

Hedged Income Fund Commentary



Market Overview

The S&P 500 Index returned 7.5% during the quarter. Ten-year U.S. Treasury yields declined more than 40 basis points (0.40%) during the quarter as investors contemplated lower inflation on the horizon counterbalanced by growing fears of a U.S. recession. In anticipation of an end to the Federal Reserve's (The Fed) cycle of monetary tightening, the technology-heavy NASDAQ Composite Index rallied 17% during the quarter. This, in turn, was driven by the largest individual stocks in the Index, such as Apple and Microsoft. The Equal-Weighted S&P 500 Index only returned 2.9% during the quarter, highlighting weak breadth as sectors that contain the largest individual stocks (technology, communication services, and consumer discretionary) significantly outperformed the sectors that do not (such as energy and financials).

Positioning the Hedged Income Fund

Portfolio composition is subject to change.

The Fed remains committed to fighting inflation at the cost of slowing the economy (even possibly into

a recession). We remain concerned that consensus outlooks for economic growth and earnings estimates are too high given these circumstances. As such, we continue to position the Fund for the late portion of the economic cycle via lower exposure to cyclical and high-beta (more volatile) stocks.

Why Should Investors Consider Investing in This Fund?

We believe the Fund's ability to protect the downside with put options makes it an attractive strategy in the current investment climate where economic risks and financial market volatility are rising.



DISCLOSURES

An investor should consider a fund's investment objectives, risks and charges and expenses carefully before investing or sending money. This and other important information about an investment company can be found in the fund's prospectus. To obtain a Cavanal Hill Funds prospectus or summary prospectus, please call 800-762-7085 or visit us at www.cavanalhillfunds.com. Please read it carefully before investing.

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The **S&P 500 Index** is regarded as a gauge of the U.S. equities market. This index includes 500 leading companies in leading industries of the U.S. economy. Although the S&P 500 focuses on the large-cap segment of the market, with approximately 75% coverage of U.S. equities, it is also an ideal proxy for the total market. This index is unmanaged and does not reflect the deduction of the expenses associated with a mutual fund, such as investment management and fund accounting fees. The Fund's performance reflects the deduction of fees for these services, but does not reflect the deduction of taxes that a shareholder would pay on fund distributions or the redemption of fund shares. Investors cannot invest directly in an index.

Investment Risks

The market value of a security may move up and down, sometimes rapidly and unpredictably. The value of a security may decline for a number of reasons which directly relate to the issuer, such as management performance, earnings and sales trends, investor perceptions financial leverage or reduced demand for the issuer's goods or services.

The risk of investing in derivative instruments, including liquidity, interest rate, market, credit and management risks, mispricing or improper valuation. Changes in the value of a derivative may not correlate perfectly with the underlying asset, rate or index, and the Fund could lose more than the principal amount invested. The risk of potential losses if equity markets or an individual security do not move as expected and the potential for greater losses than if these techniques had not been used. By writing covered call options, a fund will not benefit from any potential increases in the value of a fund asset above the exercise price, but will bear the risk of declines in the value of the asset. Writing call options may expose a fund to additional costs. Writing of covered call options are also subject to the risk that the counterparty to the transaction will not fulfill its obligations.

As a large percentage of a Fund's assets may be invested in a limited number of securities, each investment has a greater effect on a Fund's overall performance and any change in the value of those securities could significantly affect the value of your investment in the fund. Investments of a "non-diversified" mutual fund are not required to meet certain diversification requirements under Federal law. Compared with "diversified" portfolios, a non-diversified fund may invest a greater percentage of its assets in the securities of an issuer. A decline in the value of those investments would cause the Fund's overall value to decline to a greater degree than if the Fund held more diversified holdings. There is no guarantee that the investment techniques and risk analyses used by the Fund's portfolio managers will produce the desired results.

The fund's investment in dividend-paying stocks could cause the fund to underperform similar funds that invest without consideration of a company's track record of paying dividends. Stock of companies with a history of paying dividends may not participate in a broad market advance to the same degree as most other stocks, and a sharp rise in interest rates or economic downturn could cause a company to unexpectedly reduce or eliminate its dividend.

The risk that the stocks of mid-capitalization companies often have greater price volatility, lower trading volume, and less liquidity than the stocks of larger, more established companies. Small cap companies may be more vulnerable to adverse business or economic developments. They may also be less liquid and/or more volatile than securities of larger companies or the market averages in general.

Small cap companies may be adversely affected during periods when investors prefer to hold securities of large capitalization companies.

If positions held by the Fund were treated as "straddles" for federal income tax purposes, or a Fund's risk of loss with respect to a position was otherwise diminished as set forth in Treasury Regulations, dividends on stocks that are a part of such positions would not constitute qualified dividend income subjects to such favorable income tax treatment or qualify for the dividends received deduction for corporate shareholders. In addition, generally, straddles are subject to certain rules that may affect the amount, character and timing of the Fund's gains and losses with respect to straddle positions by requiring, among other things, that 1) any loss realized on disposition of one position of a straddle may not be recognized to the extent that the Fund has unrealized gains with respect to the other position in such straddle; 2) the Fund's holding period in straddle positions be suspended while the straddle exists (possibly resulting in a gain being treated as short-term capital gain rather than long-term capital gain); 3) the losses recognized with respect to certain straddle positions that are part of a nixed straddle and that are non-section 1256 contracts to be treated as 60% long-term and 40% short-term capital loss; 4) losses recognized with respect to certain straddle positions that would otherwise constitute short-term capital losses be treated as long-term capital losses; and 5) the deduction of interest and carrying charges attributable to certain straddle positions may be deferred.