FS INVESTMENTS®

Monthly commentary

April 2023

FS Chiron Capital Allocation Fund

Class I: CCAPX

Strategy AUM[1]: $1.10 billion

Performance insights

The fund returned -1.41% in April, underperforming its blended benchmark, which gained 1.10%.[2] The fund's equity exposure detracted from return, while its fixed income and precious metals-related investments each contributed to performance.[2]

- **Defensive sectors lead.** Holdings in the consumer staples, health care and utilities sectors contributed to return during April. Despite a positive month for equities overall, defensive leadership showed a more cautious mood among investors.[2]
- **Technology stocks lag.** Holdings in the technology sector were the largest detractors from performance last month. Semiconductors bore the brunt of the declines, as the Philadelphia Semiconductor Index recorded its second-worst month relative to the S&P 500 since 2019.[2]
- **Developed ex-U.S. holdings contribute.** The fund's stock holdings in developed markets outside the U.S., where it is now underweight, added to return in April. The MSCI EAFE outperformed both emerging markets (EM) and the S&P 500 as bank and energy stocks recovered.[2]
- **U.S. stocks detract.** The fund's allocation to U.S. equities, where it continues to hold a modest underweight, detracted from return as holdings in the financials and technology sectors drove downside.

Positioning

- **Reducing equity beta.** We reduced the fund's equity beta during the month, consistent with our view that recent market strength will give way to a more challenging environment for risk. We expect our equity weight to continue to decline in the coming months as the market internalizes the reality that corporate fundamentals are unlikely to improve in the second half of the year.
- **Retain overweight in EM.** While we trimmed the fund's EM exposure, consistent with a lower overall equity weight, the overweight in EM remains. China's economic cycle appears to be on a different clock than much of the developed world, and we believe improving activity may drive relative outperformance in Emerging Asia as the U.S. economy enters a challenging period.[2]
- **Growth rotation continues.** The signals coming from our quantitative work have become clearer to us: The market has entered a late-cycle environment, demonstrated by the incredibly narrow market performance in recent months. We have rotated our portfolio toward quality growth stocks and will continue to do so.
- **Fixed income offers a ballast.** The portfolio remains overweight bonds and holds a duration slightly higher than that of the benchmark. The fixed income portfolio is designed to work as a ballast, with about 60% invested in sovereign bonds and 40% in agency mortgage-backed securities.[2]

								As of 3/31/2023		
Total returns[3,4,5,6,7]	**MTD**	**QTD**	**YTD**	**1 year**	**3 year**	**5 year**	**Since inception**	**1 year**	**5 year**	**Since inception**
CCAPX (Class I; inception 11/30/2015)	-1.41%	-1.41%	2.95%	-3.81%	10.24%	2.95%	5.21%	-8.87%	2.98%	5.48%
Morningstar Global Allocation category	0.96%	0.96%	4.40%	-0.75%	7.38%	3.26%	4.06%	-6.47%	3.13%	3.97%
Benchmark	1.10%	1.10%	6.73%	1.30%	5.95%	4.98%	5.88%	-6.14%	4.81%	5.79%
MSCI ACWI (Net)	1.44%	1.44%	8.85%	2.06%	12.04%	7.03%	8.60%	-7.44%	6.93%	8.49%
Bloomberg U.S. Aggregate Total Return Index	0.61%	0.61%	3.59%	-0.43%	-3.15%	1.18%	1.28%	-4.78%	0.91%	1.21%

Total expense ratio, Class I: 1.17%. Past performance does not guarantee future results. The performance data quoted represents past performance and current returns may be higher or lower. The investment return and principal value of an investment will fluctuate so that an investor's shares, when redeemed, may be worth more or less than the original cost. Performance for periods less than one year is cumulative. The Fund's other share classes may have different performance characteristics. Please call 877-924-4766 or visit our website at www.fsinvestments.com for performance data current to the most recent month-end.

1 Strategy assets includes all vehicles/accounts managed by Chiron Investment Management under this strategy.

Outlook

- **Models point to growth, defensiveness.** Our models sit firmly in a growth setting in the U.S. and Europe, which equates to a more defensive portfolio posture. Meanwhile, emerging markets and developed Asia continue to operate on a different cycle clock and remain in a value setting. Our quantitative work continues to emphasize the importance of valuation, suggesting to us that a growth at a reasonable price (GARP) strategy within equities is the optimal path forward.
- **U.S. earnings hold up in Q1, but this isn't the trough.** As we suggested would be the case last month, the Q1 U.S. earnings season was largely better than expected. S&P 500 earnings per share (EPS) are on track to fall -3.7% year-over-year, compared to expectations for an -8% decline, largely driven by better sales growth that partially compensated for tighter margins. Our argument has been that it would be anomalous to see earnings fall substantially while nominal gross domestic product (GDP) growth remains elevated (earnings are in nominal terms, after all). Indeed, nominal GDP grew at a 5.1% annualized pace (closer to 7.3% if you exclude inventory adjustments) in Q1, keeping firms' top line growth humming along. The consensus among analysts is that the first half of this year will represent a trough for fundamentals, with earnings rising at a 5% pace in the second half followed by 12% EPS growth in 2024. We view this as a best-case outcome rather than a base case. If, as we expect, nominal growth is pressured by both slowing consumer inflation and real growth, it would be companies' top lines that take over for margins as the primary concern for profits. With the market trading at about 18x these (we would argue rosy) earnings expectations, we plan to continue taking risk out of our portfolio into the summer.[2]
- **Narrow market rally points to late-cycle environment.** The defining characteristic of the equity market's positive start to 2023 has been the narrowness of its composition. There are a multitude of ways to illustrate this; the Nasdaq 100 has gained 21.4% year-to-date (YTD), while the S&P 500 Equal-Weight Index has risen just 3.26%. Nearly half of the MSCI ACWI Index's 8.8% YTD return can be attributed to 10 U.S. stocks, which together comprise just 14% of the global equity benchmark. This is a classic late-cycle market signal. When risks to the backdrop rise—as they have with the ongoing bank stress and the upcoming debt ceiling deadline—investors generally flock to what they consider to be the most stable cash-flowing large caps, which in recent years has been U.S. megacap technology stocks. While this investor behavior is unsurprising, we continue to believe the market is overstating the defensiveness of many of these firms as we enter a potential cyclical downturn.[2]
- **A hiatus in the secular spending story.** Our core view is that deglobalization and the myriad paradigm shifts being undertaken today, from the energy transition to artificial intelligence, will fundamentally change the investing landscape. While capital spending growth is slowing this year and wary investors have rewarded companies for capital discipline, we view this as a seminal opportunity to invest in the companies that will benefit most from this spending at attractive entry points.

Market commentary

- Equity markets climbed in April, although market breadth—especially in the U.S.—was quite weak. The MSCI ACWI Index rose 1.44% while the S&P 500 gained 1.56%. Based on the MSCI Emerging Markets Index, emerging markets equities lagged, declining -1.12% on the month.[2]
- U.S. interest rates were largely flat across the yield curve, declining early in the month on continued fallout from the banking stress before recovering mid-month. The 3-month/10-year spread finished at -166 basis points (bps), the lowest for a month-end since the early 1980s. The Bloomberg Agg gained 0.61% and has now risen 3.59% YTD.[2]
- Data continues to paint a resilient picture of the U.S. economy. GDP grew at a below-consensus 1.1% in Q1, but an inventory drawdown detracted more than 2% from the headline. Real final sales to domestic purchasers—a stronger gauge of domestic demand—rose at a healthy 3.2% pace, lifted by strong consumption.[8] Inflation data from March showed price growth continues to slow, albeit at a gradual pace. Labor market data was mixed but broadly shows the worker shortage that has defined the COVID era may be softening.[9]
- The MSCI Europe Index rose 2.64% in April, outperforming the U.S. and emerging markets. A rebound in bank and energy stocks—as fears around financial stresses abated—supported a market that has a high weighting to those sectors.[2]
- The U.K. FTSE 100 Index rose 3.41% last month, outperforming most developed markets. U.K. markets benefitted from a rebound in financials and energy stocks, as well as an attractive forward price-to-earnings (P/E) ratio of only about 10x.[2]
- The MSCI Japan Index rose 2.68% last month, beating stocks in the U.S. and emerging markets. The index pushed to its highest level since an all-time high in September 2021 as a solid domestic economy and accommodative policy boost setiment.[2]
- The MSCI Emerging Markets Index declined -1.12% last month, underperforming developed markets. Markets in China fell as industrial production data disappointed, dragging down the broader index.[2]

Fund overview

FS Chiron Capital Allocation Fund is an actively managed and flexible strategy designed to dynamically invest in the global markets across market cycles.[3]

Strategy

- Ability to invest in a global opportunity set across developed and emerging markets
- Combines proprietary quantitative and fundamental research to quickly identify opportunities
- Targeting best opportunities for growth through a market cycle regardless of style, size, region, industry or sector

2. Bloomberg Finance L.P., as of April 30, 2023.
3. Effective July 16, 2021, the Fund has been renamed FS Chiron Capital Allocation Fund. Prior to that date, the Fund operated under the name Chiron Capital Allocation Fund.
4. The Morningstar category is compiled by Morningstar, an independent mutual fund research and rating service. The Morningstar category represents a universe of funds that is similar in investment objective to the Fund. The category is unmanaged and does not reflect any fees, expenses, or sales charges. You cannot invest directly in the category.
5. The blended benchmark consists of a 60% weighting of the MSCI ACWI Index and a 40% weighting of the Bloomberg Barclays U.S. Aggregate Total Return Index.
6. The MSCI ACWI (Net) is a market capitalization weighted index designed to provide a broad measure of equity-market performance throughout the world and is calculated with dividends reinvested after deduction of withholding tax.
7. The Bloomberg U.S. Aggregate Total Return Index is an investment grade index of bonds denominated in U.S. dollars.
8. U.S. BEA, as of March 31, 2023.
9. U.S. BLS, as of April 30, 2023.

Morningstar ratings are specific metrics of performance and do not represent absolute performance of any fund. For each fund with at least a three-year history, Morningstar calculates a Morningstar Rating based on a Morningstar Risk-Adjusted Return measure that accounts for variation in a fund's monthly performance, placing more emphasis on downward variations and rewarding consistent performance. Exchange-traded funds and open-ended mutual funds are considered a single population for comparative purposes. The top 10% of funds in each 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 fund is derived from a weighted average of the performance figures associated with its three-, five- and ten-year (if applicable) Morningstar Rating metrics. The Fund's other share classes may have different performance characteristics.

DEFINITIONS

Basis points (bps) refers to a common unit of measure for interest rates and other percentages. One basis point is equal to 1/100 of 1%, or 0.01%, or 0.0001, and is used to denote the percentage change in a financial instrument. **Bloomberg U.S. Aggregate Total Return Index (The Agg)** is a broad-based benchmark that measures the investment grade, U.S. dollar-denominated, fixed-rate taxable bond market. The index includes Treasuries, government-related and corporate securities, MBS (agency fixed-rate and hybrid ARM pass-throughs), ABS and CMBS (agency and non-agency). **Earnings per share** is calculated as a company's profit divided by the outstanding shares of its common stock. The resulting number serves as an indicator of a company's profitability. **The Financial Times Stock Exchange 100 Index (U.K. FTSE 100 Index)** is a share index of the 100 companies listed on the London Stock Exchange with (in principle) the highest market capitalization. **Gross domestic product (GDP)** is the total monetary or market value of all finished goods and services produced within a country's borders over the course of a specific time period. **Morningstar Global Allocation category** consists of world-allocation portfolios that seek to provide both capital appreciation and income by investing in three major areas: stocks, bonds and cash. While these portfolios do explore the whole world, most focus on the U.S., Canada, Japan and the larger markets in Europe. **Morgan Stanley Capital International (MSCI) All Country World Index (ACWI) Index** is a market capitalization weighted index designed to provide a broad measure of equity-market performance throughout the world and is calculated with dividends reinvested after deduction of withholding tax. **MSCI EAFE** region covers Developed Market countries in Europe, Australasia, Israel and the Far East. **MSCI Europe Index** captures large and mid-cap representation across 15 developed markets in Europe. **MSCI Emerging Markets Index** captures large and mid-cap representation across 27 Emerging Markets (EM) countries. **MSCI Japan Index** is designed to measure the performance of the large and mid-cap segments of the Japanese market. **Nasdaq 100** is a basket of the 100 largest, most actively traded U.S. companies listed on the Nasdaq stock exchange. **The Philadelphia Semiconductor Sector Index (SOX)** is a capitalization-weighted index composed of 30 semiconductor companies. **Price-to-earnings ratio (P/E ratio)** is the ratio for valuing a company that measures its current share price relative to its per-share earnings (EPS). P/E ratios are used by investors and analysts to determine the relative value of a company's shares in an apples-to-apples comparison**. Real final sales to domestic purchasers** is gross domestic purchases less change in private inventories. **S&P 500 (Standard & Poor's 500 Index)** is a market capitalization-weighted index of the 500 largest U.S. publicly traded companies by market value. **S&P 500 Equal-Weight Index** includes the same constituents as the capitalization weighted S&P 500, but each company in the S&P 500 EWI is allocated a fixed weight - or 0.2% of the index total at each quarterly rebalance.

Index returns do not reflect any management fees, transaction costs, or expenses. Indexes are unmanaged, and one cannot invest directly in an index.

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To determine if the Fund is an appropriate investment for you, carefully consider the Fund's investment objectives, risk, charges and expenses. This and other information can be found in the Fund (full and summary) prospectus, which can be obtained by calling 877-924-4766 or by visiting www.fsinvestments.com. Please read the prospectus carefully before investing.

RISK FACTORS

Investing involves risk, including possible loss of principal. Bonds and bond funds will decrease in value as interest rates rise. High yield bonds involve greater risks of default or downgrade and are more volatile than investment grade securities, due to the speculative nature of their investments. Mortgage-backed securities may experience significantly greater price and yield volatility than traditional debt securities. Including the potential for a complete loss of expected future cash flow based on the prepayment behavior of underlying borrowers. In addition to the normal risks associated with investing, international investments may involve risk or capital loss from unfavorable fluctuation in currency values, differences in generally accepted accounting principles or from social, economic or political instability in other nations. Emerging markets involve heightened risks related to these factors as well as increased volatility and lower trading volume. Convertible and preferred securities have many of the same characteristics as stocks, including many of the same risks. In addition, convertible securities may be more sensitive to changes in interest rates than stocks. The Fund may invest in derivatives, which are often more volatile than other investments and may magnify the Fund's gains or losses. The Fund's use of futures contracts, forward contracts, options, and swaps is subject to correlation, leverage, liquidity and market risk. Investments in smaller companies typically exhibit higher volatility. Investments by the Fund in precious metals-based companies, and in asset-based securities indexed to the value of such metals, may expose the Fund to adverse macroeconomic conditions elevating the risk of loss. Value and growth investment styles may increase the risks of investing in the Fund. If the Adviser's assessment of market conditions or a company's value is wrong, the Fund could suffer losses or produce poor performance relative to other funds. In addition, "value stocks" can continue to be undervalued by the market for long periods. If a growth company does not meet expectations, the price of its stock may decline significantly, even if it has increased earnings. Many growth companies do not pay dividends. Companies that do not pay dividends often have greater stock price declines during market downturns. There is no assurance that the Fund will meet its objective.

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