4th Annual Meeting
King County Investment Pool

January 24, 2012

King County

Today's Agenda

- Introduction – Ken Guy (5 minutes)
- Fourth Quarter 2011 Investment Pool Review – John Molloy (15 min)
- Economic forecast – Tom Goodwin (15 minutes)
- Investment Pool Infrastructure Improvements Update – Scott Matheson (5 min)
- Investment Pool Advisory Committee (IPAC) Report – Linda Glenicki (10 min)
- Basic Investment Strategies – Mike Smith (20 min)
- Credit Analysis – Christine Denis (10 min)
- Additional Questions and closing(10 min)

Quarterly Portfolio Review
King County Investment Pool

December 31, 2011

Presented by
John Molloy, CFA, Managing Director
Robert Cheddar, CFA, Managing Director
PFM Asset Management LLC

Executive Summary

Purpose, Scope and Approach	• PFM Asset Management LLC (“PFM”) prepared this report to update our ongoing analysis and to address any Investment Pool developments since PFM’s previous formal review in September 2011. • Our approach included a detailed portfolio analysis and investment policy compliance review, based on the County’s revised investment policy. • Our analysis was based on the Investment Pool’s holdings as of December 31, 2011, with reference to holdings in past periods. • The review encompasses all current investments in the County’s Investment Pool.
Investment Program and Portfolio Review	• PFM reviewed the County’s portfolio with respect to Investment Policy Compliance, Sector Allocation, Issuer Concentration, Credit Quality, and Maturity Distribution. • As with previous reports, the County’s Investment Pool appears to provide ample liquidity, is well diversified, and is of sound credit quality. All holdings are investment grade, rated at least A-1, and pose minimal risk to principal. As of December 31, 2011, the Pool had no direct corporate exposure; through its LGIP holdings, approximately 7.5% of the County’s portfolio is indirectly invested in corporate obligations (repurchase agreements).
Observations	• The portfolio possesses high credit quality. All securities are either explicitly guaranteed or carry a high level of support by the U.S. Government (U.S. Treasury and federal agency) and/or carry a high level of liquidity (Washington State LGIP). • Potential market risk has decreased over the past quarter as the total portfolio’s weighted average maturity (“WAM”) was shortened by 19 days, from 235 days on September 30th to 216 days on December 31st. The pool’s level of market risk remains consistent with the objectives of the County’s Pool and other investment programs with similar objectives, and is in keeping with the County’s cash flow expectations. • The Pool appears to provide adequate liquidity. Approximately 53% of the portfolio is held in securities that mature within the next six months. Of these securities, nearly 23% will either mature or may be called within the next month. Additionally, the Pool’s investments are highly marketable, mostly U.S. Treasury and federal agency holdings, and actively traded in the market – all of which add to the Pool’s liquidity. • Eighty-three percent of the Pool’s holdings are either explicitly guaranteed (U.S. Treasury) or implicitly supported (federal agency) by the U.S. government. If the securities held in the Washington State LGIP are taken into account, of which the Pool has allocated 11% of its holdings, this number increases from 83% to 91% of the Pool’s holdings. • The Pool’s credit exposure continues to be limited and well diversified. Corporate exposure is contained in the pool’s Washington State LGIP holdings. Less than 8% of the County pool’s assets are exposed to corporate obligations through the State LGIP. • In keeping with normal seasonal cash flow patterns, total Pool assets increased by $203 million over the quarter from $4,421 million on September 30, 2011 to $4,624 million on December 31, 2011. This net increase has been allocated predominantly to Federal Agency securities.

Portfolio Review

I. Investment Policy Compliance

II. Sector Allocation

- U.S. Treasuries
- Federal Agencies
- LGIP and Cash Equivalents

III. Issuer Concentration

IV. Overall Credit Quality

V. Maturity Distribution

I. Investment Policy Compliance – Investment Policy Summary

- The Investment Policy summary is based on the current Investment Policy for the County Investment Pool, dated July 2011.

Type	Maximum Portfolio Allocation	Issuer Restrictions	Credit Ratings	Maturity Restrictions
Repurchase Agreement	40%	5% per investment dealer; Firm must adopt a master repurchase agreement with the County. Maximum 5% per issuer applied across investment type.	Short-term credit ratings of at least A-1 / P-1 from at least 2 rating agencies. Must have a minimum asset and capital size of $25 billion in assets and $350 million in capital Collateral limited to U.S. Treasury and Agency securities.	60 days or less
Reverse Repurchase Agreement	20%	5% per investment dealer; Firm must adopt a master repurchase agreement with the County.	Short-term credit ratings of at least A-1 / P-1 from at least 2 rating agencies. Must have a minimum asset and capital size of $25 billion in assets.	6 months or less
Local Government Investment Pool ("LGIP")	25%	State of Washington LGIP	N/A	N/A
U.S. Treasuries	100%	None	N/A	Up to 5 years
U.S. Agencies	100% 20% Floating/Variable	35% exposure to any single Agency	Must carry the highest short-term or long-term credit ratings. U.S. Agencies category includes Floating and Variable Rate Notes. The use of floating and variable rate notes (FRNs and VRNs) issued by Federal Agencies of the U.S. Government is allowable in the management of the Pool provided that the following criteria are met: 1) The final maturity (at the time of purchase) is no greater than two years; 2) The rate on the FRN/VRN resets no less frequently than quarterly; 3) The rate on the FRN/VRN resets with a frequency that produces a close tracking with money market rates; 4) The FRN/VRN is indexed to a money market rate such as Federal Funds, the 3-month Treasury Bill, LIBOR, or Prime Rate which correlates very highly with overall changes in money market rates even under wide swings in interest rates; 5) Any cap on the interest rate is at least 15.00% (1500 basis points) higher than the coupon at time of purchase	Up to 5 years

I. Investment Policy Compliance – Investment Policy Summary cont'd

Type	Maximum Portfolio Allocation	Issuer Restrictions	Credit Ratings	Maturity Restrictions
Bankers' Acceptances	25%	2.5% of portfolio; secondary market purchases only. Maximum 5% per issuer applies across investment type.	Must carry highest ratings of any two nationally recognized rating agencies.	Up to 180 days
Certificates of Deposit	25%	2.5% of portfolio; must be a public depository in the State of Washington. Maximum 5% per issuer applies across investment type.	100% collateralization Moody's P-3, S&P A-3, or Fitch F-3 or better, and a Safe & Sound rating of 3 or better. No new deposits will be placed with institutions that are on credit watch or predictive indicator "negative." Those institutions not meeting the minimum credit requirements may receive deposits up to the FDIC or federally guaranteed amounts.	Up to 1 year
Commercial Paper	25%	2.5% of portfolio; secondary market purchases only. Maximum 5% per issuer applies across investment type.	Must carry highest ratings of any two nationally recognized rating agencies at time of purchase. Purchases with greater than 100 days maturity must have an issuer long-term rating of one of the two highest ratings of a nationally recognized rating agency. State law requires that Commercial Paper be purchased only from dealers.	180 days
General Obligation Municipal Bonds	20%	2.5%; bond issues by pool participants must be purchased on the secondary market only.	At time of purchase, bond must have one of the three highest credit ratings of a nationally recognized credit rating agency	5 years
Mortgage-Backed Securities	25%	Must be issued by Federal Agencies of the United States. Investments in MBS will count toward the total that can be invested on any one agency as described in U.S. Agencies above.	Must pass the Federal Financial Institutions Examination Council ("FFIEC") suitability test, which banks use to determine lowest risk securities. If rated by Fitch, must have rating between V1 and V5	5 year average life at time of purchase
Bank Notes	20%	2.5% of portfolio. Maximum 5% per issuer applies across investment type.	Bonds must be rated "A" or better by two nationally recognized rating agencies or guaranteed by an agency of the federal government	5 years

- When combined, Bankers' Acceptances, Certificates of Deposit, Commercial Paper, and Term Repos (greater than 7 days),and Bank Notes not to exceed 50% of the Pool assets.
- The Pool will maintain an effective duration of less than 1.5 years.
- The portfolio will maintain at least 40% of its total value in securities having a maturity of 12 months or less.

I. Investment Policy Compliance – County Investment Pool

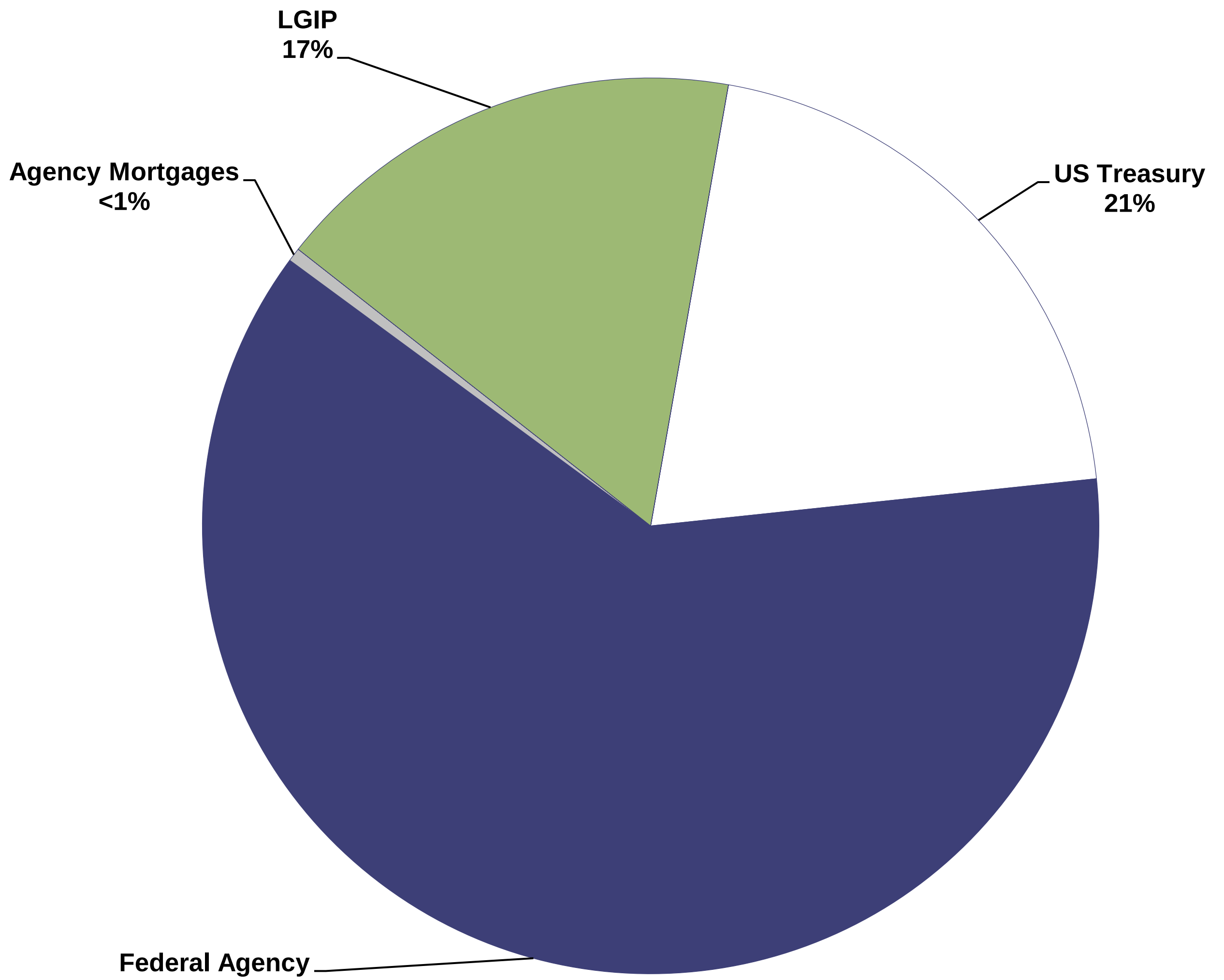
Topic	Observations
Sector Allocation	• All sector allocations fall within the limits set forth by the County's Investment Policy Statement. The Pool is predominantly invested in securities which are either explicitly guaranteed or carry a high level of support by the U.S. government. The County increased its allocation to the federal agency sector, from 50.7% on September 30th to 61.8% on December 31st , reducing its U.S. Treasury holdings by approximately 8%, from 28.3% on September 30th to 20.5% on December 31st. The County's allocation to the Washington LGIP remained approximately constant both on a percentage and dollar bases. As of quarter end the pool did not hold repurchase agreements but maintained adequate liquidity through the Washington State LGIP.
Credit Quality	• Securities held by the County are of very high quality. A majority of securities are rated AA+ and are guaranteed or supported by the U.S. government. Approximately 83% of holdings fall into this category. The remaining holdings are allocated to the Washington State LGIP (17%), which is not rated, but 47.5% of the Washing State LGIP is invested in U.S. Treasury or Federal Agency securities. • We are aware that the County is addressing potential technical changes to the credit rating language of the Investment Policy stemming largely from the Standard & Poor's downgrade of the U.S. Treasury and Federal Agencies.
Maturity Distribution	• All maturities fall within the maturity limits set forth in the County's Investment Policy. Maturities range from 1-day (the Washington State LGIP) to a Fannie Mae mortgage-backed security with a weighted average life of 4.1 years. Aside from agency mortgages, the longest maturity is a December 2016 Federal Farm Credit Bank note set to mature in 5 years with a duration of approximately 4.78 years. However, it is highly likely that this security will be called in June 2012.

Security Type	Market Value($)	Allocation Percentage	Within Policy Limits	Max Maturity Held	Within Policy Limits
Cash Equivalents	0	0.00%	✓	N/A	✓
Commercial Paper	0	0.00%	✓	N/A	✓
Repurchase Agreements	0	0.00%	✓	N/A	✓
LGIP	794,516,507	17.18%	✓	1 day	✓
Federal Agencies	2,857,361,000	61.78%	✓	5.0 years	✓
Agency Mortgages	22,815,304	0.49%	✓	4.1 years (WAL)	✓
Certificates of Deposit	0	0.00%	✓	N/A	✓
Municipal Bonds	0	0.00%	✓	N/A	✓
U.S. Treasury	950,000,000	20.54%	✓	3.0 years	✓

**Percentages may not total to 100% due to rounding.*

II. Sector Allocation

Sector Diversification
as of December 31, 2011



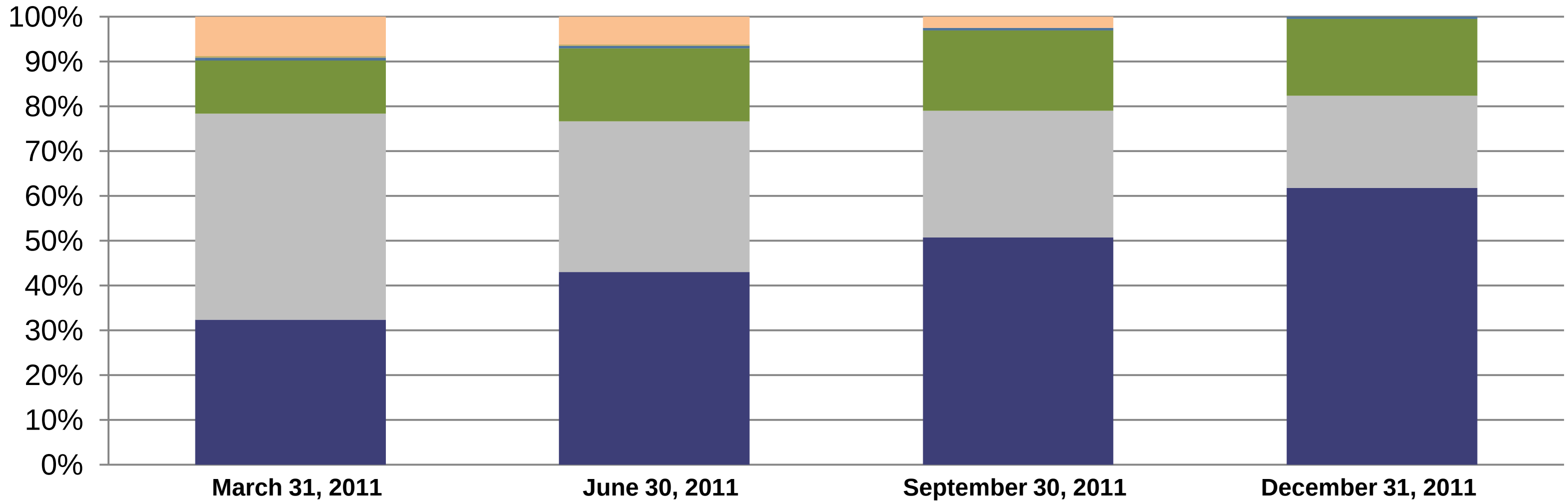
Percentages may not total to 100% due to rounding.

II. Changes in Portfolio Sector Allocation Over Past 12 Months

Changes in Sector Allocation

- Notably, over the past four quarters, the County has been increasing its Federal Agency holdings while decreasing its U.S. Treasury allocation. Since March 31, 2011, the County's exposure to Agencies has almost double, with a corresponding decrease in Treasury holdings. With rates at or near historic lows, especially among securities maturing within two years, this change in allocation may add value without adding undue risk given the Federal Reserve's pledge to keep the federal funds target rate in its current range of 0.00% to 0.25% until at least 2013 and the strong level of support the federal government is providing to the Federal Agencies.
- The County's allocation to Federal Agencies is the highest since March 2009.
- The County no longer has any funds directly invested in repurchase agreements. The County's only exposure to corporate debt comes indirectly through its investment in the Washington State LGIP which holds some repurchase agreements.

Sector Allocation March 2011 – December 2011



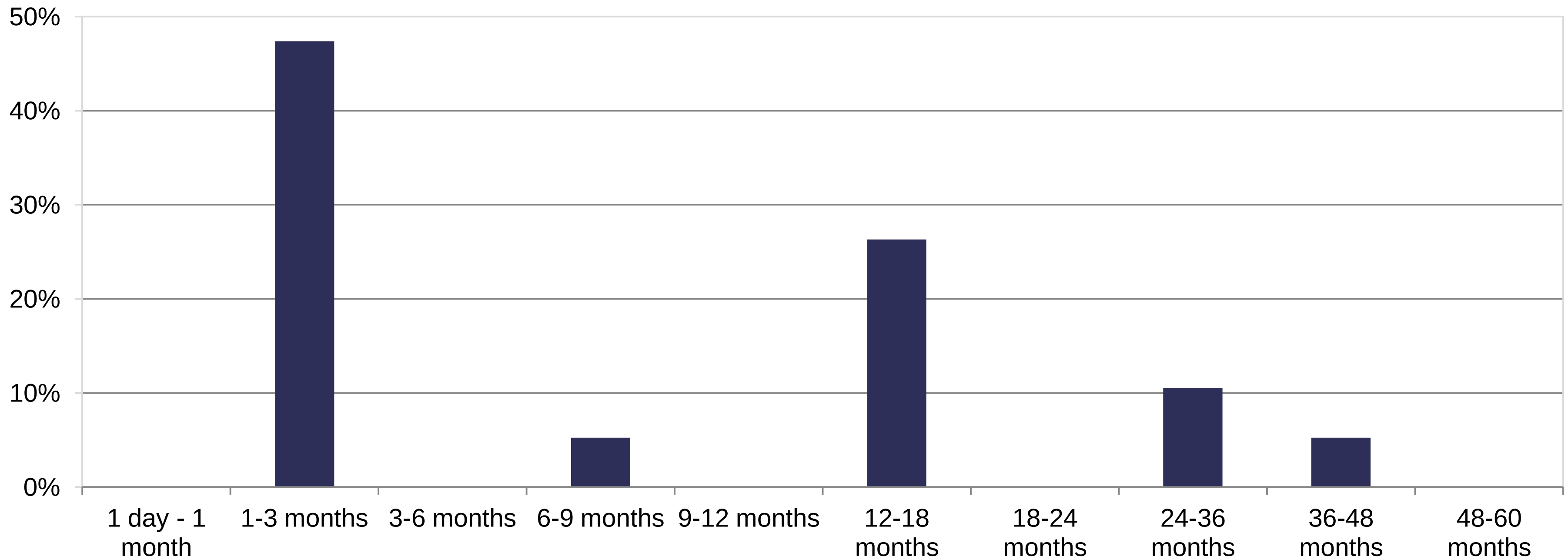
	March 31, 2011	June 30, 2011	September 30, 2011	December 31, 2011
Federal Agencies	32.32%	42.99%	50.71%	61.78%
U.S. Treasury	46.07%	33.63%	28.27%	20.54%
Washington State LGIP	11.83%	16.33%	17.96%	17.18%
Cash and Equivalents	0.00%	0.00%	0.00%	0.00%
Certificates of Deposit	0.00%	0.00%	0.00%	0.00%
Agency Mortgages	0.64%	0.55%	0.56%	0.49%
Municipal Notes	0.33%	0.31%	0.00%	0.00%
Repurchase Agreements	8.82%	6.19%	2.49%	0.00%

**Percentages may not total to 100% due to rounding.*

II. Sector Allocation – U.S. Treasury Securities

Topic	Observations
Observations	• The County's U.S. Treasury securities are allocated mostly among maturities between 0 to 18 months, with approximately 84% of securities set to mature in this range. • Anchored by the Fed's promise to keep rates low until at least mid-2013, short-term rates remained low and range-bound during the quarter. Although the economic recovery appears to have gained some momentum, long-term rates remained depressed due to the Fed's "Operation Twist" as well as the ongoing flight to quality spurred by Europe's sovereign debt crisis. • The County decreased its overall allocation to U.S. Treasuries to 21%, compared to 28% at the end of the previous period. The absolute allocation to Treasuries decreased by $300 million quarter over quarter; the relative allocation dropped also due to the County purchases of other securities with the additional $200 million in net assets that flowed into the pool. • During the quarter, $200 million in U.S. Treasury securities matured and an additional $100 million was sold. The proceeds and maturities were redeployed to other sectors, primarily the federal agency sector. • The average maturity of the County's U.S. Treasury holdings decreased by 25 days to 307 days compared to September 30th.

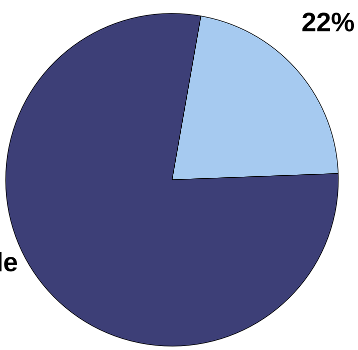
U.S. Treasury Maturity Distribution
as of December 31, 2011



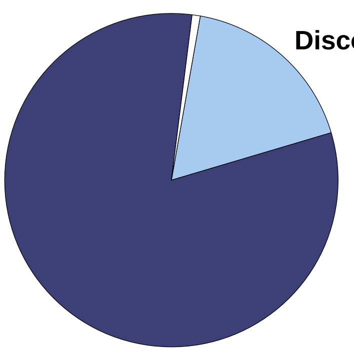
II. Sector Allocation – Federal Agencies

Topic	Observations
Structure	• Non-Callable 78% • Callable 22% • Discount Notes 18% • Coupon bearing Notes 81% • Agency Mortgage 1%
Diversification	• Freddie Mac (FHLMC) 24% • Federal Home Loan Bank (FHLB) 25% • Fannie Mae (FNMA) 38% • Federal Farm Credit Bank (FFCB) 13% • Freddie Mac Mortgage-Backed (FHR) <1% • Fannie Mae Mortgage-Backed (FNR) <1%
Conclusions	• The County's federal agency allocation is diversified among the four major issuers. Approximately $520 million of federal agency securities matured or were sold during the quarter. Over the quarter, the County purchased approximately $1 billion in new federal agency issues, adding approximately $613 million in Agency exposure as compared to September 30th. Short-term discount notes comprised $507.7 million of the new purchases made during the quarter. • The County has slightly increased its allocation to callable federal agency securities to 22% as of December 31st versus 18% on September 30th. The County purchased a number of 3, 4 and 5-year callable federal agency notes during the quarter (approximately $262 million), which are callable in 2012. In the fourth quarter, callable federal agency securities in this range offered incremental yield over comparable federal agency bullets, due to yield spreads and high probability of being called. • As of December 31st, approximately 62% of the County's pool was comprised of Federal Agency obligations.

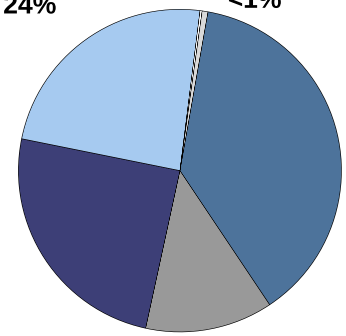
Callable vs. Non-Callable as December 31, 2011



Structure Distribution as of December 31, 2011



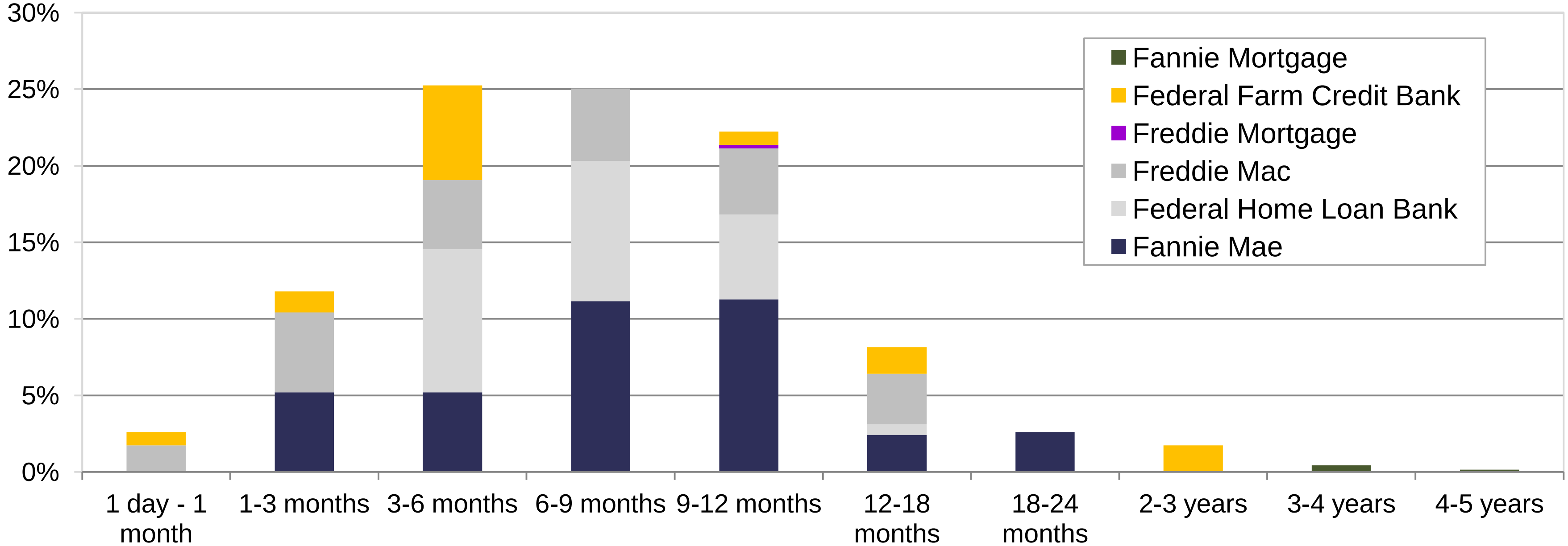
Issuer Diversification as of December 31, 2011



** All calculations above are based on total Agency exposure, not overall Portfolio*

Topic	Observations
Maturity Distribution	• The County's federal agency maturity distribution falls within the limits set forth by its investment policy statement. • Bulleted and callable federal agency securities are diversified between maturities of one day and three years (viewing callable securities to their call dates and mortgage securities on an average life basis). The weighted average life of mortgage-backed federal agency securities range from 0.9 to 4.1 years. • The County increased its holdings in short-term federal agency securities (those maturing between one day and one year) during the quarter. Eighty-seven percent (87%) of the County's federal agency holdings are set to mature in the next 12 months (viewing callable securities to their call dates and mortgage securities on an average life basis). As of September 30th, approximately 78% of securities fell into the same short-term category. • Overall, the aggregate federal agency holdings drifted to a slightly shorter overall maturity over the quarter, ending December 31st at 240 days compared to 266 days at September 30th.

Federal Agency Maturity Distribution by Name
as of December 31, 2011

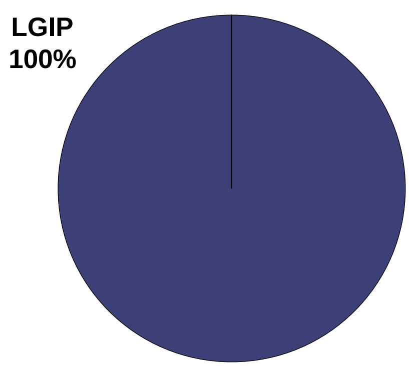


- Agency Mortgage maturities are calculated as average life. Average life data taken from Bloomberg Financial Markets
- Callable securities are shown to their next call date.
- All other Agency maturities are calculated as days to maturity.

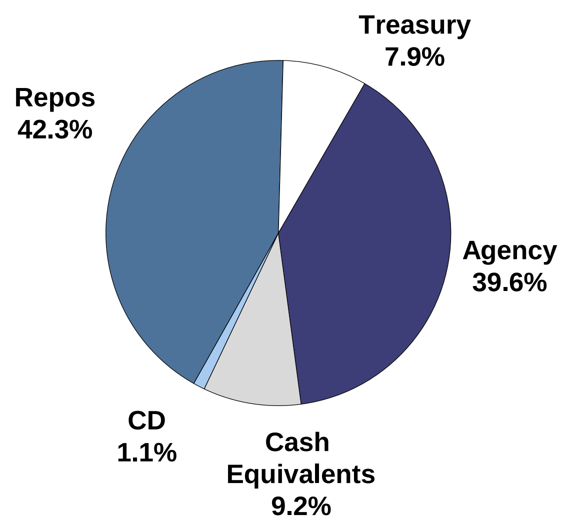
II. Sector Allocation – LGIPs and Cash Equivalents

	Underlying Investments	Rating	Observations
Washington State LGIP	• Federal Agencies 39.56% • U.S. Treasuries 7.89% • Cash Equivalents 9.17% • Certificates of Deposit 1.09% • Repurchase Agreements 42.28% *As of December 31, 2011*	• N/A	• The County currently has allocated $794.5 million to the Washington State LGIP (the “LGIP”). • Over the fourth quarter, the Washington State LGIP decreased its Federal Agency and Treasury holdings, and increased its Repurchase Agreements. • The LGIP ended the quarter with an allocation of 7.9% U.S. Treasury and 39.6% federal agency versus 8.1% and 51.6% last quarter, respectively. The State increased the LGIP’s allocation to repurchase agreements from 31.8% to 42.3% over the quarter.
Repurchase Agreements	• N/A	• N/A	• As of December 31, 2011, the County held no repurchase agreements in the pool. This is the first time since beginning to review the pool’s holdings in 2008 that we have seen no exposure to repurchase agreements. Repurchase agreement rates at December 31st were extremely low.

Issuer Distribution
as of December 31, 2011



Washington State LGIP
Sector Distribution
as of December 31, 2011

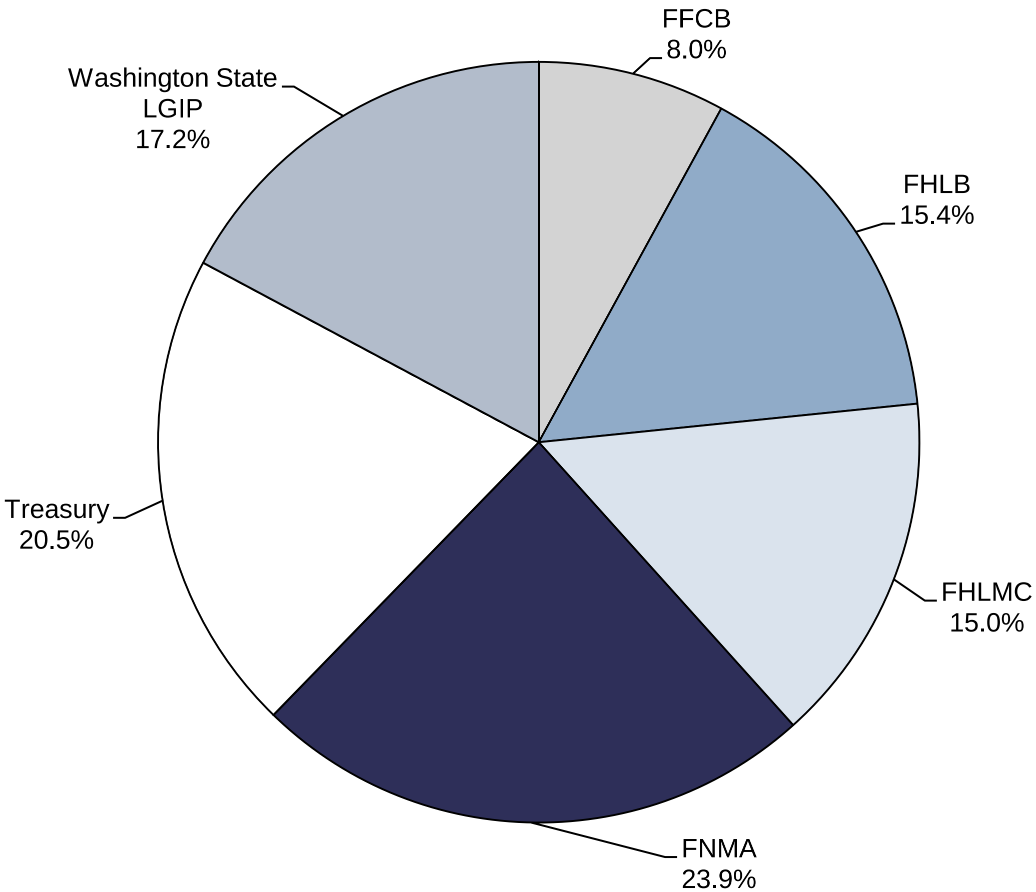


** All calculations above are based on total cash equivalents exposure, not overall Portfolio*

***Percentages may not total to 100% due to rounding.*

III. Issuer Concentration

Issuer Exposure	
	• The County has continued to diversify holdings by issuer, evident in the chart below. The County has allocated holdings among six individual issuers. • Approximately 83% of the portfolio is allocated directly to U.S. government guaranteed or government supported entities. By including the Pool's indirect exposure to these entities through its holdings in the Washington State LGIP, this percentage increases to nearly 91%. • Remaining assets are allocated among the Washington State LGIP (overnight liquidity).



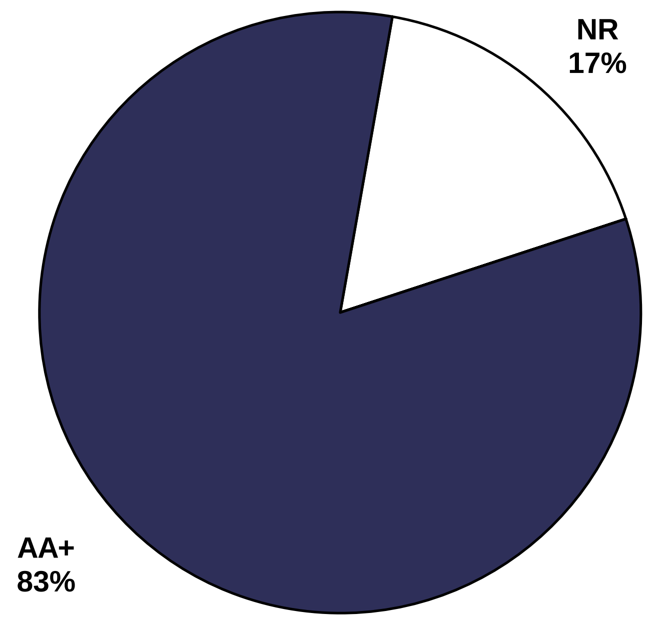
**Percentages may not add to 100.0% due to rounding.*

IV. Overall Credit Quality

County Investment Pool Credit Analysis

- The County Pool's overall average credit rating remains very strong. This quarter represents the lowest amount of corporate exposure since PFM began analyzing the portfolio in 2008.
- The County's only corporate exposure comes through its investment in the Washington LGIP. Less than 8% of the County's total portfolio is allocated indirectly to corporate securities through the LGIP.
- As of the current quarter, over 83% of holdings are either guaranteed or supported by the U.S. government.
- The 17% NR allocation represents the County's investment in the Washington State LGIP, which is not currently rated by any ratings agency.
- PFM has no concerns regarding the Pool's current credit distribution.

Credit Distribution*
as of December 31, 2011

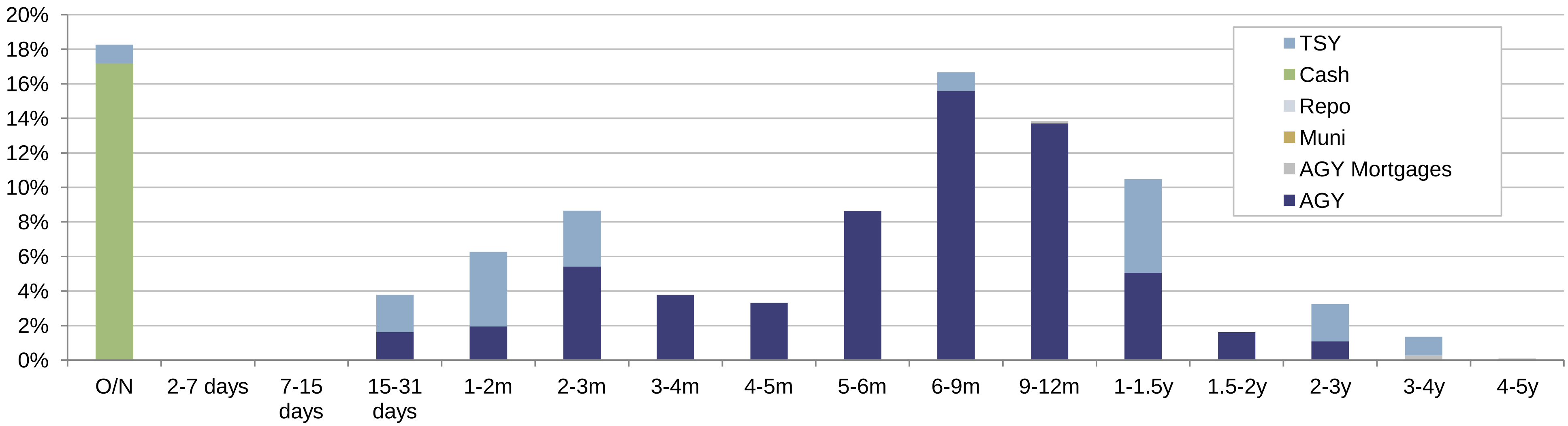


*Ratings by S&P

V. Maturity Distribution

Maturity Distribution	Observations
Weighted Average Maturity ("WAM")	• The County continues to diversify holdings among several maturity buckets, as seen in the chart below. • During the quarter, the County purchased over $850 million of Federal Agency securities maturing in the 6 to 15 month range. • By far, a majority of holdings – 79.5% of the portfolio – are scheduled to mature within the next twelve months. • With the addition of intermediate-term Federal Agency securities, clustered in the 6 to 9 month range, the overall weighted average maturity ("WAM") of the portfolio has decreased from 236 days on September 30th to 217 days at the end of December (viewing callable securities to their call dates and mortgage securities on an average life basis). • If securities with maturities longer than one year are excluded, the remaining "short" portfolio has a weighted average maturity of 139 days, up from 129 days on September 30th. New purchases of Federal Agencies in the 6-12 month range contributed to the increase in this figure. • The WAM of the portfolio offers a level of market risk that is consistent with the objectives of the County's Pool, and others with similar objectives, and is in keeping with the County's cash flow expectations.
Liquidity	• The County Pool appears to provide adequate liquidity, both in terms of final maturities and the sectors in which the Pool has invested. Approximately 22% of the portfolio's holdings are scheduled to mature within the next thirty-one days.

Maturity Distribution as of December 31, 2011



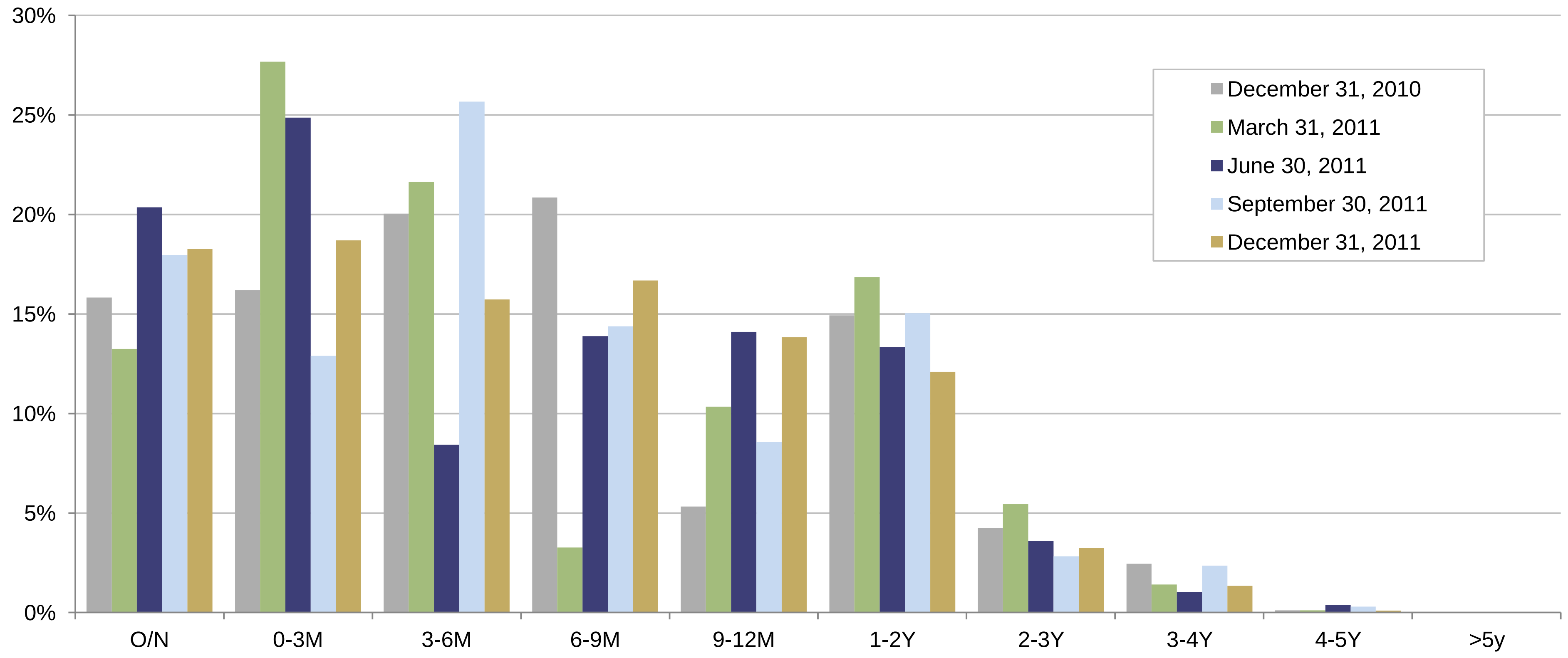
- Agency Mortgage maturities are calculated as average life. Average life data taken from Bloomberg Financial Markets
- Callable securities shown to their call date.
- All other security maturities are calculated as days to maturity. WA LGIP is considered to have a one day maturity.

V. Changes in Portfolio Maturity Distribution

Changes in Portfolio Maturity Distribution

- Securities are well diversified by maturity, and range from overnight to four years in maturity (viewing callable securities to their call dates and mortgage securities on an average life basis). Only a very small amount of the pool is allocated beyond four years, which is barely evident in the chart below.
- Compared to last quarter, the County allocated funds away from the 3-6 month and 1-4 year maturity buckets. The County increased its allocation to securities in the 0-3 month and 9-12 month maturity buckets. In turn, the County's WAM decreased slightly over the quarter to 217 days at quarter end.
- Thirty-seven percent (37%) of funds carry final maturities of three months or less. This is up from September 30th, where 31% of funds were to mature in three months. Approximately 83% of the portfolio is set to mature in the next 12 months.

Maturity Distribution December 31, 2010 to December 31, 2011



- Agency Mortgage maturities are calculated as average life. Average life data taken from Bloomberg Financial Markets
- Callable securities shown to their call date.
- All other security maturities are calculated as days to maturity. WA LGIP is considered to have a one day maturity.

King County

2012 WEATHER FORECAST: LOCALLY SUNNY, DARK CLOUDS THREATEN

Economic Outlook Presentation to the King County Investment Committee

Jan. 24, 2012

Tom Goodwin PhD, Chief Economist
Metropolitan King County

King County

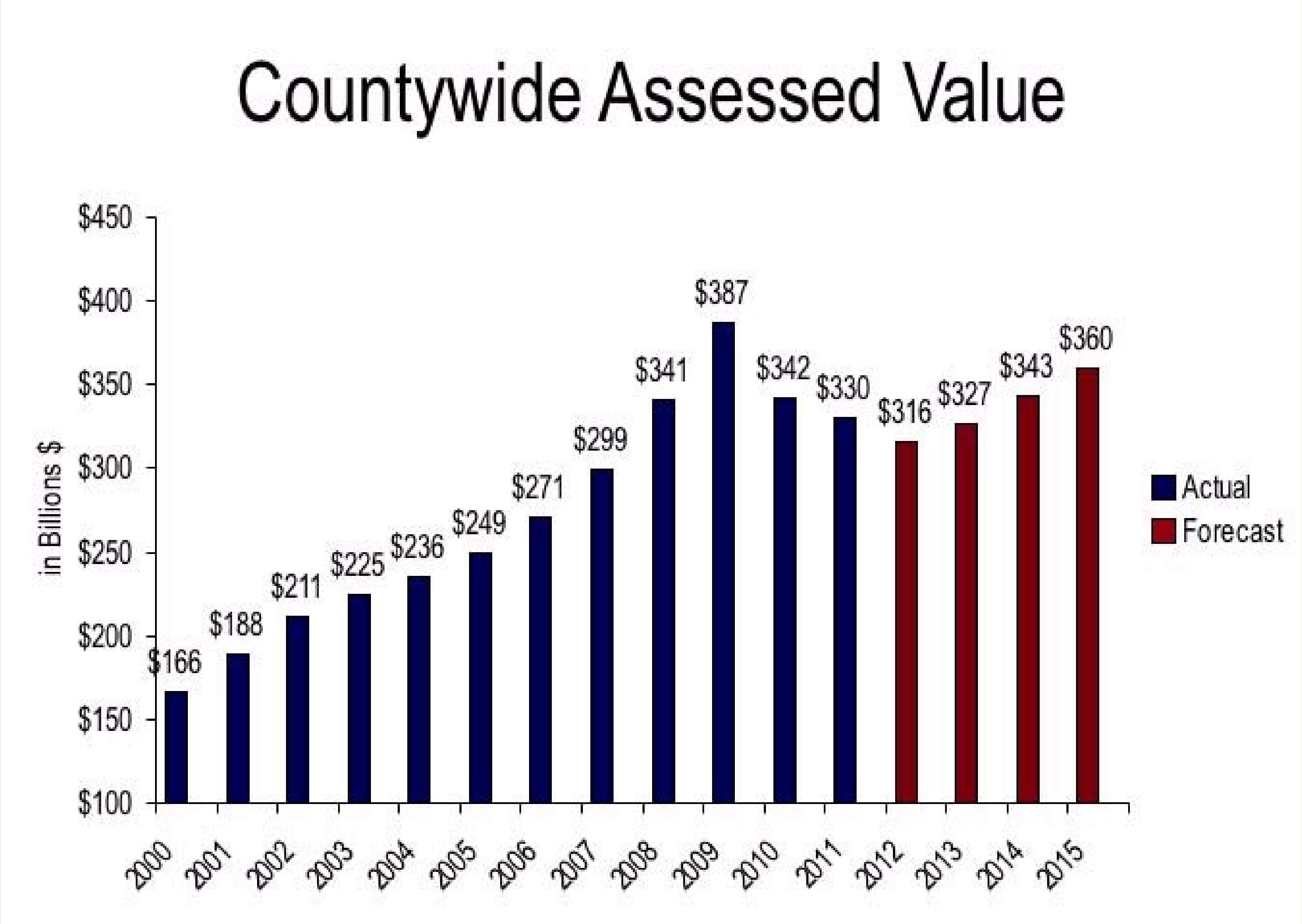
First, the sunny local weather

- Boeing outlook great
  - The 737 MAX will be built in Renton (yay!)
    - 2,000-3,000 new jobs
  - Order book tops 3,500 planes
  - New pay package includes $5,000 bonus ($140 million) ⇒ indirectly create more than1,000 new jobs
- Microsoft pay raise added $600 million to economy ⇒ 4,000-5,000 new jobs indirectly
- Puget Sound is outpacing nation in job growth – 34,000 new jobs expected in 2012
- Retail sales up 5.4% last year

2012 (tax year 2013) a return to positive AV growth

Led by industrial & commercial

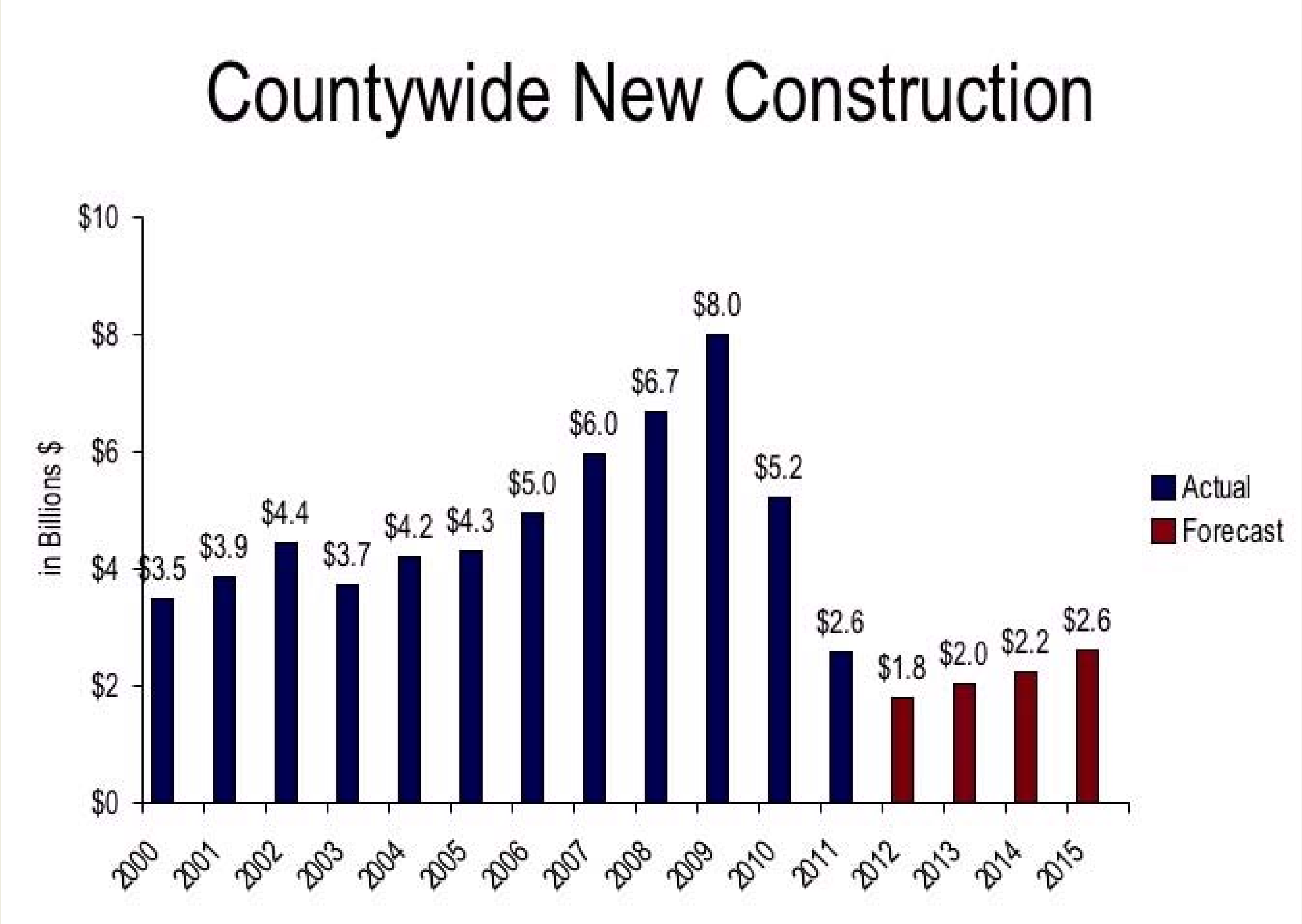
2013 3.5%
2014 5.0%
2016 6.5%



Construction finally starting to dig out of its hole

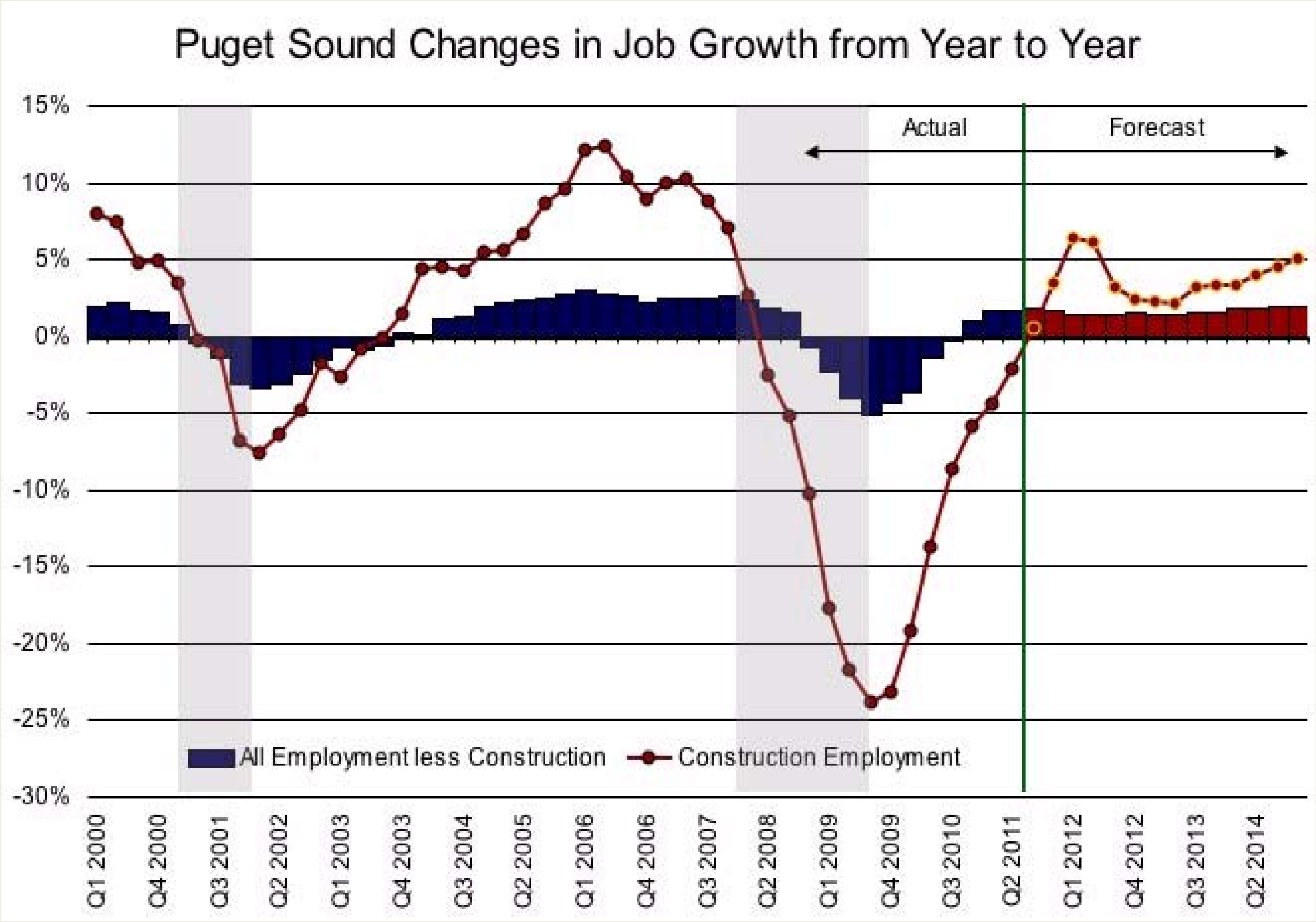
Green shoots: Apartments, top tier office & medical space

2013 13.5%
2014 10.6%
2015 17.0%



Positive job growth ahead

Construction to return to positive job growth



Source: Puget Sound Economic Forecaster

The US growth outlook for 2012 is lower than a year ago

Blue Chip Survey Forecasts for 2012	Real GDP	CPI	Indust. Product.	3-month T-Bill	10-year T-Note	Unempl. Rate
Jan 2012 Survey	2.2%	2.1%	3.0%	0.1%	2.4%	8.8%
Jan 2011 Survey	3.2%	1.9%	4.1%	1.2%	4.2%	8.7%

King County

Dark clouds: Europe

- Europe in recession
  - Consensus: it will be short and shallow (I disagree)
  - What impact on Puget Sound?
- Prediction: Greece defaults on March 20
  - Will it be "voluntary" or trigger credit default swaps?
- Will Greece & Portugal exit the Euro?
  - A "Lehman event"?

King County

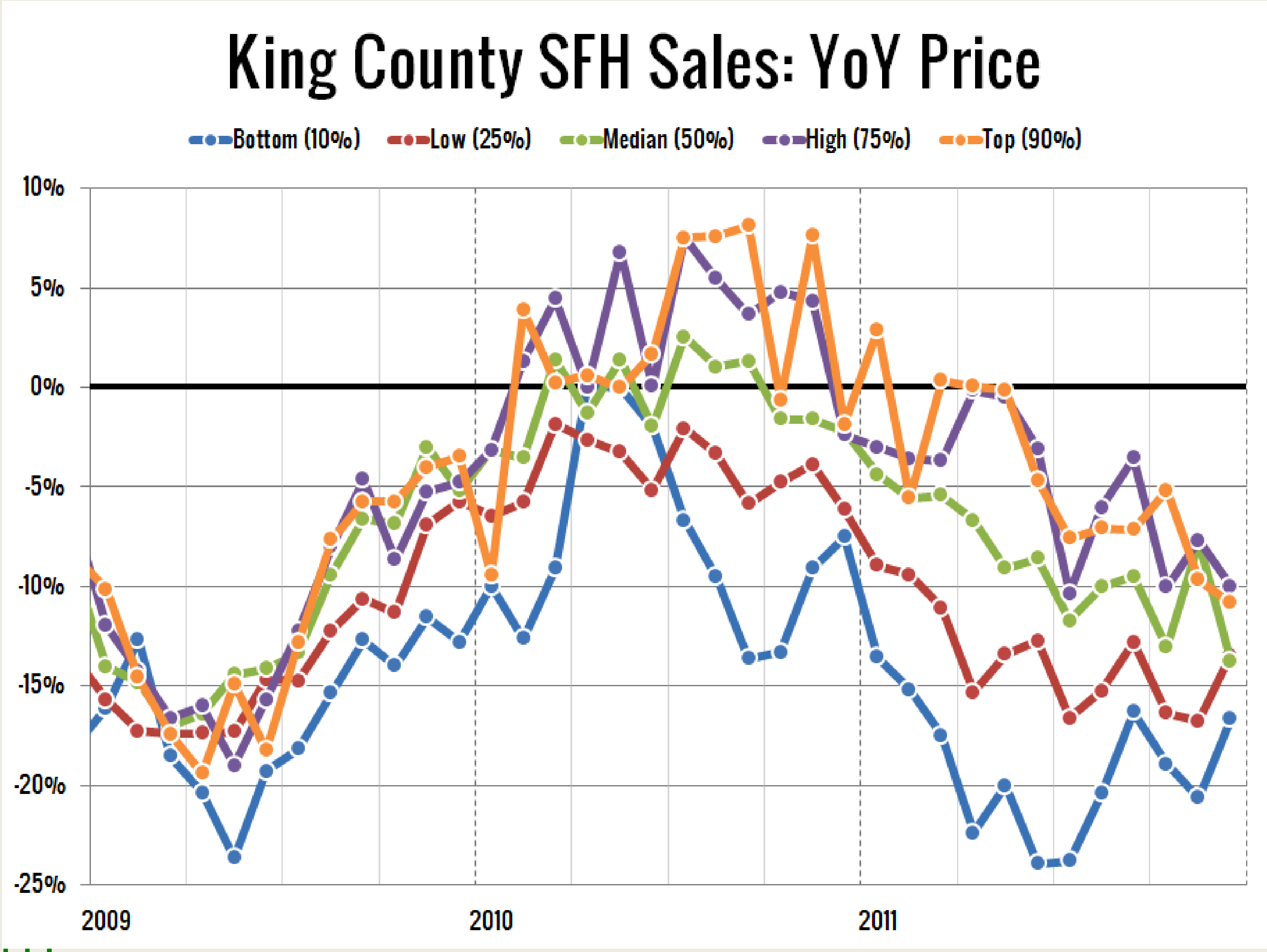
Dark clouds: US

- Consumers still “deleveraging”
  - Paradox of thrift
- Little help on the way from Congress
  - Payroll tax cut and long term unemployment benefits likely extended through 2012
  - Nothing else will happen until after November election – and then what?
- Little help on the way from the Fed
  - QE3 possible – but what good will it do?

Dark clouds: housing market

Foreclosures hit under $300,000 market hardest

Shadow inventory: death by a thousand cuts?

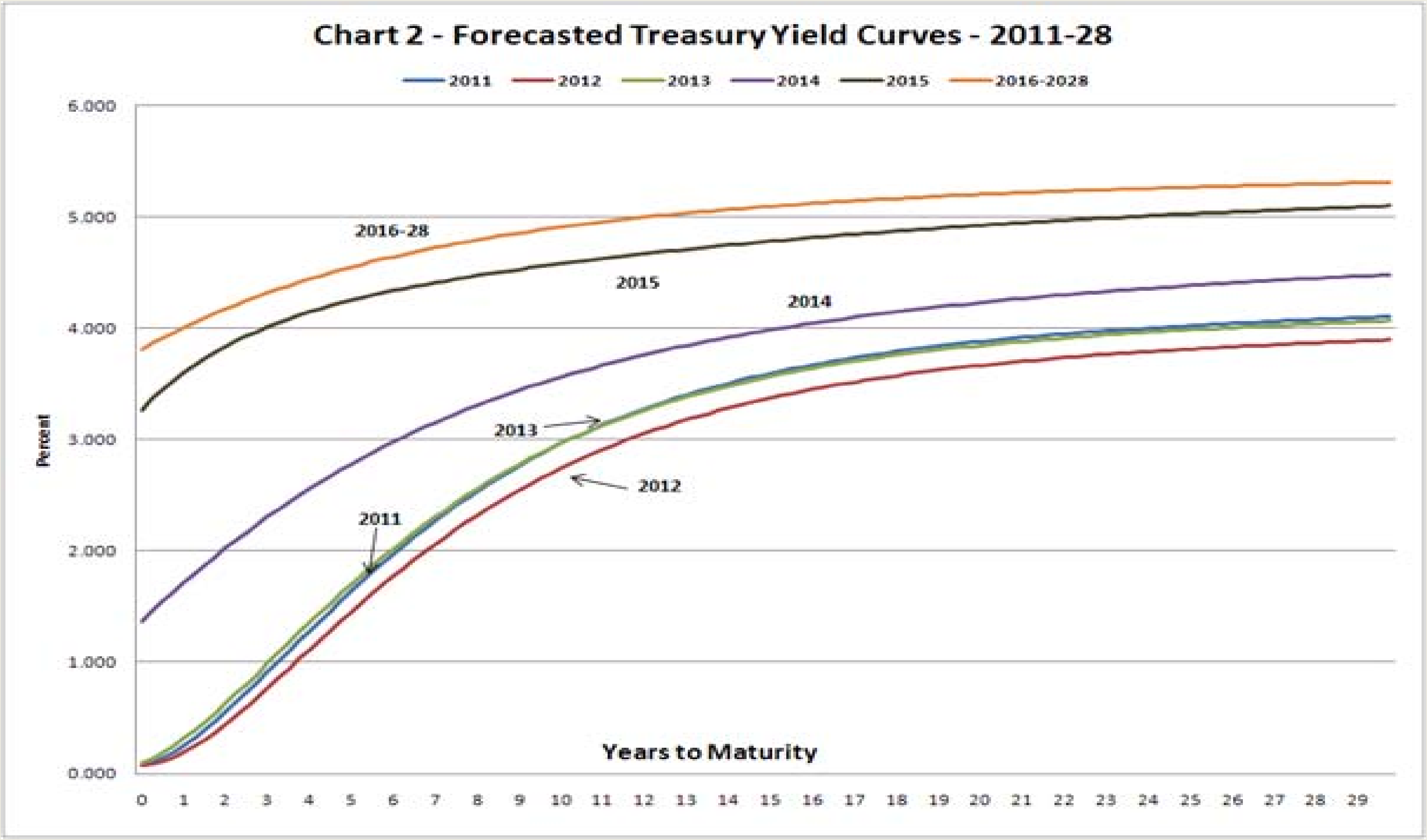


Source: Seattle Bubble

Interest rate outlook

- No Fed tightening on horizon
  - Futures market (Jan. 15) forecasts 0.7% Fed Funds rate at the end of 2014
  - QE3 possible – might not effect interest rates much
- Why is 10Y Treasury yield so low?
  - Flight to quality (“safe haven”), or
  - Deflationary stagnation (“Japan disease”)?

Yields will stay low through 2014



Source: Global Insight + OEFA calculations

Questions?

Investment Pool Changes

- New Interface to Oracle Accounting System
- More timely annual pool fee rebate
- New Credit Analyst – Christine Denis
- Investment Policy Adopted 7/27/11
- Mailing of pool reports eliminated
- Web Site revised and updated http://www.kingcounty.gov/operations/Finance/Treasury/InvestmentPool.aspx

Investment Pool Advisory Committee (IPAC)

- Purpose of Advisory Committee
  - Provide input and advice to the County's Executive Finance Committee regarding pool policies, practices and fees

- 10 members with 2–year terms
  - 2 from school districts
  - 1 from fire districts
  - 1 from water/sewer districts
  - 2 at-large members from outside districts
  - 2 King County fund managers
  - 1 King County Treasury Manager (permanent member)
  - 1 Private citizen who is an investment professional

Current IPAC Members

- Jake Kuper – Issaquah School District
- Bang Parkinson – Highline School District*
- David Lawson – South King County Fire & Rescue *(Committee Chair)*
- Ken Goodwin – Woodinville Water District
- Linda Glenicki – King County Library System *(Committee Vice Chair)*
- Margaret Raihl – Harborview Medical Center*
- Tim Aratani – King County Wastewater Treatment Division
- Duncan Mitchell – King County Dept. of Transportation*
- Scott Matheson – King County Treasury Manager
- Tim Kerr – Private Citizen Investment Professional*

* Term Expires April 2012

IPAC 2011Activities and Accomplishments

- Participated in King County Public Records Access Training
- Modified the IPAC Charter
- Obtained Nominations and Confirmation for New 2-Year Terms of Members
- Elected New Chair and Vice Chair
- Established Committee Quarterly Meeting Schedule
- Responded to EFC Regarding Investment Policy Updates
- Provided IPAC Representation at Investment Pool Annual Meeting

IPAC 2011 Activities and Accomplishments

- Established Rotation Schedule for IPAC Representation to EFC Meetings

- Considered King County Legal Review Comments Regarding
  - Prohibited Investments
  - Fiduciary Responsibilities
  - Ethics and Conflict of Interest
  - Policy Regarding Investment in Commercial Paper
  - Participation in the Investment Pool
  - Authority of Credit Oversight Committee
  - Membership on Credit Oversight Committee
    - Qualifications, Alternates, Internal Control

- Made Policy Input to EFC Regarding
  - Participation of Districts That Provide Their Own Treasurer
  - IPAC Constituent Membership on Credit Oversight Committee

3 Basic Investment Strategies for a Low Rate Environment

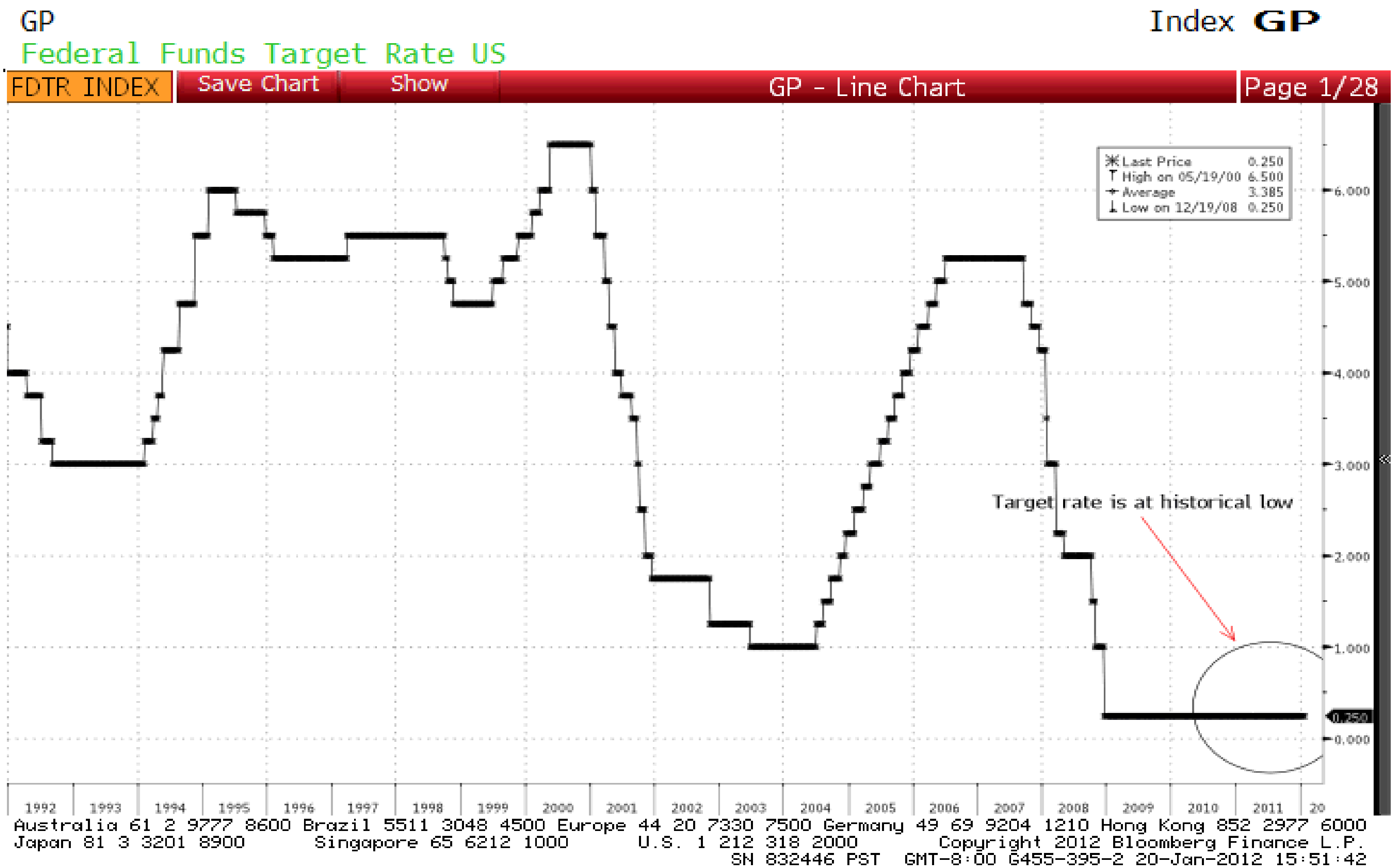
1. Extend Duration
2. Substitute Federal Agencies for U.S. Treasuries
3. Add Callable Securities

Strategy 1 – Extend Duration

- Pros:
  - Can improve pool's yield
    - If rates fall or stay stable
  - Reduce volatility of pool's yield—lower reinvestment risk

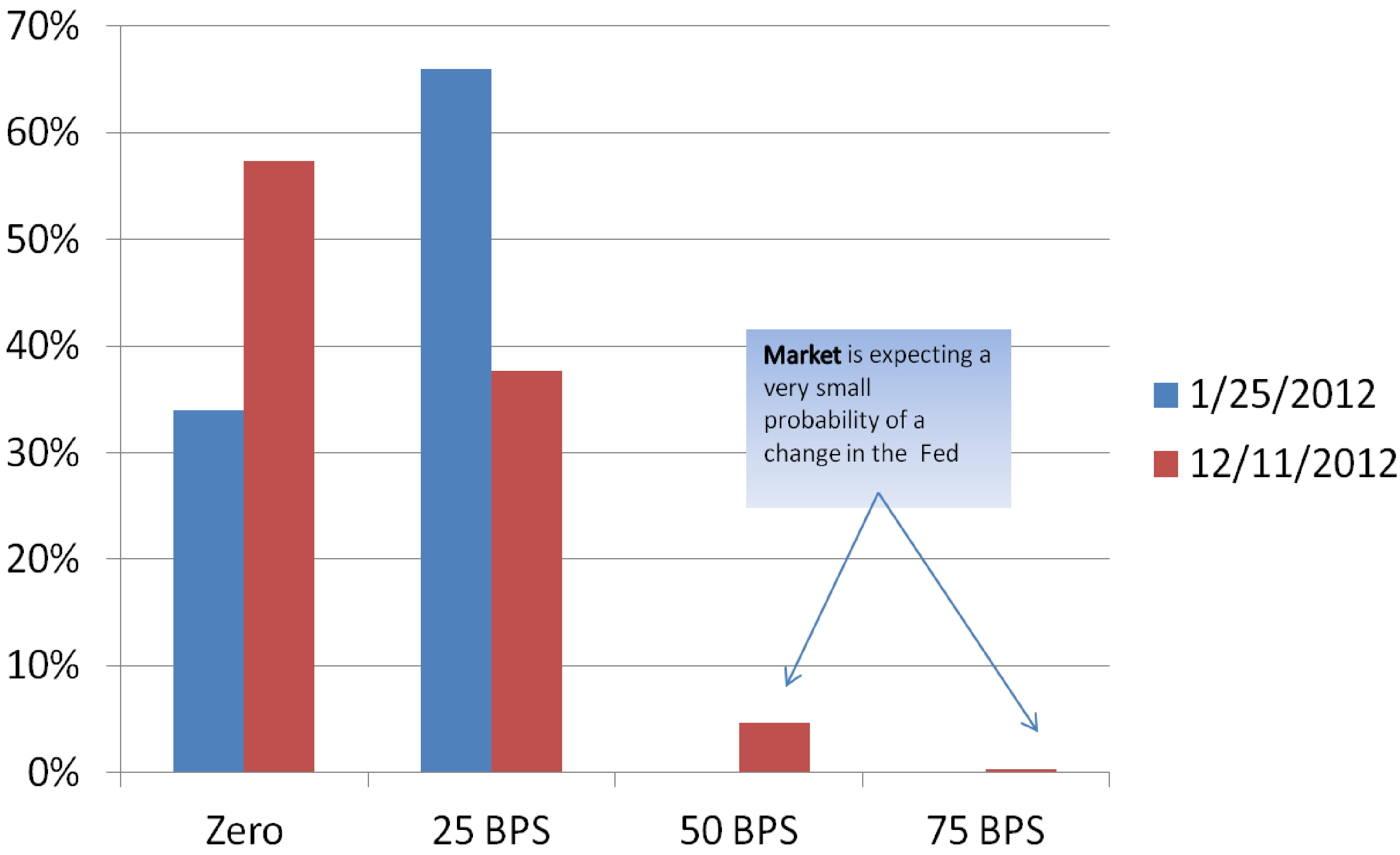
- Cons:
  - Increases pool's interest rate risk—price volatility
  - Pool's yield can lag market when rates increase

Fed Funds Target Rate 1992 to Present



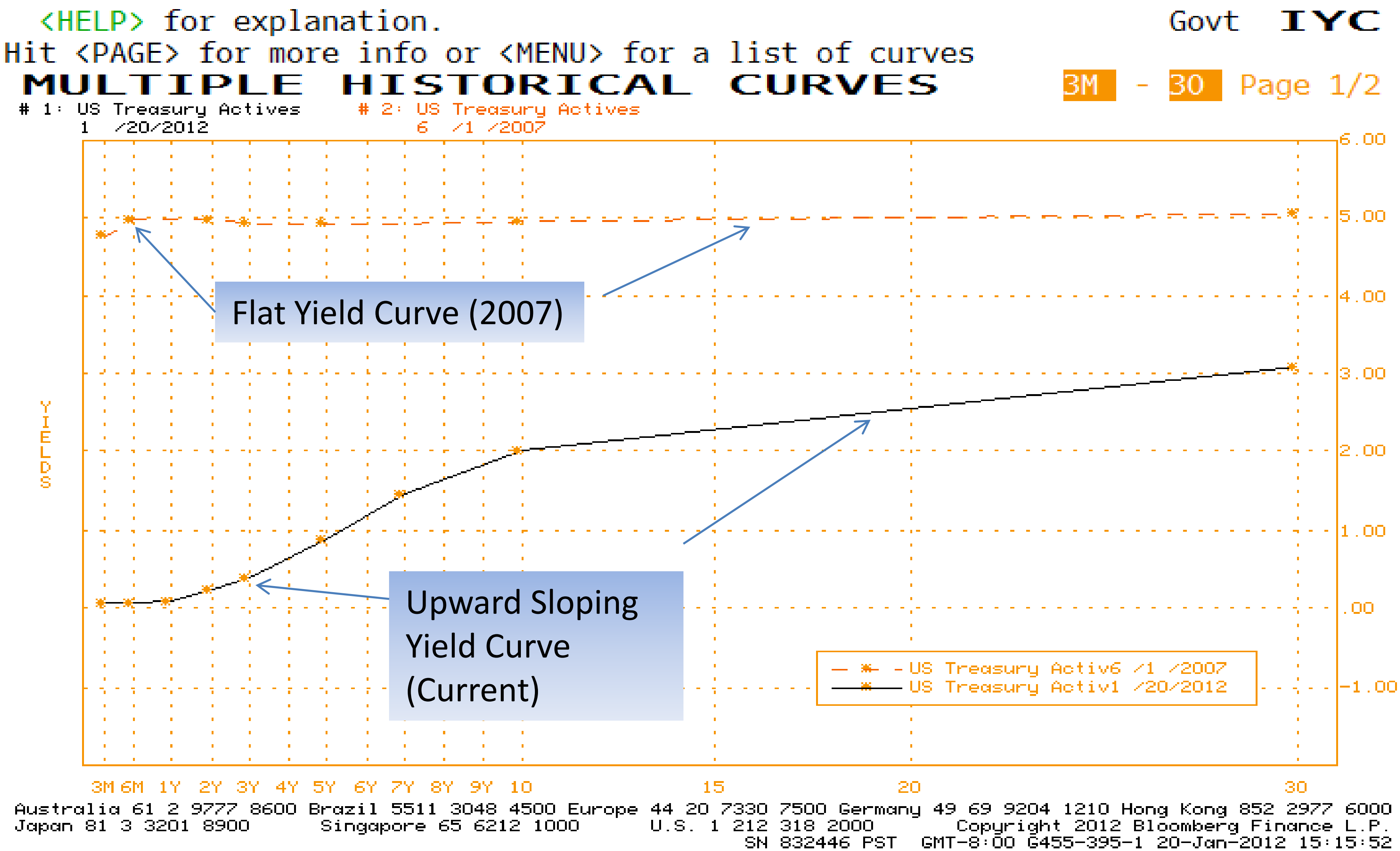
Source: Bloomberg

Expectations for Fed Funds Rate Present vs. December 2012



Source: Bloomberg

Yield Curve Shapes

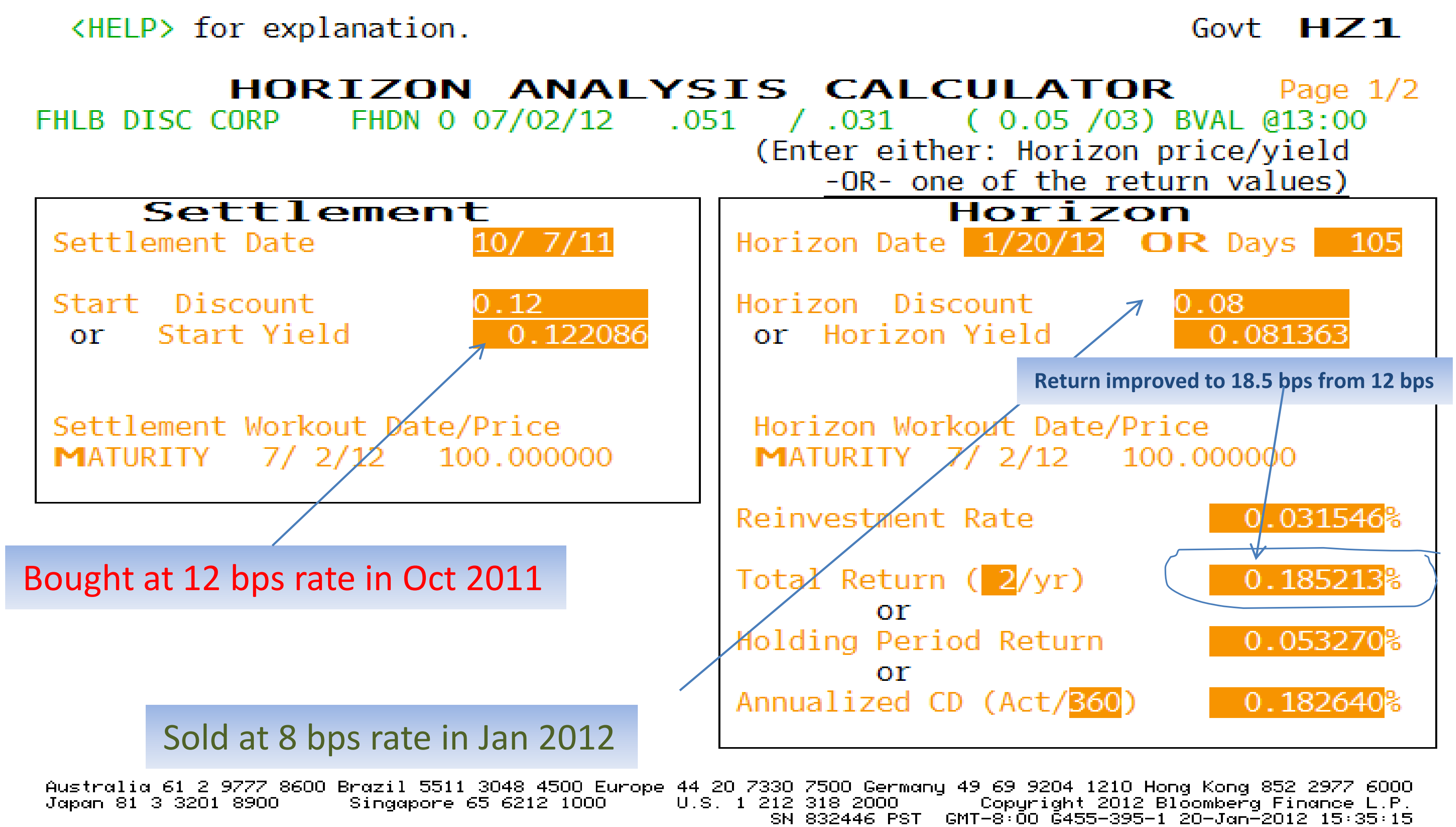


Source: Bloomberg

Managing the Pool's Duration

- Currently the pool's duration is about ¾ of a year.
- Historically the pool's duration has been about 1 ¼ years.
- Pool's current duration target range is 0.6 to 1.1 years.
- Given the prospect of low rates for an extended period, we are looking for opportunities to move the pool's duration out to higher end of the range.

Example of a Trade that Works When the Yield Curve has Positive Slope



<HELP> for explanation. Govt **HZ1**

HORIZON ANALYSIS CALCULATOR Page 1/2

FHLB DISC CORP FHDN 0 07/02/12 .051 / .031 (0.05 /03) BVAL @13:00

(Enter either: Horizon price/yield -OR- one of the return values)

Settlement

Settlement Date	10/ 7/11
Start Discount	0.12
or Start Yield	0.122086
Settlement Workout Date/Price	
MATURITY 7/ 2/12	100.000000

Horizon

Horizon Date	1/20/12 **OR** Days 105
Horizon Discount	0.08
or Horizon Yield	0.081363
Horizon Workout Date/Price	
MATURITY 7/ 2/12	100.000000
Reinvestment Rate	0.031546%
Total Return (2/yr)	0.185213%
or Holding Period Return	0.053270%
or Annualized CD (Act/360)	0.182640%

Return improved to 18.5 bps from 12 bps

Bought at 12 bps rate in Oct 2011

Sold at 8 bps rate in Jan 2012

Australia 61 2 9777 8600 Brazil 5511 3048 4500 Europe 44 20 7330 7500 Germany 49 69 9204 1210 Hong Kong 852 2977 6000
Japan 81 3 3201 8900 Singapore 65 6212 1000 U.S. 1 212 318 2000 Copyright 2012 Bloomberg Finance L.P.
SN 832446 PST GMT-8:00 G455-395-1 20-Jan-2012 15:35:15

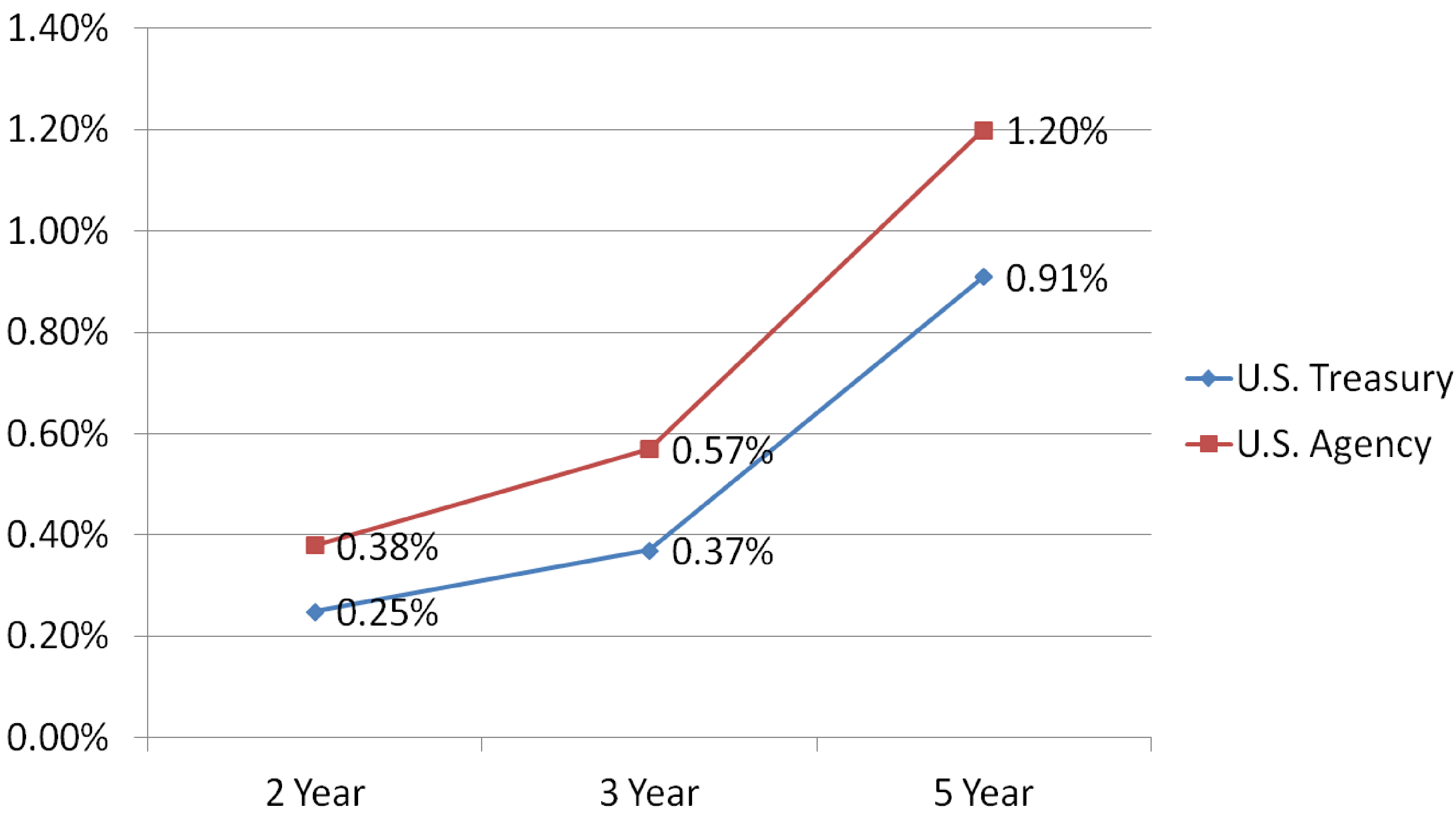
Source: Bloomberg

Strategy 2 – Substitute Federal Agency Securities for U.S. Treasuries

- Pros:
  - Maintains pool’s safety – Strong tie to U.S. Gov
  - Improves pool’s yield

- Cons:
  - Less direct tie to U.S. Government
  - Slightly less liquid than Treasury securities

U.S. Agency Spread to U.S. Treasury



Source: Bloomberg

Strategy 3 – Add Callable Securities vs. Non-Callable (Bullet) Securities

- Pros:
  - U.S. Agency issuers – Maintains pool's safety
  - Can improve the pool's yield
    - Works best in a stable interest rate environment

- Cons:
  - Increases reinvestment risk
  - Price appreciation is limited
    - High yielding security can be "called" before maturity
  - Typically, not as liquid as "bullet" securities

Example of How a Callable Note Can Add Yield to the Pool

FREDDIE MAC FHLMC 0 $\frac{5}{8}$ 07/14

Calculate (P,O,V) O | **Price** P) 100.0000 | **OAS** (bp) O) + 7.69 | **Volatility** V) 65.20

Cusip / ID# 3134G3JA9 Option Px Value: 0.18

Settle 1/25/2012 Bench settle 1/23/2012 Vega: 0.00

Spread 38.5bp vs 2Y T 0 $\frac{1}{8}$ 12/31/13 Govt @99-24$\frac{7}{8}$ (0.240)

{NUM}<GO> for:

3) Call Schedule

1/25/13	100.00
4/25/13	100.00
7/25/13	100.00
10/25/13	100.00
1/25/14	100.00
4/25/14	100.00

	OAS Method	Option Free	To Call on 1/25/2013	To Mty
Yld		0.554	0.625	0.625
Sprd		7.6	42.3	14.6
M Dur	1.70		1.00	2.48

Would pick up 42 bps to a bullet agency if call in 1 year

Picks up 14.6 bps over a bullet agency if held to maturity

Source: Bloomberg

Summary

- Even though interest rates are very low, there are strategies that can help maintain the pool's yield—without sacrificing safety or liquidity
- Questions???

Credit Analyst

- Portfolio management
- Cashflow forecasting
- Credit analysis