MUNICIPALITY OF ANCHORAGE

ASSEMBLY INFORMATION MEMORANDUM

No. AIM 55-2018

Meeting Date: June 12, 2018

FROM: Mayor

SUBJECT: Investment Advisory Commission Annual Report – 2017 Year in Review

The ordinance that created the Investment Advisory Commission (AO 95-46) requires that the Commission report annually to the Mayor and the Assembly.

Attached to this AIM is the Investment Advisory Commission Annual Report.

Prepared by: Daniel Moore, Municipal Treasurer
Concurrence: Robert E. Harris, CFO
Concurrence: William D. Falsey, Municipal Manager
Respectfully submitted: Ethan A. Berkowitz, Mayor

Municipality Of Anchorage

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Ethan Berkowitz, Mayor

INVESTMENT ADVISORY COMMISSION

June 12, 2018

Mayor Ethan Berkowitz
Municipal Assembly
Municipality of Anchorage
PO Box 196650
Anchorage, AK 99519

RE: Investment Advisory Commission Annual Report – 2017 Year in Review

Dear Mayor Berkowitz and Assembly Members:

The Investment Advisory Commission's (the "Commission") charge under the enabling ordinance AO No. 95-46 is to act in a non-fiduciary capacity to the Administration and the Assembly in giving advice on matters concerning the investment of municipal funds including the Municipality of Anchorage (the "MOA") Trust Fund (the "Trust"). In that capacity, the Commission believes that the Investment Policy Statement utilized in 2017 for the Trust represented a prudent investment policy which the Commission viewed as appropriate for the capital markets environment. This policy was reviewed and updated in 2017. In 2018, the Commission intends to review a number of the existing investment mandates, based on recommendations from the investment consultant.

AO 95-46 further requires that the Commission report annually to the Mayor and the Assembly, the text of which is as follows:

THE MOA TRUST FUND

The MOA Trust Fund and MOA Trust Reserve ("Reserve Fund") were established in May 1999, following the sale of the Anchorage Telephone Utility (ATU), with an initial total deposit of $118.6 million. In May 2000, $40 million was received from the Police/Fire Retirement Fund settlement; these new assets were allocated 50% to the Trust Fund (Fund 730) and 50% to the Reserve Fund (Fund 731). Late in 2000 approximately $15.1 million of the $20 million deposited in the Reserve Fund was used to defease two municipal revenue bonds. In January 2002, an additional $1.3 million from a Bank of America Settlement was added to the Trust Fund. In June 2014 an additional $1.93 million was deposited into the Trust following Assembly appropriation made in conjunction with the 1st Quarter 2014 General Government Operation Budget revision. Since the ATU sale closing, $126.1 million in annual dividends have been paid to the MOA as return on investment. Including the bond defeasance, just over $141.2 million has been distributed from the Trust Fund/Reserve Fund. This is now contained in its entirety within a single fund (730), as the need for the Reserve Fund was eliminated when the dividend distribution formula was changed to a percentage of market value approach in 2002.

The Trust's planning time horizon is greater than five years and its risk tolerance is moderate to moderately high with a specific stated objective to maintain purchasing power of the corpus while simultaneously generating earnings for distribution.

The projected dividend to be paid to the MOA from the Trust in 2018 is $6.3 million based on AO No. 2016-127. The spending policy was changed from 4% of the "average asset balance" to 4.25% to reflect the Trust Fund's recovery in market value from the impact of the downturn in the markets resulting from the 2008-2009 recession. For this calculation the "average asset balance" is defined as the average of the trailing 20 calendar quarters ended March 31 each year.

2017 RESULTS

The market value of the Trust Fund portfolio on 12/31/17 was $165.0 million (before net effect of year-end accruals) compared to the 12/31/2016 market value of $147.7 million. There were no additional deposits to the fund in 2017 and the total dividend withdrawal for the calendar year ended 12/31/2017 was $6.0 million. The Trust experienced an overall return of 16.32% in calendar year 2017 (results per RVK). This return exceeded the target policy index by 0.52%. The policy index is comprised of market indices weighted in the same proportion as the Trust's long term allocation policy. The policy index had a total return of 15.80% for 2017.

As per the Investment Policy Statement, the asset allocation for the Trust in 2017 covered four core asset classes, namely: Domestic Equities, International Equities, Fixed Income, and Real Estate. These asset classes are managed by seven individual managers, each tasked with a specific mandate for their respective asset class.

The individual manager's portfolio market values at year end, percentage of total portfolio, annual return for 2017, and corresponding bench mark returns as calculated by RVK, were as follows:

	Market Value	Percent of Portfolio	2017 Return
Domestic Equity Composite	**$ 61,893,464**	**37.51%**	**22.05%**
Russell 3000 Index			21.13%
Vanguard Index Fund	**$ 53,032,358**	**32.14%**	**21.79%**
Standard & Poor's 500 Index			21.83%
Mid Cap Equity Composite	**$ 4,519,256**	**2.74%**	**19.24%**
Vanguard Mid Cap Index Fund	$ 4,519,256	2.74%	19.25%
Vanguard Spl Mid Cap Index			19.30%
Small Cap Equity Composite	**$ 4,341,850**	**2.63%**	**10.79%**
BlackRock Small Cap Equity Fund	$ 4,341,850	2.63%	10.79%
Russell 2000 Index			14.65%
International Equity Composite	**$ 43,854,986**	**26.58%**	**26.99%**
EuroPacific Growth Fund	$ 22,270,424	13.50%	31.03%
Templeton Foreign Equity Fund	$ 21,584,562	13.08%	22.92%
MSCI ACW ex-US Index			27.19%
Domestic Fixed Income Composite	**$ 461,839,377**	**28.30%**	**4.63%**
FIAM Core Plus Bond Fund	$ 41,839,377	25.35%	4.80%
Western Asset Floating Rate Fund	$ 4,874,716	2.95%	3.15%
Bloomberg US Agg Bond Index			3.54%
S&P/LSTA Performing Loans Index			4.32%

	Market Value	Percent of Portfolio	2017 Return
Real Estate Composite	**$ 12,520,486**	**7.59%**	**5.21%**
UBS Trumbull Property Fund	$ 12,520,486	7.59%	5.21%
NCREIF ODCE			6.66%
Cash Account	**$ 36,298**	**0.02%**	
Total Fund	**$165,019,327**	**100.00%**	**16.32%**
Policy Target			15.80%

Overall, the Trust returned 16.32% outperforming its Investment Policy benchmark by 0.53% in what proved to be a very strong market for equity investments in general. Equity returns for the year were uniformly positive, with non-US markets outpacing US markets. Emerging Markets led the way returning 37.28% for 2017. Fixed income investments posted positive returns; while the absolute level of returns were much lower than equity markets, fixed income continues to provide meaningful diversification and downside protection. Other income focused strategies – such as core real estate – also provided positive returns in 2017.

In consideration of market forces, the Commission reiterates its belief that the core tenants of Investment Policy, diversification, and asset allocation remain the most effective strategy to achieve the long term investment goals of the Trust, while also mitigating risk and volatility within the portfolio.

The Municipal Cash Pool (MCP)

In late October 2006, the Assembly passed AO 2006-145 which broadened the investment parameters available for investment of the Municipality's general cash pool. Prior to this time the general cash pool was managed in-house with a 90 day Treasury and Agency strategy. In early 2007, the Commission participated in the process which redefined the investment strategy and created the Municipal Cash Pool ("MCP"), a subset of the general cash pool. The Commission also participated in the selection of external money managers for the MCP to invest cash on behalf of General Government, Municipal Utilities and the Anchorage School District. On June 1, 2007, the Municipality initiated the new MCP structure, which is comprised of three Portfolios of fixed income securities, each with a separate manager, targeted duration, and respective benchmark and together these three Portfolios hold the majority of funds in the general cash pool. Each year the Public Finance and Investments Division staff performs a rebalancing evaluation of the three Portfolios of the MCP in consultation with Callan Associates. This review is based upon forecasted cash flows, liquidity needs and projected issuance of Tax Anticipation Notes.

The return numbers reported below for 2017 are gross of fees and are compared to the respective benchmarks. Return gross of fees is the most appropriate comparison on how the manager is performing. We pay our managers to compete against their benchmark gross of fees.

Strategic Reserve Portfolio This Portfolio is managed by BlackRock, and at year end, had assets of approximately $223 million. This Portfolio is the longest duration Portfolio of the MCP. The intent is that this Portfolio would be the last one tapped in the event of required liquidity. The benchmark is a composite of 75% Bloomberg Barclays Intermediate US Government/Credit Index and 25% Bloomberg Barclays Intermediate US High Yield Total Return Index. Blackrock may invest up to 30% of the Portfolio into High Yield securities. For calendar 2017, the Portfolio returned 3.66% versus the blended benchmark return of 2.26%.

Contingency Portfolio This Portfolio is a Core Short Term Duration Portfolio that is currently managed by PNC Capital Advisors (PNC). The Portfolio at year end held approximately $128 million. This Portfolio is the middle duration Portfolio of the MCP. The intent of this Portfolio is to provide liquidity should the Working Capital Portfolio be depleted. PNC competes against the Bloomberg Barclays 1-3 Year US Government/Credit Index. For calendar year 2017, the Portfolio returned 1.15% versus the benchmark return of 0.84%.

Working Capital Portfolio This Portfolio is used for day to day cash flow and liquidity and is managed by Alaska Permanent Capital. Assets at year-end in this Portfolio were approximately $89 million. The benchmark for this portfolio is the BofA Merrill Lynch 3-Month U.S. Treasury Bill Index. For calendar year 2017, the Portfolio returned 0.91% versus the benchmark return of 0.86%.

Restricted/Internally Managed Portfolio This Portfolio is managed by the Municipality's Public Finance & Investments Division staff. This Portfolio is comprised of assets that are primarily bond proceeds, debt service accounts, debt service reserve accounts, short term cash and other specifically restricted assets that are required to be independent of the MCP. These funds are managed primarily for safety and liquidity rather than return, although, we continuously verify that we have the assets in the highest yielding investments that provide safety and the appropriate level of liquidity. The benchmark for this portfolio is the BofA Merrill Lynch 3-Month U.S. Treasury Bill Index. For calendar year 2017, the Portfolio returned 0.80% versus the benchmark return of 0.86%.

Summary of the Total Aggregate Portfolio – General Government

The Public Finance and Investments Division staff calculated, for period June 1, 2007 through December 31, 2017, that the new strategy return of 1.76% outperformed a benchmark representing the pre-June 2007 strategy by 1.12%. In dollar terms, this means the new investment strategy has generated an additional $80 million in investment earnings, as of December 31, 2017, for the MOA since its inception (June 1, 2007) when compared to the pre-June 2007 strategy.

Conclusion

The Commission reaffirms its commitment to the core tenants of the MOA Trust's current investment policy – namely diversity and fixed allocation guidelines and believes they will continue to serve the Trust well in the current economic environment.

The Commission also confirms that the returns of the MCP continue to validate the Best Practice investment strategy for the management of the MCP and the Total Aggregate Portfolio. The Commission also notes that Callan Associates, independent investment advisor to the Public Finance & Investments Division for the Total Aggregate Portfolio, confirms that the MCP and the Total Aggregate Portfolio are being managed under both the Prudent Investor Rule and Best Practices.

This annual report was approved unanimously by the Commission at its May 2, 2018 regular meeting.

/Alex Slivka/, Chair
Investment Advisory Commission