SEAFARER

SEAFARER OVERSEAS GROWTH AND INCOME FUND

Portfolio Review

Second Quarter 2020

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During the second quarter of 2020, the Seafarer Overseas Growth and Income Fund returned 19.43%.[1] The Fund's benchmark, the MSCI Emerging Markets Total Return Index, returned 18.18%. By way of broader comparison, the S&P 500 Index returned 20.54%.

The Fund began the quarter with a net asset value of $9.48 per share. During the quarter, the Fund paid a semi-annual distribution of approximately $0.072 per share. This payment brought the cumulative distribution, as measured from the Fund's inception, to $3.065 per share.[2] The Fund finished the quarter with a value of $11.25 per share.[3]

Performance

Despite a preponderance of challenging news regarding the COVID-19 pandemic, stock markets throughout the developing world marched uniformly higher in the second quarter. Investors willfully ignored any contrary information: during the quarter, consensus estimates for overall corporate profit growth in 2020 from the emerging markets collapsed from +12% (as measured in early January) to -13% (as measured again, at the end of June).[4] Growth estimates for 2021 are stubbornly anchored much higher, at +31%; yet this is only so because financial analysts, beset by an unprecedented degree of uncertainty about the near term, have not yet adjusted their forecasts from those made at the beginning of the year – substantively prior to the spread of COVID-19. Put simply, the markets are moving blindly forward, uncritically hoping for a better set of outcomes; the markets have ceased to know or measure anything substantive, as they normally do when engaged in the act of "price discovery." I fear that such rampant speculation has been fueled entirely by the historic levels of monetary stimulus afforded by the U.S. Federal Reserve and the People's Bank of China.

Chinese stocks dominated the surge during the quarter – bizarrely so, given a weak outlook for the domestic economy, and given the prevalence of political frictions abroad that now hamper the international expansion of many Chinese companies.

As of 6/30/20 the annualized performance of the Fund's Institutional class was: 1 year -0.20%, 3 year 0.37%, 5 year 1.98%, and since inception (2/15/12) 4.70%[1]; the gross expense ratio was 0.89%. The performance data quoted represents past performance and does not guarantee future results. Future returns may be lower or higher. The investment return and principal value will fluctuate so that an investor's shares, when redeemed, may be worth more or less than the original cost. View the Fund's most recent month-end performance at www.seafarerfunds.com/performance.

Yet it is precisely these contrary facts that appear to have pushed stock prices dramatically higher: investors in China seem to believe that such adverse events will give the Chinese government impetus not only to stimulate the local economy, but also to come to the aid of the country's many beleaguered industries. The latter premise is not entirely silly, as Beijing has historically exercised a heavy hand in promoting various companies as "national champions" and selecting "winners and losers."

Such hopes have led many stocks in China's domestic market to gain over 50% in the past three months, and some have doubled, making China's A-shares among the best-performing in the world. Yet the rampant speculation seems misguided, if only for the sheer magnitude of the government intercession it supposes. Investors are giddily pretending that nearly all technology companies – a few of which are of excellent quality, but the majority of which are of questionable capability – will somehow benefit from the state's largesse, given the government's ambition to spur native technologies under the "Made in China 2025" project. It is true China's industrial policies have grown more forceful and statist under the Xi administration. Yet there is no way that Beijing can provide succor for so many companies at once, nor can it foster so many "national champions," for it lacks the fiscal resources to do so. Further, intense competition within China will ensure that many of the companies now vaunted by the stock market will not prosper over time. Still, reality did not intrude on the Chinese dream during the quarter, and shares surged (and accelerated further in July). Thus, I am convinced large swathes of the China A-share market have entered a bubble, though I have no idea how long it will persist, or what will cause it to burst.

Amid such distorted conditions, the Growth and Income Fund kept pace with markets, but failed to capture the most aggressive returns available from the market (as mentioned above, a staggeringly large number of stocks have risen precipitously from their March lows). Most of the Fund's gains simply represent a "knee-jerk" recovery from the COVID-19-induced nadir in markets that occurred near the end of March. The Fund's outsized exposure to South Korean stocks drove the bulk of its gains, as several positions rose sharply. Two long-held and large positions – Naver, South Korea's dominant search engine and e-commerce company, and Samsung SDI, a globally competitive company in battery technologies – both rose over 50% during the quarter.

At the same time, a number of stocks imposed a substantial drag on the Fund's performance: the Fund's exposure to smaller companies, particularly those domiciled in Hong Kong, underperformed amid the market's broader rally. Companies in the Special Administrative Region saw their business prospects struggle amid the prevailing political turmoil, and investors shied away from Hong Kong stocks generally out of concern for the territory's future, particularly as local activists wrestled with the possibility that Beijing might institute greater legal control (which occurred on June 30, when China's legislature enacted the "Law of the People's Republic of China on Safeguarding National Security in the Hong Kong Special Administrative Region.")

The Fund's holdings in other regions, including Brazil and Southeast Asia, also fared poorly relative to the index's rebound. In most instances, stocks rose, but well below the pace set by the index; and falling currencies negated such gains, such that many holdings outside East Asia contributed little to the Fund's recovery.

Allocation

During the second quarter, the Fund exited five positions: Bank Rakyat (one of Indonesia's largest banks), Ayala Corp (a holding company with substantial property and utility interests in the Philippines), Techtronic (a Hong Kong and China-based producer of power tools, available in many home improvement stores across the U.S.), Texwinca (a Hong Kong-based textile firm), and Hang Lung Properties (a company historically known for its residential developments in Hong Kong, but now principally engaged in developing and managing malls in mainland China).

The first three positions were remnants of the Selected Growth component of the Fund. (See Figure 1 for definitions of the Fund's Core, Selected Growth, and Value portfolio components.) As noted in previous reviews, I undertook an effort to re-evaluate all Selected Growth positions[5] after the Fund's management change in the fourth quarter of 2019. After that review, I determined that Bank Rakyat, Ayala Corp, and Techtronic failed to satisfy the more stringent requirements that I instituted for all Selected Growth constituents of the Fund.

Figure 1: Seafarer Overseas Growth and Income Fund – Portfolio Components

Core Holdings	Moderately underappreciated growth; Moderately elevated current yield
Selected Growth Holdings	Higher growth potential; Lower current yield
Value Holdings	Lower growth potential; Higher current yield

Texwinca and Hang Lung were both former constituents of the Value component of the Fund. Both companies have struggled in recent years in the face of rising competitive burdens – Texwinca from mainland China-based garment producers that deployed advanced technologies that eclipsed its capabilities; Hang Lung from China's manifold e-commerce retailers that are steadily undermining traditional shopping malls.

The proceeds from Hang Lung were deployed to establish a new position in Mondi PLC, another constituent of the Value component of the Fund. Mondi is a global paper and packaging company with a collection of production assets that we believe to be uniquely valuable and difficult to replicate. It has a string of paper and pulp milling factories located near cheap fiber sources in South Africa, Eastern Europe, and Russia, enabling it to produce at some of the lowest costs within its industry, resulting in favorable returns on capital in the past.

Outlook

Looking forward, I remain deeply concerned that stocks in the developing world are poised for weakness – none more so than the wildly overheated markets in China. My concern stems from two sources: elevated stock prices, and poor and uncertain corporate performance (as noted above, in the Performance section). The combination is usually a recipe for volatility and declining returns.

I am happy to report that the Fund has a silver lining amid the difficult conditions: the portfolio holdings are likely, in aggregate, to produce earnings growth in 2020 (even as profits contract -13% for the broader market). At present, the portfolio's aggregate profit growth is expected to be +19%. This statistic is exaggerated due to mathematical "base effects:" one company (First Pacific) produced losses in 2019, and as its performance "normalizes" (i.e., recovers to profitability), the resulting swing amplifies the apparent rate of growth for the overall portfolio. Yet even after adjusting for this effect by removing the company in question, the portfolio will likely produce modest growth for 2020. Six months of the year remain, and much may happen to derail expectations for future profits; yet at present, the resilience of earnings power for the Fund's holdings is remarkable. The stock markets may at present favor "growth" and "technology darlings," but amid such uncertain times and bubble-prone conditions, I favor a portfolio that produces tangible results, in accordance with the Fund's strategy (which seeks companies with sustained earnings, capable of servicing ample dividends, with the potential to grow such investment income over time).

On a final note, regarding the imposition of the new security law in Hong Kong: I acknowledge that China has a sovereign right to pursue security within its borders. I also acknowledge that Hong Kong is legally, culturally and fundamentally a part of China. Yet I worry that the aggressive imposition of this law will drain Hong Kong of the unique economic, social and political freedoms that set the city-state apart from (and ahead of) the rest of the world. The law may soon render Hong Kong no different from an "average mid-sized city" in China. If so, the resilient character that distinguishes its people and the competitive drive that is a hallmark of its companies will ebb away. I cherish Hong Kong, and I fervently hope that the new law does not portend a darker future for the city, or for that of China itself.

Thank you for entrusting us with your capital. We are honored to serve as your investment adviser in the emerging markets.

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July 31, 2020

[1] References to the "Fund" pertain to the Fund's Institutional share class (ticker: SIGIX). The Investor share class (ticker: SFGIX) returned 19.28% during the quarter.

[2] The Fund's inception date is February 15, 2012.

[3] The Fund's Investor share class began the quarter with a net asset value of $9.44 per share; it paid a semi-annual distribution of approximately $0.070 per share during the quarter; and it finished the quarter with a value of $11.19 per share.

[4] "Emerging Markets Equity Strategy Steering Board," J.P. Morgan, 2 July 2020.

[5] www.seafarerfunds.com/funds/ogi/portfolio-review/2019/12/Q4#allocation

Glossary

A-Shares: a class of securitized common stock in Chinese companies, traded exclusively on Chinese stock exchanges (i.e., Shanghai and Shenzhen), and denominated in renminbi, China's currency. Historically, the renminbi was subject to strict controls, such that foreign (i.e., non-Chinese) investors were not able to obtain or use the currency for financial purposes (i.e. savings or investment). Because of this constraint on the currency, A-shares were historically inaccessible to foreign investors, de facto: foreigners could not legally obtain renminbi for portfolio investment purposes, and therefore they could not fund any purchase of A-shares. Beginning in 2002, China liberalized the use of the renminbi for investment purposes, allowing selected, large foreign institutions to apply for Qualified Foreign Institutional Investor (QFII) status. Foreign institutions granted QFII status can legally purchase renminbi under a quota scheme, and that renminbi can be used to fund the purchase of A-shares and other financial assets within China. Beginning in 2014, China launched a second program known as the Stock Connect; this program allows foreign investors to purchase selected A-shares on the Shanghai or Shenzhen exchanges. A-shares are not to be confused with H-shares (Chinese companies incorporated in China, but listed in Hong Kong) and ordinary Hong Kong-listed companies of Chinese origin (Hong Kong incorporated, and Hong Kong-listed, but with substantial economic ties to mainland China).

If a Seafarer Fund is invested in Chinese A-Shares, please note the following: 1) any reduction or elimination of access to A-Shares could have a material adverse effect on the ability of the Fund to achieve its investment objective; and 2) uncertainties regarding China's laws governing taxation of income and gains from investments in A-Shares could result in unexpected tax liabilities for the Fund, which could adversely impact Fund returns.

Current Yield: a security's annual income (interest or dividends) divided by its current price.

People's Bank of China (PBOC): the central bank of the People's Republic of China, located in Beijing.

Special Administrative Region (SAR): a provincial-level administrative region of China that possesses a high degree of autonomy. According to the constitution of the People's Republic of China, there are two SARs in China: Hong Kong SAR and Macau SAR. Generally, a SAR is not considered to constitute a part of Mainland China.

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The performance data quoted represents past performance and does not guarantee future results. Future returns may be lower or higher. The investment return and principal value will fluctuate so that an investor's shares, when redeemed, may be worth more or less than the original cost. View the Fund's most recent month-end performance at www.seafarerfunds.com/funds/ogi/performance.

The MSCI Emerging Markets Total Return Index, Standard (Large+Mid Cap) Core, Gross (dividends reinvested), USD is a free float-adjusted market capitalization index designed to measure equity market performance of emerging markets. Index code: GDUEEGF.

The S&P 500 Total Return Index is a stock market index based on the market capitalizations of 500 large companies with common stock listed on the NYSE or NASDAQ.

It is not possible to invest directly in an index.

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As of June 30, 2020, Naver Corp. comprised 2.7% of the Seafarer Overseas Growth and Income Fund, Samsung SDI Co., Ltd. comprised 4.8% of the Fund, Mondi PLC comprised 2.1% of the Fund, and First Pacific Co., Ltd. comprised 1.3% of the Fund. The Fund did not own shares in Bank Rakyat Indonesia Persero Tbk PT, Ayala Corp., Techtronic Industries Co., Ltd., Texwinca Holdings, Ltd., or Hang Lung Properties, Ltd. View the Fund's Top 10 Holdings at www.seafarerfunds.com/funds/ogi/composition. Holdings are subject to change.

ALPS Distributors, Inc. is the distributor for the Seafarer Funds.

Investors should consider the investment objectives, risks, charges and expenses carefully before making an investment decision. This and other information about the Funds are contained in the Prospectus, which is available at www.seafarerfunds.com/prospectus or by calling (855) 732-9220. Please read the Prospectus carefully before you invest or send money.

Important Risks: An investment in the Funds involves risk, including possible loss of principal. International investing involves additional risks, including social and political instability, market and currency volatility, market illiquidity, and reduced regulation. Emerging markets are often more volatile than developed markets, and investing in emerging markets involves greater risks. Fixed income investments are subject to additional risks, including but not limited to interest rate, credit, and inflation risks. Value investments are subject to the risk that their intrinsic value may not be recognized by the broad market. An investment in the Funds should be considered a long-term investment.