

City of Winter Springs

Investment Performance Review
Quarter Ended September 30, 2010



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September 30, 2010 PFM Month-End Statement

This material is based on information obtained from sources generally believed to be reliable and available to the public, however PFM Asset Management LLC cannot guarantee its accuracy, completeness or suitability. This material is for general information purposes only and is not intended to provide specific advice or recommendation. The information contained in this report is not an offer to purchase or sell any securities.

Fixed-income portfolios generated strong total returns in the third quarter, as interest rates across the yield curve declined to new record lows. All but the shortest duration benchmarks significantly outperformed money market instruments, which continued to offer near-zero yields. Longer duration benchmarks generally performed the best due to larger interest rate declines for longer maturities.

For the quarter our approach to duration was cautious, conservatively positioning portfolio durations short of benchmark durations to guard against the negative effect rising interest rates would have on portfolio market values.

Although the short bias of this strategy sacrificed some return in the quarter, value-added management techniques including strategic yield curve placement and active sector management, worked to produce returns roughly even with benchmarks.

The Federal Reserve has acknowledged a slowing recovery in recent statements, pledging to “provide additional accommodation if needed to support economic recovery and to return inflation, over time, to levels consistent with its mandate.” This “additional accommodation” would almost certainly come in the form of further quantitative easing – a process by which the central bank purchases large amounts of government securities in the open market over a period of months in an effort to push interest rates down and support economic expansion.

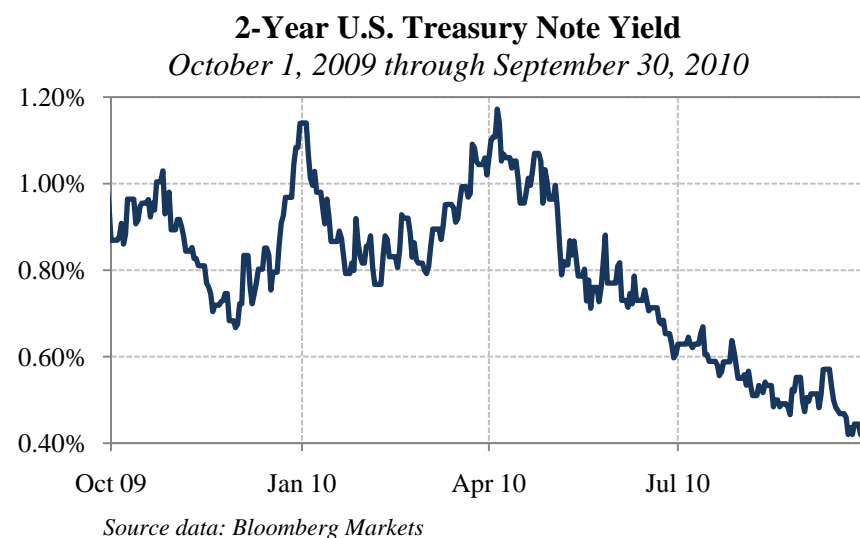
With a slower pace of economic growth and the Fed’s renewed focus on easing, it is likely that rates will remain at recent levels for months, opening a window for us to extend durations closer to those of benchmarks.

Thus our strategy for the fourth quarter is built around somewhat longer durations to take advantage of the steep yield curve. Despite the sharp decline in long term rates during the third quarter, by historic standards, the spread between 2-year and 10-year Treasuries remains wide. With the prospect of low growth and low inflation over the next several quarters, extensions to the range of 90% to 95% of benchmark durations are designed to earn somewhat higher income and benefit

from (somewhat diminished) yield curve roll-down, as the Fed signals readiness to push down rates across the yield curve.

Interest Rates and Returns

Interest rates continued to decline steadily throughout the third quarter, as shown in the chart below, in response to weaker-than-expected economic data. On July 1, a 2-year U.S. Treasury note offered a yield of 0.63%, but by September 30 it was yielding only 0.42% – an all-time low.



While short-term rates declined considerably in the quarter, the decline in rates was most dramatic in longer-term securities, where diminishing inflation expectations and the prospect of Fed intervention had a stronger effect. 5- and 10-year Treasury yields fell 40 to 50 basis points between June and September.

The table on the next page shows quarter-end yields for various U.S. Treasury securities, changes in the quarter, and changes for the past 12 months.

Summary of U.S. Treasury Security Yields

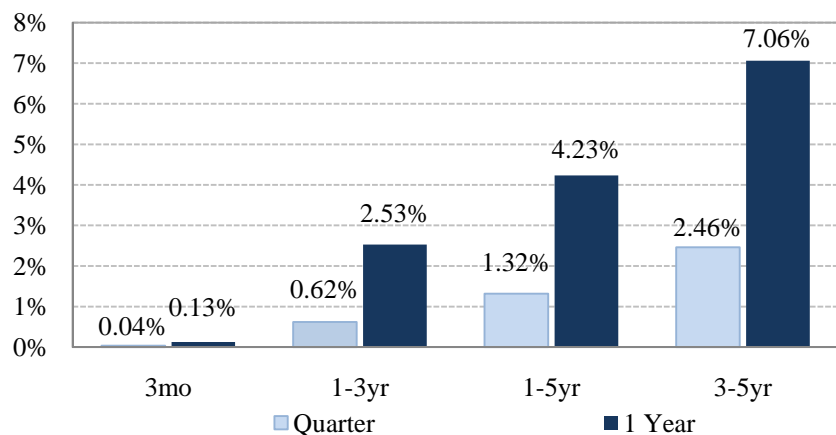
| Date | 3M | 6M | 1Y | 2Y | 3Y | 5Y | 10Y |
|---------------------|--------|--------|--------|--------|--------|--------|--------|
| September 30, 2010 | 0.15% | 0.19% | 0.25% | 0.42% | 0.63% | 1.26% | 2.51% |
| June 30, 2010 | 0.17% | 0.22% | 0.31% | 0.60% | 0.97% | 1.77% | 2.93% |
| Change over Quarter | -0.02% | -0.03% | -0.06% | -0.18% | -0.34% | -0.51% | -0.42% |
| September 30, 2009 | 0.11% | 0.17% | 0.38% | 0.95% | 1.42% | 2.31% | 3.31% |
| Change over Year | 0.04% | 0.02% | -0.13% | -0.53% | -0.79% | -1.05% | -0.80% |

Source data: Bloomberg

With the decline in interest rates, the market values of fixed-income portfolios increased considerably, both quarter-over-quarter and year-over-year. As the chart below illustrates, portfolios with longer durations outperformed those with shorter durations.

The 1- to 3-year U.S. Treasury benchmark returned 0.62% (2.50% annualized), while the 3- to 5-year U.S. Treasury benchmark returned 2.46% (10.21% annualized). The duration of the 3- to 5-year U.S. Treasury benchmark was 3.85 years, versus 1.89 years for the 1- to 3-year U.S. Treasury benchmark.

Total Returns of Merrill Lynch U.S. Treasury Indices
Quarterly and 12-Month Total Return as of September 30, 2010

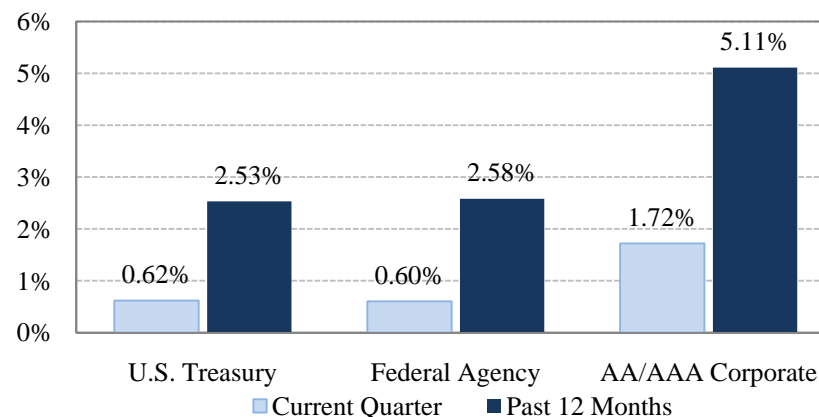


Source data: Bank of America Merrill Lynch; Bloomberg Markets

The yield curve flattened sharply, reducing the benefit of roll-down. Short-term rates remain near zero, intermediate rates have fallen to record lows, and longer rates have fallen 100 to 150 basis points from their April highs. During the quarter, the difference between 2- and 10-year U.S. Treasury yields was as high as 2.45%, but by quarter end, the difference had fallen to 2.09%.

The spread between U.S. Treasury and Federal Agency rates fluctuated within a narrow range during the quarter, though it remained tight by historic standards, reflecting a perception of reduced risk and increased liquidity for agency debt. For example, the spread on 2-year maturities ranged between 16 and 23 basis points, and the spread on 5-year maturities ranged between 20 and 28 basis points, all well below historical averages.

Duration Adjusted Returns of Merrill Lynch 1-3 Year Indices
Quarterly and 12-Month Total Return as of September 30, 2010



Source data: Bank of America Merrill Lynch; Bloomberg Markets
Duration-adjusted return incorporates an adjustment to the market value return (but not the income return) of each benchmark to account for their varied durations, making it easier for investors to assess the relative risk and return of benchmarks of different lengths.

Spreads between Treasuries and corporate securities narrowed in response to improving corporate balance sheets and greater investor appetite for risk, contributing to the strong performance of the corporate sector. As the chart above illustrates, on a duration-adjusted

basis, Treasury and Agency benchmarks performed roughly in line with one another, while corporate benchmarks significantly outperformed.

As corporate spreads continued to narrow in the quarter, we generally increased corporate holdings, selectively purchasing the securities of highly-rated issuers on our approved list. In many portfolios we incorporated commercial paper, which offered some additional value over short-dated Treasury bills, Agency discount notes, and money market instruments.

Economic Outlook

Economic data was generally weak in the third quarter, pointing toward a slowing recovery and uncertain prospects for future growth. The final measurement of second quarter GDP was an anemic 1.7% and economist estimates call for third quarter growth of under 2.0%.

Economic conditions remain subject to considerable uncertainty, with the most likely scenario being modest growth and little-to-no inflation for the foreseeable future. The current pace of expansion is insufficient to make a real dent in unemployment, with nearly 8 million jobs lost since 2008. Unemployment remains persistently high, near 10%, with most businesses still hesitant to add new employees.

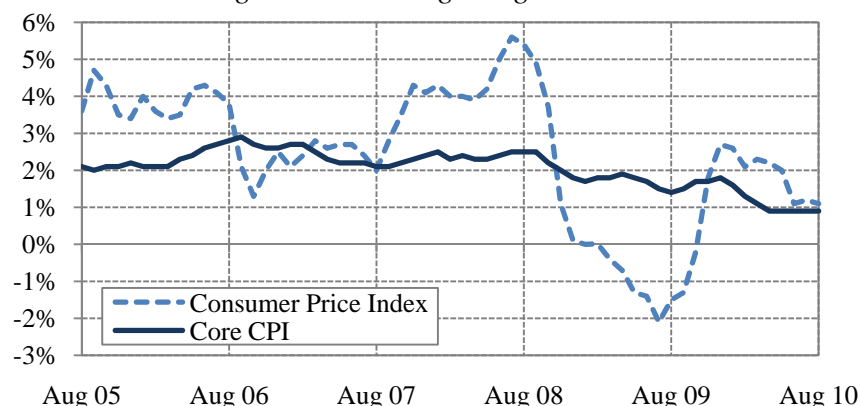
The housing sector remains weak, with housing starts, building permits, and sales relatively unchanged in recent months, and housing prices showing no signs of recovery. The pace of manufacturing activity has accelerated, but is hardly booming, as evidenced by only small upticks in factory orders, stable manufacturing employment, and continued low rates of capacity utilization. Retail sales, though positive year-over-year, are not strong enough to provide significant fuel to recovery.

Global economies, particularly in Asia and emerging markets, are outpacing the U.S. The dollar weakened significantly in the quarter (from \$1.19 to \$1.35 versus the Euro at quarter-end), as fears of a European meltdown diminished and growth picked up in Western Europe. Oil

and commodity prices have risen based on the prospect for stronger global demand. These developments should ultimately aid U.S. export sectors and large, global businesses based in the U.S., but do little to aid small, domestic firms.

The Federal Reserve has become increasingly focused on inflation—or, more properly, the lack thereof. As the following chart shows, though underlying price data show modest inflation, the majority of Fed governors have signaled support for a new round of quantitative easing that would involve the central bank purchasing \$1 trillion of government securities in an effort to push long-term interest rates even lower, ultimately encouraging modest price increases that would help debtors and, perhaps, stimulate spending.

Core and Non-Core Consumer Price Index
August 2005 through August 2010



Source data: U.S. Department of Labor, Bureau of Labor Statistics

Investment Strategy

Given the increased likelihood that low interest rates will persist over the next several quarters, we plan to manage portfolios slightly closer to those of their respective benchmarks. This cautious duration extension should offer an opportunity to add value, while providing enough flexibility to respond to changing interest rate scenarios. We remain concerned that when interest rates rise from their record lows,

as they surely will, longer duration investments will experience market value declines that will lead to strongly negative returns for an extended period. We believe the best defense is to keep portfolios somewhat shorter; even though such a strategy may give up some return in the short run, it will mitigate the effects of a rise in rates. With rates at record lows, even a slight increase has the potential to more than offset interest income, resulting in a negative total return.

We also plan to maintain or increase holdings of assets other than Treasuries because, although credit spreads are generally narrow, strong government and central bank action to promote economic growth and keep interest rates low should aid these types of investments.

Executive Summary

PORTFOLIO STRATEGY

- The City's General City Account Portfolio is of high credit quality and maintains adequate liquidity. The portfolio is invested entirely in Federal Agency, U.S. Treasury, and FDIC guaranteed corporate securities. The securities in the portfolio are allocated among high quality issuers rated AAA.
- By the end of the third quarter, the markets' fears over the European sovereign debt crisis were still not fully alleviated. Market participants, as well as members of the Federal Open Market Committee, have painted a dreary picture of slow economic growth for the foreseeable future. Second quarter growth in the U.S. was 1.7%, down from an initial reading of 2.4%. This figure was disappointing, both in terms of its overall low level and compared to growth of 3.7% and 5.0% in the previous two quarters.
- Minutes from recent Federal Open Market Committee meetings show that the fed may maintain the fed funds target rate at 0% to 0.25% for the foreseeable future. The majority of fed governors have signaled new quantitative easing strategies, with the potential for purchasing \$1 trillion of longer-term government debt. The fed would need to create cash in order to purchase these securities. The securities would most likely be purchased from banks, thus increasing banks' excess reserves. In doing so, the hope is that these increases in bank reserves will allow the banks to increase their lending, and ultimately stimulate economic growth.
- We have already seen the effects of the feds proposed quantitative easing, as Short-Term rates have recently fallen to new lows. If the fed moves forward with and is successful in implementing quantitative easing, Short-Term interest rates may fall even more. The high level of uncertainty regarding future economic growth may cause continued volatility in market rates.
- The General City Account Portfolio continues to provide the City with favorable yield relative to the benchmark. At quarter end the portfolio had a Yield to Maturity at Cost of 1.05%, exceeding the Yield to Maturity of its benchmark the Merrill Lynch 6 Month U.S. Treasury Bill Index by 90 basis points (0.90%).
- PFM will continue to follow the prudent investment strategies that have safely provided the City with favorable yield and maintained adequate liquidity during this period of significant market and economic turmoil.

The City's Investment Statistics

| <u>Account Name</u> | <u>Amortized Cost^{1,2,3}</u> | Amortized Cost ^{1,2,3} | <u>Market Value^{1,2,3}</u> | Market Value ^{1,2,3} | <u>Duration (Years)</u> |
|---|---------------------------------------|---------------------------------|-------------------------------------|-------------------------------|---------------------------|
| | <u>September 30, 2010</u> | <u>June 30, 2010</u> | <u>September 30, 2010</u> | <u>June 30, 2010</u> | <u>September 30, 2010</u> |
| General City Account Portfolio | \$16,253,670.84 | \$19,322,874.54 | \$16,319,617.28 | \$19,403,163.55 | 0.54 |
| Fidelity Institutional Money Market Fund Government Portfolio (Fund #257) | 2,809,471.47 | 5,992,302.08 | 2,809,471.47 | 5,992,302.08 | 0.003 |
| Money Market Fund - State Board of Administration Pool A | 4.06 | 40,724.18 | 4.06 | 40,724.18 | 52 Days |
| Money Market Fund - State Board of Administration Pool B | 782,763.06 | 823,035.67 | 782,763.06 | 823,035.67 | N/A |
| Bank of America Cash for Operation - depository | 3,537,881.75 | 1,518,856.56 | 3,537,881.75 | 1,518,856.56 | 0.003 |
| Water & Sewer 2000 - Fidelity Institutional Money Market Fund Government Portfolio (Account #364) | 716,566.48 | 716,548.41 | 716,566.48 | 716,548.41 | 0.003 |
| Water & Sewer 2000 - Money Market Fund - State Board of Administration Pool A | 0.11 | 1,181.93 | 0.11 | 1,181.93 | 52 Days |
| Water & Sewer 2000 - Money Market Fund - State Board of Administration Pool B | 22,717.86 | 23,886.67 | 22,717.86 | 23,886.67 | N/A |
| Water & Sewer Series 1992 Refunding Revenue Reserve - BONY | 1,305,069.93 | 1,305,069.93 | 1,305,069.93 | 1,305,069.93 | 0.003 |
| Total | \$25,428,145.56 | \$29,744,479.97 | \$25,494,092.00 | \$29,824,768.98 | |

| <u>Account Name</u> | <u>Yield to Maturity on Cost⁴</u> | Yield to Maturity on Cost ⁴ | <u>Yield to Maturity at Market</u> | Yield to Maturity at Market | <u>Duration (Years)</u> |
|---|--|--|------------------------------------|-----------------------------|-------------------------|
| | <u>September 30, 2010</u> | <u>June 30, 2010</u> | <u>September 30, 2010</u> | <u>June 30, 2010</u> | <u>June 30, 2010</u> |
| General City Account Portfolio | 1.05% | 1.00% | 0.30% | 0.39% | 0.68 |
| Fidelity Institutional Money Market Fund Government Portfolio (Fund #257) | 0.01% | 0.01% | 0.01% | 0.01% | 0.003 |
| Money Market Fund - State Board of Administration Pool A | 0.32% | 0.34% | 0.32% | 0.34% | 45.9 Days |
| Money Market Fund - State Board of Administration Pool B | 0.00% | 0.00% | 0.00% | 0.00% | N/A |
| Bank of America Cash for Operation - depository | 0.30% | 0.30% | 0.30% | 0.30% | 0.003 |
| Water & Sewer 2000 - Fidelity Institutional Money Market Fund Government Portfolio (Account #364) | 0.01% | 0.01% | 0.01% | 0.01% | 0.003 |
| Water & Sewer 2000 - Money Market Fund - State Board of Administration Pool A | 0.32% | 0.34% | 0.32% | 0.34% | 45.9 Days |
| Water & Sewer 2000 - Money Market Fund - State Board of Administration Pool B | 0.00% | 0.00% | 0.00% | 0.00% | N/A |
| Water & Sewer Series 1992 Refunding Revenue Reserve - BONY | 0.00% | 0.00% | 0.00% | 0.00% | 0.003 |
| Weighted Average Yield | 0.71% | 0.67% | 0.24% | 0.27% | |

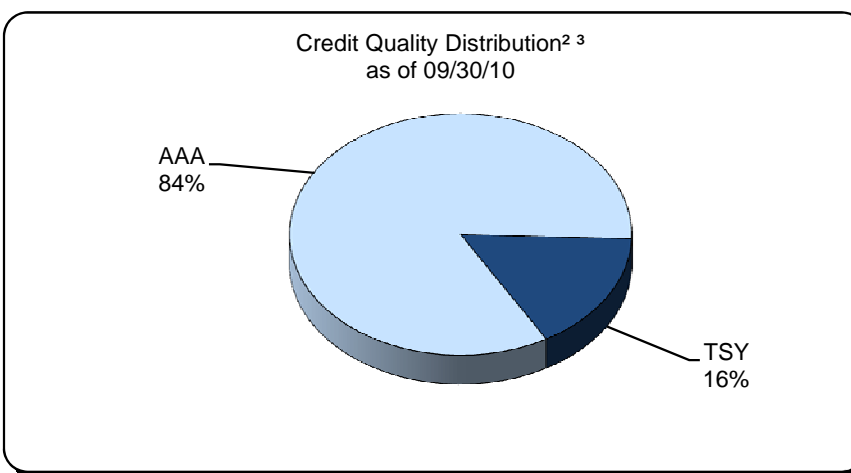
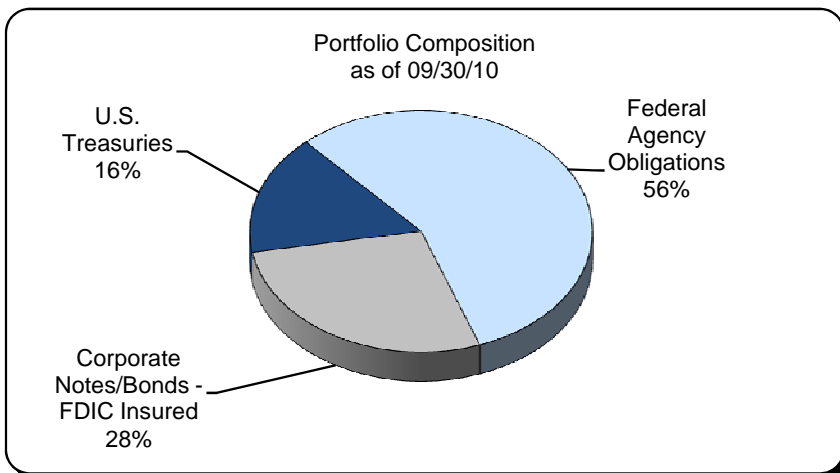
| <u>Benchmarks</u> | <u>September 30, 2010</u> | <u>June 30, 2010</u> |
|---|---------------------------|----------------------|
| Merrill Lynch 6 Month U.S. Treasury Bill Index ⁵ | 0.15% | 0.20% |

Notes:

1. On a trade-date basis, including accrued interest.
2. In order to comply with GASB accrual accounting reporting requirements; forward settling trades are included in the monthly balances.
3. Excludes any money market fund/cash balances held in custodian account.
4. Past performance is not indicative of future results.
5. Source Bloomberg.

General City Account Portfolio Composition and Credit Quality Characteristics

| <u>Security Type¹</u> | <u>September 30, 2010</u> | <u>% of Portfolio</u> | <u>June 30, 2010</u> | <u>% of Portfolio</u> |
|--------------------------------------|---------------------------|-----------------------|------------------------|-----------------------|
| U.S. Treasuries | \$2,618,551.28 | 16.05% | \$2,617,875.82 | 13.49% |
| Federal Agencies | 9,166,601.33 | 56.17% | 10,431,862.76 | 53.76% |
| Commercial Paper | 0.00 | 0.00% | 1,799,920.80 | 9.28% |
| Certificates of Deposit | 0.00 | 0.00% | 0.00 | 0.00% |
| Bankers Acceptances | 0.00 | 0.00% | 0.00 | 0.00% |
| Repurchase Agreements | 0.00 | 0.00% | 0.00 | 0.00% |
| Municipal Obligations | 0.00 | 0.00% | 0.00 | 0.00% |
| Corporate Notes/Bonds | 0.00 | 0.00% | 0.00 | 0.00% |
| Corporate Notes/Bonds - FDIC Insured | 4,534,464.67 | 27.79% | 4,553,504.17 | 23.47% |
| Mortgage Backed | 0.00 | 0.00% | 0.00 | 0.00% |
| Money Market Fund/Cash | 0.00 | 0.00% | 0.00 | 0.00% |
| Totals | \$16,319,617.28 | 100.00% | \$19,403,163.55 | 100.00% |

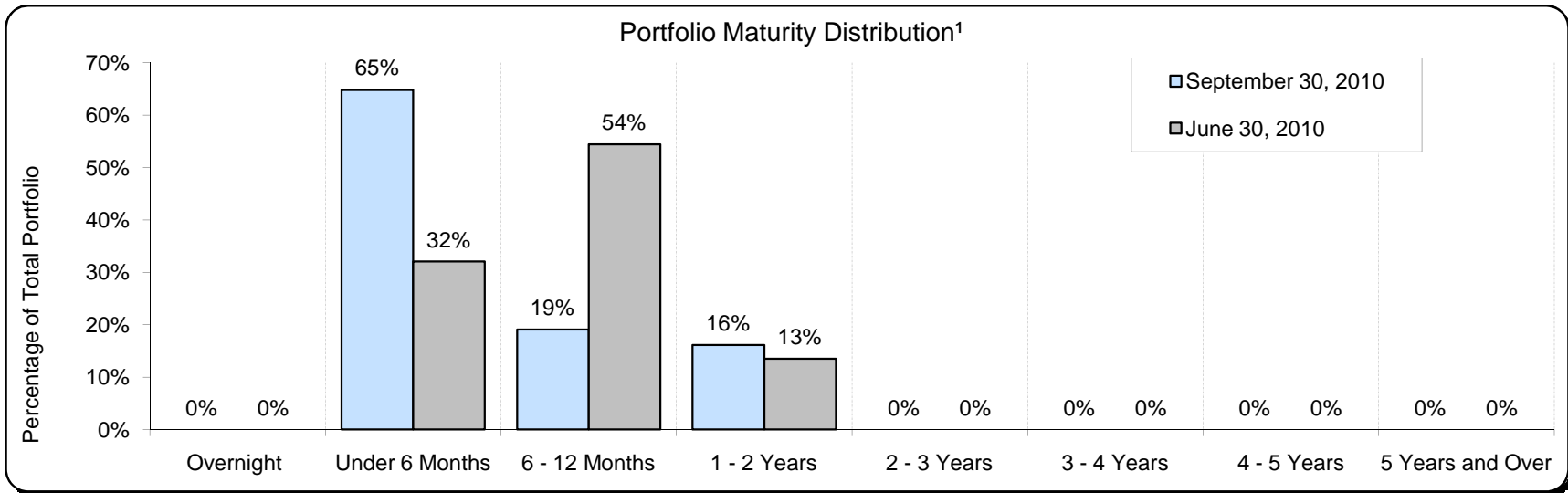


Notes:

1. End of quarter trade-date market values of portfolio holdings, including accrued interest.
2. Credit rating of securities held in portfolio, exclusive of money market fund.
3. A rating of "TSY" indicates the security is an obligation of, or explicitly guaranteed by the U. S. Government.

General City Account Portfolio Maturity Distribution

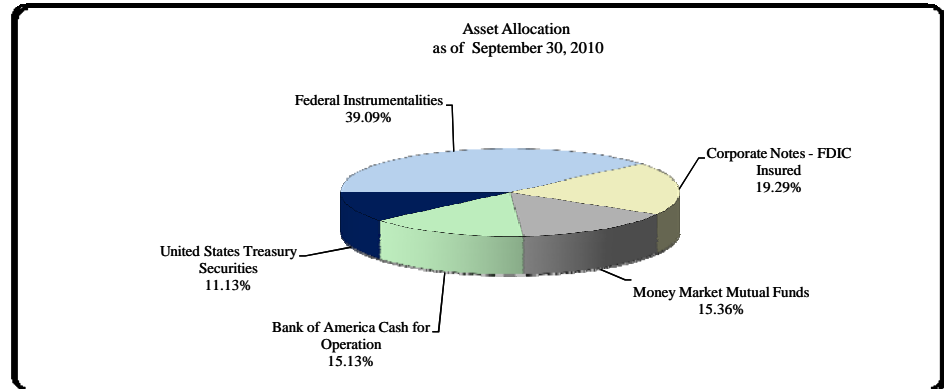
| <u>Maturity Distribution¹</u> | <u>September 30, 2010</u> | <u>June 30, 2010</u> |
|--|---------------------------|------------------------|
| Overnight (Money Market Fund) | \$0.00 | \$0.00 |
| Under 6 Months | 10,575,963.08 | 6,218,961.18 |
| 6 - 12 Months | 3,116,285.94 | 10,566,843.46 |
| 1 - 2 Years | 2,627,368.26 | 2,617,358.91 |
| 2 - 3 Years | 0.00 | 0.00 |
| 3 - 4 Years | 0.00 | 0.00 |
| 4 - 5 Years | 0.00 | 0.00 |
| 5 Years and Over | 0.00 | 0.00 |
| Totals | \$16,319,617.28 | \$19,403,163.55 |



Notes:

1. Callable securities in portfolio are included in the maturity distribution analysis to their stated maturity date, although they may be called prior to maturity.

| Security Type ¹ | September 30, 2010 | September 30, 2010 | Notes | Permitted by Policy |
|---|--------------------|--------------------|-------|---------------------|
| United States Treasury Securities | 2,602,018.71 | 11.13% | | 100% |
| United States Government Agency Securities | - | 0.00% | | 75% |
| Federal Instrumentalities | 9,139,819.75 | 39.09% | | 80% |
| Certificates of Deposit | - | 0.00% | | 25% |
| Repurchase Agreements | - | 0.00% | | 50% |
| Commercial Paper | - | 0.00% | | 30% |
| Corporate Notes - FDIC Insured | 4,511,832.38 | 19.29% | | 50% |
| Mortgage-Backed Securities | - | 0.00% | | 0% |
| Bankers' Acceptances | - | 0.00% | | 30% |
| State and/or Local Government Debt (GO and Revenue) | - | 0.00% | | 20% |
| Money Market Mutual Funds | 3,592,238.59 | 15.36% | 2 | 100% |
| Intergovernmental Investment Pool | - | 0.00% | | 25% |
| Bank of America Cash for Operation | 3,537,881.75 | 15.13% | 2 | 100% |



| Individual Issuer Breakdown | September 30, 2010 | September 30, 2010 | Notes | Permitted by Policy |
|---|--------------------|--------------------|-------|---------------------|
| Government National Mortgage Association (GNMA) | - | 0.00% | | 50% |
| US Export-Import Bank (Ex-Im) | - | 0.00% | | 50% |
| Farmers Home Administration (FMHA) | - | 0.00% | | 50% |
| Federal Financing Bank | - | 0.00% | | 50% |
| Federal Housing Administration (FHA) | - | 0.00% | | 50% |
| General Services Administration | - | 0.00% | | 50% |
| New Communities Act Debentures | - | 0.00% | | 50% |
| US Public Housing Notes & Bonds | - | 0.00% | | 50% |
| US Dept. of Housing and Urban Development | - | 0.00% | | 50% |
| Federal Farm Credit Bank (FFCB) | - | 0.00% | | 25% |
| Federal Home Loan Bank (FHLB) | 2,371,990.17 | 10.14% | | 25% |
| Federal National Mortgage Association (FNMA) | 5,172,210.42 | 22.12% | | 25% |
| Federal Home Loan Mortgage Corporation (FHLMC) | 1,595,619.16 | 6.82% | | 25% |
| Student Loan Marketing Association (SLMA) | - | 0.00% | | 25% |

| Individual Issuer Breakdown | September 30, 2010 | September 30, 2010 | Notes | Permitted by Policy |
|---|--------------------|--------------------|-------|---------------------|
| CD - Bank A | | 0.00% | | 15% |
| CD - Bank B | - | 0.00% | | 15% |
| Fully collateralized Repo - A | - | 0.00% | | 25% |
| Fully collateralized Repo - B | - | 0.00% | | 25% |
| CP A | - | 0.00% | | 10% |
| CP B | - | 0.00% | | 10% |
| General Electric Corporate Notes - FDIC insured | 1,501,523.42 | 6.42% | | 25% |
| JP Morgan Chase Corporate Notes - FDIC insured | 1,502,619.90 | 6.43% | | 25% |
| Bank of America Corporate Notes - FDIC insured | 1,507,689.06 | 6.45% | | 25% |
| Corporate Notes - FDIC insured D | - | 0.00% | | 25% |
| Corporate Notes - FDIC insured E | - | 0.00% | | 25% |
| BA Bank A | - | 0.00% | | 10% |
| BA Bank B | - | 0.00% | | 10% |
| BA Bank C | - | 0.00% | | 10% |
| Municipal Notes/Bonds | - | 0.00% | | 20% |
| Fidelity Institutional Money Market Fund Government Portfolio (Fund #257) | 2,809,471.47 | 12.01% | 2 | 25% |
| Money Market Fund - State Board of Administration | 782,767.12 | 3.35% | 2 | 25% |

Notes:
 1. Does not include bond proceeds.
 2. Managed by the City.
 3. End of month trade-date amortized cost of portfolio holdings, including accrued interest.