Fourth Quarter 2014
Investment Review

THE METROPOLITAN WATER DISTRICT
of SOUTHERN CALIFORNIA

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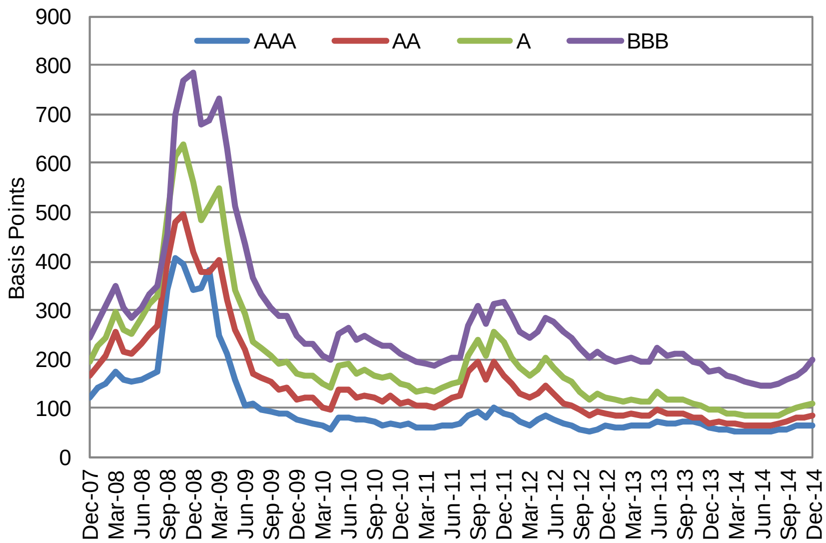
MARKET SNAPSHOT
DECEMBER 31, 2014

Index	Qtr	One Year	Three Year	Five Year
S&P 500	4.9%	13.7%	20.4%	15.5%
Dow Jones Industrial	5.2%	10.0%	16.3%	14.2%
Wilshire 5000	4.9%	12.1%	20.4%	15.6%
MSCI EAFE Index	-3.6%	-4.9%	11.1%	5.3%
Barclays Aggregate	1.8%	6.0%	2.7%	4.4%
BofA ML G/C 1-5 Yr A+	**0.5%**	**1.4%**	**1.2%**	**2.1%**
BofA ML 3 Month T-Bill	**0.0%**	**0.0%**	**0.1%**	**0.1%**

Spreads Widen Across Sectors
(Yield over treasuries)



Source: Merrill Lynch

- Large cap US stocks had another year of double digit gains, with the S&P 500 advancing +13.7% for the year. There were no clear style winners last year, as growth and value produced similar results.
- Small cap stocks rallied +9.7% in the fourth quarter, erasing the big losses from 3Q. However, small stocks still lagged the broad market in 2014 due to high valuations.
- The best performing S&P 500 sector in 2014 was Utilities (+28.9%) as a result of investors playing defense and a squeeze on the shorts. Energy was the worst sector, falling -7.8% as new crude oil supplies outpaced economic growth.
- Weakness in foreign currencies in 4Q offset small gains in the international markets; the EAFE currencies fell by -5.3% and EM currencies fell by -4.5%. Valuations of int'l markets are generally more attractive, but future growth is in doubt.
- Hedge funds produced another year of disappointing results. But real estate continues to reach new highs.
- Commodities experienced the largest decline since 2008, led by the 41% decline in WTI. Falling commodity prices and lower yields are raising questions about future growth.
- Despite the end of QE and improvements in the economy, interest rates fell and spreads widened in 4Q. Domestic bonds outperformed global bonds for the year due to a strengthening dollar and geopolitical uncertainty.
- The surprising bond market continued in 2015, with the 30-year US treasury hitting an all time low yield of 2.22%.

U.S. Remains at Center of Global Growth

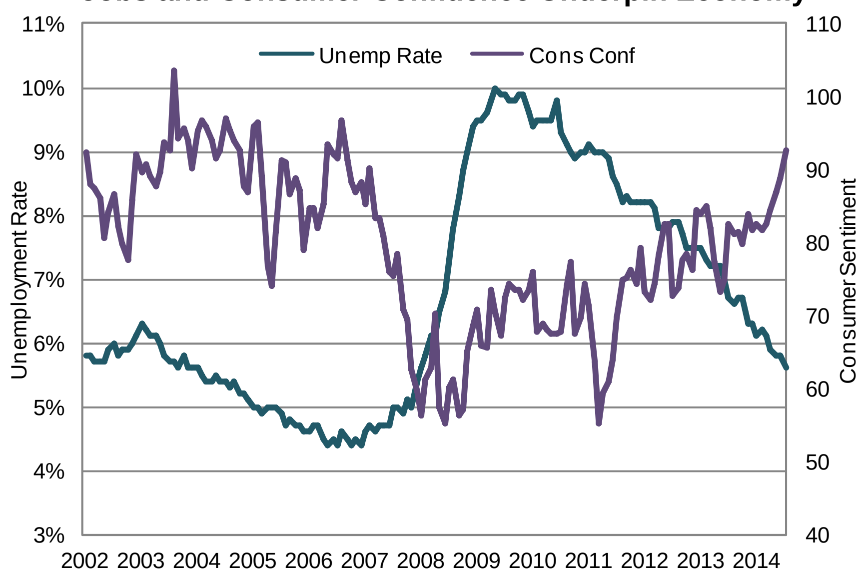
- The US continues to lead the global recovery, but economic growth in the US fell in the fourth quarter to an annual rate of +2.6%, after reaching +5.0% in the third quarter and +4.6% in the second quarter.

- One of the biggest developments in the last quarter is the 41% decline in the price of crude oil, mostly due to increased US production. OPEC is not cutting back, putting pressure on the higher cost domestic energy industry, especially the new production of shale oil.

- Retail sales (ex-gasoline) ended the year with a surprising decline of -0.4% in December, although big gains were expected due to lower energy prices. The housing market is also showing mixed results, with a modest improvement in starts, but weakness in prices.

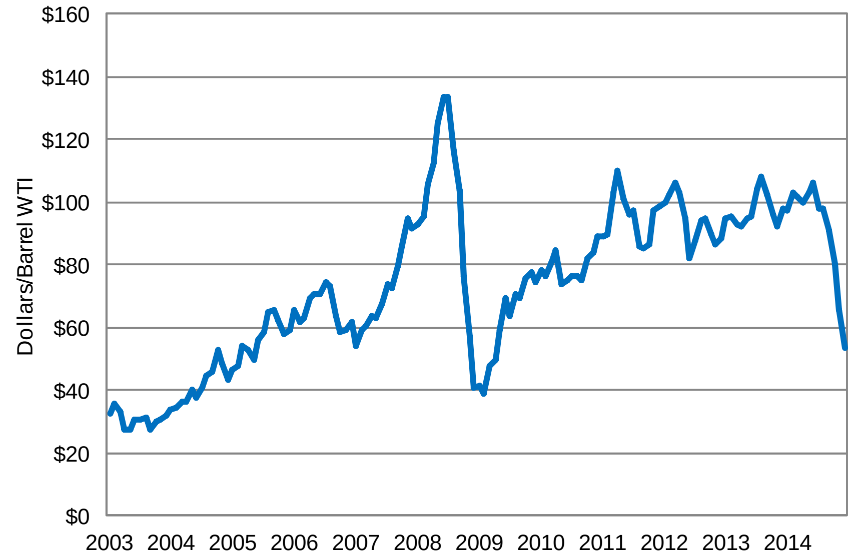
- US employment continues to trend in the right direction as the unemployment rate fell to 5.6% in December; but part of the decline was due to falling labor force participation. Wage growth is also a problem, as average hourly earnings declined by -0.2% in December due to a shift in the job mix versus an expected gain of +0.2%.

Jobs and Consumer Confidence Underpin Economy



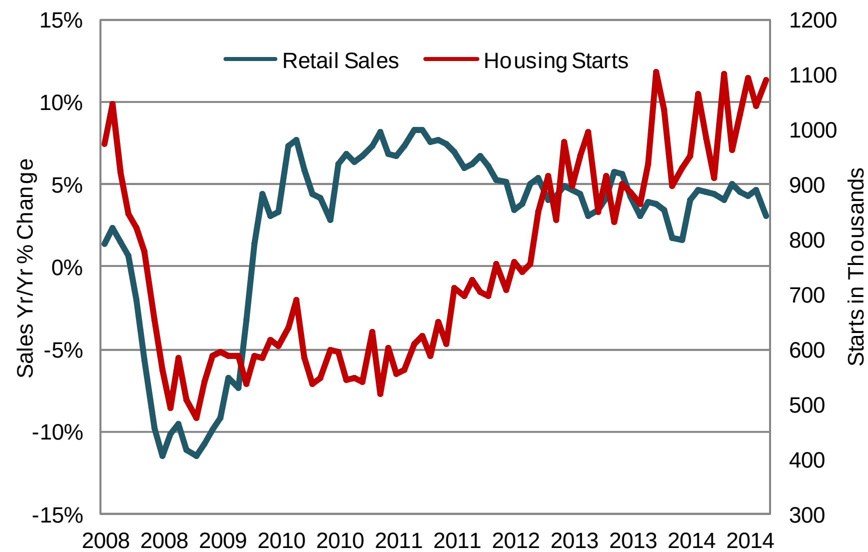
Source: Bureau of Labor Statistics, U of Michigan

Supply Leads to 41% Decline in WTI



Source: Federal Reserve

Housing is Showing Some Signs of Improvement



Source: US Census Bureau

Despite Volatility Stocks Rise to Record Highs

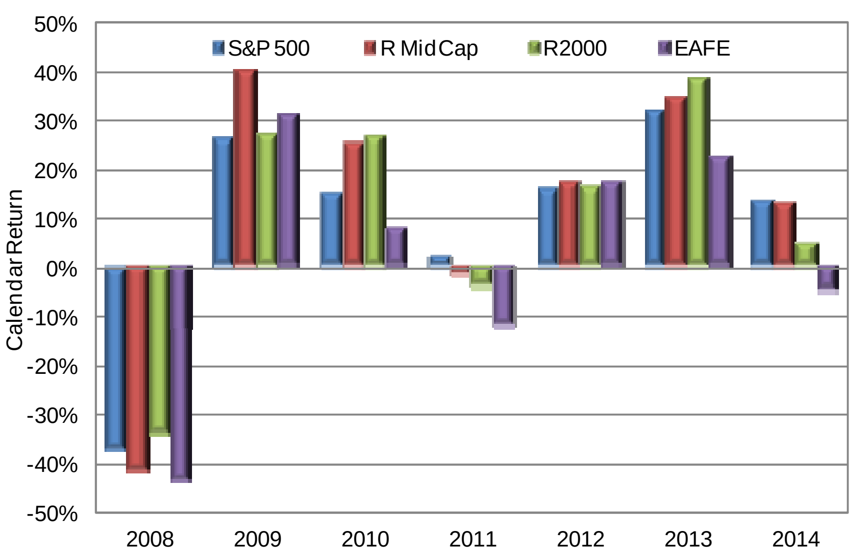
- For the first time since 1871, the US stock market advanced for six years in a row, as the S&P 500 gained +13.7% in 2014. The US stock market has never advanced for seven consecutive years, which further supports our expectation for below average returns in 2015.

- Energy stocks (-10.8% in 4Q) continued to decline in 2015, as oil prices slid to new lows. Utilities were the best performing stocks in 2014, with a gain of +28.9% due to a renewed focus on defensive stocks, and a squeeze in this heavily shorted sector.

- Small caps gained +4.9% for the year, but trailed large caps by the widest margin since 1998; despite high valuations (similar to small stocks) mid-cap stocks gained +13.2%, fueled by a boom in M&A.

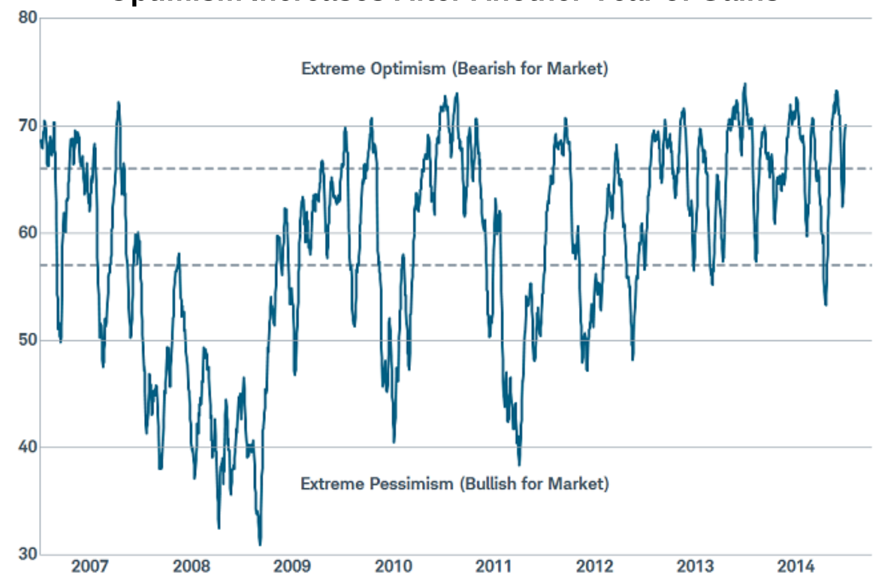
- Active managers continued to struggle in 2014, with just 19% of large cap managers beating the Russell 1000. Value managers fared even worse, with just 8% of managers outperforming the benchmark.

Large and Mid Cap US Stocks Win in 2014



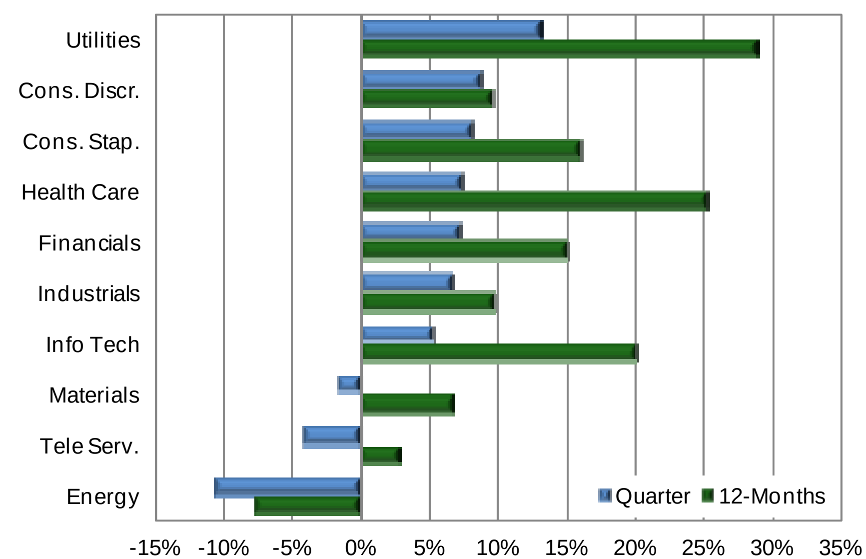
Source: Standard & Poor's, Russell, MSCI

Optimism Increases After Another Year of Gains



Source: Schwab & Ned Davis Research

Energy Sector Plagued by Oil Decline; Utilities Soar



Source: Standard & Poor's

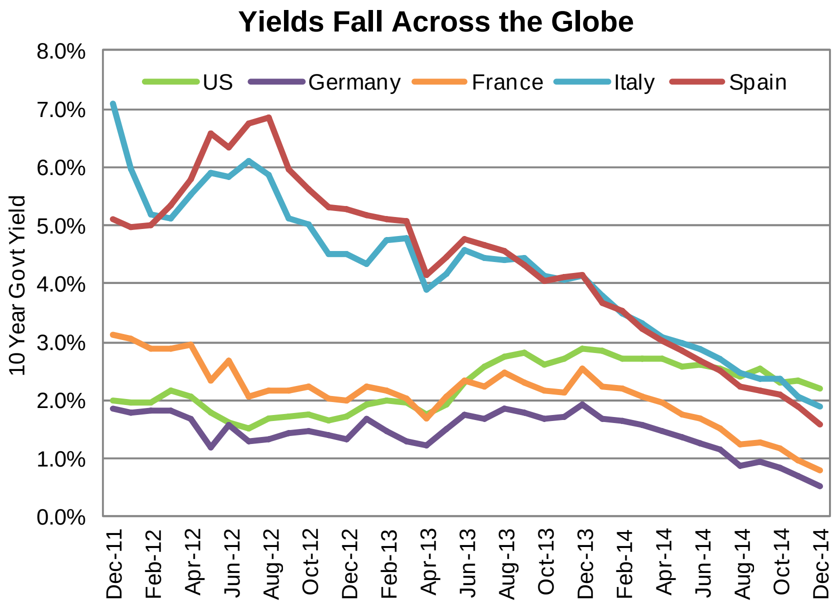
Curve Flattens and Spreads Widen

- Despite an improving economy, the US bond market surprised investors with a steady decline in rates and wider spreads for corporate bonds. In December, the 30-year treasury bond fell to 2.7%, a 30 month low, over questions of economic growth in 2015.

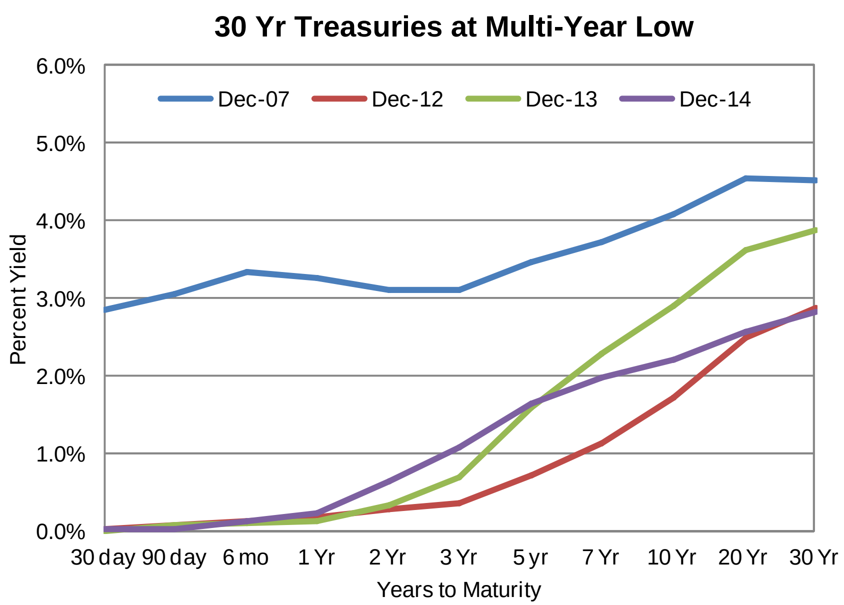
- Although the Fed ended QE purchases in October, the demand for U.S. debt remains strong due to the safe haven effect and the rising dollar. Mortgage refinancing spiked in December, which will prove a challenge for MBS returns in 2015; IG corporate bond spreads moved higher, but remain below (rich compared to) long term averages.

- High yield bonds lost -1.0% for the quarter; spreads widened by 100 bps, with the energy sector declining by -10%. Global bonds also underperformed due to the strength of the US dollar.

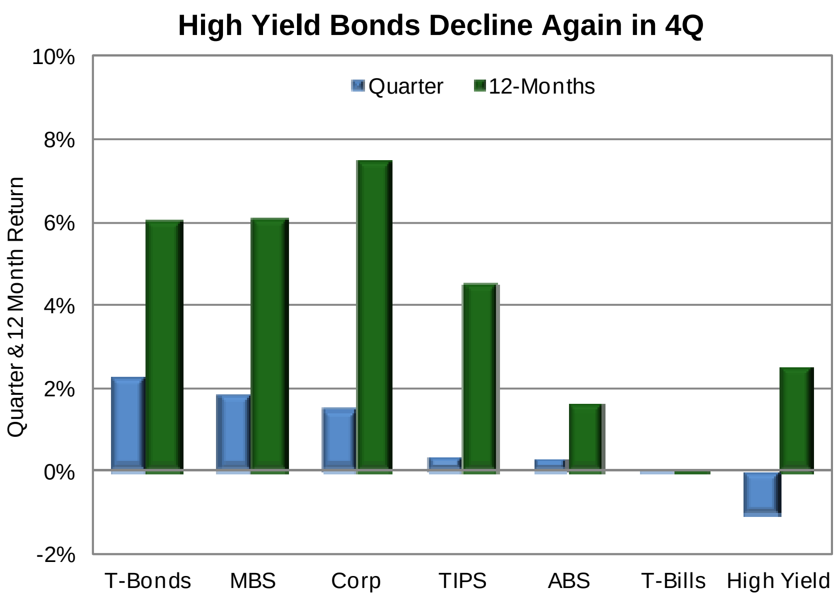
- Municipal bonds were one of the strongest performing sectors in the fourth quarter and the year. The Barclays Taxable Municipal Index was up 3.8% and 16% respectively.



Source: Federal Reserve, Bloomberg



Source: Federal Reserve



Source: Merrill Lynch

PORTFOLIO SUMMARY
DECEMBER 31, 2014

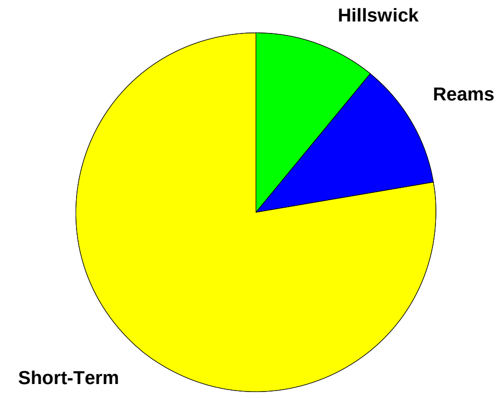
	Assets	Weight
Managed Accounts		
Hillswick Asset Mgmt	$164,420,200	11%
Reams Asset Mgmt	$170,802,100	11%
Total External Managed	$335,222,300	22%
Short-Term Account	$1,166,634,000	78%
Grand Total	**$1,501,856,300**	100%

- The value of the Total Fund increased by $213.3 million in the Fourth Quarter, due to net cash inflow of $209.6 million and gains of $3.8 million.

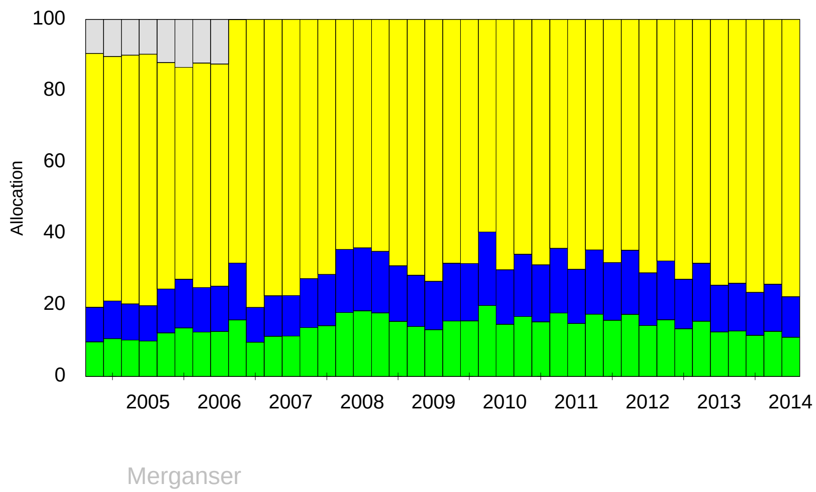
- Net investment gain/loss for the quarter were:

Hillswick	$1.8 million
Reams	$0.7 million
Short-Term	$1.3 million
Total	$3.8 million

CURRENT ALLOCATION



HISTORICAL ALLOCATION



PERFORMANCE SUMMARY - TOTAL RETURN
DECEMBER 31, 2014

Manager	QTR	Fiscal YTD	1 Year	3 Yrs	5 Yrs
Total Fund	0.3%	0.5%	1.7%	0.9%	1.4%
Benchmark[1]	0.1%	0.1%	0.4%	0.4%	0.7%
Hillswick Asset Mgmt	1.1%	1.3%	3.0%	1.2%	2.6%
BofA ML G/C 1-5 yr. A	0.5%	0.4%	1.4%	1.2%	2.1%
Reams Asset Mgmt	0.4%	0.4%	1.5%	1.8%	2.6%
BofA ML G/C 1-5 yr. A	0.5%	0.4%	1.4%	1.2%	2.1%
Total External Managers	0.7%	0.8%	2.2%	1.5%	2.6%
BofA ML G/C 1-5 yr. A	0.5%	0.4%	1.4%	1.2%	2.1%
Short-Term Account	0.1%	0.4%	1.5%	0.5%	0.8%
BofA ML 90-day T-Bill	0.0%	0.0%	0.0%	0.1%	0.1%

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

- The Total Fund posted a positive return in the fourth quarter, despite a small up-tick in corporate bond spreads. Hillswick's expectation that yields would fall and spreads would widen was a big driver of performance in 2014.

- Hillswick's performance once again proved the diversification benefits of their contrarian approach. Few fixed income managers expected yields to fall in 2014; the firm has also done a good job of managing the "yield curve" (maturity buckets) in their account.

- Hillswick still expects corporate and mortgage bonds to underperform, so they will wait for spreads to widen further before increasing the very small allocation to these sectors. Hillswick maintained a duration of 3.2 years, 20% longer than the index.

- Both Reams and Hillswick has a portfolio yield close to the benchmark of 1.2%. However, Reams did not have the capital gains from duration management produced by Hillswick, so Reams performed in-line with the benchmark over the last 12 months.

- Reams performance was negatively impacted (to a small degree) by their corporate bond allocation (37% of the account) and positively impacted by their mortgage bond exposure (35%).

- The staff-managed Short-Term Account was able to take advantage of the up-tick in yields to generate a remarkably strong 1.5% return in the last 12-months, matching the performance of Reams' longer duration account. The peer group comparisons on page 8 show the success of the overall investment program.

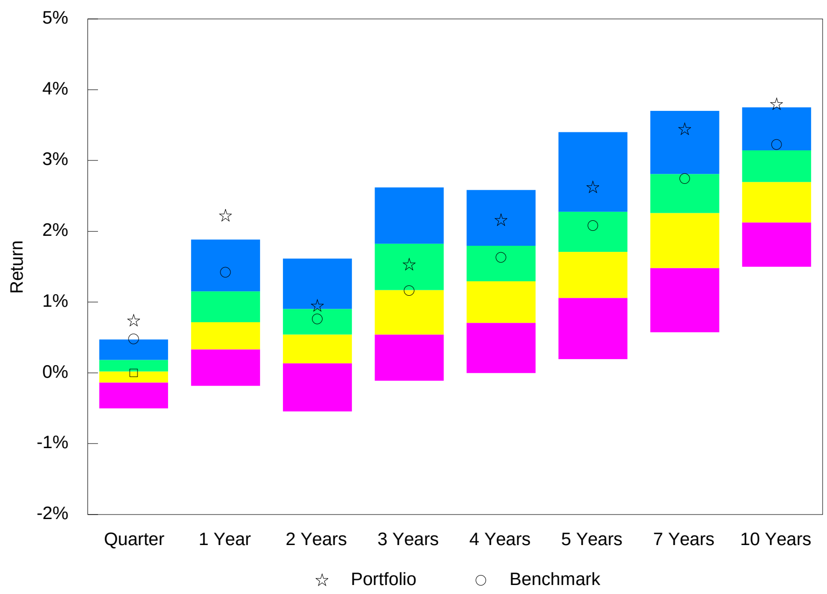
CONSOLIDATED BALANCE SHEET and CASH FLOW SUMMARY FOR THE FISCAL YEAR

JULY 1, 2014 TO DECEMBER 31, 2014

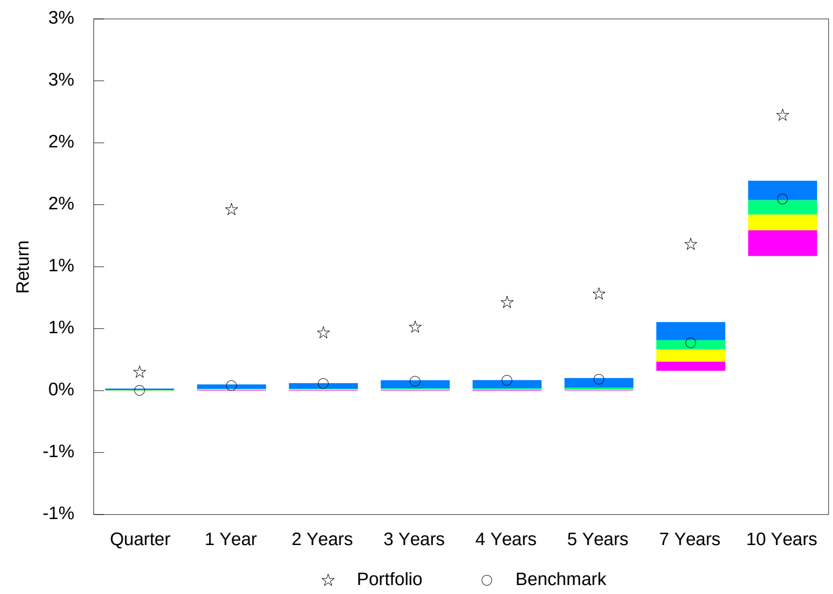
Manager	Beginning Balance	Net Cash Flows	Income	Gain/(Loss)	Ending Balance
Total Fund	**$1,412,053,200**	**$83,930,400**	**$7,034,500**	**($1,161,800)**	**$1,501,856,300**
Externally Managed					
Hillswick Asset Mgmt	$162,331,600	$0	$1,980,800	$107,800	$164,420,200
Reams Asset Mgmt	$170,169,600	$0	$1,262,600	($630,100)	$170,802,100
Total Externally Managed	$332,501,200	$0	$3,243,400	($522,300)	$335,222,300
Short-Term Account	$1,079,551,900	$83,930,400	$3,791,100	($639,400)	$1,166,634,000

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

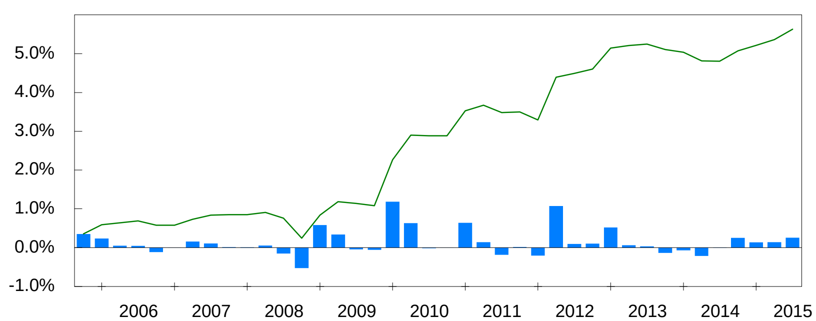
TOTAL EXTERNAL MGRS VS. PEER GROUP



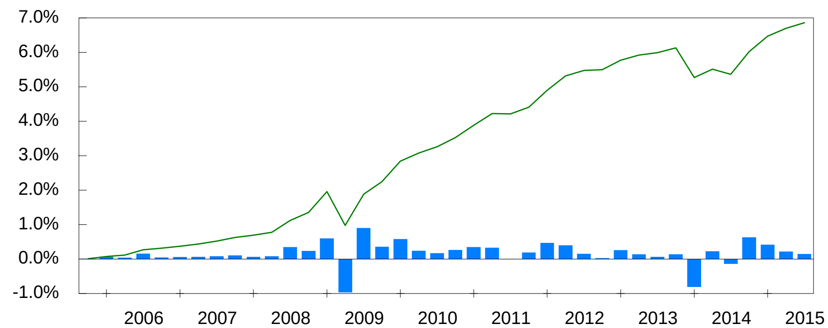
SHORT-TERM VS. PEER GROUP



TOTAL EXTERNAL MGRS VALUE ADDED



SHORT-TERM VALUE ADDED



MANAGER SCORECARD

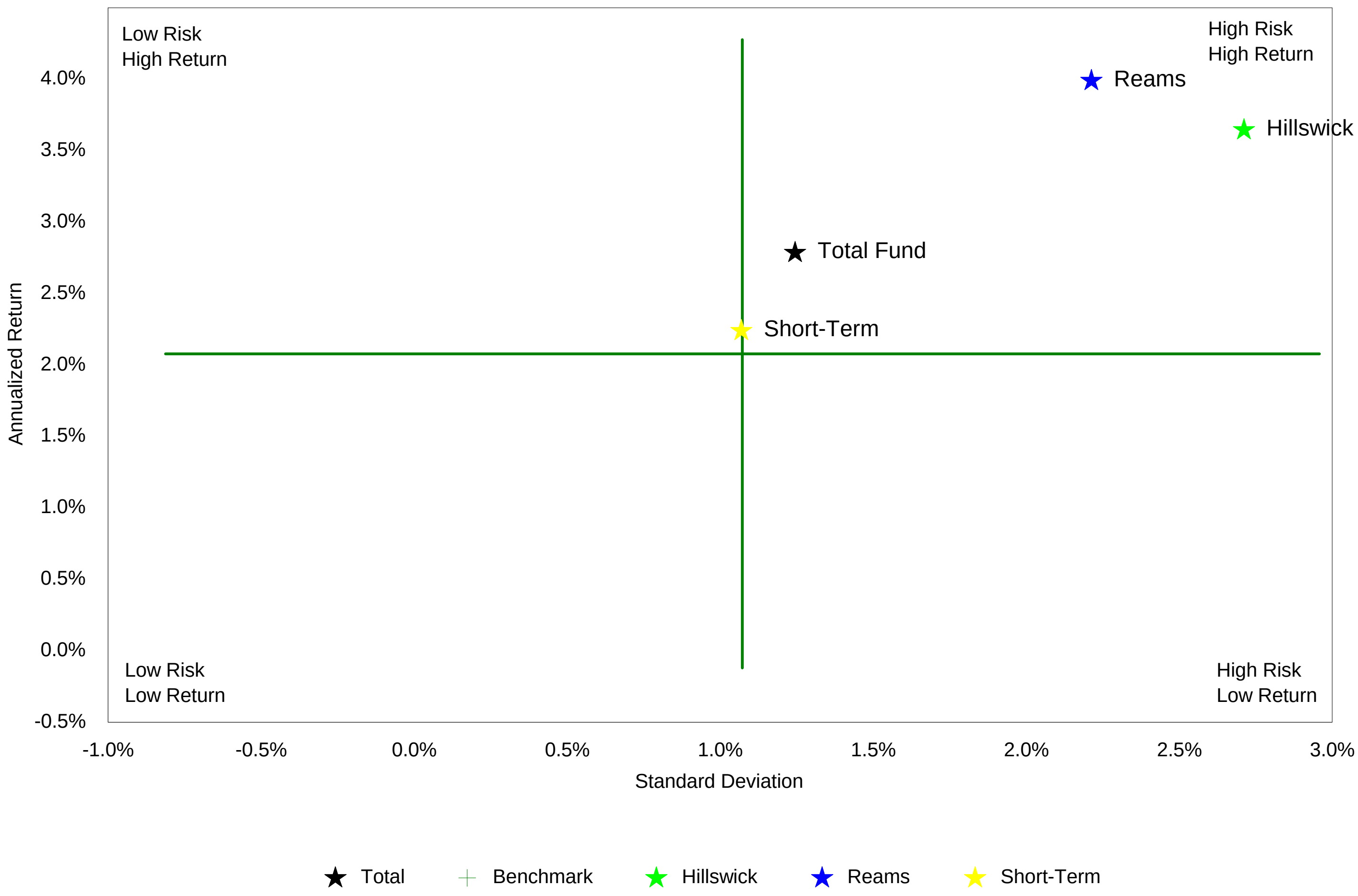
TEN-YEAR RESULTS

Manager	Return	Index Return	Std Dev	Alpha	Beta	Batting Average	Incept
Total Fund	2.79	2.08	1.25	0.46	1.35	850	1Q05
Hillswick Asset Mgmt.	3.65	3.25	2.71	0.13	1.14	450	1Q05
Reams Asset Mgmt.	3.99	3.25	2.21	0.98	0.86	725	1Q05
Short-Term Account	2.24	1.56	1.07	0.78	0.31	900	1Q05

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	NA	Exceed	NA	Positive	High
Hillswick Asset Mgmt	Exceed	Exceed	OK	OK	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.