



CITY OF MILPITAS AGENDA REPORT (AR)

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| Item Title: | Approve and Authorize the City Manager to Execute the Agreement with Chandler Asset Management for a Five-Year Not-To-Exceed contract amount of \$790,000 for Investment Services. |
| Category: | Consent Calendar-Leadership and Support Services |
| Meeting Date: | 1/21/2020 |
| Staff Contact: | Walter C. Rossmann, 408-586-3111 |
| Recommendation: | Approve and Authorize the City Manager to Execute the Agreement with Chandler Asset Management for a Five-Year Not-To-Exceed contract amount of \$790,000 with the first year of the contract in the amount of \$150,000, for Investment Services to manage the City's pooled portfolio, subject to the annual appropriation of funds. |

BACKGROUND:

The City of Milpitas currently internally manages the investment of its pooled portfolio, which as of June 30, 2019 totaled approximately \$332 million. Of this amount, approximately \$89 million was invested with the State's Local Agency Investment Fund (LAIF) to meet the City's liquidity needs. The City currently has three approved brokers from which investments are made. Portfolio evaluation and reporting are currently performed using Sympro software. For the last decade, the investment of the pooled portfolio has been assigned as a collateral duty to the Finance Technician position. The duties of this position do not provide for effectively researching and analyzing investments which resulted in a dependence on brokers, treasury bonds, LAIF and cash and generated low yields in comparison to the appropriate benchmark. As of the last quarterly investment report, the City's investment pool earned 2.16%, while the performance benchmark of the 3-year Treasury Note earned 2.17% and LAIF earned 2.28%. The average yield for the last four quarters was 2.13% earning the City \$5.2 million in investment income.

As part of the adoption of the FY 2020-21 Budget, Council approved funding to outsource the management of the City's pooled cash portfolio.

ANALYSIS:

On September 13, 2019 the Purchasing Division released a Request for Proposals (RFP) #2373 seeking proposals from qualified vendors with demonstrated experience in managing municipal investment portfolios and implementing a municipal investment policy.

The RFP was publicly noticed in accordance with the City's Municipal Code, advertised on the City's website and emailed to companies registered with the City via ProcureNow.com (the City's eProcurement system). Upon release, 76 firms received the solicitation notification and 15 firms downloaded the RFP documents. The Purchasing Division received two (2) proposals by 2:00 pm on the October 11, 2019 deadline in response to the RFP from PFM Asset Management, LLC and Chandler Asset Management, Inc.

The evaluation committee reviewed proposals based on the following criteria:

1. Cover Letter
2. Company Profile
3. Execution Plan
4. Personnel Assigned
5. Experience
6. References, and

7. Proposed Compensation

After an initial evaluation by three City staff members and one outside evaluator, who comprised the evaluation committee, both firms were invited to and attended an interview to establish their experience, approach, as well as risk and performance analysis in managing municipal investment portfolios. Onsite interviews were held at City Hall on November 7, 2019 and scoring was finalized on November 14, 2019 based on the interviews.

For Chandler, the top-rated firm, reference checks were performed from November 19-20, 2019 to further understand the firm's performance and user experience with references that Chandler included in its response to the RFP. References rated Chandler as an excellent, responsive and knowledgeable firm that assisted each City that served as a reference in increasing its investments. For one city, Chandler was able to increase the investment return by 150%. This was due to Chandler having a greater ability to focus on asset management and its greater knowledge of investing compared to an employee who was charged with these investments as additional duties to her/his job.

The table below shows the final evaluation scores with the recommended firm highlighted in green:

| RFP NO: 2373 | PFM Asset Management, LLC | Chandler Asset Management, Inc. |
|-----------------------------|---------------------------|---------------------------------|
| Final RFP Evaluation Scores | 83.75 | 90.5 |

Chandler Asset Management, Inc. has a long-standing commitment and proven record of performance as an investment manager to the public sector. It was founded in 1988 and has kept paramount the common investment objectives of public agencies of safety of principal, liquidity, and above-market returns over an investment cycle. Their risk management practices and relationship-based approach to investment management have led to the firm's growth, working with 143 public agencies nationwide currently managing over \$17.5 billion in assets.

Chandler will work as a fiduciary on every aspect of the investment program including:

- investment policy development and review,
- cash flow analysis and forecasting, and
- portfolio optimization through the careful control of risk.

Chandler will implement investment strategies that meet the City's risk and return requirements as outlined in the Council approved investment policy, ensure sufficient cash liquidity, conduct education and training to staff, and provide comprehensive investment reporting. The City will maintain its relationship with the Bank of New York (BNY) as the City's cash custodian, ensuring that Chandler will never have direct access to any money in the City's investment account. All deposits and withdrawals from the investment account with BNY will still be initiated by City staff. Chandler will only have access to initiate trades to purchase and sell securities that will remain in the investment account with BNY.

Staff recommends the City Council approve Chandler Asset Management as the most qualified vendor. Once Council approves staff's recommendation, staff will transition the investment services to Chandler by March 31, 2020.

POLICY ALTERNATIVE(S):

Alternative 1: Do not outsource the management of the City's investment pool.

Pros: The City would avoid paying annual fees estimated at \$150,000 based on the estimated amount of invested funds outside of LAIF.

Cons: The City would not take advantage of the expertise and know-how of an investment firm.

Reason for Not Recommending: To increase yields on the City's cash pool, the City would have to invest significantly in staff such as reclassify the Finance Technician position to a Financial Analyst position, dedicate

more staff time for the investment function, allocate existing staff capacity from other duties for back-up duties, and train the primary and secondary position in a complex field. In turn, to offset Chandler Asset Management, Inc. annual estimated fee of \$150,000, the firm needs to raise the average annual yield by 5.0 basis points or 0.05 percentage point, which Chandler has achieved with other cities.

FISCAL IMPACT:

The City is heavily invested in LAIF. Therefore, staff anticipates that approximately \$50 million from the City’s LAIF accounts may be transferred to the portfolio of securities to be managed by Chandler, leaving about \$40 million for liquidity needs. With this shift, Chandler may manage approximately \$300 million in the first year of the contract for an estimated annual fee of \$150,000 per the tiered fee structure based on millions of dollars invested as shown below. The annual fee would average approximately 5.0 basis points (0.05 of 1%), but may average slightly higher or lower, depending on the amount ultimately managed. Chandler’s return goals will be to enhance the portfolio’s interest income as well as underlying market value. Given Chandler’s experience and record for generating risk-adjusted above market returns while maintaining safety and liquidity (the California Government Code-mandated objectives of the City’s investment program), staff recommends the award of contract.

Fee Schedule

| Assets Under Management | Annual Asset Management Fee |
|--------------------------------|------------------------------------|
| First \$50 million | 0.08 of 1% (8 basis points) |
| Next \$75 million | 0.06 of 1% (6 basis points) |
| Next \$125 million | 0.04 of 1% (4 basis points) |
| Assets over \$250 million | 0.03 of 1% (3 basis points) |

Chandler calculates fees based on the average monthly balance of assets under their direct management. Fees are charged monthly in arrears. The fee schedule is firm for the entire five-year term of the agreement and the City will not be subject to any fee schedule increases during this period. Further, there are no separate or one-time fees associated with the investment management and advisory services provided. The proposed fee schedule is all-inclusive for the services that Chandler provides, including full time investment management, technological resources, onboarding and implementation, online access to the Chandler Client Portal, comprehensive reporting, meetings, personal visits, and educational offerings for staff as well as the treasury management support services.

To arrive at the not-to-exceed contract amount for the five-year contract, staff had to model possible future balances. The modeling assumes a 5% growth in the City’s cash pool in addition to up to \$50 million transferred to the portfolio of securities. Based on the tiered fee structure for assets under management, the estimated contract amount for the five-year contract is \$790,000.

| Contract Year | Assets Under Management | Estimated Annual Contract Amount |
|--|--------------------------------|---|
| Year 1 | \$ 300 million | \$150,000 |
| Year 2 | \$ 313 million | \$154,000 |
| Year 3 | \$ 326 million | \$158,000 |
| Year 4 | \$ 340 million | \$162,000 |
| Year 5 | \$ 354 million | \$166,000 |
| Total Five-Year Contract Estimated Amount | | \$790,000 |

California Environmental Quality Act (CEQA):

Not applicable.

Recommendation:

Approve and authorize the City Manager to Execute the Agreement with Chandler Asset Management for a Five-Year Not-To-Exceed contract amount of \$790,000 with the first year of the contract in the amount of \$150,000, for Investment Services to manage the City's pooled portfolio, subject to the annual appropriation of funds.

Attachment:

Professional Services Agreement with Chandler Asset Management