



MEMORANDUM

Agenda Item #: 3
Meeting Date: 4/28/2020

TO: HONORABLE MAYOR AND CITY COUNCIL

FROM: ELIZABETH YING, CITY TREASURER /s/

**SUBJECT: QUARTERLY REPORT OF CASH AND INVESTMENTS -
MARCH 31, 2020**

DATE: APRIL 28, 2020

ISSUE/PURPOSE

Acceptance and discussion of the Quarterly Cash and Investment Report.

BACKGROUND AND DISCUSSION

Please refer to ATTACHMENT A for the Quarterly Cash and Investment Report.

FISCAL IMPACT

No fiscal impact is associated with this report. This report is for the City Council to receive and file.

NOTIFICATION

This report has been posted and noticed consistent with the City's requirements.

ALTERNATIVES

The alternatives available to the City Council include:

1. Receive and file the report
2. Request additional information

ATTACHMENTS:

- A. Quarterly Cash and Investment Report dated March 31, 2020



City of Palos Verdes Estates

Third Quarter Cash and Investment Report March 31, 2020

BACKGROUND

The Treasurer's report is presented to the City Council in accordance with California Government Code 53646. Additionally, as required by City's Investment Policy, Sections 8 and 17, the investment portfolio and this Quarterly Report have been reviewed by the City Treasurer and the Investment Policy Advisory Committee. The Investment Policy Advisory Committee consists of the following members:

- Brad Boyd, Citizen member
- Jeff DeLarme, Citizen member
- Vacant: City Finance Director (ex officio)
- Victoria Lozzi, City Council member, former Treasurer (ex officio)
- Elizabeth (Liz) Ying, City Treasurer, Chairperson

CERTIFICATION

At March 31, 2020, the City's cash and investment portfolio totaled \$28.6 million, substantially unchanged from December 31, 2019.

The portfolio is in compliance the City's 2019-20 Investment Policy and with California Government Code Section 53601.

Although the full impact of the COVID crisis has yet to be quantified, we believe that there is sufficient cash flow from liquid and maturing securities, bank deposits, and anticipated revenues to meet the City's forecasted expenditures for the next six months.

EXECUTIVE SUMMARY

Safety: The City seeks to mitigate credit risk by limiting purchases to the safest types of investments. The portfolio is comprised of:

- \$3.3 million of available cash in the City's Union Bank Demand Deposit Accounts and Money Market Account.
- \$9.1 million in Local Agency Investment Fund (LAIF). LAIF is a program allowing local agencies to invest in a pool administered by the California State Treasurer's Office. The State cannot borrow or withhold LAIF money per California Government Code Sections 16429.3 and 16429.4.

Portfolio at a glance	Q/E 3/31/20
Total Cash & Investment Balance	28,646,815
Weighted Avg Yield Invested Assets*	1.98%
Weighted Avg Maturity Invested Assets*	2.95 years
* Excludes pooled & money market accounts	

COVID-19 IMPACT

In response to the COVID pandemic, the Fed cut the fed funds rate by 50bps in a March 3rd emergency action to 1-1.25bps, then further to 0-0.25bps on Sunday, March 15th, ahead of its scheduled meeting. Prior, as late as its Jan 29-30 meeting, the Fed had maintained its targeted 1.50-1.75 fed funds range, with expectations to hold steady through most of 2020.

3 month/5 year treasury rates tumbled from 1.48%/1.69% at 12/31/19 to 0.14%/0.34% at 4/15/20. In the interim, 3 month rates closed at 0% and was, at times, negative in intra-day trading.

As a result, issuers exercised early call options, with \$5.5 million being called over the quarter. Together with scheduled maturities, the yield of these called or maturing securities averaged 1.9%. Interestingly, CD spreads widened as investors flocked to the safety of treasuries and agencies, partially offsetting the plummeting reference rates. We were able to reinvest \$5 million at an average weighted yield of 1.6%.

In the near term, COVID will reduce City's concession revenues and development/licensing fees (FY19-20 budget of \$1.5 million and \$1.3 million vs PVE's ~\$20 million of total General Fund revenues). Long term, COVID will likely reduce property tax revenue and add to the City's pension obligations, as pension investment yields fall. Given uncertainty around the size and duration of such impacts, and pending direction from Council and Staff, we have maintained higher liquidity, by investing in pool funds. Many pooled fund yields are currently higher than new term investments, due to the benefit of prior higher yielding investments within the pools. However, yields will likely drop rapidly as pool managers reinvest. This strategy, incurs the opportunity cost of not "locking in" rates, but aligns with our mandate to prioritize safety and liquidity.



- \$0.5 million in Joint Powers Authority California Asset Management Program (CAMP). This program is one authorized under California Government Code Section 53601(p). CAMP's Cash Reserve fund is rated by S&P as AAA(m).
- \$7.6 million in FDIC- or NCUA-insured CDs, and
- \$8.0 million in Agency securities which carry an implicit government guarantee and are held in the City's Union Bank Custody account.

Liquidity: Liquidity is managed utilizing pooled funds with same day liquidity in combination with maturing securities and forecasted revenues. At 3/31/20, the City had \$13.0 million in cash and same day liquidity, and has \$1.2 million in investments maturing within six months. The COVID pandemic has resulted in unanticipated expenses, and will reduce the City's concessions revenue, licensing and development fees. Longer term expectations include: (1) lower property tax receipts beginning in FY 21-22, assuming a prolonged recession, and (2) higher pension obligations due to anticipated shortfalls in CALPERS' returns. Although the full impact is not yet quantified, together with \$9.6 million of anticipated tax and other revenue, we expect to meet the City's original six months projected expenditures of \$13.0 million.

Yield: The weighted average yield, excluding pooled funds, is 1.98%, lower than 2.07% at 12/31/19. The City's investment in the LAIF pool returned a 2.03% apportionment for the quarter, and continues to be among the highest yielding asset classes in the portfolio. We expect overall yields to drop further due to early call redemptions of higher yielding investments, and to the lower yields of new investments. For example: 2/3 year Treasuries yielded 0.20%/0.24% on 4/15/20 compared with 1.58% /1.61% on 1/8/20.

PORTFOLIO OVERVIEW

(as of 3/31/20, unless otherwise stated)

Asset Class	Book Value	Market Value*	BV % Portfolio	Policy Max
Pooled Funds	9,736,717	9,736,717	34.0%	100%
Cash	2,993,853	2,993,853	10.5%	100%
M Mkt	279,245	279,245	1.0%	100%
CDs	7,637,000	7,745,994	26.7%	30%
Gov Obligation	8,000,000	8,031,540	27.9%	100%
Total	28,646,815	28,787,349	100.0%	

* Market Value for government securities and CDs are provided by Union Bank a/o 3/31/20 and assumed accurate. Pooled Funds are assumed at book value.

At 3/31/20, market value of the portfolio totaled \$28.7 million, showing an estimated unrealized gain of \$140,534, up from \$43,680 in the previous quarter as market rates trended downward. Since the City's investment philosophy is to hold investments to maturity whenever possible in order to reduce market risk, full-face (par) value is received, and no realized gain or loss of funds is expected.

INCOME

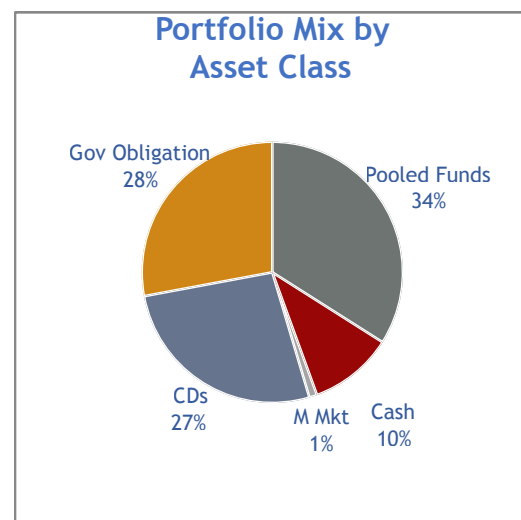
Income collected over the quarter is shown below:

Security	Interest Collected Q3/2020
Govt Obl. + CDs	92,063
LAIF	34,128
JPA Camp	2,095
LACIP (est.)	193
MMA	35
TOTAL \$	128,514

PORTFOLIO COMPOSITION

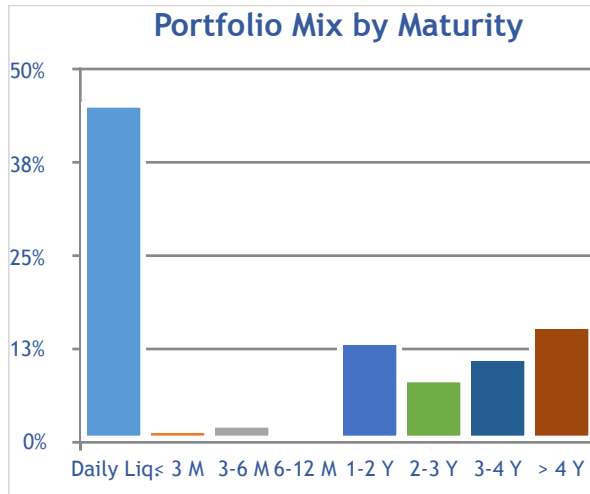
City's investment portfolio is governed by California Government Code Section 53601, and by the City's Investment Policy, which is more conservative. The City's Investment Policy is reviewed annually, and its portfolio is reviewed at least quarterly by the City Treasurer and Investment Policy Advisory Committee.

At 3/31/20, Pooled Funds, primarily LAIF, constituted 31.7% of the portfolio. We expect to invest in other pools in order to maintain some diversification among pool sponsors and servicers.



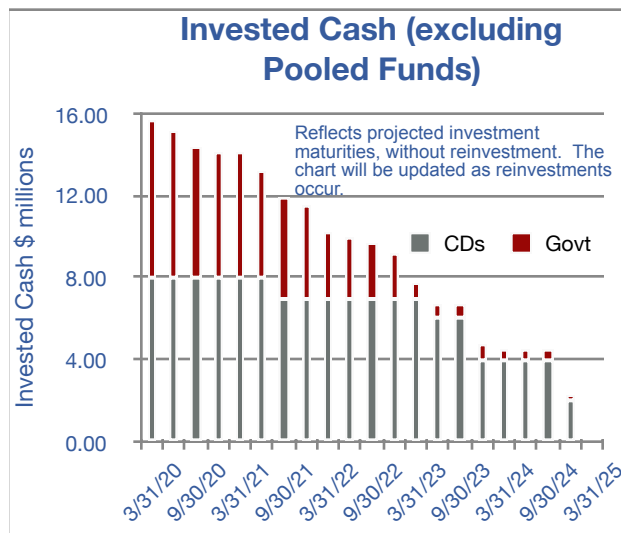


MATURITY SCHEDULE



The maximum maturity allowable by both the California Government Code and the City's Investment Policy is five years.

Plummeting market yields over the past quarter have cause issuers to exercise early call options, resulting in much higher (45%) daily liquidity than normally desired, although it also resulted in partially relieving the previously high concentration of 1-2 year maturities.



ACTIVITY

During the quarter, seven securities totaling \$5.7 million were called and one \$250,000 CD matured. 11 securities totaling almost \$5 million were purchased, with the majority being FDIC insured negotiable CDs, which provided considerably better yields over agencies in the current risk averse market.

Date	Description	Asset Name	Principal
1/10/20	PURCHASED	BMW BK NORTH AMER SA 1.750% 1/10/23	245,000
1/16/20	PURCHASED	ALLY BK MIDVALE UTAH 1.850% 1/17/23	245,000
1/17/20	PURCHASED	WELLS FARGO NATL BK 1.900% 1/17/23	245,000
1/31/20	FULL CALL	BAYCOAST BK SWANSEA 3.000% 1/31/24	-250,000
2/25/20	PURCHASED	FEDERAL NATL MTG 1.80%	1,000,000
2/26/20	FULL CALL	FHLB BDS 1.800% 11/26/21	-2,000,000
2/28/20	FULL CALL	FEDERAL HOME LOAN BA 2.150% 8/28/24	-1,000,000
2/28/20	PURCHASED	FEDERAL HOME LN MTG 1.750% 2/28/25	1,000,000
2/28/20	PURCHASED	ENERBANK USA C/D 1.700% 2/28/25	249,000
3/12/20	FULL CALL	FHLB BDS 1.500% 6/30/21	-1,000,000
3/25/20	PURCHASED	FEDERAL FARM CR 1.200% 3/25/25	1,000,000
3/26/20	PURCHASED	AXOS BK SD C/D 1.600% 3/27/23	249,000
3/27/20	PURCHASED	TEXAS EXCHANGE C/D 1.000% 3/25/22	249,000
3/30/20	FULL CALL	BAR HARBOR BKG & TR 2.650% 3/29/22	-250,000
3/30/20	FULL CALL	JPMORGAN CHASE C/D 1.700% 9/30/21	-246,000
3/30/20	FULL CALL	FNMA NT 1.600% 9/29/21	-1,000,000
3/30/20	MATURED	CITIBANK NATL ASSN 2.500% 3/30/20	-250,000
3/30/20	PURCHASED	LAKELAND BK 1.150% 3/30/23	248,000
3/31/20	PURCHASED	BANK LEUMI USA NEW 1.450% 3/31/23	245,000



MARKET OUTLOOK

It is difficult to seriously consider any forecast given the most devastating pandemic since the 1918 Spanish Flu, the greatest economic contraction since the 1929 Great Depression, the largest oil price decline ever, and greatest government/central bank intervention ever.

Furthermore, irrespective of when social distancing and other restrictions are lifted, recovery will ultimately depend on individuals and their willingness to go back to work, to gather at restaurants and entertainment venues, to shop and to travel. This in turn, depends on perceived infection rates, availability of vaccines and effective treatment therapies, and/or confidence in reaching "herd immunity."

International Monetary Fund 2020 World Economic Outlook (April, 2020):

A. Base Scenario: Assuming a Q2 peak in the pandemic and required containment, and that policy actions are effective in preventing widespread bankruptcies, extended job losses and systemic financial strains, the global economy is forecast to fall -3% in 2020, a downgrade of 6.3% points, then grow by 5.8% in 2021. US GDP is forecast to contract 5.9% in 2020, and to grow 4.7% in 2021.

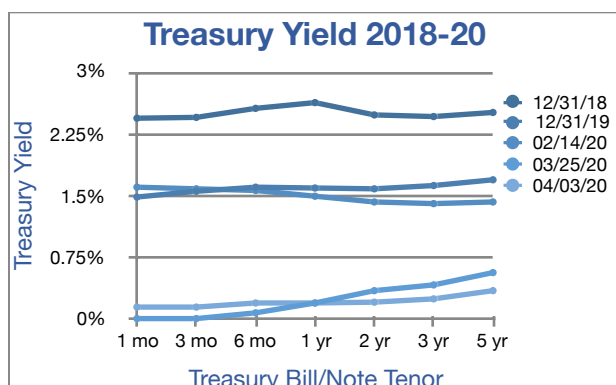
B. Scenarios 2 and 3: If the pandemic persists into 2H/2020, leading to longer containment, worsening financial conditions and further breakdown in global supply chain, IMF forecasts World GDP to fall another -3% from its baseline. If the pandemic extends into 2021, the forecast is for another -8% decline.

IMF estimated that the \$8 trillion in fiscal stimulus being poured in by governments will likely not be enough, and governments will need to bear an increasing debt load. However, according to IMF Chief Economist, Gopinath, "As long as interest rates remain very low, as we're seeing, and we get the recovery that we are projecting, then the combination should help in bringing down debt levels slowly over time."

US Outlook: Federal Reserve Bank of New York President Williams noted last week that even a swift resolution to the pandemic is unlikely to bring a fast economic recovery. "Even as a pandemic passes through and the economy comes back, I expect demand to be weak and therefore needing strong monetary support, fiscal policy support as well, to get our economy back to full strength over the next couple of years."

Rate Forecast: Post-pandemic, the US will be left with record fiscal deficits, and the burden of continued expansionary fiscal policy, which may lead to higher inflation. Others believe that rates will remain low for an extended period, as: 1) individuals and firms seek to rebuild savings and 2) to invest more conservatively, and finally, 3) that central banks will likely keep rates low, given higher debt/GDP ratios and debt servicing needs.

The issue of negative rates prompted Fed Chairman Powell to note, "We do not see negative policy rates as likely to be an appropriate policy response here in the US." That said, the market recently drove rates negative in intraday trading.



PORTFOLIO STRATEGY

As stipulated in the City's Investment Policy, the portfolio is managed with the priorities of (1) safety, (2) liquidity and finally (3) yield. As of March 31, 2020, pooled fund balances are higher than desirable and will grow further, given April tax receipts, the likelihood of additional call option exercises, and the advisability of maintaining more liquidity given unquantified COVID impacts. As such, we plan to diversify pool holdings and consider other securities, allowed within the City's investment policy, which add may value.

PORTFOLIO CHALLENGES

Challenges include:

- Uncertain COVID impact dictates keeping higher liquidity.
- Concentration in daily liquidity and one year or less maturities, due to early calls and limited investment options.
- Extreme low rate environment.

PORTFOLIO DETAIL (see chart)

