

CITY of CAMPBELL
Finance Department

**Notice of Meeting
Finance Sub-Committee**

Date: July 23, 2019
Time: 2:00 p.m.
Location: Campbell City Hall
Doetsch Conference Room
70 North First Street, Campbell CA 95008

AGENDA

- I. Call to Order
- II. Review of Investment Policy and Investment Strategy
- III. Oral Requests
- IV. Adjourn

MEMORANDUM



City of Campbell

Finance Department

To: Finance Sub-Committee

Date: July 23, 2019

From: Will Fuentes, Finance Director

Subject: Annual Investment Policy and Investment Strategy Update

A Finance Sub-Committee Meeting has been scheduled for Tuesday, July 23rd at 2:00 pm in the Doetsch Conference Room to discuss the annual review of the investment policy update.

California Government Code requires that the City Council review the City's investment policy annually. Our investment policy requires the Finance Sub-Committee to review any proposed changes and make recommendation to the Council accordingly. It also requires the Sub-Committee to review the Investment Strategy annually as well and share a summary of that strategy with Council.

The Investment Policy is updated annually to conform to California Government Code Section 53600 et. seq. Any statutory revisions made during the previous calendar year that impact the City policy are incorporated as necessary. In addition to statutory revisions, staff is presenting several minor revisions below that were recommended by an external investment advisor after an informal review. All changes are shown in an attached redline file:

- Page 4 – Changed “prudent person” to “prudent investor” to be consistent with current terminology for public investment officials.
- Page 5 – Clarified that percentage holding limits only apply at the time the security is purchased and are not recalculated upon periodic changes in market value, which would be operationally cumbersome.
- Page 7 and 11, To align with California investment code and to allow more investment flexibility, the percentage holding limit for Medium Terms notes was changed from 10% to 30%.
- Page 8, 12, 13, and 14 - To align with California investment code and to allow more investment flexibility, Asset-Backed, Mortgage-Backed, Mortgage Pass-Through Securities, Collateralized Mortgage Obligations and Supernationals were added to the list of eligible investments. These may be utilized infrequently by the city, but it gives staff another allowable investment tool to increase return if needed.
- Page 11 – Clarified process to divest in securities that are downgraded below credit rating limits.

In addition to these minor revisions, staff is also proposing one substantive revision for the Finance Subcommittee's consideration:

- Page 3, 4, 9 - The Investment Policy for FY 2018-19 and prior was inconsistent in regards to reporting, with Section IV (C) calling for monthly reporting to Council and Section VII (A) calling for quarterly reporting to Council. To make consistent throughout the Investment Policy and to mirror best practice in other agencies, staff recommends changing reporting to quarterly. This would also allow staff to concentrate on other high-value activities.

Please note that a clean Investment Policy with all recommended revisions incorporated is also attached.

The attached Investment Strategy provides a review of our current strategy with respect to the investment portfolio and recommendations for the upcoming year. The strategy is similar to the prior year with substantive changes noted in the attachment. Additionally, an economic review of the past year and summary of current economic conditions is provided.

Attachments: Investment Strategy Memorandum
Investment Policy

Distribution:
Rich Waterman, Vice Mayor
Anne Bybee, Council Member
Brian Loventhal, City Manager

MEMORANDUM



CITY OF CAMPBELL

Finance Department

To: Finance Sub-Committee

From: Will Fuentes, Finance Director

Subject: **Investment Strategy for FY 2019-20**

Date: July 23, 2019

BACKGROUND

The investment policy establishes procedures and guidelines by which the City's surplus funds can be managed in a prudent and fiscally sound manner. The policy encompasses those funds over which the City exercises fiscal control and prioritizes the objectives of public funds management as safety, liquidity and yield, in that order and consistent with guidance provided by the Government Finance Officers Association (GFOA). It also stipulates allowable and unallowable investment alternatives as well as establishes parameters for selecting broker/dealers and institutions with which the City may do business.

California Government Code Section 53646 (a) (2) requires that on an annual basis, the City Investment Policy be submitted to its legislative body and any oversight committee for consideration at a public meeting. The Finance sub-Committee is the oversight committee responsible for review of the Investment Policy. In addition to review of any proposed revisions to the Investment Policy, staff has prepared a report summarizing the past year's economic conditions and the recommended strategy for managing the City's available invested funds.

SUMMARY OF CURRENT STRATEGY AND RECOMMENDATIONS

It is recommended that the City maintain sufficient liquidity to cover daily operating cash flows for a minimum of 3 months to provide a reasonable cushion for fluctuations in the portfolio balance and for unforeseen emergencies. Average monthly disbursements are approximately \$6.0 million. Therefore, staff will retain a target of \$18.0 million in the Local Agency Investment Fund (LAIF) and use the remainder to invest in a portfolio of fixed income securities with individual maturities up to 5 years while maintaining a weighted average maturity of 3 years or less. Please note that as of June 2019, the City had \$27.1 million invested in LAIF, with an annual return of 2.43%. Given the current state of fixed income interest rates and a somewhat inverted yield curve (i.e., short-term interest rates are slightly higher than long-term interest rates), LAIF is currently outperforming other longer-term investment classes such as government securities and corporate notes. Thus, staff has recently taken a short-term investment strategy of accumulating funds in LAIF beyond the target level stated above so as to increase portfolio yield, while still maintaining excellent security and liquidity. Nevertheless, so as to protect against the natural shift in short-term interest rates downward, staff will work with the City's broker/dealers over the next year to diversify its portfolio with longer-term assets. This strategy will seek to lock in an acceptable

rate of return over the next several years, with a weighted average maturity of 3 years or less.

Interest rates, having been at historically low levels for number of years, have risen as the Federal Reserve has taken a strategy of increasing the discount rate several times in the past couple of years. However, it is anticipated that at its July 31 meeting, the Federal Reserve will decrease rates by 25 basis points (bps), with another 25-bps reduction expected by the calendar year-end. This will have the biggest impact on short-term interest rates and could correct the yield curve so that long-term interest rates are again higher than short-term interest rates; appropriately rewarding the duration risk of holding a longer-term investment. Consequently, staff will again work with the City's broker dealers to diversify its portfolio and move fund away from LAIF; thereby locking in an acceptable rate of return and countering the likely shift in short-term interest rates downward over the next year.

INVESTMENT OBJECTIVES AND OVERVIEW

The City's policy is to invest public funds in a prudent manner, provide for maximum security while meeting daily cash flow needs and comply with applicable statutes. Chief among the objectives outlined in the policy are safety, liquidity and yield, in that specific order and again consistent with GFOA guidance. Within this framework, a number of investment choices are provided to allow flexibility in meeting these objectives. The City continues to take a conservative approach with its investments that is reflected in the current investment policy.

As a means to implement the policy, it is important to develop a strategy for achieving the stated objectives. Likewise, the strategy should be reviewed periodically to determine whether it needs to be modified in light of changing economic and financial conditions. This document will serve as the City's investment strategy for the next year and will be reviewed annually in conjunction with the review of the City's investment policy or sooner if conditions warrant.

REVIEW OF PAST YEAR

Real gross domestic product (GDP) grew at an annual rate of 3.1% in the first quarter of 2019, compared to 2.2% in the same quarter in 2018 and down from a four-year high of 4.2% in the second quarter of 2018. Corporate earnings during the first quarter of 2019, despite fears of a pending recession, have mostly been very favorable and have positively impacted the stock market (DJIA). The DJIA increased from 24,271 to 26,599 in the twelve months ending June 30, 2019, an increase of approximately 9.6%. However, the stock market has been marked by a very high level of volatility over the past year as the US intensifies trade disputes with China and other countries, investors react almost daily to the President's use of social media, and a high rate of automated high-volume trading persists. While US economic fundamentals remain largely intact, the Federal Reserve has become increasingly concerned about the downside risks to the economic outlook due to ongoing headwinds from slower global growth, persistently low global inflation rates, and trade disputes. At the same time, the housing market has continued to be largely healthy nationally and, especially, in the Bay Area, but there has been softening over the past year, with average home prices leveling off and month-to-month sales activity declining. Investment in residential development expressed as a proportion of GDP also declined by 0.01% in 2018 and declined by an estimated 0.11% in the first quarter of 2019. A lowering of the

discount rate by the Federal Reserve may bolster this sector over the next year, with further strength coming from continued low unemployment in the region, high housing demand, and a persistent scarcity of housing supply.

Accordingly, unemployment declined yet again during the past year to very low levels. In California, the unemployment rate dropped even further from 3.7% in May 2018 to 3.5% in May 2019 (not seasonally adjusted). Locally, the County unemployment rate dropped from 2.2% in May 2018 to 2.1% in May 2019 (not seasonally adjusted). Lastly, the unemployment rate in Campbell also declined from 2.1% in May 2018 to 1.9% in May 2019 (not seasonally adjusted). For all intents and purposes, this is considered near “full employment”. Job creation around Silicon Valley continued to grow during the past year although the rate of growth is slowing and employers are hindered by shortage of labor able to fill vacancies. In terms of the economy as a whole, there is a low chance of a recession in the next 24 months, but staff remains cautious and will maintain an investment strategy that ensures long-term fiscal sustainability.

For the fiscal year ended June 30, 2019, the City’s average portfolio balance was approximately \$39.7 million and the average yield for this same period was 2.08% compared to \$39.7 million and 1.54%, respectively, for fiscal year ended June 30, 2018.

CURRENT MARKET CONDITIONS AND PORTFOLIO BALANCE

The State and National economies have continued to do well in recent months despite the high volatility in the stock market and damage caused by various natural events throughout the country and state during the past year such as Hurricane Michael in October 2018 and the California wildfires in November 2018. It remains unclear what the long-term effects of the national trade policies will be once these policies and other actions enacted by the current presidential administration play out over time. The US has already agreed to a new trade agreement with Mexico and Canada and may be near to a trade agreement with China. The latter remains highly uncertain though and the stock market’s fear of the harmful economic to the economy of a prolonged trade war will continue. Notwithstanding, inflation in the San Francisco Bay Area is currently running at an annual rate (June 2018 to June 2019) of approximately 3.2% and is expected to remain flat and constrained in the coming year.

As of June 30, 2019, the City’s investment portfolio was valued at approximately \$43.6 million. This was comprised of approximately \$27.1 million (62.17%) in LAIF and \$16.5 million (37.83%) in US Government Agency securities, with no funds currently invested in corporate notes or money market accounts. Almost all these funds are considered “discretionary” investments meaning that the City can invest this amount as it sees fit within the guidelines of the investment policy. With a minimum holdback of at least \$18.0 million for cash flow, that leaves up to \$25.6 million that can be invested in Agency and other securities (limitation of 75% of portfolio per investment policy). \$16.5 million is currently invested outside of LAIF. Staff will be looking to increase the City’s portfolio of Agency securities and corporate notes over FY 2019-20 so as to again protect against a decrease

in short-term interest rates, of which LAIF is highly dependent, and to lock in an acceptable rate of return consistent with the City's Investment Policy.

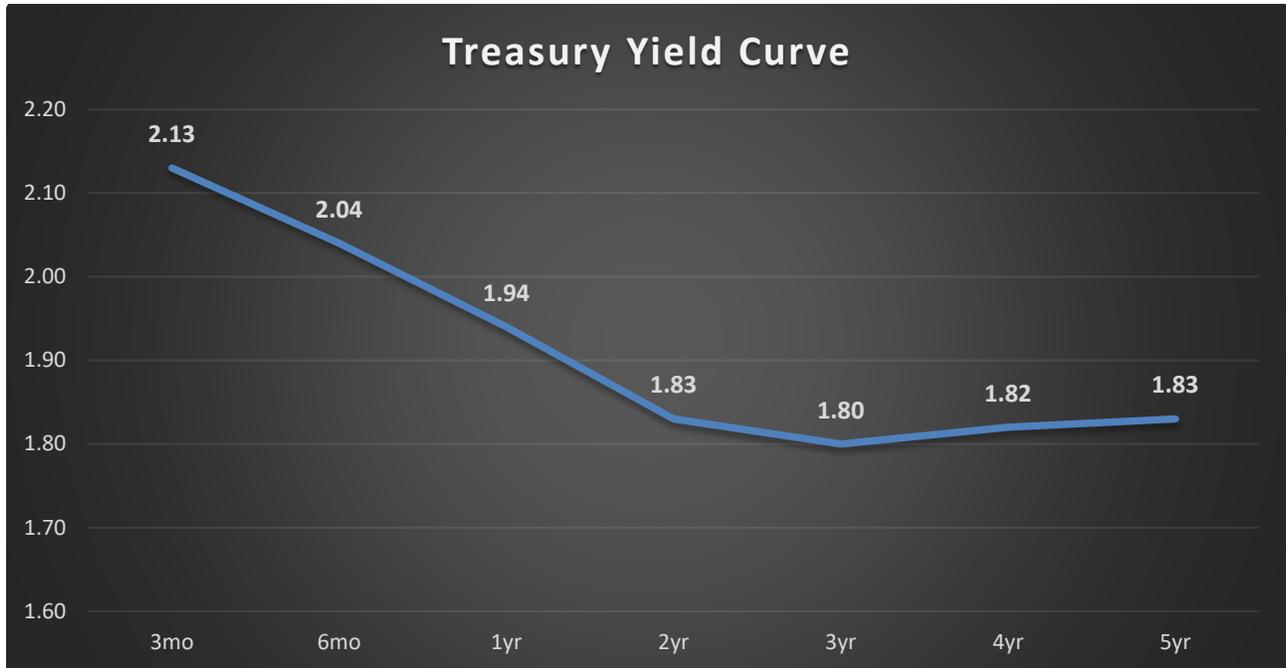
DISCUSSION OF ALLOWABLE INVESTMENTS

The City's investment policy contains a listing of allowable investment instruments along with specified limits and maturities. These include:

- State of California Local Agency Investment Fund (LAIF)
- US Treasury Bills, Notes & Bonds
- US Government Agency Issues (e.g., FNMA & GNMA)
- Corporate Medium-Term Notes
- Banker's Acceptances
- Certificates of Deposit with banks or savings & loan associations
- Repurchase Agreements
- Commercial Paper
- Mutual Funds (allowed by Calif. Gov't Code Sec. 53601(a)-(m))

It is the City's experience that LAIF provides a safe short-term investment vehicle, and the City has utilized it for its primary source of investment earnings for many years. This fund is generally viewed as a conservative and safe investment choice. In fact, the City is not aware of any municipality that has ever experienced a loss of principal in LAIF. One characteristic of LAIF is that, due to its size (combined State Investment Pool assets valued at approximately \$105.7 billion) the rate of return will typically lag the current market. Thus, in periods of rising interest rates, LAIF may have a lower return. Conversely, in a declining market, LAIF will provide investors with an above-market return. The yield as of June 2019 was approximately 2.57% compared to 1.90% one year ago. LAIF yield is expected to drop slightly to a range of 2.15% to 2.35% by the end of calendar year 2019, but a key benefit of using LAIF is that it offers a high degree of liquidity whereby funds can generally be requested and received in the same day. Another benefit is that a minimum of staff administrative effort is required, enabling the time to be spent on other departmental priorities.

US Treasuries are considered to be one of the safest investment choices available to municipalities due to their being backed by the full faith and credit of the United States Government. However, because of their popularity and under current market conditions, the rate of return tends to be lower than other types of securities. As of July 17, 2019, the 6-month and 2-year term Treasuries are yielding 2.04% and 1.83%, respectively. The 5-year Treasury has a yield of 1.83%. These rates have decreased significantly from a year ago. For reference, please see the treasury yield curve as of July 17, 2019 below. As illustrated, the fixed income market is currently experiencing a slightly inverted yield curve where short-term interest rates are higher than long-term interest rates in the 3 month to 3 year range. This is inverse of the normal relationship between interest rates and length of investment, but it indicates long-term uncertainty in the investment market and a preference towards short-term, liquid investments until uncertainty clears up. Rates in the 4 year and 5 year range are slightly higher, creating a u-shaped treasury yield curve.



US Agency issues also provide a safe and acceptable rate of return and are still considered a safe investment choice (AAA rated). Agencies can be “callable” meaning they can be redeemed by the issuer prior to maturity or “non-callable (bullet)” meaning they cannot be redeemed prior to maturity. Agencies also issue “discount notes” which have shorter term issues, generally less than 18 months, in which the note is bought at a deep discount and redeemed for face value at maturity. The City has historically purchased primarily callable structured rate agencies to maximize its yields and minimize interest rate risk in the future. As of June 30, 2019, the City held \$16.5 million in US Agency issues and earned an annual interest rate of 2.005%.

With respect to the upcoming year, it is anticipated that investments outside of LAIF will continue to be made primarily in callable agency securities with some rate protection and an average term of two to four years. Staff will also evaluate other types of investments allowed by policy that may have yields in excess of LAIF and agency issues, such as short-term commercial paper, corporate notes rated AA or higher, and non-callable agency issues, or that lock in an acceptable rate of return for a longer period of time than LAIF. And lastly, staff will also explore whether the use of an outside investment consultant would cost-effectively increase return and investment expertise, while also allowing staff to concentrate on other high-value activities.

RECOMMENDATION

It is recommended that the Finance sub-Committee approve the proposed strategy.

Distribution:

Rich Waterman, Vice Mayor
Liz Gibbons, Council Member
Brian Loventhal, City Manager



City of Campbell, California

Investment Policy

Date: August 20, 2019

I. PURPOSE

It is the policy of the City of Campbell to invest public funds in a prudent manner which conforms to all statutes governing the investment of public funds while providing security and meeting the daily cash flow needs of the City.

The purpose of this document is to identify the policies guiding prudent investment of the City's temporarily idle funds and to establish guidelines and objectives for suitable investments including delegation of authority, prudence, monitoring and reporting, policy review, diversification, eligible securities, safekeeping, collateralization, selection of financial institutions and broker/dealers, glossary of terms, and forms utilized.

II. SCOPE

A. This investment policy shall apply to all financial assets, investment activities, and debt issues of the City of Campbell including the following fund types:

1. General Fund
2. Special Revenue Funds
3. Debt Service Funds
4. Capital Projects Funds
5. Internal Service Funds
6. Trust and Agency Funds

B. The policy does not cover funds held by the Public Employees Retirement System nor funds of the Deferred Compensation program.

III. OBJECTIVES

A. It is the objective of this policy to provide a system which will monitor and forecast revenues and expenditures so that the City can invest temporarily idle funds to the fullest extent possible. The temporarily idle funds shall be invested in accordance with provisions of California Government Code Section 53600 et. seq.

B. The City adheres to conservative investment philosophies including investment of all idle cash, preservation of principal at the risk of yield, maintenance of adequate liquidity to meet anticipated cash flow needs and diversification to avoid the risks inherent in over investing in any one asset class.

C. This policy specifically prohibits trading securities for the sole purpose of speculating on the future direction of interest rates. It further prohibits reverse repurchase agreements, use of derivative products, and/or leveraging of the portfolio.

D. The City shall ensure the safety of invested funds by limiting credit and interest rate risks. The three primary objectives of the City's Investment Policy in order of priority are:



City of Campbell, California

Investment Policy

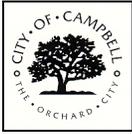
Date: August 20, 2019

1. **Safety:** Safety of principal is the foremost objective of the City of Campbell. Safety and the minimizing of risk associated with investing refer to attempts to reduce the potential for loss of principal, interest or a combination of the two. The City ensures safety of its invested idle funds and limits credit and interest rate risks by following these guidelines (all of which are detailed within the body of the Investment Policy):
 - a. Investing only in those instruments that are generally accepted as safe investment vehicles for local government as authorized by this Policy,
 - b. Carefully reviewing the qualifications and financial strength of financial institutions and broker/dealers prior to conducting business with them,
 - c. Diversifying the investment portfolio as prescribed within this Policy,
 - d. Structuring the portfolio such that securities mature to meet the City's cash requirements for ongoing operations, thereby avoiding the need to sell securities on the open market prior to their maturation,
 - e. Limiting the final maturity of purchased securities to five years; limiting the weighted average maturity of the portfolio to three years, and
 - f. Ensuring the physical security or safekeeping of the City's investments.
2. **Liquidity:** Liquidity is the second most important objective of the City's Policy. Liquidity refers to the ability to convert an investment to cash promptly without loss of principal and minimal loss of interest. For example, this is accomplished by investing either in the Local Agency Investment Fund (LAIF) with same day availability, or investing in securities with active secondary or resale markets.
3. **Yield:** Yield on the City's portfolio is last in rank among investment objectives. Investments are limited to relatively low risk securities in anticipation of earning a fair return relative to the risk being assumed.

IV. STRUCTURE AND RESPONSIBILITY

A. DELEGATION OF AUTHORITY:

1. The City Council assumes direction over the City's investments, and assigns management responsibility for the investment program to the Finance Director, who shall serve as Chief Fiscal Officer, and have legal custody of funds. The Finance Director may provide for delegation of his/her responsibilities to other persons under his/her control responsible for investment transactions, including designation of certain portions of the



City of Campbell, California

Investment Policy

Date: August 20, 2019

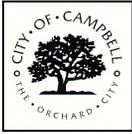
investment portfolio related to debt financing to be administered by professional portfolio administrators, i.e. California Arbitrage Management Program (C.A.M.P.) or such other designated administrators approved by the Finance Sub-Committee.

B. POLICY REVIEW:

1. This Investment Policy shall be reviewed and approved annually as required by California Government Code Section 53600 et. seq.

C. RESPONSIBILITIES:

1. **Responsibilities of the City Council:** The City Council consists of a Mayor and four Council members and is the policy setting board for the City of Campbell. The City Council has considered and adopted a written Investment Policy for the City of Campbell. Pursuant to the City's Financial Policies, the City Council shall on an annual basis, approve necessary changes to the Investment Policy as recommended by the Finance Sub-Committee. On a ~~monthly-quarterly~~ basis, the City Council shall receive, review and accept the ~~Monthly-Quarterly~~ Investment Report submitted by the Finance Department.
2. **Responsibilities of the Finance Sub-Committee:** The Finance Sub-Committee consists of two Council members, the City Manager, the Finance Director, and the Finance Manager. On an annual basis, this Sub-Committee shall review necessary revisions to the established Investment Policy of the City of Campbell and make a recommendation to the City Council accordingly. No less than once per fiscal year, the City's investment strategy will be reviewed by the Finance Sub-Committee. A summary of the investment strategy will be shared with the City Council at that time. Should market activity encourage revisions in the City's strategy, the Finance Sub-Committee shall be advised accordingly.
3. **Responsibilities of the City Manager:** The City Manager is responsible for directing and supervising the Finance Director. He/she has the responsibility of keeping the City Council fully advised as to the financial condition of the City.
 - a. **Wire Transfer Authority:** The City Manager has unlimited wire transfer authority for a single transaction. Such a transaction requires joint review, approval and verification in advance by the City Manager and Finance Director. The transaction shall be highlighted in the ~~Monthly-Quarterly~~ Investment Report to Council.
4. **Responsibilities of the Finance Director:** The Finance Director is appointed by the City Manager and serves as Chief Fiscal Officer. He/she is subject to the direction and supervision of the City Manager. The Finance Director is charged with the responsibility for the conduct of all Finance Department functions including the custody and investment of City funds, and investment of those funds in accordance with principles of sound treasury management and in accordance with applicable laws and policies. Refer to "Delegation of Authority" for additional information pertaining to delegation of investment responsibilities.



City of Campbell, California

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Date: August 20, 2019

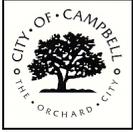
- a. **Wire Transfer Authority:** The Finance Director has wire transfer authority not to exceed \$5,000,000 for a single transaction. Such a transaction shall be reviewed, approved and verified in advance by the City Manager. The transaction shall be highlighted in the Monthly Quarterly Investment Report to Council.
5. **Responsibilities of the Finance Manager:** The Finance Manager is appointed by the Finance Director and serves as the Investment Manager for the City pursuant to specific delegation authority provided by this Investment Policy. He/she is subject to the direction and supervision of the Finance Director and is charged with the responsibility and conduct of the day-to-day accounting and cash management functions of the City. This includes the custody and investment of City funds, and investment of those funds in accordance with principles of sound treasury management and in accordance with applicable laws and policies. Refer to "Delegation of Authority" for additional information pertaining to delegation of investment responsibilities.

Implementation and maintenance of the Investment Policy are the responsibility of this individual. On an annual basis, the Finance Manager shall present to the Finance Sub-Committee, recommended changes to the City's Investment Policy. On a monthly-quarterly basis, the Finance Manager shall present to the City Council, via the City Manager, a Monthly-Quarterly Investment Report. Refer to "Monitoring and Reporting" for additional information.

- a. **Wire Transfer Authority:** The Finance Manager has wire transfer authority not to exceed \$3,000,000 for a single investment transaction. Such a transaction shall be reviewed, approved and verified in advance by the Finance Director, and shall be reported in the Monthly-Quarterly Investment Report to Council.
6. **Responsibilities of the Accountant and Sr. Accountant:** The Accountant is appointed by the Finance Director and is subject to the direction and supervision of the Finance Manager. The Accountant carries out the specific instructions provided by the Finance Manager regarding the purchase and sale of securities in accordance with principles of sound treasury management and in accordance with applicable laws and policies. Accounting for the various investment transactions is the responsibility of the Accountant.
- a. **Wire Transfer Authority:** The Accountant and Senior Accountant have wire transfer authority not to exceed \$2,100,000 for a single investment transaction. The standard operating procedure is that all cash and investment wire transfers made by the Accountant and Senior Accountant are reviewed, approved and verified in advance by the Finance Manager, and are reported in the Monthly-Quarterly Investment Report to Council.

D. Prudence:

1. It is the understanding of the individuals holding positions with investment responsibilities that the "prudent person investor" rule applies. This means that investments shall be made with judgment and care, under circumstances then prevailing, which persons of prudence, discretion and intelligence exercise in the management of their own affairs, not for speculation, but for investment, considering the probable safety of their capital and income to be derived.



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2. 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 riskless and that the investment activities of the City are a matter of public record. Accordingly, while the intent of the City is to hold purchased securities to maturity, the City recognizes that occasional measured losses may be advisable in a diversified portfolio and shall be considered within the context of the overall portfolio's return, provided that (a) adequate diversification has been implemented, (b) the sale of a security is in the best long-term interest of the City and (c) the City Manager approves in writing.

E. 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 disclose to the City Manager any business interests they have in financial institutions that conduct business with the City, and they shall subordinate their personal investment transactions to those of the City. In addition, the City Manager, the Finance Director and others with delegated investment authority shall file a Statement of Economic Interests each year pursuant to California Government Code Section 87203 and regulations of the Fair Political Practices Commission.

F. Conflict with State Statutes or Regulations

1. Any conflict between the City of Campbell Investment Policy and Government Code Section 53600 et seq, shall be interpreted in favor of the Government Code.

V. AUTHORIZED SECURITIES AND TRANSACTIONS

All investments and deposits of the City shall be made in accordance with California Government Code Sections 16429.1, 53600-53609 and 53630-53686, except that pursuant to California Government Code Section 5903(e), proceeds of bonds and any moneys set aside or pledged to secure payment of the bonds may be invested in securities or obligations described in the ordinance, resolution, indenture, agreement, or other instrument providing for the issuance of the bonds. Any revisions or extensions of these code sections will be assumed to be part of this Policy immediately upon being enacted. However, in the event that amendments to these sections conflict with this Policy and past City investment practices, the City may delay adherence to the new requirements when it is deemed in the best interest of the City to do so. Percentage holdings limits listed in this section apply at the time the security is purchased.

The City has further restricted the eligible types of securities and transactions to the following:

1. United States Treasury bills, notes, bonds, or strips with a final maturity not exceeding five years from the date of purchase.
2. Federal Agency debentures and mortgage-backed securities with a final maturity not exceeding five years from the date of purchase issued by the Government National



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Mortgage Association (GNMA). The aggregate investment in Federal Agency obligations shall not exceed 75% of the City's total portfolio.

3. 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 purchase, issued by the following only: Federal Home Loan Banks (FHLB), Federal National Mortgage Association (FNMA), Federal Farm Credit Banks (FFCB) and Federal Home Loan Mortgage Corporation (FHLMC). The aggregate investment in Federal Instrumentality obligations shall not exceed 75% of the City's total portfolio.
4. Repurchase Agreements with a final termination date not exceeding one year collateralized by U.S. Treasury obligations, Federal Agency securities, or Federal Instrumentality securities listed in items 1, 2 and 3 above with the maturity of the collateral not exceeding five 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 102% of the dollar value of the transaction. 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. The aggregate investment in repurchase agreements shall not exceed 10% of the City's total portfolio.

Repurchase Agreements shall be entered into only with broker/dealers that have executed a City approved Master Repurchase Agreement with the City. Repurchase counterparties shall be recognized as Primary Dealers with the Federal Reserve Bank of New York, or shall have a primary dealer within their holding company structure. Broker/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. The Finance Director shall maintain a copy of the City's approved Master Repurchase Agreement along with a list of the broker/dealers that have executed a Master Repurchase Agreement with the City.

5. Prime Commercial Paper with a maturity not exceeding 270 days from the date of purchase with the highest ranking or of the highest letter and number rating as provided for by a NRSRO. The entity that issues the commercial paper shall meet all of the following conditions in either sub-paragraph a. or sub-paragraph b. below:
 - a. The entity shall (1) be organized and operating in the United States as a general corporation, (2) have total assets in excess of five hundred million dollars (\$500,000,000) and (3) have debt other than commercial paper, if any, that is rated "A" or higher by a NRSRO.
 - b. 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 "A-1" or higher, or the equivalent, by a NRSRO.

Purchases of eligible commercial paper may not represent more than 10% of the outstanding commercial paper of any single corporate issuer. No more than 10% of the City's total portfolio may be invested in the commercial paper of any one issuer, and the



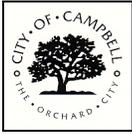
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aggregate investment in commercial paper shall not exceed 25% of the City's total portfolio.

6. Eligible Bankers Acceptances rated at least A-1 by Standard & Poor's, P-1 by Moody's, or F1 by Fitch at the time of purchase by each service that rates the commercial paper, with a maturity not exceeding 180 days from the date of purchase, issued by a state or national bank that has combined capital and surplus of at least \$250 million, whose deposits are insured by the FDIC, and whose senior long-term debt is rated at least A by Standard & Poor's, A2 by Moody's or A by Fitch at the time of purchase. No more than 10% of the City's total portfolio may be invested in banker's acceptances of any one issuer, and the aggregate investment in banker's acceptances shall not exceed 30% of the City's total portfolio.
7. 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 purchase, and rated at least AA by Standard & Poor's, Aa2 by Moody's or AA by Fitch. The aggregate investment in medium term notes shall not exceed ~~40~~30% of the City's total portfolio.
8. Non-negotiable Time Certificates of Deposit and savings deposits with a maturity not exceeding five years, in state or nationally chartered banks or savings and loans with a California branch office that are insured by the FDIC. Time Certificates of Deposit exceeding the FDIC insured amount must be secured pursuant to California Government Code Section 53652. No more than \$1 million may be invested in non-negotiable time certificates of deposit of any one issuer and the aggregate amount invested in non-negotiable time certificates of deposit shall not exceed 25% of the City's total portfolio.
9. Certificates of Deposit at commercial bank, savings bank, or savings and loan association that uses a private sector entity (Certificate of Deposit Account Registry Service) that assists in the placement of certificates of deposit, provided that the purchase of certificates of deposit do not, in total, exceed 30% of the City's funds that may be invested for this purpose. The City shall choose a nationally or state chartered commercial bank in California as the "selected" depository institution to invest the funds. The selected depository institution may submit the funds to a CDARS for the benefit of the City's account. The full amount of the principal and interest that may be accrued during the maximum term of each certificate shall be insured by the FDIC.
10. State of California's Local Agency Investment Fund (LAIF), pursuant to California Government Code Section 16429.1.
11. Mutual Funds registered under the Investment Company Act of 1940 that (1) are "no-load" (meaning no commission or fee shall be charged on purchases or sales of shares); (2) invest only in the securities and obligations authorized in this policy and (3) have a rating of AAAM by Standard and Poor's, Aaa by Moody's or AAA/V1+ by Fitch. No more than 10% of the City's total portfolio may be invested in mutual funds of any one issuer, and the aggregate investment in mutual funds shall not exceed 15% of the City's total portfolio.
12. Money Market Mutual Funds registered under the Investment Company Act of 1940 that (1) are "no-load" (meaning no commission or fee shall be charged on purchases or sales



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of shares); (2) have a constant daily net asset value per share of \$1.00; (3) invest only in the securities and obligations authorized in this policy and (4) have a rating of at least two of the following: AAAM by Standard and Poor's, Aaa by Moody's or AAA/V1+ by Fitch. No more than 10% of the City's total portfolio may be invested in money market funds of any one issuer, and the aggregate investment in money market funds shall not exceed 15% of the total portfolio.

13. Municipal and State Obligations with a minimum long-term rating of A/A-1 or higher by Standard and Poor's and not exceeding 10% of the portfolio:

(a) Bonds Issued by the Local Agency (City of Campbell) including bonds payable solely out of the revenue 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.)

(b) State Obligations including registered treasury notes or bonds of this State and any of the other 49 states in addition to California, including bonds payable solely out of the revenue from a revenue-producing property owned, controlled, or operated by a state or by a department, board, agency, or authority of the any of the other 49 United States, in addition to California.

(c) California Local Agency obligations including bonds, notes, warrants, or other evidence of indebtedness of any local agency within this state, including bonds payable solely out of the revenue from a revenue-producing property owned, controlled, or operated by the local agency or by a department, board, agency, or authority of the any of the local agency.

14. Asset-Backed, Mortgage-Backed, Mortgage Pass-Through Securities, and Collateralized Mortgage Obligations from Issuers Not Defined in Sections 1, 2, and 4 of the Authorized Investments Section of This Policy, provided that:

(a) The securities are rated in a rating category of "AA" or its equivalent or better by a NRSRO.

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

(c) No more than 5% of the portfolio may be invested in any single Asset-Backed or Commercial Mortgage security issuer.

(d) The maximum legal final maturity does not exceed five (5) years.

15. Supranationals, provided that:

(a) Issues are US dollar denominated senior unsecured unsubordinated obligations issued or unconditionally guaranteed by the International Bank for Reconstruction and Development, International Finance Corporation, or Inter-American Development Bank.

(b) The securities are rated in a rating category of "AA" or its equivalent or better by a NRSRO.

(c) No more than 30% of the total portfolio may be invested in these securities.

(d) No more than 10% of the portfolio may be invested in any single issuer.

(e) The maximum maturity does not exceed five (5) years.



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Note: Per state statute, the maximum combination of Mutual Funds and Money Market Mutual Funds is 20% of the portfolio.

It is the intent of the City that the foregoing list of authorized securities and transactions is strictly interpreted. Any deviation from this list must be preapproved by the City Council writing.

VI. PORTFOLIO MATURITIES AND LIQUIDITY

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 purchase, unless the City Council has granted authority to make such an investment at least three months prior to the date of investment. The weighted average final maturity of the City's portfolio shall at no time exceed 3 years.

VII. MONITORING AND REPORTING

A. The Finance Director shall routinely monitor the contents of the portfolio and shall file with the City Council the Finance Manager's Investment Report at the first regularly scheduled City Council meeting after 30 days from the end of the quarter~~within 30 days of the end of the quarter~~. The reports shall be prepared and submitted in accordance with California Government Code Section 53646 and shall include the following on all invested monies:

- Type of Investment and Issuer
- Beginning Balances
- Purchases During Month
- Maturities or Sales During the Month
- Ending Balances
- Maturity Date
- Weighted Average Final Maturity
- Call Provisions (if any)
- Interest Rate
- Weighted Average Yield
- Face Value or Purchase Cost
- Market Value including source
- Interest Earned During Month
- Interest Earned to Maturity
- Cash Flow Projection for the Following Month
- Summary of Cash Invested to Total Cash Balances
- Comparative Statistics by Fiscal Year
- Reconciliation of Cash & Investments to General Ledger Balances
- Investments under the Management of Contracted Parties
- Statement of Compliance with the Investment Policy
- Statement of Ability to Meet Obligations of Next Six Months

B. Each time an investment transaction is made, an "Investment Transaction Record" form shall be prepared by the Accountant and approved by the Finance Manager. Copies of the form are to be distributed to the City Manager, and Finance Director.



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VIII. SELECTION OF BROKER/DEALERS

The City shall transact business with securities broker/dealers after careful review of their qualifications and creditworthiness. In selecting broker /dealers, the Finance Director or designated staff member shall select broker/dealers representing primary dealers in government securities that have established offices and order desks within the State of California, or with such firms that have a primary dealer within their holding company structure. Exceptions to this rule will be made only upon the joint written authorization of the Finance Director and City Manager. Staff shall investigate broker/dealers wishing to do business with the City to determine if they are adequately capitalized, are reputable, have pending legal action against the firm or the individual broker, have established offices and order desks within the State of California, and make markets in the securities appropriate to the City's needs.

Before accepting funds or engaging in investment transactions with the City, the supervising officer at each authorized broker/dealer shall submit and annually update a City approved Broker/Dealer Information Request form that includes the firm's most recent audited financial statement. The Finance Director, or his or her designee, shall maintain a list of approved broker/dealers. Broker/dealers shall attest in writing that they have received and reviewed a copy of this Investment Policy, and that they will comply with it and disclose potential conflicts or risks to public funds that might arise out of business transactions between the firm and the City of Campbell.

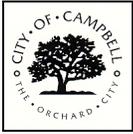
IX. SAFEKEEPING AND COLLATERALIZATION

A. Safekeeping:

1. The City shall contract with a bank or banks for the safekeeping of securities which are owned by the City as a part of the investment portfolio. Staff shall periodically review the performance and pricing of the third-party, safekeeping agent services.
2. All investment securities (except the collateral for certificates of deposit in banks, and/or savings and loans) purchased by the City shall be held in third-party safekeeping by an institution designated as primary agent. The primary agent shall issue a safekeeping receipt to the City listing the specific instrument, rate, maturity and other pertinent information, and shall provide monthly reports of activity and ending balances for all securities held on behalf of the City.

B. Collateralization:

1. Deposit-type securities (i.e. certificates of deposit) shall be collateralized through the State of California collateral pool requirements for any amount exceeding FDIC coverage in accordance with California Government Code Section 53652 and/or 53651(m) (1). Collateral for certificates of deposit shall be held in a trust company located in California, the trust department of a bank located in California or the Federal Home Loan Bank of San Francisco.
2. Other securities shall be collateralized by the actual security held in third-party safekeeping by the primary agent.



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X. DIVERSIFICATION AND ELIGIBLE SECURITIES

The City will diversify investment instruments to avoid incurring unreasonable risks in overinvesting in specific instruments, individual financial institutions or maturities. The following portfolio maximums shall apply:

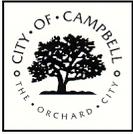
If the credit ratings of any security owned by the City are downgraded to a level below the quality required by this investment policy, it will be the City's policy to review the credit situation and make a determination as to whether to sell or retain such securities in the portfolio.

If a security is downgraded, the Finance Director will use discretion in determining whether to sell or hold the security based on its current maturity, the economic outlook for the issuer, and other relevant factors.

If a decision is made to retain a downgraded security in the portfolio, its presence in the portfolio will be monitored and reported quarterly to the City Council.

Authorized Securities and Transactions	Maximum	Portfolio
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CA. Gov't. Code Section	Authorized Investment	Maximum Maturity	Authorized Investment Limits - % of Portfolio	Credit Rating Limit
53601 (a)	City of Campbell Local Agency Bonds	5 years	None/10% Per Issuer	A/A-1 or Higher
53601 (c)	State Obligations	5 years	None/10% Per Issuer	A/A-1 or Higher
53601 (e)	California Local Agencies	5 years	None/10% Per Issuer	A/A-1 or Higher
53601(b)	United States Treasuries	5 years	None	None
53601(e)	Federal Agency Securities	5 years	75%	None
53601(e)	Federal Instrumentality	5 years	75%	None
53691(i)	Repurchase Agreements	1 year	10%	A-1/A
53601(g)	Prime Commercial Paper	270 days	25% 10% Per Issuer	A/A-1 or higher
53601(f)	Eligible Bankers Acceptances	180 days	10% per issuer/30% Aggregate	A-1/P-1/F-1
53601(j)	Medium Term Notes	5 years	40 30%	AA/Aa2/AA
53601(n)	Non-negotiable Certificates of Deposit	5 years	25% \$1 million per issuer	-

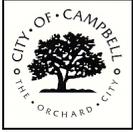


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CA. Gov't. Code Section	Authorized Investment	Maximum Maturity	Authorized Investment Limits - % of Portfolio	Credit Rating Limit
53601.8 (a)-(h)	Certificates of Deposit through Account Registry Services	5 years	7.5% Aggregate Maximum Up to the FDIC Insured Limit Per Issuer	-
16429.1	State of California LAIF	18 Months-Avg	None	-
53601(k)	*Mutual Funds	None	15%	AAAm/Aaa/AAAV1+
53601(k)	*Money Market Mutual Funds	None	15%	AAAm/Aaa/AAAV1+
<u>53601(o)</u>	<u>Asset-Backed, Mortgage-Backed, Mortgage Pass-Through Securities, and Collateralized Mortgage Obligations</u>	<u>5 years</u>	<u>20%</u>	<u>AA or higher</u>
<u>53601(q)</u>	<u>Supranationals</u>	<u>5 years</u>	<u>30%</u>	<u>AA or higher</u>
	*Combined total not to exceed 20% per State		20%	



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EXHIBIT A

GLOSSARY OF ELIGIBLE INVESTMENTS

Local Agency Investment Fund (L.A.I.F.). The L.A.I.F. was established by the state of California to enable treasurers to place funds in a pool for investments. There currently is a limitation of \$40 million per agency subject to a maximum of 15 total transactions per month. The City of Campbell uses this fund when interest rates are declining as well as for short-term investments and liquidity.

U.S. Treasury Bills. Commonly referred to as T-Bills, these are short-term marketable securities sold as obligations of the U.S. Government. T-Bills do not accrue interest but are sold at a discount to pay face value at maturity.

U.S. Treasury Notes. These are marketable, interest-bearing securities sold as obligations of the U.S. Government with original maturities of one to ten years. Interest is paid semi-annually.

U.S. Treasury Bonds. These are the same as U.S. Treasury Notes except they have original maturities of ten years or longer.

U.S. Government Agency Issues. Are securities that are unconditionally backed by the full faith and credit of the United States, including: Government National Mortgage Association (GNMA), Farmers Home Administration (FmHA), Small Business Administration (SBA), General Services Administration (GSA), Federal Housing Administration (FHA) and Housing and Urban Development (HUD).

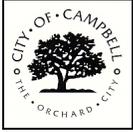
U.S. Government Instrumentality Issues. Are government sponsored enterprises that are backed by the creditworthiness of the issuing agency, not the full faith and credit of the U.S. government. They do carry an implied guarantee of government assistance to the organization should it encounter financial difficulties. Issuers include: Federal National Mortgage Association (FNMA), Federal Home Loan Bank (FHLB), Federal Farm Credit Banks (FFCB) and Federal Home Loan Mortgage Corporation (FHLMC).

Asset Backed Securities. - Securities that are supported by pools of assets, such as installment loans or leases, or by pools of revolving lines of credits. Asset-backed securities are structured as trusts in order to perfect a security interest in the underlying assets.

Banker's Acceptance. This is a negotiable time draft (bill of exchange) with a maturity of six months or less drawn on and accepted by a commercial bank. Banker's Acceptances are usually created to finance the import and export of goods, the shipment of goods within the United States and storage of readily marketable commodities. Per State Law, cities may not invest more than 30% of idle cash in Banker's Acceptances.

Certificate of Deposit (CD's). - is a receipt for funds deposited in a bank or savings and loan association for a specified period of time at a specified rate of interest. The first \$250,000 of a certificate of deposit is guaranteed by the Federal Deposit Insurance Corporation (FDIC). CD's with a face value in excess of \$250,000 can be collateralized by Treasury Department Securities, which must be at least 110% of the face value of the CD's, in excess of the first \$250,000, or by first mortgage loans which must be at least 150% of the face value of the CD balance in excess of the first \$250,000.

Repurchase Agreements (REPOS). - is a contractual arrangement between a financial institution, or dealer, and an investor. This agreement normally can run for one or more days. The investor puts up his funds for a certain number of days at a stated yield. In return, he takes a given block of securities as collateral. At maturity, the securities are repurchased and the funds repaid plus



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interest.

Commercial Paper. - Notes are unsecured promissory notes of industrial corporations, utilities and bank holding companies. State law limits a city to investments in United States corporations having assets in excess of five hundred million dollars with an "A" or higher rating. Per State law, cities may not invest more than 25% of idle cash in commercial paper.

Medium Term Notes. - are corporate or depository institution debt securities meeting certain minimum quality standards (as specified in the California Government Code) with a remaining maturity of five years or less.

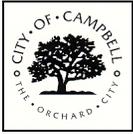
Money Market Mutual Fund. - Mutual funds that invest solely in money market instruments (short-term debt instruments, such as Treasury bills, commercial paper, bankers' acceptances, repos and federal funds).

Mortgage Backed Securities. - Mortgage-backed securities (MBS) are created when a mortgagee or a purchaser of residential real estate mortgages creates a pool of mortgages and markets undivided interests or participations in the pool. MBS owners receive a prorata share of the interest and principal cash flows (net of fees) that are "passed through" from the pool of mortgages. MBS are complex securities whose cash flow is determined by the characteristics of the mortgages that are pooled together. Investors in MBS face prepayment risk associated with the option of the underlying mortgagors to pre-pay or payoff their mortgage. Most MBS are issued and/or guaranteed by federal agencies and instrumentalities (e.g., Government National Mortgage Association (GNMA), Federal National Mortgage Association (FNMA), and Federal Home Loan Mortgage Corporation (FHLMC)).

Mortgage Pass-Through Obligations. - Securities that are created when residential mortgages (or other mortgages) are pooled together and undivided interests or participations in the stream of revenues associated with the mortgages are sold.

Mutual Fund. - An investment company that pools money and can invest in a variety of securities, including fixed-income securities and money market instruments. Mutual funds are regulated by the Investment Company Act of 1940 and must abide by strict Securities and Exchange Commission (SEC) disclosure guidelines.

Supranationals. - International institutions formed by two or more governments that transcend boundaries to pursue mutually beneficial economic or social goals. There are three supranational institutions that issue obligations that are eligible investments for California local agencies: the International Bank for Reconstruction and Development (IBRD), International Finance Corporation (IFC), and InterAmerican Development Bank (IADB).



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I. PURPOSE

It is the policy of the City of Campbell to invest public funds in a prudent manner which conforms to all statutes governing the investment of public funds while providing security and meeting the daily cash flow needs of the City.

The purpose of this document is to identify the policies guiding prudent investment of the City's temporarily idle funds and to establish guidelines and objectives for suitable investments including delegation of authority, prudence, monitoring and reporting, policy review, diversification, eligible securities, safekeeping, collateralization, selection of financial institutions and broker/dealers, glossary of terms, and forms utilized.

II. SCOPE

A. This investment policy shall apply to all financial assets, investment activities, and debt issues of the City of Campbell including the following fund types:

1. General Fund
2. Special Revenue Funds
3. Debt Service Funds
4. Capital Projects Funds
5. Internal Service Funds
6. Trust and Agency Funds

B. The policy does not cover funds held by the Public Employees Retirement System nor funds of the Deferred Compensation program.

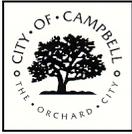
III. OBJECTIVES

A. It is the objective of this policy to provide a system which will monitor and forecast revenues and expenditures so that the City can invest temporarily idle funds to the fullest extent possible. The temporarily idle funds shall be invested in accordance with provisions of California Government Code Section 53600 et. seq.

B. The City adheres to conservative investment philosophies including investment of all idle cash, preservation of principal at the risk of yield, maintenance of adequate liquidity to meet anticipated cash flow needs and diversification to avoid the risks inherent in over investing in any one asset class.

C. This policy specifically prohibits trading securities for the sole purpose of speculating on the future direction of interest rates. It further prohibits reverse repurchase agreements, use of derivative products, and/or leveraging of the portfolio.

D. The City shall ensure the safety of invested funds by limiting credit and interest rate risks. The three primary objectives of the City's Investment Policy in order of priority are:



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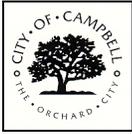
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1. **Safety:** Safety of principal is the foremost objective of the City of Campbell. Safety and the minimizing of risk associated with investing refer to attempts to reduce the potential for loss of principal, interest or a combination of the two. The City ensures safety of its invested idle funds and limits credit and interest rate risks by following these guidelines (all of which are detailed within the body of the Investment Policy):
 - a. Investing only in those instruments that are generally accepted as safe investment vehicles for local government as authorized by this Policy,
 - b. Carefully reviewing the qualifications and financial strength of financial institutions and broker/dealers prior to conducting business with them,
 - c. Diversifying the investment portfolio as prescribed within this Policy,
 - d. Structuring the portfolio such that securities mature to meet the City's cash requirements for ongoing operations, thereby avoiding the need to sell securities on the open market prior to their maturation,
 - e. Limiting the final maturity of purchased securities to five years; limiting the weighted average maturity of the portfolio to three years, and
 - f. Ensuring the physical security or safekeeping of the City's investments.
2. **Liquidity:** Liquidity is the second most important objective of the City's Policy. Liquidity refers to the ability to convert an investment to cash promptly without loss of principal and minimal loss of interest. For example, this is accomplished by investing either in the Local Agency Investment Fund (LAIF) with same day availability, or investing in securities with active secondary or resale markets.
3. **Yield:** Yield on the City's portfolio is last in rank among investment objectives. Investments are limited to relatively low risk securities in anticipation of earning a fair return relative to the risk being assumed.

IV. STRUCTURE AND RESPONSIBILITY

A. DELEGATION OF AUTHORITY:

1. The City Council assumes direction over the City's investments, and assigns management responsibility for the investment program to the Finance Director, who shall serve as Chief Fiscal Officer, and have legal custody of funds. The Finance Director may provide for delegation of his/her responsibilities to other persons under his/her control responsible for investment transactions, including designation of certain portions of the



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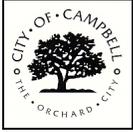
investment portfolio related to debt financing to be administered by professional portfolio administrators, i.e. California Arbitrage Management Program (C.A.M.P.) or such other designated administrators approved by the Finance Sub-Committee.

B. POLICY REVIEW:

1. This Investment Policy shall be reviewed and approved annually as required by California Government Code Section 53600 et. seq.

C. RESPONSIBILITIES:

1. **Responsibilities of the City Council:** The City Council consists of a Mayor and four Council members and is the policy setting board for the City of Campbell. The City Council has considered and adopted a written Investment Policy for the City of Campbell. Pursuant to the City's Financial Policies, the City Council shall on an annual basis, approve necessary changes to the Investment Policy as recommended by the Finance Sub-Committee. On a quarterly basis, the City Council shall receive, review and accept the Quarterly Investment Report submitted by the Finance Department.
2. **Responsibilities of the Finance Sub-Committee:** The Finance Sub-Committee consists of two Council members, the City Manager, the Finance Director, and the Finance Manager. On an annual basis, this Sub-Committee shall review necessary revisions to the established Investment Policy of the City of Campbell and make a recommendation to the City Council accordingly. No less than once per fiscal year, the City's investment strategy will be reviewed by the Finance Sub-Committee. A summary of the investment strategy will be shared with the City Council at that time. Should market activity encourage revisions in the City's strategy, the Finance Sub-Committee shall be advised accordingly.
3. **Responsibilities of the City Manager:** The City Manager is responsible for directing and supervising the Finance Director. He/she has the responsibility of keeping the City Council fully advised as to the financial condition of the City.
 - a. **Wire Transfer Authority:** The City Manager has unlimited wire transfer authority for a single transaction. Such a transaction requires joint review, approval and verification in advance by the City Manager and Finance Director. The transaction shall be highlighted in the Quarterly Investment Report to Council.
4. **Responsibilities of the Finance Director:** The Finance Director is appointed by the City Manager and serves as Chief Fiscal Officer. He/she is subject to the direction and supervision of the City Manager. The Finance Director is charged with the responsibility for the conduct of all Finance Department functions including the custody and investment of City funds, and investment of those funds in accordance with principles of sound treasury management and in accordance with applicable laws and policies. Refer to "Delegation of Authority" for additional information pertaining to delegation of investment responsibilities.



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- a. Wire Transfer Authority:** The Finance Director has wire transfer authority not to exceed \$5,000,000 for a single transaction. Such a transaction shall be reviewed, approved and verified in advance by the City Manager. The transaction shall be highlighted in the Quarterly Investment Report to Council.
- 5. Responsibilities of the Finance Manager:** The Finance Manager is appointed by the Finance Director and serves as the Investment Manager for the City pursuant to specific delegation authority provided by this Investment Policy. He/she is subject to the direction and supervision of the Finance Director and is charged with the responsibility and conduct of the day-to-day accounting and cash management functions of the City. This includes the custody and investment of City funds, and investment of those funds in accordance with principles of sound treasury management and in accordance with applicable laws and policies. Refer to "Delegation of Authority" for additional information pertaining to delegation of investment responsibilities.

Implementation and maintenance of the Investment Policy are the responsibility of this individual. On an annual basis, the Finance Manager shall present to the Finance Sub-Committee, recommended changes to the City's Investment Policy. On a quarterly basis, the Finance Manager shall present to the City Council, via the City Manager, a Quarterly Investment Report. Refer to "Monitoring and Reporting" for additional information.

- a. Wire Transfer Authority:** The Finance Manager has wire transfer authority not to exceed \$3,000,000 for a single investment transaction. Such a transaction shall be reviewed, approved and verified in advance by the Finance Director, and shall be reported in the Quarterly Investment Report to Council.
- 6. Responsibilities of the Accountant and Sr. Accountant:** The Accountant is appointed by the Finance Director and is subject to the direction and supervision of the Finance Manager. The Accountant carries out the specific instructions provided by the Finance Manager regarding the purchase and sale of securities in accordance with principles of sound treasury management and in accordance with applicable laws and policies. Accounting for the various investment transactions is the responsibility of the Accountant.
 - a. Wire Transfer Authority:** The Accountant and Senior Accountant have wire transfer authority not to exceed \$2,100,000 for a single investment transaction. The standard operating procedure is that all cash and investment wire transfers made by the Accountant and Senior Accountant are reviewed, approved and verified in advance by the Finance Manager, and are reported in the Quarterly Investment Report to Council.

D. Prudence:

1. It is the understanding of the individuals holding positions with investment responsibilities that the "prudent investor" rule applies. This means that investments shall be made with judgment and care, under circumstances then prevailing, which persons of prudence, discretion and intelligence exercise in the management of their own affairs, not for speculation, but for investment, considering the probable safety of their capital and income to be derived.



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2. 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 riskless and that the investment activities of the City are a matter of public record. Accordingly, while the intent of the City is to hold purchased securities to maturity, the City recognizes that occasional measured losses may be advisable in a diversified portfolio and shall be considered within the context of the overall portfolio's return, provided that (a) adequate diversification has been implemented, (b) the sale of a security is in the best long-term interest of the City and (c) the City Manager approves in writing.

E. 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 disclose to the City Manager any business interests they have in financial institutions that conduct business with the City, and they shall subordinate their personal investment transactions to those of the City. In addition, the City Manager, the Finance Director and others with delegated investment authority shall file a Statement of Economic Interests each year pursuant to California Government Code Section 87203 and regulations of the Fair Political Practices Commission.

F. Conflict with State Statutes or Regulations

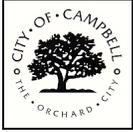
1. Any conflict between the City of Campbell Investment Policy and Government Code Section 53600 et seq, shall be interpreted in favor of the Government Code.

V. AUTHORIZED SECURITIES AND TRANSACTIONS

All investments and deposits of the City shall be made in accordance with California Government Code Sections 16429.1, 53600-53609 and 53630-53686, except that pursuant to California Government Code Section 5903(e), proceeds of bonds and any moneys set aside or pledged to secure payment of the bonds may be invested in securities or obligations described in the ordinance, resolution, indenture, agreement, or other instrument providing for the issuance of the bonds. Any revisions or extensions of these code sections will be assumed to be part of this Policy immediately upon being enacted. However, in the event that amendments to these sections conflict with this Policy and past City investment practices, the City may delay adherence to the new requirements when it is deemed in the best interest of the City to do so. Percentage holdings limits listed in this section apply at the time the security is purchased.

The City has further restricted the eligible types of securities and transactions to the following:

1. United States Treasury bills, notes, bonds, or strips with a final maturity not exceeding five years from the date of purchase.
2. Federal Agency debentures and mortgage-backed securities with a final maturity not exceeding five years from the date of purchase issued by the Government National



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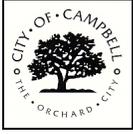
Mortgage Association (GNMA). The aggregate investment in Federal Agency obligations shall not exceed 75% of the City's total portfolio.

3. 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 purchase, issued by the following only: Federal Home Loan Banks (FHLB), Federal National Mortgage Association (FNMA), Federal Farm Credit Banks (FFCB) and Federal Home Loan Mortgage Corporation (FHLMC). The aggregate investment in Federal Instrumentality obligations shall not exceed 75% of the City's total portfolio.
4. Repurchase Agreements with a final termination date not exceeding one year collateralized by U.S. Treasury obligations, Federal Agency securities, or Federal Instrumentality securities listed in items 1, 2 and 3 above with the maturity of the collateral not exceeding five 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 102% of the dollar value of the transaction. 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. The aggregate investment in repurchase agreements shall not exceed 10% of the City's total portfolio.

Repurchase Agreements shall be entered into only with broker/dealers that have executed a City approved Master Repurchase Agreement with the City. Repurchase counterparties shall be recognized as Primary Dealers with the Federal Reserve Bank of New York, or shall have a primary dealer within their holding company structure. Broker/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. The Finance Director shall maintain a copy of the City's approved Master Repurchase Agreement along with a list of the broker/dealers that have executed a Master Repurchase Agreement with the City.

5. Prime Commercial Paper with a maturity not exceeding 270 days from the date of purchase with the highest ranking or of the highest letter and number rating as provided for by a NRSRO. The entity that issues the commercial paper shall meet all of the following conditions in either sub-paragraph a. or sub-paragraph b. below:
 - a. The entity shall (1) be organized and operating in the United States as a general corporation, (2) have total assets in excess of five hundred million dollars (\$500,000,000) and (3) have debt other than commercial paper, if any, that is rated "A" or higher by a NRSRO.
 - b. 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 "A-1" or higher, or the equivalent, by a NRSRO.

Purchases of eligible commercial paper may not represent more than 10% of the outstanding commercial paper of any single corporate issuer. No more than 10% of the City's total portfolio may be invested in the commercial paper of any one issuer, and the



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aggregate investment in commercial paper shall not exceed 25% of the City's total portfolio.

6. Eligible Bankers Acceptances rated at least A-1 by Standard & Poor's, P-1 by Moody's, or F1 by Fitch at the time of purchase by each service that rates the commercial paper, with a maturity not exceeding 180 days from the date of purchase, issued by a state or national bank that has combined capital and surplus of at least \$250 million, whose deposits are insured by the FDIC, and whose senior long-term debt is rated at least A by Standard & Poor's, A2 by Moody's or A by Fitch at the time of purchase. No more than 10% of the City's total portfolio may be invested in banker's acceptances of any one issuer, and the aggregate investment in banker's acceptances shall not exceed 30% of the City's total portfolio.
7. 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 purchase, and rated at least AA by Standard & Poor's, Aa2 by Moody's or AA by Fitch. The aggregate investment in medium term notes shall not exceed 30% of the City's total portfolio.
8. Non-negotiable Time Certificates of Deposit and savings deposits with a maturity not exceeding five years, in state or nationally chartered banks or savings and loans with a California branch office that are insured by the FDIC. Time Certificates of Deposit exceeding the FDIC insured amount must be secured pursuant to California Government Code Section 53652. No more than \$1 million may be invested in non-negotiable time certificates of deposit of any one issuer and the aggregate amount invested in non-negotiable time certificates of deposit shall not exceed 25% of the City's total portfolio.
9. Certificates of Deposit at commercial bank, savings bank, or savings and loan association that uses a private sector entity (Certificate of Deposit Account Registry Service) that assists in the placement of certificates of deposit, provided that the purchase of certificates of deposit do not, in total, exceed 30% of the City's funds that may be invested for this purpose. The City shall choose a nationally or state chartered commercial bank in California as the "selected" depository institution to invest the funds. The selected depository institution may submit the funds to a CDARS for the benefit of the City's account. The full amount of the principal and interest that may be accrued during the maximum term of each certificate shall be insured by the FDIC.
10. State of California's Local Agency Investment Fund (LAIF), pursuant to California Government Code Section 16429.1.
11. Mutual Funds registered under the Investment Company Act of 1940 that (1) are "no-load" (meaning no commission or fee shall be charged on purchases or sales of shares); (2) invest only in the securities and obligations authorized in this policy and (3) have a rating of AAAM by Standard and Poor's, Aaa by Moody's or AAA/V1+ by Fitch. No more than 10% of the City's total portfolio may be invested in mutual funds of any one issuer, and the aggregate investment in mutual funds shall not exceed 15% of the City's total portfolio.
12. Money Market Mutual Funds registered under the Investment Company Act of 1940 that (1) are "no-load" (meaning no commission or fee shall be charged on purchases or sales



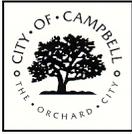
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of shares); (2) have a constant daily net asset value per share of \$1.00; (3) invest only in the securities and obligations authorized in this policy and (4) have a rating of at least two of the following: AA+ by Standard and Poor's, Aaa by Moody's or AAA/V1+ by Fitch. No more than 10% of the City's total portfolio may be invested in money market funds of any one issuer, and the aggregate investment in money market funds shall not exceed 15% of the total portfolio.

13. Municipal and State Obligations with a minimum long-term rating of A/A-1 or higher by Standard and Poor's and not exceeding 10% of the portfolio:
 - (a) Bonds Issued by the Local Agency (City of Campbell) including bonds payable solely out of the revenue 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.)
 - (b) State Obligations including registered treasury notes or bonds of this State and any of the other 49 states in addition to California, including bonds payable solely out of the revenue from a revenue-producing property owned, controlled, or operated by a state or by a department, board, agency, or authority of the any of the other 49 United States, in addition to California.
 - (c) California Local Agency obligations including bonds, notes, warrants, or other evidence of indebtedness of any local agency within this state, including bonds payable solely out of the revenue from a revenue-producing property owned, controlled, or operated by the local agency or by a department, board, agency, or authority of the any of the local agency.
14. Asset-Backed, Mortgage-Backed, Mortgage Pass-Through Securities, and Collateralized Mortgage Obligations from Issuers Not Defined in Sections 1, 2, and 4 of the Authorized Investments Section of This Policy, provided that:
 - (a) The securities are rated in a rating category of "AA" or its equivalent or better by a NRSRO.
 - (b) No more than 20% of the total portfolio may be invested in these securities.
 - (c) No more than 5% of the portfolio may be invested in any single Asset-Backed or Commercial Mortgage security issuer.
 - (d) The maximum legal final maturity does not exceed five (5) years.
15. Supranationals, provided that:
 - (a) Issues are US dollar denominated senior unsecured unsubordinated obligations issued or unconditionally guaranteed by the International Bank for Reconstruction and Development, International Finance Corporation, or Inter-American Development Bank.
 - (b) The securities are rated in a rating category of "AA" or its equivalent or better by a NRSRO.
 - (c) No more than 30% of the total portfolio may be invested in these securities.
 - (d) No more than 10% of the portfolio may be invested in any single issuer.
 - (e) The maximum maturity does not exceed five (5) years.



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Note: Per state statute, the maximum combination of Mutual Funds and Money Market Mutual Funds is 20% of the portfolio.

It is the intent of the City that the foregoing list of authorized securities and transactions is strictly interpreted. Any deviation from this list must be preapproved by the City Council writing.

VI. PORTFOLIO MATURITIES AND LIQUIDITY

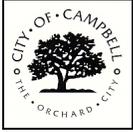
To the extent possible, investments shall be matched with anticipated cash flow requirements and known future liabilities. The City will not invest in securities maturing more than five years from the date of purchase, unless the City Council has granted authority to make such an investment at least three months prior to the date of investment. The weighted average final maturity of the City's portfolio shall at no time exceed 3 years.

VII. MONITORING AND REPORTING

A. The Finance Director shall routinely monitor the contents of the portfolio and shall file with the City Council the Finance Manager's Investment Report at the first regularly scheduled City Council meeting after 30 days from the end of the quarter. The reports shall be prepared and submitted in accordance with California Government Code Section 53646 and shall include the following on all invested monies:

- Type of Investment and Issuer
- Beginning Balances
- Purchases During Month
- Maturities or Sales During the Month
- Ending Balances
- Maturity Date
- Weighted Average Final Maturity
- Call Provisions (if any)
- Interest Rate
- Weighted Average Yield
- Face Value or Purchase Cost
- Market Value including source
- Interest Earned During Month
- Interest Earned to Maturity
- Cash Flow Projection for the Following Month
- Summary of Cash Invested to Total Cash Balances
- Comparative Statistics by Fiscal Year
- Reconciliation of Cash & Investments to General Ledger Balances
- Investments under the Management of Contracted Parties
- Statement of Compliance with the Investment Policy
- Statement of Ability to Meet Obligations of Next Six Months

B. Each time an investment transaction is made, an "Investment Transaction Record" form shall be prepared by the Accountant and approved by the Finance Manager. Copies of the form are to be distributed to the City Manager, and Finance Director.



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VIII. SELECTION OF BROKER/DEALERS

The City shall transact business with securities broker/dealers after careful review of their qualifications and creditworthiness. In selecting broker /dealers, the Finance Director or designated staff member shall select broker/dealers representing primary dealers in government securities that have established offices and order desks within the State of California, or with such firms that have a primary dealer within their holding company structure. Exceptions to this rule will be made only upon the joint written authorization of the Finance Director and City Manager. Staff shall investigate broker/dealers wishing to do business with the City to determine if they are adequately capitalized, are reputable, have pending legal action against the firm or the individual broker, have established offices and order desks within the State of California, and make markets in the securities appropriate to the City's needs.

Before accepting funds or engaging in investment transactions with the City, the supervising officer at each authorized broker/dealer shall submit and annually update a City approved Broker/Dealer Information Request form that includes the firm's most recent audited financial statement. The Finance Director, or his or her designee, shall maintain a list of approved broker/dealers. Broker/dealers shall attest in writing that they have received and reviewed a copy of this Investment Policy, and that they will comply with it and disclose potential conflicts or risks to public funds that might arise out of business transactions between the firm and the City of Campbell.

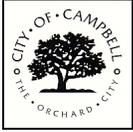
IX. SAFEKEEPING AND COLLATERALIZATION

A. Safekeeping:

1. The City shall contract with a bank or banks for the safekeeping of securities which are owned by the City as a part of the investment portfolio. Staff shall periodically review the performance and pricing of the third-party, safekeeping agent services.
2. All investment securities (except the collateral for certificates of deposit in banks, and/or savings and loans) purchased by the City shall be held in third-party safekeeping by an institution designated as primary agent. The primary agent shall issue a safekeeping receipt to the City listing the specific instrument, rate, maturity and other pertinent information, and shall provide monthly reports of activity and ending balances for all securities held on behalf of the City.

B. Collateralization:

1. Deposit-type securities (i.e. certificates of deposit) shall be collateralized through the State of California collateral pool requirements for any amount exceeding FDIC coverage in accordance with California Government Code Section 53652 and/or 53651(m) (1). Collateral for certificates of deposit shall be held in a trust company located in California, the trust department of a bank located in California or the Federal Home Loan Bank of San Francisco.
2. Other securities shall be collateralized by the actual security held in third-party safekeeping by the primary agent.



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X. DIVERSIFICATION AND ELIGIBLE SECURITIES

The City will diversify investment instruments to avoid incurring unreasonable risks in overinvesting in specific instruments, individual financial institutions or maturities. The following portfolio maximums shall apply:

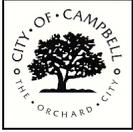
If the credit ratings of any security owned by the City are downgraded to a level below the quality required by this investment policy, it will be the City's policy to review the credit situation and make a determination as to whether to sell or retain such securities in the portfolio.

If a security is downgraded, the Finance Director will use discretion in determining whether to sell or hold the security based on its current maturity, the economic outlook for the issuer, and other relevant factors.

If a decision is made to retain a downgraded security in the portfolio, its presence in the portfolio will be monitored and reported quarterly to the City Council.

Authorized Securities and Transactions	Maximum	Portfolio
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CA. Gov't. Code Section	Authorized Investment	Maximum Maturity	Authorized Investment Limits - % of Portfolio	Credit Rating Limit
53601 (a)	City of Campbell Local Agency Bonds	5 years	None/10% Per Issuer	A/A-1 or Higher
53601 (c)	State Obligations	5 years	None/10% Per Issuer	A/A-1 or Higher
53601 (e)	California Local Agencies	5 years	None/10% Per Issuer	A/A-1 or Higher
53601(b)	United States Treasuries	5 years	None	None
53601(e)	Federal Agency Securities	5 years	75%	None
53601(e)	Federal Instrumentality	5 years	75%	None
53691(i)	Repurchase Agreements	1 year	10%	A-1/A
53601(g)	Prime Commercial Paper	270 days	25% 10% Per Issuer	A/A-1 or higher
53601(f)	Eligible Bankers Acceptances	180 days	10% per issuer/30% Aggregate	A-1/P-1/F-1
53601(j)	Medium Term Notes	5 years	30%	AA/Aa2/AA
53601(n)	Non-negotiable Certificates of Deposit	5 years	25% \$1 million per issuer	-

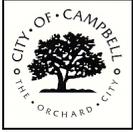


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CA. Gov't. Code Section	Authorized Investment	Maximum Maturity	Authorized Investment Limits - % of Portfolio	Credit Rating Limit
53601.8 (a)-(h)	Certificates of Deposit through Account Registry Services	5 years	7.5% Aggregate Maximum Up to the FDIC Insured Limit Per Issuer	-
16429.1	State of California LAIF	18 Months-Avg	None	-
53601(k)	*Mutual Funds	None	15%	AAAm/Aaa/AAAV1+
53601(k)	*Money Market Mutual Funds	None	15%	AAAm/Aaa/AAAV1+
53601(o)	Asset-Backed, Mortgage-Backed, Mortgage Pass-Through Securities, and Collateralized Mortgage Obligations	5 years	20%	AA or higher
53601(q)	Supranationals	5 years	30%	AA or higher
	*Combined total not to exceed 20% per State		20%	



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EXHIBIT A

GLOSSARY OF ELIGIBLE INVESTMENTS

Local Agency Investment Fund (L.A.I.F.). The L.A.I.F. was established by the state of California to enable treasurers to place funds in a pool for investments. There currently is a limitation of \$40 million per agency subject to a maximum of 15 total transactions per month. The City of Campbell uses this fund when interest rates are declining as well as for short-term investments and liquidity.

U.S. Treasury Bills. Commonly referred to as T-Bills, these are short-term marketable securities sold as obligations of the U.S. Government. T-Bills do not accrue interest but are sold at a discount to pay face value at maturity.

U.S. Treasury Notes. These are marketable, interest-bearing securities sold as obligations of the U.S. Government with original maturities of one to ten years. Interest is paid semi-annually.

U.S. Treasury Bonds. These are the same as U.S. Treasury Notes except they have original maturities of ten years or longer.

U.S. Government Agency Issues. Are securities that are unconditionally backed by the full faith and credit of the United States, including: Government National Mortgage Association (GNMA), Farmers Home Administration (FmHA), Small Business Administration (SBA), General Services Administration (GSA), Federal Housing Administration (FHA) and Housing and Urban Development (HUD).

U.S. Government Instrumentality Issues. Are government sponsored enterprises that are backed by the creditworthiness of the issuing agency, not the full faith and credit of the U.S. government. They do carry an implied guarantee of government assistance to the organization should it encounter financial difficulties. Issuers include: Federal National Mortgage Association (FNMA), Federal Home Loan Bank (FHLB), Federal Farm Credit Banks (FFCB) and Federal Home Loan Mortgage Corporation (FHLMC).

Asset Backed Securities. - Securities that are supported by pools of assets, such as installment loans or leases, or by pools of revolving lines of credits. Asset-backed securities are structured as trusts in order to perfect a security interest in the underlying assets.

Banker's Acceptance. This is a negotiable time draft (bill of exchange) with a maturity of six months or less drawn on and accepted by a commercial bank. Banker's Acceptances are usually created to finance the import and export of goods, the shipment of goods within the United States and storage of readily marketable commodities. Per State Law, cities may not invest more than 30% of idle cash in Banker's Acceptances.

Certificate of Deposit (CD's). - is a receipt for funds deposited in a bank or savings and loan association for a specified period of time at a specified rate of interest. The first \$250,000 of a certificate of deposit is guaranteed by the Federal Deposit Insurance Corporation (FDIC). CD's with a face value in excess of \$250,000 can be collateralized by Treasury Department Securities, which must be at least 110% of the face value of the CD's, in excess of the first \$250,000, or by first mortgage loans which must be at least 150% of the face value of the CD balance in excess of the first \$250,000.

Repurchase Agreements (REPOS). - is a contractual arrangement between a financial institution, or dealer, and an investor. This agreement normally can run for one or more days. The investor puts up his funds for a certain number of days at a stated yield. In return, he takes a given block of securities as collateral. At maturity, the securities are repurchased and the funds repaid plus



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interest.

Commercial Paper. - Notes are unsecured promissory notes of industrial corporations, utilities and bank holding companies. State law limits a city to investments in United States corporations having assets in excess of five hundred million dollars with an "A" or higher rating. Per State law, cities may not invest more than 25% of idle cash in commercial paper.

Medium Term Notes. - are corporate or depository institution debt securities meeting certain minimum quality standards (as specified in the California Government Code) with a remaining maturity of five years or less.

Money Market Mutual Fund. - Mutual funds that invest solely in money market instruments (short-term debt instruments, such as Treasury bills, commercial paper, bankers' acceptances, repos and federal funds).

Mortgage Backed Securities. - Mortgage-backed securities (MBS) are created when a mortgagee or a purchaser of residential real estate mortgages creates a pool of mortgages and markets undivided interests or participations in the pool. MBS owners receive a prorata share of the interest and principal cash flows (net of fees) that are "passed through" from the pool of mortgages. MBS are complex securities whose cash flow is determined by the characteristics of the mortgages that are pooled together. Investors in MBS face prepayment risk associated with the option of the underlying mortgagors to pre-pay or payoff their mortgage. Most MBS are issued and/or guaranteed by federal agencies and instrumentalities (e.g., Government National Mortgage Association (GNMA), Federal National Mortgage Association (FNMA), and Federal Home Loan Mortgage Corporation (FHLMC)).

Mortgage Pass-Through Obligations. - Securities that are created when residential mortgages (or other mortgages) are pooled together and undivided interests or participations in the stream of revenues associated with the mortgages are sold.

Mutual Fund. - An investment company that pools money and can invest in a variety of securities, including fixed-income securities and money market instruments. Mutual funds are regulated by the Investment Company Act of 1940 and must abide by strict Securities and Exchange Commission (SEC) disclosure guidelines.

Supranationals. - International institutions formed by two or more governments that transcend boundaries to pursue mutually beneficial economic or social goals. There are three supranational institutions that issue obligations that are eligible investments for California local agencies: the International Bank for Reconstruction and Development (IBRD), International Finance Corporation (IFC), and InterAmerican Development Bank (IADB).