

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

FROM: Kara Skinner, Chief Financial Officer

SUBJECT: Investment Performance as of September 30, 2023

DATE: October 17, 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.

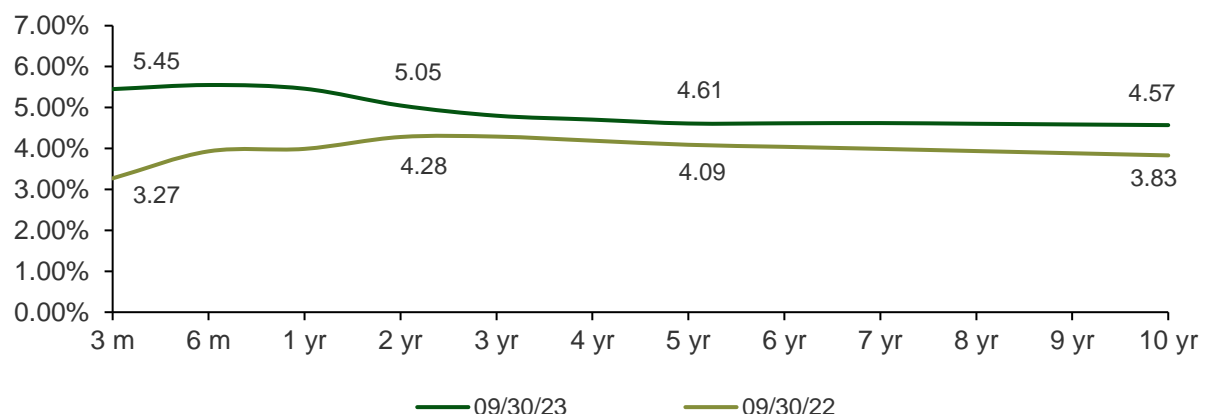
## Section 2 – Market Conditions, the Federal Reserve and the Yield Curve

- The yields of long-dated bonds move sharply upwards: Treasury yields shifted upwards as economic growth continued to show resilience and were influenced by global factors including a sharp selloff in Japanese government bonds. Two-year yields ended the quarter at 5.05%, 15bp higher. At the longer end of the curve, 30-year yields ended the quarter at 4.70%, 84bp higher.
- Don't fear an inverted curve: Despite the sharp upward move in longer-maturity Treasury yields in Q3, the Treasury yield curve remained inverted. Many are concerned that this signals a recession ahead, but this may simply reflect that the Fed will be unable to maintain rates at current levels on a sustained basis.
- Credit spreads tightened: Aggregate credit spreads tightened in Q3, with the spread of the Bloomberg US Corporate Index ending the quarter 2bp tighter than it began. The intermediate section of the credit curve underperformed on a spread basis, with spreads widening by 6bp, versus a 16bp tightening for the long duration index. Longer duration issues underperformed significantly on a price basis, however, given the sharp upward move in yields.
- The S&P 500 Index lost ground: US equity markets declined, with the S&P 500 Index falling by 3.3% in Q3. The year-to-date return remained a healthy 13.1%.

Risks include:

- Dislocations in the financial system as a result of higher interest rates
- 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: 09/30/2023 and 09/30/2022 (Source: Bloomberg)

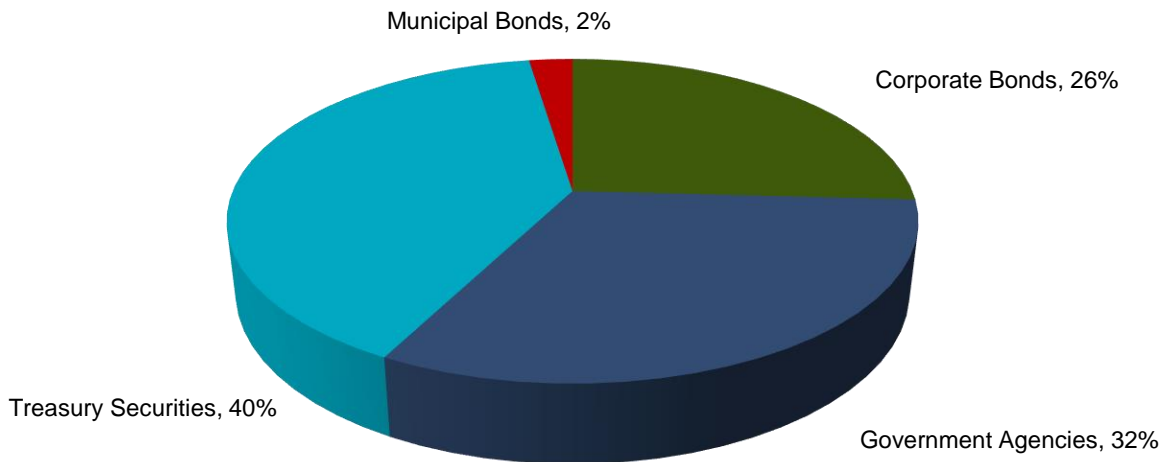


### **Section 3 – The City’s Portfolio**

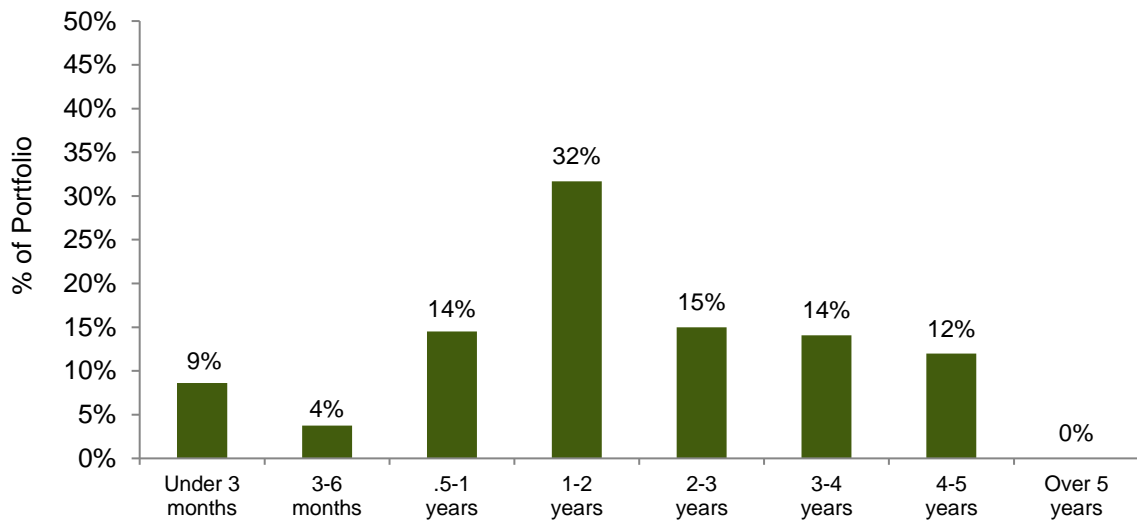
- Portfolio strategies implemented this quarter and the investments held in the portfolio comply with the City’s investment objectives and the Ordinance that specifies allowable investments.
  - The objective of safety is achieved through a well-diversified portfolio invested primarily in US Treasury 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 September 30, 2023, the WAM of the operating portfolio is 1.99 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.
  - As of September 30, the weighted average purchase yield for the operating portfolio holdings is 2.48%. The yield benchmark is the six-month trailing average of the yield on the 2-year Treasury note, which is 4.61% as of September 30. The purchase yield on the operating portfolio as of September 30 trails the benchmark yield by 2.13%.
  - For the third quarter 2023, the fair value periodic return on the operating portfolio is .64%. The 1-3 Treasury Index return for the period is .74%. The periodic return on the operating portfolio for the third quarter is .10% lower 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 third 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 4.89%. The weighted average maturity at the time of purchase for these investments is 4.27 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 September 30, 2023

## Asset Allocation - Historical Cost



## Final Maturity Distribution - Historical Cost



## Summary of Operating Portfolio Characteristics

	September 30, 2023	June 30, 2023
Average Final Maturity (years)	1.99	1.86
Modified Duration (years)	1.82	1.74
Average Purchase Yield	2.48%	2.18%
Average Market Yield	5.27%	4.99%
Average Credit Quality (S&P/Moody's)	AA+/Aa1	AA+/Aa1
Total Market Value (\$)	486,853,725	489,252,860

## Portfolio Holdings as of September 30, 2023

Issuer	Historical Cost	% Portfolio
US Treasury	202,192,495	39.80%
Federal Home Loan Bank	63,068,861	12.42%
Federal National Mortgage Association	38,954,996	7.67%
Federal Home Loan Mortgage Corp	30,049,011	5.92%
Federal Farm Credit Banks	29,861,668	5.88%
State Street Corp	19,463,109	3.83%
John Deere Capital Corp	17,263,359	3.40%
Toyota Motor Credit Corp	13,669,540	2.69%
PepsiCo Inc	12,648,873	2.49%
The Home Depot	11,936,240	2.35%
Caterpillar Financial Services Corp	10,830,545	2.13%
Colgate-Palmolive Co	10,754,910	2.12%
3M Co	9,366,900	1.84%
State of Florida	5,001,000	0.98%
State of Maryland	5,000,000	0.98%
International Business Machines Corp	4,871,700	0.96%
Cisco Systems Inc	4,669,050	0.92%
Apple Inc	4,606,145	0.91%
Johnson & Johnson	4,401,352	0.87%
Microsoft Corp	4,377,680	0.86%
Intel Corp	2,624,093	0.52%
Metro Oregon	2,349,820	0.46%
Cash	35,725	0.01%
<b>Total Historical Cost</b>	<b>507,997,071</b>	<b>100.00%</b>

## **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 7.6 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: 6.9
- MSCI Social Pillar Score: 5.4
- MSCI Governance Pillar Score: 5.5

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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