




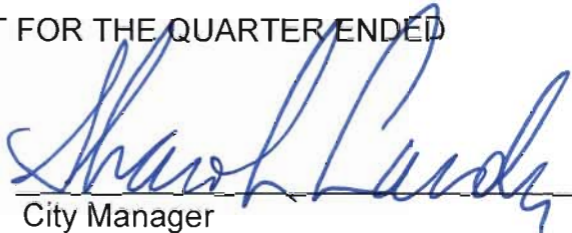
REQUEST FOR CITY COUNCIL ACTION

MEETING DATE: June 28, 2016

TITLE: TREASURER'S REPORT FOR THE QUARTER ENDED
MARCH 31, 2016



Director of Administrative Services



City Manager

RECOMMENDED ACTION

Receive and file the Treasurer's Report for the quarter ended March 31, 2016.

EXECUTIVE SUMMARY

This report provides a synopsis of investment activity for the City's three investment portfolios for the quarter ended March 31, 2016. These portfolios, which are managed by United American Capital Corporation (UACC) under the direction of the Treasurer, are categorized as the Irvine Pooled Investment Portfolio, Bond Proceeds Fund and Special District Funds. The market value of all investments under the Treasurer's management totaled \$830.56 million as of March 31, 2016.

Portfolio assets, allocations, average maturities, yields, and portfolio valuations are presented within this report. A discussion of market conditions is also provided to give perspective to these measurements.

COMMISSION/BOARD/COMMITTEE RECOMMENDATION

The Finance Commission, at its regular meeting of June 20, 2016, recommended the City Council receive and file the Treasurer's Report by a 4-0-1 vote (Chair Dressler, Commissioners Koh, Montgomery and Reyno approving; Vice Chair Bartlett absent). The Investment Advisory Committee, at its regular meeting of May 11, 2016, recommended City Council receive and file the Treasurer's Report by a 3-0-2 vote (Chair Shanahan, Vice Chair Judd, Committee Member Carney approving; Committee Members Gonzales and Greenberg absent).

ANALYSIS

The Treasurer's office is responsible for the investment of the City's three fixed income portfolios in conformance with the Annual Investment Policy adopted by City Council. In accordance with the Investment Policy, management of the Irvine Pooled Investment Portfolio, Bonds Proceeds Portfolio and the Special Districts Portfolio have been

delegated to a contract management firm, UACC, with full authority to execute investment transactions on behalf of the City. The Investment Policy is updated annually in accordance with the California State Government Code. Quarterly and annual Treasurer's reports are provided on investment activity and performance information for the City's portfolios and submitted to the Investment Advisory Committee, Finance Commission, and City Council. The primary objectives of investing public funds, in order of importance, are safety of principle, liquidity of funds, and return on investment. All securities owned by the City are held in safekeeping by a third party custodial bank acting as the agent for the City rather than held by a securities dealer or investment management firm. Any trade executed with a broker/dealer is required to settle with the City's safekeeping agent on a delivery versus payment basis, where the delivery of a security to the appropriate party is made only in the event the funds have been sent in full as payment for the security.

Irvine Pooled Investment Portfolio

The Irvine Pooled Investment Portfolio contains funds invested for the daily operational requirements of the City and funds reserved for economic uncertainties, future rehabilitation and maintenance needs. The Irvine Pooled Investment Portfolio is a combination of several operational funds, including the City's Asset Management Plan and funds earmarked for the development of the Orange County Great Park.

As of March 31, 2016, the book value (purchase price of securities as recorded on the City's books) of the Irvine Pooled Investment Portfolio was \$533.39 million and the average weighted yield to maturity was 1.05 percent. Year-to-date investment revenue (interest payments and capital gains) generated by the Irvine Pooled Investment Portfolio as of March 31, 2016 was \$3.06 million. The following chart compares the Irvine Pooled Investment Portfolio statistics over a rolling 12-month period.

**Irvine Pooled Investment Portfolio
 Rolling 12-Month Quarterly Comparison**

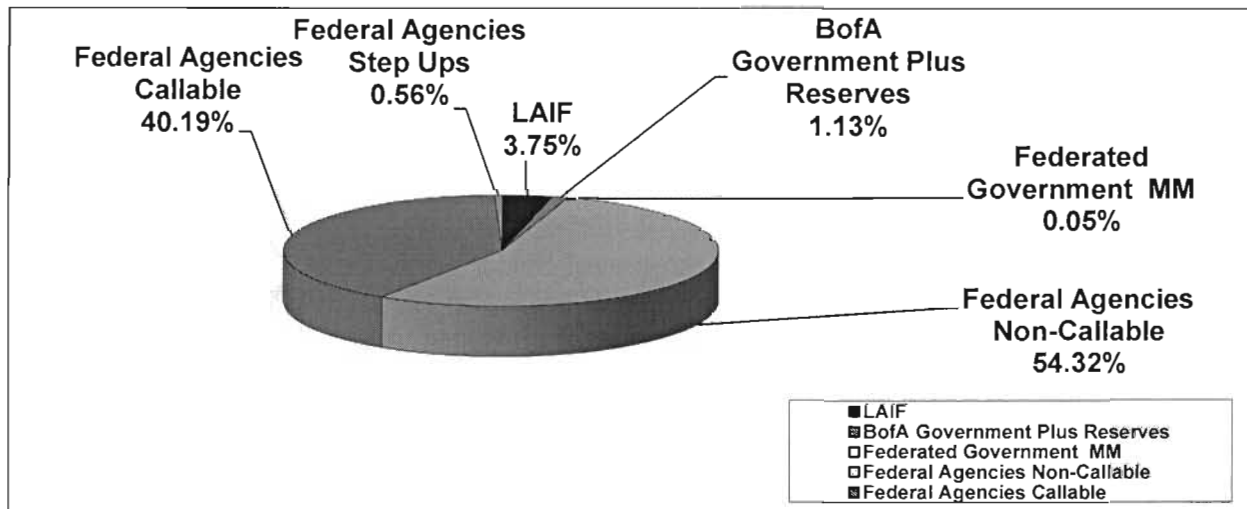
	March 31, 2016	Dec 31, 2015	Sept 30, 2015	June 30, 2015
Book Value	\$533,389,906	\$478,816,519	\$461,135,393	\$486,857,944
Market Value	\$535,191,367	\$477,843,844	\$462,618,007	\$487,453,132
Unrealized Gain/(Loss)	\$1,801,461	(\$972,675)	\$1,482,614	\$595,188
Unrealized Gain/(Loss) as % of Book Value	0.34%	(0.20%)	0.32%	0.12%
Average Yield To Maturity	1.05%	1.01%	0.98%	0.89%
Liquidity 0 –6 months	10.95%	10.95%	9.85%	14.20%
Average Years To Maturity	2.02	2.02	2.07	2.00
Modified Duration (Years)	1.98	1.96	1.99	1.85
Fiscal Year to Date Income	\$3,057,399	\$2,114,558	\$890,371	\$3,442,567

The Irvine Pooled Investment Portfolios book value increased by \$54.57 million from the last quarter. The increase in book value was due to a combination of property tax revenues, sales tax revenues, developer fees and the cyclical nature of the City's revenue stream that often fluctuates \$10 to \$50 million each quarter. Portfolio yield to maturity increased for the quarter ended March 31, 2016 by four basis points to 1.05 percent. The increase in portfolio yield was due to maturing and called securities being reinvested into higher yielding securities. With rates decreasing during the quarter ending March 31, 2016, the Irvine Pooled Investment Portfolio ended the quarter with an unrealized gain of \$1,801,461. This is a normal result of the Irvine Pooled Investment Portfolio's modified duration of 1.98 years, and its price-sensitivity to changes in market interest rates.

To ensure the safety of the portfolio, investments that hold the highest credit quality are selected. The Irvine Pooled Investment Portfolio is comprised primarily of Federal Government sponsored entity debt, otherwise known as Federal Agencies. Although the Federal Agency securities were downgraded by Standard & Poor's to AA+ in August 2011, they continue to be regarded as among the safest securities in the global market. Two of the government sponsored agencies, Federal National Mortgage Association (Fannie Mae) and Federal Home Loan Mortgage Company (Freddie Mac), remain under conservatorship by the Federal Government and carry an implicit guarantee by the Federal Government. Both of these agencies are carefully monitored by the City's investment manager to ensure the continued safety of the City's funds.

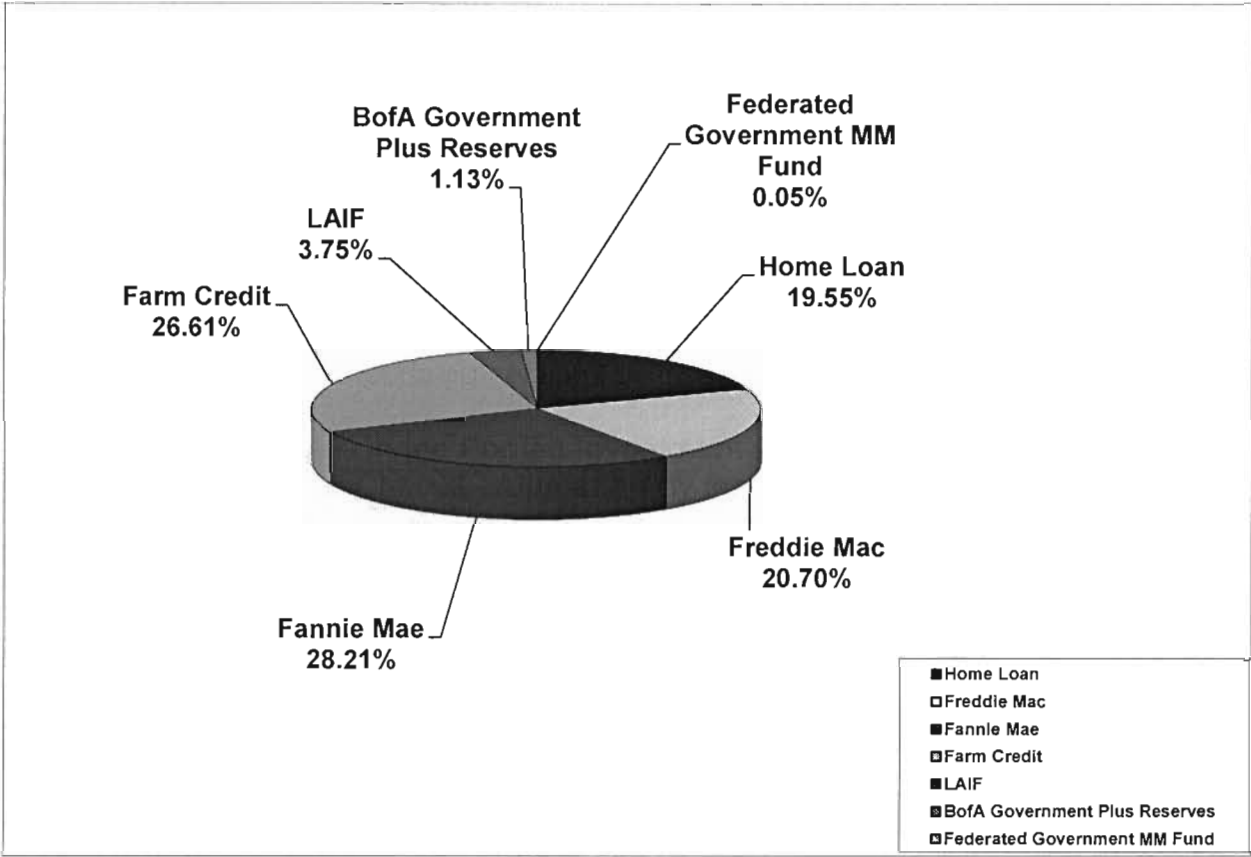
To manage liquidity, the Irvine Pooled Investment Portfolio is invested in Local Agency Investment Funds (LAIF), the Federated Government Obligation money market fund, and the Bank of America Government Plus Reserves fund. Chart 1 shows the asset allocation of the Irvine Pooled Investment Portfolio.

**Irvine Pooled Investment Portfolio
 Chart 1 - Asset Allocation
 as of March 31, 2016**



To diversify, the City purchases securities from several different Federal Agencies. The four Federal Government sponsored entities the City owns are, Federal National Mortgage Association (Fannie Mae), Federal Home Loan Mortgage Corporation (Freddie Mac), Federal Home Loan Bank (Home Loan), and Federal Farm Credit Bank (Farm Credit). Chart 2 identifies portfolio holdings by issuer name.

**Irvine Pooled Investment Portfolio
Chart 2 - Allocation by Issuer Name
as of March 31, 2016**



Another key component in portfolio management is to ensure that the City has enough funds on hand to meet current expenses. As of March 31, 2016, the overnight to 6-month liquidity level for the Irvine Pooled Investment Portfolio was at 9.78 percent versus 10.95 percent last quarter. Chart 3, on the following page, is an aging of investment maturities up to five years (the maximum maturity allowable by policy and state code) of the Irvine Pooled Investment Portfolio.

Irvine Pooled Investment Portfolio
Chart 3 - Aging of Maturing Investments (Maturity Value)
as of March 31, 2016

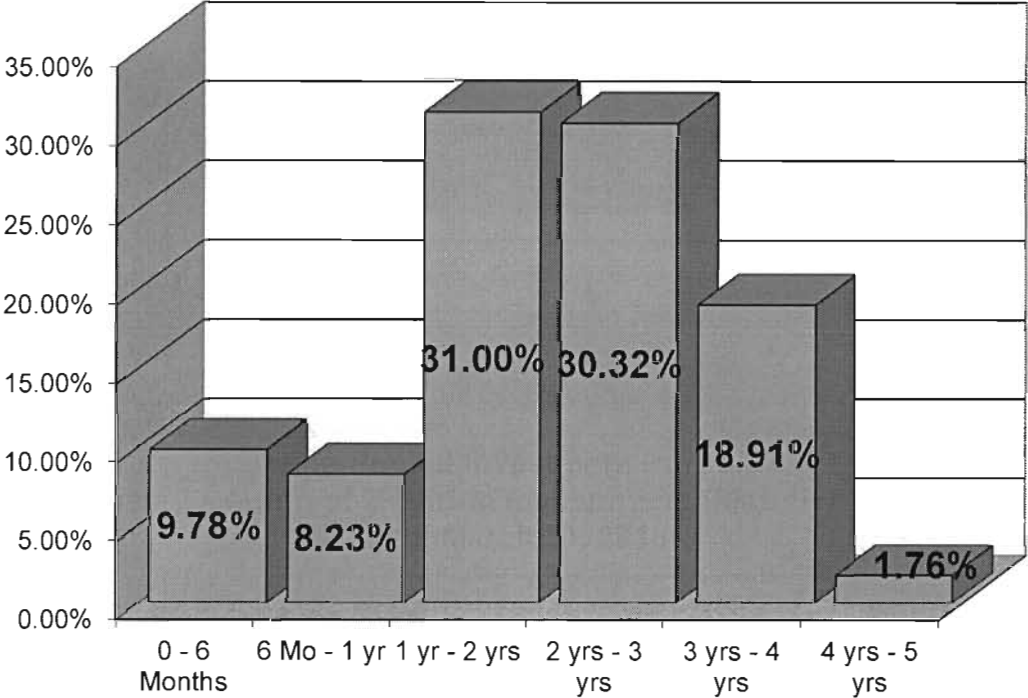
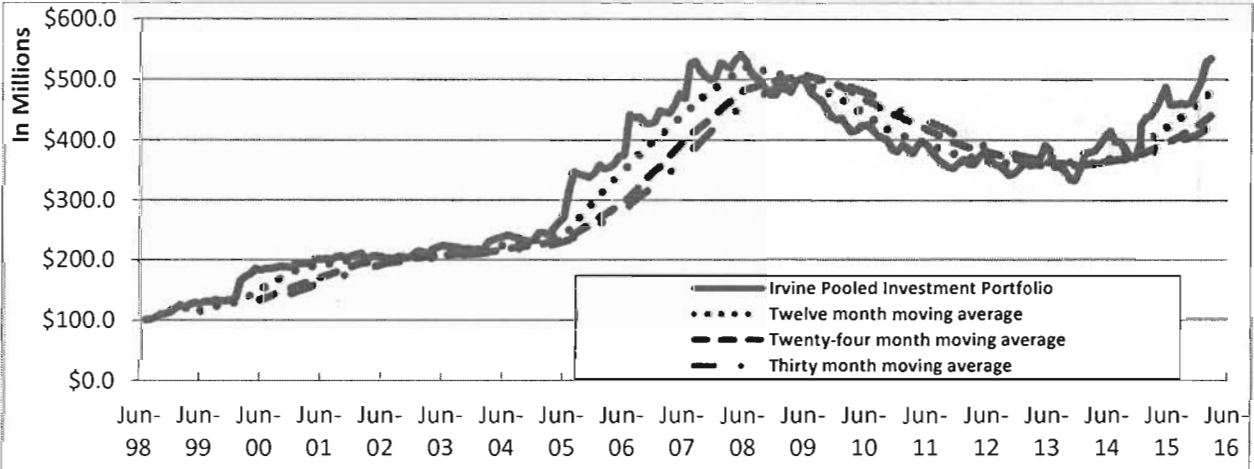
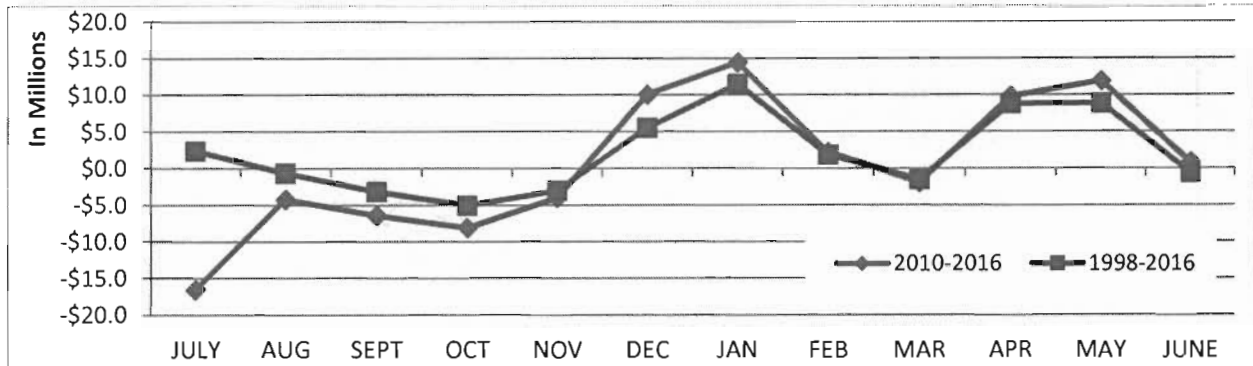


Chart 4 and chart 5 show the volatility and cyclicalty of the Irvine Pooled Investment Portfolio fund balance and cash flows between June 1998 and March 2016.

Irvine Pooled Investment Portfolio
Chart 4 - Portfolio Balance
June 30, 1998 through March 31, 2016

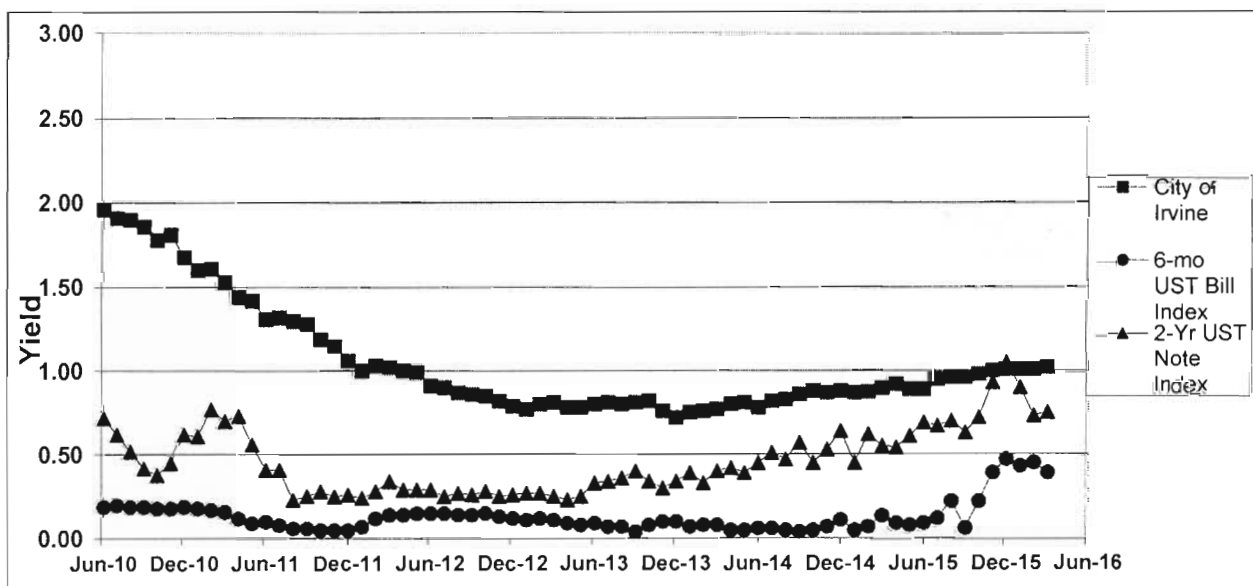


**Irvine Pooled Investment Portfolio
 Chart 5 – Balance Change Month by Month (Average)**



To gauge performance, the City compares the Irvine Pooled Investment Portfolio's yield to maturity against two benchmarks set in the City's Annual Investment Policy; the 6-month United States Treasury (UST) Bill Index and 2-year UST Note Index. The benchmarks are used as a measure of the Irvine Pooled Investment Portfolio against market movement. Chart 6 compares the average yield to maturity of the Irvine Pooled Investment Portfolio to these benchmarks, and shows the spread (difference between the index and the yield to maturity) for the past five and a half years. The Portfolio's yield is higher than the 6-month UST by 0.63 percent and higher than the 2-year UST by 0.27 percent.

**Irvine Pooled Investment Portfolio
 Chart 6 - Yield to Maturity Compared to Assigned Benchmarks
 June 30, 2010 through March 31, 2016**



Bond Proceeds Fund Portfolio

The Bond Proceeds Fund Portfolio contains special district construction and administration funds that are not held by a trustee. These include older bond issues, funds on hand to finance the City’s assessment district inspection and administration, and property assessments received from the County prior to being sent to the trustee. Investment strategy differs in the Bond Proceeds Fund Portfolio from the Irvine Pooled Investment Fund Portfolio due to different cash needs between the two. The Bond Proceeds Fund Portfolio requires greater liquidity to meet debt service payments. Fiscal year-to-date investment revenue (interest payments and capital gains) generated by the Bond Proceeds Fund Portfolio as of March 31, 2016 was \$41,276.

**Bond Proceeds Portfolio
 Rolling 12-Month Quarterly Comparison**

	March 31, 2016	Dec 31, 2015	Sept 30, 2015	June 30, 2015
Book Value	\$4,986,436	\$12,852,436	\$7,378,436	\$9,659,436
Market Value	\$4,987,538	\$12,841,987	\$7,382,823	\$9,663,068
Unrealized Gain/(Loss)	\$1,102	(\$10,449)	\$4,387	\$3,632
Unrealized Gain/(Loss) as % of Book Value	0.02%	(0.08%)	0.06%	0.04%
Average Yield To Maturity	0.51%	0.40%	0.33%	0.30%
Liquidity 0 –6 months	100.00%	100.00%	100.00%	100.00%
Average Days To Maturity	1	1	1	1
Modified Duration in Days	1	1	1	1
Fiscal Year to Date Income	\$41,276	\$33,967	\$27,359	\$57,099

Special District Funds Portfolio

The Special District Funds Portfolio contains project and reserve funds for 25 assessment district bond issues and three community facilities district bond issues. Investments in this Portfolio are made in accordance with each bond’s indenture and the strategy is set according to the cash flow needs of the individual district. The Special District Funds Portfolio must also remain very liquid to provide project funds, when requested, as well as meet debt service payment requirements. Fiscal year-to-date investment revenue (interest payments and capital gains) generated by the Special District Funds Portfolio as of March 31, 2016 was \$463,659.

**Special District Funds Portfolio
 Rolling 12-Month Quarterly Comparison**

	March 31, 2016	Dec 31, 2015	Sept 30, 2015	June 30, 2015
Book Value	\$290,492,013	\$335,498,764	\$231,674,282	\$259,740,586
Market Value	\$290,412,175	\$335,376,664	\$231,713,444	\$259,757,661
Unrealized Gain/(Loss)	(\$79,838)	(\$122,100)	\$39,162	\$17,075
Unrealized Gain/(Loss) as % of Book Value	(0.03%)	(0.04%)	0.02%	0.01%
Average Yield To Maturity	0.24%	0.15%	0.17%	0.12%
Average Days To Maturity	71	75	132	131
Fiscal Year to Date Income	\$463,659	\$188,223	\$90,717	\$266,330

Market Conditions

Interest rates decreased with the yield curve flattening between the 6-month Treasury Bill and 30-year Treasury bond during the third quarter FY 2015-16. The 6-month Treasury bill decreased 9.80 basis points ending the period at 0.37 percent. Two-year Treasury notes decreased by 32.70 basis points to 0.72 percent, and the 5-year Treasury note decreased by 55.80 basis points to 1.19 percent.

Following the first Federal Funds rate hike in December 2015 since June 2006, market consensus changed dramatically in January. A combination of worldwide financial and economic imbalances, coupled with sluggish global growth and negative interest rates in major markets, shifted market sentiment to price-in a possible recession. Equity prices fell and bond prices rose during the first half of the quarter as investors chose safe haven assets. On February 11, 2016, the U.S. Federal Reserve Chair Janet Yellen testified before the Senate Banking Committee and proceeded to calm financial markets by explaining the Federal Reserve's view of price stability and full employment. Following Janet Yellen's testimony, equity markets domestically and globally rose and ended the quarter where they began.

U.S. unemployment remained the same as reported by the Labor Department for February at 4.90 percent with average hourly earnings rising 2.30 percent year over year. The Consumer Price Index (excluding Food and Energy) continued to rise during the quarter to 2.30 percent year over year. New and existing home sales were lower at the end of the quarter but continue to remain above recent trend levels.

Looking forward to the fourth quarter FY 2015-16, the Federal Reserve has remained committed to focusing on its dual mandate of full employment and price stability. Future Federal Funds rate hikes will be subject to domestic and global financial market conditions and stability.

ALTERNATIVES CONSIDERED

None. The Treasurer's Report is intended to provide historical information about the City's investment portfolios. Pursuant to the City's Investment Policy, the Treasurer is required to submit quarterly Treasurer's reports to the City Council.

FINANCIAL IMPACT

Fiscal year-to-date investment income for the Irvine Pooled Investment Portfolio, Bond Proceeds, and Special Districts portfolios totaled \$3.56 million with investments structured for security and liquidity.

REPORT PREPARED BY Don Collins, City Treasurer