REQUEST FOR CITY COUNCIL ACTION

MEETING DATE: JANUARY 10, 2023

TITLE: TREASURER'S REPORT FOR QUARTER ENDED SEPTEMBER 30, 2022

Interim Director of Administrative Services

Oliver Chi

City Manager

RECOMMENDED ACTION

Receive and file the Treasurer's Report for the quarter ended September 30, 2022.

EXECUTIVE SUMMARY

The Treasurer's Report (Attachment 1) provides a synopsis of investment activity for the City's three investment portfolios for the quarter ended September 30, 2022. The portfolios, managed by Meeder Investment Management under the direction of the Treasurer, include the Irvine Pooled Investment Portfolio, Bond Proceeds Fund Portfolio, and the Special District Funds Portfolio. The total book value for all three portfolios was $1.24 billion as of September 30, 2022. The report provides information on assets, allocations, average maturities, yields, and valuations for each of the three portfolios. A discussion of market conditions is included to give additional perspective to these measurements.

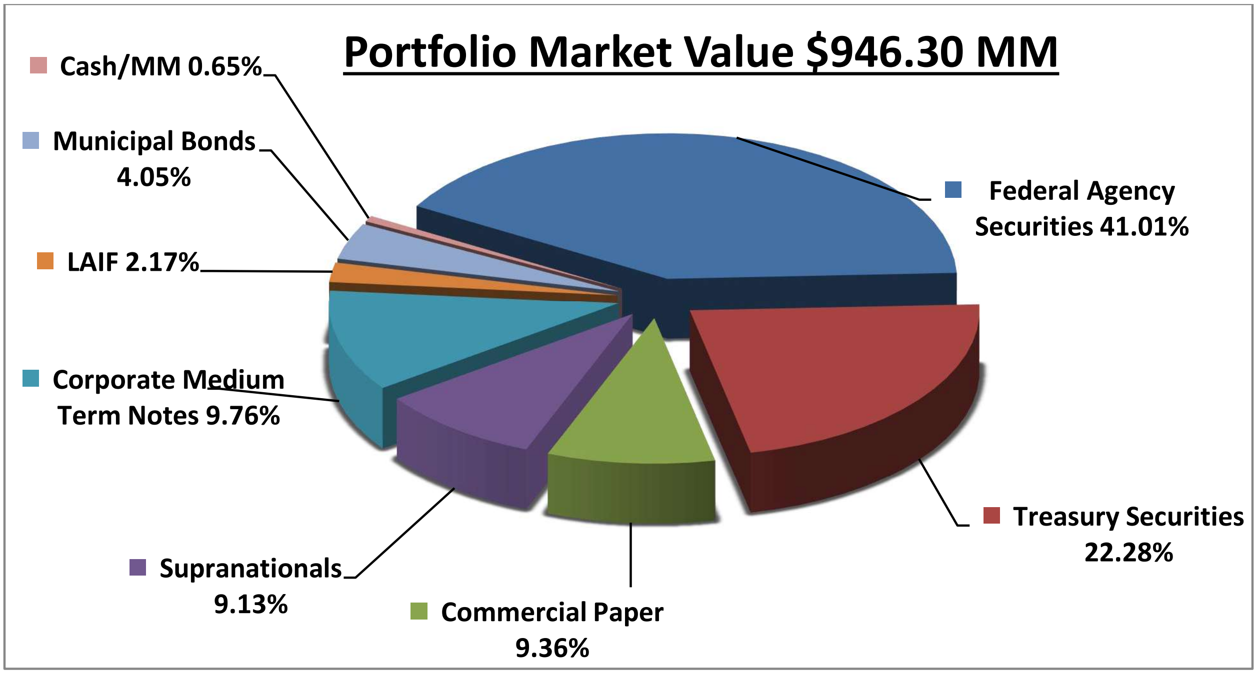
As of September 30, 2022, the City's investment portfolios are in full compliance with the City's Investment Policy, the California Government Code Section 53601, and have sufficient cash flow from a combination of liquid and maturing securities, bank deposits, and income to meet the City's expenditure requirements.

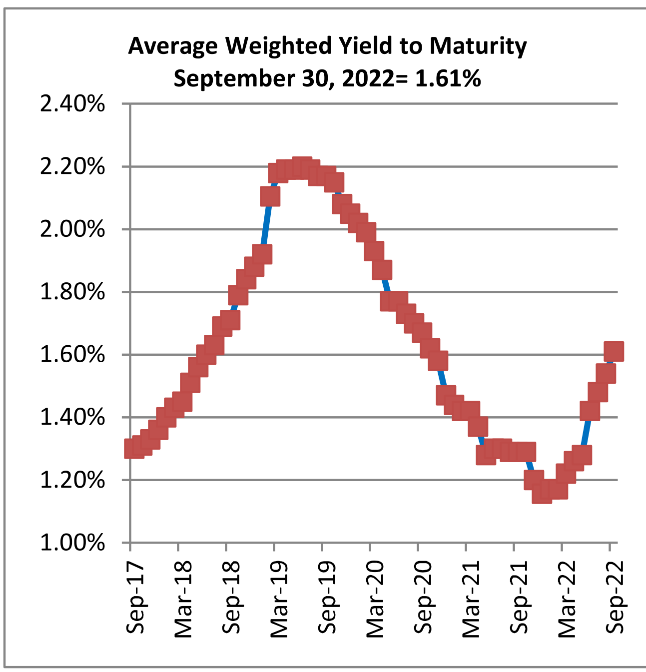
COMMISSION/BOARD/COMMITTEE RECOMMENDATION

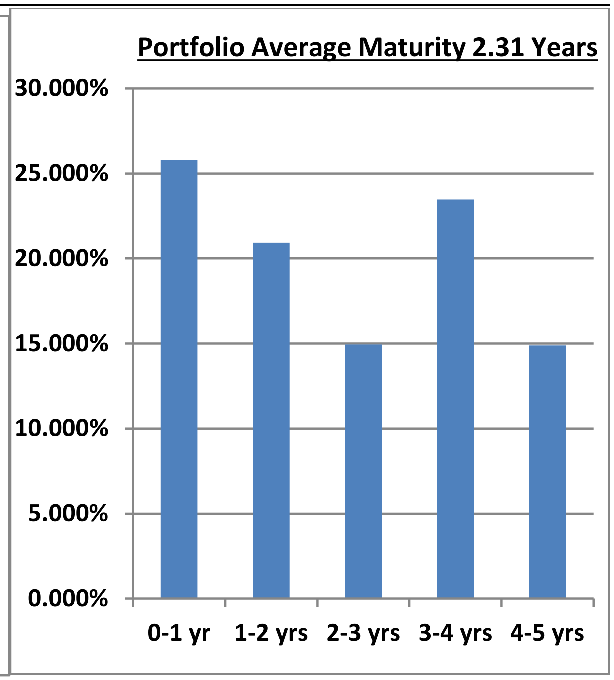
At its November 9, 2022 meeting, the Investment Advisory Committee voted 4-0-1 (Committee Member Li absent) to approve the report.

ANALYSIS

The Pooled Investment Portfolio holds the City's operating funds. Charts on following pages provide highlights on asset allocation, maturity distribution, credit quality, as well as the book yield history of this portfolio only. The Treasurer's Report provides detailed information on all three portfolios.







ALTERNATIVES CONSIDERED

None. The Treasurer's Report is intended to provide historical information about the City's investment portfolios. Pursuant to the City's Investment Policy, the Treasurer is required to submit quarterly Treasurer's reports to the Investment Advisory Committee and the City Council.

FINANCIAL IMPACT

Fiscal year-to-date investment income for the Irvine Pooled Investment Portfolio, Bond Proceeds Funds Portfolio, and Special District Funds Portfolio totaled $3.06 million with investments structured for security and liquidity.

REPORT PREPARED BY Don Collins, City Treasurer

Attachments:
1. Treasurer's Report for the quarter ended September 30, 2022
2. Summary of Irvine Pooled Investment Portfolio by Fund

CITY OF IRVINE
TREASURER'S REPORT
For Quarter Ended September 30, 2022

The City of Irvine maintains three investment portfolios, the Irvine Pooled Investment Portfolio, the Bond Proceeds Fund Portfolio, and the Special District Funds Portfolio. As of quarter ended September 30, 2022, combined book value of the three portfolios totaled $1.24 billion. This report provides detailed information of all three portfolios, along with an analysis of market conditions.

Irvine Pooled Investment Portfolio

The Irvine Pooled Investment Portfolio contains funds invested for the daily operational requirements of the City and funds reserved for economic uncertainties, future rehabilitation and maintenance needs. The portfolio is a combination of various operational funds, including the City's Asset Management Plan and funds earmarked for the development of the Great Park. A summary of Irvine Pooled Investment Portfolio by Fund is presented at the end of this report (Attachment 2).

As of September 30, 2022, the book value (purchase price of securities as recorded on the City's books) of the portfolio was $1.00 billion and the average yield to maturity was 1.61 percent. Fiscal year to date investment revenue (interest payments and capital gains) generated by the portfolio as of September 30, 2022 was $2.47 million. The table below compares the portfolio's statistics over a rolling 12-month period.

Irvine Pooled Investment Portfolio
Rolling 12-Month Quarterly Comparison

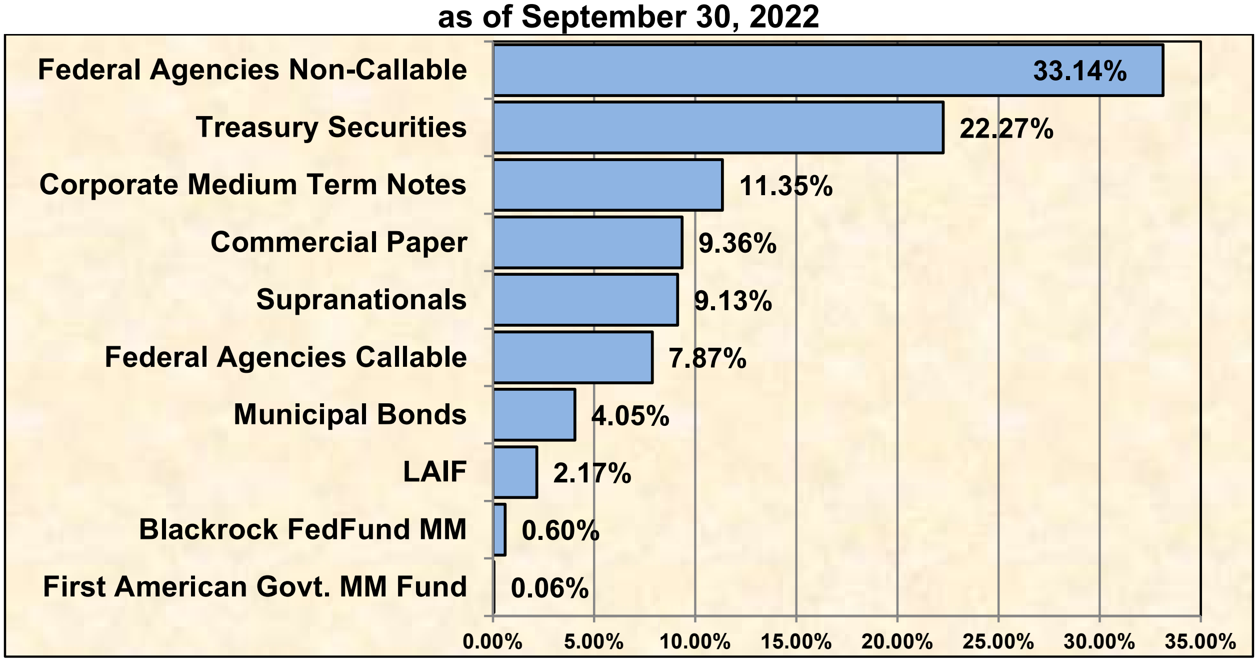
	September 30, 2022	June 30, 2022	March 31, 2022	December 31, 2021
Book Value	$1,002,649,923	$1,015,081,547	$945,748,989	$934,790,655
Market Value	$946,303,312	$979,341,599	$921,034,785	$938,325,125
Unrealized Gain/(Loss)	($56,346,611)	($35,739,948)	($24,714,204)	$3,534,470
Unrealized Gain/(Loss) as % of Book Value	(5.62%)	(3.52%)	(2.61%)	0.38%
Average Yield To Maturity	1.61%	1.42%	1.22%	1.16%
Liquidity 0–6 Months	10.36%	14.25%	11.11%	21.57%
Weighted Average Maturity	2.31	2.32	2.35	2.26
Modified Duration (Years)	2.16	2.19	2.25	2.19
Quarterly Interest Earnings	$2,468,946	$2,802,976	$3,502,502	$4,155,732
Fiscal Year to Date Income	$2,468,946	$14,096,279	$11,293,303	$7,790,801

As anticipated, the Irvine Pooled Investment Portfolio's book value decreased by $12.43 million from the previous quarter due to the prepayment of CalPERS pension liability for Fiscal Year 2021-22, as well as various planned capital improvement projects. Portfolio yield to maturity increased for the quarter ended September 30, 2022 by 19 basis points to 1.61 percent as maturing investments were reinvested in the rising rate environment. With market rates rising during the quarter, as of September 30, 2022, the portfolio ended with an unrealized loss of $56.35 million as compared to an unrealized loss of $35.74 million on June 30, 2022. This is a normal result of the portfolio's modified duration of 2.16 years and its price-sensitivity to changes in market interest rates.

To ensure the safety of the portfolio, investments held are in compliance with the Irvine Investment Policy, Bond Indentures, and State Code 53601 et al. The Irvine Pooled Investment Portfolio is comprised primarily of Treasury Securities and Federal Government sponsored entity debt, otherwise known as federal agency securities. Although federal agency securities were downgraded by Standard & Poor's to AA+ in August 2011, they continue to be regarded as among the safest securities in the global market. Two of the government sponsored agencies, Federal National Mortgage Association (Fannie Mae) and Federal Home Loan Mortgage Corporation (Freddie Mac), remain under conservatorship and carry an implicit guarantee by the Federal Government. In addition, both are carefully monitored by the City's investment manager and Treasurer to ensure the continued safety of the City's funds.

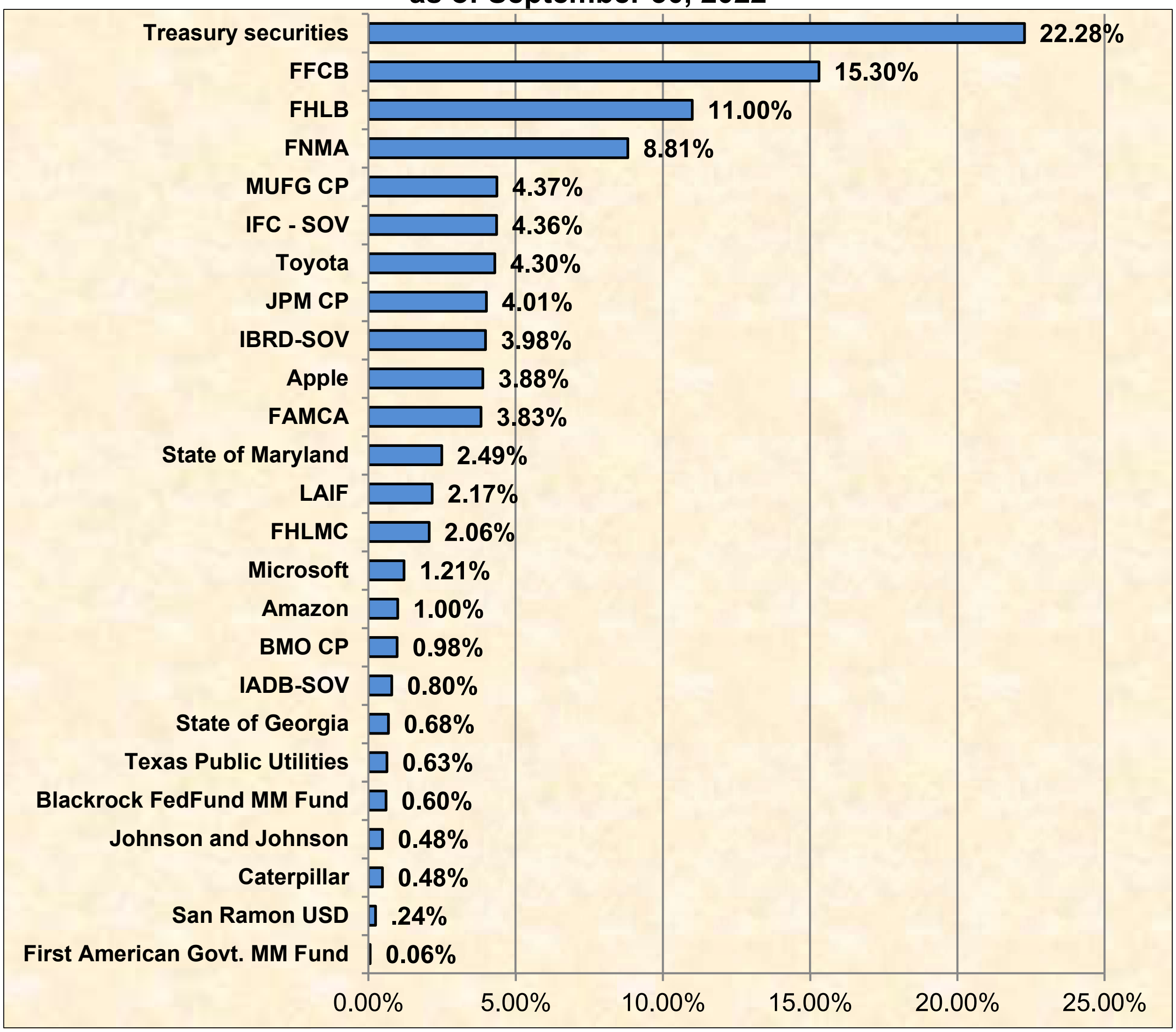
To manage liquidity, the Irvine Pooled Investment Portfolio is invested in Local Agency Investment Funds (LAIF), First American Government money market fund, Blackrock FedFund money market fund and short-term Commercial Paper. Chart 1 shows the asset allocation of the portfolio.

Irvine Pooled Investment Portfolio
Chart 1 - Asset Allocation
as of September 30, 2022



To diversify, the City purchases United States Treasury notes, Commercial Paper, Corporate Medium-term notes, Supranational notes, and securities from several different federal agencies. The five Federal Government sponsored entities the City owns are: Federal National Mortgage Association (Fannie Mae), Federal Home Loan Mortgage Corporation (Freddie Mac), Federal Home Loan Bank (Home Loan), Federal Agricultural Mortgage Corporation (Farmer Mac), and Federal Farm Credit Bank (Farm Credit). Chart 2 identifies portfolio holdings by issuer name.

Irvine Pooled Investment Portfolio
Chart 2 - Holdings by Issuer Name
as of September 30, 2022



Another key component in portfolio management is to ensure that the City has enough funds on hand to meet current expenses. As of September 30, 2022, the overnight to 6-month liquidity level for the Irvine Pooled Investment Portfolio was 10.36 percent, and 25.78 percent liquidity overnight to one year. Chart 3, on the following page, is an aging of investment maturities up to five years (the maximum maturity allowable by policy and state code) of the Irvine Pooled Investment Portfolio.

Irvine Pooled Investment Portfolio
Chart 3 - Aging of Maturing Investments (Maturity Value)
as of September 30, 2022

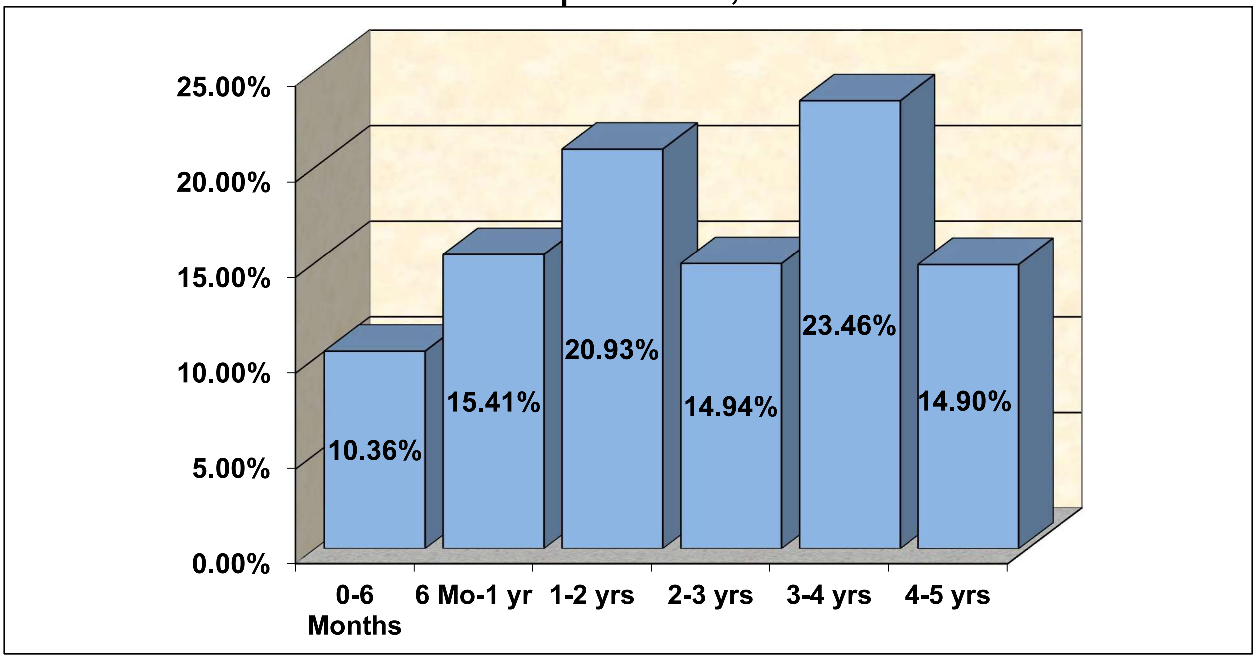
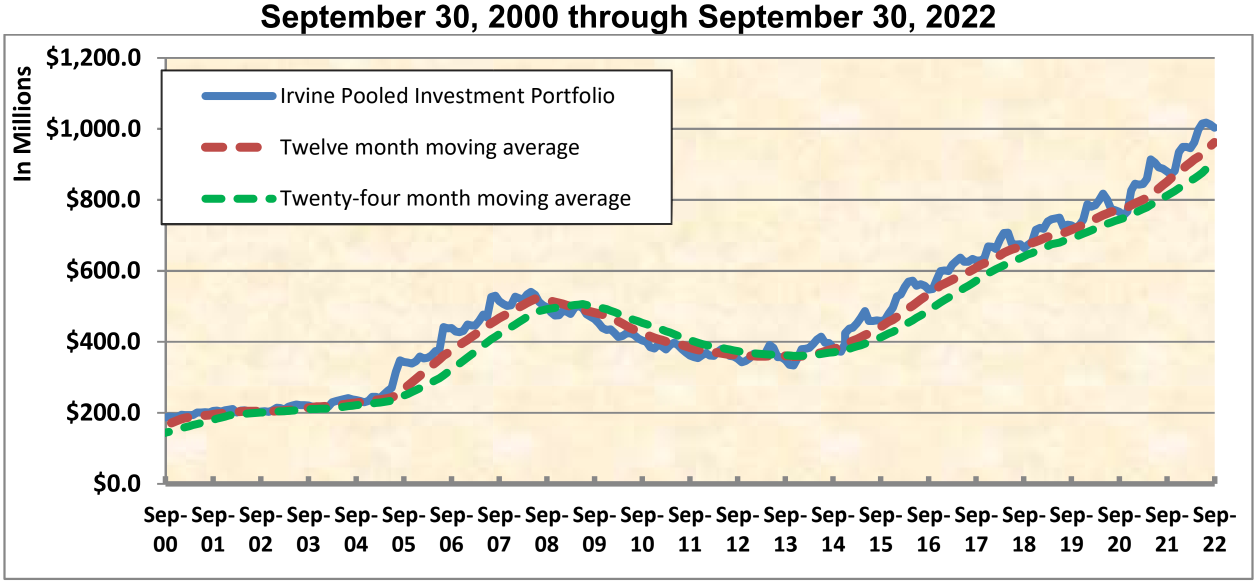
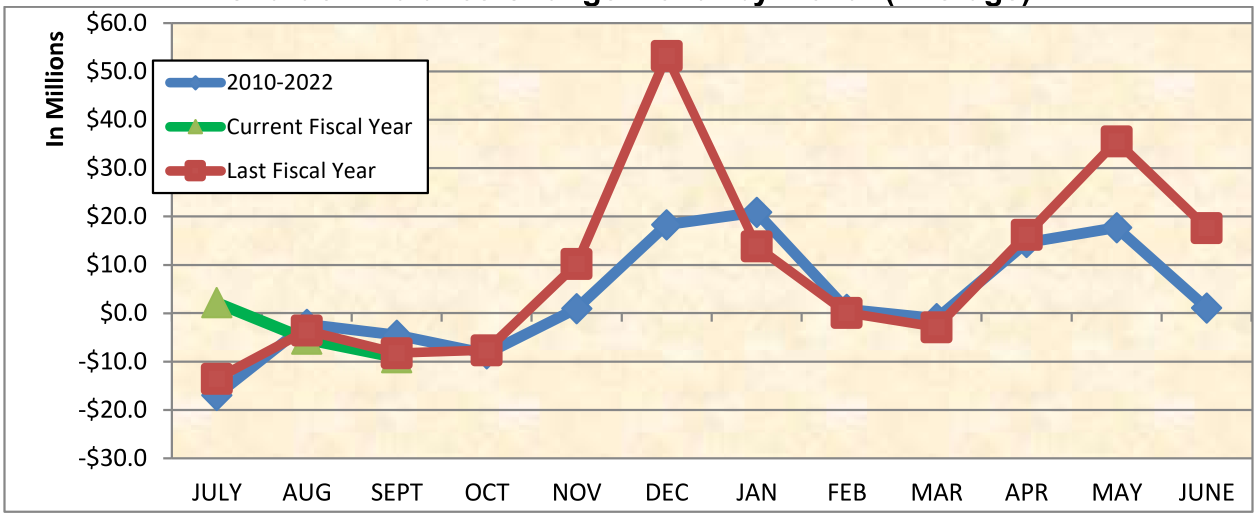


Chart 4 and Chart 5 show the volatility and cyclicality of the Irvine Pooled Investment Portfolio fund balance and cash flows between 2000 and 2022.

Irvine Pooled Investment Portfolio
Chart 4 - Portfolio Balance
September 30, 2000 through September 30, 2022

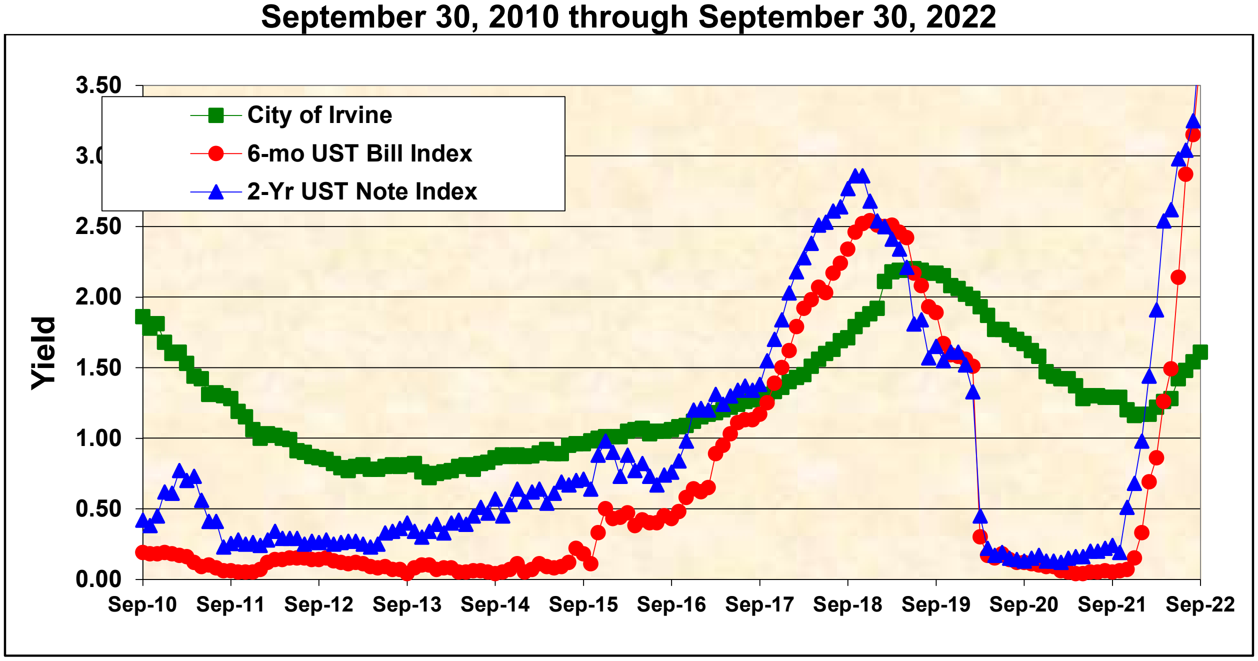


Irvine Pooled Investment Portfolio
Chart 5 – Balance Change Month by Month (Average)



To gauge performance, the City compares the Irvine Pooled Investment Portfolio's book yield to maturity against two reference notes set in the City's Annual Investment Policy: the 6-month United States Treasury (UST) Bill Index and 2-year UST Note Index. Chart 6 compares the average yield to maturity of the portfolio to these reference notes, and shows the spread (difference between the index and the yield to maturity) for the past ten years. The portfolio's book yield is lower than the 6-month UST by 2.10 percent and lower than the 2-year UST by 2.25 percent, due to the Federal Reserve rapidly increasing short term interest rates in response to inflation.

Irvine Pooled Investment Portfolio
Chart 6 - Yield to Maturity Compared to Assigned Indices
September 30, 2010 through September 30, 2022



Bond Proceeds Fund Portfolio

The Bond Proceeds Fund Portfolio contains special district construction and administration funds that are not held by a trustee. These include older bond issues, and funds on hand to finance the City's special district administration. Investment strategy in the Bond Proceeds Fund Portfolio differs from the Irvine Pooled Investment Portfolio due to the different cash needs between the two. The Bond Proceeds Fund Portfolio requires greater liquidity to meet debt-related payments. The account balance in the Bond Proceeds Fund Portfolio fluctuates from quarter to quarter due to the timing of property assessment collections from the County of Orange and subsequent distributions. Several times a year, the portfolio receives special assessments and tax levies collected by the County. The special assessments and tax levies contain three major components:

(1) The collections from the various Assessment Districts (AD), Reassessment Districts (RAD) and Community Facilities Districts (CFD). Upon receipt, the City transfers these funds to the Districts' bond trustees.
(2) The collections for the guaranteed maintenance amount of the Great Park CFD. Upon receipt, the City transfers this amount to the Great Park Fund.
(3) The collections for the Districts' construction and administration funds held and managed by the City. This portion remains in the Bond Proceeds Fund Portfolio.

Fiscal year-to-date investment revenue (interest payments and capital gains) generated by the Bond Proceeds Fund Portfolio as September 30, 2022 was $129,146.

Bond Proceeds Fund Portfolio
Rolling 12-Month Quarterly Comparison

	September 30, 2022	June 30, 2022	March 31, 2022	December 31, 2021
Book Value	$75,000,000	$70,190,000	$62,230,000	$61,987,000
Market Value	$73,557,072	$69,286,333	$61,530,133	$61,828,259
Unrealized Gain/(Loss)	($1,442,928)	($903,667)	($699,867)	($158,741)
Unrealized Gain/(Loss) as % of Book Value	(1.92%)	(1.29%)	(1.12%)	(0.26%)
Average Yield To Maturity	1.60%	0.94%	0.42%	0.22%
Liquidity 0–6 Months	100.00%	100.00%	100.00%	100.00%
Average Days To Maturity	1	1	1	1
Modified Duration in Days	1	1	1	1
Quarterly Interest Earnings	$129,146	$48,521	$31,509	$28,819
Fiscal Year to Date Income	$129,146	$146,917	$98,396	$66,887

Special District Funds Portfolio

The Special District Funds Portfolio contains project and reserve funds for 22 AD and RAD bond issues and five CFD bond issues. Investments in this portfolio are made in accordance with each bond's indenture and the strategy is based on the cash flow needs of each district. The Special District Funds Portfolio must also remain very liquid to provide project funds, when needed, as well as meet debt service payment requirements. Fiscal year to date investment revenue (interest payments and capital gains) generated by the Special District Funds Portfolio as of September 30, 2022 was $461,843.

Special District Funds Portfolio
Rolling 12-Month Quarterly Comparison

	September 30, 2022	June 30, 2022	March 31, 2022	December 31, 2021
Book Value	$165,310,164	$269,883,279	$250,677,550	$265,068,424
Market Value	$165,223,340	$269,668,838	$250,693,545	$265,082,770
Unrealized Gain/(Loss)	($86,824)	($214,441)	$15,995	$14,345
Unrealized Gain/(Loss) as % of Book Value	(0.05%)	(0.08%)	0.01%	0.01%
Average Yield To Maturity	1.88%	1.24%	0.46%	0.06%
Average Days To Maturity	75	97	91	24
Quarterly Interest Earnings	$461,843	$204,113	$22,191	$52,638
Fiscal Year to Date Income	$461,843	$300,025	$95,912	$73,721

Market Conditions

During the first quarter of FY 2022-23, interest rates increased across the yield curve. The Federal Reserve elected to raise the federal funds rate at both its scheduled meetings on July 15, 2022 by 75 basis points to 2.25 - 2.75 percent, and September 21, 2022 by 75 basis points to 3.00 - 3.25 percent. During the quarter, the yield of the 6-month Treasury bill increased 141 basis points to 3.90 percent, the 2-year Treasury note increased 132 basis points to 4.27 percent, and the 5-year notes increased by 105 basis points to 4.09 percent. The Local Agency Investment Fund (LAIF) daily rate increased from .94 percent to 1.60 percent during the quarter. The net effect to the Pooled Investment Portfolio was an increase in the unrealized market value loss to $56.35 million from an unrealized loss of $35.74 million as of September 30, 2022, which is in direct proportion to the stated duration of the portfolio, and the change in market yields.

Inflation continues to exceed the Federal Open Market Committee's (FOMC's) 2.00 percent target, with the headline Personal Consumption Expenditure (PCE) price index peaking +7.00 percent year over year (y/y) in June, while slowly softening to 6.20 percent in August. The core PCE deflator peaked at +5.41% y/y in March while falling to 4.91 percent in August. While lower than the June peak of 9.10 percent, the September Consumer Price Index (CPI) report showed stronger than expected inflation despite hopes for moderation with headline CPI rising 8.20 percent y/y, while Core CPI jumped 6.00 percent y/y. Surges in groceries, shelter, healthcare, utilities such as natural gas and electricity prices, led the upside in headline CPI.

Financial conditions continue to tighten as the FOMC has increased short term interest rates aggressively, and has maximized its goal of quantitative tightening by reducing its balance sheet $95 billion per month. Tighter financial conditions along with higher interest rates seem to be beginning to temper demand and bring it into better alignment with supply, which is still constrained. Output has decelerated so far this year by more than anticipated, suggesting that policy tightening is having some effect. Real gross domestic product (GDP) declined at an annual rate of roughly 1.00 percent in the first half. Real private domestic final purchases stepped down from a 6.40 percent pace last year to an annual rate of only 1.30 percent during the first half of this year.

The moderation in demand due to monetary policy tightening is only partly realized so far. The transmission of tighter policy is most evident in highly interest-sensitive sectors like housing, where mortgage rates have more than doubled year to date and house price appreciation has fallen sharply over recent months and is on track to soon be flat. In other sectors, lags in transmission mean that policy actions to date will have their full effect on activity in coming quarters, and the effect on price setting may take longer. The moderation in demand should be reinforced by the concurrent rapid global tightening of monetary policy.

There also seems to be some tentative signs of rebalancing in the labor market. Anecdotal reports suggest the availability and retention of workers are improving per the FOMC's September Beige Book. For the second month in a row, growth in monthly payroll employment stepped down, slowing from 315,000 in August to 263,000 in September.

There was a sharp 1.10 million decline in job openings from July to August in the Job Openings and Labor Turnover Survey (JOLTS). The ratio of job openings to job seekers declined to 1.70; for purposes of comparison, this ratio was 1.20 prior to the pandemic. The sharp fall in vacancies at a time when initial claims held steady at low levels provides support for the possibility that businesses that faced significant challenges finding and retaining qualified workers following the pandemic may be more inclined than in past cycles to retain rather than lay off their workers as demand weakens. In particular, there is still a sizable 1.20 million shortfall in employment levels relative to pre-pandemic levels in the in-person services sectors that accounted for the majority of September payroll gains, suggesting businesses in those sectors may still be trying to narrow that gap. The unemployment rate remains very low at 3.60 percent with the underemployment rate at 6.70 percent.

The supply – demand imbalance in the labor market is reflected in strong wage growth. The employment cost index increased by an annual rate of 6.3 percent over the second quarter – its highest level in decades. A more-timely data source, average hourly earnings, decelerated slightly to a 4.4 percent annual rate over the third quarter, down from 4.6 percent annual growth in the second quarter. Although it is well above levels consistent with 2 percent inflation, wage growth has been running below current inflation. Strong wage growth along with high rental and housing costs mean that inflation from core services is expected to ease only slowly from currently elevated levels. In contrast, core goods have been expected to return to something closer to the pre-pandemic trend of modest disinflation as a result of demand rotation away from goods to services, coupled with the healing of supply chains and declining core import prices. While disinflation in core goods would help offset the inflationary pressures in services, overall inflation will remain sticky over the next few quarters.

In conclusion, aggressive global and domestic monetary and fiscal tightening will eventually slow demand, and reduce inflationary pressures. Continued supply shocks due to geopolitical issues may shift the economy into a period of stagflation. The City will continue to invest in high quality assets, in a laddered approach, while maintaining its duration targets. The net effect on the City of Irvine's portfolios will be an increase in the unrealized losses as the Federal Reserve continues to raise short term interest rates, and an increase in earnings as the laddered portfolios adjust to market rates.

City of Irvine
Summary of Pooled Investment Portfolio Book Value by Fund *
As of September 30, 2022

General Reserve Funds	**$ 218,034,774**
Capital Projects Funds:	
Capital Improvement Projects	**35,898,846**
Irvine Business Complex	**114,115,054**
North Irvine Transportation Mitigation	**90,675,550**
Orange County Great Park Development	**14,039,934**
Park Development	**42,550,396**
Total	**297,279,779**
Special Revenue Funds:	
Air Quality Improvement	**632,105**
County Sales Tax Measure M	**7,607,558**
Fees and Exactions	**9,945,612**
State Gasoline Tax	**25,985,544**
Grants	**7,405,287**
I Shuttle	**569,225**
Local Park Fees	**147,142,610**
Maintenance District	**(1,092,694)**
Major Special Events	**62,547**
Orange County Great Park	**200,310,976**
Slurry Seal Fees	**167,188**
System Development	**25,272,964**
Total	**424,008,921**
Internal Service Funds:	
Equipment & Services	**34,885,029**
Inventory	**58,328**
Self-Insurance	**21,124,934**
Total	**56,068,290**
Permanent Fund:	
Senior Services	**402,556**
Senior Services Endowments	**500,000**
Total	**902,556**
Fiduciary Fund:	
Successor Agency Debt Service	**(7,262)**
Redevelopment Obligation Retirement	**6,362,865**
Total	**6,355,603**
Total Pooled Investments at September 30, 2022	**$ 1,002,649,923**

Note: Presentation of funds is consistent with the City's Annual Comprehensive Financial Report.
* Balances are not audited

ATTACHMENT 2