



**January 23, 2017**

**To:** Members of the Board of Directors  
**From:** Darrell Johnson, Chief Executive Officer  
**Subject:** Fourth Quarter 2016 Debt and Investment Report

### **Overview**

The California Government Code authorizes the Orange County Transportation Authority Treasurer to submit a quarterly investment report detailing the investment activity for the period. This investment report covers the fourth quarter of 2016, October through December, and includes a discussion on the Orange County Transportation Authority's debt portfolio.

### **Recommendation**

Receive and file the Quarterly Debt and Investment Report prepared by the Treasurer as an information item.

### **Discussion**

The Treasurer is currently managing the Orange County Transportation Authority's (OCTA) investment portfolio totaling \$1.5 billion as of December 31, 2016. The portfolio is divided into two managed portfolios: the liquid portfolio for immediate cash needs and the short-term portfolio for future budgeted expenditures. In addition to these portfolios, OCTA has funds invested in a debt service reserve fund for the 91 Express Lanes.

OCTA's debt portfolio had an outstanding principal balance of \$434.6 million as of December 31, 2016. Approximately 75 percent of the outstanding balance is comprised of Measure M2 debt and 25 percent is associated with the 91 Express Lanes Program.

**Economic Summary:** In a well-telegraphed and long-anticipated move, the Federal Open Market Committee (Fed) raised the Fed Funds rate from 0.25 percent to 0.50 percent. Fed officials later voiced growing confidence that the United States economy is moving closer to the central bank's targets on unemployment and inflation. The new focus is just how quickly to raise interest

rates this year amid investor optimism that President-elect Donald Trump can shake the economy out of its low-growth pace by delivering tax cuts and investment and regulatory reforms. Minutes of the Fed policy meeting last month showed officials were shifting their attention toward the risk that expansionary fiscal policy may warrant a faster pace of rate hikes than expected. Still, most members of the committee agreed that a gradual pace of rate increases was likely to be appropriate.

The labor market continued to grow throughout 2016 averaging 180,000 new jobs per month and a year-end unemployment rate of 4.7 percent. The bigger story, at least in the eyes of the Fed, was the increase in average hourly earnings rising 2.9 percent from a year earlier, the biggest jump since 2009. A result of lower unemployment is evidenced in job openings where there were 1.3 unemployed people applying for every opening in November, compared with 1.9 people when the recession began at the end of 2007.

**Debt Portfolio Activity:** There was no debt activity during the quarter. The outstanding balances for each of OCTA's debt securities are presented in Attachment A.

During the quarter, OCTA continued with its pursuit of a Transportation Infrastructure Finance and Innovation Act (TIFIA) loan for the Interstate 405 Improvement Project (405 Project). In December 2016, Chair Donchak, Vice-Chair Hennessey, OCTA staff, and various finance team consultants traveled to New York to meet with Standard and Poor's, Moody's Investment Service, Fitch Ratings, Kroll Bond Rating Agency, and DBRS to discuss the 405 Project and a TIFIA loan. OCTA will need to provide two investment grade ratings to TIFIA in order to close on the loan.

During the meetings, OCTA representatives discussed the background of the 405 Project, TIFIA loan, and our current schedule for funding the project. The meetings focused on risk mitigations, right-of-way acquisition, utility relocation, design-build selection, toll operating agreement, a review of our traffic and revenue study, and the financial model used to forecast future revenues and operations. The meetings were well received.

OCTA also continues to have update calls with TIFIA staff members to monitor the status of the TIFIA loan.

**Investment Portfolio Activity:** On November 9, 2016, OCTA transferred \$70 million from the liquid portfolio to the short-term portfolio. The transfer was a strategic move to increase diversification and reduce the balance of the liquid portfolio.

Investment Portfolio Compliance: There were no compliance violations during the quarter. OCTA continues its policy of reviewing the contents of the investment portfolio on a weekly basis to ensure compliance for each day of the week. Attachment B provides a comparison of the portfolio holdings as of December 31, 2016, to the diversification guidelines of the policy.

Investment Portfolio Performance Versus Selected Benchmarks: OCTA uses Clearwater Analytics to calculate performance for each manager within the respective portfolios. The performance reports calculate monthly total rates of return based upon the market value of the portfolios they manage. The securities are marked-to-market daily based on pricing data provided by the custody banks.

OCTA has calculated the total returns for each of the investment managers for short-term operating monies and has compared the returns to specific benchmarks as shown in Attachment C. Attachment D contains an annualized total return performance comparison by investment manager for the previous two years. Attachment E provides a five-year yield comparison between the short-term investment managers, Orange County Investment Portfolio, and Local Agency Investment Fund.

The returns for OCTA's short-term operating monies are compared to the Bank of America Merrill Lynch (BAML) 1-3 year Treasury (Treasury) and the BAML 1-3 year AAA-A U.S. Corporate and Government (Corporate/Government) benchmarks. The BAML 1-3 year indices are among the most commonly used short-term fixed-income benchmarks. Each of the four managers invests in a combination of securities that all conform to OCTA's 2016 Investment Policy. For the quarter ending December 31, 2016, the weighted average total return for OCTA's short-term portfolio was -0.39 percent, outperforming the Treasury benchmark return of -0.43 percent by 4 basis points, and outperforming the Corporate/Government benchmark return of -0.42 percent by three basis points. For the 12-month period ending December 31, 2016, the portfolio's return totaled 1.06 percent, exceeding the Treasury benchmark by 17 basis points while underperforming the Corporate/Government benchmark by 1 basis point for the same period.

Total return performance for the quarter was negative as yields rose across the board on the increase in short-term rates by the Fed. As yields rise, the market value of fixed-income securities falls. Total return is the interest earned during a given period of time, plus or minus any market gains or losses, both realized and unrealized. Two-year treasuries began the quarter yielding 0.86 percent. By December 31, 2016, the yields climbed to 1.20 percent. OCTA's investment

managers added value by investing in high-quality, non-government fixed-income securities with higher yields during the period.

**Investment Portfolios:** A summary of each investment manager's investment diversification, performance, and maturity schedule is provided in Attachment F. These summaries provide a tool for analyzing the different returns for each manager.

A complete listing of all securities is provided in Attachment G. Each portfolio contains a description of the security, maturity date, book value, market value, and yield provided by Clearwater Analytics.

**Cash Availability for the Next Six Months:** OCTA has reviewed the cash requirements for the next six months. It has been determined that the liquid and the short-term portfolios can fund all projected expenditures during the next six months.

### ***Summary***

As required under the California Government Code, the Orange County Transportation Authority is submitting its quarterly debt and investment report to the Board of Directors. The report summarizes the Orange County Transportation Authority's debt and investment activities for the period October 2016 through December 2016.

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***Attachments***

- A. Orange County Transportation Authority Outstanding Debt December 31, 2016.
- B. Orange County Transportation Authority Investment Policy Compliance December 31, 2016.
- C. Orange County Transportation Authority Short-term Portfolio Performance Review Quarter Ending December 31, 2016.
- D. Orange County Transportation Authority Short-term Portfolio Performance December 31, 2016.
- E. Orange County Transportation Authority Comparative Yield Performance December 31, 2016.
- F. Investment Manager Diversification and Maturity Schedules December 31, 2016.
- G. Orange County Transportation Authority Portfolio Listing as of December 31, 2016.

**Prepared by:**



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