

**City of Boulder**  
Finance Department

TO: The Mayor and Members of City Council  
Jane S. Brautigam, City Manager

FROM: Cheryl Pattelli, CFO

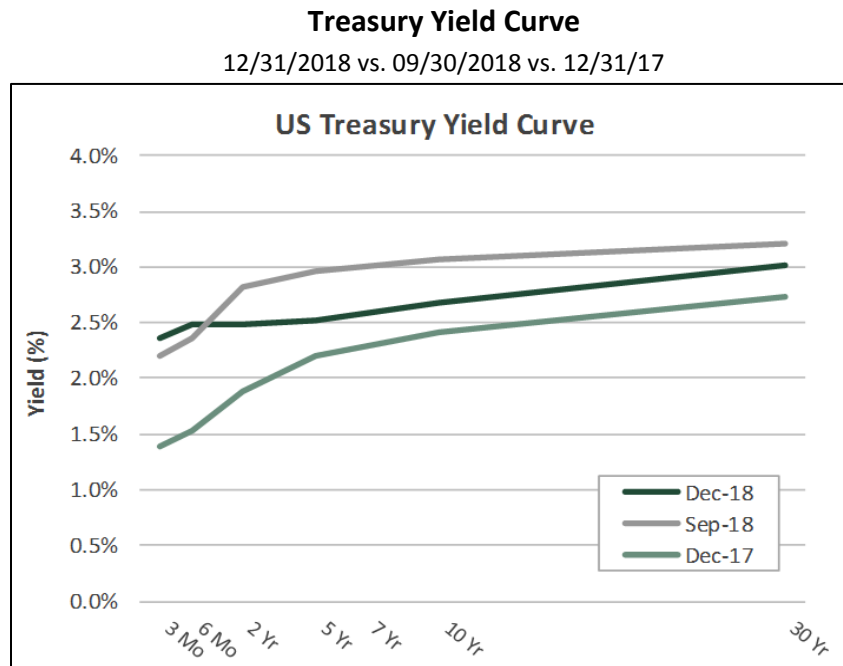
SUBJECT: Investment Performance as of December 31, 2018

DATE: January 15, 2019

**Section 1 – Background**

- This report is for City Council information only and requires no action by City Council.
- The investment of City funds is guided by and this report is submitted in compliance with the City's Investment Ordinance. (Chapter 2-10, *Investment of City Funds*, Boulder Revised Code 1981).
- The investment objectives as specified in the Ordinance, are:
  - The primary objective is preservation and protection of capital. This objective reduces the risk to which the portfolio can be subjected. To comply with this objective, investments are diversified by type and maturity horizons.
  - The second objective is to maintain adequate liquidity to meet the daily cash needs of the City. The City's ordinance requires that 5% of the portfolio matures within 30 days.
  - Yield is the third objective. The City strives to maximize return, while minimizing the risks of the market.

## Section 2 – The Yield Curve and Federal Open Market Committee (“the Fed”)



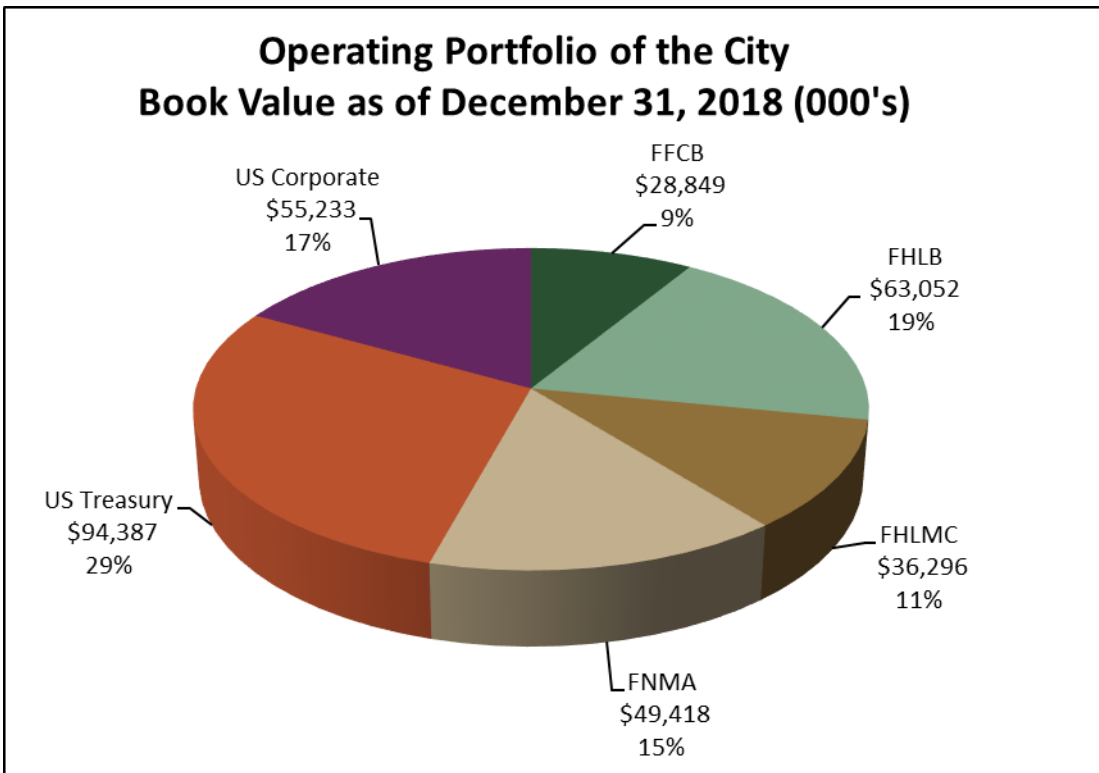
Source: Bloomberg

- On a year-over-year basis, Treasury yields have increased and the Treasury yield curve has flattened. The spread between 2-year and 10-year Treasury yields narrowed from 52 basis points to 20 basis points in 2018. Rate hikes by the Federal Reserve have put upward pressure on rates, while supply and demand imbalances, technical factors, weakening global economic growth, and subdued inflation expectations have contributed to the curve flattening.
- The Federal Open Market Committee (FOMC) raised the fed funds target rate by 25 basis points in December to a range of 2.25% - 2.50%. Although recent economic data has softened, the rate hike was widely expected. The Fed’s long run fed funds rate target was lowered to 2.80% from the previous estimate of 3.0%. However, the Fed did little to acknowledge the changing market dynamics and tightening financial conditions, reaffirming their strong economic forecast for 2019 and emphasizing the balance sheet reduction strategy remains on track. Although the modest adjustment in the Fed’s projections was a step in the right direction, some market participants were expecting a more dovish tone from the Fed chair. We continue to believe the terminal fed funds rate will be below 3.0% and believe the Fed is at risk of making a policy error if monetary policy continues to tighten at the same quarterly pace of 2018. We believe there is a high probability that the Fed will keep monetary policy on hold at least through the first quarter.

### **Section 3 – The City’s Portfolios**

- Portfolio strategies implemented this quarter and all investments held in the portfolios comply with the City’s investment objectives and the Ordinance that specifies allowable investments:
  - The objective of safety is achieved through a well-diversified portfolio, primarily among two major sectors (Treasury and Agency), the Agency issuers and various maturities along the yield curve. On March 7<sup>th</sup> 2017 the City Council approved amendments to the Investment Policy proposed by finance staff expanding opportunities to further diversify the portfolios. Pursuit of further diversification through the recently revised policies will progress strategically relative to market conditions. Market risk is managed by maintaining a low weighted average maturity (WAM) in the City’s portfolio. As of December 31, 2018, the WAM was 1.53 years while the Ordinance allows up to a five-year WAM.
  - The City maintains sufficient liquidity. As of December 31, 2018, 3.39% of the portfolio or \$11.0 million will mature over the next 30 days.
  - As of December 31, 2018, the yield on the pooled investment portfolio was 1.91%. Our current yield benchmark is the six-month trailing average on the 2-year Treasury, which was 2.73%, as of December 31, 2018. The benchmark yield exceeded the investment portfolio by 0.82%.
- There are no investments in the oil and gas industry in the City’s portfolio.
- In Q4 2018 the City’s investment adviser purchased approximately \$24.5 million of securities at an average yield of 2.76% for the City of Boulder’s investment portfolio. The proceeds of \$25.0 million of sales and maturities were used to fund these purchases. Purchases included Treasury and Agency securities maturing between November 2018 and December 2021. On a year-over year basis, short-term Treasury yields continued their move upward but we did see a decrease in yield levels toward the end of the year in November and December. The 2-year Treasury yield increased 57 basis points to 2.49% for the year but experienced a nearly 30 basis point drop in December alone. Longer term Treasury yields moved higher as well with the 10- year Treasury yield moving up 23 basis points, to 2.69% but also experienced a decline at the end of the year. The Federal Reserve raised the fed funds target rate by another 25 basis points in the fourth quarter to a range of 2.25%-2.50%. Based upon some softening of recent economic data as well as more dovish sounding members of the Fed, they might put a continued tightening of monetary policy on hold at least through the first quarter. We will remain disciplined with time proven portfolio strategies as we move into the new year.

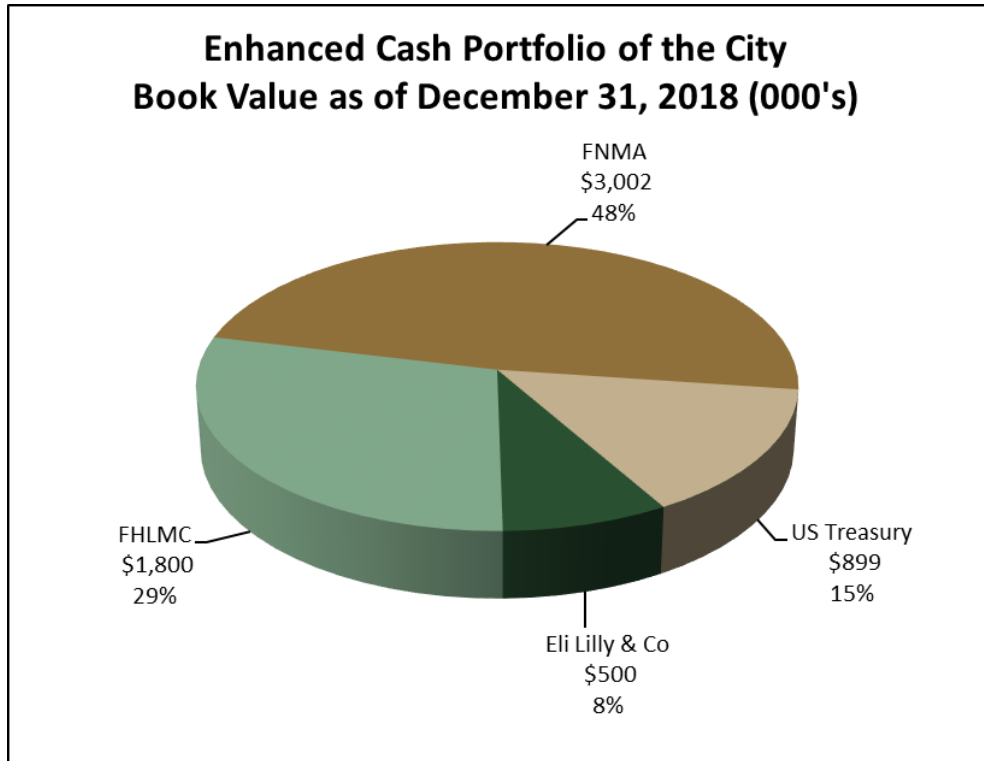
**Operating Portfolio of the City**



**Portfolio Characteristics  
Operating Portfolio of the City of Boulder**

|                        | <b>12/31/2018</b> | <b>09/30/2018</b> |
|------------------------|-------------------|-------------------|
|                        | <b>Portfolio</b>  | <b>Portfolio</b>  |
| Average Maturity (yrs) | 1.53              | 1.69              |
| Modified Duration      | 1.47              | 1.63              |
| Average Purchase Yield | 1.91%             | 1.84%             |
| Average Market Yield   | 2.54%             | 2.69%             |
| Average Quality        | AA+/Aa1           | AA+/Aa1           |
| Total Market Value     | 326,270,500       | 324,796,520       |

## Enhanced Cash Portfolio



### Portfolio Characteristics

#### City of Boulder Enhanced Cash Portfolio

|                        | 12/31/2018       | 09/30/2018       |
|------------------------|------------------|------------------|
|                        | <b>Portfolio</b> | <b>Portfolio</b> |
| Average Maturity (yrs) | 0.40             | 0.59             |
| Modified Duration      | 0.40             | 0.58             |
| Average Purchase Yield | 1.40%            | 1.39%            |
| Average Market Yield   | 2.59%            | 2.47%            |
| Average Quality        | AA+/Aaa          | AA+/Aaa          |
| Total Market Value     | 6,190,249        | 7,768,990        |

In March 2012, a separate portfolio was established to facilitate IRS required arbitrage calculations on Bond Reserve and Project Funds. The balance of \$6.2 million as of December 31, 2018 was invested as shown above in the graph and table to assure timely funding for the projected draw down schedule.

- In June 2012, the investment committee selected the one year Treasury as the benchmark for the bond proceeds based upon an average maturity of approximately one year for the portfolio at that time. As of December 31, 2018 the portfolio yield was 1.40%.
- As of December 31, 2018, 0% of the portfolio or \$0 will mature over the next 30 days.
- The average maturity of the portfolio was 146 days as of December 31, 2018. An objective of this portfolio is to safely support the liabilities of the projected project cash flows.

| <b>Holding Details for City of Boulder<br/>Operating Portfolio</b> |                   |                       |
|--|-------------------|-----------------------|
| <b>Issuer</b>  | <b>Book Value</b> | <b>% of Portfolio</b> |
| FFCB   | \$ 28,849         | 8.82%                 |
| FHLB   | \$ 63,052         | 19.27%                |
| FHLMC  | \$ 36,296         | 11.09%                |
| FNMA   | \$ 49,418         | 15.10%                |
| US Treasury  | \$ 94,387         | 28.84%                |
| Apple Inc  | \$ 3,069          | 0.94%                 |
| Bank of NY Mellon Corp   | \$ 2,935          | 0.90%                 |
| Charles Schwab Corp  | \$ 2,050          | 0.63%                 |
| Chubb INA Holdings Inc   | \$ 2,474          | 0.76%                 |
| Cisco Systems  | \$ 2,919          | 0.89%                 |
| Coca Cola Company  | \$ 1,972          | 0.60%                 |
| FirstBank  | \$ 5,155          | 1.58%                 |
| Great Western  | \$ 4,089          | 1.25%                 |
| IBM Credit Corp  | \$ 2,474          | 0.76%                 |
| Intel Corp   | \$ 2,492          | 0.76%                 |
| Microsoft  | \$ 2,906          | 0.89%                 |
| Northern Trust Company   | \$ 2,848          | 0.87%                 |
| Oracle Corp  | \$ 2,917          | 0.89%                 |
| Pepsico Inc.   | \$ 2,481          | 0.76%                 |
| Praxair  | \$ 2,466          | 0.75%                 |
| State Street Bank  | \$ 3,008          | 0.78%                 |
| UPS  | \$ 2,514          | 0.77%                 |
| Visa Inc   | \$ 2,475          | 0.76%                 |
| Wal-Mart Stores  | \$ 3,003          | 0.77%                 |
| Walt Disney Company  | \$ 985            | 0.30%                 |
| <b>Total Book Value</b>  | <b>\$ 327,234</b> | <b>100%</b>           |

| <b>Holding Details for City of Boulder<br/>Enhanced Cash Portfolio</b> |                   |                       |
|--|-------------------|-----------------------|
| <b>Issuer</b>  | <b>Book Value</b> | <b>% of Portfolio</b> |
| Eli Lilly & Co   | \$ 500            | 8.07%                 |
| FHLMC  | \$ 1,800          | 29.02%                |
| FNMA   | \$ 3,002          | 48.41%                |
| US Treasury  | \$ 899            | 14.50%                |
| <b>Total Book Value</b>  | <b>\$ 6,201</b>   | <b>100.00%</b>        |