TwentyFour ASSET MANAGEMENT

TwentyFour Select Monthly Income Fund

Monthly Commentary | 31 March 2020

Market Commentary

March was all about the spread and impact of COVID-19 on global markets, with investor sentiment taking a dramatic turn for the worse as it became clear the virus was not being contained in China but had become a worldwide pandemic. This resulted in some extraordinary and immediate downturns in asset prices, with the S&P 500 suffering its worst day since the global financial crisis in 2008 and the entire US Treasury curve trading inside 1% for the first time in history. Credit markets became frozen as investors scrambled for cash, causing bond spreads to gap wider regardless of quality or maturity, resulting in the most rapid sell-off we have ever seen. Indiscriminate selling by ETFs and leveraged accounts triggering margin calls merely added to the self-fulfilling spiral down.

The consequences were immediate with international borders being shut, central banks initiating extraordinary easing measures and governments launching massive fiscal stimulus packages. Government steps to isolate citizens via lockdowns and curfews have had an obvious impact on large swathes of the global economy, effectively ending the current economic cycle and starting a deep recession.

Unlike the previous recession, central banks were very quick to react with emergency measures, with the Federal Reserve announcing an emergency 50bp cut in Fed Funds (to 1-1.25%) on the March 3, the first time the Fed had cut outside of a scheduled meeting since August 2008. Unfortunately, this did little to alleviate market concerns and risk assets continued to plummet in the early part of the month. The UK then announced coordinated fiscal and monetary action, with the BoE cutting base rates by 50bp (to 0.25%) at an emergency meeting, in addition to a reduction in the countercyclical capital buffer to 0%, thereby freeing up bank capital equivalent to around £190bn of bank lending capacity. The UK Chancellor, Rishi Sunak, then announced a wide reaching package of fiscal measures aimed to support the economy. The ECB held its policy meeting as scheduled and although it did not cut interest rates (already at -0.5%), it did announce an increase in its asset purchase program and also reduced capital requirements for banks; viewed as being somewhat insufficient by the market.

With risk markets still in free-fall the Fed stepped back in with another emergency rate cut of 100bp (taking Fed Funds to 0-0.25%) and introduced a QE program injecting liquidity by buying government bonds, mortgage-backed securities and for the first time in its history, corporate debt and ETFs. The US Senate finally supported this (after days of political wrangling) with a $2tr package of spending and tax breaks, which finally put a floor under the sell-off and brought a general improvement in sentiment and a partial return to market liquidity. Other major economies followed suit with announcement of large-scale fiscal support measures including aid for businesses, tax breaks and support for the increasing unemployed.If that wasn't enough for investors to deal with, there was a collapse of Russia's alliance with OPEC, resulting in Saudi Arabia's decision to 'open the taps', which subsequently led to the biggest fall in the price of crude since the Gulf War in 1991. The 50% decline to under $25 a barrel added to the heightened volatility, particularly in the US high yield market, which features a large number of energy companies.

Portfolio Commentary

The portfolio looks to take advantage of liquidity premium in credit markets. The managers were not expecting a viral pandemic that would result in the complete evaporation of liquidity across all fixed income sectors. In addition, the gap lower across all bond sectors, in an indiscriminate fashion, had a material effect on the underlying NAV. The forced selling from ETF accounts and margin calls being breached from levered accounts created an unprecedented period as the 'dash for cash' left quality assets at depressed valuations.

The managers did not capitulate but saw pockets of the market as being oversold, despite appreciating the high level of uncertainty that the pandemic had created. The managers presumed that the velocity and ferocity of the market decline could not continue for too long, and that it created a medium to long term opportunity to replenish the Fund. This was in complete contrast to earlier in the year when the managers were growing concerned about re-investment risk. As a result of this opportunity, and to satisfy investor demand, the Fund issued just over 20m new shares.

Market sentiment gradually improved toward the end of the month as medium term buyers emerged to add credit at new enhanced values, although liquidity remains low as many market participants work from home. The managers very selectively added risk, though offers at the quoted levels were difficult to source, indicating an underlying supportive technical backdrop, despite the ongoing uncertainty.

As would be expected credit indices posted negative returns across the board in March with the Coco index at -15.13%, Euro HY -13.21%, STG HY -13.19% and US HY -11.76%; CLO markets declines surpassed the vanilla markets as liquidity disappeared.

The Fund returned -20.93% during the month. CLO was the biggest detractor from performance contributing -11.05%.

Market Outlook and Strategy

The managers continue to add selective credit at credit spread levels that could represent the best entry point in years, thereby adding quality yield that will benefit the Fund over the medium to longer term. The managers recognize the global economy is very much in the very early stages of recession, hence the focus will be on high quality credit from the most robust sectors. Default rates are likely to spike and downgrades will be frequent, so the more speculative end of the credit spectrum is likely to perform poorly and will be avoided, despite the high yields on offer.

Rolling Performance	31/03/2020 29/03/2019	29/03/2019 30/03/2018	30/03/2018 31/03/2017	31/03/2017 31/03/2016	31/03/2016 31/03/2015
NAV per share inc. dividends	-13.55%	0.76%	10.15%	16.92%	-4.45%

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

Gary Kirk
Partner, Portfolio Management, industry experience since 1988.

Eoin Walsh
Partner, Portfolio Management, industry experience since 1997.

Mark Holman
CEO, Partner Portfolio Management, industry experience since 1989.

David Norris
Head of US Credit, Portfolio Management, industry experience since 1988.

Felipe Villarroel
Partner, Portfolio Management, industry experience since 2007.

Pierre Beniguel
Portfolio Management, industry experience since 2010.

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.
- Fixed income carries two main risks, interest rate risk and credit risk: (1) Where long term interest rates rise, there is a corresponding decline in the market value of bonds and vice versa; (2) Credit risk refers to the possibility that the issuer of the bond will not be able to repay the principal and make interest payments.
- 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.
- The Fund can invest 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 performance 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.
- Investments in emerging markets may be affected by political developments, currency fluctuations, illiquidity and volatility.

Further Information

Further Information and Literature: TwentyFour Asset Management LLP

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