

Market Commentary First Quarter 2015

Dear Client,

I've often commented on the similarities between climbing mountains and managing investment portfolios. Both endeavors require preparation, perseverance, risk assessment and discipline.

The first quarter of 2015 was a good test of those skills as a portfolio manager. Volatility returned, with the sawtooth action in the financial markets reminding me of California's Sierra Nevada Mountains. The Dow was down nearly 3.7% in January, and then rose a steep 5.6% in February, only to slip again by 2% in March, ending the quarter about where it began. It was a similar wild ride for the Standard & Poor 500 Index and the tech-laden Nasdaq Composite.

Volatility occurs when investor sentiment swings between fear and optimism, and Q1 gave investors plenty of reasons for both. Oil prices fell but then recovered somewhat. The U.S. dollar strengthened, but created fears that U.S. goods would become too expensive and hurt earnings. (So far, those fears are largely unfounded.) Meanwhile, the Fed signaled it would raise rates in June, and then hinted it might remain "patient" a little longer. With such a muddled outlook, it's no surprise that some market pundits think the economy is picking up steam while others think it is merely chugging along.

The events of the first quarter of 2015 did nothing to make me change my cautious outlook for the financial markets. As contrarians, 7Summit Advisors aims to limit downside risk in a number of

ways, including buying out-of-favor stocks and picking through the rubble of out-of-favor sectors.

A good example is Petróleo Brasileiro S.A. (NYSE: PBR), better known as Petrobras. It's a contrarian's "twofer", an out-of-favor company in an out-of-favor sector. The Brazilian state-run oil and gas company is engulfed in a massive corruption scandal, one that reportedly involves billions of dollars in bribes and illegal funds, politically scarring Brazil's President Dilma Rousseff, a former chairwoman of the company's board of directors. At the same time, Petrobras has vast undersea reserves, and is likely to get government support. We think the stock has been oversold.

Other positions in the out-of-favor oil patch include Chesapeake Energy Corp. (NYSE: CHK), the second-largest natural gas producer in the U.S., and United States Natural Gas Fund (NYSE: UNG), a limited partnership that invests in futures contracts on natural gas. We also like Brazil-based Vale S.A. (NYSE: VALE) a metals and mining company and the world's largest iron ore producer. It's another contrarian pick. A chart showing a precipitous decline in demand for iron ore prompted me to send it to a few colleagues in early April with the subject line, "Iron Ore, so bad, it is good?"

Finally, those of you who follow me on Twitter—@Lichang8—know I worry that much of the U.S. stock market's gains these past three years can be attributed to share buybacks. Instead of reinvesting profits in their businesses, Fortune 500 companies have been

spending cash reserves or borrowing money at cheap rates to buy back their shares and/or to pay shareholders handsome dividends.

I was heartened when Laurence Fink, the chairman and CEO of BlackRock, the world's largest asset manager, recently warned Fortune 500 CEO's that investing in buybacks and dividends are being done at the expense of investing in "innovation, skilled work forces or essential capital expenditures" that propel long-term growth. Good point, but I would also re-emphasize that buybacks also drive up demand for a company's stock and lift its stock price. Again, how much of this bull market is because of buy backs? Concerns like these require vigilance and I thank you for the confidence you have placed in me and in 7Summit Advisors.

Sincerely yours,

Li Chang