BREMEN TOWNSHIP
TRUSTEES OF SCHOOLS

ANNUAL INVESTMENT REPORT
FISCAL YEAR ENDING JUNE 30, 2020

"An investment in education always pays the best interest"

- Benjamin Franklin

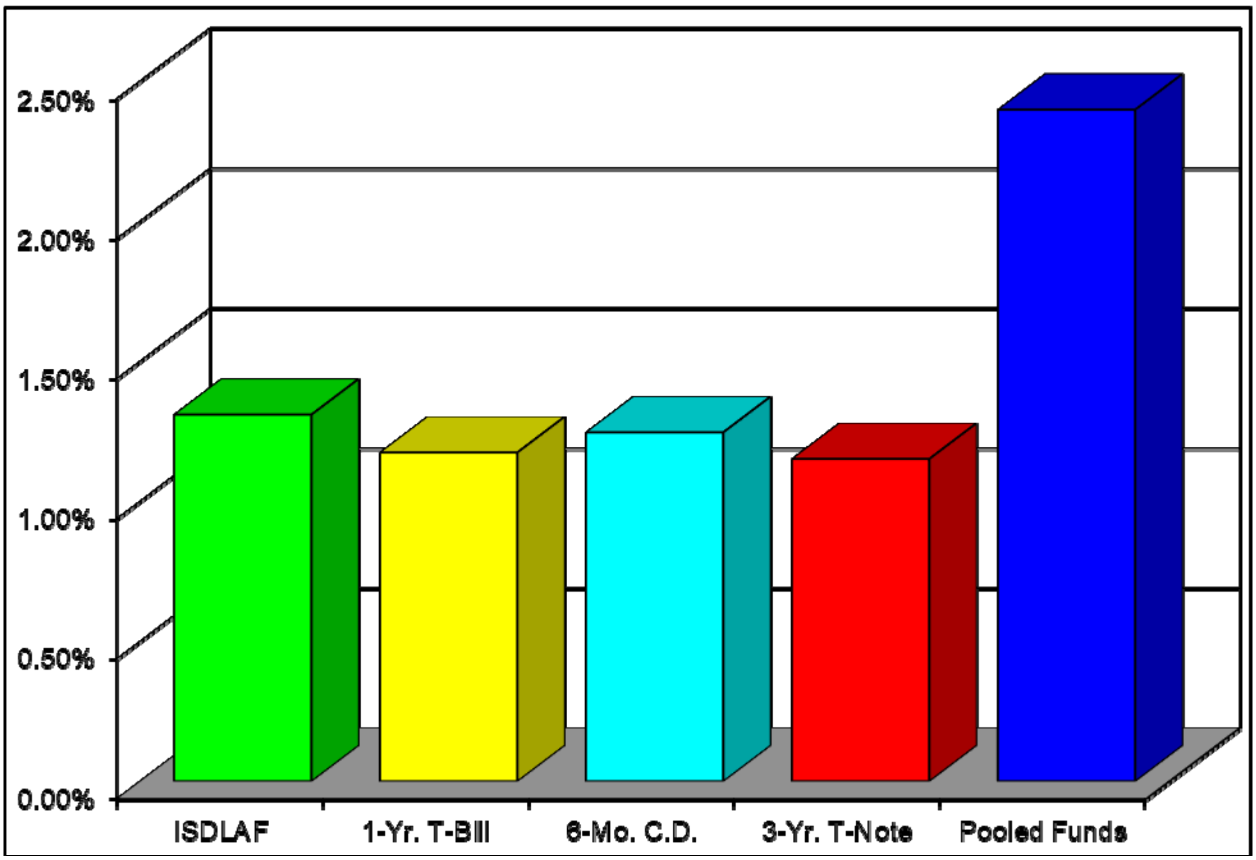
INTRODUCTION

The purpose of this report is to provide information to the administration and board members of the school districts that are serviced by the Bremen Township Trustees of Schools related to their funds for which we serve as custodian. All school districts that receive this report have their general funds invested in a pooled portfolio that consists of the funds of all the districts serviced by this office. Each district owns a portion of the pool based on their level of cash as a percentage of the entire cash being managed in the pool. There are many benefits to this investment structure, such as greater diversification, better liquidity and higher interest rates. Interest from the pooled funds is distributed to the districts based on their percentage of the fund.

The following report is divided into four sections. The first section will summarize the pooled fund's performance for the fiscal year ending June 30, 2020. The second section will provide a historical review of interest rate trends. The third section will analyze current market conditions and discuss the current portfolio as it relates to these conditions. The final section describes the general investment policy of the Bremen Township Treasurer's Office.

SUMMARY OF FISCAL YEAR INVESTMENT ACTIVITY

For the fiscal year ending June 30, 2020, I am pleased to report that the investment pool managed by the Bremen Township Treasurer's Office generated $3,638,902 in interest earnings to the school districts serviced by this office. With an average investment portfolio of $162,988,652 the cash basis rate of return for all the school districts was 2.23%. The yield on short-term investments ranged from 0.15% to 2.12% during the fiscal year. Overall, the average yield on pooled funds managed by this office for the fiscal year was 2.40% and the average yield on funds that were held for liquidity purposes were 1.51%. The current yield on the portfolio as of June 30, 2020 is 2.15%, which represents the annualized current rate of return on June 30th. The following graph compares the average monthly yield on the pooled funds with that of other investments available in the market during this same period:



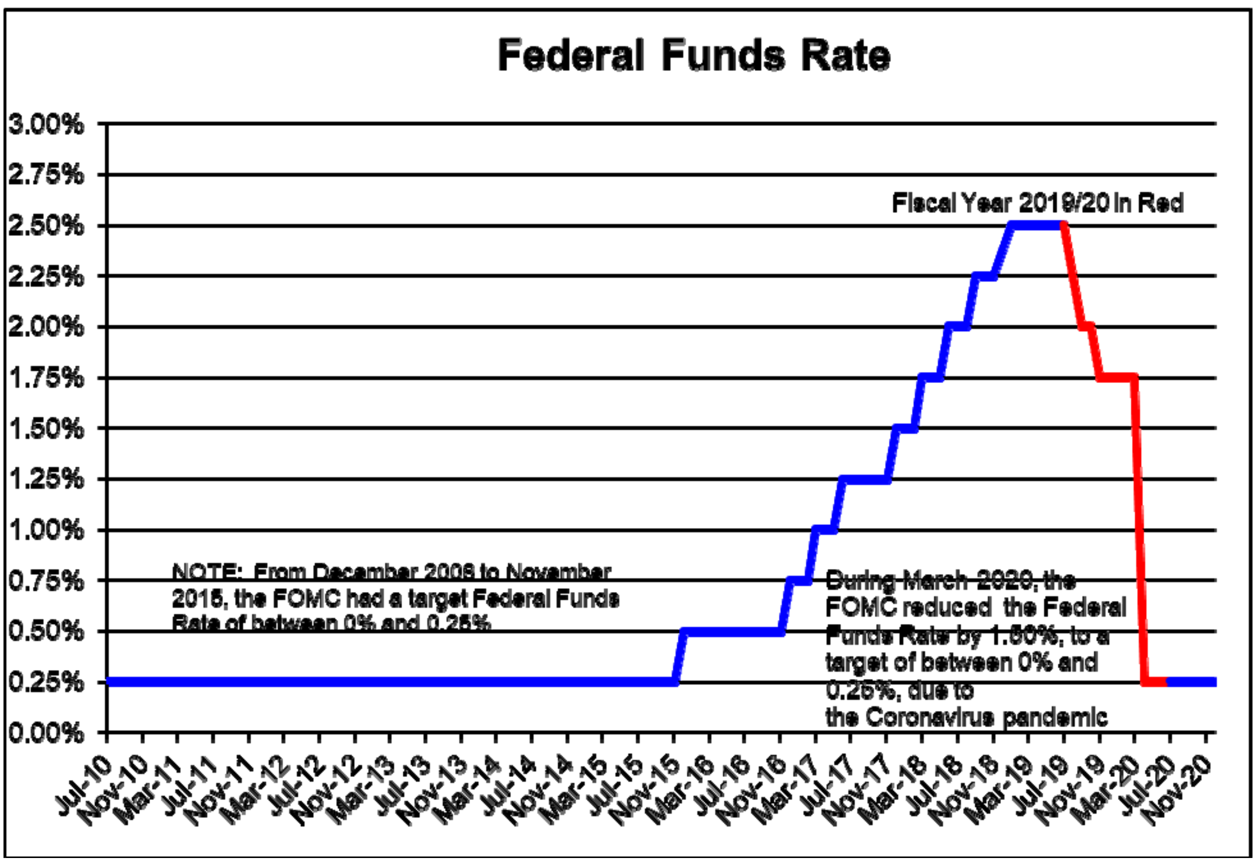
The average yield from the Illinois School District Liquid Asset Fund (ISDLAF) for the same time period was 1.31%, the one year Treasury Bill was 1.17%, the six month Certificate of Deposit averaged 1.25%, and the three year Treasury Note averaged 1.15%. The weighted average maturity on the pooled funds managed by this office was 0.36 years (131 days) as of June 30, 2020.

INTEREST RATE MOVEMENT AND ECONOMIC OUTLOOK

Between December 2015 and December 2018, the Federal Reserve raised short-term interest rates nine (9) times, bringing the Fed Funds rate up to 2.50%. Then, in a dramatic reversal, the Federal Reserve lowered rates in one-quarter of one percent intervals three times: in July, August and October of 2019 down to 1.75% with the stated objective of continuing to strengthen economic growth in the USA. By all accounts, the policy was effective, and several economic indices showed significant improvement. Then came the COVID pandemic, and with it, all economic growth came to a grinding halt. In response to the economic shutdown, the Federal Reserve slashed the Federal Funds rate by 0.50% on March 2, 2020 and an additional 1% on March 15, 2020, bringing the rate back to its historically low level of 0.25%. In all, the Federal Reserve decreased rates five (5) time during the 2020 fiscal year.

The statutory mandate of the Federal Open Market Committee ("FOMC") is to foster maximum employment and price stability. At this point in time, the FOMC is looking for maximum employment and two percent inflation. In determining the timing and size of future interest rate adjustments, the Committee assesses realized and expected economic conditions relative to its objectives. This assessment takes into account a wide range of information, including measures of labor market conditions, indicators of inflation pressures and inflation expectations, and readings on financial and international developments.

The following graph reflects movement in the Federal Funds Target Rate since July 2010:

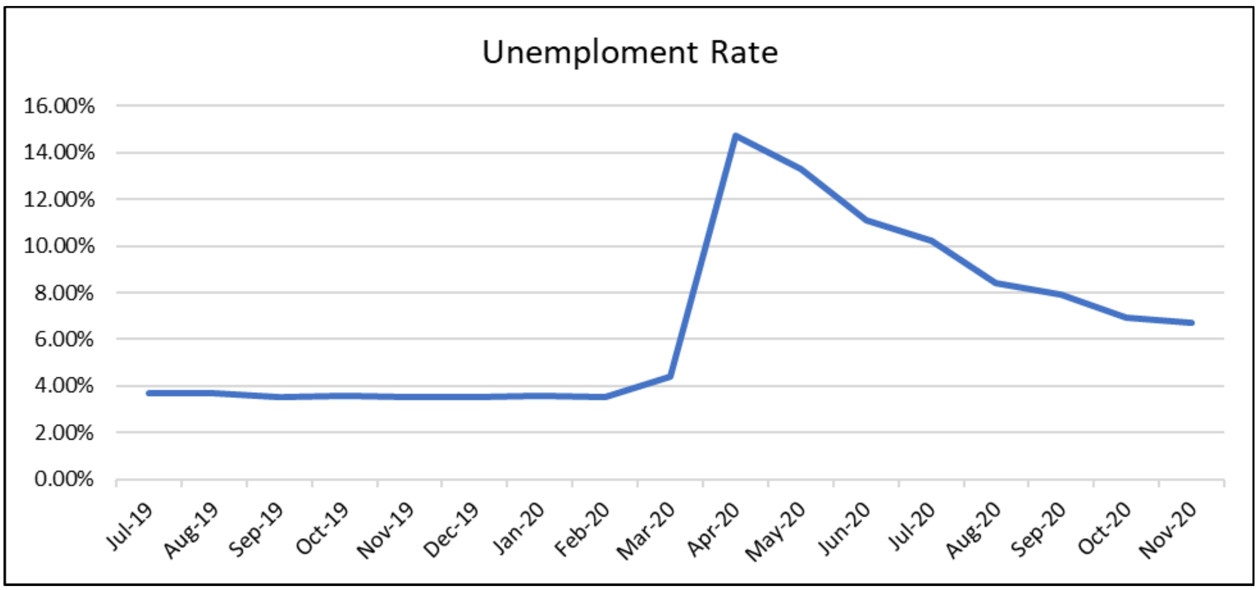


Statements made and action taken by the Federal Reserve primarily impact short and intermediate term rates, and subsequently the yield on our pooled investments. It is therefore relevant to monitor and assess both action and inaction taken by the Fed.

In an effort to mitigate the effects of a global pandemic on our economy, the Federal Reserve acted swiftly and boldly to the pending crisis. In addition to dramatically lowering interest rates, the Federal Reserve rolled out a variety of programs, throwing lifelines to individuals, corporations, States and other municipalities through its special facilities and programs. As a result of the Fed's steep interest rate cuts and bond buying program, interest rates dropped dramatically to near zero for all fixed asset classes.

In responding to these actions, Chairman Powell stated "…we have lowered interest rates to near zero in order to bring down borrowing costs. We have also committed to keeping rates at this low level until we are confident that the economy has weathered the storm and is on track to achieve our maximum-employment and price-stability goals."

Perhaps the most glaring effect of COVID on the economy is reflected in the unemployment figures. The following chart reflects the monthly unemployment rates from January 2019 through November 2020:

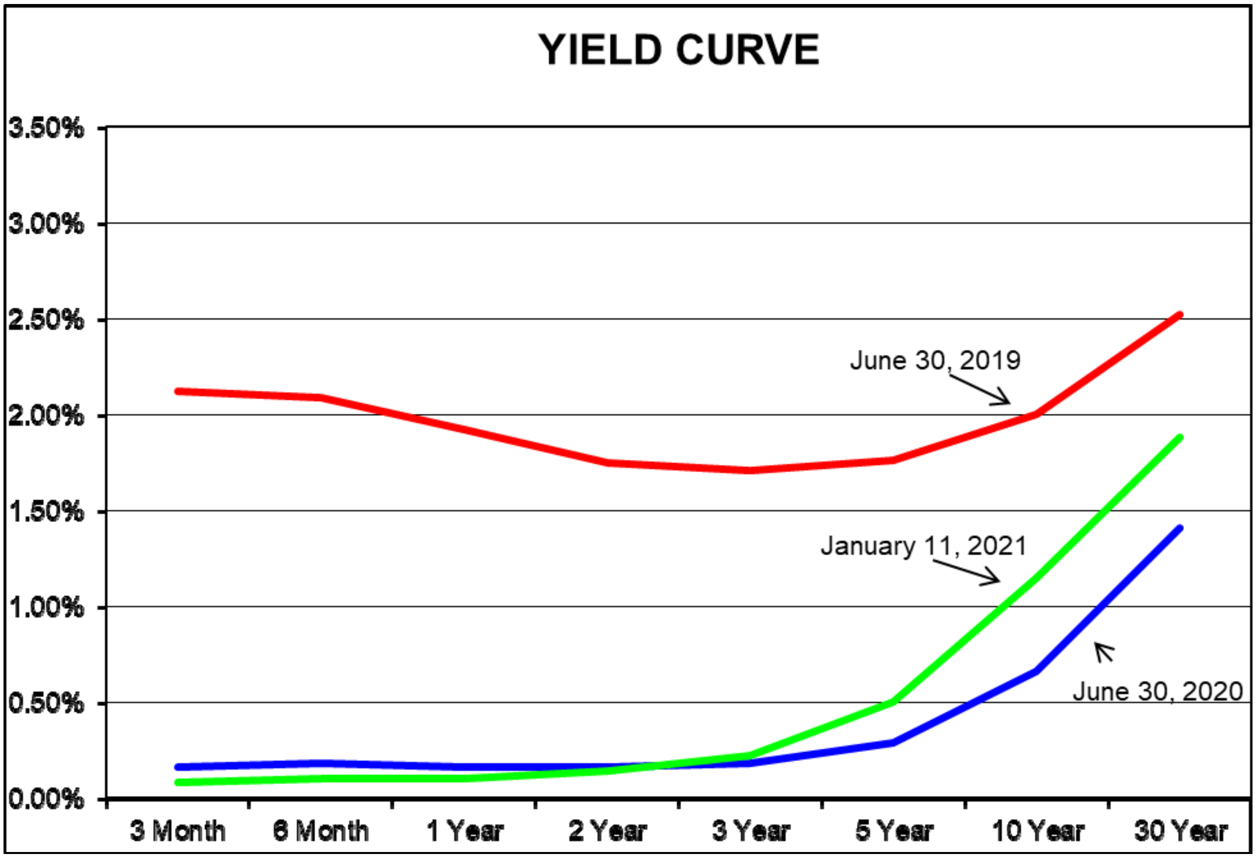


The above chart illustrates that prior to COVID, unemployment was at historically low levels. Then once COVID hit and States mandatorily closed businesses, an additional 10% of the workforce became unemployed almost instantaneously. Since the initial economic shutdown, most states have opened up somewhat and consequently unemployment rates have trended down each month since April 2020. The unemployment rate, however, remains above pre-COVID levels and the Federal Reserve will likely maintain policies that attempt to stimulate the economy until at least the time that unemployment rates get back to pre-COVID levels.

Even under an optimistic scenario for the distribution of a vaccine, most economists do not expect any major policy change from the Fed for the next several years. It will take time for the economy to rebound to pre-pandemic levels. The economy has only recovered about two-thirds of the gross domestic product (GDP) growth that it lost during the downturn and is still growing at a rate well below its potential. Consequently, inflation is not likely to be a risk until economic growth closes the gap by reaching its potential and exceeding it for a period of time. Under the Fed's new guidelines, it will not begin to tighten policy until inflation actually goes above its 2% target for a sustained period of time. Most economists doubt those conditions will be met until sometime in 2022 or later. Currently, the market expects the Fed to keep interest rates on hold until at least the end of 2023.

As a result of this expectation, the yield curve out as far as the 3 to 5 year part of the curve continues to hover at painfully low levels (0.01 – 0.20%). There is some upward slope in the yield curve beyond five years with an expectation that the economy would be gaining momentum in 2021. On January 11, 2020, the most watched part of the yield curve, which measurers the gap between yields on two and ten year Treasury notes reached its widest level since May 2017 at nearly one percent.

The following graph illustrates the yield curve on June 30, 2019, as compared to June 30, 2018 and a more recent date of January 11, 2021.



From June 2019 to January 11, 2021, the yield on U.S. Treasury securities maturing on the shortest end of the curve experienced the greatest declines. The three-month yields decreased from 2.12% to 0.08% and the five-year yields decreased from 1.76% to 0.50%. On the longer end of the curve, the drops were significantly less extreme. The ten-year yields decreased from 2.00% to 1.15% and the thirty-year yields decreased from 2.52% to 1.88%.

It is not so difficult to understand what is occurring at the short end of the yield curve, as this is the part over which the Fed exercises more direct control. What's going on at the long end of the curve gets complicated. This is the part of the yield curve that is more influenced by investor's expectations, including market sentiment and inflation expectations. The current yield curve reflects the expectations that the economy will gain momentum from its current levels.

Putting the change in interest rates over the past few years in perspective, the following summarizes the approximate short-term rates available in the marketplace for investing second installment real estate tax collections:

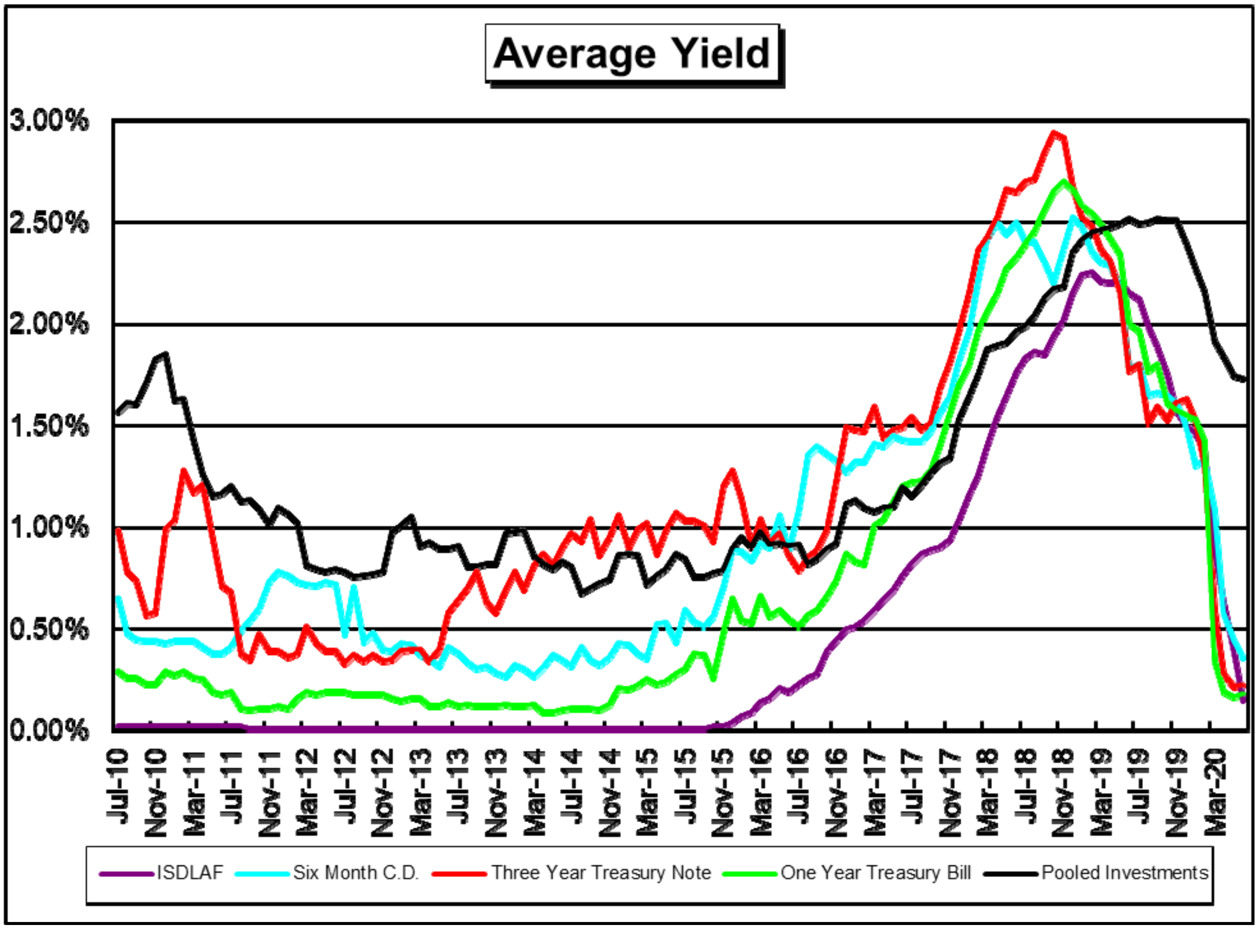
	Investment Rates
Fall of 2013	0.01% - 0.10%
Fall of 2014	0.01% - 0.10%
Fall of 2015	0.01% - 0.10%
Fall of 2016	0.10% - 0.30%
Fall of 2017	0.75% - 1.25%
Fall of 2018	1.80% - 2.10%
Fall of 2019	1.80% - 2.20%
Fall of 2020	0.02% - 0.20%

As we look into 2021, there are events that will certainly change the trajectory of the economy to some degree. Many experts believe that with the likelihood of vaccines for the coronavirus becoming widely available by mid-year, the economy could get a boost if the increased vaccination rates translate into easing of the economic lockdown in those States which remain fairly restricted. We are also expecting a rather large fiscal relief package that may also have a positive impact on economic growth. Finally, with the advent of the Biden era, tax policy, infrastructure packages, changes to regulation and trade deals all may have an impact on economic growth perhaps both positively and negatively.

There exists great uncertainty, however, on what the economic recovery will exactly look like due to the extraordinary economic circumstance created by the pandemic. Huge segments of the small business and service sectors have been wiped out and will have to be rebuilt. The future of commercial real estate has been fundamentally changed as businesses have adopted to work-from-home arrangements. Residential real estate is undergoing a massive boom as new home building trends, living preferences and Americans leaving cities have reshaped the industry. Travel, hospitality, energy and retail sectors have all been upended.

It is important to recognize, however, that while markets constantly change and interest rates have moved rather dramatically over the past several years, the yield on the pooled funds investment portfolio has remained relatively stable.

The following graph reflects interest rate patterns on the pooled funds and other investment vehicles over the past ten years and illustrates the relative stability of our pooled funds both in times of decreasing and increasing interest rate environments:



In analyzing the relative stability in the weighted average yield of the pooled investments, it is important to note that this is not a stagnant portfolio where rising interest rates have no benefit to our pooled fund holders. We receive in excess of $300 million in revenues annually into the pooled funds. While our core portfolio is affected adversely by rising interest rates, this same rise in rates provides us the opportunity to invest new funds at higher rates of interest. The reverse is true in times of declining rates. While the value of our portfolio rises, new revenues are invested at lower rate levels, driving down the yields, but the core portfolio buffers the decline. As a result, our returns are less volatile during both rising and decreasing rate environments.

CURRENT INVESTMENT STRATEGY

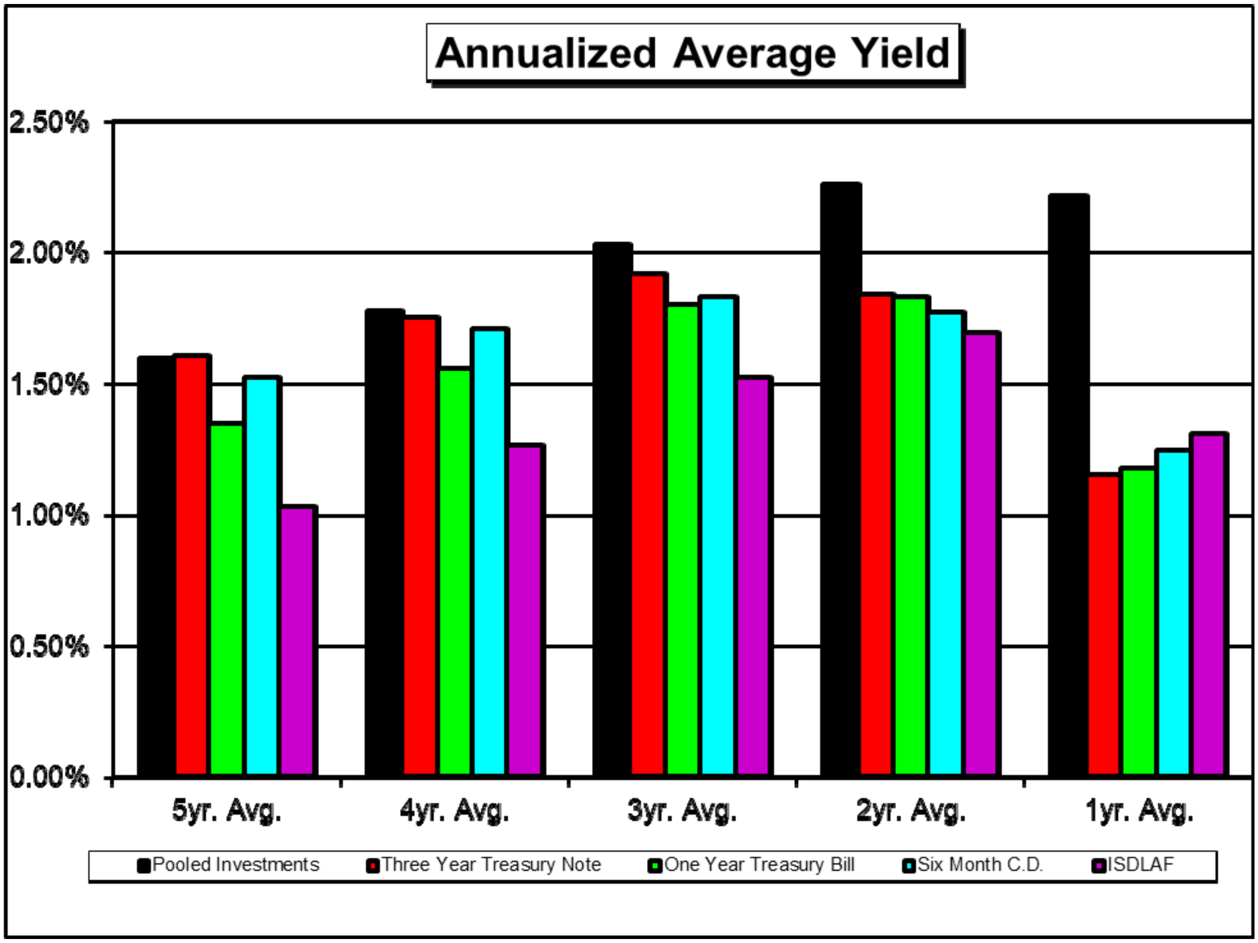
Since a significant percentage of the funds received by this office must be invested to meet short-term cash flow needs, interest rate direction is not the primary factor in investment decisions. It is important, however, to consider current interest rate conditions, yield curves and future interest rate trends in determining the overall desired duration of the portfolio.

With a backdrop of (1) historically low interest rate levels out at least five years on the yield curve; (2) money market yields at almost zero percent and (3) the prospects of an accelerating economy that may produce increasing interest rate levels out in the longer end of the yield curve, our primary investment duration target has been in the six-month to three-year range. This allows us to earn yields greater than money market funds yet also allows us sufficient liquidity in the future to capitalize on rising interest rate levels.

In addition, we continue to look at value amongst the investment vehicle options available to us. We currently are focusing on purchasing bank CD's and short-term taxable municipal bonds. We are also an active investor in in the direct purchase of municipal bonds from the school districts serviced by this office and other school districts in Illinois. These strategies have allowed the portfolio to maintain some yield above the levels that exist in money market accounts and traditional short-term investments, without compromising the objectives of the fund. We are also focused on issues that will provide above average yields that are in the three to five-year maturity range.

While risk in the credit markets seems to have diminished, we still respect the uncertainty that exists in the near future, and are concerned about the possible effects of unforeseen events on our economy and our fixed income markets. We will continue to strongly weigh all investment decisions towards maximum safety and liquidity until we are confident in the overall direction of our Federal, State and local economies.

A major benefit of pooling funds for investment purposes is the ability to invest in longer term maturities that enhance the yield on the portfolio. Although most of our investments have been in the shorter end of the yield curve, the flexibility to invest in longer term maturities has proven beneficial to the investment pool. This strategy has consistently allowed the pooled funds to compare favorably to other investment alternatives. As seen in the following graph, the five-year average interest rate yield on the pooled investments has performed well, compared to all other investment vehicles presented below.



The five-year average yield on the pooled investments was 1.59%, the three-year Treasury Note was 1.61%, the one-year Treasury Bill was 1.34%, the six-month CD was 1.52%, and the ISDLAF was 1.03%. The higher five-year average interest rate yield on the pooled funds of 0.56% above the ISDLAF average rate has generated close to $3.5 million of additional interest earnings over the prior five-year period. This higher interest rate yield is primarily due to our strategy in managing the pooled investments.

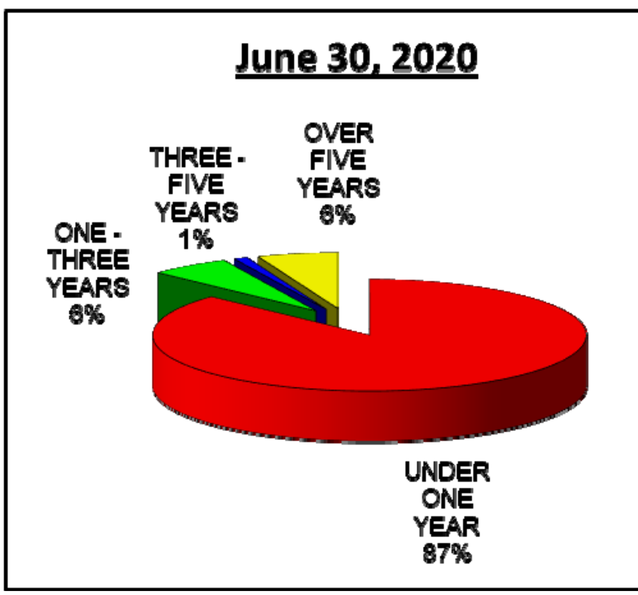
CURRENT PORTFOLIO

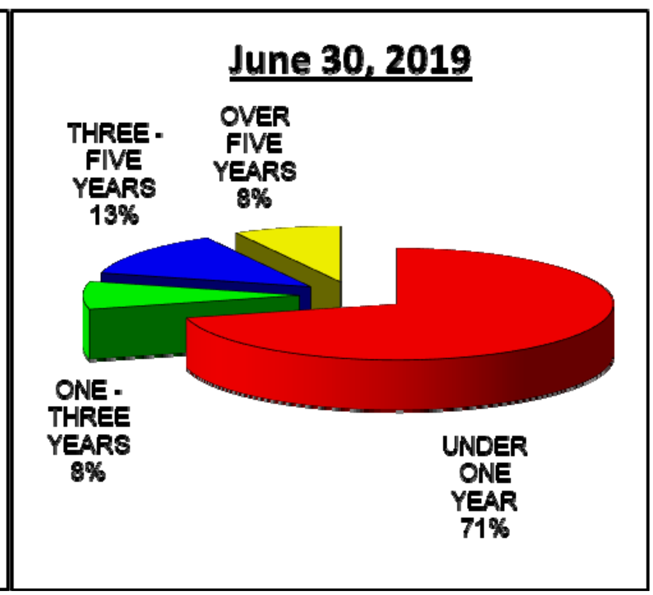
Over the past fiscal year, we have been investing in an interest rate environment that was first characterized by rapidly declining interest rates that brought rate levels down to flat unattractive rate levels throughout the area yield curve, where we normally invest funds. We remain in a rate environment in which there is little current value in extending the duration of the portfolio due to the flat yield curve. Consequently, with the exception of value purchases in the 1 to 3 year maturity range, new money into the portfolio was primarily placed in shorter maturities to meet cash flow needs.

On June 30, 2020, the expected maturity of the portfolio was laddered with consideration of the yield curve, anticipated cash flow needs and anticipated new revenues coming into the portfolio. For example, it is not critical to have maturities coming due in August and September, because that is the time that significant new real estate tax revenues come into the portfolio to cover payrolls and bills coming due in those months.

On June 30, 2020, 93% of the current pooled funds portfolio is expected to mature within three years. The percentage of the portfolio maturing in less than one year remained higher at 87% on June 30, 2020. The percentage of investments maturing in the one-three year range decreased from 8% to 6% of the portfolio. Investments maturing in the three-five year range decreased from 13% to 1% of the portfolio. Investments maturing in excess of five years decreased slightly from 8% to 6% of the portfolio.

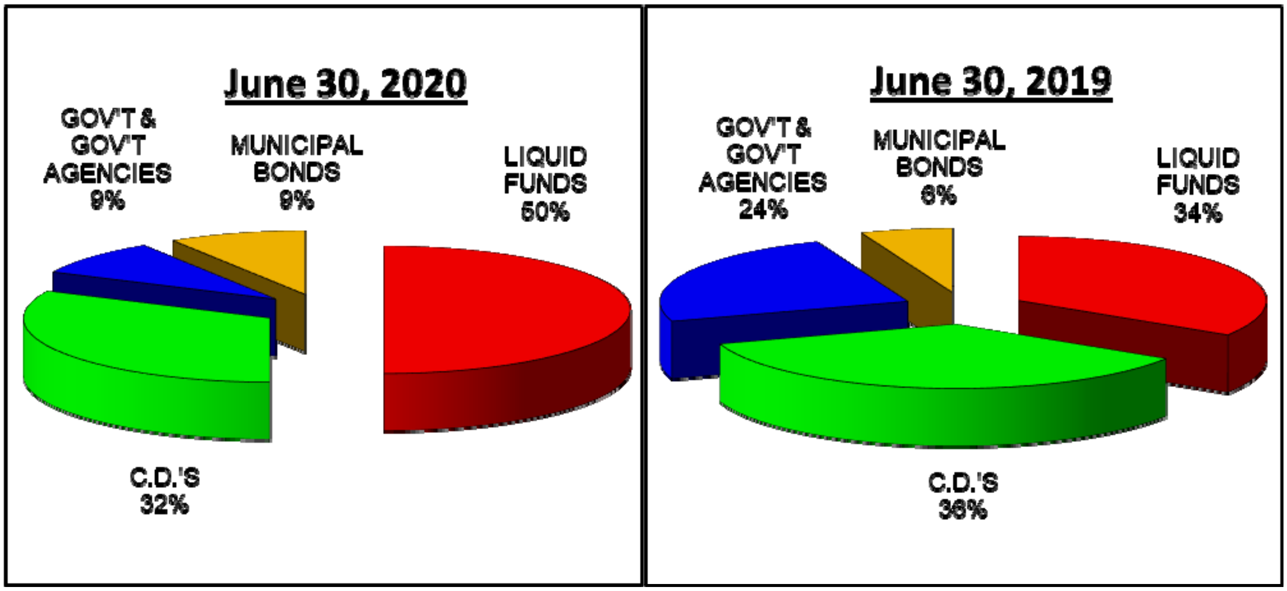
The following graph reflects the allocation of the portfolio by expected maturity date on June 30, 2020 as compared to June 30, 2019:





Although funds received by this office must be invested to meet short-term cash flow needs, we have a portfolio that gives us the opportunity to consider current interest rate conditions, yield curves and interest rate trends in determining an overall desired duration of the portfolio. As of June 30, 2020, these indicators implied the use of a more liquid portfolio, which would afford us more flexibility in implementing our investment strategy. The weighted average maturity of the portfolio was 0.36 years (131 days) on June 30, 2020, compared to 0.54 years (197 days) on June 30, 2019.

Not only is diversification of maturities essential to the performance of the portfolio, but diversification of investment types is equally important. Diversification not only minimizes the risk in the portfolio, but also allows us the ability to consider the entire investment arena in determining which investments will maximize yields while emphasizing safety. As of June 30, 2020, the pooled funds consisted of almost 100 different investments that are regularly monitored. The following pie chart reflects the investment composite of the pooled funds as of June 30, 2020 as compared to June 30, 2019:



As can be seen from the pie chart above, 50% of the pooled funds were invested in liquid funds, 32% in C.D.'s, 9% in government/government agency obligations and 9% in municipal bonds. The composition of the portfolio in terms of investment type remained relatively stable. Our percentage of C.D.'s and government/government agency obligations decreased, primarily due to the need for more liquid funds. We continue to remain active in the government agency securities market, which gives the pooled funds the credit strength of U.S. Government backed securities, with higher rates of return. As mentioned previously, we also continue our focus on purchasing short-term municipal bonds from taxing bodies in Illinois.

There are six major categories of investments available to the pool as of June 30, 2020:

1) **Liquid Funds** - These comprise funds readily available for withdrawal at any given notice and include regular checking, deposit, and money market fund accounts.

2) **Certificates of Deposit** - These are direct obligations of a United States bank which are fully insured by the FDIC up to $250,000 per entity or $2,250,000 of this pool per banking institution.

3) **Bank and Corporate Notes** – Bank notes are direct obligations of United States banks which are members of the FDIC. The banks must achieve size and profitability requirements in order to be eligible for investment. Corporate Notes are direct obligations of large U.S. Corporations that meet the stringent criteria established in the Illinois Public Funds Investment Act.

4) **Commercial Paper** - Commercial paper is a direct obligation of United States corporations having more than $500 million in assets. The maturity of such obligations must be less than 180 days. The corporations must also be rated in one of the three highest categories by the major rating agencies.

5) **Government and Government Agency Guaranteed and Collateralized Obligations** - These are investments that are guaranteed by the U. S. Government or its agencies. This also includes investments in which government/agency collateral has been pledged, as well as municipal bonds that are either insured or at the highest of rating categories.

6) **Municipal Bonds** - These are bonds issued by a city or other local government, or their agencies. Municipal bonds may be general obligations of the issuer or secured by specified revenues.

INVESTMENT POLICY

The following is a list of various policies that are followed by the Bremen Township Treasurer's Office when implementing its investment decisions:

MAXIMIZING INTEREST REVENUES

I. In order to maximize interest revenues on the funds received by this office, it is essential that all revenues earn interest as soon as this office receives them. We have streamlined our communications with the county, the state and the brokers we deal with to ensure that funds due to the districts are received promptly by our banks. We have increased the use of wiring funds wherever possible, rather than dealing with checks that greatly reduce interest earnings. At the same time, we have established agreements with the banks that service our office to allow us to earn interest on the funds on the same day that the wire is received.

II. Through the pooling of revenues of eight school districts serviced by this office, we have the ability to invest in $1,000,000+ blocks. This allows the districts' funds to be invested in instruments that would not otherwise be available in smaller lot sizes. Also, investing in $1,000,000 lots often gives us the ability to earn higher yields than if investing in smaller lot sizes.

III. The Treasurer's Office works with several different brokers who have access to investments throughout the country. This allows for more thorough investment decisions to be made.

IV. Although local banks may offer rates that are slightly lower than rates offered by other institutions, consideration is given to those local institutions which provide needed assistance to our school districts.

V. The Treasurer's Office consistently updates cash flow projections to allow pooled funds to be invested at higher yields for the longest duration possible. The balance in the liquid funds is targeted to be around 5% of the total pool.

VI. The Treasurer constantly monitors the investment and economic arena working with both fundamental and technical analysts in order to determine when investments should be purchased and sold, as well as to determine the desired weighted average maturity of the portfolio.

MINIMIZING RISK

I. All funds invested by the Treasurer's Office are invested pursuant to the Public Funds Act of the Illinois Revised Statutes and all legislation that has affected such act.

II. When Certificates of Deposits are purchased by this office, the CD's are designated as "multiple taxpayer ID deposits" to ensure that the purchase is within the aggregated FDIC insurance limits of this office, which is $2,250,000. If this is not sufficient to fully insure the investments, the CD's will be collateralized by the banking institution.

SUMMARY

There were two major objectives I had when preparing this report. The first objective was to provide an update to the administration and board members on the investment performance of the school districts' funds during the fiscal year ending June 30, 2020. The second objective was to assure the districts that all revenues, which are received by this office, are closely managed and to provide a partial list of the strategies, procedures and policies used by this office in order to ensure maximum investment performance of these funds.

We have been annually reporting our fund performance to the school districts we service for the past 25 years. In each of these years, we have performed well compared to all major financial indices we track. During that time, we have returned $74.8 million in interest earnings to the school districts we service. We take the responsibility of managing your district's funds seriously and know that the partnership we have developed over the years, combined with the inherent value of a pooled funds system and the consolidation of fiscal services, has provided substantial benefits to the taxpayers we all service.

In projecting interest earnings for the upcoming fiscal year, I expect returns on a cash basis to be significantly lower than those realized in fiscal year 2020 for two primary reasons: (1) Interest rates, and consequently reinvestment rates, are now at historically low levels; and (2) Investments that were purchased during a higher interest rate environment have either been called or matured over the past few years.

Our plans are to continue to produce this report on an annual basis. I would appreciate any suggestions or comments you may have. As always, if at any time during the year, information pertaining to the investment portfolio is desired, it will gladly be provided.

I thank you for letting us serve your district.

Joseph J. McDonnell
Bremen Township School Treasurer