TwentyFour
a boutique of Vontobel

Fund Commentary | 28 February 2023

# MI TwentyFour Investment Funds – Monument Bond Fund

**This Commentary is a marketing communication for professional UK investors only**

## Market Commentary

After a strong rally in most parts of financial markets in January, February marked a return to negative investor sentiment. Renewed inflation fears and a strong labour market in the US lowered the likelihood of a dovish pivot by the Federal Reserve this year.

The month started with markets on a firm footing, helped by the Federal Open Market Committee (FOMC), who hiked interest rates by 25bps as expected. The subsequent press conference from Jerome Powell was seen as more dovish than anticipated, which caused 10yr Treasury yields to drop below 3.4%. However, the non-farm payrolls (NFPs) report changed the tone entirely, with over 500k new jobs created, compared to an expectation of less than 200k. Moreover, the unemployment rate fell to just 3.4%, which was a 53 year low. With the US economy seemingly firing on all cylinders, investors began to debate whether the Fed would ultimately hike above their 5-5.25% median dot plot, while at the same time, discounted the likelihood of interest rate cuts in 2023. As a result, 10yr Treasury yields increased by 25bps in short order. With ISM services and consumer confidence data also coming in better than expected, the mid-month inflation data was keenly anticipated by investors. Ultimately, the month-on-month Consumer Price Index (CPI) data increased from 0.1% to 0.5% and year-on-year CPI fell less than expected to 6.4%, which made it clear that the battle with inflation was not over.

After a quiet start to the year from ABS issuers in mainland Europe, February saw a material change relative to the UK. Overall demand for ABS products remained strong throughout the month and spreads remained resilient in the face of continued widening pressure in broader risk markets and renewed interest rate volatility. The UK saw another Prime RMBS deal from Santander's Holmes Master trust issuer platform. This was well received by the market at a final spread of Sonia +58, for a slightly longer deal, which was ultimately upsized to £750mm due to strong demand. The only other deal from the UK was a legacy non-conforming offering, which was a packaged deal originally from Kensington's more complex credit portfolio. Pricing on this deal was understandably wider, reflecting the nature of the collateral, but illustrative of investor sentiment in challenging markets.

New issue from the continent had a very diverse flavour both geographically and by sector. Auto deals accounted for a large part of the volume, with deals from VW and BMW Germany being the notable prints, offering mainly AAA tranches, both of which were heavily oversubscribed and upsized. Toyota Italy priced a very successful inaugural Hybrid/EV only deal and two further mixed collateral auto deals away from non-captive Prime issuers were also well received. The healthy auto supply volume has helped take STS issuance to over €7bn which is a lot higher than levels seen last year for the same period.

Away from the auto sector there was a credit card issuer from a large French bank and a German consumer loan deal via a leading digital lending platform, doing their third deal. Residential mortgage deals from Europe remained very light with just one established Dutch repeat BTL issuer pricing, which also offered some welcome mezzanine bonds. Also from the Netherlands, a new Green Storm Prime deal from Obvion was announced at the end of the month, which, being the most liquid shelf in the ABS market, will undoubtedly see strong demand.

After a challenging few months, February proved to be very favourable for CLO managers looking to price primary deals. The market saw ten new deals for a notional €4bn in issuance, which was the highest since March 2022, as the overall cost of funding dipped to an eight-month low. This was further aided by the rumoured return of large Japanese anchor investors in AAA tranches. During February the ABS market also saw Blackstone defaulting on a single loan Finnish office within a CMBS transaction after it failed to get bond holder approval for a maturity extension. While our Funds don't have exposure to this transaction, and the income from tenants is enough to service the debt, and the LTV on the mortgage is low, we will be following the process closely. The portfolio managers have been cautious on CMBS for some time and, after a full sector review, sold various deals in the second half of last year. Overall issuance volume for the month was a healthy €10bn including CLOs.

The tone in secondary markets was by and large more subdued over the month which is typical for ABS markets during periods of elevated primary issuance. It was also understandable given the relentless tightening seen in the market during January. The month can be characterised by a further leg tighter in spreads for the first half of February across selective sectors and tranches, followed by a few basis points of widening into the latter part of the month. This was despite the very strong supply/demand technical in Primary which is where the focus was. Spreads in senior UK Prime, BTL and N/C remain around 20bps tighter across the board and spreads are generally back to levels last seen in June 2022. AAA BTL for example is now trading comfortably around S+90-100 pulling European names with them. The auto and consumer sectors in Europe tightened rapidly month on month as primary prints propelled spreads materially tighter in the AAA sector. Mezzanine bonds remain in strong demand across the capital stack, a reflection really of smaller supply on tranche size. On the CLO side, AAA levels were broadly flat over the month with lower investment grade finishing a touch wider in BBB. BB and B remained well bid over the month as levels tightened by 25-50bps and 50-75bps respectively, although it should be noted there remains a level of dispersion between manager tier and performance.

## Portfolio Commentary

The Fund saw another good performance in February as spreads continued to rally in the ABS market. The portfolio managers were active again in the primary market as deal issuance volume increased from European based originators. The portfolio managers took advantage of the healthy new issue premium offered and further improved the liquidity profile of the Fund and added a mix of UK Prime RMBS, various Prime Auto AAAs and AAA bonds from a non-prime lender. AAA CLOs continue to offer good relative value and the Fund added new positions from preferred managers at spreads of around Eur +175/185bps. Also, in primary CLOs the Fund added BBB tranches in primary at a spread above 600bps, which represents a good pick up versus tighter secondary BBB CLO and offering an all-in yield of circa 10%. Additionally, a number of relative value trades in various sectors were executed during the month and the Fund clipped some profits on primary issuance from earlier in the year. Fundamental bond performance remains good with rating upgrades seen over the month, and the portfolio managers will continue to maintain high levels of due diligence on the underlying portfolio.

## Market Outlook and Strategy

Overall, the Primary market in February was Auto ABS and CLO focussed, except for a large UK Prime deal. What is notable is that all of these deals have seen healthy levels of oversubscription from ABS investors and have added some welcome diversification for the market. This has helped to underpin the rally seen in spreads since the start of the year despite a weakening in wider credit markets following the markets re-assessment of where terminal rates might end up in this cycle due to a re-acceleration in core inflation.

Performance in ABS and CLO markets continue to be robust and house price indices are finally beginning to show a slow-down in the UK, but interestingly the Dutch market increased by 1.5% in January after falling consecutively for a few months. Rating agency actions continue to be skewed towards upgrades and the portfolio managers continue to monitor deal performance on a deal-by-deal basis to assess performance trends.

It looks likely that the primary market might take a breather at the start of March as the market consolidates the issuance over the last month, which in turn is likely to keep spreads steady, with an ongoing tightening bias in the near future. This is also supported by fairly typical secondary steady BWIC supply supporting the supply/demand technical. Later in the month we expect to see some more UK supply, which could allow the portfolio managers to rotate the book.

| Cumulative Performance | | | | | Annualised | | | |
|---|---|---|---|---|---|---|---|---|
| | 1m | 3m | 6m | 1y | 3y | 5yr | 10y | Since Inception* |
| Class I Acc (Gross) | 1.00% | 4.11% | 2.73% | 0.64% | 0.76% | 1.06% | 2.22% | 3.01% |
| SONIA | 0.30% | 0.86% | 1.44% | 1.96% | 0.71% | 0.69% | 0.54% | 0.52% |

| Discrete Performance | YTD | 2022 | 2021 | 2020 | 2019 | 2018 | 2017 | 2016 | 2015 | 2014 | 2013 |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Class I Acc (Gross) | 3.20% | -2.63% | 1.91% | 0.47% | 3.07% | 0.00% | 5.30% | 4.46% | -1.89% | 4.92% | 5.23% |
| SONIA | 0.59% | 1.41% | 0.05% | 0.19% | 0.71% | 0.56% | 0.25% | 0.36% | 0.46% | 0.43% | 0.43% |

Past performance is not a reliable indicator of future performance. The performance figures shown are in GBP on a mid-to-mid basis inclusive of net reinvested income and net of all fund expenses. Performance data does not take into account any commissions and costs charged when shares of the fund are issued and redeemed. The value of an investment and the income from it can fall as well as rise as a result of market and currency fluctuations and you may not get back the amount originally invested. *Inception date 10/08/2009.

## Key Risks

- **All financial investment involves risk. The value of your investment isn't guaranteed, and its value and income will rise and fall. Investors may not get back the full amount invested.**
- The issuer of ABS products may not receive the full amounts owed to them by underlying borrowers, which would affect the value of the Fund. Credit and prepayment risks also vary by tranche which may affect the Fund's performance.
- Past performance is not a reliable indicator of future performance, and the Fund may not achieve its investment objective.
- The Fund has the ability to use derivatives, including but not limited to FX forwards, for hedging only (EPM). This may magnify gains or losses.

## Fund Managers

**Aza Teeuwen**
Partner, Portfolio Management, industry experience since 2007.

**Douglas Charleston**
Partner, Portfolio Management, industry experience since 2006.

**Elena Rinaldi**
Portfolio Management, industry experience since 2014.

**John Lawler**
Portfolio Management, industry experience since 1987.

**Marko Feiertag**
Portfolio Management, industry experience since 2005.

**Robert Ford**
Partner, Portfolio Management, industry experience since 1986.

Further Information and Literature:
TwentyFour Asset Management LLP

T. 020 7015 8900
E. sales@twentyfouram.com
W. twentyfouram.com

**Further information on fund charges and costs are included on our website at www.twentyfouram.com**