

Dan Schwartz
State Treasurer

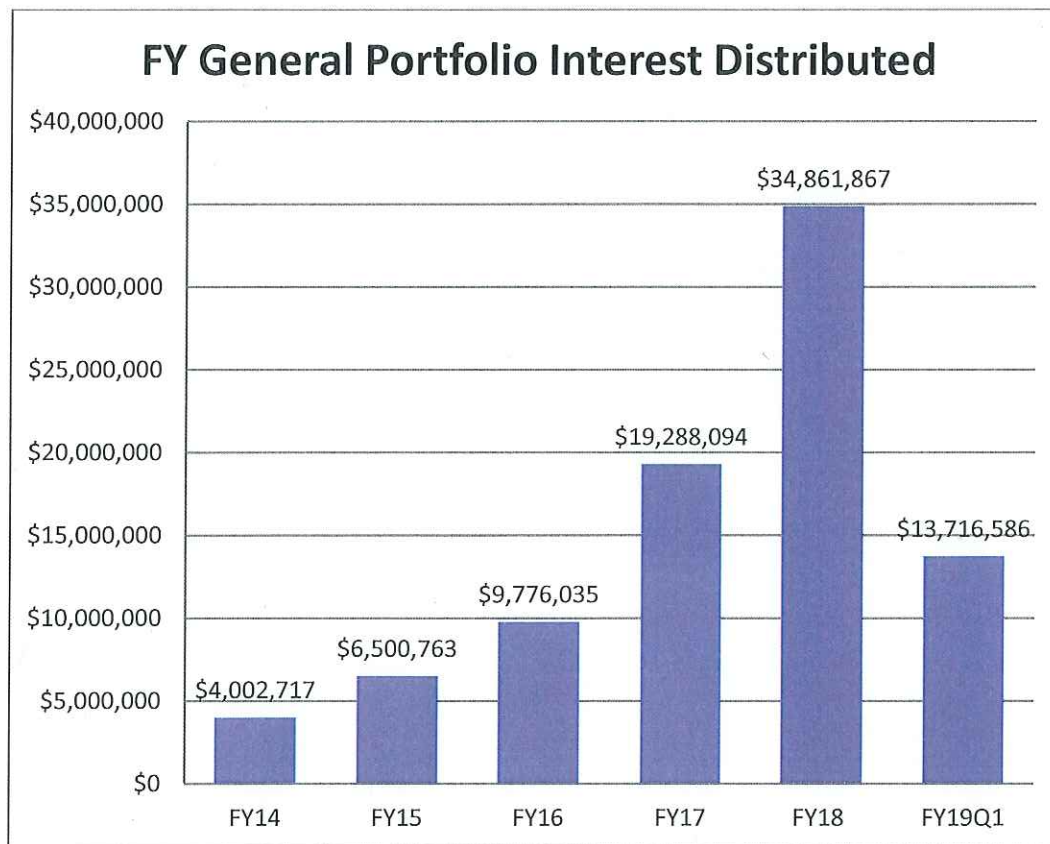


STATE OF NEVADA
OFFICE OF THE STATE TREASURER

TO: Board of Finance (BoF) Members
FROM: Tara Hagan, Chief Deputy Treasurer
SUBJECT: 11_13_18 BoF Agenda Item #3– State Treasurer Investment Report
DATE: November 7, 2018

Agenda Item #3

Discussion and possible action (a) regarding the State Treasurer's quarterly investment report for the quarter ending September 30, 2018 and (b) to approve or disapprove the Treasurer's investment policies for the General Portfolio and the Local Government Investment Pool (LGIP).



Investment Performance as of September 30, 2018

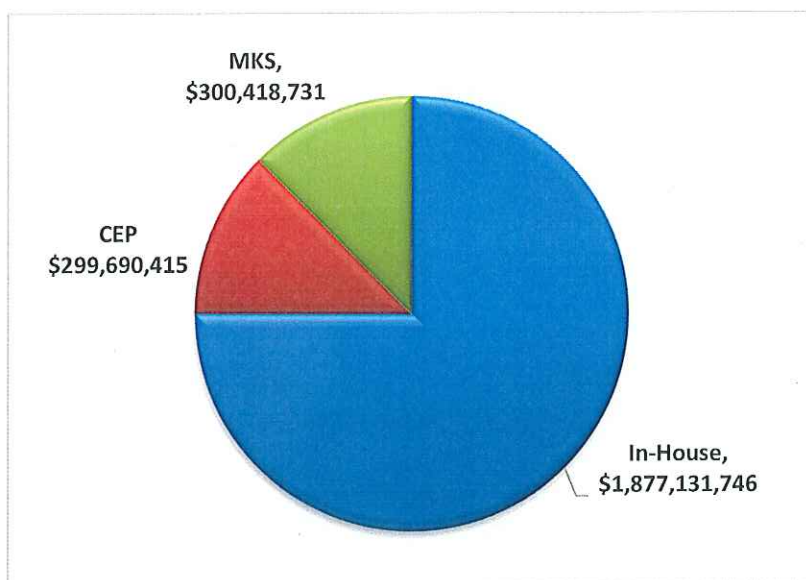
LGIP

As of September 30, 2018, the total assets under management (AUM) were \$1,081,410,833. Currently, FTN Financial manages the portfolio and the yield to maturity as of September 30, 2018 for LGIP assets was 2.25% which is 1 basis point in excess of the benchmark yield of 2.24%.

The Investment Policy Statement of the Local Government Investment Pool requires Corporate Note securities of the LGIP maintain two long term ratings of "A" or better from a nationally recognized rating agency at the time of purchase. Additionally, policy directs the Treasurer's Office to notify the Board of Finance when a security falls out of compliance and has either matured or been sold. The LGIP held a Ralph Lauren Corporation fixed income security with a par value of approximately \$3.8 million that matured September 26, 2018. The security was in compliance at the time of purchase; however, in July 2017, Ralph Lauren Corporation was downgraded by Standard & Poor's giving the security a long-term rating of A-, causing the security to fall out of compliance. Moody's maintained an A2 rating for the life of the security. Both the external manager and Treasurer's Office staff monitored the security and company closely through the maturity. The security matured on 9/28/18 without any loss to the LGIP.

General Portfolio

As of September 30, 2018, the AUM for the General Portfolio was \$2.48 billion (market value) with 75% managed internally and 25% managed by outside managers.

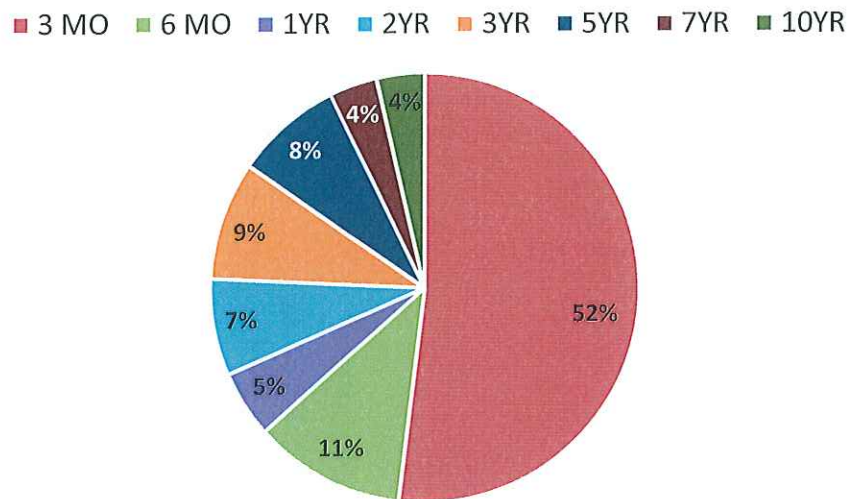


The overall yield to maturity (YTM) as of September 30, 2018 for the General Portfolio was 2.41%. Below is the YTM breakdown by portfolio:

- Internally managed portfolio was 2.25%.
- Chicago Equity Partners (CEP) portfolio was 2.90%.
- MacKay Shields (MKS) portfolio was 2.93%.

Although the outside managers' charts on page 4 indicate declines in the overall market values for the year-to-date and one-year numbers, these portfolios have not incurred any material realized losses to date, as securities have not been sold. The valuations are the result of the current rising interest rate environment which negatively affects the market value of the longer-maturity securities previously purchased by the outside managers. As noted above, if the outside managers held their respective investments to maturity, the yield would be 2.90% for CEP and 2.93% for MKS.

Below is a graphical representation of the asset weighted maturities in the General Portfolio as of September 30, 2018.





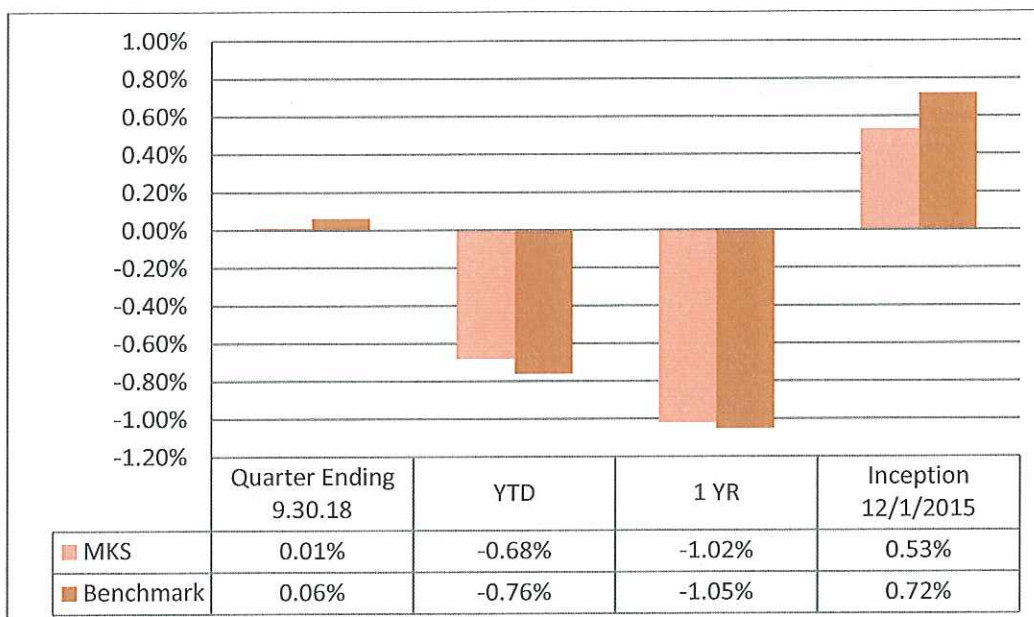
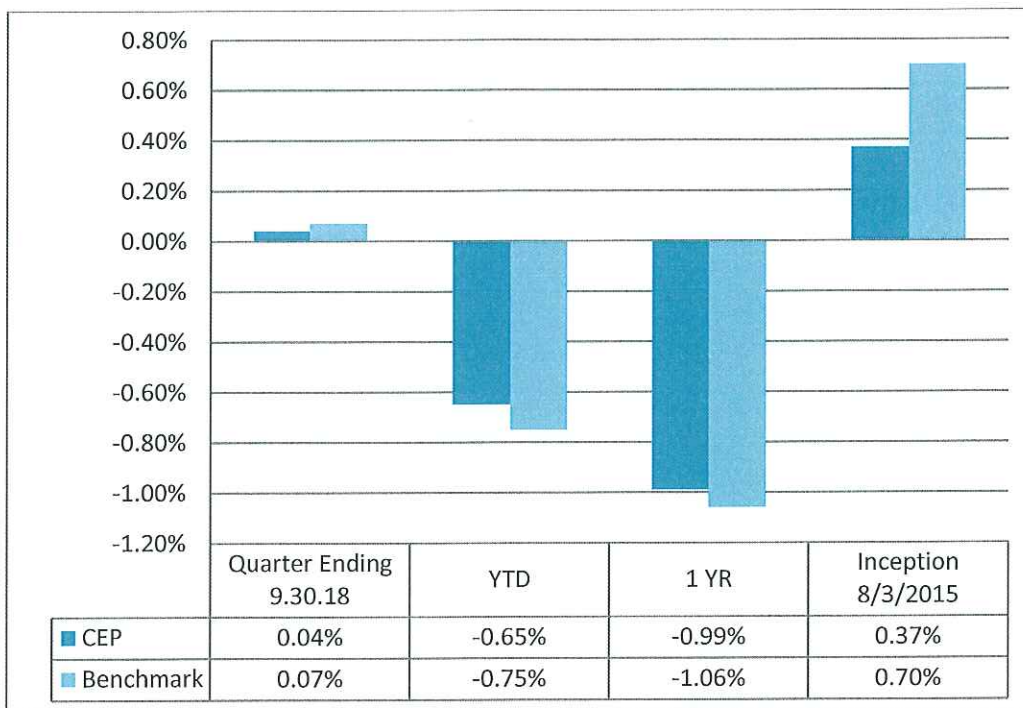
*Custom benchmark yield matches the asset-weighted maturities of the General Portfolio for each quarter to the appropriate Treasury yield.

General Portfolio Outside Managers' Performance

Chicago Equity Partners (CEP) began managing \$200 million in General Portfolio assets on August 3, 2015 with an additional \$100 million in 2016 for a total of \$300 million.

The calendar year to date time weighted performance net of fees is -0.65%. As of September 30, 2018, CEP has distributed \$11.91 million in net interest since inception. The hard dollar fees paid since inception to CEP as of September 30, 2018 were \$980,834 (31.7 basis points).

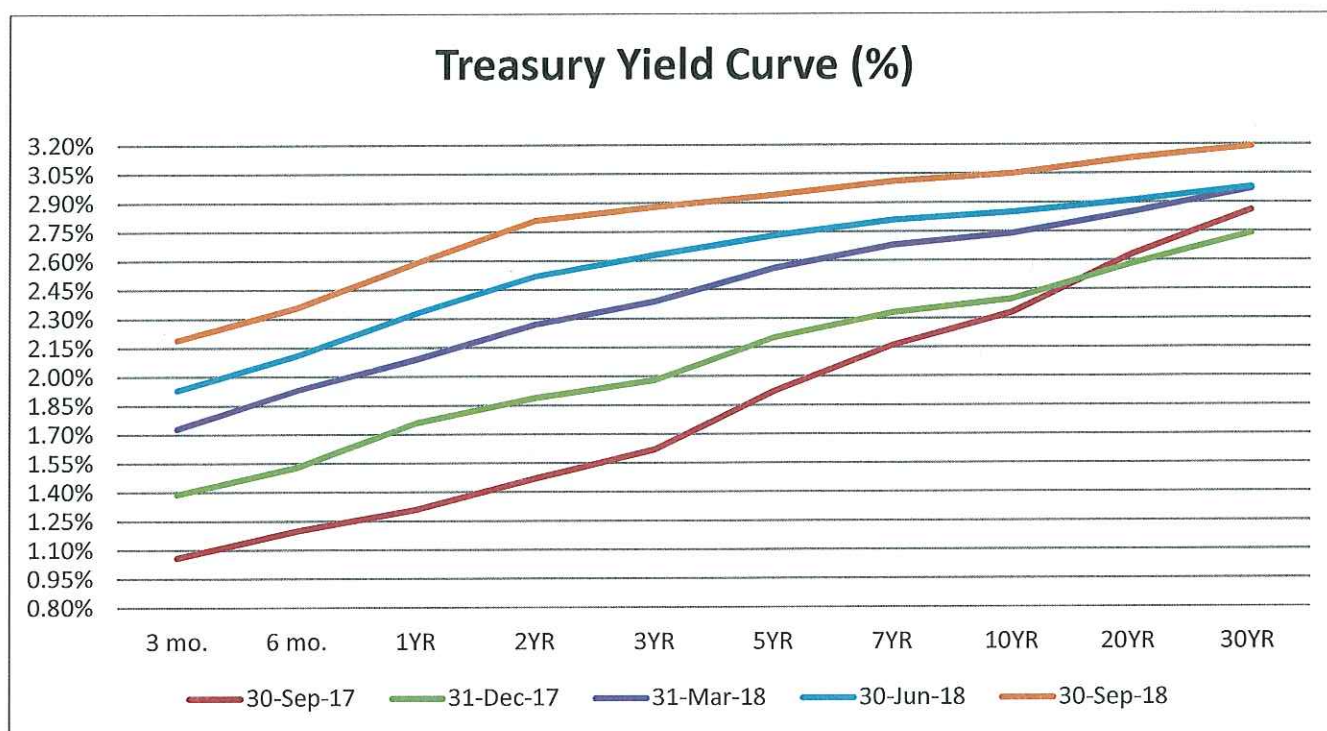
MacKay Shields (MKS) began managing \$200 million in General Portfolio assets on December 1, 2015 with an additional \$100 million for a total of \$300 million. The calendar year to date time weighted performance net of fees is -0.68%. As of September 30, 2018, MKS has distributed \$11.10 million in net interest since inception. The hard dollar fees paid since inception to MKS as of September 30, 2018 were \$1,000,041 (32.3 basis points).



Please note the applicable Nevada statutory restrictions regarding corporate notes, local authorities, foreign sovereigns, supranational and foreign agency can negatively impact each manager's portfolio performance versus the index.

Fixed Income Market Highlights as of September 30, 2018

- As expected, the Federal Reserve (Fed) raised the fed funds rate target rate by 25 basis points or a quarter of a percent in September to 2.00- 2.25%. The Fed maintained its hawkish stance by signaling for one more rate hike in December 2018 and potentially three more in 2019.
- Third calendar quarter Gross Domestic Product (GDP) increased at an annual rate of 3.5 percent, according to the "advance" estimate released by the Bureau of Economic Analysis. GDP rose to 4.1% in the second calendar quarter making it the strongest quarter since 2014.
- The US Treasury yield curve flattened further during the third calendar quarter as the difference between the 2-year and 10-year rates narrowed to 24 basis points versus 33 basis points in the second quarter.



NRS 355.170 prohibits the General Portfolio from investing in Treasuries beyond 10 years. Chart is for illustrative purposes only.

Recommendation:

I respectfully request consideration and approval of the quarterly investment reports and the Treasurer's investment policies for the General Portfolio and the LGIP.



State Treasurer
www.NevadaTreasurer.gov

INVESTMENTS

GENERAL PORTFOLIO

FISCAL YEAR 2019
Period Ending
September 30, 2018

Overview

Investment of the State of Nevada General Fund Portfolio is a function performed by the State Treasurer, who, by the provisions of NRS 355, has adopted policies for the prudent and conservative investment of these funds. The General Portfolio encompasses governmental, proprietary, enterprise and fiduciary funds of the State. Investment objectives include safety of principal, portfolio liquidity and market return.

Investment Guidelines

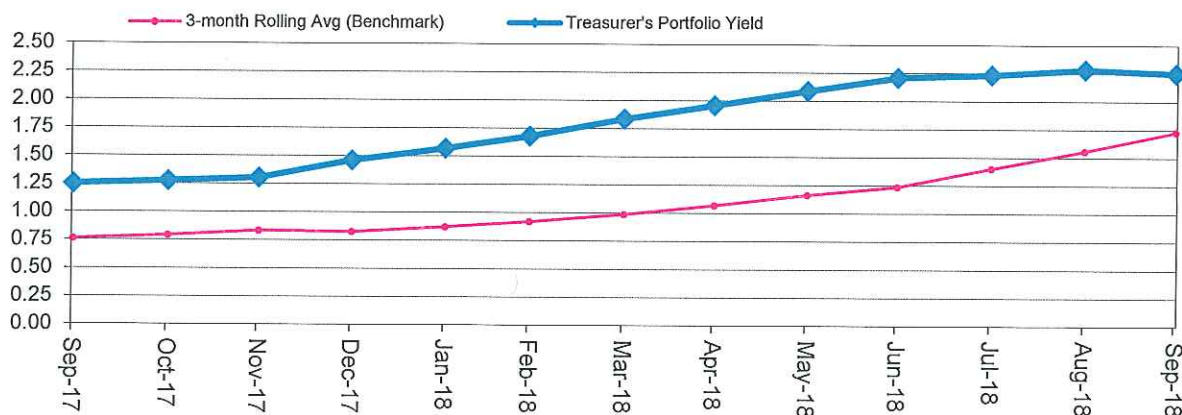
The permissible investments of the General Portfolio include United States Treasury and Agency securities, repurchase agreements, high quality corporate notes and commercial paper, negotiable certificates of deposit, municipal bonds and banker's acceptances. These securities are diversified to prevent over-concentration in a specific maturity, a specific issuer, or a specific class of securities. The targeted duration of the portfolio is one and a half years, with no security extending longer than ten years.

The State Treasurer maintains a conservative, moderately active investment strategy. Cash flow forecasts are prepared to identify operating cash requirements that can be reasonably anticipated. In order to maintain sufficient liquidity, a portion of the portfolio is structured so that securities mature concurrently with cash needs in the short and medium term. Monies deemed to have a longer investment horizon, are invested to take advantage of longer term market opportunities.

In-House Performance

As of September 30, 2018, the yield on the portion of the General Portfolio managed in-house was 2.252%. A three month rolling average of this benchmark for this period was 1.73% with the average days to maturity at 218 days. The average days to maturity for the in-house managed portfolio was .54 years or 196 days.

In-House Performance vs. Benchmark

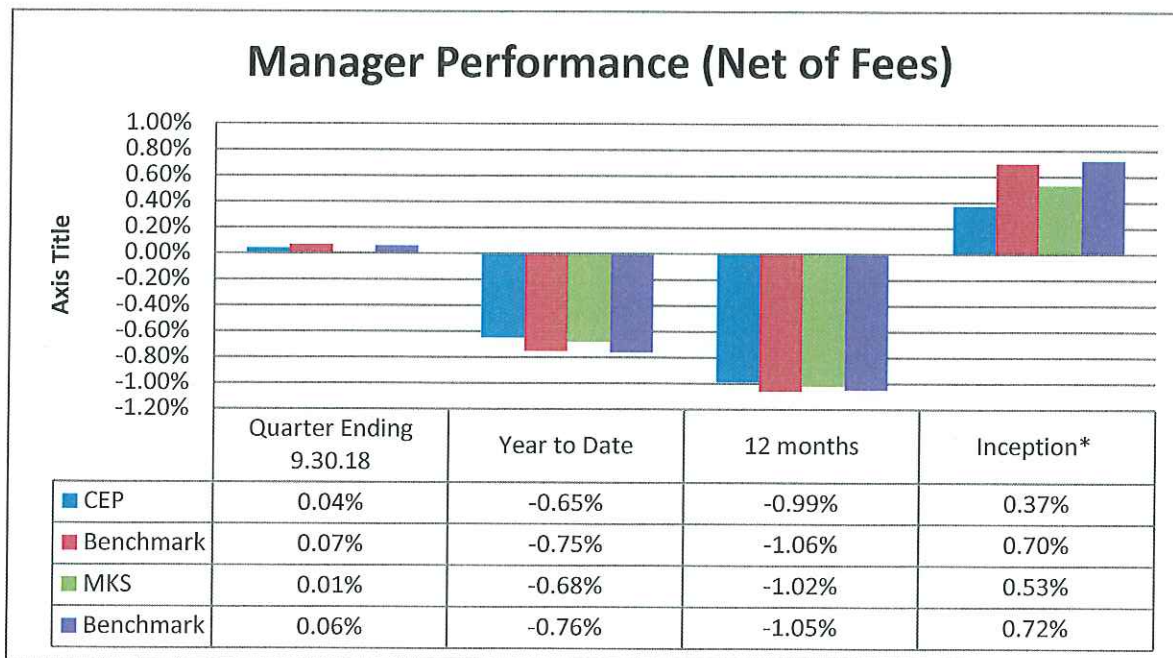


* Benchmark is 3-month rolling weighted average of 80% 3-month Treasuries and 20% 2-year Treasuries

Outside Manager Performance

The annualized performance since inception for period ending September 30, 2018 for manager Chicago Equity Partners (CEP) is 0.37% and for Mackay Shields (MKS) is 0.53%*. Both of these returns are based on time-weighted rate of return which is defined as the compounded growth rate of \$1 over the period being measured. These funds have been assigned the Bloomberg Barclays Intermediate A or better Government Credit benchmark. The Nevada statutory requirements prevent managers from investing in certain securities (supranationals and foreign sovereigns), fewer corporate notes and governmental securities longer than 10 years which is the cause of the difference in manager performance versus the benchmark. *CEP inception date is August 2015 and MKS is December 2015.

Outside Managers' Performance vs. Benchmark

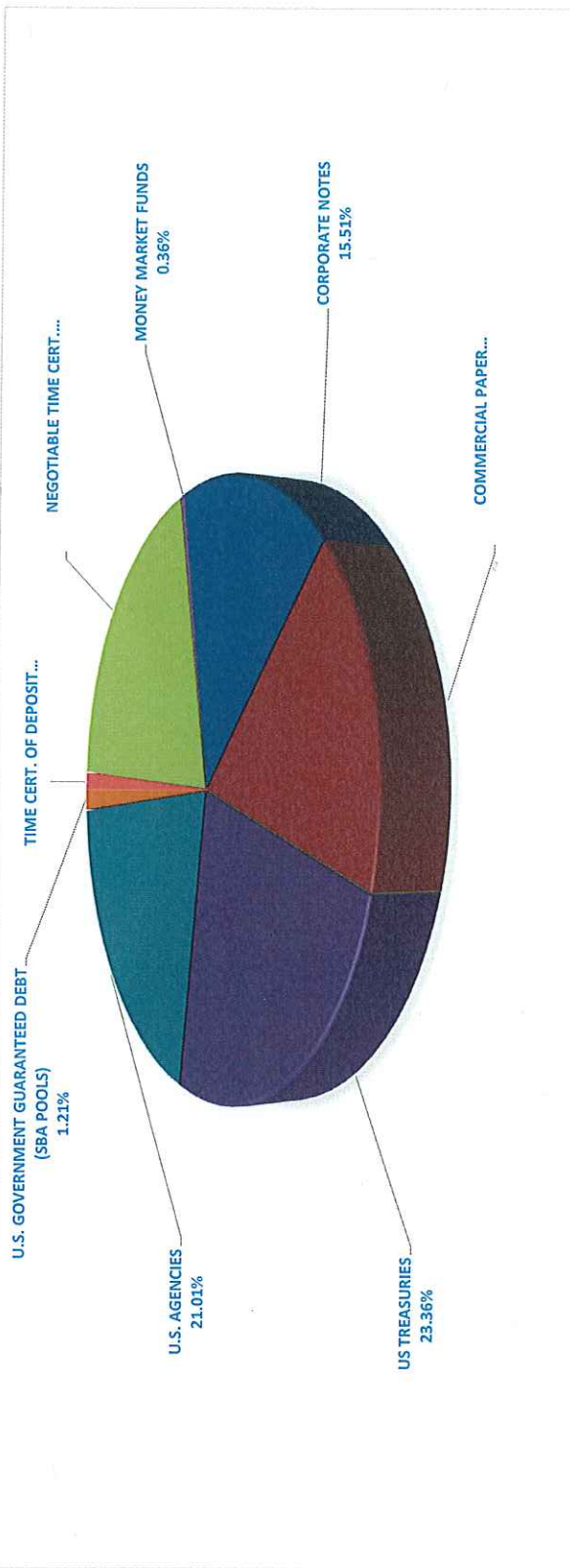


*Inception date for CEP is 8.3.15 and 12.1.15 for MKS

GENERAL PORTFOLIO

Amortized Book Value and Purchased Interest

	September 30, 2018				June 30, 2018			
	Amortized Book Value				Amortized Book Value			
	Treasurer In-House	Chicago Equity Partners	Mackay Shields		Treasurer In-House	Chicago Equity Partners	Mackay Shields	
WASHINGTON FEDERAL CHECKING ACCT.	\$ -	\$ -	\$ -		\$ 1,144	\$ -	\$ -	
TIME CERTIFICATES OF DEPOSIT	25,000,000	-	-		25,000,000	-	-	
NEGOTIABLE CERTIFICATES OF DEPOSIT	519,001,166	-	-		435,001,394	-	-	
MONEY MARKET FUNDS	5,371,232	3,468,464	82,632		3,242,379	17,186,389	54,031	
ASSET-BACKED SECURITIES	-	-	-		-	-	-	
MORTGAGE-BACKED SECURITIES	-	-	-		-	-	-	
CORPORATE NOTES	250,886,185	50,708,518	86,436,332		212,250,464	35,110,766	92,674,343	
COMMERCIAL PAPER	420,993,501	-	-		487,825,269	-	-	
MUNICIPAL BONDS	-	-	-		-	-	-	
U.S. TREASURIES	114,784,264	251,036,555	218,596,933		49,789,360	251,251,228	211,295,463	
U.S. AGENCIES	515,009,034	5,598,901	4,999,026		522,415,727	6,084,865	4,991,105	
U.S. GOVERNMENT GUARANTEED DEBT	30,277,489	-	-		35,456,489	-	-	
REPURCHASE AGREEMENTS	-	-	-		93,000,000	-	-	
TOTAL	\$ 1,881,322,870	\$ 310,812,438	\$ 310,114,924		\$ 1,863,982,227	\$ 309,633,248	\$ 309,014,942	
GRAND TOTAL	\$	\$	\$ 2,502,250,232		\$	\$	\$ 2,482,630,417	



YEAR-TO-YEAR BOOK VALUE AND PURCHASED INTEREST COMPARISON

	September 30, 2018	September 30, 2017
TOTAL PORTFOLIO	\$2,502,250,232	\$2,148,716,689

State of Nevada
Office of the State Treasurer
Schedule of General Fund Interest Revenue

	Quarter Ended 09/30/2018	Quarter Ended 12/31/2018	Quarter Ended 03/31/2019	Quarter Ended 06/30/2019	FY 2019 Totals
<u>Average Daily Balances of Funds</u>					
General Fund	806,653,832				806,653,832
All Funds	2,659,186,033				2,659,186,033
<u>Annualized Interest Rate</u>					
Cash Basis (see Note 1)	2.0386%				2.0386%
Accrual Basis	1.9953%				1.9953%
<u>Interest Distribution for General Fund (Cash Basis)</u>					
General Fund Interest Collected	4,160,873				4,160,873
General Fund Interest Revenue - Distributed	4,160,873				4,160,873
Undistributed General Fund Interest Revenue	-				-
<u>Interest Distribution for All Funds (Cash Basis)</u>					
All Funds Interest Collected	13,716,586				13,716,586
All Funds Interest Revenue - Distributed	13,716,586				13,716,586

Note 1 Interest is distributed to statutorily approved funds and budget accounts based on the cash basis of accounting. Under the cash basis of accounting, earnings are distributed in the quarter received but not necessarily in the quarter they were earned. Therefore, some of the receipts included in the Actual General Fund interest collected line were actually earned in the prior period and some of the earnings included in the General Fund interest revenue - accrual basis line will not be collected until a subsequent period.



Overview

The State of Nevada Local Government Investment Pool (LGIP) was established as an alternative investment program to be utilized by local governments for their public funds. This program's operation is the responsibility of the State Treasurer who, by the provisions of state statute, has adopted guidelines for the prudent investment of these pooled funds. Any local government, as defined by NRS 354.474, may deposit its public monies into this fund for purposes of investment. As of September 30, 2018, there were 88 members of the LGIP, which includes cities, counties, school districts, and various special districts. The LGIP's foremost investment objectives include safety of principal, portfolio liquidity, and market return, which are consistent with a conservative, short duration portfolio.

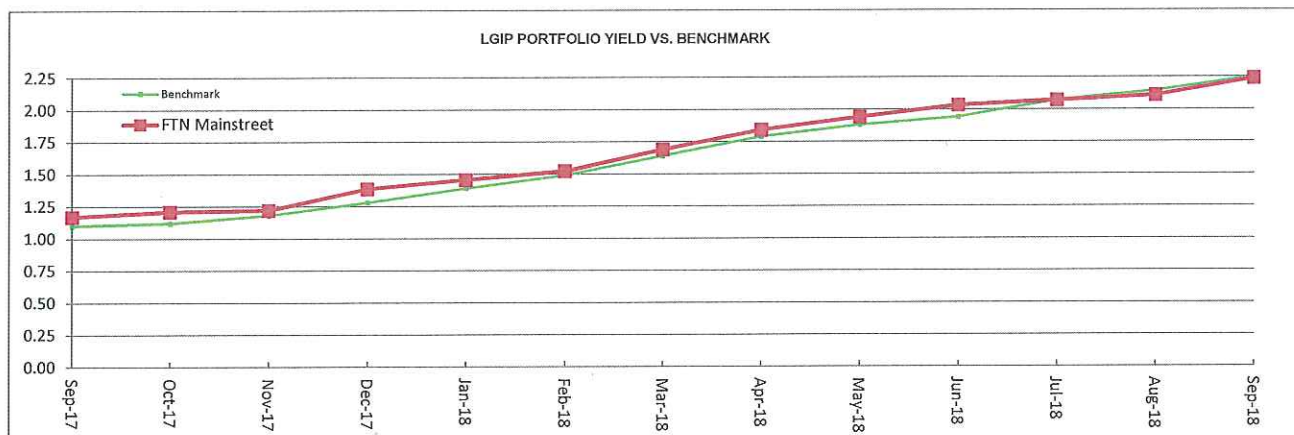
Investment Guidelines

The permissible investments of the LGIP include United States Treasury and Agency securities, repurchase agreements, high quality commercial paper, negotiable certificates of deposit, municipal bonds and banker's acceptances. These securities are diversified to prevent over-concentration in a specific maturity, a specific issuer, or a specific class of securities. The average maturity of the portfolio must not exceed 150 days, and no single security may be longer than two years.

The State Treasurer maintains a conservative investment strategy, which incorporates the matching of maturing securities to the cash needs of the participants. Approximately 10% of the fund matures on a daily basis, ensuring sufficient liquidity to meet both anticipated and unanticipated withdrawals. Additionally, at approximately 60% of the fund matures within 90 days, compared to the policy requirement of 50%. This requirement minimizes the risk that the market value of portfolio holdings will fall significantly due to adverse changes in general interest rates.

Performance

FTN Financial began managing the LGIP portfolio in July 2015. As of September 30, 2018, the LGIP's portfolio yield was 2.25%, and the blended benchmark was 2.24%. The average days to maturity of the LGIP portfolio was 128 days.

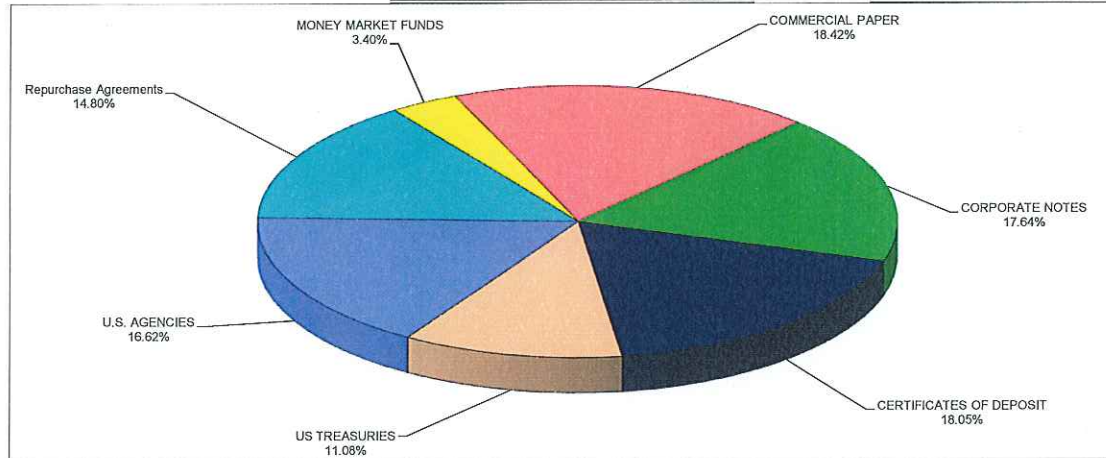


* Benchmark is 3-month rolling weighted average of 20% Dealer Commercial Paper 90-Day Index, 60% Agency Discount Note 6-Month Index, and 20% Morgan Stanley Institutional Liquidity Government Portfolio Fund.

Administration

The State Treasurer has adopted an Investment Policy relating specifically to the LGIP. The State Board of Finance shall review and approve or disapprove the policies established by the State Treasurer for investment of money of the LGIP at least every four months. The State Treasurer hereby confirms all LGIP investments are in compliance with the Terror-Free Investment Policy and the Divestiture Policy. The State Treasurer may contract with an independent auditor to review LGIP transactions for accuracy and fairness in reporting.

	<u>September 30, 2018</u>		<u>June 30, 2018</u>	
	<u>Amortized Book</u>	<u>Purchased Interest</u>	<u>Amortized Book</u>	<u>Purchased Interest</u>
MONEY MARKET FUNDS	\$ 36,797,560	\$ -	\$ 88,943,309	\$ -
COMMERCIAL PAPER	199,150,364	-	169,552,624	-
CORPORATE NOTES	190,720,086	70,574	202,465,305	351,680
CERTIFICATES OF DEPOSIT	194,992,959	148,157	204,967,254	-
MUNICIPAL BONDS	-	-	-	-
U.S. TREASURIES				
NOTES	69,829,605	60,122	139,786,865	-
BILLS	49,914,394	-	79,534,178	-
U.S. AGENCIES	179,716,551	10,461	134,940,278	1,771
ASSET-BACKED SECURITIES	-	-	-	-
REPURCHASE AGREEMENTS	160,000,000	-	100,000,000	-
TOTAL	\$ 1,081,121,519	\$ 289,315	\$ 1,120,189,813	\$ 353,450
GRAND TOTAL	\$ 1,081,410,833		\$ 1,120,543,263	



YEAR-TO-YEAR BOOK VALUE AND PURCHASED INTEREST COMPARISON

	<u>September 30, 2018</u>	<u>September 30, 2017</u>
TOTAL PORTFOLIO	\$1,081,410,833	\$998,447,501