



Callan GlidePath® Target Maturity Fund Series

THE CALLAN GLIDEPATH® FUNDS

Diversified Portfolios for a Secure Retirement

Callan Associates



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Participation in the collective trusts is governed by the terms of the trust and participation materials. An investor should carefully consider the investment objectives, risks, and charges and expenses of the collective trusts before investing. The participation materials contain this and other important information and should be read carefully before investing or sending money. Participation materials are available from Wilmington Trust Company, Callan Associates Inc., and your plan provider.

About Wilmington Trust Company

Wilmington Trust Corporation is a publicly held banking institution listed on the NYSE (WL). Wilmington Trust Company, which is part of the Wilmington Trust corporate family, is a Delaware State chartered trust company with operations in Wilmington, DE and Phoenix, AZ. The company provides directed trustee, trust administration and back-office services for their clients' clients: retirement plans, companies, foundations, organizations and financial institutions. They work exclusively with TPAs, consultants, and professional advisors, assisting them in helping their clients achieve their financial goals by using the full range of trust strategies available under Delaware law. Wilmington Trust Company is one of the largest independent trust companies in the U.S. and administers over \$21 billion in trust assets. For more information please visit www.wilmingtontrust.com.

About Callan Associates

Founded in 1973, Callan Associates Inc. is one of the country's largest independently-owned investment consulting firms. Headquartered in San Francisco, with offices across the country, the firm provides research, education, decision support, and advice to over 300 institutional fund sponsors, representing over \$1 trillion in total assets. Clients include corporate and government defined benefit plans, defined contribution plans, as well as foundations, endowments, operating funds, and other large pools of institutional capital. Callan's Trust Advisory Group is a division of the firm that specializes in building and managing discretionary multi-manager portfolios for institutional investors. The Trust Advisory Group is responsible for the management of the Callan GlidePath® Funds.

The Callan GlidePath® Funds are a series of diversified investment funds known as “Target Maturity” funds. They are designed to be a “single-investment” solution for participants of defined contribution plans. By automatically adjusting their asset allocation to become more conservative over time, these funds are designed to achieve the appropriate level of risk for each stage of a participant’s life, from their first days on the job, through their principal wealth-building years, and on into retirement.

THIS ARTICLE AND ANY OTHER INFORMATION THAT MAY BE FURNISHED TO PROSPECTIVE INVESTORS REGARDING THE GLIDEPATH FUNDS, MAY CONTAIN FORWARD-LOOKING STATEMENTS WITHIN THE MEANING OF THE FEDERAL SECURITIES LAWS. FORWARD-LOOKING STATEMENTS ARE THOSE THAT PREDICT OR DESCRIBE FUTURE EVENTS OR TRENDS AND THAT DO NOT RELATE SOLELY TO HISTORICAL MATTERS. FOR EXAMPLE, FORWARD-LOOKING STATEMENTS MAY PREDICT FUTURE ECONOMIC PERFORMANCE, DESCRIBE PLANS AND OBJECTIVES OF THE TRUSTEE OR THE ADVISOR FOR FUTURE OPERATIONS AND MAKE PROJECTIONS OF REVENUE, INVESTMENT RETURNS OR OTHER FINANCIAL ITEMS. A PROSPECTIVE INVESTOR CAN GENERALLY IDENTIFY FORWARD-LOOKING STATEMENTS AS STATEMENTS CONTAINING THE WORDS “WILL,” “BELIEVE,” “EXPECT,” “ANTICIPATE,” “INTEND,” “SEEK TO,” “CONTEMPLATE,” “ESTIMATE,” “ASSUME” OR OTHER SIMILAR EXPRESSIONS. SUCH FORWARD-LOOKING STATEMENTS ARE INHERENTLY UNCERTAIN, BECAUSE THE MATTERS THEY DESCRIBE ARE SUBJECT TO KNOWN (AND UNKNOWN) RISKS, UNCERTAINTIES AND OTHER UNPREDICTABLE FACTORS, MANY OF WHICH ARE BEYOND THE CONTROL OF THE TRUSTEE AND THE ADVISOR. NO REPRESENTATIONS OR WARRANTIES ARE MADE AS TO THE ACCURACY OF SUCH FORWARD-LOOKING STATEMENTS.

The Callan GlidePath® Funds

Diversified Portfolios for a Secure Retirement

The Callan GlidePath® Target Maturity Fund series was designed with the goal of bringing established practices employed by the world's largest defined benefit plans, to the individual retirement accounts of participants in defined contribution plans. To achieve this, the fund series was constructed with four primary objectives:

- ▶ Provide investors with efficient, diversified exposure to the key asset classes employed by large retirement plans;
- ▶ Automatically adjust the asset allocation of each fund to achieve an appropriate level of risk for each stage of a participant's life;
- ▶ Build a high caliber team of institutional portfolio managers with a diverse set of views, and a broad range of perspectives on the markets;
- ▶ Focus on fees and costs, employing a sensible blend of active and passive strategies, while working to keep fund expenses as low as possible.

As one of the largest investment consultants in the country, Callan Associates is uniquely qualified to build a series of funds that meet these objectives. The firm has been a leader in the field of asset allocation for over 30 years, pioneering the use of many of the tools that have become industry standards today. With over \$1 trillion in client assets, Callan has the knowledge, the scale, and the leverage to identify and hire institutional quality investment managers, and to combine them into cost-effective portfolios optimized for each stage of a participant's life.

Asset Allocation Design – The Glidepath

Target maturity funds are designed to serve the investment needs of defined contribution participants from the start of their career, through their wealth-building years, and on into retirement. By employing an increasingly conservative asset allocation over time, these funds provide participants with greater exposure to equity securities early in their career, and gradually move toward lower risk investments as they approach retirement. The exact route that this increasingly conservative asset allocation takes over time is commonly referred to as the fund's "glidepath."

The glidepath for the Callan series of target maturity funds was developed over a two-year period using a proprietary asset allocation model. The model was designed to simulate the behavior of a wide range of

glidepath strategies across literally thousands of different potential capital market outcomes. The model was built, and is maintained by Callan's Capital Markets Group, a team of economists, financial analysts, and actuaries that specialize in asset allocation analysis for large institutional investors. This team of analysts used the model to simulate hundreds of different glidepaths, searching for the path that best balanced the trade-offs between risk and return over a participant's lifetime. The ultimate goal of the analysis was to identify the glidepath with the highest probability of providing a secure retirement for participants who save adequately throughout their career, and use the appropriate fund (given their projected retirement date) as their primary retirement savings vehicle.

The word "glidepath" originated in the airline industry. It refers to the flight path of a plane as it descends toward a safe landing.

How Do They Work?

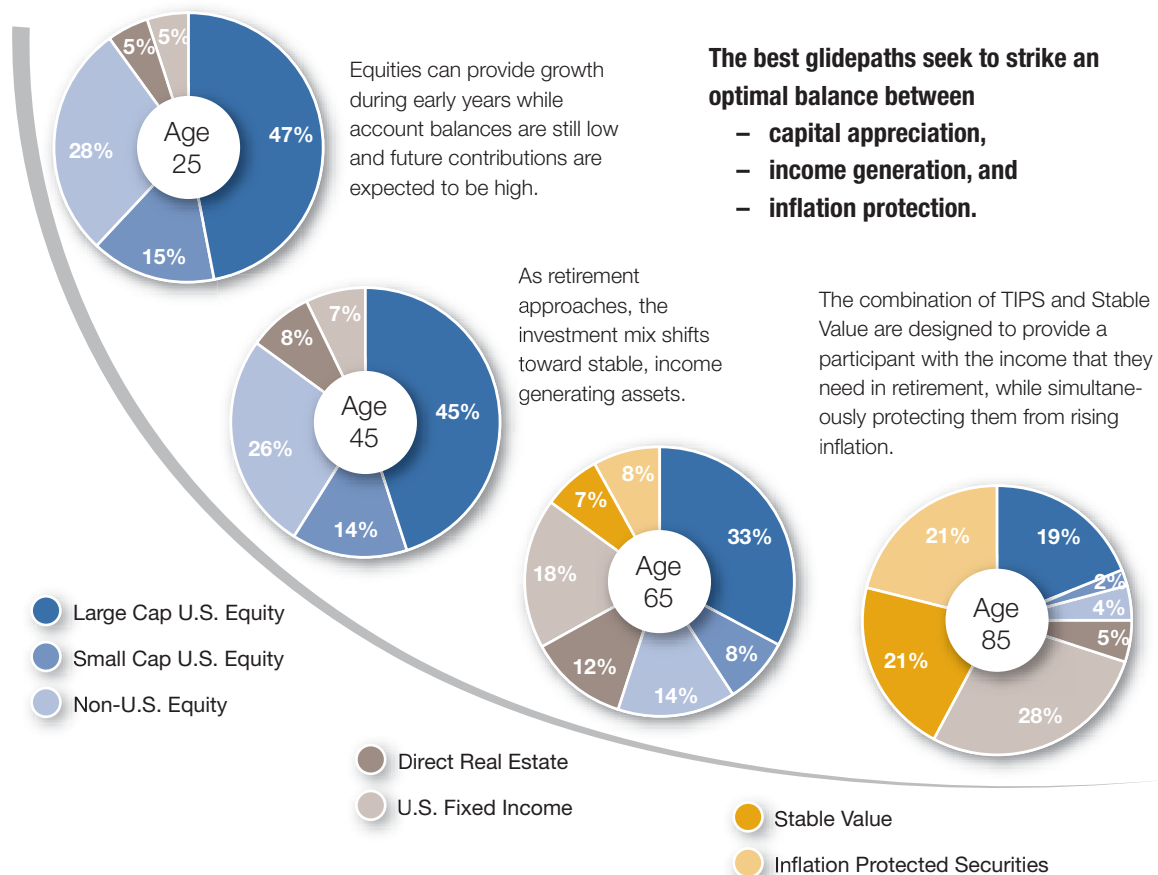
Target maturity funds are designed to be a simple "one-fund" retirement savings solution for participants of defined contribution plans. The funds are issued in five-year intervals, with each fund targeting a specific retirement date. The Callan GlidePath® 2040 Fund, for example, is designed for participants who plan to retire within five years of 2040. This Fund is invested in a diversified portfolio, with an asset allocation that is automatically adjusted each year to achieve the appropriate risk and return for each stage of a participant's life.

In evaluating the merits of all of the possible glidepaths, Callan's analysts focused on three key variables to identify the optimal path. The first variable, known as the "Income Replacement Ratio," measured the probability that a participant who saves appropriately throughout their career will achieve a targeted level of income replacement at retirement. The model searched for glidepaths that had the highest probability of generating retirement income in excess of 75% of a participant's final average pay. Industry studies indicate that this is an

appropriately targeted income level, particularly when combined with Social Security and Medicare benefits. Conservative paths, or paths that scaled back the equity exposure too soon, tended to score poorly in this dimension.

The second important variable measured the size of a "worst-case" investment loss during a participant's retirement eligibility period. Research indicates that participants are particularly sensitive to investment volatility in the years immediately pre-

Asset Allocation Over a Participant's Life



ceding their retirement date. Significant declines during this period can cause participants to abandon a long-term investment plan. This consideration must be balanced by the fact that capital appreciation is still critical during these important wealth-building years. Glidepaths that allocated up to 15% of the portfolio to direct real estate during these years achieved what Callan believes to be the most favorable balance between capital appreciation, income generation, and inflation protection.

The last key variable measured the probability that a participant will outlive their assets after retirement. As with the Income Replacement Ratio, this variable favored paths that did not start out too conservatively, and did not scale back the equity exposure too quickly. Given the fact that the typical life expectancy of a participant entering retirement at age 65 is 18 years, capital appreciation is still an important consideration even during retirement. A path that maintained at least a 50% equity allocation at retirement, and then

became increasingly focused on inflation protection after retirement produced the best result in this dimension.

Of the hundreds of paths that were considered in the simulation analysis, the glidepath that was ultimately chosen for the Callan GlidePath® Funds offered what Callan believes to be the optimal balance of all of these factors. The Funds employ a high equity allocation in the early years of a participant's career, when capital appreciation is critical, account balances are low, and future contributions are expected to be high. As retirement approaches, the equity allocation is gradually reduced, with a corresponding increase in the allocations to direct real estate and fixed income. Finally, as a participant enters into retirement, the funds shift further out of equities and into inflation protected securities and short-term fixed income (stable value). This constantly evolving asset allocation allows the Callan GlidePath® Funds to automatically adjust the level of risk and return for every stage of a participant's life.

The optimal glidepath will target an income replacement ratio of at least 75% of final average pay for the participants who save diligently throughout their career.

Diversification – The Key to Risk Control

One of the great advantages enjoyed by large defined benefit plans is the ability to invest across a complete range of asset classes and investment styles. This flexibility, afforded to them by their size, their tax-exempt status, and their legal structure, allows them to target the highest possible return for their chosen level of risk.

The GlidePath® Funds are designed to provide a level of diversification similar to that of large defined benefit plans.

The Callan GlidePath® Funds seek to provide this same level of diversification to participants in defined contribution plans. By taking advantage of their collective fund legal structure, the Funds seek to provide cost-effective access to asset classes that have traditionally been either too expensive or entirely outside the reach of defined contribution participants. By using asset classes like direct real estate, small cap equity, inflation protected securities, and stable value, the Funds attempt to achieve a level of diversification and risk-control that is competitive with that of even the largest defined benefit plans.

Investments in direct real estate funds have long been a cornerstone of the asset allocation policies employed by large defined benefit plans. Direct real estate funds have provided diversification and a stable source of income, which has significantly offset the volatility of a traditional stock and bond portfolio. Unfortunately, for a variety of operational reasons, direct real estate funds have traditionally been outside the reach of

Asset Categories Used in GlidePath® Funds

U.S. Large Cap Equity – Stocks issued by the largest U.S. companies.

Benchmark: Russell 1000® Index.

U.S. Small Cap Equity – Stocks issued by smaller U.S. companies (typically less than \$2 billion in market capitalization).

Benchmark: Russell 2000® Index.

Non-U.S. Equity – Stocks issued by companies outside the U.S. Includes both developed markets and emerging markets.

Benchmark: MSCI All Country World Ex-U.S.® Index.

Direct Real Estate – Diversified portfolio of direct investments in commercial properties, accessed through a collective fund legal structure.

Benchmark: NCREIF Property® Index.

U.S. Fixed Income – Intermediate to long-term bonds issued predominately by the U.S. based companies, and the U.S. Treasury.

Benchmark: Lehman Aggregate® Index.

Treasury Inflation Protected Securities (TIPS) – Intermediate to long bonds indexed to the rate of inflation.

Benchmark: Lehman U.S. TIPS® Index.

Stable Value – Portfolio of short to intermediate term bonds, protected against a decline in principal through the use of insurance contracts.

Benchmark: 90-Day Treasury Bills.

defined contribution participants. As a substitute, many target maturity funds have used mutual funds that invest in REITs (Real Estate Investment Trusts) to gain a measure of real estate exposure. REITs are publicly traded stocks issued by companies that own and manage real property portfolios. In practice, REITs have traded and behaved more like small cap equity securities than like an investment in a direct real estate fund. This means that they have exhibited significantly greater price volatility, and have generally delivered a lower level of current income than direct real estate funds. REIT mutual funds also tend to have higher total embedded costs than the typical direct real estate fund. The net result is that funds that invest in REITs have generally been an expensive and relatively ineffective diversifier when added to a traditional stock and bond portfolio.

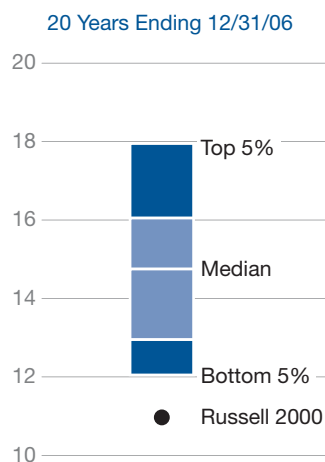
Rather than using the traditional REIT approach, the Callan GlidePath® Funds are among the first target maturity funds in the industry to invest in a direct real estate fund. Prudential Real Estate Investors (PREI®), one of the largest and most respected real estate advisory firms in the world, has recently introduced a direct real estate fund designed specifically for large defined contribution plans. The Prudential Retirement Real Estate (PRRE®) fund incorporates daily valuation and daily liquidity features into its design to allow defined contribution participants to invest in real estate side-by-side with some of

the largest defined benefit plans in the country. The PRRE® fund invests directly into a diversified mix of commercial properties, providing participants with exposure to a wide range of real estate markets, property types, and investment strategies. By investing in this powerful diversifier throughout a participant's career, the Callan GlidePath® Funds seek to achieve a level of risk-control that would be impossible using the traditional REIT approach to real estate investing.

One of the benefits created by the diversifying influence of a direct real estate fund is the ability to allocate a greater percentage of each Fund's equity portfolio to small cap stocks in the early years of a

A direct real estate fund can provide powerful diversification benefits when combined with a traditional stock and bond portfolio.

Returns for Active Small Cap Managers versus Russell 2000 Index



There are 102 actively managed small cap products in Callan's Small Cap database with a 20-year performance history. Of those, 95 have outpaced the Russell 2000 over the last 20 years. In no other asset class do active managers come close to this record.

Historically, active managers of U.S. small cap equity portfolios have been more successful in beating their benchmarks than active managers in any other asset class.

The combination of Treasury Inflation Protected Securities (TIPS) and a Stable Value portfolio provides yield and inflation protection for participants in their retirement years.

participant's career. Small cap stocks are securities issued by the smallest 20% of companies traded on U.S. exchanges. These companies tend to have higher growth rates than their larger counterparts and, as a result, have generated higher returns over the long run. They also have tended to exhibit greater volatility over the short run. This has created opportunities for portfolio managers to generate additional return (or alpha) by exploiting temporary mispricings. The use of a direct real estate fund in lieu of REITs can dampen the impact of this short-term volatility, allowing for a higher allocation to this important asset class during years where capital appreciation is critical to the success of a retirement savings plan.

In later years, as participants enter retirement, the Callan GlidePath® Funds respond to the need for inflation protection by gradually building up an allocation to Treasury Inflation Protected Securities (TIPS), and to a Stable Value portfolio. TIPS are fixed-income securities issued by the U.S. Treasury with yields that are indexed to the rate of inflation. In periods of high inflation, the higher yields on these securities provide participants with protection against an inflation-related decline

in the purchasing power of their retirement savings. Stable Value portfolios provide similar protection by combining a short to intermediate-term fixed-income portfolio and a specially designed insurance policy. The fixed-income portfolio provides higher yields than would be available from a money market account, while the insurance policy provides protection from any decline in principal value due to interest rate volatility. The combination of TIPS and Stable Value is designed to provide participants with a "belt-and-suspenders" approach to generating the income that they need in retirement, while simultaneously protecting them from rising inflation.

By providing cost-effective exposure to a complete spectrum of diversifying asset classes at the appropriate times, the Callan GlidePath® Funds are designed to deliver a level of risk-management that is on par with that employed by the largest defined benefit plans. This helps to ensure that the funds can target the appropriate trade-off between risk and return at each stage of a participant's life, from the beginning of their career, through their primary wealth-building years, and on into retirement.

Open-Architecture – Combining a Diverse Set of Perspectives

Industry best practices for large defined benefit plans have long dictated the use of an “open-architecture” approach when selecting advisors to

The Callan GlidePath® Funds employ a total of nine separate investment advisory firms, each providing a distinct perspective on the markets.

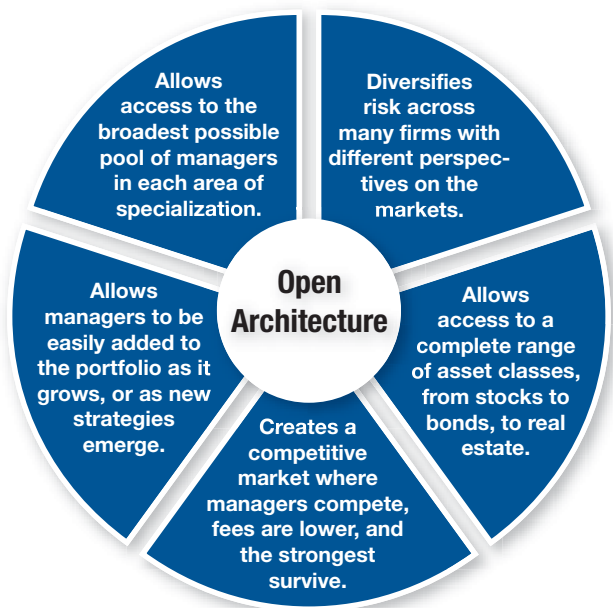
manage the overall portfolio. This means that a plan will typically hire a diverse group of advisors, attempting to select the strongest available candidates within each area of specialization. This is in contrast to a “closed-architecture” approach where a plan might entrust the entire portfolio to a single advisory firm that manages everything from large cap equities, to real estate, to short-term fixed income.

The reason that the open-architecture approach has prevailed in the large plan market is because it has a number of significant advantages for plans with the scale and infrastructure to properly implement it. First, it allows a plan sponsor to select from a much wider opportunity set of advisors and strategies, opening up a world of highly specialized “boutique” firms that may only manage one asset class or style. Second, it allows the sponsor to diversify the business risk associated with consolidating all of the assets with a single firm. Third, it allows the plan to access a complete range of asset classes and investment styles, providing a diverse set of perspectives on the markets and potentially

lowering the risk of the overall portfolio. Finally, the open-architecture approach creates a competitive environment for the advisors where only the strongest survive, and where fees remain reasonable.

The Callan GlidePath® Fund series is one of the first target maturity series to employ a truly open-architecture approach. The Funds are managed by a total of nine different investment advisory firms, each with their own area of specialization. Active managers are employed in the less efficient areas of the market where historically they have delivered the most consistent

The Advantages of an Open-Architecture over a Single-Manager Approach



An open-architecture approach seeks to diversify risk, foster healthy competition, and ultimately deliver the highest quality portfolio management at the lowest fee structure.

excess returns over their benchmarks. Passive managers are employed in the more efficient asset classes, reducing the overall expense ratios of the portfolios.

This structure is designed to diversify the business risk of the Funds, reduce the exposure to any single firm, and allow the Funds to take advantage of the specialized strengths of each advisor. It is also designed to provide the Funds with a measure of flexibility that may not be avail-

able in a closed-architecture framework. As the Funds grow, for example, some of the advisors may reach their capacity limits and have to close their portfolios to new in-flows. In that case, new firms can be added in any area of specialization to maintain the overall asset allocation of the Funds. Similarly, if an advisor experiences problems that in Callan's judgment might lead to under-performance, they can be replaced with a more suitable candidate.

Manager Selection – A Rigorous and Time-Tested Process

Having a strategic plan, or “blueprint,” for the design of each asset class is one of the keys to building a successful investment program.

In a typical year Callan Associates will conduct between 150 and 200 individual manager search projects on behalf of its large institutional clients. Over the past five years this has resulted in the placement of over \$25 billion with qualified advisors across a wide variety of asset classes and investment styles. In selecting these advisors, Callan employs a rigorous process that has been developed and continually refined by working with large institutional investors over the last three

decades. This same process is used in selecting advisors for the Callan GlidePath® Fund series.

The process begins with the development of a strategic plan, or “blueprint,” that describes the portfolio design for each asset class. This plan addresses considerations such as the number of advisors to be employed; the use of active versus passive management; the style orientation of the advisors; as well as the desired lev-

els of risk, return, and correlation that the portfolios should exhibit over time. Using this blueprint as a guide, Callan professionals then develop a set of criteria that describe the ideal advisors for each assignment within the portfolio. These criteria form the basis for the manager selection process that then follows.

The specific criteria for each assignment will vary considerably by asset class and investment style. There are, however, a number of fundamental considerations that are taken into account in every search that Callan conducts. These include:

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- ▶ **A thorough analysis of the historical track record for each strategy**, focusing on absolute return, relative return (versus both indices and peer groups), risk-adjusted return, and correlation;
 - ▶ **A holdings-based analysis of the portfolio**, looking at portfolio concentration, annual turn-over, sector weights, and a broad array of portfolio characteristics which provide insight into the character and consistency of each advisor's investment style;
 - ▶ **A qualitative evaluation of the advisor's organizational structure**, including their people, process, back-office and compliance resources, business model, compensation structure, and ownership structure;
 - ▶ **An assessment of the advisor's capacity to take on additional assets in the strategy** without undermining its prospects for future success.

Every advisor that is selected to manage a component of the Callan GlidePath® Funds is evaluated from each of these four perspectives. Experienced professionals from Callan's Global Manager Research Group comb through the entire universe of institutional advisors to produce a short list of firms that they feel are best suited for each assignment. This list, and a corresponding due-diligence report on each prospective

advisor, is carefully evaluated by the GlidePath® Funds Investment Committee. The Committee then makes the final selection for each assignment. By carefully balancing all of these important considerations, Callan's objective is to build a team of "best-in-class" advisors for each asset class that, when used in combination, create a portfolio that is designed to be greater than the sum of its parts.

Callan's objective is to build a team of "best-in-class" advisors that, when used in combination, are designed to create a portfolio that is greater than the sum of its parts.

Putting It All Together – The Callan GlidePath® Mission

The success of a retirement savings plan is guided by a simple immutable law, “dollars in, compounded by investment return, equals dollars out.”

Over the last two decades there has been a dramatic shift in the way that America saves for retirement. With the general decline in the number of corporate sponsored defined benefit plans, an increasing percentage of the country’s workers have come to rely on defined contribution plans as their primary retirement savings vehicle. This change represents a massive and unprecedented transfer of investment risk, moving retirement liabilities off of America’s corporate balance sheets, and into the accounts of the individual participants in DC plans. While we will not know the societal implications of this change for years to come, we do know that the success of this new savings system will be determined by the same fundamental law that determines the success of any defined benefit plan. That is, “Dollars in, compounded by investment return, equals dollars out.”

Under a defined benefit plan, corporate sponsors are required by law to set aside an adequate amount of money every year on behalf of each participant. They are also responsible for ensuring that their plan assets are well diversified and earn a competitive rate-of-return at an appropriate level of risk. In defined contribution plans the responsibility for saving lies with the participant, who must make consistent contributions throughout their career. It is the mission of the Callan GlidePath® Funds to uphold the investment half of the bargain. By employing well established practices of diversification and risk-management, by hiring what Callan believes to be the strongest possible team of advisors at the lowest possible cost, and by constantly adjusting the asset allocation over a participant’s career, the Callan GlidePath® Funds seek to provide participants with a single-choice retirement solution that is competitive with the portfolios of the world’s largest institutional investors.

Author



Gregory C. Allen, President and Director of Research. As President, Greg is responsible for overseeing Callan's Fund Sponsor Consulting Group, the Trust Advisory Group and all of the firm's research groups which include: Global Manager Research, Alternative Investment Research, Capital Market Research and Published Research. Additionally, he has oversight for Callan's Database Group, Client Report Services, Operations and Corporate Communications. Greg is also a member of Callan's Management Committee, the Alternatives Review Committee, and the Client Policy Review Committee. He is also a member of the Investment Committee which has oversight responsibility for all of Callan's discretionary multi-manager solutions.

Greg joined the San Francisco Office of Callan Associates in 1988 as an analyst in the Capital Markets Research Group where he focused on capital market research, quantitative analysis, product development, and asset allocation liability analysis. In 1993, Greg took over the Operations and Capital Markets Research groups. He has managed a wide variety of projects for Callan, including the development of the firm's performance measurement service, the development of Callan's web site and web-based performance reporting capabilities, and the development and launch of Callan's *PEP for Windows™* software. In 2000, Greg was promoted to Manager of Specialty Consulting (Now Director of Research) and in 2007 was promoted to President. Greg is a shareholder with the firm.

Greg earned an M.S. in Applied Economics and a B.A. in Economics (Honors, Phi Beta Kappa) from the University of California at Santa Cruz. He is a frequent speaker on investment related topics, and has numerous publications. These include "Performance Attribution for Global Portfolios" published in the Fall 1991 issue of the *Journal of Portfolio Management*, "The Active Premium in Small-Cap U.S. Equities" published in the Spring 2005 issue of the *Journal of Portfolio Management*, and "Does Size Matter?" published in the Spring 2007 issue of the *Journal of Portfolio Management*.

Callan Associates

Corporate Headquarters

101 California Street
Suite 3500
San Francisco, CA 94111
1.800.227.3288
1.415.974.5060

Regional Consulting Offices

Atlanta

300 Galleria Parkway
Suite 950
Atlanta, GA 30339
1.800.522.9782
1.770.618.2140

Chicago

120 N. LaSalle Street
Suite 2100
Chicago, IL 60602
1.800.999.3536
1.312.346.3536

Denver

1660 Wynkoop Street
Suite 950
Denver, CO 80202
1.303.861.1900

New Jersey

200 Park Avenue
Suite 230
Florham Park, NJ 07932
1.800.274.5878
1.973.593.8050

www.callan.com

