First Quarter 2012
Investment Review

THE METROPOLITAN WATER DISTRICT
of SOUTHERN CALIFORNIA

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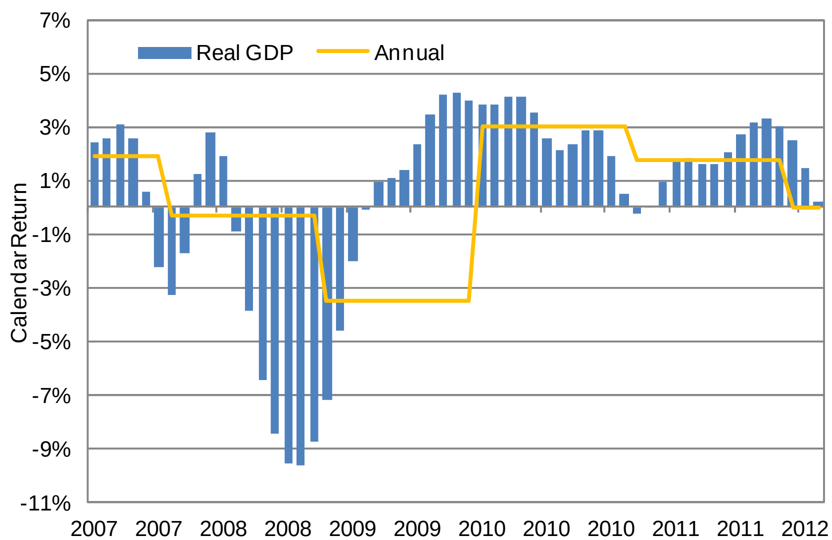
MARKET SNAPSHOT
MARCH 31, 2012

Index	Qtr	One Year	Three Year	Five Year
S&P 500	12.6%	8.5%	23.4%	2.0%
Dow Jones Industrial	8.8%	10.2%	23.6%	4.2%
Wilshire 5000	12.8%	7.0%	24.4%	2.5%
MSCI EAFE Index	10.9%	-5.8%	17.1%	-3.5%
Barclays Aggregate	0.3%	7.7%	6.8%	6.2%
ML G/C 1-5 Yr A+	**0.4%**	**3.2%**	**3.5%**	**4.4%**
ML 3 Month T-Bill	**0.0%**	**0.1%**	**0.1%**	**1.2%**

Low Interest Rates Reflect the Slow Economy



Source: US Bureau of Economic Analysis

- The stock market celebrated the third anniversary of the bull market in March, for a total gain of +109% since 2009 (37 months), compared to an average gain of +103% over 30 months for other big rallies.
- The broad US stock market gained +12.8% (W5000) and +19.0% for the NASDAQ, which was fueled by strong gains from Apple (+48%) and its suppliers. The Dow was held back by a lower weight in financials and performance of stocks like Caterpillar and Chevron.
- Growth stocks outperformed as investors moved back into economically cyclical stocks like technology (+21%) and consumer discretionary (+16%); financials (+22%) was the best performing sector. It's worthwhile to note that strong gains in the first quarter have tended to bode well for the full year.
- The international developed markets (EAFE) underperformed the US, but the emerging markets rebounded with a +14.1% gain. The slowdown in China worried investors, but not enough to offset the stronger emerging market economies.
- Commercial real estate was a story of two markets; core properties continued to advance, with income above 6%, while second tier properties lagged.
- Hedge funds struggled to keep up with the stock market; the best strategies were equity long/short (+6.3%), event driven (+5.6%), and distressed credit (+5.6%). Overall commodity indexes were flat, even with an 18% rise in gasoline prices.
- The US bond market began to show some cracks in March, reminding investors of the losses possible from higher interest rates; however, by the end of the quarter the Fed calmed fears and rates headed back down. EU bonds were generally weak, but EM bonds and currencies rebounded.

Slow Growth for the US Economy

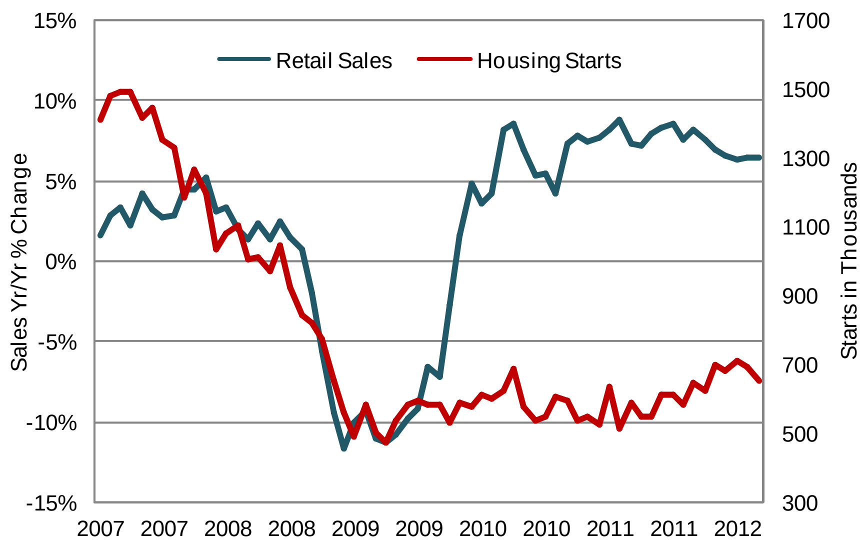
- The 2.2% GDP growth in the first quarter was a disappointment, especially since it included another increase in inventories; the results added more fuel to the expectation for slower growth ahead. However, some of the slowdown may be due to seasonal adjustments, as economists try to account for the warmest winter in at least 10 years.

- Higher gas prices did not have a significant impact on consumer spending, but the savings rate declined to 3.8%. Even though the consumer is stretched, the ISM manufacturing index rose to 53.4%, indicating an expansion in manufacturing for the 32nd consecutive month.

- The Fed appears committed to providing additional support "if needed," but investors continue to question how much of the rebound in the economy and the markets is due to monetary stimulus.

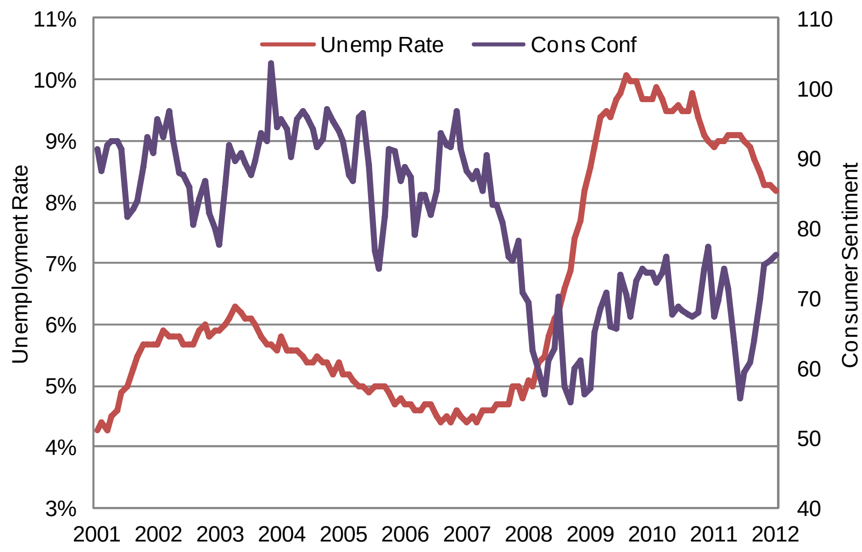
- The unemployment rate declined to 8.2% in March, but private job growth was disappointing at 120,000; initial jobless claims are also ticking up. Nevertheless, the case for a slow recovery remains intact.

Consumer Spending Came From Savings



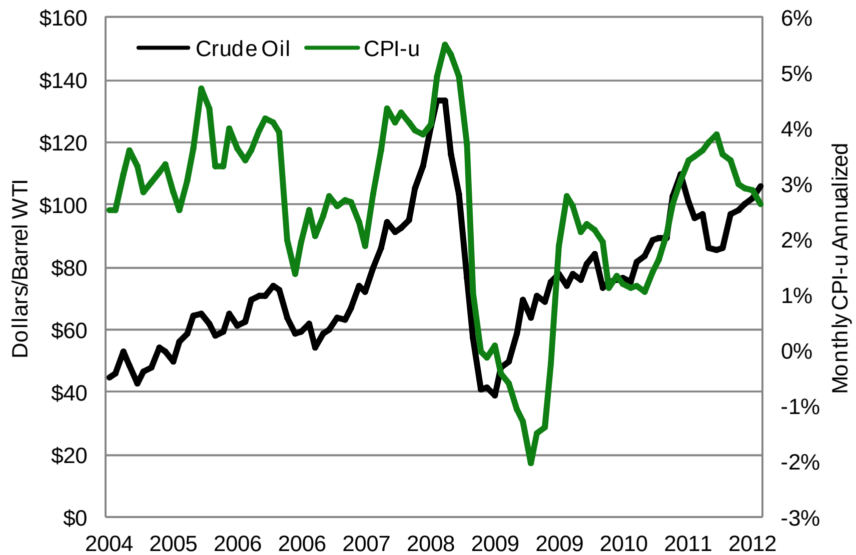
Source: US Census Bureau

Employment is Gradually Improving



Source: Bureau of Labor Statistics, University of Michigan

Oil Prices Have Not Affected Consumer Spending



Source: Bureau of Labor Statistics

Strong Quarter for US Equities

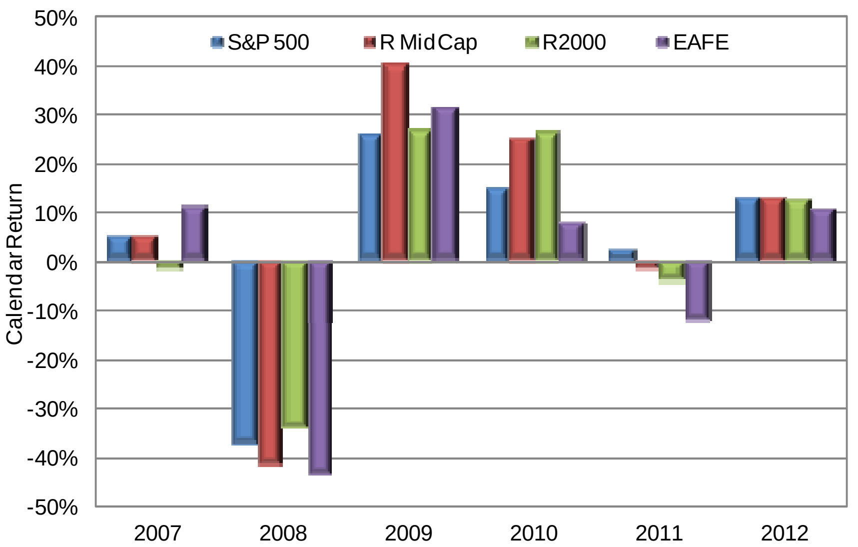
- The S&P 500 Index posted the largest quarterly gain (+12.6%) in 14 years, and earnings are on track for a year-over-year gain of as much as 8%. Although we expect growth rates to slow, corporations are performing better than expected, making the current PE ratio of 14 look reasonable.

- Financials (+22%), technology (+21%), and consumer discretionary (+16%) led the US market, which continues to cycle between economically sensitive and defensive sectors. Growth stocks exceeded value, even with the big gains in financials, and small cap stocks were constrained by relative valuations that appear 10% to 15% above norm.

- Defensive stocks underperformed, with utilities posting a negative return of -1.5%. Dividend strategies, which performed well last year, are trailing by more than 700 bps in 2012; MLPs were up only +2.0%.

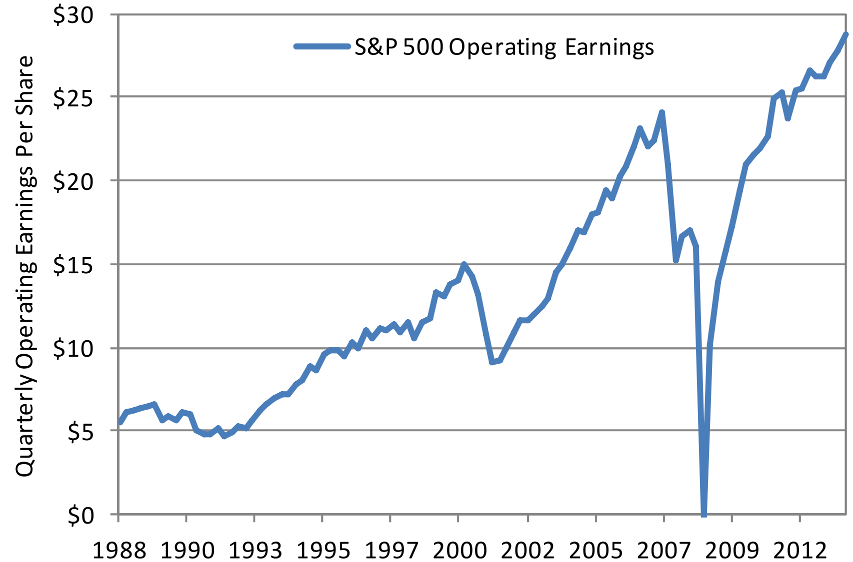
- Active managers struggled again to beat the indexes; just 3 of 9 Morningstar groups had 50%+ of managers outperforming. Large cap growth managers had the toughest time, with just 23% exceeding the index.

US Outperforms Other Developed Markets



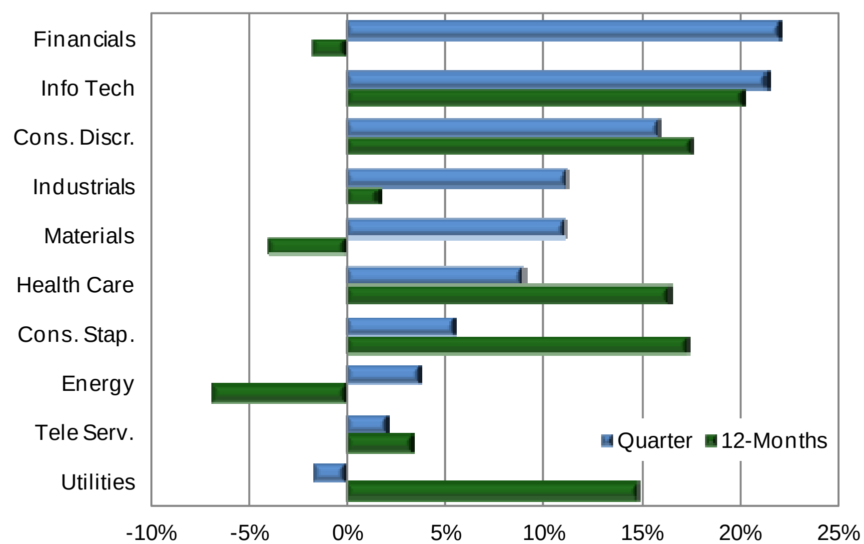
Source: Standard & Poor's, Russell, and MSCI Barra

Earnings Growth is Slowing



Source: Standard & Poor's

Cyclical Sectors Lead the Market



Source: Standard & Poor's

Treasuries Give Back Some Gains

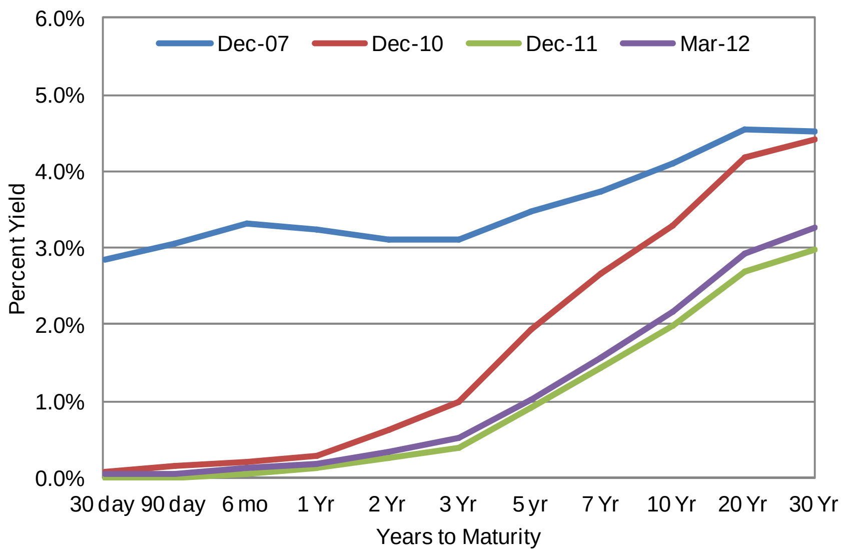
- The Barclays US Aggregate Bond Index was nearly flat in the first quarter (+0.3%), as an uptick in yields pushed down bond prices. Interest rates rose across the yield curve producing a -1.1% return on the Barclays US Government Index; the 10-year rose 31 bps to 2.2% and the 30-year rose 40 bps to 3.3%.

- Outside of the core investment grade bond market, the picture was significantly better, with a +5.3% return on high yield bonds and a +4.9% return on emerging market bonds. The European LTRO reduced fears and led to a rebound in emerging market currencies.

- Yields (and spreads) on US IG corporate bonds hit new lows, contributing to a +2% return on Barclays US Credit Index, even though issuance reached a record of $444 billion in the first quarter. Mortgages were impacted by higher treasury rates and returned only +0.6%.

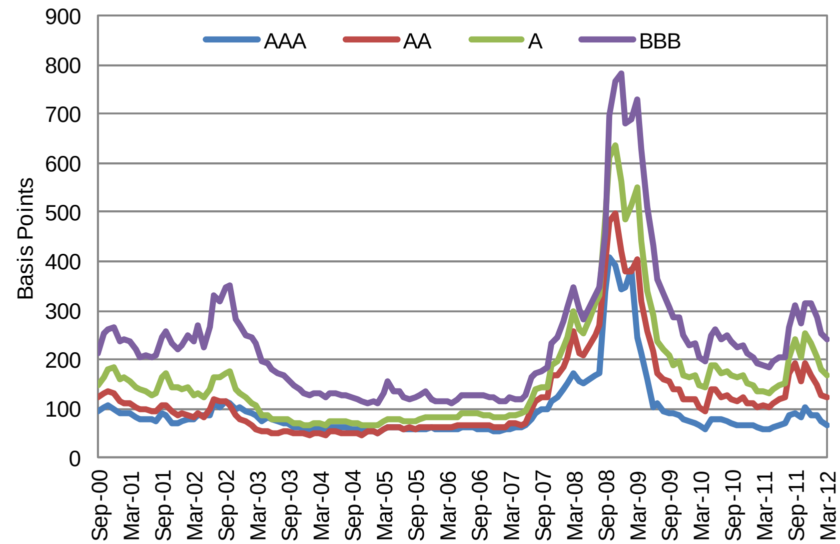
- Although emerging markets performed well, the JPM Global Bond Index lost -0.7%, as foreign government bonds fell, along with downgrades in nine EU countries, including the loss of France's AAA rating.

Low, But Rising, Treasury Yields



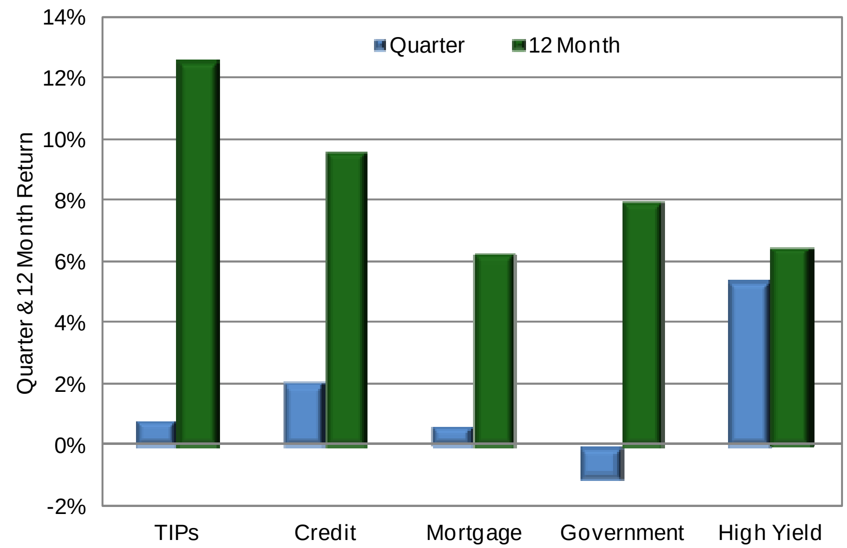
Source: Federal Reserve

Spreads Tighten with Demand for Yield



Source: Merrill Lynch

Another Good Quarter for High Yield Bonds



Source: Barclays Capital

PORTFOLIO SUMMARY

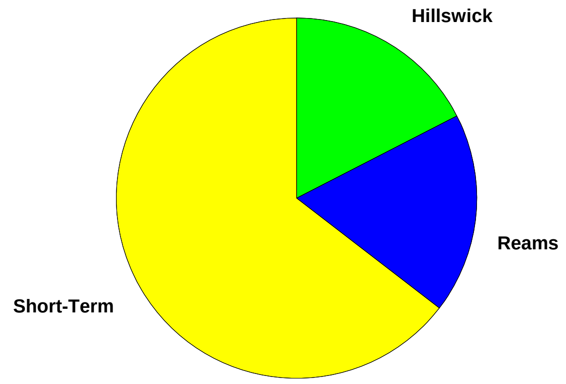
MARCH 31, 2012

	Assets	Weight
Managed Accounts		
Hillswick Asset Mgmt	$158,480,700	17%
Reams Asset Mgmt	$163,502,000	18%
Total External Managed	$321,982,700	35%
Short-Term Account	$586,360,800	65%
Grand Total	**$908,343,500**	100%

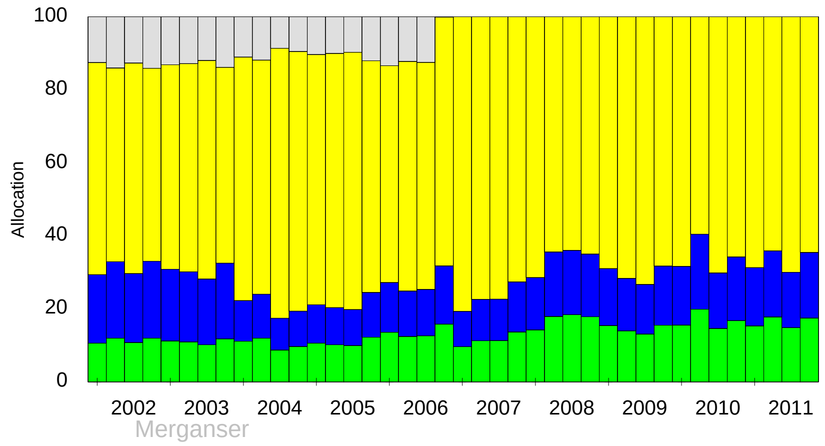
- The value of the Total Fund decreased by $159.9 million in the first quarter, due to net cash outflow of $161.9 million offset by earnings of $1.9 million.
- Net investment earnings for the quarter were:

Hillswick	-$0.2 million
Reams	$1.8 million
Short-Term	$0.3 million
Total	$1.9 million

CURRENT ALLOCATION



HISTORICAL ALLOCATION



PERFORMANCE SUMMARY - TOTAL RETURN

MARCH 31, 2012

Manager	Quarter	Fiscal YTD	1 Year	3 Years	5 Years
Total Fund	0.2%	1.5%	2.3%	2.4%	3.2%
Benchmark[1]	0.1%	0.6%	1.1%	1.2%	2.2%
Hillswick Asset Mgmt	-0.1%	3.6%	5.0%	3.5%	5.0%
ML G/C 1-5 yr. A & above	0.4%	1.8%	3.2%	3.5%	4.4%
Reams Asset Mgmt	1.1%	2.5%	3.7%	5.8%	5.4%
ML G/C 1-5 yr. A & above	0.4%	1.8%	3.2%	3.5%	4.4%
Total External Managers	0.5%	3.1%	4.3%	4.7%	5.2%
ML G/C 1-5 yr. A & above	0.4%	1.8%	3.2%	3.5%	4.4%
Short-Term Account	0.0%	0.6%	1.1%	1.2%	2.2%
ML 90-day T-Bill	0.0%	0.0%	0.1%	0.1%	1.2%

[1] The benchmark for the Total Fund is based on the average asset allocation between the Externally Managed and Short-term Accounts, incorporating the Merrill Lynch Government/Corporate 1-5 yr A+ and the Merrill Lynch 3 Month T-Bill.

- Income from the investment portfolio has remained low over the last year along with the general level of interest rates. However, relative investment performance of the Total Fund continues to rank in the top quartile (see universe comparisons on page 8).
- The return on the Total Fund exceeded the bench-mark index due to strong performance by Reams and the Staff-Managed Short-Term Account. Note that the 3-year return on 90-day TBills has now dropped to nearly zero.
- Volatility returned to the bond market in March, with several weeks of price declines (interest rate increases) in government bonds, which lost -1.1%; at the end of March and into April, the trend reversed, after comforting words by the Fed.
- Hillswick produced income of $0.7 million offset by price declines of -$0.9 million for an overall return of -0.1%. They continue to believe that Europe is not fixed and the US will not rebound, so they hold 89% in government bonds. This underweight to credit and longer duration resulted in the low return.
- Reams continues to maintain a different approach with overweights to corporate bonds (38%) and mortgages (18%). The portfolio outperformed the benchmark due to these overweights and good bond selection in the corporate bond sector.
- The challenges in cash management are reflected by the SEC hearings exploring fixes for money market funds that have virtually no yield. In contrast, the Staff-Managed Short-Term Account has performed very well with a more flexible approach to security selection among high quality issuers and a longer duration.

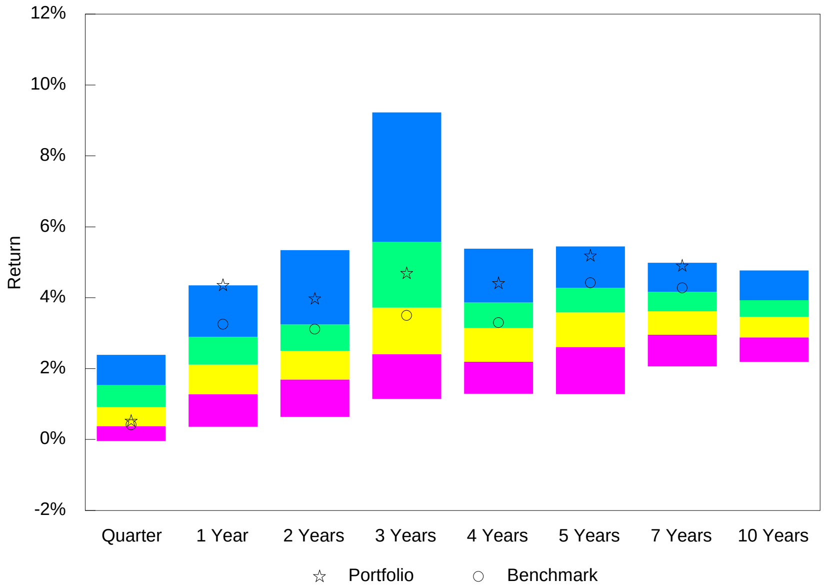
CONSOLIDATED BALANCE SHEET and CASH FLOW SUMMARY FOR THE FISCAL YEAR

JULY 1, 2011 TO MARCH 31, 2012

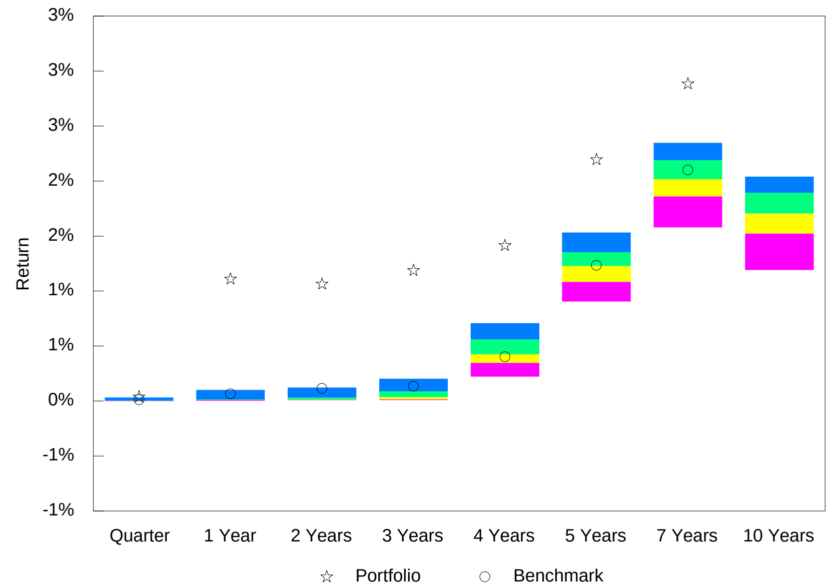
Manager	Beginning Balance	Net Cash Flows	Income	Gain/(Loss)	Ending Balance
Total Fund	**$998,822,600**	**($103,197,700)**	**$12,482,500**	**$236,100**	**$908,343,500**
Externally Managed					
Hillswick Asset Mgmt	$152,934,600	$0	$2,039,400	$3,506,700	$158,480,700
Reams Asset Mgmt	$159,512,400	$0	$2,625,100	$1,364,500	$163,502,000
Total Externally Managed	$312,447,000	$0	$4,664,500	$4,871,200	$321,982,700
Short-Term Account	$686,375,600	($103,197,700)	$7,818,000	($4,635,100)	$586,360,800

Note: The totals may differ slightly from the actual sums due to rounding.

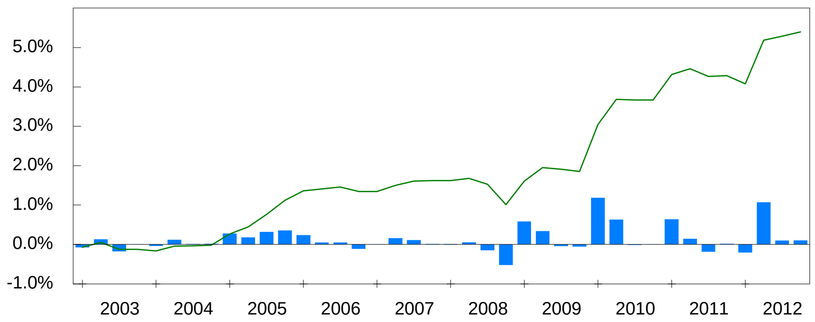
TOTAL EXTERNAL MGRS VS. PEER GROUP



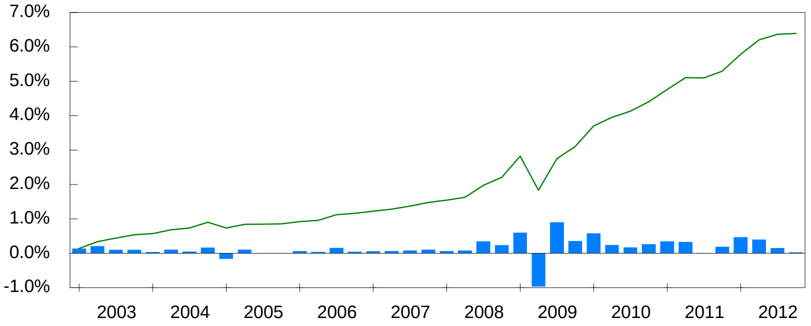
SHORT-TERM VS. PEER GROUP



TOTAL EXTERNAL MGRS VALUE ADDED



SHORT-TERM VALUE ADDED



MANAGER SCORECARD

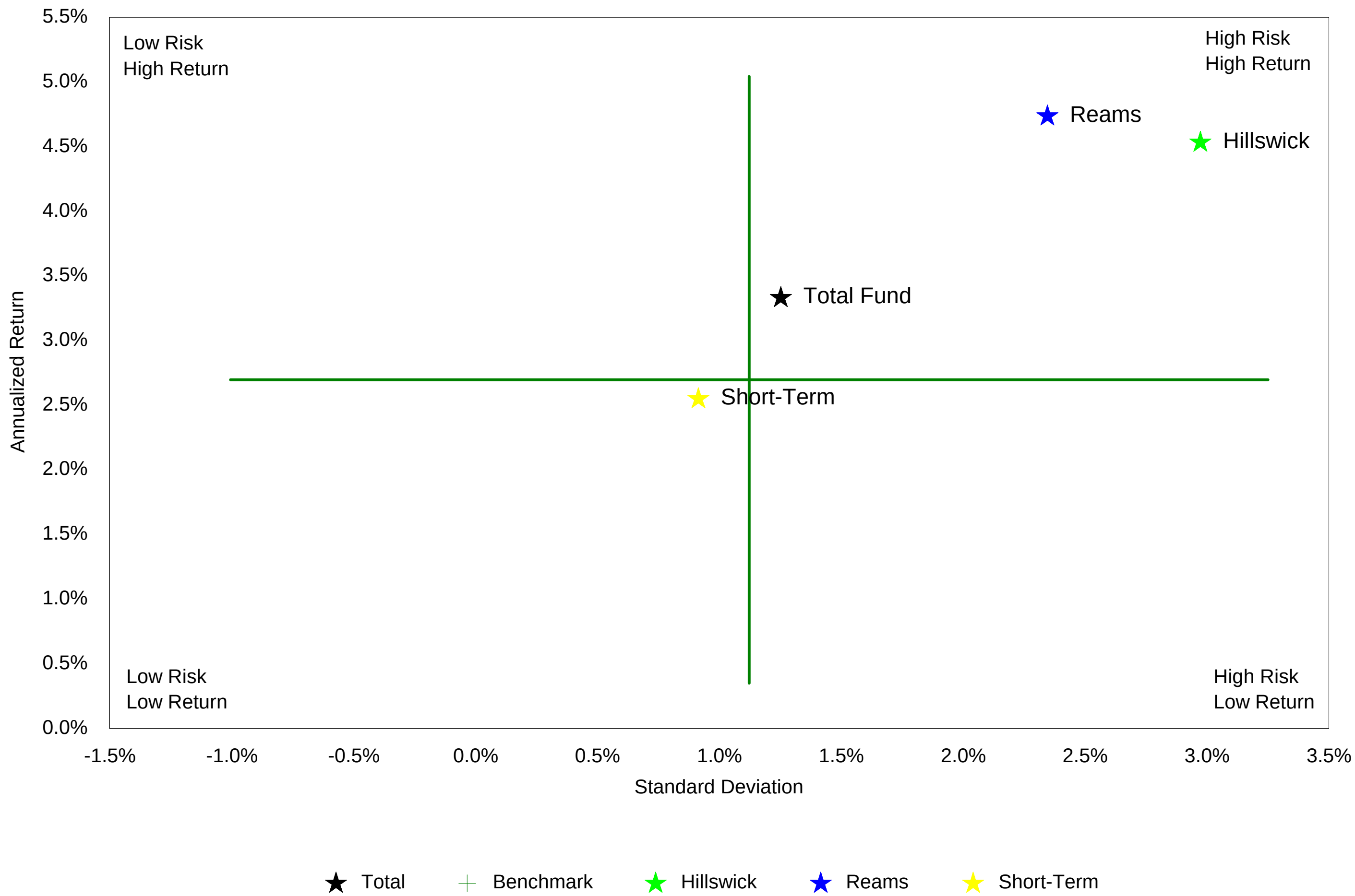
FROM INCEPTION

Manager	Return	Index Return	Std Dev	Alpha	Beta	Batting Average	Incept
Total Fund	3.33	2.70	1.25	0.43	1.20	825	2Q02
Hillswick Asset Mgmt.	4.53	4.04	2.97	0.17	1.14	475	2Q02
Reams Asset Mgmt.	4.74	4.04	2.35	1.04	0.84	650	2Q02
Short-Term Account	2.55	1.91	0.91	0.73	0.39	925	2Q02

INVESTMENTS PORTFOLIOS VS. POLICY BENCHMARKS

Manager	1 Year Benchmark	1 Year Univ Med	3 Year Benchmark	3 Year Univ Med	Alpha	Beta <1.10
Total Fund	Exceed	Exceed	Exceed	Under	Positive	High
Hillswick Asset Mgmt	Exceed	Exceed	OK	Under	Positive	High
Reams Asset Mgmt	Exceed	Exceed	Exceed	Exceed	Positive	Low
Short-Term Account	Exceed	Exceed	Exceed	Exceed	Positive	Low

RISK / RETURN ANALYSIS
(FROM INCEPTION)



Alpha

Alpha is a measure of the value added (or the excess return of a portfolio versus the benchmark - adjusted for risk) for an actively managed portfolio. It is generally interpreted as a measure of a manager's skill as the result of security selection and asset allocation - the higher the number the better.

Batting Average

Batting Average is a measure of how often the manager has beaten the benchmark. A batting average of 600 indicates that the manager has beaten the portfolio benchmark (or comparable market index) six out of every ten quarters, or 60% of the time.

Beta

Beta is a measure of a manager's risk vs the benchmark. A beta of 1.0 indicates that a portfolio has roughly the same volatility as the benchmark. A beta greater than 1.0 indicates that the portfolio is more volatile or sensitive to changes in the market.

Duration

Duration is a measure of the sensitivity in the price of a bond to changes in interest rates, so it is a measure of risk in a fixed income portfolio. As a rule of thumb, a fixed income portfolio with a duration of 5 (years) will decline 5% in value for every 1% upward movement in comparable interest rates.

Standard Deviation

Standard deviation is a measure of the dispersion of a portfolio's return around its expected return. A higher standard deviation indicates greater dispersion and, therefore, lower predictability of future returns.