

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

FROM: Cheryl Pattelli, CFO

SUBJECT: Investment Performance as of September 30, 2019

Date: October 24, 2019

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

Rhetoric on trade and Fed policy intensifies:

Rather than softening his position, President Trump doubled down in the third quarter. Domestically, the President stepped up his criticism of Federal Reserve Chairman Jerome Powell, calling for the Federal Reserve to immediately cut interest rates by 100 basis points and to resume quantitative easing to boost growth. At the same time, the conflict between the US and China further intensified. Faced with retaliatory tariffs on US goods from China, the President immediately countered with an additional 5% tariff on around \$550 billion of Chinese goods.

Bond markets continued the rally:

The US Treasury curve shifted lower and flattened in the third quarter, with 2-year Treasury yields falling by 14 basis points, 10-year yields falling by 34 basis points and 30-year yields falling by 41 basis points. Markets now expect the Federal Reserve to cut interest rates multiple times and for other global central banks to also ease policy. This caused bond yields to plummet globally.

Central bank policy:

The Federal Open Market Committee (FOMC) decreased the target range for the federal funds rate twice in the third quarter. After 25 basis point decreases on July 31 and September 18, the target range ended the quarter at 1.75% to 2.00%.

Market Risks include:

- Protectionism escalates to a point where it has a severe impact on the global growth outlook.
- Inflationary pressures unexpectedly turn upwards, forcing the Fed to abruptly change position again.
- European growth slows further, leading to more radical policy responses, with implications for global bond and credit markets.

Treasury Yield Curve: 9/30/18 and 9/30/19



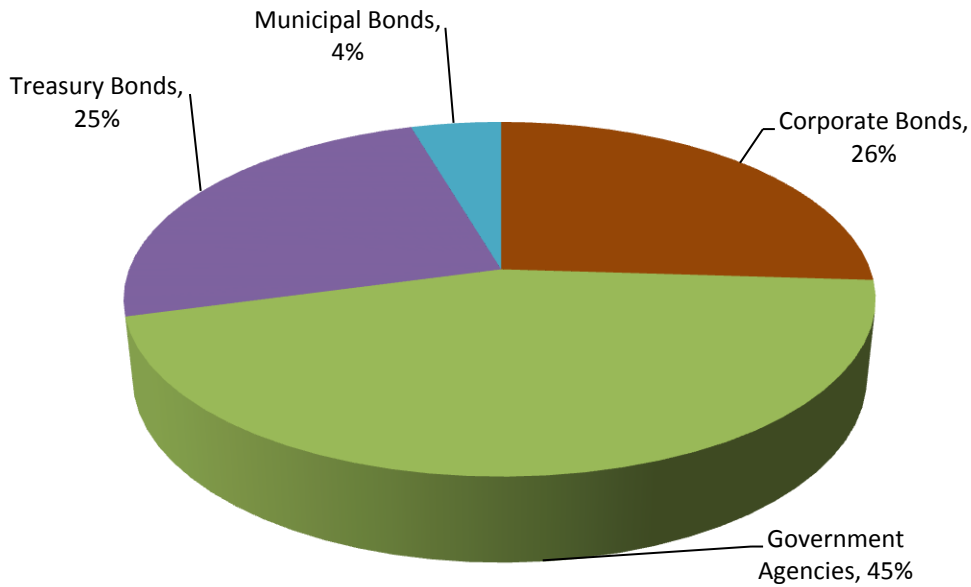
Source: Bloomberg

Section 3 – The City’s Portfolios

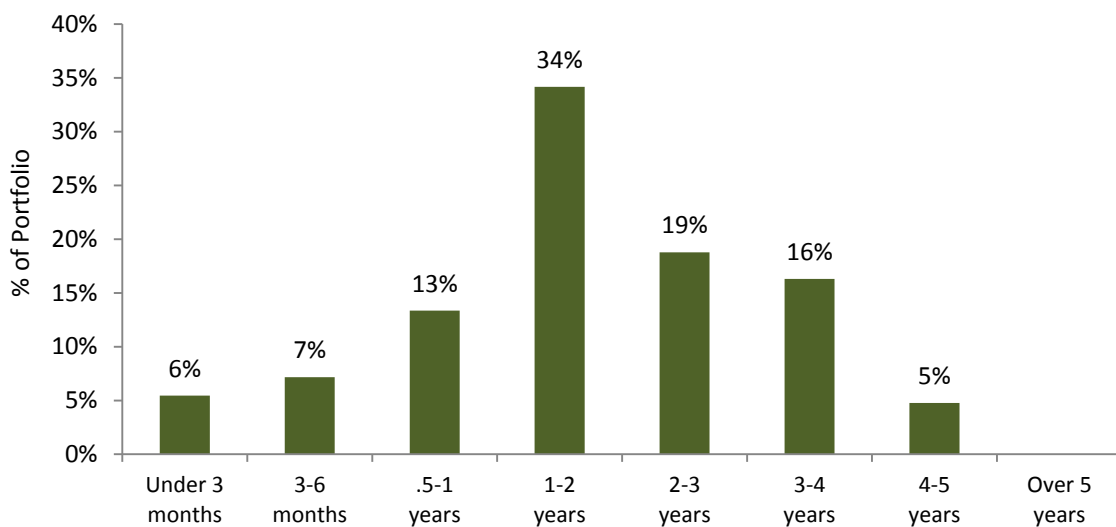
- Portfolio strategies implemented this quarter and all investments held in the portfolios comply with the City’s investment objectives and the Ordinance that specifies allowable investments.
 - The objective of safety is achieved through a well-diversified portfolio invested primarily in US Treasury 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 September 30, 2019 the WAM of the operating portfolio was 1.87 years while the Ordinance allows for up to a five-year WAM.
 - The City maintains sufficient liquidity. As of September 30, 2019, 2.83% of the term securities in the operating portfolio, or approximately 10 million, will mature within 30 days. Continuing cash balances fund the remaining liquidity requirement.
 - As of September 30, 2019, the gross yield on the operating portfolio was 2.14%. The yield benchmark is currently the six-month trailing average of the yield on the 2-year Treasury note, which was 1.91% as of September 30, 2019. The yield on the operating portfolio as of September 30 exceeded the benchmark yield by 0.23%.
 - For the third quarter of 2019, the gross fair value periodic return on the operating portfolio was 0.71%. The 1-3 Treasury Index return for the period was 0.58%. The return on the operating portfolio for the third quarter exceeded the 1-3 Treasury Index return by 0.13%.
- 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; and tobacco companies.
- In the third quarter of 2019 the City’s investment advisor invested approximately \$53 million in securities for the operating portfolio at a weighted average yield of 1.86%. Investments were made in Treasury and Instrumentality securities, general obligation municipal issues and corporate bonds. The weighted average maturity at the time of purchases for these investments was 3.7 years. The security purchases were funded by maturing investments, strategic sales of portfolio holdings and cash contributed to the term portfolio for investment during the quarter.
- The maturity extension strategy is anchored in the expectation that interest rates may have reached their peak for this interest rate cycle. Moderate increases in the maturity of recent purchases are intended to limit the impact of decreasing rates on future portfolio earnings. These active duration management strategies are designed to increase the portfolio’s exposure to longer-term interest rates, while the continued diversification to additional market sectors may enhance the portfolio’s return.
- Investments executed for the Bond Proceeds portfolio for the quarter had maturities of three months.

City of Boulder Operating Portfolio Profile As of September 30, 2019

Asset Allocation - Historical Cost



Final Maturity Distribution - Historical Cost



Summary of Portfolio Characteristics

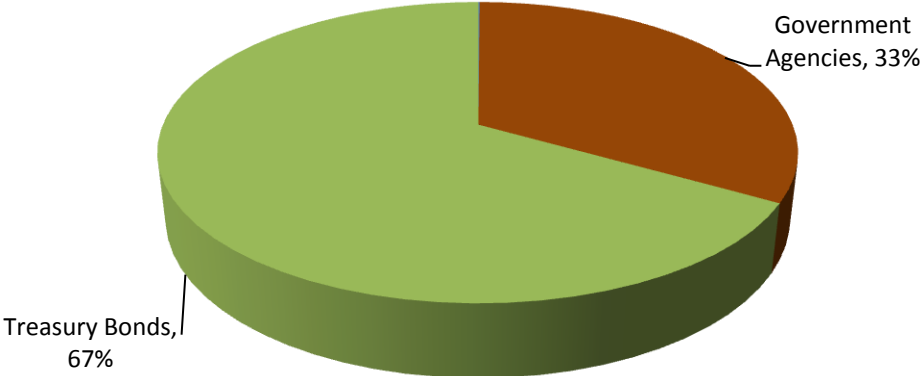
	September 30, 2019	June 30, 2019
Average Final Maturity (years)	1.87	1.68
Modified Duration (years)	1.79	1.60
Average Purchase Yield	2.14%	2.13%
Average Market Yield	1.81%	1.97%
Average Credit Quality (S&P/Moody's)	AA+/Aa1	AA+/Aa1
Total Market Value (\$)	355,584,100	333,330,800

Securities Held as of September 30, 2019

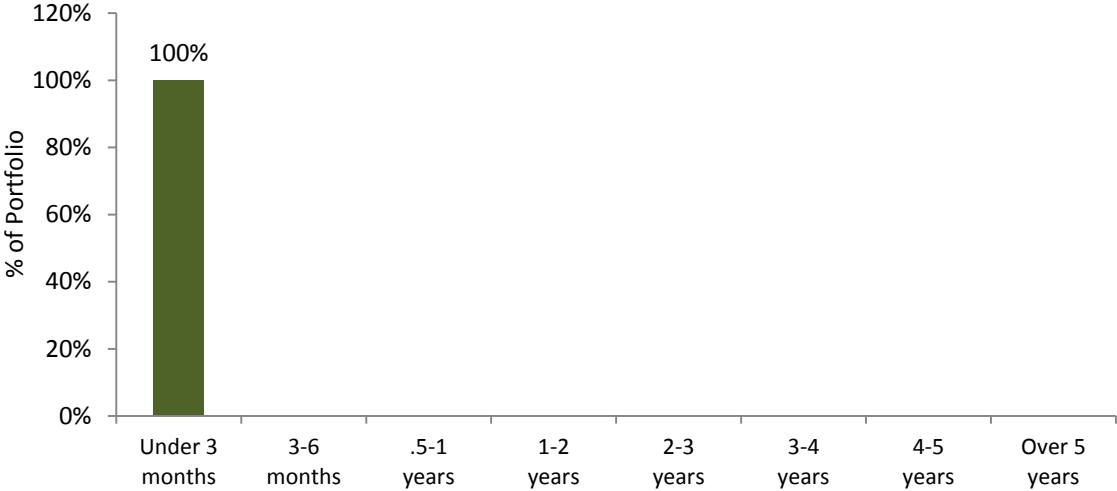
Issuer	Historical Cost	% of Portfolio
US Treasury	86,955,965	24.67%
Federal Home Loan Bank	55,143,252	15.64%
Federal National Mortgage Association	51,607,057	14.64%
Federal Farm Credit Bank	27,663,149	7.85%
Federal Home Loan Mortgage Corp	23,591,840	6.69%
American Honda Finance Corp	10,545,614	2.99%
Wal-Mart	10,033,900	2.85%
City of New York, New York	8,478,013	2.40%
Apple	8,378,915	2.38%
Toyota Motor Credit Corp	8,210,880	2.33%
Microsoft Corp	7,669,302	2.18%
Metro Oregon	7,550,720	2.14%
Coca-Cola Company	7,007,940	1.99%
TWDC Enterprises 18 Corp	5,722,720	1.62%
Johnson & Johnson	4,401,352	1.25%
State Street Corp	3,014,500	0.86%
Caterpillar Financial Services Corp	2,956,580	0.84%
Bank of New York Mellon Corp	2,912,725	0.83%
Cisco Systems Inc	2,895,870	0.82%
Oracle Corp	2,895,060	0.82%
United Parcel Service	2,519,450	0.71%
Intel Corp	2,487,550	0.71%
PepsiCo Inc	2,472,525	0.70%
Chubb INA Holdings Inc	2,462,300	0.70%
IBM Credit LLC	2,461,975	0.70%
Praxair Inc	2,456,740	0.70%
Cash	35,184	0.01%
Total Historical Cost	352,531,078	100.00%

City of Boulder Bond Proceeds Portfolio Profile As of September 30, 2019

Asset Allocation - Historical Cost



Final Maturity Distribution



Summary of Portfolio Characteristics

	September 30, 2019	June 30, 2019
Modified Duration (years)	0.13	0.20
Average Final Maturity (years)	0.13	0.21
Average Purchase Yield	1.94	1.85
Average Credit Quality (S&P/Moody's)	AA+/Aaa	AA+/Aaa
Total Market Value (\$)	4,549,378	4,523,273

Securities Held as of September 30, 2019

Issuer	Historical Cost	% of Portfolio
US Treasury	3,032,682	66.81%
Federal Home Loan Bank	1,502,858	33.11%
Cash	3,419	0.08%
Total Historical Cost	4,538,958	100.00%