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

FROM: Cheryl Pattelli, CFO

SUBJECT: Investment Performance as of December 31, 2019

Date: January 31, 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

Global central bank easing appears to have worked:
The Federal Open Market Committee (FOMC) decreased the target range for the federal funds rate once in the fourth quarter. After a 25 basis point decrease on October 30 the target range ended the quarter at 1.50% to 1.75%. The 'dot plot' released after the December FOMC meeting indicated that most members expect interest rates to remain unchanged through 2020. The committee noted that "the current stance of monetary policy is appropriate to support sustained expansion of economic activity, strong labor market conditions, and inflation near the Committee's symmetric 2 percent objective". With global economic data stabilizing over the quarter and the outlook for inflation still benign, it appears that global central banks may have successfully navigated the economic slowdown.

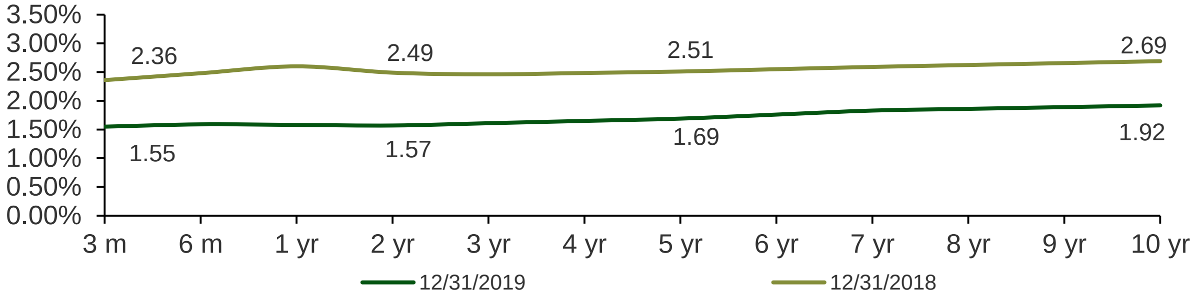
Global tail risks have faded:
The US and China have reached a Phase One trade agreement, and while tariff rollback is modest, this agreement stands in strong contrast to the spiraling escalation experienced in Q3. Additionally, an agreement on the USMCA was reached and passed by the House of Representatives. Elections in the UK have also averted a potential crash out Brexit.

The yield curve steepened:
The US Treasury curve steepened in Q4, with 2-year Treasury yields falling by 5bp, 10-year yields rising by 25bp and 30-year yields rising by 28bp.

Market Risks include:

- Trade tensions re-escalate to a point where they have 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: 12/31/2019 and 12/31/2018



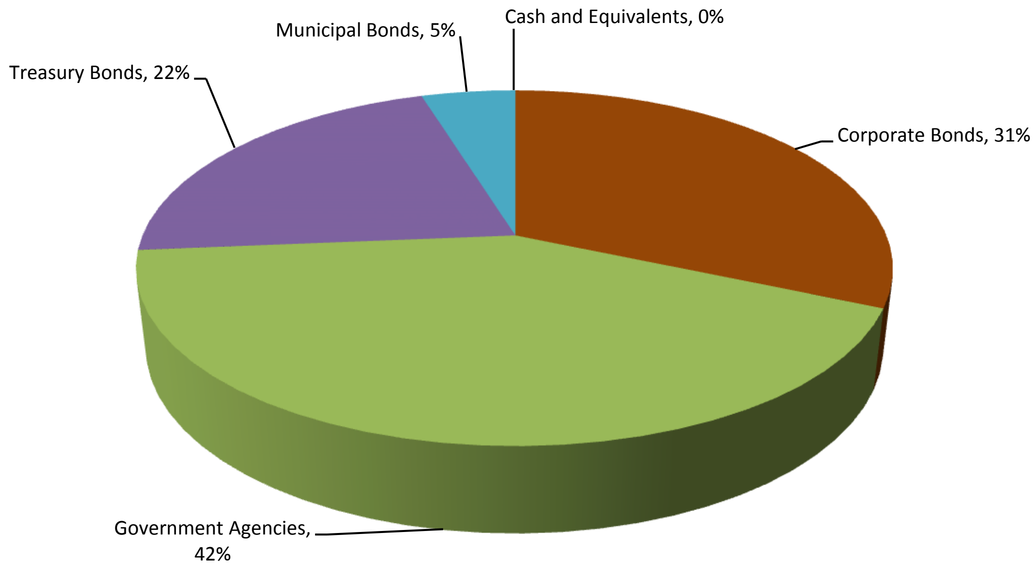
Source: Bloomberg

Section 3 – The City's Portfolios

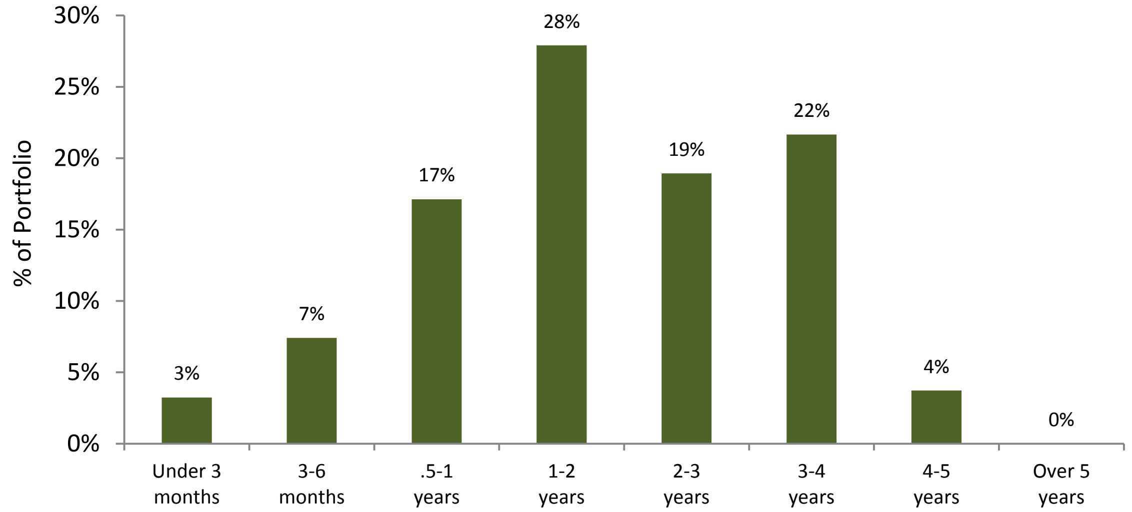
- Portfolio strategies implemented this quarter and the investments held in the portfolios comply with the City's investment objectives and the Ordinance that specifies allowable investments.
    - The objective of safety is achieved through a well-diversified portfolio invested primarily in US Treasury 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 December 31, 2019 the WAM of the operating portfolio was 2.04 years while the Ordinance allows for up to a 5-year WAM.
    - The City maintains sufficient liquidity. As of December 31, 2019, 2.54% of the term securities in the operating portfolio, or 8.5 million par value, will mature within 30 days. Continuing cash balances fund the remaining liquidity requirement.
    - As of December 31, 2019, the gross yield on the operating portfolio was 2.17%. The yield benchmark is currently the six-month trailing average of the yield on the 2-year Treasury note, which was 1.64% as of December 31, 2019. The yield on the operating portfolio as of December 31 exceeded the benchmark yield by 0.53%.
    - For the fourth quarter of 2019, the gross fair value periodic return on the operating portfolio was 0.21%. The 1-3 Treasury Index return for the period was 0.21%. The return on the operating portfolio for the fourth quarter matched 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 fourth quarter of 2019 the City's investment advisor invested approximately $62 million in securities for the operating portfolio at a weighted average yield of 1.73%. Investments were made in Treasury notes, Instrumentality securities and corporate bonds. The weighted average maturity at the time of purchases for these investments was 1.97 years. The security purchases were funded by maturing investments and sales of portfolio holdings.
- The strategy of maintaining and moderately extending duration for the operating portfolio reflects the expectation that interest rates have peaked and may now be range bound. The duration level maintains exposure to longer-term interest rates and the portfolio is well diversified to various market sectors which may enhance the portfolio's return.
- Investments executed for the bond proceeds portfolio for the quarter had maturities of less than one month.

City of Boulder Operating Portfolio Profile
As of December, 2019

Asset Allocation - Historical Cost



Final Maturity Distribution - Historical Cost



Summary of Operating Portfolio Characteristics

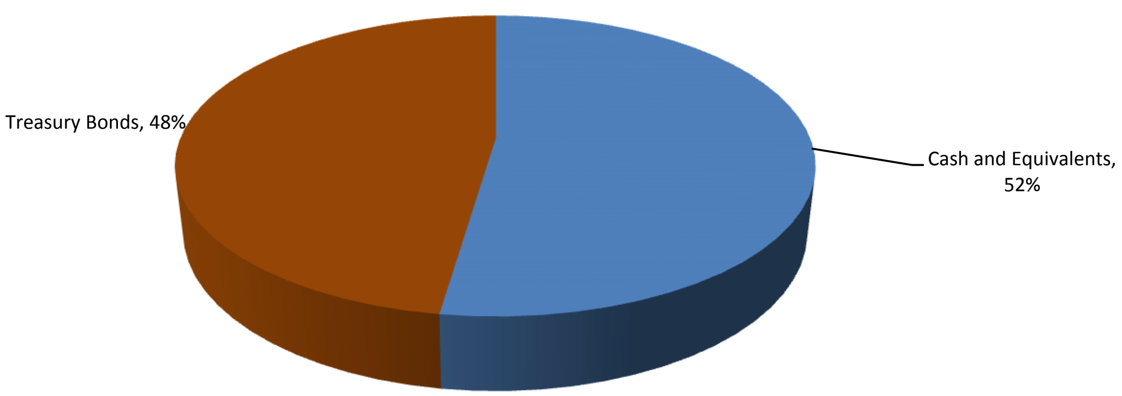
	12/31/2019	09/30/2019
Average Final Maturity (years)	2.04	1.87
Modified Duration (years)	1.90	1.79
Average Purchase Yield	2.17%	2.14%
Average Market Yield	1.66%	1.81%
Average Credit Quality (S&P/Moody's)	AA+/Aa1	AA+/Aa1
Total Market Value ($)	337,721,482	355,584,100

Securities Held as of December 31, 2019

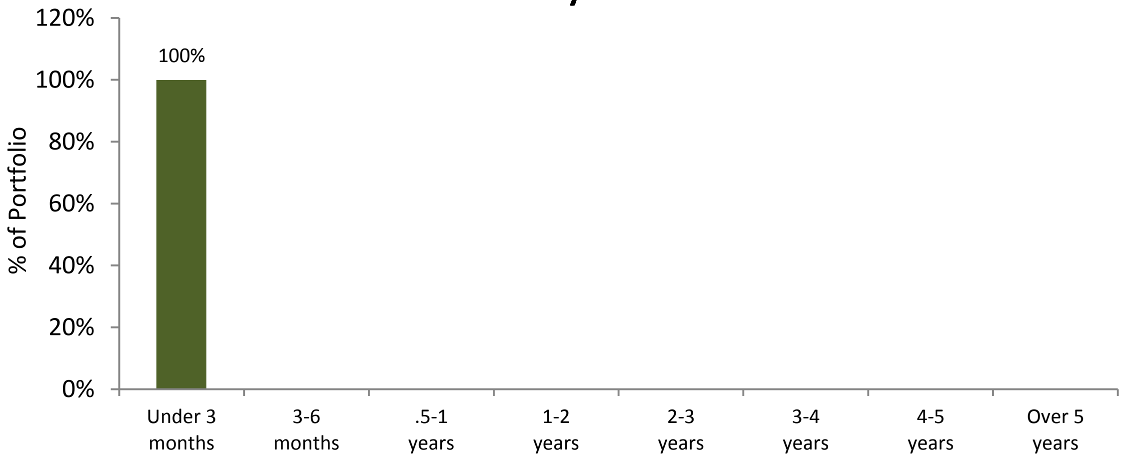
Issuer	Historical Cost	% of Portfolio
US Treasury	72,086,690	21.54%
Federal Home Loan Bank	58,785,319	17.56%
Federal National Mortgage Association	36,196,010	10.81%
Federal Farm Credit Bank	27,663,149	8.27%
Federal Home Loan Mortgage Corp	18,689,815	5.58%
Microsoft Corp	11,736,902	3.51%
American Honda Finance Corp	10,545,614	3.15%
Wal-Mart	10,033,900	3.00%
City of New York, New York	8,478,013	2.53%
Apple	8,378,915	2.50%
Toyota Motor Credit Corp	8,210,880	2.45%
Cisco Systems Inc	7,971,070	2.38%
State Street Corp	7,586,045	2.27%
Metro Oregon	7,550,720	2.26%
Coca-Cola Company	7,007,940	2.09%
TWDC Enterprises (Disney)	5,722,720	1.71%
Johnson & Johnson	4,401,352	1.32%
Caterpillar Financial Services Corp	2,956,580	0.88%
Bank of New York Mellon Corp	2,912,725	0.87%
Oracle Corp	2,895,060	0.87%
United Parcel Service	2,519,450	0.75%
Intel Corp	2,487,550	0.74%
PepsiCo Inc	2,472,525	0.74%
Chubb INA Holdings Inc	2,462,300	0.74%
IBM Credit LLC	2,461,975	0.74%
Praxair Inc	2,456,740	0.73%
Cash	17,465	0.01%
Total Historical Cost	**334,687,424**	**100.00%**

City of Boulder Bond Proceeds Portfolio Profile
As of December, 2019

Asset Allocation - Historical Cost



Final Maturity Distribution



Summary of Bond Proceeds Portfolio Characteristics

	12/31/2019	09/30/2019
Modified Duration (years)	0.03	0.13
Average Final Maturity (years)	0.03	0.13
Average Purchase Yield	1.58	1.94
Average Credit Quality (S&P/Moody's)	AA+/Aaa	AA+/Aaa
Total Market Value ($)	2,563,125	4,549,378

Securities Held as of December 31, 2019

Issuer	Historical Cost	% of Portfolio
Cash	1,339,175	52.33%
US Treasury	1,219,731	47.67%
Total Historical Cost	**2,558,906**	**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. As of December 31, 2019, the weighted average Industry-Adjusted Score from MSCI for the corporate bond holdings is 6.8 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. As of year-end the weighted average Pillar Scores for the corporate bond holdings are as follows:

- MSCI Environmental Pillar Score: 7.0
- MSCI Social Pillar Score: 4.9
- MSCI Governance Pillar Score: 5.3

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.