

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, 2013. Please read this analysis in conjunction with the letter of transmittal and the financial statements that follow.

Financial Highlights

- The LGIP reported net position as of June 30, 2013, in the amount of \$10.6 billion.
- The LGIP earned \$18 million for pool participants as a result of investment activity during the year. This was an increase of \$2 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 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 Position, Statement of Changes in Net Position, Notes to the Financial Statements, and the Schedule of Investments and Deposits. 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. The following is a description of the basic financial statements:

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

Statement of Changes in Net Position - The Statement of Changes in Net Position presents information on how the net position 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 position is presented below:

Table 1
Net Position
(expressed in thousands)

	2013	2012	Dollar Change
Pooled cash and investments	\$ 10,634,213	\$ 9,320,476	\$ 1,313,737
Receivables	714	1,078	(364)
Total Assets	10,634,927	9,321,554	1,313,373
Liabilities	90	491,388	(491,298)
Net Position	\$ 10,634,837	\$ 8,830,166	\$ 1,804,671

As the table shows, the LGIP experienced an increase in net position of \$1,804.7 million in 2013. Total assets were higher and liabilities were lower compared to last year. The large liabilities decrease was the result of the decrease in obligation under securities lending agreements and investment trades pending payables totaling \$491.0 million. The LGIP's net position total is a function of several parameters, some of which are independent of the performance of the LGIP. The remaining change in net position 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 Position
(expressed in thousands)

	2013	2012	Dollar Change
Contributions from Participants	\$ 17,487,171	\$ 16,479,607	\$ 1,007,564
Distributions to Participants	15,700,259	17,052,244	(1,351,985)
Net Investment Income	17,759	15,735	2,024
Change in Net Position	\$ 1,804,671	\$ (556,902)	\$ 2,361,573

Total Investment Income less administrative expenses ("Net Investment Income") was up 12.9 percent over the previous year. This increase was primarily due to the increase in portfolio yield, as presented in Table 3. Contributions increased 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 position, as discussed in the previous paragraph.

Table 3
Average Annualized Monthly Yield

	2009	2010	2011	2012	2013
LGIP Portfolio Yield	1.59%	0.36%	0.23%	0.14%	0.17%
iMoneyNet Inc.	0.65%	0.03%	0.02%	0.01%	0.01%
Targeted Fed Funds	0.90%	0.00%- 0.25%	0.00%- 0.25%	0.00%- 0.25%	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 the fiscal year was 16 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.