WASATCH GLOBAL INVESTORS

Quarterly Commentary

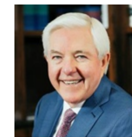
Investor
WHOSX

Wasatch-Hoisington U.S. Treasury Fund

DECEMBER 31, 2019

Thirty-Year Treasury Bond Yield Posted Lowest Close Since the Bond's Introduction in 1977

FUND MANAGERS



Van R. Hoisington
Lead Portfolio Manager
23 YEARS ON FUND

V.R. Hoisington Jr.
Portfolio Manager
3 YEARS ON FUND

David Hoisington
Portfolio Manager
3 YEARS ON FUND

OVERVIEW

The views expressed in this commentary are those of Hoisington Investment Management Company, the sub-advisor to the Fund, and may differ from the views of Wasatch Global Investors.

For the three months ended December 31, 2019, the Fund declined -5.22%, compared to the 0.18% increase in the benchmark Bloomberg Barclays US Aggregate Bond Index. For the 12-months ended December 31, 2019, the Fund returned 17.15%, outperforming the Index, which returned 8.72%. For the past three-, five- and 10-year periods and since the Fund's inception on December 6, 1986 through December 31, 2019, the Fund outperformed the benchmark.

The yield on the 30-year Treasury bond declined from 3.02% at the end of 2018, to 2.39% on December 31, 2019. This was the lowest yearly close for the 30-year bond since its introduction in 1977. The average yield of long-term Treasuries (maturities longer than 20 years) for the year was 2.5%, the second lowest since 1950.

Data show past performance and is not indicative of future performance. Current performance may be lower or higher than the data quoted. For the most recent month-end performance data, visit wasatchglobal.com. Investment returns and principal value will fluctuate and shares, when redeemed, may be worth more or less than their original cost. The Advisor may absorb certain expenses, leading to higher total shareholder returns. Wasatch Funds will deduct a 2% redemption fee on Fund shares held 60 days or less. Performance data does not reflect this redemption fee or taxes. ***Total Expense Ratio: 0.70%. The Advisor has contractually agreed to limit certain expenses to 0.75% through at least 1/31/2020.***

DETAILS OF THE QUARTER AND YEAR

The lack of inflation was once again the driving force as evidenced by the core personal consumption expenditures deflator, which dropped from 2% in December 2018 to 1.6% at the end of 2019. Inflationary expectations followed the inflation retreat. As of November 30, 2019, the median University of Michigan Survey of Expected Change in Prices During the Next 5 to 10 Years dropped to a record low of 2.2%. Also, the Federal Reserve Bank of New York Survey of Consumer Expectations declined over the course of the year for both the one- and three-year expected inflation rates. As of November 30, 2019, the median one-year expected inflation rate dropped to 2.35% from 3.00%, while the median three-year view was 2.52%, down from 2.98%.

REAL RATES

U.S. economic performance in 2019 was substantially below expectations. This was most evident in observing Federal Reserve (Fed) actions. In December 2018, the Fed increased the federal-funds target range from 2.0% to 2.25% on September 27 to 2.25% to 2.5% on December 20, while simultaneously announcing that three more rate hikes would likely be necessary in 2019. Instead, the year unfolded with the Fed cutting the target rate three times, ending at a range of 1.5% to 1.75% on October 31, 2019 as economic activity disappointed. Lower economic growth and the decline in inflation expectations reinforced investors' perception that lower real yields were warranted. The decline in U.S. real yields was consistent with global trends. Over the past 20 years, real yields have fallen, albeit irregularly, in Japan, the euro area and the United Kingdom. Based on yearly averages, real sovereign yield levels were at 21-year lows in the U.S. and all three of these other major economic regions. It is important to note that the movement of real yields appears to be associated with changing economic output, as real yields were more negative in Japan, the euro area and the U.K. than in the U.S. This reflects that U.S. economic growth, while disappointing, has exceeded that of these other economic regions.

Last year's exceptional decline in long-term U.S. Treasury bond yields occurred in spite of a large tax cut and a huge increase in federal spending in 2018 and 2019 that were financed by a major acceleration in federal debt. The benefits of these fiscal actions were largely confined to the second and third quarters of 2018, and were followed by the negative effects of inordinately high federal debt. Thus, the events of 2019 help to confirm that federal debt accelerations eventually lead to lower, not higher, bond yields.

LOWER GROWTH, INFLATION AND INTEREST RATES

Five considerations indicate that inflation, real growth and interest rates will be lower in 2020 than in 2019. First, momentum is to the downside since 2019 economic growth was fading as the domestic and global economies prepared to enter the new year. Second, U.S. monetary conditions are still restrictive. Third, the domestic and worldwide debt overhang became even greater in 2019. Fourth, average economy-wide profits in the U.S. have been flat since 2012. Fifth, excess manufacturing capacity is greater than a year ago, indicating that firms do not having pricing power.

1. Loss of Momentum

Based on yearly averages, in 2019 economic growth slowed both worldwide and in each of the four largest economic areas—the United States, China, Japan and the euro area. In the U.S., real gross domestic product (GDP) growth dropped from 2.9% to 2.3%, accompanied by noticeable declines in the euro area and China. Japan's growth held up better due to anticipatory consumer buying ahead of a major increase in the consumption tax on October 1, 2019, but as the year ended, recessionary indications were

widespread. Many other countries experienced similar fates, with Mexico leading a list of poor results from Latin America. Such typical stalwarts as India, Korea, Singapore and Canada were also exhibiting considerable frailties. Confirming the slowing GDP, the growth rate in the volume of world trade, as measured by Netherlands Bureau for Economic Policy Analysis, slipped from 4.9% in 2017 to 3.4% in 2018, and a 0.4% decrease in the first 10 months of 2019.

It might appear that global economic prospects for 2020 are better due to a potential first-round trade agreement between the U.S. and China and possible passage of the U.S.-Mexico-Canada Agreement (USMCA) on trade. Furthermore, scattered economic numbers may indicate a shallowing out of the global economic deterioration. However, incrementalism will not reverse the current situation. The fact is that the deleterious nature of excessive debt and monetary problems will prevent a turnaround in the negative trajectory of growth in the world's estimated $88 trillion economy.

2. Monetary Restraint

A restrictive monetary stance may not seem to be characterized by M2 growing at an 8.6% annual rate in the last six months, a meteoric rise in the Fed's holdings of U.S. Treasury securities of $218.6 billion, and three cuts in the target rate during 2019, however, monetary effects are a complex process. Historical instances have occurred when a surge in M2 growth was followed by an acceleration in economic growth and/or inflation. But the trend in bank loans and money velocity indicate that this will not be the case in the present situation. There are noticeable differences between the current surge in M2 and other monetary variables when compared to the monetary expansion during the first quantitative easing (QE1), which incidentally provided only a modest lift to economic growth and no sustainable increase in inflation.

After QE1, the two-year annualized rate of growth in M2 rose above the post-1900 average growth rate of 6.6%, while the latest two-year number is 4.5%. As the research of Nobel Laureate Milton Friedman documented, the typical lags between monetary change and economic fluctuations cluster around two years, confirming the importance of the two-year time frame. After QE1, the growth rate in M2 accelerated. At that time the two-year annualized rate of growth in total commercial bank loans and leases accelerated from negative to positive, indicating that a potential expanding monetary process might be underway. In the second half of 2019, this growth rate in bank loans and leases decelerated and the two-year annualized rate of growth in M2 continued to decrease, falling to a 14-year low. Thus, based on these historical lags, in corroboration with current trends in loans and velocity, monetary conditions are still restrictive. This growth rate in bank loans is a reliable cyclical indicator, decelerating prior to the post-1950 recessions.

There is, however, a further reason not to be alarmed by the recent surge in money. The simultaneous acceleration in M2 and loan growth in response to QE1 was neutralized by a sharp decline in M2 velocity. This means that the money and loan growth did not find its way into the real economy.

That is happening again, with M2 velocity declining for the past five consecutive quarters. A large decline in velocity is also a high probability for the fourth quarter of 2019. During the year, velocity was extremely close to the lowest levels recorded since 1950. As Fisher originally noted, velocity declines in highly over-indebted economies.

M2 growth in the euro area, Japan and China in the latest 12 months were all below their peaks of the decade. China's M2 growth rate fell from 29.6% to 8.2%. In Japan, the drop was from 4.3% to 2.8%. Most recently year-over-year growth in M2 in the euro area was 6.1%, which is an

acceleration from its lows but still down from its 6.7% peak. Although the history of M2 velocity is far more limited outside of the U.S., the levels of velocity in all three of these areas were at or near historic lows and far below that in the U.S. In the euro area, money turned over 0.98 times in 2019, with money turnover around 0.5 in both Japan and China, where the marginal revenue product of debt is the lowest among the major economies. Also, a composite of velocity for the U.S. and the other three areas fell again in 2019, continuing the severe downward trend since the late 1990s.

3. Decreasing Marginal Revenue Product of Debt

Each additional dollar of total nonfinancial debt outstanding over the first two quarters of 2019 generated 40 cents of GDP in the U.S., a contribution to growth that was 25% lower than 20 years ago. The contribution of each additional dollar of debt was far worse in the other major economies. In the euro area and Japan, debt generated only 38 and 26 cents of GDP growth, respectively. In the first two quarters of last year, each dollar of debt generated only 37 cents in the U.K. In China, the number was 38 cents for 2019, a decline of 57.5% from 20 years ago. The declining marginal revenue product of debt reconfirms that excessive debt usage is triggering the law of diminishing returns, which results in weaker growth in real GDP. In the euro area, Japan and China, economic policy is relying heavily on debt-financed fiscal operations to try to reverse weak economic conditions. This method has been demonstrated to be a self-defeating process.

While the aggregate debt problem is not as bad in the U.S. as in other major economies, debt levels are unprecedented in the government and corporate sector, and thus should serve as a major constraint on U.S. economic growth. Gross U.S. government debt outstanding increased to 107% of GDP late last year, the highest since the 1940s. Moreover, the bipartisan omnibus budget combined with continuing growth in off-budget increases in debt will push the government debt ratio to steadily higher levels in the years ahead. Substantial peer-reviewed economic research indicates that the U.S. economy loses one-third of its trend economic growth rate when the government debt ratio rises above 90% for a period of five years. The U.S. has met that condition since 2014. When viewed from a cyclical perspective, the increase in federal debt in 2018 and 2019 is even more serious. In late-stage expansions, economic theory indicates that budget deficits should be reduced and the debt-to-GDP ratio should fall. Deterioration in economic conditions would lead to a quick worsening, pushing the debt-to-GDP ratio further into uncharted waters, even without new fiscal measures that would likely be enacted in such circumstances.

U.S. corporate debt surged to a record 47% of GDP in the third quarter of 2019, three percentage points above the peak during the financial crisis of 2008-09. Total business debt, which includes incorporated and unincorporated firms, also surged to a record of 75% of GDP in the third quarter of 2019, two percentage points more than the 2008-09 level.

4. Stagnant Profits

In the third quarter of 2019, Corporate Profits After Tax IVA CCAdj, stood at $1.87 trillion, up from $1.71 trillion in the first quarter of 2012, a gain of $163 billion. However, the before-tax gain was a paltry $53 billion over the nearly eight-year span, or an increase of just 0.4% per year. This means that the tax cut accounted for two-thirds of the rise of aggregate profits since 2012. In real terms, corporate profits declined since inflation rose about five times more than the yearly average increase in profits. Thus, firms have had funds to spend, but not relative to the needs of the real economy.

When Corporate Profits After Tax IVA-CCAdj are viewed broadly as a percent of GDP, it is clear that profits have not kept up with the demands of an expanding economy. This ratio displays an interesting cyclical pattern that has pointed to the inception of business cycle recessions. This ratio dropped from 10.6% in the first quarter of 2012 to 8.7% in the third quarter of 2019. In real terms, since 2012 this ratio has declined 9.6% after adjusting for inflation.

In view of the stagnant corporate-profits situation, the 2019 drop in real capital spending is not surprising. Neither is the weakness in key leading indicators of capital spending. In the latest 12 months, the unfilled orders of non-defense capital goods excluding aircraft, fell 2.3%, compared with a peak increase of 3.8% in late 2017. New orders for this key area of the economy were up a mere 0.5% in the latest 12 months, a sharp decrease from the peak of over 13% in early 2017.

5. Mounting Excess Capacity

Substantial excess manufacturing capacity developed in the U.S. during 2019 in the face of slower growth and will serve to put downward pressure on inflation. Total industrial capacity of the nation's manufacturing, mining and utility companies was 77.3% in November 2019, 2.3 percentage points less than the peak reached about a year earlier and at a lower level than when the U.S. economy entered all of the recessions since 1970. Manufacturing firms were operating at even a lower rate, 75.2% late in 2019, compared to the post-1950 average of 79.9%.

The Organization for Economic Cooperation and Development (OECD) indicates that industrial sector capacity use has moved steadily lower for all OECD countries over the past five years. The latest reading showed two percentage points less capacity utilization than the cyclical peak five years ago. This provides confirmation that global manufacturing is in a recession and is a contributing factor to the list of reasons why disinflation is global.

Poor capacity use rates have broad economic implications. They serve to weaken corporate profits while simultaneously undermining capital expenditures. Thus, poor capital use rates reflect economic weakness while contributing to a persistence of these conditions in the future.

OUTLOOK FOR 2020

These five factors—loss of momentum, monetary restraint, high debt levels, flat profits and excess capacity—are expected to bring about slower growth and continue to subdue core inflation in 2020. Over the past 65 years, yields on long-dated (maturities longer than 20 years) U.S. Treasury securities (free from credit risk) moved in the same direction as core inflation on an annual basis roughly 80% of the time. We believe there is a high probability that this relationship will hold in 2020 as inflationary pressures continue to subside.

Such an environment would likely bode well for the Fund's investments in long-dated U.S. Treasury securities.

Thank you for the opportunity to manage your assets.

Sincerely,

Van Hoisington, V.R. Hoisington Jr. and
David Hoisington

AVERAGE ANNUAL TOTAL RETURNS

FOR PERIODS ENDED DECEMBER 31, 2019

	Quarter*	1 Year	3 Years	5 Years	10 Years
U.S. Treasury Fund	-5.22%	17.15%	7.56%	3.96%	7.93%
Bloomberg Barclays US Aggregate Bond Index**	0.18%	8.72%	4.03%	3.05%	3.75%

**Returns less than one year are not annualized.*

Data show past performance, which is not indicative of future performance. Current performance may be lower or higher than the data quoted. To obtain the most recent month-end performance data available, please visit wasatchglobal.com. The Advisor may absorb certain Fund expenses, without which total return would have been lower. Investment returns and principal value will fluctuate and shares, when redeemed, may be worth more or less than their original cost. **Total Expense Ratio: 0.70%**

Total Annual Fund Operating Expenses include operating expenses, including the management fee, before any expense reimbursements by the Advisor. **The Advisor has contractually agreed to limit certain expenses to 0.75% through at least 1/31/2020.** See the prospectus for additional information regarding Fund expenses.

Wasatch Funds will deduct a 2.00% redemption fee on Fund shares held 60 days or less. Performance data does not reflect the deduction of fees or taxes, which if reflected, would reduce the performance quoted. For more complete information including charges, risks and expenses, read the prospectus carefully.

Investing in bonds, you are subject, but not limited to, the same interest rate, inflation and credit risk associated with the underlying bonds owned by the Fund. Return of principal is not guaranteed. Interest rate risk is the risk that a debt security's value will decline due to changes in market interest rates. The interest rate is the amount charged, expressed as a percentage of principal, by a lender to a borrower for the use of assets. Even though some interest-bearing securities offer a stable stream of income, their prices will fluctuate with changes in interest rates. Inflation risk is the possibility that inflation will reduce the purchasing power of a currency, and subsequently reduce the value of a security or asset, and may result in rising interest rates. Inflation is the overall upward price movement of goods and services in an economy that causes the value of a dollar to decline. Credit risk is the risk that the issuer of a debt security will fail to repay principal and interest on the security when due. Credit risk is affected by the issuer's credit status, and is generally higher for non-investment grade securities.

An investor should consider investment objectives, risks, charges and expenses carefully before investing. To obtain a prospectus, containing this and other information, visit wasatchglobal.com or call 800.551.1700. Please read the prospectus carefully before investing.

***The Bloomberg Barclays US Aggregate Bond Index is a broad-based flagship benchmark that measures the investment grade, US dollar denominated, fixed-rate taxable bond market. The index includes Treasuries, government-related and corporate securities, mortgage-backed securities (MBS) (agency fixed-rate and hybrid adjustable-rate mortgage [ARM] pass-throughs), asset-backed securities (ABS) and commercial mortgage-backed securities (CMBS) (agency and non-agency). You cannot invest directly in this or any index.*

The Wasatch-Hoisington U.S. Treasury Fund's investment objective is to provide a rate of return that exceeds the rate of inflation over a business cycle by investing in U.S. Treasury securities with an emphasis on both income and capital appreciation.

Sources: Hoisington Investment Management Co., Bureau of Economic Analysis, Congressional Budget Office, Office of Management and Budget, Bureau of Economic Analysis, U.S. Federal Reserve, economists Nathan S. Balke, Robert J. Gordon and Christina D. Romer, www.measuringworth.com, Bureau of Labor Statistics, Haver Analytics, Netherlands Bureau for Economic Policy Analysis, Bank for International Settlements and the Organization for Economic Cooperation and Development.

Corporate profits with IVA and CCAdj is the income that arises from current production, measured before income taxes, of organizations treated as corporations in the national income and product accounts. With several differences, this income is measured as receipts less expenses as defined in federal tax law.

Among these differences are: Receipts exclude capital gains and dividends received; expenses exclude bad debt, depletion, and capital losses; inventory withdrawals are valued at current cost; and depreciation is on a consistent accounting basis and valued at current replacement cost.

The federal-funds rate is the interest rate at which private depository institutions (mostly banks) lend balances (federal funds) at the Federal Reserve to other depository institutions, usually overnight. It is the interest rate banks charge each other for loans.

The global financial crisis, also known as the financial crisis of 2008-09 and 2008 financial crisis, is considered by many economists to have been the worst financial crisis since the Great Depression of the 1930s.

The government debt-to-GDP ratio is the ratio of a country's public debt to it gross domestic product (GDP). By comparing what a country owes to what it produces, the debt-to-GDP ratio indicates the country's ability to pay back its debt. Often expressed as a percentage, the ratio can be interpreted as the number of years needed to pay back debt if GDP is dedicated entirely to debt repayment.

Gross domestic product (GDP) is a basic measure of a country's economic performance and is the market value of all final goods and services made within the borders of a country in a year.

M2 money supply consists of currency and checking accounts, consumer-type time and savings accounts and equivalent near monies, while M3 money supply consists of M2 plus business-type time deposits and less liquid near monies. Both M2 and M3 exclude monies and near monies owned by the Treasury, depository institutions and foreign banks and official institutions and IRA and Keogh balances owned by consumers.

The marginal revenue product of debt is the change in GDP relative to the change in debt.

The Netherlands Bureau for Economic Policy Analysis (CPB) does scientific research aimed at contributing to the economic decision-making process of politicians and policymakers.

The Organization for Economic Cooperation and Development (OECD) is a forum where the governments of 34 democracies with market economies work with each other, as well as with more than 70 non-member economies to promote economic growth, prosperity and sustainable development.

The Personal Consumption Expenditures (PCE) Deflator is part of the National Income and Products Accounts developed by the Bureau of Economic Analysis of the U.S. Commerce Department. The PCE Deflator is a variable weighted index and is widely considered to be the most reliable of all the price indexes.

Quantitative easing (QE) is a government monetary policy used to increase the money supply by buying government securities or other securities from the market. Quantitative easing increases the money supply by flooding financial institutions with capital in an effort to promote increased lending and liquidity.

The velocity of money (V) is defined as the rate at which money circulates, changes hands or turns over in an economy.

U.S. TREASURY FUND — TOP 10 HOLDINGS

AS OF SEPTEMBER 30, 2019

Security Name	Percent of Net Assets
U.S. Treasury Strip, principal only, 8/15/45	24.1%
U.S. Treasury Bond, 2.250%, 8/15/46	23.7%
U.S. Treasury Strip, principal only, 5/15/44	14.9%
U.S. Treasury Bond, 3.000%, 8/15/48	14.3%
U.S. Treasury Bond, 2.500%, 2/15/45	9.2%
U.S. Treasury Strip, principal only, 8/15/40	6.8%
U.S. Treasury Note, 2.250%, 8/15/49	4.6%
U.S. Treasury Bond, 2.875%, 5/15/49	1.9%
Total	99.4%

Portfolio holdings are subject to change at any time. References to specific securities should not be construed as recommendations by the Fund or its Advisor. Current and future holdings are subject to risk.