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THE INVESTMENT COUNSELOR
NOVEMBER 2026

BETTER INVESTORS VS. BETTOR INVESTORS



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Picking stocks or putting it all on black? While dramatic, this analogy reflects how today's market has taken on the features of a casino, driven by concentrated positions, borrowed money, and shrinking investment horizons.

Signs of a Speculative Market

Technology has contributed to the gamification of investing. It has never been easier to open an app, transfer funds, and place trades with the push of a button. While we strongly support the broader participation of Americans in investing as an incredible tool for long-term wealth building, we grow concerned when market conditions tilt toward speculation. This behavior is further fueled by the explosive popularity of prediction markets, which offer a quick-payoff thrill despite high risks of loss.

Together, these trends foster an environment that is the antithesis of ownership thinking. A clear indicator of this is how the average holding period for stock positions has dipped to less than six months according to the New York Stock Exchange, about half of what it has been since the turn of the millennium.

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Further amplifying these bets is the use of financial leverage. The usage of borrowed money to place trades has reached an all-time high of $1.5 trillion without a requisite increase in "equity" (i.e., actual ownership of the underlying investment). The volume of leveraged instruments like options is also peaking at a level not seen since 2021 during the pandemic-era stock craze. Investors that were once investing only the value of their own cash are now taking positions at multiples of that amount.

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Because leverage creates oversized trades, it acts as a dangerous accelerant; should market sentiment shift, the urgent need to cover borrowed positions can trigger a rush for the exits, setting the stage for price drops that are far steeper and more rapid than the preceding climbs.

Crowded Trades and Skewed Odds

Dispersion, defined as the magnitude of stock-specific price moves relative to other stocks and the overall S&P 500 Index, has been hovering well above the long-term average. This points to a market sharply bifurcated into clear "winners" and "losers," even though most companies land somewhere in between. Driven by crowding into the same familiar names, the 25 largest companies in the index (just 5% of all constituents) now account for over 50% of total index weight, far surpassing historical peaks of under 40%. This dynamic creates a self-reinforcing loop where rising prices attract attention and fresh capital, which drives prices even higher. Expectations for these bellwethers of the U.S. economy have never been higher, placing immense pressure on them to deliver and increasing the risk of severe market punishment if they fall short. In such an environment, the factors that should matter most to investors (valuation and underlying business fundamentals) can become an

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afterthought.

At Clifford Swan, we approach the market differently. Our work begins by evaluating a company's balance sheet strength, competitive moats, and sustainable cash flows. We calculate what the business is actually worth based on those core attributes and compare that estimate directly to today's market price.

A sports betting analogy is illuminating. Fans frequently wager emotionally on popular teams like the Yankees or Lakers, which distorts the odds. Even though those teams may be real contenders, the poor odds make them unattractive bets at the wrong price. Financial markets operate much the same way. When prices become completely disconnected from business reality, investors are left with little upside and slim margins for mistakes.

Conversely, less celebrated businesses may offer a better balance of risk and reward. These include companies that possess durable advantages that translate to robust cash generation and growth. In fact, we believe that many of today's overlooked businesses represent the winners of tomorrow.

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Thinking Like Owners

Our investment discipline rests on a simple tenet: we invest in companies, not stock tickers. While short-term trading can yield quick profits, stock prices cannot outrun underlying fundamentals forever. Eventually, business reality catches up.

In applying this approach, we caution against momentum chasing—the urge to simply follow what is currently working. While momentum investing feels comfortable in the short term, the eventual ride down is often far more dramatic than the climb up, made all the more alarming as participants frequently buy in at or near the peak. The math is unforgiving when it comes to large losses: a stock that drops 50% must double (rise 100%) just to break even.

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Ultimately, our role is not to place bets on the market's next spin, but to act as prudent stewards of our clients' capital. When the market offers a compelling opportunity to own a durable, growing business at an attractive valuation, those are the odds we will confidently play.

FROM HEIRLOOMS TO LASTING IMPACT: A PHILANTHROPIC FRAMEWORK



Lloyd K. Wong, CFA
Principal, Investment Counselor

Imagine inheriting an extensive, carefully curated collection of fine jewelry from your mother, valued at $1 million. Despite an active social schedule, you know you will never wear all these heirlooms. You hold a deep sense of gratitude for the cancer researchers who have personally impacted a family member's well-being, and you have a special place in your heart for veterans' causes given your husband's years of service. Most importantly, you realize this collection presents a unique opportunity to transform your mother's treasured jewels into a special tribute that honors her legacy.

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You already donate cash or appreciated stock annually to these areas, and you want to do more. While you want to see an immediate impact from some of your giving, you would also like

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to earmark funds for the future. Is there a flexible solution through which you can monetize this illiquid collection and create a reliable source of funding for your preferred philanthropic causes both now and later? The answer is "yes."

Or consider a different scenario: you recently lost your husband and no longer need or want to maintain his immaculately cared-for, 30-year-old vintage Jaguar. Can you simply donate this vehicle to your favorite local public radio station, create an immediate benefit for the charity, and reap the benefits of a tax deduction? Absolutely.

Philanthropy takes on many forms, driven by a multitude of motivations and executed through a wide array of giving vehicles. Relatively simpler approaches include straightforward, one-time gifts of cash, appreciated stock, or Qualified Charitable Distributions (QCDs) from an IRA. More complex

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vehicles encompass charitable trusts, private foundations, and endowments.

Because advanced strategies require legal expertise and annual tax reporting, we work with you to ensure the gift size justifies the added expense. When strategizing how to simultaneously balance your charitable ambitions with your wealth planning goals, we center the conversation around a specific framework: Why, What, Who, and How.

Why: The Motivation

The drive to give usually stems from personal experiences. It might be childhood hardships, educational

"Ultimately, a well-structured gift satisfies your philanthropic goals while optimizing your broader financial picture."

allegiances, or the desire to support local disaster recovery, such as relief efforts for last year's Eaton and Palisades fires. For some, it is a desire to address societal issues like food insecurity; for others, it is simply a desire to give back.

Your motivation to give should always drive the conversation, with the financial strategy behind your gift being an important secondary consideration. Maximizing tax deductions may be a priority during your high-earning years, while securing a stable income stream might be more important during retirement or market turbulence. Ultimately, a well-structured gift satisfies your philanthropic goals while optimizing your broader financial picture.

What: The Asset

The size and type of your intended gift dictate the level of complexity involved. We generally break this down into two categories:

Straightforward Gifts: These are simpler donations of cash, publicly traded appreciated securities, or even an unused vehicle.

Complex Gifts: This category goes beyond stock to include real estate, closely held business interests, private equity, intellectual property, cryptocurrency, and tangible assets like vintage car collections, artwork, jewelry, or mineral rights.

Complex gifts require a highly disciplined approach to due diligence. It is critical to carefully evaluate the asset's valuation, its liquidity, any transfer restrictions, and the specific tax treatments before moving forward.

Who: The Charitable Organization

Selecting the right organization goes far beyond confirming they are a registered 501(c)(3).

"The charity's mission must be fundamentally aligned with your personal values."

The charity's mission must be fundamentally aligned with your personal values. From there, we encourage an independent vetting process that evaluates several critical factors:

Gift Acceptance Policies: If you are donating a complex asset, does the organization have the expertise to evaluate and liquidate it? Furthermore, if you have specific donor restrictions, such as a designated project or naming preferences, you need absolute confidence in the organization's

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ability to honor your charitable intent. Finally, it's important to establish contingencies upfront to account for the possibility that the cause you are supporting may be completed or discontinued before the funds are fully spent.

Reputation and Accountability: Verification on platforms like Charity Navigator or Candid (previously Guidestar) is a good starting point, but it is not a substitute for true due diligence. We recommend researching proper disclosures, reviewing annual reports, and examining IRS Form 990 filings.

Financial Health and Scalability: A sustainable charity needs adequate cash reserves, diversified funding sources, and strong financial controls. We look for cost-effectiveness, meaning a high percentage of donated dollars goes directly to the mission rather than administrative overhead. Finally, we look at the longevity of the organization and their succession planning to ensure your legacy will be honored over the long run.

How: The Structure

The "What" and the "Who" ultimately drive the "How." This is where we focus on choosing a giving vehicle that will maximize your intended impact while optimizing your unique financial position.

Returning to the inherited jewelry, how might we balance the "what" and the "who" to determine the "how"? In that case, the solution was establishing a Donor-Advised Fund (DAF) with an institution that is specifically equipped to accept, evaluate, and liquidate complex assets. Once the jewelry is auctioned within the DAF (free of capital gains taxes), the donor can direct grants from the proceeds to support ongoing causes. The remaining capital stays invested, growing tax-free to fund your giving going forward.

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We are always candid about the trade-offs required in various giving structures. For example, while a DAF offers donors simplicity, it requires relinquishing direct legal control over the assets. If you prioritize multi-generational family involvement and control, you may need to be prepared to take on the administrative burdens of a Private Foundation.

The right structure also depends heavily on your time horizon. An immediate disaster recovery effort requires different urgency than a Charitable Remainder Trust (CRT) or a Charitable Gift Annuity (CGA) designed to generate a contractual income stream for you today while planting seeds for a future legacy.

In this season of Thanksgiving, our team at Clifford Swan wants to remind you that we are here to provide the strategic guidance to balance your philanthropic and financial goals.

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