

# EXECUTIVE SUMMARY

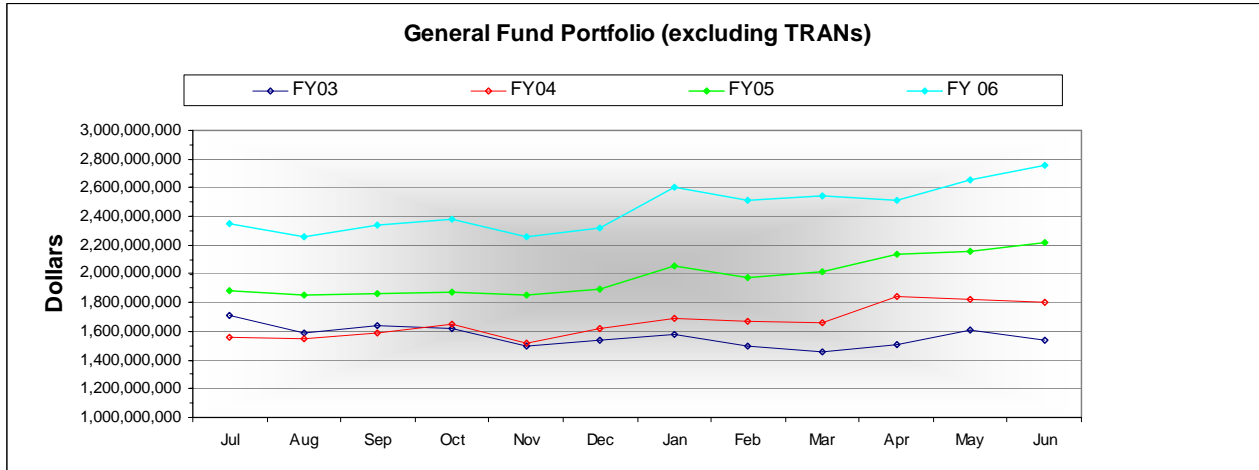
Information presented reflects the investment balances as of June 30, 2006.

## GENERAL FUND INVESTMENT PORTFOLIO SUMMARY

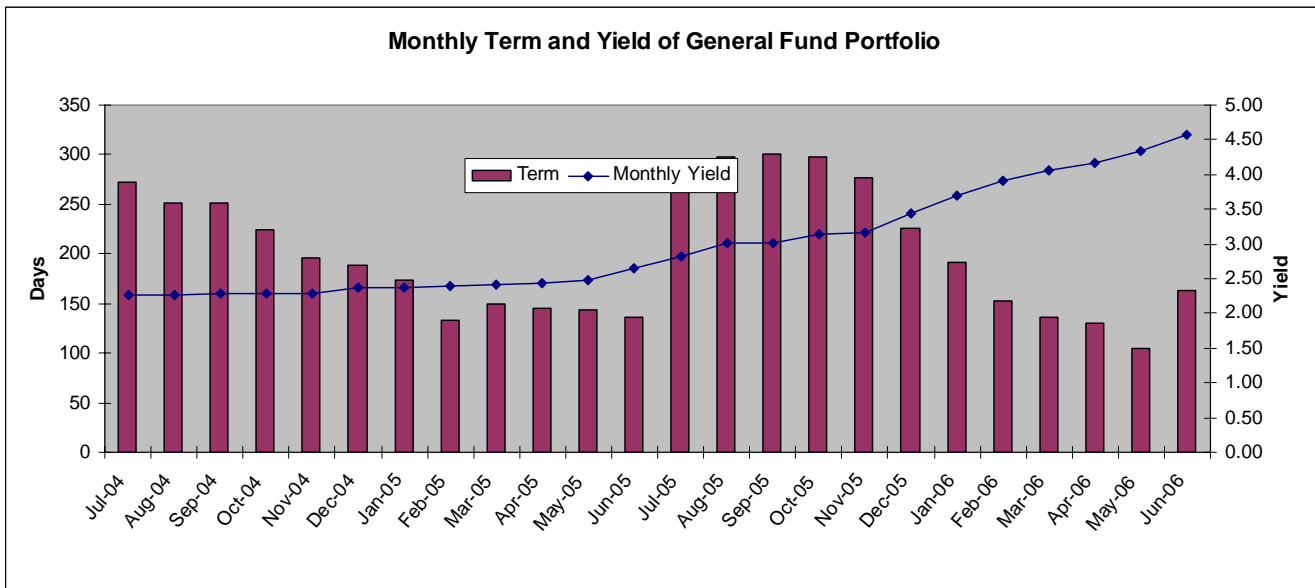
- The market value of the General Fund Investment Portfolio on June 30, 2006, was \$2.76 billion, compared to \$2.65 billion in the previous month (Graph 1).
- The yield of the General Fund Portfolio was 4.58 percent, up from 4.33 percent in May. The average term of the portfolio increased to 163 days, up from 105 days in May (Graph 2) as longer term securities were purchased at the end of June.
- The June 30, 2006, asset allocation of the General Fund was comprised of 63.8 percent in U.S. agencies, 1.8 percent in flex repurchase agreements, 25.4 percent in the overnight repurchase pool, 8.8 percent in Certificates of Deposit, and 0.2 percent in corporate bonds (Table 1).
- In June, investment activity included the purchase of \$616.2 million in commercial paper with an average yield of 5.12 percent and a term of less than 30 days, \$741.3 million in U.S. agency obligations with an average yield of 5.12 percent and terms ranging from 60 to 360 days, and \$35.5 million in Certificates of Deposit with an average yield of 5.15 percent and a term not exceeding 180 days. In addition, the General Fund purchased \$123.5 million in one-day Severance Tax Notes at a rate of 4.88 percent and a three-day \$37 million note from the City of Albuquerque also at a rate of 4.88 percent.
- The total General Fund earnings for June, as shown in Chart A, were \$11.34 million, an increase of 4.3 percent over May earnings of \$10.87 million. The fiscal year-to-date earnings totaled \$97.3 million compared to \$56.2 million at the same point last fiscal year.

# STATE TREASURER - GENERAL FUND PORTFOLIO JUNE 30, 2006

**GRAPH 1**



**GRAPH 2**

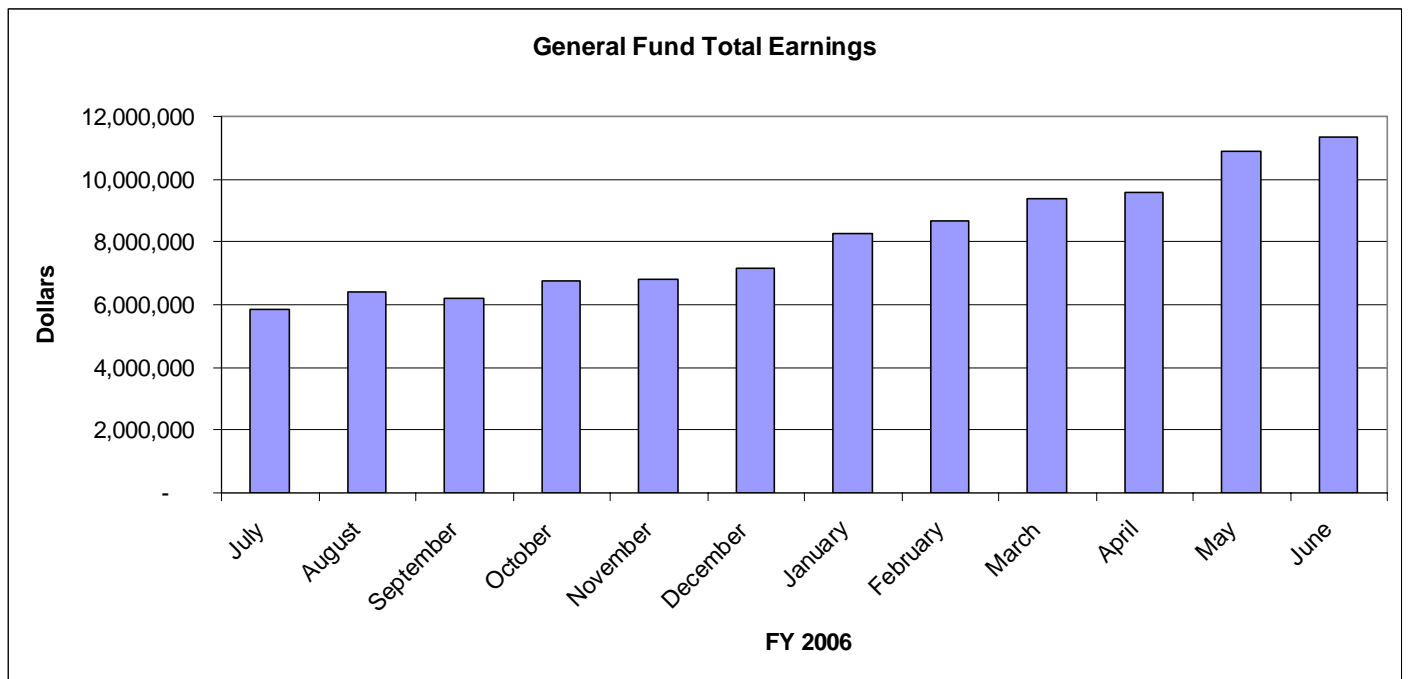


## General Fund Portfolio

TABLE 1

Asset Type	Yield	Market Value	% of Portfolio	Term (days)
Agencies	4.32%	\$ 1,761,354,682	63.8%	237
Flex Repurchase Agreements	2.46%	\$ 50,000,000	1.8%	38
Overnight Repurchase Pool	5.06%	\$ 700,254,591	25.4%	1
Commercial Paper		\$ -	0.0%	
Certificates of Deposit	4.59%	\$ 243,850,000	8.8%	146
Corporate Bonds	4.44%	\$ 4,992,600	0.2%	77
<b>Total:</b>	<b>4.58%</b>	<b>\$ 2,760,451,873</b>	<b>100.0%</b>	<b>163</b>

CHART A

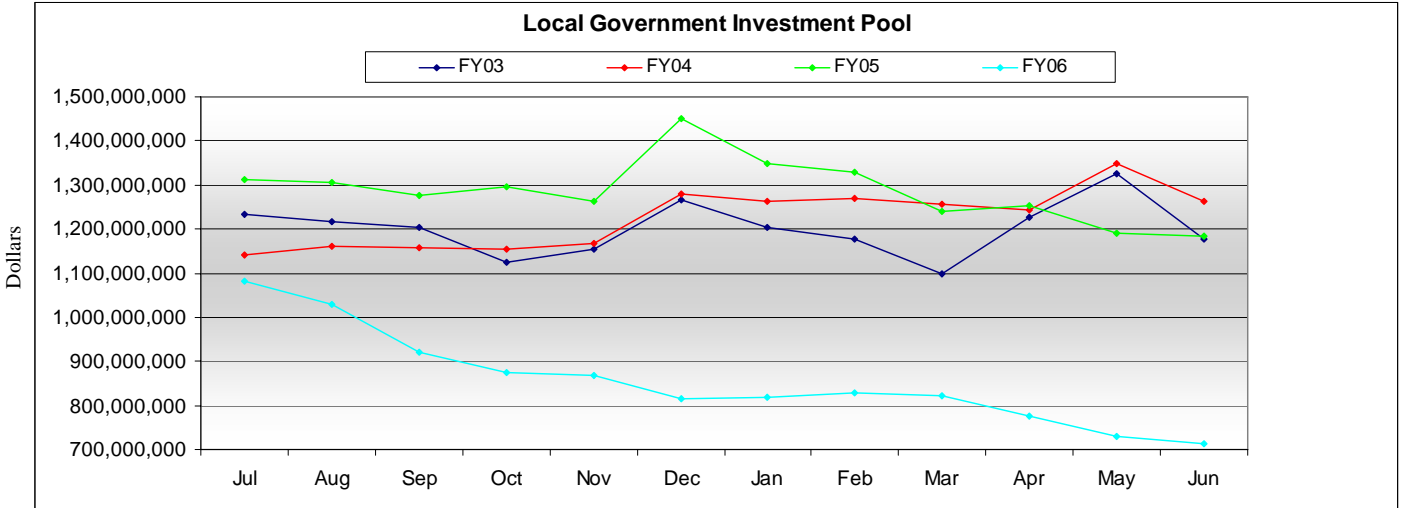


## LOCAL GOVERNMENT INVESTMENT POOL (LGIP) SUMMARY

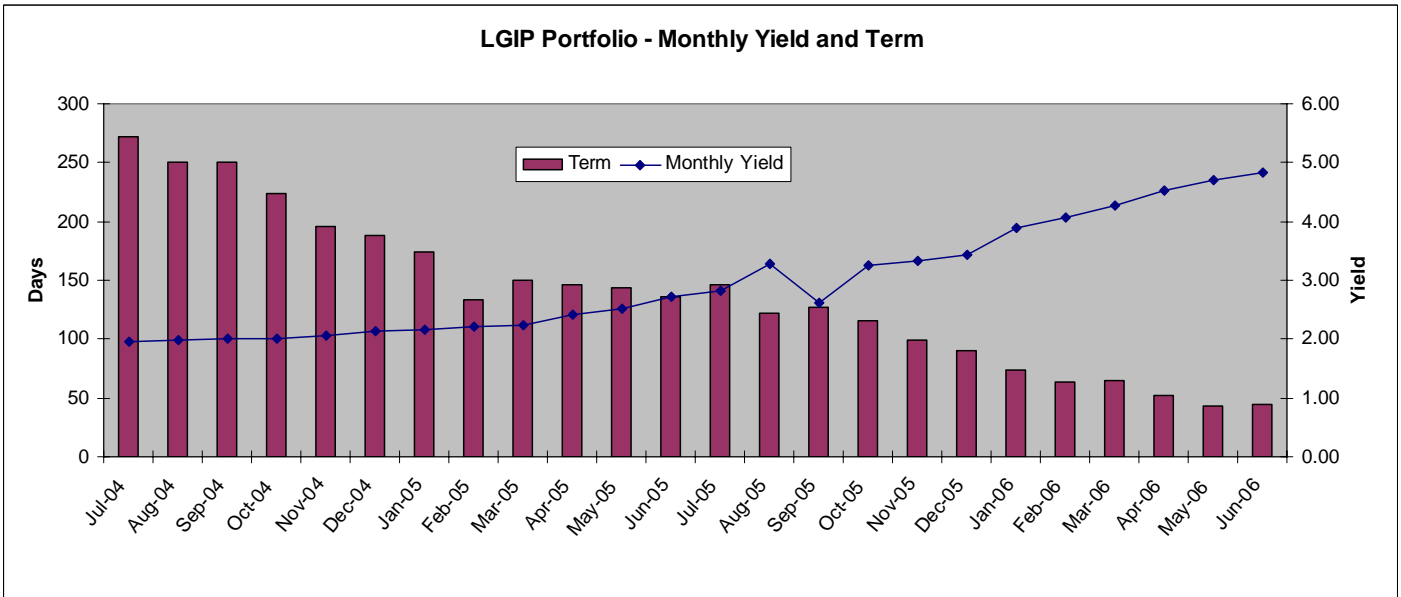
- The market value of the LGIP as of June 30, 2006, was \$712.0 million, compared to a market value of \$728.3 million in the previous month (Graph 4). The small drop in the fund level can be attributed to fiscal year-end adjustments by local governments.
- The blended yield of the LGIP portfolio at month-end was 4.84 percent, up from 4.71 percent in May. The average term of the portfolio was 44 days, comparable to May (Graph 5).
- The asset allocation of the fund was comprised of 7.0 percent in flex repurchase agreements, 64.2 percent in agencies, 26.9 percent in commercial paper, 0.2 percent in overnight repurchase agreements, and 1.6 percent in Certificates of Deposit (Table 2).
- In June, the investment activity included the purchase of \$132.5 million in commercial paper with an average yield of 5.42 percent and a term of 60 days. In addition, \$162.9 million in U.S. agency obligations were purchased with an average yield of 5.23 percent and an average term of less than 90 days.
- Total LGIP earnings for June, as shown in Chart B, were \$2.8 million, a 4.0 percent decrease from May earnings of \$2.93 million. The decline in earnings was attributed to the lower balance amount to invest. Fiscal year-to-date earnings for the LGIP totaled \$31.9 million compared to \$27.6 million at the same time last fiscal year.

# STATE TREASURER - LOCAL GOVERNMENT INVESTMENT POOL JUNE 30, 2006

**GRAPH 4**



**GRAPH 5**

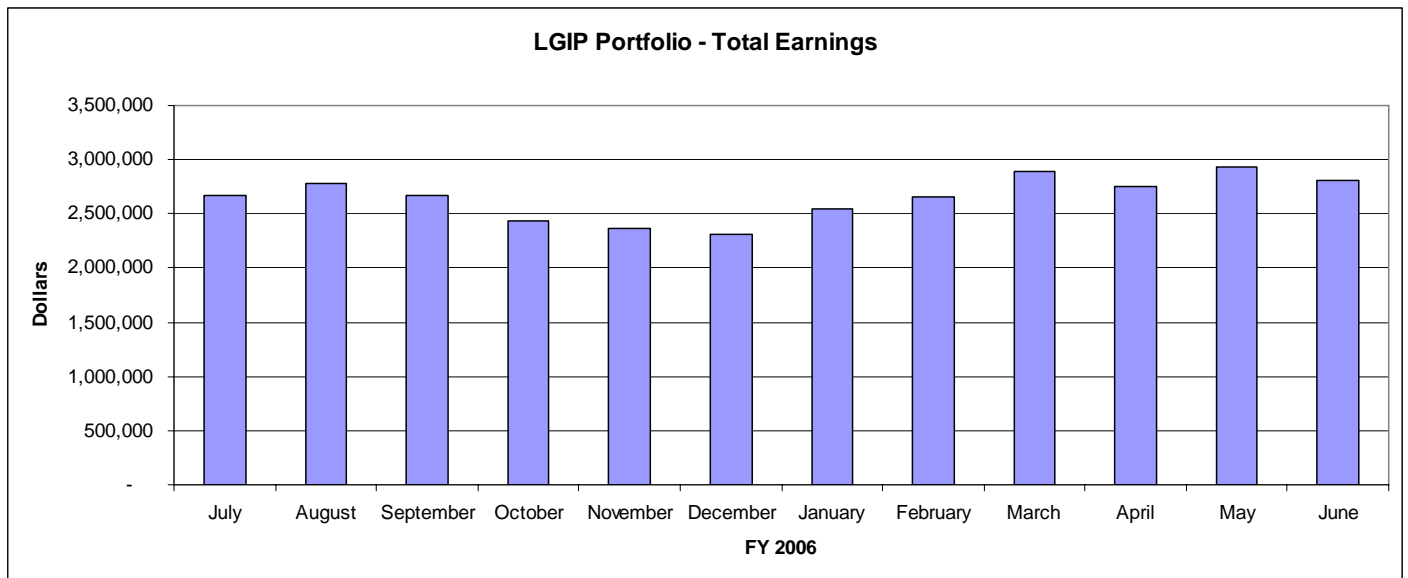


**Local Government Investment Pool Portfolio**

**TABLE 2**

<i>Asset Type</i>	<i>Yield</i>	<i>Market Value</i>	<i>% of Portfolio</i>	<i>Term (days)</i>
Flex Repurchase Agreements	2.46%	\$ 50,000,000	7.0%	38
Agencies	4.60%	\$ 457,366,756	64.2%	35
Commercial Paper	5.33%	\$ 191,653,910	26.9%	32
Overnight Repurchase Pool	5.06%	\$ 1,471,029	0.2%	1
Certificates of Deposit	4.39%	\$ 11,500,000	1.6%	146
<b>Total:</b>	<b>4.84%</b>	<b>\$ 711,991,695</b>	<b>100.0%</b>	<b>44</b>

**CHART B**



## **QUARTERLY REPORT** **QUARTER ENDED JUNE 30, 2006**

### **Investment Strategy for the Past Quarter and the Next Quarter**

The investment strategy over the past quarter was to shorten the term of the maturities on investments to take advantage of rising interest rates, until the last part of June as longer term investments were considered. As a result, the yield on the General Fund Portfolio increased from 4.1 percent from the first quarter ended March 31, 2006, to 4.6 percent at the end of the second quarter ended June 30, 2006. Likewise, the yield for the LGIP Portfolio jumped from 4.3 percent at the end of the first quarter 2006 to 4.8 percent on June 30, 2006.

The investment strategy for the next quarter is to start increasing the term of the portfolio in an effort to lock in higher yields as the Federal Reserve interest rate hikes start to slow.

### **Asset Allocation Goals**

The investment strategy over the past quarter was to focus on higher yielding allowable asset types such as commercial paper and agency notes. The maturities on these investments were matched to the Federal Reserve meetings to take advantage of interest rate hikes. As these investments have matured, the cash was invested in the overnight repurchase pool to await re-investment. As a result, allocation percentages of the portfolios varied between these three allocation classes.

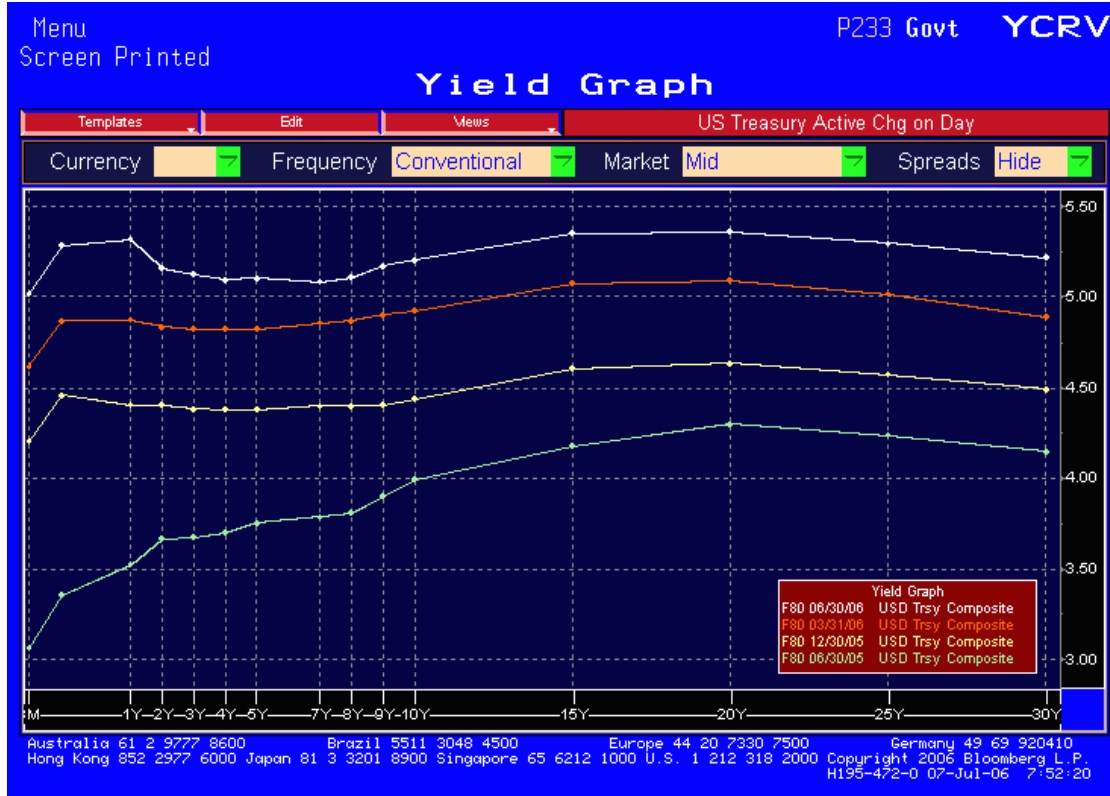
Going forward, the asset allocation percentages will continue to lean towards U.S. agency obligations and commercial paper. In consultations with the STO Investment Advisor, corporate bonds will be considered as an investment choice within the constraints of the investment policy.

### **Average Maturity Targets**

The general trend regarding investment maturities over the last quarter was to shorten the term of the portfolio to take advantage of interest rate hikes by the Federal Reserve and the flatness of the yield curve. Going forward, the investment strategy will be to start considering longer terms on securities to lock in higher yields as the interest rate hikes begin to slow and the yield curve normalizes.

## INVESTMENT OUTLOOK

- The Federal Reserve raised interest rates by a quarter of a point to 5.25 percent at its June meeting. Economic growth continues to provide fuel to the underlying inflation pressures of the economy. While growth has moderated to a more sustainable pace and inflation has not shown unreasonable acceleration, the data nevertheless give the Federal Reserve room to raise rates further. Economists from several leading financial service firms have adjusted their 12-month economic estimates to include a 6% Fed Fund rate.
- Recent economic releases are consistent with overall economic growth over 3%. Reports from the Institute of Supply Management, the Department of Labor, and others consistently show underlying strength and momentum in the economy.
- On a risk/reward basis it is clear the largest percentage increase in short term rates has already occurred. As such, the STO has begun to deploy assets into the 6- to 12-month portion of the yield curve. The STO will continue extending the duration of the General Fund Portfolio by placing investments in the 6- to 18-month time horizon as opportunities to do so arise. The STO continues to monitor market dynamics and will place investments into the 18- to 36-month time frames as those time horizons become more advantageous.



## MOVING FORWARD

**TRANS** – A \$400 million Tax and Revenue Anticipation Note was sold on June 27, 2006, through an electronic competitive bidding process. The Note was sold at a true interest cost of 3.74 percent. Twelve underwriting firms participated in the sale and 52 bids were received. Seven different underwriting firms participated in the purchase of the Note. The notes were issued on July 6, 2006.

**New Trading Platform** - The STO has incorporated a new electronic investment trading platform, Trade Web, for purchasing investments. Trade Web is a national recognized trading platform used by most government agencies and private investing firms. Trade Web will offer further diversification and competitiveness in the selection and purchasing of investments.

**LGIP** – An eligible list of AAA-rated money market funds is being completed. It is anticipated that five or six money market funds will be approved and in place for investments by the end of July.

**FY05 STO AUDIT** – The final draft of the audit report was electronically submitted to the State Auditor by Accounting and Consulting Group on June 22, 2006. The State Auditor has notified the IPA of a few changes and additions that must be made. Once those changes are made and the document is returned to the State Auditor, the final document will be approved and the document printed. It is the STO's expectation that the audit will be available to the public in July 2006.

**FY06 STO AUDIT** – Five proposals were received from the request for proposals to perform the annual audit for FY06 and quarterly audit services beginning the first quarter of FY07. An internal STO committee reviewed and evaluated proposals. The committee recommended, and the State Treasurer accepted the recommendation of the Albuquerque firm, Meyners + Company for annual and quarterly audit services. The State Treasurer met with the State Board of Finance (SBOF) *Subcommittee on Reviewing the STO Audit Process* to discuss the RFP process, evaluation criteria, and auditor recommendation. The recommendation was then reported to the SBOF at its June 22, 2006, meeting. Subsequently, STO presented this recommendation to the State Auditor, who approved Meyners + Company to perform the audit work. The contract was drafted and sent out for signatures.

**SHARE Project Update** – As planned, the new enterprise system developed by Peoplesoft went live on July 1, 2006. The system provides a comprehensive financial and human resources accounting and reporting system for all State government agencies. The new system drastically changes the workflow processes for purchasing, payroll, human resources, deposits, warrant processing, accounting, and reconciliations. Once the system is up and running and all the technical glitches are resolved, it will greatly streamline and improve the accounting and reporting for the State.

# Broker Participation – All Funds

TABLE 3

Volume  
(\$ in thousands)

<u>Broker/Dealer</u>	<u>Month</u>												<u>Total</u>	<u>Percent</u>	
	<u>Dec-05</u>	<u>Jan-06</u>	<u>Feb-06</u>	<u>Mar-06</u>	<u>Apr-06</u>	<u>May-06</u>	<u>Jun-06</u>	<u>Jul-06</u>	<u>Aug-06</u>	<u>Sep-06</u>	<u>Oct-06</u>	<u>Nov-06</u>			<u>Dec-06</u>
Bank of America	127,029	106,592	128,246	197,427	190,000	45,913	117,824							\$ 913,031	10.6%
Citigroup	177,234	240,703	154,220	239,518	149,245	241,722	322,937							\$ 1,525,579	17.6%
Merrill Lynch	216,195	211,927	237,181	421,915	209,489	353,299	90,349							\$ 1,740,355	20.1%
Morgan Stanley	10,000	49,776	257,824	182,876	124,670	160,831	330,601							\$ 1,116,578	12.9%
UBS	113,000	-	-	-	-	-	55,657							\$ 168,657	2.0%
Lehman	-	-	-	29,944	153,522	170,562	34,240							\$ 388,268	4.5%
Bear Stearns	-	-	-	59,872	30,000	-								\$ 89,872	1.0%
Goldman Sachs	-	-	62,196	330,996	194,938	196,532	220,120							\$1,004,782	11.6%
CS First Boston					110,603	144,093	361,888							\$ 616,584	7.1%
Direct Purchase	-	-	-	<u>538,861</u>	<u>184,822</u>	<u>269,671</u>	<u>89,736</u>							<u>\$ 1,083,090</u>	<u>12.5%</u>
Total	\$ 643,458	\$ 608,998	\$ 839,665	\$ 2,001,409	\$ 1,347,289	\$ 1,582,623	\$ 1,623,352							\$ 8,646,794	100.0%