

OFFICE OF THE STATE TREASURER

STATE TREASURER'S INVESTMENT COMMITTEE (STIC) MEETING MINUTES Wednesday, December 13, 2006

The State Treasurer's Investment Committee (STIC) Meeting convened at approximately 10:00 a.m. in the Bob Barth Conference Room at the Office of the State Treasurer, 2019 Galisteo Street, Santa Fe, New Mexico, on Wednesday, December 13, 2006.

I. CALL TO ORDER

Roll Call

Members Present:

Mr. Douglas Minge Brown, State Treasurer
Ms. Joelle Mevi, State Cash Manager
Ms. Olivia Padilla-Jackson, State Board of Finance Director
Mr. Steven Bohlin, Public Member
Mr. Paul Cassidy, Public Member

Staff Present:

Mr. Mark Valdes, Assistant State Treasurer
Mr. Victor Vigil, Assistant State Cash Manager
Mr. Mark Canavan, Portfolio Management Bureau Chief
Mr. Joaquin Lujan, Investment Officer
Ms. Jane Tabor, Public Information Officer
Ms. Laura Montoya, Executive Assistant
Mr. Larry Castillo

Guests:

Ms. Amy Chavez, State Board of Finance Deputy Director
Ms. Stephanie Schardin, Legislative Finance Committee
Mr. Laird Graeser, Department of Finance and Administration
Mr. William Mueller, Legislative Finance Committee

Approval of December 13, 2006, Agenda

Member Bohlin motioned for approval of the agenda; seconded by Member Mevi, the motion carried.

Approval of November 15, 2006, Minutes

Member Cassidy motioned for approval of the minutes after a correction on page 5, second line of the General Fund Benchmark discussion (from "trying not" to "not trying"); seconded by Member Mevi, the motion carried.

II. INVESTMENT REPORTS – Month Ended November 30, 2006

General Fund Monthly Report

Mr. Canavan summarized the investment activity for the General Fund portfolio. The market value, net of TRANS, was \$2.58 billion, compared to \$2.25 billion at the same point last year and \$2.17 billion at the same point two years ago. The \$2.58 billion market value of the General Fund at month-end was a decrease of 0.7% from October's

\$2.60 billion and an increase of 0.3% from September's \$2.57 billion. The yield on the General Fund was 4.93% at month-end, up from 4.91% in October. The average term of the portfolio decreased to 122.1 days, down from 139.7 days in October. As of November 30, the dollar-weighted asset mix of the General Fund was comprised of 59.4% in U.S. agency bonds, 28.8% in the overnight repurchase pool, 8.5% in certificates of deposit, and 3.3% in money market mutual funds. There was no investment activity during November. The General Fund earnings for November were \$11.4 million, a decrease of 2.1% from October's earnings of \$11.65 million and an increase of 67.1% over November 2005 earnings of \$6.82 million. Fiscal year-to-date earnings totaled \$59.2 million compared to \$32 million through the same period last fiscal year.

In a discussion of the laddering of the General Fund Core, Mr. Canavan described the model portfolio which would require overweighting of maturities in the 4 to 5 year area in order to achieved the 2 year duration of the benchmark. Member Bohlin stated that it is important to be benchmark aware and not benchmark driven to allow for taking advantage of investment opportunities and to not be confined to maintaining a 2-year duration. Member Cassidy expressed his support of a laddering strategy in order to invest and have maturities in every kind of market while paying attention to cash flow needs. Mr. Canavan asked for clarification of his performance expectations against the benchmark. Member Bohlin and Chairman Brown both assured Mr. Canavan that the collective judgement of the Committee and the Board of Finance is that the portfolio laddering will take time, especially in the inverted yield curve environment and that Mr. Canavan does not need to assume any burden related to meeting the index or beating the benchmark.

Local Government Investment Pool (LGIP) Monthly Report

Member Mevi informed the committee of the LGIP status. The market value was \$712.24 million (a 3.3% increase over October), compared to a market value of \$868 million at the same period in the prior fiscal year and \$1.26 billion at the same period two years ago. Pool members are encouraged by the yield increase and are therefore adding more funds to the Pool. The gross yield of the LGIP portfolio increased 2 basis points to 5.30% at November 30. The weighted average maturity was 34 days, up from the October weighted average maturity of 21 days, but still within the allowable limit of 50 days. The portfolio was comprised of 44.7% in U.S. government agency securities, 33.5% in A-1+ commercial paper, 20.9% in AAA money market funds, and 0.93% in the bank account balance. The remaining two certificates of deposit matured removing that asset class from the portfolio. November investment activity in the LGIP portfolio included the purchase of \$240 million in A-1+ commercial paper with an average yield of 5.36% and average term of 57.5 days. In addition, \$189 million in agency discount notes was purchased with an average yield of 5.25% and average term of 59 days. Total LGIP earnings for November were \$3.03 million, a slight decrease from October earnings of \$3.06 million, probably due to there being one less day's worth of earnings in November. Fiscal year-to-date earnings for the LGIP totaled \$14.9 million compared to \$12.9 million through the same period last fiscal year. The 30-day net yield of the LGIP as of was 5.24%, outperforming the 30-day net S&P Rated Government Investment Pool (GIP) index (5.10%) by 14 basis points. However, the 30-day gross yield of the *New MexiGROW* LGIP, 5.30%, trailed the 30-day gross S&P Rated GIP

index of 5.33% by 3 basis points. The administrative fee assessed to participants for November was 5.5 basis points. Participant contributions totaled \$51 million and withdrawals totaled \$31 million.

Bond Proceeds Investment Pool (BPIP) Monthly Report

Mr. Lujan reported that the Tax-Exempt BPIP had a market value of \$474.9 million, down from the previous month's balance due to project draws of approximately \$12 million. The yield and term were 4.66% (4 basis points above the highest arbitrage yield of any bond issue in the fund) and 132.2 days, respectively. The Tax-Exempt BPIP was comprised of 57.6% in U.S. Treasuries, 24.9% in legacy flex repurchase agreements, 9.8% in the overnight repurchase pool, and 7.7% in U.S. Agencies. \$165 million was invested in U.S. Treasuries in November with maturities laddered in \$15 million increments through November 2007 with yields ranging from 4.96% to 5.15%. Earnings were \$1.6 million.

The Taxable BPIP had a market value of \$647 million, down 6.4% due to a large draw of nearly \$43 million by the Public Education Department. The yield was 4.77% and the term was 162.8 days. It was comprised of 45% in the overnight repurchase pool, 20% in legacy flex repurchase agreements, 25.85% in U.S. Agencies, and 8% in commercial paper. \$170 million was invested in U.S. Agencies laddered in \$10 million increments through September 2008 with yields ranging from 4.91% to 5.21%. Earnings totaled \$2.6 million.

Member Cassidy asked Mr. Lujan whether he received cash flow projection information from state agencies in order to more accurately develop his investment philosophy. Mr. Lujan informed the Committee that historical analysis seems to dictate having \$50 million to \$70 million in cash in the Pool at all times so that money is available for projects. He will also work closely with Member Padilla-Jackson to communicate the program's philosophy to those agencies that draw from the Pool so they will understand how it works and the need for as much advance drawdown notice as possible.

Economic and Investment Outlook

Mr. Canavan reported that November's economic releases reflected continued slower growth but also a trend toward stabilization in the decline. The investment plan is to extend durations on both the General Fund and Bond Proceeds portfolios. To the extent possible within the 50-day weighted average maturity in the LGIP portfolio, the duration will be extended where advantageous in the 30-day to 6-month range concentrating on high quality commercial paper to the permissible limit and, as necessary, utilizing U.S. Agency securities for the remainder. Member Bohlin reiterated the "benchmark aware, not benchmark driven" philosophy and concurred with Mr. Canavan's synopsis.

III. CASH MANAGEMENT REPORT – Month Ended October 31, 2006

State Agency Deposit Balances in Financial Institutions

Mr. Victor Vigil stated that there were no financial institutions exceeding the statutory limitations on equity capital and deposit ratios. There were 512 accounts with a balance of \$89.4 million; 5 accounts were closed and 4 were opened.

Collateral Report

According to new compliance requirements as he understood them, Mr. Vigil reported that First National Bank in Ruidoso and International Bank in Raton were under-collateralized at October 31, but have since complied. However, Member Padilla-Jackson informed the Committee that the proposed changes in collateral requirements are still out for public comment and are not in effect; therefore, those banks were actually in compliance. Mr. Vigil said he would reevaluate the findings. Chairman Brown stated that the STO wants to institute a requirement that, when a bank puts its money with the Office, it is obligated to inform the Office of any adverse material change to its economic condition.

Interest Bearing vs. Non-Interest Bearing Accounts

Mr. Vigil stated that there was \$64.2 million in interest bearing accounts and \$26.8 million in non-interest bearing accounts.

IV. STAFF REPORTS

Bond Proceeds Investment Pool Benchmark

Mr. Lujan informed the Committee that the benchmark chosen for the Tax-exempt Pool was the highest Arbitrage Yield Limit for any issue presiding in the Pool with proceeds outstanding. For the Taxable Pool, Constant Maturity U.S. Government 2-year Agency (12-month moving average) and a custom Index comprising 10% of the Merrill Lynch 0-3 year Treasury Total Return Index and 90% of the Merrill Lynch 1-3 year Federal Agency Total Return Index will be used as benchmarks. Each benchmark will be reported against the respective portfolio performance on a quarterly basis. The Committee voiced its approval of these benchmarks which must also be approved by the Board of Finance at its meeting next week.

Expanded Broker/Dealer List

Mr. Canavan informed the Committee that due diligence was completed on the additional proposed companies and registered representatives, with all found in compliance. The members unanimously approved the list which must also be reviewed and approved by the Board of Finance at its next meeting.

Fiscal Year 2006 Audit

Chairman Brown informed the Committee that the preliminary audit was received from the auditors but will not be official until released by the State Auditor's Office. The number of findings came down from last fiscal year's 16 to probably 5 findings – with no findings in the investment area, but several in the transactional area due to fiscal agent changes and unreconciled items. Mr. Vigil reported to the Committee that the reconciliation process was made more difficult by the change in fiscal agent and by SHARE; however, STO has implemented functionalities and controls in SHARE to help deal with the reconciliation and journal entry processes. Mr. Valdes stated that Mr. Vigil will assign a staff member to work fulltime on reconciliation until it is current.

TRANS

Ms. Mevi informed the Committee of a successful TRANS sale with 71 bids from 13 different bidders and 16 different firms purchasing a portion of the notes - \$300 million in total at a cost of 3.507%. The sale will close on December 20.

V. NEXT MEETING

Wednesday, January 10, 2006, 10:00 a.m.

VI. ADJOURNMENT

The meeting adjourned at 11:45 a.m.