



June, 2011

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**City of Surprise**  
**Investment Guidelines and Objectives**  
**Month Ended May 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:

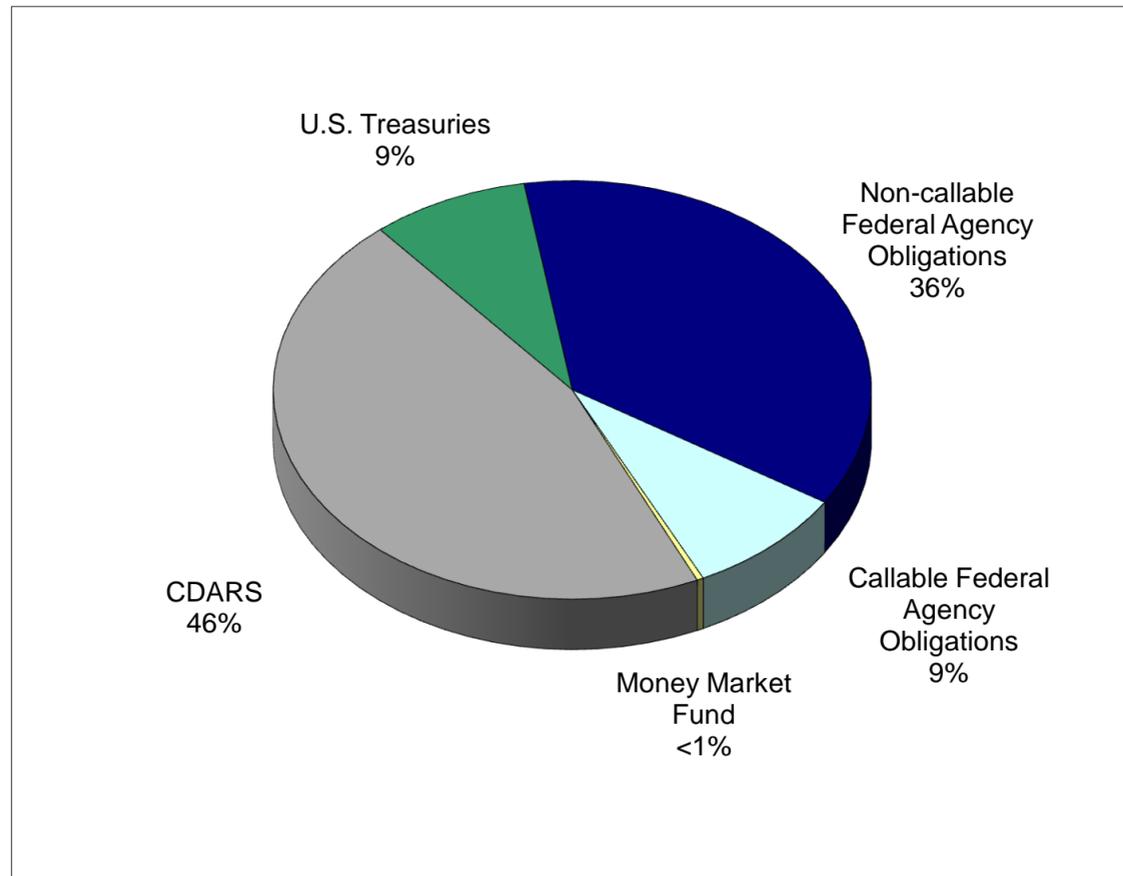
- **Permitted Investments.** The City will invest in permitted securities consistent with A.R.S.§35-323. Additionally, the City may desire to be more conservative in its investment portfolio and restrict or prohibit certain of the investments outlined in the Investment Policy.
- **Transactions prior 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

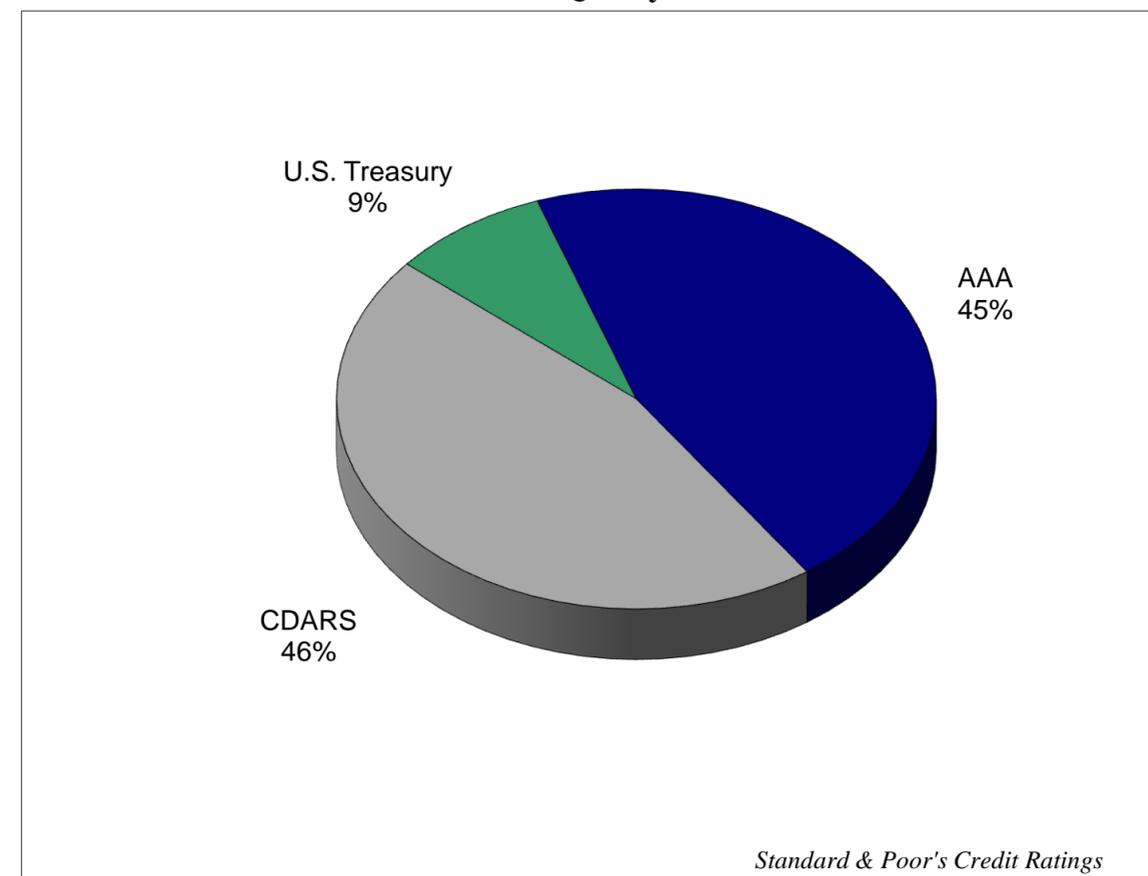
Month Ended May 31, 2011

<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>\$5,592,625.00</b>	<b>9%</b>	9%
<b>Federal Agency</b>	<b>\$29,755,510.85</b>	<b>45%</b>	45%
Callable Federal Agency	\$5,748,775.50	9%	9%
Non-callable Federal Agency	\$24,006,735.35	36%	36%
<b>CDARS</b>	<b>\$30,000,000.00</b>	<b>46%</b>	46%
<b>Wells Fargo MMF</b>	<b>\$232,107.00</b>	<b>&lt;1%</b>	<b>&lt;1%</b>
<b>Total Market Value</b>	<b>\$65,580,242.85</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 May 31, 2011**

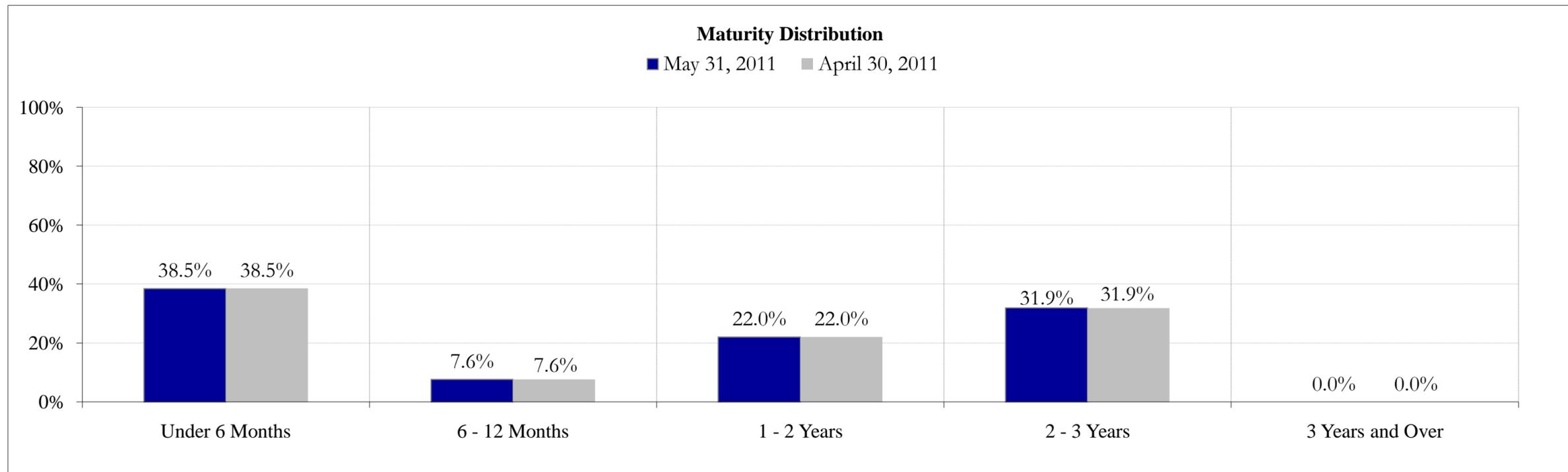
<b>Maturity Distribution Summary</b>		
<u>Maturity Class</u>	<u>Fair Value*</u>	<u>% of Portfolio</u>
<b>Under 6 Months</b>	<b>\$25,232,107.00</b>	<b>38%</b>
<b>6 - 12 Months</b>	<b>\$5,000,000.00</b>	<b>8%</b>
<b>1 - 2 Years</b>	<b>\$14,433,213.35</b>	<b>22%</b>
<b>2 - 3 Years</b>	<b>\$20,914,922.50</b>	<b>32%</b>
<b>3 Years and Over</b>	<b>\$0.00</b>	<b>0%</b>
<b>Total Market Value</b>	<b>\$65,580,242.85</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>1.39 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 05/31/2011 was 1.85
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.



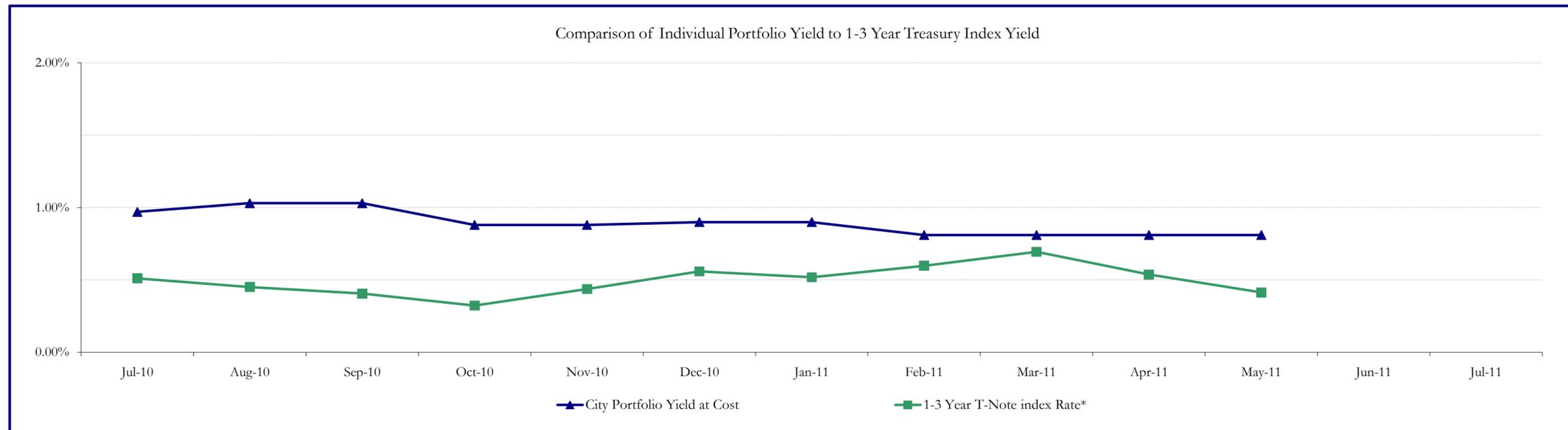
## City of Surprise Individual Portfolio Yield Summary Fiscal Year 2010-2011

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	\$34,159,429	1.72	0.88%	0.32%
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%
Apr-11	\$35,456,156	1.48	0.81%	0.54%
May-11	\$35,580,243	1.39	0.81%	0.41%

<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

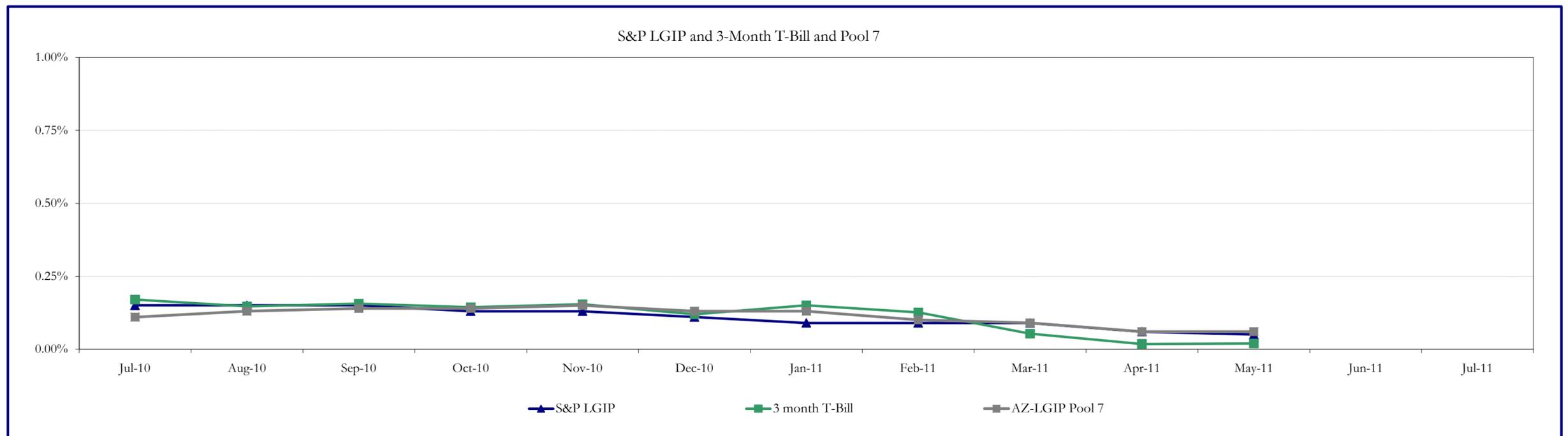


## City of Surprise Short-Term Benchmark Comparisons Fiscal Year 2010-2011

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%
Apr-11	0.06%	0.06%	0.02%
May-11	0.05%	0.06%	0.02%

<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 May 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	5/31/2011	0.00	\$232,107	0.01%		
Alliance Bank (CDARS)	6/30/2011	0.08	\$10,000,000	0.55%		
Alliance Bank (CDARS)	9/29/2011	0.33	\$15,000,000	1.01%		
Alliance Bank (CDARS)	12/29/2011	0.58	\$5,000,000	0.88%		
U.S. Treasury	6/30/2012	1.08	\$2,510,350	0.52%		
FNMA	10/30/2012	1.42	\$2,505,155	0.77%		
FHLMC	11/30/2012	1.50	\$3,000,186	0.66%		
FHLMC	12/21/2012	1.56	\$2,114,864	1.09%		
FNMA	2/26/2013	1.74	\$3,061,650	0.83%		
FHLMC	4/15/2013	1.88	\$1,241,008	0.56%		
FNMA	6/26/2013	2.07	\$2,040,202	1.41%		
FNMA	7/19/2013	2.14	\$2,002,578	1.39%	7/19/11	One-time
FFCB	9/16/2013	2.29	\$5,009,745	0.43%		
FNMA	9/23/2013	2.31	\$5,033,925	0.73%		
FHLMC	11/15/2013	2.46	\$1,248,503	1.01%	8/15/11	Quarterly
U.S. Treasury	11/15/2013	2.46	\$3,082,275	0.81%		
FNMA	11/26/2013	2.49	\$2,497,695	0.98%	8/23/11	Quarterly
<b>Total Market Value</b>			<b>\$ 65,580,243</b>			



## Managed Account Detail of Securities Held

For the Month Ending **May 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	6,560.77	2,502,928.50	2,510,350.00
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	713.72	3,066,786.62	3,082,275.00
<b>Security Type Sub-Total</b>		<b>5,590,000.00</b>					<b>5,565,828.52</b>	<b>0.68</b>	<b>7,274.49</b>	<b>5,569,715.12</b>	<b>5,592,625.00</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	1,076.39	2,490,521.53	2,505,155.00
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	31.25	2,987,145.03	3,000,186.00
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	36,666.67	2,093,237.84	2,114,864.00
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	6,026.56	3,040,574.43	3,061,650.06
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	2,522.81	1,239,133.05	1,241,008.29
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	12,916.67	2,003,827.50	2,040,202.00
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	10,083.33	1,999,485.02	2,002,578.00
FFCB (FLOATING) NOTE DTD 09/16/2010 0.340% 09/16/2013	31331JG64	5,000,000.00	AAA	Aaa	10/12/10	10/13/10	5,000,000.00	0.43	3,898.61	5,000,000.00	5,009,745.00
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	9,444.44	5,030,407.60	5,033,925.00
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	555.56	1,249,692.23	1,248,502.50
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	347.22	2,500,000.00	2,497,695.00



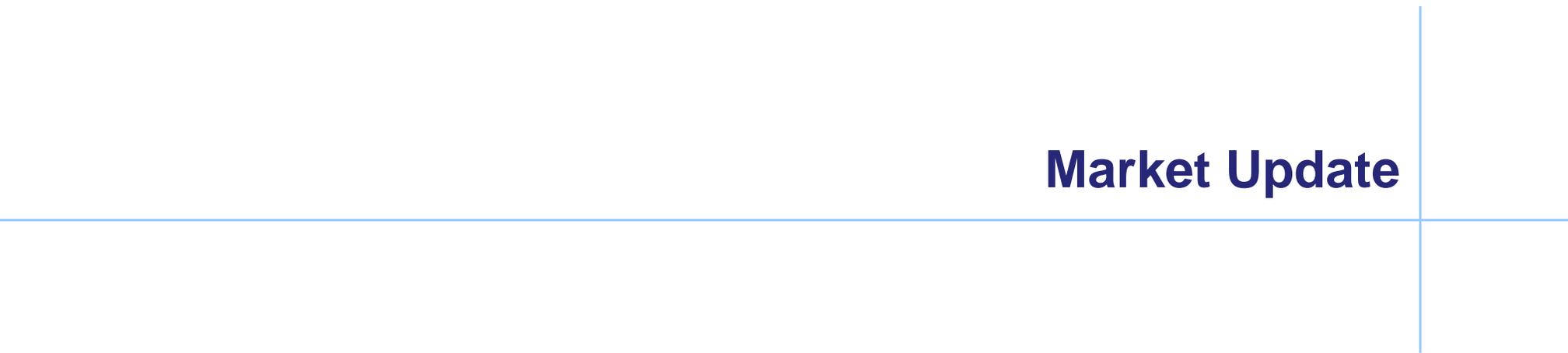
### Managed Account Detail of Securities Held

For the Month Ending **May 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>83,569.51</b>	<b>29,634,024.23</b>	<b>29,755,510.85</b>
<b>Managed Account Sub-Total</b>		<b>35,100,000.00</b>					<b>35,266,930.55</b>	<b>0.81</b>	<b>90,844.00</b>	<b>35,203,739.35</b>	<b>35,348,135.85</b>
<b>Securities Sub-Total</b>		<b>\$35,100,000.00</b>					<b>\$35,266,930.55</b>	<b>0.81%</b>	<b>\$90,844.00</b>	<b>\$35,203,739.35</b>	<b>\$35,348,135.85</b>
<b>Accrued Interest</b>											<b>\$90,844.00</b>
<b>Total Investments</b>											<b>\$35,438,979.85</b>

**Market Update**



# Yields Fall Anew on Disappointing Economic Data

- Yields on U.S. Treasuries plunged in response to more disappointing news about the economy.
- The 2-year note fell to 2011 lows, while the 10-year note moved below the psychologically key 3% mark.

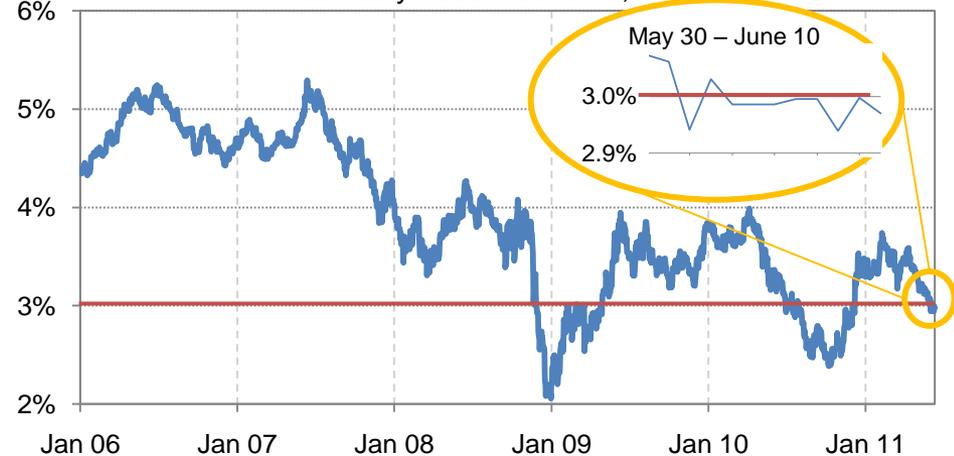
### 2-Year U.S. Treasury Yield

January 2006 – June 10, 2011



### 10-Year U.S. Treasury Yield

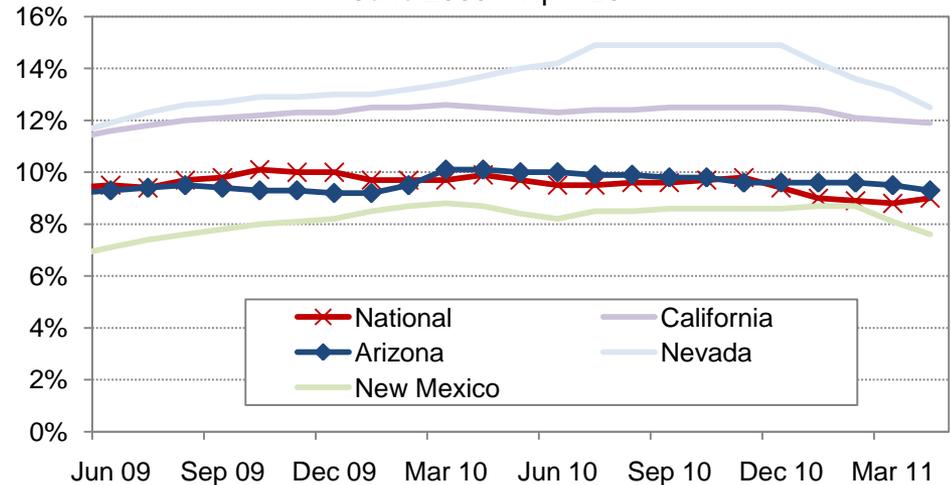
January 2006 – June 10, 2011



# Employment Reports Prove Disappointing, Again

- While the national unemployment rate moved up in April and May, Arizona's moved down in April and compares favorably to other southwestern states.
- Jobs added in May were well below economists' expectations.
  - Factories cut payrolls in May for the first time in seven months.
  - Retailers, leisure and hospitality as well as state and local governments also shed jobs during the month.
  - Government payrolls decreased by 29,000, while employment at service-providers increased by 51,000.

**Unemployment Rate**  
June 2009 – April 2011

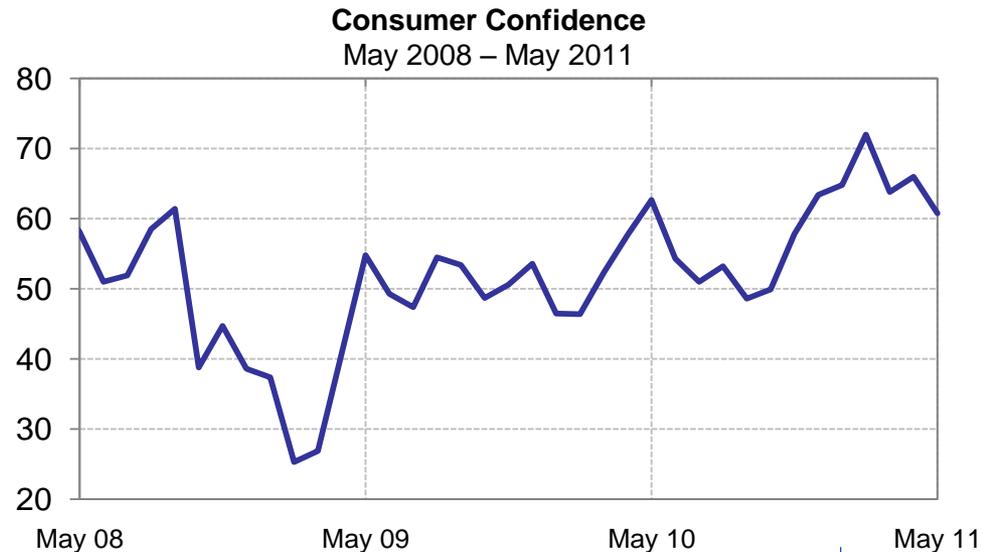


**May Jobs Report**

	Expected	Actual
<b>Nonfarm Payrolls</b>	+165,000 jobs	+54,000 jobs
<b>Private Payrolls</b>	+170,000 jobs	+86,000 jobs
<b>May Unemployment Rate</b>	8.9%	9.1%

# Manufacturing and Optimism Decline

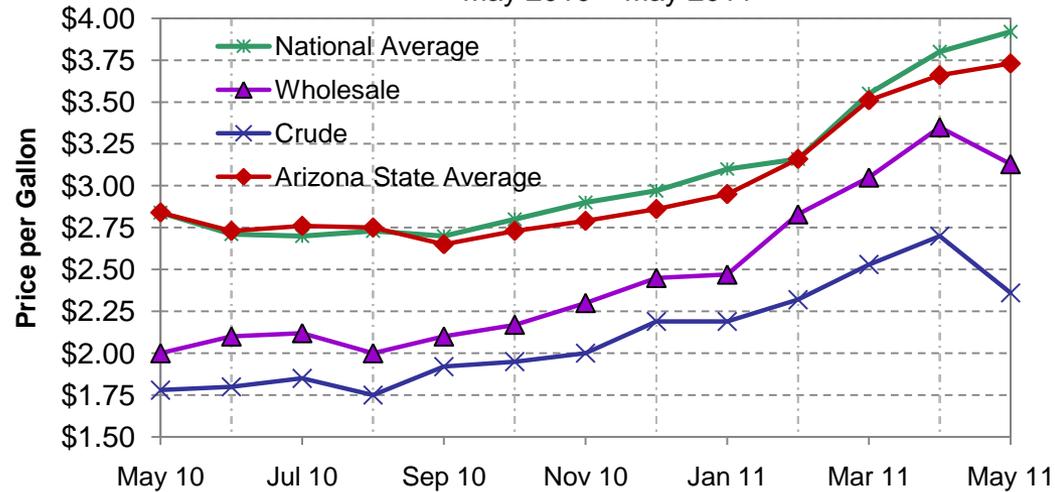
- Manufacturing growth, which has been a driver of the recovery, slowed to the slowest pace of growth since September of 2009, with ISM manufacturing recording 53.5 for May.
- While the reading indicates the sector is still expanding, the decline shows a slowdown—something the economy does not need as it struggles to revive itself.
- Consumer confidence dipped more than anticipated in May, mainly due to views on the labor market after the poor employment reports.



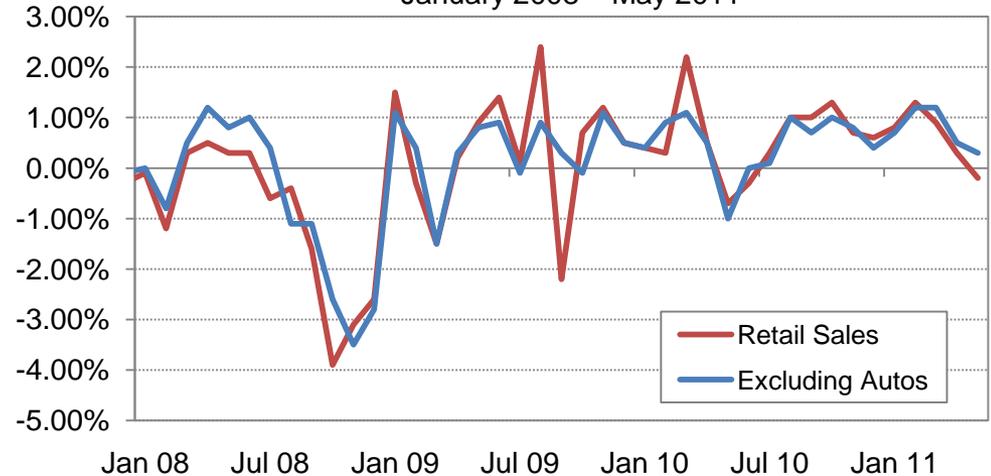
# High Gas Prices Continue to Hurt Consumers

- Prices of oil and other commodities began coming down early in May, relieving fears that inflation may grow out of control. Crude-oil futures prices hit a nearly one-month low Monday, to around \$97 a barrel.
- However, prices at the pump remain elevated and, combined with higher bills at the grocery store, have resulted in consumers cutting back on big-ticket items such as cars and appliances.
- Retail sales data which provide a snapshot of consumption, a major engine of the U.S. economy, has been slow in the first three months of 2011.

Price per Gallon of Gas  
May 2010 – May 2011



Retail Sales (month over month)  
January 2008 – May 2011



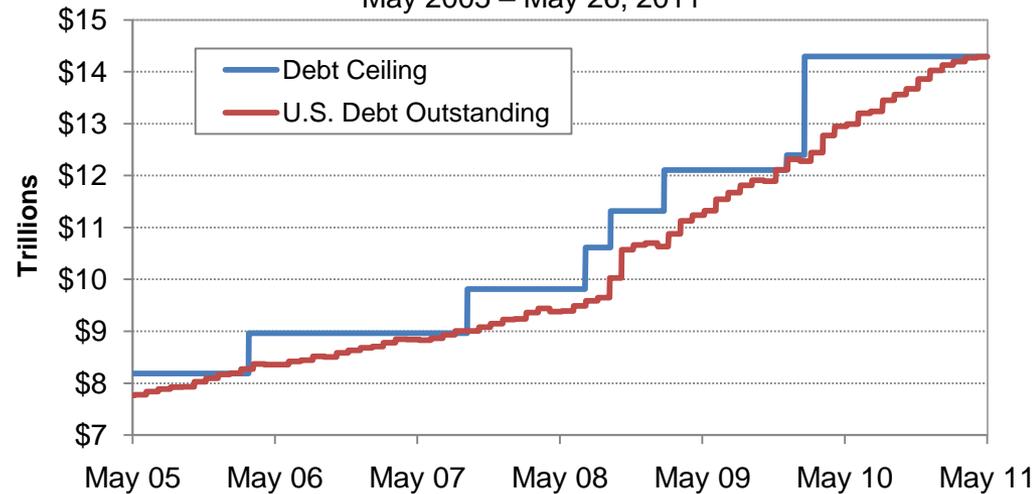
Source: *aaa.com* from surveys by Oil Price Information Service; U.S. Census Bureau

# Debt Ceiling Reached

- The U.S. hit its current debt ceiling of \$14.3 trillion on May 16, but the Treasury has several tools to avoid a default until the beginning of August.
- If Congress does not raise the debt ceiling the Treasury is not permitted to issue new bonds, federal spending would immediately be curtailed in a major way, and the Treasury might default on outstanding debt payments.
- Debt outstanding grows when Federal spending is greater than revenue.
- The Office of Management and Budget estimates the budget deficit will increase to approximately \$1.6 trillion in the current fiscal year, largely because of the massive tax cut bill enacted in December.

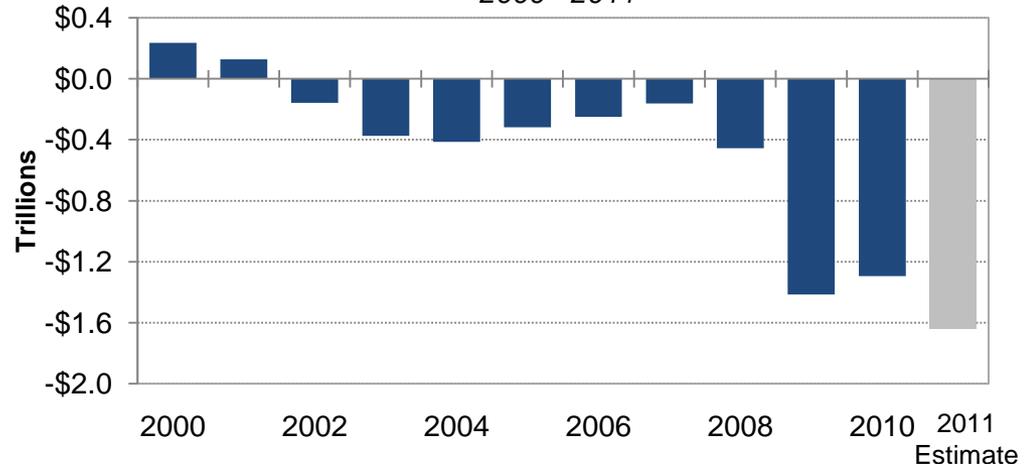
**U.S. Debt Outstanding vs. Debt Ceiling**

May 2005 – May 2011



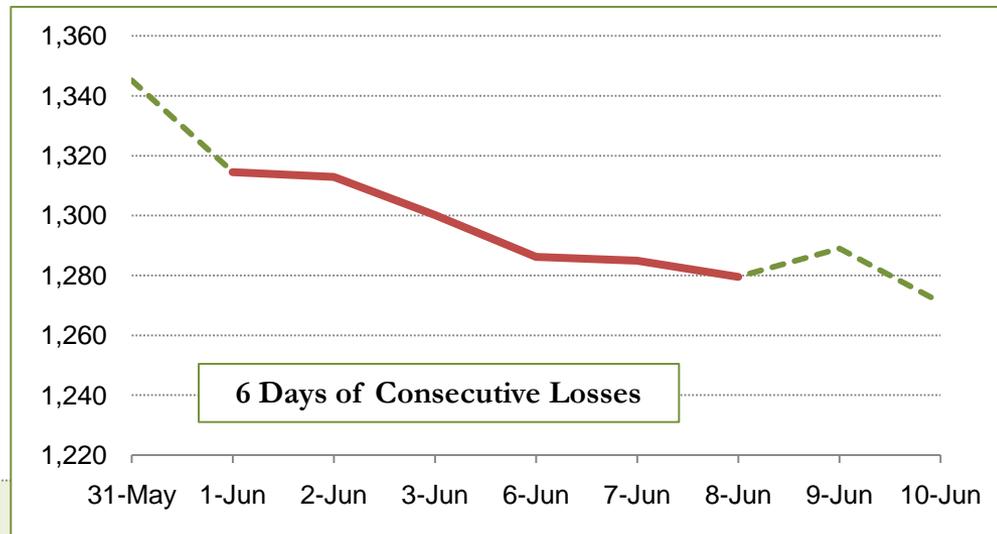
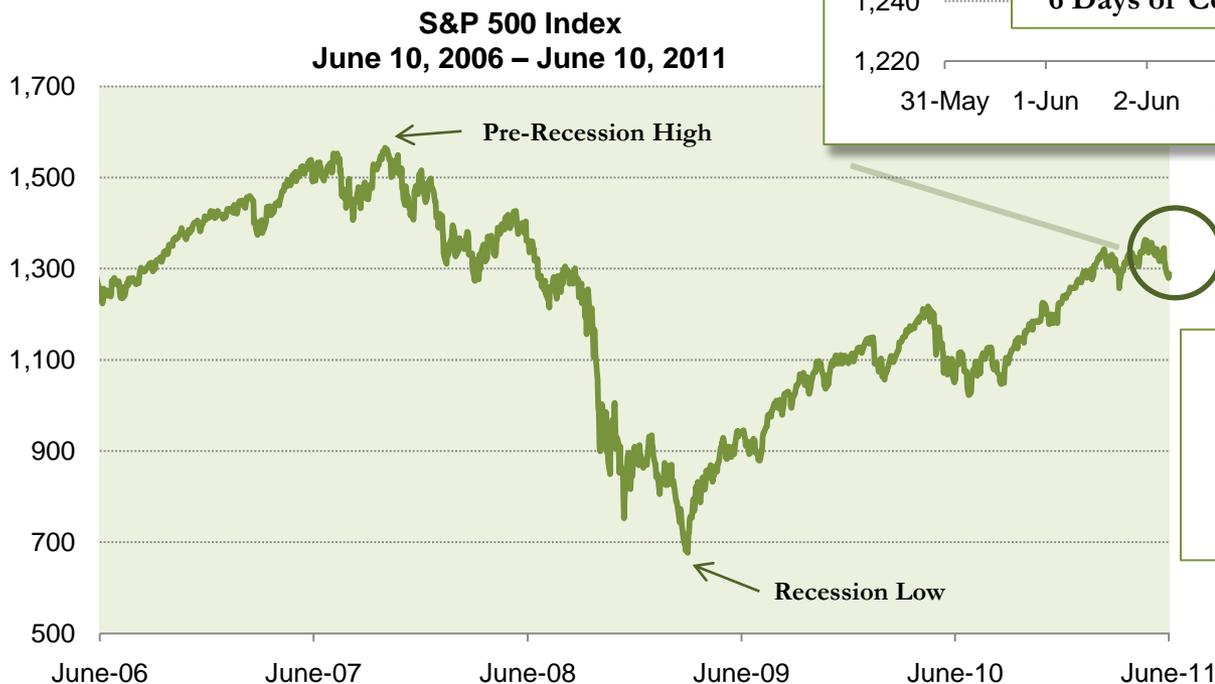
**U.S. Budget Surplus/Deficit**

2000 - 2011



# Equities: Longest Consecutive Losses Since February 2009

- In June, U.S. equities experienced 6 days of consecutive losses, the longest losing streak since February 2009. They began their fall in response to poor ADP unemployment numbers and continued to decline as more negative economic data came in over the rest of the week. Stocks fell 4.9% over this 6-day period.



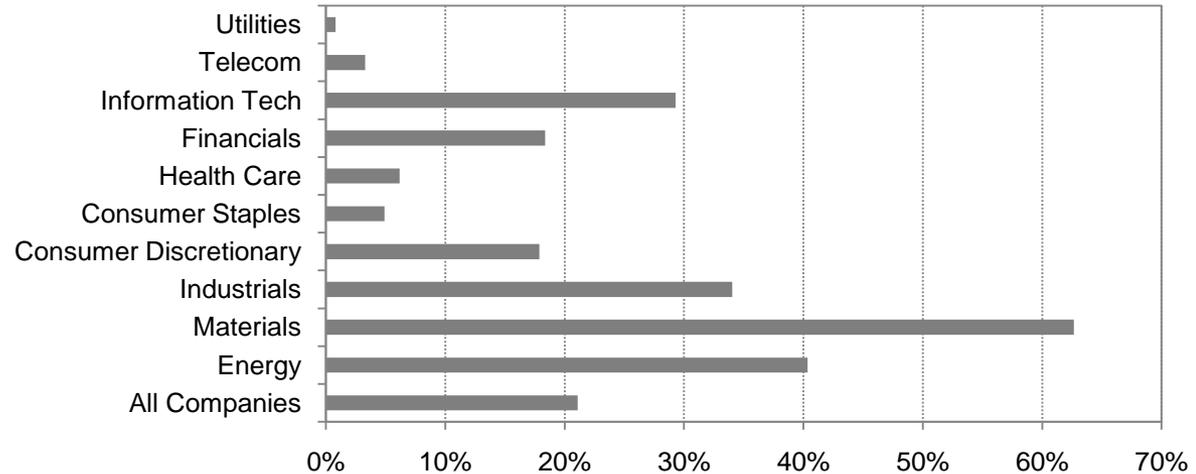
**As of June 10, 2011:**

<b>Gains since Recession Low:</b>	<b>87.9%</b>
<b>Losses since Pre-Recession High:</b>	<b>18.8%</b>

# Corporate Industry Continues to Improve

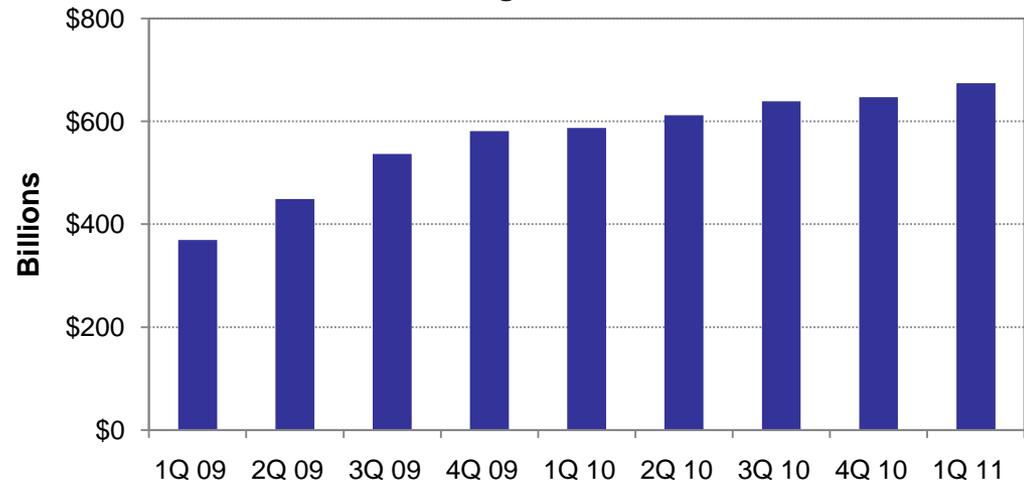
- In the first quarter of 2011, earnings on the S&P 500 increased over 20% compared to the same quarter of 2010. Every sector of the S&P 500 has shown profit improvement.

**S&P 500 Earnings Growth**  
1st Quarter 2011 (Year over Year)



- In addition, banks continue to increase their balance sheets and are flush with cash.

**Tangible Common Equity**  
25 Largest U.S. Banks



Source: FDIC; SNL and Barclays

# IMF Reform

- In 2010 the IMF agreed on reforms to address the changing world markets.
- These reforms represent, “the most fundamental governance overhaul in the Fund’s 65-year history and the biggest ever shift of influence in favor of **emerging market and developing countries to recognize their growing role in the global economy,**” said then IMF Managing Director Dominique Strauss-Kahn.
- Overall the reform results in a 6% shift of quota shares. China’s allocation will increase the most with an additional 2.676 shares.
- The United States remains the largest contributor but also has the largest number of voting shares.

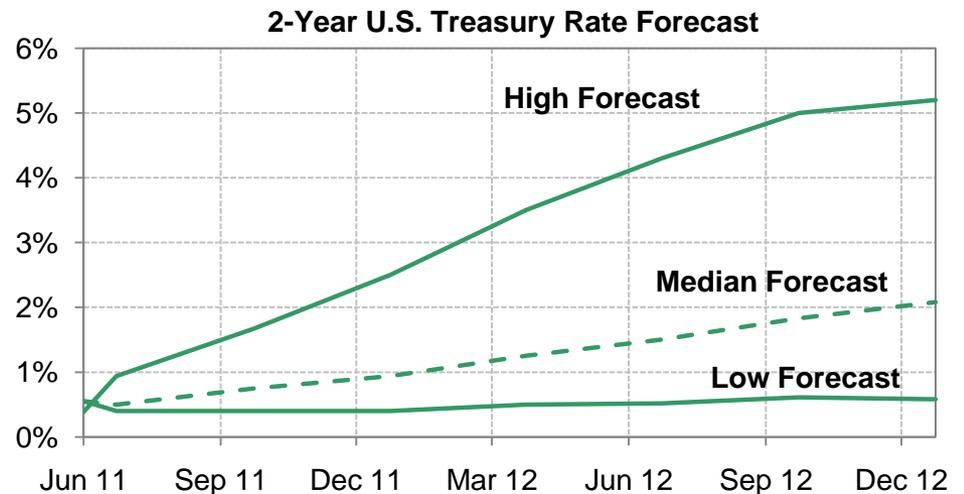
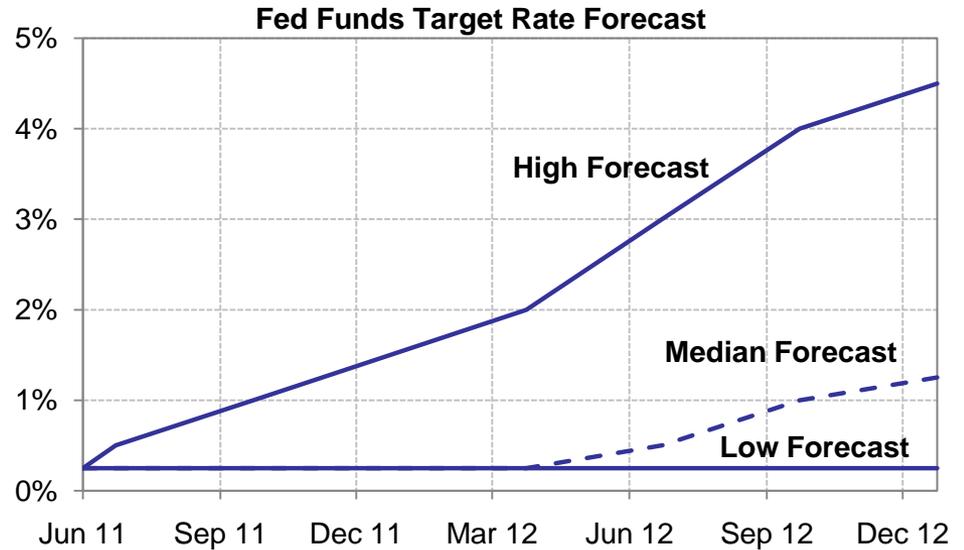
*\*Includes People’s Republic of China, Hong Kong & Macao Special Administrative Regions.  
Source: IMF website*

Quota Shares (arranged by change)			
	3/2/11	Post 2010 Reform	Change
China*	3.718	6.394	+2.676
Brazil	1.395	2.316	+0.921
India	1.911	2.751	+0.840
Spain	1.401	2.000	+0.599
Republic of Korea	1.345	1.800	+0.455
Turkey	0.547	0.977	+0.430
Mexico	1.449	1.869	+0.420
Singapore	0.396	0.816	+0.420
Japan	6.118	6.464	+0.346
United States	17.071	17.407	+0.336

Quota Shares (five largest)			
	3/2/11	Post 2010 Reform	Change
United States	17.071	17.407	0.336
Japan	6.118	6.464	0.346
China*	3.718	6.394	2.676
Germany	5.978	5.586	-0.392
France	4.935	4.227	-0.708

# Interest Rate Forecasts

- Recent weak economic data as well as economists' expectations for growth to remain slow, has resulted in the expectation of continued low rates.
- A majority of the economists surveyed by Bloomberg do not expect the first Fed rate increase until after the first quarter of 2012.
- In conjunction, most believe the 2-year Treasury rate will remain below 1% through the end of the year.



# Disclaimer

*This material is based on information obtained from sources generally believed to be reliable and available to the public, however PFM Asset Management LLC cannot guarantee its accuracy, completeness or suitability. This material is for general information purposes only and is not intended to provide specific advice or a specific recommendation. All statements as to what will or may happen under certain circumstances are based on assumptions, some but not all of which are noted in the presentation. Assumptions may or may not be proven correct as actual events occur, and results may depend on events outside of your or our control. Changes in assumptions may have a material effect on results. Past performance does not necessarily reflect and is not a guaranty of future results. The information contained in this presentation is not an offer to purchase or sell any securities.*