

Third Quarter 2023

Quarterly Commentary



Introduction

Pepper Anderson – President & Chief Executive Officer

While not over yet, 2023 has already been a year of immense change. From the evolving economic backdrop to the complicated domestic and global political landscape, market participants are left struggling to read the tea leaves.

As you read our commentary this quarter, you will note a cautionary tone across all asset classes, but also some emerging optimism in areas where we see value. While interest rates may not have peaked, waiting has been made significantly easier by cash and short-term investments being available at multi-year high yields. Despite the current dispersion within the stock market, we continue to find enhanced value in being invested in companies rather than indices and throughout this year we have been content to hold larger than usual cash balances as we wait for attractive investment opportunities.

The recent market pullback that occurred broadly in the third quarter has created opportunities for nimble investors to restructure portfolios and deploy capital. As these opportunities incrementally pull us out of cash, we are mindful that the road ahead is likely to remain bumpy and we remain focused on ensuring that appropriate cash reserves remain in place to meet our clients' needs. As challenging as market cycles like these can be, they reinforce Chilton Trust's mission and ethos. We remain committed to collaborating with our clients and supporting the realization of every family's specific goals. We recognize that this is a personal endeavor and look forward to speaking directly with each of you as we end the year. As always, we thank you for your continued confidence.

Market Overview

Concerns Crystalize but Optimism Remains

The third quarter of 2023 reversed the gains experienced in equity markets during the first and second quarters of the year, as investors grappled with the notion of “higher for longer” interest rates, political dysfunction in the U.S. and continued broader geopolitical concerns. Most of the damage took place in the month of September as global markets retreated almost in unison regardless of asset class, with the exception of energy, as oil prices remained strong.

Throughout the quarter, U.S. rates continued to climb. The 5yr, 10yr and 30yr US Treasuries all set highs not seen in sixteen years since the Great Financial Crisis. As the Fed continued to advocate for rates to be “higher for longer” and vowed to keep its tightening bias to combat inflation, rates continued their upward trajectory. Markets are bracing for one more additional hike in 2023 and then are expecting the Fed to pause to reassess the rate of inflation. The US consumer is showing signs of deterioration with increasing debt balances and lower savings. Additionally, the market continues to digest potential government shutdowns and a more stressed geopolitical environment.



Richard Lockwood Chilton, Jr.

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Equities

Timothy W. A. Horan

Executive Vice President & Chief
Investment Officer: Fixed Income

Jennifer L. Foster

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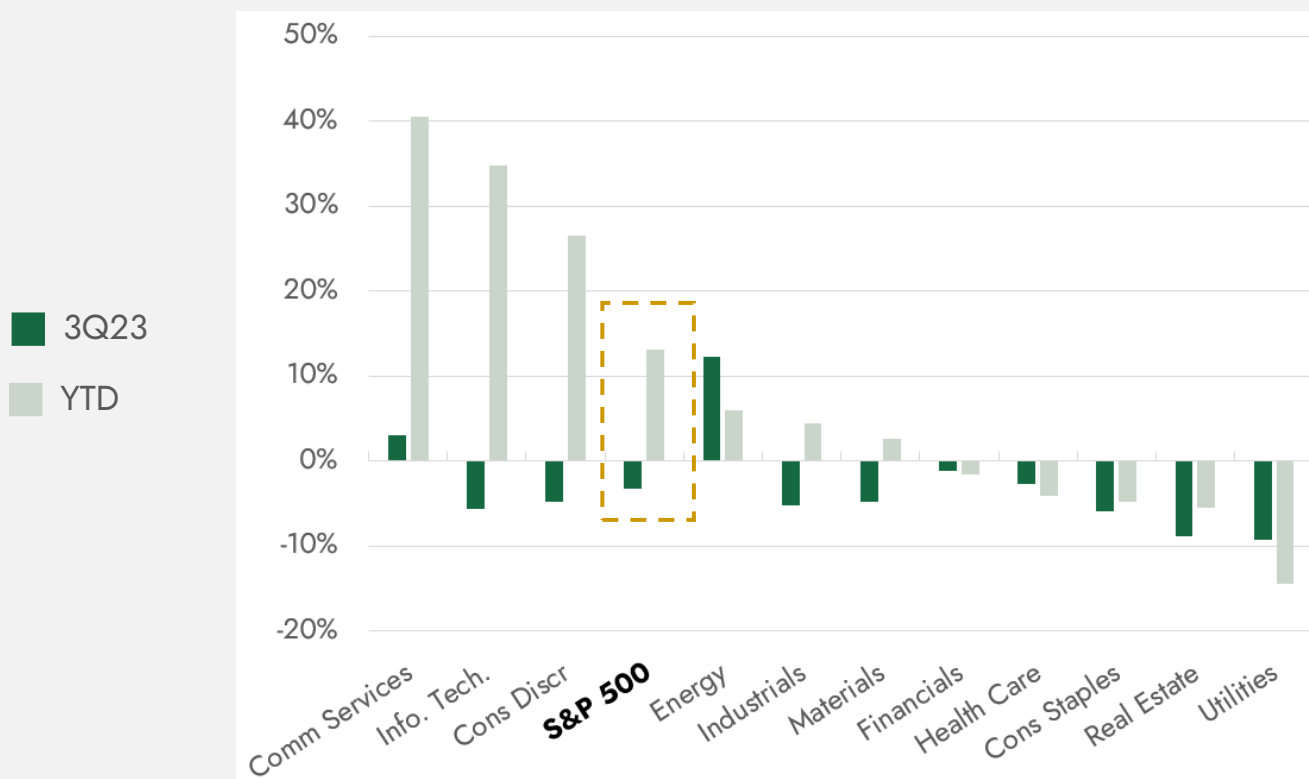
Equity Markets

This quarter, the equity market finally woke up to the many worries that have been swirling around for a while but were ignored by the enthusiasm of the Magnificent Seven (a frequently used euphemism for the largest of mega tech). Investors gained solace in the declining core CPI numbers and seemingly overlooked the recent increase in interest rates, oil prices and the firmness of the jobs market – until the music stopped.

In the U.S., the S&P 500 fell -3.3%, the Nasdaq fell -3.9%, and the Russell 2000 fell -5.1%. Markets abroad also had a challenging quarter, with the MSCI All Country World ex-U.S. falling -3.7% and MSCI Emerging Markets falling -2.8% in the third quarter. Year-to-date returns across the globe remain positive given the surge in performance witnessed during the first two quarters of the year; the S&P 500 is up +13.1%, the Nasdaq has returned +27.1%, and the MSCI All Country World ex-U.S. has returned +5.8% through the end of the third quarter. As the below graphic demonstrates, the challenging third quarter impacted almost every sector, with energy serving as a clear outlier.

Year-to-date, however, market performance continues to be dominated by communication services and technology names, as the significant gains made earlier this year by a relatively narrow group of tech names continue to dominate market performance.

S&P 500 Performance by Sector



Fixed Income Markets

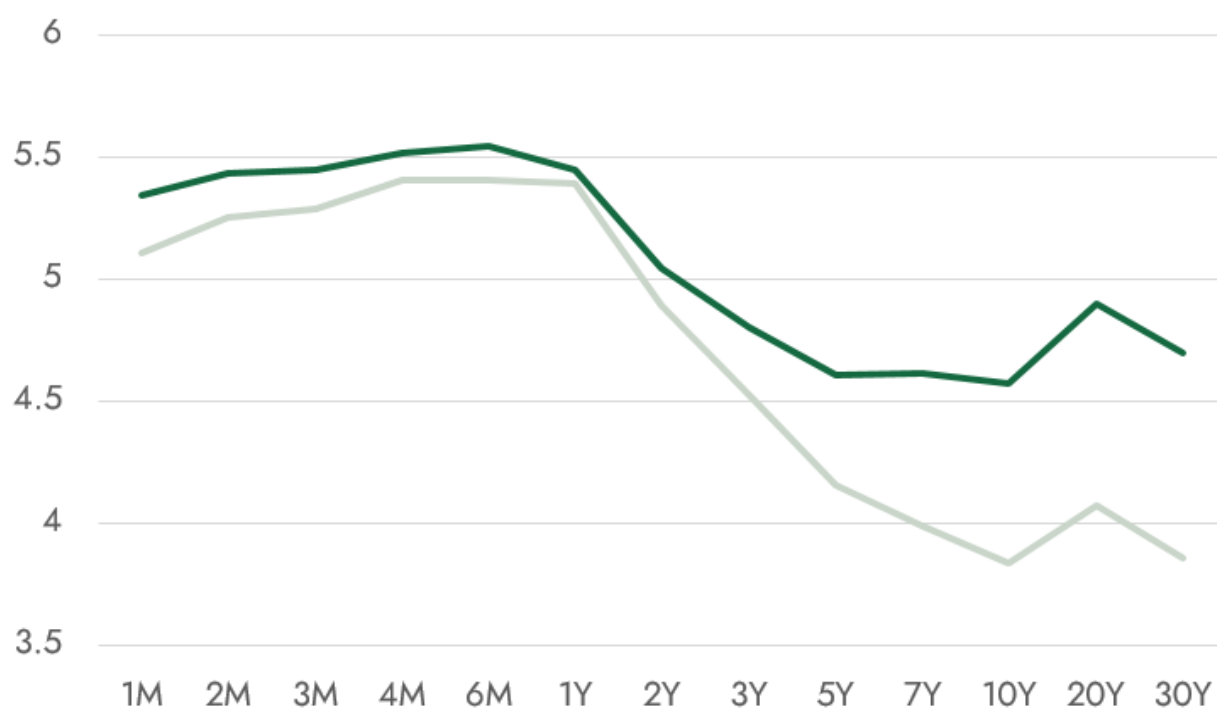
The third quarter of 2023 marked another historic period for fixed income markets as witnessed by further downward price action and yields on US Treasuries reaching multi-year highs. The Federal Reserve only raised the Fed Funds effective rate 25 basis points at its July meeting, but the hawkish tone and the underlying strength in economic data releases contributed to an overall re-pricing throughout the third quarter. The most significant movement was witnessed in mid-to-late September as the Fed reiterated its “higher for longer” message that the market had — throughout much of the year — refused to accept.

The longer end of the curve sustained the biggest repricing in an almost classic “buyer’s strike” fashion. Concerns about the rising interest rate expense to be paid by the U.S. Treasury, a pending government shutdown, and the extreme political gridlock in Congress —all weighed heavily on markets.

While the repricing impacted across the U.S. Treasury Yield curve, the U.S. Treasury 10-year reached a high yield of 4.75% — a level not seen since 2007 — amounting to an increase of almost 75 basis points quarter-over-quarter.

Bear Flattening of the UST Yield Curve in Q3

6/30/2023
9/29/2023



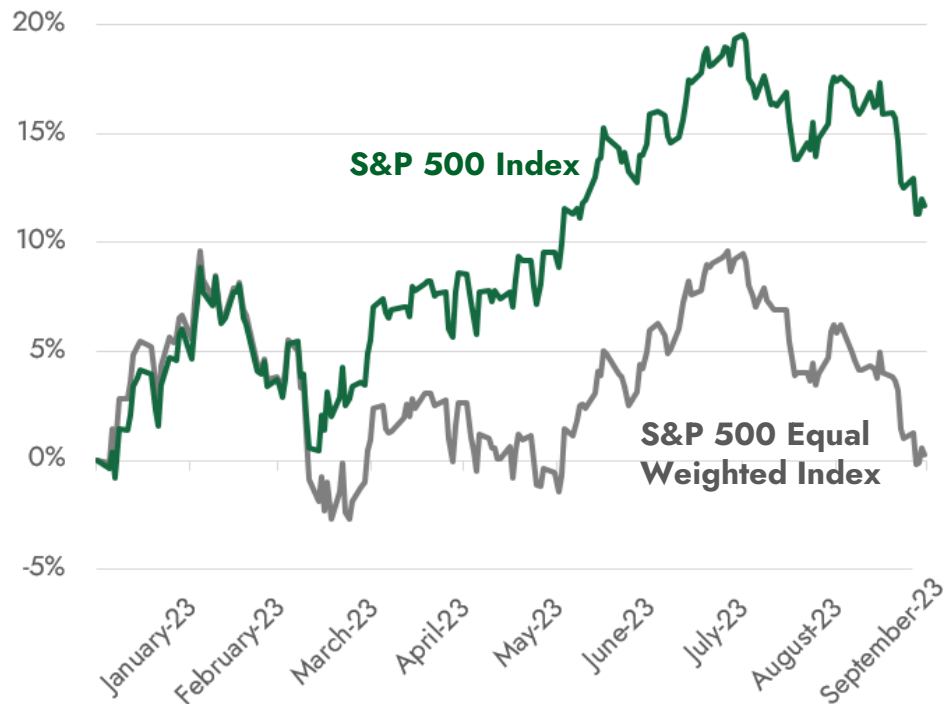
Our Portfolios

Equities: Navigating the S&P Mirage

In today's stock market, action corrections are swift and painful; this quarter was no exception. In fact, it highlighted, to a greater degree, an indicator that we have been watching for a while, which is the historic dispersion between the S&P 500 index and the S&P 500 equal weight index.

History is full of stories of people lost in the desert, trekking for days without food and water only to stumble upon what they believe to be an oasis containing both. However, this mirage exists only in their minds, as it is still a vast wasteland of sand. This analogy is similar to the market this year and important to keep in mind. Investors look at the performance of the S&P 500 and say, "The market is having a great year, it is up by 12-15%," but it is all a mirage. The S&P 500 equal weight index turned negative for the year in the first week of October, even including dividends. The underlying carnage has been swift and severe. However, when examining the implications of this, one can make a bullish case as many companies are performing exceedingly well, even in a difficult environment, and selling at very attractive valuations.

We expect many of our portfolio companies to perform well in the future, despite any struggles they may have faced this quarter, due to their strong fundamentals. Although the market has been impacted by a rapid spike in interest rates, this is not a direct issue for our high-quality businesses, as they typically operate without the need for large amounts of debt. Their earnings and, equally important, cash flows have increased or held steady, enabling them to increase shareholder returns through high dividends and buybacks.



Notes: Performance data reflects % change for period of Jan 1 – September 30, 2023
Source: Bloomberg

The higher level of interest rates has continued to affect P/E multiples across the market, but many of our businesses are trading at or below their ten-year average multiples. In fact, the S&P 500 equal weight P/E multiple is currently at 15x, which isn't excessive given inflation is coming down dramatically.



Portfolio Spotlight: IBM

IBM has been underway with an impressive transformation, which we believe positions the company for stable organic growth in the future stemming nearly a decade of revenue decline. The company has always screened as a high-quality potential investment, but the worrisome lack of organic growth kept us cautious for much of the last decade.

The transformation started with the acquisitions of Red Hat in 2019 and has been impressively executed by CEO Arvind Krishna, who was named CEO in 2020 and is the first technologist to be at the helm of IBM. As the architect of the Red Hat deal, Krishna has led the repositioning of IBM's current portfolio of businesses to focus on two promising opportunity sets: Hybrid-Cloud and AI.

Though IBM has long been known as a hardware company, it has seen hardware revenues diminish for years as computer architecture changes reduced mainframe workloads. Our research indicates that IBM's mainframe revenue is now largely stable through a hardware cycle due to the mission critical nature of existing mainframe workflows (e.g., fraud detection, airline scheduling) and the agility afforded by IBM's new hybrid-cloud products.

The exciting part of the story is the other parts of IBM's business. 80% of IBM's operating earnings now come from software and services, which are growing in the mid-to-high single digits. Because of the better durability and cash flow dynamics of these businesses, they usually warrant a higher multiple than hardware. IBM's stock has re-rated off the lows as IBM has steadily executed its new strategy, but with a current 14x P/E and a ~4.8% dividend yield, we believe there is more to go driven by further success in software and services.

The company just launched watsonx, a GenAI software platform which will help enterprises deploy GenAI. IBM has a 20+ year learning legacy with Watson, which gives them credibility in this important emerging technology. In addition, they have developed this product to address key pain points of GenAI, namely data security, accuracy of output, ease of implementation, and governance. IBM's trusted position within enterprise computing as well as its vast consulting business positions the company well to showcase its AI approach to technology decision makers. We believe watsonx could become a "killer app" in the age of AI.

IBM has a clean balance sheet, a fully funded pension, and ample free cash flow. We see all the important hallmarks of quality in this company, and we believe IBM offers investors a compelling risk/reward at current levels.

Putting It All Into Perspective

The sky over the stock market still has a number of black clouds, and to be fair maybe more than usual, but the valuation levels for the most beaten down quality names don't make sense relative to their fundamentals. These black clouds, and the negative effects on entire sub-sector valuations, have been severe and haven't distinguished between the good versus the poor when it comes to fundamentals.

Examples of this can be seen in how China's slowing economy has adversely affected the performance of luxury stocks, how the increase in student loan payments has battered consumer stocks, and in the impending risk posed by weight loss drugs to damage consumer staples. How long will these black clouds remain? It is tough to say.

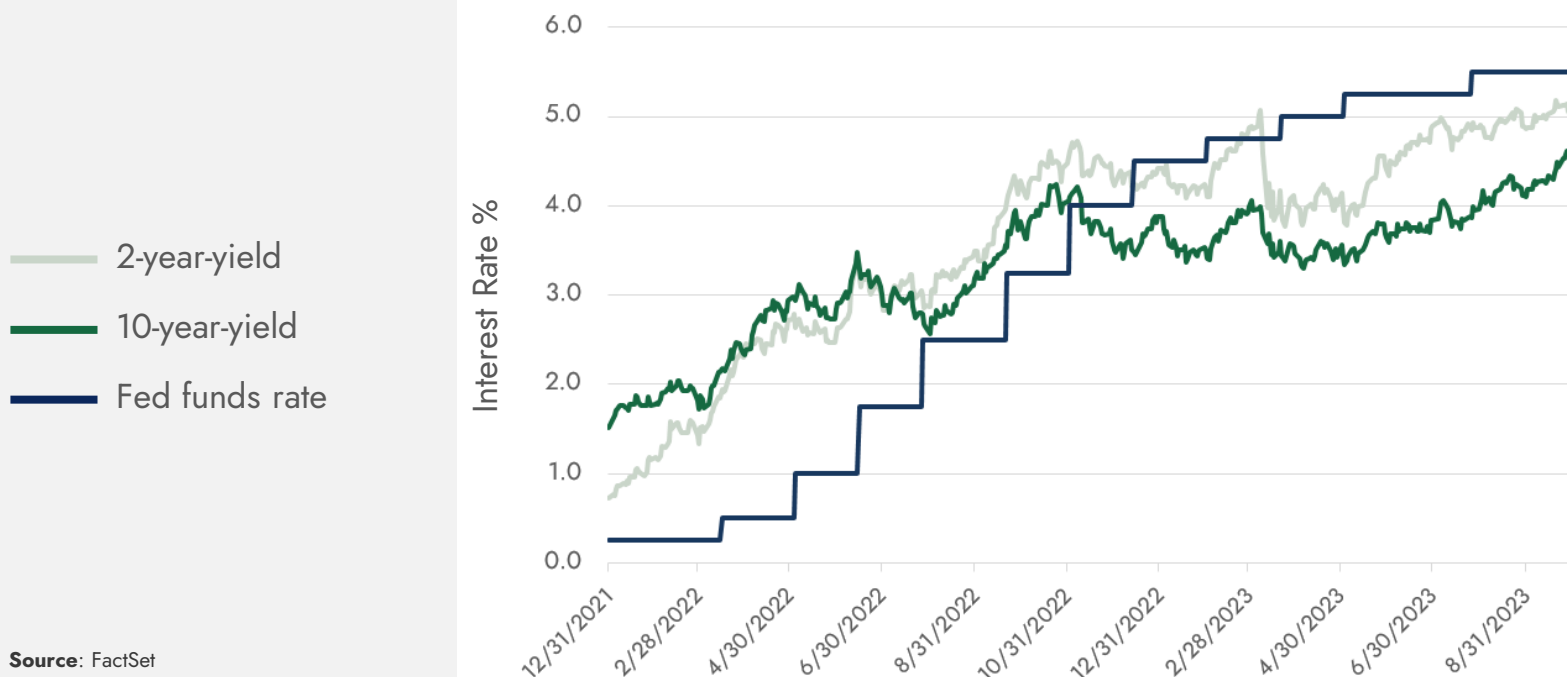
We do see the economy and sentiment in China eventually improving, although the region remains unattractive for direct investment. We believe the consumer has been extremely resilient and that without severe job losses, even if their spending dollars may shift, they will continue to spend. Lastly, we understand that while these weight loss drugs are a marvel, we believe it unlikely to have a permanent impact on consumer behavior due to obstacles preventing them from becoming mainstream, such as their high cost, uninsurable nature, and the fact that weight loss is only achieved while the drug is administered and often regained post-usage. Unfortunately, this type of "shoot first and ask questions later" mentality is all too typical to the volatile nature of Mr. Market. However, in our opinion as long-term investors, it has created buying opportunities in a number of very attractive businesses at good prices.

Our Portfolios

Fixed Income: Rising Rates, High Yields and a Very Hawkish Fed

Although U.S. government rates are at the highest level since 2007, U.S. corporations have been remarkably resilient. U.S. banks led the reporting season and the results were not as bad as feared. Generally, revenues, net interest income, and net charge offs came in better than analysts expected. Although bankruptcies are ticking up, only one out of every twenty S&P constituents are unprofitable. There are some positive themes driving investments, including the adaptation of artificial intelligence and the health benefits from the greater usage of GLP-1 medications. At the same time, the labor market remains resilient and U.S. manufacturing is benefiting from “re-shoring.”

As rates remain elevated, we have benefited from the shorter durations of our portfolios. As longer dated corporates cheapen, we will look to strategically rotate and extend durations. We view the current environment as an opportunity to position the portfolios with longer durations using quality corporate credits with elevated yields. We are using both the secondary market and the new issue market to build attractive portfolios that provide a durable yield for the next five-plus years. We view this current backdrop as an attractive investing environment that fixed income investors have not seen in quite some time and we are well positioned to take advantage of the current opportunity.



While the front-end did not see yields increase at the same magnitude, the 2 and 3-year U.S. Treasury tenors still reached multi-year highs within the third quarter. The 2-year U.S. Treasury yield reached a high of approximately 5.17% in late September having started the quarter at approximately 4.90%. This increase in yields, further out on the curve, and stability in the front end has weakened the severity of the inversion, with the inversion ending the quarter at -0.47% from -1.05% at the end of the second quarter.

With this backdrop, we are strategically making slight duration extensions and are focused on high quality issuers with a preference of high coupons. Yields remain attractive on corporate bonds but are mostly driven by the elevated U.S. Treasury yields. Corporate spreads have remained very stable, not reflecting any greater macro concerns leading us to focus on high quality names that are likely to be more durable in the event spreads begin to widen.

When adding corporate bonds to portfolios we are favorable on the new issue market, which had an active quarter and several deals offered both attractive coupons and traded at a discount.

Additionally, we continued to see value in the U.S. Treasury and agency market in this high interest rate environment. While the debate of soft versus hard landing is still widely argued, and several opinions have shifted throughout the quarter, we continue to look for value in quality issuers that will be durable through varying cycles.

At the same time, the municipal market continued to see volatility throughout the quarter as investors remained focused on inflation and expectations that rates would remain high for an extended period. Factors such as rising U.S. Treasuries yields and concerns of further Fed tightening contributed to higher yields across the municipal yield curve and negative total returns for the third quarter of 2023.

According to Bloomberg, yields on AAA-rated securities inside of 5 years increased an average of 75 basis points. Intermediate and long-dated securities closed the quarter at higher yields with rates rising 84 to 90 basis points. With this increase in rates across the curve, municipal absolute yields closed the quarter at or close to their highest of the year. Typically, tax-exempt securities outperform during market selloffs, but with the sharp move in U.S. Treasury yields investors continued to pull cash from mutual funds and remain on the sidelines as approximately \$7.3 billion from mutual funds were redeemed by retail investor per the Investment Company Institute.

Municipal and Treasury ratios widened 9 to 15 percentage points in the 1-to-10-year sector of the yield curve. The most significant adjustments occurred in the front-end of the yield curve, which was relatively rich at the end of the second quarter. With the recent increase in yields, we are now reaching more appropriate valuations versus U.S. Treasuries.

Our Portfolios

External Managers: Looking for the Green Shoots in Private Markets

Our external managers were not immune to the broad market challenges that characterized the third quarter. Our equity hedge funds generally outperformed, as hedges helped offset some of the downward pressure on long positions. Long only managers, both here and abroad, generally fell in line with their relative indices, regardless of style box. Importantly, performance from the underlying companies in our partner portfolios continues to be solid, underpinning strong conviction in company fundamentals. Our credit managers helped to buoy portfolios with better relative performance, providing some nice ballast to the drawdowns in equity markets. While the general consensus leans to a “higher for longer” rate environment, underwriting remains conservative with our credit managers, given the unknowns regarding a potential economic slowdown in 2024.

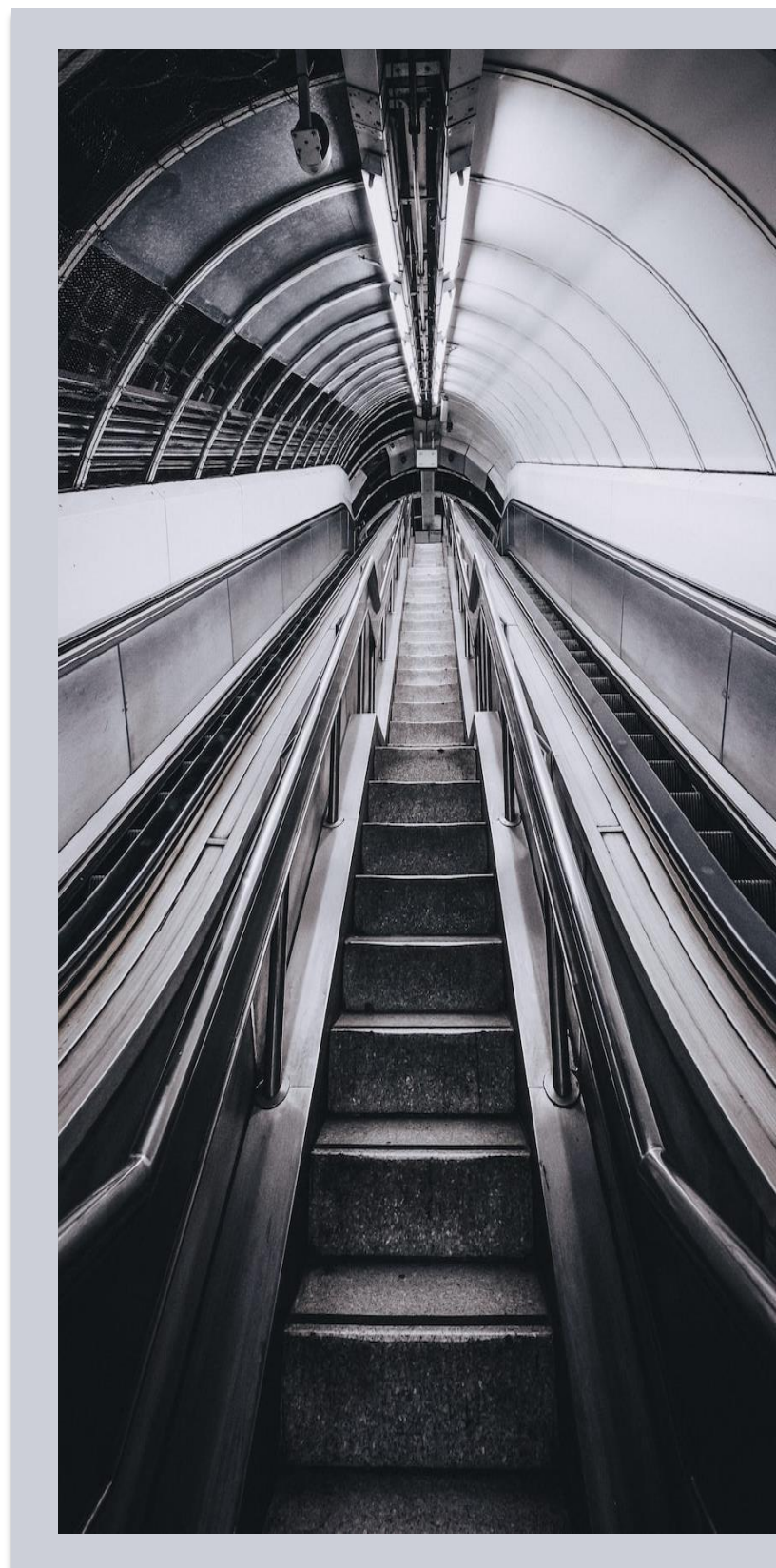
Private equity markets remained relatively subdued during the third quarter. We did see some “green shoots” of M&A and IPO activity, both of which would be a welcome change to private markets. We feel good about our existing privates exposure: companies continue to perform well, and balance sheets are generally well-fortified, minimizing the need for fresh capital. Valuations have come down and the “bid-ask spread” between what buyers will pay and where sellers will engage continues to compress, which should prove supportive for more transaction activity going forward. We are firm believers that the opportunity set for private markets, particularly in the middle market, is quite robust and the current environment is creating a compelling backdrop for future returns. That said, we continue to set the bar high for new allocations of capital, partnering very selectively with those managers with the experience, discipline and performance history that enables consistent outperformance and true alpha generation.



Our real estate exposure, expressed primarily through the Blackstone Real Estate Income Trust, had a solid quarter of positive performance, and they continue to cite strong tailwinds for their portfolio properties, particularly in the areas of data centers and student housing. Similarly, the Blackstone Private Credit Fund had a nice quarter of returns, and credit performance remains very strong within the portfolio. As questions abound about slowing in the overall economy, we have a strong appreciation for the conservative underwriting adhered to by the Blackstone real estate and credit teams. Both strategies remain good long-term holdings.

As we look out to the coming months ahead, uncertainty remains; worries about an economic slowdown, geopolitical strife which has been exacerbated by the recent conflict in Israel, and our own political dysfunction all are legitimate cause for concern. But reason for optimism abounds: interest rates are likely near their peak, valuations are more reasonable, and growth dynamics accentuated by AI and nearshoring of manufacturing all are supportive of solid company performance.

Our long-term mindset and focus on quality companies and opportunities shine a light on terrific opportunities to generate strong performance for portfolios over time.

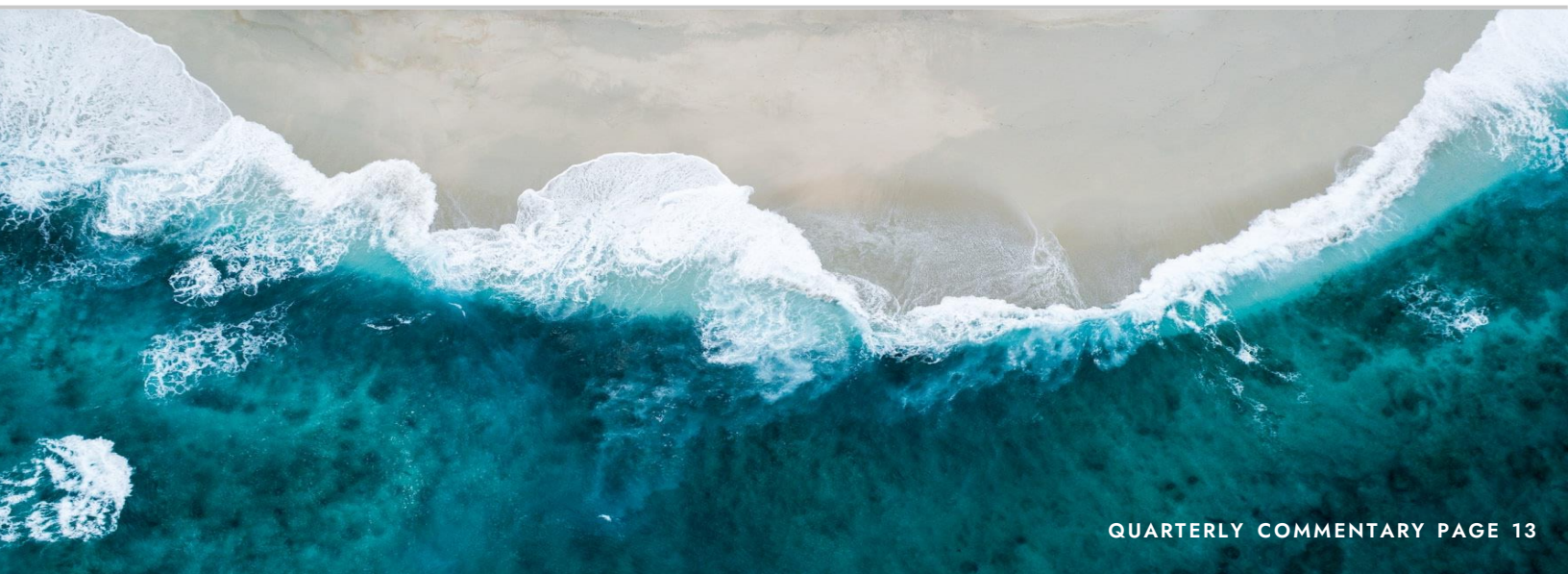


Our Outlook

Cautious Optimism Remains on the Horizon

As the U.S. equity markets come back to earth from the summer highs and endure the season of downside volatility, we are becoming more optimistic about forward returns from levels that are starting to look attractive. Although the S&P 500 Index ended the quarter with a still rich P/E multiple near 19x thanks to the continued dominance of the Magnificent Seven, the S&P Equal Weight Index – a broader measure of equity valuations – ended the quarter trading at ~15x, slightly lower than historic averages. Picking the bottom is a fool’s errand, but from these levels we have valuation support for equities for the first time this year. In addition, forward inflation expectations of the market as indicated by the “breakeven rate” show that bond investors are betting that inflation may soon be below 2.5% which could offer the Federal Reserve Bank a chance to pivot to a more dovish posture. We believe this circumstance, should it occur, would be a green light for equities.

To be sure, there are still plenty of reasons for caution in the current economic backdrop. As of this writing, we have witnessed the outbreak of unspeakable violence against Israel in an unprovoked terrorist attack by Hamas; the retaliation against Hamas is underway bringing severe humanitarian consequences. The violence being endured by civilians throughout the region is enormous, and our thoughts remain with all innocent people in harm’s way. What this conflict may mean for global growth which is already fragile is a real concern, and escalation remains a central risk. In addition, high levels of U.S. government debt with worrisome debt service increases on the horizon, alarming dysfunction in Congress, limited access to capital especially for small businesses, a small banking liquidity crunch, and elevated energy prices are all very legitimate concerns.



On the other side of the ledger, we have a largely successful war against inflation being waged by the Fed, structural growth drivers of nearshoring and AI/Infrastructure spending, as well as near full employment which has kept the economy chugging despite high interest rates through the year. Some investors worry that the rise in labor strikes and the demand for higher wages will cause wage inflation to persist and push inflation higher. We take comfort in the underpinnings of the labor market which has about 10% unionization today versus 25% in the 1970's. In addition, the use of digital technologies and robotics/automation are powerful antidotes to higher wages, and many leading companies are leaning into these powerful tools to effectively manage labor costs. The promise of higher levels of productivity as AI technologies are adopted keeps us keenly interested in monitoring this progress as well.

One thing we have learned from years of investing is not to underestimate the tremendous agility of the U.S. economy. Bearish economists suggested S&P Earnings this year could come in at \$180 given the historical impact of higher interest rates; instead, we are looking at expectations of approximately \$220 for Calendar Year End which is only a few months away.

It is true that consumer spending was more robust than feared this year and contributed

to the soft landing that we have thus far endured, but adept cost management has also been on display in an economy that is increasingly taking advantage of digital tools even as disinflationary pressures have crimped pricing power.

A large concern is that the Fed could remain hawkish for too long thus pushing the economy into a hard landing. The building fiscal pressure may diminish this possibility. The latest projections from the CBO reveal that 2023 fiscal year federal interest payments may be \$800B, up from \$500B in 2022. Tax receipts are coming in below earlier projections, contributing to budget pressure which is building. Of course, inflation needs to remain on a glide path lower to give the Fed room to pause, but with fiscal budget pressure building in an election year, the best hope to avert a budget crisis may be monetary policy.

For these reasons, we remain hopeful that 2024 brings some interest rate relief to the U.S. economy. We are finding many high-quality names with resilient businesses trading at attractive valuations and believe that an attractive buying opportunity may finally be soon at hand.

As always, we thank you for your continued confidence.

Our Team



RICHARD LOCKWOOD CHILTON, Jr. is the Founder, Chairman and Chief Investment Officer of Chilton Trust Company. Since founding Chilton Investment Company with his Flagship Strategy in 1992, Mr. Chilton has built a broad organization and a team of investment professionals focused on long term capital growth. The Chilton Flagship Strategy has generated impressive and consistent returns with moderate volatility since inception. In addition, in 2010 Mr. Chilton founded Chilton Trust Company which is a nationally chartered broad-based wealth management trust company focusing on services to high-net-worth individuals and families. Mr. Chilton is vice chairman of the Metropolitan Museum of Art, trustee emeritus of the Robin Hood Foundation, chairman emeritus of Greenwich Academy and a trustee of Classic American Homes Preservation Trust.



JENNIFER L. FOSTER is a Portfolio Manager and Co-Chief Investment Officer—Equities who has worked at Chilton for 24 years. Jennifer joined Chilton as an equity analyst and later became Director of Research and then Portfolio Manager. During her tenure at Chilton, Jennifer has served on the Risk Committee, the Executive Committee and the Board of Directors. Before Chilton, she worked at GE Capital as part of GE’s Financial Management Training program. Jennifer 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 currently serves as the chair of the Board of Trustees at St. Luke’s School in New Canaan, Ct, and as a trustee for the Mather Homestead Foundation in Darien, CT. Jennifer is married and has three children.



PEPPER ANDERSON is 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 business, 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 YMCA, as a committee chair for Impact Fairfield County and enjoys additional volunteer opportunities with her church and children’s schools.



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 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 MSSD, 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 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 Project Y Theatre Company, and on the Investment Committee of Vinalhaven, ME Land Trust.

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¹ Beta is sourced from Bloomberg and is a measure of a portfolio's volatility. Statistically, beta is the covariance of the portfolio in relation to the market. A beta of 1.00 implied perfect historical correlation of movement with the market. A higher beta manager will be more volatile than the market, whereas a lower beta manager will be less volatile. For example, a 1.10 beta portfolio has historically been 10% more volatile than the market.

² Sharpe Ratio at the security level is used purely for the comparison purposes during our portfolio construction process and does not in any form represent performance of the investment within the portfolio, Chilton has taken the position that Sharpe Ratio is not a performance figure, and to calculate this figure based on net basis would be misleading to investors.