

MINUTES OF MEETING
STATE BOARD OF FINANCE

November 13, 2018

A meeting of the State Board of Finance of the State of Arkansas was held in the conference room, office of the Treasurer of State, suite 275, Victory building, Little Rock, Arkansas, at 10:00 a.m., Tuesday, November 13, 2018, pursuant to notice duly given to each member of the Board by the Chairman.

The following members were present:

Larry Walther, Director, Department of Finance and Administration
Dennis Milligan, Treasurer of State
Edmond Waters, Arkansas Securities Commissioner
Candace Franks, Arkansas Bank Commissioner
Skot Covert, Representing Andrea Lea, Auditor of State
Cale Turner, Appointed Member
Al Harkins, Appointed Member
Keith Konecny, Appointed Member

Others present were Jason Brady, Grant Wallace, T.J. Fowler, Ed Garner, Autumn Sanson, Damon Dortch, Stacy Peterson, and Celeste Gladden of the Treasurer's staff; Debbie Rogers of the Department of Finance and Administration; Senator Jason Rapert; and Mike Wickline of the Arkansas Democrat Gazette.

Larry Walther served as acting Chairman in the absence of Governor Hutchinson and called the meeting to order with recognition of a quorum.

Minutes of the meeting held on August 8, 2018 were approved as distributed.

Chairman Walther recognized State Treasurer Dennis Milligan to present the Treasury Investment Performance Report for the First Quarter of Fiscal Year 2019. The Report is included in the Minutes as Attachment 1. Treasurer Milligan greeted the Board and stated that he is proud that the State

of Arkansas has given him the opportunity to serve four more years as the Treasurer of State and that it is an honor and a privilege to work with the Board to accomplish good things for the state. He reminded the Board that in the last meeting, he reported that the Treasurer's office had set a record of more than \$21 million dollars receipted in a single quarter. He continued by saying that the Treasurer's office has set another record: the investment receipts for the first quarter of 2019 were higher than the yearly fiscal totals for the years 2012, 2013, 2014 and 2015. Treasurer Milligan told the Board that one of the things that is contributing to such high interest receipts is the constant evaluation of the strategy and evolving with the changes in the market. Treasurer Milligan pointed the Board to the first slide, Total 1st Quarter Revenues, and said the total revenues for the first quarter of 2019 were \$25.4 million dollars. He told the Board that quarterly receipts haven't been this high since the fourth quarter of 2008 when the Treasury was averaging about \$28 million per quarter. Treasurer Milligan moved onto the next slide, Short Term Portfolio and told the Board that the short-term portfolio receipted a little over \$13 million for the first quarter of 2019, and the bulk of those receipts came from investments in commercial paper. He explained to the Board that part of the reason for the return is that rates are better now than they were six months ago, but an important part is also due to the investment strategy. Treasurer Milligan told the Board that the short-term strategy has evolved from focusing on month-end maturities to quarter-end maturities which fits into the bigger picture of investment management while earning better rates. He said that this strategy can be seen playing out on the next slide, Total Revenue Per Month, which shows the monthly comparisons for the past three fiscal years. He asked the Board to take notice of the yellow bars in December, March, and June of Fiscal year 2018, and said they can see how the money that was maturing at the end of each quarter was pushed as far out as the end of the following quarter in order to increase returns. Treasurer Milligan said that the investment team bought maturities just prior to the interest rate hikes and got better rates, which allows the portfolio to earn at the higher rate before the

interest rates go up. Treasurer Milligan pointed the Board to the next slide, Long Term Portfolio, and said that this portfolio received a total of \$12.4 million, which compares to \$13.3 million during the same quarter last year. He explained that the investment portfolio has become more liquid over the course of the last 12 to 18 months in anticipation of higher interest rates, and as the economy improves, the team is studying the market and evaluating the plan for the state's long-term portfolio. He said that with the economy gearing back up, there is potential to move investments toward the longer term and get better rates; however, the strategy at this time still focuses on staying liquid by investing in short-term securities as they monitor developments in the bond market. Treasurer Milligan pointed the Board to the next two slides, Historical Earnings and Fed Fund Rates. He told the Board that these two slides give a view of the Treasury's investment receipts over the past 15 years and detail the interest rates for that same time period. Treasurer Milligan reiterated that Treasury receipts appear to be rising in advance of federal interest rate hikes. He told the Board to take a look at the left side of the interest rate chart and see how previous receipted amounts lag behind the rising interest rates, then compare it to the right side of the chart where receipts are increasing before interest rates rise. He said that this visual helps explain how stretching out short-term investments to focus on quarter-end maturities ahead of interest rate hikes is yielding higher returns for the State of Arkansas. Treasurer Milligan moved on to the final slide, Money Management Earnings, and said that the monthly earnings for the State Treasury Money Management Trust were stable over the first quarter as was the ROI, which reflects the fact that the fund is maintaining large, stable deposits. Treasurer Milligan concluded his report by reiterating that he and his team are monitoring the market on a daily basis, more actively managing the state's \$3.5 billion dollar investment portfolio, and taking advantage of market conditions as much as possible while still maintaining liquidity and protecting the portfolio. He asked the Board for questions or comments.

Chairman Walther commented that the investment returns benefit a lot of different interests in the state, such as the highway fund and the long-term reserve fund. He said that he, along with the Governor, appreciate the work that the Treasurer Milligan and his team have done over the past four years. Treasurer Milligan responded that he believes that he and his team have started to show a little bit of consistency, and it is done with a plan and with good competent people. Chairman Walther then thanked the Board for the support it has given to Treasurer Milligan. Treasurer Milligan responded that he has wanted to earn the trust of the Board, so that when a proposal is made they can consider it with confidence.

Seeing no further questions from the Board, Chairman Walther asked for a motion for the acceptance of the Treasurer's report into the record. The motion was made by Candace Franks and seconded by Al Harkins. All members were in favor.

Next, Chairman Walther made a motion to establish that no funds are available for deposit into the State Board of Finance certificate of deposit investment program. The motion was seconded by Edmond Waters. All members were in favor.

The Chairman then made a motion that the Board direct the Treasurer of State to purchase warrants for the succeeding quarter, January 1, 2019 through March 31, 2019, pursuant to Act 1088 of 2013, and to keep reasonable amounts in demand deposit accounts and money markets during the next quarter for the transactions of the day-to-day activities of the State. The motion was seconded by Al Harkins. All members were in favor.

Chairman Walther called upon Jason Brady to present the next agenda item, legislation proposed by the Treasurer in the upcoming legislative session. Mr. Brady addressed the Board and asked them to refer to pages 4 and 5 in their handout. Amendments to A.C.A. § 19-3-518 are included in the Minutes as Attachment 2. Mr. Brady told the Board that there are two technical corrections to the law due to

antiquated language. First, he addressed a change in the section of the code relating to investments in corporate obligations, which currently reads “a corporate obligation with an investment grade rating of BBB or higher as indicated by at least two nationally recognized statistical ratings organizations.” The requested change will read, “a corporate obligation with an investment grade rating of at least BBB, A2, P2 or an equivalent rating as indicated by at least two nationally recognized statistical ratings organizations.” Mr. Brady told the Board that the change is being requested to match the way in which the Treasury operates, which is under the State Board of Finance investment policy which allows investments rated A2-P2 or higher. Next, he addressed a change to the section requiring three bids on purchases and sales of securities. He told the Board that this requirement refers to an antiquated procedure, especially relating to how the Treasury deals with commercial paper purchases. He explained to the Board that the investment team sees a screen full of commercial paper offerings and looks at the best rates available while matching cash flow and maturity dates needs. He told the Board that he can have staff provide answers to any questions and stated that there will not be any action on these items until the Board approves.

Keith Konecny asked for clarification on the bid process. Ed Garner explained that modern operation in purchasing securities is electronic, with the team seeing 10 or 15 broker offerings. He told the Board that it can be demonstrated operationally that the Treasury knows the market, is getting the best prices, and is not showing favoritism to any broker, which completely fulfills the intent of the law. Cale Turner asked if “best price” is the sole criteria for selection or if there are other factors at play. Mr. Garner responded that the criteria is best price/best value; best price being relative to maturity and volatility, which can all be demonstrated mathematically. He explained that everything the investment team does is recorded because Bloomberg records all actions and all chats; and instead of 2 or 3 brokers the team can now deal with 20, far exceeding the intent of that 3 bid process. Al Harkins

asked if when selling or buying, a record is kept of what is looked at. Mr. Garner responded that via persistent chat, which is recorded and where most of the dealings are done, you can see the range in negotiation. He told the Board that 75% of the purchases made are better than advertised on Bloomberg.

Seeing no further questions, Chairman Walther asked for a motion from the Board to approve the proposed changes to legislation. The motion to approve was made by Keith Konecny and seconded by Cale Turner. All members were in favor.

Next, Chairman Walther recognized TJ Fowler to address the next agenda item, an update on the rules adopted in the last Board meeting. TJ greeted the Board and reminded them that in the last meeting they voted on news rules for the State Treasury Investment Policy and the State Treasury Money Management Trust Investment policy. He told the Board that the rules were approved by the Board of Finance on August 8th, and then on the 9th the APA (Administrative Procedures Act) paperwork was submitted. Mr. Fowler gave the Board a timeline of the APA process, as follows: on August 29th the Governor's office approved both the emergency rule and the permanent rule; in early September the publication of the rules and the announcement for the public comment meeting required under the APA were made; on September 19th the emergency rules were approved by the rules and regs subcommittee for the legislature; on Oct 2nd the ALC approved the emergency rules; on October 29th the public comment meeting was held and no members from the public came to comment. Mr. Fowler stated that the day after the public meeting, the Treasurer's office provided a report to the Bureau of Legislative Research letting them know that the public comment period had run, that there had been no comments, and that there were not going to be any amendments to the rule as passed by the Board. He told the Board that the Treasurer's office is now scheduled to go before the rules and regs subcommittee on the permanent rule on December 18th, followed the next day by the full ALC if it passes the rules and regs subcommittee. He explained to the Board that assuming the ALC approves, the rules will become

effective ten days after the ALC meeting by filing by the Secretary of State. Mr. Fowler concluded his presentation.

Seeing no further questions or comments from the Board, Chairman Walther adjourned the meeting.

ATTEST:

Secretary of the State Board
of Finance of the State of Arkansas

Acting Chairman of the State Board
of Finance of the State of Arkansas

Secretary's Note: All documents pertaining to the issues considered are filed in the permanent records of the State Board of Finance.