

OFFICE OF THE STATE TREASURER

STATE TREASURER'S INVESTMENT COMMITTEE (STIC) MEETING MINUTES Wednesday, February 14, 2007

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 Street, Santa Fe, New Mexico, on Wednesday, February 14, 2007.

I. CALL TO ORDER

Roll Call

Members Present:

Ms. Joelle Mevi, Chief Investment Officer (Chairperson Designee)
Ms. Amy Chavez, State Board of Finance Deputy Director (Designee)
Mr. Steven Bohlin, Public Member
Mr. Paul Cassidy, Public Member (teleconference)

Member(s) Absent:

Mr. James B. Lewis, State Treasurer

Staff Present:

Mr. Mark Canavan, Senior Investment Officer
Mr. Joaquin Lujan, Investment Officer
Mr. Orlando Romero, State Cash Manager
Mr. Arsenio Garduño, Collateral Financial Analyst
Ms. Jane Tabor, Public Information Officer
Ms. Randilynn Lord, Legal Counsel

Guests:

Ms. Barbara Fava, PFM Asset Management (teleconference)
Ms. Stephanie Schardin, Legislative Finance Committee
Mr. Laird Graeser, Department of Finance and Administration
Mr. Gillis Lang, Department of Finance and Administration

Approval of February 14, 2007, Agenda

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

Approval of January 10, 2006, Minutes

Member Bohlin motioned for approval of the minutes; seconded by Member Cassidy, the motion carried.

II. INVESTMENT REPORTS – Month Ended January 31, 2007

General Fund Report

Mr. Canavan summarized the investment activity for the General Fund portfolio. The market value, net of TRANs, was \$2.77 billion, compared to \$2.61 billion at the same

point last year and \$2.07 billion at the same point two years ago, and was an increase of 8.2% from December's \$2.56 billion and an increase of 7.3% from November's \$2.58 billion. The yield was 4.98% at month-end, up from 4.96% in December. The average term of the portfolio decreased to 133.9 days from 156.8 days in December. At month-end, the dollar-weighted asset mix was comprised of 49.9% in U.S. agency bonds, 31.8% in the overnight repurchase pool, 6.9% in certificates of deposit, 6.9% in commercial paper, and 1.7% in money market mutual funds. Investment activity in January totaled \$257 million: \$17.5 million of certificates of deposit were purchased or renewed for the CD portfolio; \$200 million of commercial paper was purchased to cash match disbursements in the Liquidity Portfolio; \$40 million of U.S. Agency securities with maturities in September and October 2008 were added to the Core Portfolio. Earnings for January were \$13.15 million, an increase of 7.7% over December's earnings of \$12.21 million and an increase of 58.6% over January 2006 earnings of \$8.29 million. Fiscal year-to-date earnings totaled \$85.58 million compared to \$47.48 million through the same period last fiscal year.

Mr. Canavan explained to the Committee that the QED accounting system accounted for all fixed income bond equivalent yields on an annualized basis, not semi-annual compounded basis as is the convention. Commercial paper, therefore, looked like it had a very high yield which carried over into the calculation of the portfolio blended yield. QED adjusted the securities to reflect the actual accounting methodology and run the annualized yield on the blended yield on a semi-annual basis for a fairer representation. This change brought December's yield number down from 5.01% to 4.96%.

He also explained that, in coordination with QED, the General Fund account at Northern Trust now separates the Core Portfolio, draws the liquidity from the General Fund Liquidity Portfolio and puts it into the Core Portfolio thereby making total return calculations more accurate. Maturities continue to be laddered out on the 3-year ladder.

New MexiGROW Local Government Investment Pool (LGIP) Report

Chairperson Designee Mevi informed the committee of the LGIP status. The market value was \$792.35 million (8.5% increase over December), compared to a market value of \$819.3 million at the same point in the prior fiscal year and \$1.35 billion at the same point two years ago. Increase in the Pool balance is attributable to the positive reaction by participants to the new administration of Treasurer Lewis. The gross yield of the LGIP portfolio decreased 1 basis point to 5.30%. The weighted average maturity (WAM) was 41 days, up from the December WAM of 31 days, but within the allowable limit of 50 days. The portfolio was comprised of 38.4% in U.S. government agency securities, 34.7% in A-1+ commercial paper, 26.8% in AAA money market funds, and 0.1% in the bank account balance. January investment activity (\$273 million total) included: \$178.4 million in A-1+ commercial paper with an average yield of 5.37% and average term of 73.4 days; \$94.8 million in agency discount notes with an annualized yield of 5.27% and average term of 101.5 days. LGIP earnings totaled \$3.47 million, up from December earnings of \$3.25 million. Fiscal year-to-date earnings totaled \$21.6 million compared to \$17.8 million through the same period last fiscal year. The 30-day net yield of the LGIP was 5.25%, outperforming the 30-day net S&P Rated Government Investment Pool (GIP) index (5.12%) by 13 basis points. The 30-

day gross yield, 5.30%, trailed the 30-day gross S&P Rated GIP index of 5.33% by 3 basis points. Participant contributions totaled \$112.6 million and withdrawals totaled \$52.5 million. The administrative fee assessed to participants for January was 4.8 basis points, with a total fiscal year-to-date fee collected of \$224,000.

Member Cassidy asked if there were any major segments that are not participating in the LGIP. Ms. Mevi informed the Committee that the City of Albuquerque may participate in the LGIP after several years of non-participation now that LGIP yields are so competitive. She will meet with them in the near future.

Bond Proceeds Investment Pools (BPIP) Report

Mr. Lujan reported that the Tax-Exempt BPIP had a market value of \$450.8 million, a decrease of 1.5% from December. Earnings for the month were \$1.94 million. At month-end, the yield was 4.97% (35 basis points above the highest arbitrage yield limit of any bond issue in the fund, 4.62%, which is also the selected benchmark). The term was 111.8 days. The breakdown of holdings was 54.3% in U.S. Treasury notes and bills, 12.1% in U.S. Agency securities, 26.5% in the overnight repurchase pool, and 7.0% in flexible repurchase agreements. No purchases were made in January for this fund.

The market value of the Taxable BPIP was \$776.9 million, a 4.4% decrease from December (\$36 million was withdrawn for projects – one of the largest draw downs in the last 5 to 10 years). Earnings were \$3.20 million. The yield and term were 4.80% and 289.2 days, respectively. Benchmark yields were: 5.05% 2-year constant maturity agency 12-month moving average; and, 5.01% Merrill Lynch custom index. The holdings were 25.7% in money market mutual fund shares, 45.8% in U.S. Agency bonds, 14.3% in flex repurchase agreements, and 14.1% in the overnight repurchase pool. Approximately \$60 million of U.S. Agency bonds was purchased to match several missing maturity buckets in the existing ladder with yields ranging from 5.05% to 5.29%.

Summary of Broker Participation

Chairperson Designee Mevi pointed out to the Committee a new page in the report that summarizes, for the agency as a whole, broker participation by month for the fiscal year by primary and secondary market.

Economic and Investment Outlook

Mr. Lujan reported that strong economic indicators in December, supported by strong economic indicators again in January, changed the landscape from one in which rates were dropping precipitously to one in which rates are more market-neutral. This allows for continued extension of STO's portfolio WAM in a pre-September rate environment. Moving forward, the economy is expected to grow, albeit at a slower rate, providing a better opportunity to extend portfolio WAM than at any time in the last four months. The General Fund Core Portfolio will continue to build its three-year ladder; LGIP portfolio management will continue to be driven by compliance to credit quality rating criteria; and, the Taxable BPIP will begin investing in callable securities in this more stable rate environment.

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

State Agency Deposit Balances in Financial Institutions

Chairperson Designee Mevi stated that no financial institutions exceeded the statutory limitations on equity capital and deposit ratios at December 31. There were 505 accounts with a balance of \$93.3 million; 5 accounts were closed and 8 were opened. Account interest for December totaled \$254,876.

Collateral Report

Mr. Garduño informed the Committee that one institution, Bank of the Southwest, was out of compliance due to inclement weather deposit timing issues, but was fully compliant by early January. Mesilla Valley Bank in Las Cruces will be required to collateralize at 100% this quarter (instead of 50%) due to a decrease in its net income. All other financial institutions were properly collateralized for the month.

IV. STAFF REPORTS

Quarterly Investment Report – Barbara Fava, PFM Asset Management

Ms. Fava complimented the LGIP's performance as it now outperforms Standard & Poor's LGIP rate. She suggested that, for the LGIP, commercial paper exposure be maximized and that overnight repurchase agreements are a good alternative to money market funds and short-term federal agency discount notes. She also suggested a WAM of 40 days (already achieved in the LGIP, as pointed out by Member Bohlin). For the General Fund, Ms. Fava reported an annualized 12 basis points out performance against the benchmark and commended Mr. Canavan on his management. Ms. Fava concurred with Mr. Lujan's analysis that the Taxable BPIP should consider callable securities. She also recommended that, in the Tax-exempt BPIP, the STO should look at issues on a case-by case basis to see if there are any applicable exemptions from rebate. After discussion among the members as to the wisdom of that approach, Mr. Lujan informed the Committee that the types of projects that each bond series funds probably do not qualify. Chairperson Designee Mevi informed the group that the STO would consider the recommendation, especially if proposed legislation passes that creates a bond proceeds investment pool in the LGIP.

Memo – Follow-up to Severance Tax Transfer Error

Chairperson Designee Mevi referred the Committee to the memo reporting the resolution of the severance tax transfer payment error. A payment in the amount of \$526,252.03 representing interest earned on \$22,254,808 from July 3 through December 12, 2006, was completed on January 31, 2007. The memo was also sent to Katherine Miller/DFA and David Abbey/LFC.

V. NEXT MEETING

Wednesday, March 14, 2007, 9:00 a.m.

VI. ADJOURNMENT

Member Bohlin motioned to adjourn the meeting; seconded by Member Cassidy, the meeting adjourned at 10:02 a.m.