



CITY OF MADISON HEIGHTS
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FINANCE/TREASURER DEPARTMENT

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MEMORANDUM

DATE: January 23, 2023
TO: Mayor and City Council
Melissa Marsh, City Manager
FROM: Linda A. Kunath, Finance Director/Treasurer
SUBJECT: Investment Report 2nd Quarter Fiscal Year 2023

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, 2022, for the City of Madison Heights, is being presented in this memorandum.

Investment Overview

The scale, scope, and speed of COVID-related stimulus from the Federal Reserve and Congress are tied to the United States stock market rebound from March 2020 lows to all-time highs for both the Nasdaq Composite and S&P 500, according to Morgan Stanley Investment Outlook. This revaluation in 2022 was affected by the 42-year high inflationary increase for food, energy, labor, housing, auto supplies and semiconductors. The Federal Reserve continued interest rate hikes last year, and events in Ukraine altered geopolitical risks with potential for implications for inflation, currencies, globalization, defense spending, cybersecurity and efforts around decarbonization and climate change. Nominal growth in 2023 is forecasted at approximately 2.1% by the fourth quarter, with monetary policy tightening.

The Federal Open Market Committee (FOMC) continued to raise rates this past quarter, which included 75 basis points in September and November and 50 basis points in December. Forbes predicts rate hikes will continue to rise in 2023 and peak around 4.9%. The strong labor market is said to be driving interest rate hikes. The Federal Reserve is looking for price stability and a slowing economy to determine when to reduce or stop rate hikes.

The economic outlook for the United States in 2023 is for persistent inflation with a mild and brief recession. Expectations for jobless rate are to peak at historically low amount of 4.5 percent, due to expected labor shortages despite the downturn. The Gross Domestic Product (GDP) growth year-over-year is predicted to slow to .2 percent in 2023, then rebound to 1.7 percent in 2024, according to the Conference Board on US Economic Outlook.

The 10-year U.S. Treasury note rate of 3.78% is lower compared to 3.89% at September quarter end. The daily 5-year Treasury yield rose again this quarter to 4.14%, compared to 3.05% at beginning of the quarter. CD rates rose since the beginning of the quarter for 1-year term to 4.60% from 4.10% and for 5-year term rates lowered to 3.90% from 4.50%. 30-year municipal bonds lowered to 3.398% from 3.779% during the quarter. The food index rose 10.4% for year and Energy prices rose 7.3% over the prior year, which included a 1.5% drop in gasoline. The Consumers Price Index for all items year over year rose 6.5%.

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, 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 Listing, by Security Type							
Investment Analysis									
Qtr End: 12/31/2022									
Description	Amount	Adjusted Cost	Market Value	Unrealized Gain (Loss)	Accrued Interest	Estimated Annual Income	% of Total Portfolio	12/31/2022 Annual Yield to Maturity	12/31/2021 Annual Yield to Maturity
Fixed Income Assets									
Government Bonds	\$ 3,417,658	\$ 3,412,293	\$ 3,288,548	\$ (123,745)	\$ 17,574	\$ 85,516	9.8%	2.60%	1.00%
Government Asset Backed/CMO Securities	9,672,352	7,633,465	7,249,159	(384,306)	48,228	87,306	21.7%	2.75%	1.86%
Municipal Bonds	605,000	618,985	592,566	(26,419)	29,836	19,890	1.8%	3.36%	3.62%
Certificates of Deposit	1,972,505	1,923,043	1,936,756	13,713	-	11,621	5.8%	2.13%	0.64%
Local Government Investment Pool/Money Market	19,892,961	19,892,961	19,892,961	-	30,014	109,240	59.5%	0.82%	0.17%
Total Investments			\$32,959,990						
Cash and Equivalents			449,054						
Total Cash and Investments			\$33,409,044						

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).

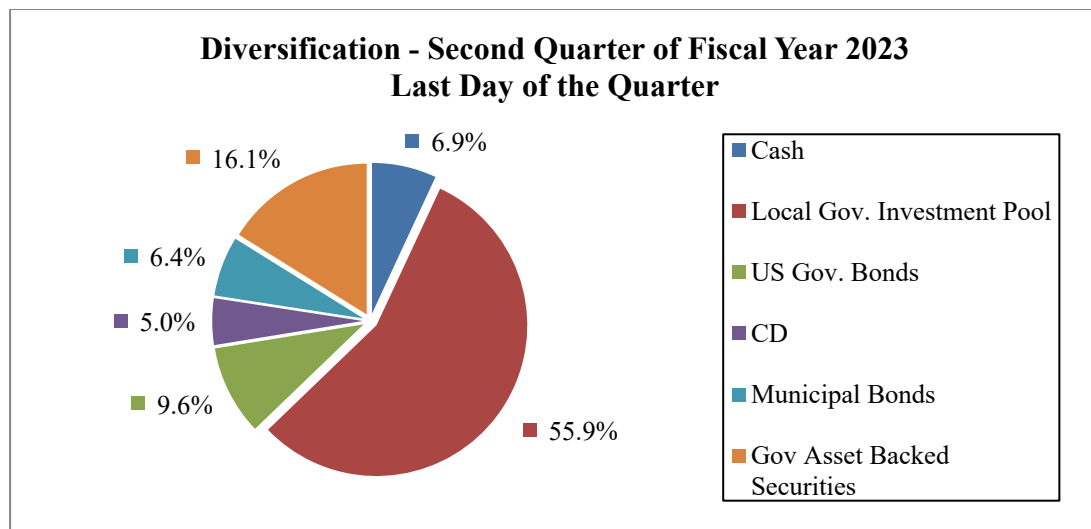
Concentration of risk occurs when the municipality is heavily invested in one issuer. The city's largest issuer is the Local Government Investment Pool managed by Oakland County. This pool is diversified with other County investments.

Quarter Investments

As of December 31, 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	\$ 173,177
Total amount in the investment accounts	<u>33,235,867</u>
	\$ 33,409,044

The following chart details the diversification of City investments as of December 31, 2022.



Cash and Investment by Fund

Fund	Amount at 12/31/2022	Amount at 12/31/2021
General Fund	\$21,815,997	\$24,693,091
Major Road	2,446,677	1,729,975
Local Road	4,002,332	2,994,635
Downtown Development Authority	362,979	270,027
Drug Forfeiture	180,975	210,964
Community Development Block Grant	(24,748)	(8,781)
Special Assessment	259,896	262,385
Municipal Building Bond	174,180	461,396
Fire Station Bond	443,780	461,396
Water and Sewer	3,414,689	4,580,575
Escrow	332,287	256,790
Total Cash and Investments	\$33,409,044	\$35,912,453

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