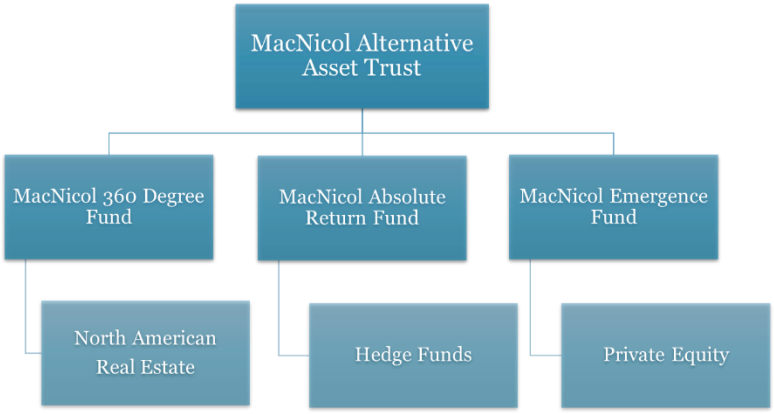
Alternative Asset Trust Fourth Quarter Report: December 31st, 2018

The MacNicol Alternative Asset Trust is a multi-strategy, alternative investment platform designed to generate positive and uncorrelated returns against the public stock and bond markets. The Trust, through its underlying limited partnerships, is invested in private real estate and mortgages, private equity and multi-strategy hedge funds. Combined, the Alternative Trust is invested in more than 150 separate real estate projects, mortgages, hedge funds and private securities. The advantage of combining different alternative asset classes and high yield investments into one Fund include tremendous diversification, enhanced liquidity, and a more predictable and less volatile pattern of returns when compared against the performance of the individual asset classes themselves.

Chart 1 – Investment Structure MacNicol Alternative Trust

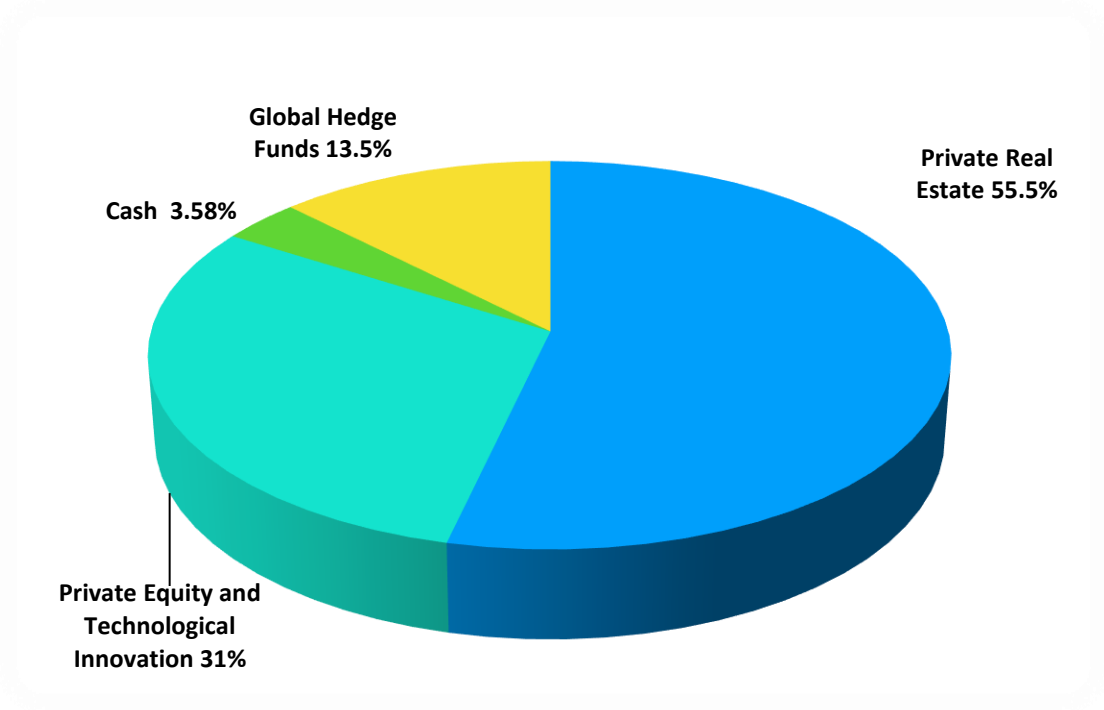


Alternative Trust Review: The goals of the Alternative Trust are to generate positive "real" returns (after-taxes and inflation) each year, and to generate annualized nominal returns of 6%-8% over rolling five-year periods. We are pleased to report that as at December 31st, 2018 the Trust has met its primary goals by generating a positive 1-year return of 9.2% and a 5-year return of 8.9%.

The 4th quarter of 2018 was marked by volatility in equity markets as concerns over: rising rates, a slowdown in China, ongoing trade skirmishes and a US-led housing downturn guided investor sentiment sharply lower. The CBOE Volatility Index, which infers equity volatility using data from the options market, briefly spiked to a level last scene during the "February flop" earlier in 2018. In our view, the elevated levels of equity market volatility mark a transitional period between a market (formerly) fixated on momentum to one more focused on quality names with more defensive attributes.

We are pleased that the MacNicol Alternative Asset Trust was able to once again provide investors with added levels of portfolio diversification and enhanced risk adjusted returns. Chart 2 below describes the Trust's overall asset mix as of the conclusion of the 4th quarter of 2018. During the 4th quarter the trust's overall asset mix was little changed. However, individual asset class updates, including a selection of relevant transactions is discussed later on in this report.

Chart 2 – MacNicol Alternative Asset Trust Asset Mix December 31st, 2018



Alternative Asset Trust Fourth Quarter 2018 Highlights

During the fourth quarter of 2018 the Alternative Asset Trust rose by 3.1%. Global hedge funds were higher in the quarter primarily on our partnership with a hedge fund based in Greenwich, CT that specializes in emerging market distressed debt investing. Unlike ad hoc approaches towards investments in emerging market stocks, the *post* hoc approach taken towards distressed debt investments in emerging markets involves patiently waiting for certain event risks to play out (such as an unsuccessful recapitalization) after which lending facilities are purchased for pennies on the dollar.

Private Equity and Technological Innovation were lower during the quarter primarily reflecting weakness in consumer technology positions in the online gaming and fire protection service spaces. Following generally mixed messages regarding the health of the real estate market, the trust's real estate holdings performed well during the fourth quarter. Our focus on growth markets in the South Eastern United States paid off as property level re-valuations due to rising tenancy (in Florida) and exits in Kansas and Georgia supported valuations and enhanced the fund's liquidity through an accelerated pace of cash distributions.

As 2019 begins the Portfolio Manager is confident that the trust will continue to support the plight of investors by providing them with the attractive risk-adjusted returns and non-correlated return profile that comes from a conscientiously constructed baskets of conservatively leveraged private investment opportunities.

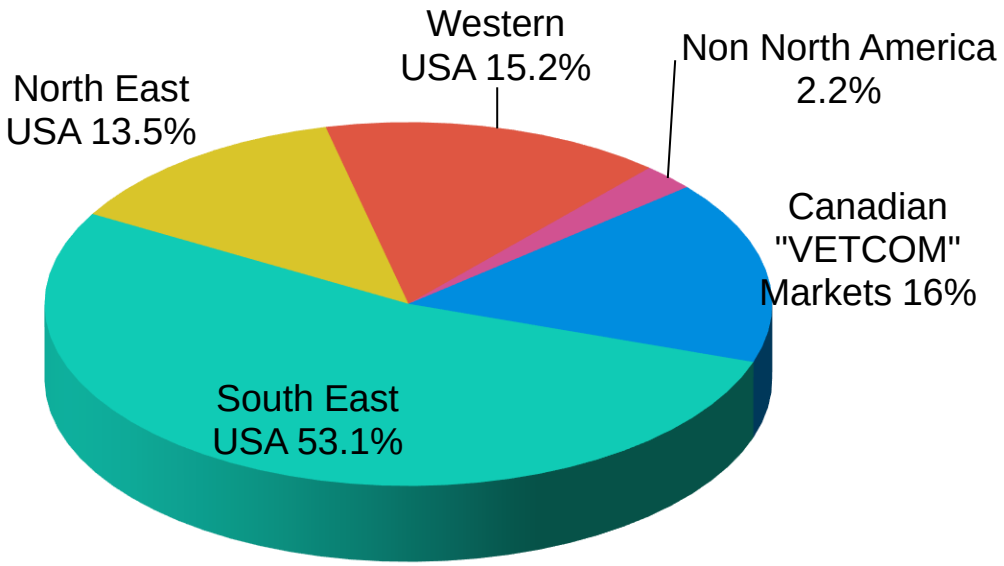
North American Private Real Estate: 360 Degree Realty Income Fund

The Alternative Asset Trust invests in North American real estate through the MacNicol 360 Degree Realty Income Fund. This fund focuses on value-added projects in the United States and Canada. The Fund also invests in financing through the residential and commercial mortgage funds of carefully selected sponsor firms. All sponsors are chosen for their high degree of local experience in deal sourcing, finance, construction, and property management. The fund has exposure to more than 140 separate real estate projects and 6 different asset classes across North America. **Chart 3** highlights the regions of North America in which our real estate projects are located as at December 31st, 2018.

360 Fund Fourth Quarter Highlights: For the 4th quarter of 2018, the fund rose by 1.7% in base currency terms and 5.7% in local currency terms. The quarter was dominated by rising occupancies, which supported higher valuations and an increase in cash distributions, which enhanced the fund's liquidity.

Chart 3 on the following page describes the fund's geographic mix as at the end of the 4th quarter of 2018. Through-out the 4th quarter the geographic mix was mainly unchanged with the high growth MSAs [Metropolitan Statistical Areas] in South Eastern United States representing the majority of the fund's assets. We note that the fund has only "token" exposure to assets located outside of North American and the Portfolio Manager does not envision this changing materially during 2019.

Chart 3 – MacNicol 360 Degree Fund Geographic Mix: December 31st, 2018



*VETCOM (Vancouver, Edmonton, Toronto, Calgary, Ottawa and Montreal)

Commercial Real Estate: Commercial real estate's appeal to investors is rising due to supportive fiscal policy and liquidity on the part of (primarily) institutional investors looking to cash in. Tenants are increasingly scrutinizing a) the adaptability and flexibility of properties b) the proximity of the said properties to commercial gateways and hubs such as airports and highway systems and c) for triple net lease tenants (commercial **leasing** term that refers to a situation in which the **tenant** pays virtually all the operating expenses associated with maintaining the property that is being rented) the environmental efficiency of assets (i.e. more efficient heating and cooling systems, "aware" lighting and security systems and more sophisticated waste management solutions).

Multi-family Residential: The performance of multifamily residential real estate is driven by several factors most notably jobs, which are closely tied to vacancy levels. Transportation solutions are a close 2nd place when formulating an overall view on a multifamily residential asset. The Portfolio Manager believes that over the next 10-years jobs and transportation infrastructure will form an important juxtaposition for multifamily

residential real estate with the former acting to telegraph NOI (Net Operating Income) growth to investors and the later acting as an "anchor" to support to property asset values. Taken together, employment growth and the ability of a given municipality to keep its roadways and transit systems as "smart" as its burgeoning population of young professionals will be essential towards attracting institutional equity investment and low cost lending facilities from banks and insurance companies. Accordingly, the Portfolio Manager believes that targeting municipalities with a plentiful supply of capital will function to lower the cost of the said capital and allow multifamily residential real estate to act as an inflation hedge in client portfolios as asset owners can raise rents at 5-10% annually.

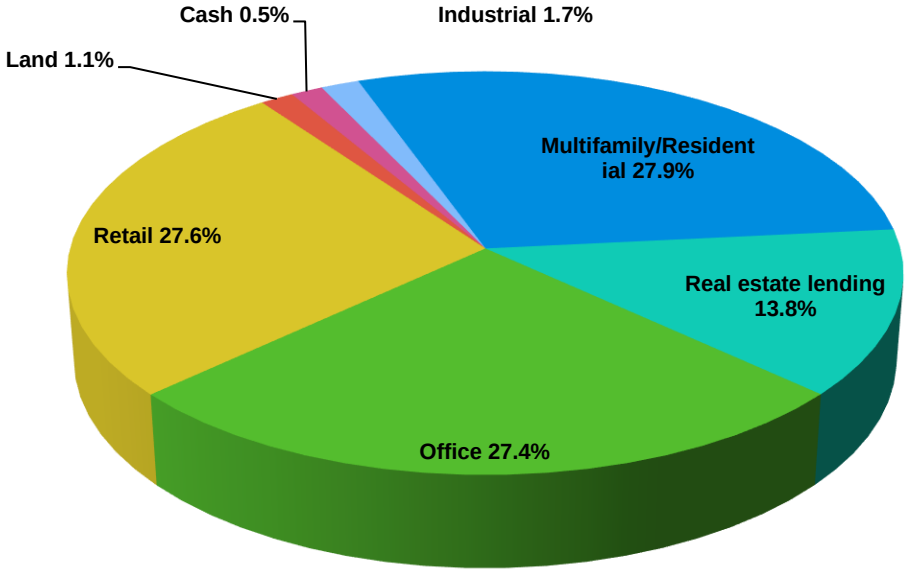
Industrial: The industrial product type has outperformed expectations in certain locations and by-far-and-away the best example of this is South Florida. To demonstrate just how hot South Florida industrial product is, last year the top five transactions were valued at $478 million which easily outperformed 2017s roster of 5-best deals, themselves valued at $401.5 million. The increase in demand for South Florida industrial assets boils down to a thriving market for e-commerce and the need for more distributions centers and more innovative distribution centers. A listing of notable transactions in the space would entail a separate report at least as long as the entire Alternative Asset Trust's own quarterly report. Nevertheless, the Portfolio Manager wishes to draw investor attention to a sample transaction as a small window of what is going on in the region. Fortress Investment Group paid $66.4 million for a SUPERVALU distribution terminal in Pompano Beach Florida. The asset sits on a 50-acre site off the North Andrews Avenue extension about 10 miles south of Boca Raton.

A commercial transport truck leaves the SUPERVALU distribution center in Pompano Beach Florida. Fortress Investment Group paid $66.4 million for the 700,000+ square foot terminal. Expectations for rent at the hub are around $30 million underscoring the demand by institutional investors and cautioning retail investors to not take this product type lightly in their own portfolios.

Office: As described later on in Chart 4 of this report, office space is a material product type for the fund. The fund pursues a combination of current income and value creation, and employs active management to: reposition, re-lease, redevelop, and/or develop real estate assets in an effort to optimize overall performance. Our target in the office is a *net* IRR of between 12% and 14% and a net profit multiple of 1.6x to 1.8x. As in most other real estate product types, property location, design, configuration, amenities and services are more important than ever to attracting/retaining tenants and driving returns.

Retail. Many retail properties are struggling to adjust to the idea that they now play a "second string" role in investment portfolios largely due to the success of internet retailing and secular changes in consumer purchasing behavior. Retail property markets nationwide are downsizing and segregated into "have" and "have-not" parcels based on quality, location and tenancy. Incursion in the retail product type has only deepened in 2018. During the H1, 2018, e-commerce sales grew by almost 16% on a YOY basis, quadrupling the 4% sales growth achieved by all other retail outlets (excluding those from restaurants and bars). However, e-commerce *now* accounts for 10% of all non-food/drink retail sales nationally, up from just 4% a decade ago with one junior analyst at our firm noting that McDonalds can (now) be ordered from one's smart phone and delivered to one's door. So much for having to drive to a pick-up window to satisfy one's late night cravings. While retail exposure in the fund endures, we are not actively adding to the space and will focus our H1, 2019 efforts to more closely examine whether any of the fund's retail assets are heading for a collision course with the Amazon and eBay's of the world.

Chart 4 – MacNicol 360 Degree Fund Product Type Mix: December 31st, 2018



Real Estate Portfolio Activity

Transaction activity in the fund was high during Q4, 2018 and can be distilled down to two primary drivers: multifamily occupancy rates that are trending slightly above target (despite widely reported concerns to the contrary) and institutional demand for commercial and industrial product types.

Arium Overland Park was sold by our partners at the Carroll Group for a net IRR of 12% on a 1.3x multiple of invested capital.

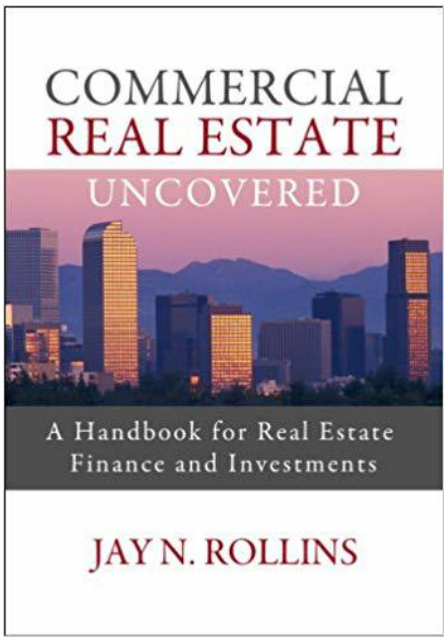
The entrance to Arium Overland Park in Kansas is shown in a recent photo.

Our partners at Rockwood Capital recently sold our partnership interest in 55 Water Street, the large commercial office complex located in the Wall Street district of lower Manhattan and owned by the retirement system of the State of Alabama.

55 Water Street is a prominent, strategically located Wall Street office tower in lower Manhattan. The asset was bought by the Alabama State retirement system in 1993 for a little over $200 million but is today modelled to be worth 15x as much.

Multiple Transactions from JCR Capital

Our Partner, commercial real estate kingpin Jay Rollins (also front man for JCR Capital) was busy during H2, 2018. In addition to very graciously sending us a copy of his excellent book *Commercial Real Estate Uncovered*, noted three key transactions, which we describe below.



Commercial Real Estate Uncovered is a book that literally sits on our coffee table at home and gets read numerous times through any given week. We happen to have an autographed copy.

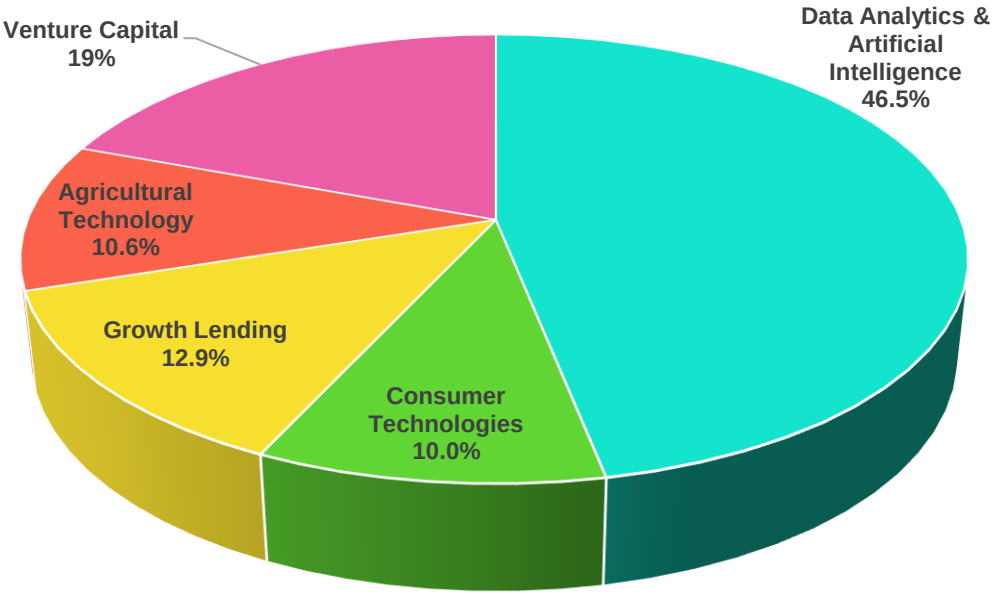
The front façade of California Industrial Facility in Redwood. The investment was a preferred joint venture transaction representing the continuation of a previous sponsor relationship based on the strategy of purchasing non-performing California industrial assets.

Club Creek was sold for a gross sale price of $16.5 million after a 34 month hold period. JCR's original underwriting projected a $12.4 million sales price and a 36-month hold. The Wildwood & Club Creek investment is now fully realized and has generated a 25.9% gross IRR and 1.67x multiple to the fund. Original underwriting projected an 18.9% IRR and 1.60x multiple. The Commerce Industrial asset within the California Industrial Facility 5.0 investment has been sold. This individual asset has returned a gross 44.1% IRR and 1.50x multiple to JCR. There is now only one asset remaining in the Facility, which is currently being marketed for sale. Following the sale of the Commerce Industrial asset, JCR has returned 82% of its equity invested in the Facility.

Private Equity and Technological Innovation:
Emergence Private Equity Fund, December 31st, 2018

Private equity is an asset class consisting of equity securities and debt in operating companies that are not publicly traded on a stock exchange.

Chart 5 – MacNicol Emergence Fund Industry Mix, December 31st, 2018



Against a backdrop of heavy selling pressure in public technology markets technology names (the NASDAQ Index at one point was down over 15% on a YTD 2018 basis and easily down well over 20% on a 2018 peak-to-trough basis) Emergence performed relatively well. Though the fund lost ground in 2018 giving back 3.1% the Portfolio Manager maintained discipline closely monitoring investments in the consumer and agricultural technologies spaces, and in blockchain technologies.

Private Equity Portfolio Activity

Our initial investment into the Dental space (an equity co-investment in a company called Tyson-Steele) is working well. Tyson-Steele and sister illumitrac provide software and services that help dental practices run more successfully. During the 4th quarter of 2018

both companies were re-branded as Dental Revolution and segmented into three core divisions: software enabled marketing solutions, continuing education services and illumitrac. During the quarter, Dental clinic tracking was at expectation and preliminary financial reporting highlights an EBITDA margin of 40% though the Portfolio Manager cautions that more formal reporting of financials versus plan will begin being reported in the first quarter of 2019. Overall though the Portfolio Manager is pleased with the company's transition to new ownership, procurement of formal office space in Portland, Oregon and pace of revenue growth.

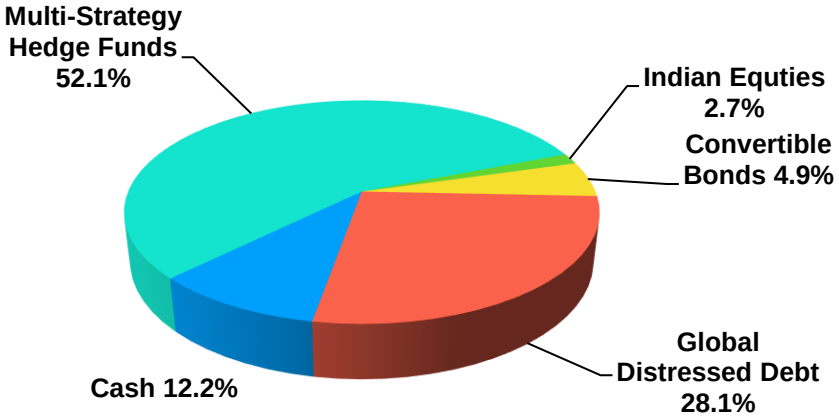
In LATAM the confirmation of Jair Bolsonaro in Brazil has brought (some) political stability to the region, after all Bolsonaro is not governing from a jail cell. In addition, LATAM beef prices have moved higher during the 4th quarter supporting livestock valuations and farm land prices in the region. While investments in agricultural technology have thus far disappointed, the Portfolio Manager feels that an important turning point has been reached in which land owners can command higher premiums for acreage both from a sales and lease perspective. To be clear, much work needs to be done in order for this sector to become an on-balance contributor to performance for the fund, but we are pleased that incoming evidence continues to support the notion that the "eye of the storm" has passed.

It has been a while since we reported on the performance of our investment in blockchain company NextBlock Global. Admittedly, we questioned this investment numerous times over the past 18 months. At one point in late 2017 cryptocurrencies and blockchain technology seemed like money in the bank. Since that time though the sector has been a disappointment. The gargantuan volatility in the underlying cryptocurrencies underscores to us that over the short-term investors tend to overestimate the potential of a new technology while over the long-term they under estimate it. With our final distribution from NextBlock Global in December, the Portfolio Manager is pleased to report that the fund's investment in this particular blockchain company was actually quite successful. NextBlock Global has so far distributed $48 million to investors: the original $20 million plus two additional profit payments of $20 million and $8 million respectively. The Emergence Fund's own investment in NextBlock Global yielded a return for investors of 140% or 2.4x the initial investment (by contrast, the crypto market is down around 85% from its peak). Most NextBlock Global company executives declined carried interest payments in the name of setting the record straight with investors and we appreciate this as the bonuses would have been lucrative.

Hedge Funds: MacNicol Absolute Return Fund

The objective of the MacNicol Absolute Return Fund is to generate positive returns under most market and economic conditions, and to have little or no correlation to the US and Canadian stock markets. During the fourth quarter of 2018 the fund was higher by over 3% and finished off the year in positive territory with a return of 6.8%. We were pleased with the fund's performance for two reasons. First the fund is designed to produce S&P like levels of return in a manner that runs counter cyclically to the S&P. Fortunately this positive result happened for the fund in 2018 and our partnership with some truly world class Hedge Funds in New York and Greenwich CT was the main reason why.

Chart 6 – MacNicol Absolute Return Fund Strategy Mix, December 31st, 2018



Though higher in the fourth quarter of 2018 and for the year as a whole the fund experienced losses in convertible bonds, which declined due principally to the discounting of the conversion premium over conventional bonds.

Closing Comments

No other word in the English language comes closer to describing what 2018 meant to investors than volatile. Fortunately, our entire team here at MacNicol & Associates Asset Management stands behind our Alternative Asset Trust and you are valuable investors.

Sincerely,

MacNicol & Associates Asset Management Inc.