SHELTON CAPITAL MANAGEMENT

Shelton Tactical Credit Fund

Quarterly
Commentary
As of March 31, 2023

Market Commentary

When the calendar flipped from 2022 to 2023, the clean-slate rally began in earnest. People put the challenges of 2022 in the rearview mirror, and the weakness over the last few weeks of December made starting valuations look cheaper, offering an even more attractive entry point. Lower credit quality bonds significantly outperformed as the risk-on momentum gathered speed. Unfortunately, the speeding car hit a speed bump in early February when markets were reminded that the fight against inflation was still raging, and interest rates re-accelerated from a low of 3.36% in mid-January to 4.05% in early March. The sharp increase in rates exacerbated underlying challenges in the banking system that had been percolating under the surface, as deposit flight from a few banks forced crystallizing of unrealized losses to fund these outflows. Ultimately, Silicon Valley Bank and Signature Bank succumbed to the pressure and were seized by regulators, triggering shudders throughout the small and mid-sized banking system. The Federal Reserve stepped in with new emergency lending programs including the Bank Term Funding Program (BTFP) to allow banks to borrow against underwater bond portfolios and avoid crystallizing further losses. Markets hunted for the next domino, bouncing from First Republic to PacWest and others. The shock waves reverberated across the Atlantic, forcing Credit Suisse into the arms of UBS in a deal brokered and backstopped by Swiss regulators, and investors pushed Deutsche Bank towards the brink as well.

Ultimately, calm was restored, at least for the moment. Economic data continued to be mixed, but the general trend seems to be a reacceleration of inflation in Q1 after what may have been false hope during the last few months of 2022. The key question on our minds is how much of an impact the stress in the small and midsize banking system will have on the economy. At the peak of tension in early March, significant rate cuts were being priced in during 2H 2023. A few weeks later, as of 3/31/23, the curve has moderated and shows a terminal rate of 4.96% and only ~2 rate cuts in Q4. The incoming economic data over the coming months will determine whether the reacceleration of inflation was temporary and then overwhelmed by the dislocation, or resilient and requiring additional rate hikes to conquer inflation, once and for all. Ultimately, we still believe the Fed will overtighten, either with higher-than-expected terminal rates or by holding rates elevated for longer, because they are more comfortable with the tools for stimulating the economy out of a recession than they are with fighting inflation that becomes entrenched. Therefore, we believe the landing will be harder than most expectations, an economic recession and most certainly an earnings recession is coming, just brought forward sooner by the incremental tightening of financial conditions. Small and mid-sized companies have been the economic engine of the economy over the last few years, driving significant employment gains; these companies will be the ones disproportionately affected by the challenges of regional and community banks, as those are their primary source of capital for operations and growth.

The Fed continued the rate hike cycle with 25 basis points in February and another 25 basis points in March. At their March meeting, the Fed updated their Summary of Economic Projections to show 0.4% real GDP growth in 2023 and 1.2% in 2024, an unemployment rate of 4.5%, and core PCE inflation of 3.6%, slightly higher than the 3.5% from December. Previous Fed Funds rate estimates from December were unchanged at 5.1% for 2023 and revised from 4.1% to 4.3% in 2024. Forward market expectations have oscillated and are currently (as of 3/31/23), anticipating less than 25 basis points in remaining hikes by June 2023, with rate cuts beginning in the second half of 2023, a significant divergence from FOMC forecasts. 10yr US Treasury yields began the quarter at 3.87%, reached an intra-quarter low of 3.37% on January 18th, then sold off and reached a high of 4.06 % on March 2nd before ending the quarter at 3.47%.

We continued to position the portfolio by reducing lower credit quality issuers that we believe are less recession resilient and adding longer-duration high quality bonds such as investment grade municipal and corporate bonds. We believed all-in yields on these high-quality bonds were compelling, and we wanted to ensure that our borrowers will undoubtedly be able to pay us all interest and principal due throughout a recession. Adding these longer maturity bonds had the effect of increasing the duration of the portfolio, as we believed that intermediate and longer-term interest rates would peak and start to decline. This positioning served us well in the quarter and should continue to do so in the months ahead. As of quarter-end, BBB-rated investment grade bonds are yielding 5.5%, BB rated bonds are yielding 6.8%, and investment grade municipal bonds are yielding 3.25% (approximately X% on a federal income tax adjusted basis). Even if credit spreads widen into a recession, the risk-free component will likely go lower from here, pushing potential total returns above 10% over the next 6-12 months.

Our conscious decision to move the portfolio up in quality to be more recession resilient may have been slightly premature when CCCs rallied hard early in the year but proved to be prudent when the turmoil of March bubbled-up. We also changed the composition and weightings of the portfolio more heavily towards corporate bonds and less municipal bonds in order to take advantage of higher interest rates and increase the yield component of our total return portfolio. 2023 may be a difficult year to capture spread tightening, and hence capital price appreciation, if the economy slows, so we purposefully want to clip coupons in the meantime and capture the move lower in rates through duration.

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Portfolio Management

Peter Higgins
Head of Fixed Income & Sr. Portfolio Manager

Peter Higgins has over 25 years of experience in fixed income investing, most notably as Partner and Lead Portfolio Manager at both Ares Management and BlueBay Asset Management. Previously, Peter specialized in global leveraged finance at investment banks such as Deutsche Bank AG, Goldman Sachs & Co. and Credit Suisse in both London, England, and New York City. Peter earned a bachelor's degree in Economics-Political Science from Columbia University.

Jeffrey Rosenkranz
Portfolio Manager

Jeffrey Rosenkranz has 25 years of experience investing in the credit markets, with an emphasis in high yield, distressed debt, and special situations and has worked at firms including Cedar Ridge Partners, LLC, Durham Asset Management, Cooperstown Capital Management and Ernst & Young LLP. He holds an MBA from the Stern School of Business at New York University and a B.A. from Duke University. He is also a Certified Public Accountant.

David Falk
Portfolio Manager

David Falk has over 30 years of broad-based fixed income experience as a trader, research analyst and investment banker for firms including Cedar Ridge Partners, LLC, Bear, Stearns & Co. Inc. and Lazard Freres with a focus on the municipal securities market. He is also a Portfolio Manager for the Green California Tax-Free Income Fund and fixed income managed accounts. He holds a Master of Regional Planning from the University of North Carolina at Chapel Hill and a B.A. from Northwestern University.

William Mock
Portfolio Manager

William Mock has 24 years of experience as a trader and portfolio manager of fixed income and derivatives portfolios, working at Citibank, Societe Generale, and TKI Capital prior to joining Shelton Capital in 2010. He is also lead portfolio manager of Shelton Capital's other municipal and government bond mutual funds. William holds a B.S. in Electrical Engineering from Kansas State University and an MBA from University of Chicago Booth School of Business.

Chris Walsh
Portfolio Analyst

Chris Walsh has over seven years of experience analyzing credit and equity markets. He has been with Shelton Capital since November 2016. Chris earned a B.A. in Economics, Villanova University.

1Q 2023 Shelton Capital Management: Fixed Income Commentary

In Q1 the Fund generated returns of +0.48% (DEBIX) and +0.38% (DEBTX). Below are our relative returns for the quarter and full-year periods. This quarter - one high yield municipal bond position experiencing a significant decline in price in January detracted from performance. Aside from this unfortunate event, the rest of the portfolio outperformed the relevant indices. Our longer-term performance remains very strong and is a testament to our ability to overcome occasional idiosyncratic hiccups because we have proven our ability to string together significantly more idiosyncratic winners than losers. We feel this is well evidenced in our 3-year performance of 7.18% (10th percentile) and our upside/downside capture ratio of 120%/15%, as of 3/31/23.

In Q1 the Fund generated returns of +0.48% (DEBIX) and +0.38% (DEBTX). Below are our relative returns.

	1Q23	YTD	1YR	3YR	5YR	Since Inception
Shelton Tactical Credit Fund (DEBIX)	0.48%	0.48%	-3.83%	7.18%	2.32%	3.15%
Bloomberg U.S. Aggregate Bond Index	2.96%	2.96%	-4.78%	-2.77%	0.90%	1.66%
Bloomberg U.S. Investment Grade Corporate Bond Index	3.50%	3.50%	-5.55%	-0.54%	1.62%	2.67%
Bloomberg U.S. High Yield Corporate Bond Index	3.57%	3.57%	-3.34%	5.91%	3.21%	3.97%
Bloomberg U.S. Investment Grade Municipal Bond Index	2.78%	2.78%	0.26%	0.35%	2.03%	2.88%
Bloomberg U.S. High Yield Municipal Bond Index	2.73%	2.73%	-4.49%	2.72%	3.07%	4.68%
Morningstar Nontraditional Bond Fund Category	1.54%	1.54%	-2.45%	2.57%	0.98%	1.33%

Performance figures represent past performance and are not a guarantee of future results. The investment return and the principal value of an investment will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost; current performance may be lower or higher than the performance data quoted. For more current month-end Fund performance information, please call our office at (800) 955-9988.

Portfolio weightings were higher in corporate bonds and lower in municipal bonds. We also reduced the amount of short positions in acknowledgement of the higher cost of carry and delayed onset of a recession Within municipal bonds, we increased the investment grade allocation and reduced both the floating rate short term component and the high yield municipal bond portions of the portfolio.

Corporate bond long positions were strong positive contributors to performance on account of credit selection and avoidance of downside surprises. Most positions were positive contributors. The lower the quality and shorter the duration, the stronger the return performance in the quarter generally given the risk on rally in January and the interest rate moves intra-quarter. We struck a good balance between prudent credit selection in single B credits we believe are underappreciated by the market and rating agencies, while avoiding weak single Bs and CCCs which will be punished in a downturn. Talos closed their acquisition of EnVen Energy announced at the end of September, and we expect the combined company to refinance both bonds which will be a catalyst for additional total return performance.

The borrowers in our portfolio reported solid Q4 earnings generally across the board, reinforcing our decision to upgrade the quality of the portfolio in the face of cost pressures and an economic slowdown. There was a little bit of single-name outperformance where strong earnings were applauded. We expect this dispersion where strong performance is rewarded, and poor performance is penalized will accelerate going forward. Issuers that materially miss earnings, call off corporate transactions, or otherwise disappoint their investors will be severely punished.

Most of the municipal bonds were also positive contributors as rates declined and market technicals provided a nice tailwind. Higher coupon/shorter duration investment grade bonds added to performance but underperformed the rally.

Our methodical and tactical approach to interest rate hedging contributed positive performance as well, while also serving to moderate volatility and allow us to position the portfolio to capture higher yields.

The top 5 contributors and detractors for the quarter are listed below:

Top 5 Contributors	**Top 5 Detractors**
PetSmart Inc.	CalPlant I LLC
AerCap Holdings NV	Pyxus International Inc. (term loan)
Guitar Center Inc.	Northrup Grumman Corp.
Pyxus International Inc.	Titan International Inc.
Iron Mountain Inc.	JBS USA

Corporate Commentary

Corporate bonds were shot out of a cannon in January, only to fall back to earth for most of February and early March, before bouncing off the safety net with a late March rally. Investment grade funds had an overall quarterly inflow of $11.5 billion, while high yield suffered an outflow of $25.2 billion. Investment grade new issuance remained disappointing, as supply totaled $404 billion, down 13% from Q1 2022, while High Yield issuance remained anemic, with bond sales of only $45 billion, down from last year's paltry $53 billion and down 75% from the $178 billion of Q1 2021. Of the $45 billion issued, over 70% was for refinancing or repayment of debt, a trend we expect to continue.

Many sectors are seeing year-over-year declines in margins as they lap a year bolstered by stimulus checks and the initial post-pandemic rebound, which may have pulled forward some demand and now the payback has arrived. This has shown up somewhat in credit metrics with leverage in the HY universe ticking upwards sequentially following six quarters of declines. However, coverage metrics remain strong and improved to a record high in the quarter (JP Morgan).

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Corporate Commentary (continued)

Generally, a few themes seem evident in high yield: corporate fundamentals remain solid after years of refinancing and terming-out at low rates, the yields currently offered by high yield bonds are relatively balanced versus the macro risks, and that investors should look first to quality but also search through lower quality buckets for idiosyncratic outperformance. How much pain will continue into the second quarter as the Fed is hiking in the face of markets? Dislocations may prove attractive entry points at all-in yields close to double digits.

We plan to continue to search for names that have been neglected or miscategorized by the market, and, as always, apply a contrarian mindset in trading. With rates having risen steeply, many higher quality (generally longer duration) names are trading at steep dollar price discounts to par. We like the safety here with the added optionality to the upside if there is some sort of event leading to a takeout at par.

Dealers continue to be very cautious in the amount of capital they are willing to commit to supporting markets and providing liquidity. While they had been net-short for much of 2022, during the latter portion of the fourth quarter this reversed to a modest net long position. Things have not improved much in Q1. This dearth of liquidity has exacerbated price swings and contributed to volatility both in rallies and selloffs. However, when the market had turned, the combined effect of dealers needing to cover their net short position and build inventory at the same time that investors are gathering inflows and needing to put those dollars to work has produced a few turbocharged rallies, even if they were short-lived. We have fully taken advantage of our tactical mandate and agility to trade around these bouts of volatility and enhance returns. We will continue to stay disciplined and opportunistic, identifying compelling opportunities in complex, out-of-favor, misunderstood credits, many of which are going through secular or regulatory changes or have cycles that are not aligned with the traditional economic cycle.

Municipal Commentary

For the full quarter, municipal market performance was positive with both investment grade (2.73%) and high yield (2.73%) tax-exempt bonds putting up solid returns. But it was a roller coaster ride getting there. Treasury market volatility was not ignored by municipal market participants as tax-exempts rallied in January, sold off in February, then rallied again in March. The table below shows the change in AAA municipal yields in basis points across the curve during the quarter.

Maturity	January	February	March	Full Quarter
2 Years	-50	78	-54	-26
5 Years	-44	53	-42	-33
10 Years	-40	40	-36	-36
30 Years	-33	37	-29	-25

From a relative value perspective, tax-exempt bonds continued to be historically rich relative to Treasuries across the curve and especially at the shorter end. AAA Muni/Treasury ratios ended the quarter at 59%, 62%, 65% and 90% in the 2-, 5-, 10-, and 30-year maturities. Direct retail and Separately Managed Account demand provided strong market support with trading desks reporting robust daily net retail buying throughout much of the quarter. This retail demand particularly helped at the shorter parts of the curve which is the traditional focus of retail and SMA interest. However, retail also began reaching a bit further out the curve searching for more yield this quarter. Tax-exempt fund flows were negative for the quarter with total outflows of $1.733 billion, consisting of $1.372 billion of outflows from open-end funds and $361 million of outflows from ETFs. This is a modest aggregate outflow relative to the beatdown of calendar year 2022. Mutual fund selling in the quarter seemed to be driven by credit, sector, and duration adjustments rather than a pressing need to satisfy investor redemptions. Further supporting overall market performance was the very limited new issue supply. First quarter issuance totaled only $74 billion – 29% less than in 2022. New tax-exempt deals totaled $63 billion, down 23% from 2022 and taxable issues totaled only $11 billion, down 50% from the prior year.

Something particular to take note of this quarter was how the municipal markets remained wide open for the business during the market-shocking Silicon Valley Bank failure, government response and related concerns over potential wider financial institution systemic stress. There was no rush to the exits by fund investors and new issues continued to come to market. While bid/offer spreads widened a bit indicating some dealer risk aversion during a period of uncertainty, overall secondary market trading continued unabated. In addition, market participants quickly concluded that there was not likely to be a near-term “fire sale” of municipal bonds from the SVB or other regional bank portfolios that would overwhelm the tax-exempt market and cause significant price declines. Our current view is that when any municipal position selling from SVB, or other might occur, the market will be readily able to absorb it --- especially if the level of new issue supply remains moderate.

We anticipate the tax-exempt bond market will continue to take much direction from the overall rates markets. Stability in rates, following an end to the FOMC hiking cycle and pause should be supportive of fund flows and municipal bond performance. At the same time, as the economy continues to slow, the credit quality of municipal bonds relative to corporates should continue to gain attention as a safe place for fixed income investors which will further support demand. We anticipate that our municipal portfolio will continue to be biased toward investment grade credits in solid general obligation and essential service revenue bond issuers that will perform well during a stressful economic environment.

Outlook

We thought that the Fed was well on its way to winning the battle on inflation, despite a temporary re-acceleration in the data recently. We know that policy operates with a lag, and as the housing market slowdown rolls through the data in coming months, this progress would be evident. The turmoil in the regional banking system will exacerbate the tightening of financial conditions and bring about a more pronounced slowing of the economy. Because the Fed is more comfortable running the playbook of re-stimulating an economy out of a recession rather than trying to re-conquer entrenched inflation, we fully expect them to try and keep financial conditions tight for longer, and over-correct in the process.

Much progress has been made on supply chains and bottlenecks, morphing from the challenge of too little inventory over to a surplus of inventory or supply in certain circumstances. Plummeting freight rates and other concurrent indicators of shipping demand indicate at least a pullback from exuberant strength if not a more pronounced slowing of the economy. Recent corporate commentary continues to signal the onset of economic contraction.

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Outlook (continued)

Consumers who faced unprecedented increases in food, energy and broader goods and services subsidized those expenditures with stimulus, savings from not consuming services during the pandemic, and wage growth from the exceptional strength of the labor market. The housing market has started to roll-over, as home prices peaked last July and have declined steadily since mortgage rates exceeded 7%. How long and deep this impending recession might be is the next key question. If it turns out to be more severe, equities and lower-quality fixed income have more downside. However, in the case of fixed income, given where all-in yields are now, we believe they are adequately compensating investors for additional spread widening all the way down to the single-B rating tier. Below single-B you better get your credit analysis and downside protection correct, as the lack of trading liquidity in that tier severely punishes mistakes.

Fourth quarter earnings season was a mixed bag overall, and delineated companies who have pricing power or moats around their businesses versus those whose products or services are discretionary to the point of unnecessary in a slowing economy, or at least not worth paying-up for. The result was a wide range of gross margin performances. Over the coming months we look for economic data to build a trend of slowing economic activity and lower inflation readings. Commodity prices and goods prices have been signaling this for several months. Whether or not services prices and the labor markets follow is the key. While job openings have started to decline, measures of participation and the number of people seeking jobs remains muted. Likely the Fed needs to push the unemployment rate close to 4.5% to achieve its objectives. This would allow the Fed to be less aggressive on forward guidance and actual rate hikes, which we believe could be a catalyst for a rate rally. However, if the Fed believes they need to keep interest rates higher for longer, more damage will be inflicted on corporate earnings. Estimates would be revised lower and create bouts of volatility as corporate fundamentals deteriorate, and cause credit spreads to widen.

We believe the sweet spots for future total returns are Investment Grade municipal bonds, and BBB, BB, and certain single-B corporate bonds we believe are stronger and more resilient than the market. Mathematically, even if spreads widen a few hundred basis points further, BBs at yields of 6.8% would still produce acceptable returns over the next 6 – 12 months. If rates go lower and/or the recession proves to be milder, then total returns could easily eclipse 10% over that time period. There are valid reasons to believe spread widening might stop short of previous recessions, as the index has a higher quality composition (more BBs, fewer CCCs), beginning all-in yields are higher than the onset of a typical recession, and the average dollar price of bonds is much lower and much closer to recovery rates. However, if spreads were to blow-out to levels above +800 basis points that are often reached in severe recessions, total returns would likely be flat or even negative. Navigating these bouts of volatility by adjusting credit quality overall and selecting the right individual securities will be the keys to success, and we are confident in our ability to thrive in such an environment.

As always, we will be cognizant of valuations, while continuing to seek value and compelling risk/reward investments across fixed income products with a focus on the corporate and municipal bond markets.

IMPORTANT INFORMATION

Investors should consider a fund's investment objectives, risks, charges and expenses carefully before investing. The prospectus contains this and other information about a fund. To obtain a prospectus, visit www.sheltoncap.com or call (800) 955-9988. A prospectus should be read carefully before investing.

Credit-related instruments typically decrease in value when interest rates increase. Concentration in a small number of issuers increases the risk that one issuer could have a large adverse impact on the Fund's return. Borrowing and frequent trading could increase the Fund's operating expenses. High-yield bonds involve greater risk of default, and may be more volatile and less liquid, than investment grade securities. Subordinated and unsecured loans may be disproportionately affected by default and downgrade. Foreign investments may be adversely affected by currency fluctuations, lower liquidity, tax regulation, and political instability. Derivatives can be highly illiquid and difficult to unwind. The Fund's short positions may equal up to 100% of the Fund's net asset value. Short sales theoretically involve unlimited loss potential since the market price of securities sold short may continuously increase. The Bloomberg Barclay U.S. Aggregate Bond Index is an unmanaged index of the U.S. dollar-denominated investment grade fixed-rate taxable bond market. It includes government, corporate, mortgage-backed, and asset-backed debt securities with a maturity of at least 1 year. It is not possible to directly invest in an index.

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