AQUILA®
Three Peaks
High Income Fund

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Investment Commentary

Period ending December 31, 2018

While 2018 was not shy of volatile market movements and increasing economic/market risks, it was really a multitude of events throughout the fourth quarter that perpetuated what ultimately became a significant risk-off/flight-to-quality rotation and focus on capital preservation heading into 2019. First, in early-October, Federal Reserve Chair Powell commented that the Fed Funds rate may be well below the "neutral" rate and suggested continued rate hikes and balance sheet normalization over the foreseeable future. The following day, Vice President Pence commented that a resolution to the U.S./China trade tensions was far from being agreed upon. The combination of these two issues started a rotation within the equity market from growth/cyclical stocks to value/defensive stocks and a sell-off of lower-quality names within the high yield market as market participants became increasing concerned with regard to an overly aggressive tightening monetary policy and increased uncertainty between U.S./China relations. While the equity and high yield indices suffered declines in October, panic did not appear to be setting in; rather a more methodical decline in risk-asset appetite amid these increasing concerns. In fact, the 10-year Treasury yield increased to 3.23% in early-October, which was the highest level since May 2011.
In early-November, the combination of the price of oil entering bear market territory as it declined below $60 a barrel, after being above $75 in early-October, and increased debt burden and liquidity concerns related to GE, added fuel to investor concerns regarding global economic growth and corporate credit strength. In hindsight, these events, in conjunction with events of early-October and a multitude of budding domestic and global economic concerns, appear to be the tipping point as yields on Treasury securities began what would become a persistent march lower to the end of the year. The yield on the 10-year Treasury Note closed at a year-to-date and multi-year high of 3.24% on November 8th, before finishing the month of November at 2.99%.

December started off with elevated concerns regarding U.S./China trade negotiations, as the U.S. Administration announced a delay in the next round of tariff increases until March 2019, from the originally planned January 2019. While on the surface this initially appeared as a positive release, investors quickly came to realize that a delay likely meant that the two sides were not close to a resolution, thus creating prolonged uncertainty. Two events during the third week of December would combine to send the S&P 500 down 9.6% and the Bloomberg Barclays U.S. Corporate High Yield Index down 2.7% in the six trading days leading up to Christmas Day. First, investment manager Jeffrey Gundlach of DoubleLine Capital, during an interview on CNBC, would sound the alarms suggesting concerns surrounding Fed actions, weakening global economic activity, corporate debt/balance sheet issues, and suggest that equities were in a bear market where he saw further downside risk. Two days later, the Federal Reserve increased the Fed Funds rate for a fourth time in 2018 and the ninth time since they began raising the rate at the end of 2015. The hike, in combination with commentary that suggested further rate hikes and continued balance sheet normalization to come in 2019, was not well received by an already skittish group of market participants and investors for reasons mentioned above. Following the worst Christmas Eve stock market performance on record, Fed officials quickly attempted to ease investor concerns with "data dependent" commentary in what appeared to be an attempt to stabilize the equity and credit markets.
While actual economic statistics were not deteriorating to the degree that markets were selling off throughout the fourth quarter, and the increased volatility may be creating some opportunities across the investment landscape, we remain cognizant of the negative impact that increased equity and credit market volatility may have on business and consumer confidence. The sensitivity of the markets to commentary out of the Federal Reserve and the China trade war highlight how market participants and investors have become increasingly concerned about how far along we are in the economic cycle. This has led us to maintain our relatively low-duration and high-quality positioning within our high yield strategy as we enter 2019.

High Yield Performance Overview – December 2018

The Aquila Three Peaks High Income Fund Class Y share (ATPYX) generated a negative 1.30% total return during the fourth quarter of 2018. By comparison, the Bloomberg Barclays U.S. Corporate High Yield Index generated a negative 4.53% return. A broad decline across risk assets and waning investor risk appetite challenged returns across the high yield market during the fourth quarter. On a monthly basis, the Barclays High Yield Index generated a negative 1.60% return during October, a negative 0.86% return during November, and a negative 2.14% return during December. The decline of the Index during December marked only the fourth time in 30 years that the Index was negative for the month of December. By comparison, the Aquila Three Peaks High Income Fund Class Y share (ATPYX) generated monthly declines of 0.51%, 0.04%, and 0.76% in October, November and December, 2018. In terms of ratings performance, lower-quality bonds (CCC-rated) significantly underperformed their higher-quality counterparts (BB and B-rated) during the quarter, reversing the segment's outperformance throughout much of the year. For the quarter, the CCC-segment of the Index generated a negative 9.28% return, with monthly declines of 2.46%, 2.84%, and 4.27% in October, November and December, 2018. While the higher-quality segment was not able to avoid losses, the degree of decline was much less severe as the BB-segment of the Index produced a negative 2.91% return for the quarter, with monthly declines of 1.37%, 0.25%, and 1.31% in October, November and December, 2018.

We had very little exposure to the CCC-segment throughout the quarter, as we have avoided this segment of the market throughout much of 2018, due to our belief that the potential risk to the downside greatly outweighed the benefit of investment. As credit spreads across the investment grade market and the higher-quality BB-segment within high yield began to rise, we felt that at some point this could have a ripple effect down the ratings spectrum. While that occurred during the fourth quarter, we still believe there is the potential for significant volatility across the lower-quality segment and have maintained minimal exposure to the segment as we enter 2019. There were no industry segments within the Barclays HY Index that produced a positive return during the quarter. The better performing industry segments were relatively defensive in nature: Utilities, Media Entertainment, Supermarkets, Lodging, and Banking. Underperforming industry segments were either commodity-related, highly-cyclical or highly-leveraged as the decline in oil and concerns about economic strength and access to capital weighed on investments in these areas. As a result, Energy, Wireline Telecommunications, Chemicals, Metals/Mining, and Retailers were the worst performing industry segments during the quarter. We had minimal to no exposure across many of these segments, which helped our relative performance throughout the quarter. Our high yield strategy's strong relative performance during the fourth quarter was due to our focus on downside protection in an increasingly uncertain environment, by targeting low-duration bonds across higher-quality companies that operate in less-cyclical industries. While yields are higher across the asset class, many of the issues that impacted the capital markets in the fourth quarter remain unresolved as we enter 2019, and could continue to be a headwind as we progress through the year. As a result, we continue to believe our relatively defensive positioning within the high yield market remains prudent in the current environment.

For the year ended December 31, 2018, the Aquila Three Peaks High Income Fund Class Y share (ATPYX) generated a negative 1.09% total return. By comparison, the Barclays U.S. Corporate High Yield Index generated a negative 2.08% return for the year. The performance of the high yield market was quite bifurcated throughout the year. During the first half of the year, investors had to contend with duration concerns and spread widening across the higher-quality segment and more rate-sensitive bonds as yields of Treasury securities rose. During this period, the lower-quality CCC-segment of the Index significantly outperformed and was up 3.2% at the end of June compared to a 1.8% decline for the higher-quality BB-segment. We viewed this as a bit of an anomaly as historically, this type of performance dispersion had not occurred. Historically, when the BB-segment was negative, it still outperformed the CCC-segment, which typically performed far worse. For this relationship to correct itself, we believed something would have to give over the balance of the year; either the BB-segment would need to start performing better or the CCC-segment would need to come under pressure. Third quarter performance was quite positive for all ratings-segments of the Index; however, the CCC-segment, which was up 5.99% for the year at the end of the third quarter, was still significantly outperforming the BB-segment, which was up only 0.51% YTD through the end of the third quarter. As noted above, the CCC-segment significantly underperformed in the fourth quarter as oil declined and a flight-to-quality and risk-off rotation started to occur. For the full year 2018, the BB-segment generated a negative 2.41% return while the CCC-segment ended the year down 3.84%. We believe this swing in performance and significant underperformance across the CCC-segment is an indication of the danger of investing across this segment when investor sentiment turns and/or when economic concerns start to increase. It also portrays the high degree of volatility that the lower-quality segment can experience in relatively short order, which can be a shock to investors expecting fixed-income-like stability rather than equity-like volatility when risk aversion increases. For this reason, we continue to take an extremely guarded approach to lower-quality names across the high yield market in the current environment. Similar to the quarterly comments on industry performance, better performing segments for the year were generally more defensive in nature while the underperforming segments were either commodity-related, highly-cyclical or highly-leveraged. As a result, Utilities, Healthcare, Telecom, Pharmaceuticals, and Supermarkets were the best performing industry segments while Energy, Automotive, Homebuilders, Banking, and Building Materials were the worst performing industry segments.

This bifurcated performance that impacted the high yield market in 2018 can also be seen when comparing various risk asset classes throughout the year. For example, the S&P 500 had significantly outperformed the 10-year Treasury throughout much of the year until this trend reversed in the fourth quarter. At its high in late-September, the S&P 500 was up over 11.0% compared to finishing the year negative 4.4%, which was actually well off the lows registered in late-December. On the other side of the risk spectrum, the 10-year Treasury was down nearly 5.0% for the year through October and early-November, before significantly rallying to finish the year essentially flat on a total return basis. Again, this is just representative of how quickly investor sentiment can shift in times of uncertainty. Similar to the performance of the 10-year Treasury, the Barclays Aggregate Index ended essentially flat on the year after being down for much of 2018. Interestingly, and despite a benefit from declining Treasury yields at the end of the year, the Barclays Investment Grade Bond Index finished the year negative 2.51%, which underperformed the Barclays High Yield Index. We are closely monitoring the Investment Grade bond market, as yield spreads increased significantly throughout 2018 and an increasing concern has developed with regard to the ballooning amount of corporate debt and potential for increased credit ratings downgrades into the high yield market as we enter 2019. We continue to focus our investments in shorter-dated bonds of relatively higher-quality companies which we believe operate in more defensive industries in the current environment. We believe this will provide a relatively stable return profile when compared to various fixed-income asset classes, let alone within the high yield market. We saw the strategy exhibit this relative stability throughout 2018. The strategy outperformed the BB-segment and other higher-quality interest rate sensitive fixed-income asset classes in the first half of 2018, while outperforming not only the lower-quality CCC-segment but all ratings segments within the high yield market during the fourth quarter. According to Lipper Inc., the Aquila Three Peaks High Income Fund Class Y share (ATPYX) performance for all of 2018 ranked in the 14th percentile, at #95 of 672 funds in Lipper's High Yield Bond category. Given the potential for heightened volatility in a restrictive monetary policy environment, we believe our approach to lessen volatility and protect on the downside continues to be prudent.

High Yield Market Review – December 2018

The average yield spread of the Barclays U.S. High Yield Index widened by 105bps during December to end the month at 541bps. For the fourth quarter, the average spread of the Index increased 208bps from 333bps at the end of September. For the year, the average spread of the Index increased 177bps from 364bps at the end of 2017. The average yield-to-worst of the Index ended December at 7.95%, which was an increase of 73bps from the end of November, and 109bps from the end of September. For the year, the average yield-to-worst of the Index finished 223bps higher than the 5.72% at the end of 2017. The yield and spread for the Index ended the year at the highest levels since early-2016. The average bond price of the Index decreased to $92.56 at the end of December from $95.18 at the end of November and $98.77 at the end of September. For the year, the average bond price of the Index finished $8.35 lower than the $100.91 average bond price at the end of 2017.

New issuance activity in the high yield primary market remained largely shut down during December due to heightened market volatility and elevated mutual fund outflows. No new issuance priced during the month of December, which is only the second time going back to 1990 that not a single deal priced during a month (November 2008 was the other occurrence). During the fourth quarter, new issuance totaled $19.0 billion, making the quarter the slowest since the first quarter of 2009. For the year, new issuance totaled $187.4 billion, which was down 43% compared to 2017's $328 billion. Notably, 2018's new issue volume was the lowest annual total since $180.7 billion priced in 2009, and compares with average annual issuance volume of $307 billion over the past nine years. Refinancing activity accounted for 61% of 2018's issuance compared to 63% for 2017. With yields and refinancing costs higher throughout much of the year, we saw a decline in the amount of "opportunistic" refinancing activity within the high yield market compared to recent years. Additionally, the leverage loan market experienced a significant increase in new issuance, some of which likely came at the expense of issuing bonds in the high yield market.

Directional changes in fund flows can be valuable in assessing the risk-appetite of investors, which can influence new issuance demand and the overall performance of the asset class. According to J.P. Morgan Credit Research, high yield mutual funds and ETFs experienced $20.2 billion of outflows during the fourth quarter and $45.1 billion of outflows for all of 2018. J.P. Morgan Credit Research also reports that the U.S. high yield default rate declined 8bps sequentially in December to 1.81%. For the year, the default rate increased 53bps from 1.28% at the end of 2017, but remains relatively low compared with the 3.57% rate at the end of 2016 and the long-term historical average of 3.46%. Many high yield strategists forecast that the default rate should remain below the historical average throughout 2019. We continually monitor credit trends, distressed debt, and default activity closely. While credit trends were generally favorable throughout much of 2018, we are cognizant that financing costs have increased and companies will likely continue to face rising operating costs in 2019, which may pressure operating and cash flow margins. These have historically been a precursor to weakening credit trends, increased credit ratings downgrade activity, and potentially, corporate solvency issues. We will be closely monitoring margin profiles and use of free cash flow across our companies and the overall corporate landscape to assess any potential ratings downgrade risk or increased solvency issues as we progress through 2019. In general, we believe these measures are key to watch not only because of what they mean for the perception of the high yield market, but also as it pertains to the future prospects of the overall investing landscape, the economy, and the health of the consumer.

Economic data, while generally supportive of an expansionary economy, did begin to show signs of slowing or deterioration throughout the fourth quarter, in particular throughout December. Business sentiment and confidence indicators will warrant close attention in the coming year. In general, these measures also began to weaken through the fourth quarter of 2018 and will be important indicators to monitor as it relates to economic activity and employment throughout 2019. Labor market data would generally suggest that momentum in the U.S. economy remains stable, however, we are cognizant that these measures are generally lagging indicators and the mind set of corporate managers can change quickly if signs of economic weakness or increased uncertainty become more prevalent. After a long period of broad improvement across the labor market, any signs of weakness related to employment/hiring/layoffs would be a reason for concern. With household spending accounting for approximately 70% of U.S. economic activity, the strength of the consumer and the willingness and ability to purchase goods and services are a key driver to corporate profits and economic activity. Monitoring data regarding consumer confidence and consumer spending will remain a high priority throughout 2019.

In December, the Federal Reserve raised interest rates for the fourth time in 2018. While this final hike of 2018 did not come as much of a surprise given Fed commentary and market expectations were suggesting a hike in December was likely, market participants were not comforted by the accompanying commentary suggesting further rate hikes and a continued balance sheet unwind over the foreseeable future. For 2019, commentary from the Federal Reserve suggests that the committee plans to continue to tighten monetary policy at a moderate pace, and expects to raise the target rate another 50 basis points using two 25 basis point rate hikes. Policy makers appear to sense a need to stay ahead of any potential overheating of the economy, despite the recent increase in market volatility and geopolitical uncertainties. Interestingly, and something we will have to monitor as we progress through 2019, even though the Fed itself suggested the potential for two hikes to come in 2019, the Fed Funds futures-implied probability has begun to suggest an increased potential for a rate cut by the time 2019 concludes. In our opinion, this suggests a clear disconnect between the Federal Reserve's expectations and market expectations for the trajectory of economic activity over the next several years. This disconnect keeps us positioned defensively from both a credit-quality and maturity/duration perspective. If Fed expectations are correct, this could increase volatility across Treasury yields, thereby impacting rate-sensitive securities. However, if market expectations are correct, this would likely indicate concerns with economic conditions and corporate solvency. As a result, we believe it is prudent to remain relatively defensive in our positioning until there is greater clarity about the economic/investment landscape and less deviation in expectations between the Fed and the market. The 10-year U.S. Treasury yield declined 30bps in December to finish the year at 2.69%, which is the lowest level since the end of January. After hitting a multi-year high yield of 3.25% in early-November, the yield declined 55bps into year-end and finished the year only 28bps higher than the 2.41% to start the year. The rally in the price of the 10-year Treasury during November and December was driven by a general risk-off/flight-to-quality tone, as well as a downward shift in the number of Fed Funds rate hikes projected for 2019. Considering the Fed raised the Fed Funds rate 100bps throughout 2018, a mere 28bps rise in the 10-year Treasury exemplifies a significantly flatter yield curve as we enter 2019. The spread between the 10-year and the 2-year Treasury ended the year at 20bps compared to 52bps at the beginning of 2018 and represents the lowest level since mid-2007. At the end of December, the spread between the 5-year and 2-year Treasury yield was 4bps, but for several weeks during December this differential was inverted, meaning the yield on the 5-year was lower than that of the 2-year. This was the first time since 2007 that any part of the Treasury curve inverted and is something investors are closely watching due to what it might be saying regarding future inflation and economic growth expectations. Historically, a prolonged inversion in the Treasury yield curve has been a precursor to economic weakness and is something we continuously monitor as we position individual security and industry weightings within our high yield strategy. This is another indicator that leads us to believe that maintaining a relatively defensive positioning is prudent in the current environment.

Our Approach – December 2018

We remain committed to our time-tested and disciplined research process that not only includes detailed analysis of companies owned in our high yield strategy, but also uncovers new opportunities within the high yield market. We continue to look for fiscally responsible management teams that are committed to growing operations prudently and who recognize they can potentially improve their credit profile by focusing on company-specific measures. Our efforts remain focused on stability and predictability in the investment selection process, so as to provide a less volatile high yield strategy that can generate a reasonably consistent total return throughout various rate and economic cycles.

The construction of the high yield strategy continues to be highlighted by securities that we believe have the ability to weather negative headlines and heightened market volatility, while benefitting from company-specific balance sheet and credit improvement. We will maintain our discipline of minimizing volatility, to the extent possible, by generally avoiding securities that appear to have equity-like characteristics, as well as by focusing on sectors we consider to be relatively stable and higher-quality in nature due to greater predictability of revenues and stability in cash flow generation. We continue to believe this approach is warranted and believe maintaining a relatively low duration and shorter maturity profile, is prudent in the current environment. Maintaining a short maturity profile not only allows the securities held within the bond portfolio to better withstand an increase in market volatility and/or rising Treasury yields, but it also increases the potential that holdings will be redeemed by the company through either a call, tender, or maturity. As cash is created by these actions, it allows us the ability to assess the opportunities present in the high yield market at that time. In instances where we have not participated in new bond issuance because we believed it carried excessive interest rate risk or did not adequately compensate for investment risk, we may have an opportunity to deploy cash at more attractive prices and yields if rising Treasury yields or increased market volatility create such opportunities.

While we continuously search for attractive investment options, we believe a strict adherence to our rigid investment philosophy, extensive research process, and discipline in choosing investments for our high yield strategy will remain essential as we enter 2019. Considering numerous uncertainties the capital markets will have to contend with over the foreseeable future, we believe it is important to not become complacent in the current investing environment. As such, we constantly monitor economic data and commentary from companies across various industries, as well as commentary from the Federal Reserve and out of Capitol Hill that may shed light on future investment opportunities or potential investment pitfalls.

In conclusion, we will continue to balance potential risks to the economy and the capital markets with the opportunities presented within high yield bonds to construct a strategy that we believe will have a very compelling risk/return profile throughout various economic/market cycles and periods of elevated market volatility. We will continue to utilize a top-down and bottom-up approach when constructing our high yield strategy as we assess the strength of the economic landscape and the potential for volatility to increase during a period of monetary policy uncertainty.

Thank you for your continued support and investment.

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Please see additional information on the following page.

AVERAGE ANNUAL TOTAL RETURNS AS OF DECEMBER 31, 2018

			CUMULATIVE RETURN			AVERAGE ANNUAL RETURN					
	SEC Yield[1]	Distri-bution Rate[2]	4th Qtr 2018	YTD	1 year	3 year	5 year	10 year	Since Inception	Inception Date	Expense Ratio
A Shares NAV	---	4.32%	-1.35%	-1.29%	-1.29%	3.03%	2.98%	6.57%	4.42%	6/01/06	1.13%
A Shares MOP	3.65%	4.15%	-5.34%	-5.28%	-5.28%	1.63%	2.15%	6.14%	4.08%	6/01/06	1.13%
C Shares w/o CDSC	2.98%	3.50%	-1.56%	-2.08%	-2.08%	2.21%	2.16%	5.72%	3.59%	6/08/06	1.93%
C Shares w/ CDSC	----	----	-2.53%	-3.03%	-3.03%	----	----		----	6/08/06	1.93%
I Shares	3.86%	4.40%	-1.35%	-1.35%	-1.35%	2.93%	2.88%	6.52%	4.46%	6/29/06	1.23%
Y Shares	3.99%	4.53%	-1.30%	-1.09%	-1.09%	3.28%	3.19%	6.80%	4.64%	6/01/06	0.93%
Bloomberg Barclays US Corp HY			-4.53%	-2.08%	-2.08%	7.23%	3.83%	11.12%	6.97%		
Bloomberg Barclays US Aggregate Bond			1.64%	0.01%	0.01%	2.06%	2.52%	3.47%	4.15%		
Lipper Ranking - Y share High-Yield Bond Funds[3]					95 of 672	555 of 582	128 of 487	302 of 312			
Lipper Percentile[3]					14th	95th	26th	97th			

Performance data represents past performance, but does not guarantee future results. Investment return and principal value will fluctuate; shares, when redeemed, may be worth more or less than their original cost; current performance may be lower or higher than the data presented. Class A shares have a maximum sales charge of 4.00%; Class C shares have no initial sales charge, but a 1.00% contingent deferred sales charge applies to Class C shares redeemed within 12 months of their purchase date. Class I shares have no initial or contingent deferred sales charge. Class Y shares have no initial or contingent deferred sales charge. Class I and Class Y shares may only be purchased through an investment professional or financial institution. Class A MOP returns reflect deduction of the maximum 4.00% sales charge; Class A NAV returns do not reflect deduction of the sales charge and would be lower if that charge were reflected. Class C returns without CDSC do not reflect deduction of the 1% CDSC applicable in the first 12 months; if applied, the CDSC would reduce the performance quoted. An explanation of the share classes appears in the Fund prospectus. The Bloomberg Barclays US Corporate High Yield Index is an unmanaged index considered representative of the universe of fixed-rate, non-investment grade debt. The Bloomberg Barclays US Aggregate Bond Index is an unmanaged index considered representative of the universe of fixed-rate, investment grade taxable debt. Performance of an index does not reflect management fees and expenses which are reflected in Fund performance. An investment cannot be made directly in an index. Current month-end performance is available at: 800-437-1020 or www.aquilafunds.com. [1]The 30-Day SEC yield is a mutual fund's yield, calculated as required by the SEC, based on the earnings of the fund's portfolio during a 30-day period, divided by the offering price per share at the end of the period. This calculation reflects an estimated yield to maturity. It should be regarded as an estimate of the fund's rate of investment income, and it may not equal the fund's actual income distribution rate. [2]The Fund's distribution rate is the percentage at which a mutual fund has distributed income to its shareholders. It is calculated by dividing a fund's annualized dividend amount by its current offering price. [3]Lipper category is as of 12/31/18 for class Y share and may not accurately represent the current composition of the portfolio. Lipper rankings are based on total return without sales charge relative to all share classes of funds with similar objectives as determined by Lipper, and each share class is ranked individually. Lipper ratings are not intended to predict future results, and Lipper does not guarantee the accuracy of this information.

Independent rating services (such as Standard & Poor's, Moody's and Fitch) assign ratings, which generally range from AAA (highest) to D (lowest), to indicate the credit worthiness of the underlying bonds in the portfolio. Where the independent rating services differ in the rating they assign to an issue or do not provide a rating for an issue, the highest available rating is used in calculating allocations by rating. Non-rated bonds are holdings that have not been rated by a nationally recognized statistical rating organization.

Investment Considerations: Mutual fund investing involves risk; loss of principal is possible. Investments in bonds may decline in value due to rising interest rates, a real or perceived decline in credit quality of the issuer, borrower, counterparty, or collateral, adverse tax or legislative changes, court decisions, market or economic conditions. The Fund's portfolio will typically include a high proportion, perhaps even 100%, of high-yield / high-risk securities rated below investment grade. High-yield corporate bonds generally have greater credit risk than other types of fixed-income securities and may be especially sensitive to economic and political changes or adverse developments specific to the company that issued the bond.

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.