

# FUNDAMENTALS OF PUBLIC FUNDS INVESTING



## AGENCY PROFILE ON THE DAY-TO-DAY INVESTMENT OF PUBLIC FUNDS

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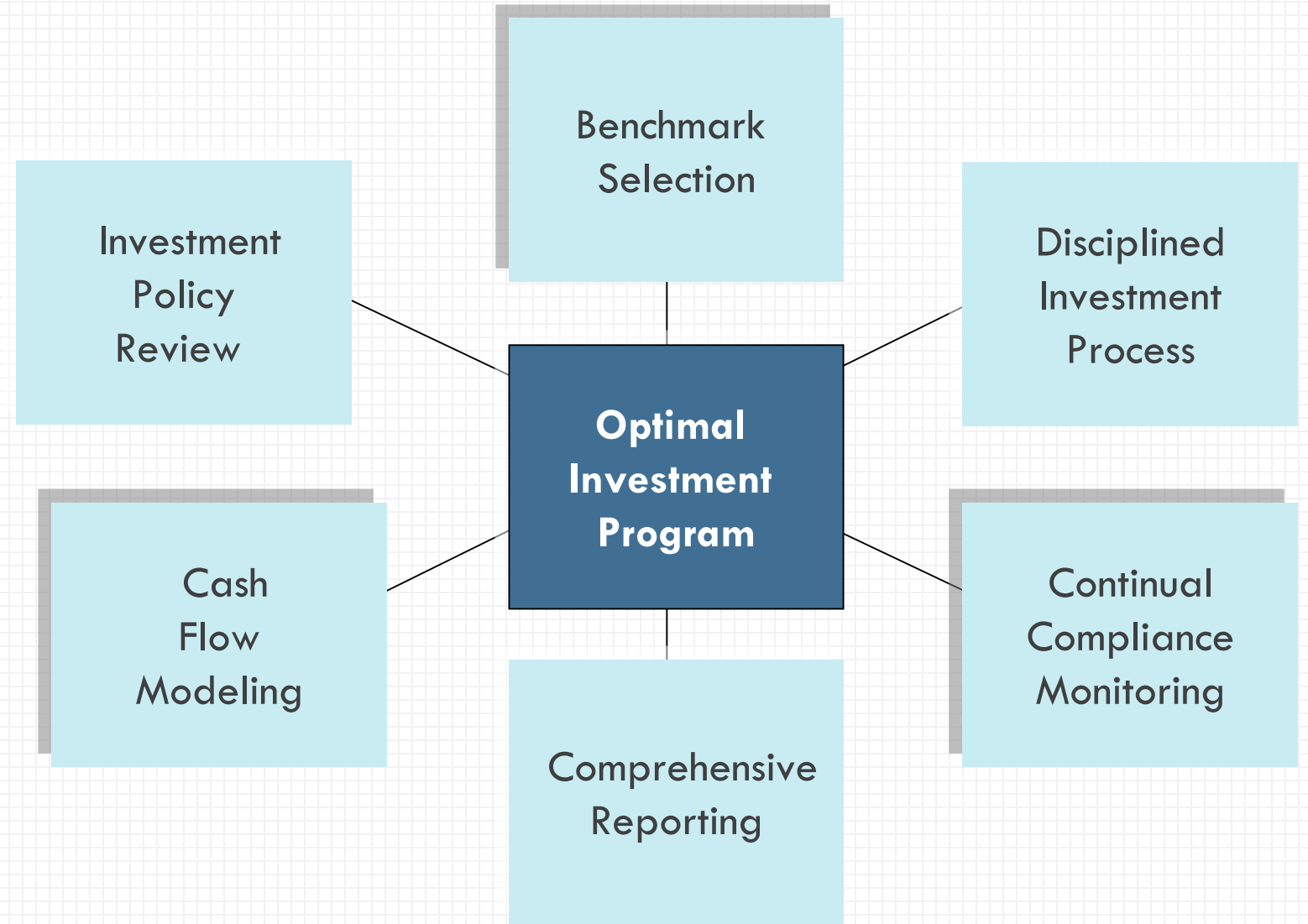
# SESSION OVERVIEW

This session will introduce many of the issues considered relevant to constructing a public fund portfolio and provides a framework for building either a book yield or a total return portfolio.

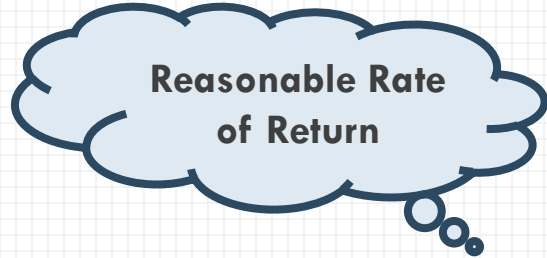
- Elements of a Comprehensive Investment Program
- Fiduciary Considerations
- Tactical Approaches
- Takeaways



# Comprehensive Investment Program



# Prudent Investment Considerations



**ADVISORY COMMITTEE**

**LEGISLATIVE BODY**

**CLEAR & COMPREHENSIVE INVESTMENT POLICY**

**Risk Mgmt.**



**INVESTMENT OFFICIAL**

**INVESTMENT ADVISOR**

**STRATEGY**

**Liquidity**



**ECONOMIC AND MARKET CONDITIONS**

**INVESTMENT DECISION PROCESS**

**CASHFLOW REQUIREMENTS**

**ADJUSTMENTS IN INVESTMENT STRATEGY MADE AS A RESULT OF CHANGES IN CIRCUMSTANCES**

Comprehensive Investment Program

# Overwhelmed by a Comprehensive Investment Program?

I don't have enough staff

Cash flow needs are uncertain

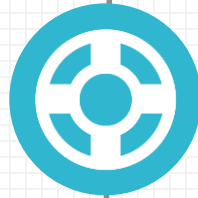
Our portfolio is too small

Can't afford an investment advisor

## RESULTING DECISIONS



Leave excessive amounts in Demand Deposit Accounts



Only participate in Local Government Investment Pool (State, County or JPA)



Relying solely on broker advice without getting separate quotes



Sacrifice market rate of return and or take on risk

## Safety, Liquidity, & Yield

California Government Code, Section [53600.5](#)

When investing, reinvesting, purchasing, acquiring, exchanging, selling, or managing public funds, the primary objective of a trustee shall be:

- 1 Safeguard the principal of the funds under its control.
- 2 The secondary objective shall be to meet the liquidity needs of the depositor.
- 3 The third objective shall be to achieve a return on the funds under its control.

# Prudent Investor & Fiduciary Duty

CA Government Code [53600.3](#)

## PRUDENCE

**...local agencies investing public funds pursuant to this chapter are trustees and therefore fiduciaries subject to the prudent investor standard.**

When investing, reinvesting, purchasing, acquiring, exchanging, selling, or managing public funds, **trustee shall act with care, skill, prudence, and diligence under the circumstances then prevailing, including, but not limited to, the general economic conditions and the anticipated needs of the agency, that a prudent person acting in a like capacity and familiarity with those matters would use in the conduct of funds of a like character and with like aims, to safeguard the principal and maintain the liquidity needs of the agency.**

## Small Agency Approach

Often works directly with a dealer broker\* (Not a Fiduciary) without an investment advisor (Fiduciary)

\*Since broker dealers do not have a fiduciary responsibility to act in your agency's best interest, it is a good practice to obtain competing quotes.



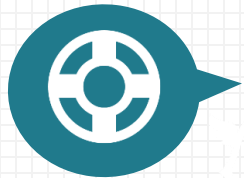
Demand Deposit Accounts



Money Market Accounts



Direct Purchase of FDIC Insured CDs  
Placement Service CDs (CDARS and others)



LALF, County Pools, Joint Powers Authority  
Pools (CAMP or CalTrust) or other Local  
Government Investment Pool (LGIP)



US Treasuries and Agencies



# Reasons to Consider a Registered Investment Advisor

**Registered Investment Advisory Firms** offer a full suite of services to achieve a comprehensive investment program that most agencies are not staffed sufficiently to achieve.



## Staffing

Lack of adequate staffing  
Lack of technical training



## Market Information

Lack of market information systems, such as Bloomberg.



## Dedicated Team

Full-time team of trained professionals  
Increased access to broker offerings  
Compliance Officer  
Credit Committee  
Added Credibility  
Redundancy



## Money

Cost savings due to economies of scale  
Investment performance  
Staff time savings

# Investment Advisory Fees

## **Range of Responses from select Investment Advisors:**

Minimum Portfolio Size: \$10 - \$25 million, depending on the investment advisor

Range of Fees: 5 to 12 Basis Points (BPS)\* of Assets Under Management (AUM)  
Usually Tiered Pricing based on AUM (\$10-\$12 thousand min annual fee)

\* 1 BPS = .01% or .0001 in decimal form

## Establishing a Liquidity Target for the Portfolio(s)



### Liquidity Component

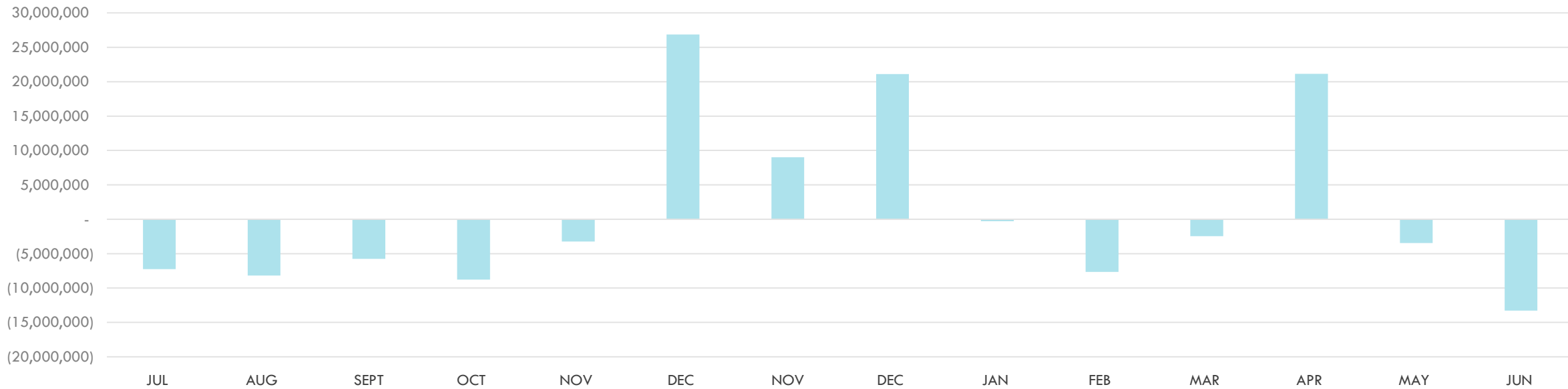
- Meets specific liquidity needs
- Invests in short-term securities
- Average maturity short
- Very low volatility
- Cash flow matching

### Reserve Component

- Targeted to highest suitable duration
- Longer-term securities
- Normally not used for liquidity, but invested in highly-marketable securities
- Greater volatility
- More stable income stream

# Cash Flow Forecasts Are Important

## High Level Seasonal Cash Flow (3 Year Rolling Average)



ESTIMATED INFLOWS	17,430,000	16,330,000	18,730,000	15,730,000	24,430,000	53,730,000	33,158,029	47,830,000	24,030,000	16,630,000	21,830,000	45,430,000	24,030,000	16,830,000
ESTIMATED OUTFLOWS	24,675,848	24,496,600	24,496,600	24,496,600	27,676,600	26,845,722	24,133,438	26,701,920	24,304,848	24,296,600	24,296,600	24,296,600	27,476,600	30,106,920
ESTIMATED NET CASH FLOW	(7,245,848)	(8,166,600)	(5,766,600)	(8,766,600)	(3,246,600)	26,884,278	9,024,591	21,128,080	(274,848)	(7,666,600)	(2,466,600)	21,133,400	(3,446,600)	(13,276,920)

# Daily Cash Needs Sample Worksheet

## Step 1 - Identify New Activity In Process

New Day's Activity In Process		1/3/2019
<b>Source:</b>	<b>OUTSTANDING BALANCE FROM PRIOR DAY</b>	<b>5,888,864</b>
A/P	Warrant Batch	
Cindy	Payroll	41,382.35
A/P	Direct Deposits	2,348,951.01
Cindy	Payroll AP	
	PAYROLL MUNIS CHECKS	12,454.13
	<b>CALPERS UAL PYMNT payroll</b>	
Bryan	Coins Ordered	
Katie	AdminSure Transfer	31,940.65
A/P	PERS HEALTH PREMIUM	
A/P	Revenue Refunds	
Statement	Returned Items	402.34
Dan/A/P/Katie	Xtrnl Withdrawals	160,898.31
Various	Wires & Other Transfers (out)	716,490.76
	Voids	
Katie	Pre-Fund Ext. W/D Epayables	300,000.00
Katie	Direct Deposit Rejects	
Various	Other Adjustments	986.51
Online Banking	Cleared Bank Prior Day	<b>(476,016)</b>
	<b>Adjustments to YB: Debit to Daily Cash</b>	<b>9,026,354</b>
	<b>Adjustments not posted</b>	
		<b>9,026,353.94</b>

## Step 2 - Updated List of Outstanding Activity (Waiting to Clear Bank)

Updated Outstanding Activity		1/4/2019
	<b>MUNIS OUTSTANDING PAYROLL</b>	<b>5,931.13</b>
	DD dated 12/24/2018	107,446.54
	DD dated 12/24/2018	88,968.45
	DD dated 12/31/2018	41,382.35
	MyCalPERS Emp.Health (HR)	
	PORAC TRUST	8,816.56
	ICMA/Payroll	69,879.01
	ICMA/Retiree-Month End	
	AdminSure Transf.	
	Move Funds to Ext.Withdrawal	
	Outgoing Wires that have not left yet	
	<b>CKS THAT HAVE NOT BEEN PRINTED YET</b>	<b>12,454.13</b>
	<b>CALPERS UAL PAYMENT WIRE</b>	
	<b>CALPERS UAL PYMNT payroll</b>	
	<b>CALPERS UAL PYMNT HR</b>	
	Murphy wire has not gone out yet 1/2/19	10,000.00
	HUD PAYMNT	
	Wire to Empower has not left the bank	160,898.31
	Bank of America CC's & Epayables	300,000.00
	Payroll Taxes will clear on Friday	637,795.19
	Payroll Direct Deposit will clear Friday	2,348,951.01
	<b>MUNIS OUTSTANDING GENERAL</b>	<b>5,233,831.26</b>
		<b>\$9,026,353.94</b>

## Step 3 - Cash to be Transferred In/Out

### Determine whether to Transfer funds In/Out

Current Available Bank Balance	\$ (5,429,584.25)	
Current outstanding AP & Pay checks	\$ 5,239,762.39	
Direct Deposits	3,303,239.11	
Estimated Payroll		
<b>OUTGOING WIRES</b>	<b>\$ 10,000.00</b>	
Deferred Compensation	\$ 160,898.31	9,026,353.94
<b>TO CALPERS</b>	<b>\$ -</b>	
Epayables		
monthly cc's	\$ 300,000.00	
MISC	12,454.13	
<b>AP Estimate</b>		
<b>Wire to (from) LAIF</b>	<b>\$ (5,000,000.00)</b>	
<b>Adjusted Book Balance</b>	<b>\$ (1,403,230.31)</b>	



Our Goal is to keep less than \$2 Million in our demand deposit account

# Example Tactical Approach



Less than 1 Full time equivalent staff member assigned to treasury under this model.

# Takeaways

## **FIDUCIARY DUTY REQUIRES A COMPREHENSIVE INVESTMENT PROGRAM:**

- Well Written & Comprehensive Investment Policy
- Regular Investment Policy Review
- Benchmark Selection
- Disciplined Investment Process
- Cash Flow Modeling
- Compliance Monitoring
- Comprehensive Reporting

## **RISK MANAGEMENT IS AN INTEGRAL COMPONENT OF A COMPREHENSIVE INVESTMENT PROGRAM:**


- Liquidity
- Market Risk
- Credit Risk
- Reinvestment Risk
- Event Risk
- Diversify to reduce exposure to risks

## **MEASURE PERFORMANCE AGAINST BENCHMARKS:**

Important to manage expectations and communicate strategy

## **MISCELLANEOUS:**

- Make use of analysis tools and resources at your disposal
- Review Policy with oversight board frequently
- Consider Investment Certification Program – CMTA, APT or Others
- Cash flow forecasts are imperative to Comprehensive Investment Program
- Opportunity cost of remaining too liquid or waiting for market changes



# THANK YOU

We look forward to your participation in the next webinar in this series, *Benchmarking*.

