

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

FROM: Cheryl Pattelli, CFO

SUBJECT: Investment Performance as of June 30, 2020

Date: July 23, 2020

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

Markets turn more optimistic, for now: Economic data clarified the catastrophic economic damage caused by efforts to control the spread of COVID-19. The National Bureau of Economic Research confirmed that the US economy entered recession in February. Despite this, optimism grew through the quarter, buoyed by signs of initial recovery and hopes that a vaccine or combination of existing drugs could bring the virus under control. Whether this optimism proves to be justified will only become clear in the coming months and years, and the start of the traditional winter flu season is likely to be a key risk point.

The yield curve steepened marginally as sentiment improved: The Treasury yield curve steepened marginally as yields were largely anchored over the quarter but drifted upwards in very long maturities. The 2-year maturity Treasury yield declined by 6bp, the 10-year maturity Treasury yield declined by 7bp and the 30-year maturity Treasury yield rose by 4bp. The US Federal Open Market Committee's 'dot plot', which signals individual member forecasts, suggested that rates would remain unchanged through 2022.

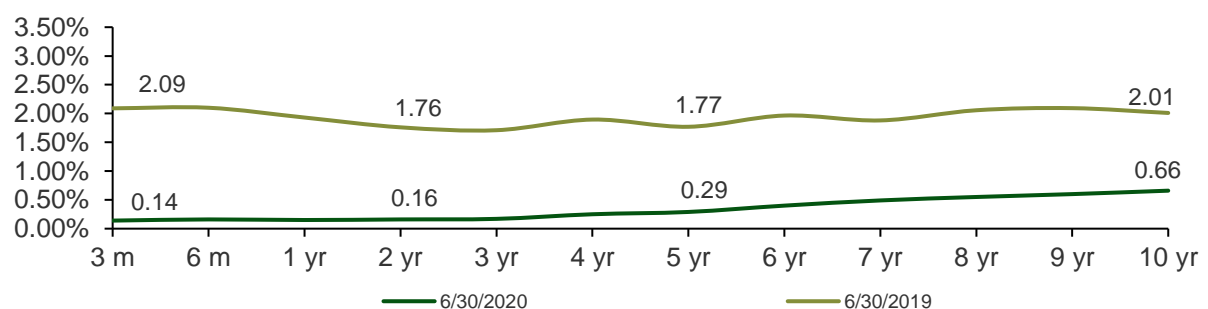
Credit spreads recover: Credit spreads tightened in Q2, with aggregate US corporate spreads ending the quarter 122bp tighter than where they began. Longer-maturity spreads tightening by a lesser 72bp with lower-rated securities outperforming given more positive sentiment. Q2 saw the surge in investment grade corporate issuance continue, with total issuance in the first half of 2020 at a similar level as for the whole of 2019. The Federal Reserve's purchases of corporate bonds and ETFs buoyed sentiment.

Equity markets rebound: Equity markets recovered a large part of their previous losses, with the S&P 500 Index gaining 20% to just under previous highs. The tech heavy NASDAQ Index broke to new all-time highs.

Risks include:

- A stop-start recovery, where further waves of the virus make it difficult for activity to recover
- Election uncertainty is likely to shift into focus as we move into the final stage of campaigning
- The role of China in the world is now uncertain as relationships between China and other powers are increasingly strained

Treasury Yield Curve: 06/30/2020 and 06/30/2019 (Source: Bloomberg)

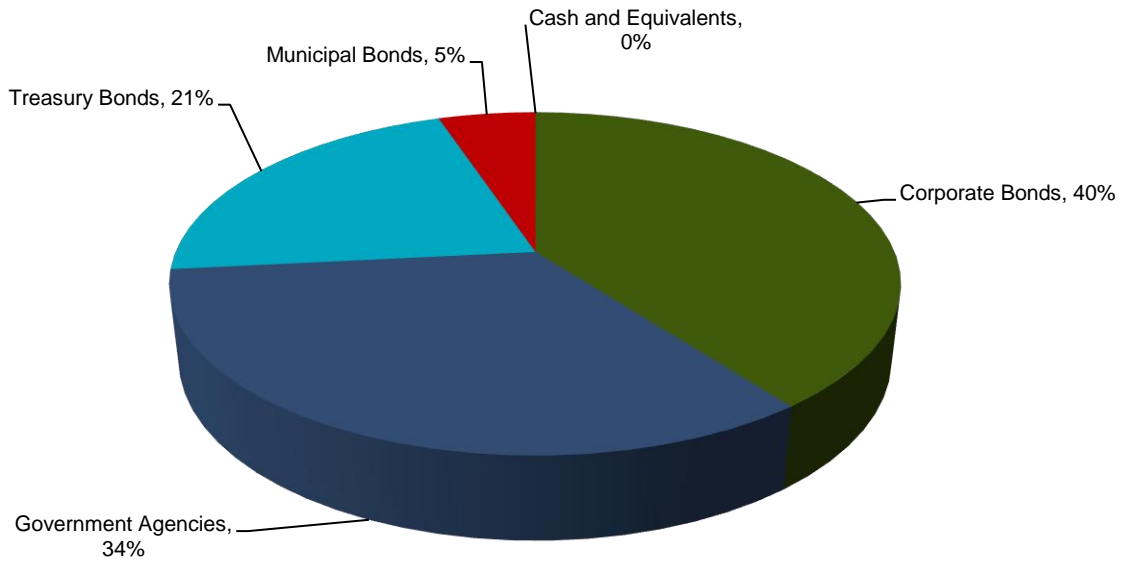


Section 3 – The City’s Portfolios

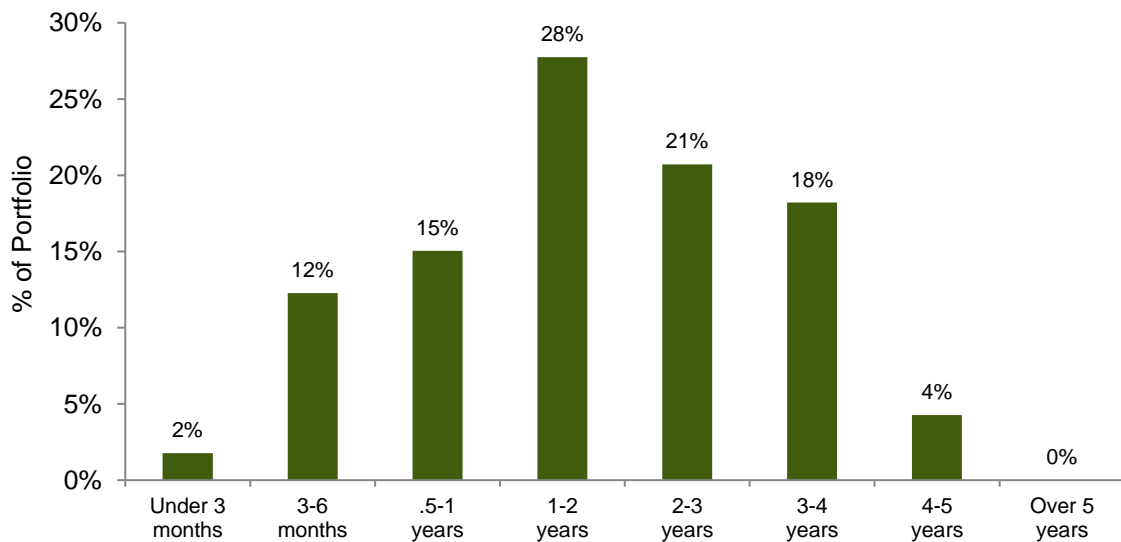
- Portfolio strategies implemented this quarter and the investments held in the portfolios comply with the City’s investment objectives and the Ordinance that specifies allowable investments.
 - The objective of safety is achieved through a well-diversified portfolio invested primarily in US Treasury 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 portfolios. Pursuit of further diversification through the revised policies will progress strategically relative to market conditions. Market risk is managed by maintaining a low weighted average maturity (WAM) in the City’s portfolios. As of June 30, 2020 the WAM of the operating portfolio was 1.9 years while the Ordinance allows for up to a 5-year WAM.
 - The City maintains sufficient liquidity. A minimum of 5% of the City’s total portfolio is held in liquidity accounts. In addition, approximately 1% of the term securities held as of June 30 will mature within 30 days.
 - As of June 30, the yield on the operating portfolio was 2.10%. The yield benchmark is currently the six-month trailing average of the yield on the 2-year Treasury note, which was .64% as of June 30. The yield on the operating portfolio as of June 30 exceeded the benchmark yield by 1.46%.
 - For the second quarter 2020, the fair value periodic return on the operating portfolio was 1.47%. The 1-3 Treasury Index return for the period was .13%. The return on the operating portfolio for the second quarter was 1.34% higher than the 1-3 Treasury Index return.
- The City’s portfolios do 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 2020 the City’s investment advisor invested approximately 8 million in longer-term securities for the operating portfolio. Corporate bonds and a US Agency security were purchased at a weighted average yield of .51%. The weighted average maturity at the time of purchase for these investments was 3.5 years. During the second quarter approximately 17.5 million was withdrawn from the operating portfolio for spending needs and to bolster liquidity account balances.
- 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.
- No investments were executed for the bond proceeds portfolio during the second quarter.

City of Boulder Operating Portfolio Profile As of June 30, 2020

Asset Allocation - Historical Cost



Final Maturity Distribution - Historical Cost



Summary of Operating Portfolio Characteristics

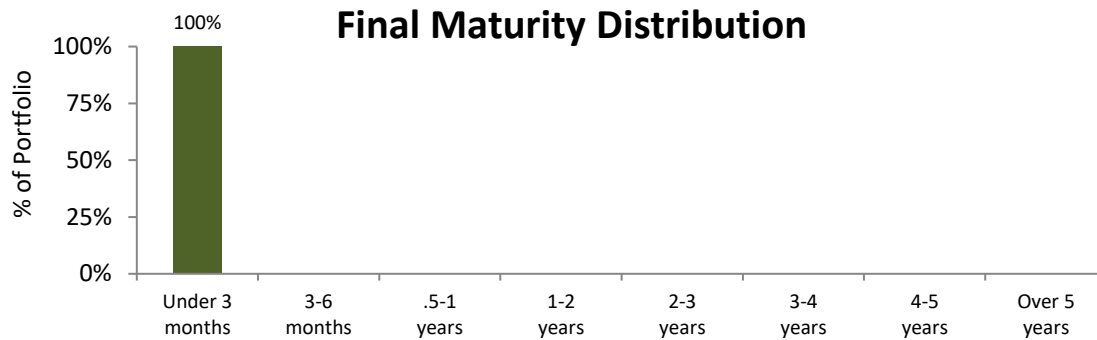
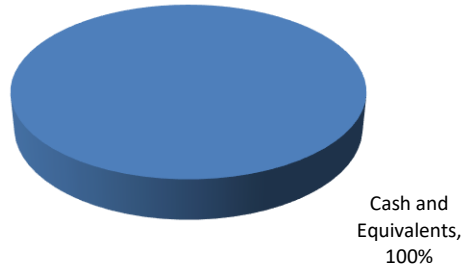
	June 30, 2020	March 31, 2020
Average Final Maturity (years)	1.90	2.03
Modified Duration (years)	1.82	1.88
Average Purchase Yield	2.10%	2.12%
Average Market Yield	0.35%	0.94%
Average Credit Quality (S&P/Moody's)	AA/Aa2	AA+/Aa1
Total Market Value (\$)	321,752,818	334,203,735

Securities Held as of June 30, 2020

Issuer	Historical Cost	% of Portfolio
US Treasury	67,163,938	21.49%
Federal Home Loan Bank	40,520,231	12.97%
Federal National Mortgage Association	31,249,910	10.00%
Federal Farm Credit Bank	23,582,003	7.55%
Microsoft Corp	11,736,902	3.76%
State Street Corp	10,832,747	3.47%
American Honda Finance Corp	10,545,614	3.37%
Apple Inc	10,457,935	3.35%
Toyota Motor Credit Corp	10,317,940	3.30%
Federal Home Loan Mortgage Corp	10,146,545	3.25%
Wal-Mart Inc	10,033,900	3.21%
City of New York, New York	8,478,013	2.71%
Cisco Systems Inc	7,971,070	2.55%
Caterpillar Financial Services Corp	7,714,253	2.47%
Metro Oregon	7,550,720	2.42%
Coca-Cola Company	7,007,940	2.24%
Intel Corp	6,258,670	2.00%
TWDC Enterprises (Disney)	5,722,720	1.83%
PepsiCo Inc	5,067,281	1.62%
Johnson & Johnson	4,401,352	1.41%
Bank of New York Mellon Corp	2,912,725	0.93%
Oracle Corp	2,895,060	0.93%
United Parcel Service Inc	2,519,450	0.81%
Chubb INA Holdings Inc	2,462,300	0.79%
IBM Credit LLC	2,461,975	0.79%
Praxair Inc	2,456,740	0.79%
Cash	29,503	0.01%
Total Historical Cost	312,497,437	100.00%

City of Boulder Bond Proceeds Portfolio Profile As of June 30, 2020

Asset Allocation - Historical Cost



Summary of Bond Proceeds Portfolio Characteristics

	June 30, 2020	March 31, 2020
Modified Duration (years)	0.00	0.04
Average Final Maturity (years)	0.00	0.04
Average Purchase Yield	0.00	0.80
Average Credit Quality (S&P/Moody's)	AA+/Aaa	AA+/Aaa
Total Market Value (\$)	2,569,521	2,561,749

Securities Held as of June 30, 2020

Issuer	Historical Cost	% of Portfolio
Cash	2,569,521	100.00%
Total Historical Cost	2,569,521	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 center

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 6.9 which maps to a letter rated of "A" 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: 4.9
- 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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