# ANNUAL INVESTMENT REPORT

FOR THE FISCAL YEAR ENDED
SEPTEMBER 30, 2010

PREPARED BY
BOB INZER
CLERK OF COURTS

LEON COUNTY, FLORIDA

**ANNUAL INVESTMENT REPORT**
Fiscal Year Ended September 30, 2010
Leon County, Florida

# EXECUTIVE SUMMARY

The County's investment Portfolio continued to perform generally, as expected. The Commission approved Investment Policy provides for a very conservatively managed portfolio. Policy controls related to portfolio duration, credit quality, liquidity and instrument selection effectively eliminates both the upside and downside surprises with respect to investment returns.

The portfolio earned $4,988,617 of interest and realized gains of $836,219 for total income of $5,824,836 for the fiscal year ended September 30, 2010. This total income provided an effective rate of return of 2.48% on an average daily balance of $235,249,514 in the fiscal year 2010. During this fiscal year the Federal Funds Rate ranged between 0.00 % and 0.25% and is expected to remain at this level for the foreseeable future. As a result of the low interest rates, the County's average portfolio return for Fiscal Year 2010 decreased from 3% to 2.48%.

Section 218.415(15), Florida Statutes requires Leon County Clerk of Courts to provide an annual report to the Board of County Commissioners of the securities in the portfolio by investment type, book value, market value and income earned. This information included below in Table I is as of September 30, 2010.

**Table I Portfolio Ending Balance and Total Income Earned**
**Fiscal Year Ended September 30, 2010**

| Investment Type | Book Value | Market Value | Realized G/L | Interest | Total Income |
|---|---|---|---|---|---|
| Cutwater Asset Mgmt | 72,602,433 | 73,052,293 | 836,219 | 2,138,101 | 2,974,320 |
| Fl Municipal Investment Trust 0-2 | 14,935,622 | 14,935,622 | | 301,319 | 301,319 |
| FL Municipal Investment Trust 1-3 | 40,420,085 | 40,420,085 | | 808,982 | 808,982 |
| Fl Local Govt Investment Trust | 38,162,936 | 38,162,936 | | 821,321 | 821,321 |
| Fl State Treasury SPIA | 33,421,313 | 34,116,476 | | 902,714 | 902,714 |
| Wachovia Cash | 12,418,466 | 12,418,466 | | 16,179 | 16,179 |
| **Total Cash and Investments** | **$211,960,855** | **$213,105,878** | **$836,219** | **$4,988,617** | **$5,824,836** |

**Table II Average Daily Balance and Total Return**
**Fiscal Year Ended September 30**

| Investment Type | FY 2009 Ave Daily Balance | Total Return | FY 2010 Ave Daily Balance | Total Return |
|---|---|---|---|---|
| Cutwater Portfolio Manager Account | 69,894,730 | 7.21% | 71,831,468 | 3.52% |
| Fla Municipal Investment Trust 1-3 YRS | 13,419,127 | 5.59% | 35,905,623 | 2.14% |
| Fla Municipal Investment Trust 0-2 YRS | 1,405,791 | 1.89% | 32,442,441 | 0.81% |
| Florida Local Gov Investment Trust | 10,079,565 | 3.76% | 29,494,884 | 2.84% |
| Certificates of Deposit | 26,244,586 | 2.47% | 4,328,767 | 0.83% |
| Florida Treasury SPIA | 41,062,565 | 2.43% | 44,528,085 | 2.54% |
| Money Market-Various | 52,271,096 | 0.75% | 2,907,342 | 0.05% |
| Wachovia Cash Pool | 13,213,180 | 0.53% | 13,810,904 | 0.40% |
| **Total Daily Average** | **$226,017,965** | | **$235,249,514** | |
| **Table I Income/ Table II Ave. Daily Bal)** | | **3%** | | **2.48%** |

**ANNUAL INVESTMENT REPORT**
Fiscal Year Ended September 30, 2010
Leon County, Florida

## Investment Oversight Committee

The Board of County Commissioners in their Investment Policy provides for an Investment Oversight Committee to work with the Clerk of the Court in the investment of the portfolio. The Committee meets quarterly unless interim issues require more frequent meetings. Meetings are noticed; open to the public and minutes of each meeting recorded. The IOC consists of the Clerk; the County Administrator Designee, Assistant County Administrator Alan Rosenzweig; and three qualified individuals with financial or investment expertise who are independent of employment and business relationships with Leon County. They are Stan Barnes, Managing Partner, Allen Mooney & Barnes Investment Advisors, LLC, Marvin M. Garland, EVP and COO Leverage, the LSCU Service Corporation, and Dr. John Lawrence, retired Public Administrator. Effective July 13, 2010, Michael Kramer, COO of Desloge Home Oxygen, was appointed by the Board to replace Dr. John Lawrence when his term expired.

Since there was little change in the markets, the Investment Oversight Committee approved only minor changes after its annual review of County's Investment Policy on August 11, 2010. Although the intent of the policy was to limit to 15% the investment in any government pool, changes were made to clarify that the limit of 15 % applies to each pool within FMIT. The policy authorizes changes in investment percentages from time to time based on market conditions. Detail was added to describe the approval procedures and removed the 5 day limit for investment of bond proceeds in excess of limit.

The revised policy was adopted by the Board on September 14, 2010. The portfolio has been managed within these guidelines and limitations of the Investment Oversight Committee recommendations and the Commission approved policy without exception.

## Economy

During the September 21, 2010 meeting of the Federal Open Market Committee, FOMC reviewed information which indicated that the pace of recovery in output and employment had slowed in recent months. The minutes from the meeting indicate that the Committee voted to maintain the target range for the federal funds rate at 0 to 1/4 percent and continues to anticipate that economic conditions, are likely to warrant exceptionally low levels for the federal funds rate for an extended period. The Committee also will maintain its existing policy of reinvesting principal payments from its securities holdings.

The Committee reported that it will continue to monitor the economic outlook and financial developments and is prepared to provide additional accommodation if needed to support the economic recovery and to return inflation, over time, to levels consistent with its mandate.

## Investment Managers

The investment portfolio end of month balances ranged from $149.4 million to $239 million during the year, with higher balances during the winter as taxes are received from the Leon County Tax Collector. The portfolio was allocated among the following government pools: Florida Treasury Special Purpose Investment Account, Florida Local Government Investment Trust (FLGIT) and the Florida Municipal Investment Trust (FMIvT). The external manager from October through April 2010 was the Royal Bank of Canada Global Asset Management, who invested 30% of the portfolio in slightly longer term investments.

**ANNUAL INVESTMENT REPORT**
Fiscal Year Ended September 30, 2010
Leon County, Florida

The Clerk of the Circuit Court in his capacity as the Chief Financial Officer of the County issued its Request for Proposal for Investment Management Services on January 4, 2010 to solicit proposals to serve as the County's external investment advisor. The responses to the RFP were evaluated by a committee in order to identify the top four proposals. The Investment Oversight Committee convened to interview the top candidates. Cutwater Asset Management's proposal was selected by the IOC as the most favorable proposal submitted. The Clerk entered into a contract with Cutwater Asset management effective May 20, 2010.

Currently, the dollars under management by Cutwater are approximately $73,000,000. Intermediate fixed income portfolios have durations of 1.5-1.8 years. The established benchmark for Cutwater is the Merrill Lynch 1-3 year Government Index.

The Clerk established its banking relationships pursuant to a competitive selection process. During the year, the investment option added in the prior fiscal year that required the bank to invest each night excess funds in Government Municipal Money Market fund was discontinued because the rates deteriorated to less than the rates earned on the checking account.

**ANNUAL INVESTMENT REPORT**
Fiscal Year Ended September 30, 2010
Leon County, Florida

## TABLE OF CONTENTS

**ANNUAL INVESTMENT REPORT**
Fiscal Year Ended September 30, 2010
Leon County, Florida

## I. INVESTMENT POLICY

Section 218.415, Florida Statutes provides units of local government the ability to adopt a written investment plan to govern the investment of their investment portfolio. The Leon County Board of County Commissioners on September 17, 2002 adopted an investment policy. It provides for among other things, an annual report to be presented to the Board of County Commissioners. On September 14, 2010 the Board adopted revisions to the Policy to provide the flexibility to manage the portfolio in the volatile market environment. The portfolio has been managed within the guidelines and limitations of the Investment Oversight Committee recommendations and Commission approved policy without exception.

The Florida Constitution provides that the Clerk of the Court will be responsible for the investment of County funds and this report is being submitted by the Clerk as provided by the Board's Investment Policy. All investment activity is conducted in accordance with written procedures and internal controls.

## II. INVESTMENT OVERSIGHT COMMITTEE

The Investment Oversight Committee (IOC) was established by the Leon County Clerk of Courts (Clerk) to formulate investment strategies, provide short-range direction and monitor the performance and structure of the County's portfolio. The IOC consists of the Clerk; the County Administrator Designee, Assistant County Administrator Alan Rosenzweig; and three qualified individuals with financial or investment expertise who are independent of employment and business relationships with Leon County. During most of the fiscal year the IOC was comprised of Stan Barnes, Managing Partner, Allen Mooney & Barnes Investment Advisors, LLC, Marvin M. Garland, EVP and COO Leverage, the LSCU Service Corporation, and Dr. John Lawrence, retired Public Administrator. Effective July 13, 2010, Michael Kramer, COO of Desloge Home Oxygen, was appointed by the Board to replace Dr. John Lawrence as his term ended.

## III. ACTIVITIES OF THE INVESTMENT OVERSIGHT COMMITTEE

The Investment Oversight Committee (IOC) scheduled periodic meetings to discuss issues relating to the investments of the County. Since there was little change in the markets, the Investment Oversight Committee approved only minor changes after its annual review of County's Investment Policy. The revised policy was adopted by the Board on September 14, 2010.

The Clerk of the Circuit Court in his capacity as the Chief Financial Officer of the County issued its Request for Proposal for Investment Management Services on January 4, 2010 to solicit proposals to serve as the County's external investment advisor. The responses to the RFP were evaluated by a committee in order to identify the top four proposals. The Investment Oversight Committee convened to interview the top candidates. Cutwater Asset Management's proposal was selected by the IOC as the most favorable proposal submitted. The Clerk entered into a contract with Cutwater Asset management effective May 20, 2010.

## IV. INVESTMENT OBJECTIVES

The Policy states that the primary objectives of all investment activities for the County should be safety of principal, maintenance of adequate liquidity and finally, return maximization.

Safety of principal is the foremost investment objective. Investment transactions should seek to keep capital losses to a minimum, whether the result of security defaults or erosion of market value. This is best insured by establishing minimum acceptable credit ratings, limiting the portfolio's overall duration, setting maximum exposures by sector, defining appropriate levels of diversification and authorized transactions and limiting exceptions.

The second objective is the provision of sufficient liquidity. A portion of the County's overall portfolio should be maintained very liquid in order to meet operating, payroll and ongoing capital requirements. Maintaining a core level of assets with the government pools such as the Treasury Special Purpose Investment Account (SPIA) or other short-term entities is viewed as the best way of maintaining secure asset values with sound investment practices. The remainder of the overall portfolio should be managed in such a manner that funds can be liquidated in a reasonable amount of time, recognizing that there are other sources for day-to-day liquidity and that this portfolio is primarily available for income generation within the constraints of this policy.

**Maximizing yield on the portfolio is of least importance compared to the safety and liquidity objectives above.** Return maximization is to be guided by the predefined and acceptable levels of risk as defined in this policy.

## V. PORTFOLIO PERFORMANCE

The portfolio earned $4,988,617 of interest and realized gains of $836,219 for total income of $5,824,836 for the fiscal year ended September 30, 2010. This total income provided an effective rate of return of 2.48% on an average daily balance of $235,249,514 in the fiscal year 2010. Acceptable portfolio performance is the result of balancing the rewards of investing, or the income earned, with the risks associated with those investments. Factors influencing the portfolio's performance are the types of permitted investments and allowable maturities, liquidity requirements, overall interest rate environment, cash flows, and the investment manager's performance.

For comparison, the portfolio earned $6,328,767 in interest and realized gains of $501,540 for total income of $6,830,307 for the fiscal year ended September 30, 2009, for an effective rate of return of 3% on an average daily balance of $227,590,639 in the fiscal year 2009. The effective rate of return for fiscal year 2010 is lower than that for fiscal year 2009 because the interest rates were higher during the first quarter of 2009.

# ANNUAL INVESTMENT REPORT

Fiscal Year Ended September 30, 2010
Leon County, Florida

The Following is an Overall Market and Portfolio Specific Commentary Provided by the County's Investment Advisor Cutwater Asset Management, Inc.

Leon County's investment portfolio managed by Cutwater effective May 20, 2010, outperformed its comparative benchmark, the Merrill Lynch 1-3 Year Government Index, for the fiscal year ending September 30, 2010. The external portfolio produced a total return, net of fees, of 1.44% compared to the Index return of 1.06%, which includes no fee charges.

**Third Quarter 2010 Review**

The market continued to question the conflicting relationship between US interest rates and growth expectations during the third quarter. Most analysts predict positive but below-trend economic growth for the foreseeable future, but US and industrialized world fiscal deficits, real estate valuations and high unemployment remain critical issues that will likely dampen growth during the recovery. Yet recovery in our opinion is becoming increasingly sustainable and the economic data, though volatile, supports this thesis. US private sector payroll growth, a component of the headline payroll statistic, continued its positive trend. The ISM Survey numbers for both Manufacturing and Non-Manufacturing remain above 50, suggestive of continued positive growth. In a typical recovery environment of more constructive labor markets, we would expect a more hawkish tone from the Federal Reserve resulting in rising short-term interest rates.

Yields in global bond markets are indicating that this is not a normal recovery and that this recovery is likely to be slower and longer than history would suggest. US ten-year yields grinded lower during the quarter to 2.51 percent. This represents the fifth consecutive month that yields on the ten-year have declined. Two-year notes also penetrated the key resistance level of 0.50 percent to end the quarter at an all-time low of 0.42 percent. The differential between ten-year and two-year yields does characteristically indicate an eventual recovery, but the historically low absolute yields on these risk-free investments continue to confound conventional market theory.

Key drivers of this inconsistency remain strong global bond flows and disinflation. Consider that equity valuations will generally reflect growth expectations and that an aging baby boomer population has been burned twice by stocks in the last decade and is becoming increasingly risk averse. Additionally, liquidity in the capital markets and historically low borrowing rates have translated into significantly improved corporate credit fundamentals making corporate bonds the sector of choice for investors. Twelve months through July, bond mutual funds have averaged inflows of $25 billion per month while equity and money market funds have averaged outflows of $6.1 billion and $65.8 billion per month respectively (Ned Davis Research, Inc., Fund Flows by Asset Class).

Perhaps even more significant and more apparent recently has been the impact of declining inflation and inflation expectations on Treasury yields. Chairman Bernanke in his recent FOMC statement shifted his stance on inflation from "…likely to remain subdued for some time…" to inflation being "…at levels somewhat below those the Committee judges most consistent, over the long run...". Five-year inflation breakevens, or the rate of inflation expected by the market, plummeted to 1.28 percent from a peak of 2.05 percent as recently as April. This acknowledgement by the Federal Reserve possibly opens the door for further quantitative easing despite the economic statistics predicting recovery and the political pressures associated with government debt expansion.

For the quarter, the Barclay's Aggregate Index provided another 2.48 percent of positive total return and is now up over 7.94 percent year to date. Comparatively, the S&P 500 Index has gained only 3.89 percent for the year, even after a strong September. Within the fixed income sectors, commercial mortgage backed securitizations continued to outperform all sectors with over 12.22 percent of excess return over Treasuries. High yield and investment grade sectors also rebounded during the third quarter while agency mortgage backed (Fannie Mae and Freddie Mac) lagged as prepayment model adjustments extended the index beyond previous expectations.

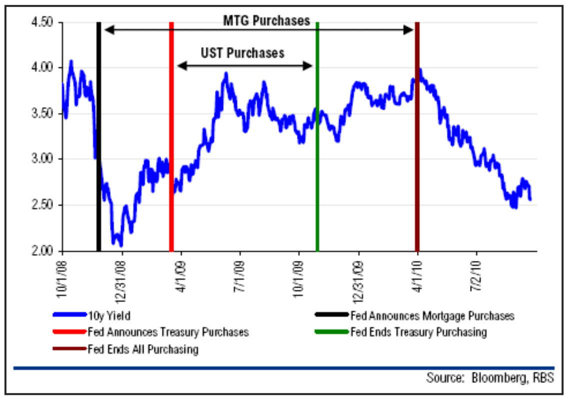



**Figure 1. Ten Year Treasury Yields and Quantitative Easing**

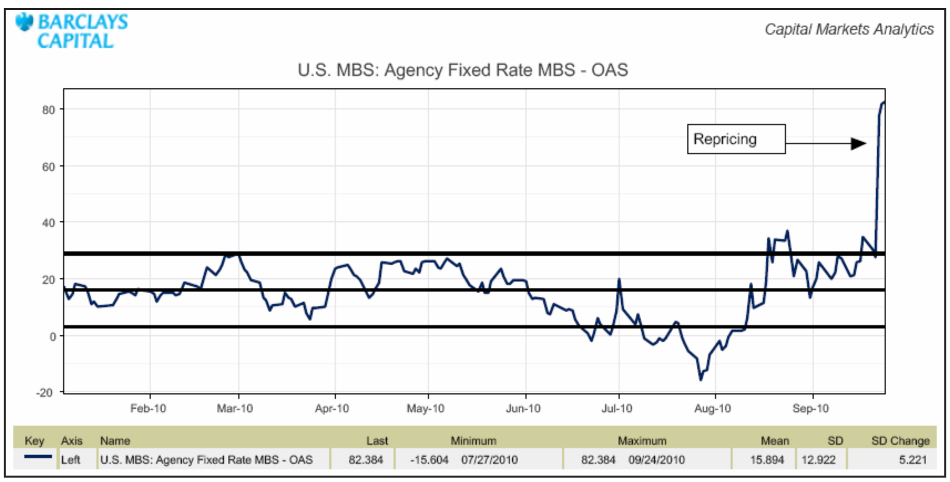



**Figure 2. Agency Mortgage Re-pricing**

## Fourth Quarter and Beyond Outlook

In the near term we expect continued price appreciation in most fixed income sectors and risk-free assets. The Federal Reserve has likely tipped its hand and is prepared to implement a new round of quantitative easing should economic data slow. The anticipated result would be temporarily lower Treasury yields or, at minimum, sustained yields at these depressed levels. It also appears that the recovery phase of this growth cycle will last longer than anticipated. The Federal Reserve appears less likely to change the Fed Funds rate until late 2011 as growth and inflation remain subdued.

Importantly, extending duration or "reaching for yield" in non-Treasury fixed income sectors is not a proposition that should be taken lightly. As we have argued in several preceding quarterly and website commentaries, our long-term outlook calls for an environment of higher interest rates. Any whiff of inflation or stronger economic data will likely reverse the trend of significantly lower yields. In either scenario, it will be difficult for the Federal Reserve to keep long-term rates depressed for long as bond investors are keen to the Treasury's significant refinancing needs. Alternatively, equity investors are becoming increasingly impatient as corporate balance sheets are flush with cash. Microsoft, by example, recently issued $4.75 billion in debt to repurchase stock. We predict that similar shareholder-friendly transactions are likely for other investment grade companies, which would be a leveraging event for credit that weakens credit fundamentals at the margin.

While our "check-mark" shaped recovery thesis appears sustainable, the challenge for the remainder of 2010 and beyond is to identify those leading indicators that will eventually predict an acceleration of growth and higher interest rates. The Federal Reserve has changed their view on inflation and we would expect monetary policy to remain accommodative until consumer prices reverse their current trend. One measure indicating a forward looking change to this thesis might be changes to the output gap, which is defined as the difference between potential growth and actual growth (Figure 3).

**OUTPUT GAP**

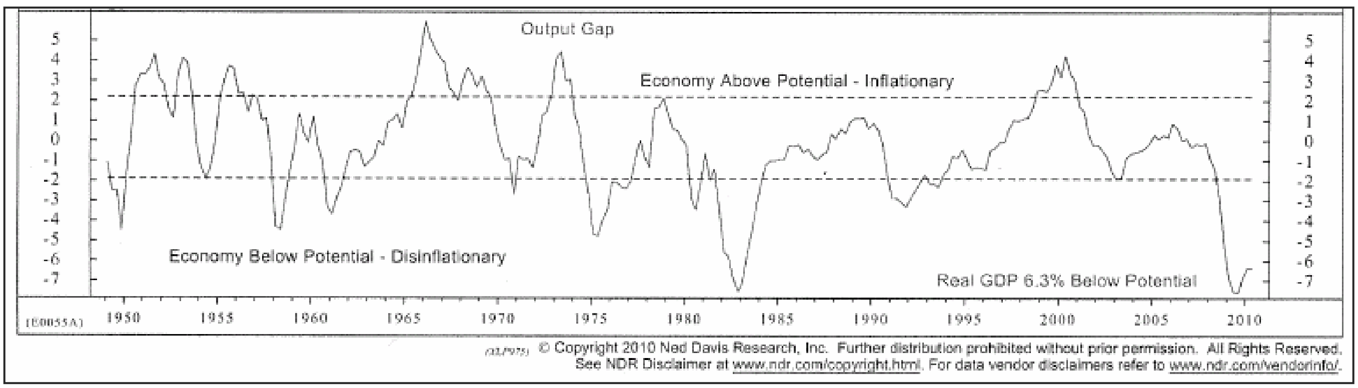
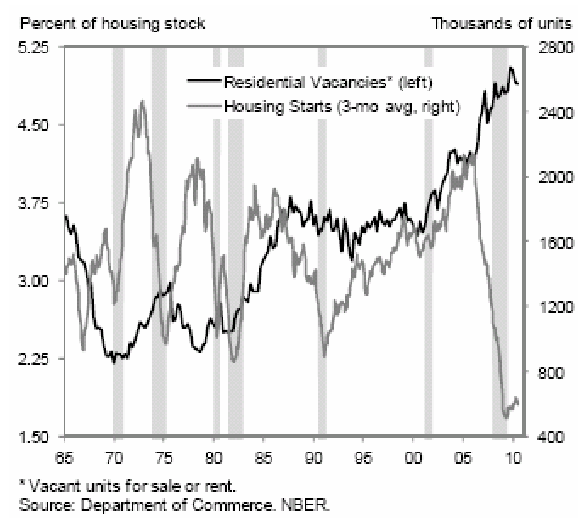



**Figure 3. Output Gap is Disinflationary**

**HOUSING IMBALANCE**




Another indicator predicting an acceleration of growth might be an improvement in housing. Clearly, housing remains a drag on consumption and expectations for price stabilization in 2010 has been dampened (Figure 4). Finally, and perhaps most importantly, the labor market needs to improve to bring the US consumer back into play as the main engine for GDP growth. To conclude, it appears that an acceleration of growth will be necessary to reverse interest rates higher -- and at least three forward looking indicators still have a long way to go.

**Figure 4. Housing Imbalances.**

## LEON COUNTY PORTFOLIO REVIEW SEPTEMBER 30, 2010

Cutwater's goal since receiving the Leon County portfolio in July 2010 was to implement our long-term investment strategy on an inherited portfolio of investments. Importantly, executing this strategy change needed to occur without impairing portfolio performance with undue turnover. To this end, Cutwater underwrote all corporate and asset-backed investments to determine appropriate liquidity and fair value.

As the second and third quarter of 2010 unfolded, corporate credit continued to improve in price versus other fixed income sectors. The continued support of mutual fund flows and improving corporate fundamentals provided enough liquidity to improve the risk profile in the portfolio. Specifically, we swapped regional bank, captive finance and cyclical sectors (BB&T, Paccar, Nucor) for better protected investments such as regulated utilities, insurance, and consumer asset-backed sectors (Georgia Power, Mass Mutual, CNH). The resulting portfolio is rated Aa1 and has an even distribution of credit sectors between Banking, Insurance, Industrials and Utilities.

Alternatively and as evidenced by market pricing, some inherited asset-backed investments will take several years to receive ultimate principal. A few are also likely to suffer permanent impairment. In order to optimize the tradeoff between impairment today and portfolio illiquidity tomorrow, Cutwater continuously underwrites these asset-backed investments to the loan level. This process determines expected return and time horizon to principal payment to determine what we believe is fair value. Only when market conditions provide a clearing price near this fair value will an impaired investment be sold.

With the exception of these few legacy asset-backed investments, the portfolio is positioned appropriately from duration, curve and sector allocation perspectives. We still anticipate a check-marked shaped economic recovery for 2011 where short-term rates will eventually rise and credit sectors will remain well-priced. We also expect the portfolio to perform well in this scenario.

## VI. PERMITTED INVESTMENTS AND ALLOWABLE MATURITIES

Table 1 summarizes the permitted investments, composition limits and maximum allowable maturities. The County's available funds are invested according to Leon County Investment Policy Section XIV, which authorizes the County to invest in specific permitted investment types. The permitted investments are restricted by the Policy in their composition limits and maximum allowable maturities. The portfolio was in compliance with all policy limits. The Policy permits maturities of the operating portfolio establishing a range of 60 days to 10 years. The actual portfolio will have a range of 0.5 years to 2.5 years, with an average duration of 1.5 years. Table 1 gives a brief description of each investment type. It is generally regarded that the following investment types are safe investments and meet the Policy's first objective: safety.

**Table 1 – Permitted Investments**

| Investment Type | Composition Limit | Max Maturity/ WAL Limit |
|---|---|---|
| Repurchase Agreements | 15%, 5% any one issuer | 60 Days |
| Bankers' Acceptances | 15%, 5% any one issuer | 270 Days |
| Commercial Paper | 20%, 5% any one issuer | 270 Days |
| CDs (Financial Deposit Instruments insured by FDIC) | 30%, 10% any one issuer | 2-Year, 1-Year Avg |
| Agencies | 100%, 20% any one issuer | 5-Year |
| Instrumentalities | 45%, 15% any one issuer | 5-Year |
| Corporate Debt | 25%, 3% any one issuer | 5-Year |
| Municipal Bonds | 35%, 3% any one issuer | 5-Year |
| Mortgage Backed Securities | 35%, 5% any one issuer | 5-Year WAL |
| Asset Backed Securities | 5%, 1.5% any one issuer | 5-Year WAL |
| Commercial Mortgage Backed Securities | 8% , 3% any one issuer | 5-Year WAL |
| Treasuries | 100% | 10-Year |
| SPIA, FLGIT, FMIT 0-2 and FMIT 1-3 | 15% each | NA |
| SBA | 50% | NA |
| Money Markets | 100% | NA |

### A. U.S. Government Securities (Treasuries)

The securities comprising Treasuries are direct obligations of the U.S. Government. The securities are designated by maturity. Treasury bills have maturities of one year or less, Treasury notes have maturities of two to ten years, and Treasury bonds have maturities of more than ten years. The longer maturities share some market risk in that their prices may be more volatile due to interest rate fluctuations. Treasury yields are typically lower than yields of other U.S. Government securities. The investment policy allows the County to invest up to 100% of the portfolio in these investments.

### B. Federal Agency Securities (Agencies)

Agencies are securities issued by agencies of, and are guaranteed directly by, the U.S. Government. The Policy limits Agency investments to bonds, debentures or notes issued or guaranteed by United States Government agencies, provided such obligations are backed by the full faith and credit of the United States Government. Such securities are limited to the following: Small Business

Administration, United States Department of Agriculture, United States Export-Import Bank, direct obligations or fully guaranteed certificates of beneficial ownership, Farms Home Administration, Federal Financing Bank, Federal Housing Administration Debentures, General Services Administration Participation Certificates, United States Maritime Administration Guaranteed, Title XI Financing, New Communities Debentures, United States Government guaranteed debentures, U. S. Public Housing Notes and Bonds, U.S. Government guaranteed public housing notes and bonds, U. S. Department of Housing and Urban Development Project notes and local authority bonds. Agencies are typically longer term and not frequently traded, creating some liquidity risk. Agency yields are generally greater than Treasury yields of similar maturities. A maximum of 20% of the portfolio may be invested in any one agency and an aggregate of up to 100%.

### C. Federal Agency Securities (Instrumentalities)

Instrumentalities are also securities issued by agencies, which are sponsored by the U.S. Government. The Policy allows purchases of bonds, debentures or notes issued or guaranteed by United States Government sponsored agencies (Federal Instrumentalities) which are non-full faith and credit agencies limited to the following: Federal Farm Credit Bank (FFCB), Federal Home Loan Bank or its district banks (FHLB), Federal National Mortgage Association (FNMA), Federal Home Loan Mortgage Corporation (FHLMC) including participation certificates, Tennessee Valley Authority (TVA). Yields on Instrumentalities are typically greater than Treasury yields of similar maturities. The Policy further restricts investments in any one agency to 15% of the portfolio and an aggregate of 45% of the portfolio.

### D. Financial Deposit Instruments Insured by FDIC (Certificates of Deposit)

Investments may be made in Financial Deposit Instruments Insured by FDIC in banks organized under the laws of this state and/or in national banks organized under the laws of the United States and doing business and situated in this state, provided that any such deposits are secured by the Florida Security for Public Deposits Act, Chapter 280, Florida Statutes and provided that the bank is not listed with any recognized credit watch information service. A maximum of 30% of the portfolio may be invested in Financial Deposit Instruments insured by FDIC.

### E. Repurchase Agreements (Repos)

A repurchase agreement is a financial transaction in which Leon County exchanges cash for ownership of specific securities with a simultaneous agreement to sell back the securities. Overnight repos mature in one day. Other repos are written to mature in specific multi-day periods and are known as term repurchase agreements. Other repos are written as open transactions with indefinite terms subject to liquidation by either party. Yields tend to run close to the federal funds rate. The Policy calls for the specific securities to be only those Treasuries or Instrumentalities allowed by the Policy with maturities. The collateral held pursuant to a repurchase agreement shall have a maturity under five years and having a market value of 102% during the term. Leon County will enter into a repo transaction only with qualified financial institutions, which have executed a Master Repurchase Agreement with the Clerk’s Office. The Policy further restricts transactions with any one financial institution to 5% of the portfolio, except for one-business day repos, with a maximum of 15%.

### F. Bankers' Acceptances (BAs)

Bankers' Acceptances are generally bearer form securities comprised of underlying letters of credit used to finance international trade. A bankers' acceptance is created from a letter of credit issued by an importer's bank to pay a foreign exporter for goods expected to be received. The exporter will normally present this letter of credit to its bank for a discounted payment. The exporter's bank then presents the letter of credit to an U.S. correspondent bank for payment at which time it is marked "Accepted". Upon acceptance, the BA becomes an irrevocable and unconditional obligation of the accepting bank and it is also an obligation of the importer and any endorser thereof. BAs typically have maturities of 180 days or less. Yields are generally greater than Treasuries and Instrumentalities of similar maturity. The Policy requires bankers' acceptances which are inventory based and issued by a bank, which has at the time of purchase, an unsecured, uninsured and un-guaranteed obligation rating of at least "Prime-1" and "A" by Moody's and "A-1" and "A" by Standard & Poor's. The Policy further restricts the investment with any one financial institution to 5% of the portfolio and an aggregate of 15% of the portfolio.

### G. Commercial Paper (CP)

Commercial paper is unsecured short-term debt issued primarily by corporations to finance receivables and other short-term needs. CP has a maximum maturity of 270 days or less. Yields are typically greater than Treasuries and Instrumentalities of similar maturity. The Policy requires the issuer to be rated Prime-1 by Moody's Investor's Service and A-1 by Standard & Poor's, and, if backed by a letter of credit, the credit provider must be ranked in the top fifty U.S. banks by the American Banker's yearly report. The Policy further restricts the investment with any one financial institution to 5% of the portfolio and an aggregate of 20% of the portfolio.

### H. Municipal Obligations (Munis)

Investments may be made in notes or bonds issued by governmental entities or territorial boundaries of the United States, provided that such instrument is rated A or better by at least one NRSRO.

### I. Constant Net Asset Value Money Market Mutual Funds

Money markets are pools of securities providing income and liquidity. The Policy enables the Clerk to invest in SEC qualified constant net asset value fixed income money market mutual funds rated AAAm or AAAg comprised of only those investment instruments as authorized in this Section XIV, Portfolio Composition, provided that such funds do not allow derivatives. The average maturity of the underlying investments may not exceed one year. A maximum of 100% of the portfolio may be invested in money markets.

### J. The Florida Local Government Investment Trust Government Fund (FLGIT)

The FLGIT is a local government investment pool created by the Florida Association of Court Clerks and Clerk, and the Florida Association of County's for the purpose of providing public entities with an investment program that focuses on longer term securities with the highest credit ratings. The effective maturity of the underlying investments is five years or less. At year end, the FLGIT was invested in money markets, Treasury Notes, asset-backed securities, and Federal agency obligations. This investment type is subject to some market risk due to fluctuating prices and liquidity risk due to advance redemption notification requirements. However, it has a professional investment advisor and an investment advisory board, and provides diversity in the Fund's portfolio. The FLGIT maintains a credit rating of AAA by Standard & Poor's. Investments in this pool are limited to a maximum of 15% of the portfolio.

### K. First Municipal Investment Trust (FMIT) 1- 3 Year High Quality Bond Fund.

The FMIT is a similar investment pool operated by the Florida League of Cities. Its rating, investment parameters and liquidity generally mirror those of the FLGIT. The 1 to 3 Year High Quality Bond Fund is designed to provide an investment pool alternative to those Members that have excess funds and that have an investment horizon greater than that of money market instruments. The investment objective is: 1) to preserve capital; 2) achieve a total rate of return that exceeds the return of T-Bills by 1% per year over rolling three-year periods; and 3) exceed the return of the Merrill Lynch One-to Three-year Government Index over three-year periods. The Portfolio will generally invest in securities with greater potential returns and risk than those offered by money market type instruments. Due to the fact that the Portfolio will be investing in securities with an average maturity of approximately two years, increases in interest rates will cause declines in the net asset value of the Portfolio. Therefore, the Portfolio may be an inappropriate investment for funds required to meet short-term needs. Investments in this government pool are limited to a maximum of 15% of the portfolio.

### L. First Municipal Investment Trust (FMIT) 0 - 2 Year High Quality Bond Fund

During the fiscal year, the County reallocated a portion of investments from money markets to this Bond Fund also operated by the Florida League of Cities. This Fund which was established in April 2009 invests in Government and high quality securities while maintaining an average maturity of approximately one year. The performance of the portfolio is measured against the Merrill Lynch 1 Year Treasury Note Index. The portfolio is managed by Atlanta Capital Management. Investments in this government pool are limited to a maximum of 15% of the portfolio.

### M. Special Purpose Investment Trust (SPIA)

Effective July 1, 2004, Section 17.61(1), Florida Statutes was amended to permit organizations created by the Florida Constitution to participate in the existing State Treasury Investment Pool "Special Purpose Investment Account (SPIA)." Historically, SPIA participants have received higher earnings reflecting the higher risk associated with the longer maturities and lower credit quality. The Board of County Commissioners approved revisions to the County's Investment Policy effective January 11, 2005, to permit up to 15% of the County portfolio to be invested with the Treasury Special Purpose Investment Account (SPIA). The financial details and disclosures for the Treasury Investment Pool are made in Note 2 to the State of Florida Comprehensive Annual Financial Report (CAFR).

The Treasury Investment Pool (Pool) earned $31,818,050.67 in September 2010. These earnings resulted in a gross effective interest rate (annualized) of 2.2356%. The Pool's fair value factor was 1.0208 for September. A factor greater than 1.0000 provides that the market value of the Pool's investments is greater than the funds invested in the Pool. For more information relating to the Treasury Investment Pool, please visit the website at www.fltreasury.org.

## VII. LIQUIDITY REQUIREMENTS

The second objective in managing the County's investments is the provision of sufficient liquidity. On a regular basis, the County's receipts and disbursements are analyzed to determine trends in cash inflow and outflow. Cash inflows are invested immediately upon receipt and become part of the portfolio. The portfolio provides cash for weekly payment of operating and capital expenditures, biweekly payment of payroll expenditures, and semiannual debt service payments. Debt service payments are funded through sinking funds held by the County.

## VIII. INVESTMENT OPERATIONS

Investing activities are conducted by the investment advisor and qualified professionals in the Clerk's Office in accordance with Florida Statutes, County Ordinances, and written policies and procedures. Monthly reports of investment activity and positions are prepared and distributed to management of the Clerk's Office, management of the BCC and the Investment Oversight Committee. Regular meetings of the IOC are held to monitor the portfolio, evaluate investment performance and discuss investment strategies.

The investment advisor and Clerk staff use sophisticated techniques in carrying out its investment activities including the use of electronic bank and trust account systems; electronic funds transfer; on-line, real-time monitoring of U.S. securities markets; and electronic trading. Bank account balances, cash requirements, investment positions and trust account activity are determined daily. Current conditions and evaluations of national economic activity are considered in making asset allocation decisions.

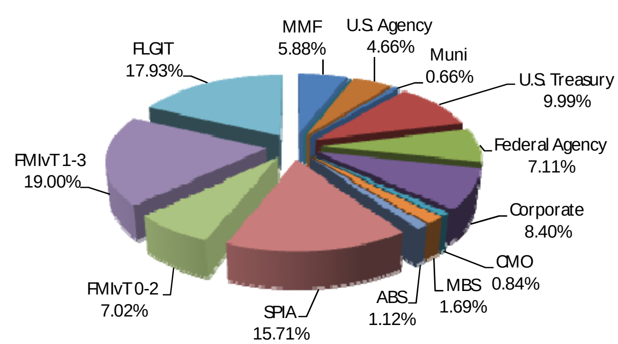
### A. Portfolio Balances

The portfolio's ending balance for fiscal year 2010 was $213,494,076 while the ending balance for 2009 was $219,356,485, a decrease of $5,862,409. The decrease in year-end balances from fiscal year 2010 to 2009 is attributable to several factors including the expenditure of funds for capital construction projects and lower interest earnings.

### B. Portfolio Composition

As of September 30, 2010, the portfolio was fully invested in permitted investments within allowable composition limits. The Clerk or the Clerk's designee (Finance Director shall have the option to further restrict or increase investment percentages from time to time based on market conditions. Any changes to the portfolio composition guidelines or limits must be in writing from the Finance Director directed to the appropriate parties and discussed at each quarterly Investment Oversight Committee meeting. The portfolio was managed in compliance with the Policy which requires the portfolio to be diversified by investment type.

**Table 2**
**Portfolio Composition - September 30, 2010**



### C. Portfolio Maturities

Portfolio management was also accomplished in compliance with the Policy that requires ensuring sufficient liquidity as well as diversity in maturities. Shown in Table 4 are the average terms of each investment type acquired in fiscal years 2010 and 2009. Average term is the average number of days from purchase to maturity of the investment. Average terms greater than one year represent investments of non-current funds, including the non-current operating portfolio, and investments of bond proceeds and debt service reserve funds. The externally managed portfolio was invested for a weighted average term of approximately 712 days in fiscal year 2010, as compared with a weighted average term of 693 days in fiscal year 2009.

Table 3 – Average Term by Investment Type

| Investment Type | FY 2010 | FY 2009 |
|---|---|---|
| Mortgages | 902 days | 1092 days |
| Treasuries | 636 days | 595 days |
| Cml/Multi | 463 days | 840 days |
| Corporates | 817 days | 773 days |
| ABS | 1,285 days | 456 days |
| Financial Deposit Instrument (CDs) | 90 days | 90 days |
| Agencies | 621 days | 759 days |
| Taxable Munis | 719 days | 515 days |
| Florida Municipal Inv. Trust | NA | NA |
| Fl Local Govt. Inv. Trust | NA | NA |
| Fl. Special Purpose Inv. Acct | NA | NA |
| Money Markets | NA | NA |

### D. Earnings and Yields

The portfolio earned $4,988,617 of interest and realized gains of $836,219 for total income of $5,824,836 for the fiscal year ended September 30, 2010. This total income provided an effective rate of return of 2.48% on an average daily balance of $235,249,514 in the fiscal year 2010. During this fiscal year the Federal Funds Rate ranged between 0.00 % and 0.25% and is expected to remain at this level for the foreseeable future. As a result of the low interest rates, the County's average portfolio return for Fiscal Year 2010 decreased from 3% to 2.48%.

The dollar amount of earnings is used in historical and budgetary comparisons, and in cash flow analysis. Actual interest earnings totaled $4,988,617 in interest in fiscal year 2010 and $6,328,767 in fiscal year 2009. Actual earnings exceeded budget in fiscal year 2009 by $949,731 and in fiscal year 2010 by $2,904,067 as shown in the following Table 4 on the following page.

**Table 4 - Budget and Actual Income**

| | FY 2010 | FY 2009 |
|---|---|---|
| Actual | $4,988,617 | $6,328,767 |
| Budget | 4,038,886 | 3,424,700 |
| Variance | $ 949,731 | $2,904,067 |

## IX. CONCLUSION

In conclusion, the results outlined in the Annual Investment Report are as follows:

- The investment portfolio is in full compliance with the Investment Policy.
- Total portfolio return was below that of last fiscal year due to reduction in interest rates and cash available to invest
- The economic environment continued to be highly volatile.

**Investment Oversight Committee**

Pursuant to investment policy requires staff to notify the IOC at any time holdings drop below the minimum credit ratings required by the policy. The IOC will then consider the market environment and make recommendations to hold and continue to monitor the investments or liquidate the investments. Accordingly, throughout the fiscal year the IOC continued to monitor closely the performance of several asset backed securities and was provided detailed reports from the external manager.

These reports and discussions at quarterly meetings included the consideration of various factors including the performance of collateral to date, absence of losses to date, presence of mid-tier insurance wrap, positive characteristics of the underlying collateral, or severe liquidity penalty currently being applied in the market. As of the September 30, 2010 the difference between original cost totaling $1,493,368 million and current market of $1,117,572, for the remaining five securities is about $375,795. This difference represents 0.51% of the $73.5 million dollar portfolio managed by the external manager and 0.18% of the $213,105,878 total portfolio. At the November 17, 2010, IOC meeting, the external manager recommended selling one of the securities and continuing to hold the four remaining securities.

Presented by:

| | |
|---|---|
| Stan Barnes, Chairman<br>Investment Oversight Committee | Bob Inzer, Clerk of the Circuit Courts<br>Leon County, Florida |