OREGON SHORT-TERM FUND
BOARD MEETING
Minutes
October 28, 2010

OSTF Location:	Orrick, Herrington & Sutcliffe LLP 1120 NW Couch Street, Suite 200 Portland, OR 97209
Board Attendees:	Douglas E. Goe, Orrick, Herrington & Sutcliffe LLP Darren Bond, Oregon State Treasury Deanne Woodring, Davidson Fixed Income Management Wayne Lowry, Sherwood School District Stewart Taylor, City of Albany (via phone)
Attendees (Staff):	Perrin Lim, Oregon State Treasury Tom Lofton, Oregon State Treasury Ellen Hanby, Oregon State Treasury Judy Whaley-Fultz, Oregon State Treasury (via phone) Norma Harvey, Oregon State Treasury (via phone) Heidi Rawe, Oregon State Treasury Nancy Baldwin, Oregon State Treasury Michael Cutler, Oregon State Treasury Andrea Belz, Oregon State Treasury
Attendees (Other):	Jason Neff, City of Redmond Rhyan Van Horn, TriMet Byron Williams, Secretary of State (SOS) Audits Division Kelly Olson, Secretary of State (SOS) Audits Division Teri Schwartz, Cutwater Asset Management (via phone) Mark McClure, Cutwater Asset Management (via phone) Emily Ferguson, Cutwater Asset Management (via phone) Mary Donovan, Cutwater Asset Management (via phone) Michael Montgomery, City of Portland (via phone) Eric Johansen, City of Portland (via phone)

i. Opening Remarks

Doug Goe welcomed all to the OSTF Board Meeting

ii. Review and Approval of Meeting Minutes

a. July 29, 2010

MOTION: Wayne Lowry moved approval of the July 29, 2010 minutes. The motion was seconded by Deanne Woodring and passed unanimously by the board.

b. September 23, 2010

MOTION: Mr. Lowry moved approval of the September 23, 2010 minutes. The motion was seconded by Ms. Woodring and passed unanimously by the board. Note: Stewart Taylor had not been given the opportunity to review the minutes prior to the meeting and therefore abstained from the vote at this time.

iii. LGP/OSTF Investment Policy Review – Sherwood School District

The Sherwood School District's Investment Policy was presented to the board by Ellen Hanby.

Comments by the Board members were:

- *In Section V, Suitable and Authorized Investments, (1) Investment Types*, in the first sentence *"…the following investments will be permitted by this policy"* Doug Goe suggested adding "*only to the extent such investment is permitted under ORS 294.035 and 294.810"* for clarification.

- *Section VI, Investment Parameters, (3) Maximum Percentages of Investments*, Deanne Woodring asked whether limiting the US Government Agencies to 20%, versus the standard 30-35% would be too restrictive in today's market. She liked that the policy incorporated bond projects as well as the whole portfolio and noted that the policy was very well written.

Comments from Sherwood School District were:

- Relating to Section VI (4), Mr. Lowry confirmed that ORS 294.052 was not included in the policy, since it did not pertain to the City of Sherwood's policy.

For the record, Mr. Goe stated that Mr. Lowry is associated with the school district and also a member of the OSTF Board, however, since the board is not an approving body, it isn't a matter of conflict. He thanked Mr. Lowry and expressed thanks for a terrific policy.

iv. LGP/OSTF Investment Policy Review – City of Redmond

Ms. Hanby presented the City of Redmond's Investment Policy to the board and noted that it was a pleasure to work with Mr. Neff.

Comments by the Board members were:

- *Delegation of Authority* - For clarification purposes, Mr. Goe suggested that in the 2nd line after "City Manager or" insert "his or her" designee.

- *Standards of Prudence, 3rd paragraph, 2nd line* - When talking broadly about compliance, referring to ORS Chapter 294, instead of citing both ORS 294.035 and ORS 294.040, would be sufficient.
- Within *Authorized Securities and Transactions, 2nd paragraph* – Deanne Woodring suggested that the language "not limited to" be added to the sentence "the city has further defined the eligible types". Relative to Ms. Woodring's comments, Mary Donovan of Cutwater Asset Management

confirmed that the intention was to define a specific list of authorized securities for the City. The City of Redmond would be authorized to recommend securities as defined in items 1 through 10 specifically. The policy would be limited to the listed securities.

- *Authorized Securities and Transactions (2) Federal Instrumentality Securities* - Darren Bond suggested that language be amended in the last paragraph, by removing "**AAA**", and using the previous language, such as "shall be rated in the highest rating category by a Nationally Recognized Statistical Rating Organization (NRSRO)".

- *Authorized Securities and Transactions, (4) Corporate Bonds* – Ms. Woodring commented that the wording in this paragraph could be confusing and suggested that the City of Redmond may want to review it.

- *Policy Revisions* – Relative to the review of policies, Mr. Bond confirmed that a future review of the City's policy is only required when substantive changes are made. Staff would advise as to what those changes would be.

- Mr. Goe, noted that the City of Redmond's policy was excellent and thanked Mr. Neff and his advisors at Cutwater Asset Management.

Comments from the City were:

- Jason Neff acknowledged Cutwater Asset Management, and thanked them for their assistance with the City of Redmond's Investment Policy; he also expressed his gratitude to Ms. Hanby for her guidance and support.

v. LGP/OSTF Investment Policy Review – City of Portland

The City of Portland's Investment Policy was brought before the board by Ms. Hanby.

Comments by the Board members were:

- *Section III, F.2, Corporate Bonds* - Deanne Woodring asked if the Weighted Average Maturity (WAM) of 18 months was too restrictive for the City's corresponding bonded debt obligations. The City of Portland responded that 18 months would be sufficient. Ms. Woodring stated that the policy was well written.
- *Section II, Responsibilities and Standards of Care* - Stewart Taylor asked what triggered a review by the OSTF Board? Ellen Hanby confirmed that it was the addition of language in Section F and G relating to corporate bonds.
- Doug Goe complimented the City of Portland on an excellent policy.

Comments from the City of Portland were:

- *Section III, H, Municipal Bonds, Minimum rating* - Eric Johansen confirmed that the second sentence of the paragraph will be amended to read as follows:

  "Only one rating from a Nationally Recognized Statistical Rating Organization (NRSRO) of the Securities and Exchange Commission (SEC) at the time of purchase **is required**".

vi. OSTF Audit Presentation – SOS Auditors

Mr. Goe introduced Kelly Olson and Byron Williams, representatives from the Secretary of State (SOS) who conducted the Financial Statement Audit of the Oregon Short-Term Fund financial statements that are distributed to the Local Governments.

Ms. Olson presented information to the OSTF Board, relative to the findings of SOS's audit. Following her presentation, staff and the board were invited to comment.

Mr. Taylor noted his appreciation to the auditors for being able to identify things that can strengthen internal control and identify areas for improvement.

Mr. Lim led a discussion which covered strengthening of internal controls within OST, relative to such topics as the transparency related to the Fund's Weighted Average Credit Quality, and third party pricing.

Darren Bond announced that Andrea Belz, who currently serves as the Chief Audit Executive at Oregon State Treasury will be stepping into a new position as the Controller. Ms. Belz will be working with Investment staff to refine procedure and documents, relative to the audit findings. He also commented that this audit team offered a level of expertise that at times has been lacking. He complimented and thanked the auditors for their diligence and efforts in this regard.

Mr. Goe thanked Ms. Olson and Mr. Williams for their presentation and attendance.

vii. Market Overview – Perrin Lim

Mr. Lim presented the OSTF Portfolio Review and Market Perspective (please see attached).

Further to a discussion at the July 29, 2010 OSTF Board meeting, Mr. Lim confirmed that he had received approval from Jeff Flynn of TRACS Financial to forward their information to Board members and staff who wish to receive it. He will send this information out via email.

viii. Market Participants Perspective – Deanne Wooding

Ms. Woodring gave a market perspective. She showed an interest for staff to give an update at January's OSTF Board meeting relating to how Fannie Mae and Freddy Mac will affect investment alternatives and the yield stretch.

ix. Global Market Perspective – Bob Woodruff

Bob Woodruff was unable to attend and will provide his perspective at the next meeting.

x. Other Items of Business – Next meeting: January 2011

No items of business.

xi. Closing Remarks

Meeting adjourned at 11:17 am.

Respectfully submitted by,

Heidi C. Rawe
Executive Assistant to the Deputy State Treasurer

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Market Overview by Perrin Lim

Market Comments

- Employment data is not expected to improve in the near-term. With no job market improvement, the housing market is not likely to see a meaningful recovery anytime soon.

- The Fed underscored its commitment to dealing with persistent economic weakness through an additional dose of quantitative easing (QE2) should conditions warrant.

    - At the August FOMC meeting, the Fed voted to reinvest principal payments on mortgage and agency debt from the Fed's current holdings into longer-term Treasuries, noting that "the pace of recovery in output and employment has slowed."

    - Also at the August meeting, Fed officials acknowledged that they were not meeting either part of their dual mandate: they tied their readiness to ease to the need to both "support the economic recovery" and "return inflation, over time, to levels consistent with its mandate" leading to the Fed's willingness to offer QE2.

    - QE2 should help growth via three main channels:
        1. Lower long-term interest rates should stimulate various forms of credit-sensitive spending – housing, other consumer goods, capital goods, and state and local construction – as well as help households reduce interest expense via refinancing.
        2. Higher equity prices should boost consumer spending via the wealth effect.
        3. A lower dollar should help narrow the trade deficit.

    - Conversely, QE2 might have no real impact and the Fed could spur inflation thereby losing its credibility.

- The possibility of significant losses among Congressional incumbents in next week's mid-term elections offers the prospect of marginally more market-friendly government policy for the balance of President Obama's current term.

- Over $200 billion of domestic debt new issuance was met with strong demand in 3Q10.

    - An accommodative Fed and slowly improving economic conditions should continue to support credit, though a double-dip recession or increasing inflation expectations would pressure corporate spreads.

    - Large cash holdings of non-financial companies make them well-positioned to increase capital expenditures, though increasing dividends, stock buyback programs and M&A are alternatives.

- The US dollar depreciated 10% against the euro in 3Q10 due to prospective Fed action and improving European fundamentals.

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Market Overview by Perrin Lim

Total Returns, Major Fixed Income Components, ending 09/30/10:

Fixed Income Sector	September	YTD
Barclays U.S. Aggregate	0.11%	7.94%
Aaa	-0.09	6.94
Aa	0.47	10.38
A	0.69	11.46
Baa	1.15	12.47
Treasuries	0.02	8.73
30-year Treasury Bonds	-2.49	20.52
10-year Treasury Notes	-0.14	14.29
5-year Treasury Notes	0.52	9.68
3-year Treasury Notes	0.31	4.76
2-year Treasury Notes	0.17	2.41
3-month Treasury Bills	0.02	0.17
3-month LIBOR	0.03	0.26
BAML 1-3 year Treasury/Agency	0.17	2.47
Agencies	0.24	5.73
MBS	-0.38	5.11
CMBS	2.12	19.32
ABS	0.36	7.45
• Credit Card	0.39	8.64
• Auto	0.25	3.19
Corporate	0.70	10.77
• Industrials	0.53	11.02
• Utility	0.19	11.96
• Financial Institutions	1.12	10.04
High Yield	3.01	11.53
• Ba	2.78	12.59
• B	2.84	10.29
• Caa	3.69	9.97
Emerging Market Sovereigns	2.38	15.54

Source: Barclays Capital, Bank of America Merrill Lynch

Oregon Short-Term Fund Information

Outlook and Strategy

Given the uncertainty with respect to employment and housing statistics, QE2, expectations for inflation, the weak US$ and the growing government deficit, the OSTF is generally structured with a defensive bias, both in terms of interest rate risk and credit risk.

Staff believes the downside risks outweigh the upside risks and, to express this view, adjustable rate securities have been a core holding for the fund. That said, with the Fed maintaining current monetary policy "for an extended period," staff continues to seek opportunities for positive carry versus the very front-end of the yield curve, where yields range between 0.05%-0.25% (1-25 bps). The weighted-

average-maturity, or WAM, of the fund was 149 days as of September 30, 2010, and is currently ~158 days.

At month-end, the 48.5% allocation to corporate indebtedness hovers close to the maximum 50% allowance as corporate fundamentals remain healthy. Currently, the allocation stands at ~35%.

The approved commercial paper list has been continuously revised over the past year to include additional high quality credits and to remove those credits that have been downgraded or that are perceived by staff to bear higher-than-desired risk or potential balance sheet pressure in the future. Staff continues to diligently review the approved credits as well as potential new programs that may add value and safety to the OSTF.

General Fund
In the fiscal year ended June 30, 2010, the General Fund had experienced negative cash balances. The current fiscal year may witness pressure on negative cash balances because of the length of time before the State will have sufficient revenue to cover the overdraft. The OSTF provides liquidity to those state agencies, including the General Fund, with short-term negative cash balances. Presently for the General Fund, compensation for these overdrafts is calculated for every day of an overdraft occurrence at the rate of the current OSTF rate plus a spread of 130 bps. The spread is based on the three year average of the "BAML U.S. Corporate & Government, 1-3 year, AA Rated and Above Bond Index" and will be revised at the end of every fiscal year.

Staff has determined that, at the time of the overdraft, the prudent maximum available per state agency will be 1.5% of monies held in the OSTF, with the exception of the General Fund, which will be limited to 10.0% of monies held in the OSTF.

Securities Lending
Net OSTF securities lending income year-to-date through September 30, 2010 amounted to $2.682 million versus $8.833 million in the prior year YTD period, a decrease of $6.151 million.

Additional Items
In the future, staff will work with the OSTF Board and the OIC to further revise and enhance the portfolio investment rules and guidelines (4.02.03).

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Select Portfolio Statistics & Compliance, as of September 30, 2010:

Compliance	Policy	Actual	Par Value
Maturity Distribution			
Portfolio maturities less than 93 days	> 50%	76.88%	$7,611,412,000
Portfolio maturities between 94 days & 1 year		11.05%	1,093,882,000
Portfolio maturities greater than 1 year	< 25%	12.07%	1,195,343,000
Maturities greater than 3 years	0%	0.00%	0
Total Maturity Distribution		100.00%	$9,900,637,000
Diversification			
Treasury and/or Agency Securities	0-100%	40.52%	$4,011,279,000
TLGP/FDIC Securities	< 50%	10.48%	1,037,215,000
Commercial Paper (minimum A-1/P-1)		18.29%	1,810,759,000
Corporate Bonds		30.25%	2,995,334,000
Total Corporate Indebtedness	< 50%	47.72%	4,956,410,000
Time Certificate of Deposit's	< 20%	0.47%	46,050,000
FDIC/NOW Deposits		0.00%	0
Total Diversification		100.00%	$9,900,637,000
Top Ten Holdings			
1. Federal Home Loan Bank	33%	13.79%	$1,365,715,000
2. Freddie Mac	33%	11.03%	$1,091,948,000
3. TLGP/FDIC	50%	10.48%	$1,037,215,000
4. Fannie Mae	33%	10.04%	$994,116,000
5. US Treasury	100%	4.55%	$450,000,000
6. Koch Resources	5%	3.36%	$332,400,000
7. UBS AG Stamford CT	5%	3.03%	$300,000,000
8. JP Morgan Chase & Co.	5%	3.00%	$297,235,000
9. General Electric Capital Corp.	5%	2.46%	$279,006,000
10. Citigroup Inc.	5%	2.80%	$277,539,000
Total Top Ten Holdings		64.90%	$6,425,174,000
Total Average Credit Quality			
Moody's or Standard & Poor's	Minimum Aa2 or AA	Aa2/AA	
Interest Rate Exposure (adjusted for variable rate securities)			
WAM, exposure in days		149 days	
Fixed versus Variable Weights:			
Fixed Rate		72.49%	$7,176,972,000
Variable Rate		27.51%	$2,723,665,000

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Total Return Performance, as of September 30, 2010:

	September	3 mos.	YTD	1 yr	2 yrs	3 yrs	4 yrs	5 yrs
OSTF	0.10	0.31	0.73	0.94	2.57	1.88	2.76	3.14
91 Day T-Bills	0.01	0.04	0.08	0.13	0.26	1.13	2.14	2.61
Value-Added	*0.09*	*0.27*	*0.65*	*0.81*	*2.31*	*0.75*	*0.62*	*0.53*

Source: State Street Investment Analytics