

TwentyFour Income Fund

This Commentary is a marketing communication for professional UK investors only

Market Commentary

September was characterised by a material repricing in the market's expectations for the future path of interest rates, with investors pricing in a more aggressive rate-cutting cycle by major central banks. This led to a bull steepening of yield curves and helped drive strong returns across a host of sectors within fixed income. Encouraging data out of the US supported the soft landing narrative, while economic growth in large parts of the Eurozone continued to weaken.

Given the weaker than anticipated labour data out of the US in August, the US jobs report at the beginning of September was a key date in investors' diaries last month. The highly anticipated report provided something for everyone. The unemployment rate ticked down to 4.2% from 4.3% previously (as expected), but non-farm payrolls (NFP) only rebounded to +142k, below the forecasted +165k figure. US headline consumer price inflation (CPI) later in the month came in at 0.19%, taking the year-on-year figure down to 2.5%, which was in line with expectations but represented the lowest annual rate since February 2021. However, there was an upside surprise for core inflation, which printed at +0.28% on a month-on-month basis, primarily driven by an uptick in owner equivalent rent, which came in at a seven-month high of +0.5% for August alone. Despite the labour market and inflation reports coming broadly in line with expectations, reports from well-sourced journalists suggesting a 50 basis points (bps) interest rate cut was on the table for the US Federal Reserve (Fed)'s September meeting fuelled a growing and subsequently dominant narrative that the Fed would indeed deliver a half-point cut. The Federal Open Market Committee (FOMC) eventually did announce a 50bps interest rate cut, marking the beginning of the cutting cycle for the US central bank as it lowered the Fed funds rate to 5%. The FOMC also revealed downward revisions to inflation projections, with 2025 personal consumption expenditures (PCE) lowered by 0.2% to 2.1%, and upward revisions to the unemployment rate forecast to 4.4% from 4.2% previously. Updated dot plot projections showed that the median FOMC member expects the Fed to cut by a further 50bps to 4.5% by year-end and 3.5% by the end of 2025, which was more hawkish than what the market was perhaps expecting. US economic data in the days following pointed towards the US economy remaining resilient and inflationary pressures being kept under control. Retail sales were stronger than anticipated and headline PCE inflation printed marginally below. In line with Fed commentary throughout September, the data served as further evidence that inflation is being tamed, although the battle is not yet completely won.

In Europe, the European Central Bank (ECB) delivered a 25bps rate cut, in line with market expectations, reducing its deposit rate to 3.5%. Updated forecasts showed marginally downgraded growth projections to +0.8% for year-end 2024, +1.3% for 2025 and +1.5% for 2026. Headline inflation forecasts were kept unchanged, but core CPI forecasts were raised. Purchasing Managers' Indices (PMI) towards month-end were very weak, with signs of significant economic weakness across large parts of the Eurozone. The Eurozone's composite PMI figure printed at 48.9 in September, down from 51.0 in August and materially underperforming the 50.5 expectation, driven by a continued decline in manufacturing activity across the bloc. The print led some investment banks to downwardly revise their GDP forecasts for the Eurozone for the remainder of the year. Markets began pricing in another quarter-point rate cut by the ECB in its October meeting as weak economic data emerged.

The Bank of England (BoE) bucked the trend and kept its policy rate unchanged at 5% last month, with members voting 8-1 in favour of holding rates, broadly in line with market forecasts. The announcement followed UK headline CPI coming in line with expectations at +2.2%. However, core inflation ticked up to 3.6% on a year-on-year basis, with the move largely driven by an increase in services inflation to 5.6% from 5.2% previously. In light of this, Governor Andrew Bailey stated that BoE members "need to be careful not to cut too fast or by too much" as core inflation is still running significantly higher than the bank's 2% target. Economic activity is not yet showing signs of material weakening in the UK; strong PMIs suggest net economic expansion as the composite figure printed at 52.9 and retail sales outperformed economist forecasts at +1% month-on-month. On the labour side, the unemployment rate fell by one-tenth to 4.1% in September, as did average weekly earnings to 4.0% on a year-on-year basis.

Summary

September was characterised by a deluge of new issuance in both asset-backed security (ABS) and collateralised loan obligation (CLO) markets. Primary markets saw a record €15.4bn of ABS issuance and €7.5bn for CLOs, bringing the year-to-date total to over €113bn. For the first time this year, we have not seen a blanket tightening in spreads over the month, as wider market volatility and supply created pockets of value opportunities in the market, particularly in AAA bonds. We expect the pace of supply to continue, as lenders look to secure funding prior to US elections, and given heightened tensions in the Middle East.

RMBS: Residential mortgage-backed security (RMBS) markets picked up during September, with nine new issues. Cumulative issuance now sits at €41.5bn. The market was dominated by UK specialist lenders at the start of the month, with transactions from Paratus, Together and Belmont Green pricing in quick succession. General coverage was strong across the board. Seniors saw a range of 79bps for Belmont Green to 96bps over SONIA for Together, all ending tighter than initial price thoughts. The Belmont Green print at 79bps was the tightest of the year, and welcomed coverage of 3.5X, although it is worth noting the considerably shorter maturity at 1.8 years versus the more standard three years. Mezzanine tranches continued to attract attention with 4-7X coverage in most cases, and BBBs managed to creep inside of 200bps over risk free, with

Belmont Green printing the BBBs at 190bps over SONIA. Later in the month, we saw the return of Dutch prime issuance, welcoming transactions from Lloyds and Tulp mortgages. The two transactions printed the senior bonds over 20bps apart at 50 and 73 over Euribor, respectively. This can partially be attributed to the former being a bank platform, but we also think evidences slight AAA indigestion. We expect the pace of RMBS issuance to remain steady through repeat and debut issuers.

CLO: CLO markets experienced a very busy September, driven by a wave of refinancings as issuers capitalised on lower funding costs and re-levered older and amortising CLOs. We welcomed €7.5bn of issuance during September, €5bn of which were refinancings. This brings the year-to-date supply to a record €54.5bn, €35bn of which is new issue. AAA levels for new issues have remained firm at 1.3% over Euribor. However, we are generally seeing issuers demand a risk premium for resets that have not cleaned the collateral pool, in the face of higher uncertainty. The same tiering can be seen at the BB level, where Capital Four managed to print inside of 600bps, at Euribor + 5.95%. However, we are seeing a range out to 7.25% (noting Invesco printing at this level) for some managers. Loans have generally moved tighter during September, with the European leverage loan index now trading close to 97.5.

Other ABS: We saw an impressive level of issuance in the ABS market during September, diverse in asset class and geography. A large share of issuance was welcomed from the peripheral consumer market, reflected in auto and consumer loan transactions. These transactions, such as Sabadell (Spanish consumer), BBVA (auto) and Stellantis (Spanish auto), gathered a healthy level of interest overall, with yields ending in the Euribor +0.8% area and healthy coverage of 2-2.5X on seniors. However, we have noticed investor sensitivity to this, with transactions that try to test inside this clearing level struggling to gather interest - perhaps as investors anticipate sufficient supply to remain selective. The mezzanine prints suggest less sensitivity to levels at the margin, and we now see BBBs inside 200bps in some cases, and large book coverage shows strong investor demand. The commercial mortgage-backed security (CMBS) market also showed signs of life during September. The Office Group printed a UK CMBS transaction, which was fully pre-placed, with AAAs at 1.9% over SONIA, down to a Single B tranche at 6.8% over. It is worth noting the mix in collateral quality we have seen during the month, which we don't think is necessarily reflected in pricing levels, such that we reiterate our preference to established issuers with a strong track record. Australian issuance can also not be overlooked for September, where we have seen over \$2bn of third quarter issuance in RMBS. The Australian market continues to look attractive on a currency-adjusted basis in our view and is seeing healthy participation from Europe.

Secondary: Bid wanted in competition (BWIC) activity picked up in tandem with primary activity, as we saw €1.1bn of ABS and close to €1.5bn of CLOs trading on BWICs. On the ABS side, we see BWIC activity as driven by accounts rotating into new issues to pick up yield, along with fast money accounts taking profits. In comparison to the first eight months of the year, we saw spreads move a few bps wider for Euro Senior ABS, citing supply here. However, UK RMBS continues to trade tighter, with spread levels now firm around 50 for prime RMBS and 70-80 for buy-to-let. In the CLO space, we saw AAAs dominating 50% of all trading activity, indicating rotations into primary transactions, with more deals now being priced to an early call.

Portfolio Commentary

September was a busy month for the Fund, as the team took advantage of an active primary market. In the CLO market, the team continue to allocate to BB and Bs, where spreads remain attractive versus corporates. The team added BB CLOs at spreads of 6.15-6.4% over Euribor, and Bs at 9% over Euribor in primary markets. The portfolio management (PM) team continue to allocate to shorter consumer assets in primary, where they see a strong credit story. During the month, this included BB rated European autos at 3.25-3.4% over Euribor, and B rated Spanish consumer paper, yielding 5.1% over Euribor. During September, the Fund successfully refinanced two pools of Dutch prime mortgages, locking in long-term funding and releasing capital back to the Fund. The gearing of the Fund remained unchanged in September, and the PM team are happy with the Fund's flexibility ahead of the US elections.

The Fund returned 0.75% for the month, with three-year volatility at 7.39%.

Market Outlook and Strategy

Despite market anticipation for a busy September, activity has surpassed expectations and, importantly, is diverse in geography and sector. The deluge of supply was generally digested well, with general risk sentiment supporting strong mezzanine prints across sectors. However, we started to see evidence of fatigue in some transactions towards the end of the month, which is most apparent in AAAs. Meanwhile, spread products continue to provide an attractive running income with a lack of material declines evident in collateral performance. We anticipate a busy October, with more transactions coming out of the UK. Additionally, we think that the level of CLO refinancing will persist in the medium term. The PM team notes heightened uncertainty going into October, driven by escalations in the Middle East and event risk surrounding the US presidential election. Therefore, the PM team value flexibility in the funds from here, while remaining opportunistic to adding good quality at attractive prices. Notwithstanding this, we caution on issuers with weaker collateral quality using the attractive pricing to lock in funding. The team continues to prefer established issuers with a long track record.

| Cumulative Performance | 1m | 3m | 6m | 1y | Annualised | | | |
|------------------------------|-------|-------|-------|--------|------------|-------|-------|------------------|
| | | | | | 3y | 5y | 10y | Since Inception* |
| NAV per share inc. dividends | 0.75% | 2.69% | 7.41% | 18.41% | 7.85% | 7.44% | 6.03% | 7.82% |

| Discrete Performance | YTD | 2023 | 2022 | 2021 | 2020 | 2019 | 2018 | 2017 | 2016 | 2015 | 2014 |
|----------------------|-----|------|------|------|------|------|------|------|------|------|------|
| | | | | | | | | | | | |

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: 06/03/2013.

Key Risks

- Limited participation in the potential of single securities
- Investments in foreign currencies are subject to currency fluctuations
- Success of single security analysis and active management cannot be guaranteed
- It cannot be guaranteed that the investor will recover the capital invested
- The structure of ABS/MBS and the pools backing them might not be transparent which exposes the fund to additional credit and prepayment risks (extension or contraction risks) depending on which tranche of ABS/MBS is purchased by the Fund
- The Fund has the ability to use derivatives, including but not limited to FX forwards, for hedging and EPM purposes only. This may magnify gains or losses
- Typically, sub-investment grade securities will have a higher risk of default, and are generally considered to be more illiquid than investment grade securities
- The Fund's investments may be subject to sustainability risks. The sustainability risks that the fund may be subject to are likely to have an immaterial impact on the value of the Fund's investments in the medium to long term due to the mitigating nature of the Fund's ESG approach
- The Fund's performance may be positively or negatively affected by its sustainability strategy
- The ability to meet social or environmental objectives might be affected by incomplete or inaccurate data from third-party providers
- Information on how environmental and social objectives are achieved and how sustainability risks are managed in this fund may be obtained from twentyfouram.com/responsible-investment

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Further information on fund charges, costs and other important information pertaining to the fund can be found in English and free of charge on the fund pages of our website and/or in the Prospectus and the Key Information Document (KID) which are available at www.twentyfouram.com/view/GG00B90J5Z95/twentyfour-income-fund

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