



Town of Fountain Hills Quarterly Investment Review Quarter Ended September 30, 2013



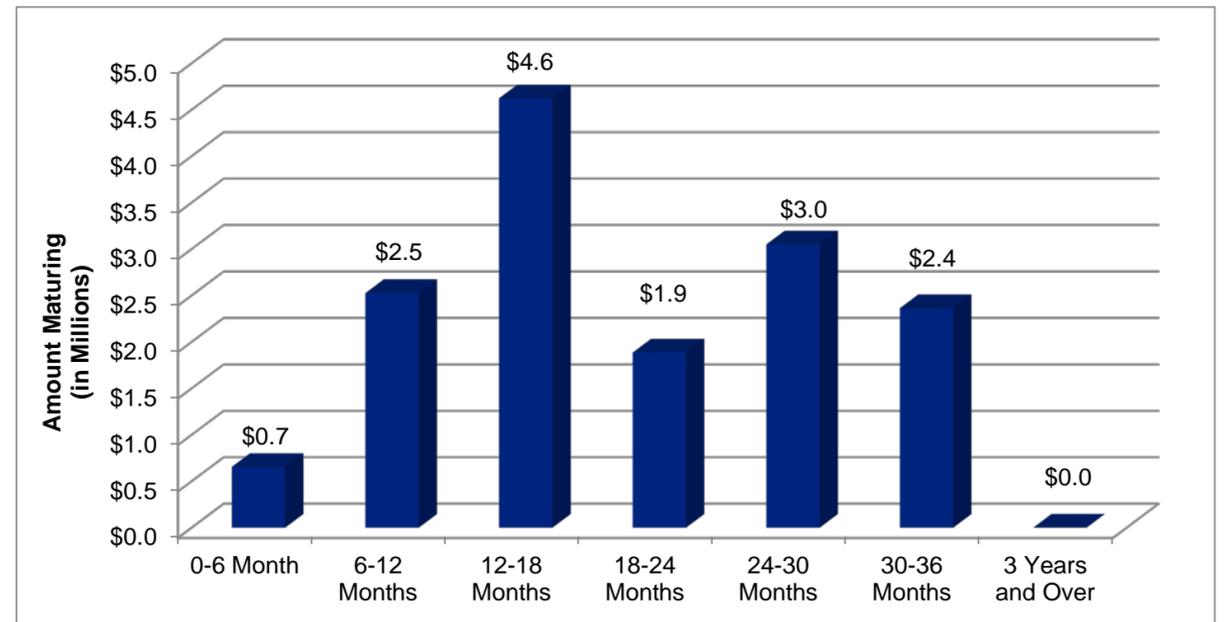
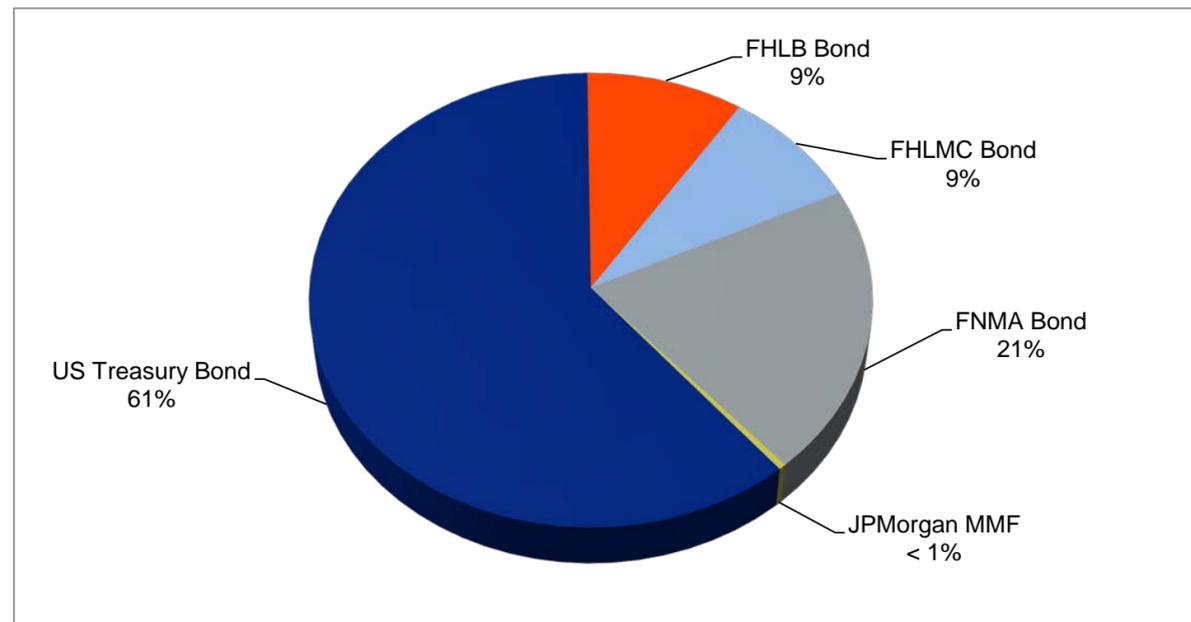
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Town of Fountain Hills Portfolio Summary Quarter Ending September 30, 2013

Summary By Type	Book Value	Market Value	Days to Maturity	% of Portfolio	% Allowed per Policy	YTM @ Cost
US Treasury Bond	9,226,673	9,233,596	643	60.91%	100%	0.41
FHLB Bond	1,440,100	1,442,989	376	9.52%	100%	0.51
FHLMC Bond	1,305,181	1,308,630	516	8.63%	100%	0.49
FNMA Bond	3,106,012	3,113,219	643	20.54%	100%	0.61
JPMorgan MMF	60,916	60,916	1	0.40%	N/A	0.01
Total including cash	15,138,882	15,159,349	604	100.00%		0.46
Total without cash	15,077,966	15,098,434				0.47

Summary by Issuer	Book Value	% of Portfolio
US Treasury	9,226,673	60.9%
FHLB	1,440,100	9.5%
FHLMC	1,305,181	8.6%
FNMA	3,106,012	20.5%
JPMorgan	60,916	0.4%
Total / Average	15,138,882	100%



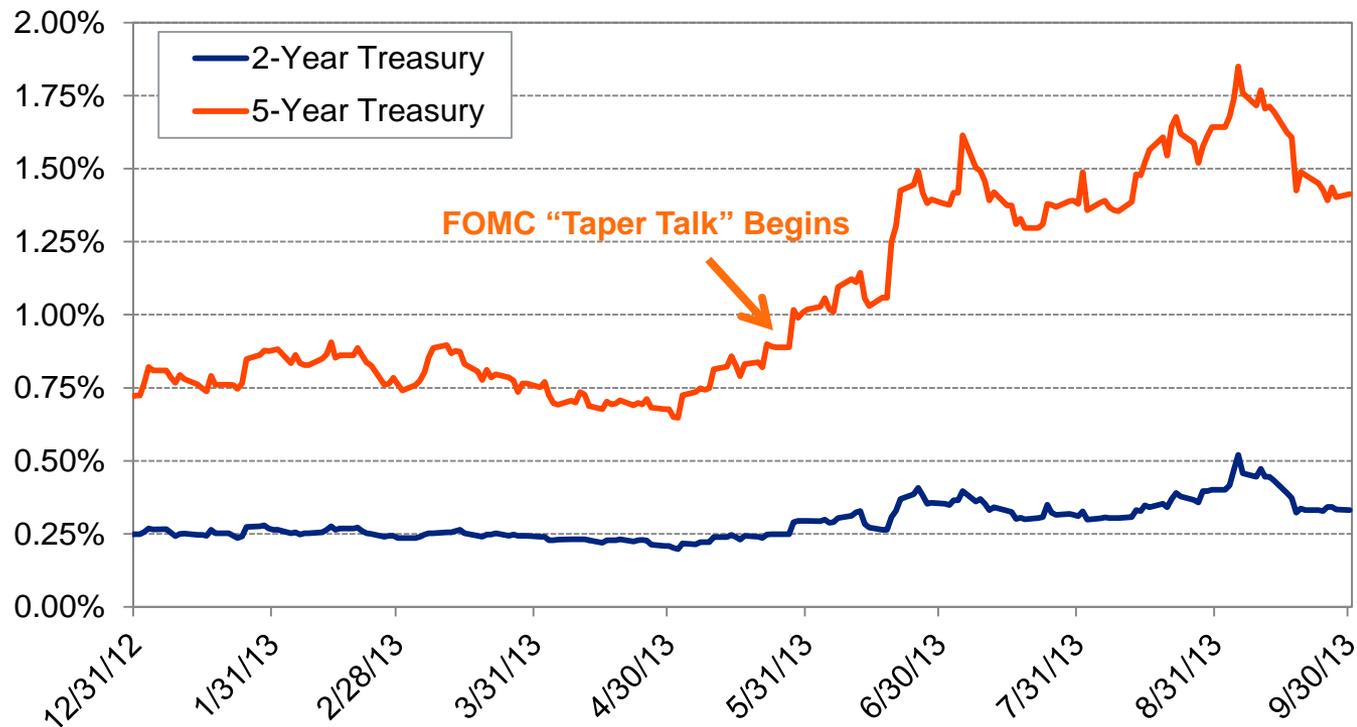
Weighted Average Maturity (in years)	1.66
Duration Allowed by Policy	5.00
Current Portfolio Duration including cash	1.63
Current Portfolio Duration without cash	1.63

End of quarter trade-date market values of portfolio holdings, including accrued interest.

Rates Rise On Anticipation of Fed Stimulus Tapering

- Interest rates rose throughout the third quarter as investors anticipated a reduction, and eventual completion, of FOMC's monthly \$85 billion asset purchases.
- There was little movement in short-term yields (maturities less than a year) as these maturities remained anchored by Fed Policy.

2- and 5- Year U.S. Treasury Yields
December 2012 – September 2013

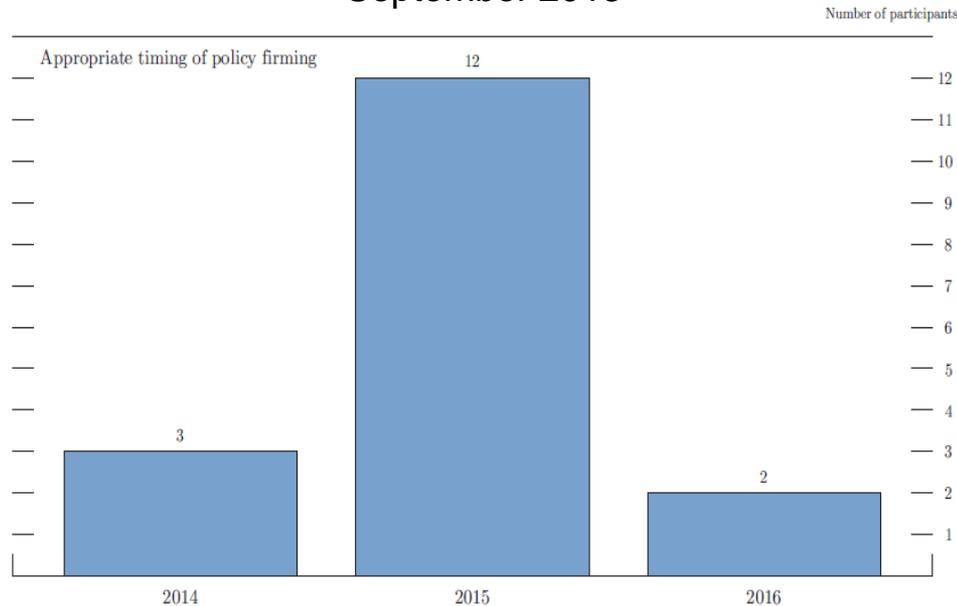


Source: Bloomberg

Taper Tantrum

- The Fed surprised the market at its September meeting with the decision to continue its \$85 billion bond buying program.
“...the Committee sees the improvement in economic activity and labor market conditions since it began its asset purchase program a year ago as consistent with growing underlying strength in the broader economy. However, the Committee decided to await more evidence that progress will be sustained before adjusting the pace of its purchases.”
- Fed continued to hold its overnight rate at 0.00%-0.25%.

Appropriate Timing of Policy Firming September 2013



Source: Federal Reserve

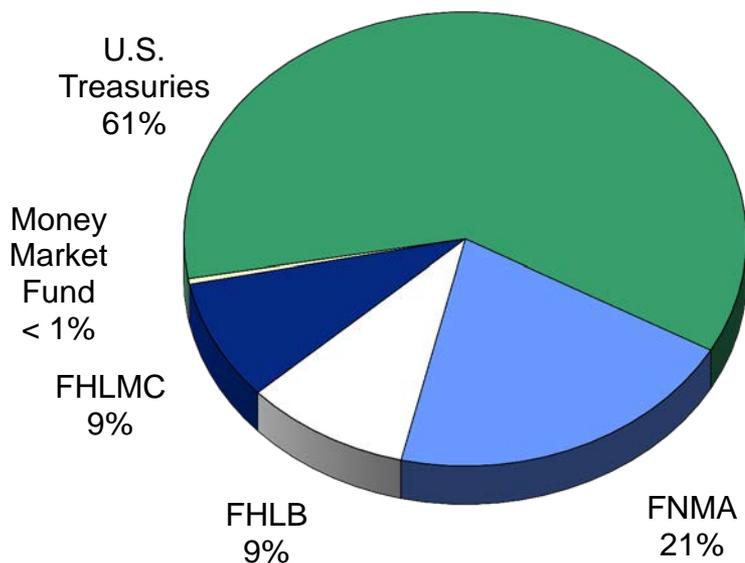
Third Quarter 2013 Strategy

- Interest rates trended gradually higher during the quarter following modest economic expansion and on expectations the Fed would taper their bond purchases.
- The Federal Reserve must eventually curtail its bond purchases and rates will begin to normalize from artificially low levels.
- The key components of our strategy included:
 - Maintaining the portfolio's duration near the benchmark by executing extensions at strategic points to guard against market volatility.
 - Executing purchases when rates were near the top of their recent range.
 - Focusing on identifying “relative value”; seeking those sectors, maturities and issues that offer the best potential for favorable returns in the context of the overall portfolio.
 - Avoiding the callable sector due to increased volatility.
- Performance relationships normalized during the third quarter with Federal Agencies enhancing overall performance.

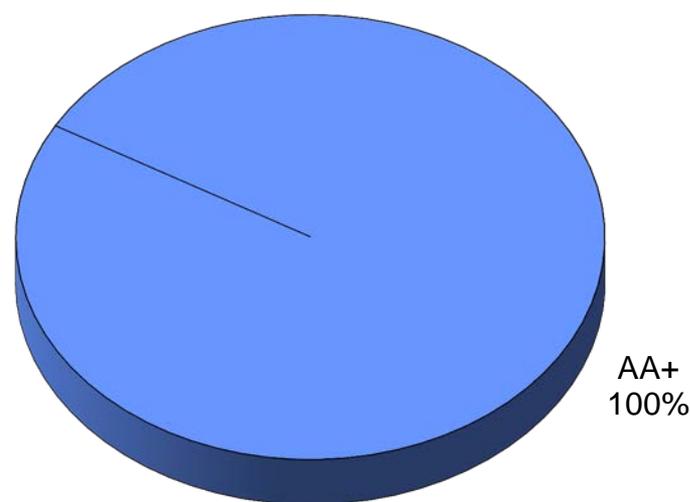
Portfolio Composition and Credit Quality Characteristics

Security Type ¹	September 30, 2013	% of Portfolio	% change from prior quarter	Permitted by Policy
U.S. Treasuries	\$9,233,595.95	61%	-5%	100%
Federal Agencies	\$5,864,837.71	39%	+6%	100%
<i>FNMA</i>	<i>\$3,113,218.82</i>	<i>21%</i>	+4%	-
<i>FHLB</i>	<i>\$1,442,989.24</i>	<i>9%</i>	+2%	-
<i>FHLMC</i>	<i>\$1,308,629.65</i>	<i>9%</i>	-	-
Money Market Fund	\$60,915.52	< 1%	-1%	
Totals	\$15,159,349.18	100%		

Portfolio Composition



Portfolio Credit Quality Distribution



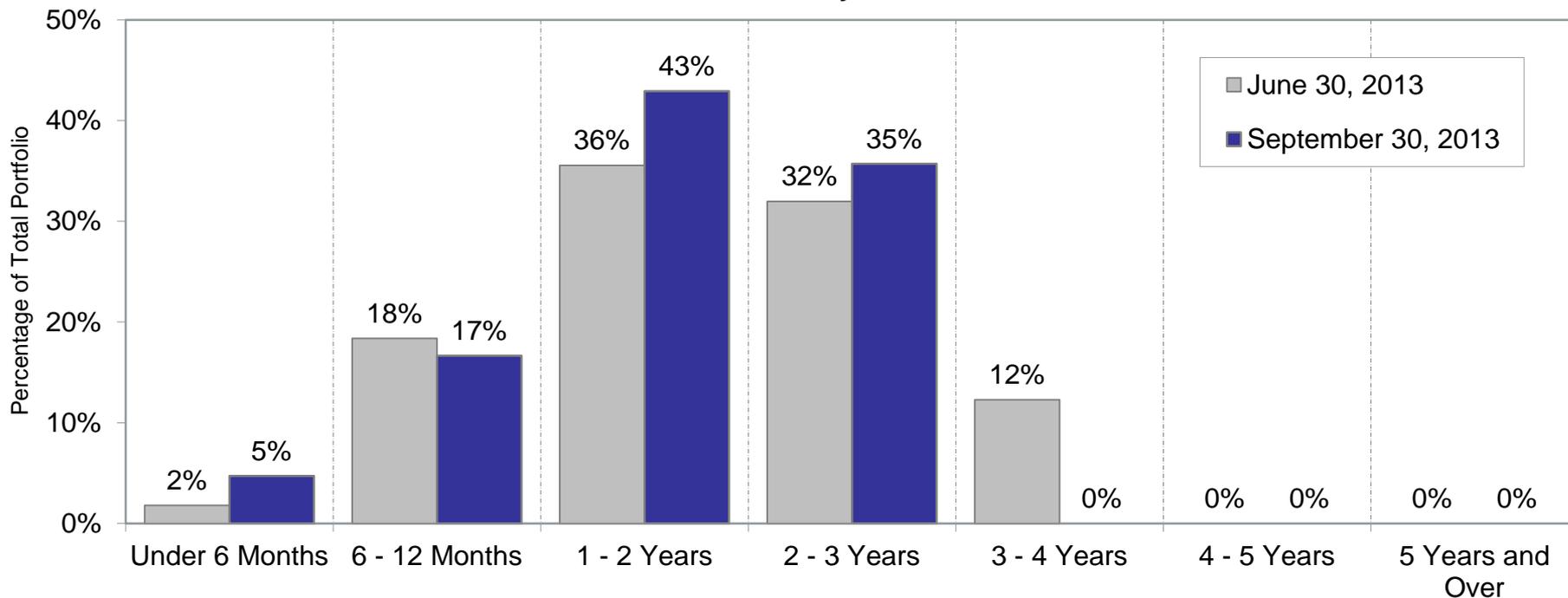
Ratings by Standard & Poor's

1. End of quarter trade-date market values of portfolio holdings, including accrued interest.

Portfolio Maturity Distribution

Maturity Distribution	September 30, 2013	June 30, 2013
Under 6 Months	\$714,804.14	\$271,553.16
6 - 12 Months	\$2,525,550.36	\$2,779,397.28
1 - 2 Years	\$6,506,932.96	\$5,377,059.27
2 - 3 Years	\$5,412,061.72	\$4,835,462.32
3 - 4 Years	\$0.00	\$1,856,952.70
4 - 5 Years	\$0.00	\$0.00
5 Years and Over	\$0.00	\$0.00
Totals	\$15,159,349.18	\$15,120,424.73

Portfolio Maturity Distribution



Strategic Timing of Duration Extension

- Bond market indices change every month—shorter maturity bonds drop out and newly-issued or longer maturity bonds roll into the designated maturity range (e.g. 1-3 year, 1-5 year)—causing the average maturity of the typical bond index to change at the beginning of each new month.
- Over the past year PFM's strategy has included executing monthly trades to align the portfolio with the benchmark. However, because rates were rising during the early part of the third quarter, PFM chose not to extend at the end of June/beginning of July, preferring to wait as rates marched higher.
- We finally extended the portfolio duration at the end of August, which worked out well for the portfolio as rates fell sharply in September.



Source: Bloomberg

Investment In Longer-Term Securities

- We increased the portfolio's allocation to Federal Agencies to take advantage of favorable spreads between this sector and Treasury Notes. As the yield curve remained steep, we sold shorter maturing securities and reinvested the proceeds in a 2.5-year Agency.

Trade Date	Transaction	Security	Maturity	Par Value	Yield	Realized Gain
8/8/13	Buy	FHLB Note	8/28/15	\$430,000	0.38%	-
8/8/13	Sell	US Treasury	7/31/15	\$325,000	0.32%	\$88
8/29/13	Buy	FNMA Note	3/30/16	\$500,000	0.71%	-
8/29/13	Sell	FHLMC Note	10/30/13	\$125,000	0.06%	\$81
8/29/13	Sell	US Treasury Note	3/15/14	\$350,000	0.09%	\$488

2-Year Treasury-Agency Yield Spread



Source: Bloomberg

Q3 Recoups Some of Q2 Losses

As of 9/30/13

Returns for periods ended 9/30/13

	Effective Duration	Yield	YTD	1 Month	3 Month	1 Year	3 Years
1-3 Year Indices							
U.S. Treasury	1.90	0.25%	0.30%	0.23%	0.29%	0.37%	0.71%
Agency	1.75	0.31%	0.27%	0.20%	0.30%	0.39%	0.87%
Corp A-AAA	1.93	1.02%	0.95%	0.35%	0.74%	1.39%	2.22%
MBS (0 to 3 Years)	1.78	0.87%	0.03%	0.50%	1.03%	(0.28%)	1.92%
Municipals	1.83	0.52%	0.73%	0.20%	0.47%	0.76%	1.25%
1-5 Year Indices							
U.S. Treasury	2.70	0.34%	(0.08%)	0.51%	0.46%	(0.03%)	1.16%
Agency	2.48	0.42%	(0.09%)	0.50%	0.52%	0.07%	1.15%
Corp A-AAA	2.83	1.26%	0.62%	0.70%	1.16%	1.17%	2.79%
MBS (0 to 5 Years)	3.26	0.91%	(0.48%)	0.74%	0.93%	(0.74%)	2.55%
Municipals	2.57	0.71%	0.68%	0.43%	0.67%	0.58%	1.72%
Master Indices (Maturities 1 Year and Greater)							
U.S. Treasury	5.70	0.91%	(2.45%)	0.76%	0.03%	(2.54%)	2.12%
Agency	3.93	0.79%	(1.59%)	0.63%	0.35%	(1.38%)	1.63%
Corp A-AAA	6.44	2.38%	(2.49%)	0.69%	0.86%	(1.72%)	3.83%
MBS (0 to 30 Years)	5.17	0.92%	(0.93%)	1.43%	1.08%	(1.20%)	2.66%
Municipals	8.04	2.48%	(3.25%)	2.34%	(0.41%)	(2.75%)	3.28%

Returns for greater than one year are annualized

Source: BofA Merrill Lynch Indices

Portfolio Performance

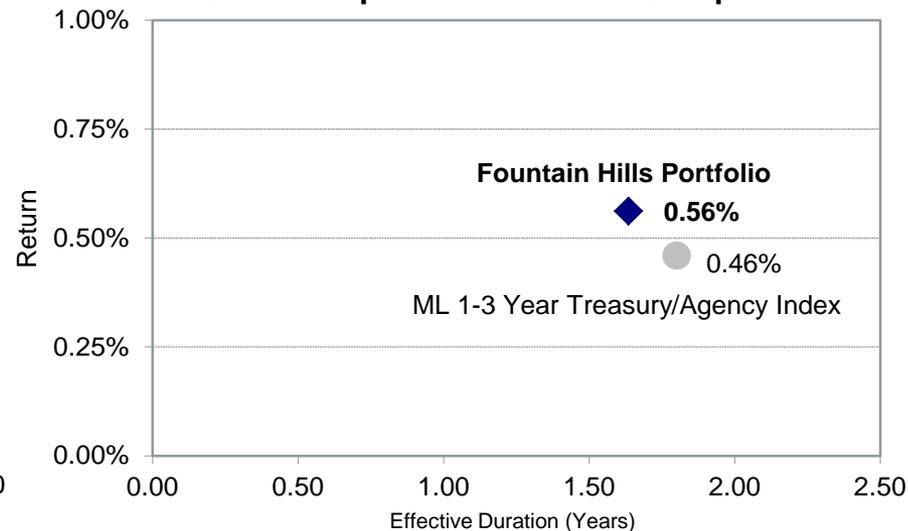
Total Return ^{1,2,3,4}	Quarter Ended September 30, 2013	Past 6 Months	Past 12 Months	Since Inception
Fountain Hills Portfolio	0.27%	0.12%	0.33%	0.56%
ML 1-3 Year Treasury/Agency Index	0.30%	0.18%	0.37%	0.46%

Effective Duration	September 30, 2013	June 30, 2013	Yields	September 30, 2013	June 30, 2013
Fountain Hills Portfolio	1.64	1.81	Yield at Market	0.31%	0.39%
ML 1-3 Year Treasury/Agency Index	1.80	1.80	Yield on Cost	0.47%	0.45%

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. Merrill Lynch Indices provided by Bloomberg Financial Markets.
3. Quarterly returns are presented on an unannualized basis. Performance numbers for periods greater than one year are presented on an annualized basis.
4. Inception date is 12/31/11.

Fourth Quarter 2013 Investment Strategy

- We expect higher volatility in the bond market in the coming quarter. Several factors will contribute to market uncertainty in the fourth quarter and beyond:
 - Pace of economic growth
 - Status and pace of Fed's bond buying taper
 - Effects of sequester cuts
- Treasury yields will likely be range bound due to the unevenness of the economic recovery, but have risen to a new higher trading range.
- The current modestly conservative duration will likely be maintained for the foreseeable future to guard against interest rate volatility and rising rates.
- We generally favor Treasuries with maturities 2 years and under and Agencies in maturities beyond 2-year. As Agency holdings shorten over time, we may swap into like maturity Treasuries, or reposition into longer maturity Agencies at higher yields and wider spreads.



Managed Account Detail of Securities Held

For the Month Ending **September 30, 2013**

TOWN OF FOUNTAIN HILLS, OPERATING FUNDS

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 03/15/2011 1.250% 03/15/2014	912828PZ7	650,000.00	AA+	Aaa	10/03/11	10/03/11	664,294.92	0.35	359.12	652,667.93	653,529.50
US TREASURY NOTES DTD 05/16/2011 1.000% 05/15/2014	912828QM5	750,000.00	AA+	Aaa	03/27/12	03/29/12	759,902.34	0.38	2,832.88	752,902.19	754,248.00
US TREASURY NOTES DTD 12/15/2011 0.250% 12/15/2014	912828RV4	725,000.00	AA+	Aaa	01/05/12	01/06/12	722,167.97	0.38	534.84	723,835.58	725,793.15
US TREASURY NOTES DTD 02/01/2010 2.250% 01/31/2015	912828MH0	250,000.00	AA+	Aaa	01/24/12	01/25/12	263,837.89	0.40	947.69	256,128.81	256,855.47
US TREASURY NOTES DTD 02/15/2012 0.250% 02/15/2015	912828SE1	750,000.00	AA+	Aaa	02/22/12	02/27/12	746,103.52	0.43	239.47	748,191.88	750,556.50
US TREASURY NOTES DTD 03/15/2012 0.375% 03/15/2015	912828SK7	300,000.00	AA+	Aaa	03/13/12	03/15/12	298,992.19	0.49	49.72	299,509.12	300,714.90
US TREASURY NOTES DTD 03/15/2012 0.375% 03/15/2015	912828SK7	1,000,000.00	AA+	Aaa	06/27/12	06/28/12	999,218.75	0.40	165.75	999,580.24	1,002,383.00
US TREASURY NOTES DTD 08/02/2010 1.750% 07/31/2015	912828NP1	450,000.00	AA+	Aaa	08/21/12	08/22/12	467,525.39	0.42	1,326.77	460,941.63	461,900.25
US TREASURY NOTES DTD 08/02/2010 1.750% 07/31/2015	912828NP1	525,000.00	AA+	Aaa	09/06/12	09/10/12	546,410.15	0.33	1,547.89	538,598.61	538,883.63
US TREASURY NOTES DTD 11/30/2010 1.375% 11/30/2015	912828PJ3	625,000.00	AA+	Aaa	11/29/12	12/05/12	644,018.55	0.35	2,888.06	638,800.65	638,378.75
US TREASURY NOTES DTD 11/30/2010 1.375% 11/30/2015	912828PJ3	640,000.00	AA+	Aaa	11/01/12	11/05/12	658,950.00	0.40	2,957.38	653,388.56	653,699.84
US TREASURY NOTES DTD 01/31/2011 2.000% 01/31/2016	912828PS3	115,000.00	AA+	Aaa	01/30/13	02/04/13	120,327.73	0.44	387.50	119,161.66	119,222.69
US TREASURY NOTES DTD 05/02/2011 2.000% 04/30/2016	912828OF0	475,000.00	AA+	Aaa	03/27/13	03/28/13	498,638.67	0.38	3,975.54	494,760.47	493,369.14
US TREASURY NOTES DTD 06/30/2009 3.250% 06/30/2016	912828KZ2	475,000.00	AA+	Aaa	05/22/13	05/24/13	516,024.41	0.44	3,901.32	511,358.69	509,883.05



Managed Account Detail of Securities Held

For the Month Ending **September 30, 2013**

TOWN OF FOUNTAIN HILLS, OPERATING FUNDS

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 06/30/2009 3.250% 06/30/2016	912828KZ2	500,000.00	AA+	Aaa	05/10/13	05/15/13	544,140.63	0.41	4,106.66	538,809.07	536,719.00
US TREASURY NOTES DTD 06/30/2009 3.250% 06/30/2016	912828KZ2	750,000.00	AA+	Aaa	05/24/13	05/31/13	812,402.34	0.53	6,159.99	805,657.00	805,078.50
Security Type Sub-Total		8,980,000.00					9,262,955.45	0.41	32,380.58	9,194,292.09	9,201,215.37
Federal Agency Bond / Note											
FEDERAL HOME LOAN BANK GLOBAL NOTES DTD 04/15/2011 1.375% 05/28/2014	313373JR4	1,000,000.00	AA+	Aaa	10/03/11	10/03/11	1,021,120.00	0.57	4,697.92	1,005,270.46	1,008,205.00
FNMA NOTES DTD 07/18/2011 0.875% 08/28/2014	3135G0BY8	750,000.00	AA+	Aaa	10/03/11	10/03/11	754,860.00	0.65	601.56	751,535.63	754,965.00
FNMA GLOBAL NOTES DTD 10/26/2009 2.625% 11/20/2014	31398AZV7	700,000.00	AA+	Aaa	10/03/11	10/03/11	741,846.00	0.69	6,686.46	715,289.79	719,631.50
FREDDIE MAC GLOBAL NOTES DTD 10/06/2011 0.750% 11/25/2014	3137EACY3	850,000.00	AA+	Aaa	05/31/12	06/01/12	855,202.00	0.50	2,231.25	852,416.81	855,528.40
FEDERAL HOME LOAN BANK GLOBAL NOTES DTD 08/09/2013 0.375% 08/28/2015	313383V81	430,000.00	AA+	Aaa	08/08/13	08/09/13	429,982.80	0.38	147.81	429,983.94	429,938.51
FREDDIE MAC GLOBAL NOTES DTD 07/11/2012 0.500% 08/28/2015	3134G3ZA1	450,000.00	AA+	Aaa	07/30/12	07/31/12	450,525.15	0.46	206.25	450,326.69	450,663.75
FANNIE MAE GLOBAL NOTES DTD 11/16/2012 0.375% 12/21/2015	3135G0SB0	375,000.00	AA+	Aaa	11/14/12	11/16/12	374,126.25	0.45	390.63	374,371.81	374,008.13
FANNIE MAE GLOBAL NOTES DTD 02/15/2013 0.500% 03/30/2016	3135G0VA8	300,000.00	AA+	Aaa	03/12/13	03/13/13	300,141.00	0.48	4.17	300,115.66	299,266.20
FANNIE MAE GLOBAL NOTES DTD 02/15/2013 0.500% 03/30/2016	3135G0VA8	460,000.00	AA+	Aaa	02/14/13	02/15/13	459,475.60	0.54	6.39	459,580.01	458,874.84
FANNIE MAE GLOBAL NOTES DTD 02/15/2013 0.500% 03/30/2016	3135G0VA8	500,000.00	AA+	Aaa	08/29/13	08/30/13	497,335.00	0.71	6.94	497,423.36	498,777.00
Security Type Sub-Total		5,815,000.00					5,884,613.80	0.56	14,979.38	5,836,314.16	5,849,858.33



Managed Account Detail of Securities Held

For the Month Ending **September 30, 2013**

TOWN OF FOUNTAIN HILLS, OPERATING FUNDS

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
Managed Account Sub-Total		14,795,000.00					15,147,569.25	0.47	47,359.96	15,030,606.25	15,051,073.70
Securities Sub-Total		\$14,795,000.00					\$15,147,569.25	0.47%	\$47,359.96	\$15,030,606.25	\$15,051,073.70
Accrued Interest											\$47,359.96
Total Investments											\$15,098,433.66

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Economic Update

Janet Yellen Nominated as Next Fed Chair

- Janet Yellen, current FOMC Vice Chair was nominated by President Obama to succeed Ben Bernanke as Fed Chair.
- Served for three years as Vice Chair, headed up the San Francisco Fed for six years, ran the Council of Economic Advisers for two years, and sat on Fed Board of Governors for three years.
- Must be confirmed by the Senate. Term will begin February 2014.
- Will be first Democrat to lead the Fed since Paul Volcker in 1979.



Economic and Policy Information

- Job creation and unemployment reduction top priority
- Likely to continue quantitative easing policies
- Advocate of strong financial regulation and Fed transparency
- “Dovish-dove with inflationary bias”: Low interest rates key to growth

Details of the Government Shutdown

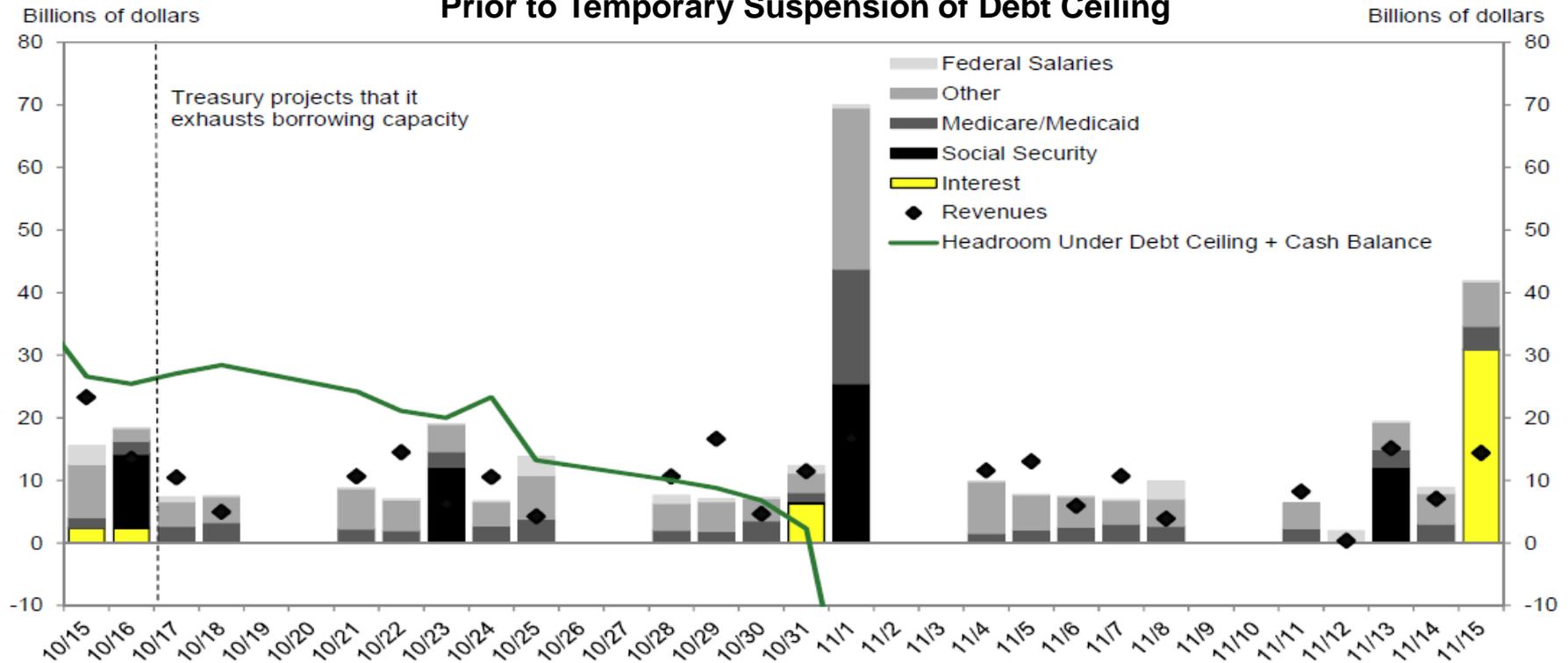
- Annually, the House and Senate are supposed to agree on 12 appropriations bills to fund the federal agencies and set spending priorities. If the bills are not passed, the government shuts down.
- Shutdown ends with the passage of a formal appropriations bill or a “continuing resolution.”



Debt Ceiling Debate

- The debt ceiling is a legislative mechanism to limit the amount of national debt that can be issued by the Treasury.
- Debt issuance is used to pay for spending already issued by Congress. The Treasury was set to hit the debt limit on October 17, and without a change to debt ceiling limit, would no longer be able to pay its bills.

**Treasury Obligations vs Revenue
Prior to Temporary Suspension of Debt Ceiling**



Source: Treasury and Goldman Sachs

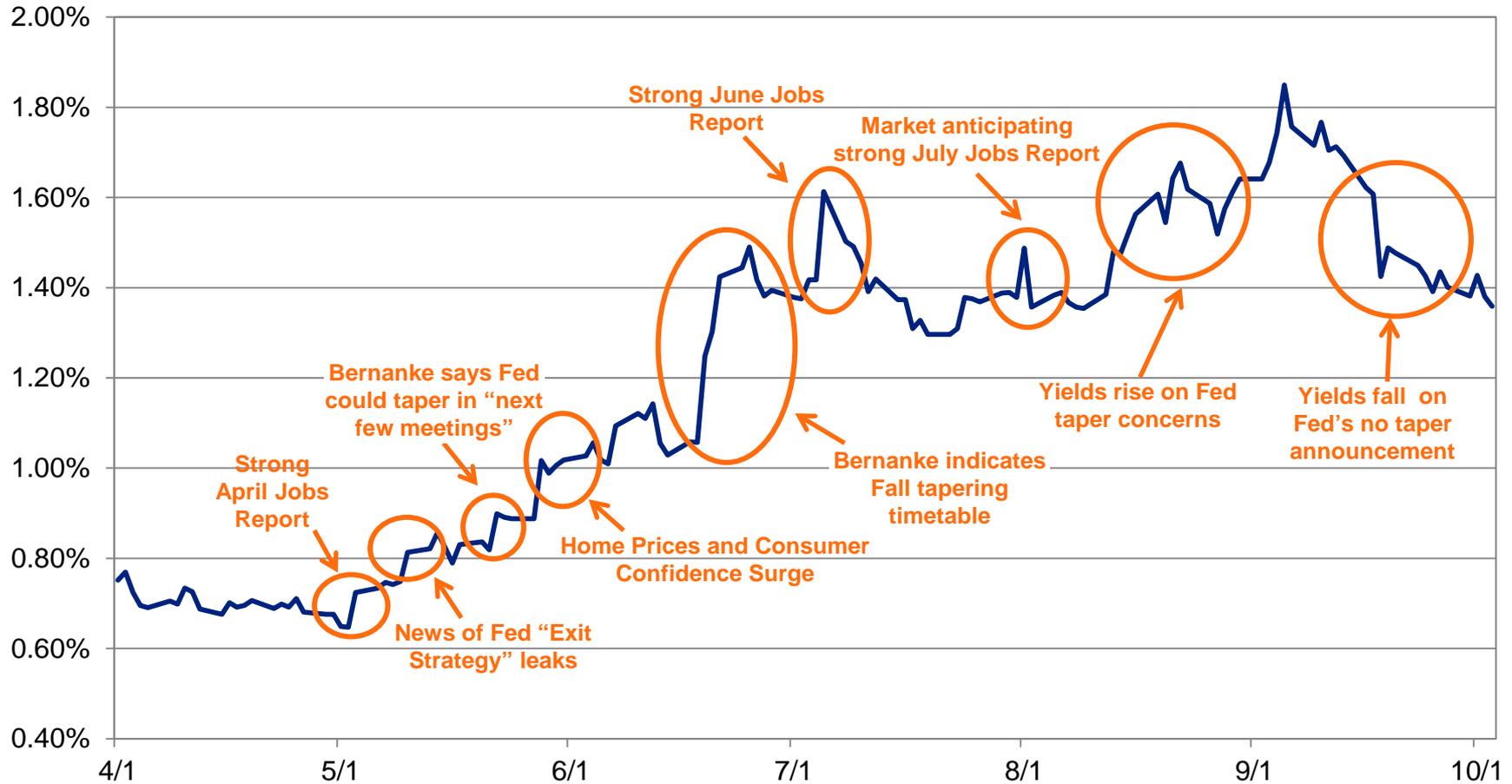
Details of the Government Re-Opening

- October 17: The President signed a bill to re-open the government through January 15 and suspend the debt ceiling through February 7.
- Impacts of the 16 day Shutdown:
 - \$24 billion loss to overall economy (Standard & Poor's).
 - Annualized 4Q13 GDP revised downward from 3% to 2.4% (Standard & Poor's).
 - Delayed economic data releases: Unemployment, construction-spending, retail sales, consumer price index.
 - \$160 million per day that federal government furloughs cost the economy (IHS Inc).
 - 70,000 furloughed federal workers filed for unemployment insurance for the week ended Oct. 5.
 - \$152 million loss per day in travel spending (U.S. Travel Assn).
 - \$76 million lost in daily visitor spending in national parks in 12 states (Coalition of National Park Service Retirees).
 - \$737.95: The amount the average consumer will spend this holiday season or 2% less than last year as the shutdown caused consumer confidence to fall (National Retail Federation).



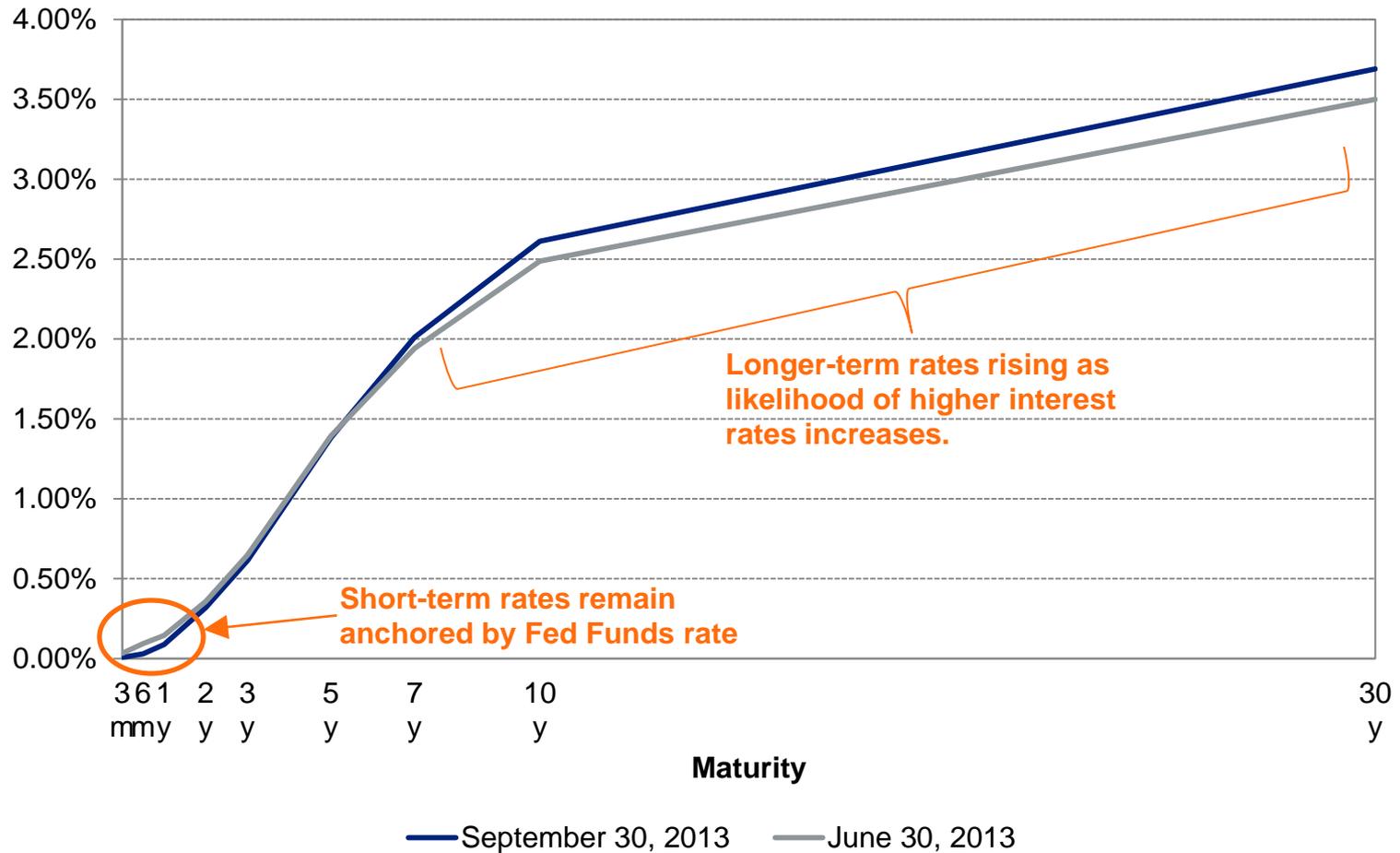
Recent Interest Rate Movers

5-Year U.S. Treasury Yield



Source: Bloomberg

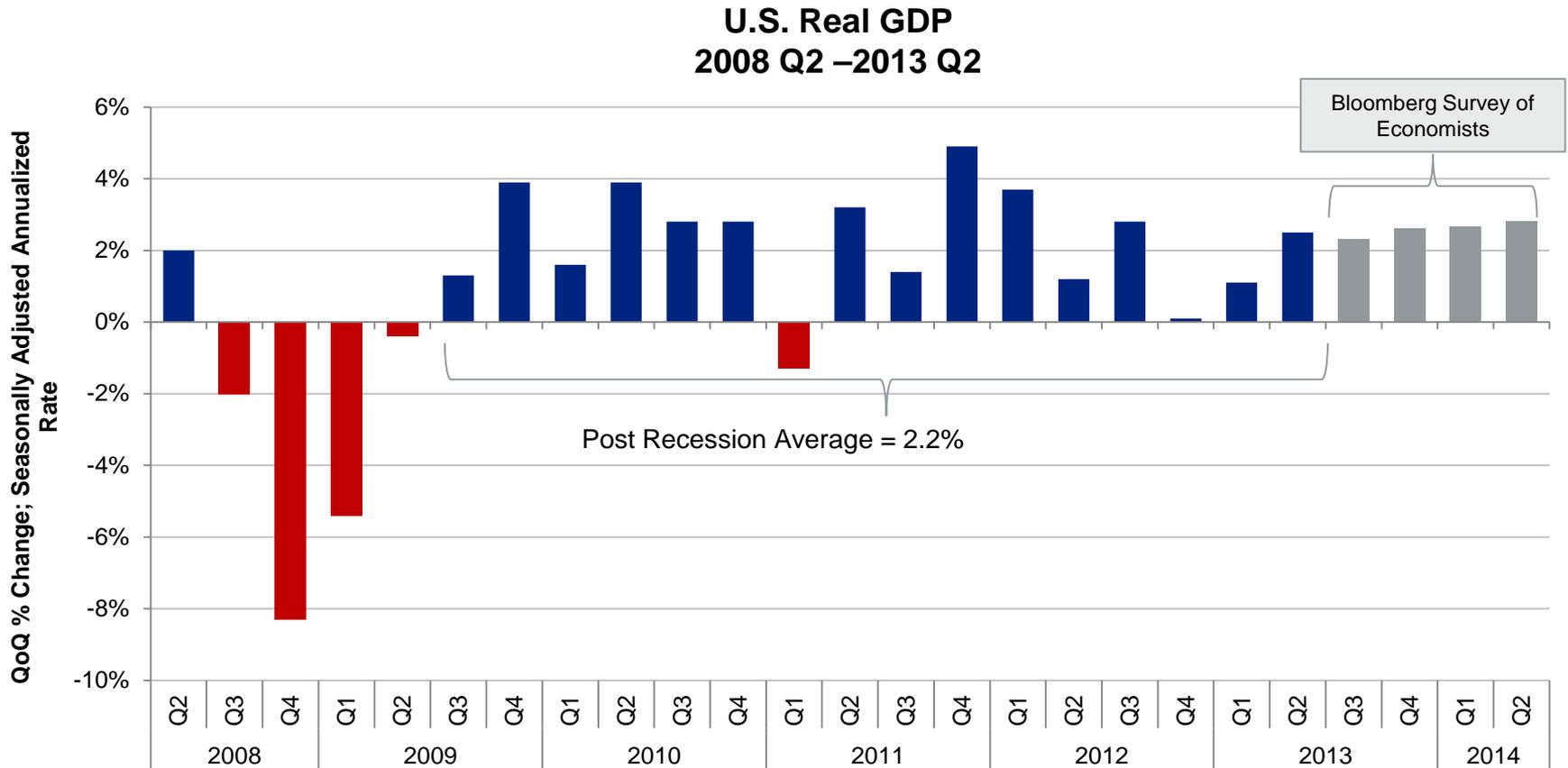
U.S. Treasury Yield Curve Steepens



Source: Bloomberg

Positive Economic Growth Revisions

- The Q2 GDP figure was revised upward to 2.5% from the previously reported 1.7%.
- Growth remains modest, but below potential.

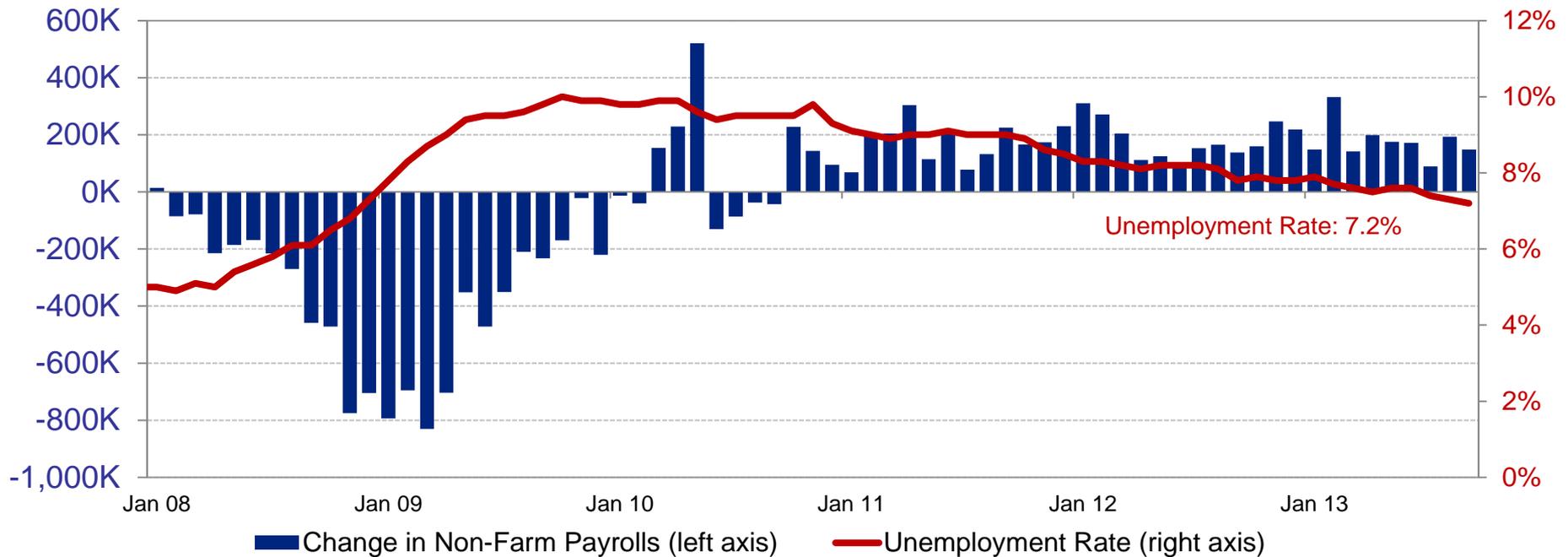


Source: Bureau of Economic Analysis

Job Market Continues Slow Improvement

- After a 2.5 week delay due to the government shutdown, the September jobs report was released on October 22. The report disappointed the markets as the economy added only 148,000 jobs versus expectations of 180,000.
- Part of the decrease in the unemployment rate is attributed to the continued decline of the labor force participation rate, which is currently 63.2%—its lowest level in over 30 years.

Change in Nonfarm Payrolls vs. Unemployment Rate
January 2008 – September 2013



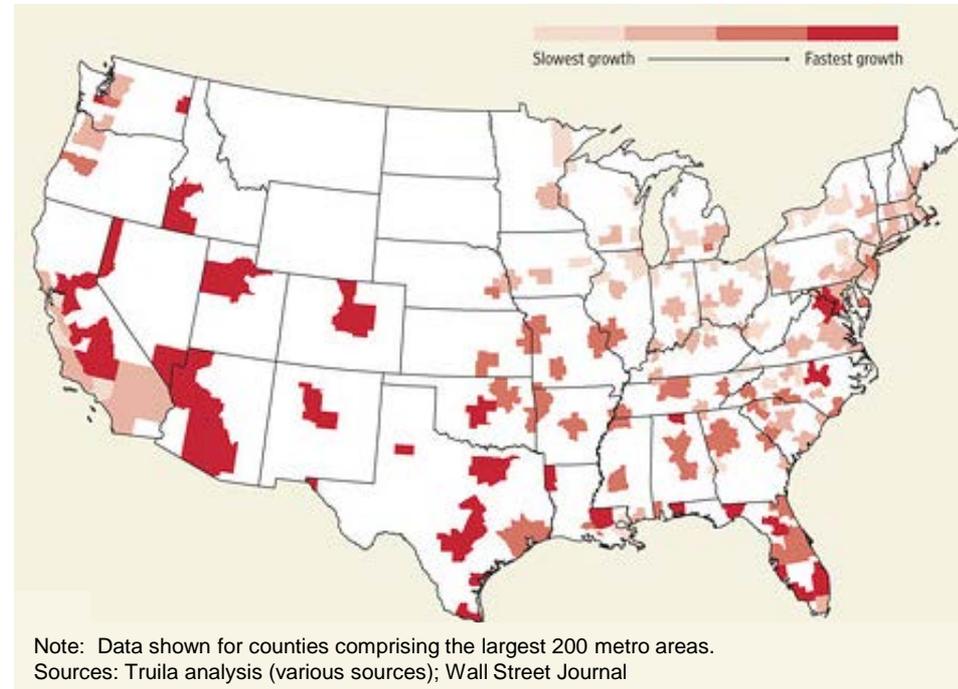
Source: Bureau of Labor Statistics

Where Will Job Growth Come from this Decade?

- Economy is projected to produce 55 million jobs over the current decade (2012-2020).

Fastest Growing Industries	Types of Jobs
Health Care	Registered nurses, physician assistants, radiology techs, and home health aides
Professional and business services	Professionals skilled in areas such as legal services, accounting, and advertising
Leisure and Hospitality	Hotel and restaurant related jobs
Business and financial operations	Credit counselors, compliance officers and financial examiners
Technology and information services	Computer-systems analysts, information-security analysts and software developers
Trade and Artisan Services	Plumbers and electricians, chefs, college coaches and construction supervisors

Projected Job Growth By Metropolitan Area 2010-2020

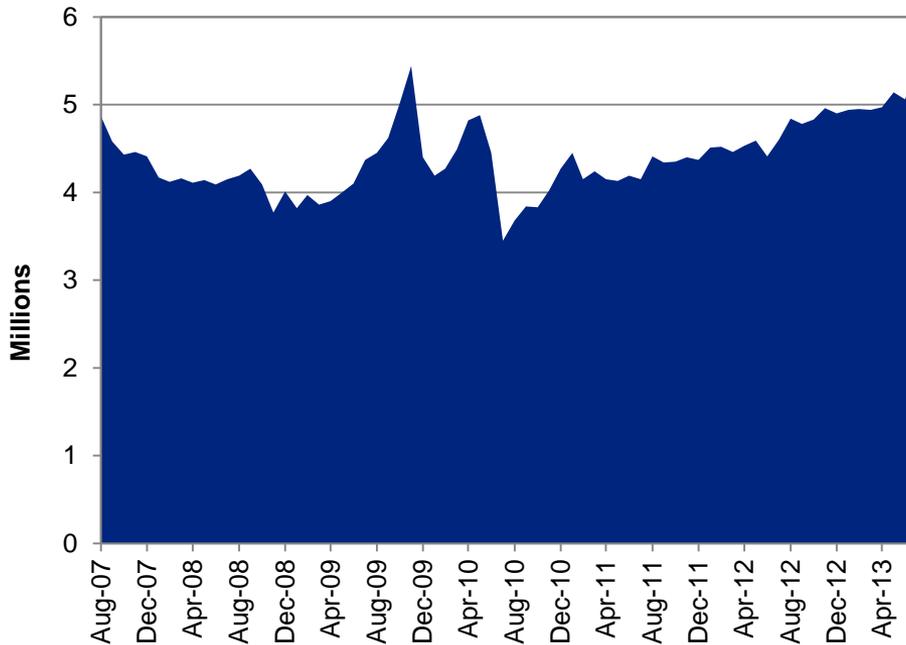


Source: Wall Street Journal

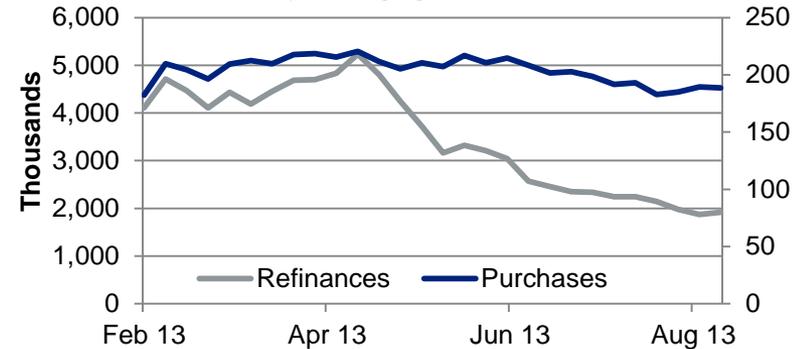
Housing Market Continues Slow Recovery

- The housing market continues to show signs of improvement as home sales have regained their pre-recession momentum.
- The impact of the recent rise in interest rates is most noticeable in the significant decline of refinance related mortgage applications, while new purchase applications have tapered only slightly.

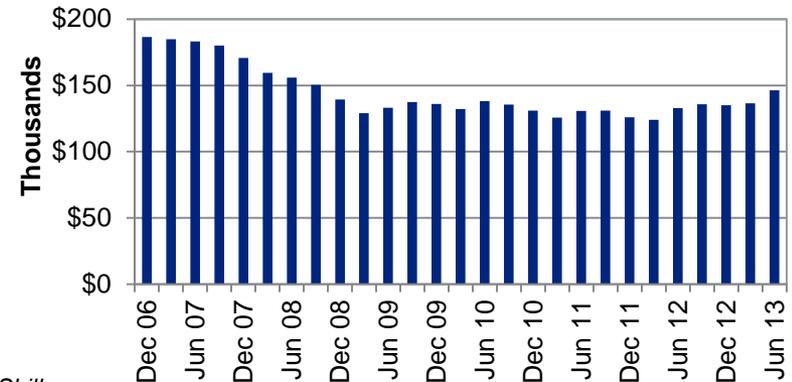
**National Association of Realtors
Existing Home Sales**



Weekly Mortgage Applications



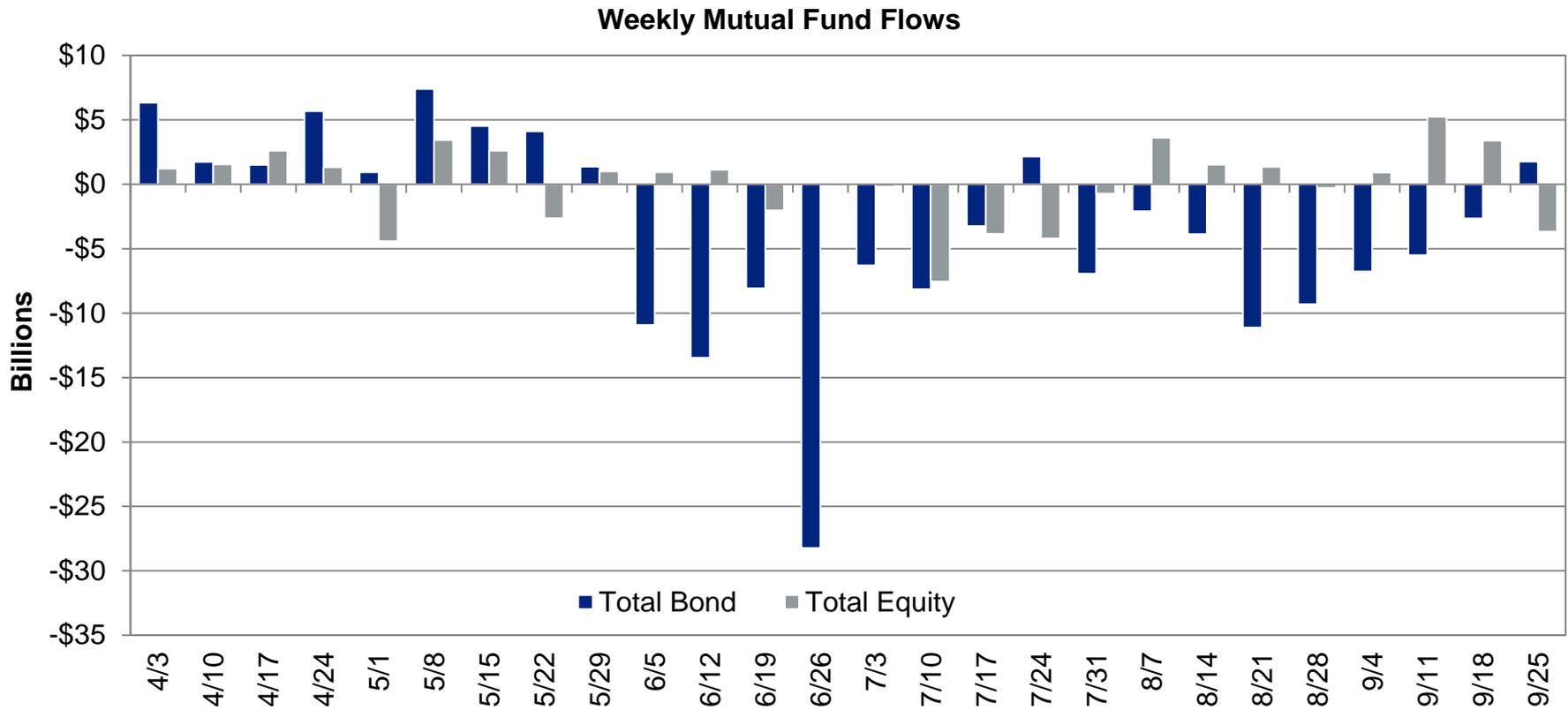
Home Price Index



Source: Bloomberg, Mortgage Bankers Association, National Association of Realtors, S&P/Case Shiller

The Great Rotation, Charlie Brown?

- The size and speed of the market sell-off was exacerbated by investors' large withdrawals from certain segments of the market, including equity and bond mutual funds.



Source: Investment Company Institute, Bloomberg

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