 2019 accounting records have not yet closed, staff estimates the General Fund's cash balance at approximately \$64 million at the end of March representing 11% of the March 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 March 31, 2019, the portfolio's duration was 1.49 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 March 31, 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 2019 Investment Policy which was adopted by the City Council on June 11, 2018 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 1/12th 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 1.22% for the first quarter of 2019. This outperforms the 0.96% return of the assigned benchmark, the Bank of America Merrill Lynch 1-3 Year US Corporate and Government Index, for the same time period. The Pooled Portfolio's book yield has been rising, reflecting the rise in interest rates since maturing investments are reinvested in securities with higher yields. The

graph below represents the historic book yield of the Pooled Portfolio over the last five years, thru March 2019.



COUNCIL POLICY CONSIDERATION:

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

FISCAL IMPACT:

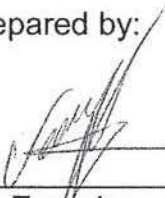
There is no fiscal impact as a result of this action nor will it have any indirect or support cost requirements. There is no anticipated impact to other operational programs or capital projects as a result of this action.

Respectfully submitted,



MATTHEW E. HAWKESWORTH
Department of Finance

Prepared by:



Vic Erganian
Deputy Director of Finance/City Treasurer

Approved by:



STEVE MERMELL
City Manager

Attachment: (1)

1) Attachment A – Quarterly Investment Report - Quarter Ending March 31, 2019