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WeatherStorm Forensic Accounting Long-Short Index (FLAGLSX) Quarterly Rebalance Review September 2017

WeatherStorm – A Vident Group of Companies – an alternative asset management company, undergoes quarterly rebalance of their long-short index strategy.

WeatherStorm Forensic Accounting Long-Short Index (FLAGLSX) seeks to enhance investors' U.S. large cap exposures by offering a long-short portfolio with full participation in the U.S. market beta while providing additional alpha potential through the careful and systematic selection and shorting of stocks based on forensic accounting analysis.

Forensic accounting is the process of critically dissecting companies' financial statements with the goal of identifying the "red flags" of aggressive accounting and revenue recognition practices. While Generally Accepted Accounting Principles (GAAP) are standardized, managers have wide latitude in interpretation. Some managers, highly incentivized to produce stock performance, will use the accounting levers at their disposal to boost short-term results at the cost of future performance. The Forensic Accounting Long-Short Index seeks to distinguish between such companies to the benefit of investors.

Rebalance Goals:

The rules-driven objective quarterly reviews ensure the index continues to accurately reflect Vident and WeatherStorm's principles-based methodology and form an essential component of the index management. The rebalance serves to update the portfolio to reflect changes in market opportunities and risks. Positions which have grown in size are reduced to decrease company concentration risks. Rebalance changes are also driven by forensic accounting assessments as each company's latest financial statements are incorporated and assessed for risks.

Outcomes of Current Rebalance

With the goal of expanding the opportunity set for picking stocks, the current rebalance saw the universe of available stocks increased from the top 500 largest US stocks to the top 1000 largest US stocks. Doing so allowed the average company forensic accounting & valuation score to improve nearly 50% as there were more stocks to choose from to go long or to sell short. In addition to the expansion of the strategy's investable universe of stocks, risk management objectives were – as always – also considered in the rebalance. Concentration risks were reduced; strong performing stocks which had grown in allocation were trimmed back. Active sector risks were also reduced and the portfolio's 130/30 exposure limits were realigned. In total, turnover this rebalance was 65% - higher than usual, resulting from the one-time move to the larger universe of eligible stocks.

Resulting from the expanded universe of eligible stocks for the strategy, the mid-cap exposure of the fund increased through this rebalance. Prior to the rebalance, mid-cap stock exposure stood at about 12% of the portfolio. After the rebalance, it now stands at around 41%. Despite the shift in market capitalization, the fund remains highly liquid, with all positions in the portfolio representing less than 1% of each stocks' average daily trading volume.

Also notable this rebalance was the improvements in the average dividend yield. On the long side, the average holding's dividend yield rose from 2.50% to 2.66%, while on the short side the average company's dividend yield fell from 1.21% to 1.11%. Since dividends on the long side accrue to the fund, while on the short side they must be paid by the fund, these improvements on both sides are helpful to the FLAG investor.

About WeatherStorm Capital

WeatherStorm Capital is a subsidiary of [Vident Financial](#) that provides all-weather investment strategies that combine deep investment research with thoughtful systematic portfolio design and risk management. WeatherStorm provides alternative investment solutions that are broadly classified into two categories: investments across asset classes designed to deliver absolute returns, and single asset class solutions designed to deliver superior risk adjusted return over respective benchmarks.

A link to the full methodology can be found [here](#).

All changes from this review were implemented at the close of business Friday, September 29, 2017 and take effect from the start of trading on Monday, October 2nd, 2017.

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