

# The Money Line

One very important aspect of running a good water utility system is financial management. There are many components to financial management: billing, collections, rate reviews, etc. Beginning with this issue of *The Kansas Lifeline*, Ranson Financial Consultants, LCC (“Ranson”), financial advisor to the Kansas Rural Water Finance Authority (“KRWFA”) is going to provide up-to-date information on investing, borrowing and the general interest rate market. A rate of return on invested funds and the interest rate charged for borrowed funds can make the difference in having a profitable system or not. In addition, Ranson will periodically introduce or reintroduce concepts in public finance.

Government T-Bills. It is important to municipal investors in the state of Kansas due to State Statutes. Generally speaking K.S.A. 12-1675 requires that banking institutions located in a

in returns for the One Year T-Bill since 1980. The current yield (as of September 20) or return on the One Year T-Bill is 3.73%. That is up from its low for the referenced time period of 1.01% in June

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community within the state of Kansas offer certificates of deposit at least equal to the T-Bill of like maturity or one can invest funds elsewhere. Therefore, as the rate of return on the T-Bill fluctuates so does a return on the investment of public funds.

2003. On the other hand, the high for the T-Bill was 16.72% in April 1981. The average return for this time period is 6.53%. However, the median interest rate for the same time period is 5.87%.

As one can determine, the current T-Bill rate of return

## Investing Money



John Haas, President  
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The U.S. Treasury Bill (“T-Bill” or “T-Bills”) is a short-term, highly liquid debt obligation of the federal government. T-Bills are purchased at a discount and returns the face amount at maturity. For example, if the face value amount of a T-Bill is \$10,000,

maturing on December 1, 2005, and is offered at a discount of 99.00%, then the T-Bill can be purchased now for \$9,900 and the purchaser will receive \$10,000 on December 1, 2005.

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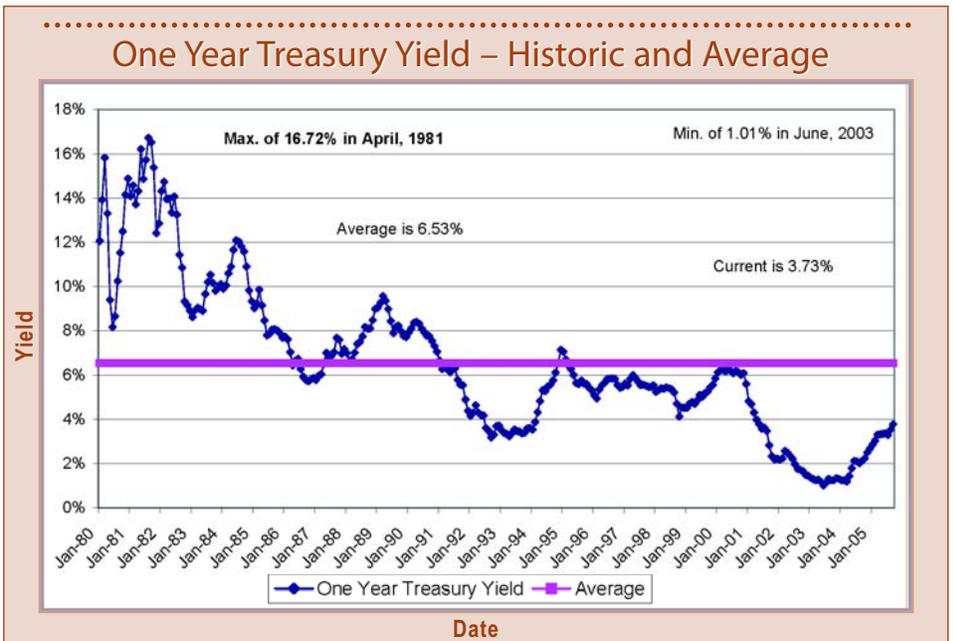


Chart A

Chart A: “One Year Treasury Yield – Historic and Average Rates”, delineates the fluctuation

(3.73%) is significantly less than its historic average (6.53% or 5.87%). The recent increase in the

return on T-Bills can be directly tied to the Federal Reserve's increase in the Discount Rate. The Discount Rate is the interest rate the Federal Reserve charges when banks borrow money from them.

disaster will affect the national economy at this time. The bottom line is to ladder your investments for different maturity dates dependent on your need for money.

### Borrowing Money

In the municipal finance business, we often use the "Bond Buyer 20 Bond Index" to keep track of interest rates. These are the interest rates that most closely define the cost of borrowing money by local units of government. The Bond Buyer 20 Bond Index is defined as "an Index of 20 actively traded dollar bonds quoted in terms of yield, as compiled and published by the Bond Buyer's weekly newspaper." The Bond Buyer has published the index since January 1953. Chart B, the "Bond Buyer Index of Municipal Bonds – 1980 to Current", demonstrates changes in the Index for the past 25 years.

As can be seen from Chart B, interest rates as defined by the Bond Buyer 20 Bond Index have had a

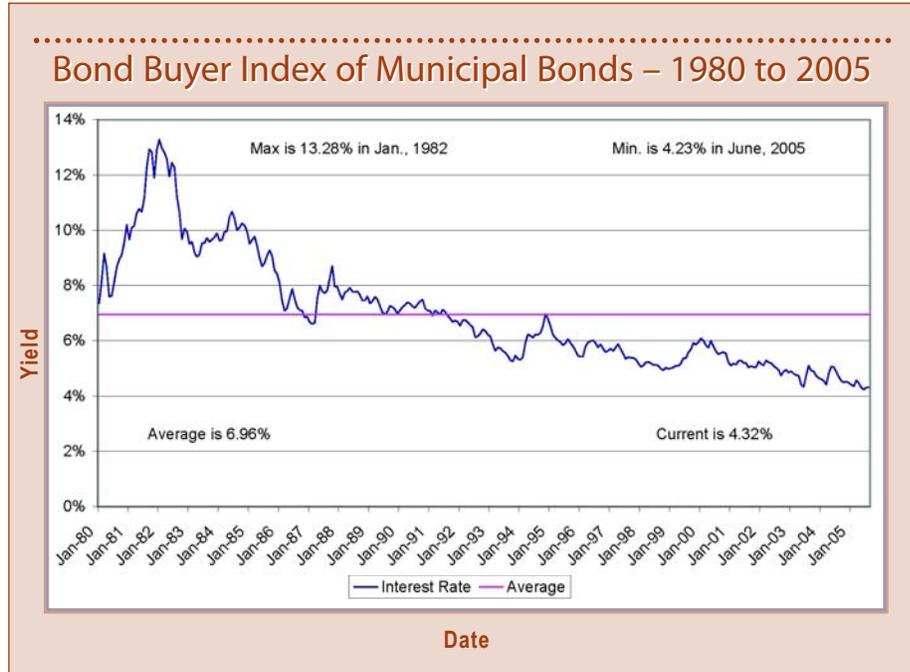


Chart B

The Federal Reserve will increase the Discount Rate if it has a concern about inflation and wishes to "tighten" money by discouraging borrowing. On the other hand, the Federal Reserve will reduce the Discount Rate if it is concerned about a soft economy and wish to "loosen" money and encourage borrowing. This will be explained more in future articles. In any case as one can tell from Chart A, the Federal Reserve has been in a "loosening" mode for most of the period from 1990 through 2003. Then in 2003 it began a series of rate increases. This was in response to perceived change in the prospect of future inflation.

The prospects for future rates will be dependent on the price of oil and other potential causes of inflation, such as hurricane Katrina. It is unknown how this natural

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wide range since 1985. In June 2005 the Index was at 4.23% (the low for the 25 year period). On the other hand, in January 1982 the Index was at an all time high of 13.28%. The average for the time period is 6.96%. The median interest rate (as previously mentioned) is 6.45%. Currently, the Index is 4.32%. Based upon this perspective, current borrowing rates are between 200 to 250 basis points less than the average. Therefore, it is a good time to borrow money if it is needed or required.

It is an interesting perspective that the Federal Reserve keeps increasing short-term interest rates while the market keeps long-term rates at historical lows. This is because the market anticipates the Federal Reserve is keeping inflation low with its recent increases in the Discount Rate. Low anticipated inflation leads to low long-term interest rates.

**The Kansas Public Water Supply Loan Fund (KPWSLF)**

The Bond Buyer 20 Bond Index is also important to borrowers in the state of Kansas

because it is the basis for rates charged by the KPWSLF.

The KPWSLF is a state revolving loan fund (SRF) program that provides financial

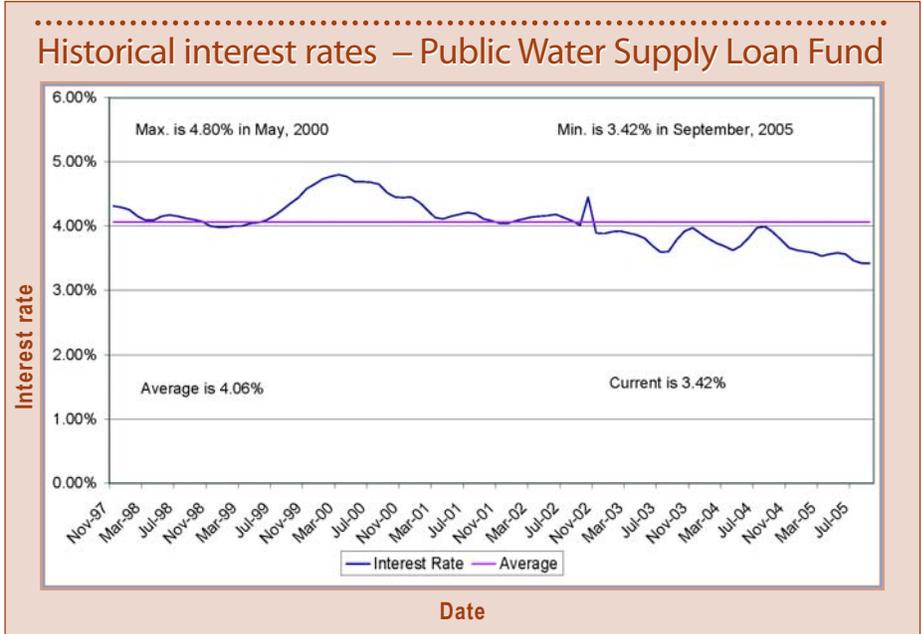


Chart C

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assistance in the form of loans to publicly owned public water systems in Kansas (cities and RWDs) at below-market interest rates for the construction of public water supply system infrastructure. The interest rate for the KPWSLF is set at 80% of the previous three months average of the Bond Buyer 20 General Obligation Bond Index. The State can offer a below-market interest rate because of grants the State receives from the National Drinking Water State Revolving Fund (DWSRF) program. The DWSRF program allows the U.S. Environmental Protection Agency (“EPA”) to award capitalization grants for the SRF. We will delve more into the mechanics of the loan program in future articles.

Chart C, “The Kansas Public Water Supply Loan Fund – Historic and Average Interest

Rates”, depicts the historic interest rates for the Loan program. The Program was initiated in 1997. Since 1997, the highest interest rate was 4.80% in May 2000. The

of borrowing and investing. These factors would include the demand and supply of money, foreign exchange markets, consumer and producer sentiments, government

.....  
**Even though the cost of borrowing has increased recently, it's still a good time to borrow funds. Interest rates are still below their historical averages, but will probably rise in the future.**

Bond Buyer Index and the T-Bill were at 6.00% and 6.17%, respectively. The lowest rate for the time period is also the current rate at 3.42%.

#### **Final Thoughts**

As an Associate Member of KRWA, Ranson Financial wishes to thank Elmer Ronnebaum and other staff members at the Kansas Rural Water Association (KRWA) for providing this forum to express opinions on the interest rate market. As financial advisor to the Kansas Rural Water Finance Authority, we intend to provide a regular column to *The Kansas Lifeline*. Readers will also have expanding opportunities to attend a variety of financial related training seminars, thanks to a partnership between the KRWA, the Rural Water Finance Authority and KDHE.

Even though the cost of borrowing has recently increased, it's still a good time to borrow funds. Interest rates are still below their historical averages, but will probably rise in the future. For investors we recommend laddering investments that meet the liquidity needs of your system.

The above observations were based on the historical rates or technical analysis. However, there are other fundamental factors that may influence and alter the costs

spending, global economic, financial and political dynamics and other variables of the macroeconomic environment, which are topics for future discussion.

Finally, if you have any questions regarding borrowing, investing or about the KPWSLF loan fund, please call me, John Haas, or M.E. Yeager at 316/264-3400. Or also contact KRWA and they will make sure help comes your way quickly. The opportunity to visit with boards and councils is one that we welcome. We can discuss funding options and help develop comprehensive capital improvement plans, adequacy of water rates, debt structuring or other financial-related issues.

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