



INVESTMENT POLICY STATEMENT
TEXAS ECONOMIC STABILIZATION INVESTMENT FUND
(TE-STIF)

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CHAPTER I. GENERAL INFORMATION

SECTION 1.

FUND BACKGROUND & PURPOSE

The Texas Economic Stabilization Investment Fund was created pursuant to Section 404.0241 of the Government Code in order to invest the assets of the economic stabilization fund.

SECTION 2.

FUND ADMINISTRATION:

Comptroller of Public Accounts and Texas Treasury Safekeeping Trust Company

The Texas Treasury Safekeeping Trust Company (“Trust Company”) shall hold and invest the TESTIF for the Texas Comptroller of Public Accounts (CPA). The Trust Company shall adopt an investment policy appropriate for the TESTIF and present it to the Comptroller’s Investment Advisory Board (“CIAB”). In accordance with Section 404.0241 of the Government Code and CIAB procedures, the Trust Company shall submit the investment policy to the CIAB and the Comptroller. The Comptroller is the sole officer, director, and shareholder of the Trust Company and charged with managing the company. The Comptroller has delegated management and investment related duties to the Chief Executive Officer and the Chief Investment Officer of the Trust Company.

Texas Treasury Safekeeping Trust Company Investment Committee

The Trust Company Investment Committee (“Investment Committee”) is responsible for oversight of Trust Company investment portfolios including: reviewing and recommending investment policies; approving certain investments; establishing strategic and tactical investment plans; evaluating and recommending the selection or dismissal of investment managers; reviewing quarterly portfolio performance; and reviewing and approving portfolio rebalancing and tactical asset allocation.

Investment committee members include: Chief Investment Officer (Chair), Chief Financial Officer, General Counsel, Director of Risk & Quantitative Analytics, General Investment Consultant, Chief Executive Officer (non-voting) and Compliance Officer (non-voting, Secretary). The Investment Committee shall review this Investment Policy Statement (“Policy”) as needed and recommend necessary changes, if any, to the CIAB and the Comptroller.

Asset Valuation Committee

The Trust Company Asset Valuation Committee is responsible for establishing and monitoring the accounting and financial process for determining the fair value measurements and disclosures included in the Trust Company’s financial statements.

The Committee is also responsible for reviewing the valuation methods including significant valuation assumptions, the computed asset valuation, and the presentation and disclosure of the fair value measurements and disclosures used in the financial statements. The Chief Financial Officer serves as chair for the Committee.

CHAPTER II. FUND INVESTMENT OBJECTIVES & EXPECTATIONS

SECTION 1.

FUND INVESTMENT OBJECTIVES

The Trust Company shall invest the Fund in accordance with Section 404.0241(a) of the Government Code, the prudent investor standard. It will consider only those investments appropriate for the TESTIF given its purpose and the potential for distribution requirements.

SECTION 2.

PERFORMANCE EXPECTATIONS

The fund will have two primary performance objectives: 1) maintaining purchasing power; and 2) delivering returns in excess of short-term cash equivalents. Maintaining the Fund's purchasing power means achieving net returns over a full market cycle that exceed inflation by at least the total expenses of managing and investing the fund. Inflation will be measured using the annualized growth rate of the national Consumer Price Index - Urban (CPI-U) published by the Federal Bureau of Labor Statistics.

The investment performance of the Fund and each investment strategy will be measured and compared to the stated benchmarks by an independent third party and reported quarterly to the Comptroller, Investment Committee and CIAB. In addition, the performance of the Fund will be compared to a customized composite of the sub-strategy performance benchmarks weighted by target allocation percentages as set out in Appendix A and as the portfolio is actually allocated.

Allocation targets, investment strategies and associated benchmarks may change as more information regarding the impact to Texas' credit rating and liquidity requirements are determined.

CHAPTER III. RISK MANAGEMENT & EXPECTATIONS

SECTION 1.

RISK TOLERANCE

A certain amount of risk must be assumed in order to achieve the Fund's investment objective. The nature of the Fund means that moderate interim fluctuations in portfolio market values and rates of return can be tolerated in seeking to achieve the investment objective. Diversification is the primary tool for managing overall portfolio risk. Asset allocation guidelines and the investment strategy structure will ensure adequate diversification to control the volatility of the overall portfolio.

The total Fund and each sub-strategy are expected to meet or exceed the total return performance objectives and risk-adjusted performance of the established benchmarks over a market cycle. Although performance expectations are established for a market cycle, performance and risk analysis will be conducted on an ongoing basis.

SECTION 2.

RISK MONITORING

Risk limits will be established for the total Fund and each major strategy. Fund and Strategy portfolio exposures and risk metrics will be regularly monitored. Although risk metrics will be measured and reviewed quarterly, evaluation will focus on a full market cycle.

The Fund will be reviewed at least quarterly, focusing on:

- > Comparison of performance results to benchmarks;
- > Comparison of risk metrics to expectations;
- > Characteristics and multi-factor exposure analysis;
- > Economic scenario and stress analysis;
- > Analysis of liquidity for the Fund and each Strategy;
- > Size of positions among individual investments, strategies, or sub-strategies; and
- > Opportunities available in relevant markets.

The overall risk of the fund will primarily be managed through investing in a diversified mix of fixed income strategies with varying styles, liquidity terms, volatility objectives, credit quality, and return expectations. Where appropriate, other complementary strategies may be utilized to further diversify the Fund's risk factors and enhance its overall return potential.

SECTION 3.

LIQUIDITY EXPECTATIONS

The Fund will remain predominantly liquid allowing for a nearly complete liquidation of the fund assets during any biennium.

SECTION 4.

DIVERSIFICATION EXPECTATIONS

- Excluding the Treasury Pool, exposure to any investment firm will generally be limited to no more than 25% of Fund assets.
- Fund investments will generally not exceed more than 25% of any firm's total assets under management (AUM).

SECTION 5.

DUE DILIGENCE

Prior to investing Fund assets, proper due diligence will be conducted by Trust Company staff and/or its Consultants. Due diligence results will be presented to the Trust Company Investment Committee as part of the review and approval process for any investment manager. Trust Company staff or its Consultants will meet with a representative of each external Investment Manager in person and on-site, as appropriate.

CHAPTER IV. INVESTMENT STRATEGIES & MANAGERS

SECTION 1.

INVESTMENT STRATEGY

The investment strategy will strike a balance between the competing needs of ensuring sufficient liquidity and generating enhanced investment returns to meet performance objectives.

The Fund will be invested in a diversified mix of fixed income investment strategies that, when combined as a portfolio are expected to produce the required returns of the program, while striving for reduced volatility. Asset types to be included in the Fund will be determined primarily by the Fund's volatility and liquidity limitations.

The Fund will be implemented using a mix of strategies that are:

- > *Highly correlated* with the strategy benchmark and are invested primarily in assets consistent with the assets included in the strategy benchmark.
- > *Less correlated* with the strategy benchmark and may be invested in assets that are not included in the strategy benchmark.

SECTION 2.

INVESTMENT MANAGERS

The term "Investment Managers" includes any firm selected by the Trust Company that is responsible for investing Fund assets. Fund assets will be managed primarily by external investment firms and advisors but may be managed directly by Trust Company investment staff. Both separate accounts and commingled vehicles (e.g., mutual funds, limited partnerships, common trust funds, exchange traded funds) may be employed. Investment Managers are expected to act in an ethical manner and with integrity in all aspects of the investment process.

Each Investment Manager has discretion to determine the mix of assets appropriate for the strategy approved by the Trust Company. To generate competitive risk adjusted returns, investment managers may be authorized to use varied approaches - investing not only in long and short positions, but also owning multiple asset classes (e.g., stocks, bonds, and currencies) and derivative instruments (e.g., futures, options, swaps).

Internal Investment Management

Certain investment positions may be managed by Trust Company staff. All transactions will be fully documented by the authorized individual executing the trade and confirmed by an independent member of the Investment Committee.

SECTION 3.

FIXED INCOME STRATEGIES

Cash is equivalent to the 90-Day U.S. Treasury Bill, which is auctioned weekly by the U.S. Treasury and is considered a risk-free investment. The performance is represented by the Federal Reserve H.15 report on Constant Maturity Treasury - 3 Month.

Fixed Income strategies are expected to generate relatively consistent positive returns with lower correlation to the public equity markets. Strategies selected are intended to provide positive returns during most economic and capital market environments. Allocations will be made to strategies that are predominantly fixed income securities, or derivatives of such, both long and short. Investment positions may be rate or credit spread sensitive and may be directional or hedged. Investment strategies utilized will include exposures to investment grade that are more rate sensitive along with credit strategies that are more spread sensitive. Strategies may include exposures to U.S. and non-U.S. sovereigns, corporates, structured notes, and asset-backed instruments.

Alternative Fixed Income strategies are intended to achieve consistently positive returns with prudent levels of risk. The primary objective is to be a fixed income replacement and achieve a long-term total return competitive with the public fixed income markets with low sensitivity to the equity markets.

Performance & Risk Expectations: While the particular vehicle's governing legal documentation will contain the specific guidelines for each offering, the following measures of performance, risk management and diversification will apply to the composite portfolio over a full market cycle:

- Total return is expected to meet or exceed the HFRI FOF: Conservative Index;
- Portfolio expected to exhibit beta less than 0.3 to the MSCI ACWI IMI Net Index;
- The portfolio will be formally reviewed at least semi-annually by the Trust Company staff and its consultants;
- The portfolio will be diversified by manager, strategy, geography, & sector focus; and
- Certain holdings will be identified as a "position capped strategy" based on the criteria outlined below and will be subject to a maximum position size of no more than 2% of the Fund's market value at any given time. These positions will be communicated to and recorded by the Chief Compliance Officer. In the event such a strategy exceeds 2% for two consecutive quarters, the position will be rebalanced back below the threshold at the next available redemption period.
 - Actual or anticipated rolling beta to the MSCI ACWI IMI Net Index that exceeds 0.5.
 - High leverage or maximum potential loss as defined by the Director of Risk & Quantitative Analytics.
 - Other unique factors as deemed appropriate solely by the Chief Investment Officer.

APPENDIX A. ASSET ALLOCATION TARGETS AND BENCHMARKS

<i>Asset Class</i>	<i>Strategy Description</i>	<i>Typical Liquidity</i>	<i>Benchmark</i>	<i>Allocation Range</i>	<i>Target</i>
<i>Cash</i>	Stable Value, AAA Rated	Daily	90-Day T-Bill	25-100%	25%
<i>Fixed Income</i>	Absolute Return	Daily / Monthly	Bloomberg Barclays 1-5 Year U.S. Credit Index	20-60%	40%
	Unconstrained rates and credit	Daily / Monthly	Bloomberg Barclays U.S. Universal Bond Index	0-50%	25%
<i>Alternative Fixed Income</i>	Long/short relative value and multi strategy	Monthly / Quarterly	HFRI FoF Conservative Index	0-25%	10%

Benchmark Descriptions

90-Day T-Bill: The 90-Day U.S. Treasury Bill is auctioned weekly by the U.S. Treasury and is considered a risk-free investment. The performance is represented by the Federal Reserve H.15 report on Constant Maturity Treasury - 3 Month.

Bloomberg Barclays 1-5 Year U.S. Credit Index: This benchmark is a subset of the full U.S. Credit Index, and measures the performance of investment grade, U.S. dollar denominated, fixed-rate, taxable corporate and government-related bonds with maturity of 1-5 years. The index includes both U.S. and non-U.S. corporates, alongside certain non-corporate issuers including non-U.S. agencies, sovereigns, supranationals and local authorities. Exclusions include private placements (144A), Eurobonds, floating rate securities, or bonds with less than \$250 million in outstanding par value. The Index has an inception date of January 1, 1976.

Bloomberg Barclays U.S. Universal Bond Index: The U.S. Universal Bond Index represents the union of the U.S. Aggregate Index, U.S. Corporate High Yield Index, Investment Grade 144A Index, Eurodollar Index, U.S. Emerging Markets Index, and the non-ERISA eligible portion of the CMBS Index. The index covers USD-denominated taxable bonds that are rated either investment grade or high-yield.

HFRI FoF Conservative Index: Hedge Fund Research, Inc., Fund of Funds classified as "Conservative" seek consistent returns by primarily investing in funds that generally engage in strategies such as Equity Market Neutral, Fixed Income Arbitrage and Convertible Arbitrage with relatively low volatility. Index return is net of manager fees.