Wealth Enhancement®

10 Rules for Fund Selection

By Michael McKeown, CFA, CPA - Chief Investment Officer

May 16, 2023



Congratulations. You are now a portfolio manager.

There was a shift away from pension plans decades ago. Previously, an investment committee managed all aspects of a portfolio for pensions. Today, everyone with a company retirement plan became responsible for deciding how to invest.

In addition, with social media today and the TikTok generation, there is a daily onslaught of new stories and “influencers” pitching products or strategies. In real

Advisory services offered through Wealth Enhancement Advisory Services, LLC, a registered investment advisor and affiliate of Wealth Enhancement Group®.

life, a contact may forward you a pitchbook on an idea that is supposedly the next amazing investment.

Having an approach that filters through this noise is a necessity. When one does not see ideas that often, a scarcity mindset creeps in that this could be the one can't miss idea.

Our research team sits in a fortunate position that allows us to canvas the capital markets, looking for ideas. This covers a range of asset classes – public equity, real estate, private equity, fixed income, and more. We look across regions, sectors, and strategy types. Of course, any firm raising capital is happy to take our call. Filtering through the ones we receive is a process.

Before we get to the rules, there is a major first step. The big step is constructing a portfolio that aligns with your future aspirations and liabilities. This means analyzing scenarios in a financial plan to determine your North Star for your target asset mix between stocks, bonds, and alternative investments. Then putting in place the guardrails around asset classes and rebalancing policy. Without this process, selecting funds puts the cart before the horse.

Back to the task at hand. Here is a short and non-exhaustive list of how to analyze a fund.

1. **Managers only get credit for risk-adjusted outperformance.** Beware of whether the right benchmarks, time frames, and peer groups are used for analysis.
2. **Make sure the outperformance is diversified over time.** No "one-hit wonders" on a sector or stock.
3. **Team-based** systems over a star approach.
4. **Understand potential taxes.** Net after-fee, after-tax is what matters.
5. **The firm and strategy must align with our goals.** Incentives matter. This sounds obvious, but the incentives, structuring, time horizon, and fees can easily be misaligned.
6. **Operational due diligence is stellar.** Use only a verified track record. Funds should have best-in-class service providers.

Advisory services offered through Wealth Enhancement Advisory Services, LLC, a registered investment advisor and affiliate of Wealth Enhancement Group®.

7. **The size of the fund is appropriate.** Raising too much capital can overwhelm an asset class or a manager's strategy. Too little capital can be a detriment to scale.
8. **Opportunity set is attractive today.** We all know the disclosures that past performance is not indicative of future results. Analyze how today's prices and market compare to the past.
9. **Fees are fair.** Understand the market pricing for this asset class and be sure it is in line.
10. **Know the downside just as much as the upside case.** If we understand the risks as well as we do what can go right, then we may be confident there is a margin of safety.

I like to ask, "Why am I so lucky?" How did this idea come to our team out of so many other people that were possible?

If you don't see a dozen pitches daily, every day of the work week for the last 15 years, getting one in your inbox may look interesting. From real estate deals to venture funds, from ETFs, to a "new" income fund, we see a lot of investment pitches.

But it also makes it easier to say "no" because we do it so often. And we follow our investment principles, strategy, and process, and invest time before any dollars are ever allocated.

Important Disclosure Information

Advisory services offered through Wealth Enhancement Advisory Services, LLC, a registered investment advisor and affiliate of Wealth Enhancement Group®.
Past performance does not guarantee future results. Different types of investments involve varying degrees of risk, and there can be no assurance that the future performance of any specific investment, investment strategy, or product or any non-investment related content, made reference to directly or indirectly in this communication, will be profitable, equal any corresponding historical performance level(s), be suitable for your portfolio or individual situation, or prove successful. Certain strategies and vehicles referenced in this communication, such as private investments, Opportunity Zones, and ESG investing, may present increased or novel risks, including potentially higher management fees, reduced liquidity, shorter performance histories, or increased legal or regulatory exposure, compared to

more traditional publicly traded securities and investment strategies. All investors should consider these potential risks in light of their individual circumstances, objectives, and risk tolerance. Due to various factors, including changing market conditions and/or applicable laws, the content may no longer be reflective of current opinions or positions. Moreover, you should not assume that any discussion or information contained in this commentary serves as the receipt of, or as a substitute for, personalized investment advice from Wealth Enhancement. The asset allocations reflected in this communication are targets only. Actual allocations can and often will deviate from these targets, including in instances of volatile markets, large deposits or withdrawals, or during account rebalancing.

Historical performance results for investment indices, benchmarks, and/or categories have been provided for general informational/comparison purposes only, and generally do not reflect the deduction of transaction and/or custodial charges, the deduction of an investment management fee, nor the impact of taxes, the incurrence of which would have the effect of decreasing historical performance results.

Not all services described herein will be necessary or appropriate for all clients. The scope of the services to be provided depends upon the needs of the client and the terms of the engagement. The potential value and benefit of the adviser's services will vary based upon a variety of factors, such as the client's investment, tax, and financial circumstances, and overall objectives. Neither personalized services nor financial or professional resources or processes should be construed as a guarantee of a particular outcome. All investing comes with risk, including risk of loss.