



Douglas La Follette, *Secretary of State*
Matt Adamczyk, *State Treasurer*
Brad D. Schimel, *Attorney General*

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Jonathan Barry, *Executive Secretary*

AGENDA

October 18, 2016

2:00 P.M.

Board of Commissioners of Public Lands
101 E. Wilson Street, 2nd Floor
Madison, Wisconsin

Routine Business:

- 1) Call to Order
- 2) Approve Minutes – October 4, 2016 (Attachment)
- 3) Approve Loans (Attachment)

Old Business:

None

New Business:

None

Routine Business:

- 4) Future Agenda Items
- 5) Executive Secretary's Report
 - BCPL Trust Fund Investment Report – 3rd Quarter 2016
 - Bond Activity Report
- 6) Adjourn

AUDIO ACCESS INFORMATION

Toll Free Number: **(888) 291-0079**
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**BOARD MEETING
OCTOBER 18, 2016**

**AGENDA ITEM 2
APPROVE MINUTES**

Attached for approval are the minutes from the October 4, 2016, board meeting.

Board Meeting Minutes
October 4, 2016

Present via teleconference were:

- | | |
|---|--|
| Doug La Follette, Commissioner | Secretary of State |
| Matt Adamczyk, Commissioner | State Treasurer |
| Brad Schimel, Board Chair | Attorney General |
| Jonathan Barry, Executive Secretary | Board of Commissioners of Public Lands |
| Tom German, Deputy Secretary | Board of Commissioners of Public Lands |
| Richard Sneider, Loan Analyst and
Chief Investment Officer | Board of Commissioners of Public Lands |
| Vicki Halverson, Office Manager | Board of Commissioners of Public Lands |

ITEM 1. CALL TO ORDER

Board Chair Schimel called the meeting to order at 2:47 p.m.

ITEM 2. APPROVE MINUTES – SEPTEMBER 20, 2016

MOTION: Commissioner La Follette moved to approve the minutes; Board Chair Schimel seconded the motion.

DISCUSSION: None.

VOTE: The motion passed 3-0.

ITEM 3. APPROVE LOANS

Executive Secretary Barry reported that the loans had been reviewed for proper public purpose.

<u>Municipality</u>	<u>Municipal Type</u>	<u>Loan Type</u>	<u>Loan Amount</u>
1. Brussels Door County Application #: 02017053 Purpose: Construct fire station/EMS building	Town Rate: 3.50% Term: 20 years	General Obligation	\$514,206.00
2. Clover Sanitary District #1 Bayfield County Application #: 02017059 Purpose: Finance sanitary system maintenance	Sanitary District Rate: 3.00% Term: 10 years	General Obligation	\$125,000.00
3. Freedom Outagamie County Application #: 02017051 Purpose: Finance road maintenance	Town Rate: 2.50% Term: 5 years	General Obligation	\$355,000.00
4. Hebron Jefferson County Application #: 02017057 Purpose: Finance road improvements	Town Rate: 2.50% Term: 2 years	General Obligation	\$120,000.00

5.	Lac La Belle Waukesha County Application #: 02017056 Purpose: Finance road repairs	Village Rate: 3.50% Term: 20 years	General Obligation	\$120,000.00
6.	Oneida Oneida County Application #: 02017058 Purpose: Finance economic development project	County Rate: 3.00% Term: 7 years	General Obligation	\$15,000,000.00
7.	Oregon Dane County Application #: 02017050 Purpose: Refinance fire/EMS building debt	Town Rate: 3.50% Term: 19 years	General Obligation	\$165,700.00
8.	Prairie Du Chien Crawford County Application #: 02017055 Purpose: Finance TID #5 developer incentive payment	City Rate: 2.50% Term: 2 years	General Obligation	\$350,000.00
9.	Saint Croix Central St Croix County Application #: 02017052 Purpose: Finance energy efficiency projects	School Rate: 2.50% Term: 5 years	General Obligation	\$2,000,000.00
10.	Viroqua Vernon County Application #: 02017054 Purpose: Finance TID # 6 economic development projects	City Rate: 3.50% Term: 14 years	General Obligation	\$700,000.00
TOTAL				\$19,449,906.00

MOTION: Board Chair Schimel moved to approve the loans; Commissioner La Follette seconded the motion.

DISCUSSION: None.

VOTE: The motion passed 2-1. Commissioner La Follette and Board Chair Schimel voted aye; Commissioner Adamczyk voted no.

ITEM 4. DISCUSS AND VOTE ON PROPOSED LAND BANK SALE – DOROTHY LAKE (\$1603)

Board Chair Schimel reported that staff had resolved a title conflict with the property and were recommending that the property, which is surrounded by DNR lands, be sold to the DNR.

MOTION: Board Chair Schimel moved to approve the land bank sale; Commissioner La Follette seconded the motion.

DISCUSSION: Executive Secretary Barry reported that an updated appraisal on the property resulted in an increased per acre value.

VOTE: The motion passed 3-0.

NOW, THEREFORE BE IT RESOLVED, that the Board of Commissioners of Public Lands approves the sale of the Property to the Wisconsin Department of Natural Resources at the price of Seventy-five Thousand Dollars (\$75,000) in accordance with Chapter 24 of the Wisconsin Statutes on such terms and conditions as the Executive Secretary determines to be reasonable and necessary. The Executive Secretary is authorized and directed to execute any documents reasonably necessary to complete such transaction.

ITEM 5. FUTURE AGENDA ITEMS

None.

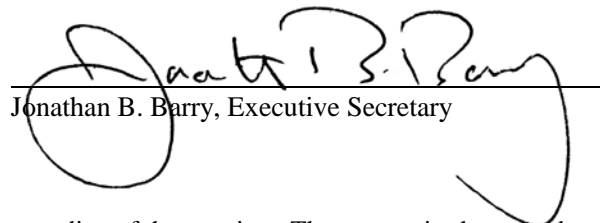
ITEM 6. EXECUTIVE SECRETARY'S REPORT

Executive Secretary Barry said the Oneida County economic development loan approved by the Board would, according to the Oneida County Economic Development Corporation, help to preserve 524 existing jobs and add 20 new jobs, with more jobs anticipated in the future. He stated that he would keep the Board informed about any additional information regarding the loan and the project as it may become available.

ITEM 7. ADJOURN

MOTION: Commissioner La Follette moved to adjourn the meeting; Commissioner Adamczyk seconded the motion.

The meeting adjourned at approximately 2:55 p.m.



Jonathan B. Barry, Executive Secretary

These minutes have been prepared from a recording of the meeting. The summaries have not been transcribed verbatim. Link to audio recording: ftp://doafpt1380.wi.gov/doadocs/BCPL/2016-10-04_BCPL-BoardMtgRecording.mp3

**BOARD MEETING
OCTOBER 18, 2016**

**AGENDA ITEM 3
APPROVE LOANS**

<u>Municipality</u>	<u>Municipal Type</u>	<u>Loan Type</u>	<u>Loan Amount</u>
1. Clark Clark County Application #: 02017065 Purpose: Finance 2017 road construction	County Rate: 2.50% Term: 2 years	General Obligation	\$1,550,000.00
2. Ellsworth Pierce County Application #: 02017062 Purpose: Finance economic development projects in TID #8	Village Rate: 3.00% Term: 10 years	General Obligation	\$80,000.00
3. Gardner Door County Application #: 02017063 Purpose: Construct fire station	Town Rate: 3.50% Term: 20 years	General Obligation	\$1,359,781.00
4. Germantown Washington County Application #: 02017061 Purpose: Finance school construction and capital projects	School Rate: 3.00% Term: 10 years	General Obligation	\$800,000.00
5. Hobart Brown County Application #: 02017060 Purpose: Finance TID #1 development incentives	Village Rate: 3.50% Term: 20 years	General Obligation	\$1,500,000.00
6. Owen-Withee Clark and Taylor Counties Application #: 02017064 Purpose: Finance public works project	School Rate: 3.00% Term: 10 years	General Obligation	\$1,750,000.00
TOTAL			\$7,039,781.00

**BOARD MEETING
OCTOBER 18, 2016**

**AGENDA ITEM 5
EXECUTIVE SECRETARY'S REPORT**

Attached for review are the following reports:

- BCPL Trust Fund Investment Report – 3rd Quarter 2016
- Bond Activity Report – October 12, 2016

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BCPL Trust Fund Investment Management

Investment Report - Third Quarter 2016

Executive Summary

BCPL investment performance continues to exceed benchmark returns. After adjusting returns for differences in both credit quality and average maturity, the BCPL-managed portfolios had a yield that was 1.13% greater than our benchmark. This difference in yield means that beneficiaries earned \$3 million more than would have been generated by an investment in the benchmark portfolio during the third quarter. This investment performance equates to nearly \$12 million in annualized interest earnings above benchmark returns, which can be attributed to the BCPL asset management team.

Unrealized gains in the bond portfolio totaled \$21.7 million at the end of the third quarter, an increase of 4.6% above the initial cost of these investments.

After postponing bond acquisitions during the record low interest rate environment experienced since June, staff took advantage of the recent increase in the interest rates and purchased a \$33.35 million participation in a pool of Taxable Revenue Anticipation Notes (TRANs) issued by a group of Wisconsin School Districts. This investment has been assigned a MIG1 credit rating by Moody's, the highest available rating for short-term issues.

Q3 Investment Highlights and Outlook

The benchmark 10 year Treasury fell to a record low yield of 1.32% at the beginning of the quarter, and has since recovered to around 1.75%. Interest rate volatility remains high, with global economic uncertainty and the flow of international funds into U.S. Treasuries providing a counterbalance to rate pressures from modest growth in the U.S. economy. Staff believes that rates will continue trending slowly higher, with short-term rates leading the way.

Loan demand is strong and relative yields on the loan portfolio remain excellent.

In this continued period of low interest rates, it has been difficult for staff to find good value in the marketplace. One exception has been in Tax Revenue Anticipation Notes (TRANs), which are taxable promissory notes issued by Wisconsin School District to smooth out district revenue streams over their fiscal year. In prior years, BCPL has had success in purchasing TRANs issued by individual school districts. This year, we were able to purchase a \$33.35 million participation (partial interest) in a pool of TRANs issued by a group of seven school districts. The credit of this investment is generally superior to TRANs issued by individual districts, which is why this issue received the highest credit rating available. The average interest rate is well above the comparable rates for short-term Treasuries and the State Investment Fund. As this investment matures over the next 3-12 months, staff anticipates a better possibility of long-term investment.

Summary and Benchmark Comparison

The overall expected yield of funds managed by BCPL was 3.21% at the end of third quarter, a decrease from the prior quarter that was anticipated with lower market interest rates.

The best measure for comparing investment performance against our benchmark is the SEC yield, which provides a standard methodology that is available for the mutual funds and bond market indexes that comprise our benchmark. Adjustments to account for our better average credit rating and longer maturity increase the BCPL yield to 1.13 % greater than benchmark returns.

BCPL Investment Summary

3rd Quarter 2016

as of September 30, 2016

Portfolio Summary	Total Assets	Expected Yield ¹	SEC Yield ²	Average Credit Quality ³	Weighted Avg Maturity	
Total BCPL Managed Financial Assets	\$ 1,060,401,968	3.21%	3.06%	Aa1	8.37	
Benchmark Performance ⁴			2.53%	A1	8.78	
BCPL Investments						
	% of Total BCPL Managed Assets					
Bonds	38.75%	\$ 410,887,885	4.36%	3.99%	Aa2	16.22
BCPL State Trust Fund Loans	37.47%	\$ 397,373,638	3.75%	3.75%	Aa1	5.45
Cash and Cash Equivalents ⁵	23.78%	\$ 252,140,444	0.48%	0.48%	Aaa	0.17
Total BCPL Managed Investments	100.00%	\$ 1,060,401,968	3.21%	3.06%	Aa1	8.37
Benchmark Components						
	Weighting					
S&P Long Intermediate Term Taxable Municipal Bond Index ⁶	60.00%		2.83%	3.37%	Aa2	9.92
S&P U.S. Treasury Bill Index ⁷	10.00%		0.24%	0.24%	Aaa	0.25
Wisconsin Tax-Exempt Bond Mutual Funds (combined) ⁸	30.00%	\$ 394,900,001	N/A	1.60%	Baa2	9.34
Total Benchmark	100.00%			2.53%	A1	8.78
Important Notes on Following Page						
Prepared by Richard Sneider						

Notes to BCPL Benchmark Comparison:

¹ **Expected Yield** is the weighted average yield to the redemption date for each bond, and assumes that issuers will redeem bonds at the earliest possible date, when it is in their best interest given current market interest rates. Also called 'yield-to-worst', this number is equal to the lower of the 'yield to call' and 'yield to maturity' for each investment in the portfolio.

² **SEC Yield** - The SEC yield should not be confused with the expected yield on invested funds. The SEC yield will vary substantially with market conditions because it is calculated using the current market value of assets, and the value of fixed income assets fluctuates with market interest rates. For example, although interest payments produced by an individual bond remain constant following the issuance of the bond, the SEC yield on this bond will increase with market interest rates solely because the value of the bond decreases (yield = income/value). If all bonds are held to maturity, the actual return to the investor would equal the "yield to maturity at cost". This calculation is not provided for benchmark components and is therefore not included in this comparison. Many investors prefer to use "yield to worst", which calculates the return using the lower of the "yield to call" and "yield to maturity". The most appropriate method to compare bond portfolios is to look at Total Return, which combines both income and changes in the market value of the underlying assets (see note 8 below). BCPL does not have the ability to use Total Return as a method of comparison because the Trust Fund Loan Portfolio has never been valued. Rather, the SEC Yield is used for comparison because it is a standardized methodology for calculating yield as required by the Securities and Exchange Commission for all mutual funds and provides a means to compare BCPL managed funds to a simple benchmark. The SEC yield is a close approximation to the net yield to maturity of the fund using the current market value of the fund, and is calculated as the yield to the investor (after fund expenses and fees) during the previous 30 days assuming all bonds are held to maturity. The SEC Yield for the State Investment Fund is for the most recent month available.

³ **Average Credit Quality** - Except for the BCPL loan portfolio, all average credit quality ratings shown equal the weighted average credit rating of individual securities held within each portfolio. A rating for the loan portfolio is provided to improve the ability to compare BCPL managed funds to other funds. The Aa1 rating presumed for the loan portfolio is considered reasonable, as there has not been a single default in the State Trust Fund loan program since inception in 1871, and BCPL has the statutory right and requirement to cure any future default by intercepting state aid otherwise due the borrower. Mutual Fund credit quality is provided by Morningstar. The global long-term rating scale of Moody's Investor Services begins at 'Aaa' for obligations judged to be of the highest quality, subject to the lowest level of risk. The ranking in order from highest to lowest quality then includes: Aa, A, Baa, Ba, B, Caa, Ca, and C. Ratings from Aa to Caa are modified with 1,2, or 3 to provide a high, middle and low ranking within each alphabetic category. 'Investment-grade' securities have ratings of Baa3 or higher.

⁴ **Benchmark Components and Weighting** - Due to the unique set of BCPL authorized investments consisting primarily of the BCPL State Trust Fund Loan Program, and bonds issued by the State of Wisconsin and Wisconsin municipalities and school districts, there are no managed funds that perfectly match the characteristics of the BCPL portfolio. However, the chosen benchmark components provide the best opportunity to compare BCPL investments to funds managed by other professionals. The justifications of including individual benchmark components are provided below. Component weighting begins with an estimate of average liquidity levels required throughout the year, with additional factors including an estimate of the proportion between taxable and tax-exempt project funding, and the use of current taxable and tax-exempt bond yields in developing program interest rates.

⁵ **Cash** - Cash and cash equivalents includes all investments in the State Investment Fund and Farm Credit adjustable rate notes, and all funds managed by ADM in FDIC-insured deposit accounts.

⁶ **S&P Long Intermediate Term Taxable Municipal Bond Index** - This taxable municipal bond index is included as a benchmark component because it properly reflects the investment strategies of BCPL managed Trust Funds, including both the direct investment in taxable municipal bonds and the influence of taxable bond yields on the development of loan program interest rates. The S&P Long Intermediate Term Taxable Municipal Bond Index matches the weighted average maturity and duration of total BCPL managed funds fairly well, although BCPL maintains better average credit quality. This index is comprised of all taxable bonds issued by any state (including the Commonwealth of Puerto Rico and U.S. territories such as the U.S. Virgin Islands and Guam) with an investment grade rating (minimum S&P BBB- or Moody's Baa3), a minimum par amount of \$1 million, and remaining maturity between 5 and 15 years. Average credit quality level is not published by S&P, but was calculated at the weighted average rating of amounts held within the separate S&P AAA, AA, A, and BBB Rated Taxable Municipal Bond Indices using a formula developed by Schwab Portfolio Center, the portfolio analysis software used by BCPL. Overall, a weighting of 60% is appropriate given the average levels of cash and tax-exempt investments held by the Trust Funds throughout the year.

⁷ **S&P U.S. Treasury Bill Index** - The U.S. Treasury Bill Index represents the average cash position held by the Trust Funds throughout the year, and is included because BCPL maintains significant levels of liquidity needed to fund expected trust fund loan demand over the next 3-6 months. The amount of portfolio liquidity (cash) varies significantly throughout the year, and is impacted by factors including the interest rate environment, the absence of prepayment penalties within the loan program, and the statutory payment structure requiring annual loan payments on March 15 each year. The S&P U.S Treasury Bill index is a market weighted index that includes all U.S. Treasury Bills with maturities ranging from 0-12 months. Because an index is not a managed portfolio, but only a collection of securities within a specific set of criteria, management expenses are not included. Overall, a weighting of 10% for this benchmark component is appropriate given the average levels of cash held by the Trust Funds throughout the year.

⁸ **Wisconsin Tax-Exempt Bond Funds** - Tax-exempt bond funds are included as a benchmark component for three reasons: BCPL invests directly in tax-exempt bonds when available at acceptable terms; a significant portion of loans made through the BCPL State Trust Fund Loan Program fund projects that would qualify as tax-exempt; and current tax-exempt bond yields are an important factor in the construction of loan program interest rates. There are three bond mutual funds that invest primarily in Wisconsin State and Municipal Bonds, investments that are similar to the securities approved for BCPL investment. These funds are sponsored by Wells Fargo, Nuveen and Nationwide Ziegler, and there are significant differences between the management of these mutual funds and BCPL trust funds. All three mutual funds are limited to tax-exempt investments, a universe of securities that generally provide lower yields than the taxable instruments favored by BCPL. On the other hand, all three of these funds invest substantial amounts in bonds that have considerable default risk including bonds issued by the Commonwealth of Puerto Rico, community development revenue bonds, hospital revenue bonds, and other bonds types not available within the risk parameters of the BCPL investment authority. Overall, a weighting of 30% for this benchmark component is appropriate given the level of Trust Fund investment in tax-exempt instruments and the influence of tax-exempt bond rates on the interest rates charged within the loan program.

⁹ **Total Return Analysis** - A total return analysis including the periodic change in asset values in addition to earnings would provide a more comprehensive and accurate comparison between the returns generated by BCPL managed funds and our benchmark. However, total return analysis requires accurate asset valuation in order to provide a reasonable basis for measuring management performance. A significant portion of BCPL managed assets are invested in loans to municipalities and school districts through the BCPL State Trust Fund Loan Program. BCPL has never sold a trust fund loan and has always held these investments to maturity. There is currently no formula or model available to determine an accurate market value of the loan portfolio. Should BCPL sell loans in the future and establish a secondary market in BCPL State Trust Fund Loans, total return analysis may provide an improvement over the current method of yield comparison as the model for measuring BCPL investment performance against the appropriate benchmarks.

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Bond Activity Report October 12, 2016

Bond Purchases

Issuer	Credit Rating	Trade Date	Par Value	Price Paid	Coupon	Call Date	Yield to Call	Maturity Date	Yield to Maturity
Wis SD TRANS	MIG1	10/11	\$1,800,000	\$1,803,060	1.50%	n/a	n/a	2/23/17	1.00%
Wis SD TRANS	MIG1	10/11	\$3,650,000	\$3,660,877	1.50%	n/a	n/a	7/21/17	1.10%
Wis SD TRANS	MIG1	10/11	\$7,600,000	\$7,624,472	1.50%	n/a	n/a	9/25/17	1.15%
Wis SD TRANS	MIG1	10/11	\$20,300,000	\$20,360,088	1.50%	n/a	n/a	10/20/17	1.20%

These Tax Revenue Anticipation Notes (TRANS) are rated MIG1 by Moody's, which is the highest rating available for short term Notes. This rating is equivalent to the 'Aaa' rating issued for longer term issues.

In prior years, BCPL has purchased TRANS issued by individual school districts. This investment is a purchase of a participation (partial interest) in TRANS issued by school districts including Waunakee, Verona, Sun Prairie, Nekoosa, Monona Grove, Merrill and Baraboo. Security includes a pledge of tax revenues and state aids to be received by each of the districts. The credit of this participation is generally superior to TRANS issued by individual districts, which is why this issue received the highest possible credit rating.

Bond Sales

Staff has not sold any bonds since the prior bond activity report.

Current Holdings

Combined Trust Fund Bond Portfolios Current Holdings as of October 12, 2016

Investment Type	
Wisconsin State General Obligation Bonds	\$118,493,413
Wisconsin State Revenue Bonds	\$46,522,378
Wisconsin Center District Bonds	\$35,000,000
Municipal General Obligation Bonds	\$142,952,307
Municipal Revenue Bonds	\$42,076,891
Farm Credit Bonds	\$99,622,156
Total Bond Investments (at cost)	\$484,667,145
(at market value)	<u>\$503,391,261</u>
Dollar Gain	\$18,447,694