City of Boulder

City of Boulder

Finance Department

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

FROM: Cheryl Pattelli, Director of Finance

SUBJECT: Investment Performance as of March 31, 2016

DATE: April 18, 2016

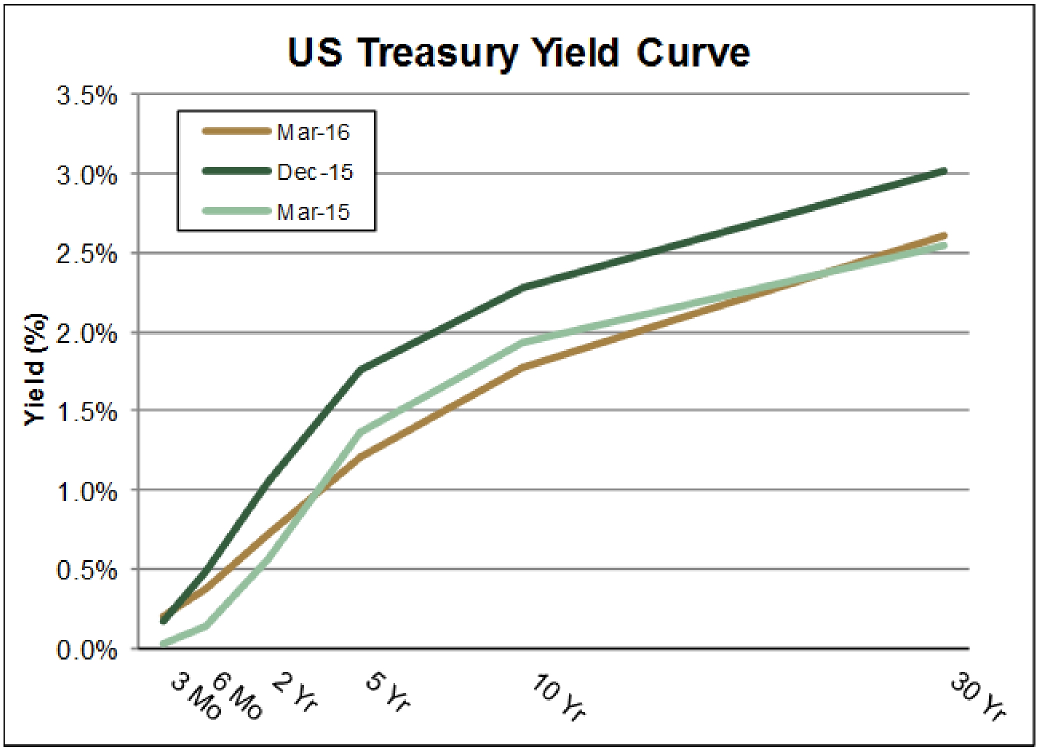
Section 1 – Background

- 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")

Treasury Yield Curve

03/31/2015 vs. 12/31/2015 vs. 03/31/16



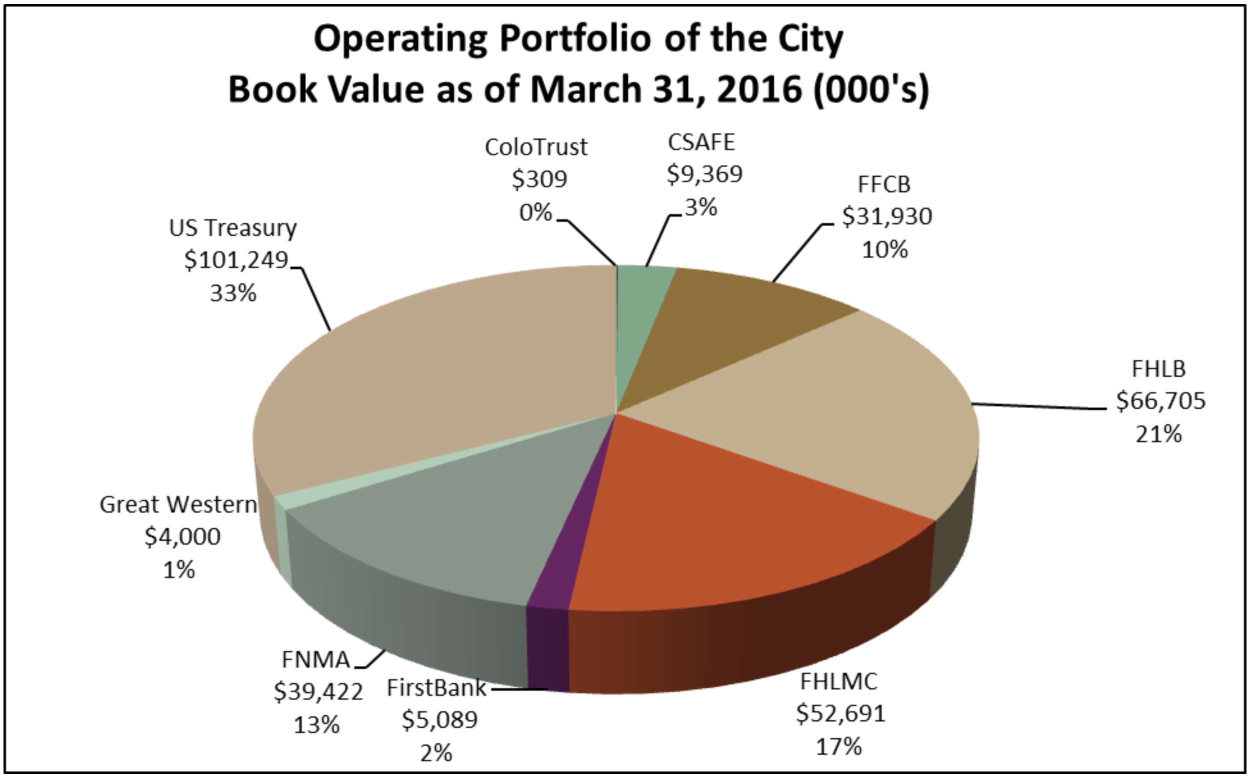
Source: Bloomberg

- During the first quarter, the yield curve flattened with the 2-year Treasury yield down about 33 basis points and the 10-year Treasury yield down about 50 basis points. Over much of the past year, financial market volatility has been elevated due to weak global economic growth, declining commodity prices, and divergent global central bank monetary policy. These concerns will likely continue to fuel financial market volatility over the medium-term.
- The Federal Open Market Committee (FOMC) left policy rates unchanged in March. The minutes from the March FOMC meeting highlighted the debate among policymakers about the appropriate pace of monetary policy normalization. Two Fed members (including the lone dissenter among voting members, Esther George) were pushing for a 25 basis point rate hike at the March meeting. Meanwhile, other Fed members expressed concern about raising rates too quickly. Several policymakers expressed the view that economic and financial conditions abroad posed risks to the US economy and labor market. Some officials suggested that a rate hike in April might signal a sense of urgency that was not appropriate, while others thought that a rate hike in April might be warranted. Meanwhile policymakers also discussed whether inflation was approaching a normal pace or if it remained too weak. Based on our view of the overall economy and our interpretation of recent comments made by members of the Fed, we believe a fed funds rate hike at the upcoming April 26-27 FOMC meeting is unlikely. However, we believe the door remains open for a 25 basis point hike in June, and potentially another 25 basis point hike at the end of this year.

Section 3 – The City's Portfolios

- Portfolio strategies implemented this quarter and all investments held in the portfolio 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. Market risk is managed by maintaining a low weighted average maturity (WAM) in the City's portfolio. As of March 31, 2016 the WAM was 1.76 years while the Ordinance allows up to a five year WAM.
    - The City maintains sufficient liquidity. As of March 31, 2016, 3.0% of the portfolio, or $9.6 million remained in overnight accounts.
    - As of March 31, 2016, the yield on the pooled investment portfolio was 1.05%. Our current benchmark is the six month trailing average on the 2-year Treasury, which was 0.84%, as of March 31, 2016. The objective was exceeded by 0.21%.
- There are no investments in the oil and gas industry in the City's portfolio.
- The City's investment adviser purchased approximately $44.9 million of securities during Q1 2016 for the City of Boulder's investment portfolio. The proceeds of $22.0 million of maturities along with existing liquid funds were used to fund the security purchases. The security purchases included Treasury and Agency securities maturing between March 2018 and February 2021. These securities were purchased in this maturity range to maintain the portfolio characteristics in line with the strategy. During the first quarter, the Federal Open Market Committee (FOMC) left the fed funds target rate unchanged at a range of 0.25%-0.50%. Throughout the quarter, the FOMC continued to emphasize that the pace of future rate hikes would be gradual. The FOMC policy statement (in March) was largely dovish and the Committee's consensus forecast for the year-end target federal funds rate was revised down to a level more closely aligned with market expectations. The FOMC's median forecast now implies two rate hikes in 2016 versus the previous forecast of four rate hikes. Based on our view of the overall economy and our interpretation of recent comments made by members of the Fed, we believe a fed funds rate hike at the upcoming April 26-27 FOMC meeting is unlikely. However, we believe the door remains open for a 25 basis point hike in June, and potentially another 25 basis point hike at the end of this year. The yield on the two-year Treasury note declined approximately 0.32% in December to 0.73%%. Meanwhile, the yield on the ten-year Treasury note decreased 0.40% in December to 1.78%. Looking ahead, we believe the pace of subsequent rate hikes will be slower than historical Fed tightening cycles, in light of ongoing sluggishness in the global economy.

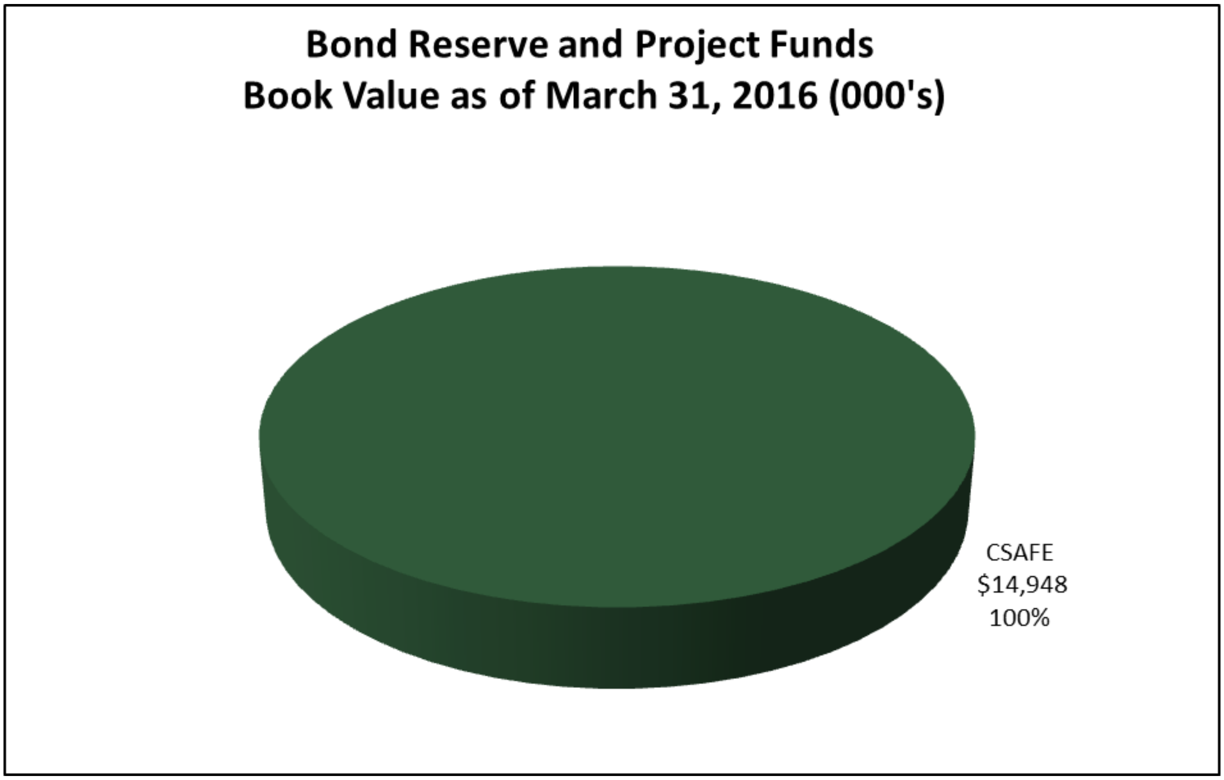
Operating Portfolio of the City



Portfolio Characteristics
City of Boulder Consolidated Non CIP

	03/31/2016	12/31/2015
	Portfolio	**Portfolio**
Average Maturity (yrs)	1.76	1.65
Modified Duration	1.72	1.61
Average Purchase Yield	1.054%	0.98%
Average Market Yield	0.746%	0.985%
Average Quality**	AA+/Aaa	AA+/Aaa
Total Market Value	313,301,575	288,266,472

Bond Reserve and Project Funds



Portfolio Characteristics
Bond Reserve and Project Funds

	03/31/2016	12/31/2015
	Portfolio	**Portfolio**
Average Maturity (yrs)	0.00	0.00
Modified Duration	0.00	0.00
Average Purchase Yield	0.50%	0.238%
Average Market Yield	0.50%	0.238%
Average Quality	AAA/NR	AAA/NR
Total Market Value	14,947,836	14,931,141

When the Bond Reserve and Project Funds proceeds of over $54 million were received in March 2012, a separate portfolio was established to facilitate IRS required arbitrage calculations. The balance of $14.9 million as of March 31, 2016 was invested as shown above in the graph and table to assure timely funding for the projected draw down schedule expected to end in January 2015.

- 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 March 31, 2016 the portfolio yield was 0.50%.
- Daily liquidity in the portfolio is currently 100% of the portfolio, or $14.9 million, resulting in a very short weighted average maturity of 0.0 years. The portfolio has virtually no market risk and 100% of the funds are available for immediate draw down as projects need funding. This portfolio structure safely supports the short liability duration of the projects that are expected to end in January 2015.