



**MINUTES OF THE MEETING
OF THE
STATE TREASURER'S INVESTMENT COMMITTEE (STIC)
Bob Barth Conference Room
Wednesday, June 10, 2009**

CALL TO ORDER AND ROLL CALL

A meeting of the State Treasurer's Investment Committee was called to order by Mark Valdes, Chairman Designee, at approximately 9:00 a.m., in the Bob Barth Conference Room, at the Office of the State Treasurer, 2019 Galisteo Building K, Santa Fe, New Mexico. Roll call revealed a quorum of the membership in attendance as follows:

MEMBERS PRESENT

Mark Valdes, Chairman Designee and Deputy State Treasurer
Scott Newman, Interim Chief Investment Officer
Stephanie Schardin, Designee for Olivia Padilla-Jackson, State Board of Finance Director
Steve Bohlin, Public Member
Paul Cassidy, Public Member

MEMBERS EXCUSED

The Honorable James B. Lewis, State Treasurer
Olivia Padilla-Jackson, State Board of Finance Director

STAFF PRESENT

Joaquin Lujan, BPIP Portfolio Manager
Orlando Romero, State Cash Manager
Arsenio Garduno, Collateral Officer
Randilynn M. Lord, Legal Counsel & PIO

OTHERS PRESENT

Frank Rendon, Local Government Division, DFA
Becky Lopez, Local Government Division, DFA
Gillis Lang, DFA Economist
Isaac Montoya, Local Government Division, DFA
Dan White, LFC Analyst
Roger Beaty, Los Alamos County
Melessia Helberg, Committee Stenographer

NOTE: All items in the Committee packet for all agenda items are incorporated herewith to these minutes by reference. The original Committee packet is on file



in the Office of the State Treasurer.

INFORMATIONAL

1. ACTION ITEM – APPROVAL OF JUNE 10, 2009 AGENDA

MOTION: Member Cassidy moved, seconded by Member Designee Schardin, to approve the June 10, 2009 Agenda, as presented.

VOTE: The motion was approved unanimously on a voice vote [5-0].

2. ACTION ITEM – APPROVAL OF MAY 13, 2009 MINUTES

The following corrections were made to the minutes of April 8, 2009:

Page 1, under “Others Present” correct as follows: “Woody ~~Barber~~Farber New Mexico ~~State Loans~~Student Loans”

Page 1, under “Others Present” correct as follows: “Stephanie ~~Gardin~~Schardin”

Page 4, paragraph 1, line 4, correct as follows: “.. Mr. ~~Ms.~~ Padilla-Jackson...”

Page 4, paragraph 1, line 4, correct as follows: “..the State Treasurer should look, at minimum, at reducing exposure ~~not necessarily~~ if not eliminating it.”

Page 7, paragraph 5, line 4, correct as follows: “...the average bank balance is...”

Page 10, paragraph 2, line 4, correct as follows: “... He She...”

Page 10, paragraph 2, line 6, correct as follows: “..spend this down soon...”

Page 10, paragraph 2, line 12, correct as follows: “..that will work exactly.”

Page 20, paragraph 3, under “Question Period,” correct as follows: “..Mr. ~~Barber~~Farber...”

MOTION: Member Cassidy moved, seconded by Member Designee Schardin, to approve the minutes of the meeting of May 13, 2009, as amended.

VOTE: The motion was approved unanimously on a voice vote [5-0].



INVESTMENT REPORTS

3. INFORMATIONAL – GENERAL FUND INVESTMENTS

Scott Newman, Interim Chief Investment Officer, reported on General Fund Investments from the materials in the Committee packet, highlighting information as follows:

- The market value of the General Fund Investment Portfolio, net of TRANS, on May 31, 2009, was \$1.63 billion, representing a decrease of \$9 million, or 0.55% from April month end.
- The purchase yield decreased to 1.46% at month-end, down from 1.58% in April. The weighted average term of the portfolio decreased to 305 days. Effective duration of the CORE segment was 1.15 year, which is 58% of the benchmark's duration at 2 years.
- Investment activity for the CORE during May, included the purchase of \$40 million in government guaranteed asset-backed commercial paper and the sale of \$250 million of treasury securities, which resulted in gains of \$563,000. These trades were made to realize gains in anticipation of higher interest rates and for liquidity purposes. Additionally, \$13 million in CDs were renewed in the LIQUIDITY portfolio.

Mr. Newman said we are going to talk about this government guaranteed asset-backed commercial paper. It is a recurring theme and we purchased it through every single portfolio last month. This program was the first of the government guaranteed student loan commercial paper which was done using FFELP paper. It is very similar to what we were doing with NMEAF, yet the government is taking our place in this. He said there was a question this morning from Olivia on this paper as A1P1plus rated. He said we bought basically our maximum throughout all our portfolios in the first go-round. It was a substantial pick up to treasury bills, roughly 20 basis points.

- The General Fund earned yield was 2.12% month end, compared to the CMT index of a 2.06%. Total return for the CORE was 10.03% for the month of May compared to 2.43% for the benchmark. We saw tremendous tightening in the non-guaranteed corporates that the benchmark does not have, explaining most of our over performance.
- WAM for the General Fund decreased to 305 days, and the effective duration of the CORE remained unchanged at 1.15 years.
- Earnings were \$2.53 million for the month and the year to date earnings are \$72.42 million. He spoke with Dan White about this earlier in the week, and we are still tracking pretty closely to revenue estimates



from the LFC.

Member Cassidy asked for an update at some point during the meeting on the cash flow pro forma exercise which was discussed at the previous meeting. He said it would be helpful, in light of the fact that the General Fund market value continues to decline, but evidently was expected.

4. INFORMATIONAL – LOCAL GOVERNMENT INVESTMENT POOL (LGIP)

Scott Newman presented information regarding this matter from materials in the packet, highlighting information as follows:

- May 31st market value of the LGIP was \$964 million, compared the market value of \$1.7 billion at the same period last year, and \$972 million at the same period two years ago.

- During the month the market value of the portfolio decreased by 18%, from \$1.17 billion at April month end to \$964 million. Participant contributions for May totaled \$54 million and withdrawals totaled \$268 million. The big number for withdrawals last month was due primarily to two accounts representing basically \$125 million of those deposits from two depositors. He said the big depositors were expecting this, in the sense that our strategy for the past two months was to concentrate on safety and liquidity, and as a result, we are trailing our benchmark of the national rated government investment pool because we are not taking as much risk as they are. We have a ladder of bills, guaranteed investments, and as a result, our yields are trailing. He said the big ones “flat out” told us they’re looking for more yield elsewhere.
- The gross yield was .30% at May 31st, which is a 3% decrease from April month-end yield of .31%. The weighted average maturity at May 31st was 43 days, down from the April 30th WAM of 50 days, and well within the rule 2a-7 requirements.
- May purchases in the LGIP portfolio totaled \$125 million, and included both the Straight A funding ABS commercial paper we discussed early and a combination of bills and notes which have rolled down the curve within the 2a-7 space.
- Earnings for the month totaled \$258,000, which is a decrease from April earnings at \$327,000. He said there is a lower interest rate environment and smaller balances.
- FY to date earnings are \$18.6 million compared to \$48 million



through the same period of last year. He said we are in the 5% yield range at this point last year, and now we are below 50 basis points.

- The 30 day net yield of LGIP as of May 22nd was 25 basis points. This under-performed the 30 day net S&P rated government investment pool index of 49 basis points. The 30 day gross yield at May 22nd was 30 basis points which under-performed the 30 day gross yield of the S&P index of 68 basis points.
- The administrative fee assessed for May was 3.7 basis points, and year to date fees collected through May are \$288,000.

Member designee Schardin noted from the chart that the LGIP balance has been somewhat consistently declining over the course of this fiscal year. She asked if he has any sense of whether those declines are more recently due to those wanting to find greater yield elsewhere, and more generally, wondering if this is a reflection of declining cash balances in local government budgets.

Member Newman said Ms. Schardin's observations are kind of the sense that they are getting. He said the big big withdrawals have been by participants looking for additional yield. He said other than that, the sense he's getting is that it is for operating expenses. He noted there were roughly \$10 million of withdrawal requests yesterday, and of those, 9 of the requests were based on operational needs. He said there has been somewhat of a lag in participants pooling funds to go after yield as they become more educated on what is happening. He believes we have already seen all of the bigger withdrawals.

Isaac Montoya, Local Government Division [LGD], said, in terms of what local governments are doing, they're not necessarily changing yield, but they are going to CDs because of the fee structures here. He said the spread is better for them. He said you logically need to increase the liquidity requirement, lowering your yield, because you have to have the monies available for that purpose. He said Local Government Division has noted that those entities are going to the bank and get a better spread as opposing to chasing yield specifically.

Frank Rendon, Local Government Division, asked if this pool had \$1.7 billion at the end of May last year, and now we have \$964 million. Mr. Newman said this is correct. Mr. Rendon said some of that is due to withdrawals for operational purposes or other reasons, and asked how much of it is lost on investments and how much is due to withdrawal.

Mr. Newman said it is 100% withdrawals, and those take two forms: one is for operational purposes and for other purposes we've discussed, and the others were due fully to the bifurcation of the LGIP between the LGIP itself and the Reserve Contingency Fund. Those assets being held in the Reserve Contingency Fund are not considered a part of the LGIP at this point. He said when, and if, those funds are



converted to cash from the Reserve Primary Fund, they will eligible to be redeposited into the LGIP. He said currently, the outstanding amount in the Reserve Contingency Fund is roughly \$39 million. Mr. Rendon said, then the other amount has been withdrawals by participants.

Member Cassidy said it might be helpful for the Treasurer's Office to brief LGD staff, as they have the participants around the state, so Local Government Division staff, who are on the front line with our local governments understand what we're doing and also what our participants are hearing from the Treasurer's Office.

Chair Valdes said the Treasurer's Office would be happy to brief the LGD, noting this is the entity which approves all of the financial activities of local governments.

Chair Valdes said, for the benefit of members and visitors, the Treasurer's Office is anticipating putting together a stakeholder committee composed of representatives from counties, municipalities, District Courts, an Indian tribe, colleges, universities and schools, and will have a membership of ten members. He said it will probably meet twice a year. He said if this is done at the end of the fiscal year, we could report fiscal year reports to this committee and get participation and comments. Treasurer Lewis said he wants to know where the stakeholders believe we should be going with this fund in the future. He said everyone else will be welcome to attend those meetings, and if necessary can meet at the Capitol or elsewhere, where there is a larger meeting space.

Member Newman said he can brief the LGD representatives after the meeting today, if they are available, on the LGIP over the past three months, or it can be scheduled at a future date.

5. ACTION ITEM – LOCAL GOVERNMENT INVESTMENT POOL BANK CD HOLDINGS

Randilynn M. Lord, Legal Counsel & PIO, said she is bringing a matter to this Committee regarding LGIP investments which appear to be contrary to the two policy sections, as outlined in the Memorandum at Tab 5 in the Committee packet. She said staff is seeking clarification of the Committee's interpretation of these sections, and based on that, the Committee suggested actions to achieve conformity with the policy if necessary.

Ms. Lord said, before submitting this to the Committee for questions and discussion, it would be helpful to provide more background to the Committee.

Member Newman said the first thing he would like to discuss, is the



interpretation that only the General Fund portfolio can hold CDs. He said two CD investments were made in December 2008 or January 2009, before this came to their attention. He said the market conditions at that time were pretty bleak, and there weren't a lot of short term alternatives at that point, and we needed to put some money to work in the LGIP. He said both Compass Bank and Wells Fargo came to us with some very attractive rates on CDs. He said these are no different from any of the CDs they hold in the General Fund, in terms of structure. He said the position from Wells Fargo matures December 30, 2009, and yields 1.63 and the Compass CD yields at 2.10, maturing on December 15, 2009.

Member Newman said there is an interpretation "flat out" that we are unable to make CD investment at all with our custodial banks. He said we have some clarification on this. At this point, Wells Fargo remains a custodial bank. He asked Mr. Garduno to talk about the custodial issue.

Arsenio Garduno, Collateral Officer, said Wells Fargo has two entities, one is a depository and one is a custodian. He said this is a little different than a CD being invested in a custodial bank, and it isn't really being held at the custodial, it is in the depository.

Member Newman said this case, the CD was issued by the depository and not the custodial side, so we do have some room there. He said, with each of these, based on a strict interpretation of the section which provides, "CD deposits shall only occur in the general fund portfolio," he submits that we are in violation of that.

Member Newman said, in terms of proposed remedies, these CDs do have a put option, and we can put them back to the bank. However, he would suggest that we do not do that. He said this provision is there for our protection, but it is a clause which in his knowledge has never been exercised, and he believes it could lead some bad will down the road and set a precedent with the banks that we may not want.

Member Newman said the other two options are: (1) acknowledge that a violation was made and that we won't do it again and let these CDs roll off. Currently these are the two highest yielding securities in the portfolio, and it would affect the yields paid to the LGIP quite a bit; and if this isn't acceptable to the Committee, he would suggest (2) that the General Fund would be more than happy to purchase these CDs from the LGIP.

Chair Valdes noted the Policy states: "The Committee will identify potential violations of and suggest remedial actions to achieve conformity with the investment policy." Chair Valdes asked the Committee members their thoughts.

Member Bohlin said the CD program we have for the General Fund is primarily to benefit local banks, and we basically accept this as a sub-market rate with lower



collateral requirement from local banking institutions. He said this was put forth by the Legislature as a mandate for the State Treasurer's Office to help local banks. He said the language which states that it will be just for the General Fund portfolio was specifically for that program of local banks within the State. He said a CD is an investment as well, and you are looking at it in the LGIP along those lines, as opposed to this program which was mandated by the Legislature to help local banks.

Member Bohlin said this is one way in which having a separate investment policy for the LGIP could make sense. He said there are opportunities in the market place where national CDs make great investment sense, and this is just such an opportunity. He said this wasn't done in the same spirit as what is contemplated in the investment policy for the General Fund. He doesn't believe these are bad investments, although we are in violation by having the LGIP invest in CDs. In the long run, we want the LGIP to be able to invest in CD's, just not under this program mandated by the Legislature.

Member Schardin asked if these two CDs purchased for the LGIP are below market rate, as would have been purchased for the General Fund, or were they purchased at market rate.

Member Newman said, at the time, these CDs were considerably higher than anything else in yield that we could get. It should be noted, based on collateral policy, that the CD with Compass Bank is 100% collateralized. The CDs at Wells Fargo, under its collateral requirements, are collateralized at 50%. He said these are still considerably higher than what the market bears.

Member Cassidy asked if the rating agency requirements on the LGIP were ever in jeopardy, and did we violate any of the rating agency requirements for AAA.

Member Newman said no, we are fully in compliance with the AAA ratings guidelines with S&P.

Member Cassidy asked if we move this from LGIP to General Fund, is there room within the General Fund, in terms of the limits of our investment policy. Member Newman said yes.

Joaquin Lujan, Investment Officer, Bond Proceeds, asked, for the record, and for his and others edification, what was the original interpretation under which these CDs were purchased.

Member Newman said his predecessor made this investment decision and he was not privy to that information.

Mr. Lujan said it seems the original interpretation was along the lines of what



the board members were asking, and Member Newman said, "Correct."

Member Bohlin said we did change the investment policy to exempt the LGIP from being required to participate in this CD program some time back, and we changed the language to say "only in the General fund."

Ms. Lord said in 2005 this language first appeared in the investment policy by the STIC committee.

Member Bohlin said he is familiar with the spirit of that change, which was since the CD Program offers below market rates to local banks, it would not be appropriate for the LGIP, and Mr. Newman said, "Correct."

Paul Cassidy asked Ms. Lord if there is any room in the investment policy to allow this Committee, in terms of direction to staff, to leave these investments in place as opposed to having to move them. Is there discretion or a waiver? He said these are the kinds of investments which our local governments would make anyway if they weren't putting money into the LGIP, and these are the banks in which our communities would be qualified to invest. He said these remarks are for the record.

Ms. Lord said she believes this would fall under the section identified by the Chair as the Committee's purview in identifying violations and recommending actions, whether to achieve conformity or what the Committee feels would be the remedial action which could be taken, whatever that may be. She believes that falls within that section. In terms of an express waiver, she doesn't see one in there, but again, it falls within the Committee's advisory capacity to make the recommendation on this particular issue.

Member Schardin asked if the policy provides that the Committee's role is to recommend an action that brings us in conformity with the policy or a remedial action, or is our role limited to bringing it back into conformity.

Ms. Lord quoted the exact language from Paragraph 2, Section F, "Identify potential violations of and suggest remedial actions to achieve conformity with the Investment Policy." She said the answer to Member Schardin's question is that it is to bring it into conformity. She said there is no express waiver in the policy.

Member Cassidy said it would be nice to leave the CDs in the LGIP, for all the reasons which were mentioned by staff as well as the Committee. He asked if this would be a finding in an audit of the State Treasurer's Office.

Ms. Lord said she believes it will be considered an audit finding in the record.



Chair Valdes asked Member Newman to summarize the discussion before we decide what to do in this matter.

Member Newman said we have made the facts quite clear “of where we are here.” He said the three options we have: (1) make a recommendation to leave these two investments as they are, and note that they are an exception, and that we more than likely will get an audit finding on them, and address this issue when we look to create a separate investment policy for the LGIP; (2) sell these two investments, and the General Fund would be more than happy to purchase them; or (3) to put these two CDs back to the issuing banks.

Chair Valdes said Member Newman mentioned it would be a problem for us in the future if we choose the third option, and asked him to comment in this regard.

Member Newman believes it could cause problems. He said we have good relations with all these financial institutions. He believes the independent bankers and the State Bankers Association could see this as precedent in terms of calling CDs. He said, this being said, as a staff member and portfolio manager for these funds, his recommendation would be: (1) to view this as an exception; and if this isn't acceptable, his next recommendation would be (2) to sell the CDs to the General Fund.

Member Schardin said the main downside risk to selling the CDs to the General Fund is there is a loss of yield for the LGIP, and Member Newman said this is correct. She asked if it is possible for the General Fund, in turn, to sell something to the LGIP – if they could almost trade and the LGIP ended up with something else which is in compliance.

Member Bohlin said cross-sales are required to be done at market value, which has to be independently verified, so we can sell the CDs to the General Fund and there would be a profit, although small because it is now a 6 month piece of paper. He said to replace it with something else, you'd also have to purchase at the lower yield. He said as much as he dislikes it, he believes we have to do the sale. He wants to push forward on the LGIP investment policy as a separate document, because there really are different mandates for the LGIP. He said the bond proceeds in the General Fund are more closely aligned than the LGIP. It would make it easier for LGIP participants to discern what we are doing when they don't have to read the entire investment policy for the Treasurer's Office for the various pools it is running and pick out what is and is not allowed in the LGIP. He is sure we are not going to be in violation of any 2a-7. He said there was no maliciousness in the investment and it was a good investment opportunity which was taken, but it was in violation of the LGIP portion of our Investment Policy.

MOTION: Member Bohlin moved that the LGIP sell the two CDs that are in violation of the investment policy for the LGIP to the General Fund or to the open market. [There was no second to the motion].



DISCUSSION ON THE MOTION PRIOR TO SECOND: Member Newman said these are not negotiable CDs, so they would have to be done in-house.

Member Bohlin said in order to do that you would have to receive the equivalent of three bids, noting since they're non-negotiable you can't actually get a bid, but you can get an indication.

Member Cassidy said there is a very active market in secondary CDs. He said we have full collateralization on the Compass Bank CD which he believes is in the A rating category, and Wells Fargo complies as a AA rated bank, but at a 50% level. He would think we can approach market by looking at the secondary, and he is sure there are screens on Bloomberg that can tell you where that is, and he proposes we do that if we go forward with this, if this is acceptable to the Committee.

Member Bohlin said he would find that acceptable.

Member Schardin wants to make sure that we are in within our role in the way the motion is worded. She heard that the motion is to sell. She said the policy is that the STIC is to meet monthly, and one of its duties is to identify violations and suggest remedial action. She wants to make clear that we are advisory and not actually directing the transaction.

Ms. Lord clarified that it is within the role of this Committee to advise on the remedial action, and thanked Member Schardin for making this point.

Chair Valdes asked Member Bohlin if he would like to restate his motion.

RESTATED MOTION AND SECOND: Member Bohlin moved that the State Treasurer's Investment Committee recommend to staff that staff use the Bloomberg electronic trading system to find the market value for the two CDs which are in violation of the LGIP investment policy, and use those indications to sell the CDs to the General Fund. The motion was seconded by Member Cassidy with an amendment to the motion to say that this will be done prior to June 30, 2009, and in terms of audit findings, that it is properly noted that this Committee is taking action just as soon as it was made aware of this violation.

DISCUSSION: Member Cassidy thanked staff for pointing this out and bringing it before this Committee as soon as they knew about this.

Ms. Lord thanked the Committee for hearing staff on this matter.

ABSTENTION: Member Newman said as staff, he will be abstaining from the vote.



VOTE: The restated motion, as amended, was approved on a voice vote, with Members Valdes, Schardin, Bohlin and Cassidy voting in favor of the motion, none voting against and Member Newman abstaining [4-0-1].

6. INFORMATIONAL – TAXABLE EXEMPT BOND PROCEEDS INVESTMENT POOL (BPIP)

Joaquin Lujan, Investment Officer, Bond Proceeds, reported on Taxable Exempt Bond Proceeds Investment Pool (BPIP) from materials in the packet, highlighting information as follows:

- The Tax-exempt BPIP portfolio as of May 31, 2009, was \$738.5 million which compares to \$524.9 million and \$547.6 million, one and two years ago, respectively.
- The increase is due exclusively to \$219 million received in new issue proceeds and the net of \$738.5 million also considers \$15 million in project expenditures.
- The month end purchase yield and term were 1.12% and 220 days. The month end yield was below the 2-year constant maturity agency index of 2.43%.
- The composition of the portfolio is listed on page 48. During May, commercial paper was purchased for the portfolio, substantial pick to bills and agency discount notes. There is almost a 68% concentration in case, roughly \$210 million of which were cash proceeds from the sale of the TLGP bonds and \$219 million from the new issue proceeds which came in on May 28th, so as of this report there wasn't enough time to put all that money to work. They are implementing strategies, as we speak, to get this cash put to work.
- Interest earnings for the month totaled less than \$1 million, a decrease from April earnings of \$3.41 million. The fluctuations seen are mainly a reflection of realizing gains in the high months and in the low months, lower yields on lower asset base.

Member Bohlin asked what is the approximate cash position at this point.

Mr. Lujan said at this point it is still in the high three hundreds. He said staff is looking at a strategy to implement a short treasury coupon ladder to use it in and looking at the option to re-enter the commercial paper market.



7. INFORMATIONAL – TAXABLE BOND PROCEEDS INVESTMENT POOL (BPIP)

Joaquin Lujan, Investment Officer, Bond Proceeds, reported on Taxable Bond Proceeds Investment Pool (BPIP) from materials in the packet, highlighting information as follows:

- The taxable pool at the end of May was \$791.4 million compared to \$648 million and \$678 million two years ago.
- During May the portfolio decreased by about \$9 million due to project expenditures. He said we have been anticipating higher numbers for two months, but finally got a draw request two days ago for \$69 million, which will be a substantial draw and bring us back in line with the historical flows we've seen in this pool.
- The month end purchase yield and term was 1.87% and 1 year respectively.
- The month end purchase yield was 56 basis points below the 2-year Constant Maturity Agency index.
- The composition of the portfolio is listed on page 59 of the packet. Purchase of commercial paper, and a very high balance in cash which are the unspent proceeds from the sale of the TLGP bonds during April. Much the same thinking as in the tax exempt pool putting the money to work out the treasury ladder and out the treasury curve a bit, 2-3 years approximately, and the rest of the cash trying to earn some pick to discount notes and treasury bills and corporate commercial paper, insofar as we find the opportunity.
- May interest earnings totaled \$1.52 million, a decrease from \$3.41 million in April.

Member Cassidy observed that our investment yields are well below the benchmark, and it is expected short term rates to rise, noting we are at the short end of the duration target with the idea that we would be reinvesting when rates rise, noting this is 56 basis points below the target.

Member Newman noted that we are looking at the earned yield vs. the constant maturity treasury index and not the total return numbers. In terms of total return, at this point, with the exception of the LGIP, all portfolios are exceeding their benchmark returns.

Mr. Lujan said those numbers are in the sub 5% total return for the year, noting this can be seen in the tax exempt portfolio on page 60 of the packet. He had been reporting the 1 month/3 month/quarter.



FY/YTD/three years versus its benchmark as required by policy. There was a glitch in the Northern Report which is supposed to do this automatically, and those will be in next month's report.

Mr. Newman said we are working very closely, and our advisor Davidson, has been instrumental in working, with Northern to come up with a comprehensive set of reports, but staff isn't prepared to present those now, but those will be coming shortly.

Member Cassidy said then we have been shortening, taking profits and sitting on cash, with the idea that we would be extending at some point in the future.

Member Newman said this is correct, noting the LFC and Board of Finance brought this to his attention – the revenue shortfalls which the State is experiencing currently. As a result, liquidity is at a premium right now, and that, in combination with an anticipation of higher rates has changed out outlook to shorten the portfolio through fixed maturities and using floating rate paper as well as getting considerably more liquid in terms of what we are buying.

8. INFORMATIONAL – SUMMARY OF BROKER PARTICIPATION

Scott Newman presented information regarding this matter from the materials in the packet under tab 8, Summary of Broker Participation, on page 72 of the Committee packet.

Mr. Newman said we are carrying the same exact trends we've been carrying the last several months in concentrating these purchases in a few dealers. He said he and Mr. Lujan had a long discussion about our strategies or practices in terms of who uses broker dealers. He said this time last year we were primarily doing agency bullets. The dealers we're using now, weren't on the radar screen at this point last year. He said to Member Bohlin's credit, when we talked about approving dealers last year, he said, "Why not approve the world," to have the ability to do business with those who are strongest in each product area. Over the past 5 months, we've been doing business in a product area where the dealers are the strongest. We haven't been using the dealers that were getting the majority of the business this time last year when we were in a different product area.

Mr. Newman said, in looking at YTD purchases and how the business has been spread between all the approved broker dealers it "pretty much shakes out on its own. The competitive basis of going to at least three offers or bids to the strongest dealers in that product area has proven to get a pretty good spread happening, with few exceptions. Those exceptions are Morgan Stanley and Bank of America who are



strong in both areas.”

Member Cassidy asked from whom we are purchasing the new ABS federally guaranteed commercial paper.

Member Newman said it was a pool deal of the majority of the primaries and Bank of America was the book runner on that, and believes everybody got credit that were in the books on that one.

Member Schardin recalled sometime in the past fiscal year, the amount being done by direct purchase was larger, as a percentage, just under 7% now, commenting she thought it was around 15-20% before. She asked the reason for that.

Member Newman said it is because of commercial paper. He noted this is the first piece of commercial paper since July 2008. He said the direct issuance you saw in August 2008 has to do more with the New Mexico EAF funds, and in December 2008 there was some TLGP issuance in commercial paper.

Member Bohlin said in doing these large programs, such as the TLGP paper, you have a large syndicate, in many respects, although Bank of America got the bulk of that, in effect you also were working with Deutsche Bank.

Member Newman said, throughout all of these deals, it has given a lot of leeway in that we talk to the majority of the participants in the syndicate and we are putting calls into every single desk, saying what the orders are, so everyone knows what we're doing and everybody is getting their pooled credit, yet since Bank of America or Morgan Stanley are the book runners, for purposes of our report, they are the ones who are getting the credit

Member Bohlin said he wanted to make this clear for the record, that it looking a lot more concentrated than it, in fact, really is.

9. INFORMATIONAL ECONOMIC AND INVESTMENT OUTLOOK

Mr. Lujan presented information from the handout regarding yield changes, dated June 9, 2009. He said during the month, he keeps a tome of various ideas in market events and dynamics for his comments for the economic outlook. He said this time, an event happens at the end of the month, so he'll leave the balance of May to history and talk about June 9th and go from there.

Mr. Lujan said the first page of the handout is a comparison of the treasury yield curves in the middle of May which is when they sold the 2 and 3 year treasury positions at a profit, and the treasury curve after last Friday. The bars at the bottom



indicate the increase in rates on the 2 and 3 year.

Mr. Lujan said, regarding the Horizon analysis on page 2, if we had purchased bonds on May 14th and had to sell them on June 9th, the analyzed full return would have been negative 10%, negative 22%, respectively. He said this is an illustration to show how much it can hurt fixed income investors when rates do back up. He said there is a balancing act. They would like to put all the cash they have to work, and put it farther out the curve so we are earning more income on that. At the same time, they want to avoid being hurt on a market value basis when rates do back up.

Mr. Lujan said he and Member Newman have been playing with lots of different scenarios and volatility figures for yields, lots of different dynamics for what the yield curve can do, back up on the long end or back up on the front end, if the fed funds rate being at near to 25 will keep it tethered, etc., etc. He said they have, initially, figured that some type of between one and three year ladder on the treasury curve will work to generate some income, and most likely will view those as buy and hold positions to generate that income until it matures, and use our cash to provide for liquidity and keep a bit of a cash balance so that we can keep reinvesting in rates as they increase.

Mr. Lujan said treasuries account for about 10% of our benchmarks, so we'll probably get back in there at that range. He said the other dynamic in the market is that treasuries are backing up, but credit spreads are coming way in. This means that risk for a long time had been really cheap, and if you buy it now, or you have been buying it, as it becomes more expensive, then the portfolios can do well. He said we are not buying more credit risk, but we are looking at the positions we hold currently, and viewing those as a potential upside, not just a potential down side. He said he is pretty close to formalizing his notes as to the investment worthiness of holding onto the Genworth funds, and we will get substantially closer to our conclusion on the AIG bonds during May.

Mr. Lujan said, regarding the Genworth bonds, for example, the CORE outperformed its total return broadly because of its corporate exposure this month, but the Genworth bonds came back 30% during the month. This is on top of news that the holding company was likely to come to market with stock issuance and be able to recapitalize in the markets on market based perspective. He said after viewing the bond that we hold, we are very comfortable with the seniority of our holdings. He said it is called funding agreement backed notes, which are senior to senior debt holder positions because they are viewed as policy holder positions. He said if Genworth, the operating company, got in trouble, then an insurance regulator would come in, and starve the holding company, noting we hold these at the operating level, and then manage an asset sale. First in line to be made whole would be policy holders. He said policy holders, according to the laws of the funding agreement back notes, are where we stand in that policy structure.



Mr. Lujan said with the market improving, with Genworth Holding Company being able to recapitalize and with our seniority position, he is getting close to finishing his remarks on the reason this is a position we should continue to hold to maturity.

CASH MANAGEMENT AND COLLATERAL REPORTS

10. STATE AGENCY DEPOSIT BALANCES IN FINANCIAL INSTITUTIONS AND INTEREST VS. NON-INTEREST BEARING ACCOUNTS – APRIL 30, 2009

Orlando Romero, State Cash Manager, presented information from his Memorandum dated June 2, 2009, to James B. Lewis, State Treasurer, which is in the Committee packet. He said the summary of those accounts is on page 75 of the packet. He said these accounts are monitored on a monthly basis.

11. COLLATERAL REPORT ON AGENCY DEPOSITS & CDs – APRIL 30, 2009

Arsenio Garduno presented the Collateral Report on Agency Deposits & CD's, beginning on page 77 of the Committee packet, highlighting information as follows:

- There was one depository institution holding public funds for the month ending April 2009, which was out of compliance. Valley National Bank was out of compliance due a change in the levels of collateral required from their institution this deficiency was corrected once they were notified of the changing levels. All other institutions holding public funds met the minimum collateral requirements. The ratio of collateral required by each institution is a result of a quarterly risk assessment analysis.
- On May 20, 2009, President Obama signed legislation to increase the deposit insurance fund from FDIC to \$250,000 to extend to 2013.
- For the quarter ending March 31, 2009, the following institutions are not at 50% collateral levels for the state funds held in their financial institution:
 - Bank 34 remains at 100%;
 - Bank of the West remains at 100%;
 - Compass Bank/Albuquerque remains at 100%;



Bank of America remains at 100%;
First Community Bank remains at 100%;
Charter Bank remains at 100%;
Union Savings remains at 100%;
First Federal Bank remains at 100%; and
Valley National Bank changed from 50% to 100% requirement.

- During the quarter, a risk assessment on depository institutions for the third quarter was done, and it is noted that earnings are still declining in depository institutions holding public fund. An increase in non-performing loans was noted and there were decreases in loans which contributed to the decline in earnings.
- Valley National Bank in Espanola changed to 100%, and the total of banks required to pledge 100% is now 9 banks.
- The banking section in general is listed on page 80, noting this was the highest earning in four quarters, but it is 61% lower than a year ago. Insured institutions set aside \$60.9 billion in loan loss provisions in the first quarter, an increase of \$23.7 billion from the first quarter 2008. The increase in loan provisions for loan loss was due to an increase in charge offs. First quarter net chargeoffs of \$37.8 billion were almost twice as high as the \$19.6 billion from the previous year.
- With regard to problem banks, the FDIC now has 305 banks on their problem bank list, which is up 252 from the previous quarter and 90 from the same point a year ago. The assets of the problem banks rose from \$159 billion to \$220 billion. During the quarter, 50 institutions were absorbed in mergers and 21 institutions failed. This is the largest number of failed institutions in a quarter since the 4th quarter 1994.

Member Schardin advised that she and Member Padilla-Jackson met yesterday with staff from STO and are planning to work on revising the collateral rule, and hopes to present that to this Committee next month. She said at the meeting, Mr. Garduno shared an analysis of banks which have failed so far this year, and how the ratio set up in our collateral rule would have treated those banks. The bottom line is that the ratio has worked fairly well, and a lot of the banks which failed nationally would have been bumped up to 100% collateral about a year before they failed under our rule.

Chair Valdes said during that discussion, we discussed going to 102% collateral for any of the banks which currently are at 100% collateral.

OTHER



QUESTION PERIOD

Member Cassidy welcomed Mr. Beatty, and said he does a good job investing the cash of Los Alamos County.

Member Cassidy asked for an update on the cash flow analysis and the exercise you are going through.

Member Schardin said they continue to work with both Bank of America and the people who are running share reports for us to get better and better data sources. She said there was a major breakthrough this week where Bank of America can exclude all of the investment activity the State is doing which is the really big difference between the two data sources and between what we need to forecast and what we were forecasting before. She said there have been some data breakthroughs and they think they are getting really close to the model actually working. They still have published no results, or given results publicly. She said in the last month, once they included the investment activity they got very close to what STO was reporting as the change in market value and that was really heartening to be able to do what they were presenting independently. They are coming along on this, and will be meeting again this afternoon just after this meeting, and will review the status of the model. She invited members to attend if they would like to do so.

Member Cassidy said the idea of the modeling is to produce cash flows on a monthly basis going forward, which was done formerly. He said it is a helpful process to determine whether TRANs makes sense for the State, saying he presumes the TRANs is still being held in abeyance pending the outcome of this analysis.

NEXT MEETING – WEDNESDAY, JULY 15, 2009, 9:00 A.M.

ADJOURNMENT

Member Designee Schardin moved, seconded by Member Cassidy, to adjourn the meeting. The motion was approved on a voice vote [5-0], and the meeting was adjourned at 10:25 a.m.

**Respectfully Submitted by MARK VALDES
CHAIRMAN DESIGNEE AND DEPUTY STATE TREASURER**



ATTEST:

Submitted electronically
Melessia Helberg, Stenographer