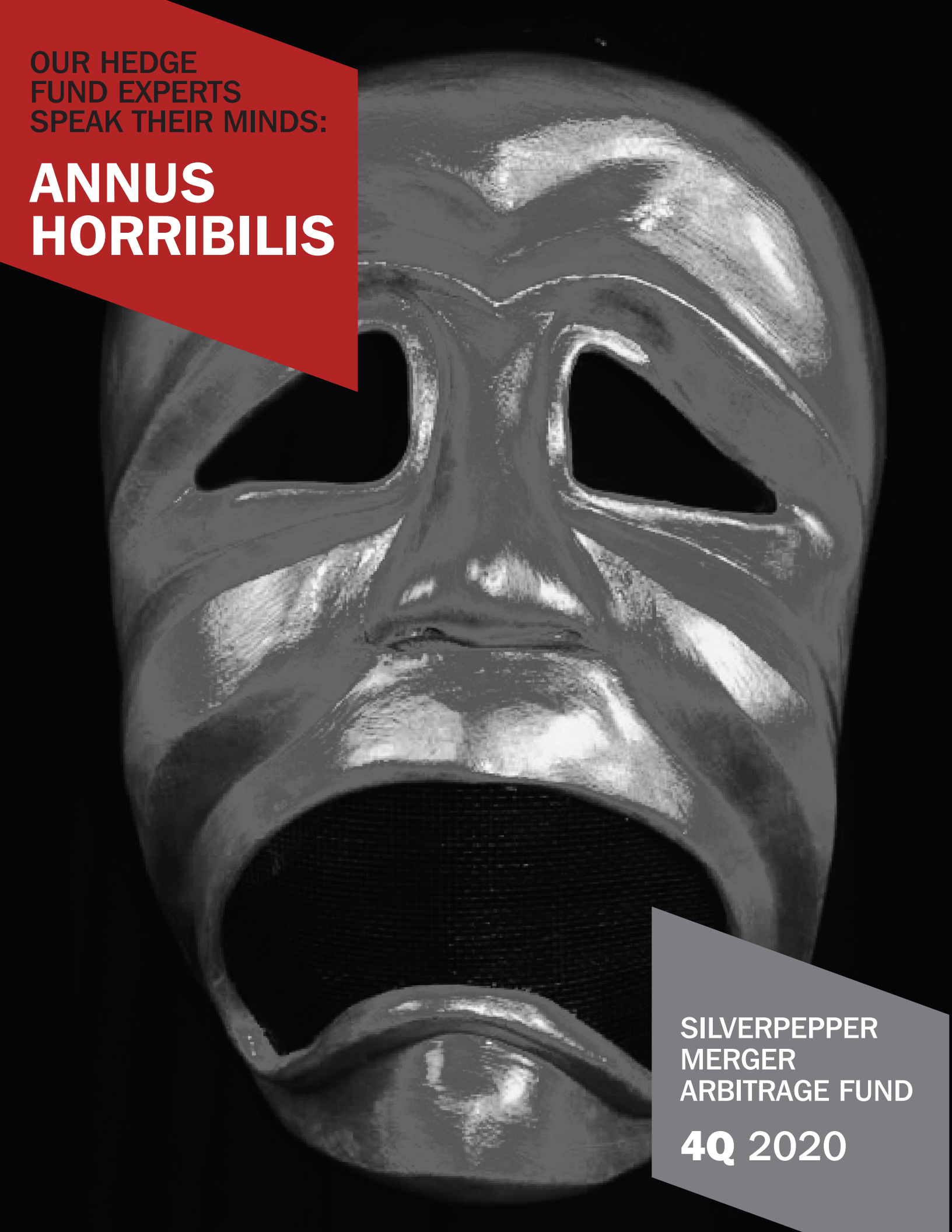
OUR HEDGE FUND EXPERTS SPEAK THEIR MINDS:

ANNUS HORRIBILIS



SILVERPEPPER MERGER ARBITRAGE FUND

4Q 2020

How bad was 2020? Awful. Terrible. The worst. So bad, that like a dreadful medical diagnosis, we can only describe it in Latin: *Annus Horribilis* — the Horrible Year.

We started the year 2020 with quaint concerns about BREXIT, and the impending trade war with China. We then experienced a biblical string of calamities: the political crisis of an impeachment, the plague of a global pandemic, a record-breaking economic recession, lockdowns which have permanently closed many small businesses, race riots, a contested election, and civil unrest. Not surprisingly, this has been the most challenging year of my investment-management career.

I'm sure you have your own horror stories from 2020, so I will only describe here the fallout from the "COVID Crash" of the financial markets. Talk about a Black Swan event. On Monday March 16th, market participants were spooked by the Fed's emergency response to the looming economic shutdown. The S&P 500 lost 11.98%, and the SilverPepper Merger Arbitrage Fund suffered the worst day in its history, contributing to the Fund's 7.76% loss in March. Almost every merger deal spread in our portfolio widened dramatically. Multiple holdings were down more than 20%. That was by far the darkest day of my investment management career.

The entire merger arbitrage sector experienced extreme, if not irrational selling. Merger spreads widened because of indiscriminate selling and forced de-risking of the merger arbitrage market. Spreads widened regardless of the underlying deals' quality, or legally agreed-upon terms. Liquidity quickly evaporated, as numerous highly-leveraged merger arbitrage hedge funds experienced margin calls, resulting in reduced position sizes. Some hedge funds were even forced to liquidate entirely. Merger arbitrage managers simply did not have the confidence necessary to keep spreads in line and market conditions did not allow for cross-over buyers to enter the market. The average merger deal spread went from 5.6% at the end of February to nearly 23% by mid-March. Riskier deals were offering spreads north of 100%.

SILVERPEPPER MERGER ARBITRAGE FUND INSTITUTIONAL MONTHLY RETURNS (%)													
	JAN	FEB	MAR	APR	MAY	JUN	JUL	AUG	SEP	OCT	NOV	DEC	YEAR
2013											0.10	1.00	1.10
2014	-0.10	0.10	0.10	- 1.48	1.40	0.69	0.79	0.68	-0.77	-0.10	1.37	-0.23	2.44
2015	0.60	0.99	0.10	0.29	0.78	0.10	0.48	0.77	0.19	2.47	0.19	1.25	8.49
2016	1.13	0.37	0.00	0.37	0.37	0.18	0.64	-0.27	0.46	-0.18	-0.09	1.25	4.30
2017	-0.18	0.00	0.36	0.36	0.18	0.54	-0.54	0.36	0.90	0.00	0.00	0.57	1.76
2018	-0.18	0.45	-0.36	0.00	0.45	0.18	0.72	0.44	-1.15	0.09	0.63	-0.81	0.44
2019	1.28	0.00	0.90	-0.36	0.09	-0.09	1.08	0.71	-0.18	0.97	-0.35	1.11	5.26
2020	-0.18	-0.36	-7.76	3.13	-1.80	0.00	-1.10	0.39	0.58	0.48	0.10	0.10	-5.66

One-Year Return as of 12/31/2020	-5.66
Five-Year Annualized Return as of 12/31/2020	1.15
Total Annualized Return Since Inception, (11/1/2013)	2.45

The returns represent past performance. Past performance does not guarantee future results. Investment returns and principal value of an investment will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted. Call 855-554-5540 for current to most recent month-end performance.

Total gross/net fund annual operating expenses are 3.04%/2.98% for Institutional and 3.23%/3.23% for the Advisor shares. The Advisor has contractually agreed to waive its fees and/or pay for expenses to ensure that total fund operating expenses (excluding, as applicable taxes, leverage interest, brokerage commissions, dividend and interest expenses on short sales, acquired fund fees and expenses (as determined in accordance with Form N-1A), incurred in connection with any merger or reorganization, or any extraordinary expenses such as litigation expenses) do not exceed 1.99% for the Institutional class and 2.24% for the Advisor class. This agreement is in effect until October 31, 2030. Inception dates for both share classes is October 31, 2013. Performance and risk measures greater than one year are annualized.

One factor that exacerbated the volatility the Fund experienced in mid-March was the weight of assets we had in cash deals. In cash deals, we only "go long" the target company — the company being acquired. Since the acquirer is not paying for the acquiree in stock, there is no short position to act as a hedge. Now, cash deals are typically good deals. They make sense when, like now, money to borrow is cheap. And they close at the same rate as stock deals. However, because of what happened with some big arb firms in March, spreads widened out, with no buyers emerging. This caused additional volatility in our portfolio.

Tallgrass (TGE) is a good example of a cash deal, with no buyers emerging, even as the spread widened dramatically. Our conviction paid off with Tallgrass — no deal risk materialized (we made money when the deal closed), but as a result, volatility was substantially increased at the overall portfolio level.

From the ashes of March 16th, we started rebuilding immediately. On March 17th, the stock and merger markets started a rocky recovery. Amazingly, the stock market bounce started soon after. March 24th was the starting point for a rally that has proven to be one of the best in market history. Driven by optimism that the economic recession would be V-shaped, and that the scientific community would be able to defeat the virus, the S&P 500 rebounded nearly 60% through the end of December. The Fund rebounded as well, up 12.89% over this period. As you can see from the table above, after our worst month in March, April was our best month in our history. This confirms that the volatility that we were forced to endure was primarily driven by fear.

As the merger market normalized, so did the Fund's performance. From August through the end of the year, the Fund averaged 32 basis points per month, which is nearly identical to its long-term monthly average through 2019. In fact, since the plunge on March 16th, our Fund performed a bit better than average among those funds specializing in merger arbitrage. While the other specialty merger arbitrage funds went up on average 12.29%, our SilverPepper Merger Arbitrage Fund went up 12.89%.

In the more than seven years since our Fund's inception, our Fund's performance has dwarfed its Morningstar "Market Neutral" category, whose funds have only managed a 0.38% gain per year, while our Fund earned 2.45% per year. The average of the Funds in the specialty merger arbitrage group did even better, at 2.87% per year.

Merger Arbitrage Deal Activity

Merger arbitrage deal activity has taken longer to revive than market performance. The merger and acquisitions markets remained basically shut down through June. During the early stages of the pandemic, management teams were scrambling around, trying to figure out how to proceed. Soon, it became apparent that the most popular course of action was to just hunker down. That caused merger announcements, and our arbitrage business, to grind to a halt. In July and August, as many states loosened their lockdowns and bankers begun to adapt to using Zoom, M&A activity showed a faint heartbeat. In September, merger activity came to life for the first time. Finally, the week before Christmas was one of the year's best for merger announcements — and usually, that week is one of the worst.

In 2021, it appears some management teams have been able to gain sufficient clarity to reengage. Investors have been waiting to see who would prevail in the elections. They now have a much better idea of which industries are more likely to benefit, and which are more likely to be scrutinized, under a government controlled in the House, Senate, and Administration by the Democrats. Armed with this information, investment bankers can quickly get back to work crafting their sales pitches.

Furthermore, with the beginning of effective vaccinations, we are hopeful that things will begin to return to normal in early 2021. How so? Because those companies that saw their business boom during COVID, now have either cash on the balance sheet, or highly appreciated stock, to use to make acquisitions. And those companies that suffered during COVID need buyers — buyers that can provide capital, economies of scale, or other synergies — to get them out of trouble. Deals will happen. And that's not just our view — basically every brokerage house is calling for 2021 to be a record year for M&A activity.

Lessons Learned From The Crisis

My team and I analyzed the potholes we hit in 2020. Yes, we've got some dented wheel-rims, but we've learned some valuable lessons.

The first lesson is that we need to prepare for another business shutdown, like we saw in March.

And here's how we've prepared the Fund:

A) We exited all deals that were announced prior to COVID-19. This should reduce our exposure to transactions that may be more likely to be terminated, or renegotiated (like the LVMH / Tiffany deal was).

B) Until industry conditions normalize, we are attempting to avoid industries susceptible to another economic shutdown, such as retail, hotels and airlines.

C) We are emphasizing deals that contain strong force-majeure clauses, which deal with such unanticipated shocks.

D) We are doing enhanced due diligence on the reputation and credibility of acquirers, especially if they are financial buyers. For example, we have been shocked that CEOs of multi-billion-dollar companies have such disregard for contracts (Eh, did we already mention LVMH's Bernard Arnault's actions with Tiffany or David Simon's actions with Taubman Centers?). These CEOs reveal their willingness to throw away their credibility as future acquirers.

E) We are monitoring more closely the percentages in the portfolio of cash versus stock transactions. Yes, we have always done this, for risk-management purposes, at the portfolio construction level. Although cash and stock deals close at similar rates, the higher percentage of cash deals in our portfolio is about the only common thread we can find among the four deals in 2020 that contributed the bulk of the Fund's volatility during COVID-19. Therefore, though we're not setting strict limits on the percent of the portfolio in cash deals, we are monitoring this factor more closely and increasing the weight of it in our decision-making process, as a way to potentially reduce volatility in the portfolio.

But the second lesson we learned is that there is some amount of merger-arbitrage risk that is very difficult to diversify away. Despite owning a diversified portfolio of merger investments, there is a certain amount of risk that we must accept. The 2020 COVID Crash, and the months-long lockdowns which followed, were a Black Swan event that caused multiple deal breaks, and multiple stressed deals — all at the same time. COVID simply exposed the limits of risk-management — and a risk-management process that has historically, at least prior to March of 2020, made us among the least risky (either volatility or downside losses) in our Morningstar, market-neutral, category.

Our Current Portfolio

Our current portfolio reflects the lessons we've learned. We have 19 deals in the portfolio. Our predominant sector exposures are in technology, healthcare and financials. We're close to fully invested, with 85% long positions. Meanwhile, our 31% exposure to short positions reduces our net equity exposure, to just over 50%. That should cushion the blow, in the event of another equity-market shock. We're optimistic overall because the spreads available on these deals are more attractive than usual. Perhaps that's a result of capital exiting merger arbitrage strategies, or perhaps because of continued concern about the return of Black Swan risk.

Finally, I want to say I hate what happened in March of 2020, and that it led to our -5.66% loss for the year. Yet, throughout my 20-plus years of managing merger portfolios, I had similar months of equally crummy performance, most notably in April of 2001, and November of 2007. Each time we learned and we tweaked our process — like we are doing now. Our process, our criteria, and our risk aversion have allowed us to make up these losses, historically, and continue to compound returns. In my 21 years of merger arbitrage management, this is only our third year of negative returns. Despite other tough periods, we have always come back strong by focusing on our "dime after dime, time after time" investment principles. That continues to be our objective.

Yes, 2020 was an *Annus Horribilis* — a Horrible Year. I thank you again for entrusting me with your hard-earned money. It is time to stop typing and to get to work making 2021, at least investment-wise, an *Annus Mirabilis* — a wonderful year.

With respect,

Steve Gerbel

Portfolio Manager

SilverPepper Merger Arbitrage Fund

Investors should carefully consider the Fund's investment objectives, risks, charges and expenses. Please see the prospectus for a complete discussion of the risks of investing in this Fund. To obtain a prospectus, please call 855-554-5540 or visit silverpepperfunds.com. The prospectus is boring but should be read carefully before investing.

All investing involves risk including the possible loss of principal. There can be no assurance that the Fund will achieve its investment objective. For the Merger Arbitrage Fund, the primary risk is event risk, which revolves around the successful or unsuccessful completion of an announced merger or acquisition. If a merger doesn't close as expected, the fund could lose money. Other risks include smaller companies risk, foreign investment risk, derivatives risk and non-diversification risk.

As of December 31, 2020 the SilverPepper Merger Arbitrage Fund's portfolio holdings did not include securities discussed in this document. Portfolio holdings are subject to change without notice and are not intended as a recommendation.

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