February 10, 2021

Dear Appleseed Shareholder:

"Deadly Charybdis—can't I possibly cut and run from her
And still fight Scylla off when Scylla strikes my men?"

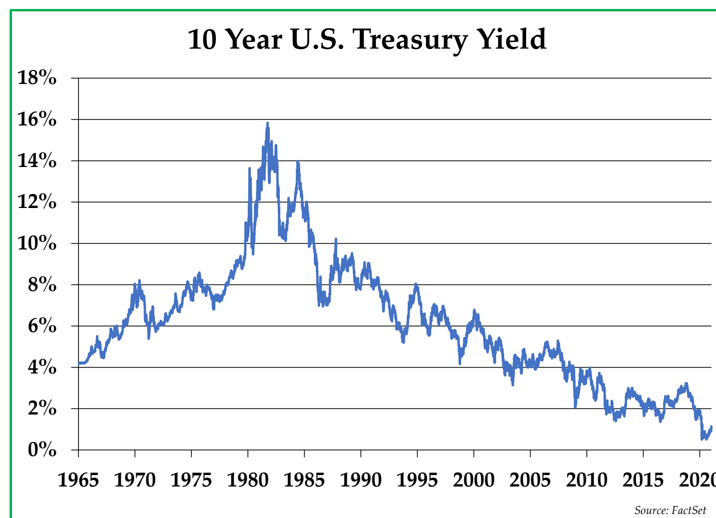
— the *Odyssey*, as spoken by Odysseus

In Homer's legendary epic, the *Odyssey*, Odysseus is forced to navigate his ship through a dangerous passage with legendary sea monsters, Scylla and Charybdis, threatening his crew on both sides. He tries his best, keeping the ship slightly closer to Scylla, which he deems to be less threatening than Charybdis. In the end, his ship makes it through the strait, but not without losing six men to Scylla.

Today, investors are being forced to navigate through a treacherous strait in the market, with bonds generating near-zero income yields on one side and stocks with increasing volatility on the other side. Making it past the strait, to a time when financial markets return to some semblance of normalcy, will be difficult and filled with challenging trade-offs. The fact that this hazardous journey will likely last for years makes it all the more perilous.

The Low Bond Yield Conundrum

Unfortunately, the bond market has become almost uninvestable. The 10-year Treasury's yield-to-maturity is currently 1.1%, which is more than it was in August 2020 when it touched an all-time low of 0.5%, but this paltry yield is still nowhere close to compensating investors for future inflation. Put differently, the real (*i.e.*, inflation-adjusted) interest rate on 10-year U.S. Treasury bonds is currently *below 0%*. While these yields are pitifully low, they stand well above the negative interest rates available from European and Japanese government bonds. The chart below shows 10-year Treasury yields dating back to 1965.



Moreover, the problem of bond yields being too low is not limited to the Treasury market. As Treasury yields have declined, so too have municipal bond yields and corporate bond yields. As recently as 15 years ago, an investor could purchase high quality, investment-grade corporate bonds that yielded 5.5% or more until maturity without too much difficulty. Today, most investment-grade corporate bonds offer inflation-adjusted yields below 0%. Currently, 75% of the global bond market pays a yield of less than 1%, while only 10% of the global bond market pays a yield

of more than 3%.[1] Unsurprisingly, those bonds that pay a yield of more than 3% today are generally classified as either 1) "junk" bonds, issued by companies with weak balance sheets and significant credit risk or 2) have maturities that force the owners to bear material interest rate risk. In fact, a record amount of global bonds trade with a negative nominal yield, representing about $17 trillion in total value, which means that holders are certain to receive a negative return from holding their bonds to maturity.

Making matters worse, we expect that bond yields could remain this low for years. The Debt/GDP ratio for the United States and for the rest of the world is currently at a record high level. As a result, should the 10-Year Treasury bond yield rise to just 4%, it would create enormous problems for the U.S. economy, as debt service costs would skyrocket for consumers, corporations, and governments alike. The result would likely be a ballooning Federal deficit, widespread debt defaults, a housing crash, and a market crash. Knowing this, the Federal Reserve printed more than $10 trillion in 2020 to purchase U.S. Treasury bonds, keeping Treasury yields low and providing financing for record-breaking U.S. deficits. As long as the Debt/GDP ratio remains high, the Federal Reserve will likely continue printing money to buy Treasuries and keep bond yields as low as possible.

As a result, our base case expectation is that investors in U.S. Treasuries, investment-grade municipal bonds, and investment grade corporate bonds are likely to generate negative real (inflation-adjusted) returns for years, to the financial detriment of bond investors.

Bond Alternatives

We have historically owned an allocation to bonds in Appleseed Fund for two reasons. First, bonds used to provide an attractive fixed income return. Second, bond prices are less volatile and tend to be uncorrelated to stock prices; Appleseed shareholders realized a diversification benefit from owning bonds and stocks together in a balanced portfolio.

Even with uncommonly low bond yields, owning bonds can still provide a portfolio diversification benefit. However, without enough yield, it is difficult to invest a meaningful allocation to investment grade bonds because the expected return is simply too low. Instead of bonds, we are looking at a wide range of bond substitutes, none of which are perfect, but all of which offer certain advantages over investment-grade corporate, municipal, and Treasury bonds today. Of course, there is no free lunch in investing; these substitutes also have their own disadvantages relative to bonds.

- Equity-like Substitutes for Corporate, Municipal, and Treasury bonds:

  - *Dividend paying stocks:* Most publicly traded stocks pay a dividend and, depending on the company and the industry, certain stocks offer investors an attractive dividend yield. The stock market is richly valued primarily because technology stocks are especially expensive, and most technology stocks do not pay a large dividend. However, blue-chip companies outside of the technology industry are not as richly valued, and many of them pay an attractive dividend to investors. For example, **SK Telecom's (SKM)** dividend yield currently stands at 3.1%.

    - *Advantages vs. bonds:* Better tax treatment on dividend payments, higher yields, potential for capital appreciation

[1] Source: Deutsche Bank.

- *Disadvantages vs. bonds:* Price volatility, potential for capital loss

- *Real estate:* Real estate investments generate cash flow from rental or lease income and generally pay out that cash flow to investors. In Appleseed Fund, we recently purchased **Simon Properties (SPG)** during the quarter, which offers a dividend yield of more than 8% at the time of our purchase.

  - *Advantages vs. bonds:* Higher yields, potential for capital appreciation
  - *Disadvantages vs. bonds:* Illiquidity, potential for capital loss, available only to accredited investors

- *Business development companies:* Business development companies ("BDCs") are investment companies that buy leveraged loans and pay out all of their earnings to investors. Leveraged loans are generally issued by companies that do not have a strong balance sheet, so the interest rate is well above the interest rates offered by investment-grade bonds. If a company goes bankrupt, leveraged loans receive the first priority in the capital stack, ahead of bonds, which means that leveraged loans generally recover more than bonds do in the case of bankruptcy.

  - *Advantages vs. bonds:* Better yield, potential for capital gain
  - *Disadvantages vs. bonds:* Price volatility, potential for capital loss

- *Mortgage REITs:* Mortgage real estate investment trusts ("REITs") are investment companies that buy mortgage-backed securities using leverage and, like BDCs, distribute nearly all of their income to investors as dividends. The safety of these investments typically depends on the investment strategy. Some REIT managers pursue a more aggressive approach by purchasing junk-rated mortgage-backed securities, while others only buy the highest quality issues. **Annaly Capital Management (NLY)** is an example of one of these mortgage REITs.

  - *Advantages vs. bonds:* Better yield, potential for capital gain
  - *Disadvantages vs. bonds:* Price volatility, potential for capital loss

- *Convertible Bonds:* Convertible bonds pay a regular coupon and have an embedded option for the investor to convert the bond to common stock at a price well above the stock price at the time of convertible issuance. During the depths of the pandemic chaos of 2020, we purchased Spirit Airlines (SAVE) convertibles at an attractive price, and that convertible is now well into the money.

  - *Advantages vs. bonds:* Potential for capital gain
  - *Disadvantages vs. bonds:* Price volatility, potential for capital loss, lower in the capital stack

- <u>Bond-like Substitutes for U.S. Corporate, Municipal, and Treasury bonds</u>

  - *Closed-end bond funds:* Closed-end bond funds are pooled investment funds that are deployed in a specific bond strategy. As "closed-end" funds, their shares can be purchased throughout the trading day, and the price of those shares could trade at a premium or a discount to the net asset value of the underlying assets. In some instances, we can find closed-end bond funds that are trading at

substantial discounts to net asset values, allowing us to indirectly purchase bond portfolios that offer investors a better yield than buying investment grade fixed income securities.

- *Advantages vs. bonds:* Better yield
- *Disadvantages vs. bonds:* Price volatility, liquidity.

- *Preferred stocks:* Preferred stocks are fixed-income issues of companies that receive a lower priority than bonds in the capital stack. A wide variety of companies issue preferred stock, but financial services companies tend to issue preferred stock more than the companies from other industries. Because preferred stocks are riskier than straight bond issues, the yield is typically far higher. Most preferred stocks do not mature for years, which means that the price of preferred stock issues will decline should interest rates rise significantly.

    - *Advantages vs. bonds:* Better yield, sometimes better tax treatment
    - *Disadvantages vs. bonds:* Price volatility, potential for greater capital loss in a bankruptcy

- *Inflation protected bonds:* Many kinds of inflation-protected bonds exist, but the most common are Treasury Inflation-Protected Securities ("TIPS"). The par value of these bonds step up with the Consumer Price Index, which provides some inflation protection for investors. Inflation protected bonds perform best when inflation expectations are rising quickly, and they perform worst when inflation expectations are falling quickly.

    - *Advantages vs. bonds:* Potential for capital appreciation
    - *Disadvantages vs. bonds:* Price volatility, lower yield

- *Emerging market debt*: Emerging market debt is issued by emerging market sovereign governments or companies and is denominated in foreign currency. Emerging market debt typically pays a somewhat attractive yield because investors need to be paid for the currency risk and credit risk of owning such bonds. Emerging market debt can be an attractive asset class to own when the dollar is depreciating but an unattractive asset class to own when the dollar is appreciating against various emerging market currencies.

    - *Advantages vs. bonds:* More yield, potential for capital appreciation
    - *Disadvantages vs. bonds:* More volatility, potential for capital losses

- <u>Other Substitutes for U.S. Corporate, Municipal, and Treasury bonds</u>

- *Precious metals:* Gold is also a worthwhile bond alternative. It does not pay investors any income, but bonds do not pay investors much income anymore either. Unlike U.S. dollar-denominated bonds, however, gold can appreciate in price as the dollar depreciates. Gold also tends to rise in price when real bond yields are negative, as they are today. Moreover, the gold price is uncorrelated to stocks. It can provide significant diversification benefits to a portfolio, which is an important consideration for investors who own stocks and are reducing their fixed income exposure. For example, between February and March of last year, the S&P 500 Index declined by 33.9%, while gold only declined by 2.8%. Appleseed Fund owns a meaningful allocation to several trusts that own physical gold bullion stored in a vault.

Biggest S&P 500 Declines	S&P 500	Gold
9/1976-3/1978	-19.4%	53.8%
8/1987-12/1987	-33.5%	6.2%
7/1990/10/1990	-19.9%	6.8%
3/2000-10/2002	-49.0%	12.4%
10/2007-3/2009	-56.8%	25.5%
5/2011-10/2011	-19.0%	9.4%
2/2020-3/2020	-33.9%	-2.8%

Source: Incrementum AG, Factset.

  - *Advantages vs. bonds:* Potential for capital appreciation, hedge against inflation.
  - *Disadvantages vs. bonds:* No yield.

- *Bitcoin:* While gold is a commodity currency, bitcoin is a digital currency. We favor gold over bitcoin, but, like gold, bitcoin provides diversification benefits due to its low correlation to other asset classes. As investors move capital into assets which might serve as a better store of value than low-yielding bonds or cash, bitcoin's price will have to rise to accommodate the inflows. Appleseed Fund currently has a modest position in bitcoin through the **Grayscale Bitcoin Trust (GBTC)**.

  - *Advantages vs. bonds:* Potential for capital appreciation, hedge against inflation.
  - *Disadvantages vs. bonds:* No yield.

- *Cash*: Put simply, cash is cash. It yields nothing currently, but it is safe and has no volatility. Moreover, cash is the very definition of what it means to be liquid. As a short-term store of value, cash still works perfectly well as a bond substitute.

  - *Advantages vs. bonds:* No price volatility, more liquidity
  - *Disadvantages vs. bonds:* Lower yield

Portfolio Construction

Each of these bond substitutes acts somewhat differently, with varying volatility, yield, liquidity, and diversification parameters along with unique advantages and disadvantages versus bonds. Unfortunately, there is no single perfect replacement for corporate, municipal, and government bonds. Our general approach in the coming years will be to employ a mix of substitutes depending on valuation and the risk/reward profile that we perceive there to be. We are more likely to own an equity-centric portfolio, as we do today, along with the additional volatility that comes with owning more equities.

Our goal in making these adjustments is to generate more income than we would otherwise earn with a straight bond portfolio while managing the additional volatility as best we can that comes with some of these alternative securities. Navigating between the bond market Scylla of low rates and the stock market Charibdys of increased volatility requires thoughtfulness, prudence, and an intense focus on investment ideas that maintain or increase the inflation-adjusted value of your Appleseed Fund portfolio.

Performance

Appleseed Fund's absolute and relative performance was strong coming into the end of 2020. Appleseed Fund Investor shares generated a 27.21% return during Q4 2020 and a 7.50% during the full year of 2020. Since its inception in December 2006, Appleseed Fund has generated an annualized return of 5.70% per annum. Our performance between the second half of 2020 and the first half of 2020 could not be more different, although our strategy remains the same. We look to commit capital to high quality, sustainable, and undervalued businesses. We are encouraged to finally see Mr. Market start to appreciate some of the value that we have always seen in our investment portfolio.

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We wish you and your families a happy, healthy, and prosperous 2021. Thank you again for your trust in our firm's ability to navigate your Appleseed investment through this uncertain time. Should you have any follow up questions, please do not hesitate to contact Colin Rennich (colin@appleseedfund.com).

Sincerely,

William Pekin, CFA

Josh Strauss, CFA

Adam Strauss, CFA

Shaun Roach, CFA

ANNUALIZED RETURNS- as of 12/31/2020					
	1 Year	3 Years	5 Years	10 Years	Since Inception
Investor Class (APPLX)	7.50%	6.30%	9.17%	6.18%	6.63%
Institutional Class (APPIX)	7.77%	6.52%	9.38%	*6.40%*	*6.66%*
Morningstar Gbl SMID Cap Index	14.53%	7.71%	11.14%	8.70%	6.89%
MSCI World Index	15.90%	10.54%	12.19%	9.87%	6.52%

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 12/31/2020, the Fund's Top Ten Holdings can be found at: www.appleseedfund.com.
Holdings are subject to change.

Current and future portfolio holdings are subject to risk. Pekin Hardy Strauss Inc. holds Annaly Capital Management (NLY) in some of their separately managed accounts.

The gross expense ratio of the Fund's investor class is 1.50%, and the institutional class is 1.25%; the net expense ratio after contractual fee waivers through January 31, 2022 is 1.19% and 1.00%. 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. The Russell 2000 Value Index is a widely recognized unmanaged index that measures the performance of the small-cap value segment of the US equity universe. 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 Cyclically Adjusted P/E Ratio (CAPE) is a valuation measure usually applied to the S&P 500 equity market. It is price divided by the average of ten years of earnings, adjusted for inflation. EBITDA (earnings before interest, taxes, depreciation and amortization) is a measure of company profitability. CAGR

(compound annual growth rate) is the rate of return that would be required for an investment to grow from its beginning balance to its ending balance. ROIC (return on invested capital) is a profitability ratio that aims to measure the percentage return that a company earns on invested capital. EPS (earnings per share) is the monetary value of earnings per outstanding share of common stock for a company.

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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