

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: 6_12_18 BoF Agenda Item #9– State Treasurer Investment Report

DATE: June 4, 2018

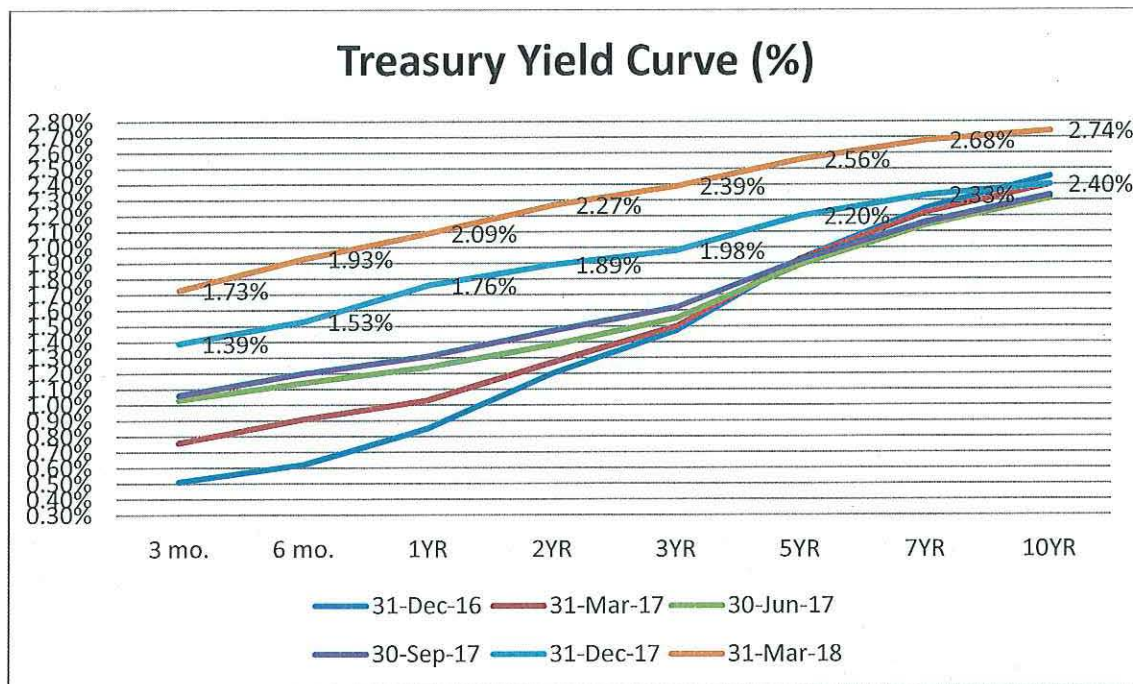
Agenda Item #9

Discussion and possible action (a) regarding the State Treasurer's quarterly investment report for the quarter ending March 31, 2018 and (b) to approve or disapprove the Treasurer's investment policies for the General Portfolio and the Local Government Investment Pool (LGIP).

Fixed Income Markets

During the first calendar year, the Federal Reserve (Fed) increased the Federal Funds rate 25 basis points, bringing the rate up to 1.50% - 1.75%, the fifth increase since December 2016. The core PCE (Personal Consumption Expenditures), the Fed's preferred measure of inflation, remained below its 2% target. US employment growth remained solid, creating an average of 200,000 jobs a month in the first quarter.

The US Treasury Yield curve continued to flatten (see chart on top of page 2) during the quarter, with 1 – 2 year notes performing better than the longer 30-year. US corporate spreads widened 16 basis points over comparable duration Treasuries despite improving company fundamentals. The market fully expects an interest rate increase of 25 basis points to be announced at the next Fed meeting on June 12-13 which would bring the rate up to 1.75%- 2.00%.

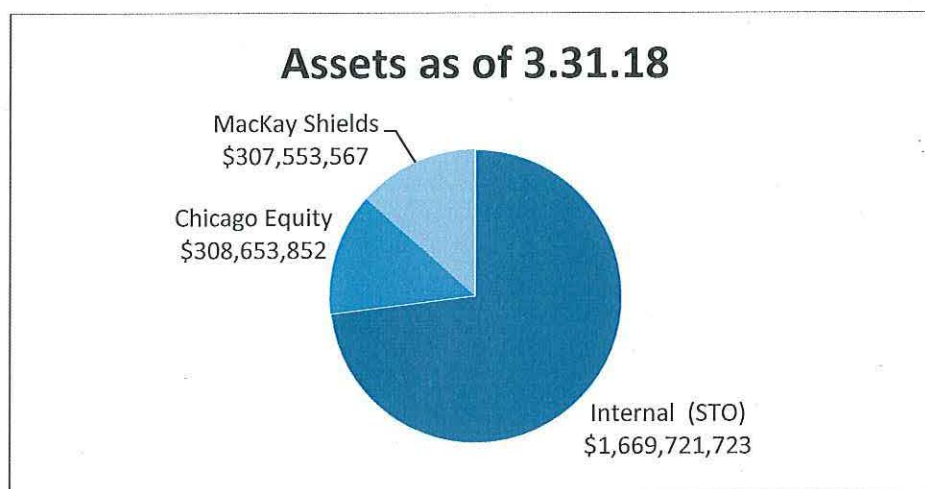


LGIP

As of March 31, 2018, the total assets under management (AUM) were \$1,157,653,007. Currently, FTN Financial manages the portfolio and the yield to maturity as of March 31, 2018 for LGIP assets was 1.69% which is 5 basis points in excess of the benchmark yield of 1.64%.

General Portfolio

As of March 31, 2018, the total AUM for the General Portfolio was \$2.29 billion with 73% managed internally and 27% managed by outside managers.



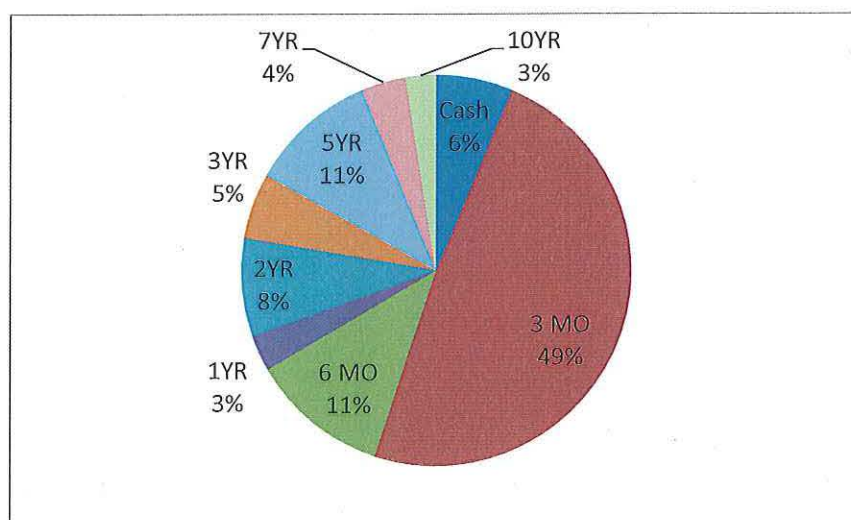
The overall yield to maturity (YTM) as of March 31, 2018 for the General Portfolio was 2.02%. Below is the YTM breakdown by portfolio:

- Internally managed portfolios were 1.84%
- Chicago Equity Partners (CEP) portfolio was 2.47%.
- MacKay Shields (MKS) portfolio was 2.58%

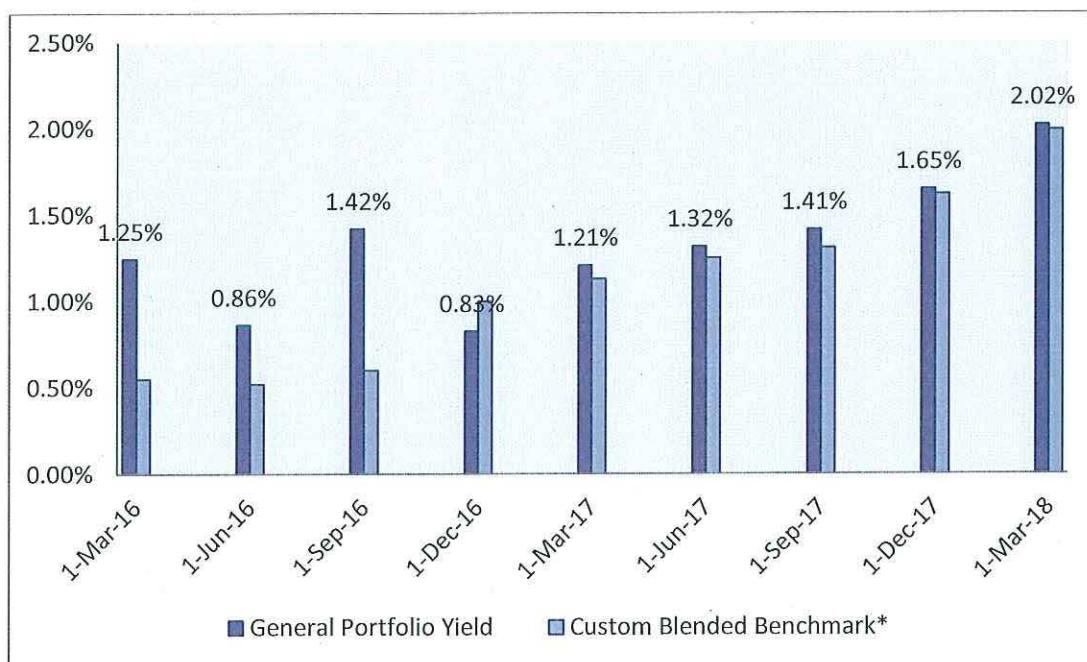
Although the outside managers' charts on pages 4 and 5 indicate declines in the overall market values, these portfolios have not incurred any realized losses to date, as securities have not been sold. The valuations are the result of the current rising interest rate environment which negatively affects the market value of the longer-term securities being invested with the outside managers. As noted above, if the outside managers held their respective investments to maturity, the yield would be 2.47% for CEP and 2.58% for MKS.

Treasurer's staff indicated at the March meeting that it is currently working to create a more applicable custom benchmark for the overall General Portfolio. To date, we are currently working with the Attorney General's Office to purchase a subscription of an index service (ICEBAML Indices subscription).

Therefore, for this report, staff has created a customized benchmark using the actual General Portfolio asset weighted maturities each quarter versus Treasury yields on maturities which match that of the General Portfolio. Below is a graphical representation of the asset weighted maturities in the General Portfolio as of March 31, 2018.



The asset weighted maturities of the General Portfolio has remained fairly consistent with the chart as of March 31, 2018. Although the General Portfolio contains other fixed income categories beyond Treasuries, staff will continue to work on a benchmark which contains various asset categories, such as agencies and corporate fixed income.

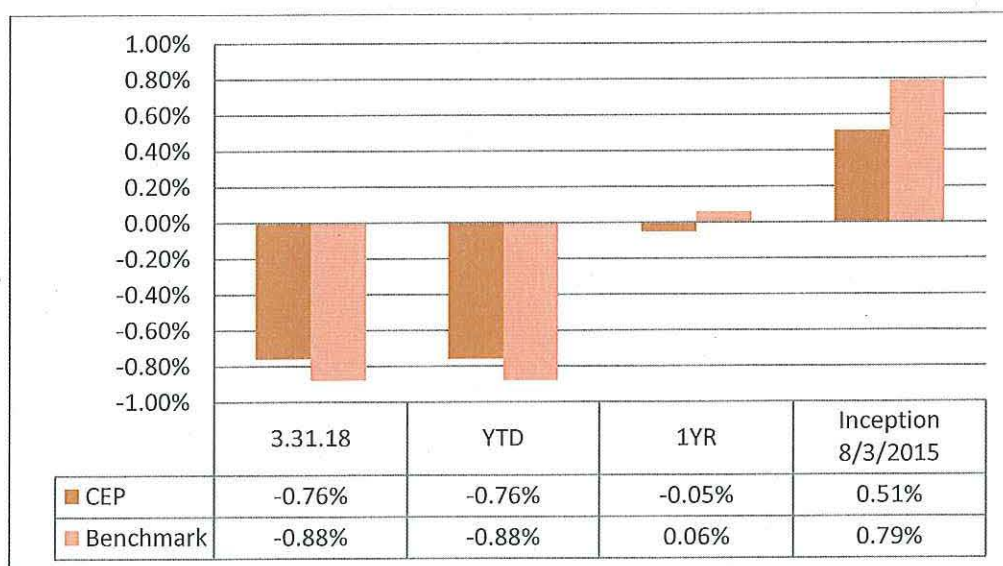


*Custom benchmark yield matches the asset-weighted maturities of the General Portfolio for each quarter to the appropriate Treasury yield.

General Portfolio Outside Managers' Performance

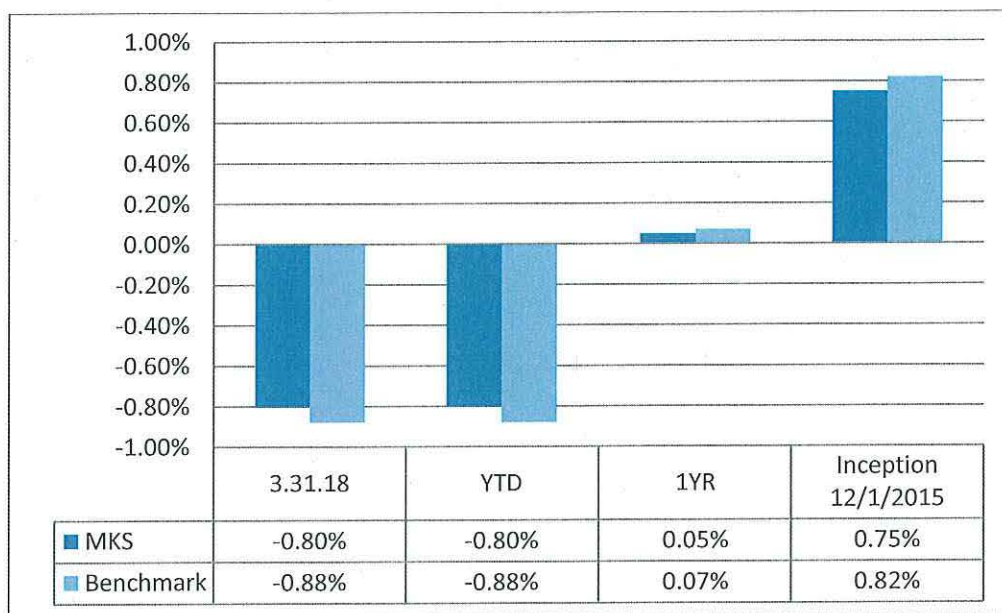
Chicago Equity Partners (CEP) began managing \$200 million in General Portfolio assets on August 3, 2015 with an additional \$100 million in 2016 for a total of \$300 million.

The year to date time weighted performance is 0.51%. As of March 31, 2018, CEP has distributed \$8.63 million in net interest since inception. The hard dollar fees paid since inception to CEP as of March 31, 2018 were \$890,388 (.029%).

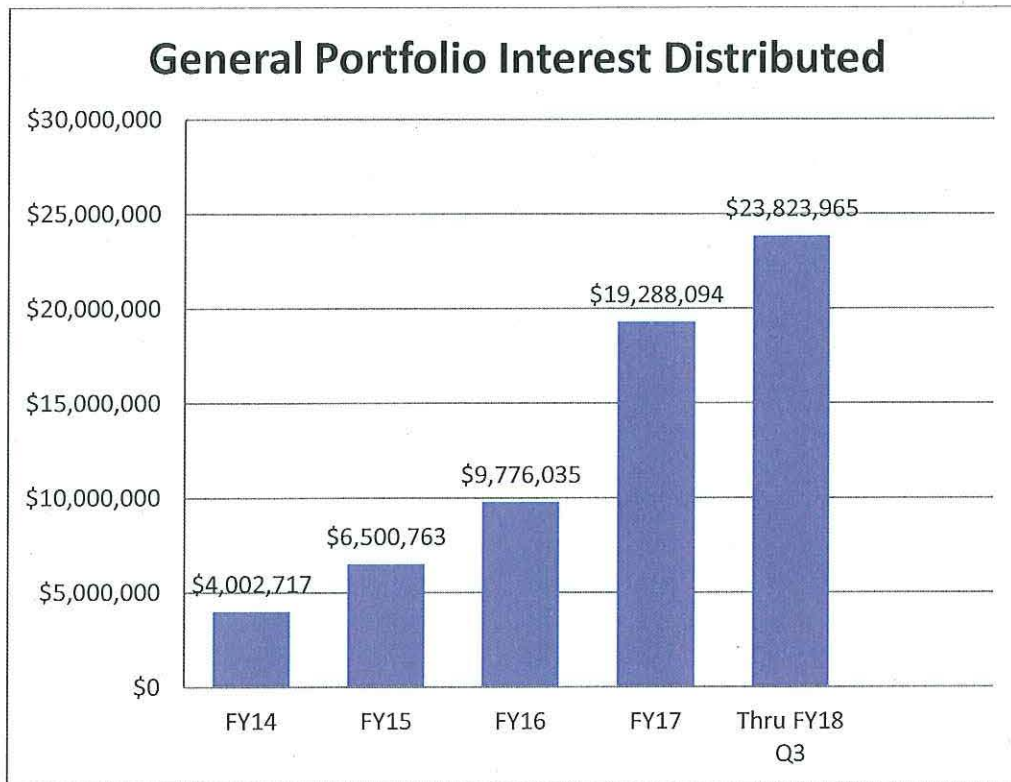


MacKay Shields (MKS) began managing \$200 million in General Portfolio assets on December 1, 2015 with an additional \$100 million for a total of \$300 million.

The year to date time weighted performance is 0.75%. As of March 31, 2018, MKS has distributed \$7.49 million in net interest since inception. The hard dollar fees paid since inception to MKS as of March 31, 2018 were \$917,127 (.026%).



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. Staff provides additional attribution information at each meeting in regards to these differences and their impact on the portfolios.



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 2018
Period Ending
March 31, 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

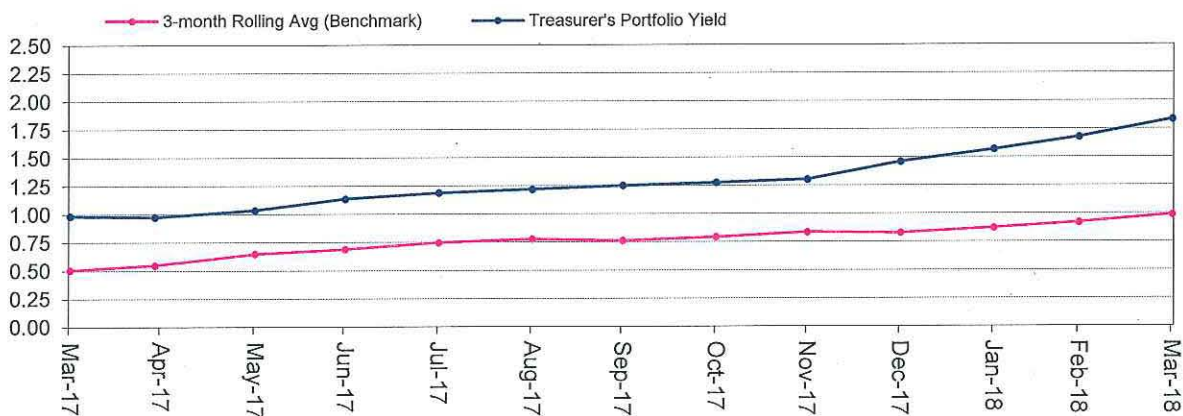
The permissible investments of the General Portfolio include United States Treasury and Agency securities, repurchase agreements, high quality corporate notes and commercial paper, negotiable certificates of deposit, municipal bonds and banker's acceptances. These securities are diversified to prevent 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 March 31, 2018, the yield on the portion of the General Portfolio managed in-house was 1.835%. A three month rolling average of this benchmark for this period was .99% with the average days to maturity at 218 days. The average days to maturity for the in-house managed portfolio was .48 years or 176 days.

In-House Performance vs. Benchmark

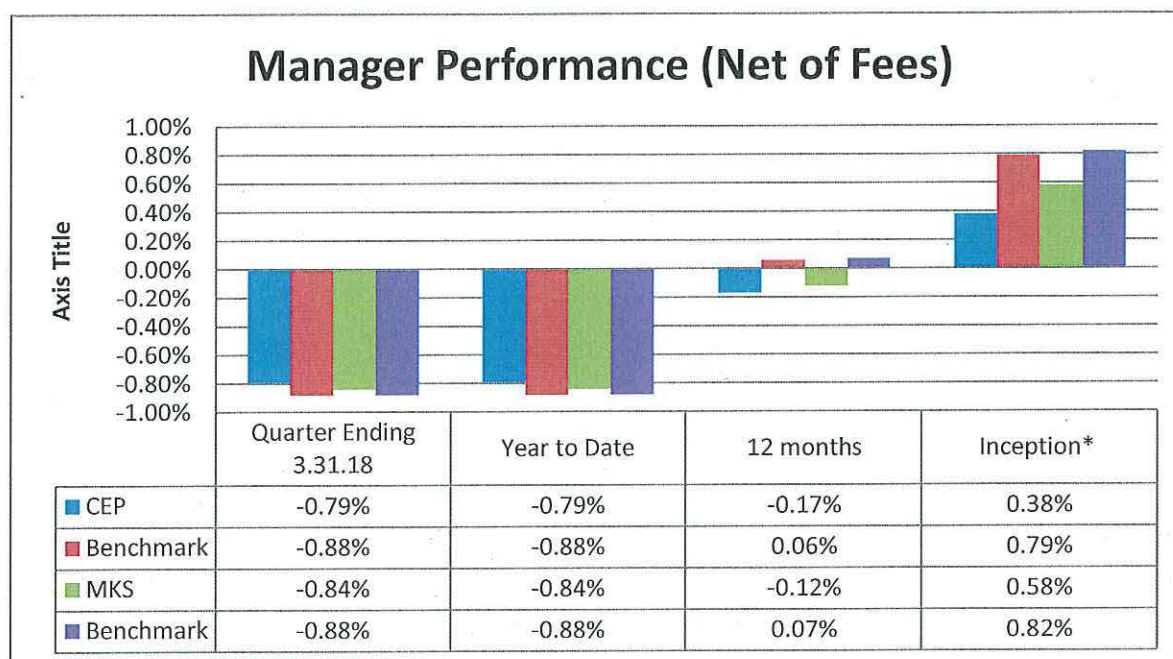


* Benchmark is 3-month rolling weighted average of 80% 3-month Treasuries and 20% 2-year Treasuries

Outside Manager Performance

The annualized performance since inception for period ending March 31, 2018 for manager Chicago Equity Partners (CEP) is 0.38% and for Mackay Shields (MKS) is 0.58%*. 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



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 March 31, 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.

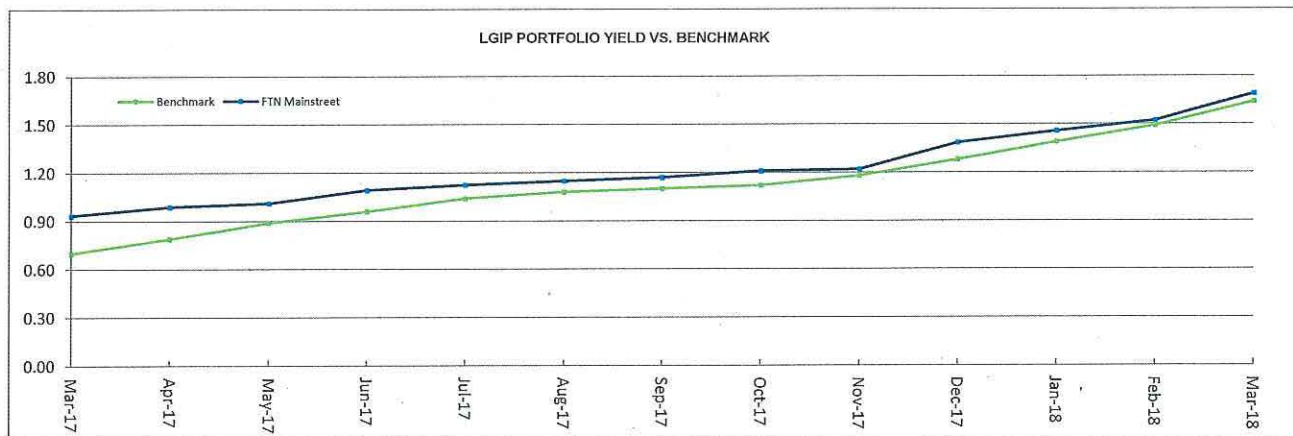
Investment Guidelines

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 20% 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 March 31, 2018, the LGIP's portfolio yield was 1.69%, and the blended benchmark was 1.64%. The average days to maturity of the LGIP portfolio was 123 days.

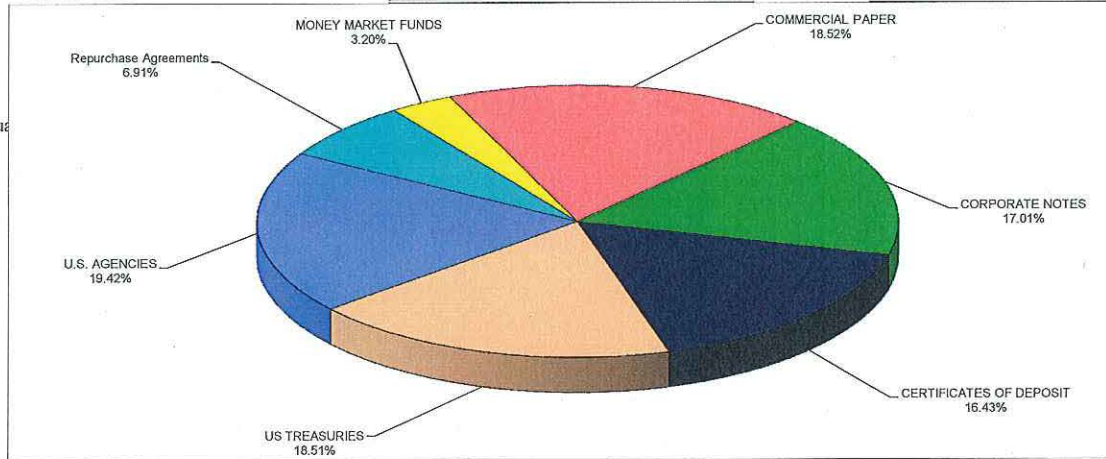


* Benchmark is 3-month rolling weighted average of 20% Dealer Commercial Paper 90-Day Index, 60% Agency Discount Note 6-Month Index, and 20% Morgan Stanley Institutional Liquidity Government Portfolio Fund.

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>March 31, 2018</u>		<u>December 31, 2017</u>	
	<u>Amortized Book</u>	<u>Purchased Interest</u>	<u>Amortized Book</u>	<u>Purchased Interest</u>
MONEY MARKET FUNDS	\$ 36,944,799	\$ -	\$ 22,728,725	\$ -
COMMERCIAL PAPER	214,380,338	-	188,417,335	-
CORPORATE NOTES	196,404,837	554,938	170,399,606	525,233
CERTIFICATES OF DEPOSIT	190,210,203	-	177,203,058	-
MUNICIPAL BONDS	-	-	-	-
U.S. TREASURIES				
NOTES	184,594,834	-	199,552,122	396,095
BILLS	29,732,110	-	-	-
U.S. AGENCIES	224,813,829	17,118	114,805,855	24,340
ASSET-BACKED SECURITIES	-	-	-	-
REPURCHASE AGREEMENTS	80,000,000	-	155,000,000	-
TOTAL	\$ 1,157,080,951	\$ 572,056	\$ 1,028,106,701	\$ 945,669
GRAND TOTAL	\$ 1,157,653,007		\$ 1,029,052,369	



YEAR-TO-YEAR BOOK VALUE AND PURCHASED INTEREST COMPARISON

	<u>March 31, 2018</u>	<u>March 31, 2017</u>
TOTAL PORTFOLIO	\$1,157,653,007	\$984,789,340