# AlphaCentric LifeSci Healthcare Fund
## Quarterly Commentary 2Q2022

LYFIX
LYFAX
LYFCX

*June 30, 2022* — Careful stock selection and active portfolio management enabled the Fund to outperform in 2Q 2022 compared to the primary benchmark, the S&P Biotechnology Select Industry Index. Conviction to average down cost basis in the face of extreme selling and full deployment of all cash reserves near the quarter lows helped enable the ability to participate in the quarter end rally. YTD through 2Q 2022, the Fund produced +24.20% outperformance relative to the primary benchmark.

### Fund Performance as of 6/30/22 *(Annualized if greater than 1 year)*

| *Inception Date: 11/29/19* | QTD | 6 Mos | YTD | 1 Year | 2 Year | Inception |
|---|---|---|---|---|---|---|
| **LYFIX** | -11.85 | -9.42 | -9.42 | -17.11 | 10.31 | 12.99 |
| **LYFAX** | -11.88 | -9.52 | -9.52 | -17.33 | 10.03 | 12.76 |
| **LYFCX** | -12.02 | -9.85 | -9.85 | -17.94 | 9.38 | 12.25 |
| ***S&P Biotechnology Select Industry TR Index*** | *-17.49* | *-33.62* | *-33.62* | *-45.14* | *-18.46* | *-8.40* |
| *S&P 500 Health Care Sector TR Index* | *-5.91* | *-8.33* | *-8.33* | *3.37* | *14.99* | *12.58* |
| **Class A After Sales Charges** | -16.97 | -14.69 | -14.69 | -22.06 | 6.80 | 10.21 |

*The performance data quoted represents past performance, past performance does not guarantee future results, the investment return and principal value of an investment will fluctuate so that when redeemed, it may be worth more or less than their original cost, and current performance may be lower or higher than the performance data quoted. To obtain performance data current to the most recent month-end, please call 844-ACFUNDS (844-223-8637) or at our website www.AlphaCentricFunds.com.*

*The maximum sales charge for Class "A" Shares is 5.75%. The Fund's total operating expenses are 2.77%, 3.52%, and 2.52% for the Class A, C, and I Shares respectively.*

### Market Overview

Despite the quarter end rally, the S&P Biotechnology Select Index ended 2Q 2022 with its worst start to any year ever. The index has fallen for six quarters in a row, tripling the prior record of only two, and remains in the midst of the longest and deepest bear market in its history. Mid-June's low marked a nearly 65% drawdown from the February 2021 index peak. Investors were reminded of the importance of staying invested, however, as the index rallied >15% in the last two weeks of the quarter.

Drug pricing legislation headlines returned with the mid-June FTC workshop on antitrust laws in pharma. Policy analysts noted actual passage of any drug pricing reforms must proceed through the reconciliation process since the Build Back Better legislation has been put on the shelf. Likewise, adoption of material reforms is viewed as unlikely given disagreement on specific policy proposals across key stakeholders and a tight timeline that would be required (note: the reconciliation window closes September 30th, lawmakers only have a few weeks in July, then are out again on recess in August). Clinical and regulatory news headlines were mixed overall during the quarter, with seemingly more setbacks than advances. Updates around major medical meetings such as the American Society of Clinical Oncology (ASCO) meeting or American Association for Cancer Research (AACR) meeting were not enough to rally the sector. Stock moves generally reflected a "glass half empty" perspective with the magnitude of drawdowns significantly exceeding that seen in rallies.

*During 2Q, a record >200 publicly listed biotech companies trading at negative enterprise value were acquired or entered into strategic partnerships that led to >100% rallies.*

Blockbuster M&A news for the biotech sector remained unwritten, but a number of midsize deals continued to get done including Pfizer's (PFE) acquisition of Biohaven Pharmaceuticals (BHVN). The $11.6 billion deal consisted of $148.50 per share of cash consideration plus 0.5 shares of new BHVN which contained several early stage assets that were being spun out. The upfront payment was a ~70% premium to the prior day's close price and ~33% to the 3 month VWAP, but still 3% under the 52 week high. Several analysts commented the deal appeared to be fully valued at just under a 4x revenue multiple on 2025 consensus numbers. BHVN's Nurtec ODT is one of the most successful new drug launches by a SMID-cap biopharma company in the past five years, highlighting the strategic interest for robust revenue streams. The velocity of 'fire sale' strategic deals accelerated materially, highlighting the number of assets that are trading below what acquirers view as fair value. During the quarter, a record >200 publicly listed biotechnology companies were trading at a negative enterprise value (EV = market capitalization net of cash and debt). Several of these negative EV companies were acquired or otherwise entered into strategic partnerships that led to >100% rallies.

### Enterprise Value

Enterprise value (EV) is a measure of a company's total value, often used as a comprehensive alternative to equity market capitalization that includes debt.

EV = Market capitalization + Preferred stock + Outstanding debt + Minority interest – Cash and cash equivalents

Capital markets activity was significantly muted compared to the comparable periods in 2021, with a 60% reduction in Q2 and 73% reduction YTD. Specifically:

| Q2 2022 | Q2 2021 |
|---|---|
| 40 biotech transactions | 64 biotech transactions |
| <$4 billion | >$10 billion |

| 1H 2022 | 1H 2021 |
|---|---|
| 65 biotech transactions | 202 biotech transactions |
| >$7 billion | >$26 billion |

Pressure is mounting on the record number of newly listed biotechs as capital availability tightens. Culling of the biotech herd began in earnest in the quarter with a broad range of strategic decisions being taken, including restructurings, winding down operations and transacting the public shell, and even plans to distribute substantially all operating cash to shareholders. Reduction in the number of listed biotechnology companies and concentration of investor capital on a smaller number of compelling programs should enhance the return profile of the sector moving forward.

Finally, earnings reports from the quarter reminded investors that addressing unmet medical needs is an imperative to creating value for patients. In this context, the contrast between Pfizer's (PFE) COVID-19 vaccine and oral antiviral therapy and Biogen's (BIIB) Alzheimer's drug Aduhelm couldn't be more striking. While the former reiterated total 2022 COVID-19 revenues will exceed $50 billion, the latter announced suspension of commercial efforts and the transition of the CEO following a paltry $2.8 million of Aduhelm revenue in the quarter. Put another way, PFE

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expects to generate more revenue every 30 minutes of 2022 on average from its COVID-19 franchise than BIIB's Aduhelm could muster in the entire first quarter. With hype and momentum now heavily discounted from the sector, public biotech companies will need to deliver on fundamentals to create shareholder value moving forward.

## Fund Overview

The Fund continued to decrease exposure to early stage biotech, especially those with the potential near-term need to raise additional capital. The Fund also minimized exposure to data events with large potential drawdowns given the generally unfavorable reaction of individual stocks to news announcements. Companies with robust revenue and cash flow growth profiles were prioritized. Select 'fallen angel' biotechs that had traded down 50-80+% YTD and a basket of negative EV companies were also added as the selling appeared indiscriminate. The Fund will continue to exercise sell discipline and raise cash when holdings reach fair value and look to opportunistically redeploy proceeds into companies trading below fair value with more attractive risk/reward profiles. Active management of the cash balance provided an additional source of alpha during the quarter.

The Fund continued to benefit from M&A and had exposure to several M&A deals announced during the quarter. Specifically, fund holding Sierra Oncology (SRRA) was acquired by Glaxosmithkline PLC (GSK) for $1.9 billion, a 39% premium to prior close and 63% to the volume-weighted-average-price (VWAP) over 30 days. The transaction was focused on SRRA's myelofibrosis drug momelotinib, which had positive pivotal data from the phase 3 MOMENTUM trial reported earlier in the year. SRRA raised $135 million immediately following the data announcement in January at $27 per share, making the takeout price of $55 per share a 104% premium for the investors who participated in the offering. Analysts viewed the deal as a win-win as investors get to cash out at an estimated peak sales multiple of ~3x prior to approval/launch while GSK achieved strategic synergy and potential accretion in 2024-2025. The Fund also filed in the past on holding Turning Point Therapeutics (TPTX) that was acquired by Bristol Myers Squibb (BMY) for $4 billion. The deal was a 122% premium to the prior close and showed the continued interest of big pharma for differentiated targeted oncology assets. TPTX was recently granted breakthrough therapy designation by FDA for lead drug candidate repotrectinib, a small molecule kinase inhibitor targeting the ROS1 and TRK oncogenic drivers of non-small cell lung cancer and advanced solid tumors. Finally, fund holding Galapagos (GLPG) acquired private companies CellPoint and AboundBio for ~€138MM in cash upfront to expand their pipeline to include next generation cellular and antibody therapies. GLPG is perhaps the poster child of the negative EV companies and has nearly $5 billion in cash to advance development, but surprisingly trades at a negative $1.1 billion EV.

Remarkably, several market makers were reporting the short interest in the SPDR S&P Biotech ETF (XBI, the passive vehicle that tracks the S&P Biotechnology Select Index) was nearly 50% of the float during 2Q. Further, open option interest in XBI as a percentage of shares outstanding exceeded 100%. Several other healthcare stock baskets and ETFs were reportedly under similar pressure, potentially exaggerating stock moves in underlying members. The Fund used the outsized volatility to identify attractive entry points or opportunities to average down cost basis based on fundamentals in hopes of a turnaround. One such example was Adapthealth Corp's (AHCO) May announcement of a new $200 million share buyback, 1Q earnings beat and raise of 2022 guidance. Going into the print, AHCO was down ~50% and has since rallied nearly 60%. Likewise fund holding Cogent Biosciences (COGT) rallied >100% upon announcing new clinical data that led analysts to believe their respective oncology drug offered a clear benefit to patients and will likely be approved. COGT was down ~40% YTD the day before the data was announced, showing that as least in some cases, persistent selling pressure, particularly in smaller caps, can throw out the baby with the bathwater.

### Float

Float is the regular shares a company has issued to the public that are available for investors to trade.

Float = Outstanding shares – Restricted stock

There is an inverse correlation between the size of a company's float and the volatility of the stock's price.

### Top Ten Holdings as of 6/30/22

| Holding | % of Portfolio |
|---|---|
| Cash | 11.96% |
| Aerie Pharmaceuticals Inc | 5.46% |
| Galapagos NV | 5.33% |
| Collegium Pharmaceutical Inc | 3.87% |
| Puma Biotechnology Inc | 3.77% |
| AdaptHealth Corp | 3.59% |
| Agios Pharmaceuticals Inc | 3.43% |
| Takeda Pharmaceutical Co Ltd | 3.15% |
| Bicycle Therapeutics PLC | 3.13% |
| 2seventy bio Inc | 3.11% |

*Holdings are subject to change and should not be considered investment advice.*

### Outlook

The nearly 18-month long pullback and associated volatility have many investors wondering if the life sciences innovator business model is broken. Therapeutics products have traditionally been counter cyclical, especially those addressing critical medical needs with limited alternatives. High margins and regulatory scrutiny of manufacturing processes of complex drug products leads to the majority of these products being produced in developed countries. The supply chains and delivery logistics are generally quite robust and have been largely immune from headwinds facing broader consumer products. Thus, the big picture business prospects continue to look favorable regarding demand, logistics and margins. The outlook for pricing power remains intact as well with limited prospects for material legislative changes in the foreseeable future. Further, virtually no politician is saying that we shouldn't pay for therapies that extend the lives of patients battling cancer or other severe diseases, which are the focus of disruptive innovators on the frontier.

> "If there was ever a time for active biotech fund managers to **differentiate performance through stock selection**, this is it."

With the fundamental picture generally intact, the key question becomes the rate of success of product development. Over the past decade, the average number of novel drug FDA approvals per year is approximately 40 annually. Clearly this is a small fraction compared to the many hundreds of discovery programs being run at biotechnology and pharma companies over that timeframe. The post pandemic financing boom led to the expansion of the number of biotech companies (and discovery programs funded) to levels never before seen, especially those at early stages with high risk profiles. It should be expected many of these companies will burn through all their cash without anything to show for it, but the subset of companies with successful programs have the potential to create non-linear value of patients and shareholders. If there was ever a time for active biotech fund managers to differentiate performance through stock selection, this is it.

The majority of big pharma companies will lose 33-50+% of their 2023 revenue by 2030, making every viable revenue stream in SMID biotech a potential acquisition target at a certain price relative to the underlying growth rate and duration. PFE alone will need to do another ~$40+ billion in deals to meet previously guided revenue targets from external sources. Big pharmas are flush with cash with $100 billion generated from COVID-19 vaccines and therapeutics revenue alone. We continue to expect M&A volume to materially increase in 2022 as depressed valuations entice more deals.

The Fund's fundamental, thesis-driven portfolio is designed to capture alpha even in an environment where the broad sector may be under pressure. We continue to expect fundamentals to play an outsized role in the appreciation of many life sciences companies throughout 2022. Material upside is expected when the balance of sector news turns favorable.

## Important Risk Information

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.

The S&P Biotechnology Select Industry Total Return Index represents the bio-technology sub-industry portion of the S&P Total Markets Index. The S&P 500 Health Care Sector TR Index comprises those companies included in the S&P 500 that are classified as members of the GICS health care sector. You cannot invest directly in an index. Unmanaged index returns do not reflect fees, expenses or sales charges. There is no assurance that the Fund will achieve its investment objective.

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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- 12+ year career as an investor at several specialized $1B+ AUM healthcare funds
- Led Medicinal Chemistry Lab at the Novartis Institutes for BioMedical Research focused on Oncology drug discovery
- Inventor on 8 drug patents
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