COMMONWEALTH LIQUID ALPHA FUND

Commonwealth Bank & Trust Company

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4Q17 PERFORMANCE REVIEW

Commonwealth Liquid Alpha Fund ("Liquid Alpha") generated another year of reasonable relative, but frustrating, absolute performance in 2017. The fund returned 1.73% in 4Q17 and 1.18% for full-year 2017 (net of all fees and expenses). This trailed the (non-investable) benchmark SG CTA Index, which returned 5.21% for the quarter and 2.35% for the year. Liquid Alpha had been outperforming the benchmark at the end of every calendar month during 2017 through November, but surrendered its lead at year-end. Underperformance in 4Q and especially December was driven by the significant long equity index exposures held by the trendfollowing managers that largely comprise the benchmark. Due to Liquid Alpha's greater diversification across factors and conscious avoidance of heavy equity beta, the fund underperformed over this period. However, Liquid Alpha did outperform the largest comparable public fund, AQR Managed Futures (AQMIX), which lost -0.82% on the year.

Along with most other macro/quantitative managers, we risk sounding like a broken record bemoaning the lack of volatility, inflation, or persistent momentous trends across asset classes. But the reality is that historically low volatility and market complacency have been a headwind for Liquid Alpha over the past two years. Non-correlated alternative investments of any kind are unlikely to be viewed as attractive when the S&P 500 sports a trailing 2-year Sharpe Ratio of 2.0 (far above the long-term average Sharpe Ratio of the stock market, which is closer to 0.5).[1] Put another way, no one thinks they need hurricane insurance when there hasn't been a storm in a few years.

No less a global macro investing authority than Stanley Druckenmiller[2] asserted that 2017 was "the worst year I've had relative to the set of opportunities out there," explaining that he "really, really mis-traded macro," and stating that he would have had a negative return for the year (for the first time in the history of his career!) had it not been for his sizeable holdings in technology stocks. (Liquid Alpha holds no such high beta investments, though CB&T clients certainly do in their equity portfolios.) We mention this not to excuse our own uninspiring absolute performance or because misery loves company, but because it underscores that the rules which have proven profitable in macro investing for the past several decades didn't generate great returns this year, in large part because some very strange things were going on in 2017.

To review the environmental drivers of Liquid Alpha and its value proposition: Volatility, sustained market trends (regardless of their direction), and wide valuation or interest rate differentials across asset classes and countries tend to create profitable investment opportunities for our managers. Extreme low volatility within narrow ranges, in the context of globally coordinated central bank policy and narrow interest rate differentials, on the other hand, does not benefit our managers. 2017 was perhaps the most anomalous year in financial history in this regard. A few pieces of trivia:

- **Stocks:** The S&P 500 rose in all 12 calendar months (first time in US history)
- **Volatility:** Realized 1-year monthly volatility of the S&P 500 was less than 4% (lowest level in history)
- **Bonds:** The Merrill Lynch MOVE Index, which measures the volatility of bond markets, like its equity market counterpart the VIX, fell to the lowest level in history
- **Credit:** US investment grade credit spreads fell to the lowest level since 2007 and European high yield spreads fell to their lowest level in history
- **Currencies:** Realized FX volatility approached all-time low levels seen in 2007 and 2014
- **Commodities:** Volatility for gold and oil fell to the lowest level in history and since the all-time lows in 2014, respectively

[1] The monthly Sharpe Ratio for the S&P 500 for 2017 was a preposterous 4.7. By way of comparison, the fraudulent track record which was used to market Bernie Madoff's Ponzi scheme was "only" a 2.7 Sharpe. By comparison, using Robert Shiller's S&P 500 data, which goes back to 1871, we calculate a monthly Sharpe Ratio of 0.31. This number rises to 0.62 when dividends are included.

[2] Druckenmiller is perhaps not as well-known as his former boss/partner, George Soros, but it was Druckenmiller who was behind Soros' famous (or infamous, depending on your point of view) short trade in the British pound in 1992 that "broke" the Bank of England and made over $1 billion in profit in a single day. Druckenmiller generated 30% annualized returns over his career and hedge fund manager Scott Bessent has called him "the greatest moneymaking machine in history."

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Against this backdrop, it's useful to revisit the primary goals of the strategy against our 2017 performance:

1. Make money over a market cycle. The fund made money in 2017 but has run well below target return of 8-10% since inception, in large part due to the environmental drivers described above. As long-term investors, we remain confident in the additive nature of the managers in our portfolio over a multi-year observation period, and believe the investment experience of the past 30 years is more indicative of the future than the investment experience of the last 30 months, weeks, or days.
2. Make money in a way that's uncorrelated to traditional investment portfolios. Life-to-date correlation to the S&P 500 and Barclays Bond Aggregate is -0.1 and 0.0, respectively. So it's safe to say the strategy has, for better or worse, looked nothing like the stock market over the past two years. In fact, the only two bursts of truly outsize performance to date came during the only stress periods for equities during that time (Jan/Feb 2016 and Brexit).
3. Provide the potential for downside diversification in market stress periods. There were no meaningful market stress periods in 2017, so we have to rate ourselves as "N/A" in this area last year.
4. A very mixed performance overall, but it's worth noting that even in one of the best periods in history for equities, and one of the most challenging periods for non-correlated strategies like managed futures, market-neutral, and global macro, a 20% allocation to Liquid Alpha has enhanced risk-adjusted returns for traditional portfolios. *(See table)*

	FY 2017	Since Inception (Jan 2016)	Sharpe Ratio (LTD)
Liquid Alpha	1.18%	0.18%	0.01
SG CTA Index	2.55%	0.04%	0.00
S&P 500	19.95%	30.35%	2.05
Barclays Aggregate	3.10%	6.20%	1.12
50 / 30 / 20 Stock / Bond / Alts	10.93%	17.22%	2.18

Source: Morningstar, CBandT estimates

We should also point out that the Liquid Alpha strategy, which was previously only available to CB&T trust clients, is now available in a Limited Partnership (LP) structure with the same liquidity and investment terms. This allows CB&T clients who hold assets in agency or retirement accounts to access the strategy, as well as investors who are not currently clients of the firm. If you have questions about the strategy and how it works to mitigate risk in your portfolio, please don't hesitate to contact us.

HOW WE MADE MONEY THIS YEAR

Whether it was the exponential and mystifying rise in the price of digital currencies and tokens, the New England Patriots' improbable Super Bowl comeback, or a US President who blasts out incendiary tweets on a daily basis, there was much that felt surreal in 2017. While the endless bid for US equities benefited the fund (Liquid Alpha made the bulk of its profits last year in equity index trading), remember that the S&P 500 is just one market out of about 250 tradable instruments in which our managers invest. Moreover, as discussed at the outset, the Liquid Alpha portfolio is purpose-built to avoid huge levels of equity beta. We believe most of our clients have enough stock market exposure elsewhere, and it's not the job of this fund to amplify that risk. Our focus is alpha (uncorrelated, diversifying excess returns) not levered market beta.

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Few macro markets exhibited sustained volatility and, outside of equities, most were generally range-bound. The fund made some profits from the downtrend in the US dollar, but other currencies proved trickier, trading in tight ranges and prone to whipsaw reversals. As a result of losses in the British pound sterling, Japanese yen, and assorted emerging market currencies, overall FX trading was a losing proposition in 2017.

Global fixed income trading was modestly profitable, but the opportunity set was depressed relative to long-term expectations due to the range-bound and whipsawing nature of US interest rates in 2017. Short rates trended well and provided some profitable opportunities, as did European bonds. However, US 10-year interest rates were stuck in a 2.1% to 2.6% trading range and finished the year almost exactly where they began it.

Commodities proved frustrating. There were some strong trends in energy, especially crude oil, but we failed to capture them in an efficient way. Though we profited from some of the strong moves seen late in the year, the momentum- and carry-based strategies employed by our managers were badly whipsawed and generated meaningful losses early in the year. Late year gains across many commodity markets pared these losses markedly, but commodities were still a net loser on the year.

	2017 Return
Global Equity Indices	3.29%
Global Currencies	-1.79%
Global Fixed Income	0.34%
Commodities	-0.65%
TOTAL	1.18%

Source: CBandT estimates

From a style attribution perspective, as might be expected in a year when every market correction was met with a flurry of dip-buying, short-term mean reversion strategies fared well. Carry strategies also benefitted from low volatility. A wise man once told us, "There are three states of the world: up, down, and unchanged." If momentum investing is a bet on past performance perpetuating into the future, and value or reversion investing is a bet on it reversing, than carry trades are bets on "unchanged": the status quo. As such, carry strategies were profitable across all four asset classes.

Strategies that generally showed lackluster performance were anything related to momentum. Trend-following, especially commodities, lost money in aggregate, though certain trend strategies with very long holding periods and/or very dynamic portfolio construction performed quite well. While there were some large moves in commodities in 2017 to be sure, their amplitude and cadence didn't lend themselves to being cleanly captured on the time scale over which most of our momentum strategies operate. The reversal in crude oil would be a good example of this: the first five months of the year were a choppy environment not conducive to trend strategies. Just when it appeared prices had broken decidedly lower in June, and most trendfollowers had established short positions, the market reversed higher, whipsawing them. It wasn't until October that prices moved decidedly above $50, creating the profitable trend trade we saw in 4Q17.

If we define trendfollowing strategies as seeking to capture market trends of 3-12 months, we can define momentum or breakout strategies as seeking to capture momentum moves of 3-10 days. These strategies did badly in 2017. Luckily, we have little exposure to such strategies in Liquid Alpha, and what we do have is embedded in large suites of models run by diversified managers.

HOW WE LOST MONEY THIS YEAR

Liquid Alpha faced some macro headwinds this year in the form of low volatility and whipsaw markets. We can skew toward different factors or style types, but these environmental factors are out of our control. In the world that's within our control, we made several timely tactical changes and portfolio management decisions that benefitted

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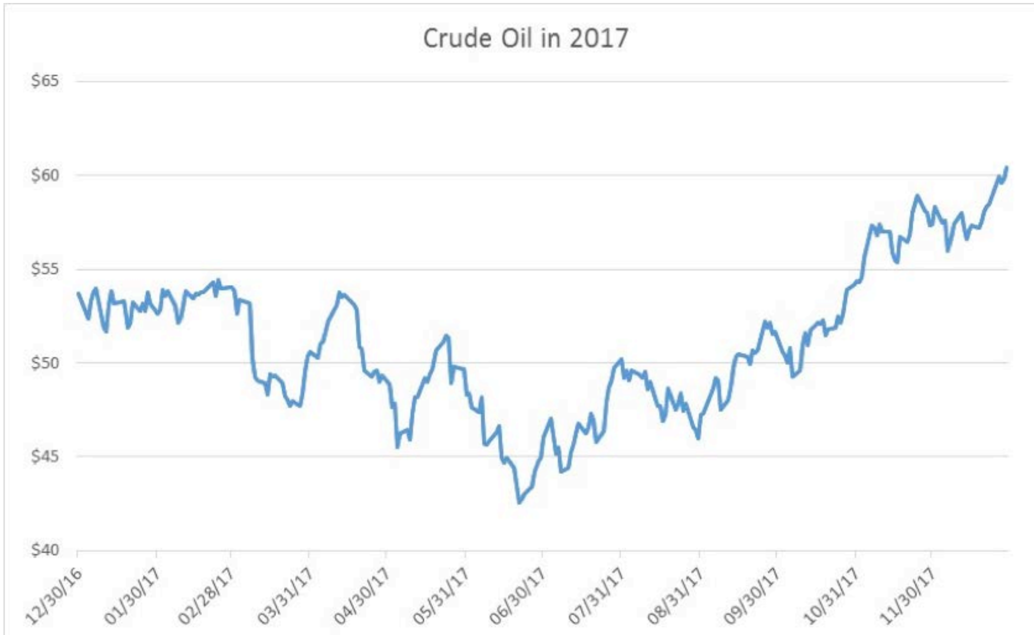

Source: Thomson Reuters

investors, but we also made some mistakes that provide learning experiences that we hope will make us better investors going forward.

Volatility is mean reverting, but it also tends to trade in structural regimes over periods of years. Over the past 3 years, we've had really only two significant stock market pullbacks. One was quite violent and sudden, but lasted less than a single week (when China devalued their currency in late August 2015). The other lasted for about the first 6 weeks of 2016, and also appeared to have been triggered by worries over China. After seeing both these sell-offs met with a wall of buying power, rather than worry, it was clear that liquidity was ample in the system, and we were not on the verge of a 2007/08 style crisis of confidence. As such, it would have made sense to increase the allocation to the only manager in our portfolio that has historically shown high exposure to the reversion factor. We were overly cautious, preferring to maintain fairly balanced factor diversification, and missed out on excess returns as a result. We are working on some process-based methods of refining our factor/style tilts within the portfolio that we think will improve returns in the future.

Within Liquid Alpha, we seek to discover and invest with niche managers that may not be on the radar of larger, less nimble allocators. This activity requires identifying managers that are high quality and institutional caliber, but aren't yet at institutional size. Allocate to a manager too soon in their life cycle, and one may get a good deal on fees and other investment terms, but take on excessive business risk, as well as potentially not having enough data points to adequately gauge the quality of a manager's process and performance. Wait too long, and an investor may miss out on the prime performance years of an emerging manager,[3] be unable to secure preferred investment terms or, in the case of capacity-constrained managers, miss out on the ability to invest with them entirely. This happened in spades this year as a very high quality manager which we'd been in discussions with for over a year hit their capacity targets and hard-closed their fund before we were able to hammer out investment terms with them. We couldn't arrive at a structure that worked for both sides before the investment window closed, and so we missed out on an accretive investment for the portfolio. Often the difference between making an investment and not is a very

[3] *Early-stage managers tend to outperformance late life-cycle ones, as shown in many academic studies, including this one: http://www.allaboutalpha.com/blog/2013/02/18/smaller-hedge-fund-managers-outperform-a-study-of-nearly-3000-equity-longshort-hedge-funds/.*

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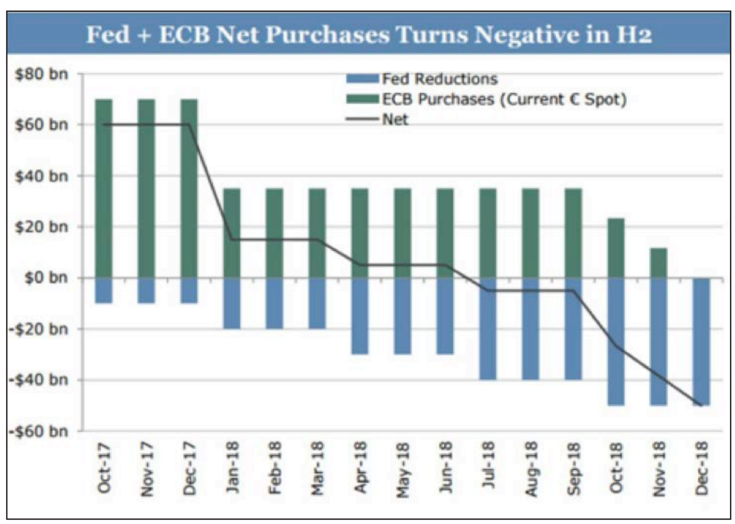
slim one. This is frustrating, especially given the time and energy we spent in due diligence on this manager. But opportunities are made up more easily than losses, so if we have to make one of these errors, better they be sins of omission rather than commission.

2018 OUTLOOK

It's hard to believe, but 2018 will mark a full decade since the Global Financial Crisis and the genesis of the unconventional monetary policy known as Quantitative Easing (a.k.a creating money out of thin air to buy financial assets). This massive, coordinated, and unprecedented injection of liquidity on the part of global central banks (CBs) has begun to reverse in the US, where the Fed stopped expanding their balance sheet in 2015, and has since hiked the Fed Funds rate from ostensibly zero to 1.5%. Importantly, the Fed embarked on "Quantitative Tightening" (though you won't hear Janet Yellen or Jay Powell call it that) this Fall, beginning to (ever so slowly) reduce the size of their $4.5 trillion holdings in Treasury and Agency bonds. It's now consensus thinking that QE was unambiguously bullish for stocks and credit. It's hard to see how the opposite policy can also be unambiguously bullish. The other major global CBs, namely the European Central Bank (ECB) and the Bank of Japan (BoJ), remain very much in easing mode, though this could change later in the year. In the case of the ECB, this is despite persistently better-than-expected economic data (no doubt one reason that the Euro currency appreciated relative to the dollar and European equities outperformed those in the US in 2017). In Japan, where QE has not been limited to bond purchases, the BoJ has become so aggressive and unconventional that they are now a top-10 holder of almost 90% of Japanese stocks. So 2018 looks to be a year of divergent CB policy, with the Fed determined to hike rates multiple times, while other CBs remain accommodative. Even so, liquidity and financial conditions in aggregate look set to tighten in 2H18.

While it may take time to percolate through the system, we believe that the reversal of the Fed's near-decade long policy of liquidity provision, the slowing of ECB bond-buying, and the reduction in Chinese fixed asset investment together represent a three-pronged attack that will likely lead to less complacent, more volatile, and more divergent markets.[4] This need not mean a widespread stock market sell-off. For instance, it's quite possible that a deliberate reduction in Chinese steel production, which is widely anticipated in 2018, will lead to tighter commodity markets and a blow-off rally in certain resource stocks. Or, rather than equities, it could be bonds that are surprisingly weak. Regardless, within Liquid Alpha, we remain committed to combining uncorrelated macro investment strategies that generate reasonable returns over a market cycle, with little to no correlation to the rest of client portfolios, and maintain the potential to generate "crisis alpha" when markets enter extreme environments, be they deflationary or inflationary. Thank you for your support and best of luck in 2018.



Source: Wells Fargo Securities, Bloomberg, Doubleline

[4] *Year-on-year growth of fixed asset investment in China has decelerated from over 15% just 3 years ago, and 10% in 2016, to 7.2% in December 2017.*