

CPIM

CENTER FOR PUBLIC INVESTMENT MANAGEMENT



A PROGRAM BROUGHT TO YOU BY:

ROBERT SPRAGUE

OHIO TREASURER

INV 106:

Basics of Investing

Presenter

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Agenda

- Developing an Investment Policy
- Permissible Investments
- Yield Measures
- Safekeeping of Investment Securities
- Ohio Pooled Collateral System
- Cash vs Core

DEVELOPING AN INVESTMENT POLICY

What is an Investment Policy?

- An Investment Policy (IP) is an entity's plan for investment-related decision making.
- An IP should consider the laws, rules, guidelines and regulations applicable to the accounts, funds, plans or programs that are managed.
- An IP should summarize the principles, goals and strategies for the investment program.

Investment Policy

Requirements

- Create, adopt and file with Auditor of State
- Sent to investments@ohioauditor.gov
- Not required if annual average portfolio of investments is \$100,000 or less
- Service providers sign-off

Best Practice

- Review annually
 - Stay current with changes in Ohio law

PERMISSIBLE INVESTMENTS

Current Ohio Investment Laws

- ORC 135.14: Schools, Townships, Cities, etc.
- ORC 135.35: Mainly Counties or other agencies
- Charter City: May not follow state guidelines

Treasury Securities

- Full faith and credit of the U.S. government
- Very liquid type of security
- Purchase directly from U.S. Treasury or through a broker/dealer

Government Securities

- Full faith and credit or implied backing by U.S. government
- Customized structures – call types and steps
- Things to Consider
 - Compare bond with other dealers
 - Know the difference between the yield and coupon rate!

Bank Deposits

- Savings and money market savings accounts
- CDs
- Know the requirements for protection
 - FDIC insurance
 - Collateral

Certificates of Deposit

135.144 Investment of interim moneys in federally insured certificates of deposit.

(A) In addition to the authority provided in section 135.14 or 135.143 of the Revised Code, the treasurer of state or the treasurer or governing board of a political subdivision may invest interim moneys in certificates of deposit in accordance with all of the following:

(1) The interim moneys initially are deposited with an eligible public depository described in section 135.03 of the Revised Code and selected, pursuant to section 135.12 of the Revised Code, by the treasurer of state or the treasurer or governing board of a political subdivision, for interim moneys of the state or of the political subdivision.

(2) For the treasurer of state or the treasurer or governing board of the political subdivision depositing the interim moneys pursuant to division (A)(1) of this section, the eligible public depository selected pursuant to that division invests the interim moneys in certificates of deposit of one or more federally insured banks, savings banks, or savings and loan associations, wherever located. The full amount of principal and any accrued interest of each certificate of deposit invested in pursuant to division (A)(2) of this section shall be insured by federal deposit insurance.

(3) For the treasurer of state or the treasurer or governing board of the political subdivision depositing the interim moneys pursuant to division (A)(1) of this section, the eligible public depository selected pursuant to that division acts as custodian of the certificates of deposit described in division (A)(2) of this section.

(4) On the same date the public moneys are redeposited by the public depository, the public depository may, in its sole discretion, choose whether to receive deposits, in any amount, from other banks, savings banks, or savings and loan associations.

(5) The public depository provides to the treasurer of state or the treasurer or governing board of a political subdivision a monthly account statement that includes the amount of its funds deposited and held at each bank, savings bank, or savings and loan association for which the public depository acts as a custodian pursuant to this section.

(B) Interim moneys deposited or invested in accordance with division (A) of this section are not subject to any pledging requirements described in section 135.18 or 135.181 of the Revised Code.

Amended by 129th General Assembly File No. 67, HB 209, §1, eff. 3/22/2012.

Effective Date: 07-04-2006

Certificates of Deposit

2014 Ohio Compliance Supplement

Indirect Laws & Statutorily Mandated Tests

- Any CD's purchased by a broker must be held in the name of the government. Also, the broker cannot be in possession of cash at any time. If we believe a broker has held cash for any length of time, AOS auditors should refer the matter to the Center for Audit Excellence and AOS Legal division for further evaluation. A way to verify compliance is to request monthly statements provided by the public depository located in Ohio. Ohio Rev. Code §135.144(A)(5) requires the initial public depository to provide public offices with a monthly account statement that includes the amount of its funds deposited and held at each bank, savings bank, or savings and loan association for which the public depository acts as a custodian pursuant to Ohio Rev. Code §135.144. If a public office does not have these statements, it may indicate that the money is being held by a broker-dealer in violation of Ohio Rev. Code §135.144.

Commercial Paper

- Need additional training approved by TOS
- Max of 40%
- Max maturity restriction of 270 days
- Highest rating category from two rating agencies (Moody's, S&P, Fitch)
- Maximum of 5% of total portfolio in any issuer at time of purchase

Corporate Securities

- ORC 135.35 permits up to 15% of interim funds in corporate securities
- Must be rated A or better and have a three year maximum maturity
- Know what you are buying and the risk associated
 - Credit risk
 - Liquidity risk

Municipal Securities

- Permits entities to purchase general obligations of the State or political subdivisions of the State (20% max under ORC 135.14)
- Must be rated in three highest categories (ORC 135.14)
- Cannot be the sole owner of an entire issue (ORC 135.14)
- Must complete training with TOS (ORC 135.14)

Repurchase Agreements

- Term loan with collateral in the form of securities
- Master Repurchase Agreement outlines procedures
- Reverse repo enables investment officer to leverage the portfolio – **PROHIBITED**

Bankers Acceptances

- Need additional training approved by TOS
- Max of 40% portfolio allocation
- Maturity restriction of 180 days

STAR Ohio

- AAAm rated by Standard and Poor's (highest)
- Similar to money market fund
- Daily interest income
- Daily liquidity (within guidelines)
- State administered



STAR Plus

- All deposits are demand deposits and are 100% FDIC-insured
- Up to \$50 million in deposits per legal entity
- Next day liquidity
- Daily transparency with 24/7 online access to account information



INVESTMENT MARKETS

Primary aka New Issue

- Auction
- Negotiated
- Issued at par

Secondary

- Owned by prior investor
 - Accrued interest may be a factor
- Price based on market rates
 - Par, premium or discount

STRUCTURES

Maturity

- Bullet
- Callable
 - Issuer redeems at par based on call frequency
 - Continuous, monthly, quarterly, one-time
 - May be a partial call

Coupon

- Fixed
- Floating
- Step-up

ROLE OF INVESTMENT PROVIDERS

RISKS OF INVESTING

- **Market Risk →**
 - Decline in market value
- **Credit Risk →**
 - Securities, dealers, banks, CDs
- **Liquidity Risk →**
 - Ability to sell
- **Reinvestment Rate Risk →**
 - Reinvesting maturities in lower interest rates
- **Political Risk →**
 - Risk to your career

Who Will Help You Invest?

Know the Types of Service Providers

<i>STAR Ohio/Plus</i>	<i>Banks</i>	<i>Investment Advisors</i>	<i>Brokers</i>
<ul style="list-style-type: none">• STAR Ohio<ul style="list-style-type: none">• Know the investments of STAR Ohio• Look over the annual report• STAR Plus<ul style="list-style-type: none">• Understand how program works• Monitor deposit Banks	<ul style="list-style-type: none">• Make sure they understand nuances of public entities• Work with banks you know and trust	<ul style="list-style-type: none">• Acts as a fiduciary in the client's best interest• Who do they work with?• What are their credentials?• Check them out: www.investor.gov	<ul style="list-style-type: none">• Recommends suitable investments• Who do they work with?• What do they do and how much do they charge?• Check them out: www.finra.org

Perform the Due Diligence Before Investing

External Managers – Advisor

- Provides investment advice
- Fiduciary responsibility
- May or may not have direct control (discretionary vs. non-discretionary)
- Executes purchases/sales
- Manages or provides advice on overall portfolio
- May coordinate safekeeping (3rd party custodian)

Definition of “Fiduciary” - fi·du·cia·ry - noun

- In law, a person in a position of authority whom the law obligates to act solely on behalf of the person he or she represents and in good faith.

Source: Merriam-Webster

External Managers – Broker/Dealer

- Provides investment advice
- No fiduciary responsibility
- Does not have direct control
- Acts as a broker when executing orders on behalf of clients
- Acts as a dealer when trading from its own account
- May provide safekeeping

Benefits of Using External Managers

- Professional manager – that is their business
- Greater access to investment markets/information
- Broker network – potentially more sources to receive best price execution of trades
- Enhanced credit research available for unsecured investments (i.e., commercial paper)
- Can complement internal resources or personnel
- Could increase internal control and “separation of duties”
- Be careful and know what role the provider is playing

YIELD MEASURES

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Coupon Rate

Annual interest payment to be received

Current Yield

Yield based on market price and coupon rate

Yield at Cost or Yield to Maturity

Yield based on purchase price and coupon rate

Total Return

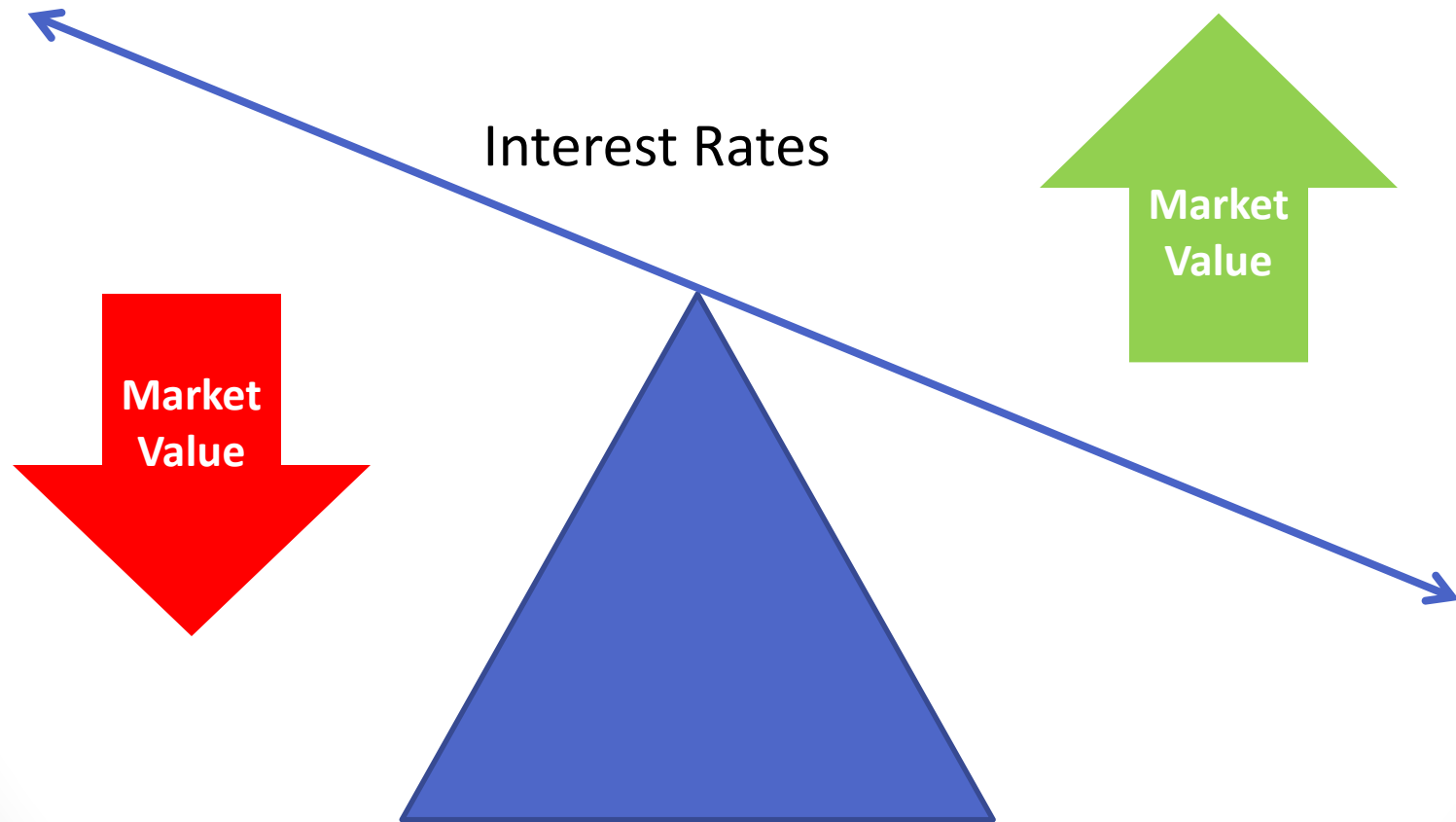
Return based on purchase price, coupon rate and unrealized gains or losses

YIELD MEASURE EXAMPLES

	US Treasury Note	FDIC Insured CD	US Government Agency	Commercial Paper
Issuer	US Treasury	Morgan Stanley Bank	FHLB	JP Morgan Securities
Par Value	\$247,000	\$247,000	\$247,000	\$247,000
Maturity Date	2/29/20	3/6/20	3/30/20	11/22/19
Coupon Rate	1.375%	2.50%	2.375%	n/a
Purchase Price	\$244,163	\$247,000	\$246,487	\$242,182
Yield at Cost	2.55%	2.50%	2.57%	2.68%
Market Value (3/31/19)	\$244,723	\$247,101	\$246,919	n/a
Current Yield	1.39%	2.46%	2.38%	n/a

For illustration purposes only.

INVERSE RELATIONSHIP



SAFEKEEPING OF INVESTMENT SECURITIES

SAFEKEEPING OPTIONS

- **Safekeeping provided by broker or bank acting as a broker**
 - Securities held in brokerage account
 - Broker controls account
 - Securities not held in public entity's name
 - Safekeeping cost bundled with other services
- **Third party custodian**
 - Securities held in public entity's account at bank trust department
 - Public entity controls account
 - Securities held in public entity's name
 - Written custodial agreement
 - GFOA best practice

Ohio Pooled Collateral System

Ohio Pooled Collateral System

Ohio Revised Code 135.182

- House Bill 64, House Bill 340 and House Bill 374
- Effective July 1, 2017
- Lien perfection required
- Bank must select one method of collateralization for all public depositors
- Ohio Pooled Collateral System (OPCS)
 - Treasurer of State sole regulator and monitor of program
 - Market value of collateral equal to or greater than
 - 102% of uninsured public deposits , or
 - Amount determined by rules adopted by Treasurer of State
 - Website access for reporting of collateral to public depositor

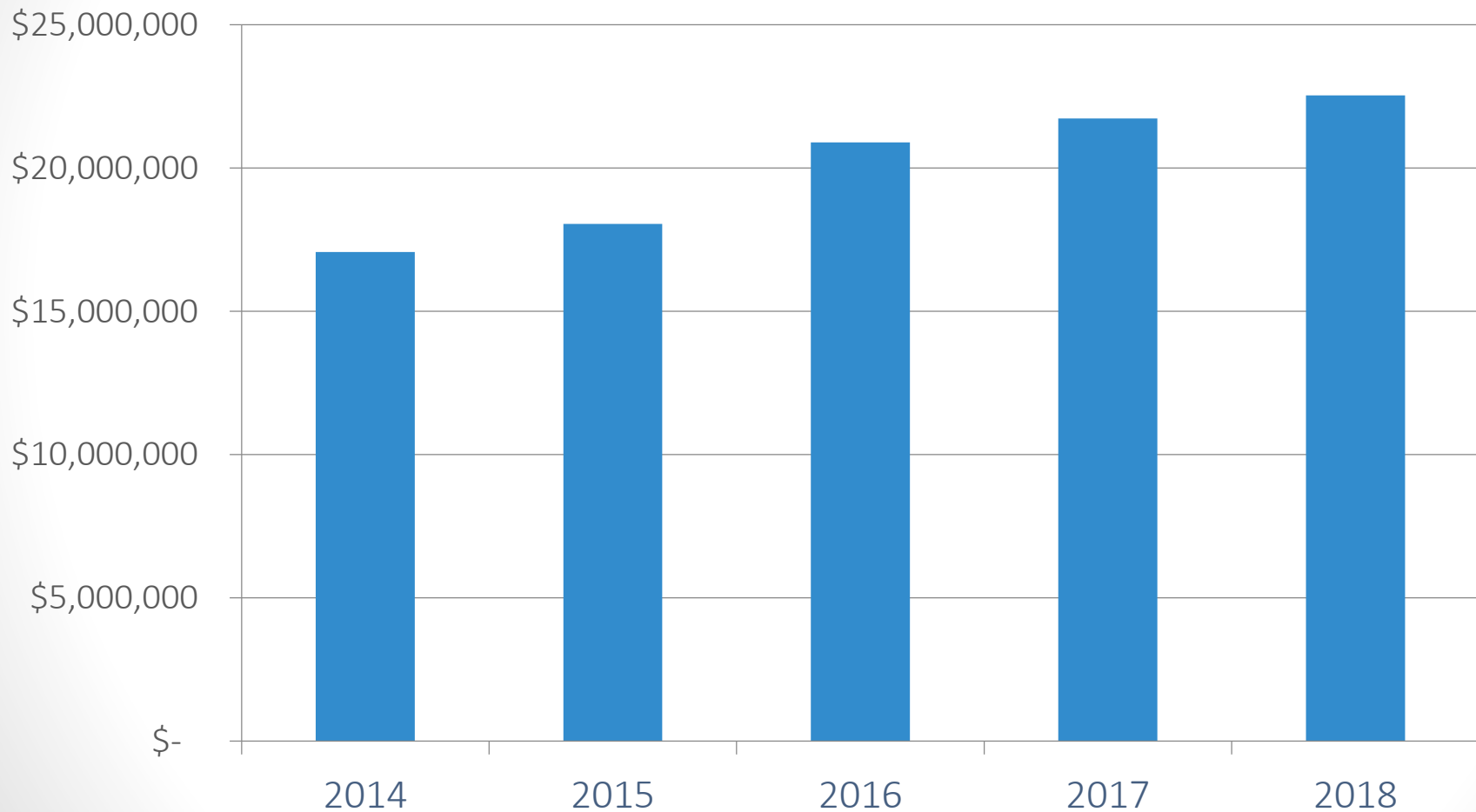
CASH VS CORE

CASH VS CORE

- **Cash Management - “Cash” Portfolio**
 - Operating needs for current year
 - Funds with uncertain time horizon
- **Investment Management – “Core” Portfolio**
 - Time horizon greater than one year
 - Apply investment strategy to maximize earnings

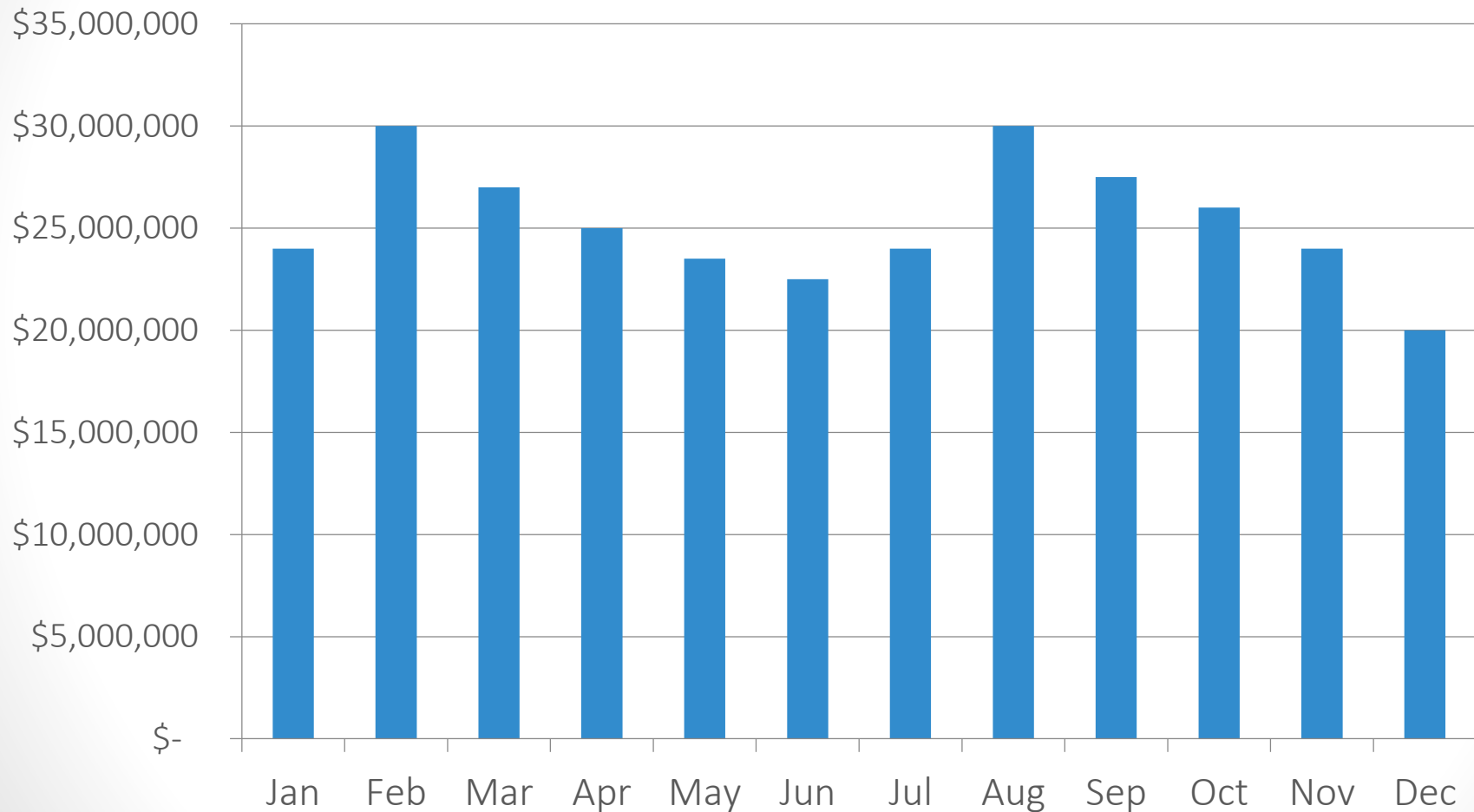
CASH VS CORE

Year-end Balances



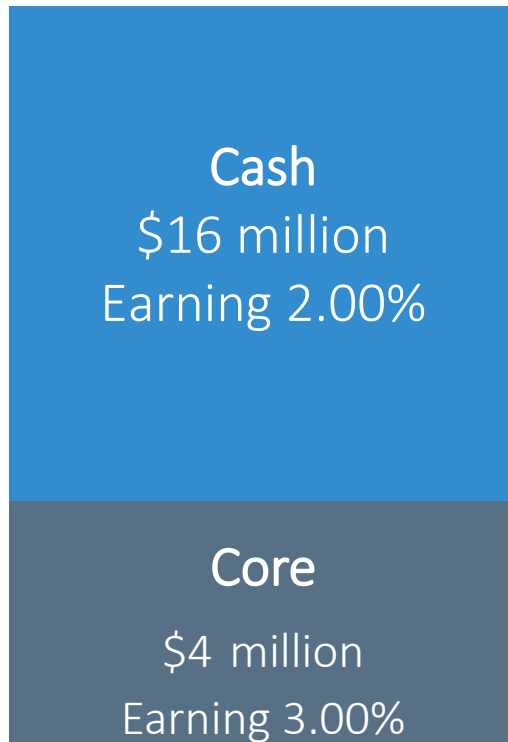
CASH VS CORE

Month-end Balances



CASH VS CORE

Current



Right-Sized



Projected Additional Interest Income of \$80,000

Summary

- Ask questions
- Know the details
- Protect yourself – follow the law
- Seek help when appropriate

ULTIMATELY IT IS YOUR RESPONSIBILITY!

MyCPIM Password