Building and managing your investment portfolio

After we have worked together to develop an appropriate asset allocation, it is time to start building the portfolio. Based on your allocation we will start to build out each asset class. With $100,000 or more to invest in individual stocks, we believe this is a great method to build and manage a portfolio. In our opinion investing is simple: we rely on the following principles, although each one has many layers of depth:

- Don't put all your eggs in one basket (diversify)
- Buy Quality
- Pay a fair price (Don't overpay for a company that is "too popular")
- Be willing to hold for a long time (Find companies that you think can endure)
- When a stock drops, find the facts and then face the facts (Buy more, hold or sell)
- Realize investing is a lifetime endeavor; hope prices drop after you buy (so you can buy more at a lower price)

Building a portfolio:

In addition to allocating assets based on your goals and objectives, combining Large-cap, Mid-cap and Small-cap companies, diversify portfolios among 8-10 industry groups, so you are not too heavily weighted in any one sector, while having representation in most industries. I do not necessarily mirror the S&P 500 allocation in portfolios that I manage, and maintain an awareness of why we are over or underweighted in any specific industry relative to the S&P.

Managing the buy and sell process:

Sometimes I will want to add companies that are trading above what I wish to pay for them. Therefore, I may wait to add them to the portfolio until they are at a more reasonable price. In managing your Stock Portfolio, I generally start reducing your position as the price increases, i.e. up 100% sell 1/4 - 1/3. To help manage risk and maintain a reasonable position size.

Number of holdings:

For example with a $100,000 individual stock portfolio, you will want to consider investing in 20 companies +/- @ $5,000 (average) per position diversified in a minimum of 8 industries, with no more than 10% ($10,000) in any one position or 25% ($25,000) in any one industry. For larger portfolios, you'd consider increasing the # of companies and position size.

Equities (Stocks)

Large Cap

- While the Diversified Stock Income Plan (DSIP)* is a separate firm program, I will use the DSIP (see DSIP, Dividend Stock Income Plan) list in constructing the core holdings in your portfolio. I will choose 10-25 of these companies depending on the size of your portfolio. The larger the portfolio, the more companies will be added.
- Around this core I will add additional companies for diversification that are more growth oriented and may or may not pay a dividend. These companies will be chosen based on Valuation (P.E. – Price/Earnings), Balance sheet, cash flow & sales growth. They will typically be an industry leader.
- In an effort to manage risk, my portfolios tend to overweight this asset class.

Small and Medium sized companies*

- I plan to use low cost value oriented mutual funds.
- For larger portfolios, I may use a few individual companies.
- Due to higher risk, my portfolios tend to underweight this asset class.

International and Emerging Markets*

- After a discussion around your comfort level with this asset class, I tend to utilize managed mutual funds. I think it is very important in these markets to have "boots on the ground" Business practices & accounting standards tend to be significantly different than those for a US company and I feel it is important to have a team that understands the differences when making investment decisions. (An index fund does not take these differences into account.)
- Due to the higher risk, I tend to underweight this asset class.

Real Asset*

- Real Estate- I utilize Real Estate Investment Trusts, "REITS" as they are liquid and transparent as to their assets and liabilities.
- Stocks of Publically Traded Energy Pipeline companies are classified in this category- These pipelines are used to transport oil and gas from where they are extracted, to where they are processed to the end user.

*The theory behind adding these asset classes is they also offer higher potential returns and in the Efficient Frontier theory lower overall portfolio risk.

Cash Alternatives

- Bank Deposit Sweep (FDIC Insured)
- Money Market Mutual Funds
- Short term CDs and Treasuries

Fixed Income/ Bonds

In creating this part of the portfolio, I take into consideration your longer term liquidity needs, yield, interest rate risk, and quality risk. Based on our discussions around your risk tolerance I try to diversify risk while trying to maximize yield within your parameters. In a rising rate environment, will tend to skew the portfolio towards short term bonds utilizing a bond ladder* and Floating rate securities. In a stable and falling interest rate scenario, I tend to use more intermediate and long term bonds.

- **Short Term (1-3 year maturity)**
  - Low cost Mutual Funds, individual corporate, municipal and treasury securities
- **Intermediate Term (3-7 year maturity)**
  - Low cost Mutual Funds, individual corporate, municipal and treasury securities
- **Long Term (8+ year maturity)**
  - Low cost Mutual Funds, individual corporate, municipal and treasury securities
- **Floating Rate/High Yield**
  - Lower quality bonds
  - Floating rate Senior Bank Loans (mutual fund)
- **International**
  - Mutual Funds- If the yields are higher than domestic securities and provides diversification which can potentially lower portfolio risk

The prices of small-cap and mid-cap company stocks are generally more volatile than large company stocks. They often involve higher risks because small-cap and mid-cap companies may lack the management expertise, financial resources, product diversification and competitive strengths to endure adverse economic conditions. Investing in foreign securities presents certain risks not associated with domestic investments, such as currency fluctuation, political and economic instability, and different accounting standards. This may result in greater share price volatility. There are special risks associated with an investment in real estate, including credit risk, interest rate fluctuations and the impact of varied economic conditions. Bond laddering does not assure a profit or protect against loss in a declining market. The FDIC standard maximum deposit insurance amount per depositor per insured depository institution for each account ownership category is $250,000. At Wells Fargo Advisors, we offer an Expanded Bank Deposit Sweep and a Standard Bank Deposit Sweep. Please contact the Portfolio Manager for additional details regarding these programs. All investing involves risk including the possible loss of principal. There is no assurance any investment strategy will be successful or that a fund will meet its investment objectives. Each asset class has its own risk and return characteristics. The level of risk associated with a particular investment or asset class generally correlates with the level of return the investment or asset class might achieve. Stock values may fluctuate in response to general economic and market conditions, the prospects of individual companies, and industry sectors. Bonds are subject to market, interest rate, price, credit/default, call, liquidity, inflation and other risks. Prices tend to be inversely affected by changes in interest rates. Income from municipal securities is generally free from federal taxes and state taxes for residents of the issuing state. While the interest income is tax-free, capital gains, if any, will be subject to taxes. Income for some investors may be subject to the federal Alternative Minimum Tax (AMT). Mutual Funds and ETFs are subject to risks similar to those of stocks and may yield investment results that, before expenses, generally correspond to the price and yield of a particular index. There is no assurance that the price and yield performance of the index can be fully matched.

As each Private Investment Management (PIM®) program account is individually managed, construction and ongoing management of portfolios may vary from those discussed in this Philosophy Statement. Past performance is not indicative of future results, and there is no assurance that any investment strategy will be successful. The PIM program is not designed for excessively traded or inactive accounts and are not suitable for all investors. Please carefully review the Wells Fargo Advisors advisory disclosure document for a full description of our services. The minimum account size for this program is $50,000.

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