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 June 30, 2014

DATE:

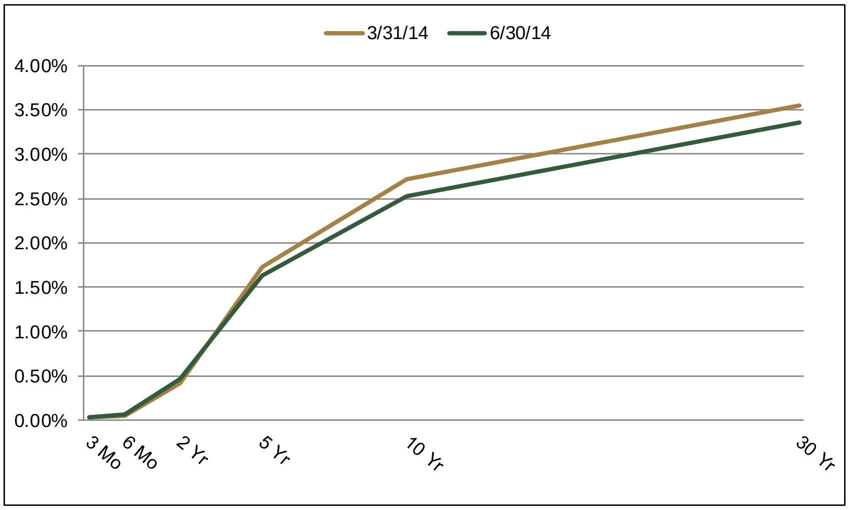
Section 1 – Background

- 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

3/31/2014 vs. 6/30/14



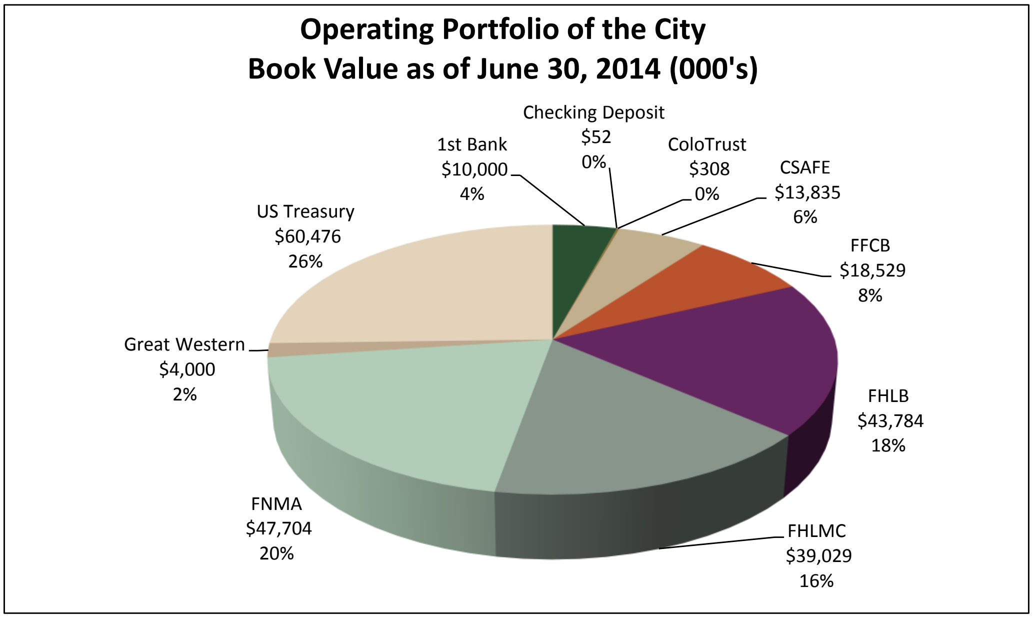
- During the past three months, the yield curve has flattened even as the Fed has been tapering its purchases of long-term Treasury bonds. Market participants have reacted to mixed domestic economic data, as well as fears of euro zone deflation, geopolitical tensions, and volatility in emerging markets over the past several months. These concerns have fueled a flight to quality, putting downward pressure on longer yields, although some of this pressure has recently dissipated.

- As expected, the Federal Open Market Committee left policy rates unchanged at its June 17-18 meeting, and announced another $10 billion reduction in asset purchases (to a level of $35 billion per month from $45 billion, comprised of $20 billion in treasuries and $15 billion in mortgage-backed securities). We expect the process of unwinding quantitative easing will continue at a steady pace with the Fed announcing another $10 billion reduction in asset purchases at its July 29-30 meeting. The Fed reduced their GDP growth projections for 2014 to 2.1%-2.3% from 2.8%-3.0%, but improved their outlook for unemployment. At Chair Yellen's press conference, she reinforced that the Fed will continue to monitor the economy and does not project raising short term rates for a considerable amount of time after the asset purchases end.

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 June 30, 2014 the average duration was 1.30 years while the Ordinance allows up to a five year WAM.
    - The City maintains sufficient liquidity. As of June 30, 2014, 6% of the portfolio, or $14.1 million remained in overnight accounts.
    - As of June 30, 2014, the yield on the pooled investment portfolio was 0.63%. Our current benchmark is the six month trailing average on the 2-year Treasury, which was 0.39%, as of June 30, 2014. The objective was exceeded by 0.24%.
- There are no direct investments in the oil and gas industry in the City's portfolio.
- The City's investment adviser purchased approximately $21 million of securities during Q2 2014 for the City of Boulder's investment portfolio. Recent purchases included $8 million from maturing security balances and new investments of about $13 million. The security purchases included Treasury and Agency securities maturing between February 2017 and March 2018. Recent investments continued to take advantage of the historically steep yield curve. The historically steep yield curve is a result of the Federal Reserve's accommodative monetary policy. The purchase of these securities moved the portfolio closer to the characteristics of the style and strategy selected by the City. Future securities purchases will rebalance the City's investment portfolio closer to the targeted risk characteristics. This will be accomplished by investing liquidity not needed for other operations and reinvesting funds from maturing bonds.

Operating Portfolio of the City

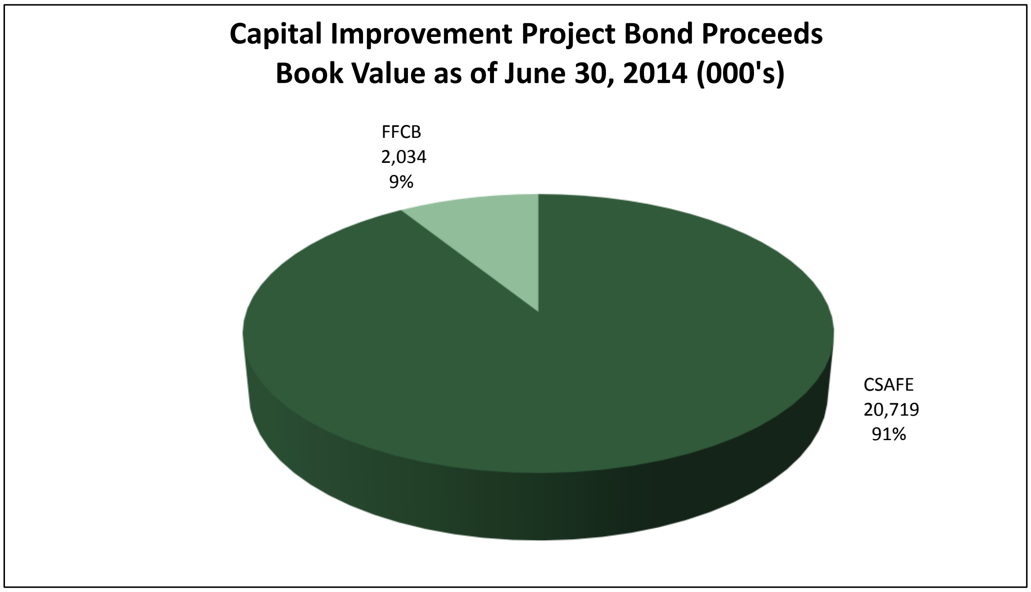


Portfolio Characteristics

Operating Portfolio of the City

	06/30/2014	03/31/2014
	Portfolio	**Portfolio**
Average Maturity (yrs)	1.32	1.33
Modified Duration	1.30	1.31
Average Purchase Yield	0.63%	0.59%
Average Market Yield	0.37%	0.34%
Average Quality**	AA+/Aaa	AA+/Aaa
Total Market Value	238,866,373	226,016,829

Capital Improvement Project 2012 Bond Proceeds



Portfolio Characteristics
Capital Improvement Project 2012 Bond Proceeds

	06/30/2014	03/31/2014
	Portfolio	**Portfolio**
Average Maturity (yrs)	0.04	0.08
Modified Duration	0.04	0.08
Average Purchase Yield	0.06%	0.10%
Average Market Yield	0.02%	0.03%
Average Quality**	AA+/Aaa	AA+/Aaa
Total Market Value	22,760,277	28,866,739

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 $22.8 million as of June 30, 2014 is 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 June 30, 2014 the portfolio yield was 0.06% compared to a yield of 0.10% on the one year Treasury.
- Daily liquidity in the portfolio is currently 91% of the portfolio, or $20.7 million, resulting in a very short weighted average maturity of 0.04 years. The portfolio has virtually no market risk and 91% 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.