Quarterly Portfolio Review
King County Investment Pool

November 30, 2008

Presented by
John Molloy, CFA, Senior Managing Consultant
Robert Cheddar, CFA, Senior Portfolio Manager
PFM Asset Management LLC

Executive Summary

Purpose, Scope and Approach	• PFM Asset Management LLC ("PFM") conducted this report to update our analysis and address any Investment Pool developments since PFM's formal July review. • Our approach to this review included a detailed portfolio analysis and investment policy compliance review. • Our analysis was based on the Pool's holdings as of November 30, 2008, with some reference to holdings in past periods. • The review encompassed all 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, Credit Quality, and Maturity Structure. • The County's investment pool is of sound credit quality, well diversified, and has ample liquidity. Nearly all assets are rated at the highest quality and pose minimal risk to principal. As in July, where longer-term assets are held, they possess high investment grade or better quality ratings and an acceptable risk profile for a slightly longer-term fund. • In this report, we have made specific mention of recent developments in the Federal Agency sector as well as updated some of our commentary on the banking sector (regarding CDs).
Observations and Recommendations	• Portfolio is generally of very high quality. The gradual shortening of the maturity of the portfolio has served to reduce potential market risk. • Liquidity appears to be more than adequate given the levels of cash and cash equivalents, Washington State LGIP holdings, and marketability of Agencies. • Credit exposure is well-diversified among sectors. The reintroduction of high quality corporate instruments would provide opportunity for additional diversification. New opportunities in government guaranteed corporate instruments should be considered. • Despite recent concerns, the Agencies remain sound and are expected to be able to pay interest and principal. The level of exposure to Agencies is not a significant concern given their relative safety and support measures from the Federal Reserve and U.S. Treasury. • Recent portfolio changes, such as leveling the allocation to each agency, reduction in the regional/community CD allocation and decrease in the percentage allocated to any single issuer, should prove beneficial from a safety perspective and have served to increase the overall portfolio credit quality.

© 2008 PFM Asset Management LLC

Investment Pool Portfolio Review

Interim Portfolio Review

I. Investment Policy Compliance

II. Risk Factors by sector

- Federal Agencies
- Non-Negotiable CDs
- Repurchase Agreements
- LGIP and Cash Equivalents
- Municipal Securities

III. Overall Credit Quality

IV. Maturity Breakdown

- Overall
- Sector

© 2008 PFM Asset Management LLC

I. Investment Policy Compliance – Investment Policy Summary

Type	Maximum Portfolio Allocation	Issuer Restrictions	Credit Ratings	Maturity Restrictions
Repurchase Agreement	40%	10% per investment dealer; Firm must adopt a master repurchase agreement with the County		60 days or less
Reverse Repurchase Agreement	20% of the total balance of the investment pool at any one time	Firm must adopt a master repurchase agreement with the County		180 days or less
Local Government Investment Pool ("LGIP")	Not addressed in policy	State of Washington LGIP		N/A
U.S. Treasuries	100%	None		Up to 5 years
U.S. Agencies	75%	None		Up to 5 years
Bankers' Acceptances	40%	10%	Any BA purchase must be issued by any of the top 50 world banks in terms of assets as listed by American Banker or by approved domestic banks	Up to 180 days
Certificates of Deposit	20%	7.5% Must be a public depository in the State of Washington		Up to 5 years
Commercial Paper	25%	5% per name per Portfolio	Must carry highest ratings of any two nationally recognized rating agencies at time of purchase	180 days
Municipal Bonds	20%	5%	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	25%	Must be issued by Federal Agencies of the United States	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%	5%	Bonds must be rated "A" or better by two nationally recognized rating agencies or guaranteed by an agency of the federal government	5 years

© 2008 PFM Asset Management LLC

I. Investment Policy Compliance – County Investment Pool

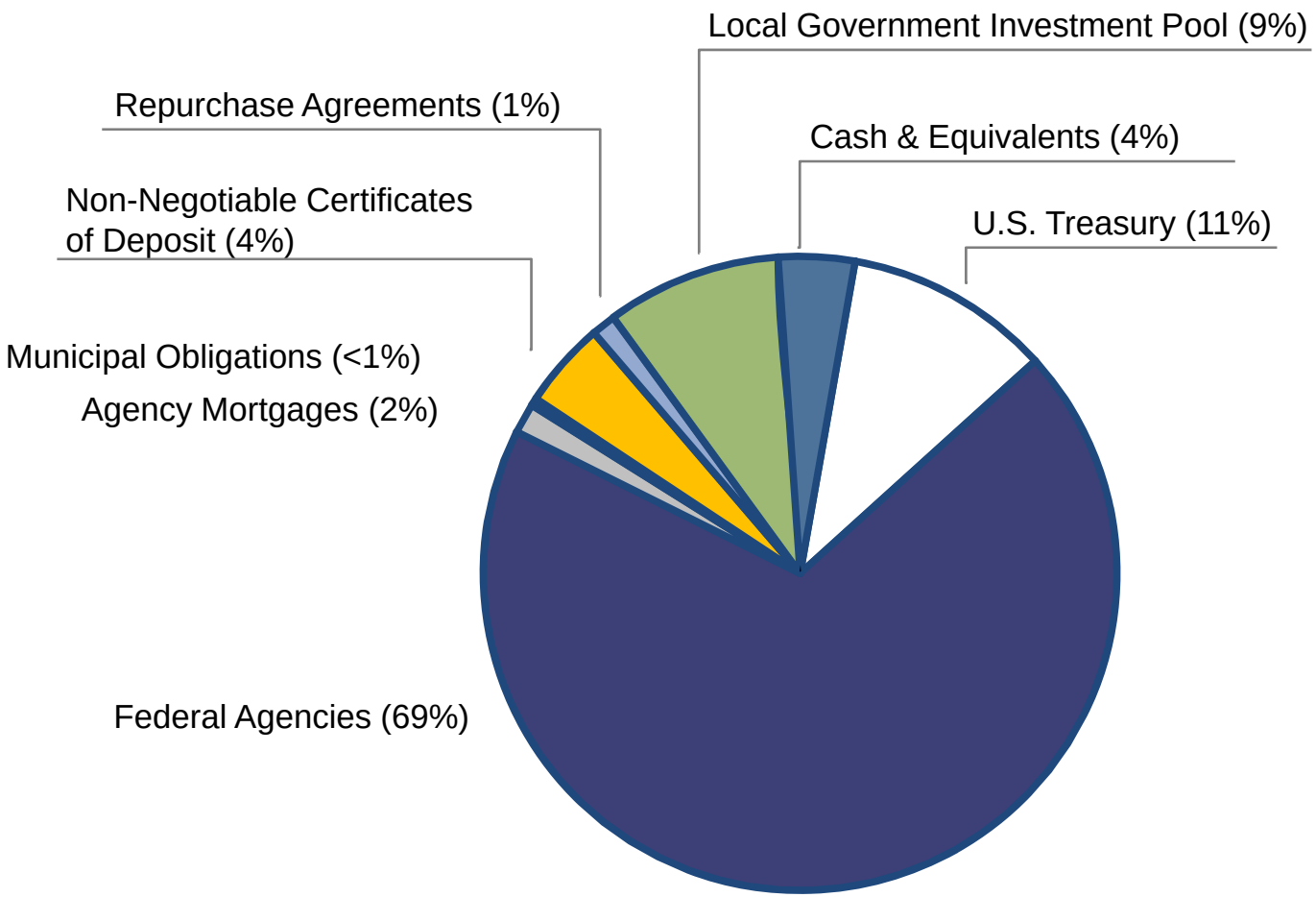
Topic	Observations
Sector Allocation	• All sectors are within the County's Investment Policy limits. Federal Agency holdings (Agency + Mortgage) are at 71%, and approaching the County's approved Agency allocation limit of 75%. The County's allocation to Municipal securities is less than 1%. Although less liquid than Treasury and Agency securities, municipals are currently adding considerable value above Treasury and Agency securities.
Credit Analysis	• All securities in the County's Investment Pool are in compliance with the County's Investment Policy per credit ratings. The portfolio holding with the lowest issuer rating (A-1) is the Key Bank savings account* valued at approximately $176 million.
Maturity Distribution	• Maturity distributions all fall within the County's Investment Policy Statement. The longest maturity for all securities is an Agency Mortgage with an average life of 4.0 years, noted in the table below. The longest maturing Agency Note has a time to maturity of 3.9 years.

Security Type	Market Value($)	Allocation Percentage	Within Policy Limits	Max Maturity Held	Within Policy Limits
Cash Equivalents	$175,686,286	3.9%	✓	1 day	✓
Commercial Paper	$0	0.0%	✓	N/A	N/A
Repurchase Agreements	$56,000,000	1.3%	✓	1 day	✓
LGIP	$403,096,564	8.9%	✓	1 day	✓
Federal Agencies	$$3,118,896,000	69.1%	✓	3.9 years	✓
Mortgages	$69,348,571	1.5%	✓	4.0 years	✓
Certificates of Deposit	$200,000,000	4.4%	✓	3.6 months	✓
Municipal Bonds	$17,335,000	0.4%	✓	2.6 years	✓
U.S. Treasury	$475,000,000	10.5%	✓	1.9 years	✓

**Based on Key Bank NA Certificate of Deposit rating by Standard and Poor's*

© 2008 PFM Asset Management LLC

Sector Diversification
as of November 30, 2008

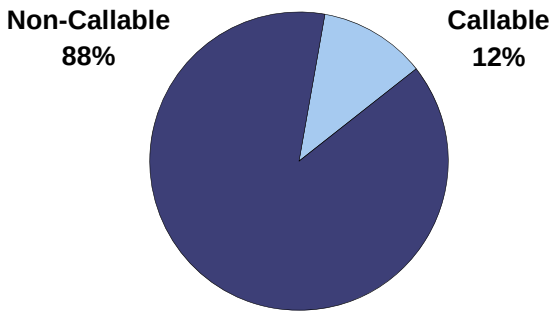


© 2008 PFM Asset Management LLC

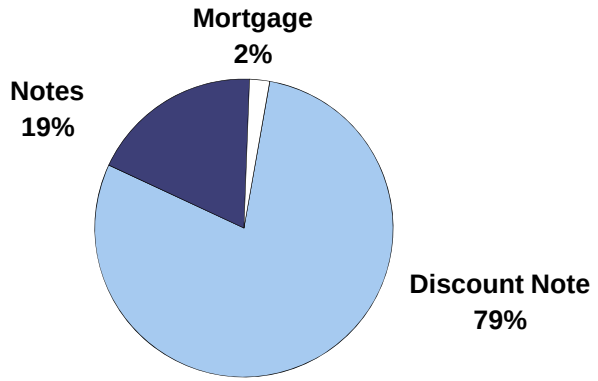
II. Risk Factors by Sector – Federal Agencies

Topic	Observations
Structure	• Non-Callable 88% • Callable 12% • Discount Note 79% • Notes 19% • Agency Mortgage 2%
Diversification	• Freddie Mac (FHLMC) 35% • Federal Home Loan Bank (FHLB) 29% • Fannie Mae (FNMA) 27% • Federal Farm Credit Bank (FFCB) 8% • FNR (Mortgages) 1% • FHR (Mortgages) <1%
Conclusions	• On September 7, 2008 the U.S. Treasury Department placed Fannie Mae and Freddie Mac under conservatorship of the Federal Housing Finance Agency ("FHFA"). With this, the U.S. Government has implemented an even stronger commitment of support for the Agencies' debt. As described more fully later in this report, we continue to be of the opinion that Federal Agencies' senior debt is an appropriate investment for public entities.

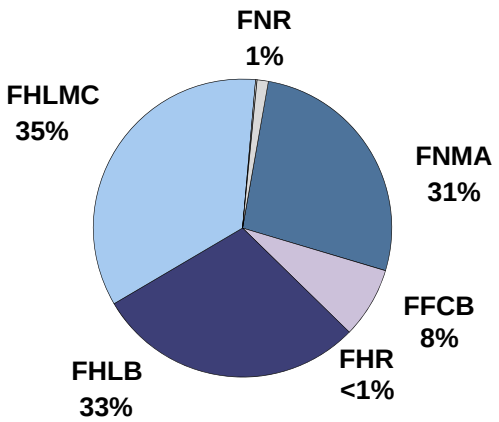
Callable vs. Non-Callable
as of November 30, 2008



Structure Distribution
as of November 30, 2008



Issuer Diversification
as of November 30, 2008

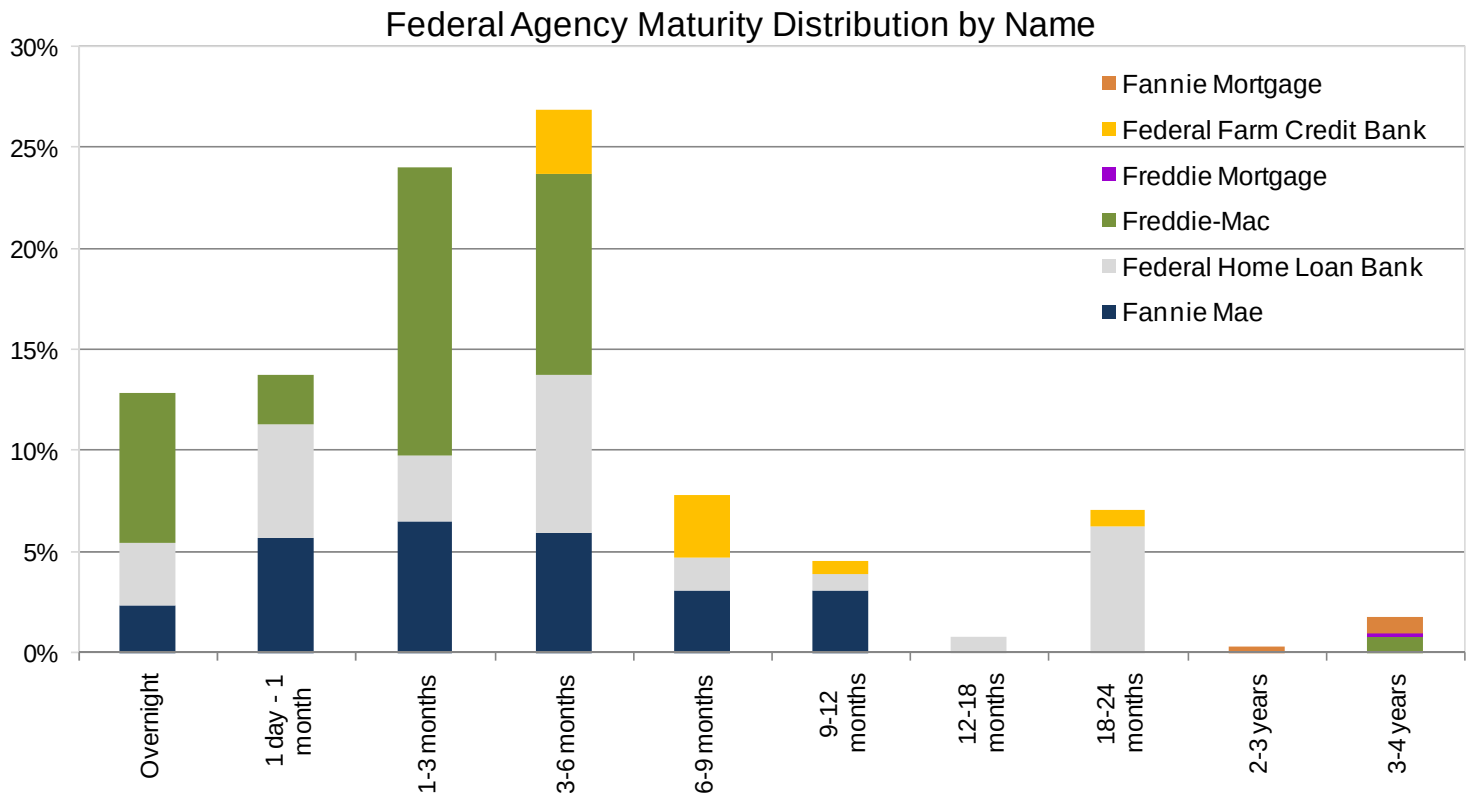


** All calculations above are based on total Agency exposure, not overall Portfolio*

© 2008 PFM Asset Management LLC

II. Risk Factors by Sector – Federal Agencies

Topic	Observations
Maturity Distribution	• Maturity distributions all fall within the County's Investment Policy Statement. The longest maturity for all securities is an Agency Mortgage with an average life of 4.0 years, as seen in the table below. The longest maturing Agency Note has a time to maturity of 3.9 years. • Agency holdings are well diversified by issuer and maturity as well as simply by issuer. The high level of overnight maturities in the Agency holdings (see chart below) were not actually overnight investments but securities that had been purchased over a longer period of time. The County planned the maturity of these investments to expected pool outflows (debt service payments and other expenditures) for December 1st. The County appears to maintain adequate liquidity through other holdings (Washington State LGIP, repurchase agreements, and Key Bank account).



- 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

© 2008 PFM Asset Management LLC

II. Discussion Regarding FDIC-Insured Commercial Paper and Corporate Notes

Topic	Comments on FDIC-insured Corporate Securities
Conclusion	With a majority of pool assets invested in Federal Agency instruments, we understand the County's concern for the credit standing, and ultimately the safety of these investments. • We continue to view Fannie Mae, Freddie Mac, Federal Home Loan Bank, and Federal Farm Credit Bank senior debt as a suitable investment for public agencies. The support arrangements for Fannie Mae and Freddie Mac are substantial. Recently Treasury, Federal Reserve and FHFA officials have used strong language to communicate their support for the GSE's. This opinion is based on the following:

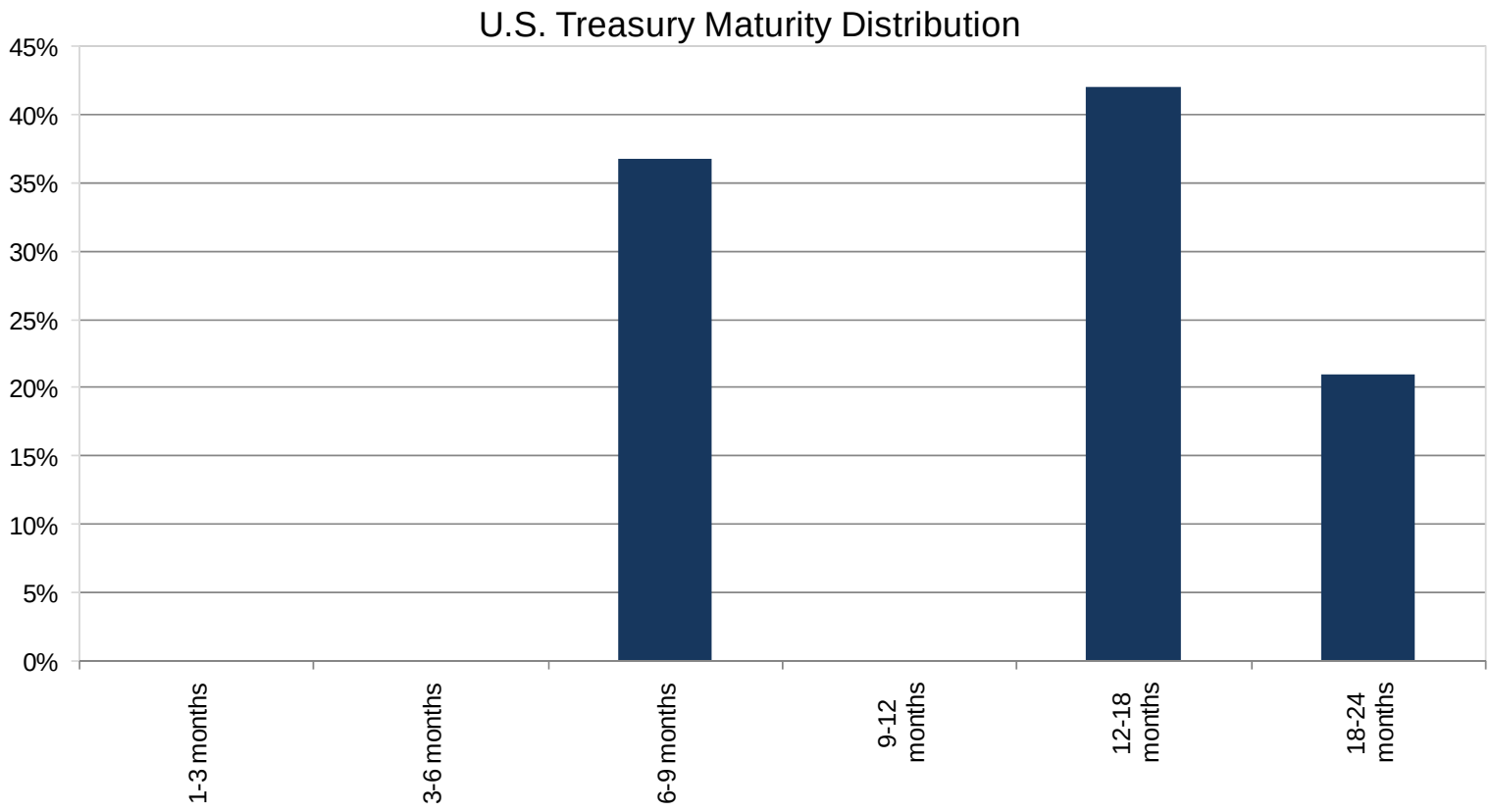
Recent Federal action	• With the passage and signing of the recent Housing Recovery bill Fannie Mae and Freddie Mac have additional government support in place to bolster their activities. Specifically the bill and other measures include:
	  • The Federal Reserve may lend directly to Fannie Mae and Freddie Mac at the primary credit rate (now 2.25%) that it makes available to investment banks. This lending facility would be in place for 18 months, but could be extended if needed.
	  • The GSEs' line of credit to the Treasury which now totals $2.25 billion has been increased as much as $300 billion. This line would be used to provide liquidity to the agencies if needed.
	  • The Treasury is now permitted to make direct equity investments in the two GSEs in unlimited amounts if necessary. In November, in line with Freddie Mac's agreement with Treasury under the terms of conservatorship the company has submitted a requested for $13.8 billion in capital from The Treasury Department. This will allow Freddie Mac to maintain positive stockholders equity. Freddie Mac will be eligible to apply for additional capital if further losses are taken. Fannie Mae is also able to apply for capital infusions if their equity position becomes negative.
	  • The Federal Reserve will assume a "consultative role" in regulating the agencies.
	  • The Treasury also will offer a temporary large line of credit to the Federal Home Loan Banks.

Quality of mortgage portfolios	• Agency mortgage portfolios remain well diversified and historically have experienced significantly lower credit losses than bank portfolios. • It is likely that both Fannie Mae and Freddie Mac will experience further losses, but those losses are likely to be much lower than other financial institutions.
Recent market activities	• The Fed has started to purchase agency securities in the open market. This provides additional support to the agency sector. As a result, agency spreads have dropped dramatically. Fannie Mae, Freddie Mac and FHLB will likely be used as policy tools to help stabilize the mortgage and housing markets.

© 2008 PFM Asset Management LLC

II. Risk Factors by Sector – U.S. Treasury Securities

Topic	Observations
Maturity Distribution	• Maturity distributions all fall within the County's Investment Policy Statement. U.S. Treasury securities are allocated between 7 months and 2 years. • Treasury holdings have nearly doubled as a percentage of portfolio holdings in the last 3-4 months. • Nearly 80% of Treasury securities are coupon bearing notes; 20% of Treasury holdings are discount bills.



© 2008 PFM Asset Management LLC

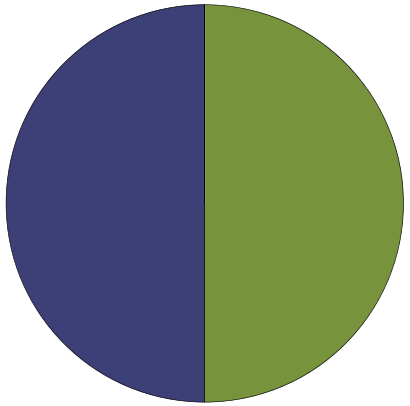
II. Risk Factors by Sector – Non-Negotiable Certificates of Deposit

Issuing Bank	Short-Term Credit Rating	Max Maturity (days)	Total Par Value
Bank of America NA	A-1+/P-1/F1+	96	$100,000,000
U.S. Bank NA	A-1+/P-1/F1+	110	$100,000,000

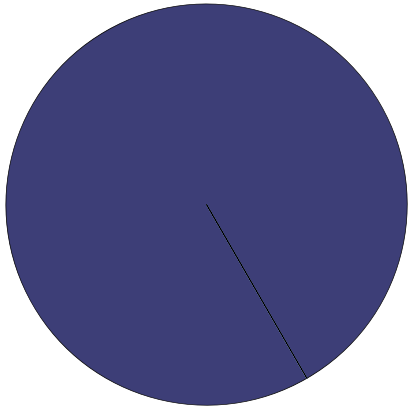
Conclusion

- The County has allocated 100% of its CD balance towards highly rated, large, national corporate and banks.
- We encourage the County to continue making any new CD investments with the highly rated larger national corporate banks.
- A variety of recently created government programs have served to stabilized the commercial banking sector. This is especially true of the banks that have received capital injections and are issuing debt under the Temporary Liquidity Guarantee Program. It now seems unlikely that a large commercial bank will be allowed to fail.
- The County may wish to consider allocating some funds to investments under the umbrella of the TLGP program. Guaranteed commercial paper and corporate bonds can be purchased that carry the full faith and credit of the US government. Floating rate instruments issued under this program may be of particular interest to a money market fund or pool.
- There may still be risk in smaller banks, as described in our previous reports. The FDIC troubled bank list continues to grow and there have been additional failures. Care should be taken when investing in this sector outside of the FDIC insurance of the TLGP program
- The County's CD exposure has fallen from 8% in July to 4% at the end of November.

Issuer Diversification
as of November 30, 2008



Credit Distribution (S&P)
as of November 30, 2008



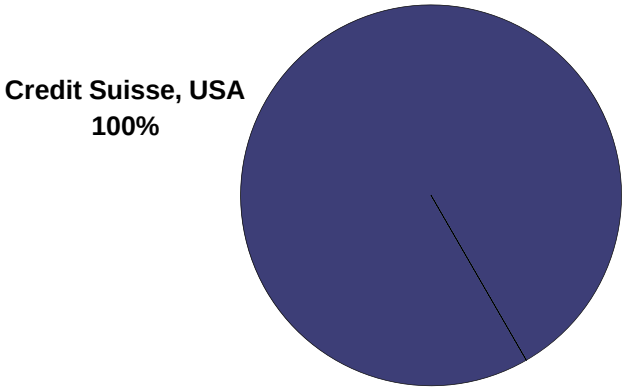
** All calculations above are based on total CD exposure, not overall Portfolio*

© 2008 PFM Asset Management LLC

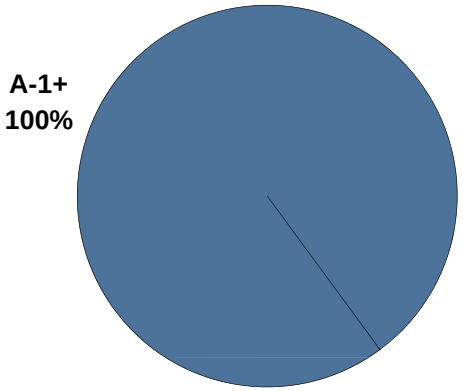
II. Risk Factors by Sector – Repurchase Agreements

	Counter-Party Risk	Collateral Sufficiency
Observation	• As of November 30, the only Repurchase Agreement counterparty used was Credit Suisse. • Credit Suisse, USA is a highly rated broker/dealer. • On December 4, Standard & Poor's placed the short- and long-term ratings of Credit Suisse USA on "Watch Effective." The County should frequently monitor the credit status of Credit Suisse for possible changes to its credit rating.	• The County monitors collateral on a daily basis and limits collateral to Treasury and Agency securities. • Substitutions are permitted.
Conclusion	• We see little risk in Credit Suisse as a counterparty. • The County advised us in April that it had recently completed legal agreements expanding the number of counterparties. • To safeguard against the potential that Credit Suisse may not be able to provide the County with capacity each day, we recommend the County periodically shop its repurchase agreement placements and place a portion of its allocation with other counterparties. This competitive bidding process may also enhance the County's yield for this allocation.	• The County should continue to permit only Treasury and Federal Agency collateral. • The County should continue to monitor the market value of collateral on a daily basis to ensure the committed amount and type is sufficient.

Issuer Distribution
as of November 30, 2008



Credit Distribution
as of November 30, 2008



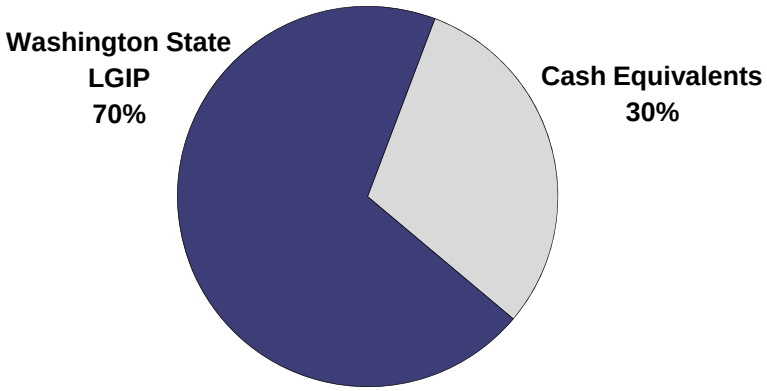
** All calculations above are based on total Repo exposure, not overall Portfolio*

© 2008 PFM Asset Management LLC

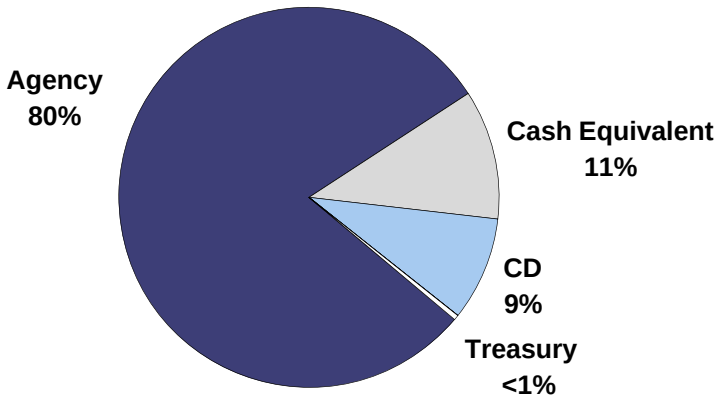
II. Risk Factors by Sector – LGIPs and Cash Equivalents

	Underlying Investments	Rating	Observations
Washington State LGIP	• Federal Agencies 79.7% • Repurchase Agreements 0.0% • Certificates of Deposit 8.9% • Cash Equivalents 11.0% • U.S. Treasuries 0.4% *As of 11/30/2008*	• N/A	• The State LGIP's 80% allocation to Federal Agencies indirectly raises the County pool's exposure to Federal agencies to 78%.
Key Bank, NA Overnight Savings Account	• Not known	• A-1 short-term by S & P; on negative outlook • P-1 short-term by Moody's • F1 short-term by Fitch	• The County holds approximately $176 million in the Key Bank savings account. At just under 4% of total pool assets, this holding falls within our recommendation of limiting issuer exposure to no more than 5%. With Key Bank on negative outlook, we encourage the County to diligently monitor the amount in the savings account to ensure it does not exceed appropriate levels.

Issuer Distribution
as of November 30, 2008



Washington State LGIP
Sector Distribution
as of November 30, 2008



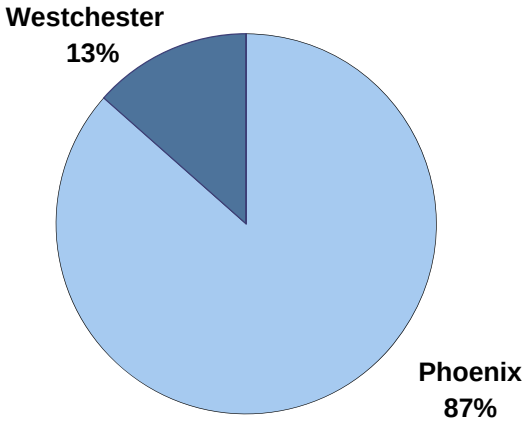
** All calculations above are based on total cash equivalents exposure, not overall Portfolio*

© 2008 PFM Asset Management LLC

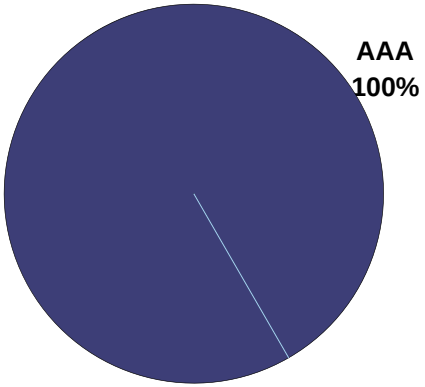
II. Risk Factors by Sector – Municipal Bonds

	Observations
Issuer Diversification	• Since our last portfolio review in July 2008, the County's Sacramento, CA holding has matured. Since then, the County has not taken additional action regarding its municipal security holdings. This maturity has increased the pool's municipal credit distribution to 100% AAA securities (rated by Standard & Poor's) • Current municipal allocation is $17 million (or 0.40% or portfolio holdings) compared to $38 million (1.00% of portfolio holdings) as of July 31, 2008.
Credit Distribution	• At this time, we see no adverse credit issues with the Westchester and Phoenix bonds. The municipal bond holdings carry investment grade long term credit rating from Standard and Poor's, Moodys, and/or Fitch.
Conclusion	• There have been no ratings changes on either issue since our July report. Both issues represent minimal credit risk. • Ongoing market disruptions may limit liquidity of municipal issues which may have the potential to impair pricing temporarily. • As yields on U.S. Treasury and other short-term securities have fallen dramatically, municipal securities now offer significant yield advantage. The County may wish to selectively add exposure to the municipal sector; however, as with any spread product, we recommend a detailed credit review prior to any potential purchases.

Issuer Distribution
as of November 30, 2008



Credit Distribution
as of November 30, 2008



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

© 2008 PFM Asset Management LLC

II. Risk Factors by Sector – Municipal Bonds (cont'd.)

Issuer	Underlying Credit Rating of Issuer	Credit Rating of Bonds	Insurance Provider	Insurance Provider Rating
Phoenix, Arizona Unlimited General Obligation	Aa1/AAA	Aa1/AAA	N/A	N/A
	• Phoenix Arizona has benefited from changing demographics within the US, making it one of the fastest growing cities in the country. • The economy is well diversified with thriving education and research, high-tech, telecom, and tourism industries. Also, they are positioned in what may become the "Persian Gulf of alternative energy", with great prospects for wind and solar power generation. Payroll growth continues to be strong and the unemployment rate is 4.1%. • The bonds are rated Aa1/AAA and there are no watches on the ratings. • **The debt obligations of the City of Phoenix Arizona represent minimal risk.**			
Westchester County, New York Unlimited General Obligation	Aaa/AAA/AA+	Aaa/AAA/AA+	N/A	N/A
	• Westchester County New York is comprised of suburban communities with commuters traveling to both New York City and Greenwich and Stamford CT. • The county includes some of the wealthiest zip codes in the US. While there may be some concentration of risk based around a slowdown in the financial markets, the county has not yet felt any pressure. • The bonds are rated Aaa/AAA/AA+ and Fitch, the only rating agency to not have a AAA rating on them put a positive outlook on the bonds in October 2006. • **The debt obligations of Westchester County have minimal risk.**			

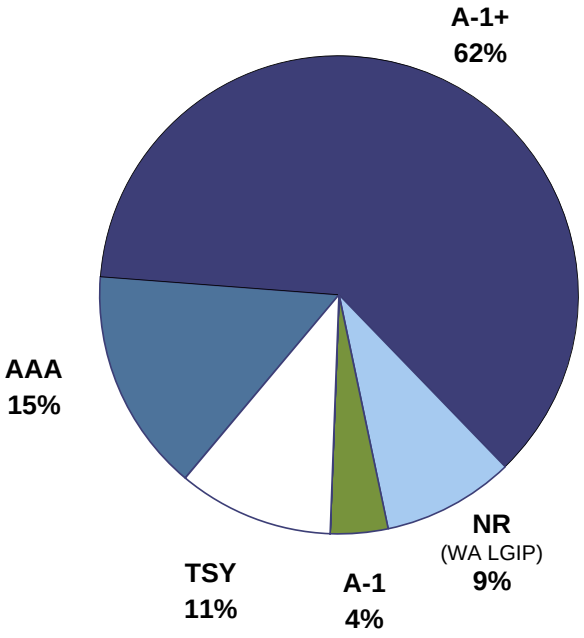
Ratings as of December 9, 2008

III. Credit Quality

County Investment Pool Credit Analysis

- Since our July portfolio summary, the County Pool's overall average credit rating has increased. The maturity of certain Certificates of Deposit, an increase in the Agency and Treasury holdings, and modest reduction on the not rated Washington State LGIP have all pushed the credit profile of the pool higher.
- Over 87% of the County's Pool investments are in the highest rating category by Standard and Poor's, including 15% rated AAA, 62% rated A-1+, and 11% rated Treasury.
- We are unable to determine a specific rating for the Key bank overnight savings account. A Key Bank Certificate of Deposit has a short term rating of A-1; we've used this rating in evaluating the Key bank account in the chart at right. Standard and Poor's has Key Bank on negative outlook, which bears monitoring.
- The Washington State LGIP does not carry a rating, although the pool's underlying investments are 80% Federal Agency securities.

Credit Distribution*
as of November 30, 2008

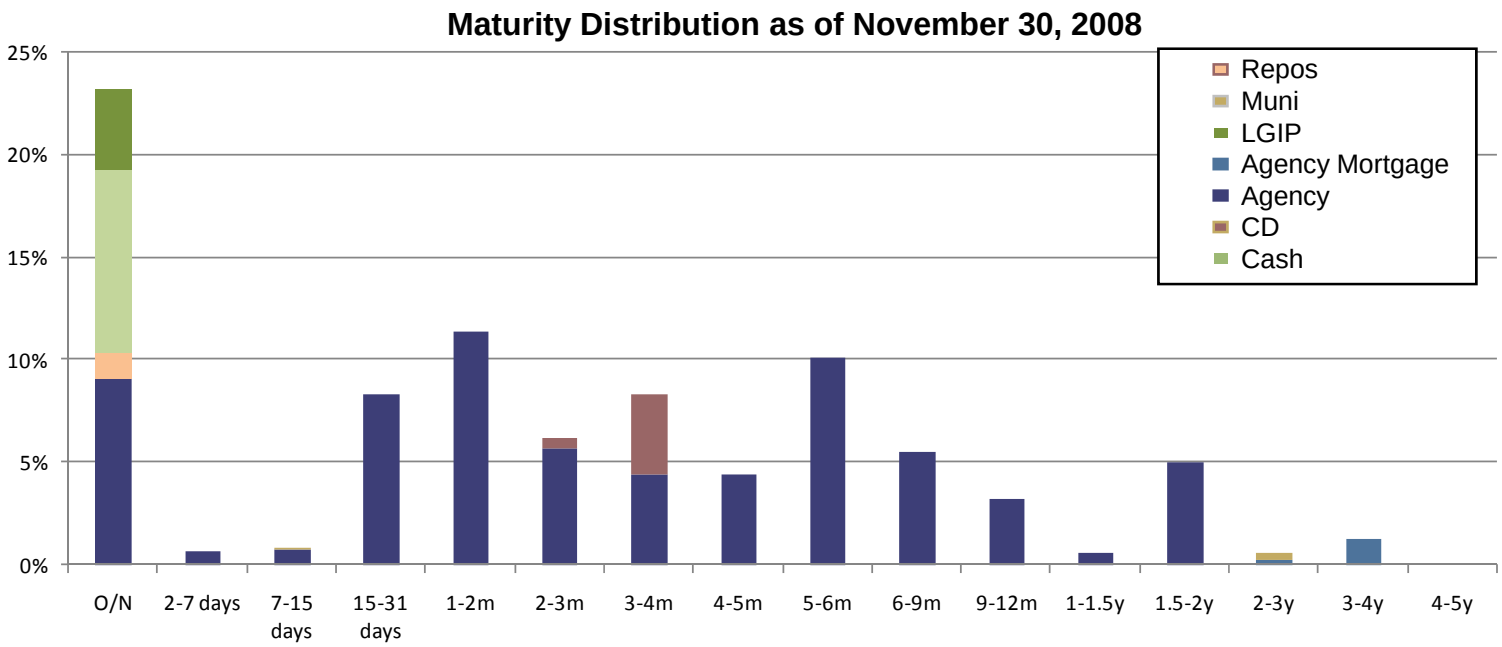


*Ratings by S&P

© 2008 PFM Asset Management LLC

IV. Maturity Distribution

Maturity Distribution	Observations
Weighted Average Maturity ("WAM")	• The overall weighted average maturity ("WAM") of the portfolio is 169 days (viewing callable securities to their call dates and mortgage securities on an average life basis). • If securities with maturity longer than one year are excluded, the remaining "short" portfolio has a weighted average maturity of 70 days.
Liquidity	• The portfolio appears to maintain more than adequate liquidity. Just over 14% of securities are allocated towards "overnight" liquid vehicles, such as the Washington State LGIP, the Key Bank overnight savings account and Repurchase Agreements. Over 32% of the portfolio matures within 31 days. • Additional analysis would be required to determine if the allocation between shorter and longer maturity securities is appropriate. Detailed history of pool balances, inflows and outflows would be needed.



- 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.

© 2008 PFM Asset Management LLC