



**STANDARD & POOR'S
RATINGS SERVICES**

McGRAW HILL FINANCIAL

Session One:

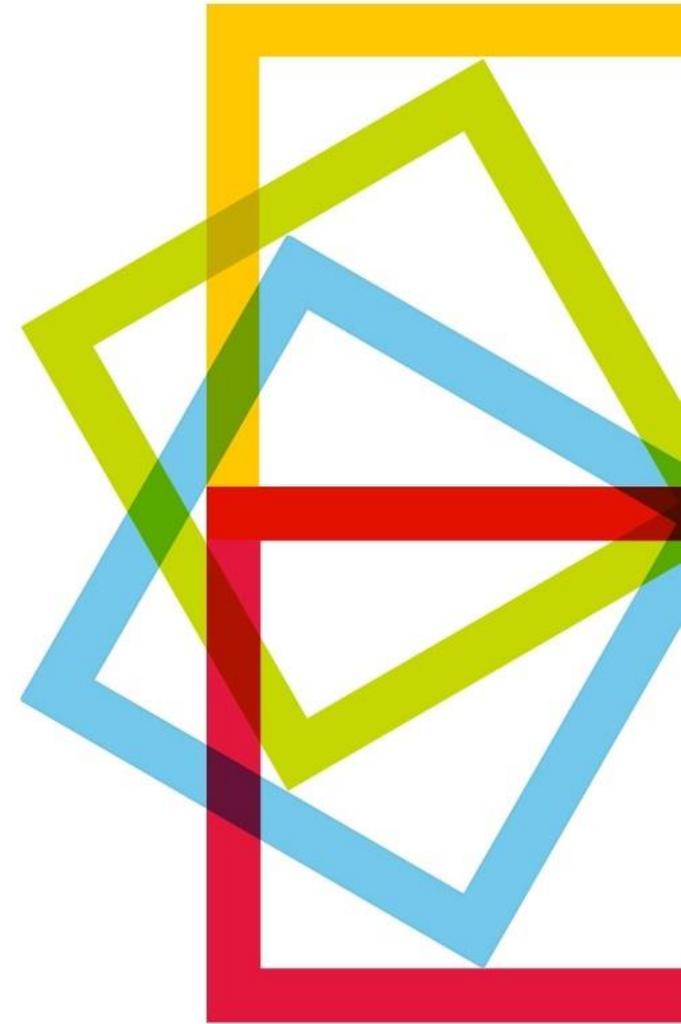
Keeping up with Federal Regulations Impacting Public Investing

Standard & Poor's Fund Ratings

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Agenda

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Trends & Strategies in MMF Investments

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Overview

Overview of Standard & Poor's Fund Ratings

- Standard & Poor's has been rating fixed income funds since December 1983
- The Fund Ratings Group was officially formed in 1989
- Global team is comprised of 20+ fund analysts in 5 countries averaging 10+ years of fixed-income and fund ratings experience
- Provides ratings and evaluations for over 800 “funds” globally, from over 200 fund sponsors:
 - 400+ Principal Stability Fund Ratings – money market funds
 - 250+ Fund Credit and Volatility rated funds – fixed income funds
 - Includes 90+ Local Government Investment Pools
 - Includes approximately 60+ Liquidity Assessments

Three Main Components of Fund Ratings

1. **Principal Stability Fund Ratings (PSFRs)** – Globally 400+ funds with AUM of US\$3 trillion
 - Also known as Money Market Fund Ratings or Stable NAV Fund Ratings
 - Represented by ‘m’ suffix after the traditional rating symbology (AAAm)
 - Address the ability of a fund to maintain principal stability and to limit exposure to principal losses due to credit risk
2. **Fund Credit Quality & Fund Volatility Ratings** – Globally 250+ funds
 - Fund Credit Quality Ratings (FCQRs)
 - Addresses level of protection against losses from credit defaults
 - Represented by ‘f’ suffix after the traditional rating symbology (AAAf)
 - Fund Volatility Ratings (FVRs)
 - Represented by ‘S’ scale (S1, S2, etc.); added in 1994 to complement FCQRs
 - Addresses a fund’s sensitivity to changing market conditions
3. **Liquidity Assessments** - Globally 100 funds
 - Began in 2000 and is also referred to as “self-liquidity”
 - An evaluation of the adequacy and liquidity of an issuer’s assets relative to its potential short-term debt obligations.
 - Generally limited to issuers rated at least ‘A’ with “excess” highly liquid and available assets sufficient to meet all debt obligations on full & timely basis.

Types of Government Investment Pool (Fund) Ratings

Principal Stability Fund Ratings

- Assigned to funds whose investment policies are consistent with providing a stable or accumulating NAV (*i.e.* 2a-7 \$1.00 NAV funds)
 - ⇒ max WAM to Reset 60 days (AAAm)
 - ⇒ max WAM to Final 90-120 days (AAAm)
 - ⇒ max final maturity 397 days (fixed rate)
 - ⇒ high credit quality (Tier 1 only)
 - ⇒ highly diversified (issuers, counterparties, etc.)
- Also known as Money Market Fund Ratings or Stable NAV Fund Ratings
- Represented by 'm' suffix after the traditional rating symbology (AAAm)
- Address the ability of a fund to maintain principal stability and to limit exposure to principal losses due to credit risk

Fund Credit Quality & Volatility Ratings

- Assigned to funds with investment policies beyond what is permitted by rule 2a-7 (*i.e.* Variable NAV Funds)
 - ⇒ max WAM to Reset > 90 days
 - ⇒ max WAM to Final > 120 days
 - ⇒ max final maturity > 397 days (fixed rate)
- Fund Credit Quality Ratings
 - ⇒ Addresses level of protection a fund's portfolio holdings provide against losses from credit defaults
 - ⇒ Represented by 'f' suffix after the traditional rating symbology (AAAf)
- Fund Volatility Ratings
 - ⇒ Represented by 'S' scale (S1, S2, etc.)
 - ⇒ Addresses a fund's sensitivity to changing market conditions

Principal Stability Fund Ratings (PSFRs)

- Also known as Money Market Fund Ratings
- Represented by 'm' suffix after the traditional rating symbology (AAAm)
- Address the ability of a fund to maintain principal stability and to limit exposure to principal losses due to credit risk
-

Principal Stability Fund Ratings (PSFRs)

- Assigned to funds whose investment policies are consistent with providing a stable or accumulating NAV (i.e. 2a-7 \$1.00 NAV funds)
 - max WAM to Reset 60 days (AAAm)
 - max WAM to Final 90-120 days (AAAm)
 - max final maturity 397 days (fixed rate)
 - high credit quality (Tier 1 only)
 - highly diversified (issuers, counterparties, etc.)
- Each rating category corresponds with a NAV range.
 - For example, a fund can maintain a 'AAAm' rating so long as its marked-to-market per-share NAV does not deviate more than +/- 0.25%.
 - AAAm +/- 0.25%
 - AAm +/- 0.30%
 - Am +/- 0.35%
 - BBBm +/- 0.40%
 - BBm +/- 0.50%
 - Dm > 0.50%
 - For all funds (regardless of rating), daily portfolio pricing, marked-to-market NAV calculations, and stress testing are monitored when NAV goes beyond +/- 0.15% deviation.

Principal Stability Fund Ratings Definitions

AAAm	A fund rated 'AAAm' demonstrates extremely strong capacity to maintain principal stability and to limit exposure to principal losses due to credit risk. 'AAAm' is the highest principal stability fund rating assigned by Standard & Poor's.
AAm	A fund rated 'AAm' demonstrates very strong capacity to maintain principal stability and to limit exposure to principal losses due to credit risk. It differs from the highest-rated funds only to a small degree.
Am	A fund rated 'Am' demonstrates strong capacity to maintain principal stability and to limit exposure to principal losses due to credit risk, but is somewhat more susceptible to the adverse effects of changes in circumstances and economic conditions than funds in higher-rated categories.
BBBm	A fund rated 'BBBm' demonstrates adequate capacity to maintain principal stability and to limit exposure to principal losses due to credit risk. However, adverse economic conditions or changing circumstances are more likely to lead to a reduced capacity to maintain principal stability.
BBm	A fund rated 'BBm' demonstrates speculative characteristics and uncertain capacity to maintain principal stability. It is vulnerable to principal losses due to credit risk. While such funds will likely have some quality and protective characteristics, these may be outweighed by large uncertainties or major exposures to adverse conditions.
Dm	A fund rated 'Dm' has failed to maintain principal stability resulting in a realized or unrealized loss of principal.

Plus (+) or minus (-)

The ratings from 'AAm' to 'BBm' may be modified by the addition of a plus (+) or minus (-) sign to show relative standing within the rating categories.

Differences In Criteria For Rated & Unrated PSFRs

	Non Rated (2a-7 Like)	AAAm Rated	AAm Rated	Am Rated
Maturity				
Max Fund WAM (R)	60 days	60 days	70 days	80 days
Max Fund WAM (F)	120 days	90* days	100* days	110* days
Max maturity per security (Floating - Government)	None	2 years	3 years	4 years
Max maturity per security (Fixed & Floating - Corp)	397 days	397 days	397 days	397 days
Credit Quality				
Minimum A-1+ allocation	N/A	50%	20%	0%
Maximum A-1 allocation	N/A	50%	80%	100%
Maximum A-2 allocation	3%	0%	0%	0%
Pricing				
Frequency	Discretionary	Weekly	Weekly	Weekly
Diversification				
Max per Security/Industry	5%/25%	5%/25%	5%/25%	5%/25%
Max per Repo Counterparty	Unrestricted	Restricted	Restricted	Restricted
Minimum Liquidity				
Overnight/7 days	10%/30%	N/A	N/A	N/A

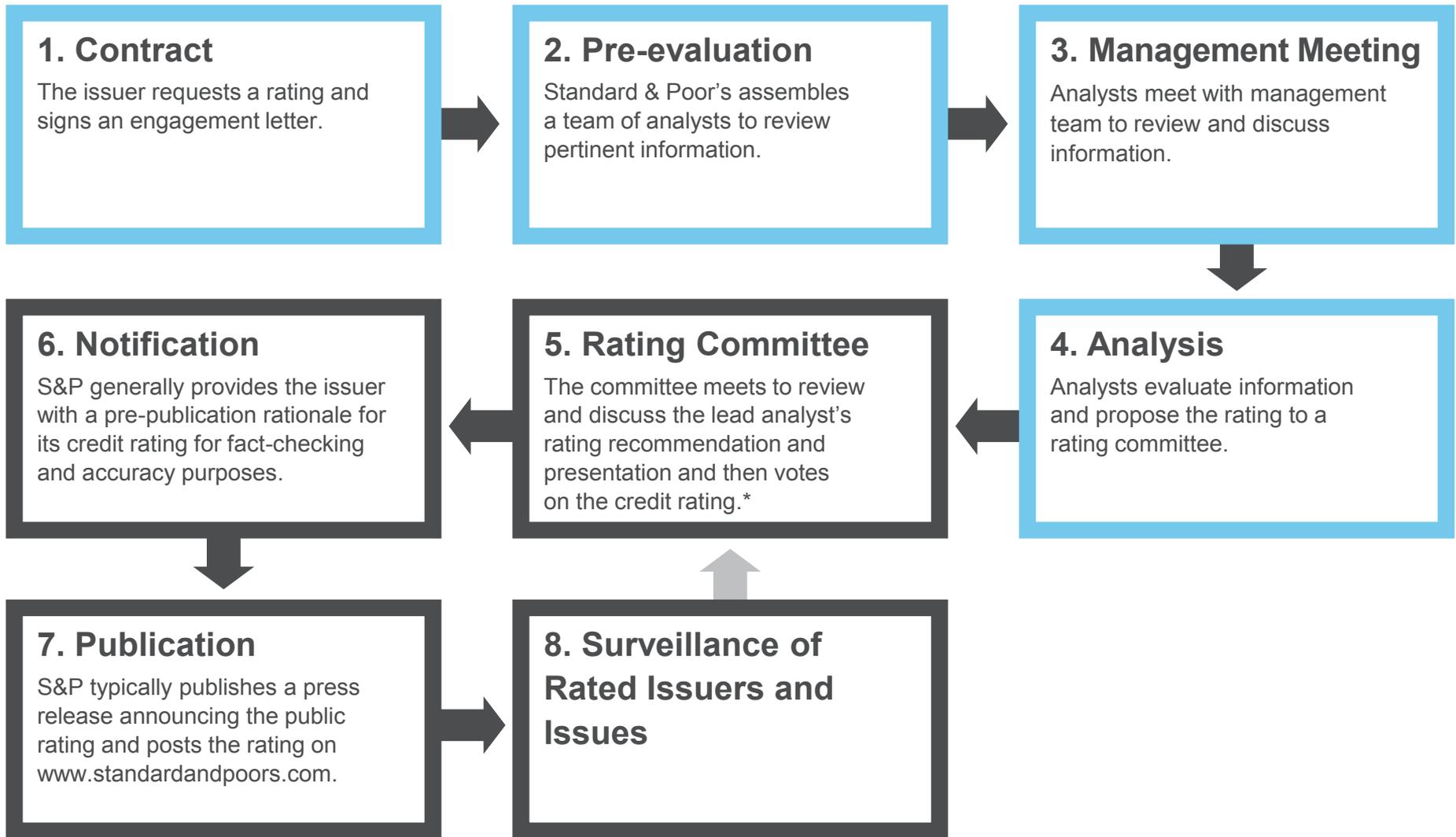
* WAM(F) criteria for all rating categories may be adjusted upward by 30 days (e.g. 'AAAm' 120 days) if a fund invests only in national government (sovereign) and/or government-sponsored entity (GSE) floating-rate notes. In addition, if a fund invests in a combination of government and nongovernment floating-rate instruments, a sliding scale between 90 and 120 days will be applied based on percentage exposures to each type of floater.

Process: Key Criteria Elements

Why Do Managers Request an S&P Fund Rating?

- **Asset Growth / Retention**
- **Third Party Credibility**
- **Board Oversight**
- **Diversified Product Mix**
- **Regulatory/Compliance**
 - N.A.I.C. Reduced Capital Reserve Requirements - Investments by insurance companies in AAAM rated funds have 0% capital reserve requirements. Capital reserve requirements are reduced to 1% when investing in AAM or Am rated money market funds or AAAf rated government bond funds.
 - State & Local Governments - GFOA recommends AAAM rated funds as investments for local & state governments.
 - Bond Proceeds - AAAM rated funds are Eligible Investments for bond proceeds of Standard & Poor's rated debt issues

The Rating Process



*S&P may allow for an appeal only if the issuer can provide new and significant information to support a potentially difficult rating conclusion.

Key Criteria Elements - Principal Stability Fund Rating (MMF)

Credit Quality

- Minimum 50% exposure to securities A-1+ and A-1 securities \leq 5 business days
- Maximum 50% exposure to securities A-1 $>$ 5 business days.

WAM and WAM (Final)

- 60 days and 90 – 120 days*

Cure Periods Apply For Breaches of Quantitative Metrics including:

- NAV / Diversification / 10% illiquid basket / Overall credit quality or an issuer downgrade below A-1

Monitoring Frequency

- Weekly monitoring of portfolio holdings and summary statistics and annual onsite management review meeting.

Annual On-site Management Review Meeting

- The fund rating is based on a fund's independent ability to maintain principal stability and does not include a fund sponsor's willingness and/or ability to support the fund's NAV.

Surveillance (Monitoring) of Fund Ratings

- Dedicated Staff of Surveillance Analysts & Proprietary System (MFDB)
- Portfolio Holdings, Cash Flows & Risk Parameters are reviewed:
 - ☑ Weekly for PSFRs
 - ☑ Monthly for FCQR & FVRs
- Portfolio Level & Security Level Analysis
 - ✓ portfolio maturity
 - ✓ credit quality
 - ✓ illiquid and market sensitive securities
 - ✓ sector allocations
 - ✓ variable / floating rate instruments
 - ✓ net asset value (pricing) fluctuations
 - ✓ Comparison of CDS vs. current ratings
 - ✓ Highest yielding fund analysis
- Internal Monthly Surveillance Meetings to Review Material Events
- Frequent Communication with Fund Management
- Annual On-Site Management Review Meeting

Regulatory Developments

SEC's MMF Reform Proposals – June 5, 2013

SEC is proposing two alternatives for consideration:

1. Alternative One: Floating Net Asset Value
2. Alternative Two: Liquidity Fees and Redemption Gates

Comment Period Closed September 17, 2013

As of October 3, 2013, over 1,200 comments received by the SEC*

* Source: <http://www.sec.gov/comments/s7-03-13/s70313.shtml>

Impact On S&P PSFRs

- Depends on the details of the final proposals and whether they impair an fund's ability to maintain a stable net asset value.

- Ψ Devil is in the details



- Article “Assessing The Impact That Recent U.S. Money Market Fund Reform Proposals Could Have On Principal Stability Fund Ratings” (June 18, 2013)

Impact Of Potential Changes On Fund Ratings

Floating The NAV

- We view a floating NAV as a neutral rating factor
- We expect to continue to apply our methodology as is
- We believe if required to float, fund managers will still likely aim to minimize share price fluctuations. So, we could continue to apply our 0.25% deviation for the 'AAAm' rating.

\$1.00 per share = \$0.9975 to \$1.0025

\$10.00 per share = \$9.975 to \$10.025

\$100.00 per share = \$99.75 to \$100.25

Example: DWS Variable NAV Money Fund, which we rated 'AAAm' in January 2012.

- This fund is a floating-NAV fund pegged at \$10.00 per share
- Its objectives specify that it follows all of the provisions of Rule 2a-7.
- We monitor whether the fund's NAV per share remains within the +/- 0.25% deviation range for 'AAAm' rated funds.

Liquidity Fees And Redemption Gates

LIQUIDITY FEE

- Important Questions:
 - *How is the liquidity fee applied?*
 - *Does the liquidity fee affect the fund's marked-to-market NAV?*
- This proposal could be a positive rating factor if the fee is administered after a shareholder redeems. This would benefit the remaining shareholders and would likely increase the NAV of the fund.

REDEMPTION GATES

- Under the current definitions and methodology, redemption gates could be a negative rating factor.
- The impact could be negative because the gate may be imposed for a maximum of 30 days, which is beyond the five business days outlined in the current PSFR definitions. If adopted, we would evaluate whether a change in our methodology is warranted.

Additional Proposals

- Stronger Diversification of Holdings
- Improved Reporting
- Enhanced Disclosure
- Stress Testing

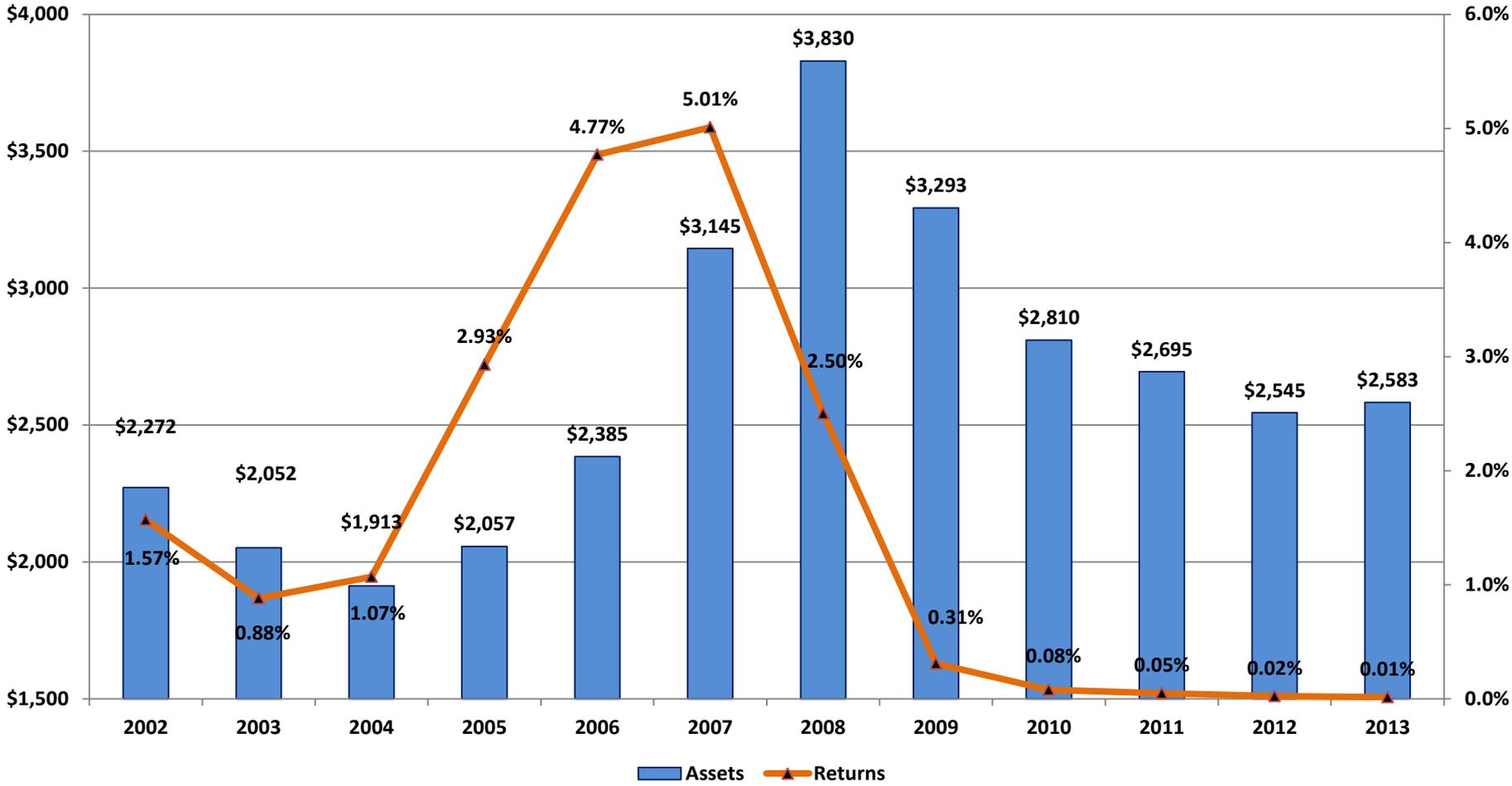
These proposals are also viewed as positive rating factors because they aim to increase transparency and mitigate risk in money funds.

Trends & Strategies in MMF Investments

Other Market Factors

- Regulatory Uncertainties
- Low Interest Rate Environment
- Consolidation
- Alternative Products in Light of Low Yields

Money Market Fund Assets (\$B) & Annual Returns (%)



Source: Crane Data, ICI.

A Question of Size

10 Largest Money Market Funds*

Rank	Money Market Fund Name	Type#	Assets (\$MM)	S&P PSFR
1	Vanguard Prime Money Market Fund	PrmInst	131,634	
2	Fidelity Cash Reserves	PrmRet	118,515	
3	JPMorgan Prime Money Market Fund	PrmInst	114,297	AAAm
4	Western Asset Institutional Liquid Reserves	PrmInst	78,047	
5	Fidelity Institutional Money Market: Money Market Portfolio	PrmInst	69,707	
6	BlackRock Liquidity TempFund	PrmInst	56,620	AAAm
7	JP Morgan US Government Money Market Fund	Gvtinst	56,050	AAAm
8	BlackRock Cash Institutional Money Market Fund	PrmInst	44,641	
9	Federated Prime Obligations Fund	PrmInst	42,682	AAAm
10	Wells Fargo Advantage Heritage	PrmInst	41,828	AAAm

*As of December 2013

#Type: Prminst = Prime Institutional; PrmRet = Prime Retail; Gvtinst = Government Institutional

Source: Crane Data LLC

Extended Family

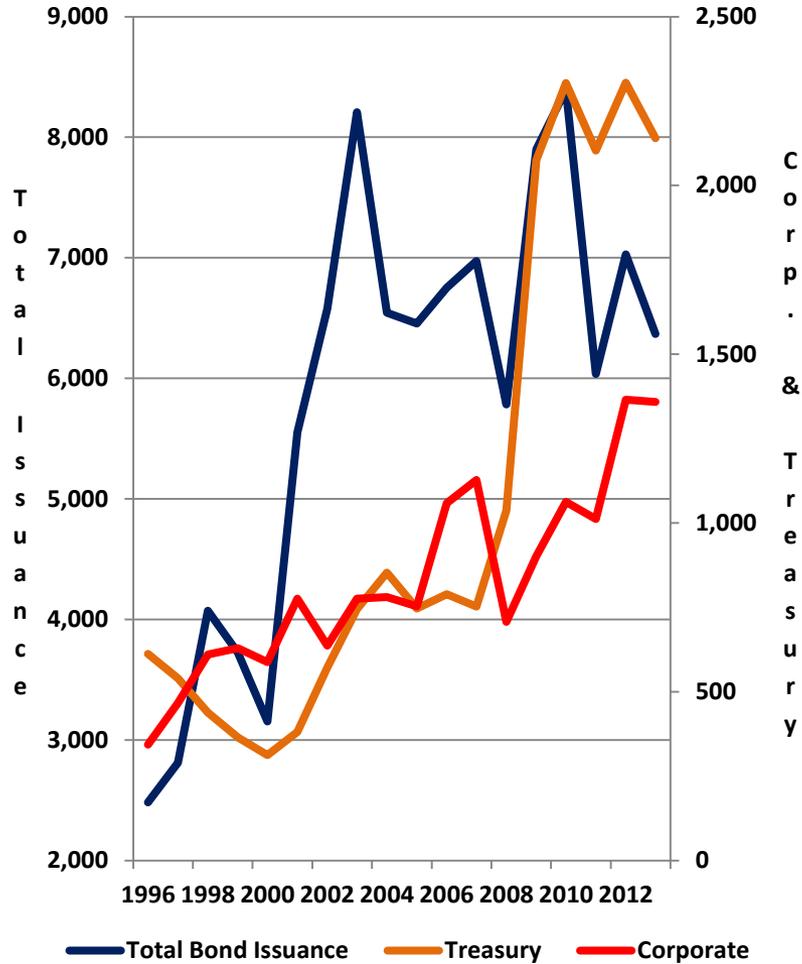
Top 15 Largest MMF Houses*

<u>Rank</u>	<u>House</u>	<u>AUM (\$MM)</u>
1	Fidelity	429,950
2	JPMorgan	249,994
3	Federated	221,037
4	BlackRock	204,971
5	Vanguard	175,115
6	Dreyfus	166,569
7	Schwab	162,551
8	Goldman Sachs	131,199
9	Wells Fargo	119,855
10	Morgan Stanley	94,511
11	SSgA	84,805
12	Northern	73,365
13	Invesco	61,831
14	BofA	48,732
15	UBS	45,077

*As of December 2013
Source: Crane Data LLC

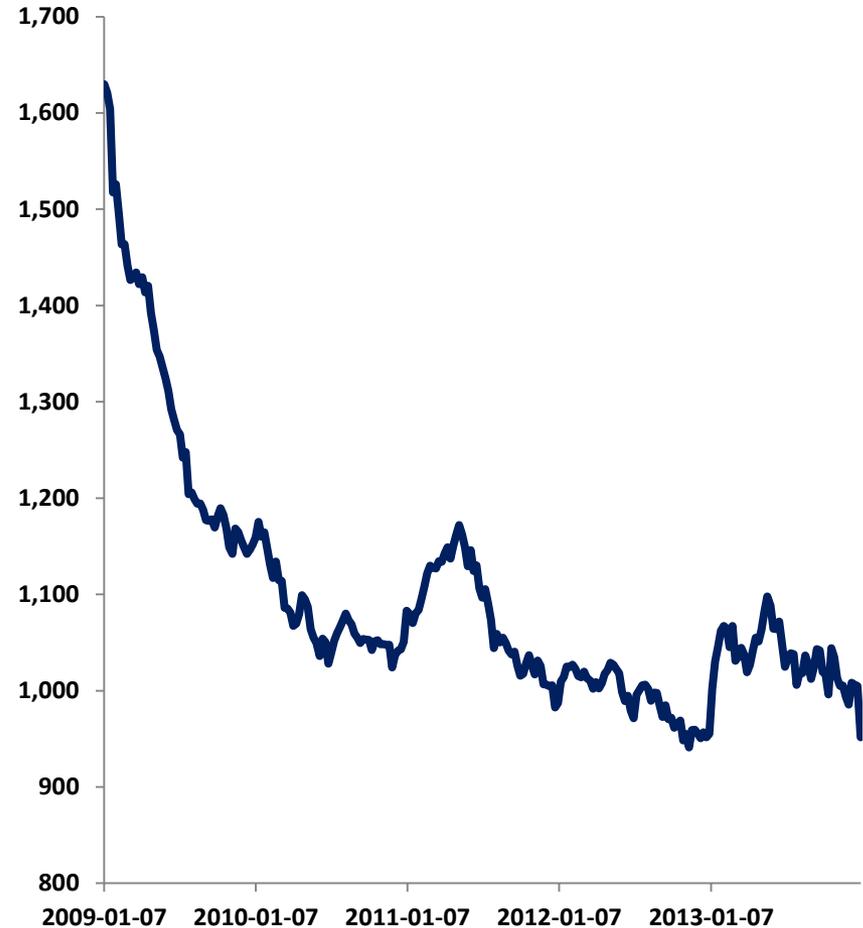
Investment Trends: Issuance

US Bond Issuance (\$B)



Source: SIFMA

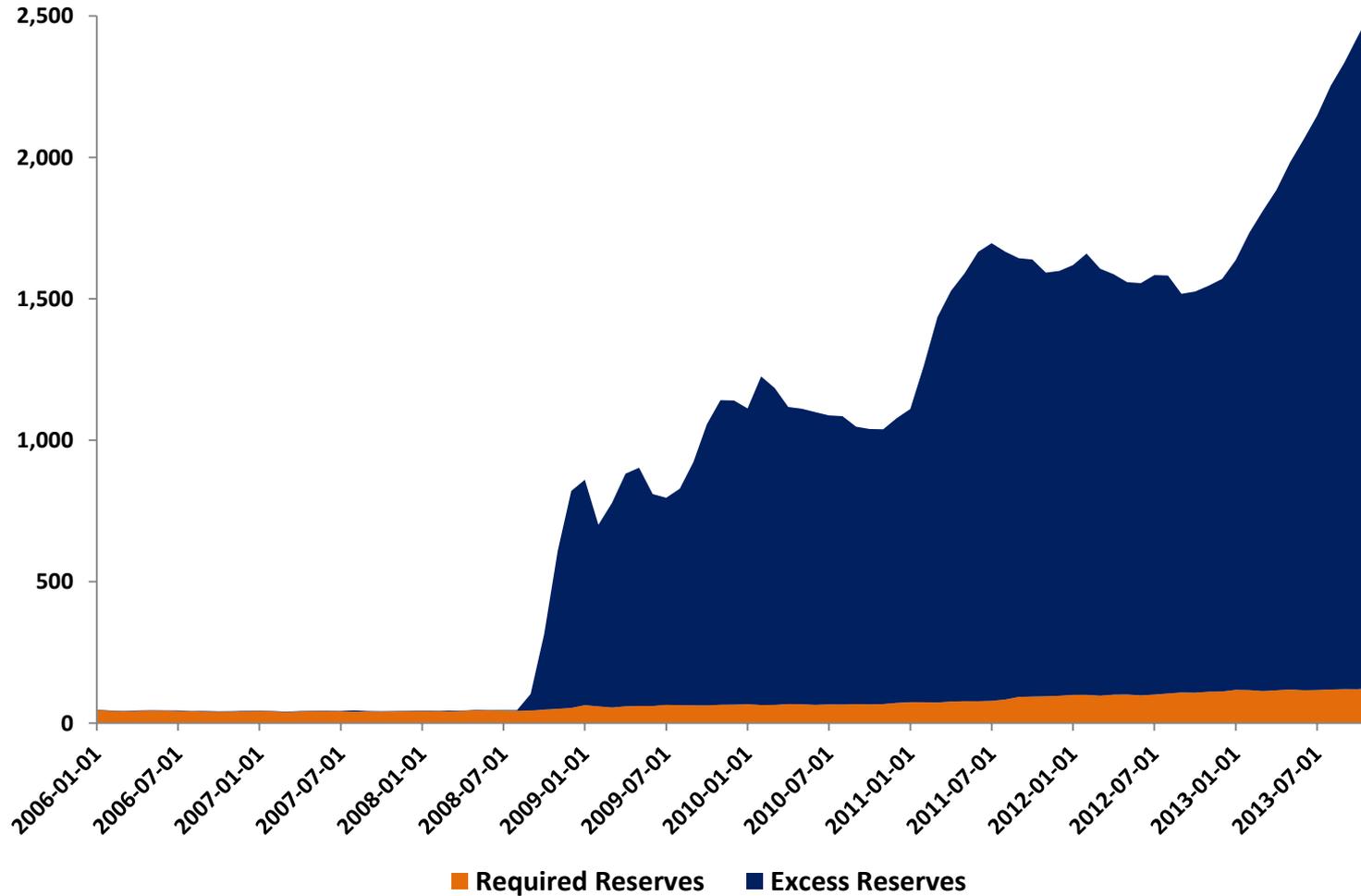
CP Outstanding



Source: Federal Reserve

Investment Trends: Issuance

Reserves of Depository Institutions



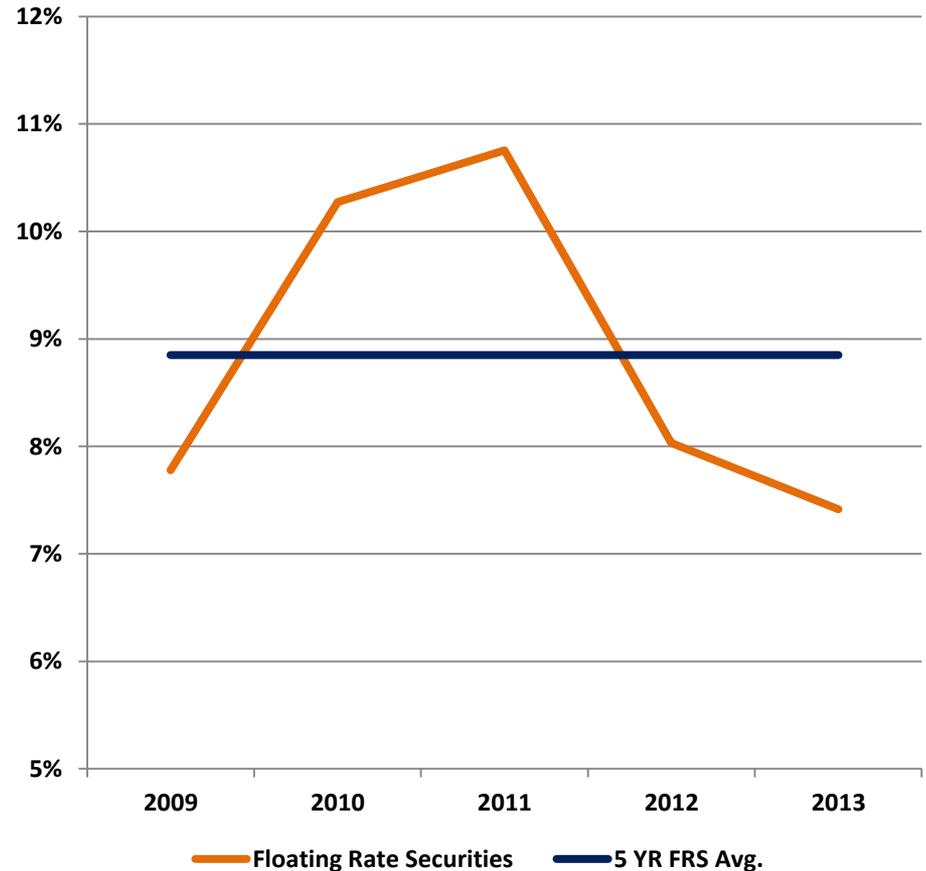
Source: Federal Reserve

Investment Trends: Treasury FRNs

How Do You Look At It?

- Credit
- Supply
 - T-bill Substitute
 - Treasury Cannibalization
- **Floater**
- S&P: 13-week Auction High Rate is consistent with our PSFR criteria.

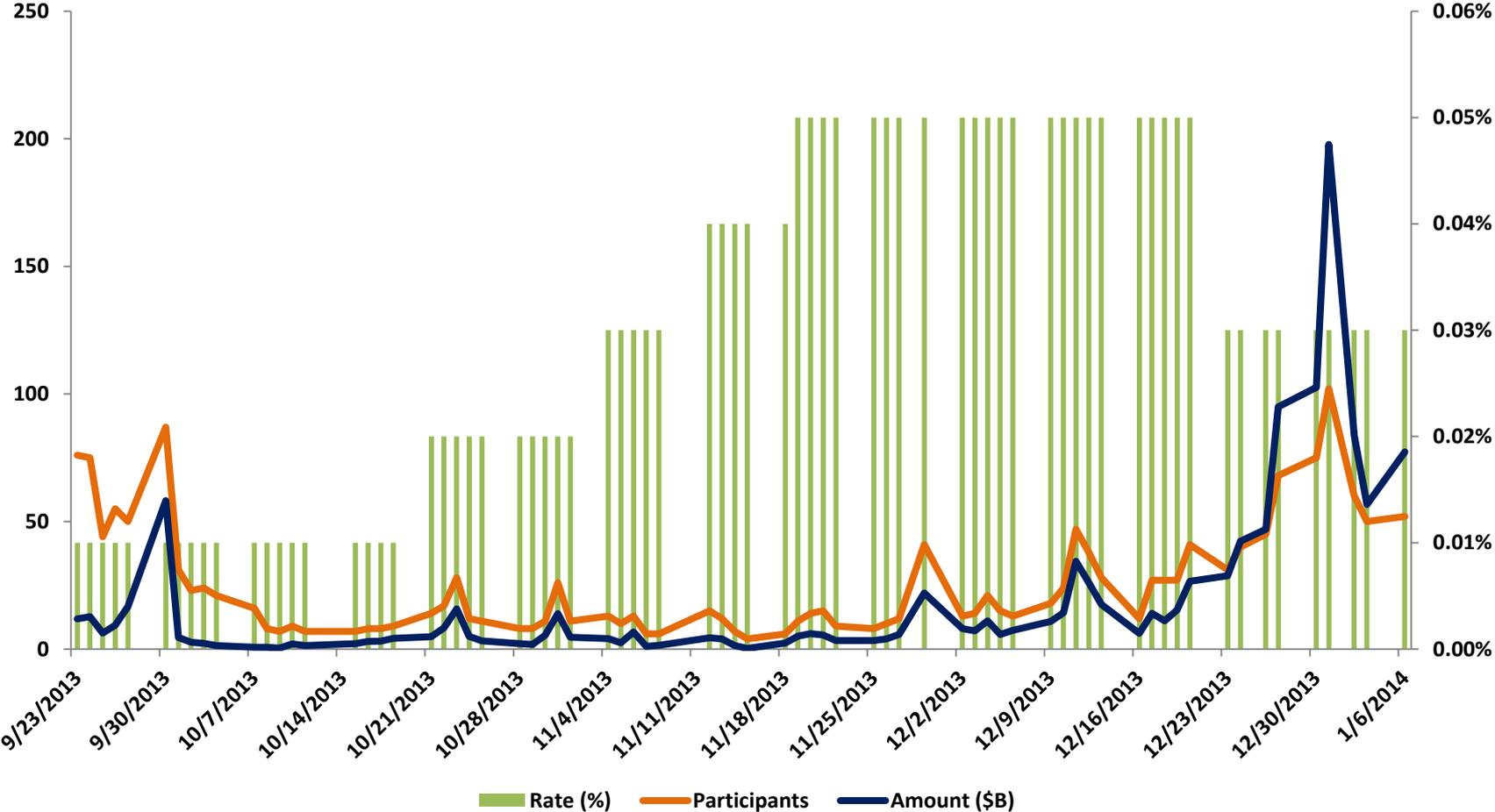
S&P PSFR Universe: FRN Concentration



Source: Standard & Poor's

Investment Trends: Fed Reserve & A Matter of Convenience

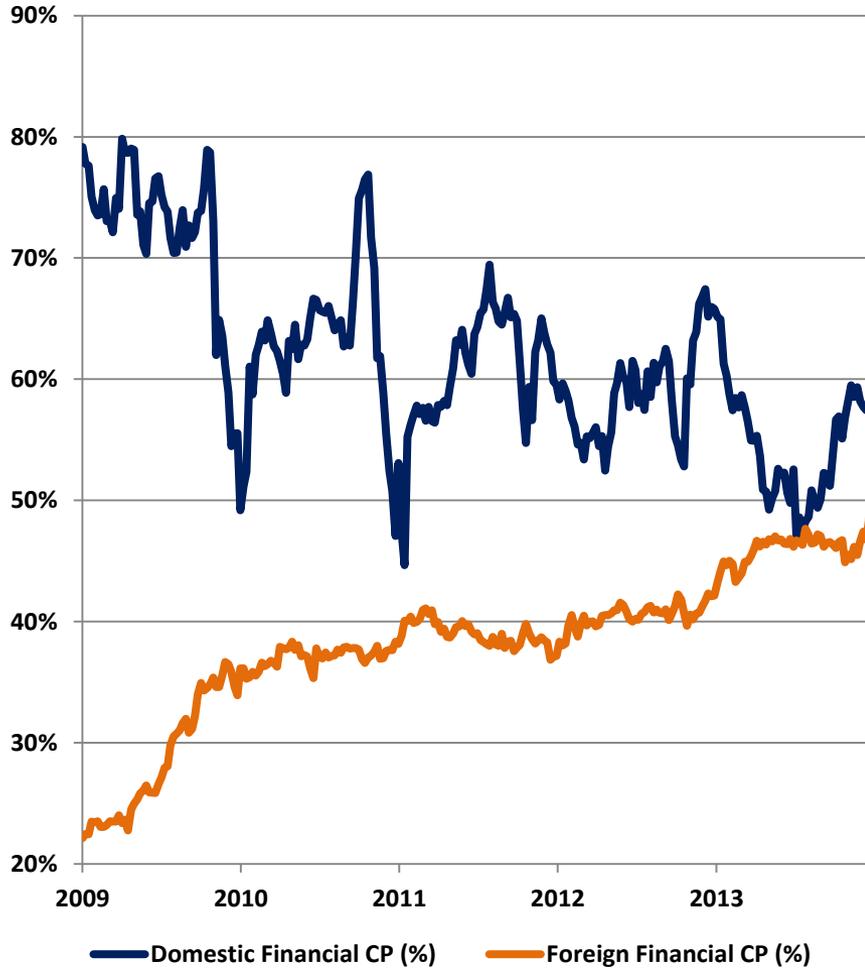
Fed Reserve Reverse Repo Facility



Source: Federal Reserve

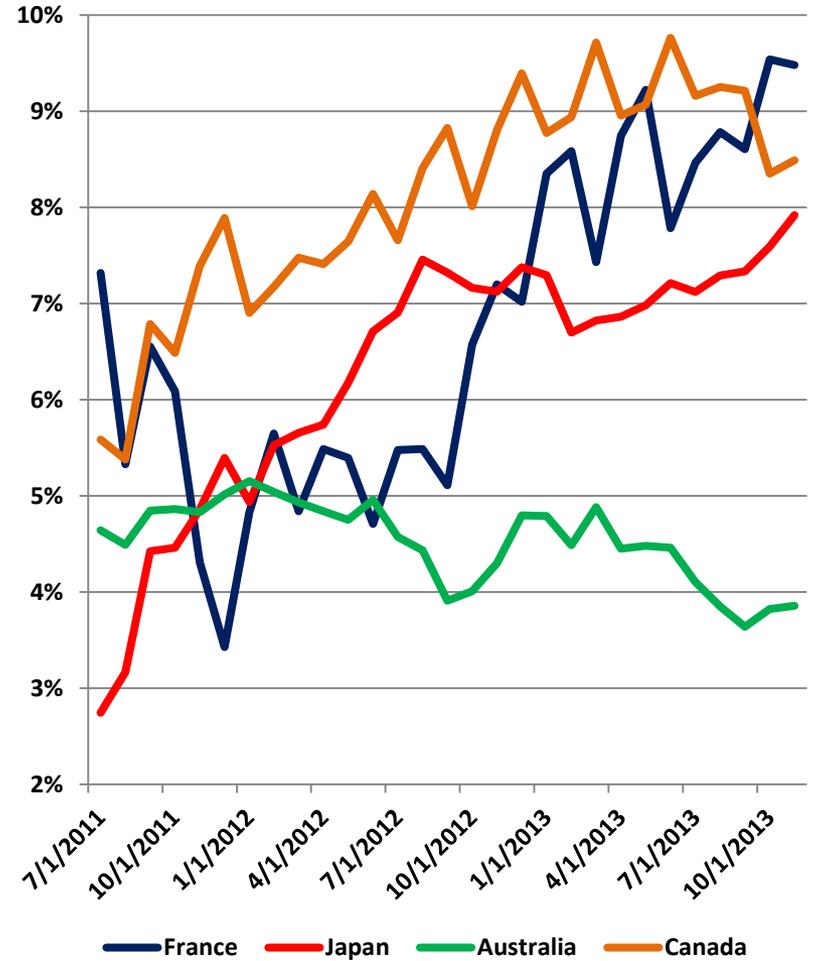
Investment Trends: Portfolio Credit Quality

Financial Corp CP



Source: Federal Reserve

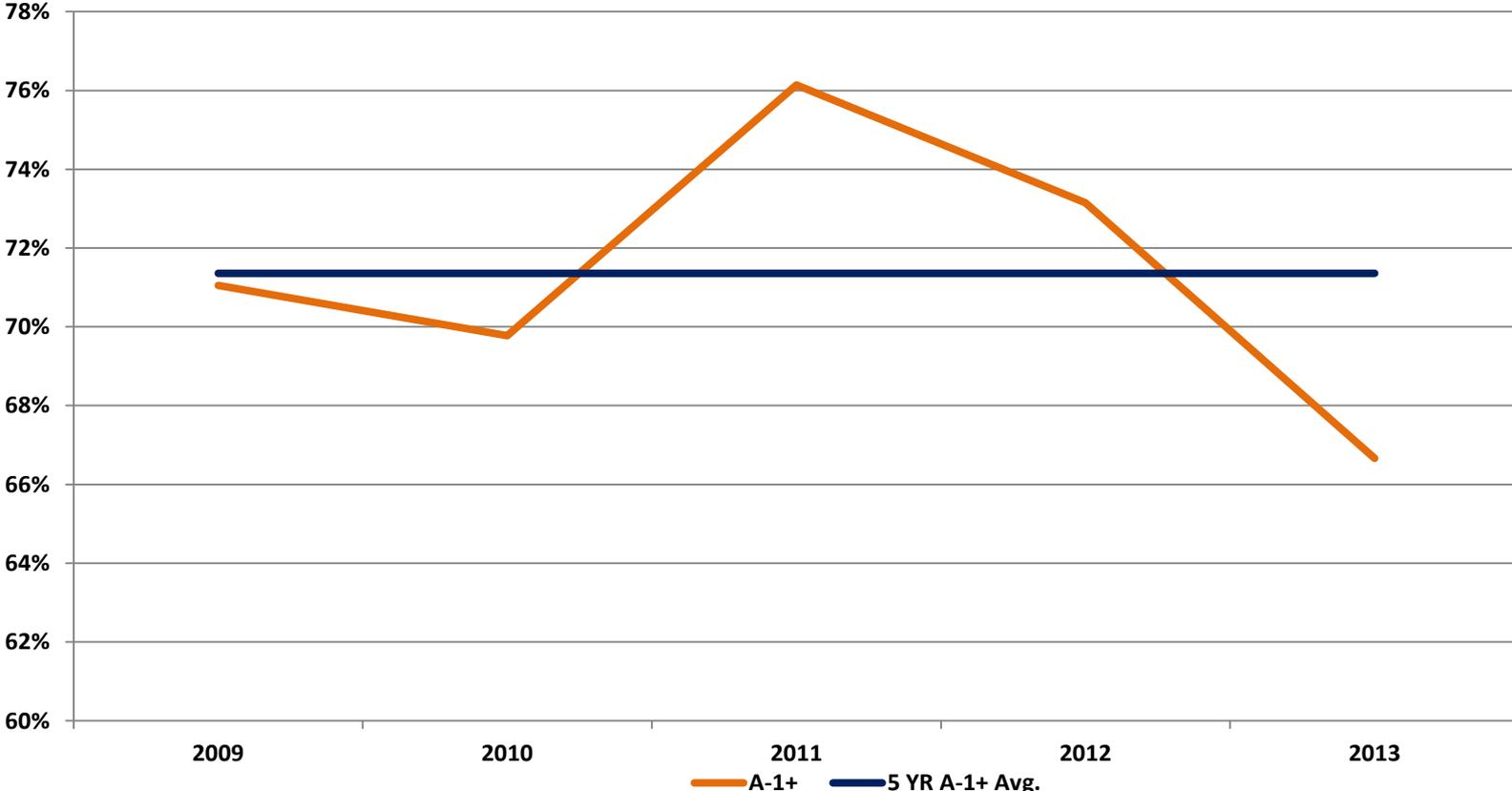
Country Exposure in MMF



Source: Crane Data LLC

Investment Trends: Portfolio Credit Quality

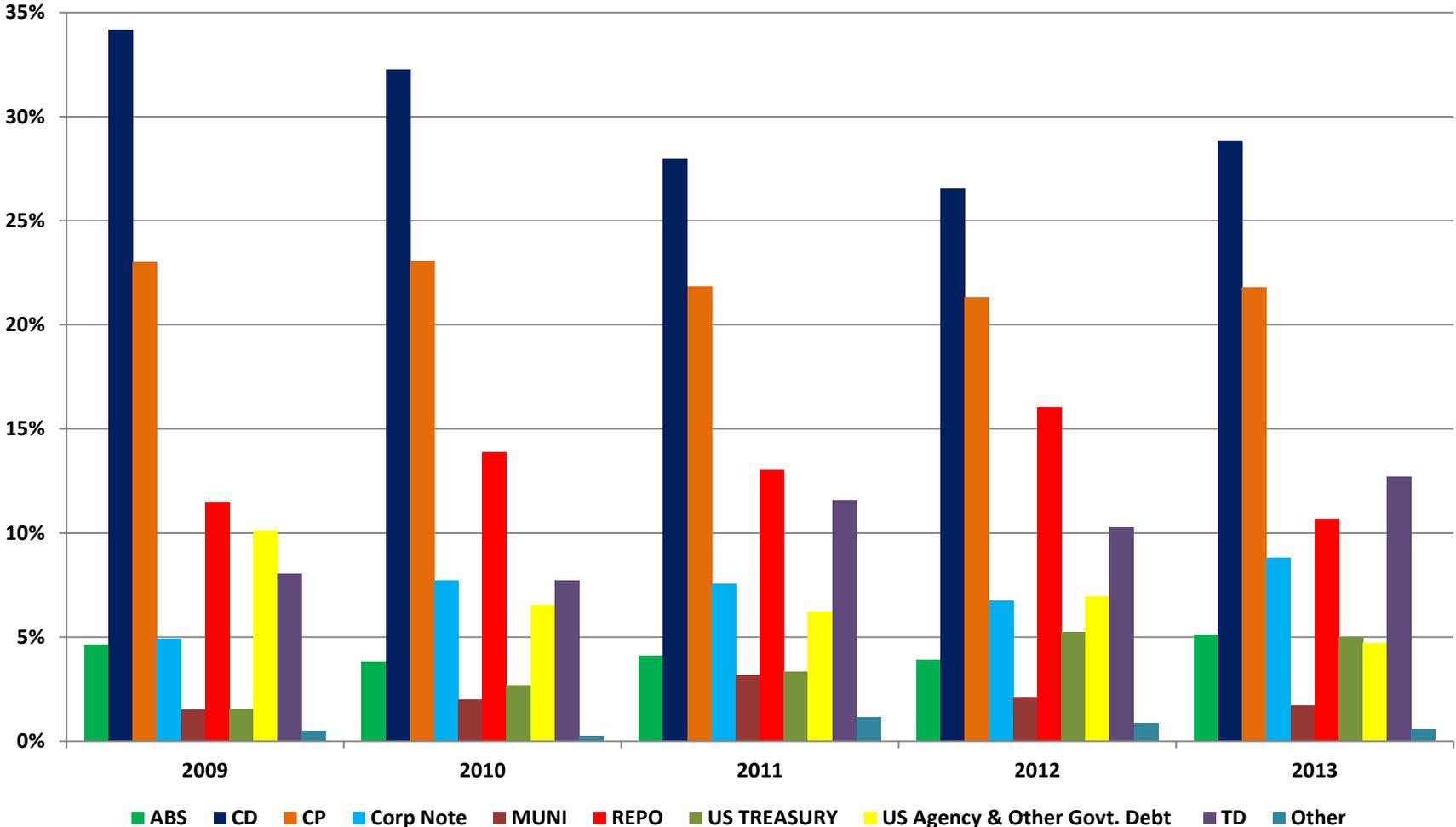
S&P PSFR Universe: Credit Quality



Source: Standard & Poor's

Investment Trends: Portfolio Composition

S&P PSFR Universe: Security Type



Source: Standard & Poor's

Appendix

Principal Stability Fund Ratings Definitions *(Effective January 5, 2010)*

- **A Standard & Poor's principal stability fund rating, also known as a "money market fund rating," is a forward-looking opinion about a fixed income fund's capacity to maintain stable principal (net asset value).** When assigning a principal stability rating to a fund, Standard & Poor's analysis focuses primarily on the creditworthiness of the fund's investments and counterparties, and also its investments' maturity structure and management's ability and policies to maintain the fund's stable net asset value. Principal stability fund ratings are assigned to funds that seek to maintain a stable or an accumulating net asset value.
- Generally, when faced with an unanticipated level of redemption requests during periods of high market stress, the manager of any fund may suspend redemptions for up to five business days or meet redemption requests with payments in-kind in lieu of cash. **A temporary suspension of redemptions or meeting redemption requests with distributions in-kind does not constitute a failure to maintain stable net asset values.** However, higher rated funds are expected to have stronger capacities to pay investor redemptions in cash during times of high market stress because they generally comprise shorter maturity and higher quality investments.
- **Principal stability fund ratings, or money market fund ratings, are identified by the 'm' suffix** (e.g., 'AAAm') to distinguish the principal stability rating from a Standard & Poor's traditional issue or issuer credit rating. A traditional issue or issuer credit rating reflects Standard & Poor's view of a borrower's ability to meet its financial obligations. Principal stability fund ratings are not commentaries on yield levels.

Summary of Main Differences Amongst 'm' & 'f' ratings

	Principal Stability Fund Ratings; aka Money Market Fund Ratings (eg. 'AAAm')	Fund Credit Quality & Volatility Ratings; aka Bond Fund Ratings (eg. 'AAAf/S1')
Eligible Investments (According to Rating)	We require a short term rating of at least 'A-1'. If it is not rated by S&P but has the highest short-term rating of another NRSRO, it must either be backed by a highly rated LOC provider, or have an S&P long term rating of at least 'AA'.	The securities must be rated by S&P or another NRSRO. If it is unrated by S&P, certain notching rules may apply.
Ratings Breakdown	For 'AAAm' rated funds, at least 50% must be in 'A-1+', with the other 50% in 'A-1' securities. For 'AAM' funds, 20% is required in 'A-1+', with the other 80% in 'A-1' securities, with up to 5% in overnight 'A-2' securities. For 'Am' funds, 100% may be in 'A-1', with up to 10% in overnight 'A-2' securities.	There is no minimum requirement, but the outcome of the rating will be dependent on our "ratings matrix." The Fund Credit Quality Ratings Matrix takes into account the rating on the security (long term or short term), the maturity (< 90 days, > 90 but <= 365 days, > 365 days), and the percentage held by the fund in each security.
Types of Securities	Common security types are Repurchase Agreements, Fixed and Floating Corporate Bonds, Commercial Paper, Certificates of Deposits, U.S. Treasury Securities, U.S. Agency Securities, etc.	Common security types are Mortgage Backed Securities, Fixed and Floating Rate Corporate Bonds, Commercial Paper, Certificates of Deposits, U.S. Treasuries, U.S. Agencies, Municipal Bonds, etc.
Reporting Frequency	Fund must submit weekly surveillance.	Fund must submit monthly surveillance.
NAV	When the NAV of a 'AAAm' rated fund moves outside 0.9985 and 1.0015, daily pricing is required. If the NAV for a 'AAAm' fund continues to deviate beyond 0.9975 or 1.0025, rating action may be taken.	The NAV may fluctuate but a material deviation may impact the fund volatility rating.
Weighted Average Maturity (WAM) Guidelines	'AAAm' - 60 days, 'AAM' - 75 days, 'Am' and 'BBBm' - 90 days	There is no WAM limit, but the longer the maturity dates, the more likely it is that the security will contribute to a lower rating.

Fund Credit Quality Ratings Symbols & Definitions

AAAf	Portfolio holdings provide EXTREMELY STRONG protection against losses from credit defaults
AAf	Portfolio holdings provide VERY STRONG protection against losses from credit defaults
Af	Portfolio holdings provide STRONG protection against losses from credit defaults
BBBf	Portfolio holdings provide ADEQUATE protection against losses from credit defaults
BBf	Portfolio holdings provide UNCERTAIN protection against losses from credit defaults
Bf	Portfolio holdings provide VULNERABLE protection against losses from credit defaults
CCCf	Portfolio holdings provide EXTREMELY VULNERABLE protection against losses from credit defaults

Plus (+) or minus (-)

The ratings from 'AAf' to 'CCCf' may be modified by the addition of a plus (+) or minus (-) sign to show relative standing within the rating categories.

Fund Credit Quality Ratings Methodology

- **Evaluation of Fund's Portfolio Credit Risk**
 - Use of credit matrix approach derived from S&P's historical default and ratings transition studies based on singular, discrete, worst-case one-year default rates experienced since 1981.
 - Factors and scores from matrix applied to fund's portfolio holdings.
 - All securities rated by a nationally recognized statistical rating organisation.
- **Maturity of Securities Considered**
 - Maturity buckets within matrix distinguish long term securities from short term securities.
 - Recognizes that probability of default decreases as security nears maturity.
- **Treatment of Non-Standard & Poor's Rated Issues**
 - Securities rated by other rating agencies (not exceeding 25% in total) are "haircut" for purposes of credit matrix score.
- **Management**
 - Detailed assessment of depth and quality of research and analysis, consistency of approach, and risk tolerance.
- **Qualitative Credit Overlay Process**
 - The strength of manager's overall credit analysis may allow rating to be enhanced by one notch.

Fund Volatility Ratings Methodology

Portfolio-level risk analysis

- **Focuses on interest rate risk, currency risk, credit quality, liquidity, concentration, call and option risks. The effects of various portfolio strategies such as the use of leverage, hedging, and derivative instruments are also factored in.**

Historical return volatility analysis

- **A minimum of 36 months are looked at in relation to established fixed income government indices with different maturity bands and we review how past volatility relates to the portfolio's investment objectives and construction process**

Management assessment

- **In depth understanding of different factors that could affect a fund's overall risk profile: Management sophistication and experience, portfolio strategies, internal research capabilities, risk controls, portfolio rotation, etc.**

NOTES:

- *A fund volatility rating has no influence on an assigned fund credit quality rating but a fund's credit quality rating could impact a fund's volatility rating.*
- *A volatility rating can be assigned with or without a credit rating but a credit rating must have a volatility rating if it differs by more than two categories. (i.e. AAAf rated funds must take the volatility rating if it would be less than S3)*

Fund Volatility Ratings Symbols & Definitions

<i>Rating</i>	<i>Pool's Sensitivity To Changing Market Conditions</i>	<i>Aggregate Risk Level</i>
S1*	Low	1 To 3 Year U.S. Governments
S2	Low To Moderate	3 To 7 Year U.S. Governments
S3	Moderate	7 To 10 Year U.S. Governments
S4	Moderate To High	10+ Year U.S. Governments
S5	High	Concentrated, Illiquid /Leveraged
S6	Highest	Highly Speculative

* Within the S-1 category certain pools may be designated with a plus sign (+). This indicates the pool's extremely low sensitivity to changing market conditions. Additionally, these pools possess a risk level that is less than or equal to a portfolio comprised of the highest quality instruments with an average maturity of one year or less.



Questions & Answers

Thank You

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