

“Where there is no vision, the people perish.” Proverbs 29:18



## Active Management Optimizer<sup>SM</sup>

— Quantifying an Advantage

Spectrum Financial is a strong proponent of utilizing Active Management in its investment strategies through VISIONMAXX<sup>SM</sup>. The strategies are actively managed to anticipate and respond to trends in differing types of capital markets. With strategies that identify, quantify, and control elements of risk, Spectrum Financial can provide investors with reduced risk and volatility.

Proponents of a buy-and-hold passive investment strategy warn of missing the best “up” market days and the disaster to your investment account that will surely occur. Buy-and-hold proponents frequently pose questions such as — “What happens if Spectrum sells prematurely and not at the top?” or “What happens if Spectrum doesn’t buy at the bottom?”

Answers to these questions are found in one of the concepts underlying Active Management. Spectrum’s strategies are actively managed to seek steady gains while limiting losses. The

goal of active management is not to buy at the exact low or to sell at the exact high. The goal is to move into cash and to side-step the volatile negative periods so that cash is available to reenter the market when an uptrend begins. Spectrum strives to optimize the amount of time its strategies are invested in an up-trending market as well as optimize the amount of time its strategies are invested in cash in a down-trending market. Spectrum calls this strategy advantage the Active Management Optimizer<sup>SM</sup>.

### Active Management Optimizer<sup>SM</sup>

Spectrum conducted an internal research study comprised of seventeen (17) plus years of daily price data of a Spectrum financial strategy. The time period contained multiple market drawdowns and recoveries.

The Active Management Optimizer<sup>SM</sup> represents the percentage of the market advance that could be missed and the percentage of the market decline that could have been participated in while still matching the performance of a passive buy-and-hold investor (Figure 1).

The Active Management Optimizer<sup>SM</sup> was calculated by first determining the average performances of the Spectrum strategy, the S&P 500 and the High Yield Bond Index during market corrections. The average performance of each of the latter two indexes was subtracted separately from the Spectrum strategy performance. The remainder is then multiplied by 0.50 to represent the percentage of the market advance that could be missed and the percentage of the market decline that could have been participated in while matching the performance of a buy-and-hold investor.

The internal study’s results provided two conclusions:

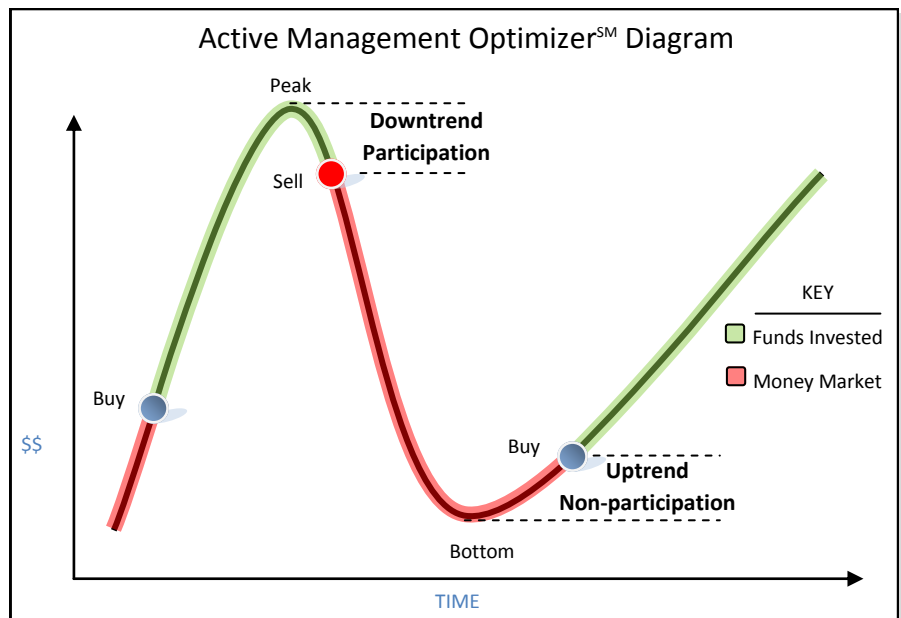


Figure 1—Active Management Optimizer<sup>SM</sup>

- active management provides a sizeable advantage over a passive buy-and-hold strategy; and
- As the size of the market drawdown increases the Active Management Optimizer<sup>SM</sup> increases.

To clarify this active management concept, Figure 2 illustrates its power. The example uses a scenario from a previous technical paper for the Active Management Multiplier<sup>SM</sup>. The example spans a 3-year cycle and involves the purchase of \$5,000.00 of XYZ mutual fund by two investors—one using an active management strategy and one using a buy-and-hold passive strategy.

Both investors purchased the same number of shares of XYZ mutual fund on the same day—100 shares @ \$50.00 for a \$5,000.00 investment. During the 3-year time span, the market enjoyed a 20% uptrend during Year 1 and a 20% downtrend in Year 2. The Active Management Investor detected a 3% price decline as Year 2's downtrend began and sold XYZ shares realizing an \$820.00 profit. In contrast, the Buy & Hold Investor began the ride down the market slope to a year-end price of \$48.00. The beginning of Year 3 saw an end to XYZ's downtrend and rebounded 20% to close at \$57.60. The Active Management Investor's technical signals detected the uptrend after a 3% price increase and repurchased 117.72 shares of XYZ mutual fund at \$58.20. The newly purchased shares appreciated the remainder of the year to end at \$57.60.

The Active Management Optimizer<sup>SM</sup> for XYZ mutual fund is calculated by determining the final account performance increase at Year 3's end. The Active Management Investor's account increased by 36.19% while the Buy & Hold Investor's account increased by a much smaller percentage, 15.20%. The final account balances show that the Active Management Investor enjoyed an overall advantage of 20.41% (35.61% - 15.20% = 20.41%). Even though the Active Management Investor participated in a small portion of the downtrend and missed a small portion of the uptrend, his account grew 20.41% larger due to the Active Management Multiplier<sup>SM</sup> effect over the full three-year market cycle.

In summary, the Active Management Optimizer<sup>SM</sup> quantifies how an active management investor can enjoy wide percentage latitude in his entry and exit points while continuing to match or exceed the performance of a buy-and-hold investor. By avoiding drawdowns and optimizing the time spent participating in uptrends an active management investor can realize significant returns as compared with a buy-and-hold investor.

<b>Active Management Optimizer<sup>SM</sup> Example</b>								
<b>Year 1 - Uptrending Market XYZ Mutual Fund</b>								
	<u>Shares</u>	<u>Buy</u>	<u>Total</u>	<u>Year-End</u>	<u>Year-End Balance</u>			
Active Management Investor	100	\$ 50.00	\$ 5,000.00	\$ 60.00	\$ 6,000.00			
Buy & Hold Investor	100	\$ 50.00	\$ 5,000.00	\$ 60.00	\$ 6,000.00			
<b>Year 2 - Drawdown Market XYZ Mutual Fund</b>								
	<u>Shares</u>	<u>Sell - 3% decline</u>	<u>Acct. Balance</u>	<u>Price Year-End</u>	<u>Year-End Balance</u>			
Active Management Investor	100	\$ 58.20	\$ 5,820.00 (cash)	n/a	\$ 5,820.00			
Buy & Hold Investor	100	n/a	\$ 5,820.00	\$ 48.00	\$ 4,800.00			
<b>Year 3 - Uptrending Market XYZ Mutual Fund</b>							<b>Final</b>	<b>Final</b>
	<u>Shares</u>	<u>Buy - 3% uptrend</u>	<u>Total</u>	<u>Year-End</u>	<u>Year-End Balance</u>	<u>Amt. Increase</u>	<u>% Increase</u>	
Active Management Investor	117.72	\$ 49.44	\$ 5,820.00	\$ 57.60	\$ 6,780.67	\$ 1,780.67	35.61%	
Buy & Hold Investor	100	n/a	\$ 4,944.00	\$ 57.60	\$ 5,760.00	\$ 760.00	15.20%	
						<b>Active Management Optimizer<sup>SM</sup></b>	<b>20.41%</b>	

Figure 2: Active Management Optimizer<sup>SM</sup> Example

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