Your Investments | September 2018

Greetings,

The US economy is on fire and the stock market is in full rally mode with the S&P 500 posting back-to-back 3%+ returns in the months of July and August. So much for "Sell in May."

Over the last several months we've discussed the many catalysts behind the ever improving domestic economic picture, including tax reform, deregulation, inflation, record low unemployment and increased consumer confidence.

So, with the March 2019 "Brexit" (Britain's exit from the European Union) deadline less than seven months away, we'll take a break from the US to examine the future of the Euro currency and what it means to our investment outlook.

Examining the Euro

The Euro currency launched in 1999, managed to avoid collapse in 2008 and survived the Greek crisis. But how sustainable is this currency long term?

According to Vanguard, the four biggest threats to the Euro are poor economic performance, large current account balances, rising and diverging debt levels, and negative attitudes towards Euro membership.

Economic Performance

Initially, the ECB was precluded by law from quantitative easing (QE), the process of introducing new money into the money supply by a central bank in order to stimulate the economy and make it easier for businesses to borrow money, such as the US did in 2008 and throughout the recent Great Recession. While the ECB eventually went to court and won the right to QE, it was nearly five years after the Fed began QE in the US. As a result, the US appears 3-4 years ahead of the Euro economic recovery. Measured by GDP growth per capita, only Germany has performed better than the US since the financial crisis. Several EU countries have suffered negative GDP growth per capita.

Large Current Account Balances

Germany has a large current account surplus, meaning it exports more than it imports. Countries like Italy, Spain, Portugal, Greece and Ireland have large current account deficits. Unfortunately, this has contributed to a loss of job opportunity for the young people in those countries, many of whom move abroad to look for work. These same forces are behind the US effort to tear down international trade barriers.

Rising Debt Levels

Debt to GDP (revenue) levels have skyrocketed in countries such as Greece, Ireland, Portugal and Spain. Weak economies and job losses in these countries exacerbate the problem. On the other hand, Germany, Austria, the Netherlands and Belgium have not seen much increase in debt to GDP over the last 20 years. Per Vanguard, Greece finds itself in a virtual debtor's prison, unable to default on its debt and forced into austerity while its young people flee for better opportunity elsewhere.

Negative Attitudes

Euro-sceptic attitudes run high in many countries, and indeed have become a political force as we saw with Brexit. The political risk (countries electing an anti-Euro government) could lead to contagion risk (other countries leaving).

Solutions

- Vanguard proposes several reforms which could save the Euro:
- Develop a European rescue plan to handle financial crises;
- Allow automatic budget stabilizers to increase public spending in downturns and decrease public spending in upswings;
- Establish a fiscal union with a new European treasury to direct fiscal policy;
- Establish a banking union with banking supervision, deposit insurance, common regulations and a resolution procedure; and
- Restructure Greek debt.

Prognosis

According to Vanguard, here are the chances of Euro survival:

	Next 5 Years	Next 30 Years
No Breakup	95%	60-70%
Partial Breakup	5%	20-30%
Full Breakup	<1%	10-15%

So what does this mean for the US? Any breakup would likely result in heightened market volatility in the short term. A full breakup would be a major financial event with far reaching consequences. However, the risk of an immediate Euro crisis is low. And to some extent, concerns about the Euro are already reflected in asset prices. We therefore do not believe Euro currency risk currently requires us to engage in a radically different investment approach.

KCM Macro Trends Fund – 10 Year Anniversary!

We are excited to announce that the KCM Macro Trends Fund (KCMTX) turned 10 years old on August 4! Not many funds survive this long, much less an alternative fund strategy. And unlike most alternative funds around today, we can say that we have successfully managed money during both bull and bear markets.

KCMTX has beaten 99% of its Morningstar Multi-Alternative Category peers based on total return for the one-, five- and ten-year periods ending August 31, 2018 out of 367, 160 and 51 funds respectively. KCMTX similarly outperformed 98% of the category's funds for the three-year period ending August 31 (out of 301).**

KCMTX also holds the 2018 Thompson Reuters Lipper Award for Best Alternative Global Macro Fund.***

To learn more about the Fund, please visit KernsCapital.com or contact Octavia Grimston at 713.993.0949

How Are We Doing?

The KCM Risk-Based Portfolios were flat in June (and on the year) due in large part to the disproportionately negative impact of tariffs on our international allocation; and no help from the bond market. We expect things to turn around very soon, as described above.

Model	August	YTD	1-Year
KCM Aggressive	3.51%	4.68%	18.21%
KCM Moderate	2.67%	4.33%	15.37%
KCM Conservative	2.23%	3.71%	12.75%
Morningstar Moderate Target Risk TR	0.88%	2.31%	7.36%
S&P 500 TR	3.26%	9.94%	19.66%
AGG Barclays Int Bond	0.57%	-1.11%	-1.26%

In Closing

The US economy continues to accelerate, and the stock market is advancing. After two exceptional months we're expecting a September pause in the markets; but would not be surprised to see another gain should global trade talks progress.

On a personal note, the Kerns had a great summer together with our son home from college. In August we vacationed in Cabo where my kids talked me into bungee jumping and a canyon swing that began with an 80-foot free fall. Crazy fun! But one and done.

In closing, we'll leave you with a few words of wisdom from Warren Buffet:

"You will continue to suffer if you have an emotional reaction to everything that is said to you. True power is sitting back and observing things with logic. True power is restraint. If words control you that means everyone else can control you. Breathe and allow things to pass."

Sincerely,

Marty Kerns
President & Chief Executive Officer

Parker Binion
Chief Investment Officer

Octavia Grimston
Investor Relations

About Kerns Capital Management

Kerns Capital Management is a leading asset management firm with a focus on quantitative, liquid alternative investment strategies, including the KCM Macro Trends Fund. We are value-oriented investors in long/short equity, credit and volatility, and apply the same attention to risk in the deployment of capital that has guided us since our inception as a fiduciary investment manager to corporate pensions, trusts and high net worth individuals. Kerns was founded in 1996, and is based in Houston, Texas.

For more information on our products, including fund performance or to sign up for this newsletter, please visit www.kernscapital.com or contact our Investor Relations director Octavia Grimston at 1.993.0949 x115 or ir@kernscapital.com

IMPORTANT DISCLOSURES

Performance data represents past performance and is not a guarantee of future results.
Performance current to the most recent month-end may be lower or higher, and can be obtained by calling 800-945-2125.

*Kerns Capital Management Risk-Based Portfolios. Performance figures, unless otherwise described, represent a composite of all individual portfolios managed in accordance with the investment strategy, include reinvestment of dividends and other earnings, and are after the deduction of all fees including KCM's advisory fee, brokerage or other commissions, and any other expenses that a client actually paid. Long-term capital appreciation is the primary objective of the models. As a secondary objective, the portfolios strive to preserve capital during bear markets. There is the possibility of loss. The composites contain accounts structured with mutual funds that are tactically managed with a view towards capital appreciation. Models generally included exposure to US and International equities, bonds, real estate, currencies and/or commodities.

Composites do not include 401(k) accounts which are managed differently due to Department of Labor rules.

Marty Kerns, KCM's Chief Compliance Officer, remains available to address any questions regarding this performance presentation, including its limitations. Mr. Kerns can be contacted via email at marty@kernscapital.com or toll-free at 800.945.2125.

** KCM Macro Trends Fund. Investors should carefully consider the investment objectives, risks, charges and expenses of the KCM Macro Trends Fund. This and other important information about the Fund is contained in the prospectus, which can be obtained at kernscapital.com or by calling 800.945.2125. Read the prospectus carefully before investing.
The KCM Macro Trends Fund is distributed by Northern Lights Distributors, LLC. Member FINRA/SIPC. Kerns Capital Management, Inc. and Northern Lights Distributors, LLC are not affiliated.

Morningstar Rankings. The KCM Macro Trends Fund (KCMTX) ranks in the top 1% of its Morningstar Multi-alternative category out of 367, 160 and 51 funds, respectively, for the one-, five- and ten-year periods ending August 31, 2018 based on total return. KCMTX also ranks in the top 2% out of 301 funds for the three-year periods ending August 31. Rankings are just one form of performance measurement.

Morningstar Ratings. The Morningstar RatingTM for funds, or "star rating", is calculated for managed products (including mutual funds, variable annuity and variable life subaccounts, exchange-traded funds, closed-end funds, and separate accounts) with at least a three-year history. Exchange-traded funds and open-ended mutual funds are considered a single population for comparative purposes. It is calculated based on a Morningstar Risk-Adjusted Return measure that accounts for variation in a managed product's monthly excess performance, placing more emphasis on downward variations and rewarding consistent performance. The Morningstar Rating does not include any adjustment for sales loads. The top 10% of products in each product category receive 5 stars, the next 22.5% receive 4 stars, the next 35% receive 3 stars, the next 22.5% receive 2 stars, and the bottom 10% receive 1 star. The Overall Morningstar Rating for a managed product is derived from a weighted average of the performance figures associated with its three-, five-, and 10-year (if applicable) Morningstar Rating metrics. KCMTX received ratings of five stars for both the three- and five-year periods as at July 31, 2018 out of 226 and 119 funds respectively
Morningstar Multialternative Category includes funds that have a majority of their assets exposed to alternative asset strategies, including long/short, and can include funds with static allocations to alternative strategies and funds tactically allocating among alternative strategies and asset classes.

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*** Source: Lipper, Inc. The Best Alternative Global Macro Fund award is granted to the fund in the Alternative Global Macro category with the highest Lipper Leader score for Consistent Return over the 5-year period as of 11.30 of the prior year. Lipper awards are granted annually to the funds in each Lipper classification that achieve the highest score for Consistent Return, a measure of funds' historical risk-adjusted returns, relative to peers. Thomson Reuters Lipper Awards, © 2018 Thomson Reuters. All rights reserved. Used by permission and protected by the Copyright Laws of the United States. The printing, copying, redistribution, or retransmission of this Content without express written permission is prohibited. Lipper, a wholly owned subsidiary of Thomson Reuters, is a leading global provider of mutual fund information and analysis to fund companies, financial intermediaries and media organizations.

The S&P TR 500 Index is an unmanaged composite of 500 common stocks. This index is widely used by professional investors as a performance benchmark. Total return includes reinvestment of dividends. You cannot invest directly in an index. The Dow Jones Industrial Average is a price-weighted average of 30 of the largest and most widely held stocks traded on the New York Stock Exchange and the Nasdaq. The Nasdaq Composite Index is a market-capitalization weighted index of the more than 3,000 common equities listed on the Nasdaq stock exchange. The types of securities in the index include American depository receipts, common stocks, real estate investment trusts (REITs) and tracking stocks. The iShares Core U.S. Aggregate Bond Index is an ETF (AGG) that seeks to track the investment results of an index composed of the total U.S. investment-grade bond market. The Morningstar Moderate Target Risk Index is based on a well-established asset allocation methodology from Ibbotson Associates, a Morningstar company and a leader in the field of asset allocation theory. The securities selected for the asset allocation indexes are driven by the rules-based indexing methodologies that power Morningstar's comprehensive index family. Morningstar indexes are specifically designed to be seamless, investable building blocks that deliver pure asset-class exposure. Morningstar indexes cover a global set of stocks, bonds, and commodities.