TwentyFour ASSET MANAGEMENT

UK Mortgages Limited

28 August 2020

UK Mortgages Limited is a LSE-quoted listed closed-ended fund managed by TwentyFour Asset Management LLP.

Commentary

Mortgage and Housing Market

The strong rally in the housing market has continued once again, with Nationwide reporting house prices increased by 5% annually in September, the highest growth rate in four years. Reports also show that the price of the average UK house hit a new record, pushing over £225,000 for the first time. Undoubtedly much of this has been boosted by the reduction in Stamp Duty which, according to Onrec, has also had associated knock-on benefits to the construction, property development, mortgage broking and real estate industries who have benefitted from increased business and enquiries. According to the Bank of England, around 84,700 mortgages were approved in August, the highest since October 2017 and taking the overall number to 415,000 approvals this year, and GetAgent's latest homebuyer demand hotspots index showed current buyer demand levels are at their highest since the start of last year, up 9% annually and 8% in the last quarter. Some commentators such as RICS warned that following a fourth consecutive month of increasing demand, sales are expected to weaken in the year ahead as unemployment rises, and a PwC report cautioned on potential weaker or negative markets in 2021 depending on the development of different Covid-19 scenarios, but Savills reported more than a million homes are expected to sell by the end of the year and predicted a 4% increase in prices this year, followed by stagnation next year when the Stamp Duty effect comes to an end but a return to growth in 2022 and 2023 with a total expectation of a 20% by 2024.

RMBS Market

The UK RMBS market also continued to recover after a quieter summer, albeit the primary market saw just two publicly distributed new deals along with another privately placed refinancing transaction, and with a fairly small pipeline building. Interestingly, one of those placed deals was a pool of BTL loans originated by TML, funded by their BTL partner Shawbrook Bank rather than UKML. The deal priced competitively with the senior notes placed at a spread of Sonia+110bps. Meanwhile secondary markets tightened slowly and steadily particularly in the Prime STS sector where bids are now comfortably inside pre-Covid levels, and this in turn led spreads in BTL and Non-Conforming deals to continue to grind tighter across the capital stack.

Fund Commentary

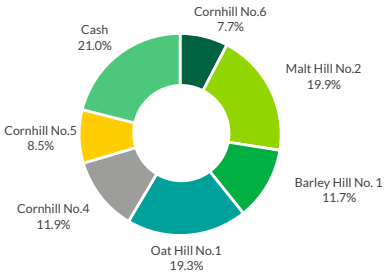
The number of remaining borrowers taking payment holidays continues to fall as the first cohorts of borrowers who took extension start to come to an end, albeit not enough data is available yet to fully assess where the final quantum might settle. Undoubtedly, all of our BTL portfolios have performed extremely well, and whilst a small proportion may ultimately result in longer term arrears, the vast majority of borrowers have or are now returning to making payments. The owner-occupied TML portfolios unsurprisingly saw the highest number of payment holidays but these have also fallen sharply and the residual number that may fall into arrears is still difficult to gauge at this time with next month's data likely to be key to making that judgement. Meanwhile, the portfolio managers have been making early preparations for future securitisation activity. As part of this, a virtual investor meeting was held to introduce RMBS investors to Keystone, following a similar pattern to the introductory meetings held for TML back in the summer of 2018 leading up to the marketing and launch of the Barley Hill No.1 transaction in Q1 of the following year. Whilst Keystone have been originating mortgages since 2007, their loans have either been purchased directly onto bank balance sheets or typically formed a smaller part of larger securitisation loan pools purchased by an established originator, and so RMBS investors have rarely had the opportunity to meet the Keystone team and analyse their origination and processes more closely. Given the outstanding performance of their loan book through Covid-19 period, this slightly quieter period in RMBS markets was an excellent opportunity to begin to familiarise investors with Keystone and their products and to start the investor education process on a positive note.

Investment Outlook

The market continues to pay close attention to payment holiday reporting across all ABS transactions and, generally, as many of the initial three-month payment holidays have expired and not been extended, concentrations have been dropping. We expect this trend to continue over the forthcoming reporting periods, as the window for applications in the UK closes at the end of October, but there may be pockets of underperformance in some sectors with the potential for arrears to increase. However, it is worth reiterating that arrears do not necessarily translate into defaults and the portfolio managers monitor the performance of all transactions on an ongoing basis. Following the relatively quiet amount of primary issuance since the summer, there is a small pipeline signalled for the next month or so, although the pace of issuance is likely to tail off after that. The supply-demand technical will in all likelihood remain in place, particularly for primary RMBS issuance, which will lend further support to spreads but the pace of overall retracement in RMBS will most likely slow in line with the wider market.

Portfolio Summary	Buy-to-Let				Owner Occupied	
	Purchased			Forward Flow Originated		
	Cornhill 6	Malt Hill 2	Oat Hill 1	Cornhill 4	Barley Hill 1	Cornhill 5
Originator	Coventry Building Society	Coventry Building Society	Capital Home Loans	Keystone Property Finance	The Mortgage Lender	The Mortgage Lender
Outstanding Balance	£160m	£337m	£481m	£264m*	£167m	£238m*
Number Accounts	888	1,932	3,771	1,219*	961	1,215*
Average Mortgage Size	£180k	£175k	£127k	£217k	£174k	£196k
WA Indexed LTV	62.07%	60.26%	64.13%	71.68%	65.55%	71.94%
WA Interest Rate	2.42%	2.71%	1.37%	3.41%	4.17%	3.88%
WA Remaining Term (mth)	189	214	115	265	279	309
WA Seasoning (mth)	61	43	163	9	24	8
3mth + Arrears (% balance)	0.00%	0.14%	0.78%	0.00%	1.59%	0.30%

Investment breakdown



as at 28/08/2020

1. Dividend guidance in this factsheet is a target only and not a profit forecast and there can be no assurance that this target will be met.
* from February 2020, pipeline has been excluded and figure refers to completed loans only

as at 28/08/2020

Fund Facts

Type of Fund:	Closed-ended Investment Scheme
Listing & Trading:	LSE Specialist Fund Market
ISA & SIPP Eligible:	Yes
Launch Date:	7th July 2015
Currency:	£ denominated
NAV Calculation:	As of the last business day of each month
Dealing:	Daily during LSE opening hours
Dividend:	Quarterly from April 2016
Market Capitalisation:*	£172.7mn
Shares in Issue:	273mn
Price per Share:*	63.25p
NAV per Share:*	80.41p
NAV per Share (inc Dividend):*	104.04p
Premium / (Discount) to NAV:*	-21.34%

Source: TwentyFour Asset Management. * as at 31/07/2020

Glossary

BTL:	Buy-to-Let
RICS:	Royal Institute of Chartered Surveyors
RMBS:	Residential Mortgage Backed Securities
STS:	Simple, Transparent and Standardised Securitisation
TML:	The Mortgage Lender

Trading Information

TIDM	UKML
ISIN	GG00BXDZMK63
SEDOL	BXDZMK6
AMC (%)	0.60

Investment Objective

The Company aims to provide Shareholders with stable income returns through low leveraged exposure to portfolios of loans secured against UK residential property.

Investment Policy

The Company's investment policy is to invest in a diversified portfolio of UK residential mortgages.

- The Company will purchase legacy portfolios with strong observable performance histories or new portfolios with robust underwriting standards
- Primary origination mechanism may also be put in place
- Leverage will be used, initially via a banking facility, before fully securitized term structure put in place

This is only a summary; details of the Company's investment policy, including investment restrictions, are set out in the Prospectus.

IFRS 9

With regards to IFRS 9 – the company has been reporting its results in accordance with IFRS 9 since 1 July 2018. When making future loss provisions under IFRS 9 the low level of historic defaults in the UK mortgage sector and the credit protection afforded by the low LTV of the loans within our portfolio is factored into our provision calculations, along with the recent addition of mortgage payment holidays. The unaudited impact of IFRS 9 has been calculated at 0.92% on the Fund's NAV, for the 30 June 2020. The impact of expected credit losses is already modelled in the IRR calculations for our portfolios and is also included in our portfolio dividend and NAV models.

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 can invest in portfolios of mortgages or the equivalent risk. The lenders of such products may not receive in full the amounts owed to them by underlying borrowers, affecting the performance of the Fund.
- Prepayment risks also vary and can impact returns.
- The fund employs leverage, which may increase volatility of the Net Asset Value.

OCF Breakdown

UK Mortgages Ltd	0.81%
UK Mortgages DAC and SPVs (excl. servicing and transaction costs)	0.15%
	Total 0.96%
Servicing and Transaction costs (for information)*	2.16%

*Servicing and transaction costs are provided for information only as deal specific servicing and other transaction costs are included in IRR projections per investment. As at 30/06/2020.

Fund Managers

Robert Ford
Partner, Portfolio Management, industry experience since 1986. Previously a Managing Director and Head of European ABS Trading at Barclays Capital.

Ben Hayward
Partner, Portfolio Management, industry experience since 1998. Previously he was a senior fund manager to four portfolios at Citi Alternatives.

Douglas Charleston
Portfolio Management, industry experience since 2006. Previous roles include structuring ABS at Lloyds, ratings analyst at S&P and a portfolio manager at Nationwide.

Silvia Piva
Portfolio Management, industry experience since 2007. Previously she was a structurer and originator at RBS covering UK financial institutions.

Shilpa Pathak
Portfolio Assistant, industry experience since 2013. Previous roles include an application development consultant at Dow Jones and a software developer at Dell.

Further Information

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