

TACTICAL MANAGED ACCOUNTS QUARTERLY

Quarterly Recap:

July 29, 2014

US and selected European stock markets reached new highs on major averages during the second quarter. Momentum in stock prices continues to be driven by short-term interest rates that remain close to zero in developed countries as central bank policies continue to be expansive, and by falling long-term government bond rates. On a comparative basis then, stocks still seem attractive. Although the US Federal Reserve will likely conclude its tapering program sometime in the third quarter, it is still expanding excess reserves and acquiring assets onto its balance sheet. Strong M&A activity and signs of a rebounding US economy also helped drive global equities higher.

US stock market valuations seem to be high relative to GDP. The only other time the valuation has been higher on this valuation metric was at the peak of the tech bubble at the turn of the millennium. Although this sole metric doesn't portend an immediate market decline, it does express that stocks are high relative to GDP, and along with additional sentiment gauges suggest that the probability of a material decline in equity prices may be rising.

The slowdown in China's economy, which in the first half had been one of the negative factors affecting the global economy and equity markets, appear to have come to an end, with Chinese manufacturers reporting improvement in business conditions in June (and July), the first improvement since last December. Demand is strengthening and destocking is accelerating. GDP growth of 7.5% for the year now looks attainable, with expectations for a slight pick-up for 2015.

Portfolio Positioning:

Activity levels picked up over the quarter as we increased our exposure to US equities, particularly US small cap names after their near 10% retracement in April-May.

We added to US technology and as a result, increased our non-AUD currency exposure. We continue to exit our US bond/credit exposures as the effects of a difficult winter soft patch fade in the rear view mirror.

Activity Details:

- Added US small cap equity exposure
- Added to short EUR/USD position
- Added small China/Japan equity positions
- Added to US Technology exposure

Market Outlook

Income Strategies: Despite the bounce in the AUD, it remains vulnerable to continued sharp declines as growth remains unbalanced in Australia. A short AUD view also helps hedge our growing China/HK allocation. While US policy maker's public comments around talking down rates continues, the aforementioned growth in the US economy should start to lift interest rates over the remainder of the year.

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This eventually should underpin USD strength. We look to increase our USD strengthening view across the Euro & Yen over the coming months. Covered call positions should perform reasonably well despite the dramatic fall in volatility levels as we expect markets to gradually move in a sideways to slightly higher direction.

Option Strategies:

Market volatility was unusually low during the quarter. Poor volatility levels and unattractive prices resulted in less put option activity over the quarter. Despite low levels of activity, the put program added roughly .75% over the quarter. We took advantage of range-bound equity markets to write some call options against some existing positions – especially in some large cap US technology names and listed gold miners on positive price momentum. The global consumer discretionary and technology sector remain the more attractive for identifying put program names. The put program capacity is currently around 30%. We have been expecting volatility to pick up, and with upcoming earnings seasons, capacity levels should increase.

Opportunistic Strategies:

We increased our non-AUD currency exposure over the quarter- more notably in the USD. We also increased our EUR/USD short position as this remains Katahdin's top currency view. We added US equity exposure over the quarter, primarily in the technology sector, and continue to increase our exposure in Asian equities – notably Japanese and Chinese equities.

Performance Overview:

Managed accounts were up roughly 4.02% over the quarter. This compares to returns of .93% for the ASX200, and 2.18% for A\$ balanced returns. YTD returns are slightly less than 9%. Returns since inception have been achieved with average 55% gross market exposure and half (5% annualized) the equity market volatility over the comparable time period and have been negatively correlated to both the ASX 200 equity index, and the A\$ balanced index.

		JAN	FEB	MAR	APR	MAY	JUN	JUL	AUG	SEP	OCT	NOV	DEC	YTD	CUM	RISK
Katahdin TMA	2012					-0.80%	0.55%	2.80%	0.50%	0.68%	-0.25%	0.86%	1.60%	6.05%		
	2013	0.52%	0.91%	0.26%	-0.74%	5.84%	-0.74%	1.76%	0.90%	0.26%	0.85%	2.47%	2.23%	15.33%		
	2014	0.98%	3.21%	0.45%	0.36%	1.17%	2.45%							8.90%	33.19%	5.06%
ASX200*	2012					-6.64%	0.66%	4.28%	2.14%	2.18%	2.98%	0.47%	3.35%	9.27%		
	2013	4.95%	5.37%	-2.21%	4.54%	-4.50%	-2.32%	5.20%	2.50%	2.19%	3.97%	-1.31%	0.79%	20.20%		
	2014	-3.03%	4.97%	0.29%	1.77%	0.68%	-1.50%							3.03%	35.32%	11.32%
A\$ Balanced^	2012					-1.71%	0.24%	2.35%	1.41%	1.59%	1.50%	0.24%	1.78%	7.57%		
	2013	2.53%	3.00%	-1.19%	3.05%	-2.29%	-1.74%	3.06%	1.07%	1.36%	1.94%	0.61%	0.66%	12.52%		
	2014	-0.92%	2.66%	0.15%	1.37%	1.12%	-0.32%							4.08%	25.98%	5.61%

*Accumulation

^50% ASX200/50%BAML BMI

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Global Relative Value

The following table highlights markets we feel offer above average compensating risks, and markets where we don't think investors are adequately being compensated for exposures.

KATAHDIN RELATIVE VALUE	EQUITY	FI & FX	COMMODITY	OPPORTUNISTIC
ATTRACTIVE Rewarding Risk	US JAPAN CHINA	USD	COTTON AG - CORN/WHEAT NATURAL GAS	US EQUITY VOL GLOBAL TECHNOLOGY
UNATTRACTIVE Non-rewarding Risk	AUSTRALIA EM ASIA	EURO AUD US BONDS		AUSTRALIAN BANKS

About Katahdin Capital:

Katahdin is an independent, non-aligned investment advisor that provides customized investment advice and implementation assistance to Wholesale Investors.

Services include serving as an Outsourced Chief Investment Officer, providing tactical investment solutions, including the Tactical Managed Account, and unbiased, objective portfolio reviews.

Katahdin Capital's competitive advantage is its ability to provide transparent, conflict-free investment advice in a flat fee, or performance aligned arrangement. Most of Katahdin's clients where we act as their Outsourced CIO, enjoy ongoing cost savings of over 60% across both their existing advice and implementation channels.

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