



Legislation Text

File #: AF16-012, **Version:** 1

Agenda Information Sheet

DEPARTMENT: Finance

ACM: Bryan Langley

Date: September 27, 2016

SUBJECT

Receive a report, hold a discussion, and give staff direction regarding revisions to the City of Denton's Investment Policy.

BACKGROUND

The City of Denton has a formal Investment Policy to guide decision making in managing and investing public funds. The City's Policy is modeled after, and in compliance with, the provisions of the Public Funds Investment Act (PFIA) of Texas, Government Code Chapter 2256. In accordance with the Code, and in order of importance, are the following prioritized objectives for managing the portfolio's fixed income investments: safety of principal, liquidity, and yield. Since it is the City's practice to hold securities until they mature, temporary market value gains and losses are unlikely to be realized. The general investment strategy, while taking into account the current interest rate environment, is to match maturities to cash flow needs.

The Audit/Finance Committee and the City Council are required by the PFIA to review and approve the Investment Policy at least annually. This year, the Investment Committee and the City's investment advisor (First Southwest Asset Management, LLC.) recommended three changes that are detailed below and highlighted on pages 11 and 12 of the City's red-lined version of the Investment Policy. They are as follows:

- 1) More clearly differentiate between local government investment pools that invest in government securities only and those that invest in prime (corporate) securities with appropriate portfolio allocations to each.
- 2) Increase the commercial paper (CP) portfolio exposure through direct purchases from 5% to 15% of the portfolio using the approved list of CP issuers provided by the City's investment advisor.
- 3) Limit the portfolio's individual issuer CP exposure to no more than 5%.

These changes are proposed in light of the increasing yield advantage of CP as SEC money market reforms are implemented next month and institutional investors move out of prime money market mutual funds due to the fluctuating net asset value (NAV) and the possible imposition of liquidity fees and redemption gates. This has forced CP issuers (mainly large banks and corporations covering short term financial needs) to offer more enticing yields without any corresponding change in the risk parameters of this investment. The City would like to take further advantage of this market pricing dislocation by increasing its exposure. The decline in CP purchases by prime money market mutual funds has created a vacuum. A current example illustrating the yield

differential dated 9-7-16 shows that purchasing a government agency discount note dated (maturing on) June 9, 2017 would yield 0.541% while Toyota Motor Credit CP dated June 5, 2017 yielded 1.196%. This yield differential of approximately 65 basis points on a \$10 million investment would produce about \$48,000 additional dollars investing in CP over the time period.

It should be noted that the City's CP purchases are restricted to an issuer's paper that is rated not less than A1/P1 by at least two rating agencies, which is the second highest possible rating; only A1+/P1 is better and the list of top issuers is further culled by our investment advisor. Also CP issuance cannot exceed a maximum maturity of 270 days.

The City's investment advisor and the Investment Committee have reviewed and approved the revised Investment Policy. If the Audit/Finance Committee concurs with the proposed changes, a resolution to approve the revisions will be presented to Council for consideration on November 1, 2016.

RECOMMENDATION

Staff recommends forwarding the revised Investment Policy to the City Council for review and approval.

STRATEGIC PLAN RELATIONSHIP

The City of Denton's Strategic Plan is an action-oriented road map that will help the City achieve its vision. The foundation for the plan is the five long-term Key Focus Areas (KFA): Organizational Excellence; Public Infrastructure; Economic Development; Safe, Livable, and Family-Friendly Community; and Sustainability and Environmental Stewardship. While individual items may support multiple KFAs, this specific City Council agenda item contributes most directly to the following KFA and goal:

Related Key Focus Area: Organizational Excellence
Related Goal: 1.1 Manage financial resources in a responsible manner

EXHIBITS

1. Redlined Investment Policy

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