

**ANNUAL INVESTMENT REPORT  
LEON COUNTY, FLORIDA**

FOR THE FISCAL YEAR ENDED  
SEPTEMBER, 2003

PREPARED BY  
BOB INZER  
CLERK OF COURTS

## EXECUTIVE SUMMARY

Available cash was invested according to the Investment Policy in permitted investments within composition limits and allowable duration. The only exception to the policy was action by the Investment Oversight Committee to liquidate all corporate securities due to financial reporting scandals by several fortune 500 companies. This is discussed in more detail later in the report.

Domestic monetary policy measured by Federal Funds rates reflected Federal Open Market Committee (FOMC) concerns about a weak economy. Interest rates continued their decline during the year hitting a 40-year low. Interest rates on short-term government securities fell below 1% for part of the year and ended the year slightly above their low point. The average portfolio return for FY 2003 also dropped to 2.506% from 3.58 last year. Unfortunately, most economist continue to forecast interest rates remaining at near this level for the most of next year and rising slightly during the latter half of FY 2004.

The portfolio earned \$4,120,618 on an average daily balance of \$164,467,163 in the fiscal year 2003. Total earnings (interest plus capital gains/losses) exceeded budget earnings by \$668,095.

During the calendar year of 2002, the corporate bond market was shaken because of major corporate business failures. The instability in the corporate bond market which was brought on by major business failures caused the Investment Oversight Committee (IOC) to take pause and to revisit the safety of owning corporate securities given the unstable climate. The Board approved Investment Policy provides for limited investments in high quality corporate securities. However, considering the fact that companies like Worldcom and Enron were unexpectedly experiencing financial disasters, the IOC felt this was a time for caution. The IOC recognized the most important principal in investing is safety and believed that the investment policy was designed for normal market conditions and was inappropriate in this market environment.

After much consideration and deliberation as to what would be the most prudent action to take when considering the status of the market, on July 22, 2002, the IOC voted to recommend elimination of all corporate securities from the investment portfolio. The IOC advised the Board of this recommendation and provided the Board an opportunity to respond prior to taking action. Without objection from the Board, the Clerk's staff subsequently coordinated with the County's investment advisor to liquidate the corporate investment holdings and to invest in higher quality less risky instruments. This included a greater utilization of the SBA, which carried the County over its 50% cap as outlined in the policy of which the Board was notified.

The IOC recognized that their recommendation would result in a less risky portfolio and also a lower rate of return. The IOC was unsure the depth of the problem in financial reporting by private corporations and determined that the potential additional earnings from having a portion of our portfolio in corporate securities was of less value than the “sleep insurance” we received by not taking the risk. The IOC in making this decision believed this was a temporary situation and therefore did not recommend a change in the Investment policy. In the third quarter of 2003, the IOC recommended that the Board resume investing in the corporate bond market.

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 is presented below as of September 30, 2003.

**Table I**

Summary Table of Portfolio Performance

<u>Investment Type</u>	<u>Average Daily Book Value</u>	<u>Average Daily Market Value</u>	<u>Interest Earned</u>	<u>Capital Gains/Losses</u>	<u>Total Earnings</u>
Voyageur Asset Mgmt Intermediate	59,389,444	60,621,021	613,022	1,916,158	2,529,180
Voyageur Asset Mgmt Landfill	3,902,944	3,985,847	456,090	131,180	587,270
SBA (Intermediate)	66,069,599	66,069,599	966,368	-	966,368
SBA (landfill)	5,190,115	5,190,115	78,103	-	78,103
Wachovia Bank Portfolio Manager's Acct	548,884	548,884	3,122	-	3,122
Wachovia Bank Depository Acct	24,232,873	24,232,873	188,944	-	188,944
<u>Bank of New York Repo</u>	<u>5,133,304</u>	<u>5,133,304</u>	<u>185,056</u>	<u>-</u>	<u>185,056</u>
Total of all funds	164,467,163	165,871,643	2,490,705	2,047,338	4,538,043
Rate of Return (Interest only)				1.514%	
Total Return (Interest plus Capital gains/losses)				2.506%	

**Table II**  
**Average Portfolio Balance and Daily Return**

**FY 2003**

**FY 2002**

<u>Investment Type</u>	<u>Average Daily Balance</u>	<u>Average Daily Rate</u>	<u>Average Daily Balance</u>	<u>Average Daily Rate</u>
Funds Trust Fund (SBA)	\$71,259,714	1.52%	\$31,923,783	2.08%
Voyageur Portfolio Manager Account (Fixed Income Securities)	63,292,388	3.41%	61,290,160	4.16%
First Union Sweep/Depository	24,232,873	1.48%	24,812,608	1.78%
First Union Money Market/Portfolio Manager	548,884	0.52%	40,677,964	1.86%
Bank of New York (Repo)	5,133,304	7.21%	5,133,133	7.21%
Totals	\$164,467,163	2.506%	\$163,837,648	3.58%

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**ANNUAL INVESTMENT REPORT**  
For the year ended September 30,2003  
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 Commissions. 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 Director of OMB and three qualified individuals with financial or investment expertise who are independent of employment and business relationships with Leon County. They are Mr. Randy Pople, IOC Chairman, President of Capital City Trust Company; Mr. John Lawrence, retired Public Administrator; and Charles Cooper, Real Estate and Tax Attorney, Partner at Cooper and Byrne.

III. ACTIVITIES OF THE INVESTMENT OVERSIGHT COMMITTEE

The Investment Oversight Committee (IOC) scheduled quarterly meetings to discuss issues relating to the investments of the County. In addition to the regular meetings, the IOC scheduled several intra-quarterly meetings to discuss the full investment status to Voyageur Asset Management (VAM). On July 22, 2002, the IOC recommended the elimination of all corporate bonds in the investment portfolio. At the July 30, 2003 meeting, the IOC, after much discussion, rescinded their previous position regarding including corporate securities and all other investments permitted in the Investment portfolio. Presently, VAM is authorized to use all of the investments provided for in the Investment Policy.

IV. INVESTMENT OBJECTIVES

The Policy describes three specific objectives to be applied in managing the County's investments. The primary objective is **safety** of the County's funds. Safe investments are those that ensure minimum credit risk, the risk that the principal will not be repaid. Safe investments are also those that carry minimum market risk, the risk that the principal value will not decrease over the life of the investment. This objective also considers

methods to **control risks and diversify** the portfolio by security types, maturities and financial institutions.

The second objective is the provision of sufficient **liquidity**. The County's funds are invested so that the County can meet its expenditures of operating, payroll, and capital needs when they become due. Liquidity is also the ability to sell an investment when necessary, with minimal delay and minimal loss of principal. The portfolio's investments are held to maturity, when possible, to avoid selling the investment prior to maturity and risking a capital loss.

**Maximizing yield** on the portfolio is the County's third investment objective. This objective is only sought after the County has met its first two investment objectives.

#### V. PORTFOLIO PERFORMANCE

**The portfolio earned \$4,120,618 for an effective total rate of return of 2.506% on an average monthly balance of \$164,467,163 in the fiscal year 2003.** 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 \$5,858,134 for an effective rate of return of 3.58% on an average daily balance of \$163,837,648 in fiscal year 2002. As stated earlier in the executive summary, the effective rate of return for fiscal year 2003 is lower than that for fiscal year 2002 because of the overall decline in interest rates and the elimination of corporate securities from the investment portfolio. The instability in the corporate bond market which was brought on by major business failures caused the Investment Oversight Committee (IOC) to take pause and to revisit the safety of owning corporate securities given the unstable climate.

After review by the Board, they accepted the IOC recommendation to divest from corporate bonds. The Clerk's staff subsequently coordinated with the County's investment advisor actions to liquidate the corporate investment holdings and to invest in higher quality less risky instruments. It was understood that because the County was taking less risk the returns on investments would be less. Although it was understood that the return on investments would be less, the County felt that the risk of losing the principle far outweighed any excess income that would be realized.

In addition to increasing the quality of our investments, the reduction in interest earnings of \$1,737,516 can be attributed to the Federal Reserve reducing the Federal Funds Rate to the lowest level in over 40 years (1%). During FY/2003, the Federal Reserve lowered the Fed Funds Rate twice, from 1.75% to 1.00% in an effort to boost the economy.

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 with the exception that more than 50% of the portfolio was invested in the SBA for a portion of the year. The Policy addressed maturities of the operating portfolio establishing a range of 0.5 to 2.5 years, and assumes the normal portfolio will have 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**

<u>Investment Type</u>	<u>Composition Limit</u>	<u>Maximum Maturity</u>
SBA	50%	NA
Treasuries	100%	Ten Years
Agencies	45%, 15% any one issuer	Five Years
Instrumentalities	45%, 15% any one issuer	Ten Years
CDs & Savings Accounts	20%, 10% any one issuer	One Year
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, avg. 90 days
Municipal Obligations	10%	Three Years
Money Markets	25%	NA
FLGIT and/or FMIT	15% combined	NA

A. Florida Local Government Surplus Funds Trust Fund Investment Pool (SBA)

The SBA is administered and invested by the Florida State Board of Administration for the purpose of pooling investment funds of local governments in an investment portfolio of money market instruments that provide liquidity while preserving capital. As of October 1, 1997, the SBA had converted to a “2a-7 like” investment pool (SEC Rule 2a-7 of the Investment Company Act of 1940). Some of the pertinent investment constraints of a “2a-7 like” pool include weighted average maturities limited to 90 days, maximum maturities for government securities limited to 762 days, money market instruments limited to 397 days, and top tier credit ratings. At September 30, 2003, the SBA was invested in Treasury Bills 9.1%; federal agency obligations 32.07%; commercial paper 44.891%; medium term and variable rate notes 13.94%; and certificates of deposit. This investment type is subject to some market risk. However, since it operates as a “2a-7 like” pool, interest rate risk (the risk that interest rate fluctuations might impair the portfolio’s profitability or viability) is minimal. A maximum of 50% of the portfolio may be

invested in the SBA, but when combined with money market mutual funds, may not exceed 60% of the portfolio. Bond proceeds temporarily deposited with the SBA are not considered in calculating the composition maximum.

B. U.S. Treasury 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.

C. 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 direct obligations or guaranteed certificates of the Export-Import Bank, certificates of beneficial ownership of the Farmers Home Administration, discount notes of the Federal Financing Bank, Federal Housing Administration debentures, General Services Administration participation certificates, Maritime Administration guaranteed Title XI financing, guaranteed Public Housing notes and bonds, and HUD 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 agencies.

D. 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, notes or debentures of the issuing agencies including Federal Farm Credit Banks, Federal Home Loan Bank or its district banks, Federal National Mortgage Corporation, and the Student Loan Marketing Association. Instrumentalities vary in maturities. 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.

E. Certificates of Deposit and Savings Accounts (CD's/Savings)

The Comptroller may invest in nonnegotiable, interest bearing certificates of deposit and savings accounts in state or national banks located in Florida, and having their deposits secured by Chapter 280, Florida Statutes, known as the Florida Security for Public Deposits Act. The Policy provides that the issuing bank may not be listed

with any nationally known credit watch organization. There is some liquidity risk in that this investment type is subject to penalties for early withdrawal. The Policy further restricts investments in any one bank to 10% of the portfolio with an aggregate limit of 20%.

#### F. 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 Comptroller'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%.

#### G. Bankers' Acceptances (BAs)

Bankers' Acceptances are generally bearer form securities comprised of underlying letters of credit used to finance international trade. A BA 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 BAs to be inventory-based, issued by a domestic bank, rated Prime-1 and A by Moody's Investors Service and A-1 and A by Standard & Poor's, and 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 15% of the portfolio.

#### H. 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.

I. Municipal Obligations (Munis)

For situations necessary to comply with arbitrage regulations, the Clerk may invest in taxable and tax-exempt debt, and general obligation and revenue bonds issued by states and local governments. Long-term debt must be rated at least AAAM or AAAG.

J. Fixed Income Money Market Mutual Funds (Money Markets)

Money markets are pools of securities providing income and liquidity. The Policy enables the Comptroller to invest in SEC qualified fixed income money markets with underlying investments only in Treasuries, Instrumentalities, Repos, Munis, CP and BAs. The average maturity of the underlying investments may not exceed one year. A maximum of 25% of the portfolio may be invested in money markets, but when combined with the SBA may not exceed 50% of the portfolio. The Policy further restricts the investment with any one fund to 3% of the portfolio.

K. The Florida Local Government Investment Trust Government Fund (FLGIT) or the First Municipal Investment Trust (FMIT)

The FLGIT is a local government investment pool created by the Florida Association of Court Clerks and Comptroller, and the Florida Association of Counties 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 September 30, 2003, 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. 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.

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. Average weekly expenditures for payroll, operating and capital expenditures during the fiscal year were \$2.7 million, approximately \$0.4 million more than the prior fiscal year.

## 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.

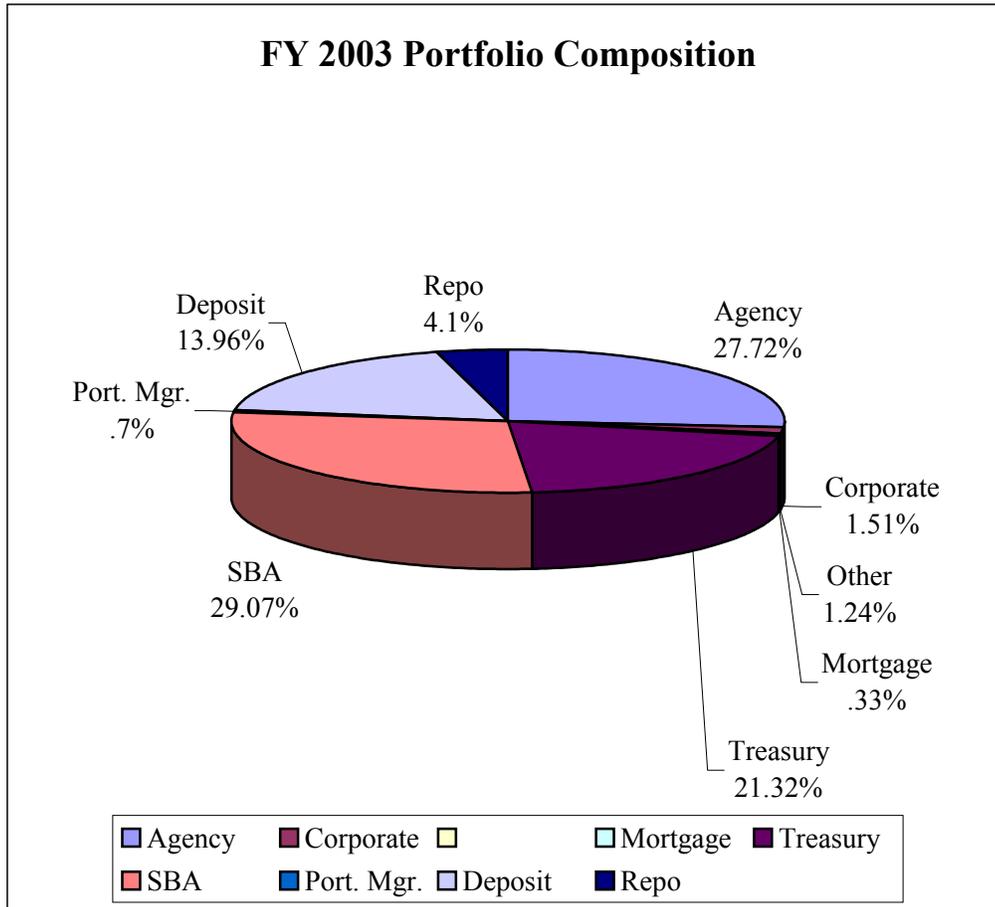
### A. Portfolio Balances

The portfolio's ending balance for fiscal year 2002 was \$146,231,998 while the ending balance for fiscal year 2003 was \$124,534,053, down from the ending balance of the prior year by \$21,691,945. The decrease in year-end balances from fiscal year 2002 to 2003 is attributable to the use of funds loaned to DOT for road construction projects and major capital expenditures.

### B. Portfolio Composition

As of September 30, 2003, the portfolio was fully invested in permitted investments within allowable composition limits. The portfolio was managed in compliance with the Policy with the exception of the issues stated above, which requires the portfolio to be diversified by investment type. The portfolio consisted of agencies in the amount of \$34.8 million; this represents 27.72% of the entire portfolio. Mortgage backed obligations were in the amount of \$0.43 million or 0.33% of the portfolio. The investment in treasuries amounted to \$26.8 million or 21.32% of the portfolio. As a result of the recent IOC approval of corporate investments, this position has \$1.9 million or 1.51%. The remaining funds \$35.9 million were invested in the SBA (State investment pool) representing 29.07%, the Wachovia sweep with \$17.1 million (now known as the Depository Account) 13.96%, the Wachovia Money Market Fund with \$.86 million (now known as the Portfolio Account) .7%, and Bank of New York (Repo) with \$5.13 million at 4.16%.

Table 2



Portfolio Maturities

Table 3 – Average Term by Investment Type

<u>Investment Type</u>	<u>FY 2003</u>	<u>FY 2002</u>
Agencies	452 days	726 days
Treasuries	627 days	321 days
Mortgages	306 days	416 days
Corporates	901 days	772 days
Repos	731 days	1,275 days
SBA	93 days	63 days
Money Market Funds	1 day	1 day

Portfolio management was also accomplished in compliance with the Policy that requires ensuring sufficient liquidity as well as diversity in maturities. Shown in Table 2 are the average terms of each investment type acquired in fiscal years 2003 and 2002. 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. Available funds were invested for a weighted average term of 526 days in fiscal year 2003, as compared with a weighted average term of 243.78 days in fiscal year 2002.

D. Interest Earnings and Yields

The dollar amount of interest earnings is used in historical and budgetary comparisons, and in cashflow analysis. The portfolio earned **\$4,120,618** on its invested principal in fiscal year 2003. For comparison, the portfolio earned \$5,858,134 on its invested principal in fiscal year 2002. Actual interest income exceeded budget in fiscal year 2002 by \$604,952 and in fiscal year 2003 by \$604,952, as shown in Table 3 below. Interest rates for fiscal year 2002 were at a thirty-year low.

Table 4 - Budget and Actual Interest Earnings

	<u><b>FY 2003</b></u>	<u><b>FY 2002</b></u>
Actual	\$4,120,168	\$5,858,134
Budget	\$3,522,363	\$5,253,182
Variance	\$597,805	\$604,952

## 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.
- Overall portfolio risk has been reduced through reduced portfolio duration and improved asset quality.
- Actual interest earnings exceeded budget estimates by \$.598 million.
- Total portfolio return was below that of last fiscal year for the following reasons:
  - Shorter duration (13.86 days)
  - Elimination of all corporate debt from the portfolio
  - Interest rates, in general, fell to 30 year lows
  - “Flight to Quality” resulted in interest rates in government and government agencies declining more than other securities or comparable duration.
  - Federal Reserve lowering of Fed Funds Rate two times, from 1.75% to 1.00% resulting in lower interest rates for instruments held in our portfolio
- The Investment Oversight Committee made recommendations to:
  - Get back into corporate securities, thus returning to normal risk levels with the expectation that the yield will be increased.
  - Recommended the removal of all restrictions on the investment advisor and making investments in compliance with the Investment Policy

Presented by:

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Randy Pople, Chairman  
Investment Oversight Committee

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Bob Inzer, Clerk of the Circuit Courts  
Leon County, Florida