

TO: The Mayor and Members of City Council
Nuria Rivera-Vandermyde, City Manager

FROM: Kara Skinner, Chief Financial Officer

SUBJECT: Investment Performance as of June 30, 2023

DATE: July 18, 2023

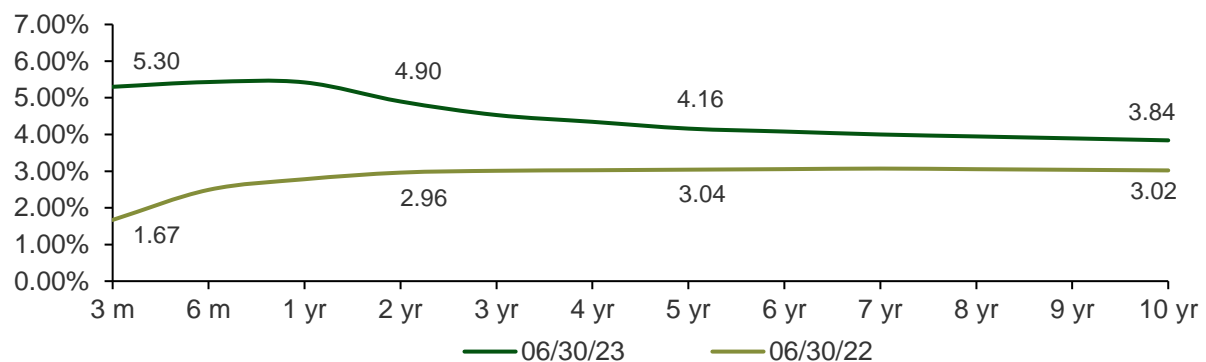
Section 1 – Background

- 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 – Market Conditions, the Federal Reserve and the Yield Curve

- A hawkish pause: After hiking rates at ten consecutive meetings, the Fed paused in June to assess the lagged impact of previous policy moves. The accompanying statement suggested further tightening ahead, and this was reinforced by hawkish comments from members of the Federal Open Markets Committee, including chair Jerome Powell. Markets repriced, building in further rate hikes.
- The Treasury curve inverted further: Government bond yields moved higher, in part reflecting a reassessment of where the peak in interest rates may be, and in part driven by jitters around the debt ceiling standoff, although this was resolved by the end of the quarter. This resulted in a further inversion of the Treasury curve, with the spread between two- and thirty-year Treasuries reaching levels not seen since the 1980s. Two-year yields ended the quarter at 4.90%, 87bp higher. At the longer end of the curve, 30-year yields ended the quarter at 3.86%, 21bp higher.
- Credit spreads tightened: Aggregate Credit spreads tightened in Q2, with aggregate US corporate spreads ending the quarter 15bp tighter than where they began. The intermediate section of the credit curve outperformed on a spread basis, with spreads tightening by 18bp. In longer maturities AA credit marginally outperformed other rating categories on a spread basis.
- The S&P 500 Index made a strong gain: US equity markets continued to perform well, with the S&P 500 Index rising by over 8.7% in Q2, taking the first half return to 16.9%.
- Risks include:
 - Further dislocations in the financial system if the Fed does keep hiking
 - Events in Europe spiral, drawing in more countries and causing market dislocations around the world
 - Tensions between China and the US spill over into conflict

Treasury Yield Curve: 06/30/2023 and 06/30/2022 (Source: Bloomberg)

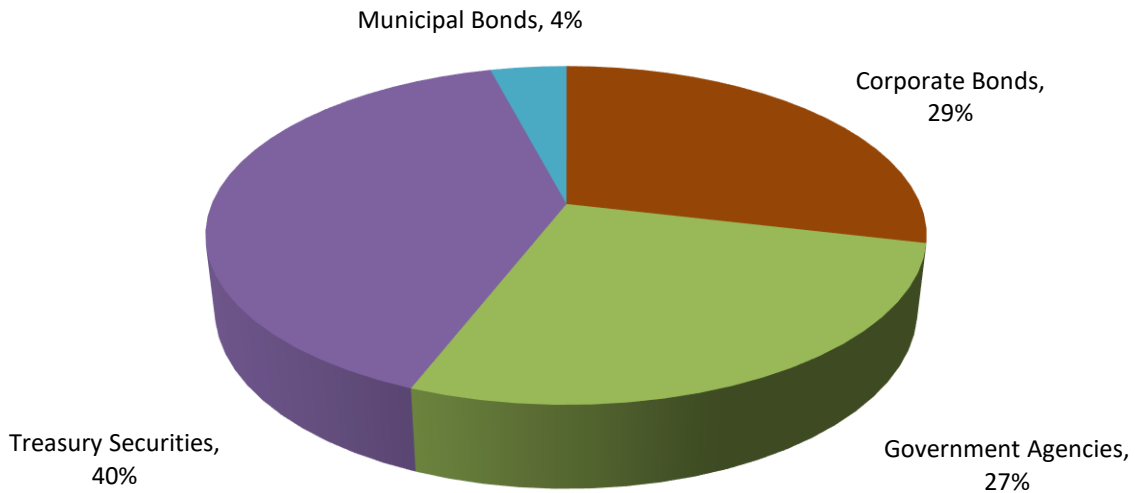


Section 3 – The City’s Portfolio

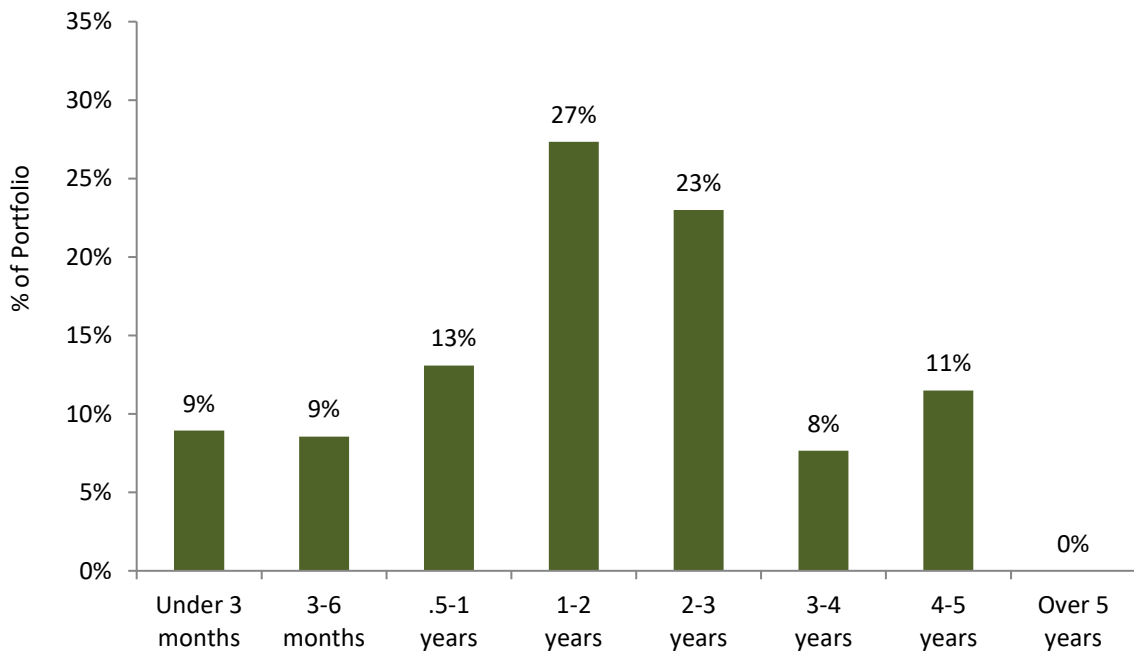
- Portfolio strategies implemented this quarter and the investments held in the portfolio comply with the City’s investment objectives and the Ordinance that specifies allowable investments.
 - The objective of safety is achieved through a well-diversified portfolio invested primarily in US Treasury and Agency securities of various maturities. In March 2017 the City Council approved amendments to the Investment Policy proposed by finance staff expanding opportunities to further diversify the portfolio. Pursuit of further diversification through the revised policies is progressing strategically relative to market conditions. Market risk is managed by maintaining a low weighted average final maturity (WAM) in the City’s portfolios. As of June 30, 2023, the WAM of the operating portfolio is 1.88 years while the Ordinance allows for a WAM of up to 5 years.
 - The City maintains sufficient liquidity. A minimum of 5% of the City’s total portfolio is held in liquidity accounts. In addition, 1.1% of the term portfolio holdings as of June 30 will mature within 30 days.
 - As of June 30, the weighted average purchase yield for the operating portfolio holdings is 2.18%. The yield benchmark is the six-month trailing average of the yield on the 2-year Treasury note, which is 4.32% as of June 30. The purchase yield on the operating portfolio as of June 30 trails the benchmark yield by 2.14%.
 - For the second quarter 2023, the fair value periodic return on the operating portfolio is negative .18%. The 1-3 Treasury Index return for the period is negative .57%. The periodic return on the operating portfolio for the second quarter is .39% higher than the 1-3 Treasury Index return.
- The City’s portfolio does not hold any investments in the following: fossil fuels inclusive of pipeline construction and extraction; firearms or weapons not used in national defense; tobacco companies; and firms related to mass incarceration/private prisons/detention centers.
- In the second quarter 2023, the City’s investment advisor invested approximately \$40 million in long-term securities for the operating portfolio. US Treasury securities, Agency bonds and corporate notes were purchased at a weighted average purchase yield of 3.97%. The weighted average maturity at the time of purchase for these investments is 4.13 years.
- The portfolio duration maintains exposure to longer-term interest rates and the portfolio is well diversified to various market sectors which may enhance the portfolio’s return over time.

City of Boulder Operating Portfolio Profile As of June 30, 2023

Asset Allocation - Historical Cost



Final Maturity Distribution - Historical Cost



Summary of Operating Portfolio Characteristics

	June 30, 2023	March 31, 2023
Average Final Maturity (years)	1.86	1.86
Modified Duration (years)	1.74	1.74
Average Purchase Yield	2.18%	2.00%
Average Market Yield	4.99%	4.37%
Average Credit Quality (S&P/Moody's)	AA+/Aa1	AA+/Aa1
Total Market Value (\$)	489,252,860	480,262,635

Portfolio Holdings as of June 30, 2023

Issuer	Historical Cost	% Portfolio
US Treasury	204,653,582	40.05%
Federal Home Loan Bank	54,889,076	10.74%
Federal National Mortgage Association	38,954,996	7.62%
Federal Farm Credit Banks	23,078,185	4.52%
Federal Home Loan Mortgage Corp	22,149,011	4.33%
John Deere Capital Corp	19,320,069	3.78%
Toyota Motor Credit Corp	17,875,160	3.50%
State Street Corp	15,961,324	3.12%
Caterpillar Financial Services Corp	15,933,213	3.12%
The Home Depot	11,936,240	2.34%
Colgate-Palmolive Co	10,754,910	2.10%
PepsiCo Inc	9,846,003	1.93%
Cisco Systems Inc	9,744,250	1.91%
3M Co	9,366,900	1.83%
Microsoft Corp	9,169,712	1.79%
City of New York, New York	8,478,013	1.66%
State of Florida	5,001,000	0.98%
State of Maryland	5,000,000	0.98%
International Business Machines Corp	4,871,700	0.95%
Apple Inc	4,606,145	0.90%
Johnson & Johnson	4,401,352	0.86%
Intel Corp	2,624,093	0.51%
Metro Oregon	2,349,820	0.46%
Cash	51,251	0.01%
Total Historical Cost	511,016,003	100.00%

Section 4 - The City's Socially Responsible Investment (SRI) Initiative

The City's investment framework includes considering socially responsible investment factors. The City's SRI program intends to allow the City to better achieve its sustainability and resilience goals, remain financially strong and better align community values. The program incorporates the strategies described below.

Exclusionary Screening. Exclusionary screening, or negative screening, is the process of excluding from investment certain sectors or companies involved in activities which are unacceptable or controversial. Investments for the City's portfolio exclude the following sectors:

- Fossil fuels inclusive of pipeline construction and extraction
- Firearms or weapons not used in national defense
- Tobacco companies
- Firms related to mass incarceration/private prisons/detention centers

Included in these negative screens is the prohibition of financial firms associated with pipeline construction. The City has further applied this limitation on financial firms to the group of broker/dealers through which investments may be transacted and the City has taken steps to remove any money market funds or cash pools that invest in the above sectors.

Positive Screening and Impact Investing. Positive screening and impact investing consider the impact that an investment is making. Implementation of this strategy is illustrated by the investment in a municipal bond issued for the construction and management of affordable housing. Other potential impact investing opportunities include investing in securities issued by the World Bank, which is an approved asset class per the City's investment policy.

Environmental, Social and Governance (ESG) Integration. The City's goal is to bring ESG integration to the heart of the investment decision process. The City monitors the ESG ratings provided by MSCI for the corporate bonds in the portfolio. The MSCI ratings are provided on a scale of 1 to 10 with ten being the highest. At this time, the weighted average Industry-Adjusted Score from MSCI for the corporate bond holdings is 7.5 which maps to a letter rated of "AA" on a scale of triple-C to triple-A.

The City also monitors the unadjusted Pillar Scores from MSCI for the corporate holdings. At this time, the weighted average Pillar Scores for the corporate bond holdings are as follows:

- MSCI Environmental Pillar Score: 6.8
- MSCI Social Pillar Score: 5.4
- MSCI Governance Pillar Score: 5.4

The City's ESG model can be refined to reflect the issues that matter most to the citizens of Boulder by applying customized weights to the MSCI Pillar Scores, thus creating ESG scores that better reflect the City's values, goals and policies.

Active Ownership/Corporate Engagement. Corporate engagement involves discussions with issuers about ESG risks and opportunities. The City is partnering with Insight Investment to seek the benefits of this goal. Insight requests and participates in meetings with management to understand key risks and potentially influence outcomes. Company engagement is critical to Insight's credit process and their analysts meet with issuers to address ESG factors as well as other credit-related concerns or questions.

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