



WASECA COUNTY BOARD OF COMMISSIONERS WORK SESSION

June 15, 2021 · 8:30 a.m.

County Commissioners Room

300 North State Street – East Annex · Waseca, Minnesota 56093

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8:30 a.m.

- 1. Call to Order and Pledge of Allegiance**
- 2. Waseca County Investment Management Recommendations
Fran Windschitl, CPA**
- 3. Adjourn**

June 6, 2021

Waseca County Board of Commissioners
Mr. Michael Johnson – County Administrator
Ms. Tammy Spooner – County Auditor/Treasurer
307 N State Street
Waseca, MN 56093

Re: Investment management recommendations project

Dear Waseca County Board and Administrative Staff,

Thank you for allowing me to assist the Waseca County in reviewing the management of your investments as a contract employee. I believe my recommendations contained within this letter will help the County build a successful investment program. Throughout my career, I have gained extensive knowledge by reviewing/auditing/working with the cash and investments of over 28 Counties with the Office of the State Auditor, Employment with other Counties and then by managing the Rice County portfolio for the past 30 years. Over this time, I have developed a real passion for maximizing the return on Rice County's investments given the first priorities of safety and liquidity. These past experiences and knowledge have helped Rice County earn among the highest long-term fixed income returns for all local units of governments in the State of Minnesota.

My review included discussions with Mr. Michael Johnson and extensively with Ms. Tammy Spooner regarding the County's investment program. I was provided the County's investment policy, a list of investments the County held as of April 2021 and statements from the County's brokers. In addition, I was provided the quarterly cash report and cash book.

I was asked by Mr. Johnson and Ms. Spooner to review Waseca County's Investments and provide a written summary of recommendations as follows:

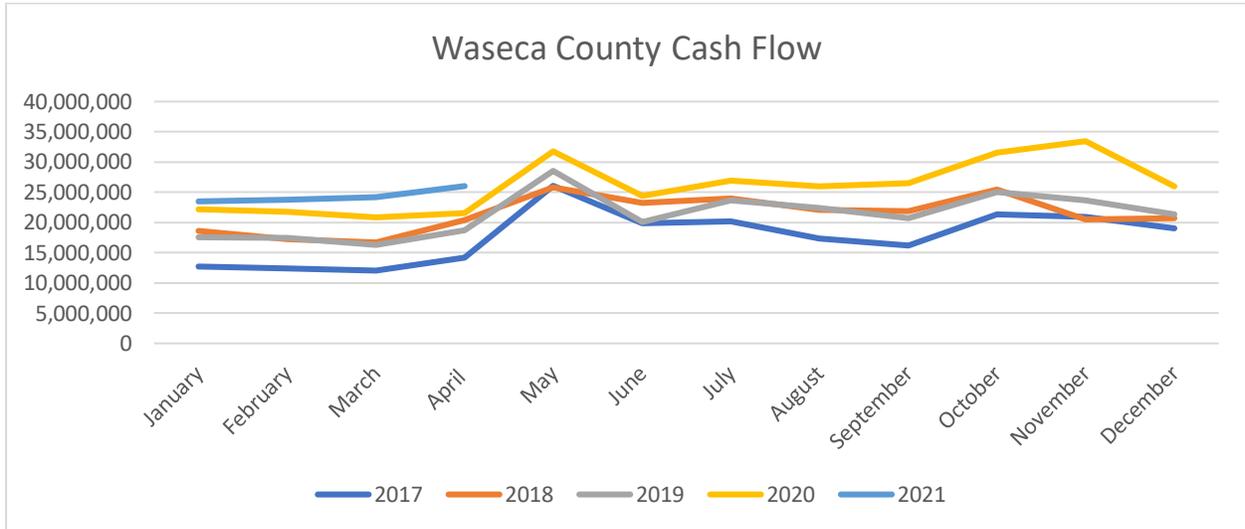
- Review Investment portfolio and cash flow considerations
- Provide recommendations on reinvesting investments that are maturing and that are currently liquid
- Provide staff with the knowledge and skills to find more optimal returns for the portfolio given safety of principal and adequate liquidity to meet cash flow needs.

Here are my findings.

Cash flow patterns

From the County's cash balances spreadsheet by year, I was able to graph its cash flow patterns. The County also provided a comparison of historical investments to total cash, which revealed that it has typically invested around 70% of its total cash. Attached is a cash flow graph indicating options which may be attainable given historical cash flow and discussion of future cash flows with Tammy. Please note that I have indicated a \$3.0 million buffer which could be invested in liquid or investments that

could easily be converted to cash should a unexpected need arise. The cash flow chart indicates a three year low of total cash to be about \$16.3 million in March 2019. Given the current economic environment with the additional reserves provided by federal economic stimulus and the correlating spend down, the core portfolio could be expanded to around 18 million with targeted maturities around low cash flow points (typically March, April, August September which are before tax collection).



I have reviewed the current year cash flow analysis provided by Tammy and it appears reasonable and conservative. I have also provided the Best Practices - Cash Flow Analysis recommendations from the GFOA link for your review.

<https://www.gfoa.org/materials/using-cash-forecasts-for-treasury-and-operations-liquidity>

It is important that Tammy be included in conversations regarding future departmental cash flow considerations. The better understanding Tammy has the more that can be invested to gain better rates of return. The chart below contains the historical interest earnings per either the audit or on a cash basis compared to average monthly cash balance of the county. From the rates of return, you can see that the County has taken on more of a position of safety as balances are highly correlated with its short-term portfolio performance.

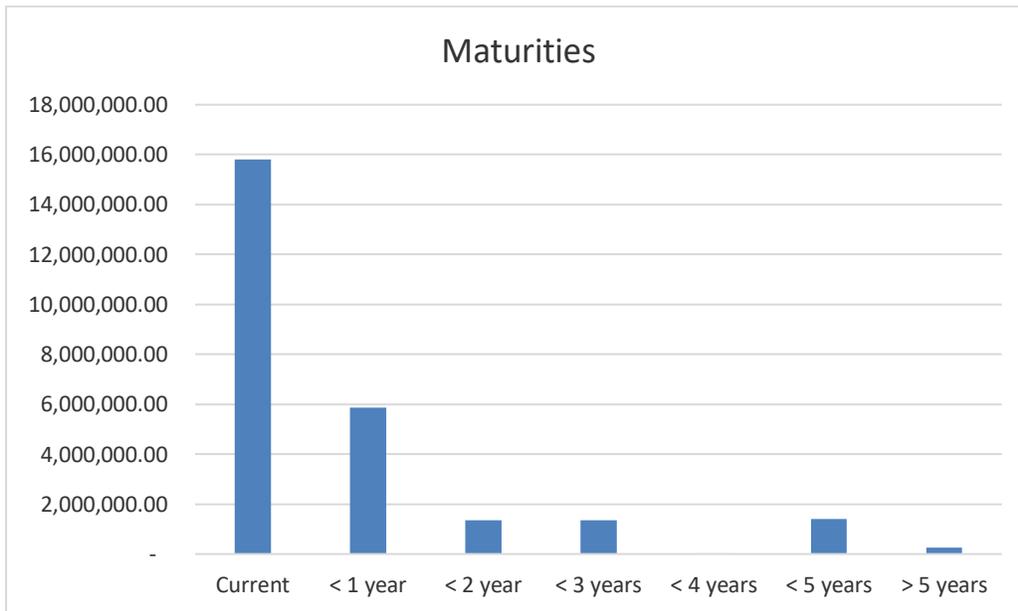
Waseca County Rates of Return

	2017	2018	2019	2020	2021
Report Basis	Audited	Audited	Audited	Cash	Cash
Interest Earnings	81,462	236,120	427,419	219,849	40,410
Rate of Return	0.46%	1.10%	2.01%	0.84%	0.17%
Rate of return calculated on average monthly cash balance					

The current weighted average coupon for the entire portfolio is .37% and the weighted average life is .63 years. The weighted average coupon for the invested portfolio is .91% and weighted average life is 1.61 years. If you trying to establish a 5 year laddered portfolio, the weighted average life should be in around 2.5 years.

Laddering of Investments

I also was provided with the Waseca County's current investment portfolio. This revealed that the County has \$10.2 million invested with maturities greater than 1 day as of April 30, 2021 out of a total of \$26 million. Below is a graph with the current annual maturities. I have also provided Tammy with a spreadsheet to analyze how the total annual maturities change given a date supplied.



There are several strategies that I have seen deployed in the past regarding structuring maturities. The goal would be to match expenditures with cash on hand and then have investments periodically coming due to take advantage of changing interest rates. This is beneficial because it is difficult to time the market. Generally, the longer an entity ladders its investments the greater return it will achieve. Conservative entities ladder out to 3 years and many I have seen ladder over 5 years with some isolated balances designated out longer to meet long-term needs. It appears as if the County may have used this strategy in the past. This would put a target of about \$3.6 million maturing each year. It would appear from the chart, the County may be short in establishing these maturities and may want to target future purchases to build an investment ladder. I will provide the Auditor/Treasurer the spreadsheet to see how annual maturities change as new data and measurement dates are supplied. The key is to always have a reasonable amount of liquidity available to meet current cash flow, with the remainder invested.

An evenly laddered portfolio has the same amount coming due each month. This strategy makes the decision on when to invest and the general amount to invest very easy. However, this strategy may have investments mature when you do not need the extra cash flow.

At Rice County, the strategy has been to ladder the investments by year mostly targeting maturities when we would most likely to need the cash to meet operational needs. From the chart above it would appear that the County's high points are May and October while March April, August September are lower points. If the County were to employ this strategy, the low points would be when more maturities could be focused.

Another strategy the County may wish to consider would be a bar bell strategy. This would position a larger share of the portfolio short and a large share long with less in between. This strategy can be effective when a steep yield curve is present or when investment rates may be trending down.

In addition, I have the following recommendations that I have found successful in providing municipalities the best return on their investments over the long run.

Currently the County invests \$4.1 million or 16% with its two brokers MBS and Wells Fargo. Most of this is invested in Negotiable Brokered CD's and callable Government Agency Bonds. As interest rates rise above the rates in which these investments were purchased, the unrealized losses grow. This provides for less liquidity options and prevents the movement of investment dollars to higher yielding instruments. Currently, the County has a buy and hold strategy however the County maybe missing out on yield enhancement opportunities. If the County purchased more direct CD's from bank with short penalties for early withdrawal, you may have the option to upgrade yields as rates rise.

Developing relationships with local banks helps also enhance the yield on your investments. I have found if you leverage market knowledge, you may be able to get 10 to 50 basis points better yielding investments than what brokers are providing. Also investing locally is good for the community. Banks are more willing to provide higher rates and waive penalties if you have a personal connection. Wouldn't you rather do business with someone you know rather than a stranger?

Periodically survey the market. Generally, the more quotes you get the better returns you will find. Rice County obtains as many as nine when it buys or sells brokered securities and surveys more than 400 banks annually on direct bank deposits.

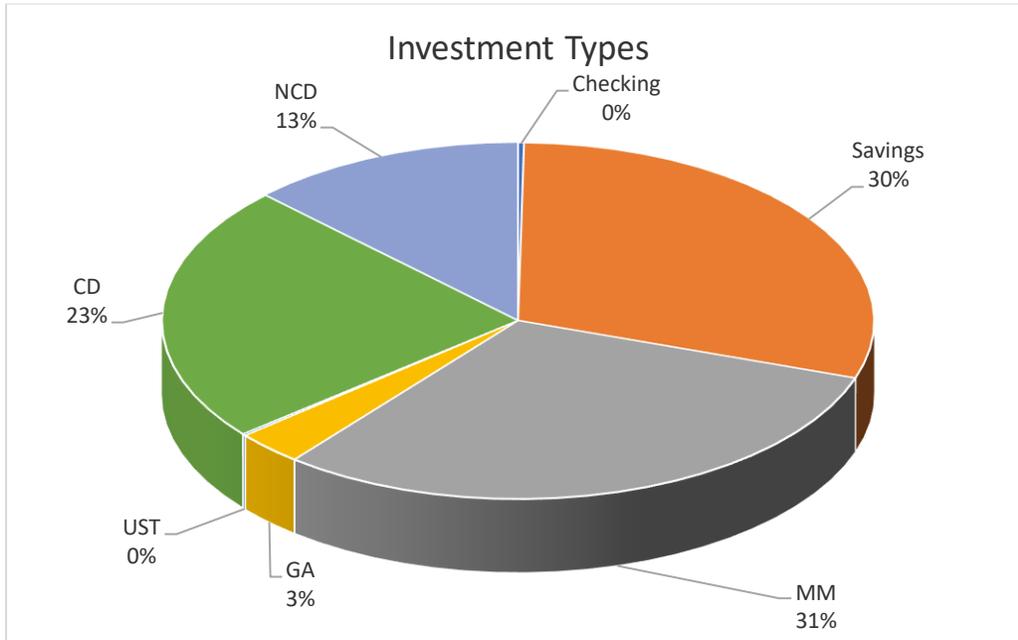
Develop an investment strategy for market changes and liquidity need changes.

Manage the portfolio based on total return. Opportunities may be presented to sell investments at a loss but make a greater return over time.

Develop an investment strategy for diversification. Below is a link to best practice recommendations from the GFOA.

<https://www.gfoa.org/materials/diversifying-the-investment-portfolio>

Here is how the Waseca Portfolio is diversified by investment type:



CD - Certificate of Deposit, NCD - Negotiable Certificate of Deposit, UST - US Treasury, GA - Government Agency

Gain an understanding of the market through emails from brokers, Qwickrate and other online resources. Use this knowledge to leverage market and above market rates with appropriate investment choices.

Prioritize staff time to manage this function. It is very important and can provide significant non tax resources to the County.

Provide periodic reports to the County Council or Investment Committee.

Safekeep your investments with a Third-Party custodian. This is a GFOA best practice link has been included for your review. The benefits include improved protection and control against fraud to minimize custodial risk. It also enhances the competitive bidding process, centralizes reporting, and provides easier access to investment information.

<https://www.gfoa.org/materials/using-safekeeping-and-third-party-custodian-services>

As of my start date May 10th, here are some of the new investment placements Tammy and I have made:

- CD Granite Falls Bank 1.45%, 5 year maturity
- CD First National Bank of Osakis 1.25%, 4 year maturity
- CD Rushford State Bank 1.6%, 5 year maturity
- CD Pioneer Bank .85%, 32 month maturity
- CD United Prairie Bank 1.05%, 5 year maturity
- Money market Community Bank Eagle Lake .4%
- CD Minn Star Bank 1.05%, 5 year maturity
- CD Cornerstone Bank .9%, 5 year maturity

These placements will significantly improve the rate of return on the portfolio, provide flexibility for liquidity when rates change, and many are invested in the banks of the local community.

In conclusion, I am anxious to assist the County in its selection of investments and believe I can make a significant difference in the amount of interest revenue the County may earn over time. It will require some changes in current practices to be made. I have already built a strong network of bank and broker contacts and have a comprehensive understanding of the marketplace. I understand that the goal is for me to provide staff with the knowledge to carry on best practices so that I may be phased out in the future (which fits my retirement objectives including spending time on my wife, kids, grand kids, travel biking, hiking, skiing, canoeing, other volunteer activities etc....)

Thank you again for allowing me the opportunity to help you with your investments.

Sincerely,

Fran Windschitl, CPA