

- Stable Value: What Is It? 2
- Risk/Return Management
Liquidity, Diversification, Credit Quality 3-7
- Meet the Managers 8
- Stable Value: What are the components? 10

The VantageTrust PLUS Fund: A Balanced Approach to Stable Value

STABLE VALUE FUNDS PLAY AN IMPORTANT ROLE IN DEFINED CONTRIBUTION PLANS. Offering current income coupled with capital preservation, they are a unique option for conservative investors and diversified investment programs alike. The VantageTrust PLUS Fund’s balanced approach to stable value investing helps investors achieve competitive income levels in a well-managed, risk-controlled environment.

Stable value-like products have evolved over the decades, from annuity products to deposit certificates to money market funds. Stable value funds have likewise evolved and offer features that are an improvement over less-diversified alternatives.

Today, a state-of-the-art stable value fund may incorporate top tier investment managers investing globally, world-class risk-management models, and sophisticated insurance policies.

For almost 15 years, ICMA-RC has provided access to stable value through the VantageTrust PLUS Fund. The Fund’s objective is “To provide a high rate of income consistent with preservation of capital.” The results achieved demonstrate that the Fund has been successful in meeting this important objective for investors.

What is behind the success? A balanced approach to management – managing for return and, importantly, managing risk.

**The PLUS Fund offers investors what they desire:
a competitive rate of income consistent with preservation of capital.**

#1 Fund for 10 Years
Hueler Stable Value Universe 6/30/05

	1 Year	3 Year	5 Year	10 Year
PLUS Fund	4.78%	4.75%	5.20%	6.11%
% Rank	4%	17%	50%	1%
Number of Funds	24	24	20	19

Note: Data provided by Hueler Analytics and reflects gross returns before fees for all pooled stable value funds tracked within the index universe. For the ten-year period ending June 30, 2005, Hueler Analytics lists the VantageTrust PLUS Fund as the highest returning fund among the 19 funds within the Hueler database that have a ten-year performance record.

Please consult Making Sound Investment Decisions: A Retirement Investment Guide carefully for a complete summary of all fees, expenses, charges, financial highlights, investment objectives, risks and performance information. Investors should consider the Fund’s investment objectives, risks, charges and expenses before investing or sending money. For a copy, contact ICMA-RC Services LLC, 777 North Capitol Street NE, Washington, DC 20002-4240. 1-800-669-7400.

Stable Value: What is it?

A Unique Asset Class

Although stable value exhibits characteristics shared with both bonds and cash, it is neither of these. It is a unique asset class with its own distinct advantages and disadvantages. Reserved solely for retirement plans, Stable Value funds are unique in providing both the liquidity and low risk of money market funds, combined with higher returns similar to intermediate-bond funds.

The chart below demonstrates these advantages, showing stable value funds with lower risk than both cash equivalents and intermediate bonds, and returns well above cash and just slightly below bonds.

In the table below, we highlight some other features of stable value funds relative to other asset classes. Like cash, stable

value funds (measured by the Hueler index*) have experienced no monthly periods over the past 20 years with a negative return. Like cash, their risk, as represented by standard deviation, is low.

The low risk levels are due to book value accounting for the assets, a result of insurance and wrap contract arrangements. This gives them a return volatility pattern more similar to a money market fund while, on average, producing higher income passed through to investors over time.

Why might stable value funds be considered a unique asset class? Not only do stable value funds have unique risk/return characteristics, they also have a very low correlation to other asset classes. This means that the funds' returns, as measured by the Heuler index, do not move in concert with, say, stocks or bonds. This makes stable value funds a particularly good diversifier in an investment program.

Glossary of Stable Value Terms:

Book value – the initial cost of an investment, plus accrued interest. For stable value, the dollar amount of deposits, plus interest minus withdrawals.

GIC - Guaranteed investment contract; the two primary types of GICs in which Stable Value fund's invest include:

Traditional GIC – issued by an insurance company, with the financial backing of the insurance company's general account assets. (See page 10.)

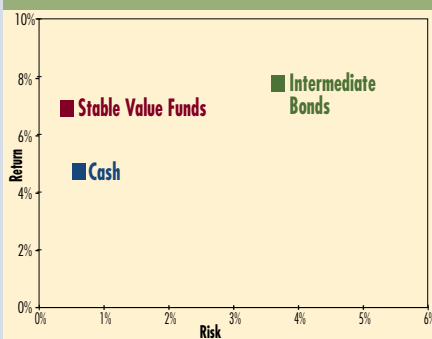
Synthetic GIC – a traditional GIC substitute that utilizes a bond portfolio with an insurance wrapper (contract) to provide for book value accounting and mimic the performance and risk of a traditional GIC. (See page 10.)

Insurance policy or (wrap) contract - generic term used to refer to a traditional GIC or wrap contract (for a synthetic GIC). A contract that provides book value accounting for participant-initiated withdrawals.

Crediting rate – the rate used to credit income in a stable value portfolio; for a synthetic GIC, it is determined based on a portfolio's yield and the amortization of the realized and unrealized gains and losses on the value of the underlying securities.

Portfolio or blended rate – the rate used to credit income to a participant's account; it is determined by combining the rates of component parts of a stable value fund. For example, if a fund holds both traditional and synthetic GICs, the portfolio rate will be the weighted average of the traditional GIC rates combined with the crediting rate of the synthetic GIC portion of the fund.

Risk vs. Return: July 1985 - June 2005



This risk/return chart shows the annualized return and standard deviation of three asset classes: cash (30-day T-bill), bonds (Lehman Brothers Intermediate Government/Credit Bond Index) and stable value (Hueler) for the 20 year period ending 6/30/05.

Twenty Years of Principal Preservation

(Based on Monthly Periods Through 6/30/05)

	# of Negative Periods	# of Positive Periods	Sharpe Ratio	Standard Deviation	Correlation (relative to Hueler)
Stable Value (Hueler)	0	240	1.83	0.43	1.00
Cash (30 Day T-bill)	0	240	0.00	0.61	0.85
Bonds (LB IT G/C)	62	178	0.25	3.69	0.20
Stocks (S&P 500)	87	153	0.15	17.41	0.06

Source: Ibbotson Associates, Inc.

Past performance is no guarantee of future results.

*Hueler Companies offers the only Stable Value Indices available that represent the performance returns of actual stable value pooled funds and stable value separate account portfolios. The Hueler Pooled Funds Universe is the Stable Value Fund industry benchmark used by institutional investors, consultants, advisors and plan sponsors for monitoring the pooled fund universe.

The PLUS Fund has provided favorable returns versus the stable value fund universe. But returns are only half of what investors seek. **Capital preservation** is also paramount, and it is achieved through thoughtful risk management.

Retirement plan sponsors and participants utilizing a stable value fund want assurance that their capital is being preserved, without chance of loss. This depends on risk management methodologies that are specific to stable value.

For stable value funds, there are three important components to risk protection – liquidity, diversification and credit quality. These components are the responsibility of both the Fund’s adviser and the insurers selected to insure the Fund’s book value (thus providing capital preservation):

- **Liquidity** – the first line of protection for investors as well as the Fund’s insurer responsible for insuring participant payouts at par, without capital loss.
- **Diversification** – a second line of protection for both investors and Fund insurers. Investing across multiple asset types, sectors and securities helps mitigate the multitude of specific investment risks.
- **Credit quality** – a third line of protection to specifically avoid default risk. This is most important at the insurance policy level.

Plan sponsors and participants can rely on these risk protections, with the same assurance as the insurance/contract issuers that ultimately protect the Fund’s capital preservation feature.

1. Liquidity

Liquidity is the primary risk protection for stable value funds. Investors, like the Fund’s insurers, need to be confident that the PLUS Fund liquidity structure is sufficient to meet normal cash flow requirements and special risks (e.g., large client transfer risk, market event risk).

When insurance/contract issuers evaluate the risk of a stable value fund, they prefer liquidity structures that incorporate both an adequate cash buffer as well as layers of liquidity within the remainder of the fund. Additionally, the liquidity risk is mitigated by the existence of a **large, diversified base of investors**. The larger the fund and the more diverse the investor base, the lower the risk to insur-

ers, the lower the policy fee and the more benefit to investors in investment flexibility and lower fees. This is why the most important factors that insurers consider when making risk assessments are cash flow history, potential cash flow requirements and cash flow diversification.

The nature of the PLUS Fund’s client base is of great benefit to the Fund, and ultimately, to its investors. Cash flow protection comes from fact that there are over 7,000 employer plans and 650,000 investors or potential investors providing steady cash inflows to the Fund and a consistently growing employer plan base. This dynamic allows the Fund to maintain a liquidity pool of 3-5 percent of Fund assets. These cash equivalents are more than adequate to satisfy normal participant distributions, transfers, and other cash flow needs, since, over the history of the fund, daily outflows from the Fund rarely exceed 0.1 percent of the \$4.8 billion Fund. (Assets as of July 31, 2005)

In addition to the liquidity pool there are **layers of liquidity** implicit in the structure of the remainder of the Fund. For example, the traditional GICs are benefit responsive (available for liquidity needs) and the synthetic GIC portfolios consisting of underlying marketable bonds are readily accessible if needed in an emergency situation. Additionally, the Fund’s **laddered maturity structure** for the traditional GIC portfolio provides ongoing liquidity if needed.

Finally, an important component of liquidity management is the existence of other payout protections, such as rules regarding participant and employer payouts. The PLUS Fund offers daily liquidity to individual investors, but reserves the right to limit employer plan payouts over a 12-month period. This provides liquidity protection for the Fund and its investors.

2. Diversification

Diversification of fund assets is the second risk protection because it helps mitigate the multitude of investment-related risks faced by Fund managers and insurers. Diversification offers benefits but needs to be well managed to avoid unintended biases and potentially higher management fees.

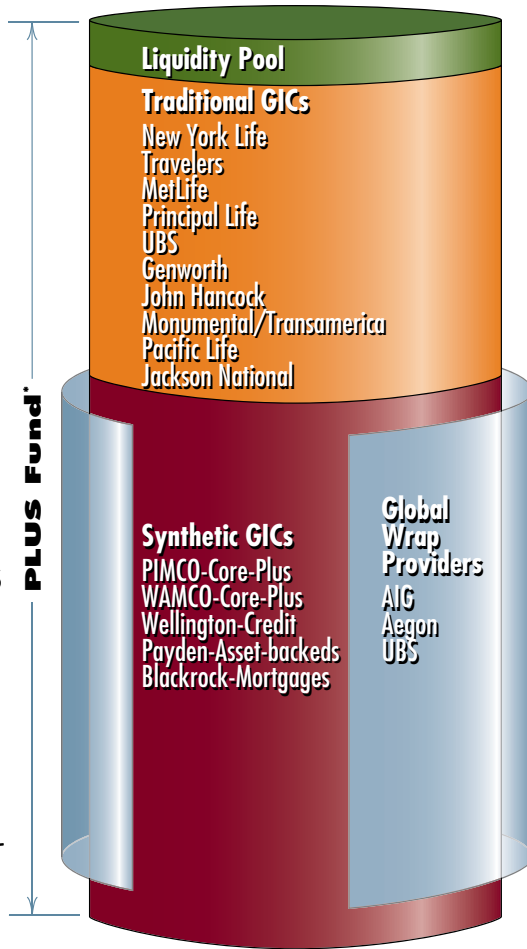
A BALANCED, FLEXIBLE FUND STRUCTURE

The PLUS Fund is designed to increase safety of principal and smooth returns through **both asset and insurance company diversification**. The Fund pursues its objec-

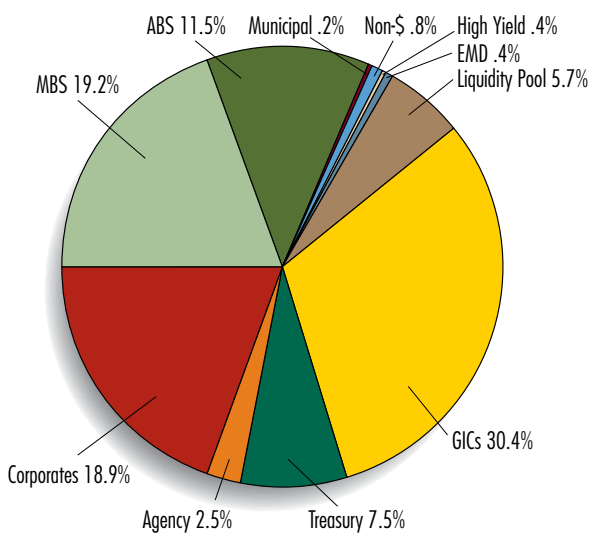
tive by investing a small portion of assets for liquidity and investing the remainder in a combination of traditional and synthetic GICs.

With almost \$5 billion in assets, the VantageTrust PLUS Fund benefits from **economies of scale**. With this asset size comes the opportunity to invest in a broadly diversified selection of assets and investment strategies in a cost effective manner.

As of June 30, 2005, traditional GICs represented approximately 30 percent of the Fund, with synthetic GICs making up 65 percent and 5 percent in the liquidity pool. These allocations represent a recent point in time and it is anticipated that **these percentages will change as investment opportunities arise**.



*as of 6/30/05



The weighting to different asset types within the PLUS Fund portfolio is flexible and will change over time, depending on the market environment and investment opportunities.

DIVERSIFICATION OF THE TRADITIONAL GIC PORTFOLIO

Diversification is achieved in the traditional GIC holdings by combining multiple investment contract issuers, contract maturities and contract types. As of June 30, 2005, the Fund held 23 different contracts issued by nine separate insurance companies. Each issuer must pass the independent scrutiny of ICMA-RC's Credit Research Group and **the credit quality of the traditional GIC portfolio is Aa2**.

The PLUS Fund limits investment in traditional GIC contracts of any single issuer based on credit quality with a maximum allocation to any one firm of 10 percent. At present, the highest allocation is 8 percent and the remainder are 1 to 5 percent. In addition, PLUS Fund contract issuers must have a Moody's rating within the high-grade classification (at least Aa3) at the time of investment.

The portfolio is also laddered, meaning that maturity dates are scheduled sequentially over several years. This structure is beneficial to the Fund because it provides known future liquidity, and reduces re-investment risk. If all of the contracts matured at approximately the same time, the future yield would be unacceptably time dependent.

This staggered maturity structure allows this portion of the PLUS Fund's yield to follow the general direction of interest rates, albeit at a slower pace. To further smooth returns and moderate reinvestment risks, the Fund's portfolio is **diversified among fixed, indexed, and floating interest rate contracts** and is structured to hold contracts containing a variety of maturity dates and payout configurations.

The laddered structure also provides a known future liquidity source for substantial cash flow needs that may develop.

DIVERSIFICATION OF THE SYNTHETIC GIC PORTFOLIO

Diversification is achieved in the Fund's synthetic GIC portfolio by utilizing a **multi-manager approach** to bond and issuer management.

For a traditional GIC, the same insurance company managing the underlying general account assets also provides the insurance wrapper.

A synthetic GIC can be thought of as a deconstructed traditional GIC with the two primary functions, yield and insurance of principal, being provided by (at least) two separate product experts. A synthetic GIC allows the fund adviser to hire the best available bond manager and the best available insurance company. By separating these two essential functions, a primary disadvantage of traditional GICs and insurance company general accounts, single issuer risk, is mitigated.

BOND COMPONENT OF THE SYNTHETIC GIC PORTFOLIO

Managed by five top-tier fixed income management firms, adhering to four distinct disciplines, the bond portfolio of the Fund's synthetic GIC holds **over 900 separate securities representing numerous issuers**.

Selected using the rigorous due diligence process employed at ICMA-RC for years, these five subadvisers follow ICMA-RC's investment guidelines to ensure the combined portfolio meets the PLUS Fund's risk and return objectives.

Manager	Portfolio Segment / Bond management focus
Payden & Rygel	Asset-backed (ABS)
Blackrock	Mortgage-backed (MBS)
Wellington	Credit (corporate bonds)
PIMCO	Diversified
WAMCO	Diversified

(Please see further descriptions provided on Page 8.)

WRAP CONTRACT PROVIDERS FOR THE SYNTHETIC GIC PORTFOLIO

The synthetic GIC portfolio's insurance wrapper consists of three wrap contracts issued by **three separate high quality companies**. These companies protect the bond portfolio's book value against market loss. They include AIG, Aegon and UBS. In a global wrap structure, each is responsible for one third of any claim.

Each of these highly rated firms has performed its own stringent due diligence on the PLUS Fund, evaluating liquidity needs, fund structure, management and resources prior to issuing the wrap contract.

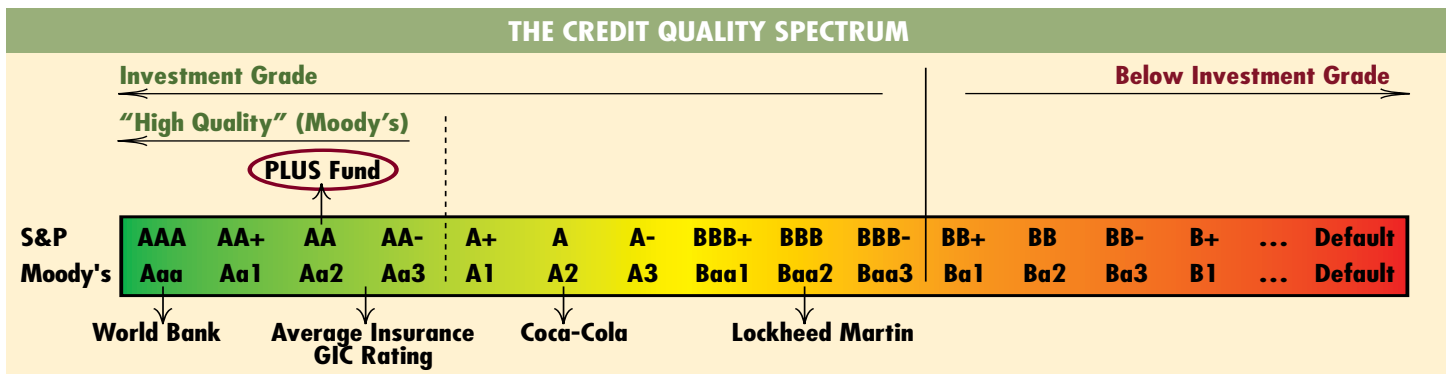
Duration: **WHAT IS IT?**

Duration is a risk measure used for fixed income securities that fluctuate in value as a result of interest rate changes. It is computed using maturity and cash flow (payout) characteristics, and measures a bond's price sensitivity to interest rate changes. For example, a longer duration, for most fixed income securities, indicates increased interest rate sensitivity and potential price volatility.

While it is a commonly used in fixed income management, it is not commonly used as a risk measure in the stable value industry. A GICs "price" (value) does not change with interest rates because they are not "marked-to-market". Rather, they are held at book value and, therefore, **duration is not an accurate measure** of their risk. Regardless of the direction or magnitude of a change in interest rates, the price of a traditional or synthetic GIC remains unchanged at book value as do the terms of repayment and interim cash flows. Therefore, industry specialists view a GICs duration to be, essentially, zero.

While a stable value fund's duration is not a meaningful risk measure for a plan sponsor or participants, it is monitored by wrap providers who insure the synthetic GICs' book value. Duration is computed and reported in some industry publications. Based on calculations by Hueier Analytics, a leading industry data source, the PLUS Fund's duration was 3.28 years, as of June 30, 2005. Within the Hueier Analytics database, durations for stable value funds range from 1.90 to 3.80 years with the average at 2.58 years, and the median at 2.52 years. The PLUS Fund is at the longer end of this range, and is explained by the Fund's opportunistic approach to traditional GICs and corporate bond investments insured by high-quality wrappers.

Because both traditional and synthetic GICs are insured by high-quality issuers that protect a shortfall between book and market value, duration is not a meaningful risk measure for a stable value fund.



3. Credit Quality

The third type of risk protection within a stable value fund is maintaining a high credit quality. Most investors choose a stable value fund because they are seeking preservation of principal, and steady value growth through a steady crediting of income. Understanding the importance of principal safety to these investors, the PLUS Fund’s management team adheres to strict credit-quality standards. As the chart below shows, **Moody’s overall credit rating of the PLUS Fund is Aa2, the third highest possible, which the rating firm terms “high quality by all standards.”**

TRADITIONAL GIC CREDIT MANAGEMENT

ICMA-RC’s Due Diligence and Credit Analysis

PLUS Fund traditional GIC contracts are underwritten by nine carefully analyzed, top-rated, insurance companies offering significant diversification of credit risk.

Rigorous credit standards are applied and all approved issuers are highly rated by the major rating agencies. All **approved issuers are rated Aa3 (excellent financial security) or higher** by Moody’s Investors Service at the time of purchase. However, the Aa3 Moody’s rating is merely a minimum standard. ICMA-RC conducts its own internal review, thoroughly researching each potential issuer before final approval. The approval review process includes meeting on-site with company management, in addition to conducting an in-depth analysis of statutory financial statements and (when available) SEC filings.

Ongoing Credit Review

Once approved, a contract issuer must continue to meet stringent credit criteria to remain eligible for new investment. ICMA-RC staff **continuously monitors the issuers and their credit ratings**. The on-going monitoring process includes the same stringent process used in the approval process and includes monitoring of financial statements, financial news and major credit agency ratings, reports and press releases, as well as discussions with rating agency analysts.

Proprietary Credit Rating System

ICMA-RC employs its own numeric credit rating system for use with contract issuers. By assigning internally developed numeric ratings to each contract issuer, ICMA-RC has generated a database that allows for a systematic assessment, a tool for comparing the relative credit quality of companies, and a means of tracking companies over time.

ICMA-RC’s numeric rating consists of both a **quantitative and qualitative component**. The quantitative component focuses on key financial measures traditionally reviewed by ICMA-RC’s due diligence unit, including asset quality, capitalization, liquidity, profitability and interest rate risk. The qualitative component incorporates factors such as capital size, competitive position, asset and interest rate risk, quality of earnings and earnings potential, management, and subsidiary and/or parent company exposure. The quantitative component provides a snapshot of a company’s financial condition at a point in time, while the qualitative analysis provides a more prospective evaluation.

When ICMA-RC's internal ratings vary from Moody's ratings, or indicate a downward trend in a company's risk profile that might result in a Moody's downgrade, ICMA-RC will make appropriate adjustments to its maximum exposure limits. For example, **in early 2002, ICMA-RC's internal rating for a specific issuer fell** below Aa3. Therefore, the firm was removed from the approved list for future placements; **10 months later Moody's downgraded the company** from Aa3 to A1. When this downgrade occurred, ICMA-RC was able to re-negotiate the contract to provide more favorable terms for investors. Specifically, the maturity of the contract was accelerated. The Fund has already received half of the contract's principal with the remainder (less than 1 percent of the Fund) to be paid in early 2006, more than one year ahead of the initial maturity.

The PLUS Fund has never experienced a default of any GIC contract in its entire history.

SYNTHETIC GIC CREDIT MANAGEMENT

A clear risk of investing in fixed income securities is that one (or more) of the issues could experience a significant drop in price or, in an extreme situation, even default.

Several layers of safeguards are at work within the PLUS Fund to protect against this risk.

First, and most important in ICMA-RC's synthetic GIC credit management, is the credit quality and structure of the insurance wrapper that protects the portfolio's book value. ICMA-RC utilizes multiple providers to diversify issuer credit risk and **only employs very high quality firms** (Aa3 or higher, meaning excellent financial strength as rated by Moody's). Currently, the Fund's synthetic GIC is insured through a global wrap contract, which means that each firm shares equally in the portfolio's book-to-market risk. The firms include AIG, Aegon and UBS. Because they are the ultimate "credit" that stands in front of the underlying bond portfolios, ICMA-RC conducts intense credit research, selects only very high quality firms and will take action if any single issuer's credit quality deteriorates.

Second, the bond portfolio underlying the synthetic portion of the Fund is highly diversified. Over 900 separate securities are managed by five top-tier fixed income management firms with no single manager responsible for more than 20% of the PLUS Fund. Each manager must follow stringent ICMA-RC investment guidelines, approved by the Fund's governing Boards and insurers. For example, the credit component of the Fund, managed by a leading credit-focused firm, must follow strict diversification and credit limits. Specifically, minimum quality limits are established for each component of the bond portfolio. While minimum quality standards are set, higher standards are targeted and achieved.

The underlying asset structure and credit quality of the bond portion of the PLUS Fund's synthetic GIC as of June 30, 2005 is:

Manager	Portfolio Benchmark	Portfolio Credit Quality	Benchmark Quality
P&R	Lehman ABS	Aa1	AAA/AA1
Blackrock	Lehman MBS Fixed Rate	Aaa	AAA
Wellington	Lehman Credit	A2	A1/A2
PIMCO	Lehman Aggregate	Aaa	AA1/AA2
WAMCO	Lehman Aggregate	Aa1	AA1/AA2

Portfolio quality reflects Moody's ratings and are equal to those of S&P and Fitch. The benchmark quality is computed by Lehman Brothers, using blended ratings by Moody's, S&P and Fitch.

The overall credit quality of the bond portfolio is Aa2 (defined as "high" by Moody's). This strong credit rating is further supported by the high credit quality of the portfolio's book insurers.

Finally, the strict investment guidelines in place with each manager dictate the steps required to be taken should a security downgrade occur and policy limits pierced. This ensures focused attention to any such event, which is of particular importance to the portfolio's book value insurers.

Meet our Managers:

ICMA-RC VANTAGETRUST PLUS FUND MANAGEMENT TEAM

Stable value management has been a hallmark of ICMA-RC's investment program for over two decades. The dedicated, experienced stable value team is led by Chief Investment Officer Wayne Wicker, CFA, and Daryl Dennis, CFA, Vice President, Fixed Income. Both have over two decades of fixed income experience and are joined by 13 investment professionals, most of whom are CFA charterholders.

The team's resources are deep, including access to extensive research and state-of-the-art analytical tools. CFA charterholders experienced in insurance company analysis are responsible for the credit research and due diligence analysis of current and prospective GIC issuers and wrap contract providers. ICMA-RC's recognized skill with the multi-management approach to investing enables the PLUS Fund to leverage industry knowledge and experience from leading bond management and insurance industry firms.

In addition to setting fund strategy, the investment team's key focus is on retaining and monitoring these top-in-class bond management firms and wrap contract providers to ensure, through compliance with stringent guidelines and comprehensive forward-looking due diligence, the PLUS Fund will continue to meet investor objectives.

THREE HIGH-QUALITY FINANCIAL SERVICES FIRMS PROVIDE WRAP CONTRACTS FOR THE SYNTHETIC GIC SEGMENT OF THE PLUS FUND. THEY ARE LEADERS AMONG WRAP ISSUERS.

AIG FINANCIAL PRODUCTS CORP. (AIG-FP)

AIG-FP is a wholly-owned subsidiary of American International Group (AIG). AIG is a holding company for (1) the largest life insurance organization in the US, (2) one of the largest general insurance organizations worldwide, and (3) diversified financial services and asset management businesses.

AEGON USA LIFE GROUP (AEGON USA)

The ultimate parent of AEGON USA is AEGON N.V., the second largest insurer in the Netherlands and one of the largest publicly-traded insurance holding company worldwide. A US-based subsidiary serves as the wrap contract conduit.

UBS

UBS is a financial services firm with leading market positions worldwide in wealth management, investment banking, asset management, and retail and commercial banking.

FIVE NATIONALLY RECOGNIZED TOP-TIER INVESTMENT MANAGEMENT FIRMS SERVE THE SYNTHETIC SEGMENT OF THE PLUS FUND PORTFOLIO.

PACIFIC INVESTMENT MANAGEMENT COMPANY (PIMCO)

PIMCO is recognized as a leader in the fixed income industry, and manages over \$455 billion in fixed income assets, under multiple fixed income mandates. Owned by Allianz, PIMCO serves as the fixed income platform for Allianz Global Investors (AGI). PIMCO manages a portion of the PLUS Fund under a **modified Core-plus** mandate.

A Core-plus mandate typically permits use of assets in the Lehman Aggregate Bond Index (considered core assets), as well as non US Dollar, high yield, and emerging market assets. ICMA-RC has set very conservative (less than 10%) limits for these three non-core asset segments to create the modified Core-plus strategy.

WESTERN ASSET MANAGEMENT COMPANY (WAMCO)

WAMCO is a leader in core and core-plus fixed income strategies. WAMCO is a wholly owned subsidiary of Legg Mason, Inc., and manages \$290 billion in fixed income assets. WAMCO manages a segment of the PLUS Fund synthetic GIC portfolio using a **modified Core-plus** strategy.

PAYDEN & RYGEL

Payden & Rygel is one of the largest, privately owned global investment managers, with more than \$50 billion in assets. The firm is a leading provider of actively managed fixed income portfolios and is recognized for its strength in managing low duration strategies. Payden & Rygel manages the **asset backed securities (ABS)** segment of the PLUS Fund portfolio.

WELLINGTON MANAGEMENT COMPANY, LLP (WELLINGTON MANAGEMENT)

Wellington Management is a leading provider of global investment management services, serving \$500 billion in both equities and fixed income assets. Noted for its bottom-up research-oriented process and credit sector rotation skills, Wellington Management manages a segment of the PLUS Fund portfolio using a **credit-only** mandate.

BLACKROCK FINANCIAL MANAGEMENT (BLACKROCK)

BlackRock is a premier provider of global investment and risk management products. With \$414 billion in assets under management (\$281 billion in fixed income assets), BlackRock is recognized as a leader in the mortgage-asset market. BlackRock manages the **mortgage backed securities (MBS)** segment of the PLUS Fund portfolio.

Conclusion

IN THE MIDST OF MARKET GYRATIONS AND NEW ALTERNATIVE INVESTMENT opportunities, stable value continues to be a popular safe haven for conservative investors saving for or during retirement. Funds that offer the opportunity for competitive rates of income coupled with capital preservation are an attractive option either as a single investment or as part of a well-diversified retirement portfolio.

ICMA-RC's VantageTrust PLUS Fund stands out as one of the highest yielding and well-diversified, risk-managed funds in the industry. In recent years, the PLUS fund has actively sought opportunities for higher yield while simultaneously improving diversification of assets and mitigating issuer risk. This has been accomplished by investing in a variety of investment products designed to maximize returns to investors while maintaining a stable value. Recent focus groups with PLUS Fund investors confirmed that the use of diversification and sophisticated risk management to achieve greater return is meeting their objectives.

Finally, as evidenced here, ICMA-RC offers a level of transparency to investors that is uncommon in the defined contribution stable value industry.

With decades of experience, ICMA-RC's record stands on its own.

INVESTORS CAN INVEST WITH THE CONFIDENCE THAT INVESTMENT PROFESSIONALS AND INSURERS HAVE INVESTORS' ULTIMATE GOAL IN MIND – BUILDING RETIREMENT SECURITY.

Stable Value: What are the components?

Stable value funds invest in insured products known as guaranteed investment contracts, or “GICs”. The two primary types of GICs are described below, along with key characteristics, advantages and disadvantages.

Traditional GICs

A traditional GIC is a private contract between a plan sponsor or commingled fund and an insurance company that pays a specified rate of return for a specific period of time. The guarantee applies to the interest rate, principal repayment, and the payment schedule. GIC owners are considered policyholders of the issuer with a senior lien over the general creditors of the insurer. Therefore, a traditional GIC is a privately placed super-senior promissory note.

ADVANTAGES

A primary advantage of GICs is the stability of returns provided. Traditionally, the industry has valued and recorded these instruments at book value (principal plus accrued interest), instead of market value. When using “book value” accounting, the price return of a traditional GIC is always zero. As market interest rates rise and fall, GIC book values will remain constant. The only source of return to investors is the contract’s stated yield payout rate.

Another advantage is that, historically, GIC yields have been much higher than yields offered by money market instruments, but with the same level of capital preservation. The higher yields of GICs can be explained by their longer maturities (usually 2-5 years).

DISADVANTAGES

A primary disadvantage of traditional GICs, like insurance company general accounts, is issuer-specific credit risk. These contracts are issued through an insurance company’s general account and are liabilities of the issuer. The general account is a primary part of an insurance company’s balance sheet containing the portfolio of unpledged assets that backs its guaranteed products. In the event of an insurance company default liquidation, a GIC contract holder has to stand in line with other policyholders for repayment of obligations, and assets may not be sufficient to meet all liabilities.

Another traditional GIC shortcoming is the lack of liquidity resulting from the absence of a secondary GIC trading market. The contract holder may realize liquidity from a GIC only through a sale or early termination (discontinuance) as allowed for in the contract, frequently with a penalty. The liquidity problem exacerbates the credit risk exposure by preventing the sale or transfer of GICs as the creditworthiness of the issuer deteriorates.

GICs also lack transparency, like insurance company general accounts. There is not a separate identification of general account assets for any particular liability, and there is no disclosure of the general account’s underlying assets. GIC investors do not own the assets purchased with the proceeds of their individual GICs, provide no input on the manner in which the assets are managed, and receive no disclosure of what securities the portfolio contains.

For investors, these disadvantages are mitigated by ICMA-RC’s rigorous internal due diligence process.

Synthetic GICs

Synthetic GICs were developed in the early 1990’s as the insurance industry’s answer to client and adviser concerns following the S&L scandals, the bankruptcy of Executive Life, and other credit quality concerns. They are constructed to mitigate the disadvantages of traditional GICs. Issuer risk, liquidity, and transparency are all improved through use of a synthetic GIC.

Simply put, a thoughtfully structured synthetic GIC is comprised of two distinct parts: a bond portfolio and an insurance policy (wrap contract). Each of these pieces offers their own unique and important benefits to investors.

BOND PORTFOLIO

The fund adviser establishes a bond portfolio, managed either in house or through a subadviser. The portfolio strategy and objectives are determined by the fund's adviser. Ownership and control over the investment of the fund's assets is a key benefit compared to traditional GICs.

Given the dynamic nature of the investment business, another key benefit is management flexibility. For example, single or multiple (sub)advisers may be retained and replaced as needed depending on strategies employed and changing market or business conditions.

Hand in hand with the opportunity to control the investment process comes the opportunity to control risks. Formal investment management policies at the portfolio level dictate acceptable types and levels of risk that the adviser can take in managing the portfolio. Importantly, the issuer of the insurance policy (wrap contract) considers these investment guidelines very carefully as it completes its risk assessment and determines the insurance cost. If and when changes are made to the guidelines, the policy issuer has the right to approve or disapprove, adding a level of protection for fund shareholders.

INSURANCE POLICY (WRAP CONTRACT)

The fund adviser also purchases on behalf of the fund at least one, preferably more, insurance policies and wrap contracts (referenced above). These special policies, called wrap contracts, insure the bond portfolio against market value fluctuation. Simply put, if the price of the bond portfolio falls, the wrap contracts would pay the fund the difference between book value (the amount originally invested) and the current market value of the bond portfolio in the event of liquidation. This is what allows the synthetic bond portfolio to keep a stable value.

Wrap contract issuers are selected by the fund adviser based on a variety of factors. A key consideration is the credit quality of the issuer, since the book value guarantee that the policy provides is only as good as the credit worthiness of the issuer(s), as with any insurance policy. Experience as a wrap contract issuer is also important, as the management of the synthetic GIC is a partnership of sorts, with both the adviser and the insurance issuers working together to seek to achieve the very important feature – capital preservation.

By separating the two necessary functions of asset management (providing yield) and book value accounting (capital preservation), held by one insurance company under a traditional GIC structure, synthetic GICs reduce issuer risk.

Synthetic GICs: The crediting rate

The yield paid to investors from the synthetic GIC (or “wrapped”) portion of the PLUS Fund is determined by a crediting rate.

The monthly crediting rate is determined by (1) amortizing (spreading out) market gains or losses, determined monthly, and (2) factoring in current portfolio yield. This industry protocol seeks to smooth the impact of market value changes and factors in current yield.

This rate is reset at predetermined intervals, typically monthly or quarterly. The crediting rate methodology minimizes the impact of price changes of the underlying holdings, and recognizes yield as the most important factor in the current rate.

While the crediting rate will lag market rates in both directions, it acts to smooth out volatility. This volatility-neutralizing effect addresses participants' desire for stability of value and returns.

If, like the VantageTrust PLUS Fund, a fund holds traditional GICs in addition to synthetics, the crediting rate is calculated for the synthetic GIC portion of the fund only. At the fund level, the overall portfolio rate (blended rate) is established by combining, on a pro rata basis, the synthetic crediting rate, the weighted average of GIC yields and the average yield of the liquidity pool.

About ICMA-RC

ICMA Retirement Corporation (ICMA-RC) is a not-for-profit, leading provider of retirement investment services for public sector employees. Founded in 1972, the corporation manages and administers \$23 billion in retirement plan assets for more than 650,000 public sector participants as of July 31, 2005.

The firm offers innovative products and services to assist public sector employees build secure retirements.

Based in Washington, DC, with 550 employees, the corporation maintains field offices across the United States staffed by NASD-registered professionals.



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