

Ultra Short Tax-Free Income Fund Commentary



Market Overview

The third quarter was fairly quiet in the short end of the municipal market, as yields remained muted due to the continued theme of solid supply offset by steady inflows into municipal bond funds. It's evident that many investors are willing to accept lower yields in anticipation of rates rising in the lower end during the coming months once the Federal Reserve begins tapering its purchase program. As a result of the demand on the short end, the SIFMA index, which is an average of variable rate demand notes (VRDNs), was 0.02% for the entire quarter until the last week of September, when it moved up to 0.05%. Yields in the 1-year fixed rate market were similarly range-bound throughout the period, with a slight uptick at the end of the quarter.

Positioning the Ultra Short Tax-Free Income Fund

Portfolio composition is subject to change.

Given the low VRDN yields, the Fund reduced its exposure to that sector while increasing its fixed

rate holdings. The Fund will continue to look for opportunities in the fixed rate market going forward as well, as the Fed has reiterated its stance of keeping the overnight lending rate near zero for the foreseeable future.

Notable Changes to the Portfolio

As mentioned above, the Fund shifted its investment mix by extending duration through the purchase of fixed rate bonds while reducing its VRDN exposure.

Why should investors consider investing in this Fund?

While yields in the short end of the fixed income markets are low, we believe municipal bonds continue to offer value on a tax-equivalent basis and the Fund is relatively stable from a net asset value perspective, which is especially important if rates begin to rise.



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 SIFMA Municipal Swap index is a 7-day high-grade market index comprised of tax-exempt VRDOs reset rates that are reported to the Municipal Securities Rule Making Board's (MSRBs) SHORT reporting system. The index is calculated on an actual/actual basis and is published every Wednesday by 4pm Eastern Time. The bonds going into the index are selected from all eligible bonds reporting data through the SHORT system that meet the index criteria as set forth by SIFMA. The index is calculated by Bloomberg as the calculation agent for SIFMA.

Investment Risks

Fixed income securities are subject to interest rate risks. The principal value of a bond falls when interest rates rise and rise when interest rates fall. During periods of rising interest rates, the value of a bond investment is at greater risk than during periods of stable or falling rates. Short term investment grade bonds offer less risk and generally a lower rate of return than longer term higher yielding bonds. Bond funds will tend to experience smaller fluctuations in value than stock funds. However, investors in any bond fund should anticipate fluctuations in price, especially for longer term issues and in environments of changing interest rates. The Fund's income may be subject to certain state and local taxes and, depending on one's tax status, to the federal alternative minimum tax.