

# Investing Best Practices – Starting at the Beginning

Government Finance Officers Association of Texas

Fall 2017

Presented By: Susan K. Anderson



# Overall Objectives:

- Assess your Tools & Abilities
- Starting/Monitoring the Investment Process
- Interacting with the “Market”
- Managing Expectations/  
Communicating with the Boss(es)
- Finding Resources for Assistance

# Assess Your Tools & Abilities:

- What Tools are Available – Internally or Externally?
- How Much Time Can be Dedicated?
- Is the Benefit Worthwhile?
- What Talents Are Available?
- How Can I Optimize the Tools and Talents Available?

# Starting/Monitoring the Investment Process:

- Identify Key Strategy Objectives
- Develop Basic Strategy Tools
- Consider CIP Strategies
- Compare Eligible Options
- Encourage Strategy Enhancements
- Strong Internal Controls

# Public Funds Investment Act – Broad Parameters

- Investment Policy –

***What Is Appropriate For Your Government?***

- Investment Strategy –

***Primarily emphasize safety of principal and liquidity***

# Strategy Development

- Disciplined Approach
- Evaluate Cash Flows
- Prudently Allocate
- Build and Maintain
- Be Flexible As Needs Change



# #1 Quickest “Added Value”

- Depository Bank Account Analysis Statement
- Way Too Much Over-compensation!
- Excess Balances Accrue FDIC Assessment
  - Recoupment Monthly
  - Insurance and Regulation Fee
  - Deposit Insurance Fee
  - FDIC Insurance
- Talk to Banker
- Determine Adequate Level
- Arrange Hard-Interest For Extra Balances



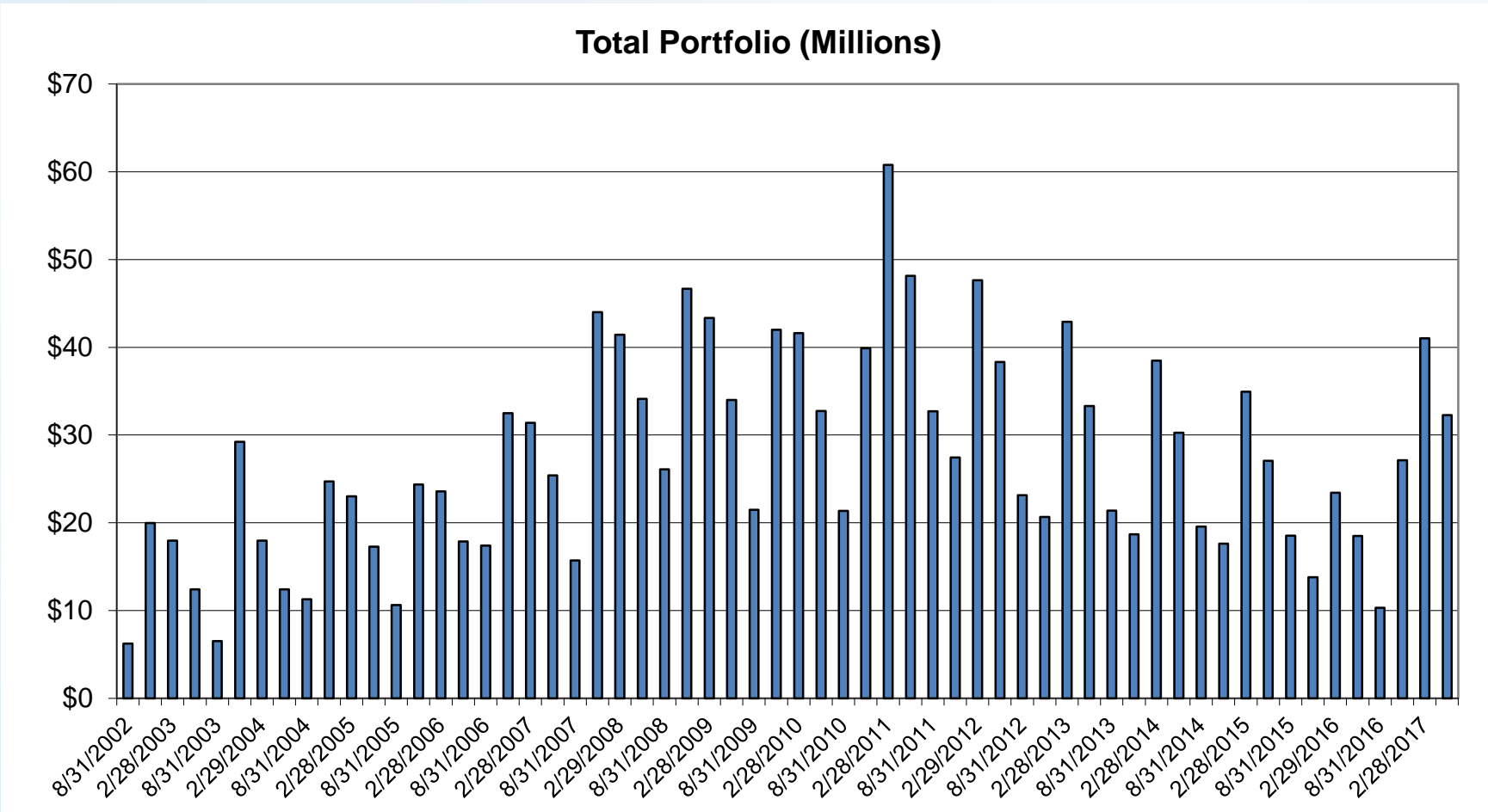
Primarily Emphasize Safety and Liquidity

“Cash Flow,  
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Cash Flow”

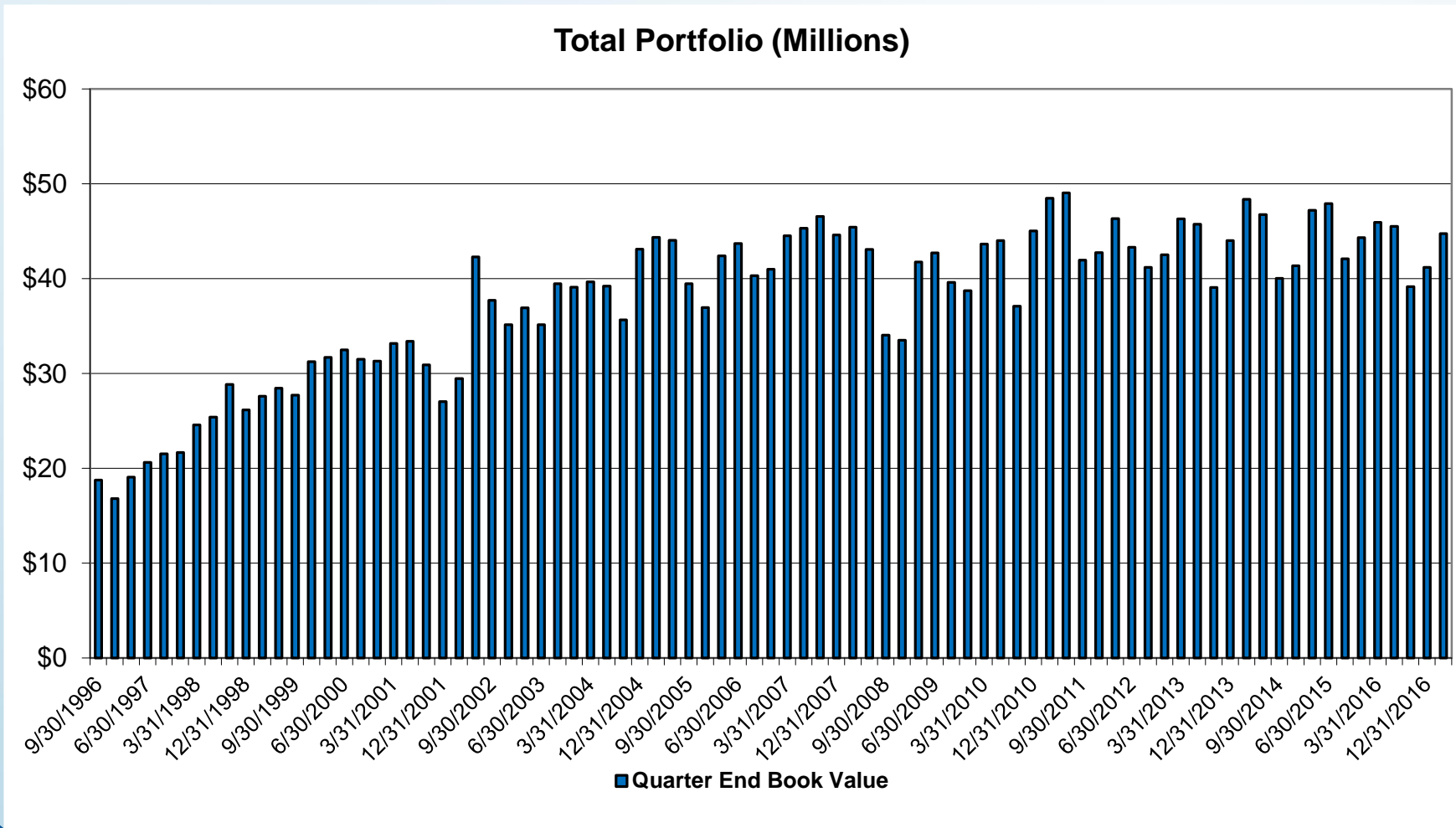




# Peaks and Valleys



# Gentle Waves



# Cash Projections

- Level One – Casual Understanding
- Level Two – Reasonable Estimates
- Level Three – Mega Detail



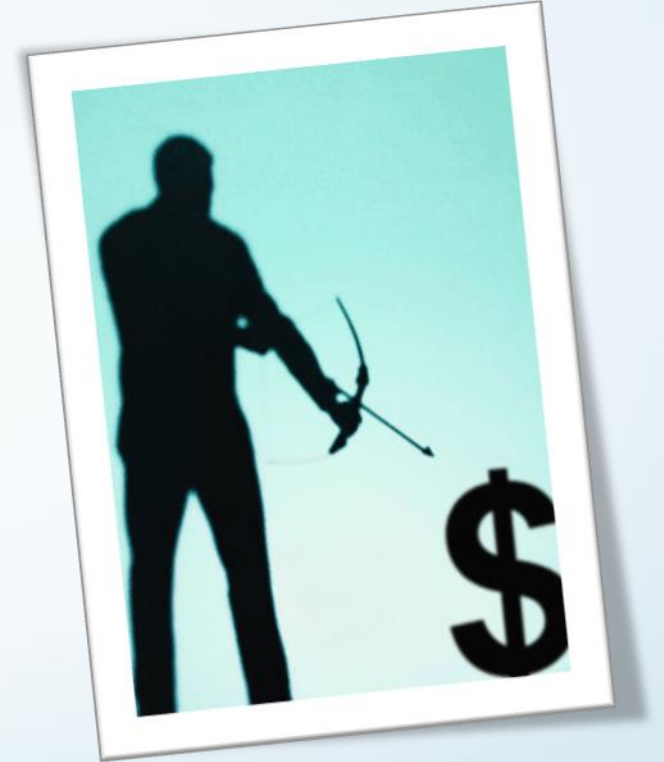
# Build Reasonable Estimates

- Basic Flows
  - Payroll
  - Debt Service
  - Operating
- Increase Detail (?)
- Compare to Current Balances

# CIP Draw Schedules

## CIP – Three Questions

- Project Cost?
- Start Date?
- Completion Target?

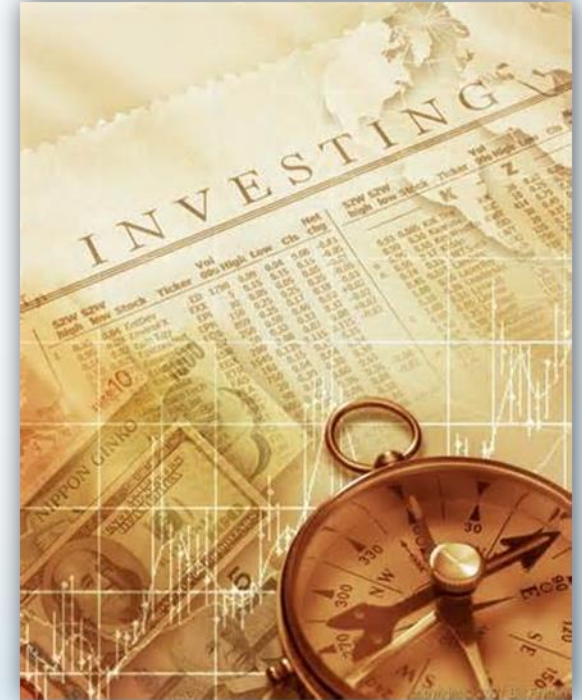


# Recap:

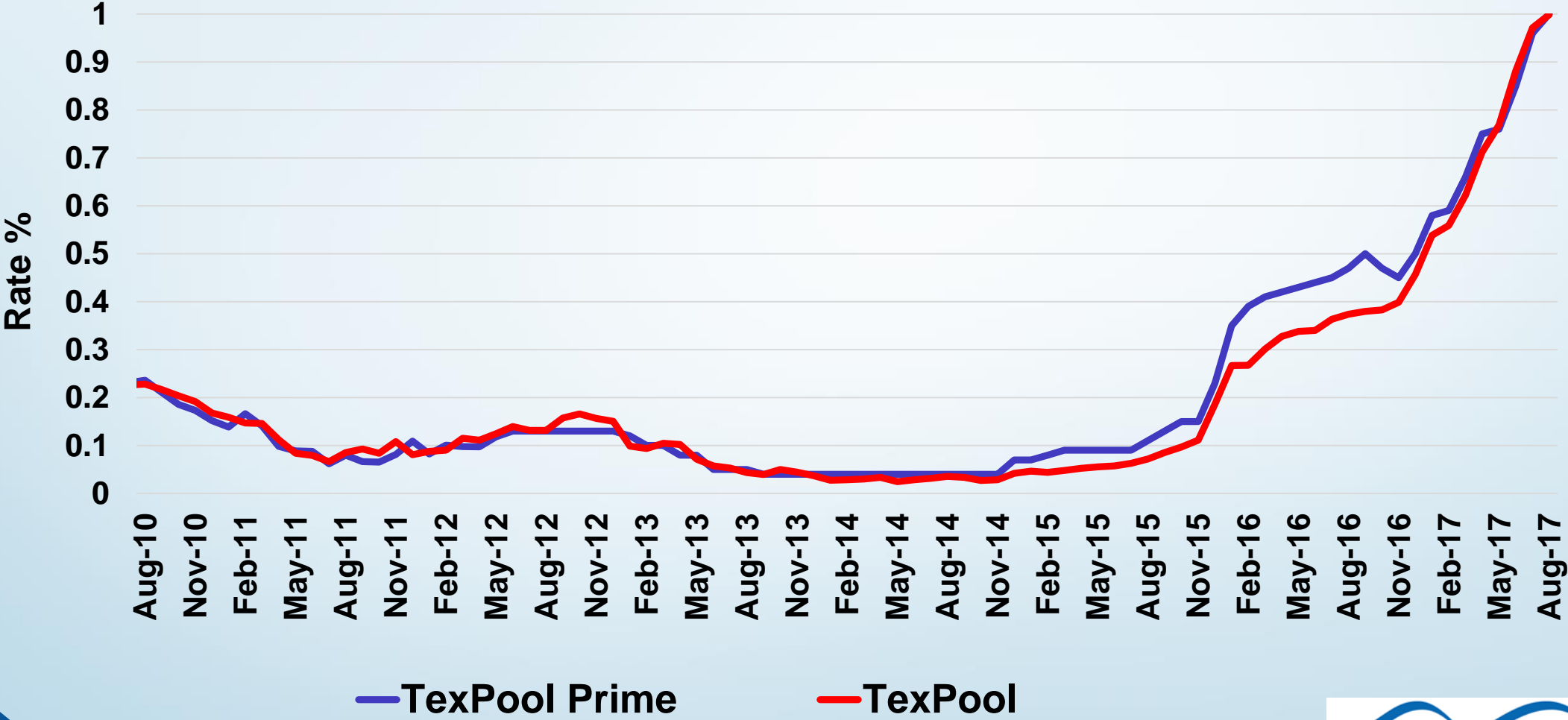
- Accessed Your Tools and Abilities
- Established or Reviewed the Investment Process
- Reviewed Investment Policy/Investment Strategy Documents
- Analyzed Cash Flow Needs

# Eligible Options (Conservative)

- Bank Money Market Account (MMA)
- Local Government Investment Pools
- Money Market Fund (MMF)
- Bank CDs
- Securities

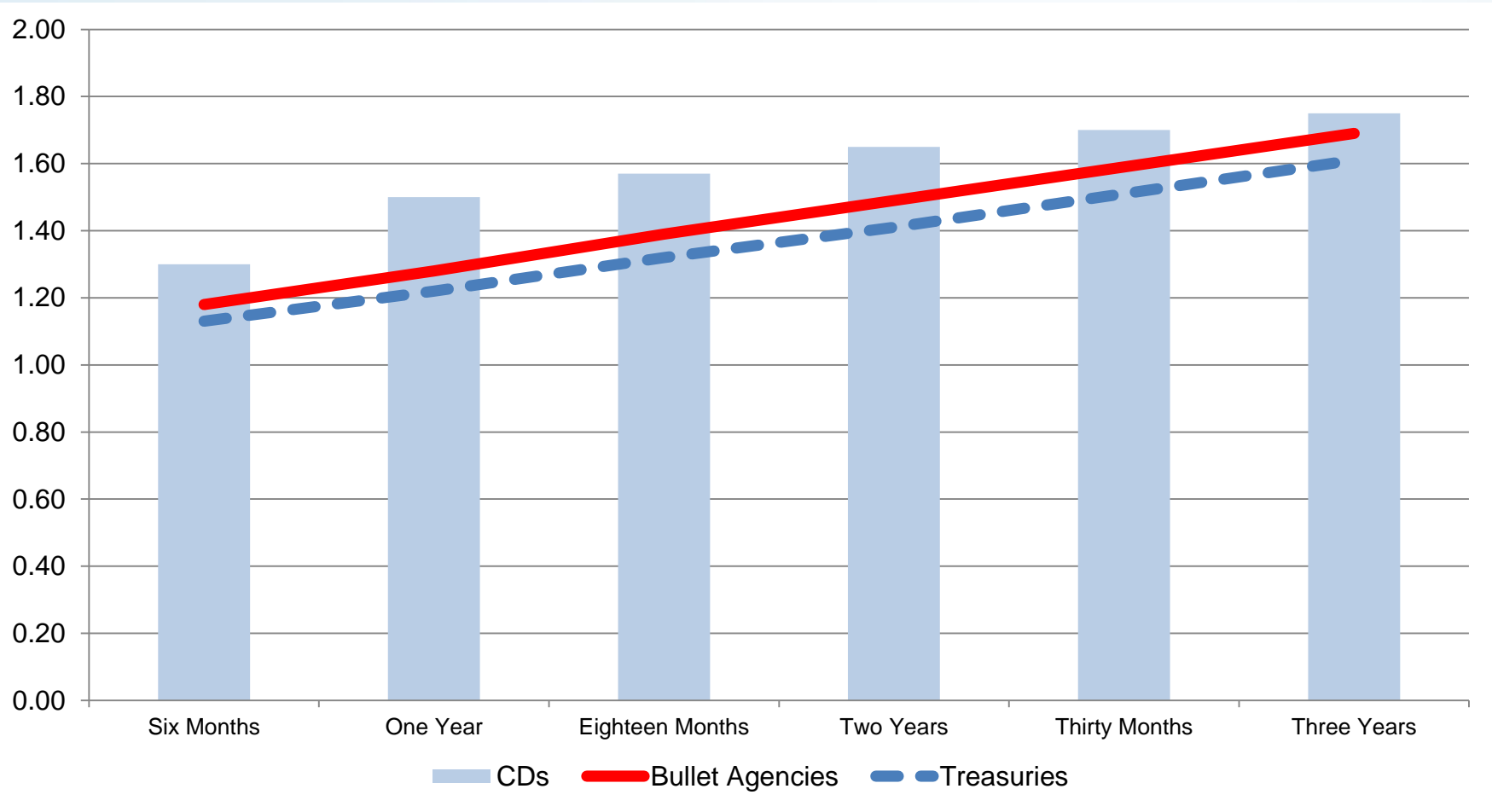


# TexPool Vs. TexPool Prime





# Current Yield Curves



# Holding Period Yield – Rising Rates

## Moderate Tightening

	\$1,000,000			CD @
Quarter	Fed Funds Target	LGIP Yields	LGIP Interest	1.70%
1	1.25%	1.10%	\$ 2,750	\$ 4,250
2	1.25%	1.10%	2,750	4,250
3	1.50%	1.35%	3,375	4,250
4	1.50%	1.35%	3,375	4,250
5	1.75%	1.60%	4,000	4,250
6	1.75%	1.60%	4,000	4,250
7	2.00%	1.85%	4,625	4,250
8	2.00%	1.85%	4,625	4,250
<b>Totals</b>			<b>\$29,500</b>	<b>\$34,000</b>

## Aggressive Tightening

	\$1,000,000			CD @
Quarter	Fed Funds Target	LGIP Yields	LGIP Interest	1.70%
1	1.25%	1.10%	\$ 2,750	\$ 4,250
2	1.25%	1.10%	2,750	4,250
3	1.50%	1.35%	3,375	4,250
4	1.75%	1.60%	4,000	4,250
5	2.00%	1.85%	4,625	4,250
6	2.25%	2.10%	5,250	4,250
7	2.50%	2.35%	5,875	4,250
8	2.75%	2.60%	6,500	4,250
<b>Totals</b>			<b>\$35,125</b>	<b>\$34,000</b>



# Interacting with the Market

- Keep Discipline/Control Process
- Analyze Risk/Return
- Maintain Competitive Environment
- Avoid “Noise”
  - Deal of the Day
  - New Structures
  - “Advertised “ Maturity
  - Delayed Settlement

**“IGNORE THE NOISE”**  
-Bill Belichick

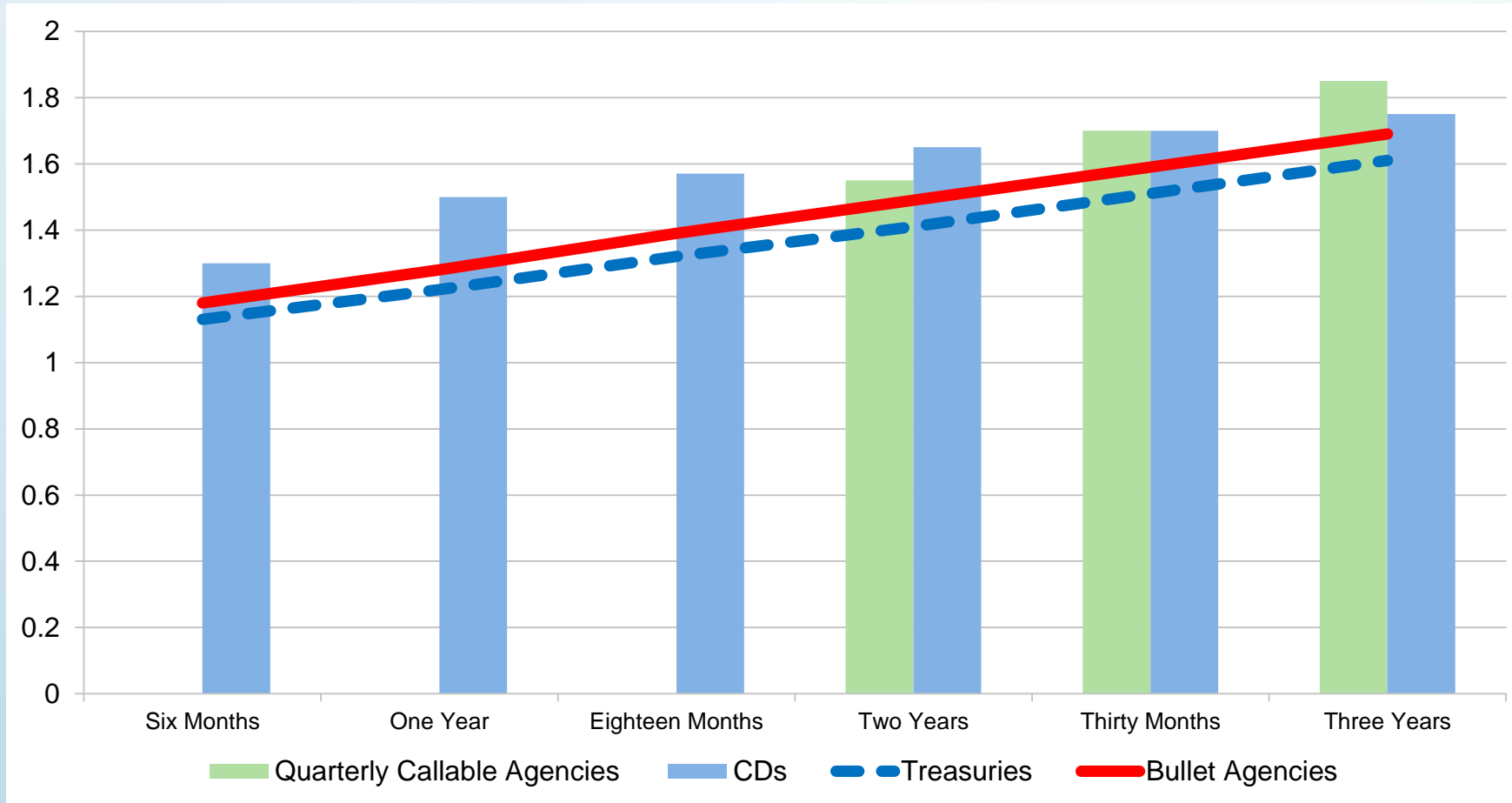
# Recap:

- Accessed Your Tools and Abilities
- Established or Reviewed the Investment Process
- Reviewed Investment Policy/Investment Strategy Documents
- Analyzed Cash Flow Needs
- Considered Appropriate Investment Options
  - Current Risk/Return Choices
- Interacting With the Market

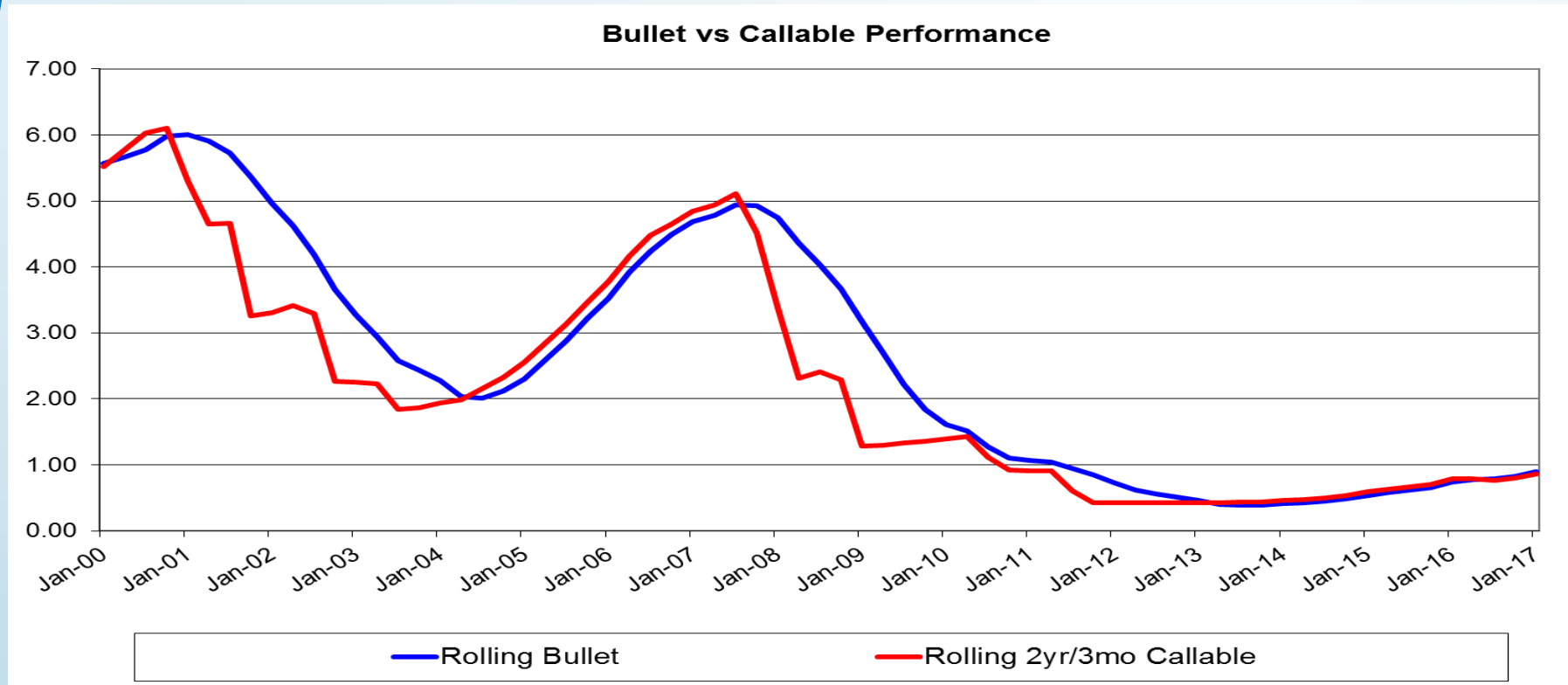
# Callables and Step-Ups

- Callables: Issuer Call Option
- Step Ups: Rising Coupon with Call Option
- Need to Project Market Movements
  - Yield To Call (YTC)
  - Yield to Maturity (YTM)
  - Yield to Worst (YTW)

# Callable Yield Curve



# Callable Advantage?



	<u>Rolling 2Yr Note</u>	<u>Rolling 2Yr Bullet</u>	<u>Rolling 2Yr/3MoCallable</u>
Ave since 1/2000	2.38	2.58	2.23



# Step-up Example

Maturity: 3 Years Callable: 6 Months

Steps:

Six Months = 1.25%

Six Months = 1.50%

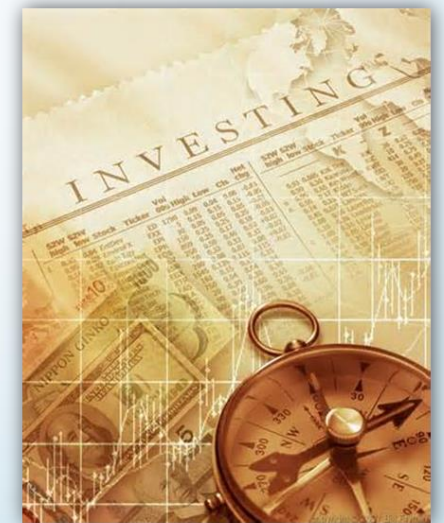
Six Months = 1.75%

Six Months = 2.00%

Six Months = 2.50%

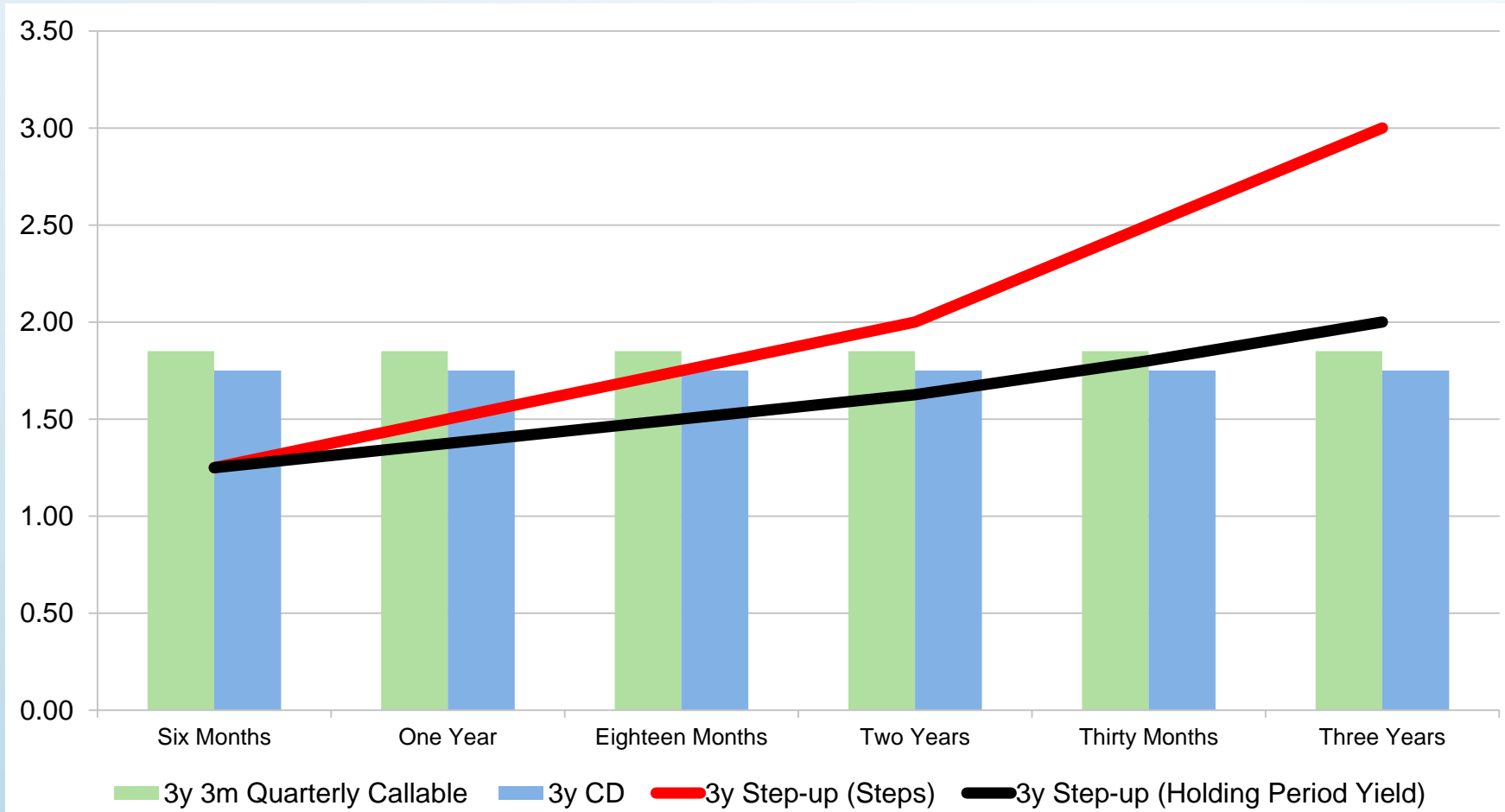
Six Months = 3.00%

Internal Rate of Return (IRR) = 2.00%



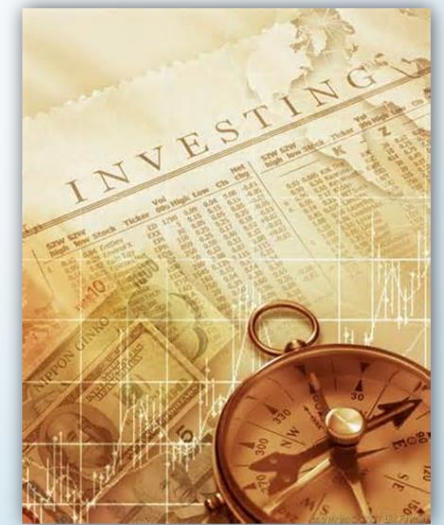


# Step Up – No Advantage Until The End



Major B/D Quote:

“Studies of step-up performance continue to show they work as advertised – **called sooner** than fixed-rate callables in stable markets”

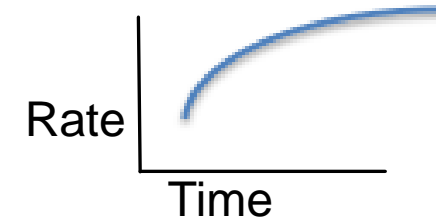


# Investment Strategy

- Yield Curves

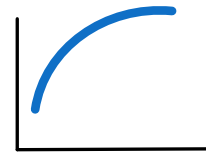
- Normal

- Implications – shape when economy is healthy



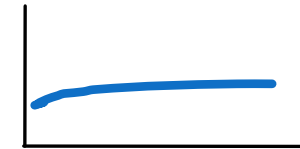
- Steep

- Implications – economy may be growing too fast (inflation concerns)



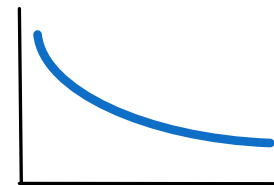
- Flat

- Future of economy is uncertain



- Inverted

- Future of economy is bleak



# Investment Strategy - Laddering

Think of it as an extension ladder:



**Rising Rates = Shorter Ladder**

**Falling Rates = Long Ladder Strategy**

# Recap:

- Accessed Your Tools and Abilities
- Established or Reviewed the Investment Process
- Reviewed Investment Policy/Investment Strategy Documents
- Analyzed Cash Flow Needs
- Considered Appropriate Investment Options
  - Current Risk/Return Choices
- Interacting With the Market
- Understanding Callables & Step-ups
- Understanding Yield Curves
- Laddering Strategy

# Documentation

- Maintain Your Files
  - Type of Investment and Document Needs
    - Securities
      - Trade Ticket
      - Safekeeping Receipt
      - Monthly Custodial Reports
    - CDs
      - Bank Agreement
      - FIRREA Documents (Board Approval Resolution, Minutes)
      - Certificate
      - Collateral Documents/Receipts/Monthly Reports

# Documentation

- Maintain Your Files
  - Type of Investment and Document Needs
    - Pools/MMMFs
      - Participation Agreement
      - Transaction Receipts
      - Monthly Reports
    - Money Market Accounts
      - Bank Agreement
      - FIRREA Documents (Board Approval Resolution, Minutes)
      - Transaction Receipts
      - Collateral Documents/Receipts/Monthly Reports

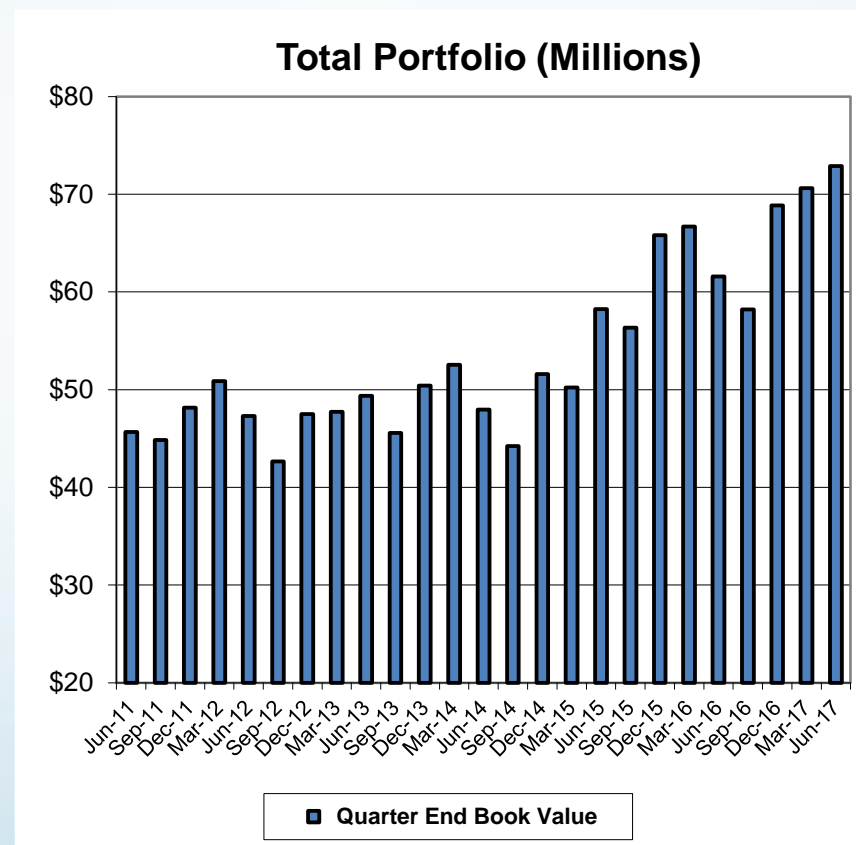
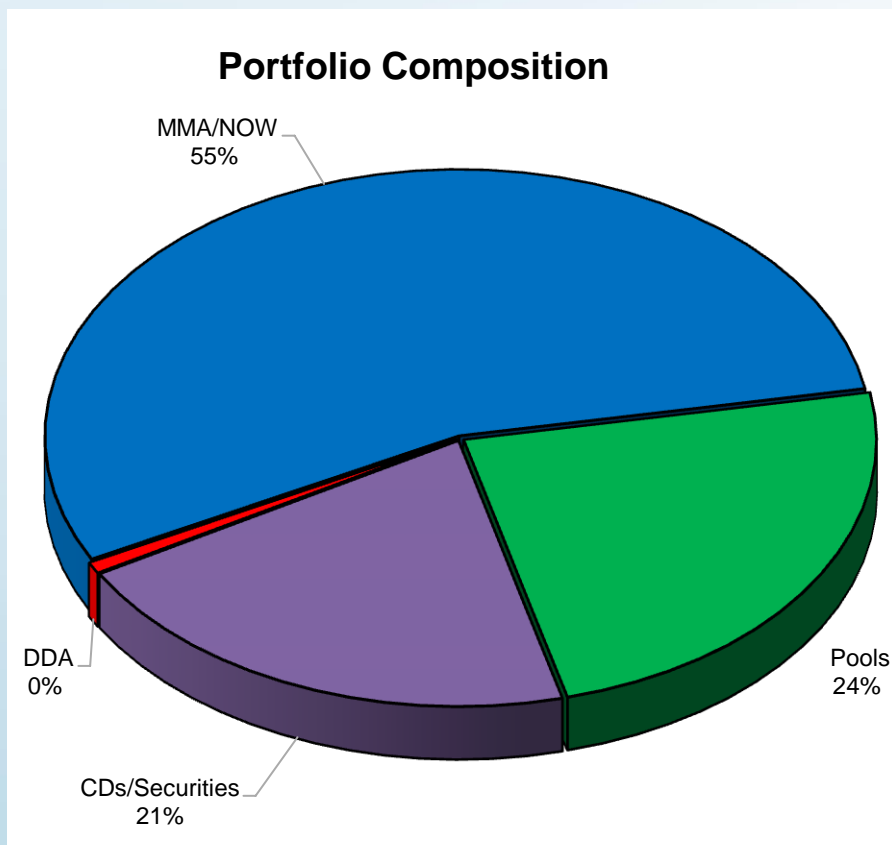
# Managing Expectations/Communicating

## Quarter End Summary

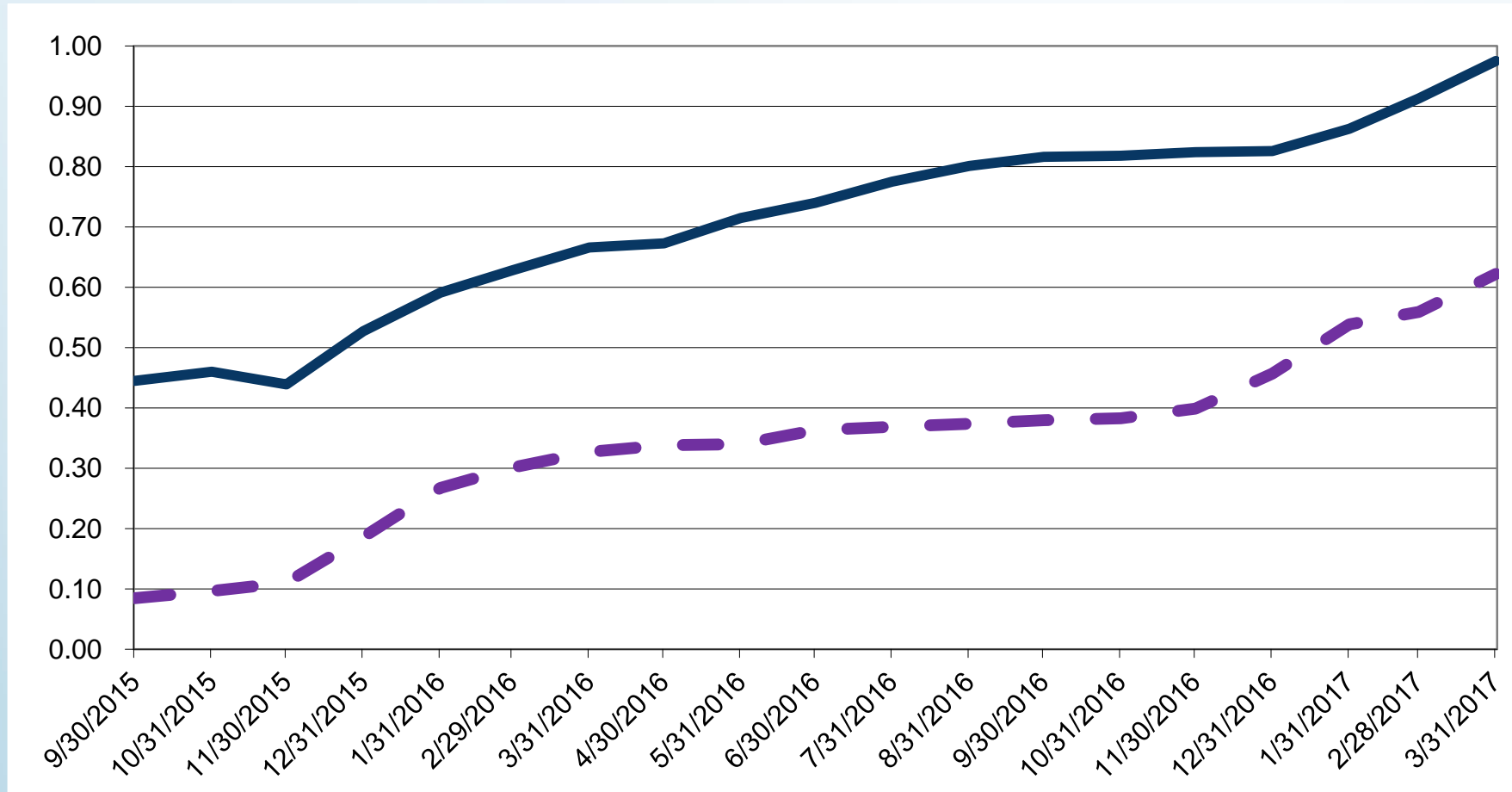
<u>Asset Type</u>	<u>Ave. Yield</u>	<u>March 31, 2017</u>		<u>June 30, 2017</u>	
		<u>Book Value</u>	<u>Market Value</u>	<u>Book Value</u>	<u>Market Value</u>
Demand Accounts	0.35%	\$16,679,952	\$16,679,952	\$ 8,568,337	\$ 8,568,337
NOW/MMA/Pools	1.25%	36,167,404	36,167,404	41,283,295	41,283,295
Certificates of Deposit	1.51%	6,231,735	6,231,735	6,174,761	6,174,761
<b>Totals</b>		<b>\$59,079,091</b>	<b>\$59,079,091</b>	<b>\$56,026,393</b>	<b>\$56,026,393</b>
Portfolio Average Yield	1.14%				



# Charts & Graphs Help



# Performance Communicates “Value”

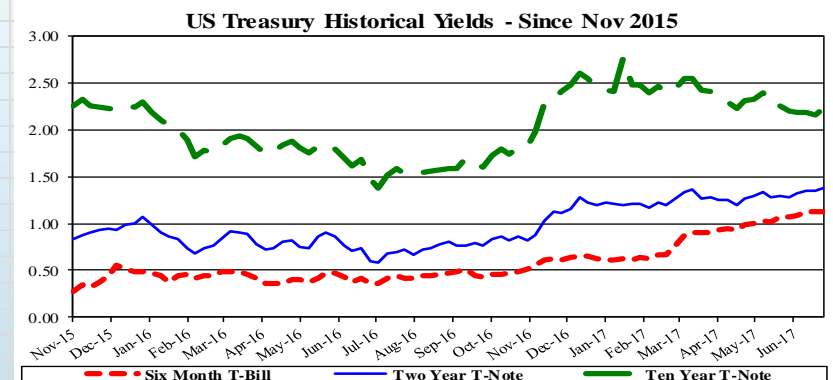
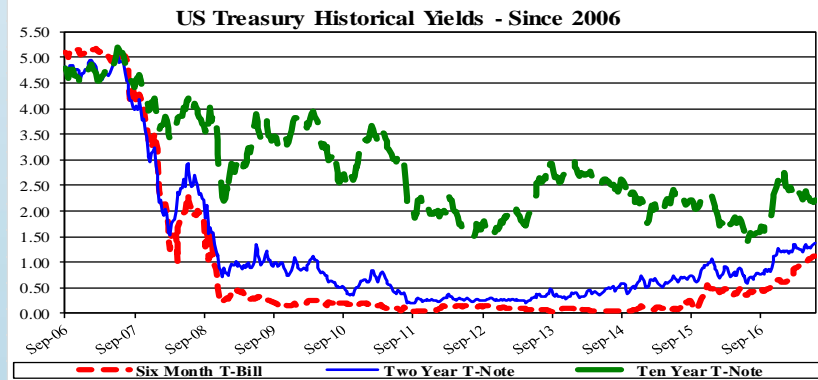
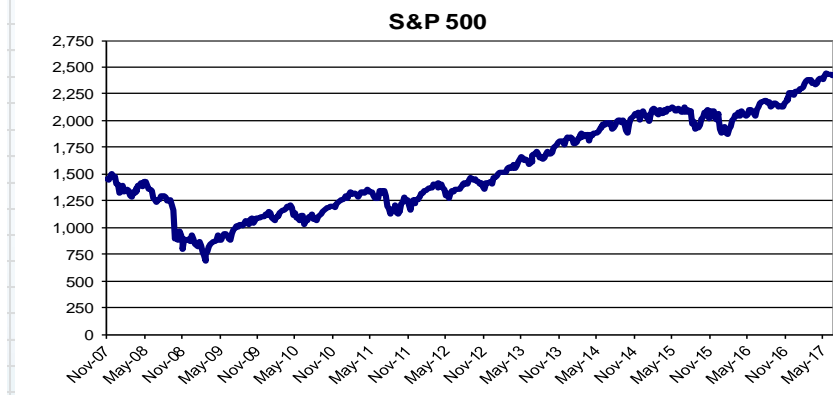
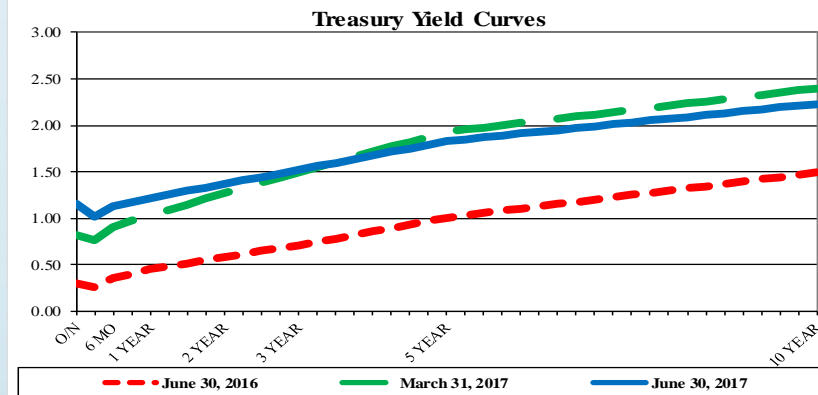


# Include Some Economic Data

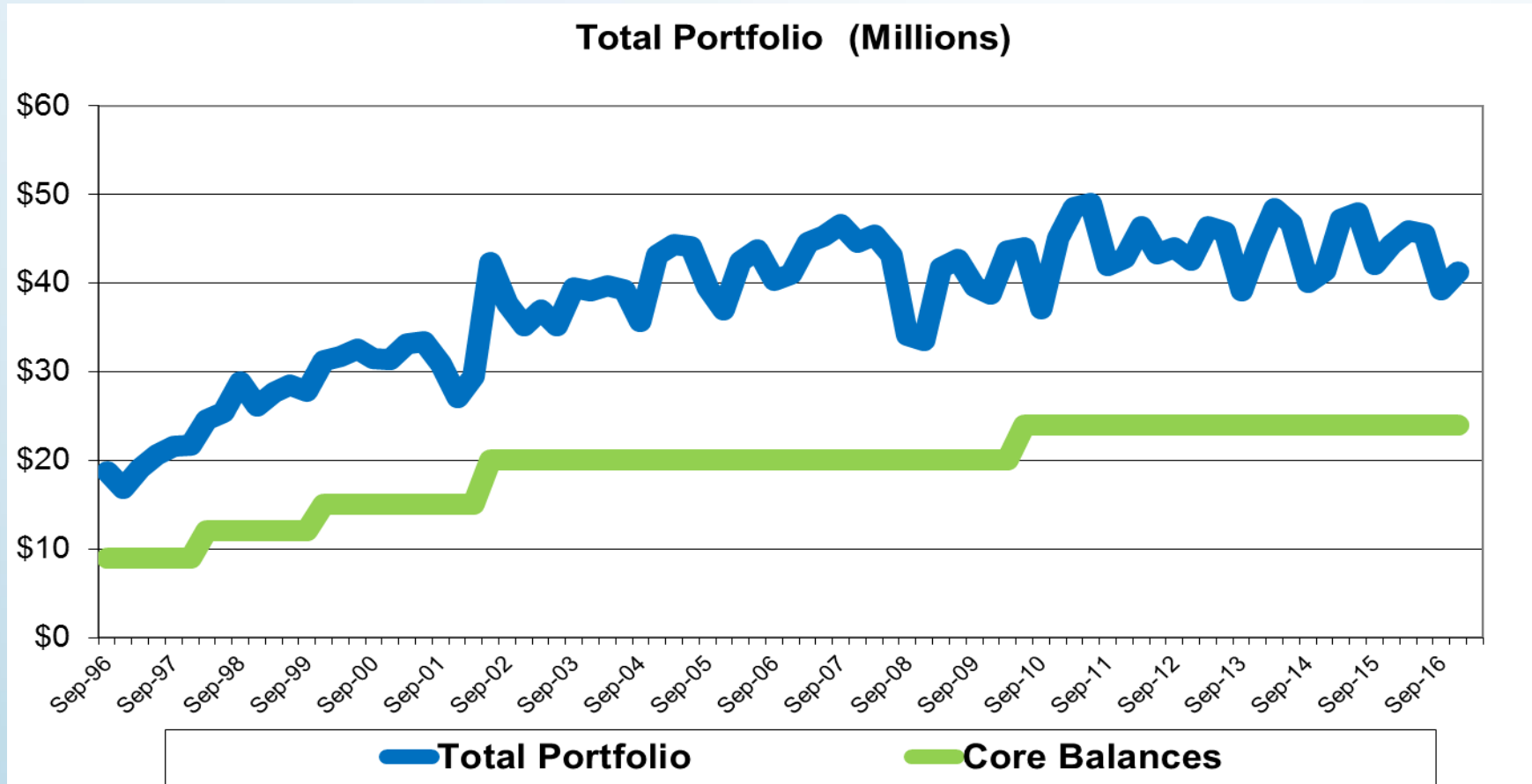
## Economic Overview

6/30/2017

The Federal Open Market Committee (FOMC) raised the Fed Funds target range to 1.00% - 1.25% (Effective Fed Funds are trading +/-1.16%) at the June FOMC meeting. The market is not confident additional increases will occur during 2017. The Fed anticipates gradually reducing its government bond holdings. Third revision 1st Quarter 2017 GDP was a increased to 1.4%. June Non-Farm Payroll increased 222k, with +47k adjustment to Apr/May. Other US data remained volatile with some negative numbers. The Stock Markets remain high. Monitoring estimated balances and needs will determine laddering opportunities.



# Investment Strategy Enhancements



Questions?





**Susan K. Anderson**

(830) 637-7755

[skanderson@valleyviewconsultingllc.com](mailto:skanderson@valleyviewconsultingllc.com)