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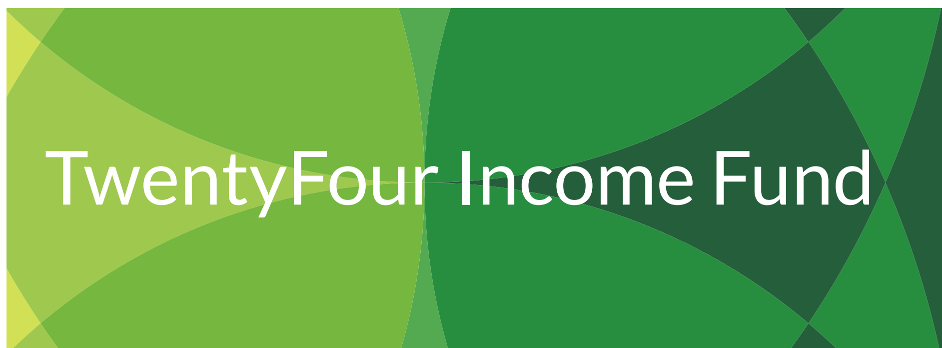
TwentyFour ASSET MANAGEMENT



Monthly Commentary | 30 September 2021

Market Commentary

September was a weak month for broader risk-on assets generally, as inflation and tapering weighed heavily on sentiment. In Asia, new and onerous regulatory oversight and the potential failure of Evergrande added to investor angst. Fears of market contagion grew as the company edged closer to default, and the market grew concerned about the fallout from a messy default and the form of any potential intervention from the authorities.

Meanwhile, the FOMC kept policy unchanged but signalled that tapering could begin "if progress continues broadly as expected". The consensus now seems to be for the Fed's to announce tapering at its next meeting in November. The dot plots were updated to show that two more Fed members now expect a first rate hike in 2022, leaving the FOMC split down the middle. The median forecast now sits at 0.25% (previously 0.125%). The Committee also increased its inflation forecast, with Core PCE expected to finish 2021 at 3.7%, an increase on from 3.0%. All of this led to some relatively large moves in US Treasuries; the bellwether 10-year yield started September at 1.31% before widening by around 23bps to a high of 1.54%, before closing out the month slightly off the wides at 1.49%. Meanwhile, the Bank of England's (BoE) Monetary Policy Committee kept policy unchanged but made some hawkish comments regarding the trajectory and quantity of future interest rate rises. Like the Fed, the BoE increased its inflation forecasts for Q4 to "slightly above 4%" from 4%. The UK has witnessed several inflationary pressures during the month. Accordingly, the August CPI print came in at 3.2% versus a consensus of 2.9%. The August figures followed a July reading of 2.0%, representing the largest monthly jump since records began. The yield on the 10-year gilt rose steadily over the month to finish at 1.02%, an increase of over 30bps.

Primary market ABS issuance bounced back strongly in September, contributing to the busiest quarter of the year so far. Gross YTD issuance now stands at around €81bn, including €25bn of new issue CLOs. September saw €13bn of placed bonds with RMBS across Europe accounting for the largest sector, followed by CLOs. The UK saw four RMBS deals placed, both offering senior and mezzanine bonds with all-seeing solid demand across the capital stack. There has been a growing trend in the UK for BTL borrowers to opt for five-year fixed-rate mortgages. The trend has pushed some call dates out beyond four years and has naturally led to longer weighted average lives of Senior AAA bonds, thereby precluding some investors from participating in these deals. However, oversubscription levels so far remain consistently strong, with issuers achieving attractive pricing for longer maturities. As a result, AAA pricing is now comfortably in the Sonia +60-70 area on AAA. The main theme in Europe was an increase in Auto and Consumer deals. On the Auto side, there were six deals from Italy, Spain, Germany, Portugal and Belgium offering a mixture of senior and mezzanine bonds, giving investors some added diversification. Pricing on all these deals was broadly in line with each other. The mezzanine saw particularly strong oversubscription levels resulting in a few rounds of price testing at significantly tighter levels than initial IPTs. The consumer loan side saw a deal from an inaugural issuer in Germany and a repeat issuer launching its first Portuguese deal. Neither was particularly large, but one was a representative example of a deal being placed into a strong supply-demand technical backdrop that might otherwise have struggled and yet achieved one of the tightest pricing prints seen this year at 30dm for a sub-one year AAA class. The portfolio has very high defaults offset by very high rates of interest and upfront costs giving rise to ESG concerns, compounded by weak bond investor alignment of interest through aggressive structuring. Primary CLOs saw healthy issuance of around €4bn, wrapping up the busiest quarter for primary issuance at €11bn since the start of the 2.0 era. AAA pricing, which had widened a little over the summer, has started to retrace with new deal coupons now testing inside 1.0% yield with a floor benefit of around 16bps. Further down the capital stack spreads remained more range-bound in the face of elevated supply, which we expect to continue for the rest of the year. The tone in secondary markets remained positive over the month, although spreads were a little weaker into month-end due to weakness in broader credit markets. Although BWIC volumes increased, secondary trading was a little more subdued. Activity mainly centred around the rotation of short-dated Senior AAA bonds into primary issuance and leveraged investors looking to lock in quite large price moves on high coupon mezzanine bonds issued in 2019-2020. Spreads were generally unchanged across most sectors with modest tightening in Dutch RMBS seniors and UK Prime RMBS. Secondary CLO activity picked up following a very subdued August, and the market saw around 200mm of BWIC supply in sub-investment grade risk. This supply was absorbed quite strongly, and good demand for longer-dated high coupon AAA remains.

Portfolio Commentary

In September, the portfolio managers focussed on the secondary market, although this remained relatively quiet. The fund added positions in CLO bonds in sub-investment grade positions from preferred managers at attractive yields. The managers also add-ed a rare UK non-conforming deal. Secondary market pricing remained relatively sta-ble throughout the month. Fundamentals in the ABS market remain robust, and the team will continue to maintain high levels of due diligence on the underlying portfolio through the recovery stage of the cycle.

The fund returned 0.61% for the month, with 3-year annualised monthly volatility at 11.35%.

Market Outlook and Strategy

The end of September saw the Global ABS conference take place in London over a two day period. The general takeaway from market participants was the positive tone of European structured finance market, particularly considering the robust perfor-mance for all asset classes over the last 18 months. The other prevalent topic on al-most all panels was ESG and the approach required for qualification, which will be an ongoing theme. Regarding the transition away from LIBOR, the FCA has announced if contracts are unable to be transitioned in time, it will permit the use of synthetic Sterling LIBOR for the duration of 2022. However, they will clarify which legacy contracts will be allowed to use the rate as soon as practical following a consultation closing on 20th October

The UK Rates market is now pricing in two base rate hikes in 2022; one in Q1 and one in Q3. It is worth noting that this is positive for ABS bonds being almost entirely floating-rate notes. In September, Moody's upgraded 71 bonds from UK Non-conforming and BTL RMBS on the back of improved credit enhancement due to deleveraging. Al-so upgraded were 40 tranches of legacy 1.0 deals in the UK and 11 tranches in Dutch RMBS. As we move into Q4, the pipeline for primary deals looks reasonably steady against a continued supportive backdrop in the ABS market.

Rolling Performance	30/09/2020 - 30/09/2021	30/09/2019 - 30/09/2020	28/09/2018 - 30/09/2019	29/09/2017 - 28/09/2018	30/09/2016 - 29/09/2017
NAV per share inc. dividends	11.50%	2.32%	3.14%	5.38%	12.51%

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

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

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