TREASURY OVERSIGHT COMMITTEE MINUTES
January 25, 2013 at 10 a.m.
Room 316, City Hall

1. Call to Order and Roll Call

The meeting was called to order at 10 a.m. by Ben Rosenfield, Controller. The following Committee members were present: Joe Grazioli, Peter Goldstein and Todd Rydstrom. James Whitaker, Property Tax Manager for the Controller's Office, was introduced. He will fill the position previously held by Leo Levenson.

2. Discussion and Action to Approve Minutes

The minutes from the meeting on October 19, 2012 were unanimously approved.
There was no public comment.

3. Review of the Treasurer's Recent Investment Performance

Michelle Durgy, Chief Investment Officer, reviewed the following topics: 1) the economic review and outlook; 2) market overview; 3) Pooled Fund review; 4) liquidity strategy; and 5) the December 2012 monthly report.

Economic Review and Outlook: Ms. Durgy reviewed world events that had influence on the financial markets in 2012. The situations in Europe weighed heavily on the markets. The Greek debt was restructured, Spain came into focus and Greece voted "yes" to the European Union. Whenever there is a bit of instability in other nations, it causes investors to move to quality. Investors moved from the European bond holdings to U.S. Treasuries. This forced yields lower. Mario Draghi's (the European Central Bank President) remarks reflected his willingness to do whatever is necessary to help the struggling European economies so they're not paying such high rates. At the end of the year, Mr. Draghi announced the monetary transactions program in which unlimited government debt would be purchased in order to improve the economic picture. This action has calmed the markets.

Domestically, the Facebook IPO (initial public offering), iPhone sales, iPad Mini, Sandy and the elections had the results of a little less liquidity in the market. The fiscal cliff picture resulted in uncertainty in the market. Investors fled toward Treasuries. Any benefits from the OMT deal (outright monetary transactions) were offset by the fiscal cliff. In late 2014, the Federal Open Market Committee will likely raise rates, if economic conditions continue to improve. In the third quarter, the Fed began making open market purchases of treasuries, which lowers long term treasury rates. Operation Twist and Operation Twist Extended sell short term treasuries to shore up cash to buy long-end treasuries. The Federal Reserve continues to purchase $85 billion dollars mortgage backed securities and treasuries per month. The effects of the QE3 and Operation Twist caused higher overnight yields of about 23 basis points per year in 2012.

In October 2012, the Fed said it would probably keep rates low. In December 2012, the Fed provided information regarding a change in guidance for the period of near-zero Fed funds rate. The guidance specified exceptionally low rates for Fed funds until, at least: 1) unemployment is less than or equal to 6.5%; 2) future inflation (1-2 years forward) is equal to or greater than 2.5%; and 3) long term inflation expectations remain well anchored. The 2.5% is very important because the inflation target used to be 2%. Previous language regarding guidance for the period of near-zero Fed funds rate was "likely to be warranted at least through mid-2015".

The key economic data is positive as compared to last year at the same time. The economic outlook continues to improve. The job market is looking better. In the recession, 8.78 million jobs were lost. Now, 4.78 million jobs have been added. Jobless claims have also dropped. There is a rebound in the housing market. Gas prices are lower. There is greater consumer spending. However, the payroll tax implementation in January 2013 will constrain growth. The 10-Year U.S. Treasury Note yield has shown small upward momentum because of the positive economic indicators.

The year-over-year Treasury yield curve (1/18/2012 – 1/18/2013) shows no movement. In terms of the 5-year U.S. Treasury volatility, more volatility creates greater opportunities. Ms. Durgy also reviewed yields, short-term interest rates and the changing investment landscape given the expiration of the Transaction Account Guarantee (TAG) program on December 31, 2012.
Treasurer Cisneros asked the Committee whether they found the background information about market activity useful. He noted that sometimes pool participants simply want to know why rates are so low and when they will go up. The background information provided by Ms. Durgy provides the context to illustrate the point that rates won't be going up anytime soon. Ms. Marx noted that the information is very positive in many ways. Although a number of things are going up, the Feds are saying that for the next 1-2 years, don't look for any real interest rate increases. The Committee members responded that the briefings are helpful because of the context provided as well as the subject matter. The briefings also provide "reality" so there is an understanding of how well the portfolio is performing.

County pooled fund statistics, as of November 2012, were discussed. Ms. Durgy noted that when the Committee next meets in April, the "dot" on the "weighted average maturity (in days)" will have moved to the left of the chart. The reason for this expected movement is that the City is shortening its duration. This means the "dot" will also move down and "be closer to the position of Los Angeles (on the chart". Because of the shorter duration, there will be more money invested on the shorter end yield curve.

Relative to other counties, Ms. Durgy noted that in the past, CCSF had about $4 billion in pooled assets but – to date – the assets under management for CCSF is currently at $5.9 billion. This is an all-time record for the City.

Ms. Durgy reviewed investment fund participants as of January 17^{th}. The PUC represents 29% of the fund, followed by a variety of other City agencies. There was also discussion about the City's portfolio comparison of December 31, 2011 and December 31, 2012. Key points included the increase in U.S. Treasuries from 9% in 2011 to 18.2 % in 2012 because of the relative value in Treasuries over Federal Agency securities in 2012. Federal agencies decreased slightly from 69.8% to 68.5%. The final maturities in the Temporary Liquidity Guarantee Program (TLGP), which in 2011, made up as much as 12.1% of the Pool, rolled off on December 31, 2012 when the program expired. Some of the monies from that program were moved into municipal bonds and certificates of deposit (CD). The allocation for negotiable CDs has been increased by $13 million.
Short-Term Cash: Surplus cash previously invested under the TAG program will be moved into other securities at the end of the year, due to the program's expiration. Ms. Durgy expects to invest the money in money market accounts, repurchase agreements, and commercial paper/Certificates of Deposits. The goal is to have about 5% of the portfolio in liquid assets.

There was no public comment.

4. Review of Pooled Cash Balance

The review of pooled cash balances will be presented by James Whitaker, Property Tax Manager for the Controller's Office, for the next few months. Updated cash balance information will be provided at the April 2013 meeting.

There was no public comment.

5. Public Comment

There was no public comment.

The meeting adjourned at 10:45 a.m.