Inflection Commentary

INFLECTION
Alternative Assets

Inflection Performance: October 2017

The Evolution Continues

Inflection Management was founded in 2010 to make our team's expertise managing alternative investments for high net worth clients available to more investors. Following the crisis of 2008, many people saw safety and good sense in devoting part of their portfolio to non-correlated assets designed to appreciate independently of the stock market, and ISOF provided a ready-made portfolio of best-of-breed international managers that aimed to stay one step ahead of what, at the time, were fast-moving macroeconomic cycles.

We called what we did 'The Evolution of Investing', because it avoided some of the classic risks of traditional long-only investing that had led to 2008 losses averaging 60% for stock market investors.

Fast forward to 2017, when the world's major economies have for the most part stabilized, we are again at stock market highs after a prolonged up cycle, and many experts are arguing that we are overdue for a correction. Once again, the equity portion of investors' portfolios has grown so big that it is in danger of introducing too much risk when the inevitable downturn occurs. This is in some ways a good problem to have, because years of strong equity gains has made it easy to exercise prudent investing discipline by allocating some of those gains to diversification.

It's also a rare second chance for investors who heedlessly marched headlong into 2008 to take a more thoughtful approach this time around. Although stock market investors who stayed invested through 2008 largely saw their portfolios recover in 2009, it's important to realize that there was an opportunity cost that they never actually recovered. Had they prudently diversified their portfolio ahead of 2008, they would not have suffered the drawdowns and would be considerably further ahead today.

And that's not just wishful thinking. Our previous fund's portfolio included John Paulson as a manager, whose 2008 sub-prime debt payday is now the stuff of legend (as dramatized in the movie The Big Short).

The solution we advocate now is the same one we advocated pre-2008: Allocate a portion of your wealth to a ready-made portfolio of alternative assets that do not take a substantial amount of market risk and invest in market-neutral, arbitrage, and relative value strategies that can produce returns whether the stock market goes up, down, or sideways. Ideally, such a portfolio would provide a fourth leg (along with an investor's primary business, real estate, and a stock portfolio), that would be uncorrelated to the other legs and thereby reduce the risk of the overall investment portfolio.

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We have spent over 20 years searching for managers who meet that criteria and then selecting which are most appropriate to the macroeconomic conditions at any given time. Rather than obsess over economic forecasts, our managers focus on the specifics of their markets and make the most of their trading edge, often through superior technology. We further strengthen those advantages by avoiding correlations between managers and being thoughtful about position sizing.

After 2 decades of sticking to our knitting, distilling our ultimate benefit to investors, perfecting our methodology (by learning from our mistakes), and persevering through vastly different economic environments (some of which famously were nicknamed TINA, as in There Is No Alternative to stocks), we believe the time is right for the next stage of our evolution. Accordingly, we are very pleased to announce the launch of our second fund, ISOF ULTRA starting in January 2018.

Like ISOF, ULTRA aims to produce consistent, high risk-adjusted returns, that are uncorrelated to nearly everything else likely to be in our investors' portfolios and balances allocations across 20-25 managers, each of whom maintains diversification in their own market niche. Whereas ISOF targets an average net return of 8-10% with 4-6% volatility and a low correlation to equity and bond indices, ISOF ULTRA applies an additional turn of leverage to the same underlying strategies and targets an average net return of 12-15% with 6-9% volatility and the same low correlation to equity and bond indices. Both funds utilize the same structure that may be advantageous to taxable investors.

ULTRA is a good fit for investors who like the inherently conservative approach of ISOF but are looking for a higher return. Investors interested in committing to ULTRA prior to its January launch may be eligible for preferred rates. Please contact jlee@inflectionmanagement.com for more information.

Contribution

ISOF Series A finished October up 1.32%, bringing our year to date return to 2.31%, and 7.45% over the trailing twelve months. Series B finished the month up 1.43%, bringing our year to date return to 2.83% and our trailing twelve month return to 8.08%. Our risk adjusted returns over the last 12 months have been high with a Sharpe ratio (return/risk) of 1.87.

Strategies in our Macro bucket performed well contributing 0.79% to our return for the month. Some of the contributing managers were: AEV, a CTA, up 3.55% and contributing 0.52% to the portfolio; AND, an energy strategy, up 5.06% and contributing 0.23%; and ALP, another CTA up 6.93% and contributing 0.21%.

The largest detractors for the month were ART, a volatility hedge, down -0.51% and detracting -0.08% from performance, and a handful of arbitrage and relative value managers that detracted -0.01 to -0.04 from performance.

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Though our 'Volatility Bucket' remains the worst performer for the year, we still view it as an important hedge against unforeseen events even during (or perhaps especially during) such serene markets as these. We believe ourselves quite fortunate to have sourced insurance policies that pay us to own them over the long term. Nevertheless, this year's highly anomalous all-time low volatility has, for the time being, been a drag on performance.

Strategy	# of Managers	Ending Weight	October	YTD
Arbitrage	5	28.07%	0.14%	1.43%
Relative Value	7	38.29%	0.32%	2.62%
Macro	3	15.01%	0.79%	0.78%
Volatility	2	6.09%	0.13%	-2.22%
CASH	-	12.54%	-0.06%	-0.26%

Sincerely,

The Inflection Team

The Inflection Strategic Opportunities Fund (ISOF) invests in a broad array of carefully selected hedge fund strategies in order to capitalize on dislocations and market opportunities. The Fund has a global mandate and focuses primarily on the Americas, Europe and Asia, providing access to the expertise of hedge fund managers in identifying what we believe are exceptional investment opportunities throughout the world. Some taxable investors may find that the Fund's option structure has significant tax benefits. Please refer to the attached Factsheet for additional information.

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Disclosure

ISOF performance presented are USD net returns after investment management and performance fees and is not an estimate of any specific investor's actual performance, which may be materially different from such performance depending on numerous factors. ISOF returns represent historical returns adjusted for the June 2015 performance fee structure change to the current fee structure. Information presented is believed to be correct and accurate at the time of production but may change due to circumstances beyond our control. Returns may be amended after these numbers have been reported due to repricing adjustments or receipt of more recent data, among other things, and will be reflected in the most recent document. Comparative returns selected are for informational purposes only and may or may not accurately represent the composition or potential performance of Inflection Strategic Opportunities Fund and may not be useful for comparison purposes. The HFRI Fund Weighted Composite Index is a global, equal-weighted index of over 2,000 single-manager hedge funds that report to HFR Database. Constituent funds report monthly net of all fees performance in US Dollars and have a minimum of $50 Million under management or a twelve (12) month track record of active performance. The HFRI Fund Weighted Composite Index does not include Funds of Hedge Funds. The S&P/TSX Composite Index (Net TR) is the Net Total Return version of the S&P/TSX Composite Index and is presented in Canadian Dollars. The Net Total Return Index Value is based on the aggregate, float quoted market value of the index constituents (Stock Price Index Value) plus their paid net dividends/distributions after applying a withholding tax at the national level. The Barclays Global Aggregate Bond Index is a market capitalization-weighted index denominated in US Dollars representing the universe of investment grade bonds available for purchase in the United States, securities underlying the index include Treasuries, Agencies, Mortgages, and Corporate Bonds. ISOF is an exempt market fund available to Canadian resident accredited investors in British Columbia, Alberta, Ontario, and Quebec and to a limited investor base in certain provinces under the Minimum Amount exemption. Investing involves risk. Please seek professional advice before making any investment. This is not an offer to purchase or sell securities. It is for information only. Please refer to the Confidential Information Memorandum for more detailed information