Weekly 3

WHAT YOU NEED TO KNOW ABOUT THE MARKETS

January 2, 2020

CLS INVESTMENTS

Week in Review

Stock, bond, and commodity markets around the globe continued their winning streak last week. Most major asset classes ended the week positive, except U.S. small-caps. The U.S. dollar depreciated against other currencies, which may help explain the weakness in small-cap stocks (relative to large-caps), as a weak dollar typically hurts smaller companies that rely on the domestic market for most of their revenue.

Commodities and emerging market stocks typically perform well when the dollar weakens. Those two asset classes were atop the leader board last week, up more than 1% each. They've had a blockbuster December, too, both up more than 5%. In single-country markets, Greece and Argentina were up the most last week. Greece has climbed nearly 50% in 2019 alone.

Bonds were roughly flat as the benchmark U.S. 10-year Treasury fell from 1.93% to 1.88%.

As we wrap up a joyous 2019 for the markets, we reflect on some of the best bets of the last decade, focus on a different way to look at the behavior gap, and dissect the current risk environment. In addition, our first quarter 2020 Quarterly Market Outlook, which reviews opportunities in major markets, will be available soon.

Happy New Year!

1 *The impressive performance of the stock market in 2019 is nothing to be surprised about.*

2 *How can we help investors overcome the behavior gap? By understanding the pain gap.*

3 *Why do emerging markets and the U.S. currently have equal risk but different expected returns?*

Market Performance

as of 12/27/2019

FIXED INCOME	10-YEAR	5-YEAR	3-YEAR	1-YEAR	YTD	QTD	LAST WEEK
Cash Equivalent[1]	+0.54%	+1.03%	+1.62%	+2.18%	+2.14	+0.42%	+0.03
U.S. Investment Grade Bonds[2]	+3.76%	+3.15%	+4.34%	+9.18%	+8.87%	+0.32%	+0.30%
EQUITIES	**10-YEAR**	**5-YEAR**	**3-YEAR**	**1-YEAR**	**YTD**	**QTD**	**LAST WEEK**
Global Equity Market[3]	+9.00%	+8.32%	+12.49%	+28.41%	+26.83%	+9.24%	+0.73%
Total U.S. Market[4]	+13.42%	+11.14%	+14.43%	+32.63%	+31.56%	+9.27%	+0.52%
Domestic Large-Cap Equity[5]	+13.52%	+11.83%	+15.65%	+33.28%	+32.23%	+9.99%	+0.70%
Domestic Small-Cap Equity[6]	+11.90%	+7.63%	+7.89%	+27.29%	+25.99%	+8.69%	-0.25%
International Equity[7]	+5.43%	+5.76%	+10.55%	+24.16%	+22.04%	+9.34%	+0.91%
Developed International Equity[8]	+5.69%	+5.58%	+9.93%	+25.29%	+23.00%	+8.35%	+0.81%
Emerging Market Equity[9]	+4.55%	+6.32%	+12.81%	+20.80%	+19.15%	+12.30%	+1.19%
DIVERSIFIERS	**10-YEAR**	**5-YEAR**	**3-YEAR**	**1-YEAR**	**YTD**	**QTD**	**LAST WEEK**
Diversified Alternatives[10]	+3.08%	+0.87%	+1.96%	+7.23%	+7.18%	+2.30%	+0.05%
Commodity[11]	-4.60%	-4.21%	-0.79%	+6.81%	+8.29%	+5.00%	+1.22%

[1]Morningstar Cash Index [2]Bloomberg Barclay's Capital U.S. Aggregate Bond Index [3]Morningstar Global Market Large-Mid Index [4]Morningstar U.S. Market Index [5]Morningstar U.S. Large Cap Index [6]Morningstar U.S. Small Cap Index [7]Morningstar Gbl ex U.S. Large-Mid Index [8]Morningstar DM ex U.S. Large-Mid Index [9]Morningstar EM Large-Mid Index [10]Morningstar Diversified Alternatives Index [11]Bloomberg Commodity Index.

The Year's Best Stocks: Global Edition

1

Are you surprised by how well the stock market performed this year? Don't be. More than half of the time, the market is up double digits, and a little over a third of the time, it is up more than 20%!

12-MONTH ROLLING RETURNS	LONG-TERM AVERAGE
Returns > 20%	34%
Returns between 10 and 20%	23%
Returns between 5 and 10%	11%
Returns between 0 and 5%	8%
Returns between 0 and -5%	6%
Returns between -5 and -10%	5%
Returns < -10%	13%

According to the S&P 500 index

With two market sessions remaining in 2019 at the time of this writing, four stocks in the S&P 500 index were up more than 100%.

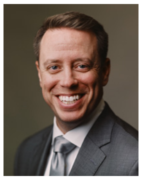
STOCK	RETURN (%)
ADVANCED MICRO DEVICES	150.16
LAM RESEARCH CORP	120.29
KLA CORP	104.39
TARGET CORP	101.71

Pretty solid returns, no doubt. But can we find higher-returning stocks if we expand our opportunity set? The answer is typically yes, which is why we believe it is a good idea to invest with a global mindset.

Below is a sampling of developed international stocks' performance, via the Vanguard FTSE Developed Markets index:

STOCK	RETURN (%)
ARROWHEAD PHARMACEUTICALS IN	422.79
VARTA AG	374.87
LASERTEC CORP	312.47
DOOSAN SOLUS CO LTD	272.96
STRIKE CO LTD	246.50

The top five stocks more than doubled the best performers of the S&P 500, and 42 stocks on the index returned more than 150%!



CASE EICHENBERGER, CIMA
Senior Client Portfolio Manager

Case Eichenberger co-manages CLS's American Funds strategies and the CLS Shelter Fund, works closely with CLS's separate account strategies (Master Manager), and communicates with advisors and their clients both remotely and in-person.

Since joining CLS in 2007, Mr. Eichenberger has held various roles, including Relationship Representative and Internal Wholesaler. In 2015, he accepted the role of Client Portfolio Manager and was promoted to Senior Client Portfolio Manager in 2018.

Mr. Eichenberger received his Bachelor of Science degree in Business Administration from Midland University. He holds the Series 65 license and Certified Investment Management Analyst (CIMA®) designation. During the accreditation process, he attended the Wharton School of Business at the University of Pennsylvania.

Mr. Eichenberger is a member of Greater Omaha Young Professionals and a volunteer for Habitat for Humanity.

Did you know? Case comes from a long line of educators.

The Year's Best Stocks: Global Edition (cont.)

1

Below is a look at emerging market stocks, via the MSCI Emerging Markets index:

STOCK	RETURN (%)
IMPALA PLATINUM HOLDINGS LTD	301.30
SIBANYE GOLD LTD	251.84
PIRAEUS BANK S.A	249.89
QUALICORP CONS E CORR SEG SA	231.35
PUBLIC POWER CORP	219.94

Pretty stellar returns, too.

My point is not that it's easy to pick the winners each year, but that an expanded investment universe presents more opportunities.

The last decade was dominated by the U.S. stock market. Some investors would say that is always the case. But, as the table below shows, it was a different story just 20 years ago.

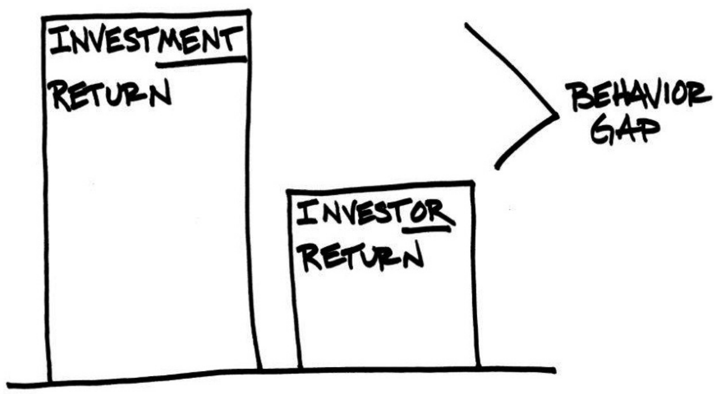
10 Year Performance Ranks

Region	Rank	1999-2009	Rank	2009-2019
MSCI USA	10	-20%	1	282%
MSCI ACWI	9	-2%	2	181%
MSCI Emerging Asia Index	4	100%	3	163%
MSCI Emerging Markets	2	137%	4	125%
MSCI ACWI ex USA	5	21%	5	106%
MSCI EAFE	7	8%	6	102%
MSCI Europe	8	4%	7	101%
MSCI Pacific	6	20%	8	92%
MSCI Emerging Europe	3	123%	9	77%
MSCI Emerging Latin America	1	288%	10	68%

Where do you want to be invested now? Markets do not run on 10-year cycles, but we believe the more valuations get stretched in countries, regions, and stocks, the more investors should **expand opportunities to grab the up-and-coming winners of the next 10 years.**

How Can We Help Bridge The Gap?

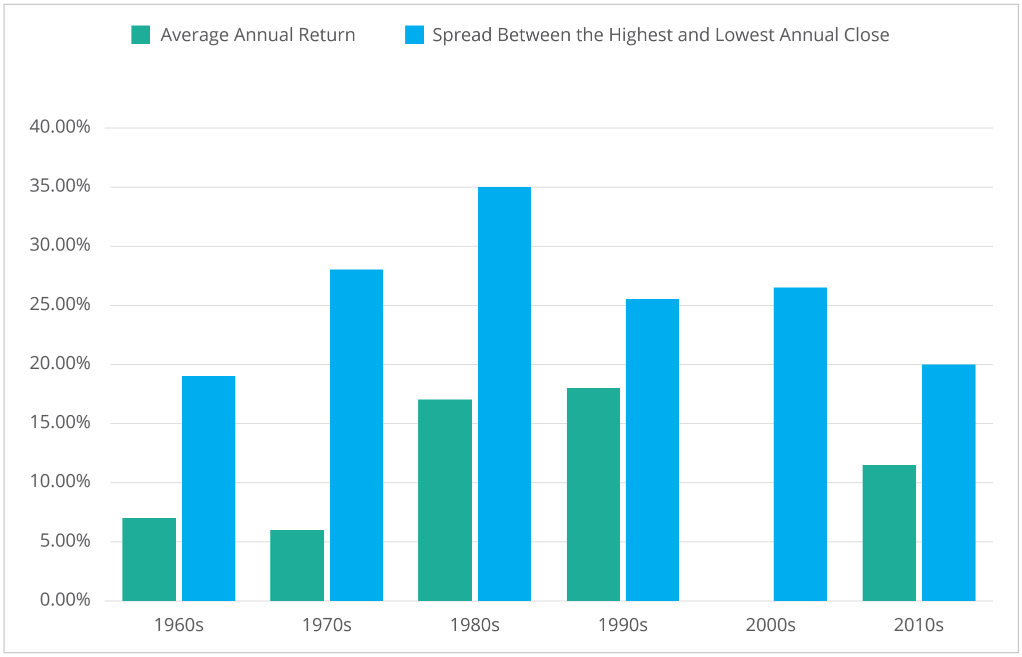
2



You've seen this illustration before — it can be found in CLS's Reference Guide. It shows the difference between actual stock market returns and the returns attained by a typical investor. This gap is called the behavior gap, a term coined by Carl Richards. The behavior gap is caused by the tendency to chase returns at the top only to get scared out at the bottom.

What explains the behavior gap? The pain gap. The pain gap is the difference between what the market returns in a year and what it did during that year.

Let's visualize this: The chart below shows the average return in the U.S. by decade since the 1960s (light green bar). The bar shows the difference between the highest and lowest annual close during each decade. The light blue bar is another way to see the volatility investors endured during the decades.



Source: Morningstar as of 11/30/2019

JEOVANY ZELAYA
Client Portfolio Manager

Jeovany Zelaya is a Client Portfolio Manager at CLS Investments. He is responsible for communicating CLS's investment philosophy, process, strategies, and performance to external clients and prospects.

Prior to beginning his current role, Mr. Zelaya served as an Internal Wholesaler of Qualified Plans starting in 2016. His background in sales gives him an edge in providing ongoing updates, analysis, and support to CLS's Sales Team.

Mr. Zelaya holds a Master of Business Administration degree from the University of Nebraska at Omaha. He received his Bachelor of Business Administration degree from the University of Houston and is currently pursuing a Bachelor of Science in Accounting degree from Auburn University. Mr. Zelaya holds his Series 65 license and is currently a Level III candidate in the Chartered Financial Analyst (CFA®) Program.

Did you know? Jeovany grew up in El Salvador.

How Can We Help Bridge The Gap? (cont.)

2

In a [2016 article] for *The Motley Fool*, author and investor Morgan Housel said:

"Take 1998. It's glorified as part of the late 1990s stock boom where markets went one way — up. Sure enough, the S&P soared 28% in 1998, one of the biggest gains of all time.

But 1998 was actually a vicious nightmare for most investors. It started with a 20% surge by July, then gave everything back and was down for the year by October, only to log one of the best quarters in history to finish the year up 28%.

In isolation 1998 is the kind of year investors dream about and financial marketers use to show how lucrative investing can be. But actually living through 1998 meant waking up every morning wondering what the hell was going on, not knowing if the next 90 days meant you'd make or lose a third of your life savings. That's the pain gap."

Morningstar and Dalbar provide quantitative data to explain these gaps. In fact, Morningstar recently released Mind the Gap 2019 — a report on investor returns from around the globe. It showcases the difference in returns an investor receives compared to a fund's actual returns. Here are some surprising findings:

1. Australian investors had the best investor returns.
2. European investors had the worst investor returns.
3. For U.S. investors:
    - The gap between stock market and investor returns has shrunk over the past 10 years, which can mostly be explained by the 10-year bull market and below-average volatility.
    - The higher the cost of a fund, the wider the behavior gap.
    - The more volatile the investment vehicle, the wider the behavior gap.

Two Markets with Equal Risk But Different Expected Returns

3

When visiting and speaking with investors and advisors alike, we often get on the subject of global investing and risk management, two subjects CLS is an expert on.

When we invest as fiduciaries, on behalf of clients, **it is our role to find areas that present attractive expected returns and build portfolios that take on the appropriate amount of risk to achieve a set of specific goals for the client.**

This brings us to two broad asset classes – U.S. stocks and emerging market stocks. The current CLS Risk Budget* score for each is 106 (106% of the global stock market), meaning as stand-alone investments, they are both riskier than the global stock market. But how can this be? First, there is a correlation benefit when combining these two markets with developed international stocks to bring down the overall Risk Budget of the portfolio to 100. Second, over the past year, the U.S. market trounced emerging markets in terms of returns by about 13%. Why would the risk be equal still? Return is not risk, and risk is not return. Even though they are somewhat linked in the very long term, certain markets become less risky due to correlation effects in the shorter term. One year ago, many markets were in turmoil and U.S. markets were in freefall, but other parts of the world fared better.

Let's look at the data:

ETF NAME	CURRENT RB SCORE	1-YEAR BETA	1-YEAR RR	1-YEAR CORRELATION	3-YEAR BETA	3-YEAR RR	5-YEAR BETA	5-YEAR RR	10-YEAR BETA	10-YEAR RR	10-YEAR CORRELATION
Vanguard Total Stock Market ETF	106	1.15	1.18	0.97	1.06	1.09	1.01	1.05	0.97	0.99	0.97
Vanguard FTSE Emerging Markets ETF	106	0.81	1.09	0.75	0.96	1.16	1.02	1.30	1.12	1.32	0.85

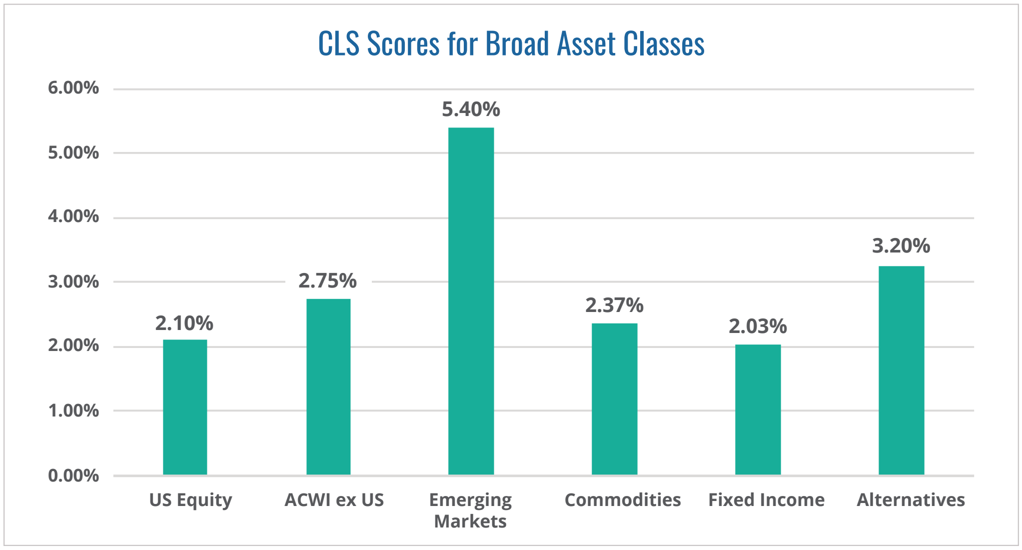
Over shorter timeframes (one-year and three-year), emerging market stocks have less beta exposure to the global market, but over longer timeframes (five-year and 10-year), they have more. In the end, the numbers even out.

** CLS's Risk Budgeting Methodology is the foundation of our portfolio construction process. We start by defining an investor's personalized Risk Budget, based on his or her unique investing time horizon, ability to tolerate risk, and investment goals. This number, which is expressed as a percentage of a well-diversified, global equity portfolio, represents the amount of risk an investor is comfortable taking on in exchange for potential returns. An investor's Risk Budget is the risk level at which we manage his or her portfolio.*

Two Markets with Equal Risk But Different Expected Returns (cont.)

3

However, this is only part of the equation. When building portfolios, we must look at expected returns, too. **Given the data below, we have an emphasis on emerging market stocks.** They have higher expected returns and similar risk to U.S. stocks, which we believe gives our investors a good chance of achieving their long-term goals.



In our upcoming Quarterly Market Outlook, we will discuss our recently updated and improved Risk Budgeting methodology, which we consistently work to enhance to better serve investors. Stay tuned!

The Morningstar Global Market Large-Mid Index is an index that measures the performance of the global market's equity markets targeting the top 90% of stocks by market capitalization. The Morningstar U.S. Market Index is an index that measures the performance of U.S. securities and targets 97% market capitalization coverage of the investable universe. It is a diversified broad market index. The Morningstar U.S. Large Cap Index is an index that measures the performance of U.S. large-cap stocks. These stocks represent the largest 70% capitalization of the investable universe. The Morningstar U.S. Small Cap Index is an index that measures the performance of U.S. small-cap stocks. These stocks fall between the 90th and 97th percentile in market capitalization of the investable universe. In aggregate, the Small Cap Index represents 7% of the investable universe. Morningstar Global ex U.S. Large-Mid Index is an index that measures the performance of Global Markets (ex-U.S.) equity markets targeting the top 90% of stocks by market capitalization. The Morningstar DM ex U.S. Large-Mid Index is an index that measures the performance of developed markets ex-U.S. equity markets targeting the top 90% of stocks by market capitalization. The Morningstar EM Large-Mid Index is an index that measures the performance of emerging markets targeting the top 90% of stocks by market capitalization. The Barclay's Capital U.S. Aggregate Bond® Index measures the performance of the total United States investment-grade bond market. The Morningstar Cash Index is an index that measures the performance of a Treasury Bill with six to eight weeks until maturity in the U.S. market. The Morningstar Diversified Alternatives Index allocates among a comprehensive set of alternative underlying ETFs that employ alternative and non-traditional strategies such as long/short, market neutral, managed futures, hedge fund replication, private equity, infrastructure or inflation-related investments. The Bloomberg Commodity Index is made up of exchange-traded futures on physical commodities and represents commodities that are weighted to account for economic significant and market liquidity. This index provides investors with a means of understanding the performance of commodity futures markets and serves as a benchmark for investment performance of commodities as an asset class. The volatility of the indexes may be materially different from the individual performance attained by a specific investor. In addition, portfolio holdings of investors may differ significantly from the securities that comprise the indexes. You cannot invest directly in an index.

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Beta is a measure of the volatility, or systematic risk of a security or a portfolio in comparison to the market as a whole.

Bonds are a type of debt instrument issued by a government or corporate entity for a defined period of time at a fixed interest rate. Bonds may be subject to unsystematic risks including, but are not limited to, call risk and reinvestment risk. High yield bonds, or junk bonds, will be subject to an even greater degree of these risks as well as subject to the credit risk.

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0006-CLS-1/2/2020