TwentyFour ASSET MANAGEMENT

29 March 2019

TwentyFour Income Fund

Market Commentary

Another strong month for markets and a firm finish to the first quarter of 2019. The S&P saw its biggest Q1 rise in 21 years and the US 10 year treasury rallied the most for a March quarter since 2016. The key event of the month was the FOMC meeting and the dot plots update. This was much anticipated as the market speculated whether the Fed would maintain their forecast for further hikes, stay patient as they had recently guided to, or even point to a rate cut this year. The results were more dovish than many had expected with the median forecast showing rates would stay put for this year and only one hike forecast in 2020. This saw the 10yr US Treasury tighten by 35bps on the month to 2.41%. This also caused the 3m vs 10yr treasury curve to invert; a much watched signal for a US recession.

Trade talks between China and the US took a backseat although headlines continued in the background as US trade representatives visited China at the end of the month to continue talks. With a deal looking increasingly likely, President Trump seems to be turning his attentions to Europe as we await a decision on auto tariffs following the Commerce Department's review. Back in Europe, Mario Draghi also struck a dovish tone at the ECB press conference. The guidance for a potential rate hike was pushed back and the Eurozone growth forecast was cut from 1.7% to 1.1%. Supportive for banks, albeit largely expected, was the announcement of another round of TLTROs. With the growth being guided lower and potential risks to the downside, we saw increased demand for safe havens leading to yields on bunds to turn negative for the first time since 2016 as Germany sold 10 year debt at an average yield of -0.05%.

March saw the much anticipated Brexit deadline come and go, with the UK seemingly no closer to a resolution to leave the EU. Over the month, MPs had two further votes on Prime Minister May's withdrawal agreement and have taken control of Parliament to have indicative votes on several alternatives to May's deal. The EU agreed to grant a short extension to the March 29th deadline to April 12th, by which date, if nothing has been agreed by Parliament for the EU to vote on, a no-deal Brexit would be the default. The European ABS market by and large took all the backdrop geopolitical turmoil in its stride. March started off on a busier note in the primary market where we saw the widely expected and sizeable refinancing of the 2016 TPMF Granite transaction successfully completed across senior and mezzanine tranches. This faster than expected transaction was a pleasant surprise to the market removing supply overhang and a possible concern that the call dates were close to potential Brexit related dates. Deal execution was strong and supports the theme of steadily tightening spreads that has characterized Q1 2019. The market also saw the first STS ("Simple Transparent and Standardized") deal come to the market in the form of a benchmark Euro denominated Auto deal from Volkswagen which was equally well received, particularly by European investors who have seen very little investment opportunities so far this year, and emphasizes the demand in the sector. The market expects that this transaction will serve as a likely blueprint for further STS deals which are expected to start coming to the market.

Overall year to date primary issuance is around Eur 15bn, which is around 40% lower than the same period last year. The tone in secondary markets also continued to be constructive in Q1 supported by the strong negative net issuance technical and healthy client appetite. We have seen senior prime RMBS spreads compress by around 20bps so far with UK non-prime tightening by about 40bps respectively.

In CLOs, Japanese risk-retention rules were finalised last month, with the market interpreting the rules to be accommodative and workable for US CLO managers. The direct impact is likely to be muted in Europe, as most deals already comply with European risk retention rules and the indirect impact is likely to be positive for spreads. Indeed we have seen steady issuance of European CLOs in Q1, despite the ongoing inefficiency of the arbitrage, and liability spreads have materially tightened particularly in mezzanine tranches during the period reflecting strong investor appetite in both primary and secondary markets.

Portfolio Commentary

March proved to be a busy month for the portfolio managers in both primary and secondary markets. The fund selectively added risk via UK RMBS senior and mezzanine bonds together with mezzanine CMBS transactions, a UK lease deal via Rabobank and seasoned secondary mezzanine CLOs funded via inflows during the month and the sale of liquidity assets. Whilst the focus remains predominantly in shorter duration investment grade bonds the portfolio managers added a little duration via longer dated senior UK RMBS. Secondary liquidity provided by dealers was very strong during the month as the market remained in a risk on mode despite the macro backdrop. Fundamental performance across all asset classes remains consistently good and the portfolio managers continue to be comfortable with the current balanced positioning including a strong liquidity profile.

The fund returned 1.09% (Class I Acc Gross) for the month with 3yr volatility at 3.49%.

Market Outlook and Strategy

With the Brexit can kicked further down the road, the situation continues to develop with constantly possible outcomes in the balance so the portfolio managers will continue to watch closely to see how the situation evolves; although it's worth reiterating that as we proceed towards the conclusion of the process up to 12th April, the market fundamentals which tend to drive the ABS market are now a lot stronger than they were during the global financial crisis and the 1989-1993 recession. Additionally the performance of the underlying pools of assets within ABS transactions are equally at their strongest since the financial crisis.

The portfolio managers will continue to maintain a diversified portfolio with high liquidity, ready to react to any developments. Despite the favourable tailwinds witnessed in Q1, the funds will continue to believe that maintaining a skew to lower duration is key to minimizing any potential future volatility.

On the positive side it has been encouraging to see further primary deals announced in UK, Irish and Dutch Mortgages, CMBS, SME lending and the first STS labeled deal plus a rumoured large Dutch STS RMBS in the pipeline, which will all likely see good levels of demand from the market.

In secondary markets, market interest is still largely focussed on the shorter end of the duration curve in both RMBS and CLOs and this is likely to continue in the foreseeable future. In the latter, the spread curve versus duration is steeper versus the start of the year, and so it will be interesting to see if recent deals point to a revival of interest at the longer end of the curve which could be seen to be materialising supported by spread moves.

Further Information and Literature:
TwentyFour Asset Management LLP. Telephone: 020 7015 8900 Email: sales@twentyfouram.com

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Fund Managers


Robert Ford
Partner, Portfolio Manager, industry experience since 1986.


Ben Hayward
Partner, Portfolio Manager, industry experience since 1998.


Aza Teeuwen
Partner, Portfolio Manager, industry experience since 2007.


Douglas Charleston
Partner, Portfolio Manager, industry experience since 2006.


John Lawler
Portfolio Manager, industry experience since 1987.


Luca Beldi
Portfolio Manager, industry experience since 2013.

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

TwentyFour AM
John Magrath
Tel. 020 7015 8912
john.magrath@twentyfouram.com

Numis Securities
Chris Gook
Tel. 020 7260 1378
c.gook@numis.com

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