Finance and Investment Committee Minutes

☒ **ACTION ITEM**	☐ **CONSENT ITEM**
☐ **New Contract**	☐ **Contract Amendment**
☐ **Contract Amendment**	☐ **Existing Contract Extension**
☒ **Other - Committee Charter**	☐ **Existing Contract Additional Spend**
	☐ **Previous Board Approval**______________
	☐ **Other**_______________________________

Action Items: Items requiring detailed explanation to the Board. When a requested action item is a day-to-day operational item or unanimously passed through committee it may be moved forward to the board on the Consent Index.

☐ **Move forward as Consent**: This Action item is a day-to-day operational item, unanimously passed through committee or qualifies to be moved forward on the Consent Index.

Consent Items: Items not requiring detailed explanation to the Board of Governors. Consent items are contract extensions, amendments or additional spending authorities for items previously approved by the Board.

Item Description	The Finance and Investment Committee meeting Minutes December 5, 2023
Purpose/Scope	Review of the December 5, 2023 Finance and Investment Committee to provide opportunity for corrections and historical accuracy.
Contract ID	N/A
Budgeted Item	☐Yes ☒No
Procurement Method	N/A
Contract Amount	N/A
Contract Terms	N/A
Committee Recommendation	Staff recommends the review and approval of the December 5, 2023 Finance and Investment Committee minutes.
Contacts	Jennifer Montero, Chief Financial Officer

CITIZENS PROPERTY INSURANCE CORPORATION

MINUTES OF THE
FINANCE AND INVESTMENT COMMITTEE MEETING
Tuesday, December 5, 2023

The Finance and Investment Committee (FIC) of Citizens Property Insurance Corporation (Citizens) convened at New College of Florida, College Hall, Tuesday, December 5, 2023.

The following members of the FIC were present:

Chair Erin Knight
Carlos Beruff (Board Chair)
Charlie Lydecker
LeAnna Cumber

The following Citizens staff members were present:

Jennifer Montero
Barbara Walker
Tim Cerio
Kelly Booten
Michael Peltier
Jeremy Pope
Jay Adams
Joe Martins
Mark Kagy
Paul Kutter
Brian Donovan
Andrew Woodward

The following people were present:

Kapil Bhatia	Raymond James
Sasha Stipanovich	Raymond James
John Generalli	Wells Fargo
Duane Draper	Bryant, Miller, Olive
Mark Weinberg	Citi Bank
Coleman Cardell	Bank of America
Matthew Sansbury	RBC Capital Markets

Call Meeting to Order

Barbara Walker: Good afternoon, and welcome to Citizens' December 5, 2023, Finance and Investment Committee Meeting that is publicly noticed in the Florida Administrative Register to convene immediately following the Audit Committee Meeting and will be recorded with transcribed Minutes available on our website. For those attending today's session through the public link, you are automatically in listen-only mode. Panelists, thank you for identifying yourself prior to addressing the Committee. May I proceed with the official roll call?

Chair Knight: Yes.

Roll was called and quorum established with Chair Knight, Board Chair Beruff, Governor Lydecker and Governor Cumber.

a. Approval of Prior Meeting's Minutes

Chair Knight: Thank you. Welcome. I would like to call the December 5th Finance and Investment committee meeting to order. Our first order of business is approval of the September 26th Minutes.

Governor Lydecker: So moved.

Chair Knight: Okay. Any opposed? The Minutes will be adopted. And I would also like to welcome Governor Cumber to our committee.

Governor Cumber: Thank you, I am excited to be here.

Chair Knight: And Mr. Bhatia from Raymond James, looking forward to hearing your market update.

b. Raymond James - Financial Advisor

a. Market Update

Kapil Bhatia: Thank you, Madam Chair. And good afternoon, Madam Chair, Mr. Chairman and Board members. For the record, Kapil Bhatia from Raymond James & Associates. We are your financial adviser and investments consultant. I will briefly go through the market update, but please stop me at any time for any questions or additional clarifications. Inflation was unchanged in October at .4% and over the last 12 months the all-items index or inflation has increased by 3.2% before any seasonal adjustments. A smaller increase than 3.7% increase for the last 12 months ending in September of 2023. The index for shelter or homes continues to rise in October, offsetting a decline in the gasoline index, resulting in a seasonally adjusted index being unchanged over the month. The all-items index, which is more commonly used less food and energy effectively rose by four percent over the last 12 months. The smallest 12-month change since the period ending September of 2021. Inflation is slowing down, but still far away from the Fed's target rate of two percent. Non-farm payroll employment increased by 150,000 in October, and the unemployment rate has basically remained unchanged at 3.9% with 6.5 million unemployed persons. This employment increase is below the average monthly gain of over 250,000 during the prior 12 months. However, since the recent low in April, the unemployment rate and number of unemployed persons are up by half a percent and 850,000 respectively. All of this reflects that the labor market is slowing down. We will get the revised employment number for the month of October this Friday, and we expect that number to show further slowdown. Since March of 2022, as we all know, the Fed has increased benchmark rates 11 times to the current Fed funds rate of five and a quarter to 5.5%. The market does not expect the Fed to raise rates at a December meeting next week and is now projecting two to three rate cuts in the second half of 2024, which would put the Fed fund's rates to around 4.50% to 4.75% by the end of 2024. However, we expect the Fed to cut more than that or three to four times in 2024. As I said earlier, the inflation is coming down and economic conditions continue to slow down. In addition to holding rates at relatively elevated levels, the Fed is continuing to reduce its bond holdings and since June 2022, the Fed has decreased their balance sheet by approximately $1 trillion . The Fed is also allowing approximately $100 billion in treasury bonds to mature and roll up each month instead of reinvesting them, and at the same time the Treasury is issuing significantly additional debt to fund fiscal deficits. Both of these factors are leading the rates to remain higher than the current economic conditions otherwise would necessitate. The Fed is projecting inflation to steadily cool or slow down, while labor market remains historically strong, but is slowing down, and energy prices have recently started to come down. We expect GDP to increase by 2.4% this year, but to only increase by less than one percent next year as we are looking at slowdown in 2024, and before recovering it in 2025 to approximately two percent or similar to pre COVID levels in 2025.

Consumers who make up two-thirds of our economic activity have slowed spending but remain engaged as their current wage growth is outpacing the inflation rate. However, in addition, they continue to borrow on credit cards and the credit card debt has reached to a record level of over $1 trillion. One of the reasons so far, we have been able to avoid recession is the continuous large fiscal spending and its multiplier effect, even though various programs are towards the end, but there are still some cash floating around from the 2021 and 2022 fiscal programs, including the CHIPS Act and the Inflation Reduction Act. However, at the same time that is also adding to the sticky inflation. As we know, monitoring policy works with significant, and variable lags, so we still have not yet seen the full impact of interest rate hikes. In addition, as most of the cash infusion from fiscal stimulus is gone, student loan repayments have started. We expect economic conditions to slow down and lead to at least a mild recession in early 2024. This has been a relatively rolling slowdown. Simply we have been talking about for more than a year, but fiscal spending continues to come in and most of the corporations and homeowners have low interest rates locked and is not yet matured. So, we still have not seen the full impact of higher interest rate increases which we expect in 2024 and 2025 as the corporate debt is concerned. However, the homeowners have a locked in mortgage rate and they're not moving, and that is putting pressure on the housing. Based on the projection of maintaining current Fed rate levels through the first half of 2024 with no additional rate increases, and over the last month rates have started to come down. The yield curve remains inverted still with the spread between the three-month and 10-year treasury at 114 basis points and 36 basis points respectively. Since the beginning of the year, one year and two-year treasury rates have basically unchanged and five and 10-year treasury rates have increased by approximately by 15 basis points. As Jennifer mentioned earlier during the Audit committee meeting, all of the recent increases in interest rates have increased resulting in a negative mark to market in our investment portfolio. The current mark to market value as of yesterday was $742 million. These values again are non-economic and non-cash, and as these negative values will continue to pull to PAR as the securities mature and our portfolio duration is much shorter today than it was last year, and the evaporation pace has accelerated significantly.

Lastly, our income return is stable and historically high rates are economically beneficial as they all lead to higher interest income. And now we have really started to realize the benefits of higher interest rates by investing the remaining portion of our maturing securities after paying for existing claims, as well as additional premiums at higher interest rates. We have approximately $4 billion maturing over the next 12 months and that will give us sufficient liquidity for the upcoming 2024 season, as well as give us the higher interest income which is reflected in the budget. And lastly, about the reinsurance market. Global reinsurance markets are heading into 2024 with a positive outlook and expectations of an orderly market as compared to the prior few years, with a marginal rate increase. That will again depend on the cedent, how efficient they are in the strength of the management, but the supply is expected to exceed demand. We expect rate increases to be approximately zero to five percent. Again, it will depend on the cedent. I will stop here and be happy to answer any questions.

Chair Knight: Questions from the committee? I have a question. Regarding the global insurance or reinsurance markets, what are you attributing this sort of, it seems like a normalization from last year, too?

Kapil Bhatia: We had significant rate increases over the last couple of years, that is one of the reasons. Even though global reinsured losses are over $100 billion this year or projected to be over $100 billion this year, we had no large event. We had Idalia, but relatively not any significant losses. Interest rates have started to come down. Mark to market have started to evaporate for reinsurance. So, there is a little bit more capital available as well as the legislative changes are going to help us. So, the reinsurance capital is there with no losses and some mark to market loss evaporation. We also see additional stability in the marketplace, and because there is a relatively higher return in the reinsurance market, a little bit more capital has come in, especially in the capital markets. All of that should lead to a relatively modest increase. Again, it will be a function of cedent, management and the strength and working of claims processing and we have all of these things.

Chair Knight: Thank you. Thank you for the report.

Kapil Bhatia: Thank you.

Chair Knight: Moving to Ms. Montero. We have four items on the agenda, two of which are action items. We will start with the 2023/2024 budgeted and projected on a combined basis layer charts for '24.

c. **Chief Financial Officer Report**

a. 2023 and 2024 Budget/Projected Layer Charts

Jennifer Montero: Thank you. If you turn behind tab three you should see the layer charts the Chair just mentioned. So, the first slide is the coastal account layer charts. So, these as we have talked in the past, the layer charts are always projected to 9/30 of that current year, as that is the exposure amounts that our reinsurance is based on. Our TIV is at 9/30. So, we do project out and the last meeting was 6/30 actual projected to 9/30. This is the actual 9/30 PMLs. So, on the coastal account the only thing that really changed is the 1-in-100 year PML went down by $293 million to $8.249 billion. And the Cat Fund coverage is $2.074 billion which is a reduction of $89 million. The private reinsurance program is $2.461 billion, and the Citizens policyholder surcharge doesn't clicks in until the 1-in-85 year event, which you can see on the far left which is about $6.95 billion dollars of loss in LAE, and the emergency assessment -- sorry, the regular assessment doesn't kick in until the 1-in-91 year event, which would be $7.324 billion. Any questions on this? I will just go over these that you have seen a million times. It is just a high level.

Governor Lydecker: Sightly off topic, but either last year or the year before I think you all requested software to help place this reinsurance portfolio.

Jennifer Montero: The modeling software, yes.

Governor Lydecker: Because this seems more sophisticated and, you know, just because of the dynamics of the marketplace the last couple of years. I was curious, how is that software working and is it adding value to what we are doing here?

Jennifer Montero: Well, we don't really use it for these. The software, the modeling software we use in the event that to look at our exposure and when a storm comes, we can model what we have, what those losses would be. And I actually have the modeling king here in the back if Paul would like to make a comment on the modeling software.

Governor Lydecker: Well, my question is really, is it working as, as advertised and –

Jennifer Montero: Yes. The question is a few years, a couple of years ago we had a meeting where we had modeling software and Governor Lydecker is asking specifically how that is working out and is it -- how we use it with the layer charts, if at all.

Paul Kutter: Sure, yes. This is Paul Kutter, director of actuarial data science. Yes, the model is working great. You know, it's got a number of additional more sophisticated features to it that we, you know, use like if a storm is approaching, for example, to estimate what the losses from that storm might be. You know that particular software does help out with these layer charts, but it is really the model produces those numbers you see on the side that connect the probability of that loss happening to the dollar amount. The layer chart, itself, you know, the nice –

Governor Lydecker: Can it help us in modeling for pricing purposes? And do you use it at all, or do we accept the modeling of the reinsurers?

Jennifer Montero: We do use the modeling of the reinsurers in conjunction with both using our own because they model differently.

Governor Lydecker: Right.

Jennifer Montero: We have AIR in-house license. They can provide the other models to us and the results from those, because they do, they do model differently depending on which one you are using for which account.

Governor Lydecker: Got it. Thank you, Paul.

Kapil Bhatia: Just one more thing. As you see as Paul said, the numbers on the left side which tells us 1- in-100 years or 1-in-50 years. So, when we, when we look at the probabilities as to where to place the reinsurance program before running the data, this gives us like stability and a better understanding of how to place the program, what the expected loss will be, what our pricing will be. That is how we basically structure the budget, and then when we say, we will spend this amount of money to get this amount of program, this, all of the data is really instrumental behind the scenes for us to make the decisions. So, better input data, hence, the better output and a better decision-making. The brokers tell us RMS and the others are fine, but we use the AIR. So, all of this is basically integral to what you see here and to calculate the projected losses from any approaching storms.

Governor Lydecker: Thank you.

Jennifer Montero: Any other questions on the coastal account before we move on to the personal lines account? Okay. So, the next slide is -- I am sorry.

Governor Cumber: I have a quick question. Just to make it more concrete when we are talking like 100 -- you know, approximately 100% of coastal account surplus is exposed in a 1-in-100 year event. Of the storms we have had, like what would that -- what would have qualified, like of the named storms, so you can kind of understand, because I think it is, you know, it is very detailed, it is very in the weeds, but when people like in the reality and just kind of practicality, where, what kind of storm are we looking at that would -- and then just when you are answering that, I assume, I assume that when we say 1-in-91 year storm, it would hit that $7.3 billion. I assume that is depending on where it hits as well. So –

Jennifer Montero: Yes, that is the maximum loss based on it hitting in the State of Florida with what we have. Obviously, that is everything, it is not our total exposure.

Governor Cumber: Right.

Jennifer Montero: Because everything would be gone, but to answer your question, I can tell you on this chart, Hurricane Andrew for example is a 1-in-43. So, you can see it would be $4.146 billion. Hurricane Ian we just looked up and it is between 1-in-20 and a 1-in-25 year event with Hurricane Ian.

Governor Cumber: So, what about Irma, is that about the same?

Jennifer Montero: Irma would have been a little bit, was very -- had little bit higher than Ian. In fact –

Kapil Bhatia: Approximately 1-in-25.

Jennifer Montero: Yes, about 1-in-25, because Irma was, Irma was a $2.6 billion. No, Ian would be higher because this is $3.6 billion. Irma would be about a 1-in-20.

Governor Cumber: Okay. So, so to get to that, that exposure you would be looking at having two or three -- two or three storms kind of 2005.

Jennifer Montero: That is correct. We do not have reinstatements. So, it is not like you would extinguish all of it, it doesn't return. So, it is gone. So, it would take either one huge killer of a storm or multiple storms like in 2004 and 2005 when we had eight storms in those two years.

Paul Kutter: Yes, Paul Kutter again. Yes, the, I think it is 1926 Great Miami hurricane we model is a little more than a 1-in-100 year storm. I think that is a 1-in-103 years or something, but it is about a 1-in-100 year storm that 1926 Great Miami hurricane.

Governor Cumber: Sorry, just one more question on that. With the, with the modeling with these storms look like, obviously -- I mean, I think everyone can see that we are getting, the weather is changing, and they are getting more intense and so forth. Does the storm modeling change? Is it being updated or are we still modeling based on what it would have looked like back 10 years ago, 20 years ago?

Jennifer Montero: So, we, for going forward we use the model, for example, Idalia hit at the end of September. So, we don't have enough information. Jay doesn't have enough claims yet to really – so we work with the actuaries and Brian Donovan is our reserving actuary back there, he works with Paul. And what we do is we get the model, and we use the model data because it is the best data that we have. Brian can sometimes have enough data to add maybe litigation rates in there, inflation rates in there, things like, but it is pretty basic. We only use that as the interim for September reporting. When we get to December, Brian does a full actuarial review where he looks at everything, and he also has the IBNR which is the incurred but not reported. That is the piece that with the claim you have the call in. You tell them about it, you have cases are set up. As you make payments those case reserves go down as payments. So, you have pays, you have case reserves, and you have what is known as incurred but not reported, IBNR. Which the actuaries provide because we are required to book the entire cost of the storm in the year that it occurs. And then over time if that changes, then if we start to see that there is not enough IBNR then Brian reevaluates at each quarter and then you have development up or down, but the model is the starting point. So, then the model for Idalia was $128 million, and at -- and was that Idalia, yes, yes. When did she happen? She was in August, I think, and then when we got to September 30th I just went through. Brian did an actuarial review and now it is $133 million because he has looked at what the model had and we put in stuff that we have seen, the claims that we have gotten. He looks both backwards and historical and looks forward on what is happening in the market, like litigation. He knows it is not going to be nearly as high as two years ago when we had Irma or three years ago when we had Irma or however long ago it was. So, there is a full actuarial review, but the model is just the starting point and then sometimes, right there and sometimes they're off. That is the best we have.

Governor Cumber: Thank you.

Jennifer Montero: No other questions? Okay. If we can turn to the next slide, it is the personal lines account. Again, this is the actual 9/30 data. The PML at a one-in-100-year event went down by $253 million and the Cat Fund coverage of $3.088 billion is also a reduction of $132 million, and we did have private reinsurance of $2.919 billion in this account. We had the Citizens policyholder surcharge quick in at one in five-year event and the emergency assessment in at a one in 10-year event, and then exhausting at the 1 in 17 and then back again at the 1 in 52 and exhausting at 1 in 61 and then back again at the 1 in 68. Any questions about this, this, this slide? Again, this is also where we expose 100 percent of surplus in a one-in-100-year event. Okay, moving on to the commercial lines account and the reason that this one is actually important. We don't usually talk about the commercial lines account very often because we do not buy traditional private reinsurance in this account. This account did go down to the, the PML went down by $112 million and the Cat Fund of $229 million went down by $2 million. This account is made of a commercial residential and commercial non-residential business. Over the last three or four years we have not purchased commercial non-residential reinsurance, only commercial residential in the coastal account. So, when we merge the accounts, we will have this commercial residential that will be mixed in with the coastal' s commercial residential that was not covered by reinsurance. So, this is why the amount of coverage in our budget you will see is increasing is because we have more eligible coverage that will be included when we merge the accounts. Any questions on the commercial lines account? And we also get all the surplus that is in here once the accounts are merged. The next slide is just a hypothetical, what if we had combined the accounts in 2023 of which we did have some outstanding financial obligations that we had to, we had to take care of before we could merge which is why we are merging in January 2024, and the defeasance did close yesterday, Mr. Chairman, we got confirmation. Thank you for getting that back to us. In this event you can see that we have Cat Fund coverage of $5.39 billion, private reinsurance of $5.38 billion and of accounts combined we do not have a Citizens' policyholder surcharge until you hit the 1-in-85 year event. There is no regular assessment once the accounts are merged. So, it goes straight into an emergency assessment. It is a 1-in-92. So, this is a much better situation than what you saw in the personal lines accounts.

The next slide is a budgeted projected slide. This kind of goes with the budget that we presented. So, what we have here is Cat Fund coverage of $5.6 billion on a combined basis. Our reinsurance program, and this is a placeholder like we always talk about when we get to the budget, we put a placeholder in, and this is $5.5 billion. The PML, the one-in-100-year event is $17.796 billion, and we do not have a policyholder surcharge until you hit a 1-in-95 year event. The Citizens' policyholder surcharge is $416 million on this slide, but don't forget the Citizens' policyholder surcharge is 15 percent of premium. The budgeted premium for 2024 is $7.1 billion. So, 15% of that is $1.067 billion. So, you would not hit an emergency assessment would not kick in until $17.78 billion, which is way above the 1-in-100. There is way more, there is about $600 million more of Citizens' policyholder surcharge above the 1-in-100 before you hit the emergency assessment. This was all of the policyholder surcharge, and the emergency assessment was right after that and it is not, just FYI. There is no action item on this. This is more just to show you what the layer chart looks like based off what the budget numbers are. We will be going to the market, and typically at our March meeting which I believe has been moved to April, we will come back to the Board with this yellow that will be sliced and diced and layers and look like the PLA and the coastal account did with recommended Cat bond stuff and recommended traditional market, and we can come book with pricing, et cetera, that we are seeing in the market, and then, of course, we always have a special Board meeting around the May time period where we come to the Board for a specific approval for the spend. The budget is not the approval for the spend, it is just a placeholder so that we can complete the budget. Any questions on the layer charts?

Chair Knight: Questions? Thank you. That leads us into our action item to approve the redemption on the 2022 Everglades Re Cat bonds.

b. Redemption of the 2022 Everglades Re II CAT Bonds [AI]

Jennifer Montero: Yes, so this is the Everglades Re II, series 2022-1 Cat bonds were issued in 2022 for coverage of $200 million for the benefit of personal lines account only with maturity date of May 19th, 2025. The bonds were structured with the optionality to account for the potential of merging the accounts. So, this gives flexibility to redeem the bonds without any additional call premium. So once the accounts are merged, Citizens can call the bonds after April 30th of 2024, and the reinsurance contract will be terminated for the third annual risk period from May 15th, 2024, to May 19th, 2025. And the reason that we want to do this is because we want to merge the accounts, and this is specific to the personal lines account. We call this and then that will be part of our restructuring and we would like to restructure on a consolidated basis on the combined account basis, any Cat bonds or traditional reinsurances going forward.

(Recommendation: Staff proposes that the Finance & Investment Committee review, and if approved recommend the Board of Governors: a) Approve the recommendation to call the 2022-1 Everglades Re II Catastrophe Bond of $200 million without a call premium; and b) Authorize staff to take any appropriate or necessary action consistent with this Action Item.)

Governor Lydecker: Would the Chair entertain a motion?

Chair Knight: Yes.

Governor Lydecker: **So moved.**

Chair Beruff: **I will second.**

Chair Knight: **Okay, any opposed? Okay, the action item for the redemption of the Everglades Re II series 2022-1 catastrophe bonds was approved**.

Jennifer Montero: Thank you.

Chair Knight: Moving on to the annual review of the charter.

c. 2024 FIC Charter – Annual Review

Jennifer Montero: Yes. We bring the charter for the Finance and Investment committee to the committee once a year just to see if we need any updates or edits. Staff does not have any edits or comments. No updates are recommended by staff, but I am happy to hear if the committee has any changes they would like.

Chair Beruff: Madam chair, I have a question. Does the charter dictates where our investment strategy is?

Kapil Bhatia: Yes, it allows the Board to come to the investment quality review. You approve the investment -- it is all there.

Chair Beruff: How much does our investment policies differ from the state pension fund investment policy?

Jennifer Montero: That is long term, and we are short term.

Kapil Bhatia: The state pension fund, has different policies in the sense that they invest, based on my understanding of the state pension fund, and SBA also manages the money for the Florida Hurricane Catastrophe Fund. Their investment policy is different. They have the other accounts which are short duration. So, they have multiple investment policies, but the pension fund allows them to invest in real estate and global securities. Equities and everything and it is meant to be because their liabilities are known effectively because they know when the people are going to retire, not based on the age formula. So, it's more based on the life cycle than the property and casualty policy. So, it is very different.

Chair Beruff: I articulate the better question, you mentioned that it also manages it for the Cat Fund.

Kapil Bhatia: Correct.

Chair Beruff: How much does our investment policy differ from the Cat Fund investment policies they have?

Kapil Bhatia: For the record, we are also financial adviser to the Cat Fund.

Chair Beruff: So, you should be able to answer the question.

Kapil Bhatia: So, their investment policy, our liability structure goes up to 1-in-100 years as you saw in the layer charts. However, they have a limited liability of $17 billion. So, their liability structure is different. Their portfolio has a relatively shorter duration in fixed income securities, and based on their asset balance, it is much shorter than ours.

Chair Beruff: So, their investment criteria is less broad than ours?

Kapil Bhatia: Correct, because typically they are stronger in ratings with shorter duration.

Governor Lydecker: So, they got lower than a 2.2% return.

Kapil Bhatia: Last year?

Governor Lydecker: Last year.

Kapil Bhatia: Because the yield curve has been inverted –

Governor Lydecker: I assume where you are going with that is increased flexibility you had to get more than a 2.21% return.

Kapil Bhatia: We expect our income to be this year to be approximately 3%, and Jennifer will go through that because that is of September.

Chair Beruff: The only reason I want the Board to think about it is, is there any mechanism that we could change, whether it is policy at this Board level or statutorily that would give you broader parameters to investments that would give us a better yield?

Kapil Bhatia: I think we have, Mr. Chairman, we have all the flexibility. We expect next year's income to be over $400 million. You will see that in the budget.

Chair Beruff: No, no, I am not complaining about where we are at. I am just wondering if there is anything that we could do as a Board or legislatively change that would give you a broader path to invest in the future, but still consistent with liquidity and all of the rest of the parameters that we take for granted that we know we have to have. We have to have liquidity to be available when we need it.

Kapil Bhatia: I believe at this time we have all of the necessary tools because we have three different policies, liquidity fund, claims paying funds and long duration claims paying fund.
We have spent quite a lot of our resources to pay claims from Irma and Ian and the market movement, but we have -- the policy allows us complete flexibility within the legislative constraints and what the statute allows to maximize the investment income. So, at this point in time, we have not, but we are happy to walk you through –

Governor Lydecker: Maybe another way to ask the question is notwithstanding our short-term liquidity needs we are investing on, on the thesis, on 2.8 years. What if we said three and-a-half years? Like if we changed the underlying criteria a tad, would that -- how would that change, because I know it will, how would that change the investment thesis. Is it 3% or 4% return given what we know about the market today, you know. We are at 2.2% return.

Chair Beruff: If I could add on that comment. So, we know that we can bridge liquidity, right, because we did it this year. We can bridge liquidity, but by adding six months or nine months to our investment window, would that help your return significant enough so that we could bridge liquidity from a year-to-year basis like we did with the $1.25 billion line of credit we took out this past year?

Governor Lydecker: What percentage point to $100 million?

Kapil Bhatia: Our investment policies allow us to go up to five years in duration in claims paying fund and seven years in long duration. It depends on whether we are going with a claims paying fund or the long duration claims paying fund. We have been intentionally shortening our portfolio firstly because of market conditions as I mentioned earlier negative mark to market value. And secondly, yield curve is inverted. So, the one-year treasury rate is higher than five or seven years. So, there is actually a negative inversion. As our portfolio matures and we get more premium, we will be able to extend our duration once the yield curve becomes normal. That will allow us to increase our investment income as we are going from 3% in 2023, we are projected to increase to 4% next year to probably over 4% after 2024.

Chair Beruff: I am going to get a little whimsical, Madam Chair, if you will allow me. It is the holiday season. If you had a magic wand, is there anything that you would want to change, whether it is statutorily or policies of this Board that would make you feel better about the parameters that you have to invest?

Governor Lydecker: The answer has to be yes.

Kapil Bhatia: If I have a magic wand, if we can have Fed do its job quickly and faster and fiscal deficits are differently behaving, assuming I have a magic wand, but the investment policy has given us all of the tools. It is just that the markets have been behaving irrationally over the last 18 months because of what Fed is doing and the economic slowdown. I think you have given us all the tools. So, we can my magic wand or our magic wand is not going to work in Washington, but monetary policy and fiscal policies once they become normal –

Chair Beruff: I gave you too much power with the magic wand.

Kapil Bhatia: Yes. So, you have given us all the tools. We are happy to share the investment policy. We are intentionally shortening our duration to maximize the investments.

Governor Lydecker: I think we should, you are saying it is an investment policy issue. It may be an investment strategy issue, and do we need to revisit your investment strategy?

Kapil Bhatia: We will come back to you once we have our reinsurance program in place and see how it was and see how much cash we need below the Cat Fund, because if we need something in that first ten years, we would rather be liquid instead of going up to the market and borrowing it at a higher rate. Anything above the attachment point of our reinsurance program which Jennifer just went through it, or anything above where the Cat Fund attaches, we can go longer and maximize the income once the yield curve becomes normal, and we will approach that. So, we are trying to match our assets and unknown liabilities to maximize the investment income, and I think that we are there. So, you have given us all of the tools over the last couple of years, it is just that the market has not been working with us, but we will suddenly come back to you if we think we can maximize –

Governor Lydecker: Madam Chair, I for one think that we could ask for recommendations for enhancing our returns and we can then check the tolerance of the Board and our financial adviser recommendation at that point. Risk tolerances.

Chair Knight: Understood, noted. What month would you like to come back to us on some of that review of the investment policy?

Jennifer Montero: We usually bring the investment policies to this committee once a year. So, I think March has been moved to April. To the next Board meeting whichever one is the next Board meeting.

Governor Lydecker: This doesn't take very long, right. It is a game of percentages.

Jennifer Montero: We won't have as many because the account will be combined now.

Chair Knight: I think it will be beneficial to do, like you said, in conjunction with going out to market and buying reinsurance, et cetera.

Kapil Bhatia: That is right, Madam Chair.

Chair Knight: **So, if we can then continue with this action item on just the charter, the construes, rules, responsibilities of the committee, realizing we are going to pull aside and dig deeper into our responsibility and authority for the investment policy statement at the March or April meeting, whenever it happens. Apart from that, do I have a motion to approve?**

Governor Lydecker: **So moved.**

Chair Knight: All right, any opposed? **Okay, then we will adopt the charter,** the review of it as of the committee, thank you.

d. Investment Portfolio Update

Jennifer Montero: Thank you. And my last item is the investment portfolio update. So, the total portfolio is $9.78 billion with approximately $8.25 billion or 84% externally managed by ten investments managers. The remaining $1.53 billion or 16% is internally managed and primarily consists of liquidity for claims, operating funds, debt service funds and debt service reserve funds. Internally managed funds are invested in short term U.S. Treasury securities or money market funds. The taxable portfolio is $9.5 billion or 97% and the tax-exempt portfolio is $280 million or 3% of the total portfolio. The portfolio is very conservative and stable with sufficient liquidity to pay any current or potential future claims. The total portfolio average duration is just over 2.73 years and continues to decline. The annualized net income return for the past five years is approximately 2.55% annually. The 2022 net income return was 2.21% and the year-to-date October 2023 net income return is 2.41%. On slide two, treasury rates have exponentially increased over the last 18 years, I am sorry, 18 months. However, in November they started to come down. The increase in rates reflects the Fed's 11 rate increases to the current Fed funds rate of 5.25 to 5.5% which Kapil mentioned earlier. The Fed is done with increasing rates as inflation has started to come down. The yield curve is still inverted. The current two to 10-year spread is negative 34 basis points and the three-month to 10-year spread is negative 115 basis points. Both spreads are still at significant negative levels as the financial markets are still expecting a slowdown or even a recession. The tax-exempt rates have also increased. On slide three –

Governor Lydecker: Could I just ask a question?

Jennifer Montero: Sure.

Governor Lydecker: Year over year, shouldn't our, shouldn't our net income return in the form of a percentage have improved this year versus declined? Because a third of your portfolio is renewing within a higher interest rate environment. I am just reflecting on the page before, the 2021 to 2022.

Kapil Bhatia: Governor Lydecker. So, two points to that. The 2022 net income return for the whole year was 2.21% as Jennifer said, and so far, year-to-date of October returns is 2.41%. So that –

Governor Lydecker: I missed that.

Kapil Bhatia: Year-to-date, October 2023 returns. It is a 10-month return. It is 2.41%. So, we have 20 basis points more, but still two months to go.

Governor Lydecker: Got it.

Kapil Bhatia: We expect our '23 income to be 3%. In addition, even though a third of our portfolio has turned over, we used part of our turnover portfolio to pay Ian's claims because we are not taking any mark to market losses, all of that stuff.

Governor Lydecker: The term return, this is a pure return. This is –

Kapil Bhatia: But some of the securities maturities which mature –

Governor Lydecker: Yes.

Kapil Bhatia: -- we pay the claims. So, we don't get to reinvest at a higher rate.

Jennifer Montero: So, once they mature, we take a cast and put it to the side when we have a hurricane.

Governor Lydecker: Yes.

Jennifer Montero: Because if we have to take any of the fixed income and cash it out, we are going to take huge losses. Those are the unrealized losses.

Governor Lydecker: Yes. So that sounds like a, you know, really thoughtful way of doing it, but year over year, I guess.

Kapil Bhatia: We have 80 basis points of incremental -- income.

Governor Lydecker: So, you are saying by year end it would reflect a 3%.

Kapil Bhatia: Correct, as we say it and Jennifer will go through that, but that is our projections of three percent by the year end and the total return will be four percent. And next year we project –

Governor Lydecker: Okay.

Kapil Bhatia: -- 3% to 4%.

Governor Lydecker: Thank you.

Jennifer Montero: Turning to slide three. Both the taxable and the tax-exempt portfolios have very strong credit quality. Over 79% of the taxable portfolio is in money market funds are rate A or higher. 100% of the tax-exempt portfolio in money market funds are rated A or higher. And approximately 48% of the total portfolio is in treasury and agency securities or in money market funds. And then the final slide, slide four, the portfolio income return is stable, and we expect the income return for 2023, to be approximately 3%. As we continue to get the incremental interest income from rising interest rates with increase investment in short durations severities. We expect 2023 total return to be over 3.5%, however, the portfolio still has negative mark to mark value, but it is declining as interest rates are coming down and our portfolio is naturing with declining duration. We expect our 2024 total return to be over 4%. And that concludes my report unless there are any other questions.

Governor Lydecker: Thank you.

Jennifer Montero: Thank you. That is all I had.

Chair Knight: Ok, Any new business? Thank you. The FIC December 5th meeting is adjourned. Thank you.

Whereupon, the meeting was adjourned.