



Semper MBS Total Return Fund Quarterly Conference Call

January 25, 2018, 11:30 a.m., E.T.

Chairperson: Greg Parsons, CEO, Semper Capital Management, L.P.

Definitions:

HPA: Housing Price Appreciation.

SFR: Single Family Rental Securitizations.

Cash Flow: Mortgages typically have required monthly interest and principal payments which are collected by servicers of mortgage-backed securities trusts, which in turn distribute these payments to MBS investors.

Duration: Measure of a bond or bond portfolio's sensitivity to changes in interest rates. Generally, the longer the duration, the greater the price change relative to interest rate movements.

Basis Points: A unit of measure that is equal to 1/100th of 1%, and is used to denote the change in a financial instrument.

Bloomberg Barclays 1-3 Year Government Index: The Index includes Treasury and Agency securities issued by the U.S. Government with a maturity from 1 up to (but not including) 3 years. This unmanaged Index contains only dollar-denominated, investment grade issues with at least \$250 million par outstanding. One cannot invest directly in an index.

Bloomberg Barclays Aggregate Index: The Index is a market capitalization-weighted index, meaning the securities in the index are weighted according to the market size of each bond type. Most U.S. traded investment grade bonds are represented. Municipal bonds, and Treasury Inflation-Protected Securities are excluded, due to tax treatment issues. The index includes Treasury securities, Government agency bonds, Mortgage-backed bonds, Corporate bonds, and a small amount of foreign bonds traded in U.S. One cannot invest directly in an index.

Bloomberg Barclays MBS Index: Covers agency mortgage-backed pass-through securities - both fixed-rate and hybrid ARM - issued by Ginnie Mae (GNMA), Fannie Mae (FNMA), and Freddie Mac (FHLMC). Pool aggregates must have at least \$250 million outstanding with a weighted average maturity of at least 1 year. One cannot invest directly in an index.

NAV: Net Asset Value, i.e. the value of the Fund's assets minus the value of its liabilities.

Yield to Maturity: Anticipated rate of return on a bond if held until the maturity date.

Correlation: Statistic measure of how two securities move in relation to each other.

SEC Yield: A standard yield calculation developed by the Securities and Exchange Commission (SEC) that is based on the most recent 30-day period covered by a fund's filings with the SEC. The yield figure reflects the dividends and interest earned during the period, after the deduction of the fund's expenses.

Effective Duration: Calculation for bonds with cash flow variability. It takes into account that expected cash flows will fluctuate as interest rates change.

S&P 500: An index of 500 stocks seen as a leading indicator of U.S. equities and a reflection of the performance of the large cap universe, made up of companies selected by economists.

Indicated yield: The dividend yield that a share of stock would return based on its current indicated dividend. The share class referenced on the conference call is SEMIX.

Par: The face value of a bond.

SASB: Single asset single borrower.

Alt-A: A classification of mortgages where the risk profile falls between prime and subprime.

Credit Quality weights by rating are derived from the highest bond rating as determined by Standard & Poor's ("S&P"), Moody's or Fitch. Bond ratings are grades given to bonds that indicate their credit quality as determined by private independent rating services such as S&P, Moody's and Fitch. These firms evaluate a bond issuer's financial strength, or its ability to pay a bond's principal and interest in a timely fashion. Ratings are expressed as letters ranging from 'AAA', which is the highest grade, to 'D', which is the lowest grade. In limited situations when none of the three rating agencies have issued a formal rating, the Advisor will classify the security as nonrated.

Morningstar Proprietary Ratings reflect risk-adjusted performance as of 1/31/18. The Morningstar Rating™ for funds, or "star rating", is calculated for managed products (including mutual funds, variable annuity and variable life subaccounts, exchange-traded funds, closed-end funds, and separate accounts) with at least a three-year history, without adjustment for sales loads. Exchange-traded funds and open-ended mutual funds are considered a single population for comparative purposes. It is calculated based on a Morningstar Risk-Adjusted Return measure that accounts for variation in a managed product's monthly excess performance, placing more emphasis on downward variations and rewarding consistent performance. The top 10% of products in each product category receive 5 stars, the next 22.5% receive 4 stars, the next 35% receive 3 stars, the next 22.5% receive 2 stars, and the bottom 10% receive 1 star. The Overall Morningstar Rating™ for a managed product is derived from a weighted average of the performance figures associated with its three-, five-, and 10-year (if applicable) Morningstar Rating™ metrics. The weights are: 100% three-year rating for 36-59 months of total returns,

60% five-year rating/40% three-year rating for 60-119 months of total returns, and 50% 10-year rating/30% five-year rating/20% three-year rating for 120 or more months of total returns. While the 10-year overall star rating formula seems to give the most weight to the 10-year period, the most recent three-year period actually has the greatest impact because it is included in all three rating periods. As of 1/31/18 the Semper Short Duration Fund received a 5-Star Overall Morningstar Rating™ and 5-Star 3-Year Morningstar Rating™ among 141 ultrashort-term bond funds. The Fund received a 5 star rating for the 5 year period out of 110 Ultrashort- term bond funds. The rating is specific to SEMIX and SEMRX. The Overall Morningstar Rating for a fund is derived from a weighted average of the performance figures associated with its three-, five- and ten-year (if applicable) Morningstar Rating metrics. ©2017 Morningstar, Inc. All Rights Reserved. The information contained herein (1) is proprietary to Morningstar (2) may not be copied or distributed and (3) is not warranted to be accurate, complete or timely. Neither Morningstar nor its content providers are responsible for any damages or losses arising from any use of this information.

Diversification does not guarantee a profit or protect against a loss in declining markets. Fund holdings and/or sector allocations are subject to change at any time and are not recommendations to buy or sell any security.

Past performance does not guarantee future results.

Operator: Ladies and gentlemen, thank you for standing by. At this time, I would like to welcome everyone to the Semper MBS Total Return Fund Quarterly Call. The views expressed on this call are the current views of the participants and are not intended as a forecast or as investment recommendations. Any information provided with respect to the fund is as of the date described and is subject to change at any time. Performance data quoted represents past performance. Past performance does not guarantee future results. The investment return and principal of 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 of the funds may be lower or higher than the performance quoted. Performance data current to the most recent month end may be obtained by calling 855-736-7799. After the speakers' remarks, there'll be a question-and-answer session. To ask a question, please press "star" then the number "one" on your telephone keypad. To withdraw your question at any time, please press the "pound" key. I will now turn the call over to Greg Parsons of Semper Capital Management.

Greg Parsons: Thank you. Well, I want to start off by saying thank you for everyone whose called in today for our quarterly conference call on the MBS Total Return Fund. My name is Greg Parsons and I'm the CEO of Semper Capital Management. I'm joined on today's call by Tom Mandel, co-founder of the firm and a senior portfolio manager on the fund.

Tom and I will spend, give or take, 20 minutes providing an update on the Semper MBS Total Return Fund, a mortgage focused mutual fund we launched in mid-2013 and we'll break the call into three parts. First, we'll give you a quick update on Semper and what we're seeing in the overall markets, second, Tom will go into greater detail around the specifics of the Fund, and last, we'll open it up to questions.

As many of you know, Semper is a privately-owned asset management platform and we focus our efforts within the structured credit space, specifically residential mortgage-backed securities (RMBS), commercial mortgage-backed securities (CMBS), and asset-backed securities (ABS). Our AUM now is pushing on \$2 billion and it's spread across a range of structured credit strategies that include absolute return, total return and index-based solutions. Our skill set is available across multiple product formats to include public funds, private funds and institutional separate accounts.

Frankly, 2017 was a year of milestones for us. We crossed the 25-year mark since our founding in 1992. We crossed the 20-year mark for one of our institutional clients in the mortgage space and the MBS Total Return Fund crossed a billion in assets. It's continued to grow up to about \$1.2 billion at the time of this call. Our platform is as strong as it's ever been with respect to people, resources and products and we believe our distinct positioning within the universe of fixed-income investments will allow us to continue to capitalize on opportunities for our clients and partners.

Let me share some of Semper's current thoughts related to the opportunity we continue to see in market. Again, we remain grossly long-biased the opportunity on both an absolute and relative basis within the structured credit space. Even in today's levels, with most non-agency MBS and other mortgage and structured credit sectors at post-crisis tights, we continue to see

opportunities to drive value on both an absolute and relative basis. Strengthening in real estate credit fundamentals, the structure of the market and strong technical factors continue to work together to create what we believe to be one of, if not the best, source of risk-adjusted returns in the fixed income landscape.

With respect to credit fundamentals, home price appreciation has continued at a very strong pace, but at the same time, home affordability continues to remain robust relative to historical levels of affordability, meaning that the average disposable income is relatively high compared the cost of buying and financing a home. Again, a great underpinning for continued strength in the underlying collateral of the assets we're analyzing.

Second, as the universe of these legacy assets continues to season and the overall credit quality of the residential real estate base continues to improve, we continue to see opportunities for a nimble opportunistic strategy to invest in attractively valued real estate debt securities. The legacy non-agency RMBS market is now roughly \$500 billion in size and, we at Semper think our size allows us to be optimally positioned to take advantage of opportunities in the space. At the same time, in a relatively and increasing trend, new issuance has continued to increase totaling about \$60 billion last year. While still small compared to most markets, extremely meaningful for a firm of our size.

Third, our sectors remain extremely well positioned within the fixed income landscape with respect to rates and price volatility. A large swath of securities in the non-agency RMBS sector and other securitized debt sectors have low interest rate sensitivity, including floating rate and other features limiting effective duration. Volatility continues to be low in many of these sectors and correlations to other fixed income assets and risk assets continues to be low.

January's performance so far continues to support these theses. The combination of the tax reform legislation, some hint of inflation, expectations of tapering by a number of the western central banks and the positive slant to the earnings season has led to rising rate expectations for up to three Fed

tightenings this year. Equities have performed well so far but the treasury curve has risen as we would expect.

The 10 year is up from 2.4% at the end of the month to about 2.65% today. The Bloomberg Barclays Aggregate Index, a proxy for the overall domestic bond market is down 85 basis points to January 23rd. The Bloomberg Barclays MBS index, our funds benchmark index, is down 78 basis points in return month to date, largely driven in mostly by duration or interest rate sensitivity. Counter to that, our fund's institutional class has returned 66 basis points positive during the same time-period.

To summarize our views at the highest level, we believe that the mortgage credit sector continues to offer an extremely advantaged yield profile, lower duration, low correlation to other fixed income assets and low volatility at the sector level. All these continue to make RMBS a great diversifier, a good anchor investment for a short duration strategy and the sector continues to offer the bench for a higher risk-adjusted returns. And now, I'll turn the call over to Tom and talk more specifically about the fund.

Tom Mandel: Thank you. The Total Return Fund is now about four and a half years old and we remain very pleased with performance to date with our current positioning and with our outlook for the fund and for the sectors that we're invested in. We saw continued growth again this past quarter with assets increasing by about \$85 million, ending the year at \$1.15 billion and we continue to estimate that the fund has about \$2 billion of incremental capacity. The fund's primary investment strategy is investing in mortgage securities and we have a target minimum of 80%, and our primary sector concentration, as it has been, is non-agency RMBS.

The final quarter of 2017 was another good one for risk assets overall. We've now seen seven consecutive quarters of essentially declining volatility and appreciating valuations. The Fed raised their target Fed Funds rate again in December, which is the third for the year and, once again, the market took it in stride. The 10-year Treasury rose by about 5 basis points during the quarter ending at 2.40%, as Greg mentioned, which was virtually unchanged for the full year. Meanwhile, the two-year treasury, which is a lot more sensitive to

Fed policy, started the quarter at 1.50% and ended at 1.90%. The 2-10 spread, which was about 120 basis points at the start of the year, ended 2017 at about 50 basis points and today, the spread is a little wider at about 55 basis points with the two year rising 20 basis points month to date and the 10 year rising about 25 basis points month to date.

The Bloomberg Barclays Aggregate Index, which is again the broad measure for the overall domestic investment grade bond market returned 39 basis points for the fourth quarter and 3.54% for the full year. The Bloomberg Barclays MBS Index, which is our fund's benchmark index returned just 15 basis points for the quarter and 2.47% for the full year. Turning to the fund's performance for the fourth quarter of 2017, the institutional class returned 1.05% net, which is an excess return 90 basis points relative to the MBS Index. For the full year of 2017, the institutional class returned 6.19%, an excess return of over 3.5%.

Annualized from inception, which was July 22nd of 2013 through December 31st, 7.15% was the net performance for the institutional class versus the MBS Index return, annualized return of 2.74%, for an excess return of about 4.4% for the year on average. As an aside, I do want to let you know that both Morningstar and Bloomberg were showing, for a brief period, incorrect performance for the month of December and for the full year for our fund. So, if you looked at reporting early in January from those sources, the performance you saw is a little bit different from what I have given you but the fact sheets that have gone out do have the correct information and those services are correct as of now.

The Fund's total return has been positive for the last 22 months at this point, and for 51 of 53 months since inception, which is over 95% of the time, which contrast to the index, which has been positive about two-thirds of the time.

The primary source of positive performance during the fourth quarter and for the full year was interest income, with a contribution of about 5% for the full year. The share price for the institutional share class ended the year at \$10.66, up from \$10.58 at the beginning of the year and unchanged from

September 30th. And then finally, the cumulative monthly dividend for the year was 5.25%.

Next, let me touch on the composition and structure of the Fund. At the end of December, non-agency RMBS totaled 72% of the portfolio, and that consisted of an allocation to prime. So, 10% of the 72% was in prime, 15% in Alt-A, 40% in subprime, 5% in 2.0 and NPL paper, 10% in Option ARMs and 20% in CRT paper. Non-agency CMBS was just 6% of the portfolio of which 2% was in small balance commercial paper; 21% of the Fund was in ABS, including a 7% allocation to single family rental securitizations or SFR; and then about a 1% allocation to cash.

So, there's a few sector data points I'd like to highlight. First of all, RMBS was up for the quarter to 72% from about 68% at the end of September. In particular, our allocation to subprime was up from about 30% of the total RMBS exposure to 40% of the total RMBS exposure. This really consists of two different trades.

The first is the Rep and Warranty settlement trade that we had talked about a couple times last year. We had talked about a JPMorgan \$4.5 billion settlement that was expected early in 2018. So, last year as this settlement had started to crystallize, we had bought senior bonds, which then rose in price as that settlement became more certain. We actually then sold a bunch of those bonds and bought bonds a little bit down in the cap structure, generally in the '80s with an '80s dollar handle that we expected would benefit as the senior bonds were paid down and credit enhancement for the deals increased as a result of these settlements. In fact, the first billion dollars of that settlement is expected today with the rest of it over the next few months.

And then the second set of trade is a little broader. It involves buying subprime bonds generally with a 70s handle, with several sources of upside in our view. Number one is credit upgrades as credit performance continues to improve in the underlying collateral; and refinancing upside as we've continued to see a slow but steady increase in subprime refinancings. And, again, as we buy bonds at a discount and we get paid back at par from these refinancings, that's a very nice upside for performance. We're also buying

these in anticipation of various kinds of cash flow upside. As coupons on the bonds go up, as the Fed tightens, as the coupons of the underlying loans in many cases reset higher over time and other litigation recoveries and so on. And then finally, much of that increase was offset by a decrease in some of what we like to call the next generation bonds: NPL deals, 2.0 deals, being decreased after reaching some of our price targets. So, then these new issue sectors, again, including NPLs, 2.0s, agency credit risk transfer deals, new non-agency origination, single-family rental, that now accounts for close to 30% or about one-third of our non-agency RMBS exposure today. Generally speaking as I've mentioned in the past, these new sectors offer more liquidity, they're actively traded by more dealers, they're often securitized by loans made under strict underwriting standards and they often offer some structural differences when compared to legacy paper. So, this growing universe of bonds continues to give us more tools to make the tactical decisions that we want to make to be able to add value to the portfolio in terms of expected liquidity, rate sensitivity, quality, exposure to real estate credit fundamentals, etc.

And finally, I just want to mention that our cash balance remains low at roughly 1%. So, our comfort in holding less cash comes from the overall improvement that we've continued to see in liquidity for the sectors that we're investing in, in particular, these next generation RMBS.

Our overall tactical strategy remains the same as a quarter ago. With the credit spread compression that we've continued to see and a flattening of the credit curve in the space, we still think it's prudent to, in general, be taking less risk in anticipation of what we hope to be some inevitable weakness and volatility and then opportunities.

We continue to focus on higher-quality cash flows with more liquidity, with less rate sensitivity and we continue to expect a low correlation to other risk assets. But, we've also seen increased opportunities to own bonds with upgrade potential with the upside optionality to Rep and Warranty payments as I talked about a little bit in the subprime space and other opportunities for relative value trades.

We have continued to increase the portfolio's allocation to floating rate securities. It's now at about 70% versus 55% a quarter ago. Some of those floaters, about a third of them actually have some model duration. This is because of structural nuances in the bonds, caps on coupons, modifications of some of the underlying loans, etc. But, importantly, most of these are still trading with no empirical duration and that is what we are very carefully monitoring.

The portfolio's loss adjusted yield for the fund is currently close to 4.75%, which is up from a quarter ago. The dividend for the quarter annualized was approximately 5.5% and that's compared to that 5.25% for the full year.

In terms of duration, we are continuing to keep duration low, which frankly is the primary reason that performance is positive this month along with some nice price appreciation that we've seen in particular bonds and sectors. Duration at the end of September was about 1.9 years. Again, we are still not seeing material interest rate-driven price movements in most of the portfolio. We expect that to persist for some time but, of course, as the treasury curve rises and we think there's a chance that it will continue to rise, although we also expect it's most likely for it to flatten at the same time, we're keeping very careful eye on the duration of those securities. So, in our view this low rate sensitivity that our fund has demonstrated adds overall to the attractive diversification that this non-agency sector provides within a fixed income portfolio.

We think that rates are still low overall and durations are relatively long in most other sectors. So, we think that any rise in rates will have, as we've seen this month, have an increasingly negative impact on much of the bond market and we think the mortgage credit can provide one source of stability while generating current yield.

The average dollar price of the portfolio is about \$90.5, that's down on average about two points from the last quarter. It's down because of the increase in subprime bonds that we have purchased, it is not because of price depreciation. The average price of our legacy RMBS is about \$85 on average and for the next-generation issues, or the newer issues, it's about \$100 on

average. Our CMBS and ABS are close to par, with the exception of the small balance commercial sector, which is trading with an average dollar price of around \$93.

Trading activity continues to run at a higher level as it has over the last few quarters: annualized turnover of around 200%. This has resulted from continued strength in the liquidity of our holdings, continued uncertainty surrounding real estate losses from last year's hurricanes and fires which we find to be an opportunity for us that caused volatility in the CRT sector. In fact, just as an example, last cash flow CRT bonds started last year at around a spread of 300. They tightened by late last summer to around low to mid 200s representing a 6 or 7 point increase or rise in prices. And then following the hurricanes, these bonds as a whole, widened from 75 to 100 basis points, so prices has moved back down 4 or 5 points and now we're even tighter than where they were at the beginning of, or at the middle of last summer where today, this on the run issuance is now at around 180 basis points. Again, about 120 basis points tighter than it was. So, we've seen lots of opportunities to trade bonds and we expect that to continue.

The Fund remains long only with no leverage or hedges in place. We have no plans to change that. We remain very comfortable with the level of credit risk that we're analyzing and taking in the portfolio, which, we believe, is a very important source of the performance that we're generating. We believe today that we have an appropriate amount of liquidity in the portfolio and we remain confident that the limited interest rate risk is going to serve us well this year.

We still have a borrowing facility from U.S. Bancorp, our fund custodian and administrator, which is equal to 20% of assets under management, which we can use only for redemption purposes. This of course, is another strong source of liquidity in addition to our near cash positions.

Looking forward from here, we are increasingly of the view that the legacy and new issue non-agency RMBS are the sectors to be in, in these coming quarters for a whole host of reasons. Greg mentioned that we expect the Fed to continue to increase their target Fed funds rate and we believe that the current consensus for three increases make sense. We also believe that the

Fed will continue their tapering program, which is set to increase a little bit more this quarter. If all goes well, these will be well-balanced, well-anticipated moves that the market takes in stride. We believe that it's fair to say that absent a significant risk-off environment, rates won't go down from here and we believe that owning a portfolio with relatively short duration and a now 70% allocation to floating rate paper will look very good on a relative basis.

With respect to the Fed's tapering plans, there should be an impact to agency MBS over time and we've seen a little bit of that in recent days. But, the Fed does not own non-agencies and the connection between agency paper and non-agency paper remains pretty loose. If agency spreads widen, which we expect, we certainly believe that some of the AAA rated new issue paper, a fairly small piece of the overall non-agency market could widen in tandem, but that's about it for now. Credit quality of homeowners continues to increase at a healthy clip through rising home prices and job creation. Home price appreciation has continued at about a 5% to 6% pace, and this fundamental strength has allowed subprime mortgage refinancings and voluntary prepayments to rise. Again, owning this paper at a discount, it's accretive to performance. And, as Greg mentioned, home affordability continues to be much better than pre-recession levels and better than long-term averages. The enhancements that we're seeing in fundamentals we think can support further price increases in legacy paper, even if we see more rate rises.

And just a point about the new tax legislation, clearly it will be punitive for pockets of the country, but we believe the overall impact will be fairly small to HPA at a national level.

So, we've positioned the portfolio to be the beneficiary of volatility should a risk-off scenario develop. We thought that we'd see some volatility last summer, first with the Wells Fargo call activity that we saw, then with some of the natural disasters that we saw. It really hasn't happened. If a risk-off scenario does develop, however, although we do expect some positive correlation between RMBS and other risk assets, we continue to believe that

our bonds will hold up much better, probably even better than it did back in the first quarter of 2016 the last time we saw a real risk-off trade.

Within mortgage credit, there's a range of spread durations, which is a measure of how much prices will change given the change in credit spreads and we have actively kept ours on the shorter side, so currently around four years.

But to summarize we will continue to position the portfolio with relatively low duration, higher liquidity, limited spread duration with the goal of continuing to target solid multi-returns, which we expect to be largely from interest income, while managing downside volatility and at the same time continuing to buy and trade opportunistically as this market permits. And, we strongly believe that our small size and ability to be nimble is increasingly valuable. While we're slowly and steadily growing, that nimbleness and that advantage is 100% intact. So, we think that the combination of yield, rate and sensitivity and improving credit fundamentals position the Fund well going forward within the universe of bond funds, as well as within the more specific universe of the nontraditional bond funds. And thank you and I'll pass it back to Greg.

Greg Parsons: Great, Tom. Appreciate the overview.

Look, again, we remain very excited about the fund's performance, its growth and its pipeline. We're excited as ever about opportunities we continue to see in the market to drive value from both the legacy and now increasingly new issuance, new opportunities.

I'd like to thank those on the phone who are already investors for your support to date and for those that are new to the platform, we welcome any kind of inbound questions about the platform or the fund. We continue to add content to our mutual fund web site www.semperfunds.com and we invite you to visit. You can also see information about our other mutual fund, the Semper Short Duration Fund, our five-star fund in the Morningstar's ultra short duration universe. If there's anything we can be providing you or telling you, please let us know. We'll now open-up to questions.

Operator: At this time, I would like to remind everyone in order to ask a question, that is “star,” “one” on your telephone keypad. “Star,” “one” to ask a question and we will pause for just a moment to compile the Q&A roster. We do have a question from the line of Heather.

Heather Zumarraga: Hi, can you guys talk a little bit about - is there a mandate in terms of non-agency versus agency within the portfolio? I know you said it's about 42% right now, non-agency. How often does that change? If you said it all ready I apologize if I missed it. And what, if any, is the mandate?

Tom Mandel: Well, there is no mandate. The one mandate we have is that the portfolio will always be at least 80% invested in mortgage securities. And there is no mandate whether that's non-agencies or agencies. At the moment, we have no agency exposure. Everything we own is mortgage credit, and we firmly believe that mortgage credit offers significantly more value with less downside risk than the agency sector, which is characterized currently with relatively low yields, relatively long durations with negative convexity that, of course, can extend those durations as rates are rising and then finally the Fed owns \$2 trillion of this agency paper and we know that as they continue their tapering program, they're going to be buying less of the net supply out there and that should pressure agency spreads, in our opinion. So, we are avoiding them for now.

Operator: We have no further questions at this time.

Greg Parsons: Great. Well, thanks again. We appreciate the support and look forward to speaking next quarter. Have great day.

Operator: This does conclude today's conference call; you may now disconnect.

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