

## Sanctity Capital Management

Your Solution to Profit and Peace of Mind  
Managed Futures/Options for Risk Management  
and Business Development

#39

### Benchmark Applications for SafeMoneyMetrics™

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This month we elaborate on how the Reward to Variability Ratio is used with SafeMoneyMetrics™ as IT'S ONE DRIVING Benchmark. The benefit is a focused simple method of defining and eliminating unwanted risk from the investment process.

#### Natural Laws and Risk Management

The greatest strength of SafeMoneyMetrics™ is that it is designed to produce results that closely align with universal principals that support all life. Specifically we believe that everything needed for prudent analysis is internal to the investment, rather than external to it. Risk management simply "flows" by itself at a vital level when we get out of the way. Since God or the creative Principal that sustains all life does a remarkable job – our attitude is to align our risk management strategy with eternal success and stay out of the way. As a filter SafeMoneyMetrics™ easily determines what investments should probably be avoided and it maximizes opportunity with any investment that we choose to be involved with.

#### Thunder of Silence – Joel Goldsmith

We discern that there is a creative Principle which produces Its own image and likeness, and that this creative Principle is also the sustaining Principle of life, and therefore Its creation must necessarily be of Its own essence – Life, Love Spirit, Soul this is the true nature of man.

When mankind learns to release all blocks to the presence of Spirit living within and through us, we become vehicles or forms for Its' natural expression. Everything needed to support ALL life is internal to and surrounds each physical creation. Man's interference with natural law causes unnecessary risk and weakness that eliminates itself once we realize that our beliefs are THE cause for and support life as we currently experience it.

Again, SafeMoneyMetrics™ is a risk management model that financially defines how a trader's talent, naturally expressed through their trading strategy

interacts with current market conditions. It never deviates from its original intention.

SafeMoneyMetrics™ defines, maximizes and monitors for potential profitability at minimal cost and risk under current market conditions.

#### The Initial Selection Process

Any and all advisors are initially selected by applying a few simple ratios to all data. It can be done by hand and the information is easily obtained from their disclosure documents and/or by asking a few questions. In previous articles we have already discussed the basic four ratios used for all analysis. ( see [www.sanctity.com/](http://www.sanctity.com/) Monthly Articles) For practical purposes their usefulness is briefly defined below.

#### Ratios we have NOT discussed are:

**Cost Ratio (CR):** Defined by a relationship between account costs relative to the Net or Funding Level Ratio. Traditionally costs are evaluated as a percent of fully funded account value annualized. We perceive that it is more accurate to evaluate costs relative to return and capital at risk. For example - traditionally one of the industry's greatest traders had a 20% cost factor. Looking at trading costs in isolation, anyone would inaccurately assume that his cost and risk was high. The trader earned over 100% annually on the fully funded account using 25% margin (Capital at risk). Now we "**see**" that he earned 400% on capital at risk and his costs were 20% relative to the 400% return or Net Ratio.

When someone says: "Gee costs are 9% that's high!" We now have a more accurate frame of reference for evaluation.

**Cost/MAS:** Annual cost to the account relative to the Minimum Account Size (MAS) accepted by the advisor.

**Cost/FLR:** Annual costs as a percentage of the annual return earned on cash used to fund the account.

**Cost/NR:** Annual costs as a percentage of annual returns earned on actual capital at risk.

**Minimum Acct Size(MAS):** Account size accepted by the advisor (Management fees are calculated on this account size).

**Funding Level %:** Cash used to fund an account expressed as a percentage of the Minimum Account Size.

**Margin Minimum%:** Margin used for trading expressed as a percent of the fully funded account size.

**Margin Funding%:** Margin used for trading expressed as a percent of actual cash funding an account.

We now see how traditional risk/return and cost analysis applied to a database of advisors perpetuated via electronic communication alone or within any investment presentation can be misleading. Since electronic communication can perpetuate error internationally at lightning speed – it can also be used to perpetuate increased accuracy – at lower cost and risk than what we are currently doing!

**Formulas we use throughout all analysis as previously discussed are:**

**Capital at Risk (CAR):** Represents only capital used to produce a return. NOT the account size an advisor asks for, or the funding level. CAR is the foundation for all ratios. Adapted for different situations, possibilities are actual margin requirements for each trade, a percent of total account capital expressed as a dollar value allocated to each trade or when evaluating monthly data the advisors maximum margin allowed for trading is usually a conservative number. CAR is also used to evaluate capital waste built into the investment. For example - assume we are evaluating two advisors each having a \$1M required account size. The advisor using the least amount of capital at risk to produce the highest realized return relative to the lowest volatility would probably be a better choice. Capital at Risk must be accurate for SafeMoneyMetrics to optimally function. A good question to always keep in mind is: What is the capital at risk formula being used for this analysis?

**Realized Ratio (RR):** Used to evaluate realized profitability relative to real capital used to produce the return. (Net Realized Profits / Capital at Risk Formula.)

**Volatility Ratio (VR):** Evaluates fluctuations of open trade positions relative to capital required to maintain the position. Wide fluctuations in the VR can indicate increased volatility and risk. (Open Trade Equity / Capital at Risk Formula.)

**Net Ratio (NR):** Quantifies the composite value of realized and open equity on actual capital at risk. High net ratios relative to low volatility ratios can indicate increased stability. (Realized Ratio + or - Volatility Ratio/ Capital at Risk Formula).

**Funding Level Ratios (FLR):** Realized, Volatility and Net Ratios are calculated using a formula representing the advisors minimum funding level rather than capital at risk. Account stability is indicated when the FLR is consistently below the NR, especially when the difference is wide. Leverage is too high when the NR begins to fall into and below the FLR. To hide volatility some advisors ask for excessive account sizes - charging management fees

on the entire account while using only 5 or 10% of total assets for trading.

## Overview

Performance trends and potential actions are defined by quantifying relationships between ratios in current reality relative to past performance data over time frames. The entire model takes in daily investment data for each client account, transforms it into Ratios and applies it to time frames. Every client account is monitored daily as Today, 7, 21, 28 day then 3, 6, 9, and 12 month time frames relative to monthly data for the advisor or strategy they are using over 3, 6, 9, 12, 18, 24 and 36 months. Because the average maximum and minimum for all times frames consistently move forward in time, the past and current reality “flow” with each other rather than remain annualized and separated.

The model (95% completed) is built so as data is taken in, it can be analyzed as a composite portfolio, then information filters to each advisor within the composite and when necessary each market traded by each advisor. Nothing deviates from the initial process.

Every client has “private label” risk management for their account and can request their SafeMoney analysis during variable time frames. Monthly weekly, or daily reports are a standard. The risk management service and fee schedule is described in our new disclosure document at [www.sanctity.com/](http://www.sanctity.com/) disclosure document. I’m 88% comfortable saying that by mid next month the first version of our automated model should be completed and a demonstration will be available at [www.safemoneymetrics.com](http://www.safemoneymetrics.com) and [www.sanctity.com](http://www.sanctity.com) I’m 1000% comfortable saying that the model will evolve over time.

## Benchmarks and Their Purpose

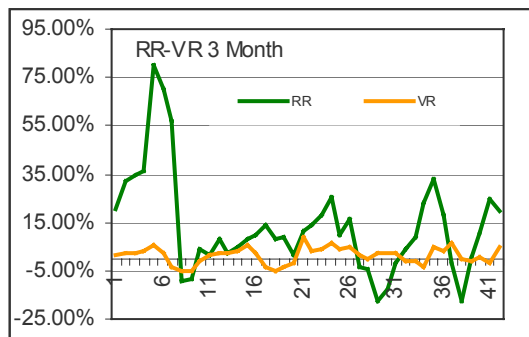
The ONLY ONE “Ratio” consistently living through all data driving the analysis is our version of a Reward to Variability Ratio (RVR). The exact process is computed for the composite portfolio, each advisor within and probably for each market within each advisor. Everything then filters into the 51% rule (a separate excel file).

Level ONE is the advisor RVR in current reality to past data and Level TWO is the client account to the composite strategy or advisor. Nothing else matters for now so monitoring several hundred accounts even with multiple advisor strategies becomes easy within a master file!

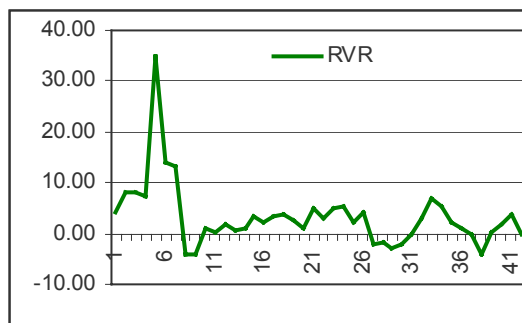
SafeMoney Reward to Variability Ratio (SMRVR) estimates the capability to produce realized profits with respect to managing the risk of open trades. Traditionally the RVR is calculated by dividing the Risk Premium (RP is a return above the risk free

ROR) by the Standard Deviation (SD) of returns. Since SD measures volatility and RP risk premium the result is a risk/reward ratio. We divide the RR by a SD of the Volatility Ratio. (RR/SDVR) – A high number indicates lower risk.

Two graphs below PROVE that ONE Reward to Variability Ratio serves THE basic purpose for monitoring an ever-changing relationship between the Realized and Volatility Ratios, THE two essential ingredients of our risk management process.



Above is the Realized and Volatility Ratios over three month time frames. Below is only the RVR during the same time frames. As the RVR increases one of two things are happening, either volatility is decreasing relative to realized returns or realized returns are increasing relative to volatility. The opposite is also true, as the RVR decreases realized returns are lower and or volatility is higher.



When the RVR for TODAY reaches a specific level relative to the maximum or minimum over time frames used for a particular strategy, each advisor within the composite is evaluated to see how the investment can be rebalanced. Rebalanced for us is also simple

1. Distributing profits
2. Moving profits from one advisor to another
3. Increasing or decreasing leverage or
4. Replacing an advisor

Profits are proportionally moved two ways – 1) aligned with the original allocation or 2) by reevaluating the current mix until the new composite produces the maximum RVR – Capital is then allocated relative to the new proportions.

Unless a client has reason to drive the decision process – it is driven by how the ratios are positioned and the 51% rule.

Determining the quality of risk/return in current reality is evaluated by looking at the Standard Deviation “trend” of all ratios. Also if the Net to Funding level ratios remains wide risk is low – if the Net ratio is falling relative to the funding level ( the difference narrows) risk is increased. Leveraged should be decreased and profits probably taken.

*Happy Spring!*  
*We Pray for Peace From Within for Every*  
*Individual*

Services offered by  
Sanctity/SafeMoneyMetrics.

**Kim Hunter** – editor of Risk and Reward magazine is also a Freelance Writer. – She is available to write about SafeMoneyMetrics™ for print and electronic media. Based in London Kim’s skills are exceptional for people interested in communicating the benefits of SafeMoneyMetrics™ Risk Management Services to the International and Institutional marketplace. My esoteric state of consciousness, incorrect grammar and excessive wordiness is automatically removed from the writing, allowing SafeMoneyMetrics™ to reach a larger international audience.

Kim’s first article on SafeMoneyMetrics™ was published in Risk and Reward Magazine. You can access the magazine FREE at [www.fow.com](http://www.fow.com)

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**For Hedge Funds of Funds** – In conjunction with the industry’s most prominent traditional trading managers we build and manage dynamic managed futures and options strategies. Because SafeMoneyMetrics™ is integrated into every aspect of the service. Our composite efforts offer less risk than what ANY traditional resource alone can probably provide.

**For Broker Dealers, Banks and Other Financial Institutions** Sanctity/SafeMoneyMetrics™ will design and support profit centers for broker-dealers, futures commission merchants or any group interested in managed futures and options. The process begins with management and filters into a vigorous marketing strategy for advisors and educational process for clients of each participating advisor. Compensation is negotiable and includes revenue sharing or annual retainer paid monthly. Broker-dealers and other institutions may be exempt from registration if managed futures are under 10% of their gross revenues. ALL RISK MANAGEMENT

MARKETING AND CLIENT EDUCATION STRATEGIES  
INCLUDE SAFEMONEY METRICS.

**For Traditional Financial Advisors or Introducing Brokers** – we act as Risk Managers and General Partners for private label limited risk partnerships beginning at \$500,000.

**For Trading Advisors** –SafeMoneyMetrics™ can be offered as a third party risk management and marketing strategy. Trading Advisors have no out of pocket costs. We can be compensated by the client or FCM sponsoring your services.

**For Electronic and Print Media** - SafeMoneyMetrics™ designs investment models teaching prudent integration of managed futures into other alternative investments and a traditional portfolio. Services can be supported with monthly articles, research and simple ratios on a data-base of advisors.

**For National and International Commodity Exchanges and Associations** - SafeMoneyMetrics™ can be integrated into managed futures and options marketing. Services can be offered through the exchange as a benefit to clearing member firms and their clients.

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