



Quarterly Review of Investment Strategy

September 30, 2018

Bernalillo County, NM

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Bernalillo County Investment Committee

October 18, 2018

Bernalillo County Board of Finance

November 13, 2018








Table of Contents

- Investment Priorities
- Economic Update – Separate Document
- Investment Strategy: Operating Funds Portfolio
 - Current Portfolio
 - Strategy
- Investment Strategy: Bond Proceeds Portfolio
 - Current Portfolio
 - Strategy
- Fiduciary Standard

Investment Priorities

Investment Priorities

Our investment objectives and philosophy are consistent with all of our clients:

-  ***Safety is primary objective***
-  Transparency
-  Compliance
-  Liquidity
-  Yield

Investment Strategy – Operating Funds Portfolio

Bernalillo County Operating Funds Portfolio – Sept 30, 2018

	Market Value + Accrued	% of Total	Book Yield
<u>Highly Liquid Portfolio: Must Mature Within 30 Days Per Policy</u>			
CDARS/ICS:			
Bank of the West	\$ 75,997,884.15	25.54%	1.875%
Total Month-end CDARS/ICS Balances	\$ 75,997,884.15	25.54%	
<u>Liquid Portfolio: Must Mature Within 12 Months</u>			
Investments:			
US Treasury Securities	\$ 92,603,667.53	31.12%	1.947%
US Agency Securities	\$ 8,109,481.79	2.73%	1.688%
Cash - Wells Fargo MMF	\$ 10,290,789.39	3.46%	1.960%
Cash/Receivable	\$ 98,746.35	0.03%	0.00%
Summary of Negotiated Bank Deposits:*			
Wells Fargo Savings	\$ 5,460,305.18	1.84%	0.170%
Bank of the West	\$ 10,692.51	0.00%	0.079%
Total Month-end Bank Balances	\$ 5,470,997.69	1.84%	
Total Liquid Portfolio: 0-12 months	\$ 192,571,566.90	64.72%	1.857%
Core Portfolio	\$ 104,990,867.10	35.28%	2.042%
Total Operating Funds	\$ 297,562,434.00	100.00%	1.922%
Previous Month Operating Funds	\$ 295,556,503.73		1.827%

Bernalillo County Operating Funds Liquidity Portfolio

(ex. Highly Liquid Portfolio and Bank Products)

Balance Sheet Summary

	Bernalillo County Liq Op
Book Value	111,053,657.19
Accrued Balance	175,766.82
Net Unrealized Gain/Loss	-126,738.95
Market Value + Accrued	111,102,685.06

Net Income

	Bernalillo County Liq Op
Current Units	111,589,535.74
Interest Income	90,359.59
Net Amortization/Accretion Income	78,911.03
Net Realized Gain/Loss	0.00
Misc Income	0.00
Expense	0.00
Net Income	169,270.62

Index Comparison Summary

Risk Metric	Portfolio	Index	Difference
Duration	0.362	0.936	-0.574
Yield	2.244	2.620	-0.376
Years to Effective Maturity	0.361	0.951	-0.590
Years to Final Maturity	0.361	0.951	-0.590
Average Credit Rating	AAA	AAA	---

Fixed Income Holdings by Market Sector

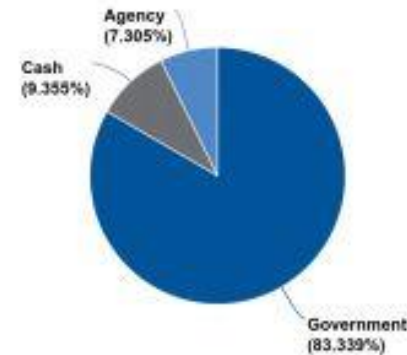
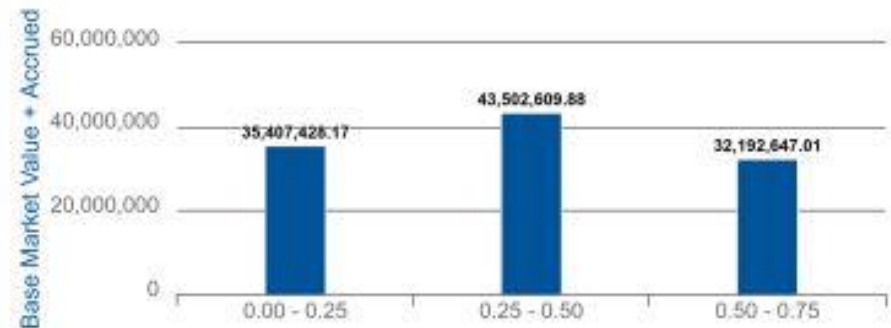


Chart calculated by: % of Book Value

Duration



Bernalillo County Operating Funds Core Portfolio

Balance Sheet Summary

	Bernalillo County Core Op
Book Value	105,512,840.90
Accrued Balance	465,516.82
Net Unrealized Gain/Loss	-987,490.62
Market Value + Accrued	104,990,867.10

Net Income

	Bernalillo County Core Op
Current Units	105,870,968.03
Interest Income	154,692.51
Net Amortization/Accretion Income	7,632.57
Net Realized Gain/Loss	-115,259.62
Misc Income	0.00
Expense	0.00
Net Income	47,065.46

Index Comparison Summary

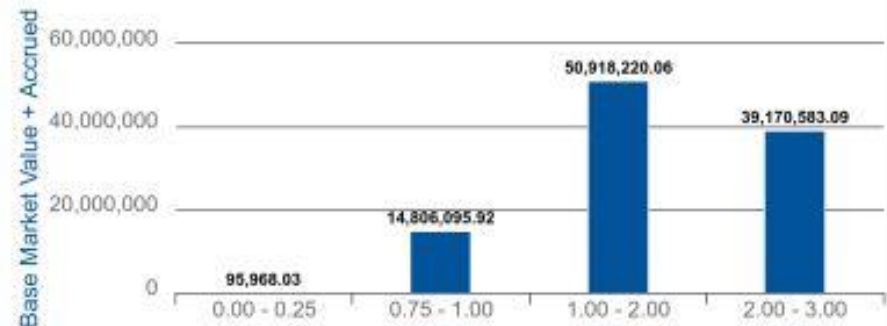
Risk Metric	Portfolio	Index	Difference
Duration	1.693	1.861	-0.168
Yield	2.767	2.808	-0.041
Years to Effective Maturity	1.749	1.932	-0.183
Years to Final Maturity	1.749	1.932	-0.183
Average Credit Rating	AAA	AAA	--

Fixed Income Holdings by Market Sector

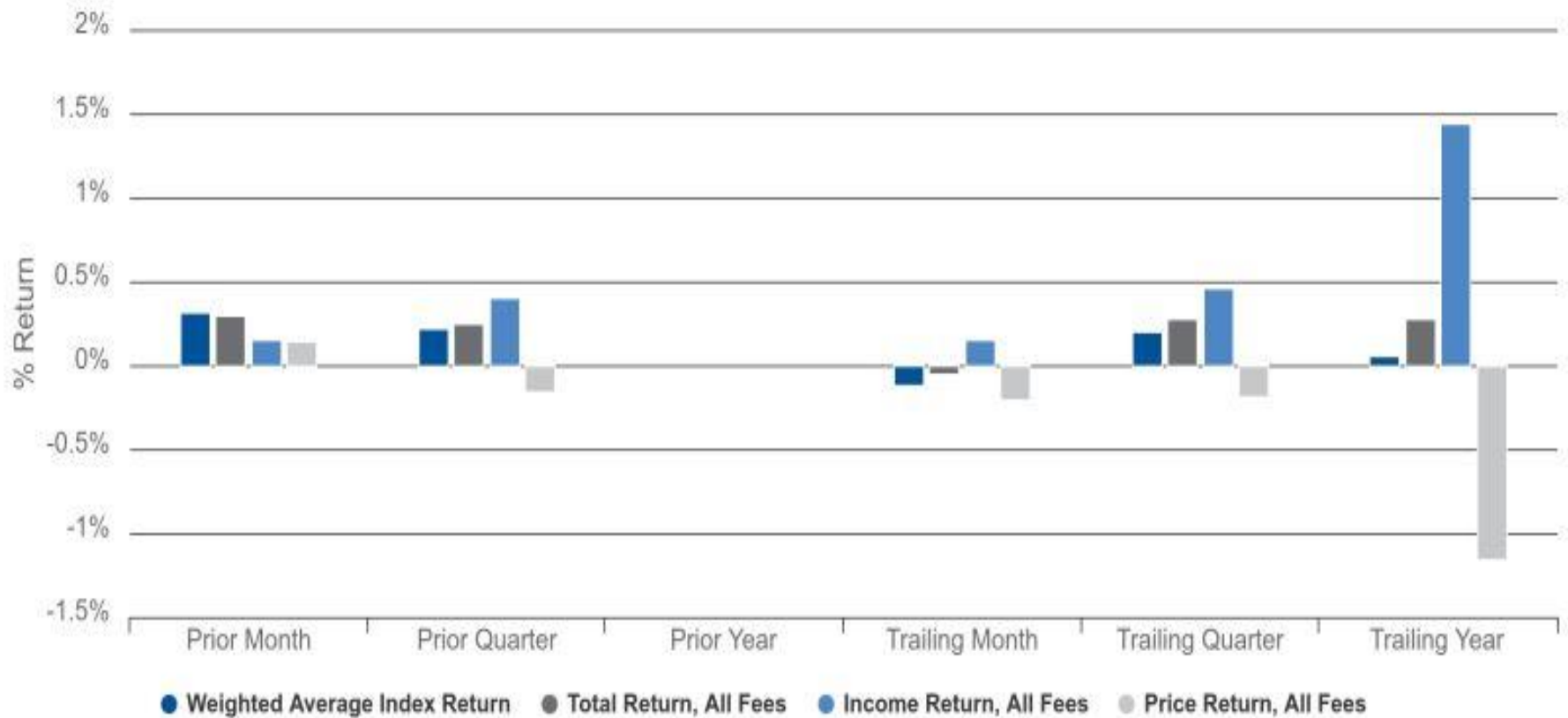


Chart calculated by: % of Book Value

Duration

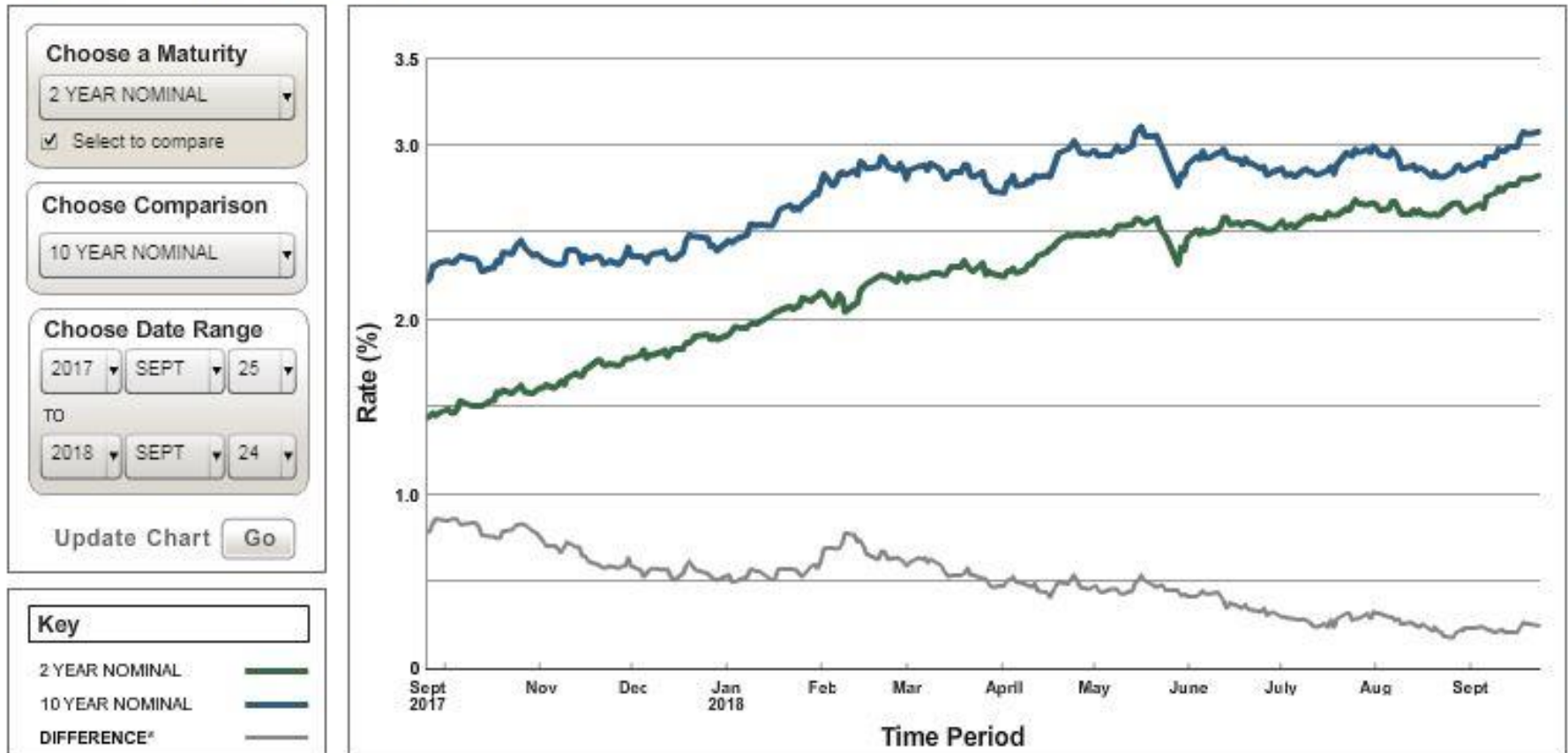


Bernalillo County Op Funds Core Portfolio - Performance



Flattening Yield Curve

Historical Treasury Rates



Source: US Department of the Treasury. <http://www.treasury.gov/resource-center/data-chart-center/interest-rates/Pages/Historic-LongTerm-Rate-Data-Visualization.aspx>, as of September 24, 2018

Quarterly Strategy Update – Operating Funds Portfolio

- The “Three Bucket” strategy is in place:
 - Bucket #1: “15% Rule”- Must Mature Within 30 Days
 - Includes the 15% Liquidity requirement as defined in the investment policy
 - Amount updated per FY19 budget, now \$73 million
 - Add benchmark
 - Bucket #2: Liquidity Ladder
 - Benchmark – 1 year T-bill
 - Includes smooth ladder of minimum \$5mm monthly maturities through 12months for a minimum total \$60 million to mature within 12 months
 - Bucket #3: Core Operating Funds
 - Benchmark – 1-3 year Treasury/Agency
 - Made up of reserve dollars
 - Actively managed
- Strategy approval for the operating funds portfolios will happen on a quarterly basis.
- The Bernalillo County Treasurer manages Bucket #1. Public Trust manages Buckets #2 and #3 on a non-discretionary basis.
- Annual Investment Policy updates will be presented for review by this committee and approval by the Board of Finance.

Investment Strategy: Three Buckets

Bucket	Policy Parameter (\$)	Current Position (\$ 9/30/18)	Goal (\$)	Strategy Comments
30 Day*	\$73 million	\$76.0 mm	\$73million	\$10mm WF MMF buffer
Liquidity	Balance of Funds	\$116.6mm	Balance of funds	With adoption of new policy, \$60mm must mature w/in 12 months
Core	Undefined	\$105.0mm	\$104million	After the low balance point in October 2018, check to see if there is another \$5-10mm to move here

* Defined as 15% of budget per Investment Policy

- ☰ Strategy approval for the operating funds portfolios will happen on a quarterly basis.
- ☰ Public Trust manages the Laddered Liquidity and Core portfolios on a non-discretionary basis.
- ☰ Bernalillo County manages the Highly Liquid 30 Day portfolio.
- ☰ Investment Policy updates presented for approval last quarter.

Investment Strategy – Bond Proceeds Portfolio

Bernalillo County Bond Proceeds Portfolio

Balance Sheet Summary

	Bernalillo County Bond Proceed
Book Value	72,663,392.07
Accrued Balance	246,718.22
Net Unrealized Gain/Loss	-179,400.86
Market Value + Accrued	72,730,709.43

Net Income

	Bernalillo County Bond Proceed
Current Units	73,017,804.06
Interest Income	88,494.57
Net Amortization/Accretion Income	34,853.71
Net Realized Gain/Loss	0.00
Misc Income	0.00
Expense	0.00
Net Income	123,348.29

Index Comparison Summary

Risk Metric	Portfolio	Index	Difference
Duration	0.737	0.936	-0.199
Yield	2.396	2.620	-0.224
Years to Effective Maturity	0.747	0.951	-0.204
Years to Final Maturity	0.747	0.951	-0.204
Average Credit Rating	AAA	AAA	--

Fixed Income Holdings by Market Sector

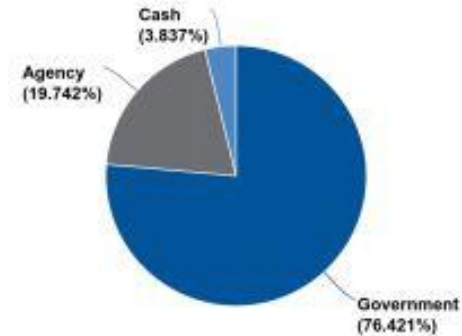
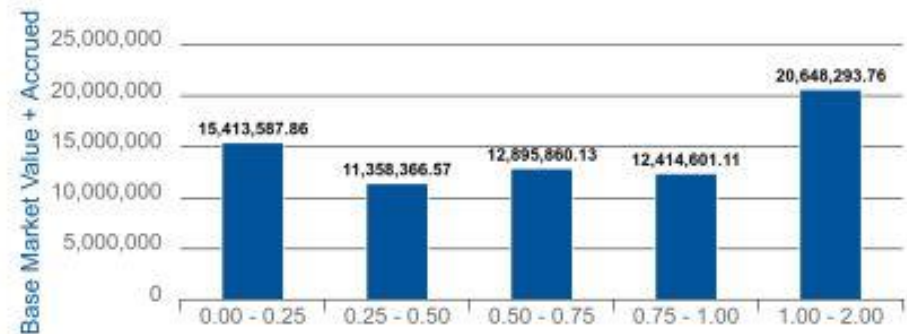


Chart calculated by: % of Book Value

Duration



Stable Strategy: Bond Proceeds Portfolio, Manage to Project Draws

- This portfolio strategy remains the same quarter to quarter.
- The GO bond proceeds portfolio maturities are laddered monthly to fund project draws. Any funds not needed for capital project draws will be invested at the end of the ladder.
- The working group is actively discusses cash flows for both GO Bond Proceeds and the GRT funded projects.
- Trade authorization will be required for each trade for both GO and GRT bond proceeds investments.
- A new bond issue was sold in July funded (\$16 million) on August 15, 2018.
- Please note that there was a compliance issue in this portfolio during the quarter ended September 30, 2018. The 5% cap on US Agency paper, as stated in the investment policy, was breached.
- Public Trust provided to the County two options for resolving this issue, both of which have no financial impact to the County and maintain the smooth ladder strategy. The trades to bring the portfolio into compliance were executed on October 16-17, 2018.
- Please see detailed description of the issue and the solution chosen by the County on the next three slides.

Compliance Issue: Bond Proceeds Portfolio

Bernalillo County's Investment Policy (dated August 2018) provides the guidelines and restrictions that governs the County's investment management program. Section VIII (Investment Parameters) provides diversification limits that apply individually to the operating fund and bond proceeds accounts. On August 28, 2018, Public Trust purchased multiple Government Sponsored Enterprise (GSE) securities in the bond account that violated the provisions as outlined under Section VIII. Bernalillo County's Investment Policy states that no more than 5% of the Bond portfolio may be invested in US Agency debt. The purchases on August 28th increased the bond portfolio's GSE exposure from 0% to 19%, triggering the violation in the bond account.

Public Trust utilizes Bloomberg's Asset and Investment Manager (AIM) system to monitor and verify investment policy compliance for all transactions on a pre- and post-trade basis. The Portfolio Management Team works in conjunction with Public Trust's Chief Compliance Officer (CCO) to ensure our Client's Investment Policies are properly coded into AIM. After reviewing the circumstances of the August 28th trades, Public Trust has identified the breakdown that allowed the violation to occur in AIM. The issue stems from the common use of the term "US Agency Securities". Technically speaking, "US Agency" implies securities that are backed by the full faith and credit of the United States Government. The U.S. Small Business Administration, Government National Mortgage Association and Federal Housing Administration are issuers of US Agency Debt. In contrast, Government Sponsored Enterprises (GSE) are financial service corporations formed by Congress that provide credit to targeted markets, predominantly the housing market. The Federal National Mortgage Association, Federal Home Loan Mortgage Corporation, Federal Home Loan Bank and Federal Farm Credit Bank are issuers of GSE debt. While GSEs carries a credit rating *pari passu* the United States Government, there is only an *implied* guarantee from the US Government. Despite this critical difference, Public Trust acknowledges the common practice of aggregating GSE debt into the "US Agency" classification. However, Bloomberg's AIM system *does* differentiate between Agency and GSE debt when processing compliance rules. Unfortunately, Public Trust did not catch the intent of the Bernalillo County Investment Policy when aggregating GSE and Agency Debt under the "Agency" classification. As a result, AIM did not catch the trades in question on August 28th as only Agency Debt, and not GSE were coded with the 5% restriction for the bond portfolio.

Compliance Issue: Bond Proceeds Portfolio

To put the bond portfolio back into compliance, Public Trust recommends the sale of the following securities:

Par	Cusip	Description	Coupon	Final Maturity
1,000,000	313396GK3	FEDERAL HOME LOAN MORTGAGE CORP	0.000	6/3/2019
1,500,000	313383VN8	FEDERAL HOME LOAN BANKS	2.000	9/13/2019
1,500,000	3137EADM8	FREDDIE MAC	1.250	10/2/2019
1,500,000	3135G0ZY2	FEDERAL NATIONAL MORTGAGE ASSOC	1.750	11/26/2019
1,500,000	3135G0A78	FEDERAL NATIONAL MORTGAGE ASSOC	1.625	1/21/2020
1,500,000	3135G0T29	FEDERAL NATIONAL MORTGAGE ASSOC	1.500	2/28/2020
1,000,000	3137EAEF2	FREDDIE MAC	1.375	4/20/2020
1,500,000	313370E38	FEDERAL HOME LOAN BANKS	3.375	6/12/2020

With the sale of these securities, the overall exposure to “Agency” debt will be reduced to roughly 4.5%. We would then recommend reinvesting the proceeds in the following US Treasury Securities:

Par	Cusip	Description	Coupon	Final Maturity
1,000,000	912828R85	UNITED STATES TREASURY	0.875	6/15/2019
1,500,000	9128282G4	UNITED STATES TREASURY	0.875	9/15/2019
1,500,000	912828T59	UNITED STATES TREASURY	1.000	10/15/2019
1,500,000	912828U32	UNITED STATES TREASURY	1.000	11/15/2019
1,500,000	912828V31	UNITED STATES TREASURY	1.375	1/15/2020
1,500,000	9128283Y4	UNITED STATES TREASURY	2.250	2/29/2020
1,000,000	912828X21	UNITED STATES TREASURY	1.500	4/15/2020
1,500,000	912828XU9	UNITED STATES TREASURY	1.500	6/15/2020

Compliance Issue: Bond Proceeds Portfolio

The yield curve has moved higher since late August, causing the market value to fall for the Agency bonds we are proposing to sell. The loss is purely a result of the yield curve shifting higher and not a reflection on the fundamental credit of the GSE issuers. Public Trust will document the realized loss that will occur from this sale and directly reimburse the County's bond account.

Due to the breach in the County's Investment Policy, Public Trust will institute an additional step to our firm-wide compliance process. After coding all policy rules into AIM, the Portfolio Manager and the CCO will jointly review the policy to ensure proper implementation.

Registered Investment Advisor – Standard of Care

Per Public Trust Advisors' current scope of work for Bernalillo County, we are required to prepare a quarterly investment review and present it to the Investment Committee and the Board of Finance. As a Registered Investment Advisor (RIA) under the Securities Exchange Act of 1940, we act in a fiduciary capacity for the County.

*A **fiduciary** relationship is generally viewed as the highest standard of customer care available under law. Fiduciary duty includes both a duty of care and a duty of loyalty. Collectively, and generally speaking, these duties require a fiduciary to act in the best interest of the customer, and to provide full and fair disclosure of material facts and conflicts of interest.*

~ Securities Industry and Financial Markets Association (SIFMA)

SIFMA Fiduciary Standard Resource Center, <https://www.sifma.org/issues/private-client/fiduciary-standard/overview/>

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Performance comparisons will be affected by changes in interest rates. Many factors affect performance including changes in market conditions and interest rates and in response to other economic, political or financial developments.. Investment involves risk, including the possible loss of principal. No assurance can be given that the performance objectives of a given strategy will be achieved. Past performance is not an indicator of future performance or results. Any financial and/or investment decision may incur losses.

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Benchmarks are provided for illustrative purposes only. Comparisons to benchmarks have limitations because benchmarks have volatility and other material characteristics that may differ from the portfolio. Performance results for benchmarks do not reflect payment of investment management/incentive fees and other fund expenses. Because of these differences, benchmarks should not be relied upon as an accurate measure of comparison.