



January 29, 2020

Dear Appleseed Shareholder:

“The future ain’t what it used to be.”

– Yogi Berra, Baseball Hall of Fame Catcher & Manager

The 2010s represented the longest-ever period of sustained, uninterrupted economic growth and associated market gains. With shrinking unemployment, growing average household wealth, and increasing income disparity – driven by the most activist Federal Reserve in history – the stock market climbed to historic highs and the housing market was resuscitated, as bond yields declined to all-time lows. The economy has experienced 110 months of sequential job gains thus far, and unemployment has reached a 50-year low.

2010 - 2019
A Decade of Immense Change

	1/1/2010	12/31/2019	% Change	
			Annual	Total
U.S. Statistics				
S&P 500 Index	1,074	3,231	11.6%	270.0%
CBOE Volatility Index	19.96	13.78	-3.6%	-31.0%
Fed Funds Rate	0.00%	2.25%	2.25%	
10-Year Treasury Bond Yield	3.83%	1.92%		-1.91%
Household Wealth (\$ Trillion)	\$ 59	\$ 107	6.1%	81.4%
Unemployment Rate	9.9%	3.5%		-6.4%
Population (Million People)	309	330	0.7%	7.0%
Real GDP Growth			2.3%	25.5%
Inflation			1.7%	18.4%
World Statistics				
MSCI EAFE Equity Index	757	1,190	4.6%	51.7%
Gold	\$ 1,095.20	\$ 1,523.10	3.4%	39.1%
WTI Crude Oil	\$ 72.89	\$ 61.06	-1.8%	-16.2%
Bitcoin	\$ 1	\$ 7,194	143.0%	719260.0%
10-Year German Government Bond Yield	3.36%	-0.19%		-3.6%
10-Year Japanese Government Bond Yield	1.36%	-0.20%		-1.6%
World Population (Million People)	6,896	7,622	1.0%	10.5%

Sources: Standard & Poor's, MSCI, St. Louis Federal Reserve, U.S. Census Bureau, FactSet.

Over this decade of immense change, the United States experienced many fascinating investing phenomena:

The United States lost its AAA credit rating.

Until 2011, the Federal government had always raised the debt ceiling in a collegial, bipartisan manner, so that the Federal government would continue to operate without a hitch. In 2011, the Republican-controlled House of Representatives required spending concessions from President Obama before it would agree to raise the debt ceiling. Although a last-minute deal was eventually reached, the capital markets reacted violently to the negotiations. Accordingly, Standard & Poor's downgraded the U.S. credit rating for the first time in history, dropping it two notches from AAA to AA+.

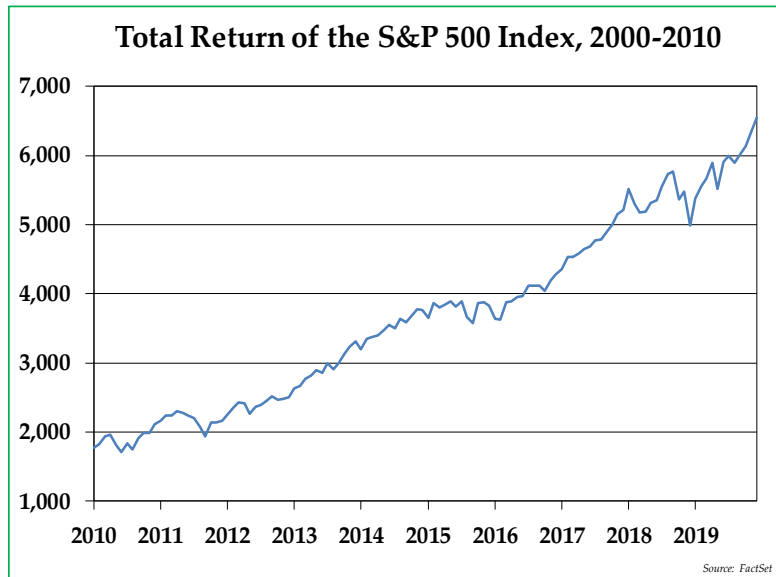


“Too Big to Fail” got a whole lot bigger.

During the Financial Crisis, 982 U.S. banks, insurers, and finance companies were deemed to be “Too Big to Fail,” thus justifying unprecedented, massive cash bailouts and an extended period of zero percent interest rates. Despite the risks looming from these large-scale enterprises, the biggest banks have become far larger over the past decade. Today, Citigroup, Bank of America, JPMorgan Chase, and Wells Fargo each have more than \$2 trillion in total assets.¹ Beyond that, the notional amount of derivatives on the balance sheets of the Too Big to Fail banks, now measured in the hundreds of trillions of dollars, should warrant, in our view, considerably more concern from investors and regulators.

Zero percent and negative interest rates played a critical role in driving asset prices north.

Central banks across the globe ventured into uncharted territory in the past decade by cutting interest rates to zero percent and, in certain countries, below zero percent. The European Central Bank, as well as the central banks of Japan, Sweden, Denmark, and Switzerland cut their respective interest rates into negative territory. For the first time in 5,000 recorded years of economic history, government bonds traded with a negative rate of return. In 2019, Germany issued a 30-year bond with a zero percent yield for the first time. Roughly *one-third* of non-U.S. bonds now sport a negative rate of return.² Relatedly, wealth inequality worsened considerably in the United States as the rich-with-financial-assets got richer while the not-rich-without-financial-assets didn’t.



Quantitative Easing (QE) played a significant role in stimulating financial asset prices.

In addition to zero percent and negative interest rates, the Federal Reserve and other central banks across the globe purchased trillions of dollars of government bonds, mortgage-backed securities, and, in certain cases, equity ETFs, reducing borrowing costs for governments, corporations, and households alike. U.S. companies issued record levels of corporate debt and used much of the proceeds to repurchase stock. From 2008 to 2015, the Federal Reserve expanded its balance sheet from \$800 billion to \$4.5 trillion.

¹ To provide a sense of scale, 2018 U.S. GDP was only \$20.5 trillion.

² Source: Deutsche Bank.



The 2010s represented an uninterrupted bull market.

The decade began and ended in one extended bull market, with record-low interest rates, record-high profit margins, tax cuts, and unconventional monetary policies like quantitative easing pushing U.S. stock prices upward with seemingly no pause in pace. The S&P 500 Index trumped all other global markets this past decade in terms of investment performance with a 270% total return, as demonstrated in the chart on the previous page.

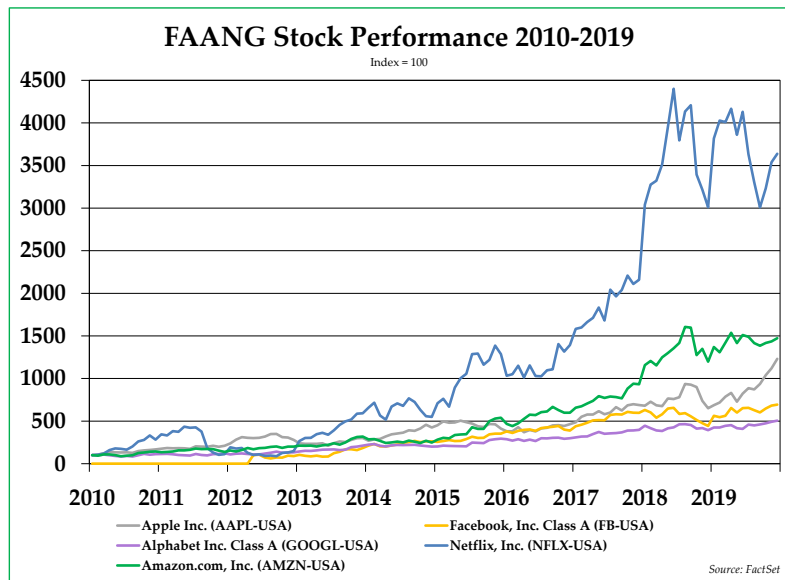
Big tech monopolies formed and outperformed.

Investment performance for the FAANG technology companies (Facebook, Amazon, Apple, Netflix, and Alphabet/Google) dominated the performance of the S&P 500 and the Nasdaq Composite; the best performing stock in the 2010s amongst the FAANG stocks was Netflix with a 4,111% total return, and the “worst” performing stock of these six companies was Alphabet with a 432% total return. Notably, despite the increasing monopolization of several U.S. technology sectors such as social media and search, the U.S. Department of Justice did not bring an antitrust lawsuit against any technology company during the 2010s.

Unicorns became rampant.

In financial jargon, a “unicorn” is a privately held startup with a valuation of over \$1 billion. Although unicorns are supposed to be creatures only found in fairy tales, there were as many as nearly 300 financial unicorns in 2018.³ The proliferation of

unicorns has been driven by 1) venture capitalists intensely pushing the “get big fast” strategy, 2) richly-priced acquisitions by large corporations who have easy access to cheap money, and 3) the considerable increase in the amount of private capital invested in startups.



Shale oil transforms the U.S. energy industry.

Extracted from oil shale rock fragments, shale oil is now being produced unconventionally in many locations in the United States and elsewhere. While technological advancements increased the amount of unconventional oil and gas reserves in the United States during the 2010s, the costs of extracting shale oil, both in terms of dollars spent and environmental risks, are much higher than the costs of conventional oil production. The lifetime of shale oil wells is also much shorter than

³ Source: TechCrunch.



that of conventional wells. Nevertheless, this drilling innovation contributed significantly to GDP growth during the 2010s and transformed the United States from a net oil importer to a net oil exporter.

Cryptocurrencies became a new asset class.

While bitcoin was launched in 2008, most Americans were not aware of bitcoin and other digital currencies until 2017 when cryptocurrency prices hit the stratosphere. In fact, bitcoin was the top performing asset class of the 2010s with a whopping price increase of 719,260%. Many investors and technology entrepreneurs remain excited about the long-term potential of cryptocurrencies to revolutionize money, payment systems, and banking.

Globalization began to reverse.

Reversing a decades-long trend, international trade began to decline in 2018. President Trump took aim at the trading policies of the European Union, South Korea, Japan, and, most notably, China. Since then, billions of dollars of new tariffs have been established, causing increased economic uncertainty. With China alone, the United States has imposed tariffs on \$550 billion in Chinese goods, which were countered by \$185 billion in tariffs on U.S. exports to China.

An extraordinary decade for the capital markets has just drawn to a close. During the past month, many investment firms and financial media outlets have been making predictions about the year 2020. Instead, we would like to take a stab at making some predictions about the next *decade*, while knowing definitively that a number of astounding, unforeseen events will unfold.

The capital markets are generally very skilled at making fools of people who make broad, sweeping predictions that turn out to be dead wrong. While acknowledging that some of our predictions will prove to be incorrect, we present ten of our predictions for the 2020s:

- 1) **The dollar-centric international monetary system becomes a multi-polar monetary system.**
The U.S. dollar share of foreign central bank holdings continues to decline, as the dollar is used less in international trade. Conversely, the Chinese Yuan, the Euro, the Japanese Yen, and gold will play an increasingly important role in foreign central bank holdings. With lower international demand for dollars, the U.S. dollar exchange rate declines, benefiting U.S. producers with increased export competitiveness while harming U.S. consumers with higher import prices. With dollar weakness, U.S. manufacturing resurges, inflation accelerates, and Federal debt levels become more manageable by the end of the decade.
- 2) **Without reform, the Federal Reserve's monetary role increase, and interest rates remain low.**
With foreign central banks backing away from U.S. Treasuries and a ballooning budget deficit, the Federal Reserve becomes the last resort buyer of U.S. Treasuries in a significant and noticeable way. These Treasury purchases fund the government's defense spending, entitlement obligations, and interest payments, while also capping interest rates on U.S. Treasuries at low levels. With interest rates capped by the Federal Reserve, U.S. fixed income



investments generate rates of return that do not exceed the inflation rate.

3) A resurgent U.S. Department of Justice pursues antitrust actions against monopolistic corporations.

Several large, near-monopolistic technology companies face new regulations while others are broken up as the U.S. government attempts to curtail their power and foster increased competition. As part of this breakup, many of the free or heavily discounted services provided by these companies dissipate. The U.S. government also places size limitations on commercial and investment banks, causing the largest banks to break up into smaller pieces.

4) The S&P 500 disappoints.

After one of the longest bull markets in history, the stock market disappoints in the 2020s. Weaker S&P 500 investment returns are driven by the following:

- Stock valuations in the United States are sky-high at the beginning of the decade and come down to more reasonable levels by 2030. Accelerating inflation reduces the present value of companies' future cash flows, resulting in a stock market P/E ratio at the end of the decade that is well lower than the start of the decade.
- Corporate share buybacks cease. Because corporations have been the predominant buyer of stocks throughout the post-Financial Crisis period, the lack of buybacks has a considerable impact on demand for equities, negatively affecting share prices.
- Corporate profit margins, which began the decade at record high levels, decline over the next ten years due in large part to higher wages, increased import prices, and efforts taken by the Federal government to prosecute antitrust cases and foster increased competition.
- To fund living expenses during retirement, aging baby boomers sell their housing, stock, and bond holdings at discounted prices to a smaller population of Generation Xers and Millennials.

5) Value stocks meaningfully outperform growth stocks.

As investors start to pay attention to business fundamentals, earnings, and cash flows, investors rotate out of expensive tech companies and into relatively inexpensive value stocks. The cheapest part of the stock market at the beginning of the decade considerably outperforms the most expensive stocks in the stock market, similar to what transpired during the 2000s after the dot-com bubble ended.

6) International stocks outperform U.S. stocks, led by emerging market stocks.

As the dollar weakens, foreign stock markets as denominated in U.S. dollars outperform the U.S. market. In many of these international markets, cyclically-adjusted price/earnings (CAPE) ratios begin the decade at undemanding levels, and particularly so in emerging markets, which means that the valuations of foreign stocks are likely to rise during the next ten years. Some of the big winners include now out-of-favor stock markets like China, Italy, Russia, Brazil, and South Korea, all of which trade at CAPE ratios well below that of the S&P 500.



7) Gold shines.

With 10-year bond yields below the rate of inflation, investors increasingly rely less on fixed income investments as a foundational store of value within investment portfolios. Conversely, with interest rates low and inflation accelerating, gold's investment attractiveness improves, as gold becomes an essential part of many investors' strategic asset allocations. At the same time, central banks continue to increase their purchases of gold as a neutral reserve asset to settle accounts with other countries. As a result of increased demand by central banks and private investors alike, the gold price more than triples by the end of the decade.

8) Blockchain-based cryptocurrencies like bitcoin become the biggest loser of the decade.

Digital currencies continue to grow, but bitcoin and other blockchain-based cryptocurrencies lose their luster. Private cryptocurrencies become one of the worst-performing asset classes of the decade as it becomes evident that cryptocurrencies will never be embraced by the international monetary system as alternative currencies. Concurrently, a group of central banks collaborates to issue and administer a new and revolutionary digital currency system, which allows for far greater transparency, efficiency, safety, reliability, and government control than the current non-digital currency system. This new system enables a myriad of new monetary tools that could not be applied today.

9) Underfunded public pension plans receive a Federal bailout.

With increasing liabilities and unreasonable assumed investment rates of returns, underfunded public pension plans create a financial crisis. Municipal bond markets freeze up and social unrest grows, as retired teachers, police officers, and firefighters across the country demand assistance from the Federal government. Congress appropriately bails out insolvent pension plans in return for structural reforms that prevent the problem from recurring in the future. The pension bailout causes further weakness in the U.S. dollar exchange rate as foreign investors worry further about the weakening fiscal discipline of the United States.

10) The explosion in student debt forces dramatic changes in higher education.

As college unaffordability worsens further, scores of Tier Two and Tier Three private universities declare bankruptcy and liquidate. At the same time, new startups that focus entirely on vocational training proliferate and take significant market share from traditional educational institutions. Responding to these changes, large companies in the United States stop insisting on a college degree as a hiring prerequisite for many white-collar jobs.

A decade is a long time, and we expect significant trends to develop that we are not even contemplating, nor for that matter, is anyone else contemplating. One thing we expect will not change is our approach towards investing. We will be looking for value, we will be wary of risk, we will be closely examining risks related to environment, social, and governance issues, we will be co-invested with Appleseed shareholders, and we will continue to invest Appleseed Fund with prudence and discipline.



Appleseed Portfolio Commentary

We continue to maintain an overweight position in foreign stocks, gold, and companies whose earnings should benefit from a weaker dollar.

Despite the recent run up across many asset classes in 2019, we remain heavily invested in stocks. We expect that central banks generally and the Federal Reserve in particular will continue to provide unprecedented levels of liquidity to support the market, and we are finding companies to buy and hold which continue to be undervalued in our estimation.

During the fourth quarter of 2019, we sold two investments, **Cosco Shipping** and **Osram Licht**. We sold Cosco Shipping to reduce our exposure to China, and Cosco was the least attractive of our China related investments. We sold Osram Licht after the share price had risen sharply in response to a bidding war for the company between Bain Capital and AMS AG. Since investing in Osram Licht, the fundamentals have only worsened as the worldwide automobile market slowed, but Appleseed's return was satisfactory due to the depressed price at which we bought shares of this LED producer.

At the same time, we invested in two new equity holdings during the fourth quarter, **Heron Therapeutics (HRTX)** and **Annaly Capital Management (NLY)**.

Heron is currently marketing two drugs, Sustol and Cinvanti, which have been approved for the prevention of chemotherapy-induced nausea and vomiting. Sustol is somewhat of a me-too drug and is largely irrelevant to our thesis. Cinvanti, on the other hand, is a new formulation of an established active compound that offers significant advantages when compared to alternatives. Not only is Cinvanti much quicker to prepare and administer, but it also has a reduced risk of severe allergic reactions. Cinvanti's highly differentiated profile is reflected in its strong sales ramp since the FDA approved it several years ago.

Beyond the company's existing approved drugs, Heron is developing a new drug, HTX-011, which holds the promise of revolutionizing post-operative pain management. For a long time, surgeons and anesthesiologists have been limited to opioids and local anesthetics, both of which have significant limitations. Opioids come with unwanted side effects and are highly addictive, while the effect from local anesthetics wears off soon after administration. With HTX-011, Heron is developing a long-acting formulation of a local anesthetic that provides meaningful reduction in pain through 72 hours after surgery; as a result, it also has the potential to reduce opioid usage related to postoperative pain management dramatically (and hopefully put a dent into the opioid crisis in the United States).

Market sentiment related to Heron turned sharply negative after a major insider sale in September 2018 and after the FDA chose to delay approval of HTX-011 in May 2019. As a result, Heron's stock price declined from \$40+ to less than \$20 at Appleseed's purchase price. We bought the stock because we believe that HTX-011 is an extremely valuable asset and that current investor



pessimism is unfounded, in our estimation.

We are confident that HTX-011 will be approved soon. The opioid epidemic is real, and a long-acting local anesthetic would be a perfect solution; HTX-011 is the only drug of this category that is truly long-acting. For that reason, the FDA designated HTX-011 as a Breakthrough Therapy and put it on the Fast Track for approval. We suspect that the FDA ran out of time before the tight May 2019 deadline, and we are not worried about Heron having to resubmit its new drug application for HTX-011 after receiving a complete response letter from the FDA. The active ingredient in HTX-011, bupivacaine, has been used for decades, and the proprietary drug delivery technology used with HTX-011 has already been approved for use in Sustol.

Annaly Capital Management is a mortgage REIT which used to be a top holding in Appleseed Fund during the Financial Crisis. We owned Annaly then because the economy was slowing considerably, the Federal Reserve was cutting short-term interest rates, most of its assets were highly liquid and safer agency mortgage-backed securities, and we expected the yield curve to steepen as a result of increasing liquidity on the part of the Federal Reserve. Also, we had high regard for the management team, and we were paid a double-digit dividend yield while we waited for our thesis to play out. We purchased Annaly Capital Management during the fourth quarter of 2019 for the exact same reasons.

Appleseed Fund Investor shares generated a 15.68% return during calendar year 2019. Since its inception in December 2006, Appleseed Fund has generated an annualized return of 6.56% per annum. The most significant contributors to 2019 performance among the Fund's equity positions were **Ardelyx (ARDX)**, **Heron Therapeutics (HRTX)**, and **Oaktree Capital Group (OAK)**. We sold our position in Oaktree soon after it was announced that Brookfield Asset Management would be acquiring the company. However, Ardelyx and Heron remain top holdings for Appleseed Fund, as we believe their share prices remain significantly undervalued. Returns from these winners were partially offset by several performance detractors which included **Sina Corporation (SINA)**, **Hyundai Home Shopping (057050-Korea)**, and **Titan International (TWI)**. All three of these companies generated negative returns due to increasing investor concerns about global growth and global trade. We continue to hold all of these positions, although our Sina position has declined even as our position in Sina-controlled **Weibo (WB)** has increased. We decided to move out of Sina and into Weibo in order to realize tax losses to offset portfolio gains and also to take advantage of weakness in the Weibo share price relative to that of Sina.

During the last week of 2019, former Appleseed portfolio manager, Ron Strauss, unexpectedly passed away at the age of 80. Ron played a larger-than-life role for those of us who were lucky enough to work with him. His role as mentor, partner, friend, father, and father figure was invaluable to all of us. He taught us by example: working hard, putting investors first, caring about the good of our associates, using ethics as a guide stone, investing behind responsible management teams, and being committed to prudent, disciplined value investing. Ron positively influenced all



of us at Appleseed Capital; we will miss him terribly.

Farewell, our friend and mentor.

We wish you and your families a happy, healthy, and prosperous decade, and we look forward to working hard on your behalf in an effort to generate attractive risk-adjusted returns with your investment in Appleseed Fund.

Should you have any follow up questions, please do not hesitate to contact Colin Rennich (colin@appleseedcapital.com).

Sincerely,

William Pekin, CFA

Josh Strauss, CFA

Adam Strauss, CFA

Shaun Roach, CFA



ANNUALIZED RETURNS- as of 12/31/2019					
	1 Year	3 Years	5 Years	10 Years	Since Inception
Investor Class (APPLX)	15.68%	9.48%	5.56%	5.92%	6.56%
Institutional Class (APPIX)	15.85%	9.66%	5.77%	<i>6.12%</i>	<i>6.71%</i>
MSCI World Index	27.67%	12.57%	8.73%	9.46%	5.83%

Fund Inception Date: 12/8/2006.

Fund's past performance does not guarantee future results. The investment return and principal value of an investment in the Fund will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. Current performance of the Fund may be lower or higher than the performance quoted. Performance data current to the most recent month end may be obtained by calling 1-800-470-1029. Italics indicates extended performance, as APPIX did not exist until 1/31/11. APPIX extended performance is an estimate based on the performance of APPLX, adjusted for the difference in fees.

As of 12/31/2019, the Fund's Top Ten Holdings can be found at: www.appleseedfund.com.

The gross expense ratio of the Fund's investor class is 1.47%, and the institutional class is 1.22%; the net expense ratio after contractual fee waivers through January 31, 2020 is 1.25% and 1.06%. The Fund's ninety day redemption fee is 2.00%.

The S&P 500 Index is a widely recognized, unmanaged group of stocks that is representative of a broad market. The index provides returns in U.S. dollars, assumes reinvestment of all distributions, and does not reflect the deduction of taxes and fees. The MSCI World Index is a widely followed, unmanaged group of stocks from 23 international markets and is not available for purchase. These indices provide total returns in U.S. dollars with net dividends reinvested. These index returns do not reflect the deduction of expenses, which have been deducted from the Fund's returns. These index returns assume reinvestment of all distributions and do not reflect the deduction of taxes and fees. Individuals cannot invest directly in these indices, however, an individual can invest in exchange traded funds or other investment vehicles that attempt to track the performance of a benchmark index. The Consumer Price Index (CPI) is an unmanaged index representing the rate of the inflation of U.S. consumer prices as determined by the U.S. Department of Labor Statistics.

The use of options involves substantial higher risks and may subject the Fund to higher price volatility. Investments in international markets present special risks, including currency fluctuation, the potential for diplomatic and political instability, regulatory and liquidity risks, foreign taxation, and differences in auditing or other financial standards. Risks of foreign investing are generally intensified for investments in emerging markets. Value investing involves the risk that an investment made in undervalued securities may not appreciate in value as anticipated or remain undervalued for long periods of time.

Small and Mid-Cap investing involve greater risk not associated with investing in more established companies, such as greater price volatility, business risk, less liquidity and increased competitive threat.



Diversification does not ensure a profit or guarantee against loss.

Investments in commodities such as gold may be affected by overall market movements, changes in interest rates, and other factors such as embargoes and international economic and political developments. Commodities are assets that have tangible properties, such as oil, metals, and agricultural products. These instruments may subject the Fund to greater volatility than investments in traditional securities.

The views and opinions expressed in this material are those of the authors. While we believe we have a reasonable basis for our appraisals and we have confidence in our opinions, actual results may differ materially from those we anticipate. These opinions are current as of the date of this letter but are subject to change. There is no guarantee that any forecasts or opinions in this material will be realized. Information should not be construed as investment advice nor be considered a recommendation to buy, sell or hold any particular security.

You should carefully consider the investment objectives, potential risks, management fees, and charges and expenses of the Fund before investing. The Fund's prospectus contains this and other information about the Fund, and should be read carefully before investing. You may obtain a current copy of the Fund's prospectus by calling 1-800-470-1029.

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