

Detroit Water and Sewerage Department

Investment Update

September 4, 2024

616.780.2404

[pfmam.com](https://www.pfmam.com)

PFM Asset Management LLC

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Gray Lepley, Senior Director

Current Economic Environment



Current Market Themes (June 30, 2024)



- ▶ The U.S. economy is characterized by:
 - ▶ Moderating economic growth following two quarters of exceptional strength
 - ▶ Recent inflation prints resuming the path towards the Federal Reserve (Fed)'s 2% target
 - ▶ Labor markets continuing to show strength while unemployment has ticked up modestly
 - ▶ Resilient consumer spending supported by wage growth that is outpacing inflation

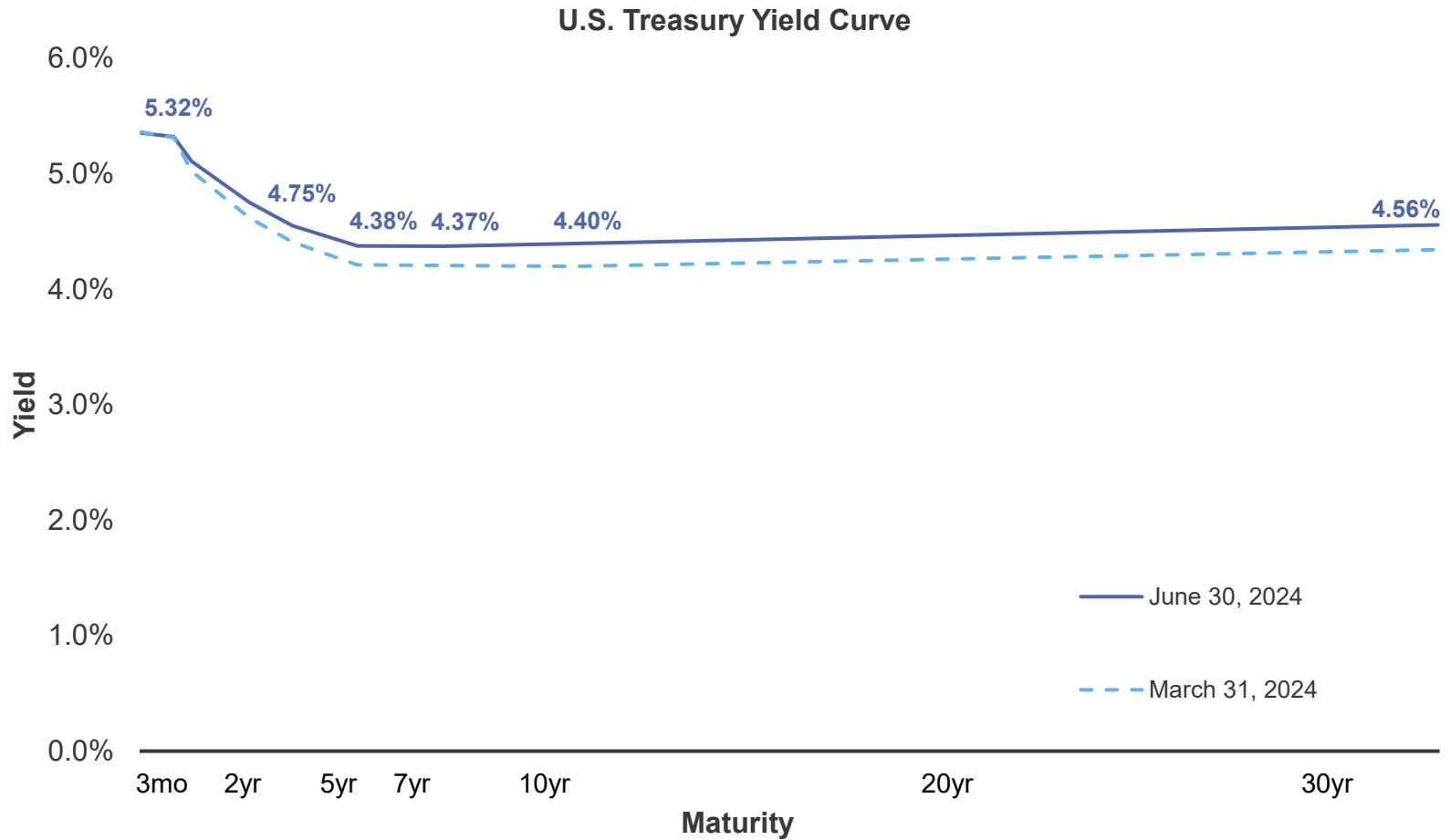


- ▶ Federal Reserve pushes out rate cuts
 - ▶ Fed revises expectations from 3 rate cuts in 2024 to 1 by year end following a lack of progress in the fight against inflation
 - ▶ Market continues to expect 1 or 2 rate cuts in 2024
 - ▶ Fed officials note that the risks to its “dual mandate” of stable inflation and maximum employment are becoming more balanced



- ▶ Treasury yields increase in response to economic data over the quarter
 - ▶ Yields on maturities between 2 and 10 years rose 13-20 basis points during the quarter
 - ▶ The yield curve has now been inverted for 24 months, the longest period in history
 - ▶ Spreads across most sectors remain near multi-year tight and represent market expectations for a soft landing

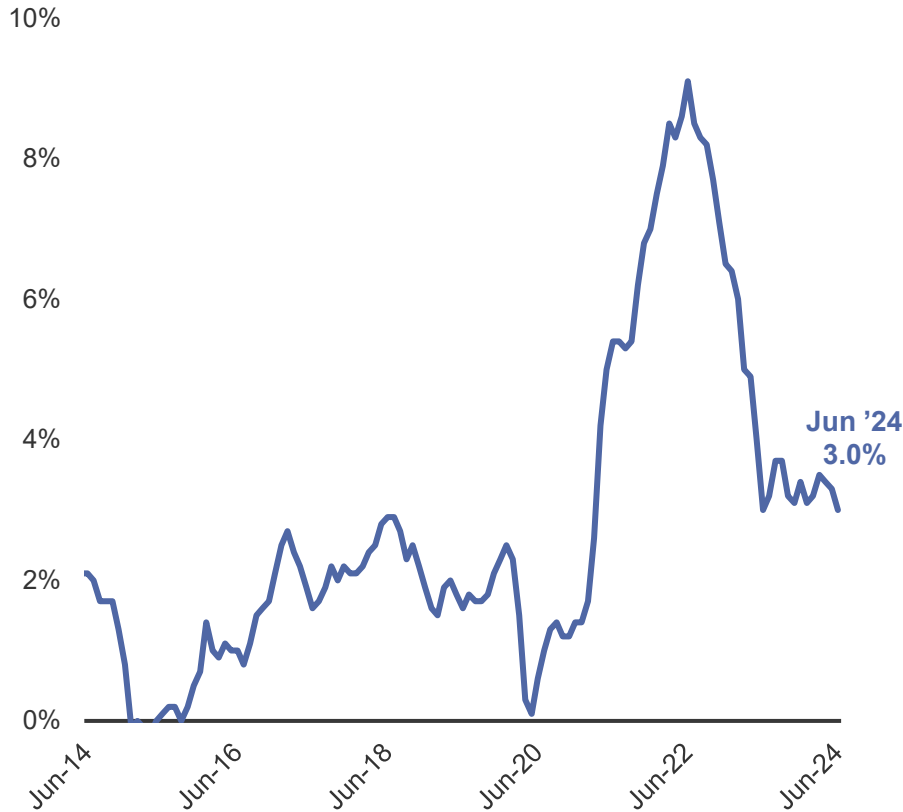
Treasury Yields Move Higher the Quarter as Market Evolves to Revised Fed Expectations



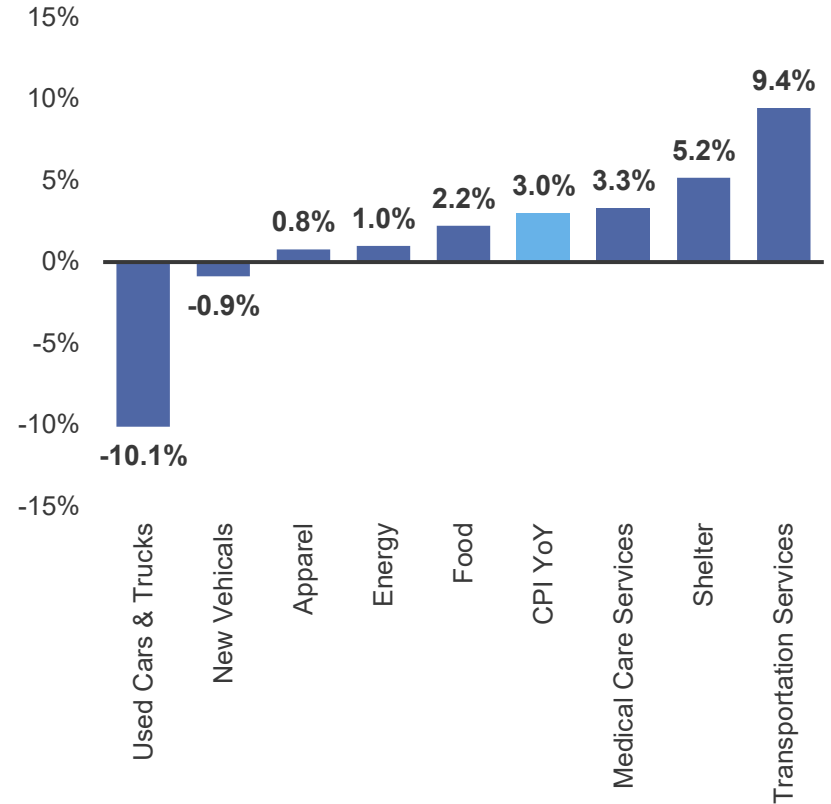
Source: Bloomberg L.P., as of 06/30/2024.

Inflation Continues to Abate

Consumer Price Index % Change YoY



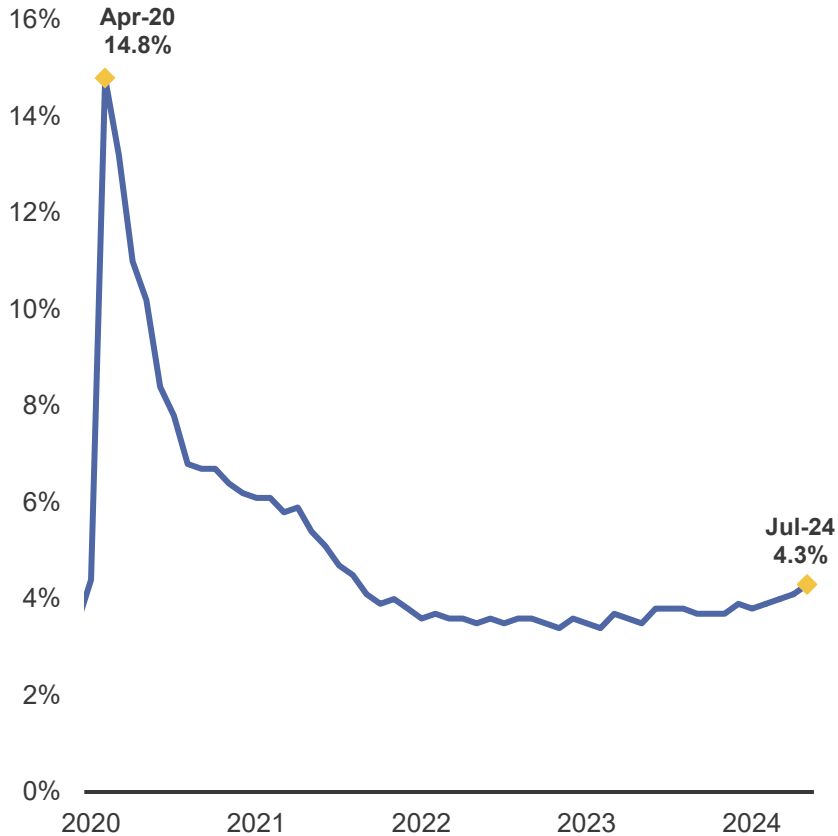
Key Consumer Price Index Components % Change YoY



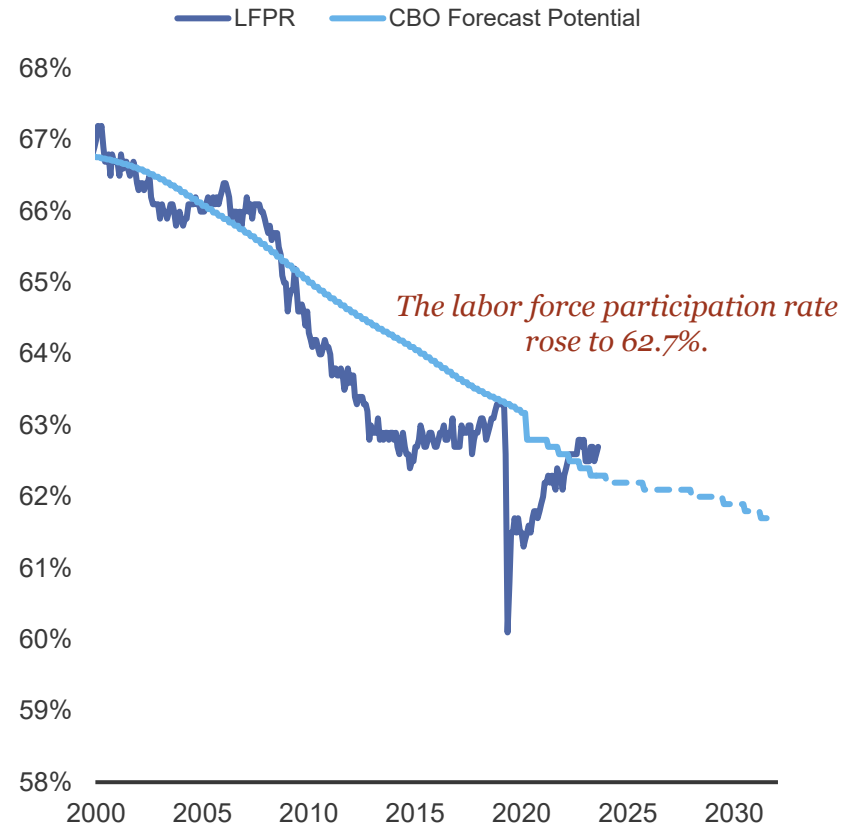
Source: Bloomberg L.P., as of June 2024.

Unemployment Rate Increases

Unemployment Rate



Labor Force Participation Rate



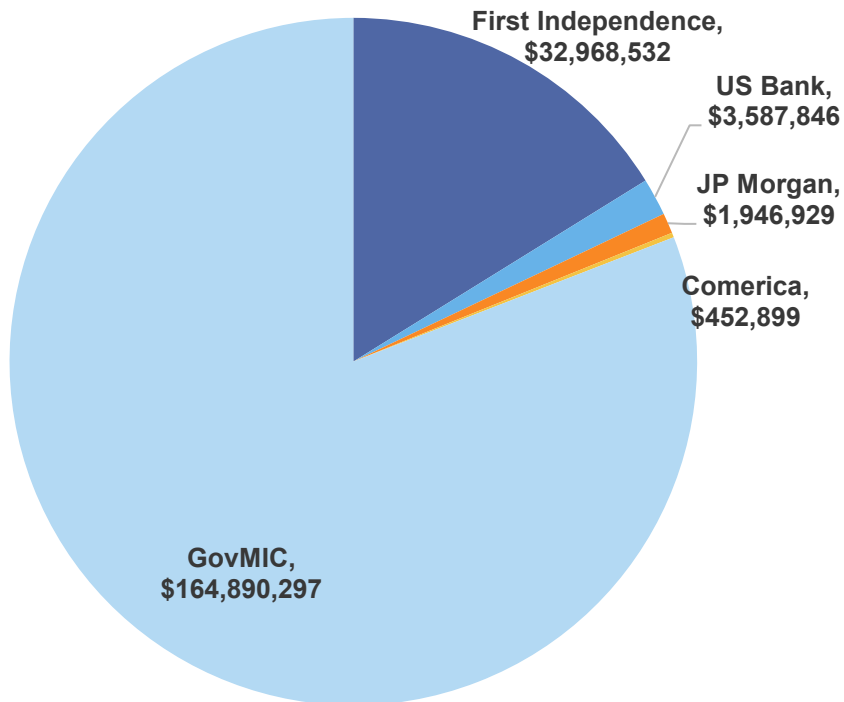
Source: Congressional Budget Office May 2024 economic projections, Bureau of Labor Statistics. Bloomberg L.P., as of July 2024. Data is seasonally adjusted.

Fiscal 2024 Portfolio Review



Portfolio Summary

Investment Allocation – June 30, 2024



Investment Overview

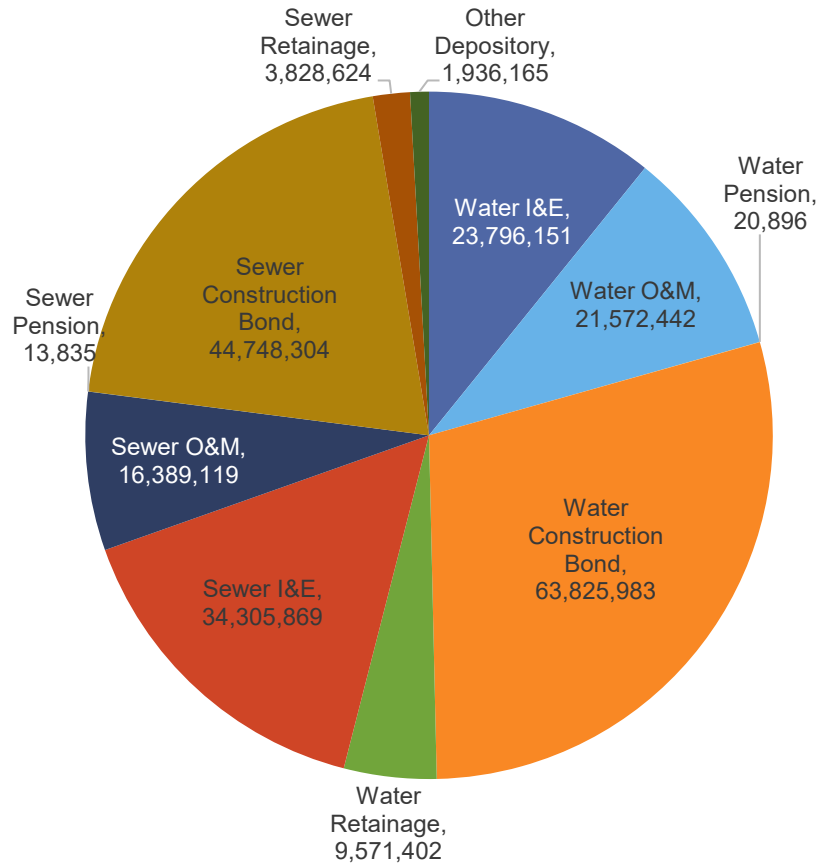
- ▶ At June 30, 2024, the majority of the Department’s funds were held in overnight bank deposits or a Local Government Investment Pool (LGIP)
- ▶ Current investment yields of up to 5.53%
- ▶ Credit ratings and balances are listed below:

Institution	Balances as of June 30, 2024	Bank S&P Rating
US Bank	\$3,587,846	A+/A1
JP Morgan	\$1,946,929	A+/A1
First Independence	\$32,968,532	NR
Comerica	\$452,899	BBB+/A2
GovMIC	\$164,890,297	AAAm
Total	\$203,846,502	

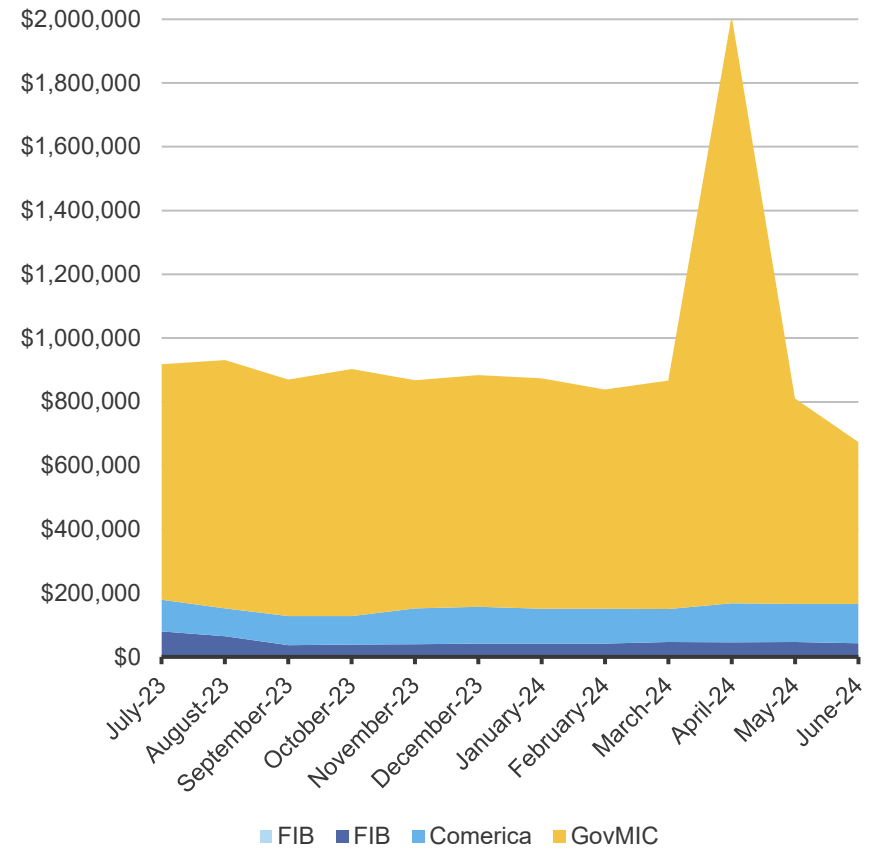
Source: Investment allocation at June 30, 2024 provided by DWSD, Istakur Rahman and NiKole Howard-Whitsett. Bank credit ratings taken from each bank’s Investor Resources webpage. Ratings reflect the Standard and Poor’s Long / Short-term credit ratings at the bank level. See important ratings disclosures at end of presentation.

Investment Portfolio Review – Fiscal 2024

Fund Allocation at June 30, 2024



Monthly Interest Earnings – Fiscal 2024



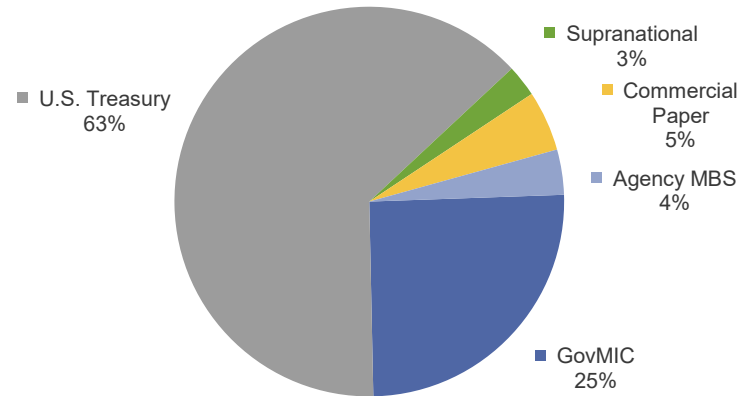
Source: Fund Allocation & Monthly Interest Earnings provided by DWSD at June 30, 2024 by Istakur Rahman and NiKole Howard-Whitsett.

Sewer I&E Investment Summary

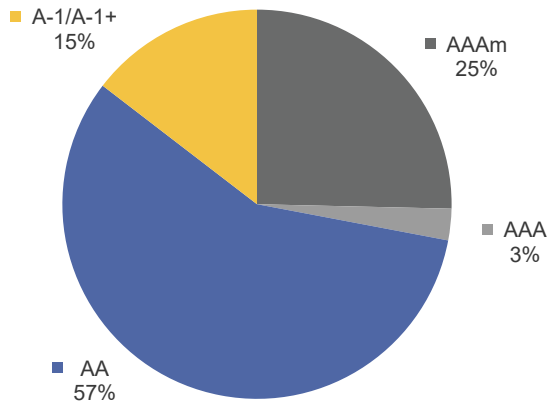
Portfolio Statistics

Market Value & Accrued Interest	\$52,681,609
Average Duration	1.07 years
Average Yield at Cost	5.02%
Average Yield at Market	4.99%

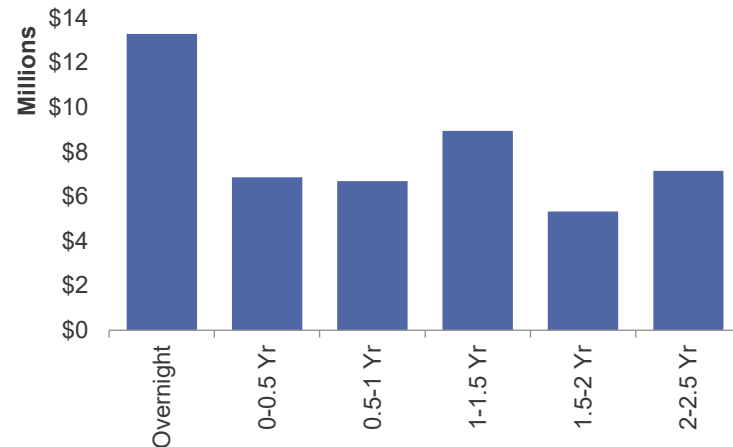
Sector Allocation



Credit Quality



Duration Distribution



All data as of June 30, 2024.
S&P rating, or Moody's equivalent if not rated by S&P.

Portfolio Update



PFMAM's Cash Flow Model

- ▶ Analyzes historical portfolio balances
- ▶ Determines “seasonality” and historical seasonal factors
- ▶ The cash flow model helps identify an appropriate allocation between assets invested short term (“liquidity”) to meet cash needs and assets that can be invested longer-term

Portfolio Type	Strategy Components	Uses
Liquidity/Short-term	Overnight to 12 months	<ul style="list-style-type: none">• Highly Liquid for daily needs and unforeseen expenditures• Funds are meant to cover specific, predictable cash flows (payrolls, debt service)• Can be lower during periods of net cash inflow• Comprised of short-term money market instruments, e.g., bank deposits, money market mutual funds, and LGIP
Core	Longer Duration Strategy	<ul style="list-style-type: none">• Funds that are not expected to be spent—may be disbursed in extraordinary circumstances• Can be invested in longer-term securities

Identifying Investable Funds

Liquidity

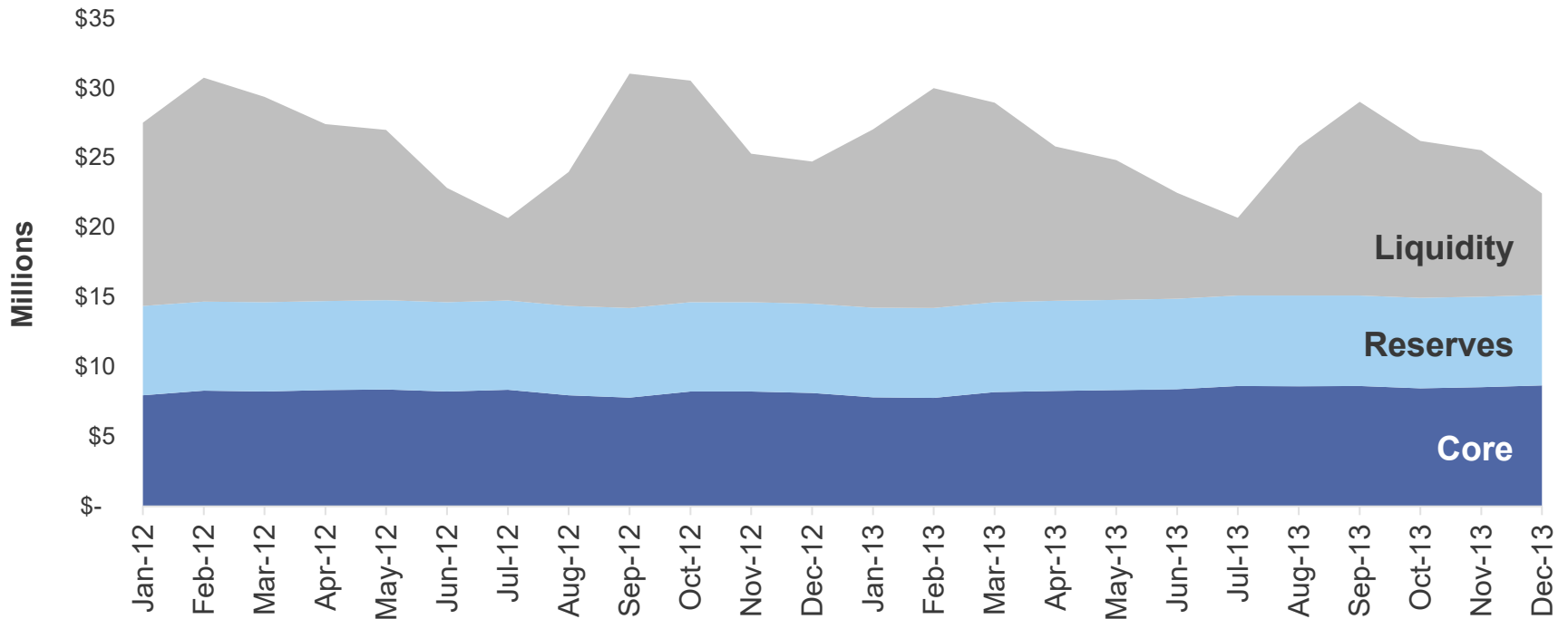
- ▶ Tailored to liquidity needs
- ▶ Lower risk
- ▶ Lower expected earnings
- ▶ Cash and equivalents

Reserves

- ▶ Supplement to Liquidity funds
- ▶ Highly liquid
- ▶ Matched to potential liabilities
- ▶ High quality intermediate-term fixed income

Core

- ▶ Funds not expected to be spent in foreseeable future
- ▶ More volatile
- ▶ High quality longer-term fixed income investments



For illustrative purposes only.

Investment Strategy Recommendations (2023)

- ▶ **Consistent Core** – DWSD has relatively steady historical core balances and may benefit from investing funds farther out on the yield curve.
- ▶ **Extend Duration** – The investment policy allows average duration of up to three years on the overall portfolio; DWSD could increase duration to capture higher expected returns.
- ▶ **Diversification** – A large portion of the current portfolio is invested in bank accounts and overnight liquidity vehicles, which will continue to trend downwards in the current rate environment; DWSD could consider further diversifying and increasing allocations in other types of permitted investments, such as U.S. Treasury notes and Agency MBS.
- ▶ **Active Management** – PFM utilizes active management strategies to improve returns relative to benchmarks; active management techniques include swapping sectors to take advantage of changes in spreads and rolling down the yield curve.

Implementation Progress

✓ Investment Program Review

- Review investment portfolio strategies and practices

✓ Cash Flow Analysis

- Determined an appropriate allocation to a short-term liquidity portfolio to meet ongoing liquidity needs
- Identified the core balance that is available for longer term investments to capture higher expected returns

✓ Investment Policy

- Review for policy in Compliance with Public Act 20 and Government Finance Officer's Association Best Practices

✓ Portfolio Segmentation

- Determine amounts to be invested in each portfolio strategy

✓ Strategy Approval and Implementation

✓ Continual Review of Strategy

Important Rating Disclosures

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GovMIC

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