South Atlantic Capital Management Group, Inc.
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All Weather Investing

-Edward Nowell, President

While downside protection may be a top concern for many stock investors, that's probably not enough. What many investors want is downside protection while also participating in up markets—an "all weather" portfolio. Shifting to very conservative holdings, such as cash, to ride out a market downturn can accomplish the goal of downside protection but can get in the way of the goal of participating in up markets. The technical definition for all weather investing would be positive asymmetric risk and returns, where the investment opportunity is unbalanced favorably towards the upside.

We feel investors need to recognize that their odds of capturing the long-term potential for capital appreciation is higher by staying invested through the downturns than by trying to time markets. All weather investing, where the downside is limited but you participate in up markets, can help investors achieve positive results through cycles since limiting the downside helps create the patience to stay invested.

One way to assess whether a fund or portfolio has positive asymmetric risks and returns is to look at its Overall Capture Ratio—Upside Capture divided by Downside Capture. For example, if the stock market (using the S&P 500 Index) rises 10% in a quarter and your portfolio rises 9%, that equates to a 90% upside capture. Similarly, if the market falls 10% but your investments only decline 6%, that would be a very good downside capture of just 60%. Thus, "overall capture" would equal 90% divided by 60%, or 150%.

South Atlantic Capital's overall capture ratio since our inception is compared below to the average broad market mutual fund. We think not just investing, but consistently investing in a risk averse way, has helped us achieve an asymmetrically positive overall capture ratio since January 1, 1992. We don't believe we would have achieved the same overall capture ratio by trying to time markets or forecast economic environments.

	Downside	Upside	Overall
South Atlantic Capital	56.9%	91.4%	161%
Active Large Cap Blend	101%	94%	93%

Source: PSN Informa and Morningstar (results through 12/31/21)

The Capital Group identified the following three traits that are common among funds that exhibited strong returns through complete market cycles:

Active Funds. By definition, passive funds replicate the return of an index. They capture 100% of the upside but also 100% of the downside so they provide no downside protection, while active funds have that opportunity through their stock selection.

Flexible funds that consider shifting between "growth" and "value" stocks for example, versus never investing outside a specific style box, have an opportunity to optimize results by having a larger investment universe to choose from. However, this can create risks if a fund manager invests too far afield from his circle of competence.

Higher yielding funds were found to provide more downside protection in an analysis of fund performance since 1993. Funds with the best downside protection (averaging 85%) had higher yields in all time periods studied.

The asymmetry of gains versus losses over time can be significant. Minimizing drawdowns means getting back to square one more quickly, and then moving ahead requires lower returns versus funds with less downside protection. This type of investing can also lead to lower volatility in your returns, thus helping to create the patience to remain invested through inevitable downturns.

Even if you are well invested for "All Weather," there are some important things to proactively take into consideration to prevail through market downturns by avoiding emotional mistakes.

- Try to accept that downturns are a natural part of investing and that they have been common but temporary. Since 1952, 20% downturns happen on average every 6 years or so and last 370 days. Although past events don't guarantee future results, the market has recovered from these downturns every time.

- Studies have shown people put too much emphasis on recent events, ignoring long-term realities such as the historical pattern where markets have recovered from every downturn.

- Measuring from the bottom of the market, the average return during the first year after downturns of at least 15% (since 1929) is a gain of 55%, and studies have shown it's very difficult to capture those returns by trying to time markets.

Sources: Capital Group, Rimes, Standard and Poor's (as of 12/31/21).

Mr. Nowell has over thirty-nine years of experience in the finance business. Prior to founding South Atlantic Capital, he worked in the leveraged lending department of Bankers Trust Company, New York as an Assistant Vice President. His primary responsibility was arranging bank financing for leveraged buyouts led by Kohlberg, Kravis, Roberts & Company and other leading private equity companies. During graduate school he interned with Merrill Lynch's Capital Markets Group in New York. Later he served as an institutional fixed income salesman for Carolina Securities/Prudential Bache Securities and worked with Fox, Graham, and Mintz Securities. Mr. Nowell graduated from the University of North Carolina with a B. S. in Economics and received his MBA from the University of Virginia.

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