

Council Meeting  
March 21, 2005

Honorable Mayor and Members  
of the City Council  
City Hall  
Torrance, California

Members of the Council:

**Subject: 2<sup>nd</sup> Quarter 2005-06 Budget Review**

**RECOMMENDATION**

The Finance and Governmental Operations Committee recommends that Your Honorable Body concur with the following recommendations:

- Accept the Mid Year 2005-06 Budget Review Report
- Accept the City Treasurer's Investment Report

**BACKGROUND/ANALYSIS**

On Tuesday, March 7, the Finance and Governmental Operations Committee heard a presentation from staff on the Second Quarter (Mid-Year) 2005-06 Budget Review. The following sections of the report are attached: the Executive Summary and the City Treasurer's Investment Report.

The Committee voted and accepted unanimously the Second Quarter 2005-06 Budget Review Report and the City Treasurer's Investment Report.

Respectfully submitted,

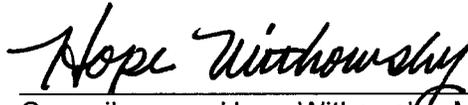
Finance and Governmental Operations Committee



Councilman Frank Scotto, Chair



Councilwoman Pat McIntyre, Member



Councilwoman Hope Witkowski, Member

Attachments:

- Executive Summary
- City Treasurer's Investment Report



**ATTACHMENT A**

Committee Meeting  
March 7, 2006

Honorable Chair and Members  
of the Finance and Governmental Operation Committee  
City Hall  
Torrance, California

Members of the Committee:

**Subject: Mid-Year 2005-06 Budget Review**

**RECOMMENDATION**

The City Manager and the Finance Director recommend that the following items be approved by the Finance and Governmental Operations Committee and recommended to the Council for action:

- Accept the Mid-Year 2005-06 Budget Review Report
- Accept the City Treasurer's Investment Report

**EXECUTIVE SUMMARY**

Revenues for mid-year are projected to meet budget estimates and expenditures for the City are well within budgeted guidelines. As of mid-year, all departments are within budget projections and are projected to be at or below budget by fiscal year end.

As reported earlier, Torrance continues to have a strong underlying economy. The City's tax and economic base includes a mix of high-end residential properties and a sizable commercial and retail component, as evidenced by the City's high per capita retail sales of 210% of U.S. averages. The City has a large property tax base of \$16.7 billion in fiscal 2004, growing 34% over the past 4 years. Wealth and income indicators are above average, with a per capita effective buying power of 121% of the national level and a median household income at 128% of the national level with median home values near \$500,000.

People often say that if the U.S. economy sneezes the World economy catches a cold. The same could be said about the State of California. The gross product, which is broadly defined as the output of goods and services, of California would rank 8th in the world right behind China. The

<b>Gross Product Comparisons, 2004</b>		
All nations with gross product over US\$300 billion		
Rank	Country/Economy	GDP (US\$bil.)
1	United States	\$ 11,733.5
2	Japan	4,668.4
3	Germany	2,706.7
4	United Kingdom	2,125.5
5	France	2,018.1
6	Italy	1,680.7
7	China * (excluding Hong Kong & Macao)	1,649.4
	<b>California</b>	<b>1,524.9</b>
8	Canada	995.8
9	Spain	993.0
	<b>Los Angeles 5-County Area</b>	<b>703.3</b>
10	South Korea	681.5
11	Mexico	676.5
12	India	661.0
13	Australia	617.6
14	Brazil	599.7
15	Russia	582.7
16	The Netherlands	578.0
	<b>Los Angeles County</b>	<b>408.0</b>
17	Switzerland	358.0
18	Belgium	352.0
19	Sweden	346.5
20	Taiwan	305.2
21	Turkey	300.1

Note: Most of the changes in ranking came from exchange rate fluctuations.  
Sources: IMF (WEO Database, 9/2005), LAEDC estimates

California gross product represents about 13% of the U.S. economy. The five-county area of Southern California which includes Los Angeles, Orange, Riverside-San Bernardino, San Diego, and Ventura would rank 10<sup>th</sup> behind Canada and Spain and Los Angeles County alone would rank 17th behind Russia and the Netherlands.

### **Budget Outlook**

The economic forecast for California continues to project moderate economic growth. The Los Angeles County Economic Development Corporation (LAEDC) characterizes the California economy as "steady as she goes". Overall, there is not a great deal of variation among recent forecasts by the Legislative Analyst's Office (LAO), University of California at Los Angeles (UCLA) and the State's Department of Finance (DOF). However, it is interesting that the projections from the DOF are consistently more optimistic than both UCLA, which appears more conservative, and LAO which is in-between. Only time will tell to see whose forecast is most accurate.

The State's budgetary outlook has improved and benefited greatly from an over \$11 billion three year revenue increase since the 2005-06 budget was enacted. The Legislative Analyst Office latest forecast on the State budget has the current 2005-06 fiscal year expenditures exceeding revenues by \$2.6 billion, leaving a \$6.5 billion in the reserve. If the Governor's proposed 2006-07 budget was fully adopted, the State would end with a reserve of \$2.6 billion or \$2 billion more than assumed in the Governor's budget. However, in 2007-08 and 2008-09 the State would continue to have a structural deficit of \$4 billion and \$5 billion respectively.

### **Budgetary Concerns**

#### ***Fuel Costs***

The cost of fuel directly impacts the City's budget. An increase or decrease in a gallon of fuel by \$0.10 will translate to about \$87,500 because the City consumes approximately 850,000 gallons of diesel fuel and 25,000 gallons of unleaded fuel per year. The majority of the diesel fuel, 555,000 gallons, is used for the City's Transit buses. During the calendar year 2003, diesel and unleaded fuel had an average cost of \$1.16 and \$1.42 per gallon respectively. In 2004 average fuel costs for diesel and unleaded were \$1.60 and \$1.77 gallon respectively, an increase of 38% and 25%. At the height of the 2005 hurricane season, diesel and unleaded fuel hit \$2.75 and \$2.73 respectively. Current prices of \$2.16 for diesel and \$2.21 for unleaded, though still high, are much more manageable. The current projection of fuel costs for the General Fund and Transit Operations that fuel will both exceed their budget by approximately \$200,000 and approximately

	Summary of Economic Outlook		
	Forecast		
	2005	2006	2007
United States Real GDP:			
UCLA December	3.6	2.8	2.5
DOF January	3.6	3.2	3.0
LAEDC February	3.5	3.3	3.1
LAO February	3.5	3.3	2.9
Payroll Jobs			
UCLA December	1.6	1.1	0.8
DOF January	1.4	1.3	1.3
LAEDC February	1.4	1.5	1.4
LAO February	1.6	1.5	1.5
California Personal Income			
UCLA December	6.2	5.2	4.5
DOF January	6.0	5.8	5.5
LAEDC February	6.0	6.1	5.9
LAO February	6.3	5.7	5.5
California Taxable Sales			
UCLA December	6.9	5.1	4.0
DOF January	5.3	4.9	5.0
LAEDC February	9.6	9.4	8.7
LAO February	6.5	5.3	5.4
Consumer Price Index			
UCLA December	3.6	2.9	2.1
DOF January	3.9	3.6	3.0
LAEDCO February	3.4	2.8	2.4
LAO February	4.0	2.8	2.1

\$100,000 for all other funds. The City set aside \$300,000 to cover current year fuel increases not including Transit operations. Transit continues to implement operational changes to reduce fuel consumption and stream lined all other areas of their budget to ensure Transit at year-end will overall be within budget parameters.

### ***Workers' Compensation***

Prior to the 2004-05 fiscal year, the cost of workers' compensation has grown significantly over the last few years. However, in 2004-05 and the early part of 2005-06 the City reduced medical, temporary and permanent disability and other expenses for workers' compensation by \$1.8 million due to the implementation of elements of workers' compensation reform. Should this trend continue, this reduction will bring this fund more into balance and require less funds from year end carryover.

On a more optimistic note, revenues are strong at this time and will meet budget projections for the current fiscal year. If current fiscal year receipts continue their strong trend, projected revenues for the 2005-06 fiscal year will likely be revised to reflect slightly higher receipts.

Respectfully submitted,



Eric E. Tsao  
Finance Director

CONCUR:

  
LeRoy J. Jackson  
City Manager



February 27, 2006

COMMITTEE MEETING  
March 7, 2006

Honorable Chair and Members  
 of the Finance & Governmental Operations Committee  
 City Hall  
 Torrance, California

The Treasurer's Office and the Investment Advisory Committee have set out to develop and implement investment procedures that insure the City's investment objectives of a high degree of asset safety, an adequate liquidity to meet operating and capital expenditure needs and a reasonable return of the City's investment assets given the City's foremost goals of safety and liquidity.

### Investment Summary

As of December 31, 2005 total investments of \$232.7 million consisted of the following categories:

1) Pooled Funds (Investment Portfolio)	\$108.2 million
2) Restricted Funds:	
a. Debt issue proceeds	\$ 19.4 million
b. Deferred Compensation	
1) 457	\$ 99.9 million
2) 401(a)	\$ 3.0 million
c. Retirement Health Savings Plan	\$ 2.2 million

The pooled Funds consist of surplus funds invested and managed directly by the City Treasurer. To date the fund has generated year-to-date interest earnings of \$1.8million and the effective rate of return equaled 3.17 %.

The restricted funds, made up of the Debt issue proceeds, Deferred Compensation funds and the Retirement Health Savings Plan are invested accordingly:

- 1) Debt issue proceeds are invested through a trustee appointed under the Debt Trust Indenture. The funds are invested at the direction of the City Treasurer.
- 2) Deferred Compensation fund is managed by a third party administrator - Great West Life. Investment options made available to the participants are selected and approved by the Deferred Compensation Committee. The fund is a self-

directed program. Participants have the ability to direct their contributions among several different investment options.

- 3) The Retirement Health Savings Plan is managed by a third party administrator – ICMA Retirement. Investment Options are made available to the participants and are selected by ICMA Retirement. Participants can direct their contributions among several different investment options. This tax-deferred program has been offered to employees for the purpose of saving dollars to supplement the cost of health expenses upon retirement.

**NOTE:** The Deferred Compensation Plans and the Retirement Health Savings Plan are held in Trust for the benefit of the Participant or their Beneficiaries and are not an asset of the City of Torrance.

### **Investment Forecast**

The Federal Reserve Board has continued to raise rates by 25 basis points (bps) each meeting over the last year. The current Fed Fund Rate is 4.50% and future rate hikes are on the horizon. What does this mean to rates across the short and intermediate curve? Usually you would expect to see a wider spread on the short in the curve and tapering off as it moves out further. However, the curve has been flat with an inverted curve around 3 years out. The FOMC will meet again in March and it is expected that continued tightening will be the agenda.

### **GASB 31 Impact on Investments**

GASB 31 took effect June 1997. The intent of GASB 31 is to bring to light potential liquidity problems by requiring municipalities to mark to market their securities with a maturity greater than one year. This paper gain or loss must be booked against investment earnings at year-end.

One way to avoid the gain/loss issue is to limit all purchases to maturities of less than one year. This condition would then preclude a market valuation and allow investments to be carried on a book value basis. This situation could reduce earnings potential in the loss of yield that a security with a longer term would usually offer.

Within our investment policy we adhere to a buy and hold philosophy. Therefore, our current strategy will not change in light of GASB 31. We will continue to place a percentage of the portfolio out longer on the yield curve to take advantage of higher earnings. At the same time we keep in excess of 35% of the portfolio liquid in order to meet current and future obligations.

At the present time the monthly investment report tracks all securities by listing the face value, book value and market value. The portfolio paper gain or loss is the difference

between book and market value. The unrealized gain/loss is noted monthly even though it is not physically applied to earnings until year-end.

### **Investment Strategy**

For the past three months, there has been very little activity. The Portfolio continued to decline over the last quarter by \$7.6 million. During this time of the year, the City's expenses are greater than the revenue received.

Beginning in January, the City will begin to receive the seasonal revenue sources and the portfolio will begin to increase. Strategically, we will begin to place money out in the market. However, because of the inverted yield curve, any purchases will remain within 2 years. Interest rates have risen over last year and the portfolio will begin to pick up a higher interest rate return on the investments.

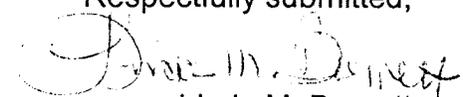
Cash Flow will play an important variable when making investment decisions. During down times it is not unusual to see an average negative monthly cash flow of \$3 million, therefore, it will be our goal to assure adequate coverage during the months of June through December of 2006.

To be consistent with the City's objectives of high degree of Asset safety, all investments will be invested in high quality rated instruments or those guaranteed by the "full faith and credit" of the government.

### **Recommendation**

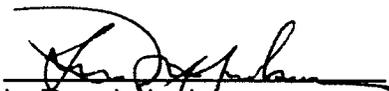
Accept and file the 2<sup>nd</sup> Quarter Report.

Respectfully submitted,



Linda M. Barnett  
City Treasurer

CONCUR:



LeRoy J. Jackson  
Investment Committee Member