

To: Benjamin I. Myers, City Manager

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

Date: July 31, 2015

RE: Investment Report 4th Quarter of Fiscal Year 2015

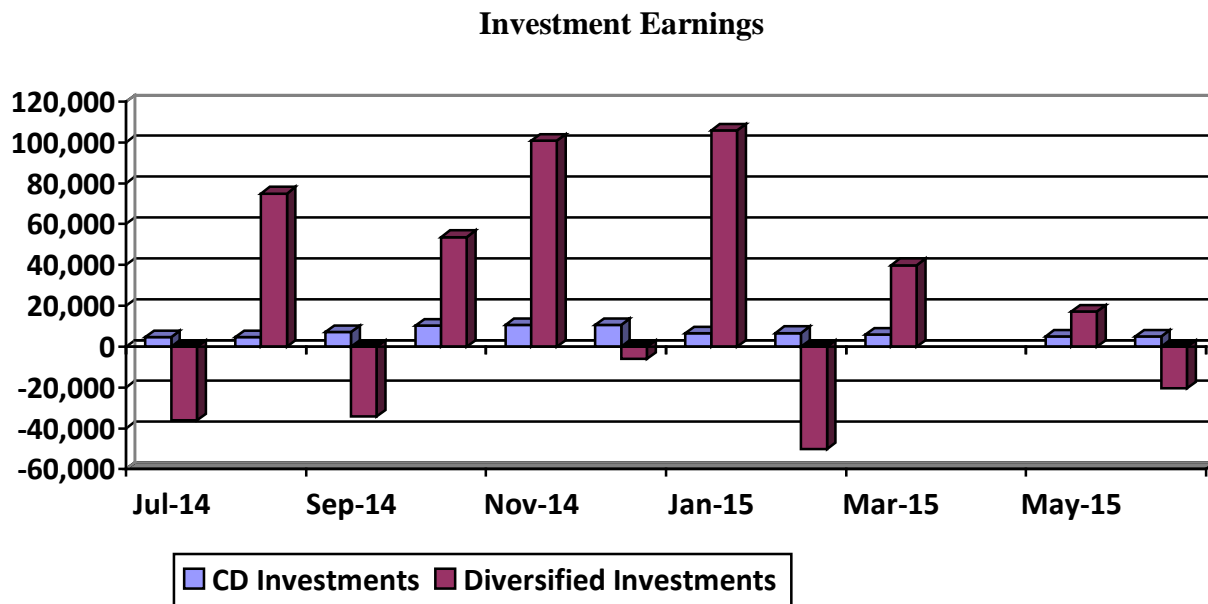
A summary of the investments for the City of Madison Heights as of June 30, 2015 is included in this memo. The requirements of the City of Madison Heights Investment Policy and P.A. 20 of 1943, as amended, govern the investments held by the City.

Interest Rate Overview:

At the June meeting of the Federal Open Market Committee (FOMC) staff reported that economic growth in the second half was projected to be a little lower than in the projection prepared for the April meeting, largely reflecting a small downward revision to the forecast for household spending. The staff's medium-term projection for real GDP growth was essentially unrevised from the previous forecast. The staff's forecast for inflation in the near term was little changed, and it was unrevised over the medium term.

In July 2015, Federal Reserve Chair Janet Yellen offered a few insights about the timing of the first rate hike in her semi-annual testimony to Congress. If the economy keeps improving in line with the Federal Reserve's expectations, she indicated that a rate hike in 2015 would be appropriate. If the first rate hike is delayed, the Federal Reserve would have to be more aggressive in future rate hikes. Yellen suggested that a benefit of a 2015 rate hike would be that it would make it easier to raise rates gradually. It's clear that the first rate hike will just be the start of a long road back to more normal interest rates. Unlike the last time the Federal Reserve increased rates when a rate hike occurred at every FOMC meeting, this time there will likely be several meetings of rate-hike pauses.

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 0.30% for 12-17 month investment during the April - June period (the average rate of return for CDs). Investing completely in CDs for the fiscal year to date would have yielded approximately \$55,292 in investment earnings; instead we earned \$264,587 through June by following our diversified investment plan.



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.

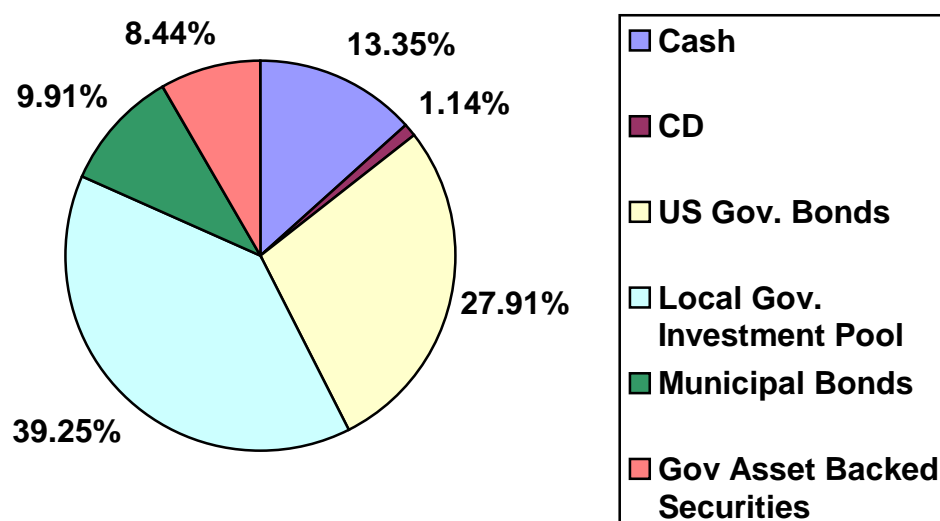
Quarter Investments:

As of June 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	\$ 2,471,012
Total amount in Investments	<u>19,900,644</u>
	\$22,371,656

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

Diversification – Fourth Quarter of Fiscal Year 2015
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 June 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)	Annual Yield to Maturity	Accrued Interest	Estimated Annual Income	% of Total Portfolio
Fixed Income Assets								
Government Bonds	\$ 6,265,100	\$ 6,277,345	\$ 6,244,247	\$ (33,098)	1.95%	\$ 17,448	\$ 68,624	27.91%
Securities	2,487,192	1,906,912	1,888,498	(18,414)	3.64%	9,124	111,194	8.44%
Municipal Bonds	2,170,000	2,224,274	2,215,969	(8,306)	2.20%	12,134	54,648	9.91%
Flagstar Certificates of Deposit	255,505	255,505	255,505	-	0.50%	638.50	1,277	1.14%
Local Government Investment Pool/Money Market	11,767,438	11,767,438	11,767,438	-	1.15%	-	70,289	52.60%
Total Investments			\$22,371,656					100.0%

Cash and Investments by Fund

Fund	Amount at 06/30/15
General Fund	\$7,200,506
Major Road	515,886
Local Road	3,389,337
Downtown Development Authority	(11,657)
Drug Forfeiture	116,924
Community Development Block Grant	(9,027)
Special Assessment	1,279,127
Fire Station Bond	77,142
Water and Sewer	9,437,302
Motorpool	76,919
Escrow	299,197
Total Cash and Investments	\$22,371,656

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