



REQUEST FOR CITY COUNCIL ACTION

MEETING DATE: MARCH 22, 2016

TITLE: TREASURER'S REPORT FOR THE QUARTER ENDED
DECEMBER 31, 2015



Director of Administrative Services



City Manager

RECOMMENDED ACTION

Receive and file the Treasurer's Report for the quarter ended December 31, 2015.

EXECUTIVE SUMMARY

This report provides a synopsis of investment activity for the City's three investment portfolios for the quarter ended December 31, 2015. 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 \$826.06 million as of December 31, 2015.

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 March 7, 2016, recommended the City Council receive and file the Treasurer's Report for the quarter ended December 31, 2015 by a unanimous vote of 4-0 (Commissioner Montgomery absent). The Investment Advisory Committee, at its regular meeting of February 10, 2016, recommended City Council receive and file the Treasurer's Report by a unanimous vote of 4-0 (Committee Member 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 principal, 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 December 31, 2015, the book value (purchase price of securities as recorded on the City’s books) of the Irvine Pooled Investment Portfolio was \$478.8 million and the average weighted yield to maturity was 1.01 percent. Year-to-date investment revenue (interest payments and capital gains) generated by the Irvine Pooled Investment Portfolio as of December 31, 2015 was \$2.11 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**

	Dec 31, 2015	Sept 30, 2015	June 30, 2015	March 31, 2015
Book Value	\$478,816,519	\$461,135,393	\$486,857,944	\$439,932,507
Market Value	\$477,843,844	\$462,618,007	\$487,453,132	\$440,906,767
Unrealized Gain/(Loss)	(\$972,675)	\$1,482,614	\$595,188	\$974,260
Unrealized Gain/(Loss) as % of Book Value	(0.20%)	0.32%	0.12%	0.22%
Average Yield To Maturity	1.01%	0.98%	0.89%	0.90%
Liquidity 0 –6 months	10.95%	9.85%	14.20%	9.07%
Average Years To Maturity	2.02	2.07	2	2.17
Modified Duration (Years)	1.97	1.99	1.85	2.09
Fiscal Year to Date Income	\$2,114,558	\$890,371	\$3,442,567	\$2,389,389

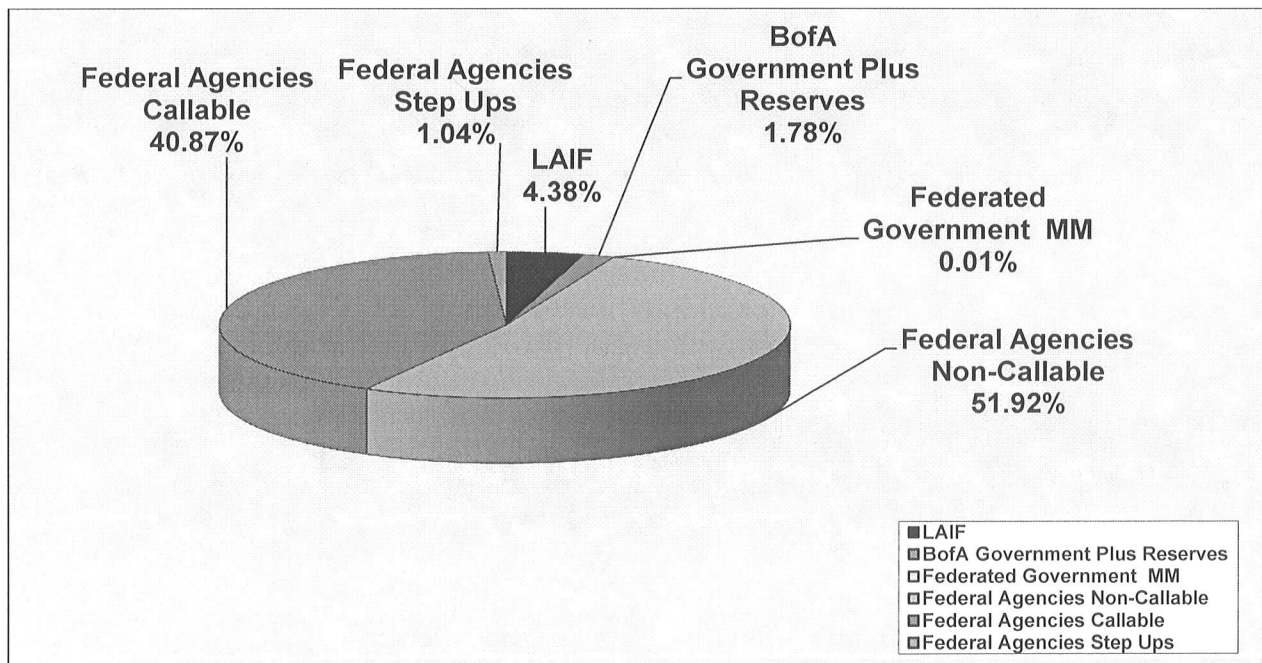
The Irvine Pooled Investment Portfolios book value increased by \$17.68 million from the last quarter. The increase in book value was due to receipt of December property tax revenues and the cyclical nature of the City’s revenue stream that often fluctuates \$10 to \$40 million each

quarter. Portfolio yield to maturity increased for the quarter ended December 31, 2015 by 3 basis points to 1.01 percent as available liquidity was invested in higher yielding assets. With rates increasing during the quarter ending December 31, 2015, the Irvine Pooled Investment Portfolio ended the quarter with an unrealized loss of \$972,675. This is a normal result of the Irvine Pooled Investment Portfolio's modified duration of 1.97 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.

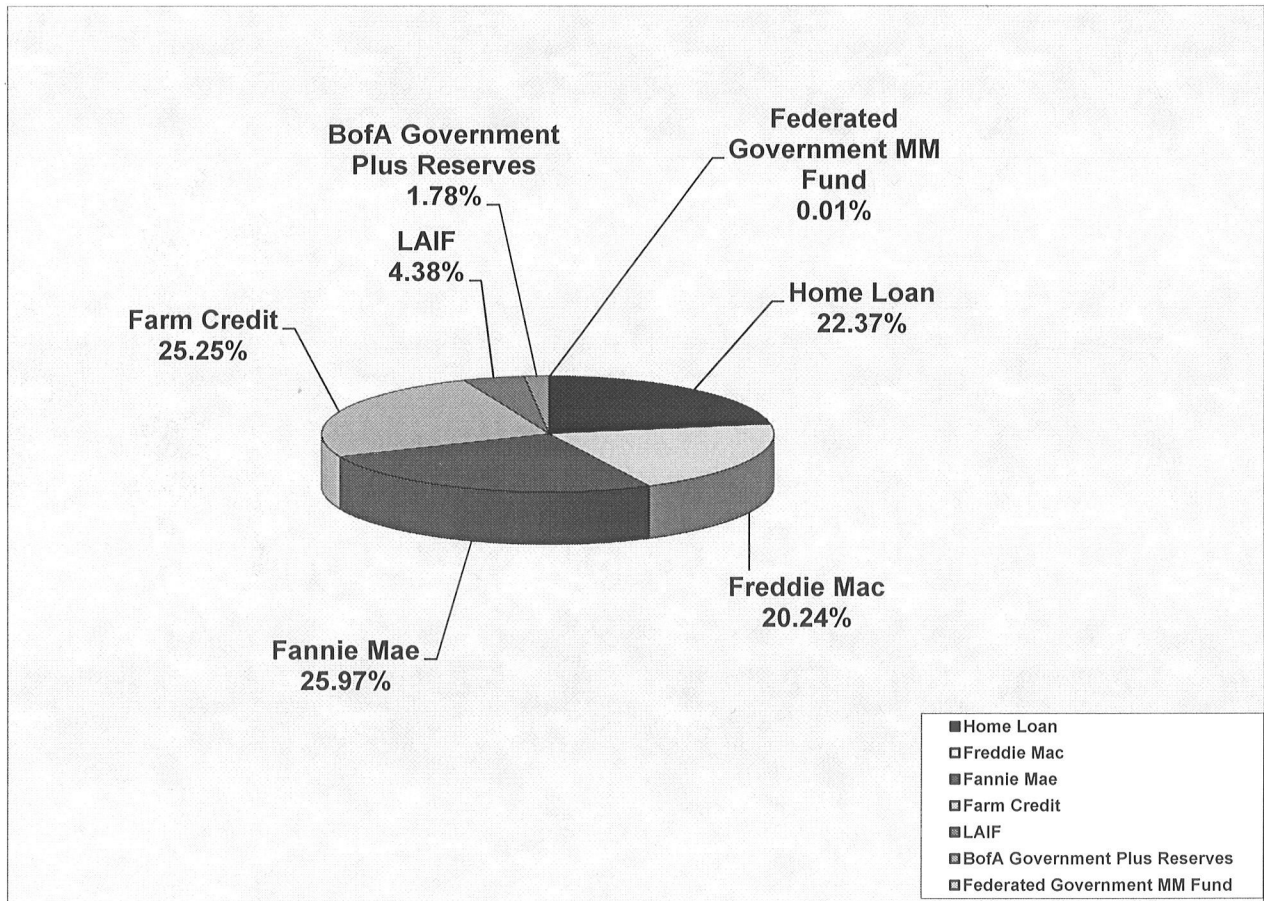
To manage liquidity, the Irvine Pooled Investment Portfolio is invested in Local Agency Investment Funds (LAIF), Federated Government Obligation money market fund, and the Bank of America Government Plus Reserves fund. Chart 1 shows the asset allocation of the Irvine Pooled Investment Portfolio.

**Irvine Pooled Investment Portfolio
Chart 1 - Asset Allocation
as of December 31, 2015**



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 December 31, 2015**



Another key component in portfolio management is to ensure that the City has enough funds on hand to meet current expenses. As of December 31, 2015, the overnight to 6-month liquidity level for the Irvine Pooled Investment Portfolio was at 10.95 percent versus 9.85 percent last quarter. Chart 3, on the following page, is an aging of investment maturities up to 5 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 December 31, 2015

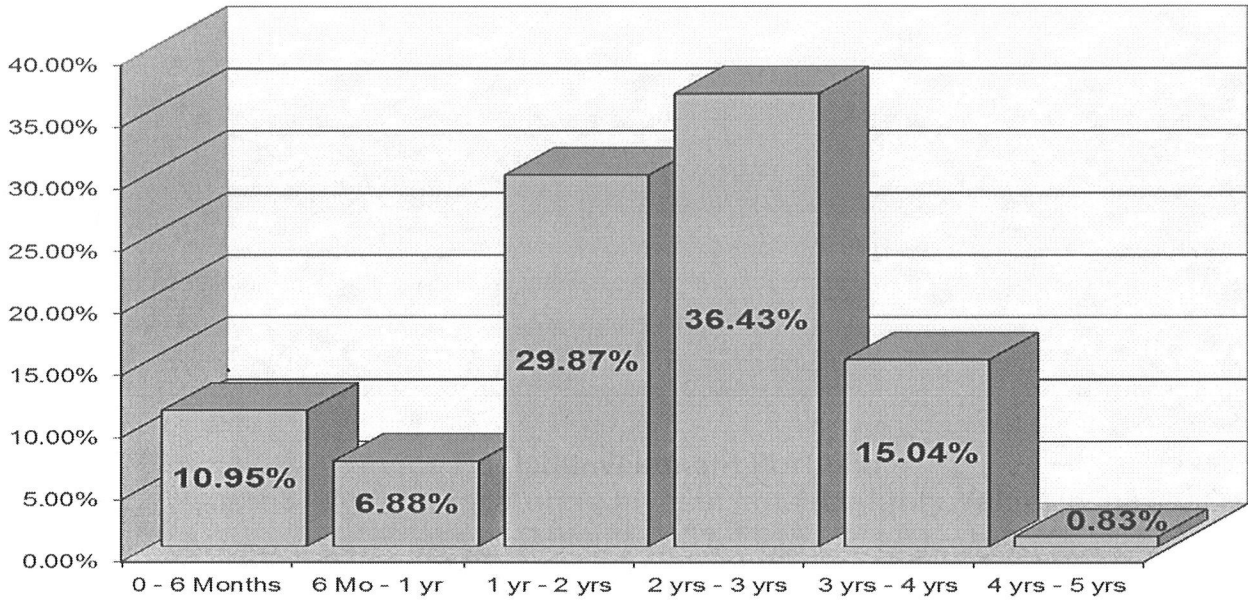
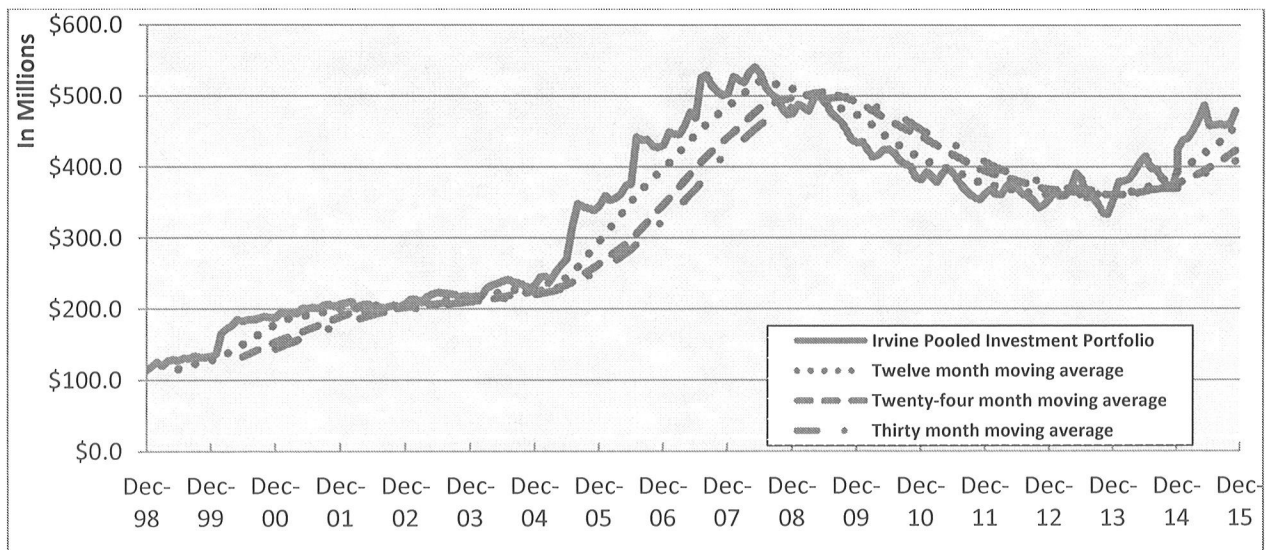
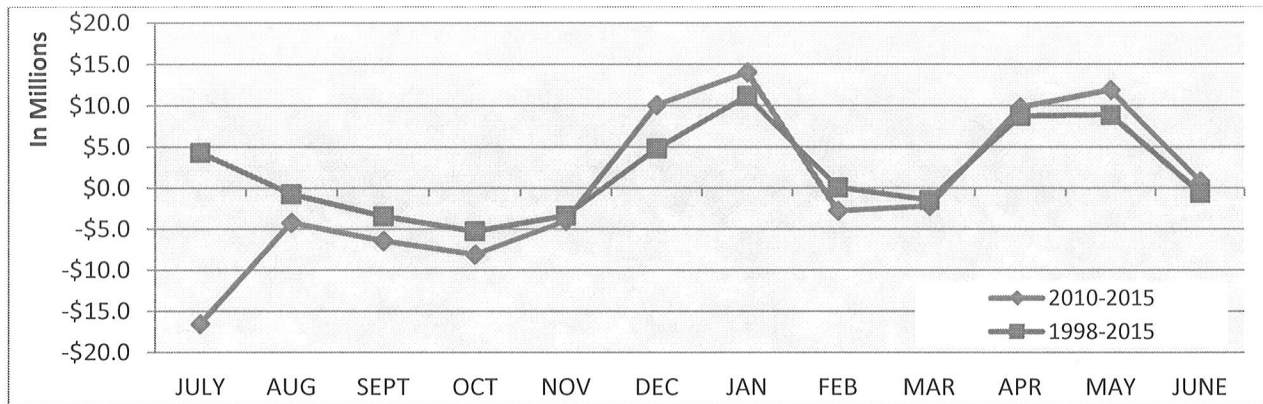


Chart 4 and chart 5 show the volatility and cyclicity of the Irvine Pooled Investment Portfolio fund balance and cash flows between December 1998 and December 2015.

Irvine Pooled Investment Portfolio
Chart 4 - Portfolio Balance
December 31, 1998 through December 31, 2015

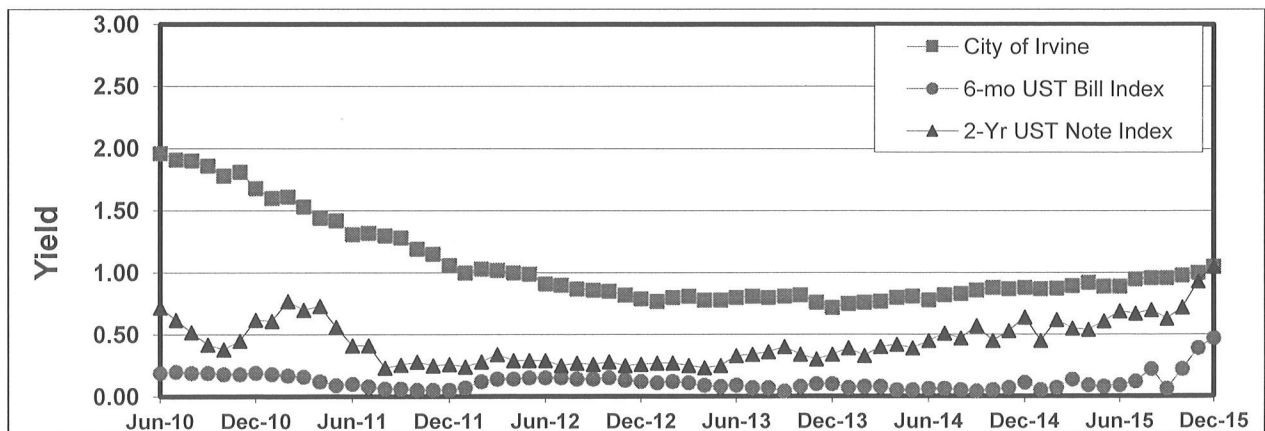


Irvine Pooled Investment Portfolio
Chart 5 – Balance Change Month by Month (Average)
 July 31, 1998 through December 31, 2015



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 0.54 percent and lower than the 2-year UST by 0.04 percent.

Irvine Pooled Investment Portfolio
Chart 6 - Yield to Maturity Compared to Assigned Benchmarks
 June 2010 through December 2015



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 December 31, 2015 was \$33,965.

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

	Dec 31, 2015	Sept 30, 2015	June 30, 2015	March 31, 2015
Book Value	\$12,852,436	\$7,378,436	\$9,659,436	\$50,000,436
Market Value	\$12,841,987	\$7,382,823	\$9,663,068	\$50,019,622
Unrealized Gain/(Loss)	(\$10,449)	\$4,387	\$3,632	\$19,186
Unrealized Gain/(Loss) as % of Book Value	(0.08%)	0.06%	0.04%	0.04%
Average Yield To Maturity	0.40%	0.33%	0.30%	0.28%
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	\$33,965	\$27,359	\$57,099	\$36,823

Special District Funds Portfolio

The Special District Funds Portfolio contains project and reserve funds for 25 assessment district bond issues and four 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 December 31, 2015 was \$188,223.

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

	Dec 31, 2015	Sept 30, 2015	June 30, 2015	March 31, 2015
Book Value	\$335,498,764	\$231,674,282	\$259,740,586	\$239,814,616
Market Value	\$335,376,664	\$231,713,444	\$259,757,661	\$239,814,344
Unrealized Gain/(Loss)	(\$122,100)	\$39,162	\$17,075	(272)
Unrealized Gain/(Loss) as % of Book Value	(0.04%)	0.02%	0.01%	0.00%
Average Yield To Maturity	0.15%	0.17%	0.12%	0.13%
Average Days To Maturity	75	132	131	149
Fiscal Year to Date Income	\$188,223	\$90,717	\$266,330	\$199,440

Market Conditions

Interest rates increased with the yield curve flattening between the two-year Treasury note and thirty-year Treasury bond during the second quarter FY 2015-16. The 3-month Treasury bill increased 18.10 basis points ending the period at 0.16 percent. Two-year Treasury notes increased by 41.90 basis points to 1.05 percent, and the five-year Treasury note increased by 40.30 basis points to 1.76 percent.

During the second quarter FY 2015-16, trading continued to be dominated by speculation that the Federal Open Market Committee (FOMC) would raise the Federal Funds rate by the December 16 meeting. Two-year Treasury note yields rose to 0.96 percent by December 15. On December 16, the FOMC increased the Federal Funds rate to 0.50 percent stating that economic activity has been expanding at a moderate pace. Household spending and business fixed investment both increased, and the housing market improved. Net exports continued to be weak due to the strong dollar.

The United States unemployment rate continued to improve during second quarter FY 2015-16, decreasing to 5.0 percent from 5.10 percent. Automobile sales reached an all-time high of 18.12 million units annualized on October 31 and remain robust. Retail sales and consumer confidence ended the quarter with gains.

The trade weighted dollar increased as the price of oil and commodities decreased during the quarter, which may lead to the importation of disinflation into the United States. Additionally, geopolitical conflicts continue to weigh on global trade and financial markets.

Looking forward to the third quarter FY 2015-16, the FOMC committee expects to raise the Fed Funds rate at its March 16 meeting with potentially three more rate hikes in 2016. Future Federal Funds rate hikes will be subject to financial market conditions both domestically and globally.

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 \$2.34 million with investments structured for security and liquidity.

REPORT PREPARED BY Don Collins, City Treasurer