

Cash Management
Policy Board

ANNUAL REPORT

To the Governor and
General Assembly



Fiscal Year 2017
July 1, 2016 – June 30, 2017

LETTER FROM THE CHAIR

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

The Cash Management Policy Board has spent FY 17 by reviewing key elements of Delaware's investment and banking architecture, with an eye towards implementing meaningful changes in FY 18. The Board continues to seek out industry leaders to provide financial services to the State, ensuring an optimal combination of value and quality of service to State citizens and agencies alike. Each of the Board's decisions in FY 17 was guided by the Board's commitment to improving its mandate: to keep Delaware's financial resources secure and liquid while earning a reasonable return. The hard work of FY 17 laid the foundation for what the Board hopes will be a year of crucial changes in FY 18. This year's annual report highlights a few of the key initiatives that the Board completed during the past year and outlines our goals for next year.



The Board oversaw several key accomplishments in its oversight of Delaware's investments. The Board's financial advisors at NEPC finalized a liquidity analysis of the State's investment portfolio. The results of this analysis brought about a proposal to revise the State's investment architecture in such a way that will reduce costs that are present in the current investment architecture, while maintaining the same level of security and liquidity. This conversion in FY 18 will mark a sea-change in the how the State manages both its liquidity and reserve portfolios. Additionally, the Board worked to complete a successful transition to the State's newly selected investment custodian, Northern Trust. Simultaneously, the Board conducted a review of the rate of return that school and special funds receive on their deposits held with the State Treasurer. The Board agreed upon a rate which, if implemented in FY 18, will provide a fairer and more equitable rate of return to school and special fund depositors.

The Board's oversight of Delaware's banking services in FY 17 continued the theme of foundation building for big changes in FY 18. The Board engaged PFM to begin the work of analyzing the State's banking architecture, with the goal of identifying increased opportunities for the efficiency and efficacy of service delivery. Additionally, the Board's work helped to modernize the banking services landscape in the state by entering into a contract with Bank of America Merchant Services in an effort to stabilize the State's credit card processing abilities. This transition highlights the Board's commitment to providing safety and continuity of service to citizens and customers of the State's many agencies. The Board continued with some of the longer-term projects which carried over from FY 16, including the continued research conducted on collateralization methods used to further safeguard state funds against risk.

Many of these highlighted areas will carry over into FY 18—and we are excited to see all of this hard work come to fruition. The Board works diligently to keep Delaware state funds safe, while ensuring that value is delivered through the most efficient and modern channels. For over 30 years, the Cash Management Policy Board has helped to shape the field of public finance in Delaware with 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,

[JOHN]

OVERVIEW OF THE BOARD'S WORK IN FY17

- Approved and posted new investment guidelines that defined each set of accounts held by managers under most recent investment architecture
- Transitioned smoothly and successfully to the new investment custodian, Northern Trust.
- Contracted PNC Bank to take over direct deposit services through second quarter of FY19 from Wells Fargo
- Finalized the liquidity analysis with NEPC, and proposed new investment architecture to optimize the state's portfolio returns while ensuring security and liquidity of assets
- Engaged PFM to analyze and develop a series of recommendations to increase the efficiency and effectiveness of the state's banking architecture
- Entered into a contract with Bank of America Merchant Services to stabilize the State's credit card processing abilities
- Continued research on collateralization methods used to safeguard against intraday risk, and will finalize with recommendations in early FY18
- Developed a fair and equitable methodology for calculating interest rate paid on school and special funds for inclusion in the new guidelines for approval in first quarter FY18

OVERVIEW OF THE BOARD'S GOALS FOR FY18

- Amend and approve new investment guidelines that will be used for new managers selected by the end of first quarter FY18
- Re-bid all Liquidity and Reserve investment manager contracts and complete transition by the third quarter of FY18
- Exercise first one-year extension of Endowment manager contracts in fourth quarter of FY2018.
- Complete transfer of school district scholarship funds to current Endowment managers to comply with investment guidelines by third quarter of FY18
- Develop and implement with PFM's help a vendor management process no later than second quarter of FY18
- Finalize banking structure analysis with PFM, and develop scope of services for banking services
- Re-bid all banking services contracts in the third quarter of FY18, and begin transition by fourth quarter of FY18 for completion by second quarter of FY19.
- Approve and post new guidelines for collateralization standards for State funds
- Stabilize the ability of State agencies to process credit card payments by fully converting to Bank of America Merchant Services by the fourth quarter of FY18

INVESTMENT PERFORMANCE RESULTS FOR FISCAL YEAR 2017

Total Liquidity Portfolio Results

As of June 30, 2017 the market value of the Liquidity Portfolio was \$988,680,359. The Liquidity Pool generated a Fiscal Year 2017 return of 0.90%, which outperformed its Custom Index return by 0.40%. Contribution to the above benchmark return was due to all four actively managed accounts exceeding the benchmark. An overweight to high quality corporate, structured credit securities, and CD's performed well during the fiscal year. In addition, allocating away from treasury and agency securities was beneficial to the portfolio, as the credit spread between corporate securities and comparable treasuries narrowed over the course of the fiscal year.

Total Reserve and Operating Portfolio Results

As of June 30, 2017 the market value of the Reserve and Operating Portfolio was \$855,371,971. The Reserve and Operating Portfolio generated a Fiscal Year 2017 return of 0.19%, which outperformed its Custom Index return by 0.16%. Contribution to the above benchmark return was due all five of the actively managed accounts exceeding the benchmark. Overweight positions, relative to the Custom Index, in corporate and structured securities were beneficial to the portfolio as credit spreads narrowed during the year.

Total Land and Water Endowment Fund Results

As of June 30, 2017 the market value of the Land and Water Endowment Fund Portfolio was \$66,328,713. The Land and Water Endowment Fund generated a Fiscal Year 2017 return of 12.42%, which outperformed its Custom Index return by 1.95%. Contribution to the above benchmark return during Fiscal Year 2017 was due to all three of the actively managed strategies generating above benchmark results. Contributing to strong returns was an above benchmark allocation to non-US equity markets, which trailed the outperformed the US equity market during the year. An overweight to corporate bonds also added to the strong returns as corporate bonds outperformed treasury securities during fiscal year 2017.

**Cash Management Policy Board Annual Report
Fiscal Year ending June 30, 2017**

	Market Value(\$) Ending June 30, 2017	% of Portfolio	1 Yr(%)	3 Yrs(%)	5 Yrs(%)	10 Yrs(%)
Delaware Total Consolidation	1,910,381,043	100	0.93	1.04	0.85	1.45
Total Liquidity	988,680,359	51.75	0.92	0.72	0.61	1.19
Liquidity Custom Index			0.5	0.54	0.46	1.24
Over/Under			0.42	0.18	0.15	-0.05
Insight Investment	245,868,623	12.87	0.86	0.66	--	--
PFM Asset Management	248,829,522	13.03	1.06	0.83	--	--
Wells Capital Inv. Liquidity	247,394,630	12.95	1.05	0.74	0.62	1.13
Wilmington Liquidity	246,587,584	12.91	0.71	0.67	0.56	1.4
Total Reserve (Including Operating)	855,371,971	44.77	0.25	1.12	0.94	1.98
Reserve Custom Index			0.03	1.05	0.95	2.33
Over/Under			0.22	0.07	-0.01	-0.35
Chandler Asset Management	104,214,660	5.46	0.17	1.26	--	--
Federated Investors	146,429,584	7.66	0.08	1.16	--	--
JPM Intermediate	246,533,929	12.9	0.17	1.11	--	--
Morgan Stanley	156,784,983	8.21	0.28	1.11	--	--
Schroder Intermediate	201,408,815	10.54	0.44	1.09	0.98	1.9
Total Endowment	66,328,713	3.47	12.42	--	--	--
Endowment Custom Index			10.47	4.28	7.76	--
Over/Under			1.95			
SEI Funds	22,788,788	1.19	13.71	--	--	--
MSIFT Global Strategist	21,618,353	1.13	12.07	--	--	--
JP Morgan Diversified	21,920,165	1.15	13.28	--	--	--
Cash Account	1,407	0	0.33	--	--	--

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.
Liquidity Custom Index is comprised of 25% BofA Merrill Lynch 1-3 year Govt/Corporate A+ or Better/ 75% 6 Month Treasury Bill.
Reserve Custom Index is comprised of 75% BofA Merrill Lynch 1-5 year Govt/Corporate A+ or Better/ 25% 6 Month Treasury Bill.
L&W Endowment Custom Index is comprised of 60% MSCI World Index/40% Barclays Capital Aggregate.

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 FY 2017, 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
CEO, MK Consulting, Inc.

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