AlphaCentric Premium Opportunity Fund Q3 2020 Commentary

HMXAX | HMXCX | HMXIX

Coming out of a successful quarter like Q1 2020, it would be easy to rest on laurels. Our models worked. Mission accomplished! However, we find that examining our successes is twice as critical as doing so with our mistakes. Because the biggest mistake the smartest guys in the room make, is thinking they're smartest guys and never leaving the room. Years of managing money teaches us to approach everything with a beginner's mind. Humility first. All that said…we are proud of the Fund's performance so far this year. Ante-COVID, if our consistent history of performance didn't already prove we aren't a pony of one trick, our continued steady performance in Q2 should put that to rest. We shifted gears from Q1 and gently continued our ascent as the market ran like a sugar-charged toddler chasing a balloon. And then, September. While for Q3 we ended up 2.1%, the last month of the quarter hit us hard. We stumbled. October continued this poor trend. Not horrifically to be sure. While we are clear with investors that there will be periods of negative performance, no one likes to see them. Our down periods are not long ones historically, but they will happen. Like every other manager, we encourage our investors to look at our performance over a "full-market cycle". Unlike other managers, in our experience a full cycle is eighteen to twenty-four months. As you can see, we are doing well and maintain our significant lead over most asset classes year to date and since inception.

PERFORMANCE

Fund Performance (9/30/20) (Annualized if greater than 1 year)

Share Class/Benchmark	QTD	YTD	1 YR	3 YR	5 YR	Inception*
Class I	2.18	22.85	28.01	11.02	8.47	11.12
S&P 500 TR Index	8.93	5.57	15.15	12.28	14.15	14.17
Morningstar Options-Based Category	3.95	0.36	3.90	2.91	4.26	4.83
Class A	2.14	22.57	27.67	10.53		9.17
Class C	1.93	21.93	26.69	9.92		8.55
S&P 500 TR Index	8.93	5.57	15.15	12.28		13.83
Morningstar Options-Based Category	3.95	0.36	3.90	2.91		4.05
Class A w/ Sales Charge	-3.75	15.51	20.32	8.36		7.57

The maximum sales charge for Class "A" Shares is 5.75%. Performance is historic and does not guarantee future results. Investment return and principal value will fluctuate with changing market conditions so that when redeemed, shares may be worth more or less than their original cost. Total annual operating expenses are 3.19%, 3.94%, and 2.94% for Class A, C and I shares, respectively. Current performance may be lower or higher than the performance data quoted. To obtain the most recent month end performance information or the funds prospectus please call the fund, toll free at 1-844-ACFUNDS (844-223-8637). You can also obtain a prospectus at www.AlphaCentricFunds.com.

	Sep Return	YTD	2011-20 Return	Standard Deviation	Sharpe Ratio	Sortino Ratio	Up Capture	Down Capture	Alpha	High Water	Drawdown Start	Max Drawdown	% Back to High
HMXIX	-3.0%	22.8%	11.1%	8.5%	1.12	2.34	38.1%	0.7%	10.23%	Aug-20	Feb-18	-13.0%	3.1%
MSTR Options	-1.3%	-0.4%	4.8%	7.1%	0.59	0.97	59.6%	60.1%	-2.27%	Aug-20	Jan-20	-13.1%	1.3%
Barclays Agg	-0.1%	6.8%	3.5%	3.0%	0.96	2.27	7.0%	-14.6%	3.75%	Jul-20	May-13	-3.7%	4.8%
Barclay Hedge	-0.7%	1.7%	4.6%	6.2%	0.64	1.05	34.9%	50.0%	-1.20%	Aug-20	Jan-20	-11.9%	0.7%
HFRX: Cmdty	0.6%	1.5%	-1.6%	4.7%	(0.47)	(0.42)	3.5%	25.9%	-3.67%	Sep-11	Aug-11	-19.1%	15.5%
S&P GSCI Gold	-4.2%	21.4%	-0.5%	15.5%	(0.07)	(0.04)	-0.5%	3.4%	-1.71%	Jul-20	Mar-11	-43.4%	4.8%
HFRX: REIT	-2.5%	-10.6%	3.2%	8.9%	0.30	0.46	32.5%	55.5%	-3.47%	Feb-20	Jan-20	-20.8%	13.1%
S&P 500	-3.8%	5.6%	14.2%	13.4%	1.01	1.70	100.0%	100.0%	0.00%	Aug-20	Mar-20	-19.6%	4.0%

Inception: 9/1/11 (Class I) | 9/30/16 (Class A & C)

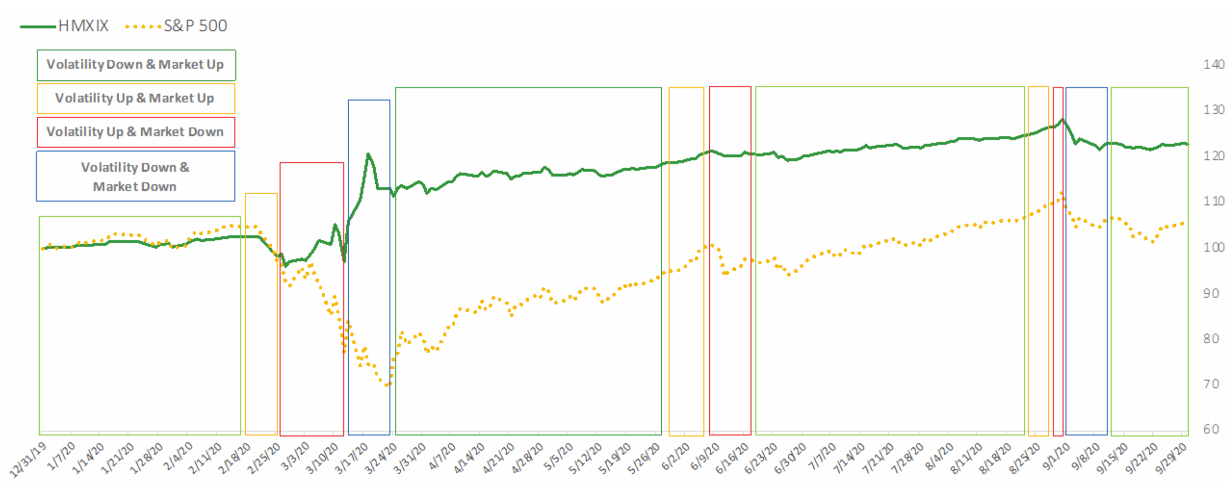
Past performance does not guarantee future results and there is no assurance that the Fund will achieve its investment objective.

REGIME RETROSPECTIVE

Markets rise and volatility tends to be inversely correlated - up when markets are down and vice versa. As with all things, there are always exception and there are periods when this inverse relationship doesn't apply. We use a simple schema of four quadrants describing the different market regimes that matter to a premium harvester.

1. 70% of the time: Markets up and volatility down
2. 20% of the time: Markets down and volatility up
3. 5% of the time: Markets up and volatility up
4. 5% of the time: Markets down and volatility down

These cycle about fairly reliably. But not always. Sometimes skipping over one and directly to the other. In such markets we do less well. Q3 was one of those times. The first two-thirds of Q3 we outperformed nicely, and the last month saw significant swings. Within seven days we experienced a quick shift between three different regimes. The goal of our risk shock absorbers is to attempt to protect us, especially in unprecedented times like these, but sometimes the very mechanisms we use to mitigate risk can cost us. And so it did at the end of Q3.



POSITIVE EXPECTATIONS

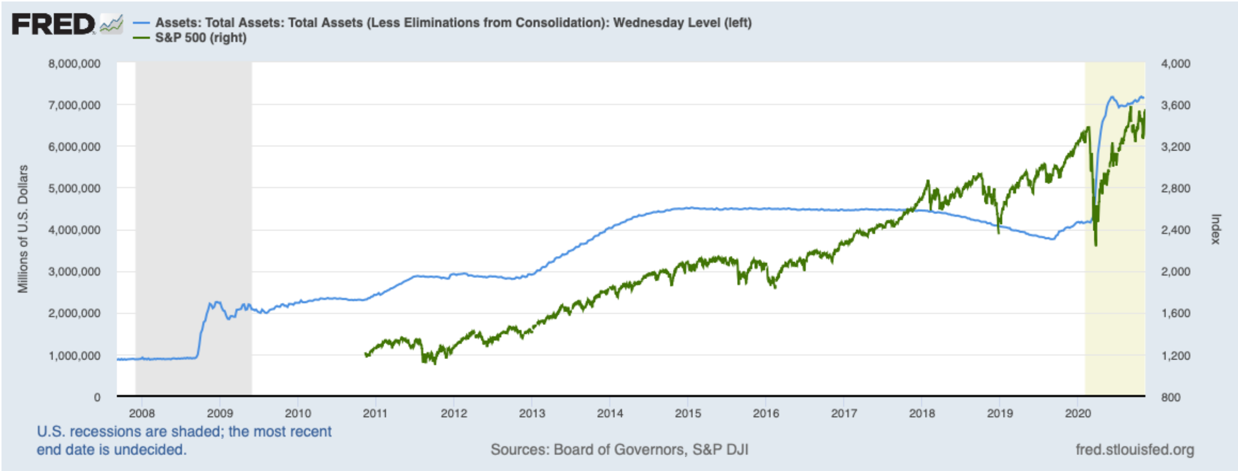
Frequently we are asked if we are a bond replacement? Or, if we're a hedged way to own stocks? We're neither. Volatility as an asset is truly its own thing. Over time, equities increase with the growth of earnings; fixed income investments grow as interest is received and bonds mature. Both of these are, at some level, driven by economic growth and inflation. Going back centuries, which asset class did better varies over long cycles. Both having positive returns. Eventually. Unique to our time - the reality of effectively zero interest rates. Held to maturity, all of a bond's return are in its interest payments to the holder. Net of inflation, we surmise that Treasury returns won't be nearly as robust over the coming years as they were in the past. Most likely net of inflation they will be negative. In fact, we wonder if this may now make bonds an alternative investment?

In the case of most alternatives, we hold that there isn't an inherently positive expected return. Most "alternatives" are really just an illusion of low correlation and a clever way to charge more fees. For the most part, market neutral, trend-following, "arbitrage" and many alternative strategies are really just a leveraged mix of bonds, cash, equities and, to some degree, short-volatility. Once you throw on fees and tax inefficiency and illiquidity, we posit that alternative investment returns – relative to a diversified portfolio of bonds, stocks, cash and premium harvesting – are just an alternative way to lose money. Investors are better off just owning those key components – bonds, stocks and premium harvesting - and rebalancing. Fees are lower; tax efficiency superior; liquidity daily; rebalancing simpler. Below is a risk-to-risk comparison of three different risk-parity portfolios adjusted to the same level as a classic 60/40 portfolio (i.e., 60% stocks and 40% bonds). We are highlighted in green. The one below us allocates to a broad hedge fund index. On a return and risk basis we think the winning combination is pretty clear. The one with us in it. But once you throw on the relative tax efficiencies of our strategy, the liquidity and the positive future expected return, we hope you'll see why we tell investors that we are a core and not a satellite investment

	Sep Return	YTD	2011-20 Return	Standard Deviation	Sharpe Ratio	Sortino Ratio	Up Capture	Down Capture	Alpha	High Water	Drawdown Start	Max Drawdown	% Back to High
SPX/AGG: 60/40	-2.3%	6.4%	9.9%	8.0%	1.16	2.08	59.6%	60.1%	1.44%	Aug-20	Jan-20	-11.6%	2.4%
SPX/AGG/HMXIX: 55/15/35	-3.0%	11.2%	11.8%	8.0%	1.39	2.63	65.2%	57.4%	3.52%	Aug-20	Feb-18	-7.3%	3.1%
SPX/AGG/HFI: 45/15/45	-1.8%	4.2%	8.3%	8.0%	0.96	1.62	54.8%	63.2%	-0.02%	Aug-20	Feb-20	-13.1%	1.9%
S&P 500	-3.8%	5.6%	14.2%	13.4%	1.01	1.70	100.0%	100.0%	0.00%	Aug-20	Jan-20	-19.6%	4.0%

THE "FED PUT"

One of the questions we get from time to time: Why own hedges if the Fed will just ride to the rescue of the markets? A fair point. Perhaps we should go to the Fed's Official Title for guidance. "An Act To provide for the establishment of Federal reserve banks…" Yes, that makes sense. "…[T]o furnish an elastic currency, to afford means of rediscounting commercial paper, to establish a more effective supervision of banking in the United States…" Yes, yes and yes. "[A]nd for other purposes." Hm, that seems fairly broad, right? Perhaps over the years they've sharpened the mandate – honed it, if you will – to a fine point? One would think so, until you get to Section 31. Reservation of right to amend, "The right to amend, alter, or repeal this Act is hereby expressly reserved." Which, you know, when combined with the extremely long official title of the Act, seems like a pretty expansive yet confusing mandate. People have posited the real mandate is to maintain employment. But another, more compelling directive, makes sense to us: The Fed's true mandate is to assure that everyone believes what it does is essential. The money markets are built on faith that they will function. For now, the Fed is the totem of the financial system and it will do whatever is necessary to assure that it is a relevant yet benevolent god, mindful of moral hazard yet not inclined to let great floods consume the world. This includes propping up financial levees by floating its balance sheet like an anti-gravity money machine; which, as you can see from the image below, the FED is very good at doing.



While correlation isn't causation and all that stuff, if, after inflation, risk-free rates are negative - even 30-year treasuries yielding less than the dividend yield of the S&P 500 these days - then you can bet that people will own more stock. Because what else is left? Well, we would argue, us. That is, volatility as an asset class.

For a moment lets step away from our standard deviations and Sharpes and other ratios. Simply stated, what is financial risk? It is not having the money you need when and how you need it. That's it. What are futures and options? They are contracts that guarantee a price to buy or sell a stock (or some other asset) at a certain point in the future. So, in a world with more and more people buying stock, and who need to insure they have money when they need it, and fearful that bonds don't pay enough, and won't necessarily offset tumult as they have in the past, derivatives will be in high demand. And, like any market that insures against risk, the option market will demand a premium to insure. Which is a long and winding way to say, yes, people will still need to buy and sell futures and options. Because who else will insure against the possibility of the Fed's failure to balloon-animal the markets into a bull?

VIX HAPPENS

Sometimes we get questions about the increase in the VIX and the commensurate decrease in VX future volumes. The second point, volumes, is easily explained by notional values. For example, when the VIX future is 10 and trades 1,000,000 contracts a day, the notional amount is $10mm; when the VIX future is 60 and trades 500,000 contracts, the notional amount is $30mm. Volume went down, but the value of contracts went up.

Which speaks to the second point: why do the VIX futures go up so much and so fast but not as much as the VIX spot itself? The best answer is toilet paper. Not actually toilet paper, but the analogy of toilet paper. In the early COVID crisis days, one of the first things to disappear off the shelves and onto eBay at a premium was toilet paper. There are a variety of reasons for this:

1. People worried about the unknowable time they'd be sequestered at home and only knew they'd need at least two things- pasta and toilet paper and beer. Ok, three things.
2. Seeing pictures of empty grocery shelves bare of that two-ply goodness, people, in a fit of anticipatory anxiety, ran out and collectively hoarded Charmin ultra-soft and any other secondary brands they could scrounge.

3. Supply chain. While it is reasonable to assume that the reduction in commercial toilet paper use would balance out the increase in residential wiping, the reality is that there are two different supply chains.

And the same is true for volatility-based products like options and VIX futures in times of crisis. People worry about not being able to sell stock when they need to at the price they want, so they buy options. But there aren't enough counterparties selling options, so the metaphoric shelves empty and, as with toilet paper, people begin bidding up the price of options. Well why can't they just make more options? Because the market makers supply chain is different when demand is low, rather than when it's high. I won't bore you with hypothecation costs, slippage, gamma-risk and a variety of other esoterica. All you need to remember: Volatility is like toilet paper. Like the price of toilet paper when everyone anticipates going to the bathroom at the same time, when market participants believe there is much risk, the price of options can become an order magnitude more expensive.

So how did a lot of hedge funds and prop traders foresee and profit from 2020s blackish swan? Traders make money when volatility happens and when clients trade and pay commissions. Sometimes being big is an edge. This year is a good example. Traders at global prop desks sitting in New York see their colleagues in Hong Kong forced to work from home for a month in January and February. And the New York trader naturally thinks, "Hey, this is maybe more serious than certain people are saying…maybe we should start lightening up on risk, increase volatility premiums (to help clients should they need to sell margined stock and buy puts)." Low and behold, they did. And the VIX did what it did. And all was good in the land of the prop trader and her biggest clients.

DERIVATIVE DIVINATION

How does one become a market wonk? Easy. You think of a long-term investor and then you remove patience and accountability and skin in the game. History-based predictions are a pleasing and safe way for professional prognosticators to predict but not be held accountable. But, because a global pandemic and economic shutdown has never happened before, it is especially hard for financial soothsayers and macro strategists this year. Conundrum: the market-rebound tea leaves indicate a recovery is going to maybe always happen, but what if it doesn't and the prognosticator is wrong? They'll end up being that guy they interview on CNBC with the chyron at the bottom of the screen tarring them forever as "This person who was wrong in 2020". The obvious solution to reputational landmines is the pundit equivalent of Brian Fontana's (Anchorman), "There've been studies you know. 60% of the time it works every time."

This brings us to the election and the polls and the gambling markets that assured us a cut-and-dry result: A definitive Biden win. And…they were wrong. Sort of. Despite exhaustive and sophisticated polling and clever tertiary data points (like calculating the number of a candidate's signs sold on Amazon to specific zip codes), still they misjudged significantly, if not the outcome, the margin of victory. But you know what wasn't wrong? The Volatility markets. They didn't predict a specific outcome, merely that there was much uncertainty. Consequently, insurance against market risk was very costly, and those who took to collecting premium (like us) had a lot of cushion to be wrong and still profit. Only uncertainty is certain, but sometimes the perception of uncertainty is uncertain. Hence, the reality and margin of uncertainty is why a risk premium exists, why strategies like ours will predictably make money over time, and why we have reliably recovered from our periodic negative periods. We believe this one is no different and, as in the past, offers a great opportunity to invest with us.

S&P 500 Index: is considered to be generally representative of the U.S. large capitalization stock market as a whole. Morningstar Options-Based Category funds use options as a significant and consistent part of their overall investment strategy.

VIX: the ticker symbol and the popular name for the Chicago Board Options Exchange's CBOE Volatility Index, a popular measure of the stock market's expectation of volatility based on S&P 500 index options

Sharpe Ratio: measures the performance of an investment compared to a risk-free asset, after adjusting for its risk. It is defined as the difference between the returns of the investment and the risk-free return, divided by the standard deviation of the investment.

Sortino Ratio: measures the risk-adjusted return of an investment asset, portfolio, or strategy. It is a modification of the Sharpe ratio but penalizes only those returns falling below a user-specified target or required rate of return, while the Sharpe ratio penalizes both upside and downside volatility equally.

Standard Deviation: a measure of the amount of variation or dispersion of a set of values. A low standard deviation indicates that the values tend to be close to the mean of the set, while a high standard deviation indicates that the values are spread out over a wider range.

Trading options may introduce asymmetric return properties to an equity investment portfolio. There is no assurance that the Fund will achieve its investment objective. You cannot invest directly in an index. Unmanaged index returns do not reflect fees, expenses or sales charges.

Important Risk Information

Fund Inception: 9/1/2011 (Class I) & 9/30/2016 (Class A & C). The Performance shown before December 31, 2016 is for the Fund's Predecessor Fund (Theta Funds, L.P.) The Fund's management practices, investment goals, policies, objectives, guidelines and restrictions are, in all material respects, equivalent to the predecessor limited partnership. From its inception date, the predecessor limited partnership was not subject to certain investment restrictions, diversification requirements and other restrictions of the 1940 Act of the Code, if they had been applicable, it might have adversely affected its performance. In addition, the predecessor limited partnership was not subject to sales loads that would have adversely affected performance. Performance of the predecessor fund is not an indicator of future results.

The Performance shown before September 30, 2016 is for the Fund's Predecessor Fund (Theta Funds, L.P.) The Fund's management practices, investment goals, policies, objectives, guidelines and restrictions are, in all material respects, equivalent to the predecessor limited partnership. From its inception date, the predecessor limited partnership was not subject to certain investment restrictions, diversification requirements and other restrictions of the 1940 Act of the Code, if they had been applicable, it might have adversely affected its performance. In addition, the predecessor limited partnership was not subject to sales loads that would have adversely affected performance. Performance of the predecessor fund is not an indicator of future results.

Investing in the Fund carries certain risks. The Fund will invest a percentage of its assets in derivatives, such as futures and options contracts. The use of such derivatives and the resulting high portfolio turn-over may expose the Fund to additional risks that it would not be subject to if it invested directly in the securities and commodities underlying those derivatives. The Fund may experience losses that exceed those experienced by funds that do not use futures contracts and options strategies. Investing in commodities markets may subject the Fund to greater volatility than investments in traditional securities. Currency trading risks include market risk, credit risk and country risk. Foreign investing involves risks not typically associated with U.S. investments. Changes in interest rates and the liquidity of certain investments could affect the Fund's overall performance. The Fund is non-diversified and as a result, changes in the value of a single security may have significant effect on the Fund's value. Other risks include U.S. Government securities risks and investments in fixed income securities. Typically, a rise in interest rates causes a decline in the value of fixed income securities or derivatives owned by the Fund. Furthermore, the use of leveraging can magnify the potential for gain or loss and amplify the effects of market volatility on the Fund's share price. The Fund is subject to regulatory change and tax risks; changes to current rules could increase costs associated with an investment in the Fund. These factors may affect the value of your investment.

Investors should carefully consider the investment objectives, risks, charges and expenses of the AlphaCentric Funds. This and other important information about the Fund is contained in the prospectus, which can be obtained by calling 844-ACFUNDS (844-223-8637) or at www.AlphaCentricFunds.com. The prospectus should be read carefully before investing. The AlphaCentric Funds are distributed by Northern Lights Distributors, LLC, member FINRA/SIPC. AlphaCentric Advisors, LLC is not affiliated with Northern Lights Distributors, LLC.

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