



City of Surprise

Quarterly Performance Review

Fourth Quarter Ended December 31, 2014



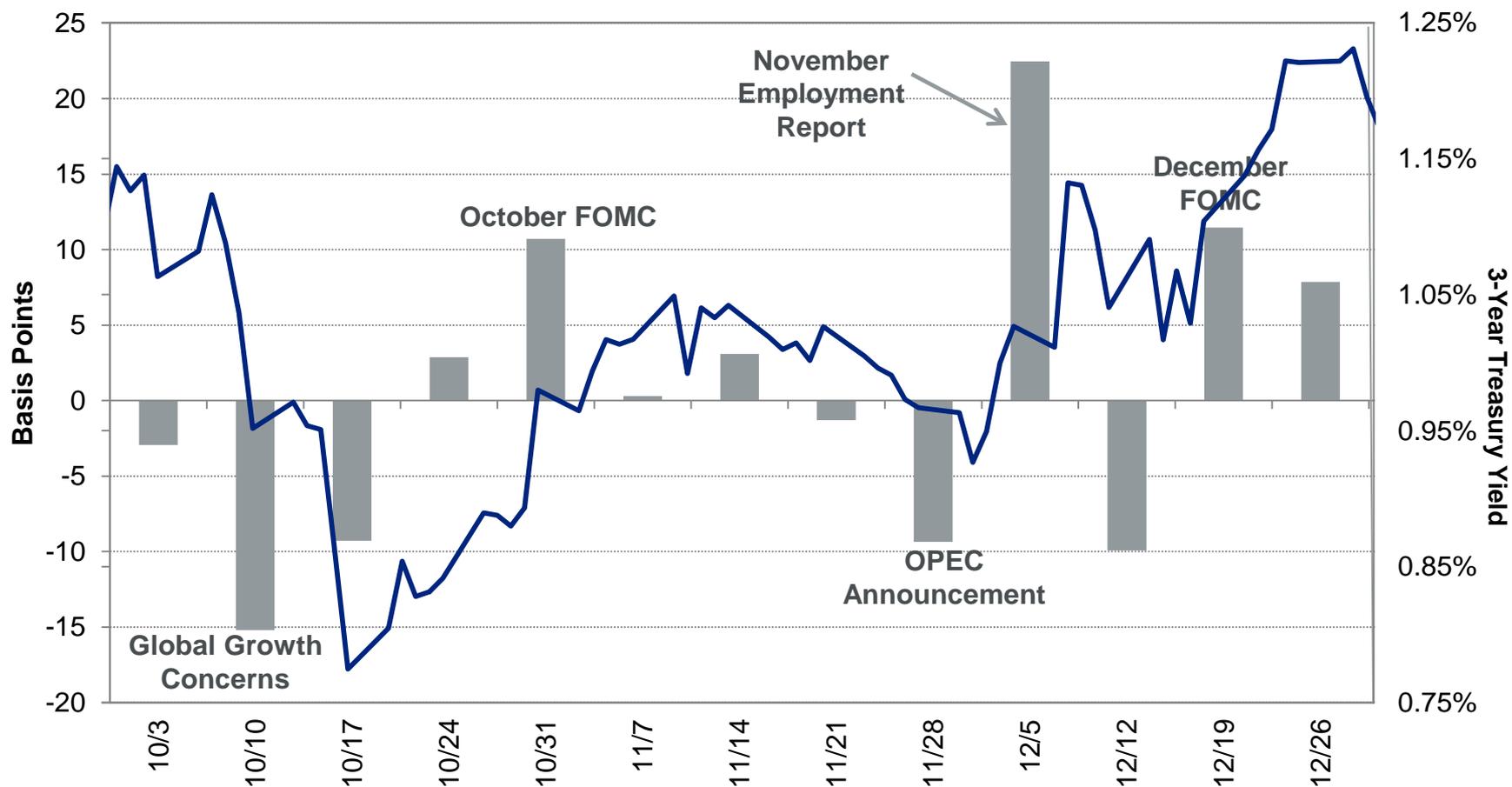
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Fourth Quarter 2014 Strategy and Recap

- Interest rates were volatile in the fourth quarter as market participants continued to weigh an improving domestic economy against declining growth prospects abroad, global deflationary pressures, and diverging policies from central banks around the world.
- Yields under five years continued their trend higher, while longer-term rates trended lower. This resulted in an overall flattening of the yield curve.
- We maintained a modestly defensive duration strategy—keeping the average portfolio maturity shorter than the benchmark—throughout the quarter in an effort to mitigate the impact that rising rates would have on the portfolio's performance.
- The yield spread between Treasuries and Agencies was narrow for most maturities and so we favored the Treasury sector for the majority of new purchases.
- The portfolio performed inline with the benchmark for the quarter on a total return basis. In addition, the yield of the portfolio increased by +0.07% (cost basis) compared to the end of the third quarter as a result of taking advantage of higher rates by redeploying shorter maturities into longer-maturities at higher yields.
 - These actions will positively impact the income generated by the portfolio.

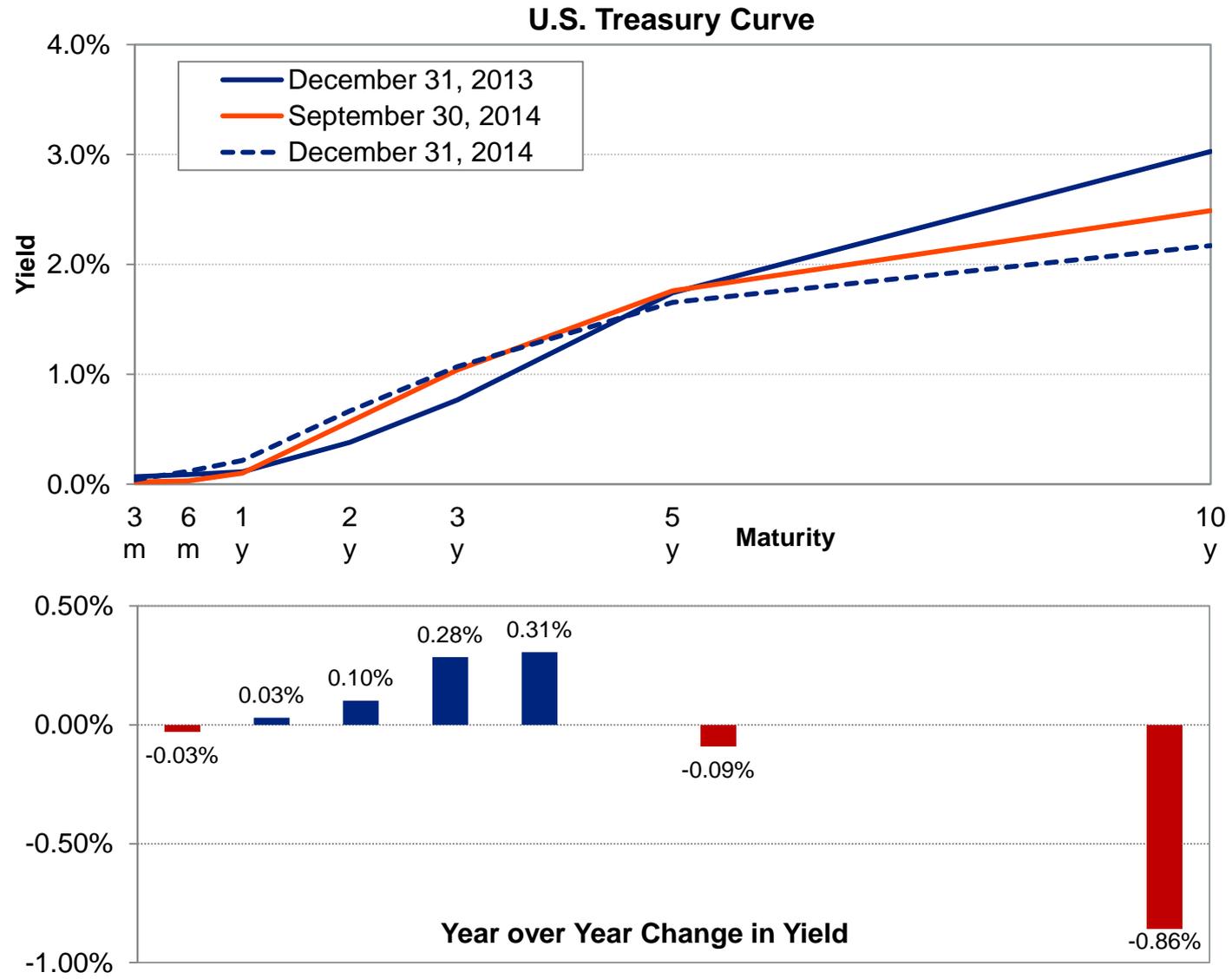
Treasury Yields Volatile in 4th Quarter

3-Year U.S. Treasury Yield and Week over Week Change in Basis Points



Source: Bloomberg.

Intermediate-Term Yields Rose; Longer Fell

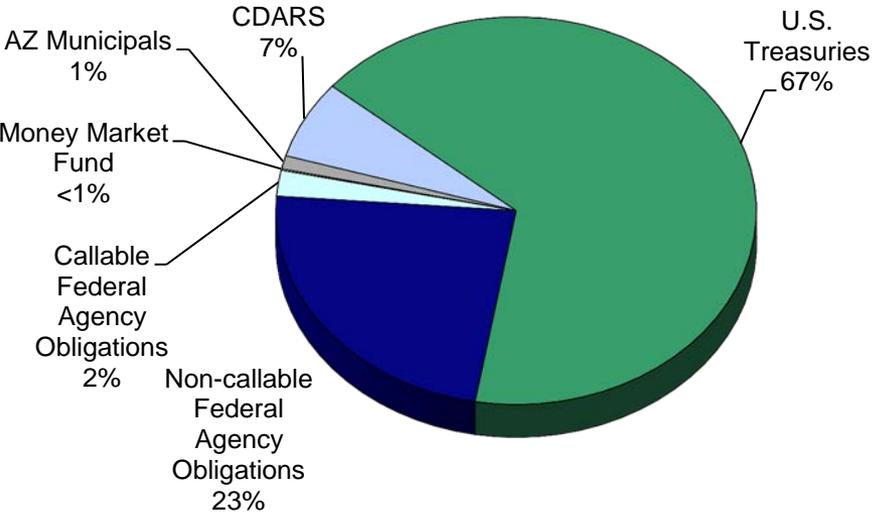


Source: Bloomberg.

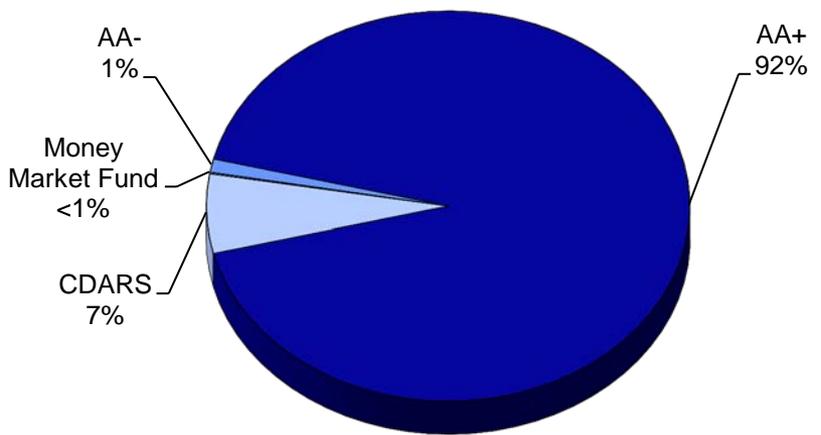
Portfolio Summary and Characteristics

Security Type ¹	December 31, 2014	Current Quarter % of Portfolio	Previous Quarter % of Portfolio
U.S. Treasury	\$51,421,430	67%	69%
Federal Agency	\$19,765,353	25%	23%
Callable Federal Agency	\$1,657,113	2%	4%
Non-callable Federal Agency	\$18,108,239	23%	19%
CDARS²	\$5,044,024	7%	7%
AZ Municipals	\$852,597	1%	1%
Wells Fargo MMF	\$94,040	<1%	<1%
Total Market Value	\$77,177,443	100%	100%

Sector Distribution



Credit Quality Distribution



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

¹ Security market values excluding accrued interest as of trade date. Note that PFM statements reflect holdings as of trade date.

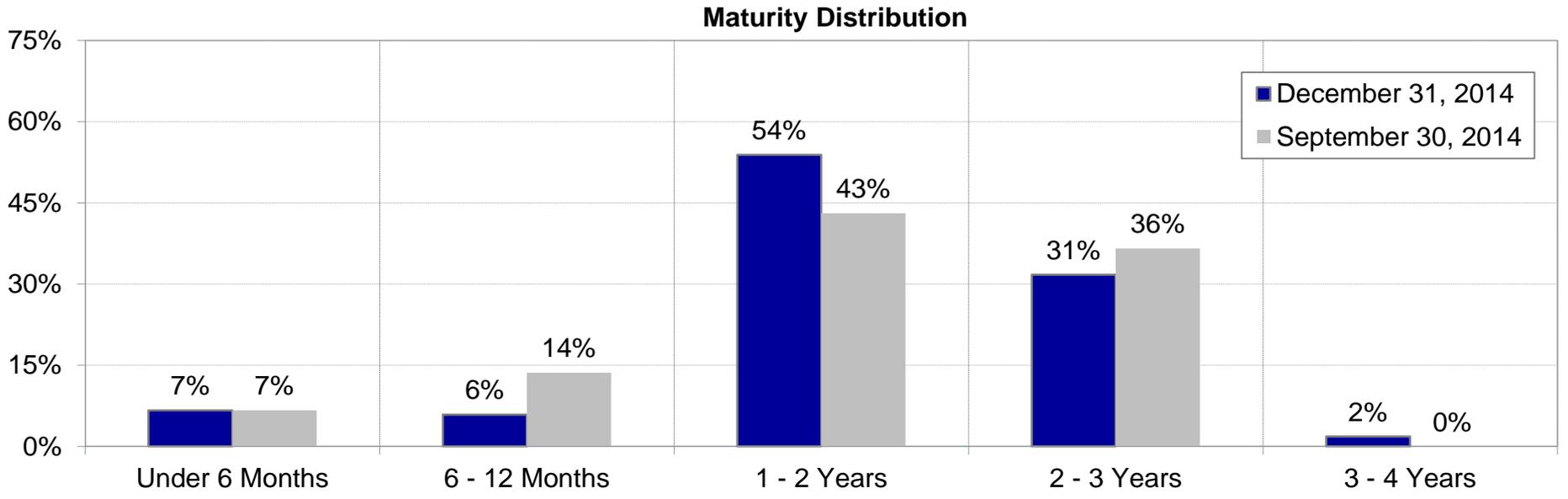
² CDARS: FDIC-insured time certificate of deposit program through Alliance Bank of AZ. CDARS funds are managed internally by the City and are not included in the PFM-managed portfolio or performance data. Value includes principal and interest tat maturity.

Maturity Summary and Key Portfolio Statistics

Maturity Distribution		
<u>Maturity Class</u>	<u>Fair Value</u> ³	<u>% of Portfolio</u>
Under 6 Months	\$5,138,064	7%
6 - 12 Months	\$4,555,377	6%
1 - 2 Years	\$41,571,808	54%
2 - 3 Years	\$24,478,821	31%
3 - 4 Years	\$1,433,372	2%
Total Market Value	\$77,177,443	100%

Key Portfolio Statistics	
Effective Duration ¹	1.77 years
Benchmark Duration ²	1.82 years
Yield at Cost	0.67%

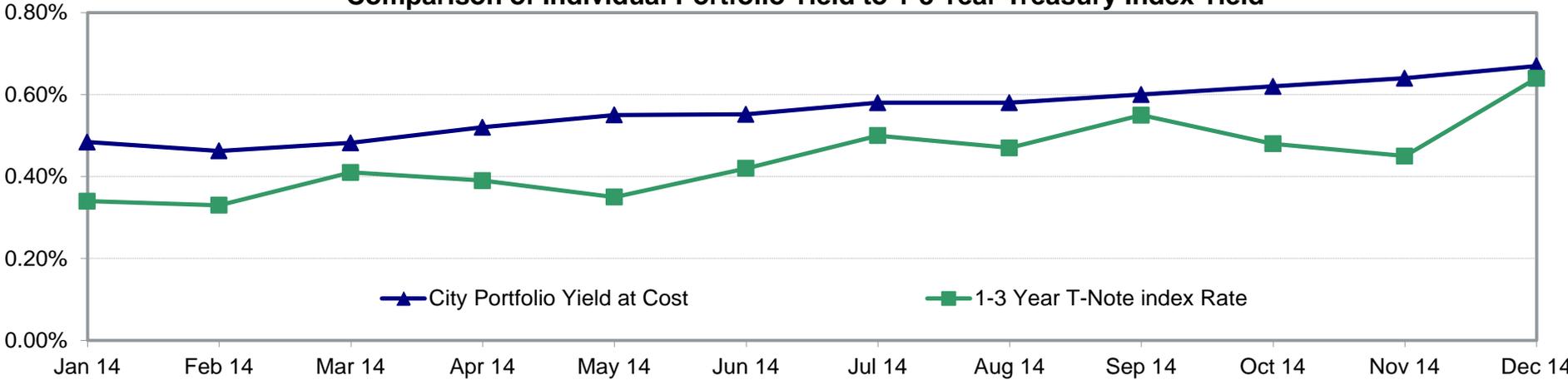
1. Portfolio statistics excludes funds invested in CDARS. Duration to worst as of 12/31/2014 was 1.76.
 2. The City's benchmark is the Bank of America /Merrill Lynch 1-3 Year U.S. Treasury Index.
 3. Security market values excluding accrued interest as of trade date. Note that PFM monthly statements reflect holdings as of trade date.



Individual Portfolio Yield Summary

Date	Month-End Market Value ^{1,2}	Duration ²	Portfolio YTM at Cost ²	1-3 Year T-Note Index Rate ³
Jan-14	\$71,692,788	1.63	0.48%	0.34%
Feb-14	\$71,765,140	1.66	0.46%	0.33%
Mar-14	\$71,619,187	1.66	0.48%	0.41%
Apr-14	\$71,700,877	1.59	0.52%	0.39%
May-14	\$71,951,724	1.67	0.55%	0.35%
Jun-14	\$71,929,301	1.72	0.55%	0.42%
Jul-14	\$72,119,635	1.77	0.58%	0.50%
Aug-14	\$72,229,199	1.70	0.58%	0.47%
Sep-14	\$71,922,824	1.72	0.60%	0.55%
Oct-14	\$72,142,335	1.70	0.62%	0.48%
Nov-14	\$72,289,236	1.71	0.64%	0.45%
Dec-14	\$72,133,418	1.77	0.67%	0.64%

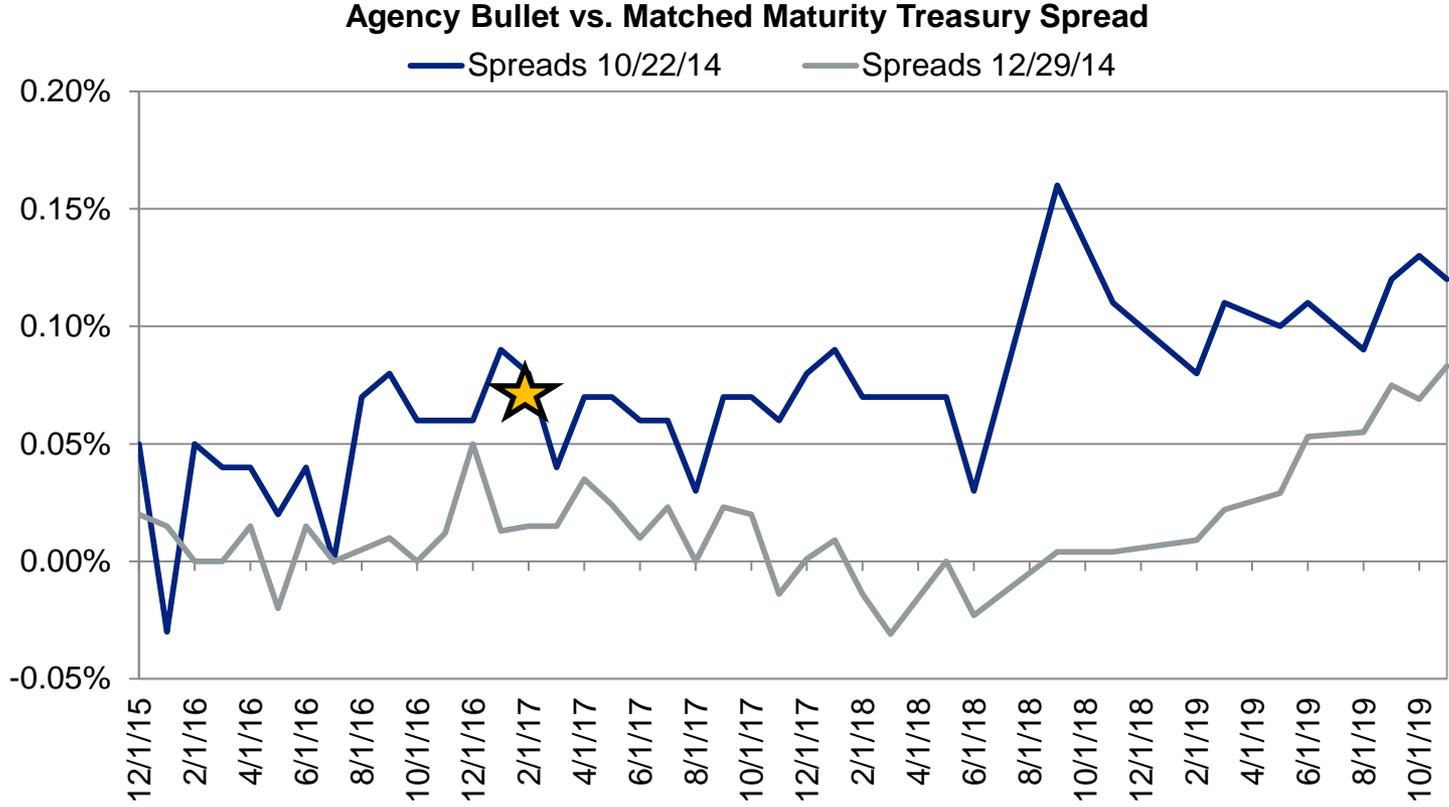
Comparison of Individual Portfolio Yield to 1-3 Year Treasury Index Yield



¹ Excludes accrued interest, CDARS. Includes balance in the custody account MMF.
² Excludes CDARS and custody money market fund.
³ Rate represents the BoA/Merrill Lynch 1-3 Year U.S. Treasury Note Index month-end yield. Source: Bloomberg.

Relative Value Analysis: Treasuries vs. Agencies

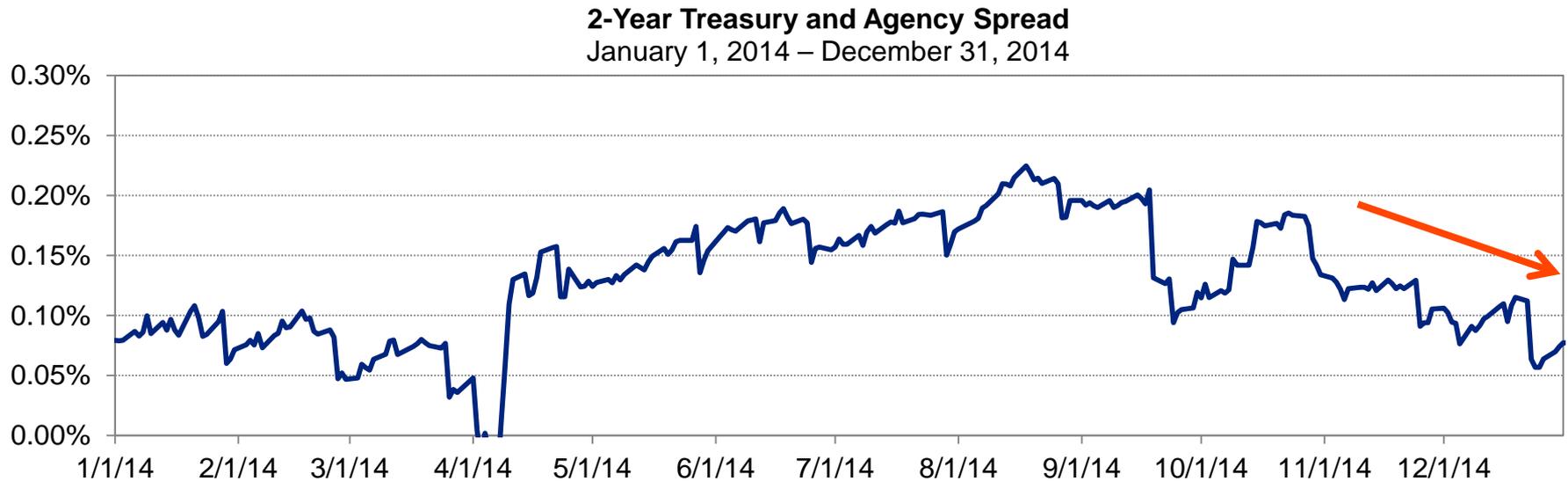
- Although, generally speaking, yield spreads between Treasuries and Agencies favor Treasuries, the relationship fluctuates and depends on the security maturity.
- When spreads are wide, we favor Agencies, as was the case in early October when we purchased a 2.3 year Agency for the City's portfolio at a spread of 0.06%.



Source: Bloomberg.

Treasury Purchases Add Yield and Duration

- Yield spreads on Federal Agency securities reversed the temporary widening that occurred in the third quarter to return to historically tight levels.



- This provided opportunities sell select shorter maturity Agency and Treasury securities to purchase longer-maturity Treasuries for their higher yields, as well as to position the portfolio's duration at its target.
- Summary of Treasuries purchased during fourth quarter:

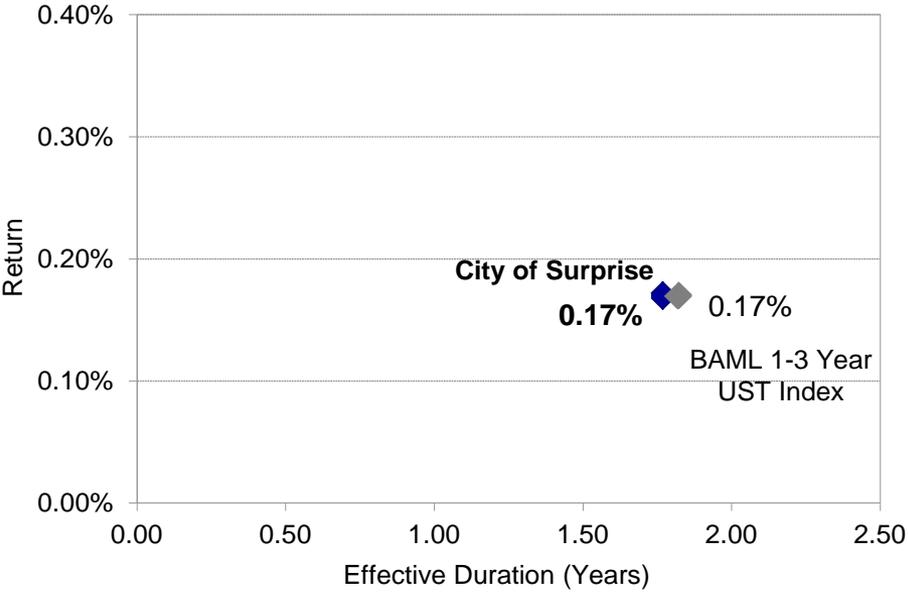
Trade Date	Security	Maturity	Par Value	Yield
11/3/14	U.S. Treasury Notes	6/30/17	\$1,500,000	0.82%
11/3/14	U.S. Treasury Notes	11/30/17	\$1,275,000	1.02%
12/4/14	U.S. Treasury Notes	6/30/17	\$2,000,000	0.84%
12/9/14	U.S. Treasury Notes	6/30/17	\$1,785,000	0.88%
12/30/14	U.S. Treasury Notes	1/31/18	\$1,445,000	1.18%

Source: Bloomberg.

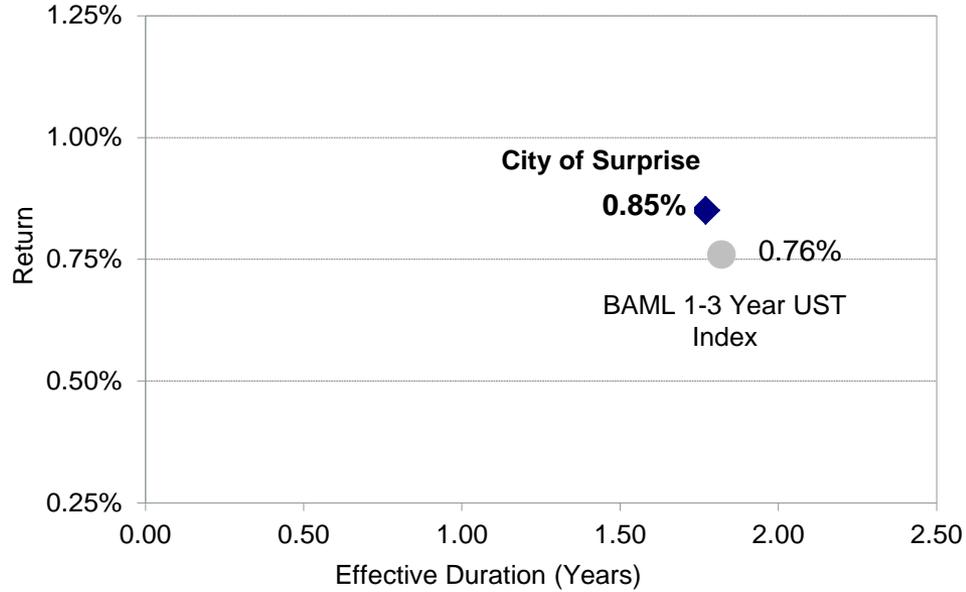
Portfolio Performance

Total Return ^{1,2,3,4,5}	Quarter Ended December 31, 2014	Past 1 Year	Past 2 Years	Past 3 Years	Since Inception	
City of Surprise	0.17%	0.63%	0.48%	0.60%	0.85%	
BAML1-3 Year UST Index	0.17%	0.62%	0.49%	0.47%	0.76%	
Effective Duration ⁴	December 31, 2014	September 30, 2014	Yields		December 31, 2014	September 30, 2014
City of Surprise	1.77	1.72	Yield at Market	0.66%	0.56%	
BAML 1-3 Year UST Index	1.82	1.84	Yield on Cost	0.67%	0.60%	

Quarter Total Return Comparison



Since Inception Total Return Comparison



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. Bank of America Merrill Lynch (BAML) Indices provided by Bloomberg Financial Markets.
 4. Excludes money market fund and CDARS/NOW Account in duration and performance computations.
 5. Inception date is June 16, 2010.

2015 Strategy and Outlook

- **We expect similar market forces in 2015:**
 - Central bank action
 - Diverging global economic activity
 - Geopolitical risk
- **Closely monitor movements of the FOMC:**
 - Expect first rate hike in 2015
 - Timing uncertain—possibly late summer to early fall
 - Continue to employ conservative duration management
- **Treasury Agency spreads are very narrow:**
 - Prefer Treasuries where yields are narrow
 - Look to swap between sectors as spreads fluctuate to safely increase earnings



Managed Account Detail of Securities Held

For the Month Ending **December 31, 2014**

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 12/31/2010 2.125% 12/31/2015	912828PM6	1,500,000.00	AA+	Aaa	07/02/14	07/07/14	1,540,839.84	0.28	88.05	1,527,519.00	1,527,304.50
US TREASURY NOTES DTD 01/31/2011 2.000% 01/31/2016	912828PS3	1,135,000.00	AA+	Aaa	07/30/14	07/31/14	1,163,641.02	0.31	9,499.46	1,155,663.06	1,155,216.62
US TREASURY NOTES DTD 01/31/2011 2.000% 01/31/2016	912828PS3	3,350,000.00	AA+	Aaa	01/30/13	01/31/13	3,507,162.11	0.42	28,038.04	3,406,884.91	3,409,670.20
US TREASURY NOTES DTD 05/02/2011 2.000% 04/30/2016	912828QF0	2,150,000.00	AA+	Aaa	05/13/13	05/14/13	2,251,705.08	0.39	7,364.64	2,195,767.59	2,195,352.10
US TREASURY NOTES DTD 05/02/2011 2.000% 04/30/2016	912828QF0	3,800,000.00	AA+	Aaa	03/28/13	04/01/13	3,988,070.31	0.38	13,016.57	3,881,398.51	3,880,157.20
US TREASURY NOTES DTD 05/31/2011 1.750% 05/31/2016	912828QP8	3,280,000.00	AA+	Aaa	05/30/13	05/31/13	3,401,334.38	0.51	5,046.15	3,337,337.09	3,339,705.84
US TREASURY NOTES DTD 06/30/2009 3.250% 06/30/2016	912828KZ2	1,860,000.00	AA+	Aaa	05/23/13	05/28/13	2,020,642.97	0.43	166.99	1,938,080.33	1,935,852.66
US TREASURY NOTES DTD 08/01/2011 1.500% 07/31/2016	912828OX1	1,925,000.00	AA+	Aaa	02/04/14	02/07/14	1,973,500.98	0.48	12,083.56	1,955,986.34	1,954,475.60
US TREASURY NOTES DTD 08/01/2011 1.500% 07/31/2016	912828OX1	3,420,000.00	AA+	Aaa	06/02/14	06/05/14	3,495,881.25	0.46	21,467.93	3,475,771.72	3,472,367.04
US TREASURY NOTES DTD 08/31/2011 1.000% 08/31/2016	912828RF9	2,030,000.00	AA+	Aaa	09/12/13	09/13/13	2,038,246.87	0.86	6,897.51	2,034,645.19	2,045,225.00
US TREASURY NOTES DTD 10/31/2011 1.000% 10/31/2016	912828RM4	2,600,000.00	AA+	Aaa	05/07/14	05/08/14	2,622,648.44	0.65	4,453.04	2,616,746.37	2,618,688.80
US TREASURY NOTES DTD 10/31/2011 1.000% 10/31/2016	912828RM4	3,420,000.00	AA+	Aaa	06/02/14	06/05/14	3,455,001.56	0.57	5,857.46	3,446,690.09	3,444,582.96
US TREASURY NOTES DTD 11/30/2009 2.750% 11/30/2016	912828MA5	2,310,000.00	AA+	Aaa	10/31/13	11/01/13	2,457,352.73	0.65	5,584.62	2,401,847.47	2,401,496.79
US TREASURY NOTES DTD 11/30/2009 2.750% 11/30/2016	912828MA5	3,600,000.00	AA+	Aaa	12/03/13	12/04/13	3,831,328.13	0.58	8,703.30	3,748,434.73	3,742,592.40



Managed Account Detail of Securities Held

For the Month Ending **December 31, 2014**

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 01/31/2012 0.875% 01/31/2017	912828SC5	1,175,000.00	AA+	Aaa	07/30/14	07/31/14	1,175,688.48	0.85	4,302.48	1,175,574.21	1,178,396.93
US TREASURY NOTES DTD 03/31/2012 1.000% 03/31/2017	912828SM3	2,780,000.00	AA+	Aaa	03/24/14	03/25/14	2,783,475.00	0.96	7,102.75	2,782,595.63	2,791,728.82
US TREASURY NOTES DTD 05/31/2012 0.625% 05/31/2017	912828SY7	2,385,000.00	AA+	Aaa	06/02/14	06/05/14	2,369,721.09	0.84	1,310.44	2,372,630.51	2,371,398.05
US TREASURY NOTES DTD 07/02/2012 0.750% 06/30/2017	912828TB6	1,500,000.00	AA+	Aaa	11/03/14	11/04/14	1,497,246.09	0.82	31.08	1,497,410.28	1,494,375.00
US TREASURY NOTES DTD 07/02/2012 0.750% 06/30/2017	912828TB6	1,785,000.00	AA+	Aaa	12/09/14	12/10/14	1,779,142.97	0.88	36.98	1,779,279.97	1,778,306.25
US TREASURY NOTES DTD 07/02/2012 0.750% 06/30/2017	912828TB6	2,000,000.00	AA+	Aaa	12/04/14	12/05/14	1,995,625.00	0.84	41.44	1,995,750.50	1,992,500.00
US TREASURY NOTES DTD 11/30/2012 0.625% 11/30/2017	912828UA6	1,275,000.00	AA+	Aaa	11/03/14	11/04/14	1,259,660.16	1.02	700.55	1,260,444.46	1,258,664.70
US TREASURY NOTES DTD 01/31/2013 0.875% 01/31/2018	912828UJ7	1,445,000.00	AA+	Aaa	12/30/14	12/31/14	1,431,735.35	1.18	5,291.13	1,431,746.91	1,433,372.09
Security Type Sub-Total		50,725,000.00					52,039,649.81	0.62	147,084.17	51,418,204.87	51,421,429.55
Municipal Bond / Note											
MESA, AZ T/E GO 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	8,450.00	850,174.34	852,596.55
Security Type Sub-Total		845,000.00					878,200.05	0.77	8,450.00	850,174.34	852,596.55
Federal Agency Bond / Note											
FHLB (EX-CALLABLE) GLOBAL NOTES DTD 12/30/2013 0.375% 12/30/2015	3130A0GK0	2,175,000.00	AA+	Aaa	12/16/13	12/30/13	2,174,238.75	0.39	22.66	2,174,619.68	2,175,476.33
FEDERAL HOME LOAN BANK GLOBAL NOTES DTD 01/24/2014 0.375% 02/19/2016	3130A0SD3	1,925,000.00	AA+	Aaa	02/04/14	02/07/14	1,925,115.50	0.37	2,646.88	1,925,064.39	1,924,382.08



Managed Account Detail of Securities Held

For the Month Ending **December 31, 2014**

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 NOTES DTD 08/07/2014 0.500% 09/28/2016	3130A2T97	1,485,000.00	AA+	Aaa	08/06/14	08/07/14	1,481,658.75	0.61	1,918.13	1,482,278.89	1,481,063.27
FNMA NOTES DTD 08/19/2011 1.250% 09/28/2016	3135G0CM3	2,545,000.00	AA+	Aaa	10/02/13	10/03/13	2,583,760.35	0.73	8,218.23	2,567,707.64	2,570,979.36
FHLMC NOTES DTD 01/21/2014 0.875% 02/22/2017	3137EADT3	3,320,000.00	AA+	Aaa	10/08/14	10/09/14	3,326,540.40	0.79	10,409.58	3,325,919.49	3,325,381.72
FNMA NOTES DTD 03/01/2012 1.125% 04/27/2017	3135G0JA2	3,400,000.00	AA+	Aaa	09/03/14	09/04/14	3,416,252.00	0.94	6,800.00	3,414,285.00	3,418,965.20
FHLB GLOBAL NOTE (CALLABLE) DTD 04/28/2014 1.625% 04/28/2017	3130A1LJ5	1,650,000.00	AA+	Aaa	04/03/14	04/28/14	1,668,315.00	1.25	4,692.19	1,655,959.97	1,657,113.15
FREDDIE MAC GLOBAL NOTES DTD 06/25/2012 1.000% 07/28/2017	3137EADJ5	2,115,000.00	AA+	Aaa	08/13/14	08/14/14	2,117,305.35	0.96	8,988.75	2,117,013.52	2,114,206.88
FNMA NOTES DTD 08/25/2014 1.000% 09/27/2017	3135G0ZL0	1,100,000.00	AA+	Aaa	08/21/14	08/25/14	1,096,073.00	1.12	2,872.22	1,096,509.66	1,097,784.60
Security Type Sub-Total		19,715,000.00					19,789,259.10	0.79	46,568.64	19,759,358.24	19,765,352.59
Managed Account Sub-Total		71,285,000.00					72,707,108.96	0.67	202,102.81	72,027,737.45	72,039,378.69
Securities Sub-Total		\$71,285,000.00					\$72,707,108.96	0.67%	\$202,102.81	\$72,027,737.45	\$72,039,378.69
Accrued Interest											\$202,102.81
Total Investments											\$72,241,481.50

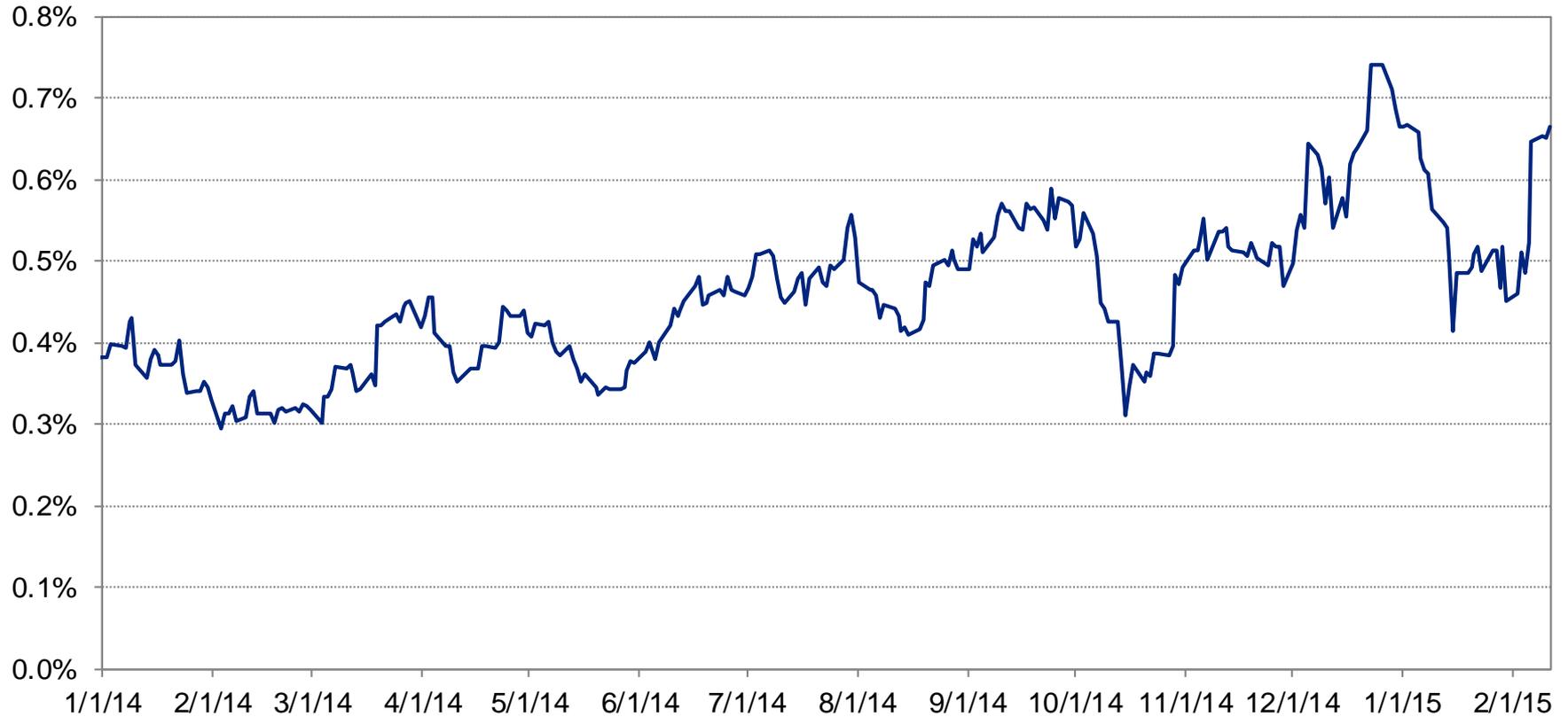


Economic Update

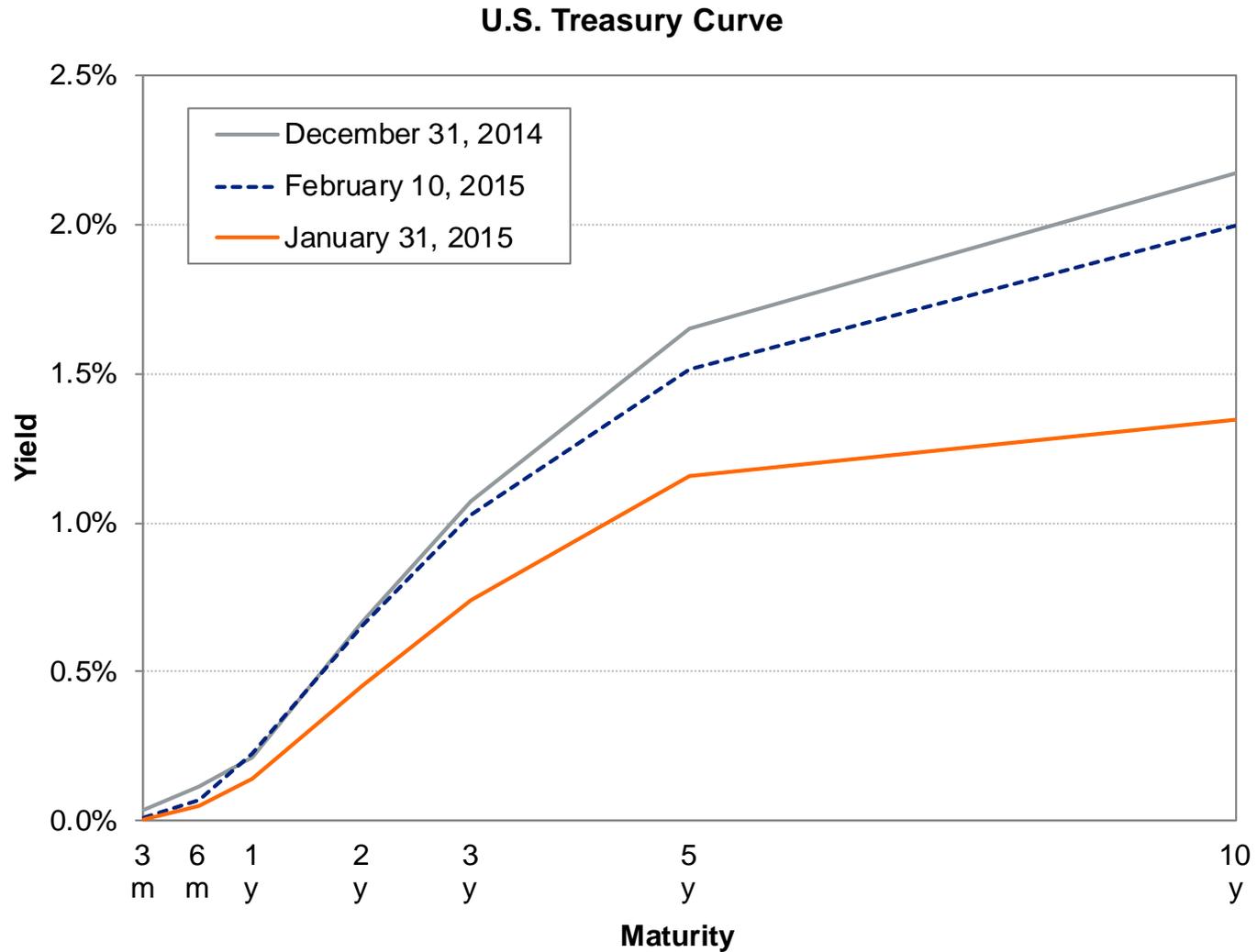
Yields Fall to Start 2015 But Have Bounced Back

2-Year Treasury Yield

January 1, 2014 – February 11, 2015



Yield Curve Update

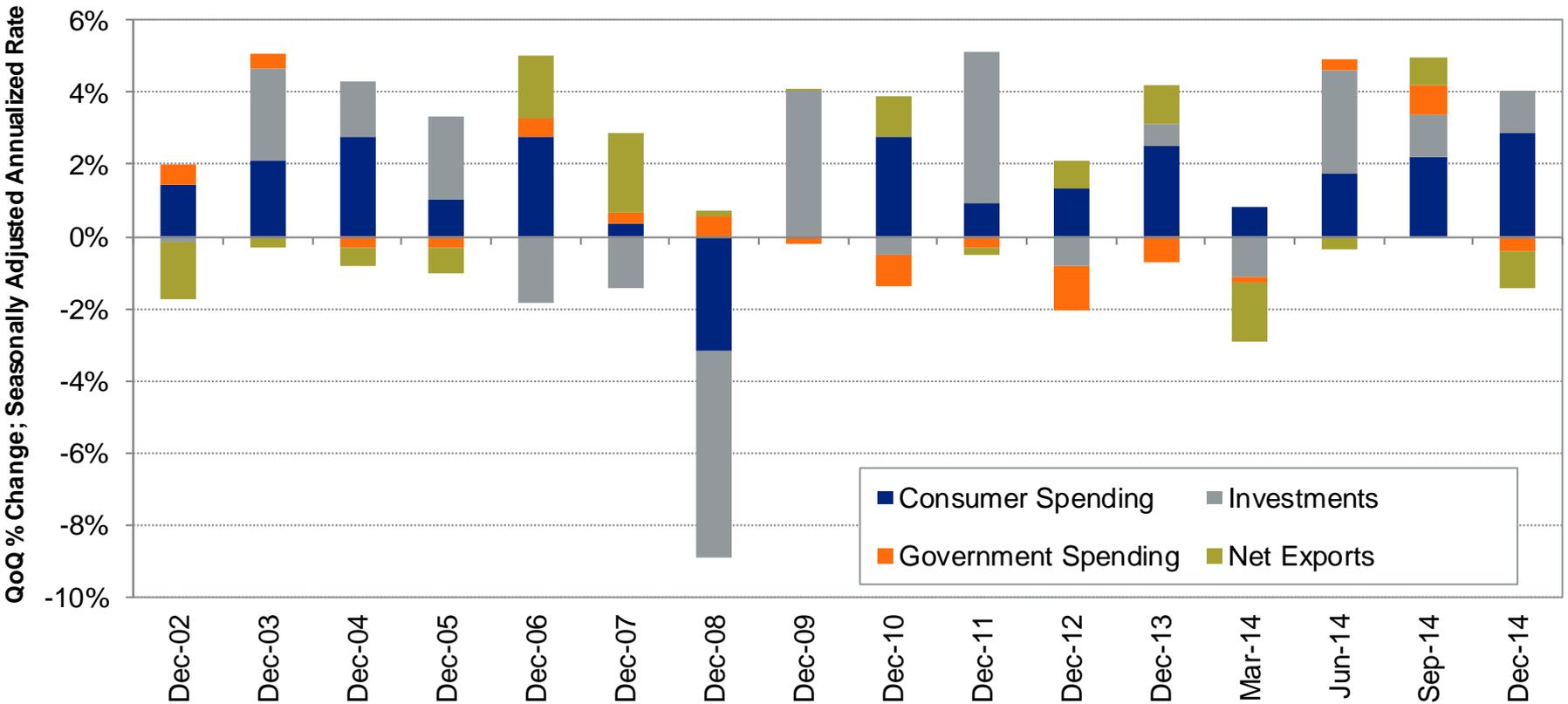


Source: Bloomberg.

U.S. Economic Growth Slows in 4th Quarter

- U.S. GDP slowed to a rate of 2.6% (advanced estimate) from third quarter's 5% rate, which was the strongest in a decade.
- The slowdown in fourth quarter's GDP growth was largely due to weak business spending, lower defense spending, and a widened U.S. trade gap that offset the fastest pace of growth in consumer spending since 2006.

U.S. GDP Composition
Fourth Quarter 2002 – Fourth Quarter 2014

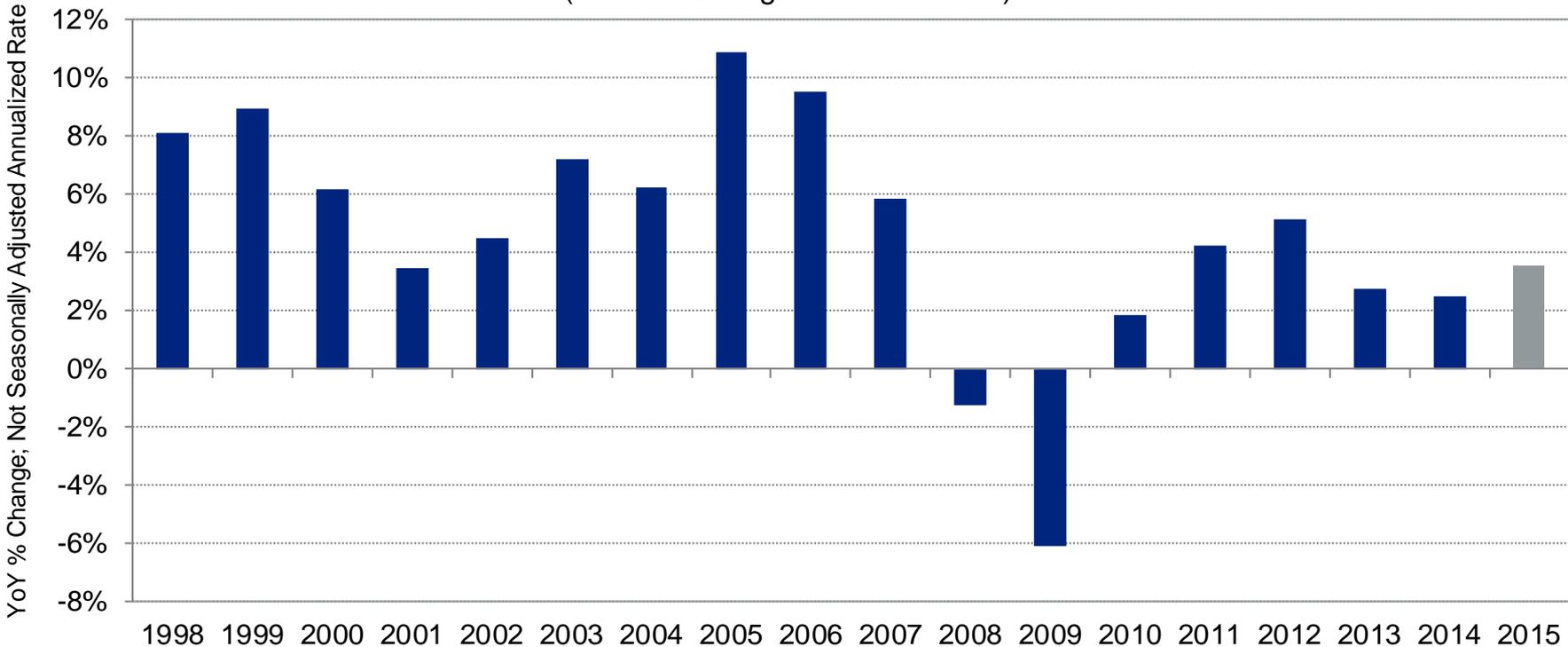


Source: Bureau Of Economic Analysis.

Arizona Growth Expected to Pick Up in 2015

- Arizona's growth in 2014 is expected to come in at 2.5%, on pace with the U.S. In 2015 however, projections for Arizona growth exceeds U.S. projections, at 3.5% versus 3.1%.
- Growth in Arizona is supported by broad based job gains, the housing-market recovery, and population growth.

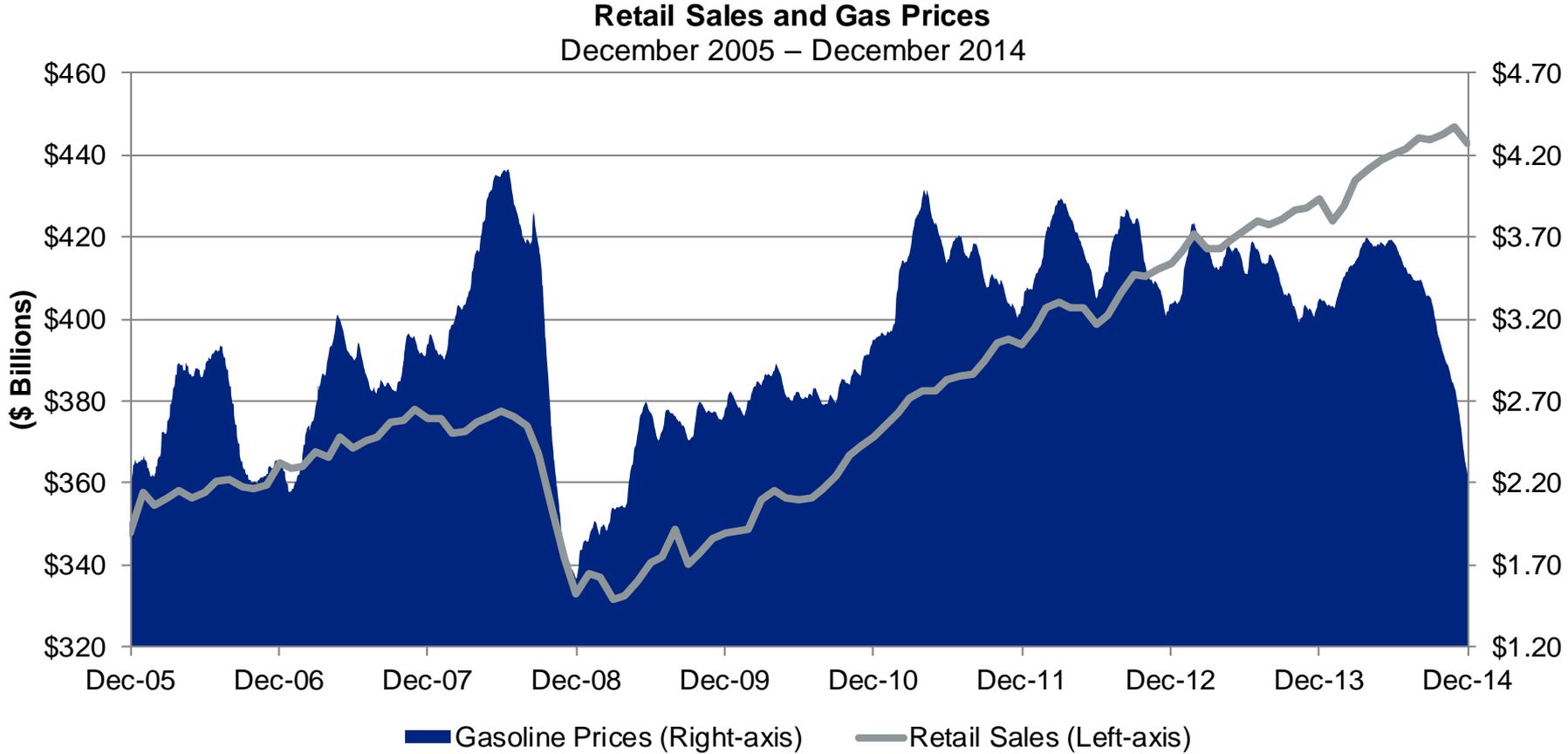
Arizona GDP 1998 - 2014
(Percent Change Year over Year)



Source: Bureau Of Economic Analysis and AZ Central; 2014 is preliminary and the 2015 projection is by BMO Capital Market.

Retail Sales Dip Despite Lower Gasoline Prices

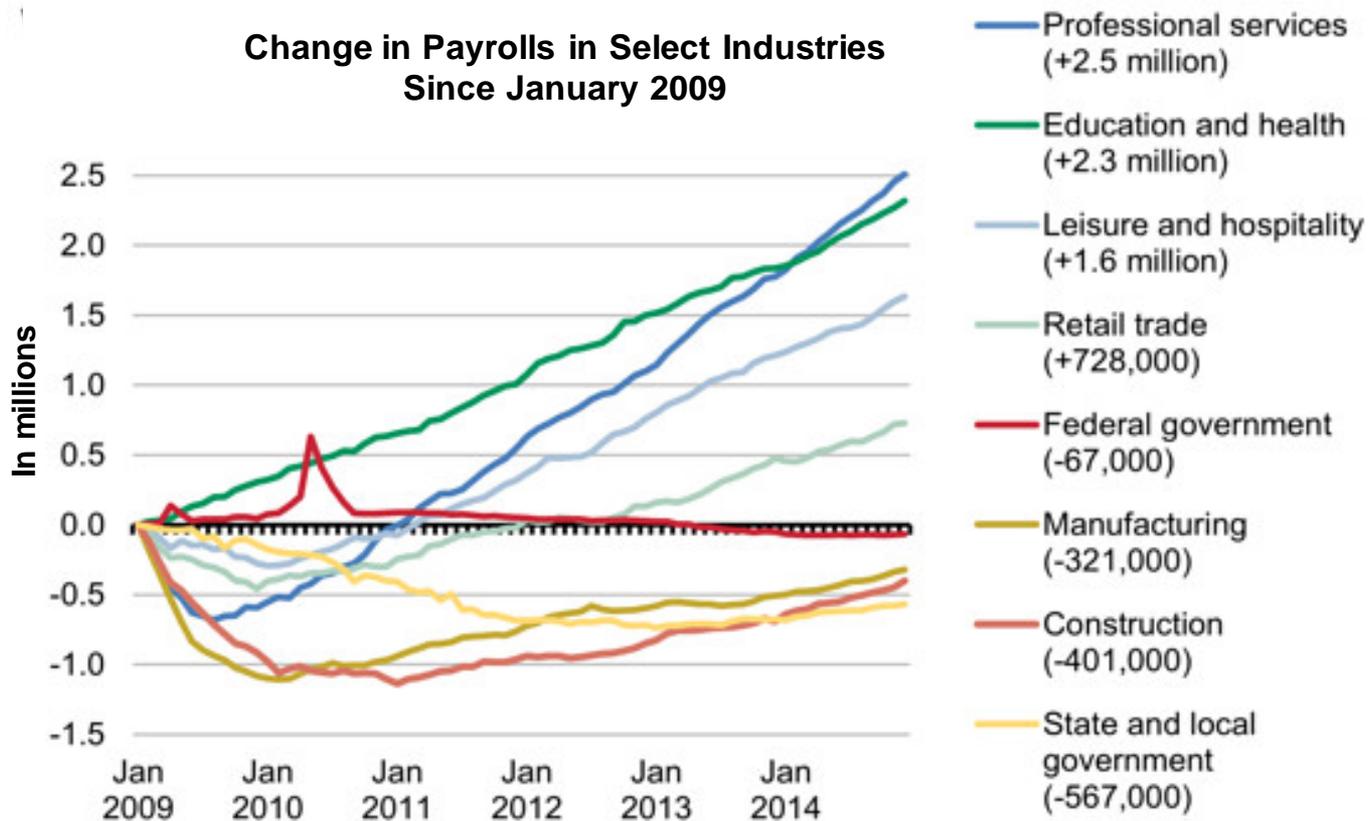
- U.S. retail sales pulled back in December, reflecting consumer caution despite falling gasoline prices. The tumble in U.S. gas prices over the last 6 months have boosted consumer confidence, but had a less consistent impact on consumer spending.



Source: Bloomberg.

Winning and Losing Industries

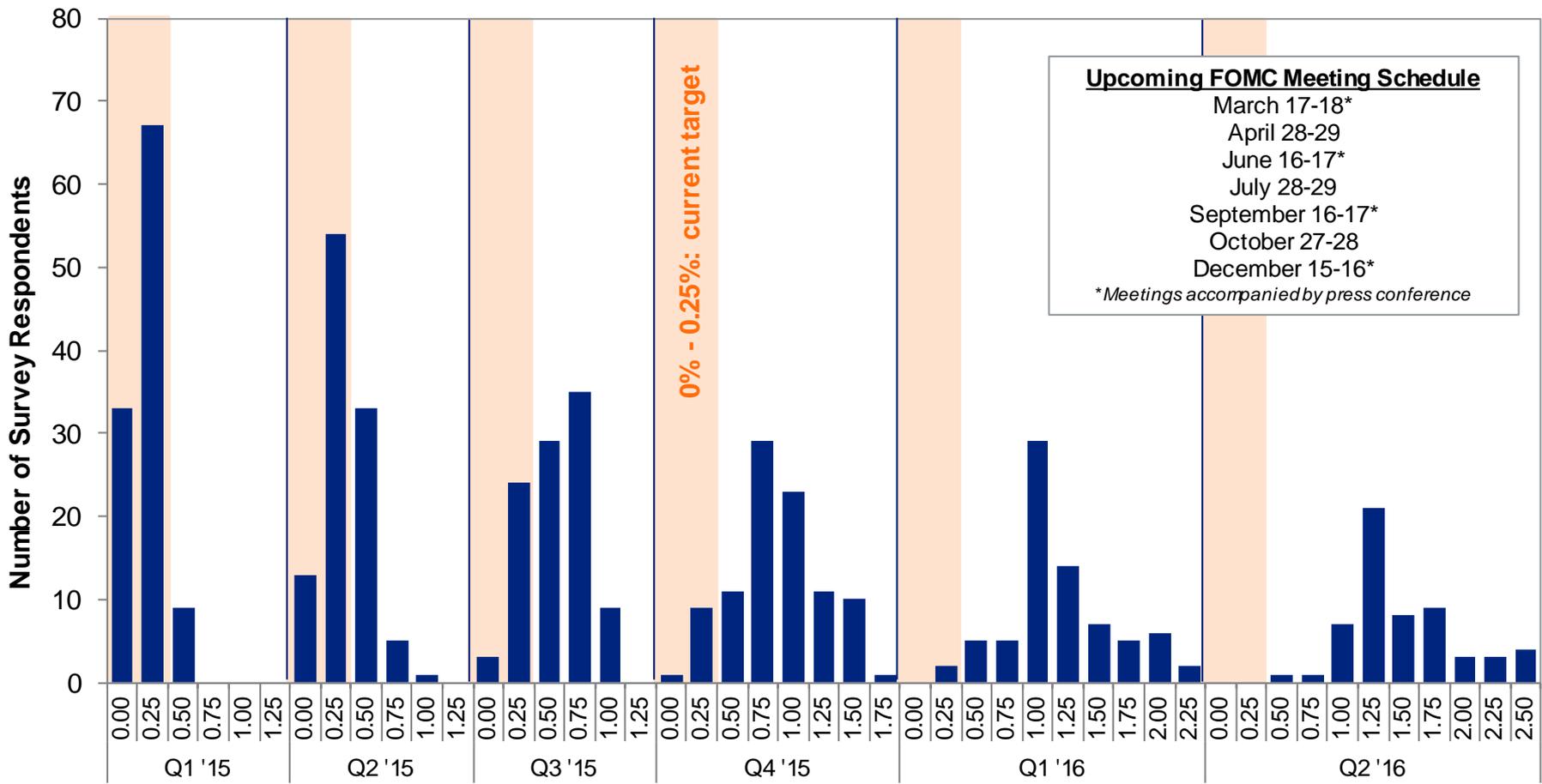
- U.S. job creation added 257,000 net new jobs in January, and the unemployment rate rose to 5.7% from the prior month's 5.6% as more Americans began searching for jobs.



Source: Labor Department, WSJ.com.

Fed Funds Rate Survey

Economist Surveys: Federal Funds Rate



Source: Bloomberg.

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