SAN MATEO COUNTY TREASURY OVERSIGHT COMMITTEE

MINUTES

Monday, May 19, 2025

1. **CALL TO ORDER**

   The meeting, in person and via MS Teams, was called to order at 12:01 p.m. by Daneca Halvorson.

2. **ROLL CALL**

   Members and guests were asked to introduce themselves by name and title during roll call.

   MEMBERS IN ATTENDANCE:

   Daneca Halvorson, Chair (City of Daly City)
   Sandie Arnott (Treasurer-Tax Collector)
   Virginia Chang Kiraly (San Mateo County Harbor District and Menlo Park Fire Protection District Board)
   Helen Fisicaro (Town of Colma)
   Stephanie Osaze (Bay Area Air Quality Management District)
   Robert Manchia (San Mateo County Executive's Office)
   Connie Mobley-Ritter (Public Member)

   STAFF IN ATTENDANCE:

   Tiffany Htwe (Treasurer's Office)
   Angela Moreno (Treasurer's Office)

   MEMBERS OF THE PUBLIC IN ATTENDANCE:

   Ken Schiebel (PFM)
   Meredith LaBuda Sullivan (PFM)
   Nancy Jones (PFM)
   Allison Kaune (PFM)

3. **APPROVAL OF MINUTES – February 24, 2025**

   Helen Fisicaro made a motion to approve minutes from February 24, 2025, meeting and seconded by Virginia Chang Kiraly. The meeting minutes were unanimously approved.

4. **TREASURER'S REPORT – Sandie Arnott (Treasurer-Tax Collector, SMC)**

   Sandie Arnott reported on the annual audit that was conducted by Macias Gini & O'Connell LLP, for fiscal year 2024-25, there were no exceptions noted. Sandie also noted the Treasurer's Office will be reviewing the investment policy page-by-page with plans to have the policy certified by California Municipal Treasurers Association (CMTA). The team will be conducting a thorough review to determine if there are any changes that need to occur for the Board of Supervisors' approval in January 2026. Since this will be the Treasurer's Office's first certification, it's important to ensure the investment policy meets the state's standard. The cost of the certification will be $175, and Sandie will update the team at the next Treasury Oversight Committee (TOC) meeting in October 2025 of any updates or changes.

5. **INVESTMENT REPORT - Tiffany Htwe (SMC), Ken Schiebel & Meredith Sullivan (PFM)**

Tiffany presented the liquidity-investment maturities and cash flow analysis as of April 2025, highlighting the cash portfolio between PFM and the Treasurer's Office. She explained that the team consistently reviews historical cash flow to ensure the investment portfolio strategy is adjusted periodically in response to changing cash positions and financial activities, such as general obligation funding bonds, property tax income, and year-end cash withdrawals.

She then presented the County's 24-month cash flow projections. Tiffany noted that, together with funds held in bank accounts, all maturities are well structured to align with ongoing operational cash flow requirements. She emphasized that the County's priorities remain principal protection and liquidity.

Tiffany also reported that the portfolio has grown steadily over previous years, showing consistent improvement in the pool's average balance. She concluded by sharing that the current pool balance exceeds $9 million.

Tiffany displayed the cash management portfolio that she and her team oversee and explained that all investments are well-diversified and in strong positions. She noted that, beginning in April 2025, an industrial allocation chart was added to the monthly report to further enhance transparency around the County's investments.

Tiffany went on to share that she, Sandie, and Angela met with the Council on American Islamic Relations (CAIR) on April 3, 2025. During that meeting, CAIR inquired about specific investments and companies with potential exposure to the Israel war, particularly Caterpillar, Inc. Tiffany explained that, after verifying in Bloomberg, Caterpillar is categorized under Construction Machinery. Sandie also provided a thorough explanation of the existing socially responsible investment objectives within the policy. She further emphasized that the County's portfolio has no exposure to petroleum or defense-related investments, based on the official descriptions of the holdings.

Connie Mobley-Ritter asked Tiffany about the $20 million difference between par value and market value. Tiffany responded that the market values were down across the categories due to volatility in April. Overall, the portfolio shows a net unrealized market gain of $94.06 million when comparing market value to cost, despite an $88.06 million loss vs. par value as a reflection of market price fluctuations.

The portfolio is well-diversified across safe and stable investments like Treasuries, agencies, corporate bonds, CDs, and LGIPs, which helps maintain strong liquidity and resilience. Although market shifts caused the County's holdings to dip below par, the overall value remains higher than the original cost which is a positive sign. Additionally, with a GASB factor of 1.01, the market is pricing in a slight premium to the portfolio, indicating strong positioning.

Stephanie Osaze asked about the allocation of investments between PFM and the County. Tiffany explained that the allocation percentages can shift depending on market conditions and where funds are best placed. PFM manages the County's core portfolio with a focus on long-term performance. When market conditions make it less favorable for us to reinvest internally, we allocate more to PFM for longer-term strategies. At the same time, the County maintains a range of strong short-term investment options, including CalTRUST, CAMP-Term, Agencies and U.S. Treasuries.

Robert Manchia noted that budgeting interest earnings based on current market conditions may not be sustainable over the next few years, as unexpected changes can occur. The Federal Reserve has indicated that a rate cut is likely at its next meeting. As a result, we should not expect to continue earning around 3.85%; rates are more likely to move closer to 2%.

Connie also asked about the Federal Reserve's policy and where we are headed, given that interest rates are expected to fall. She wanted to know if we are planning to extend the duration of the portfolio further to lock in some of the current rates. Ken Schiebel responded that over the past couple of years, when rates had been elevated, the Federal Reserve engineered a series of increases in 2022. Since then, rates have continued to rise but began to decline in the fourth quarter of 2024. PFM has been using that opportunity, where feasible, to reinvest at longer durations. Their strategy is to lock in current yields, which remain attractive from a historical standpoint. Some of the highest yields since the 2008 financial crisis were seen in early 2024, and while they have since moderated, they remain elevated relative to expectations for where the Federal Reserve is headed. He explained that the Federal Reserve is in a difficult position because current administration policies are negative for growth but positive for inflation. While the Fed supports both full employment and economic growth, its priority is combating elevated inflation. The expectation is that the first rate cut might not occur until September 2025, though this depends on how economic conditions evolve. Additional cuts could follow in the fourth quarter or into next year. PFM does not expect the Federal Reserve to return to near zero rates as seen after COVID or the 2008 financial crisis. Instead, the floor for short-term rates now appears to be roughly 3%. They believe that the steady state in a normal environment where prices and employment are stable will likely settle closer to 3%, though it may take another year or longer to reach that point.

Ken introduced Allison Kaune to the committee explaining she is a senior client service representative for PFM. Allison has worked for the firm for more than 17 years, and she is replacing Richard Babbe who retired on March 31, 2025.

Ken reported that U.S. tariffs have risen significantly, with the average rate now around 13% compared to 2.3% prior to April 2025. Current policies impose a 10% tariff on most imports, 25% on steel, aluminum, automobiles, and auto parts, and 25% on certain Canadian and Mexican goods outside the USMCA, while partial rollbacks on China tariffs still leave effective rates elevated. He noted that every 10% increase in tariffs is estimated to reduce GDP by about 1.4%. In the first quarter of 2025, GDP contracted 0.3% due to trade impacts, and tariffs are expected to add roughly 1% to inflation, already above the Federal Reserve's 2% target. Ken emphasized that the elevated tariff environment poses risks to both economic growth and inflation going forward.

Ken presented key insights from the investment update, beginning with consumer sentiment, which has fallen to one of its lowest levels in 40 years as households worry about jobs, tariffs, rising costs, and recession risks. Consumers currently expect prices to rise 6.5%–7% over the next year, leading to hesitation on major purchases, while companies are delaying capital investments due to uncertainty. He noted that GDP, which was strong in late 2024, has weakened, with Q1 2025 showing a negative 0.3% reading and forecasts revised downward following the April tariff announcement. On inflation, recent monthly readings suggest a pace of about 2.5%, but economists expect it to rise as high as 3.5% by year-end. Ken cautioned that tariffs complicate both demand and pricing, higher costs could reduce consumer spending and leave businesses holding excess inventory. If inflation rises above 3%, the Federal Reserve may hold rates at elevated levels longer or even raise them, while a rise in unemployment toward 5% could prompt rate cuts. Meanwhile, the labor market remains resilient, adding 177,000 jobs in April, though unemployment is projected to climb from 4.2% toward the mid-4% to 5% range.

Connie asked if lower unemployment was mainly from government cuts. Ken said the impact is minimal, about 0.2%, and broader economic conditions will drive trends.

Ken highlighted recent market volatility, noting that two-year Treasury yields swung by 30–40 basis points in a single day following the April 2 tariff announcement, leading President Trump to pause the tariff due to its impact on bond and stock markets. Equity market swings have influenced expectations for Federal Reserve rate cuts in 2025, which at one point were priced at five but have since settled closer to two, aligning with the Fed's outlook. On yields, long-term Treasury rates remain in the mid-to-high range, with the two-year around 4% and the five-year slightly higher, while short-term rates are lower due to a 1% Fed rate cut in late 2024. Although yields remain elevated, they are still considered attractive compared to the near-zero levels seen in the post-financial crisis era and after the COVID pandemic.

Meredith presented the County's portfolio structure, highlighting strategies to maintain liquidity while generating high-quality returns. The County internally manages short-term, government-type securities for immediate liquidity, while PFM oversees several portfolios: CAMP TERM, a short-maturity vehicle under one year; PFMAM Managed Short-Term, targeting short-term credits like commercial paper and CDs in coordination with Tiffany to optimize yields and manage excess liquidity; and the Core Portfolio, focusing on securities with one- to five-year maturities and longer durations.

Meredith presented the County's aggregate portfolio as of April 30, 2025, with a total market value of $9.5 billion and a core portfolio of $4.2 billion. The aggregate duration is 1.97 years, and the core duration is 2.06 years, below the 2.5-year target due to market volatility and intraday yield swings. Yield at cost has risen to 3.38%, and as maturities totaling $600 million are reinvested, the portfolio can move closer to target duration. Initially expecting four to five Federal Reserve rate cuts, forecasts now call for two, with the first in September 2025, allowing opportunities to lock in current yields across the curve. Average purchase yield remains around 85 basis points due to post-COVID lower interest rate investments.

Meredith noted that the core portfolio is well-diversified across high-quality issuers and has focused on extending duration since rates peaked in late 2023. When Connie asked about the recent S&P Treasury downgrade, Meredith said the impact is negligible. A minor rate selloff occurred but quickly reversed, and no changes to the investment strategy are needed, as PFM had anticipated the potential downgrade.

Meredith noted minimal changes in sector allocation from 2021–2025, with reductions in CDs to extend portfolio duration and increased U.S. Treasury holdings due to tight credit spreads in 2024. Since February 2025, most purchases were in Treasuries with attractive yields, along with selective corporate offerings from BNY, Procter & Gamble, Colgate, Palmolive, and Toyota. Credit spreads widened post-April 2, 2025, allowing opportunities to increase portfolio duration toward the 2.5-year target for the one-to-five-year Treasury index. The gap between book yield and market yield is narrowing and is expected to continue as ultra-low-yield assets roll off and are reinvested. Earnings, which hit a low in 2022, are projected to grow as yields rise and reinvestment continues, allowing the portfolio to catch up to market yield. Even if rates fall, reinvesting along the curve can help lock in higher yields.

Tiffany asked about opportunities in asset-backed securities, and Meredith confirmed they are allowed under state and county policy. While past accounting challenges limited use, they can revisit allocations since these securities are highly rated, offer good value, and typically provide 40–50 basis points over Treasuries with 2–2.5-year durations. Tiffany noted prior accounting issues but expressed interest in reviewing allocations if PFM identifies strong opportunities.

Connie raised concerns about investing in credit-based asset-backed securities amid rising unemployment and potential credit card losses. Ken explained that they only invest in AAA-rated tranches, primarily prime auto loans or high-quality credit card receivables, which are structured with excess collateral, strong credit enhancements, and robust repayment safeguards. While some credit card delinquencies have risen, these securities pay down over time with increasing support relative to the balance. Connie cautioned that economic downturns remain likely, but noted the portfolio's allocation to asset-backed securities is minimal and unlikely to have a major impact.

Virginia asked about higher-end corporates, and Ken highlighted that while supply was strong early in 2025, it slowed with tariff-related volatility but has since stabilized and remains decent, though not as robust as last year. New issues still provide the best entry point with yield concessions, and there are quality issuers available on the approved list. Ken also noted that as low-yield investments from 2020–2021 roll off through 2026, reinvestment at today's higher yields will continue improving the overall book yield.

6. **ORAL COMMUNICATIONS AND PUBLIC COMMENT**
None

7. **OTHER BUSINESS**
None

8. **ADJOURN**
The meeting was adjourned at 12:59 p.m.

Daneca Halvorson (Chair)

Sandie Arnott (Treasurer-Tax Collector)