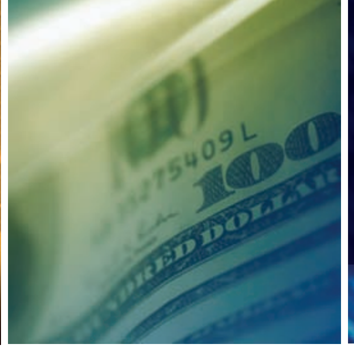


SimonDavis

ASSET MANAGEMENT INC.

SIMONDAVIS

We believe that markets are not 100% efficient; therefore, our approach is founded on the belief that a passively managed investment strategy can't possibly cope with the market's constant fluctuations.

SimonDavis Asset Management, Inc. is an SEC Registered Investment Advisor headquartered in Denver, Colorado. Since our inception we have evolved into a premier asset management firm. We pride ourselves on providing independent, integrated and comprehensive asset management to Registered Investment Advisors throughout the country.

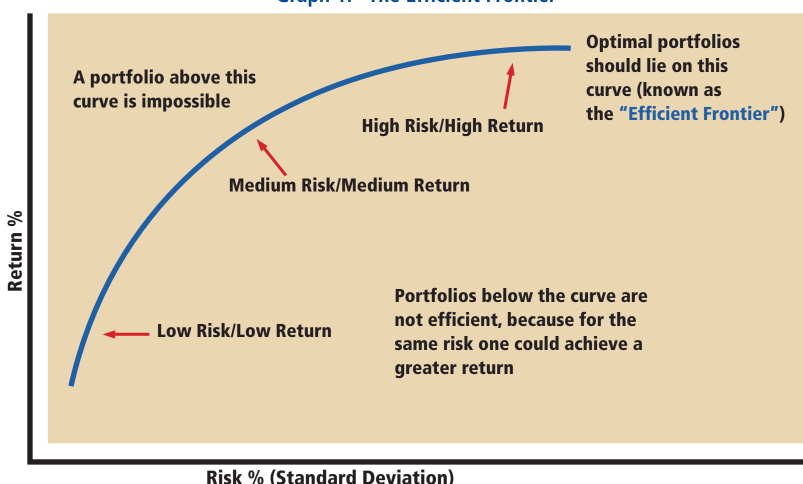
Our Overriding Investment Philosophy

Constructing a successful investment portfolio is among the most fundamental of requirements for financial success. It demands strict discipline and a keen understanding of risk, the markets and the economy.

Our goal is to achieve superior risk-adjusted returns in all market conditions. We do this through a proprietary process grounded in rigorous research, superior security selection and a cutting-edge diversification methodology.

Superior performance can best be achieved through active management. Active management is dynamic and flexible and allows us to utilize the best components of proven investment strategies while giving us the flexibility to pursue new and progressive investment ideas given the continually changing landscape of the markets.

Graph 1: "The Efficient Frontier"



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The Case for Active vs. Passive Management

For decades individuals have turned to financial advisors to construct diversified portfolios for their investments which have largely been based on the diversification principles of ***Modern Portfolio Theory*** as outlined in Harry Markowitz's famous 1952 Nobel Prize winning paper. The basic premise is that there is an optimum way to create a portfolio given an individual's appetite for risk. In other words, for each level of risk there is an optimal mix of asset classes that will maximize a portfolio's return over time. When this risk/return relationship is graphed it forms a line that is known as the **"Efficient Frontier"** (see Graph 1).

What is Passive Asset Allocation?

Markowitz's Efficient Frontier is based on the belief that it is difficult, if not impossible to out-perform the market on a consistent basis. As a result the majority of investment advisors construct portfolios via a passive asset allocation model. These portfolios are static, infrequently monitored and are often subject to much greater risk than anticipated given the fact that the historical data used to create these models has fundamentally changed and thus generates calculations that are flawed.

The power of the theory rests in the framework that when combining non-correlated asset classes an investor can achieve greater returns with less risk than when combining asset classes that move together or investing in a single asset class.

Regardless of stock market behavior, we believe a passively managed portfolio is only changed during periodic rebalancing, the primary purpose of which is to return the portfolio to its original allocation.

Our proprietary research strongly suggests that the Efficient Frontier is both outdated and broken. Nothing provides greater evidence of this fact than what has happened to passively managed "diversified" portfolios over the past few years.

Table 1: Correlations Between the S&P 500 Index and Select Foreign Asset Classes

Time Period	S&P 500	MSCI EAFA Developed Markets	MSCI Emerging Markets
1970-1981	1.00	0.57	-0.09
2003-2007	1.00	0.93	0.98

*Source: Guerite Advisors, Imbriglia Proprietary Research

Portfolios constructed using Modern Portfolio Theory methods have plummeted alongside the broad market despite statistical output that suggested they would have performed better.

The statistical foundation of Markowitz's Modern Portfolio Theory is based on the assertion that asset classes – stocks, bonds, real estate, cash, etc. – are not perfectly correlated. The power of the theory rests in the framework that when combining non-correlated asset classes an investor can achieve greater returns with less risk than when combining asset classes that move together or investing in a single asset class. One point that immediately becomes clear when thinking about this assertion is the importance of data used to construct the efficient frontier – the model is only as good as the input.

It is no secret in the investment community that assets are becoming more correlated. For example, during the 1970's and 1980's U.S. stocks and foreign stocks did not necessarily move in lock step; however, in the 1990's and the 2000's globalization caused disparate markets to be influenced by the same factors, and the benefits of balancing one of these assets against another diminished. This is an obvious, but important, observation.

The historical data used in Modern Portfolio Theory has fundamentally and permanently changed thus rendering its output less effective.

Table 1 above shows basic correlations between the S&P 500 and international stocks in both developed and emerging markets. This data nicely frames the discussion around correlation – even at a brief glance the message is clear – domestic stocks have been much more correlated to international stocks recently than they were in the past. Versus the 1970's, in the last five years the S&P 500 went from having a mild correlation to International Developed Markets (0.57) to having a near perfect correlation to them (0.93), and went from having a negative correlation to Emerging Markets (-0.09) to an even higher correlation than to Developed Markets (0.98).

TABLE 2: Five Year Asset Class Correlations (2004-2008) ***less*** Twenty-Five Year Correlations (1984-2008)

	Small Cap Value	Small Cap Growth	Mid Cap	Large Cap Value	Large Cap Growth	Foreign Stocks	Invstmt Grade Bonds	High Yield Bonds	REITs
Small Cap Value	**0**								
Small Cap Growth	0.16	**0**							
Mid Cap	0.11	0.26	**0**						
Large Cap Value	0.16	0.19	0.02	**0**					
Large Cap Growth	0.31	0.18	0.19	0.12	**0**				
Foreign Stocks	0.47	0.38	0.29	0.29	0.41	**0**			
Investment Grade Bonds	**-0.73**	**-0.29**	**-0.54**	**-0.63**	**-0.37**	**-0.42**	**0**		
High Yield Bonds	0.11	0.17	0.39	0.30	0.35	0.41	**-0.55**	**0**	
REITs	0.16	0.36	0.32	0.32	0.52	0.51	**-0.73**	0.20	**0**

*Source: Proprietary Research

Table 2 goes into more depth around the data set chosen for this study – it indicates the differences in the five year correlation coefficients and the twenty-five year coefficients. That is, if two assets were correlated perfectly (1.00) over the last five year period and only 0.75 correlated over the last twenty-five year period, the chart would read 0.25 (1.00 minus 0.75). The positive numbers in the graph indicate by how much two assets have become more correlated over the last five years versus the last twenty-five years; the negative numbers the reverse.

Notice in Table 2 that all asset classes, except Investment Grade Bonds, have become to some degree more correlated over the last five years than they have been over the last twenty-five. Given what we know about the world this should come as no surprise. What is surprising is that most investment advisors continue to use outdated historical data while attempting to optimize portfolios for clients.

Table 3 (right) illustrates how differently asset classes as a whole have behaved during past bear markets. As you can see during the bear markets of 1990 and 2000-2002, asset class returns varied greatly. For example in 2000 and 2001 three asset classes achieved positive returns for the year and five were negative. Additionally, the range of returns in negative returning asset classes was quite wide in all years of the prior two bear markets.

TABLE 3: Bear Market Period & Total Peak to Trough Decline (%)

Bear Market Period & Total Peak to Trough Decline (%)

JUL 16, 1990 to OCT 11, 1990 -20%	MAR 24, 2000 to OCT 29, 2002 -49%			OCT 12, 2007 to MAR 9, 2009 -58%
1990	**2000**	**2001**	**2002**	**2008**
BC Agg **8.96%**	Russell 2000 Value **22.83%**	Russell 2000 Value **14.02%**	BC Agg **10.26%**	BC Agg **5.24%**
S&P/Citi 500 Growth **0.20%**	BC Agg **11.63**	BC Agg **8.43%**	Russell 2000 Value **-11.43%**	Russell 2000 Value **-28.92%**
S&P 500 **-3.11%**	S&P/Citi 500 Value **6.08%**	Russell 2000 **2.49%**	MSCI EAFE **-15.94%**	Russell 2000 **-33.79%**
S&P/ Citi 500 Value **-6.85%**	Russell 2000 **-3.02%**	Russell 2000 Growth **-9.23%**	Russell 2000 **-20.48%**	S&P/Citi 500 Growth **-34.92%**
Russell 2000 Growth **-17.42%**	S&P 500 **-9.11%**	S&P/Citi 500 Value **-11.71%**	S&P/Citi 500 Value **-20.85**	S&P 500 **-37.00%**
Russell 2000 **-19.50%**	MSCI EAFE **-14.17%**	S&P 500 **-11.89%**	S&P 500 **-22.10%**	Russell 2000 Growth **-38.54%**
Russell 2000 Value **-21.77%**	S&P/Citi 500 Growth **-22.08%**	S&P/Citi 500 Growth **-12.73%**	S&P/Citi 500 Growth **-23.59%**	S&P/Citi 500 Value **-39.22%**
MSCI EAFE **-23.45%**	Russell 2000 Growth **-22.43%**	MSCI EAFE **-21.44%**	Russell 2000 Growth **-30.26%**	MSCI EAFE **-43.38%**

*Source: Proprietary Research

Flexible and dynamic active management styles allow us to optimize portfolio performance while managing risk in all market conditions.

Juxtapose these facts to those of the most recent 2007-2009 bear market (which primarily occurred during 2008) and the data clearly supports the theory that asset classes are behaving more alike. During the 2008 decline only one asset class (Investment Grade Bonds) achieved a positive return for the year of 5.24%. All other asset classes had negative returns and all of these asset classes returned less than -28.92%.

What we can conclude from the data in Tables 1, 2 and 3 is that virtually all asset classes are becoming more correlated and that returns are not only unstable, but that they evolve radically over time. This creates a unique challenge for a money manager – strategic asset allocation can only be as effective as the manager who understands the data that goes into the model. Designing properly diversified investment portfolios has become increasingly difficult and we no longer can rely on traditional asset allocation methods. SimonDavis is on the cutting edge of progressive portfolio construction.

What is Active Asset Allocation?

Active asset allocation is based on the belief that with an advanced understanding of the markets there is a more effective way to manage money.

In contrast to a "buy and hold at any cost" strategy the active manager has the flexibility to tactically move the investor's money into or out of market segments that are perceived to be gaining or losing strength.

At SimonDavis Asset Management, Inc. all of our strategies offer the flexibility to meet the investor's long-term goals, as well as to seize market opportunities related to market and economic cycles. Each of our strategies is actively managed, rooted in the same dynamic philosophy and fine tunes its holdings and strategy for a specific risk appetite and tax situation.

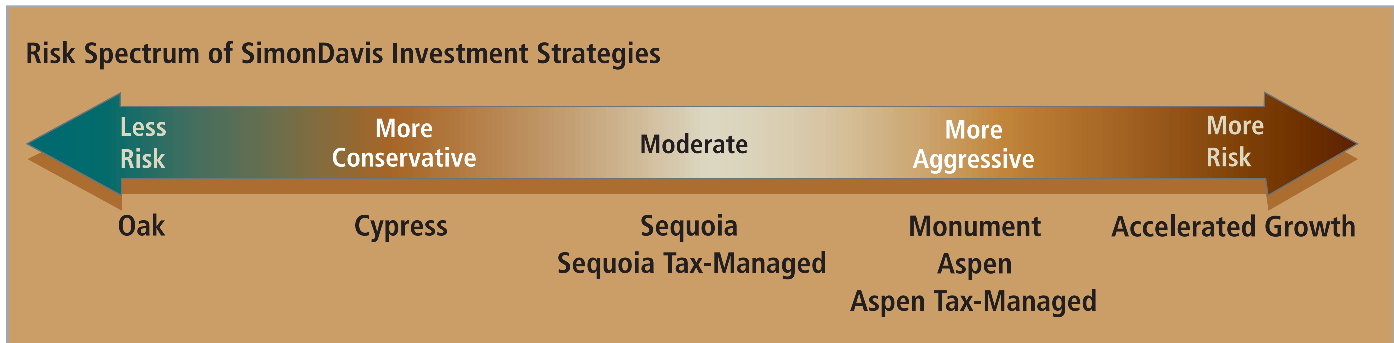
Overview of SimonDavis Asset Management, Inc. Proprietary Equity and New Frontier Investment Strategies

At SimonDavis we strive to offer a wide array of investment alternatives and strategies that enable us to meet the ever changing needs of the investor. In general, we provide *two Proprietary Equity SMAs and six New Frontier SMA Series investment strategies.* Each offers a unique opportunity designed to meet the investor's personal investing goals and risk tolerance and is able to respond appropriately to broad economic and market cycles. The various SimonDavis investment strategies are as follows:

SimonDavis Proprietary Investment Strategies:

- Monument
- Accelerated Growth
- New Frontier SMA Series
  - *Aspen*
  - *Aspen Tax-Managed*
  - *Sequoia*
  - *Sequoia Tax-Manged*
  - *Cypress*
  - *Oak*

For complete details regarding all SimonDavis investment platforms and strategies please see our most recent Form ADV part II and Performance Report which are available on our website at: **www.simondavisinc.com**; or, contact your financial advisor.



Strategy Details

Beyond the Efficient Frontier - Proprietary Investment Strategies

All proprietary investment strategies are managed on a fully discretionary basis and each offers a unique opportunity to customize your specific risk tolerance and tax situation. There are six different strategies in the New Frontier SMA Series all rooted in our **"Beyond the Efficient Frontier"** methodology of tactical asset allocation described below. The six strategies are:

NEW FRONTIER SMA SERIES

- ASPEN
- ASPEN TAX-MANAGED
- SEQUOIA
- SEQUOIA TAX-MANAGED
- CYPRESS
- OAK

The only way to truly control and manage risk is through a properly diversified investment portfolio. Using old asset allocation methods is not effective and may produce inaccurate statistical predictions.

Our Beyond the Efficient Frontier Methodology enables us to construct portfolios that we believe are superior to traditional allocation methods – thereby giving our investors the best chance of achieving superior returns for their individual appetite.

All of the investment strategies are built on a properly diversified foundation essential to long-term planning and growth and are supplemented with positions that we believe give the portfolio a high statistical probability to outperform its benchmark.

We believe that the combination of our proprietary research on asset allocation and our fundamental and quantitative analysis enable us to construct portfolios that go "**Beyond the Efficient Frontier**" giving the investor the greatest chance of achieving superior risk-adjusted returns.

Traditional asset allocation is passive and produces results that are much more volatile than predicted given the fact that many historical uncorrelated asset classes now move together.

The portfolios are typically invested in approximately 10-15 positions from a broad universe of primarily exchange-traded-funds (ETFs). ETFs provide the best opportunity to create portfolios with different asset class exposures and risk profiles. Through ETFs we can access a plethora of asset classes, styles, sectors, countries, and regions with precision.

Other advantages of ETFs include:

- Significantly lower expenses;
- Improved transparency;
- Flexible intra-day trading; and,
- Greater tax control and efficiency

SIMONDAVIS
ASSET MANAGEMENT INC.

PROPRIETARY EQUITY SMAS

- **MONUMENT**
- **ACCELERATED GROWTH**

Monument

Monument utilizes both technical and fundamental analysis as a three tiered approach to investing: ***Market Direction, Stock Selection and Money Management.***

The Market Direction component relies on proprietary technical analysis and seeks to determine general and established trends of the equity markets. Specifically, when the technical analysis suggests the market is likely to trend up (or is in the process of doing so), the manager will deliberately pursue a fully invested allocation.

Alternately, if the indicators identify a likely downward bias, the manager will seek a cash/cash equivalent position with the majority (if not all) of the portfolio and wait for opportunities to emerge to strategically re-enter. Last, if the market is trending laterally in a consolidated fashion (or is already doing so), the manager will pursue an appropriate blend of cash/cash equivalents and equities. In addition, the portfolio will be predominately in cash for a period of time if the consolidation is after a sell-off. From this position, the manager will wait for a confirmed uptrend to re-enter the market with select equities. If the sideways trendless consolidation pattern is after a run-up in the market, the portfolio will remain allocated in its equity positions until a confirmed sell signal is given. At that point the manager will scale back exposure to the systematic risk, capture gains, and deploy the portfolio's assets to the safety of cash/cash equivalents.

The Stock Selection component is fundamental in nature and relies on a series of proprietary sorts which include, but are not limited to, valuation ratios, per share ratios, dividend ratios and solvency ratios. The analysis focuses on high quality stocks which exhibit the greatest potential for growth while trading at a discount to their intrinsic value.

Analysis of ratios that have historically identified stocks with lower volatility than the markets can also play a prominent role in equity selection. Equity positions are evaluated on a constant basis to determine their appropriateness in the portfolio's allocation.

The Money Management component is more stylistic in nature. It is engaged when the technical indicators referenced above (Market Direction) determine whether a move in or out of the markets is in order.

One of the portfolio manager's primary drivers for decisions is determining the direction of the markets. Once a change of trend is signaled, the manager will begin to scale positions either in or out of the market. Markets have a history of randomly defying technical and fundamental analysis and the manager is acutely aware of the ever-present risk this poses to the success of the strategy.

Therefore, equity positions will be phased in and out over several weeks to allow the emerging pattern to fully establish itself and subsequently reduce the risk of a "whipsaw" event.

Accelerated Growth

Accelerated Growth is our most aggressive investment strategy emphasizing capital appreciation over the long-term. The portfolio is typically fully invested in approximately 20 positions from a broad universe of primarily individual stocks and exchange-traded-funds (ETFs). Accelerated Growth reserves the right to move into cash during times of extreme market turbulence. The primary focus is to continually seek out growth opportunities in an effort to outperform the S&P 500 on a risk-adjusted basis.

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