Passive
Capital Management

Why "Passive?"

The name of our firm often causes a moment of confusion for those learning about us for the first time. We frequently hear the question "why ***Passive*** Capital Management? Wouldn't I want ***active*** management of my precious financial resources?"

Often the name is associated with excessive risk aversion, or a slow and steady **"hare and tortoise"** approach to investing. We do pay significant attention to risk – knowing that it is the inherent flipside of the coin when it comes to returns. We also see investing as a long term process. However, **neither of these characterizations accurately reflects what we mean by a "passive" approach to a successful investment experience.**

The activity that generates investment returns takes place in fields and factories, in corporate headquarters and R&D laboratories. The activity that generates investment returns takes place in the **boundless imaginations of entrepreneurs, and in the work ethic that has built the modern world** over hundreds of years of human enterprise.

Activity in brokerage houses and investment firms, on the other hand, generally **has one purpose – to generate revenues for those firms.** Even well-intentioned activity by money managers can **substantially erode the value created by the activity of entrepreneurs and managers, designers and skilled workers.** Consider this fact – each year, **more than 70%** of the highly talented, highly trained, highly motivated portfolio **managers of mutual funds fail to meet their relevant benchmark** (source: S&P, Morningstar). This means that, year in and year out, **activity by money management professionals** (stock picking or market timing) **dilutes the value created by the activity of participants in the capitalist enterprise.** Capitalism can be diagrammed simply as follows:

Unfortunately, the experience of participating in capitalism for many investors can be diagrammed as follows:

The term **"passive" essentially means avoiding the <u>subtraction of value through adverse manager activity.</u>**

The particular **“active” behaviors that we avoid** are as follows:

- **Picking individual stocks** that are expected to outperform (and thus risking potentially spectacular underperformance);
- **Churning a portfolio** in pursuit of outperformance (and thus guaranteeing greater transaction costs and taxable events);
- **Selecting a star fund manager** based on past performance or rumors of ability (and thus rolling the dice on whether he or she will be in the 30% delivering or beating market returns that year);
- **Predicting the future** and making directional bets based on guesses or hunches (and suffering the consequences of what amounts to off-track gambling).

There is plenty of activity in our investing model. We provide investors with access and exposure to all the hurly-burly **activity of capitalism** around the globe**.** We are highly active in our **responsive customer service** and **our attention to the specific needs of each client,** including tax considerations, the complex needs of multi-generational client families, and the operating needs of our nonprofit clients. We are active in **educating clients** about their portfolios and objectively assessing their investment opportunities and returns outside of our firm.

We are active in **controlling what we can control** – asset allocation, costs, diversification, tax efficiency and discipline.

We are **“passive” in that we avoid the potentially destructive active money management behaviors** outlined above, and in that we choose to execute our investment philosophy using **funds that are, in turn, passively managed. This means that they provide thorough, broadly-diversified and consistent exposure to global asset classes**, with minimized annual costs and turnover and maximized tax-efficiency. **Index funds, asset class funds (ACFs) and exchange-traded funds (ETFs)** are examples of products that serve us and our clients in this way. We are authorized to build portfolios using asset class funds from Dimensional Fund Advisors.

The chart below summarizes the differences between a passive and an active approach.

Passive Management	Active Management
Understands that capitalism creates market returns, which are attractive when captured consistently and in their entirety.	Believes that investment managers create returns, and attempts to “beat the market” with stock picks or market-timing decisions.
Delivers market returns through low-cost fund vehicles used throughout an appropriately allocated portfolio.	Advertises the “latest and greatest” product expected to outperform.
Sets an appropriate strategic asset allocation, depending upon individual risk tolerance and return objectives, that will serve the client in all market cycles.	Attempts to make tactical directional bets on predicted market movements.
Keeps costs as low as possible to return as much as possible to the investor.	Increases costs when there is periodic outperformance, in the hope of returning more to the investment firm and its shareholders.
Controls the controllable – asset allocation, costs, diversification, taxes and discipline.	Attempts to control (or predict) the uncontrollable – global markets, company performance, unexpected macro events.
Understands that a disciplined investment philosophy and thoughtful asset allocation drive portfolio returns.	Believes that products and managers drive portfolio returns.

We look forward to talking with you about how the professional advisors at Passive Capital Management can help you to have a successful investment experience.

Passive Capital Management, LLC
2328 West Joppa Road, Suite 120, Lutherville, MD 21093, 443-275-2703
Two Clinton Square, Suite 215, Syracuse, NY 13202, 315-478-3130
www.passivecapital.com
A registered investment advisor