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Alternative Investments Observer

Contents

MORNINGSTAR®

An August Test for Alts Funds

Did liquid alternative funds prove their mettle in the August drawdown?

by
Josh Charlson, CFA
Director of Manager Research
Alternative Strategies

When the markets swooned in late August 2015, many eyes pivoted to liquid alternatives. Having been promoted in part for their ability to provide a cushion to portfolios during times of turbulence for the markets, would alternative mutual funds fulfill their promise? A sharp six-day market correction (or even a multimonth downturn, if you count the S&P 500's decline from its high point in May 2015) is probably not sufficient to take the full measure of these funds, but it's enough of a deviation from the largely placid bull market of the past half-decade to at least offer some relevant insights. Call it a stress-test, if you will, of alternative mutual funds' resiliency.

The Wall Street Journal weighed in quickly with a fairly negative assessment: Alternative funds offer "limited protection," read the headline (I was quoted as a source in that article, in full disclosure). But the disappointment voiced in the article seems to be based on faulty, or at least overly ambitious, expectations that alternatives should provide complete protection in a downturn or at a minimum outperform intermediate-term bonds.

This somewhat misses the point and ignores the design of most alternative funds, however. Indeed, they should provide diversification from equities, which tend to be responsible for most of the risk in investor portfolios, and ideally will protect better on the downside than stocks while allowing for some upside participation. But most of the funds in Morningstar's alternative categories do have some exposure to the markets—sometimes through direct stock market investments, or at times through exposure to other global asset classes correlated to equities—so in a sell-off as widespread and steep as we saw in late August, it's unreasonable to expect complete immunity. From that perspective, using U.S. Treasuries as a benchmark seems like an unfair comparison.

Investors should expect a muted downside capture, and that's what we've seen. By my reckoning, liquid alts have performed well within expectations. Of course, within any given Morningstar Category there are a range of outcomes, and I'll explore that variability and some of the potential reasons for it further below. But here are the averages for Morningstar's alternative categories (expanded to include nontraditional bond) for the period from Aug. 17 to Aug. 24, compared with the S&P 500 and MSCI World Indexes. During the six trading days covered, the S&P 500 was down 9.43%, very close to the negative 10% threshold generally ascribed to a true market correction.

Exhibit 1 Morningstar Alternative Category Returns During August Downturn (Aug. 17–24)

Morningstar Category	Return
Bear Market	14.52
Managed Futures	0.21
Multicurrency	-0.58
Nontraditional Bond	-0.95
Market Neutral	-1.06
Multialternative	-2.59
Long-Short Equity	-4.79
S&P 500	-9.43
MSCI World Index	-8.85

Source: Morningstar

Unsurprisingly, bear-market funds, which bet against the stock market at all times, fared best. Morningstar believes that bear-market funds have a limited place in investor portfolios, given that the long-term direction of the stock market is upward. The bear-market category still has a negative 20% annualized return over the trailing five years through Sept. 30, 2015.

Of more interest is the second-best-performing category, managed futures. Managed-futures strategies tend to have very low, and even negative, correlations to the stock market, and they gained notice after 2008, when the small number of funds around at the time held up very well, as did their much larger set of hedge fund counterparts. Since then, the number of managed-futures funds has skyrocketed to more than 50. Based on the results of that week in August, those diversifying qualities are still in force, as the managed-futures category was the only one other than a bear market to post a number in the black.

Other alternatives categories were in the red, but usually only slightly so, and generally well ahead of the major stock indexes. The multi-currency, non-traditional-bond, and market-neutral categories were all down about 1% or less, while the S&P 500 and MSCI World lost about 9 times that much (losses of 9.43% and 8.85%, respectively). Currency funds generally have little correlation to the movements of stock markets (though many are short-dollar and may take a hit when investors flee to dollar safety), while market-neutral funds are expressly designed to minimize exposure to beta (though in reality, a number of them are slightly net long, as detailed in the deeper dive below).

The biggest losses came in the long-short equity and multialternative categories, but even those were well within expectations. For instance, the long-short equity group lost 4.79%, about half the S&P 500's decline. Given that the average beta for the category has hovered around 0.5 during the past three years, that degree of downside capture is right on schedule. There is, however, a wide range of betas within the category around that average, so individual fund results vary quite a bit.

Multialternatives constitute a fairly heterogeneous group, but many take an absolute return approach or strive to achieve set return and/or volatility targets. In recent years, we've expressed concerns about relatively high correlations across the group, but the results in the August downturn provided some reassurance. The 2.59% category loss was about one fourth that of the stock market, a reasonable though not stellar result, considering the category's average trailing beta of 0.28.

Beware Beta Drift

Although the average returns, and the bulk of results across the alternative categories, were in line with expectations in August, significant variance does exist; particularly at the margins, certain funds turned in results that might call into question whether given managers are implementing their strategies in the way investors would expect. It's worth taking note of this wide range, and exploring some of the reasons for it, so that investors can get a better understanding of how to approach such situations.

Below, I show scatterplot graphs for four alternative categories—long-short equity, market neutral, multialternative, and managed futures—covering the Aug. 17-Aug. 24 period. The x-axis plots each fund's return during the period, while the y-axis plots the three-month beta for each fund, using weekly returns to calculate beta. I have used three-month beta in order to reflect the funds' market exposure in the period leading up to late August, on the theory that managers' shifting market exposures could be a significant factor in returns that deviated from the norm. Funds that did not have a long enough history to calculate a three-month beta are excluded from the charts, though their returns remain part of the category averages. Where there are significant deviations from the trend line, these may be the result of negative or positive alpha.

First take note of the wide absolute range of returns in each category. The ranges for the four categories are 22.4 percentage points (managed futures), 21.7 (multialternative), 18.8 (market neutral), and 18.3 (long-short equity). By comparison, the moderate-allocation category's range of returns for period was 12.9 percentage points, and that figure is substantially skewed by a single outlier.

A key observation from the scatterplot graphs is the largely stable and monotonic relationship between returns and short-term beta. In short, the more market exposure a fund had taken on in recent months, the worse it did during the downturn. The graphs do reveal patterns of differentiation, however, related to the degree and directionality of returns dispersion. For instance, market-neutral funds are more concentrated and constrained in their range of returns and beta, whereas long-short equity funds are more dispersed, befitting the wider range of strategies and betas within the long-short equity category. (See Exhibits 2 and 3.) Managed-futures funds show the strongest tendency toward positive returns, but the wide absolute range of returns reflects significant differences in volatility targets across the category. (See Exhibit 5.) Beta is probably also least stable among managed-futures strategies, since they can quickly and dramatically move from long to short net exposures. Multialternatives display a strong upward tilt to the left (higher beta and lower returns.) Given the category's three-year average beta of 0.28, the number of higher-beta funds during the three-month period gives pause and points to a larger theme in the results. (See Exhibit 4.)

Namely, a meaningful number of alternative-fund managers take an active or tactical approach to shifting their market exposures. It is no accident that in the multialternative, long-short equity, and market-neutral categories, a majority of the top and bottom performers are macro- or tactically oriented strategies. Such fluidity makes it harder for investors to trust the level of protection those funds will offer during down markets. For example, while the 10 best-performing funds in the long-short equity category during the six-day period show an average three-month beta of essentially zero (-0.01), the worst 10 had an average beta of 0.80, at the top of the beta range that Morningstar uses to classify long-short equity funds. With long-short equity funds, beta is one of the most significant predictors of returns.

The bottom 10 market-neutral funds had an average three-month beta of 0.38, which is higher than the 0.30 maximum beta that Morningstar generally looks for in market-neutral funds (although that is assessed over a longer-term three-year lens). Meanwhile, the top 10 funds exhibited an average beta of negative 0.09. Managers who can tactically pivot to provide protection in down markets or exposure in up markets can provide a benefit to investors. But such moves are hard to get consistently right, and performance during the downturn may

Exhibit 2 Long-Short Equity Returns and Beta in August Drawdown

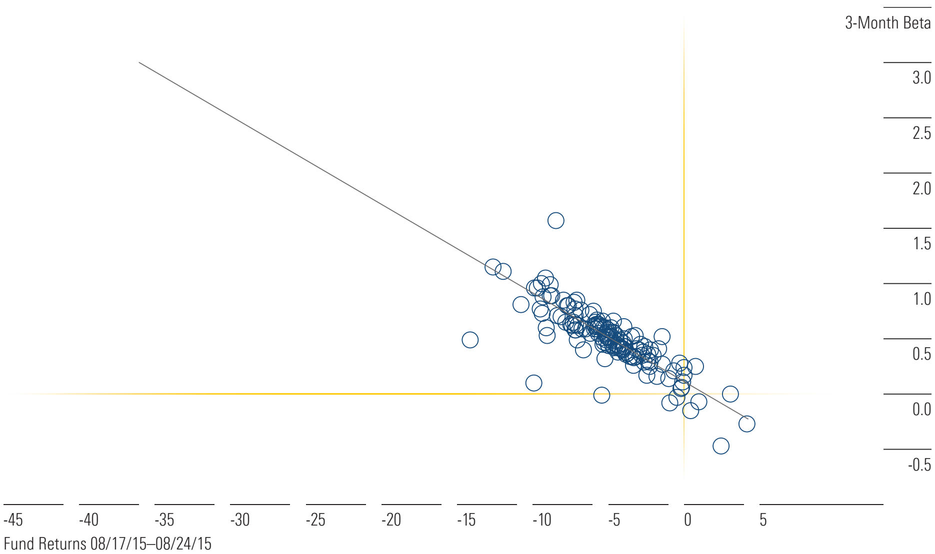
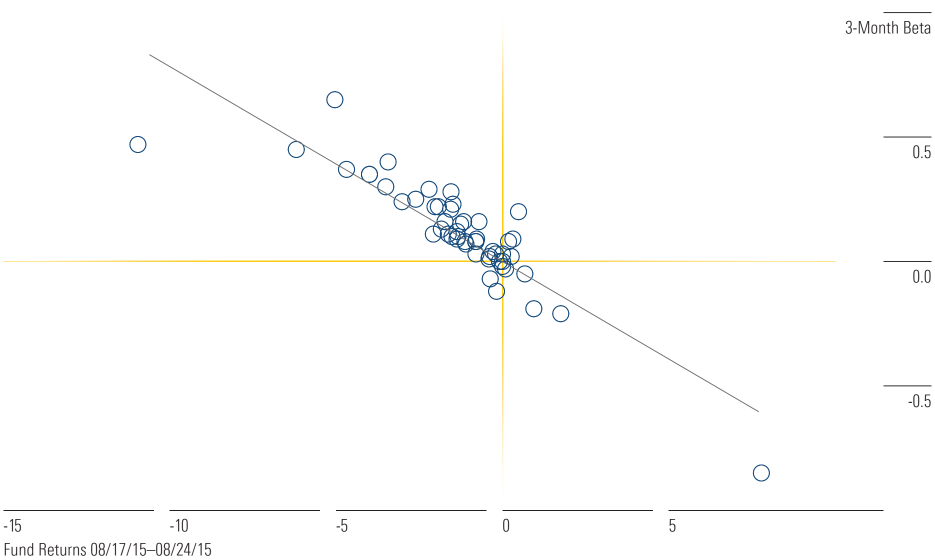


Exhibit 3 Market Neutral Returns and Beta in August Drawdown



reveal upon closer examination that some alternative fund managers just don't have that skill. In a handful of these cases, we may find that funds with more market exposure than expected simply don't belong in their assigned categories, because that market exposure is a more constant part of their approach, or they were taking other unforeseen risks.

From that perspective, the starker properties of a market correction provide a useful test case to determine whether managers are really following their strategies as claimed. Investors in liquid alternative funds should first make sure they understand whether the portfolio manager keeps market exposure static or moves it around. With those expectations set, one is in a position to assess whether a fund's behavior and performance characteristics during the correction were within expected boundaries. If not—if either beta shifted substantially beyond expectations or, conversely, a dynamic beta approach was expected but the call was wrong—then a second look at the fund is warranted.

Notable Morningstar Medalist Performances

Within the stout managed-futures category, AQR Managed Futures Strategy AQMIX was a standout. The firm's flagship fund, which has a Morningstar Analyst Rating of Silver, gained 4.90% during the Aug. 17–Aug. 24 period, while its more leveraged sibling AQR Managed Futures HV [high volatility] gained 7.22%. The fund benefited from its long-standing short on commodities and was boosted further when its models shifted into short emerging-markets equities in late August.

Among Morningstar Medalists in the long-short category, the best-performing fund in the downdraft was Bronze-rated Schooner SCNAX. The fund's managers take a fairly active approach to their option-collar strategy and had been positioning the fund for a sharp market move by increasing its put protection. On the flip side was another options-based strategy, Bronze-rated Swan Defined Risk SDRAX, which lost 7.82%. In this case, while the fund's hedges worked, its put-writing component led to losses because of the extreme spike in volatility. Management says it has seen similar patterns in the past and expects a resumption of normal volatility patterns to result in outperformance down the road. Still, both situations should serve as a reminder that options-based strategies carry a degree of nonlinearity that's often not captured in standard volatility measures.

Among more traditional long-short equity managers, Silver-rated Boston Partners Long/Short Equity lost only 0.94%; it typically takes significant short positions on individual stocks, and its top short as of its most recently disclosed portfolio, American Railcar Industries ARII (a negative 16% position), was down was much as 23%. Meanwhile, rules-based Gotham Absolute Return GARIX lost 5.5%, but the Bronze-rated fund's typical beta of 0.7 means it will incur greater losses than the norm in down periods. And although it's no longer a medalist, Neutral-rated MainStay Marketfield MFLDX remains a prominent category stalwart. It's suffered a rough period since the start of 2014, but its positive 0.98% re-

Exhibit 4 Multialternative Returns and Beta in August Drawdown

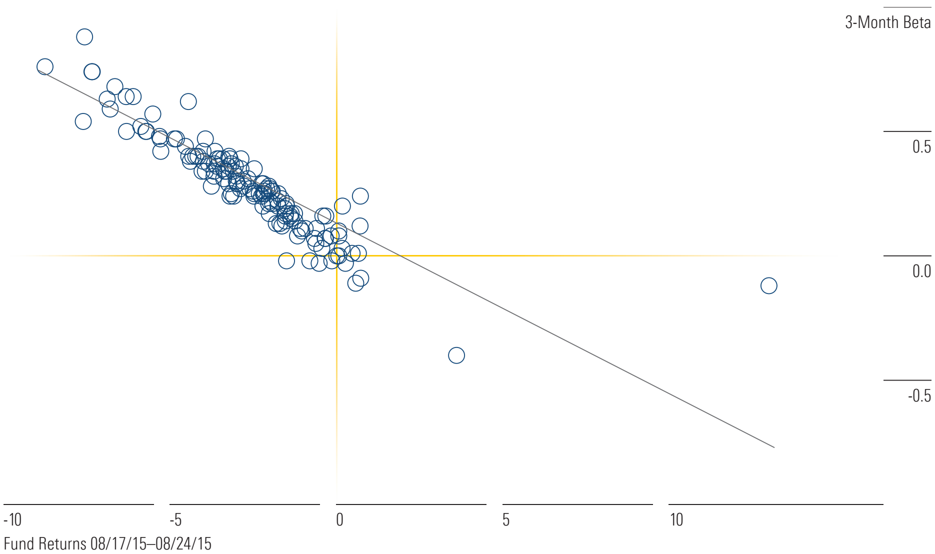
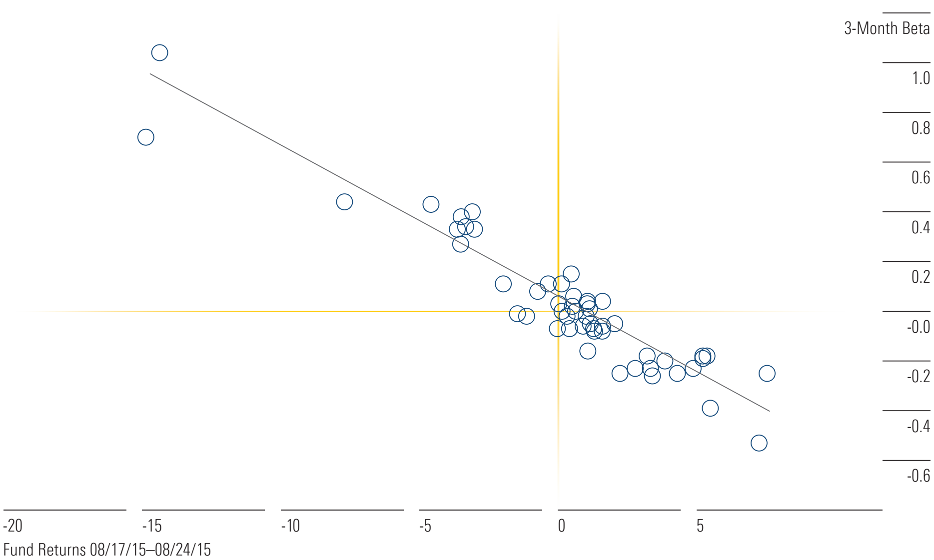


Exhibit 5 Managed Futures Returns and Beta in August Downturn



turn during the downturn should give some comfort to its investors. Marketfield's positioning has changed recently, so it's hard to make assertions about the source of this outperformance, but the managers have indicated that they had been pulling back on their China exposure, and its trailing three-month beta at the end of August was negative 0.07.

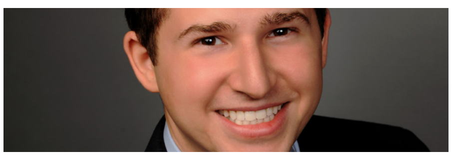
Within the multialternative category, global-macro type strategies, which typically have heavier directional components, have struggled more than many of the risk-aware multistrategy vehicles. Bronze-rated MFS Global Alternative Strategy DVRIX, for example, was down 4%, more than a percentage point beyond the category average. Another Bronze-rated fund, Litman Gregory Masters Alternative Strategies MASFX, beat the category results with a loss of 1.58%. The multistrategy vehicle aims to produce results on par with a 40/60 stock/bond portfolio, and with a relatively low correlation to equities. It's worth noting that the top-performing multialternative fund covered by Morningstar in the downdraft was Neutral-rated Absolute Strategies ASFIX, with a 3.54% return, reflecting the bearish stance taken by the manager in recent times, as the fund's beta had drifted into negative territory (its trailing one-year beta was negative 0.34).

The week provided a note of vindication, at least in the short term, for one other notable bear. Hussman Strategic Growth HSGFX, which receives a Negative rating, generated a 7.78% return, as manager John Hussman's extreme concerns about the economy and market valuations have led him to run the fund as essentially a bear-market vehicle in recent years. The fund's trailing three-month beta of negative 0.85 made it an outlier even in the very conservative market-neutral category.

The Hussman fund's performance raises one final point. Downside performance for alternatives is important, but it's not the be-all and end-all. Return-generating potential is important, too. Despite the fund's sterling downmarket results in August, its negative 1.11% return through the end of September is in the bottom half of the market-neutral category, and its three-, five-, and 10-year returns are all in the red in the category's bottom percentile. This should serve as a reminder to investors to always keep the larger performance context in mind.

Morningstar Barron's Alternative Investment Survey Results

The alternative funds cometh.



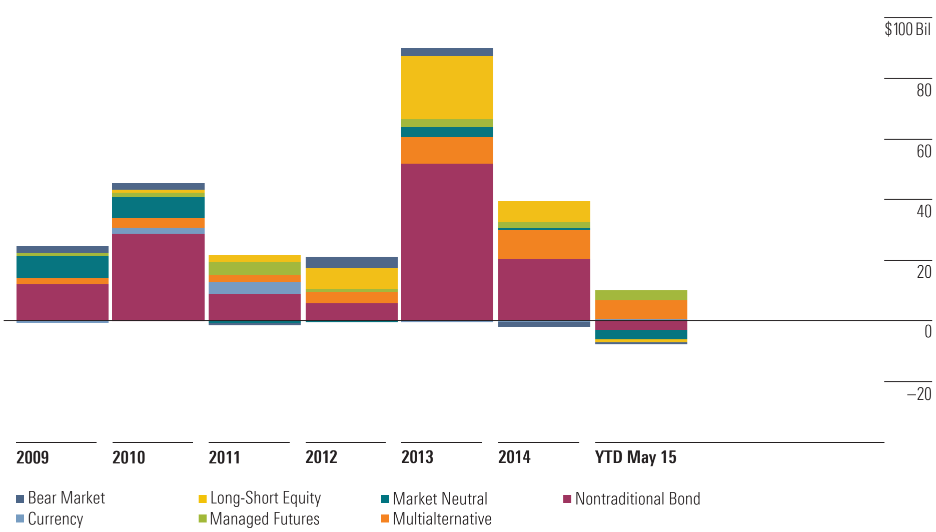
by
Josh Charney, CFA
Investment Consultant

Each year, we survey a wide sampling of advisors and institutions in order to understand investor sentiment regarding the emerging alternative investment space. Some of the results this year were surprising. For instance, there was a divide between advisors and institutions as to whether they will increase or decrease future alternative allocations, as we'll see later. But before diving in, it's important to understand the respondents' views in the context of strong market currents. For several years, alternative funds have benefited from recurrent financial market concerns.
As investors have at various times agonized over possible stock market corrections or an end to the 20-plus-year bull market in bonds, they've often reacted by piling into alternatives. More recently, though, as the bull market has continued largely unabated, investors seem to have become more sanguine about the markets, or perhaps less content with missing out on the upside. Our survey helps get at the motivations behind the flow trends and offers insight into where the opportunities and potholes may lie for the alternatives industry and those who invest in these products.

Investor Returns Leave Much to Be Desired
Unfortunately, those market currents have led investors to make poor market-timing decisions. While mutual fund investors aren't exactly known for making great market-timing decisions in the first place, the data for alternatives show several disturbing trends. Long-short equity fund assets, for instance, have grown almost fivefold since 2008 as investors were attracted to this Morningstar Category's relatively superior performance during the financial crisis—the long-short equity category dropped only 15.4% while the market had a 37.0% pullback. While the category does offer investors better downside protection than long-only vehicles, the funds, as expected, haven't kept up as well during market rallies, since the category's beta is only 0.51 relative to the S&P 500. The funds lagged the market by an astounding 11.5 percentage points per year from 2009 through June 2015, while only beating the Barclays U.S. Aggregate Bond Index by 0.2% during the same time period.

There are other examples of poor market-timing. In 2013, investors poured $55 billion into nontraditional-bond funds, in part to protect against anticipated rising interest rates—a move that hasn't proved fruitful so far. (See Exhibit 1.) Also, we've witnessed a fair amount of performance-chasing during the past few years as investors poured $13.4 billion into MainStay Marketfield after several outstanding years of performance,

Exhibit 1 Alternative Mutual Fund Flows



Source: Morningstar, Inc.

Exhibit 2A Institutions: Anticipated Allocation to Alternatives Five Years from Now

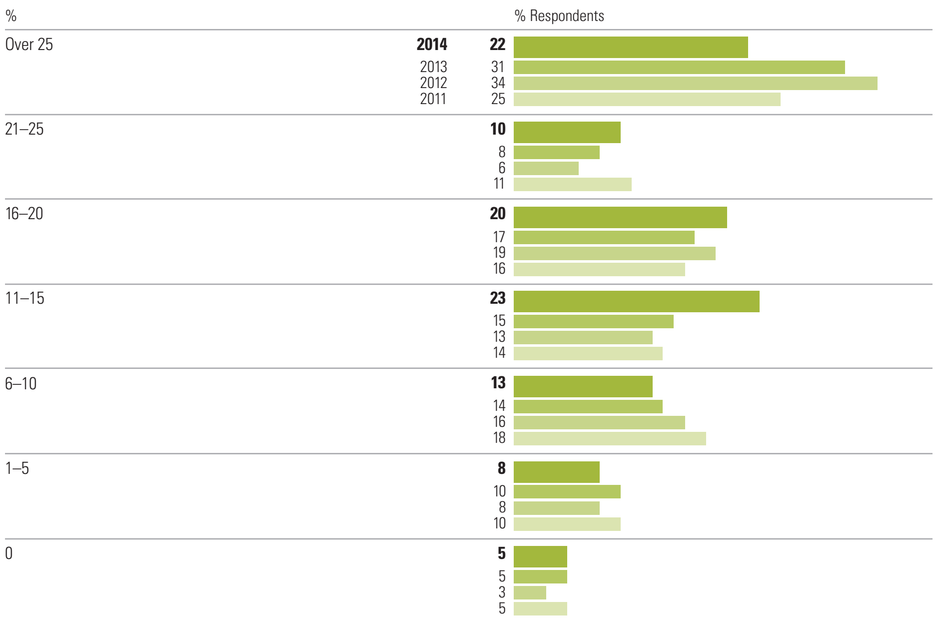
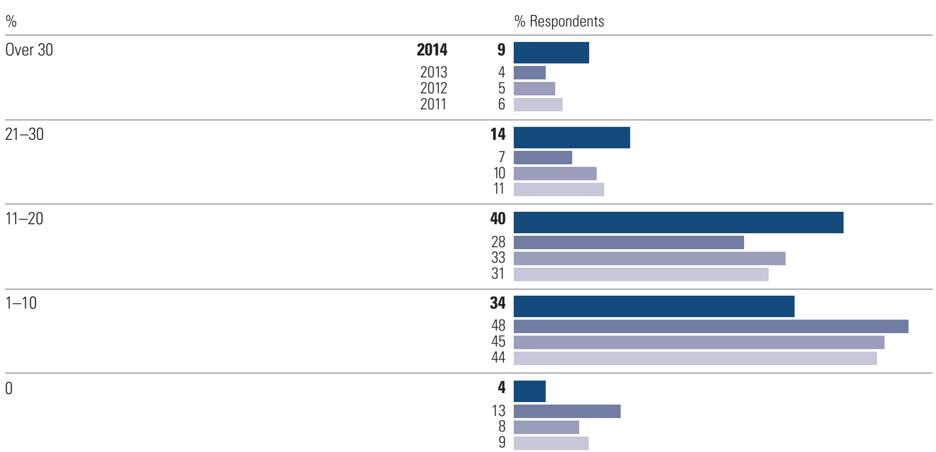


Exhibit 2B Advisors: Anticipated Allocation to Alternatives Five Years from Now



only to pull out $7.8 billion during the fund's abysmal 2014. All these market-timing missteps add up: The negative 2.2% returns gap for alternatives funds, which is calculated as the equal-weighted performance minus the asset-weighted returns, is worse than any other broad asset class' during the past three years. Clearly, investors need to focus their efforts on making long-term strategic allocations with alternatives, as opposed to short-term tactical shifts.

Advisors Still Positive, While Institutions Waffle

Given the performance challenges, we had anticipated a possible decline in interest around alternative investments. While that was the case for institutions, advisor interest actually increased, as advisors indicated that they expect their alternative allocations will continue to rise. In 2014, 63% of advisors allocated more than 11% to alternatives, compared with 39% of advisors for the previous year. (See Exhibit 3.) Most advisors (59%) allocate between 6% and 20% to alternatives.

But institutional sentiment declined slightly from previous years, especially at the extreme levels. For example, institutional respondents who said they expect to allocate more than 25% to alternatives over the next five years declined from 31% to 18%. (See Exhibits 2A and 2B.) Similarly, institutions that currently allocate more than 40% to alternatives saw a steep decline, from 18% of institutions in 2013 to 9% in 2014. Moreover, 45% of institutions stated that alternatives were "somewhat less important" or "much less important" than traditional investments, as compared with 28% in 2013.

A number of factors could be behind these shifts. First, institutions likely allocate more to hedge funds than to liquid 1940-Act mutual funds, and hedge funds have faced their own set of challenges. While alternative mutual funds are still growing at a healthy clip, assets in Morningstar's single-strategy hedge fund database (a representative sample of the hedge fund universe) actually fell slightly from 2013 to 2014. The survey found that institutions were concerned with high hedge fund fees, lack of liquidity, and poor transparency. We also found that institutions weren't affected by Calpers' decision to exit the space (or at least were not willing to admit it). But there may be other factors at play as well. Institutions have also been ahead of the curve, compared with advisors, in using alternatives, and perhaps they've reached a saturation point and are now starting to pull back.

In light of the shifting tides of sentiment, it was reassuring to see that both institutions and advisors continue to cite diversification/low correlation as their top reason for investing in alternatives, and by a wide margin. (See Exhibit 4.) This provides reassurance that the gatekeepers for these products understand their role in a portfolio.

Multistrategy Funds Get a Boost

Morningstar's multialternative category has garnered a lot of attention lately, as flows into the space have topped $9 billion per year during the past two years. These funds are meant to serve as a "core" alternative holding (a bit of an oxymoron) or as a one-stop shop for alternatives exposure. Given that investors appear to be struggling with timing certain alternative-allocation decisions, these funds seem like a potential remedy. Institutions cited multi-

Exhibit 3 Institutions and Advisors: Allocation to Alternative Investments in 2014

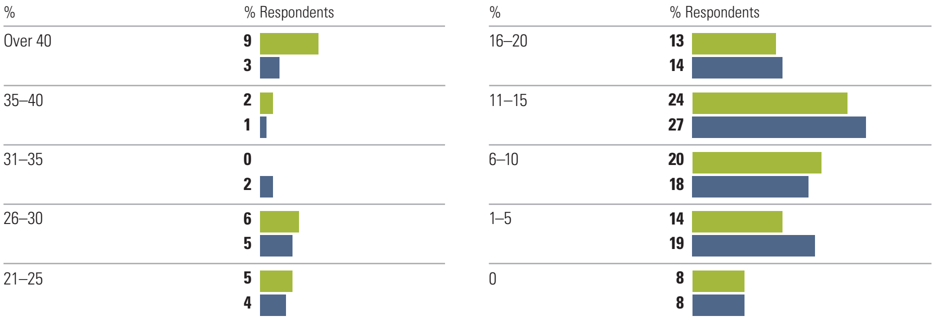
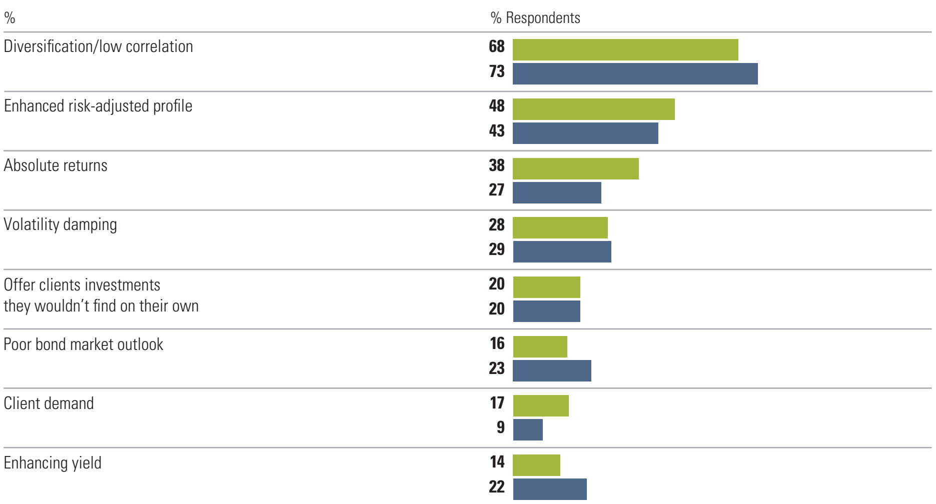


Exhibit 4 Institutions and Advisors: Top Drivers of Investments in Alternatives (Up to Three Responses Selected)



strategy funds as the fastest-growing part of their alternative allocations during the past five years, as well as the top strategy for increased allocation. (See Exhibit 5.) On a similar note, advisors rated multistrategy/fund of funds as the third-fastest grower, behind master limited partnerships and other alternative strategies.

That institutions may be more interested in multialternative funds than advisors is somewhat surprising, given that many of these products are tailor-made for advisors. Generally, institutions have more investment personnel and have the resources to build out a dedicated alternative fund selection team. So, one might expect institutions to build their own array of custom alternative portfolios and advisors to clamor for multialternative funds.

Perhaps the survey demographic data can shed some light on this quandary. The data show that 58% of institutions that participated in the survey have less than $11 billion in assets under management, while 38% have less than $1 billion. So, it might be reasonable to conclude that many of our respondents have fewer resources than the very largest institutions but have the desire to include alternative allocations. Multistrategy funds would thus be an ideal choice if an institution doesn’t have a dedicated alternative fund selection team but does have the drive to invest in them. Meanwhile, it seems that advisors are somewhat behind the alternative-allocation curve and are catching up to institutions by allocating more to alternatives.

Picturing the Ideal Client for Alts

As part of our annual set of new “hot topic” questions, we asked both advisors and institutions to picture the ideal client for alternative investments, on five different dimensions (client sophistication, distance from retirement, level of assets, level of required return, and level of risk tolerance). The results gave us a window into the necessary criteria that financial professionals look for in order to decide if alternatives are suitable for a particular client. (See Exhibit 6.) Both groups agreed that, for clients to be considered optimal for an alternative allocation, a higher level of sophistication and a higher asset threshold were required. But interestingly, the group also agreed that clients should be midway through their careers and not too close to retirement. While these results aren’t shocking, it does show that alternatives still carry a stigma of riskiness, in that respondents believe they aren’t appropriate for a client near retirement. Given that alternatives actually tend to be somewhat less risky than stocks and that there are also decent fixed-income alternatives worth considering, this stereotype might be worth trying to break.

In terms of required return and risk tolerance, for instance, both advisors and institutions agreed that about average required levels of return and average levels of risk tolerance were ideal for considering adding alternatives to a client’s portfolio. The responses show that alternatives probably aren’t suitable for very conservative clients, nor are they acceptable for clients seeking high-octane returns.

A Slowdown Ahead?

The survey highlights some astonishing trends at a time when alternative flows are starting to moderate. While organic growth rates for liquid alternative mutual funds during 2014 were still larger than any other broad Morningstar Category, they were the slowest on record since 2008, at 12%. But the survey shows that advisors aren’t all doom and gloom and may be looking to allocate more into alternatives during the next couple of years. But the pace at which institutions appear to be withdrawing from alternatives does raise an eyebrow. It’s possible that many of them are abandoning certain less-liquid strategies, and therefore their allocations into liquid alternative mutual funds might actually stand to increase. We have heard anecdotally that, although just a trickle so far, more institutions are taking advantage of liquid alternative strategies when offered as

Exhibit 5 Institutions: Top Alternative Strategies for Increased Allocation

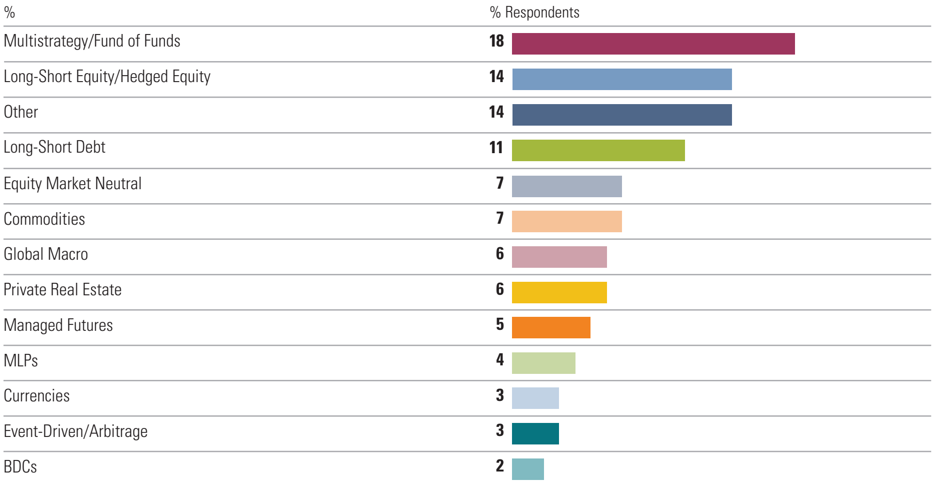
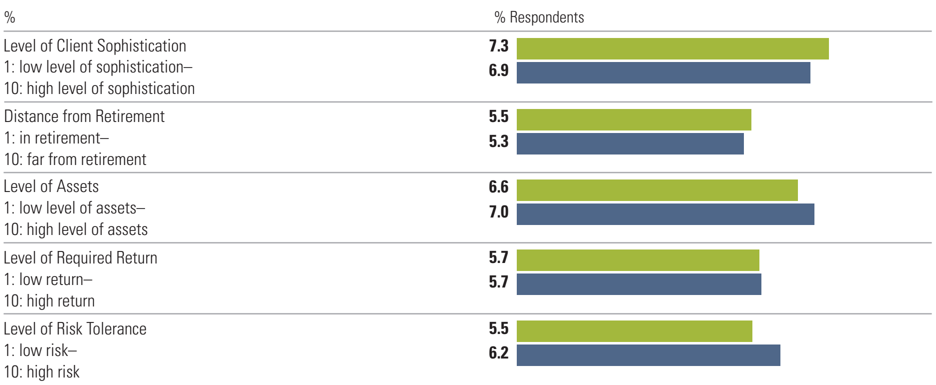


Exhibit 6 Hot Topics: Client Characteristics Most Suitable for Alternatives



reasonable version of an existing investment. Regardless of how this plays out, it's worth paying attention. Are liquid alternatives now a more mature asset class (and therefore will exhibit slower growth), or will flows pick back up again if market volatility increases? (The jury is still out on the effect of the August 2015 correction.) While the tea leaves are a bit murky, the magnitude of new fund launches by fund companies indicates that the smart money is on these products continuing to take in sizable flows.

Alternative Investments in Target-Date Funds

Alternatives are making incremental advances.

by
Janet Yang, CFA
Director, Multi-Asset Strategies,
Manager Research

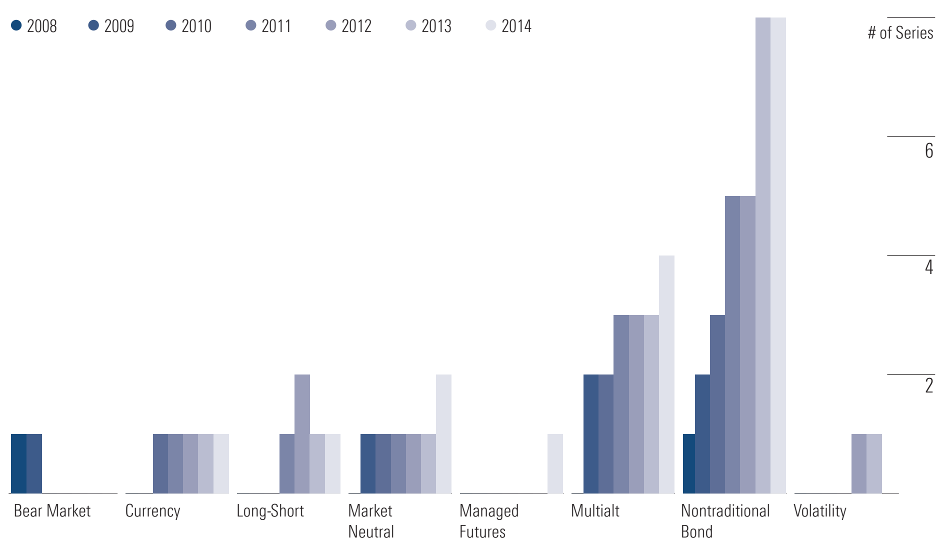
In Morningstar's 2011 Target Date Industry Survey, we took an initial look at the use of alternatives in the portfolios of target-date series. In the time since, the liquid alternatives boom has only accelerated, making a greater number of alternative strategies available to managers in mutual fund form. From a diversification standpoint, alternatives make a great deal of sense in the multiasset and long-term framework of target-date funds. From a practical perspective, though, many managers have balked at the high fees and unproven track records of many of these strategies. Since we last looked at the question, have matters on the ground changed in the target-date universe?

Exhibit 1 shows the number of target-date series that over the years have invested in some of the main Morningstar Categories housed under the alternative investments group. These strategies have become increasingly accessible to target-date funds via the alternatives managers who continue to take their strategies from the exclusive world of hedge funds to the more democratic mutual fund vehicle; investors have deluged the funds with new assets, and many target-date managers have joined the stream.

Target-date funds' use of alternative investments notably increased after 2008's financial crisis, at least in a partial attempt to prevent the funds from suffering as badly in future market corrections as many did during 2008's rocky period. The multialternative category, which serves as a catchall for funds simultaneously pursuing a variety of alternative investment strategies (such as long-short equity and merger arbitrage), has become more popular of late.

The category's heterogeneous mix of funds makes comparisons among them challenging, though investors tend to favor them for their ability to provide a diversified mix of alternative strategies in a single package. In 2009, the MFS Lifetime and Putnam RetirementReady series were among the first to use funds in that category, via MFS Diversified Target Return and Putnam's various Absolute Return funds, respectively. In 2011, the John Hancock Retirement Living Through series began using its firm's Global Absolute Return Strategies (subadvised by Scotland-based Standard Life) to become one of the first target-date series to use a true global macro strategy. The firm

Exhibit 1 Number of Series Using Alternative Investments Mutual Funds, 2008–14

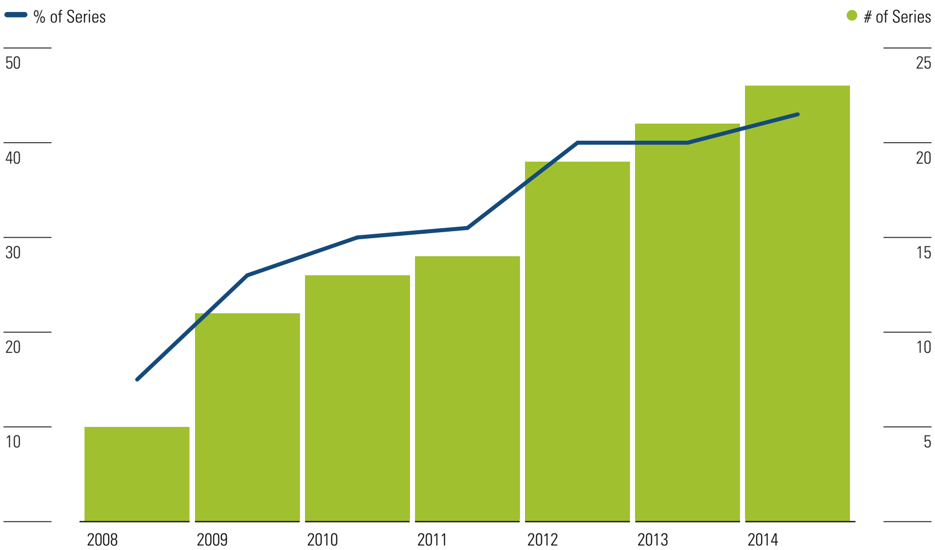


Source: Morningstar, Inc. Data as of 12-31-2014.

has also incorporated single-strategy alternatives funds, including a long-short currency fund and a buy-writing options-based strategy, within the target-date portfolios.

Target-date managers have also been adding stakes in non-traditional-bond funds—those that often run unconstrained sector or duration strategies. These funds can also pursue an absolute return mandate, where the goal is to generate positive returns regardless of market movements. Such strategies should help compensate for low yields and guard against future rising interest rates. For these funds, Putnam was also on the industry's leading edge. Morningstar first launched the non-traditional-bond fund category in 2011, and the Putnam RetirementReady series has used Putnam Diversified Income, now part of the non-traditional-bond fund group, since 2007. Target-date series registered their first use of managed-futures strategies in 2014. The PIMCO RealPath series added PIMCO Trends Managed Futures Strategy earlier in the year. Manning & Napier also carved out an allocation to managed futures from its bond portfolio, citing concerns about higher-quality bonds' anemic yields. (The strategy doesn't register on Exhibit 1, though, because it's implemented within the target-date series' underlying Pro-Blend funds rather than as a stand-alone fund.) Managed-futures strategies may have particular appeal to target-date allocators because of the extremely low correlations to standard equity and fixed-income benchmarks that they have historically exhibited.

Exhibit 2 Number of Series Using Commodities Mutual Funds, 2008–14



Source: Morningstar, Inc. Data as of 12-31-2014.

Exhibit 3 Target-Date Assets in Commodities Mutual Funds and Index Returns, 2008–14

Source: Morningstar, Inc. Data as of 12-31-2014.

Commodities: Old News?

Exhibit 2 looks at the prevalence of commodities in target-date funds. In some respects, the increasingly common use of commodities has put them into the mainstream, and Morningstar does not explicitly include commodity-related categories within its alternatives umbrella. Still, it wasn't too long ago that they were considered a more fringe offering, with only five series using a commodities-focused strategy in 2008. While commodities maintain characteristics that investors often look for in alternative investments—such as lower correlation to stocks and bonds—they're typically used as an inflation hedge by many target-date managers. Morningstar first registered a series' use of a broad-basket commodities fund in the Deutsche LifeCompass series in 2005 via Scudder Commodity Securities. The numbers have steadily risen since then, with almost half of target-date mutual fund series now investing in a commodities category fund.

Gaining exposure in the space can take various forms, including investing in the physical products (most commonly via metals investments), using commodities derivatives, and buying equities of companies that produce or depend on commodities. The last type serves as a reminder that likely all series have exposure to commodities, whether or not it's via a dedicated allocation or fund. Exhibit 2's numbers don't tell the whole story of commodity funds' history in target-date series, though. For while the chart shows a steady upward trend, assets devoted to those investments have been coming down over time, as shown in Exhibit 3. (That pattern is all the more striking considering how much overall target-date assets have been rising.) Target-date managers' pulling of assets from their commodities investments coincides with a multiyear period of the asset class delivering negative returns, as depicted by the Bloomberg Commodity Index's annual results.

The decrease in target-date funds' commodities assets has come from the category's negative returns as well as managers pulling money from those strategies. With its large market share and as one of the category's more ardent believers, Fidelity has accounted for much of the latter. The firm initially showed its enthusiasm for the asset class in 2010. That year, for instance, Fidelity Freedom 2050's stake in Fidelity Series Commodity Strategy grew from 1.8% to 8.9% by the end of the year. While that allocation stayed relatively constant for a few years, by the end of 2013, it dropped to 2.4%, and it stood at 0.8% of the portfolio at the end of 2014. The team cites changing capital market assumptions—in particular, waning demand from emerging markets—as a main cause for the retraction. That line of reasoning hasn't been uncommon among investors, yet it also suggests that target-date funds aren't immune to the performance-chasing patterns that they're theoretically set up to avoid.

Looking Ahead

Ideally, target-date managers should view investments in alternatives as long-term strategic allocations and resist the mercurial forces of short-term performance. It does appear that target-date funds are continuing to come around to the benefits of alternatives, but the pace of adoption remains incremental. Perhaps managers have been leery of adding hedged strategies in the midst of an equity bull market; no doubt, many firms are reluctant to take steps that would raise the fees of their funds, given the intensively cost-sensitive nature of the 401(k) market. Still, there is a strong streak of "me-too-ism" in target-date product creation, so if some of the early adopters show a strong benefit from their alternatives allocations, it would not be a surprise to see an avalanche of competitors follow suit.

Fund Reports

AQR Long-Short Equity

by **Jason Kephart**

Advisor
AQR Capital Management LLC

Advisor Location
Greenwich, Connecticut

Assets Under Management
$402.6 million

Inception Date
July 16, 2013

Investment Type
Mutual fund

Morningstar Category
Long-Short Equity

People
AQR principals Jacques Friedman, Andrea Frazzini, and Lars Nielsen have been the named managers on this fund since its inception. They are also the named managers on AQR Equity Market Neutral QMNNX, which serves as the core of this strategy. The team has been running the market-neutral version in a hedge fund since 2000. They are supported by AQR's deep research, risk management, and trading teams. Friedman heads up the global-stock-selection team and plays a key role in the firm's equity market-related research efforts and portfolio management. Frazzini is also a member of the global-stock-selection team and focuses on equity factor research. Nielsen oversees research for the group.

Friedman and Nielsen have between $100,001 and $500,000 invested alongside shareholders in the fund. Frazzini has between $10,001 and $50,000 invested.

Purpose

This long-short equity fund is designed to offer investors a lower-volatility way to access global equity markets than a long-only fund. It has potential as a tool to diversify a traditional portfolio of global equities.

Process

This global long-short equity fund is built around AQR's equity market-neutral strategy. The fund adds global equity market beta exposure to the equity market strategy via futures contracts to increase the fund's beta to 0.5 (the market-neutral strategy has a target beta of zero to the MSCI World Index). The fund uses individual country futures contracts, based on each country's weighting in the MSCI World Index, to layer on the beta. The individual country contracts are cheaper and more liquid than futures contracts on the MSCI World Index, according to management. The team can tactically adjust the overall beta up to 0.7 or down to 0.3 based on a combination of overall equity market valuations, directional stock price momentum, and fundamental momentum (that is, momentum in fundamentals like revenue or earnings growth in the overall global stock market). Over a full market cycle, management expects the beta timing to add 50 to 100 basis points of performance a year.
The equity market-neutral strategy ranks the 1,500 largest global stocks by a composite score based primarily on industry-relative valuation and momentum metrics. The managers target volatility for the portfolio of 6%, which has typically translated into gross exposure of 200% long and 200% short. There is no target volatility for the overall fund's volatility as the added beta will be tied to the volatility of global equity markets.

Portfolio

Valuation and momentum make up about 60% of the composite score used to rank stocks, split evenly between the two factors. The remainder is divided between earnings quality, which looks at balance sheet ratios like debt coverage; investor sentiment (the strategy won't bet on stocks with high short interest); and stability, which identifies characteristics such as volatility in earnings. Valuation and momentum are the two largest components because of the strength of the academic research behind those factors and their historically uncorrelated relationship. Management will consider increasing the weighting of the other factors as more research is done to validate them. Industry-relative metrics, which measure stocks versus industry peers, make up 85% of the composite. The other 15% is based on the relative attractiveness of industries versus other industries and countries versus other countries. The fund is rebalanced once every two to three weeks to keep the market-neutral portfolio at an expected beta of zero and to keep the overall fund's beta consistent.

Price

This fund is offered in two share classes, both of which have high minimum investment requirements. The N shares have a minimum investment of $1 million and an expense ratio of 1.55%, which earns a Morningstar Fee Level of Average. The I shares have a $5 million minimum investment and an expense ratio of 1.30%, which is Below Average compared with similarly distributed peers.
It's also the same expense ratio as AQR Equity Market Neutral, which means AQR isn't charging investors extra for equity market beta, which is fairly cheap to obtain. M

AQR Long-Short Equity N QLENX

Standard Index	Category Index	Morningstar Cat
S&P 500 TR USD	S&P 500 TR USD	US OE Long/Short Equity

Performance 09-30-2015

Quarterly Returns	1st Qtr	2nd Qtr	3rd Qtr	4th Qtr	Total %
2013	—	—	—	8.76	—
2014	1.96	2.59	3.28	6.03	14.55
2015	3.69	0.62	5.75	—	10.33

Trailing Returns	1 Yr	3 Yr	5 Yr	10 Yr	Incept
Load-adj Mthly	16.98	—	—	—	16.60
Std 09-30-2015	16.98	—	—	—	16.60
Total Return	16.98	—	—	—	16.60
+/- Std Index	17.60	—	—	—	—
+/- Cat Index	17.60	—	—	—	—
% Rank Cat	2	—	—	—	
No. in Cat	411	—	—	—	

	Subsidized	Unsubsidized
7-day Yield	—	—
30-day SEC Yield	—	—

Performance Disclosure

The Overall Morningstar Rating is based on risk-adjusted returns, derived from a weighted average of the three-, five-, and 10-year (if applicable) Morningstar metrics.

The performance data quoted represents past performance and does not guarantee future results. The investment return and principal value of an investment will fluctuate; thus an investor's shares, when sold or redeemed, may be worth more or less than their original cost.

Current performance may be lower or higher than return data quoted herein. For performance data current to the most recent month-end, please call 866-290-2688 or visit www.aqrfunds.com.

Fees and Expenses

Sales Charges

Front-End Load %	**NA**
Deferred Load %	**NA**

Fund Expenses

Management Fees %	1.10
12b1 Expense %	0.25
Net Expense Ratio %	**1.61**
Gross Expense Ratio %	**2.52**

Risk and Return Profile

	3 Yr 180 funds	5 Yr 91 funds	10 Yr 32 funds
Morningstar Rating™	—	—	—
Morningstar Risk	—	—	—
Morningstar Return	—	—	—

	3 Yr	5 Yr	10 Yr
Standard Deviation	—	—	—
Mean	—	—	—
Sharpe Ratio	—	—	—

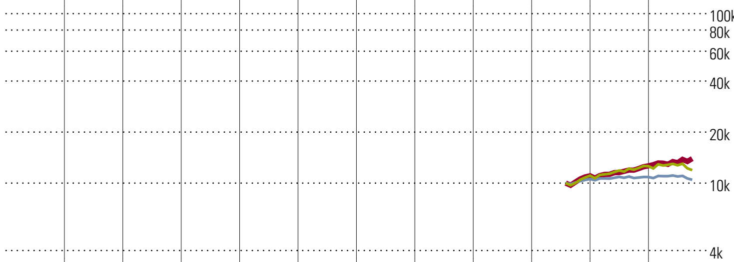
MPT Statistics	Standard Index	Best Fit Index
Alpha	—	—
Beta	—	—
R-Squared	—	—

12-Month Yield	—
Potential Cap Gains Exp	7.87%

Investment Style
Fixed-Income
Bond %

2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	09-15
—	—	—	—	—	—	—	—	—	0	0	0

Growth of $10,000



AQR Long-Short Equity N 13,950
Category Average 10,457
Standard Index 11,918

Performance Quartile (within category)

2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	09-15	History
—	—	—	—	—	—	—	—	—	10.21	10.84	11.96	NAV/Price
—	—	—	—	—	—	—	—	—	—	14.55	10.33	Total Return %
—	—	—	—	—	—	—	—	—	—	0.86	15.62	+/- Standard Index
—	—	—	—	—	—	—	—	—	—	0.86	15.62	+/- Category Index
—	—	—	—	—	—	—	—	—	—	3	—	% Rank Cat
—	—	—	—	—	—	—	—	—	—	326	453	No. of Funds in Cat

Portfolio Analysis 08-31-2015

Asset Allocation %	Net %	Long %	Short %
Cash	55.67	74.27	18.61
US Stocks	-2.99	4.76	7.76
Non-US Stocks	45.37	137.34	91.97
Bonds	0.00	0.00	0.00
Other/Not Clsfd	1.95	9.35	7.40
Total	100.00	225.72	125.72

Equity Style (Value, Blend, Growth / Large, Mid, Small)

Portfolio Statistics	Port Avg	Rel Index	Rel Cat
P/E Ratio TTM	—	—	—
P/C Ratio TTM	—	—	—
P/B Ratio TTM	—	—	—
Geo Avg Mkt Cap $mil	—	—	—

Fixed-Income Style (Ltd, Mod, Ext / High, Med, Low)

Avg Eff Maturity	—
Avg Eff Duration	—
Avg Wtd Coupon	—
Avg Wtd Price	—

Credit Quality Breakdown —	Bond %
AAA	—
AA	—
A	—
BBB	—
BB	—
B	—
Below B	—
NR	—

Regional Exposure	Stock %	Rel Std Index
Americas	—	—
Greater Europe	—	—
Greater Asia	—	—

Share Chg since 06-2015	Share Amount	Holdings: 1,339 Total Stocks , 48 Total Fixed-Income, 0% Turnover Ratio	% Net Assets
☼	787	E-mini S&P 500	20.14
⊕	91	Topix Idx Fut Sep15	2.99
⊕	103	Ftse 100 Idx Fut Sep15	2.55
☼	103	CAC 40 Index Future Sept15	1.40
⊕	54	Swiss Market Index Future Sept15	1.27
⊕	17	DAX Index Future Sept15	1.27
⊕	513,357	Seek Limited Npv	-1.17
⊖	35	S&P Canada 60 Index Future Sept15	1.13
⊕	39,866	Pepsico Inc Usd0.	0.96
⊕	14,008	Tesla Motors Inc Usd0	-0.91
⊕	67,971	Sensata Technolog	-0.84
⊕	35	SFE SPI 200 Index Future Sept15	0.84
⊕	319,500	Ricoh Co Npv	-0.81
⊕	27,011	Aetna Inc New Com	0.80
⊕	101,468	Schwab(Charles)co	-0.80

Sector Weightings	Stocks %	Rel Std Index
Cyclical	—	—
Basic Materials	—	—
Consumer Cyclical	—	—
Financial Services	—	—
Real Estate	—	—
Sensitive	—	—
Communication Services	—	—
Energy	—	—
Industrials	—	—
Technology	—	—
Defensive	—	—
Consumer Defensive	—	—
Healthcare	—	—
Utilities	—	—

Operations

Family:	AQR Funds	Base Currency:	USD	Incept:	07-16-2013
Manager:	Multiple	Ticker:	QLENX	Type:	MF
Tenure:	2.3 Years	Minimum Initial Purchase:	$1 mil	Total Assets:	$328.18 mil
Objective:	Growth	Purchase Constraints:	A		

Fund Reports

Invesco Global Targeted Returns

by **Josh Charlson, CFA**

Advisor
Invesco Advisers

Advisor Location
Houston, Texas

Assets Under Management
$147.2 mil

Inception Date
Dec. 19, 2013

Investment Type
Mutual fund

Morningstar Category
Multialternative

People
The fund is run by the multiasset group at Invesco Perpetual, the British division of Invesco Asset Management. The key members of the team were hired from Standard Life, where they helped run the hugely successful Global Absolute Return Strategies franchise, after which this fund is modeled. Lead manager and head of multiasset David Millar joined Invesco Perpetual in 2013 from Standard Life and previously managed fixed income at Scottish Widows. Comanagers Richard Batty and Dave Jubb also joined the firm from Standard Life in 2013. Batty was the global investment strategist at Standard Life, while Jubb had been with Standard Life since 1982. They are supported by three analysts, a risk manager, and a trader.

Purpose
This fund pursues a global macro strategy with an absolute return objective. It aims to produce returns of cash plus 5% over rolling three-year periods (gross of fees) and volatility of less than half of the global equity markets (as reflected in the MSCI World Index) over rolling three-year periods. The fund could fit well within a goals-based portfolio, or for investors seeking a diversified stream of multiasset-class returns.

Process
This fund's philosophy and approach are significantly modeled after the design of Standard Life Global Absolute Return Strategies, where this fund's lead managers previously worked. That process centers around an absolute return, unconstrained, and global multiasset investment philosophy. The process is also heavily team-oriented, and the multiasset team's eight investment professionals begin by developing a central economic thesis and generating global themes that fit the thesis. Analysts present specific trade ideas to an investment committee, and each trade must come with projected return targets under different economic scenarios. The portfolio generally consists of 20–30 total trade ideas, which may take long or short positions and often incorporate a hedge. The fund is evaluated at the portfolio level to ensure overall risk targets are being met and that there is sufficient diversification between individual trades. Methods used include scenario stress-testing, value at risk, and the risk contribution of individual positions. Risk oversight includes a dedicated risk manager on the multiasset team as well as an independent risk function that also monitors the strategy. The managers also rely on research and investment ideas from the entire asset management arms of Invesco and Invesco U.S.

Portfolio
Management has been operating under a thesis of low but positive global economic growth with low inflation, accompanied by spurts of volatility and market shocks driven by central-bank actions, political events, and other factors. As of June 30, 2015, the portfolio included 22 trade ideas, across credit (two), currency (five), equities (nine), interest rates (three), and volatility (three). Trades added in 2015 include emerging-markets equities versus the U.S., on the theory that emerging markets are relatively cheap and could benefit from monetary stimulus; U.S. consumer staples over discretionary stocks, based the belief that earnings projections for discretionary stocks are overly optimistic; and a rates play on Australia versus Europe, on the view that Australian interest rates do not fully reflect the country's economic slowdown and a looser monetary policy. The fund's gross exposures were 259% long and 192% short; most trades are designed as pair trades.

Price
The fund earns Morningstar Fee Level Rankings of Low for all of its share classes. The two largest share classes have net prospectus expense ratios of 1.80% (A shares) and 1.55% (Y shares), respectively. However, all share classes are currently operating under a fee waiver set to expire in 2016, subject to renewal by the mutual fund board.

Invesco Global Targeted Returns A GLTAX

Standard Index	Category Index	Morningstar Cat
Morningstar Mod Tgt Risk TR USD	Morningstar Mod Tgt Risk TR USD	US OE Multialternative

Performance 09-30-2015

Quarterly Returns	1st Qtr	2nd Qtr	3rd Qtr	4th Qtr	Total %
2013	—	—	—	—	—
2014	2.40	1.27	0.00	2.64	6.44
2015	0.38	-2.00	0.49	—	-1.15

Trailing Returns	1 Yr	3 Yr	5 Yr	10 Yr	Incept
Load-adj Mthly	-4.12	—	—	—	-0.37
Std 09-30-2015	-4.12	—	—	—	-0.37
Total Return	1.46	—	—	—	2.84
+/- Std Index	4.38	—	—	—	—
+/- Cat Index	4.38	—	—	—	—
% Rank Cat	20	—	—	—	
No. in Cat	409	—	—	—	

	Subsidized	Unsubsidized
7-day Yield	—	—
30-day SEC Yield	—	—

Performance Disclosure

The Overall Morningstar Rating is based on risk-adjusted returns, derived from a weighted average of the three-, five-, and 10-year (if applicable) Morningstar metrics.

The performance data quoted represents past performance and does not guarantee future results. The investment return and principal value of an investment will fluctuate; thus an investor's shares, when sold or redeemed, may be worth more or less than their original cost.

Current performance may be lower or higher than return data quoted herein. For performance data current to the most recent month-end, please call 800-959-4246 or visit www.invesco.com.

Fees and Expenses

Sales Charges

Front-End Load %	**5.50**
Deferred Load %	**NA**

Fund Expenses

Management Fees %	1.50
12b1 Expense %	0.25
Net Expense Ratio %	**1.80**
Gross Expense Ratio %	**3.66**

Risk and Return Profile

	3 Yr 227 funds	5 Yr 140 funds	10 Yr 28 funds
Morningstar Rating™	—	—	—
Morningstar Risk	—	—	—
Morningstar Return	—	—	—

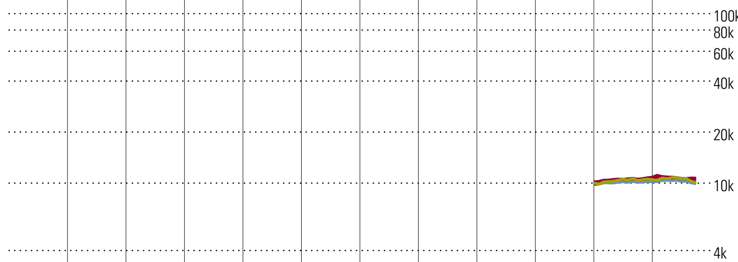
	3 Yr	5 Yr	10 Yr
Standard Deviation	—	—	—
Mean	—	—	—
Sharpe Ratio	—	—	—

MPT Statistics	Standard Index	Best Fit Index
Alpha	—	—
Beta	—	—
R-Squared	—	—

12-Month Yield	—
Potential Cap Gains Exp	1.35%

Investment Style
Equity
Stock %

—	—	—	—	—	—	—	—	—	—	50	37



Growth of $10,000
Invesco Global Targeted Returns A 10,522
Category Average 9,897
Standard Index 10,066

Performance Quartile (within category)

2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	09-15	History
—	—	—	—	—	—	—	—	—	*9.99*	10.47	10.35	NAV/Price
—	—	—	—	—	—	—	—	—	—	6.44	-1.15	Total Return %
—	—	—	—	—	—	—	—	—	—	1.55	2.89	+/- Standard Index
—	—	—	—	—	—	—	—	—	—	1.55	2.89	+/- Category Index
—	—	—	—	—	—	—	—	—	—	5	—	% Rank Cat
—	—	—	—	—	—	—	—	—	—	373	470	No. of Funds in Cat

Portfolio Analysis 06-30-2015

Asset Allocation %	Net %	Long %	Short %
Cash	55.23	62.78	7.55
US Stocks	5.41	5.41	0.00
Non-US Stocks	15.75	47.91	32.16
Bonds	17.90	20.67	2.77
Other/Not Clsfd	5.71	8.92	3.21
Total	100.00	145.68	45.68

Equity Style
Value Blend Growth
Large Mid Small

Portfolio Statistics	Port Avg	Rel Index	Rel Cat
P/E Ratio TTM	15.5	0.94	0.87
P/C Ratio TTM	10.6	1.18	1.10
P/B Ratio TTM	2.1	1.11	1.15
Geo Avg Mkt Cap $mil	19185	0.88	1.07

Fixed-Income Style
Ltd Mod Ext
High Med Low

Avg Eff Maturity	5.40
Avg Eff Duration	4.35
Avg Wtd Coupon	—
Avg Wtd Price	76.05

Credit Quality Breakdown 06-30-2015	Bond %
AAA	-0.35
AA	0.00
A	0.00
BBB	2.12
BB	42.50
B	44.00
Below B	9.95
NR	1.78

Regional Exposure	Stock %	Rel Std Index
Americas	19.7	0.27
Greater Europe	46.4	3.10
Greater Asia	33.9	2.64

Share Chg since 03-2015	Share Amount	Holdings: 227 Total Stocks , 482 Total Fixed-Income, 20% Turnover Ratio	% Net Assets
⊕	3 mil	Invesco High Yield R6	13.19
⊕	265,852	Invesco European Growth Y	11.09
⊕	290,817	Invesco International Growth R6	10.98
⊕	267,650	Invesco Asia Pacific Growth Y	9.63
	0	Ftse 100 Index Future	7.98
⊕	317,977	Invesco Diversified Dividend R6	6.58
	0	Russell 2000 Mini	-6.56
	600	Invesco Cayman Cmdty Fd Vii Gtr	6.02
	0	Msci Ac Asia Index Future	-5.55
	0	E-Mini S&P 500	-5.39
	0	Stoxx Europe 600 Index Future	-4.91
	0	Mini Msci Emg	4.34
	0	Dow Jones Eurostoxx 50	-4.32
	0	Caa Index	2.99
	0	Spi 200 Futures (Sydeny)	-2.21

Sector Weightings	Stocks %	Rel Std Index
Cyclical	**48.3**	**1.20**
Basic Materials	3.0	0.62
Consumer Cyclical	19.5	1.61
Financial Services	20.4	1.12
Real Estate	5.4	1.08
Sensitive	**28.6**	**0.82**
Communication Services	4.4	1.18
Energy	6.0	1.00
Industrials	8.9	0.75
Technology	9.4	0.69
Defensive	**23.1**	**0.93**
Consumer Defensive	11.6	1.29
Healthcare	6.9	0.61
Utilities	4.6	1.06

Operations

Family:	Invesco	Ticker:	GLTAX	Incept:	12-19-2013
Manager:	Multiple	Minimum Initial Purchase:	$1,000	Type:	MF
Tenure:	1.8 Years	Min Auto Investment Plan:	$50	Total Assets:	$138.60 mil
Objective:	Growth and Income	Minimum IRA Purchase:	$250		
Base Currency:	USD	Purchase Constraints:	—		

Fund Reports

JPMorgan Multi-Manager Alternatives

by **Elizabeth Weilburg**

Advisor
J.P. Morgan Alternative Asset Management

Advisor Location
New York, New York

Assets Under Management
$213.6 million

Inception Date
Nov. 3, 2014

Investment Type
Mutual fund

Morningstar Category
Multialternative

People
The fund is comanaged by Paul Zummo, Randy Wachtel, and Christopher Marshall. Zummo is the CIO of J.P. Morgan Alternative Asset Management and also co-founded the group in 1994. He sits on the six-person investment committee, which requires a two thirds approval to add a new manager to the portfolio. The investment committee has an average of 13 years' experience within the group and includes a risk management officer who wields a veto vote. Wachtel is a managing director of JPMAAM and joined the group in 2001, specializing in long-short equity and event-driven strategies. Marshall joined the group in 2007 and is an executive director with expertise in relative-value due diligence. Prior to joining the team, Marshall founded an equity derivatives trading firm. None of the three has any investment in the fund, as of the most recent Statement of Additional Information.

Purpose
Like many multimanager funds in the multialternative category, this fund looks to produce consistent absolute returns (middle-single-digit net returns over the U.S. Treasury bill) along with reduced levels of correlation and volatility, defined by management as a beta of less than 0.3 relative to the S&P 500 and the Barclays U.S. Aggregate Bond Index, with expected volatility of 4% to 6%.

Process
The Alternative Asset Management Hedge Fund Solutions (JPMAAM HFS) group at J.P. Morgan oversees the management of this fund. This 78-person team, founded in 1994, selects managers and constructs portfolios for J.P. Morgan's private alternative hedge funds and thus leverages significant experience applicable to the mutual fund. A six-person investment committee includes the group's president and CIO and a risk management officer who holds veto power. Two strategy teams focused broadly on relative value and long-short or event-driven equity strategies collaborate on due diligence and allocation decisions. Manager selection is informed by an actively monitored hedge fund manager database, and a subset of these managers is identified as appropriate for use in a mutual fund. To determine manager allocations, the team first identified 23 substrategies or styles that it considers well-suited to a mutual fund. From there, the team uses its expertise to qualitatively evaluate each strategy on expected future performance, dislocation/inefficiency, and riskiness. The team also monitors correlation between managers as part of its risk management process to ensure portfolio diversification. The managers expect the fund to increase the number of underlying managers from eight to between 12 and 15 as assets increase, and they expect 10%–15% manager turnover over 18-month periods.

Portfolio
The fund's portfolio was allocated to five substrategies and eight subadvisors as of July 31, 2015. Relative value represents the largest stake in the portfolio at 32.8%, while event-driven is at the upper end of its designated range at 29.5%. Long-short equity and opportunistic/macro (essentially a managed-futures strategy) are currently at the middle of their target ranges, with 22.7% and 9.7% allocated, respectively. The fund does not currently hold any credit strategies, as the managers believe the credit environment offers limited opportunities. The fund's allocation to event-driven is divided between P. Schoenfeld Asset Management and Owl Creek, both multi-event-driven managers, while the relative-value allocation is composed of Ionic (traditional multistrategy), Achievement (fundamental equity market-neutral), and J.P. Morgan (quantitative multistrategy). Passport Capital was recently added as long-short equity manager, but the fund has not changed any other managers to date.

Price
With an expense ratio of 2.35% for the A share class and 2.10% for the institutional class, this fund looks relatively expensive when compared with its similarly distributed peers. When compared with all funds in the alternative space, the fund receives a Morningstar Fee Level of Above Average, which is the second-highest-percentile fee designation.

JPMorgan Multi-Manager Alternatives A JMMAX

Standard Index	Category Index	Morningstar Cat
Morningstar Mod Tgt Risk TR USD	Morningstar Mod Tgt Risk TR USD	US OE Multialternative

Performance 09-30-2015

Quarterly Returns	1st Qtr	2nd Qtr	3rd Qtr	4th Qtr	Total %
2013	—	—	—	—	—
2014	—	—	—	—	—
2015	2.24	-1.61	-1.44	—	-0.85

Trailing Returns	1 Yr	3 Yr	5 Yr	10 Yr	Incept
Load-adj Mthly	—	—	—	—	-4.74
Std 09-30-2015	—	—	—	—	-4.74
Total Return	—	—	—	—	0.53
+/- Std Index	—	—	—	—	—
+/- Cat Index	—	—	—	—	—
% Rank Cat	—	—	—	—	
No. in Cat	—	—	—	—	

	Subsidized	Unsubsidized
7-day Yield	—	—
30-day SEC Yield	—	—

Performance Disclosure

The Overall Morningstar Rating is based on risk-adjusted returns, derived from a weighted average of the three-, five-, and 10-year (if applicable) Morningstar metrics.

The performance data quoted represents past performance and does not guarantee future results. The investment return and principal value of an investment will fluctuate; thus an investor's shares, when sold or redeemed, may be worth more or less than their original cost.

Current performance may be lower or higher than return data quoted herein. For performance data current to the most recent month-end, please call 800-480-4111 or visit www.jpmorganfunds.com.

Fees and Expenses

Sales Charges

Front-End Load %	**5.25**
Deferred Load %	**NA**

Fund Expenses

Management Fees %	1.75
12b1 Expense %	0.25
Net Expense Ratio %	**2.35**
Gross Expense Ratio %	**3.36**

Risk and Return Profile

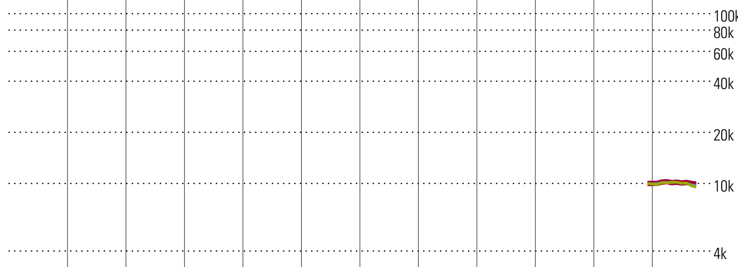
	3 Yr 227 funds	5 Yr 140 funds	10 Yr 28 funds
Morningstar Rating™	—	—	—
Morningstar Risk	—	—	—
Morningstar Return	—	—	—

	3 Yr	5 Yr	10 Yr
Standard Deviation	—	—	—
Mean	—	—	—
Sharpe Ratio	—	—	—

MPT Statistics	Standard Index	Best Fit Index
Alpha	—	—
Beta	—	—
R-Squared	—	—

12-Month Yield	—
Potential Cap Gains Exp	—

	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	09-15
Investment Style Equity Stock %	—	—	—	—	—	—	—	—	—	—	—	71



Growth of $10,000

- JPMorgan Multi-Manager Alternatives A 9,915
- Category Average 9,701
- Standard Index 9,513

Performance Quartile (within category)

History	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	09-15
NAV/Price	—	—	—	—	—	—	—	—	—	—	15.21	15.08
Total Return %	—	—	—	—	—	—	—	—	—	—	—	-0.85
+/- Standard Index	—	—	—	—	—	—	—	—	—	—	—	3.18
+/- Category Index	—	—	—	—	—	—	—	—	—	—	—	3.18
% Rank Cat	—	—	—	—	—	—	—	—	—	—	—	—
No. of Funds in Cat	—	—	—	—	—	—	—	—	—	—	—	470

Portfolio Analysis 08-31-2015

Asset Allocation %	Net %	Long %	Short %
Cash	22.15	22.35	0.20
US Stocks	40.35	109.21	68.86
Non-US Stocks	9.67	20.48	10.81
Bonds	12.53	13.09	0.56
Other/Not Clsfd	15.30	17.93	2.63
Total	100.00	183.05	83.05

Equity Style (Value / Blend / Growth; Large / Mid / Small)

Portfolio Statistics	Port Avg	Rel Index	Rel Cat
P/E Ratio TTM	18.4	1.12	1.03
P/C Ratio TTM	10.3	1.15	1.07
P/B Ratio TTM	2.5	1.29	1.34
Geo Avg Mkt Cap $mil	21790	1.00	1.22

Fixed-Income Style (Ltd / Mod / Ext; High / Med / Low)

Avg Eff Maturity	—
Avg Eff Duration	—
Avg Wtd Coupon	—
Avg Wtd Price	197.07

Credit Quality Breakdown —	Bond %
AAA	—
AA	—
A	—
BBB	—
BB	—
B	—
Below B	—
NR	—

Regional Exposure	Stock %	Rel Std Index
Americas	84.8	1.17
Greater Europe	11.6	0.78
Greater Asia	3.6	0.28

Share Chg since 07-2015	Share Amount	Holdings: 1,342 Total Stocks , 3,465 Total Fixed-Income, — Turnover Ratio	% Net Assets
⊕	84,454	SPDR® S&P 500 ETF	-27.70
⊕	9,316	Allergan PLC	4.70
⊕	60,490	Yahoo! Inc	3.24
⊕	19,736	Yum Brands Inc	2.61
⊕	36,131	AerCap Holdings NV	2.52
⊕	21,751	Alibaba Group Holding Ltd ADR	-2.39
⊕	26,891	US Concrete Inc	-2.31
⊕	50,100	eBay Inc	2.25
⊕	2,169	Google Inc Class C Capital Stock	2.23
⊕	13,362	W R Grace & Co	2.19
⊕	5,986	Time Warner Cable Inc	1.85
✲	4,834	Precision Castparts Corp	1.85
⊕	20,365	Broadcom Corp	1.75
⊕	11,017	Hospira Inc	1.64
⊖	20,890	Consumer Staples Select Sector SPD	-1.64

Sector Weightings	Stocks %	Rel Std Index
Cyclical	**41.2**	**1.02**
Basic Materials	9.1	1.88
Consumer Cyclical	19.9	1.64
Financial Services	11.0	0.61
Real Estate	1.1	0.23
Sensitive	**37.2**	**1.06**
Communication Services	4.6	1.24
Energy	4.3	0.71
Industrials	14.3	1.21
Technology	14.1	1.04
Defensive	**21.6**	**0.87**
Consumer Defensive	6.4	0.71
Healthcare	13.6	1.20
Utilities	1.6	0.37

Operations

Family:	JPMorgan	Base Currency:	USD	Purchase Constraints:	—
Manager:	Multiple	Ticker:	JMMAX	Incept:	11-03-2014
Tenure:	0.9 Year	Minimum Initial Purchase:	$1,000	Type:	MF
Objective:	Growth	Min Auto Investment Plan:	$1,000	Total Assets:	$208.43 mil

Fund Reports

Kellner Merger

by **Josh Charlson, CFA**

Advisor
Kellner Management, LP

Advisor Location
New York, New York

Assets Under Management
$133.7 million

Inception Date
June 29, 2012

Investment Type
Mutual Fund

Morningstar Category
Market Neutral

People
George Kellner founded Kellner DiLeo & Co., LP (the predecessor to Kellner Capital) in 1981 and launched a merger-arbitrage limited partnership. In 2012, the strategy debuted as a mutual fund. Kellner began his career as a securities lawyer at Carter, Ledyard and Milburn, became a portfolio manager at the Madison Fund, and later founded the arbitrage department at Donaldson, Lufkin & Jenrette. He is a Chartered Financial Analyst and holds a bachelor's degree from Trinity College, a law degree from Columbia Law School, and a master's from New York University's Stern School of Business. He oversees portfolio construction and risk management. Kellner invests more than $1 million in the fund.

Christopher Pultz joined Kellner Capital in 1999 and became the lead portfolio manager of the merger-arbitrage strategy in 2009. He began his career at Neuberger Berman. Pultz holds a bachelor's degree in finance from Fairfield University and a master's in business administration from Fordham University. He invests between $10,001 and $50,000 in the mutual fund. Pultz is supported by director of research Scott Kim and one trader.

Purpose
This fund follows a merger-arbitrage strategy. It should offer returns in the low- to mid-single digits with low correlations to stock and bond markets. Merger-arbitrage returns increase with short-term interest rates, making it a potential substitute for fixed income in a rising-rate environment.

Process
The fund employs a classic merger-arbitrage strategy, eschewing noncore positions in fixed income or special-situations equities. Typically, merger-arbitrage strategies involve buying the stock of the company being acquired in an announced stock deal while shorting the stock of the acquisitor in order to capture the spread between the announced deal price and the current trading price of the target company. The managers scan the market daily for potential merger-arbitrage opportunities and narrow down the universe based on the deal's likelihood of completion, rate of return, and value at risk. They will invest only in announced deals.

A key differentiator of this fund is its concentrated approach, as management typically invests in 25–50 deals. The major risk to merger-arbitrage strategies is a deal break (that is, when an announced deal fails to complete), and a more concentrated approach raises the stakes in this regard. To control those risks, George Kellner and Christopher Pultz implement portfolio-level risk management measures. They limit any individual position to no more than 10% of the portfolio and, more importantly, look to put no more than 2% of the fund's net asset value at risk in the event of a deal break on a single transaction. That hasn't made the fund immune to deal breaks (such as the AbbVie-Shire deal in 2014), but the fund has nevertheless posted category-beating returns since inception.

Portfolio
As of June 30, 2015, the fund was invested in 41 total deals, represented in the portfolio through 41 long positions and 17 short positions. The largest positions in the fund were Family Dollar Stores, at 7.71% (and net 5.82% in the deal when considering the short position in acquirer Dollar Tree), and 6.6% in a Time Warner private placement (net of 5.03% with the corresponding short on Charter Communications). The fund's largest sector concentrations were in financial services (18.5%), consumer cyclical (18%), and technology (14.2%). The median market cap of the fund was $6.5 billion, with nearly 70% of the portfolio in small- and mid-cap stocks. Nearly all of the holdings were concentrated in North America (98%), where the managers have historically focused their research efforts.

Price
Kellner Merger is offered in Institutional and Investor share classes, which charge 1.50% and 1.75%, respectively. Fees are average compared with similarly distributed alternative mutual funds.

Kellner Merger Investor GAKAX

Overall Morningstar Rating™	Standard Index	Category Index	Morningstar Cat
★★★★ 99 US OE Market Neutral	Barclays US Agg Bond TR USD	USTREAS T-Bill Auction Ave 3 Mon	US OE Market Neutral

Performance 09-30-2015

Quarterly Returns	1st Qtr	2nd Qtr	3rd Qtr	4th Qtr	Total %
2013	1.47	0.68	1.34	0.89	4.45
2014	0.98	0.39	0.58	1.32	3.31
2015	2.01	1.13	-1.49	—	1.63

Trailing Returns	1 Yr	3 Yr	5 Yr	10 Yr	Incept
Load-adj Mthly	2.98	3.60	—	—	3.51
Std 09-30-2015	2.98	—	—	—	3.51
Total Return	2.98	3.60	—	—	3.51
+/- Std Index	0.04	1.89	—	—	—
+/- Cat Index	2.95	3.56	—	—	—
% Rank Cat	19	9	—	—	
No. in Cat	164	99	—	—	

	Subsidized	Unsubsidized
7-day Yield	—	—
30-day SEC Yield	—	—

Performance Disclosure

The Overall Morningstar Rating is based on risk-adjusted returns, derived from a weighted average of the three-, five-, and 10-year (if applicable) Morningstar metrics.

The performance data quoted represents past performance and does not guarantee future results. The investment return and principal value of an investment will fluctuate; thus an investor's shares, when sold or redeemed, may be worth more or less than their original cost.

Current performance may be lower or higher than return data quoted herein. For performance data current to the most recent month-end, please call 855-535-5637 or visit www.kellnerfunds.com.

Fees and Expenses

Sales Charges

Front-End Load %	**NA**
Deferred Load %	**NA**

Fund Expenses

Management Fees %	1.25
12b1 Expense %	0.25
Net Expense Ratio %	**1.77**
Gross Expense Ratio %	**4.77**

Risk and Return Profile

	3 Yr 99 funds	5 Yr 74 funds	10 Yr 31 funds
Morningstar Rating™	4★	—	—
Morningstar Risk	Avg	—	—
Morningstar Return	+Avg	—	—

	3 Yr	5 Yr	10 Yr
Standard Deviation	3.12	—	—
Mean	3.60	—	—
Sharpe Ratio	1.14	—	—

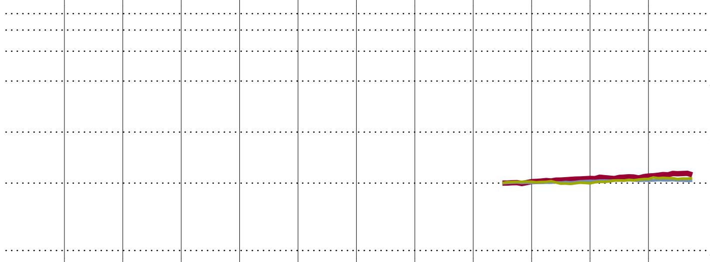
MPT Statistics	Standard Index	Best Fit Index Morningstar Small Growth TR USD
Alpha	3.89	2.26
Beta	-0.21	0.11
R-Squared	3.66	22.14

12-Month Yield	—
Potential Cap Gains Exp	1.35%

Investment Style
Equity Stock %

2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	09-15
—	—	—	—	—	—	—	—	55	70	63	75

Growth of $10,000
- Kellner Merger Investor 11,186
- Category Average 10,328
- Standard Index 10,688



Performance Quartile (within category)

	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	09-15	**History**
	—	—	—	—	—	—	—	—	10.20	10.21	10.43	10.60	NAV/Price
	—	—	—	—	—	—	—	—	—	4.45	3.31	1.63	Total Return %
	—	—	—	—	—	—	—	—	—	6.48	-2.66	0.50	+/- Standard Index
	—	—	—	—	—	—	—	—	—	4.39	3.28	1.61	+/- Category Index
	—	—	—	—	—	—	—	—	—	32	26	—	% Rank Cat
	—	—	—	—	—	—	—	—	—	132	188	173	No. of Funds in Cat

Portfolio Analysis 06-30-2015

Asset Allocation %	Net %	Long %	Short %
Cash	32.63	32.63	0.00
US Stocks	45.03	61.17	16.14
Non-US Stocks	23.35	36.13	12.79
Bonds	0.00	0.00	0.00
Other/Not Clsfd	-1.00	0.00	1.00
Total	100.00	129.93	29.93

Equity Style
Value Blend Growth
Large Mid Small

Portfolio Statistics	Port Avg	Rel Index	Rel Cat
P/E Ratio TTM	29.0	—	1.70
P/C Ratio TTM	—	—	—
P/B Ratio TTM	2.4	—	1.13
Geo Avg Mkt Cap $mil	6462	—	0.19

Fixed-Income Style
Ltd Mod Ext
High Med Low

Avg Eff Maturity	—
Avg Eff Duration	—
Avg Wtd Coupon	—
Avg Wtd Price	—

Credit Quality Breakdown —	Bond %
AAA	—
AA	—
A	—
BBB	—
BB	—
B	—
Below B	—
NR	—

Regional Exposure	Stock %	Rel Std Index
Americas	98.4	—
Greater Europe	1.6	—
Greater Asia	0.0	—

Share Chg since 03-2015	Share Amount	Holdings: 65 Total Stocks , 3 Total Fixed-Income, 214% Turnover Ratio	% Net Assets
⊕	113,600	Family Dollar Stores Inc	7.71
⊕	43,400	Twc Time Warner Cable Private Plac	6.66
⊕	119,150	Rock-Tenn Co	-6.18
⊕	102,700	MeadWestvaco Corp	4.18
☼	80,600	Ppo Equity Swap	4.16
☼	89,500	Brcm Eq Swap	3.97
⊕	33,000	Sigma-Aldrich Corp	3.96
☼	94,500	Ann Inc	3.93
⊕	35,610	M&T Bank Corp	-3.83
☼	35,700	Pll Equity Swap	3.83
⊕	49,000	Hospira Inc Swap	3.75
☼	58,000	Home Properties Inc	3.65
⊕	423,800	Hudson City Bancorp Inc	3.61
⊕	45,000	City National Corp	3.51
☼	81,200	Informatica Corp	3.39

Sector Weightings	Stocks %	Rel Std Index
Cyclical	**50.8**	**—**
Basic Materials	6.3	—
Consumer Cyclical	18.0	—
Financial Services	18.5	—
Real Estate	8.0	—
Sensitive	**28.5**	**—**
Communication Services	5.4	—
Energy	4.9	—
Industrials	4.0	—
Technology	14.2	—
Defensive	**20.7**	**—**
Consumer Defensive	12.2	—
Healthcare	7.5	—
Utilities	1.0	—

Operations

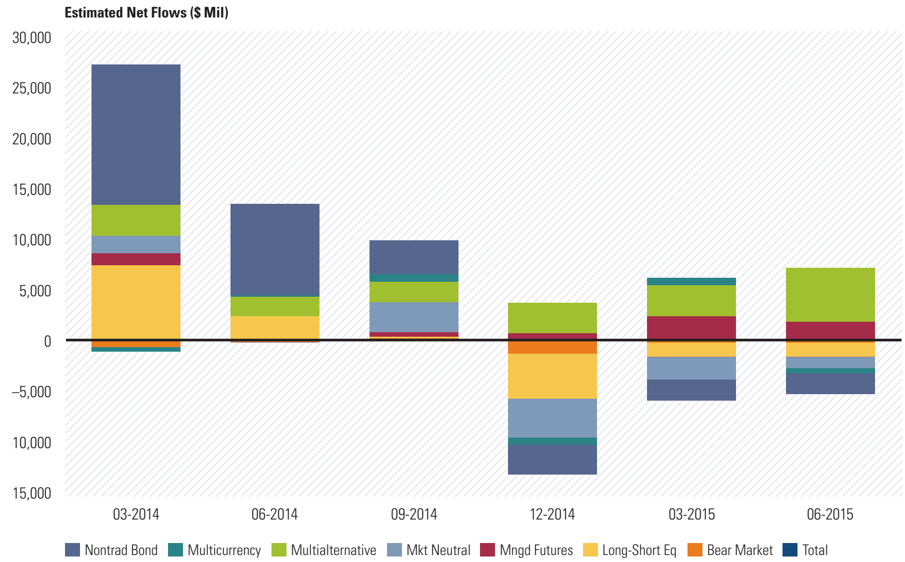
Family:	Kellner	Ticker:	GAKAX	Incept:	06-29-2012
Manager:	Multiple	Minimum Initial Purchase:	$2,000	Type:	MF
Tenure:	3.3 Years	Min Auto Investment Plan:	$100	Total Assets:	$120.77 mil
Objective:	World Stock	Minimum IRA Purchase:	$2,000		
Base Currency:	USD	Purchase Constraints:	—		

MORNINGSTAR®

Flows and Assets Under Management: Alternative Mutual Funds

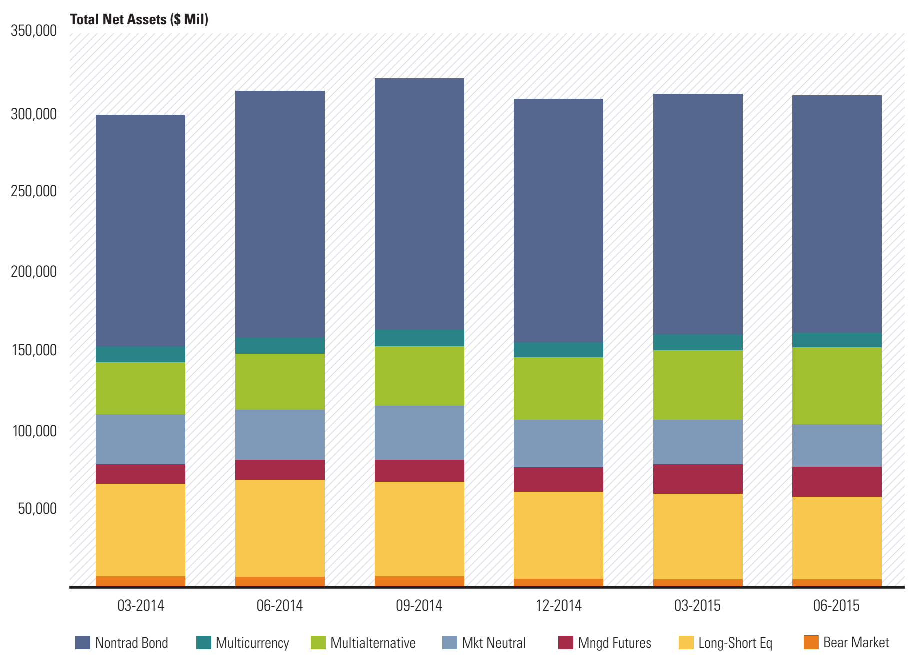
Quarterly Alternative Mutual Fund Flows

During the second quarter of 2015, alternative mutual funds' net inflows amounted to $1.9 billion, an expansion from last quarter's inflows of roughly $312 million. The multialternative and the managed-futures Morningstar Categories were the only categories that experienced inflows this quarter, with $5.2 billion and $1.8 billion, respectively, continuing an ongoing trend of significant inflows since 2014. The non-traditional-bond ($2 billion), long-short equity ($1.3 billion), market neutral ($1.1 billion), and bear-market ($157 million) categories experienced outflows for the third consecutive quarter, while multicurrency funds ($485 million) experienced a decline, despite inflows in the previous quarter.



Quarterly Alternative Mutual Fund Assets Under Management

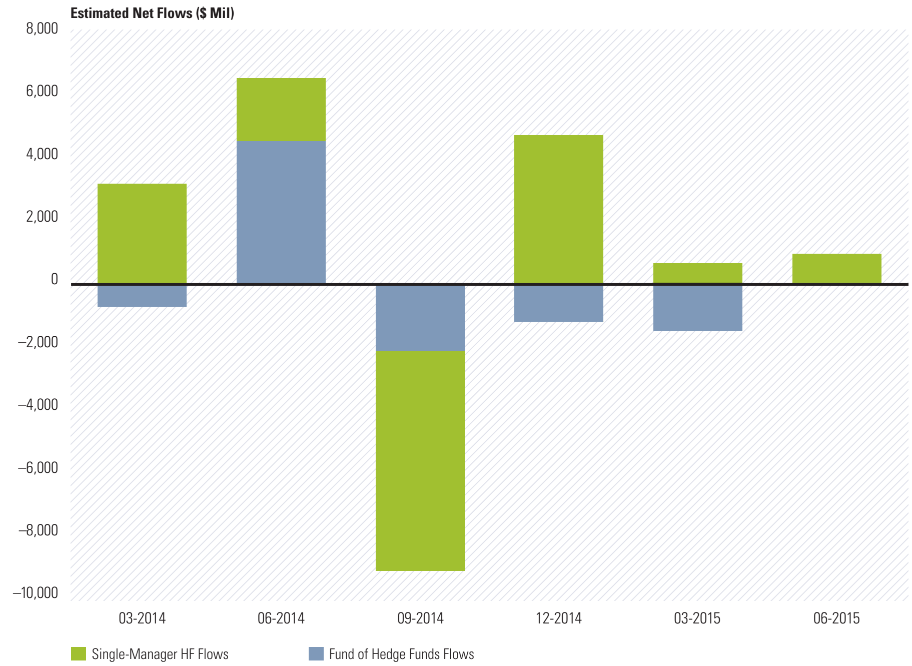
Assets under management for all alternative mutual funds decreased by 0.93% quarter over quarter, totaling more than $311 billion at the end of June 2015. Five of the seven alternative mutual fund categories decreased in assets in the second quarter. Bear-market and market-neutral funds experienced the largest percentage losses in assets, losing 30.34% and 15.27% since 2014, respectively, and losing 4.25% and 4.17% this quarter. Long-short equity, multi-currency, and non-traditional-bond funds all also showed losses both this quarter and year over year. Multialternative and managed-futures funds fared well over the quarterly and yearly time frames, increasing assets 10.37% and 2.02% this past quarter, respectively, and 37.00% and 52.91% over the year.



Flows and Assets Under Management: Hedge Funds

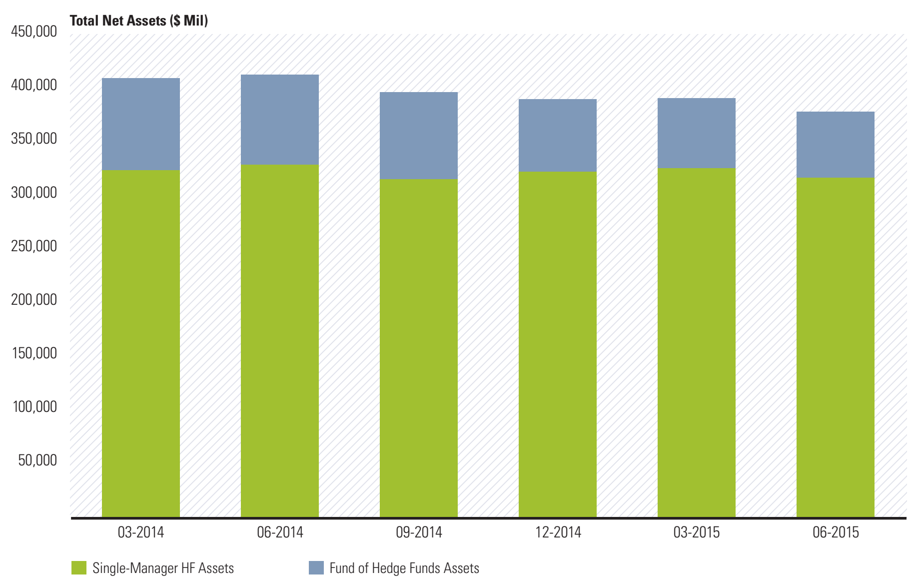
Quarterly Hedge Fund Flows

Single-manager hedge funds in Morningstar's database experienced inflows of $914 million, and funds of hedge funds recorded inflows of $19 million during the second quarter of 2015. Multistrategy (single-manager) hedge funds experienced the highest inflows, with nearly $2.9 billion. Long-short debt (single manager) trailed with the second-highest inflows ($1.1 billion), marking a fourth consecutive quarter of inflows. Distressed securities, long-only other, and long-only equity (single-manager) hedge funds demonstrated the largest outflows of $933 million, $543 million, and $514 million, respectively. For the funds of hedge funds, debt and macro-systematic were the only categories to display positive flows this quarter, with inflows of $660 million and $49 million, respectively. Multistrategy funds, on the other hand, experienced the largest outflows ($481 million) for the fourth quarter in a row. Event-driven and equity funds of funds displayed the next largest outflows, at $96 million and $68 million, respectively.



Quarterly Hedge Fund Assets Under Management

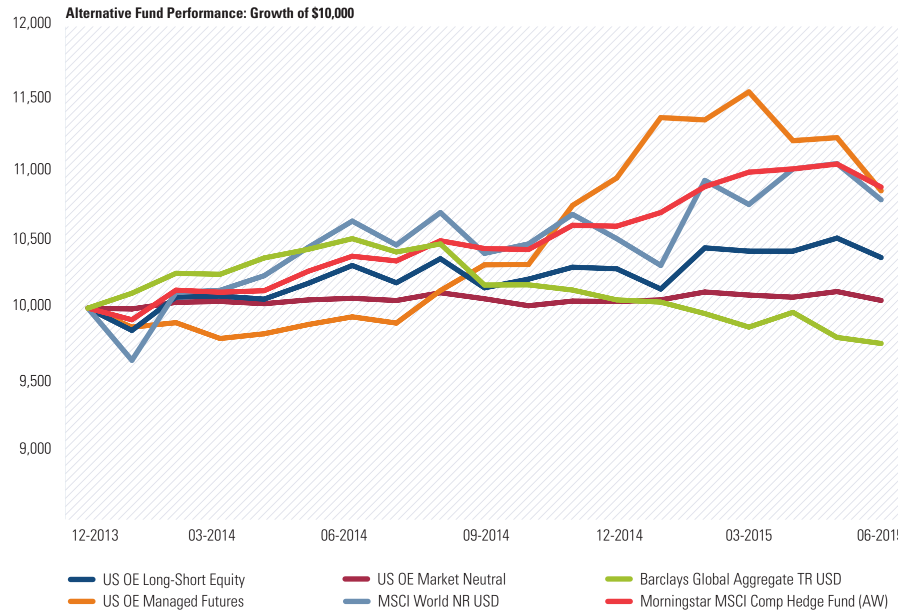
In the second quarter of 2015, assets under management for single-manager hedge funds in Morningstar's database decreased by 2.80%, to $316.6 billion. Despite gains over the previous two quarters, however, assets decreased by a total margin of 3.69% during the past year. Hedge funds of funds in Morningstar's database also managed 4.97% fewer assets than in the prior quarter, with $62.1 billion assets recorded as of June 30, 2015. Assets under management for hedge funds of funds decreased 26.41% year over year (from June 2014). Overall, assets declined by 3.16% this quarter, and 8.33% since June 2014.



Alternative Investment Performance

Growth of a $10,000 Alternative Investment

In the second quarter of 2015, global stocks, as represented by the MSCI World NR Index, displayed the only positive increase in comparison with all other alternative investment categories, growing by a mere 0.31%. The managed-futures category average experienced the sharpest decline this quarter, losing 6.09%. Hedge funds, as represented by the Morningstar MSCI Comp Hedge Fund Index, bond funds, as represented by the Barclays Global Bond Index, as well as the long-short equity and market-neutral category averages all experienced losses of approximately 1% during the same time period. During the 18 months ended June 30, 2015, the Morningstar MSCI Comp Hedge Fund Index displayed the highest return among the categories, at 8.6%. Managed-futures and global-stock funds experienced similar high-single-digit returns during this time period as well. During the same period, the Barclays Global Bond Index experienced the only negative returns among its peers, losing 2.51%.



*Morningstar no longer publishes proprietary hedge fund indexes. Morningstar now uses the Morningstar MSCI series of indexes, including the Morningstar MSCI Composite AW, a currency-hedged asset-weighted index of 1000 hedge funds, or the applicable category averages.

Performance of Alternative Investments Over Time

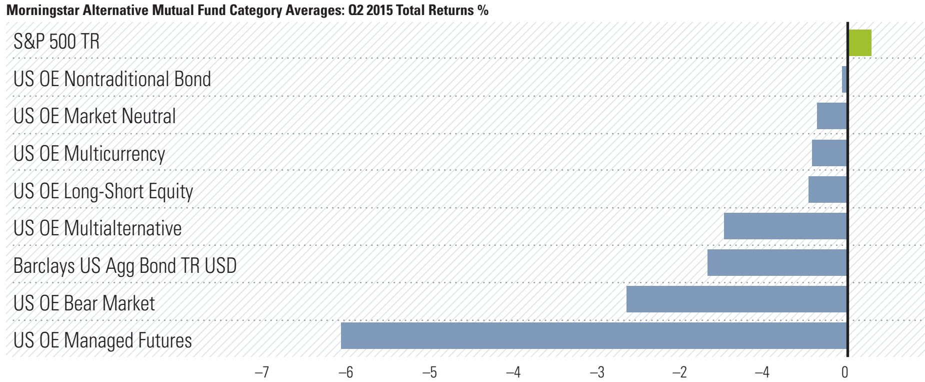
Despite losses in the previous quarter, alternative investments have had a relatively strong performance during the past one, three, and five years. Global stocks, as represented by the MSCI World NR Index, steadily outperformed all other alternative investments over the three- and five-year time frames (ended June 30) and sustained positive returns over the one-year period, as well as in the past quarter. Long-short equity funds, as well as hedge funds (as represented by the Morningstar MSCI Comp Hedge Fund Index) also displayed strong positive single-digit returns over the three- and five-year periods, with more-modest returns over the one-year period. Managed-futures funds displayed the highest one-year return but were slightly outpaced over the three- and five-year time frames and displayed the highest losses in the past quarter.

Second-Quarter Performance by Category

Alternative Mutual Funds

Alternative mutual funds struggled in the second quarter of 2015, with all categories displaying negative returns. The largest loss was experienced by the managed futures category, with a negative 6.06% return. Bear-market funds, which move inversely to the stock market, lost 2.65%, while multialternative funds lost 1.48%. the smallest losses were experienced by the long-short equity (-0.47%), multicurrency (-0.43%), market neutral (-0.37%), and non-traditional bond (-0.07%) categories. During the quarter the S&P 500 was up modestly at 0.28%, while the Barclays US Aggregate Bond Index lost 1.68%.

Morningstar Alternative Mutual Fund Category Averages: Q2 2015 Total Returns %

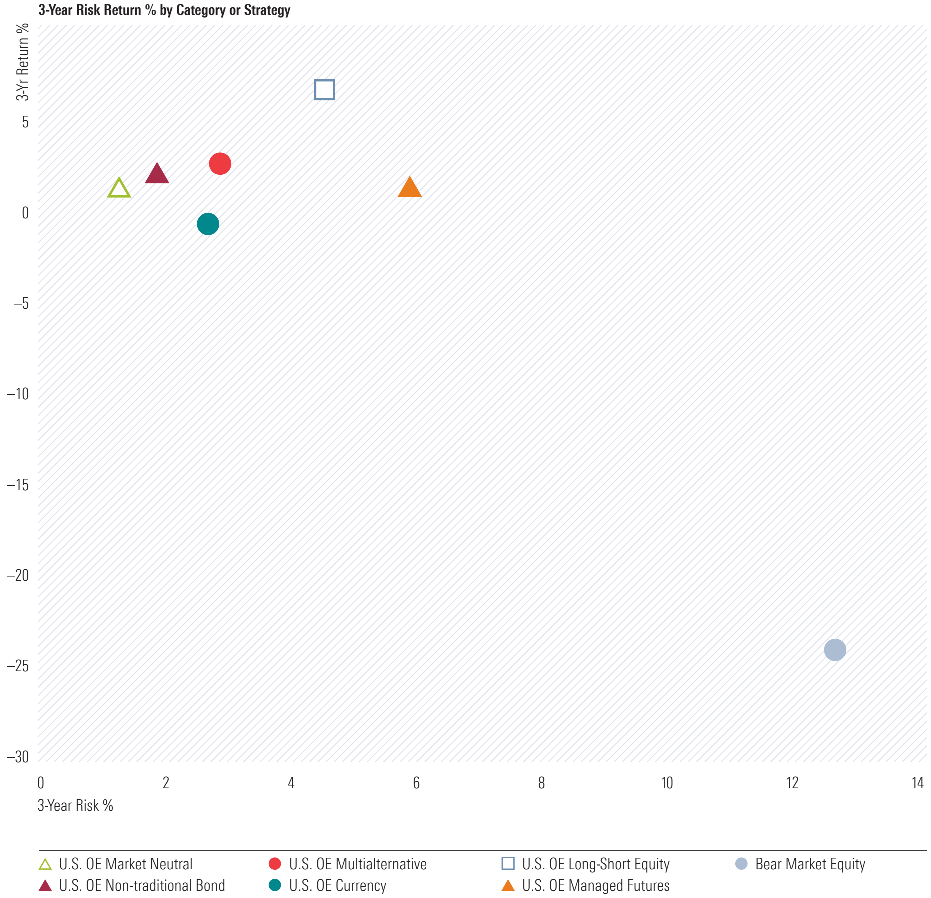


Risk Versus Return: Alternative Mutual Funds

Three-Year Standard Deviation and Return

Of the seven alternative mutual fund category averages, five displayed positive returns over the three-year period ending June 30, 2015. Long-short equity funds produced the highest three-year total returns, at 6.6%, while bear-market and multicurrency funds had the lowest returns, at negative 23.94% and negative 0.73%, respectively. Consequently, long/short equity funds also showed the highest risk-adjusted return (1.44%), while bear-market and multicurrency funds displayed the lowest (negative 1.89% and negative 0.27%).

3-Year Risk Return % by Category or Strategy



Correlations by Alternative Fund Strategy

Three-Year Correlations: Alternative Mutual Fund Categories	1	2	3	4	5	6	7
1 US OE Bear Market	1.00						
2 US OE Long-Short Equity	-0.96	1.00					
3 US OE Managed Futures	-0.12	0.14	1.00				
4 US OE Market Neutral	-0.68	0.77	0.31	1.00			
5 US OE Multialternative	-0.83	0.84	0.48	0.77	1.00		
6 US OE Multicurrency	-0.45	0.37	0.00	0.31	0.49	1.00	
7 US OE Nontraditional Bond	-0.51	0.49	0.09	0.41	0.72	0.61	1.00

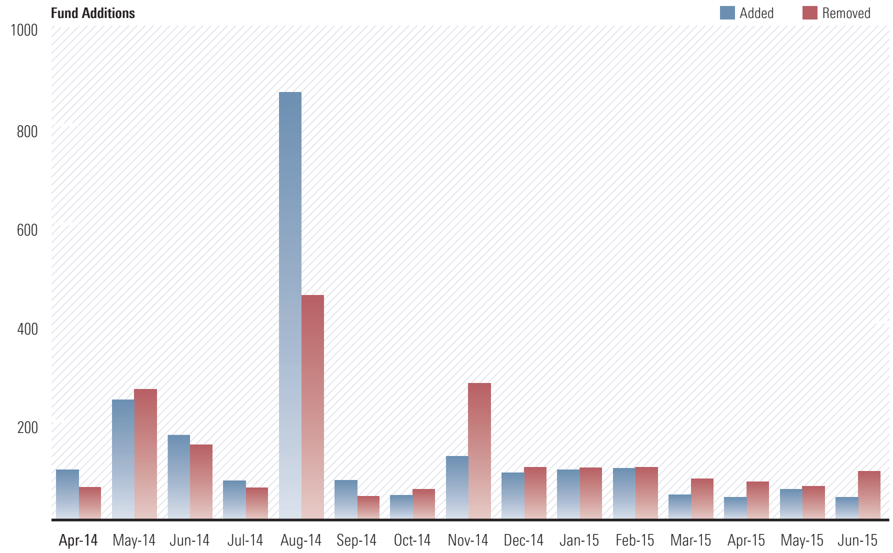
Correlations of Alternative Funds to Traditional Asset Classes

Correlation of Mutual Funds to U.S. Stocks and Bonds	S&P 500 Correlation (USD)			Barclays U.S. Agg Correlation (USD)		
	3-Year	5-Year	10-Year	3-Year	5-Year	10-Year
US OE Bear Market	-0.96	-0.95	-0.96	-0.01	0.14	-0.10
US OE Managed Futures	0.11	-0.05	—	0.46	0.40	—
US OE Multicurrency	0.39	0.67	0.45	0.33	0.12	0.11
US OE Multialternative	0.86	0.88	0.92	0.30	0.13	0.19
US OE Nontraditional Bond	0.62	0.68	0.70	0.15	0.14	0.19
US OE Market Neutral	0.76	0.82	0.20	0.25	-0.08	-0.03
US OE Long/Short Equity	0.96	0.98	0.95	0.03	-0.20	0.02

Morningstar Hedge Fund Database Overview as of 6-30-2015

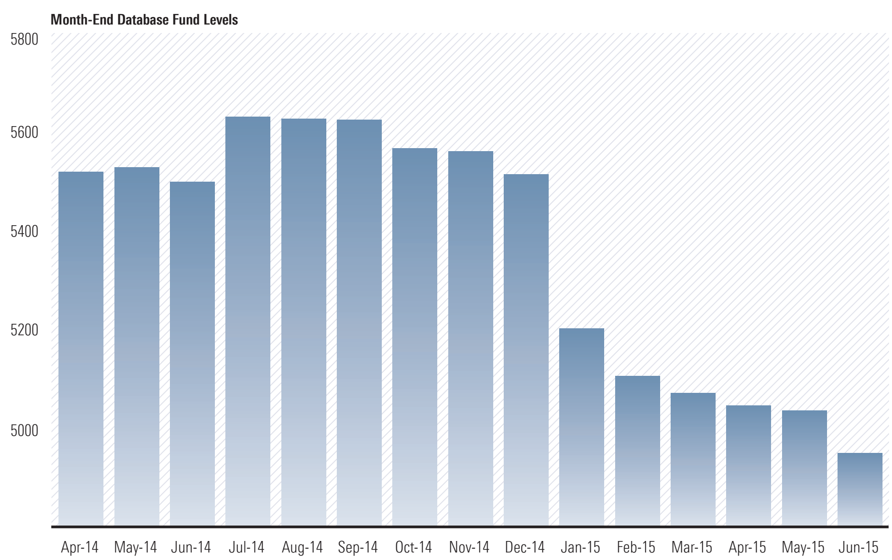
Net Fund Additions by Month

In the second quarter of 2015, Morningstar's hedge fund database experienced a net removal of 89 funds. During the quarter, the database saw 154 additions and 243 fund withdrawals. Funds drop out because they have liquidated or because they cease sharing performance data, typically because of poor performance. Fund additions occur as a result of new fund launches or a recent decision to supply data to Morningstar.



Month-End Database Fund Levels

As of June 30, 2015, the Morningstar hedge fund database contained 4,948 funds that actively report performance and assets-under-management data. This figure includes 3,201 single-manager hedge funds, 1,341 funds of hedge funds, and 406 CTAs and managed futures. As of quarter-end, the number of funds in the database had dropped approximately 1.02% from April 2015 levels.

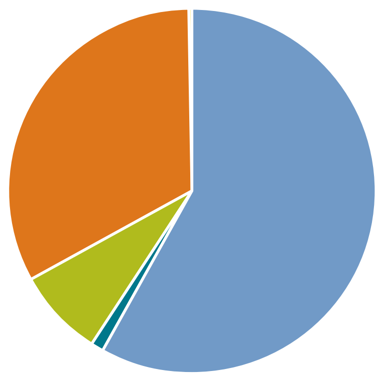


Morningstar Hedge Fund Database Overview as of 6-30-2015

Hedge Funds by Region

Approximately 58% of hedge funds in the Morningstar database are legally domiciled in the North American/Caribbean region, primarily in the Cayman Islands and United States. A large percentage of U.K. hedge funds are also domiciled in the Cayman Islands for tax and regulatory purposes. Roughly 32% of funds in Morningstar's database are domiciled in Europe, including both European Union and non-EU jurisdictions, and almost 8% of funds are domiciled in Asia and Australia, primarily in China (94%). All figures are as of June 30, 2015.

Morningstar Hedge Fund Database by Region



Region	# Funds
N. America/Caribbean	2,879
Africa	50
Asia/Australia	394
Europe	1,624
South America	1
Total	**4,948**

Hedge Funds by Location

Approximately 81% of the hedge funds in Morningstar's database are domiciled in the United States, the Cayman Islands, China, Canada, the British Virgin Islands, Bermuda, and Luxembourg. Switzerland, France, and Ireland continue to domicile a large portion of European hedge funds as well, trailing Luxembourg.

N. America / Caribbean	**2,879**
Cayman Islands	1,160
United States	1,039
British Virgin Islands	258
Canada	211
Bermuda	162
Curaçao	39
Bahamas	9
Barbados	1

Africa	**50**
Mauritius	24
South Africa	21
Seychelles	2
United Arab Emirates	2
Swaziland	1

Asia/Australia	**394**
China	371
Australia	12
Israel	3
Bahrain	2
Hong Kong	2
Christmas Island	1
India	1
Japan	1
Marshall Islands	1
Vanuatu	1

Europe	**1,624**
Luxembourg	791
Ireland	244
Switzerland	103
France	93
Guernsey	93
Spain	58
Italy	56
Liechtenstein	33
Jersey	30
Netherlands	26
United Kingdom	25
Malta	16
Gibraltar	15
Sweden	8
Germany	6
Isle of Man	6
Austria	5
Macedonia	4
Channel Islands	3
Finland	3
Norway	2
Portugal	2
Belgium	1
Denmark	1

South America	**1**
Chile	1

Morningstar Hedge Fund Database Overview as of 6-30-2015

Service Providers

Morgan Stanley, Goldman Sachs, and Credit Suisse AG are the largest prime brokerage-service providers to hedge funds in Morningstar's database, serving an almost 18% share combined. The big four accounting firms are employed by approximately 78% of the hedge funds listed in Morningstar's database, with PricewaterhouseCoopers leading the pack. Citco provides administration services to 7.01% of funds in Morningstar's database, while BNY services 6.09% of funds in the database. Maples & Calder; Elvinger, Hoss & Prussen; and Walkers are the three largest legal-counsel-service providers to hedge funds in the database, with a combined market share of almost 17%. This data is as of June 2015.

Type	Rank	Service Provider	% of Database
Prime Broker	1	Morgan Stanley	6.89
	2	Goldman Sachs	6.60
	3	Credit Suisse AG	4.29
	4	UBS	4.11
	5	J.P. Morgan	4.08
	6	Deutsche Bank	2.60
	7	Newedge Group	2.31
	8	Interactive Brokers	1.98
	9	BNP Paribas	1.69
	10	Bank of America	1.26
Legal Counsel	1	Maples & Calder	6.80
	2	Elvinger, Hoss & Prussen	5.24
	3	Walkers	4.79
	4	Seward & Kissel	4.28
	5	Dechert	3.38
	6	Sidley Austin	3.26
	7	Schulte Roth & Zabel	2.49
	8	Ogier	2.39
	9	Simmons & Simmons	2.01
	10	Matheson Ormsby Prentice	1.76
Auditor	1	Pricewaterhouse Coopers	23.55
	2	Ernst & Young	22.16
	3	KPMG	17.59
	4	Deloitte	15.48
	5	Rothstein Kass	4.26
	6	McGladrey LLP	2.21
	7	BDO	1.41
	8	Grant Thornton	1.74
	9	Eisner Amper	1.18
	10	Arthur Bell	0.29
Administrator	1	Citco	7.01
	2	BNY	6.09
	3	Fund Partner Solutions	4.37
	4	UBS	3.96
	5	State Street	3.12
	6	Northern Trust	2.74
	7	RBC	2.63
	8	HSBC	2.27
	9	Citi	2.05
	10	Credit Suisse	2.02

Alternative Investments Observer

Editor
Josh Charlson

Contributors
Josh Charney; Janet Yang;
Elizabeth Weilburg; Jason Kephart

Copy Editor
Edward Cavanaugh

Design
Chris Cantore; Barbara Kennedy; Christine Lee

Data Collection
Elizabeth Weilburg

Publisher/Director of Global Manager Research
Jeff Ptak

Director of Manager Research, North America
Jon Hale

President of Research
Haywood Kelly

For inquiries contact: **newslettersupport@morningstar.com** or **josh.charlson@morningstar.com**