



**April 28, 2011**

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**City of Surprise**  
**Investment Guidelines and Objectives**  
**Month Ended March 31, 2011**

**Investment Objectives:** In accordance with the City's Investment Policy, the City's primary objectives in order of priority are:

- A. Safety** – Investments shall be undertaken in a manner that seeks to ensure the preservation of capital in the overall portfolio. The objective will be to prudently mitigate credit risk and interest rate risk. It is understood by the City that no investment is completely free of risk.
- B. Liquidity** – The investment portfolio shall remain sufficiently liquid to meet anticipated cash flow requirements. This is to be accomplished by structuring the portfolio so that securities mature concurrent with anticipated cash flow needs (static liquidity). Furthermore, because all possible cash demands cannot be anticipated, the portfolio should consist of securities for which there are active secondary markets (dynamic liquidity).
- C. Optimal Yield** – Return on investment is of lesser importance compared to the safety and liquidity objectives described above. The investment portfolio shall be designed to optimize the yield the City obtains from the portfolio taking into account the criteria of the investment policy, the dynamic liquidity needs of the City, and the current interest rate outlook/economic condition.

**Investment Guidelines:** In relation to the investment portfolio, the City's investment strategy focuses on the following:

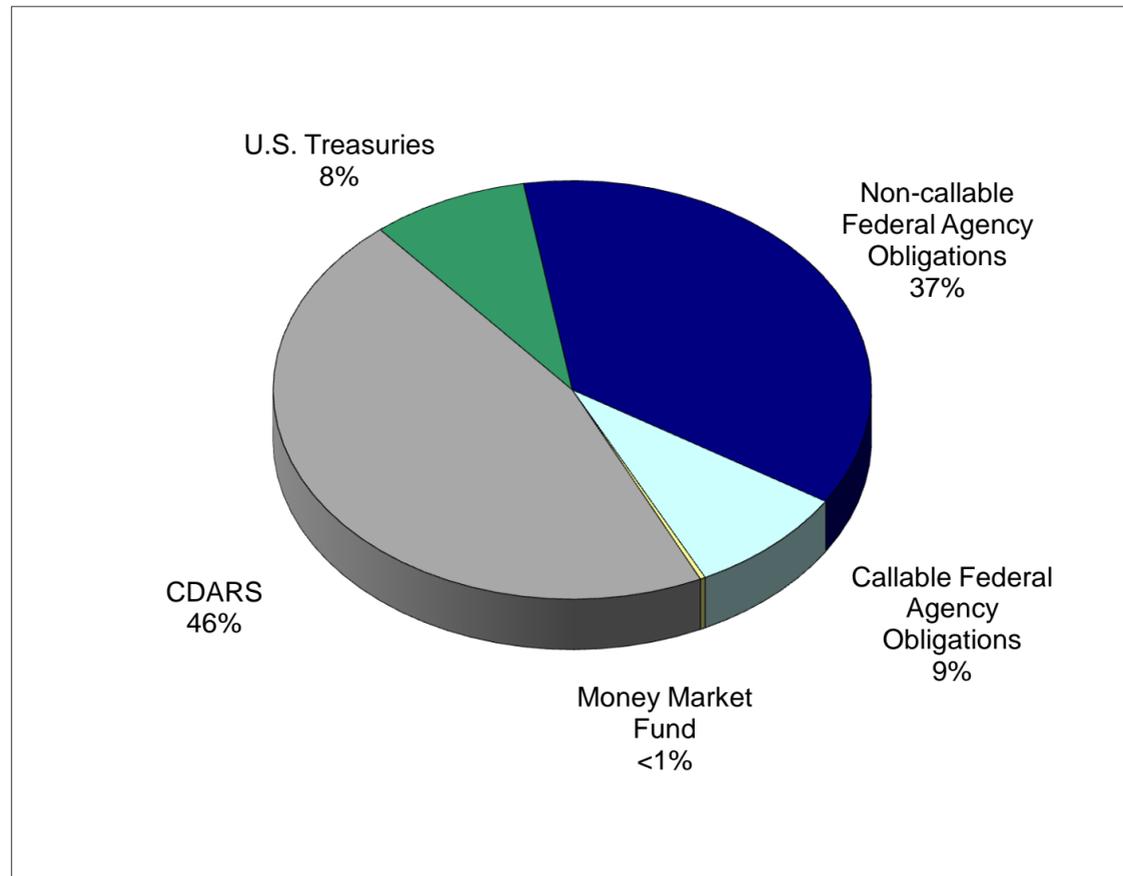
- **Permitted Investments.** The City will invest in permitted securities consistent with A.R.S.§35-323. Additionally, the City may desire to be more conservative in its investment portfolio and restrict or prohibit certain of the investments outlined in the Investment Policy.
- **Transactions prior to maturity** – Securities shall generally be held to maturity with the following exceptions:
  - A security with a declining credit may be sold early to minimize loss of principal.
  - Liquidity needs of the portfolio require that the security be sold.
  - Securities may be sold to better position the portfolio in accordance with better market opportunities. The City will approve all of these transactions but only after PFM Asset Management LLC, the City's investment advisor, provides detailed information about the transaction, including the qualitative and quantitative impacts on the portfolio, and will be cognizant of trades that will result in large material realized losses.

## City of Surprise Portfolio Summary and Characteristics

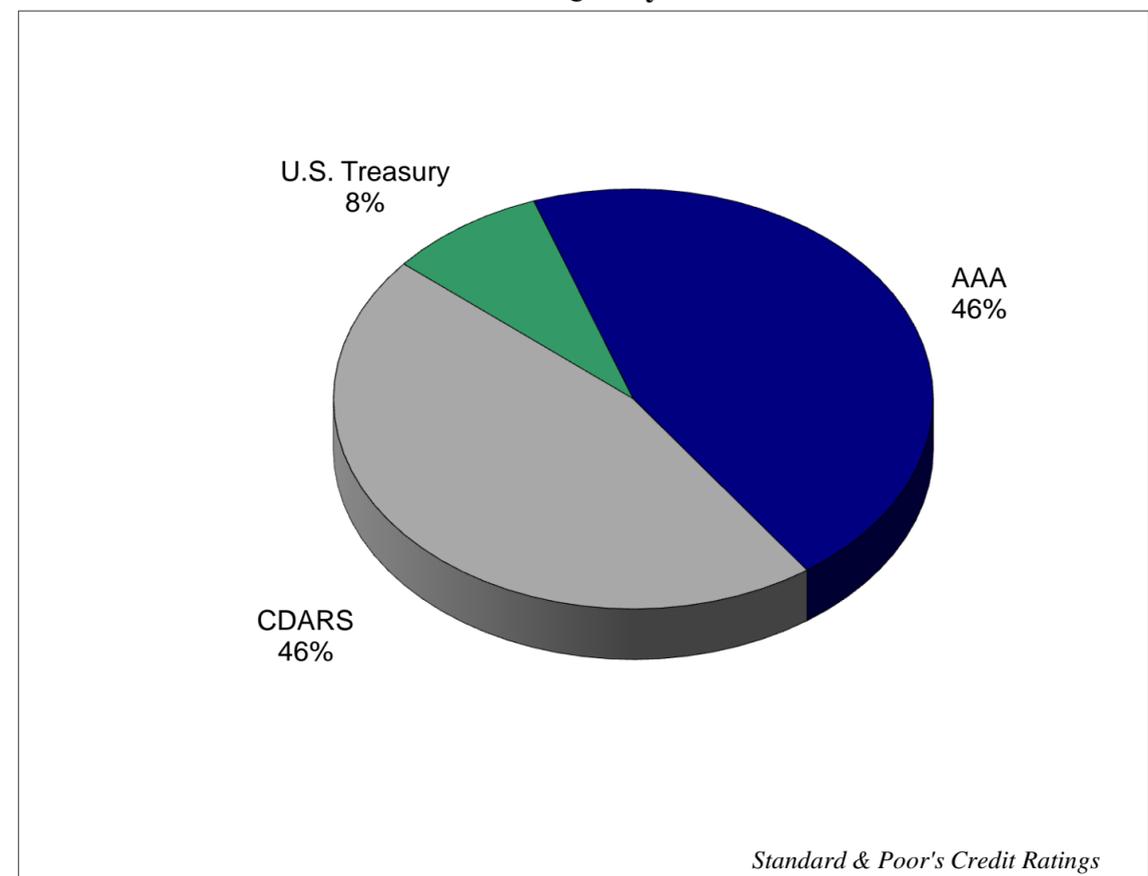
Month Ended March 31, 2011

<u>Security Type</u>	<u>Current Holdings*</u>	<u>Current Month % of Portfolio</u>	<u>Previous Month % of Portfolio</u>
<b>U.S. Treasury</b>	<b>\$5,549,858.59</b>	<b>8%</b>	9%
<b>Federal Agency</b>	<b>\$29,579,329.26</b>	<b>46%</b>	45%
Callable Federal Agency	\$5,702,287.75	9%	9%
Non-callable Federal Agency	\$23,877,041.51	37%	36%
<b>CDARS</b>	<b>\$30,000,000.00</b>	<b>46%</b>	46%
<b>Wells Fargo MMF</b>	<b>\$182,694.69</b>	<b>&lt;1%</b>	<b>&lt;1%</b>
<b>Total Market Value</b>	<b>\$65,311,882.54</b>	<b>100%</b>	<b>100%</b>

**Sector Distribution**



**Credit Quality Distribution**



The City's portfolio complies with the investment policy and the Arizona Revised Statutes

\*Security market values excluding accrued interest as of settlement date. Note that PFM monthly statements reflect holdings as of trade date.

**City of Surprise Maturity Summary and Key Portfolio Statistics**  
**Month Ended March 31, 2011**

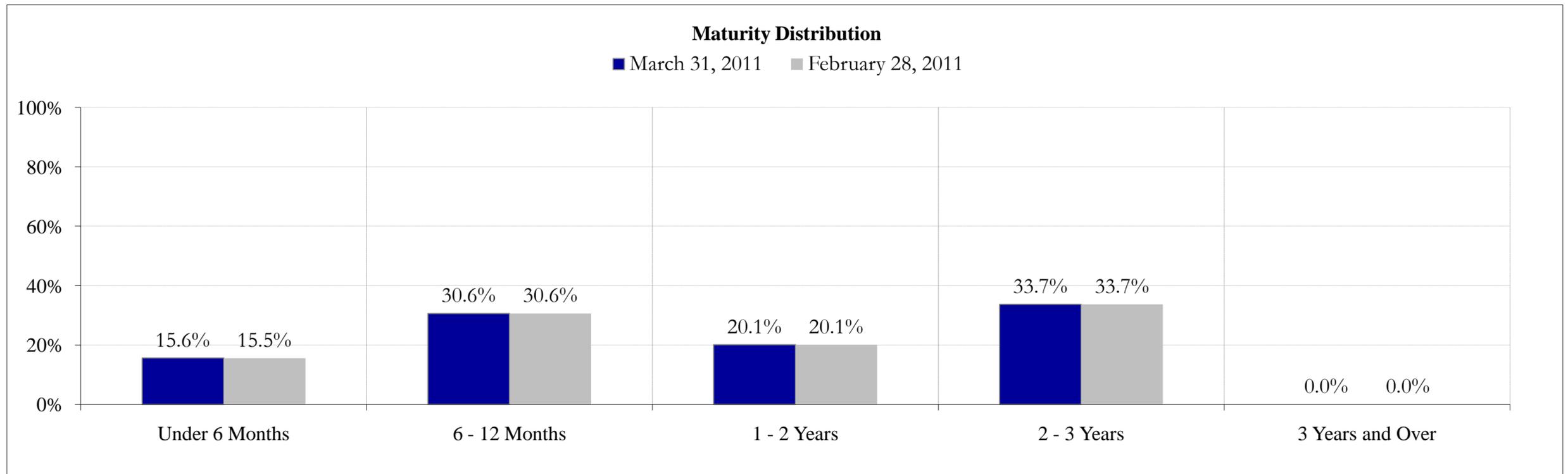
<b>Maturity Distribution Summary</b>		
<u>Maturity Class</u>	<u>Fair Value*</u>	<u>% of Portfolio</u>
<b>Under 6 Months</b>	<b>\$10,182,694.69</b>	<b>15.6%</b>
<b>6 - 12 Months</b>	<b>\$20,000,000.00</b>	<b>30.6%</b>
<b>1 - 2 Years</b>	<b>\$13,139,310.88</b>	<b>20.1%</b>
<b>2 - 3 Years</b>	<b>\$21,989,876.97</b>	<b>33.7%</b>
<b>3 Years and Over</b>	<b>\$0.00</b>	<b>0.0%</b>
<b>Total Market Value</b>	<b>\$65,311,882.54</b>	<b>100%</b>

\*Security market values excluding accrued interest as of settlement date. Note that PFM monthly statements reflect holdings as of trade date.

<b>Key Portfolio Statistics</b>	
<b>Effective Duration<sup>1</sup></b>	<b>1.66 years</b>
<b>Benchmark Duration<sup>2</sup></b>	<b>1.78 years</b>
<b>Yield at Cost</b>	<b>0.81%</b>

1. Duration to worst as of 03/31/2011 was 2.01
2. The City's benchmark is the Merrill Lynch 1-3 year U.S. Treasury Index Performance statistics exclude money market fund and CDARS investments

Please note that the percentages on this page are rounded and may not add up to 100% due to the rounding.



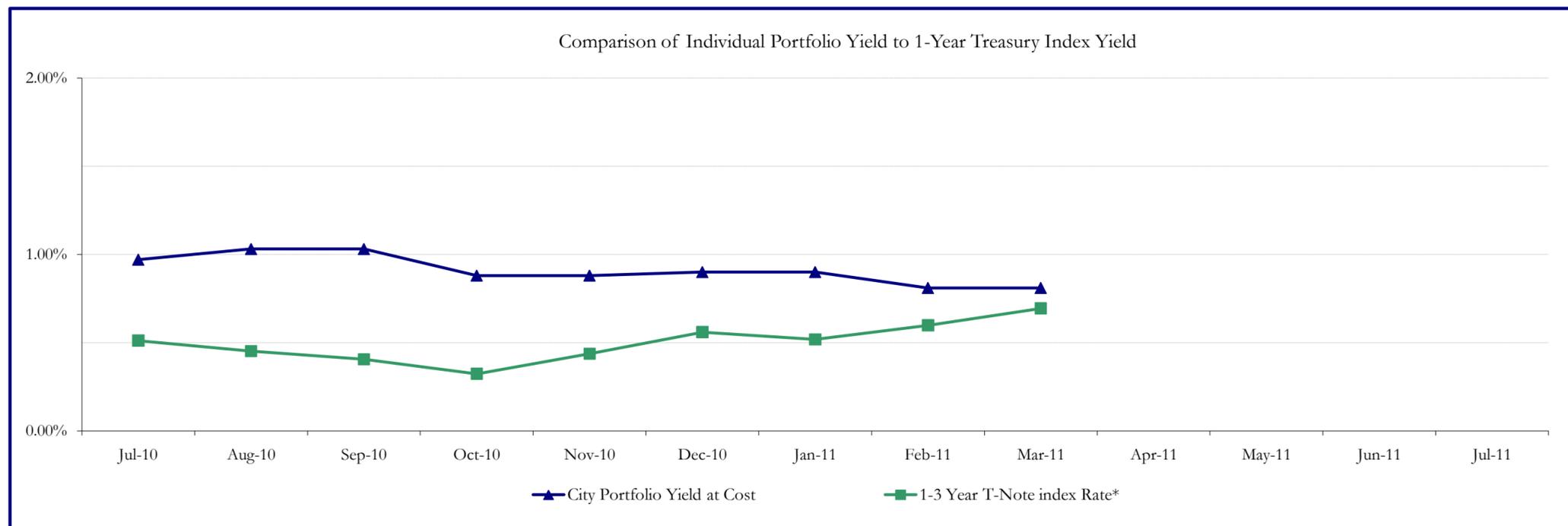
**City of Surprise Individual Portfolio Yield Summary  
Fiscal Year 2010-2011**

Date	Month-End Market Value <sup>1</sup>	Duration <sup>2</sup>	Portfolio YTM at Cost <sup>2</sup>	1-3 Year T-Note Index Rate <sup>3</sup>
Jul-10	\$15,279,792	1.75	0.97%	0.51%
Aug-10	\$20,296,127	1.37	1.03%	0.45%
Sep-10	\$20,306,987	1.29	1.03%	0.41%
Oct-10	\$34,159,429	1.72	0.88%	0.32%
Nov-10	\$35,295,699	1.82	0.88%	0.44%
Dec-10	\$35,315,499	1.73	0.90%	0.56%
Jan-11	\$35,342,530	1.50	0.90%	0.52%
Feb-11	\$35,312,485	1.75	0.81%	0.60%
Mar-11	\$35,311,883	1.66	0.81%	0.69%

<sup>1</sup> Excludes accrued interest and CDARS. Includes balance in the custody account MMF

<sup>2</sup> Excludes CDARS and custoday account MMF

<sup>3</sup> Rate represents the Merrill Lynch 1-3 Year U.S. Treasury Note Index month-end yield. Source Bloomberg

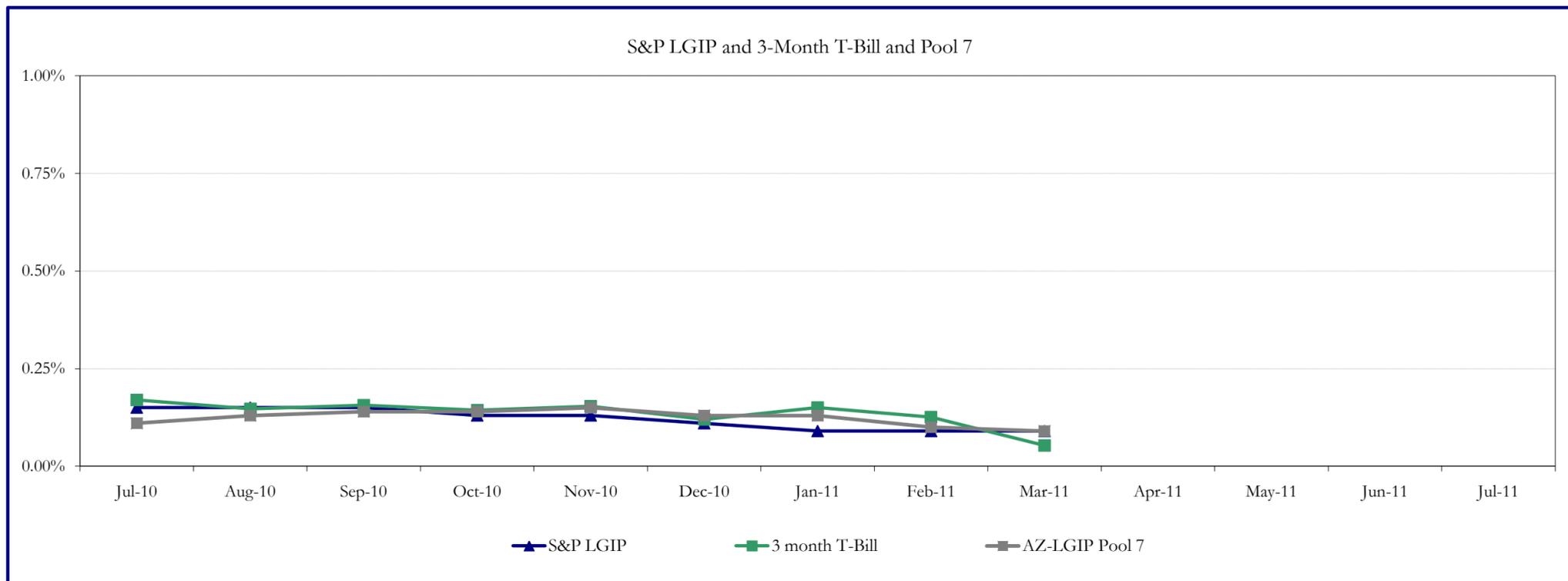


**City of Surprise Short-Term Benchmark Comparisons  
Fiscal Year 2010-2011**

Date	S&P LGIP	AZ-LGIP Pool 7 <sup>1</sup>	3 month Treasury Bill <sup>2</sup>
Jul-10	0.15%	0.11%	0.17%
Aug-10	0.15%	0.13%	0.15%
Sep-10	0.15%	0.14%	0.16%
Oct-10	0.13%	0.14%	0.14%
Nov-10	0.13%	0.14%	0.14%
Dec-10	0.11%	0.13%	0.12%
Jan-11	0.09%	0.13%	0.15%
Feb-11	0.09%	0.10%	0.13%
Mar-11	0.09%	0.09%	0.05%

<sup>1</sup> Monthly Apportionment Yields. Source: Office of the Arizona State Treasurer

<sup>2</sup> Rate represents the Merrill Lynch 3-Month U.S. Treasury Bill Index month-end yield (G001). Source: Bloomberg



**City of Surprise Holdings**  
**Month Ended March 31, 2011**

**Operating Funds Investment Inventory by Maturity Date**

<b>Issuer</b>	<b>Maturity</b>	<b>Years to Maturity</b>	<b>Fair Value</b>	<b>Yield to Maturity</b>	<b>Next Call Date</b>	<b>Frequency</b>
Wells Fargo MMF	3/31/2011	0.00	\$182,695	0.01%		
Alliance Bank	6/30/2011	0.25	\$10,000,000	0.55%		
Alliance Bank	9/29/2011	0.50	\$15,000,000	1.01%		
Alliance Bank	12/29/2011	0.75	\$5,000,000	0.88%		
U.S. Treasury	6/30/2012	1.25	\$2,506,450	0.52%		
FNMA	10/30/2012	1.58	\$2,493,035	0.77%		
FHLMC	11/30/2012	1.67	\$2,983,824	0.66%		
FHLMC	12/21/2012	1.73	\$2,115,070	1.09%		
FNMA	2/26/2013	1.91	\$3,040,932	0.83%		
FHLMC	4/15/2013	2.04	\$1,233,568	0.56%		
FNMA	6/26/2013	2.24	\$2,022,558	1.41%		
FNMA	7/19/2013	2.30	\$2,001,324	1.39%	7/19/11	One-time
FFCB	9/16/2013	2.46	\$5,009,925	0.43%		
FNMA	9/23/2013	2.48	\$4,978,130	0.73%		
FHLMC	11/15/2013	2.63	\$1,233,924	1.01%	5/15/11	Quarterly
U.S. Treasury	11/15/2013	2.63	\$3,043,409	0.81%		
FNMA	11/26/2013	2.66	\$2,467,040	0.98%	5/23/11	Quarterly
<b>Total Market Value</b>			<b>\$ 65,311,883</b>			

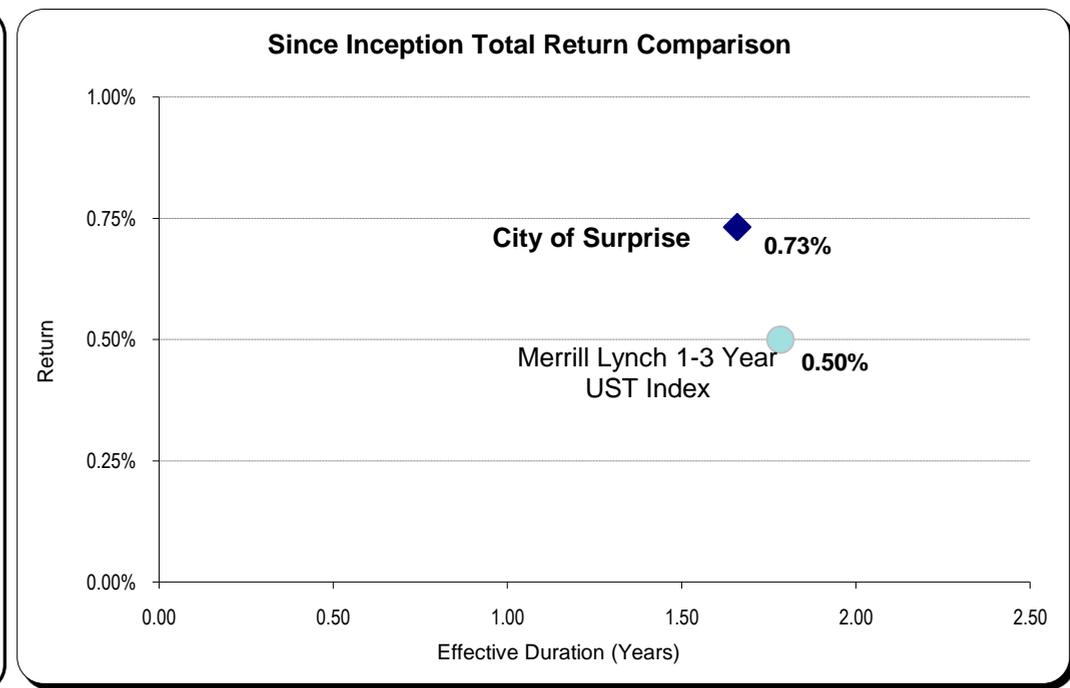
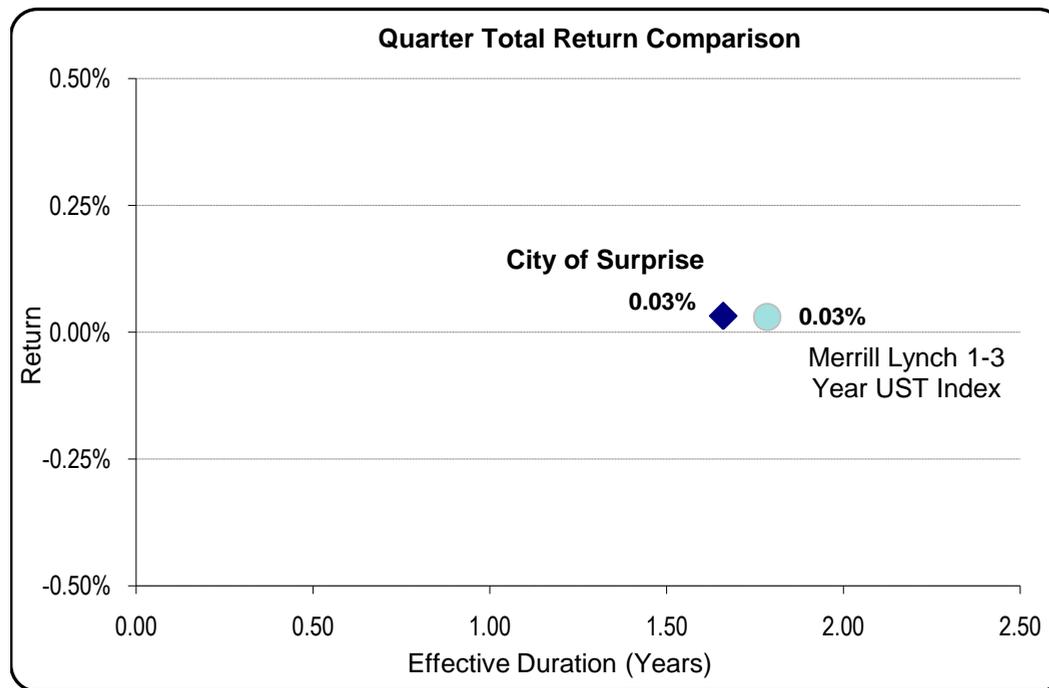
## City of Surprise Quarterly Performance Month Ended March 31, 2011

### Portfolio Performance

<b>Total Return</b> <sup>1,2,3,5</sup>	Quarter Ended March 31, 2011	Past 6 Months	Since Inception		
<b>City of Surprise</b>	<b>0.03%</b>	<b>0.01%</b>	<b>0.73%</b>		
Merrill Lynch 1-3 Year UST Index	0.03%	-0.12%	0.50%		

<b>Effective Duration</b> <sup>4</sup>	March 31, 2011	December 31, 2010	<b>Yields</b>	March 31, 2011	December 31, 2010
<b>City of Surprise</b>	<b>1.66</b>	<b>1.73</b>	Yield at Market	<b>0.88%</b>	0.88%
Merrill Lynch 1-3 Year UST Index	1.78	1.77	Yield on Cost	<b>0.81%</b>	0.90%



**Notes:**

1. Performance on trade date basis, gross (i.e., before fees), in accordance with the CFA Institute's Global Investment Performance Standards (GIPS).
2. Quarterly returns are presented on an unannualized basis. Performance numbers for periods greater than one year are presented on an annualized basis.
3. Merrill Lynch Indices provided by Bloomberg Financial Markets.
4. Excludes money market fund in duration and performance computations.
5. Inception date is June 16, 2010.



## Managed Account Detail of Securities Held

For the Month Ending **March 31, 2011**

### CITY OF SURPRISE OPERATING FUND

Security Type/Description Dated Date/Coupon/Maturity	CUSIP	Par	S&P Rating	Moody's Rating	Trade Date	Settle Date	Original Cost	YTM at Cost	Accrued Interest	Amortized Cost	Market Value
<b>U.S. Treasury Bond / Note</b>											
US TREASURY NOTES DTD 06/30/2010 0.625% 06/30/2012	912828NS5	2,500,000.00	TSY	TSY	02/16/11	02/16/11	2,503,710.94	0.52	3,927.83	2,503,383.05	2,506,450.00
US TREASURY NOTES DTD 11/15/2010 0.500% 11/15/2013	912828PU8	3,090,000.00	TSY	TSY	12/01/10	12/02/10	3,062,117.58	0.81	5,847.10	3,065,216.81	3,043,408.59
<b>Security Type Sub-Total</b>		<b>5,590,000.00</b>					<b>5,565,828.52</b>	<b>0.68</b>	<b>9,774.93</b>	<b>5,568,599.86</b>	<b>5,549,858.59</b>
<b>Federal Agency Bond / Note</b>											
FANNIE MAE GLOBAL NOTES DTD 10/08/2010 0.500% 10/30/2012	31398A4T6	2,500,000.00	AAA	Aaa	02/16/11	02/16/11	2,488,575.00	0.77	5,243.06	2,489,409.08	2,493,035.00
FHLMC NOTES DTD 10/22/2010 0.375% 11/30/2012	3137EACP2	3,000,000.00	AAA	Aaa	12/01/10	12/02/10	2,982,900.00	0.66	4,968.75	2,985,722.07	2,983,824.00
FHLMC GLOBAL REFERENCE NOTES DTD 12/17/2007 4.125% 12/21/2012	3137EABE8	2,000,000.00	AAA	Aaa	06/23/10	06/24/10	2,148,600.00	1.09	22,916.67	2,103,122.94	2,115,070.00
FNMA NOTES DTD 01/18/2011 0.750% 02/26/2013	3135G0AK9	3,045,000.00	AAA	Aaa	02/02/11	02/03/11	3,039,747.38	0.83	2,220.31	3,040,152.60	3,040,931.88
FHLMC GLOBAL NOTES DTD 03/04/2010 1.625% 04/15/2013	3137EACJ6	1,215,000.00	AAA	Aaa	10/28/10	11/01/10	1,246,602.15	0.56	9,104.06	1,241,270.40	1,233,567.63
FNMA GLOBAL NOTES DTD 05/21/2010 1.500% 06/26/2013	31398AT44	2,000,000.00	AAA	Aaa	06/16/10	06/17/10	2,005,560.00	1.41	7,916.67	2,004,130.56	2,022,558.00
FANNIE MAE (CALLABLE) GLOBAL NOTES DTD 07/19/2010 1.375% 07/19/2013	31398AW32	2,000,000.00	AAA	Aaa	07/13/10	07/19/10	1,999,280.00	1.39	5,500.00	1,999,445.44	2,001,324.00
FFCB (FLOATING) NOTE DTD 09/16/2010 0.380% 09/16/2013	31331JG64	5,000,000.00	AAA	Aaa	10/12/10	10/13/10	5,000,000.00	0.43	877.78	5,000,000.00	5,009,925.00
FANNIE MAE GLOBAL NOTES DTD 08/06/2010 1.000% 09/23/2013	31398A2S0	5,000,000.00	AAA	Aaa	10/12/10	10/13/10	5,038,650.00	0.73	1,111.11	5,032,583.10	4,978,130.00
FREDDIE MAC GLOBAL NOTES (CALLABLE) DTD 11/15/2010 1.000% 11/15/2013	3134G1XN9	1,250,000.00	AAA	Aaa	10/28/10	11/15/10	1,249,625.00	1.01	4,722.22	1,249,671.63	1,233,923.75
FNMA NOTES (CALLABLE) DTD 11/26/2010 1.000% 11/26/2013	31398A5Y4	2,500,000.00	AAA	Aaa	11/05/10	11/26/10	2,501,562.50	0.98	8,680.56	2,500,459.05	2,467,040.00



### Managed Account Detail of Securities Held

For the Month Ending **March 31, 2011**

#### CITY OF SURPRISE OPERATING FUND

Security Type/Description Dated Date/Coupon/Maturity	CUSIP	Par	S&P Rating	Moody's Rating	Trade Date	Settle Date	Original Cost	YTM at Cost	Accrued Interest	Amortized Cost	Market Value
<b>Security Type Sub-Total</b>		<b>29,510,000.00</b>					<b>29,701,102.03</b>	<b>0.83</b>	<b>73,261.19</b>	<b>29,645,966.87</b>	<b>29,579,329.26</b>
<b>Managed Account Sub-Total</b>		<b>35,100,000.00</b>					<b>35,266,930.55</b>	<b>0.81</b>	<b>83,036.12</b>	<b>35,214,566.73</b>	<b>35,129,187.85</b>
<b>Securities Sub-Total</b>		<b>\$35,100,000.00</b>					<b>\$35,266,930.55</b>	<b>0.81%</b>	<b>\$83,036.12</b>	<b>\$35,214,566.73</b>	<b>\$35,129,187.85</b>
<b>Accrued Interest</b>											<b>\$83,036.12</b>
<b>Total Investments</b>											<b>\$35,212,223.97</b>

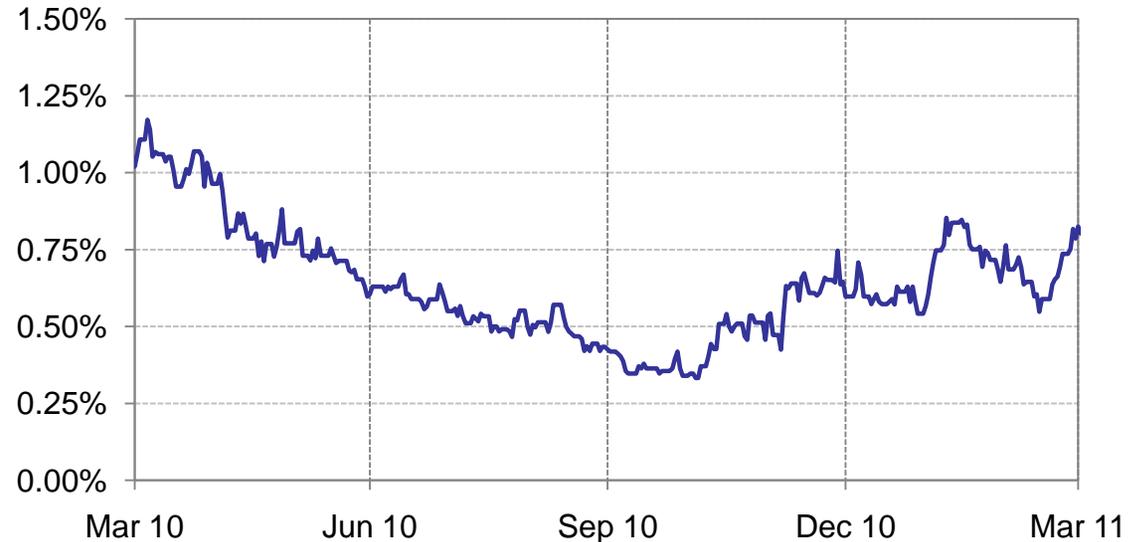
# Market Update

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# Yields Recently Rebounded, But Remain Low

- While yields were volatile during the quarter, they ended up modestly higher on positive economic data and inflation fears.

**2-Year U.S. Treasury Yields**  
March 1, 2010– March 31, 2011



- At the same time, yields on U.S. Treasuries remain well below their 10-year averages and near historical lows.

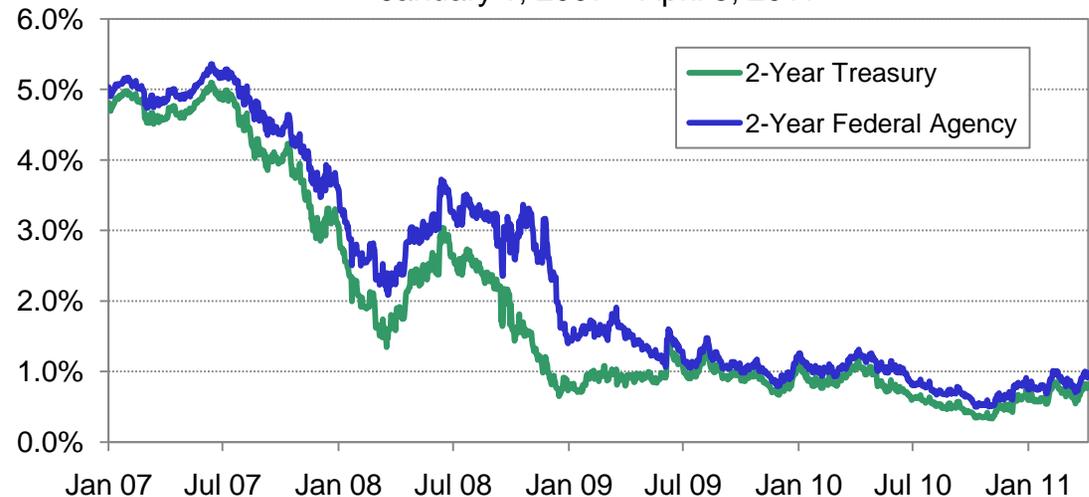
U.S. Treasury	January 31, 2011	March 31, 2011	10-year Average
1-year	0.25%	0.30%	2.32%
2-year	0.57%	0.80%	2.61%
5-year	1.94%	2.24%	3.41%
10-year	3.37%	3.47%	4.12%
30-year	4.57%	4.51%	4.74%

# Spreads Grew Tighter, and Yields More Volatile

- Yield spreads between Treasuries and Agencies have been narrow since 2009 and that trend has continued.

- At times in March, Treasuries yielded higher than similar maturity Agencies.

**2-Year U.S. Treasury Yields vs 2-Year Federal Agency Yields**  
January 1, 2007 – April 5, 2011

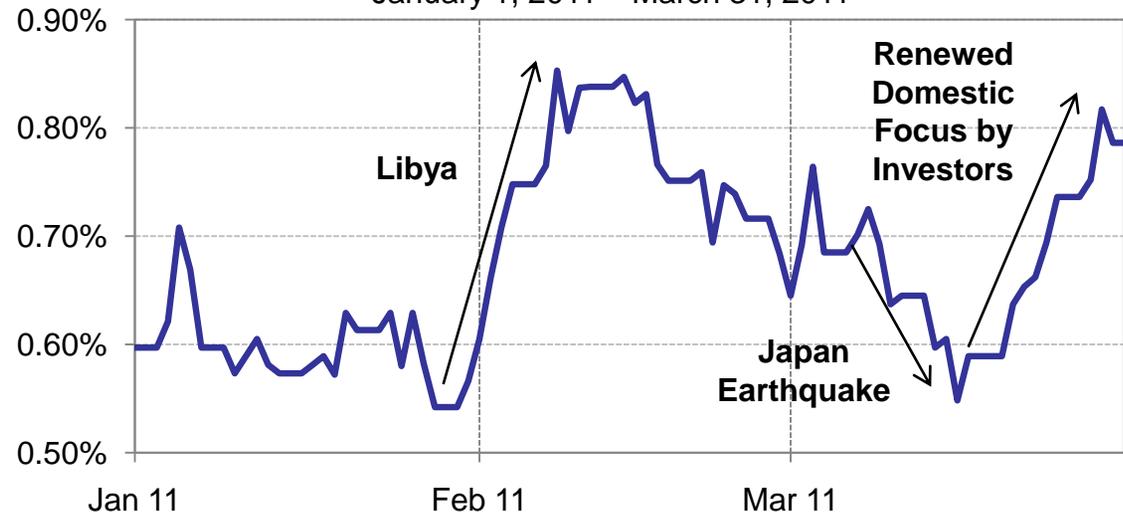


- Fixed-income volatility was a result of actions home and abroad:

- Abroad: unrest in the Middle East, natural disasters, and European sovereign debt concerns

- At home: Federal Reserve Governors publicly expressing opinions regarding the strength of the economic recovery

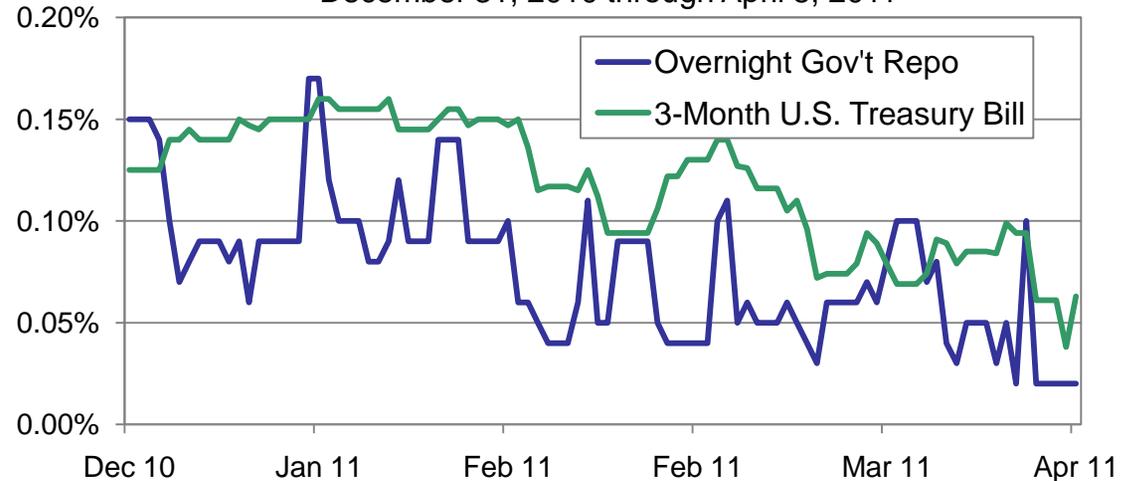
**2-Year U.S. Treasury Yields**  
January 1, 2011 – March 31, 2011



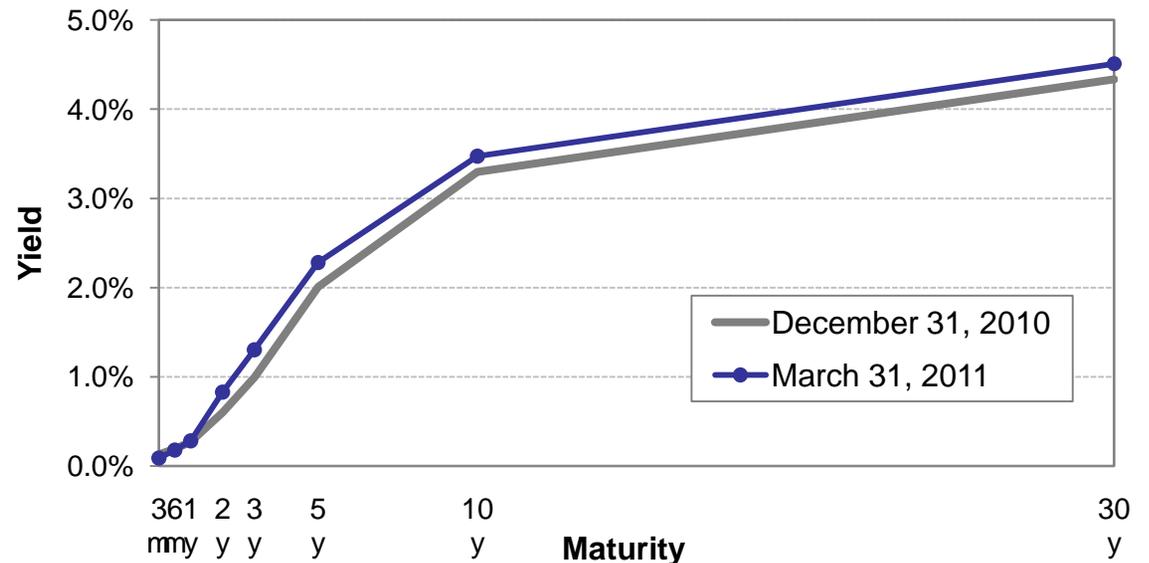
# Short-Term Yields Actually Declined, Causing Further Steepening in Yield Curve

- Overnight repo rates, along with very short Treasuries and Agencies, declined the past few weeks due to a combination of factors:
  - Available collateral shrunk sharply as dealers tightened their balance sheets over quarter end.
  - New FDIC fee imposed on banks essentially eliminates a previous arbitrage opportunity in the repo market, causing less banks to offer collateral in the repo market.
- The yield curve remains steep due to a combination of intermediate yields moving up and short term yields being held down by factors above as well as by the Fed's low target rate.

**3-Month U.S. Treasury Bill and Overnight Gov't Repo Yields**  
December 31, 2010 through April 5, 2011



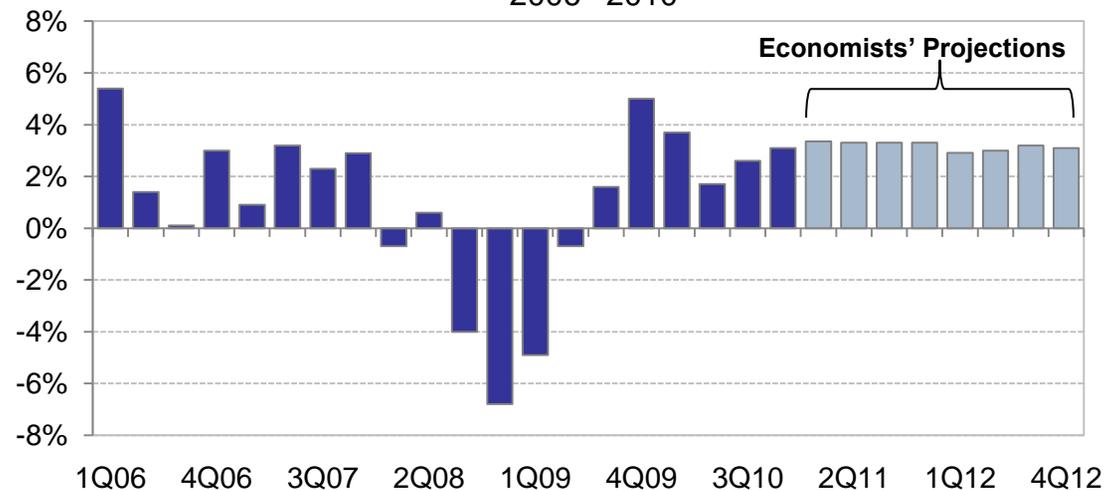
**U.S. Treasury Yield Curve**  
December 31, 2010 vs. March 31, 2011



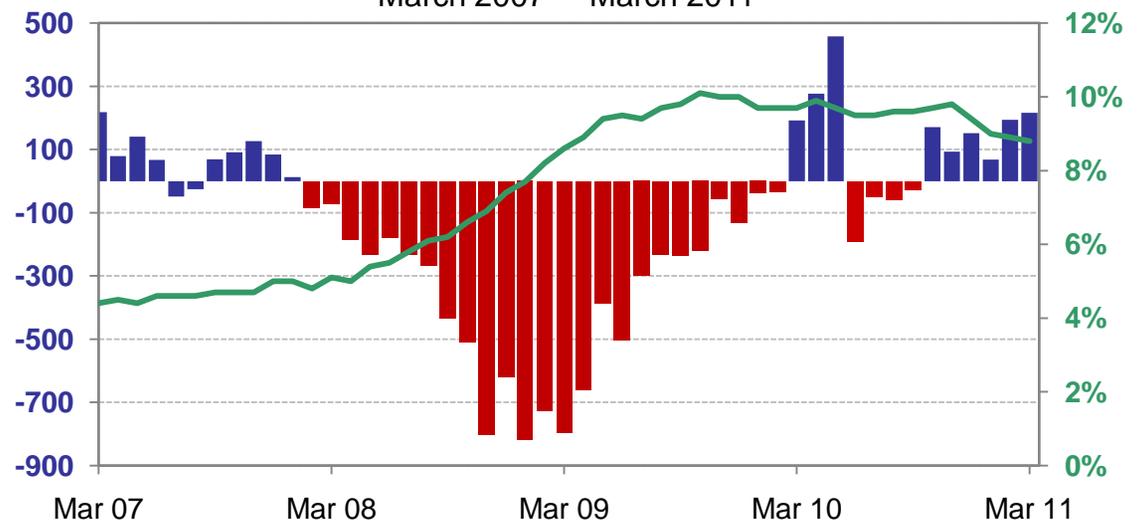
# Economic Data Continues To Reflect Slow Recovery

- The final GDP reading for 4Q10 was revised higher to 3.1%.
- Strong corporate profits, consumer spending, and exports drove growth, while reduced state and local government spending remained obstacles to recovery.
- Overall unemployment fell to 8.8% in March.
  - New jobs were created in the private sector, in factories, retail, health care, education, and professional services.
  - If job creation continues at its current pace, 2.5 million new jobs will be added by year end.

**Gross Domestic Product (GDP) Growth**  
2006 –2010

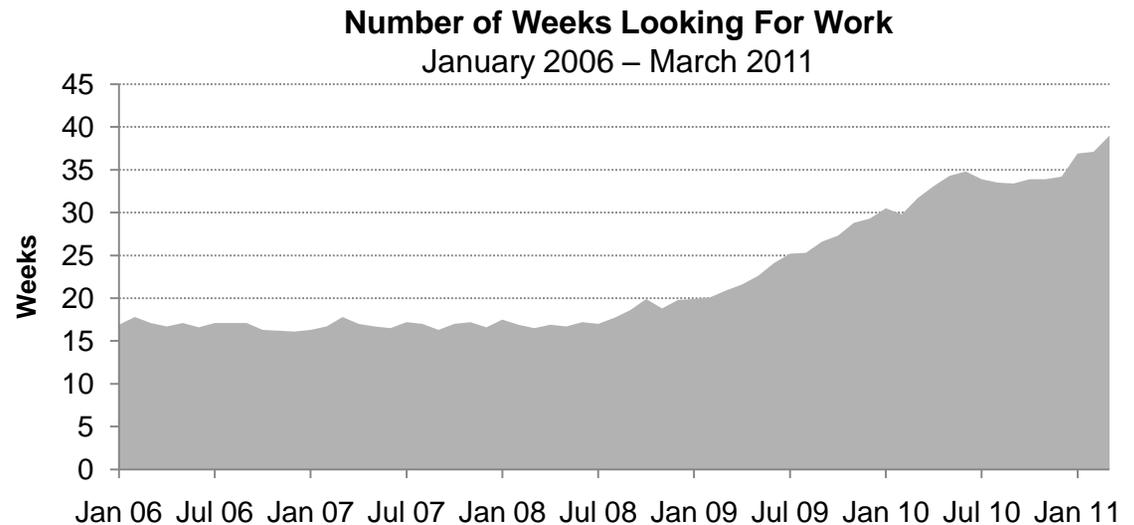


**Change in Non-Farm Payrolls/ Unemployment Rate**  
March 2007 – March 2011



# However, Unemployment Data Not As Positive as it May Seem

- The number of weeks those classified as unemployed have been looking for work continues to increase, with the latest reading at 39 weeks, or almost 10 months.



- Meanwhile, average hourly earnings for those working were flat in March for the fourth time in five months.
- After adjusting for inflation, real wages are actually falling. The consumer-price index was up 2.1% in February from a year earlier; average hourly earnings, as of March, were up just 1.7%.

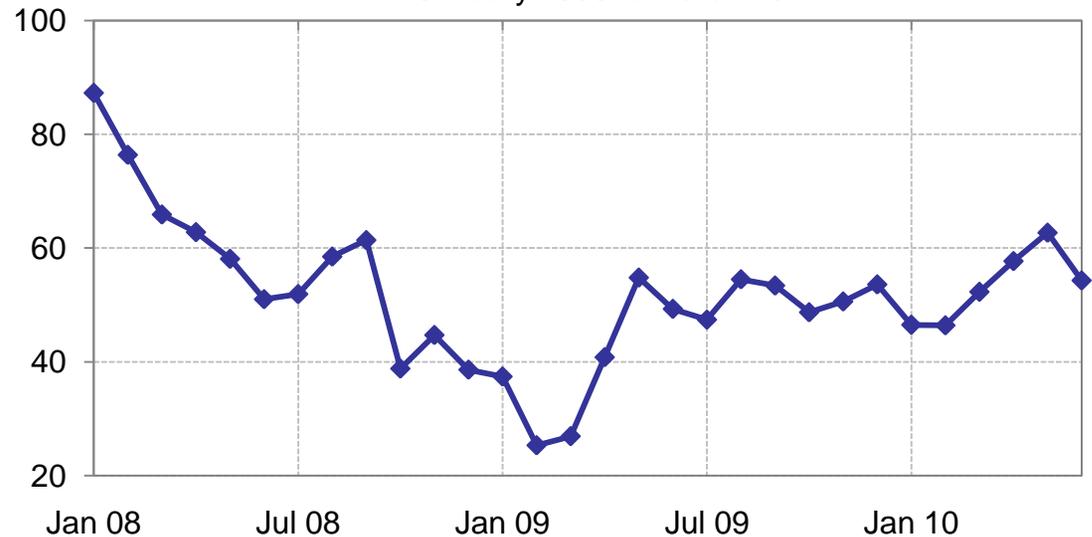


# In Addition, Consumers Have Lost Confidence

- Consumer confidence, which had increased in February, declined in March partly due to increasing gas prices and fears of inflation.

- Compared to last month, consumers have a more negative outlook on jobs, business conditions, and their personal incomes.

**Consumer Confidence**  
January 2008 to March 2011



	February Reading	March Reading	Change
Expect business conditions to improve in next 6 months	25.2%	20.6%	-4.6%
Anticipating business conditions to worsen	10.3%	16.2%	+5.9%
Expecting more jobs in the months ahead	21.2%	19.9%	-1.3%
Anticipating fewer jobs	15.0%	20.7%	+5.7%
Expect an increase in income	17.4%	15.3%	-2.1%

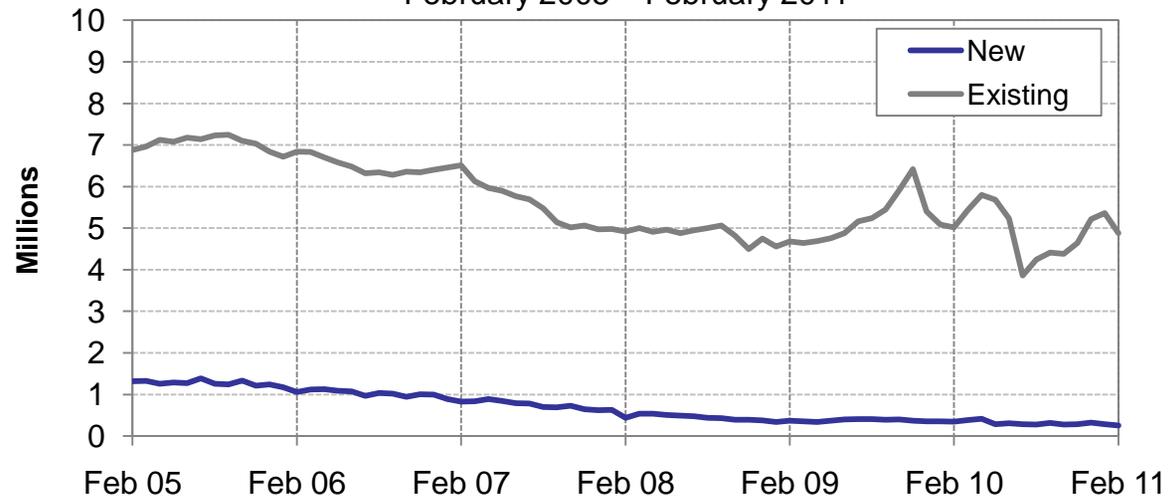
# Weak Housing in Region Remains a Headwind to Recovery

- New and existing home sales continue to decline.
- Eleven markets — including Phoenix— hit their lowest points since home values started dropping more than four years ago, pushing prices in those areas below the lows seen in most regions in spring 2009.
- Of the 20 composite areas, Phoenix had the largest decline year over year.

*\*The Case Shiller indices have a base value of 100 in January 2000. So a current index value of 150 translates to a 50% appreciation rate since January 2000 for a typical home located within the metro market.*

Sources: National Association of Realtors & Bloomberg/ S&P Case Shiller

**New and Existing Homes Sales**  
February 2005 – February 2011



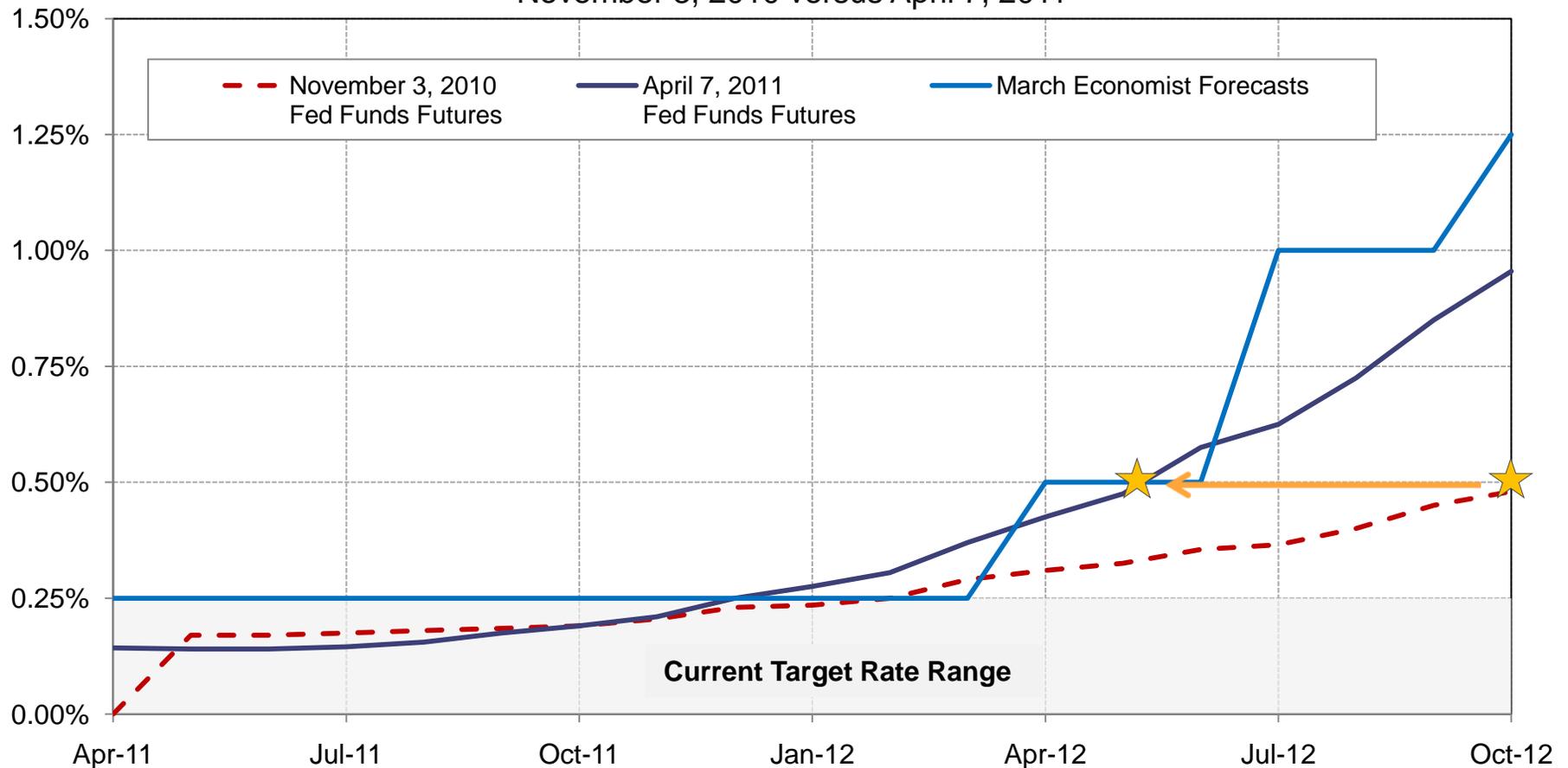
**S&P /Case Shiller Composite Home Price Index**

Metro Area	January 2011 Level*	Monthly Change	Annual Change
Phoenix	101.54	-1.5%	-9.1%
Detroit	66.02	-1.7%	-8.1%
Portland	135.80	-1.8%	-7.8%
Minneapolis	113.21	-3.4%	-7.6%
Chicago	115.78	-1.8%	-7.5%
Atlanta	99.59	-0.4%	-7.0%
Tampa	128.52	-1.0%	-7.0%
Seattle	135.41	-2.4%	-6.7%
Charlotte	111.50	-1.1%	-4.8%
Miami	141.30	-1.3%	-4.7%

# Fed Funds Target Rate Expectations

- The market currently expects the first Fed rate hike will occur in May 2012 – five months earlier than was forecast before the commencement of QE2 on November 3, 2010.

**Expectation for Fed Funds Target Rate**  
November 3, 2010 versus April 7, 2011



## Disclaimer

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