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

Compound Correlator℠

— A Continuous Advantage

Spectrum Financial is a strong proponent of utilizing Active Management in its investment strategies employed through VISIONMAXX℠. Investors seeking to achieve their financial goals by low-cost index investing have been disappointed in recent years by the markets' lack-of-performance. Investors who use a "buy-and-hold" investment strategy realized positive returns in the extended 1990's bull market. Unfortunately for these investors, recent years have delivered two economic recessions with severe market corrections that ravaged many investors' portfolios. Diversifying a portfolio only by asset class did not protect these investors' funds as asset class correlations rose to record high levels in periods of market distress. In contrast, Spectrum Financial utilizes two investing principles that provided positive results—compound growth and low correlation.

Compound Growth

Spectrum's Active Management strategies strive to preserve excess performance and original principal by attempting to sidestep market downturns by moving to cash. Once the market correction has ended, the funds are reinvested in larger positions at reduced price levels. These larger positions benefit from market uptrends resulting in greater wealth. This "growth" reinvestment is a form of continuous compounding. The growing fund creates more wealth which creates additional funds, building even more wealth. For continuous growth to proceed unimpeded, it is imperative that funds avoid a negative drawdown. Incurring consecutive drawdown periods signifies compound decay. For an account to return to its previous highs it must realize larger percentage gains than its prior percentage losses. (See table below, Years 2001—2004 and Years 2008—2010). Compound growth means your interest earns interest. A real world example of compound growth is shown in the time period between 2001—2010. The table compares Spectrum's High Yield Bond Strategy to the S&P 500, highlighting the steady growth generated by positive returns for the High Yield Bond Strategy. The table also shows the damaging consequences of negative returns to the S&P 500 fund. Consecutive years of negative growth represent compound decline and it requires years for a portfolio to recover. In this example, growth of the High Yield Bond Strategy is compounded over many periods resulted in a sizable fund balance advantage of $189,038 ($301,827-112,789).

Initial Investment $100,000				
	High Yield Bond Strategy		S&P 500 Index	
Year	**Return %**	**Balance**	**Return %**	**Balance**
2001	12.8%	112,789	-2.0%	98,044
2002	9.6%	123,637	3.9%	101,876
2003	25.9%	155,636	14.8%	116,943
2004	9.0%	169,605	4.9%	122,669
2005	4.7%	177,544	2.8%	126,077
2006	7.9%	191,503	10.6%	139,497
2007	1.5%	194,292	1.9%	142,090
2008	-0.5%	193,385	-21.8%	111,180
2009	40.3%	271,254	8.4%	120,523
2010	11.3%	301,827	6.5%	128,344

The High Yield Bond Strategy performance is calculated by using the non-weighted quarterly average of actual bond mutual funds used in the trading strategy during the timeframe. Fees for these accounts are assumed to be 0.50% per quarter. Performance numbers were selected from client accounts having no purchases or withdrawals during the period, and may have been obtained from personal or related accounts. Some performance may vary due to fund restrictions and/or limitations imposed by the mutual fund families. Dividends are assumed to be reinvested. The initial commission on funds is not taken into account but could reduce performance. Past performance does not guarantee future results. Current performance may be lower or higher than data quoted.

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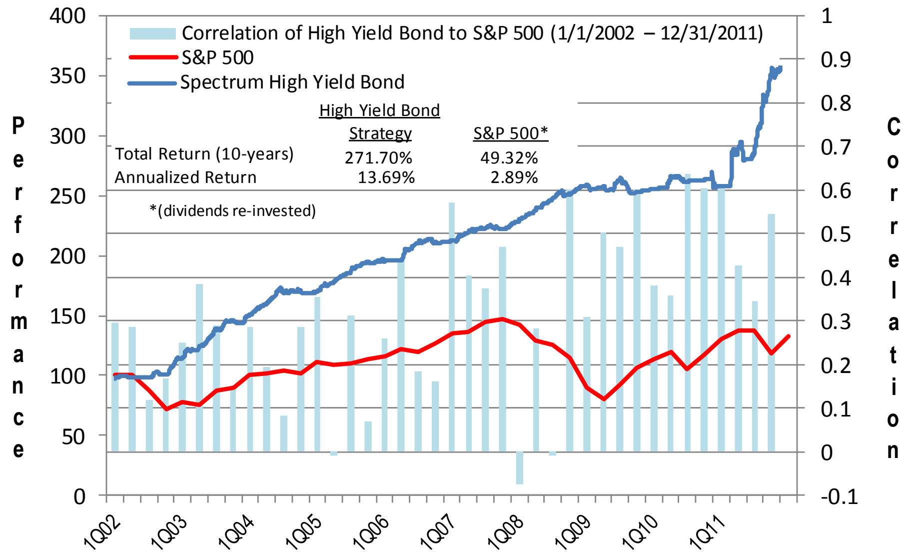
TRANSFORMING THE *way* YOU INVEST

Low Correlation

One financial metric that provides an indication of how an asset class or strategy will perform in a general market downtrend is its “correlation coefficient” with the S&P 500 Index. Investment strategies that side-step a downtrend possess a low-to-negative correlation for that specific time period. The negative correlations signify that a directional move by the strategy’s asset class would be opposite from the S&P 500 Index movement.



This chart illustrates Spectrum’s SecurityMaxx High Yield Bond Strategy signals as applied to the Average High Yield Bond Fund which is calculated by an equal weighting of all the high yield bond funds’ daily net asset values tracked by the FastTrack database. Daily pricing is adjusted for dividend reinvestment and does not reflect sales loads. Performance numbers are not derived from actual account values. Performance for individual bond funds may vary somewhat due to fund restrictions and/or limitations imposed by the fund family. Spectrum’s High Yield Bond Strategy has fees of 1.9% deducted annually in advance. The S&P 500 is a capitalization-weighted index of 500 stocks representing all major industries. Dividends are reinvested. Past performance does not guarantee future results. Current performance may be lower or higher than data quoted.

Recent years have seen correlations between asset classes rise to all-time highs. Periods of financial distress have shown a trend of correlations to the S&P 500 Index of almost 1.0. These trends reveal that markets are beginning to move in synch with each other, thus negating their intended diversification properties.

The accompanying figure illustrates compound performance over a ten year period (January, 2002—December, 2011) for Spectrum’s High Yield Bond Strategy. The bar chart highlights the quarterly correlations of the High Yield Bond Strategy to the S&P 500 Index. During this highly volatile ten year time period, the High Yield Bond Strategy exhibited variable correlations to the S&P500. The correlations ranged from negative in the down-trending markets of 2005 and 2008 to a high of 0.62 in the 2010 up-trending market. The negative correlations validate one of active management’s core tenets —avoiding market drawdowns. The higher positive correlations validate yet another active management core tenet —participating in market uptrends.

Active management strategies are considered successful by evaluating two metrics—performance and risk mitigation. An investment strategy that achieves a positive annual return that exceeds a relevant benchmark through a full market cycle is successful. In addition, a risk mitigation strategy is successful if investment safeguards undertaken to minimize the chances of a “drawdown” occurring in a portfolio prove sound.

Spectrum Financial’s High Yield Bond Strategy has successfully combined the two investing principles of compound growth and low correlation in the Compound Correlator[SM]. Compounding the positive returns on a yearly basis while avoiding negative returns has enabled the High Yield Bond strategy to outperform the S&P 500 Index. New strategies and investment risk management techniques must be employed to meet the challenges presented by an ever-evolving global financial environment. For financial advisors and investors searching for an alternative to a “buy-and-hold” strategy, Spectrum’s Compound Correlator’s ability to enhance compounding and maintain variable correlations when market environments warrant, provides an additional way to diversify a portfolio which is often overlooked by investors.

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