PAC INSIGHTS

PAC Insights is Park Avenue Capital's monthly commentary exclusively for our clients. This commentary is designed to provide you with digestible take-aways that offer perspective on the market, but always in the context of long-term financial planning.

This month's topic: **Investment Tenets - Simplicity, Transparency and Control.**

QUICK HITS

- There are three core investment implementation tenets that anchor Park Avenue Capital's investment philosophy: **simplicity, transparency, and control.**

- **Simplicity**: Our approach centers around owning a globally diversified equity portfolio across different size companies using 9 index-based ETFs.

- **Transparency:** Complex vehicles often have additional fees such as (but not limited to) upfront fees, performance fees, and leverage costs. In our role as fiduciaries to your financial success and portfolios, transparency is non-negotiable.

- **Control:** Our focus on core asset class Exchange Traded Funds (ETF)s provides us control over costs, taxes, and risk exposures. Core ETFs are the most affordable way to access the markets without taking individual security bets.

Investment Tenets - Simplicity, Transparency and Control

The investment landscape is cluttered with complexity and opacity driven by an industry that profits from investor anxiety. We challenge this status quo.

There are three core investment implementation tenets that anchor Park Avenue Capital's investment philosophy: **simplicity, transparency, and control**.

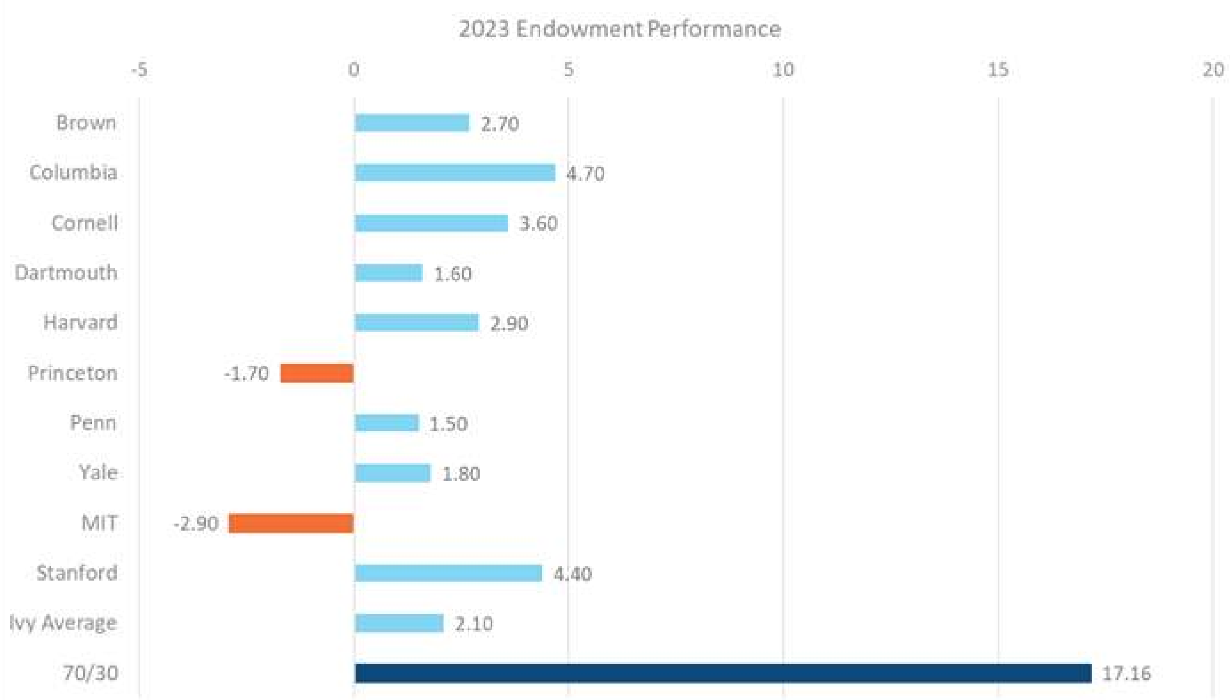
We referenced these tenets in our 2023 year-end letter:

> "Human beings are inherently wired with a survival-based decision process that does not lend itself to making sound investment decisions. The media thrives on generating content designed to stimulate those synapses, because fear ridden consumers stay engaged with advertisers. The financial community thrives when consumers are scared because profit centers like complex products promise you can have your cake (equity-like returns) and eat it too (muted volatility). If the

media's core message was to keep things simple, transparent and stay invested, would investors care as much about the headlines?"

This philosophy is supported by compelling data from the institutional investment community. Probably the best proxy for measuring the success of a complex portfolio approach is an honest look at the performance of the endowment community. Many universities have in recent years adopted the "Yale Model", which dedicates most investments to private market strategies.

Most major endowments had a terrible fiscal year ending in 2023, even in light of the outstanding performance of global stocks (as measured by Vanguard Total World Stock Index – VT) - a notable 22.02% in 2023. Some highlights:



Source: Bloomberg and Markov Processes International. 70/30 portfolio represented by 70% Vanguard Total World Stock ETF and 30% iShares Core U.S. Aggregate Bond ETF.

As you zoom out, five -year average endowment returns significantly underperform liquid benchmarks on a pure return basis and does not even consider:

- Daily liquidity vs significant lock-ups.
- Knowing exactly where you stand each day vs not at all.

- Doing that all with a cost structure of 0.07% vs a heck of a lot more than that.
- No leverage vs a lot of leverage. Most private investments have significant leverage involved in generating returns.

There is a high barrier of entry for an investment to be included in your portfolios. Our approach is underpinned by the belief that planning and behavior, not product or security selection, drives real-life investment outcomes, emphasizing the need for a disciplined straightforward investment strategy.

Simplicity

The investment management industry often promotes complex products and services. Many advisors take the easy path—they pander to clients' emotions with products designed for the market concern of the day. Unfortunately, this approach often results in more expensive portfolios that are packaged with more risk than commonly understood.

It is common to see portfolios from our competitors with 200+ unique holdings where security selection, not financial planning, is the focus. We consistently see investment products in client portfolios that use leverage or derivative contracts to try and enhance returns. Active management is still central to portfolios despite studies like Morningstar's Active/Passive Barometer showing that the probability of long-term outperformance is less than a coin flip.

The industry doubles down and designs complex products that create the illusion you can have high returns, diversification, and low volatility all at once – the proverbial free lunch. Plus, add to that hundreds of pages of monthly portfolio activity and voluminous annual tax reporting (we just reviewed one from a competitor that was over 2,000 pages long!).

Our approach centers around owning a globally diversified equity portfolio across different size companies using 9 index-based ETFs. We can explain each investment we own in the portfolio with a sentence or two. While many advisors may advocate for complexity, we believe that simplicity is the ultimate solution for sophisticated investors.

Transparency

In our role as fiduciaries to your financial success and portfolios, transparency is non-negotiable. Our implementation is grounded in clarity.

Complex vehicles often have additional fees such as (but not limited to) upfront fees, performance fees, and leverage costs. Compare this to our global equity ETF portfolio which has an expense ratio of 0.10%.

Control

Our focus on core asset class Exchange Traded Funds (ETF)s provides us control over costs, taxes, and risk exposures. Core ETFs are the most affordable way to access the markets without taking individual security bets.

Additionally, ETFs offer a distinct advantage over actively managed mutual funds due to their more favorable capital gains tax structure. Unlike mutual funds, ETFs do not have to pass realized capital gains to shareholders. Through persistent recent outflows, many mutual funds have been forced to liquidate holdings to meet redemptions, causing unfavorable (and often unnoticed) taxable gains.

Finally, we do not outsource investments to third party managers. Should we have a long-term market view (for example, an overweight to U.S. stocks vs. global), we can express marginal allocation tilts through low-cost ETFs. This ensures that we understand all risk exposures in the portfolio and have control over them.

CONCLUSION

The investment industry profits from prognostication, especially in times of crisis. Selling a product in response to a market crisis is not a philosophy; it's a sales pitch. We believe the superior behavioral investor will most likely outperform a reactive approach.

Behavior is the primary driver of real-life investment outcomes, and our investment philosophy is grounded in probabilities and sound decision making over the long-term. The end result is a portfolio that lives in service of the plan and is ultra-competitive in the marketplace.

- The Park Avenue Capital Team

Appendix

Common examples that do not meet our three tenets.

Private Equity. Many private investments clearly state in their offering documents that there is a lack of transparency in the investment vehicle. Because of the complex product structure, investors will not have clear visibility into the underlying investments.

Private Equity, (and related investments like Venture, Private Credit, and Private Real Estate) typically have either hard lock ups or limited redemption periods/amounts. Additionally, these products are subject to capital commitments, where cash is needed to fund the investment with limited advance notice. This cash tends to sit on the sidelines in short-term fixed income instruments as it waits to get called into these products. Cash and short-term instruments that are waiting to be called to fund the private investments also results in cash drag within the portfolio. Private investments might meet client objectives but at the retail investment offering level, however, the challenges are more pronounced.

Liquid Alternatives. Many liquid alternative funds were created as a reaction to the 2008 financial crisis, promising to protect investors' portfolios, while capturing asset flows that would otherwise go to cash. However, they fail to deliver meaningful returns over the long-term. Liquid alternative funds tend to outperform equities in down markets by holding lower equity exposure and exhibiting less volatility, which results in the suppression of long-term returns as required by the planning framework. However, correctly timing entries and exits is crucial for the long-term success of liquid alternatives, which significantly decreases the probability of favorable outcomes.

The planning framework should inform the stock to bond mix for every client, and therefore, any further reduction in volatility deviates from the plan.

Structured Products/Notes. Structured notes are financial products that are often sold to a client as an investment that provides exposure to a basket of equities, an equity index, commodities, or currencies while claiming to protect on the downside. The complexity of these offerings is daunting, and include such concepts as participation rates, caps on returns and knock-in features. Even seasoned investment professionals have a difficult time deciphering returns or implications. These products cater to emotionally anxiety around volatility, and individuals lacking a well-articulated financial planning framework are prime candidates for their implementation.

Bitcoin. Bitcoin is neither simple nor transparent. We do not see it meeting our hurdle for portfolio consideration.

Unlike any other investment we can think of today Bitcoin requires unrelenting marketing and promotion to acquire interest. Its short history relative to traditional core assets like stocks and bonds fails to meet any standard for currency, store of value or a claim on earnings or future cash flows.

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Exchange traded funds (ETFs) have risks and trade similar to stocks. Shares of ETFs are bought and sold in the market at a market price, as a result, they may trade at a premium or discount to the fund's actual net asset value. Investors selling ETF shares in the market may lose money including the original amount invested.

With fixed income securities, such as bonds, interest rates and bond prices tend to move in opposite directions. When interest rates fall, bond prices typically rise and conversely when interest rates rise, bond prices typically fall. This also holds true for bond mutual funds. When interest rates are at low levels there is risk that a sustained rise in interest rates may cause losses to the price of bonds or market value of bond funds that you own. At maturity, however, the issuer of the bond is obligated to return the principal to the investor. The longer the maturity of a bond or of bonds held in a bond fund, the greater the degree of a price or market value change resulting from a change in interest rates (also known as duration risk). Bond funds continuously replace the bonds they hold as they mature and thus do not usually have maturity dates, and are not obligated to return the investor's principal. Additionally, high yield bonds and bond funds that invest in high yield bonds present greater credit risk than investment grade bonds. Bond and bond fund investors should carefully consider risks such as: interest rate risk, credit risk, liquidity risk and inflation risk before investing in a particular bond or bond fund

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Forbes Best-In-State Wealth Management Teams (1/12/2024), Data provided by SHOOK ® Research, LLC – Data as of 3/31/23. Forbes "Best-in-State Wealth Advisors" list (April 2023), Research and ranking provided by SHOOK Research, LLC. Based upon data as of 6/30/2022. Forbes Best-in-State Top Financial Security Professionals list (July 2023), Research and ranking provided by SHOOK Research, LLC. Based upon data as of 12/31/2022. Barron's 2024 Top 1200 Financial Advisors (3/21/2024). Northwestern Mutual (NM) and its advisors do not pay for placement on 3rd party rating or ranking lists. NM and its advisors do, however, pay marketing fees to these organizations to promote the rating or ranking(s). Rankings and recognitions are no guarantee of future investment success.