California State Treasurer's Office

Investment Policy

Pooled Money Investment Account

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Introduction and Overview

The State Treasurer's Investment Division manages the Pooled Money Investment Account (PMIA) under statutory authority granted by Government Code sections 16430 and 16480 et. seq. All state money held by the State Treasurer in treasury trust accounts, and all money in the State Treasury, is appropriated for the purpose of investment and deposit.

Through the PMIA, the State Treasurer invests taxpayers' money to help manage the State's cash flow, as well as provide an investment option for local governments through the Local Agency Investment Fund (LAIF). The PMIA's primary investment objectives are safety, liquidity and yield.

The PMIA has three primary sources of funds: the State General Fund; special funds held by State agencies; and moneys deposited by cities, counties, and other local agencies into the LAIF.

The Pooled Money Investment Board (PMIB) governs the PMIA. The State Treasurer chairs the PMIB, which also includes the State Controller and the Director of Finance.

The State Treasurer's Investment Division shall present a written statement of investment policy to the PMIB at a public meeting annually, as well as promptly notify the PMIB of any material change in the statement of investment policy. This document serves as the statement of investment policy.

Investment Division Mission Statement

The Investment Division prudently invests the State's and local governments' idle cash through the Pooled Money Investment Account, consistent with the objectives of safety, liquidity, and yield.

Investment Division Vision Statement

To provide the highest and most consistent level of service, leadership and accountability through innovation, collaboration, and teamwork, while maintaining investor confidence and trust.

Portfolio Management Goals, Objectives, and Policies

The following goals, objectives, and policies shall direct the daily investment decisions in the management of the PMIA:

Goal 1. Portfolio Safety/Diversification

The PMIA will be managed to ensure the safety of the portfolio by investing in high credit quality securities and maintaining a mix of securities with various terms that in aggregate provides reasonable protection that no single investment, or class of investments, will have a disproportionate impact on the total portfolio.

<u>OBJECTIVE</u>: In addition to the safety provided by investing in high credit quality securities, the safety of the portfolio is enhanced by maintaining a diverse, prudent mix of investments, and includes:

1) Spreading investments over different investment types to minimize the impact that any one industry/investment class can have on the portfolio;

2) Spreading investments over multiple credits/issuers within an investment type to minimize the credit exposure of the portfolio to any single firm/institution; and

3) Spreading investments over various maturities to minimize the risk of portfolio depreciation due to a rise in interest rates.

<u>POLICY</u>: The portfolio shall contain a sufficient number and diversity of marketable securities so that a reasonable portion of the portfolio can be readily converted to cash without causing a material change in the value of the portfolio. Limitation and eligibility as to specific investments are to be determined by the PMIB in the case of Commercial Paper and the State Treasurer’s Investment Division in all other matters.

In the absence of direct statutory limitations, the “prudent person rule” shall govern all investment decisions. Changing market conditions that warrant consideration of significantly modifying investment strategies (e.g. altering credit quality, marketability, yield spreads, securities availability) shall be discussed with the Director of Investments. At the Director of Investments’ determination, the situation may be discussed with the State Treasurer or the State Treasurer’s designee.

Goal 2. Liquidity

The PMIA will be managed to ensure that scheduled and unscheduled cash needs can be met.

OBJECTIVE: The PMIA will maintain a "cash flow generated" portfolio balance sufficient to cover specifically the one-month cash disbursement forecast, as well as generally the six-month disbursement forecast.

POLICY: The first priority is to maintain specific calendar liquidity, as dictated by the most recent cash forecast provided by the Centralized Treasury & Securities Management Division. The second priority is to maintain adequate marketable securities positions to meet the potential risk of unscheduled cash needs arising.

Due to the diverse requirements of cash flow management, an average life of 120 days to 18 months will be maintained.

Goal 3. Rate of Return

The PMIA investments and deposits shall be made in such a way as to realize the maximum return consistent with safe and prudent treasury management.

OBJECTIVE: The rate of return will be maintained on a consistent level representative of current high credit quality fixed income market yields.

POLICY: Gains and losses from the sale of securities will not be incurred at levels that would noticeably alter the PMIA's quarterly apportionment rate of return. Significant sales gains will be offset for restructuring purposes to maintain consistent current return, as well as to maximize future portfolio performance. Significant sales losses shall be incurred only with the consent of the State Treasurer, or when sufficient gains from other sales minimize the overall change in the apportionment rate of return.

To protect the portfolio rate of return, long positions shall never exceed the amount intended to be purchased during a "when issued" (W.I.) period, and short positions shall never be taken.

Authorized Investments

The following table provides a summary of parameters for the PMIA investment portfolio with respect to a specific investment type's maximum maturity, concentrations within the portfolio or investment, and minimum credit ratings:

Investment Type	Maximum Maturity	Maximum % of Portfolio	Maximum Per Issuer	Minimum Credit Rating (4)
Agencies (Federal and Supranational)	5 years	None	None	AA category
Bankers Acceptances (Domestic and Foreign)	180 days	None	None	A-1/P-1/F1
Certificates of Deposits	5 years	None	None	A-1/P-1/F1
Collateralized Time Deposits	1 year	5%	(1)	Satisfactory
Commercial Paper	270 days	30%	10%	A-1/P-1/F1
Corporate Bonds/Notes	5 years	10%	None	A category
Foreign Government Bonds/Notes	5 years	1%	None	AA category
Money Market Mutual Funds	Open ended	10%	10%	AAA/Aaa
Negotiable Order of Withdrawal (NOW) Accounts	Open ended	5%	(3)	A-1/P-1/F1
Repurchases (RP) and Reverse Repurchases (RRP)	1 year	(2)	None	N/A
U.S. Treasury Securities	5 years	None	None	N/A

(1) Shall not exceed the net worth of the institution or an amount considered prudent, whichever is less.
(2) RRP is limited to 10% of the current portfolio.
(3) Shall not exceed the net worth of the institution.
(4) By one or more nationally recognized statistical rating organizations as specified in 'Credit Considerations Per Investment Type.'

Credit Considerations Per Investment Type

<u>Agencies (Federal and Supranational)</u> – Agencies shall have a minimum credit rating category of AA by at least two nationally recognized statistical rating organizations utilized by the State Treasurer's Investment Division.

<u>Banker's Acceptances (Domestic and Foreign)</u> – Institutions shall have a minimum credit rating of A-1, P-1, or F1 by at least one nationally recognized statistical rating organization utilized by the State Treasurer's Investment Division and pass an internal credit evaluation. This evaluation may include a review of criteria such as geographic location, market perception, management factors, and overall fiscal soundness.

<u>Certificates of Deposits</u> – Institutions shall have a minimum credit rating of A-1, P-1, or F1 by at least one nationally recognized statistical rating organization utilized by the State Treasurer's Investment Division and pass an internal credit evaluation. This evaluation may include a review of criteria such as geographic location, market perception, management factors, and overall fiscal soundness. The approved investments will be regularly posted to the STO website.

<u>Collateralized Time Deposits: Time Deposit Program and Small Business Lending Time Deposit Program</u> – Institutions must be headquartered in the State of California (except for institutions participating in the Small Business Lending Time Deposit Program, which only requires a California presence), have a Community Reinvestment Act (CRA) rating of Satisfactory or better, and pass an internal credit evaluation. This evaluation may include a review of criteria such as geographic location, market perception, loan diversity, management factors, and overall fiscal soundness. If a participating institution is downgraded below acceptable levels, an appropriate plan of action will be determined, which may include early termination of the time deposit. Collateral must comply with Government Code section 16500 et seq. (bank deposits) and section 16600 et. seq. (savings and loans association and credit union deposits).

<u>Commercial Paper</u> – Commercial paper shall have a minimum credit rating of A-1, P-1, or F1 by at least one nationally recognized statistical rating organization utilized by the State Treasurer's Investment Division, must be issued by a federally or state-chartered bank or a state-licensed branch of a foreign bank, corporation, trust, special purpose corporation, or limited liability company approved by the PMIB, and pass an internal credit evaluation. This evaluation may include a review of criteria such as geographic location, market perception, management factors, and overall fiscal soundness. Furthermore, these entities must be either (1) organized and operating within the United States and have total assets in excess of five hundred million dollars ($500,000,000) or (2) must be organized within the United States and have program wide credit enhancements, including, but not limited to, overcollateralization, letters of credit, or surety bonds. The approved investments will be regularly posted to the STO website.

<u>Corporate Bonds/Notes</u> – Corporate Bonds or Notes must be issued by corporations (including banks) that are organized and operating within the United States, have a minimum credit rating category of A by at least two nationally recognized statistical rating organizations utilized by the State Treasurer's Investment Division, and pass an internal credit evaluation. This evaluation may include a review of criteria such as geographic location, market perception, management factors, and overall fiscal soundness. The approved investments will be regularly posted to the STO website.

<u>Foreign Government Bonds/Notes</u> – Foreign Government Bonds or Notes must be direct obligations of the government of a foreign country that the International Monetary Fund lists as an advanced economy and for which the full faith and credit of that country has been pledged for the payment of principal and interest. In addition, they shall have a minimum credit rating category of AA by at least two nationally recognized statistical rating organizations utilized by the State Treasurer's Investment Division.

<u>Money Market Mutual Funds</u> – Money market mutual funds must invest in U.S. Treasury Securities, Agencies, Repurchases, or Reverse Repurchases as described by this Policy. The financial institutions issuing the shares must have at least five years of investment experience in managing these funds and have at least $10 billion in assets under management. In addition, money market mutual funds must have a credit rating of AAA or Aaa by at least two nationally recognized statistical rating organizations utilized by the State Treasurer's Investment Division.

<u>Negotiable Order of Withdrawal (NOW) Accounts</u> – Institutions shall have a minimum credit rating of A-1, P-1, or F1 by at least one nationally recognized statistical rating organization utilized by the State Treasurer's Investment Division and pass an internal credit evaluation. This evaluation may include a review of criteria such as geographic location, market perception, management factors, and overall fiscal soundness. All other conditions, regulations, or requirements associated with demand and time deposits will also apply.

<u>Repurchases (RP) and Reverse Repurchases (RRP)</u> – RP and RRP Agreements are only done with primary dealers of the Federal Reserve Bank of New York. A signed Master Repurchase Agreement must be on file before engaging in a transaction.

<u>U.S. Treasury Securities</u> – U.S. Treasury Securities are backed by the full faith and credit of the Federal Government.

Reporting

In accordance with Government Code section 16480.7, the State Treasurer is required to prepare and submit a monthly report of investment activity. The report will detail the portfolio composition, investment transactions made during the month, deposits in banks and savings and loan associations, and the designation by the PMIB.

In accordance with Government Code section 16481.2(b), the State Treasurer is required to prepare and submit a quarterly report of investment holdings and market valuation to the PMIB. This report will detail the investment type, issuer, maturity date, par value, market value, source of the valuation, weighted average maturity of the investments and a statement of compliance with the investment policy.

These reports are available on the STO website.

Authorized Broker-Dealer

The State Treasurer shall transact business with a broker-dealer that meets the qualifications criteria established by the State Treasurer, which includes, but is not limited to, the review of audited financial statements and Financial Industry Regulatory Authority (FINRA) certifications. The Investment Division will annually review each broker-dealer to ensure ongoing qualification. The Investment Division is permitted to deal directly with the issuers of any securities that are authorized for purchase and meet all the qualifications of this policy.

Glossary

Agencies (Federal) – Securities issued or guaranteed by U.S. federal government agencies and by government-sponsored enterprises (GSEs)—corporations created by Congress to foster a public purpose, such as affordable housing. Bonds issued or guaranteed by federal agencies are backed by the full faith and credit of the U.S. government.

Agencies (Supranational) – U.S. dollar denominated debt obligations issued by entities formed by two or more central governments to promote economic opportunity for the member countries.

Banker's Acceptance (BA) –Short-term credit investments created by a non-financial firm and guaranteed by a bank to make payment. BAs are traded at discounts from face value in the secondary market.

Certificates Of Deposit (CD) – Issued by commercial banks and thrift institutions against funds deposited for specified periods of seven days or longer and earn specific rates of interest. Major banks and thrifts also issue variable rate CDs with maturities of up to five years. Variable rates are adjusted every 30, 90, or 180 days, and usually include a fixed spread to the benchmark rate for major bank CDs, as compiled and published by the Federal Reserve Bank of New York. Yankee CDs, also authorized by statute, are U.S. dollar-denominated CDs issued by foreign banks domiciled in the United States.

Commercial Paper (CP) – Short-term discounted obligations with maturities ranging from one to 270 days issued by banks, corporations and limited liability companies. CP can be issued directly or through a broker.

Corporate Bonds/Notes – Debt securities issued by a company to raise capital for their operations or for a specific project.

Foreign Government Bonds/Notes – U.S. dollar denominated bonds issued in a domestic market by a foreign government as a means of raising capital and to pay for services or other obligations.

Money Market Mutual Funds – A mutual fund that invests in highly liquid, near-term instruments and are considered low-risk investments that can be suitable for short-term investment goals.

Negotiable Order of Withdrawal (NOW Account) – An account that pays interest on deposits and are offered by commercial banks, mutual savings banks, and savings and loan associations.

Repurchase Agreements (RP or Repo) – Consists of two simultaneous transactions. One is the purchase of securities by an investor from a bank or dealer. The other is the commitment by the bank or dealer to repurchase the securities at the same price at some mutually agreed upon future date. Most transactions are for maturities from one to three days.

Reverse Repurchases (RRP or Reverse Repo) – Matched sales-purchase agreements that are the opposite of a Repurchase Agreement. In this instance, the investor is the owner of the collateral, and the bank or dealer is the lender of money.

Time Deposits – Interest-bearing deposits with specific maturities negotiated with California banks, savings and loans and credit unions. These deposits are secured by collateral pledged by the financial institution and in compliance with the Government Code. Required collateralization levels are monitored daily. In addition, financial institutions are evaluated for credit quality.

U.S. Treasury Bills – A short-term (maturities up to a year) discounted government security (secured by the full-faith and credit of the U.S. government) sold through competitive bidding at weekly and monthly auctions. One-, three-, four- and six-month bills are auctioned weekly, and one-year bills are auctioned monthly.

U.S. Treasury Notes – Debt obligations of the U.S. government, issued at various schedules (monthly in most cases) and are intermediate securities with maturities from one to 10 years.

U.S. Treasury Strips – Originally issued by the U.S. Treasury in complete form as principal and interest obligations. Strips, or Zero Coupons as they are often referred, are the result of separating the interest obligation from the principal and trading the principal of the bond and the individual coupon obligations as separate securities.