“The Supply Conundrum”

Rick Coryell, CFA
Senior Portfolio Manager
City of Los Angeles
COLA General Pool – $7.3 billion

Two portfolios

Core (Liquidity account) – $1.3 billion - Eff Duration - .10 or 36 days

1. Liquidity
2. Safety of principal
3. Rate of return

Reserve (1 to 5 years) - $6.0 billion – Eff Duration – 2.68 years

1. Rate of return
2. Safety of principal
3. Liquidity
Expanding Possibilities for Core Account

• Agency Mortgage Backed Securities
• Asset Backed Securities
• Asset Backed Commercial Paper
• Tri Party Repo
• Sovereign and Supranational Issuers
Agency Mortgage Backed Securities

• Offers Monthly liquidity
• Currently Overvalued due to Fed purchases
• COLA hasn’t purchased any since 2010
• Only purchase if you have the ability to analyze
  • Bloomberg – OAS₁ screen
  • Analytical software (Bondedge)
• Negotiate on price only
• Look at recent TRACE activity for guidance
• Don’t increase prepayment speeds
• Ask broker for a Bloomberg printout of
Asset Backed Securities

• Offers Monthly liquidity
• Hard to manage if not in your index
• City of LA currently does not purchase due to index constraints and credit monitoring (Merton Model uses Stock price)
• Cant use Probability of Default (Merton model)
Asset Backed Commercial Paper

Many of the offerings are private placements
• CDIAC report and COLA’s Advisor recommends against buying 144A securities.
• Only selected issuers can be approved
• FCAR (Ford Credit Auto Receivables) is one we are currently reviewing
  • A₁/P₁ and registered
  • Issuance is still low
Tri Party Repo

• Custodian acts as a intermediary
• COLA only takes in 1-5 year government bonds as collateral (same as securities lending)
• Don’t accept money market funds or long term bonds.
• Currently getting agreements approved
• Best option to expand short term choices
Sovereigns and Supranationals

Issuers are still trying to work with the State of California to get them approved.

COLA does not invest due to current restrictions

Some are trading through U.S. Agencies making them less attractive as an alternative.
Since 2008 COLA has responded to the supply issue by:

Better Financial Management
• More information on future cash flow means less reliance on short term investments.
• Push money out on the curve

Use monthly Reserve rebalance to fund liquidity
• Net sellers in debt service months
• Net buys in months with high tax receipts
Since 2008 COLA has responded to the supply issue by:

Keeping some banks approved, but:
• Keep them short - inside 60 days (Some limit to 14 days)
• Limit exposure to 1 to 3% (depending on each credit)
• Low Probability of Default (Merton Model)
Since 2008 COLA has responded to the supply issue by:

Transfer Corporate and Agency Securities (1 year or less) from Reserve to Core

• Transfer the securities within one year to the Core (liquidity) portfolio.
• Keep corporate and agency issuers even as short term offerings are limited.
• Transfer in months where there is a cash flow need a year out.
• Reduces transaction costs
Some of the things COLA is currently considering

- Tri Party Repo
- Very selected Asset Backed CP programs
- Continuously improving our Cash Flow model
- Visiting Clients (LADWP, LA Airports, Port of Los Angeles, LA Public Works) to gain even more information on future expenditures and bond issuance
  - Talk to Finance and Accounting
  - Talk to Engineers
  - Talk to Senior staff about future plans