Gateway Active Index-Option Overwrite Composite Commentary

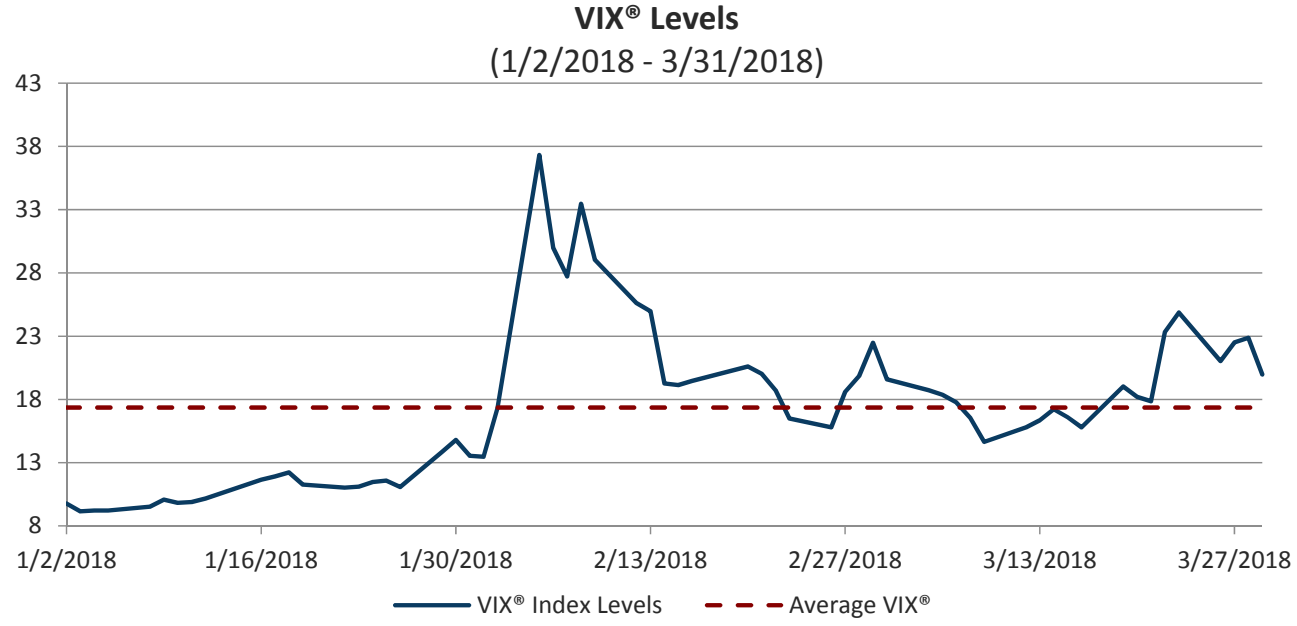
Q1 2018

MARKET RECAP

The S&P 500® Index declined 0.76% for the first quarter. The slight loss for the quarter masked significant equity market volatility. The S&P 500® Index returned 5.73%, -3.69% and -2.54% for January, February and March, respectively, and the equity market had its first back-to-back losing months since January and February of 2016.

The precise path of equity market advances and declines over the course of the quarter was more severe than the monthly returns. The strong, low volatility advance of the equity market in Q4 2017 continued over the first three weeks of 2018 as the S&P 500® Index returned 7.55% through January 26th. Economic data releases and corporate earnings reports were positive and optimism about the impact of tax cuts also helped drive the market higher. But inflationary fears crept into the market and its momentum quickly changed direction. From its all-time closing high on January 26th through February 8th, the S&P 500® Index lost 10.10%. A significant portion of the decline occurred on Monday, February 5th when the S&P 500® Index lost 4.10% and volatility measures spiked to levels not seen since August of 2015. From its closing value on February 8th through March 9th, the equity market staged a partial recovery with the S&P 500® Index returning 8.21%. But the recovery stalled out as fears of a trade war grew while technology stocks slumped. Several leading technology companies came under pressure in mid-March, including Facebook, Inc. which acknowledged mishandling user profile data, specifically in connection with political consultant Cambridge Analytica's use of data on over 50 million users to target voters in the 2016 election. As the Facebook scandal built, the Trump administration enacted tariffs on steel and aluminum imported from multiple countries and threatened additional trade restrictions on China, ostensibly in retaliation for years of trade and intellectual property violations. The S&P 500® Index declined 7.06% from March 9th through March 23rd, putting the market back near correction territory. A 2.05% advance for the S&P 500® Index over the shortened final week of March was not enough to avoid a negative return for the quarter.

Implied volatility, as measured by the Cboe® Volatility Index (the VIX®), averaged 17.35 for the quarter, while S&P 500® Index realized volatility (as measured by its annualized standard deviation of daily returns) was 20.17%. It was the first time since the third quarter of 2015 that realized volatility exceeded average implied volatility for a quarter. The VIX® had a closing high of 37.32 on February 5th and an intra-day high of 50.30 on February 6th, the highest VIX® reading since August 2015. The closing low for the VIX® was 9.15 on January 3rd.



Datasource: Bloomberg, L.P.

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EQUITY MARKETS

Despite equity market losses and a significant uptick in volatility, data releases suggested the market backdrop of an expanding economy and robust earnings growth remained intact, while inflationary pressures showed unexpected signs of life. The January Consumer Price Index (CPI) release on February 14th reported a 0.5% increase in prices for the month and a year-over-year change of 2.1%, both data points exceeded consensus expectations. The February CPI showed a year-over-year change of 2.2%. On March 28th, the final estimate of fourth quarter GDP growth came in at 2.9%, which exceeded consensus expectations and was an upward revision of the previous estimate of 2.5%. Nearly 84% of S&P 500® Index companies reporting fourth quarter earnings results met or exceeded expectations, as aggregate operating earnings grew 5.0% during Q4 and 17.2% year-over-year.

The Cboe® S&P 500 BuyWrite℠ Index (the BXM℠)[1], had a return of -1.56% for the first quarter. The BXM's℠ underperformance relative to the S&P 500® Index for the quarter was primarily due to the BXM's℠ lagging performance during the market advance in January. Specifically, the BXM℠ returned 1.46% from the beginning of the year through January 26th, underperforming the S&P 500® Index by 609 basis points (bps). The BXM℠ delivered downside protection relative to the equity market during both the January-February correction and the mid-March market decline. From January 26th through February 8th, the BXM℠ returned -7.72% and from March 9th through March 23rd it returned -4.53%. The BXM℠ outperformed the S&P 500® Index by 238 bps and 253 bps in each respective period.

On the third Friday of each month of the quarter, the BXM℠ wrote a new index call option as the option it wrote the previous month expired. The premiums collected on written options had significant influence on downside protection the BXM℠ delivered during equity market declines and its upside participation during equity market advances. Premiums collected as a percentage of the BXM's℠ underlying value were 0.92%, 1.62% and 1.39% in January, February and March, respectively. Higher premiums in February and March relative to January are reflective of the higher implied volatility levels in February and March.

The Bloomberg Barclays U.S. Aggregate Bond Index returned -1.46% for the first quarter. It was the first quarter since Q3 2008 that returns for both the stock and bond markets were negative. The yield on the 10-year U.S. Treasury Note rose from 2.41% on December 31st to a high for the quarter of 2.95% on February 21st, and then declined to end the quarter at 2.74%.

COMPOSITE PERFORMANCE

The Gateway Active Index-Option Overwrite Composite (the Composite) returned -3.49%, net of fees, for the first quarter, underperforming the BXM℠ by 193 bps. With monthly returns of 1.12%, -2.81% and -1.80% for January, February and March, respectively, the Composite outperformed in January but underperformed in February and March.

The portfolio performance contributions, annualized standard deviation and portfolio statistics quoted for the Composite in the following paragraphs are those measured by a representative account.*

The Composite's underperformance relative to the BXM℠ for the quarter was primarily due to the market's strong advance from February 8th to March 9th when the BXM℠ returned 8.02%, nearly matching the return of the S&P 500® Index and outperforming the Composite's 4.63% return by 339 bps. The January 26th through February 8th equity market correction that occurred prior to this advance resulted in the Composite and the BXM℠ having different amounts of market exposure. The static approach of the BXM℠ resulted in its written index call option being very far out-of-the money when the equity market began its recovery, thus giving the BXM℠ nearly full market exposure, while the Composite's active approach gradually lowered the strike prices of its diversified portfolio of written call options as the market declined. This resulted in the Composite having less market exposure than the BXM℠ when the market began its recovery and thus less participation in the market advance.

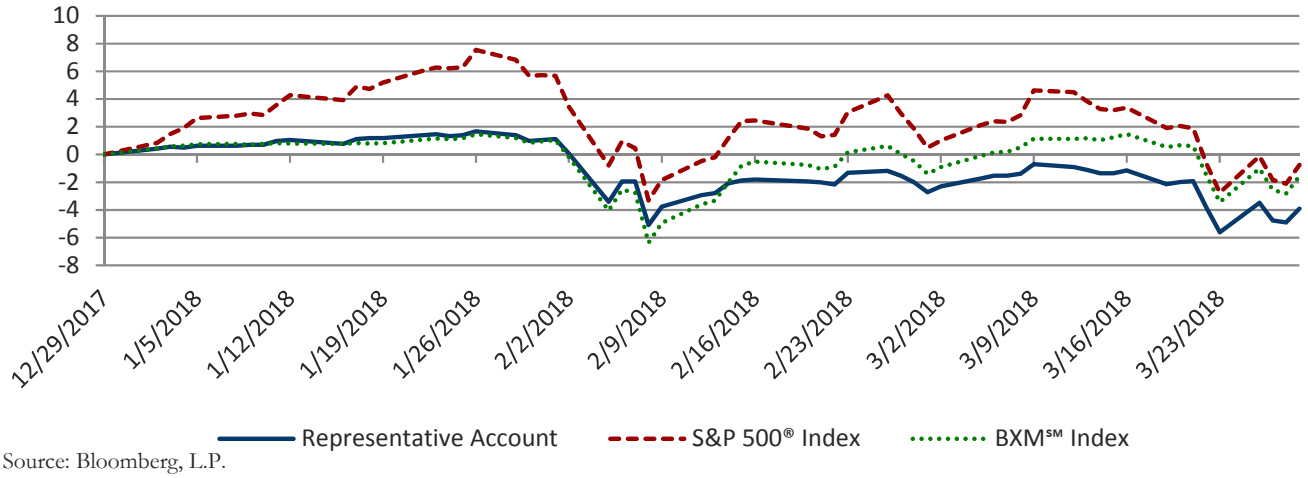
[1] The Cboe® S&P 500 BuyWrite℠ Index (the BXM℠) is a passive total return index designed to track the performance of a hypothetical buy-write strategy on the S&P 500® Index. The construction methodology of the index includes buying an equity portfolio replicating the holdings of the S&P 500® Index and selling a single one-month S&P 500® Index call option with a strike price approximately at-the-money each month on the Friday of the standard index-option expiration cycle and holding that position until the next expiration.

*Represents supplemental information to the GIPS-compliant presentation. This representative account was selected as it is the largest account in the Composite.

For the first quarter, the underlying equity portfolio of the Composite's representative account contributed a total return of -1.27%, resulting in a performance differential of negative 51 bps relative to the S&P 500® Index. Equity performance differentials are varied for each account in the Composite. The Composite's index call option portfolio generated risk-reducing cash flow throughout the quarter, detracting from returns in January and contributing positively to returns in February and March. January's loss on index call options was expected in a period when call premiums earned were insufficient to keep pace with the equity market's advance. The Composite's annualized standard deviation of daily returns for the quarter was 14.54% as compared to 16.84% for the BXM℠ and 20.17% for the S&P 500® Index. The Composite exhibited a beta to the BXM℠ of 0.85 for the quarter.

In January, Gateway's index call option activity was focused on exchanging contracts well in advance of their expiration dates for ones with later expiration dates and higher strike prices to maintain a typical amount of market exposure as the market advanced. As implied volatility increased and the market declined in February and March, the investment team focused on index call option decisions that would add significant cash flow potential and maintain diversification of expiration dates while not deviating significantly from the Composite's typical risk profile.

Cumulative Performance (%)
(12/29/17 - 3/31/18)



Source: Bloomberg, L.P.

Performance data shown represents past performance and is no guarantee of, and not necessarily indicative of, future results.

As of March 31st, the Composite's diversified equity portfolio was over 95% hedged with index call options with the weighted-average strike price between 1.5% and 2.5% out-of-the-money, average time to expiration of 32 days and annualized premium to earn of 15% to 20%. Relative to the beginning of the quarter, this positioning represented similar market exposure and significantly higher net cash flow potential.

MARKET PERSPECTIVE

Option writing strategies are often positioned as suitable components of the risk management portion of a diversified investment program due to their reliable downside protection and features that benefit from elevated equity market volatility. But when both of the foremost option writing strategy benchmarks, the Cboe® S&P 500 BuyWrite℠ Index (BXM℠) and the Cboe® S&P 500 PutWrite Index (PUT), deliver a larger loss than the S&P 500® Index in a quarter that featured the first equity market correction in two years and elevated volatility levels for two months, the effectiveness of option writing strategies as risk management tools might be questioned.

A snapshot look at the outcomes for any investment strategy and its associated market over any given month, quarter or year can often mask the way risk and return were realized over the course of the time period in question. When looking at the path the equity market took in Q1 2018 (Figure 1), it is clear to see that the lower return of the option writing benchmarks relative to the S&P 500® Index was due to a low level of participation in the significant market advance that began the year, rather than a lack of downside protection after the equity market reached its year-to-date high in late January.

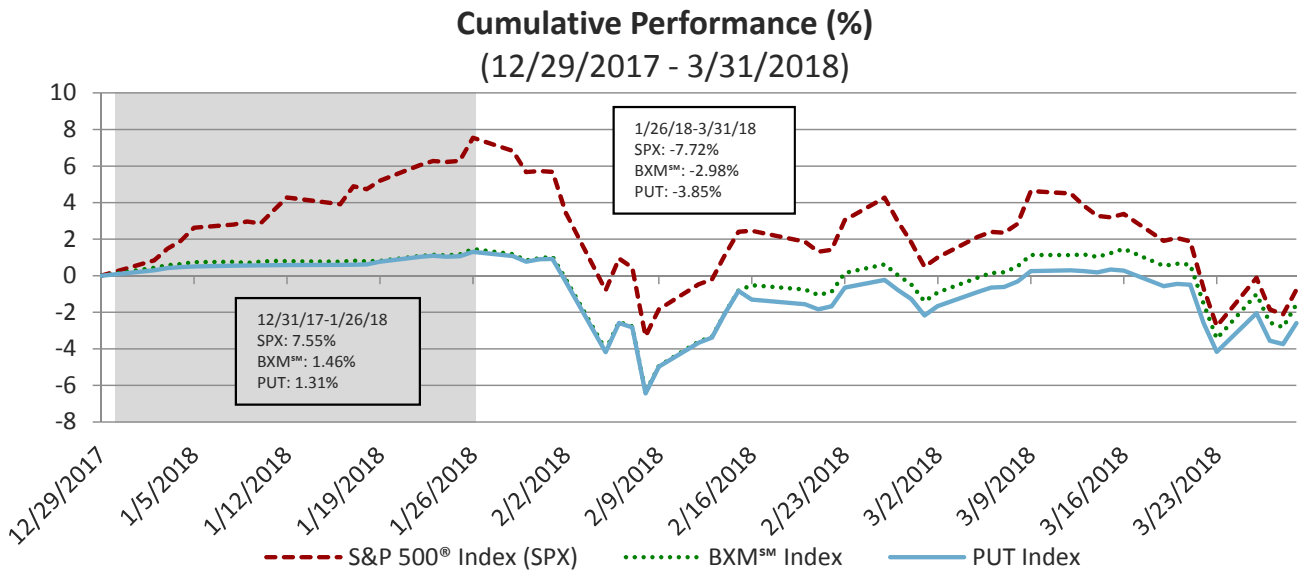


Figure 1: From the year-to-date high for the S&P 500® Index on January 26th through quarter-end, both BXM℠ and PUT experienced less than half the decline of the S&P 500® Index.
Source: Bloomberg, L.P.

What about the idea that option writing strategies benefit from elevated volatility levels? Both option writing benchmarks received higher premiums when implied volatility was elevated in February and March than they had during January when implied volatility was lower. BXM℠ collected premiums of 1.62% and 1.39% in February and March versus a premium of 0.92% in January. PUT's premiums were 0.92%, 1.35% and 1.31% for January, February and March, respectively. The longer-term relationship between VIX® levels and the premiums BXM℠ and PUT collect for writing at-the-money options can be seen in Figure 2 below.

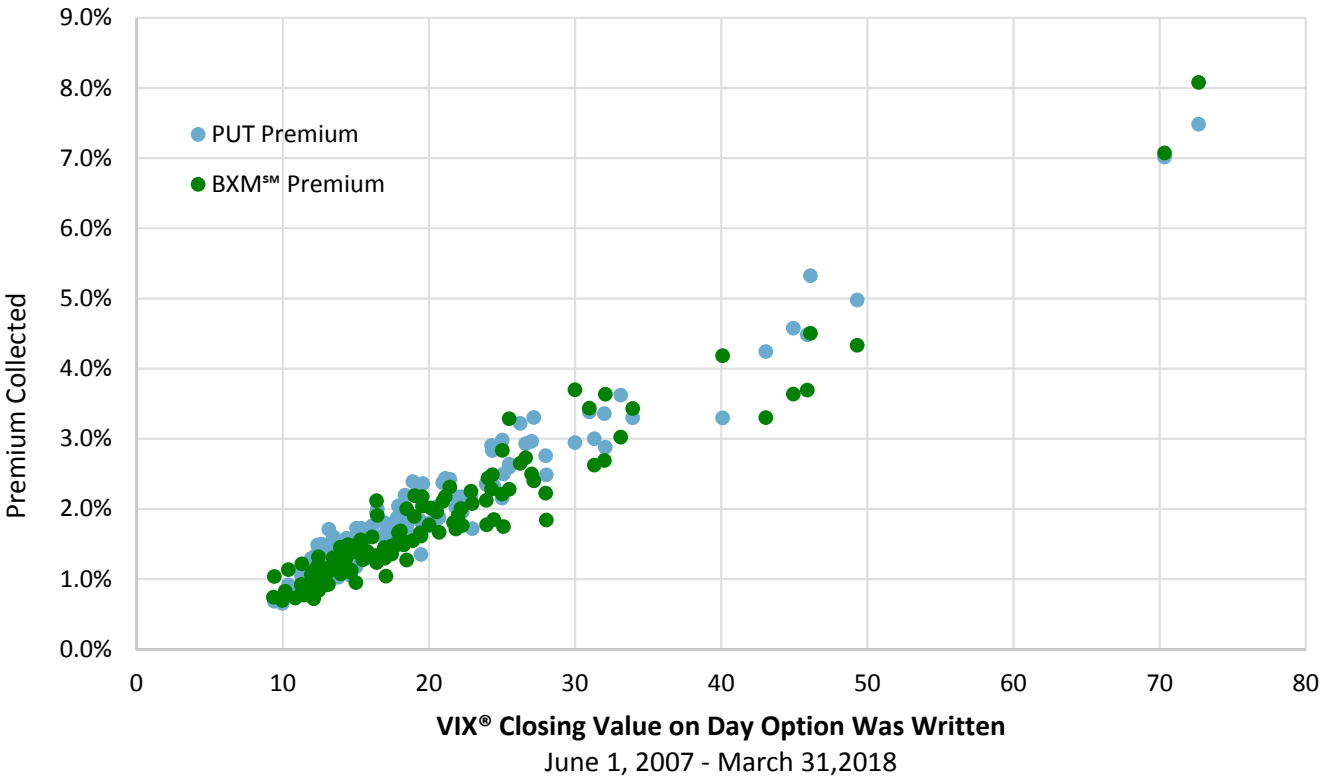


Figure 2: BXM℠ and PUT receive higher premiums at higher levels of implied volatility.
Source: Bloomberg, L.P.
BXM℠ premium is the price of the call option the BXM℠ sells divided by the set price of the S&P 500® Index. PUT Premium is the price of the put option PUT sells divided by its strike price. PUT monthly premium data not available prior to June 2007.

The total return impact of the relationship between implied volatility and option premiums can be seen in Figures 3, 4 and 5. The table in Figure 3 shows that average monthly returns for the option writing benchmarks relative to the S&P 500® Index improve as the monthly average VIX® levels increase. This improvement in relative performance happens for two reasons. The first reason is that higher volatility periods feature larger and more frequent monthly losses for the S&P 500® Index while the premiums collected by the option writing strategies tend to produce smaller and less frequent losses than the S&P 500® Index during those higher volatility periods.

		Implied Volatility Monthly Average Range (January 1988 to March 2018)					
		10 to 14	14 to 18	18 to 22	22 to 26	26 to 30	> 30
Frequency	Months	88	102	66	54	25	28
	Percentage	24%	28%	18%	15%	7%	8%
Average Monthly Return	PUT	1.0%	1.0%	0.9%	1.2%	1.0%	-1.0%
	BXM℠	1.1%	0.9%	0.8%	1.1%	0.6%	-0.9%
	SPX	1.8%	1.0%	1.4%	0.5%	-0.4%	-1.4%
Percentage of Months with Positive Returns	PUT	86%	83%	65%	74%	72%	54%
	BXM℠	85%	75%	62%	67%	68%	54%
	SPX	86%	68%	61%	52%	44%	50%

Figure 3: On average, implied volatility levels in the 22 to 26 range have historically produced the most attractive combination of absolute and relative return for the BXM℠ and PUT.
Source: Bloomberg, L.P.

The second reason for improved relative performance in higher volatility months is illustrated in Figures 4 and 5. The larger option premiums collected in higher volatility periods result in better relative returns when the market advances and improved downside protection when the market declines.

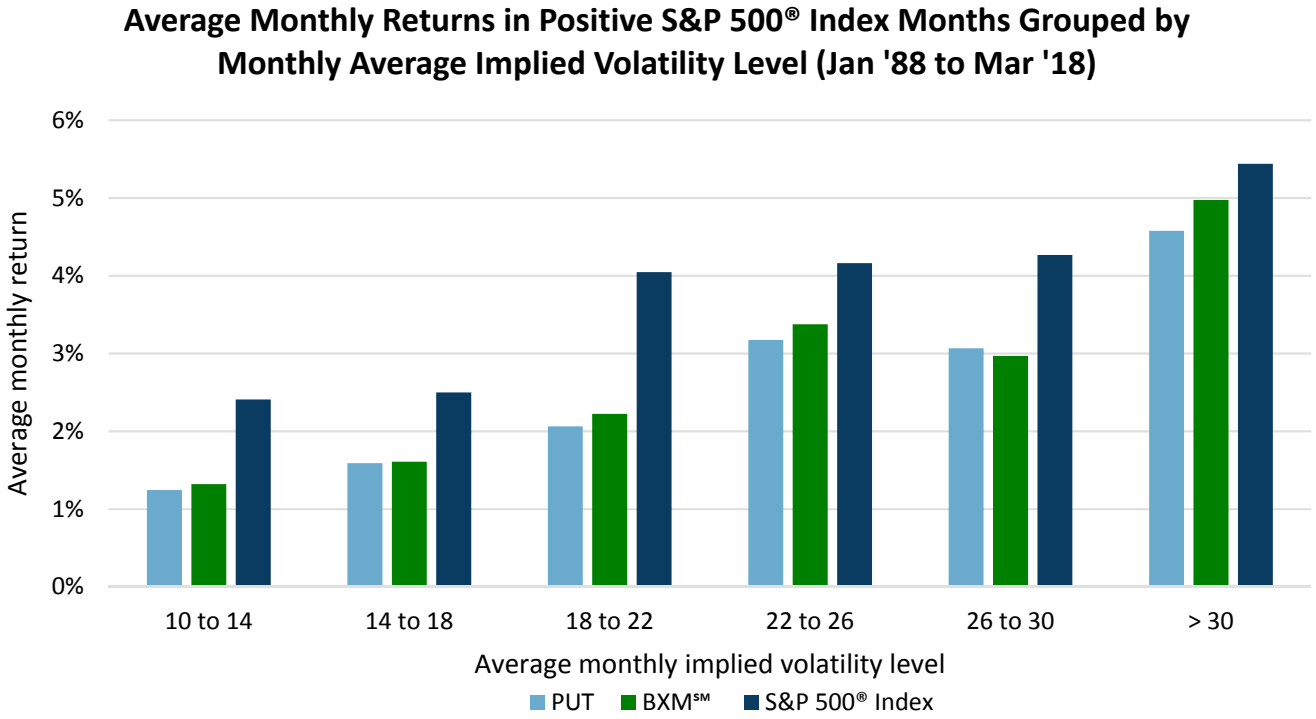


Figure 4: Historically, as implied volatility increased, higher option premiums drove higher cash flow, resulting in increased returns for BXM℠ and PUT relative to lower implied volatility levels.
Source: Bloomberg, L.P.

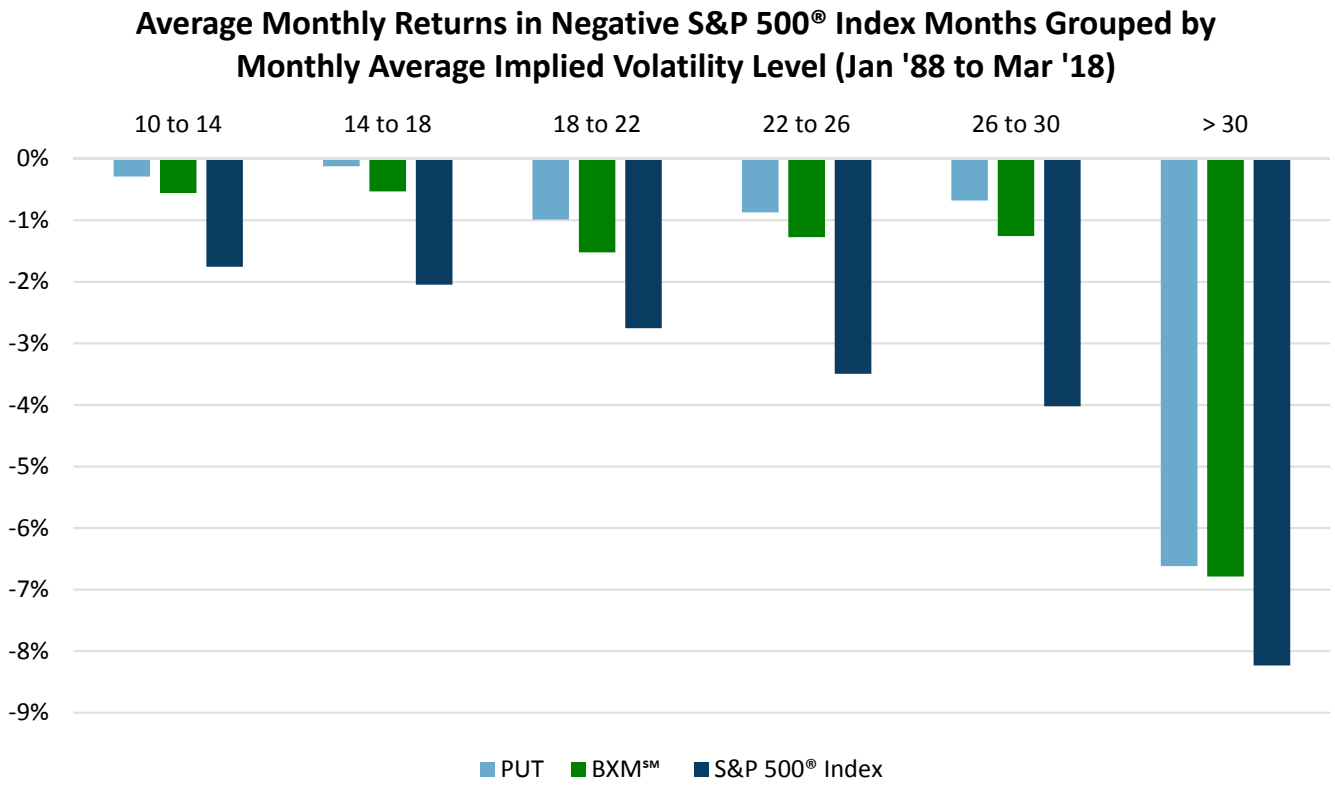


Figure 5: Historically, as implied volatility increased, higher option premiums translated into increased protection, i.e. return differential to the S&P 500® Index, for BXM℠ and PUT at all but the highest implied volatility level.
Source: Bloomberg, L.P.

Figure 5 shows that the downside protection delivered by option writing benchmarks is not as effective in extremely volatile markets, relative to markets with lower volatility levels. This phenomenon is part of the case for applying active management to option writing. The option writing benchmarks write their options once a month and hold their respective option positions until they expire the next month. This aspect of the option writing benchmarks' construction methodology makes their outcomes relative to the S&P 500® Index highly path-dependent. If there is a reversal of market direction mid-month with a large market move on one or both sides of the reversal, an option writing benchmark with a single contract can end up having much higher participation in the down leg of the reversal than the up leg. Moreover, when the reversal happens in close proximity to the day its option expires and it writes a new one, an option writing benchmark is particularly susceptible to the negative outcomes of a market reversal. Active management has the potential to soften the path dependency inherent in managing risk with one instrument that expires. This risk can potentially be reduced by writing a portfolio of options that is diversified by strike price and expiration date and also through active decision-making regarding whether or not to hold contracts to expiration.

Despite the slightly larger losses for option writing benchmarks versus the S&P 500® Index in Q1, option writing strategies remain a viable risk management approach for investors looking for reliable protection against equity market declines. If the elevated levels of implied volatility observed in February and March persist, premiums collected by option writing strategies will continue to be more attractive than premiums collected in recent years. For strategies that combine equity market exposure with option writing, the higher premiums that come with elevated volatility could help maintain positioning for improved participation in market advances relative to the participation of the market advances of recent years. Additionally, in the event the equity market falls further below January's highwater mark, these strategies are potentially well positioned to continue delivering meaningful downside protection.

Standard Performance

Average Annual Performance As of March 31, 2018					
	One Year	Three Years	Five Years	Return Since Inception*	Risk** Since Inception*
Active Index-Option Overwrite (Net)	5.33%	7.11%	7.99%	6.60%	9.70%
BXM℠ Index	6.95%	7.22%	7.42%	5.09%	11.16%
S&P 500® Index	13.99%	10.78%	13.31%	9.49%	15.05%

*Inception of Gateway Active Index-Option Overwrite Composite is April 1, 2008
** Standard deviation is based on monthly performance

Periods over one year are annualized.
Datasource: Morningstar Direct℠ and Gateway Investment Advisers, LLC
Past performance is no guarantee of future results. For important disclosures, please refer to page 6.

GATEWAY INVESTMENT ADVISERS, LLC
GATEWAY ACTIVE INDEX-OPTION OVERWRITE COMPOSITE
ANNUAL DISCLOSURE PRESENTATION

Year End	Annual Performance Results				Composite 3-Year Std. Dev	S&P 500® 3-Year Std. Dev	BXM℠ Index 3-Year Std. Dev	Number of Composite Accounts	Composite Assets (millions)	Firm Assets (millions)
	Composite		S&P	BXM℠						
	Gross	Net	500®	Index						
9 Months Ended 12/31/2008	-19.54%	-19.72%	-30.43%	-26.10%	N/A	N/A	N/A	1	$492	$7,071
2009	15.15	14.78	26.46	25.91	N/A	N/A	N/A	1	502	7,188
2010	13.30	12.91	15.06	5.86	N/A	N/A	N/A	1	516	7,699
2011	6.73	6.33	2.11	5.72	11.26%	18.97%	13.66%	1	496	8,081
2012	11.46	11.02	16.00	5.20	8.54	15.30	11.56	4	717	10,517
2013	14.91	14.46	32.39	13.26	6.28	12.11	9.39	4	1,233	12,475
2014	7.64	7.26	13.69	5.64	4.37	9.10	6.07	5	2,263	12,239
2015	5.98	5.57	1.38	5.24	5.37	10.62	6.52	6	2,404	12,210
2016	9.10	8.74	11.96	7.07	5.83	10.74	6.68	4	2,627	11,601
2017	13.83	13.44	21.83	13.00	5.47	10.07	5.83	4	2,665	12,559

N/A: The three year annualized ex-post standard deviation of the Composite and benchmarks is not presented as 36-month returns are not available. For all periods shown, the Composite has less than six accounts for the full year. As such, the Composite dispersion of portfolio returns is not applicable.

Gateway Active Index-Option Overwrite Composite contains fully discretionary hedged equity accounts that hold common stock and sell index call options on at least 95% of the underlying stock value. Indexes utilized for call option activity are U.S. domestic equity indexes that include all sectors of the economy. This call activity reduces volatility and provides cash flow. The Gateway Active Index-Option Overwrite Composite was created April 1, 2008.

For comparison purposes the Composite is measured against two indexes, the S&P 500® Index, a popular indicator of the performance of the large capitalization sector of the U. S. stock market, and, beginning January 1, 2014, the Cboe® S&P 500 BuyWrite℠ Index (the BXM℠ Index), a passive total return index designed to track the performance of a hypothetical buy-write strategy on the S&P 500® Index. The BXM℠ Index was added as a secondary index as it is viewed to be representative of the Composite strategy.

Performance results are expressed in U. S. dollars. Returns are presented gross and net of actual management fees and include the reinvestment of all income. Past performance is not indicative of future results. The annual Composite dispersion, if applicable, is an asset-weighted standard deviation calculated for the accounts in the Composite the entire year.

Net of fee performance was calculated using actual management fees. The current investment management fee schedule is as follows: 0.85% on the first $5 million; 0.65% on the next $5 million; 0.50% on the next $40 million; and 0.45% on assets in excess of $50 million. Actual investment management fees incurred by Composite accounts may vary.

Gateway Investment Advisers, LLC (Gateway) is an independent registered investment adviser and a successor in interest to Gateway Investment Advisers, L.P. as of February 15, 2008. Gateway claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS® standards. Gateway has been independently verified for the periods January 1, 1993 through December 31, 2017.

Verification assesses whether (1) the firm has complied with all the composite construction requirements of the GIPS® standards on a firm-wide basis and (2) the firm's policies and procedures are designed to calculate and present performance in compliance with the GIPS® standards. The Gateway Active Index-Option Overwrite Composite has been examined for the periods April 1, 2008 through December 31, 2017. The verification and performance examination reports are available upon request.

Policies for valuing portfolios, calculating performance and preparing compliant presentations are available upon request. A list of composite descriptions is also available upon request.