CHILTON TRUST

Quarterly Commentary: Second Quarter 2019

Highlights:

- A healthy economy, low inflation and increasing liquidity from a dovish Federal Reserve presents a constructive backdrop for equities.
- As we mentioned at the close of the first quarter, we are now in an investing backdrop that is more fully valued and tempers our return expectations for the coming months ahead. We would not be surprised by a pause or a pullback in markets between now and the end of the year, but as long term investors would seek to capitalize on any opportunities as they arise.

Introduction

PEPPER ANDERSON, Chief Executive Officer

This year has, so far, been an exciting one for me. At the time of this note, I am closing in on my first month as the new President and CEO of Chilton Trust. I join you, and the Chilton team, from J.P. Morgan where I spent over twenty years in the Private Bank. My career there began in fixed income and evolved to include a variety of other investment roles, with the second half of my tenure spent leading teams of advisors focused on delivering the full suite of the firm's capabilities. The breadth of this experience, especially given the changing landscape both for financial markets and the wealth management industry overall during that time, I hope will enable me to be a valued member of your team.

The opportunity to join and lead Chilton Trust, a firm anchored in investing excellence and committed to putting clients' best interests above all else, is one for which I am very grateful. I have been fortunate enough to meet with some of our valued clients already, and am struck by the feeling of family that permeates each relationship. My goal is to continue to grow our firm through word of mouth driven by exceeding your expectations. We are also committed to expanding our platform in whatever ways enable us to serve as your "first call" advisor for any financial concerns or opportunities that are on your mind. To that end, I plan to spend time in person over the coming months with each of our clients and friends with the hope of hearing your feedback and sharing with you some of our plans to enable us to continually serve you better.

As you will read in the updates to follow, our investment team continues to be constructive on markets, albeit mindful of year to date performance as well as the geopolitical and global economic challenges that are present. Our focus continues to be on portfolio resilience, reflected in both our equity and fixed income approaches. We look forward to continuing to collaborate with you on your portfolio and asset allocation over the remainder of the year.

Thank you, as always, for your continued trust and confidence. I look forward to getting to know you.

Equity Markets Review

RICHARD L. CHILTON, JR, Chairman & Chief Investment Officer – Equities
JENNIFER L. FOSTER, Co-Chief Investment Officer & Portfolio Manager– Equities

Market Commentary

The volatility drumbeat got louder during the second quarter as the now infamous Chinese tariff tweet by President Trump threw cold water over the white hot economic embers. Suddenly, the rhetoric turned towards economic uncertainty and the Federal Reserve shifted sentiment towards a more accommodative monetary policy. This economic uncertainty, coupled with policy moves in Washington regarding trade with Mexico, had a chilling effect on investor risk appetite.

Your investments performed exceedingly well with some superb gains from a broad list of your holdings whose fundamentals are performing above expectations.

One company in particular really delivered. The largest global manufacturer of aluminum cans, this company is especially exciting at present with nearly all aspects of their business performing well after years of careful planning. Demand for aluminum cans, and specialty cans in particular where this company dominates, is strong with beverage makers responding to the environmental and recycling challenges of plastic packaging by shifting to aluminum packaging. In addition, innovation continues with a new disposable aluminum cup that they developed about to be launched commercially and positioned to compete with the famous red Solo cup. Even the company's aerospace division (10% of revenues) which focuses on the alumina alloy is humming with strong demand from government and commercial interests alike. We are excited to see what the rest of the year holds for this investment.

When we think about making an investment, which we hope will be for the long term, our investment criteria of owning great business models at attractive entry prices is our hallmark. The difference in our approach today versus twenty years ago is our understanding of what truly constitutes a great business. We have three buckets in determining these businesses… 'yes', 'no' and 'I don't understand it'. Sometimes, we do get it wrong, but the vast majority of the time we succeed because we can analyze and understand the business that we invest in without the high seduction of what the young kids call… F.O.M.O. or the Fear of Missing Out. We have missed a lot of stock market winners and that's ok as long as we get right the ones we own. This maturity in our business model selection has made us better investors and has also helped us avoid a lot of losses.

We were struck by how much the Fear of Missing Out led to the seduction in Theranos, the fraudulent blood testing company profiled in the book *Bad Blood*, which we just finished and loved. This amazingly well researched and written book by Wall Street Journal reporter John Carreyrou is F.O.M.O. on steroids. Investors, board members, and strategic partners were all led astray by their fear of missing the really big one. This fear hugely manifests itself today in not only venture capital but also public stock markets.

We always keep an open mind and will evaluate any company's business model, but at the end of the day we have to be very comfortable with the long term sustainability of the business and future cash flows; we don't care if we miss out on big investments as

long as we get the ones we make right.

Investment Outlook

U.S. equity markets have had a strong move in 2019, though some of this was make-up for last year's fourth quarter sell-off that proved overdone. The Federal Reserve's recently revealed dovish posture as well as the temporary trade truce have fueled equities higher of late, and markets may have to consolidate a bit to digest the move. Inflation remains very low, and though some manufacturing indicators are showing signs of slowing, housing and confidence remain strong and liquidity is ample. We see a slowing but healthy economy at hand, with trade being one factor creating uncertainty and weather having been a cause of temporary demand disruption through some of the first half. We believe the timing of the U.S. 2020 political cycle will act as a governor on trade policy and while negotiations could continue to be choppy, both sides have strong motivations to find a compromise before we enter 2020. A healthy economy, low inflation and increasing liquidity from a dovish Federal Reserve presents a constructive backdrop for equities. Earnings season may show some companies underperforming because of weather or trade issues causing individual volatility; as always, we will be searching for the highest quality companies that may present compelling buys because of short term disruptions.

In addition to trade, another risk to future equity performance is the 2020 election cycle. While early, it is possible that acute fears of future policy change will develop among investors and hit markets, especially given the hard left policy proposals being floated through the primary process. If a more moderate candidate was to emerge as the leader, this risk would be mitigated, and it is still early enough for this to happen though the tenor of the race thus far is not rewarding moderate positions. In addition, geopolitical risks continue to mount as governments around the world turn more nationalistic and key tenets of globalization are challenged. These are hard risks to handicap, but ones which we follow with keen interest and analyze as events unfold. Much of the portfolio remains exposed to strong domestic companies, and small and mid-cap stocks' valuations are more in-line with historical averages than larger caps. We are very comfortable with our equity positioning given the strength of the business models in which we invest, many of which historically have demonstrated strong revenue durability through changing economic cycles.

Many thanks for the confidence and trust you have placed in us; we wish you a happy summer and we look forward to the balance of the year.

Fixed Income Markets Review

TIMOTHY W. A. HORAN

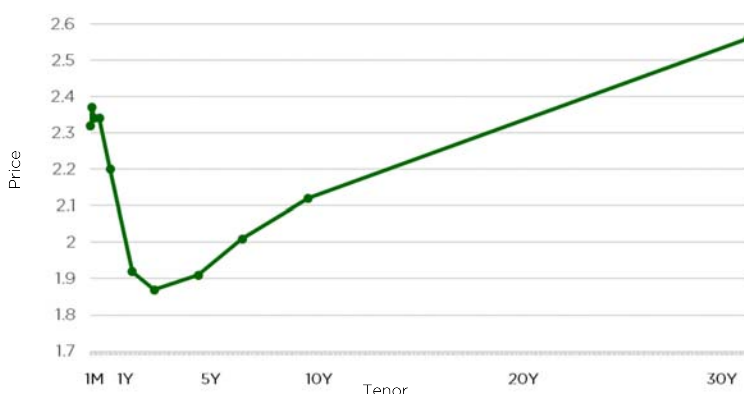
Executive Vice President & Chief Investment Officer - Fixed Income

Themes in the Second Quarter 2019

Although the second quarter began with firm readings on the robust health of the U.S. economy (in particular full employment and strong consumer data), as the quarter unfolded escalating trade tensions between the U.S. and China began to undermine business confidence and raise key questions about whether the growing global economic slowdown would result in an outright global recession.

While having already shifted its policy paradigm in the first quarter from "Rate Normalization" to "PDF—Patient, Data dependent, Flexible", the Federal Reserve increasingly struggled with conflicting signals from trade tensions and from the real economy. Asset markets increasingly began to anticipate the need for Fed action, epitomized in the inversion of the U.S. Treasury curve between 1 and 5 years.

Chart 1: U.S. Treasury Yield Curve Inversion



Source: Bloomberg

While an inversion has typically signaled a pending recession, in this instance the gravitational pull of negative interest rates in Europe and Japan, together with foreign central bank buying of 2-5 year U.S. Treasury securities has played a critical role in the shaping of this inversion.

At the 19th June meeting, the Federal Reserve dropped the word "patient" from its outlook, downgraded its assessment of economic activity from "solid" to "moderate", and paved the way for a first rate cut as soon as the July 31st meeting, stating "uncertainties about the outlook have increased" despite a robust labor market and muted inflationary expectations. At his press conference following the Fed meeting, Chairman Powell elevated the importance of "global" risks in assessing the chances for a sustained expansion of the U.S. economy: "The ratcheting up of international trade tensions, including tariffs applied by the U.S. and China, as well as the threat to imposed tariffs on Mexico, could lead to higher price and a possible reduction in consumer and business confidence."

The U.S. economy is unlikely to be able to withstand the growing slowdown in global growth, even with a robust labor market and a strong banking sector. Pronounced weakness in Germany and other European economies, together with China slowing further despite moderate stimulus measures, and continued disappointing results from Japan has compelled the Fed to prepare markets for its paradigm shift to rate cutting, joining ranks with other world central banks in a global rate cutting cycle.

As expected in our central case, the first rate cut of 25 basis points took place; we expect an additional cut later in the year. As a policy objective, we see this initial cut as an insurance policy for sustaining U.S. growth.

Short Term Market Overview

In the second quarter, the short end of the bond

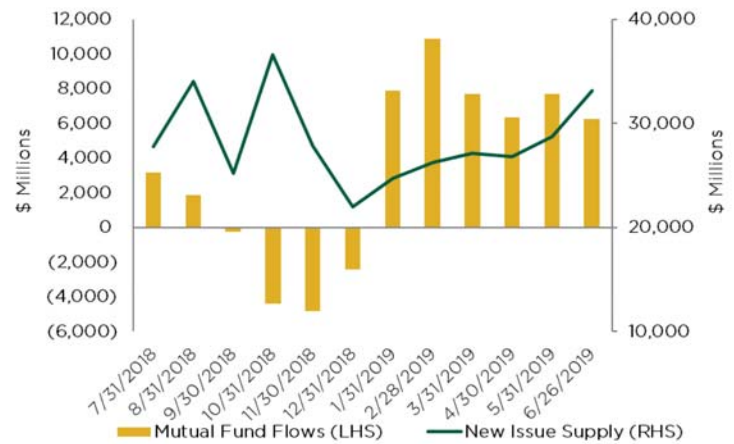
market reacted strongly to an erosion in economic sentiment, reversing the stability witnessed in the first quarter and resulting in a significant decline in yields. The 2-year tenor of the U.S. Treasury curve saw the most significant decrease in rates with yields declining ~50 basis points over the quarter. With this rally further increasing the inversion of the Treasury curve from 6 months to 3 years (our maximum maturity for this strategy), relative value of 2-6 month bills improved and we utilized this component of the market to improve the liquidity profile of the portfolios. As a complement to this ultra-short treasury exposure, we found opportunity in high credit quality corporate bonds in the 2-3 year range, slightly extending duration and increasing overall credit exposure.

Municipal Market Overview

The municipal market continued to exhibit solid performance and positive total returns for the second quarter. A global slowdown, weaker domestic economic data, fears of a U.S. recession and heightened U.S.-China trade tensions contributed to declining yields. U.S. Treasury rates plunged as investors believed the Federal Reserve would lower short-term interest rates. In addition, according to Fed Fund Futures (Source: Bloomberg), the dealer community started to price in future rate cuts starting at July's FOMC meeting.

Besides weaker macroeconomic data, the decline in municipal yields was driven by strong technicals. A combination of positive fund flows and moderate new issue supply was particularly supportive to the asset class. According to the Bond Buyer, issuance for the second quarter was $88.7 billion, an 11% decrease than the same period last year when issuers sold $100 billion in new issue debt. As reported by the Investment Company Institute (ICI), retail investors continued to pour money into mutual funds. ICI reported second quarter inflows of approximately $20.3 billion, thus bringing year-to-date inflows to all municipal bond funds to a record $46.8 billion (Chart 2).

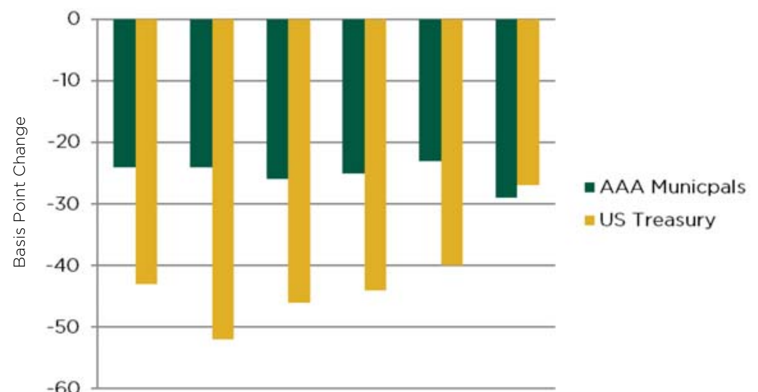
Chart 2: Municipal Mutual Fund Flows vs. New Issue Supply



Source: Bond Buyer, Investment Company Institute

The drop in U.S. Treasury yields spilled over into the municipal market with AAA-rated yields falling 23 to 29 basis points. Along with strong municipal market technicals and global growth concerns, the decline in municipal yields did not keep pace with their taxable counterpart (Chart 3).

Chart 3: Municipal and Treasury Rate Changes 2Q19



Source: Bloomberg

The sector's underperformance, relative to U.S. Treasuries, triggered a spike in ratios. Ratios, which are AAA-municipal yields divided by comparative U.S. Treasury yields, increased in 2, 5 and 10-year

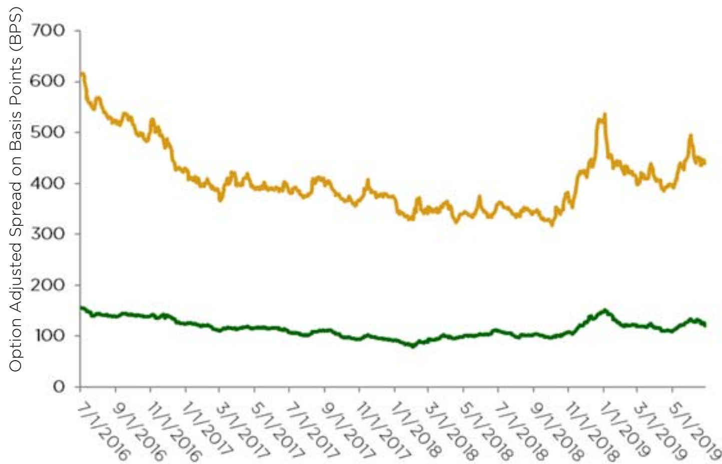
maturities by 4 to 5 percentage points, bringing valuation more in line or cheaper than their year-to-date averages relative to the treasury market.

Corporate Market Overview

The corporate market experienced some spread volatility during the quarter but by the end of the quarter spreads were largely unchanged and returns were positive. The lowest rated high yield corporates performed worst, but managed to eke out a positive return as CCC-C rated corporates were the lowest performing ratings cohort, the ICE BofAML CCC-C rated Index earning only 0.65% in the quarter. Only CCC-C and B rated at 2.42% earned less than the US Government index which turned in 3.04%. The theme of the quarter seemed to be "safe yield" as all investment grade corporates returned 4.35%, better than either government securities or high yield.

Early in the quarter spreads tightened on economic optimism but reversed in early May (Chart 4) as President Trump's May 5 tweet regarding increasing tariffs on China dulled the optimism.

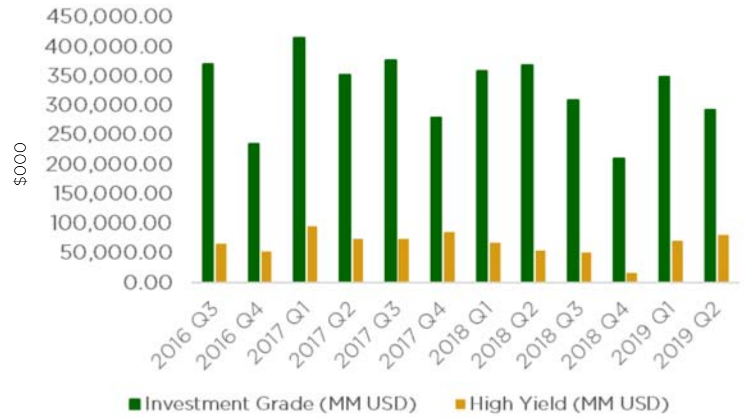
Chart 4: Corporate Credit Spreads



Source: Bloomberg

Spread widening in the quarter occurred in healthcare and drug company names, as concerns over legislative actions affecting those businesses heightened as well. By the end of the quarter, the market was trading as if a Fed funds rate cut of at least 25 basis points was fait accompli, and both the fall in the Treasury yield curve and narrowing spreads boosted returns.

Chart 5: Corporate Bond Supply



Source: Bloomberg

Supply technicals were modestly positive for investment grade and a modest headwind for high yield. All the issuance was generally quite well received as Investment grade issuance was slightly lower than the first quarter but a still robust $293 billion was issued. In the high yield space $81.7 billion was issued which was the busiest quarter for high yield issuance since the fourth quarter of 2017.

The supply was readily absorbed by the market as investors piled into the market, and with the German 10 year bond ending the quarter at negative 33 basis points (-0.33) foreign investors had significant incentive to move into U.S. fixed income to get any yield. Notable investment grade issuers included IBM bringing $20 billion to purchase Red Hat Software and Saudi Aramco bringing $12 billion in the Kingdom's first ever U.S. Dollar borrowing. The high yield market liked Sirius XM's tune and accommodated a $2.75 billion financing to purchase radio streaming company Pandora Radio.

Preferred securities performed well, earning 3.02%. The sector benefitted from still strong bank earnings and the fall in treasury yields. Pricing performance was somewhat limited as callability is beginning to come into play, and with rates falling we would expect major preferred issuers to begin writing new deals at lower coupon levels, possibly at or below the 5% coupon.

External Manager Investment Review

LOUISA M. IVES

Managing Director & Head of Manager Research

Market Overview

The second quarter of 2019 continued the upward trajectory of the first quarter, though at a bit of a more measured pace. Within the quarter, however, were some fairly significant swings in sentiment and performance. While U.S. markets closed at a high at the end of April, May proved to be far more challenging, as tariff and global growth slowdown fears rattled investors; the S&P 500 fell 7% in May alone. In June, however, trade fears moved to the back burner and the Fed's dovish stance helped markets reverse May's pullback and add some incremental performance to most indices. Collectively, the S&P 500 advanced during the quarter 4.30%, and the Nasdaq gained 3.6%. International markets lagged the U.S. a bit, but largely demonstrated a solid quarter. The MSCI All Country World Index advanced 3.6%, the MSCI All Country World ex-U.S. advanced 3.0% and the MSCI EAFE advancing 3.7%. Emerging markets did not fare as well in the quarter, with the MSCI Emerging Markets Index advancing just 0.6%. Broadly, growth investing continued to trump value, continuation of a long term theme in the markets.

While it is clear that trade and action/inaction by the Federal Reserve will continue to dominate headlines and affect near term market price action, rising tensions with Iran will be an important factor to watch carefully. There are signs that the U.S. economy is slowing, and the Fed has recently followed through on its well-advertised intention to shift to a more accommodative stance, lowering rates 25 bps. The language out of the Fed continues to indicate a willingness to make future rate cuts, and they remain acutely focused on the implications of the slowdown in global growth and it's effect on the U.S. economy.

More broadly, as global growth falters outside of the U.S., monetary policies are decidedly accommodative and should prove supportive in the form of stimulative efforts out of Europe (the ECB), China, etc. While we may see periods of volatility ahead, particularly given geopolitical risks, low inflation and low interest rates should continue to favor equity markets. As we look across the globe, we remain most constructive on the U.S., and continue to lean heavily in favor of actively managed, high quality portfolios.

In credit markets, the yield on the 10-year Treasury closed the quarter at 2.01%.

With 10-year yields hovering near 2%, the 2-10 year slope has been flirting with inversion, though it has steepened a bit since December lows. With rates as low as they are, we remain cautious on credit in general, acutely aware of the significant pools of capital chasing yield. As with equities, we stress the importance of favoring experienced, more conservative partners in the credit space to help navigate these markets.

Second Quarter Performance

The performance of our recommended managers in the second quarter of 2019 was solid across all strategies. At the midyear mark, the majority of the hedge funds with whom we partner have kept pace with their relative benchmarks, no small feat given an average 60% net exposure. Our long only managers,

too, have had nice performance, with strong outperformance coming from those managers with focused growth portfolios. Our international and global managers have done very well year to date, particularly given the more challenging economic backdrop that continues abroad. The returns generated by our credit managers have been more muted, given the challenging rate backdrop, but we remain impressed by their ability to generate solid, steady returns.

As we mentioned at the close of the first quarter, we are now in an investing backdrop that is more fully valued and tempers our return expectations for the coming months ahead. We would not be surprised by a pause or a pullback in markets between now and the end of the year, but as long term investors would seek to capitalize on any opportunities as they arise.

As always, we are grateful for your support. If you have any questions, please don't hesitate to reach out.

Richard L. Chilton, Jr. is the founder, Chairman and Chief Investment Officer of Chilton Trust Company, which in April 2012 was the first company in eight years to be awarded a trust charter in Florida. Mr. Chilton also serves as the Chairman, CEO and Chief Investment Officer – Equities of Chilton Investment Services and is the founder, Chairman, CEO and Chief Investment Officer of Chilton Investment Company.

Since founding Chilton Investment Company in 1992, Mr. Chilton has built a team of investment professionals focused on building wealth in favorable markets and preserving capital in declining markets. Under Mr. Chilton's leadership, Chilton Investment Company has developed an investment approach committed to fundamental, bottom-up stock selection and disciplined portfolio management.

Prior to forming Chilton Investment Company, Mr. Chilton was a managing director of Allen Value Incorporated and a vice president and equity portfolio manager at Alliance Capital Management Corporation. Mr. Chilton began his career in the Mergers and Acquisitions group at Merrill Lynch and Company.

Mr. Chilton is a trustee of The Metropolitan Museum of Art and a trustee of the Classic American Homes Preservation Trust, both located in New York.

Jennifer L. Foster is an Executive Vice President, Co-Chief Investment Officer & Portfolio Manager– Equities and is an equity specialist who has worked at Chilton Investment Company for over 20 years. Prior to taking on her role as Portfolio Manager in September 2012, Ms. Foster served as Chilton Investment Company's Director of Research for seven years. She also serves on the Chilton Investment Company Risk Management Committee, Board of Directors, and Executive Board. Preceding her tenure as Director of Research, Ms. Foster served for seven years as an equity analyst at Chilton covering the Software and Technology sectors.

Before joining Chilton, Ms. Foster worked at GE Capital as a financial analyst in several divisions of the company including commercial finance, commercial real estate, equipment leasing and corporate planning. Ms. Foster graduated summa cum laude with a B.A. in English from Boston College and earned an M.B.A. with distinction from Harvard Business School. She is a current trustee of St. Luke's School and the Calvin Coolidge Presidential Foundation.

Timothy W.A. Horan is an Executive Vice President & Chief Investment Officer – Fixed Income. With over 30 years of experience, Mr. Horan is a specialist in fixed income investing, ranging from municipal and US taxable securities to international bonds and currencies. He leads a team of nine professionals managing client assets across a variety of strategies including intermediate liquidity, tax-advantaged, taxable, international and global.

Prior to joining Chilton Trust, Mr. Horan was a Managing Director at Morgan Stanley Smith Barney and served as MSSB's Chief Investment Officer of Fixed Income Investment Advisers, a division of MSSB, providing customized portfolio management to ultra-high net worth private clients, charities, endowments, foundations, and family offices, primarily in North America, the Caribbean and Latin America. Earlier, Mr. Horan led Morgan Stanley's Private Wealth Management Fixed Income business in London serving European, Middle Eastern and Swiss private bank clients. Mr. Horan also served on the Morgan Stanley Global Asset Allocation Committee. Before joining Morgan Stanley, Mr. Horan was Director of International Fixed Income at Lord Abbett & Co. He also held senior management positions in fixed income and foreign exchange portfolio management at Credit Suisse, Aubrey G. Lanston & Company, Inc. and Bankers Trust. At Bankers Trust, he helped pioneer the fixed income risk management frameworks. Mr. Horan began his career at the Federal Reserve. During the Volcker years, he was an Economist in the Sovereign Debt Unit at the New York Fed, working on the debt restructuring of Brazil, Mexico and Argentina. Following the Plaza Accord, he also served as a foreign exchange trader for the Federal Reserve Bank of New York. Mr. Horan earned an AB with honors in Economics and History from the University of Pennsylvania, Wharton-Sloan Program. He was an Andrew Mutch Scholar in Economics and Politics at the University of Edinburgh and holds a post graduate law degree from the University of Cambridge, where he was a Thouron Scholar.

Louisa M. Ives is a Managing Director & Head of Manager Research. Ms. Ives is responsible for external manager selection and due diligence for Chilton clients and is also a member of the Executive and Investment Committees at Chilton Trust. Prior to joining Chilton, Ms. Ives was a Managing Director at Chilton Investment Company, where she was a research analyst covering the financial services sector. She also served on the company's Board of Directors. Prior to joining Chilton, she worked at Coopers & Lybrand Consulting Group, reporting directly to the CEO, and began her career at Chemical Bank in their Middle Market Lending Group. Ms. Ives graduated cum laude from St. Lawrence University with a B.A. in English Literature and earned an M.B.A from Harvard Business School.

Ms. Ives serves on the boards of The First National Bank of Long Island, the North Haven, ME Casino (Yacht Club), The Project Y Theatre Company, and on the Investment Committee of Vinalhaven, ME Land Trust.

Pepper Anderson is a President & Chief Executive Officer. Pepper Anderson is President and Chief Executive Officer of Chilton Trust, with nearly three decades of experience in financial services and wealth management. Prior to joining Chilton, Ms. Anderson spent more than 20 years with J.P. Morgan Private Bank, where she most recently served as Managing Director and Market Manager for Connecticut and Westchester County, NY. During her tenure at J.P. Morgan, Ms. Anderson developed a deep understanding of both technical investing and private client relationship management, holding roles of increasing responsibility across a diverse range of businesses, including U.S. Head of Discretionary Fixed Income, Head of the Private Bank's Fiduciary Investor Group, and Investment Team Lead for High Net Worth and Fiduciary. After obtaining her B.A. degree from Tulane University, Pepper's successful foray into the financial world began in equity trading at Bear Stearns & Co. She then held roles in fixed income portfolio management at Meredith, Martin & Kaye and the Union Bank of Switzerland.

Pepper serves on the board of the Greenwich YWCA, as a committee chair for Impact Fairfield County and enjoys additional volunteer opportunities with her church and children's schools.

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