

Stable and Risk Averse

It would hardly be a surprise that the Summit Short-Term Government Fund invests the majority of its assets in government and agency bonds. Targeted for risk-averse investors who seek stable income, the fund eliminates the credit risk from the portfolio and manages the interest rate risk with different strategies. In addition, Mike Schultz, the manager of the fund, aims to add alpha through investments in the agency mortgage-backed area.

Q: What's your investment philosophy? Why do you believe that this is the right way to manage money?

A: A key element of our philosophy is considering who would invest in short-term government bonds, what the investors are looking for, and what their risk tolerance is. That is why we manage the fund from the standpoint of risk-averse investors, those seeking attractive returns without taking a lot of market risk. The general investment philosophy in the fund is to add incremental income while limiting interest rate risk and avoiding credit risk.

Having that profile in mind, I am very cognizant of maintaining a very stable return and not taking excessive risk in the portfolio. To add alpha, the fund invests in mortgage-backed securities in addition to U.S. Treasuries and agency notes. My background is in the mortgage-backed area and I believe that's an extra key for adding relative value to the portfolio through that market. By limiting the fund's mortgage exposure to agency securities, we have avoided the current turmoil in the subprime marketplace.

Q: What types of risks are investors trying to avoid through the fund?

A: Since the majority of the fund is invested in government and agency securities, the credit risk is largely eliminated from the portfolio. That's very different from the general bond funds, which carry credit risk to the investors. Obviously, the interest rate risk is still there, given the fact that interest and mortgage rates change, and respectively, the potential of the bond price to change. But a short-term government fund would add value through the interest rate risk part of the equation. The fund also limits risk in the mortgage-backed sector by investing in securities that maintain a relatively stable average life over a wide range of interest rates, as opposed to simply purchasing a security based upon the current yield.

Q: What is your definition of the short term?

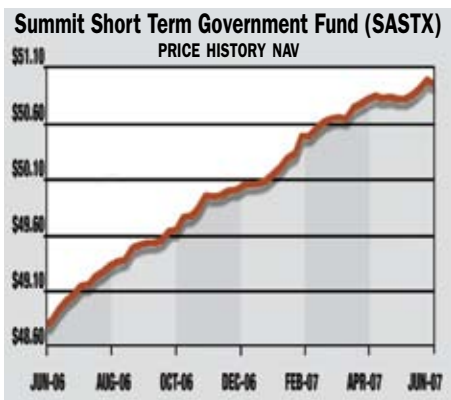
A: According to the prospectus, it is defined as less than five years, but the average life of the portfolio is in the two to three year range, which is a little shorter than that of the typical bond



MIKE SCHULTZ is the Managing Director of Mortgage-Backed Securities and Asset-Backed Securities, Portfolio Manager of the Summit Short-Term Government Fund and Co-Portfolio Manager of the Summit Bond Fund. He manages \$1.8 billion of structured securities invested in mutual funds, separate accounts and a Collateralized Debt Obligation.

Schultz has more than 24 years of investment management experience. He began as a cash management specialist with Corporate One in 1982 before moving to the School Employees Retirement System of Ohio in 1984. There he worked as a fixed income analyst and then a portfolio manager with responsibility for both the mortgage and corporate sectors. In 1988, Schultz joined ICH Capital Management as a fixed income portfolio manager. He joined Summit Investment Partners in 1992.

Schultz graduated from The Ohio State University in 1977 with a Bachelor of Arts in Economics and a Masters of Business Administration in 1980.



fund. The idea is that since I don't want to take a lot of equity and credit risk, I want something that's fairly short-term in nature. In that way I know what problems to consider in the time frame that I need the income or the principal.

Q: How does that philosophy translate into an investment strategy? How do you select the securities?

A: The investment process of trying to identify undervalued securities refers mostly to the government agency and mortgage-backed market. The Treasury market is quite rigid and I think that it is very hard to identify undervalued securities there.

Overall, when we select the securities, we have to consider the trend of the interest rates, the risk, the duration, the spread differential, as well as the overall outlook of the economy. Different strategies are required when interest rates are increasing, decreasing or are stable. For example, in a declining interest rate environment, you can add a little bit to the duration of your portfolio because the market value of the bonds will increase as interest rates decrease.

Overall, we would take a look on a duration basis but the final decisions are made considering the total risk for the fund and in which parts of the market we expect stability. The individual asset and its relative value within a given environment are an important part of the decision. But our process of adjusting the portfolio to the interest-rate environment is gradual and is usually done in small steps, as opposed to attempting to hit the ball out of the park. I should also say that I place greater importance on the economic indicators that come out on a monthly basis than on the weekly indicators.

Q: Do you also consider global trends, such as the international

trade deficit, and domestic budget deficit?

A: Yes, we definitely pay attention to such trends because it all goes back to the economic background, the supply and the demand. I don't believe that the short-term or the long-term rates exist in a vacuum. Certainly, the liquidity from global investments has helped keep our interest rates low, but if other countries that have a significant portion invested in the United States decide to pull these investments out, that will definitely affect the overall interest rate curve. It will probably have more long-term effect, but it can still have an effect on short-term interest rates as well.

Q: What's the typical allocation of the three main components of the portfolio- treasuries, agency notes and mortgage-backed securities?

A: Typically, government and agency securities represent the majority of the portfolio, or 55% to 60%. Mortgage-backed securities account for 30% to 40% of the portfolio. Since this is a government bond fund, it will always be invested mainly in government bonds, but the mortgage-backed securities typically provide value above the Treasuries. The allocation will vary depending on the current market conditions. If the spread relationship between the treasury sector and the agency or mortgage sector changes, the fund will adjust its allocation to take advantage of market dislocations.

By prospectus, we may invest up to 20% of the assets in futures and options but we would use those derivatives only to maintain liquidity or minimize trading costs. Currently, the fund is not invested in any derivative securities. We have a small portion of the portfolio invested in TIPS, which have been a good performer for us in the recent timeframe. I think that such instruments can be very useful in a

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short-term portfolio, especially when the inflation is increasing. In an increasing inflation environment, TIPS should outperform similar maturity fixed rate treasury securities.

Q: How many securities do you typically hold? What's your selling and buying discipline?

A: We have roughly 25 names but that may vary depending on the environment. There are times when I would add smaller pieces, especially in the mortgage-backed area. At times, smaller mortgage-backed positions offer relative value in the marketplace simply because many managers generally prefer larger positions. The willingness to evaluate smaller positions while maintaining the overall fund liquidity, allows the fund to add incremental value for the investor.

When buying securities, we are very cognizant of the relative percentages for the overall portfolio allocation and risk. I wouldn't stray too far away from those ranges and increase the mortgage component to where it would become a majority holding because this is a short-term government fund. The next step is to look for where we feel is the best relative value given the general interest rate environment and where on the yield curve we would position ourselves.


In our selling process, we're constantly evaluating the underlying securities and comparing them to similar things within the specific market. For example, within the mortgage-backed area sometimes a certain sector is cheaper to others, and that would be a time to go into that sector. So we constantly look at the various different options and we try to add relative value to the fund by selling securities or sectors that are too rich and buying those that are cheap.

Q: What are the main differentiators of this fund as compared to other bond funds?

A: Overall, a short-term government bond fund has fewer moving parts than a general bond fund. The main difference is related to the philosophy for stability of the principle and risk aversion. In a general bond fund, you would be buying bonds from highly rated companies such as General Electric or 3M to below investment grade securities and there is always the possibility of a credit event, especially with the tremendous amount of leverage buyouts business in the marketplace currently.

I believe that this has definitely been a risk to the credit markets recently. There's so much private equity in the marketplace right now and no company is too big to be bought anymore. Different than in the past, there are no longer supposedly safe investments like utilities. For example, Texas Utilities was taken over by a private equity fund through a leverage buyout.

From that standpoint, all other things – like duration and average life - being equal, you should expect greater incremental income from a general bond fund. But you're also taking greater incremental risk, and some investors aren't interested in taking any risk.

So it all goes back to the advisor figuring out the risk tolerance of the client and his financial goals. There are investors who know that they will need their money in two or three years because their kids are going to college, for example. That's why they need a very good idea of how much money they're going to need in a certain period of time, and that's where a short-term government fund offers advantages as compared to other instruments. 

Summit Short-Term Government Fund

Symbol	SFSTX (Class A), SASTX (Class I)
Website	www.summitfunds.com
Address	Summit Investment Partners Inc 312 Walnut Street Suite 2500 Cincinnati, OH 45202
Tel. No.	888-259-7565
Inception	04/03/2000

PORTFOLIO

Total Net Assets*	\$26.8
Average Maturity	2.37 years
Average Coupon	4.5%
Average Duration	1.32 years
Turnover Ratio	39%

INVESTMENT INFORMATION

	SFSTX (Class A)	SASTX (Class I)
New Investment	Open	Open
Min Initial Investment	\$2,000	\$250,000
Min Subsequent Investment	\$50	\$0
Min Initial IRA Investment	\$500	\$500

RISK (AGAINST CITIGROUP 1-5 YEAR TREASURY)

Alpha	0.04
Beta	0.90
R-Squared	0.92
Ann. Std Deviation	2.56
Sharpe Ratio	0.57

RETURNS VS. CITIGROUP 1-5 YEAR TREASURY

	SASTX (Class I)	Index
1 Year (Cum.)	4.62%	5.19%
3 Year (Ann.)	3.01%	2.86%
5 Year (Ann.)	2.72%	2.99%
Since Inception	4.18%	4.61%

RETURNS VS. CITIGROUP 1-5 YEAR TREASURY

	SFSTX (Class A)		Index
	W/O LOAD	W/LOAD	
1 Year (Cum.)	4.38%	1.25%	5.19%
3 Year (Ann.)	2.76%	1.72%	2.86%
5 Year (Ann.)	2.47%	1.85%	2.99%
Since Inception	3.92%	3.49%	4.61%

FEES AND EXPENSES

Max Sales Charge - Front	3.00%
Max Sales Charge - Deferred	0.00%
Max Redemption Fee	0.00%
Total Expense Ratio SASTX (Class I)	0.73%
Total Expense Ratio SFSTX (Class A)	0.98%

PORTFOLIO MANAGER

Michael Schultz	04/03/2000
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*millions

Data through: 06/30/07

Source: Company Documents; Lipper

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