

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_14_17 BoF Agenda Item #8– State Treasurer Investment Report

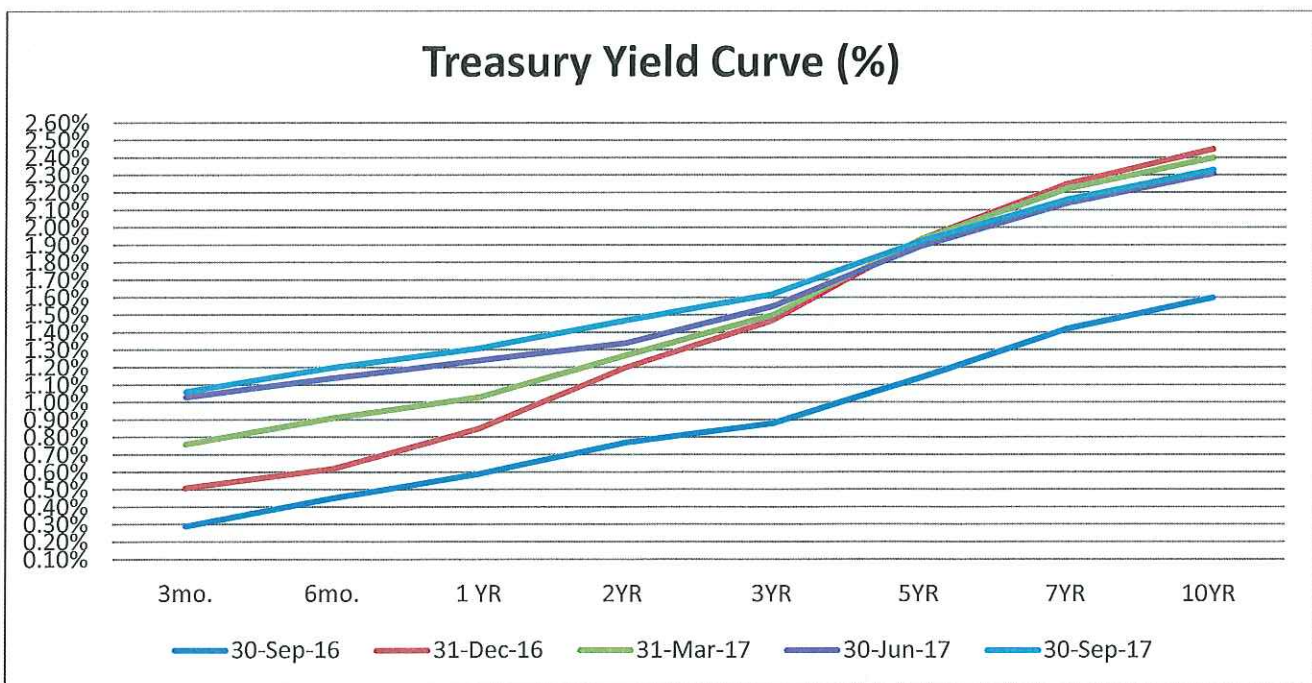
DATE: November 3, 2017

Agenda Item #8

Discussion and possible action (a) regarding the State Treasurer's quarterly investment report for the quarter ending September 30, 2017 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

Interest rates rose modestly across the maturities in the past three months (July 1 – September 30), with somewhat larger increases in shorter maturities. As a result, the Treasury curve flattened another 7 basis points. The Federal Reserve has begun its tapering program. The Fed will reduce its holdings of US Treasuries by \$6 billion a month and agency mortgage-backed securities by \$4 billion a month. The markets attach a high probability (~82%) of a rate increase after the December Federal Open Market Committee (FOMC) meeting.



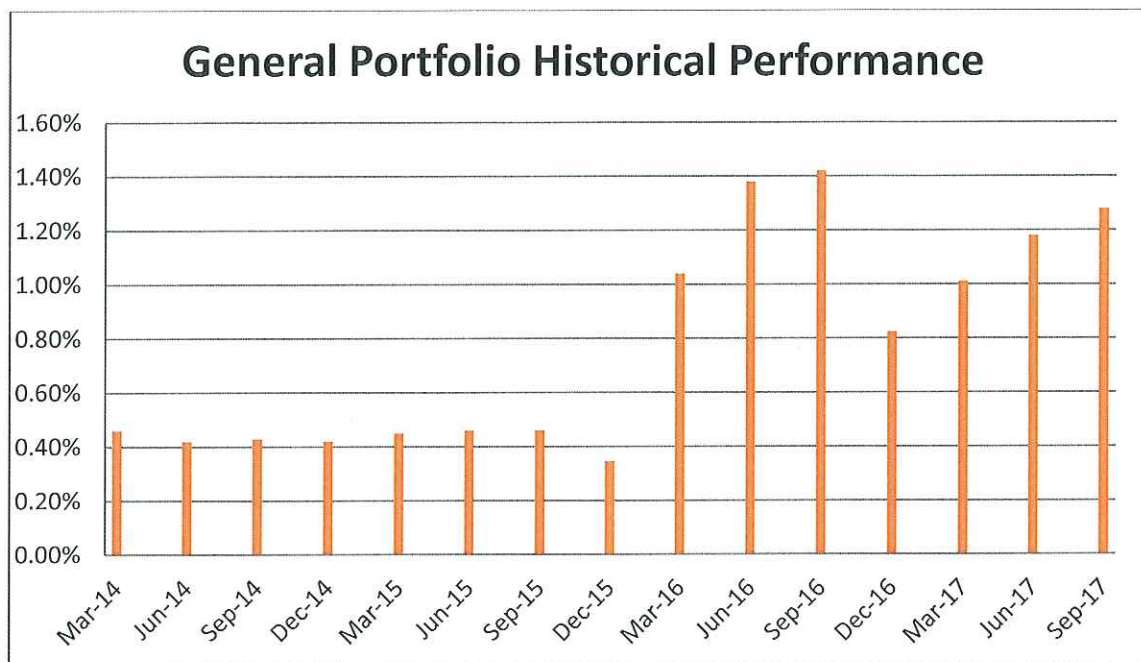
Current Performance:

The attached reports indicate performance for the quarter ending September 30, 2017.

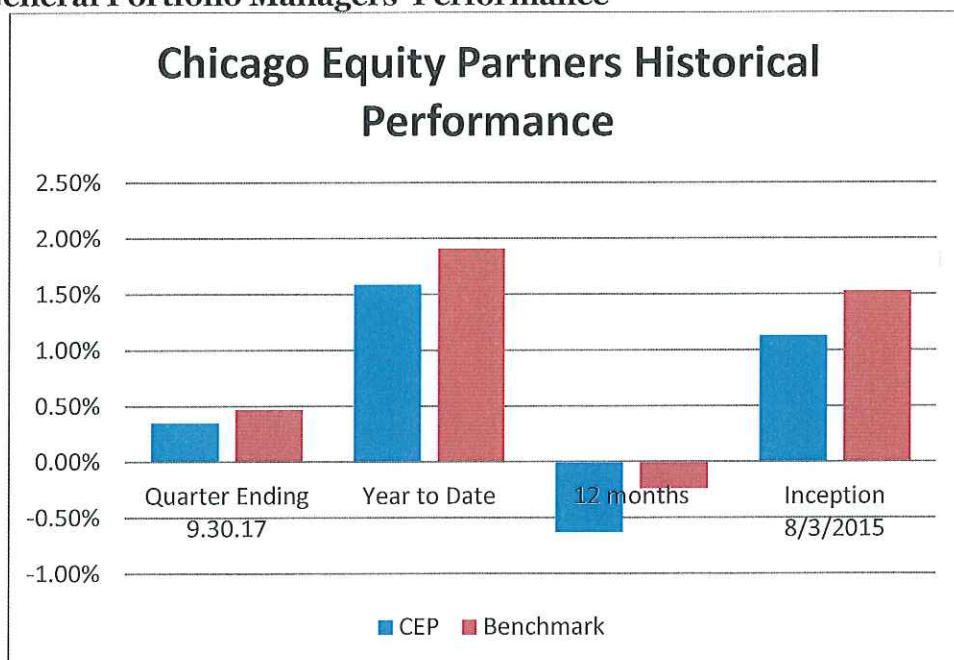
- FTN Financial began managing the LGIP portfolio in July 2015. The yield to maturity as of September 30, 2017 for LGIP assets was 1.17% which is 0.07% in excess of the benchmark return of 1.10%.
- The yield to maturity as of September 30, 2017 for total assets in the General Portfolio is 1.65% and the effective duration is 1.42 years which is in compliance with the requirement to maintain an effective duration of less than 1.50 years.
 - The yield to maturity of the internally managed portion of the General Portfolio was 1.252% which is 0.49% in excess of the custom blended benchmark return of 0.76%.
 - 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 1.59%. As of September 30, 2017, CEP has distributed \$6.80 million in net interest since inception. The hard dollar fees paid since inception to CEP as of September 30, 2017 were \$707,914.
 - 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 1.84%. As of September 30, 2017, MKS has distributed \$5.02 million in net interest since inception. The hard dollar fees paid since inception to MKS as of September 30, 2017 were \$750,210.

Historical General Portfolio Performance (includes external and internal management)

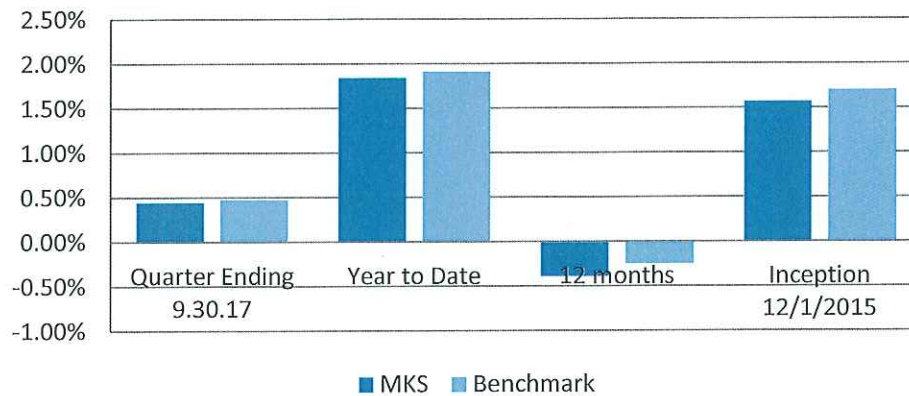
The General Portfolio performance as noted in the graph below began to improve in calendar year 2016 with the longer maturity holdings outperforming the shorter maturity holdings. The managers' performance during mid-2016 was ~2.50% - 3.57%; however, in the 4th quarter of 2016, interest rates rose and fixed income returns on the longer maturity holdings sharply decreased which resulted in substantially lower returns. The increase in interest rates over the past three quarters has increased the return on the shorter maturities which has helped boost performance in 2017.



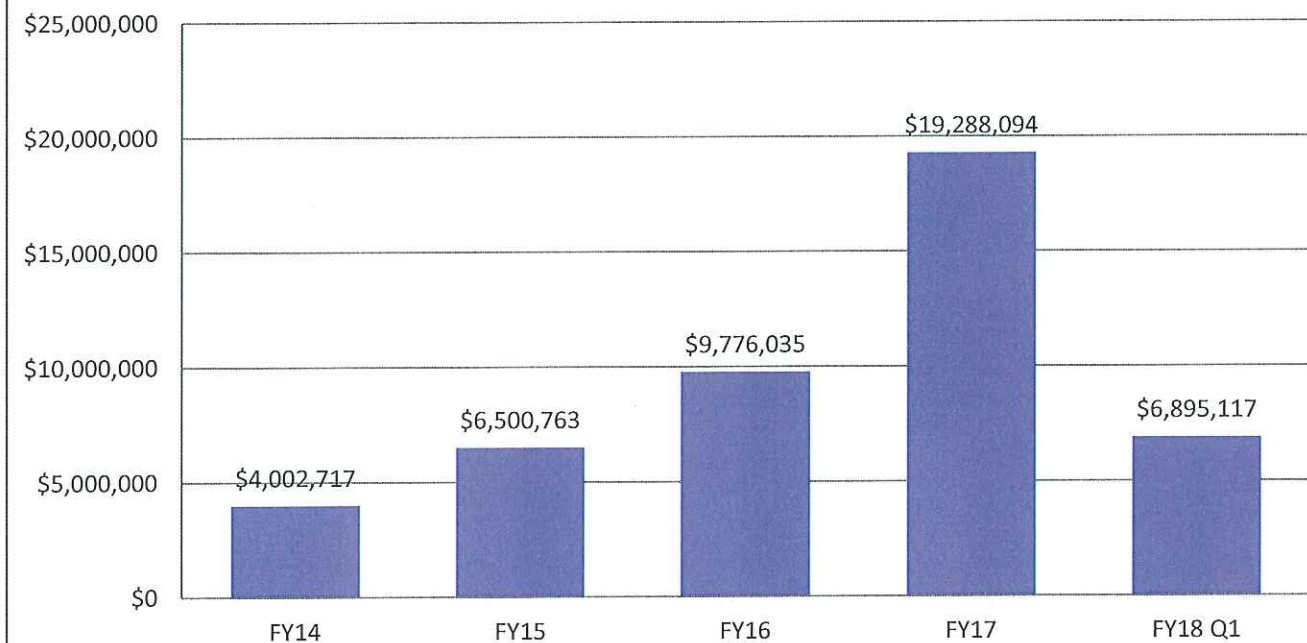
Historical General Portfolio Managers' Performance



MacKay Shields Historical Performance



General Portfolio Interest Distributed



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
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INVESTMENTS

GENERAL PORTFOLIO

FISCAL YEAR 2018
Period Ending
September 30, 2017

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

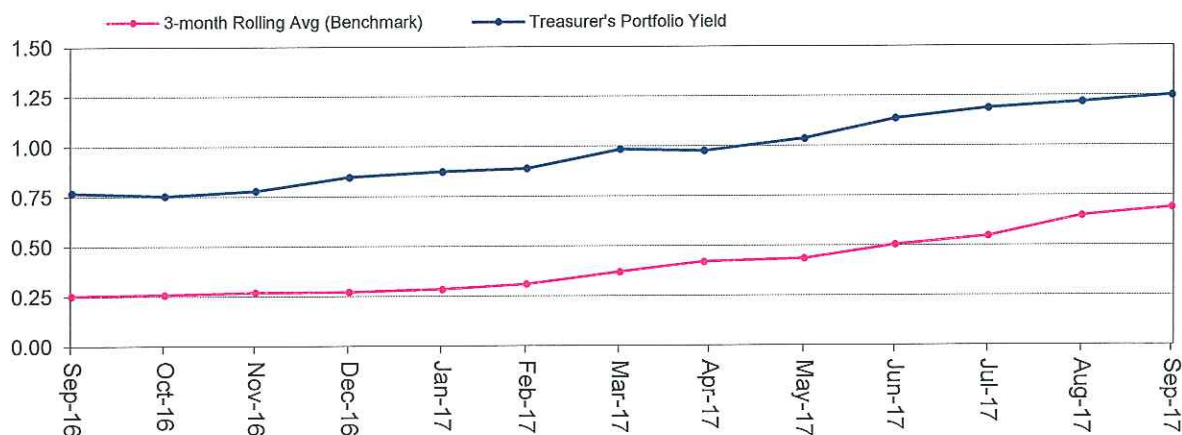
The permissible investments of the General Portfolio include United States Treasury and Agency securities, repurchase agreements, high quality corporate notes and commercial paper, negotiable certificates of deposit, municipal bonds and banker's acceptances. These securities are diversified to prevent 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, 2017, the yield on the portion of the General Portfolio managed in-house was 1.252%. A three month rolling average of this benchmark for this period was .76% with the average days to maturity at 218 days. The average days to maturity for the in-house managed portfolio was .44 years or 161 days.

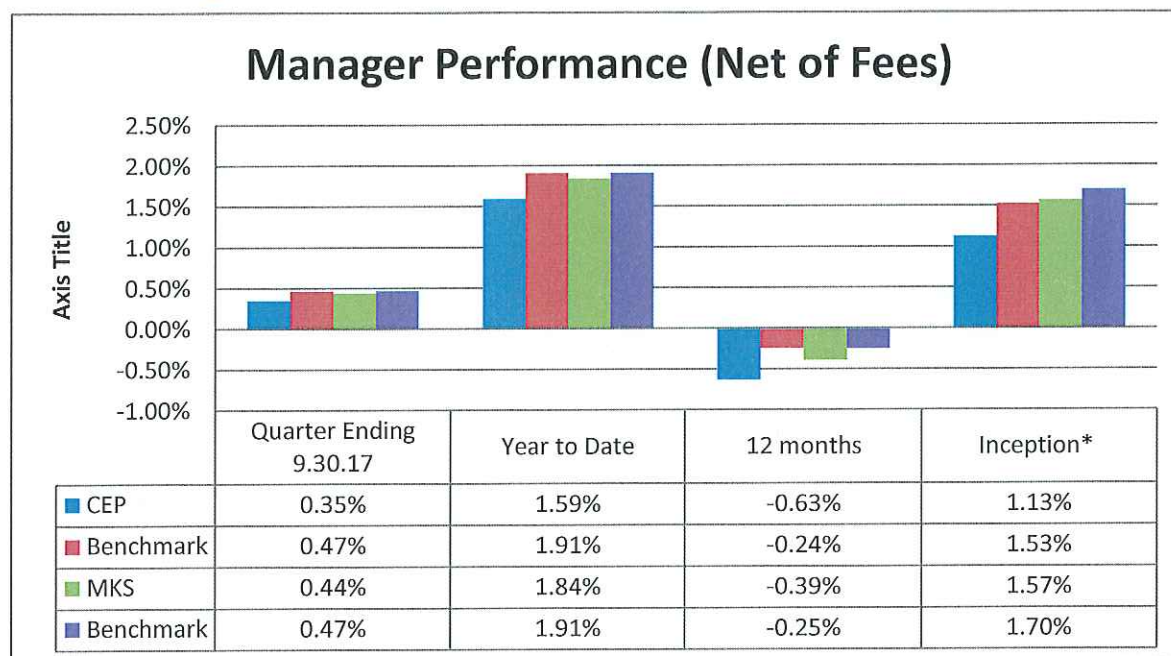
In-House Performance vs. Benchmark



Outside Manager Performance

The performance since inception for period ending September 30, 2017 for manager Chicago Equity Partners (CEP) is 1.13% and for Mackay Shields (MKS) is 1.57%*. 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 September 2015 and MKS is December 2015.

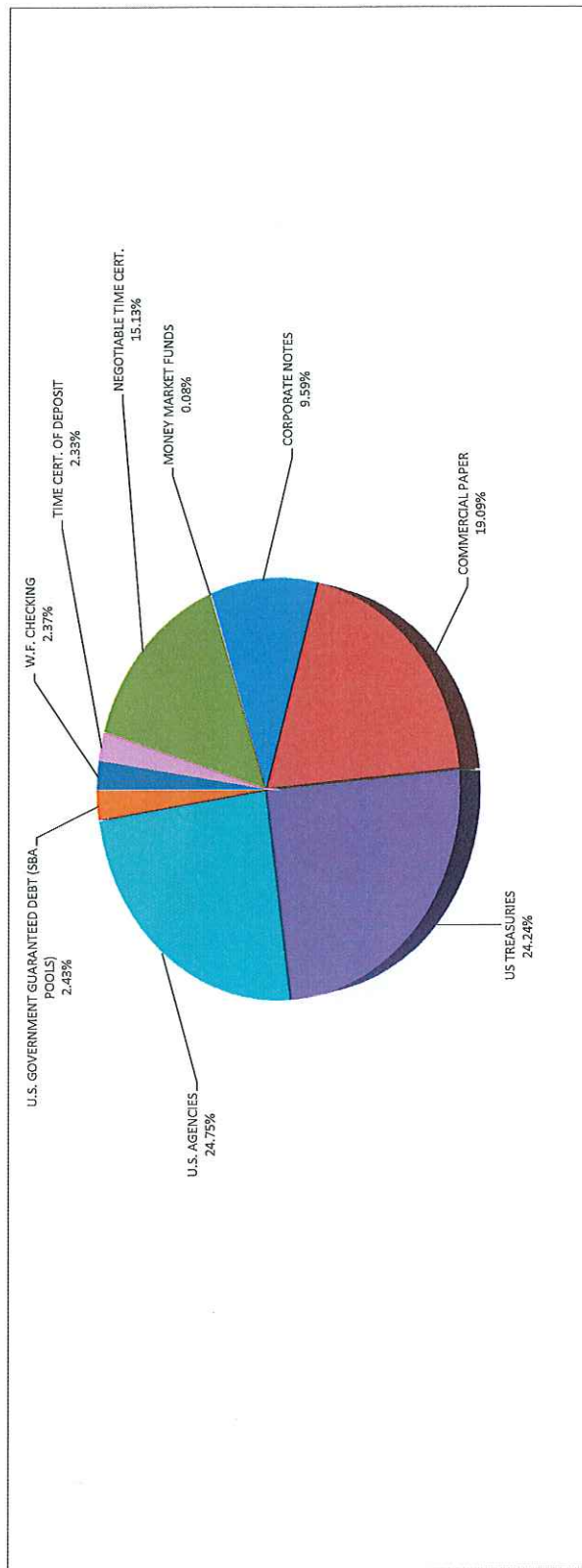
Outside Managers' Performance vs. Benchmark



*Inception date for CEP is 8.3.15 and 12.1.15 for MKS

GENERAL PORTFOLIO Amortized Book Value and Purchased Interest

	September 30, 2017			
	Amortized Book Value		Amortized Book Value	
	Treasurer In-House	Chicago Equity Partners	Treasurer In-House	Chicago Equity Partners
	\$		\$	
WASHINGTON FEDERAL CHECKING ACCT.	50,905,701		50,774,756	
TIME CERTIFICATES OF DEPOSIT	50,000,000		50,000,000	
NEGOTIABLE CERTIFICATES OF DEPOSIT	325,005,989		477,000,000	
MONEY MARKET FUNDS	1,024,428	567,716	2,537,402	649,075
ASSET-BACKED SECURITIES	0	0	0	276,152
MORTGAGE-BACKED SECURITIES	0	0	0	
CORPORATE NOTES	89,756,292	22,899,952	68,498,000	22,929,843
COMMERCIAL PAPER	410,165,594	93,440,114	356,000,000	87,823,863
MUNICIPAL BONDS	0		2,350,000	
U.S. TREASURIES	47,951,586	266,251,858	30,000,000	263,266,334
U.S. AGENCIES	509,888,002	16,975,242	529,900,000	211,183,137
U.S. GOVERNMENT GUARANTEED DEBT	52,212,732	4,999,867	18,967,899	4,999,711
REPURCHASE AGREEMENTS	0		51,119,194	
TOTAL	1,536,910,323	306,694,766	1,714,179,352	305,813,150
GRAND TOTAL	\$	\$	\$	\$
		2,148,716,689		2,324,275,365



YEAR-TO-YEAR BOOK VALUE AND PURCHASED INTEREST COMPARISON

	September 30, 2017	September 30, 2016
TOTAL PORTFOLIO	\$2,148,716,689	\$2,035,614,383

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

	Quarter Ended 09/30/2017	Quarter Ended 12/31/2017	Quarter Ended 03/31/2018	Quarter Ended 06/30/2018	FY 2018 Totals
<u>Average Daily Balances of Funds</u>					
General Fund	600,557,399				600,557,399
All Funds	2,422,777,800				2,422,777,800
<u>Annualized Interest Rate</u>					
Cash Basis (see Note 1)	1.1599%				1.1599%
Accrual Basis	1.1272%				1.1272%
<u>Interest Distribution for General Fund (Cash Basis)</u>					
General Fund Interest Collected	1,709,131				1,709,131
General Fund Interest Revenue - Distributed	1,709,131				1,709,131
Undistributed General Fund Interest Revenue	-				-
<u>Interest Distribution for All Funds (Cash Basis)</u>					
All Funds Interest Collected	6,895,117				6,895,117
All Funds Interest Revenue - Distributed	6,895,117				6,895,117

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, 2017, 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.

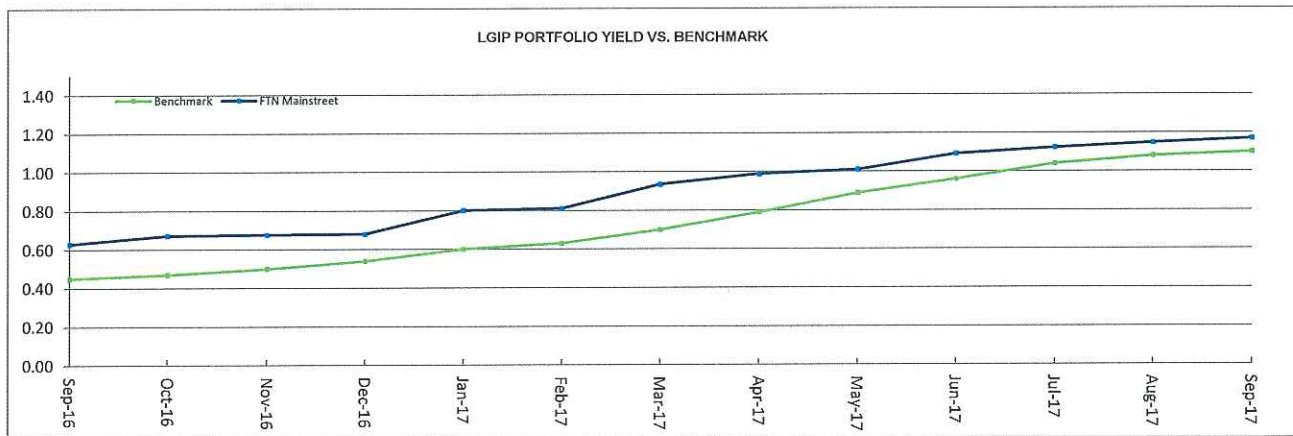
Investment Guidelines

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

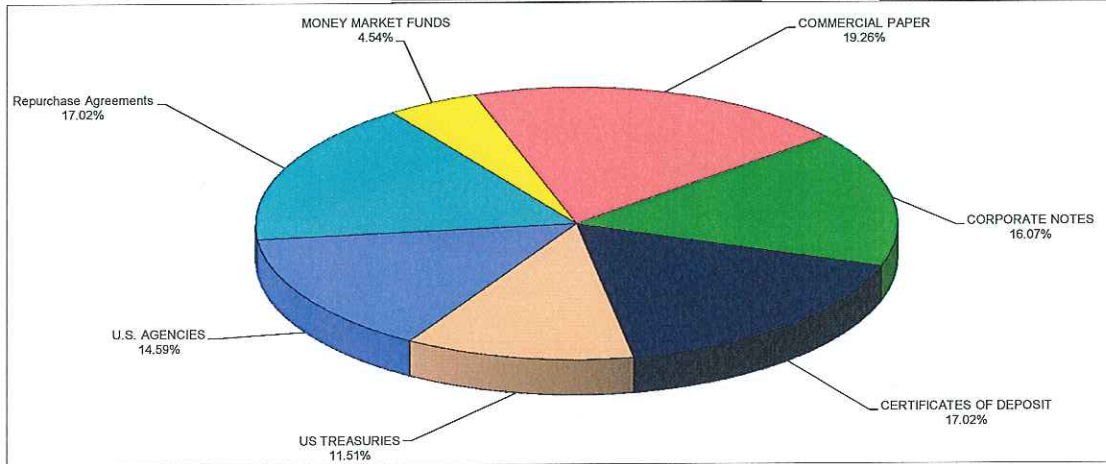
FTN Financial began managing the LGIP portfolio in July 2015. As of September 30, 2017, the LGIP's portfolio yield was 1.17%, and the blended benchmark was 1.10%. The average days to maturity of the LGIP portfolio was 113 days.



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, 2017</u>		<u>June 30, 2017</u>	
	<u>Amortized Book</u>	<u>Purchased Interest</u>	<u>Amortized Book</u>	<u>Purchased Interest</u>
MONEY MARKET FUNDS	\$ 45,381,810		\$ 12,492,647	
COMMERCIAL PAPER	192,342,772		150,000,000	
CORPORATE NOTES	160,145,087	359,396	157,514,000	99,054
CERTIFICATES OF DEPOSIT	170,016,961		135,000,000	
MUNICIPAL BONDS				
U.S. TREASURIES				
NOTES	114,873,229	54,295	85,000,000	1,537
BILLS				
U.S. AGENCIES	145,687,642		155,000,000	20,222
ASSET-BACKED SECURITIES	-		-	
REPURCHASE AGREEMENTS	170,000,000		135,000,000	
TOTAL	\$ 998,447,501	\$ 413,692	\$ 830,006,647	\$ 120,813
GRAND TOTAL	\$ 998,447,501	\$ 998,861,192	\$ 830,006,647	\$ 120,813



YEAR-TO-YEAR BOOK VALUE AND PURCHASED INTEREST COMPARISON

	<u>September 30, 2017</u>	<u>September 30, 2016</u>
TOTAL PORTFOLIO	\$998,861,192	\$766,288,676