

ISC

INTERNATIONAL
SMALL CAP FUND
ISMIX | ISMRX

LMCG
FUNDS



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as of December 31, 2018

International Small Cap Fund Quarterly Commentary

FUND OVERVIEW

The LMC International Small Cap Fund seeks to deliver long-term capital appreciation by capturing the growth potential of international small cap stocks through active management and a bottom-up quantitative approach.

MARKET OVERVIEW

After nine months of low to moderate volatility in 2018, the fourth quarter witnessed material spikes in volatility and an associated decline in asset prices. There were very few places to hide for equity investors as the vast majority of markets tumbled. Larger companies fared better than their smaller brethren, as the S&P 500 declined 13.5% in the quarter and the MSCI EAFE Index retreated 12.54% in the three-month period. US small caps (Russell 2000) declined over 20% while the developed market small caps (MSCI EAFE SC) experienced a 16.05% decline. Emerging markets provided a (relative) safe haven as the MSCI Emerging Markets index posted a 7.47% decline.

There were a number of different cross currents contributing to the equity markets' malaise in the quarter; Fears of a protracted trade war with China - although the two sides agreed to a 90-day truce in early December. Trade wars can obviously impact growth but can also have a related impact on capital expenditures - as companies pause in making major investments when the trade relationships are not clear. Uncertainty regarding Brexit has also come into the headlines again generating a good deal of angst in the UK and European markets. Another contributor to investor concern was the valuation level that many stocks - especially technology stocks had attained in the latter stages of the nine year plus bull market. Many of these technology stocks were among the biggest decliners in the fourth quarter.

Interest rates were somewhat volatile in the quarter. Rates rose in October and fixed income securities sold off somewhat, but rates declined in November and December resulting in a strong posting for the Bloomberg Barclays US Aggregate Index - returning 1.64% in the last three months of the year. In December, the Federal Reserve raised rates for the fourth time in 2018 but reduced the number of projected hikes in 2019 from three to two.

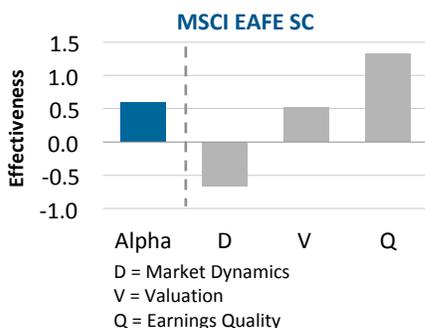
Past performance does not guarantee and is not a reliable indicator of future results. Investment returns and principal values will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. Current performance may be lower or higher than that shown. Call 877-591-4667 for current to most recent month-end performance.

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PERFORMANCE ATTRIBUTION

The LMC International Small Cap Fund declined -15.98% versus -16.05% for the MSCI EAFE Small Cap Index during the fourth quarter and posted a -19.65% return for the year versus -17.89% for the Index. Since its 8/26/2010 inception, the Fund has outperformed the benchmark with an annualized return of 9.29% versus 8.01% for the MSCI EAFE Small Cap Index.

**FIGURE 1:
FACTOR PAYOFFS
FOR THE QUARTER
ENDING 12/31/18
SOURCE: LMC INVESTMENTS**



The LMC International Small Cap Fund modestly outperformed its benchmark for the quarter. The overall stock selection model (Alpha) was slightly positive in the quarter (see Figure 1). *Earnings Quality* was the strongest of the three composite factors and worked particularly well in October and December. *Value* worked on average but was volatile from month to month. It worked very well in October and December but was quite negative in November. *Market Dynamics*, which includes *Earnings Revision*

and *Price Momentum*, was the least effective of the three major factor components and only contributed positively in December.

In October and November, investors embraced risk and higher beta stocks outperformed lower beta stocks. In December there was a dramatic shift away from risk as tariff discussions between the US and China heated back up and worries of a global economic slowdown dampened investor sentiment. Correlations among international small cap stocks spiked during the month and stocks traded more together. Despite this difficult environment where stocks were moving more on macro events than company fundamentals, our process was able to keep pace with its benchmark as all three of our major factor components worked.

Stock selection within countries was slightly positive led by selections in Norway, France and Japan. The worst stock selection was in Germany and Spain. Country allocation was a drag on performance led by underweight positions in New Zealand and Japan. Within sectors, stock selection was positive led by selections in Energy and Financials, which offset negative contributions from Materials and Industrials. Allocation to sectors was also modestly positive led by an underweight position in Energy.

STYLE DISCUSSION

We use a core approach to investing that combines value and growth characteristics. For the last couple of years, this approach has had a difficult time adding value as the performance of the value and growth styles have been extreme and often pulling in different directions. A core approach that has exposure to both styles struggled. For the first six months of 2018, the growth style outperformed with the MSCI EAFE Small Cap Growth Index returning 1.3% and the MSCI EAFE Small Cap Value Index returning -3.9%. Our core style struggled during this time. In the July through December 2018 period, the MSCI EAFE Small Cap Growth Index underperformed, declining 18.6% versus -14.9% for the MSCI EAFE Small Cap Value Index. In terms of our investment process, our *Value* factors also worked better during the latter part of the year but our *Market Dynamics* factors, which include some more growth-oriented characteristics, underperformed and offset positive contributions from *Value* factors resulting in the fund performing roughly in line with the benchmark.

Going into 2019, we are hopeful that developed international markets will outperform US markets and that the extreme performance differences between the Value and Growth

styles will moderate. To evaluate the attractiveness of international small cap stocks versus US small caps, we compared valuation levels using the Price-to-Earnings ratios for the MSCI EAFE Small Cap Index and the Russell 2000 from December 2013–December 2018 (see Figure 2). While international developed market small caps usually trade at a discount to US small caps, the average for the five-year period ending December 2017

**FIGURE 2:
PRICE-TO-EARNINGS
COMPARISON – MSCI EAFE-SC
VS. RUSSELL 2000**

SOURCE: LMCG INVESTMENTS

Month	Price-to-Earnings Ratio		MSCI EAFE-SC PE Discount to Russell 2000
	MSCI EAFE-SC	Russell 2000	
Dec-13	23.3 x	28.8 x	-19%
Dec-14	18.0	27.5	-35%
Dec-15	20.3	25.1	-19%
Dec-16	20.2	28.5	-29%
Dec-17	20.5	32.1	-36%
Oct-18	16.2	31.4	-49%
Nov-18	16.4	29.6	-45%
Dec-18	15.2	25.8	-41%

Discount calculated as (P/E for MSCI EAFE-SC divided by P/E for Russell 2000) - 1.

was approximately 28%. This year, the discount widened and reached 49% by October 2018, the biggest we've seen in recent years. It seems to have bottomed in that month and developed small caps outperformed US small caps in November and December. In addition, during the last two months of the year the performance between the value and growth styles were more similar, which should bode well for the fund if the trend persists going forward.

OUTLOOK

Given the uncertainty related to trade negotiations between the US and China and concerns over global economic growth, we expect equity market volatility to remain elevated in the near term. So far in January, we have seen this to be the case. When markets are jittery, we tend to see investors become more defensive and more risk averse. In the past, we have observed that investors also favor the growth style over value in this environment, as cheapness is perceived as more risky. However, given the declines that we have already seen and the relative attractiveness of international markets, we are hopeful that much of the bad news is priced in and investors will start to look through the macro events and focus on company fundamentals again. As this happens, we would expect the value style to do well. We have designed the fund to combine elements of value and growth so that it can do well in either of these environments as long as neither style is underperforming dramatically. We continue to employ a balanced approach with respect to our major stock selection components: *Value*, *Market Dynamics* and *Quality*. We believe it is important to invest in stocks with good *Valuations* that also have a catalyst such as *Estimate Revision* or *Price Momentum*.

STRATEGY

Our investment philosophy is based on a bottom-up quantitative approach to investing. We believe inefficiencies in the market create opportunities and a quantitative process is well-suited to capture these inefficiencies and outperform. Our stock selection model groups factors into three major categories: *Market Dynamics*, *Value* and *Quality*. Our *Market Dynamic* factors are designed to exploit short-term trends as we believe investors under react in the short term. Our *Value* factors are intended to capture mean reversion as investors tend to overreact in the longer term.

NET PERFORMANCE AS OF 12/31/18	Q4 2018	ONE YEAR	THREE YEAR*	FIVE YEAR*	SINCE INCEPTION**
LMCG INTERNATIONAL SMALL CAP FUND INSTITUTIONAL SHARES (ISMIX)	-15.98%	-19.65%	1.84%	3.78%	9.29%
LMCG INTERNATIONAL SMALL CAP FUND INVESTOR SHARES (ISMRX)	-15.99%	-19.80%	1.61%	3.64%	9.20%
MSCI EAFE SMALL CAP INDEX	-16.05%	-17.89%	3.73%	3.06%	8.01%

+ Annualized. * Inception: 8/26/2010. The Fund has adopted the historical performance of LMCG International Small Cap Collective Fund, a separate collective investment fund of LMCG Collective Trust (the "Predecessor Fund") managed by LMCG Investments, LLC as the result of a reorganization in which the Fund acquired all of the assets, subject to liabilities, of the Predecessor Fund, effective as of the close of business on April 1, 2016. The returns presented for the Fund prior to this date reflect the performance of the Predecessor Fund. The Predecessor Fund commenced operations on August 26, 2010. The Predecessor Fund was not registered as an investment company under the Investment Company Act of 1940, and therefore the Predecessor Fund was not subject to certain investment limitations, diversification requirements, liquidity requirements, and other restrictions imposed by the Investment Company Act of 1940 and the Internal Revenue Code of 1986 which, if applicable, may have adversely affected its performance. The Predecessor Fund had an investment objective and strategies that were, in all material respects, equivalent to those of the Fund.

The Fund's performance for periods prior to the commencement of operations is that of the Predecessor Fund and is based on calculations that are different from the standardized method of calculations adopted by the Securities and Exchange Commission (the "SEC"). The performance of the Predecessor Fund was calculated net of the Predecessor Fund's fees and expenses. The performance of the Predecessor Fund is not the performance information of the Fund, and has not been restated to reflect the fees, estimated expenses and fee waivers and/or expense limitations of the Fund. If the performance of the Predecessor Fund had been restated to reflect the applicable fees and expenses of the Fund, the performance may have been higher or lower than the performance shown.

Performance data provided represents 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 what is stated. For current month-end performance call 1-877-591-4667. See prospectus for other fees and expenses that apply to a continued investment in the Fund. Fees (Institutional Shares ISMIX/Investor Shares ISMRX): Gross Expense Ratio 2.09%/5.02% equal to the Fund's total annual operating expense before reimbursement as set forth in the Fund's most recent prospectus dated August 1, 2018. Net Expense Ratio 0.86%/1.11% reflects the reduction of expenses from fee reimbursements. LMCG Investments, LLC (the "Adviser") has contractually agreed to waive its fee and/or reimburse Fund expenses to limit Total Annual Fund Operating Expenses (Institutional Shares ISMIX/Investor Shares ISMRX) to 0.85%/1.10% through July 31, 2019 ("Expense Cap"), excluding all taxes, interest, portfolio transaction expenses, dividend and interest expenses on short sales, acquired fund fees and expenses, proxy expenses and extraordinary expenses. It is the Adviser's intention to maintain the Expense Cap indefinitely. The Expense Cap may only be raised or eliminated with the consent of the Board of Trustees. Elimination of the Expense Cap at current asset levels will result in higher expenses and lower performance. Performance includes operating expenses and reinvested distributions. Index returns assume reinvestment of all distributions and do not reflect fees or expenses. It is not possible to invest directly in an index. The MSCI EAFE Small Cap Index is a free float-adjusted market capitalization weighted index that is designed to measure developed market equity performance of small cap stocks in European, Australasian and Far Eastern Markets.

IMPORTANT RISKS & INVESTMENT CONSIDERATIONS

Beta Beta represents the systematic risk of a portfolio and measures its sensitivity to a benchmark. A beta of 1 implies that you can expect movement of a manager's return series to match that of the benchmark used to measure beta.

Equity Risk The Fund's equity holdings, including common stocks, may decline in value. The value of a security may decline for a number of reasons, which are detailed in the prospectus.

Foreign & Emerging Markets Investing Risks As a result of political or economic instability in foreign countries, there can be special risks associated with investing in foreign securities, including fluctuations in currency exchange rates, increased price volatility and difficulty obtaining information. In addition, emerging markets may present additional risk due to potential for greater economic and political instability in less developed countries.

Market Events Risk Turbulence in the financial markets and reduced liquidity in equity, credit and fixed-income markets may negatively affect issuers, which could adversely affect the Fund.

Small Cap Risk The Fund's investments in small capitalization companies may be less liquid and their securities' prices may fluctuate more than those of larger, more established companies.

Price to Book Ratio (P/B Ratio) A ratio used to compare a stock's market value to its book value.

Price to Equity Ratio (P/E Ratio) The ratio of a company's share price to its per-share earnings.

Return on Equity (ROE) A measure of profitability that calculates how many dollars of profit a company generates with each dollar of shareholders' equity.

There can be no guarantee that any strategy (risk management or otherwise) will be successful. All investing involves risk, including the potential loss of principal.

Investors should consider the investment objectives, risks, and charges and expenses of the Fund carefully before investing. The prospectus and SAI contain this and other information about the Fund. You may obtain a prospectus and SAI by calling (877) 591-4667. The prospectus should be read carefully before investing.

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