

# Village of Wellington, Florida



## Investment Performance Review Quarter Ended December 31, 2015

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**Table of Contents**

Tab I.

A. Market Review

Tab II.

B. Investment Portfolio Performance

C. Asset Allocation Chart as of December 31, 2015

Tab III. December 31, 2015 Month-End Statement

(statements are available online at [www.pfm.com](http://www.pfm.com))

PFM Funds December 31, 2015 Month-End Statement

(statements are available online at [www.pfmfunds.com](http://www.pfmfunds.com))

Tab IV. Surplus Fund Portfolio Transaction Page for the Quarter

This material is based on information obtained from sources generally believed to be reliable and available to the public, however PFM Asset Management LLC cannot guarantee its accuracy, completeness or suitability. This material is for general information purposes only and is not intended to provide specific advice or recommendation. The information contained in this report is not an offer to purchase or sell any securities.

# TAB I

## **Summary**

- The Federal Open Market Committee (FOMC) increased the target federal funds rate by 25 basis points (bps) (0.25%) at its December meeting — its first rate hike since 2006. In doing so, the FOMC stressed its intention to normalize rates at a gradual pace.
- The year ended with strong job growth momentum as the economy added 292,000 new jobs in December. This brought the 2015 tally to 2.65 million new jobs in total — enough to shrink the unemployment rate to 5%. Wage inflation edged up modestly, suggesting a chance for future inflation.
- While the Federal Reserve (Fed) took the first step to normalize interest rates, other central banks have continued to implement accommodative monetary policies. The European Central Bank (ECB) extended its monetary easing policy through the first quarter of 2017 and cut its deposit rate further into negative territory (-0.3%). The Bank of Japan (BOJ) and People's Bank of China (PBOC) also remain accommodative.

### **Economic Snapshot**

- U.S. gross domestic product (GDP) expanded at a 2% rate in the third quarter, down from the second quarter due to a reduction in inventory accumulation.
- In a year-end bipartisan negotiation, Congress passed a \$1.1 trillion spending and tax budget, which also lifted the 40-year ban on U.S. crude oil exports.
- Global commodity prices continued to fall, increasing concerns over global growth and the sustainability of producers within the energy sector. Headlining this rout were oil prices, which continued to slide, sinking to less than \$35 per barrel in December — the lowest level since February 2009.
- China continued to allow the yuan to weaken, ending the year at its lowest level versus the U.S. dollar in nearly six years. The Chinese economy continued to slow — stoking market concern over the world's second-largest economy — though it is expected to meet its major economic targets for the year.

## **Interest Rates**

- The new target range for the federal funds rate, as established by the FOMC, is 25 to 50 bps, ending the FOMC's seven-year "zero interest rate policy."
- Interest rates across the curve moved up significantly throughout the quarter, with the 10-year rising approximately 23 bps to 2.27% and the two-year moving almost 42 bps to 1.05%.
- On the shorter end, 12-month Treasury bills ticked up approximately 30 bps to 0.60%.

## **Sector Performance**

- U.S. Treasury benchmark returns were negative for all but the shortest maturities (six months and under), as rates rose across the curve. While the rate increase was less pronounced for longer maturities, their extended durations — and accompanying sensitivity to changes in rates — caused their performance to trail the greatest.
- Non-callable federal agency securities performed in line with comparable maturity Treasuries; callable securities modestly outperformed as their incremental yield helped as rates rose.
- Corporate yield spreads reversed the prior quarter's widening, which helped the sector to outperform government-related sectors; however, absolute return was still negative. A-rated issuers were the best-performing quality category.
- Mortgage-backed securities (MBS) were among the strongest-performing sectors in the fourth quarter, aided by slowly rising long-term rates, which helped to slow prepayments; this was particularly true for higher coupon issues. MBS joined municipals as the lone sectors to produce positive performance for the quarter.

### Economic Snapshot

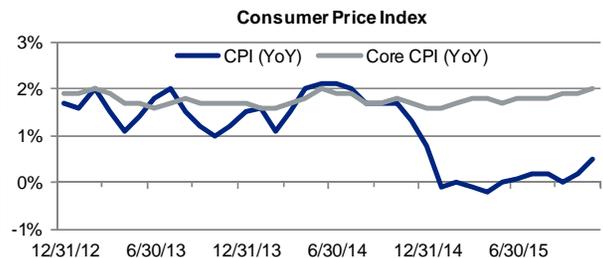
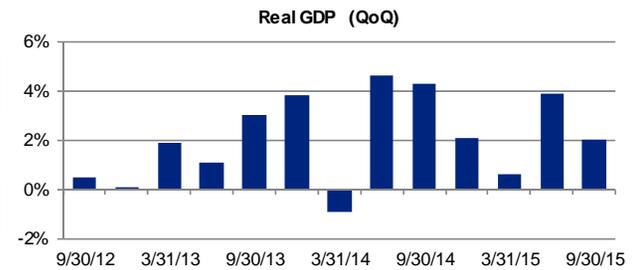
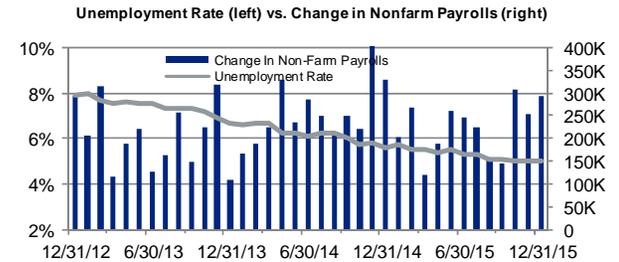
Labor Market		Latest	Sep 2015	Dec 2014
Unemployment Rate	Dec'15	5.0%	5.1%	5.6%
Change In Non-Farm Payrolls	Dec'15	292,000	145,000	329,000
Average Hourly Earnings (YoY)	Dec'15	2.5%	2.3%	1.8%
Personal Income (YoY)	Nov'15	4.4%	4.6%	5.2%
Initial Jobless Claims (week)	1/1/16	277,000	276,000	293,000

Growth				
Real GDP (QoQ SAAR)	2015Q3	2.0%	3.9% <sup>1</sup>	4.3% <sup>2</sup>
GDP Personal Consumption (QoQ SAAR)	2015Q3	3.0%	3.6% <sup>1</sup>	3.5% <sup>2</sup>
Retail Sales (YoY)	Nov'15	1.4%	2.2%	3.3%
ISM Manufacturing Survey (month)	Dec'15	48.2	50.2	55.1
Existing Home Sales SAAR (month)	Nov'15	4.76 mil.	5.55 mil.	5.07 mil.

Inflation / Prices				
Personal Consumption Expenditures (YoY)	Nov'15	0.4%	0.2%	0.8%
Consumer Price Index (YoY)	Nov'15	0.5%	0.0%	0.8%
Consumer Price Index Core (YoY)	Nov'15	2.0%	1.9%	1.6%
Crude Oil Futures (WTI, per barrel)	Dec 31	\$37.04	\$45.09	\$53.27
Gold Futures (oz.)	Dec 31	\$1,060	\$1,116	\$1,184



1. Data as of Second Quarter 2015

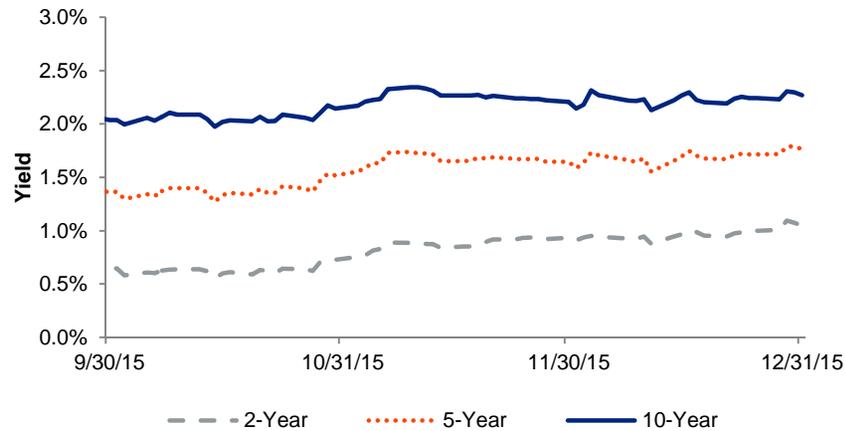
2. Data as of Third Quarter 2014

Note: YoY = year over year, QoQ = quarter over quarter, SAAR = seasonally adjusted annual rate, WTI = West Texas Intermediate crude oil

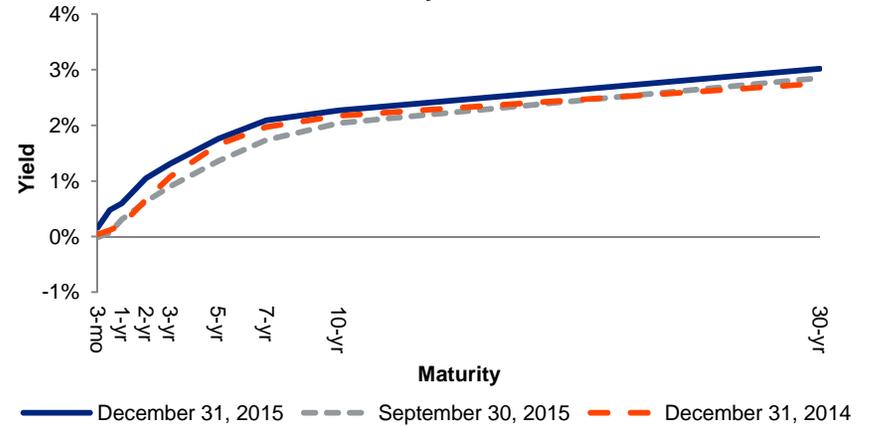
Source: Bloomberg

### Investment Rate Overview

U.S. Treasury Note Yields



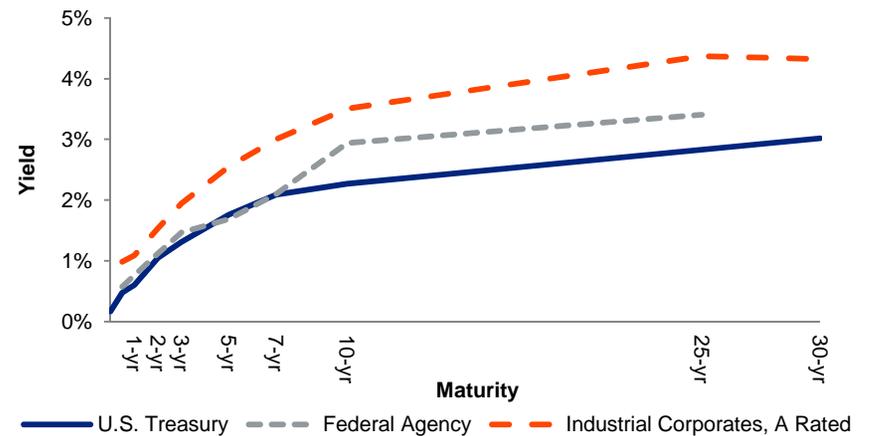
U.S. Treasury Yield Curve



U.S. Treasury Yields

Maturity	12/31/15	9/30/15	Change over Quarter	12/31/14	Change over Year
3-month	0.17%	(0.02%)	0.19%	0.04%	0.13%
1-year	0.60%	0.31%	0.29%	0.22%	0.38%
2-year	1.05%	0.63%	0.42%	0.67%	0.38%
5-year	1.76%	1.36%	0.40%	1.65%	0.11%
10-year	2.27%	2.04%	0.23%	2.17%	0.10%
30-year	3.02%	2.85%	0.17%	2.75%	0.27%

Yield Curves as of 12/31/2015



Source: Bloomberg

## BofA Merrill Lynch Index Returns

	As of 12/31/2015		Returns for Periods ended 12/31/2015		
	Duration	Yield	3 Month	1 Year	3 Years
<b>1-3 Year Indices</b>					
U.S. Treasury	1.87	1.06%	(0.44%)	0.54%	0.51%
Federal Agency	1.73	1.14%	(0.37%)	0.69%	0.61%
U.S. Corporates, A-AAA rated	1.90	1.82%	(0.05%)	1.16%	1.22%
Agency MBS (0 to 3 years)	1.89	1.46%	0.98%	1.68%	1.20%
Municipals	1.84	0.96%	(0.08%)	0.76%	0.85%
<b>1-5 Year Indices</b>					
U.S. Treasury	2.70	1.29%	(0.66%)	0.98%	0.67%
Federal Agency	2.20	1.31%	(0.49%)	0.97%	0.76%
U.S. Corporates, A-AAA rated	2.71	2.13%	(0.16%)	1.52%	1.59%
Agency MBS (0 to 5 years)	3.35	2.23%	0.16%	1.22%	1.69%
Municipals	2.52	1.15%	0.08%	1.20%	1.24%
<b>Master Indices (Maturities 1 Year or Greater)</b>					
U.S. Treasury	6.19	1.77%	(0.93%)	0.83%	1.09%
Federal Agency	3.75	1.69%	(0.65%)	0.99%	1.05%
U.S. Corporates, A-AAA rated	6.64	3.08%	(0.09%)	0.67%	1.97%
Agency MBS (0 to 30 years)	4.53	2.63%	(0.06%)	1.46%	2.00%
Municipals	6.74	2.34%	1.72%	3.55%	3.35%

Returns for periods greater than one year are annualized

Source: BofA Merrill Lynch Indices

**Disclosures**

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**TAB II**

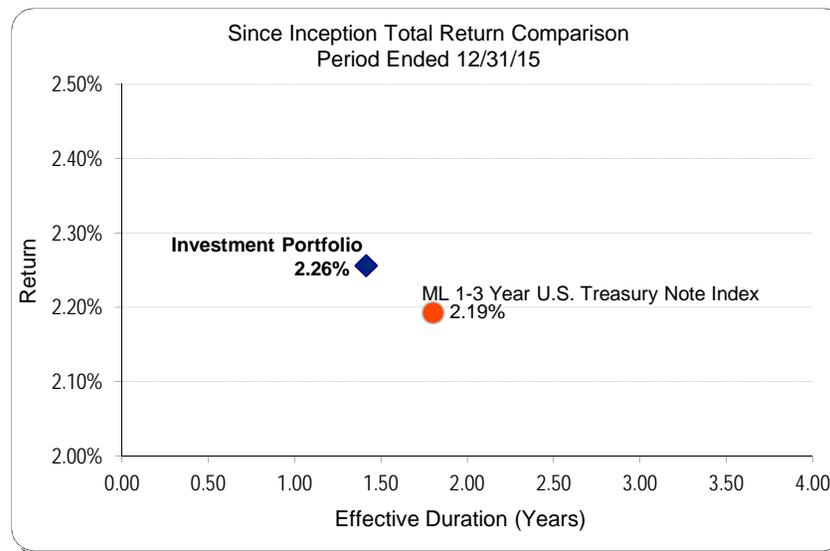
## Executive Summary

## PORTFOLIO STRATEGY

- The Village's Investment Portfolio is of high credit quality and invested in U.S. Treasury, Federal Agency securities, high quality corporate notes, and commercial paper.
- The Investment Portfolio's quarterly total return performance of -0.30% outperformed the benchmark performance of -0.44% by 0.14%. Over the past the year, the Portfolio earned 0.39% versus 0.54% for the benchmark.
- PFMAM maintained a modestly defensive duration position for much of the quarter as rates trended higher. As rates approached the upper end of recent ranges ahead of the FOMC meeting, we extended portfolio durations from short of the benchmark's duration to a near-neutral position; this more closely aligned portfolio durations with the durations of their respective benchmarks.
- Ahead of the December FOMC meeting, market expectations were for an initial Fed Funds hike, supported by assurances that future policy changes would be gradual. Market reaction after the FOMC's announcement to raise the target range for the federal funds rate was relatively subdued, evidence that the action was in line with these expectations, a goal of the FOMC's effort to provide transparency to investors.
- Recent FOMC projections indicate that Committee members anticipate that three or four rate hikes may be appropriate in 2016 – projections that most market participants believe to be overstated. We believe that expectations for low inflation will limit this year's rate hikes to two or three, and that short term yields will trend only modestly higher in the near term. We expect long-term rates to remain within modest ranges, resulting in further flattening of the yield curve.
- We maintain the outlook that the economy will continue to expand at a moderate pace in the intermediate term. We will continue to monitor any spillover effect that modest global growth and muted inflation may have on the U.S. economy. These factors will help justify the FOMC's stated intention to remain patient in the pace at which it raises the federal funds rate.
- PFM will continue to navigate the market environment with a keen focus on relative value sector analysis and efficient yield curve placement. While producing strong investment returns remains a priority, it is secondary to maintaining safety and liquidity, particularly in the current environment where we expect yields to trend higher.

Investment Portfolio Performance

<b>Total Portfolio Value<sup>1</sup></b>	<b>December 31, 2015</b>	<b>September 30, 2015</b>				
Market Value	<b>\$93,050,875.13</b>	\$83,307,308.00				
Amortized Cost	<b>\$93,263,512.79</b>	\$83,090,620.71				
<b>Total Return<sup>2,3,4,5</sup></b>	<b>Quarterly Return December 31, 2015</b>	<b>Last 12 Months</b>	<b>Last 3 Years</b>	<b>Last 5 Years</b>	<b>Last 10 Years</b>	<b>Since Inception on March 31, 2004</b>
<b>Investment Portfolio</b>	<b>-0.30%</b>	<b>0.39%</b>	<b>0.40%</b>	<b>0.61%</b>	<b>2.41%</b>	<b>2.26%</b>
Merrill Lynch 1-3 Year U.S. Treasury Note Index	-0.44%	0.54%	0.51%	0.70%	2.42%	2.19%
<b>Effective Duration(Years)<sup>4,5</sup></b>	<b>December 31, 2015</b>	<b>September 30, 2015</b>			<b>Yields</b>	
<b>Investment Portfolio</b>	<b>1.41</b>	<b>1.41</b>			<b>Yield at Market<sup>6</sup></b>	<b>December 31, 2015</b>
Merrill Lynch 1-3 Year U.S. Treasury Note Index	1.80	1.79			<b>Yield at Cost<sup>7</sup></b>	<b>September 30, 2015</b>
Portfolio Duration % of Benchmark Duration	78%	79%			<b>SBA Yield</b>	<b>0.35%</b>
						<b>0.25%</b>

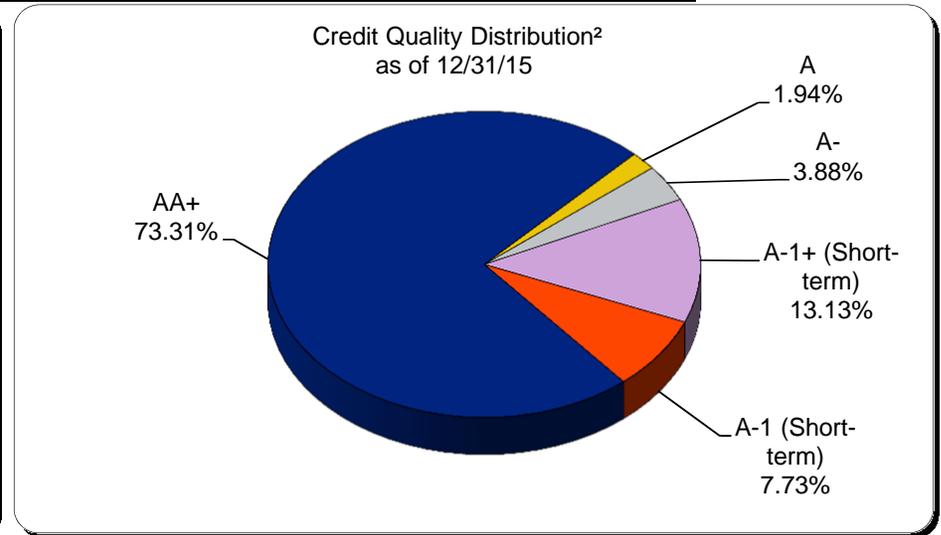
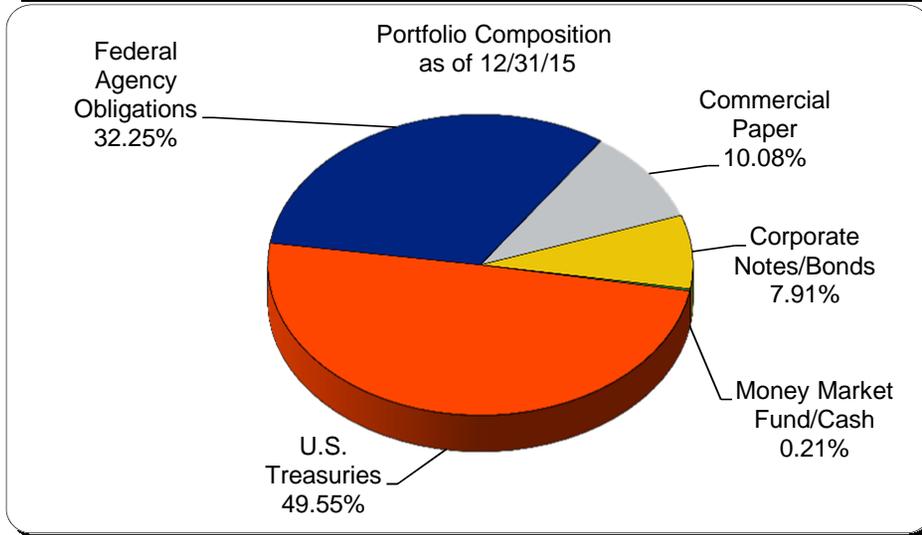


Notes:

- In order to comply with GASB accrual accounting reporting requirements; forward settling trades are included in the monthly balances. End of quarter trade-date market values of portfolio holdings, including accrued interest.
- Performance on trade date basis, gross (i.e., before fees), is in accordance with The CFA Institute's Global Investment Performance Standards (GIPS). Quarterly returns are presented on an unannualized basis. Returns presented for 12 months or longer are presented on an annual basis. Past performance is not indicative of future results.
- Since Inception the benchmark has been the Merrill Lynch 1-3 Year U.S. Treasury Note.
- Merrill Lynch Indices provided by Bloomberg Financial Markets.
- Includes money market fund/cash in performance and duration computations.
- YTM at Market: The yield to maturity at market is the rate of return, based on the current market value, the annual interest receipts, maturity value and the time period remaining until maturity, stated on percentage.
- YTM at Cost: The yield to maturity at cost is the expected rate of return, based on the original cost, the annual interest receipts, maturity value and the time period from purchase date to maturity, stated in percentage.

Investment Portfolio Composition and Credit Quality Characteristics

<u>Security Type<sup>1</sup></u>	<u>December 31, 2015</u>	<u>% of Portfolio</u>	<u>September 30, 2015</u>	<u>% of Portfolio</u>
U.S. Treasuries	\$46,102,944.10	49.5%	\$44,507,912.79	53.4%
Federal Agencies	30,010,962.32	32.3%	26,745,183.93	32.1%
Commercial Paper	9,379,256.80	10.1%	4,392,201.00	5.3%
Certificates of Deposit	0.00	0.0%	0.00	0.0%
Bankers Acceptances	0.00	0.0%	0.00	0.0%
Repurchase Agreements	0.00	0.0%	0.00	0.0%
Municipal Obligations	0.00	0.0%	0.00	0.0%
Corporate Notes/Bonds	7,359,121.80	7.9%	7,369,510.36	8.8%
Mortgage Backed	0.00	0.0%	0.00	0.0%
Money Market Fund/Cash	198,590.11	0.2%	292,499.92	0.4%
<b>Totals</b>	<b>\$93,050,875.13</b>	<b>100.0%</b>	<b>\$83,307,308.00</b>	<b>100.0%</b>

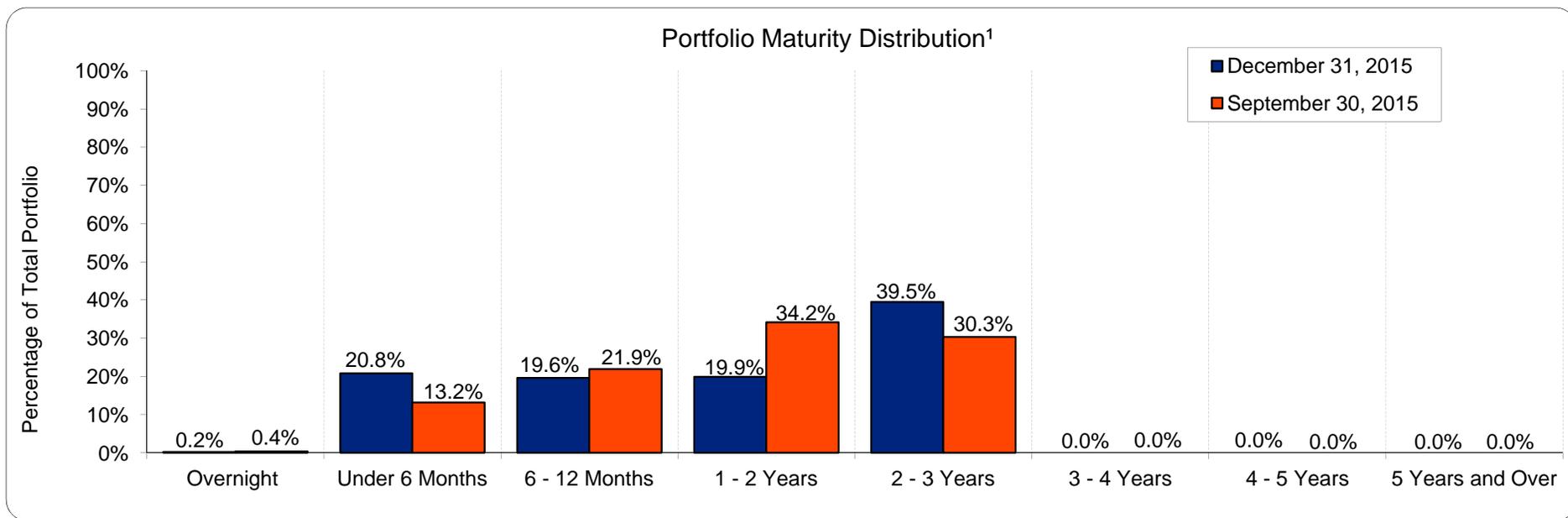


Notes:

1. End of quarter trade-date market values of portfolio holdings, including accrued interest.
2. Credit rating of securities held in portfolio, exclusive of money market fund/LGIP. Standard & Poor's is the source of the credit ratings.

Investment Portfolio Portfolio Maturity Distribution

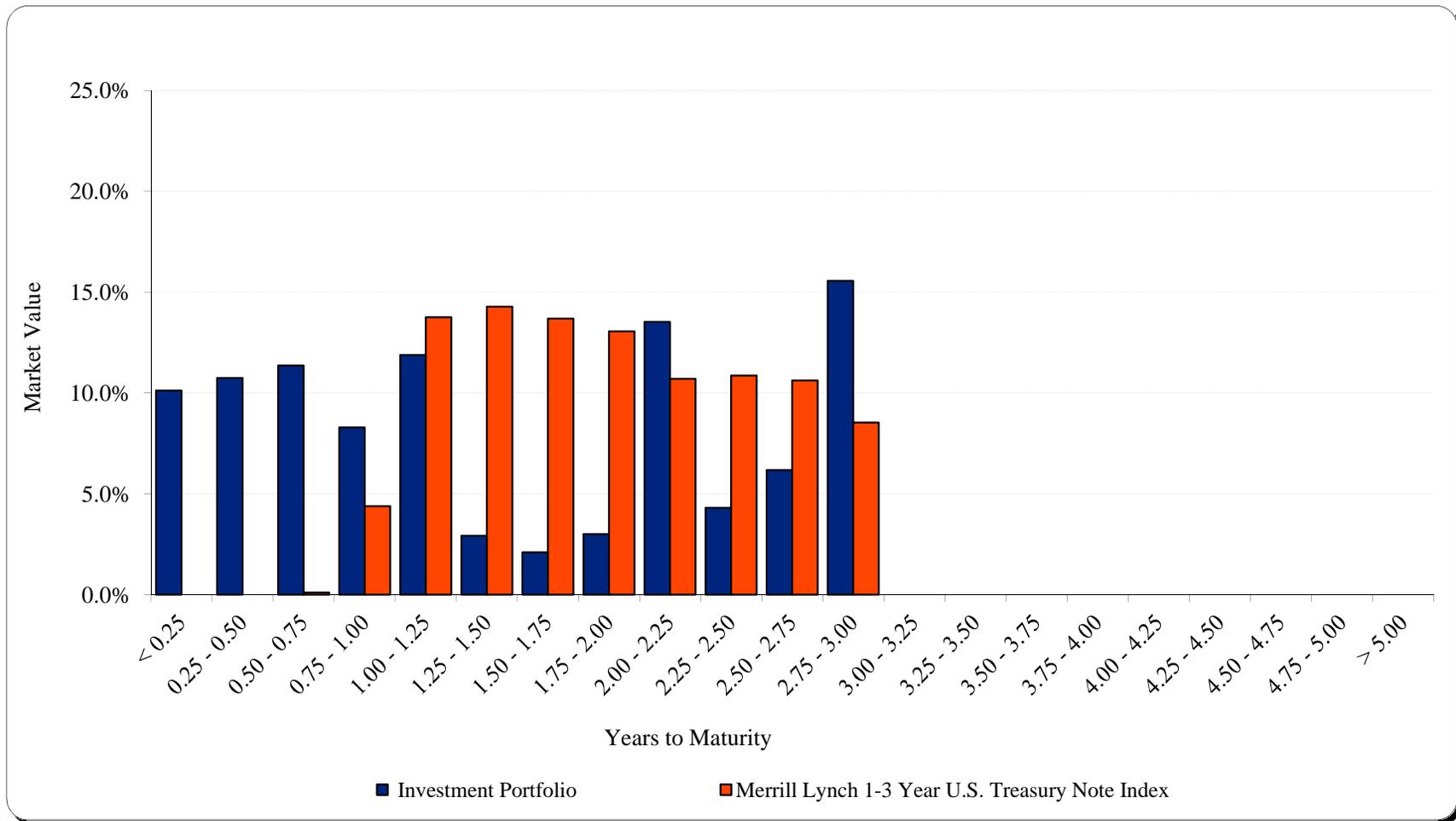
<u>Maturity Distribution<sup>1</sup></u>	<u>December 31, 2015</u>	<u>September 30, 2015</u>
Overnight (Money Market Fund)	\$198,590.11	\$292,499.92
Under 6 Months	19,369,972.90	10,998,238.71
6 - 12 Months	18,239,975.54	18,267,381.51
1 - 2 Years	18,486,608.16	28,480,959.41
2 - 3 Years	36,755,728.42	25,268,228.45
3 - 4 Years	0.00	0.00
4 - 5 Years	0.00	0.00
5 Years and Over	0.00	0.00
<b>Totals</b>	<b>\$93,050,875.13</b>	<b>\$83,307,308.00</b>



Notes:

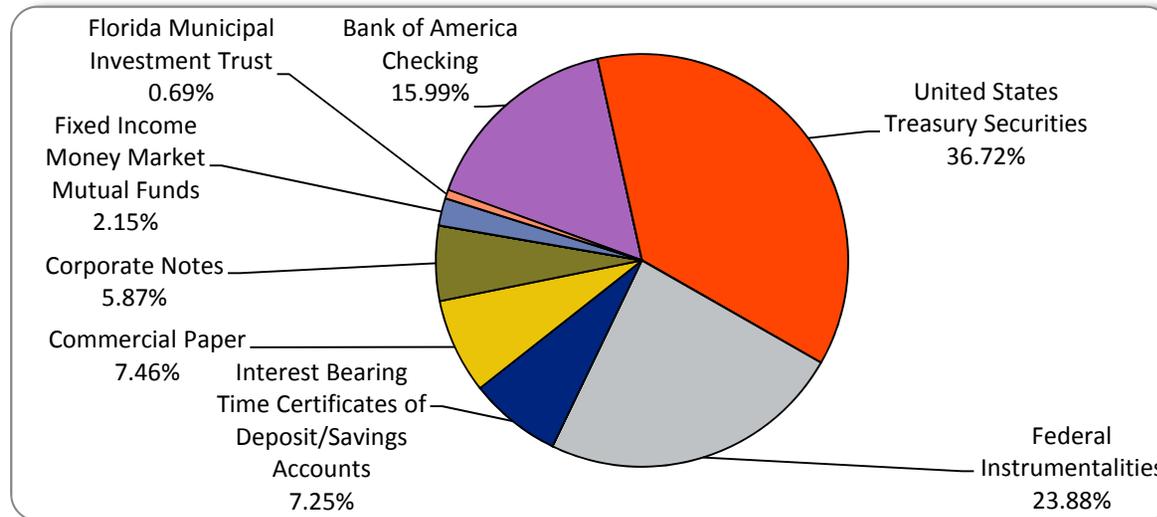
1. Callable securities in portfolio are included in the maturity distribution analysis to their stated maturity date, although they may be called prior to maturity.

Investment Portfolio Maturity Distribution versus the Benchmark<sup>1</sup>



Notes:

1. Due to the nature of the security, Mortgage-Backed Securities are represented based on their average life maturity rather than their final maturity.



Security Type <sup>1</sup>	Amortized Cost (Includes Interest)	Allocation Percentage	Notes	Permitted by Policy	In Compliance
Bank of America Checking	20,118,720.09	15.99%	2,3	100%	YES
Florida SBA Prime Fund	-	0.00%	3	25%	YES
United States Treasury Securities	46,206,806.98	36.72%		100%	YES
United States Government Agency Securities	-	0.00%		50%	YES
Federal Instrumentalities	30,049,122.89	23.88%	4	80%	YES
Mortgage-Backed Securities	-	0.00%	4	20%	YES
Interest Bearing Time Certificates of Deposit/Savings Accounts	9,118,034.77	7.25%	2,3	25%	YES
Repurchase Agreements	-	0.00%		50%	YES
Commercial Paper	9,384,807.50	7.46%		25%	YES
Corporate Notes	7,384,133.07	5.87%		15%	YES
Bankers' Acceptances	-	0.00%		25%	YES
State and/or Local Government Debt	-	0.00%		20%	YES
Fixed Income Money Market Mutual Funds	2,708,493.89	2.15%		50%	YES
Florida Municipal Investment Trust	872,573.28	0.69%	3	15%	YES

Notes:

1. End of month trade-date amortized cost of portfolio holdings, including accrued interest.
2. Assets invested in overnight demand deposit accounts with Qualified Public Depositories are collateralized in accordance with Florida Statutes Chapter 280.
3. Managed by the Village.
4. The combined total of Federal Instrumentalities and Mortgage Backed Securities can not be more than 80%. The combined total as of December 31, 2015 is 23.88%.

\* All Assets

Individual Issuer Breakdown	Amortized Cost (Includes Interest)	Allocation Percentage	Notes	Permitted by Policy	In Compliance
Government National Mortgage Association (GNMA)	-	0.00%		25%	YES
Federal Farm Credit Bank (FFCB)	-	0.00%		40%	YES
Federal Home Loan Bank (FHLB)	9,010,118.22	7.16%		40%	YES
Federal National Mortgage Association (FNMA)	13,032,427.51	10.36%		40%	YES
Federal Home Loan Mortgage Corporation (FHLMC)	8,006,577.16	6.36%		40%	YES
American Express Company Corporate Notes	2,017,158.08	1.60%		5%	YES
General Electric Capital Corporation Corporate Notes	1,962,620.06	1.56%		5%	YES
JP Morgan Chase & Company Corporate Notes	1,607,301.31	1.28%		5%	YES
Wells Fargo & Company Corporate Notes	1,797,053.62	1.43%		5%	YES
Bank of Tokyo Mitsubishi, Inc. Commercial Paper	2,493,590.28	1.98%		5%	YES
BNP Paribas Commercial Paper	2,493,319.45	1.98%		5%	YES
JP Morgan Chase & Company Commercial Paper	2,198,887.77	1.75%		5%	YES
Toyota Motor Corporation Commercial Paper	2,199,010.00	1.75%		5%	YES
Fidelity (BONY) Money Market Fund	198,590.11	0.16%		25%	YES
Bank of America Operating	20,118,720.09	15.99%	2,3	100%	YES
Bank of America Money Market Savings	9,118,034.77	7.25%	2,3	15%	YES
FMLvT - Intermediate	771,187.38	0.61%	3	15%	YES
FMLvT - 1-3 years	101,385.90	0.08%	3	15%	YES
PFM Funds Government Series Money Market Fund	2,509,903.78	1.99%		25%	YES

Notes:

1. End of month trade-date amortized cost of portfolio holdings, including accrued interest.
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- \* All Assets