STATE OF MONTANA BOARD OF INVESTMENTS
SHORT TERM INVESTMENT POOL FINANCIAL STATEMENTS
STATEMENT OF NET ASSET VALUE JUNE 30, 2016 AND 2015
(in thousands)

Assets		2016		2015
Investments (FY16 at fair value / FY15 at amortized cost) (Notes 2, and 4)	$	2,823,099	$	2,538,469
Security lending cash collateral (Notes 3 and 4)		11,844		5,806
Security lending income receivable		10		1
Interest receivable (Note 4)	$	1,894	$	1,353
Total assets	$	2,836,847	$	2,545,629
Liabilities				
Income due participants	$	1,298	$	409
Security lending obligations		11,844		5,806
Security lending expense payable		5		-
STIP reserve (Note 6)	$	13,143	$	28,591
Total liabilities	$	26,290	$	34,806
Net asset value	$	2,810,557	$	2,510,823
Units Outstanding		2,809,975		2,510,823
Unit Value (not in thousands)		1.000207		1.000000

STATEMENT OF CHANGES IN NET ASSET VALUE
FOR THE FISCAL YEARS ENDED JUNE 30, 2016 AND 2015
(in thousands)

Net asset value, beginning of year	$	2,510,823	$	2,511,512
Value of units purchased by participants		6,910,236		6,616,770
Value of units sold by participants		(6,611,084)		(6,617,459)
Changes in current value of investments managed	$	582	$	-
Net asset value, end of year	$	2,810,557	$	2,510,823

STATEMENT OF INVESTMENT INCOME AND DISTRIBUTION
FOR THE FISCAL YEARS ENDED JUNE 30, 2016 AND 2015
(in thousands)

Interest income	$	11,270	$	6,132
Amortization/accretion		3,048		1,615
Security lending income		48		10
Other income (Note 6 and 7)		5,209		394
Security lending expense		(18)		(1)
Administrative expenses		(897)		(770)
STIP reserve expense (Note 6)		(8,137)		(4,151)
Income due participants, beginning of year	$	409	$	245
Income available for distribution		10,932		3,474
Distribution	$	(9,634)	$	(3,065)
Income due participants, end of year	$	1,298	$	409

The accompanying notes are an integral part of these financial statements.

JUNE 30, 2016 AND 2015

1. HISTORY AND ORGANIZATION

The Legislature created the Board to invest and manage Montana's Unified Investment Program. The Board created the Short Term Investment Pool (STIP) to allow qualifying funds, per sections 17-6-201, 202, and 204, MCA, to participate in a diversified pool. Although state agencies with accounts that retain their interest earnings are legally required to invest in STIP, local governments may voluntarily participate in the STIP.

The Board manages the STIP to preserve principal while providing 24-hour liquidity for state agency and local government participants. Funds may be invested in the STIP for one or more days. The STIP investments and the income are owned by the participants and are managed on their behalf by the Board.

For the fiscal year ending June 30, 2016, STIP is presented in the Statement of Net Asset Value at fair value. For the fiscal year ending June 30, 2015, STIP is presented in the Statement of Net Asset Value at "book" or amortized cost.

The STIP financial statements are included in the Board's Consolidated Unified Investment Program financial statements, which are audited by the Montana Legislative Auditor. These stand-alone STIP financial statements are for informational purposes only and are not separately audited. The Board's audited annual financial information is available from the Board at 2401 Colonial Drive 3rd Floor, PO Box 200126, Helena, MT 59620-0126 or by calling 406-444-0001. The Board's information can also be found on the Board's website at www.investmentmt.com.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Investments

The STIP investments are managed in accordance with the statutorily mandated "Prudent Expert Principle".

The portfolio may include asset-backed securities, commercial paper, corporate, U.S. Government direct obligations, U.S. Government agency securities, repurchase agreements, institutional government money market funds, certificates of deposit, and variable-rate (floating-rate) instruments. Investments must have a maximum maturity of 397 days or less unless they are a variable rate security.

Asset-backed securities represent debt securities collateralized by a pool of mortgage and non-mortgage assets such as trade and loan receivables, equipment leases, credit cards, etc. Commercial paper is unsecured short-term debt with maturities ranging from 2 to 270 days. U.S. Government direct obligations include U.S. Treasury securities and debt explicitly guaranteed by the U.S. Government. U.S. Government agency securities include U.S. Government agency. Repurchase agreements (REPOs) represent an agreement between a seller and a buyer, usually of U.S. Government securities, whereby the seller agrees to repurchase the securities at an agreed upon price and stated time. Variable rate securities pay a variable rate of interest until maturity. The STIP portfolio's variable rate securities reset to LIBOR (London Interbank Offered Rate).

Pool Net Asset Value/Investments Managed

The NAV must include the fair value of the investment portfolio (except for STIP at book value for the June 30, 2015 fiscal year) and any liabilities payable by the Pool and receivables due the Pool on the NAV calculation date. Investment accounting uses the "accrual" basis, which means bond interest due is recorded when earned, rather than when cash is received. Interest "due" is recorded as a receivable (asset) and included in the NAV on the date of the calculation. Income due to Pool participants is recorded on the date due to the participants, rather than on actual distribution date. Income Due Participants is a payable (liability) and included in the NAV on the calculation date. The difference between Pool investment portfolios at fair value and the NAV is the net of other assets and liabilities.

For the period ended June 30, 2016, the STIP portfolio is shown in the Statement of Net Asset Value at fair value. For the period ended June 30, 2015, the STIP portfolio is shown in the Statement of Net Asset Value at amortized cost or "book" value.

Participant Units / Valuation

The STIP unit value is fixed at $1.00 for both participant buys and sells. A purchased unit earns income on the purchase date and ceases to earn income on the day before the unit is sold. Participants may buy or sell fractional shares. For fiscal years 2016 and 2015, income was distributed on the first business day of each month. Participants may automatically reinvest their income in additional units. STIP is managed to closely align fair value with amortized cost.

Broker Receivable/Payable

The STIP security transactions are recorded as of the trade date rather than the settlement date. This results in a purchased security included in the investment portfolio on the trade date even though payment will not occur until the settlement date. Conversely, a sold security will be eliminated from the investment portfolio on the trade date even though the sale proceeds will not be received until the settlement date. "Receivables" and "payables" for securities sold/purchased but not yet settled are reported in the financial statement and calculated in the Net Asset Value.

Other

Administrative expenses incurred by the Board are charged daily to STIP based on the Board's expenses applicable to STIP.

3. SECURITIES LENDING

The Board is authorized by law to lend its securities and has contracted with the custodial bank, State Street Bank and Trust, "the Bank", to lend the Board's securities to broker-dealers and other entities with a simultaneous agreement to return the collateral for the same securities in the future. The Bank is required to maintain collateral equal to 102 percent of the fair value of domestic securities and 105 percent of the fair value of international securities while the securities are on loan. On any day, including June 30th, the markets may move in a positive or negative direction resulting in under or over collateralization. The Bank compensates for market movement by recalculating on the following business day to meet the collateralization requirements. The Board and the Bank split the earnings, 80/20% respectively, on security lending activities. The Board retains all rights and risks of ownership during the loan period.

During fiscal years 2016 and 2015, the Bank lent Board public securities and received as collateral: U.S. dollar cash; U.S. Government and government sponsored agency securities; U.S. corporate debt securities and structured securities rated AA-/Aa3 or higher; sovereign debt securities of the G10 nations; and debt securities issued by certain supranational agencies. The Bank does not have the ability to sell collateral securities unless the borrower defaults.

The Board imposed no restrictions on the amount of securities available to lend during fiscal years 2016 and 2015. There were no failures by any borrowers to return loaned securities or pay distributions thereon during the period that resulted in a declaration and notice of Default of the Borrower. There were no losses during fiscal years 2016 and 2015 resulting from a borrower default.

During fiscal years 2016 and 2015, the Board and the borrowers maintained the right to terminate all securities lending transactions on notice. Security lending collateral is invested in one of two investment funds, the Quality D Short Term Investment Fund or the Security Lending Quality Lending Trust Fund. Each fund is comprised of a liquidity pool. STIP is only invested in the Securities Lending Quality Trust Fund. In March 2015, the Board sold all of the holding within the duration pool, which resulted in a loss of $26 thousand. Security lending income offset the entire amount of the loss within the investment fund. Because the securities lending transactions were terminable at will, their duration did not generally match the duration of the investments made with the cash collateral received from the borrower. At year-end 2016 and 2015, State Street Bank indemnified the Board's credit risk exposure to borrowers. The average duration and average weighted final maturity for each investment fund is as follows:

	Quality D ST Investment Fund		Security Lending Quality Trust	
Liquidity Pool	FY16	FY15	FY16	FY15
Average Duration	43 days	28 days	32 days	30 days
Average Weighted Final Maturity	83 days	109 days	92 days	115 days

As of June 30, 2016, the fair value of the underlying securities on loan, categorized as corporate debt for the Short Term Investment Pool was $12.6 million. The collateral provided for the securities on loan totaled $11.8 million in cash and $1.0 million in securities. As of June 30, 2015, the fair value of the underlying securities on loan, categorized as corporate debt for the Short Term Investment Pool was $5.7 million. The collateral provided for the securities on loan totaled $5.8 million in cash. For June 30, 2016, the security lending gross income was $48 thousand with expenses of $18 thousand for net income of $29 thousand. For June 30, 2015, the security lending gross and net income was $10 thousand, with expenses of $1 thousand for net income of $9 thousand.

4. INVESTMENT RISK DISCLOSURES

Deposit and Investment Risk Disclosures

In the following paragraphs described below are the investment risk disclosures.

Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligation. With the exception of the U.S. Government securities, the STIP securities have credit risk as measured by major credit rating services. This risk is that the issuer of a STIP security may default in making timely principal and interest payments. The Board's policy specifies that STIP securities have a minimum of two separate credit ratings as provided by Standard and Poor's, Moody's, or Fitch that meet the minimum as stated in the STIP investment policy depending on the type of investment.

The U.S. Government guarantees the U.S. Government securities directly or indirectly. Obligations of the U.S. Government or obligations explicitly guaranteed by the U.S. Government are not considered to have credit risk and do not require disclosure of credit quality per GASB Statement No. 40. The S&P rating service provide the credit ratings presented in the following tables. If an S&P rating is not available, a Moody's rating has been used.

Custodial Credit Risk

Investments-Custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, the Board will not be able to recover the value of the investment or collateral securities that are in the possession of an outside party. Per policy, the Board's custodial institution must hold short-term and long-term credit rating by at least one Nationally Recognized Statistical Rating Organization with a minimum requirement of A1/P1 (short term) and A3/A-1 (long-term).

As of June 30, 2016 and 2015, all the public securities as well as securities held by the separate public equity account managers were registered in the nominee name for the Montana Board of Investments and held in the possession of the Board's custodial bank, State Street Bank. The Equity Index funds, US Bank repurchase agreement, real estate, mortgage and loan investments were purchased and recorded in the Board's name. Commingled fund investments are registered in the name of the Montana Board of Investments.

Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the magnitude of the Board's investment in a single issuer. Investments explicitly guaranteed by the U.S. Government are excluded from the concentration of credit risk requirement. The U.S. government extended the explicit guarantee to certain government agencies such as Federal National Mortgage Association (Fannie Mae) and Federal Home Loan Mortgage Corporation (FHLMC-Freddie Mac). Given the explicit guarantee extension, the Board had no concentration of credit risk exposure to Fannie Mae and Freddie Mac in STIP.

The STIP Investment Policy limits concentration of credit risk exposure by limiting portfolio investment types to 3% in any issuer with the exception of US Treasury and US Agency securities as well as any repurchase agreements with a financial institution. Concentration risk was within the policy as set by the Board.

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. According to the STIP investment policy "the STIP portfolio will minimize interest rate risk by:

1) structuring the investment portfolio so securities mature to meet cash requirements for ongoing operations thereby normally avoiding the need to sell securities on the open market prior to maturity;
2) maintaining a dollar-weighted average portfolio maturity (WAM) of 60 days or less (for this purpose, the date to the next coupon reset date will be used for all floating or variable rate securities); and
3) STIP will maintain a reserve account.

Asset-backed securities are based on cash flows from principal and interest payments emanating from a Trust containing a pool of underlying auto loan receivables, credit card receivables, and other receivables. These securities, while sensitive to prepayments due to interest rate changes, generally have less credit risk than unsecured bonds. Their credit risk is based on the structure itself rather than balance sheet risk. This includes such factors as default rates, overcollateralization, and quality of collateral. STIP held certain variable rate issues where the interest payments on these securities are based on an underlying reference rate, e.g., LIBOR.

STIP investments are categorized as follows to disclose credit rate risk and weighted average maturity (WAM) as of June 30, 2016 and June 30, 2015. Credit risk reflects the weighted security quality rating by investment type as of the June 30 report date. If a security investment type is unrated, the quality type is indicated by NR (not rated). Although the STIP investments have been rated by investment security type, STIP, as an external investment pool, has not been rated. The short-term credit ratings, provided by S&P's rating services, are presented in the table below. An A1+ rating is the highest short-term rating by the S&P rating service. STIP interest rate risk is determined using the WAM method. The WAM measure expresses investment time horizons – the time when investments are due or reset and payable in days, months, or years – weighted to reflect the dollar size of the individual investments within an investment type. Shown on the next page is the WAM, calculated in days, for the STIP portfolio.

STIP Credit Quality Ratings and Weighted Average Maturity as of June 30, 2016
(in thousands)

Security Investment Type		Fair Value *	Credit Quality Rating**	WAM in Days
Treasuries	$	75,122	A-1+	133
Asset Backed Commercial Paper		786,486	A-1	22
Corporate Commercial Paper		262,021	A-1	82
Corporate Variable Rate		467,046	A-1	45
Certificates of Deposit Fixed Rate		25,004	A-1	15
Certificates of Deposit Variable Rate		500,023	A-1	47
U.S. Government Agency Fixed		241,350	A-1+	75
U.S. Government Agency Variable Rate		263,901	A-1+	16
Money Market Funds (Unrated)		13,143	NR	1
Money Market Funds (Rated)		189,003	A-1+	1
Total Investments	$	2,823,099	A-1	41
Securities Lending Collateral Investment Pool	$	11,844	NR	32

*Beginning with the period of June 30, 2016, the STIP portfolio is shown at fair value. For the period prior to June 30, 2016, the STIP portfolio was shown at amortized cost.

**Credit Quality Rating is weighted.

STIP Credit Quality Ratings and Weighted Average Maturity as of June 30, 2015
(in thousands)

Security Investment Type		Amortized Cost	Credit Quality Rating*	WAM in Days
Asset Backed Commercial Paper	$	779,579	A-1	25
Corporate Commercial Paper		101,299	A-1	102
Corporate Variable Rate		571,672	A-1+	42
Certificates of Deposit Fixed Rate		150,000	A-1	259
Certificates of Deposit Variable Rate		450,000	A-1+	47
Other Asset Backed		27,821	NR	NA
U.S. Government Agency Fixed		54,498	A-1+	236
U.S. Government Agency Variable Rate		239,008	A-1+	24
Money Market Funds (Unrated)		161,592	NR	1
Money Market Funds (Rated)		3,000	A-1+	1
Total Investments	$	2,538,469	A-1	52
Securities Lending Collateral Investment Pool	$	5,806	NR	30

*Credit Quality Rating is weighted.

Legal and Credit Risk

In January 2007, the Board purchased a $25 million par issue of Orion Finance USA. In April 2007, the Board purchased two issues of Axon Financial Funding totaling $90 million par and another $25 million par issue of Orion Finance USA. As of June 30, 2007, these Structured Investment Vehicle (SIV) securities held in the STIP portfolio carried a combined amortized cost of $140 million representing 5.02% of the total portfolio. At the time of purchase and as of June 30, 2007, these four issues received the highest investment grade rating of AAA by Standard & Poor's and Aaa by Moody's. Since June 30, 2008 and through June 30, 2010, these issues carried a D rating by Standard & Poor's. On November 20, 2007, an insolvency event was declared by Axon Financial Funding. Orion Finance USA declared an insolvency event on January 14, 2008. On the January and April 2008 maturity dates, these securities matured at their amortized cost of $140 million.

The Board had determined it was in the best interest of the STIP to hold these securities in the investment portfolio. In May 2016, the Board wrote-off the entire outstanding SIV balance of $23.6 million against the STIP reserve. Any further flows of either principle or interest will be deemed as recovery monies and be applied to the STIP reserve. From May 31, 2016 until June 30, 2016, $4.4 million was recorded as recovery monies and applied to the STIP reserve. Refer to Note 6 – STIP Reserve for additional detail.

Axon Financial Funding payments total $27.5 million from November 2008 to October 2011. On July 6, 2010, Axon Financial Funding foreclosed with the issuance of a promissory note for $66.8 million from AFF Financing LLC with a July 5, 2011 maturity date. The Board, with the majority of other holders, elected on June 3, 2015 to extend the AFF Financing LLC promissory note maturity date to July 2, 2016. Similar one-year extensions have been granted since 2011. In June and December 2009, the Board applied $13.5 million, in total, from the STIP reserve to the outstanding principal for the Axon Financial Funding securities. Fiscal year 2016 payments thru May 30, 2016 from AFF Financing LLC totaled $3.2 million consisting of $3.1 million in principle and $71 thousand in interest. Fiscal year 2015 payments from AFF Financing LLC totaled $8.2 million consisting of $8.2 million in principal and $52 thousand in interest. As of June 30, 2016 and 2015, the AFF Financing LLC, classified as an Other Asset -Backed security, had outstanding amortized cost balances, respectively, of $0.000 million and $14.7 million. Refer to Note 7 – Subsequent Events for additional information.

On October 14, 2009, the Board received its initial payment from Orion Finance USA. From this date through November 2010, payments from Orion Finance USA included principal of $13.4 million and interest compensation of $1.8 million in excess of the $904 thousand accrued interest receivable for a total of $16.1 million. In November 2010, Orion Finance Corporation "granted a security interest in substantially all of its assets (the Collateral) to the Bank of New York Mellon, as Security Trustee". On December 8, 2010, the Security Trustee conducted "a public sale of 60 structured credit and 7 financial securities including but not limited to asset backed securities, collateralized debt obligations, collateralized loan obligations and residential mortgage backed securities included within the Collateral". The Board participated in the sale and collectively holds these individual securities as Orion Finance. In June and December 2009, the Board applied $7.5 million, in total; from the STIP reserve to the outstanding principal for the Orion Finance USA securities. From December 2010 through May 31, 2016, the Board received principal and interest payments of $17.0 million and $2.91 million, respectively. As of June 30, 2016 and 2015, the Orion Finance collective holding, classified as Other Asset- Backed, had outstanding amortized cost balances, respectively, of $0.000 million and $13.2 million. Refer to Note 7 – Subsequent Events for additional information.

As of June 30, 2016 and 2015, the Federal National Mortgage Association and Federal Home Loan Mortgage Corp. remain in conservatorship from September 7, 2008.

In August 2011, S&P downgraded the U.S. AAA bond rating to AA+.

5. FAIR VALUE MEASUREMENTS

The Board categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles as follows:

- Level 1—Quoted prices for identical assets or liabilities in active markets.
- Level 2—Prices determined using inputs, other than quoted prices included within Level 1, that are observable for an asset or liability, either directly or indirectly.
- Level 3—Prices determined using unobservable inputs.

STIP has the following recurring fair value measurements as of June 30, 2016:

STIP Investments Measured at Fair Value
(in thousands)

		Fair Value Measurements Using		
	June 30, 2016	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable (Level 3)
Investments by fair value level				
Treasuries	$ 75,122	$ 75,122		
Asset Backed Commercial Paper	786,486		$ 786,486	
Corporate Commercial Paper	262,021		262,021	
Corporate Variable Rate	467,046		467,046	
Certificates of Deposit Fixed Rate	25,004		25,004	
Certificates of Deposit Variable Rate	500,023		500,023	
U.S. Government Agency Fixed	241,350		241,350	
U.S. Government Agency Variable Rate	263,901		263,901	
Money Market Funds (Unrated)	13,143		13,143	
Money Market Funds (Rated)	$ 189,003		$ 189,003	
Total Investments by fair value level	$ 2,823,099	$ 75,122	$ 2,747,977	$ -

Fixed income investments classified in Level 1 of the fair value hierarchy are valued using prices quoted in active markets for those securities. Fixed income investments classified in Level 2 of the fair value hierarchy are valued using a matrix pricing technique. Matrix pricing is used to value securities based on the securities' relationship to benchmark quoted prices.

For the fiscal year ended June 30, 2015, STIP investments were recorded at amortized cost. Therefore, a fair value table is not presented.

6. STIP RESERVE

In November 2007, the STIP Reserve account was established. The STIP reserve account may be used to offset losses within the STIP portfolio. STIP distributes income to STIP participants based on accrued interest and discount amortization, net of fees and STIP reserve expense. The STIP reserve expense is detailed as follows:

STIP Reserve Expense (in thousands)	2016	2015
Other income		
Accrued interest received on SIV related assets (7/1/2015 - 5/31/2016)	$ 535	$ 260
Recovery from sale of SIV related assets	4,097	-
Recovery from SIV related assets (6/01/2016 - 6/30/2016)	320	-
Realized gains on sale of any STIP asset	257	134
Daily reserve accrual	2,928	3,757
Total reserve expense	$ 8,137	$ 4,151
SIV Write off	$ (23,585)	$ -
Change in STIP reserve	$ (15,448)	$ 4,151

In May 2016, the Board wrote-off the entire outstanding SIV balance of $23.6 million against the STIP reserve. Any further flows of either principle or interest will be deemed as recovery monies and be applied to the STIP reserve. Refer to Note 4 – Legal and Credit Risk Section and Note 7 – Subsequent Events for additional detail.

The STIP Reserve balance was $13.1 million and $28.6 million as of June 30, 2016 and June 30, 2015, respectively.

7. SUBSEQUENT EVENTS

From July 1 through October 17, 2016, AFF Financing LLC recovery payments total $1.5 thousand, representing $1.5 thousand in principal and $40 thousand in interest. For the same period, the Board received recovery payments associated with the Orion Finance collective holding of $489 thousand with $460 thousand and $29 thousand applied to principal and interest, respectively. Both the principal and interest was treated as recovery money and applied to the reserve. Please see the STIP Legal and Credit Risk section of Note 4 for further information on AFF and Orion.

As of November 2016, STIP will no longer participate in the Security Lending program.

8. POOL RESTRUCTURE

On October 6, 2015, the Board based on staff recommendations approved that for financial reporting purposes the STIP portfolio be reported on a NAV or “fair value” basis beginning with the fiscal year ended June 30, 2016. Prior to this change, the STIP portfolio was reported on a “book” or amortized cost basis within the financial statements.