REQUEST FOR CITY COUNCIL ACTION

MEETING DATE: MARCH 14, 2023

TITLE: TREASURER'S REPORT FOR QUARTER ENDED DECEMBER 31, 2022

Director of Administrative Services

Oliver Chi
City Manager

RECOMMENDED ACTION

Receive and file the Treasurer's Report for the quarter ended December 31, 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 December 31, 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 \$1.32 billion as of December 31, 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.

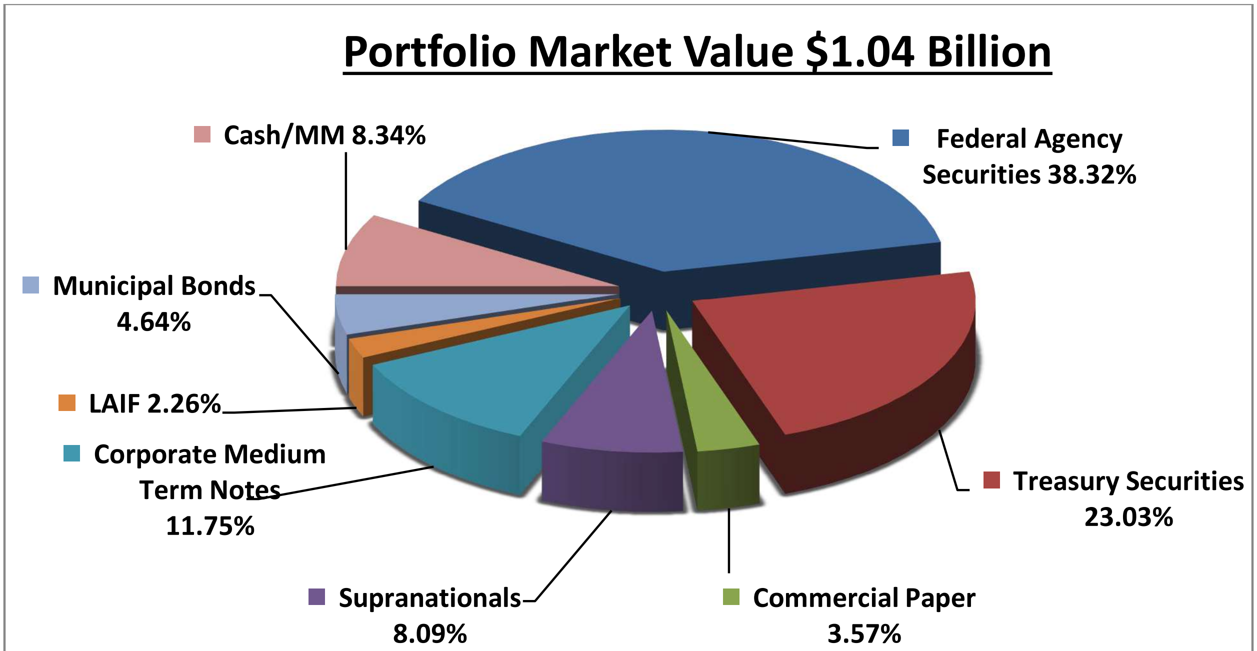
As of December 31, 2022, the City's investment portfolios are in full compliance with the City's Investment Policy, the California Government Code Section 53601, and have sufficient cash flow from a combination of liquid and maturing securities, bank deposits, and income to meet the City's expenditure requirements.

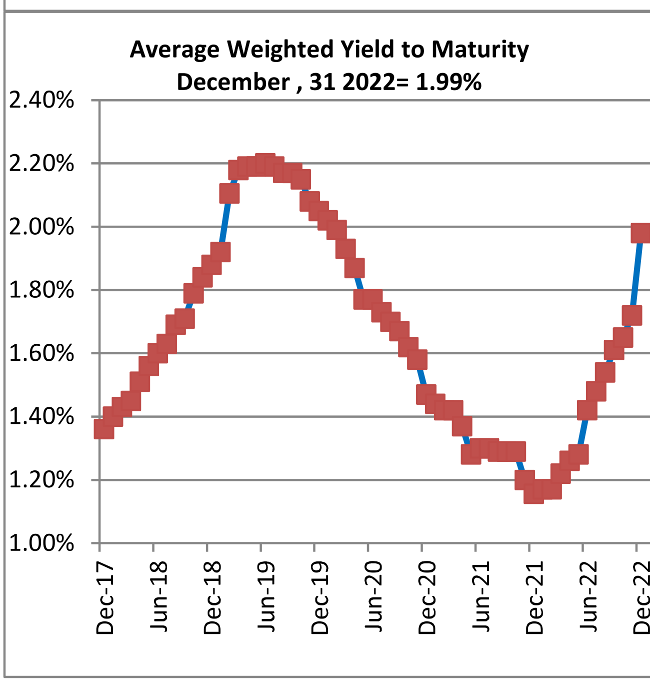
COMMISSION/BOARD/COMMITTEE RECOMMENDATION

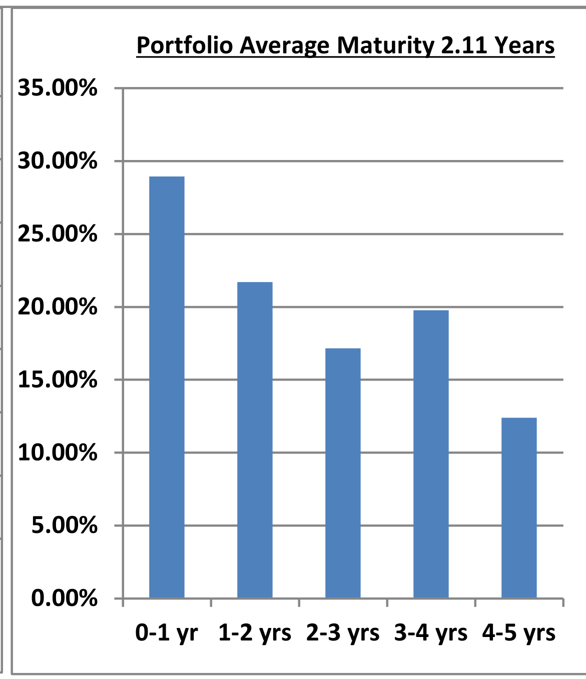
At its regular meeting of February 8, 2023, the Investment Advisory Committee recommended that the City Council receive and file the Treasurer's Report for the quarter ended December 31, 2021 by a 3-0-1 vote (Committee Member Wei absent).

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, the Finance Commission, 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 $8.12 million with investments structured for security and liquidity.

REPORT PREPARED BY Don Collins, City Treasurer

Attachments:

1. Treasurer's Report for the quarter ended December 31, 2022
2. Summary of Irvine Pooled Investment Portfolio by Fund

CITY OF IRVINE
TREASURER'S REPORT
For Quarter Ended December 31, 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 December 31, 2022, combined book value of the three portfolios totaled $1.32 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 December 31, 2022, the book value (purchase price of securities as recorded on the City's books) of the portfolio was $1.09 billion and the average yield to maturity was 1.99 percent. Fiscal year to date investment revenue (interest payments and capital gains) generated by the portfolio as of December 31, 2022 was $6.26 million. The table below compares the portfolio's statistics over a rolling 12-month period.

Irvine Pooled Investment Portfolio
Rolling 12-Month Quarterly Comparison

	December 31, 2022	September 30, 2022	June 30, 2022	March 31, 2022
Book Value	$1,094,758,092	$1,002,649,923	$1,015,081,547	$945,748,989
Market Value	$1,042,801,093	$946,303,312	$979,341,599	$921,034,785
Unrealized Gain/(Loss)	($51,956,999)	($56,346,611)	($35,739,948)	($24,714,204)
Unrealized Gain/(Loss) as % of Book Value	(4.75%)	(5.62%)	(3.52%)	(2.61%)
Average Yield To Maturity	1.99%	1.61%	1.42%	1.22%
Liquidity 0–6 Months	19.82%	10.36%	14.25%	11.11%
Weighted Average Maturity	2.11	2.31	2.32	2.35
Modified Duration (Years)	1.98	2.16	2.19	2.25
Quarterly Interest Earnings	$3,788,206	$2,468,946	$2,802,976	$3,502,502
Fiscal Year to Date Income	$6,257,152	$2,468,946	$14,096,279	$11,293,303

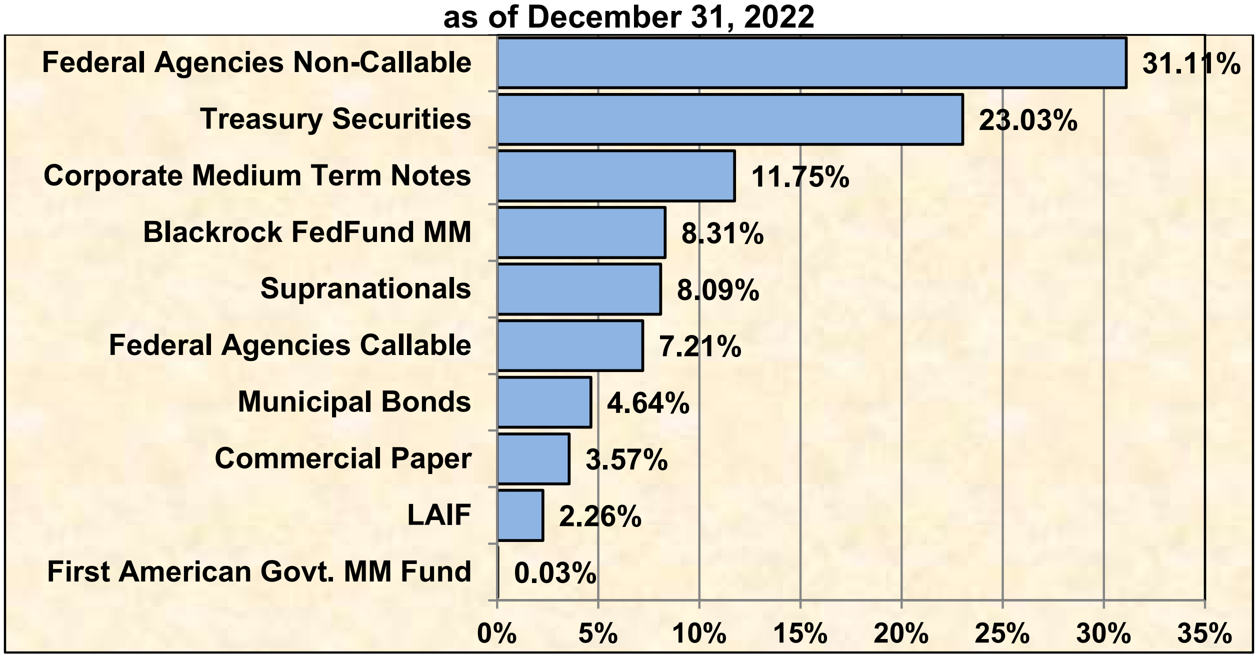
As anticipated, the Irvine Pooled Investment Portfolio's book value increased by $92.11 million from the previous quarter due to a combination of the receipt of property taxes, sales tax, developer fees, temporary holding of bond funds from LAIF (Local Agency Investment

Fund) Pool Two, and a successor agency transfer. Portfolio yield to maturity increased for the quarter ended December 31, 2022 by 38 basis points to 1.99 percent as maturing investments were reinvested in the rising rate environment. With market rates remaining elevated during the quarter, as of December 31, 2022, the portfolio ended with an unrealized loss of $51.96 million as compared to an unrealized loss of $56.35 million on September 30, 2022. This is a normal result of the portfolio's modified duration of 1.98 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.

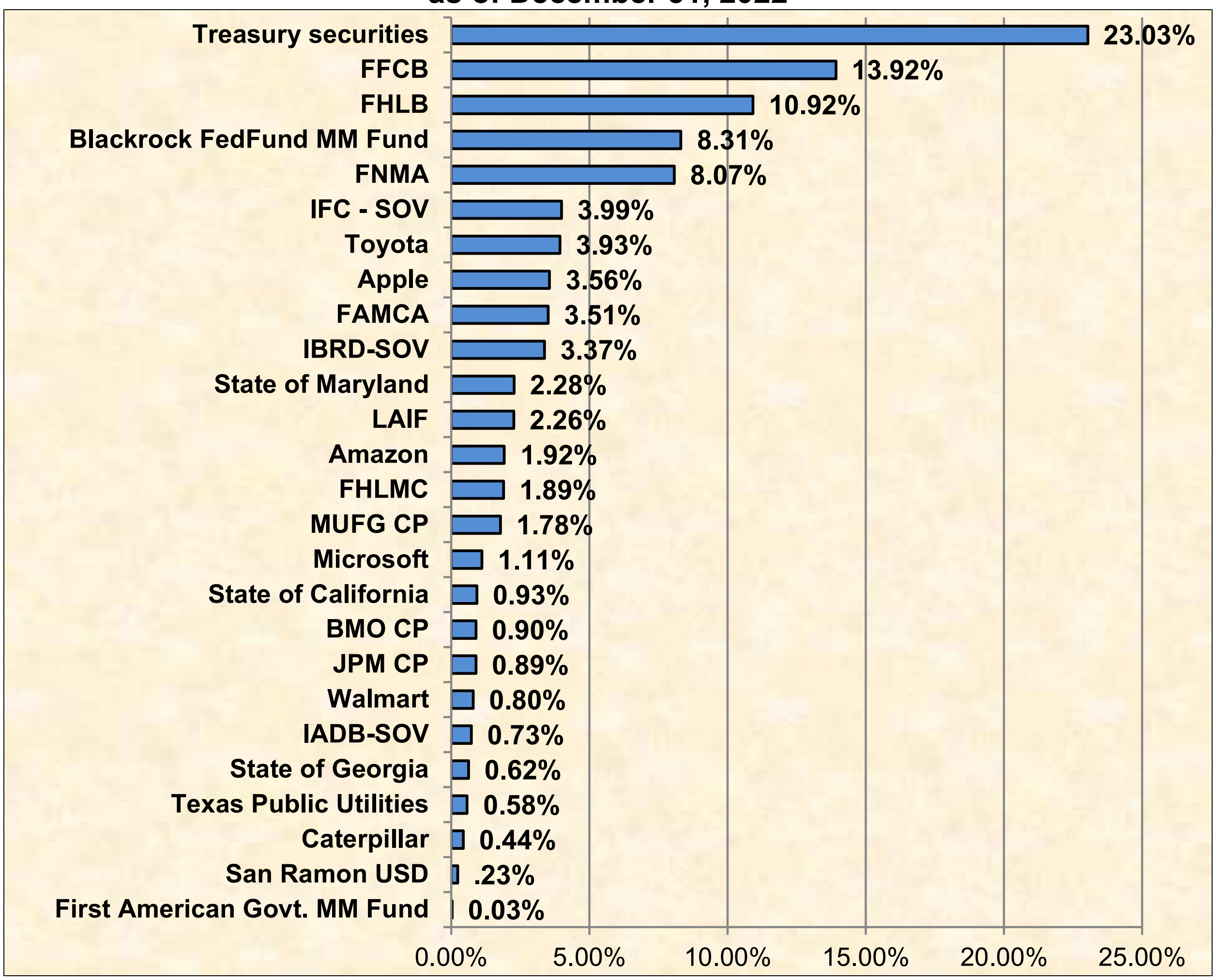
To manage liquidity, the Irvine Pooled Investment Portfolio is invested in Local Agency Investment Funds (LAIF), First American Government money market fund, Blackrock FedFund money market fund and short-term Commercial Paper. Chart 1 shows the asset allocation of the portfolio.

Irvine Pooled Investment Portfolio
Chart 1 - Asset Allocation
as of December 31, 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 December 31, 2022



Another key component in portfolio management is to ensure that the City has enough funds on hand to meet current expenses. As of December 31, 2022, the overnight to 6-month liquidity level for the Irvine Pooled Investment Portfolio was 19.82 percent, and 28.95 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 December 31, 2022

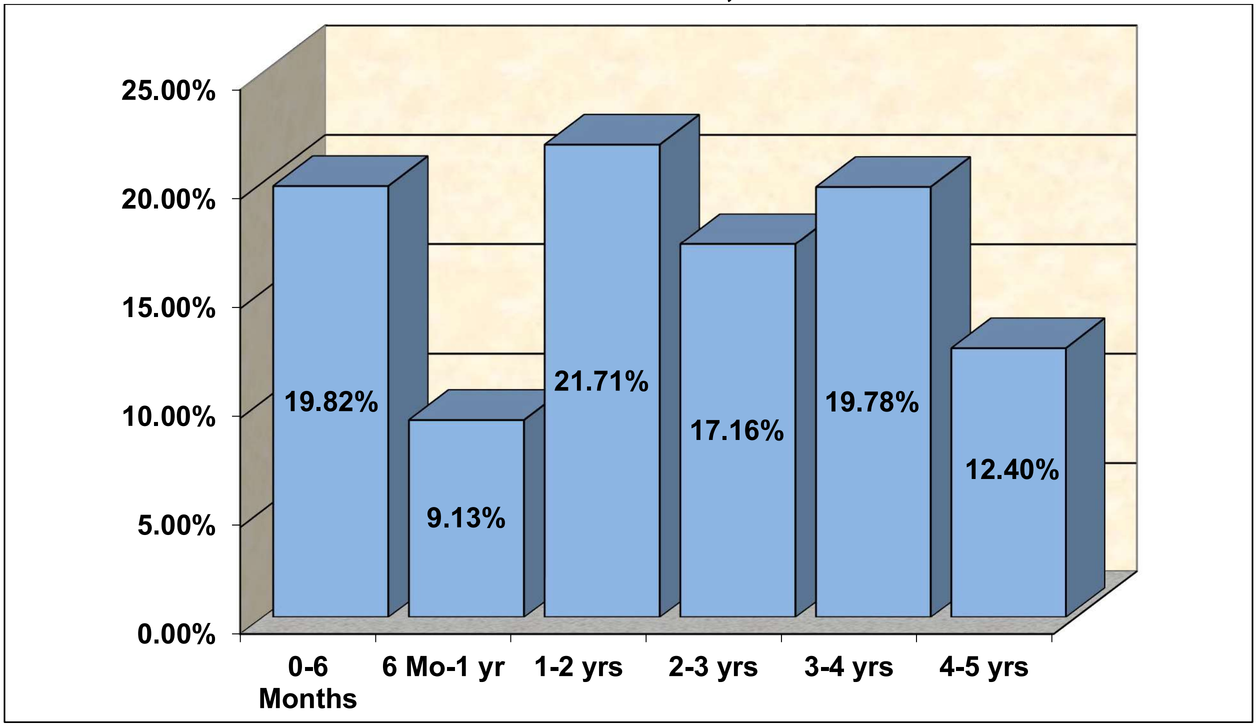
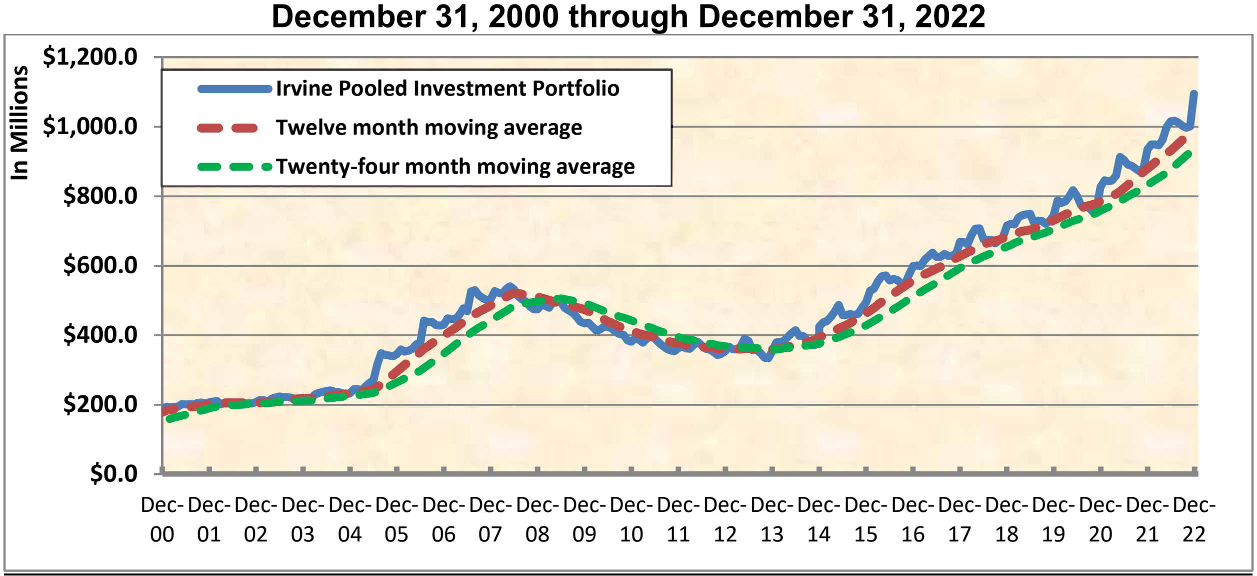
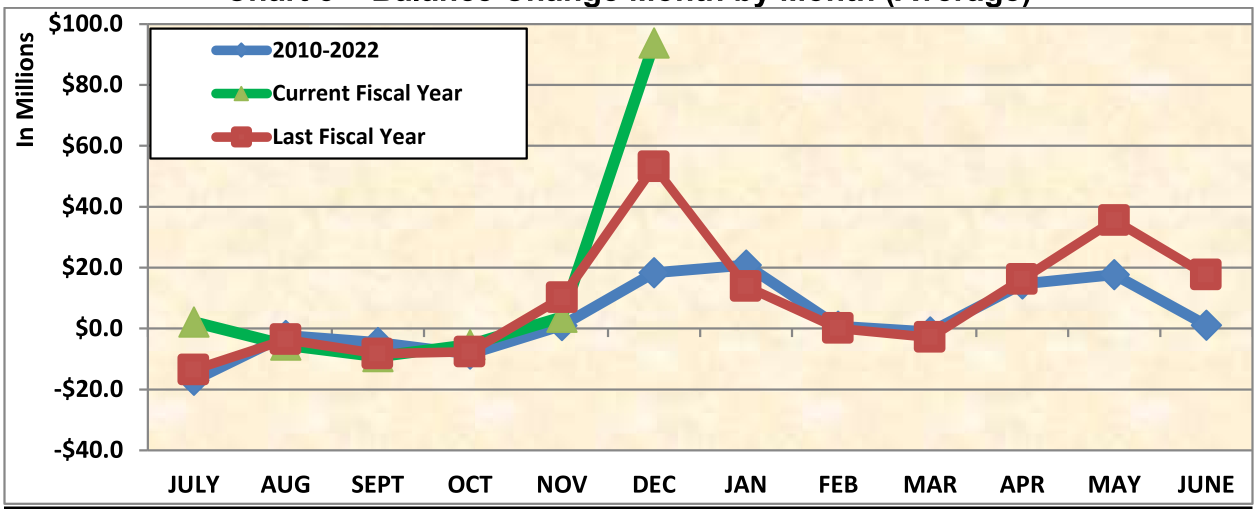


Chart 4 and Chart 5 show the volatility and cyclicality of the Irvine Pooled Investment Portfolio fund balance and cash flows between 2000 and 2022.

Irvine Pooled Investment Portfolio
Chart 4 - Portfolio Balance
December 31, 2000 through December 31, 2022

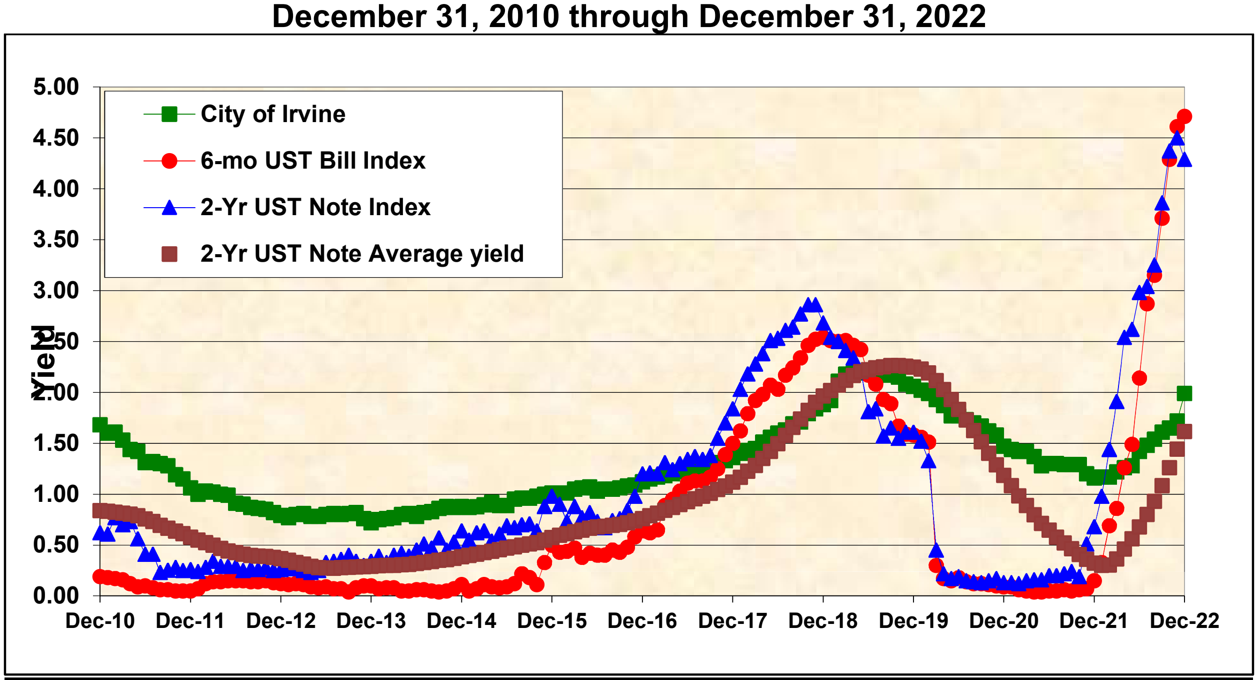


Irvine Pooled Investment Portfolio
Chart 5 – Balance Change Month by Month (Average)



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 2.72 percent and lower than the 2-year UST by 2.30 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
December 31, 2010 through December 31, 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 December 31, 2022 was $372,470.

Bond Proceeds Fund Portfolio
Rolling 12-Month Quarterly Comparison

	December 31, 2022	September 30, 2022	June 30, 2022	March 31, 2022
Book Value	$55,000,000	$75,000,000	$70,190,000	$62,230,000
Market Value	$53,976,409	$73,557,072	$69,286,333	$61,530,133
Unrealized Gain/(Loss)	($1,023,591)	($1,442,928)	($903,667)	($699,867)
Unrealized Gain/(Loss) as % of Book Value	(1.86%)	(1.92%)	(1.29%)	(1.12%)
Average Yield To Maturity	2.29%	1.60%	0.94%	0.42%
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	$243,324	$129,146	$48,521	$31,509
Fiscal Year to Date Income	$372,470	$129,146	$146,917	$98,396

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 December 31, 2022 was $1,485,841.

Special District Funds Portfolio
Rolling 12-Month Quarterly Comparison

	December 31, 2022	September 30, 2022	June 30, 2022	March 31, 2022
Book Value	$165,943,966	$165,310,164	$269,883,279	$250,677,550
Market Value	$165,882,750	$165,223,340	$269,668,838	$250,693,545
Unrealized Gain/(Loss)	($61,216)	($86,824)	($214,441)	$15,995
Unrealized Gain/(Loss) as % of Book Value	0.04%	0.05%	0.08%	0.01%
Average Yield To Maturity	3.60%	1.88%	1.24%	0.46%
Average Days To Maturity	32	75	97	91
Quarterly Interest Earnings	$1,023,998	$461,843	$204,113	$22,191
Fiscal Year to Date Income	$1,485,841	$461,843	$300,025	$95,912

Market Conditions

During the second quarter of FY 2022-23, interest rates continued to increase in the short end of the yield curve between the one month and two year treasuries, with yields dropping slightly in three to five year maturities. Yields also increase in the long end of the yield curve in ten and thirty year maturities. The Federal Reserve elected to raise the federal funds rate at both its scheduled meetings on November 2, 2022 by 75 basis points to 3.75 - 4.00 percent, and December 14, 2022 by 50 basis points to 4.25 - 4.50 percent. During the quarter, the yield of the 6-month Treasury bill increased 85 basis points to 4.75 percent, the 2-year Treasury note increased 14 basis points to 4.42 percent, and the 5-year notes decreased by 9 basis points to 4.00 percent. The Local Agency Investment Fund (LAIF) daily rate increased from 1.60 percent to 2.29 percent during the quarter. The net effect to the Pooled Investment Portfolio as of December 31, 2022 was a small decrease in the unrealized market value loss to $51.96 million from an unrealized loss of $56.35 million, which is in direct proportion to the stated duration of the portfolio, and the change in market yields.

The effects of the pandemic and Russia's war against Ukraine have turned a spotlight on the supply side of the economy and its ability to adapt to rapid changes in demand and to navigate a seemingly never-ending sequence of adverse supply shocks. Inflation remains far too high despite some encouraging signs lately, and therefore remains of great concern to the Federal Reserve. Since last March, the Federal Open Market Committee (FOMC), has been tightening monetary policy through a combination of increasing the federal funds rate by 425 basis points and reducing its balance sheet holdings. Despite seeing a decline in some measures of inflation recently, I expect the FOMC will continue raising interest rates to tighten monetary policy, as stated after the FOMC December meeting. Federal Reserve (Fed) Chairman Jerome Powell stated that "we (the Fed) have the resolve it will take to restore price stability on behalf of American families and businesses." He notes that price stability is a primary Fed responsibility and seems to indicate that the Fed recognizes the importance of tamping down the inflation threat. "Without price stability, the economy does not work for anyone," according to Powell. The appropriate size of future rate increases and on the ultimate level of the federal funds rate will continue to be guided by the incoming data and its implications for the outlook for inflation and economic activity.

Disinflationary pressures are beginning to rise as supply disfunction slowly corrects itself. Core goods consumer prices are deflating, and outside of rents, the sticky service sector is showing visible signs of disinflation as well. Another forward looking data point is the Baltic dry index which has now dropped below pre-COVID-19 levels to levels last seen in 1990. The reopening of China should also continue to put downward pressure on the goods sector. Due to the aggressive tightening of monetary policy by the Fed this past year, money supply (M2) has been contracting at a 3.50 percent annual rate for the first time on record. I suspect this will shed some light on where the real economy will be heading in the next year.

Wage gains have also moderated as measured by the Atlanta Fed, from 6.50 percent in November to 5.50 percent in December. All measures of this index receded and are suggesting we are past peak wage growth. The unemployment rate remained unchanged, ending the quarter at 3.50 percent, but continuing jobless claims rose during the quarter to 1.70 million which may indicate that it is becoming increasingly difficult for those in the labor market, and in a job search to find new work.

Housing continues to be under pressure as well, as existing home sales fell 7.70 percent in November on top of the 5.90 percent slide in October to a 4.09 million annualized unit rate. This is the tenth consecutive decline in resale activity which is the longest on record – data back to 1968. With home prices remaining relatively elevated in conjunction with the rapid rise in interest rates, homebuyer affordability has dropped 36.5 percent in the past twelve months.

U.S. motor vehicle sales fell 6.00 percent month-over-month (MOM) in December after falling 5.60 percent MOM in November to a four-month low of 13.6 million units at an annual rate. Inventory supply days continued to climb to 21 days as this is no longer about supply constraints, it is all about how rising interest rates and tighter credit conditions are impinging on the demand for autos just as has already been the case in the housing market.

Despite measured weakening in high frequency economic data, the recent shift by equity and bond market traders anticipating a Fed "pivot", may in fact delay an easing of monetary conditions as the Fed continues in its attempts to meet their dual mandate of full employment and stable price conditions. 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 may 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 December 31, 2022

General Reserve Funds	$ 267,190,162
Capital Projects Funds:	
Capital Improvement Projects	36,726,062
Irvine Business Complex	116,072,946
North Irvine Transportation Mitigation	90,091,846
Orange County Great Park Development	14,977,574
Park Development	44,161,769
Total	302,030,198
Special Revenue Funds:	
Air Quality Improvement	664,900
County Sales Tax Measure M	8,039,163
Fees and Exactions	9,346,273
State Gasoline Tax	24,071,050
Grants	7,368,812
I Shuttle	571,381
Local Park Fees	149,841,602
Maintenance District	3,629,512
Major Special Events	256,887
Orange County Great Park	240,734,593
Slurry Seal Fees	1,481,938
System Development	19,471,333
Total	465,477,444
Internal Service Funds:	
Equipment & Services	35,711,095
Inventory	33,317
Self-Insurance	20,204,797
Total	55,949,209
Permanent Fund:	
Senior Services	378,340
Senior Services Endowments	500,000
Total	878,340
Fiduciary Funds:	
Successor Agency Debt Service	3,232,739
Redevelopment Obligation Retirement	-
Total	3,232,739
Total Pooled Investments at December 31, 2022	$ 1,094,758,092

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

ATTACHMENT 2