



McHenry  
County College

# Review of Investment Portfolios Third Quarter 2015

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PFM Asset Management LLC

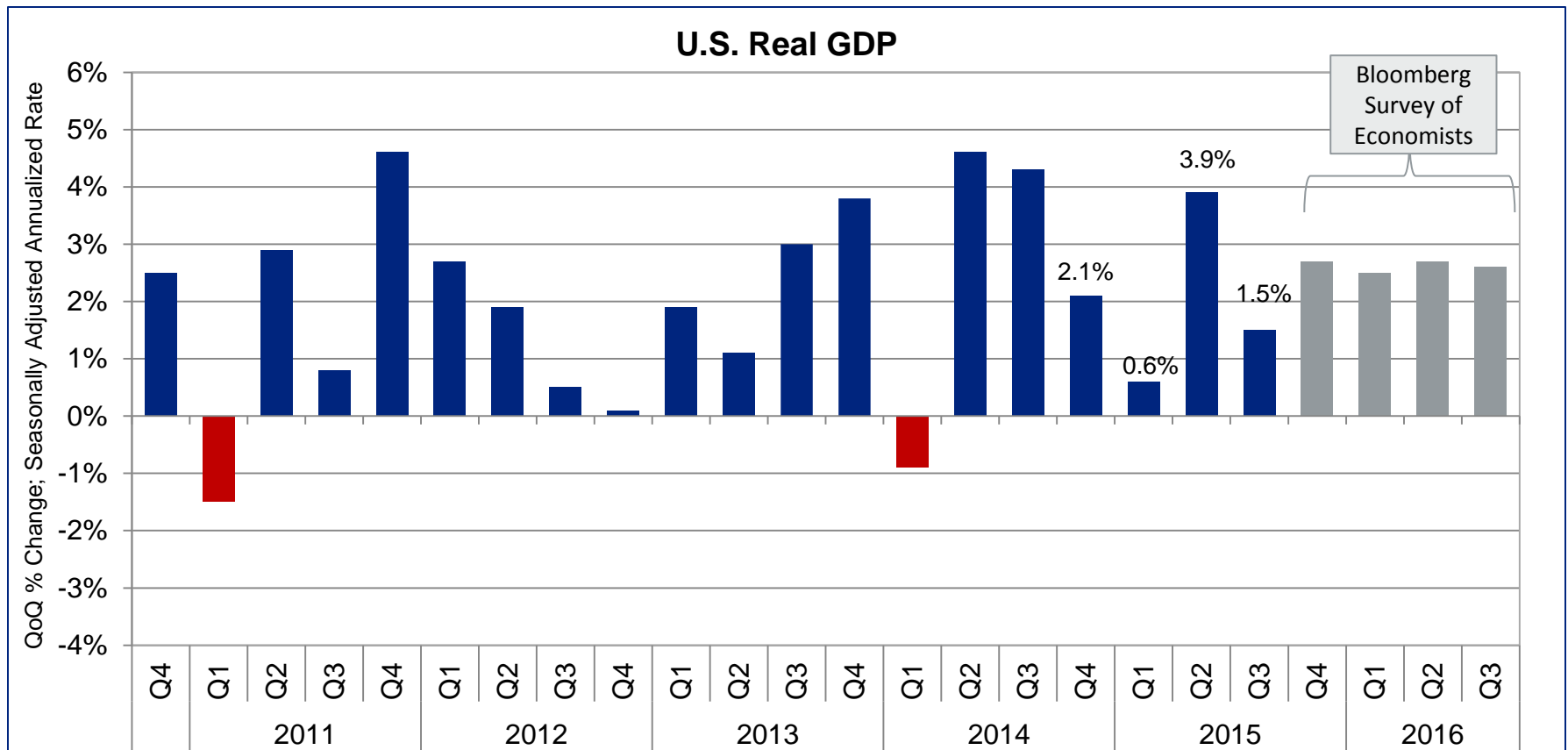
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# I. Market Update

# U.S. Economy Slows in the 3rd Quarter

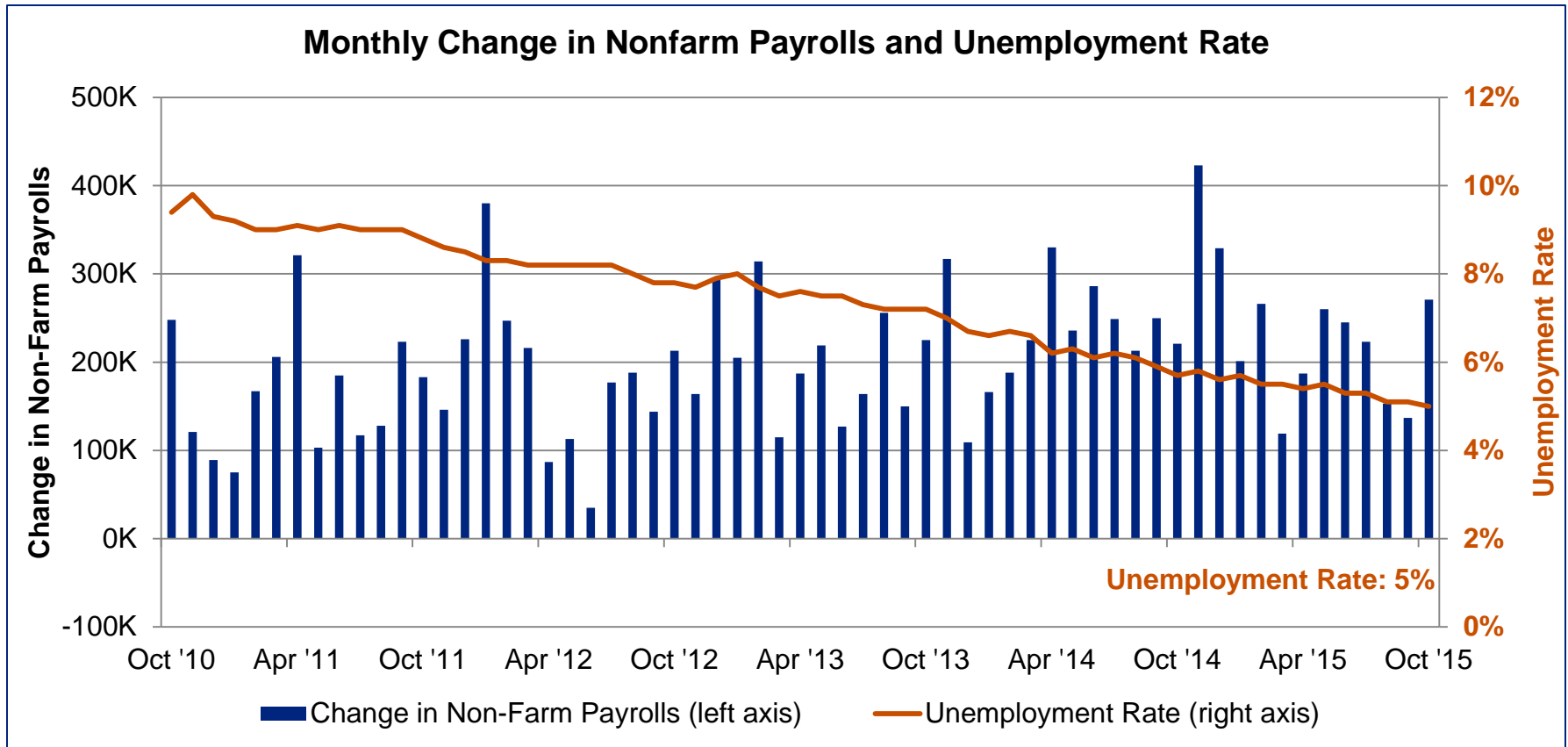
- U.S. GDP grew at a slower pace in the third quarter, growing at an estimated 1.5% according to the “advance” estimate released by the Bureau of Economic Analysis. Third quarter growth was led by gains in consumer spending, state and local government spending, and business investment in equipment, but was reduced by a large decline in inventories, which subtracted nearly 1.5% from Q3 GDP.



Source: Bureau Of Economic Analysis; Bloomberg survey results as of 10/31/2015.

# U.S. Job Creation Cools in Q3 and Rebounds

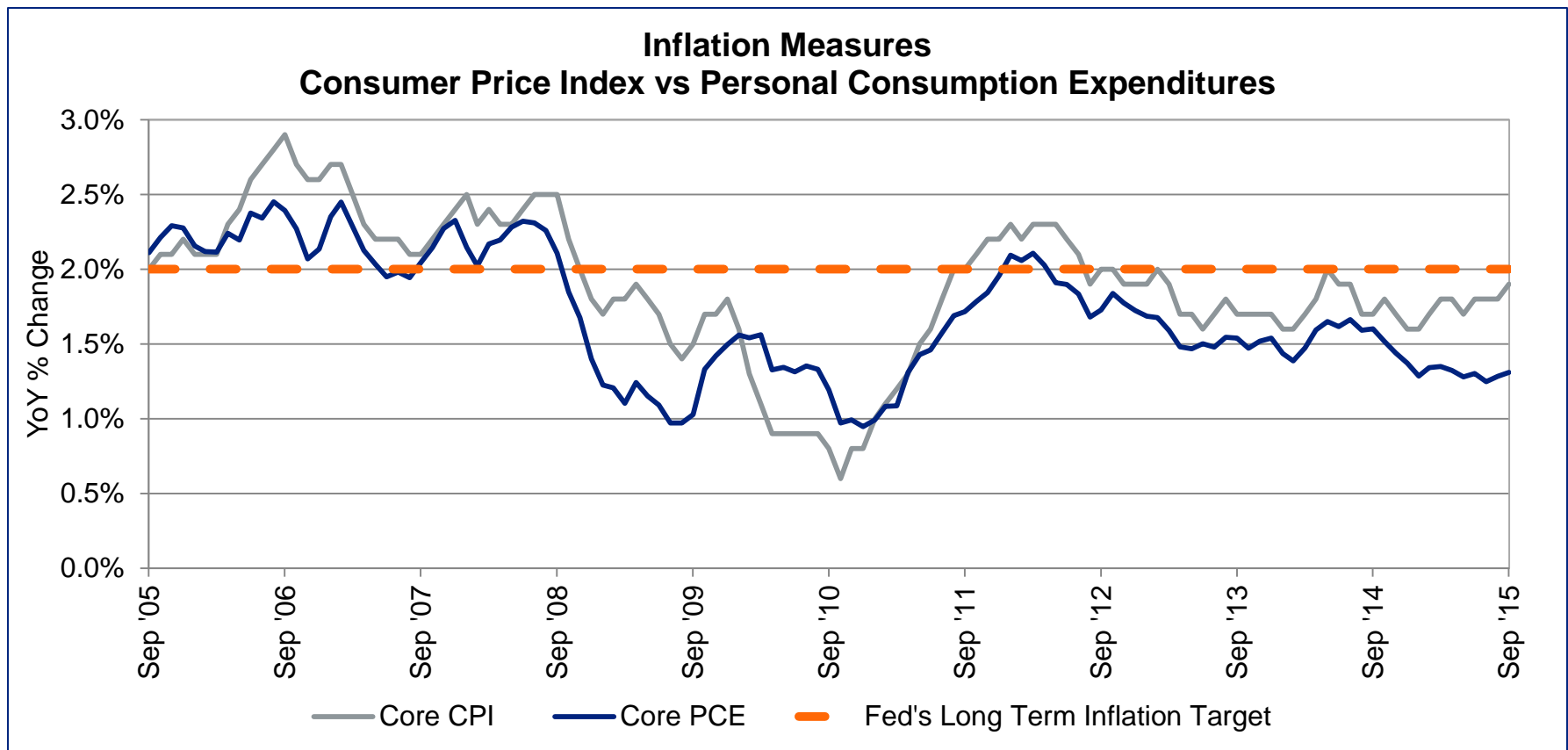
- U.S. Labor market added 275,000 jobs in October, well above the expectation for 185,000. The labor market shows signs of strength as average hourly earnings rose and labor market slack diminished.
- The unemployment rate fell to 5% as the labor force participation rate remained at its lowest level since 1977.



Source: Bureau of Labor Statistics

# Inflation Remains Muted

- The personal consumption expenditures (PCE) price index, the Fed's preferred gauge of core inflation, continues to undershoot the 2% target; it advanced just 1.3% year-over-year through September.
- Falling oil prices and lack of wage pressure are helping keep inflation low.

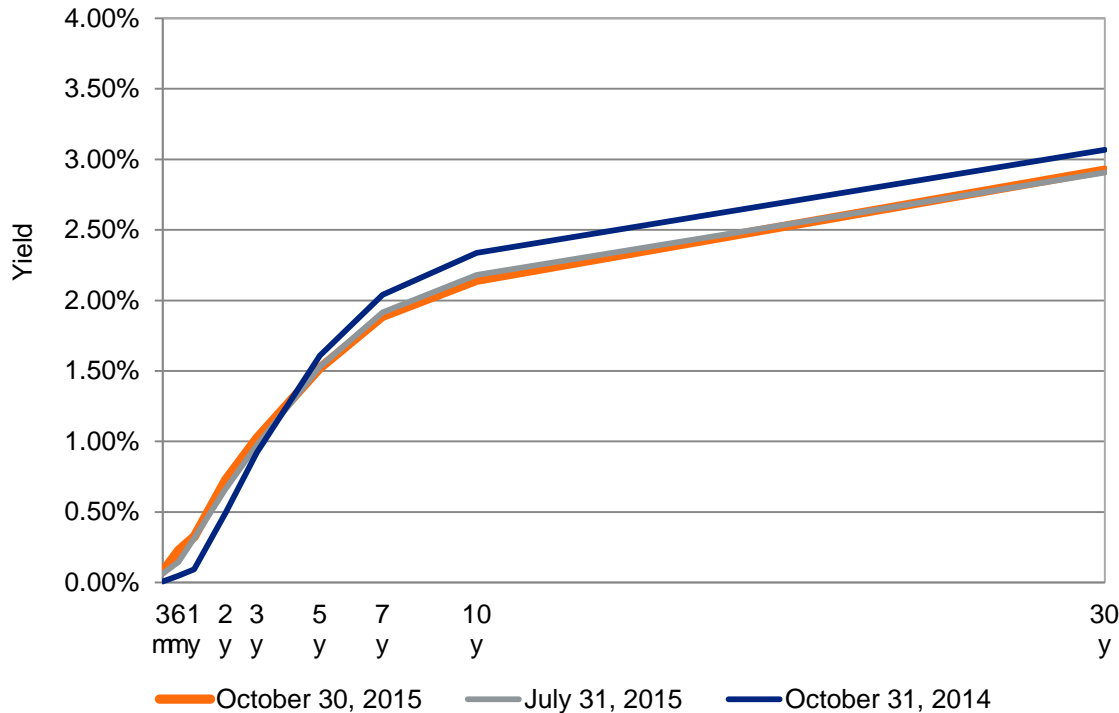


Source: Bloomberg

# U.S. Treasury Curve

- The yield curve flattened over the past three months as short-term yields rose in anticipation of a Fed rate hike; however, low inflation and growth expectations kept long-term yields subdued.

### U.S. Treasury Yield Curve

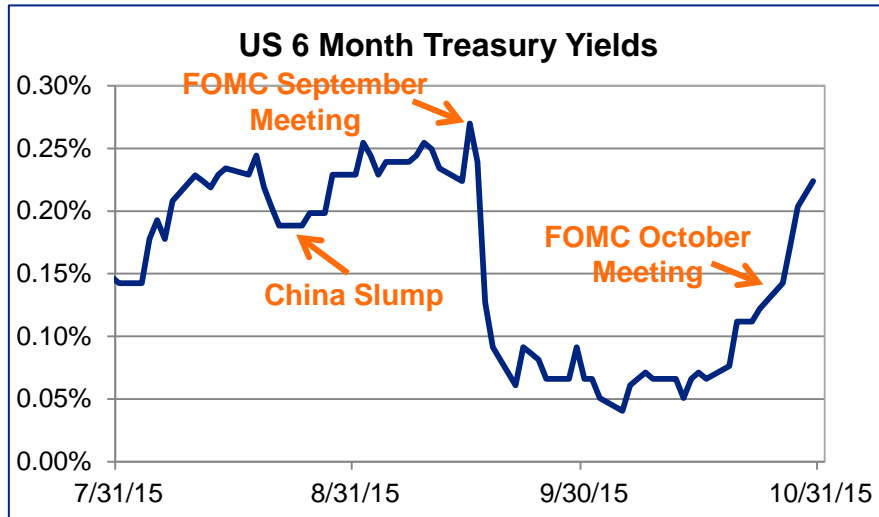


### Yield Curve History

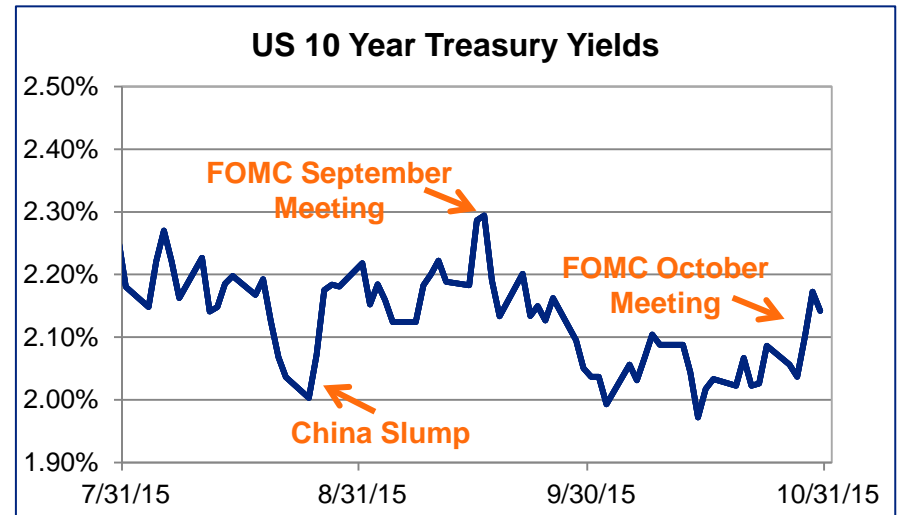
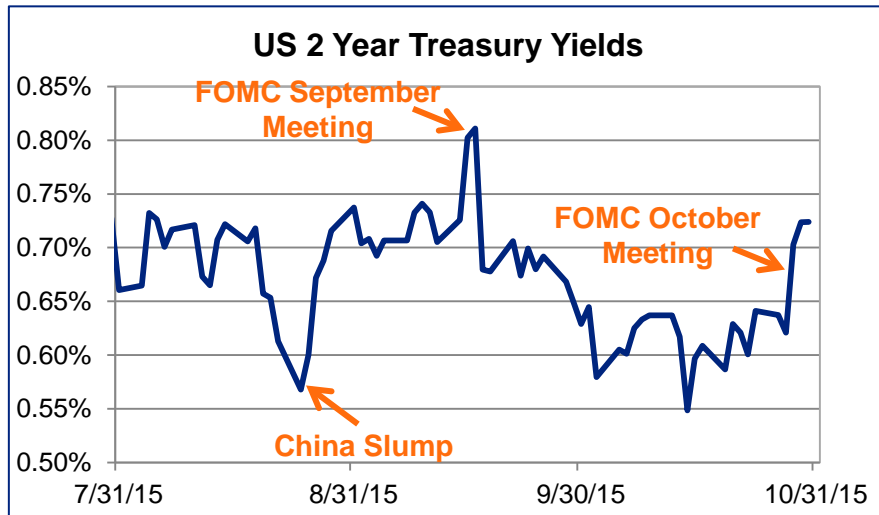
|        | 10/31/14 | 7/31/15 | 10/30/15 |
|--------|----------|---------|----------|
| 1-Mo.  | 0.00     | 0.03    | 0.01     |
| 3-Mo.  | 0.01     | 0.06    | 0.08     |
| 6-Mo.  | 0.05     | 0.15    | 0.23     |
| 1-Yr.  | 0.09     | 0.31    | 0.33     |
| 2-Yr.  | 0.49     | 0.66    | 0.73     |
| 3-Yr.  | 0.92     | 0.97    | 1.03     |
| 5-Yr.  | 1.61     | 1.53    | 1.52     |
| 7-Yr.  | 2.04     | 1.92    | 1.89     |
| 10-Yr. | 2.34     | 2.18    | 2.15     |
| 30-Yr. | 3.07     | 2.91    | 2.93     |

Source: Bloomberg

# Drivers of Yield Changes



- Yields rose across the curve following the October FOMC meeting in which the Federal Reserve signaled it remains prepared to raise interest rates as soon as December amid “moderate” economic growth in the US.
- Short and intermediate maturities were most impacted by changing FOMC expectations while longer maturities were driven more by global economic conditions.



Source: Bloomberg



# FOMC Statement Highlights

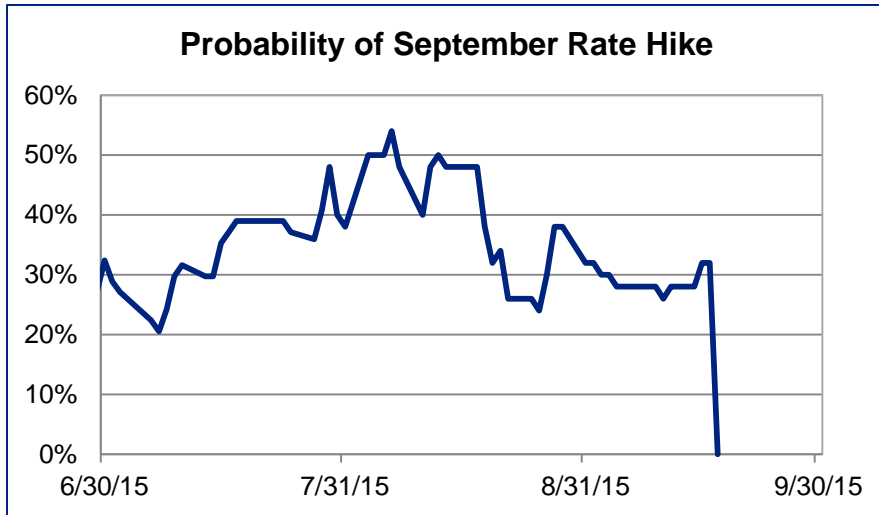
October

28

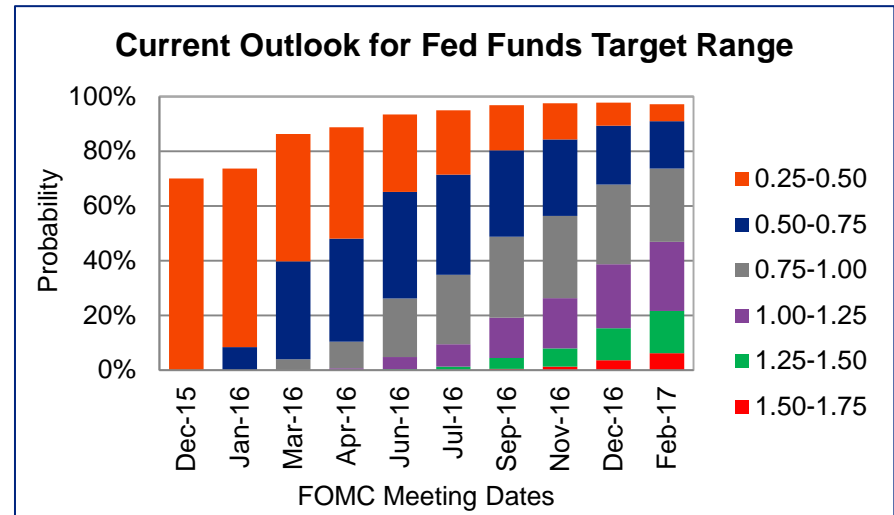
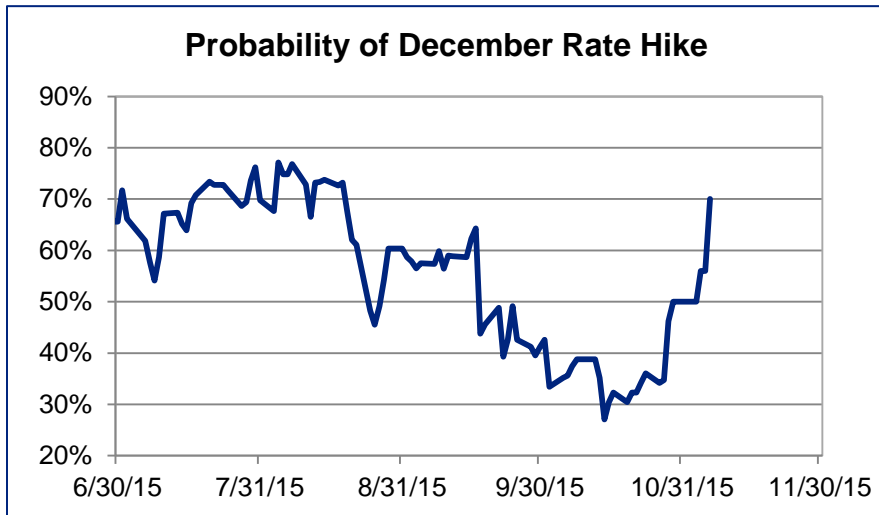
- Economic activity has been expanding at a moderate pace. Household spending and business fixed investment have been increasing at solid rates in recent months, and the housing sector has improved further... ***The pace of job gains slowed and the unemployment rate held steady.***
- ***Inflation has continued to run below the Committee's longer-run objective, partly reflecting declines in energy prices*** and in prices of non-energy imports... The Committee continues to see the risks to the outlook for economic activity and the labor market as nearly ***balanced but is monitoring global economic and financial developments.***
- The current 0 – 0.25% target range for the federal funds rate remains appropriate ...In determining whether it will be appropriate to raise the target range ***at its next meeting,*** the Committee will assess progress - ***both realized and expected*** - toward its objective of maximum employment at 2% inflation
- Committee anticipates that it will be ***appropriate to raise the target range for the federal funds rate*** when it has seen further improvements in the labor market and is ***reasonably confident that inflation will move back to its 2% objective over the medium term.***

Source: Federal Reserve.

# Outlook for the Fed Funds Target Rate



- Market expectations for a September hike fluctuated as participants digested the impact that deteriorating economic data would have on the FOMC's view of progress towards its goals.
- While investors are torn on the timing of an initial rate hike, the expectations for a December rate hike increased after the October FOMC meeting and strong October jobs report.



Source: Bloomberg, "Current Outlook" as of 11/6/15.

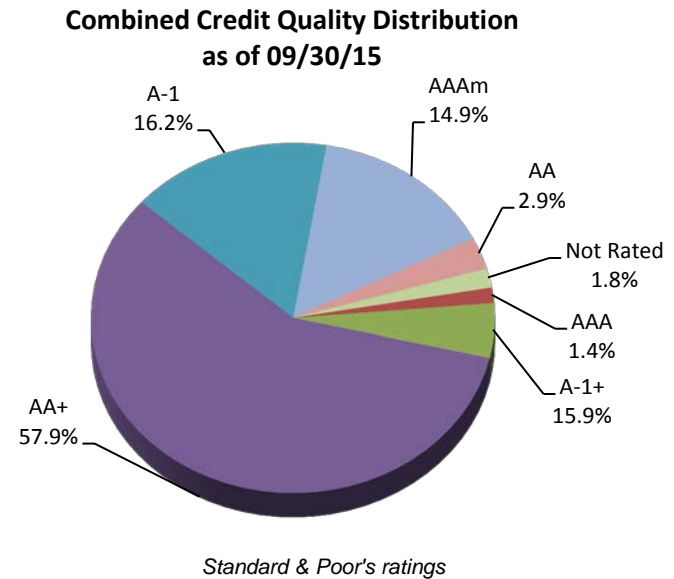
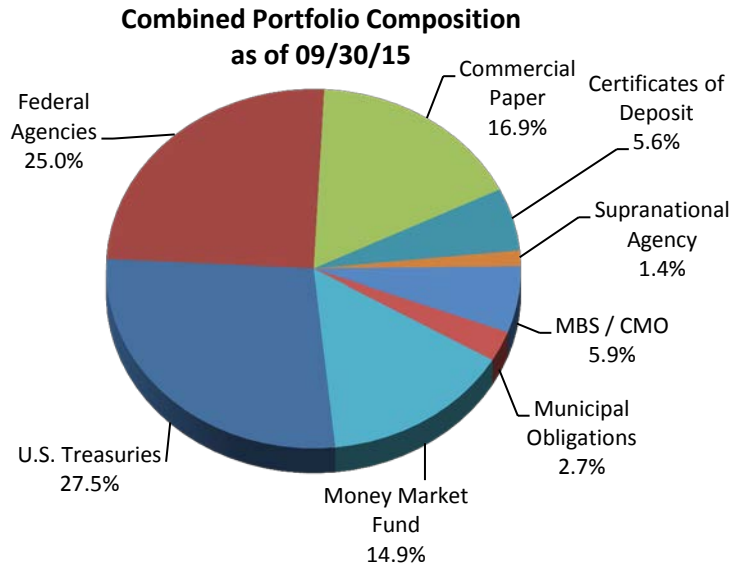
# Disclosures

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## II. Portfolio Review

# Combined Portfolio Characteristics

As of September 30, 2015



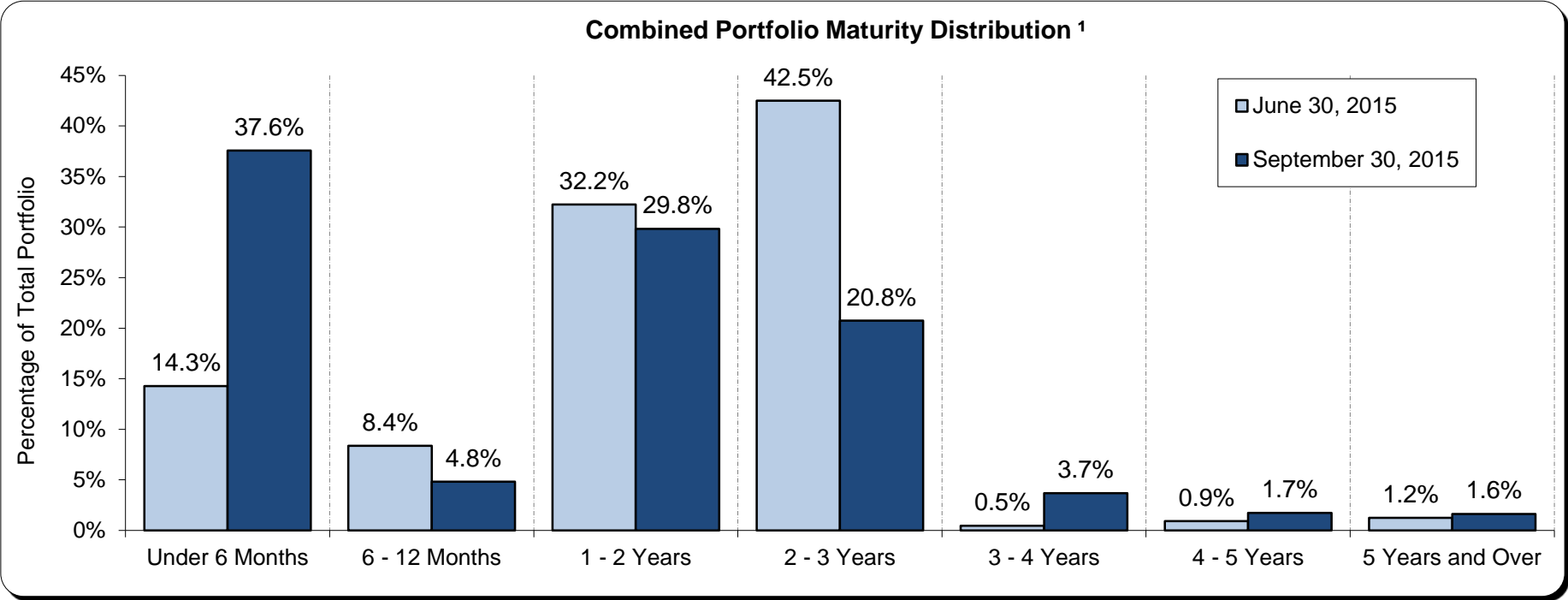
**Security Type**

**as of September 30, 2015**

|                         |                        |
|-------------------------|------------------------|
| U.S. Treasuries         | \$9,754,779.43         |
| Federal Agencies        | \$8,850,140.39         |
| Commercial Paper        | \$5,997,163.41         |
| Certificates of Deposit | \$2,002,529.96         |
| Supranational Agency    | \$503,378.50           |
| MBS / CMO               | \$2,102,630.77         |
| Municipal Obligations   | \$968,701.63           |
| Money Market Fund       | \$5,270,866.19         |
| <b>Total</b>            | <b>\$35,450,190.28</b> |

# Combined Portfolio Characteristics

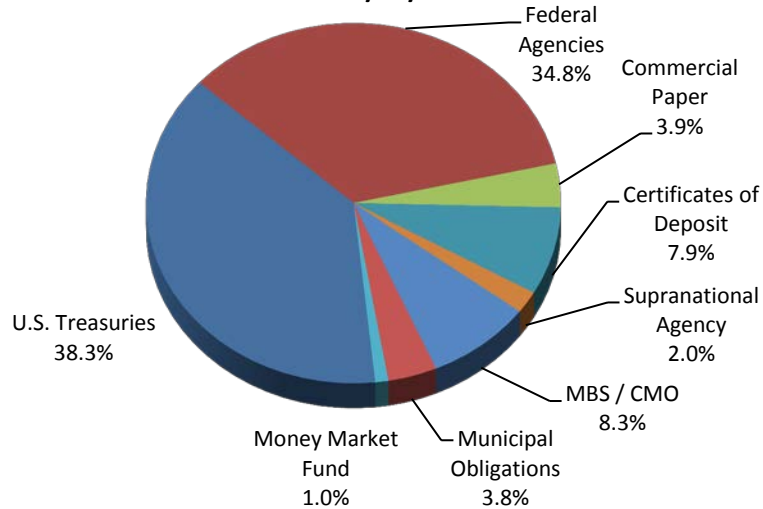
As of September 30, 2015



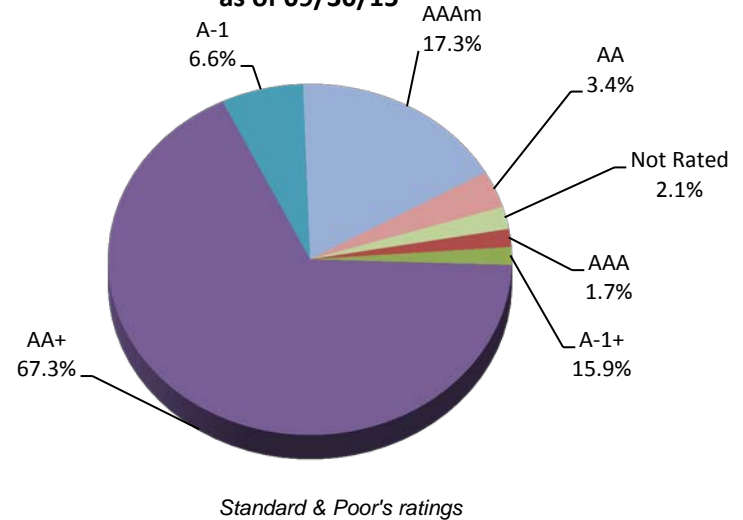
# Long-Term Portfolio Characteristics

As of September 30, 2015

Long-Term Portfolio Composition  
as of 09/30/15



Long-Term Credit Quality Distribution  
as of 09/30/15



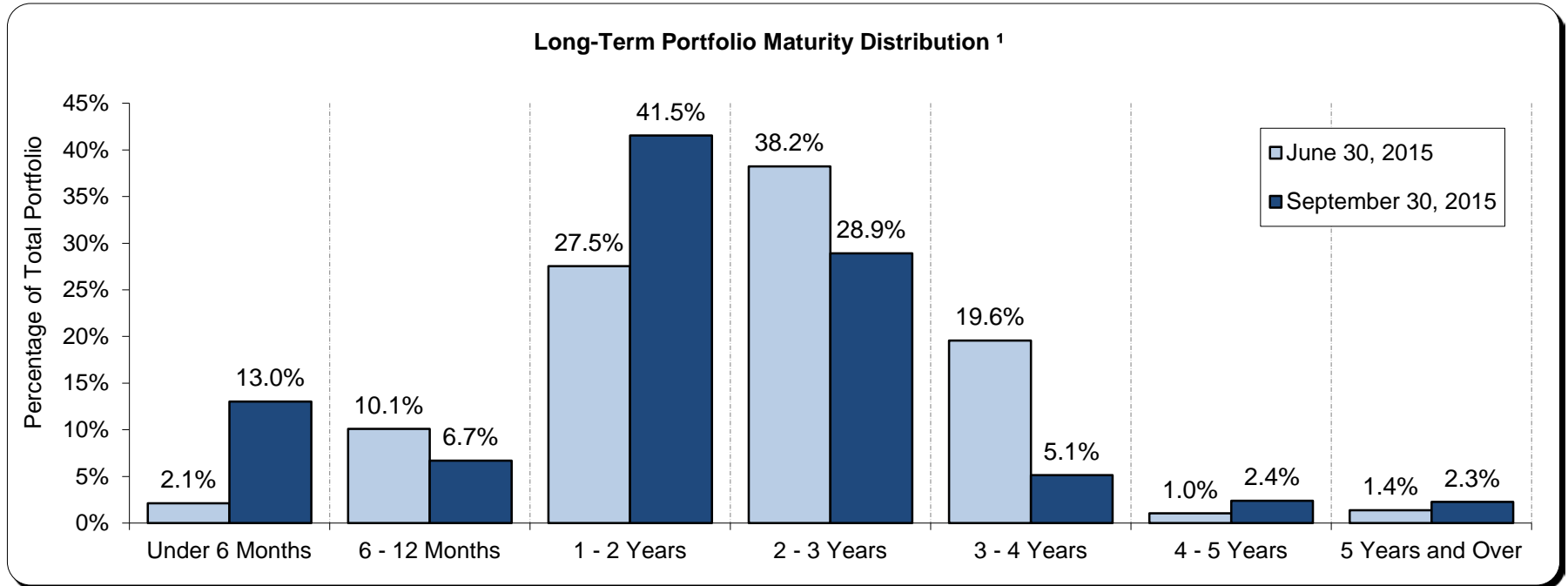
**Security Type<sup>1</sup>**

**September 30, 2015**

|                         |                        |
|-------------------------|------------------------|
| U.S. Treasuries         | \$9,754,779.43         |
| Federal Agencies        | \$8,850,140.39         |
| Commercial Paper        | \$999,673.50           |
| Certificates of Deposit | \$2,002,529.96         |
| Supranational Agency    | \$503,378.50           |
| MBS / CMO               | \$2,102,630.77         |
| Municipal Obligations   | \$968,701.63           |
| Money Market Fund       | \$259,820.86           |
| <b>Total</b>            | <b>\$25,441,655.04</b> |

# Long-Term Portfolio Characteristics

As of September 30, 2015

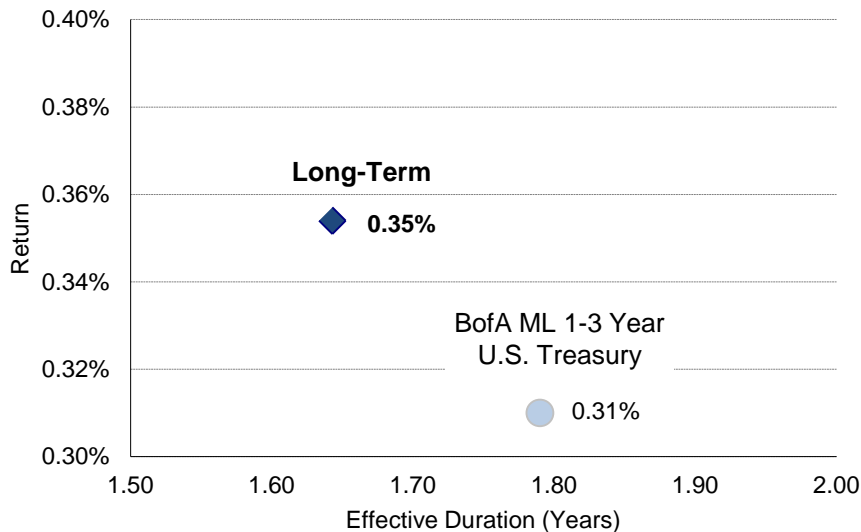




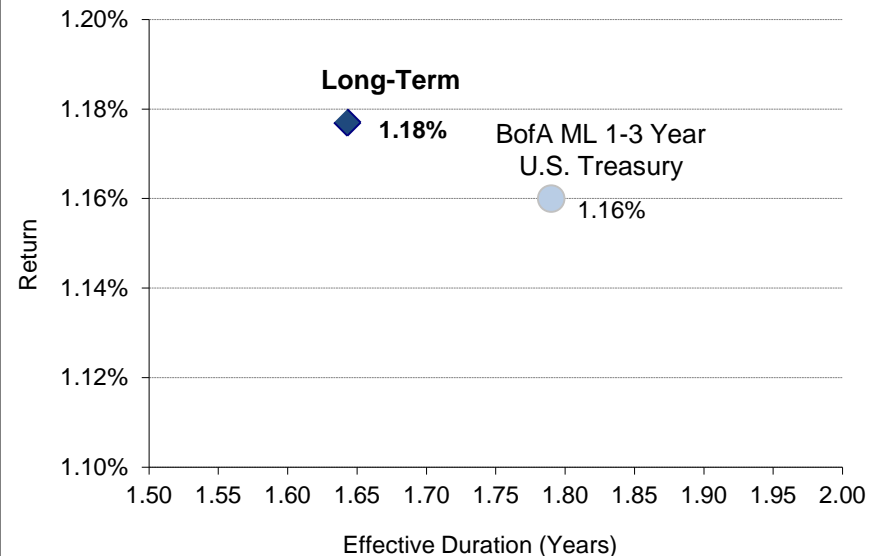
# Long-Term Portfolio Performance

| Long-Term Portfolio Performance      |                    |                      |              |                        |
|--------------------------------------|--------------------|----------------------|--------------|------------------------|
|                                      | Quarter Ended      | Annualized           | Trailing     | Since                  |
| Total Return <sup>1,2</sup>          | September 30, 2015 | Quarter <sup>3</sup> | 12 Months    | Inception <sup>4</sup> |
| <b>Long-Term</b>                     | <b>0.35%</b>       | <b>1.41%</b>         | <b>1.18%</b> | <b>1.18%</b>           |
| BofA ML 1-3 Year U.S. Treasury Index | 0.31%              | 1.24%                | 1.16%        | 1.16%                  |

**Quarter Total Return Comparison  
(Quarter Ended September 30, 2015)**



**Since Inception Total Return Comparison  
(As of September 30, 2015)**



1. Performance on trade-date basis, gross (i.e., before fees) in accordance with standards of the CFA Institute.

2. Bank of America/ Merrill Lynch Indices provided by Bloomberg Financial Markets.

3. Quarterly returns are presented on both an unannualized and annualized basis. The annualized return assumes the quarterly return is compounded at the same rate for four quarters and is presented for reference only. The actual annual return will be the result of chaining the most recent four quarterly returns.

4. Since inception return is the annualized return from the quarter ended 9/30/14 to 9/30/15

# Examples of Active Management

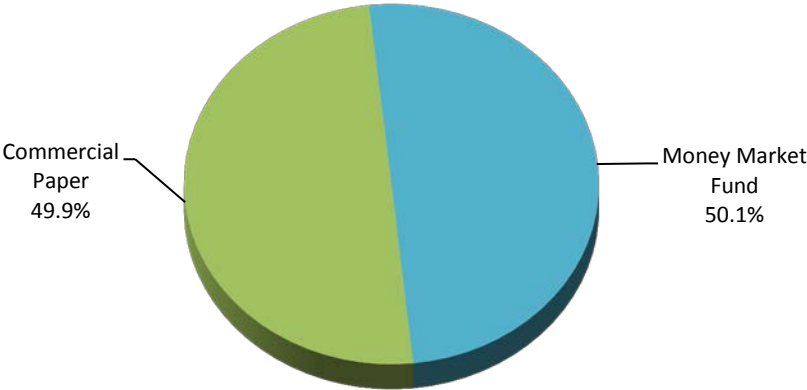
| Settle Date                | Trade Type | Security           | Par         | Maturity | Yield at Cost | Yield at Market                  | Total Trade Benefit |
|----------------------------|------------|--------------------|-------------|----------|---------------|----------------------------------|---------------------|
| 7/6/15                     | Purchase   | U.S. Treasury Note | \$1,300,000 | 7/31/18  | 1.11%         | 1.11%                            | -----               |
| 7/6/15                     | Sell       | FHLB Note          | \$665,000   | 9/28/16  | 0.61%         | 0.51%                            | \$4,616             |
| 7/6/15                     | Sell       | FHLMC Note         | \$625,000   | 8/25/16  | 0.60%         | 0.47%                            | \$4,732             |
| <b>Long Term Portfolio</b> |            |                    |             |          |               | <b>Additional Net Benefit to</b> |                     |
| <b>8/25/2016</b>           |            |                    |             |          |               | <b>\$9,348</b>                   |                     |

| Settle Date                | Trade Type | Security           | Par         | Maturity | Yield at Cost | Yield at Market                  | Total Trade Benefit |
|----------------------------|------------|--------------------|-------------|----------|---------------|----------------------------------|---------------------|
| 9/1/15                     | Purchase   | FNMA Note          | \$1,250,000 | 10/19/18 | 1.18%         | 1.18%                            | -----               |
| 9/1/15                     | Sell       | U.S. Treasury Note | \$1,000,000 | 7/31/18  | 1.11%         | 1.13%                            | \$4,473             |
| <b>Long Term Portfolio</b> |            |                    |             |          |               | <b>Additional Net Benefit to</b> |                     |
| <b>7/31/2018</b>           |            |                    |             |          |               | <b>\$4,473</b>                   |                     |

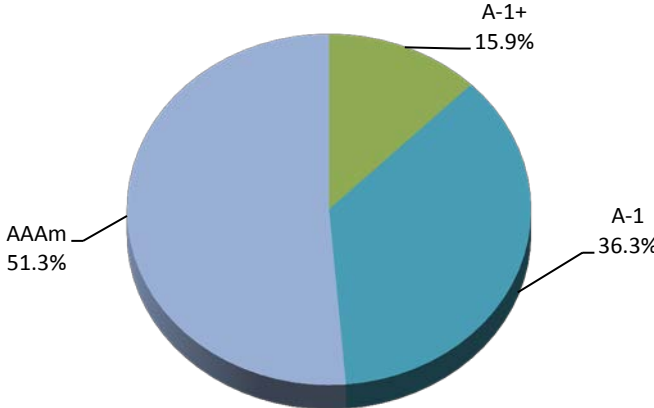
# Short-Term Portfolio Characteristics

As of September 30, 2015

Short-Term Portfolio Composition  
as of 09/30/15



Short-Term Credit Quality Distribution  
as of 09/30/15

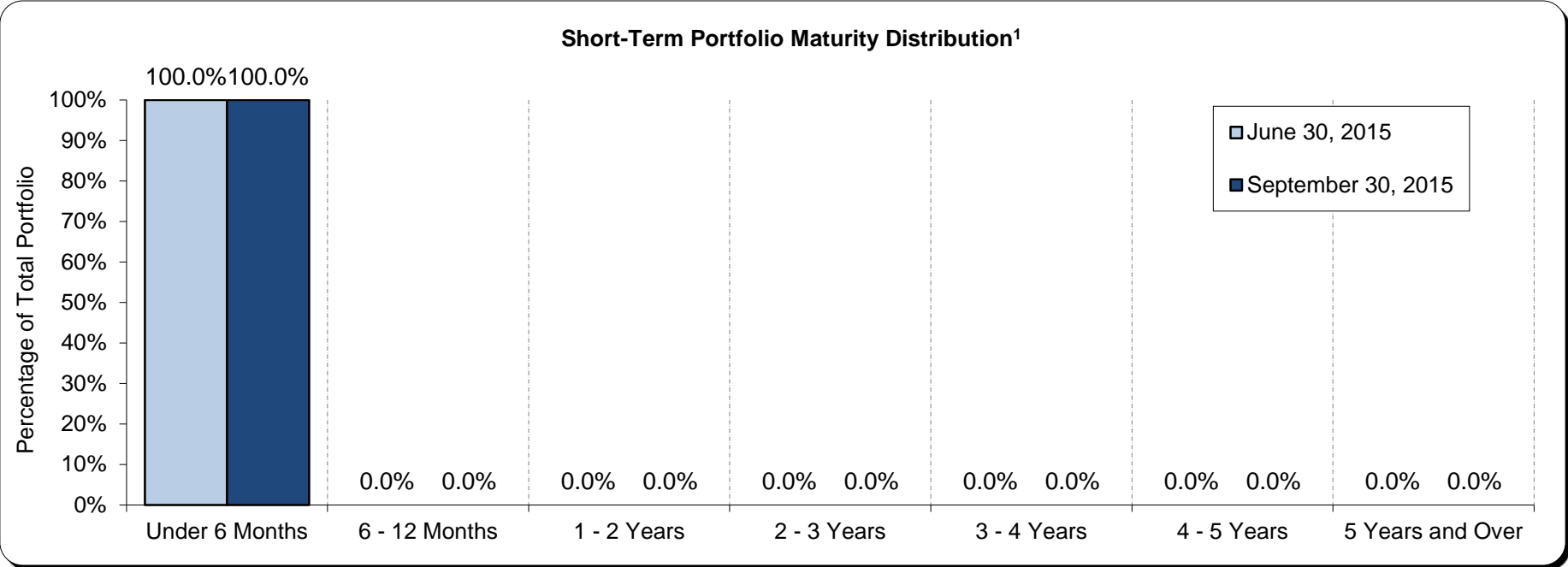


Standard & Poor's ratings

| <u>Security Type<sup>1</sup></u> | <u>September 30, 2015</u> |
|----------------------------------|---------------------------|
| Commercial Paper                 | \$4,997,489.91            |
| Money Market Fund                | \$5,011,045.33            |
| <b>Total</b>                     | <b>\$10,008,535.24</b>    |

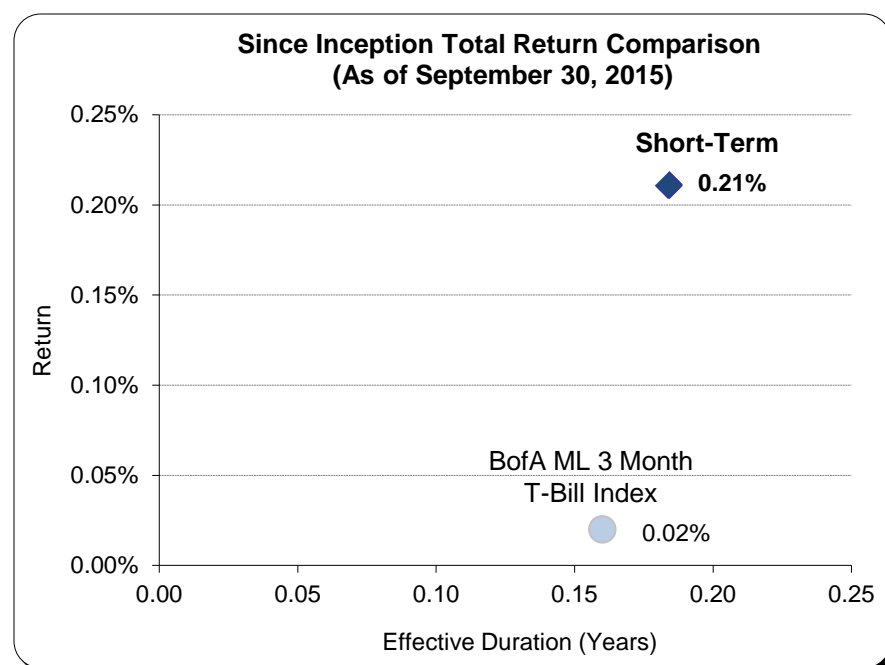
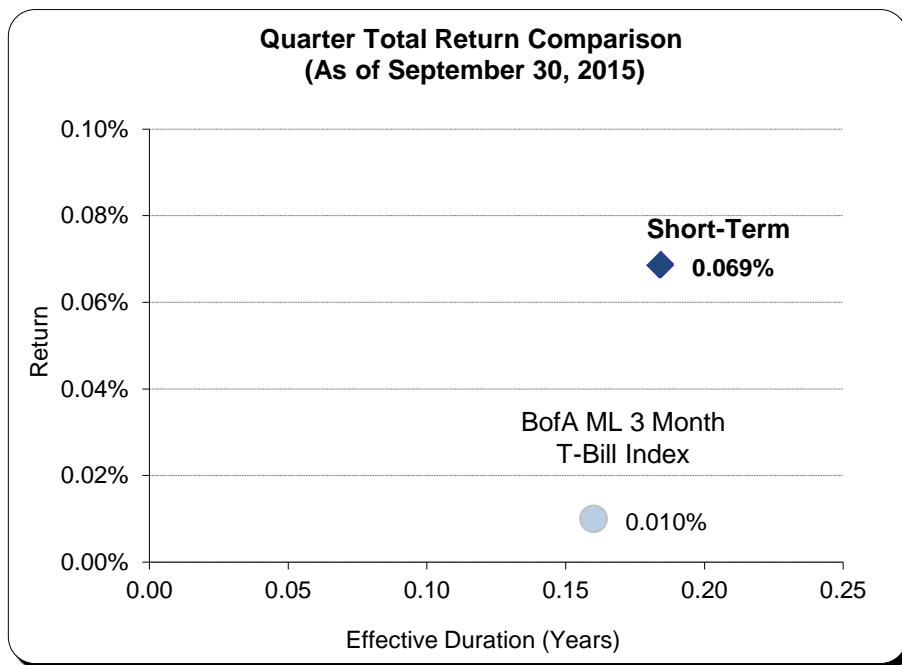
# Short-Term Portfolio Characteristics

As of September 30, 2015



# Short-Term Portfolio Performance

| Short-Term Portfolio Performance |                                     |                       |                    |
|----------------------------------|-------------------------------------|-----------------------|--------------------|
| Total Return <sup>1,2,3</sup>    | Quarter Ended<br>September 30, 2015 | Annualized<br>Quarter | Since<br>Inception |
| <b>Short-Term</b>                | <b>0.07%</b>                        | <b>0.27%</b>          | <b>0.21%</b>       |
| BofA ML 3 Month T-Bill Index     | 0.01%                               | 0.05%                 | 0.02%              |



1. Performance on trade-date basis, gross (i.e., before fees) in accordance with standards of the CFA Institute.

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