



First Quarter 2012

PFM Asset Management LLC

1820 East Ray Road

Chandler, AZ 85225

855.885.9621

www.pfm.com

City of Surprise
Investment Guidelines and Objectives
Quarter Ended March 31, 2012

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.

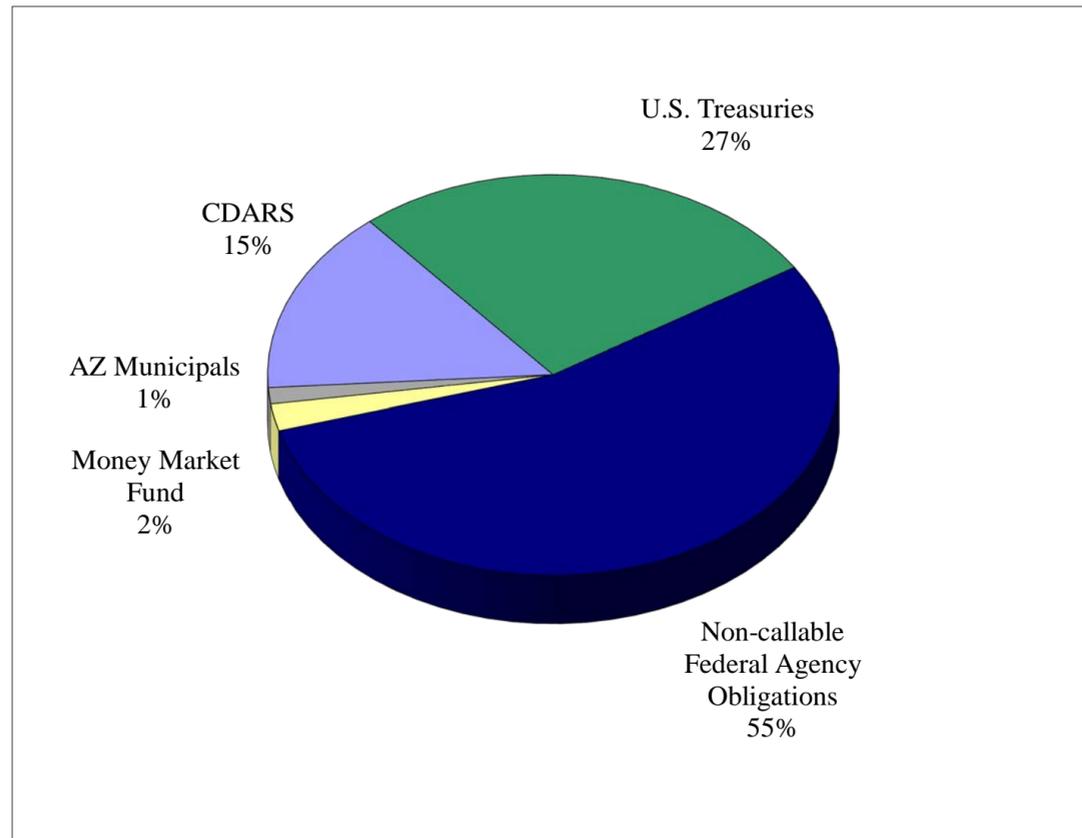
Investment Guidelines: In relation to the investment portfolio, the City's investment strategy focuses on the following:

- **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.

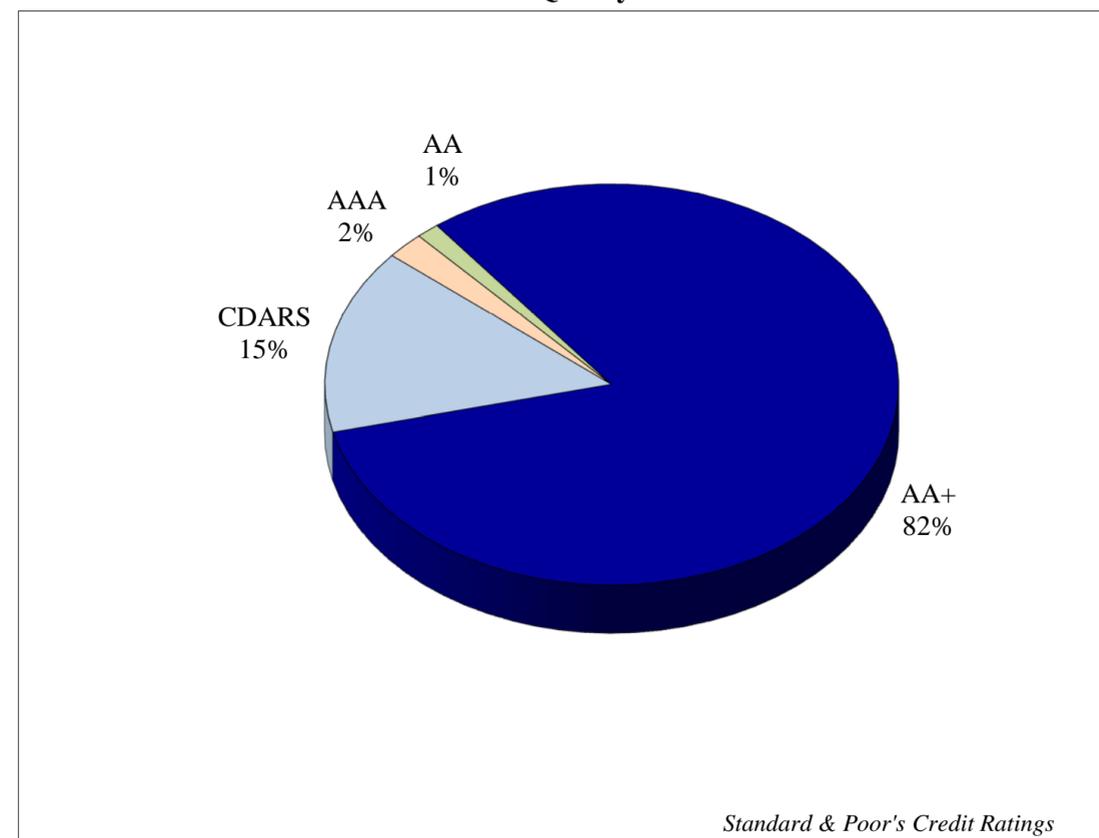
City of Surprise Portfolio Summary and Characteristics
Quarter Ended March 31, 2012

<u>Security Type</u>	<u>Current Holdings*</u>	<u>Current Quarter % of Portfolio</u>	<u>Previous Quarter % of Portfolio</u>
U.S. Treasury	\$18,164,133.95	27%	5%
Federal Agency	\$36,556,488.59	55%	78%
Callable Federal Agency	\$0.00	0%	10%
Non-callable Federal Agency	\$36,556,488.59	55%	68%
CDARS	\$10,000,000.00	15%	17%
AZ Municipals	\$874,625.70	1%	0%
Wells Fargo MMF	\$1,446,612.59	2%	<1%
Total Market Value	\$67,041,860.83	100%	100%

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 trade date. Note that PFM monthly statements reflect holdings as of trade date.

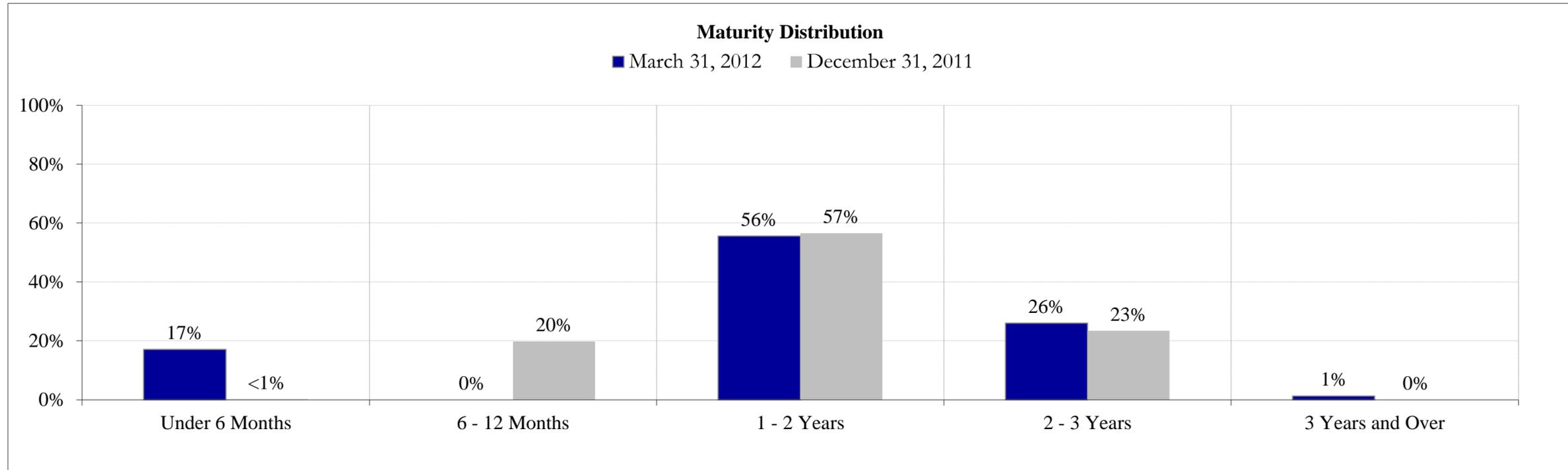
City of Surprise Maturity Summary and Key Portfolio Statistics
Quarter Ended March 31, 2012

Maturity Distribution Summary		
<u>Maturity Class</u>	<u>Fair Value*</u>	<u>% of Portfolio</u>
Under 6 Months	\$11,446,612.59	17%
6 - 12 Months	\$0.00	0%
1 - 2 Years	\$37,268,041.01	56%
2 - 3 Years	\$17,452,581.53	26%
3 Years and Over	\$874,625.70	1%
Total Market Value	\$67,041,860.83	100%

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

Key Portfolio Statistics	
Effective Duration¹	1.77 years
Benchmark Duration²	1.82 years
Yield at Cost	0.53%

1. Duration to worst as of 03/31/2012 was 1.90
 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.



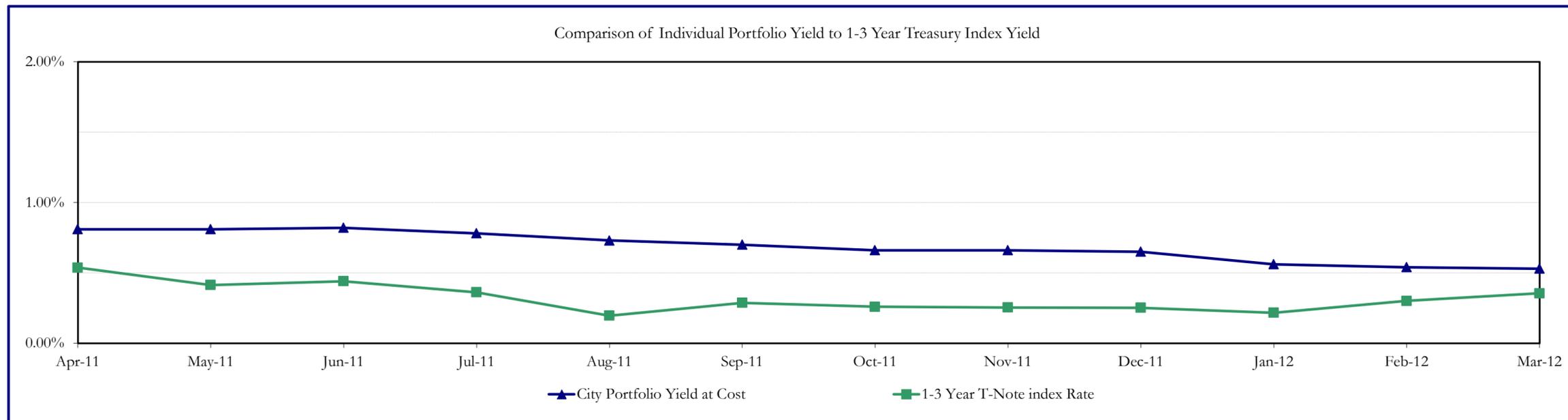
City of Surprise Individual Portfolio Yield Summary Trailing 12 Months

Date	Month-End Market Value ¹	Duration ²	Portfolio YTM at Cost ²	1-3 Year T-Note Index Rate ³
Apr-11	\$35,456,156	1.48	0.81%	0.54%
May-11	\$35,580,243	1.39	0.81%	0.41%
Jun-11	\$35,649,124	1.41	0.82%	0.44%
Jul-11	\$35,675,772	1.41	0.78%	0.36%
Aug-11	\$35,758,718	1.60	0.73%	0.20%
Sep-11	\$50,880,671	1.59	0.70%	0.29%
Oct-11	\$50,889,100	1.66	0.66%	0.26%
Nov-11	\$50,879,151	1.55	0.66%	0.25%
Dec-11	\$50,936,190	1.58	0.65%	0.25%
Jan-12	\$56,125,698	1.74	0.56%	0.22%
Feb-12	\$56,219,709	1.77	0.54%	0.30%
Mar-12	\$57,041,861	1.77	0.53%	0.35%

¹ Excludes accrued interest and CDARS. Includes balance in the custody account MMF

² Excludes CDARS and custoday account MMF

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

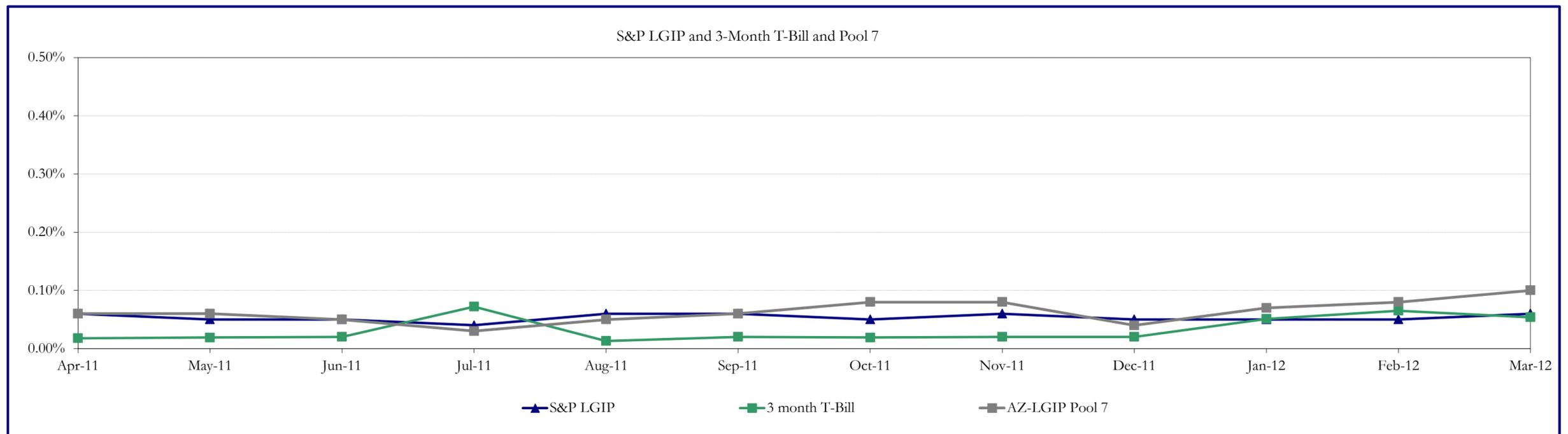


City of Surprise Short-Term Benchmark Comparisons Trailing 12 Months

Date	S&P LGIP	AZ-LGIP Pool 7 ¹	3 month Treasury Bill ²
Apr-11	0.06%	0.06%	0.02%
May-11	0.05%	0.06%	0.02%
Jun-11	0.05%	0.05%	0.02%
Jul-11	0.04%	0.03%	0.07%
Aug-11	0.06%	0.05%	0.01%
Sep-11	0.06%	0.06%	0.02%
Oct-11	0.05%	0.08%	0.02%
Nov-11	0.06%	0.08%	0.02%
Dec-11	0.06%	0.08%	0.02%
Jan-12	0.06%	0.08%	0.02%
Feb-12	0.06%	0.08%	0.02%
Mar-12	0.06%	0.10%	0.05%

¹ Monthly Apportionment Yields. Source: Office of the Arizona State Treasurer

² Rate represents the Merrill Lynch 3-Month U.S. Treasury Bill Index month-end yield. Source: Bloomberg



City of Surprise Holdings
Quarter Ended March 31, 2012

Operating Funds Investment Inventory by Maturity Date

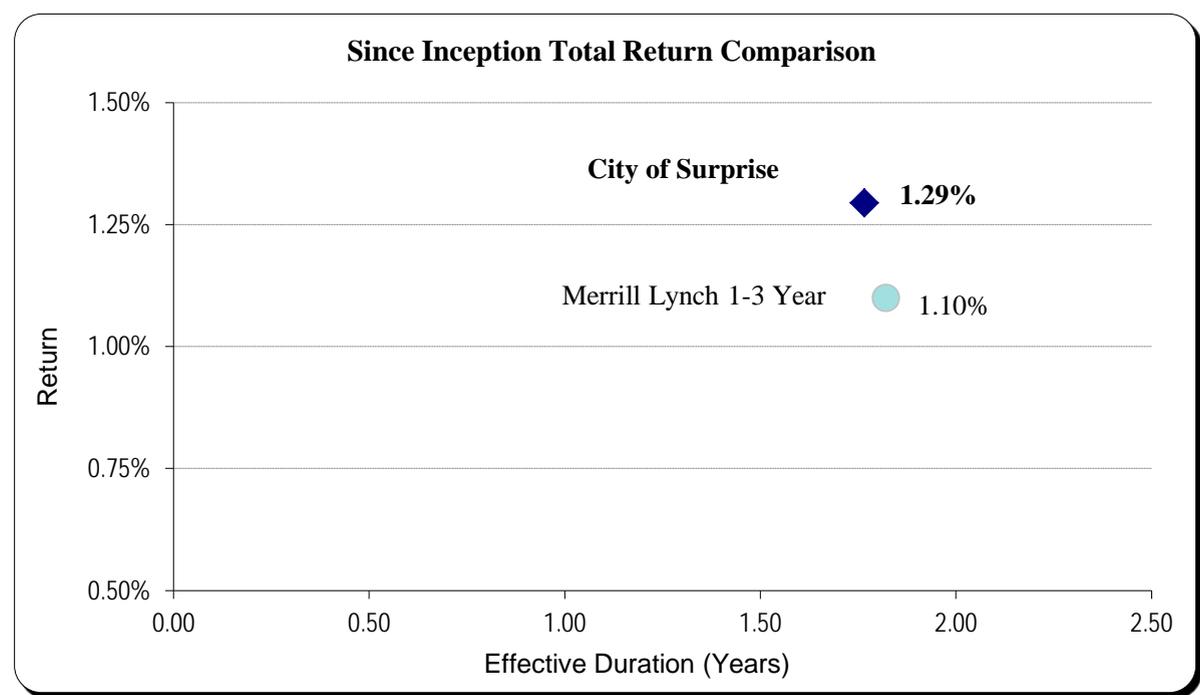
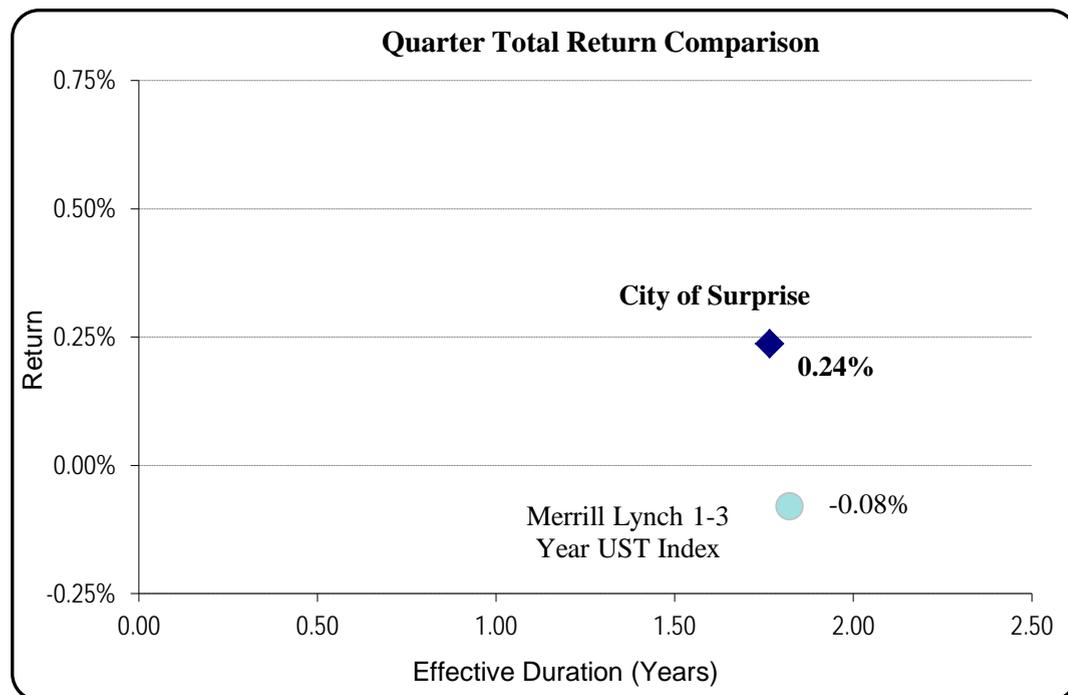
Issuer	Maturity	Years to Maturity	Fair Value	Yield to Maturity	Next Call Date	Frequency
Wells Fargo MMF	3/31/2012	0.00	\$1,446,613	0.01%		
CDARS	6/29/2012	0.25	\$10,000,000	0.66%		
FNMA	6/26/2013	1.24	\$1,015,158	1.41%		
FNMA	8/9/2013	1.36	\$1,253,168	0.36%		
U.S. Treasury	8/15/2013	1.38	\$2,476,771	0.21%		
FHLB	8/28/2013	1.41	\$1,002,486	0.57%		
FHLB	8/28/2013	1.41	\$3,884,633	0.42%		
FFCB	9/16/2013	1.46	\$5,008,985	0.43%		
FNMA	9/23/2013	1.48	\$5,047,270	0.73%		
U.S. Treasury	10/31/2013	1.58	\$3,799,966	0.27%		
U.S. Treasury	11/15/2013	1.63	\$3,099,295	0.81%		
FHLMC	12/23/2013	1.73	\$2,509,545	0.48%		
U.S. Treasury	12/31/2013	1.75	\$3,034,531	0.26%		
FNMA	2/27/2014	1.91	\$1,242,062	0.44%		
FNMA	2/27/2014	1.91	\$3,894,171	0.55%		
FHLMC	8/27/2014	2.41	\$1,012,930	0.94%		
FHLMC	8/27/2014	2.41	\$1,256,033	0.54%		
FHLMC	8/27/2014	2.41	\$2,532,325	0.52%		
FNMA	8/28/2014	2.41	\$3,892,814	0.64%		
U.S. Treasury	12/15/2014	2.71	\$1,093,382	0.39%		
FHLMC	12/29/2014	2.75	\$3,004,908	0.66%		
U.S. Treasury	1/31/2015	2.83	\$2,453,892	0.40%		
U.S. Treasury	2/28/2015	2.91	\$2,206,297	0.51%		
AZ Municipal	7/1/2015	3.25	\$874,626	0.77%		
Total Market Value			\$ 67,041,861			

City of Surprise Quarterly Performance
Quarter Ended March 31, 2012

Portfolio Performance

Total Return ^{1,2,3,5}	Quarter Ended March 31, 2012	Past 6 Months	Past 1 Year	Since Inception
City of Surprise	0.24%	0.40%	1.54%	1.29%
Merrill Lynch 1-3 Year UST I	-0.08%	0.11%	1.44%	1.10%

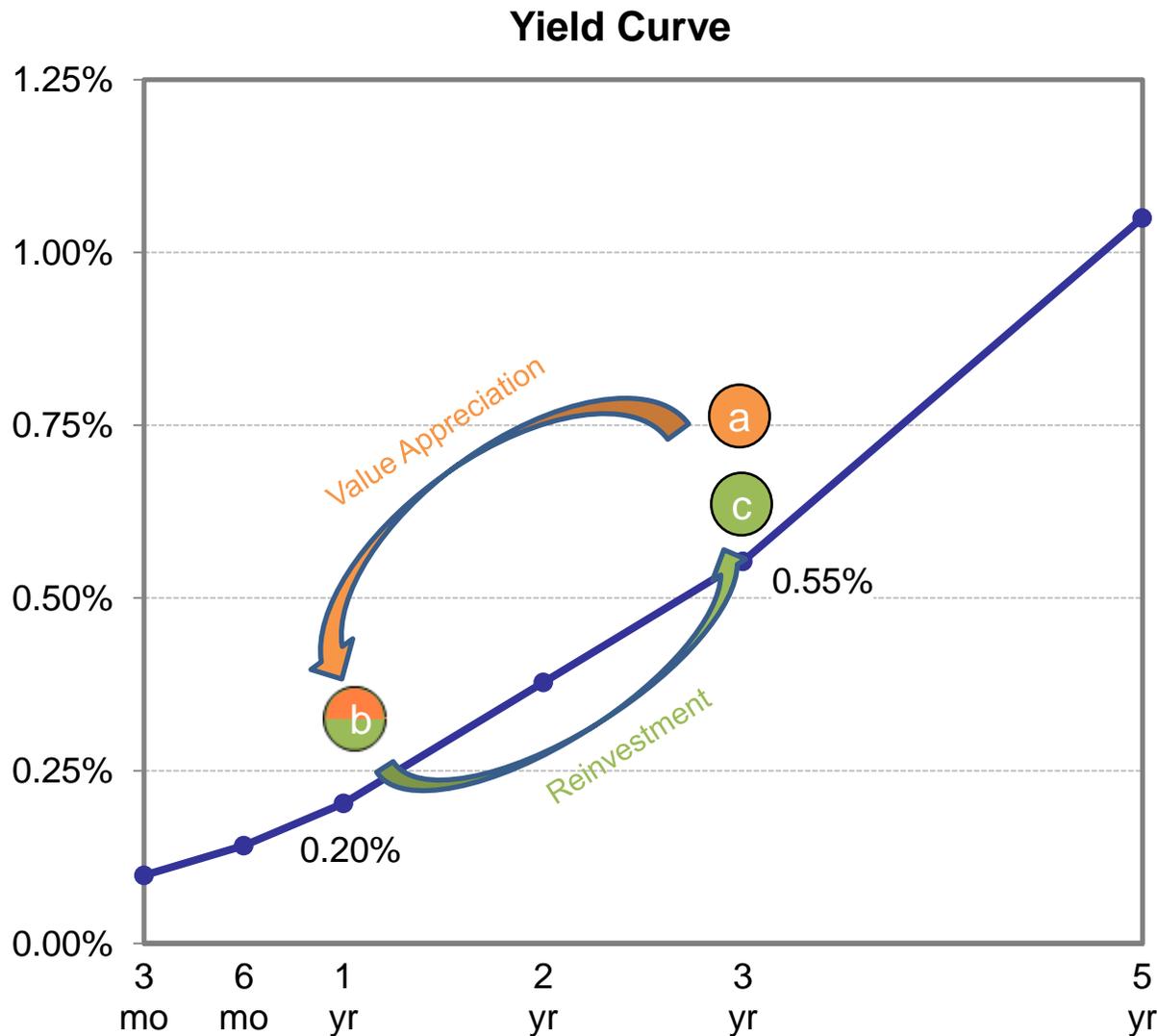
Effective Duration ⁴	March 31, 2012	December 31, 2011	Yields	March 31, 2012	December 31, 2011
City of Surprise	1.77	1.58	Yield at Market	0.39%	0.46%
Merrill Lynch 1-3 Year UST I	1.82	1.81	Yield on Cost	0.53%	0.65%



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.

“Rolling Down” the Yield Curve



Today:

- a) Invest \$10 million in 3-year Agency at 0.55%.

2 Years from Today:

- b) Sell \$10 million 1-year Agency notes at yield of 0.20%.

Realize gain of \$34,000 due to market value appreciation.

- c) Reinvest \$10,034,000 in a 3-year Agency at 0.55%.

Yield Spreads Are Historically Narrow

- The yield difference between fixed-income sectors has narrowed substantially since last quarter.

Difference Between 2-Year Treasury and 2-Federal Agency Yields
September 2011 – March 2012



Increased Allocation to the Treasury Sector

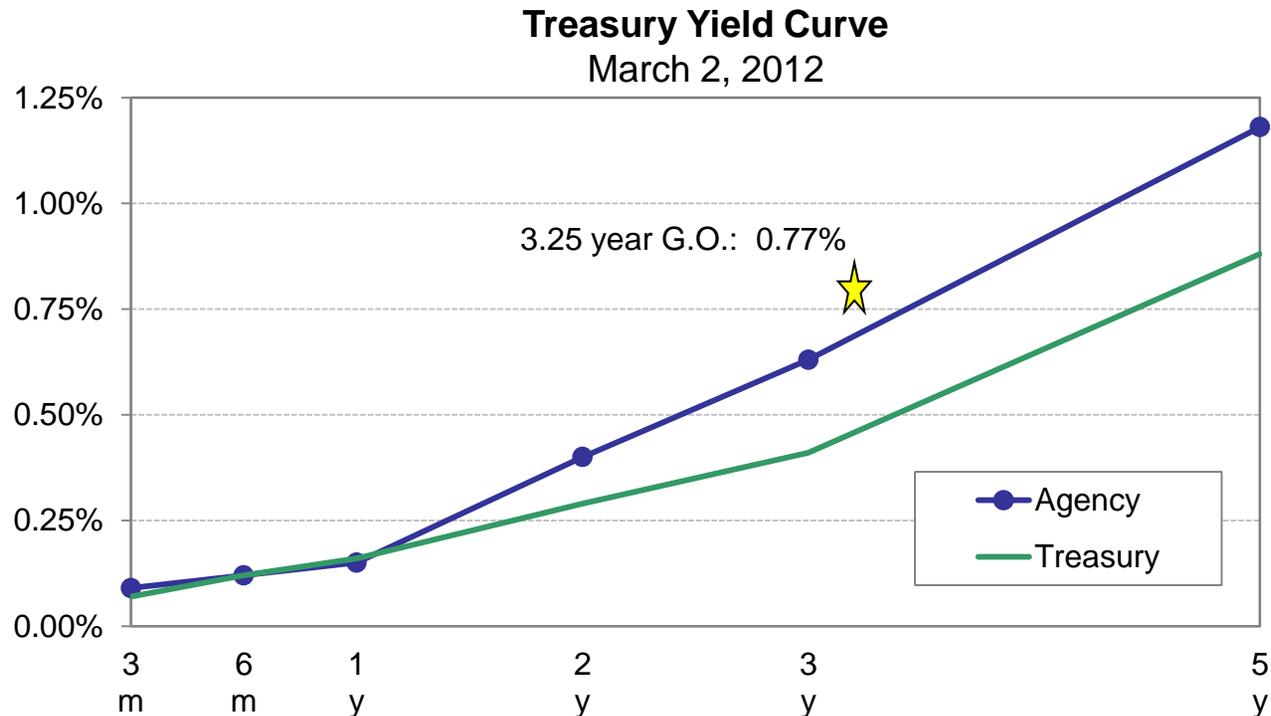
- As yield spreads compressed, we sold Agencies and purchased Treasuries.
 - Trades realized appreciation from “roll down” resulting in gains of \$57,300.
 - Reinvestment of the proceeds picked-up an average of 0.14%.
 - New purchases helped to maintain the portfolio’s duration target.

Date	Transaction	Security	Maturity	Par (millions)	Yield	Realized G/L
1/9/12	Sell	FNMA Notes	2/26/13	3.04	0.22%	21,159
1/9/12	Sell	FHLMC Notes	12/21/12	2.00	0.18%	17,693
1/9/12	Buy	U.S. Treasury Notes	12/15/14	2.00	0.39%	-
1/9/12	Buy	U.S. Treasury Notes	12/31/13	3.04	0.26%	-
3/14/12	Sell	FHLMC Notes	4/15/13	1.21	0.25%	4,061
3/14/12	Sell	FNMA Notes	6/26/13	1.00	0.28%	14,387
3/14/12	Buy	U.S. Treasury Notes	2/28/15	2.09	0.51%	-

Added Municipal Securities

- Purchased 3.25 year City of Mesa G.O. Bond that took advantage of the steepness of the yield curve and offered an attractive yield relative to other sectors.
- Further diversified the sector and issuer holdings of the portfolio.

Trade Date	Settle Date	Transaction	Security	Maturity	Par	Yield	S&P Rating
3/2/12	4/4/12	Buy	City of Mesa G.O. Bonds	7/1/15	845,000	0.77%	AA





Managed Account Detail of Securities Held

For the Month Ending **March 31, 2012**

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
U.S. Treasury Bond / Note											
US TREASURY NOTES DTD 08/15/2003 4.250% 08/15/2013	912828BH2	2,350,000.00	AA+	Aaa	01/13/12	01/13/12	2,500,730.47	0.21	12,621.57	2,480,272.84	2,476,770.75
US TREASURY NOTES DTD 10/31/2008 2.750% 10/31/2013	912828JO4	3,660,000.00	AA+	Aaa	02/10/12	02/13/12	3,814,692.19	0.27	42,306.18	3,802,802.62	3,799,965.72
US TREASURY NOTES DTD 11/15/2010 0.500% 11/15/2013	912828PU8	3,090,000.00	AA+	Aaa	12/01/10	12/02/10	3,062,117.58	0.81	5,857.42	3,074,615.88	3,099,294.72
US TREASURY N/B DTD 01/03/2012 0.125% 12/31/2013	912828RW2	3,045,000.00	AA+	Aaa	01/05/12	01/09/12	3,036,792.77	0.26	962.02	3,037,738.34	3,034,531.29
US TREASURY NOTES DTD 12/15/2011 0.250% 12/15/2014	912828RV4	1,100,000.00	AA+	Aaa	01/05/12	01/09/12	1,095,445.31	0.39	811.48	1,095,795.98	1,093,382.40
US TREASURY NOTES DTD 02/01/2010 2.250% 01/31/2015	912828MH0	2,340,000.00	AA+	Aaa	01/23/12	01/26/12	2,469,522.66	0.40	8,823.21	2,461,775.99	2,453,892.19
US TREASURY NOTES DTD 03/01/2010 2.375% 02/28/2015	912828MR8	2,095,000.00	AA+	Aaa	03/13/12	03/14/12	2,209,570.31	0.51	4,326.63	2,207,690.59	2,206,296.88
Security Type Sub-Total		17,680,000.00					18,188,871.29	0.41	75,708.51	18,160,692.24	18,164,133.95
Municipal Bond / Note											
MESA AZ GO MUNI BONDS DTD 04/04/2012 2.000% 07/01/2015	590485WN4	845,000.00	AA	Aa2	03/02/12	04/04/12	878,200.05	0.77	0.00	878,200.05	874,625.70
Security Type Sub-Total		845,000.00					878,200.05	0.77	0.00	878,200.05	874,625.70
Federal Agency Bond / Note											
FNMA GLOBAL NOTES DTD 05/21/2010 1.500% 06/26/2013	31398AT44	1,000,000.00	AA+	Aaa	06/16/10	06/17/10	1,002,780.00	1.41	3,958.33	1,001,149.49	1,015,158.00
FNMA NOTES DTD 06/17/2011 0.500% 08/09/2013	3135G0BR3	1,250,000.00	AA+	Aaa	08/26/11	08/29/11	1,253,437.50	0.36	902.78	1,252,398.98	1,253,167.50
FHLB GLOBAL NOTES DTD 07/21/2011 0.500% 08/28/2013	313374Y61	1,000,000.00	AA+	Aaa	07/20/11	07/21/11	998,610.00	0.57	458.33	999,066.90	1,002,486.00



Managed Account Detail of Securities Held

For the Month Ending **March 31, 2012**

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
Federal Agency Bond / Note											
FHLB GLOBAL NOTES DTD 07/21/2011 0.500% 08/28/2013	313374Y61	3,875,000.00	AA+	Aaa	10/03/11	10/04/11	3,880,735.00	0.42	1,776.04	3,879,256.30	3,884,633.25
FFCB (FLOATING) NOTE DTD 09/16/2010 0.380% 09/16/2013	31331JG64	5,000,000.00	AA+	Aaa	10/12/10	10/13/10	5,000,000.00	0.43	868.06	5,000,000.00	5,008,985.00
FANNIE MAE GLOBAL NOTES DTD 08/06/2010 1.000% 09/23/2013	31398A2S0	5,000,000.00	AA+	Aaa	10/12/10	10/13/10	5,038,650.00	0.73	1,111.11	5,019,503.95	5,047,270.00
FHLMC NOTES DTD 11/18/2011 0.625% 12/23/2013	3134G3BF6	2,500,000.00	AA+	Aaa	12/19/11	12/20/11	2,507,025.00	0.48	4,253.47	2,506,047.13	2,509,545.00
FNMA GLOBAL NOTES DTD 02/01/2011 1.250% 02/27/2014	3135G0AP8	1,220,000.00	AA+	Aaa	08/15/11	08/15/11	1,244,900.20	0.44	1,440.28	1,238,755.07	1,242,062.48
FNMA GLOBAL NOTES DTD 02/01/2011 1.250% 02/27/2014	3135G0AP8	3,825,000.00	AA+	Aaa	10/03/11	10/04/11	3,889,068.75	0.55	4,515.63	3,875,997.92	3,894,171.30
FHLMC NOTES DTD 07/05/2011 1.000% 08/27/2014	3137EACV9	1,000,000.00	AA+	Aaa	07/19/11	07/20/11	1,001,860.00	0.94	944.44	1,001,445.46	1,012,930.00
FHLMC NOTES DTD 07/05/2011 1.000% 08/27/2014	3137EACV9	1,240,000.00	AA+	Aaa	08/26/11	08/29/11	1,257,099.60	0.54	1,171.11	1,253,757.86	1,256,033.20
FHLMC NOTES DTD 07/05/2011 1.000% 08/27/2014	3137EACV9	2,500,000.00	AA+	Aaa	01/13/12	01/13/12	2,531,275.00	0.52	2,361.11	2,528,708.50	2,532,325.00
FNMA NOTES DTD 07/18/2011 0.875% 08/28/2014	3135G0BY8	3,860,000.00	AA+	Aaa	10/03/11	10/04/11	3,885,669.00	0.64	3,096.04	3,881,353.21	3,892,813.86
FHLMC NOTES DTD 12/16/2011 0.625% 12/29/2014	3137EADA4	3,000,000.00	AA+	Aaa	12/16/11	12/19/11	2,996,850.00	0.66	5,468.75	2,997,142.98	3,004,908.00
Security Type Sub-Total		36,270,000.00					36,487,960.05	0.58	32,325.48	36,434,583.75	36,556,488.59
Managed Account Sub-Total		54,795,000.00					55,555,031.39	0.53	108,033.99	55,473,476.04	55,595,248.24



Managed Account Detail of Securities Held

For the Month Ending **March 31, 2012**

CITY OF SURPRISE OPERATING FUND

Securities Sub-Total	\$54,795,000.00	\$55,555,031.39	0.53%	\$108,033.99	\$55,473,476.04	\$55,595,248.24
Accrued Interest						\$108,033.99
Total Investments						\$55,703,282.23

Bolded items are forward settling trades.

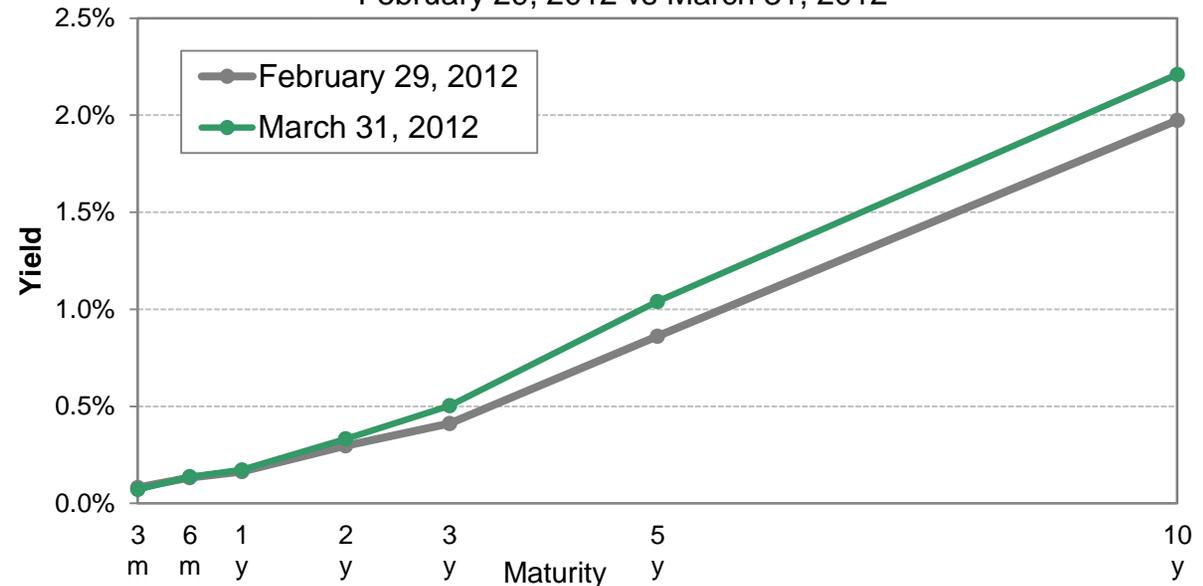


Market Update

Yields Up Over Month End and For Quarter

- Very short-term yields remain unchanged from last month, held down by the Fed's zero interest rate policy.
- Longer-term investments increased on good news from Europe, positive U.S. economic data, and diminished expectations for Fed stimulus.
- After trading in a narrow range for many months, 2-3 year Treasury yields moved up in March to 8-month highs.
- Despite the move higher we do not believe this represents a fundamental change in the market place or warrants a significant change in strategy.
- The Fed has committed to keep low rates through late 2014 and economic conditions continue to reflect only moderate growth.

U.S. Treasury Yield Curve
February 29, 2012 vs March 31, 2012



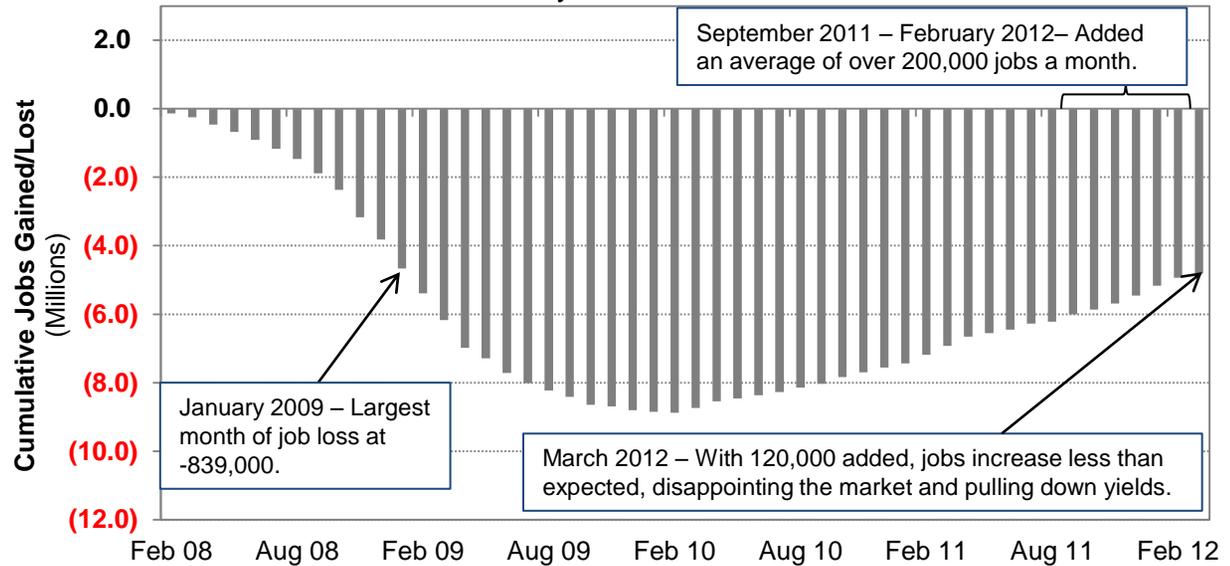
2-Year U.S. Treasury Yield
December 31, 2011 – April 9, 2012



Job Data Improving But Has a Ways To Go

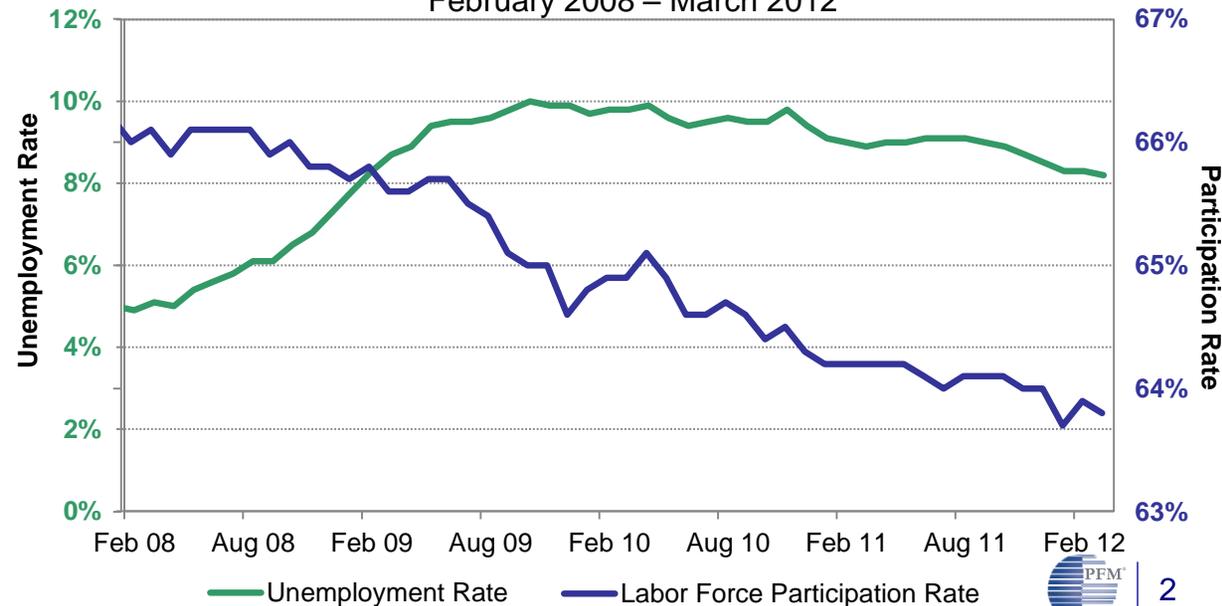
- Beginning February 2008, the U.S. experienced 25 months of decreasing jobs, totaling 8.8 million jobs lost.
- Since March 2012, the U.S. has added jobs for 25 straight months, totaling 4 million gained.
- From February 2008 to March 2012, the result is a net loss of 4.8 million jobs.

Cumulative Jobs Gained and Lost
February 2008 – March 2012



- The Unemployment Rate declined in March to 8.2%, the lowest level in three years.
- However, the labor force participation rate also declined, suggesting the decrease in unemployment was a result of people leaving the labor force.
- On the bright side, baby boomers retiring are a big reason for the declining participation rate and not frustrated job seekers.

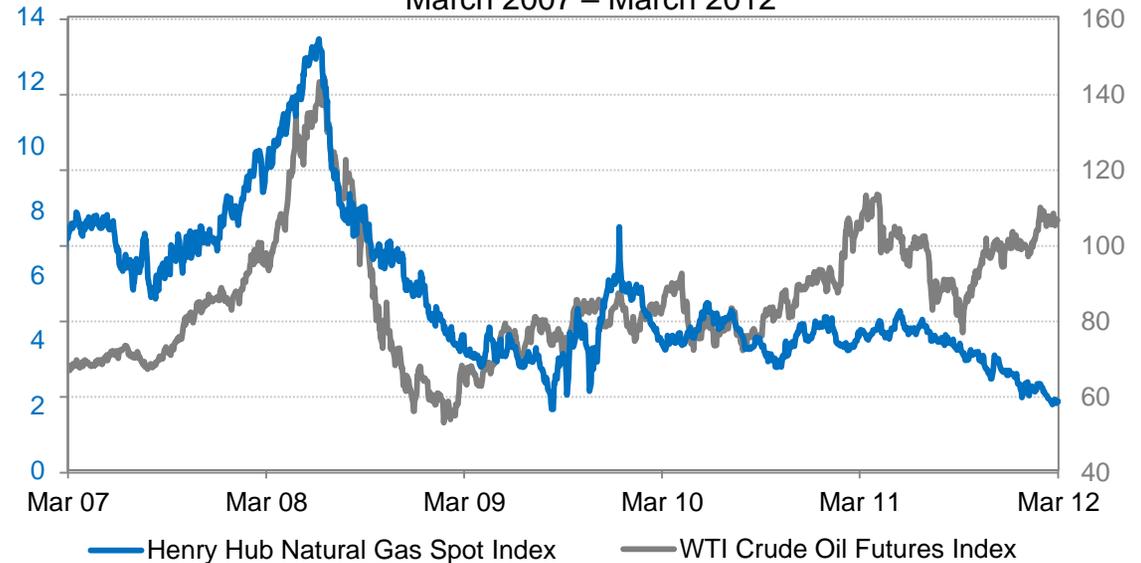
Unemployment Rate vs. Labor Force Participation Rate
February 2008 – March 2012



With High Oil Prices Countered By Low Natural Gas Prices Confidence Remains Strong

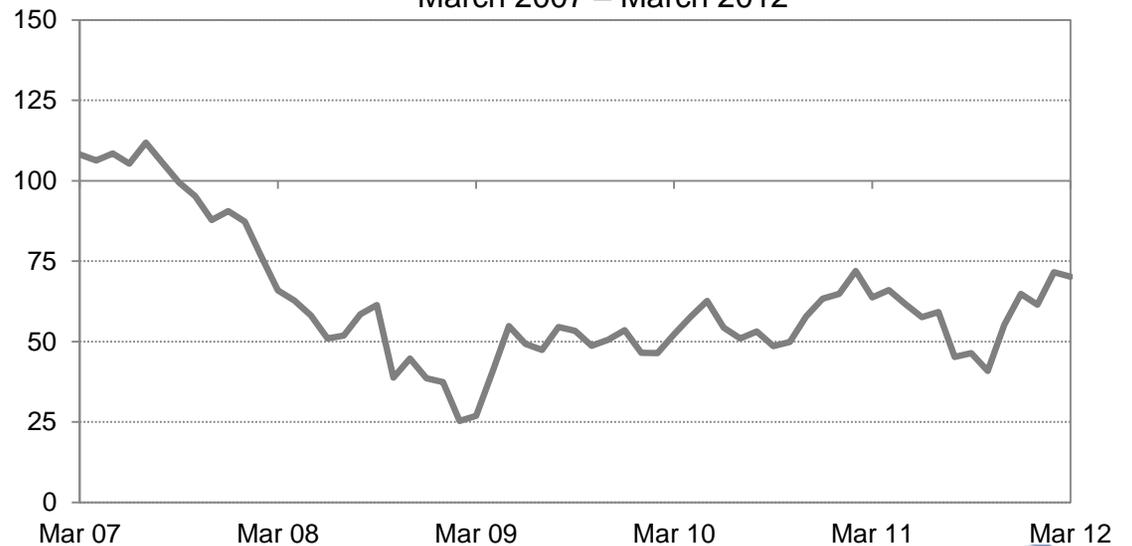
- While oil prices, and therefore gas at the pump, has been on the rise, natural gas prices and a mild winter have helped ease the consumer's burden.

Henry Hub Natural Gas Spot Index vs. WTI Crude Oil Futures Index
March 2007 – March 2012



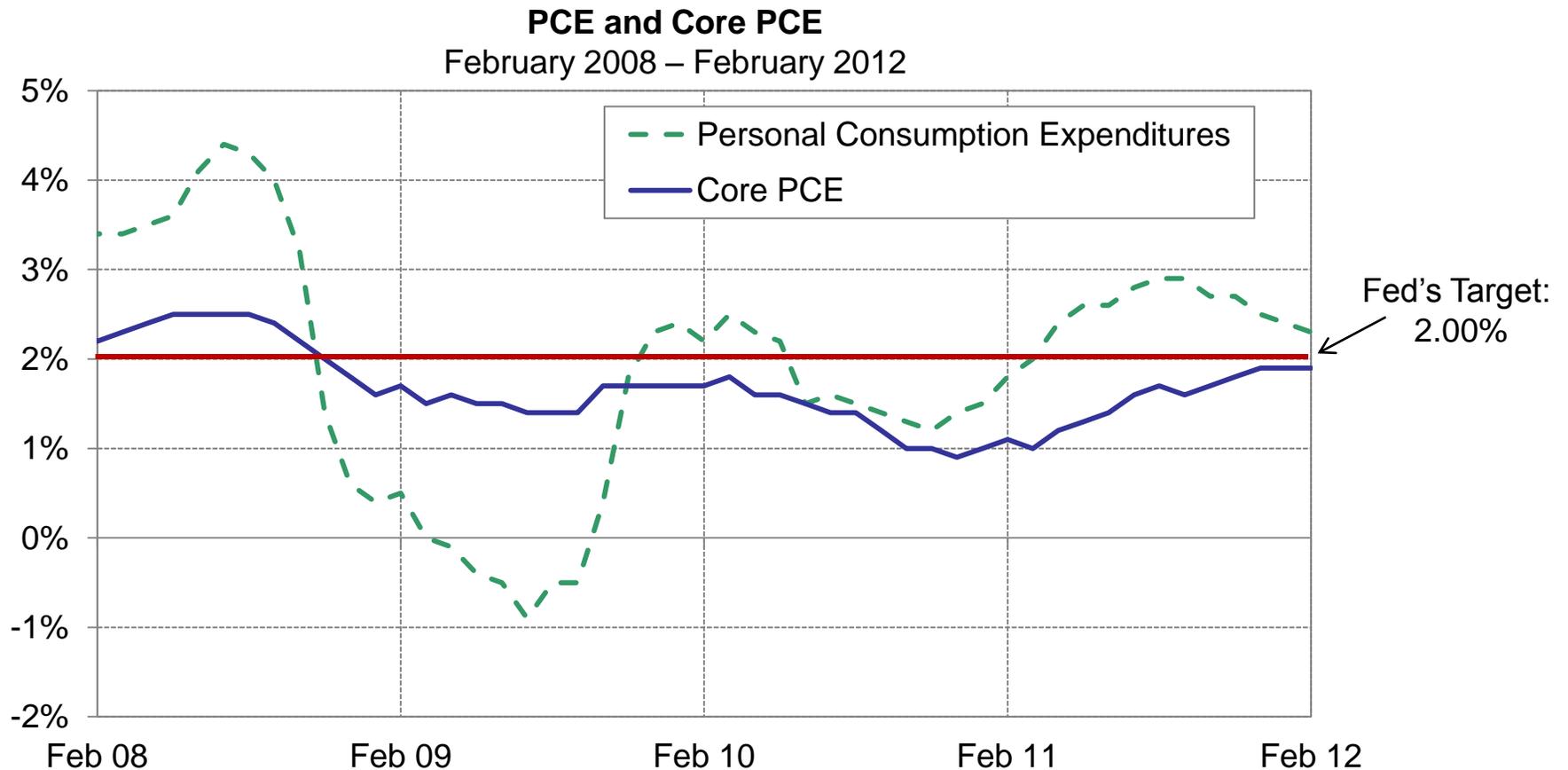
- This could help explain why consumer confidence has not declined as gas prices have risen.
- Employment growth, income gains and higher stock prices are helping sustain the improvement in confidence that may help lift consumer spending.

Consumer Confidence
March 2007 – March 2012



Fed Remains Unconcerned About Inflation

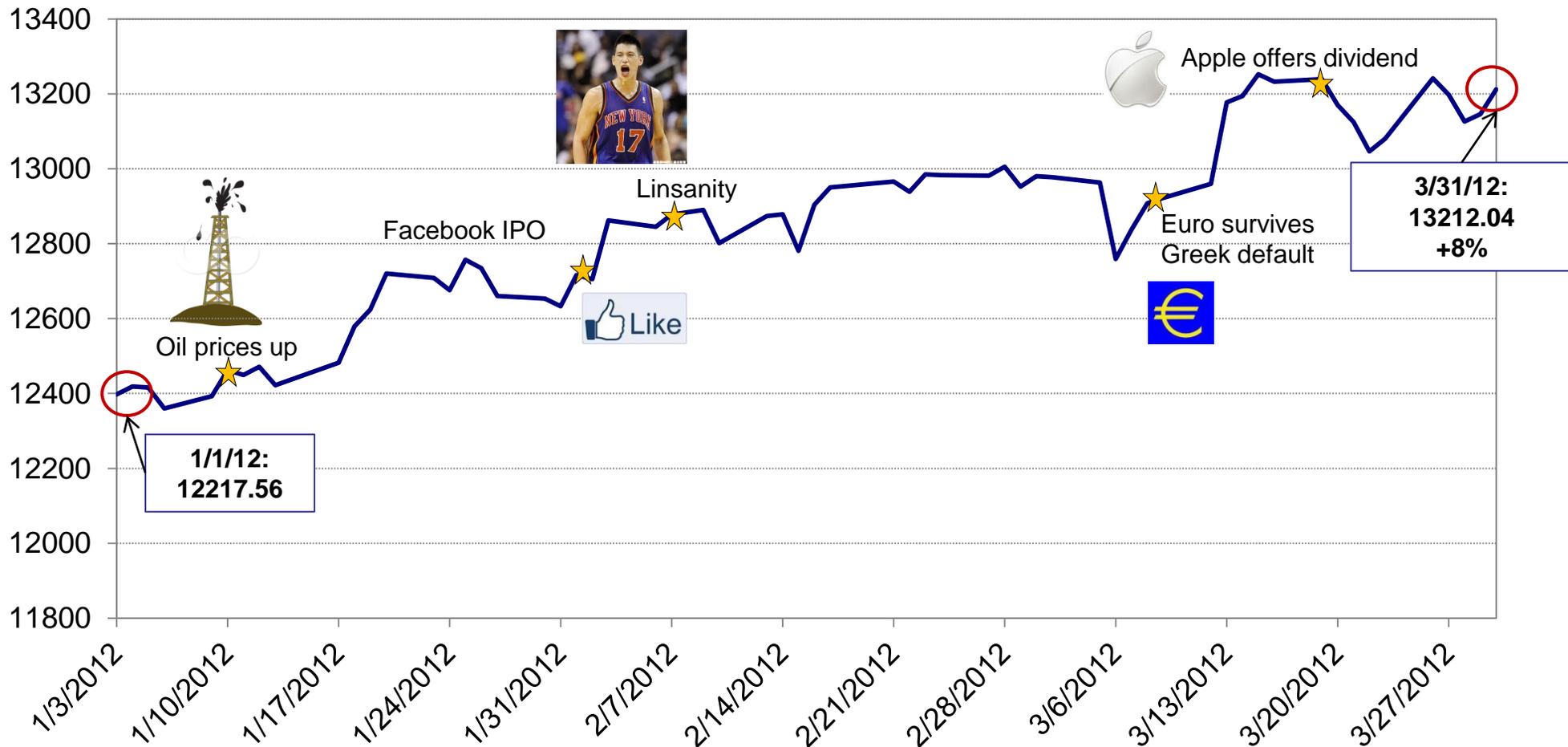
- While the price of food in the grocery store and the price of gas at the pump are on the rise, Core Personal Consumption Expenditures (PCE), the Fed's preferred measure of inflation, is low and slightly below the Fed's target.
- Core PCE, which excludes the price of food and energy, was at 1.9% at the end of February. Including the more volatile food and energy, inflation is slightly higher, however very close to the Fed's target.



Good News: Stock Market and Corporate Earnings

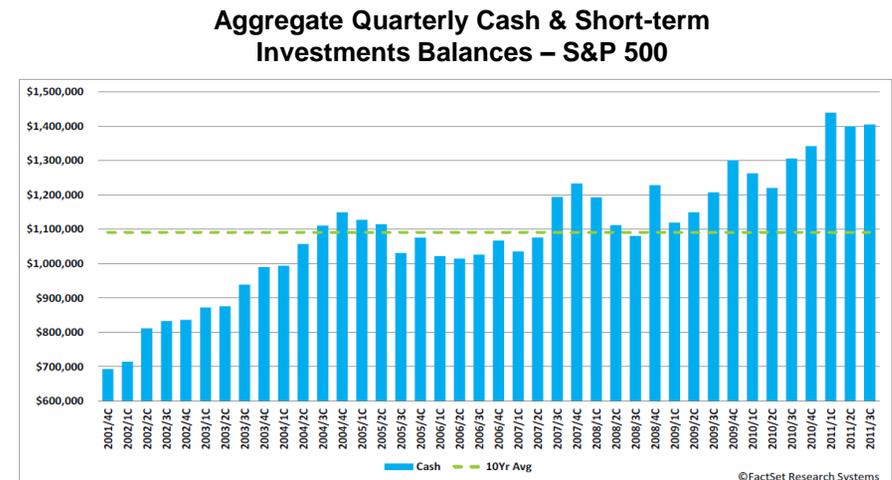
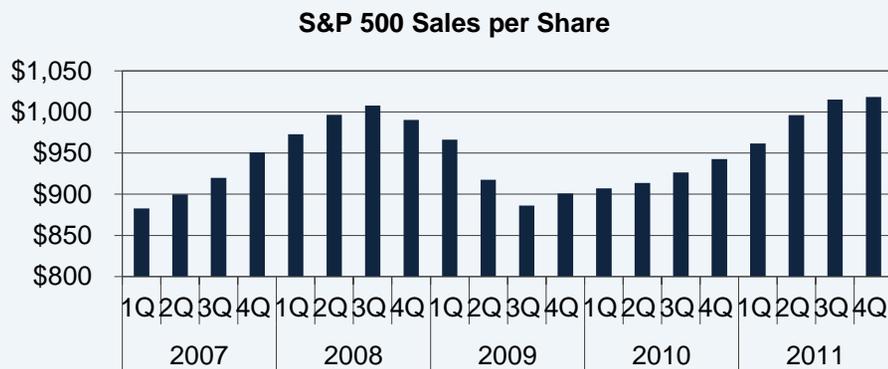
- The Dow Jones recorded its best first quarter since 1998, up 8% from January 1 to March 31.
- Corporate earnings, which are just beginning to be released, are expected to come in strong.

Dow Jones



Despite Stronger Balance Sheets, Persistent Downward Trend in Ratings

- Although corporate balance sheets are strong, credit ratings continue to decline.



Why Credit Ratings Are Being Downgraded

- Standard & Poor's has changed the rating methodology for banks.
- Moody's has changed their view on the risks associated with banks.
- Credit rating criteria is now a moving target for managers.
- The string of sovereign rating downgrades has impacted bank ratings.
- Management views high credit ratings as less important.
- Shareholder friendly activities have negatively impacted credit ratings.

Despite the trend toward lower ratings in the banking sector, more stringent regulation likely makes the banking sector more stable.

Downgrades Will Continue

- The trend of lower credit ratings will continue.
- Changes primarily due to changing methodologies at rating agencies.
- It will take years, if ever, for ratings to return to previous levels.
- Fewer companies will have ratings high enough to meet statutes.
- There are highly rated investable foreign issuers.

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