

As a buyer of credit default swaps, an Underlying Fund is subject to certain risks in addition to those described under “—Derivatives,” above. In circumstances in which an Underlying Fund does not own the debt securities that are deliverable under a credit default swap, an Underlying Fund is exposed to the risk that deliverable securities will not be available in the market, or will be available only at unfavorable prices, as would be the case in a so-called “short squeeze.” While the credit default swap market auction protocols reduce this risk, it is still possible that an auction will not be organized or will not be successful. In certain instances of issuer defaults or restructurings, it has been unclear under the standard industry documentation for credit default swaps whether or not a “credit event” triggering the seller’s payment obligation had occurred. The creation of the International Swaps and Derivatives Association Credit Derivatives Determination Committee (the “Determination Committee”) is intended to reduce this uncertainty and create uniformity across the market, although it is possible that the Determination Committee will not be able to reach a resolution or do so on a timely basis. In either of these cases, an Underlying Fund would not be able to realize the full value of the credit default swap upon a default by the reference entity.

As a seller of credit default swaps, an Underlying Fund incurs leveraged exposure to the credit of the reference entity and is subject to many of the same risks it would incur if it were holding debt securities issued by the reference entity. However, an Underlying Fund will not have any legal recourse against the reference entity and may not benefit from any collateral securing the reference entity’s debt obligations. In addition, the credit default swap buyer may have broad discretion to select which of the reference entity’s debt obligations to deliver to an Underlying Fund following a credit event and may choose the obligations with the lowest market value in order to maximize the payment obligations of the Underlying Fund.

The Underlying Funds also enter into credit default swap recovery locks. Under a recovery swap, the parties agree in advance to the recovery rate if a credit event occurs with respect to the reference entity. The actual price of the debt securities of the reference entity at the time of the credit event may be more or less than the agreed upon recovery rate.

In addition, credit default swaps generally trade on the basis of theoretical pricing and valuation models, which may not accurately value such swap positions when established or when subsequently traded or unwound under actual market conditions. The credit default market may become subject to increased regulation, which could increase costs or even prevent participation by an Underlying Fund.

The credit default swap market in high yield securities is comparatively new and rapidly evolving compared to the credit default swap market for more seasoned and liquid investment grade Securities. Swap transactions dependent upon credit events are priced incorporating many variables including the pricing and volatility of the common stock, potential loss upon default and the shape of the U.S. Treasury Yield curve, among other factors. As such, there are many factors upon which market participants may have divergent views.

Non-U.S. Securities and Emerging Markets

The Underlying Funds trade and invest in Securities of companies domiciled or operating in one or more non-U.S. countries and makes other investments in entities located outside the U.S.,