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 December 31, 2015

DATE: January 19, 2016

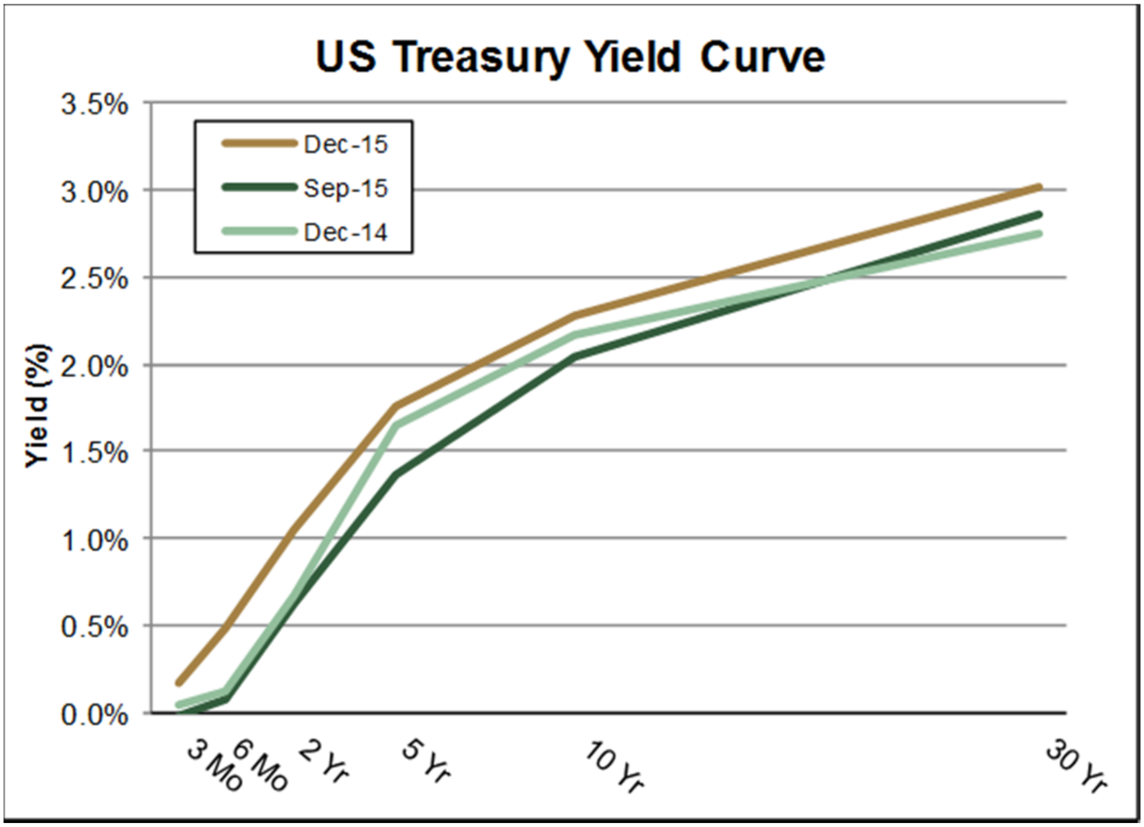
Section 1 – Background

- 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. 09/30/2015 vs. 12/31/15

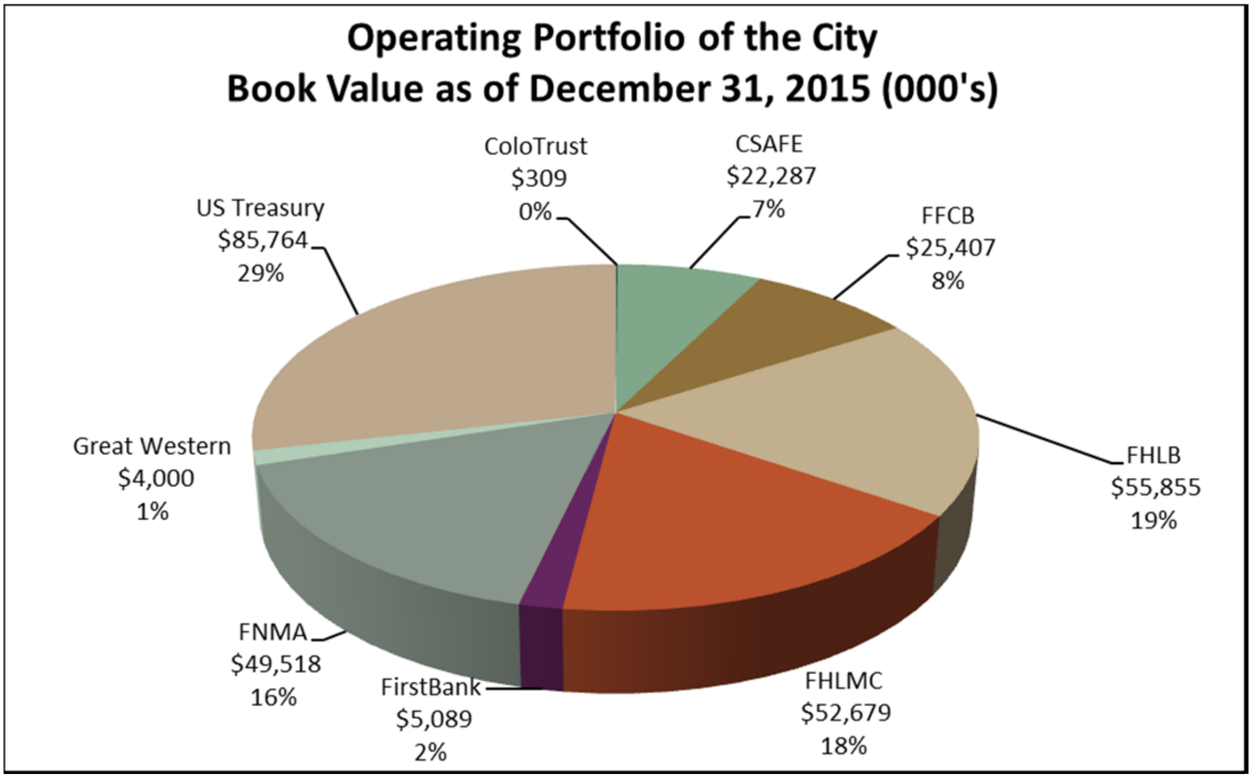


- The yield on the two-year Treasury note rose roughly 12 basis points in December to 1.05%. Meanwhile, the yield on the ten-year Treasury note rose just six basis points in December to 2.27%. Overall, the Treasury yield curve flattened during 2015 in anticipation of monetary policy normalization by the Federal Reserve and we expect this trend to continue.
- As expected, in December the Federal Open Market Committee (FOMC) increased the fed funds target rate by 25 basis points. It was the first fed funds target rate increase since June 2006. Although the fed took its first step toward normalizing monetary policy, the tone of the FOMC statement was dovish, suggesting the pace of additional policy tightening will be slower than historical Fed tightening cycles. Policymakers' median projection for the fed funds rate at the end of 2016 is 1.375%. In the longer-run, the target fed funds rate is roughly 3.5%. However, the FOMC has emphasized that monetary policy adjustments will be gradual and the path of the fed funds rate will depend on the economic outlook. Notably, the FOMC will continue to reinvest principal payments from its holdings of Agency and Mortgage-Backed securities and will continue rolling over maturing Treasury securities until normalization of the fed funds rate is well underway. Overall, monetary policy remains highly accommodative and the Fed is proceeding with caution as it moves toward a more normalized policy stance.

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 December 31, 2015 the WAM was 1.58 years while the Ordinance allows up to a five year WAM.
    - The City maintains sufficient liquidity. As of December 31, 2015, 7.0% of the portfolio, or $22.6 million remained in overnight accounts.
    - As of December 31, 2015, the yield on the pooled investment portfolio was 0.948%. Our current benchmark is the six month trailing average on the 2-year Treasury, which was 0.763%, as of December 31, 2015. The objective was exceeded by 0.185%.
- There are no investments in the oil and gas industry in the City's portfolio.
- The City's investment adviser purchased approximately $22.0 million of securities during Q4 2015 for the City of Boulder's investment portfolio. The proceeds of $18.5 million of maturities along with existing liquid funds were used to fund the security purchases. The security purchases included Treasury and Agency securities maturing between April 2018 and November 2020. These securities were purchased in this maturity range to maintain the portfolio characteristics in line with the strategy. As expected, in December the Federal Open Market Committee (FOMC) increased the fed funds target rate by 0.25% putting pressure on bond yields. The yield on the two-year Treasury note rose roughly 0.12% in December to 1.05%. Meanwhile, the yield on the ten-year Treasury note increased just 0.06% in December to 2.27%. Looking ahead, we believe the pace of subsequent rate hikes will be slower than historical Fed tightening cycles, in light of ongoing sluggishness in the global economy.

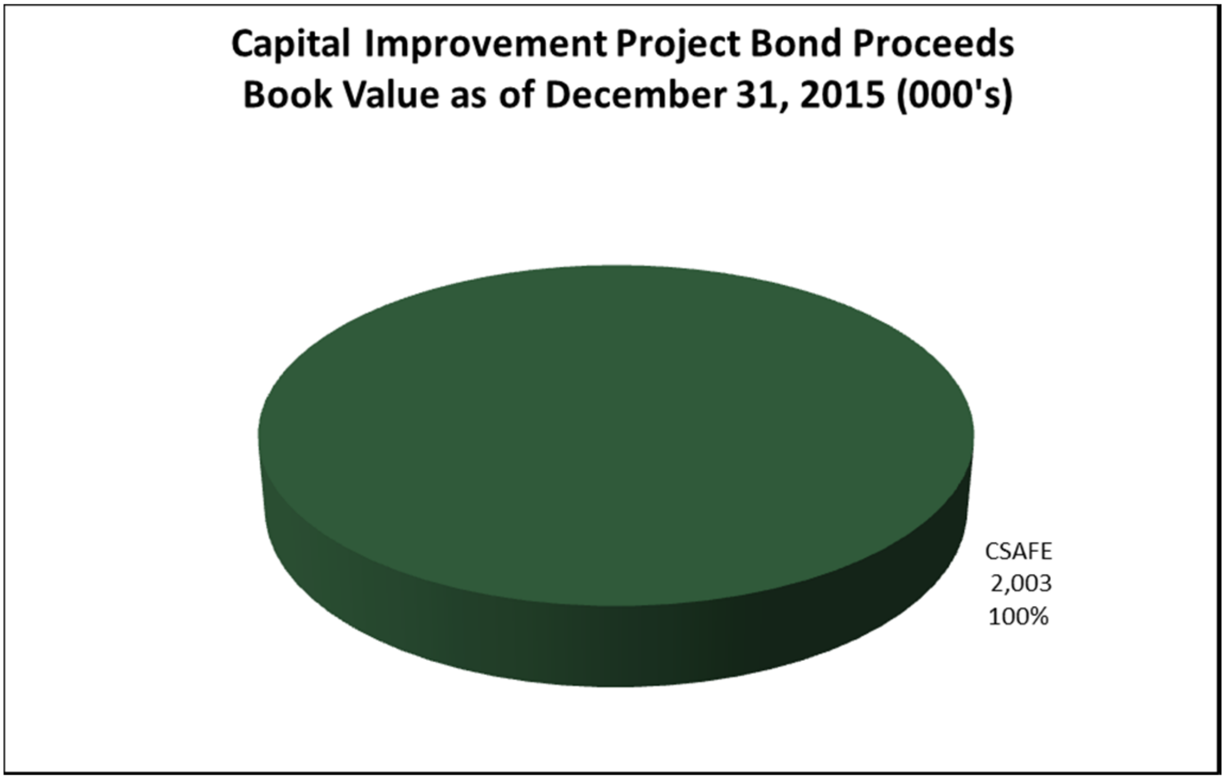
Operating Portfolio of the City



Portfolio Characteristics
City of Boulder Consolidated Non CIP

	12/31/2015	09/30/2015
	Portfolio	**Portfolio**
Average Maturity (yrs)	1.58	1.59
Modified Duration	1.54	1.56
Average Purchase Yield	0.948%	0.896%
Average Market Yield	0.953%	0.591%
Average Quality	AA+/Aaa	AA+/Aaa
Total Market Value	301,195,037	286,563,732

Capital Improvement Project 2012 Bond Proceeds



Portfolio Characteristics
Capital Improvement Project 2012 Bond Proceeds

	12/31/2015	09/30/2015
	Portfolio	**Portfolio**
Average Maturity (yrs)	0.00	0.00
Modified Duration	0.00	0.00
Average Purchase Yield	0.29%	0.19%
Average Market Yield	0.29%	0.19%
Average Quality	NR/NR	NR/NR
Total Market Value	2,002,576	4,963,302

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 $2.0 million as of December 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 December 31, 2015 the portfolio yield was 0.29%.
- Daily liquidity in the portfolio is currently 100% of the portfolio, or $2.0 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.