

Section:	FB-4 Finance and Business Services	Approval Date:	7/29/2016
Policy:	FB-4.5 Investments	Latest Revision:	2/3/2023

FB-4.5 Investments

It is the policy of the Association that the Investment Subcommittee, through the Finance Committee, will provide recommendations to the Board for the investing of Association funds pursuant to the conditions and restrictions herein. This Investment Policy Statement establishes the policies and guidelines for three distinct investment pools: a short-term investment fund, a medium-term investment fund, and a long-term investment fund (the “Accounts”) and is intended to assist the Finance Committee (the “Committee”) in effectively selecting, monitoring and evaluating investment alternatives utilized in the Accounts. Specifically, this Investment Policy Statement:

- Establishes an investment plan for ACWA. which correlates with cash flow needs, funding activities, and both short-term and long-term investment goals.
- Defines the roles and responsibilities of those responsible for the Plan’s investment options.
- Establishes the benchmarks and guidelines against which performance will be evaluated.
- Defines the investment risk appetite and establish written guidelines on how funds may be invested.

This Statement is intended to be dynamic in nature. The Committee will review this document on an intermittent basis and revise it to reflect changing benchmarks, goals, capital market conditions and spending initiatives. The Committee will evaluate the performance of the investments over a complete market cycle and rolling multi-year time periods.

4.5.1 Investment Authority

The Executive Director/Secretary and Controller/Treasurer will have the full authority to invest funds in accordance with this policy. A separate investment report showing a minimum of, if applicable, the investment type, issuing institution, date of purchase, date of maturity, cost, yield, current value and maturity value will be maintained by the Executive Director/Secretary and Controller/Treasurer and made available to the Board on a quarterly basis.

4.5.2 General Provisions and Objectives

There are three separate accounts covered under this investment policy.

The purpose of this policy for the short-term and medium- term investment fund is to ensure the investment of Association funds is accomplished in a safe and secure manner, particularly with respect to limiting exposure of the Association to unnecessary risk. It is to provide for adequate liquidity to cover expenditures and other obligations as they occur. Funds not required for immediate expenditure will be invested in compliance with this policy. Criteria for selecting investments and the absolute order of priority are safety, liquidity, and yield. Investments will be made in a range of instruments and maturity

dates to ensure diversification and liquidity of assets in the event of an emergency or when a large cash outlay is necessary. The time horizon for the short-term investment fund is 2 years or less. The time horizon for the medium-term investment fund is less than five years.

The purpose of this policy for the long-term investment fund is to generate long-term investment growth consistent with the overall market, including equities. The time horizon for the long-term investment fund is greater than five years.

4.5.3 Policies for the Short-Term and Medium-Term Investment Funds

4.5.3.1 Safety of Principal

Safety of principal is the foremost objective of the Association. Each investment transaction will seek to ensure that capital losses are avoided, whether from securities default, broker-dealer default, or erosion of market value. The Association will seek to preserve principal by mitigating the two types of risk: credit risk and market risk.

4.5.3.1.1 Credit Risk

Credit risk, defined as the risk of loss due to failure of the issuer of a security, will be mitigated by investing in investment grade securities and by diversifying the investment portfolio so that the failure of any one issuer does not unduly harm the Association's capital base and cash flow.

4.5.3.1.2 Market Risk

Market risk, defined as market value fluctuations due to overall changes in the general level of interest rates, will be mitigated by limiting the average maturity of the Association's investment portfolio to one year for short-term funds and a maximum maturity of five years for medium-term funds.

4.5.3.2 Liquidity

Historical cash flow trends are to be compared to current cash flow requirements on an ongoing basis in an effort to ensure that the Association's investment portfolio will remain sufficiently liquid to meet all reasonably anticipated operating requirements. All investments should be laddered for maximum liquidity.

4.5.3.3 Return on Investment

Maximizing the return on investment is of utmost importance. Tying a benchmark to a specific index is difficult due to volatile market conditions; therefore, the objective is to seek the highest level of return consistent with the risk tolerance of the authorized investment vehicles stated in this policy.

4.5.3.4 Prudent Investor Standard

The investment process will recognize that the investment portfolio is subject to the prudent investor standard and will seek to act responsibly as fiduciary of Association members. Investments will be made with the care, skill, prudence, and diligence under the circumstances then prevailing, including, but not limited to, the general economic conditions and the anticipated needs of the Association, that a prudent person acting in a like capacity and familiar with those matters would use in the conduct of funds of like aims, to safeguard the principal and maintain the liquidity needs of the Association. In a diversified

portfolio, occasional measured losses may be inevitable and must be considered within the context of the overall portfolio's return and the cash flow requirements of the Association.

4.5.3.5 Authorized Investments

The Association's approved investments are as follows:

1. Certificates of Deposit representing a deposit of funds at a commercial bank or credit union for a specified period of time and for a specified return at maturity. Eligible Certificates of Deposit will be issued by a nationally or state chartered bank or a state or federal association whose senior debt obligations are rated "AAA" or equivalent by Standard & Poor's or Moody's. The full amount of the principal and interest that may be accrued during the maximum term of each Certificate of Deposit will at all times be insured by the Federal Deposit Insurance Corporation or the National Credit Union Administration, or fully collateralized.
2. Instruments fully guaranteed by the Federal Government, such as Treasury Bills, Notes, etc.
3. Savings Account or Money Market Account fully insured by the Federal Deposit Insurance Corporation, or fully collateralized.
4. Authorized Investment Institutions.
 - a. State of California Local Agency Investment Fund (LAIF)
 - b. CalTrust

4.5.3.6 Investment Funds

There will be two investment funds, operating/short-term and medium-term, as detailed below:

1. Operating/Short-term Investment Fund
These are funds expected to be spent in the normal course of business during the current budget cycle. Authorized funds are all those specified in Policy 4.5.3.5.
2. Medium-term Investment Fund
These are funds not required to meet the immediate needs of the Association. The maturities on the Medium-term Fund will be limited to five years or less. Authorized funds are all those specified in Policy 4.5.3.5.

4.5.3.7 Oversight, Monitoring and Review

The short-term and medium-term investment portfolios will be managed in accordance with the parameters specified within this policy. The objective of the portfolio should be to obtain a stable rate of return taking into consideration economic constraints commensurate with the investment risk and cash flow requirements. Portfolio performance should be compared to appropriate benchmarks on a regular basis as determined by the Controller/Treasurer.

This investment policy will be reviewed annually by the Investment Subcommittee for any necessary revisions.

4.5.4 Policies for the Long-Term Investment Fund

4.5.4.1 Asset Class Guidelines

Long-term investment performance is primarily a function of asset class mix. In choosing which asset classes should be included in the Accounts, the Committee weighs the long-term performance and risk characteristics of the asset category. Historically, while interest-generating investments, such as bonds, have the advantage of relative stability of principal value, they provide little opportunity for real long-term capital growth due to their susceptibility to inflation. On the other hand, equity investments, such as common stocks, clearly have a significantly higher expected return but have the disadvantage of much greater year-by-year variability of returns.

Even more important than an investment's standalone performance and risk characteristics is its potential to enhance the overall risk-return profile of the portfolio.

The following asset classes may be included in the long-term Account's overall asset allocation strategy:

Cash or Cash Equivalents	
Money Market	
Bonds	
Ultrashort Bond	Bank Loans
Short-Term Government / Bond	High Yield Bond
Intermediate-Term Government / Bond	Convertibles
Long-Term Government / Bond	International Bonds
Inflation-Protected Bond	Emerging Markets Debt
Multisector Bond	Non-Traditional Bonds
Domestic Equity	
Large Cap (Value / Blend / Growth)	Small Cap (Value / Blend / Growth)
Mid-Cap (Value / Blend / Growth)	
International Equity	
Foreign Large Cap (Value / Blend / Growth)	Small-Value, Small Blend, Small Growth
Foreign Small-Mid Cap (Value / Blend / Growth)	Diversified Emerging Markets
Global Equity	
World Stock	
Non-Traditional	
Absolute Return	Multi-alternative
Commodity	Real Estate (US / Global)

4.5.4.2 Investment Objectives

The investment objective of the Long-Term Account is to generate growth and income to fund future programs and expenses of ACWA within an acceptable, established risk tolerance.

4.5.4.2.1 Long-Term Account

1. **Time Horizon:** 5 years or greater
2. **Risk:** Moderate, growth oriented
3. **Acceptable Investments:** index/mutual funds, collective investment trusts (CITs), ETFs
4. **Liquidity:** The Account should be fully invested as long-term cash holdings will tend to reduce long-term rates of return.

Subject to any statutory or regulatory limitations, investment alternatives will be publicly available mutual funds, index funds, exchange traded funds, or similar vehicles. Investments being offered will fluctuate in value with market conditions and, when redeemed, may be worth more or less than the amount originally invested. Each of the offered investment alternatives will be designed to follow a specific stated investment objective.

4.5.4.3 Selection of Investments

In selecting the investments for the Accounts, the Committee may consider a variety of quantitative and qualitative factors. These factors may include but are not limited to the investment option's investment objectives, performance relative to its index and peer group, risk characteristics, investment style, fees, manager tenure.

The Committee also anticipates each investment will be examined with the objective of determining if it appropriately complements the overall diversification and risk and return parameters of the Accounts.

ACWA, with the assistance of the Investment Consultant, will review the Investment Policy and monitor each investment on an ongoing basis. ACWA and the Consultant will periodically evaluate the investment results of the investments.

Each investment is evaluated on an ongoing basis using several measures that quantify the expenses, returns and risk-adjusted performance of each fund within its peer group.

Each investment is reviewed at least annually against its peer group and benchmark index to determine the performance and quality of each offering. Each is evaluated using the following criteria:

- a. Trailing one-, three-, five-, and ten-year returns
- b. Rolling 12-month returns (five years)
- c. Batting Average
- d. Sharpe Ratio (five years)
- e. Alpha (five years)
- f. Up Capture Ratio (ten years)
- g. Down Capture Ratio (ten years)
- h. Style Consistency to the appropriate index (R-Squared)
- i. Expense Ratio

As noted in Appendix B, each fund is benchmarked to a specific market index, and fund performance is evaluated and compared to a relevant peer group using Morningstar category classifications.

In addition to the quantitative methodology described above, many qualitative criteria and possible warning signs are monitored in order to highlight a fund's potential exposure to risk that may make it unsuitable as an investment. The warning signs may include (but are not limited to):

- a. Above-average operating expenses
- b. Above-average style drift (as determined by returns-based and holdings-based analyses)
- c. High degrees of portfolio concentration among individual holdings
- d. High degrees of portfolio concentration among economic sectors
- e. Above-average performance volatility
- f. Above-average portfolio turnover
- g. Below-average Alpha
- h. Below-average manager tenure and/or above-average turnover
- i. Rapid fund size growth
- j. Significantly positive and negative cash flows
- k. Unusual levels of corporate scrutiny; poor public perception
- l. For bond portfolios, very low average credit quality relative to peers
- m. For bond portfolios, significantly above- or below-average portfolio duration
- n. Recent changes to or concerns with the firm structure / ownership
- o. Recent changes to or concerns with the corporate management team structure

As a general guideline, subject to any further delegation to an investment consultant or investment manager, the Committee should consider following the below procedure:

Whenever the average ranking score for an investment alternative is in the 3rd quartile based on the Investment Consultant's scoring system, except as previously noted for index funds or funds that are not scored, it should be placed on the Watch List. The alternative will be monitored and remain on the Watch List for four consecutive quarters, even if its performance improves. If the alternative remains in the 3rd quartile for four consecutive quarters, a detailed review of the alternative should be made and a recommendation to replace or retain the alternative should be presented to the Committee. The alternative may be reviewed sooner at the Committee's discretion.

Whenever an investment alternative falls into the 4th quartile based on the Investment Consultant's scoring system, a detailed review of the alternative should be made as soon as possible or at the next investment subcommittee meeting, and a recommendation to replace or retain the alternative should be presented. Any actions will be reported at the next scheduled Finance Committee meeting.

Investment alternatives that fail to meet qualitative criteria (i.e.: manager changes, fund company reorganizations, strategy changes) will be put on the Watch List by the Committee.

4.5.4.4 Investment Monitoring Criteria

The ongoing monitoring of investment options should be a regular process. It is the mechanism for revisiting the investment options selected and verifying that the criteria originally satisfied continues to be satisfied within an acceptable range. Each investment is evaluated on an ongoing basis using several measures that quantify the expenses, returns and risk-adjusted performance of each fund within its

peer group. Each investment is reviewed at least annually against its peer group and benchmark index to determine the performance and quality of each offering.

The Committee may remove an investment option if they determine that such removal is in the best interests of the Accounts, taking into account the relevant factors including the fund's current and potential future performance as well as market conditions.

The Committee shall have the discretion to establish, modify, amend, or adjust acceptable performance measurement standards by which each investment is to be evaluated.

Final selection, replacement and/or removal of an investment shall be completed only after conducting a thorough review of the identified investment alternative.

4.5.4.5 Proxy Voting

All voting of proxies is to be done in a timely manner by the Investment Managers.

Review and Revisions

The Committee reserves the right to amend the Investment Policy Statement at any time it deems such amendment to be necessary or to comply with changes in applicable law, as these changes affect the investment of the Plan's assets. Until revised or amended by the Committee, the Investment Policy Statement shall remain in effect.

References:

Previous Board Policy G.5.

See Administrative Procedure: To be determined.

Revision History:

Revision Date	Description of Changes	Requested By
7/29/2016	Initial Release	ACWA Staff and Finance Committee
7/28/2017	Policy renumbered from FB-4.2 to FB-4.5 for organizational purposes within the section.	ACWA Staff and Governance Workgroup
11/22/2019	Minor edits to Policies FB-4.5, FB-4.5.1, and FB-4.5.2.3 to fine-tune policy language.	ACWA Staff and Finance Committee.
6/4/2021	Revised Policy 4.5.1 Investment Authority to delete reference to the Director of Finance and Business Services and replace with updated language.	ACWA Staff based on organizational changes approved by the Executive Committee and Board of Directors, effective January 2021.

Revision Date	Description of Changes	Requested By
6/4/2021	Revised Policy 4.5.5 Oversight, Monitoring and Review to delete reference to the Director of Finance and Business Services and replace with updated language.	ACWA Staff based on organizational changes approved by the Executive Committee and Board of Directors, effective January 2021.
2/3/2023	Comprehensive revision of Policy FB-4.5 Investments to incorporate provision to help increase the long-term return on investments.	ACWA Staff and Finance Committee

APPENDIX A – Asset Allocation

The broad asset class allocation target and range for the long-term Account is:

Asset Class	Strategic Target	Permitted Range
Equities/Growth	60%	50-80%
Bonds/Stability	40%	20-50%
Cash	0%	0-30%

The committee will determine, update, and monitor specific fund allocations during quarterly or semi-annual investment reviews. Rebalancing will take place at least annually and occur if the broad asset class allocations vary more than 5% from target allocations. Taxes and transaction costs will be evaluated to determine if rebalancing should take place.

APPENDIX B – Asset Category, Peer Group Universe, Benchmark/Index

Investment categories are defined based on their Morningstar category classifications, which also serve as the peer groups against which investment are assessed. The following list of investment categories and their corresponding benchmarks which may be used in the investment alternative evaluation process, includes but is not limited to:

Investment Alternative Category	Benchmark/Index	APPENDIX B
Money Market-Taxable	ICE Bank of America Merrill Lynch 3-Month T-Bill Index	
Bond		
Ultrashort Bond	Bloomberg Barclays US Govt/Credit 1-3 Yr TR USD	
Short-Term Bond	Bloomberg Barclays US Govt/Credit 1-3 Yr TR USD	
Short Government	Bloomberg Barclays Government 1-5 Yr TR USD	
Intermediate Government	Bloomberg Barclays US Govt/Mortgage TR USD	
Intermediate Core Bond	Bloomberg Barclays US Agg Bond TR USD	
Intermediate Core-Plus Bond	Bloomberg Barclays US Agg Bond TR USD	
Long Government	Bloomberg Barclays US Government Long TR USD	

Investment Alternative Category	Benchmark/Index	APPENDIX B
Long-Term Bond	Bloomberg Barclays US Govt/Credit Long TR USD	
Inflation-Protected Bond	Bloomberg Barclays US Treasury US TIPS TR USD	
Corporate Bond	Bloomberg Barclays US Credit TR USD	
Multisector Bond	Bloomberg Barclays US Agg Bond TR USD	
High Yield Bond	Bloomberg Barclays US HY 2% Issuer Cap TR USD	
World Bond	Bloomberg Barclays Global Aggregate TR USD	
Emerging Markets Bond	JPM EMBI Global TR USD	
Nontraditional Bond	Wilshire Liquid Alts TR	
Large Cap		
Large Value	Russell 1000 Value TR USD	
Large Blend	S&P 500 Index Russell 3000 Index CRSP U.S. Total Market Index	
Large Growth	Russell 1000 Growth TR USD	
Mid-Cap		
Mid-Cap Value	Russell Mid Cap Value TR USD	
Mid-Cap Blend	Russell Mid Cap TR USD S&P Mid Cap 400 Index MSCI U.S. Mid Cap 450 Index CRSP U.S. Mid Cap Index S&P Completion Index DJ US Completion Total Stock Market Index	
Mid-Cap Growth	Russell Mid Cap Growth TR USD	
Small-Cap		
Small Value	Russell 2000 Value TR USD	
Small Cap Blend	Russell 2000 TR USD	