TO:        HONORABLE CITY COUNCIL

FROM:      CITY MANAGER   DEPARTMENT: ADMINISTRATIVE SERVICES

DATE:      JULY 22, 2002   CMR: 345:02

SUBJECT:   CITY OF PALO ALTO’S INVESTMENT ACTIVITY REPORT
FOR THE FOURTH QUARTER, FISCAL YEAR 2001-02

This is an information report and no Council action is required.

BACKGROUND

The purpose of this report is to inform Council of the status of the City’s investment portfolio
as of the end of the fourth quarter of Fiscal Year 2001-02. The City’s investment policy
requires that staff report to Council on the City’s portfolio composition compared to Council-
adopted policy; portfolio performance; and other key investment and cash flow information.

DISCUSSION

Investment Portfolio as of June 30, 2002
The City’s investment portfolio is detailed in Attachment B. It is grouped by investment type
and includes the investment issuer, date of maturity, current market value, the book and face
(par) value, and the weighted average maturity of each type of investment and of the entire
portfolio as of Error! Not a valid link..

The face value of the City’s portfolio is $339.7 million; in comparison, last quarter it was
$330.1 and last year it was $326.1 million. Growth in the portfolio of $9.6 million quarterly
results from reimbursement of past expenditures from Utility bond proceeds and from Utility
revenues.

The portfolio consists of $24.4 million in liquid accounts and $315.3 million in U. S.
government agency securities. The $315.3 million includes $128.1 million in investments
maturing in less than two years, comprising 40.6 percent of the City’s investment in notes
and securities. The current market value of the portfolio is 103.6 percent of the book value.
Because the City’s practice is to hold securities until they mature, changes in market price do
not affect the City’s investment principal. The market valuation is provided by Union Bank
of California, which is the City’s safekeeping agent. The average life to maturity of the investment portfolio is 2.27 years.

Investments Made During the Fourth Quarter
During the fourth quarter, $23.0 million of government agency securities with an average yield of 6.4 percent matured. During the same period, government securities totaling $31.5 million with an average yield of 4.3 percent were purchased. The City’s short-term money market and pool account increased by $3.6 million compared to the third quarter of 2001-02.

Availability of Funds for the Next Six Months
The normal flow of revenues from the City’s utility billings and general fund sources is sufficient to provide funds for ongoing expenditures. Projections indicate receipts will be $155.3 million and expenditures will be $154.4 million over the next six months, indicating an overall growth of the portfolio of about $0.9 million.

As of June 30, 2002, the City had $24.4 million deposited in the Local Agency Investment Fund (LAIF) and a money market account that could be withdrawn on a daily basis. In addition, securities totaling $43.8 million will mature between July 1, 2002 and December 31, 2002. On the basis of the above projections, staff is confident that the City will have more than sufficient funds to meet expenditure requirements for the next six months.

Compliance with City Investment Policy
During the fourth quarter of 2001-02, staff complied with all aspects of the investment policy. Attachment C lists the restrictions in the City’s investment policy, compared with the portfolio’s actual compliance.

Investment Yields
Interest income on an accrual basis for the fourth quarter of 2001-02 was $4.7 million while the total for the fiscal year was $18.8 million. This is 5.6 percent more than the 2001-02 adjusted budget of $17.8 million. The increase in the size of the portfolio contributed to the higher than expected earnings. As of June 30, 2002, the yield to maturity of the City’s portfolio was 5.39 percent. This compares to a yield of 5.63 percent in the third quarter of 2001-02 and 5.92 percent in June 30, 2001. The City’s portfolio yield is expected to decrease in the first quarter of 2002-03 as a result of reinvestment of maturing securities at lower interest rates. The City’s portfolio yield compares to LAIF’s average yield for the quarter of 2.8 percent and an average yield on the two-year and five-year Treasury bond during the fourth quarter of approximately 3.20 percent and 4.39 percent respectively.

Yield Trends
The Federal Open Market Committee (FOMC) did not change rates in the last two quarters. The federal funds and discount rates remain at 1.75 and 1.25 percent, respectively. The financial community does not expect the FOMC to raise or reduce rates in the near future.
The FOMC views the economy as continuing to recover but at a slower pace than originally expected. The weakness in the stock market, international tensions, and continuing accounting and corporate improprieties have contributed significantly to a weak economy. Staff expects interest rates to remain low, resulting in lower yields on the City’s portfolio in 2002-03.

Funds Held by the City or Managed Under Contract
Attachment A is a consolidated report of all City investment funds, including those not held directly in the investment portfolio. These include cash in the City’s regular bank account with Bank of America. The bond proceeds, bond reserves, and debt service payments being held by the City’s fiscal agents are subject to the requirements of the underlying debt indenture. The trustees for the bond funds are U.S. Bank and California Asset Management Program (CAMP). U.S. Bank investments are in money market mutual funds that exclusively invest in U.S. Treasury securities. CAMP investments, which are also in money market mutual fund, invest in banker’s acceptance, certificate of deposit, commercial paper, federal agency securities, and repurchase agreements. The most recent data on funds held by the fiscal agent is as of June 30, 2002.

ATTACHMENTS:
A) Consolidated Report of Cash and Investments
B) Investment Portfolio, as of June 30, 2002
C) Investment Policy Compliance
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