City of Boulder

City of Boulder

Finance Department

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

FROM: Bob Eichem, Chief Financial Officer

SUBJECT: Investment Performance as of March 31, 2015

DATE:

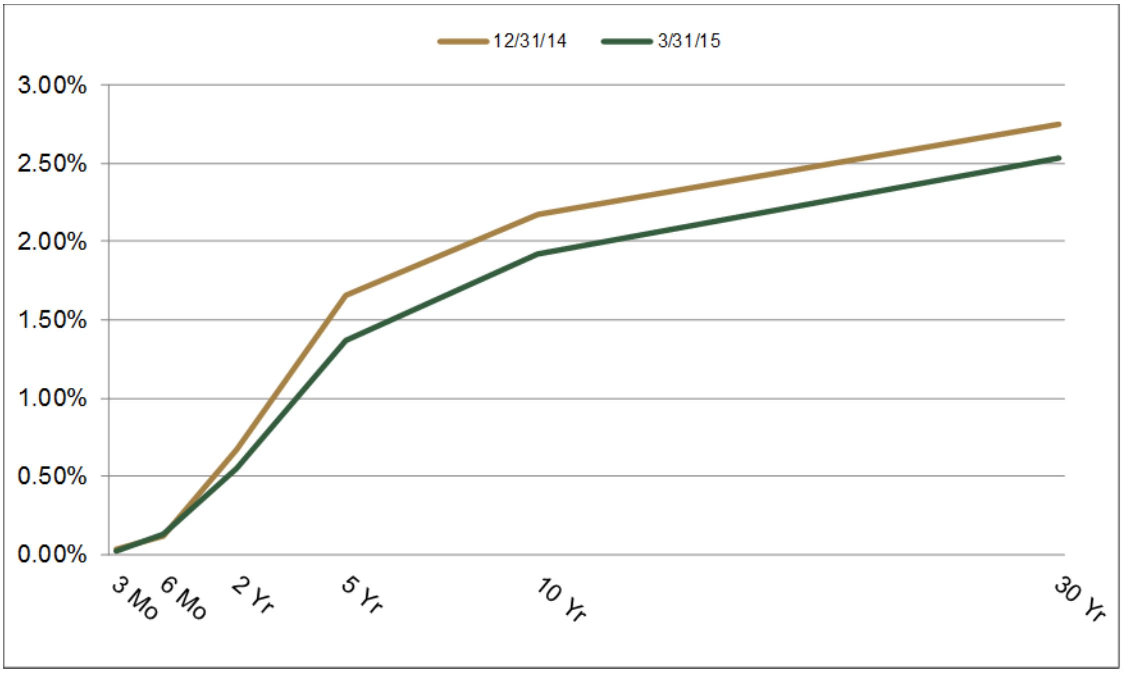
Section 1 – Background

- 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 – The Yield Curve and Federal Open Market Committee ("the Fed")

Treasury Yield Curve

12/31/2014 vs. 03/31/15

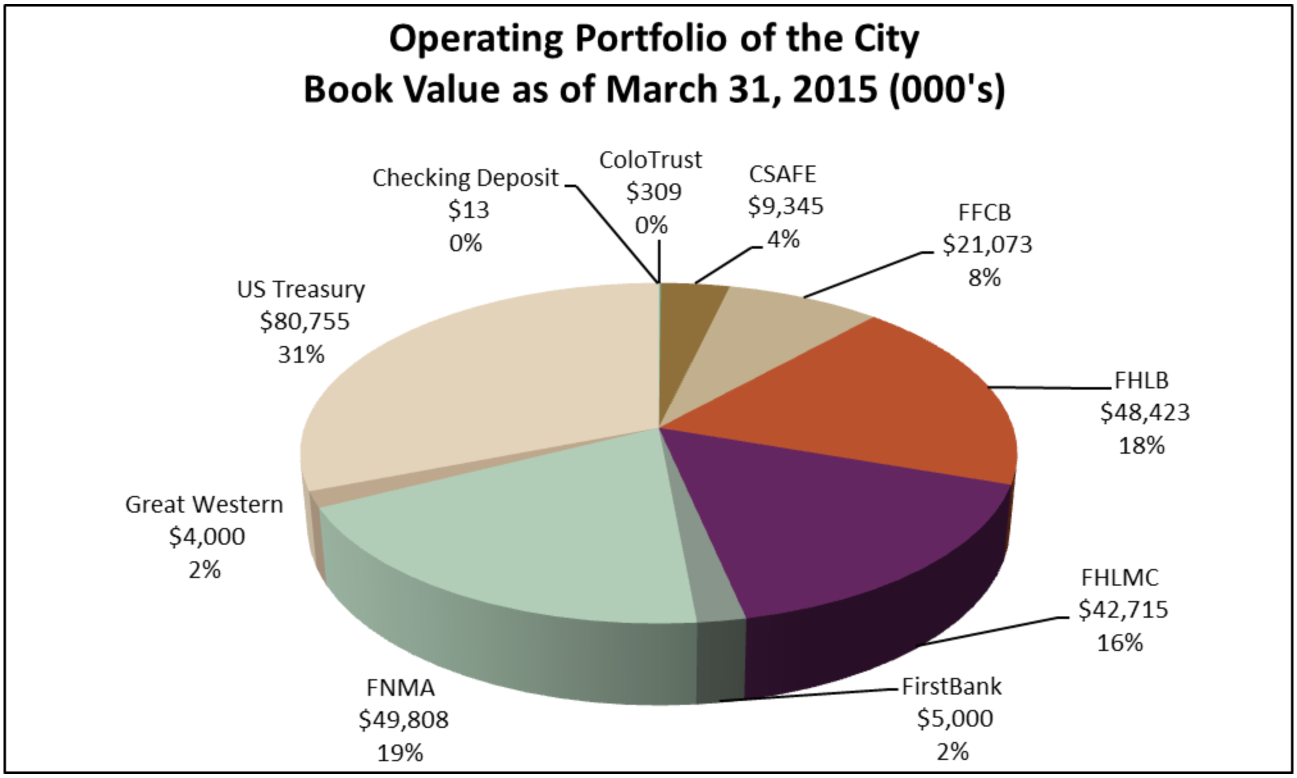


- During the past three months, the yield curve flattened. When the yield curve flattens, it means that the difference between the yields on short-term bonds and long-term bonds decreases. The flattening occurred because yields on long-term U.S. Treasury bonds fell faster than yields on short-term Treasury bonds during the quarter. Concerns about weak global economic growth kept downward pressure on longer US Treasury yields, even as the Fed signaled the possibility of a fed funds rate hike this year.
- The Federal Open Market Committee (FOMC) left policy rates unchanged at its March 17-18 meeting, without any dissenting votes. The Committee noted economic activity moderated and the inflation rate declined further. The word "patient" (with regard to the timing of a potential future rate hike) was removed from the policy statement but the Committee indicated a rate hike at the next FOMC meeting in April is unlikely. The Fed left the door open for a possible rate hike in June, but we believe the first rate hike is likely to occur later in the second half of this year. Notably, the Fed expects to see further improvement in the labor market before it starts to raise rates, which implies the Fed remains dissatisfied with current employment conditions. The Committee also needs to be confident inflation will move back to its 2% target, before they raise rates. With inflation low, we believe the Fed faces no urgency to begin raising rates. Even though the Committee removed the word "patient" from its policy statement, we believe the Fed's overall message was somewhat dovish, which makes a June rate hike unlikely, in our view. We believe ongoing uncertainty about the timing of the Federal Reserve's first interest rate hike will likely continue to fuel market volatility.

Section 3 – The City's Portfolios

- Portfolio strategies implemented this quarter and all 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, primarily among two major sectors (Treasury and Agency), the Agency issuers and various maturities along the yield curve. Market risk is managed by maintaining a low weighted average maturity (WAM) in the City's portfolio. As of March 31, 2015 the WAM was 1.70 years while the Ordinance allows up to a five year WAM.
    - The City maintains sufficient liquidity. As of March 31, 2015, 3.7% of the portfolio, or $9.7 million remained in overnight accounts.
    - As of March 31, 2015, the yield on the pooled investment portfolio was 0.813%. Our current benchmark is the six month trailing average on the 2-year Treasury, which was 0.556%, as of March 31, 2015. The objective was exceeded by 0.257%.
- There are no investments in the oil and gas industry in the City's portfolio.
- The City's investment adviser purchased approximately $31.0 million of securities during Q1 2015 for the City of Boulder's investment portfolio. The security purchases included Treasury and Agency securities maturing between November 2016 and January 2019. The securities were purchased in this maturity range to take advantage of the area on the yield curve that offers the best tradeoff between yield and maturity while and maintaining the portfolio characteristics. The yield differential in short maturity versus long maturity securities is a result of the Federal Reserve's accommodative monetary policy along with an expanding US economy. The proceeds of $16.0 million of maturities along with existing liquid funds were used to fund the security purchases.

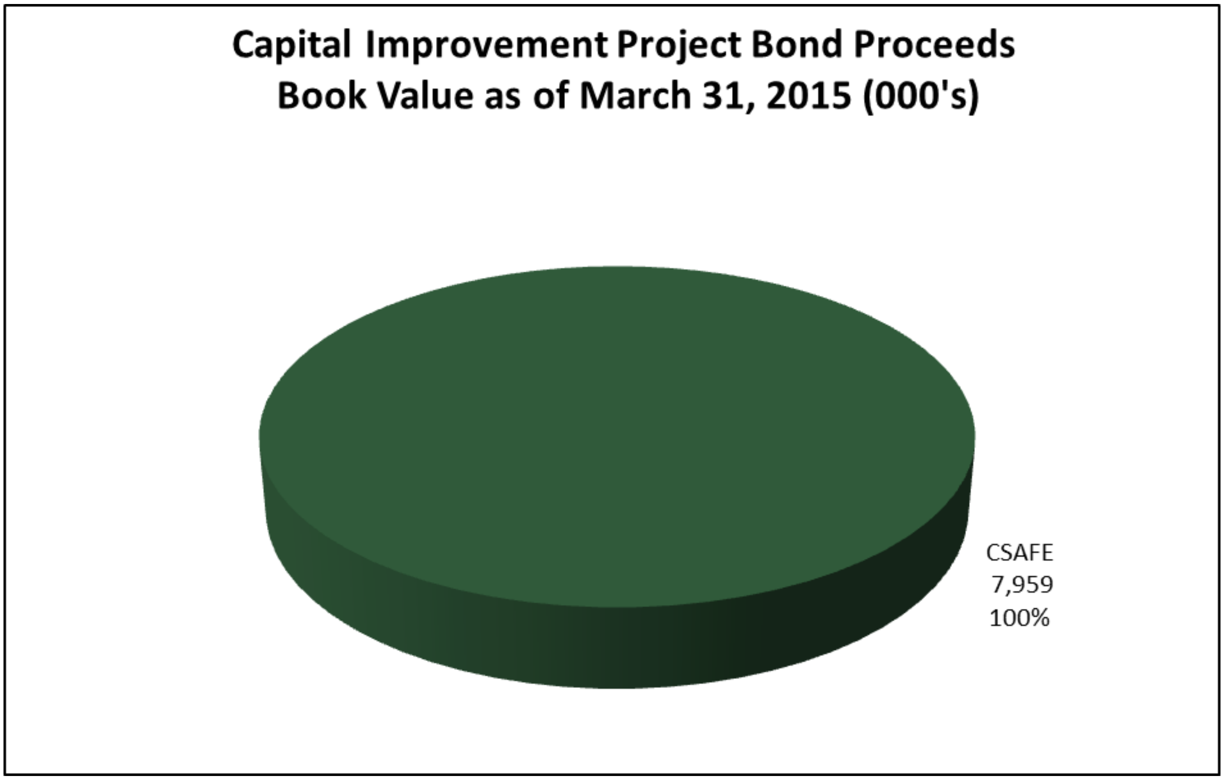
Operating Portfolio of the City



Portfolio Characteristics
City of Boulder Consolidated Non CIP

	03/31/2015	12/31/2014
	Portfolio	**Portfolio**
Average Maturity (yrs)	1.70	1.67
Modified Duration	1.67	1.65
Average Purchase Yield	0.813%	0.76%
Average Market Yield	0.557%	0.642%
Average Quality	AA+/Aaa	AA+/Aaa
Total Market Value	263,242,497	247,335,546

Capital Improvement Project 2012 Bond Proceeds



Portfolio Characteristics
Capital Improvement Project 2012 Bond Proceeds

	03/31/2015	12/31/2014
	Portfolio	**Portfolio**
Average Maturity (yrs)	0.00	0.00
Modified Duration	0.00	0.00
Average Purchase Yield	0.14%	0.12%
Average Market Yield	0.14%	0.12%
Average Quality	NR/NR	NR/NR
Total Market Value	7,958,590	9,385,093

When the Capital Improvement Bond proceeds of over $54 million were received in March 2012, a separate portfolio was established to facilitate IRS required arbitrage calculations. The balance of $7.9 million as of March 31, 2015 was invested as shown above in the graph and table to assure timely funding for the projected draw down schedule expected to end in January 2015.

- In June 2012, the investment committee selected the one year Treasury as the benchmark for the bond proceeds based upon an average maturity of approximately one year for the portfolio at that time. As of March 31, 2015 the portfolio yield was 0.14% compared to a yield of 0.23% on the one year Treasury.

- Daily liquidity in the portfolio is currently 100% of the portfolio, or $7.9 million, resulting in a very short weighted average maturity of 0.0 years. The portfolio has virtually no market risk and 100% of the funds are available for immediate draw down as projects need funding. This portfolio structure safely supports the short liability duration of the projects that are expected to end in January 2015.