LCM
LEE CAPITAL MANAGEMENT

Lee Adaptive Strategies Update

Monthly Commentary

December 2019

2019: The Year that Wasn't

We can exhale now. The markets had a mishap-free December, with the S&P 500 quietly up a solid 3.02% on a total return basis. That brought the year's return to 31.49%, which is the S&P's best since 2013 and the second-best year since the gravity defying 1990s.

Of course, 2019 followed a down year. The S&P lost -4.38% in 2018, which now seems trivial but at the time felt sobering, if not ominous. We generally try to resist the temptation to impose a narrative on market returns, but much of the 2019 gain occurred in the first few weeks of the year, as if the market was correcting a mistakenly poor end to 2018.

For the two years combined, S&P returns averaged 12.13%. That is a good number. Most investors would be pleased with it as a long term average. But it is hardly glorious. Nor is it high enough to inspire hand-wringing over insupportably high valuations.

For several months now we have been wondering how 2019 will be remembered. We are still not sure. Indeed, we are beginning to question the assumption that 2019 will be remembered at all. It was a year without a defining event. And here in early January 2020, what appears most notable about 2019 is the number of things that failed to happen.

First among the non-developments was the recession that was expected by many in the early months of the year. The Great Yield Curve Inversion of 2019 was accompanied by numerous less definitive signs of impending doom. And while a recession could still appear inside the 18-month yield curve prediction window, current consensus seems to be that the whole thing was a false alarm. So never mind.

Not at all coincidentally, the campaign of continued Fed tightening expected by most of us a year ago did not merely fail to arrive, it was replaced by a round of loosening. Fed fans (they must exist) would argue that the would-be recession was fought off by this "pivot." We are not sure it is quite that simple, and in any case we were never entirely convinced by the recession tea leaves.

The other alleged achievement of the Fed's in 2019 was the avoidance of a crisis in the repo markets. In the end, the fix was as mundane and arcane as the problem itself. The Fed fulfilled its chartered purpose and provided liquidity to the money markets. Then we all went back to not knowing what a repo was.

In the more familiar (to us) equity market, the year saw another round of anxiety about the concentration of attention and value in the FAANG stocks. This seemed like a powder keg ready to go, as an increasingly narrow market became a bubble in five stocks. And then not much of anything happened. FAANG stocks went up. So did the market.

There was more substantive consternation in the thematically related area of unicorn IPOs. Just when we had all become accustomed to high-profile and hip companies such as Uber and Pinterest being permanently private, 2019 saw a wave of much anticipated tech (and tech-ish) IPOs. It did not go well. Uber was floated at about half its expected valuation. And there was the epic failure of WeWork, whose prospective public market valuation was so far below its most recent private one that the deal had to be called off entirely.

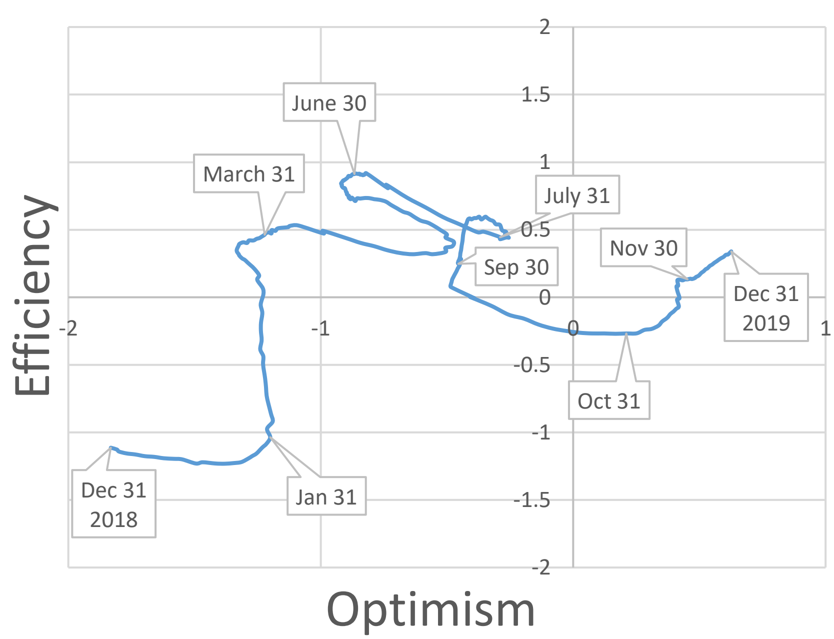
A few months ago in this letter we predicted that the cold water tossed on the private equity markets by the public equity markets could lead to trouble. There is an element of suspension of disbelief in the valuation of many high growth companies and a crisis in private equity could easily have a confidence destroying ripple effect. But we would be the first to admit that there has been nary a sign of that so far.

Internationally, there were more important things that did not happen. Brexit made progress, and there was an increase in political clarity by the end of the year, but the UK still has not left the EU. A formal agreement is expected by the end of this month, but it is essentially an agreement to negotiate another agreement over the following year. In the meantime, economic relations remain as before.

US-China relations generated headlines in 2019. Progress was not obvious. We now seem to be on the verge of a preliminary trade deal, which has been true for some months, if not the entire year. And in China's southeast corner, protests in Hong Kong escalated progressively to an inevitable violent crescendo threatening the entire city, and then dissipated.

In all fairness, most of these things that failed to happen in 2019 could very well happen in 2020 or even in 2021. But they were feared, if not anticipated, in 2019 and they did not occur. And the market went up nicely. Sometimes good news exceeds expectations. And sometimes no news does.

The Market Sentiment Framework



We use our Market Sentiment Framework to adapt the mechanics and weightings of our full quantitative models to changing market conditions. The Sentiment Framework gauges the current state of market psychology on two dimensions. Efficiency measures the crowdedness of the market, the volume of participants seeking investment opportunities. Lower levels of efficiency imply more market mispricing. Optimism measures the willingness of investors to take on risk in exchange for distant and uncertain rewards. Higher levels of optimism imply a better outlook for risky asset classes.

December saw both Efficiency and Optimism continue recent modest increases.

Optimism had a strong spring, a back and forth summer, and then a positive fall and winter. During October it crossed into positive territory for the first time since 2017, and it then added to its gains in the final two months of the year, ending at 0.63.

Although not high in absolute terms, Optimism is far above its levels at the start of 2019, implying a meaningfully rosier outlook, or at a minimum a less pessimistic outlook, than we had a year ago.

Efficiency also rose in December, from 0.13 to 0.34. The past two months have seen an increase in Efficiency, reversing a down trend that covered several months before.

The current positioning of the Sentiment Framework implies a market that is still functioning fairly well but is less efficient than it could be, with moderate opportunities for relative gains from stock picking as well as from momentum. Optimism is at a level that would suggest courage in market exposure.

Performance and Portfolio Positioning as of December 31, 2019:

Lee Adaptive Large Cap Sector (LALCS)

For the month of December 2019, the LALCS composite, on a net of fee basis, was up an estimated +2.75%, behind the S&P 500, which was up +3.02% on a total return basis. The three month return for the LALCS composite, on a net of fee basis, was up an estimated +6.85%, behind the S&P 500, which was up +9.07% on a total return basis.

The strategy began and ended December holding all sectors and did not make any trades.

Lee Adaptive Broad Market Sector (LABMS)

For the month of December 2019, the LABMS composite, on a net of fee basis, was up an estimated +2.75%, behind the Russell 3000, which was up +2.89% on a total return basis. The three month return for the LABMS composite, on a net of fee basis, was up an estimated +7.13%, behind the Russell 3000, which was up +9.10% on a total return basis.

The strategy began and ended December holding all sectors and did not make any trades.

Lee Adaptive Global Equity (LAGES)

For the month of December 2019, the LAGES composite gained +3.45%. This was just behind the MSCI All Country World Index, which gained +3.56% on a total return basis. The three month return for the LAGES composite, on a net of fee basis, was up an estimated +7.63%, behind the MSCI All Country World Index, which was up +9.06% on a total return basis.

The portfolio made no trades during December, holding positions that were approximately 48% US, 7% Japan, 11% Emerging Markets, 22% Europe, and 11% Asia ex-Japan.

Lee Adaptive Global Allocation (LAGAS)

For the month of December 2019, the LAGAS composite, on a net of fee basis, gained an estimated +2.24%, ahead of our blended benchmark, which was up +2.11% on a total return basis. The three month return for the LAGAS composite, on a net of fee basis, was up an estimated +5.31%, behind the blended benchmark, which was up +5.45% on a total return basis.

The strategy remained fully invested during December, making no trades. Fixed income remained somewhat overweighted, at 42%, while US equity was somewhat underweighted at 27%.

Lee Adaptive China (LACS)

For the month of December 2019, the LACS composite, on a net of fee basis, was up an estimated +8.13%. This was behind the MSCI China Index, which was up +8.33% on a total return Net US Dollar basis. For the three month return the LACS composite, on a net of fee basis, was up an estimated +11.77%, behind the MSCI China Index, which was up +14.71 % on a total return Net US Dollar basis.

The portfolio began and ended the month fully invested in equity. It started December holding 50% in KBA, the broad market A Shares ETF, 25% in TAO, the real estate ETF, and 25% in OBOR, the transportation infrastructure ETF. Near the end of the month, on December 27th, it sold TAO and replaced it with KURE, the healthcare ETF.

Definitions:

Lee Adaptive Large Cap Sector Composite ("LALCS Composite"). A capital weighted performance composite of an investment strategy known as the Lee Adaptive Large Cap Sector strategy (the "LALCS Strategy") that holds some combination of the U.S. large cap sector ETFs and/or cash, as determined by a proprietary quantitative model. The LALCS Composite performance is based on actual trading profits/losses/expenses net of a management fee of 0.50%. Actual expenses of operating the LALCS Strategy may vary, depending on the investment structure in which the Strategy is used, which could result in lower returns than those stated for the LALCS Composite. Such expenses may detract materially from the performance of the LALCS Strategy and, consequently, the results shown above may not be fully indicative of the actual performance results of the LALCS Strategy.

THE LALCS COMPOSITE IS BEING SHOWN FOR ILLUSTRATION PURPOSES ONLY AND SHOULD NOT BE RELIED UPON. NO REPRESENTATION OR ASSURANCE IS MADE THAT ANY INVESTOR WILL OR IS LIKELY TO ACHIEVE RESULTS COMPARABLE TO THOSE SHOWN ABOVE OR WILL MAKE ANY PROFIT OR WILL BE ABLE TO AVOID INCURRING SUBSTANTIAL LOSSES.
PAST PERFORMANCE OF THE STRATEGY AND THE LALCS COMPOSITE ARE NOT INDICATIVE, OR A GUARANTEE, OF FUTURE RESULTS. IT SHOULD NOT BE EXPECTED THAT THE LALCS STRATEGY'S ACTUAL RETURNS WILL REPLICATE THE RETURNS SHOWN IN THE PERFORMANCE MODEL.

Lee Adaptive Broad Market Composite ("LABMS Composite"). A capital weighted performance composite of an investment strategy known as the Lee Adaptive Broad Market Strategy (the "LABMS Strategy") that holds some combination of the U.S. large cap sector ETFs, a small cap ETF and/or cash, as determined by a proprietary quantitative model. The LABMS Composite performance is based on actual trading profits/losses/expenses net of a management fee of 0.50%. Actual expenses of operating the LABMS Strategy may vary, depending on the investment structure in which the Strategy is used, which could result in lower returns than those stated for the LAUSE Composite. Such expenses may detract materially from the performance of the LABMS Strategy and, consequently, the results shown above may not be fully indicative of the actual performance results of the LABMS Strategy.

THE LABMS COMPOSITE IS BEING SHOWN FOR ILLUSTRATION PURPOSES ONLY AND SHOULD NOT BE RELIED UPON. NO REPRESENTATION OR ASSURANCE IS MADE THAT ANY INVESTOR WILL OR IS LIKELY TO ACHIEVE RESULTS COMPARABLE TO THOSE SHOWN ABOVE OR WILL MAKE ANY PROFIT OR WILL BE ABLE TO AVOID INCURRING SUBSTANTIAL LOSSES.
PAST PERFORMANCE OF THE STRATEGY AND THE LABMS COMPOSITE ARE NOT INDICATIVE, OR A GUARANTEE, OF FUTURE RESULTS. IT SHOULD NOT BE EXPECTED THAT THE LABMS STRATEGY'S ACTUAL RETURNS WILL REPLICATE THE RETURNS SHOWN IN THE PERFORMANCE MODEL.

Lee Adaptive Global Equity Composite ("LAGE Composite") Performance. A capital weighted performance composite of the of an investment strategy known as the Lee Adaptive Global Equity strategy (the "LAGE Strategy"). The LAGE Strategy is currently offered by LCM to certain qualified investors through certain accounts managed by LCM on a discretionary basis ("LAGE Managed Accounts"). The LAGE Managed Accounts use the same investment program as the LAGE Strategy. The LAGE Composite performance is based on actual trading profits/losses/expenses net of a management fee of 0.50%. Actual expenses of operating the LAGE Strategy may vary, depending on the investment structure in which the LAGE Strategy is used, which could result in lower returns than those stated for the LAGE Composite. Such expenses may detract materially from the performance of the LAGE Strategy and, consequently, the results shown above may not be fully indicative of the actual performance results of the LAGE Strategy.

THE LAGE COMPOSITE IS BEING SHOWN FOR ILLUSTRATION PURPOSES ONLY AND SHOULD NOT BE RELIED UPON. NO REPRESENTATION OR ASSURANCE IS MADE THAT ANY INVESTOR WILL OR IS LIKELY TO ACHIEVE RESULTS COMPARABLE TO THOSE SHOWN ABOVE OR WILL MAKE ANY PROFIT OR WILL BE ABLE TO AVOID INCURRING SUBSTANTIAL LOSSES.
PAST PERFORMANCE OF THE LAGE STRATEGY AND THE LAGE COMPOSITE ARE NOT INDICATIVE, OR A GUARANTEE, OF FUTURE RESULTS. IT SHOULD NOT BE EXPECTED THAT THE LAGE STRATEGY'S ACTUAL RETURNS WILL REPLICATE THE RETURNS SHOWN IN THE PERFORMANCE MODEL.

Lee Adaptive Global Allocation ("LAGA Composite"). A capital weighted performance composite of the of an investment strategy known as the Lee Adaptive Global Equity strategy (the "LAGA Strategy"). The LAGA Strategy is currently offered by LCM to certain qualified investors through certain accounts managed by LCM on a discretionary basis ("LAGA Managed Accounts"). The LAGA Managed Accounts use the same investment program as the LAGA Strategy. The LAGA Composite performance is based on actual trading profits/losses/expenses net of a management fee of 0.50%. Actual expenses of operating the LAGA Strategy may vary, depending on the investment structure in which the LAGA Strategy is used, which could result in lower returns than those stated for the LAGA Composite. Such expenses may detract materially from the performance of the LAGA Strategy and, consequently, the results shown above may not be fully indicative of the actual performance results of the LAGA Strategy.

THE LAGA COMPOSITE IS BEING SHOWN FOR ILLUSTRATION PURPOSES ONLY AND SHOULD NOT BE RELIED UPON. NO REPRESENTATION OR ASSURANCE IS MADE THAT ANY INVESTOR WILL OR IS LIKELY TO ACHIEVE RESULTS COMPARABLE TO THOSE SHOWN ABOVE OR WILL MAKE ANY PROFIT OR WILL BE ABLE TO AVOID INCURRING SUBSTANTIAL LOSSES.
PAST PERFORMANCE OF THE LAGA STRATEGY AND THE LAGA COMPOSITE ARE NOT INDICATIVE, OR A GUARANTEE, OF FUTURE RESULTS. IT SHOULD NOT BE EXPECTED THAT THE LAGA STRATEGY'S ACTUAL RETURNS WILL REPLICATE THE RETURNS SHOWN IN THE PERFORMANCE MODEL.

Lee Adaptive China Equity Composite ("LACS Composite") Performance. A capital weighted performance composite of the of an investment strategy known as the Lee Adaptive China strategy (the "LACS Strategy"). The LACS Strategy is currently offered by LCM to certain qualified investors through certain accounts managed by LCM on a discretionary basis ("LACS Managed Accounts"). The LACS Managed Accounts use the same investment program as the LACS Strategy. The Composite performance is based on actual trading profits/losses/expenses net of a management fee of 0.35%. Actual expenses of operating the LACS Strategy may vary, depending on the investment structure in which the LACS Strategy is used, which could result in lower returns than those stated for the LACS Composite. Such expenses may detract materially from the performance of the LACS Strategy and, consequently, the results shown above may not be fully indicative of the actual performance results of the LACS Strategy.

THE LACS COMPOSITE IS BEING SHOWN FOR ILLUSTRATION PURPOSES ONLY AND SHOULD NOT BE RELIED UPON. NO REPRESENTATION OR ASSURANCE IS MADE THAT ANY INVESTOR WILL OR IS LIKELY TO ACHIEVE RESULTS COMPARABLE TO THOSE SHOWN ABOVE OR WILL MAKE ANY PROFIT OR WILL BE ABLE TO AVOID INCURRING SUBSTANTIAL LOSSES.
PAST PERFORMANCE OF THE LACS STRATEGY AND THE LACS COMPOSITE ARE NOT INDICATIVE, OR A GUARANTEE, OF FUTURE RESULTS. IT SHOULD NOT BE EXPECTED THAT THE LACS STRATEGY'S ACTUAL RETURNS WILL REPLICATE THE RETURNS SHOWN IN THE PERFORMANCE MODEL.

S&P 500 Total Returns Index. The returns for the S&P 500 index on a total return basis, that is, with dividends included and does not reflect the deduction of fees and expenses. You cannot invest directly in this index. The returns for the S&P 500 Index are provided for comparison purposes only to show how the LALCS Composite compares to a broad-based index of securities. The S&P 500 is comprised of a representative sample of 500 large-cap companies. The index is an unmanaged, float-weighted index with each stock's weight in the index in proportion to its float, as determined by Standard & Poors. The index is one of the most widely used benchmarks of U.S. equity performance. The index is not subject to any of the fees or expenses to which the LALCS Composite is subject. It is not possible to invest in this index. The index is used for comparison purposes only. It should not be assumed that the LALCS Strategy will invest in any specific securities that comprise the index or that the investment program of the LALCS Strategy will track the index. Consequently, the returns of the LALCS Composite may or may not be highly correlated with those of the index.

Russell 3000 Index. The Russell 3000 Index is a market-capitalization-weighted equity index maintained by FTSE Russell that seeks to be a benchmark of the entire U.S. stock market. It measures the performance of the 3,000 largest publicly held companies incorporated in America as measured by total market capitalization and represents approximately 98% of the American public equity market. The returns for the Russell 3000 index are provided for comparison purposes only to show how the LABMS Composite compares to a broad-based index of securities. The index is not subject to any of the fees or expenses to which the LABMS Composite is subject. It is not possible to invest in this index. It should not be assumed that the LABMS Strategy will invest in any specific securities that comprise the index or that the investment program of the LABMS Strategy will track the index. Consequently, the returns of the LABMS Composite may or may not be highly correlated with those of the index.

MSCI All Country World Index. The returns for the MSCI All Country World Index ("ACWI") on a total return basis, that is, with dividends included and does not reflect the deduction of fees and expenses. The returns for the index are provided for comparison purposes only to show how the above composite returns compare to a broad-based index of securities. The MSCI AC World Index is composed of large and mid-capitalization developed and emerging market equities. The index is one of the most widely used benchmarks for global equity performance. You cannot invest directly in this index. It should not be assumed that the strategies above will invest in any specific securities that comprise the index or that the investment program of the strategies above will track the index. Consequently, the returns of the composites above may or may not be highly correlated with those of the index.

MSCI China Index Net. The returns for the MSCI China Index Net on a total return basis, that is, with net dividend tax withholding and does not reflect the deduction of fees and expenses. The returns for the index are provided for comparison purposes only to show how the above composite returns compare to a broad-based index of securities. The MSCI China Index represents large and mid-capitalization across H shares, B shares, Red chips, P chips and foreign listings (e.g. ADRs). With 495 constituents, the index covers about 85% of this China equity universe. Currently, the index also includes Large Cap A shares represented at 5% of their free float adjusted market capitalization**.** It should not be assumed that the LACS strategy will invest in any specific securities that comprise the index or that the investment program of the LACS strategy will track the index. Consequently, the returns of the composite above may or may not be highly correlated with those of the index.

Bloomberg Barclays US Aggregate Bond Index. The returns for the Bloomberg Barclays US Aggregate Bond Index ("US Agg") on a total return basis, that is, with dividends included and does not reflect the deduction of fees and expenses. The returns for the index are provided for comparison purposes only to show how the above composite returns compare to a broad-based index of securities. The US Agg is a broad-based flagship benchmark that measures the investment grade, US dollar-denominated, fixed-rate taxable bond market. The US Agg index includes Treasuries, government-related and corporate securities, MBS (agency fixed-rate and hybrid ARM pass-throughs), ABS and CMBS (agency and non-agency). The index is one of the most widely used benchmarks for fixed income performance. You cannot invest directly in this index. It should not be assumed that the strategies above will invest in any specific securities that comprise the index or that the investment program of the strategies above will track the index. Consequently, the returns of the composites above may or may not be highly correlated with those of the index.

Blended Benchmark. Is a hypothetical index comprised of 60% MSCI AC World Index and 40% the Bloomberg BarCap US Aggregate Bond Index. You cannot invest directly in this index.

Disclaimer:

PAST PERFORMANCE IS NO GUARANTEE OF FUTURE RESULTS OR PROFITABILITY.

This document ("Update") does not constitute an offer to sell or a solicitation of an offer to purchase interests in any investment vehicles or securities. This Update is not, and under no circumstances is it to be construed as, a prospectus, advertisement or an offering of any interests in either the Strategy or other portfolios. This Update is intended for informational purposes only. It does not constitute investment advice or a recommendation with respect to investment in the LALCS Composite, LABMS Composite, LAGA Composite, LAGE Composite, LACS Composite, the LALCS Strategy, the LAGA Strategy, the LAGE Strategy, the LABMS Strategy, the LACS Strategy or any other portfolio.

Lee Capital Management LP ("LCM") has relied upon and assumed in the LALCS Strategy, the LAGA Strategy, the LAGE Strategy, the LABMS Strategy and the LACS, without independent verification, the accuracy and completeness of all information available from public sources. No assurance can be given that an investor will receive a return of all or a part of his or her initial investment, and investment results may vary substantially over any given time period. An investment is not a deposit and is not insured or guaranteed by the FDIC or any other government agency or by LCM, its affiliates or subsidiaries.

This Update and the material contained herein are confidential and may not be distributed in whole or in part to anyone other than the intended recipients. By accepting receipt of this Update, the recipient will be deemed to represent that they possess, either individually or through their advisers, sufficient investment expertise to understand the risks involved in any purchase or sale of any financial instruments discussed herein. Lee Capital Management makes no determination as to the suitability of any strategy for any investor. Unauthorized reproduction or distribution of all or any of this material or the information contained herein is strictly prohibited.