

To: Benjamin I. Myers, City Manager

From: Melissa R. Marsh, Deputy City Manager - Administrative Services

Date: October 26, 2015

RE: Investment Report 1st Quarter of Fiscal Year 2016

A summary of the investments for the City of Madison Heights as of September 30, 2015 is included in this memo. The requirements of the City of Madison Heights Investment Policy and P.A. 20 of 1943, as amended, govern the investments held by the City.

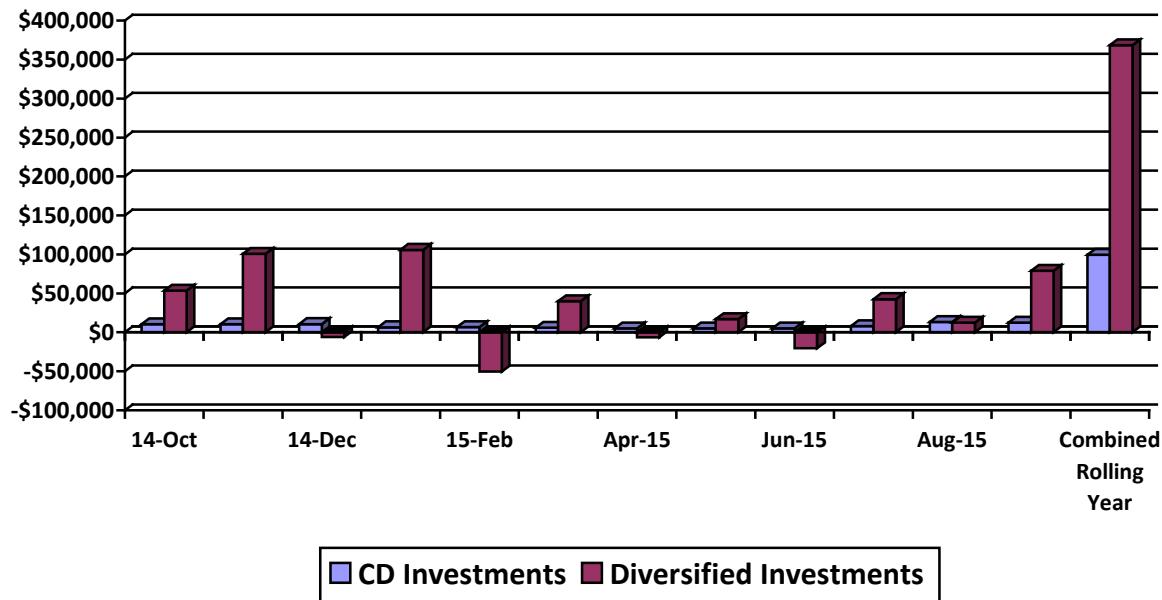
Interest Rate Overview:

Interest rates continue to be low and uncertainties surrounding the health of the global economy continue to intensify July – September. Conflicting economic reports in the U.S. leaves it unclear whether the Fed would or should raise rates in September. These uncertainties led, in part, to a concerted global market selloff across most stocks and bonds, while the U.S. dollar essentially remained flat. U.S. Treasuries and fixed income continues to gather some “safe-haven” interest. As the Fed moved toward hiking rates, it is anticipated that stocks may again start gaining interest over bonds which may lead to market value in bonds declining over the next quarter as rates increase. It is important to note that this may cause reduction in the market yeild of our bonds but will not result in a loss of original principal.

Locally we continue to diversify investments instead of moving to vehicles such as 100% Certificates of Deposit. This is due to the long term nature of our fixed rate investments and the higher rate of return we will realize by holding these fixed rate vehicles such as bonds and treasuries until either the call date or maturity. As explained in previous reports, in any given quarter, the method of marking investments to market value (which refers to accounting for the fair value of an asset or liability based on its current market price) may result in loss; however, holding bonds until maturity would result in the total return of investment. I have included a chart below that compares our current returns with what our returns would be if we were invested 100% in Certificates of Deposit at the rate of 0.48% for 12-17 month investment during the July - September period (the average rate of return for CDs). Investing completely in CDs for the fiscal year to date would have yielded approximately \$37,612 in investment earnings; instead we earned \$134,208 through September by following our diversified investment plan.

The chart on the next pages shows the differential between investments 100% in certificates of deposit vs. the City's diversified investment strategy:

Investment Earnings



Risk:

Interest rate risk is the risk that interest rates will change and adversely affect the fair value of the investment of the government's cash flows. The City attempts to limit exposure to a possible decline in fair market value by diversifying maturity dates.

Credit risk is the risk that the investment will not fulfill its promise to pay the investor when required. There is a credit risk associated with all financial institutions, brokers and investment vehicles. The City attempts to limit exposure to credit risk by diversifying the holders of investments, maintaining a high credit rating for investments, and restricting Certificates of Deposit investments to those with financial institutions that are members of the Federal Deposit Insurance Corporation (FDIC).

Concentration of risk occurs when the municipality is heavily invested in one issuer. The city's largest issuer is the Local Government Investment Pool managed by Oakland County. This pool is diversified with other County investments.

Quarter Investments:

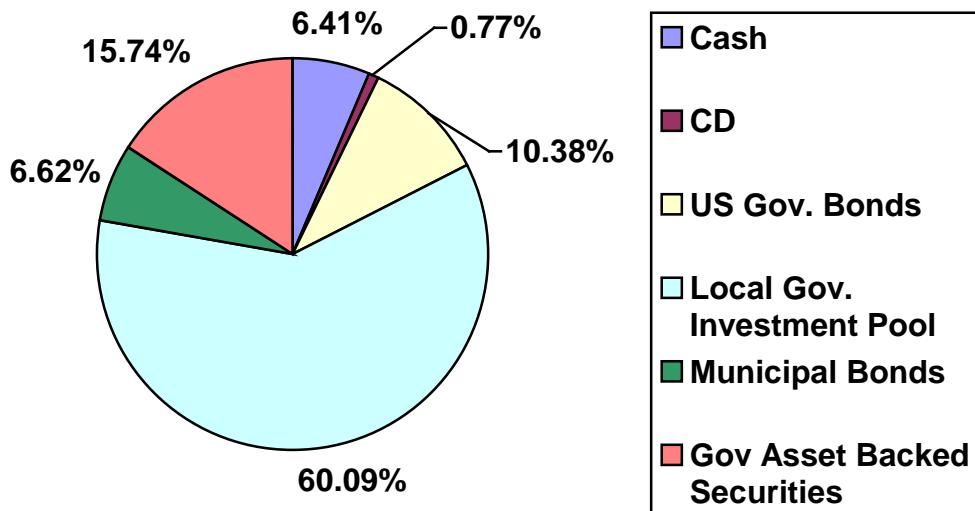
As of September 30, 2015, the City has the following Cash and Investment balances (combination of all funds, excluding pension and health care savings funds).

Total amount in the cash accounts	\$ 2,147,266
Total amount in Investments	<u>31,343,058</u>
	\$33,490,324

The chart below details the diversification of the City investments as of September 30, 2015.

Diversification – First Quarter of Fiscal Year 2016

Last Day of the Quarter



In accordance with the City's investment policy, the City limits its exposure to possible decline in fair market value by maintaining diversification and controlling maturity dates. The table below details the amounts at September 30, 2015. There is a difference between the coupon rate (i.e. yield at issue date) and the estimated quarterly annual yield. When a bond is issued, it has a coupon rate until it matures. This rate is related to the current interest rates. When a bond is sold or called before maturity, the value of the bond, not the coupon, will be affected by the current market interest rates. If current interest rates are higher than the coupon, the bond will sell below its face value. When interest rates are lower, they are sold at a premium or higher than face value. A bond's estimated annual yield is related to the current prevailing interest rates. A bond's yield is its annual interest (coupon) divided by its current market price.

Investment Listing, by Security Type

Description		Amount	Adjusted Cost	Market Value	Unrealized Gain (Loss)	Accrued Interest	Estimated Annual Income	% of Total Portfolio	9/30/2015 Annual Yield to Maturity	9/30/2014 Annual Yield to Maturity
Fixed Income Assets										
Government Bonds		\$3,461,696	\$ 3,461,696	\$ 3,475,377	\$ 13,681	\$ 12,563	\$ 37,900	24.0%	1.95%	1.79%
Securities		5,971,077	5,272,005	5,271,562	(443)	14,518	145,137	16.8%	2.75%	3.63%
Municipal Bonds		2,170,000	2,217,746	2,216,362	(1,384)	25,796	54,648	7.1%	2.20%	2.14%
Certificates of Deposit		256,463	256,463	256,463	-	638.50	1,282	0.8%	0.50%	0.30%
Local Government Investment										
Pool/Money Market		20,123,294	20,123,294	20,123,294	-	-	243,523	64.2%	1.21%	1.25%
Total Investments				\$31,343,058				100.0%		

Cash and Investments by Fund

Fund	Amount at 09/30/14	Amount at 09/30/15
General Fund	\$16,977,756	\$18,114,990
Major Road	549,382	(23,921)
Local Road	4,341,519	3,432,498
Downtown Development Authority	6,813	38,720
Drug Forfeiture	12,680	118,144
Community Development Block Grant	104,246	(16,082)
Special Assessment	(1,456)	1,512,370
Fire Station Bond	1,091,972	427,967
Water and Sewer	426,024	9,646,199
Motorpool	7,837,344	0
Escrow	292,829	230,196
Total Cash and Investments	\$31,639,108	\$33,490,324

* Amounts of cash/investments by fund are prior to year end closing and subject to change with necessary month-end adjustments.