



CITY OF MADISON HEIGHTS
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FINANCE/TREASURER DEPARTMENT

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MEMORANDUM

DATE: January 21, 2022
TO: Mayor and City Council
Melissa Marsh, City Manager
FROM: Linda A. Kunath, Finance Director/Treasurer
SUBJECT: Investment Report 2nd Quarter Fiscal Year 2022

In compliance with the City of Madison Heights Investment Policy and P.A. 20 of 1945, as amended, the following summary of investments as of December 31, 2021, for the City of Madison Heights, is being presented in this memorandum.

Investment Overview

Risks and uncertainties continue into 2022. The pandemic is not over, as noted by the high transmission of the Omicron variant of COVID-19. Inflation is not as transitory as many had expected and the Fed's are preparing to raise rates. The United States finished December at 7.0%, according to the year-over-year change in the Consumer Price Index, which is a level not seen since 1982, 40 years ago. Supply chain bottlenecks continue to contribute to inflation. Slower delivery times on goods continue to create bottleneck on supply chains along with a shortage of truck drivers contributing to the backlog of containership at sea. These issues continue driving price increases across the manufacturing industry and resulting in persistent inflationary pressures.

The Federal Open Market Committee (FOMC), led by the Federal Reserve Board of Governors Chair Jerome Powell, made clear its intent to let inflation run somewhat above target to achieve a quicker labor market recovery. The FOMC is scheduled to meet late January and the Fed's will be considering US and international economic conditions, impact of fiscal stimulus and growth of inflation. October unemployment rate decreased to 4.6%, then to 3.9% in December. Labor participation rate remained sluggish at 61.9% while average hourly earnings rose by 0.6% in December. November Personal Consumption Expenditures (PCE) measure registered 5.7% increase year over year, 4.7% excluding volatile food and energy. Increased prices on durable goods have far exceeded increased prices on services. The Fed view is shifting to persistent inflation from transitory, according to Plante Moran wealth management.

Bakertilly investment services noted in their recent Interest rate update publication that minutes from the Fed's December meeting signaled tighter monetary policy given higher inflation, wage gains (+4.7%) and full employment (3.9% unemployment rate). There is a 78% chance that the Fed hike rates by 0.25% at their March meeting. The market is currently pricing in 3-4 hikes during 2022. The Fed is also expected to continue to shrink its balance sheet by reducing its monthly bond purchase.

The 10-year U.S. Treasury note rate was 1.52% in December 2021 and is forecasted to decrease to 1.18% by May 2022. The daily 5-year Treasury yield rose to 1.590% currently from 1.056% on 9/30/21. According to the Bureau of Labor Statistics (BLS), the Consumer Price Index is projected to average 7.0% the first quarter of 2022 before decelerating to 3.8% by the end of 2022.

The City of Madison Heights's investments continue to be diversified and maturity dates are balanced with cash flow needs. Following a long term view for fixed rate investments, a higher rate of return is realized by holding fixed rate vehicles, such as bonds and treasuries, until either the call date or maturity. As stated 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. 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 on the following page details the amounts at December 31, 2021. 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.

City of Madison Heights		Investment Listing, by Security Type							
Investment Analysis									
Qtr End: 12/31/2021									
Description	Amount	Adjusted Cost	Market Value	Unrealized Gain (Loss)	Accrued Interest	Estimated Annual Income	% of Total Portfolio	12/31/2021 Annual Yield to Maturity	12/31/2020 Annual Yield to Maturity
Fixed Income Assets									
Government Bonds	\$ 3,362,648	\$ 3,361,265	\$ 3,353,755	\$ (7,510)	\$ 9,059	\$ 33,563	9.5%	1.00%	1.08%
Government Asset Backed/CMO Securities	5,690,668	3,666,958	3,554,377	(112,581)	102,208	93,841	10.0%	1.86%	3.00%
Municipal Bonds	3,000,000	3,105,327	3,061,714	(43,613)	166,113	110,742	8.6%	3.62%	3.29%
Certificates of Deposit	3,829,876	3,829,332	3,828,383	(949)	70,921	44,071	10.8%	0.64%	1.20%
Local Government Investment Pool/Money Market	20,256,665	20,256,665	20,256,665	-	15,128	38,666	57.1%	0.17%	0.96%
Total Investments			\$34,054,894						
Cash and Equivalents			1,396,163						
Total Cash and Investments			\$35,451,057						

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).

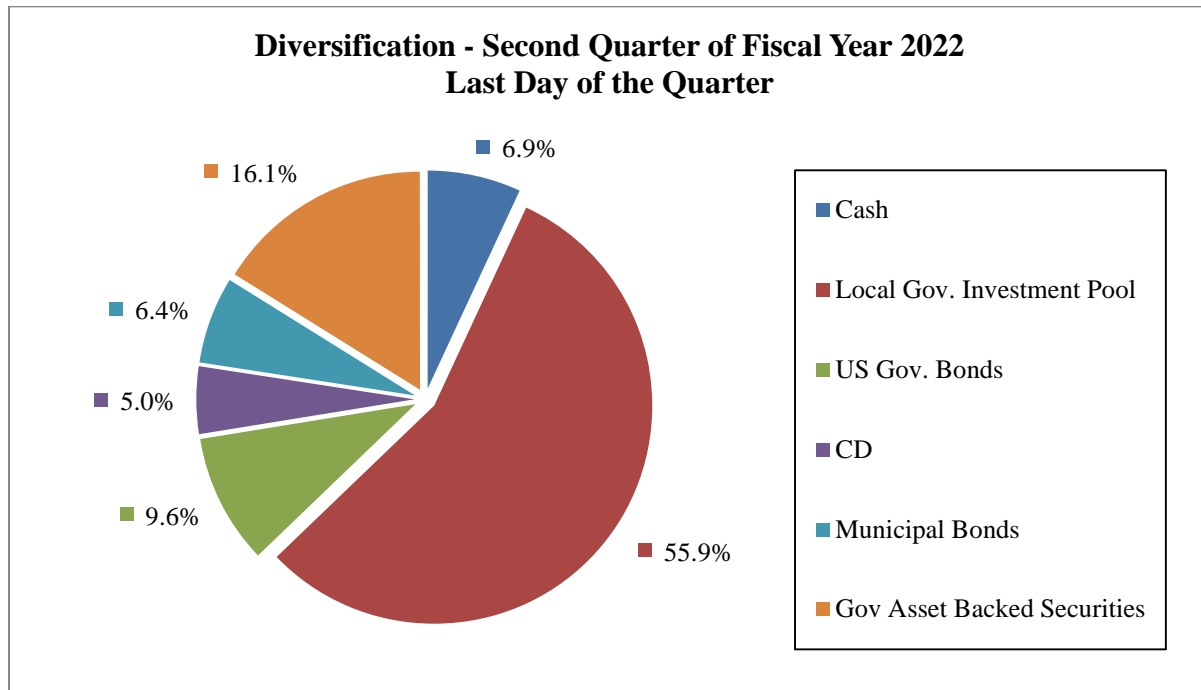
Concentration of risk occurs when the municipality is heavily invested in one issuer. The city's largest issuer is the Local Government Investment Pool managed by Oakland County. This pool is diversified with other County investments.

Quarter Investments

As of December 31, 2021, 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	\$ 1,271,413
Total amount in the investment accounts	<u>34,179,644</u>
	\$ 35,451,057

The following chart details the diversification of City investments as of December 31, 2021.



Fund	Amount at 12/31/2021	Amount at 12/31/2020
General Fund	\$24,693,091	\$19,505,632
Major Road	1,729,975	876,825
Local Road	2,994,635	3,027,183
Downtown Development Authority	270,027	233,895
Drug Forfeiture	210,964	267,581
Community Development Block Grant	(8,781)	(32,606)
Special Assessment	262,385	558,350
Fire Station Bond	461,396	424,308
Water and Sewer	4,580,575	7,369,682
Escrow	256,790	80,490
Total Cash and Investments	\$35,451,057	\$32,311,340

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