

City of San Leandro

INVESTMENT POLICY STATEMENT



Legislative History:

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CC Res. 2000-121, 07/16/00
CC Res. 2001-214, 12/17/01
CC Res. 2003-144, 05/22/03
CC Res. 2004-116, 06/19/04
CC Res. 2005-081, 06/20/05
CC Res. 2006-063, 06/19/06
CC Res. 2007-098, 07/16/07
CC Res. 2008-083, 07/21/08
CC Res. 2009-108, 07/20/09
CC Res. 2010-072, 06/21/10
CC Res. 2011-111, 06/20/11
CC Res. 2012-093, 07/16/12
CC Res. 2013-063, 05/20/13
CC Res. 2014-048, 06/02/14
CC Res. 2015-111, 06/15/15
CC Res. 2016-080, 06/20/16
CC Res. 2017-087, 06/19/17
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CC Res. 2019-106, 06/17/19
CC Res. 2020-097, 07/20/20
CC Res. 2021-079, 05/17/21

I. Policy Statement

The City of San Leandro (City) invests public funds not required to meet current City obligations in compliance with the State of California (State) Government Code and this policy. The City's overall goal is to invest as close to 100% of these funds as possible to provide the maximum return and security while meeting the City's daily cash flow needs.

II. Policy Scope

This investment policy is applicable to all financial assets of the City of San Leandro, the Successor Agency to the Redevelopment Agency of the City of San Leandro, the City of San Leandro Parking Authority, the San Leandro Public Financing Authority, and the San Leandro Economic Development Agency. These assets are accounted for in the City's *Comprehensive Annual Financial Report* in the following funds:

- General Fund
- Special Revenue Funds
- Capital Project Funds
- Debt Service Funds
- Enterprise Funds
- Internal Service Funds
- Agency Funds

This policy applies to component units and funds subsequently established by the City.

III. Delegation of Investment Authority/Prudence

California Government Code Sections 53600 and 53646 states that the ultimate responsibility for the prudent investment of public funds rests with the governing body, or City Council. Through City Council resolution No. 94-143 the Council has delegated investment authority to the Finance Director and his/her designee. The Finance Director and his/her designee are trustees and fiduciaries that shall use the "prudent investor" standard in managing the City's portfolio. When investing, reinvesting, purchasing acquiring, exchanging, selling, or managing public funds, the 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 City, 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 City. Within the limitations of this section and considering individual investments as part of an overall strategy, investments may be acquired as authorized by law.

The City may engage the services of one or more external investment managers to assist in the management of the City's investment portfolio in a manner consistent with the City's objectives. Such managers must be registered under the Investment Advisers Act of 1940.

IV. Investment Objectives

1. *Safety*: Safety of principal is the foremost objective of the investment program. Investments shall be undertaken in a manner that seeks to ensure the preservation of capital in the overall portfolio. The objective will be to mitigate credit risk and interest rate risk.
2. *Liquidity*: The investment portfolio shall remain sufficiently liquid to meet all operating requirements that may be reasonably anticipated.
3. *Yield*: The investment portfolio shall be designed with the objective of attaining a market rate of return throughout budgetary and economic cycles, taking into account the investment risk constraints for safety and liquidity needs. Return on investment is of least importance compared to the safety and liquidity of the City's assets as described above.
4. *Other*: Investments are to be made that will bear in mind the responsibility of city government to its citizens. Alternative investments which enhance the quality of life will be given full consideration.

V. Investment Criteria

The City invests its funds in accordance with the following criteria:

1. Ensure that funds not needed for current City obligations are fully invested.
2. Ensure that yield-restricted funds are monitored to ensure compliance with federal arbitrage rebate requirements.
3. Ensure that the specific requirements outlined in the Bond Indentures of Trust are maintained.

VI. Ethics and Conflicts of Interest

Officers and employees involved in the investment process will refrain from personal business activity that would conflict with the proper execution of the investment program or would impair their ability to make impartial investment decisions. Employees and investment officials will disclose to the Finance Director any material interests in financial institutions that conduct business with the City. Furthermore, they will disclose any personal financial/investment positions that could be related to the financial performance of the City, particularly at the time of investment purchases and sales. Investment officers and employees who fail to comply with this disclosure requirement will be subject to administrative action.

VII. Authorized Financial Dealers and Institutions

The Finance Director shall maintain a list of financial institutions and depositories authorized to provide investment services. In addition, a list shall be maintained of approved security broker/dealers selected after conducting a process of due diligence. These may include "primary" dealers or regional dealers that qualify under Securities and Exchange Commission (SEC) Rule 15C3-1 (uniform net capital rule). The City's Finance Director/Treasurer will determine which financial institutions are authorized to provide investment services directly to the City. Institutions eligible to transact investment business with the City include:

1. Primary dealers and regional dealers.
 2. Nationally or state-chartered banks.
 3. The Federal Reserve Bank.
 4. Direct issuers of securities eligible for purchase.
- A. Selection of financial institutions and broker/dealers authorized to engage in transactions with the City will be at the sole discretion of the City.
 - B. All financial institutions which desire to become qualified bidders for investment transactions (and which are not dealing only with the investment adviser) must supply the Finance Director/Treasurer with a statement certifying that the institution has reviewed the California Government Code Section 53600 *et seq.* and the City's Investment Policy.
 - C. Selection of broker/dealers used by an external investment adviser retained by the City will be at the sole discretion of the investment adviser.
 - D. Public deposits will be made only in qualified public depositories as established by State law. Deposits will be insured by the Federal Deposit Insurance Corporation, or, to the extent the amount exceeds the insured maximum, will be collateralized in accordance with State law.

VIII. Authorized and Suitable Investments

All investments shall be made in accordance with California Government Code Sections 53600 *et seq.* and as described within this Investment Policy.

No investment shall be made in any security that has a remaining term to maturity in excess of five years unless City Council has granted express authority to make the investment either specifically or as part of an approved investment program.

Eligible Local Institutions must have received an overall Community Reinvestment Act (CRA) rating of at least "satisfactory" on its most recent evaluation by the appropriate federal financial agency to receive deposits from the City. This applies to banks, savings and loans, and credit unions.

The City's investment portfolio may include the following instruments:

Negotiable Certificates of Deposit (CD's) are a fixed deposit certificate that may be negotiated (traded) to a third party and is issued by a local bank or savings and loan institution. Certificates of Deposit will either be insured by the Federal Deposit Insurance Corporation (FDIC) or be fully collateralized by delivery to a third-party custodian. Securities pledged as collateral shall have a market value of at least 110% of the value of all deposits. Purchases of these instruments may not exceed 30% of the entire portfolio.

Certificate of Deposit Account Registry Service (CDARS) No more than 30% of the total portfolio may be invested in a combination of certificates of deposit including CDARS. The maturity of CDARS deposits does not exceed five years.

U.S. Government Agency Securities include a wide variety of government securities. These securities include U.S. government-sponsored enterprise obligations, such as the Federal Farm Credit Bank (FFCB), the Federal Home Loan Bank (FHLB), the Federal National Mortgage Association (FNMA), the Federal Home Loan Mortgage Corporation (FHLMC), or any other U.S. government agency. There are no portfolio limitations on the amount.

U.S. Treasury Instruments include bills, notes and bonds or certificates of indebtedness for which the full faith and credit of the United States is pledged for the payment of principal and interest. There are no portfolio limitations on the amount.

The State of California Local Agency Investment Fund (LAIF) (Government Code Section 16429.1). Local agencies may invest in LAIF, a pooled investment fund managed by the State Treasurer's Office. The City may deposit up to the maximum program limit in each City account.

Banker's Acceptances allows for 40% of the City's portfolio to be invested in Banker's Acceptances. These are known as bills of exchange or time drafts that are drawn on and accepted by a commercial bank, with maturities no longer than 180 days. No more than 30% of the entire portfolio may be invested in the banker's acceptances of a single bank. The bank must have an "A" or highest money market rating from a nationally recognized statistical-rating organization (NRSO), such as Standard & Poor's or Moody's.

Commercial Paper is a short-term, unsecured promissory note issued by financial and non-financial companies to raise short-term cash. Up to 25% of the City's portfolio may be invested in commercial paper the highest quality ranking or of the highest rating by a nationally recognized statistical-rating organization (NRSO). The issuer must be a domestic corporation having assets more than \$500 million and a minimum quality rating of A-1 from Standard and Poor's and P-1 from Moody's for its debt other than commercial paper. Maturities of individual commercial paper securities cannot exceed 270 days and the city may purchase no more than 10% of the outstanding commercial paper of any single issuer. No more than 25% of the portfolio can be invested in commercial paper.

Medium-Term Corporate Notes are corporate bonds and notes of industrial companies, banks, bank holding companies, insurance companies, thrifts, and finance companies with a maximum maturity of five years. Issuers must be corporations organized and operating in the United States or by depository institutions licensed by the United States, any state or operating within the United States. Securities issued by corporations must be rated "A" or better by an NRSO. Purchases may not exceed 30% of the City's portfolio.

Repurchase Agreements are agreements between the City and seller for the City to purchase government securities to be resold back to the seller at a specific date and for a specific amount. The legal maximum maturity on these investments is 360 days; however, repurchase agreements are generally short-term investments. Investments in Repurchase Agreements must be collateralized, with collateral limited to Treasury and Agency securities at 102% of market value of principal and accrued interest; and these investments must be supported by a master repurchase agreement with the bank or dealer. Holdings cannot exceed 20% of the City's portfolio.

Reverse Repurchase Agreements are a sale of securities by the local agency with a simultaneous agreement for the local agency to repurchase the securities on or before a specified date. Reverse purchase agreements must comply with statutory requirements and are fully collateralized by delivery to a third-party custodian. The maximum term for reverse repurchase agreements shall be 92 days. The proceeds of reverse repurchase transactions must be invested in securities having maturities shorter than or equal to the term of the underlying agreement. Reverse repurchase agreements cannot exceed 20% of the City's portfolio.

Passbook Savings Accounts or **Time Certificates of Deposit** are fixed term, non-negotiable investments which are required to be collateralized 110% by eligible pooled U.S. Government Securities. Promissory notes secured by first mortgages or trust deeds used as collateral require a market value of at least 150% of the amount deposited. There are no portfolio limits.

Money Market Mutual Funds consisting of investment securities permitted under Sections 53601 and 53635 of the California Government Code. To be eligible for City investments, companies providing mutual funds shall have either or both of the following:

1. The highest rating provided by not less than two of the three largest nationally recognized statistical-rating services (NRSO).
2. An investment advisor registered with the Securities and Exchange Commission for not less than five years having investment experience in the underlying securities and with assets under management in excess of \$500 million.

Holdings cannot exceed 20% of the City's portfolio.

Other Investment Pools – The City will conduct a thorough investigation of investment pools prior to making an investment. To become eligible, an investment pool will provide the following information to the City:

- A description of eligible securities and a written statement of investment policy and objectives.
- A description of interest calculation methods, how interest is distributed, and how gains and losses are treated.
- A description of safekeeping procedures and settlement processes, how often securities are priced, and how often the program is audited.
- A description of who are eligible to invest in the program and how often, and any limitations on deposits and/or withdrawals.
- A schedule for receiving statements and portfolio listings.
- Any policies regarding the use of reserves or retained earnings by the pool.
- A fee schedule and a description of how and when fees are assessed.
- Any policies regarding the pool's eligibility for bond proceeds if applicable.

Securities Issued by the City of San Leandro and its Agencies. The City may elect to sell or purchase its securities through secondary markets when conditions are favorable.

Asset-Backed, Mortgage-Backed, Mortgage Pass-Through Securities, and Collateralized Mortgage Obligations, provided that:

- The securities are rated "AA" or higher by a NRSO.
- No more than 20% of the total portfolio may be invested in these securities.
- No more than 5% of the portfolio may be invested in any single Asset-Backed or Commercial Mortgage security issuer. There is no issuer limitation on any Mortgage security where the issuer is the US Treasury or a Federal Agency/Government-sponsored Enterprise (GSE).
- The maximum legal final maturity does not exceed five (5) years.

Supranational Securities, provided that:

- Issues are unsubordinated obligations issued by the International Bank for Reconstruction and Development (IBRD), International Finance Corporation (IFC), or Inter-American Development Bank (IADB).
- The securities are rated "AA" or higher by a national recognized statistical rating organization.
- No more than 30% of the total portfolio may be invested in these securities.
- No more than 10% of the portfolio per issuer.
- The maximum maturity does not exceed 5 years.

See Appendix A *City of San Leandro Summary of Eligible Investments* on pages 9, 10 and 11 for a tabular listing of the restrictions regarding authorized investments.

IX. Socially Responsible Investing

The investment policy prohibits investing in an entity that receives a significant portion of their revenues from the gun manufacturing, fossil fuel production, private prisons and tobacco producers.

X. Competitive Transactions

All investment transactions shall be conducted on a competitive basis with quotes from a minimum of three brokers or financial institutions when possible.

XI. Safekeeping

Purchased securities are held in third party safekeeping by the trust department of the City's bank or other designated third party in the City's name and control. All security transactions entered into by the City will be conducted on a delivery-versus-payment (DVP) basis and evidenced by a receipt issued by the safekeeping agent.

XII. Collateralization

An independent third party with whom the City of San Leandro has a current custodial agreement will always hold collateral. A clearly marked evidence of ownership must be supplied to the City.

XIII. Internal Control and Review

The Finance Director will establish an annual review process to ensure compliance with the established Investment Policy and routine reporting requirements.

XIV. Performance Standards

The investment portfolio shall be designed with the overall objective of obtaining a total rate of return throughout economic cycles, commensurate with investment risk constraints and cash flow needs.

The investment performance objective for the portfolio shall be to earn a total rate of return over a market cycle which is approximately equal to the return on a Market Benchmark Index of similar risk characteristics as that of the City's investment portfolio.

Other market investments that may be used as yield comparisons include:

- The State of California Local Agency Investment Fund (LAIF)
- The two-year U.S. Treasury Bill
- The five-year U.S. Treasury Note

XV. Reporting

This policy will be reviewed annually with the City Council to ensure compliance with the objectives of safety, liquidity and yield and adherence with applicable laws. The City Council Finance Committee will review and approve all changes to this policy statement prior to submittal to the full City Council for approval.

California Government Code Section 53646 states that the Finance Director may render a quarterly report on the status of the City's investment portfolio to the City Manager and the City Council within 30 days after the end of the calendar quarter. The report will provide detailed information regarding the type of investments, the amount invested with various institutions, purchase and maturity dates, and interest yield on all investments. The report shall state if the City's investments are in compliance with this policy and if the City will be able to meet its cash obligations during the next six-month period. The Finance Director

will submit a monthly transactions report on the portfolio's activity to the City Manager and City Council consistent with the requirements of the State Code.

XVI. Prohibited Investment Vehicles and Practices

- State law notwithstanding, any investments not specifically described herein are prohibited, including, but not limited to futures and options.
- In accordance with Government Code, Section 53601.6, investment in inverse floaters, range notes, or mortgage derived interest-only strips is prohibited.
- Investment in any security that could result in a zero interest accrual if held to maturity is prohibited. Under a provision sunseting 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.
- Trading securities for the sole purpose of speculating on the future direction of interest rates is prohibited.
- Purchasing or selling securities on margin is prohibited.
- The use of reverse repurchase agreements, securities lending or any other form of borrowing or leverage is prohibited.
- The purchase of foreign currency denominated securities is prohibited.
- Agencies that are not Qualified Institutional Buyers (QIB) as defined by the Securities and Exchange Commission are prohibited from purchasing Private Placement Securities. The SEC defines a QIB as having at least \$100,000,000 in securities owned and invested.

Appendix A
City of San Leandro
Summary of Eligible Investments

Investment Type	Maximum Maturity	Maximum Amount	Other Requirements
Negotiated Certificates of Deposit (CDs) and CDARs	5 Years	30 % of Portfolio	CDs require Market Value of Collateral at Least 110% of Deposit if not FDIC insured; CDARs are FDIC insured
U.S. Government Agency Securities	5 Years, Longer Maturities if Approved by Council	None	None
U.S. Treasury Securities	5 Years, Longer Maturities if Approved by Council	None	None
State Local Agency Investment Fund (LAIF)	N/A	Maximum Program Limits	None
Bankers Acceptances	180 Days	30% per Issuer 40% of Portfolio	Minimum Rating of "A" from Moody's or S&P
Commercial Paper	270 Days	10% of Issuer's Paper 25% of Portfolio	Prime Quality Rating of "A-1" and "P-1" from S&P and Moody's Respectively
Medium Term Corporate Notes	5 Years	30% of Portfolio	Minimum Rating of "A" from Moody's or S&P

Appendix A (continued)

City of San Leandro
Summary of Eligible Investments

Investment Type	Maximum Maturity	Maximum Amount	Other Requirements
Repurchase Agreements	1 Year	20% of Portfolio	Master Agreement & Fully Collateralized
Reverse Repurchase Agreements	92 Days	20% of Portfolio	Proceeds Must be Invested in Securities Having Maturities Shorter Than or Equal to Term of Underlying Agreement
Passbook Accounts	5 Years	None	Minimum of 110% Collateral if Secured by U.S. Government Securities, 150% if Secured by Mortgage or Trust Deed
Money Market Mutual Funds	N/A	20% of Portfolio	Highest Rating from at Least Two Rating Agencies and/or Advisor with 5 Years of Experience Managing Assets in Excess of \$500 Million
Other Investment Pools	N/A	N/A	Must Provide Comprehensive Information Prior to City Investment
City Issued Securities	N/A	N/A	Usually Purchased When Originally Issued

Appendix A (continued)

City of San Leandro
Summary of Eligible Investments

Investment Type	Maximum Maturity	Maximum Amount	Other Requirements
Asset-Backed, Mortgage-Backed, Mortgage Pass-Through Securities, Collateralized Mortgage Obligations	5 Years	20% of portfolio	Securities rated "AA" or higher by one Nationally Recognized Statistical-rating Organization (NRSO) No limitation on mortgage securities when issuer is US Treasury or Agency
Supranational Securities	5 Years	30% of portfolio 10% per issuer	Permitted issuers are International Bank for Reconstruction and Development (IBRD), International Finance Corporation (IFC), and Inter-American Development Bank (IADB)

Appendix B 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 and are payable upon order to the bearer or initial depositor (investor).

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.