TwentyFour ASSET MANAGEMENT

TwentyFour Income Fund

Monthly Commentary | 31 May 2019

Market Commentary

Trade wars were the main drivers of market sentiment this month. The increasing friction between the US and China led risk assets to underperform with most equity markets posting their first negative month since December last year. Trade disputes were not confined to China, as President Trump turned his attention to Mexico and threatened a 5% tariff on goods which added to the already deteriorating global growth expectations and increased concerns of a US recession. The expectations of a cut from the Fed increased significantly over the course of the month; the market was pricing in around a 50% chance of a 2019 cut at the start of May, but by the end of the month this expectation had reached almost 95%.

Italy was back in focus with tensions flaring not only with the EU, but also within the fragile coalition government. The EU Commission sent a formal letter to the government stating that Italy could face disciplinary action unless it takes steps to reduce its deficit.

In the UK, Prime Minister May announced her resignation after the proposal for a vote on her revised deal was rejected by MPs and calls from her own party intensified for her to step down. The new prime minister is expected to be in place by the time that Parliament goes into summer recess (usually at the end of the 3rd week of July).

In the European ABS market fairly light supply in Primary issuance at the beginning of the month lent technical support to the market, with spreads continuing to grind tighter across most asset classes albeit at a slower pace. As the month progressed the market saw multiple new issues being announced culminating in what was the busiest two weeks of the year in ABS markets taking YTD supply to Eur33billion, although this is still 25% lower than up to the same period last year. This has subsequently seen a couple of ABS research desks revise their full year issuance forecasts slightly lower. The momentum in STS issuance continued with several deals pricing and the market also saw SONIA deals pricing from BTL RMBS transactions which indicates that SONIA is gaining acceptance as the alternative reference rate to LIBOR.

Throughout the month the tone of the market was positive despite the risk-off tone in wider credit markets and although there was more supply, the levels of oversubscription and pricing being at the tighter end of the range suggests that the supply is not sufficient to fill investor demand. Secondary activity remained fairly quiet at the start of the month with fairly balanced flows and spread levels remained broadly unchanged. However supply picked up steadily as the month progressed and we started to see a little weakness seep into the ABS market, as broader volatility and wider Crossover and Main Indices started to feed into dealer pricing at the end of the month.

Primary CLO issuance was slower over the month compared to April and although CLO spreads continued to lag the Credit and Loan market overall year to date performance, particularly in the AAA and mezzanine space, remained positive. Some of the focus on primary deals was at the shorter end as we see a pick-up in CLO refinancing deals and we continue to see a steeper tiering on a spread basis develop between manager, maturity and tranche rating. Demand for secondary CLOs remained robust, with offers hard to come by away from dealer inventory and although BWIC activity picked up execution remained strong especially at the short end of the curve.

Portfolio Commentary

May was a busy month for the portfolio managers following the successful capital raise of approximately GBP 80mm. Positions were added in UK Prime, NC and BTL RMBS senior and mezzanine bonds, Prime mezzanine RMBS from Netherlands and European CMBS. The fund also added mezzanine shorter maturity secondary CLO positions from preferred managers, adding incremental yield. Purchases were funded mainly from inflows into the fund and selective short dated sales. Secondary liquidity observed in the market and provided by dealers was strong as the market remained in a risk-on mode until the last few trading sessions despite a progressively weakening macro and wider market backdrop. Fundamental performance across all asset classes remains strong and the portfolio managers continue to be comfortable with the current balanced positioning including a strong liquidity profile. The Fund returned 0.63% for the month with 3yr volatility at 3.35%.

Market Outlook and Strategy

With continued macro volatility in the very latter part of the month the secondary market has lost some momentum. Spread levels moved tighter initially and held in reasonably well in the last week but the tone is becoming more cautious, which is understandable given the wider market backdrop. While there seems to be consensus that a reduced supply outlook in H2 should be supportive for spreads, this is being weighed up against risk-off moves in other markets and the result is that spreads are likely to trade sideways in the interim until there is a bit more conviction away from ABS markets.

It is worth noting that while paper might clear wider in secondary markets, primary markets will probably continue to see ongoing demand at the tighter end of pricing ranges and the market will see strong customer interest at wider secondary levels which presents an interesting dynamic to source cheaper bonds than in Primary . Looking forward we think that we will see some near to mid-term tightening when there's a little more balance in the supply demand picture, in particular as the final deals are closed ahead of the annual ABS market conference in June. The portfolio managers have the flexibility and liquidity to react to any further market weakness.

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 and Literature: TwentyFour Asset Management LLP
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Further information on fund charges and costs are included on our website at www.twentyfouram.com