Bluestone CAPITAL MANAGEMENT

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Bluestone Elite - Strategy Commentary

3rd Quarter - 2015

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We apologize that this quarterly commentary is being released later than usual. We're sure you understand why that is the case given all of the volatile movement in the markets and the fact that our team must remain focused primarily on the markets during times of heightened volatility. The third quarter of 2015 was a definite wake-up call for investors as the broad markets experienced the most significant sell-off since 2011. Fears of a global deflation, a Chinese market crash, slumping commodity prices, and some weak domestic economic data all contributed to the dramatic and panicked selling that saw the S&P 500 decline just over 12% from a high of 2,128.28 on July 20th to a low of 1,867.61 on August 25th. During that time, the volatility index as tracked by the VIX spiked over 300% to 40.74. The volatility didn't stop there, however, as the markets tried to resolve conflicting macro data with the prospect of a Fed rate hike looming, volatility remaining elevated and selling pressure continuing.

The Bluestone Elite strategy made several tactical moves during the 3rd quarter aimed at providing protection during these volatile market movements. The first tactical move we employed was a significant increase to our cash position. On Friday August 21st, after a decline in the S&P 500 of 7% off of its July 20th high, we trimmed exposure from most of our core holdings to double our cash position from 8% to 16%. This move helped protect the portfolio as the Dow opened down almost 1,000 points on Monday August 24th, and the S&P sold-off a further 5% through Tuesday August 24th. At the same time, we decided to increase our exposure to gold as a defensive hedge. This position, while not as beneficial as the cash allocation, did reduce the beta of the portfolio and provided some volatility protection in that high fear environment. In addition to these more significant actions, we also increased our allocations to financials, mainly by taking individual positions in several of the banks that we feel are best positioned to take advantage of rising interest rates. Due to the fact that the financial sector has largely underperformed the markets in aggregate over the past few years and is relatively fairly valued when compared to the S&P 500 as measured by P/E ratio, we felt that adding exposure here was prudent both as a beta reduction strategy and as a long term value play. Given our expectations of long term interest rate increases and expected regulatory relief in the form of additional capital flexibility, we expect these banks to be able to increase both their net interest margins and fee revenue, as well as begin to return more capital to shareholders in the form of both buybacks and dividends. These positions brought our total financial exposure to 18.5% of the portfolio; a slight overweighting as compared to the S&P 500's financial exposure of 16.6%. Rounding out our more

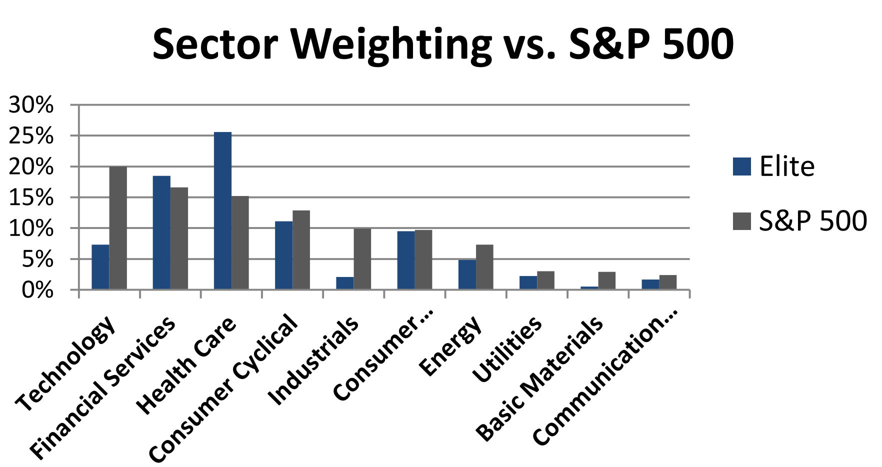

Figure 1 - (Bluestone Elite vs S&P 500)

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significant tactical decisions, we also increased our allocations to the consumer staples and consumer cyclical sectors. Given the steadily decreasing unemployement numbers, increasing wage pressures, and increases in real estate values, we believe the fundamentals of the US labor market are sound and that US consumer demand will be strong throughout the 4th quarter and into 2016 as consumers continue to increase their spending power and leverage cheap credit.

As our long term investors know, we believe the underlying fundamentals of the healthcare sector remain strong given its wide moat, high margins, and strong demographic driven demand in conjunction with an aging population. Unfortunately, these facts turned out to be immaterial in the short term as a tweet by democratic presidential candidate Hilary Clinton and a widely published news story on drug prescription prices sparked a dramatic decline in stock price for many of the largest pharmaceutical companies that dragged down the whole sector. Valuations had been elevated in healthcare early in the year (see figure 2 - right), which gave long term investors a reason to take profits and short term momentum traders a reason to exit the sector. Considering the fact that healthcare continues to be our most overwight holding, this position definitely hurt our third quarter performance, but healthcare is still outperforming the S&P 500 year-to-date and we anticipate this sector's long term trend continuing to improve the risk adjusted returns for our investors.

Figure 2 - Ratio of Price to Morningstar Fair Value (Healthcare Sector)

There are still significant headwinds in the global economy and some faltering domestic economic indicators that leave us cautious of further volatility and potential declines in US equities. With that being said, we remain focused on the long term, and we try to remind our investors to do the same. We maintained a 15% cash position through the end of the quarter as both a buffer to the increased volatility and to provide the ability to capitalize on any potential buying opportunities as well as any indication that the heightened uncertainty surrounding the global economy was abating. This decision turned out to be a prudent one, as the healthcare sector saw its most dramatic selloff in years and the S&P tested its August lows again in late September.

Looking ahead, we believe that the Bluestone Elite strategy is well positioned with a reduced risk profile, significant upside potential in the form of both earnings increases and multiple expansion of the underlying positions, and a significant cash position to deploy when the opportunity presents itself.