



CITY OF MADISON HEIGHTS
300 WEST 13 MILE ROAD, MADISON HEIGHTS, MI 48071

FINANCE/TREASURER DEPARTMENT

Linda A. Kunath,
Finance Director/Treasurer

(248) 837-2639
LindaKunath@Madison-Heights.org

MEMORANDUM

DATE: July 18, 2022
TO: Mayor and City Council
Melissa Marsh, City Manager
FROM: Linda A. Kunath, Finance Director/Treasurer
SUBJECT: Investment Report 4th 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 June 30, 2022, for the City of Madison Heights, is being presented in this memorandum.

Investment Overview

The annual inflation rate in the United States accelerated to 9.1% in June, 2022, the highest since November, 1981, which exceeded the market forecast of 8.8%. The Consumers Price Index (CPI) increased 1.3% in June, which was higher than the month-over-month expected increase of 1.1%. CPI data reflects sector increases in energy, gasoline, food, and airline fares, which are the most since the early 1980's. Before the Russian invasion of Ukraine, the rise in prices was related to supply chain problems, which have subsided with consumer spending rotating from goods to services and businesses finding ways around the shortages. March increases were mainly due to higher energy costs, however this past quarter, April to June, saw much higher core inflation.

According to Raymond James Weekly Primer report, these inflation increases are projected to pressure the Federal Reserve Board to hike interest rates at least 75 basis points up to 100 basis points at their end of July meeting. The interest rate hikes are likely to be large and persistent until the Federal Reserve observes a measurable slowdown in the economy, according to Kiplinger's Economic Outlook. The current forecast includes up to two interest hikes this year and three more in 2023.

The current period of increasing inflation, construction slowdowns, the not fully recovered auto industry due to semiconductor shortages, and backlog of manufacturing, is forecasting an inflation-driven rather than credit-driven recession, according to Morgan Stanley Wealth Management report. A recession is forecasted to likely happen in the next 12 months, a mild recession to begin late 2022 according to Bloomberg or starting mid-2023 is projected by Wells Fargo. Kiplinger reports the slowing economy will take the edge off the shortage of workers and the overheated housing and motor vehicle markets, which could be good for bringing inflation under control.

The 10-year U.S. Treasury note rate of 2.93% is higher compared to 2.38% at March quarter end. The daily 5-year Treasury yield rose again this quarter to 3.050%, compared to 2.560% at beginning of the quarter. CD rates rose since the beginning of the quarter for 1-year term to 3.000% from 1.250% and for 5-year term rates to 3.450% from 2.650%. 30-year municipal bonds rose from 2.546% to 2.993% during the quarter. Energy prices increased 32%, namely gasoline and fuel oil. Food prices jumped 8.8%, most since May, 1981. Excluding volatile energy and food categories, the CPI rose 6.5%, the most in 40 years.

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 June 30, 2022. 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 Analysis		Investment Listing, by Security Type										
											6/30/2022	6/30/2021
Description	Amount	Adjusted Cost	Market Value	Unrealized Gain (Loss)	Accrued Interest	Estimated Annual Income	% of Total Portfolio	6/30/2022 Annual Yield to Maturity	6/30/2021 Annual Yield to Maturity			
Fixed Income Assets												
Government Bonds	\$ 3,488,986	\$ 3,486,268	\$ 3,436,430	\$ (49,838)	\$ 11,664	\$ 71,879	12.0%	2.09%	0.92%			
Government Asset Backed/CMO Securities	6,164,637	4,048,973	3,748,076	(300,897)	154,239	84,648	13.1%	2.72%	2.89%			
Municipal Bonds	1,620,000	1,662,072	1,619,044	(43,028)	76,803	51,202	5.7%	3.16%	3.29%			
Certificates of Deposit	4,558,494	4,546,364	4,541,787	(4,577)	16,350	13,290	15.9%	0.69%	0.63%			
Local Government Investment Pool/Money Market	9,789,920	9,789,920	9,789,920	-	15,128	73,177	34.3%	0.17%	0.42%			
Total Investments			\$23,135,257									
Cash and Equivalents			5,393,070									
Total Cash and Investments			\$28,528,327									

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).

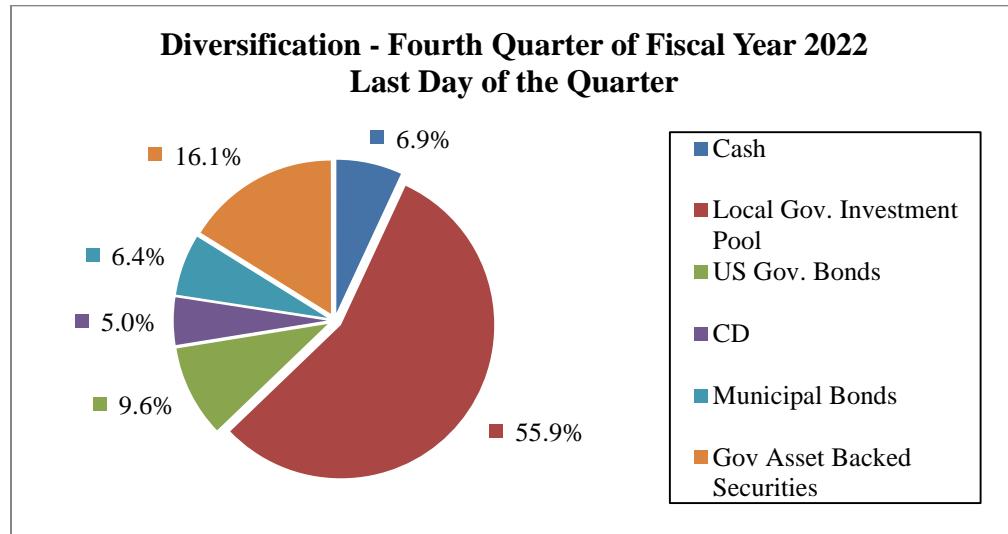
Concentration of risk occurs when the municipality is heavily invested in one issuer. The city's largest issuer is the Local Government Investment Pool managed by Oakland County. This pool is diversified with other County investments.

Quarter Investments

As of June 30, 2022, 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	\$ 5,246,417
Total amount in the investment accounts	<u>23,281,910</u>
	\$ 28,528,327

The following chart details the diversification of City investments as of June 30, 2022.



<u>Cash and Investment by Fund</u>		
Fund	Amount at 06/30/2022	Amount at 6/30/2021
General Fund	\$18,051,517	\$12,949,685
Major Road	2,387,582	1,037,211
Local Road	3,582,971	2,521,847
Downtown Development Authority	288,832	236,528
Drug Forfeiture	164,613	235,815
Community Development Block Grant	(8,296)	(21,563)
Special Assessment	260,315	267,223
Fire Station Bond	27,908	(6,719)
Water and Sewer	3,495,933	6,497,199
Escrow	276,952	272,030
Total Cash and Investments	\$28,528,327	\$23,989,256

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