

California Debt and Investment  
Advisory Commission

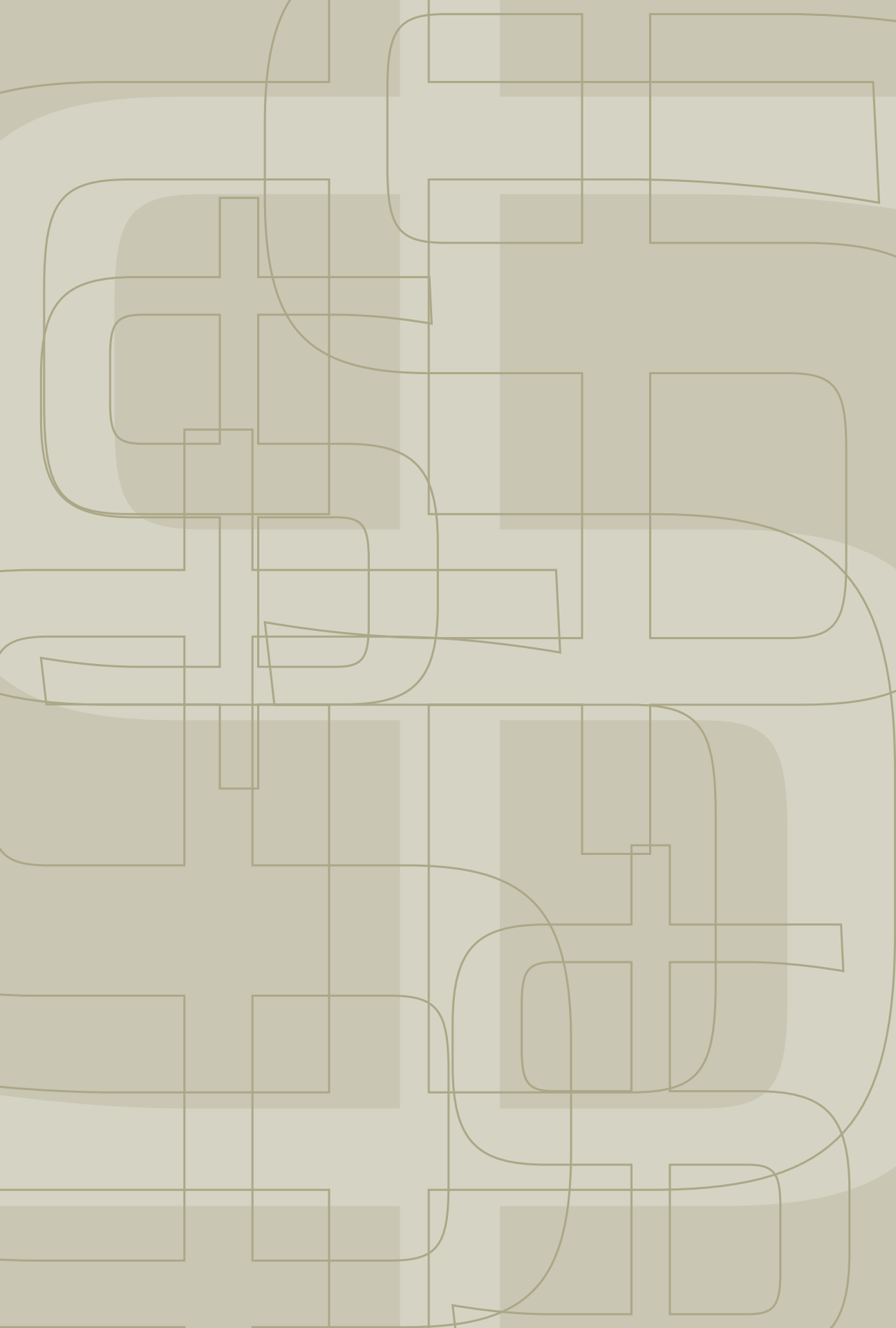
# Investment Portfolio Reporting Practices:

An Informational Guide



State Treasurer Phil Angelides, Chair

CDIAC 04-5



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Advisory Commission

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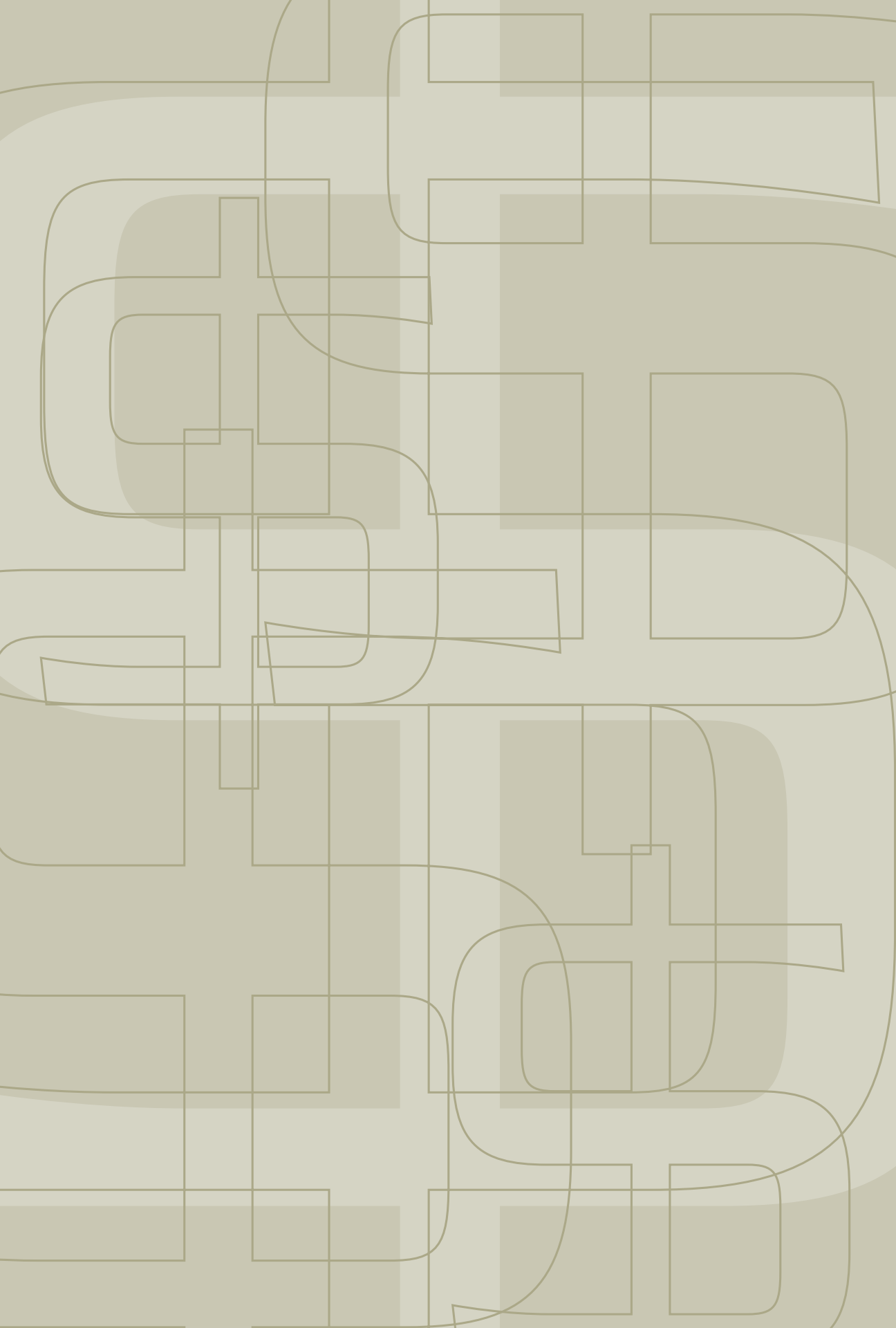
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## I. INTRODUCTION

Prior to the 2003-04 Budget Act [Chapter 157, Statutes of 2003 (AB 1765, Oropeza)], California Government Code Section 53646<sup>1</sup> required, with certain exceptions, California local governments to submit a quarterly investment report to the agency's legislative body, its chief executive officer, and its internal auditor. This section was modified by Chapter 687, Statutes of 2000 (AB 943, Dutra), requiring that cities and counties, with some exceptions, submit a copy of the same investment reports to the California Debt and Investment Advisory Commission (CDIAC) within sixty days of the close of the second and fourth quarter of each calendar year. These requirements generally are intended to provide the legislative body the ability to meet its fiduciary obligations as a trustee and to increase the exposure of the agency's investment activities to those outside the agency.

Since receiving the first quarterly investment reports submitted by local agencies under AB 943, CDIAC has improved its understanding of

the investment reporting activities of California cities and counties. In November 2003, CDIAC published an article summarizing its analysis of a sample of reports received for the quarter ending December 31, 2002. In that article, CDIAC reported that not all of the reports examined included the required information.<sup>2</sup> For example, only 54 percent of the counties and 46 percent of cities reported the source of valuation of the portfolio market value. Only three-quarters of the counties provided the required statement of compliance with investment policy or the statement of the agency's ability to meet expenditures for the next six months.

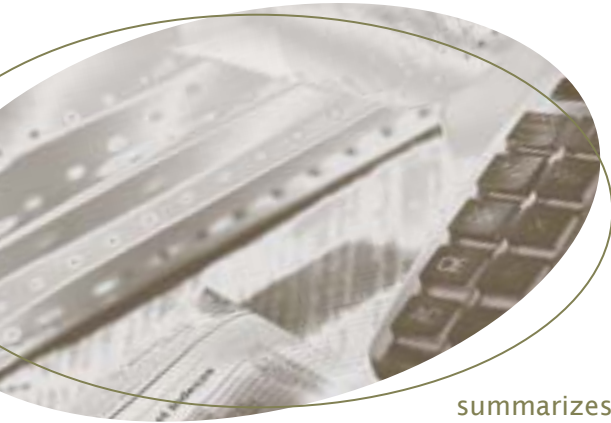
The 2003-04 and 2004-05 Budget Acts temporarily suspended the original reporting mandate (but not that covered by AB 943). While this requirement has been temporarily suspended, its intended purpose of providing fiduciaries information necessary to meeting their obligations, remains valid. The role of investment reports in safeguarding public funds combined

<sup>1</sup> Requirement established by Chapter 783, Statutes of 1995 (SB 564, Johnson).

<sup>2</sup> See *Review of Investment Portfolio Reporting Requirements and Recommendations*, **DEBT LINE** Offprint, November 2003.

with the results of CDIAC's review of local agency portfolio reports suggests additional information on best reporting practices may provide helpful information to investment officials and staff.

Using information gathered from portfolio reports filed, this report



summarizes the different goals, methods, and formats used by cities and counties in California to report investments. It provides a basis by which reporting agencies may evaluate their investment reports and identify alternative practices that effectively and efficiently communicate the agency's investment activities to fiduciaries and the public. This report does not establish additional requirements or set standards to which local agencies must conform beyond those set forth in California Government Code Section 53646. Rather, it provides examples and describes approaches

to reporting investments that have been successfully used by other local agencies to report their investments to their legislative body. Indirectly, it encourages local governments to be complete and deliberate in identifying the information that fiduciaries need to have to fulfill their duties as well as the presentation format most suited to delivering that information. Public agencies that adopt the methods and formats recommended herein will meet the reporting requirements set forth in California Government Code Section 53646. The goal of this report is to provide local agencies with examples of common reporting practices that may add to the readability of their reports and assist those with fiduciary responsibilities in assessing the costs and benefits of the agency's investment activities.

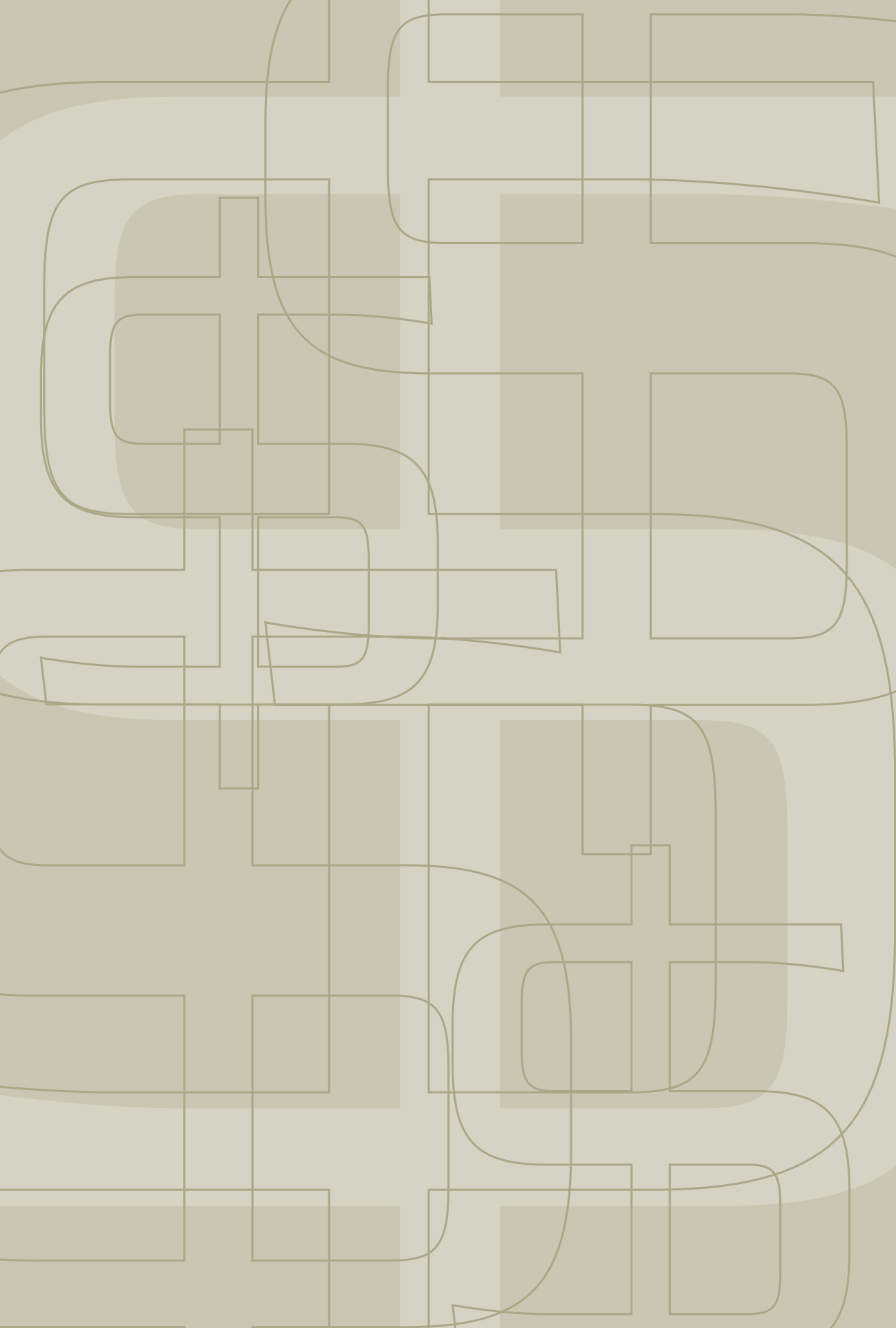
The report addresses the following questions:

- What is the purpose behind investment reporting?
- What information should cities and counties report to their legislative bodies?
- What good examples of presentation formats are used to summarize the agency's investment activities and to reveal current condition of those investments?



The report does not consider other reporting requirements than those established in Government Code Section 53646, including the monthly transactional reports submitted by county treasurers to their legislative body. Readers of this report are encouraged to consult CDIAC's *Understanding Public*

*Investment Reporting: A Handbook for Local Elected Officials* for a more comprehensive discussion of investment reporting. That publication also includes a review of state laws applying to public investments as well as a glossary of investment terms.

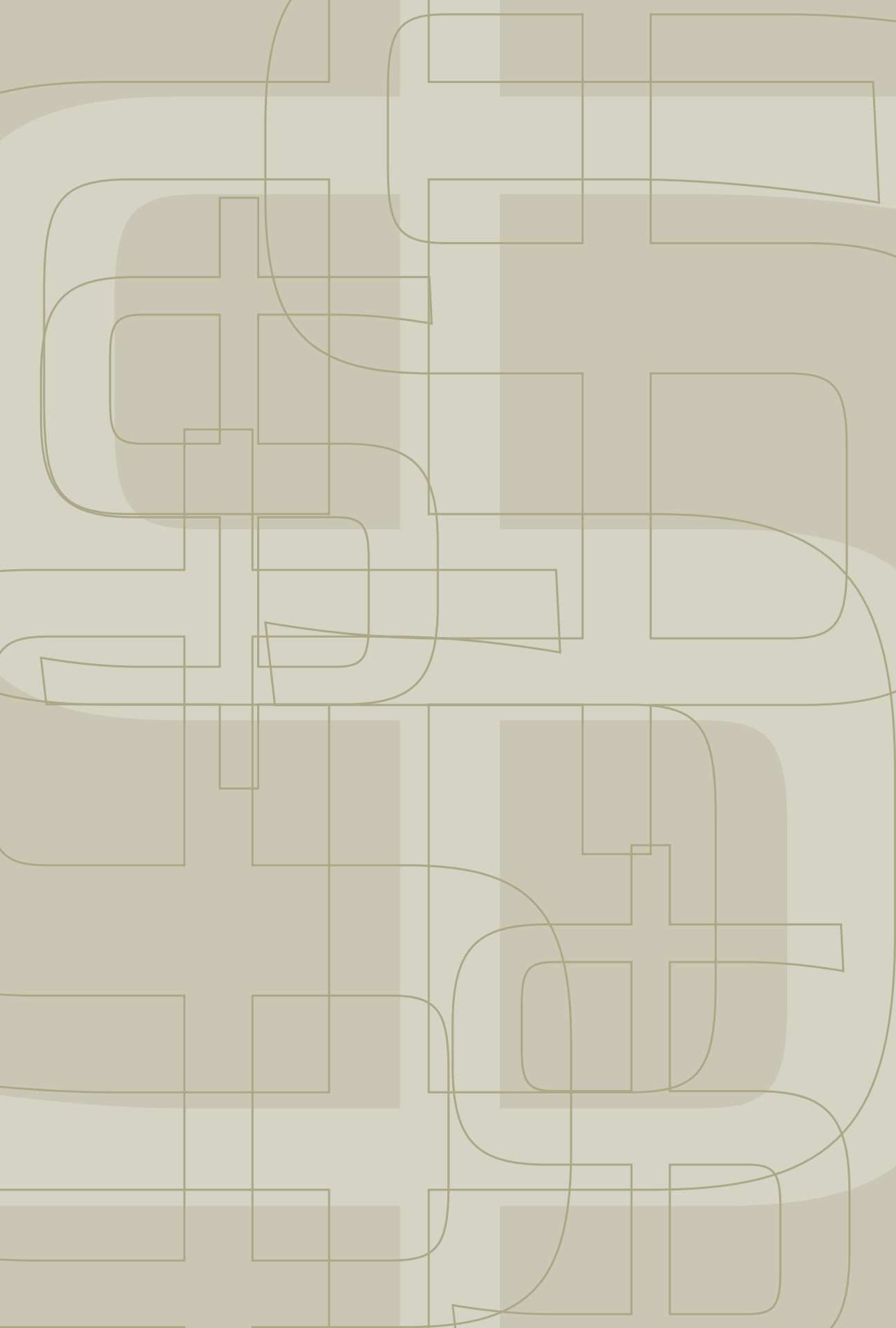


## II. INVESTMENT REPORTING REQUIREMENTS

**P**rior to the 2003-04 Budget Act, California Government Code Section 53646 required, with some exceptions, treasurers and chief fiscal officers of local agencies to submit a quarterly investment report to the chief executive officer, the internal auditor, and the legislative body of the local agency within 30 days following the end of the quarter covered by the report<sup>3</sup>. Section 53646 also provided that a legislative body of a local agency might elect to receive the report on a monthly basis. As a consequence of the State's fiscal condition, the 2003-04 and 2004-05 Budget Acts suspended these mandates for these fiscal years.

In addition to the reporting requirements set forth by Section 53646, a local agency treasurer who has been delegated authority to invest or reinvest funds of the local agency by the legislative body under Government Code Section 53607 has to submit a monthly report to the legislative body accounting for investments or reinvestments of funds and the sale or exchange of securities purchase during the prior reporting period. This report is separate and distinct from the quarterly report submitted under Section 53646.

<sup>3</sup> Government Code Section 53646 refers to both investment policies and quarterly reports. While the code provides no formal definition of either term, their meanings have been established by common practice. An "investment policy" is generally considered to be a statement of the local agency's objectives and methods of investing public funds. An investment policy may include a list of investment securities that the legislative body has approved for use by the local agency. It also may include performance measures or benchmarks that will be used to evaluate the return on investments, standards of care for the management of funds, and minimum credit quality requirements for investment securities. Government Code Section 27133 sets forth the contents of an investment policy prepared by a county treasurer for an investment oversight committee. A "quarterly report" is generally considered to be a statement of investments, fund balances, activity, and return on investments made by the local agency. Quarterly reports should reflect the current position and past performance of a portfolio of investments for the period of time under consideration.



### III. REQUIRED CONTENTS OF INVESTMENT REPORTS

**G**overnment Code Section 53646 mandates that the quarterly investment reports of a local agency contain certain items (see text box on page 12). These include the type of investment, the issuer's name, the date of maturity of the security, the par amount of the instrument, the market value, and the dollar amount invested in each security. The source of the market value also should be included in the report. The report must reference all funds that are under the management of investment providers, such as investment advisors, investment managers, and the investment advisory functions of banks and brokers and dealers. A local government's quarterly report also must state the portfolio's compliance with the agency's investment policy, or manner in which the portfolio is not in compliance, and include a statement regarding the local agency's ability to meet its cash flow needs for the next six months.

Quarterly investment reports may contain information in addition to that required by Section 53646. This information may be of particular

interest to the legislative body or to the reporting officer, such as a list of approved brokers and dealers or a cash flow statement. In place of a list of approved brokers and dealers, the quarterly report may include a listing of brokers and dealers actually used. Such a listing might be used to ensure that there is a competitive shopping process. A cash flow statement might entail a record of transfers to and from various cash accounts along with details on the uses and sources of each transfer. The report may go so far as to tie each disbursement to the appropriate trade confirmation received from a broker or dealer. While local agencies account for cash transfers as a part of their comprehensive financial reporting, paying special attention to these transfers in the context of a quarterly report increases accountability and supports the efforts of fiduciaries to meet their obligations.

Local agencies that invest in the Local Agency Investment Fund (LAIF), created by Government Code Section 16429.1, in National

Credit Union Share Insurance Fund-insured accounts in a credit union, in accounts insured or guaranteed pursuant to Financial Code Section 14858, in Federal Deposit Insurance Corporation-insured accounts in a bank or savings and loan association, in a county investment pool, or any combination of these may submit the most recent statements provided by these institutions in place of a separate investment report.

Furthermore, school district or county offices of education that hold less than \$25,000 in investments at the end of a quarter for which a report is to be submitted to the district's legislative body are not required to submit such a report. Local agencies included under these two exemptions shall be referred to as "exempt agencies."

#### **Investment Report Required Contents Pursuant to California Government Code Section 53646**

1. Type of investment
2. Issuer name
3. Date of maturity
4. Par amount
5. Dollar amount invested in all securities, investments, and moneys held by the local agency (CDIAC defines this as cost or book value of investments)
6. Description of any of the local agency's funds, investments, or programs under the management of contracted parties
7. Current market value of all funds held by the local agency and under the management of any outside party that is not also a local agency or the California Local Agency Investment Fund and the source of that value
8. Statement of compliance with local agency investment policy
9. Statement of the local agency's ability to meet its cash flow needs for the next six months

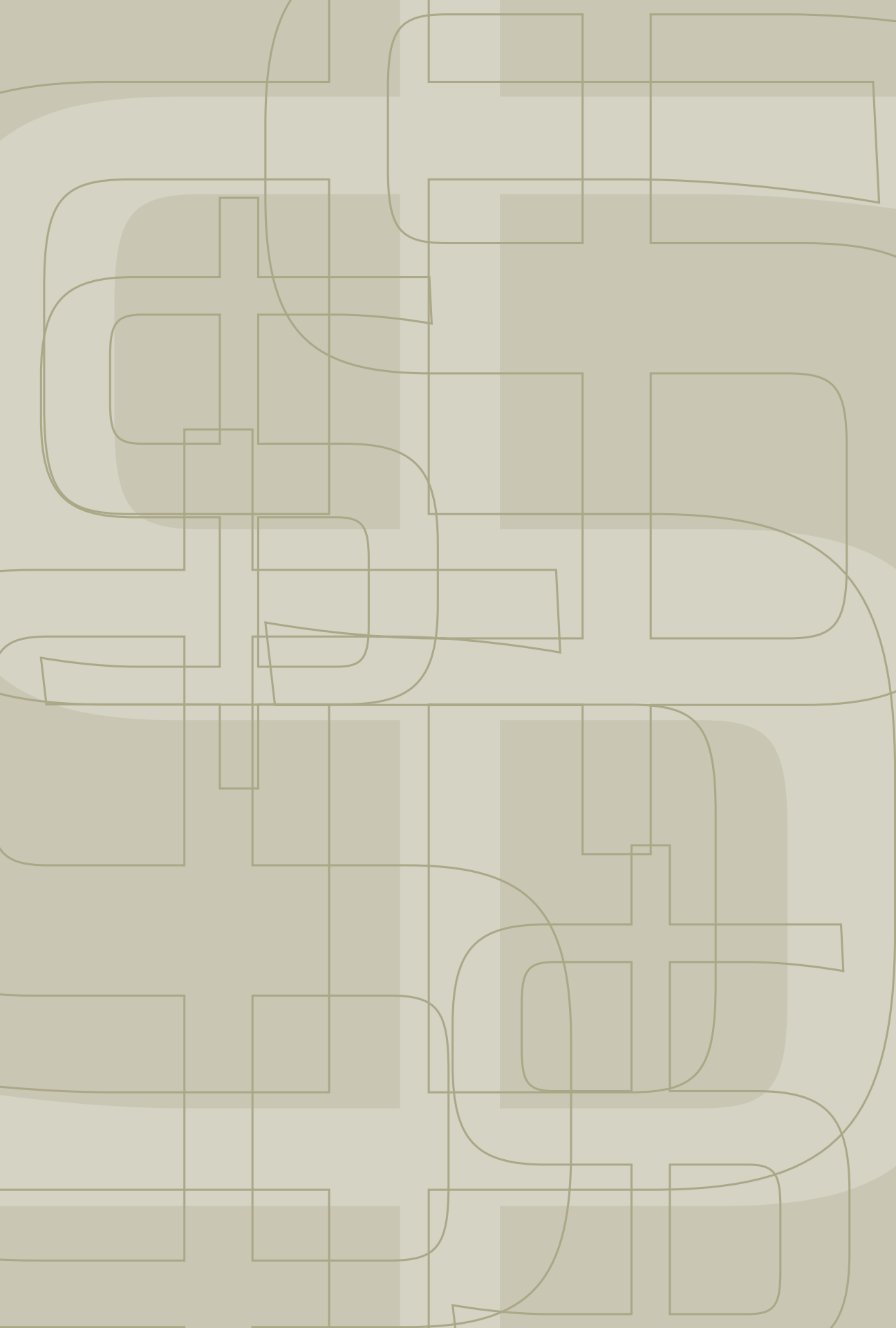
## IV. REVIEWING QUARTERLY REPORTS

Although state law does not specifically require the members of a legislative body to take action on the quarterly report submitted to them as fiduciaries, they should review and understand its contents. With certain exceptions<sup>4</sup>, the legislative body of a local agency cannot delegate its fiduciary responsibility although it may delegate the day-to-day authority to make investment decisions.

When evaluating information provided by the report that is beyond that required by Section 53646, the legislative body should refer to the guidance provided by the agency's investment policy or other statements that reveal the rationale for providing the information. The legislative

body may use a reported list of approved brokers and dealers, for example, to determine whether the agency has used contracted services appropriately. The legislative body may track cash transfers reported in a quarterly investment report to verify the correct payments made to settle transactions. Finally, the legislative body may review investments made from funds other than those reported under Section 53646 (such as debt service, special revenue, capital project, and other fiduciary type agency funds) to conduct a comprehensive evaluation of the safety and liquidity needs of the local agency.

<sup>4</sup> Government Code Section 27000.3 allows county boards of supervisors to delegate fiduciary responsibility to the county treasurer for funds deposited in the county treasury. In this case, the county treasurer would serve as the agent and fiduciary and be subject to the prudent investor standard.



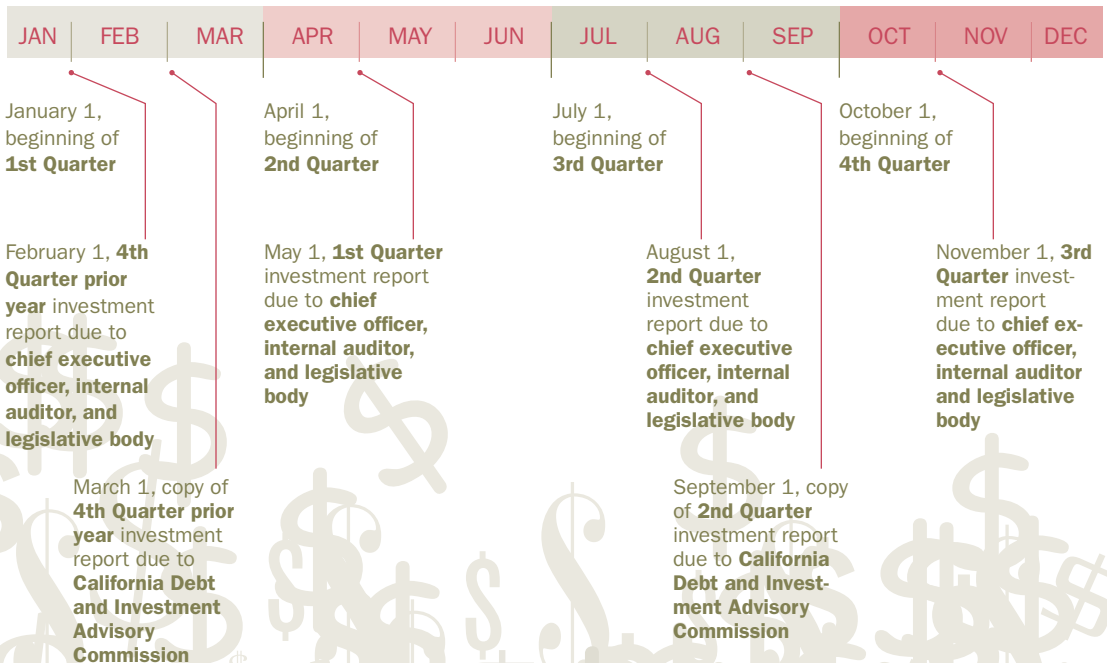


## V. REPORTING SCHEDULE

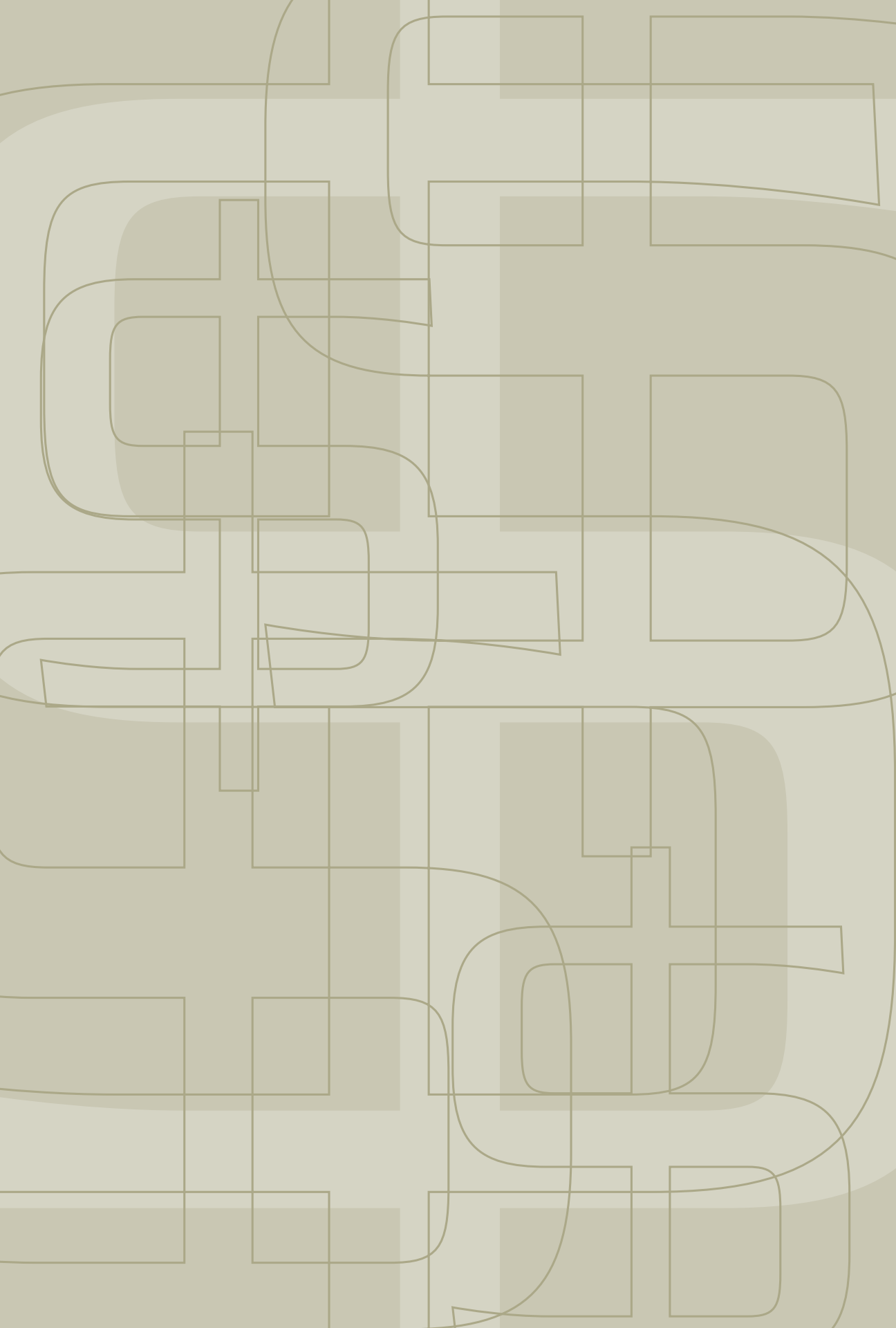
Figure 1 below provides a sample of the reporting schedule set forth by Section 53646. This schedule reflects the quarterly investment reporting requirements specified in Government Code Section 53646, even though the 2003-04 and 2004-05 Budget Acts suspended these requirements for these fiscal years. Cities and

counties, with some exceptions, are required to submit their second and fourth quarter calendar year reports to CDIAC within 60 days of the close of the quarter (approximately March 1st and September 1st) if they filed these reports with their chief executive officer, internal auditor, and legislative body.

**Figure 1**  
**Reporting Schedule <sup>5</sup>**



<sup>5</sup> Pursuant to California Government Code Section 53646(b).



## VI. PRESENTING MANDATED INFORMATION

Figure 2 shows a sample investment portfolio report for a local agency. The columns entitled Security Type, Issuer, Maturity Date, Par Value, Market Value, Book Value, Pricing Source, and Manager, and the two certifications at the bottom of the figure are mandatory. Local agencies that provide the information contained in these columns in any suitable format will meet the minimum reporting requirements set forth in Government Code Section 53646. The rest of the columns, namely those entitled CUSIP Number, Purchase Date, Earliest Call Date, Weighted Average Maturity, Coupon, Rating, Percent Portfolio Value, Unrealized Gain/Loss, Yield-to-Maturity, and Broker/Dealer are optional. The portfolio shown is provided purely as an example of how information for various types of allowable instruments could be displayed. It is not indicative of a typical portfolio distribution of investments.

As noted above, some local agencies are exempt from the full reporting

requirement specified in Government Code Section 53646(b)(1-4). In lieu of an investment report, they may submit the most recent account statements from LAIF, insured bank accounts, or county investment pools. Despite the exemptions provided by law, some exempt local agencies continue to report to their boards in the same format as non-exempt cities, providing information in a clear and concise manner to these decision-makers.

After the sample investment portfolio report, this document contains a glossary of terms used in the sample portfolio, then goes on to describe some additional recommended best practices that staff took note of in its review of actual county and city investment portfolio reports. This section describes the practices, discusses the use of the practices, then gives examples of how they could appear in the sample portfolio report or as they appeared in actual local agency portfolio reports.



## Figure 2 | Sample Investment Portfolio Report As of 3/31/03

Security Type	Issuer	CUSIP Number	Purchase Date	Maturity Date	Earliest Call Date	Weighted Average Maturity	Coupon	Rating
Local Agency Bonds	Sacramento MUD	999999AA9	23-Aug-02	15-Nov-04	none	595	6.75%	AAA
	Sacramento PFA	999998AA9	23-Feb-99	2-Sep-03	none	155	8.50%	AAA
<b>Local Agency Bond Totals</b>						338	7.77%	
U.S. Treasury Obligations	U.S. Treasury Note	999997AA9	12-Apr-01	31-Aug-04	none	519	2.25%	AAA
	U.S. Treasury Note	999997AB9	16-May-01	16-May-06	16-May-05	1142	3.50%	AAA
<b>Treasury Totals</b>						601	2.41%	
State of California Obligations	State of California RAWs	999996AA9	11-Jun-03	16-Jun-04	none	443	2.00%	BBB
	State of California GOs	999996AB9	20-Jun-02	20-Jun-05	20-Jun-03	812	2.50%	A+
<b>State of California Totals</b>						707	2.36%	
U.S. Agency Securities	FNMA Note	999995AA9	13-Apr-01	15-Apr-03	none	15	5.75%	AAA
	FHLB Note	999994AA9	16-Apr-01	23-Apr-03	none	23	5.25%	AAA
<b>Agency Totals</b>						20	5.42%	
Banker's Acceptances	Bank of New York	999993AA9	17-Oct-02	2-Jul-03	none	93	1.75%	NR
	RaboBank	999992AA9	18-Oct-02	16-Jul-03	none	107	1.50%	NR
<b>Banker's Acceptances Totals</b>						97	1.68%	
Commercial Paper	Ascension Health DC/P	999991AA9	12-Dec-02	1-Apr-03	none	1	NA	A-1
	Bear Sterns COS DC/P	999990AA9	10-Oct-02	1-Apr-03	none	1	NA	A-1
<b>Commercial Paper Totals</b>						1		
Negotiable CDs	Bank of Nova Scotia	999989AA9	13-Feb-03	14-May-03	none	44	1.50%	A-1+
	Royal Bank of Scotland	999988AA9	18-Feb-03	19-May-03	none	49	1.25%	A-1
<b>Negotiable CD Totals</b>						47	1.37%	
Repurchase Agreement	Lehman Agency Repo	999987AA9	11-Oct-02	1-Apr-03	none	1	1.25%	NR
	Morgan Stanley Repo	999986AA9	11-Nov-02	1-Apr-03	none	1	1.25%	NR
<b>Repurchase Agreement Totals</b>						1	1.25%	
Medium Term Note	Wachovia Corp NT	999985AA9	22-Oct-02	15-Apr-03	none	15	6.50%	AA-
	GAP Inc.	999984AA9	15-Aug-02	1-May-03	none	31	6.25%	A+
<b>Medium Term Note Totals</b>						28	6.29%	
Mutual Fund	Fidelity	999983AA9	3-May-99	1-Apr-03	none	1	1.00%	AAA
	Trust Proven Fund	999982AA9	12-Jun-98	1-Apr-03	none	1	1.25%	AAA
<b>Mutual Fund Totals</b>						1	1.04%	
Money Market Mutual Fund	Goldman Sachs Prime Obl.	999981AA9	4-May-00	1-Apr-03	none	1	1.25%	AAA
	Federated Govt. Obl. Fund	999980AA9	18-Sep-02	1-Apr-03	none	1	1.50%	AAA
<b>MMM Fund Totals</b>						1	1.45%	
Cash	Secured MKT DEP Acct			1-Apr-03	none	1	0.50%	NR
	Vault			1-Apr-03	none	1	0.00%	NR
	Bank of Trust			1-Apr-03	none	1	1.00%	NR
<b>Cash Totals</b>						1	0.94%	
Asset Backed Securities	Daimler Chrysler Auto Trust	999979AA9	31-Dec-02	6-Apr-05	6-Apr-04	737	2.25%	AA-
<b>Asset Backed Securities Totals</b>						737	2.25%	
LAIF	LAIF -- Treasury			1-Apr-03	none	1	2.00%	NR
<b>Managed Pool Accounts Totals</b>						1	2.00%	
<b>Total Portfolio</b>						35	2.52%	

I certify that this report accurately reflects all City investments, and is in conformance with the adopted City Investment Policy. Furthermore, I certify to the best of my knowledge, sufficient investment liquidity and anticipated revenues are available to meet the City's budgeted expenditures.

Duration can be used in place of weighted average maturity.

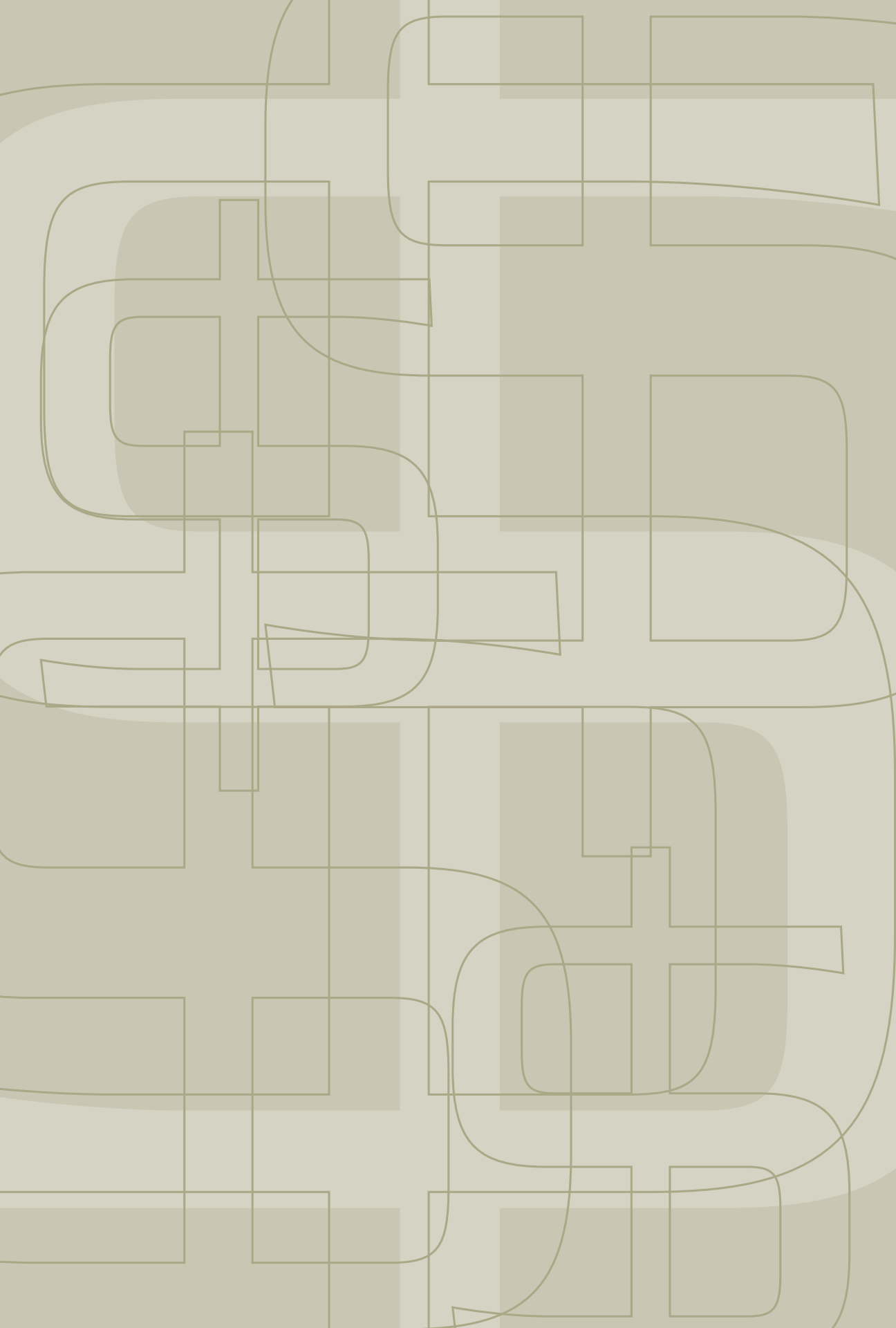
Market values should be reported for each asset as of the date of the investment report. The source of the market value should be indicated, as well.

Book value is also understood to be the amortized cost value of an asset.

Par Value	Market Value	Percent Portfolio Value (Market)	Book Value	Unrealized Gain/Loss	Yield-to-Maturity	Pricing Source	Manager	Broker/Dealer
\$ 1,000,000	\$ 1,031,096	1.01%	\$ 1,066,302	\$ (35,206)	3.00%	JJ Kenny	City	Merrill Lynch
1,500,000	1,500,000	1.47%	1,500,000	-	8.50%	JJ Kenny	City	Merrill Lynch
\$ 2,500,000	\$ 2,531,096	2.49%	\$ 2,566,302	\$ (35,206)	6.21%			
\$ 2,000,000	\$ 2,023,000	1.99%	\$ 2,004,000	\$ 19,000	2.03%	FTI	Broker	
300,000	313,000	0.31%	303,000	10,000	3.24%	FTI	Broker	
\$ 2,300,000	\$ 2,336,000	2.30%	\$ 2,307,000	\$ 29,000	2.19%			
\$ 200,000	\$ 195,920	0.19%	\$ 196,541	\$ (621)	1.15%	JJ Kenny	City	Salomon
500,000	507,500	0.50%	495,481	12,019	2.58%	JJ Kenny	City	Salomon
\$ 700,000	\$ 703,420	0.69%	\$ 692,021	\$ 11,399	2.17%			
\$ 5,000,000	\$ 5,009,000	4.92%	\$ 5,159,000	\$ (150,000)	2.37%	FTI	City	Morgan Stanley
10,000,000	10,043,750	9.87%	10,065,000	(21,250)	1.21%	FTI	City	Morgan Stanley
\$ 15,000,000	\$ 15,052,750	14.79%	\$ 15,224,000	\$ (171,250)	1.60%			
\$ 1,000,000	\$ 996,714	0.98%	\$ 992,207	\$ 4,507	1.69%	Bloomberg	Broker	
400,000	398,483	0.39%	396,560	1,923	1.73%	Bloomberg	Broker	
\$ 1,400,000	\$ 1,395,197	1.37%	\$ 1,388,767	\$ 6,431	1.71%			
\$ 5,000,000	\$ 5,000,000	4.91%	\$ 4,989,000	\$ 11,000	1.29%	Bloomberg	City	Paine Webber
1,000,000	1,000,000	0.98%	999,700	300	1.31%	Bloomberg	City	Paine Webber
\$ 6,000,000	\$ 6,000,000	5.90%	\$ 5,988,700	\$ 11,300	1.29%			
\$ 300,000	\$ 300,070	0.29%	\$ 300,050	\$ 20	1.32%	Bloomberg	City	Bear Stearns
300,000	301,000	0.30%	300,800	200	1.33%	Bloomberg	City	Bear Stearns
\$ 600,000	\$ 601,070	0.59%	\$ 600,850	\$ 220	1.33%			
\$ 150,000	\$ 151,000	0.15%	\$ 150,000	\$ 1,000	1.25%	IDC	Broker	
2,400,000	2,400,000	2.36%	2,400,000	-	1.25%	IDC	Broker	
\$ 2,550,000	\$ 2,551,000	2.51%	\$ 2,550,000	\$ 1,000	1.25%			
\$ 1,000,000	\$ 1,001,700	0.98%	\$ 1,030,000	\$ (28,300)	3.01%	FTI	City	Barclay's Capital
5,000,000	5,006,500	4.92%	5,018,000	(11,500)	5.43%	FTI	City	Barclay's Capital
\$ 6,000,000	\$ 6,008,200	5.90%	\$ 6,048,000	\$ (39,800)	5.02%			
\$ 5,800,000	\$ 5,800,000	5.70%	\$ 5,800,000	\$ -	1.00%	IDC	City	Citigroup
1,198,000	1,198,000	1.18%	1,198,000	-	1.25%	IDC	Broker	
\$ 6,998,000	\$ 6,998,000	6.88%	\$ 6,998,000	\$ -	1.04%			
\$ 35,634	\$ 35,634	0.04%	\$ 35,634	\$ -	1.25%	IDC	City	Union Bank
132,686	132,686	0.13%	132,686	-	1.50%	IDC	City	Union Bank
\$ 168,320	\$ 168,320	0.17%	\$ 168,320	\$ -	1.45%			
\$ 827,000	\$ 827,000	0.81%	\$ 827,000	\$ -	0.50%	Bank	Bank	Goldman Sachs
540,000	540,000	0.53%	540,000	-	0.00%		City	
15,961,000	15,961,000	15.68%	15,961,000	-	1.00%	Bank	Bank	
\$ 17,328,000	\$ 17,328,000	17.03%	\$ 17,328,000	\$ -	0.94%			
\$ 100,000	\$ 100,354	0.10%	\$ 99,996	\$ 358	0.48%	FTI	Broker	
\$ 100,000	\$ 100,354	0.10%	\$ 99,996	\$ 358	0.48%			
\$ 40,000,000	\$ 40,000,000	39.30%	\$ 40,000,000	\$ -	2.00%	LAIF	LAIF	
\$ 40,000,000	\$ 40,000,000	39.30%	\$ 40,000,000	\$ -	2.00%			
\$ 101,644,320	\$ 101,773,407	100%	\$ 101,959,956	\$ (186,549)	1.92%			

requirements for the next six months.

Signature \_\_\_\_\_



## VII. DEFINITIONS OF TERMS USED IN THE SAMPLE INVESTMENT PORTFOLIO REPORT

### **Book Value**

Represents the value at which an asset is carried on a balance sheet.

### **Coupon**

The interest rate on a debt security the issuer promises to pay to the holder until maturity, expressed as an annual percentage of face value.

### **CUSIP Number**

Committee on Uniform Security Identification Procedures (CUSIP) numbers are unique identification numbers assigned to each maturity of a domestic debt or equity issuance. A similar system exists for foreign securities. These numbers are used by all sectors of the financial industry for identifying, clearing, and settling securities as well as for other functions. Securities with different interest rate structures and/or maturities are assigned unique numbers. Under the CUSIP system, a unique nine-digit number is assigned to a security. The first six digits identify the issuer and are assigned to issuers alphabetically. The next

two digits identify the issue. The ninth digit is the check digit, which provides the means of determining the accuracy of the whole number used in data transmission.

### **Manager**

The name of the contracted party to whom decision-making has been authorized. Local agencies are required to describe and provide the market value of investments under the management of contracted entities.

### **Market Value**

Represents the current price knowledgeable buyers are willing to pay for the security.

### **Par Value**

Represents a security's face or nominal value, before any discounts or premiums are taken. If interest rates are higher than the coupon rate, the bond will be sold below par value. If interest rates are lower than the coupon rate, the bond will sell above the par value.



### Pricing Source

The industry source for all market value information in the portfolio.

### Rating

A published ranking of one's financial history, based on detailed financial analyses by a nationally recognized statistical rating organization (NRSRO), specifically as it related to the ability to meet debt obligations. This example uses Standard and Poors' and Fitch's system for long-term debt issuance in which the highest rating is AAA and the lowest is D. The example uses Standard and Poor's system for short-term debt in which the highest rating is A-1 and the lowest is D.

### Unrealized Gain or Loss

The difference between the security's reported market value and its initial cost at the time of purchase.

### Weighted Average Maturity (WAM)

Provides an estimate of the average maturity of all assets held. It weights the time difference between the date of the report and the date an asset

matures according to its share of the total portfolio. Assets accounting for a larger portion of the portfolio's total value have a greater influence in determining the average maturity of the portfolio. The definition of WAM that takes into account the current value of the portfolio is  $\Sigma$  (days to maturity x market value)/total market value.

### Yield-to-Maturity

The yield-to-maturity is the rate of return on an investment or a portfolio that equates the future cash flow (future values) to the initial cost or purchase price (present value). It is typically reported on a 360-day year or a 365-day year basis. Yield may be represented in other ways, including current yield (market), current yield (cost), and yield-to-call. For a more complete discussion of these yield calculations, see CDIAC's *Understanding Investment Reporting Requirements: A Handbook for Local Elected Officials*.





## VIII. ADDITIONAL REPORTING PRACTICES

Besides the legally required information, CDIAC's examination of submitted investment reports revealed a number of additional items that local agencies may wish to present to their legislative bodies in the content of an investment report. Local agencies should consider reporting this information to the extent that it assists their legislative bodies meet its fiduciary obligations. The following charts (some of which are based on information displayed in Figure 2 on pages 18-19) name and describe the practices, discuss each, and provide examples of the practice based on the sample investment portfolio report or actual quotes from

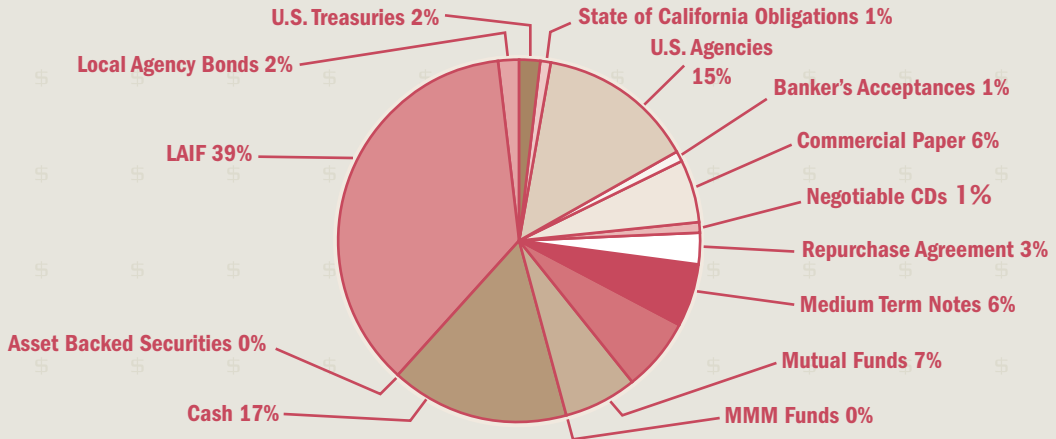
the investment reports that have been submitted to CDIAC.

- Distribution by Sector
- Distribution by Manager Type
- Distribution by Credit Quality
- Distribution by Maturity
- Distribution by Issuer
- Using Benchmarking to Evaluate Performance
- Annual WAM and Yield Trends
- Cash Flow Projections
- Investment Compliance Checklist
- Describing the General Economic Climate
- Discussion of Investment Strategy
- Chronicling Economic Announcements
- Reporting Yield



## Distribution by Sector

### Asset Distribution (Market Value) As of 3/31/03



#### SECURITY TYPE

#### MARKET VALUE

Local Agency Bonds	\$2,531,096
U.S. Treasuries	2,336,000
State of California Obligations	703,420
U.S. Agencies	15,052,750
Banker's Acceptances	1,395,197
Commercial Paper	6,000,000
Negotiable CDs	601,070
Repurchase Agreements	2,551,000
Medium Term Notes	6,008,200
Mutual Funds	6,998,000
MMM Funds	168,320
Cash	17,328,000
Asset Backed Securities	100,354
LAIF	40,000,000

#### TOTAL PORTFOLIO

**\$101,773,407**

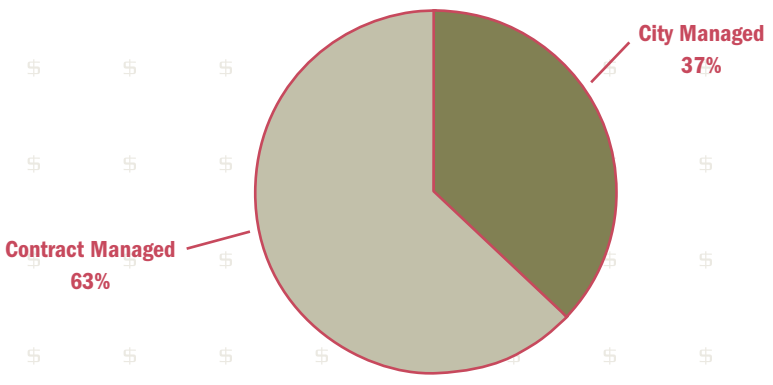
**SUMMARY** | Local agencies may choose to use a chart to illustrate the distribution by sector. The agency must make clear what the basis (par, market, or cost) is for the evaluation being used, as different bases may yield different results.

**DISCUSSION** | Local agencies may find it helpful to display required information in graphic form. Doing so will make reading and interpreting the information easier. The agency's legislative body can use this information to understand the agency's exposure to a particular sector. For example, if the legislative body believes that the banking industry is about to take a downturn, then perhaps a good strategy would be to lower the exposure to banker's acceptances and negotiable CDs.

Including just a graphical representation without the accompanying value of sector in dollar terms will not represent a full picture to the legislative body.

# Distribution by Manager Type

## Value by Manager Type (Market Value) As of 3/31/03



MANAGER TYPE	MARKET VALUE
City Managed	\$37,404,856
Contract Managed	64,368,551
<b>TOTAL PORTFOLIO</b>	<b>\$101,773,407</b>

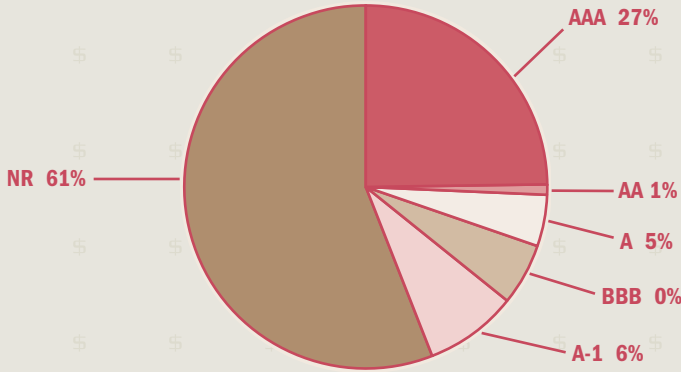
**SUMMARY** | Local agencies may choose to use a chart to illustrate the distribution by type of manager. The agency must make clear what the basis (par, market, or cost) is for the evaluation being used, as different bases may yield different results.

**DISCUSSION** | Local agencies may find it helpful to display required information in graphic form. Doing so will make reading and interpreting the information easier.

Although it may be helpful to visualize the ratio of a portfolio that is internally versus externally managed, the legislative body may be more concerned that securities of a particular type are being managed under external contract. This is not apparent in a chart.

## Distribution by Credit Quality

### Ratings Distribution (Market Value) As of 3/31/03



RATING	MARKET VALUE
AAA	\$ 27,086,166
AA	1,102,054
A	5,514,000
BBB	195,920
A-1	6,601,070
NR	61,274,197
<b>TOTAL PORTFOLIO</b>	<b>\$101,773,407</b>

#### AAA Investments Include:

U.S. Agencies (55%)  
Mutual Funds (27%)  
Local Agency Bonds (9%)  
Treasury Notes (9%)

#### AA Investments Include:

Medium Term Notes (91%)  
Asset Backed Securities (9%)

#### A Investments Include:

Medium Term Notes (91%)  
State of California Obligations (9%)

#### BBB Investments Include:

State of California Obligations (100%)

#### A-1 Investments Include:

Commercial Paper (91%)  
Negotiable CDs (9%)

#### Non-Rated Investments Include:

Managed Pool Accounts (65%)  
Cash (28%)  
Repurchase Agreements (4%)  
Banker's Acceptances (3%)

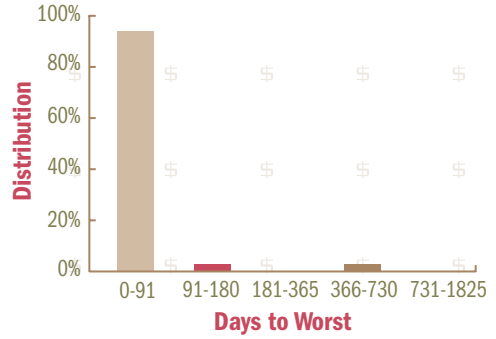
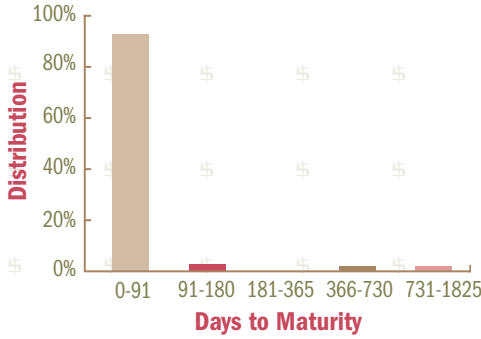
**SUMMARY** | Local agencies may choose to use a pie chart to illustrate the credit quality composition of the portfolio. The agency must make certain that each rating is drawn from the same rating scale, as the rating used by different rating agencies may refer to different credit qualities.

**DISCUSSION** | Using a chart or graph to display the credit quality of the portfolio is a tool that can quickly describe the credit risk inherent in the portfolio. A local agency's legislative body can use the chart to anticipate potential threats to the portfolio's safety. It can also use the chart to evaluate the tradeoff between the portfolio's yield and the implied credit risk.

A chart or graph displaying the credit quality of the portfolio may reduce the importance and unique aspects of the individual securities within the portfolio. To the degree that the chart addresses ratings independent of yield or liquidity measure, it would not provide the legislative body sufficient information to effectively evaluate the portfolio's composition.

# Distribution by Maturity

Maturity Distribution (Market Value) As of 3/31/03



DAYS TO MATURITY	MARKET VALUE	MATURITY DISTRIBUTION	DAYS TO WORST	MARKET VALUE	MATURITY DISTRIBUTION
0-91	\$94,707,340	93%	0-91	\$95,214,840	94%
91-180	2,895,197	3%	91-180	2,895,197	3%
181-365	-	-	181-365	-	-
366-730	2,218,920	2%	366-730	3,350,370	3%
731-1825	1,951,950	2%	731-1825	313,000	0%
<b>TOTAL PORTFOLIO</b>	<b>\$101,773,407</b>	<b>100%</b>		<b>\$101,773,407</b>	<b>100%</b>

**SUMMARY** | Many local agencies illustrate their interest rate exposure by aging their portfolios. This is done in a number of ways, including spreadsheets that list a range of days to maturity and the percent of the portfolio in each range. This information can be converted into a chart to enable the legislative body to gauge the liquidity of the portfolio and ability to meet any near-term cash needs.

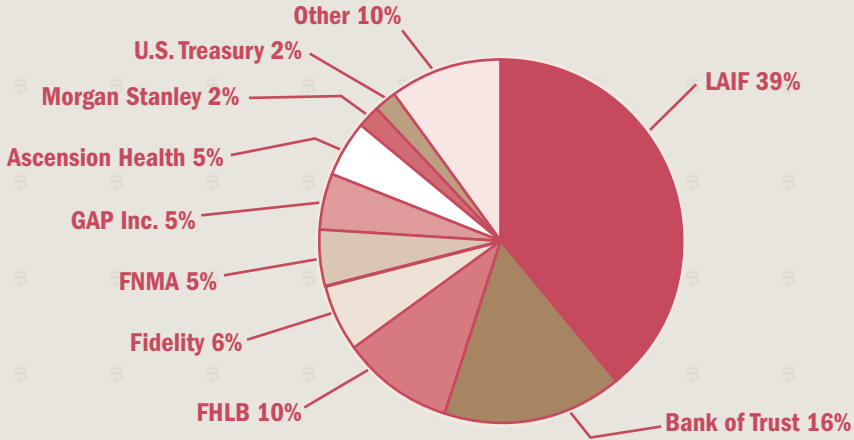
**DISCUSSION** | By understanding the liquidity of the portfolio, the legislative body can better report on the agency's ability to meet its cash flows needs and determine the source and costs of providing liquidity in the future.

The chart provides a rough gauge of the distribution of the investments, the accuracy of which depends on how narrowly defined are the intervals. Broadly defined intervals may not provide the legislative body with enough information if significant cash needs must be met at certain time frames.

If your local agency invests in callable securities, consider incorporating the worst-case scenario calls into this maturity distribution.

## Distribution by Issuer

### Issuer Concentration (Market Value) As of 3/31/03



ISSUER	MARKET VALUE
LAIF	\$ 40,000,000
Bank of Trust	15,961,000
FHLB	10,043,750
Fidelity	5,800,000
FNMA	5,009,000
GAP Inc.	5,006,500
Ascension Health	5,000,000
Morgan Stanley	2,400,000
U.S. Treasury	2,336,000
Other *	10,217,157
<b>TOTAL PORTFOLIO</b>	<b>\$ 101,773,407</b>

\* Includes all issuers with concentrations less than 2 percent.

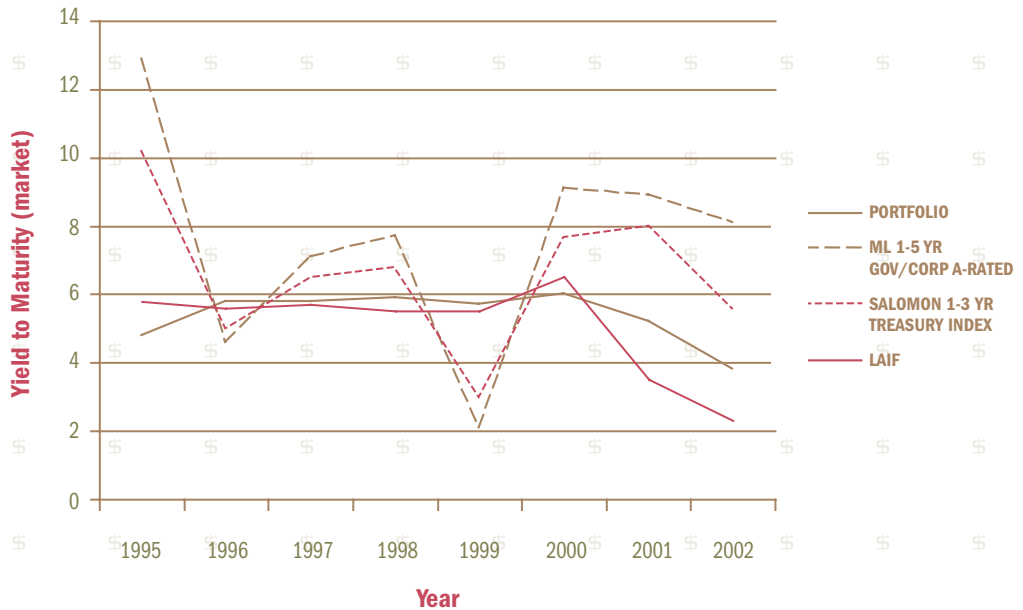
**SUMMARY** | Local agencies may list the largest issuers in their portfolios and the percent of the total portfolio represented by each. Decision-makers can use this chart as a rough gauge of the portfolio's diversity and exposure to default risk.

**DISCUSSION** | A local agency can use graphs or charts to represent the concentration of investments in specific issuers, which would assist in ensuring it is in compliance with applicable state law concentration limits. The agency's legislative body can use this information to understand the agency's exposure to default risk.

To the extent that the portfolio experiences a high turnover among its assets, a breakdown by issuers may not provide useful information to the agency's legislative body. In addition, without additional information such as issuer credit rating, it would be difficult to make any definitive determination regarding default risk of the portfolio.

# Using Benchmarking to Evaluate Performance

## Treasurer's Investment Portfolio vs. Benchmarks

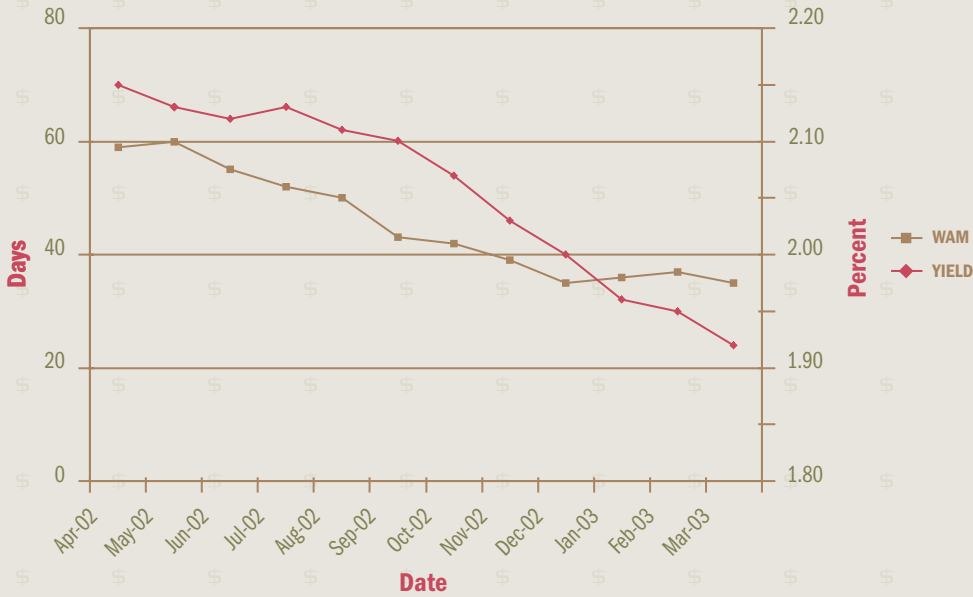


**SUMMARY** | Many local agencies compare their yields against a benchmark. Local agencies differ according to their cash flows, investment policies, etc., making it important to identify a benchmark that contains a distribution of assets that reflects their safety and liquidity goals. An example of a commonly used benchmark is LAIF. Commonly used total return benchmarks include the Merrill Lynch Index of 1-5 Year Government/Corporate A-Rated Securities or the Salomon Index of 1-3 Year Treasury Securities. When comparing a portfolio to a benchmark, it is important to use yield to maturity (market) value of all investments, not yield to maturity (cost).

**DISCUSSION** | The agency can evaluate the performance of its investment portfolio based upon a measure that incorporates its goals for safety and liquidity.

If an inappropriate benchmark is selected, interpreting the results of a comparison between the agency's portfolio and the benchmark are hampered. If YTM (cost) is used when comparing the portfolio to a benchmark, it will be higher than the benchmark YTM in a falling interest rate environment and lower than the benchmark in a rising interest rate environment. In such an instance, the comparison may not provide useful information.

# Annual WAM and Yield Trends



MONTH	WAM	YIELD	MONTH	WAM	YIELD
Apr-02	59	2.15	Oct-02	42	2.07
May-02	60	2.13	Nov-02	39	2.03
Jun-02	55	2.12	Dec-02	35	2.00
Jul-02	52	2.13	Jan-03	36	1.96
Aug-02	50	2.11	Feb-03	37	1.95
Sep-02	43	2.10	Mar-03	35	1.92

**SUMMARY** | Some local agencies chart their portfolio weighted average days to maturity and portfolio month-end yield.

**DISCUSSION** | Performing a trend analysis of changes in the local agency’s weighted average maturity and portfolio yield allows the agency’s legislative body to consider the relationship between factors internal and external to the agency and the composition of the portfolio. For example, economic conditions may have created a yield curve that provides similar investment benefits in the short-term as in the long-term (i.e., a flat yield curve). As a result, the agency’s weighted average maturity would be expected to decline because there would be little benefit for accepting the risks that accompany long-term investments. A trend analysis would illustrate this change in the agency’s investment practices. To be useful, trend analyses should be accompanied by supporting information that reveals the rationale, causes, and effects of these changes in the portfolio’s structure or performance. In the absence of this information, the agency’s legislative body may misinterpret trends. For example, a trend analysis that reveals declining yields may drive the legislative body to emphasize yield over safety and liquidity goals. In such a case, a push for improved yield may force the agency to select investments that carry greater risk than it normally would select.



# Cash Flow Projections

## Six Month Cash Availability Projection

MONTH	MONTH END EXPECTED BALANCE	INVESTMENT MATURITIES	DEPOSITS	DISBURSEMENTS	EXCESS CASHFLOW	MONTH END CUMULATIVE BALANCE
Apr-03	\$ 900,000	\$ 300,000	\$ 4,000,000	\$ 3,200,000	\$ 500,000	\$ 800,000
May-03	800,000	300,000	3,700,000	3,600,000	100,000	900,000
Jun-03	\$ 500,000	\$ 200,000	\$ 3,000,000	\$ 3,500,000	- 500,000	\$ 400,000
Jul-03	400,000	100,000	3,000,000	3,200,000	- 200,000	200,000
Aug-03	600,000	400,000	3,500,000	3,300,000	200,000	800,000
Sep-03	\$ 800,000	\$ 200,000	\$ 3,800,000	\$ 3,800,000	\$ 0	\$ 1,000,000

Note: Expected cash flow projections for the next six months continue to indicate that sufficient cash is available for estimated needs.

**SUMMARY** | Local agencies illustrate the cash flows of the municipality six to 12 months out and evaluate the ability of the portfolio to meet the expected cash flow demands during this period.

**DISCUSSION** | The local agency treasurer must include a statement in the investment report that sufficient cash is available to meet the agency's needs for the next six months. Cash flow projections that accompany the investment report add clarity and detail to this statement, thus aiding the legislative body in their investment decisions and evaluation.

Cash flow projections are based upon a variety of assumptions that may change due to conditions beyond the agency's control (i.e., state economic climate and budgetary issues). If these factors are not monitored regularly, the cash flow forecast may not accurately represent the revenue/expenditure conditions facing the local agency.

# Investment Compliance Checklist

CALIFORNIA GOVERNMENT CODE SECTION	INVESTMENT CATEGORY	MAXIMUM MATURITY	AUTHORIZED INVESTMENT LIMITS (PERCENT OF PORTFOLIO)*	CREDIT RATING LIMITS	COMPLIANCE CHECK	COMMENTS
53601(a)	Local Agency Bonds	5 years	None	None	✓	
53601(b)	U.S. Treasuries	5 years	None	None	✓	
53601(c)	State of California Obligations	5 years	None	None		None
53601(d)	California Local Agency Obligations	5 years	None	None		None
53601(e)	U.S. Agencies	5 years	None	None	✓	
53601(f)	Banker's Acceptances	180 days	40%	None	✓	
53601(g), 53635	Commercial Paper	270 days	25% of portfolio	A-1/P-1/F-1	✓	
53601(h)	Negotiable CDs	5 years	30%	None	✓	
53601(i)	Repurchase Agreements	1 year	None	None	✓	
	Reverse Repurchase Agreements & Securities Lending Agreements	92 days	20% of the base value of the portfolio	None		None
53601(j)	Medium Term Notes	5 years	30%	A	✓	
53601(k)	Mutual Funds	None	20%	Multiple	✓	
	MMM Funds	None	20%	Multiple	✓	
53601 (m)	Collateralized Bank Deposits (including non-negotiable CDs)	5 years	None	None		None
53601(n)	Asset Backed Securities	5 years	20%	AA	✓	
	Time Deposits	5 years	None	None		None
53684	County Pooled Investment Funds	None	None	None		None
	Cash	None	None	None	✓	
16429.1	LAIF	None	None	None	✓	

\* Based upon weighted average maturity of the fund's investments.

Note: This portfolio is in compliance with the Statement of Investment Policy.

**SUMMARY** | California Government Code Section 53646 requires local agencies to indicate in their investment reports whether their investments comply with the agency's investment policies.

**DISCUSSION** | The local agency can graphically illustrate its compliance with its own investment policy in tabular format. If a limit is exceeded, the reason can be stated in the comments column.

The legislative body may just hone in on whether or not the local agency's investments are in compliance with its policy, without paying attention to other factors, like ratings, maturity distribution, comparison to benchmark, etc.

## Describing the General Economic Climate

*Generalized excerpt from local agency portfolio report:* “With geopolitical stresses and continued sluggish economies around the world, economic conditions in the U.S. remained soft and slow throughout most of the country. We end the year in modestly better shape than where we were a year ago with signs pointing to possible improvement in the early part of next year. The uncertainties surrounding a prospective war and the political crises in several countries have all contributed to higher oil prices. These uncertainties have also limited gains in the equity markets and helped drive down interest rates even further.

In its meeting at the beginning of the month, the Federal Open Market Committee (FOMC), the Federal Reserve’s policy-setting arm, decided to keep short-term interest rates unchanged. After the surprise drop of 50 basis points in November, it came as no surprise that the FOMC left rates where they were. In the Beige Book, the report on economic conditions throughout the country prepared for the FOMC, the Federal Reserve reported that economic activity grew slowly. The report also noted the following observations:

- Consumer spending varied widely around the country
- Manufacturing remained soft
- Business capital spending continued to be limited
- Commercial real estate markets continued to be slack

- Agricultural conditions have been adversely affected by heavy rain and cold weather
- Bank lending remains strong for residential real estate, but other categories of lending have been lackluster
- Labor markets continued to be soft, while wage and salary pressures were subdued
- Prices were reported as steady at both the consumer and producer levels

The data reported during the month supported these views. The unemployment rate jumped back up to the high reached in April. Consumer confidence has begun to show some signs of having bottomed and is rebounding slowly. The housing market has remained strong, due to very low mortgage rates, and is providing excellent support to the economy as a whole.

Interest rates continued to drop, primarily responding to the geopolitical concerns mentioned earlier. Short-term rates dropped by a modest 5 to 10 basis points while longer-term rates dropped 25 to 50 basis points. Most interest rate sectors are at or near record lows and likely will remain at low levels until the economy shows sustainable improvement.

Given the current interest rate environment, we anticipate the local agency’s yield to decline. Further, we continue to seek investment opportunities in order to optimize earnings.”

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**SUMMARY** | Local agencies can provide information on federal, state, and local economies by describing economic indicators such as yield curves, consumer confidence, employment, manufacturing activity, commodity prices, inflation, and retail sales, and indicating how such world events may affect the market and, in return, the agency’s portfolio.

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**DISCUSSION** | Will provide legislative body and public some perspective on the portfolio’s performance. Can reflect the importance of the international, national, state, and regional economy on performance, and provide an indirect measure of the portfolio’s distribution and exposure to economic risks.

A detailed description of the relationship between economic conditions and the performance of specific investment assets in the portfolio may be beyond the resources available in-house. The services of external consultants may be required to interpret economic measures, leading to additional costs to the agency.

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## Discussion of Investment Strategy

Generalized excerpt from local agency investment report: “Since the Federal Reserve dropped overnight interest rates to 1.25 percent, it has become very difficult to achieve a 2 percent return on any new investment that is less than two years in maturity. The 2-year U.S. Treasury has been yielding approximately 1.75 percent. Even short-term callable agencies do not provide much above 2 percent. With the continued weakness in the economy, it is not expected that rates will change very much over the next few months.

With quality concerns rising in a slow economy, there has been very little value in purchasing corporate securities. Securities issued by federal agencies such as the Federal Home Loan Bank, Freddie Mac, and Fannie Mae have

about the same yield as those issued by corporations. Although the U.S. government does not guarantee these issues, they all have AAA ratings and an implied support of the federal government, so this is where most new investments have been made.

It is expected that interest rates will be higher in two years, so virtually all new investments have been two years or less in maturity, so that the funds will be available for reinvestment when rates do go up. The average maturity of the portfolio has been extended to take advantage of the sharp yield curve when extending beyond one year; however, in anticipation that rates will begin to rise in the future, most new investments will continue to be in the two year or less range.”

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**SUMMARY** | Some local agencies describe their investment strategy within the context of the current state of the economy and with the projected direction of interest rates. Other local agencies make a general statement in their investment reports associating investment decisions with the shape of the yield curve.

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**DISCUSSION** | A discussion of the local agency’s investment strategy with respect to economic conditions allows the legislative body to better understand the portfolio’s composition and rationale for certain investment decisions. In general, understanding the basis for the development of the portfolio will assist the legislative body in determining whether its decisions meet the agency’s policies and goals.

Generalized discussion of economic conditions as they relate to investing may encourage inappropriate decision-making and the desire to “time the market,” which may distract the agency from achieving its safety, liquidity, and yield goals.

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# Chronicing Economic Announcements

## REPORTED IN DECEMBER

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### **Durable Goods Orders – for March 24th**

1.4 percent actual vs. 0.8 percent survey

### **Gross Domestic Product (GDP) – for March 20th**

4.0 percent actual vs. 4.0 percent survey

### **Consumer Confidence Index – for March 31st**

80.3 percent actual vs. 86.0 percent survey

### **Factory Orders – for March 4th**

1.5 percent actual vs. 1.7 percent survey

### **Unemployment Rate – for March 6th**

6.0 percent actual vs. 5.8 percent survey

### **FOMC Rate Decision – for March 10th**

Unchanged at 1.25 percent actual vs. 1.25 percent survey

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**SUMMARY** | Local agencies may describe the upcoming economic calendar, including the release of data on retail sales, changes in the consumer price index, and other economic indicators. This, along with an economic market commentary, may enable decision makers to better understand the environment in which investment decisions are to be made.

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**DISCUSSION** | A well-documented analysis of the relationship between economic announcements and investment performance may help the agency's legislative body to interpret its exposure to risk. To the degree employed in making investment decisions, it can reflect the local agency's commitment to anticipate changing economic conditions.

Using such information requires a comprehensive understanding of the relationship between economic announcements and investment performance. The time commitment to develop such an understanding and track changes regularly may be beyond the resources of the local agency.

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## Reporting Yield

See sample portfolio displayed in Figure 2 on page 18-19 for examples of the use of yields (total coupon rate and yield-maturity). If the portfolio had a significant number of investments that were callable, yield-to-call could be an appropriate measure of yield to include.

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**SUMMARY** | Local agencies may present their yields in a number of different ways, including average weighted yield, total coupon rate, yield-to-call, and yield-to-maturity. Yield figures may be calculated on the basis of a 360-day or a 365-day calendar.

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**DISCUSSION** | Reporting the agency's yield provides a measure of investment performance. An agency may use this information to determine the costs and benefits of its investment strategy.

Reporting yield may stimulate the natural desire among portfolio managers to compare returns among local agencies. Yield comparisons may, indirectly, stimulate managers to make decisions that do not maximize the important objectives of portfolio safety or liquidity.

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## ACKNOWLEDGEMENTS

This publication was written by Mark Campbell and Frank Moore, Senior Research Specialists, with the assistance of Nova Edwards, Research Analyst, all of CDIAC's Policy Research Unit. CDIAC acknowledges the contributions of several individuals and organizations in the production of this document. They include: Lisa Marie Harris, CDIAC Executive Director; Kristin Szakaly-Moore, CDIAC's Director of Policy Research; Bill Blackwill; Lee Buffington; Kay Chandler; Raymond Day; Nancy Jones; the California Municipal Treasurers Association; and the California Association of County Treasurers and Tax Collectors.

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