

What We Do: Portfolio Construction and Management

LPL Financial Research

Investment Philosophy

LPL Financial Research is an opportunistic, all-market, all-weather due diligence provider and portfolio manager. Through our investment and portfolio recommendations, we aim to avoid downside and capture upside. To this end, we are conservative when markets are tough and aggressive when they are rising. Though a very broad investment mandate, we believe this is the only way to effectively provide recommendations for our advisors and their clients.

The Portfolio Strategy Group within LPL Financial Research is responsible for the construction and management of all recommended portfolios that the team offers. It lies between the top-down macro idea generation machine that is the Investment Strategy Group and the bottom-up due diligence implementation experience of the Manager Strategy Group. Portfolio Strategy is charged with combining the best ideas at each end to create recommended portfolios that regularly beat their respective benchmarks and meet their specific mandates.

To accomplish this goal, the Portfolio Strategy Group has developed its own set of proprietary tools and processes for portfolio construction and management. There are two main facets of the Portfolio Strategy process: construction through combination analysis and management through dashboard analysis.

Portfolio Construction Through Combination Analysis

When viewing an overall portfolio, its characteristics and behavior are more important than any one of the individual pieces of which it is comprised. This is the most important concept in portfolio construction. In building portfolios, the Portfolio Strategy Group heavily leverages Manager Strategy analysts to understand and track manager biases. We believe that even the best managers exhibit biases such that they perform in certain ways during different market conditions. When we have a strong understanding of which factors drive performance and are confident they can persist, we can then combine managers to exploit opportunities we see in the market and create robust combinations that we believe can outperform in numerous market environments.

A key instrument utilized in this process is the Scenario Attribution Tool (SAT), which LPL Financial Research has developed in order to assist in this endeavor. It has the power to combine different return streams of individual and combinations of investments to determine which arrangement makes the most sense for the market environment we expect, as well as help to determine what margin of safety we might have if our predictions are wrong. Collaboration and the right tools are integral to mastering this process.

Portfolio Management Through Dashboard Analysis

There is then a high degree of monitoring the portfolios once they are constructed. Portfolio construction helps us buy and dashboard analysis helps us track what we actually bought and now own. The goal is to have a deep understanding of what the portfolio holds, what external factors it is exposed to, how explicit risks are being rewarded by the market, and what implicit risks are being taken for which we need to watch out. The Portfolio Strategy Group has developed a series of dashboards that address each of these aspects individually.

- **Daily Performance Report Dashboard:** Monitors relative performance
- **Excess Return Dashboard:** Determines rolling excess return trends



Dashboards

A car has many moving parts and numerous data points that can be conveyed to its driver, but a car's dashboard only has a few of the most relevant gauges on which the driver needs to keep a constant eye. This is a particularly appropriate analogy to the dashboard analysis conducted on the portfolios which we manage.

- **Holdings Asset Level Dashboard:** Monitors our allocations to underlying model holdings in dollars
- **Model Dashboard:** Provides a snapshot of our positioning
- **Positioning Dashboard:** Tracks our underlying holdings
- **Return-Based Factor Exposure Dashboard:** Examines breadth of returns-based factor exposures
- **Risk Dashboard:** Determines our overall risk stances relative to market conditions
- **Roll-Off Dashboard:** Highlights the figures that are rolling off our rolling performance figures
- **Universe Dashboard:** Compares our models versus the universe
- **Valuation Dashboard:** Details how valuations are trending

A car has many moving parts and numerous data points that can be conveyed to its driver, but a car's dashboard only has a few of the most relevant gauges on which the driver needs to keep a constant eye. This is a particularly appropriate analogy to the dashboard analysis conducted on the portfolios which we manage. From what drives the markets to how a portfolio is behaving, there is no shortage of data. However, the LPL Financial Research team has spent considerable time in determining which of those data points are the most important, and then creating a system to constantly watch how these factors are progressing, and finally establishing at which points action is required. This process starts with the Investment Strategy Group to identify opportunities in the market and ends with the Portfolio Strategy Group tracking these prospects in the models.

Putting the Pieces Together

When the final puzzle of portfolio construction and management is put together, one can see that it is made of very specific proprietary tools and dashboards created by LPL Financial Research, it leverages the collaboration of all groups within the department, and it is overseen by a team whose goal is to consistently deliver a substantial amount of excess return over time with no surprises.

IMPORTANT DISCLOSURES

The opinions voiced in this material are for general information only and are not intended to provide any specific advice or recommendations for any individual. To determine which investment(s) may be appropriate for you, consult your financial advisor prior to investing.

Past performance is no guarantee of future results.

There is no assurance that the techniques and strategies discussed are suitable for all investors or will yield positive outcomes. The purchase of certain securities may be required to effect some of the strategies. Investing involves risks including possible loss of principal.

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