

City of Oakland Operating Fund

Full Rating Report

Ratings

Security Class	Current Ratings
City of Oakland Operating Fund	AAA/V1

Key Rating Drivers

High Quality Credit Portfolio: The City of Oakland Operating Fund invests primarily in U.S. government agency obligations, the local agency investment fund (LAIF), a local government investment pool managed by California's Pooled Money Investment Board, and certificates of deposit issued by community banks in amounts qualifying for Federal Deposit Insurance Corporation (FDIC) protection.

Active Liquidity Management: The fund is actively managed to meet the projected cash needs of the city of Oakland, CA, and its port by matching portfolio asset maturities with scheduled cash outflows. By its policy, the fund seeks to maintain adequate cash on hand to meet cash disbursements and payroll through maturing investments.

Predictable Cash Flows: The fund benefits from the highly predictable cash outflow needs of the city development projects and the fact that there are no outside participants. Cash flow projections are an integral part of the overall cash management responsibilities of the Treasury Division of the finance and management agency of the city of Oakland.

Appropriate Management and Oversight: Portfolio oversight and operational controls are consistent with the assigned ratings. The City of Oakland Operating Fund is managed by the treasury division of the finance and management agency of the city of Oakland.

What Could Trigger a Rating Action

Changes in the Portfolio: The fund credit and volatility ratings may be sensitive to material changes in the composition, credit quality, and liquidity profile of the portfolio or an increase in unanticipated cash outflows. A materially adverse deviation from Fitch Ratings guidelines for any key rating driver could cause ratings to be lowered by Fitch.

Changes in U.S. Financial Condition: Given that the portfolio consists largely of U.S. Treasury and government agency securities, the ratings may also be sensitive to material adverse changes in the U.S. government's financial condition and that of the broader U.S. economy. On Nov. 28, 2011, Fitch revised the Rating Outlook on the U.S. government's long-term rating to Negative from Stable.

Related Research

[City of Oakland Operating Fund, Oct. 27, 2010](#)
[Local Gov't Investment Pool Ratings Not Affected by U.S. Negative Outlook, Dec. 13, 2011](#)

Analysts

Russ Thomas
+1 312 368-3189
russ.thomas@fitchratings.com

Viktoria Baklanova, CFA
+1 212 908-9162
viktoria.baklanova@fitchratings.com



Rating Rationale

City of Oakland Operating Fund is rated 'AAA/V1' by Fitch. The 'AAA' fund credit rating reflects the investment portfolio's vulnerability to losses as a result of defaults in its bond holdings and is based on the actual and prospective average credit quality of the portfolio's investments.

The 'V1' fund volatility rating reflects the relative sensitivity of the investment portfolio's net asset value to assumed changes in credit spreads and interest rates as well as certain other market risk parameters.

Fitch's evaluation of the fund also considers the management and operational capabilities of Oakland's treasury division and the legal and regulatory framework under which the investment portfolio operates. Fund valuation reports are submitted to Fitch on a monthly basis. As of Sept. 30, 2011, the fund had approximately \$360 million in assets.

Organizational Overview

City of Oakland Operating Fund is the city's primary operating fund. It accounts for all financial activities and resources of the general government except those required to be accounted for in other funds. These activities are funded principally by property taxes, sales and use taxes, business, utility and real estate transfer taxes, interest and investment income, and charges for services. The fund is managed by a team that includes the treasury manager, principal financial analyst, and any other designees who work for the benefit of the city. Authorization for investment decisions is limited to the treasurer and treasury manager. An investment oversight committee composed of representatives of the city council and the public reviews the fund's investment practices and policies on an annual basis. The committee is required to initiate the performance of an annual audit to ensure compliance with established investment policies.

Fund Investment Practices

The fund seeks to pursue its investment objectives by investing mainly in U.S. government agency securities, as well as certificates of deposit insured by the FDIC or overcollateralized by the U.S. government agency securities. Other investments permitted under the fund's investment policy include direct bank obligations, such as certificates of deposit and bankers' acceptances, commercial paper, corporate notes, repurchase agreements, money market mutual funds, and LAIF.

As of Sept. 30, 2011, the pool invested approximately 58% of its total assets in U.S. government agency securities, 15% in money market funds, 14% in LAIF, 9% in commercial paper, 4% in collateralized certificates of deposit and less than 1% in state of California revenue anticipation notes maturing June 26, 2012.

Per the fund's investment policy, permitted securities must be rated at least 'A/F1' by Fitch or equivalent. The fund's investment policy also mandates that investments in a single corporate issuer not exceed 5%, with the exception of investments in U.S. government agency securities, money market funds, and LAIF.

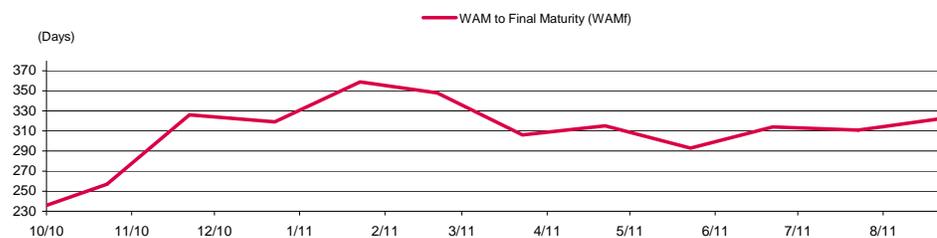
By its investment policy, the fund may invest in repurchase agreements with counterparties rated at least 'A+/F1' by Fitch or equivalent and overcollateralized by at least 102%. Repurchase agreement collateral is restricted to U.S. government agency securities. As of Sept. 30, 2011, the fund did not have any investments in repurchase agreements.

Related Criteria

[Global Bond Fund Rating Criteria, Aug. 16, 2011](#)

The fund's investment policy permits investments in government agency callable step-up and floating-rate securities tied to a short-term index. Securities tied to long-term or lagged indexes, such as the cost of funds index or residual-interest securities, are not eligible for portfolio investments. The fund may enter into reverse-repurchase agreements with broker/dealers for purposes of temporary borrowing to meet unanticipated cash outflow. No such agreements have been used during the past year.

Portfolio Weighted Average Final Maturity
(As of Sept. 30, 2011)



Source: City of Oakland Treasury Division.

As of Sept. 30, 2011, the weighted average final maturity (WAMf) of securities held in the fund was approximately 323 days and the effective duration was 0.6 years, according to Fitch's calculations and based on information provided to Fitch by the City of Oakland. WAMf is the asset-weighted average number of days to the final maturity of all portfolio assets and measures sensitivity to changing credit spreads.

Asset Credit Quality

LAIF is a local government investment pool (LGIP) with assets under management of \$24 billion as of June 30, 2011. LAIF funds are not comingled with the state's cash or in any way available for state use. Fitch does not rate LAIF; however, Fitch views it as being managed in a manner generally consistent with other Fitch-rated LGIPs operating in the state of California, in terms of asset credit quality, issuer diversification, investor diversification, and liquidity management.

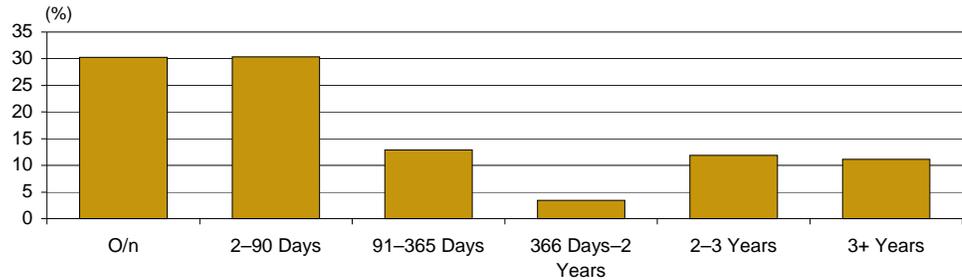
To maintain investor diversification, LAIF limits the maximum size of a single depositor's account to \$50 million, which equates to approximately 14% based on the City of Oakland Operating Fund's assets under management as of Sept. 30, 2011. Aside from this limit, any amount of eligible bond proceeds could be invested in LAIF. As of Sept. 30, 2011, the City of Oakland Operating Fund had a total of \$49.4 million in LAIF.

Fitch generally views investments in LAIF by other rated entities of less than or equal to 15% as consistent with 'AAA/V1' ratings, particularly if such investments serve as the sole or primary source of overnight liquidity. Higher levels of exposure to LAIF may be viewed as consistent with 'AAA/V1' ratings, provided that such additional investment does not serve as the sole or primary source of the portfolio's overnight liquidity.

Weighted Average Rating Factor

Based on the portfolio credit quality and maturity profile as of Sept. 30, 2011, Fitch calculated the weighted average rating factor (WARF) to be consistent with an 'AAA' fund credit rating. This analysis includes a reduction of the credit factors for securities maturing within 13 months, in recognition of the lower default probability of such securities relative to longer dated securities.

Portfolio Maturity Profile^a
(As of Sept. 30, 2011)



^aRepresents final maturity. O/n — Overnight.
Source: City of Oakland Treasury Division.

In calculating a fund’s WARF, Fitch applies higher credit rating factors for ‘AAA’ securities with Negative Rating Outlooks versus ‘AAA’ securities with Stable Rating Outlooks. While the effect of Fitch’s placement of the U.S. government’s long-term rating on Negative Rating Outlook on Nov. 28, 2011 marginally increased the WARF for the fund, the WARF remains consistent with an ‘AAA’ fund credit rating.

Rating Distribution and Minimum Ratings

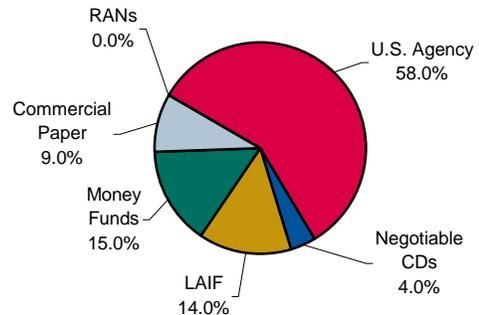
In evaluating the fund, Fitch also considered the portfolio’s minimum asset ratings as well as the extent to which the fund may undertake a barbelled investment strategy. As of Sept. 30, 2011, 99.97% of the portfolio consisted of long-term assets rated ‘AAA’ and short-term assets rated ‘F1’ (or equivalent) or higher. The balance consisted of one bank certificate of deposit with a face amount well under the FDIC-insured limit of \$250,000. The high ratings and absence of a barbelled investment strategy are viewed as consistent with the ‘AAA’ fund credit rating assigned to the portfolio.

Diversification

The fund is highly concentrated in U.S. agency securities, with 27.5% of its total assets in securities issued by Fannie Mae, 11.7% issued by Freddie Mac, 12.3% issued by Federal Home Loan Banks, and 7.4% issued by Federal Farm Credit Banks.

Given the implicit support afforded to the agencies by the U.S. government, the liquidity of the assets, and the diversity by individual agency, Fitch views the exposure as consistent with the assigned ratings. However, the ratings assigned to the fund can be sensitive to any negative rating actions with respect to the U.S. government and its agencies.

Portfolio Composition
(As of Sept. 30, 2011)



RAN – Revenue enhancement notes. Source: City of Oakland Treasury Division.

While the investment portfolio also maintains material exposure to LAIF, Fitch acknowledges that this investment is itself composed of many different underlying obligors, thereby mitigating concentration risk.

Liquidity Management

The fund's cash flows are forecast by the city of Oakland's treasurer's division each month for the following one-year period. The basis for this forecast is the prior year's cash flows, with additional consideration given to identifiable changes in the forecast period. The historically observed stability of cash outflows is supported by on the fund's composition, which has no other participants but the city and its port.

By the fund's policy, the fund is obligated to invest in securities with maturities matched to anticipated cash disbursements and payroll. Cash flow projections are an integral part of the overall cash management responsibilities of the treasurer's office. The fund seeks to meet its liquidity needs by investing in maturity-matching eligible securities. In addition, the fund maintains a portion of its net assets in overnight investments, such as money market funds and LAIF, to provide additional sources of liquidity to meet daily cash outflows.

As of Sept. 30, 2011, 42.7% of the fund's portfolio assets matured within 30 days. Finally, the pool maintains a significant position (approximately 58.9% of total assets) in U.S. government agency securities that are expected to demonstrate secondary market liquidity even during periods of market stress.

The ratings above were solicited by, or on behalf of, the issuer, and therefore, Fitch has been compensated for the provision of the ratings.

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