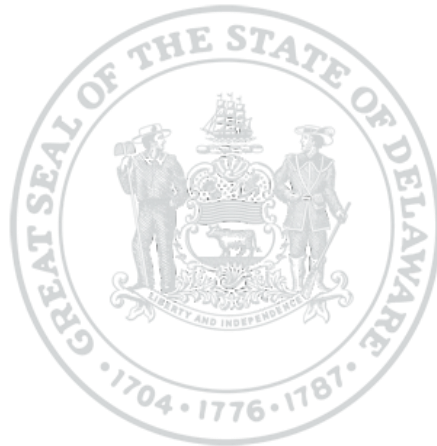


Cash Management
Policy Board

ANNUAL REPORT

To the Governor and
General Assembly



Fiscal Year 2018

July 1, 2017 – June 30, 2018

LETTER FROM THE CHAIR

John V. Flynn, Jr., Ph.D.

When I penned this letter at the close of FY17, I wrote that the Cash Management Policy Board anticipated crucial changes to the State's investment and banking architectures in FY18. The Board spent the past several years undertaking a careful review of the State's investment practices to ensure that the Board's commitment to its mandate – ensuring security, liquidity and adequate return on the State's invested funds, is being fully realized. This fiscal year presented Delawareans with the opportunity to reap the financial benefits of the Board's recent investment restructuring. With the investment initiative complete, we anticipate shifting our focus in FY 19 to the State's banking services landscape, where we hope to yield similarly transformative results. This report highlights the key achievements of FY18 and outlines our goals for what we hope will be a productive FY19.



In FY17, the Board's financial advisors, NEPC, conducted a liquidity analysis of the State's investments, which catalyzed a proposal to revise the underlying portfolio architecture. The goal of this proposal was to reduce costs associated with the incumbent investment architecture, while maintaining the same level of security and liquidity. In FY18, the Board approved the requisite changes to the State's investment guidelines to facilitate the redesign, and moved forward with re-bidding the investment manager contracts. By the end of FY18, the State's new portfolio managers and their respective investment mandates were fully implemented. Additionally, the Board conducted its first review of the State's current endowment portfolio managers since the inception of their contracts three years ago. The results were satisfactory and as a result, the Board granted a one-year extension for each manager. With the enhanced investment architecture now in place, we anticipate that FY19 will be spent carefully monitoring the results under the new architecture and fine-tuning the investment guidelines as needed.

In FY18, the Board laid the foundation for a comprehensive banking services redesign with a structural analysis performed by the State's banking consultant, PFM. Upon completing the review and presenting their findings, the Board elected to re-bid all general banking services contracts, with the intention of awarding new contracts beginning in FY19. The Board also anticipates re-bidding and awarding contracts for the State's local banking services needs in FY 19. We intend to continue our partnership with PFM in FY19, as we collaborate to develop and implement a rigorous vendor management program, which will minimize third party risk, and maximize results from the State's new banking services structure.

This fiscal year was a truly exciting and productive year for the Cash Management Policy Board. We realized the fruits of our labor in optimizing the State's investment portfolio, while sowing the seeds for more exciting changes in the State's banking architecture. The Board works diligently to keep Delaware State funds safe, while ensuring value and efficient service delivery. It has been an honor to uphold that mandate for another year. The Cash Management Policy Board has helped to shape the field of public finance in Delaware for over 30 years through the guidance and insight of a collective body of government and industry leaders. We look forward to continue serving Delaware in this upcoming fiscal year.

Sincerely,

A handwritten signature in black ink, appearing to read "John V. Flynn, Jr.", written over a horizontal line.

OVERVIEW OF THE BOARD'S WORK IN FY18

- Amended and approved the investment guidelines to facilitate a new investment architecture in the second quarter of FY18
- Re-bid all Liquidity and Reserve investment manager contracts in the second quarter of FY18, and completed transition to the new investment architecture in the third quarter of FY18
- Completed transfer of school district scholarship funds to current Endowment managers to comply with investment guidelines in third quarter of FY18
- Finalized banking structure analysis with PFM, and developed scope of services for banking services Request for Proposals in the third quarter of FY18
- Exercised first one-year extension of Endowment manager contracts in fourth quarter of FY18.
- Approved and posted new guidelines for collateralization standards for State funds in the fourth quarter of FY18
- Ensured the ability of State agencies to continue processing credit card payments by completing the conversion to Bank of America Merchant Services in the fourth quarter of FY18
- Amended and approved a new, more equitable interest rate calculation for School and Special Funds on deposit with the State in the fourth quarter of FY18
- Began the process to re-bid all banking services contracts in the fourth quarter of FY18

OVERVIEW OF THE BOARD'S GOALS FOR FY19

- Exercise contract extensions with the State's incumbent banking services providers and banking consultant to ensure adequate coverage for the duration of the banking services transition in the first quarter of FY19
- Review and approve a removal of the 5% cash requirement in the endowment manager portfolios in the second quarter of FY19
- Exercise the first one-year extension of the Board's investment consultant contract with NEPC in the second quarter of FY19
- Commence contract negotiations with banking services finalists in the second quarter of FY19
- Finalize and award general banking services contracts in the third quarter of FY19
- Issue a Request for Proposals for Local Banks in the third quarter of FY19
- Finalize and award local bank contracts in the fourth quarter of FY19
- Develop and implement vendor management process with PFM by the end of FY19

INVESTMENT PERFORMANCE RESULTS FOR FISCAL YEAR 2018

Total Liquidity Portfolio Results

As of June 30, 2018, the market value of the Liquidity Portfolio was \$982,576,144. The Liquidity Pool generated a Fiscal Year 2018 return of 1.27%. The restructuring of the Liquidity portfolio during the year shifted the focus from a return perspective to a liquidity perspective. This shift resulted in the underlying portfolios focusing on ensuring that adequate liquidity existed to fund operations. The resultant portfolio at year-end consisted of high quality U.S. government, agency and select investment grade securities, which performed well during the fiscal year.

Total Reserve and Operating Portfolio Results

As of June 30, 2018, the market value of the Reserve and Operating Portfolio was \$1,215,261,960. The Reserve and Operating Portfolio generated a Fiscal Year 2018 return of 0.28%, which outperformed its Custom Index return by 0.39%. Contribution to the above benchmark return was due to the actively managed accounts exceeding their respective benchmarks. Overweight positions, relative to the Custom Index, in corporate and structured securities were beneficial to the portfolio as credit spreads narrowed during the fiscal year.

Total Land and Water Endowment Fund Results

As of June 30, 2018, the market value of the Land and Water Endowment Fund Portfolio was \$69,344,500. The Land and Water Endowment Fund generated a Fiscal Year 2018 return of 6.41%, which trailed its Custom Index return by 0.04%. Contribution to the shortfall was the Fund holding a 5% cash position, which detracted 0.24% from the Endowment Fund's results. Two of the three actively managed accounts generated above benchmark results. The excess returns generated by these two strategies was due to an overweight position in U.S. equities with corresponding underweight positions to non-U.S. equities and fixed income during the fiscal year.

**Cash Management Policy Board Annual Report
Fiscal Year ending June 30, 2018**

| | Market Value (\$) | % of Portfolio | 3 Mo (%) | 1 Yr (%) | 3 Yrs (%) | 5 Yrs (%) | Inception (%) | Inception Date |
|---|----------------------|-------------------|--------------|-------------|--------------|--------------|------------------|-------------------|
| Delaware Total Consolidation | 2,267,182,604 | 100 | 0.33 | 0.92 | 1.13 | 1.02 | 1.88 | Jan-05 |
| Total Liquidity & Reserve | 2,197,838,104 | 96.94 | 0.36 | 0.68 | -- | -- | 0.9 | Jan-16 |
| Total Liquidity | 982,576,144 | 43.34 | 0.58 | 1.27 | 1 | 0.78 | 1.73 | Jan-05 |
| Liquidity Custom Index | | | 0.43 | 1.09 | 0.79 | 0.62 | 1.73 | Jan-05 |
| <i>eV US Cash Management Net Median</i> | | | 0.48 | 1.37 | 0.85 | 0.57 | 1.46 | Jan-05 |
| PFM Asset Management | 492,906,444 | 21.74 | 0.62 | 1.39 | 1.13 | 0.9 | 0.89 | Jun-13 |
| Wilmington Liquidity | 489,669,700 | 21.6 | 0.53 | 1.05 | 0.87 | 0.68 | 4.23 | Jan-85 |
| Total Reserve | 1,215,261,960 | 53.6 | 0.27 | 0.28 | 0.94 | 1.02 | 2.14 | Jan-05 |
| <i>Reserve Custom Index</i> | | | -0.05 | -0.11 | 0.65 | 0.86 | 2.33 | Jan-05 |
| <i>eV US Interm Duration Fixed Inc Net Median</i> | | | 0.03 | -0.35 | 1.24 | 1.66 | 3.45 | Jan-05 |
| JPM Intermediate | 302,598,195 | 13.35 | 0.39 | 0.31 | 0.91 | 1.02 | 0.92 | Jun-13 |
| <i>J.P. Morgan Custom Index</i> | | | 0.27 | 0.21 | 0.76 | 0.92 | 0.83 | Jun-13 |
| Blackrock Financial Mangement | 304,178,445 | 13.42 | 0.38 | -- | -- | -- | 0.57 | Mar-18 |
| <i>Blackrock Custom Index</i> | | | 0.17 | 0.11 | 0.72 | 0.9 | 0.4 | Mar-18 |
| Chandler Asset Management | 306,602,083 | 13.52 | 0.35 | 0.2 | 0.97 | 1.15 | 0.96 | Jun-13 |
| Lazard Financial Management | 301,883,237 | 13.32 | -0.07 | -- | -- | -- | 0.42 | Mar-18 |
| <i>Chandler/Lazard Custom Index</i> | | | -0.18 | -0.24 | 0.61 | 0.83 | 0.05 | Mar-18 |
| Total Endowment | 69,344,500 | 3.06 | -0.59 | 6.41 | -- | -- | 5.76 | Aug-15 |
| <i>Endowment Custom Index</i> | | | 0.98 | 6.45 | 5.87 | 6.95 | 5.56 | Aug-15 |
| <i>eV Global Balanced Net Median</i> | | | 0.83 | 5.11 | 6.05 | 6.42 | 5.58 | Aug-15 |
| SEI Funds | 22,673,974 | 1 | -0.01 | 6.91 | -- | -- | 7.11 | Aug-15 |
| MSIFT Global Strategist | 21,282,497 | 0.94 | -1.57 | 5.91 | -- | -- | 5.04 | Aug-15 |
| JP Morgan Diversified | 21,816,446 | 0.96 | -0.38 | 7.08 | -- | -- | 6.07 | Aug-15 |
| Cash Account | 3,571,583 | 0.16 | 0.38 | 1.05 | -- | -- | 0.53 | Aug-15 |

Source: NEPC

Notes: Net of Fees. Results for periods longer than one year are annualized.

Performance history through 12/2015 is from BNY Mellon. NEPC Performance start date is January 2016. Fiscal Year end is June 30.

Prior to 03/01/2018 Reserve Custom Index is comprised of 75% BofA Merrill Lynch 1-5 year Govt/Corporate A+ or Better/ 25% 6 Month Treasury Bill.

Endowment Custom Index is comprised of 60% MSCI World Index/40% Barclays Capital Aggregate.

Blackrock Custom Index consists of 100% BofA Merrill Lynch 1-5 year Corporate/Gov A+ or Better.

J.P Morgan Custom Index consists of 100% BofA Merrill Lynch 1-3 year Corporate/Gov A+ or Better

Chandler/Lazard Custom Index consists of 100% BofA Merrill Lynch 5-10 year Gov/Credit A+ or Better

OVERVIEW OF THE CASH MANAGEMENT POLICY BOARD

Creation of the Board. The Cash Management Policy Board was created by the General Assembly as a provision of Title 29, Section 2716 of the Delaware Code when it was signed into law on July 13, 1981. In accordance with the code, the Board is required to submit an annual report to the governor and General Assembly that reviews the State’s cash management practices and performance.

Mission. The Board exists to create policies and provide oversight for the investment of all money belonging to the State or on deposit from its political subdivisions, except money deposited in any state pension fund or the State Deferred Compensation Program, and to determine the terms, conditions and other matters relating to those investments, including the designation of permissible investments.

Responsibility. In carrying out its function to designate permissible investments, the members of the Board are required to exercise the same level of prudence, discretion and intelligence as they would in the management of their own affairs with due regard to the probable income and level of risk from investments belonging to the State.

Authority. The Board is authorized to adopt rules and regulations for the general administration of its duties, and to enter into agreements or contract for the services of private and public consultants, research, or other services, and facilities whenever deemed necessary by the Board.

Composition of the Board. The Board is comprised of nine members, four of whom are government officials serving “ex officio” and five of whom are financial experts from the private sector appointed by the Governor and approved by the Senate. At the end of FY18, the Board was comprised of these members:

Appointed members

Mr. John V. Flynn, Jr. (Chairman)
Managing Director, Healthcare Resource Solutions

Mr. David F. Marvin
Partner, Marvin & Palmer Associates, Inc.

Mr. Warren C. Engle
Retired, Senior Vice President, PNC Bank

Mr. Mike Karia
Board Member

Ms. Lynda A. Messick
Consultant – Bank Governance Advisors

Ex Officio members

Mr. Richard J. Geisenberger
Secretary of Finance

Mr. Jeffery W. Bullock
Secretary of State

Mr. Kenneth A. Simpler
State Treasurer

Mr. Michael L. Morton
Controller General