

ELF CAPITAL MANAGEMENT, LLC

(ENDOWMENT LIKE FUND MANAGEMENT)

October 5, 2011

This is the August / September 2011 ELF Capital Management, LLC Market Letter. If you do not wish to be included in our circulation, please reply indicating your desire to be removed and we will be happy to oblige. Alternatively, any of your friends or colleagues may receive this on a regular basis by entering their email address on our list-server via this [link](#). Feel free to forward this to any of your friends! Thanks for your interest and we hope you enjoy the letter.

The Folly of Impatience

Have you ever gone grocery shopping or entered a restaurant when you were really hungry? How did that work out for you?

It's widely known that hungry people order more food than they can eat – experiencing the “your eyes are bigger than your stomach” effect. This reaction is so common that you've likely experienced this kind of impatience before. It is also a popular topic for academic researchers. Studies show that hungry people buy more food than originally intended (Gilbert, Grill, and Wilson 2002; Nisbett and Kanouse 1969), have a stronger preference for candy over fruit (Read and van Leeuwen 1998) and demonstrate less self-control (Kirk and Logue 1997).

Impatient overeating may only bring you brief stomach discomfort and modest anxiety from having lost self-control. However, impatience can impact us in more negative ways. It can lead us to make poor financial decisions, harm or destroy relationships, add to anxiety and even harm our health. The impulse to obtain instant gratification can do more harm than good. Indulging impatience can contribute more to self-imposed stress and unhappiness than the brief pleasure gained.

The parenthetical opposite of impatience is procrastination. Whether from the paralysis of analysis or outright avoidance, constant procrastination can also cause anxiety. Have you ever found yourself frantically trying to meet a deadline at the last minute or waited so long that you missed an opportunity altogether? Procrastination can foster disorder and clutter in one's life as well as low self esteem.

In digging up information for this article, I found more than enough empirical research on the cause and effect of impatience. Apparently, there is and has been considerable interest by marketing and consumer behavioral academics about this topic. And on the topic of procrastination, not much study at all.

Why do you think impatience is such a hot topic for research?

Controlling the Minds of Consumers

Among the many reasons for studying consumer behavior, a primary use is to help business and political professionals improve their marketing strategy. And impatience heads the list of consumer behavior topics.

One open source study I found was in the August 2005 Journal of Marketing Research. Professors Chen, Ng and Rao set out to reinforce the belief that people from Western

ELF CAPITAL MANAGEMENT, LLC
(ENDOWMENT LIKE FUND MANAGEMENT)

October 5, 2011

cultures are less patient than those from Eastern cultures. While the research was insightful, I found more interesting the introduction they provided. Words in [brackets] are my own:

“Whether and how people incorporate the future into their decision making about consumption options is a topic of considerable interest to scholars of marketing and consumer behavior from both a normative [what is commonly observed] and a descriptive [more detailed] standpoint. Normatively, the time value of money is an integral component of standard economic prescriptions for consumption, investment, and expenditure decisions. For example, according to the normative view, in general, people should prefer receiving money immediately rather than later because all future outcomes should be discounted positively [valued less]. Descriptively, research has examined precisely how the future is discounted and whether discount rates vary across situations and people. ...

Discounting the future is akin to displaying impatience. A high discount rate implies that the future is considerably less important than the present, and people who employ high discount rates manifest relatively high levels of impatience, or the preference for instant rather than delayed gratification. This impatience likely applies to the acquisition of not only money but also other material objects, and it is likely to be reflected in consumers’ (1) desire for quicker service and delivery of products, (2) greater preferences for options that offer early rather than late payoffs, and (3) enhanced willingness to pay for immediate rather than delayed gratification. Thus, the general issue of impatience is of substantial interest to marketing and consumer behavior.”

They are saying that the more impatient a consumer becomes, the more likely they will pay more for something, settle for less quality or pay more for less quality. Basically, impatience drives consumers to make poor financial decisions.

So how do marketing professionals instigate impatience? You’ve heard “sex sells”, right?

Another study in the September 2007 Journal of Consumer Research investigated this very topic. The title of Belgian Economics Professors Van den Bergh, Dewitte and Warlop’s research paper says it all: “Bikinis Instigate Generalized Impatience in Intertemporal Choice”.

I swear that I’m not making this stuff up! By the way, “intertemporal choice” is the study of the how people choose among two or more alternatives that are available at different points in time. For example, should I save for a “rainy day” or spend my money now?

Now, let’s take a look at their introduction:

“Advertisers search for a way to break through the clutter by using sexually oriented appeals in marketing campaigns. Previous research on the use of sexual imagery in advertising has focused on, among other things, consumer’s brand recall and recognition, appeal evaluation, attention, purchase intentions, and product perception. The present study differs from earlier work by showing that the consequences of using sexual imagery extend further than the evaluation of the product or brand itself. In line with previous research demonstrating that exposure to sexual cues influences economic decision making (e.g. Van den Bergh and Dewitte 2006; Wilson and Daly 2004), we will argue that exposure to sexual cues may affect decisions such as whether to purchase a less expensive item that can be enjoyed now or to save for a more expensive one.

...We propose that exposure to ‘hot stimuli’ (Metcalf and Mischel 1999) leads to a non-specific time perspective collapse towards the present. Based on recent neurological findings, suggesting

ELF CAPITAL MANAGEMENT, LLC
(ENDOWMENT LIKE FUND MANAGEMENT)

October 5, 2011

that rewards are processed similarly in the brain, we propose that exposure to 'hot stimuli' may instigate general impatience in intertemporal choice. We will argue that a greater appetite causes a greater urgency to consume anything rewarding."

This article argues that sexual cues produce statistically significant results of inciting impulsively impatient behavior among young heterosexual males and a more mild, but similar effect on others. The research paper also referred to many additional studies that discussed how impatience can be vigorously triggered in other types of people.

Now some of you might be saying: I know I'm being manipulated by advertising, or by political rhetoric, or by the media. But I don't have time to labor every decision or read every message between the lines. And that may be true. However, constantly giving in to impatient behavior will likely form habits that can harm your pockets and your health. How, you might say?

Effects of Impatience

Impatience can vary in degree from one person to the next. and the effect is often negative for the person displaying it as well as those around them. Rather than entertain you with my own opinions, I'll keep this in the realm of the research found.

Let me begin with a study on how impatience impacts the unemployed. In the July 2005 Journal of Labor Economics, researchers Della Vigna and Passerman presented a paper on "Job Search and Impatience":

"How does impatience affect job search? More impatient workers search less intensively and set a lower reservation wage [minimum acceptable wage offer]... In this paper we show that, if agents have exponential time preferences, the reservation wage effect dominates for sufficiently patient individuals, so increases in impatience lead to higher exit rates [being unemployed longer]. The opposite is true for agents with hyperbolic time preferences: more impatient workers search less and exit unemployment later. Using two large longitudinal data sets, we find that various measures of impatience are negatively correlated with search effort and the exit rate from unemployment, and are orthogonal to reservation wages. Overall, impatience has a large effect on job search outcomes in the direction predicted by the hyperbolic discounting model."

Simply put, the more impatient someone is, the more likely they will remain unemployed longer than a more patient person.

The next two studies focus on Type A personalities and how impatience impacts their ability for achievement and their health.

"The Effects Of Type A Behavior Dimensions And Optimism On Coping Strategy, Health, And Performance" by Ashford, Jamieson and Lee. Found in the March 1993 Journal of Organizational Behavior.

"Type A behavior dimensions and optimism were examined as predictors of health and performance. In addition, this research also explored the ways that Type As and optimists cope with stressful situations. The achievement striving dimension of the Type A behavior pattern and optimism were positively related to class performance, while the anger/hostility dimension was positively related to the health symptom of anxiety. Optimism, on the other hand, was negatively

ELF CAPITAL MANAGEMENT, LLC
(ENDOWMENT LIKE FUND MANAGEMENT)

October 5, 2011

related to anxiety. The interaction of achievement striving and optimism was negatively related to anxiety. Additionally, while achievement striving was positively related to problem-focused coping, irritability showed a negative association with problem-focused coping strategy. The results of this study provide insights for both individuals and organizations regarding how to cope with daily stresses in order to lower health risks and improve performance."

"Impatience Versus Achievement Strivings In The Type A Pattern: Differential Effects On Students' Health And Academic Achievement" by Helmreich, Pred and Spence. Found in the November 1987 Journal of Applied Psychology.

"Psychometric analyses of college students' responses to the Jenkins Activity Survey, a self-report measure of the Type A behavior pattern, revealed the presence of two relatively independent factors. On the basis of these analyses, two scales, labeled Achievement Strivings (AS) and Impatience-Irritability (II), were developed. In two samples of male and female college students, scores on AS but not on II were found to be significantly correlated with grade average. Responses to a health survey, on the other hand, indicated that frequency of physical complaints was significantly correlated with II but not with AS. These results suggest that there are two relatively independent factors in the Type A pattern that have differential effects on performance and health. Future research on the personality factors related to coronary heart disease and other disorders might more profitably focus on the syndrome reflected in the II scale than on the Type A pattern."

While it is good to see that Type A behavior is not considered synonymous with impatience; and it should be troubling to see that impatience is highly correlated with poor academic and work performance, irritability, anxiety and other health issues.

Some Closing Thoughts

In the investment world, the most influential factors driving the decision-making process are the emotions of fear and greed. These emotions, together with crowd behavior, can promote impatience in novice and experienced investors alike.

Have you ever noticed that when the price of something that you may be interested in buying is drifting lower or looks to be abundantly available, you feel no urgency to act and exhibit great patience? And when the price begins to move up, you feel more compelled to act? This is called the "scarcity effect" and is a pretty common trigger for creating impatience among investors. However, this trigger can work against you if you haven't done your homework or set your desired purchase price limit beforehand.

In my opinion, impatience makes the emotions of greed and fear work against you. This belief comes from my observation that most of the great investors share one common characteristic – patience. Take Warren Buffett for example. His favorite saying has been: *"be greedy when others are fearful and be fearful when others are greedy"*. This is Buffett's clever way to say that we should be buying when prices are low and selling when prices are high – basically investing contrary to the mentality of the crowd.

I always cringe when I read or hear market pundits promote *"why it pays to be an impatient investor"*. What they don't tell you is that that trading or trying to time the markets are the most challenging strategies to be successful at. They might as well parade a bikini clad model with that ad.

ELF CAPITAL MANAGEMENT, LLC
(ENDOWMENT LIKE FUND MANAGEMENT)

October 5, 2011

Now I'm not advocating that my reader's become procrastinators. Procrastination has its drawbacks as well. Yet, in the current poor economic and investing climate we are experiencing, I thought it would be helpful to point out that patience can be more than a virtue.

As aptly worded by an anonymous Wiki-How contributor post:

"It has never been easy to be patient, but it's probably even harder now than at any time in history. In a world where messages can be sent across the world instantly, seemingly everything is available with a few clicks of the mouse, and a swift movement of your thumbs can take you into a fantasy game world, it's very hard not to expect instant satisfaction. But patience remains a valuable tool in life. We don't always get instant gratification, and some of the best things in life require years of hard work and waiting. Fortunately, patience is a virtue that can be cultivated and nurtured. It does take time to fulfill this goal, but once this has grown into an ordinary skill for you, you certainly won't be disappointed at what life can offer you with some spare time. You will be surprised by how boring, restless, and lagging hours can evolve into a passing time of relaxation and peace of mind."

ELF's Outlook and Performance

If events that occurred in 1967 made history books remember it as the Summer of Love, the market's action in 2011 should be remembered by investors as the Summer of Volatility. At the onset of this summer, I can remember discussing with one of my clients that this could very well be an ugly summer for investing. I had no idea how accurate those thoughts would be.

Over the past two months, more pronounced in September, the markets have swung from euphoric to impatient. The Greek debt drama has garnered center stage and speculative scenarios abound on how a default on their government debt will trigger another financial crisis and a global recession. Worries about a slowing Chinese economy and falling oil and copper prices have weighed heavily on the markets as well.

Prices are reflecting too much impatience and the markets seem to have already discounted a fairly dire outcome. Except for the Euro-zone, where the potential risk seems more fairly priced, markets elsewhere look oversold in anticipation of a global recession. We've been trained to think the worst when we hear "recession". Recent history has imprinted it to be a high drama event. It doesn't have to be and that outcome remains uncertain. Yet, the markets have gone far to price in that scenario.

As for China, the Chinese government has been tightening monetary policy for more than a year to fend off high inflation. And much of those inflationary forces were being exported by the US through QE2 and China's peg to the US Dollar. We're no longer exporting inflation, commodity prices have been abating and inflation is moderating over there and here in the US. This is strongly positive for both economies.

While the Greek drama continues to play out, it is likely that we will also continue to see volatility in the markets. Yet stock prices are attractive here given earnings levels, corporate insiders are buying and managers, on the whole, are signaling that earnings look to be unimpaired. We'll soon find out as the third quarter's earning releases begin to roll out in the next couple of days.

ELF CAPITAL MANAGEMENT, LLC
(ENDOWMENT LIKE FUND MANAGEMENT)

October 5, 2011

We went into the summer raising our aggregate cash levels to roughly 55% of portfolio assets. This buffered us from the beginning of the recent correction. Then, in July and August we reduced cash levels to roughly 15%. We thought we had seen the worst after the drop that ensued S&P's downgrade of US Treasury debt. We are holding overweight positions in US markets in large and small capitalization stocks with exposures in Asian and Latin American emerging markets. Technology is our favored sector with positions in energy, copper, agricultural and industrial sectors as well.

Our portfolio clients ended the month of September down 12.05%. Here are some comparative numbers for you to review:

	Sept 2011	3 Month	Y-T-D	1 Year
ELF's ETF Strategy (net)	-12.05%	-16.99%	-13.23%	-10.03%
S&P 500	-7.18%	-14.33%	-10.04%	-0.86%
Russell 2000	-11.37%	-22.15%	-17.80%	-4.73%
MSCI EAFE Index	-9.86%	-19.60%	-17.18%	-12.02%
MSCI All County World	-9.65%	-17.90%	-15.12%	-8.04%

For disclosure purposes, past performance is not necessarily indicative of future results and ELF Capital Management LLC (ELF), formerly Hoffman White & Kaelber Financial Services LLC, cannot guarantee the success of its services. There is a chance that investments managed by ELF may lose a substantial amount of their initial value.

ELF is an independent discretionary investment management firm established in February 2003. ELF manages a strategic allocation of primarily exchange-traded index funds (ETFs), and may invest in other carefully selected securities. ELF may also employ hedging techniques, through the use of short positions and options. ELF manages individual portfolio accounts for both individual and business clients.

The ELF ETF Strategy returns presented herein represents a composite of actual results from all client portfolios managed by ELF. Currently, it is the only composite presented by ELF and separate client account portfolio positions are substantially similar, except as may be modified for retirement plan accounts and accounts with net equity of \$60,000 or less. There is no minimum account size for inclusion into ELF's ETF Strategy composite and accounts with net equity of \$60,000 or less have a tendency to downwardly skew the combined results.

ELF's performance data presented herein includes the reinvestment of dividends and capital gains; as well, ELF's ETF Strategy composite returns are presented after deducting actual management fees, transaction costs or other expenses, if any. ELF charges an annual investment management fee as follows: 1.25% on the first \$250,000; 1.00% on the next \$750,000; 0.95% on the next \$4,000,000; and, 0.75% thereafter.

Broad market index information provided is solely for the purpose of comparison. This index data was obtained from third party sources believed reliable; however, ELF does not guaranty its accuracy. An investment account managed by ELF should not be construed as an investment in an index or in a program that seeks to replicate any index. In most cases, investors choose a market "index" having comparable characteristics to their portfolio as a benchmark. An ETF is a security that tracks an index benchmark or components thereof. As ELF actively manages a strategic allocation of primarily ETFs, selecting a comparable benchmark poses significant challenges. Over time, the broad market indices provided above may exhibit more, similar or less variability of returns and risk than ELF's strategic allocation. As well, the broad market index information provided above reflects gross returns and have not been reduced by any estimated fees or expenses that a person might incur in trying to replicate an index.