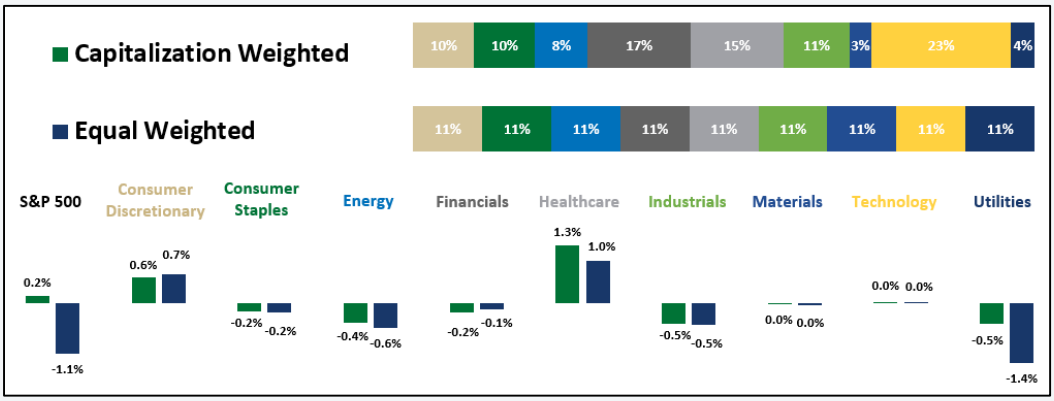
Beaumont Capital Management

Sector Rotation and Equal Weight Methodology

The premise behind a tactical sector rotation strategy is simple: pick an index, such as the S&P 500® Index, and attempt to outperform by selectively investing in its underlying sectors. While this concept is easy for investors to understand, from time to time it can produce an odd result. At times the strategy can work exactly as planned, owning the winners and avoiding the losers, and *underperform* the index. How is this possible? It is possible because the sectors in the S&P 500 are weighted based on their market capitalization, as opposed to a tactical sector rotation strategy where sectors are typically weighted equally in the portfolio. The visualization to the right illustrates this concept. The largest sector, Technology, comprises 23% of the index compared to the smallest sector, Materials, which comprises only 3% of the index. In a fully invested equal weight strategy, each sector will comprise 11% of the portfolio, creating underweight positions in certain sectors and overweight positions in others. In a given year, these disparities can create a fairly large performance differential. Take the current year for instance: Healthcare has been the best performing sector while Utilities has been the worst. Situations such as this, where the larger (underweight) sectors perform relatively better than the smaller (overweight) sectors are when an equal weight methodology is likely to detract from performance; conversely an equal weight methodology is likely to add to performance when the smaller sectors perform relatively better than the larger sectors.

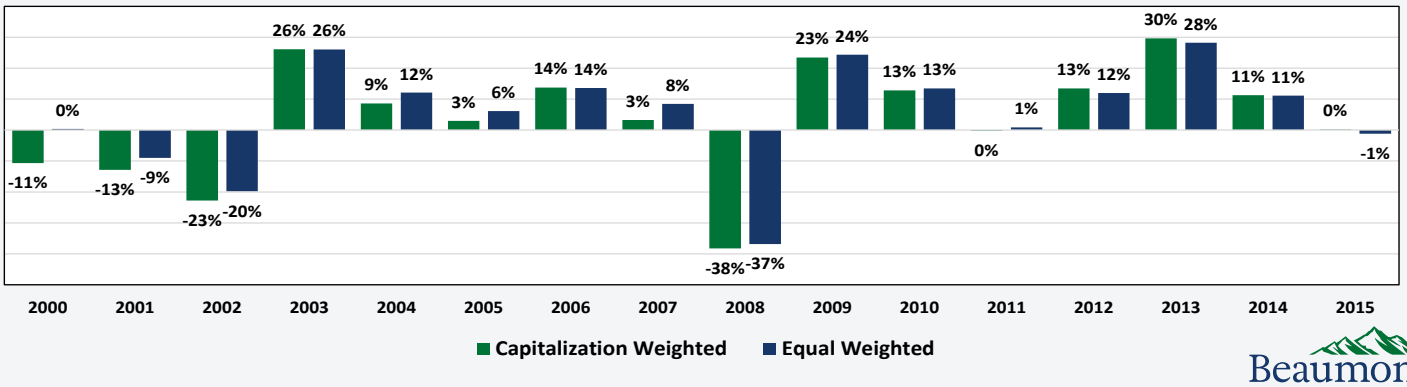
Sector Weightings and Performance Attribution[1]



Rationale Behind an Equal Weighted Portfolio

The chart below shows the prior fifteen yearly returns for both weighting methodologies. In most years the performance is relatively similar and over the time period seen equal weighting actually outperformed the market capitalization weighting. Equal weighting also could help to avoid situations where a sector's weighting, and hence allocation, increases in a bubble. This occurred in 2000, when the Technology sector reached a weighting of nearly 35% in the S&P 500[2]. As it is unlikely that we are sacrificing performance over the long term, an equal weighted methodology makes the most sense for a quantitative strategy such as sector rotation. This is because our quantitative process evaluates each sector on its individual merits. We are attempting to determine which sectors we should own and which we should not, but have no compelling reason to own differing weights of each sector. While relatively different sector weights may cause moderate performance differentials in the short term, it is important to remember that over long periods of time, the value of a sector rotation strategy isn't what it owns, but what it doesn't—and the losses it may avoid as a result.

Yearly Returns by Weighting for the S&P 500[3]



Beaumont
CAPITAL MANAGEMENT

Authored by:
Denis J. Rezendes, Research Analyst

Monday July 27th, 2015

Disclosures:

1. Performance is presented from January 1st, 2015 through June 30th, 2015, sector allocations for the market capitalization weighting are as of June 30th, 2015. Performance was derived from the daily closing prices of the State Street SPDR S&P 500 ETF (SPY) as a proxy for the S&P 500 Index and the State Street Select Sector SPDR ETFs, as listed, for sector performance: Consumer Discretionary Select Sector SPDR ETF (XLY), Consumer Staples: Consumer Staples Select Sector SPDR ETF (XLP), Energy: Energy Select Sector SPDR ETF (XLE), Financials: Financial Select Sector SPDR ETF (XLF), Healthcare: Health Care Select Sector SPDR ETF (XLV), Industrials: Industrial Select Sector SPDR ETF (XLI), Materials: Materials Select Sector SPDR ETF (XLB), Technology: Technology Select Sector SPDR ETF (XLK), and Utilities: Utilities Select Sector SPDR ETF (XLU).

2. S&P 500 Sector Weightings. (2015, March 10). Retrieved July 27, 2015, from https://www.bespokepremium.com/think-big-blog/sp-500-sector-weightings/

3. Capitalization weighted performance was derived from the daily closing prices of the State Street SPDR S&P 500 ETF (SPY) as a proxy for the S&P 500 Index, equal weighted performance was calculated using equally weighted daily performance derived from the daily closing prices of the nine State Street Select Sector SPDR ETFs as listed in 1.

This material is provided for informational purposes only and does not in any sense constitute a solicitation or offer for the purchase or sale of securities nor does it constitute investment advice for any person. The information presented in this report is based on data obtained from third party sources. Although it is believed to be accurate, no representation or warranty is made as to its accuracy or completeness.

Past performance is no guarantee of future results. Diversification does not ensure a profit or guarantee against a loss. As with all investments, there are associated inherent risks. An investment cannot be made directly in an index. The information contained above is for illustrative purposes only and does not represent the returns of an investment in any Beaumont Capital Management strategy.

The Standard & Poor's (S&P) 500® Index is an unmanaged index that tracks the performance of 500 widely held, large-capitalization U.S. stocks. Indices are not managed and do not incur fees or expenses. "S&P 500®" is a registered mark of Standard & Poor's Financial Services, LLC a division of McGraw Hill Financial, Inc.

The S&P 500 Index contains ten sectors, the State Street Select Sector SPDR ETFs include the Telecom sector as a part of the Technology Sector. For illustration purposes, equal weighted performance is calculated using the nine available State Street Select Sector SPDR ETFs.

Please contact your Relationship Manager for more information or to address any questions that you may have.

Beaumont Financial Partners, LLC- DBA Beaumont Capital Management, 250 1st Avenue,
Needham,MA 02494 (844-401-7699).

FOR INVESTMENT PROFESSIONAL AND CLIENT USE ONLY

Beaumont
CAPITAL MANAGEMENT