

STATE INVESTMENT COMMISSION
MINUTES
DECEMBER 5, 2024
10:00 AM

The State Investment Commission (“SIC” or “the Commission”) meeting was called to order on Thursday, December 5, 2024, in Conference Room C109 of the Transportation Cabinet Office Building by Sam Burchett, proxy for Treasurer Mark Metcalf, Kentucky State Treasury. Mr. Burchett asked for a roll call. Other members present were Secretary Holly M. Johnson, Finance and Administration Cabinet (“FAC”); and Controller Joe McDaniel, Office of the Controller.

Office of Financial Management (“OFM”) Staff Present: Chelsey Couch, Executive Director of OFM; Kim Bechtel, Deputy Executive Director; Steven Starkweather, Deputy Executive Director; Amber Lee; Daniel Auxier; Richard Osborn; Brad Vickers; and Aubry McDonald.

Other Guests: Robert Gullette, Kentucky State Treasury.

Mr. Burchett verified a quorum was present, and the press was notified of the meeting.

Mr. Burchett called for a motion to approve the minutes from the September 10, 2024, meeting. A motion was made by McDaniel and was seconded by Ms. Johnson to approve the minutes. Motion **CARRIED**.

Compliance Reporting – Mr. Vickers referred to the letter in the packet and stated there were no Statute or Administrative Regulation violations during the reporting period.

Investment Overview – Ms. Bechtel directed the Commission’s attention to Attachment C for an additional topic for this meeting, Investment Overview. She stated the Overview was created several years ago and used to share valuable guidelines about the Pools that are managed by OFM staff. Considering that everyone in the meeting had seen a version of the overview, a refresh was given to the presentation, for future use, while also providing a quick review of what is allowed in statutes and regulations.

Ms. Bechtel stated the Investment Objectives are outlined in Section 2 of 200 KAR 14:011. The main objective and primary goal is preservation of principal. In the remaining sections of this regulation, it details the investment securities and criteria that will support this objective. The second objective is to maintain liquidity. With 3,000+ accounts in three different Pools, OFM constantly monitors daily movements and projects future needs to make sure cash will be available. Several agencies and universities that will have very large movements are great about communicating those movements in advance. She stated, even though it isn’t a perfect world, and mistakes happen, or communication fails, we are ready to handle those issues with ease. The third and final objective is maximization of return. Benchmarks have been established for each Pool.

The second slide details the Investment Pools. The Pool placement of the 3,000+ accounts has been determined by various factors detailed in KRS 42.500 and also in 200 KAR 14:011 (such as

universities and agencies not addressed in KRS 42.500). The next slide details the permitted Investments and Limits for each Pool. The original slides have been consolidated into a table format that summarizes the parameters outlined in 200 KAR 14:011, 14:081 and 14:091. The Short and Intermediate are permitted to purchase the same types of investments but are managed differently based on investment needs as outlined in the previous slide. The Limited can only purchase Money Market Securities to maintain the Net Asset Value of \$1. The final slide lists our website resources.

Market Overview – Mr. Auxier directed the Commission’s attention to Attachment D, the fourth quarter Market Overview. He noted the data in the packet was compiled about three weeks ago which in today’s fast moving market, is an eternity, but would do his best to update some of these numbers as we go. As the story has been all year, interest rates have swung wildly this quarter as the market attempted to find a direction. The chart shows the two-year treasury climbing back up to 4.33% but since then has fallen back to 4.15%, further highlighting the continued volatility. The election results played no small role in this as traders digested both future policy plans and additional labor market and inflation data. The bottom line is traders still have no idea which way the market will go and the consensus seems to change every week. On the next page, a snapshot of the yield curve as it was on November 12th. It largely looks similar today however the initial dip that you see in the mid-term is even more pronounced now with the two-year and five-year dropping in recent weeks. While still inverted, recent cuts by the Fed have made enough of a dent on the front end that the 2/10 spread is actually positive at the moment. It will take further cuts in order to remove the inversion entirely but right now, the prospect of future cuts is up in the air as we will discuss shortly. He pointed out, on the right side you will see a box explaining what this means for our portfolios. While earnings are off to another strong start this year, it’s unlikely we’ll approach the highs of last year will rate cuts already taking effect on the short-end. On the third page you’ll see a chart of the consumer price index. After stalling out around 3%, progress towards the 2% inflation goal resumed in the past few months but still remains above the target. While the chart here shows inflation reaching 2.4%, the latest reading since then actually ticked up to 2.6%, showing there’s work still to be done. Currently there’s a 74% chance of a 25bps cut priced in for the December 18th meeting, but after that it remains to be seen how much more rates will drop in the near term. At this point, with inflation staying above 2% and the job market remaining relatively healthy, it doesn’t appear further cuts are entirely justified over the next quarter. The Commission took no action.

Cash Flow – Mr. Osborn presented the Monthly Average Investable Balances Cash Flow Summary. Looking at the fiscal year 2025, represented by the red line, the average investable balance was around \$14.6 billion. He noted the receipts in the General Fund for August, fell 4.5% compared to August of 2023. For September, receipts fell 2.8% compared to September of 2023. For October, receipts fell 3.9% compared to October of 2023. This brings year to date receipts to even with fiscal year 2024 receipts. The Commission took no action.

Short Term Pool – Ms. Lee directed the Commission to Attachment F, on PDF page 23, you can see the Average Investable Balances Graph. The average investable balance in the Short Pool was just under \$6 billion, which is a slight decline since July due to spending that typically occurs during the beginning of the fiscal year. She then directed the Commission to the next page showing the Short Term Pool Portfolio Composition as of October 31st. There were no significant changes

since the last meeting. The allocation to money market funds increased 2.6% with all other changes in allocations less than 1.5%. Page 25, the Portfolio Performance, the orange bar represents the Short Term Pool and the dark blue bar represents the benchmark, which is the Bank of America Merrill Lynch 0-3 Month U.S. Treasury Bill Index. As of October 31st, the short-term portfolio remained in-line with the benchmark. The Commission took no action.

Limited Term Pool – Ms. Bechtel presented the Limited Term Pool monthly report and directed the Commission to the Limited Term Pool monthly performance graph, Attachment G on page 28. She stated for October the one month return of 0.407% slightly underperformed the benchmarks. The next page, the Limited Pool Holdings Summary, the total amortized cost as of October 31, 2024, was slightly under \$3.1 billion with a net outflow of approximately \$94 million for the month.

Ms. Bechtel directed the Commission to page 30 which detailed the Pool Ratings and Sector Distribution. The credit rating distribution percentages based on short term and long term ratings are on the left side of the page. The right side of the page, the distribution was mainly invested in U.S. Treasuries at 15%, government agencies at 45% and money market funds at 32% of the Pool. Moving forward to the Liquidity and Maturity page, the Limited Pool continued to stay within guidelines. As of October 31, 2024, the Weighted Average Maturity was 23 days with the last three-month average at 24 days. The daily liquidity was 43.6% with weekly at 48.5% and remained above requirements. She then directed the Commission to page 32 for the Limited Pool, Net Asset Value graph. The line of the shadow NAV continued to show slight fluctuations in value but has not exceeded 0.0025 level to trigger a notification to SIC.

The final document under attachment G is the Limited Pool Liquidity Analysis detailing transactions and largest accounts in the portfolio. The largest daily withdrawals occurred in the Medicaid Trust and Benefits in September and University of Kentucky Accounts in August. The largest weekly withdrawals occurred in Medicaid Account in September and University of Kentucky Accounts in August and October. The largest accounts for October were University of Kentucky, Personnel Self-Insurance and Medicaid Benefits Fund. The staff will continue to maintain daily and weekly liquidity of 15% and 30%, respectively. The Commission took no action.

Intermediate Pool Performance – Mr. Auxier directed the Commission to page 36 of Attachment H, titled Intermediate Term Pool Fundamentals. While August and September saw typical outflows, State Prop 131 closed in October and boosted the portfolio balance by \$570 million to a record \$5.7 billion. Duration has increased to .84 as we invested some of the new money further out the curve but more importantly, a continued rotation out of US Treasuries has resulted in market yields that are currently topping both benchmarks. He then directed the Commission to the pie charts, showing Intermediate pool currently consists of 50% treasuries while the remainder is a diversified mix of higher yielding securities that still maintain an overall AAA quality rating. On the next page you can see the results of that sector allocation as Intermediate Pool continues to perform well relative to the benchmarks. The Commission took no action.

Credit Considerations – Mr. Auxier directed the Commission to the first page of Attachment I and stated that it was very simple this time, there were no changes this quarter. This item will

require approval from the Commission. Mr. Burchett called for a motion. A motion was made by Ms. Johnson and was seconded by Mr. McDaniel. Motion **CARRIED**.

Trading Limits – Ms. Bechtel directed the Commission to Attachment J, Trading Limits. It was suggested that Mr. Osborn’s, who handles the Money Market Trader position, trading limit be increase as well as bring the whole groups limits up due to the amount of cash OFM continues to have. This item will require approval from the Commission. Mr. Burchett called for a motion. A motion was made by Mr. McDaniel and was seconded by Ms. Johnson. Motion **CARRIED**.

There being no further business, Mr. Burchett called for a motion to adjourn. Ms. Johnson made a motion to adjourn which was seconded by Mr. McDaniel. With no further business before the Commission, the meeting adjourned at 10:18 AM ET.

Respectfully submitted,

Signed by:

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Secretary