KATHMERE
CAPITAL MANAGEMENT

2023 Year End CIO Market & Economic Perspectives

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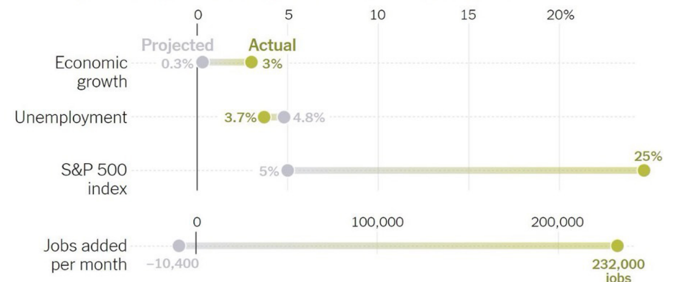
Market and Economic Recap

Economy: The Recession That Didn't Arrive

The most important economic theme of 2023 was the widely anticipated US recession that never came. Coming into the year, it was a near consensus expectation that the Fed's rate hikes designed to bring inflation back under control from multi-decade highs would tip the economy into a recession as higher interest rates would limit borrowing, increase the cost of capital, encourage saving and ultimately stifle economic activity.

As 2023 came and went, the Fed's rate hikes continued — the Fed raised rates by a quarter percentage point on four occasions and brought their target policy rate to the highest it's been since 2007 — and yet a recession never came.

Instead, **the economy demonstrated remarkable resilience in 2023** with significantly stronger growth, more job creation, lower unemployment and far better stock market performance than projected as shown in the graphic below from the New York Times. And all of this occurred while inflation steadily and materially cooled throughout the year.



Source: "More Than Words: 10 Charts the Defined 2023." New York Times. 12/28/2023.

One question I've frequently received from investors has been: how has the economy avoided a recession despite the Fed's unrelenting rate hikes? I believe are few factors played a significant role in disrupting the transmission of monetary policy, including:

- **Household resilience.** Consumers broadly accumulated a massive build-up of savings that bolstered their balance sheets and supported ongoing spending. In addition, consumers have benefitted greatly from inexpensive long-term, fixed-rate loans (e.g., 30-year mortgages) that have shielded them from higher interest rates.
- **Corporate resilience.** Like households, companies have yet to fully feel the impact of higher interest rates as large-cap companies extended the maturity of their borrowing and locked in low rates amid the lower rates that persisted prior to the start of 2022.
- **Fiscal easing.** The federal government has continued to run substantial budget deficits which provide a near-term boost to consumption and investment activity. Notably, the Bipartisan Infrastructure Law, the CHIPS Act and the Inflation Reduction Act — all enacted between November 2021 and August 2022 — have contributed to a surge in energy transition and manufacturing investment.

Ultimately, however, it takes some time for monetary policy actions (e.g., rate hikes) to affect the macroeconomy. Economist and Nobel laureate Milton Friedman originated this concept when he said that "monetary changes have their effect only after a considerable lag and over a long period." He further added that this lag is "rather variable." Thus, it's been said that **monetary policy operates with "long and variable lags."**

In my view, **monetary policy simply hasn't been restrictive enough for long enough to significantly impact the economy yet.** While the Fed has raised rates aggressively to levels not seen in more than a decade, rates haven't been high for very long — remember, the Fed didn't begin its current hiking cycle until March 2022.

With that in mind, it's worth pointing out that some signs for concern have started to emerge in the economic data. In recent months, we've seen that higher interest rates combined with the impact of the series of regional bank failures during the first half of the year has led to a broad-based drop in the demand for borrowing plus a notable tightening of lending standards by banks to both consumers and businesses alike. The real-world implication is that every day there are consumers and business that cannot get a new loan or refinance a maturing loan. And, for those fortunate to secure a new loan, they must pay significantly more for it. This is the reality of what the Fed has been seeking to accomplish with its rate hikes — it is deliberately trying to raise the cost of capital to slow down financings and ultimately growth and inflation.

As a result, we've started to see a rise in delinquencies and defaults among both consumers (e.g., credit cards and auto loans) and corporations (e.g., bonds and loans), albeit from historically low levels in both cases. In addition, a variety of indicators are showing ongoing signs of weaking in labor markets.

Looking forward, **I expect that the market will remain fixated on inflation's trend and on the outlook for Fed policy.** As mentioned at the outset, during the second half of 2022 and into 2023, concerns about inflation fanned fears about Fed policy become overly restrictive and driving the economy into a recession. In recent months, the welcome combination of sustained economic growth and cooling inflation has all but vanquished those fears. **Markets have instead become optimistic (possibly even certain) that the inflation dragon has been slayed** and that as a result, **the Fed will be able to execute its "pivot" and shift its priorities from fighting inflation to focusing on supporting economic growth.**

Markets are now expecting that the Fed will preemptively cut rates in 2024 and that doing so will forestall the worst of the negative impact from the Fed's past hikes and will enable economic growth to be sustained through 2024 and beyond. The consensus expectation for 2024 now is for continued economic growth, low inflation and lower interest rates. It's somewhat surprising to me that there seems to be so much investor conviction in this outcome and so little concern that economic growth will deteriorate further or that inflation proves stickier than expected.

It follows then that **a key risk to the economic and market outlook for 2024 is a resurgence in inflation which forces the Fed to once again prioritize fighting inflation** at the expense of focusing on supporting economic growth via rate hikes.

Beyond monetary policy and inflation, there is, of course, a usual list of other potential recession triggers that bear monitoring closely. These include a disruption to global oil supplies from escalating conflicts in the Middle East and beyond, a potential conflict directly involving China and ongoing political instability as home. However, for now, even as recession risks gradually rise, **it is still quite possible for the surprise good times of 2023 to be extended into 2024 and beyond.**

Stocks: A "Magnificent" Bounce Back Performance

The cooling of inflation from its multi-decade highs and the resiliency of the US economy helped to drive **a bounce back performance for stocks globally in 2023.** For the year, global equity markets were up 23%, led by the US (+26%) with foreign developed markets (+19%) and emerging markets (+10%) both lagging in relative terms yet still delivering double digit gains for the year. As of the end of the year, **both US and foreign developed markets were hovering around their all-time highs.**

Within equity markets, **the story of 2023 was the exceptionally strong performance of seven mega-cap tech and tech-adjacent stocks (the "Magnificent Seven" – Apple, Microsoft, Amazon, Alphabet, Meta, NVIDIA and Tesla).**

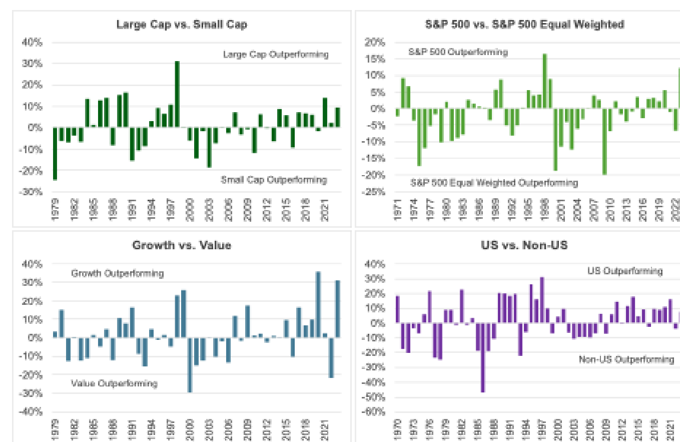
As the chart below demonstrates, an index of mega-cap growth companies (of which the Magnificent Seven companies currently comprise nearly 60% of the index) gained more than 50% in 2023, nearly doubling the S&P 500's 26% gain. Meanwhile, an equal-weighted version of the S&P 500, which is a good proxy for the performance of the average stock in the market, gained 14%, while small-cap stocks gained 17%. Notably, both the equal-weighted and small-cap indexes were in negative territory for the year as late as early November prior to rallying strongly to finish the year with double-digit gains.

> "The resiliency of the US economy helped to drive a bounce back performance for stocks globally in 2023."

> "As of the end of the year, both US and foreign developed markets were within an earshot of their all-time highs on a total return basis."

As a direct result of the market's top-heavy, mega-cap growth leadership, **there was a historically wide divergence between stock market performance across company size, styles and geographies.**

- **Large caps vs. small caps.** The S&P 500 (large caps) outperformed the Russell 2000 (small caps) by 9% in 2023. In the last 30 years, large cap outperformance has only been greater two times: 1998 (large caps outperformed by 31%) and 2021 (14%).
- **Market-cap weighted vs. equal weight.** The S&P 500 outperformed its equally weighted version by 12% in 2023, marking the 2nd largest outperformance of the cap-weighted version on record going back to 1971 (only 1998 was larger with a 16% gap).
- **Growth vs. value.** Growth stocks (Russell 1000 Growth Index) outperformed value stocks (Russell 1000 Value Index) in 2023 by 31%, which was the 2nd largest annual outperformance on record going back to 1979 (only 2020 saw a larger gap of 36%).
- **US vs. non-US.** US stocks (S&P 500 Index) outperformed non-US stocks (MSCI World ex USA Index) by 8% in 2023. Since 2009, the US has outperformed in 11 out of the last 14 years.



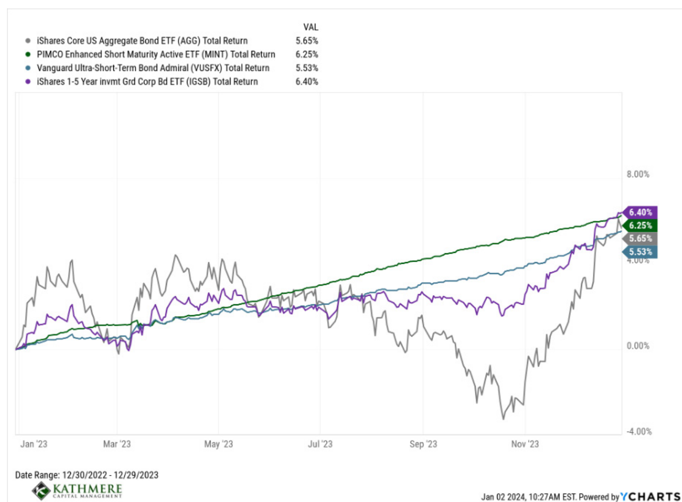
Source: Ycharts and Dimensional Fund Advisors Returns Web.

Outside of US borders, positive performance was far more widespread and style performance favored value and small caps over growth and large caps in both developed and emerging markets.

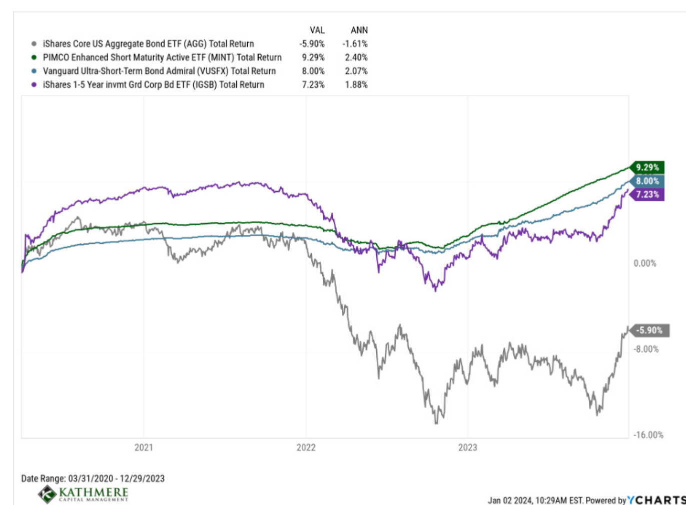
Bonds: Fourth Quarter Rally Saves the Day

Much like stocks, after last year's historic losses, bonds didn't have too high of a bar to clear to deliver an improvement upon 2022. It was a wild ride for bond investors, but through it all, thanks to higher starting yields and a fourth quarter rally the **bond market avoided registering an unprecedent third consecutive year of losses.**

Once again, **ultra-short-term and short-term bonds — which is where our clients' core bond holdings are and have been exclusively invested — delivered returns that either matched or exceeded the broad market.** And they did so while delivering a considerably smoother ride along the way as shown in the chart below.



Looking back further, **short-term bonds have significantly outperformed the broad market since interest rates moved to historically low levels during the depths of the pandemic-induced market crises in March 2020.** It was around this time, when the 10-year Treasury yield moved below 1%, that we shifted our positioning to favor the types of bonds based on our view that we didn't believe investors in intermediate- and longer-term bonds were being adequately compensated for the risk of rising interest rates. We felt that these types of bonds had become "return-free risk," an inversion of the conventional view of high-quality bonds as a source "risk-free return." Ultimately, our view has been proven correct over the last few years as the chart below demonstrates.



Looking forward, for core fixed income allocations, we continue to remain biased towards short-term bonds (i.e., those with five years or less to maturity). In recent months, however, we slightly altered our positioning to modestly increase the maturity profile of bond holdings to effectively "lock-in" the high yields available on slightly longer term, but still short-term bonds. We continue to believe this move is prudent given the current level of yields and the outlook for monetary policy as described previously.

> "Once again, ultra-short-term and short-term bonds—which is where our clients' core bond holdings are and have been exclusively invested—outperformed the broad market."

Long Term Capital Markets Assumptions Round Up

At this time of the year, I always like to pull together a round-up of the long-term capital markets assumptions published by a selection of leading global asset managers. These estimates are published by the asset managers to assist investors with their strategic allocation and planning decisions and with setting appropriate, grounded-in-reality medium-term return expectations. I cannot emphasize enough that they are highly uncertain and importantly are not intended for market timing.

Disclaimers aside, presented below are the expected annualized compounded return expectations for a variety of major asset classes over the next 10 years and beyond from J.P. Morgan, BlackRock and Vanguard.

I chose to present these because, in addition to being household names familiar to most all investors, I've found that their methodologies — while modestly different — are all sensible and grounded in solid economic logic.

Broadly speaking, these forecasts are based on the empirically demonstrated fact that over intermediate horizons such as 10 years or so, initial market yields and valuations tend to be the most important driver of returns. Over longer periods (i.e., multiple decades) the impact of starting yields and valuations is diluted and theory and long-term historical returns matter more for forecasting returns. For shorter horizons (i.e., less than 5 years) returns are largely unpredictable.

	JP Morgan *Long-Term*	**BlackRock** *10 Years*	**Vanguard** *10 Years*	**Average**
Stocks				
US Large Cap	7.0	5.2	5.2	5.8
Non-US Developed Markets	9.2	9.7	8.0	9.0
Emerging Markets	8.8	9.1	7.6	8.5
Bonds				
US Treasury Bonds	3.9	4.5	4.9	4.4
US Aggregate Bonds	5.1	5..0	5.3	5.1
US Investment Grade Bonds	5.8	5.0	5.8	5.5
US High Yield Bonds	6.5	6.8	6.9	6.7
Bank Loans	6.5	8.0		7.3
Private Credit				
Private Credit	8.5	10.0		9.3
Real Estate				
US REITs	8.2		5.6	6.9
US Core Real Estate	7.5			7.5
US Value-Addded Real Estate	9.7			9.7
Private Equity				
Private Equity-Buyouts	9.7	6.6		8.2
Cash				
US Cash	2.9	4.1	4.6	3.9
Inflation				
US Inflation	2.5		2.5	2.5

Source: J.P. Morgan, BlackRock and Vanguard. All forecasts as of 9/30/2023.

While the individual forecasts are no doubt varied, a few general observations are worth highlighting.

- **Stocks.** US large cap returns are broadly expected to be unimpressive relative to the long-term average of 10% or so. Meanwhile, both developed and emerging markets are uniformly expected to outperform (more on this later).
- **Core bonds.** Bonds are back. Short-term pain can lead to long-term gain. The return outlook for treasury, aggregate and investment-grade bonds is much improved relative to a few years ago due to today's higher yields — a significant silver-lining for bond investors after enduring a challenging past few years.
- **Credit.** Both publicly traded high yield bonds and loans as well as private credit appear very attractive given the current yield environment and have the potential to offer equity-like performance that's considerably less volatile and is contractual (more on this later).

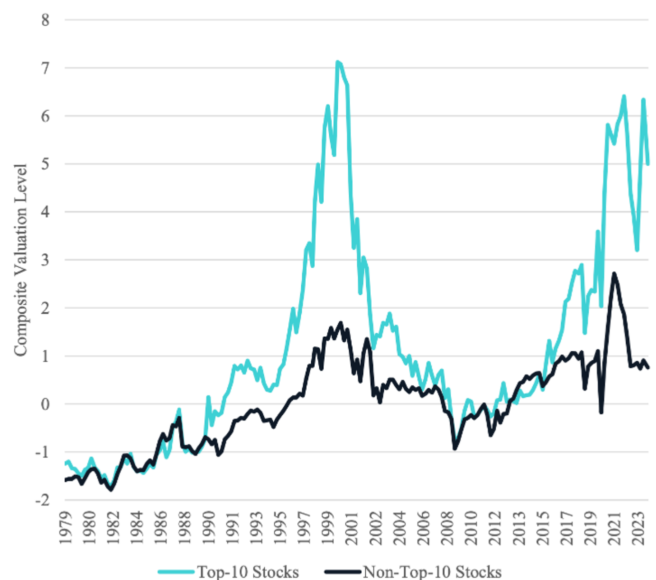
US Stocks: Concerning Concentration and Mega-Cap Valuations

The high recent returns for the Magnificent Seven have once again given rise to a concern I was last warning investors about in earnest for much of 2021 — the stock market's increasing dependence on a narrow selection of companies.

Market concentration of the largest stocks in traditional market indexes is currently at its highest levels in history, more pronounced than even during the recent peak in 2021 and during the late stages of dot-com bubble in the late 1990s, as shown in the chart below from Goldman Sachs.

Source: "A Historical Perspective on the Recent Outperformance of Mega-Cap Stocks." Goldman Sachs Asset Management. November 2023.

While today's mega-cap companies are undoubtably more fundamentally sound than their predecessors during the .com era and generate billions in earnings and cash flow, their dominance in traditional indexes is nevertheless concerning for investors. These concerns are magnified by the fact that **today's largest companies are currently very expensive compared to the rest of the large cap universe** based on a combination of valuation metrics (i.e., price-to-earnings, price-to-sales and price-to-book ratios) as demonstrated in the chart below from Goldman Sachs.



Source: "A Historical Perspective on the Recent Outperformance of Mega-Cap Stocks." Goldman Sachs Asset Management. November 2023.

History has demonstrated that past periods of similar concentration and expensive valuations have led to trying times for market averages and the previous market titans. Specifically, the unraveling of the dot-com bubble began in early 2000 and ushered in a bear market that lasted two and half years. The leadership coming out of that downturn was much different from the technology and telecommunications cohort that led previously. More recently, markets experienced a similar rotation out of mega cap leadership last year which resulted in a comparatively brief bear market that saw growth stocks underperform value stocks by more than 20 percentage points as many of the pandemic era's winners came crashing back to reality.

Ultimately, the outsized influence of the market's largest companies on market indexes magnifies the scrutiny of their fundamentals which leads to justified worries that any blemishes or misses relative to lofty expectations could be a catalyst for more difficult times ahead.

Fortunately for investors, there are alternatives to traditional capitalization-weighted indexes that reduce the outsized influence of the largest stocks in the market and, in my view, offer higher potential returns in the future. In our clients' portfolio, we utilize a variety of factor-tilted "active index" strategies that systematically emphasize stocks with characteristics associated with historical outperformance (e.g., cheap valuations, high profitability and strong recent past performance) while simultaneously de-emphasizing those with the opposite characteristics as well as equal-weighted strategies. Both types of strategies reduce the outsized influence of any single stock within investor portfolios while still preserving the many of the key benefits of traditional indexing — broad diversification, low costs and a rules-based approach to security selection and rebalancing.

Non-US Stocks: Still Cheap and a Possible Refuge from US Concentration and Valuation Concerns

Non-US stocks can appropriately be described as an asset allocator's purgatory for much of the last decade. As mentioned earlier, non-US stocks have trailed their US counterparts in 11 of the last 14 years since the start of 2010. When considering their non-US allocations, it's quite reasonable for investors to ask: "why bother?"

I believe that non-US stocks play an important role in equity portfolios today for two key reasons:

1. **Diversification:** Absent a crystal ball that tells us exactly how the future will unfold and where returns will come from, the best we can do is to diversify so that we can ensure that we have exposure to the areas of the markets that deliver those returns.
2. **Return potential:** I believe that better times are indeed ahead for non-US stocks — a belief that we saw in an earlier section is share by the world's largest asset managers — the rationale for which I describe below.

It's a matter of arithmetic that the rate of return received by an investor over a given period for an index (or basket) of stocks is simply the dividends received from those stocks plus the change in the prices of those stocks. Price changes are ultimately a function of growth in earnings per share and changes in the multiple paid for those earnings (i.e., the price-to-earnings ratio). Put differently, price changes are a function of fundamental growth and valuation growth. Investments in foreign stocks are also subject to changes in the value of foreign currencies relative to the US dollar.

Since the beginning of 2010, when US stocks began their sustained run of outperformance vs. non-US stocks (developed markets), through the third quarter of 2023, the composition of returns has been as follows:

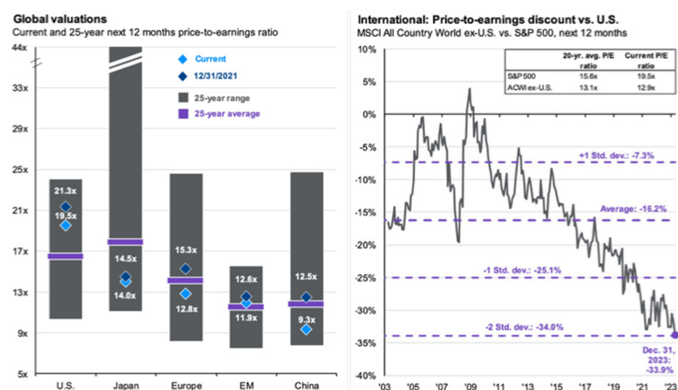
- **Dividends:** Non-US stocks delivered modestly higher dividends of 3.1% per year vs. 1.9% for US stocks.
- **Fundamental growth:** The US incrementally outperformed, delivering earnings per share growth of 7.6% per year vs. 6.4% for non-US.
- **Valuation growth:** US returns were boosted to the tune of 0.6% per year by multiple expansion (P/E ratios increasing) while non-US markets saw changes in valuations subtract 3.3% per year from performance as their P/E ratios progressively cheapened.

- **Currency movements**: The relative strengthening of the US dollar (and weaking of foreign currencies) served as a further drag on non-US performance as currency movements detracted 3.0% per year from non-US performance, respectively.

Ultimately, over the last 14 years, the combination of valuation changes and currency movements was responsible for of the nearly the entirety of the approximately 7% per year performance shortfall of non-US developed markets stocks vs. the US. In other words, **the US' outperformance over the last decade plus has been largely driven by the US getting more expensive vs. non-US and the US dollar appreciating relative to foreign currencies.** Had valuations and currencies not changed over the last 14 years, performance would have been more or less the same.

This is important as valuations and currency movements tend to be mean reverting over time. To the extent that valuations and currency movements hurt foreign stocks' relative performance over the last 14 years, they're likely to help during the next 14 years. At a minimum, it's highly unlikely that they continue to detract from relative performance to the same extent as they have in the recent past.

The case for mean reversion — and thus foreign outperformance — is further bolstered by the fact that **foreign stocks currently trade at historically discounted valuations vs. the US,** as shown in the charts below from J.P. Morgan. At the same time, **foreign currencies similarly appear cheap vs. the US dollar** when adjusted for inflation dynamics.



Source: "Guide to the Markets – U.S." J.P. Morgan Asset Management. Data as of December 31, 2023.

"Non-US stocks delivered modestly higher dividends of 3.1% per year vs. 1.9% for US stocks."

"Non-US stocks can appropriately be described as an asset allocator's purgatory for much of the last decade. As mentioned earlier, non-US stocks have trailed their US counterparts in 11 of the last 14 years since the start of 2010. When considering their non-US allocations, it's quite reasonable for investors to ask: "why bother?""

A decade plus of underperformance from foreign stocks has rightfully caused many investors to question the wisdom of a globally diversified approach to investing. As a general perspective, I always advocate for global diversification simply based on the recognition that absent a crystal ball, the best we can do is to diversify thoughtfully. That said, I believe the case for investing beyond US borders is today stronger than average. As I see things today:

- The US market is historically concentrated among the largest companies...
- ...and the largest companies are expensively valued relative to the rest of the large-cap universe.
- As a result, the overall US market is trading at historically rich valuations.
- Meanwhile, valuations on non-US stocks are more attractive...
- ...and the US dollar appears to be overvalued on a fundamental basis (relative to foreign currencies) and thus faces more headwinds than tailwinds in the coming decade.

Accordingly, **I believe global diversification is of increased importance today and offers investors a potential refuge from high concentration and expensive valuations.**

The Case for Public and Private Credit Amid High Rates

Over the last century, since 1926, US stocks, as measured by the S&P 500 Index have returned just over 10% per year. Today, high yield bonds and leveraged loans offer yields of 8.3% and 9.7%, respectively. Private loans carry even higher yields presently approaching 12%. Thus, pre-tax yields on non-investment grade public and private debt investments now approach or exceed the historical returns delivered by stocks. And those are historical returns. As we saw earlier, expectations for US large cap stock returns over the next decade are muted relative to the long-term historical record. Thus, because the sharp move higher in interest rates that's occurred over the last two years, **investors today have an opportunity to earn equity-like returns from investments in below-investment grade bonds and loans.**

And importantly, the returns from bonds and loans are contractual based on the contract between the lender and the borrower. The lender gives the borrower money up front; the borrower pays the lender interest payments along the way; and the borrower pays back the principal balance at the end. If the borrower doesn't make good on their payments, the lender gets to take ownership of the company and its assets via the bankruptcy process. **The credit investor (i.e., lender) thus isn't dependent on the movements of the markets for their returns.**

Stock returns, on the other hand, particularly over the short- to medium-term, are driven by stories and the overall behavior of the market. As Ben Graham (Warren Buffett's mentor and teacher) put it, if Mr. Market is in a good mood, stock returns benefit and if he's in not such a good mood, stock returns suffer. Ultimately, the difference between the sources of returns from stocks and bonds is profound.

For investors, the bottom line is that credit (public and private) offers prospective returns today that:

- are highly competitive relative to historical returns on stocks,
- better than prospective returns on US large cap stock indexes,
- are contractually driven and thus much less uncertain than stock returns, and
- exceed many investor's target returns.

We've been advocating for private credit to play a larger role in portfolios for a few years now — back before private credit became the increasingly mainstream investment it is today. Today's higher interest rates have continued to increase the appeal of credit investments as it's been some time since the prospective returns on credit were this attractive on both an absolute and relative basis. As a result, **I continue to believe that serious consideration should be given to credit investments — both public and private — in diversified portfolios today.**

> "Pre-tax yields on non-investment grade public and private debt investments now approach or exceed the historical returns delivered by stocks."

Kathmere Capital Management
Long-Term Outlook and Positioning

Reserve	Risk-Aware Growth	Long-Term Growth
Bonds & Cash Equivalents • Future return outlook has significantly improved over the last two years due to higher prevailing interest rates. • Minimize exposure to traditional, core intermediate-duration fixed income in favor short-duration strategies that strike an appropriate balance between reinvestment risk and interest rate risk. • Bias toward high quality securities given modestly tight credit spreads and uncertain economic outlook. • Emphasis remains on safety and preservation of capital.	**Credit** • Publicly-traded and private credit appear to be attractive relative to public stocks on a risk-adjusted basis owing to today's higher prevailing interest rates/yields. **Real Assets** • Tangible core real asset exposure including real estate, infrastructure, timberland and farmland may serve as a potential hedge against sustained high inflation and as an effective complement to traditional fixed income allocations. **Risk-Managed/Hedged Equity** • Attractive complement to a core equity portfolio in a potentially range-bound equity market over the intermediate-term horizon.	**Public stocks** • Public stocks provide attractive long-term opportunity to capture the risk premia from profit-creating enterprise. • Continue to tilt away from expensively-valued mega-cap U.S. stocks and towards relatively more attractively valued areas of the market. • Overweight value strategies globally relative to cap-weighted indexes. • Overweight non-US developed and emerging markets relative to US markets due to comparatively more attractive valuations. **Private equity** • Private equity offers further opportunity for diversification and return enhancement for public equity heavy investors.

2023 Year End CIO Market & Economic Perspectives

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Economic forecasts set forth may not develop as predicted and there can be no guarantee that strategies promoted will be successful.

There is no guarantee that a diversified portfolio will enhance overall returns or outperform a non-diversified portfolio. Diversification does not ensure against market risk. Asset allocation and diversification do not assure or guarantee better performance and cannot eliminate the risk of investment losses.

Tactical allocation may involve more frequent buying and selling of assets and will tend to generate higher transaction cost. Investors should consider the tax consequences of moving positions more frequently.

Stock Investment Risk

Stock investing involves risk including loss of principal.

Investing in stock includes numerous specific risks including: the fluctuation of dividend, loss of principal and potential illiquidity of the investment in a falling market.

Investing in foreign and emerging markets securities involves special additional risks. These risks include, but are not limited to, currency risk, geopolitical risk, and risk associated with varying accounting standards. Investing in emerging markets may accentuate these risks.

Currency risk is a form of risk that arises from the change in price of one currency against another. Whenever investors or companies have assets or business operations across national borders, they face currency risk if their positions are not hedged.

Bond Investment Risk

Bonds are subject to market and interest rate risk if sold prior to maturity. Bond and bond mutual fund values and yields will decline as interest rates rise and bonds are subject to availability and change in price.

Government bonds and Treasury bills are guaranteed by the U.S. government as to the timely payment of principal and interest and, if held to maturity, offer a fixed rate of return and fixed principal value. However, the value of fund shares is not guaranteed and will fluctuate.

High-yield/junk bonds are not investment-grade securities, involve substantial risks, and generally should be part of the diversified portfolio of sophisticated investors.

Municipal bonds are subject to availability, price, and to market and interest rate risk if sold prior to maturity. Bond values will decline as interest rate rise. Interest income may be subject to the alternative minimum tax. Federally tax-free but other state and local taxes may apply.

Investing in foreign and emerging markets debt securities involves special additional risks. These risks include, but are not limited to, currency risk, geopolitical and regulatory risk, and risk associated with varying settlement standards.

Alternative Investments Risk

Alternative strategies may not be suitable for all investors and should be considered as an investment for the risk capital portion of the investor's portfolio. The strategies employed in the management of alternative investments may accelerate the velocity of potential losses.

Investing in real estate/REITs involves special risks such as potential illiquidity and may not be suitable for all investors. There is no assurance that the investment objectives of this program will be attained.

Commodity-linked investments may be more volatile and less liquid than the underlying instruments or measures, and their value may be affected by the performance of the overall commodities baskets as well as weather, geopolitical events, and regulatory developments.

The fast price swings of commodities may result in significant volatility in an investor's holdings.

There is a risk of substantial loss associated with trading commodities, futures, options, derivatives and other financial instruments. Before trading, investors should carefully consider their financial position and risk tolerance to determine if the proposed trading style is appropriate. Investors should realize that when trading futures, commodities, options, derivatives and other financial instruments one could lose the full balance of their account. It is also possible to lose more than the initial deposit when trading derivatives or using leverage. All funds committed to such a trading strategy should be purely risk capital.

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