STATE INVESTMENT COMMISSION
DECEMBER 7, 2007

MINUTES

The State Investment Commission was called to order on Friday, December 7 2007, at 1:30 p.m. in Room 76 of the Capitol Annex by Jonathan Miller, State Treasurer. Other members present were Kristin Webb, Deputy Secretary of the Finance and Administration, Secretary, Finance and Administration Cabinet; and George Spragens, President, Farmers National Bank in Lebanon, Kentucky.

Treasurer Miller verified that a quorum was present and that the press had been notified of the meeting.

Treasurer Miller called for a motion to approve the minutes of the September 26, 2007 meeting. A motion was made by Mr. Spragens and seconded by Ms. Webb to approve the minutes of the September 26, 2007 meeting. Motion CARRIED.

Dwight Price, Portfolio Administrator, Office of Financial Management, stated that discussion would begin with issues with non-Kentucky state funds. Mr. Price stated that Bloomberg reported several weeks ago that the asset-backed commercial paper market fell as some structured investment vehicles (SIVs) began to experience mark-to-market losses. Mr. Price explained a SIV is a fund which borrows money by issuing commercial paper at low interest rates and then lends that money by buying long-term securities at higher interest rate. He further explained that the underlying investments for the SIVs in most instances was sub-prime mortgages. Mr. Price stated that the state of Florida revealed, after an open records request, that they owned $1.5 billion of downgraded and defaulted debt affected by the collapse of the sub-prime market. He further stated that this resulted in local governments and schools pulling out $13 in assets before the fund was frozen. Mr. Howard stated that Maine, Orange County, California and the city of Seattle also have this problem. Mr. Price informed the members that the Commonwealth does not own any commercial paper issues by SIVs.

Mr. Howard noted that the Commonwealth's portfolio is marked to market daily and staff knows the value of each underlying security.

Steve Jones, Portfolio Administrator, Office of Financial Management, presented a complete list of the holdings of mortgage related securities owned by the Commonwealth. Mr. Jones stated that the Commonwealth holds approximately $629 million of mortgage related securities out of a $3.9 billion portfolio, or 16 percent. Mr. Jones pointed that out of that 16 percent; over 10 percent is backed by Agency or GNMA (Ginnie Mae) securities.

George Spragens pointed out that the net loss on the $630 million is approximately $2.2 million and represents approximately one third of one percentage point. Mr. Spragens further added that unless the security is actually sold, the loss is only a paper loss.
Mr. Jones added that each of the securities has been reviewed by the rating agencies and the ratings have been reaffirmed at AAA. Mr. Price further added that with 22 percent of the portfolio in cash, liquidity is not an issue for the Commonwealth.

Mr. Price stated that staff will continue to monitor the securities in the portfolio and should the rating drop appropriate steps would be taken to minimize the loss to the portfolio.

Mr. Jones presented an update on the 2008 TRAN. He stated that the spread on the TRAN is approximately 150 basis points. Mr. Jones pointed out that the Commonwealth has earned approximately $581,000 on the floating side of the swap. He further stated that the Commonwealth has earned approximately $1.5 million on the fixed side of the swap for a total net income to date of $2.4 million. Mr. Jones stated the projected earnings on the TRAN were approximately $5.5 million and it appears that the TRAN is on target to meet that target.

Treasurer Miller asked if the earnings were reported to the Consensus Forecasting Group. Mr. Price indicated that was correct.

With no further business before the Commission, a motion was made by Mr. Spragens and seconded by Ms. Webb to adjourn the meeting. Motion carried and the meeting was adjourned.

Respectfully submitted,

F. Thomas Howard
Secretary