

**REGULAR MEETING OF THE
MONTANA BOARD OF INVESTMENTS
DEPARTMENT OF COMMERCE**

March 1 and 2, 2001

**2401 Colonial Drive, 3rd Floor
Helena, Montana**

Thursday, March 1, 2001

AGENDA

- I. CALL TO ORDER** **1:00 p.m.**
- A. Roll Call
 - B. Approval of the January 18 & 19, 2001 Regular Meeting Minutes
 - C. Administrative Business
- II. EXECUTIVE DIRECTOR REPORTS Carroll South** **1:30 p.m.**
- A. Value-added Definition
 - B. Venture Capital Investments from Permanent Coal Tax Trust Fund
 - C. Legislative Update (Verbal)
 - D. Out-of-State Travel Requests
- III. BOND PROGRAM Geri Burton** **2:30 p.m.**
- A. INTERCAP
 - 1. Activity Report
 - 2. Staff Approved Loans Report
 - 3. Loan Requests
 - B. United Materials, Great Falls Preliminary Inducement Resolution #195 Peter Blouke
- IV. CHIEF INVESTMENT OFFICER REPORTS Jim Penner, CFA** **3:00 p.m.**
- A. Economic Overview Newsletter
 - B. Asset Allocation
 - C. REIT Proposal
 - D. Personnel Update
 - E. Quarterly Investment Performance Report
- V. MONTANA LOAN PROGRAM Delrene Rasmussen** **3:45 p.m.**
- A. Consider Commercial/Multi-Family Loans
 - 1. Curtis & Lanni Jacobson
 - 2. DSD Properties, LLC.
 - 3. KML Company, LLC.
 - 4. Kathryn L. Ogren
 - B. Staff Approved Value Added Loans
 - 1. Sonju Body Shop, Inc.
 - C. Coal Tax Loan Activity Report December and January
 - D. Mortgage Program Activity Report December and January
 - E. Commercial Loan Delinquency Report
 - F. Residential Loan Delinquency Report
- VI. PRESENTATION PYRFORD INTERNATIONAL** **4:30 p.m.**
- Mr. Bruce L. Campbell, Managing Director, and
Mr. Tony Cousins, CFA, Director, Portfolio Management

**REGULAR MEETING OF THE
MONTANA BOARD OF INVESTMENTS
DEPARTMENT OF COMMERCE**

Friday, March 2, 2001

AGENDA

VII. INVESTMENT ACTIVITY

8:30 a.m.

- A. Domestic Equities (Montcomp) Rande Muffick, CFA
 - 1. Transactions December and January
 - 2. Holdings Report
 - 3. Strategy
 - 4. Portfolio Additions
 - a. Aflac
 - b. MGIC Investment
 - c. Ambac Financial
 - d. Applied Materials
 - e. Bank of New York
 - f. Scientific Atlanta
- B. International Equities (MTIP) David Ewer
 - 1. Europe and Americas
 - a. Internal Transactions December and January
 - b. Internal International Holdings Report
 - c. Strategy
- C. Private Equities Ed Kelly
 - 1. Transactions December and January
 - 2. Venture Capital Update
- D. Montana Real Estate Portfolio (MTRP) Ed Kelly
 - 1. Transactions December and January
 - 2. Holdings Report
 - 3. Strategy
- E. Fixed Income Bob Bugni, CFA
 - 1. Transactions December and January
 - 2. Strategy
 - 3. Periodic Reports
 - a. Non-Investment Grade Holdings
- F. Security Lending Rich Cooley, CFA
- G. STIP and Treasurer's Funds Rich Cooley, CFA
 - 1. STIP Transactions December and January
 - 2. STIP Holdings Report
 - 3. Treasurer's Fund Transactions December and January
 - 4. Treasurer's Fund Holdings Report
 - 5. Strategy

VIII. BOND PROGRAM - continued

9:30 a.m.

- A. Northern Express Transportation Authority/Shelby Port Authority
Increase Recommendation David Ewer

IX. ADJOURNMENT

11:30 a.m.

The Board of Investments makes reasonable accommodations for any known disability that may interfere with a person's ability to participate in public meetings. Persons needing an accommodations must notify the Board (call 444-0001) or write to P.O. Box 200126, Helena, Montana 59620) no later than three days prior to the meeting to allow adequate time to make needed arrangements.

**MONTANA BOARD OF INVESTMENTS
DEPARTMENT OF COMMERCE**

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**2401 Colonial Drive, 3 Floor
Helena, Montana
March 1 & 2, 2001**

MINUTES

BOARD MEMBERS PRESENT:

Dick Anderson, Chairman
Douglas Bardwell
Dennis Beams
Maureen Fleming
Jay Klawon
Joel Long
F. Lee Robinson
Tim Ryan
Calvin Wilson

BOARD MEMBERS ABSENT:

STAFF PRESENT:

Peter S. Blouke, Deputy Director
Robert T. Bugni, CFA, Assistant Investment Officer
Geri Burton, Bond Program Officer
Sandra Conrady, Mortgage Analyst
Richard Cooley, CFA, Assistant Investment Officer
Kimberly Dallas, Program Assistant
David Ewer, Senior Portfolio Manager
Mona Freshour, Bond Program Assistant
Edward Kelly, Assistant Investment Officer
Herbert Kulow, Senior Portfolio Manager
Rande Muffick, CFA, Assistant Investment Officer
James R. Penner, CFA, Chief Investment Officer
Carroll V. South, Executive Director

GUESTS:

Mr. Steve Kologi
Mr. Bob Pancich
Mr. Tom Swenson, Montana Business Capital Corp.
Mr. Maurice Steinman, Cutthroat Communications, Bozeman
Mr. Bob Murdo
Mr. John Mathia, CFA, Backfin Capital LLC.

CALL TO ORDER

Chairman Anderson called the regular meeting of the Board of Investments (Board) to order at 1:00 p.m. in the conference room at 2401 Colonial Drive, 3rd Floor, Helena, Montana. As noted above, the meeting convened with nine members of the Board present.

Member Bardwell motioned for approval of the January 18 & 19, 2001 minutes; Member Fleming seconded the motion and the motion was passed 9-0.

ADMINISTRATIVE BUSINESS

- Chairman Anderson presented the following Administrative Business:

1. Chairman Anderson welcomed the newly appointed Board members Mr. Jay Klawon, Mr. Joel T. Long and Mr. Dennis Beams. Each Board member then introduced themselves and gave a brief overview of their involvement with and on the Board.

EXECUTIVE DIRECTOR REPORTS

Value Added Definition

Mr. Carroll South presented staff recommendation that the Board adopt a written definition of "Value Added" to provide direction to staff, financial institutions, and potential business borrowers when using the Value Added Loan Program. After further discussion and hearing testimony from Mr. Tom Swenson and Mr. Maurice Steinman, Member Bardwell motioned for approval to adopt the definition as written and to use this as a guideline for all future Value Added Loans; Member Wilson seconded the motion and the motion was passed 9-0.

Venture Capital Investments from Permanent Coal Tax Trust Fund

Mr. Carroll South presented to the Board research as to whether funds from Coal Tax Trust (Trust) could be invested in or through Montana Venture Capital companies. Mr. South's findings show that investments can be made out of the Trust for Montana Venture Capital companies as long as it is not in the form of an equity investment, which is precluded by the Constitution. In order for the Board to make investments out of the Trust, the "Prudent Expert Principle" is the governing law for the investment of public funds.

Mr. South also reports that the Board can invest the Trust in Debentures issued by capital companies. Neither the state constitution nor state law precludes the type of investment. The Board is given specific legal authority to purchase debentures directly from the issuer.

Should the Board wish to invest Trust funds in Montana Venture Capital Companies the investment could be structured similar to the two debentures currently held in the MSTTA portfolio. Staff suggests following the steps listed:

1. Board establishes minimum criteria for applicants, including investment staff.
2. Board develops application process and solicits applications.
3. Board selects one or more applicants based on pre-determined criteria.
4. Board sets maximum management fees.
5. Board sets maximum percentage of Board investment.
6. Board sets minimum financial contribution of company owners.
7. Board sets the maximum initial draw amount.
8. Remainder of draw based on venture capital investments completed.
9. Board determines whether venture capital investments are limited to Montana.
10. Debenture term would be seven to ten years or as outlined below*.
11. Compound interest rates set based on risk and absence of equity upside.
12. Maximum aggregate amount for debenture investment is 1.0 percent of the Trust.

*The MSTTA debentures require total payment of principal and compound interest at the end of the 10-year term. Debt investments in venture capital companies structured in this way would require careful planning on the part of the companies to ensure that adequate liquidity is available at the end of the term to repay both principal and interest. This end-of-term payback structure would likely require the company to build up a large cash position towards the end of the debenture term. Another alternative would be to accept distributions at the same time and rate as the equity partners and apply the distribution

against principal. This approach may also reduce the risk as principal is paid down prior to the end of the term.

The Board chose to take no action on Venture Capital Investments from Permanent Coal Tax Trust Fund at this time.

Legislative Update

Executive Director Carroll South presented a verbal update on the current legislative session. Mr. South reported

Carroll, would you please assist me with this.

Out-of-State Travel

Executive Director Carroll South, presented travel recommendations for Paul Runnalls to attend the Standard & Poor's Banking Insurance Conference, March 18 - 20, 2001 in Las Vegas; Sandi Conrady to attend the Commercial Real Estate Financial Underwriting Course, March 11 - 14, 2001 in Fullerton, CA., Peter Blouke to attend the Council of Development Finance Agencies Educational Conference, March 20 - 25, 2001 in New Orleans, Jim Penner to attend the Public Funds Summit, March 10 - 14, 2001 in Phoenix, and Jim Penner to attend the "Building a Balance Scorecard" Conference, April 2 - 5, 2001 in Washington DC. Member Bardwell moved for approval of this recommendation; Member Ryan seconded the motion and the motion was passed 9-0.

BOND PROGRAM

Activity Report

The Board reviewed this report for the period ending February 16, 2001.

Staff Approved Loans Report

Borrower: Smith Valley Fire District (Kalispell)
Purpose: To finance a portion of the costs of purchasing a fire truck.
Staff Approval Date: January 24, 2001
Board Loan Amount: \$65,000
Term: 10 Years

Borrower: Badrock Rural Fire District (Columbia Falls)
Purpose: To finance the purchase of a fire truck.
Staff Approval Date: January 24, 2001
Board Loan Amount: \$50,000
Term: 5 Years

Borrower: Sheaver's Creek Water & Sewer District (Bigfork)
Purpose: To finance a preliminary engineering study.
Staff Approval Date: January 25, 2001
Board Loan Amount: \$12,500
Term: 3 Years

Borrower: York Fire Service Area (Helena)
Purpose: To finance the purchase of a water tender.
Staff Approval Date: January 26, 2001

Board Loan Amount: \$28,000
Term: 10 Years

Borrower: City of Three Forks
Purpose: To finance the purchase of a GMC truck to be used by the sewer dept.
Staff Approval Date: January 31, 2001
Board Loan Amount: \$20,000
Term: 5 Years

Borrower: Sweet Grass County
Purpose: To finance a fire truck.
Staff Approval Date: January 31, 2001
Board Loan Amount: \$130,262
Term: 10 Years

Borrower: Town of West Yellowstone
Purpose: To finance the purchase of a snow blower.
Staff Approval Date: February 7, 2001
Board Loan Amount: \$108,900
Term: 5 Years

INTERCAP

- Ms. Geri Burton presented staff's recommendation that the Board authorize staff to proceed with processing and closing the following loans using the Board's standard Bond Program Office procedures:

Miles City
\$258,987
5 Years

To finance costs associated with the construction of a 20" water main across the Tongue River and the extension of two water lines under the railroad tracks

Town of Opheim
\$288,000

In anticipation of Rural Development long term financing.

Water system improvements including construction and engineering of new municipal water wells and improvements to the distribution system.

City of Thompson Falls

\$610,400

In anticipation of Rural Development long term financing.

For water system improvements.

Member Fleming moved for approval of this recommendation; Member Wilson seconded the motion and the motion was passed 9-0.

United Materials of Great Falls Resolution #195

Mr. Peter Blouke, Deputy Director, presented Preliminary Inducement Resolution #195, giving preliminary approval

on the proposed issuance by the Board of Investments of Industrial Development Revenue Bonds in an approximate principal amount not to exceed \$3.5 million, the proceeds of which will be loaned to United Materials of Great Falls.

Based on preliminary review, Mr. Blouke presented staff recommendation that the Board adopt the Preliminary Inducement resolution to cover eligible economic development efforts by the United Materials of Great Falls, inc., under the terms and conditions of the Economic Development Bond Act of 1983.

After much discussion by the Board, Member Fleming moved to table the decision until staff could obtain further information. This motion died due to lack of a second.

Member Fleming motioned to adopt the Preliminary Inducement Resolution and staff recommendation. This motion died due to lack of a second.

Member Fleming motioned to **not** adopt the Preliminary Inducement Resolution or the staff recommendation; Member Klawon seconded the motion and the motion passed 7-1. Member Fleming voted "Nay" and Member Long abstained. This decision reflected a policy decision by the Board to not participate in Industrial Development Bonds until the Board has adopted a set of policy guidelines.

CHIEF INVESTMENT OFFICER REPORTS

Chief Investment Officer, James Penner, recapped the preceding reports and presentations.

Asset Allocation Report

Mr. Jim Penner, Chief Investment Officer, presented staff recommendation for the following Asset Allocation for April 1, 2001:

- \$15 million to the Domestic Equity Indexing Pool;
- \$4 million to Domestic Equity Indexing Pool for the State Fund
- \$2.5 million to each of the two external Asian Pacific managers, SG PAM and Schrodgers
- \$5 million to the external European manager, Pyrford International
- If the REIT Proposal is accepted, staff is asking for authority to increase the equity index allocation from \$15 to \$25 million, only for the month of April.

Member Long motioned for approval of staff recommendation; Member Wilson seconded the motion and the motion was passed 8-1.

REIT Proposal

Mr. Jim Penner presented staff recommendation that the Real Estate Investment Trust (REIT) Pool be liquidated on a best efforts basis during the current fiscal year ending June 30, 2001. The proposed exit will benefit future pension fund investment performance by freeing dollars for investment in equity investments with higher returns and increasing the Research Manager's time to enhance investment research for the \$2.5 billion Montcomp portfolio.

Member Wilson moved for approval of this recommendation; Member Klawon seconded the motion and the motion was passed 9-0.

Quarterly Investment Performance Report

Mr. Penner presented the MTCP, International-Asia, International-Europe, Total International Equities, Real Estate Trusts Portfolio, RFBP, TFBP, STIP, PERS, State Fund Performance and Returns by Asset Type quarterly report through the December 31, 2000.

PRESENTATION

Mr. Bruce L. Campbell and Mr. Tony Cousins gave the Board the annual Pyrford performance review.

ADJOURNED

The meeting adjourned for the day at 5:30 p.m.

CALL TO ORDER

The meeting was reconvened Friday, March 2, 2001 at 8:30 a.m. Eight members of the Board were present.

LOAN PROGRAMS

Consideration of Commercial Loan Participation Permanent Coal Trust Fund

Mr. Herb Kulow presented staff's recommendation to participate in the following loan request:

Borrower:	Curtis Jacobson and Lanni Jacobson
Lender:	Mountain West Bank, Missoula
Purpose of Loan:	To refinance a construction loan and provide long term financing for a commercial building.
Amount of Loan:	\$400,000
Board Loan Amount:	\$320,000
Board Participation:	80%
Term of Loan:	10 Years
Interest Rate:	7.80% + .25% LSF = 8.05%

Member Wilson arrived during Mr. Kulow's presentation. Member Bardwell moved for approval of this recommendation; Member Fleming seconded the motion and the motion was passed 9-0.

Borrower:	DSD Properties, LLC.
Lender:	Mountain West Bank, Great Falls
Purpose of Loan:	Purchase of a building.
Amount of Loan:	\$664,000
Board Loan Amount:	\$498,000
Board Participation:	75%
Term of Loan:	20 Years
Interest Rate:	7.50% + 1.00% LSF = 8.50%

Member Wilson moved for approval of this recommendation; Member Long seconded the motion and the motion was passed 9-0.

Borrower:	KML Company, LLC.
Lender:	Glacier Bank, Whitefish
Purpose of Loan:	To provide permanent financing for the purchase of investment real estate.
Amount of Loan:	\$2,250,000
Board Loan Amount:	\$1,800,000
Board Participation:	80%
Term of Loan:	25 Years
Interest Rate:	7.65% + .75% = 8.40%

Board directed staff to require certification by the Montana Department of Environmental Quality showing that the site conforms to all laws and standards of the Montana Environmental Protection Act or a report acceptable to the BOI from an environmental firm, that certifies that subject site conforms to all laws and standards of the Montana Environmental Protection Act. This will be added to the Schedule A Loan Requirements.

Member Ryan moved for approval of this recommendation; Member Wilson seconded the motion and the motion was passed 8-0. Member Beams abstained from the vote.

Borrower:	Kathryn L. Ogren
Lender:	First Security Bank, Missoula
Purpose of Loan:	To refinance an existing loan of \$820,000 and pay off an escrow in the amount of \$280,000.
Amount of Loan:	\$1,100,000
Board Loan Amount:	\$880,000
Board Participation:	80%
Term of Loan:	15 Years
Interest Rate:	To be determined

Member Bardwell moved for approval of this recommendation; Member Ryan seconded the motion and the motion was passed 8-0. Member Beams abstained from the vote.

Staff Approved Value Added Loan

Borrower:	Sonju Body Shop, Inc.
Lender:	First Interstate Bank, Kalispell
Staff Approval Date	December 27, 2000
Board Loan Amount:	\$348,405

Coal Tax Loan Activity

Mr. Herb Kulow presented and the Board reviewed this report for December and January.

Staff Approved Loans Committed

The Board reviewed this report for December and January.

Mortgage Program Activity Review

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The Board reviewed this report for December and January.

In addition, Mr. Kulow presented the Commercial Loan Delinquency Report and the Residential Loan Delinquency Report, dated December 31, 2000.

INVESTMENT ACTIVITY

Montcomp

-
Mr. Rande Muffick presented December and January transactions, the holdings report as of January 31, 2001 and the current investment strategy. Member Fleming moved for approval of the Montcomp strategy as presented; Member Wilson seconded the motion and the motion was passed 9-0.

In addition, Mr. Muffick presented Aflac, Ambac Financial Group, Bank of New York, MGIC Investment, Applied

Materials, and Scientific-Atlanta as Portfolio Additions.

International Investment

- Mr. David Ewer presented December and January transactions, the holdings report as of January 31, 2001 and the current investment strategy. Member Fleming moved for approval of the International Investment strategy as presented; Member Beams seconded the motion and the motion was passed 9-0.

Private Equities

- Mr. Jim Penner presented December and January transactions. In addition, Mr. Kelly presented the Venture Capital Update and the Leveraged Buyout Update.

Montana Real Estate Portfolio (MTRP)

- Mr. Jim Penner presented December and January transactions and the holdings report as of January 31, 2001. There was no investment strategy presented due to the Board's unanimous decision to accept the recommendation of staff to liquidate the Real Estate Investment Trust portfolio.

Fixed Income

- Mr. Robert Bugni presented December and January transactions, and the current investment strategy. Member Bardwell moved for approval of the Fixed Income strategy as presented; Member Wilson seconded the motion and the motion was passed 9-0.

In addition, Mr. Bugni presented the Non-Investment Grade Holdings Report.

Security Lending

Mr. Richard Cooley presented this report for December and January.

Treasurer's and STIP Funds

Mr. Cooley also presented December and January STIP transactions the STIP holdings report as of January 31, 2001, the December and January Treasurer's Fund transactions, the Treasurer's Fund holdings report as of January 31, 2001 and the current investment strategy for both of these funds. Member Ryan moved for approval of the STIP Fund and Treasurer's Fund strategy as presented; Member Long seconded the motion and the motion was passed 9-0. Member Wilson left the meeting at this time.

BOND PROGRAM continued

Northern Express Transportation Authority Shelby

Mr. David Ewer presented staff recommendation that the Board authorize an increase of up to \$1.5 million to the original loan request of \$1.5 million, for a total loan amount of up to \$3 million.

At its September 2000 meeting, the Board approved a loan in the amount of \$1.5 million for a term of 15 years to the Northern Express Transportation Authority, a port authority in Shelby, for a rail infrastructure project. The loan would be in the form of a limited obligation bond of the Authority and funds from the Trust Fund Bond Pool would be used to make the loan.

Member Ryan moved for approval of staff recommendation; Member Long seconded the motion and the motion was passed 8-0.

ADMINISTRATIVE BUSINESS continued

Chairman Anderson accepted nominations from the Board for the position of Vice-Chairman. Member Bardwell nominated Member Ryan as Vice Chairman; Member Long seconded and the vote was 8-0. Member Wilson was not present for the vote.

In addition, Member Bardwell will succeed Member Price on the Personnel Committee and will also be in charge of Board education and travel.

Next Meeting

The next regularly scheduled meeting of the Board will be April 12 & 13, 2001.

ADJOURNMENT

There being no further business, the meeting was adjourned at 10:50 a.m.

BOARD OF INVESTMENTS

APPROVE: _____
Dick Anderson, Chairman

ATTEST: _____
Carroll South, Executive Director

DATE: