Private Client Program

An Intraday Approach

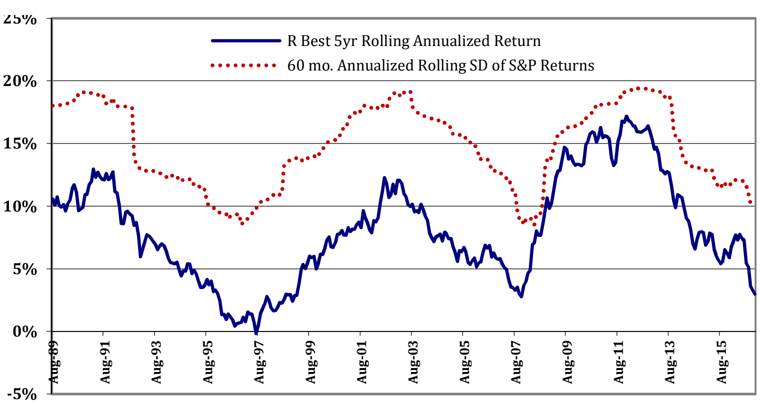
2016 Report 4Q

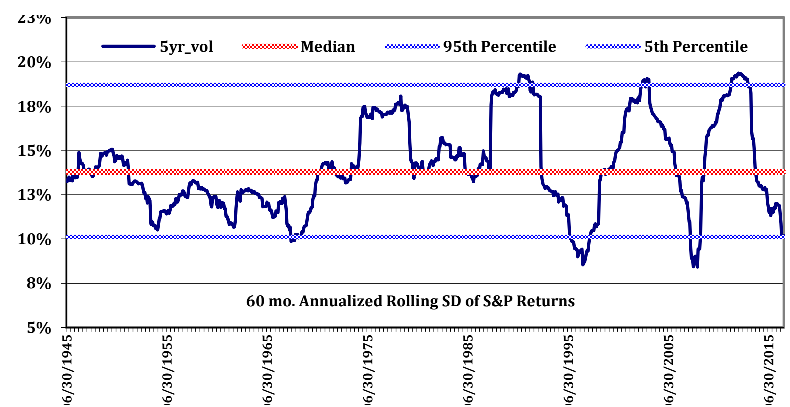
Global stocks rose in the 4th Quarter of 2016 amid signs of accelerating US economic growth and optimism over Donald Trump's US presidency. Several key indices hit record highs on expectations of market-friendly policies under the new administration. Plans to cut taxes, boost infrastructure spending, and reduce regulations were seen as positive for domestic growth, while equities looked past the possible negative implications, including the risk of a rise in protectionist trade policies. Moreover, the fiscally expansive policies of the incoming administration coupled with continued reliance on monetary stimulus, despite one more FOMC rate hike in December, acted to spur inflation expectations already buoyed by the modestly improved global growth outlook since the summer. The S&P 500 advanced 3.8% for the quarter bringing its YTD return to an impressive 11%, while 10 year treasuries finished the year down a bit after a 6% rally from Jan to July, followed by a 7% drop during the 2nd half of the year.

Concerning stock market volatility, Q4 was a continuation of the pattern that emerged more than 5 years ago of equities being mostly stable in the face of turmoil elsewhere - commodities, currencies, etc. - and despite the uncertain geopolitical landscape. Whether it's Brexit, the Italian referendum, the ongoing troubles in the Middle East, a Eurozone that appears on the verge of disintegrating, or periodic fears of a "hard landing" in the Chinese economy, US stocks have managed to continue rising. The VIX, a short term measure of implied volatility, posted a low of 10.93% in December, one of its lowest ever, while median daily range (MDR) in the S&P 500 futures, one of the measures of realized volatility that we track, stood at 0.76% - its lowest quarterly reading since Q4 of 2006 and second lowest since the E-mini contract started trading. Similarly, with an MDR of 0.39%, 10 year treasury futures have now recorded three consecutive quarters below their long run average of 0.53%, with 2016 being the 5th consecutive year of subpar activity in the treasury complex. In that environment, the only logical course of action for our strategies was inaction, and they did precisely that, generating only four (4) trades in the quarter- our lowest output since we started trading S&P futures. Despite producing a small positive return for the quarter, such periods of inactivity are never easy as they require patience and conviction in our approach, both on our part and on the part of our investors. At R Best, we have researched this issue extensively and have concluded long ago that during such periods when the market is quietly drifting (usually higher) and lacking any kind of follow through, not trading often is superior and far more rewarding than taking marginal trades that don't have potential for the kind of favorable risk/reward that we seek, but still incur commissions and other trading related costs. We have also recognized that due to the cyclical nature of markets, no investment approach is always "in style" and identifying where we are in the cycle as well as the relevant measures that drive our performance is a critical aspect of managing investments, as well as managing expectations.

As the graphs below* make clear, when sufficiently smoothed, both realized volatility in the equity market as measured by the rolling 60 month standard deviation of returns, and the simulated performance of our strategies (net of all fees and transaction costs) tend to exhibit very cyclical and mean reverting behavior. Since 1945 we observe 6 distinct low points in volatility prior to the current down cycle, with an average of 10.2% and an average duration of roughly 4 years from high to low, compared to a most recent reading of 10.17% in Dec 2016, 4.5 years removed from the high in the summer of 2012. Given that background, it's not unreasonable to conclude that unless we're on the verge of a regime shift, where stock market volatility goes lower than it has in the last 70 years and stays there, we could well be at or near a turning point. It's always dangerous to predict if and when that could happen but we do know that in markets and economies stability tends to breed instability, and that towards the end of a bull cycle complacency often leads to reckless behavior on the part of investors and corporations. At R Best our view is shaped in part by placing the present in its proper historical context by assessing the data, but also by acknowledging that the future is inherently unpredictable. In the short run the stock market may very well continue on its upward trajectory, but the medium term outlook for long-volatility strategies like ours remains very promising.

PAST PERFORMANCE IS NOT NECESSARILY INDICATIVE OF FUTURE RESULTS





*** HYPOTHETICAL PERFORMANCE RESULTS HAVE MANY INHERENT LIMITATIONS, SOME OF WHICH ARE DESCRIBED BELOW. NO REPRESENTATION IS BEING MADE THAT ANY ACCOUNT WILL OR IS LIKELY TO ACHIEVE PROFITS OR LOSSES SIMILAR TO THOSE SHOWN. IN FACT, THERE ARE FREQUENTLY SHARP DIFFERENCES BETWEEN HYPOTHETICAL PERFORMANCE RESULTS AND THE ACTUAL RESULTS SUBSEQUENTLY ACHIEVED BY ANY PARTICULAR TRADING PROGRAM. ONE OF THE LIMITATIONS OF HYPOTHETICAL PERFORMANCE RESULTS IS THAT THEY ARE GENERALLY PREPARED WITH THE BENEFIT OF HINDSIGHT. IN ADDITION, HYPOTHETICAL TRADING DOES NOT INVOLVE 15 FINANCIAL RISK, AND NO HYPOTHETICAL TRADING RECORD CAN COMPLETELY ACCOUNT FOR THE IMPACT OF FINANCIAL RISK IN ACTUAL TRADING. FOR EXAMPLE, THE ABILITY TO WITHSTAND LOSSES OR ADHERE TO A PARTICULAR TRADING PROGRAM IN SPITE OF TRADING LOSSES ARE MATERIAL POINTS WHICH CAN ALSO ADVERSELY AFFECT ACTUAL TRADING RESULTS. THERE ARE NUMEROUS OTHER FACTORS RELATED TO THE MARKETS IN GENERAL OR TO THE IMPLEMENTATION OF ANY SPECIFIC TRADING PROGRAM WHICH CANNOT BE FULLY ACCOUNTED FOR IN THE PREPARATION OF HYPOTHETICAL PERFORMANCE RESULTS AND ALL OF WHICH CAN ADVERSELY AFFECT ACTUAL TRADING RESULTS.**