

To: Benjamin I. Myers, City Manager

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

Date: October 13, 2016

RE: Investment Report 1st Quarter of Fiscal Year 2017

A summary of the investments for the City of Madison Heights as of September 30, 2016 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.

Investment Update:

Typically I would use this section to discuss the recent events at the Federal Open Market Committee (FOMC) and the US economy as a whole. However, this quarter I find it more relevant to discuss two events that are directly related to the City of Madison Heights and our investments and banking relationships with a brief summary of national economic events.

First, in May of 2015 we moved our business banking relationship from JP Morgan Chase to Talmer Bank and Trust based on Talmer's increased banking options, competitive pricing, and local presence within the City. As of November 10, 2016, Talmer will be completely converted to Chemical Bank due to a recent merger. We are working with our Talmer relationship manager to determine how this will affect the City fees and services. Assuming the fees are the same or lower, and services offered will be the same or more robust, we will plan to continue this relationship. If not we will be issuing a Request for Proposal for banking services.

Second, recently Wells Fargo Bank announced settlement agreements with the City of Los Angeles, the Consumer Financial Protection Bureau and the Office of the Comptroller of the Currency over the wrongful sales practices that resulted in many Wells Fargo retail bank clients receiving products and service they did not want. More recently, Wells Fargo Chairman and Chief Executive Officer John Stumpf addressed lawmakers at a public hearing, emphasizing that this behavior is inconsistent with Wells Fargo values and the culture they strive to live up to everyday. As noted in past investment reports the City has had a long standing relationship with Wells Fargo and use their advisory services for two main pieces of our investment portfolio 1) investment of the Parks Funds that is invested under a separate public act than regular funds and 2) treasury money market fixed income securities. I have followed up with our Wells Fargo representative and have been provided evidence that the City's accounts are held by Wells Fargo Advisors not Wells Fargo Retail Banks and that our investment accounts are unaffected by the events association with the settlement. I have included a report she provided but would also like to bring to your attention the representative's responsiveness to the City and the returns which have been above expectations. Enclosed with this report is the Wells Fargo performance summary through September 30, 2016. As you will see, they have solid investment returns for the City's general fund. Since May 18, 2010 the account has returned an annual rate of 1.0% net of fees. To compare, money market returns (as measured by 3-month Treasury Bills) for the same time period is only 0.1%. The account has investment earnings over this time period of \$339,734.

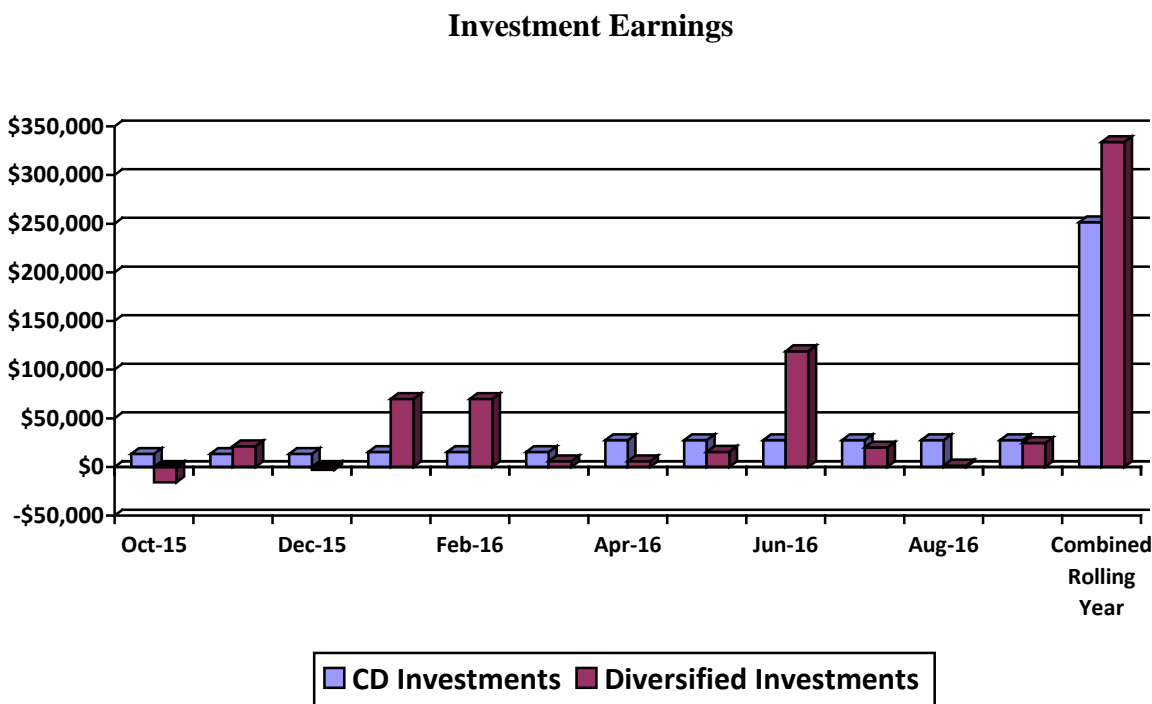
Economic Overview:

US Treasury yields saw modest declines in the month of September and investment grade fixed income performance was relatively neutral. The Barclays U.S. Aggregate index fell -0.1%. With the exception of

maturities 10 years and greater, yields fell across most maturities as the curve steepened slightly near its tail end. Most of the short-term maturities also fell when the Fed announced it would not raise rates in September.

Locally we continue to diversify investments and balance maturity dates with cash flow needs. 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 on the next page that compares our current returns with what our returns would be if we were invested 100% in Certificates of Deposit at the average rate of rate of 1.03% for 12 month investment during the October - September period (the current rate of a 12-month CD is 1.35%). Investing completely in CDs for the fiscal year to date would have yielded approximately \$251,415 in investment earnings; instead we earned \$333,896 through September by following our diversified investment plan.

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



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.

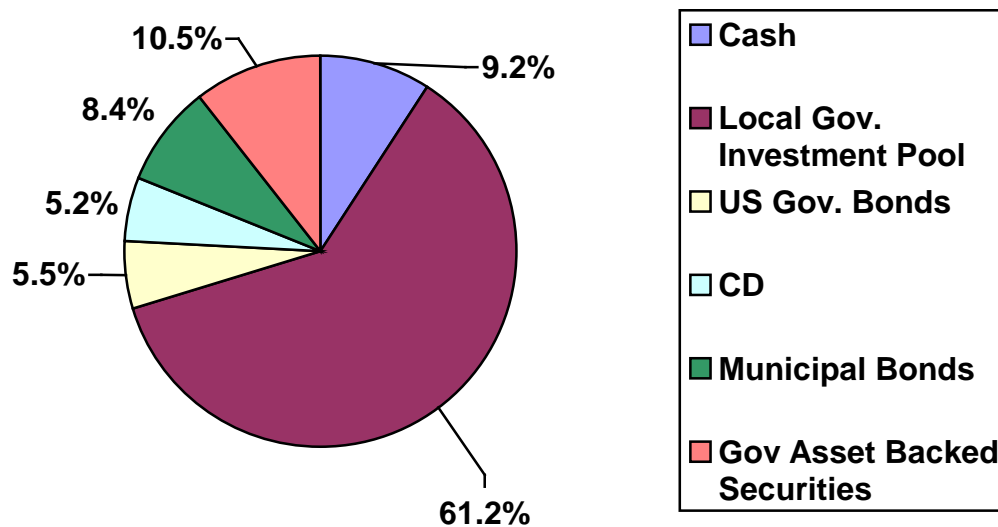
Quarter Investments:

As of September 30, 2016, 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	\$ 3,123,622
Total amount in Investments	<u>30,721,057</u>
	\$33,844,679

The chart on the following page details the diversification of the City investments as of September 30, 2016.

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, 2016. 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	9/30/2016 Annual Yield to Maturity	9/30/2015 Annual Yield to Maturity
Fixed Income Assets									
Government Bonds	\$1,865,000	\$ 1,865,391	\$ 1,869,961	\$ 4,570	\$ 2,746	\$ 22,071	6.1%	1.18%	1.88%
Securities	3,587,200	3,591,228	3,554,062	(37,166)	11,123	134,973	11.6%	3.80%	3.64%
Municipal Bonds	2,600,696	2,839,025	2,843,585	(4,560)	4,921	59,317	9.3%	1.90%	2.08%
Certificates of Deposit	1,748,000	1,748,000	1,752,412	-	4,412	27,444	67.4%	1.57%	0.50%
Local Government Investment Pool/Money Market	20,701,037	20,701,037	20,701,037	0	23,968	117,739	43.6%	1.21%	0.92%
Total Investments			\$30,721,057				100.0%		

Cash and Investments by Fund

Fund	Amount at 09/30/15	Amount at 09/30/16
General Fund	\$18,114,990	\$18,453,559
Major Road	(23,921)	(337,690)
Local Road	3,432,498	2,441,123
Downtown Development Authority	38,720	67,640
Drug Forfeiture	118,144	113,439
Community Development Block Grant	(16,082)	(25,612)
Special Assessment	1,512,370	1,372,998
Fire Station Bond	427,967	391,624
Water and Sewer	9,646,199	11,054,684
Escrow	230,196	312,914
Total Cash and Investments	\$33,490,324	\$33,844,679

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



What Does It Mean to Be a Fiduciary?

Fiduciary duty represents the highest degree of trust and confidence that the investment advisor will act in your best interest.

Investment Advisors are governed by the Investment Advisers Act of 1940 and applicable state securities laws, which govern conduct and disclosure requirements, creating a high legal standard referred to as "fiduciary" duty.

As a fiduciary, your investment advisor has the duty to:

- ❖ Make full and fair disclosure of all material facts, particularly where the advisor's interests may conflict with the client's
- ❖ Have a reasonable, independent basis for their investment advice
- ❖ Obtain best execution for clients' securities transactions where the advisor is in a position to direct brokerage transactions
- ❖ Ensure that investment advice is suitable to the client's objectives, needs and circumstances
- ❖ Refrain from effecting personal securities transactions inconsistent with client's interests
- ❖ Be loyal to clients

An advisor will be measured against a higher standard of conduct than a broker.

How do I enter into a fiduciary relationship with my Financial Advisor?

Only after you and the firm enter into a written agreement with Wells Fargo Advisors does the Financial Advisor become a fiduciary. In such agreements, the firm and your Financial Advisor explicitly acknowledge an advisory relationship and obligations to you. When acting as your investment advisor, we provide you with disclosure documents about our Advisory services.

What will be the role of your Financial Advisor?

In advisory programs, your Financial Advisor will act as a consultant, helping you monitor performance and adjust your portfolio on an ongoing basis.

Advisory accounts are not designed for excessively traded or inactive accounts and may not be suitable for all investors. Please carefully review the Wells Fargo Advisors advisory disclosure document for a full description of our services, including fees and expenses. The minimum account size for these programs is between \$25,000 and \$250,000.

Wells Fargo Advisors is the trade name used by two separate registered broker-dealers: Wells Fargo Advisors, LLC and Wells Fargo Advisors Financial Network, LLC, Members SIPC, non-bank affiliates of Wells Fargo & Company. First Clearing, LLC is a registered broker dealer and non-bank affiliate of Wells Fargo & Company. ©2015 Wells Fargo Advisors, LLC. All rights reserved. CAR# 0815-05084

Investment and insurance products:

NOT FDIC Insured	NO Bank Guarantee	MAY Lose Value
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Presented by: JULIE MOLL
248-433-8350
Total assets reported as of Sep 30, 2016

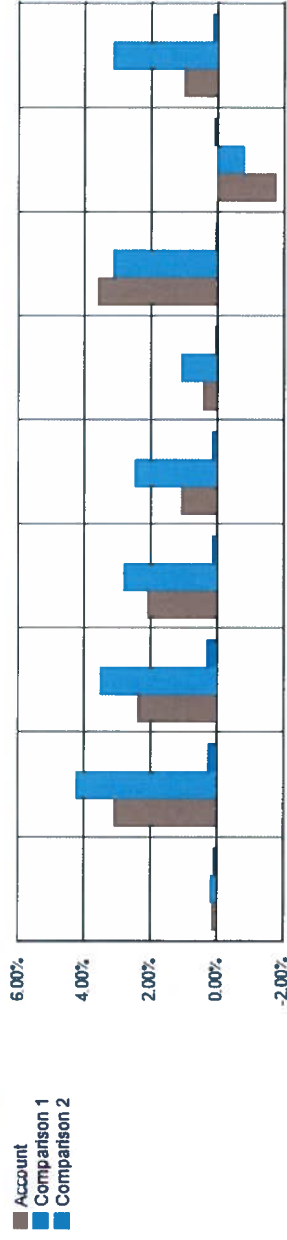
CITY OF MADISON HTS
XXXX8260
MASTERS/DELAWARE INVESTMENTS (FORMERLY MACQUARIE-TAXABLE
FIXED INT DURATION (AAA)

Summary of your account's investment growth

	MTD	QTD	YTD	Since 05/28/10
Beginning market value	\$5,692,052	\$5,694,644	\$5,532,441	\$4,348,847
Deposits minus withdrawals	\$0	\$0	\$0	\$1,013,126
Net invested capital	\$5,692,052	\$5,694,644	\$5,532,441	\$5,361,973
Investment results	\$9,655	\$7,063	\$169,266	\$339,734
Total assets ending market value	\$5,701,707	\$5,701,707	\$5,701,707	\$5,701,707
Your net money-weighted returns	0.2%	0.1%	3.1%	1.0%
Advisory assets ending market value				\$5,701,707
Non-advisory assets				\$0

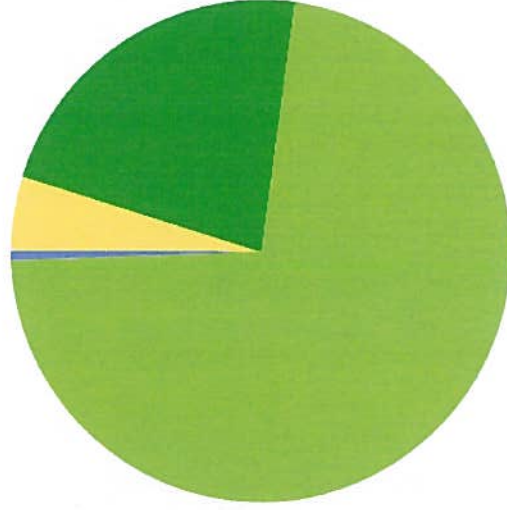
Net invested capital is your combined market value at the beginning of a stated time period plus deposits and minus withdrawals. Returns are annualized for the time periods greater than one year and are calculated after the deduction of program fees. Net money-weighted rates of return reflect your decisions to deposit or withdraw assets and should not be used to measure performance of an investment manager. Past performance is no guarantee of future results.

Total net time-weighted performance:



	QTD	YTD	1 Yr	3 Yrs	5 Yrs	2013	2014	2015	Since 05/28/10
Account (After Fees)	0.1%	3.1%	2.4%	2.1%	1.1%	0.4%	3.6%	1.1%	1.0%
Comparison 1	0.2%	4.2%	3.5%	2.8%	2.4%	1.1%	3.1%	1.1%	3.1%
Comparison 2	0.1%	0.2%	0.3%	0.1%	0.1%	0.1%	0.0%	0.1%	0.1%
Market indices									
S&P 500	3.9%	7.8%	15.4%	11.2%	16.4%	1.4%	13.7%	32.4%	13.9%
RUSSELL MIDCAP	4.5%	10.3%	14.2%	9.7%	16.7%	-2.4%	13.2%	34.8%	13.8%
RUSSELL 2000	9.0%	11.5%	15.5%	6.7%	15.8%	-4.4%	4.9%	38.8%	12.1%
MSCI EAFE NET	6.4%	1.7%	6.5%	0.5%	7.4%	-0.8%	-4.9%	22.8%	6.5%
MSCI EMERGING MKTS NET	9.0%	16.0%	16.8%	-0.6%	3.0%	-14.9%	-2.2%	-2.6%	2.3%
60S&P500/40SLAB	2.5%	7.1%	11.4%	8.4%	11.1%	1.3%	10.6%	17.6%	10.0%
BARCAP US AGGREGATE	0.5%	5.8%	5.2%	4.0%	3.1%	6.0%	6.0%	-2.0%	3.9%
BLOOMBERG COMMODITY	-3.9%	8.6%	-2.8%	-12.4%	-9.5%	-24.7%	-17.0%	-9.6%	-5.9%
ML 3M TBILL	0.1%	0.2%	0.3%	0.1%	0.1%	0.1%	0.0%	0.1%	0.1%
CPI ALL URBAN NSA	-0.1%	1.8%	1.2%	0.9%	1.2%	0.8%	0.8%	1.5%	1.6%

Total level asset allocation



	Market value	% of assets
Cash Alternative	\$275,208	4.8%
Short Term Fixed Income	\$1,266,835	22.2%
Intermediate Fixed Income	\$4,121,555	72.4%
High Yield Fixed Income	\$31,605	0.6%
Total assets	\$5,695,202	100.0%
Accrued interest	\$6,505	
Ending market value	\$5,701,707	
Total top holdings		%
FHLMC GOLD PASS THRU		7.6
FHLMC GOLD PASS THRU		6.4
US TREASURY		6.3
US TREASURY		6.0
US TREASURY		5.7
FNMA PASS THRU		4.9
BANK DEPOSIT SWEEP		4.8
US TREASURY		4.0
FNMA PASS THRU		3.8
FEDERAL NATL MTG ASSN		3.3



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MASTERS/DELAWARE INVESTMENTS (FORMERLY MACQUARIE-TAXABLE
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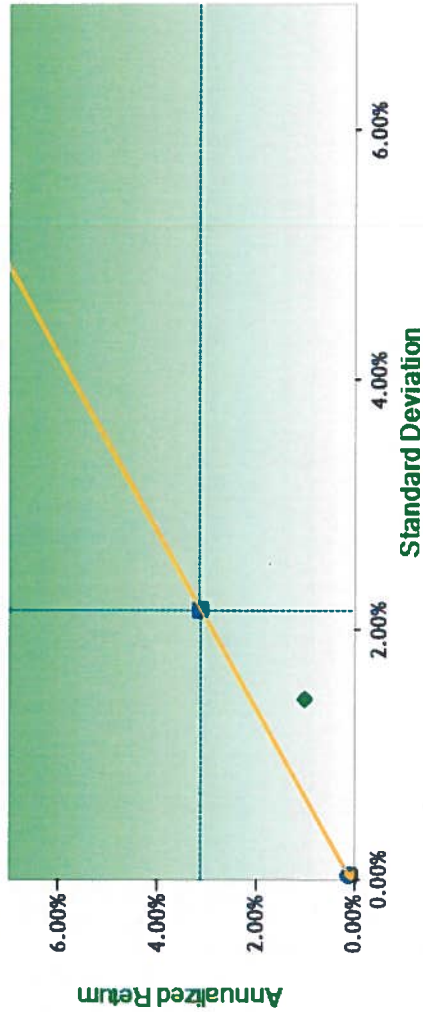
Returns are annualized for time periods greater than one year. Gross time-weighted returns are independent of the timing and magnitude of your cash flow decisions and are calculated before the deduction of program fees. Each return period is given an equal weighting, regardless of portfolio value. They are appropriate for measuring the performance of an investment manager. Past performance is no guarantee of future results.

Comparison History

Comparison 1:
5/28/2010 SLIGC is the BARCAP G/C INT index

Comparison 2:
5/28/2010 MLTBILL is the ML 3M TBILL index

Risk / Return analysis for your account since inception on May 28, 2010



	Annualized Return	Standard Deviation
Account (after fees)	1.01%	1.44%
Comparison 1	3.12%	2.16%
Comparison 2	0.11%	0.04%
Risk-free comparison	0.11%	0.04%

Comparison 1 (Benchmark) - is the BARCAP G/C INT index
Comparison 2 (Benchmark) - is the ML 3M TBILL index
Risk-free rate - The return of an investment with little, or no risk (US T-Bills)

Standard Deviation (Risk) - is a statistical measure of risk reflecting the extent to which rates of return for an asset or portfolio may vary from period to period and gauges the dispersion of monthly returns around the average return. The larger the standard deviation, the greater the range of possible returns and, therefore, the more risky the asset or portfolio.

Risk/Return Chart - Shows how well the manager has done managing the portfolio's risk (as measured by variability of returns) to earn its return. The line running from the risk-free rate (T-bill) to an appropriate market index is called the Capital Market Line. If the manager's risk/return plot is above the line, it earned a higher rate of return than expected given the level of risk taken. If the manager's risk/return plot is below the line, it earned a lower rate of return than expected given the level of risk taken.

Disclaimers

The report is not the official record of your account. However, it has been prepared to assist you with your investment planning and is for informational purposes only. Your Client Statements are the official record of your account. Therefore, if there are any discrepancies between this report and your Client Statement, you should rely on the Client Statement and call your local Branch Manager with any questions. Transactions requiring tax consideration should be reviewed carefully with your accountant or tax advisor. Unless otherwise indicated, market prices/values are the most recent closing prices available at the time of this report, and are subject to change. Prices may not reflect the value at which securities could be sold.



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Total assets reported as of Sep 30, 2016

CITY OF MADISON HTS
XXXX8260
MASTERS/DELAWARE INVESTMENTS (FORMERLY MACQUARIE-TAXABLE
FIXED INT DURATION (AAA)

The indices are presented to provide you with an understanding of their historic long-term performance, and are not presented to illustrate the performance of any security. Individual investors cannot directly purchase an index.

Indexes

BARCAP G/C INT (SLIGC)	The Barclays Capital Government/Credit Intermediate Bond Index is composed of all bonds that are investment grade (rated Baa or higher by Moody's or BBB or higher by S&P, if unrated by Moody's) with maturities between 1 and 9.99 years. Issues must have at least one year to maturity. Total return comprises price appreciation/depreciation and income as a percentage of the original investment. The index is rebalanced monthly by market capitalization.
BARCAP US AGGREGATE (SLAB)	The Barclays Capital U.S. Aggregate Bond Index covers the USD-denominated, investment-grade, fixed-rate, taxable bond market of SEC-registered securities. The index is composed of government and corporate securities, mortgage pass-through securities, and asset-backed securities. All securities are rated investment grade (Baa3/BBB-/BBB- or above) using the middle rating of Moody's, S&P, and Fitch, respectively and have a maturity greater than one year.
BLOOMBERG COMMODITY (DJAIG)	A broadly diversified index of commodity futures on 20 physical commodities, subdivided into energy, U.S. agriculture, livestock, precious metals, and industrial metals sectors. Commodity weights are derived in a manner that attempts to fairly represent the importance of a diversified group of commodities to the world economy. To that end, liquidity and product data is used to derive individual weights. To ensure diversification, there is a maximum weight limit of 33 percent and a minimum weight limit of two percent. The index family formerly known as the Dow Jones-UBS Commodity Index family has been rebranded as the Bloomberg Commodity Index Family as of July 1, 2014 and Bloomberg will replace Dow Jones & Company, Inc. as the index administrator.
CPI ALL URBAN NSA (CPI)	The CPI All Urban Consumers NSA Index (CPI) is a non-seasonally adjusted measure of the average change over time in the prices paid by urban consumers for a market basket of consumer goods and services. The CPI is calculated by the Bureau of Labor Statistics and published monthly. Due to a late publishing date each month, the index number provided always includes an estimated return for the prior month.
ML 3M TBILL (MLTBILL)	The Merrill Lynch U.S. 3-Month Treasury Bill Index is comprised of a single issue purchased at the beginning of the month and held for a full month. At the end of the month that issue is sold and rolled into a weekly selected issue. The issue selected at each month-end-rebalancing is the outstanding Treasury Bill that matures closest to, but not beyond, three months from the rebalancing date.
MSCI EAFE NET (MSEAFANR)	The MSCI EAFE (Europe, Australasia, Far East) Net Returns Index is a free float-adjusted market capitalization index that is designed to measure the equity market performance of developed markets, excluding the US & Canada. The Net Total Return methodology employs a standard withholding tax by applying the maximum rate of the company's country of incorporation applicable to institutional investors.
MSCI EMERGING MKTS NET (MSCIEMNR)	The MSCI Emerging Markets Net Returns index is a free float-adjusted market capitalization index that is designed to measure equity market performance of emerging markets. The Net Total Return methodology employs a standard withholding tax by applying the maximum rate of the company's country of incorporation applicable to institutional investors.
RUSSELL 2000 (FR2000)	The Russell 2000 Index consists of the smallest 2,000 securities in the Frank Russell 3000 Index. This is the Russell Company's small-capitalization index that is widely regarded in the industry as the premier measure of small-capitalization stocks.
RUSSELL MIDCAP (FRMIDCAP)	The Russell Midcap Index measures the performance of the 800 smallest companies by market capitalization in the Russell 1000 Index. This mid-cap index represents approximately 31% of the Russell 1000 Index total market capitalization.
S&P 500 (S&P500)	The S&P 500 Index consists of 500 stocks chosen for market size, liquidity, and industry group representation. It is a market-value weighted index (stock price times number of shares outstanding) with each stock's weight in the index proportionate to its market value. The S&P 500 is one of the most widely-used benchmarks of U.S. equity performance. Performance includes reinvestment of dividends.

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