



PFM

Quarterly Portfolio Review King County Investment Pool

September 30, 2011

Presented by
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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 June 2011.
- Our approach included a detailed portfolio analysis and investment policy compliance review, based on the County’s new investment policy.
- Our analysis was based on the Investment Pool’s holdings as of September 30, 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. Aside from tri-party repurchase agreement counterparties, the Pool has no other corporate exposure.

Observations

- The Pool is comprised of highly liquid securities. Nearly 80% of securities are scheduled to mature in the next twelve months, versus 81.2% on June 30, 2011. Although slightly lower when compared to last quarter, this represents the second highest amount of liquidity since November 2008, and is above the 78% average since PFM began monitoring and reporting on the pool.
- 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), fully collateralized (repurchase agreements), and/or carry a high level of liquidity (Washington State LGIP).
- S&P downgraded the United States’ long-term rating on August 5th from AAA to AA+. The downgrade had virtually no lasting impact on the Treasury and Agency market. We recommended no changes to portfolio strategy as a result of the downgrade.
- Approximately 80% 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 18% of its holdings, this number increases from 80% to 90% of the Pool’s holdings.
- Potential market risk (sensitivity to changes in interest rates) has changed slightly over the past quarter as the total portfolio’s weighted average maturity (“WAM”) was extended by 11 days, from 225 days on June 30th to 236 days on September 30th. This level of market risk is 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 addition of intermediate-term U.S. Treasury and federal agency securities helped to push the quarter-ending WAM slightly higher versus the previous quarter.
- The WAM of the Pool’s short-term securities (those securities with one year or less to final maturity) also rose slightly over the quarter, from 121 days on June 30, 2011 to 129 days on September 30, 2011.
- In keeping with normal seasonal cash flow patterns, total Pool assets decreased by \$440 million over the quarter from \$4,862 million on June 30, 2011 to \$4,421 million on September 30th, 2011.

Portfolio Review

- I. Investment Policy Compliance
- II. Sector Allocation
 - U.S. Treasuries
 - Federal Agencies
 - LGIP and Cash Equivalents
 - Repurchase Agreements
- 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

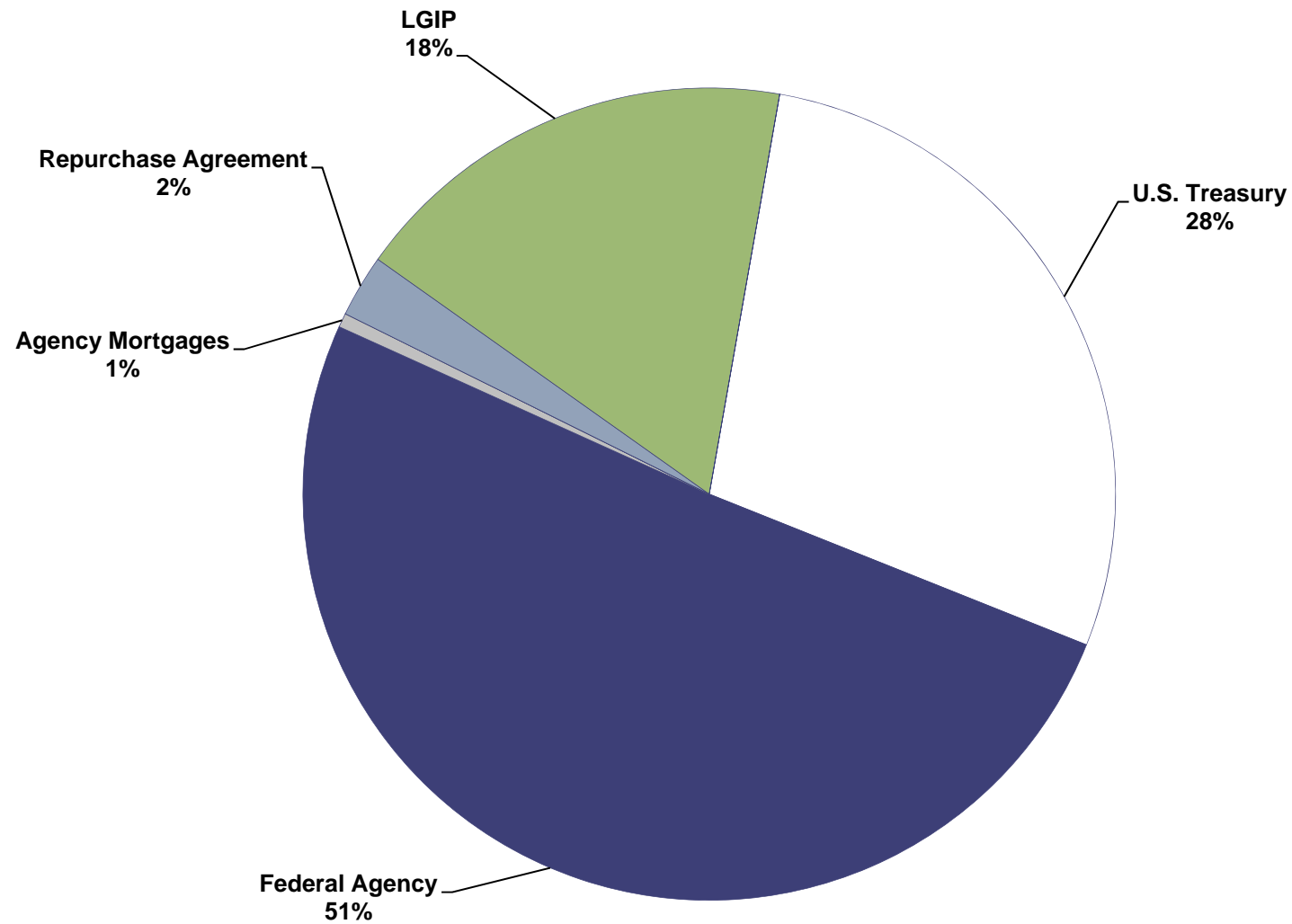


Topic	Observations
Sector Allocation	<ul style="list-style-type: none"> All sector allocations fall within the limits set forth by the County's Investment Policy Statement. The Pool is predominantly invested in securities which are either explicitly guaranteed or carry a high level of support by the U.S. government and the Washington State LGIP. The County increased its allocation to the federal agency sector, from 43.0% on June 30th to 50.7% on September 30th. In doing so, the County reduced its holdings in U.S. Treasury securities by approximately 5%, from 33.6% on June 30th to 28.3% on September 30th. In addition, the County pool no longer holds any municipal debt.
Credit Quality	<ul style="list-style-type: none"> All credit ratings fall within the limits set forth by the County's Investment Policy Statement. The Pool's holdings are of the highest credit quality. A majority of securities are guaranteed or supported by the U.S. government, while the remaining securities, or their issuing entities, hold credit ratings that are rated A-1 by Standard & Poor's, or are invested in a money market pool (Washington State LGIP) that invests in non-corporate issuers and certificates of deposit.
Maturity Distribution	<ul style="list-style-type: none"> All maturities fall within the limits set forth by the County's Investment Policy Statement. The County's holdings are concentrated between overnight and one-year securities, with a small amount of assets invested beyond one year (20.5%).

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	110,000,000	2.49%	✓	4 days	✓
LGIP	794,255,861	17.96%	✓	1 day	✓
Federal Agencies	2,242,041,000	50.71%	✓	3.9 years	✓
Agency Mortgages	24,882,766	0.56%	✓	4.2 years (WAL)	✓
Certificates of Deposit	0	0.00%	✓	N/A	✓
Municipal Bonds	0	0.00%	✓	N/A	✓
U.S. Treasury	1,250,000,000	28.27%	✓	3.3 years	✓

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

Sector Diversification
as of September 30, 2011



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

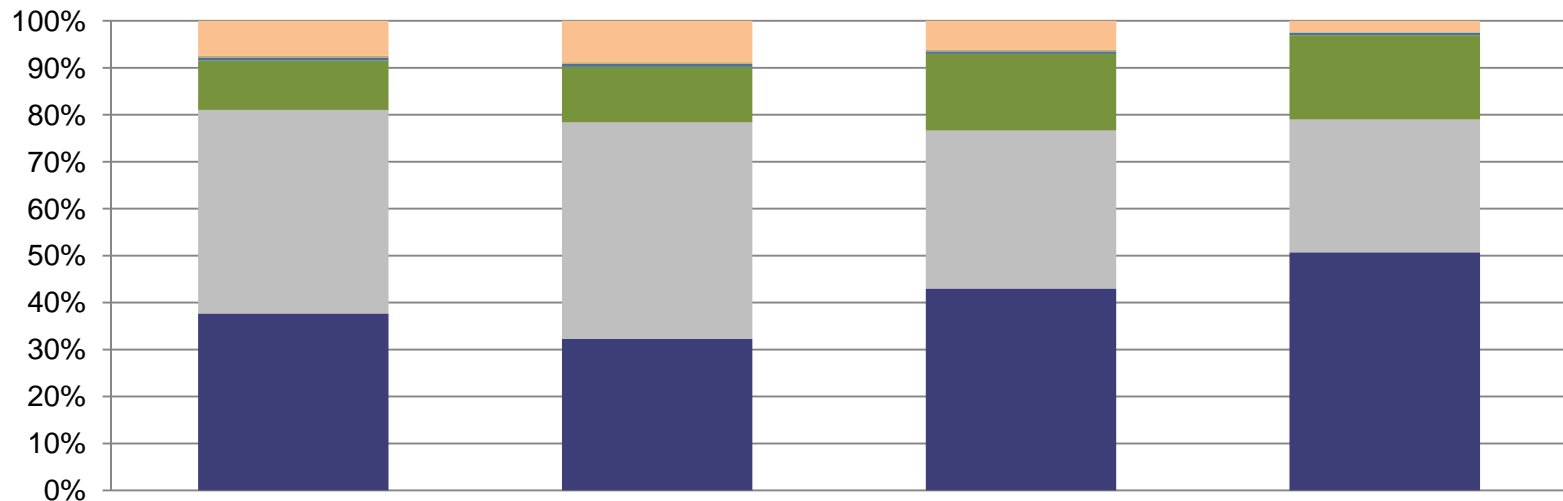
II. Changes in Portfolio Sector Allocation Over Past 12 Months



Changes in Sector Allocation

- Notable for the third quarter is an increase in the allocation to federal agency securities and a corresponding decrease in U.S. Treasury securities. With the recent and continued decline in market yields, especially among securities maturing within two years, this change in allocation may add value without adding undue risk given the Federal Reserve's recent comments about keeping the federal funds target rate in its current range of 0.00% to 0.25% until at least 2013.
- The County's allocation to Federal Agencies is the highest since September 2010. Given the widening of spreads between Treasuries and Agencies, the County's choice of Federal Agency securities over U.S. Treasuries is justified from credit, liquidity, and yield perspectives.
- On July 1, 2011, the County's Phoenix AZ municipal bond matured. The County no longer has any funds invested in municipal debt.

Sector Allocation December 2010 – September 2011



	December 31, 2010	March 31, 2011	June 30, 2011	September 30, 2011
Federal Agencies	37.69%	32.32%	42.99%	50.71%
U.S. Treasury	43.34%	46.07%	33.63%	28.27%
Washington State LGIP	10.50%	11.83%	16.33%	17.96%
Cash and Equivalents	0.00%	0.00%	0.00%	0.00%
Certificates of Deposit	0.00%	0.00%	0.00%	0.00%
Agency Mortgages	0.69%	0.64%	0.55%	0.56%
Municipal Notes	0.32%	0.33%	0.31%	0.00%
Repurchase Agreements	7.45%	8.82%	6.19%	2.49%

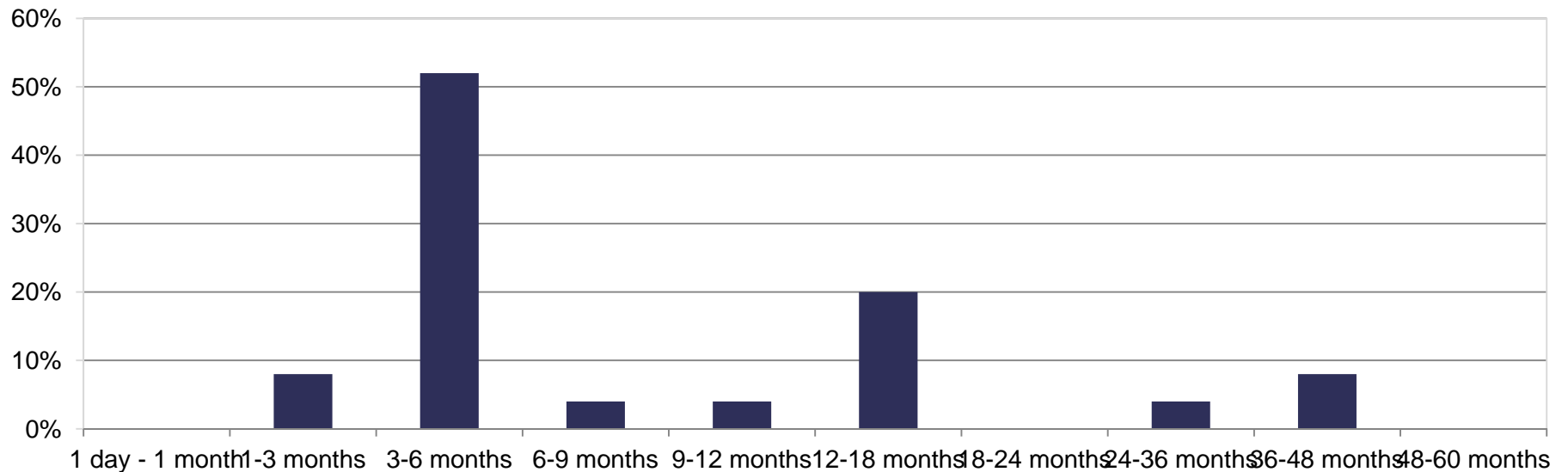
*Percentages may not total to 100% due to rounding.

II. Sector Allocation – U.S. Treasury Securities



Topic	Observations
Observations	<ul style="list-style-type: none"> • The County's U.S. Treasury securities are allocated mostly among maturities between 0 to 18 months, with approximately 88% of securities set to mature in this range. • Although the quarter began with rates very low, longer-term Treasury yields fell further in response to weakening economic fundamentals and the Fed's aggressively accommodative monetary policy actions. Treasuries of 10 year maturity and longer fell the most, as the market anticipated "Operation Twist," which was officially announced in late September. • The County decreased its overall allocation to U.S. Treasuries to 28%, compared to 34% at the end of the previous period. • During the quarter, \$435 million in U.S. Treasury securities matured, and \$50 million was reinvested in Treasury securities maturing in the 36 to 48 month range. The remaining maturities were redeployed to other sectors, primarily the federal agency sector, where a slight yield spread added value for the portfolio. • The average maturity of the County's U.S. Treasury holdings increased slightly (by 3 days) to 305 days, compared to June 30th. The quarterly change is attributable to reinvesting a large portion of maturing Treasuries in short-term federal agency investments instead of short-term Treasuries.

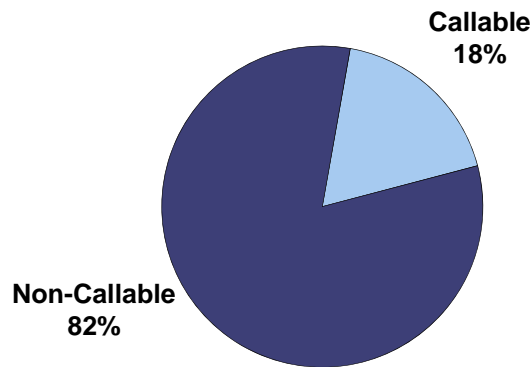
**U.S. Treasury Maturity Distribution
as of September 30, 2011**



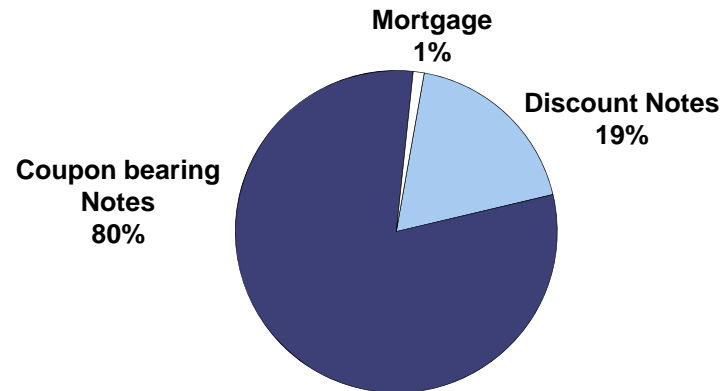
II. Sector Allocation – Federal Agencies

Topic	Observations
Structure	<ul style="list-style-type: none"> • Non-Callable 82% • Callable 18% • Discount Notes 19% • Coupon bearing Notes 80% • Agency Mortgage 1%
Diversification	<ul style="list-style-type: none"> • Freddie Mac (FHLMC) 26% • Federal Home Loan Bank (FHLB) 15% • Fannie Mae (FNMA) 43% • Federal Farm Credit Bank (FFCB) 15% • Freddie Mac Mortgage-Backed (FHR) <1% • Fannie Mae Mortgage-Backed (FNR) <1%
Conclusions	<ul style="list-style-type: none"> • During the quarter, the County increased its allocation to the federal agency sector by approximately \$152 million. Although approximately \$704 million of federal agency securities matured or were called during the quarter, the County added over \$856 million in federal agency holdings to the portfolio. <ul style="list-style-type: none"> • Federal Agency purchases were concentrated in the 1 to 2 year timeframe, with 41% of the purchases falling into this category. 34.5% of the purchases targeted maturities of 1 year or less. The remaining 24.5% were purchased in the 2 to 4 year timeframe. • The County's allocation to callable federal agency securities increased by 13.4%, from 4.72% on June 30th to 18.12% as of September 30th. The high volatility of August and September made callable agencies cheaper, as large swings in yield create more value in the underlying option. The County purchased \$411 million in callable federal agency securities during the quarter.

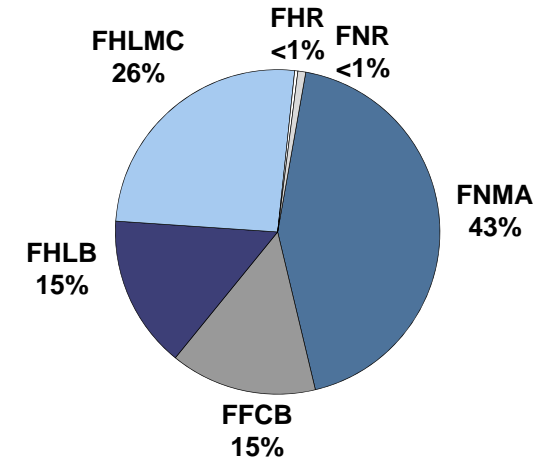
Callable vs. Non-Callable as September 30, 2011



Structure Distribution September 30, 2011



Issuer Diversification as of September 30, 2011



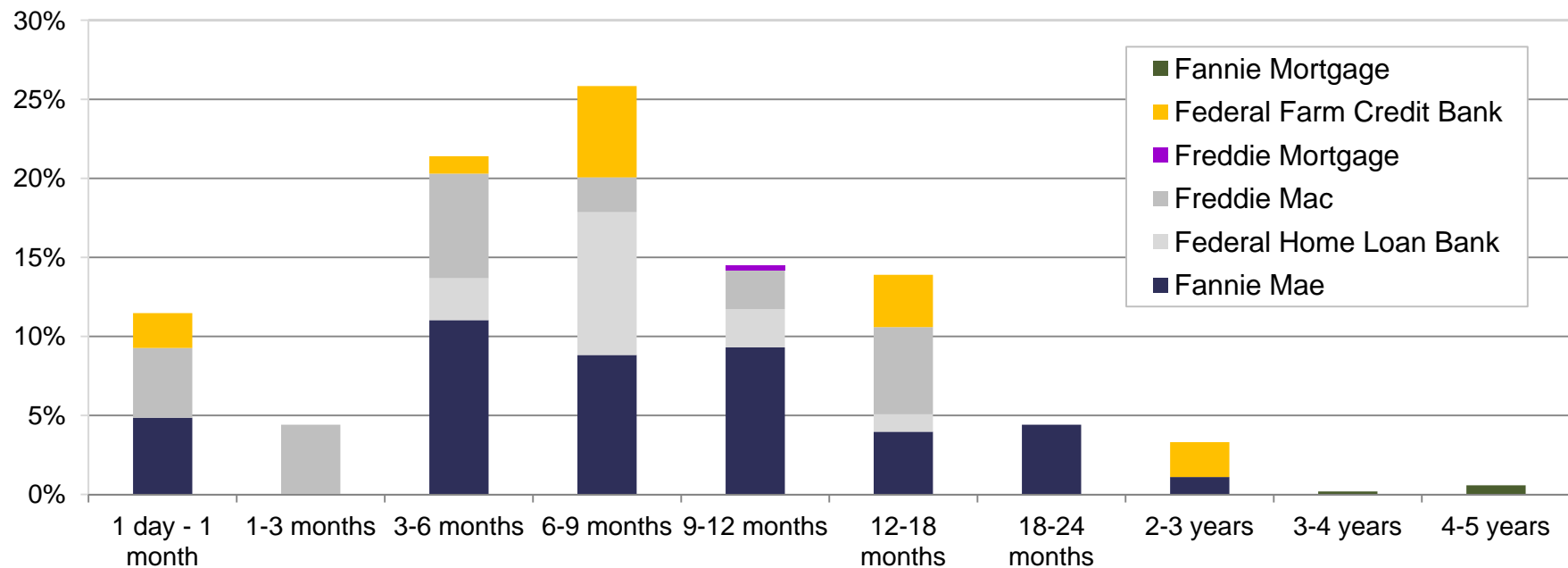
* All calculations above are based on total Agency exposure, not overall Portfolio

II. Sector Allocation – Federal Agencies



Topic	Observations
Maturity Distribution	<ul style="list-style-type: none"> The County's federal agency maturity distribution falls within the limits set forth by its Investment Policy Statement. No agency security holds a final maturity greater than five years. A majority of holdings are in securities with maturities of one year or less (77.6%), with the majority of these securities allocated between 3 to 6 months (21.4%) and 6 to 9 months (25.8%). The weighted average life of mortgage-backed federal agency securities range from 1.0 to 4.2 years. Overall, the aggregate federal agency holdings drifted to a slightly shorter maturity over the quarter, ending September 30th at 266 days compared to 270 days at June 30th.

**Federal Agency Maturity Distribution by Name
as of September 30, 2011**



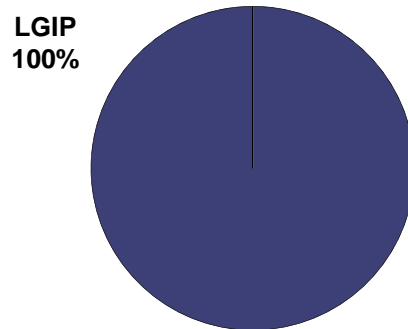
- Agency Mortgage maturities are calculated as average life. Average life data taken from Bloomberg Financial Markets
- All other Agency maturities are calculated as days to maturity

II. Sector Allocation – LGIPs and Cash Equivalents

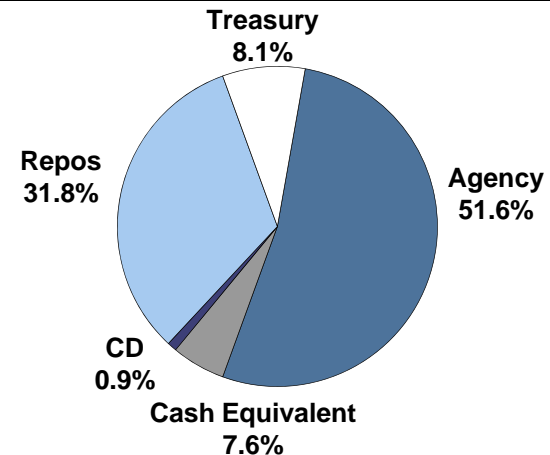


	Underlying Investments	Rating	Observations
Washington State LGIP	<ul style="list-style-type: none"> Federal Agencies 51.56% U.S. Treasuries 8.14% Cash Equivalents 7.61% Certificates of Deposit 0.93% Repurchase Agreements 31.76% <p><i>As of September 30, 2011</i></p>	<ul style="list-style-type: none"> N/A 	<ul style="list-style-type: none"> The County currently has allocated \$794 million to the Washington State LGIP (the "LGIP"). With the dollar allocation to the LGIP remaining approximately the same as the end of the 2nd quarter, normal seasonal declines in the pool's assets during the 3rd quarter are largely responsible for the relative 2% increase in the LGIP allocation to 18%. The Washington State LGIP decreased its Federal Agency and Treasury holdings, and increase its Repurchase Agreements. The LGIP ended the quarter with an allocation of 8% U.S. Treasury and 52% federal agency versus 21% and 63% last quarter, respectively. The State increased the LGIP's allocation to repurchase agreements from 9% to 32% over the quarter.

**Issuer Distribution
as of September 30, 2011**



**Washington State LGIP
Sector Distribution
as of September 30, 2011**



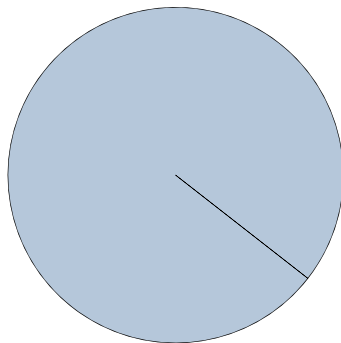
* All calculations above are based on total cash equivalents exposure, not overall Portfolio

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

II. Sector Allocation – Repurchase Agreements

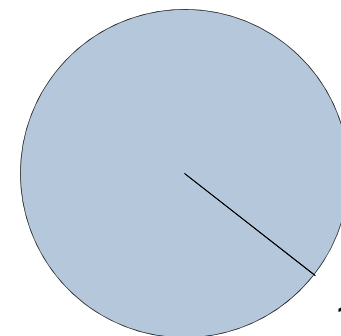
	Observations												
Issuer Diversification	<ul style="list-style-type: none"> The Pool holds two repurchase agreements from Credit Suisse in the amount of \$110 million. These securities make up approximately 2.5% of the Pool's overall holdings. The Credit Suisse repos fall within the County's Investment Policy restrictions of 10% per issuer and 40% portfolio allocation. 												
Credit Distribution	<ul style="list-style-type: none"> Ratings and Outlooks of the three major ratings agencies are as follows: <table border="1" style="margin-left: auto; margin-right: auto;"> <thead> <tr> <th><u>Credit Suisse</u></th> <th><u>Short-Term Rating</u></th> <th><u>Outlook</u></th> </tr> </thead> <tbody> <tr> <td>Standard & Poor's</td> <td>A-1</td> <td>Stable</td> </tr> <tr> <td>Moody's</td> <td>P-1</td> <td>Negative</td> </tr> <tr> <td>Fitch</td> <td>F1+</td> <td>Negative</td> </tr> </tbody> </table>	<u>Credit Suisse</u>	<u>Short-Term Rating</u>	<u>Outlook</u>	Standard & Poor's	A-1	Stable	Moody's	P-1	Negative	Fitch	F1+	Negative
<u>Credit Suisse</u>	<u>Short-Term Rating</u>	<u>Outlook</u>											
Standard & Poor's	A-1	Stable											
Moody's	P-1	Negative											
Fitch	F1+	Negative											
Conclusion	<ul style="list-style-type: none"> Overnight repurchase agreements remain an appropriate means for the Pool to provide daily/overnight liquidity. Rates on overnight repurchase agreements remain at or near their historical lows, and were volatile during the quarter, trading in a range of 0.00% - 0.30% during the quarter. Although repo rates are likely to remain in the current trading range, repurchase agreements continue to be necessary for liquidity purposes. 												

**Issuer Distribution
as of September 30, 2011**



**Credit Suisse
100%**

**Credit Distribution
as of September 30, 2011**



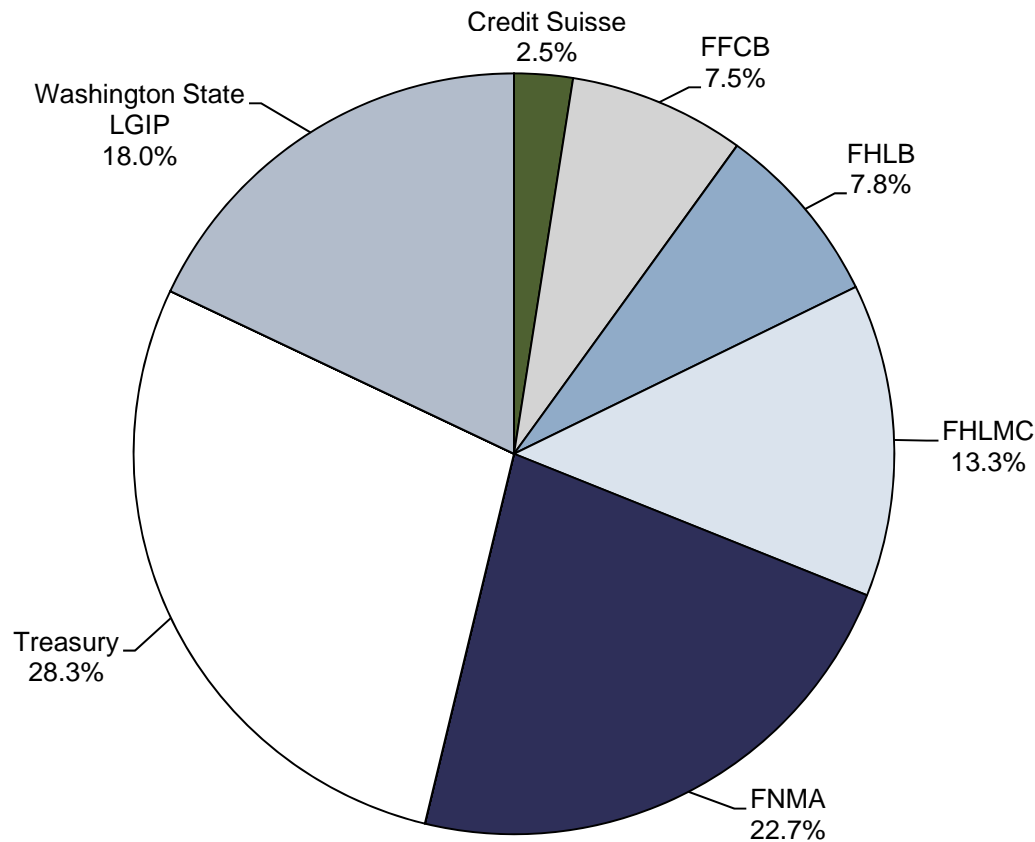
**A-1
100%**

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

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 seven individual issuers.
- A majority of holdings are allocated among U.S. government guaranteed and government supported issuers. Combined, these issuers, which include the U.S. Treasury and four federal agencies, comprise 79.6% of the entire portfolio.
- Remaining holdings are allocated to two repurchase agreements with Credit Suisse, and the Washington State LGIP.
- When the Washington State LGIP's U.S. Treasury and federal agency allocations are included, the Pool's indirect allocation to U.S. Treasury and federal agency securities jumps to 90.3% of all holdings.

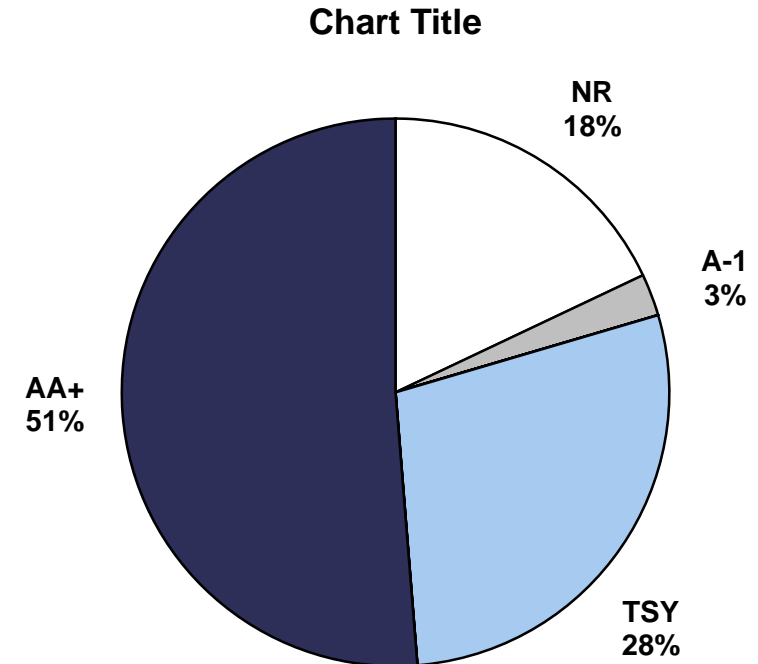


*Percentages may not add to 100.0% due to rounding.

County Investment Pool Credit Analysis

- The County Pool's overall average credit rating remains strong. This quarter represents the lowest amount of corporate exposure since PFM began analyzing the portfolio in 2008.
- Due to S&P's August downgrade of Treasuries and Federal Agencies, the County's exposure to AA+ rated securities increased significantly during the quarter. PFM believes Treasury and Agency securities remain sound investment vehicles; the downgrade warrants no action by the County.
- As of the current quarter, over 79% of holdings are either guaranteed or supported by the U.S. government. Even among corporate issuers rated A-1 by Standard & Poor's, these securities (repurchase agreements) are ultra-short and are scheduled to mature between three and four days.
- The 18% 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 September 30, 2011



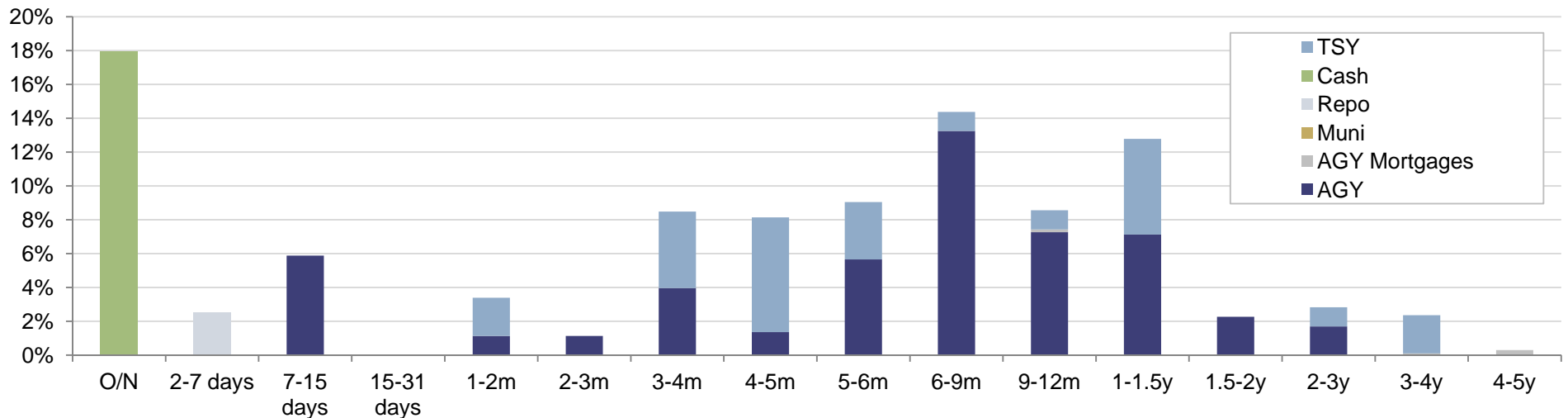
*Ratings by S&P

V. Maturity Distribution



Maturity Distribution	Observations
Weighted Average Maturity (“WAM”)	<ul style="list-style-type: none"> The County continues to diversify holdings among several maturity buckets, as seen in the chart below. During the quarter, the County added a large amount of Federal Agency purchases in the 3-month to 3-year range, as well as \$50 million in treasuries maturing in three years. By far, a majority of holdings – 79.5% of the portfolio – are scheduled to mature within the next twelve months. With the addition of some intermediate-term Federal Agency securities, the overall weighted average maturity (“WAM”) of the portfolio has increased from 225 days on June 30th to 236 days at the end of September (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 129 days, up slightly from 121 days on June 30th. Federal Agencies in the 3-6 month range helped to increase this figure. As with last quarter, even though WAMs are slightly higher than the previous quarter, this level of market risk 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	<ul style="list-style-type: none"> The County Pool appears to provide adequate liquidity, both in terms of final maturities and the sectors in which the Pool has invested. 26.3% of the portfolio’s holdings are scheduled to mature within the next thirty-one days.

Maturity Distribution as of September 30, 2011



• Agency Mortgage maturities are calculated as average life. Average life data taken from Bloomberg Financial Markets;
 • 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

- The Pool's maturity structure continues to display a high level of liquidity.
- Securities remain laddered between overnight and 4.2 years (using the weighted average life calculation for mortgage backed federal agency securities).
- Compared to previous quarters, the Pool has invested a larger amount of assets in the 3-6 month maturity bucket. As several securities either matured or were called back by their issuers during the quarter, many of the new investments were made in the 3-6 month area (par amount of \$360 million).
- Over the next few months, approximately \$300 million in callable federal agency notes are likely going to be called back by their issuer. Approximately 56.5% of the portfolio is expected to mature or be called over the next three months.

Maturity Distribution September 30, 2010 to September 30, 2011

