

# NCCMT Cash & Term Overview

## NCLGIA Winter Conference

February 2016

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# Agenda

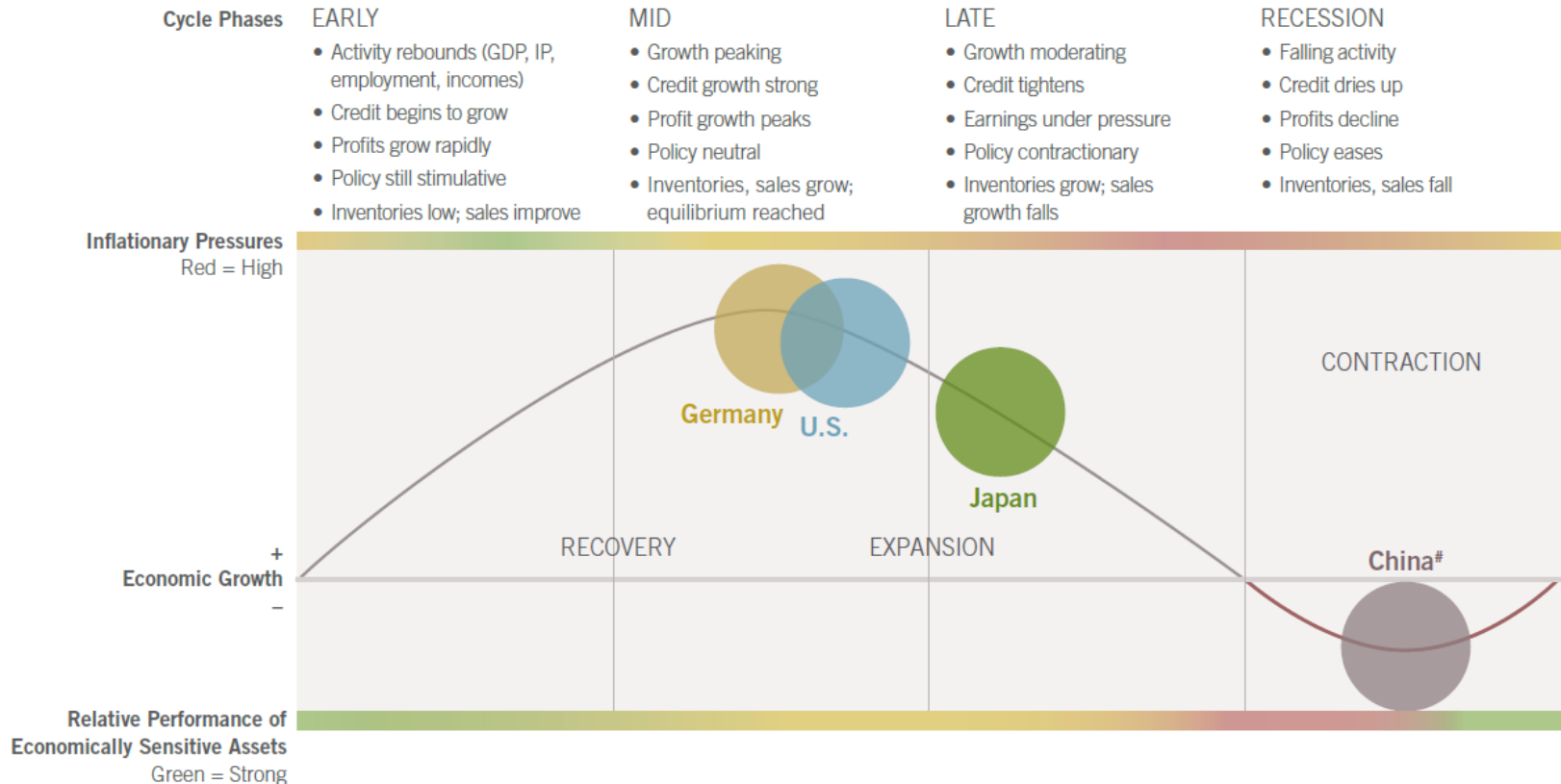
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1. Global Macro Update
2. Current Money Market Conditions
3. Regulatory Reform Update
4. Cash & Term Portfolio Overview
5. Question & Answer



# Global Macro Update

# Global Business Cycle in a Trend of Modest Improvement



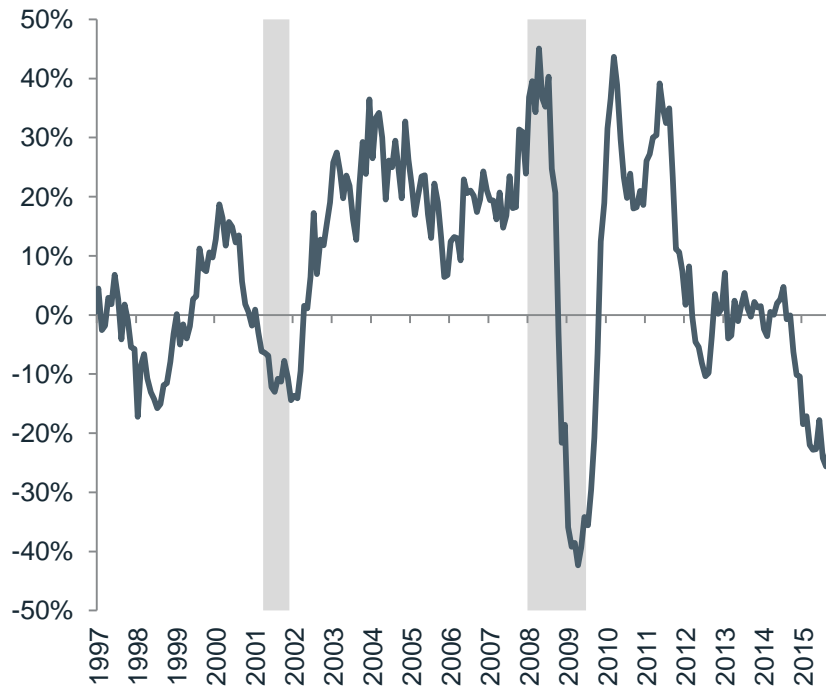
Note: The diagram above is a hypothetical illustration of the business cycle. There is not always a chronological, linear progression among the phases of the business cycle, and there have been cycles when the economy has skipped a phase or retraced an earlier one. #A growth recession is a significant decline in activity relative to a country's long-term economic potential. We have adopted the "growth cycle" definition for most developing economies, such as China, because they tend to exhibit strong trend performance driven by rapid factor accumulation and increases in productivity, and the deviation from the trend tends to matter the most for asset returns. We use the classic definition of recession, involving an outright contraction in economic activity, for developed economies. Source: Fidelity Investments (AART).

# Global Trade Slumped but Inventory Correction Mostly Over

## Global Export Growth

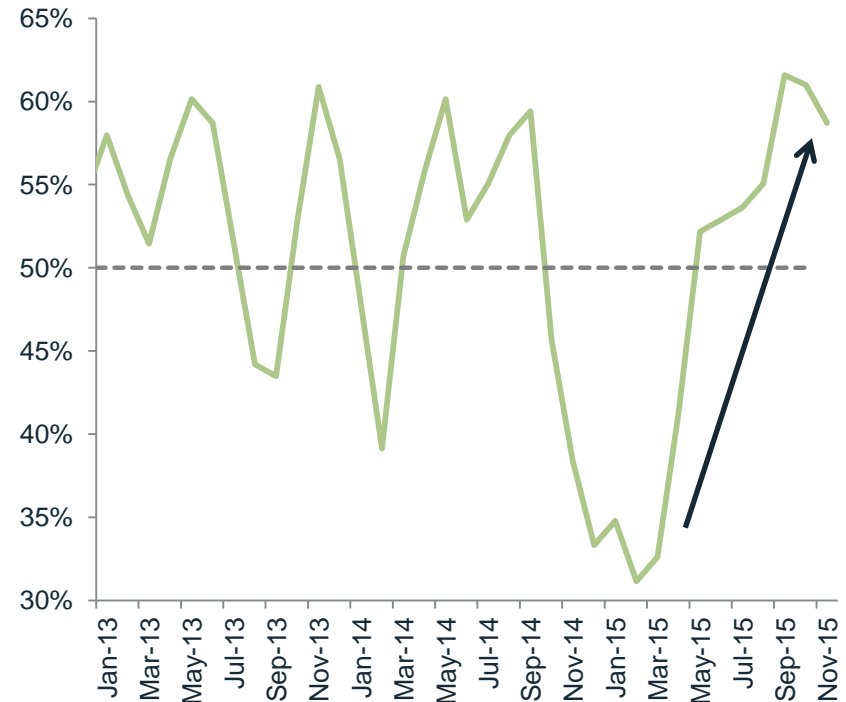
— Value of World Exports (\$)

Change (Year-Over-Year)



## U.S. Durable Goods Inventory-to-Shipment Ratio

— % of Industries with Improving I/S Ratio (3-Month Average)



**LEFT:** Grey area represents U.S. recession as defined by National Bureau of Economic Research (NBER). Export value in USD, adjusted for changes in currency. Source: International Monetary Fund, Haver Analytics, Fidelity Investments (AART), as of 10/31/15. **RIGHT:** Source: Census Bureau, Haver Analytics, Fidelity Investments (AART), as of 11/30/15.



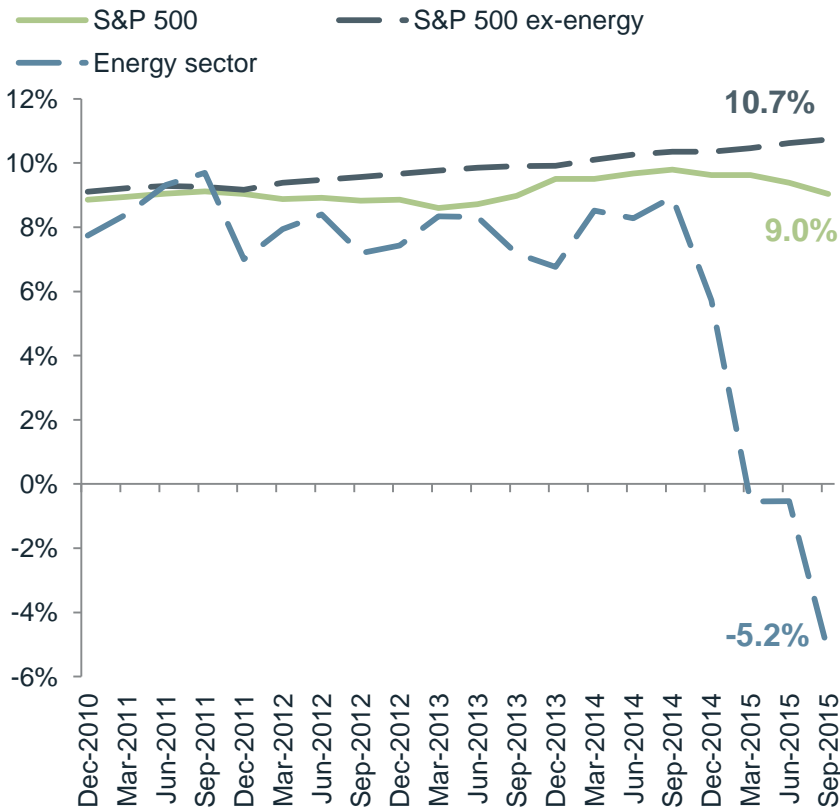


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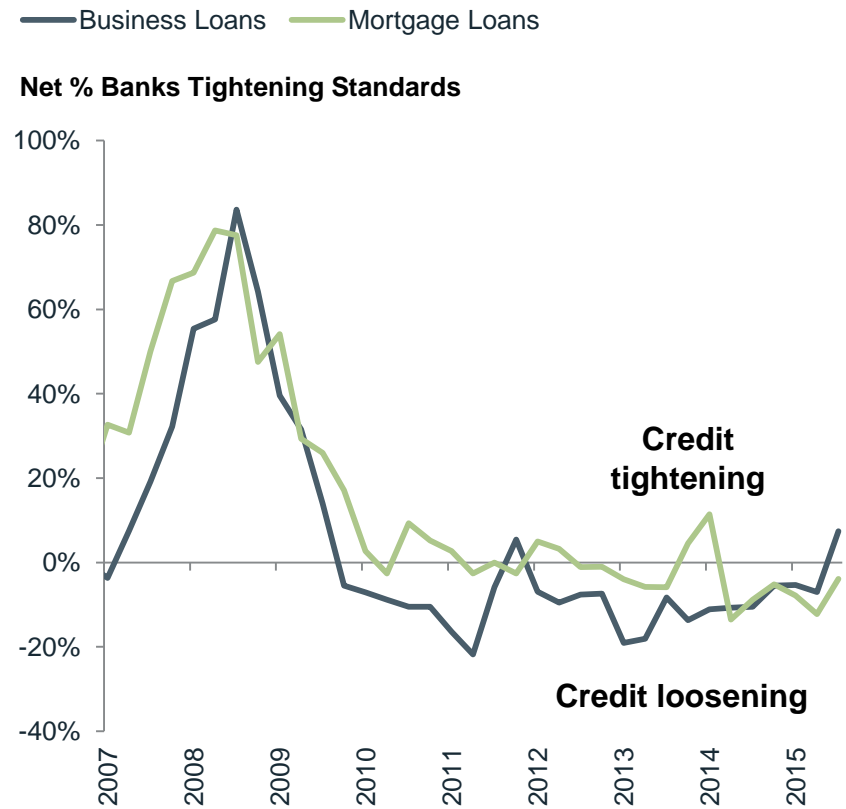


# Late-Cycle Signals Remain Generally Absent in U.S.

## S&P 500 Profit Margins



## Bank Lending Standards

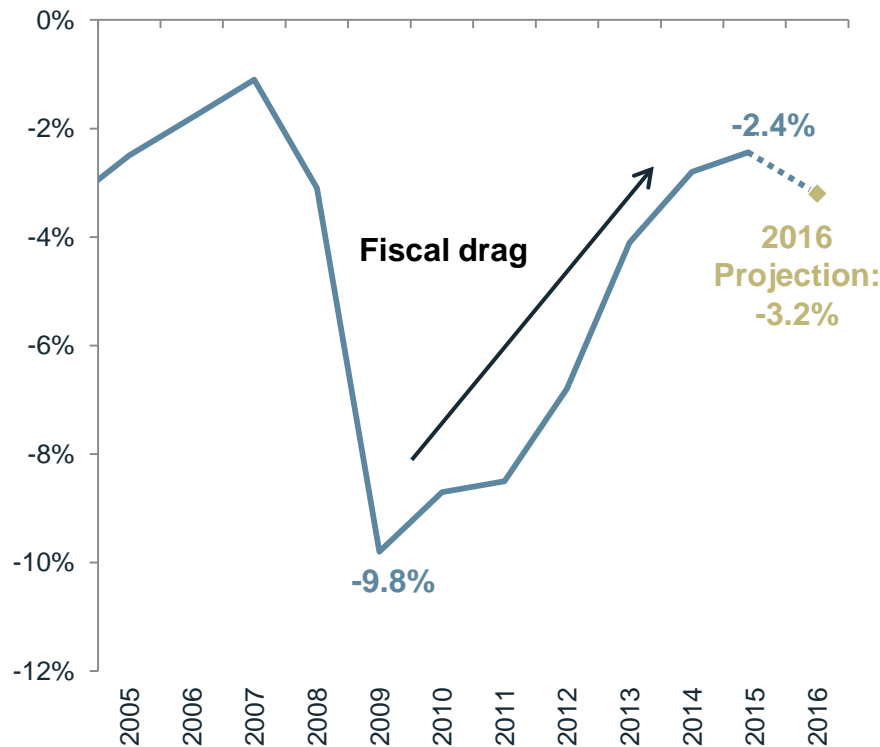


LEFT: Source: Standard & Poor's, FactSet, Fidelity Investments (AART), as of 9/30/15. RIGHT: Source: Federal Reserve, Haver Analytics, Fidelity Investments (AART), as of 11/2/15.

# Fed Hiked, but Global Policy Measures Are Mixed

## U.S. Fiscal Deficit

Percent of U.S. GDP



- Tightening
- Neutral
- Easing
- Extraordinary Easing

## Global Monetary Policy



LEFT: 2016 projection from Evercore ISI. Source: Congressional Budget Office, Evercore ISI, Haver Analytics, Fidelity Investments (AART), as of 12/31/15. RIGHT: Source: Bloomberg Finance L.P., Fidelity Investments (AART), as of 12/31/15.



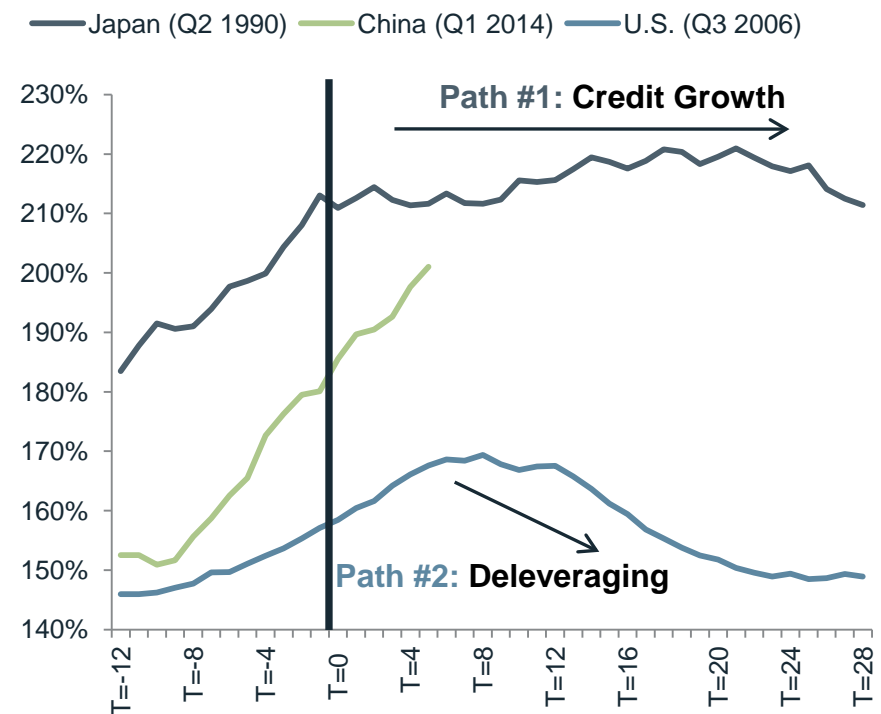
# China Following Japan's Playbook: Stimulus and Stability

China's Policy Easing	
Fiscal Policy	2016 budget deficit may be biggest ever
Monetary Policy	Broad-based easing
FX	Managed depreciation

## Post-Bubble Paths: 2 Choices

#1 Stabilization: Slow burn		#2 Restructuring: Rapid adjustment	
Example: Japan in 1990s	China Today	Example: U.S. in 2000s	
<b>Banking forbearance</b>	NPLs still only 1.6%	<b>Write off bad loans</b>	
<b>Maintain employment</b>	Stable unemployment at 4.1%	<b>Unemployment rises</b>	
<b>Corporate profits weak</b>	Industrial profits -2.0% YoY	<b>Profits sharply drop, then recover</b>	
<b>Construction activity weak</b>	Starts -15% YoY	<b>Construction plummets, then recovers</b>	

## Private Credit-to-GDP



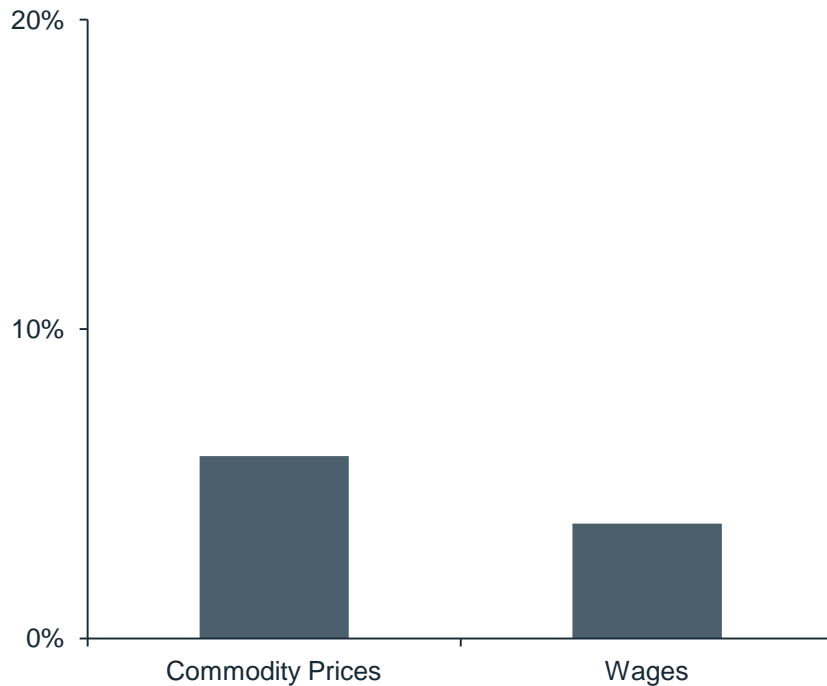
**LEFT:** NPL = Non-performing loan. Source: China Banking Regulatory Commission, China National Bureau of Statistics, Haver Analytics, Fidelity Investments (AART), as of 11/30/15. **RIGHT:** T=0 represents peak of home prices. Data are quarterly. Source: Bank for International Settlements, Cabinet Office of Japan, Organization for Economic Cooperation & Development, Haver Analytics, Fidelity Investments (AART), as of 11/30/15.



# Inflation Impulse is Typically Key to Late-Cycle Transition

## Mid-Cycle Inflation, 1966–2010

Average Annualized Inflation



### Improving macro conditions

- Profit growth solid / peaks
- Credit accessible / spreads narrow
- Monetary policy accommodative / neutralized

## Late-Cycle Inflation, 1966–2010

Average Annualized Inflation



### Deteriorating macro conditions

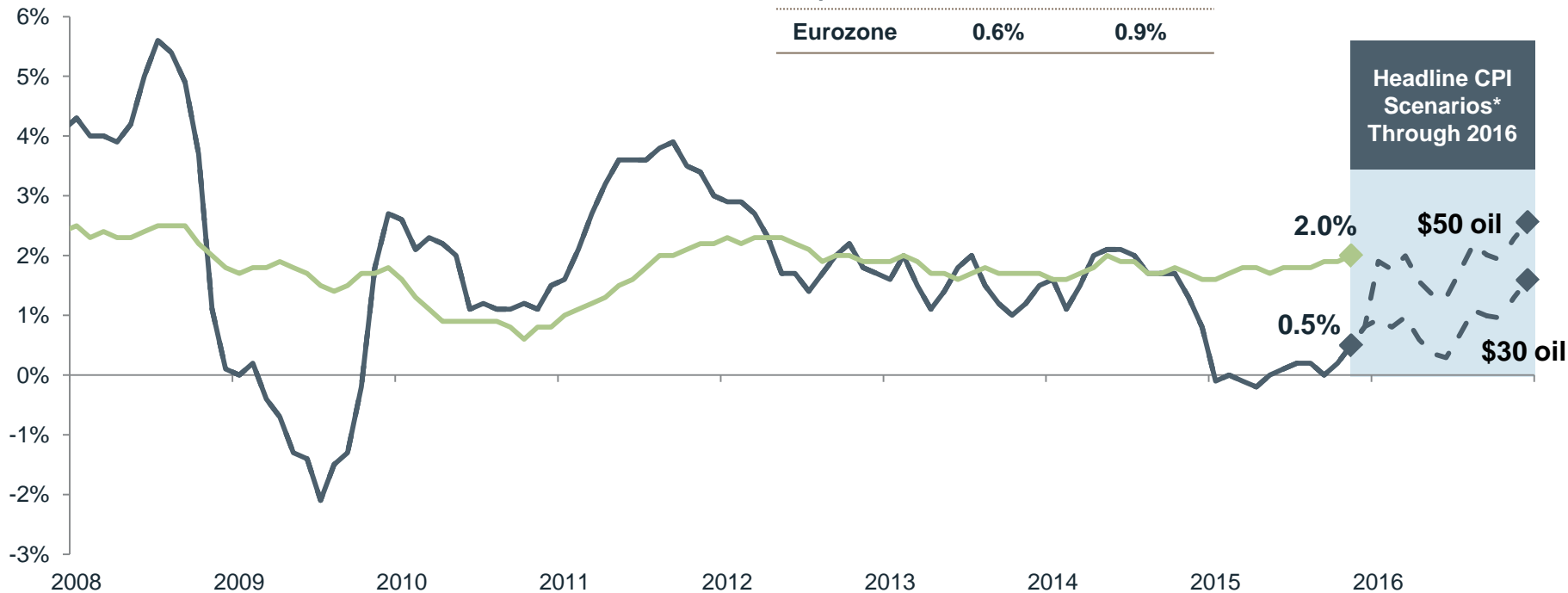
- Profit margins under pressure
- Credit tightens / spreads widen
- Monetary policy becomes restrictive

# Global “Base Effect” Likely to Lift Inflation in 2016

## U.S. Inflation: The Base Effect

— Headline CPI — Core CPI

Change (Year Over Year)



**CHART:** \*Scenarios assume core CPI and food cost growth rates remain constant and vary only by the cost of oil each month. Source: Bureau of Labor Statistics, Haver Analytics, Fidelity Investments (AART), as of 11/30/15. **TABLE:** Data shown are year over year. Japan low: April 2015. Eurozone low: March 2015. Source: Japan Ministry of Internal Affairs and Communications, Eurostat, Haver Analytics, Fidelity Investments (AART), as of 11/30/15.



# Outlook: Market Assessment

U.S. remains mid-cycle, supported by positive consumer outlook

Global macro environment stabilizing

Pace of Fed tightening will likely be gradual

## Asset Allocation Considerations

- Global macro stabilization should benefit developed-market risk assets
- Potential for upside inflation surprises not priced into asset markets
- Lower international equity valuations and wider credit spreads may provide more attractive opportunities

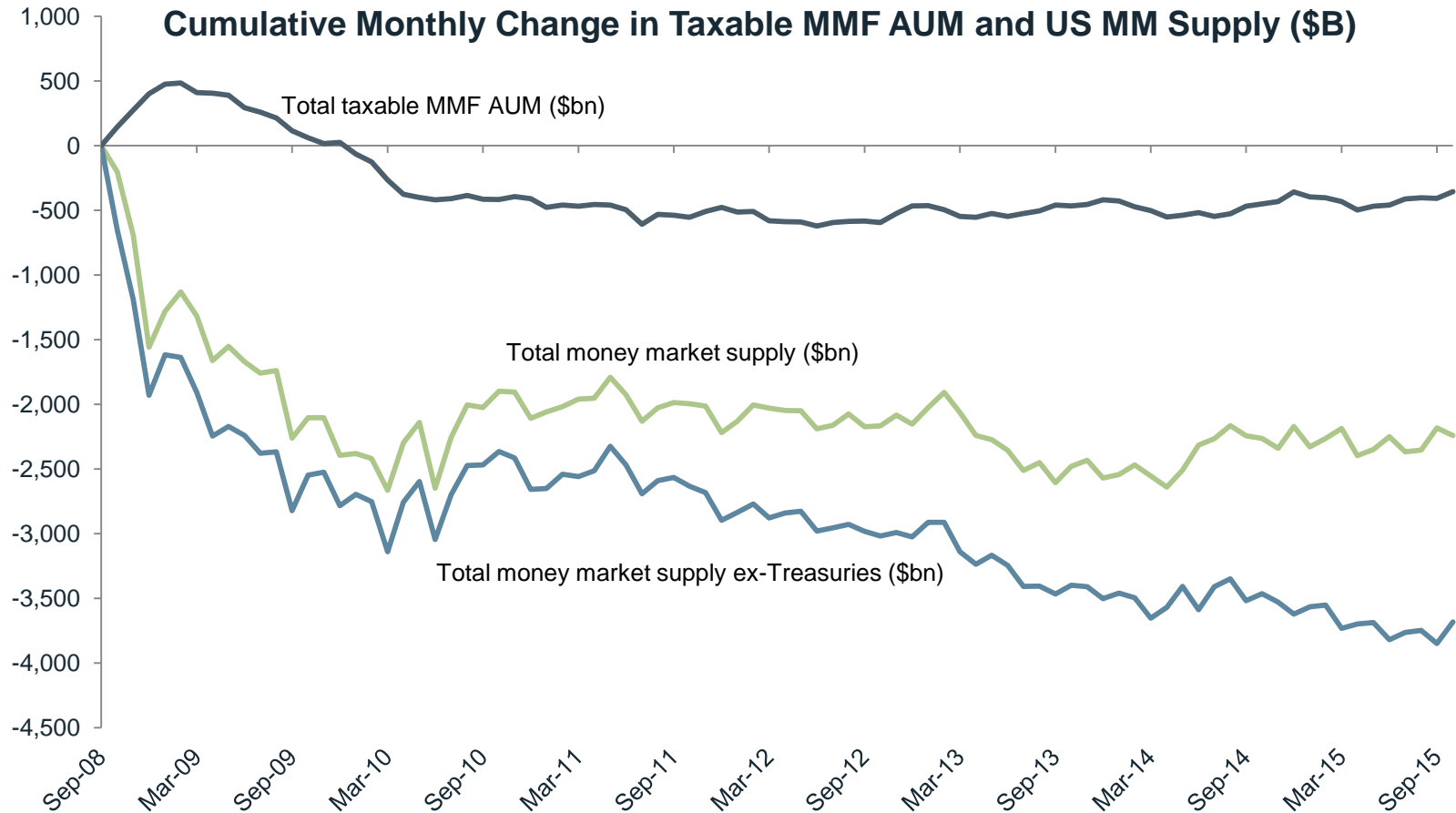
## Potential Risks

- Diverging global monetary policy backdrop has potential for generating policy mistakes
- Higher volatility warrants smaller asset allocation bets and prudent risk management



# Current Money Market Conditions

# Supply Stabilizes - Industry Assets Trend Higher

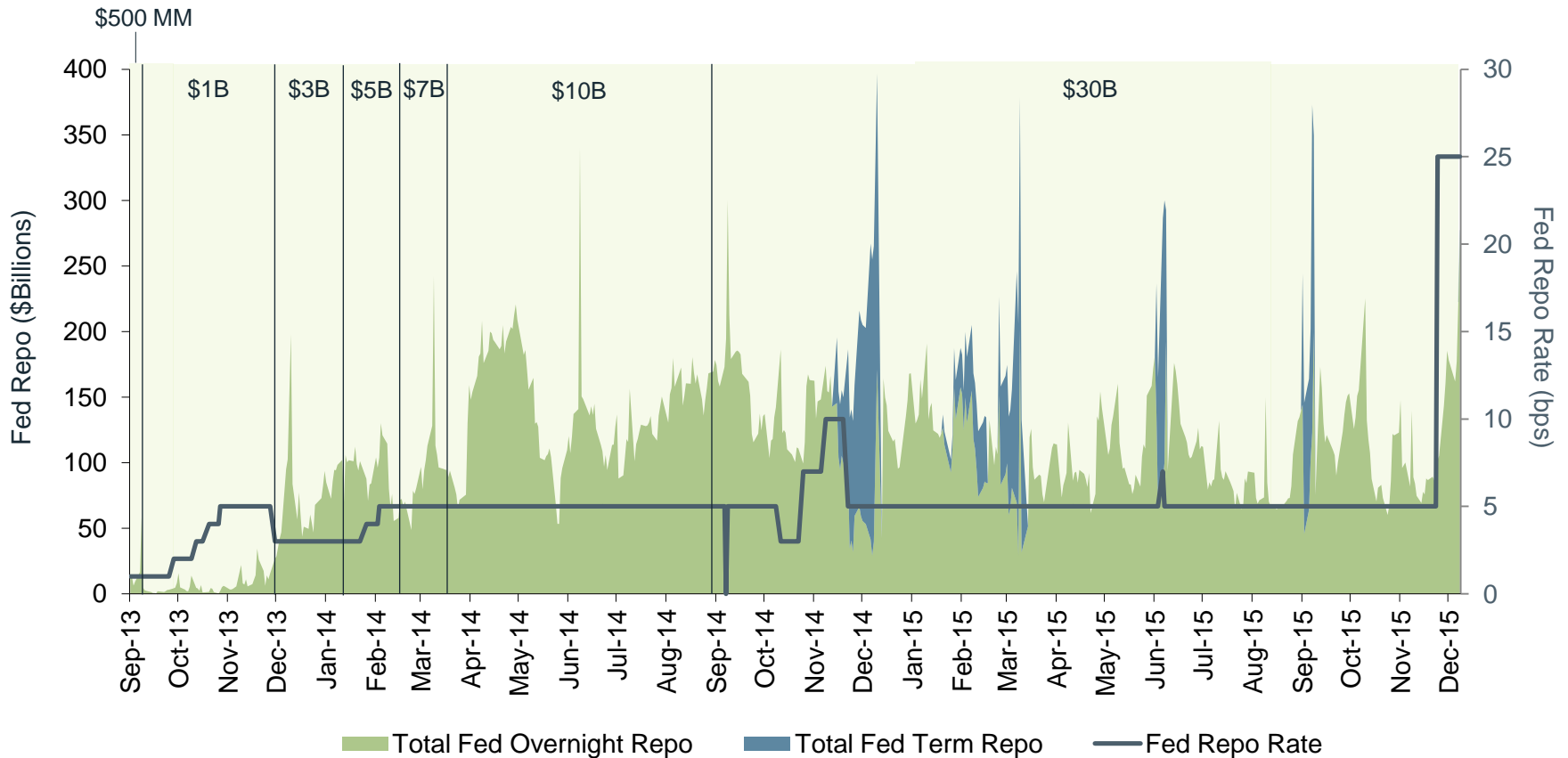


Source: J.P. Morgan, iMoneyNet as of 10/31/2015.



# Federal Reserve's RRP Adds Supply

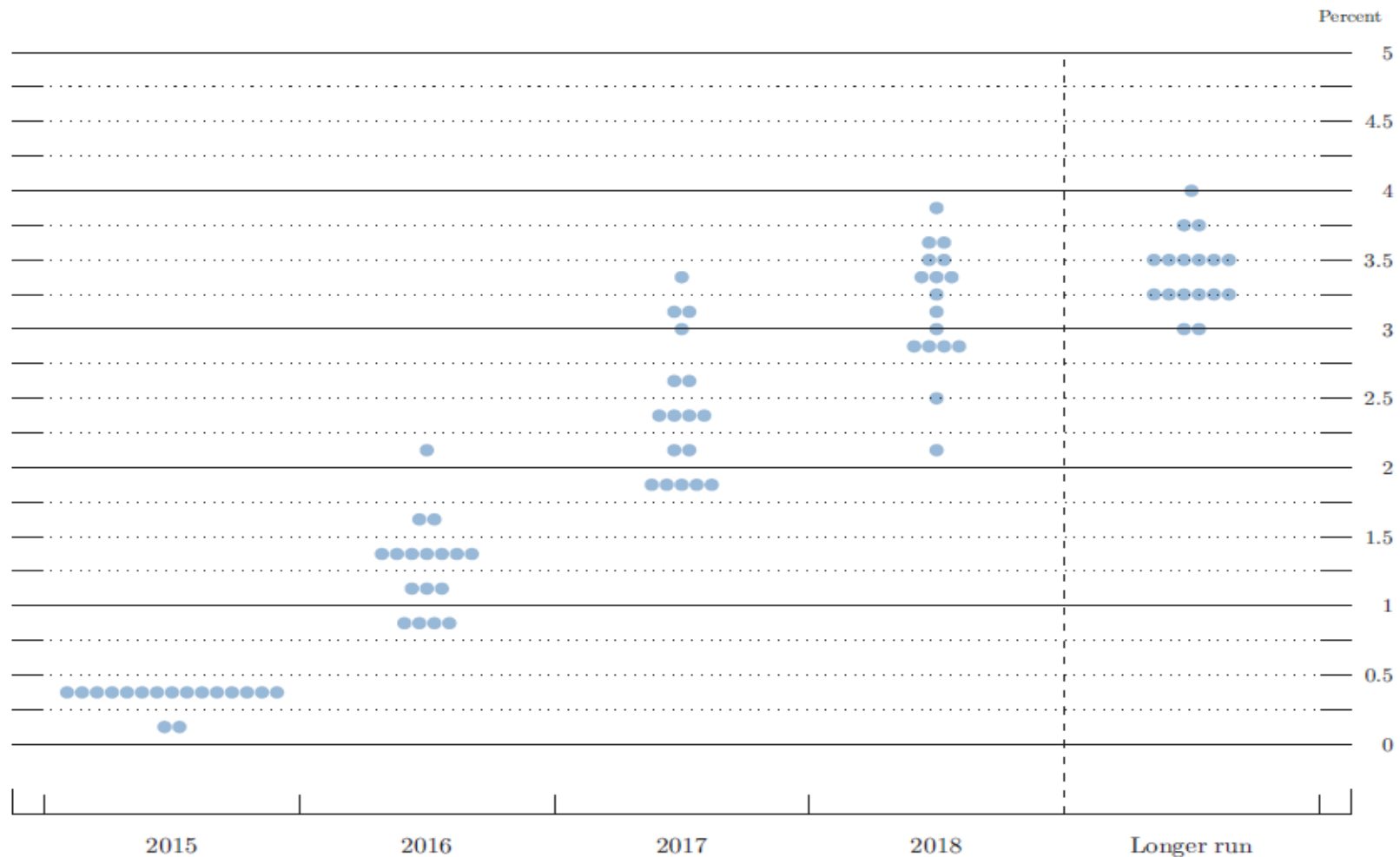
## Maximum Allotment Cap, Fixed Rate, Outstanding Amounts



Sources: Federal Reserve and Fidelity Investments as of 12/31/2015

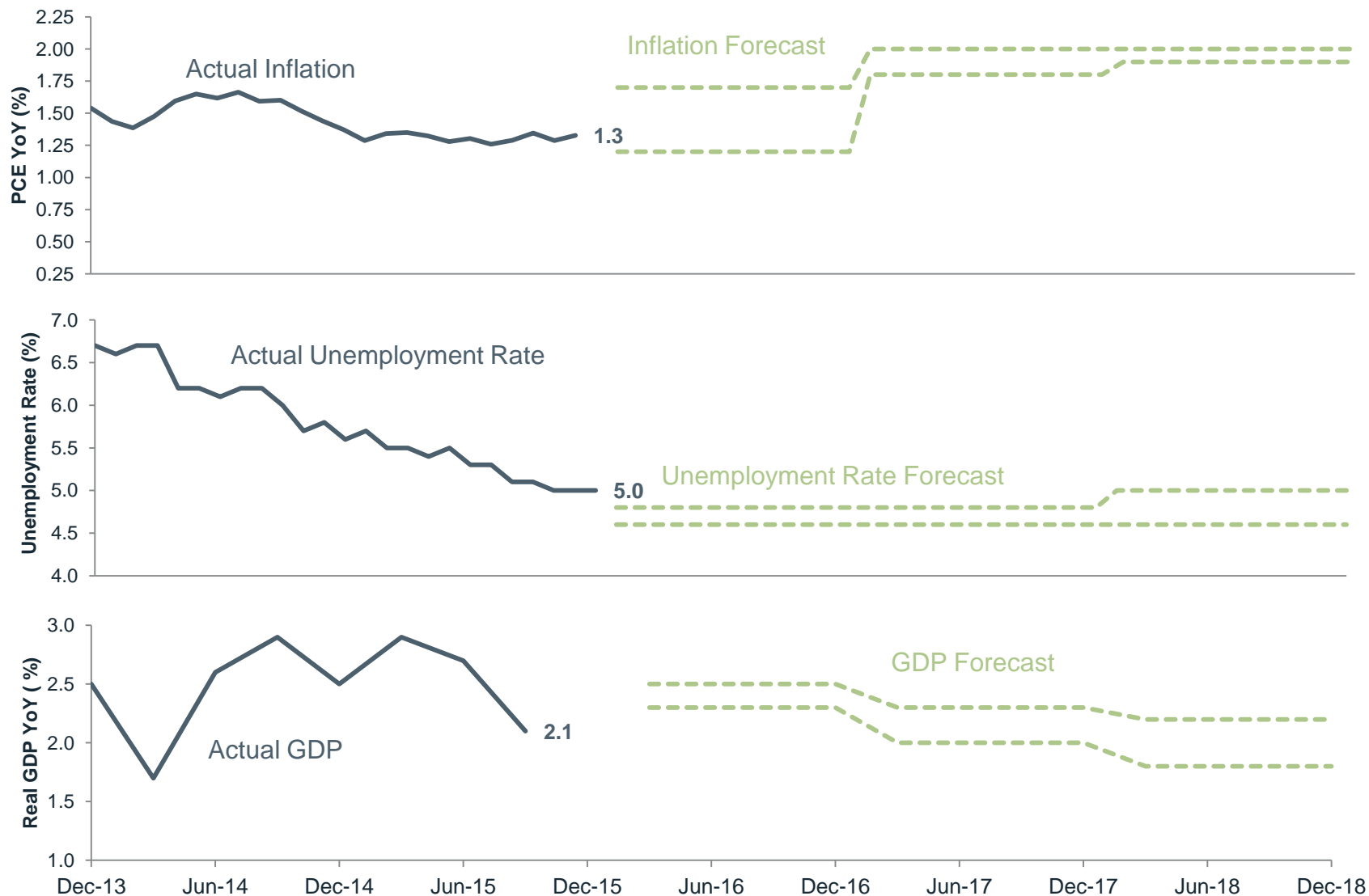


# Fed's Dispersion of Interest Rate Forecast





# Federal Reserve's Economic Projections



Source: Bloomberg and Federal Reserve

Actual Inflation as of 11/30/2015, Actual Unemployment Rate as of 12/31/2015, and Actual GDP as of 9/30/2015

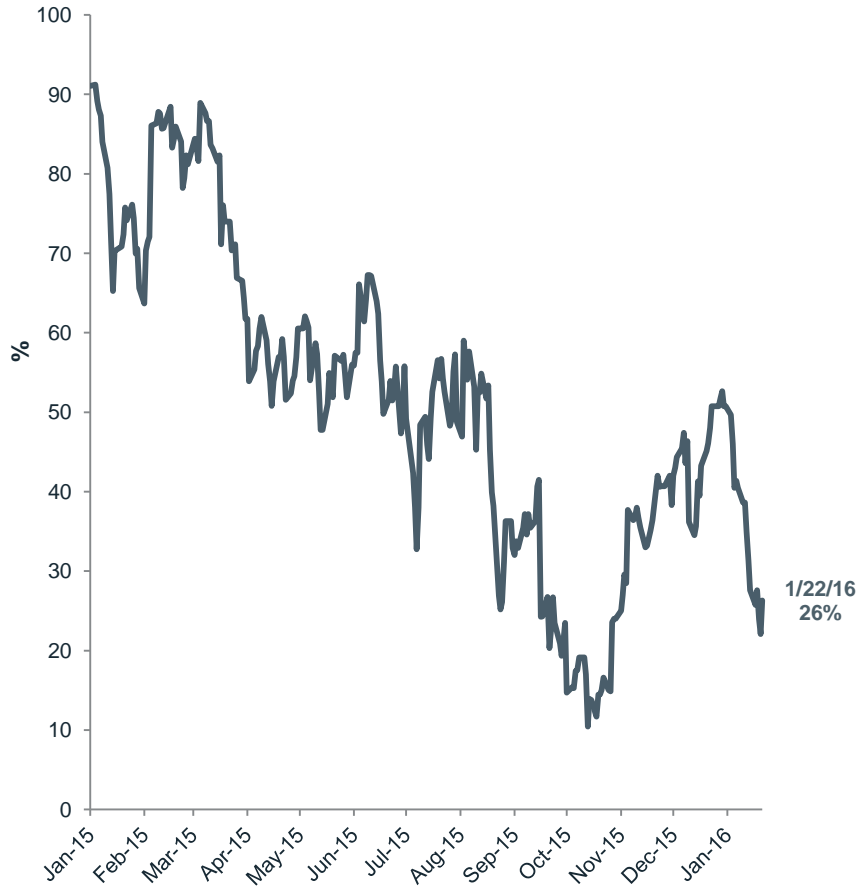
FOMC Forecast based on the central tendency (excludes the three highest and three lowest projections for each variable in each year) as of 12/16/2015

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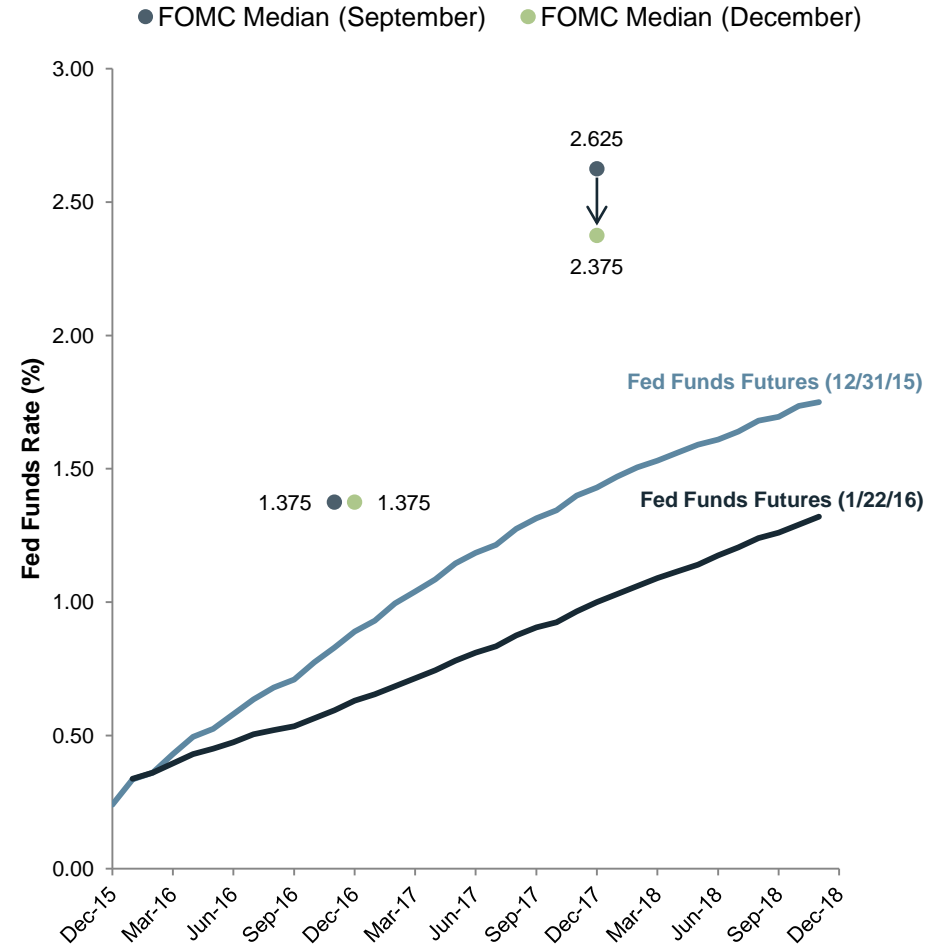


# Forward Rate Guidance Trends Lower

## Probability of a March Fed Rate Hike

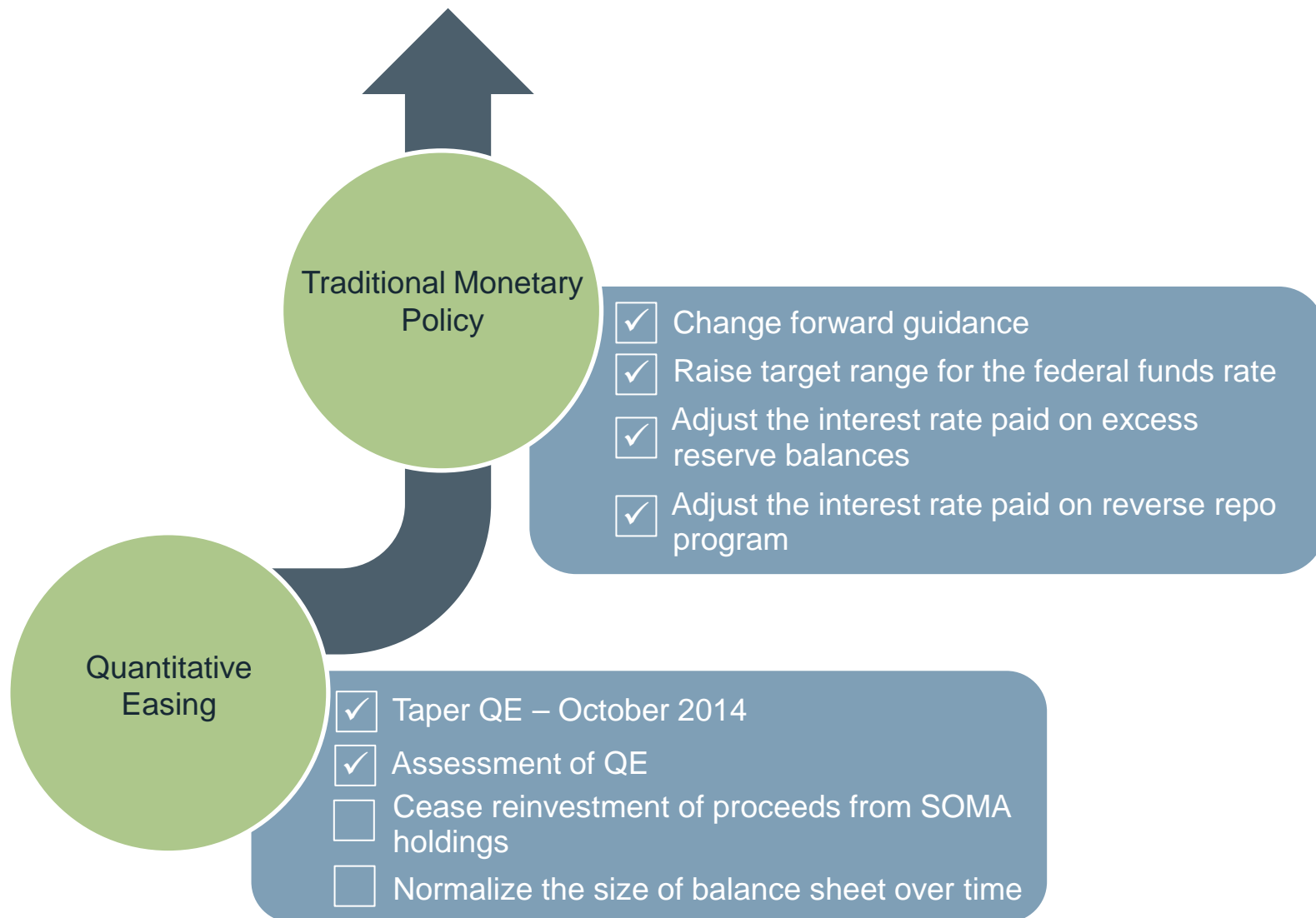


## Forward Fed Funds Futures



Source: Federal Reserve as of 12/16/2015 and Bloomberg as of 1/22/2016

# FOMC on Path Towards Higher Interest Rates





# Regulatory Reform Update

# Overview of Final SEC Rules on Money Market Mutual Funds

Fund Type	Net Asset Value (NAV)	Liquidity Fee	Redemption Gate
U.S. Treasury	Stable	No	No
Government	Stable	No	No
Retail Municipal/Tax-Exempt	Stable	<b>Yes</b>	<b>Yes</b>
Retail Prime/General Purpose	Stable	<b>Yes</b>	<b>Yes</b>
Institutional Municipal/Tax-Exempt	<b>Floating</b>	<b>Yes</b>	<b>Yes</b>
Institutional Prime/General Purpose	<b>Floating</b>	<b>Yes</b>	<b>Yes</b>

MMF Reform	Final Rule	Implementation Date
<b>Floating NAV</b>	Applicable funds will price and transact at a net asset value per share that can change or “float,” based on pricing the underlying fund holdings out to four decimal places (\$1.0000)	October 14, 2016
<b>Liquidity Fee</b>	If a fund’s weekly liquid assets were to fall below 30%, fund’s board may impose a 2% fee on redemptions  If a fund’s weekly liquid assets were to fall below 10%, redemptions will be subject to a 1% fee, unless the fund’s board determines otherwise	October 14, 2016
<b>Redemption Gate</b>	If a fund’s weekly liquid assets were to fall below 30%, fund’s board may suspend redemptions for up to 10 days	October 14, 2016
<b>Retail Fund Definition</b>	Retail funds limit shareholders to beneficial ownership by “natural persons” (individuals)  Institutional funds are open to any shareholders, including individuals, small businesses, and large corporations	October 14, 2016

# Implementation Update

## NCCMT Cash Portfolio

### Convert to a Government Money Market Fund

- Delivers attributes most desired by clients (stable \$1 NAV with no fees/gates)
- Least disruptive option for clients and state
- Results in a product suite with both a government and credit investment option providing different risk/return profiles and performance history

### Tasks Completed

- Obtained Board approval in April
- Determined level of government approval required
- Received favorable response from State Treasurer
- Communicate to clients/prospects and obtain shareholder approval

### Next Steps/Implementation

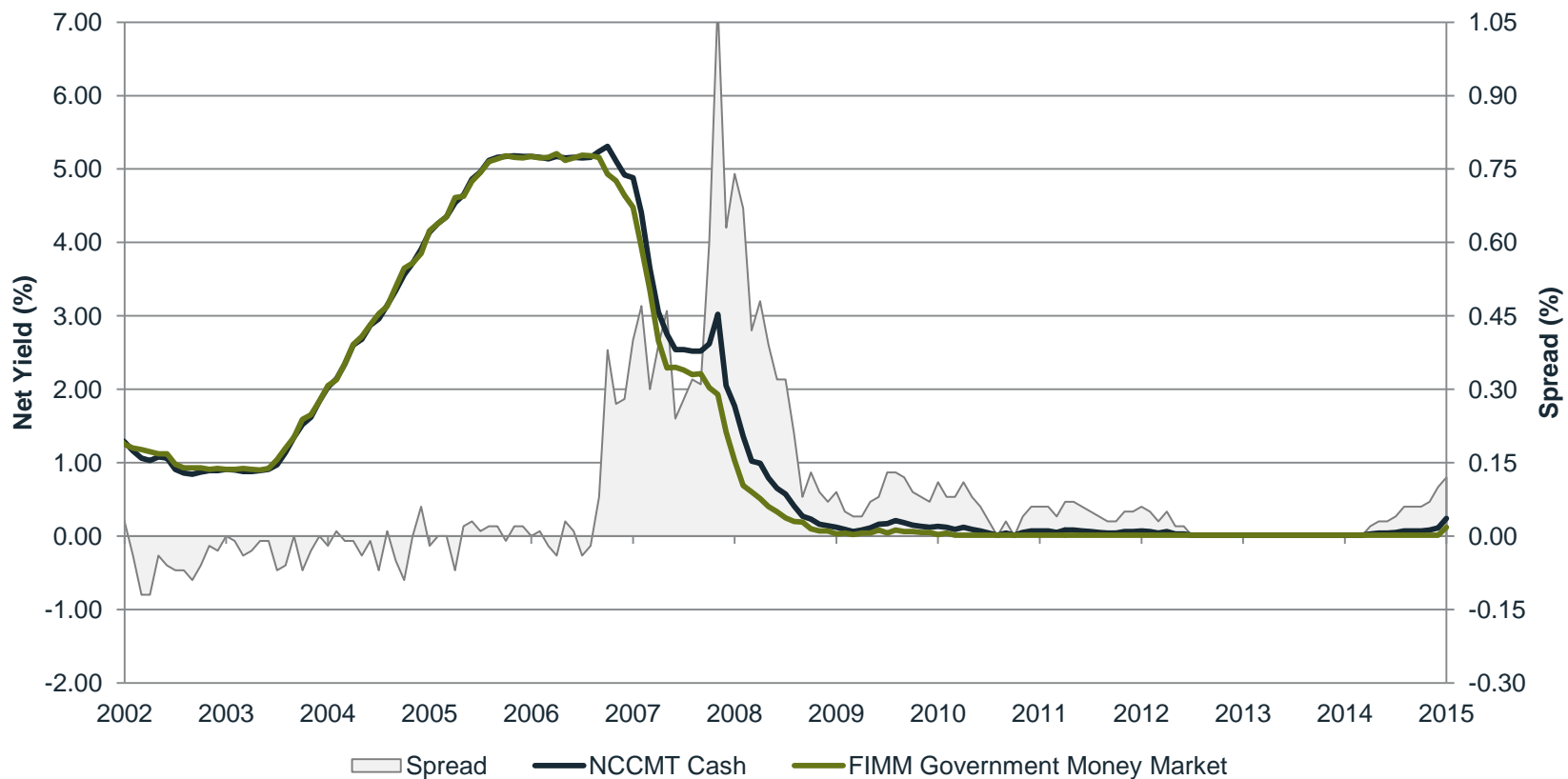
- Update shareholder disclosure
- Implement investment strategy

# Proposed Implementation Timeline

## NCCMT Cash Portfolio

	Q1 '15	April	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Q1 '16	Q2 '16	Q3 '16
Discuss recommendations with State Treasurer	★ — ★												
Board Meeting		★											
Preliminary Proxy Statement filed with SEC				★									
Definitive Proxy Statement filed with SEC					★								
Mail Date/Record Date						★							
Proxy Solicitation						★ — ★							
Shareholder Meeting								★					
Complete conversion to Government Fund												★ — ★	

# Yield Spreads



**NCCMT/Government Spread**  
Average Spread Over Entire Period 0.08

Source: Fidelity Investments as of 12/31/2015

Notes: Yields shown are month end net 7-day annualized yields. In the chart, spread refers to the difference between NCCMT and FIMM Government Money Market yield. Past performance is no guarantee of future results.

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# Potential Impact of Regulatory Reforms

## Prepare for changes to the short-term markets

### Regulations create a new demand for government securities

- New MMF regulations strengthen demand for government funds as clients seek to avoid floating NAVs and gates/fees
- Banks increase allocation to High Quality Liquid Assets to comply with Liquidity Coverage Ratio requirements
- Lower short-term bank issuance (under 30 days) causes money markets to build liquidity utilizing government securities
- Banks pass regulatory costs to institutional clients and restructure products driving depositors to seek quality alternatives
- Depositors consider market-based investment alternatives as yields trend above bank administered rates

### Demand for government assets continues to be addressed

- The Federal Reserve's O/N RRP Facility was increased to \$2 trillion from \$300 billion
- Treasury increases its cash reserve to \$344 billion, considers increasing Bill issuance, explores introduction of a 2-week and 2-month bill to broaden the amount of government supply in the front-end of the market

### Yield spreads between prime and government MMFs widen

- Banks pay-up for longer-dated & operational deposits to meet new regulations
- Demand for deposits is reduced as shareholders prefer government MMFs with a stable NAV and no liquidity gates/fees

### Review investment strategy & guidelines

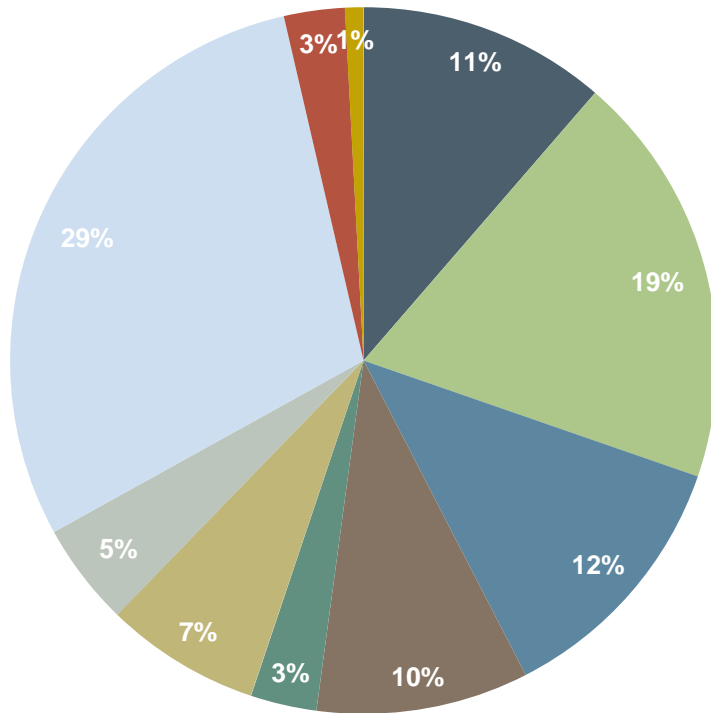
- Segment liquidity by establishing multiple portfolios that define your investment objectives
- Define investment objectives (operational vs. strategic) and establish appropriate constraints, controls and reports
- Ensure that investment strategies comply with investment guidelines and account for current market environment
- Broaden eligible investments as appropriate to enhance flexibility (managed products such as private placements and ultra-short bond funds may be appropriate to consider)
- Communicate and socialize approved changes to investment guidelines and investment strategy



# Cash & Term Portfolio Overview

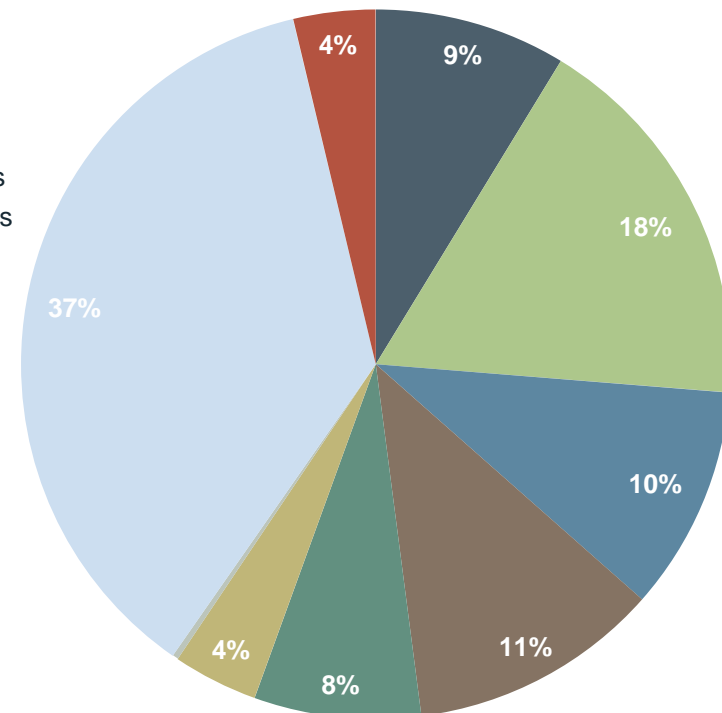
# NCCMT Cash Portfolio Positioning

December 31, 2015



- North American Banks
- Asian/Australian Banks
- Eurozone
- Nordic/Swiss Banks
- UK Banks
- Asset Backed CP
- Other Corp/VRDN
- Government/Repo
- Finance Companies
- Net Other Assets\*

December 31, 2014



## Fund Characteristics

Weighted Average Maturity (WAM)	48 Days
Weighted Average Life (WAL)	90 Days

## Fund Characteristics

Weighted Average Maturity (WAM)	43 Days
Weighted Average Life (WAL)	76 Days

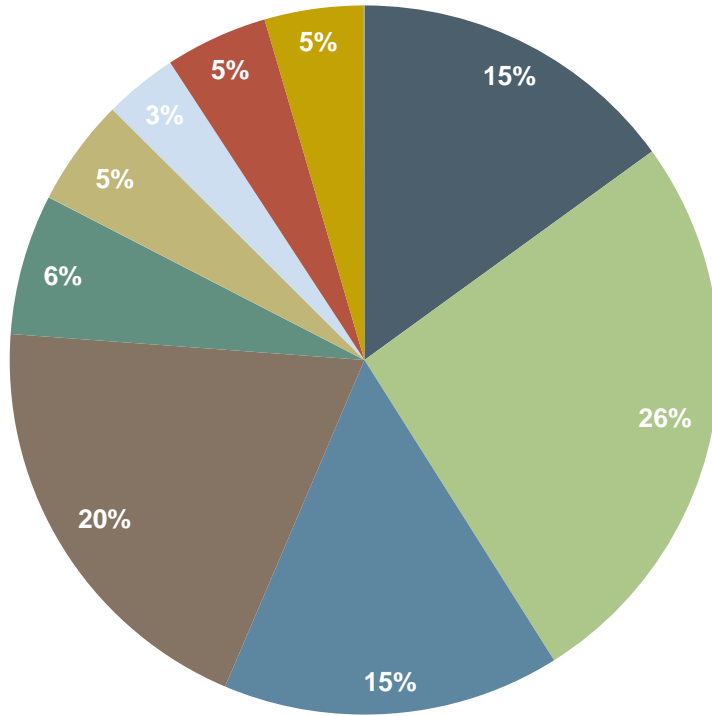
Portfolio diversification is presented to illustrate examples of the securities that each fund has bought and may not be representative of a fund's current or future investments. Each fund's investments may change at any time. Percentages may not add up to 100 due to rounding.

\*Net Other Assets may include cash and receivables and payables related to open security or capital stock trades.

Source: Fidelity Investments as of 12/31/2015

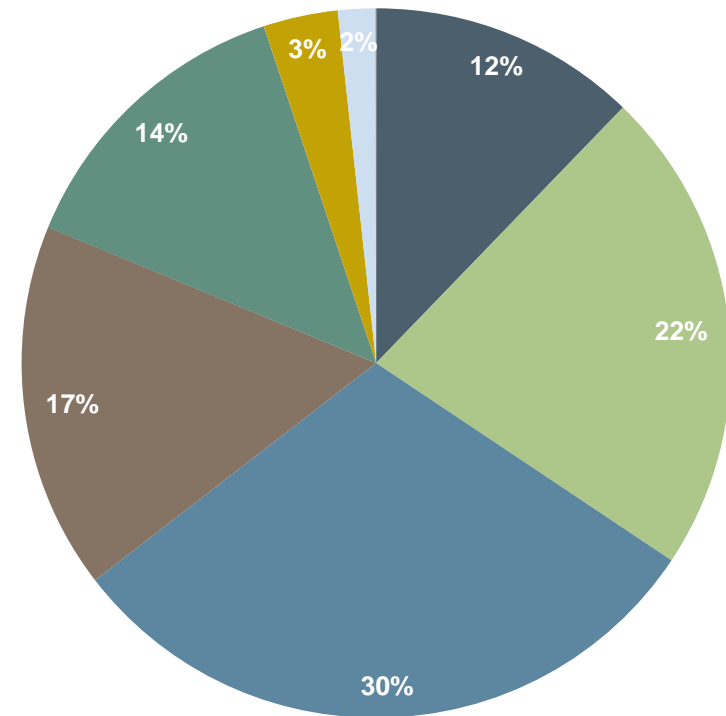
# NCCMT Term Portfolio Positioning

December 31, 2015



- North American Banks
- Asian/Australian Banks
- Eurozone
- Nordic/Swiss Banks
- UK Banks
- Asset Backed CP
- Government/Repo
- Finance Companies
- Industrials
- Net Other Assets\*

December 31, 2014



## Fund Characteristics

Option Adjusted Duration (OAD) 0.13 Years

## Fund Characteristics

Option Adjusted Duration (OAD) 0.26 Years

Portfolio diversification is presented to illustrate examples of the securities that each fund has bought and may not be representative of a fund's current or future investments.

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\*Net Other Assets may include cash and receivables and payables related to open security or capital stock trades.

Source: Fidelity Investments as of 12/31/2015

# First Quarter Investment Strategy and Outlook

## Investment Strategy

- Seeking to preserve principal, maintain liquidity and achieve superior risk-adjusted performance
  - Emphasize fundamental and macro research in formulating portfolio structures
  - Meet fund liquidity targets through repurchase agreements, Treasuries, agencies and short-dated investments
  - Manage weighted average maturities (WAM) and weighted average life (WAL) constraints to enhance NAV stability, liquidity and performance
  - Position portfolios based on our assessment of relative value across the money market yield curve within the context of our approved credits
  - Take advantage of rising money market rates as potential Fed tightening approaches

## Outlook

- US economy may slow into 2016
  - Consumer fundamentals are decent but readings from the manufacturing sector look bleak
  - Weakness in China and other emerging market economies creates a headwind to global growth
  - Strengthening dollar, growing wage pressures, higher interest rates may reduce hiring and investment plans
  - Ageing/retiring workforce and the elevated level of global debt continue to weigh on the medium-term outlook
- Monetary policy divergence remains the key macro theme
  - Global market volatility remains elevated
  - Fed lifting rates for the first time in seven years, while the ECB and BOJ expanded accommodation further
- Federal Reserve enhances forward guidance
  - Fed guidance suggests that rates will increase about 100 bps or 4 hikes in 2016
  - Fed futures are pricing in about 50 bps or 2 hikes in 2016
- Supply adjusting to market demands
  - Fed's RRP facility increased to \$2 trillion from \$300 billion
  - Treasury has announced increased Bill issuance and is exploring a 2-week and 2-month Bill

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