

MONTANA BOARD OF INVESTMENTS
INVESTMENT POLICY STATEMENT
TREASURE STATE ENDOWMENT REGIONAL WATER SYSTEM FUNDS
(FUNDS 09046 & 09047)
APRIL 2015

INTRODUCTION

The purpose of an investment policy statement is to give the investment manager guidance in developing an investment program to achieve the objectives agreed upon and enable the sponsor, Department of Revenue, to monitor the progress of the plan.

OBJECTIVES

Return Requirement: To maximize the total rate of return through a broadly diversified portfolio of fixed income assets while exceeding the Salomon Broad Investment-Grade Bond Index and/or the Lehman Aggregate Bond Index over a five-year moving average.

Current income is important since the Legislature is transferring 100 percent of income earned to the treasure state water special revenue account to fund water projects.

Risk Tolerance: This fund is being managed as a long-term, permanent fund; therefore, the fund has an above average ability to assume risk. The ability to tolerate volatility in value of the portfolio is larger than the ability to tolerate volatility in total spendable return.

CONSTRAINTS

Liquidity: As a long-term constitutional trust fund, liquidity needs are low, except for investment purposes. There is no need to maintain any sizeable short-term holdings.

Time Horizon: The fund is considered a permanent long-term fund that has a time horizon well beyond normal market cycles.

Tax Considerations: This fund is tax-exempt; therefore, tax advantage investments will not be used.

Legal Considerations: This fund is governed by state regulations, specifically, the "prudent expert principle" which requires the Board of Investments to: (a) discharge the duties with the care, skill, prudence, and diligence, under the circumstances then prevailing, that a prudent person acting in a like capacity with the same resources and familiar with like manners exercises in the conduct of an enterprise of a like character with like aims; (b) diversify the holdings of each fund within the unified investment program to minimize the risk of loss and to maximize the rate of return unless, under the circumstances, it is clearly prudent not to do so; and (c) discharge the duties solely in the interest of and for the benefit of the funds forming the unified investment program.

The Montana Constitution does not allow equity type investments in non-retirement funds.

Cash Investments

Cash investments held at the pool level, any managed account within it, or any separate account entail an element of credit risk. Thus, only approved cash investment vehicles are permitted. These include the custodian's STIF vehicle, STIP, or any SEC-registered money market fund, all of which specifically address credit risk in their respective investment guidelines.

Unique Circumstance: None.

Client Preference: None

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BACKGROUND INFORMATION

MCA 17-5-703

Coal severance tax trust funds. This sub fund of the Permanent Trust (Trust) was created during the 1999 Special Session. As a sub fund of the Trust, it is afforded the same constitutional protection as is principal in the Trust. The Montana constitution states, "The principal of the trust shall forever remain inviolate unless appropriated by vote of three-fourths of the members of each house of the legislature".

Beginning July 1, 1999 and ending June 30, 2016, it will receive 25 percent of the coal severance taxes constitutionally earmarked for the Trust.

The state treasurer shall monthly transfer from the treasure state endowment regional water system fund to the treasurer state endowment regional water system special revenue account the amount of earnings, excluding unrealized gains and losses, required to meet the obligations of the state that are payable from the account for regional water systems under 90-6-715. Earnings not transferred to the treasure state endowment regional water system special revenue account must be retained in the treasure state endowment regional water system fund.

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CASH FLOW SUMMARY
(in millions)

<u>Fiscal Year</u>	<u>Additions to Fund</u>	<u>Book</u>	<u>Market</u>	<u>Total Inv. Income</u>	<u>Income Return</u>
2000	\$3.4	\$3.4	\$3.4	0.032	--
2001	3.6	7.0	7.1	0.370	7.05%
2002	3.9	10.9	11.1	0.643	7.18
2003	4.1	15.0	16.0	0.894	6.91
3/31/2004	2.4	17.4	18.3		

ASSET ALLOCATION
(at market)

<u>FIXED INCOME</u>	<u>6-02</u>	<u>6-03</u>	<u>3-04</u>	<u>Ranges</u>
Trust Funds Bond Pool (TFBP)	94.6%	99.7%	99.5%	75-100%
Montana Investments	0.0	0.0	0.0	0-25
Short-Term Investment Pool (STIP)	<u>5.4</u>	<u>0.3</u>	<u>0.5</u>	<u>0-5</u>
Total Fixed Income	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>