STATEMENT OF INVESTMENT POLICY

Purpose

The City Council has adopted this Investment Policy (the Policy) in order to establish the scope of the investment policy, investment objectives, standards of care, authorized investments, investment parameters, reporting, investment policy compliance and adoption, and the safekeeping and custody of assets.

This Policy is organized in the following sections:

A. SCOPE OF INVESTMENT POLICY

1. Pooling of Funds
All cash shall be pooled for investment purposes. The investment income derived from the pooled investment shall be allocated to the contributing funds, net of all banking and investing expenses, based upon the proportion of the respective average balances relative to the total pooled balance. Investment income shall be distributed to the individual funds not less than annually.

2. Funds Included in the Policy
The provisions of this Policy shall apply to all financial assets of the City as accounted for in the City's Comprehensive Annual Financial Report, including;
a) General Fund
b) Special Revenue Funds
c) Capital Project Funds
d) Enterprise Funds
e) Internal Service Funds
f) Trust and Agency Funds
g) Permanent Endowment Funds
h) Any new fund created unless specifically exempted

If the City invests funds on behalf of another agency and, if that agency does not have its own investment policy, this Policy shall govern the agency's investments.

3. Funds Excluded from the Policy
Bond Proceeds – Investment of bond proceeds will be made in accordance with applicable bond indentures.

B. INVESTMENT OBJECTIVES

The City's funds shall be invested in accordance with all applicable City policies and codes, State statutes, and Federal regulations, and in a manner designed to accomplish the following objectives, which are listed in priority order:

1. Safety
Preservation of principal is the foremost objective of the investment program. Investments of the City shall be undertaken in a manner that seeks to ensure the preservation of capital in the overall portfolio. The objective shall be to mitigate credit risk and interest rate risk. To attain this objective, the City shall diversify its investments by investing funds among several financial institutions and a variety of securities offering independent returns.

a) <u>Credit Risk</u>
The City shall minimize credit risk, the risk of loss due to the failure of the security issuer or backer, by:

- Limiting investments in securities that have higher credit risks, pre-qualifying the financial institutions, broker/dealers, intermediaries, and advisors with which the City will do business
- Diversifying the investment portfolio so as to minimize the impact any one industry/investment class can have on the portfolio

b) <u>Interest Rate Risk</u>
To minimize the negative impact of material changes in the market value of securities in the portfolio, the City shall:

- Structure the investment portfolio so that securities mature concurrent with cash needs to meet anticipated demands, thereby avoiding the need to sell securities on the open market prior to maturity
- Invest in securities of varying maturities

2. Liquidity
The City's investment portfolio shall remain sufficiently liquid to enable the City to meet all operating requirements which might be reasonably anticipated without requiring a sale of securities. Since all possible cash demands cannot be anticipated, the portfolio should consist largely of securities with active secondary or resale markets. A portion of the portfolio also may be placed in money market mutual funds or LAIF which offer same-day liquidity for short-term funds.

3. Yield
The City's investment portfolio shall be designed with the objective of attaining a benchmark rate of return throughout budgetary and economic cycles, commensurate with the City's investment risk constraints and the liquidity characteristics of the portfolio. Return on investment is of secondary importance compared to the safety and liquidity objectives described above. The core of investments is limited to relatively low risk securities in anticipation of earning a fair return relative to the risk being assumed.

C. STANDARDS OF CARE

1. Prudence
The standard of prudence to be used for managing the City's investment program is California Government Code Section 53600.3, the prudent investor standard, which states that "when investing, reinvesting, purchasing, acquiring, exchanging, selling, or managing public funds, a trustee shall act with care, skill, prudence, and diligence under the circumstances then prevailing, including, but not limited to, the general economic conditions and the anticipated needs of the agency, that a prudent person acting in a like capacity and familiarity with those matters would use in the conduct of funds of a like character and with like aims, to safeguard the principal and maintain the liquidity needs of the agency."

The City's overall investment program shall be designed and managed with a degree of professionalism that is worthy of the public trust. The City recognizes that no investment is totally without risk and that the investment activities of the City are a matter of public record. Accordingly, the City recognizes that occasional measured losses may occur in a diversified portfolio and shall be considered within the context of the overall portfolio's return, provided that adequate diversification has been implemented and that the sale of a security is in the best long-term interest of the City.

The Finance Director and authorized investment personnel acting in accordance with established procedures and exercising due diligence shall be relieved of personal responsibility for an individual security's credit risk or market price changes, provided that deviations from expectations are reported in a timely fashion to the City Council and appropriate action is taken to control adverse developments.

2. Ethics and Conflicts of Interest

Elected officials and employees involved in the investment process shall refrain from personal business activity that could conflict with proper execution of the City's investment program or could impair or create the appearance of an impairment of their ability to make impartial investment decisions. Employees and investment officials shall subordinate their personal investment transactions to those of the City. In addition, City Council members, the City Manager, and the Finance Director shall file a Statement of Economic Interests each year as required by California Government Code Section 87203 and regulations of the Fair Political Practices Commission.

3. Delegation of Authority

Authority to manage the City's investment program is derived from the Charter of the City of Newport Beach section 605 (j). The Finance Director shall assume the title of and act as City Treasurer and with the approval of the City Manager appoint deputies annually as necessary to act under the provisions of any law requiring or permitting action by the City Treasurer. The Finance Director may then delegate the authority to conduct investment transactions and to manage the operation of the investment portfolio to other specifically authorized staff members. No person may engage in an investment transaction except as expressly provided under the terms of this Policy.

The City may engage the support services of outside investment advisors with respect to its investment program, so long as it can be demonstrated that these services produce a net financial advantage or necessary financial protection of the City's financial resources. Such companies must be registered under the Investment Advisors Act of 1940, be well-established and exceptionally reputable. Members of the staff of such companies who will have primary responsibility for managing the City's investments must have a working familiarity with the special requirements and constraints of investing municipal funds in general and this City's funds in particular. These firms must insure that the portion of the portfolio under their management complies with various concentration and other constraints specified herein, and contractually agree to conform to all provisions of governing law and the collateralization and other requirements of this Policy. Selection and retention of broker/dealers by investment advisors shall be at their sole discretion and dependent upon selection and retention criteria as stated in the Uniform Application for Investment Advisor Registration and related Amendments (SEC Form ADV 2A).

4. Internal Controls
The Finance Director is responsible for establishing and maintaining a system of internal controls. The internal controls shall be designed to prevent losses of public funds arising from fraud, employee error, and misrepresentation by third parties, unanticipated changes in financial markets, or imprudent action by City employees and officers. The internal structure shall be designed to provide reasonable assurance that these objectives are met. The concept of reasonable assurance recognizes that (1) the cost of a control should not exceed the benefits likely to be derived, and (2) the valuation of costs and benefits requires estimates and judgments by management.

D. BANKING SERVICES

Banking services for the City shall be provided by FDIC insured banks approved to provide depository and other banking services. To be eligible, a bank shall qualify as a depository of public funds in the State of California as defined in California Government Code Section 53630.5 and shall secure deposits in excess of FDIC insurance coverage in accordance with California Government Code Section 53652.

E. BROKER/DEALERS

In the event that an investment advisor is not used to purchase securities, the City will select broker/dealers on the basis of their expertise in public cash management and their ability to provide service to the City’s account.

Each approved broker/dealer must possess an authorizing certificate from the California Commissioner of Corporations as required by Section 25210 of the California Corporations Code.

To be eligible, a firm must meet at least one of the following criteria:

1. Be recognized as Primary Dealers by the Federal Reserve Bank of New York or have a primary dealer within their holding company structure, or
2. Report voluntarily to the Federal Reserve Bank of New York, or
3. Qualify under Securities and Exchange Commission (SEC) Rule 15c3-1 (Uniform Net Capital Rule).

F. SAFEKEEPING AND CUSTODY OF ASSETS

The Finance Director shall select one or more banks to provide safekeeping and custodial services for the City. A Safekeeping Agreement approved by the City shall be executed with each custodian bank prior to utilizing that bank's safekeeping services.

Custodian banks will be selected on the basis of their ability to provide services for the City's account and the competitive pricing of their safekeeping related services.

The purchase and sale of securities and repurchase agreement transactions shall be settled on a delivery versus payment basis. All securities shall be perfected in the name of the City. Sufficient evidence to title shall be consistent with modern investment, banking and commercial practices.

All investment securities, except non-negotiable Certificates of Deposit, Money Market Funds and local government investment pools, purchased by the City will

be delivered by book entry and will be held in third-party safekeeping by a City approved custodian bank, its correspondent bank or its Depository Trust Company (DTC) participant account.

All Fed wireable book entry securities owned by the City shall be held in the Federal Reserve system in a customer account for the custodian bank which will name the City as “customer.”

All DTC eligible securities shall be held in the custodian bank’s DTC participant account and the custodian bank shall provide evidence that the securities are held for the City as “customer.”

G. AUTHORIZED INVESTMENTS

All investments and deposits of the City shall be made in accordance with California Government Code Sections 16429.1, 53600-53609 and 53630-53686. Any revisions or extensions of these code sections will be assumed to be part of this Policy immediately upon being enacted. The City has further restricted the eligible types of securities and transactions. The foregoing list of authorized securities and transactions shall be strictly interpreted. Any deviation from this list must be pre-approved by resolution of the City Council. In the event an apparent discrepancy is found between this Policy and the Government Code, the more restrictive parameter(s) will take precedence.

Where this section specifies a percentage limitation or minimum credit rating for a particular security type, that percentage or credit rating minimum is applicable only at the date of purchase.

1. Investments Specifically Permitted

    a) United States Treasury bills, notes, or bonds with a final maturity not exceeding five years from the date of trade settlement. There is no limitation as to the percentage of the City’s portfolio that may be invested in this category.

b) Federal Instrumentality (government-sponsored enterprise) debentures, discount notes, callable and step-up securities, with a final maturity not exceeding five years from the date of trade settlement. There is no limitation as to the percentage of the portfolio that can be invested in this category. No more than thirty percent (30%) of the portfolio may be invested in any single Federal Instrumentality/GSE issuer. The maximum percentage of callable Federal Instrumentality/GSE securities in the portfolio will be twenty percent (20%.)

c) Federal Agency Obligations for which the full faith and credit of the United States are pledged for the payment of principal and interest and which have a final maturity not exceeding five years from the date of trade settlement. There is no limitation as to the percentage of the portfolio that can be invested in this category.

d) Mortgage-backed Securities, Collateralized Mortgage Obligation (CMO) and Asset-backed Securities from issuers not defined sections a, b and c of the Investments Specifically Permitted section of this investment policy are limited to bonds with a final maturity not exceeding five years from the date of trade settlement. The security itself shall be rated at least “AAA” or the equivalent by an NRSRO. No more than five percent (5%) of the City’s total portfolio shall be invested in any one issuer of mortgage-backed and asset-backed securities listed above, and the aggregate investment in mortgage-backed and asset-backed securities shall not exceed twenty percent (20%) of the City’s total portfolio.

e) Medium-Term Notes issued by corporations organized and operating within the United States or by depository institutions licensed by the United States or any state and operating within the United States, with a final maturity not exceeding five years from the date of trade settlement, and rated in at least the “A” category or the equivalent by an NRSRO. No more than five percent (5%) of the City’s total portfolio shall be invested in any one issuer of medium- term notes, and the aggregate investment in medium-term notes shall not exceed thirty percent (30%) of the City’s total portfolio.

f) Municipal Bonds including bonds issued by the City of Newport Beach, including bonds payable solely out of the revenues from a revenue-producing property owned, controlled, or operated by the City or by a department, board, agency, or authority of the City.

State of California registered warrants or treasury notes or bonds, including bonds payable solely out of the revenues from a revenue- producing property owned, controlled, or operated by the state or by a department, board, agency, or authority of the state.

Registered treasury notes or bonds of any of the other 49 states in addition to California, including bonds payable solely out of the revenues from a revenue producing property owned, controlled, or operated by a state or by a department, board, agency, or authority of any of the other 49 states, in addition to California.

Bonds, notes, warrants, or other evidences of indebtedness of a local agency within California, including bonds payable solely out of the revenues from a revenue-producing property owned, controlled, or operated by the local agency, or by a department, board, agency, or authority of the local agency.

In addition, these securities must be rated in at least the “A” category or the equivalent by a NRSRO with maturities not exceeding five years from the date of trade settlement. No more than five percent (5%) of the City’s total portfolio shall be invested in any one municipal issuer. In addition, the aggregate investment in municipal bonds may not exceed thirty percent (30%) of the portfolio.

g) <u>Non-negotiable Certificates of Deposit</u> and savings deposits with a maturity not exceeding two years from the date of trade settlement, in FDIC insured state or nationally chartered banks or savings banks that qualify as a depository of public funds in the State of California as defined in California Government Code Section 53630.5. Deposits exceeding the FDIC insured amount shall be secured pursuant to California Government Code Section 53652. No one issuer shall exceed more than five percent (5%) of the portfolio, and investment in negotiable and nonnegotiable certificates of deposit shall be limited to thirty percent (30%) of the portfolio combined.

h) <u>Negotiable Certificates of Deposit</u> only with a nationally or state- chartered bank, a savings association or a federal association (as defined by Section 5102 of the Financial Code), a state or federal credit union, or by a federally licensed or state-licensed branch of a foreign bank whose senior long-term debt is rated in at least the “A” category, or the equivalent, or short-term debt is rated at least “A-1” or the equivalent by an NRSRO and having assets in excess of $10 billion, so as to ensure security and a large, well-established secondary market. Ease of subsequent marketability should be further ascertained prior to initial investment by examining currently quoted bids by primary dealers and the acceptability of the issuer by these dealers. No one issuer shall exceed more than five percent (5%) of the portfolio, and maturity shall not exceed two years. Investment in negotiable and non- negotiable certificates of deposit shall be limited to thirty percent (30%) of the portfolio combined.

i) <u>Prime Commercial Paper</u> with a maturity not exceeding 270 days from the date of trade settlement that is rated “A-1”, or the equivalent, by an NRSRO. The entity that issues the commercial paper shall meet all of the following conditions in either sub- paragraph i. or sub-paragraph ii. below:

i. The entity shall (1) be organized and operating in the United States as a general corporation, (2) have total assets in excess of $500,000,000 and (3) have debt other than commercial paper, if any, that is rated in at least the “A” category or the equivalent by an NRSRO.

ii. The entity shall (1) be organized within the United States as a special purpose corporation, trust, or limited liability company, (2) have program wide credit enhancements, including, but not limited to, over collateralization, letters of credit or surety bond and (3) have commercial paper that is rated at least “A-1” or the equivalent, by an NRSRO.

iii. No more than five percent (5%) of the City’s total portfolio shall be invested in the commercial paper of any one issuer, and the aggregate investment in commercial paper shall not exceed twenty-five percent (25%) of the City’s total portfolio. Under a provision sunsetting on January 1, 2026, no more than forty percent (40%) of the portfolio may be invested in commercial paper if the City’s assets under management are greater than $100,000,000.

j) Eligible Banker’s Acceptances with a maturity not exceeding 180 days from the date of trade settlement, drawn on and accepted by a commercial bank whose senior long-term debt is rated in at least the “A” category or the equivalent by an NRSRO at the time of purchase. Banker’s Acceptances shall be rated at least “A-1”, or the equivalent at the time of purchase by an NRSRO. If the bank has senior debt outstanding, it must be rated in at least the “A” category or the equivalent by an NRSRO. The aggregate investment in banker’s acceptances shall not exceed forty percent (40%) of the City’s total portfolio, and no more than five percent (5%) of the City’s total portfolio shall be invested in banker’s acceptances of any one bank.

k) Repurchase Agreements and Reverse Repurchase Agreements with a final termination date not exceeding 30 days collateralized by U.S. Treasury obligations or Federal Instrumentality securities listed in items 1 and 2 above with the maturity of the collateral not exceeding ten years. For the purpose of this section, the term collateral shall mean purchased securities under the terms of the City’s approved Master Repurchase Agreement. The purchased securities shall have a minimum market value including accrued interest of one hundred and two percent (102%) of the dollar value of the funds borrowed. Collateral shall be held in the City's custodian bank, as safekeeping agent, and the market value of the collateral securities shall be marked-to-the-market daily.

Repurchase Agreements and Reverse Repurchase Agreements shall be entered into only with broker/dealers and who are recognized as Primary Dealers with the Federal Reserve Bank of New York, or with firms that have a Primary Dealer within their holding company structure. Primary Dealers approved as Repurchase Agreement counterparties shall have a short-term credit rating of at least “A-1” or the equivalent and a long-term credit rating of at least “A” or the equivalent. Repurchase agreement counterparties shall execute a City approved Master Repurchase Agreement with the City. The Finance Director shall maintain a copy of the City's approved Master Repurchase Agreement and a list of the broker/dealers who have executed same.

In addition, the City must own assets for more than 30 days before they can be used as collateral for a reverse repurchase agreement. No more than ten percent (10%) of the portfolio can be involved in reverse repurchase agreements.

l) State of California’s Local Agency Investment Fund (LAIF), pursuant to California Government Code Section 16429.1.

m) California Asset Management Trust Cash Reserve Portfolio (CAMP): Investments in CAMP shall not exceed the same maximum limit established for LAIF.

n)

o) Mutual Funds and Money Market Mutual Funds registered under the Investment Company Act of 1940, provided that:

   i. **MUTUAL FUNDS** that invest in the securities and obligations as authorized under California Government Code, Section 53601 (a) to (k) and (m) to (q) inclusive and that meet either of the following criteria:

      1) Attained the highest ranking or the highest letter and numerical rating provided by not less than two (2) NRSROs; or

2) Have retained an investment adviser registered or exempt from registration with the Securities and Exchange Commission with not less than five years' experience investing in the securities and obligations authorized by California Government Code, Section 53601 and with assets under management in excess of $500 million.

3) No more than 10% of the total portfolio may be invested in shares of any one mutual fund.

ii. **MONEY MARKET MUTUAL FUNDS** registered with the Securities and Exchange Commission under the Investment Company Act of 1940 and issued by diversified management companies and meet either of the following criteria:

1) Have attained the highest ranking or the highest letter and numerical rating provided by not less than two (2) NRSROs; or

2) Have retained an investment adviser registered or exempt from registration with the Securities and Exchange Commission with not less than five years' experience managing money market mutual funds with assets under management in excess of $500 million.

3) No more than 20% of the total portfolio may be invested in Money Market Mutual Funds.

iii. No more than 20% of the total portfolio may be invested in these securities.

p) <u>Supranationals</u> which are United States dollar denominated senior unsecured unsubordinated obligations issued or unconditionally guaranteed by the International Bank for Reconstruction and Development (IBRD), International Finance Corporation (IFC), or Inter-American Development Bank (IADB), with a maximum remaining maturity of five years or less from the date of trade settlement, and eligible for purchase and sale within the United States. Investments under this paragraph shall be rated in the "AA" category, its equivalent, or better by at least one NRSRO.

No more than ten percent (10%) of the City's total portfolio shall be invested in any one issuer of supranational obligations. Purchases of supranational obligations shall not exceed twenty percent (20%) of the investment portfolio of the City.

2. Investments Specifically Not Permitted

Any security type or structure not specifically approved by this policy is hereby prohibited. Security types, which are thereby prohibited include, but are not limited to: "exotic" derivative structures such as range notes, dual index notes, inverse floating rate notes, leveraged or de-leveraged floating rate notes, interest only strips that are derived from a pool of mortgages and any security that could result in zero interest accrual if held to maturity, or any other complex variable or structured note with an unusually high degree of volatility risk.

Under a provision sunsetting on January 1, 2026, securities backed by the U.S. Government that could result in a zero or negative interest accrual if held to maturity are permitted.

The City shall not invest funds with the Orange County Pool.

The purchase of a security with a forward settlement date exceeding 45 days from the time of the investment is prohibited.

3. Exceptions to Prohibited and Restricted Investments

The City shall not be required to sell securities prohibited or restricted in this policy, or any future policies, or prohibited or restricted by new State regulations, if purchased prior to their prohibition and/or restriction. Insofar as these securities provided no notable credit risk to the City, holding of these securities until maturity is approved. At maturity or liquidation, such monies shall be reinvested as provided by this policy.

H. INVESTMENT PARAMETERS

1. Diversification

The City shall diversify its investments to avoid incurring unreasonable risks inherent in over-investing in specific instruments, individual financial institutions or maturities. As such, no more than five percent (5%) of the City's portfolio may be invested in the instruments of any one issuer, except governmental issuers, supranationals, investment pools, mutual funds and money market funds, or unless otherwise specified in this investment policy. This restriction does not apply to any type of Federal Instrumentality or Federal Agency Security listed in Sections G1 b and G1 c above. Nevertheless, the asset allocation in the investment portfolio should be flexible depending upon the outlook for the economy, the securities markets and the City's anticipated cash flow needs.

2. Maximum Maturities

To the extent possible, investments shall be matched with anticipated cash flow requirements and known future liabilities. The City will not invest in securities maturing more than five years from the date of trade settlement, unless the City Council has by resolution granted authority to make such an investment at least three months prior to the date of investment.

3. Credit Quality

   Each investment manager will monitor the credit quality of the securities in their respective portfolio. In the event a security held by the City is downgraded to a level below the requirements of this policy, making the security ineligible for additional purchases, the following steps will be taken:

   - Any actions taken related to the downgrade by the investment manager will be communicated to the Finance Director in a timely manner.
   - If a decision is made to retain the security, the credit quality will be monitored and reported to the City Council.

4. Competitive Transactions

   Investment advisors shall make best effort to price investment transactions on a competitive basis with broker/dealers selected consistent with their practices disclosed in form ADV 2A filed with the SEC. Where possible, at least three broker/dealers shall be contacted for each transaction and their bid or offering prices shall be recorded. If there is no other readily available competitive offering, the investment advisor shall make their best efforts to document quotations for comparable or alternative securities. If qualitative characteristics of a transaction, including, but not limited to, complexity of the transaction, or sector expertise of the broker, prevent a competitive selection process, investment advisors shall use brokerage selection practices as described above.

I. PORTFOLIO PERFORMANCE

The investment portfolio shall be designed to attain a market rate of return throughout budgetary and economic cycles, taking into account prevailing market conditions, risk constraints for eligible securities, and cash flow requirements. The performance of the City's investments shall be compared to the total return of a benchmark that most closely corresponds to the portfolio's duration, universe of allowable securities, risk profile, and other relevant characteristics. When comparing the performance of the City's portfolio, its rate of return will be computed consistent with Global Investment Performance Standards (GIPS).

J. REPORTING

Monthly, the Finance Director shall produce a treasury report of the investment portfolio balances, transactions, risk characteristics, earnings, and performance results of the City's investment portfolio available to City Council and the public on the City's Website. The report shall include the following information:

1. Investment type, issuer, date of maturity, par value and dollar amount invested in all securities, and investments and monies held by the City;
2. A description of the funds, investments and programs;

3. A market value as of the date of the report (or the most recent valuation as to assets not valued monthly) and the source of the valuation;
4. A statement of compliance with this Policy or an explanation for non-compliance

K. INVESTMENT POLICY COMPLIANCE AND ADOPTION

1. Compliance
   Any deviation from the policy shall be reported to Finance Committee as soon as practical, but no later than the next scheduled Finance Committee meeting. Upon recommendation of the Finance Committee, the Finance Director shall review deviations from policy with the City Council.

2. Adoption
   The Finance Director shall review the Investment Policy with the Finance Committee at least annually to ensure its consistency with the overall

   objectives of preservation of principal, liquidity and return, and its relevance to current law and financial and economic trends.

   The Finance Director shall review the Investment Policy with City Council at a public meeting if there are changes recommended to the Investment Policy.

History

Adopted F-1 – 4-6-1959
Reaffirmed F-1 – 8-15-1966
Reaffirmed F-1 – 11-12-1968
Reaffirmed F-1 – 3-9-1970
Amended F-1 – 11-9-1970
Reaffirmed F-1 – 2-8-1971
Reaffirmed F-1 – 2-14-1972
Reaffirmed F-1 – 12-10-1973
Amended F-1 – 2-11-1974
Amended F-1 –2-9-1981
Amended F-1 –10-27-1986
Rewritten F-1 – 10-22-1990
Amended F-1 – 1-28-1991

Amended F-1 – 1-24-1994
Amended F-1 – 1-9-1995
Amended F-1 – 4-22-1996
Corrected F-1 – 1-27-1997
Amended F-1 – 2-24-1997
Amended F-1 – 5-26-1998
Reaffirmed F-1 – 3-22-1999
Reaffirmed F-1 – 3-14-2000
Amended and Reaffirmed F-1 – 5-8-2001
Amended and Reaffirmed F-1 – 4-23-2002
Amended and Reaffirmed F-1 – 4-8-2003
Amended and Reaffirmed F-1 – 4-13-2004
Amended and Reaffirmed F-1 – 9-13-2005
Amended F-1 – 8-11-2009
Amended and Reaffirmed F-1 – 8-10-2010
Amended and Reaffirmed F-1 – 9-28-2010
Reaffirmed F-1 – 6-28-2011
Amended and Reaffirmed F-1 – 10-9-2012
Amended F-1 – 8-13-2013
Amended F-1 – 9-8-2015
Amended F-1 – 3-28-2017
Amended F-1 – 1-28-2020
Amended F-1 – 9-28-2021
Amended F-1 – 10-10-2023
Amended F-1 – 4-9-2024

GLOSSARY OF INVESTMENT TERMS

AGENCIES. Shorthand market terminology for any obligation issued by *a government-sponsored entity (GSE)*, or a *federally related institution*. Most obligations of GSEs are not guaranteed by the full faith and credit of the US government. Examples are:

FFCB. The Federal Farm Credit Bank System provides credit and liquidity in the agricultural industry. FFCB issues discount notes and bonds.

FHLB. The Federal Home Loan Bank provides credit and liquidity in the housing market. FHLB issues discount notes and bonds.

FHLMC. Like FHLB, the Federal Home Loan Mortgage Corporation provides credit and liquidity in the housing market. FHLMC, also called "FreddieMac" issues discount notes, bonds and mortgage pass-through securities.

FNMA. Like FHLB and FreddieMac, the Federal National Mortgage Association was established to provide credit and liquidity in the housing market. FNMA, also known as "FannieMae," issues discount notes, bonds and mortgage pass-through securities.

GNMA. The Government National Mortgage Association, known as "GinnieMae," issues mortgage pass-through securities, which are guaranteed by the full faith and credit of the US Government.

PEFCO. The Private Export Funding Corporation assists exporters. Obligations of PEFCO are not guaranteed by the full faith and credit of the US government.

TVA. The Tennessee Valley Authority provides flood control and power and promotes development in portions of the Tennessee, Ohio, and Mississippi River valleys. TVA currently issues discount notes and bonds.

ASKED. The price at which a seller offers to sell a security.

ASSET BACKED SECURITIES. Securities supported by pools of installment loans or leases or by pools of revolving lines of credit.

AVERAGE LIFE. In mortgage-related investments, including CMOs, the average time to expected receipt of principal payments, weighted by the amount of principal expected.

BANKER'S ACCEPTANCE. A money market instrument created to facilitate international trade transactions. It is highly liquid and safe because the risk of the trade transaction is transferred to the bank which "accepts" the obligation to pay the investor.

BENCHMARK. A comparison security or portfolio. A performance benchmark is a partial market index, which reflects the mix of securities allowed under a specific investment policy.

BID. The price at which a buyer offers to buy a security.

BROKER. A broker brings buyers and sellers together for a transaction for which the broker receives a commission. A broker does not sell securities from his own position.

CALLABLE. A callable security gives the issuer the option to call it from the investor prior to its maturity. The main cause of a call is a decline in interest rates. If interest rates decline since an issuer issues securities, it will likely call its current securities and reissue them at a lower rate of interest. Callable securities have reinvestment risk as the investor may receive its principal back when interest rates are lower than when the investment was initially made.

CERTIFICATE OF DEPOSIT (CD). A time deposit with a specific maturity evidenced by a certificate. Large denomination CDs may be marketable.

CERTIFICATE OF DEPOSIT ACCOUNT REGISTRY SYSTEM (CDARS). A private placement service that allows local agencies to purchase more than $250,000 in CDs from a single financial institution (must be a participating institution of CDARS) while still maintaining FDIC insurance coverage. CDARS is currently the only entity providing this service. CDARS facilitates the trading of deposits between the California institution and other participating institutions in amounts that are less than $250,000 each, so that FDIC coverage is maintained.

COLLATERAL. Securities or cash pledged by a borrower to secure repayment of a loan or repurchase agreement. Also, securities pledged by a financial institution to secure deposits of public monies.

COLLATERALIZED MORTGAGE OBLIGATIONS (CMO). Classes of bonds that redistribute the cash flows of mortgage securities (and whole loans) to create securities that have different levels of prepayment risk, as compared to the underlying mortgage securities.

COMMERCIAL PAPER. The short-term unsecured debt of corporations.

COST YIELD. The annual income from an investment divided by the purchase cost. Because it does not give effect to premiums and discounts which may have been included in the purchase cost, it is an incomplete measure of return.

COUPON. The rate of return at which interest is paid on a bond.

CREDIT RISK. The risk that principal and/or interest on an investment will not be paid in a timely manner due to changes in the condition of the issuer.

CURRENT YIELD. The annual income from an investment divided by the current market value. Since the mathematical calculation relies on the current market value rather than the investor's cost, current yield is unrelated to the actual return the investor will earn if the security is held to maturity.

DEALER. A dealer acts as a principal in security transactions, selling securities from and buying securities for his own position.

DEBENTURE. A bond secured only by the general credit of the issuer.

DELIVERY VS. PAYMENT (DVP). A securities industry procedure whereby payment for a security must be made at the time the security is delivered to the purchaser's agent.

DERIVATIVE. Any security that has principal and/or interest payments which are subject to uncertainty (but not for reasons of default or credit risk) as to timing and/or amount, or any security which represents a component of another security which has been separated from other components ("Stripped" coupons and principal). A derivative is also defined as a financial instrument the value of which is totally or partially derived from the value of another instrument, interest rate, or index.

DISCOUNT. The difference between the par value of a bond and the cost of the bond, when the cost is below par. Some short-term securities, such as T-bills and banker's acceptances, are known as discount securities. They sell at a discount from par, and return the par value to the investor at maturity without additional interest. Other securities, which have fixed coupons, trade at a discount when the coupon rate is lower than the current market rate for securities of that maturity and/or quality.

DIVERSIFICATION. Dividing investment funds among a variety of investments to avoid excessive exposure to any one source of risk.

DURATION. The weighted average time to maturity of a bond where the weights are the present values of the future cash flows. Duration measures the price sensitivity of a bond to changes in interest rates. (See Modified Duration).

FEDERAL FUNDS RATE. The rate of interest charged by banks for short-term loans to other banks. The Federal Reserve Bank through open-market operations establishes it.

FEDERAL OPEN MARKET COMMITTEE. A committee of the Federal Reserve Board that establishes monetary policy and executes it through temporary and permanent changes to the supply of bank reserves.

LEVERAGE. Borrowing funds in order to invest in securities that have the potential to pay earnings at a rate higher than the cost of borrowing.

LIQUIDITY. The speed and ease with which an asset can be converted to cash.

LOCAL AGENCY INVESTMENT FUND (LAIF). A voluntary investment fund open to government entities and certain non-profit organizations in California that is managed by the State Treasurer's Office.

LOCAL GOVERNMENT INVESTMENT POOL. Investment pools that range from the State Treasurer's Office Local Agency Investment Fund (LAIF) to county pools, to Joint Powers Authorities (JPAs). These funds are not subject to the same SEC rules applicable to money market mutual funds.

MAKE WHOLE CALL. A type of call provision on a bond that allows the issuer to pay off the remaining debt early. Unlike a call option, with a make whole call provision, the issuer makes a lump sum payment that equals the net present value (NPV) of future coupon payments that will not be paid because of the call. With this type of call, an investor is compensated, or "made whole."

MARGIN. The difference between the market value of a security and the loan a broker makes using that security as collateral.

MARKET RISK. The risk that the value of securities will fluctuate with changes in overall market conditions or interest rates.

MARKET VALUE. The price at which a security can be traded.

MARKING TO MARKET. The process of posting current market values for securities in a portfolio.

MATURITY. The final date upon which the principal of a security becomes due and payable.

MEDIUM TERM NOTES. Unsecured, investment-grade senior debt securities of major corporations which are sold in relatively small amounts on either a continuous or an intermittent basis. MTNs are highly flexible debt instruments that can be structured to respond to market opportunities or to investor preferences.

MODIFIED DURATION. The percent change in price for a 100 basis point change in yields. Modified duration is the best single measure of a portfolio's or security's exposure to market risk.

MONEY MARKET. The market in which short-term debt instruments (T-bills, discount notes, commercial paper, and banker's acceptances) are issued and traded.

MORTGAGE PASS-THROUGH SECURITIES. A securitized participation in the interest and principal cash flows from a specified pool of mortgages. Principal and interest payments made on the mortgages are passed through to the holder of the security.

MUNICIPAL SECURITIES. Securities issued by state and local agencies to finance capital and operating expenses.

MUTUAL FUND. An entity which pools the funds of investors and invests those funds in a set of securities which is specifically defined in the fund's prospectus. Mutual funds can be invested in various types of domestic and/or international stocks, bonds, and money market instruments, as set forth in the individual fund's prospectus. For most large, institutional investors, the costs associated with investing in mutual funds are higher than the investor can obtain through an individually managed portfolio.

NATIONALLY RECOGNIZED STATISTICAL RATING ORGANIZATION (NRSRO). A credit rating agency that the Securities and Exchange Commission in the United States uses for regulatory purposes. Credit rating agencies provide assessments of an investment's risk. The issuers of investments, especially debt securities, pay credit rating agencies to provide them with ratings. The three most prominent NRSROs are Fitch, S&P, and Moody's.

NEGOTIABLE CD. A short-term debt instrument that pays interest and is issued by a bank, savings or federal association, state or federal credit union, or state-licensed branch of a foreign bank. Negotiable CDs are traded in a secondary market.

PREMIUM. The difference between the par value of a bond and the cost of the bond, when the cost is above par.

PREPAYMENT SPEED. A measure of how quickly principal is repaid to investors in mortgage securities.

PREPAYMENT WINDOW. The time period over which principal repayments will be received on mortgage securities at a specified prepayment speed.

PRIMARY DEALER. A financial institution (1) that is a trading counterparty with the Federal Reserve in its execution of market operations to carry out U.S. monetary policy, and (2) that participates for statistical reporting purposes in compiling data on activity in the U.S. Government securities market.

PRUDENT PERSON (PRUDENT INVESTOR) RULE. A standard of responsibility which applies to fiduciaries. In California, the rule is stated as "Investments shall be managed with the care, skill, prudence and diligence, under the circumstances then prevailing, that a prudent person, acting in a like capacity and familiar with such matters, would use in the conduct of an enterprise of like character and with like aims to accomplish similar purposes."

REALIZED YIELD. The change in value of the portfolio due to interest received and interest earned and realized gains and losses. It does not give effect to changes in market value on securities, which have not been sold from the portfolio.

REGIONAL DEALER. A financial intermediary that buys and sells securities for the benefit of its customers without maintaining substantial inventories of securities and that is not a primary dealer.

REPURCHASE AGREEMENT. Short-term purchases of securities with a simultaneous agreement to sell the securities back at a higher price. From the seller's point of view, the same transaction is a reverse repurchase agreement.

SAFEKEEPING. A service to bank customers whereby securities are held by the bank in the customer's name.

STRUCTURED NOTE. A complex, fixed income instrument, which pays interest, based on a formula tied to other interest rates, commodities or indices. Examples include inverse floating rate notes which have coupons that increase when other interest rates are falling, and which fall when other interest rates are rising, and "dual index floaters," which pay interest based on the relationship between two other interest rates - for example, the yield on the ten-year Treasury note minus the Libor rate. Issuers of such notes lock in a reduced cost of borrowing by purchasing interest rate swap agreements.

SUPRANATIONAL. A Supranational is a multi-national organization whereby member states transcend national boundaries or interests to share in the decision making to promote economic development in the member countries.

TOTAL RATE OF RETURN. A measure of a portfolio's performance over time. It is the internal rate of return, which equates the beginning value of the portfolio with the ending value; it includes interest earnings, realized and unrealized gains, and losses in the portfolio.

U.S. TREASURY OBLIGATIONS. Securities issued by the U.S. Treasury and backed by the full faith and credit of the United States. Treasuries are considered to have no credit risk, and are the benchmark for interest rates on all other securities in the US and overseas. The Treasury issues both discounted securities and fixed coupon notes and bonds.

TREASURY BILLS. All securities issued with initial maturities of one year or less are issued as discounted instruments, and are called Treasury bills. The Treasury currently issues three- and six-month T-bills at regular weekly auctions. It also issues "cash management" bills as needed to smooth out cash flows.

TREASURY NOTES. All securities issued with initial maturities of two to ten years are called Treasury notes, and pay interest semi-annually.

TREASURY BONDS. All securities issued with initial maturities greater than ten years are called Treasury bonds. Like Treasury notes, they pay interest semi-annually.

VOLATILITY. The rate at which security prices change with changes in general economic conditions or the general level of interest rates.

YIELD TO MATURITY. The annualized internal rate of return on an investment which equates the expected cash flows from the investment to its cost.