MUNICIPALITY OF ANCHORAGE

ASSEMBLY INFORMATION MEMORANDUM

AIM 86-2021

Meeting Date: **June 8, 2021**

FROM: Mayor

SUBJECT: Investment Advisory Commission Annual Report – 2020 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: Alexander Slivka, CFO
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Respectfully submitted: Austin Quinn-Davidson, Acting Mayor

Municipality Of Anchorage

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Austin Quinn-Davidson, Acting Mayor

INVESTMENT ADVISORY COMMISSION

June 8, 2021

Acting Mayor Austin Quinn-Davidson
Municipal Assembly
Municipality of Anchorage
PO Box 196650
Anchorage, AK 99519

RE: Investment Advisory Commission Annual Report – 2020 Year in Review

Dear Acting Mayor Quinn-Davidson 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 ("MOA") Trust Fund ("Trust"). In that capacity, the Commission believes that the Investment Policy Statement utilized in 2020 for the Trust represented a prudent investment policy which the Commission viewed as appropriate for the capital markets environment. The investment policy was last reviewed and updated September 1, 2020. For the new calendar year, the Commission intends to work with the investment consultant to monitor placement of the initial investment with two newly chosen direct real estate managers and the newly chosen private credit manager, each of which was chosen to further diversify the Trust. 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. In late October 2020, the Trust received an additional $229.6 million from the proceeds of the sale of Municipal Light & Power (ML&P). Since the ATU and the ML&P sale closings, $152.87 million in annual dividends have been paid to the MOA as return on investment through 2020. Including the year 2000 bond defeasance, a grand total of approximately $168 million has been distributed from the Trust Fund/Reserve Fund since the Trust's inception. All monies of the Trust are accounted for within a single fund (SAP Fund 730000), 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.

Per AO No. 2016-127, the spending policy changed from 4.00% 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 in Anchorage Municipal Code (AMC) 6.50.060 as the average of a specified number of trailing calendar quarters ended March 31 each year. In connection with the October 2020 sale of Municipal Light & Power (ML&P) the spending policy formula was further revised per AO 2020-98 to increase the long-term payout rate to 4.50% starting in 2021. Both the Commission and the investment consultant (RVK) were actively engaged in the details of this ordinance and its presentation to the Assembly. The current 4.5% long-term payout rate is intended to keep pace with real return assumptions (i.e., long-term expected return, "net" of long-term expected inflation).

2020 RESULTS

The market value of the Trust Fund portfolio on 12/31/20 was approximately $418.0 million (excluding net effect of year-end accruals), as compared to the 12/31/2019 market value of $171.8 million. The Trust received $229.6 million of newly deposited from the ML&P sale proceeds on October 30, 2020. This increased the market value of the Trust by approximately 2.5 times its previous value. In 2020, the annual dividend payout was $14.0 million, as compared to the prior year 2019 payout of $6.5 million. All portfolio returns for the Trust cited in this report are shown net of fees. The Trust experienced an overall return of 8.75% in calendar year 2020 (results per RVK). 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 12.77% for 2020.

As per the Investment Policy Statement, the asset allocation for the Trust in 2020 covered four core asset classes, namely: Domestic Equities, International Equities, Fixed Income, and Real Estate. These asset classes are managed by nine individual managers, each tasked with a specific mandate for their respective asset class.

The individual managers' portfolio market value at year end, percentage of total portfolio, annual return for 2020, and corresponding benchmark return as calculated by RVK, were as follows:

	Market Value	Percent of Portfolio	2020 Return
DOMESTIC EQUITY COMPOSITE	**$135,024,183**	**32.30%**	**17.14%**
Russell 3000 Index			20.89%
Vanguard Institutional Index Fund	$113,736,490	27.21%	**18.40%**
S&P 500 Index (Cap Wtd)			18.40%
Vanguard Mid Cap Index Fund	$10,372,869	2.48%	**18.23%**
Vanguard Spliced Mid Cap Index			18.24%
BlackRock Small Cap Equity Fund	$10,914,824	2.61%	**19.57%**
Russell 2000 Index			19.96%

INTERNATIONAL EQUITY COMPOSITE	**$101,999,888**	**24.40%**	**15.22%**
MSCI ACW ex-US Index (USD) (Net)			10.65%
EuroPacific Growth Fund	$51,249,245	12.26%	**25.24%**
MSCI ACW Ex US Grth Index (USD) (Net)			22.20%
Vanguard Intl Value Fund (eff. 5/22/20)	$50,750,643	12.14%	**N/A**
MSCI ACW Ex US Val Index (USD) (Net)			
DOMESTIC FIXED INCOME COMPOSITE	**$128,297,654**	**30.69%**	**6.90%**
Bloomberg US Aggregate Bond Index			7.51%
FIAM Core Plus Bond Fund	$61,584,432	14.73%	**7.52%**
Garcia Hamilton Core Bond Fund	$61,719,346	14.77%	**8.34%**
Bloomberg US Aggregate Bond Index			7.51%
Western Asset Floating Rate High Inc Fund	$4,993,875	1.19%	**-0.07%**
S&P/LSTA Performing Loans Index			3.50%
EMERGING MARKETS DEBT COMPOSITE	**$20,769,972**	**4.97%**	**4.04%**
EMD Blended Index			4.56%
Ashmore Emerging Mkts Debt Fund	$10,451,376	2.50%	**2.56%**
Ashmore:Ems Tot Rtn Custom Index			3.86%
BlueBay Emerging Mkts Debt Fund	$10,318,596	2.47%	**7.01%**
JPM Emg Mkts Gond Gbl Dvf'd Index (TR)			5.26%
REAL ESTATE COMPOSITE	**$11,883,055**	**2.84%**	**-4.78%**
UBS Trumbull Property Fund	$11,883,055	2.84%	**-4.78%**
NCREIF ODCE Index (AWA) (Net)			0.34%
Cash Account	**$20,031,490**	**4.79%**	
Total Fund	**$418,006,242**	**100.00%**	**8.75%**
Policy Target			**12.77%**

Overall, the Trust returned 8.75% and lagged its Investment Policy benchmark by 4.02% in an extraordinarily strong year end market performance for both equity and fixed income investments. The relative underperformance of the Trust was directly attributable to the effects of holding high levels of one-time cash from the ML&P sale during the final two months of 2020 while the sale proceeds were being invested over four phases lasting six and a half weeks in the Trust's existing fixed income and equity portfolios.

In excluding the impact of the ML&P sale proceeds cash on the portfolio, the Trust experienced a return of 12.1% (vs. 8.8% as listed above), slightly underperforming its Investment Policy benchmark by 66 basis points. This underperformance is primarily due to some intricacies with the Trust's chosen domestic large and mid-capitalization indices underperforming the broad domestic market index, although poor benchmark relative performance by UBS and Western Asset also contributed to the underperformance.

In 2021, $59 million of the Trust's assets will be reallocated and newly placed with two new direct real estate managers and a new private credit portfolio manager, as part of further diversifying the Trust's investments. The managers most lagging their benchmarks were UBS and Western Asset, which underperformed their stated benchmarks by 512 and 357 basis points, respectively. In 2021, the Commission intends to focus on individual money manager performance, including these newly added real estate and private credit managers, and to see the Trust's asset allocation targets fully realized.

Further, the asset class composite and underlying manager performance figures shown above vary from one another because of the timing of the material cash flows invested over the six and a half weeks following the ML&P sale proceeds. The methodology for calculating performance varies between managers and composites where cash flow impact is mitigated for managers given this was not a decision made by the managers. But performance shown for composites reflects experienced levels of performance as impacted by the timing and magnitude of the cash flows from the ML&P sale proceeds over the last 2 months of 2020.

The Municipal Cash Pool (MCP)

In October 2006, the Assembly passed AO 2006-145 which broadened the parameters for investment of the Municipality's General Cash Pool (GCP). Prior to this, the GCP, along with much of the Anchorage School District's (ASD) general cash, was managed in-house but separately using a very short duration buy-and-hold strategy that obtained a return comparable to the 90-day Treasury Bill. In early 2007, the Commission participated in the process which redefined the investment strategy and created the Municipal Cash Pool (MCP). The Commission also participated in the selection of external money managers for the MCP. On June 1, 2007, the MCP was funded with MOA and ASD general cash. In June 2013, the Anchorage Community Development Authority (ACDA) began investing in the MCP as well.

The MCP is comprised of three Portfolios of fixed income securities, each with a separate manager, targeted duration, and respective benchmark. Each year Public Finance and Investments Division staff performs a rebalancing review of the three portfolios of the MCP in consultation with independent investment advisor Callan LLC. This review is based upon forecasted cash flows, including liquidity needs and projected issuance of Tax Anticipation Notes.

The returns below are reported gross of fees and are compared to each manager's respective benchmark. The Commission periodically reviews manager fees against appropriate peer groups for reasonableness.

Working Capital Portfolio

This portfolio is managed by Alaska Permanent Capital Management (APCM), and held assets in excess of $94 million at December 31, 2020. It is the shortest portfolio of the MCP, with a duration target of 90 days, and is used for day to day cash flow and liquidity needs. The benchmark for this portfolio is the B of A Merrill Lynch 3-

Month U.S. Treasury Bill Index. In calendar year 2020, the APCM Portfolio returned 0.65%, while its benchmark returned 0.67%.

Contingency Portfolio

This portfolio is managed by PNC Capital Advisors (PNC), and held assets in excess of $96 million at December 31, 2020. It is the middle portfolio of the MCP, with a duration target of 1-3 years. This portfolio provides liquidity when the Working Capital Portfolio has been exhausted, or when rebalancing is required. Its benchmark is the Bloomberg Barclays 1-3 Year US Government/Credit Index. In calendar year 2020, the PNC Portfolio returned 3.78%, while its benchmark returned 3.33%.

Strategic Reserve Portfolio

This portfolio is managed by BlackRock, and held assets in excess of $222 million at December 31, 2020. It is the longest portfolio in the MCP, with a duration target of 3-5 years. This portfolio provides liquidity only when the shorter duration portfolios have been exhausted, or when rebalancing is required. Its benchmark consists of 75% Bloomberg Barclays Intermediate US Government/Credit Index and 25% Bloomberg Barclays Intermediate US High Yield Total Return Index. BlackRock has discretion to invest up to 30% of this portfolio in high yield securities. In calendar year 2020, the BlackRock Portfolio returned 6.89%, while its benchmark returned of 6.47%.

Restricted/Internally Managed Portfolio

This portfolio is managed by the Municipality's Public Finance & Investments Division staff. It is a collection of discretely managed accounts, each containing specifically restricted assets that are required to be managed independent of the MCP. Examples include: Grant proceeds, bond proceeds, debt service reserve accounts, utility customer deposits and other receipts restricted by regulatory order, and certain ASD funds. These accounts are managed primarily for safety and liquidity rather than for return. As of December 31, 2020, the aggregate market value of these accounts was in excess of $200 million. Returns for each account vary and are influenced by the specific restrictions that apply. In 2020, returns for individual accounts ranged from 0.01% to 1.50%.

Conclusion

The Commission reaffirms its commitment to the core tenants of the Trust's investment policy – namely, that diversification and asset allocation remain the most effective strategy to achieve the long-term investment goals of the Trust, while mitigating risk and volatility within the portfolio. The Commission also reaffirms that the MCP and the Restricted/Internally Managed Portfolio are being managed in an appropriate manner consistent with investment parameters approved by the Assembly, and with an appropriate level of review and input by the Investment Advisory Commission.

This annual report was approved unanimously by the Commission at its May 12, 2021 regular meeting.

/Ty Schommer/, Chair
Investment Advisory Commission