

THE STORY BEHIND LITMAN GREGORY'S NEW ALTERNATIVES FUND

An interview with Ken Gregory, Chief Investment Strategist and Founding Partner of Litman Gregory Asset Management, LLC and Litman Gregory Fund Advisors, LLC.

Why is this a good time to launch an alternatives fund?

We remain concerned about the global macro environment, specifically the deleveraging that must take place in the private sector in some countries, the public sector in some countries, and both sectors in other countries. A deleveraging headwind will challenge global growth, raise the risk of policy mistakes, and we think in general will continue to present investors with a high-risk environment for several years. There are negative scenarios which are not certain but still possible that we don't believe are fully priced into the equity markets. And, based on our analysis, we believe that the other major financial asset class -- investment-grade bonds -- is set for low nominal returns over the next three to five years given today's low yield level.

So with that backdrop, alternative strategies that offer relatively low correlation to stocks and bonds, relatively low risk, and the potential for alpha generation that can lead to above average risk-adjusted returns -- are appealing. The key though is in the execution. What is appealing in theory is not necessarily easy to implement in the real world, something we've seen over and over again with various financial products.

As we've searched through the alternatives world over the last few years we have found a few interesting funds but not many. So despite the fact that there is enormous demand, as evidenced by money flows, we believe the universe of funds generally represents a lot of mediocrity. We began thinking about creating our own fund because we wanted to offer a diversified, very high-quality alternatives option to our clients. We didn't believe it existed in the marketplace so we set out to see if we could do it better ourselves.

What is Litman Gregory's experience in alternative investing?

We've been investing in some alternative areas for clients of Litman Gregory Asset Management, our wealth management affiliate, for a long time. We started with private real estate investments back in 1988. Since then we've expanded into hedge funds¹ and, in a more limited way, into private equity. The hedge fund investments have mostly been in private funds, but we have invested in a couple of public funds.

Our hedge fund investments go back to 2003. We've invested in a couple of fund-of-funds for some of our clients. We also invested in a number of individual hedge funds in a private partnership we run, going back to 2003. We've been extremely pleased with our investment in these hedge funds and they informed our thinking about our strategy and manager selection for our fund. Two of the private funds we've owned are funds run by two of the managers to the Litman Gregory Masters Alternative Strategies Fund.

You mentioned that you want a “high-quality alternatives option for your clients.” What do you mean by that?

First, we wanted exceptionally skilled managers. In our view the manager quality in the public alternative funds world is not particularly impressive. Now there are some exceptions and, certainly, we have not researched every fund. In fact, funds are being launched so rapidly that the universe is experiencing truly enormous growth. But we believe that too many investors are placing their capital in alternatives funds just for the cachet of having an alternatives position. This makes no sense to us. In our view neither the average hedge fund nor the average alternative public fund has been compelling in terms of adding portfolio value. For example, we looked at Morningstar’s *Multialternative* category. There are about 70 funds in the category and the average net expense ratio is just over 2%. Most of the funds are new; there are just over 20 with a three-year record. But if you look back at the category performance you would have done better going with a basic 60%/40% bond/stock blend using the Barclays Aggregate Bond Index and the S&P 500 Index as proxies for bonds and stocks over the three- and five-year periods ended August 31 of this year. You would have had a materially higher return over these three and five year periods with comparable risk.ⁱⁱ Now you might say that’s just an average, but looking at the list of funds there are few that really looked compelling to us on a performance basis. For example, the largest fund in the category had over \$3 billion as of August 31—far larger than any other fund in the category. Its performance has been quite good relative to the average hedge fund-of-fund, but again, if we compare to simply what an investor could have done with traditional assets—meaning long positions in stocks and bonds such as the 60/40 blend using the same proxies—the fund did not add meaningfully in terms of risk control and trailed on a return basis for the three- and five-year periods ended 8/31/2011 and had a lower Sharpe Ratioⁱⁱⁱ over both time frames.^{iv} So our thinking was that if we launched a fund, we had to really believe that we had skilled managers running the money; managers who, based on our analysis, we believed were likely to add meaningful return alpha – meaning excess return relative to the risk they took.

Importantly, we wanted to accomplish that and do so with relatively low volatility^v and relatively low correlation^{vi} to stocks and bonds.

As far as specifics, our goals relative to a 60/40 bond/stock blend are less volatility, better down market performance, fewer negative 12-month losses, and higher returns over a market cycle. We believe we can achieve these objectives with relatively low correlation to the stock and bond markets.

Does the fund have volatility and correlation goals?

We would like to see annual volatility in the 4% to 8% range and believe this is a realistic goal. That’s about one-quarter to one-half the historical stock market volatility and potentially equal to double the volatility of the bond market.^{vii} We believe correlation with stocks of about 0.50 offers valuable diversification and we believe that is achievable on average, however, the fund’s correlation will vary over time and there could be periods where it is somewhat higher or lower.

Is this an “absolute return” fund?

Based on how the industry uses this term, the fund might be considered absolute return, but we actually think the absolute return label is misleading to investors. The reality is that pursuing return requires taking some risk. No investor is smart enough to always capture only the return side of the equation. Now in theory, proper portfolio structuring, skilled security selection, smart hedging, and risk controls can lead to alpha generation and strong risk-adjusted returns. But, as we saw in 2008, many, probably most, “absolute return” funds^{viii} suffered bigger losses compared to expectations, given that they tend to be marketed as able to deliver positive or near positive returns in all market environments. For example, HFRI has a diversified hedge fund of fund index. It represents portfolios of hedge funds that were hand-picked by firms that presumably have expertise in selecting well-run hedge funds. That index lost 21% in 2008. The Morningstar *Multialternative* category was down 20% in 2008. For our fund we are seeking decent solid returns and alpha, so we will have to take on some risk. Although there can be no guarantees and our opinion is based solely on our due diligence on the managers and the strategies we’ve employed for our fund, we are seeking to do better in a highly stressed 2008-type environment and believe that this is a realistic objective given our qualitative assessment of the managers’ investment processes and risk controls and on our quantitative historical performance evaluation of their strategies in recent extreme bear markets.

What is the basis for your expectations of fund performance?

They’re based on our qualitative and quantitative analysis. On the qualitative side, we think we know the managers very well. We’ve known Steven Romick since the early 1990s, done heavy due diligence on his strategy since then, and we’ve owned his private hedge fund for eight years. We started doing intensive due diligence on Jeffrey Gundlach in 2008. That year we invested in a private fund he ran at TCW. We are also invested in a private hedge fund he runs at DoubleLine. We’ve been more than happy with our investment in each of these funds. Our due diligence work on John Orrico and the Water Island team goes back to 2003. We started investing client money in their public fund last year. We’ve been pleased with how they execute their arbitrage strategy, which is basically intended to be a moderate return, low-volatility strategy. And our exposure to and investment with the Loomis Sayles fixed-income group goes back almost 20 years starting with Dan Fuss, whom we know well. Over the years we’ve gotten to know many members of the Loomis bond team including Matt Eagan. So we believe we understand each of the strategies well and what may affect their performance in different environments.

The second part of the answer is that each strategy has a performance history—some public and some private. As part of our research we’ve examined the numbers and looked at how the strategies correlated and how they would have performed if they had been part of a single portfolio. There was also a qualitative element to this analysis because some of the strategies that we looked at are slightly different in terms of objectives and risks than what we are asking the managers to run for this fund, and in some cases the fees were different. However, we did not believe that the differences would materially impact our risk analysis. The fact that we’ve had such severe bear markets over the last 10 years has been helpful in that we can see how these strategies performed in exceptionally stressed environments. Each of the managers has a very long record with their strategy we analyzed, with the exception of Loomis. In Loomis’ case, the strategy does have a record going back six years, which pre-

dates the financial crisis, but it is not nearly as long as the other three managers who all have records going back at least 10 years. However, the team is experienced, and Loomis has been around a long time. Some members of the Loomis team have been with the firm and worked with Dan Fuss going back as far as 14 years. Matt Eagan, one of the team members, also co-manages Loomis Sayles Bond with Dan Fuss. We looked at how these four managers did with their strategies combined into a single portfolio. We ran all the important numbers—standard deviation, downside standard deviation, correlations, Sharpe ratio, and obviously we looked at performance in various different return environments. Our findings were one important factor that encouraged us to move forward with this fund.

Our due diligence approach in alternatives is similar to what we do on the long-only side in that it is very thorough and requires that we have a clear understanding of the process, team, execution, and risk controls. We delve deep into the manager's thinking on individual positions and overall portfolio structure. And of course we want to know that the manager has had significant success running the strategy, and we want to understand what drove the success so we can assess whether that success has the potential to carry forward.

How did you pick the managers?

It was driven by what we are trying to accomplish with this fund. First, obviously we wanted highly skilled managers who we strongly believed have the ability to add significant alpha over time. We based our opinion on our qualitative analysis and our analysis of their track records. Important to us was the willingness to be opportunistic from a tactical standpoint – specifically a willingness to increase or reduce risk based on their assessment of risk/reward trade-offs. But we also wanted to create a fund that is not highly correlated with stocks and bonds, and that we believe would be relatively low risk compared to stocks and also on an absolute basis. Both of these objectives are very important. We didn't want a low-risk fund that wouldn't have the potential to generate much return or, conversely, a fund that would turn out to be too volatile.

With respect to risk management we sought to hire managers who met two criteria: First, they each would have a different investment approach and/or investment universe that collectively would result in a portfolio that we believed would not be highly correlated to the stock market and the bond market. Second, we were only interested in managers who we believed would be low risk by virtue of their investment approach or investment universe, and/or because of their risk mindset. So take Steven Romick's team at FPA, for example. Romick invests anywhere in the capital structure, so he buys bonds and stocks. He can short. He is global. And he is creative in looking at opportunities even if they are not easy to invest in. So for example, he invested in a private farm land partnership, which he believes is attractive on a long-term basis. In fact, one time I called him on his cell phone and he was doing due diligence and was actually about to get on a tractor. This investment might find its way into our portfolio. He's also done things like participate in a commercial real estate loan on a building backed by substantial equity. So Romick definitely will invest in assets that potentially expose his portfolio to risk. But he is also extremely risk averse. He is an absolute-value guy—he won't buy something because it is cheap relative to something else that might be unattractively priced; it has to be absolutely cheap. He hates to lose money and while he is willing to take on some short-term market volatility, he is strongly

averse to risking permanent loss of capital. So, for example, he's more than willing to sit on cash and be patient at times when he doesn't believe he is being paid enough to take on risk. He doesn't worry that this might lead him to give up some return in the short term. We've known Steven for years and invested with him in his hedge fund and his public fund. Based on our experiences and knowledge of his approach and risk-averse mindset we are confident that he takes an unusually risk-sensitive approach to investing in the areas he pursues.

The Water Island team falls into a different category. Their approach to various types of arbitrage plays is inherently a low-risk approach to investing since stock market risk is largely hedged away. It comes through in the numbers as evidenced by the HFRI Merger Arbitrage Index, which did lose 5% in 2008, but that was its worst year ever and equity indexes fared far worse with the S&P 500 down 37% for the year. In 2002, another bear market year, it was down less than 1% and in 2000 and 2001, also bear market years, it had a positive return. It also was positive in 1990, a down year for equities. Again, these results are not surprising since there is minimal stock market risk in this type of strategy.

Jeffrey Gundlach's DoubleLine portfolio has a lot of flexibility to pursue various segments in the fixed-income markets – ranging widely from his specialty in the mortgage area to other sectors such as emerging-markets bonds -- and he has a definite tactical element in his approach to running a portfolio. So there is the potential to take risk. But like Romick, Gundlach has an extremely risk-averse mindset. The same is true for the Loomis team and they have a mandate to target a low level of volatility ranging from 6% to 8%.

So the fund came together by virtue of our objectives and the fact that we have known and observed each of these investors in real time for years, have done an enormous amount of due diligence work on each, and have invested with each either through their public or private funds.

Since we've touched on risk, will the fund use leverage, which obviously can add to return but also to risk?

This is a public mutual fund, which means leverage can't exceed 33% of assets. So leverage levels will be quite moderate, not like the much heavier leverage levels found at times in some private hedge funds. However, several of the managers will use leverage. We expect leverage to be one of the tools they will use selectively to try to add alpha, by overweighting opportunities they consider to be compelling from a return and risk standpoint compared to the cost of borrowing.

Did you consider other managers for the fund?

We did look at others but for a number of reasons we chose these four. The primary reason, of course, is that we believe they are exceptional investors. We know them well, they bring different things to the table from a portfolio structure standpoint, and they have had success over the years. They are not unknowns to us or to the investment industry. Also, and this is important, each was very enthusiastic about being part of this fund and partnering with Litman Gregory. That is important to us because it gives us confidence that they will be working hard for our shareholders to deliver the maximum value

they are capable of, including taking advantage of the smaller asset base they will be running for this fund.

Why did you decide on multiple managers?

We believe that manager and strategy diversification is extremely important in the alternatives world. It allows for risk reduction due to diversification, and it helps to mitigate the risk of having too much with a single manager who makes a serious mistake, which can happen with any manager, no matter how skilled. We have great confidence in each of our managers but we have even more confidence in the overall fund largely because of the diversification.

Will you be adding managers in the future?

We expect to add managers as the fund grows. We like the idea of building in more manager diversification but we will only do so if we can find managers who meet our high standards and whom we can hire without hurting the fund's expense structure.

How did you decide to allocate the fund's assets to the managers?

Our starting point is to equally weight among the managers. Based on our qualitative work and also our examination of each manager's historical track record and their correlations with each other, we believe that an equal weighting would accomplish our risk, return, and diversification objectives for the fund very effectively. It is likely that much of the time the managers will be equally weighted. However, Jeremy DeGroot, Litman Gregory's Chief Investment Officer and this fund's portfolio manager, will also make tactical moves at times, and we give ourselves the leeway to be plus or minus 10% to any manager--so allocations could range from 15% to 35% of the fund's assets to each manager.

We will only overweight a manager if we believe that their investment universe is significantly more attractive than the others and we are confident in our ability to make that assessment. The thinking is that we believe an equal weight will be very effective, so we don't want to risk getting whipsawed by messing with something that we believe will work, unless we are extremely confident the move will add value. We have a long history of investing this way in our private client accounts where our core competence is valuation-based tactical asset allocation. It's a long-term value-driven approach. As it turns out, as we launch the fund we are making a 5% overweight to Gundlach's strategy because we believe his risk-integrated mortgage portfolio is very compelling now relative to other investment opportunities. As an aside, we made a tactical move in our client portfolios in late September 2008 into non-agency mortgages for clients who had account sizes large enough to own a private fund Gundlach ran when he was at TCW. That has turned out to be one of the best asset plays we could have possibly pursued at that time for our clients. Remember that was right in the middle of the financial meltdown, shortly after Lehman went under. So that is an example of seeing an opportunity in a particular strategy.

You've capped the expenses at 1.49% for the institutional share class, a relatively low number in the alternative world. How were you able to do that?

In the mutual fund world 1.49% may not seem low but it is low in the alternatives world. When we were thinking about creating this fund we felt it was important to keep expenses under 2%, but we were somewhat uncomfortable with that level even though that is around the average for public alternatives funds^{ix}. However, we felt that with the right managers, the fund could work at that fee level. As it turned out, we were able to negotiate what we believe are very good fees with our managers which translated into lower overall expenses. We've also tried to keep our own fee low at 50 basis points^x, with break points that drop it down to 30 basis points at higher asset levels.

By the way, while the institutional share class has a \$100,000 minimum, financial advisors can aggregate client assets to meet that minimum on most supermarket platforms. Also, we will selectively waive the minimum. The investor share class has a \$1,000 minimum and expenses are capped at 1.74%, which is still quite a bit below the Morningstar category average.

Each of your managers runs their own public fund. Why not invest directly with their funds? ^{xi}

Each does run their own fund, but in each case there are differences in the portfolio they are running for us. In essence we've asked them to run an enhanced portfolio for this fund and the multi-manager structure gives them the flexibility to do so.

For example, Jeffrey Gundlach is running a portfolio for us that has a similar mandate to the private hedge fund he runs, which we've invested in, including me personally. The portfolio will have some leverage. It will have higher potential volatility and in turn seek a higher return and is really quite different than the portfolios he runs in DoubleLine's public fixed-income funds^{xii}.

Steven Romick and his FPA team are running a portfolio for us that is also intended to look more like his private hedge fund. Our expectation is that it will fall somewhere in between his public fund and the private fund.^{xiii} There will also be some potential differences. For example, because he will be running a small asset base for us, we could, if warranted, see more global micro/smaller-cap stocks in the Litman Gregory portfolio. We have also done something creative within the fund's structure that will allow him to run a portfolio that is closer to his private hedge fund portfolio. When we first approached him he let us know that there were opportunities that he would not be able to pursue if he had to manage to daily liquidity. We allayed that concern based on input from the other managers that they expected to have sufficient liquidity to cover the fund's needs, should there be redemptions, on a daily basis. The FPA team will be asked to fund redemptions, if there are redemptions, only on a quarterly basis. Romick's strategy is also quite liquid but some of his positions may have less liquidity and this gives him the flexibility to pursue them.

The Water Island team, led by John Orrico, will be running a best-ideas portfolio for us so that will be focused on their top 30 or so merger arbitrage deals based on their assessment of risk-adjusted returns. In addition, they will invest up to 20% of their portfolio in special situations that could include restructurings, refinancing plays, spin-offs, and other arbitrage plays that they believe are very attractive. They are able to do this because of the relatively low asset base they expect to be running for this fund. Their portfolio will also utilize some leverage.^{xiv}

The Loomis team will be running a portfolio that is more flexible than their public fund in pursuing value in three areas -- credit, curve and currencies. In doing so it will have a somewhat higher targeted cap on volatility as it seeks higher returns. However, the volatility target is still low at 6% to 8%. The flexibility comes into play in allowing them to potentially make bigger bets in the areas in which they have the most conviction.^{xv}

The fact that the fund has four managers running different strategies is one reason why they are able and willing to run strategies that are different from what they run in their public funds. The use of a low-correlated multi-manager format somewhat alleviates shorter-term volatility concerns from a standalone strategy, making it possible for each to pursue more alpha and accept somewhat more short-term volatility, though even at the individual strategy level we believe volatility will be relatively mild.

So individually each of these strategies will be somewhat different than the managers' own public funds with the goal of delivering more long-term alpha. Collectively we believe they will do so at the risk level we are targeting.

What do you think the fund's role is in a portfolio? How are you using it with your own clients?

In our opinion it could be used several ways.

First and foremost we view it as a core alternatives position. It could be a sole alternatives holding or one that could be supplemented with other diversified funds or single-strategy funds. Generally we believe that it is appropriate to substitute the fund in a portfolio for a portion of the stock and bond allocation. For example, for each dollar invested in the fund, an investor could reduce their allocation to stocks and bonds, with 60% coming from bonds and 40% from stocks. We think this is a reasonable allocation approach and this is how we think of the fund when using it in our own client portfolios, but some investors may choose to fund it with a slightly larger or smaller equity reduction. And for the record, we rebate our fee on client accounts, so we have no financial incentive for investing them in this fund. To the contrary, we created it because we believe it would benefit them, and we hope it will benefit others with the same risk-reduction goals we have.

Some investors and advisors sometimes look at the low volatility targeted by some alternative funds and think they are good bond substitutes. We don't agree and think it is a mistake to fund this type of investment entirely from bonds in a balanced portfolio because in a severe bear market, it's likely that high-quality investment-grade bonds would perform better and provide more diversification value. But based on the reasons I mentioned earlier—how the strategies may correlate, the risk averse mindset of the managers, and our assessment of the risks in their investment universes and strategies, it's our belief that the fund will hold up better in a severe market downturn than the approximate stock/bond mix we are funding it from, while delivering higher long-term returns.

We also believe the fund could be a sizable core holding for a moderate to low risk portfolio.

Alternatives are a rapidly growing investment category in the investment world in general and the mutual fund world in particular. As someone who has spent over 30 years in the investment management business, what mistakes should investors watch out for when investing in alternative funds?

Properly understanding the risk expectations is essential. And just as important is having confidence in the quality of management and their ability to deliver alpha. In my opinion, there is a lot of mediocrity out there.

Any other thoughts you'd like to share?

We're very excited about this fund and, personally, my confidence is high enough that I've already made a very large investment of my own in the fund. Others who have been closely involved in the development of this fund have also put major portions of their own portfolios in the fund. We've also taken meaningful positions in our client portfolios so all of that speaks to our confidence.

ABOUT THE LITMAN GREGORY MASTERS ALTERNATIVE STRATEGIES FUND

The Litman Gregory Masters Alternative Strategies Fund is a multi-manager, multi-strategy fund that combines alternative and absolute-return-oriented strategies chosen based on Litman Gregory's conviction that each individual manager's strategy is compelling, and that collectively the strategies are well diversified. The fund seeks to achieve long-term returns with lower risk and lower volatility than the stock market, and with relatively low correlation to stock and bond market indexes at a reasonable cost.

The fund is run by Litman Gregory Fund Advisors and Jeremy DeGroot is the portfolio manager. Day-to-day management is handled by four managers running for distinct strategies:

DoubleLine Capital—Jeffrey Gundlach: Opportunistic Income

First Pacific Advisors (FPA)—Steven Romick, Brian Selmo, Mike Landecker: Contrarian Strategy

Loomis Sayles—Matt Eagan, Kevin Kearns, Todd Vandam: Absolute Return Fixed Income

Water Island Capital—John Orrico, Todd Munn, Roger Foltynowicz, Gregg Loprete: Arbitrage

Institutional Share Class

Net Expenses: 1.49%

Investment Minimum: \$100,000

Symbol: MASFx

Cusip: 53700T 801

Investor Share Class

Net Expenses: 1.74%

Investment Minimum: \$1,000

Symbol: MASNx

Cusip: 53700T 884

Available on most trading platforms.

For more information contact Scott Jones at (925) 253-5249 or lg-fa@lgam.com.
www.mastersfunds.com

Past performance does not guarantee future results. Index performance is not illustrative of fund performance. An investment cannot be made directly in an index. The fund is new and performance information is not available. Once performance is available, it can be obtained by calling 1-800-960-0188 or visiting www.mastersfunds.com.

Investment in absolute return strategies are not intended to outperform stocks and bonds during strong market rallies.

The fund's investment objectives, risks, charges, and expenses must be considered carefully before investing. The statutory and summary prospectuses contain this and other important information about the investment company, and it may be obtained by calling 1-800-960-0188. Read it carefully before investing.

Though not an international fund, the fund may invest in foreign securities. Investing in foreign securities exposes investors to economic, political and market risks, and fluctuations in foreign currencies. Investments in debt securities typically decrease when interest rates rise. This risk is usually greater for longer-term debt securities. Investments in mortgage-backed securities include additional risks that investor should be aware of including credit risk, prepayment risk, possible illiquidity, and default, as well as increased susceptibility to adverse economic developments. Investments in lower-rated and non-rated securities present a greater risk of loss to principal and interest than higher-rated securities. Derivatives may involve certain costs and risks such as liquidity, interest rate, market, credit, management, and the risk that a position could not be closed when most advantageous. Investing in derivatives could lose more than the amount invested. The fund may make short sales of securities, which involves the risk that losses may exceed the original amount invested. Merger arbitrage investments risk loss if a proposed reorganization in which the fund invests is renegotiated or terminated.

Leverage may cause the effect of an increase or decrease in the value of the portfolio securities to be magnified and the fund to be more volatile than if leverage was not used.

Litman Gregory Fund Advisors, LLC has ultimate responsibility for the performance of the Litman Gregory Masters Funds due to its responsibility to oversee the funds' investment managers and recommend their hiring, termination, and replacement.

Diversification does not assure a profit nor protect against loss in a declining market.

The S&P 500 Index consists of 500 stocks that represent a sample of the leading companies in leading industries. The index is widely regarded as the standard for measuring large-cap U.S. stock market performance.

The Barclays Aggregate Bond Index is a market capitalization-weighted index, meaning the securities in the index are weighted according to the market size of each bond type. Most U.S. traded investment grade bonds are represented. The index includes US Treasury Securities (non TIPS), Government agency bonds, Mortgage backed bonds, Corporate bonds, and a small amount of foreign bonds traded in U.S.

The HFRI Diversified Fund of Funds Index measures the performance of a group of constituent hedge funds, which are required to report monthly, net of all fees performance and assets under management

U.S. dollars. Constituent funds must have either (a) \$50 million under management or (b) a track record of greater than twelve (12) months. The HFRI Diversified Fund of Funds index is fund-weighted (equal-weighted) index that measures the net of fees performance of diversified hedge funds. For a fund to be classified as "Diversified" it must exhibit one or more of the following characteristics: invests in a variety of strategies among multiple managers; historical annual return and/or a standard deviation generally similar to the HFRI Fund of Fund Composite index; demonstrates generally close performance and returns distribution correlation to the HFRI Fund of Fund Composite Index. A fund in the HFRI FOF Diversified Index tends to show minimal loss in down markets while achieving superior returns in up markets.

The HFRI Merger Arbitrage Index is a fund weighted (equal weighted) index that measures the net of fees performance of hedge funds that invest in merger arbitrage strategies. Merger Arbitrage strategies typically employ an investment process primarily focused on opportunities in equity and equity related instruments of companies which are currently engaged in a corporate transaction.

Mutual fund investing involves risk. Principal loss is possible.

The Litman Gregory Masters Funds are distributed by Quasar Distributors, LLC.

ⁱ Hedge funds are typically aggressively managed portfolios that use advanced investment strategies such as leveraged, long, short and derivative positions in both domestic and international markets with the goal of generating high returns (either in an absolute sense or over a specified market benchmark). Hedge funds are most often set up as unregulated private investment partnerships that are open to a limited number of investors and require a very large initial minimum investment. Investments in hedge funds are illiquid as they often require investors keep their money in the fund for at least one year.

ⁱⁱ Portfolio risk is the forecasted annualized standard deviation of portfolio returns. Standard deviation measures the variance of a portfolio's returns compared to its average return. Downside standard deviation measures the variance of a portfolio's returns that fall below a minimum acceptable returns

ⁱⁱⁱ Sharpe Ratio is a measure of the excess return (or risk premium) per unit of deviation in an investment asset or a trading strategy, typically referred to as risk. The Sharpe ratio is used to characterize how well the return of an asset compensates the investor for the risk taken, the higher the Sharpe ratio number the better. When comparing two assets each with the expected return against the same benchmark with return, the asset with the higher Sharpe ratio gives more return for the same risk.

^{iv} The trailing three and five year annualized returns for a blended portfolio composed of 60% Barclays Aggregate Bond Index and 40% S&P 500 Index as of 8/31/2011 were 4.56% and 4.25%, respectively. The trailing three and five year annualized returns for the largest fund in the Morningstar Multialternative Category as of 8/31/2011 were 3.48% and 3.14% respectively.

^v Portfolio volatility measures the dispersion of a portfolio's return over time, and can be measured either as the variance of a portfolio's return over time compared to its average return, or as the variance of the portfolio's return over time relative to the return of a benchmark

^{vi} Correlation is a statistical measure of how two securities move in relation to each other. High correlation means that movement up or down in the price of one security will closely match the movement of the other; low correlation means that movement in one security will not be closely matched in the movement of the other.

^{vii} Historical volatility is based on the S&P 500 Index and the Barclays Capital Aggregate Bond Index.

^{viii} Based on the performance of the funds that compose the Morningstar Multialternative Fund Category.

^{ix} Morningstar Multialternative Fund Category average expense ratio as of 9/30/2011 was 2.01%

^x A basis point equals one hundredth of 1 percentage point.

^{xii} The private hedge fund managed by Jeffrey Gundlach charges a management fee of 1.00 plus a provisional performance fee. The fund does not offer daily liquidity to investors and is available to a limited number of qualified investors. The fund is structured as a partnership for federal income tax purposes, as such investors must report on their federal tax returns their share of the fund's income, gains, losses, deductions and credits for each taxable year. The DoubleLine mutual funds managed by Gundlach pay management fees ranging from 0.50% to 1.00% and have total net expense ratios ranging from 0.54% to 1.42%, net of fee waivers and expense reimbursements. The investment objectives for the DoubleLine mutual funds managed by Gundlach include capital appreciation, current income and total return, and total return. The DoubleLine Multiasset Growth Fund may invest in equity securities, fixed income securities, real estate related securities, commodities related securities and currencies. Total net assets in the three funds as of 9/30/2011 were \$12.2 billion.

^{xiii} The private hedge fund managed by Stevonn Romick charges a management fee of 1.00% plus a provisional performance fee. The fund does not offer daily liquidity to investors and is available to a limited number of accredited and qualified investors. The fund is structured as a partnership for federal income tax purposes; as such investors must report on their federal tax returns their share of the fund's income, gains, losses, deductions and credits for each taxable year. The FPA Crescent Fund, a mutual fund managed by Stevonn Romick, pays a base management fee equal to 1.00% and has a total annual operating expense ratio of 1.28%. FPA Crescent Fund's objective is to provide a total return consistent with reasonable investment risk, through a combination of income and capital appreciation. Total net assets in the fund as of 9/30/2011 were \$6.5 billion.

^{xiv} The Arbitrage Fund managed by John Orrico pays a management fee of 1.05% and has a net total annual expense ratio of 1.92% after fee waivers and expense reimbursements. Total net assets in the fund as of 9/30/2011 were \$xx and the fund held XX securities as of that date. The fund's objective is capital growth.

^{xv} The Loomis Sayles Absolute Strategies Fund pays a management fee of 0.70% and has a total annual expense ratio of 1.03%. Total net assets in the fund as of 9/30/2011 were \$549 million. The fund's objective is absolute total return with relatively low volatility. The Fund's long and short investment exposures may, at times, each reach 100% of the assets invested in the Fund (excluding instruments primarily used for duration management and short-term investments (such as cash and money market instruments)), although these exposures may be higher or lower at any given time.