AQUILA®
GROUP OF FUNDS

Investment Commentary

Period ending August 31, 2019

AQUILA®
Three Peaks
High Income Fund

A Shares: ATPAX **C Shares: ATPCX** **I Shares: ATIPX** **Y Shares: ATPYX**

Lipper Category: High Yield Bond
Morningstar Category: High Yield Bond

Market Overview

The month of August was characterized by an escalation of the trade war between the US and China, which caused significant stock market volatility and a strong flight-to-quality trade within the bond market. The stock market started the month of August on a positive note following the July Federal Reserve rate cut, but this favorable performance was short-lived, as President Trump announced a 10% tariff on $300 billion of additional Chinese goods during the first few hours of stock trading on August 1st. Many of these new tariffs impact US consumers directly, as the tariffs include items such as consumer electronics and apparel. Following these additional tariffs, China retaliated by allowing its currency to weaken relative to the dollar and announcing retaliatory tariffs against the US. The US then responded to these Chinese actions by labeling China as a currency manipulator and by announcing incremental tariffs against China. While there were some periods of reprieve, such as a delay in some of the consumer-related tariffs, the trade situation with China remained an overhang for the markets throughout August.

While the S&P 500 was only down -1.58% for the month of August, there was considerable volatility during the month, including 11 of the 22 trading days in the month that experienced over a 1% change from the previous close. The bond market performance during August also reflected the increased uncertainty and elevated concerns, as the yield on the 10-year Treasury bond declined by over 50bps to a 1.50% yield, which is the lowest yield since before the 2016 presidential election. The yield on the 2-year Treasury declined by 37bps to a 1.50% yield, which raised additional concerns about the yield curve inversion and what it suggests about future economic growth. While the high yield market benefited from the decline in Treasury yields, the higher quality segment continued to outperform the lower quality segment which reflected a more risk adverse investor appetite as seen throughout the capital markets in August. As we enter September, market participants will be focused on the US/China trade dynamics, global economic data (which has generally been weakening), US economic data (which has generally been stable), and Federal Reserve commentary. September also brings the next Fed meeting which is expected to result in a second reduction to the Fed Funds Rate for the year, barring any significantly positive developments on the economic data front. Commentary stemming from the meeting will be closely monitored as is relates to future monetary policy.

Aquila Three Peaks High Income Fund and the High Yield Market

The Aquila Three Peaks High Income Fund Class Y share (ATPYX) generated a total return of +0.56% (net of mutual fund expenses) in August. By comparison, the Bloomberg Barclays High Yield Corporate Bond Index produced a return of +0.40%. As has been a theme throughout much of the year due to the decline in Treasury yields, higher-quality bonds outperformed during the month, with BB-rated bonds returning +1.13%, B-rated bonds returning +0.40%, and CCC-rated bonds returning +0.33%. We continue to be cautious of lower credit quality names and remain significantly underweight CCC-rated bonds compared to the Index's 13.1% weighting of this rating segment at the end of August.

Industry performance appears more correlated to credit ratings than any specific cyclical or defensive in nature themes. In general, and at present time, the ratings of many of the constituents within the leading industries are higher rated while many constituents within the laggard industries are lower rated. The best performing industries were Banking (+2.14%), Construction Machinery (+1.91%), Home Construction (+1.72%), Lodging (+1.56%), and Wireless (+1.44%). The worst performing industries were Oil Field Services (-5.17%), Independent Oil & Gas (-3.30%), Wirelines (-0.57%), Retailers (-0.28%), and Automotive (-0.23%). A near 8% decline in WTI oil price during August weighed on the Energy sector, which continues to lag the overall market YTD. We have begun to see default activity increase across the Energy sector and as such remain cautious with regards to the sector and significantly underweight compared to the Index's near 13% weighting in the sector at the end of August. Due to the decline of Treasury yields during the month, longer-duration bonds continued to outperform the overall market as the 6+ year duration segment of the Index produced a +1.41% return compared to a +0.24% return for the 0-3-year duration segment.

While a shorter average maturity and lower duration positioning hindered our strategy's performance relative to the Index during the month, our higher quality focus and limited exposure to the Energy sector benefited our strategy's relative performance. We continue to focus our research efforts on finding companies that operate in relatively stable industries that have management teams who are focused on maintaining a reasonably strong balance sheet, while seeking out securities that we believe will exhibit less price fluctuation should market volatility increase. 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 compelling risk/return profile throughout various economic and market cycles and periods of elevated market volatility.

Corporate Bond Index Update

As a reference, the Bloomberg Barclays U.S. Aggregate Bond Index generated a positive +2.59% return during the month, the BofA Merrill Lynch Current 10-Year Treasury generated a positive +4.67% during the month, and the Bloomberg Barclays U.S. Corp Investment Grade Index was positive 3.14% during the month. The yield-to-worst of the U.S. Aggregate Bond Index ended August at 2.13%, while the yield-to-worst of the U.S. Corp Investment Grade Index ended August at 2.81%. Both indexes have experienced over 150bps of decline in their yield-to-worst since November 2018 and are now at the lowest level since before the 2016 presidential election.

Treasury yields moved significantly lower during the month as the 5-year and 10-year U.S. Treasury yields declined 44bps and 51bps, respectively. The 5-year Treasury yield ended August at 1.39% (down 112bps since 12/31/18), while the 10-year Treasury yield ended August at 1.50% (down 119bps since 12/31/18). Furthermore, the 30-year US Treasury yield declined below 2.0% for the first time in its history. We don't often talk about the 30-year security because the maturity is much longer than what is typically seen in the high yield market; however, we believe the low absolute level of this long bond is indicative of the vast economic uncertainties and seemingly insatiable need for yield as a result of low fixed income yields around the world. We continue to monitor the Treasury market and the shape of the Treasury curve very closely. The yield curve remains very flat and, in many cases, inverted, while overall yields are significantly lower than where they were in mid-November 2018. Investors are closely watching the yield curve due to what it might be saying regarding future economic growth and monetary policy actions. We believe that the dichotomy between a flat/inverted yield curve with longer-term yields significantly lower on the year and yet general support for risk assets with many equity indices near all-time high levels is perplexing.

We remain concerned by the significant shift in Federal Reserve commentary throughout the year and what the potential for multiple rate cuts are indicating about future economic conditions. Due to a lack of clarity with regard to many issues, we believe our relatively lower-duration and higher-quality positioning within the high yield market continues to be prudent in the current environment, as we attempt to limit volatility by balancing out duration and credit risk. This approach served the strategy well throughout 2018, as it weathered interest rate pressure during the first three quarters of the year and then significantly outperformed during the volatile fourth quarter, as credit concerns began to rise.

The average yield spread of the Bloomberg Barclays U.S. High Yield Corporate Bond Index increased 23bps during August to end the month at 421bps. Year-to-date, the average yield spread has declined 120bps. The average yield-to-worst of the Index decreased 16bps during the month to end August at 5.72%. The average yield-to-worst of the Index has declined 223bps from the 7.95% level to start the year. The average bond price of the Index rose slightly to $99.65 at the end of August from $99.60 at the end of July and $92.56 at the start of the year.

According to JPMorgan Credit Research, a YTD monthly low of $11.0 billion of new issuance priced during the month which was a stark contrast to the robust $24.3 billion that priced in July. Despite the slowdown in amount, issuers continued to take advantage of the decline yields to refinance nearing maturities. Refinancing comprised 95% and acquisition/LBO comprised 5% of total new issuance during the month. Year-to-date, $176.9 billion of new issuance has priced with refinancing comprising 68% and acquisition/LBO comprising 20% of total YTD new issuance. Year-to-date, new issuance is now 18% higher compared to the same time last year. The quality of new issuance has been reasonably good with approximately 11% of the YTD issuance carrying a CCC-rating by one of the ratings agencies (would be lowest annual percentage since 2009) and 68% being used for refinancing purposes (continues to track the highest percentage since 2009).

According to JPMorgan Credit Research, there were two high yield bond defaults in August, making 18 year-to-date (none of which we owned), with the U.S. high yield last-twelve-month default rate at 2.54% at the end of August compared to 1.81% at the end of 2018. While the rise in the default rate is concerning, much of the increase has come from stress in the Energy sector and does not currently look to be spreading more broadly across the high yield market. Nevertheless, it is something we will continue to evaluate and monitor closely. As we have been commenting more about recently, credit rating trends have been under pressure during 2019 with both the number and dollar amount of downgrades outpacing upgrades. Credit rating trends continued to deteriorate in August as 21 companies received an upgrade compared to 31 companies being downgraded. This is something we will continue to monitor closely as it can be an indication of increased risk taking or financial leverage that could lead to higher future solvency issues or bond yield/spread widening.

According to JPMorgan Credit Research, high yield bond mutual funds and ETFs reported a $4.5 billion outflow in August following a $3.1 billion inflow in July. August's outflow brings the YTD inflow to $11.1 billion. For reference, high yield mutual funds reported a total of $45.1 billion in outflows for all of 2018. The direction and magnitude of fund flows will remain a key indicator to watch over the balance of the year as they can has a significant influence on the performance of the asset class.

AVERAGE ANNUAL TOTAL RETURNS AS OF AUGUST 31, 2019

	CUMULATIVE RETURN			AVERAGE ANNUAL RETURN					
	MTD	YTD	1 year	3 year	5 year	10 year	Since Inception	Inception Date	Expense Ratio
A Shares NAV	1.41%	4.97%	5.02%	3.96%	3.21%	5.68%	4.64%	6/01/06	1.15%
A Shares MOP	-2.68%	0.75%	0.88%	2.56%	2.37%	5.25%	4.31%	6/01/06	1.15%
Y Shares	1.58%	5.07%	5.36%	4.17%	3.41%	5.88%	4.85%	6/01/06	0.95%
Bloomberg Barclays US Corp HY	0.40%	11.00%	6.56%	6.15%	4.85%	8.50%	7.45%		
Bloomberg Barclays US Aggregate Bond	3.08%	6.11%	7.87%	2.31%	2.97%	3.89%	4.46%		
Bloomberg Barclays US IG Index	3.14%	13.94%	13.33%	4.64%	4.56%	5.85%	5.89%		
S&P 500® Index	-1.58%	18.34%	2.92%	12.70%	10.11%	13.45%	--		

AVERAGE ANNUAL TOTAL RETURNS AS OF JUNE 30, 2019

	CUMULATIVE RETURN			AVERAGE ANNUAL RETURN					
	2nd Qtr 2019	YTD	1 year	3 year	5 year	10 year	Since Inception	Inception Date	Expense Ratio
A Shares NAV	1.41%	4.97%	5.02%	3.96%	3.21%	5.68%	4.64%	6/01/06	1.15%
A Shares MOP	-2.68%	0.75%	0.88%	2.56%	2.37%	5.25%	4.31%	6/01/06	1.15%
Y Shares	1.58%	5.07%	5.36%	4.17%	3.41%	5.88%	4.85%	6/01/06	0.95%
Bloomberg Barclays US Corp HY	2.50%	9.94%	7.48%	7.83%	4.70%	9.29%	7.47%		
Bloomberg Barclays US Aggregate Bond	3.08%	6.11%	7.87%	2.31%	2.97%	3.89%	4.46%		
Bloomberg Barclays US IG Index	4.48%	9.85%	10.72%	3.96%	4.10%	6.08%	5.67%		
S&P 500® Index	4.30%	18.54%	10.42%	14.19%	10.71%	14.70%	--		

Performance current to the most recent month-end and a full list of holdings is available at: 800-437-1020 or www.aquilafunds.

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 Y shares have no initial or contingent deferred sales charge. 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. 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. The Bloomberg Barclays Investment Grade Index is representative of the investment grade, fixed-rate, taxable corporate bond market. The S&P 500® Index is a stock index representative of the 500 largest US companies. 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.

Yield to worst is the lowest potential yield that can be received on a bond without the issuer actually defaulting.

Independent rating services (such as Standard & Poor's, Moody's and Fitch) assign bond ratings, which generally range from AAA (highest) to D (lowest), to indicate the credit worthiness of the underlying bonds in the portfolio. Securities are classified as high-yield if the middle rating of Moody's, Fitch, and S&P is Ba1/BB+/BB+ or below. 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.

Information contained herein has been obtained from sources we consider reliable, but its accuracy is not guaranteed. Any opinions expressed are based on the interpretation of data available to Three Peaks Capital Management, LLC, investment sub-adviser of Aquila Three Peaks High Income Fund and Aquila Three Peaks Opportunity Growth Fund, and are subject to change at any time without notice. This report is for informational purposes only and is not intended as an offer or solicitation for the purchase or sale of a security.

The Members, Officers and Employees of Three Peaks Capital Management, as a policy of the firm, are required to disclose and report investments in reportable securities as defined in Rule 204A-1(e)(10) of the Investment Advisers Act of 1940. Three Peaks Capital Management, LLC may from time to time buy or sell securities of companies mentioned in this report for its advisory clients. Aquila Investment Management LLC, as well as certain of its Investment Companies or Investment Advisory accounts, may own the Securities being reviewed or recommended in this report. Aquila Investment Management LLC and others associated with it may from time to time have long or short positions and effect transactions in the securities of companies mentioned in this report.

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.