TwentyFour Income Fund

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Market Commentary

July was a strong month for markets with sentiment rebounding after a very weak June. In equities all major indices saw strong rallies, while in credit the iTraxx Crossover Index tightened by over 70bp. The risk-on tone was driven by attractive valuations, a strong earnings season and a firmness in rates as government bond yields tightened on both sides of the pond.

The Fed was closely watched and as expected hiked rates by 75bp in July for the second meeting in a row. The market latched on to the FOMC statement that the US economy had "softened", as well as comments from Fed chair Jerome Powell that the pace of hikes was likely to slow, interpreting these as a signal for a Fed pivot despite a higher than expected headline inflation figure of 9.1%.

Meanwhile, the European Central Bank exited negative rates at its July meeting and surprised markets by hiking 50bp. This was accompanied by the ECB's new anti-fragmentation tool (officially the Transmission Protection Instrument or TPI), however details remain vague at this stage. A collapse of Mario Draghi's government in Italy saw fresh elections scheduled for September and increased volatility for Italian spreads, and elsewhere in Europe volatility was also elevated amid ongoing uncertainty over Russian gas supply.

Despite the ongoing market volatility and uncertain sentiment, several European ABS issuers placed deals in July ahead of the traditional summer primary lull. These were essentially all either fully or partially pre-placed, reflecting current market conditions, and giving certainty of execution to the sponsor.

The UK saw two placed BTL RMBS and one non-conforming deal, all from established platforms. All three offered the full capital stack of bonds and while it's difficult to gauge overall appetite in pre-placed deals due to the opacity of the book build process, it's fair to assume from their very launch that investor interest was good at these wider spreads. Also in the UK ABS market a credit card deal from a regular issuer saw the senior tranche (interestingly only rated to AA rather than AAA) bought by one of the lead manager banks and the mezzanine bonds saw good levels of oversubscription. The highlight though was the successful return to the market of a Prime UK RMBS deal from Santander UK's Holmes Master Trust platform; the £600m 4.65yr senior-only STS labelled deal was the first from the platform since 2018 and saw strong demand, ultimately being priced at Sonia+73bp.

In Europe two deals were seen in the Consumer ABS space; a French bank privately placed senior notes at Eur+55bp and retained all the mezzanine, while a Spanish consumer deal via Banco Sabadell saw €759m of STS labelled bonds placed across the capital stack. Both deals saw good subscription levels from investors looking at wider re-entry points into the market. Elsewhere an RMBS deal priced in Ireland comprising a portfolio of reperforming loans and an Italian RMBS deal retained by a bank in 2019 was also placed with investors.

The CLO primary market remained subdued for most of the month due to ongoing challenges around the arbitrage, with wider liability spreads and a rallying leveraged loan market making primary deals largely uneconomic despite the return of some larger anchor investors in AAAs. The WAC of the debt stack is now averaging a spread in the high 300s, which is the widest level since the COVID period, whilst the European Leveraged Loan Index gained for the fourth consecutive week and while it remains negative YTD, the month-on-month rally was the highest seen so far this year. Towards the end of the month two new issues managed to price, with the AAA bonds still pricing above Eur+200 and sub-IG levels still at the widest spreads seen in the CLO 2.0 era. There are several other deals currently in marketing, though ramping portfolios remains a challenge with limited supply in both leveraged loans and high yield bonds. This has seen CLO managers moving to use more of their bond allocations which have increased from 12% on average to around 15%.

By the end of the month overall European ABS supply had increased to around €53bn including €15bn of CLOs.

Given current market conditions there had been some uncertainty around the fate of bonds which have calls in the second half of 2022; one of these being a very large UK non-conforming deal, Hawksmoor 2019-1, which is due to be called in mid-August with £1.6bn still outstanding. In a positive move for the market, the refinancing of this deal has now been announced and has additionally been upsized to £2bn, in combination with three other legacy portfolios from the same sponsor, which has now been fully preplaced in the market across the whole capital structure at tighter spreads than currently offered in secondary markets.

Secondary market sentiment generally improved during the course of the month and limited flows saw senior RMBS spreads finally start to trade tighter, albeit in fairly thin summer market trading. AAA senior bonds stabilized and saw tightening of 5-10bp into month-end, though there is an observable dispersion developing between stronger BTL names and non-conforming deals as some traders began factoring in non-call scenarios for deals with lower coupon step-ups. Prime UK RMBS saw ongoing demand, in particular from bank treasuries. The constructive tone continued in the CLO market too, with AAAs dominating the flow and having widened to low-200s in the first half of the month, retraced in the latter part with shorter cleaner profiles tightening to high-100s. Other CLO IG bonds finished around 25bp tighter, with BB and B bonds seeing the most tightening of 75-100bp.

Portfolio Commentary

Wider spreads in the early part of the month presented the portfolio managers with the opportunity to add assets selectively at incremental yields, and subsequently benefit from the tightening in the second half as ABS spreads followed the rally in wider fixed income markets. In the secondary market the Fund added to existing BB CLO positions in the 1000bp discount margin area, which equates to a forward yield of around 12%, and by month-end these were around 50-75bp tighter. Despite traders quoting wider spreads in mezzanine bonds, sourcing RMBS at cheaper levels proved to be challenging with light BWIC flow, little dealer inventory and elevated bid-offer spreads. However, we did manage to source some positions at elevated yields in UK BTL RMBS. In primary markets the Fund purchased a new UK non-conforming deal at BBB to B, adding a little diversification. Also added in primary was a Spanish consumer deal from a mainstream bank at BBB and BB. Fundamental bond performance remains good with multiple rating upgrades seen over the month, though the portfolio managers will continue to maintain high levels of due diligence on the underlying portfolio.

The Fund returned -0.61% for the month with 3yr volatility at 11.84%.

Market Outlook and Strategy

The primary ABS market has been slow into the typically quiet August period, but there are expectations building that September will be busier. While this is usually the case, consideration to the wider geopolitical and macro backdrop will remain relevant, especially central bank rate policy, elevated inflation and concerns around recession, as well as the situation in Ukraine. In the UK and Europe we have seen relatively stable two-year swap spreads over the last month, but the retracement by over 50bp in five-year swaps and the more positive tone will be a boost to mortgage lenders and could spur some RMBS issuance in the UK, freeing up warehouse lines for further mortgage origination, which has remained buoyant in recent months despite something of a flattening in house price indicators. CLO managers have open warehouses as they continue to ramp deals in various stages of marketing with lower more expensive supply. Trying to construe all these factors into a realistic pipeline of new issuance in this market remains a challenge, but investor demand has stabilised in the real-money sector with outflows having slowed, while bank demand remains generally consistent at these levels.

Rolling Performance	30/07/2021 - 29/07/2022	31/07/2020 - 30/07/2021	31/07/2019 - 31/07/2020	31/07/2018 - 31/07/2019	31/07/2017 - 31/07/2018
NAV per share inc. dividends	-5.23%	14.53%	-1.13%	3.55%	6.37%

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.

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.

Fund Managers

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