

DEALER CONFERENCE CALL NOVEMBER 30

Morgan Stanley

_____ And of course Bob and I are here.

_____ OK

_____ Bob, we've assembled, you know, everybody that you've asked me to

Citron Oh, all right fine. And here besides myself is Matt Raabe, the Chief Assistant County Treasurer and Bob Austin of the County Counsel's Office, and John Abbott of the County Counsel's Office, Chuck Hulse the Chief Deputy County Auditor-Controller, who is sitting in for Steve Lewis the Auditor-Controller who is on vacation, Jean Costanza of the Los Angeles firm of Leboeuf, Lamb, Green and McGrave, and Judy Jacobson the County Treasurer's Investment Officers. Yes.

Costanza This is Jean Costanza, and we noted that the conference call was being recorded, and with your permission we would like to do the same thing.

_____ Not sure. New York would you have somebody respond to that.

New York That's fine.

Costanza Thank you. It's a legal requirement in California. We can't record a conference call or any other conversation without asking permission and letting you know, so that's why I wanted to clarify that at first.

Citron A few weeks ago, we identified a concern in the operation of the County Treasury. The main concern was liquidity, cash flow. One of the larger parts of that concern was that when we roll over reverse repos with you and others, because of rising interest rates, the dollar value of the securities that we reverse keeps coming down, so we borrow less money, and have to keep putting up additional funds to pay off the old reverse and start the new one. Because of this problem in the County Treasury, we formed a team of myself, Matt Raabe, the County Counsel's Office, and Ernie Schneider, who is the County's Administrative Officer, and certainly Steve Lewis of the Auditor-Controller's Office. We then

went to the firm of LeBoeuf, Lamb and Green, who Jean Costanza is the principle of and asked for their assistance because Ms. Costanza over the years has been the bond counsel to the County in the issuances of many County debt positions, so therefore, she was very knowledgeable of County finances and workings, and certainly operation of the County Treasury. They, in turn, hired a company in New York called Capital Market Risk Advisors, who is non-market participant, and has a excellent reputation in analyzing portfolios of various types and recommendations for their restructuring if needed. I will now give it over to Matt, who will explain to you some of the answers that Capital Market Risk Advisors have come up with, and what they are going to be doing ongoing.

Raabe

What I would like to do is start out just with a brief overview of what the County's investment strategy has been for the last 15 years, and how that strategy puts us where we happen to be today. Certainly, as you know, we've been engaging in reverse repurchase agreements for many, many years now, and we have always believed in holding a base portfolio of treasuries and agencies, and we still have that as our general portfolio; that the vast, vast majority of the portfolio is in agency securities, home loan banks, Fanny Maes, Salley Maes, so forth, and we have a portfolio with about 7 1/2 billion dollars in participant deposits. Through reverse repos, that position is leveraged to a total asset under management of 20 billion dollars, meaning that we have about 14 billion dollars in reverse repos. Additionally, within the last few years as interest rates declined, we began to take substantial positions in structured notes, and about a third of total asset base, or just under a third of our total asset base is in some form of structured securities. What we have always done in the past to safeguard the portfolio is to maintain about ten percent of the participant deposits in the form of overnight repurchase agreements and short-term cash, and that has always allowed us to cover changes in interest rates; to pay down reverses if we felt we need to do that; to fund any withdrawals that came through the pool; and recover our ordinary expenses. As interest rates have jumped up, at least in our cases, it was much swifter and certainly more unexpected that we had anticipated would happen with rates. The market value of the securities were holding, in particular, the structured notes has been falling, and as you know there's not very much of a market for structured notes at all right now. What that's meant to us is that we have been able to _____ significantly less money that we had been able to borrow in the past, so we made the decision to use our existing liquidity to cover the amounts that we

were no longer able to borrow. What that has left us with is a short term to intermediate term liquidity problem. We engaged CMRA to look at the portfolio and they have preliminarily come back with four findings for us, and I say preliminarily because they expect to have a more complete findings for us very early next week, but the four findings right now is that the pool does, in fact, have a liquidity problem; that it needs to retain its existing liquidity; and obtain additional liquidity in order to be a going concern. Number 2, that further market losses in the pool are probable until interest rates stabilize. Number 3, that if all of the depositing participants in the investment pool remain in the investment pool, it is quite possible that the market value losses will not become realized losses. As you may not know, 40 percent of the deposits in the Orange County pool are by voluntary participants who have made the discretionary choice to put their money in the pool. Sixty percent of the money is in the pool on a mandatory basis; that would include the County, entities controlled by the County Board of Supervisors, and the 37 educational districts in Orange County. The last thing they told us is that the investment pool is at this point in time extremely dependent on the reverse repurchase program in order to continue going forward. The market losses do not allow us to extricate ourselves from those positions. There is at this point in time, an estimated \$1.5 billion.

New York

Excuse me one second, there was some noise on the line when you went through the four points. Could you just repeat that one more time.

Raabe

Sure, that the existing reverse repurchase program that we're engaged we will need to continue with for the next 2-3 years in order to extricate ourselves from this situation. It would not be advisable for us to try to stop that program at this point. We do know that we have an estimated 1.5 billion dollar market value loss in the portfolio today. That would represent approximately a 7 percent decline in the market value of the total assets under management, but when applied against the depositor base, would translate to roughly a 20 percent market value loss against deposits. Naturally, that concerns us. We have put the management team together, and we are trying to do some of the following things in response to that. Number 1, we are looking at methods of retaining the existing liquidity and obtaining additional liquidity. Obviously retaining the current liquidity involves meeting with the participants in the investment pool. We yesterday met with the 11 largest investors in the pool. Together with the County and the schools, who are the mandatory participants, those 11 major participants constitute 91 percent of

the investment pool, so certainly they are our first target audience. We explained the liquidity situation to them, and we asked for their cooperation and their commitment to stay in the investment pool. We informed them that if they chose not to stay in the investment pool, we would have to liquidate their investments at market value instead of at cost. As far as obtaining additional liquidity, we are looking at a number of options which would include selling some of the existing securities in the portfolio, obtaining lines of credit from some of the major banks that the County does business with, obtaining forms of liquidity from the investment brokers that we are doing business with, and any other idea that gets presented to us. The second thing that we are looking at is how to react to the market value decline, and what one of the options we are looking is buying hedges into the portfolio so that should interest rates continue to rise we can limit the market value losses to where they are today. We are looking at what the cost of that would be and trying to evaluate as to what the likelihood is that interest rates are going to increase substantially further, and weigh those costs against the benefits. We are also looking at whether we should restructure the portfolio, whether we should buy swaps, whether we should trade some of the securities that we currently have for other securities and amortize the loss over a period of time. As I said, we did meet with our largest participants. Tomorrow we will be meeting with the rest of the participants in the pool in explaining the situation to them, and again reminding them that currently what we have is a cash flow problem. We do not have losses. We have not taken losses, and it is our anticipation with everyone's cooperation, we may not have to take any losses. We have spoken this morning with Merrill Lynch and First Boston and asked for their cooperation. After our phone call with you we intend to talk to several other firms who we do business with and solicit their cooperation and assistance. On the investment side we are taking any new monies that come in, and we are investing them in overnight to 30-day securities so that we can maintain as much liquidity as possible. Next week, some of our management team will be going to New York, and we are going to have meetings with Standard and _____ and with Moody's. We have already given them a preliminary update as to what we view the situation being, and that our belief that it is a workable situation. We intend to go back and spend some time with them and go through the portfolio and explain completely how we intend to move forward and ask for any help they can give us.

Citron

We believe there are two linchpins to the solving _____ of this problem. The first is the understanding and participation of all of our investors in the pool. In our meeting yesterday afternoon

with 11 of our largest investors, which include the Orange County Transportation Authority, which is an amalgamation of managing public transit throughout Orange County, and also the administration of funds for the building of roads and the widening of freeways. The Transportation Corridor Agency, which is an agency that is building the tollroad here in Orange County, and we have two pools. We have the largest is the commingle pool, and then we have a municipal bond pool in which because of arbitrage reasons interest rates are restrictive, and TCA is in that pool. The Irvine Ranch Water District; the cities of Anaheim, Irvine, Santa Ana, and Huntington Beach; the Moulton Niguel Water District; the Orange County Employees Retirement System; and the Orange County Sanitation District; and the Orange County Water District; which have been with us for over 25 years. In the case of the Orange County Transportation Authority, they are the largest single investor in the pool, with approximately one billion dollars. The Director of the Agency, Mr. _____, and the Chief Financial Mr. Keenan, were present yesterday, and they indicated that we have their complete cooperation in this matter, and, in fact, today or tomorrow, they will be sending out a press release to all the participants in the pool, as well as Standard and Poor, telling them of their positive response to this problem and their cooperation in solving it. I also had after the meeting preliminary information. These people have to go back to their management of course, but I believe we will have complete cooperation from the cities of Anaheim, Irvine, and Santa Ana, as well as the other districts that I have just mentioned. As indicated by Matt, tomorrow we will be meeting with the school districts, which are mandatory participants in the pool, as well as a few of the smaller cities, which are discretionary, and some smaller special district, which are either in some cases mandatory and other cases are not, and I believe with certainty that when we present what we did yesterday to them, that I am assured that we will have very complete cooperation as well. Therefore, the other linchpin to solving this problem is the cooperation and assistance from the dealer community. Certainly, the rolling over of our financing of our reverse repurchase program. And with that, I will hand it over to Jean Costanza that has a few comments to make.

Costanza

I'd just like to spend a couple of minutes in talking a little bit about the consultants Capital Market Risk Advisors. I don't know if you know them. The principles we are dealing with are Tanya _____ and Leslie _____. They are as Bob pointed out earlier, not market participants, so that we are confident that the advice we will be getting from them won't be tainted with any conflict. They have a lot of detailed information about the securities in the

County pool. As Matt said, they have given us preliminary findings. However, they are now in the process of finalizing their findings. What they are doing actually, is working on a model, and the model will provide us information that will tell us how each of the securities will act under various interest rate scenarios, and it will tell us liquidity issues as well. They have confirmed both in the preliminary discussions, and I expect that we will hear again to reiterate what both Matt and Bob had said, that the critical features of ongoing liability with respect to the pool involved the participants, the depositors, and the broker dealers and your cooperation in that regard is something we are seeking to get, and that is the purpose of this phone call, as well as to of course give you a heads up as to the preliminary findings. As time goes on, we can offer to your additional conversations or conversations with the consultants, and is a matter of fact, in talking with both Merrill and First Boston as a group, you want to have a meeting we would be happy to arrange that once the final information is finalized. I think that the key for us next week after we're dealing with the depositors, as well as all of the broker dealers will be the rating agency conversations, and to that's our next step in going forward, and again, once we get the information from Capital Market we expect to share that with you. We'd like your input. They'll also be providing us with various recommendation in terms of strategy in how to handle the liquidity problems and market value deterioration in the pool.

New York _____, New York. Question. You have not made any _____ decisions, is that what I take from your last comment? _____ still evaluating what strategic steps you may take?

Costanza I think that that's correct.

New York Additional equi_____ or sales of cor_____ portfolio or sales of structured _____ portfolio. You have not yet made any strategic decisions as to how exactly you are going to proceed.

_____ No, we haven't done that, and actually before we would implement anything, we would really appreciate any guidance you would have. We would like to run any recommendations by you to see what your thoughts would be on the matter. We believe that this would be a cooperative venture, and that we would need your technical assistance, as well as any financial assistance in going forward.

_____ Well, I see the work you're doing in terms of _____ portfolios is important. We don't have all that information because we don't have your portfolio. I mean we could certainly offer our own opinion a scenario analysis of the portfolio. _____ that's obviously key equation in terms of being able to quantify what the potential exposure as you stated in your analysis we're obviously in a sharply rising interest rate environment, and its not clear when its going to stop, so in order to ascertain what risk is still in the portfolio, you need to have a picture of that.

New York Correct, and we probably, this is M _____, we probably want at some point to talk to these consultants to understand the assumptions that they're building in when they say the model's going illustrate the performance of the future interest rate scenarios, we want to at least understand how they are analyzing that and what assumptions they're using in there, a whole lot of different variables.

Costanza That should be fine. We again would be happy to have your input into that and we would anticipate that after the meeting with the rating agencies at some point thereafter, we can again either do it by conference call or we can do it by a meeting, and we'll just have to keep that open and be a little bit flexible. I would like to just pint out that in a way there have been two strategic decisions with respect to the pool. The first is to take the new money coming in and invest that in overnight and short-term securities, and the second is alerting the pool participants that any redemptions that they have for the voluntary participants would be at market value, so those are two of what I would call strategic decisions, not certainly with respect to the purchase of sale of securities in the pool itself, however. There was one other point that I failed to mention and would just like to tell you about right now. We anticipate on Thursday afternoon on issuing a press release, and we'd like to, we'd be happy to actually send you a copy of it on just prior to release so that you'll be aware of what it will say.

New York The sorts of things that we'd want to look when, again we can only analyze the bonds that we know over the ones that we sold, but we want to look at pool analysis, but we may also want to look at some bond by bond analysis, because it may that there are different decisions you're going to make for different securities within the portfolio as to what specific ones are more _____.

Raabe We'd be happy today to send you a copy of the portfolio as we know it, and then we would be happy next week to give you a copy

of the breakdown of the portfolio as the consultants have it, and theirs will certainly be in significantly greater detail. Our breakdown is really from an accounting standpoint. They have collected every term sheet on every security, and have modeled it, and so certainly what they will be able to provide us for you next week will be much more useful than what we can provide today, but we are very happy to provide you whatever we have. Where would you like me to send it.

New York I have a secure fax machine _____. You can send it to area code 212-296-5256.

Raabe Ok, you'll have that within an hour.

New York Ok.

Raabe And who should I address that to.

New York To Ken deRegc

Raabe And your title.

deRegc I'm Managing Director of Morgan Stanley.

Raabe Thank you.

deRegc I think that would be helpful, and we'll have to. I guess we'll start from that point.

Raabe Ok, we will definitely send that out.

New York What is your timeframe in terms of analysis versus when you want to start deciding what other strategic tactics need to implemented?

_____ Well, we certainly expect to have all of the analysis by next week. We would like to have input from you folks on that as to what timing should be. Certainly, if we're talking about buying hedges, then we would presume the sooner the better. Some of the other strategies that may be recommended to us may be on a more of a layer-in basis. And certainly if we're going to sell securities we wouldn't be wanting to dump a lot of securities out on the market right now.

New York And in terms of the short-term rolling of the repurchase program, how did you plan to proceed as far as securities to _____ and _____.

Well, we believe initially that we have enough liquidity to get us through the month of December on the rolling of those as long as all of you continue to finance the positions you have committed to finance in the past, and perhaps we may even have to ask for some additional financing, but we do not believe at this point that there is a problem in December. It, the problem time may come later, and of course, you know that's based on some assumptions going into the portfolio. One of the main ones being that _____ are not going to be changing the haircuts.

New York OK, it wouldn't be our intention to change the haircut. Obviously it would be normal to remark the securities to market.

We certainly understand that. That would always be the case.

New York Would always be the case as normal, exactly, as normal. OK, well I think that gives us something to start with. J _____ you want _____.

New York _____ mentioned the press release, and you offered to show us a copy in advance I appreciate that. What do you expect to say in the press release_____.

Raabe Generally, what we're going to say is that we have experienced a market value decline in the portfolio; that in response to that market value decline we have met with the participants in the investment pool and the brokers with whom we do business; and that we look forward to cooperating with all parties on resolution of the problem. It will not be very detailed.

New York The other questions I had was in your conversations with the participants, how much are you sharing with them in terms of your discussions with dealers like us.

Raabe As to what we're going to tell the dealers or the information we imparted during this discussion.

New York _____.

Raabe We gave them all of the information that we have given you, and we did tell them that we would be speaking to the dealers to obtain their cooperation. Obviously, you folks are much more sophisticated in the investment business than most of the people who invest in our pool. While we told them we had cash flow difficulties, we told them that it was relayed to the reverse repurchase program, and so forth, obviously the nuances of

structured securities are not something we can converse with them on.

Costanza

We're basically taking the position again of giving them information that they ask for. We will likely be meeting with them and the participants later on in December, to have them. I'm sorry, the consultants, to have the consultants available to answer any questions that they have.

New York

Just one other questions. If we start to get our creative juices going here to think about combinations of _____ expect _____, help solve the problem, you mentioned before potential strategies that include hedges. Does that mean that we can look at things like that and not have to worry about the ability of the pool of the County _____ just flops an outright hedging as opposed to just buying securities; that they can do all that kind of stuff.

Austin

We'd have to look at the nature of the hedge. There is some authority for the County entering into hedges. We'd have to look at that. I can't really answer that question at the moment, but we'll take a look at that.

deRegc

This is Ken deRegc. Just in _____. In response to the cooperation comment. Our attention given the information you've given us would be that we would be willing to roll _____ position. I don't see any issue _____. We need more information really to make any decision beyond that present right now.

Thank you.

_____ This kind of information is really helpful, and what it helps you to do is avoid the _____ reaction when something hits the news we're going to say oops, we got to _____ media _____.

That's right.

New York

_____ going forward, we don't really have enough _____ to make an evaluation of what's going on, and a deficit problem, you know, how the agencies are going to react. We tend not to commit to repo financing as a long-term decision, but right now with what you told us, everything seems pretty reasonable.

Thank you. I believe that with certainty that we have our hands around the problem, and that it is really a cash flow problem, and not a market risk problem, and that with the cooperation of the entities that have invested in our portfolio which I believe with certainty that we have, and the cooperation of the dealer community, this problem will be resolved to everybody's satisfaction, and I repeat again, I appreciate your understanding and cooperation, and your ongoing advice, and I believe if handled correctly here in the next few days that it will not be a media situation.

Costanza

Do you have any other questions?

New York

_____ offer, obviously offer assistance. I _____ respond by saying there obviously is an ongoing risk question here, and we'll try to look at this portfolio and offer whatever assistance we can, and if you _____ something more specifically that you'd like us to do accepting the risk, because there is an ongoing risk issue here.

Costanza

Ok, and obviously we get the more detailed analysis we will be able to talk more concretely about those things.

New York

Right.

Costanza

Ok.

New York

Thank you.

Costanza

Thanks.

Thank you.

New York

Thank you.

Goodby.