The Summer Shock— Fertile Ground for "Crisis Alpha"

A Time for Global Macro and Managed Futures to Prosper

October 2011

The Macro-driven Market

As investors look back on the third quarter of 2011, most will reluctantly recall the 14% decline in US equities and the radical volatility that accompanied it. It was the S&P 500's worst quarter since the 2008 crisis. At one point, several global indices had declined nearly 20%, a level many strategists associate with bear markets. Fears of a European debt default, ongoing budgetary politics in Washington, a US debt downgrade, recessionary fears in the US and a slowing pace of economic global growth (including China) are just a few of the headlines that battered the markets last quarter.

The market action was dominated by what we in the investment world call "macro events," or large, overarching themes that have broad impact across markets and often trump security specific fundamentals such as earnings. Given the unresolved nature of the previously mentioned concerns, many economists believe macro events will continue to dominate the marketplace in the foreseeable future. Unfortunately, macro-driven markets are often difficult for traditional long-only (buy and hold) investors. For example, traditional equity investors often look to invest in growing companies with strong balance sheets and "attractive" valuations based upon fundamental metrics. Unfortunately, as we saw during Q3, when macro events dominate the markets, stock specific fundamentals don't always matter.

A recent study by Goldman Sachs pointed out that the 3-month correlation[1] among the stocks that make up the S&P 500 stood at 0.73, the highest reading in at least 20 years. This further highlights the reason why stock selection hasn't been working for many investors: stocks have generally been moving in unison, with little regard for company-specific fundamentals and/or valuation. This extremely high correlation, along with a level of intraday volatility not seen since the 2008 Credit Crisis, reflects a macro "risk-on/risk-off" trade cycle, meaning the overall market's appetite for "risky" assets has demonstrated significant ebbs and flows. In an environment like this, an investor could spend a lot of time picking a fundamentally strong stock at what seems like an attractive valuation, only to see a macro headline trump his analysis as the "risk-off" trade results in losses across equities, regardless of company specific fundamentals.

[1] **Correlation.** *A statistical measure of how returns move together over time; a correlation of 1 indicates the two returns move perfectly together, 0 indicates movements are random, and -1 indicates opposite movements. "High" correlation is when two returns experience similar positive or negative returns over a certain time period. Correlations by definition will vary over time, and while this data is true for the historical performance over this time period, there is no guarantee that these correlations will persist.*

The Precipice of Crisis

For as long as there have been markets, there have been financial crises. Many of these events end up as little more than footnotes in economic history, but some of the more well-known include the Tulip Mania during the 1630s, the South Sea Bubble during the 1720s, and more recently, the Great Depression during the 1930s. While history books are littered with other such events (the Latin American Debt Crisis, the Asian Financial Crisis, etc.) there is much debate about whether or not these crises are becoming more frequent (and severe) or if investors' memories are simply too short.

Academic debates aside, there is no question that little more than a decade into the 21st century, investors have already been forced to cope with two severe crises: the bursting of the Tech Bubble between 2000 and 2002, followed by the collapse of the housing and credit markets between 2007 and 2009. While we are not in the business of forecasting financial crises, the recent downgrade of US government securities and the ongoing European debt debacle seem to provide ample justification for the fear that has come to grip the market. The sharp losses experienced across equity, credit, and many commodity markets during Q3 2011 (what we're calling the Summer Shock) force one to acknowledge the possibility that we could be at the precipice of yet another crisis. While both the Tech Bubble and the Credit Crisis were largely private sector events, markets are now contending with the possibility of a crisis precipitated not by corporations or individuals, but by the governments of some of the world's largest and most developed economies.

During times of stress, investors have historically turned to traditional safe havens such as treasuries and the US dollar. However, fears of rising inflation and dollar devaluation caused by excessive government debt and quantitative easing have resulted in many investors questioning the safety of these so-called "safe havens." The political stalemate in Washington has only served to exacerbate these fears, as the rancor surrounding the recent debt ceiling debate contributed to the decision by Standard & Poor's to downgrade US government securities for the first time in history, throwing into question their long-held status as "risk free" (and with interest rates near zero, some believe treasuries now represent "return free risk"). These concerns have left investors scrambling for alternatives, begging the question: if we are in fact on the verge of another crisis, which strategies have the potential to thrive during periods of market stress?

What's the Alternative?

We believe the answer to this question can possibly be found in the way markets have behaved during past crises: macro events and investor panic often result in markets becoming highly correlated (as we saw during Q3). This has historically resulted in large capital flows across global markets and created strong trends in interest rates, currencies, equities and commodities. Knowing past performance is no guarantee of future results, two strategies have historically been able to generate strong profits in these environments, generating "crisis alpha" by anticipating market dislocations and/or capitalizing on their resulting trends. These strategies are global macro and managed futures. Of course, there is no guarantee that any investment strategy will achieve its objectives, generate profits, or avoid losses.

Opportunities in Crisis

Global macro and managed futures managers employ extremely dynamic trading strategies. Not only can these managers move fluidly between markets, they can also hold long[2] and/or short[3] positions across any combination of commodities, currencies, interest rates, and equity indices. This broad mandate allows both global macro and managed futures managers to take advantage of opportunities regardless of what market they are in or which direction that market is moving. This stands in stark contrast to most long-only investment strategies, which often focus on just a single market, severely limiting their opportunity sets (FIGURE 1).

[2] **Long.** *Buying an asset/security that gives partial ownership to the buyer of the position. Long positions profit from an increase in price.*

[3] **Short.** *Selling an asset/security that may have been borrowed from a third party with the intention of buying back at a later date. Short positions profit from a decline in price. If a short position increases in price, covering the short position at a higher price may result in a loss.*

Figure 1.
INVESTMENT OPPORTUNITIES FOR MANAGED FUTURES AND GLOBAL MACRO

MANAGED FUTURES

Primary Investment Driver
Price

Manager Action
React to data
Primarily systematic

GLOBAL MACRO

Primary Investment Driver
Fundamental data

Manager Action
Predict future direction
Primarily discretionary

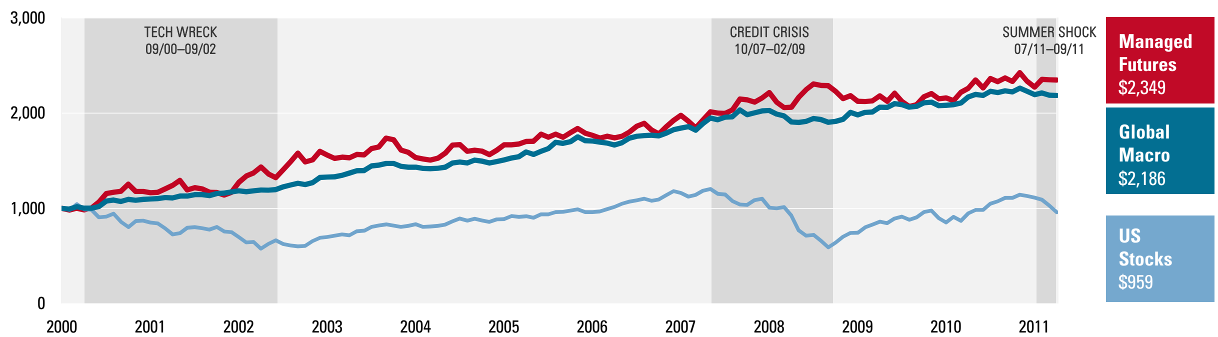
Not all managers trade across all asset classes. There is no guarantee that any investment product will achieve its objectives, generate profits or avoid losses. Source: Altegris.

Another reason why managed futures and global macro strategies can each outperform during periods of crisis lies in one of the key differences between the two strategies: global macro strategies are predictive, while managed futures strategies are reactive.

Global macro managers often employ economists and financial analysts who utilize fundamental economic data in order to predict which direction global markets will move. In contrast, managed futures managers typically ignore fundamental economic data, and instead rely upon complex computer models (often developed by teams of scientists and/or engineers) in order to identify trends or other patterns in the prices themselves. This means global macro managers can profit by correctly identifying the same imbalances that often result in crises, while managed futures managers can profit by taking advantage of the strong directional price movements (i.e. trends) that typically emerge once a crisis begins; investor panic and other behavioral biases often result in these trends persisting much longer than one would normally expect, resulting in opportunities for outsized performance for trend followers. While both global macro and managed futures maintain broad investment flexibility, we believe their different approaches can be complementary (FIGURE 2).

Figure 2.

HISTORICAL PERFORMANCE DURING CRISIS PERIODS:
MANAGED FUTURES VS. GLOBAL MACRO VS. US STOCKS | July 2000–September 2011



PAST PERFORMANCE IS NOT INDICATIVE OF FUTURE RESULTS. The total return of an investment is only one measure of performance. See page 7 for performance returns over various time frames. US stocks represented by S&P 500 Total Return Index; managed futures represented by Altegris 40 Index® (started in July 2000; data is available back to 1990); Global macro represented by Barclay Global Macro Index. The referenced indices are shown for general market comparisons and are not meant to represent any particular Fund. An investor cannot invest directly in an index. Moreover, indices do not reflect commissions or fees that may be charged to an investment product based on the index, which may materially affect the performance data presented. There is no guarantee an investment will achieve its objective, generate profits or avoid losses. Performance should never be the sole consideration when making an investment decision. The S&P 500 Total Return Index is the total return version of the S&P 500 Index, which is unmanaged and generally representative of certain portions of the U.S. equity markets. The Altegris 40 Index tracks the performance of the 40 leading managed futures programs, by ending monthly equity (assets) for the previous month, as reported to Altegris. The Barclay Global Macro Index tracks the performance of ~175 global macro programs, by ending monthly values, net of fees, as reported to Barclay Hedge. See page 8 for additional definitions, descriptions, and risks of managed futures, global macro, and US stocks.

Crisis Alpha

As noted earlier, both managed futures and global macro exhibit several characteristics which we believe give them the potential to outperform other investment strategies during periods of crisis. While past performance is not necessarily indicative of future results, managed futures and global macro managers have historically been able to generate strong returns during crises. During the Tech Bubble, US stocks fell by -45% while global macro and managed futures managers gained 17% and 43%, respectively. Similar results were achieved during the recent Credit Crisis, with US stocks falling -50% while global macro and managed futures managers gained 1% and 19%, respectively. During Q3, the S&P 500 TR fell -14% while global macro managers remained flat and managed futures managers gained 3% (FIGURE 3).

Figure 3.

HISTORICAL RETURNS

July 2000–September 2011

Crisis Periods	US Stocks	Managed Futures	Global Macro
Tech Bubble (09/00-09/02)	-45%	43%	17%
Credit Crisis (10/07-02/09)	-50%	19%	1%
Summer Shock (07/11-09/11)	-14%	3%	0%
Non-Crisis Periods	**US Stocks**	**Managed Futures**	**Global Macro**
Oct 2002–Sep 2007	105%	35%	58%
Mar 2009–Jun 2011	89%	-1%	15%

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Altegris Mutual Funds

Comprised of professionals with vast experience in alternative investments, the Altegris team has one core mission: to find the best alternative investment managers in the industry and make them available to advisers and their clients. Until recently however, many of these managers had only been available to large institutions and high net worth investors. That is, until now. After extensive research and due diligence by the Altegris team, investors of all sizes can now access what we believe to be some of the best global macro and managed futures managers in the world via Altegris mutual funds.

During the volatile markets experience during Q3 2011, the Altegris Managed Futures Strategy Fund (MFTAX) gained 3.23% and the Altegris Macro Strategy Fund (MCRAX) gained 2.13%. Past performance is not necessarily indicative of future results, but we believe global macro and managed futures strategies have shown the ability to generate attractive returns across market environments. While it's yet to be seen if Summer Shock was the start of a new financial crisis, or just a blip on the long road to recovery, we believe that global macro and managed futures strategies warrant an allocation in well diversified portfolios.

Managed Futures	Q3 2011	YTD	1-Year	Since Inception*
MFTAX	3.23%	-5.16%	-0.76%	-0.43%

* *Inception data for Class A was August 26, 2010. PAST PERFORMANCE IS NOT INDICATIVE OF FUTURE RESULTS. Current performance may be lower or higher than the performance data quoted above. Investment return and principal value will fluctuate, so that shares, when redeemed, may be worth more or less than their original cost. A fund's performance, especially for very short periods of time, should not be the sole factor in making your investment decisions. Performance shown is for Class A shares. Performance of Class A does not reflect the deduction of the sales charge. Inclusion of the sales charge would reduce the performance quoted. MFTAX: Altegris Managed Futures Strategy Fund (Class A). SOURCE: Altegris, Gemini.*

Global Macro	Q3 2011	YTD	1-Year	Since Inception*
MCRAX	2.13%	NA	NA	0.60%

* *Inception data for Class A was June 1, 2011. PAST PERFORMANCE IS NOT INDICATIVE OF FUTURE RESULTS. Current performance may be lower or higher than the performance data quoted above. Investment return and principal value will fluctuate, so that shares, when redeemed, may be worth more or less than their original cost. A fund's performance, especially for very short periods of time, should not be the sole factor in making your investment decisions. Performance shown is for Class A shares. Performance of Class A does not reflect the deduction of the sales charge. Inclusion of the sales charge would reduce the performance quoted. MCRAX: Altegris Macro Strategy Fund (Class A). SOURCE: Altegris, Gemini.*

Appendix: Historical Performance

HISTORICAL PERFORMANCE: 1-YEAR, 3-YEAR, 5-YEAR AND 10-YEAR COMPARISON

As of September 2011

Annualized Returns	1-Year	3-Year	5-Year	10-Year
Managed Futures	3.91%	4.43%	6.19%	6.59%
Global Macro	0.72%	4.65%	5.59%	7.02%
US Stocks	1.15%	1.22%	-1.18%	2.81%

Annualized Standard Deviation[4]	1-Year	3-Year	5-Year	10-Year
Managed Futures	9.99%	9.45%	9.77%	10.85%
Global Macro	4.13%	4.64%	5.38%	5.21%
US Stocks	13.12%	20.95%	18.17%	15.68%

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[4] **Standard deviation.** *The most widely accepted measurement of volatility (risk). Specifically, it measures the degree to which returns have been spread out around their historical mean or average. It is the square root of the variance (average squared difference between the actual return and the average return). Standard deviation does not distinguish between positive and negative volatility. In other words, it interprets any movement above or below the historical mean as undesirable. Upside volatility is "good risk."*

INDEX DEFINITIONS

An investor cannot invest directly in an index. Moreover, indices do not reflect commissions or fees that may be charged to an investment product based on the index, which may materially affect the performance data presented.

Altegris 40 Index.® The Altegris 40 Index tracks the performance of the 40 leading managed futures programs as reported to managedfutures.com each month. Each month, managedfutures.com ranks its' database to find the top 40 Composite CTA Programs based on ending monthly equity for the previous month. Managedfutures.com then calculates the dollar-weighted average performance of those 40 programs for the monthly Altegris 40 Index performance. Although the Altegris 40 tracks only 10% of the CTAs who report their performance, their combined equity represents approximately 50% of the equity of the entire managed futures industry. The Index was started in July 2000; data is available back to 1990.

Barclay Global Macro Index. The Barclay Global Macro Index tracks the performance of ~175 global macro programs, by ending monthly values, net of fees, as reported to Barclay Hedge.

S&P 500 Total Return Index. The S&P 500 Total Return Index is the total return version of S&P 500 Index. The S&P 500 Index is unmanaged and is generally representative of certain portions of the U.S. equity markets. For the S&P 500 Total Return Index, dividends are reinvested on a daily basis and the base date for the index is January 4, 1988. All regular cash dividends are assumed reinvested in the S&P 500 Index on the ex-date. Special cash dividends trigger a price adjustment in the price return index.

INDEX DESCRIPTIONS AND RISKS

US Stocks	Managed Futures	Global Macro
Representative Index S&P 500 Total Return (TR) Index	**Representative Index** Altegris 40 Index®	**Representative Index** Barclay Global Macro Index
Characteristics 500 US stocks; Weighted towards large capitalizations	**Characteristics** Forty top AUM managed futures programs, monthly, as reported to Altegris	**Characteristics** ~175 global macro programs by monthly values as reported to Barclay
Key Risks STOCK MARKET RISK: Stock prices may decline	**Key Risks** MARKET RISK: Prices may decline LEVERAGE RISK: Volatility and risk of loss may magnify with use of leverage COUNTRY/REGIONAL RISK: World events may adversely affect values	**Key Risks** MARKET RISK: Prices may decline LEVERAGE RISK: Volatility and risk of loss may magnify with use of leverage COUNTRY/REGIONAL RISK: World events may adversely affect values

About Altegris

Altegris searches the world to find what we believe are the best alternative investments. Our suite of private funds, actively managed mutual funds and managed accounts provides an efficient solution for financial professionals and individuals seeking to improve portfolio diversification.

With one of the leading Research and Investment groups focused solely on alternatives, Altegris follows a disciplined process for identifying, evaluating, selecting and monitoring investment talent across a spectrum of alternative strategies including managed futures, global macro, long/short equity, event-driven and others.

Veteran experts in the art and science of alternatives, Altegris guides investors through the complex and often opaque universe of alternative investing.

Alternatives are in our DNA. Our very name, Altegris, highlights our singular focus on alternatives, the highest standards of integrity, and a process that constantly seeks to minimize investor risk while maximizing potential returns.

The Altegris Companies,* wholly owned subsidiaries of Genworth Financial, Inc., include Altegris Investments, Altegris Advisors, Altegris Funds, and Altegris Clearing Solutions. Altegris currently has approximately $2.88 billion in client assets, and provides clearing services to $780 million in institutional client assets.

* *Altegris and its affiliates are subsidiaries of Genworth Financial, Inc. and are affiliated with Genworth Financial Wealth Management, Inc., and include: (1) Altegris Advisors, LLC, an SEC registered investment adviser; (2) Altegris Investments, Inc., an SEC-registered broker-dealer and FINRA member; (3) Altegris Portfolio Management, Inc. (dba Altegris Funds), a CFTC-registered commodity pool operator, NFA member and California registered investment adviser; and (4) Altegris Clearing Solutions, LLC, a CFTC-registered futures introducing broker and commodity trading advisor and NFA member. The Altegris Companies and their affiliates have a financial interest in the products they sponsor, advise and/or recommend, as applicable. Depending on the investment, the Altegris Companies and their affiliates and employees may receive sales commissions, a portion of management or incentive fees, investment advisory fees, 12b-1 fees or similar payment for distribution, a portion of commodity futures trading commissions, margin interest and other futures-related charges, fee revenue, and/or advisory consulting fees.*

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Hedge funds, commodity pools and other alternative investments involve a high degree of risk and can be illiquid due to restrictions on transfer and lack of a secondary trading market. They can be highly leveraged, speculative and volatile, and an investor could lose all or a substantial amount of an investment. Alternative investments may lack transparency as to share price, valuation and portfolio holdings. Complex tax structures often result in delayed tax reporting. Compared to mutual funds, hedge funds and commodity pools are subject to less regulation and often charge higher fees. Alternative investment managers typically exercise broad investment discretion and may apply similar strategies across multiple investment vehicles, resulting in less diversification. Trading may occur outside the United States which may pose greater risks than trading on U.S. exchanges and in U.S. markets. PAST RESULTS ARE NOT NECESSARILY INDICATIVE OF FUTURE RESULTS.

There are substantial risks and conflicts of interests associated with Managed Futures and commodities accounts, and you should only invest risk capital. The success of an investment is dependent upon the ability of a commodity trading advisor (CTA) to identify profitable investment opportunities and successfully trade. The identification of attractive trading opportunities is difficult, requires skill, and involves a significant degree of uncertainty. CTAs have total trading authority, and the use of a single CTA could mean a lack of diversification and higher risk. The high degree of leverage often obtainable in commodity trading can work against you as well as for you, and can lead to large losses as well as gains. Returns generated from a CTA's trading, if any, may not adequately compensate you for the business and financial risks you assume. CTAs may trade highly illiquid markets, or on foreign markets, and may not be able to close or offset positions immediately upon request. You may have market exposure even after the CTA has a request for closure or liquidation. You can lose all or a substantial amount of your investment. Managed Futures and commodities accounts may be subject to substantial charges for management and advisory fees. It may be necessary for accounts that are subject to these charges to make substantial trading profits in order to avoid depletion or exhaustion of their assets. The disclosure document contains a complete description of each fee to be charged to your account by a CTA. If you use notional funding, you may lose more than your initial cash investment. If you purchase a commodity option you may sustain a total loss of the premium and of all transaction costs. If you purchase or sell a commodity future or sell a commodity option you may sustain a total loss of the initial margin funds and any additional funds that you deposit with your broker to establish or maintain your position. If the market moves against your position, you may be called upon by your broker to deposit a substantial amount of additional margin funds, on short notice, in order to maintain your position. If you do not provide the requested funds within the prescribed time, your position may be liquidated at a loss, and you will be liable for any resulting deficit in your account. This brief statement cannot disclose all the risks and other significant aspects of the commodity markets, and you should carefully study the disclosure document before you trade, including the description of the principal risk factors of an investment. PAST RESULTS ARE NOT NECESSARILY INDICATIVE OF FUTURE RESULTS.

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Investors should carefully consider the investment objectives, risks, charges and expenses of the Fund or Funds described herein. This and other important information about a Fund is contained in a Fund's Prospectus, which can be obtained by calling (877) 772-5838. The Prospectus should be read carefully before investing. Funds are distributed by Northern Lights Distributors, LLC member FINRA. Altegris Advisors, J.P. Morgan Investment Management and Northern Lights Distributors are not affiliated.

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The Fund is "non-diversified" for purposes of the Investment Company Act of 1940, which means that the Fund may invest in fewer securities at any one time than a diversified fund. When the Fund invests in fixed income securities or derivatives, the value of your investment in the Fund will fluctuate with changes in interest rates. Typically, a rise in interest rates causes a decline in the value of fixed *income securities or derivatives owned by the Fund. In general, the market price of debt securities with longer maturities will increase or decrease more in response to changes in interest rates than shorter-term securities. Other risk factors include credit risk (the debtor may default) and prepayment risk (the debtor may pay its obligation early, reducing the amount of interest payments). These risks could affect the value of a particular investment by the Fund possibly causing the Fund's share price and total return to be reduced and fluctuate more than other types of investments. To respond to adverse market, economic, political or other conditions, the Fund may invest 100% of its total assets, without limitation, in high-quality short-term debt securities and money market instruments. The Fund's indirect and direct exposure to foreign currencies subjects the Fund to the risk that those currencies will decline in value relative to the U.S. Dollar, or, in the case of short positions, that the U.S. Dollar will decline in value relative to the currency that the Fund is short. Currency rates in foreign countries may fluctuate significantly over short periods of time for a number of reasons, including changes in interest rates and the imposition of currency controls or other political developments in the U.S. or abroad. In addition, the Fund may incur transaction costs in connection with conversions between various currencies.*

The Fund will invest a percentage of its assets in derivatives, such as futures and options contracts. The use of such derivatives may expose the Fund to additional risks that it would not be subject to if it invested directly in the securities and commodities underlying those derivatives. The Fund may experience losses that exceed losses experienced by funds that do not use futures contracts and options. There may be an imperfect correlation between the changes in market value of the securities held by the Fund and the prices of futures and options on futures. Although futures contracts are generally liquid instruments, under certain market conditions there may not always be a liquid secondary market for a futures contract. As a result, the Fund may be unable to close out its futures contracts at a time which is advantageous. Trading restrictions or limitations may be imposed by an exchange, and government regulations may restrict trading in futures contracts and options. Because option premiums paid or received by the Fund are small in relation to the market value of the investments underlying the options, buying and selling put and call options can be more speculative than investing directly in securities. Over-the-counter transactions are subject to little, if any, regulation and may be subject to the risk of counterparty default. A portion of the Fund's assets may be used to trade OTC commodity interest contracts, such as forward contracts, option contracts in foreign currencies and other commodities, or swaps or spot contracts.

A substantial portion of the trades of the global macro programs are expected to take place on markets or exchanges outside the United States. Some foreign markets present additional risk, because they are not subject to the same degree of regulation as their U.S. counterparts. Trading on foreign exchanges is subject to the risks presented by exchange controls, expropriation, increased tax burdens and exposure to local economic declines and political instability. An adverse development with respect to any of these variables could reduce the profit or increase the loss earned on trades in the affected international markets. International trading activities are subject to foreign exchange risk.

The Fund may employ leverage and may invest in leveraged instruments. The more the Fund invests in leveraged instruments, the more this leverage will magnify any losses on those investments. Leverage will cause the value of the Fund's shares to be more volatile than if the Fund did not use leverage. The Fund may take short positions, directly and indirectly through the Subsidiary, in derivatives. If a derivative in which the Fund has a short position increases in price, the underlying Fund may have to cover its short position at a higher price than the short sale price, resulting in a loss. Structured notes involve leverage risk, tracking risk and issuer default risk. Taxation Risk involves investing in commodities indirectly through the Subsidiary, through which the Fund will obtain exposure to the commodities markets within the federal tax requirements that apply to the Fund. However because the Subsidiary is a controlled foreign corporation, any income received from the Subsidiary's investments in Underlying Funds/Pools will be passed through to the Fund as ordinary income, which may be taxed at less favorable rates than capital gains. Underlying Funds/Pools in which the Subsidiary invests will retain investment managers and be subject to investment advisory and other expenses which are indirectly paid by the Fund. As a result, the cost of investing in the Fund may be higher than other mutual funds that invest directly in stocks and bonds. Each Underlying Fund/Pool will pay management fees, brokerage commissions, operating expenses and performance based fees to each manager it retains. Performance based fees will be paid without regard to the performance of any other managers retained or to the overall profitability of the Underlying Fund/Pool. Underlying Funds/Pools are subject to specific risks, depending on the nature of the managers they retain. There is no guarantee that any of the trading strategies used by the managers retained by an Underlying Fund/Pool will be profitable or avoid losses.

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