City of Unalaska

Strategies to Increase Return on Excess Reserves

September 14, 2021

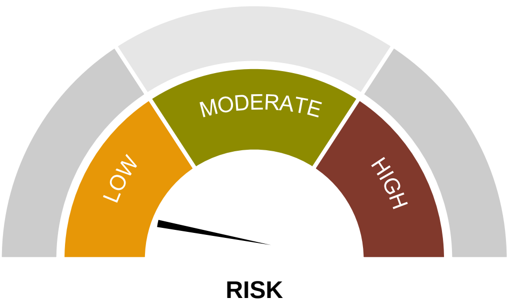
ALASKA PERMANENT CAPITAL MANAGEMENT
Registered Investment Adviser

Agenda & Next Steps

- This presentation focuses on providing details regarding the recommended strategic asset allocations of the new proposed buckets and expected outcomes.
- If the Council chooses to pursue one of the options, APCM will assist the City to implement the new strategy, including:
  - Policy drafting assistance
  - Account creation
  - Funds transfers
- Once all of the new accounts, policies, and necessary Code changes are in place, APCM will implement the new strategic plan.

Summary of Current Strategy

- The City currently invests excess Reserves in cash, cash equivalents, and short-term bonds.
- The risk levels for these investments are low, which also means that the return potential is low. Particularly in today's low interest rate environment.



- The City can utilize the strong Reserve levels (approximately $160M) the Council has built over time to improve long-term fiscal sustainability by diversifying revenue sources.

Operating Cash (<1 Year)	Short-Term Reserves (1-3 Years)
• $1.8M – KeyBank • $47.2M – AMLIP	• $112.3M – 1-3 Year Government (APCM)

*Account values based upon June 30, 2021 market values as detailed in a Memorandum to Council provided to APCM by the City.

Match Reserves to Time Horizon

- Many clients utilize a holistic portfolio approach for cash assets when funds will be withdrawn over time to enhance earnings potential without sacrificing budgetary stability.
- **If cash needs can be predicted fairly well**, pools of assets can be identified to meet budgetary needs over time.
  - Assets needed soon are invested in safer, more liquid assets with lower earnings potential.
  - Assets not needed until later are invested in longer-term assets with higher earnings potential and higher risk.
- As shorter-term assets are utilized, longer-term assets can be sold to replenish short and rainy day reserves, and vice versa.
- **This strategy improves fiscal sustainability through maximization of the City's revenue from investments without jeopardizing budgetary stability.**

Operating Cash	Short-Term Reserves	Rainy Day Reserves	Permanent Fund
Operating cash is placed in either demand deposits or cash equivalents. These are Reserves that will be needed within a one-year time horizon and should be invested to maximize availability and minimize risk rather than improve yield.	Short-Term Reserves are meant for budgetary needs that are 1-3 years out. These Reserves would be invested in short-term Government securities that provide slightly higher yield while maintaining strong liquidity and a low risk profile.	Rainy Day Reserves are meant to provide a source of funds in emergency or crisis situations. These reserves must be available when needed with no specific time horizon. Best invested in longer dated fixed income assets to improve yield and provide capital appreciation in economic downturns.	Permanent Funds can be utilized to improve fiscal sustainability by providing an additional source of revenue. Permanent Funds generally take advantage of higher risk capacity to improve earnings via additional asset classes that improve return expectations.

Bucketing Strategy Breakout

Current Operating Cash

$1.8M – KeyBank*

$47.2M – AMLIP*

Current Short-Term Reserves

$112.3M – 1-3 Year Government (APCM)*

Proposed Bucketing Strategy

Operating Cash

$1.8M – KeyBank

$13.2M – AMLIP

Short-Term Reserves

$95.0M – APCM

Rainy Day Reserves

$25.0M – APCM

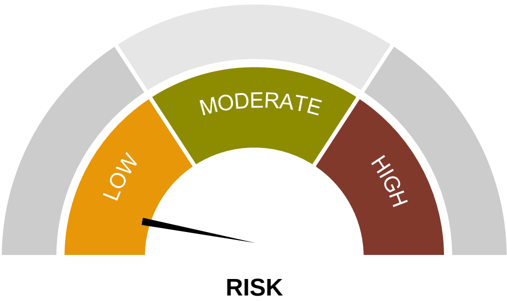
Permanent Fund

$25.0M – APCM

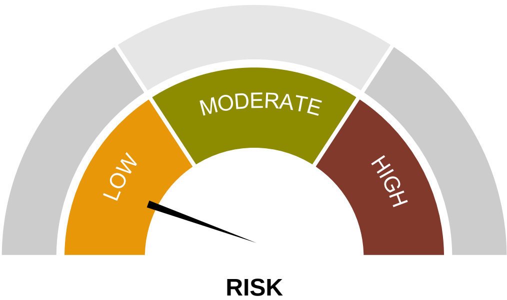
*Account values based upon June 30, 2021 market values as detailed in a Memorandum to Council provided to APCM by the City.

Total Portfolio Risk Remains Low

- With the City's current strategy, **only two types of assets are employed**: cash and equivalents, and short-term fixed income. This keeps risk levels low, but expected returns are also low, given today's low interest rate environment.



- The inclusion of additional types of assets, such as intermediate-term fixed income, equities, and alternatives, **improve the City's revenue possibilities, and provide diversification of the City's Reserves**.
- By introducing stronger diversification, the **improvement in the City's revenue expectations from Reserves can be accomplished with just an incremental increase in expected risk levels**.
- At the Total Portfolio level, the increase in risk is minor, even after including higher risk asset types such as equities into the overall strategic asset allocation. At least 89% of total portfolio assets would remain in cash or fixed income securities.



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Strategy Benefits for the City of Unalaska

01

Risk Increases Only As Risk Capacity Increases

Additional risk is taken only on those Reserves with the capacity for it – a prudent framework to increase earnings without jeopardizing budgets.

02

Improved Earnings Enhance Fiscal Sustainability

The strategy improves earnings expectations from unused Reserves. These earnings can then supplement other revenue if necessary.

03

Budgetary Stability Remains Solid

The approach allows asset levels for each bucket to be adjusted to address the City's changing needs and improve peace of mind.

04

Takes Advantage of Diversification

Because bonds, equities, and alternative asset classes do not behave the same in all market environments, the City can take advantage of diversification to improve return with minimal additional risk.

Bucketing Strategy Recommendations

Investment Horizon

<1 Year	1-3 Years	3-10 Years	>10 Years
Operating Cash	**Short-Term Reserves**	**Rainy Day Reserves**	**Permanent Fund**
$1.8M – KeyBank $13.2M – AMLIP	$95.0M – 1-3 Year Government (APCM)	$25.0M – Intermediate Term Government & Investment Grade Credit (APCM)	$25.0M – Multi-Asset Account (APCM)
No change to strategy recommended, remain in cash and cash equivalents	No change to strategy recommended, remain in 1-3 Year Fixed Income	Extend duration as time horizon for the use of funds is longer than three years	Employ equities, alternatives, and fixed income to create perpetual investment fund to diversify revenue sources

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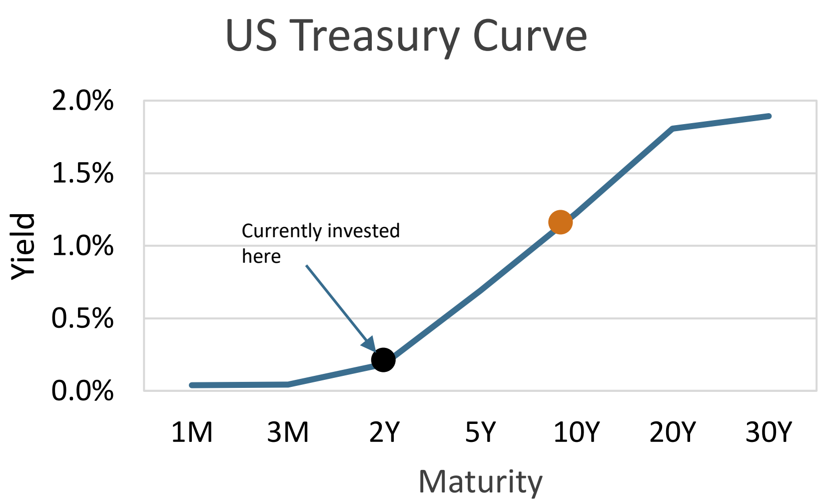
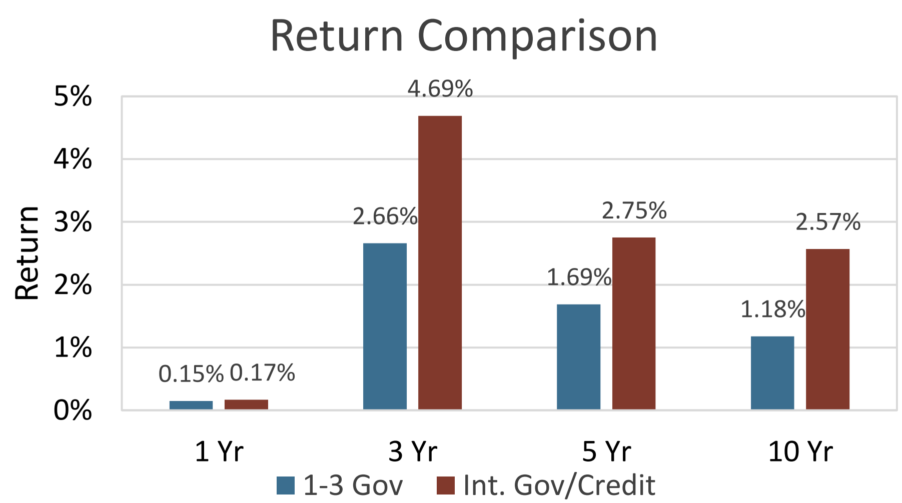
Rainy Day Reserve Recommendation



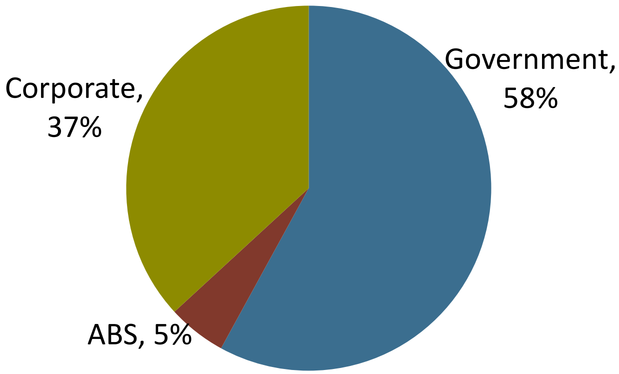


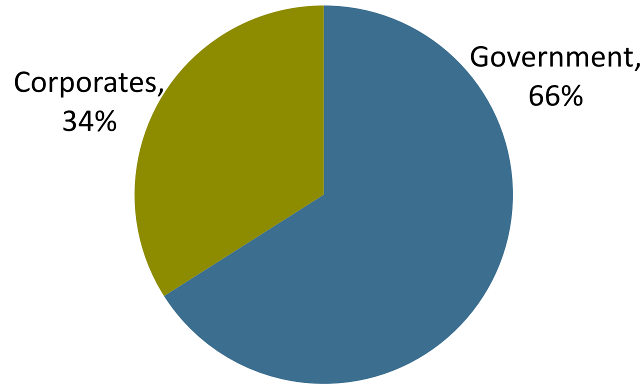
Bloomberg Data as of 8/31/2021

Medium-Term Reserve: $25MM

This account would have a longer time horizon than short-term Reserves and hold securities with maturities between 1 and 10 years, including investment grade corporate bonds. While maturities would be different, the majority of holdings would remain in Treasury securities. Investment grade corporate bonds would add incremental yield to the portfolio. Should the City have a greater cash need than anticipated, funds would be taken from here and moved to the short-term reserves.

Rainy Day Reserve Recommendation

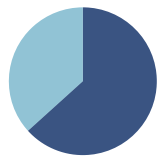
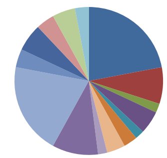
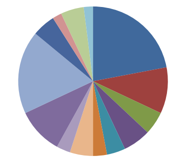




Current APCM Portfolio Characteristics		
Duration		1.95
Yield		0.45%
Maturity		1-3 Years
Quality	AAA	60.8%
	AA	2.4%
	A	11.9%
	BBB	24.9%

Intermediate Gov/Credit Characteristics		
Duration		4.18
Yield		0.87%
Maturity		1-10 Years
Quality	AAA	63.6%
	AA	5.4%
	A	14.1%
	BBB	16.9%

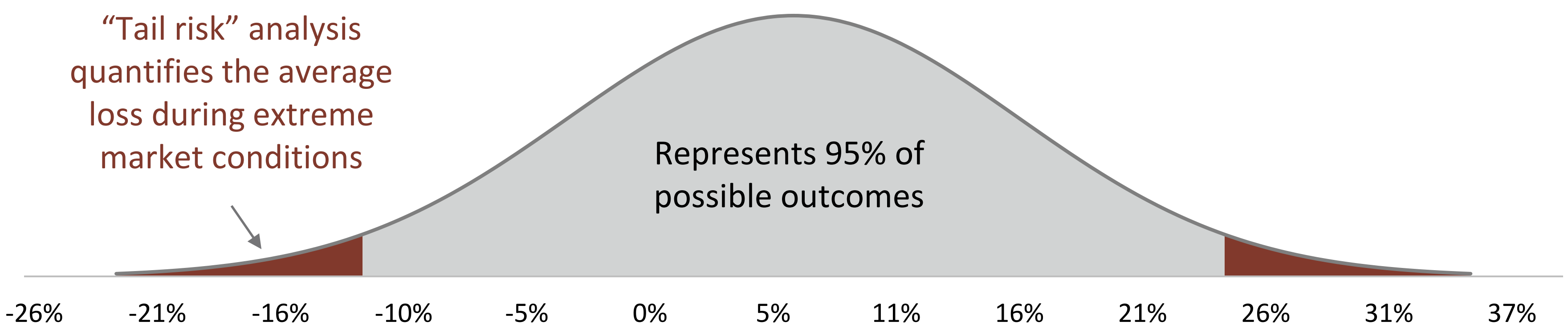
Permanent Fund Portfolio Options

Asset Class	Current Total Portfolio	Option 1	Option 2
Total Equity	**0.0%**	**39.0%**	**47.0%**
Large Cap Equity	0.0%	22.0%	22.0%
Mid Cap Equity	0.0%	8.0%	10.0%
Small Cap Equity	0.0%	2.0%	5.0%
International Equity	0.0%	5.0%	6.0%
Emerging Markets Equity	0.0%	2.0%	4.0%
Total Alternatives	**0.0%**	**19.0%**	**21.0%**
REITs	0.0%	3.0%	3.0%
Infrastructure	0.0%	4.0%	5.0%
Commodities	0.0%	2.0%	3.0%
Alternative Beta	0.0%	10.0%	10.0%
Total Fixed Income	**100.0%**	**42.0%**	**32.0%**
U.S. Fixed Income	0.0%	20.0%	18.0%
U.S. 1-5 Year Gov/Credit	0.0%	4.0%	0.0%
U.S. Corporate High Yield	0.0%	6.0%	5.0%
U.S. 1-3 Year Government	63.3%	0.0%	0.0%
TIPS	0.0%	4.0%	2.0%
International Fixed Income	0.0%	5.0%	5.0%
Cash	36.7%	3.0%	2.0%
Expected Annual Return	1.5%	5.8%	6.6%
Long Term Expected Return	1.5%	5.5%	6.1%
Net Earnings (less inflation)	**-0.5%**	**3.5%**	**4.1%**

* Range denotes the 95% confidence interval. Risk and return data from Windham Portfolio Advisor. Inflation expectation 2%.

Permanent Fund Characteristics

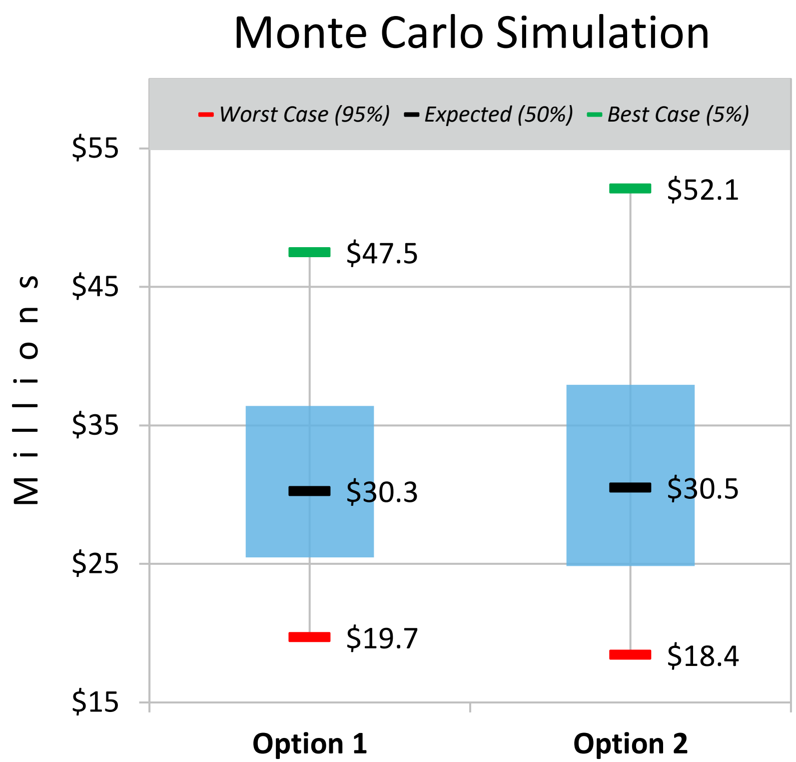


Characteristics	Example Permanent Fund (Option 1)		Example Permanent Fund (Option 2)	
	Expected	Range*	Expected	Range*
Annual Return	5.8%	-11.3% to 22.9%	6.6%	-13.7% to 26.8%
Long-Term Return	5.5%	5.2% to 5.7%	6.1%	5.8% to 6.4%
Net Earnings *Long-Term Return Less 2% Expected Inflation*	3.5%	3.2% to 3.7%	4.1%	3.8% to 4.4%
Average Loss in Extreme Conditions *Within a 1-Year Horizon*	-21.0%	–	-24.3%	–

* Range denotes the 95% confidence interval. Risk and return data from Windham Portfolio Advisor. Graphic is for illustrative purposes only.

Sustainable Distributions 10-Year Horizon

- The simulations depicted on the right were based upon a starting value of $25M and no contributions.
- Annual withdrawals begin starting with the next fiscal year (July 1, 2022).
- Withdrawals are based upon the sustainable rate for each option:
  - Option 1: 3.5%
  - Option 2: 4.0%

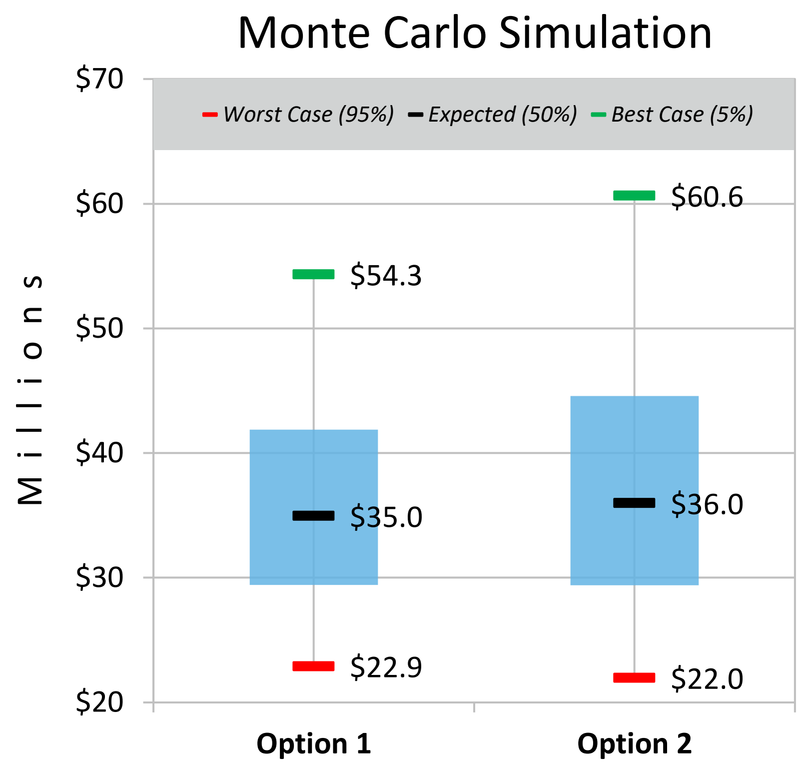


Distributions *($ thousands)*	**2022**	**2023**	**2024**	**2025**	**2026**	**2027**	**2028**	**2029**	**2030**	**2031**
Option 1	894	907	918	928	950	971	991	1,012	1,033	1,054
Option 2	1,024	1,035	1,045	1,054	1,075	1,092	1,109	1,126	1,144	1,160

Risk and return data from Windham Portfolio Advisor.

Sustainable Distributions After 5 Years 10-Year Horizon

- The simulations depicted on the right were based upon a starting value of $25M and no contributions.
- Annual withdrawals begin in year five (July 1, 2026).
- Withdrawals are based upon the sustainable rate for each option:
  - Option 1: 3.5%
  - Option 2: 4.0%

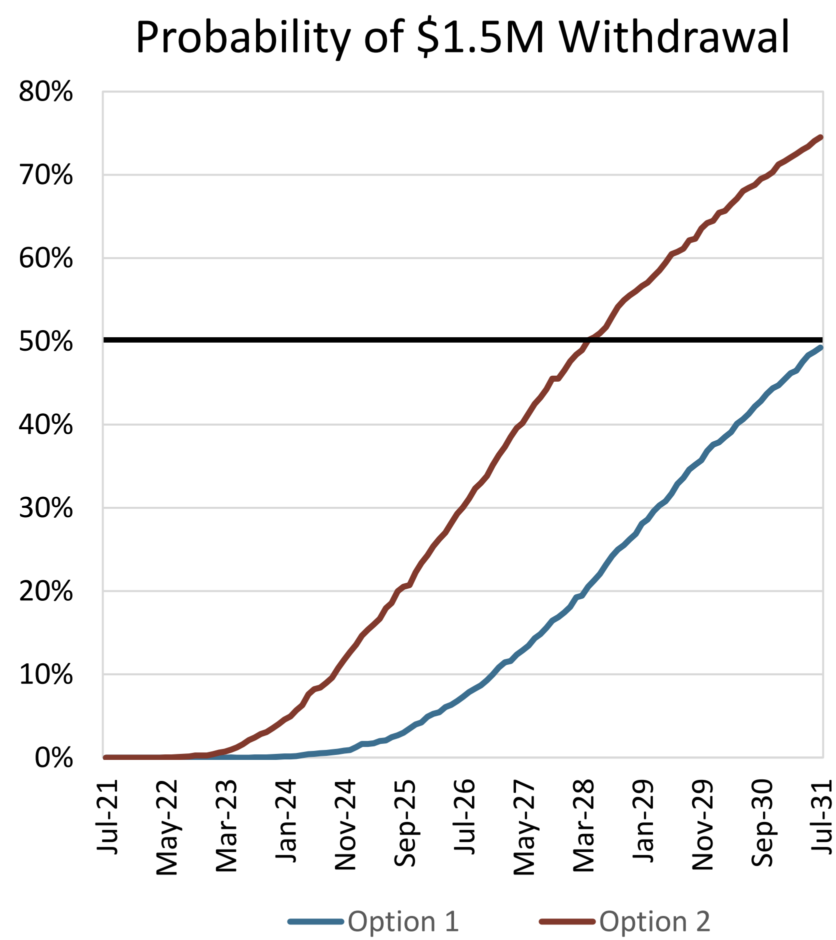


Distributions *($ thousands)*	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031
Option 1	–	–	–	–	1,021	1,072	1,116	1,157	1,189	1,214
Option 2	–	–	–	–	1,188	1,253	1,311	1,361	1,404	1,435

Risk and return data from Windham Portfolio Advisor.

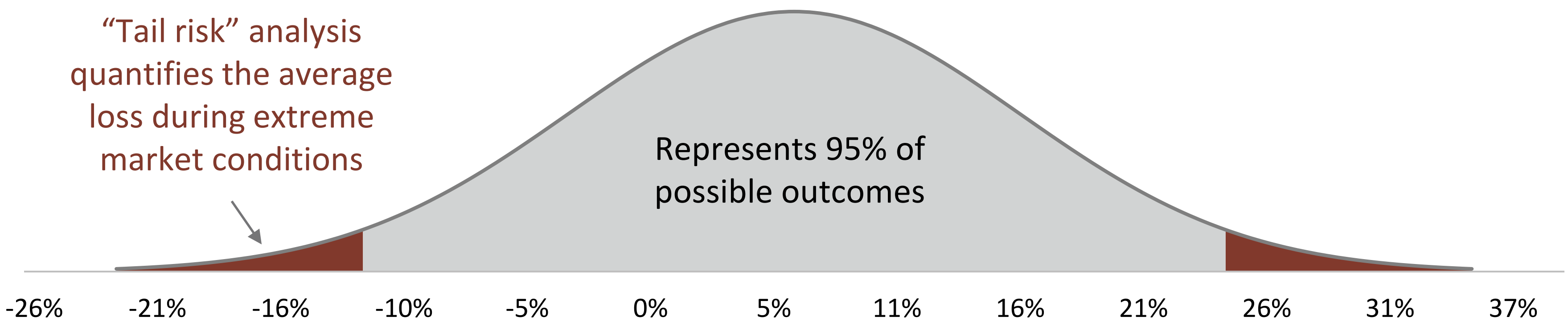
$1.5M Distributions 10-Year Horizon

- The probabilities depicted on the right were based upon a starting value of $25M and no contributions or withdrawals.
- For Option 1, a $1.5M withdrawal at the sustainable rate (3.5%) would require a market value of $42.9M, which is not expected to occur within a 10-year horizon at the 50% confidence level.
- For Option 2, a $1.5M withdrawal at the sustainable rate (4.0%) would be possible with a market value of $37.5M, which is expected to occur for the July 1, 2028 fiscal year.



Risk and return data from Windham Portfolio Advisor.

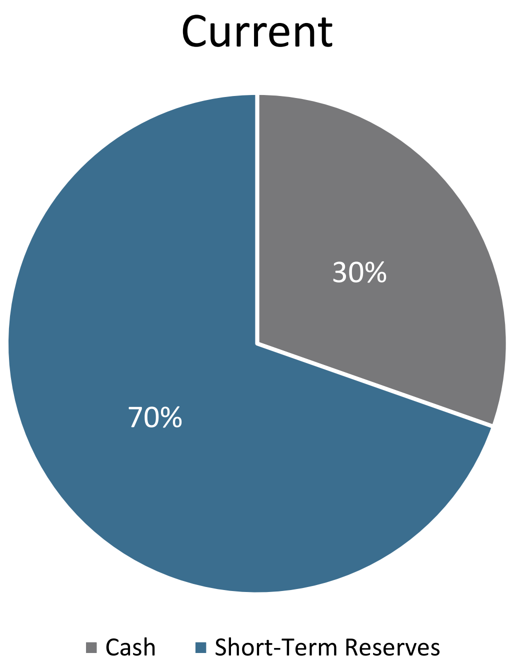
Total Portfolio Characteristics

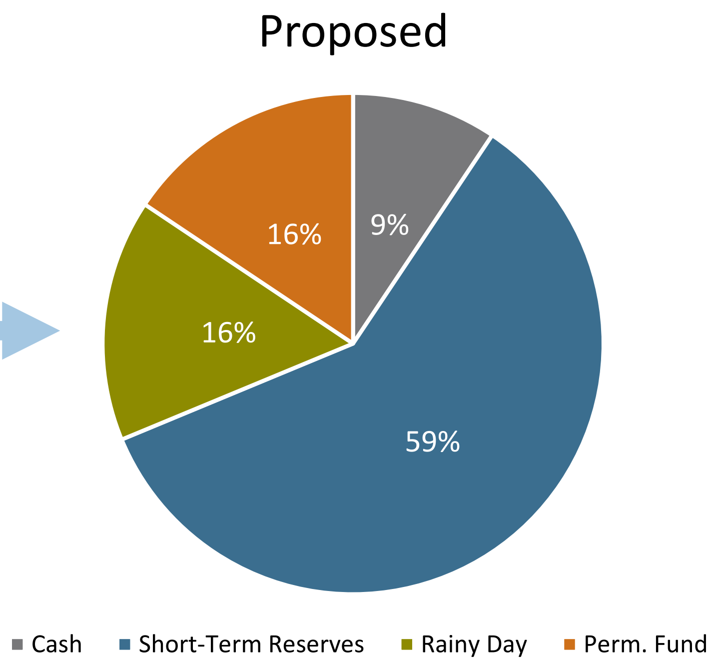


Characteristics	Total Portfolio (Current)		Total Portfolio (Option 1)		Total Portfolio (Option 2)	
	Expected	Range*	Expected	Range*	Expected	Range*
Annual Return	1.5%	-0.4% to 3.4%	2.3%	-0.9% to 5.5%	2.4%	-1.1% to 5.9%
Long-Term Return	1.5%	1.4% to 1.5%	2.3%	2.2% to 2.3%	2.4%	2.3% to 2.4%
Average Loss in Extreme Conditions *Within a 1-Year Horizon*	-2.1%	–	-3.6%	–	-4.0%	
Strategic Asset Allocation	37% Cash / 63% Fixed Income		10% Cash / 81% Fixed Income / 6% Equity / 3% Alternatives		10% Cash / 80% Fixed Income / 7% Equity / 3% Alternatives	

* Range denotes the 95% confidence interval. Risk and return data from Windham Portfolio Advisor.
Graphic is for illustrative purposes only.

Summary





- The proposed strategy optimizes the City's portfolio returns by aligning the investment strategy with the appropriate reserve levels.
- APCM's current 10-year expected long-term return on the City's existing strategy is 1.5%, annualized. The bucketing strategy would increase that to at least 2.3%, **a 0.8% increase or $1.28M for a $160M total portfolio**.
- The new bucketing strategy with the adoption of a Permanent Fund will help the City increase and diversify revenues in order to provide additional budgetary stability.

Next Steps

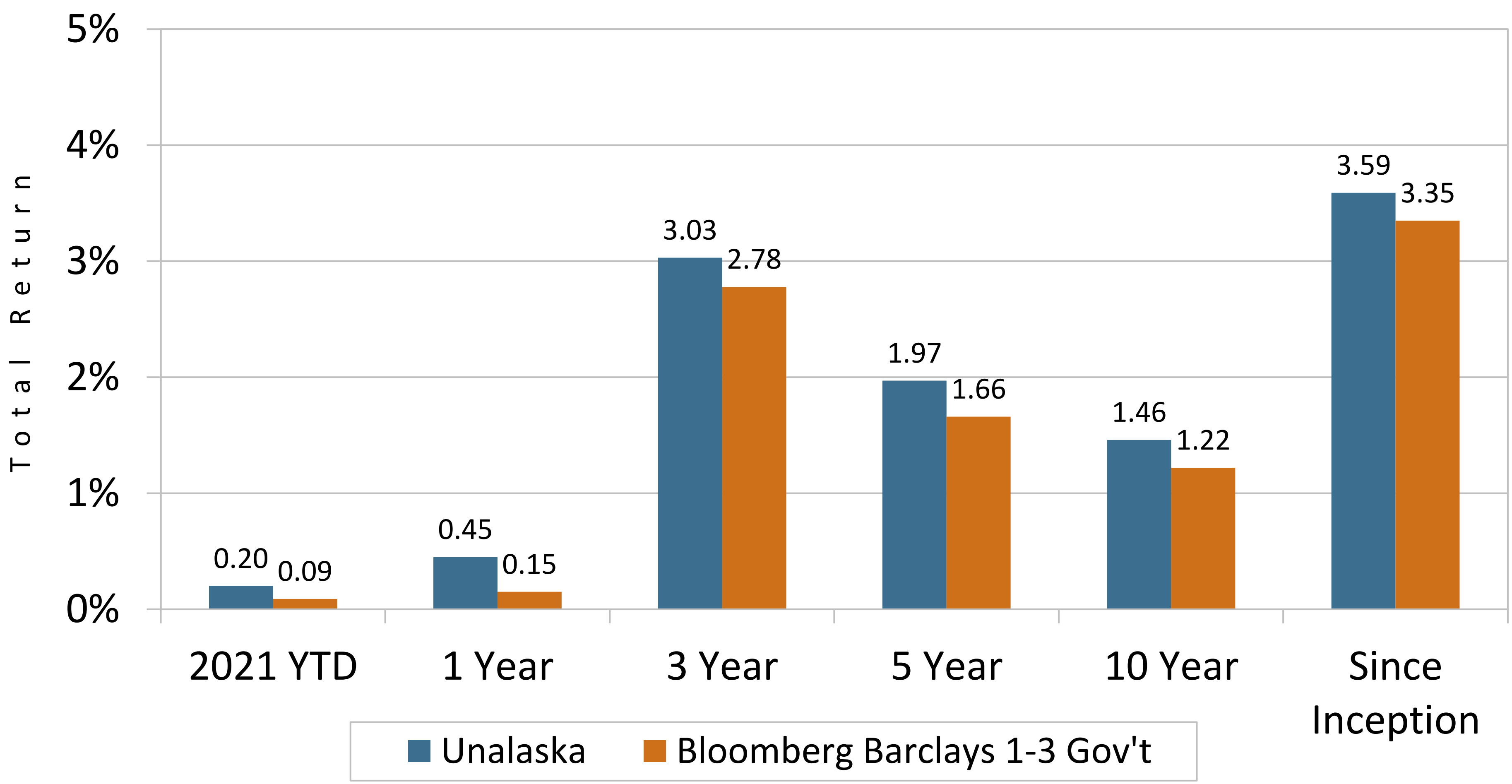
- If the Council chooses to pursue one of the options, APCM will assist the City to prepare for the new strategy, including:
  - Drafting new investment policy statements
  - Opening new accounts as necessary
  - Funds transfers
- Once all of the new accounts, policies, and necessary Code changes are in place, APCM will implement the new strategic plan.

1. **Bucketing Strategy Proposal**
2. **Board Reviews Proposal and Selects Optimal Portfolio**
3. **Develop Necessary Policy Changes for Council Approval**
4. **APCM Implements the Strategic Plan**

Appendix

Account Performance as of July 31, 2021

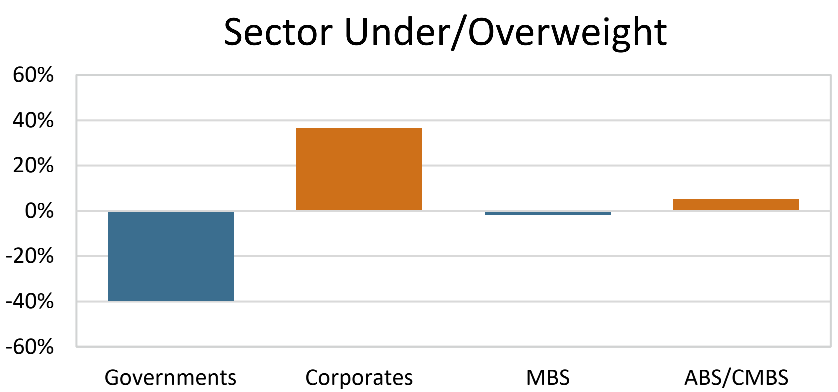
City of Unalaska



Performance is gross of fees and annualized for periods greater than one year. Inception performance begins on June 30, 1995. Benchmark is the Bloomberg Barclays 1-3 Year Government Index.

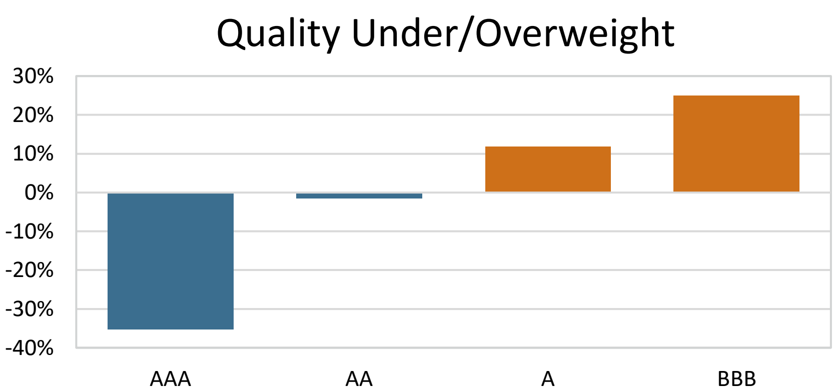
U.S. Fixed Income Positioning as of August 31, 2021

City of Unalaska



Bond Sector Comparison

	Unalaska	Bloomberg Barclays 1-3
Treasuries	55.8%	95.5%
Corporates	36.7%	0.1%
Agencies	2.4%	4.4%
ABS/CMBS	5.1%	0.0%
Total	**100%**	**100%**



Quality Comparison

	Unalaska	Bloomberg Barclays 1-3
AAA	60.8%	96.1%
AA	2.4%	3.9%
A	11.9%	0.0%
BBB	24.9%	0.0%
Total	**100%**	**100%**

Source: Bloomberg

Funds Utilized For Implementation

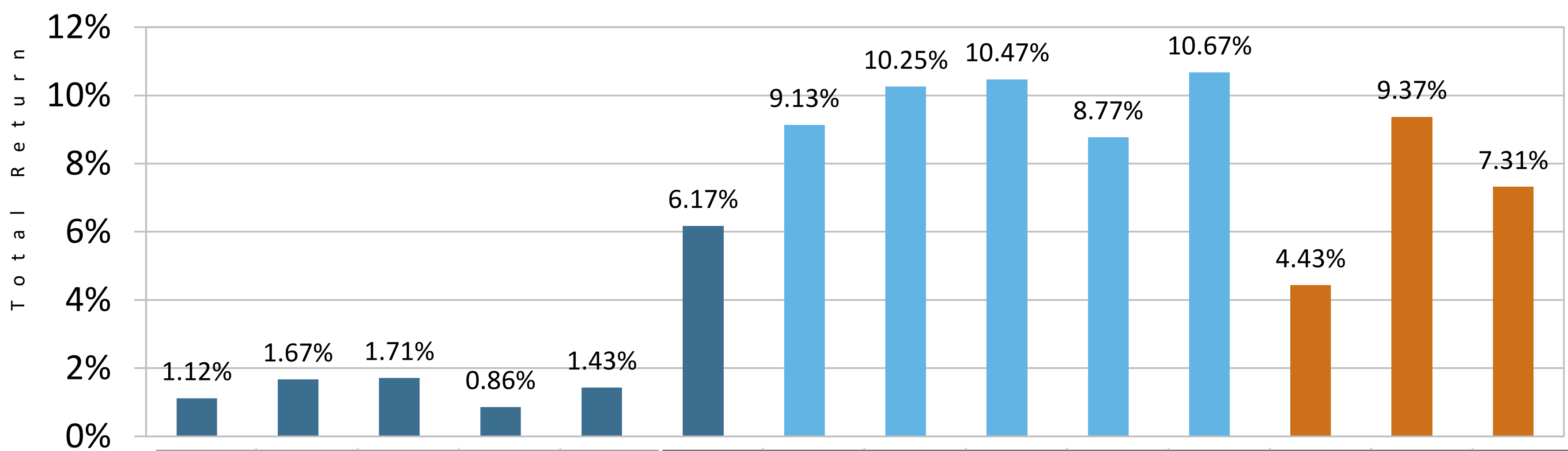
Asset Class	Ticker	Core Holding	Expense Ratio
Large Cap Equity	SPY	SPDR S&P 500 ETF Trust	0.10%
Mid Cap Equity	IJH	iShares Core S&P Mid-Cap ETF	0.05%
Small Cap Equity	IJR	iShares Core S&P Small-Cap ETF	0.06%
International Equity	IEFA	iShares Core MSCI EAFE ETF	0.07%
Emerging Markets Equity	IEMG	iShares Core MSCI Emerging Markets ETF	0.11%
REITs	BBRE	JPMorgan BetaBuilders MSCI U.S. REIT ETF	0.11%
Infrastructure	NFRA	FlexShares STOXX Global Broad Infrastructure Index Fund	0.47%
Commodities	CMDY	iShares Bloomberg Roll Select Commodity Strategy ETF	0.28%
Alternative Beta	BIMBX QAI	BlackRock Systematic Multi-Strategy Fund IQ Hedge Multi-Strategy Tracker ETF	0.98% 0.79%
U.S. Fixed Income	BND	Vanguard Total Bond Market ETF	0.04%
U.S. 1-5 Year Gov/Credit	BSV	Vanguard Short-Term Bond ETF	0.05%
U.S. Corporate High Yield	VWEAX	Vanguard High-Yield Corporate Fund	0.13%
TIPS	VTIP	Vanguard Short-Term Inflation-Protected ETF	0.05%
International Fixed Income	BNDX	Vanguard Total International Bond ETF	0.08%
Cash			

The Case for High Yield Fixed Income

Accept, Prepare, ***Adapt***

High yield bonds are issued by corporations with ratings below BBB– or Baa3 by established credit rating agencies.

In a company's capital structure, debt securities rank ahead of equity securities, so if a company was unable to pay all of their obligations and/or the valuation of the company dramatically declines, the **debt securities are paid back first** and are the first to capture any remaining value in the company before anything is allocated to the equity (preferred and common) holders.



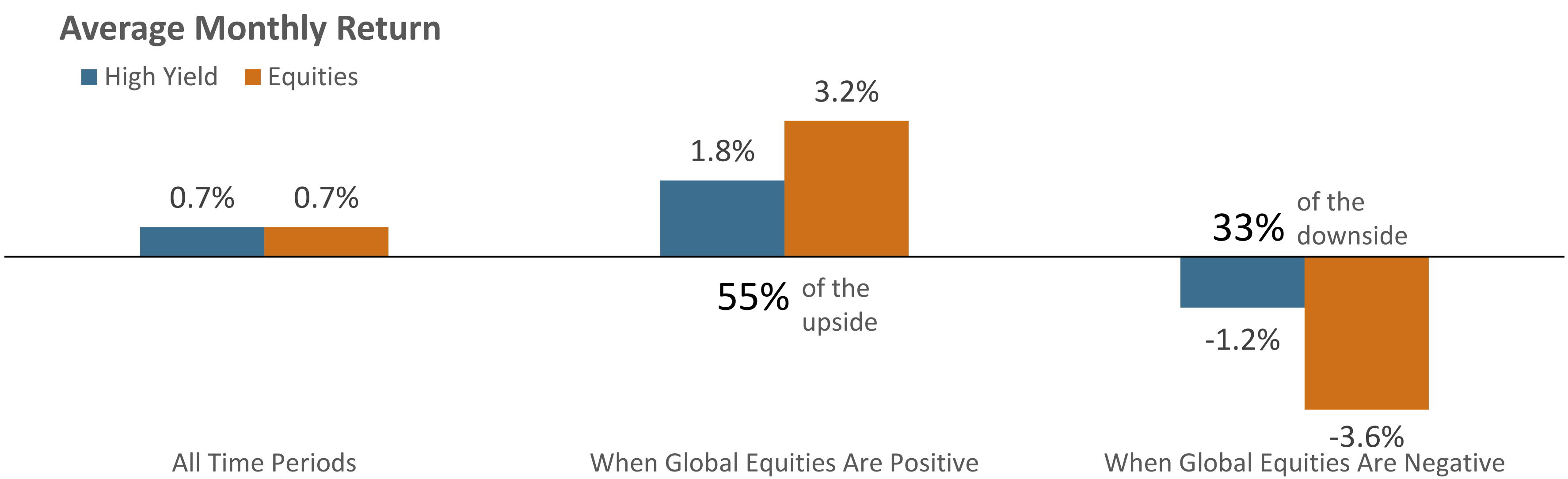
	RISK CONTROL					RISK ASSETS								
	FIXED INCOME						EQUITIES					REAL ASSETS		
	Cash	Muni. Bonds	U.S. Fixed	TIPS	Intl. Fixed	US. HY Bonds	U.S. Large	U.S. Mid Cap	U.S. Small	Dev. Ex-U.S.	Emerging Markets	Comm.	Real Estate	Infra.
Expected Return*	1.12%	1.67%	1.71%	0.86%	1.43%	6.17%	9.13%	10.25%	10.47%	8.77%	10.67%	4.43%	9.37%	7.31%

* CMAs are 10-year projected returns and do not represent actual returns.

The Case for High Yield Fixed Income

Accept, Prepare, ***Adapt***

An allocation to high yield has provided investors with upside participation in positive risk environments and downside protection in negative risk environments.



- Since 1993, high yield has averaged a 0.7% monthly return; this is similar to global equities but with less volatility and less downside risk.
- High yield's asymmetric return profile – 55% of the upside with only 33% of the downside – makes it an attractive addition to a fully diversified multi-asset portfolio.

Source: Northern Trust Global Asset Allocation, Bloomberg. Data from 1/29/1993 to 5/29/2020. Global equities = MSCI ACWI; Global high yield = Bloomberg Barclays Global High Yield Index.

Diversifying Benefits of Alternative Beta

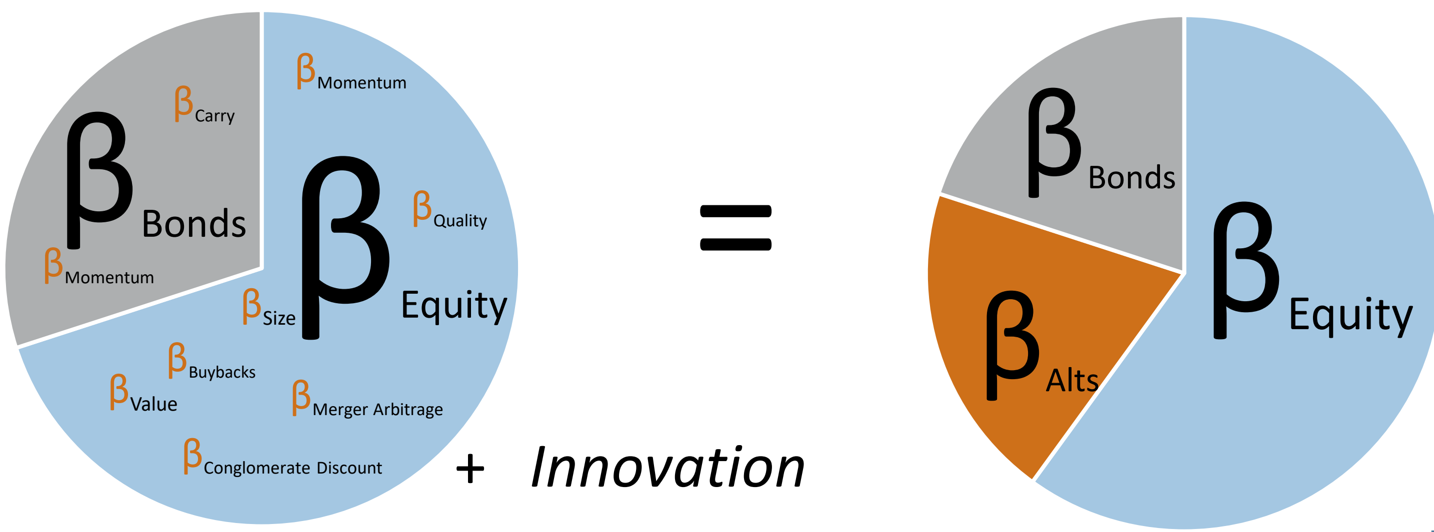
*Accept, **Prepare**, Adapt*

Alternative beta captures sources of return that exist,
but are not emphasized, in traditional stock and bond portfolios.

*The **industry's broader understanding of sources of return** now allow these strategies to be accessed in a quantitative, systematic manner that **does not require a specific manager's subjective judgment.***

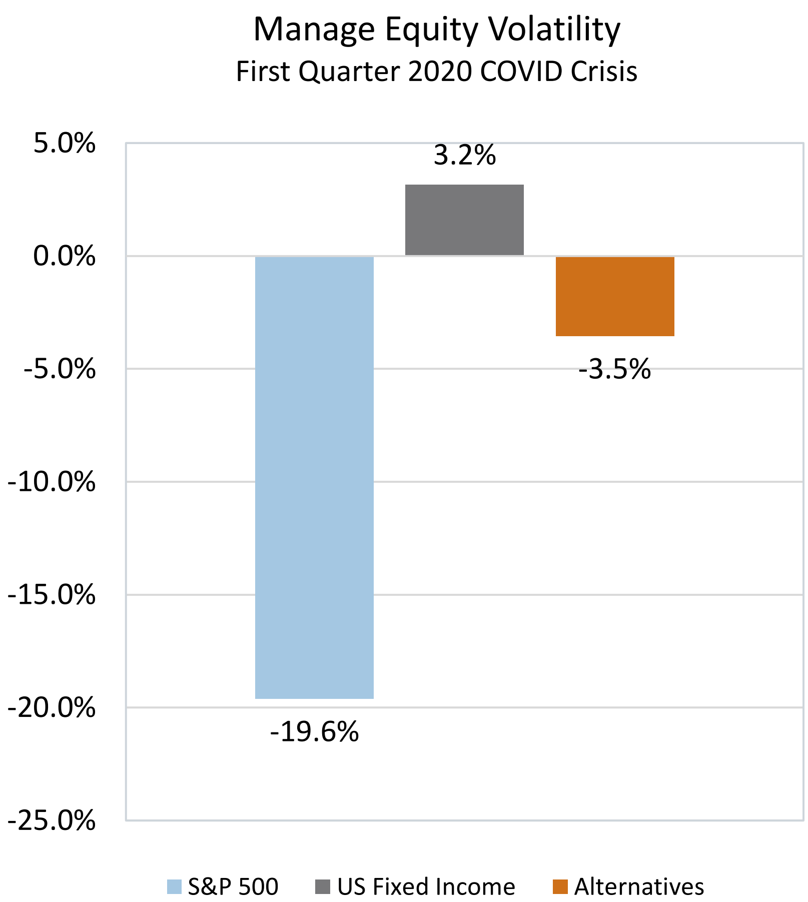
*These **alternative sources of returns can further diversify a stock and bond portfolio,** but all require complex trading strategies.*

*The risks associated with these trading strategies **require proper risk management and controls.***

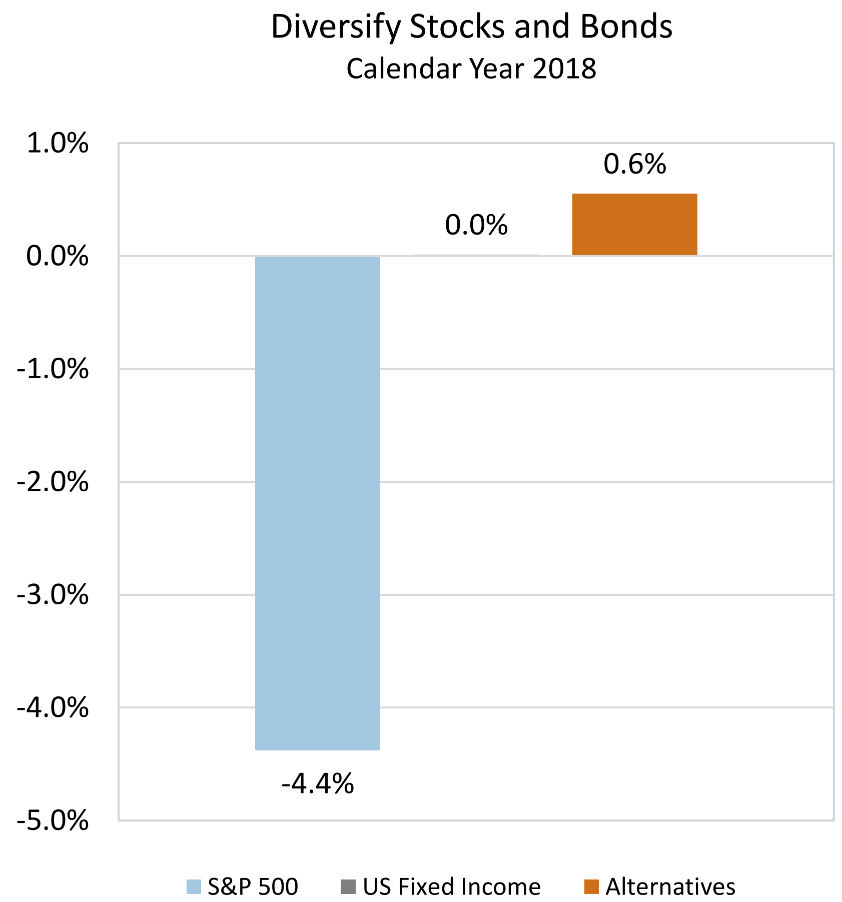


Diversifying Benefits of Alternative Beta

*Accept, **Prepare**, Adapt*



Source: Bloomberg from December 31, 2019 to March 31, 2020.
Alternatives represented by a portfolio of 75% BIMBX 25% QAI.



Source: Bloomberg from December 31, 2017 to December 31, 2018.
Alternatives represented by a portfolio of 75% BIMBX 25% QAI.

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Disclosures

Important Assumptions

IMPORTANT: The projections or other information generated by Alaska Permanent Capital Management Company (APCM) regarding the likelihood of various outcomes are hypothetical in nature, do not reflect actual investment results, and are not guarantees of future results. There can be no assurance that the projected or simulated results will be achieved or sustained. The charts and data only present a range of possible outcomes. Actual results will vary over time, and such results may be better or worse than the simulated scenarios. Clients should be aware that the potential for loss (or gain) may be greater than that demonstrated in the simulations. Please note that the analysis does not take into consideration all asset classes, and other asset classes not considered may have characteristics similar or superior to those being analyzed.

Important Legal Information

These calculations are designed to be informational and educational only, and when used alone, do not constitute investment advice. APCM encourages investors to review their investment strategy periodically as financial circumstances do change.

Model results are provided as a rough approximation of future financial performance. Actual results could produce different outcomes (either better or worse) than those illustrated by the model, since it is not possible to anticipate every possible combination of financial market returns. APCM is not responsible for the consequences of any decisions or actions taken in reliance upon or as a result of the information provided by the results of the model.

Other Influences on Rates of Return

Investment management fees: Returns are presented gross of management fees and include the reinvestment of all income. Actual returns will be reduced by investment advisory fees and other expenses that may be incurred in the management of the account. The collection of fees produces a compounding effect on the total rate of return net of management fees. As an example, the effect of investment management fees on the total value of a client's portfolio assuming (a) quarterly fee assessment, (b) $1,000,000 investment, (c) portfolio return of 8% a year, and (d) 1.00% annual investment advisory fee would be $10,416 in the first year, and cumulative effects of $59,816 over five years and $143,430 over ten years. Actual investment advisory fees incurred by clients may vary.

Taxes: Unless noted otherwise, model results have not been adjusted for any state or federal taxes or penalties.

Inflation: Unless noted otherwise, model results do not adjust any inputs or outcomes for inflation. Inflation is assumed to be constant over the investment horizon.

Limitations Inherent in Model Results

Limitations include but are not restricted to the following:

Model results do not represent actual trading and may not reflect the impact that material economic and market factors might have had on APCM's decision making if the actual client money were being managed.

Extreme market movements may occur more frequently than represented in the model.

Some asset classes have relatively limited histories. While future results for all asset classes in the model may materially differ from those assumed in APCM's calculations, the future results for asset classes with limited histories may diverge to a greater extent than the future results of asset classes with longer track records.

Market crises can cause asset classes to perform similarly over time; reducing the accuracy of the projected portfolio volatility and returns. The model is based on the long-term behavior of the asset classes and therefore is less reliable for short-term periods. This means that the model does not reflect the average periods of "bull" and "bear" markets, which can be longer than those modeled.

The model represent APCM's best view of the next 7-10 years, but is unlikely to reflect actual investment returns worldwide over this period.