



VICE FUND

Long Term Trends in the Vice Fund

July 2018

The Vice Fund (VICEX) has a 16-year history of investing in Alcohol, Tobacco, Gaming, and Aerospace Defense. We believe that the long-term opportunities that our sectors have before them are compelling. We elaborate on the trends in each sector below.

Alcohol

- Urbanization in Emerging Markets – We believe growing urbanization generally benefits beer makers in emerging markets. Urban consumers have higher incomes and more access to products. With 50% of the emerging market populations in cities currently, there is significant potential for continued growth in these areas. Emerging market urbanization was estimated to be 40% in 2000 and is expected to be 60% by 2030.
- Increasing Middle Class Spending in Emerging Markets – Middle-class spending growth is particularly prevalent in China and India where marginal gains translate into significant opportunities for companies that deliver desirable or aspirational brands. China's middle-class total spending is projecting to be greater than the U.S. in 2020 and India is expected to pass the U.S. by 2030. The result for alcohol companies can be seen in China, where Johnnie Walker and Chivas sales (among others) continue to expand supporting Diageo and Pernod Ricard.
- Maturing Millennials Preferences – Millennials are the largest consumer group domestically. They are larger than the baby boomers, and they are earning more than they ever have as they cross into their 30's. Millennials like wine and the renaissance in craft cocktails, and as they mature millennials are consuming more spirits. Companies like Constellation, Brown Forman, and Diageo have all benefited from this trend.

Aerospace Defense

- Domestic Defense Spending – The U.S. has begun the long-term spending to maintain battlefield superiority and allow U.S. fighting forces to complete the missions we ask them to perform. In 2017, President Trump proposed a 10% increase in defense spending, and Congress approved an 18% increase. These budgets fund long-term projects that should support our defense companies long-term cash flow predictability.
- Cyber Warfare – Major contractors are rapidly expanding the cyber warfare capabilities of the military, as that is where the modern "cold war" is fought. The cyber defense budget has expanded 31% in the past two years, and this spending should continue.
- International Defense Spending – In 2014, NATO reiterated its commitment to spending 2% of GDP. At the time, only three countries hit that target (outside of the US). This year, eight are expected to hit the 2% target. By 2024, 15 nations should reach the 2% of GDP level. This offers opportunities for defense makers overseas as well as new markets for domestic defense contractors to participate in.

Gaming

- Macau – The growth of gaming in Chinese Macau is a well-known story, blending with the overall economic growth of China. When China modified gaming in Macau to its current form in February 2002, the market was an underdeveloped opportunity generating \$2.2 USD in revenue per year. Last year, Macau produced \$33.1 billion in gaming revenue. With more visitors each year and additional casinos opening, the trend appears set to continue.
- Domestic Sports Betting – The recent ruling by the Supreme Court in the case of NCAA v Christie has opened the door to domestic sports betting. This offers another opportunity for casinos to grow significantly. If we compare the populations and GDP of the U.S. and the U.K., we would estimate the opportunity in sports betting could be as high as \$50 billion in revenue. While not every state will approve betting, this gives us an idea of the opportunity for casinos.
- Japan – The government of Japan has recently approved Casino Gambling. The opportunity for international casinos to partner with Japanese business interests to create Las Vegas style casino resorts in Japan would be significant with estimates ranging from \$10 billion to \$28 billion in revenue.

Tobacco

- Cash Cows – Tobacco is a cash cow with big names like Phillip Morris and Altria paying 5%+ dividends. There has been little that has changed the overall trend in diminishing smoker numbers in the past decades. However, most investors are surprised to learn that the highest smoking rate is among Millennials. This would indicate that tobacco is not going away any time soon.
- Heat Not Burn E-Cigarettes – These new products have gained significant traction in Japan and South Korea where Phillip Morris, British American Tobacco, Japan Tobacco, and KT&G have been unable to keep up with demand. These products deal with the dangers of smoking directly (short of quitting). It is proving a success overseas.
- Marijuana – Cannabis offers a unique opportunity for Tobacco companies. These companies have experience operating under significant restrictions on distribution, excise taxes, and marketing restrictions as well as doing so in a profitable manner. It is our belief that when cannabis is legalized at the federal level, tobacco will be well positioned to move into this market and use enormous economies of scale to set the market for cannabis.

Cannabis

A final word on one more trend that we are investing in. Given the long-term trends towards legalization of recreational and medical marijuana domestically and in the western world, we have decided to start building positions in companies operating where cannabis is legal. Right now, this investment is small and limited to Canada, which is projecting to be a \$7 billion market by 2021. However, we will continue to build these positions, and we are keeping a close eye on legalization in other markets. We have focused our investments on companies with international reach and established relationships outside of Canada. The key for us is identifying the companies that we think can compete on the global stage as new markets open.

We feel that the long-term trends in the Vice Fund are compelling and offer investors a unique opportunity for entry into companies who benefit from global trends in growth.

If you would like to know more about how we invest or have additional questions about the Vice Fund or USA Mutuals, please contact us at 1.800.MUTUALS, email at FA.sales@usamutuals.com or visit us at www.usamutuals.com.

Disclaimers

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The above includes discussion about the estimated growth of certain sectors. It is impossible to predict future growth and actual results may vary. The potential growth or decline of any sector does not represent the performance of the Fund. Each of these sectors has its own set of investment characteristics and risks that may differ from actual investments and investors should consider these risks carefully prior to making any investment decisions.

Mutual fund investing involves risk; principal loss is possible. The Fund will concentrate its net assets in industries that have significant barriers to entry including the alcoholic beverages, tobacco, gaming and defense/aerospace industries, the Fund may be subject to the risks affecting those industries, including the risk that the securities of companies within those industries will underperform due to adverse economic conditions, regulatory or legislative changes or increased competition affecting those industries, more than would a fund that invests in a wide variety of industries. The Fund invests in foreign securities which involve greater volatility and political, economic and currency risks and differences in accounting methods. The Fund invests in smaller companies, which involve additional risks, such as limited liquidity and greater volatility. Derivatives may involve certain costs and risks such as liquidity, interest rate, market, credit, management and the risk that a position could not be closed when most advantageous. Investing in derivatives could result in losing more than the amount invested. If a security sold short increases in price, the Fund may have to cover its short position at a higher price than the short sale price, resulting in a loss.

Investors should consider the investment objectives, risks, charges and expenses of the Vice Fund. Read the prospectus carefully before investing.

For USA Mutuals Vice Fund holdings information click [here](#).

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