# CLARK COUNTY FINANCE COMMITTEE
## Second Quarter 2019

Alishia Topper, Chair
Greg Kimsey, Secretary
Eileen Quiring, Councilor Chair

# MINUTES

The meeting was called to order on August 27, 2019 by Treasurer Alishia Topper at 10:00am in room 243 of the Clark County Public Service Center at 1300 Franklin Street, Vancouver, WA 98660. The finance committee members present were Alishia Topper and Greg Kimsey. Also present were Sara Lowe, Rachel Wilson, Amira Ajami, Nick Bundy, and Nicole Antonacci, with Deanne Woodring attending via phone.

**Call to Order & Introductions**

Treasurer Topper began by inviting introductions. Chair Quiring was unable to attend the meeting.

**Investment Pool Report**

Investment Officer Wilson

**Market Summary:** The stock market performed well in the second quarter. Interest rates have continued to decline since November. The 3-month to 10-year yield curve inverted further. At the end of June, the market priced in a 100% probability of a rate cut at the end of July, which happened. An additional 75 basis points in cuts is predicted in the next 12 months. That's all priced in to the yield curve. The strategy is to maintain discipline and keep the portfolio laddered and to diversify.

**Economic Summary:** All the fundamentals were very strong in second quarter. What the bond market is saying with yields decreasing is that a recession is impending. The stock market rise does not suggest a recession. Average of $156 thousand in payrolls year-to-date, which is lower than last year's average, but that is to be expected with the low unemployment rate. Average hourly earnings remained at 2.3%, that is a little bit higher than it was before. Inflation has been subdued at 1.8% which is less than wages, which means that the real purchasing power of the consumer has increased. We've seen that purchasing power in the consumer consumption numbers. The second quarter GDP came in at 2.1%, which beat expectations thanks to consumer consumption of 4.3%. The areas of weakness remain in business fixed investment and exports, which are likely tied to the trade uncertainly. In addition to the on-going trade war, other top risk factors include: weakness in the global market (Germany just posted its first negative GDP report), our diminishing supply of labor, and a large federal deficit.

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**County Pool:** As far as our pool, we remained at around $840 million, 20% of which was invested in the state pool. We hit $1.1 billion at tax time, then the money was spent down due to construction spending. The second quarter average yield was 2.51, which was the same as the state pool's yield average. The 12-month rolling average market return, which includes the change in market price, which has been going up, we've got some huge gains in our portfolio right now due to declining interest rates. That was 3.06% and the benchmark was 2.91%. Duration was 0.76 years and the benchmark at the time was 0.8. Going forward, we are going to use the new benchmark's duration of 0.95. The NAV was $1.004480, which is within the bandwidth.

**Quarterly Activity:** We made our first purchase in corporate bonds in Apple and Microsoft. Apple was 50 basis points over Treasury yield and essentially rated the same across the board. We purchased $10 million in municipal bonds, which are hard to find, and $117 million in callables. A lot of the callables have a lock-out of one year or two years, but in a declining rate environment, those will be called so we manage the portfolio to these expected call dates. We had one maturity in commercial paper that matured in July, $9 million in supranationals, some in agencies and treasuries, we had some called investments and $50 million in sales.

<u>**Government Portfolio Advisors Report, Market Update**</u>

GPA President Woodring

We continue to operate in a volatile market environment that is helping the portfolio but making it challenging for how we're investing. The tactics that were implemented since the beginning of the year have been adding longer maturities into the portfolio and have provided a lockdown of rates. We will definitely see that drift down as expected, as Wilson is reinvesting into the lower rate environment. Our focus to separate the portfolio is going to help. The volatility makes it really challenging to ensure that liquidity is solid and ensure that the investment components are managed to the right levels. The chart shows the rate rise we had in December. The Fed has been telling us since March that the rates will be going lower. The market is pricing in two more rate drops, it is a probability that the numbers will go back down to 1%. This is driven by what's happening globally at the tariff level. When we look at global rates across the world, most rates are actually negative. We need to be positioned to that and manage with discipline. We've had a great benefit from rising rates, but now we need to expect those rates to go down and continue to manage in

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the portfolio. In terms of the inversion, we have two things to be aware of as we're buying. As we're going into the corporate market, it's important to stay in the higher-quality corporate names, which Wilson is doing, because the probability of spreads widening is greater and it will widen more in the single-A space. Also, starting to keep a little shorter on those corporate notes because the longer maturities will widen more. So in a recessionary period we'll see some gap out and we should manage to that and expect that to happen. The other would be for a continued decline in the front end of rates. The 10-year has already priced in that drop. Normally the spread between 2- and 10- is more like +25 to +30, so either the 10-year goes up or the front end comes down. Given what's happening with the Fed, the probability is that those rates are going to come down. The management of the core and the liquidity is the best strategy.

The Fed cut is still a concern. There will continually be debate on whether the Fed does 2 or 3 cuts going forward and it will depend on the economic numbers. The economy is doing OK, jobs are picking up, but all trends based on what the market is telling us is that we'll be seeing lower rates. For the strategy, it's recommended moving the effective duration of the whole portfolio out closer to 1-year from today's 0.76.

The compliance report on the callable sector is at 30%, it was reviewed and determined the pool balance was higher at the time of purchase, and callables were within the policy limit of 25%. Wilson is holding off on buying more callables. Some of them are being called, it's an active market. The balance of the pool creates percentage fluctuations that we have to watch as balances flow up and down. Now balances are back up a little bit because of the increase in school district bond revenue. On the maximum weighted maturity, we are right up against that edge so we will need to keep an eye on those longer maturities. The policies and the compliance report are there to maintain and guide the investment strategy.

**Debt Report**

Deputy Treasurer Lowe presented the debt report through June 30, 2019. Clark County's debt is holding steady at $95 million; all other district debt is approximately $861,610,000, for a total of $956.6 million. There are no significant changes through this second quarter report, but there was some debt issued by Vancouver School District that was significant in size, and there are some additional upcoming issuances that are going to be quite large, which will add to the county's debt portfolio and correspondingly add to the investment pool. There are some impacts related to those large debt issuances. With respect to our bond rating, nothing has changed. Our last rating was in May of 2018, which is when we did the conservation futures bond issuance, so we are at Aa-1.

There's not a lot to talk about with respect to debt capacity, nothing has changed since last quarter's report. We still have a significant amount of debt capacity available. With respect to the line of credit, we have a low balance. Facilities was able to completely pay off what they were owing, which is positive because they had been on the line of credit for almost a year. We do have a policy marker with respect to being on the line of credit for more than a year. If that is going to be the case, we usually have to take that to council and there has to be a decision made to put them on an external line of credit. That's a pretty costly process, so we do try to encourage county departments and funds that are allowed to go on the line of credit to really make those payoffs so they don't have to deal with those other factors. Facilities is chronically under-funded, so this is an issue that will persist, unless the council makes a decision to either reduce expenses or to fully fund operations for Facilities. This is something we'll continue to watch. They did enroll right back on, I think they've been off now for several weeks so that's a good thing. They did a bunch of transfers and actually pre-funded some of these, so they sent them extra money to keep the operations afloat. In the spring supplemental they were awarded some additional funding, which should get them to the end of the year. In 2020 there will be decision packages for council consideration and they'll have to make determinations from a priority perspective. This is an audit issue, so it is something that will continue to be watched because Facilities needs additional general fund.

In terms of what's upcoming and the outlook for debt and finance: Evergreen School District is in the midst of a $200 million bond issuance. This is part of the $600 million that was passed by voters two years ago. This is the second in the series, so they've already issued a very significant block of debt. They should have a third and potentially a fourth issuance depending on the sizing of those future bond issuances. This will add to our pool in October, which is also when we're receiving tax proceeds. That combined will put us back over $1 billion. Camas has a small bond issuance at $5.2 million, for the purchase of some properties. The next issuance related to the county is the Public Facilities District sales tax rebate extension. The PFD is under discussion about whether to extend the current debt issuance on the exhibition hall or bringing on some new debt. It allows us to continue getting the sales tax credit rebate from the state. This is money that the county has access to from the state if they choose to do one of those two options.

An update on LIBOR: As a reminder, LIBOR is the benchmark interest rate the county uses for the line of credit. We are monitoring to see what the market determines as a replacement and will adopt the replacement rate. We list the jail and 179th on here, there's no direct action that needs to be taken immediately, those are also on a watch list.

One thing to note is the new and upcoming debt that was issued by Vancouver School District. That closed in third quarter, so it does not show on this quarterly report. When Topper was reviewing the investment policy, she found a nuanced line in the policy regarding if a district's holdings are over 25%, then an investment needs to be made outside of the pool to mitigate risk. When this $152 million was issued by the Vancouver School District and we received the proceeds that pushed their holdings over that percentage threshold. A purchase was made outside of the pool. It's very short term, because once we get those tax proceeds in and some of these other district bond proceeds that's going to change the proration of holdings by district participants.

Topper said that Wilson did a $40 million placement for 45 days. That should provide enough time to get October tax revenue in and push the Vancouver School District's holdings down.

Kimsey asked for clarification on the policy.

Topper discussed with Woodring regarding the risk and why the policy would cap it at 25%. Woodring said it is standard within pools to not allow entities that could pull out their money to control too much of the assets. It's a protective measure, as an entity that could withdraw from the pool would have a potentially large influence over the yield and performance of the pool. The school districts can't, since they are required to leave their money with us. The wording in the policy may need to be revised to account for this. With pools, you don't want to have the vulnerability of participants being able to pull out at an untimely time in the portfolio.

Topper stated that the wording was explicit in the financial statement. It may not have been as explicit in the policy. The risk will need to be considered and the policy would need to differentiate between voluntary and statutory participants for additional clarity.

Lowe noted that Evergreen's bond proceeds will be something to watch in relation to this policy. We also need to be keenly aware of when we make our large debt payments in December. The county's percentage will drop significantly in terms of their tax proceeds what they get in, so we will have to be monitoring.

Lastly, Facilities has a large share on this line of credit breakdown. Not only have there been concerns about how long they've been on the line, but also almost 50% of the line is being taken by Facilities, sometimes for large portions of the year. The line of credit is meant to be short-term, temporary and not more than 50%. We will be supporters of them trying to find a more permanent solution to the funding issues.

**Good of the Order & Adjournment**

Topper would like to go forward with approving minutes from the previous meeting. Kimsey made a motion to add the minutes to the agenda. Topper seconded the motion and the motion was carried. Kimsey made a motion to approve the minutes. Topper seconded the motion and the motion was carried.

With no other items for the good of the order, Topper adjourned the meeting at 10:30am.

Prepared by: ______________________
Nicole Antonacci

Submitted by: ______________________
Greg Kimsey