

A Closer Look at Vice Fund's Defensive Qualities

Defensive: "Serving to defend or protect." – Merriam-Webster Dictionary

Consumer staples like tobacco and beverages are widely considered to be defensive, which means that they are generally thought to be uncorrelated with moves in the broad equity market. The aerospace and defense sector, too, is more directly tied to budgetary cycles than fluctuations in the economy, and the stocks of defense contractors also aren't very linked to moves in the broader market.

To put some data behind it, the investment firm Sanford Bernstein put out a research report a few weeks back quantifying the aerospace/defense sector's low correlation to the S&P 500. The report's conclusion is that, "Over the last 20 years, pure-play defense stocks have had almost no correlation with the S&P 500, although in the period from 1962 to 1983, the correlation was significant. The reason for the higher correlation in the 1960s and 70s was the fact that US defense spending was an important driver of the overall economy, representing 6% to 9% of GDP in that period – it is not today, with spending only at 3% to 4% of GDP." ¹

As for tobacco, in light of the recent market hysteria, UBS put out a note last week looking at how the tobacco sector has fared in periods of high volatility. According to UBS, there have been 1,336 days since 1997 when the CBOE Volatility Index, or VIX, an index that measures volatility, has closed above 20; over those days, tobacco stocks gained 12.5% while the S&P 500 declined 39.2%. ²

What does this mean? In simple terms, a fund focused on the aerospace/defense, tobacco and beverages sectors has elevated defensive characteristics, which can be a good thing in uncertain times. As you know, in addition to these three areas of the market, the Vice Fund also focuses on the gaming sector, which, in stark contrast to the others, is characterized by higher growth, higher beta, and little or no dividends to speak of. But, like the rest of our target sectors, demand for gambling is pretty resistant to fluctuations in the economy; consumers continue to wager more and more every year. ³

So with the Vice Fund, we have a fund dedicated to economically independent growth. It's defensive, no doubt, but with a growth component to it as well.

That's nice on paper, but the recent sub-prime crisis has been a real test of the Vice Fund's defensive qualities.

Thus far, the Vice Fund has fared well this year despite the recent headlines, and we believe that it is well positioned to continue to do so because: (1) the defensive nature of the Vice Fund's core areas of focus; (2) its strong international component, with nearly thirty percent of its net assets invested in foreign companies; and (3) our short exposures.

As the sub-prime mess continues to unfold, we believe that there are benefits to be derived from investments in defensive sectors. From our perch, there's never been a better time to be a Vice Fund investor.

¹ Bernstein Research, "Aerospace & Defense: Defense as a Defensive Play - Low Broader Market Exposure, Strong Near/Medium Term Outlook," Douglas S. Harned, Aug. 7, 2007

² UBS Securities LLC, "Best Offense is a Good Defense," Nik Modi, Aug. 15, 2007

³ American Gaming Association
(http://www.americangaming.org/Industry/factsheets/statistics_detail.cfv?id=8)

Please see page 2 for important disclosure information.

Mutual fund investing involves risk; principal loss is possible. The Fund is nondiversified, meaning it may concentrate its assets in fewer individual holdings than a diversified fund. Therefore, the Fund is more exposed to individual stock volatility than a diversified fund. The Fund invests in foreign securities which involve greater volatility and political, economic and currency risks and differences in accounting methods. The Fund also invests in smaller companies, which involve additional risks such as limited liquidity and greater volatility.

Opinions expressed are those of Charles Norton, and is not intended to be a forecast of future events, a guarantee of future results, nor investment advice.

The S&P 500 Index is a broad based unmanaged index of 500 stocks, which is widely recognized as representative of the equity market in general. You cannot invest directly in an index. Dividend yield: Annual percentage of return earned by an investor on a common or preferred stock, calculated by dividing the annual dividend per share by the current market price per share of the stock. Beta: A standardized measure of systematic risk based upon an asset's covariance with the market portfolio. A beta above 1 is more volatile than the overall market, while a beta below 1 is less volatile. Correlation: A measure of the relationship between two variables.

The funds' investment objectives, risks, charges and expenses must be considered carefully before investing. The prospectus contains this and other important information about the investment company, and it may be obtained from www.vicfund.com, or by calling Shareholder Services toll free at 866-264-8783. Read it carefully before investing.

Quasar Distributors, LLC, distributor. (08/07)