I. OBJECTIVES

This passively managed currency hedging overlay portfolio will consist of foreign exchange spot and forward contracts. The base currency of the overlay portfolio is the U.S. dollar. The objectives of this portfolio are to implement passively managed hedging strategies at the overall PSERS Fund level and within individual asset classes when deemed prudent. The IO will provide the manager with the hedge notional value of currencies to be hedged.

II. PORTFOLIO RISK MANAGEMENT

The Board’s expectations are that this portfolio be passively managed within the spirit of a Passive Currency Hedging Overlay Program mandate. Within this framework, the following are the portfolio risk constraints under which the manager is required to operate:

A. Currency Risk

1. Currency positions in countries not in the MSCI World ex US IMI Net Index are prohibited without the written permission of the CIO or a Managing Director in the CIO’s absence.
2. Cash, if any, in the portfolio shall be invested in the Fund’s cash account (the “STIF”).

B. Derivative Counterparty Risk

1. The commercial and investment banks used for forward/spot currency transactions must be rated A3 or better by Moody’s Counterparty Ratings, (if not rated by Moody’s, then rated A- or better by Standard and Poor’s Counterparty Ratings or rated B or better by Fitch’s Bank Individual Ratings).
2. Exposure to any counterparty will not exceed 30% of the notional value of the portfolio at the time of entering into a trade. “Exposure” for this purpose is defined as the sum of US dollar currency purchases minus the sum of US dollar sales for all outstanding transactions with a counterparty.
C. Absolute Restrictions

All investments, except currency derivatives and investment into the Fund’s STIF, are strictly prohibited without the written permission of the CIO. The following are examples of some of the prohibited types of transactions and is not meant to be an all-inclusive list: common and preferred stock, letter stock, private placements, physical real estate, commodities, etc.

D. Overdraft Risk

Since this is an unfunded account, the manager will advise PSERS’ Investment Office and Investment Accounting Division at least five (5) business days prior to the forward contract settlement date of the estimated value of the settlement amount payable from the counterparty banks. The manager will follow up with an exact cash amount no later than one (1) full business day prior to the settlement date. The manager will advise PSERS’ Investment Office and Investment Accounting Division at least one (1) full business day prior to the forward contract settlement date of the estimated value of the settlement amount receivable for the counterparty banks.

Once advised of the settlement amount, PSERS will be responsible for sweeping the appropriate amount receivable from the portfolio or for funding the portfolio with the appropriate amount payable for settlement of currency derivative contracts to the portfolio, as applicable.

III. DERIVATIVES

The portfolio is permitted to establish and maintain long and short positions in currency forward commitments.

IV. AMENDMENTS

A written request to the CIO should be made if the manager believes that these portfolio risk constraints significantly limit the ability of the manager to achieve the objectives of the portfolio. A written amendment will be issued from the CIO, or a Managing Director in the CIO’s absence, if the request is approved.