

PLAN UPDATE



FIXED-INCOME INVESTING WITH OSGP

As an OSGP participant you can select from nine investment options ranging from conservative to aggressive risk levels. The OSGP investment lineup gives you broad diversification across many asset classes and within each option. Since you may invest in one option or up to all nine, you can allocate your contributions according to your individual financial goals, your individual risk tolerance, and your individual time horizon.

To diversify your portfolio and make an appropriate asset allocation, the OSGP investment array includes fixed-income options:

- **Short-Term Fixed Option** – This option invests in short-term money market securities, including debt instruments such as U.S. Treasury and government agency notes. Yields on these securities follow short-term interest rate cycles. The performance benchmark for this option is the 91-day Treasury bill, a common industry barometer for government security money market funds. This benchmark provides a good comparison of average maturity and credit risk for the investment portfolio.
- **Stable Value Option** – This option invests primarily in a diversified portfolio of fixed-income investments and agreements that support capital preservation and liquidity. The investments include, but are not limited to, contracts with life insurance companies, deposit agreements with banks, obligations of the U.S. government or its agencies, asset-backed securities, and other high quality fixed-income securities. The fixed-income investments will, in each case, represent an issuer's promise to repay principal plus a rate of interest. Performance benchmarks are not available because of the unique nature of the option's various holdings.
- **Intermediate-Term Fixed Income Option** – This option invests mostly in intermediate-term bonds with maturities ranging from three to ten years. A majority of the bonds are investment quality as rated by one or more of the major rating agencies or, if not rated, judged by the managers to be of comparable quality. The performance benchmark for this option is the Lehman Brothers Aggregate Bond Index, used for good quality bonds.

More About Bonds

A bond represents a promise on its issuer's behalf to pay back the amount invested, essentially a loan, with interest. Bonds are called "fixed-income" investments because both the length of time it takes for a particular bond to mature and its interest rate are unchanging or "fixed." The amount earned on a bond, based on the price paid for the bond, is called "yield." The overall earnings in a bond fund, however, do fluctuate and can, at times, become negative.

Risks of Investing in Bonds

Bonds are potentially lower in market risk than stocks because of the promise of returned principal at maturity. Over the long term, however, they have had lower returns than stocks. The price of bonds is generally straightforward: when interest rates go down, bond prices go up; and when interest rates go up, bond prices go down.

For example, when interest rates go down, the value of a bond increases, because the bond is paying a premium over the rates offered by new bonds. Investors typically are willing to pay more than face value for the bond to get extra income from the higher interest rate. The bond is now considered to be trading at a **premium**. Consider an investor who buys several bonds for \$1,000. The bonds pay a fixed interest rate of 6 percent or \$60 a year. If interest rates drop, the bonds are now more valuable because no one can buy new bonds at 6 percent any longer.

When market interest rates go up, however, the bond whose interest rate is fixed is now earning less than market value. Investors would take this below-market rate into consideration and only be willing to pay less than face value for the bond. The bond is now trading at a **discount**. The 6 percent bonds are now less valuable because investors can do better than 6 percent by buying new bonds. If the rate is 8 percent, for example, sellers may be forced to sell at a discount to attract potential buyers. This explains why bond funds have negative returns under certain market conditions.

The term of the bond, its time to maturity, and the creditworthiness of its issuer can also affect its value.

(continued on reverse side)

An Important Part of Your Portfolio

Fixed investments can be appealing at times of stock market volatility and are a key part of the portfolios of investors with certain risk profiles and/or time horizons. While these investments may not have the potential for return of sometimes high-flying stocks, they play an important role in a well-managed retirement or long-term savings portfolio because they tend to have a more predictable income stream than stocks.

Investors with longer time horizons and a higher tolerance for risk need to consider carefully the tradeoff they make on the potential for reward when they move to fixed instruments in the short term. Research shows that those who attempt to "time the market" do less well in the long term than those who carefully select a diversified balance of investments that relates to their personal risk profiles and years to retirement.

INVESTMENT OPTION ALLOCATION CHANGES

The Oregon Investment Council (OIC) monitors the underlying investments within each of the nine options in the OSGP. As a result of its annual review of OSGP investments, the OIC made minor adjustments to specific options, effective December 31, 2002. These adjustments are designed to support the goal in each option of meeting or exceeding the performance of its benchmark.

The council approved a change in the weightings of the funds within the Intermediate-Term Fixed Income Option. Assets in the Wellington, Fidelity and Barclays Global Investors (BGI) funds will be weighted at 33.3 percent each.

In the International Option, the OIC approved closure of the BGI Morgan Stanley Capital International Europe Asia Far East (MSCI EAFE) Index fund and a reallocation of assets among the three remaining funds with Artisan, Oakmark and Grantham, Mayo, Van Otterloo (GMO) weighted at 33.3 percent each.

Participants need take no action since the underlying funds are selected and reviewed by the OIC.

ADVISORY CORNER

Learn and Serve

Oregon state law provides for a deferred compensation advisory committee. The committee gives information and advice to the Public Employees Retirement System Board and has seven members selected by the Board to reflect a cross section of participant groups. The key role of the advisory committee can best be described as participant representation. It provides a forum for feedback and an opportunity for interaction. This committee typically meets four times yearly.

There is a single vacancy on this seven-member body. This position is open to any participant employed by one of our nearly 100 local government plan sponsors. We invite

employees interested in filling this vacancy to send a letter of interest along with a brief resume to our Salem office at 800 Summer St. NE, Suite 200, Salem, OR 97301. Applications will be accepted until May 30, 2003. We look forward to hearing from you.

PERS PENSION AND OSGP

You can simplify the management of your retirement accounts and reduce costs by rolling your tax-deferred accounts into the OSGP. Tax laws allow OSGP participants to roll retirement assets from 401(k), 403(b) and IRAs into the OSGP. PERS-covered employees may select the Lump-Sum or Total Lump-Sum Option at retirement and roll most or all of their benefit into the OSGP. Police and fire classification employees who are participating in the "units" program may be eligible to roll excess units as well. If you would like more information, call 503-378-3730.

SURVEY RESULTS

We are pleased to report that 855 customer service surveys were returned representing the opinions of a balanced cross section of participants. Generally, the news was very good. In all categories of service, between 85 and 90 percent of respondents were satisfied or very satisfied. More than half of all plan participants have attended one or more of our free seminars; 99 percent of the attendees found the seminars useful or very valuable. In addition, 65 percent find account access on the Internet valuable and 87 percent appreciate continued account access by telephone.

As we continue to evaluate existing services and service extensions, we will use your responses to focus and guide our efforts. Thank you for your time and the candid feedback.

MORE INFORMATION MORE QUICKLY

This summer OSGP will introduce enhancements to the way you access your account information. You will be able to navigate all of the options available through the automated Customer Service Information Line with a faster touch-tone system. You will also be able to see your account statement on the online Internet site at osgp.csplans.com. With this feature, you are only a mouse click away from the most up-to-date information available, giving you more tools to make sound choices for your retirement savings.

Editorial Contributions

Deatrice Johnson, CitiStreet
Jon Springer, OSGP
David Crosley, PERS
Marsha Bacon, PERS

The foregoing newsletter is not intended to provide legal, tax, or investment advice. For such advice, participants should contact legal, tax, or investment advisers.