Capital Defender

Asset Allocation Series

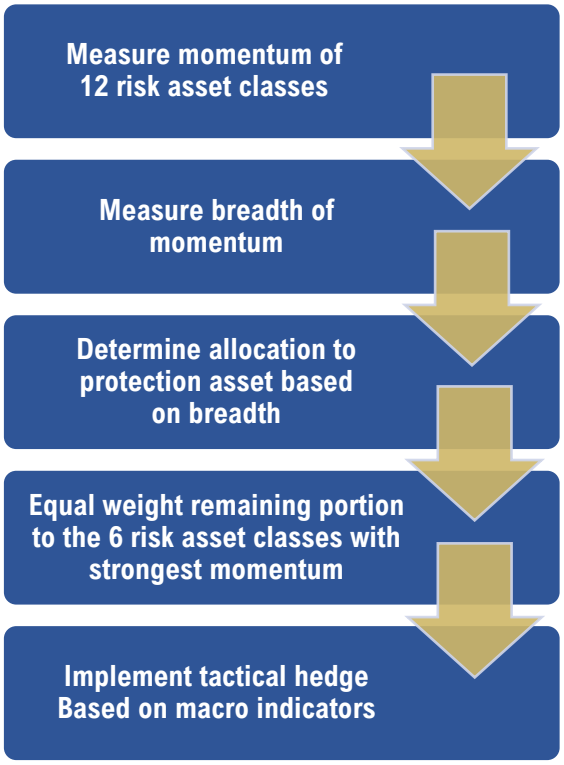
A disciplined approach to capital preservation & growth in volatile markets

THE PACIFIC FINANCIAL GROUP

Overview

"Sequence of return risks" can be a substantial when an individual is close to and especially during retirement; an untimely market drawdown can significantly impair finances and retirement goals. Risk management is key, however, most retirement plans and traditional asset allocation models become over-dependent upon bonds for this task. The risk of rising rates, low yields, and longer duration have the potential to make bonds a relatively poor risk management strategy going forward. Future bond returns are expected to be significantly lower than past historic returns, posing a drag on retirement portfolio performance. To further complicate the environment investors are experiencing extended equity valuations, heightened volatility, and bond duration risk. The TPFG Capital Defender Asset Allocation Series can be an alternative risk management approach. These risk-based strategies can replace some equity and bond allocations to potentially improve risk-adjusted returns.

The Defender approach involves the utilization of a lower risk/absolute return portfolio. It is a tactical variation of traditional 60% equity and 40% bond portfolio that seeks to increase the chances of positive returns through an optimal asset class mix using multi-market breadth and dual momentum. The purpose of this approach is risk management to provide more consistent rates of returns without simply relaying on bonds and broad market diversification alone.



Strategy Description

The TPFG Capital Defender Asset Allocation Series looks at the market as a whole and adjusts and rebalances once per month to account for multi-asset market movement as compared to the traditional equity and bond silos. The process determines how much of the portfolio should be allocated to "risky" assets within the overall investment policy. This approach and others like it are being utilized more due to the 2008 financial crisis and most recent COVID-19 market downturn. The three risk models also incorporate other strategy styles and signals that can complement one another across various economic environments and conditions.

The goal is to look at the market risk first and then make adjustments in the basket of investments and strategies utilized in the model. That basket of investments used is the same but the allocation to the riskier assets in the allocation changes depending on the absolute and relative momentum. This has produced a leveling of the returns and avoidance of the downturns because crash protection is built into the process. It is important to note that the crash protection and minimal historical drawdowns are not guaranteed, but rather active management that provides investors with an increased chance of positive returns.

Based on the model, Defender may be out of the market completely, partially invested or totally in the market. This is not a timing system but rather a rigorous discipline evaluating the relative valuations, comparing to other valuations, and making portfolio adjustments with the overall goal to reduce portfolio risk.

TFPG Capital Defender has been successful in generating comparable returns while reducing the risk. There are different levels of risk protection that can be implemented depending on how much downside or volatility the portfolio can support where investors can now choose between a moderately conservative allocation, a moderate allocation, or a moderately growth-oriented allocations.

The bottom line is this, TPFG Capital Defender Asset Allocation Series is built to help control the downside risk but still capture upside returns. This approach is valuable in many situations because it provides:

- A more predictable rate of return;
- Downside and crash protection;
- Better cash flow management because there is less volatility in the portfolio;
- Better ability to compound returns since the portfolio is not subject to large downturns.

A way to say how we believe the Defender Series works is a statement that has been attributed to Warren Buffet:

- There are two rules of successful investing
- Rule #1 – Do not lose money.
- Rule #2 – Do not forget the first rule.

The concept is to lose less whenever possible because you must produce a greater rate of return to get back to even. To recover a 20% loss takes a 25% return. Warren Buffet's approach to investments is long term value driven and has had periods of underperformance, but it is an opportunistic approach and buying when there is a difference in valuation and the price makes sense. The same holds true with the Defender approach but based on the differences between asset pricing movement.

Three Risk Based Choices:

Since there is not a one size fits all approach to every investor and situation, the TPFG Capital Defender Series now offers three risk-based choices with specific targets on returns and volatility.

1. **TPFG Capital Defender Series Moderate Conservative**
   a. Seeks downside protection and minimal account drawdown as the primary goal
   b. Targets 5%-6% annualized rates of return with a 6%-8% drawdown

2. **TPFG Capital Defender Series Moderate**
   a. Seeks downside protection and reduced account drawdown as the primary goal
   b. Targets 6%-8% annualized rates of return with an 8%-10% drawdown

3. **TPFG Capital Defender Series Moderate Growth**
   a. Seeks downside protection and moderate account drawdown as the primary goal
   b. Targets 8%-10% annualized rates of return with a 10%-12% drawdown

Assets & Hedge Options

The selected core asset classes, protection investments, and hedge options are as follows[1]:

Fund Name	Ticker	Morningstar Category
Asset Classes		
SPDR® Portfolio Emerging Markets ETF	SPEM	US Fund Diversified Emerging Mkts
Vanguard FTSE Europe ETF	VGK	US Fund Europe Stock
Franklin FTSE Japan ETF	FLJP	US Fund Japan Stock
SPDR® Portfolio S&P 500 ETF	SPLG	US Fund Large Blend
Invesco QQQ Trust	QQQ	US Fund Large Growth
Vanguard Real Estate ETF	VNQ	US Fund Real Estate
SPDR® Portfolio S&P 600 Sm Cap ETF	SPSM	US Fund Small Blend
SPDR® Portfolio Interm Term Corp Bd ETF	SPIB	US Fund Corporate Bond
SPDR® Blmbg Barclays High Yield Bd ETF	JNK	US Fund High Yield Bond
SPDR® Portfolio Long Term Treasury ETF	SPTL	US Fund Long Government
Invesco Optm Yd Dvrs Cdty Stra No K1 ETF	PDBC	US Fund Commodities Broad Basket
Aberdeen Standard Gold ETF	SGOL	US Fund Commodities Focused
Protection Assets		
iShares 7-10 Year Treasury Bond ETF	IEF	US Fund Long Government
SPDR® Blmbg Barclays 1-3 Mth T-Bill ETF	BIL	US Fund Ultrashort Bond
iShares 1-3 Year Treasury Bond ETF	SHY	US Fund Short Government
Hedge Options		
Simplify Volatility Premium ETF	SVOL	US Fund Large Blend
Quadratic Intrst Rt Vol & Infl H ETF	IVOL	US Fund Inflation-Protected Bond
Simplify US Equity PLUS Downside Convexity ETF	SPD	US Fund Large Blend
ProShares VIX Short-Term Futures ETF	VIXY	US Fund Volatility
Alternative Strategist Signals		
Kensington Dynamic Growth Fund I Share	KAGIX	US Fund Tactical Allocation
Counterpoint Tactical Income Fund	CPITX	US Fund Non-Traditional Bond

Overall, we believe this approach should provide opportunity to capture returns in upward trending markets through exposure to the risk asset classes along with capital preservation from protection assets. Also, the hedge options provide the prospect of improving returns during downward volatility. This approach is supported by strong academic research and has been thoroughly tested and analyzed.

[1]This is a representative list of options. The specific funds utilized for risk asset classes, protection assets and hedge options are subject to change from time to time at the investment manager's discretion.