TwentyFour ASSET MANAGEMENT

TwentyFour Income Fund

Monthly Commentary | 30 October 2020

Market Commentary

This was a challenging month for risk sentiment as the second wave of COVID-19 spread across Europe, leading to countries imposing secondary lockdowns. France, Germany and the UK all announced new lockdown measures, albeit slightly less restrictive than those imposed in March and April, resulting in underperformance across European assets. With Europe facing another wave of economic headwinds, the ECB meeting at month-end was closely watched, and while the consensus view was for no policy changes the market was looking for any indication of increased stimulus in the near future. Christine Lagarde did not disappoint as she suggested the board were discussing increasing stimulus at the next meeting in December, referring to a "recalibration" of the ECB's asset purchase programme no less than 20 times in her press conference. Brexit talks were also in focus as the soft deadline of October 15 set by the UK government passed and negotiations between the two sides continued. As of the end of October, both parties sounded optimistic for a deal to be agreed, with fishing quotas seemingly the only key blocker left in reaching an agreement. Staying with the UK, rating agency Moody's downgraded the country's sovereign rating to Aa3, citing "weaker economic growth, an erosion of fiscal strength and a weakening in institutions and governance". UK GDP for August also disappointed at 2.1% vs. expectations of 4.6%, and well below last month's revised figure of 6.4%. However, the market reaction to both was largely muted as investors chose to focus on Brexit developments. Most importantly, voting for November's US presidential election was well under way in October, as many voters took the opportunity to use early voting and postal votes. Around two-thirds of 2016's turnout had already cast their votes by month-end. The significant number of postal votes however could cause a delay in a winner being announced, with several key states involved in litigation over vote counting rules. Nevertheless, at the end of October, the Democrat candidate Joe Biden was ahead in the polls with FiveThirtyEight, a key polling website, giving him an 8.5-point lead over President Trump. The positive momentum in primary European ABS and CLO markets continued throughout October as issuers sought to print their deals ahead of impending broader macro events and a rapidly approaching year-end, which will begin to curtail the window of opportunity. Around €13bn of new issue supply was placed, with the vast majority being from mainland Europe and predominantly from the auto and consumer ABS sectors. Auto transactions came from Spain, France, Germany, Switzerland and Finland, consumer deals came from Italy, France and Germany, and there was also a Dutch BTL RMBS. The UK saw two new issuers making RMBS market debuts, meanwhile, one being a housing association deal from an established sponsor more commonly seen in the CMBS market, together with a new buy-to-let lender. One large deal of around €2bn which securitised German consumer loan receivables saw very strong demand across the capital stack, and enabled the borrower to increase the deal size and tighten the price guidance. CLO year-to-date issuance now stands at just under €20bn following the successful placement of several deals over the month, with the more established managers achieving the best pricing execution, and investors attracted by the spread premium offered by new issues and the ongoing intrinsic value of the Euribor floor.Given October has proved to be the most active so far this year for primary issuance, it was encouraging to see nearly all deals multiple times oversubscribed and pricing at the tighter end of initial indications, though investor interest understandably began to taper towards the end of the month and one or two deals didn't quite reach the tighter levels; a combination of issuer fatigue after a very heavy pipeline and wider market concerns, particularly the renewed COVID-19 fears. Primary market issuance YTD now stands at around €62bn, around 30% lower than at the same point last year. Secondary ABS markets in the UK continued where they left off in September, as the strong technical prevailed in the absence of any material new issues in the RMBS sector and spreads remained firm. Trading flows in the UK were interrupted mid-month by a very large £600m UK NC/BTL BWIC across senior and mezzanine bonds, and with a week's notice given ahead of the auction very little flow was seen in advance of the deadline. Investors hoping to source bonds in the auction at discounted levels were left disappointed as there was strong participation from both investors and bank trading desks across the capital stack. Nearly all bonds traded apart from some of the non-investment grade bonds, where reserve levels were not met and were therefore these were retained by the seller. Demand also continues in legacy 1.0 UK deals offering more convexity and duration, where the theme of potential earlier calls from issuers continues to prevail. As if to back this up, the market saw notices from two issuers seeking to amend the clean-up notional outstanding calls, suggesting these might come sooner than previously anticipated. Similarly in euro denominated bonds, for the most part, spreads continued to grind tighter over the month despite the very high level of primary issuance and consequential uptick in secondary selling of shorter dated bonds as investors rotated into new issues. CLOs overall saw spreads trade sideways, on lower secondary volumes following elevated trading levels in September with an ongoing spread dispersion basis between different managers and deal performance. However, despite the market comfortably absorbing the very high level of primary and secondary market activity with no underperformance, the combined weight of renewed COVID-19 lockdowns, the US election, a looming Brexit deadline, weaker broader equity and credit markets saw ABS markets indirectly affected in the last few days of the month. In order of magnitude the Senior Prime RMBS and Auto space saw a couple of basis points of widening, with the higher beta sectors such as mezzanine CLOs observed to be about 20-30bp wider.

Portfolio Commentary

In October the portfolio managers bought several new positions in the primary market. Firstly a UK RMBS deal form a specialist lender offering BTL and owner-occupied mortgages was added in the mezzanine tranches at attractive yields. Also added was a highly granular liquid German consumer receivables transaction from a mainstream bank where the Fund invested in the mezzanine tranches. Lastly in primary the team added a Dutch RMBS in the mezzanine tranche from a non-bank issuer which has now built a good track record in the market with good performance observed in previous deals. These purchases were funded from rotation out of short dated positions trading at a premium. With wider ongoing macro volatility observed in markets the managers continued to optimise the fund in terms of positioning and yield. All outstanding positions in senior AAA CMBS were sold during the month and reinvested into a mixture of more liquid high conviction CLOs at similar yields. Several positions in mezzanine RMBS were sold and the cash balance was increased slightly to take advantage of any spread weakness in the course of the next few weeks caused by any wider market volatility. Liquidity offered by trading desks remained satisfactory, though in the last few trading sessions of the month the portfolio managers observed a reduction in appetite to position certain risk assets on balance sheet. The portfolio managers will maintain appropriate levels of liquidity and balanced positioning across rating and sector in the Fund. Fundamentals in the ABS market remain robust, with investment grade ABS continuing to benefit from strong subordination levels and the team will continue to maintain high levels of due diligence on the underlying portfolio. The fund returned 0.14% (NAV Per Share) for the month with 3yr volatility since inception at 11.24%.

Market Outlook and Strategy

There are just a handful of primary deals in the current visible pipeline and in comparison to the last two months, activity is likely to start to tail off for the rest of the year. Issuers were keen to print ahead of the approaching macro headwinds and any subsequent spread widening will in all likelihood result in a reluctance to come to the market, unless there is a compelling reason to conclude a transaction. We continue to have a positive outlook for mainstream ABS markets and are encouraged by their resilience and performance against a very challenging backdrop, and also by the ongoing inflows into the sector, however we remain cognizant that a significant uptick in broader market volatility could also flow through to the ABS sector. The anticipated lower levels of primary supply should continue to support the strong technical into year-end, and we believe that any spread underperformance in the sector will represent a good buying opportunity for mainstream asset classes. The managers continue to monitor the performance of every deal across portfolios and while COVID-19 developments remain fluid, ABS deals are doing exactly what they are designed to do; provide a stable level of income from highly granular portfolios, within a bankruptcy remote vehicle, and very robust structure affording ample and increasing levels of protection via tranched credit enhancement which is accretive over time.

Rolling Performance	31/10/2019 - 30/10/2020	31/10/2018 - 31/10/2019	31/10/2017 - 31/10/2018	31/10/2016 - 31/10/2017	30/10/2015 - 31/10/2016
NAV per share inc. dividends	2.74%	2.30%	4.96%	13.09%	4.00%

The performance figures shown are in GBP on a mid-to-mid basis inclusive of net reinvested income and, with the exception of share price performance figures, net of all fund expenses. Past performance is not a reliable indicator of future performance. Performance data does not take into account any commissions and costs charged when shares of the portfolio are purchased and disposed of.

Fund Managers

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

Ben Hayward
Partner, Portfolio Management, industry experience since 1998.

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

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

John Lawler
Portfolio Management, industry experience since 1987.

Marko Feiertag
Portfolio Management, industry experience since 2005.

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.**
- Past performance is not a reliable indicator of future performance, and the Fund may not achieve its investment objective.
- The Fund invests in structured credit products or asset-backed securities (ABS). The issuer of such 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.
- 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.
- Typically, sub-investment grade securities will have a higher risk of issuer default, and are generally considered to be more illiquid than investment grade securities.

Further Information

Further Information and Literature: TwentyFour Asset Management LLP

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