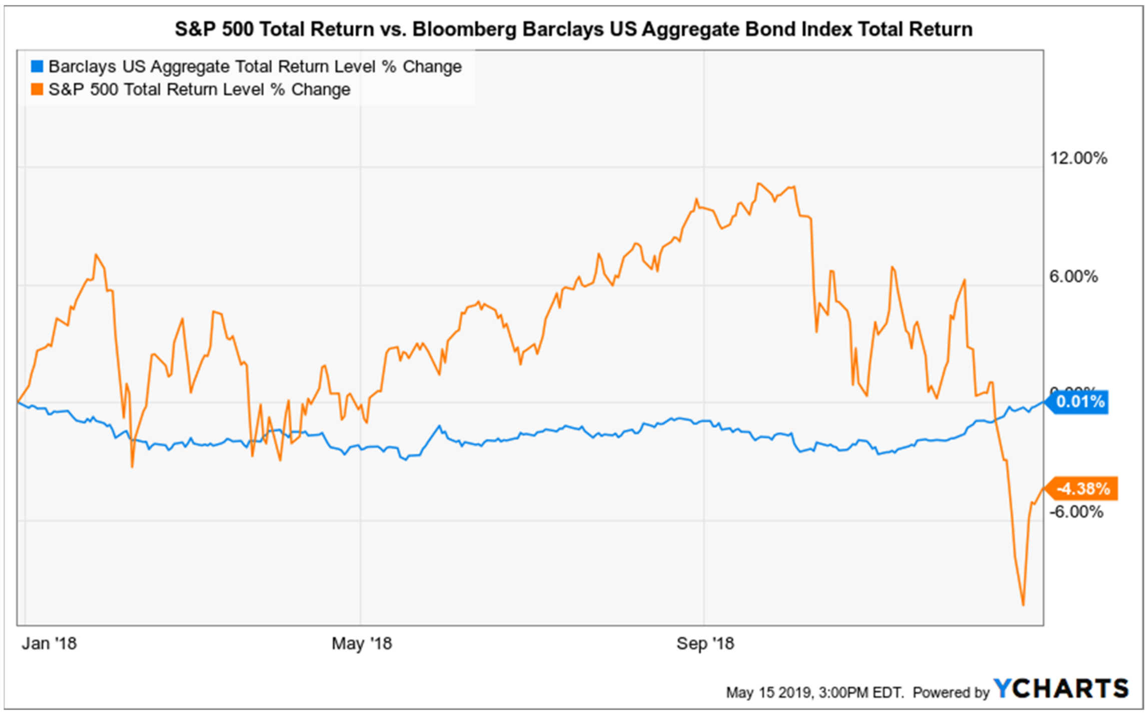
AGGravation: Exploring the limitations of the traditional core bond benchmark

May 2019

The standard benchmark for fixed income is the Bloomberg Barclays Aggregate Bond Index or the "Agg." The index ignores a vast amount of the world of fixed income, however.

Last year while the equity markets took investors on a wild ride, the Agg plodded along and eked out a 1 basis point gain on the year. While performance in the Agg was much more palatable than the 20% swing from peak to trough in the S&P, opportunities in the fixed income markets were missed.[1]



Investors cannot directly invest in an index and unmanaged index returns do not reflect any fees, expenses or sales charges. Past performance is no guarantee of future results.

What is wrong with the Agg?

The Agg is generally considered to be representative of the broad bond market. While this is true on a total debt outstanding basis, the reality is that its composition is highly concentrated in treasuries and government-related securities. In 2018, the Agg was comprised of nearly 70% of these types of

[1] Ycharts.com

securities and in 2019, that number has crept above 70% as of April.[2] The result of this is higher correlation risk and yields that revert to the mean which in this case is the US 10-Year treasury note. One of the pitfalls of the Agg is the high correlation of its largest components. In 2018, the two largest components, Treasuries and Agency MBS, were over 90% correlated for the majority of the year.

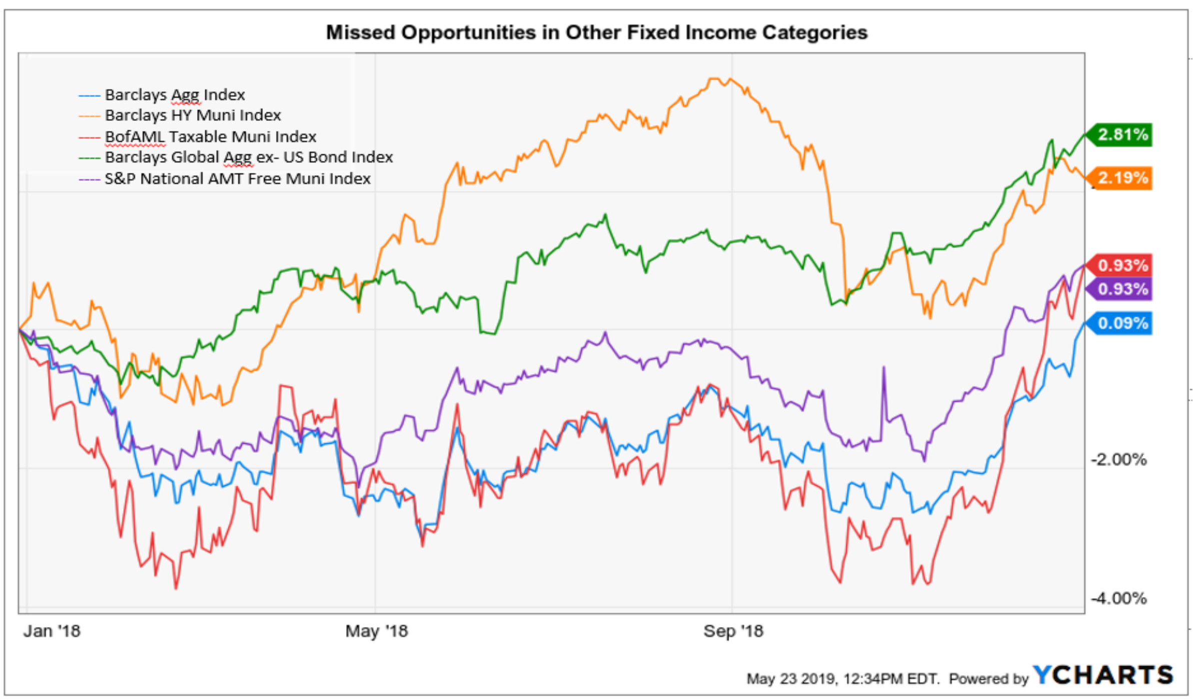
Missed opportunities in other segments of the bond market!

Although the Agg is the standard benchmark for fixed income strategies, the limitations of the index as a true barometer of the overall bond market are fairly stark.

Excluded from the Agg are:

- Munis (investment grade, high yield, and taxable)
- Preferred stock
- Bank loans
- High yield bonds
- Foreign bonds (developed & emerging of any credit quality or currency denomination)
- Convertible bonds

While the Agg returned its solitary basis point of performance in 2018, some of the other asset classes listed above fared much better. International bonds (investment grade), investment grade munis, high yield munis, and taxable munis all had positive total return in 2018.



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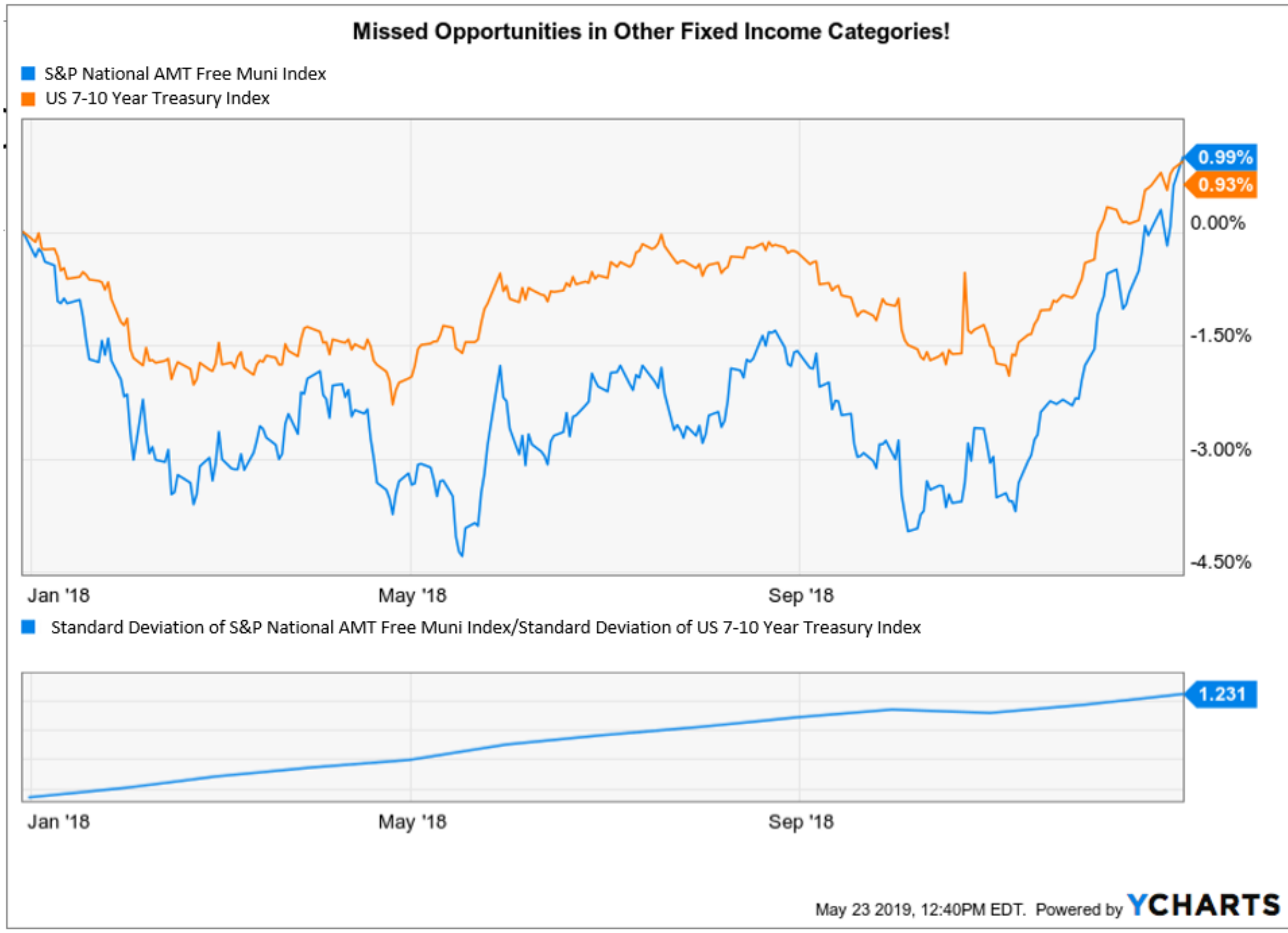
[2] Columbia Threadneedle & State Street Global Advisors

To examine one scenario, the National Muni Index delivered virtually the same performance (93bps vs 99) as the 7-10 Year Treasury Bond Index with less volatility (std. dev.) on a total return basis.[3]



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The ACM approach

What is the solution? A manager whose discipline is designed with flexibility to allocate to the asset classes not included in the Agg. The ACM Tactical Income Fund does not have a mandated percentage of the portfolio that must be invested in traditional core bond holdings like the Agg. Rather, the ACM Tactical Income Fund invests across 17 different income-oriented asset classes.

[3] Ycharts.com & JP Morgan Chase

How we do it:

1. Reduce correlation risk by limiting position sizes and allocating to excluded sectors
2. Prioritizing the highest yielding positions

The ACM Tactical Income Fund's investment mandate applies these rules to portfolio construction. The Fund invests in all the core asset classes that make up the Agg, but the process goes further. Our tactical discipline seeks to avoid over correlation by limiting positions at 12%. Additionally, we prioritize our allocations based on yield which, in some circumstances, can result in a higher yield than the Agg due to our use of asset classes that are excluded from the Bloomberg Barclays Aggregate Bond Index.

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Important Risk Information

Investors should carefully consider the investment objectives, risks, charges and expenses of the ACM Tactical Income Fund. This and other important information about the Fund is contained in the prospectus, which can be obtained by calling 1-844-798-3833. The prospectus should be read carefully before investing. The Tactical Income Fund is distributed by Northern Lights Distributors, LLC, member FINRA/SIPC. Northern Lights Distributors, LLC and Ascendant Capital Management, LLC are not affiliated.

Mutual Funds involve risk including possible loss of principal. Adverse changes in currency exchange rates may erode or reverse any potential gains from the Fund's investments. ETF's are subject to specific risks, depending on the nature of the underlying strategy of the fund. These risks could include liquidity risk, sector risk, as well as risks associated with fixed income securities, real estate investments, and commodities, to name a few. Investments in underlying funds that own small and mid-capitalization companies may be more vulnerable than larger, more established organizations. Derivative instruments involve risks different from, or possibly greater than, the risks associated with investing directly in securities and other traditional investments. Investments in foreign securities could subject the Fund to greater risks including, currency fluctuation, economic conditions, and different governmental and accounting standards. In addition to the risks generally associated with investing in securities of foreign companies, countries with emerging markets also may have relatively unstable governments, social and legal systems that do not protect shareholders, economies based on only a few industries, and securities markets that trade a small number of issues.

Investors bear the risk that the Fund may not be able to implement its investment strategies or attract sufficient assets. Purchased put options may decline in value or expire worthless and may have imperfect correlation to the value of the Fund's portfolio securities. Written call and put options may limit the Fund's participation in equity market gains and may amplify losses in market declines. The Fund's losses are potentially large in a written put or call transaction. If unhedged, written calls expose the Fund to potentially unlimited losses. The Fund will incur a loss as a result of a short position if the price of the short position instrument increases in value between the date of the short position sale and the date on which an offsetting position is purchased. Short positions may be considered speculative transactions and involve special risks, including greater reliance on the ability to accurately anticipate the future value of a security or instrument. The Fund's losses are potentially large in a short position transaction.

Investors are not able to invest directly in the indices referenced in this illustration and unmanaged index returns do not reflect any fees, expenses or sales charges.

Definitions:

Bloomberg Barclays Aggregate Bond Index: The Bloomberg Barclays US Aggregate Bond Index is a broad-based flagship benchmark that measures the investment grade, US dollar-denominated, fixed-rate taxable bond market. The index includes Treasuries, government-related and corporate securities, MBS (agency fixed-rate and hybrid ARM pass-throughs), ABS and CMBS (agency and non-agency).

S&P National AMT Free Muni Index: An index composed of investment-grade U.S. municipal bonds.

US 7-10 Year Treasury Index: An index composed of U.S. Treasury bonds with remaining maturities between seven and ten years.

Bloomberg Barclays Municipal Custom High Yield Composite Index: Intended to track the overall performance of the U.S. dollar denominated high yield long-term tax-exempt bond market.

ICE BofAML US Taxable Municipal Securities Plus Index: The Index is designed to track the performance of US dollar-denominated taxable municipal debt publicly issued by US states and territories, and their political subdivisions, in the US market.

Bloomberg Barclays Global Aggregate ex-US: The Bloomberg Barclays Global Aggregate Index ex-US is a measure of global investment grade debt from 24 local currency markets excluding the US.

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