AQUILA®
Three Peaks
High Income Fund

AQUILA®
GROUP OF FUNDS

AQUILA®
Three Peaks
Opportunity Growth Fund

Investment Commentary

May 31, 2015

- The month of May was a relatively strong month for the equity market, while the high yield market was more subdued in price movement due to increased volatility in Treasury securities throughout the month and upward movements in Treasury yields since mid-April. The yield of the 10-year Treasury increased to 2.12% at the end May from 1.87% in mid-April and reached 2.29% in mid-May before declining into month-end. Increased volatility in Treasury yields is largely being caused by improving economic data in the U.S. and Europe, which is creating increased uncertainty with regard to Federal Reserve actions as they look to begin monetary policy normalization at some point in the near-future. Timing of such action has been highly debated by many market participants although it seems as if the current consensus is pointing towards a September 2015 lift-off. Economic data began to show signs of life in May after a fairly lackluster start to the year, which has been blamed on adverse weather, the West Coast port closure, and a strengthening dollar.

- First quarter 2015 corporate earnings reports concluded in May, with many companies generally reporting better-than-expected earnings on what would be considered slightly better revenue growth. Expectations were fairly low for the first quarter, as many analysts recognized the strength of the dollar throughout the quarter would impact corporate results. That being said, not all companies got a hall pass and those that did not show reasonable revenue growth or the ability to maintain margins experienced volatility in their equity price. Merger and acquisition activity continued to be prevalent and has been spreading across many industries, as companies look to bolster product offerings and/or generate cost synergies to drive shareholder value. According to Bloomberg, announced global M&A activity for April and May combined already surpasses $1 trillion, making the second quarter of 2015 the fifth consecutive quarter above $1 trillion. After several years of balance sheet discipline by many companies, we are starting to see a more meaningful use of debt and increased leverage to fund shareholder activity. This is a trend we will closely monitor as we progress through the year, as excessive use of debt could create future solvency issues.

- The average spread of the JPM High Yield Index declined to 515bp at the end of May from 522bp at the end of April, while the average yield-to-worst of the Index declined slightly during the month to 6.41% from 6.43%. The high yield primary market remained fairly active throughout the month as market sentiment continues to allow for the elevated supply. A total of $35.0 billion of new issuance priced during May compared with $37.7 billion, $40.1 billion, and $33.5 billion for April, March, and February, respectively. Refinancing activity increased to 63% of proceeds for May compared to 45% during the first quarter of 2015, as companies seemed to accelerate refinancing activity in light of rising Treasury yields. Year-to-date new issuance is $168.3 billion compared to $173.2 billion over the same timeframe last year. Refinancing and acquisition proceeds account for 53% and 28%, respectively, of YTD 2015 volume, compared to 54% and 26% for all of 2014. While we believe there will continue to be opportunities for companies to refinance debt maturities, the trend toward more aggressive use of proceeds (i.e. M&A, dividends, stock repurchases) is likely to continue to increase as we progress through the year. The LTM default rate decreased to 1.6%, while the LTM rate excluding the default of Caesars Entertainment remains below 1.0%. Bonds trading at distressed levels (below $70) remained stable at 3.3%, indicating that default activity is expected to remain relatively benign in the current environment.

- We continue to focus our research efforts on finding companies that operate in stable industries and with management teams that are exceptionally communicative and focused on strengthening the balance sheet while growing operations. We remain committed to finding companies and securities that we believe will exhibit less price fluctuation should volatility increase within the high yield market or should Treasury yields rise. We believe this strategy is exceptionally prudent at this time. We also believe our approach to selecting companies who are using leverage prudently will benefit the performance of our equity strategy, should the equity market remain on solid footing.

- Thank you for your continued support and investment.

Before investing in a Fund, carefully read about and consider the investment objectives, risks, charges, expenses, and other information found in the Fund prospectus. The prospectus is available from your financial advisor, and when you call 800-437-1020 or visit www.aquilafunds.com.

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