

STATE INVESTMENT COMMISSION
MINUTES
JUNE 18, 2024
2:30 PM

The State Investment Commission (“SIC” or “the Commission”) meeting was called to order on Tuesday, June 18, 2024, in Conference Room C106 of the Transportation Cabinet Office Building by Mark Metcalf, Kentucky State Treasury. Treasurer Metcalf asked for a roll call. Other members present were Geri Grigsby, proxy for Secretary Holly M. Johnson, Finance and Administration Cabinet (“FAC”); Controller Joe McDaniel, Office of the Controller; and Paul Goodpaster, representing the Bluegrass Bankers Association.

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

Other Guests: Robert Gullette and Sam Burchett, Kentucky State Treasury; and Megan Poe, FAC.

Treasurer Metcalf verified a quorum was present, and the press was notified of the meeting.

Treasurer Metcalf called for a motion to approve the minutes from the March 12, 2024, meeting. A motion was made by Ms. Grigsby and was seconded by Mr. McDaniel to approve the minutes. Motion **CARRIED**.

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

Market Overview – Mr. Auxier directed the Commission’s attention to Attachment C, Market Overview. He stated this is done every quarter to help provide larger context for the portfolio metrics presented. The question looming over the first half of the year continues to be: when will the Federal Reserve decide inflation has cooled enough to justify beginning the rate cut cycle? Until that’s decided, he stated the market is in a wait-and-see mode. This is shown in the chart for the two-year treasury on the right. After the relentless rise in 2022, yields have remained constrained since, bouncing between 4% and 5% but never breaking out in either direction. Mr. Auxier stated as of this morning, the first cut is fully priced in for the November meeting and according to traders, there’s a 92% chance of a second cut immediately after in the December. He then directed the Commission to the following page, you will see what this current rate environment means for the yield curve and by extension, our portfolios. As stated, before in previous market updates, the yield curve will remain inverted until rate cuts actually begin and rates on the short-end finally start to fall. Even with the sharp inversion, yields across the curve remain elevated and this has a large impact on our portfolios. FYTD we have posted over \$607 million in earnings with one month still remaining, by far the most profitable year our portfolios have ever seen. This compares to earnings of \$344 million for all of FY23. In addition, the Office of the State Budget Director last week stated that in May the general fund alone earned \$30.2 million in investment income, the highest total ever reported. On page 14, included is a chart of

the headline consumer price index to show what the Fed has been looking at when trying to decide when to begin cutting rates. While the stated long-term inflation goal is 2%, you can see that the decrease that began in 2022 ended suddenly above 3% and has remained there ever since, prompting the higher-for-long environment we find ourselves in now. The Commission took no action.

Cash Flow – Mr. Osborn presented the Monthly Average Investable Balances Cash Flow Summary. Looking at the fiscal year 2024, represented by the red line, the average investable balance stood at about \$14.7 billion, a 19% increase from May 2023. He noted the receipts in the General Fund for March, rose 12.7% compared to March of 2023. April, receipts rose 2.0% compared to April of 2023. May, receipts fell 5.0% compared to May of 2023. This brings the year-to-date receipts up 2.9%. The Commission took no action.

Short Term Pool – Ms. Lee directed the Commission to Attachment E, on PDF page 18, you can see the Average Investable Balances for fiscal years 2022 to 2024. Looking at fiscal year 2024, represented by the red bar, you can see that the average investable balance for May was \$7.3 billion. The next page shows the Short Term Pool Portfolio Composition as of May 31st. US Treasury Debt made up about 39% of the portfolio, US Government Agency Debt 33%, Government Money Market Funds 24%, Repurchase Agreements less than 3%, and Commercial Paper 1%. She then directed the Commission to page 20 of the PDF, Portfolio Performance and showed numbers as of May 31st. The orange bar represents the Short Term Pool and the dark blue bar represents the benchmark, which is the Fed Funds Rate Index. As you can see, the portfolio slightly underperformed the benchmark for the three and six month time periods, as well as the inception date of July 2022 but outperformed the benchmark for the one month fiscal year to date and one year time periods. 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 F on page 23. She stated for May the one month return of 0.453% slightly outperformed the benchmarks. The next page, the Limited Pool Holdings Summary, the total amortized cost as of May 31, 2024, was approximately \$2.9 billion with a net inflow of \$190 million for the month.

Ms. Bechtel directed the Commission to page 25 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 30%, government agencies at 34% and money market funds at 27% of the Pool. Moving forward to the Liquidity and Maturity page, the Limited Pool continued to stay within guidelines. As of May 31, 2024, the Weighted Average Maturity was 32 days with the last three-month average at 29 days. The daily liquidity was 36.5% with weekly at 39.9% and remained above requirements. She then directed the Commission to page 27 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 maximum divergence continued to be 0.0005871 which occurred on November 23, 2022, and remained within the guidelines.

The final document under attachment F 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 Accounts in March and May. The largest weekly withdrawals occurred in the Medicaid and University of Kentucky Accounts in March and May. 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 31 of Attachment G, titled Intermediate Term Pool Fundamentals. May saw a large jump in Pool assets as a bond closing for State Prop 130 and the funding of the GRANT program combined to boost the balance by \$532 million over the previous month. Both yield and duration came in as expected for all three months, largely falling in between both benchmarks. At the bottom of the page, you can see the sector allocation for the portfolio and how it compares to the benchmarks. There has been little change since the last quarter, with treasury allocation continuing to slowly drift downward as we shift into higher yielding securities without noticeably increasing risk. He stated the effects of this can be seen on the following page in the Intermediate Pool returns. Despite falling between the two benchmarks in terms of duration, the Intermediate Pool has exceeded both benchmarks comfortably Fiscal Year to Date. He stated this will not last forever because benchmark A, with its longer duration, will see strong returns once rates begin to fall. But until then, an advantageous rebalancing of assets has resulted in the Pool's healthy performance. The Commission took no action.

Credit Considerations – Mr. Auxier directed the Commission to the first page of Attachment H and presented that there were a few changes for this quarter, as you can see at the bottom MUFG Securities Americas was removed and added MUFG Bank Ltd/NY. While this is the same parent company and carries the same credit rating, commercial paper is only issued under the second name, so we wanted the approved list to reflect that since that is the primary reason MUFG is on our list to begin with. The other two additions are Bank of America and Cantor Fitzgerald, and both are added solely for overnight repurchase agreements, which you can see reflected in the list above where those two names are not approved for CP or bonds. This item will require approval from the Commission. Treasurer Metcalf called for a motion. A motion was made by Mr. Goodpaster and was seconded by Mr. McDaniel. Motion **CARRIED**.

Approval of Broker Dealer – Mr. Auxier directed the Commission to Attachment I on page 36, the list of approved broker/dealers. He stated lately we have had several requests to be added to this list so after vetting the companies and making sure they met the qualifications; it was agreed to add them to the non-primary dealer section. These names are Canadian Imperial Bank of Commerce, Hilltop Securities, Keybank Securities, and South Street Securities. Truist Securities was removed from this year's list because they have exited the fixed income market for now. This item will also require approval from the Commission. Treasurer Metcalf called for a motion. A motion was made by Mr. McDaniel and was seconded by Ms. Grigsby. Motion **CARRIED**.

Approval of NRSRO's – Mr. Osborn directed the Commission to Attachment J, for the Nationally Recognized Statistical Rating Organization (or NRSRO) Approval. He stated the NRSRO Approval is presented annually in June for the upcoming Fiscal year. There were no surprises with Moody's, S&P, and Fitch remaining the largest rating agencies. He recommended Moody's, S&P, and Fitch be adopted as the NRSROs used for credit compliance in FY2025. This item will also

require approval from the Commission. Treasurer Metcalf called for a motion. A motion was made by Mr. Goodpaster and was seconded by Ms. Grigsby. Motion **CARRIED**.

Next on the agenda were three Kentucky Administrative Regulations that needed to be updated. Ms. Bechtel presented amendments for each.

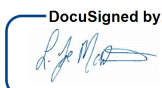
200 KAR 14:011 Amendment – Ms. Bechtel directed the Commission to Attachment K, 200 KAR 14:011 Amendment. This amendment clarifies investment limits on individual pools. In addition, it increases the limits, by less than inflation, of capital requirements for approved broker dealers in Section 10. This item will require approval from the Commission. Treasurer Metcalf called for a motion. A motion was made by Ms. Grigsby and was seconded by Mr. Goodpaster. Motion **CARRIED**.

200 KAR 14:081 Amendment – Ms. Bechtel directed the Commission to Attachment L, 200 KAR 14:081 Amendment. This amendment contains primarily technical and grammatical updates. This amendment brings the regulation up to the current standards adopted by the State Investment Commission. This item will require approval from the Commission. Treasurer Metcalf called for a motion. A motion was made by Mr. Goodpaster and was seconded by Mr. McDaniel. Motion **CARRIED**.

200 KAR 14:091 Amendment – Ms. Bechtel directed the Commission to Attachment M, 200 KAR 14:091 Amendment. This amendment contains primarily technical, formatting, and grammatical updates. This item will require approval from the Commission. Treasurer Metcalf called for a motion. A motion was made by Mr. Goodpaster and was seconded by Ms. Grigsby. Motion **CARRIED**.

There being no further business, Treasurer Metcalf called for a motion to adjourn. Mr. Goodpaster made a motion to adjourn which was seconded by Mr. McDaniel. With no further business before the Commission, the meeting adjourned at 3:02 PM ET.

Respectfully submitted,

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Secretary