

OFFICE OF THE STATE TREASURER

STATE TREASURER'S INVESTMENT COMMITTEE (STIC) MEETING MINUTES
Wednesday, April 9, 2008

The State Treasurer's Investment Committee (STIC) meeting convened at approximately 9:00 a.m. in the Bob Barth Conference Room at the Office of The State Treasurer, 2019 Galisteo St., Bldg. K, Santa Fe, New Mexico, on Wednesday, April 9, 2008.

I. CALL TO ORDER

Roll Call

Members Present:

Ms. Joelle Mevi, Chairperson Designee, Chief Investment Officer
Ms. Olivia Padilla-Jackson, State Board of Finance Director
Mr. Paul Cassidy, Public Member

Members Absent:

Mr. James B. Lewis, State Treasurer
Mr. Steven Bohlin, Public Member

Staff Present:

Ms. Randilynn Lord, Legal Counsel
Mr. Clarence L. Smith, Chief Operations Officer
Ms. Kirene Bargas, LGIP Portfolio Manager
Mr. Joaquin Lujan, GF, BPIP Portfolio Manager
Mr. Victor Vigil, State Cash Manager (acting)
Mr. Arsenio Garduño, Collateral Manager
Ms. Eliza Anaya, LGIP Account Technician

Guests:

Ms. Stephanie Schardin, Board of Finance
Mr. Gillis Lang, Department of Finance and Administration
Mr. Norton Francis, Legislative Finance Committee

Approval of April 9, 2008 Agenda

Member Olivia Padilla-Jackson motioned for approval of the agenda; seconded by Member Paul Cassidy. The motion carried.

Approval of March 12, 2008 Minutes

Member Olivia Padilla-Jackson motioned for approval of the minutes; seconded by Member Paul Cassidy. The motion carried.

II. INVESTMENT REPORTS- Month and Quarter Ended March 31, 2008

General Fund Report

Mr. Joaquin Lujan presented a summarization of the market value, change in balance, investment activity, and interest earnings for the General Fund Investment Portfolio for the month and quarter ending March 31, 2008.

Member Olivia Padilla-Jackson inquired on the declining balance being reflected on the General Fund LIQUIDITY segment; how it was being monitored. Mr. Lujan reviewed some of the steps STO utilizes to monitor the LIQUIDITY segment including cash flow projections, communications with the Investment Accounting Bureau, research on receipts and expenditures, and restricted use of the CD Program. Mr. Lujan reported that STO has requested three years of the Master Depository account records from archives in order to analyze. During a meeting with LFC, Director David Abbey informed STO that they use a query designed by DFA that can extract certain data which could also be helpful in identifying trends for STO; it would require query authority from DFA. Mr. Lujan reported that, since the General Fund portfolio has been separated into the CORE and LIQUIDITY, the volatility is being experienced in the LIQUIDITY segment. This is due, in part, because some STB transfers or gas revenues flow through this portfolio briefly prior to being shifted to the appropriate BPIP.

Chairperson Mevi commented that the General Fund balance has increased in this last month over month period, but is still lower than the same period from prior years since 2005. Member Padilla-Jackson suggested that it may have to do with differing budget levels and questioned the LFC representative whether this might be the case. Mr. Norton Francis, LFC analyst, stated that the general fund expenditure appropriation for FY 08 was about 10.3% higher than FY 07, while only a 3% increase was budgeted for FY 08 revenues; this may account for why the General Fund portfolio balances are declining in FY 08. Mr. Francis will email the FY08 General Fund budget to STO.

Mr. Lujan reported that the General Fund CORE investments during the quarter were 'laddered out' to five years and LIQUIDITY portfolio investments were allowed to mature into cash. For the CORE portfolio, extending duration by purchasing longer dated high quality assets took precedence and directed much of the trading activity during the first quarter.

New MexiGROW Local Government Investment Pool (LGIP) Report

Ms. Kirene Bargas presented a summarization of the market value, change in balance, investment activity, and interest earnings for the LGIP portfolio the month and quarter ending March 31, 2008.

Member Paul Cassidy commented that it is nice to see the LGIP growing.

Bond Proceed Investment Pools (BPIP)

Mr. Joaquin Lujan presented a summarization of the market value, change in

balance, investment activity, and interest earnings for the Tax-Exempt and the Taxable Bond Proceed Investment Pools for the month and quarter ending March 31, 2008.

Summary of Broker Participation

Chairperson Mevi presented a summarization of the broker participation for purchases by asset type, market, and by broker in total for all portfolios through March 2008.

Economic and Investment Outlook

Mr. Joaquin Lujan reported that in March the Fed created more surgical tools through which they intend to stabilize financial markets, avoiding the need to use the blunt policy tool of changes to the Fed Funds target rate...and taking it down to 1%.

We are at an important inflection point—not a turning point: the securitized product and credit markets will continue to produce significant losses for investors but no longer at an accelerating rate. Though not out of the woods by any means, we are now less worried about systemic market risk and more focused on business cycle risk, the issues and language of which are more familiar to most people: unemployment, negative GDP growth, and for bond investors corporate defaults.

Unfortunately recession talk is not whether, but how deep and how long? Already since the end of March the cost of protection against a corporate default has risen to levels that imply we will see a 10-15% default rate of investment-grade issuers sometime in the near future. While this implied default rate is probably a bit high and influenced plenty fear, it's clearly a signal that waters ahead remain rough. Our job here at STO, protecting principal and liquidity, while eking out some return, will not be getting any easier.

III. CASH MANAGEMENT & COLLATERAL REPORTS: February 29, 2008

Cash Management Report

Acting Cash Manager Victor Vigil reported pursuant to section 8-6-3.1 NMSA 1978; the State Cash Manager shall submit to the State Board of Finance a report showing state fund balances in each financial institution established pursuant to this section. He presented a summary of state agency accounts in each institution though the month ended February, 2008.

Mr. Vigil reported that the Judicial District Courts may soon begin utilizing the LGIP instead of bank accounts for the purpose of maintaining litigant funds.

Member Paul Cassidy asked if non-interest bearing accounts are still being monitored. Mr. Vigil replied yes, and that he would create a spreadsheet or a graph showing all the accounts. Member Olivia Padilla-Jackson asked if he could also get a list of accounts that do not have legal justification for independent accounts.

Collateral Report

Mr. Arsenio Garduño reported that all depository institutions holding public funds for the month ending February 2008 met the minimum collateral requirements. The ratio of collateral required by each institution is a result of a quarterly risk assessment analysis.

Member Paul Cassidy asked if the collateral policy has been reviewed and/or modified since the last STIC meeting discussions regarding potential weakness in the banking sector. Member Olivia Padilla-Jackson replied that no changes have yet been made to the collateral policy. She recommended a special meeting to discuss additional information requirements that STO may want to incorporate to the NMAC rule to better assess bank strength. Chairperson Mevi agreed and will schedule a meeting. Mr. Lujan added that he was researching appropriate ratios and FDIC-available information that could be helpful for this analysis and will have some recommendations ready for the special meeting.

IV. STAFF REPORTS

None

V. COMMITTEE REPORTS

None

Update on NMFA Auction Rate Securities

Legal Counsel Randilynn Lord provided an update to the New Mexico Finance Authority auction rate securities transaction issue which was presented to STIC in March. Of the \$470 million total NMFA ARS, \$135.2 million remain outstanding consisting of \$84.8 million 2004C bonds covered by Ambac insurance and \$50.4 million taxable 2006C bonds covered by an XL insurance policy.

Ms. Lord reported that, at this time, no firm bank commitment has been received by NMFA for the remaining \$135.2 million necessary to refund. At the March STIC discussion it was reported that two major concerns needed to be resolved prior to a decision for STO to bid on the NMFA securities. The first concern to be addressed was that, for tax purposes, the purchase by an issuer of its own securities “extinguishes” the debt so that it cannot be refunded thereafter. This issue was resolved favorably when the IRS issued a revised ruling permitting such purchases under certain conditions. A second concern was whether the participation of an issuer in the purchase of its own ARS ran afoul of the market manipulation restrictions of federal securities laws. The SEC released a “no action” letter on March 14, 2008 spelling out necessary procedures in order for issuers to avoid this problem. The procedures involve advance public disclosure (two business days) of the issuer’s intentions concerning bidding in an auction, the amount and interest rate to be bid for the securities, substantial disclosures concerning the immediately preceding auction, and disclosure of steps taken to ensure that the auction would not result in a below market interest rate compared to appropriate benchmarks. The SEC also advised issuers to determine whether original offering disclosure documents for the securities indicated that the issuer could not bid on its own securities. We have found no such statements in the NMFA offering disclosures. The SEC also advised the issuer to research any contractual provisions that

could prohibit the issuer from purchasing their securities. A third concern that has recently surfaced relates to whether the purchase by the issuer creates a voidable preference under the bankruptcy laws. Ms. Lord is working with NMFA legal counsel to definitively resolve this issue.

Member Olivia Padilla-Jackson motioned to take no action regarding a recommendation for STO to either purchase or not purchase the NMFA auction rate securities. The motion was seconded by Member Paul Cassidy and the motion carried.

VI. NEXT MEETING

Wednesday May 14, 2008 at 9:00 a.m.

VII. ADJOURNMENT

Member Paul Cassidy motioned to adjourn the meeting, seconded by Member Olivia Padilla-Jackson. The meeting adjourned at 10:28 a.m.