

City of Aurora

Investment management quarterly report

December 2016

➤ A BNY MELLON COMPANYSM



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US Fixed Income commentary

Fourth quarter 2016



On November 8th, Donald Trump was elected as the next president, suggesting significant changes to global trade arrangements, tax policies and industrial policy over the next four years. Going into 2017, the timing and details of these policies and the response from important trading partners will be a determining factor for the global economic outlook. Many initial appointments to president-elect Trump's cabinet have come from the business community and are likely to support tax cuts, which should boost investor confidence. With domestic economic data remaining robust, the market had fully priced in the rate hike of 25bp to the Federal funds target rate, to a range of 0.50% to 0.75%, at the time of the Federal Open Market Committee meeting on December 13-14. In Europe the focus is likely to be on upcoming elections in France, the Netherlands, and Germany as well as the Brexit negotiations. The outlook for emerging markets is likely to be heavily influenced by potential Trump policies as well as their implications for the US dollar. Fundamentally, we continue to see some further improvements in the Asian trade complex, but idiosyncratic issues including politics and the collateral damage from fiat money reform to encourage banking usage (India, Venezuela) has the potential to reduce their contribution to global growth.

From a domestic inflation perspective, oil prices and broader commodities have remained volatile, but are firmly in positive territory year-to-date. With West Texas crude prices above \$50, year-over-year declines washed out at the beginning of December. Personal consumption expenditure releases are likely to move into focus next year, although the latest core consumption reading was weaker than expected at 1.6% for November. Similarly, core inflation in the US should continue to face upward pressure from the rental component next year, after a fall from 2.3% to 2.1% since August. Producer price inflation has continued on its upward trajectory at 1.3% for November.

One result from this improving economic and inflation landscape was a significant rise in US Treasury yields. Yields on 10-year US Treasuries steadily climbed from the 1.35% summer low to 1.80% partly in response to improving growth fundamentals, but also due to growing concern that

extraordinarily accommodative global monetary policy may be nearing an end. Then abruptly, following the one-two punch of the election and the December Federal Reserve rate hike, 10-year notes finished the year at 2.45%.

The credit sectors within the fixed income market finished the fourth quarter and 2016 with positive momentum. The performance turnaround from the beginning of the year was supported generally by accommodative global central bank policy, rebounding commodity markets and improving economic data. After all, both the European Central Bank and the Bank of England introduced corporate bond purchase programs as part of their mandates that eventually took risk premiums tighter. The final potential negative catalyst for the year took the form of the US election, which resulted in further risk premium compression on optimism for growth-oriented fiscal policy in 2017. The net result for US investment grade and below investment grade corporate securities was outperformance versus US Treasuries of 4.9% and 15.7% respectively, during 2016. The worst performing sector of significance within fixed income proved to be agency mortgage-backed securities as this sector remains prone to interest rate volatility.

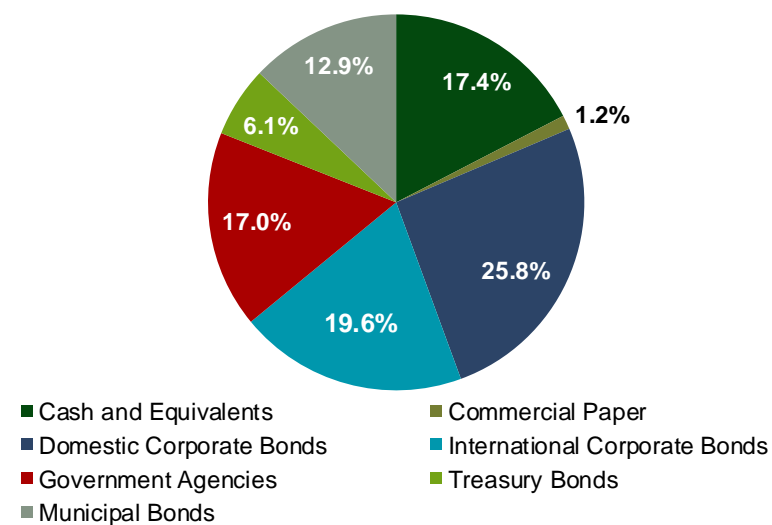
During the past three years market direction was primarily dictated by central bank policy. In thinking about 2017, a more balanced approach to managing macro risks is likely required. Namely, central bank policy, government policy and realized economic growth will likely have equal contributions to market direction. As such, we anticipate evaluating fiscal policies and economic fundamentals more substantially in 2017 as potential catalysts for market change. Perhaps this will lead to healthier investment markets that are not distorted by central bank policy. Maybe true market diversification will be the result, as returns from duration positioning, sector and sub sector allocation will potentially be less correlated.

As of December 31, 2016.

Market environment and strategies

Asset allocation

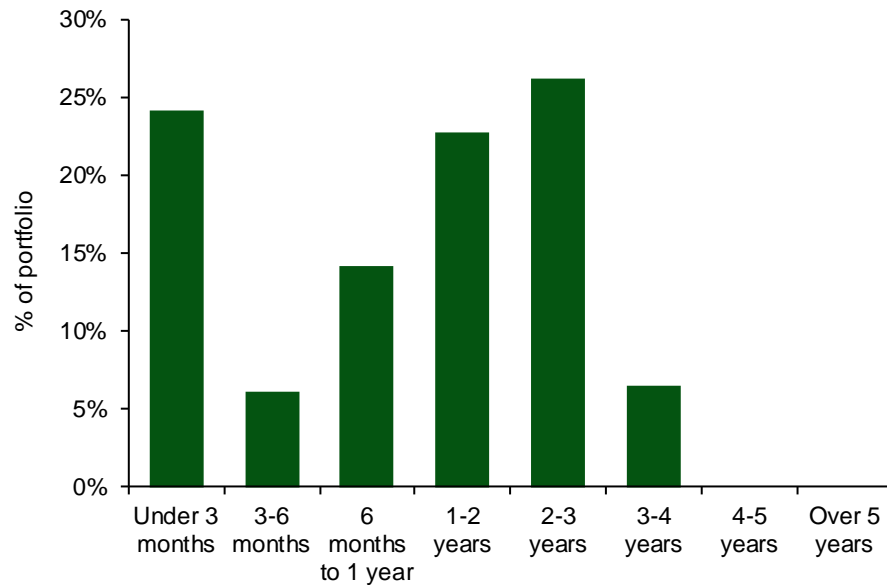
Investment Type	Allocation	Maturity (days)
Cash and Equivalents	17.4%	1
Commercial Paper	1.2%	143
Domestic Corporate Bonds	25.8%	689
International Corporate Bonds	19.6%	525
Government Agencies	17.0%	803
Treasury Bonds	6.1%	1,235
Municipal Bonds	12.9%	471
Total	100.0%	562



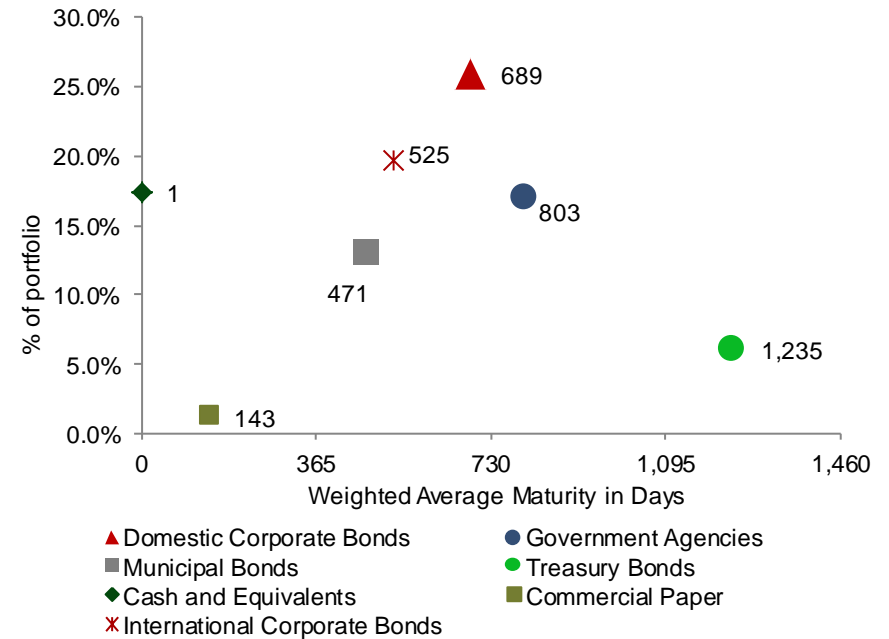
As of December 31, 2016. Asset allocations are subject to change without notice, may not represent current or future decisions and should not be construed as investment recommendations. Please refer to the important disclosures at the back of this presentation

Market environment and strategies

Maturity distribution



Maturity allocation map



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Important disclosures



Important disclosures

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