

CITY OF OAKLAND
AGENDA REPORT

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OFFICE OF THE CITY CLERK
OAKLAND
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TO: Office of the City Administrator
ATTN: Dan Lindheim
FROM: Finance and Management Agency
DATE: December 2, 2008

RE: Cash Management Report for the Quarter Ended September 30, 2008

SUMMARY

The Investment Policy for the City of Oakland (the "City") and the Redevelopment Agency (the "Agency") 2008-2009 requires the City to submit a quarterly investment report to the City Council. The report includes the following information: type of investment, issuer, date of maturity, and par and dollar amount invested.

In accordance with the Investment Policy for the City and the Agency, the attached Cash Management Report provides information on the investments of the City's Operating Fund and the Agency's Operating Fund for the quarter ended September 30, 2008. The report summarizes the characteristics of the investment portfolios, along with attachments showing the Funds' monthly transactions and holdings for the quarter ended September 30, 2008.

During the October 14, 2008 Finance and Management Committee meeting, staff was requested to provide the similarities and differences between the City of Oakland Investment Policy and the California State Government Code, Section 53601. Please refer to the table under "Key Issues and Impacts" highlighting this comparison..

This report is presented for Council's information and review only and requires no Council action.

FISCAL IMPACTS

This is an informational report. There is no fiscal impact.

BACKGROUND

This report presents information regarding the portfolios' composition including safety, creditworthiness, liquidity, and diversity. As of September 30, 2008, the portfolios are in compliance with the Investment Policy of the City for Fiscal Year 2008-2009. The portfolios' credit quality remains high and well within Investment Policy parameters. Liquidity remains sufficient to meet projected cash flow needs. Provided below are each portfolio's current market value and yield as of September 30, 2008, as well as comparisons to

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other market benchmarks. This report confirms that no leverage was utilized nor derivatives held during the reporting period. Also included are reviews of key economic factors, which may affect the portfolios and potential investment results.

KEY ISSUES AND IMPACTS

In addition to the permitted investments by the California State Government Code No. 53601, the City's Investment Policy includes the following:

- December 16, 1988 City Council approved Ordinance No. 11062 C.M.S., which restricted the City's investment in U.S. Government Treasuries. However on October 21, 2008, City Council passed Resolution No. 81629 C.M.S. that allows the City to invest in U.S. Treasuries for a period of 60 days.
- The City of Oakland has a preference to invest in companies that promote the use and production of renewable energy resources and any other socially responsible investments, subject to the prudent investment standard.
- February 17, 1998 City Council adopted Resolution No. 74074 C.M.S., which prohibits investment in businesses deriving greater than 15 percent of their revenues from tobacco products.

Our analysis of the portfolio investments over the past several years shows that the added policies have varied by the degree of impact on both the City and the Agency portfolios. Summarized below are some of the key assumptions:

- The availability of investing in U.S. Treasuries will provide more on-going liquidity and safety for the City's portfolio. U.S. Treasuries are direct obligations and backed by the full faith and credit of the U.S. Government thus making them one of the safest possible investments for the City at this time.
- The City has experienced slightly higher pricing levels when investing in Medium Term Notes of renewable energy resources and other socially responsible investments. The higher price of the securities translates into a lower yield for the portfolio.
- The City's inability to invest in businesses that generate greater than 15 percent of their revenue from tobacco products has had the least impact on the City's Portfolio due to the limited number of such businesses.

Below is a side by side comparison of the California State Government Code Section No. 53601 and the City of Oakland 2008-2009 Investment Policy.

PERMITTED INVESTMENT TYPES	STATE OF CALIFORNIA GOVERNMENT CODE SECTION No. 53601	CITY OF OAKLAND 2008-2009 INVESTMENT POLICY
Bonds issued by the local Agency	No exposure limitation. Up to 5 years maximum maturity.	No Change.
U.S. Treasury Notes, Bonds, Bills or Certificates of Indebtedness	No exposure limitation. Up to 5 years maximum maturity.	City Council has granted permission to invest up to 20% of the City's portfolio in U.S. Treasuries for 60 days as of October 21, 2008.
State of California Bonds	No amount limitation. Up to 5 years maximum maturity.	No Change.
Other Local Agency Bonds from the other 49 States	No exposure limitation. Up to 5 years maximum maturity.	No Change.
Bankers Acceptance	Limited to 40% portfolio exposure, or 30% in any one commercial bank. Up to 180 days maximum maturity.	No Change.
Local Agency Investment Fund (LAIF)*	Limited \$40,000,000 portfolio exposure. No maximum maturity.	No Change.
Federal Agency or United States Government-sponsored enterprise obligations (i.e. Fanny Mae, Freddie Mac)	No exposure limitation. Up to 5 years maximum maturity.	No Change.
Commercial Paper	Limited to 25% portfolio exposure. Up to 270 days maximum maturity.	No Change.
Negotiable Certificates of Deposit	Limited to 30% portfolio exposure. Up to 5 years maximum maturity.	No Change.
Repurchase Agreements	No exposure limitation. Up to 1 year maximum maturity.	No Change.
Medium Term Notes	Limited to 30% portfolio exposure. Up to 5 years maximum maturity.	No Change.
Money Market Funds	Limited to 20% portfolio Exposure. No maximum maturity.	No Change.
Collateralized Mortgage Obligations	Limited to 20% portfolio Exposure. Up to 5 years maximum maturity.	Per the City of Oakland 2008-2009 Investment Policy, this is not a permitted investment

* Per the guidelines of the Local Agency Investment Fund (LAIF)

SUSTAINABLE OPPORTUNITIES

Economic: The Cash Management Report summarizes the characteristics of the investment portfolios for the quarter. The portfolios' credit quality remains high and well within the parameters of the City's Investment Policy. Moreover, liquidity remains sufficient to meet the City's projected needs.

Environmental: To the extent that new investment opportunities are found in companies involved in environmentally positive activities, the City will be supporting these actions.

Social Equity: The City's policy is to invest, when possible, in companies that promote the use and production of renewable energy resources and any other types of socially responsible investments. Optimization of the portfolios while observing those key areas will produce interest earnings to the General Fund. These monies may be available for services to disadvantaged areas, or enhanced recreational or social venues. Furthermore, the Treasury Division is making every effort to identify and purchase additional qualifying investments from renewable energy and other socially responsible companies.

DISABILITY AND SENIOR CITIZEN ACCESS

There are no disability and senior citizen access issues identified in this report.

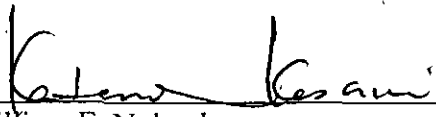
RECOMMENDATION(S) AND RATIONALE

Staff recommends Council's acceptance of this informational report.

ACTION REQUESTED OF THE CITY COUNCIL

Staff requests that Council accept this informational report.

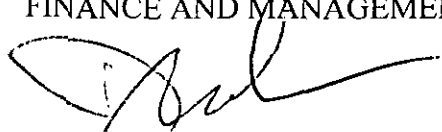
Respectfully Submitted,

for 

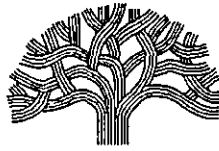
William E. Noland
Director, Finance and Management Agency

Prepared by:
Katano Kasaine, Treasury Manager
Treasury Division

APPROVED AND FORWARDED TO THE
FINANCE AND MANAGEMENT COMMITTEE:



Office of the City Administrator



**CITY OF OAKLAND AND OAKLAND REDEVELOPMENT AGENCY
CASH MANAGEMENT REPORT
FOR THE QUARTER ENDED SEPTEMBER 30, 2008**

**PREPARED BY THE
FINANCE AND MANAGEMENT AGENCY
TREASURY DIVISION**

OCTOBER 31, 2008

CITY OF OAKLAND AND OAKLAND REDEVELOPMENT AGENCY
CASH MANAGEMENT REPORT
FOR QUARTER ENDED SEPTEMBER 30, 2008

I. ECONOMIC REVIEW

MARKET OVERVIEW

The collapse of the sub-prime mortgage market has created a credit squeeze in the financial market. It has now spread to all aspect of the financial industry leading to the current credit crunch in the United States economy as well as internationally. The turmoil in the market has caused many financial companies to file for bankruptcy or force sale to other banks to stay afloat; e.g., Lehman Brothers, Washington Mutual, Wachovia, and Merrill Lynch. Money market funds, traditionally viewed as a safe haven for money funds, are losing value and closing.

The national financial crisis has also lead to large-scale government intervention. The takeover of the country's two largest mortgage companies, Fannie Mae and Freddie Mac, along with an emergency loan of \$85 billion to AIG to rescue the company from bankruptcy, and the \$700 billion bailout plan were attempts by the US government to stabilize the market. As the global financial crisis is still lingering, the reality of a global recession looms.

The U.S. economy contracted at a 0.3 percent annualized rate in the third quarter as consumer spending declined, a significant slowdown after a growth of 2.8 percent in the second quarter. The impact of the economic stimulus program that helped boost the consumer spending in the second quarter faded and consumer confidence was shaken by the upheavals on global markets. Consumer spending, which accounts for two-thirds of the economy, dropped at a 3.1 percent annualized rate for one quarter, the largest drop in 28 years in the third quarter.

As the labor market slump worsens, it continues to threaten the growth of the economy. The U.S. unemployment rate remained stable in September at 6.1 percent, the highest level in five years. Eight months of job losses and continued a decline in construction, manufacturing, and retail trade has experts forecasting that the unemployment rate will increase in the next few months.

Consumer prices increased at a seasonally adjusted annualized rate of 2.6 percent in the third quarter of 2008, following increases in the first and second quarters at annual rates of 3.1 and 7.9 percent, respectively. This brings the year-to-date annual rate to 4.5 percent and compares with an increase of 4.1 percent for all of 2007. The main contributors to the rise in the CPI during the third quarter of 2008 were higher food prices, mainly rice and meat, and a large variety of other food products; higher prices of gasoline and diesel in July 2008; and higher prices of cigarettes in September 2008. With the impact of the financial crisis clearly taking a toll on consumers' confidence, it appears that the fourth quarter is off to a weaker start than the third quarter.

The deterioration of the housing market has American homeowners in a choke-hold. The combination of sinking home values, tighter mortgage lending criteria and a weak economy that has already slipped into a recession, hundreds of thousands of homeowners are left with few options. Home values in the U.S. posted a seventh consecutive quarterly decline, with nearly one-third of Americans who sold in

the past year losing money. Home values fell 9.7 percent year-over-year in the third quarter. Foreclosures jumped more than 70 percent in the third quarter of 2008 compared to the same period last year. Even though, foreclosure filings have decrease by 12 percent in September, largely as a result of several states housing laws, these changes only temporarily slowed down the pace at which lenders are moving forward with foreclosures.

The value of the dollar slumped in currency markets at historic lows, as the dollar continues to fall against the 15-nation Euro and British pound at weak news of labor, gross domestic product, and consumer price index. Oil prices plunged below \$56 a barrel, more than 60 percent, in the last four months as demand declined sharply. These are indications of weak economic growth in the coming months.

INTEREST RATES

After making cuts through all of 2007 and the first half of 2008, the Federal Reserve has halted an aggressive rate-cutting campaign in June out of fears that low rates would worsen inflation. The Fed started signaling that rates would probably go up to fend off inflation. The Fed shifted signals back to a rate cut because of a housing bust, a credit clog, and a financial meltdown, imperiling the U.S. and global economy leading to an emergency rate cut on October 8, 2008. The Fed and other central banks joined to slash rates, the first coordinated move of that kind in the Fed's history. That dropped the Fed's key rate down to its current 1.50 percent. Fear of further deterioration of market condition, the Fed again cut rates for the second time in October by 50 basis points to 1.00 percent.

The Fed hopes that lower borrowing costs will entice people and businesses to spend again, which would help revive the economy. The Fed also hopes that other actions such as the bailout plan, and lowering rates will shore up the U.S. financial system and get credit flowing more freely again.

Rather than take a position on the future direction of interest rates, we expect to continue to manage the investments of the City and the Agency Operating Fund Portfolios consistent with the City's policy objectives and with a primary focus on meeting liquidity needs.

II. CITY OF OAKLAND

PORTFOLIO REVIEW

The City's Portfolio balances decreased from \$281 million on June 30, 2008 to \$237.25 million by September 30, 2008. The decrease was due to repayment of 2007-2008 Tax and Revenue Anticipation Notes, debt service payments, normal operating expenses, vendor payments offset by receipt of property tax and business tax revenues, and the ongoing financial crisis linked to the sub prime mortgages.

PORTFOLIO RATING

In November 2008, Fitch assigned its highest managed fund credit rating of *AAA* and market risk rating of *V1+* to the City's Operating Fund Portfolio (attached). The *AAA* credit rating reflects the highest credit quality based on asset diversification, management strength and operational capabilities. The *V1+* market risk rating represents the lowest market risk that can be expected with no loss of

principal value even in adverse market conditions. Fitch’s market risk ratings reflect the rating agency’s assessment of relative market risks and total return stability in the portfolio based on analyses of various market indicators such as interest rates, liquidity and leverage risk, if any. As a condition of maintaining these ratings, the City provides monthly information to Fitch for review of the Operating Fund Portfolio activity and holdings.

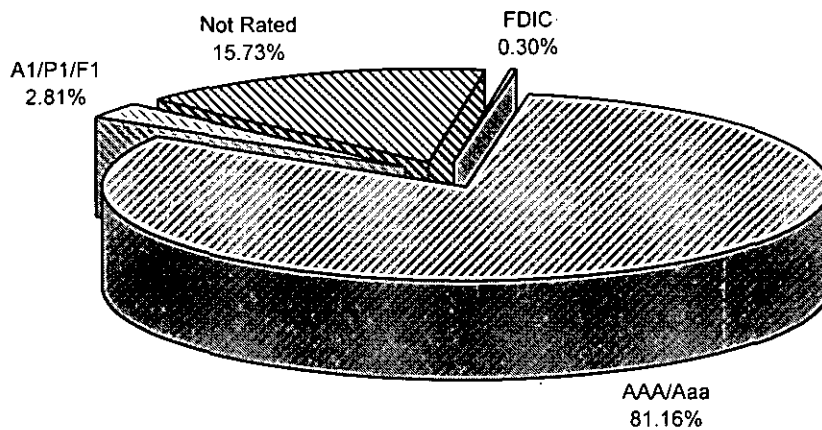
PORTFOLIO COMPOSITION

The Portfolio continues to comply with all provisions of the City’s adopted Investment Policy for Fiscal Year 2008-2009, including compliance with applicable local ordinances and resolutions such as Linked Banking, and Tobacco Divestiture. On October 21, 2008 City Council passed resolution No. 2008-0091 C.M.S. that allows the City to invest up to 20% of its portfolio in U.S. Treasuries for a period of 60 days. In addition, the City will invest, when possible, in companies that promote the use and production of renewable energy resources and any other type of socially responsible investments.

The following discussion addresses the City’s investment portfolio characteristics in terms of the Investment Policy’s four objectives: safety, liquidity, diversity and return. Portfolio detail for each month of the current quarter is attached to this report.

Preservation of Capital/Safety. In the chart below, the City’s holdings are depicted by credit rating category as of September 30, 2008. Approximately 81.16% of Operating Fund investments were rated in the AAA/Aaa category while 2.81% were rated in the A1/P1/F1 category. And 15.73%, primary unrated holdings represent the Fund’s investments in the Local Agency Investment Fund (“LAIF”). FDIC-insured Certificates of Deposit constituted less than 1% of the total Operating Fund.

**City of Oakland Operating Fund
Portfolio Credit Quality
(As of 09/30/08)**



Liquidity. Liquidity continues to be a primary objective when making investment decisions for the Operating Pool portfolio. With ongoing capital projects at the Port and within the City, and to ensure that sufficient liquidity is available to meet day-to-day expenditures, the City maintains a sufficient “cushion” in money market funds to meet unanticipated project expenditures.

Debt service payable from the City's Operating Pool for the Port and the City for the six months following September 30, 2008, is approximately \$94.79 million. Consequently, staff will continue to invest in short-term instruments and money markets as investment tools to maintain adequate short-term liquidity.

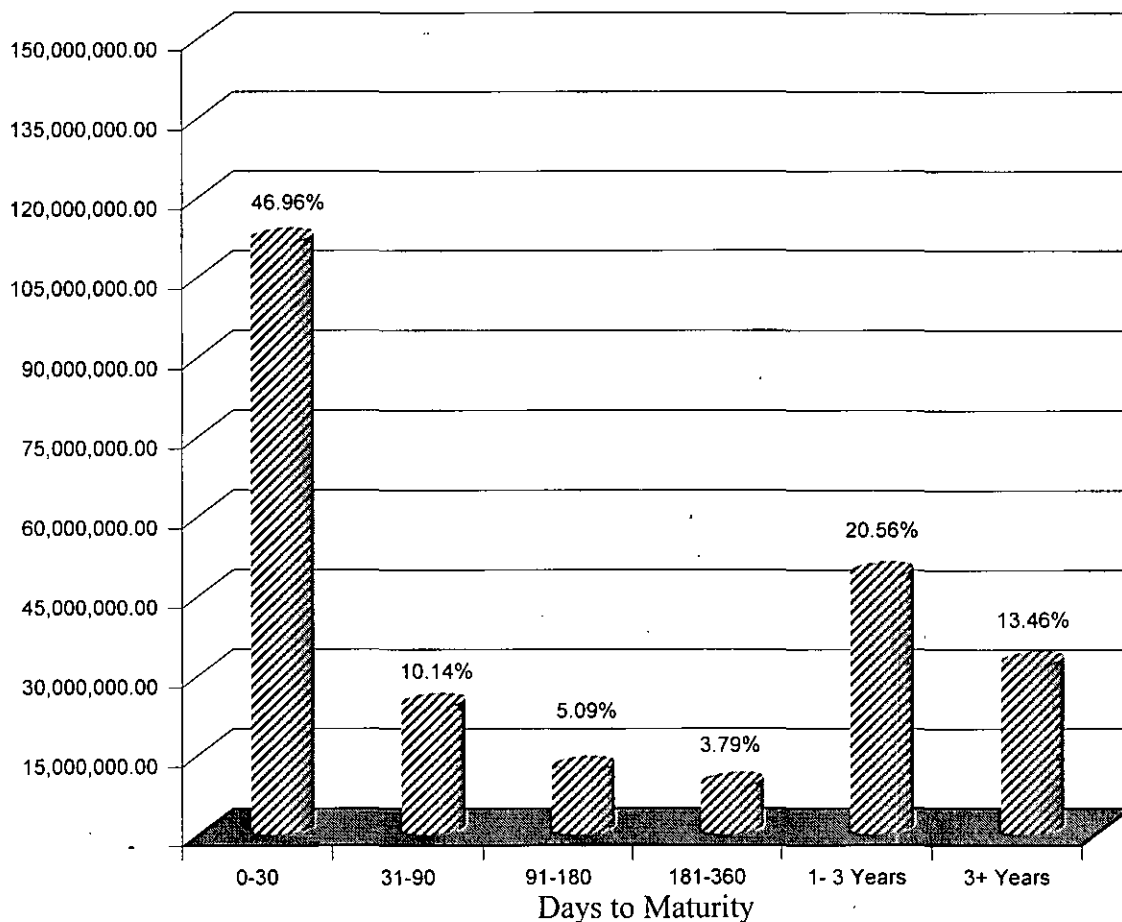
Investments maturing over the next six months are as follows:

Days	Amount(s)	Percent
0-30	\$111,610,0000	46.96%
31-180	\$ 36,199,000	15.23%
Total	\$ 147,809,000	62.19%

The total amount maturing within 180 days includes \$37 million in LAIF and \$38.1 million in money market funds, both of which are considered to have a one-day maturity due to the ability to withdraw funds daily.

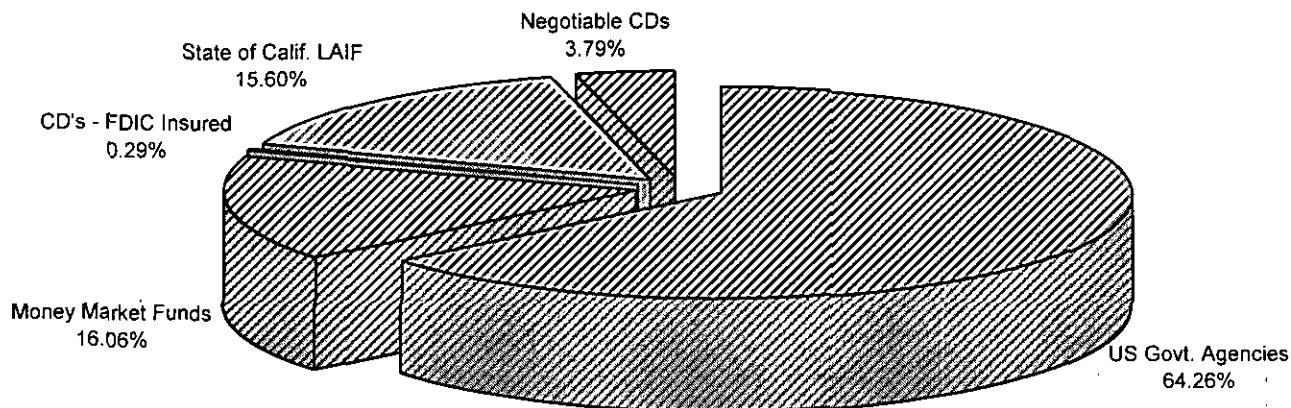
The following graph depicts the Operating Fund Portfolio by dollars invested and the percentage in each maturity range as of September 30, 2008.

**City of Oakland Operating Fund
Portfolio Maturity
(As of 09/30/08)**



Diversity. To reduce the risks of investing, the portfolio is diversified among a variety of financial instruments, as depicted by the following chart. In addition to limiting the types of investments permissible in any one category as outlined in the Investment Policy, no more than 5% of the total cash portfolio may be invested in any one issue. This single-issue provision does not apply to money market funds or to LAIF, as they each are backed by a large portfolio of highly diversified assets.

**City of Oakland Operating Fund
Portfolio Diversity
(As of 09/30/08)**



Derivatives. The Operating Fund Portfolio contained no derivative instruments during this reporting period.

Yield. Total interest earned for the quarter ended September 30, 2008, was approximately \$1.9 million. The effective rate of return on total assets in the Operating Fund Portfolio for month-end September 30, 2008, was 3.13% as compared to 2.69% for June 30, 2008. This is primarily due to the longer duration of the September 30, 2008 portfolio (397 days average maturity) versus the June 30, 2008 portfolio (342 days to maturity). It continues to be the City's practice to hold investments to maturity rather than to sell at a loss and adjust to the market's yield curve. The primary investment objective of the City for the portfolio is to maximize safety, liquidity, and return in that respective order.

Comparative yields for the quarter are shown below.

**City of Oakland Operating Fund
Comparative Annualized Yields
(As of 09/30/08)**

As of Month-end	6-month Treasury	LAIF¹	Operating Fund
July 2008	1.86%	2.79%	2.97%
August 2008	1.91%	2.78%	3.07%
September 2008	1.61%	2.77%	3.13%

¹Effective monthly average return.

Benchmark Comparison.

The effective rate of return on total assets in the Operating Fund Portfolio for the month ending September 30, 2008 was 3.13%. The City's Operating Fund Portfolio outperformed the 6-month Treasury Bill which yielded a rate of 1.61% at the end of September 30, 2008. The City's Operating Fund Portfolio slightly outperformed the Local Agency Investment Fund ("LAIF"), which ended the month at 2.77%.

The performance comparison to LAIF must be considered in light of LAIF's historical tendency to lag market changes in both rising and falling interest rate environments.

The City does not actively sell securities in the portfolio to take advantage of cyclical swings in the market, which could result in the loss of principal.

The primary investment objective of the City for the portfolio is to maximize safety, liquidity, and return in that respective order.

Valuation and Leverage. Based on information received from Interactive Data Corporation, the market value of the Operating Fund was \$237.79 million, which was above book value by \$537,095. There was no leverage in the portfolio during the reported period and liquidity was maintained at sufficient levels.

III. OAKLAND REDEVELOPMENT AGENCY

PORTFOLIO REVIEW

The Agency's portfolio decreased from a balance of \$229.38 million at the end of June 30, 2008 to \$177.79 million at the end of September 30, 2008. Contributing to the portfolio decrease was largely due to debt service payments.

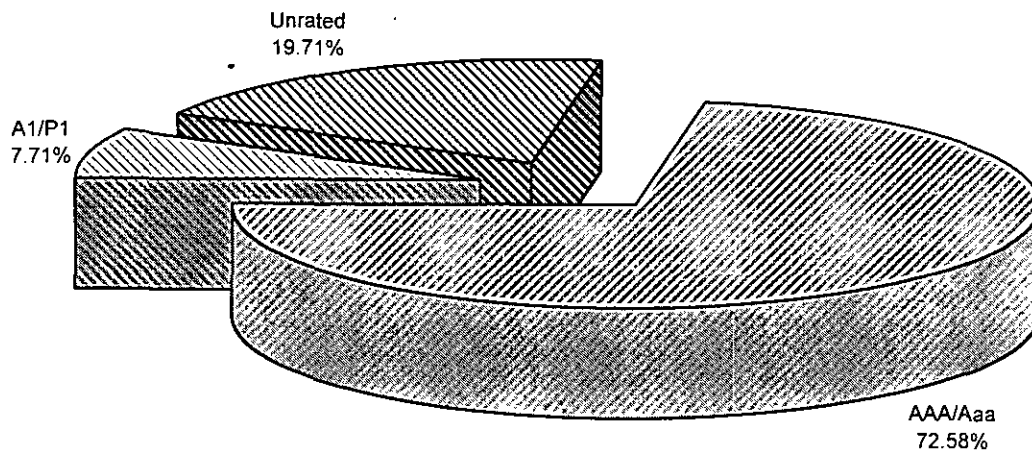
PORTFOLIO COMPOSITION

The Portfolio continues to comply with all provisions of the City's adopted Investment Policy for Fiscal Year 2008-2009, including compliance with applicable local ordinances and resolutions such as Nuclear Free Zone, Linked Banking, and Tobacco Divestiture. In addition, the City will invest, when possible, in companies that promote the use and production of renewable energy resources and any other type of socially responsible investments.

The following discussion addresses the Agency investment portfolio characteristics in terms of the Investment Policy's four objectives of safety, liquidity, diversity and return. Portfolio detail for each of the months in the current quarter is attached to this report.

Preservation of Capital/Safety. The Agency's holdings by credit rating category are depicted in the chart below. Approximately 72.58% of the Agency's Operating Fund investments are rated in the AAA category. Primary unrated holdings represent 19.71% of the Fund's investments in LAIF, and A1/P1 ratings represent 7.71% of the Agency's holdings.

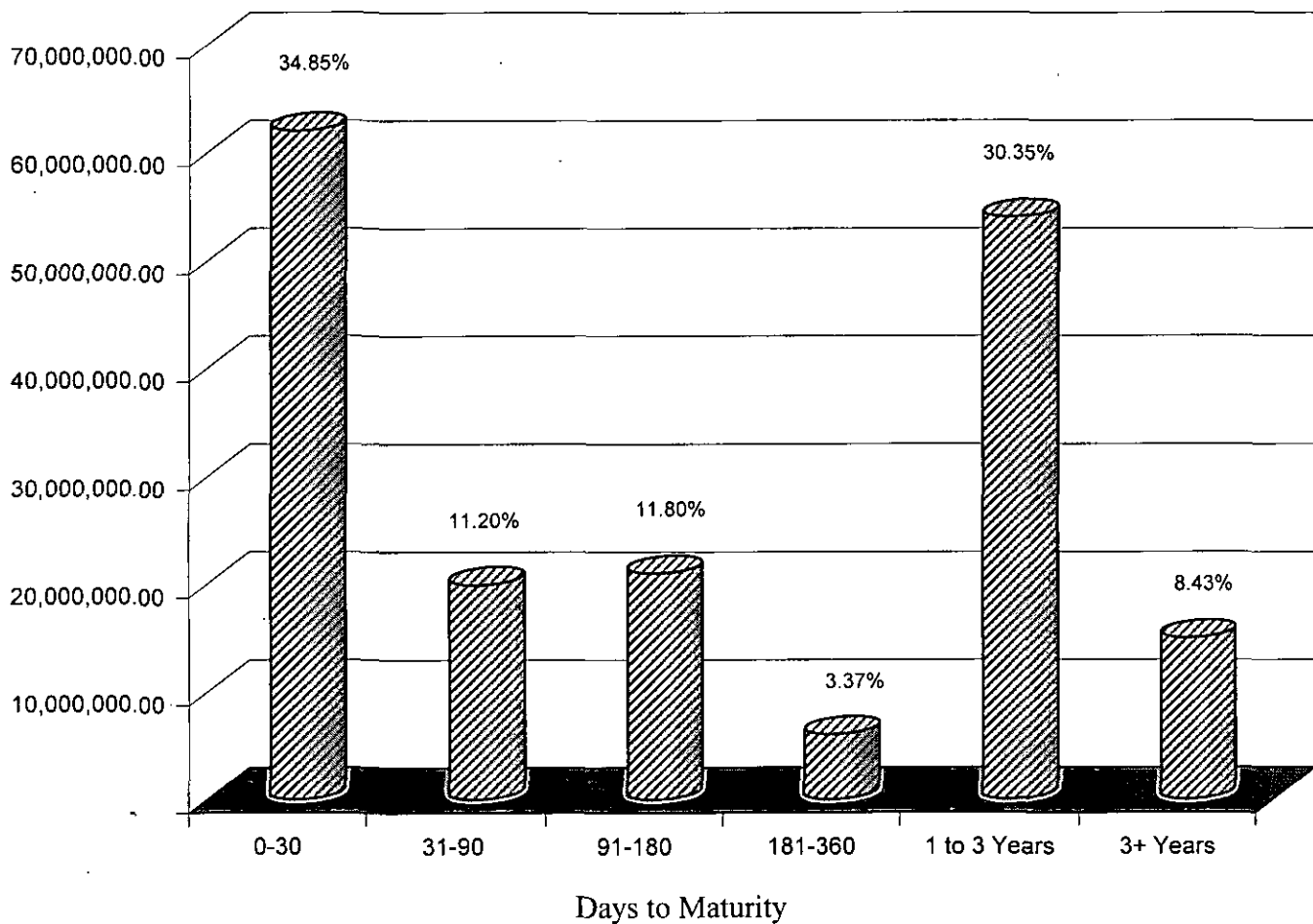
**Oakland Redevelopment Agency
Portfolio Credit Quality
(As of 09/30/08)**



Liquidity. Liquidity within the Agency’s Portfolio remains sufficient to meet all expected cash flow needs of the Agency for the next six months and beyond. The debt service payment for the next six months for the Agency is approximately \$19.40 million. The Agency also maintains sufficient “cushion” in highly liquid instruments to meet unanticipated project expenditures.

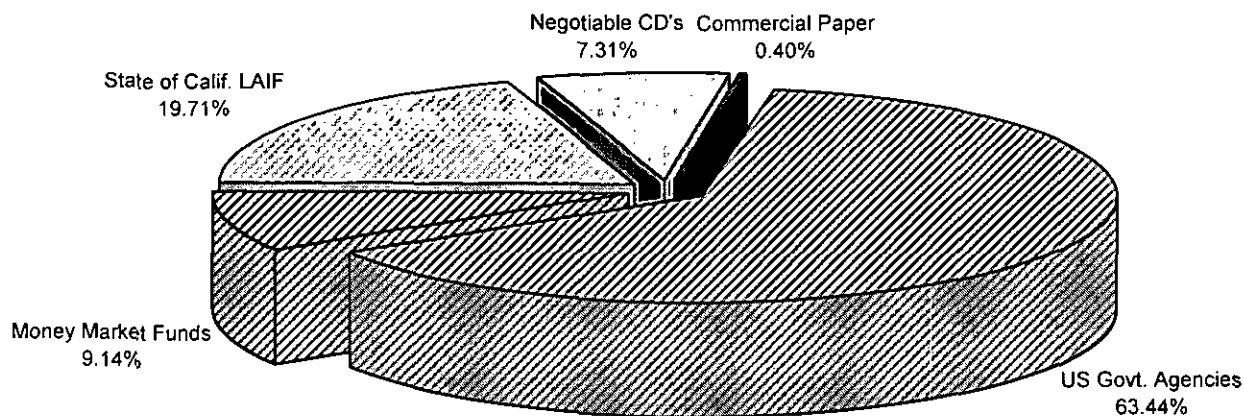
The following chart depicts the Agency’s Portfolio by percentage and dollars invested in each maturity range.

**Oakland Redevelopment Agency
Portfolio Maturity
(As of 09/30/08)**



Diversity. To reduce the risks of investing, the portfolio is diversified among a variety of instruments, as depicted by the following chart. In addition to limiting the types of investment in any one category, as outlined in the Investment Policy, no more than 5% of the total cash portfolio may be invested in any one issue.

**Oakland Redevelopment Agency
Portfolio Diversity
(As of 09/30/08)**



Derivatives. The Agency Portfolio contained no derivative instruments during this reporting period.

Yield. Total interest earned for the quarter ended September 30, 2008, was approximately \$1.55 million. The effective rate of return on total assets in the Agency's Portfolio was 3.17% for month ending September 30, 2008. The Agency's Portfolio has outperformed LAIF due to the fact that the average days to maturity for LAIF is 249 days and the Agency's average days to maturity is 385 days as of September 30, 2008. The market is now seeing an upward sloping yield curve, therefore LAIF's shorter average life will continue to cause their yield to decline more rapidly as interest rates continue their decent.

Comparative yields for the quarter are shown below.

**Oakland Redevelopment Agency
Comparative Annualized Yields
(As of 09/30/08)**

As of Month-end	6-month Treasury	LAIF ¹	ORA
July 2008	1.91%	2.79%	2.90%
August 2008	1.86%	2.78%	2.95%
September 2008	1.61%	2.77%	3.17%

¹Effective monthly average return

Valuation and Leverage. Based on information received from Interactive Data Corporation, the market value of the Agency portfolio for the quarter ended September 30, 2008 was \$177.79 million, which was above book value by \$174,526. There was no leverage in the portfolio during the reporting period and liquidity was maintained at sufficient levels.

TREASURY YIELD CURVE

