

Achieving Dependable Investment Performance

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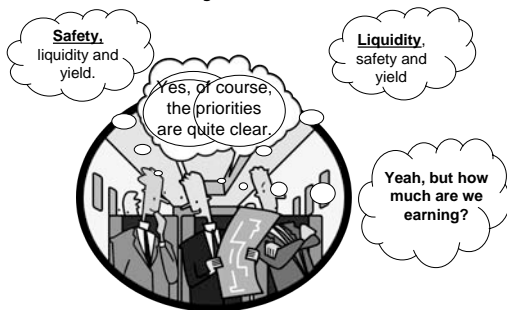
Topics Covered

1. Defining Investment Objectives
2. Improving Investment Performance
3. Developing an Investment Strategy
4. Protecting Against Risk
5. Opportunities in Today's Market
6. Evaluating the Investment Program

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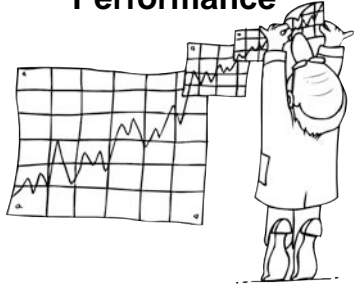
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Defining Investment Objectives



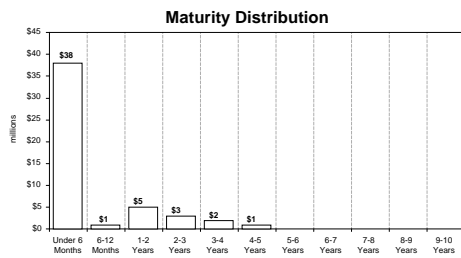
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Improving Investment Performance



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The Most Effective Way to Improve a Portfolio's Performance Is to Reduce Excess Liquidity



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Benefits of Cash Flow Analysis

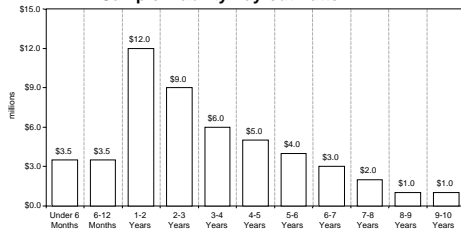
- Identifies cash needs and periods of shortfalls
- Ensures liquidity when needed
- Improves investment returns

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Analyze Cash Flow Data to Determine Appropriate Maturity Structure

Sample Liability Pay-out Pattern

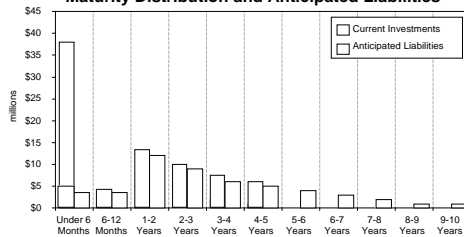


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Getting From Here to There

Maturity Distribution and Anticipated Liabilities



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Value of Investing Longer

Risk/Return of Various Benchmarks
10 Years Ended 3/31/07

Merrill Lynch Index	Duration	Overall Return	Cumulative Value of \$50 Million
3-Month Treasury Bill	0.16 Years	3.80%	\$72,611,063
6-Month Treasury Bill	0.39 Years	3.99%	\$73,973,511
1-3 Year Treasury Index	1.68 Years	4.76%	\$79,631,919
1-5 Year Treasury Index	2.28 Years	5.09%	\$82,173,068
3-5 Year Treasury Index	3.54 Years	5.82%	\$88,024,714
5-7 Year Treasury Index	4.78 Years	6.35%	\$92,532,753
7-10 Year Treasury Index	6.56 Years	6.65%	\$88,024,714

Source: Bloomberg - Merrill Lynch Global Bond Indices

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Essential Components

- Understand your cash flows
 - Financial reports
 - Operating expenses

- Understand your tolerance for risk
 - Credit
 - Maturity
 - Diversification

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**Investment Checklist
Long Term Perspective**

- Ensure safety of principal
 - Managing interest rate risk, credit risk, safety of instruments
 - In the government services business, not in the investment gambling business – don't need to take double the risk

- Ensure adequate liquidity

- Understand permitted investments, risk tolerance, selected performance benchmark, guidelines

- Establish duration target

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**Investment Checklist
Current Perspective**

- Emphasize the optimal portfolio structure

- Identify relative value amongst sectors or investments

- Select individual maturities based on analysis of the yield curve

- Analyze specific issuers and issues for the best value

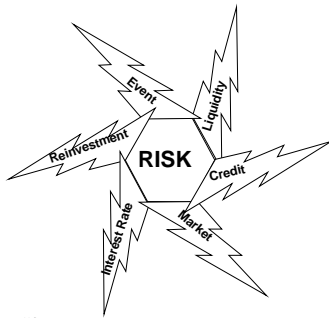
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Protecting Against Risk



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Types of Risk



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Defining Risk—What Do You Consider Risky?

1. Buying securities with longer maturities?
2. Investing the whole portfolio in the state pool?
3. Investing the whole portfolio in one sector?
4. Investing in corporate debt?
5. Purchasing callable notes?
6. Selling at a loss?

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Risk Considerations

	U.S. Treasury	Federal Agency	Corporate
Risk Characteristics	<ul style="list-style-type: none"> • AAA rated • Virtually no risk • Lower yields • Very liquid 	<ul style="list-style-type: none"> • AAA rated • Low risk • Intermediate yields • Liquidity varies 	<ul style="list-style-type: none"> • AAA – D rated • Moderate to high risk • Higher yields • Low liquidity
Short-term	Bills	Discount notes	Commercial Paper Bankers' Acceptances Certificates of Deposit
Long Term	Notes and bonds	Notes	Medium-term notes

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Ensure Liquidity by Using Liquid Securities

More Liquid	Less Liquid
Investment Pools and Money Market Mutual Funds U.S. Treasuries Federal Agencies Discount Notes BAs, CDs, CP (A-1/P-1) Federal Agencies Notes > \$50 million Federal Agencies Notes < \$50 million Federal Agencies Floating Rate Notes	Federal Agencies Callable Notes Reverse/Repurchase Agreements Mortgage Backed Securities Federal Agencies Structured Notes

* In descending order of liquidity

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Strategy for a Falling Interest Rate Environment

- Extend duration of the portfolio
- Target more of the portfolio to longer-term maturities to lock in long-term rates before they fall

2-Year U.S. Treasury Note
2000 - 2002



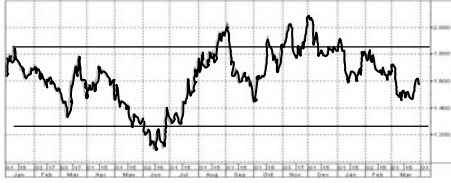
Source: Bloomberg
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Strategy for a Stable Interest Rate Environment

- Maintain duration near target
 - Avoid the trap of getting too liquid while waiting for rates to rise
- Concentrate investments in the steepest part of the yield curve

2-Year U.S. Treasury Yield History
January 2003 – March 2004



Source: Bloomberg

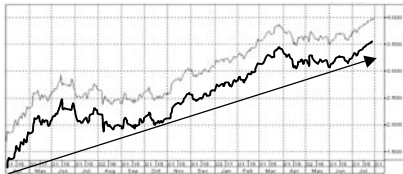
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Strategy for a Rising Interest Rate Environment

- Shorten portfolio
- Capitalize on opportunities to capture higher rates

2-Year U.S. Treasury Yield History
April 2004 – July 2005



Source: Bloomberg

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Pay Attention to Corporate Names in the News

WE DELIVER ENERGY™

BUSINESS WITHOUT BOUNDARIES

SEC Probes

**Chapter 11
Bankruptcy**

Accounting Investigations

An EDISON INTERNATIONAL™ Company

**Credit Ratings
Downgrades**

Lucent Technologies
Bell Labs Intellectual

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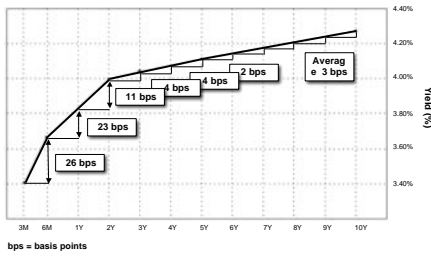
Opportunities In Today's Market



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Assess Value Along the Yield Curve

U.S. Treasury Yield Curve
July 28, 2005



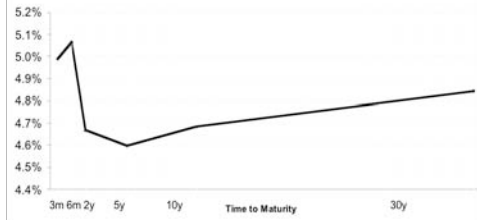
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Assess Value Along the Yield Curve

U.S. Treasury Yield Curve
April 17, 2007



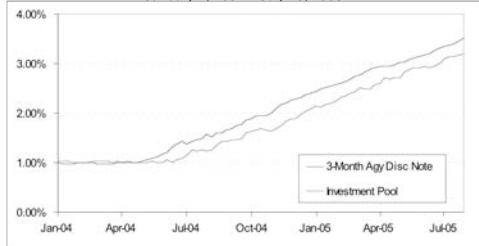
Source: Bloomberg

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Benefit of Buying a 3-Month Investment

3-Month Agency Discount Note vs. Investment Pool
January 1, 2004 – July 29, 2005



Source: TexasDAILY and Bloomberg

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Benefit of Fixed-Rate Investments

Sample Rates on July 29, 2005

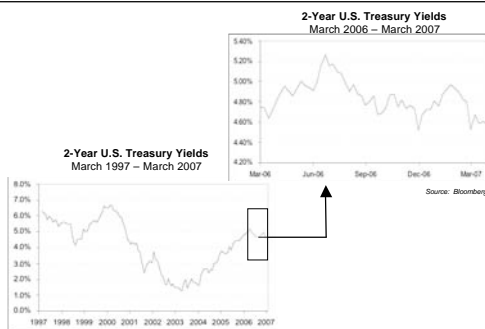
Security Type	Term to Maturity					
	3 months	6 months	1 year	2 years	3 years	5 years
U.S. Treasury	3.40%	3.66%	3.89%	3.99%	4.03%	4.11%
Federal Agency (bullet)	3.53%	3.72%	4.03%	4.17%	4.26%	4.38%
Federal Agency (callable, 1 year n/c)	-	-	-	4.32%	4.60%	5.00%
Prime Commercial Paper	3.57%	3.77%	-	-	-	-
"AA" Rated Corporate Note	-	-	4.15%	4.30%	4.41%	4.62%

Source: Bloomberg

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Interest Rate History

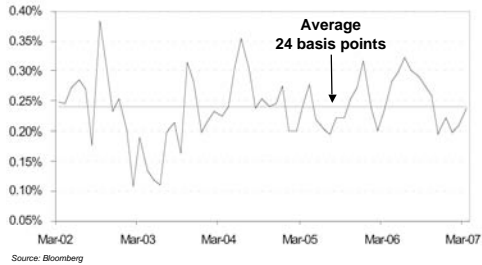


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Value Between Treasury and Agency

Spread Between 2-Year U.S. Treasury and 2-Year Federal Agency
March 2002 – March 2007

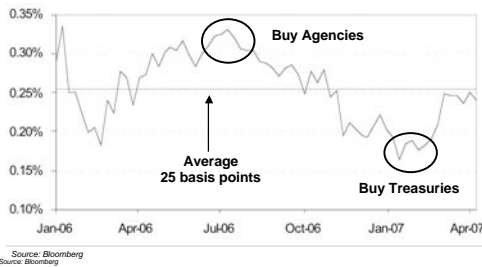


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Value Between Treasury and Agency 2006 to Today

Spread Between 2-Year U.S. Treasury and 2-Year Federal Agency
January 2006 – April 2007



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Evaluating the Investment Program

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Which Portfolio Is Most Dependable?

If Short-Term Rates Fall 25 basis-points:

- **Portfolio A?**
 - Weighted Average Maturity stays at 1 day
 - Rate falls from 5.002% to 4.752%
- **Portfolio B**
 - Weighted Average Maturity stays at 99 days
 - Rate falls from 5.17% to 5.05%
- **Portfolio C?**
 - Weighted Average Maturity falls from 99 days to 54 days
 - Rate falls from 5.19% to 4.93%

Which Portfolio Is Most Dependable?

If Short-Term Rates Fall 50 basis-points:

- **Portfolio A?**
 - Weighted Average Maturity stays at 1 day
 - Rate falls from 5.002% to 4.502%
- **Portfolio B**
 - Weighted Average Maturity stays at 99 days
 - Rate falls from 5.17% to 4.93%
- **Portfolio C?**
 - Weighted Average Maturity falls from 99 days to 54 days
 - Rate falls from 5.19% to 4.77%

Which Portfolio Is the Most Dependable?

Portfolio:	Rate on 1/01/2xx1	Short-Term Rates - 25 bps	Short-Term Rates - 50 bps	Short-Term Rates + 25 bps	Short-Term Rates + 50 bps
A	5.00%	4.75%	4.50%	5.25%	5.50%
B	5.17%	5.05%	4.93%	5.29%	5.41%
C	5.19%	4.93%	4.77%	5.31%	5.43%

All rates are spread representation rates

Which Portfolio Is the Most Dependable?

Portfolio:	Rate on 1/01/2x1	Short-Term Rates - 25 bps	Short-Term Rates - 50 bps	Short-Term Rates + 25 bps	Short-Term Rates + 50 bps
A	5.00%	4.75%	4.50%	5.25%	5.50%
B	5.17%	5.05%	4.93%	5.29%	5.41%
C	5.19%	4.93%	4.77%	5.31%	5.43%

All rates are spread representation rates

Questions?

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