

AN INTRODUCTION TO INVESTING

Questions about investing?

Here are some
straightforward answers.



DIVERSIFIED INVESTMENT ADVISORS

Diversified Investment Advisors is committed to helping you save and invest wisely, and this investment guide is an example of that commitment.

On the pages that follow, you'll find information that can help you get the most out of the investment flexibility that your retirement plan offers. You'll learn more about three key topics: what investment options are available to you, how to create the right mix of investments for your situation, and how to keep your retirement plan working hard for you over time.

We hope you find this information helpful as you create or fine-tune your *Plan of a Lifetime*.

Table of Contents

Reviewing your investment choices	1
Assembling your investment mix	8
Managing your account	10

Reviewing your investment choices

Remember the old saying: "Don't put all your eggs in one basket"? That advice is especially sound when you're saving for retirement. Fortunately, your investment choices can be grouped into three main *asset classes* or categories of investments:

- *stocks* (sometimes referred to as equities)
- *bonds* (also called fixed-income investments)
- *cash* (or money markets)

Since different investments within these asset classes share common characteristics, you can learn a lot about your options by learning more about these asset classes.

Why are asset classes so important?

All investments carry some degree of risk. But risk isn't all bad. In fact, the greater an investment's risk, the greater its potential for return over the long-term. This is known as the *risk/return ratio*, and it is different for each asset class.

For example, stocks can be considered the riskiest type of investment because over the

short term, stock prices rise and fall often. But over the long term, stocks have also tended to deliver higher returns. So the more you're trying to save—and the longer you have to ride out the market's ups and downs—the more of your nest egg you may want to put in the stock "basket."

On the other hand, bonds and cash are generally considered less risky than stocks. However, the long-term returns generated by these types of investments also tend to be lower than stocks. It's always a trade-off...if you want less risk, you may need to expect lower returns—and vice versa.

Of course there's no guarantee that any asset class will outperform another, but it pays to learn about the risk and reward potential of each, so that you'll be ready to evaluate which options are best suited for your goals and your investment timeframe.



What should I know about stocks and stock funds?



When you own shares of stock, you actually own a percentage of the company issuing the stock. Since the price of stocks tends to rise and fall based on the success of the company, investors literally “share” in the company’s gains—or losses.

Researching and buying individual stocks can require a lot of time and expertise. That’s why so many investors prefer to buy into a collection of stocks—referred to as a *stock fund*.

Stock funds are managed by professional investment managers. Based on the objectives of the fund, the manager decides what—and when—to buy and sell. How well the manager’s selections perform is what determines the value of your investment in the stock fund.

Though people refer to the “stock market” as if it’s all one entity, fund managers often focus on specific

segments of the stock market. Sometimes they focus on stocks from certain size companies. They may also scour the market looking for stocks that have similar characteristics. In fact, stock funds are often categorized based on:

- 1) *market capitalization* and
- 2) *investment style*.

Classifying by market capitalization

One way to distinguish between stock funds is to look at the size of the companies they invest in. But how do you measure a company’s size? Sales? Number of employees? Revenue? Investment experts often use a measurement called *market capitalization*, which means the total value of all of the company’s outstanding shares.

EXAMPLE	
Price	\$50
x Shares Outstanding	x 100 million
<hr/>	
= Market Capitalization	= \$5 billion

Using this measure, stock investments are often referred to as either large-cap, mid-cap or small-cap. Typically, the larger the company, the greater its market capitalization.

Stock Funds Classified by Market Cap

Large-cap Over \$10 billion in outstanding shares

Companies that tend to be older, larger and better-known.

Mid-cap \$2-10 billion

Medium size companies that are often a little more volatile than their larger counterparts.

Small-cap <\$2 billion

Small companies, including young companies that are just starting out. Stock prices of such companies tend to fluctuate more than those of larger, more established companies.

Because stock funds with different market capitalization tend to react differently to the same economic conditions, diversifying among funds can help you cushion your portfolio from a downturn in any one segment of the stock market.

Classifying by investment style

Stocks can also be categorized by investment style—meaning whether the fund emphasizes “value stocks” that appear to be selling for a bargain or “growth stocks” that appear to be rapidly accelerating in value.

Investors in value stocks are bargain shoppers. They seek out the “fallen

angels” they think have been overlooked or are underappreciated by the market. These stocks tend to be priced relatively low based on the company’s fundamental strengths.

On the other hand, growth stocks tend to be priced relatively high based on the company’s current earnings. But investors in these types of stocks feel that these stocks are worth the higher price, because they believe these rising stars are destined for future growth.

Stock Funds Classified by Investment Style

Value Stock prices are considered low relative to underlying value of company.
Typically pays higher dividends.

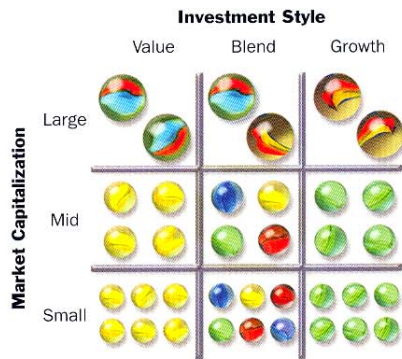
Growth Stock prices are expected to increase as company experiences high rate of growth.
Often pays no dividends, as extra cash is reinvested in company.

Value and growth stocks tend to be in favor at different periods of time—when one is up, the other is down. So again, it makes sense to include both of these types of stock investments in your retirement portfolio.

Combining size and style

To build a diversified mix of stock funds, you need to know which segment of the stock market each of your fund options is focusing on.

One way to think about your stock funds is to organize them by market capitalization and investment style using a nine-box grid.



You will need to do some research on your funds to learn where they fit in this classification system. Mutual fund rating agencies and the fund's prospectus may be helpful in determining whether the majority of the fund's investments are in small, medium or large companies, and whether the fund manager typically shops for hidden bargains, rising stars or a blend of both.

To diversify your investment portfolio, you may want to invest in different types of funds, giving

you exposure to multiple investment styles.

Some stock funds are difficult to classify by a single market capitalization or investment style, and they may move across one or more categories over time. Such funds make maintaining your diversification more difficult. Diversified Investment Advisors only offers "style-specific" funds, to help ensure that your diversification decisions remain effective.

What should I know about bonds and bond funds?

For asset class diversification, you may also want to consider bonds. Also called fixed-income securities, bonds are like IOUs. Investors in bonds or bond funds are effectively lending money to borrowers (such as governments or corporations) in return for regular interest payments. When a bond matures, the borrower repays the original investment amount to the lender.



Although bonds are generally less risky than stocks, bond investing is not without risk. The biggest factor in bond investing is movements in interest rates that can cause the value of an investment to fluctuate. The value of a bond moves inversely to changes in interest rates. For example, if interest rates in the market go up, then the value of bonds tends to go down. This is known as interest rate risk. The portfolio manager of a bond fund actively buys and sells securities in an attempt to manage this risk, but it can never be completely eliminated.

Like stocks, bonds and bond funds can also be classified by certain characteristics, including the bond's issuer, the length of time until the bond's maturity, and credit quality.

Classifying by issuer

When you're considering bond funds, take a close look at what types of organizations are backing or "issuing" the bonds. You can tell a lot about a bond fund just by knowing who's asking for the loan and guaranteeing its repayment.

Some portfolio managers focus on loans to the U.S. government; others invest in corporate bonds. Still others may spread their shareholders'

capital across a variety of different types of issuers.

U.S. Government.

Since these types of bonds, often referred to as Treasuries, are backed by "the full faith and credit of the U.S. government," they are generally regarded as the safest bond investments.



But remember that lower risk usually means lower returns. In general, U.S. Treasuries tend to provide lower interest income than other fixed-income securities.

Types of U.S. Treasuries

Length of Maturity

Bills	90 days to 1 year
Notes	2 to 10 years
Bonds	10 to 30 years

Corporations. Corporate bonds tend to be the riskiest fixed-income securities because companies—even large, stable ones—can be affected by a variety of factors within their company, across their industry or by the economy as a whole. But corporate bonds can also be the highest paying fixed-income investments, since you are generally rewarded for the extra risk you're taking.

Classifying by maturity

Bond funds are also categorized by the length of time before the bonds are due to be repaid:

- Short-term (1 to 5 years);
- Intermediate-term (5 to 15 years); and
- Long-term (greater than 15 years).

Bonds and bond funds with longer maturities typically carry more risk than those with shorter-term maturities. That's because the greater the time until a bond "matures," the greater the chances that interest rates will fluctuate. Say fund managers invest in 30-year bonds paying a 6% interest rate...but in 10 years the rates go up to 9%. In a sense, they're locked into the lower interest paying bonds. Of course, the managers could sell the 30-year bonds before they mature, but then the current prices would reflect their lower current value.

Classifying by credit quality

Bonds are also categorized by how likely the issuer is to pay its debts over time. Those ratings—expressed as AAA, AA, A, B, BB, BBB, etc.—help determine the interest rate that the issuer has to pay its investors. The lower a bond's rating, the higher the risk

that its issuer may default on the loan, and the higher the interest the issuer will have to pay to attract investors. "Investment grade" bonds are those with the highest ratings; "junk" bonds are those with the lowest ratings.

What are money market investments?



This third major asset class, also referred to as cash and cash equivalents, includes everything from dollars and Certificates of Deposit to money market funds. It also encompasses other investments used by institutions to secure short-term capital, like commercial paper.

These types of investments tend to offer a modest yield—with little risk. The value of these investments doesn't fluctuate very much over time. So there's less risk your balance will have dipped dramatically just when you need to "cash in" your shares.

Some investors keep a small portion of their money in cash or short-term investments to provide a buffer against the ups and downs of the stock and bond markets.

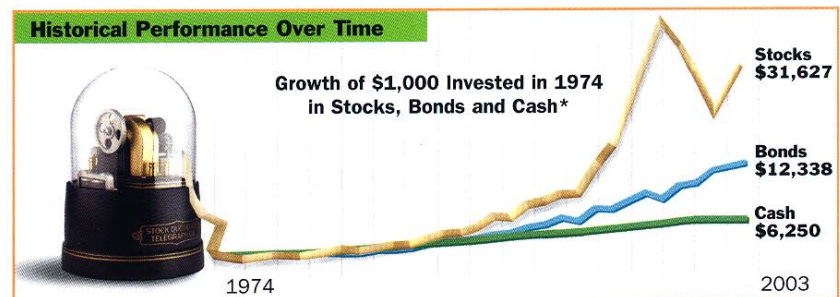
How do different investments perform?

Now that you know more about the different investment options, let's compare the performance of these options over time. Over the long term, stocks have historically offered the highest returns of the three major asset classes. Since 1926, annual returns on U.S. equities have averaged 10.5%, compared to 4.9% for bonds and 3.8% for cash.*

But don't forget...with stocks' greater potential for reward comes greater risk. So you shouldn't be surprised to learn that stocks have also subjected their investors to the bumpiest ride over the short term. And the shorter the investment period, the greater the likelihood of loss.

As you review all of the investment options your retirement plan offers, carefully consider their risk/reward payoffs. But don't forget to factor in other types of risk that may apply.

Most investors tend to focus on market risk, which is the chance that your investment's value can rise or fall based on market conditions. But as we've seen, there are other types of risk that can have an even more detrimental effect on your long-term financial health. For example, if you invest too little or too conservatively, you risk that inflation could leave you with too little buying power for your golden years. In fact, one of the greatest risks of all is that you simply won't have enough money to live on when you retire. So it's important to balance your aversion for risk with your need for growth.



*Source: ChartSource, Standard & Poor's Financial Communications. Stocks are represented by the S&P 500 Index. It is not possible to invest in an index. Bonds are represented by long-term Treasuries (10+ years) and constructed from yields published by the Federal Reserve. Cash is represented by the yield of 90-day Treasury bills. Past performance does not guarantee future results. There is no guarantee that any asset class will achieve a certain rate of return or outperform another asset class. 2GM78LIN

Assembling your investment mix

If someone asked you what the key to investment success was, what would you say? Knowing *which* stocks to invest in? Or knowing *when* to get in—or out—of the market?

The truth is that neither your timing nor your selection of individual investments has much to do with long-term returns. As the illustration below shows, it's *how* you divide your money across the various asset classes that accounts for over 92% of your investment returns.

In short, diversification is the real key to long-term investment success. Quickly defined, diversification simply means spreading your money across different types of investments.

Remember, each asset class tends to react differently to the same market conditions. So when one type of investment is up, the others tend to be down. That's why it's so important to strategically decide how to divide your money across the various asset classes.

This process, called *asset allocation*, can help you maximize potential market gains as well as minimize investment losses. When your money is spread across different asset classes, you stand a better chance of capturing some of the gain of whatever segment of the market is in favor. Plus, you minimize the risk that your entire portfolio will be dragged down by losses in an out-of-favor segment.

Factors with the Biggest Impact on Your Investment Returns

92% Investment Mix



3% Luck

3% Security Selection

2% Timing

Source: "Determinants of Portfolio Performance," Brinson, Hood and Beebower, *Financial Analysts Journal*, July/August, 1986.

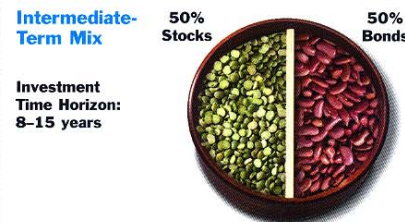
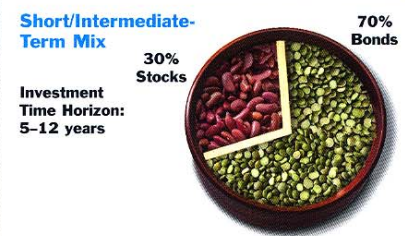
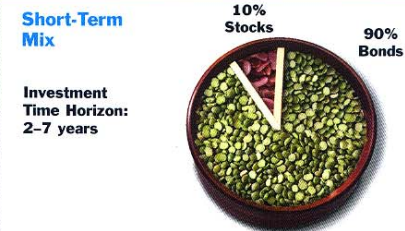
What investment mix is right for you?

Of course, there's no single answer to this question. But there are models you can use to help you decide how to allocate your retirement savings among the different types of investments.

Which model you should select depends largely on how long you have to invest. The longer your time horizon, the more heavily you may want to weight your allocation toward stocks. With more time to recover from stock market dips, you may also have more time to benefit from stock market upswings.

Take a few minutes now to calculate just how many years you have to invest before you're planning to retire. Simply match your investment time horizon to an allocation model at the right.

Then all you have to do is choose specific funds that fall within each of these major categories. You can learn more about these specific investment options by reviewing the materials you received, or by visiting Diversified Direct Online at www.divinvest.com.



Managing your account

Once you decide how to allocate your retirement plan contributions across asset classes and you choose specific funds within each of those classes, you're all set. Right?

Not quite. Keep in mind that you'll likely be contributing to your retirement plan for decades—and withdrawing from it for decades more. Over all that time, markets will fluctuate. Your goals may shift. Even laws may change. So it's important to understand all the ways Diversified Investment Advisors makes it easy to adjust your investment strategy to reflect your changing needs.

What's wrong with timing the market?

Don't mistake managing your account with trying to time your investments. Many people think they need to wait for just the right time to buy low or sell high.

Problem is, even experts find it impossible to predict market shifts with any accuracy. So novice and veteran investors alike often spend too much time sitting on the investment sidelines, just waiting for the "right" moment to jump in.

But "time in" the market tends to have a much bigger impact on your financial success than "timing" the market. Since 1994, if you had missed out on just the best 20 months of performance, your average annual return would have been just -2.95%. But if you had stayed invested that entire time, your return would have averaged 11.07%. So it's more important to stay focused on your long-term goals—and to ride out the short-term storms.

Why Market Timing Doesn't Pay



If you invested \$100 in 1994...

...and stayed invested the entire time, you'd have \$286 in 2003.

...and missed just the top 20 months of market performance, you'd have \$74 in 2003.



Source: ChartSource, Standard & Poor's Financial Communications. Stocks are represented by the S&P 500 Index. It is not possible to invest directly in an index. Past performance does not guarantee future results. 3NM885BA

Why do I need to rebalance my account?

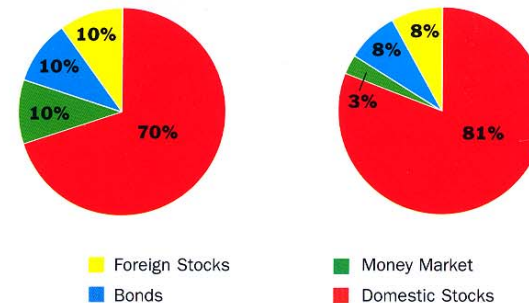
Investing for the long term doesn't mean you shouldn't ever adjust your account. In fact, it's essential that you rebalance your retirement account on a regular basis, particularly after volatile market periods. Diversified offers services to make this process easy.

Let's take a closer look at why this is so important. Say you've decided your ideal mix includes a 70%

allocation to stocks. But different investments grow at different rates. Stocks generally grow faster than bonds, and aggressive stocks tend to grow faster than conservative issues. So if left "unbalanced" during bull markets, stocks in general—and the most aggressive stocks in particular—may come to represent an increasingly larger portion of your entire portfolio. That means your account may end up unduly exposed to more risk than you had originally intended.

How Your Account Can Become "Unbalanced" Over Time

Asset allocation left unadjusted between December 31, 1983 and December 31, 2003



Source: ChartSource, Standard & Poor's Financial Communications. Domestic stocks are represented by the S&P 500 Index. Foreign stocks are represented by the Morgan Stanley Capital International Europe, Australia, Far East (EAFE®) Index. It is not possible to invest directly in an index. Bonds are represented by long-term Treasuries (10+ years) as published by the Federal Reserve. Cash is represented by the yield of 90-day Treasury bills, as published by the Federal Reserve. Past performance does not guarantee future results.

What changes should I make when I retire?

Conventional wisdom says that as you near retirement, you should move your retirement funds into fixed-income funds. But given that today's retirees may spend 20 to 30 years in retirement, that may not always be the best course of action. All too often, investors lose sight of a significant risk—*having too little money to fund their retirement*. And investing too conservatively for too long can certainly increase this risk.

Moving a portion of your savings into less risky investments may make sense. However, if you are short of your investment goals, you may need to also keep a portion of your money invested in more aggressive options. That way some of your money can still be “growing,” which is the only way you can stay ahead of inflation.

How can I protect my nest egg?

Investing for retirement is a balancing act—the objective is to invest aggressively enough to reach a specific retirement income goal, while at the same time managing risk. By following the time-tested principles of asset allocation, diversification and ongoing rebalancing as outlined in this guide, you'll be able to strike the balance you need to stay on track!



Start saving and investing wisely—today

We hope you've found this guide helpful and that you now feel better equipped to make investment decisions for your *Plan of a Lifetime*.

We know, however, that you may have questions regarding your particular financial situation. We invite you to call us for more information, or visit Diversified Direct Online at www.divinvest.com.

Securities offered through Diversified Investors Securities Corp. (DISC), 4 Manhattanville Road, Purchase, NY 10577. Contact DISC to obtain a prospectus. You should consider the investment objectives, risks, charges, expenses and other information in the prospectus before investing. Diversified and DISC are affiliated companies.

The information in this guide is general in nature and may be subject to change. Neither Diversified or DISC give legal or tax advice. Applicable laws and regulations are complex and subject to change. For legal or tax advice concerning your situation, please consult your attorney or professional tax advisor.