



ADMINISTRATIVE SERVICES DEPARTMENT

CITY HALL
10300 TORRE AVENUE • CUPERTINO, CA 95014-3255
TELEPHONE: (408) 777-3220 • FAX: (408) 777-3109
CUPERTINO.ORG

CITY COUNCIL STAFF REPORT

Meeting: November 15, 2022

Subject

Consider the Treasurer's Investment Report for Quarter Ending September 30, 2022

Recommended Action

Accept the Treasurer's Investment Report for Quarter Ending September 30, 2022

Discussion

Background

On May 19, 2022, the City Council approved the City Investment Policy. Per the City's Investment Policy, the Treasurer shall submit a quarterly investment report to the City Council approximately 45 days following the end of the quarter. In addition to the quarterly investment reports, monthly transaction reports are submitted to the City Council within 30 days of the end of the reporting period per California Government Code Section 53607. The quarterly investment report offers a more extensive discussion of the City's economy, cash flow, and investments.

Treasurer's Investment Report

The report provides an update on the City's investment portfolio for the quarter ending September 30, 2022. The report is as of October 20, 2022.

The attached statements include balances and transactions of the City's investments with the Local Agency Investment Fund (LAIF) and Chandler Asset Management. The Chandler investment report provides information on the investment type, issuer, purchase date, maturity date, cost value, par value, and market value for each security, as well as the weighted average maturity and weighted average yield of all investments.

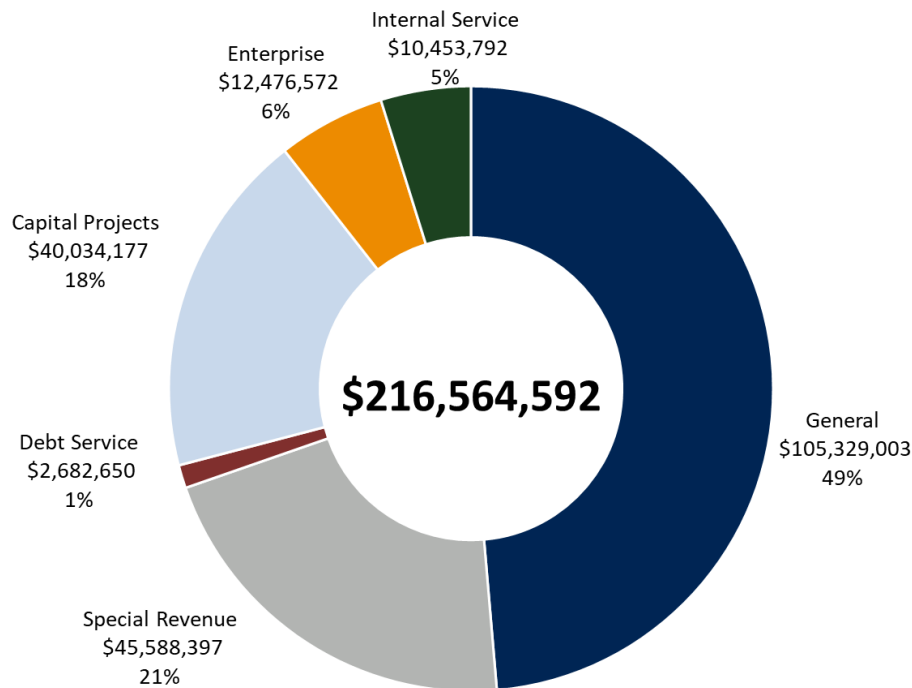
While not governed by the City's Investment Policy, statements for the Public Agency Retirement Services (PARS) Section 115 Trusts are also attached per a request from the Treasurer's Report sub-committee.

As of September 30, 2022, the City's General Ledger cash and investments balance was \$216.6 million, a \$2.6 million decrease from the prior quarter.

Cash and Investments – General Ledger Balance

Fund Type	Quarter Ending June 30, 2022	Quarter Ending September 30, 2022
General Fund	116,013,718	105,329,003
Special Revenue	45,485,096	45,588,397
Debt Service	6,850	2,682,650
Capital Projects	37,826,578	40,034,177
Enterprise	12,276,728	12,476,572
Internal Service	7,615,442	10,453,792
Total	\$219,224,412	\$216,564,592

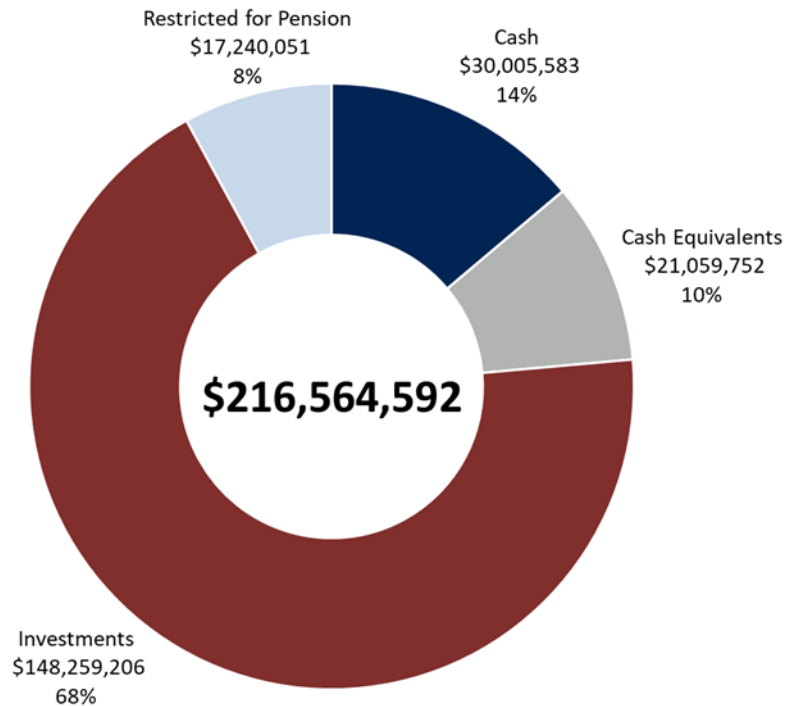
Cash and Investments by Fund



The \$216.6 million in cash and investments includes \$30.0 million in cash, \$21.1 million in cash equivalents, \$148.3 million in investments, and \$17.2 million restricted for funding pension costs.

The City pools cash for all funds except restricted funds. However, the City accounts for interest earnings, revenues, and expenditures separately for each fund to adequately meet the purpose and restrictions of each funding source. Pooling funds is a common and appropriate practice used in public agencies. By pooling funds, the City can benefit from economies of scale, diversification, liquidity, and ease of administration.

Cash and Investments by Type



Cash and Investments – General Ledger Balance

	Quarter Ending June 30, 2022	Quarter Ending September 30, 2022	% of Portfolio
Cash in banks and on hand			
Operating Checking (Wells Fargo)	32,634,316	29,966,945	14%
Workers' Compensation Checking (Wells Fargo)	17,654	25,305	0%
Payroll Checking (Wells Fargo)	-	-	0%
Restricted for Bond Repayments ¹ (BNY Mellon)	8,333	8,333	0%
Petty Cash and Change	5,100	5,000	0%
Cash Equivalents			
Local Agency Investment Fund	21,059,752	21,059,752	10%
Investments			
Investments (Chandler)	148,259,206	148,259,206	68%
Restricted for Pension ² (PARS)	17,240,051	17,240,051	8%
Total Cash and Investments³	\$219,224,412	\$216,564,592	100%

¹ Cash held by fiscal agent for bond repayments

² In accordance with GASB 67/68, the assets in the Section 115 Pension Trust are reported as restricted cash and investments in the General Fund. The assets can only be used to fund CalPERS costs.

³ Assets in the Section 115 OPEB Trust are excluded as the City cannot use these assets to fund its own operations. The assets are held in trust for retirees' post-employment health benefits.

The table below shows the bank balances for the City's cash and investments. Bank and General Ledger balances differ due to timing. Bank balances do not include outstanding checks and deposits in transit. The General Ledger is updated quarterly with interest earnings and annually with the year-end investment market values.

Cash and Investments – Bank Balance

	Quarter Ending June 30, 2022	Quarter Ending September 30, 2022	% of Portfolio
Cash in banks and on hand			
Operating Checking (Wells Fargo)	32,249,699	31,613,882	15%
Workers' Compensation Checking (Wells Fargo)	19,738	25,694	0%
Payroll Checking (Wells Fargo)	-	-	0%
Restricted for Bond Repayments ¹ (BNY Mellon)	8,333	8,333	0%
Cash Equivalents			
Local Agency Investment Fund	21,059,752	21,099,180	10%
Investments			
Investments (Chandler)	148,744,657	145,810,488	68%
Restricted for Pension ² (PARS)	17,240,051	16,385,602	8%
Total Cash and Investments³	\$219,322,230	\$214,943,179	100%

¹ Cash held by fiscal agent for bond repayments

² In accordance with GASB 67/68, the assets in the Section 115 Pension Trust are reported as restricted cash and investments in the General Fund. The assets can only be used to fund CalPERS costs.

³ Assets in the Section 115 OPEB Trust are excluded as the City cannot use these assets to fund its own operations. The assets are held in trust for retirees' post-employment health benefits.

Local Agency Investment Fund (LAIF)

LAIF is an investment pool administered by the State of California Treasurer and governed by California Government Code. The City can withdraw funds from LAIF at any time. As a result, the City uses LAIF for short-term investment, liquidity, and yield.

As of September 30, 2022, the City's LAIF account had a balance of \$21.1 million. In July 2022, the City received a quarterly interest deposit of \$39,428 for the quarter ending June 30, 2022. The interest rate was 0.75%. The City did not make any deposits or withdrawals in the quarter ending September 30, 2022.

Investment Portfolio

In FY 2018-19, the City selected Chandler Asset Management for investment management services through a Request for Proposal (RFP). Chandler began their work with the City in the winter of 2018, conducting multiple meetings with staff to determine an investment structure and strategy. Starting in March 2019, Chandler invested the City's portfolio by purchasing agency issues, corporate medium-term notes, and negotiable certificates of deposit.

Under the City's Treasurer's direction, Chandler Asset Management manages the City's investment portfolio per the City's investment objectives. The City's investment objectives, in order of priority, are to provide:

- Safety to ensure the preservation of capital in the overall portfolio
- Sufficient liquidity for cash needs
- A market rate of return consistent with the investment program

The performance objective is to earn a total rate of return through a market cycle equal to or above the return on the benchmark index. Chandler Asset Management invests in high-quality fixed-income securities consistent with the City's Investment Policy and California Government Code to achieve the objective.

As of September 30, 2022, the portfolio's market value was \$145.8 million, compared to \$148.7 million at the end of the previous quarter. The table below includes historical comparisons of the City's portfolio:

	June 30, 2022	September 30, 2022
Market Value	148,744,657	145,810,488
Par Value	155,016,024	155,548,714
Book Value	155,117,380	155,475,533
Average Maturity	2.74 years	2.76 years
Average Modified Duration	2.39	2.38
Average Purchase Yield	1.41%	1.58%
Average Market Yield	3.25%	4.49%
Average Quality ¹	AA+/Aa1	AA/Aa1

¹ S&P and Moody's respectively

The portfolio's market value fluctuates depending on interest rates. When interest rates decrease after an investment is purchased, the market value of the investment increases. In contrast, when interest rates increase after an investment is purchased, the market value of the investment decreases. At the time of purchase, the City intends to hold all investments until maturity, so changes in market price do not affect the City's investment principal. The market values were provided by Chandler Asset Management.

Section 115 Trust Investment Portfolio

The City established Section 115 Trusts to reduce pension rate volatility, and pre-fund Other Post-Employment Benefits (OPEB) costs. A Section 115 Trust is a tax-exempt investment tool that allows local governments to pre-fund pension and retiree health costs. Once contributions are placed into the trust, assets from the trust can only be used to fund retirement plans.

The Section 115 Trusts are not governed by the City's Investment Policy but by separate investment policies. On December 7, 2021, City Council approved the Pension Trust Investment Policy and OPEB Trust Investment Policy. Public Agency Retirement Services (PARS) administers the trust, and US Bank manages the investments per the investment policies.

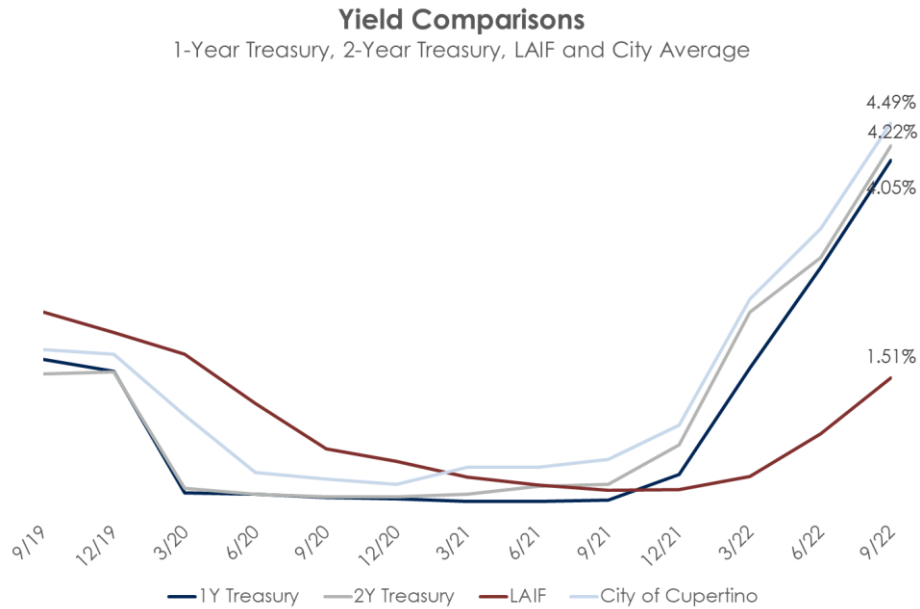
Both Section 115 Trusts are invested in "balanced" portfolios. The investment objective is designed to provide a moderate amount of current income with moderate growth of capital. It is recommended for investors with a long-term time horizon. The strategic asset allocation ranges and targets for this objective are:

Asset Class	Range	Target
Equities	50-70%	63%
Fixed Income	20-40%	29%
Real Estate	0-15%	5%
Commodities	0-10%	2%
Cash	0-10%	1%

As of September 30, 2022, the Section 115 Pension Trust had a balance of \$16.4 million, a decrease of \$0.8 million from the prior month due to investment losses. The Section 115 OPEB Trust had a balance of \$29.8 million, a decrease of \$1.5 million from the prior month due to investment losses. The quarterly investment returns were -4.9% for both the Pension Trust and OPEB Trust.

Analysis

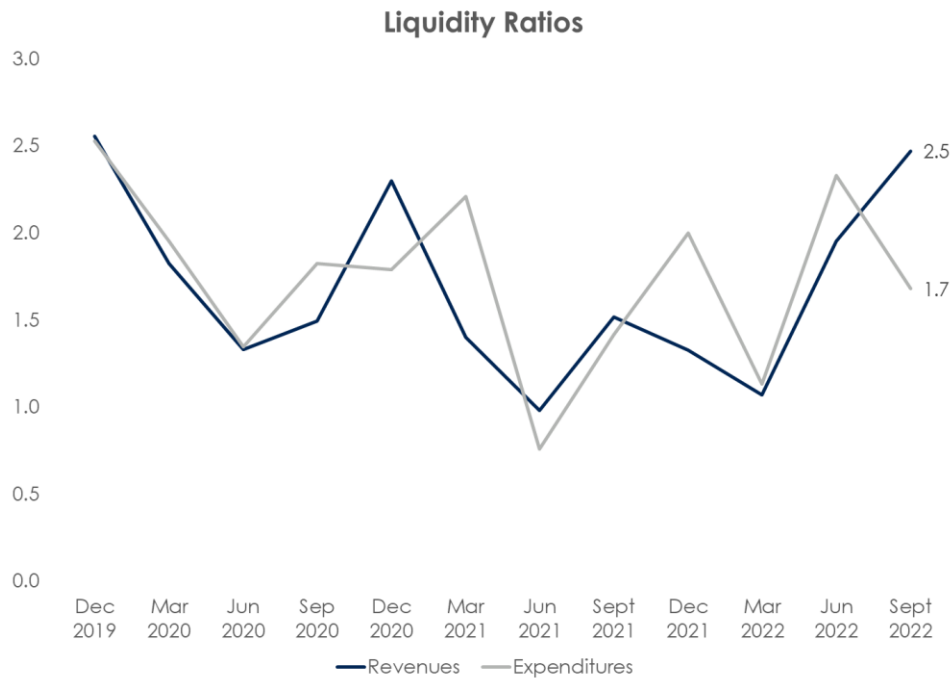
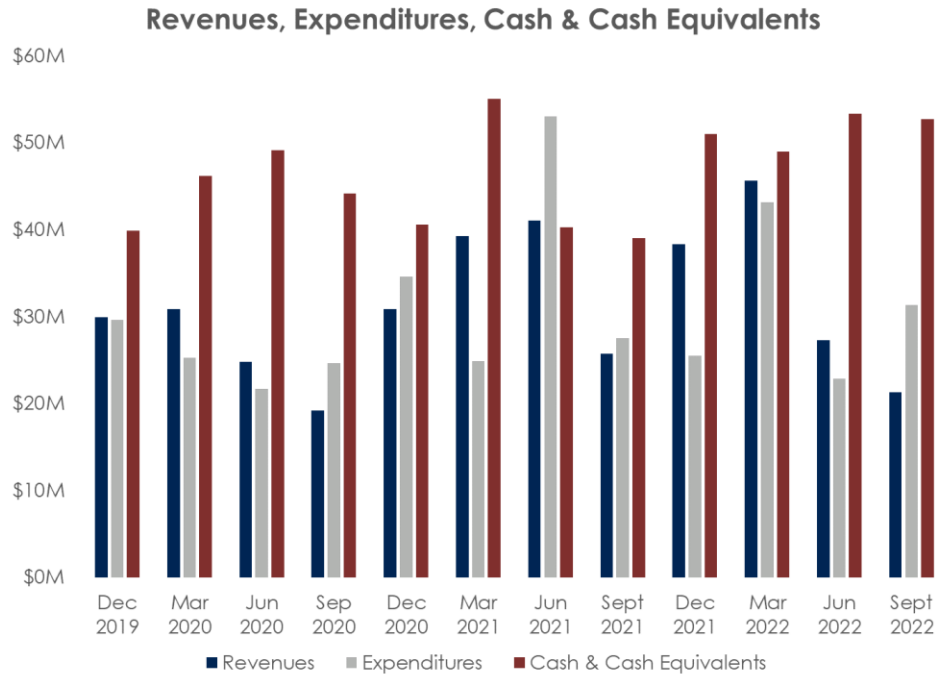
The City compares its portfolio to LAIF and one-year and two-year Treasury yields. Yield comparisons for the one-year Treasury, two-year Treasury, LAIF, and City average are presented below:



In September, yields rose significantly across the curve. The yield curve remained inverted and the spread between the two-year and 10-year Treasury yield became more inverted. As of September 30, 2022, the one-year and two-year Treasury yields were 4.05% and 4.22%, respectively. The one-year Treasury yield increased by 125 basis points, and the two-year Treasury yield increased by 130 basis points from June 30, 2022. The yield of the City's investment portfolio was 4.49%, higher than LAIF and one-year and two-year Treasury yields.

Cash Flow History

Historical revenues, expenditures, and liquidity ratios are presented below:



As the City's portfolio becomes more or less liquid over time, the ratio of cash and cash equivalents to revenues and expenditures will increase or decrease, respectively. The portfolio's investment structure is complete, so the City anticipates the ratio of cash and cash equivalents to revenues and expenditures to continue to flatten out moving forward. While a formal liquidity level has not been established, significant and consistent fluctuations in the ratio may indicate that additional funds should be invested or,

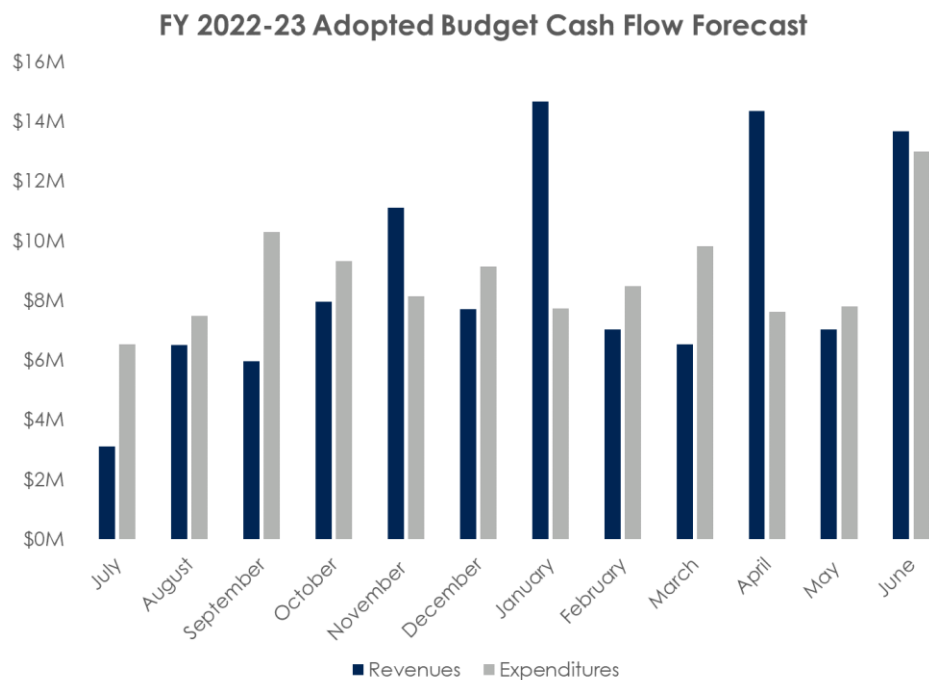
conversely, that investments should be liquidated. In recent years, sufficient liquidity levels for operating revenues and expenditures have approximated a ratio of 1.0. In March 2022, the City transferred \$15.0 million from the operating account to the investment portfolio, which reduced the March 2022 liquidity ratios.

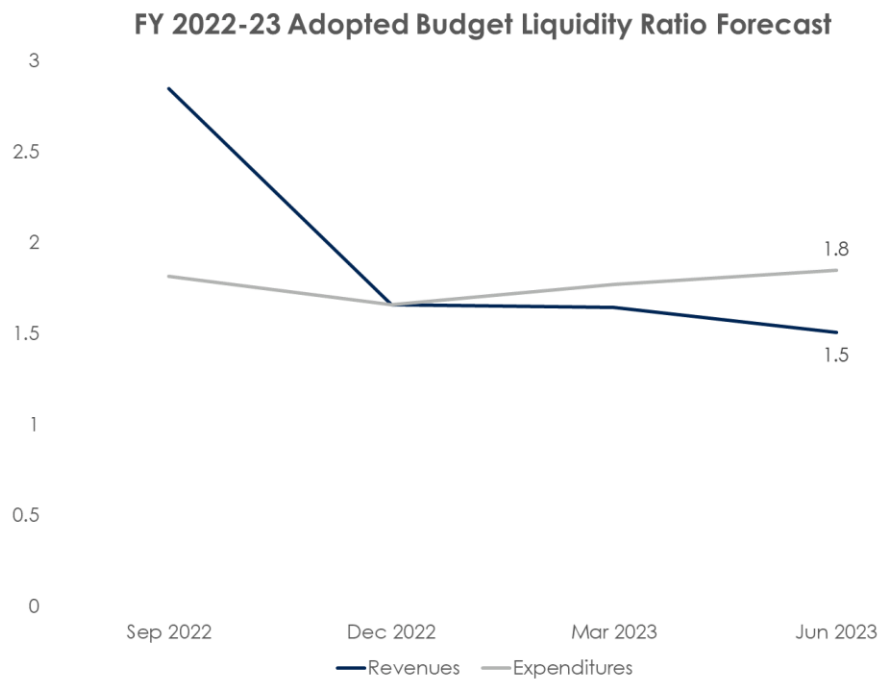
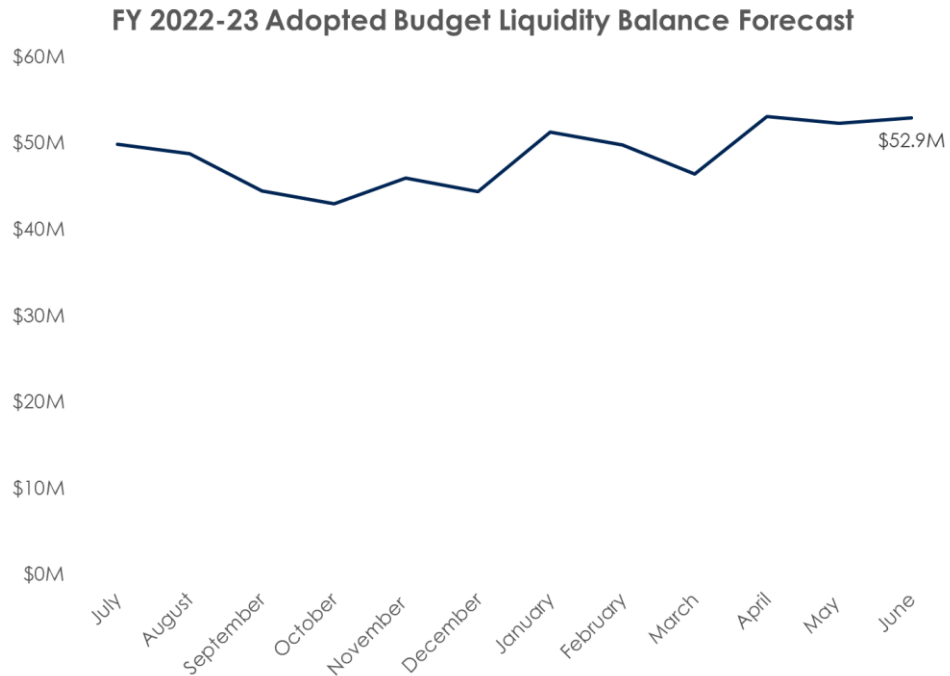
As of September 30, 2022, the liquidity ratio was 2.5 and 1.7 for revenues and expenditures, respectively. The City will monitor inflows and outflows during the second quarter of FY 2022-23 and bring recommendations for the City's investment portfolio as necessary and applicable.

As of September 30, 2022, the City had \$52.7 million in cash and cash equivalents in the bank and on hand. Based on the cash flow forecast, the City maintains the ability to meet its expenditure requirements for the next six months.

Cash Flow Forecast

Applying three-year historical trend data for each of the City's revenue and expenditure line items to the FY 2022-23 Adopted Budget, the City estimated the following cash flow forecast for FY 2022-23:





The purpose of this cash flow and liquidity forecast is to illustrate the timing of the City's revenues and expenditures throughout a fiscal year using historical trend data. The first quarter of the fiscal year experiences expenditures exceeding revenues since the City begins receiving its property tax distributions in November and April of the respective fiscal year. In January and April, the City receives additional property tax revenues due to the Vehicle License Fee (VLF) swap. In June, the City tends to experience higher

activities, particularly expenditures, due to the year-end close and accrual process. From one fiscal year to the next, the City typically incurs one-time special project or capital expenditure costs. The timing of these costs is more difficult to pinpoint to a particular month.

From a cash flow analysis perspective, the Adopted and Amended Budgets are efficient planning tools for determining cash flow needs for a single fiscal year. If a budget is adopted at a position in which revenues and expenditures are balanced, then it is reasonable to conclude cash flow is unlikely to be of concern. Beyond one fiscal year, a City prepares a twenty-year forward-looking forecast using historical and prospective assumptions. This forecast model is incorporated and presented to the City Council as part of the City's Adopted Budget.

Compliance

All of the City's investments comply with state law and the City's Investment Policy. In compliance with California Government Code 53646 (b)(3), the City maintains the ability to meet its expenditure requirements for the next six months.

Sustainability Impact

No sustainability impact.

Fiscal Impact

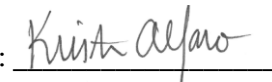
No fiscal impact.

Prepared by:



Thomas Leung
Budget Manager

Reviewed by:



Kristina Alfaro
Director of Administrative Services and City Treasurer

Approved for Submission by:



Pamela Wu
City Manager

Attachments:

- A – Chandler Investment Report September 2022
- B – Chandler Custodial Statement September 2022
- C – PARS Pension and OPEB Account Statement September 2022
- D – Pension and OPEB Performance Report for Quarter Ending September 30, 2022
- E – LAIF Account Statement September 2022