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THE WALL STREET TRANSCRIPT
Connecting Market Leaders with Investors

Finding Optimal Balance Sheets by Utilizing High Yield Market Expertise

ZACH MILLER, CFA, is the Co-Portfolio Manager of the Aquila Three Peaks Opportunity Growth Fund and Director of Research at Three Peaks Capital Management, LLC, subadviser to the Fund. Mr. Miller was named Co-Portfolio Manager of the Aquila Three Peaks Opportunity Growth Fund as of October 2013. Since January 2012, Mr. Miller has been Director of Research for the subadviser. Mr. Miller joined the subadviser in 2008 as a research analyst. Mr. Miller received his CFA designation in June 2012 and is a graduate of the University of Northern Colorado, holding a degree in business administration with an emphasis in finance and a minor in economics.

SECTOR — GENERAL INVESTING

TWST: Could you explain briefly a little bit about the fund that you are representing today?

Mr. Miller: Three Peaks Capital Management was founded in 2003 by Sandy Rufenacht, who had managed the Janus High Yield Fund prior to starting Three Peaks. Three Peaks was initially started as a high-yield-focused investment manager, but we always realized that many of the companies we were investing in on the high yield side had really attractive equity stories as well. A lot of these equity stories we were finding were being driven by what the companies were doing with their balance sheets. In 2008, Three Peaks launched our equity strategy using the same research process as our high yield strategy. Then, in 2010, we took over as subadviser for the Aquila Three Peaks Opportunity Growth Fund.

TWST: What are the current assets under management?

Mr. Miller: The mutual fund manages $635 million as of the end of June. At Three Peaks, we have roughly $700 million in equity assets, including that $635 million in the mutual fund. We are also the subadviser for the Aquila Three Peaks High Income Fund, and that represents another roughly $230 million in assets. Overall, Three Peaks has $1.1 billion in total assets under management.

TWST: Can you describe your investment process and to what extent it is quantitative versus qualitative?

Mr. Miller: The core of our strategy is that we want to find companies that are using debt well and making positive balance sheet decisions. We utilize our expertise in the high yield market and our analysis of the whole capital structure to be able to find these optimal balance sheet ideas. There are several attributes that we look for that we think can help companies create value while having debt on their balance sheets. The first thing we look for are companies with stable and predictable cash flow generation through an economic cycle. This means that we avoid the cyclicals as well as the companies that have too much debt because we feel like when the economic cycle turns south, a lot of these companies won't be able to manage the debt on their balance sheets.

Second, we look for companies that have solid asset coverage, which could come from hard asset collateral but also from attributes like leading market positions or growing end markets, or even high revenue visibility from contracts, licenses or patents. Since the stocks that we own have debt on them, we want to make sure that we don't wake up one morning and find that there is nothing left of these businesses after some adverse event happens. We want to make sure that there is asset value.

Third, we look for management teams that have the desire and the ability to pay down debt. We prioritize face-to-face meetings with management teams, and there is nothing like sitting across the table from an executive and hearing him or her

express a commitment and desire to pay down debt and to improve the balance sheet.

Then, the last attribute is we like to see companies that have paid down debt in the past. We feel that this signals a desire to pay down debt in the future. When many companies borrow or take on debt to do a big deal, if they don't pay it back, we think that that's indicative of their aggressive nature toward the balance sheet, whereas if they are paying back the debt, that is a positive sign.

In addition, we also feel like debt paydown is a very sure way of creating value for the equity holders. Each dollar of debt reduction theoretically accretes to a dollar of equity value. This is something we quantify using a metric we call "return on debt paydown," or RODP, which is the total debt paydown divided by the company's market cap. So when a company is paying down debt, we think it is really positive since the value of debt paydown is accreting to the equity, plus the risk profile is improving at the same time. When all of these attributes are in place, we feel like we can find companies with optimal balance sheets, whereby they are maximizing their return on their equity while at the same time minimizing the risk of financial distress.

Highlights

Zach Miller discusses Three Peaks Capital Management, LLC and the Aquila Three Peaks Opportunity Growth Fund. Mr. Miller seeks companies that use debt well and make positive balance sheet decisions. He analyzes this aspect of a company by utilizing his expertise in the high yield market. There are certain attributes that Mr. Miller thinks can help companies create value when they're carrying debt. He looks for stable and predictable cash flow generation through an economic cycle, solid asset coverage, management teams with the desire and ability to pay down debt, and a history of paying down debt. Mr. Miller believes these characteristics are good indicators of optimal balance sheets and companies that can maximize their return on equity as well as minimize the risk of financial distress.

Companies discussed: Liberty Sirius XM Group (NASDAQ:LSXMK); Sirius XM Holdings (NASDAQ:SIRI); Ball Corporation (NYSE:BLL); Charter Communications (NASDAQ:CHTR) and Aramark (NYSE:ARMK).

TWST: Do you monitor macro trends? And if so, which ones, and why?

Mr. Miller: Yes, we do look at a macro and a micro level. From the macro perspective, one of the key indicators that we look at is the overall high yield market. One of the reasons that we feel like this is a good indicator to look at is often we have found that high yield tends to be a leading indicator for the overall risk market when it comes to market selloffs, as we start to see spreads widening prior to equities selling off. We believe that this is driven by the fact that, since high yield bond investors don't have the same upside as an equity investor, they are inherently going to be more risk-averse and cautious. When the market starts feeling like things are running a little too hot, we believe this is when the high yield market sells off in advance of equities. We have seen that happen in the past for the equity strategy.

Another one of the macro leading indicators that we tend to look at is the health of the overall high yield market. We believe that high yield is the fuel that drives a lot of the equity market in terms of when companies want to make acquisitions or increase leverage on their balance sheets to buy back stock. Often, they utilize the high yield market. In many ways, high yield, a $1.7 trillion market, is the lifeblood of the economy when it comes to growth and expansion for a lot of the companies. We feel that watching and considering the health of that market is very important to understand the direction and the health of the overall equity market.

TWST: What sorts of rules govern the fund, including any limits or weights to number of holdings as well as sector allocations?

Mr. Miller: The fund generally holds about 60 to 90 stocks at any given time. We look at the sector allocation a little bit, but it just kind of grows out of the opportunity set that we see in front of us. When we see companies that are doing positive balance sheet actions, if it just so happens they are more weighted toward one industry or another, then we feel like we are going to go to where those opportunities are.

I would add that there are a lot of industries that we will tend to avoid such as cyclical industries that we don't feel have the ability to handle the amount of leverage on their balance sheets. Those tend to be airlines, autos, chemicals, paper

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companies. We tend to avoid those and try to find companies that are more consistent in their cash flow generation.

TWST: What are your top two sectors at this point, and why are they like this? Why are you putting so much in those sectors? For example, a statement from March on the fund shows you had consumer discretionary at 28.63% and health care, which I don't necessarily consider cyclical, at 5.41%.

Mr. Miller: A lot of times people see the consumer discretionary and tend to attribute that to cyclicality, whereas one of the main things that we look at is the cash flows of the business and understanding the stability of those cash flows. Within consumer discretionary, we believe our companies are less cyclical than you might think based on the discretionary sector name. For example, we are invested in cable television and movie theaters. We feel like the stability of these industries' cash flow and their ability to maintain the debt-servicing requirements of their balance sheets are really good.

TWST: Can you talk about some of your top current holdings right now and walk us through how they were selected and maybe even how long they have been held? What is some of your thinking around that particular holding?

Mr. Miller: Liberty Sirius (NASDAQ:LSXMK), which is the tracking stock for **Liberty Media's** investment in **Sirius XM** (NASDAQ:SIRI), has been one of our largest holdings for a while. **Sirius XM** is really synonymous with satellite radio, as **Sirius XM's** equipment now comes pre-installed in about 75% of all new vehicles. The company has done a great job of managing its balance sheet over the years.

One of the things that we have liked about **Sirius XM** is the significant improvement they made to their balance sheet since 2009, which has enabled the company to realize relief on their bond covenants and has been a positive balance sheet catalyst for the company. Covenant relief is something that we feel can act as a positive catalyst for companies. These covenants typically restrict a company's

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1-Year Daily Chart of Liberty Sirius XM Group

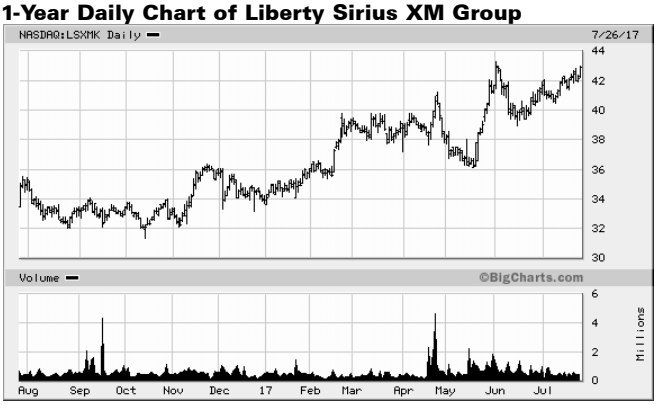

Chart provided by www.BigCharts.com

We watch the high yield bond spreads of the individual issuers in these industries, and we often find that they trade at a low spread relative to the Treasury bond. We feel that this is a positive sign for the company, in that the high yield market, which is a gauge of risk sentiment, is telling investors that they don't view the risk as very significant for these specific companies. That is one of the ways that we mitigate risk, in that we look at the individual credit spreads of these bonds or of these companies that we own. That tends to give us confidence in addition to our own analysis that the high yield market is positive on these companies.

ability to buy back stock or pay dividends, or even increase leverage for acquisitions. Understanding the rules that govern these debt agreements is important for both debt investors as well as equity investors, even though most equity investors don't really take the time to understand the nuances of these

1-Year Daily Chart of Ball Corporation

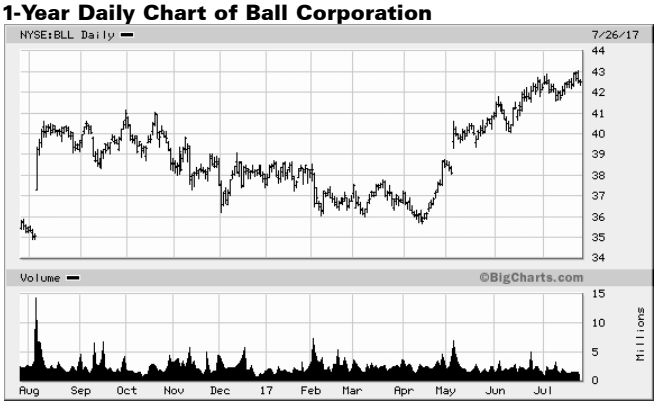

Chart provided by www.BigCharts.com

covenants. We like to see really stringent covenants when companies are highly levered, as **Sirius XM** was early in the company's history.

Going back to 2009, the company's leverage was 6 times debt to earnings before interest, taxes, depreciation and

amortization (EBITDA). That was at a really high level. As companies improve their balance sheets and reduce leverage, we feel like it is only fair to give them relief from the covenants that were put in place when the company had much riskier credit. For **Sirius XM**, in 2012, they refinanced a lot of their more cumbersome high yield bonds, which we had owned at the time in our high yield strategy.

The purpose of the refinancings was to primarily alleviate a lot of the covenants that were in these bonds that restricted their ability to buy back stock. Once they tendered or called at a premium the old bonds and gained relief from these covenants, **Sirius XM** began repurchasing $2 billion of their shares annually, which has now accumulated to $8 billion of total share repurchases. We feel like that has been a very positive catalyst for the stock, and so we feel like they are doing a very good job of utilizing the balance sheet.

TWST: Do you track your average holding time?

Mr. Miller: Our average holding period for the fund has generally ranged from about two to three years. That does include some names where we may own them for a year, and the balance sheet catalyst plays itself out, and then we sell the stock. But then, we may also have some like **Ball Corporation** whereby they are perennially in the fund. We will increase and decrease weights over time as we see the risk/reward changing, but there are some cases where we might own a stock for well more than three years.

TWST: If you had to describe the triggers and/or indicators that you would use to sell a stock, what would they be?

Mr. Miller: We look at what we call an "out-of-bounds leverage ratio." Since all our companies have debt on their balance sheets, we always want to make sure that they are not taking undue risk. When a company increases its leverage above our out-of-bounds leverage range, we feel like that the balance sheet risk is greater risk than what is healthy for the stock, so we sell. Typically, this happens when a company levers up its balance sheet to make acquisitions, or to perhaps even buy back stock or pay a special dividend.

"We will also sell a stock if the management team doesn't communicate with us. We feel like face-to-face interactions with companies are very important, especially when these companies have balance sheets that are highly levered. It is very important to maintain a relationship with the management team."

Another name that we feel has exemplified the Aquila Three Peaks Opportunity Growth Fund strategy is **Ball Corporation** (NYSE:BLL), which is the largest beverage-can producer in the world, with about a $15 billion market cap. We really like the company's very stable cash flows and number one market position in a lot of its end markets. **Ball** has done a great job of exemplifying what we consider an optimal balance sheet. It has managed its balance sheet with an average debt to EBITDA of 3 times, which we feel like is a very conservative level within the high yield market. When you have an optimal balance sheet, it allows companies to use their cash flow in ways that may positively affect the company and equity shareholders.

Most recently, **Ball** acquired its largest competitor **Rexam** for $8 billion. **Ball Corporation** increased its leverage from the low 3 times, all the way to the mid-4-times range as a result of the deal. We expect that leverage should be able to get back down to the low-3-times range over the next two years through debt reduction. By that time, the company is back in that optimal leverage range, and then, they can go and pursue the next opportunity.

We have owned **Ball's** stock ever since we initiated this strategy back in 2008, during which time **Ball's** stock price has increased at a 16% compound annual growth rate (CAGR) compared to 8% for the S&P 500. We have felt like the company's ability to optimally use its balance sheet has been the main driver for the stock, especially when you consider the fact that the company's volumes have essentially been flat on an organic basis since 2008.

We will also sell a stock if the management team doesn't communicate with us. We feel like face-to-face interactions with companies are very important, especially when these companies have balance sheets that are highly levered. It is very important to maintain a relationship with the management team. Our general philosophy is that we really understand the balance sheet, but sometimes, there are things that are happening at the company that we cannot analyze. If we don't feel like we can properly understand what's going on at the company because management won't talk to us, then we will just sell the stock. Those are several of the sell indicators, but selling and risk management is very important for the strategy.

TWST: Can you provide detail on another holding that is different from the ones that you have described?

Mr. Miller: Charter Communications (NASDAQ:CHTR) is a great example of a company that benefited from favorable debt refinancing. In 2009, **Charter** had a very cumbersome balance sheet with its debt at very high interest rates. Through several iterations of debt refinancings, the company was able to reduce its interest

rate on its debt and to reinvest those increased cash flows to accelerate growth. At the end of 2009, **Charter** had about $13 billion of debt, and the average coupon on its bonds was 10.5%.

Through refinancing, it reduced its interest rate to 8% by 2011. By 2013, the interest rate was roughly 6.5%. At the end of 2014, it was nearly 5%. During that period, the company accelerated its capital investments back into the business, which led to an increase in the growth rates for revenue and EBITDA growth. After **Charter** improved its balance sheet flexibility, this also helped **Charter** execute a $60 billion acquisition of **Time Warner Cable** in 2016.

What is really nice about our fund is that we are a rather distinctive strategy in that the approach that we are taking is a bit different than most active equity managers today.

As a further sign of how far that balance sheet has come, **Charter's** secured bonds are now investment-grade-rated today by S&P. **Charter's** stock price has performed very well over this period of time. Much of that was driven by the work that the company was doing on the balance sheet side.

Another stock that has experienced a positive catalyst from balance sheet management is **Aramark** (NYSE:ARMK), which is one of our top holdings currently. A lot of the value that **Aramark** has created over the last several years has been through debt paydown but also from what that debt paydown has allowed the company to do. We have known **Aramark** since their 2007 leveraged buyout. We had built a very strong relationship with the management team of **Aramark** during the period of their private ownership. When they did an IPO in 2013, we had already built models, had the conversations with management, as well as a clear understanding of the business and the strategy going forward.

In a conversation that I had with the **Aramark** CFO when they were a private company, he explained to me how they were really running the business at that time to maximize free cash flow rather than revenue growth or margin expansion, and they were using that cash flow to pay down debt. As a private company, the company had paid down nearly $1 billion of debt, and then, after **Aramark** came public in 2013, it paid down another chunk of debt using the proceeds from the IPO. This gave them the opportunity to reinvest back into the business and focus less on the cash flow element and more on growing that cash flow over time through margin expansion and revenue growth. Since the IPO, the company has been able to expand its EBITDA margins by 100 basis points, so they have gone from 8.5% at the IPO to 9.5% today.

This reinvestment and the lower leverage since the IPO have also resulted in what we always look at as a one-two punch that companies often get from the benefits of an improved balance sheet. They have the possibility of being rewarded even greater in the equity market by an expanded multiple. When we look at valuations, we look at enterprise value (EV) to EBITDA multiples or EV to EBITDA. With **Aramark**, we have seen the EV to EBITDA multiple expand over the past year. We feel like it has really been driven by the efforts that the company has been doing since the IPO to improve the benefits from that improved balance sheet by reinvesting back into the business and accelerating the margin expansion and revenue growth. We feel like **Aramark** is really a good picture of not just the life cycle of companies in our portfolio, that we may know them from the time they are private companies to the time they have gone public, but it is also a good representation of how beneficial balance sheet improvement can be for the whole company.

TWST: Do you have any final words on why an investor would want to choose your fund over, say, a similar type of fund?

Mr. Miller: What is really nice about our fund is that we are a rather distinctive strategy in that the approach that we are taking is a bit different than most active equity managers today. We are very focused on analyzing the balance sheet aspect of a company by utilizing the high yield market. Our expertise in the high yield market goes back many years really to Sandy Rufenacht, who started Three Peaks and who has a history dating all the way back into the late 1980s, which is truly the beginning of the high yield market. We have seen how this market can really be a beneficial catalyst for equities, and so we feel like this understanding differentiates us from other active managers, especially in the midcap space, which is generally where our fund tends to reside. In this environment, where investors are being pitted against active versus passive investment options, we feel like this is an option that has a very strong track record.

We have also been able to show that we can mitigate risk. Looking back to early 2016, as well as even prior selloffs in the overall market, we have shown a strong risk-mitigation capability. That has really helped set this fund apart from many other equity strategies as a really interesting strategy. We feel like when companies utilize their balance sheets in an optimal way, then that is a catalyst that can play out regardless of what the rest of the market is doing. This really positions our fund well for the future.

TWST: Thank you. (KJL)

AQUILA THREE PEAKS OPPORTUNITY GROWTH FUND PERFORMANCE STATISTICS AS OF SEPTEMBER 30, 2017

	Cumulative Return			Average Annual Return							
	3rd Qtr 2017	YTD	1 year	3 year	5 year	10 year	Since Inception	Inception Date	Max Sales Charge	Max CDSC	Total Operating Expense
A Shares NAV	3.27%	12.49%	12.11%	8.88%	15.42%	6.68%	8.55%	7/22/94	--	--	1.40%
A Shares MOP	-1.11%	7.72%	7.35%	7.31%	14.42%	6.22%	8.34%	7/22/94	4.25%	--	1.40%
C Shares w/o CDSC	3.10%	11.90%	11.34%	8.10%	14.59%	5.90%	7.24%	5/1/96	--	--	2.11%
C Shares w/ CDSC	2.10%	10.90%	10.34%	--	--	--	--	5/1/96	--	1.00%	2.11%
I Shares	3.30%	12.59%	12.22%	9.05%	15.66%	7.03%	7.38%	12/01/05	--	--	1.37%
Y Shares	3.36%	12.75%	12.46%	9.20%	15.77%	7.00%	8.29%	5/01/96	--	--	1.11%
Russell 3000	4.57%	13.91%	18.71%	10.74%	14.23%	7.57%	--				

On October 8, 2010, Fund shareholders approved changes in the name, investment sub-advisor and investment strategy of the Fund. On October 15, 2010, the Fund began operations under the name Aquila Three Peaks Opportunity Growth Fund, with Three Peaks Capital Management, LLC as sub-adviser, and an investment strategy that differs meaningfully from the strategy pursued by the previous Fund. Performance prior to that date reflects the previous investment strategy of the Fund.

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. Performance current to the most recent month-end is available at: 800-437-1020 or www.aquilafunds.com. Class A shares have a maximum sales charge of 4.25%. Class A MOP returns reflect deduction of the maximum 4.25% sales charge; Class A NAV returns do not reflect deduction of the sales charge and would be lower if that charge were reflected. Class Y shares, which are available only through a financial professional, have no front-end sales charge or contingent deferred sales charge. Other classes of shares are offered and their performance will vary due to differences in sales charges and fees. Russell 3000 is an index representative of the largest 3000 US Companies. An investment cannot be made directly in an index.

This material must be preceded or accompanied by a copy of the Fund's current prospectus. Before investing in the Fund, carefully read about and consider the investment objectives, risks, charges, expenses, and other information found in the Fund prospectus.

Mutual fund investing involves risk and loss of principal is possible. Risks include, but are not limited to, potential loss of value, market risk, financial risk, interest rate and credit risk, and investments in highly-leveraged companies, lower quality debt securities, foreign markets and foreign currencies.

Definitions:

***Bond Covenants** are legally binding agreements between a bond issuer and a bond holder. Bond covenants can be restrictive, forbiding the issuer from engaging in certain activities, or they can require that the issuer meet specific requirements.*

***EBITDA** stands for earnings before interest, tax, depreciation and amortization and is a measure of a company's operating performance. It is a way to evaluate how a company is performing without having to take financing decisions, accounting or taxes into account.*

***CAGR** stands for compounded growth rate and is a measure of growth over multiple time periods.*

TOP TEN HOLDINGS as of 9/30/17

Republic Services Inc.	2.34%
Aramark	2.33%
Liberty Media Corp.	2.16%
Extended Stay America Inc.	1.99%
Viasat Inc.	1.84%
Cott Corp.	1.78%
Performance Food Group Co.	1.77%
Nielsen Holdings PLC	1.76%
Berry Global Group Inc.	1.74%
Crown Castle Intel Corp.	1.74%

Information regarding holdings is subject to change and is not necessarily representative of the entire portfolio. This is not a recommendation to buy or sell specific securities, and should not be considered investment advice of any kind.