



# City of Sunnyvale

## Agenda Item-No Attachments (PDF)

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### REPORT TO COUNCIL

#### **SUBJECT**

Receive and File the City of Sunnyvale Investment Report - 1st Quarter 2019

#### **REPORT IN BRIEF**

In accordance with California Government Code Section 53646, staff is submitting the attached investment report for Council's review. The report includes all investments held by the City of Sunnyvale. Funds not immediately needed for disbursement and held in investments are managed by Chandler Asset Management.

Funds for the City's Deferred Compensation Plan, the City's Retirement Plan, the City's Pension Trust, Other Post-Employment Benefits (OPEB) Trust, and any proceeds from debt issuance are not included in this report. These funds are managed and held by third party administrators and trustee custodial banks.

#### **EXISTING POLICY**

California Government Code Section 53600 et seq., strictly governs which investments public agencies can hold. In some cases, State law also governs what percentage of the portfolio can be invested in certain security types, maximum maturities, and minimum credit ratings by the major rating agencies (Standard & Poor's and Moody's Investors Service). Public agencies can only invest in fixed income securities. The purchase of stock is prohibited. As a result, the City primarily invests in highly rated securities such as U.S. Treasury, Federal agencies, and government sponsored enterprise debt as well as high credit quality, non-governmental debt securities.

The California Government Code also requires investment objectives of safety, liquidity, and return in that order. As such, safety of principal is the foremost objective of the City's investment program. The portfolio must remain sufficiently liquid to enable the City to meet all cash requirements.

The City Council first adopted a policy (7.1.2 Investment and Cash Management) governing the investment of City funds on July 30, 1985. This policy is reviewed and adopted annually. Council adopted an updated policy for FY 2018/19 at its August 14, 2018 meeting. The City's investment policy follows the Government Code and includes additional restrictions on some investments such as a lower allowable percentage per investment type or issuer than State law.

#### **ENVIRONMENTAL REVIEW**

This action does not require environmental review because it is not a project that has the potential for causing a significant impact on the environment. (CEQA Guideline 15061(b)(3)). Furthermore, the action being considered does not constitute a "project" with the meaning of the California Environmental Quality Act ("CEQA") pursuant to CEQA Guidelines section 15378 (b) (4) in that it is a

fiscal activity that does not involve any commitment to any specific project which may result in a potential significant impact on the environment.

## **DISCUSSION**

This report provides information on the values (par, book and market), the type of investment, issuer, maturity date and yield of each investment. The par value of a bond is the amount that the issuer agrees to repay the City by the maturity date. The book value is what the City initially paid for the bond and it changes gradually if a premium or discount is amortized. The market value is what the bond is worth now.

The City has adopted a portfolio structure to address liquidity and return, all while maintaining safety. Funds formerly held in a separate liquidity portfolio have recently been rolled into the core investments portfolio. These funds continue to be actively managed with maturities ranging between 0 and 5 years and have an average duration target of approximately 2.5 years to capture yield and enhance long-term returns. The duration for these funds is currently 1.6 years, which is slightly lower than at the end of last quarter because of the co-mingling of shorter-term investments. The duration, however, continues to be deliberately moved closer to its target slowly in consideration of volatile rates and an inverted yield curve. These funds currently total \$563,755,782.

Funds needed to meet cash needs (liquid investments) are now solely managed in Local Agency Investment Fund (totaling \$59,999,044). Local Agency Investment Fund (LAIF) is a program created by statute as an investment alternative for California's local governments and special districts.

Summary and detailed information on each security is provided in Attachment 1. Also included is an activity report of sales, purchases and maturities for this accounting period as required by Government Code section 53607. The current portfolio market value is \$623,754,826. This amount does not include \$2,961,467 of accrued interest, which has been earned, but not yet received. The portfolio's average yield to maturity was 2.48 percent as of April 6, 2019. The value of the portfolio is impacted by market forces in the bond market, as well as by growing property tax revenues, development related activity such as park impact fees, housing impact fees, developer contributions, building and planning fees, increased utility enterprise fund revenues and other City financial activities.

## **Economic Update**

The Federal Open Market Committee kept the target fed funds rate unchanged in March at a range of 2.25%-2.50%. However, the Fed's economic projections, along with the tone of the policy statement and the Fed Chair's press conference, were more dovish than expected. The Fed's median forecast now calls for a target fed funds rate of 2.4% at year-end, which implies that there will be no further rate hikes this year. The Fed is projecting one rate hike in 2020 (to an effective rate of 2.6%) and then expects to keep policy on hold in 2021. The Fed's longer-run fed funds rate target is still 2.8%. This implies that the Fed intends to keep the target fed funds rate below the neutral rate for the foreseeable future. Furthermore, the Fed announced that they will begin slowing down the reduction of their balance sheet and conclude their balance sheet reduction program at the end of September 2019. This will leave the Fed with a larger balance sheet (slightly higher than \$3.5 trillion) than they originally expected.

Domestic and global economic growth has slowed and inflation pressures remain muted. However, the labor market remains a bright spot in the US economy. We believe some of the factors hindering current economic growth (e.g., trade disputes, recent government shutdown, Brexit uncertainty) may be somewhat transitory. While economic growth is likely to remain under pressure over the near-term, we believe a strong labor market coupled with an increasingly dovish Fed may lead to better than expected economic growth later this year. Overall, the economy is expected to grow 2.0%-2.5% this year versus 2.9% in 2018.

The yield curve inverted in March with the 10-year Treasury yield temporarily falling below the 3-month T-bill yield. At month-end, the 3-month T-bill yield was down 5 basis points to 2.38%, the 2-year Treasury yield was down about 25 basis points to 2.26%, and the 10-year Treasury yield was down 31 basis points to 2.41%. The spread between 2- and 10-year Treasury yields was less than 15 basis points at March month-end. An inversion of the yield curve in which the 10-year Treasury yield is lower than the 3-month T-bill is generally viewed as a powerful predictive signal of an upcoming recession. However, staff, in consultation with our investment manager, does not expect a recession is imminent.

Generally lower-than-last-quarter yields have impacted the City's investments up to March 2019 primarily in two ways:

- Interest income continued to grow as portions of the portfolio that were purchased when yields were low have been maturing. Reinvestment of these funds continue to be at higher yields than that of the initial investment. Interest income for this fiscal year's first ten reporting periods totaled \$9,039,087. In comparison, interest income for the same period last year totaled \$3,991,333.
- Yields fell slightly for a period, causing the fair value of the City's investments to appreciate.

### **FISCAL IMPACT**

The City-wide projection for interest income for FY 2018/19 totals approximately \$6.6 million. Interest earnings as of the end of the first quarter of 2019 (third quarter of FY 2018/19) totaled \$9,039,087, tracking above our forecast.

### **PUBLIC CONTACT**

Public contact was made by posting the Council agenda on the City's official-notice bulletin board outside City Hall, at the Sunnyvale Senior Center, Community Center and Department of Public Safety; and by making the agenda and report available at the Sunnyvale Public Library, the Office of the City Clerk and on the City's website.

### **RECOMMENDATION**

Receive and file the City of Sunnyvale - First Quarter 2019 Investment Report.

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Reviewed by: Teri Silva, Assistant City Manager  
Approved by: Kent Steffens, City Manager

### **ATTACHMENTS**

1. City of Sunnyvale First Quarter Investment Report