SAN DIEGO COUNTY TREASURER-TAX COLLECTOR

MARKET WATCH

THIRD QUARTER | 2016

2.9%

U.S. GDP grew by 2.9% in the third quarter (+1.4% in Q2)

2.1%

Personal consumption growth decelerated to 2.1% from 4.3% in Q2

5.0%

The national unemployment rate rose modestly in Q3 from 4.9% to 5.0%

4.7%

Unemployment in San Diego County was 4.7% in September 2016

Orange	4.1%
Los Angeles	5.2%
Riverside	6.5%
California	5.3%

MARKET OVERVIEW

U.S. stocks advanced during the third quarter based on generally good economic data, especially in the areas of employment and housing, and a lack of rate actions by the Fed. The Dow Jones and S&P 500 indexes rose 3% and 4%, respectively, while the Nasdaq composite surged 10%.

The bond market overall ended the quarter approximately flat, though this masked fluctuations during the period and disparities in performance among sectors. Treasuries sold off across the curve, but longer-dated bonds again outperformed as the yield curve flattened. After reaching a record low of 1.37% on July 8, the yield on the 10-year Treasury note ended up 11 bps for the quarter at 1.60%. High yield was the best fixed income performer with a 5% return, while the municipal market was slightly negative.

Although markets expected the Fed could raise rates in Q3, policymakers decided to hold off due to mixed economic data and, later, the approach of the election. GDP growth rebounded, but concerns over weak inflation and slowing productivity prevailed.

Crude oil futures traded in a fairly narrow range and ended Q3 virtually unchanged at just over $48 per barrel. Gold prices were also quite stable, finishing at $1,317 per ounce.

UPCOMING EVENTS

CASH HANDLING WORKSHOP
February/March 2017

INVESTMENT SYMPOSIUM
Friday, February 10, 2017

FRAUD PREVENTION SEMINAR
Friday, August 4, 2017

DEBT SYMPOSIUM
Friday, November 3, 2017

Location:
CROWNE PLAZA HOTEL
2270 Hotel Circle North
San Diego, CA92108

Register online at www.sdtreastax.com

U.S. ECONOMY

U.S. GDP growth improved in Q3 to 2.9%, which was the highest reading in two years. The acceleration after Q2's 1.4% rate was driven by a 10.0% jump in exports and 3.1% growth in business investment, compared to a 7.9% decline in the prior quarter. Consumer spending, which accounts for more than two-thirds of economic output, experienced slower growth than the 4.3% jump seen in Q2, but still rose a fairly healthy 2.1%. 2.3% growth in imports was a slight drag on the GDP number. The national unemployment rate ticked up slightly in Q2 to 5.0% because of labor force growth, and wages continued to rise modestly. Inflation, however, remains below the Fed's 2% target, with the September PCE index (the Fed's preferred measure) at +1.2% year-over-year.

SAN DIEGO AREA ECONOMIC TRENDS

San Diego County's unemployment rate declined to 4.7% in September and remained below that of Los Angeles (5.2%) and Riverside (6.5%) Counties, California as a whole (5.3%), and the nation overall (5.0%). The rate declined 0.1% year-over-year as local nonfarm payrolls grew by 30,700 workers, or 2.2%. Private sector gains drove much of the employment growth, accounting for 24,100 new jobs, although the government sector also added 6,600 workers.

Within the private sector, the educational and health services industry posted the best performance, adding 7,600 jobs since September 2015, or a 3.9% increase. Most of these new positions were in health-related fields, indicating a core segment of our innovative local economy remains strong.

Other industries with significant year-over-year growth included professional and business services (+7,200 jobs), leisure and hospitality (+6,100 jobs), trade, transportation and utilities (+2,100 jobs), and financial activities (+1,700 jobs). Other than healthcare, specific subsectors that outperformed were architecture and engineering, administrative and support services, and restaurants.

The University of San Diego's Index of Leading Economic Indicators remained virtually unchanged during Q3. The Index hit its highest level in almost 10 years in April, but has since declined slightly as local construction activity has slowed. Still, modest economic growth is expected for the region over the near term.

The reduction in building permits highlights a primary area of concern for the local economy over the next few years: a lack of affordable housing supply. SANDAG estimates the region will need to add about 325,000 housing units by 2050 to accommodate demand, or about 12,000 per year just to keep up with population growth. The last year in which permits reached that level, however, was 2005. Even worse, the vast majority of permits are issued for properties only upper-income residents can afford. Just 7% of units approved in 2015 were valued below the median County home price.

Real estate values have risen to a point where over 70% of area residents cannot afford to purchase a median-priced home. These same residents have also been squeezed by rising rents; average rents are up 32% since 2000, despite median wages falling 2%. Clearly, this issue needs to be addressed to attract and retain the best workers, including millennials.

Nevertheless, it should be noted that San Diego County's median sales price in September of $569,000 is still lower than in other parts of Southern California, such as Orange County, and far below average prices in the Bay Area. Prices locally are rising faster than in most other areas, however, indicating the lack of supply is affecting our market.

Book Value
$7.44 B

Last Quarter	Last Month
$8.69 B	$7.55 B

Liquidity 0-1 Yr
65.24%

1-5 Year Maturity
34.76%

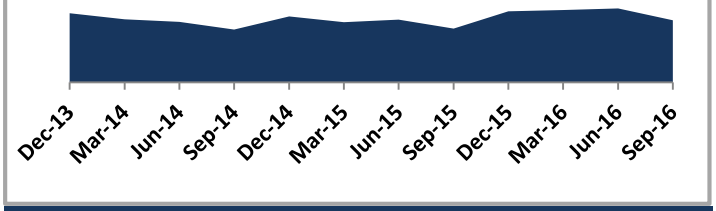
Asset Allocation
Top 3 Asset Classes

Federal Agency Paper – 29.31%
Negotiable CDs – 25.45%
Commercial Paper – 19.77%

Top 3 Pool Participants

K-12 Schools – 44.69%
County Funds – 34.35%
Community Colleges – 10.64%

12-Quarter Book Value Trend



Portfolio Summary Statistics

Performance Measure	*Sep. 2016*	*Sep. 2015*
Book Balance	$7,440,530,417	$6,448,187,297
Effective Duration	0.89 yrs.	0.81 yrs.
YTM	0.981%	0.58%
S&P Credit Rating	AAAf/S1	AAAf/S1

Investment Pool Valuation

	Q3-2016	Q3-2015
Market Value	$7,445,151,492	$6,456,480,043
Accrued Interest	$14,978,489	$8,573,856
Book Value	$7,440,530,417	$6,448,187,297
Net Unrealized Gain/(Loss)	**$4,621,075**	**$8,292,746**

The market value of the Investment Pool at the end of Q3 was $7,445,151,492, down from $8,698,263,281 at the end of Q2. Book value was $7,440,530,417, equating to an unrealized gain of $4,621,075. Current accrued interest was $14,978,489.

PORTFOLIO REVIEW

The County Pool's balance decreased from $8.7 billion to $7.4 billion during the third quarter due to planned seasonal spending, including annual outflows for County pension contributions, debt service, and school aid apportionment. The effective duration of the portfolio, which measures the overall sensitivity to changes in interest rates, rose from 0.65 years to 0.89 years because a significant amount of short-duration securities matured in the beginning of the quarter to fund these outflows. The yield to maturity of the portfolio increased from 0.85% at the end of Q2 2016 to 0.98% at the end of Q3. Year over year, the pool yield was up 40 basis points from 0.58% at Q3 2015. This was primarily the result of Federal Reserve actions and increasing yields in certain money market instruments ahead of money market mutual fund reform.

The pool maintained its AAAf/S1 rating from Standard and Poor's (S&P). This is the highest rating assigned by S&P and is a measure of the Pool's strong protection against losses from credit defaults. The S1 volatility rating signifies that the pool possesses low sensitivity to changing market conditions, given its low risk profile and conservative investment policies.

LIQUIDITY

Liquidity remains a primary objective in both the Investment Policy Statement (IPS) and in our strategy. Our IPS requires that at least 25% of the portfolio matures in 90 days or fewer and at least 50% matures within one year. There are no minimums for maturities over one year. The maximum maturity allowed is five years, and effective duration is capped at 1.5 years. As of the end of Q3 2016, we have 29% maturing within 90 days, 65% within one year, and 35% between 1 and 5 years.

PARTICIPANT BALANCES

The San Diego County Pooled Money Fund contains balances from several different categories of investors. County funds represent 34% of the portfolio at the end of Q3, down from 37% in Q2. The decrease was primarily due to normal spending, including annual outflows for pensions and debt service. The K-12 schools comprise 45% of the portfolio, unchanged from the prior quarter. Local community colleges, cities, agencies (both County and independent), and non-County funds make up the remaining 21% of the Pool.

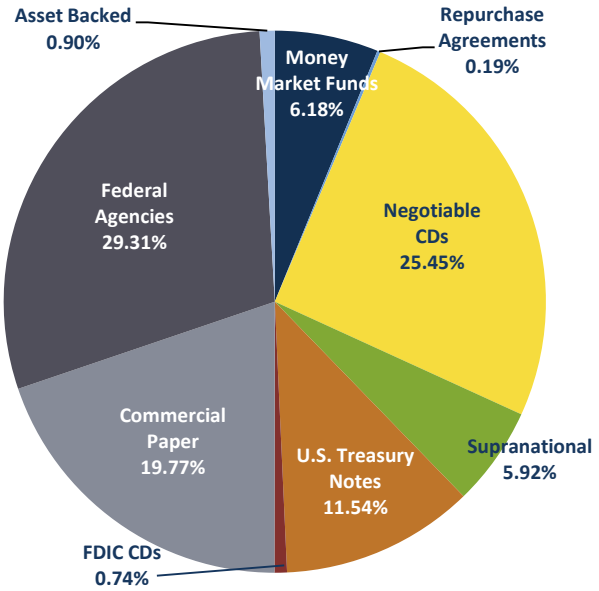
ASSET ALLOCATION

The Pool remains in compliance with the standards set forth in the IPS and with all statutory regulations. The largest asset class is Federal Agencies (29.31% of the portfolio), followed by Negotiable CDs at 25.45% and Commercial Paper at 19.77%. 11.54% of our total assets are invested in U.S. Treasury Notes, 6.18% is in Money Market Funds, 5.92% is allocated to Supranationals, 0.90% is in Asset-Backed Securities, and 0.74% is in FDIC CDs.

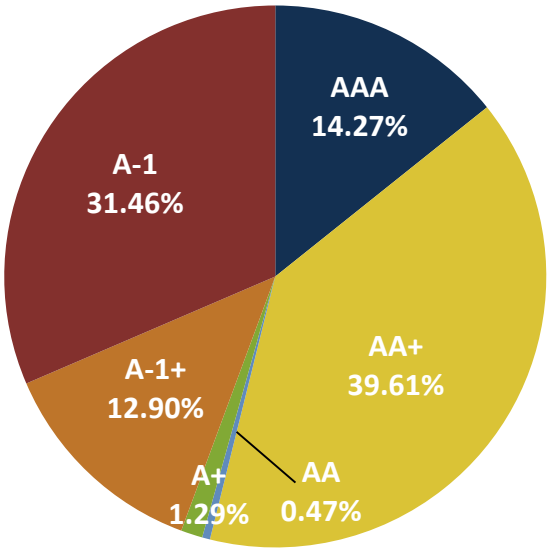
San Diego County Pooled Money Fund

As of September 30, 2016

Asset Allocation



Credit Quality



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