

Nowhere to Run, Nowhere to Hide – Options for Short-Term Capital

AFP Winter Seminar– December 9, 2011

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WELLS CAPITAL MANAGEMENT



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Agenda

- Macro Economic Environment
- Corporate Investment Guidelines
- Investment Opportunities & Risks
- Questions & Comments



Macro Economic Environment

Current Environment



Current Environment

Financial Market Volatility

- Fall-out from 2008 crisis
- Threat of another market melt down
- U.S. Treasury yields at record lows
- Fears of a double-dip recession in the U.S. and Global economies
- Sovereign European debt problems
- S&P downgrade of the U.S. Government



Corporate Investment Guidelines

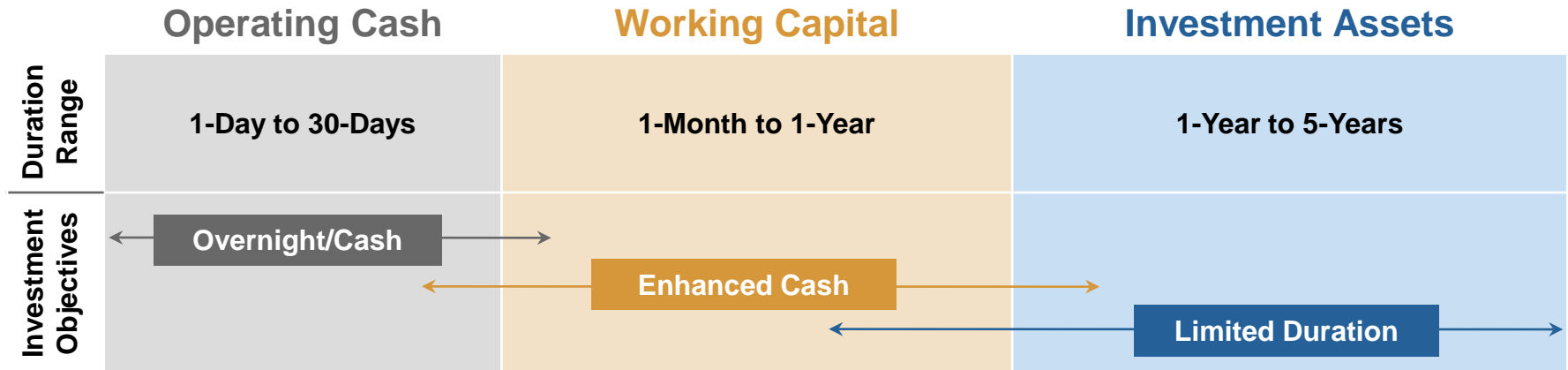
Understanding Your Organization

What are some unique investment guideline drivers:

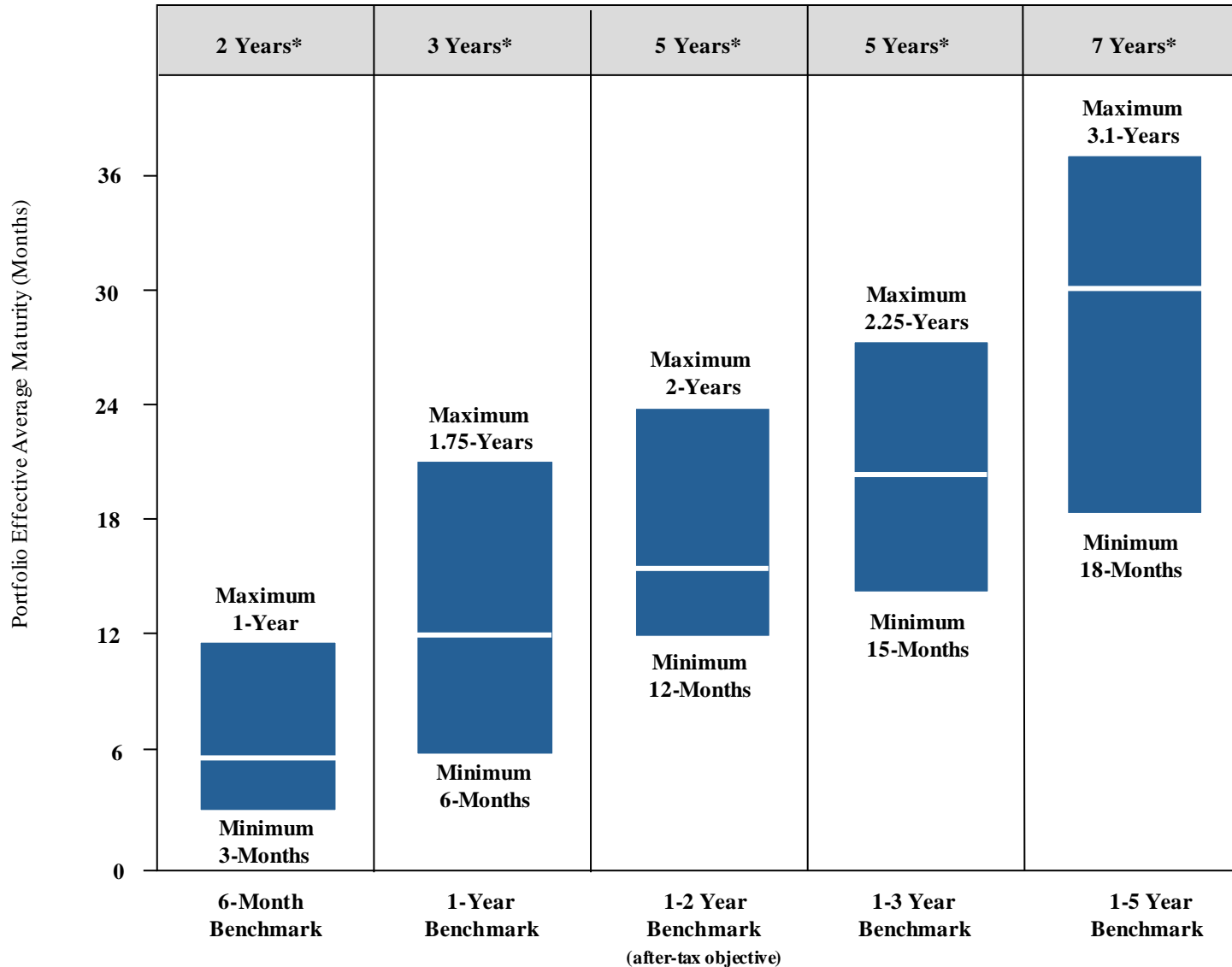
- Liquidity Needs
- Cash Flow Schedule
- Gain/Loss Sensitivity
- Accounting/Financial Statement Implications
 - Accounting Classification: FAS 115
 - Hold-to-Maturity
 - Available For Sale
 - EITF 03-01/FAS 115-1
 - FAS 157 and 157-4
 - FAS 95
 - GAS 40 and 45
- Credit Rating Sensitivity
- Shareholder Sensitivities and Expectations
- Unique Business Risks and Biases



Liquidity Tiers

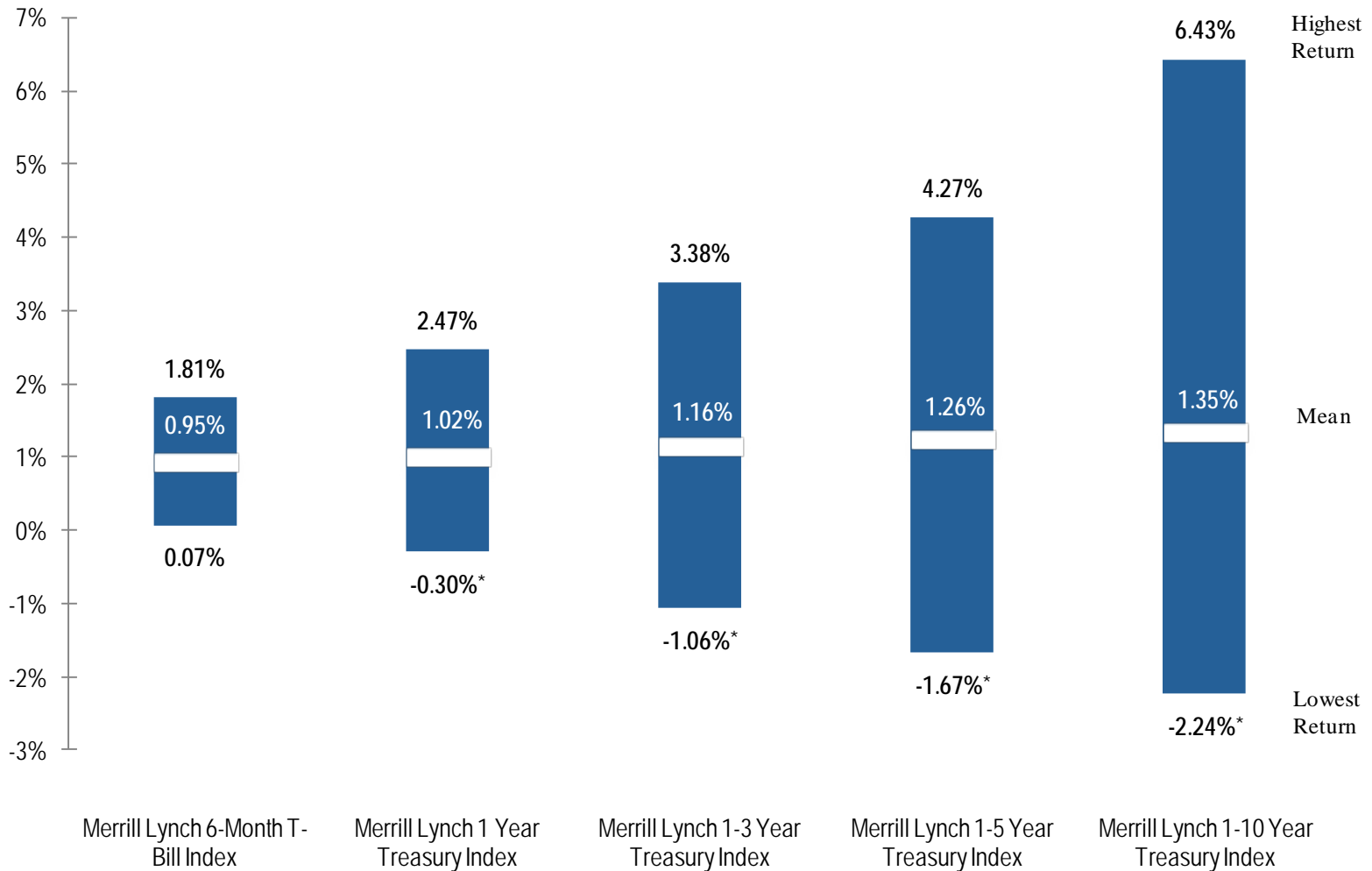


Maturity Constraints



Total Return For Quarterly Holding Periods

January 1994 - December 2010



*The 1994-2010 period includes three negative return periods for the 1 Year Index, six negative return periods for the 1-3 Year Index, fifteen negative return periods for the 1-5 Year Index, and twenty negative return periods for the 1-10 Year Index.
Source: Merrill Lynch and Bloomberg

Performance Benchmark

A performance benchmark should reflect:

- Organization's goals and objectives
- Risk tolerance
- Return expectations over the long run

Performance benchmark should be:

- Representative of the portfolio's duration/time horizon
- A meaningful measurement of investment performance vs. the market and/or alternative solutions
- Consistent across all managers with similar mandates
- Consistently calculated and obtained from a third party



Investment Policy Statement

Investment Objectives

- Preservation of principal
- High degree of liquidity
- Maximum “After Tax”, “Nominal”, “Total”, or “Book” return

Acceptable Investments (U.S. Dollar-Denominated Only)^{1,2}

- | | | |
|--|---|--------------------------------------|
| ➤ U.S. Treasury Securities | ➤ Money Market Funds/Sweep Vehicle | ➤ Municipal Notes/Bonds |
| ➤ Federal Agency Securities (GSEs) | ➤ Mortgage-Backed Securities | ➤ Municipal Variable Rate Securities |
| ➤ FDIC-Guaranteed Securities | ➤ Collateralized Mortgage Obligations | ➤ Pre-refunded bonds |
| ➤ Repurchase Agreements | ➤ Commercial Mortgage-Backed Securities | ➤ Tax-Exempt Commercial Paper |
| ➤ Commercial Paper (foreign and domestic issues) | ➤ Foreign Government Related Securities | ➤ Asset-Backed Securities |
| ➤ Corporate Notes/Bonds | ➤ Taxable Short-Term Municipal Debt | Certificates of Deposit |

Benchmark

Maturity Parameters

- Maximum Maturity/Demand Feature/Average Life:
- Maximum Average Maturity Deviation From Benchmark:

Concentration and Diversification

- No more than 5% in any single issue/issuer at the time of purchase (except U.S. Treasury and Agency securities).
- No more than 50% of the portfolio shall be invested in any single GSE/Federal Agency at the time of purchase.

Minimum Acceptable Credit Quality

- The obligor must be rated in the rating category as indicated below by at least two of the Nationally Recognized Statistical Rating Organizations (NRSRO).

	<u>S&P</u>	<u>Moody's</u>	<u>Fitch</u>
Minimum Short-Term Rating	A-1	P-1	F-1
Minimum Long-Term Rating	[A- or BBB-]	[A3 or Baa3]	[A- or BBB-]

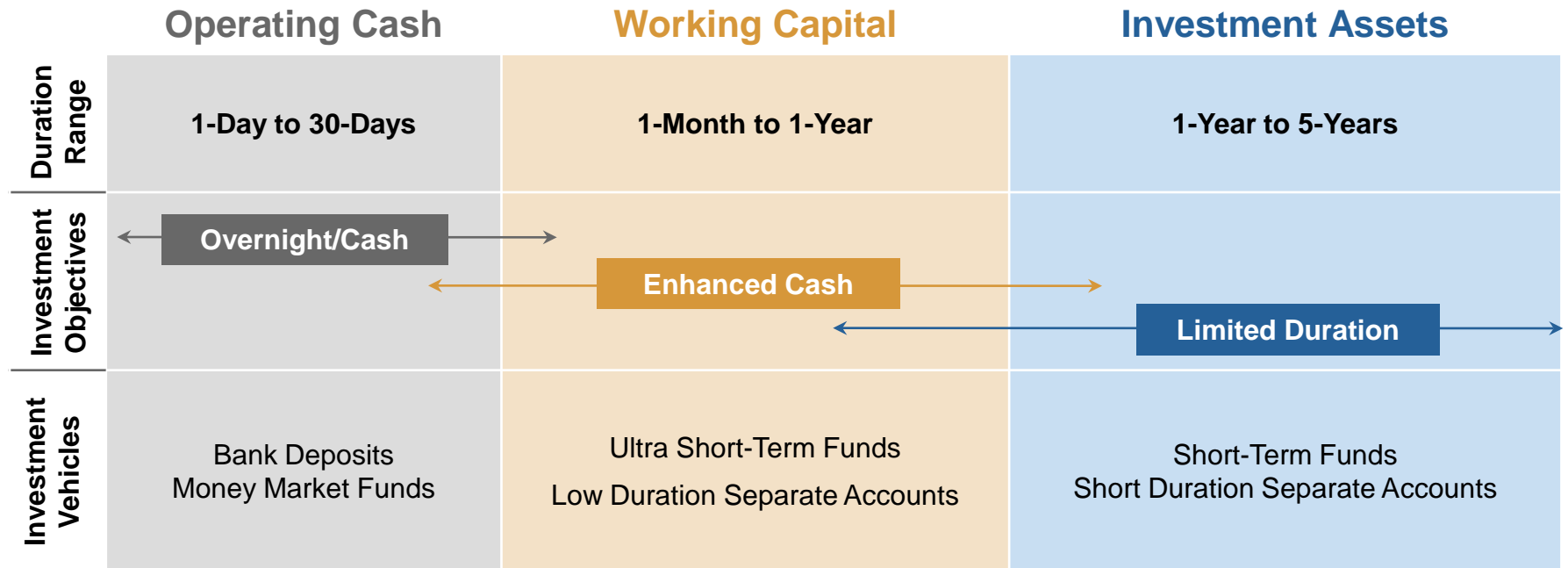
¹Non-rated and non-re-rated, pre-refunded issues may be purchased (collateralized by U.S. Treasuries and Agencies).

²Tax Status: 35% Federal Tax Rate; Securities subject to the Alternative Minimum Tax (AMT) may be purchased.



Investment Opportunities & Risks

Liquidity Tiers



Money Market Fund Flows

in Millions

Date	12/31/2010	9/30/2011	YTD Change	% Change
Category Avg/Total Current	Assets (dly)	Assets (dly)	Assets (dly)	
Prime Institutional	1,061,029.4	918,867.7	(142,161.7)	-13%
Prime Retail	544,974.4	530,181.5	(14,792.9)	-3%
Govt & Agencies Instit	382,609.0	349,743.3	(32,865.7)	-9%
Govt & Agency Retail	108,234.9	111,269.3	3,034.4	3%
Treasury & Repo Instit	150,603.8	180,262.0	29,658.2	20%
Treas & Repo Retail	18,592.4	17,386.4	(1,206.0)	-6%
Treasury Instit	114,386.4	136,244.7	21,858.3	19%
Treasury Retail	62,051.4	69,779.4	7,728.0	12%
T-F National Instit	114,940.5	87,548.8	(27,391.7)	-24%
T-F National Retail	124,560.6	116,642.5	(7,918.1)	-6%
T-F State Instit	15,161.8	13,094.1	(2,067.7)	-14%
T-F State Retail	74,763.7	69,281.4	(5,482.3)	-7%
	2,771,908.3	2,600,301.1	(171,607.2)	-6%
All Institutional	1,838,730.9	1,685,760.6	(152,970.3)	-8%
All Retail	933,177.4	914,540.5	(18,636.9)	-2%

Source: iMoneyNet

Managed Accounts

Buying Decision Priorities

- Investment Style
- Performance
- Philosophy and Process
- Risk/return profile
- Organization structure
- Fees



Trade Execution Example: Harnessing the Power of Competition

Example from August 2011: Sell \$3mm FHR 3597 ML

- FHR 3597 ML is a relatively liquid U.S. Government Agency CMO with a 2.6-year average life.
- In order to fully benefit from competitive forces we “cast a broad net” soliciting bids from 19 Broker-Dealers. Results are listed below:

Broker	Price	Broker	Price	Broker	Price	Broker	Price
Broker 1	no bid	Broker 6	104-13	Broker 11	105-05	Broker 16	105-30
Broker 2	no bid	Broker 7	104-16	Broker 12	105-05	Broker 17	106-00
Broker 3	no bid	Broker 8	104-27+	Broker 13	105-09	Broker 18	106-14
Broker 4	no bid	Broker 9	104-28	Broker 14	105-17	Broker 19	106-22
Broker 5	no bid	Broker 10	105-02	Broker 15	105-18		

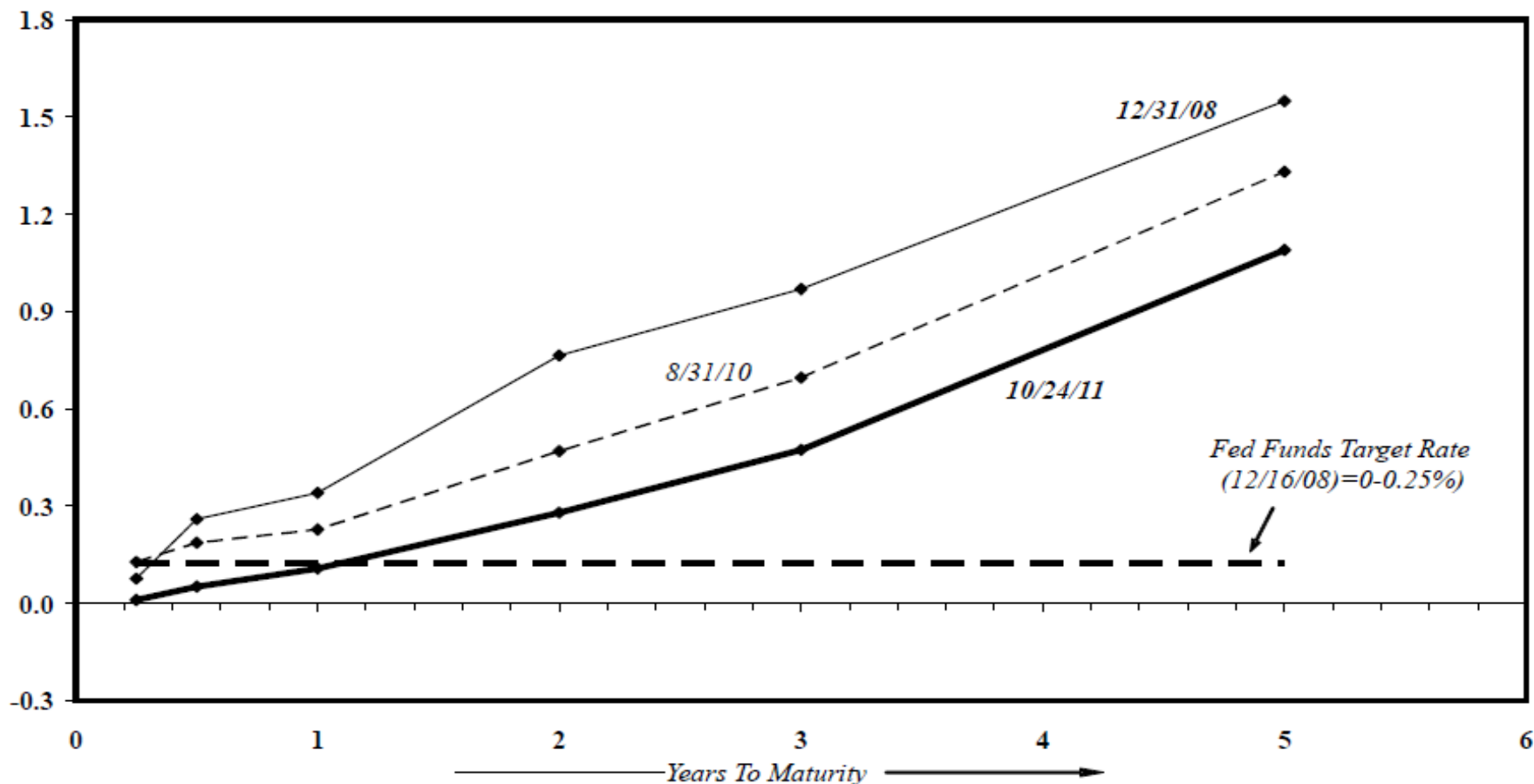
Takeaway: It is vital to locate the most aggressive bid on the Street because superior execution adds directly to the bottom line.

- The range of bids was \$2-09 which is worth \$68,438 for a \$3 million trade.
- The second best bid was a quarter point below the winning bid. Difference is worth \$7500.
- Over the course of a year, execution advantage alone can offset investment management fees.



Yield Curve

SHORT-TERM AND INTERMEDIATE YIELDS STILL BELOW THEIR "MELTDOWN" LOWS
The Treasury Yield Curve, Selected Periods; Yields In Percent



The Treasury "yield curve" (i.e., the path traced by interest rates at various maturities) has oscillated with the ebb and flow of the economy, and with associated inflation expectations, since this growth cycle began in mid-2009. Most recently, fears of a Europe-induced, financial upheaval and an associated "flight" to the safety of Treasury securities, have sent yields down below their low point during the 2008 "meltdown" at the end of that year: With economic "fundamentals" (e.g., growth and inflation) stronger now than they were then, yields are vulnerable to an increase once financial conditions in Europe calm.

Table of Short Duration Returns: A Case For Diversification

Annual Returns for Key Sector Indices – Taxable Equivalent

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
1	U.S. Corporates, 1-3 Years 9.59%	Mortgages 0-3 Years WAL 7.50%	U.S. Corporates, 1-3 Years 5.33%	Municipals 1-3 Years 3.41%	Municipals 1-3 Years 3.79%	Municipals 1-3 Years 5.81%	Municipals 1-3 Years 7.45%	Municipals 1-3 Years 7.93%	U.S. Corporates, 1-3 Years 14.69%	Mortgages 0-3 Years WAL 5.42%
2	Municipals 1-3 Years 8.87%	Municipals 1-3 Years 7.40%	Municipals 1-3 Years 4.28%	Mortgages 0-3 Years WAL 2.80%	Asset Backed Securities, 0-3 Years 2.60%	Asset Backed Securities, 0-3 Years 4.73%	U.S. Treasuries, 1-3 Years 7.32%	U.S. Agencies, 1-3 Years 7.05%	Asset Backed Securities, 0-3 Years 13.80%	U.S. Corporates, 1-3 Years 4.86%
3	U.S. Agencies, 1-3 Years 8.64%	U.S. Corporates, 1-3 Years 6.53%	Asset Backed Securities, 0-3 Years 2.74%	Asset Backed Securities, 0-3 Years 2.16%	Mortgages 0-3 Years WAL 2.15%	U.S. Corporates, 1-3 Years 4.71%	Mortgages 0-3 Years WAL 6.95%	U.S. Treasuries, 1-3 Years 6.61%	Municipals 1-3 Years 6.77%	Municipals 1-3 Years 3.53%
4	U.S. Treasuries, 1-3 Years 8.30%	U.S. Agencies, 1-3 Years 6.11%	U.S. Agencies, 1-3 Years 2.18%	U.S. Corporates, 1-3 Years 1.82%	U.S. Corporates, 1-3 Years 1.89%	Mortgages 0-3 Years WAL 4.64%	U.S. Agencies, 1-3 Years 6.74%	Mortgages 0-3 Years WAL 5.27%	Mortgages 0-3 Years WAL 5.98%	Asset Backed Securities, 0-3 Years 3.35%
5	Asset Backed Securities, 0-3 Years 8.16%	Asset Backed Securities, 0-3 Years 5.95%	U.S. Treasuries, 1-3 Years 1.90%	U.S. Agencies, 1-3 Years 1.18%	U.S. Agencies, 1-3 Years 1.77%	U.S. Agencies, 1-3 Years 4.52%	U.S. Corporates, 1-3 Years 5.67%	Asset Backed Securities, 0-3 Years -1.22%	U.S. Agencies, 1-3 Years 2.17%	U.S. Treasuries, 1-3 Years 2.35%
6	Mortgages 0-3 Years WAL 7.79%	U.S. Treasuries, 1-3 Years 5.76%	Mortgages 0-3 Years WAL 1.83%	U.S. Treasuries, 1-3 Years 0.91%	U.S. Treasuries, 1-3 Years 1.67%	U.S. Treasuries, 1-3 Years 3.96%	Asset Backed Securities, 0-3 Years 4.84%	U.S. Corporates, 1-3 Years -2.68%	U.S. Treasuries, 1-3 Years 0.79%	U.S. Agencies, 1-3 Years 2.32%

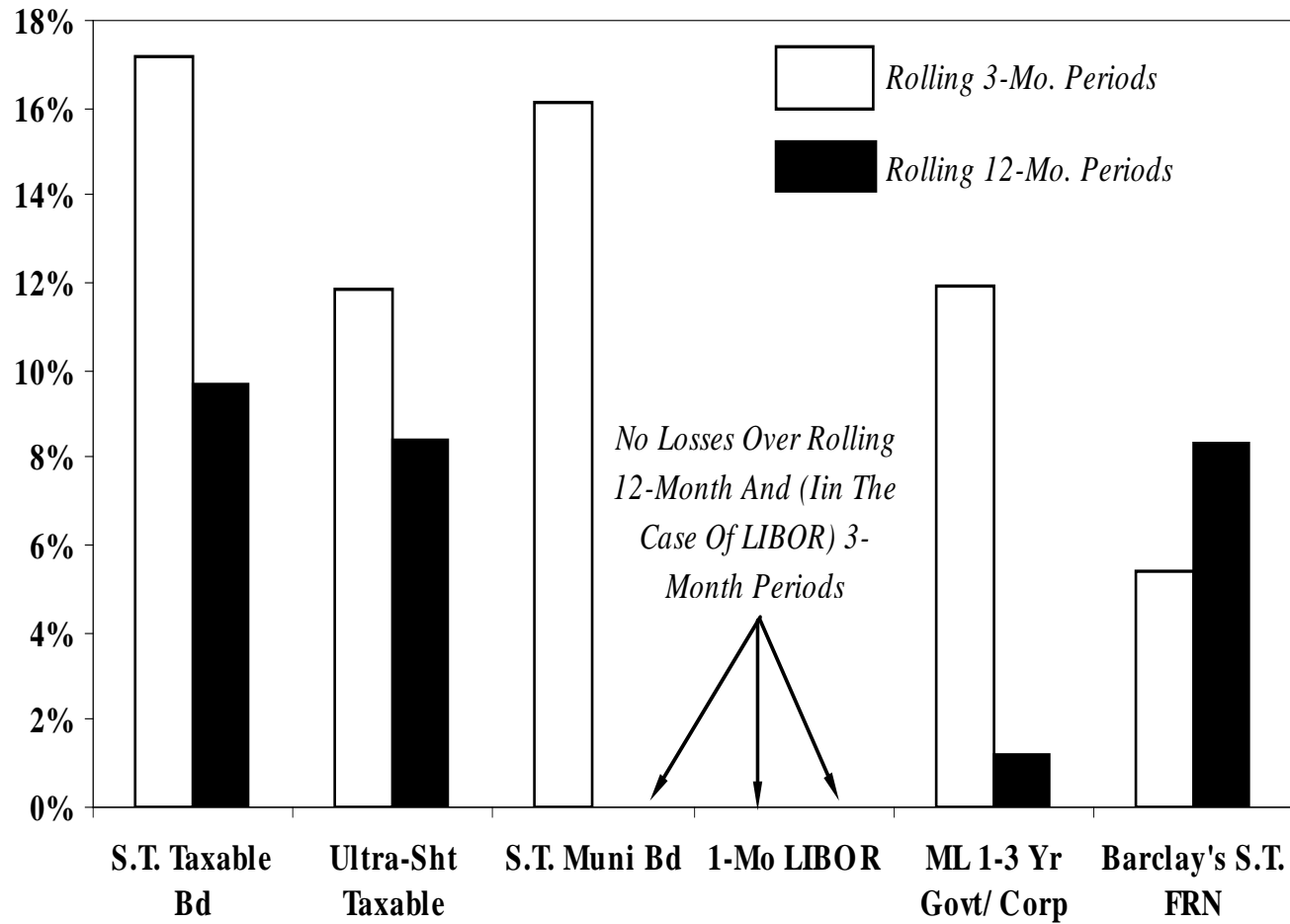
Source: Bloomberg

Returns shown are the annual total returns of select Merrill Lynch indices. This Periodic Table of Sector Returns is a comprehensive representation of relative sector performance for a 10-year period through 12/31/2010. Municipal index returns are presented as taxable equivalent returns, assuming a 35% tax rate. This material is offered compliments of Wells Capital Management to its clients. It is for your own personal information and we are not soliciting an action based upon it. Past performance is not indicative of future results.



Loss Incidence of Alternative Liquidity Investments

Percent Of Periods With Losses, December 2003-July or August 2011



Municipal Debt

Comparative Default Rates for Municipal and Corporate Debt

	Municipal (%)	Corporate (%)
AAA	0.00	1.09
AA	0.06	1.15
A	0.10	2.77
BBB	0.39	7.71
BB	2.04	20.52
B	8.84	34.54
CCC/C ²	41.45	56.55
Investment-Grade	0.15	3.83
Speculative-Grade	6.75	29.40

(15-Year Cumulative Default Rates)¹

- Historically, a BBB Municipal bond has a cumulative default rate less than a AAA Corporate bond.
- Credit decision is a large driver of the crossover investment decision.
- Credit fundamentals in the Municipal market supports attractive risk-adjusted returns.

¹For municipal defaults, S&P's study period was Jan. 1, 1986, to Dec. 31, 2010. For corporate defaults, S&P's study period was Jan. 1, 1981 to Dec. 31, 2010.

²Calculations include all ratings in the C category, from Caa/CCC to C/C.
Source: S&P

Questions & Comments

Thank You

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