

Merrill Lynch

April 1, 1993

Mr. Robert L. Citron
Orange County Treasurer
630 N. Broadway, Room 209
Santa Ana, CA 92702

Dear Bob:

The following are a few "Bullet Points" you may wish to include in your next report to the Board of Supervisors:

The investment results of Fiscal Year 92/93 reflect a multifaceted strategy geared to the rate environment. The strategy includes the utilization of leverage. We implement this leverage by using the investment technique of reverse repos, as well as the purchase of structured securities. This enables the portfolio to approximate a leverage figure of 2 to 1.

We plan on streamlining this strategy of leverage by increasing our investment in fixed rate instruments, thus lowering our overall leverage. Without altering our strategy, if rates were to continue to lay low or trend lower, our performance could be expected to continue. If rates were to rise, it is reasonable to expect that the overall performance of the portfolio will decline. Accordingly, we may consider strategies to lessen this leverage ratio and diversify our interest risk, given the possibility of such a rise. It is also part of our investment strategy to hold the securities we buy to their maturity, as appears prudent, therefore, assuring principal repayment and protecting against market volatility.

However, if a sudden high interest rate environment were to return, there could be an erosion of principal. It is for this reason we are working toward decreasing our leverage ratio.

We are, of course, consistently monitoring these factors that might cause a sudden and extended rise in interest rates in order to protect our principal. To this end, we want to preserve the option of reducing the size of our portfolio to take into consideration possible future changes in rates.

Sincerely,

Michael G. Stamenson
Director
Municipality Unit

MGS:mk