



ANNUAL INVESTMENT REPORT
FISCAL YEAR ENDING JUNE 30, 2019

Luciano Panici, Jr., President
Alice Peterson, Vice-President
Thomas Planera II, Secretary
Robert Grossi, Treasurer

"An investment in education always pays the best interest."
Benjamin Franklin

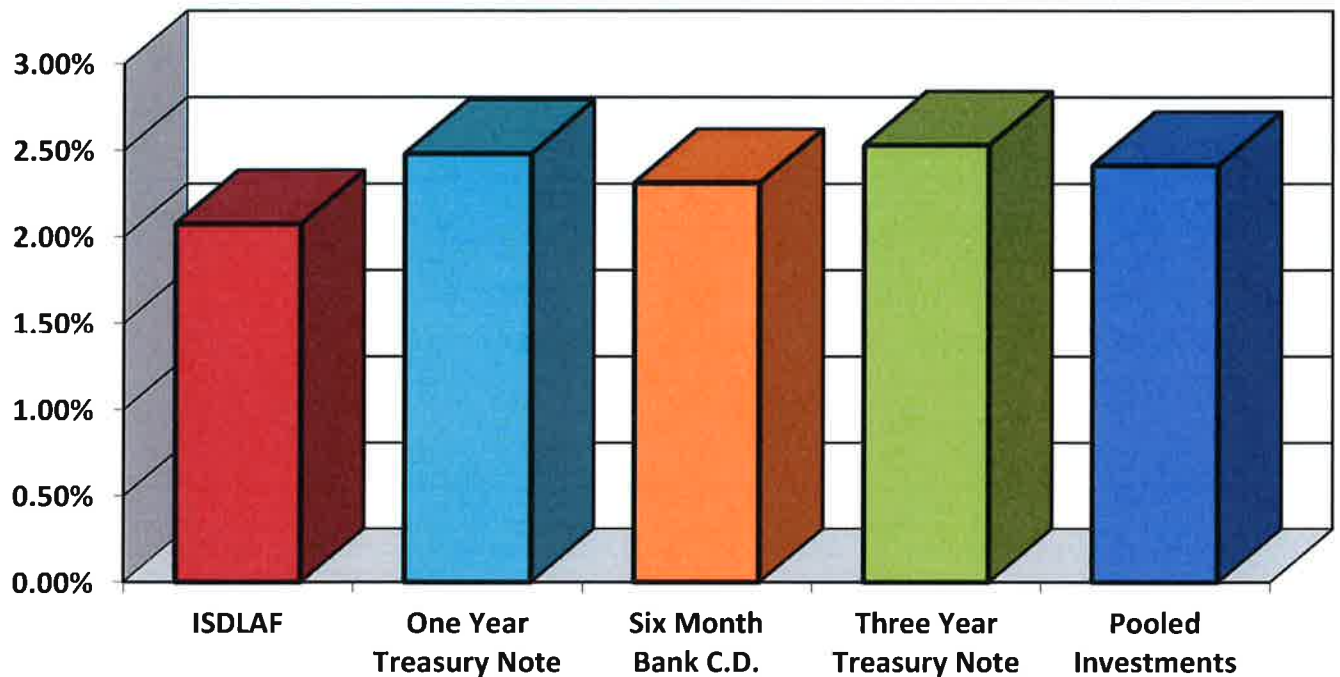
INTRODUCTION

The purpose of this report is to provide information to the administration and the board of education of the school districts and agencies that are serviced by the Bloom Township Trustees of Schools related to their funds for which we serve as custodian. All school districts and agencies that receive this report have their fund balances invested in a pooled portfolio, which consists of the fund balances of all the entities. Each entity owns a portion of the pool based on their level of cash as a percentage of the entire cash being managed in the pool. There are many benefits to this investment structure such as greater diversification, better liquidity and higher, more stable interest rates. Interest from the pooled funds is distributed to the districts based on their percentage of the fund.

The following report is divided into four sections. The first section will summarize the pooled fund's performance for the fiscal year ending June 30, 2019. The second section will provide a review of interest rate movement during the fiscal year and provide our economic outlook. The third section will discuss our current investment strategy and the positioning of the investment portfolio as it relates to market conditions. The final section describes the general investment policy of the Bloom Township School Treasurer's Office.

SUMMARY OF INVESTMENT PERFORMANCE

For the fiscal year ending June 30, 2019, I am pleased to report that the investment pool managed by the Bloom Township Treasurer's Office generated \$8,655,000 in interest earnings to the school districts serviced by this office. Real estate tax revenues and state and federal revenues received during the fiscal year were generally placed in investments yielding between 1.80% and 2.60%. With an average investment portfolio size of \$431,248,000 (pooled investment portfolio plus money markets), the cash basis rate of return to the school districts was 2.01%. The return is a combination of interest earned on the pooled investment portfolio, interest earned in money market funds and changes in market value. The average monthly yield of the pooled investment portfolio for the fiscal year was 2.41%. The following graph compares the average monthly yield on the pooled funds with the average monthly yield of other investments available in the market during this same period:



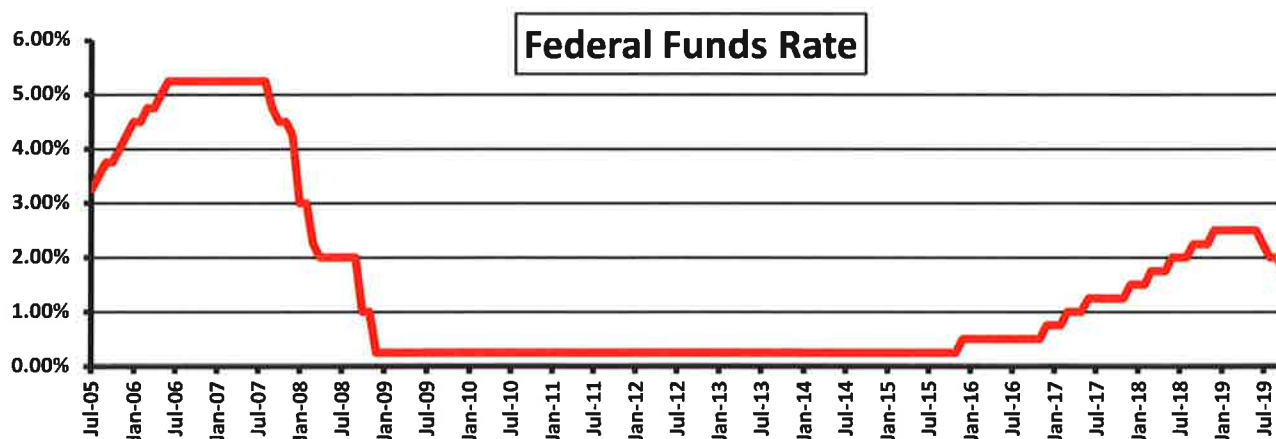
The average monthly yield from the Illinois School District Liquid Asset Fund for the same time period was 2.08%, the one-year Treasury bill was 2.48%, the six-month Certificate of Deposit averaged 2.31%, and the three-year Treasury note averaged 2.53%.

INTEREST RATE MOVEMENT AND ECONOMIC OUTLOOK

For perhaps the first time during one reporting period, the Federal Reserve both raised and decreased short-term interest rates. In both September and December 2018, the Federal Reserve increased short-term interest rates by one-quarter of one percent, raising the Fed Funds rate from 2.0% to 2.5%. This marked the eighth and ninth time since December 2015 that the Fed has hiked its policy rate. Then in a dramatic reversal, the Federal Reserve lowered rates in one-quarter of one percent intervals three times: in July, August and October of 2019. At the end of October 2019, the Fed Funds Rate was 1.75%.

The statutory mandate of the Federal Open Market Committee ("FOMC") is to foster maximum employment and price stability. Specifically at this point in time, the FOMC is looking for maximum employment and two percent inflation. In determining the timing and size of future adjustments, the Committee assesses realized and expected economic conditions relative to its objectives. This assessment takes into account a wide range of information, including measures of labor market conditions, indicators of inflation pressures and inflation expectations, and readings on financial and international developments.

The following graph reflects movement in the Federal Funds Target Rate since July 2005:



Statements made and action taken by the Federal Reserve primarily impact short and intermediate term rates, and subsequently the yield on our pooled investments. It is therefore relevant to monitor and assess both action and inaction taken by this body.

Federal Reserve Chairman Jerome Powell, in his remarks to the U.S. House of Representatives on July 18, 2018 stated that he strongly supported the goals Congress set for monetary policy of maximum employment and price stability. He stated that for the past three

years, the Fed has been gradually raising rates to more normal levels as the economy strengthened. He stated that the Fed believed that this strategy was the best way to set conditions in which Americans who wanted a job could find one and in which inflation would remain low and stable.

In his assessment of the then-current economic situation and outlook, which is closely watched by investors, he stated that the job market continued to strengthen. He stressed that the labor market was robust, with unemployment rates for virtually all sub groups of Americans at their lowest levels since the Bureau of Labor Statistics began tracking such data in 1972. Alongside the strong job market, he added that the U.S. economy had grown at a solid pace during the year. At the time of the last hike in December, it was anticipated that the Federal Reserve would raise rates again two more times in the coming quarters. The question then must be explored is: what happened that caused the Fed to first pause on its policy to raise rates and then to completely reverse course on interest rates and begin lowering rates for the first time since 2008?

First, President Trump was vehemently against these rate hikes, stating, “it incredible” that “the Fed is even considering yet another interest rate hike.” From Trump’s perspective, countries such as China and the European Union were engaging in an aggressive rate-cutting cycle in order to stimulate their economies, while the United States was raising rates, which theoretically slows economic growth. His consistent messaging and policy actions have been geared towards strengthening the US economy and Fed policy, in his mind, was in direct conflict with his vision. Without a current threat of inflation, he believed that raising the Fed Funds rate was wrong and would lower US competitiveness and growth in the world.

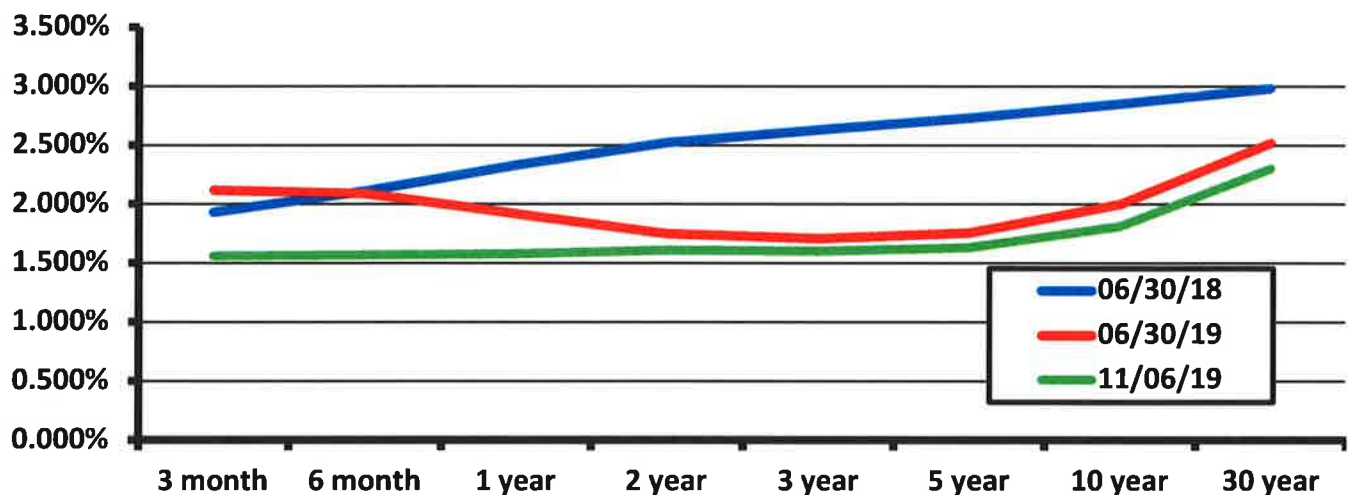
While the U.S. economy showed no immediate signs of slowing down, as it did the last time it lowered rates, the Fed cited a variety of risks that could put a damper on growth. These include fears of global slowing and U.S.-China tariff action. Additionally, there existed no signs of inflationary pressures that would prompt action to slow down economic growth. By cutting rates before any kind of broad-based slowdown occurs, officials judged that they were cushioning the U.S. Economy from any downside risks.

Looking ahead, it is difficult to predict what the next move will be from the FOMC, although most experts expect the next move to likely be a continued decrease in rates. The most significant question at this point is when. If it were up to President Trump, rates would continue to aggressively decline with the goal of maximizing the strength of the U.S. economy. Chairman Powell however seems to be taking a more “wait-and-see” attitude regarding future action by the Fed. The current consensus is that rates will be cut at least one more time in early 2020. Future economic data will likely drive the magnitude of future rate declines.

In August of 2018, the yield curve was briefly inverted with the two-year Treasury having a higher interest rate than the 10-year Treasury, but the yield curve has gradually

reverted to its historically normal upward sloping line. The recent moves in yields largely reflect trade optimism. In the short-term, the announcement of a Phase 1 trade deal between the United States and China created optimism of economic stimulus and consequently raising interest rates. However, with the Fed unlikely to raise the Fed Funds rate any time soon, such move would seem limited. The yield curve still remains extremely flat. From an investment perspective, the difference in interest rate levels between purchasing a three-month Treasury (1.56%) and a five-year treasury (1.63%) is negligible.

The following graph compares the yield curve on June 30, 2018 to the yield curve on June 30, 2019 and the yield curve as of the date of this report (November 6, 2019).



From June 2018 to October 2019, the yield on U.S. Treasury securities maturing in three months decreased from 1.93% to 1.56%. While all areas of the yield curve decreased, the most significant decrease was in the two-ten-year maturity range. Throughout that range, interest rates have dropped approximately 1% during the period. The five-year Treasury, for example, dropped from 2.73% to 1.63%, a decrease of 1.1%.

It is not so difficult to understand what is occurring at the short end of the yield curve which the Fed exercises direct control. What's going on at the long end of the curve gets complicated. This is the part of the yield curve that is more influenced by investor's expectations, including market sentiment and inflation expectations. The current yield curve reflects the expectations that inflation will remain low in spite of continued economic growth. The market is also anticipating the Federal Reserve to continue to lower rates in the future.

Another factor that is putting downward pressure on the longer end of the yield curve is that investing in U.S. Treasuries still generates significantly higher rates of return than other major countries. For example, as of the date of this report, in comparison to the current

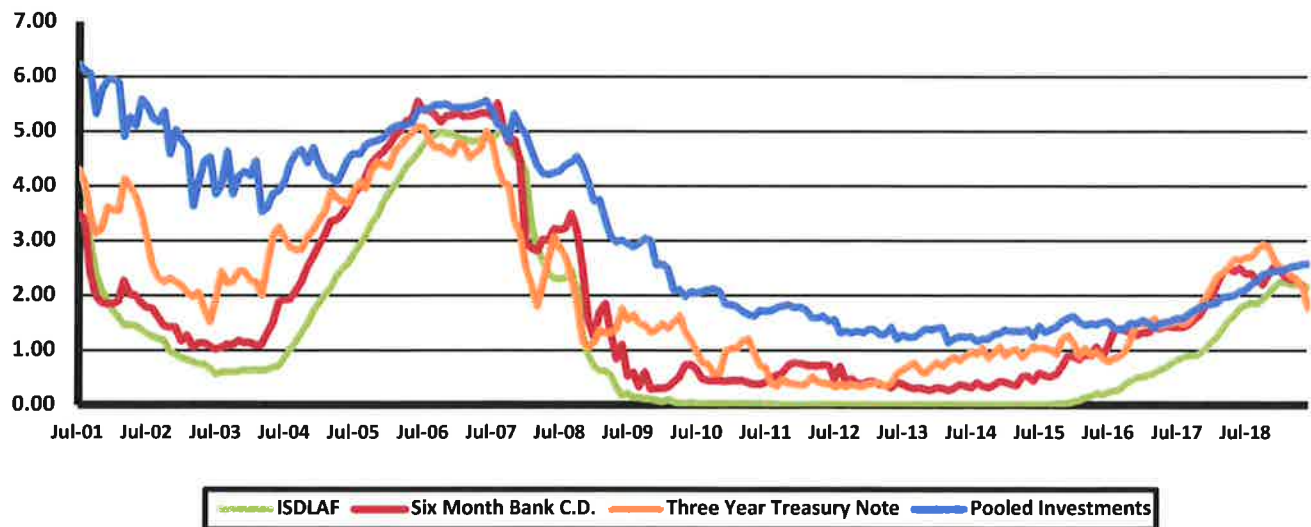
yield on the 10-year United States Treasury of 1.77%, the 10-year yield in the UK is 0.73%, the 10-year yield in Japan is -0.08% and the 10-year yield in Germany is -0.28%.

Putting the change in interest rates over the past few years in perspective, the following summarizes the approximate short-term rates available in the marketplace for investing second installment real estate tax collections:

	<u>Investment Rates</u>		<u>Investment Rates</u>
Fall 2006	4.80% - 5.40%	Fall 2013	0.01% - 0.10%
Fall 2007	3.80% - 4.50%	Fall 2014	0.01% - 0.10%
Fall 2008	1.00% - 3.00%	Fall 2015	0.01% - 0.10%
Fall 2009	0.10% - 0.80%	Fall 2016	0.10% - 0.30%
Fall 2010	0.02% - 0.40%	Fall 2017	0.75% - 1.25%
Fall 2011	0.02% - 0.20%	Fall 2018	1.80% - 2.10%
Fall 2012	0.01% - 0.15%	Fall 2019	1.80% - 2.20%

Concerning the future direction of interest rate levels, there are several major issues that must be closely monitored including (1) future FOMC, (2) geopolitical tensions, primarily with China and (3) the volatility and direction of the U.S. stock markets. Each of these events can influence the fixed income market and subsequently change the overall performance of the pooled portfolio. It is important to recognize, however, that while events such as these and changes in economic activity and inflation have caused interest rates to fluctuate dramatically over the past several years, the yield on the pooled funds investment portfolio has remained relatively stable.

The following graph illustrates interest rate patterns on pooled funds and other investment vehicles since 2001 and illustrates the relative stability of our funds both in times of decreasing and increasing interest rate periods:



In analyzing the relative stability of the weighted average yield of the pooled investments it is important to note that this is not a stagnant portfolio where rising and falling interest rates have no benefit to our pool holders. We receive in excess of \$500 million in revenues annually into the pooled funds. While our core portfolio is affected adversely by rising interest rates, this same rise in rates provides us the opportunity to invest new funds at higher rates of interest. The reverse is true in times of declining rates. While the value of our portfolio rises in a declining interest rate environment, new revenues are invested at lower rate levels, driving down the yields but the core portfolio buffers the decline. As a result, our returns are generally less volatile during both rising and decreasing rate periods.

CURRENT INVESTMENT STRATEGY

Since a significant percentage of the funds received by this office during the fiscal year must be invested to meet short-term cash flow needs, interest rate direction is not the primary factor in investment decisions. It is important, however, to consider current interest rate conditions, yield curves and interest rate trends in determining the overall desired duration of the portfolio.

With little differential in interest rates between money market funds and longer-term investments, there is no immediate benefit to extend out on the yield curve. However, with interest rates declining, there is value in allocating a percentage of the portfolio into longer-term investments in order to preserve current rate levels in the event that rates do continue to decline. For example, if the FOMC continues to drop rates and money market fund yields drop to levels closer to 1%, a portion of the pool would continue to be earning in the 2% range until the investments mature.

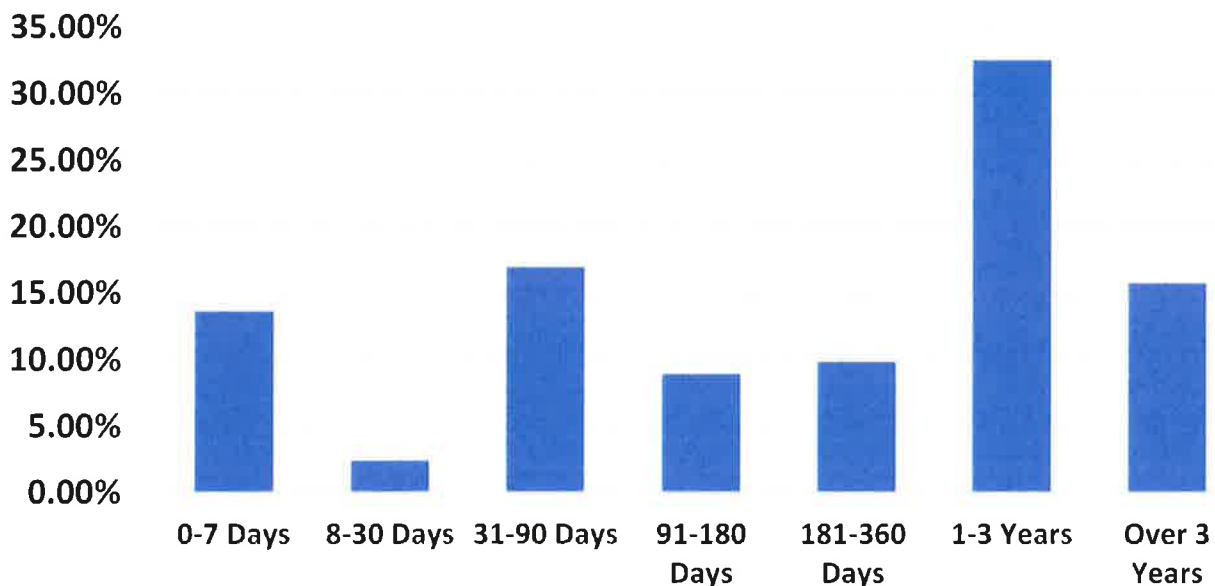
In addition, we continue to look at value amongst the investment vehicle options available to us. We currently are focusing on purchasing bank CD's, bank notes and short-term taxable municipal bonds. We are also active players in the direct purchase of municipal bonds from other school districts and municipalities in Illinois. These strategies have allowed the portfolio to maintain yields above the levels that exist in money market accounts and traditional short-term investments without compromising the objectives of the fund. We are also focused on investment pieces that will provide above average yields in the three-seven year maturity range.

While risk in the credit markets seems to have diminished, we still respect the uncertainty that exists in the near future and are concerned about the possible effects of unforeseen events on our economy and our fixed income markets. We will continue to strongly weigh all investment decisions towards maximum safety and liquidity.

CURRENT PORTFOLIO

Over the past year, we have been investing in an interest rate environment that was first characterized by rising interest rates and then declining interest rates. We continue to be in a rate environment in which there is little current value in extending the duration of the portfolio due to the flat yield curve. Consequently, with the exception of value purchases in the 3- to 7-year maturity range, new money into the portfolio was primarily placed in shorter maturities to meet cash flow needs. Over 84% of the current pooled funds portfolio is expected to mature within three years.

On June 30, 2019, the expected maturity of the portfolio was laddered with consideration of the yield curve, anticipated cash flow needs and anticipated new revenues coming into the portfolio. For example, it is not critical to have maturities coming due in August and September, because that is the time that significant new real estate tax revenues come into the portfolio to cover payrolls and bills coming due in those months.



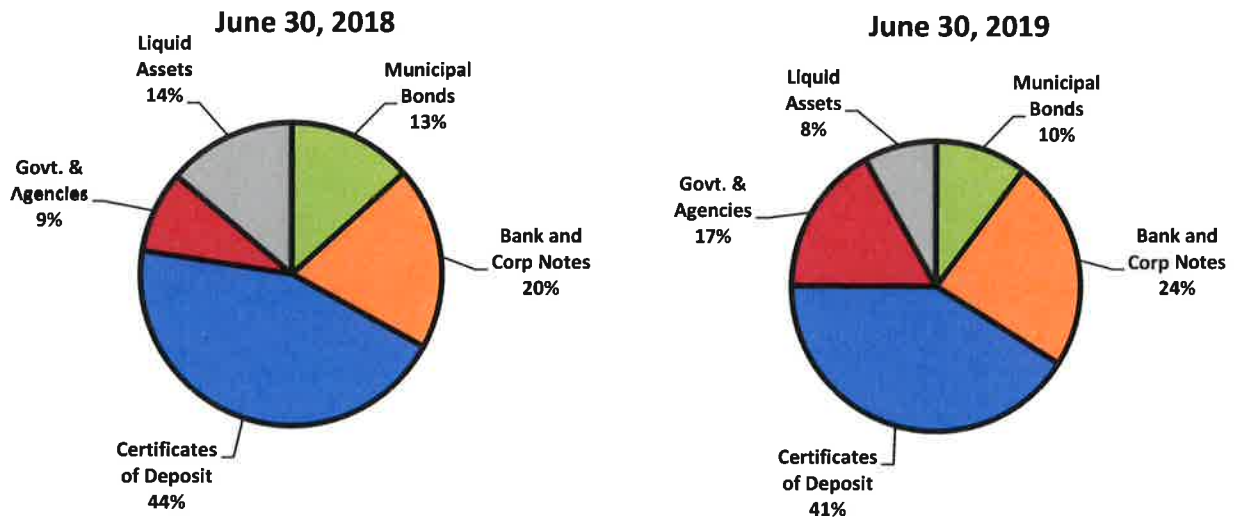
Not only is diversification of maturities essential to the performance of the pool, but also diversification of investment types is equally important. Diversification not only minimizes the risk in the pool but also allows us the ability to consider the entire investment arena in determining which investments will maximize yields while emphasizing safety. The Pooled Funds of Bloom Township consists of over 280 different investments that are monitored regularly.

There are six major categories of investments in the pool:

- 1) Certificates of Deposit - These are direct obligations of a United States bank that are fully insured by the FDIC up to \$250,000 per entity for which this office serves as custodian of funds. Since the Bloom Township Trustees of Schools service 18 entities, the fund is covered for up to \$4,500,000 per banking institution.
- 2) Commercial Paper - Commercial paper is a direct obligation of United States corporations having more than \$500 million in assets. The maturity of such obligations must be under 180 days. The corporations must also be rated in one of the three highest categories by the major rating agencies.
- 3) Bank and Corporate Notes - Bank notes are direct obligations of United States banks which are members of the FDIC. The banks must achieve size and profitability requirements in order to be eligible for investment. Corporate Notes are direct obligations of large U. S. Corporations that meet the stringent criteria established in the Illinois Public Funds Investment Act.
- 4) Government and Government Agency Guaranteed and Collateralized Obligations - These are investments, which are guaranteed by the United States Government or its agencies.
- 5) Municipal Bonds - Bonds issued by a city or other local government, or their agencies. Municipal bonds may be general obligations of the issuer or secured by specified revenues.
- 6) Liquid Assets – Money market accounts in which funds are immediately assessable to the Districts.

During the fiscal year the greatest value in investment type available in the marketplace was in bank and corporate notes and certificates of deposits. Consequently, we increased our position in bank notes, corporate notes from 20% of the portfolio to 24% of the portfolio and we maintained a strong position in certificates of deposits at 41%. The pool is currently invested in certificates of deposit from sixty different banking institutions throughout the Country.

The following pie charts reflect the investment composite of the pooled funds as of June 30, 2019 as compared to June 30, 2018:



INVESTMENT POLICY

The following is a list of various policies, which are followed by the Bloom Township Treasurer's Office when implementing its investment decisions:

MAXIMIZING INTEREST REVENUES

I. In order to maximize interest revenues on the funds received by this office, it is essential that all revenues earn interest as soon as this office receives them. During the past three years we have streamlined our communications with the county, the state and the brokers we deal with to ensure that funds due to the districts are received promptly by our banks. We have increased the use of wiring funds wherever possible rather than dealing with checks, which greatly reduce interest earnings. At the same time, we have established agreements with the banks that service our office to allow us to earn interest on the funds on the same day that a wire is received.

II. Through the pooling of the revenues of seventeen school districts/school agencies serviced by this office, we have the ability to invest in \$1,000,000+ blocks. This allows the districts' funds to be invested in investment types that may not otherwise be available in smaller lot sizes. Also, investing in \$1,000,000 lots often gives us greater liquidity than if investing in smaller sizes.

III. The Treasurer's Office works with several different brokers who have access to investments throughout the country. This allows for more thorough investment decisions to be made.

IV. The Treasurer's Office has established relationships with a large amount of trading desks which contact this office if a seller of an investment desires to liquidate an odd-lot (small size) investment. Odd-lot investments tend to offer higher yields because they are less liquid. Due to the fact that the trading desks already have a buyer for these investments, they will offer them at higher yields to this office, taking less spread out of the transaction.

V. Although local banks may offer rates which are slightly lower than rates offered by other institutions, consideration is given to those local institutions which provide needed assistance to our Districts. This includes banks, which lend Districts funds in times of financial hardship, as well as those banks, which provide scholarships and loans to the students of this community.

VI. The Treasurer's Office consistently updates cash flow projections to allow pooled funds to be invested at higher yields for the longest duration possible. The balance in the Liquid Asset Fund is targeted to be below 6% of the total pool.

VII. The Treasurer closely monitors the investment and economic arena working with both fundamental and technical analysts in order to determine when investments should be purchased and sold as well as to determine the desired weighted average maturity of the portfolio.

MINIMIZING RISK

I. All funds invested by the Treasurer's Office are invested pursuant to the Public Funds Act of the Illinois Revised Statutes and all legislation, which has affected such Act.

II. When Certificates of Deposits are purchased by this office, an effort is made to ensure that the purchase is within the aggregated FDIC insurance limits of this office, which is \$4,500,000. (18 entities x \$250,000 FDIC insurance amount)

SUMMARY

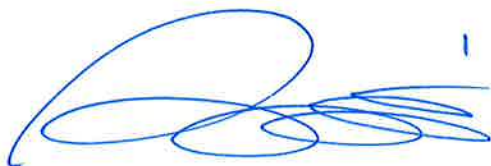
There were two major objectives I had when preparing this report. The first objective was to provide an update to the administration and board members on the investment performance of the districts' funds during the fiscal year ending June 30, 2019. The second objective was to provide a partial list of the strategies, procedures and policies used by this office in order to ensure maximum investment performance of these funds.

We have been annually reporting our fund performance to the school districts we service for the past 28 years. In each of these years, we have performed well compared to all major financial indices we track. During that time, we have returned in excess of \$147 million in interest earnings to the school districts we service. We take the responsibility of managing your district's funds seriously and know that the partnership we have developed over the years, combined with the inherent value of a pooled funds system and the consolidation of fiscal services, has provided benefits to the taxpayers we all service.

In projecting interest earnings for the upcoming fiscal year, I expect returns to be below prior levels realized in FY 2019 for two primary reasons: (1) Interest rates, and consequently reinvestment rates, are projected to decline pursuant to expected action by the Federal Reserve; and (2) investments that were purchased during a higher interest rate environment have generally been called or matured over the past few years.

I would appreciate any suggestions or comments the districts may have. This report will continue to be produced annually. If at any time during the year information pertaining to the investment portfolio is desired, it will gladly be provided.

I thank you for letting us serve your district.



Robert G. Grossi
Bloom Township School Treasurer