

SHELTER FUND: ROLLER COASTERS AREN'T FOR EVERYONE

When Paula Wieck looks at the stock market, she doesn't just see numbers on the ticker and data pouring in. She sees people. "The market can be quite a roller coaster," Wieck said, "a roller coaster driven almost entirely by human emotion."

For Wieck, studying the human behavior that drives the markets is the most interesting part of managing portfolios. Human behavior not only influences how the markets look on a day-to-day basis; it can often determine just how successful investors may be. Whether they reach their financial goals is not always about the performance of a fund, or the stock market as a whole. Often, it's about whether investors stay put as the market turns.

The study of human behavior in investing is known as behavioral finance, a subject in which Wieck, a portfolio manager at CLS Investments, has significant expertise. (CLS is currently conducting a firm-wide study into the ways in which behavioral biases impact investing.) Biases, such as recency bias (believing what has happened recently is likely to continue) or overconfidence (after a string of good luck), typically lead to poor investing decisions. Other human emotions, such as the fear of missing out and loss-

aversion, lead to chasing performance: buying when stocks are popular (overpriced) and selling when they've hit a bad news cycle (underpriced).

Emotional investors — those who can't stomach the market's highs and lows — are most susceptible to these behavioral biases. At CLS Investments, Wieck manages a fund, in partnership with portfolio analyst Gene Frerichs, designed specifically for these emotional investors. Founded in 2009, the AdvisorOne CLS Shelter Fund is a protection-focused fund that attempts to adjust the amount of market risk it assumes in line with the ups and downs of the marketplace. That means if the market declines, the risk adjusts accordingly. Importantly, the fund seeks to ensure investors stay invested for the long haul.

"We can tell investors over and over that it's not a good idea to leave the market," Frerichs said. "But if they are very loss-averse, they won't want to stay in." We believe loss-averse investors would prefer to miss out on gains than suffer losses, so the Shelter Fund seeks to limit the impact of large equity market declines. Frerichs uses an example he recently heard from Nick Arreola from Creighton University, who is working with CLS on the behavioral finance study. Two clients: one gains \$50 from her investment; the other gains \$100 and then loses \$50. They both end up with \$50, but their emotional experiences are very different. "While logically we know the results are the same," Frerichs said, "clients who suffer a loss have a negative emotional experience. By providing a systematic way to react to market downturns, the Shelter Fund seeks to help investors who have a stronger emotional reaction to losses, helping them ride out periods of market loss and participate in periods of market gains."

Frerichs has worked in performance reporting for more than 10 years. He said he's seen the impact of clients moving in and out of the markets over the years

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by studying the data of their returns. "We see it over and over again," he said, "clients hurting themselves by exiting the market at a low point and not getting back until after a recovery."

The fund is rules-based, so it's a great fit for Frerichs, who has been part of the team involved in behind-the-scenes technical work on the fund since its beginning. "Gene is such a deep, analytical thinker," Wieck said. "He understands all the intricacies of reporting performance because he developed the techniques. So he adds a lot of value."

Wieck's background is in nutritional science, which she says has given her a unique understanding of behavioral finance. She says people are driven by emotion, not rationality, when it comes to healthy living, just as they are in investing. "People know they should eat less and exercise more, but do they do it?" she said. "Not always. Most people know they should save more and spend less, but they don't always do it."

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The Shelter Fund attempts to help investors overcome those emotions and stay disciplined. Instead of getting spooked and pulling their funds into cash, investors in the Shelter Fund are offered a step-by-step process that seeks to move them away from market volatility, while keeping them invested. Wieck said, "Basically, the Shelter Fund seeks to provide a way for emotional investors to stay invested."



Paula Wieck, CFA
Portfolio Manager



Gene Frerichs
Senior Performance Analyst

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