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MANAGER'S OFFICE
RECEIVED
FEB 10 1989

OFFICE OF THE
CITY TREASURER

CITY OF SACRAMENTO
CALIFORNIA

800 TENTH STREET
SUITE ONE
SACRAMENTO, CA
95814-2688

THOMAS P. FRIERY
TREASURER

February 10, 1989

916-449-5318
OPERATIONS

DONALD E. SPERLING
ASSISTANT TREASURER

APPROVED
BY THE CITY COUNCIL

916-449-5168
INVESTMENTS &
ADMINISTRATION

City Council
Sacramento, California

FEB 28 1989

OFFICE OF THE
CITY CLERK

916-448-3139
DEX TRANSCIEVER

Honorable Members in Session:

SUBJECT: Resolution Authorizing the City Treasurer to Implement the
Exclusion Stipulated in Assembly Bill 4089 (AB4089)
Allowing the Purchase of Securities Longer than 5 Years.

SUMMARY

This report recommends that the Council adopt the attached Resolution authorizing the City Treasurer to implement the 5-year maturity exclusion imposed by AB4089 as he deems necessary to maximize investment income consistent with safe and prudent investment practices per the Investment Authority Resolution previously adopted by the Sacramento City Council. In addition, as the bill stipulates that this authorization will have to be reaffirmed quarterly, it is recommended that a copy be included within each pooled investment report.

BACKGROUND

Assembly Bill 4089 was created by Assemblyman Johnston in an attempt to prevent investment losses of the type and magnitude suffered recently by San Jose and Camarillo. The bill (AB4089) purports to do this by restricting the maturity of any security purchased subsequent to its passage on January 1, 1989, to 5 years - barring the expressed quarterly consent of the appropriate legislative body.

City Council
February 10, 1989

When the City Treasurer's office was made aware of this pending legislation last May, an in depth analysis of what we felt were the repercussions of this type of restriction was prepared and forwarded to Ken Emmanuals, our Legislative Analyst.

Other professional organizations and investment managers similarly found the bill unrealistic in terms of its ability to eliminate investment losses. Eventually their opposition was withdrawn as a result of the inclusion of language permitting local governing bodies the authority to be exempted from the restriction. Our office, however, still opposed the passage of AB4089 as misleading and presented such to the Law and Legislation Committee on May 26, 1988. (See Attachment A)

Although it is true that investments within the 5-year area tend to react with less volatility than those further out, it cannot be assumed that this action would eliminate the potential for losses entirely. Therefore, there is a false sense of security that investment losses would become a thing of the past. Basically, we do not believe it is possible to legislate against ignorance or a decision of an individual to act imprudently. Further, we believe restricting authority to less than five years will adversely impact our earnings rates. The committee heard our position and, in turn, supported our opposition.

FINANCIAL DATA

The financial implications of the passage of AB4089 are difficult to ascertain. Namely, this would entail the estimation of the potential income lost due to the inability to purchase securities with maturities longer than 5 years. This restriction would most likely have a negative impact on the City of Sacramento as we have made a practice of varying the average life of Pool A significantly over the last 8 - 10 years. (See table below.)

The concept of the average life of a portfolio is an important one in that it measures how long all the dollars in a portfolio are invested at that particular time. Furthermore, it is a weighted average which means that it is a combination of all the investments that comprise the portfolio - those that are as short as overnight Repurchase Agreements and those that are as long as 30-year Treasury Bonds. This strategy of lengthening and shortening the maturities with the changing business cycles has proven not only to be safe, but successful in terms of effective portfolio management.

This is evidenced by the exceptional performance results we've experienced over other short term portfolios. In fact, as a result of this ability to choose the maturities within our portfolio, the funds we manage for the City have earned in excess of \$54 million more over the last five years than the shorter term fund managers. (See Attachment B)

City Council
February 10, 1989

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POOL A COMPARISON
Data by Fiscal Year)

| | <u>80-81</u> | <u>81-82</u> | <u>82-83</u> | <u>83-84</u> | <u>84-85</u> | <u>85-86</u> | <u>86-87</u> | <u>87-88</u> |
|------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|
| Life (Yrs) | 8.02 | 8.95 | 7.84 | 8.75 | 3.05 | 1.41 | 2.41 | 3.12 |
| Yield (%) | 14.36 | 14.24 | 14.37 | 12.24 | 11.40 | 10.01 | 8.41 | 8.14 |
| LAIF | 10.80 | 12.05 | 10.53 | 10.35 | 10.80 | 9.13 | 7.44 | 7.80 |
| Fed Funds | 15.00 | 14.98 | 9.46 | 9.70 | 9.26 | 7.69 | 6.42 | 6.87 |
| MLPFS | 13.18 | 14.51 | 9.50 | 9.09 | 9.41 | 7.22 | 5.68 | 6.43 |
| UST Bills | 12.69 | 13.09 | 8.59 | 9.23 | 8.70 | 6.97 | 5.60 | 5.96 |

POLICY CONSIDERATIONS

There are no deviations from the current policy of maximizing investment income consistent with safe and prudent investment practices as a result of this item.

MBE/WBE EFFORTS

No impact.

RECOMMENDATION

Based on our analysis of the implications of the passage of AB4089, it is recommended that City Council adopt the attached Resolution, thus enabling the City Treasurer to purchase securities with maturities of longer than 5 years based on market conditions and the principles of prudent investment management.

City Council
February 10, 1989

Furthermore, as it will be necessary to review this authorization quarterly, a copy of the resolution will be included with each Pooled Investment Quarterly Report presented to Council.

Respectfully submitted,



Thomas P. Friery
City Treasurer

Recommendation Approved:

Date to Council: 2/28/89
Districts: All



WALTER J. SLIPH
City Manager

CONTACT PERSON

Michelle Stenoski, Investment Officer II
449-5168

Attachments A & B

RESOLUTION NO. 89-167

ADOPTED BY THE SACRAMENTO CITY COUNCIL ON DATE OF

A RESOLUTION AMENDING RESOLUTION NO. 446, ADOPTED
DECEMBER 17, 1964, RELATING TO THE AUTHORIZATION OF
THE INVESTMENT OF SURPLUS MONEY IN THE TREASURY OF
THE CITY OF SACRAMENTO

WHEREAS, Government Code Section 53601 provides that investment of municipal funds cannot be made in certain securities having a term remaining to maturity in excess of five years unless the legislative body has approved such investments as part of an investment program, no less than three months prior to the investment; and

WHEREAS, the City Treasurer has recommended that the City Council amend Resolution 446, relating to investment of surplus funds by the City Treasurer, to provide that the Treasurer's authority extend to investments having a term remaining to maturity in excess of five years;

NOW THEREFORE BE IT RESOLVED BY THE COUNCIL OF THE CITY OF SACRAMENTO:

1. Resolution No. 446 is hereby amended to read as follows under item 1: "The City Treasurer is hereby authorized and instructed to invest such portion of any such surplus in such a manner as he deems wise and prudent as long as such investments are legal for cities as set forth in the Government Code of the State of California. This includes those investments with maturities in excess of five years."

Mayor

ATTEST:

City Clerk

APPROVED
BY THE CITY COUNCIL

FEB 28 1989

OFFICE OF THE
CITY CLERK



OFFICE OF THE
CITY TREASURER

THOMAS P. FRIERY
TREASURER

DONALD E. SPERLING
ASSISTANT TREASURER

CITY OF SACRAMENTO
CALIFORNIA

May 18, 1988

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Mr. Kenneth Emmanuel
Kenneth Emmanuel and Associates
1127 Eleventh Street
Suite 512
Sacramento, California 95814

Re: Legislative Analysis of AB 4089

Dear Ken:

The legislation known as Assembly Bill 4089 (AB 4089), currently before review, places unnecessary restrictions on local agencies with respect to the term remaining to maturity. The proposed revision to Sections 53601 and 53635 of the Government Code would limit the maturity of securities purchased subsequent to its passage to 5 years without specific authority granted by the respective legislative body (City Council, for example). Exceptions to this rule would be securities underlying a repurchase or reverse repurchase agreement.

It is generally believed by its supporters that this legislation would prevent investment losses as experienced recently by Camarillo and San Jose. While it is true that investments within the 5-year area tend to react with less volatility than those further out, it cannot be assumed that this action would eliminate the potential for losses entirely. Therefore, there is a false sense of security that this would reduce investment losses.

In addition, although there does remain the opportunity to approach the local legislative body for specific authority, this places an unusual burden on that particular body as to whether or not it should openly oppose what the rest of the State can legally invest in.

Mr. Kenneth Emmanuel
May 18, 1988
Page 2

Finally, it is felt that this restriction would simply tie the hands of larger local governments with portfolios in excess of \$100 million. Specifically, the City of Sacramento has varied the average life of its portfolio significantly over the last 8 - 10 years. (See table below.) This strategy of lengthening and shortening the maturities with the changing business cycles has proven not only to be safe but successful in terms of effective portfolio management.

| | <u>1980-81</u> | <u>1981-82</u> | <u>1982-83</u> | <u>1983-84</u> | <u>1984-85</u> | <u>1985-86</u> | <u>1986-87</u> |
|------------|----------------|----------------|----------------|----------------|----------------|----------------|----------------|
| Life (yrs) | 8.02 | 8.95 | 7.84 | 8.75 | 3.05 | 1.41 | 2.41? |
| Yield (%) | 14.36 | 14.24 | 14.37 | 12.24 | 11.40 | 10.01 | 8.41 |
| LAIF | 10.80 | 12.05 | 10.53 | 10.35 | 10.80 | 9.13 | 7.44 |
| Fed Funds | 15.00 | 14.98 | 9.46 | 9.70 | 9.26 | 7.69 | 6.42 |
| MLPFS | 13.18 | 14.51 | 9.50 | 9.09 | 9.41 | 7.22 | 5.68 |
| USTBills | 12.69 | 13.09 | 8.59 | 9.23 | 8.70 | 6.97 | 5.60 |

In summary, the City of Sacramento fully understands the intention of this legislation to prevent in the future the unfortunate loss of public fund monies experienced recently. It is not felt, however, that this measure would answer as many problems as it appears to present. First of all, it will not impact either the State or Pension Fund managers thereby creating a conflict--should local governments, prohibited to buy securities longer than 5 years themselves, be allowed to invest in a portfolio which itself does not follow that same strategy? (LAIF, for example.) Also, how would this impact the future debt financing of many cities--should we issue debt for a term which we ourselves would not buy?

We all regret losses of the magnitude experienced recently. However, before the types of restrictions as stipulated in AB 4089 are to be placed on the investment portfolios of local agencies, perhaps the Legislature's explicit and rigorous reporting requirements that have already been passed should be put to better use. This should be accomplished by directing the local legislative bodies to devote adequate time to hearing the investment reports--even to the extent of scheduling special meetings. Also, it could be considered that these local governing bodies should make annual determinations as to whether in-house staff should manage the money or whether they prefer investment with the LAIF.

Mr. Kenneth Emmanuel
May 18, 1988
Page 3

In closing, we do not believe it is possible to legislate against ignorance or a decision of an individual to act imprudently. It would be unwise to punish the overwhelming majority for the actions of 3 or 4 individuals over the last 10 years. We do not believe any legislative changes should be made at this time.

Sincerely,



Thomas P. Frierly
City Treasurer

cc: James P. Jackson, City Attorney
Betty Masuoka, Director of Finance
Jack Crist, Deputy City Manager

IMPACT OF A 1% DECLINE ON VARIOUS COUPONS WITH VARIOUS MATURITY DATES
 CITY OF SACRAMENTO
 a: IMPACT

| @ PAR - \$100 | 1 YEAR | 2 YEAR | 3 YEAR | 5 YEAR | 7 YEAR | 10 YEAR | 20 YEAR | 30 YEAR |
|--------------------|----------|----------|----------|----------|----------|----------|-----------|-----------|
| ***** | | | | | | | | |
| 10% SECURITY @ PAR | \$100.00 | \$100.00 | \$100.00 | \$100.00 | \$100.00 | \$100.00 | \$100.00 | \$100.00 |
| 10% SECURITY @ 11% | \$99.08 | \$98.25 | \$97.50 | \$96.23 | \$95.21 | \$94.02 | \$91.98 | \$91.28 |
| PRINC. LOSS | (\$0.92) | (\$1.75) | (\$2.50) | (\$3.77) | (\$4.79) | (\$5.98) | (\$8.02) | (\$8.72) |
| ----- | | | | | | | | |
| 9% SECURITY @ PAR | \$100.00 | \$100.00 | \$100.00 | \$100.00 | \$100.00 | \$100.00 | \$100.00 | \$100.00 |
| 9% SECURITY @ 10% | \$99.07 | \$98.23 | \$97.46 | \$96.14 | \$95.05 | \$93.77 | \$91.42 | \$90.54 |
| PRINC. LOSS | (\$0.93) | (\$1.77) | (\$2.54) | (\$3.86) | (\$4.95) | (\$6.23) | (\$8.58) | (\$9.46) |
| ----- | | | | | | | | |
| 8% SECURITY @ PAR | \$100.00 | \$100.00 | \$100.00 | \$100.00 | \$100.00 | \$100.00 | \$100.00 | \$100.00 |
| 8% SECURITY @ 9% | \$99.06 | \$98.21 | \$97.42 | \$96.04 | \$94.89 | \$93.50 | \$90.80 | \$89.68 |
| PRINC. LOSS | (\$0.94) | (\$1.79) | (\$2.58) | (\$3.96) | (\$5.11) | (\$6.50) | (\$9.20) | (\$10.32) |
| ----- | | | | | | | | |
| 7% SECURITY @ PAR | \$100.00 | \$100.00 | \$100.00 | \$100.00 | \$100.00 | \$100.00 | \$100.00 | \$100.00 |
| 7% SECURITY @ 8% | \$99.06 | \$98.19 | \$97.38 | \$95.94 | \$94.72 | \$93.20 | \$90.10 | \$88.69 |
| PRINC. LOSS | (\$0.94) | (\$1.81) | (\$2.62) | (\$4.06) | (\$5.28) | (\$6.80) | (\$9.90) | (\$11.31) |
| ----- | | | | | | | | |
| 6% SECURITY @ PAR | \$100.00 | \$100.00 | \$100.00 | \$100.00 | \$100.00 | \$100.00 | \$100.00 | \$100.00 |
| 6% SECURITY @ 7% | \$99.05 | \$98.16 | \$97.34 | \$95.84 | \$94.54 | \$92.89 | \$89.32 | \$87.53 |
| PRINC. LOSS | (\$0.95) | (\$1.84) | (\$2.66) | (\$4.16) | (\$5.46) | (\$7.11) | (\$10.68) | (\$12.47) |
| ----- | | | | | | | | |
| 5% SECURITY @ PAR | \$100.00 | \$100.00 | \$100.00 | \$100.00 | \$100.00 | \$100.00 | \$100.00 | \$100.00 |
| 5% SECURITY @ 6% | \$99.04 | \$98.14 | \$97.29 | \$95.73 | \$94.35 | \$92.56 | \$88.44 | \$86.16 |
| PRINC. LOSS | (\$0.96) | (\$1.86) | (\$2.71) | (\$4.27) | (\$5.65) | (\$7.44) | (\$11.56) | (\$13.84) |

THE TABLE DEMONSTRATES THE IMPACT OF INTEREST RATES ON VARIOUS TERM SECURITIES. IT SHOULD BE CONSIDERED FURTHER THAT THIS IMPACT IS POSITIVE WHEN RATES DECLINE AND NEGATIVE WHEN RATES INCREASE. ALSO IT SHOWS THAT LOWER COUPON ON LONGER TERM SECURITIES PROVIDE HIGHER POTENTIAL GAINS/(LOSSES) THAN DO HIGHER COUPON SECURITIES. LONGER TERM SECURITIES CAN BE EFFECTIVE PORTFOLIO TOOLS SO LONG AS NO MORE THAN A PRUDENT PERCENTAGE OF SECURITIES ARE INVESTED IN THESE INSTRUMENTS.

CITY TREASURER

(in 000's)

| Benefit of Treasury Management Over LAIF | | | | | | Benefit of Treasury Management Over Merrill Lynch | | | | |
|--|-------|-------|-------|-------|--|---|-------|-------|-------|-------|
| 87/88 | 86/87 | 85/86 | 84/85 | 83/84 | | 87/88 | 86/87 | 85/86 | 84/85 | 83/84 |

| | | | | | | | | | | | |
|--------------------|------------|--------------|------------|------------|--------------|--------------------|--------------|--------------|--------------|--------------|--------------|
| Pool A | 404 | 1,080 | 846 | 487 | 1,426 | Pool A | 2,031 | 3,039 | 2,682 | 1,614 | 2,377 |
| Pool B | 203 | 338 | 212 | 130 | 288 | Pool B | 497 | 712 | 605 | 399 | 494 |
| Pool C | (6) | 28 | (23) | 30 | 108 | Pool C | 22 | 83 | 103 | 183 | 278 |
| Pool D | (73) | (26) | (195) | (15) | 44 | Pool D | 206 | 549 | 301 | 158 | 241 |
| Pool E | (55) | n/a | n/a | n/a | n/a | Pool E | 271 | n/a | n/a | n/a | n/a |
| Pool F | (149) | n/a | n/a | n/a | n/a | Pool F | 113 | n/a | n/a | n/a | n/a |
| Total Benef | 324 | 1,420 | 840 | 631 | 1,866 | Total Benef | 3,140 | 4,384 | 3,691 | 2,354 | 3,390 |

| Benefit of Treasury Management Over 90 Day T-Bill | | | | | | Benefit of Treasury Management Over Federal Funds | | | | |
|---|-------|-------|-------|-------|--|---|-------|-------|-------|-------|
| 87/88 | 86/87 | 85/86 | 84/85 | 83/84 | | 87/88 | 86/87 | 85/86 | 84/85 | 83/84 |

| | | | | | | | | | | | |
|--------------------|--------------|--------------|--------------|--------------|--------------|--------------------|--------------|--------------|--------------|--------------|--------------|
| Pool A | 2,589 | 3,128 | 2,932 | 2,190 | 2,272 | Pool A | 1,508 | 2,215 | 2,230 | 1,736 | 1,917 |
| Pool B | 598 | 729 | 659 | 536 | 471 | Pool B | 403 | 555 | 508 | 428 | 394 |
| Pool C | 32 | 85 | 120 | 261 | 259 | Pool C | 13 | 60 | 72 | 199 | 195 |
| Pool D | 301 | 575 | 368 | 247 | 219 | Pool D | 116 | 307 | 179 | 177 | 145 |
| Pool E | 383 | n/a | n/a | n/a | n/a | Pool E | 167 | n/a | n/a | n/a | n/a |
| Pool F | 203 | n/a | n/a | n/a | n/a | Pool F | 29 | n/a | n/a | n/a | n/a |
| Total Benef | 4,106 | 4,518 | 4,079 | 3,233 | 3,220 | Total Benef | 2,235 | 3,138 | 2,990 | 2,539 | 2,652 |

- Pool 38,705
- Pool 9,157
- Pool 2,099
- Pool 3,826
- Pool 766
- Pool 195

54,749
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24

OFFICE OF THE
CITY TREASURER

THOMAS P. FRIERY
TREASURER

DONALD E. SPERLING
ASSISTANT TREASURER

Budget and Finance Committee
Sacramento, California

Honorable Members in Session:

SUBJECT: Resolution Authorizing the City Treasurer to Exceed the
5-Year Maturity Restriction on Investments Purchased
Subsequent to the Passage of Assembly Bill 4089 (AB4089)

SUMMARY

The attached report recommends approval of an amendment to the previously adopted Investment Authority Resolution enabling the City Treasurer to exceed the 5 year maturity restriction imposed by AB4089.

BACKGROUND

Assembly Bill 4089 was created by Assemblyman Johnston in an attempt to prevent investment losses of the type and magnitude suffered recently by San Jose and Camarillo. The bill (AB4089) purports to do this by restricting the maturity of any security purchased subsequent to its passage on January 1, 1989, to 5 years - barring the expressed quarterly consent of the appropriate legislative body.

When the City Treasurer's office was made aware of this pending legislation last May, an in depth analysis of what we felt were the repercussions of this type of restriction was prepared and forwarded to Ken Emmanuals, our Legislative Analyst.

Other professional organizations and investment managers similarly found the bill unrealistic in terms of its ability to eliminate investment losses. Eventually, their proposition was withdrawn as a result of the inclusion of language permitting local governing bodies the authority to be exempted from the restriction. Our office, however, still opposed the passage of AB4089 as misleading and presented such to the Law and Legislation Committee on May 26, 1988. (See Attachment A of City Council Report copy.)

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Budget and Finance Committee
February 10, 1989

Although it is true that investments within the 5-year area tend to react with less volatility than those further out, it cannot be assumed that this action would eliminate the potential for losses entirely. Therefore, there is a false sense of security that investment losses would become a thing of the past. Basically, we do not believe it is possible to legislate against ignorance or a decision of an individual to act imprudently. Further, we believe restricting authority to less than five years will adversely impact our earnings rates. The committee heard our position and, in turn, supported our opposition.

FINANCIAL DATA

See City Council Report (copy attached).

POLICY CONSIDERATIONS

There are no deviations from the current policy of maximizing investment income consistent with safe and prudent investment practices as a result of this item.

MBE/WBE EFFORTS

No impact.

RECOMMENDATION

It is recommended that after hearing the attached report, the Budget and Finance Committee recommend adoption and forward the report to the full City Council.

Respectfully submitted


Thomas P. Friery
City Treasurer

Recommendation Approved:

To City Council: 2/28/89
Districts: All

Jack R. Crist
Deputy City Manager
Attachments