

MANAGEMENT'S DISCUSSION AND ANALYSIS

The Washington State Treasurer's Office provides the Management's Discussion and Analysis of the Local Government Investment Pool's (LGIP) Comprehensive Annual Financial Report (CAFR) for readers of the financial statements. This overview and analysis of the LGIP's financial activity is for the fiscal year ended June 30, 2012. Please read this analysis in conjunction with the letter of transmittal and the financial statements that follow.

Financial Highlights

- The LGIP reported net assets as of June 30, 2012, in the amount of \$8.8 billion.
- The LGIP earned \$16 million for pool participants as a result of investment activity during the year. This was a decrease of \$7 million from the previous year.

Overview of the Financial Statements

The LGIP invests in a portfolio of securities in a manner generally consistent with Rule 2a-7 money market funds, as currently recognized by the Securities and Exchange Commission. Rule 2a-7 funds are limited to high quality obligations with limited maximum and average maturities in order to minimize both market and credit risk. Investments are reported on a trade date basis in accordance with generally accepted accounting principles (GAAP). This is based on the assumption that governments face custodial risk in connection with sold investments up to the date of settlement and face no custodial risk in association with purchases recorded on the balance sheet prior to the settlement date. This report consists of the Statement of Net Assets, Statement of Changes in Net Assets, Notes to the Financial Statements, and the Schedule of Investments and Deposits. In addition, this CAFR also contains supplementary and statistical information to aid the reader in further understanding the financial position of the LGIP and the results of its operation for the fiscal year ended June 30, 2012. The following is a description of the basic financial statements:

Statement of Net Assets - The Statement of Net Assets presents all of the LGIP's assets and liabilities, with the difference between the two reported as net assets. It also provides information on the types of investments held by the LGIP.

Statement of Changes in Net Assets – The Statement of Changes in Net Assets presents information on how the net assets changed during the fiscal year. Additions consist of the contributions from participants and investment income. Deductions consist of distributions to participants and administrative expenses.

Notes to the Financial Statements - The Notes to the Financial Statements serve to describe the LGIP as a reporting entity and to further clarify its financial activity as reported in the financial statements.

Financial Analysis

To gain an understanding of the financial position of the LGIP, the reader should examine the financial statements as a whole, rather than in isolation from one another. This will provide a more comprehensive picture of the activity.

A summary of the LGIP's net assets is presented below:

Table 1
Net Assets
(expressed in millions)

	2012	2011	Dollar Change	Percent Change
Pooled cash and investments	\$ 9,320.4	\$ 9,385.1	\$ (64.7)	(0.7) %
Receivables	1.1	1.9	(.8)	(42.1)
Total Assets	9,321.5	9,387.0	(65.5)	(0.7)
Liabilities	491.4	0.0	491.4	---
Net Assets	\$ 8,830.1	\$ 9,387.0	\$ (556.9)	(5.9) %

As the table shows, the LGIP experienced a decrease in net assets of \$556.9 million in 2012. Total assets were lower and liabilities were higher compared to last year. The LGIP's Net Asset total is a function of several parameters, some of which are independent of the performance of the LGIP. The resulting change in net assets can best be explained simply by changes in deposits and withdrawals of the participants in the fund. Since the LGIP is a 100% voluntary investment option for local governments, participants may use the LGIP at their discretion. The percentage of total funds that individual participants have available for investment in the LGIP changes over time and can vary from near zero to 100%.

Table 2
Changes in Net Assets
(expressed in millions)

	2012	2011	Dollar Change	Percent Change
Contributions from Participants	\$ 16,479.6	\$ 17,578.1	\$ (1,098.5)	(6.2) %
Distributions to Participants	17,052.2	17,212.6	(160.4)	(0.9)
Net Investment Income	15.7	22.7	(7.0)	(30.8)
Change in Net Assets	\$ (556.9)	\$ 388.2	\$ (945.1)	(243.5) %

Total Investment Income less administrative expenses ("Net Investment Income") was down 30.8 percent over the previous year. This decrease was due to the decrease in portfolio yield, as presented in Table 3. Contributions and distributions decreased over the prior year. Due to the discretionary nature of the LGIP as an investment option, it is difficult to ascertain the reasons behind the changes in net assets, as discussed in the previous paragraph.

Table 3
Average Annualized Monthly Yield

	2008	2009	2010	2011	2012
LGIP Portfolio Yield	4.04%	1.59%	0.36%	0.23%	0.14%
iMoneyNet Inc.	3.25%	0.65%	0.03%	0.02%	0.01%
Targeted Fed Funds	3.74%	0.90%	0.00%- 0.25%*	0.00%- 0.25%*	0.00%- 0.25%*

* Since December 2008 the FOMC has maintained a range for the targeted fed funds rate between 0.00-0.25%.

The average annualized monthly yield represents the annualized percent return of LGIP investments based on the average invested balance for the month. Table 3 shows an average of the annualized monthly portfolio yields for each of the last five fiscal years. The average annualized monthly yields have shown a significant variation over the last five years. Those changes can be explained by the significant variation in the average level of the targeted Fed Funds rate during that time period. The targeted Fed Funds rate, which is the interest rate that banks charge each other for the use of funds, is set by the Federal Open Market Committee in an attempt to balance the competing forces of inflation and economic growth. Due to the short-term nature of the LGIP portfolio, and the types of investment that are utilized, the LGIP yields will closely follow the targeted Fed Funds rate.

The best measure of the LGIP's performance is not the change in the yield of the portfolio over time, but rather a comparison of the LGIP yield to the yield of its benchmark, iMoneyNet Inc., Government Only/Institutional Only Money Market Funds (formerly IBC Donoghue). This benchmark is comprised of privately managed money market funds similar in portfolio composition and investment guidelines to the LGIP. The LGIP net yield during Fiscal Year 2012 was 13 basis points higher than that of the benchmark. The LGIP continues to be a sound investment option for local governments, obtaining a competitive yield while preserving principal and liquidity.