

TEXPOOL INVESTMENT ADVISORY BOARD MEETING
Monday, August 20, 2018
Minutes

The TexPool Investment Advisory Board (the “Board”) met at 10:00 a.m. on Monday, August 20, 2018, at the LBJ State Office Building, 111 E. 17th Street, Room 114, Austin, Texas.

Board Members Present

Jerry Dale, Patrick Krishock, David Landeros, Sharon Mathews, Michele Tuttle, Belinda Weaver, and Vivian Wood.

Board Members Absent

Jose Elizondo, Jr.

Comptroller of Public Accounts Staff Present

Comptroller Glenn Hegar; Mike Reissig, Deputy Comptroller; Phillip Ashley, Associate Deputy Comptroller; and Cheryl Scott, Internal Auditor.

Texas Treasury Safekeeping Trust Company (“Trust Company”) Staff Present

Paul Ballard, CEO/CIO; Danny Sachnowitz, Deputy CIO; Marianne Dwight, General Counsel; Frank Zahn, Chief Financial Officer; Spencer Brown, Compliance Officer; Hugh Ohn, Director of Accounting Strategy and Planning; Eduardo Torres, Portfolio Manager; and Nora Arredondo, Program Specialist.

Additional Participants

Deborah Cunningham and Amy Michaliszyn, Federated Advisory Companies; Ed Sanchez and Jerry Landrum, Federated Securities Corporation.

Call to Order

Comptroller Hegar declared that a quorum was present and called the meeting to order at 10:06 a.m.

Approval of Minutes (Tab 1)

A motion was made by Mr. Patrick Krishock to accept and approve the minutes from the May 16, 2018 board meeting. The motion was seconded by Mr. Jerry Dale and unanimously approved by the Board.

Annual Review of TexPool and TexPool Prime Investment Policies (Tab 2)

Mr. Paul Ballard reviewed the recommended revisions to the TexPool and TexPool Prime Investment Policies behind Tab 2. He explained that the recommended revisions were non-substantive but will better align the policies with the revisions to the Public Funds Investment Act made by the legislature. A summary of the recommended changes are as follows: at the end of each business day, cash is primarily swept into repurchase agreements and/or an eligible money market fund; the Federal Home Loan Bank notes are categorized as government securities; and money market mutual funds must now also comply with Rule 2a-7 as promulgated under the Investment Company Act of 1940. Also under the TexPool Prime Investment Policy, certificates of deposit may now be secured in accordance with

Chapter 2257 of the Texas Government Code or in any manner and amount provided by other law for deposits of the investing entity.

A motion was made by Ms. Vivian Wood to recommend the proposed revisions to the Comptroller as presented by the Trust Company. The motion was seconded by Ms. Michele Tuttle and unanimous approved by the Board.

Economic Update and Discussion of Portfolio Positioning (Tab 3)

Ms. Deborah Cunningham from Federated reviewed Federated's investment report for TexPool and TexPool Prime for the quarter ending June 30, 2018. She reported that the TexPool and TexPool Prime portfolios were in compliance with the Texas Public Funds Investment Act, Governmental Accounting Standards Board Statement No. 79, and their respective investment policies. Both pools maintained AAAM ratings by Standard and Poor's and net asset values were never less than \$0.995 or greater than \$1.005. Both pools also met specific portfolio composition and maturity limitation guidelines set out in their respective investment policies.

Ms. Cunningham reported that the TexPool portfolio's assets experienced a seasonal decline but continued to be well above the levels during the same period in 2017. As of June 30, 2018, TexPool's portfolio balance was approximately \$18.29 billion, a decrease of approximately \$1.2 billion from the previous quarter. The TexPool portfolio produced a net yield of approximately 1.81%, up 29 basis points from the previous quarter. Similar to TexPool, Ms. Cunningham reported that TexPool Prime's assets experienced a slight decline with assets under management for the quarter totaling approximately \$4.98 billion, a decrease of approximately \$746 million from the previous quarter. The TexPool Prime portfolio produced a net yield of approximately 2.10 %, up from 1.71% in the previous quarter and reflective of Libor yields rising more than treasury bills. The portfolio's composition changed slightly with commercial paper increasing from 39.1% to 43.9% and variable rate notes decreasing from 31.5% to 29.8%. The increased allocation in commercial paper benefited the TexPool Prime portfolio and the rising interest rate environment benefited both pools.

Both pools remained competitive among their peer groups. TexPool was ranked number two and TexPool Prime was ranked number four among their peer groups in yield comparisons. Ms. Cunningham explained the various stress test scenarios and results for both pools which demonstrated the Pools' ability to maintain a constant dollar value under unlikely extreme or extraordinary scenarios.

Ms. Cunningham reviewed U.S. economic market conditions during the second quarter of 2018. She explained that the Federal Reserve (the "Fed") seemed to be entering a tightening cycle after an interest rate hike in June that raised the fed funds rate to a target range of 1.75-2% and also projecting two more rate hikes in 2018 instead of one. Another contributing factor to quantitative tapering is the fact that the Fed continued to reduce its balance sheet by approximately \$30 billion per month. Ms. Cunningham reported that the labor market was strong, the unemployment rate was 3.8% and inflation remained below 2%. She stated that Federated believes there will be two but possibly three more interest rate increases through 2019. Overall, Federated continues to expect slow and steady economic growth for the remainder of the year.

TexPool and TexPool Prime Portfolio and Performance Review for the 2nd Quarter of 2018 and Related Matters (Tab 4)

Mr. Danny Sachnowitz presented a portfolio review of TexPool and TexPool Prime for the second quarter of 2018. He reviewed the new graphs that depicted each Pool's investor base diversification. He presented an overview of the historical yields for both Pools compared to the Federal Funds rate and other target benchmarks. Mr. Sachnowitz reviewed the average Libor and U.S. Treasury Bill yield curves, both higher than the previous quarter and benefiting both Pools. He explained that the

graph on page five, depicting historical pool yields, demonstrated the positive effect of the Federal Reserve's interest rate hike and noted that TexPool Prime has continued to surpass the Fed Funds rate since June 2016. Both Pools were keeping up with the rising interest rate environment and performing as expected. Mr. Sachnowitz reviewed the asset allocation and maturity charts for both portfolios. The charts depicted the shortening of maturities and increased liquidity of the pools as they prepared for seasonal outflows. He reported that TexPool and TexPool Prime quarterly and annual average yields remained competitive with other Texas local government investment pools.

Report on Services Provided to TexPool and TexPool Prime Participants and Related Matters (Tab 5)

Mr. Ed Sanchez reviewed the information behind Tab 5. He reported that the combined assets in both Pools have increased steadily over the years. He stated that since the Fed began raising interest rates, participant inflows began sooner and were disproportionately higher. Federated informs participants almost immediately after an interest rate announcement. Mr. Sanchez reviewed the participant growth chart for both Pools and explained that TexPool participants had more than tripled from the third quarter of 2013 to present and that participant growth for TexPool Prime has quadrupled during the same period. Thirty new participants have been added to TexPool and 16 new participants to TexPool Prime for the quarter. There are now 2,486 TexPool Participants and 321 TexPool Prime participants. Mr. Sanchez reported that no complaints were reported or filed for the quarter.

Public Comments

Comptroller Hegar asked if there were any public comments. There were none.

Discussion of Next Meeting and Agenda Items

No future agenda items were discussed. The next meeting will be in November and the Board will be contacted regarding a date.

Adjourn

Meeting was adjourned at 10:49 a.m.