Structured Finance Investing in Mutual Funds

Introduction to the Fund

The Fund offers retail investors access to a distinctive fixed income strategy, previously available only through a private limited partnership[1] but **recently converted into this mutual fund.**

Investment Objective

The investment objective of the Fund is to seek total return with an emphasis on providing current income to its shareholders.

Investment Strategy and Process

The Fund's portfolio managers will select securities they believe are undervalued, demonstrate attractive risk/reward profiles, and aim to provide investors a consistent return in various interest rate environments. Braddock performs an extensive bottom-up analysis of the market and evaluates the following variables in assessing each potential position.

- Deal structure and asset credit support
- Quality of the collateral that underlies the security
- Diversification across collateral characteristics
- Capital appreciation opportunity
- Duration risk
- Market liquidity

The Fund focuses on securities that will achieve the target of a short duration and low interest rate risk profile by investing primarily in floating rate securities. Additionally, the Fund invests predominantly in non-investment grade securities that aim to provide a higher level of income relative to broader fixed income markets, while remaining relatively liquid, within a market of investors such as insurance companies, institutional investors and pension plans. Braddock maintains relationships with institutional broker-dealers that have top tier access to and competitive pricing for these securities.

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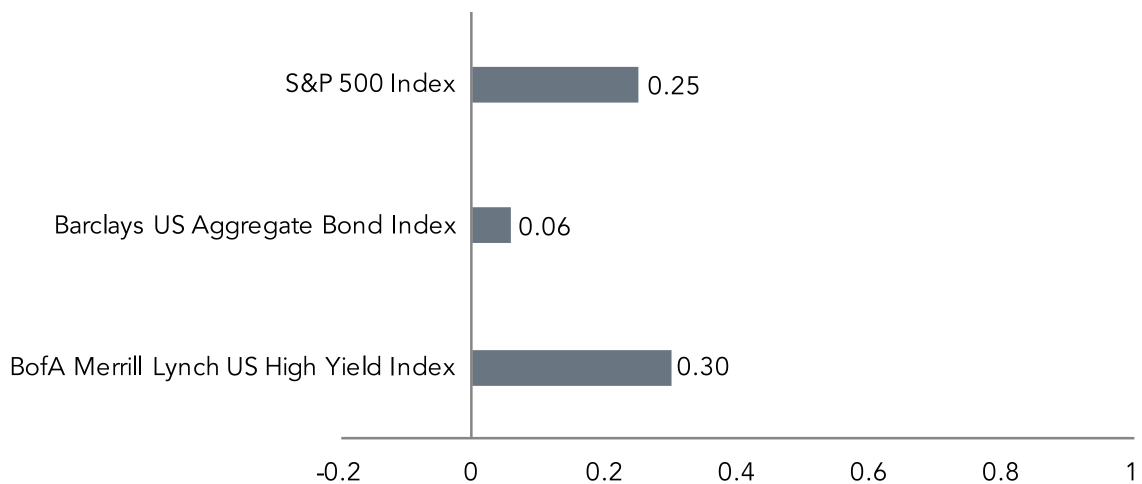
[1] *The Fund commenced investment operations on December 31, 2015, after the conversion of a limited partnership Account, Braddock Structured Opportunities Fund Series A, L.P., which commenced operations on 7/31/2009, (the "Predecessor Account"), into shares of the Fund's Institutional Class.*

Structured Finance: A Distinctive Fixed Income Strategy

- Structured finance is composed of asset classes traditionally accessed by institutional investors (insurance companies, pension funds and financial institutions) as well as hedge fund managers. Investors have long been attracted to structured finance securities due to their variety of targeted yield and maturity profiles versus less complex traditional fixed income asset classes.
- Securities in these market sectors exhibit a wide variety of coupon, yield and duration opportunities. This offers the potential for a higher yielding shorter duration strategy than offered by traditional fixed income asset classes.
- The skill sets required for structured finance investing limits the sector to a smaller group of experienced investors relative to other market sectors.
- Historically, Braddock's strategy of investing in structured finance has generated low volatility and low correlation when compared to high yield bonds, broad market investment grade bonds and equities.

Exhibit 1: Fund Correlation to Market Indices
Inception to 12/31/16



<u>Economic Environment Supportive for Many Structured Finance Sectors</u>

During the past five years, the U.S. economy and the ability of borrowers to perform on their debt obligations has steadily improved, benefitting many structured finance securities. Consistent increases in employment have helped both consumer incomes and consumer confidence. Additionally, consumers are currently enjoying the rewards from falling energy prices through lower driving, heating, cooling and overall utility costs. Finally, a strengthening U.S. Dollar has made

import purchases more affordable. Thus far, these consumer savings have largely been utilized by consumers to pay down their debt, improving their creditworthiness. In the future, consumers may use cost savings toward more consumption as well as paying down debt, further benefitting the economy.

The U.S. housing market has exhibited a dramatic turnaround from the difficult conditions experienced in the immediate aftermath of the 2007/2008 financial crisis. The national real estate downturn that began in 2007 was quite unusual from an historical perspective. Since that time, home prices have appreciated significantly, and the risk profile of housing has fallen. After a number of years of outsized home price gains, price gains are now normalizing to historical averages in the low-to-mid single digits. Notably, housing markets have returned to traditional risk characteristics where regional economic performance dictates housing performance. Existing home sales have returned to normal levels of approximately 5 million units per year. Mortgage applications for the purchase of homes are increasing from the depressed levels that characterized credit from 2010 to 2014. Finally, pent-up housing demand is expected to support long term growth as the middle class homebuyer gains access to mortgages at more normalized, historical levels.

These improved housing market factors, combined with strengthened consumer balance sheets and conservative loan underwriting standards, point to positive fundamentals and collateral performance for the pools securing many asset backed debt securities.

The Braddock Advantage

Braddock has extensive structured finance and residential real estate experience, having managed a number of investment vehicles since the firm's inception in 1994. The Fund offers retail investors access to an alternative fixed income class, previously available only through a private limited partnership, which seeks to target total returns with an emphasis on providing current income. Braddock employs a disciplined and research-intensive bottom up investment strategy dedicated to finding undervalued securities that can provide alpha to its shareholders. This bottom up process utilizes extensive loan-level analysis on the underlying collateral to identify attractive income and capital appreciation opportunities in this current challenging yield environment.

Braddock's private fund experience and skill set demonstrates the ability to manage market volatility and to target absolute returns regardless of interest rate environment.

- 20 years of firm experience managing structured credit private funds
- Braddock's Portfolio Management team has worked together for over 10 years

Introduction to Structured Finance Markets

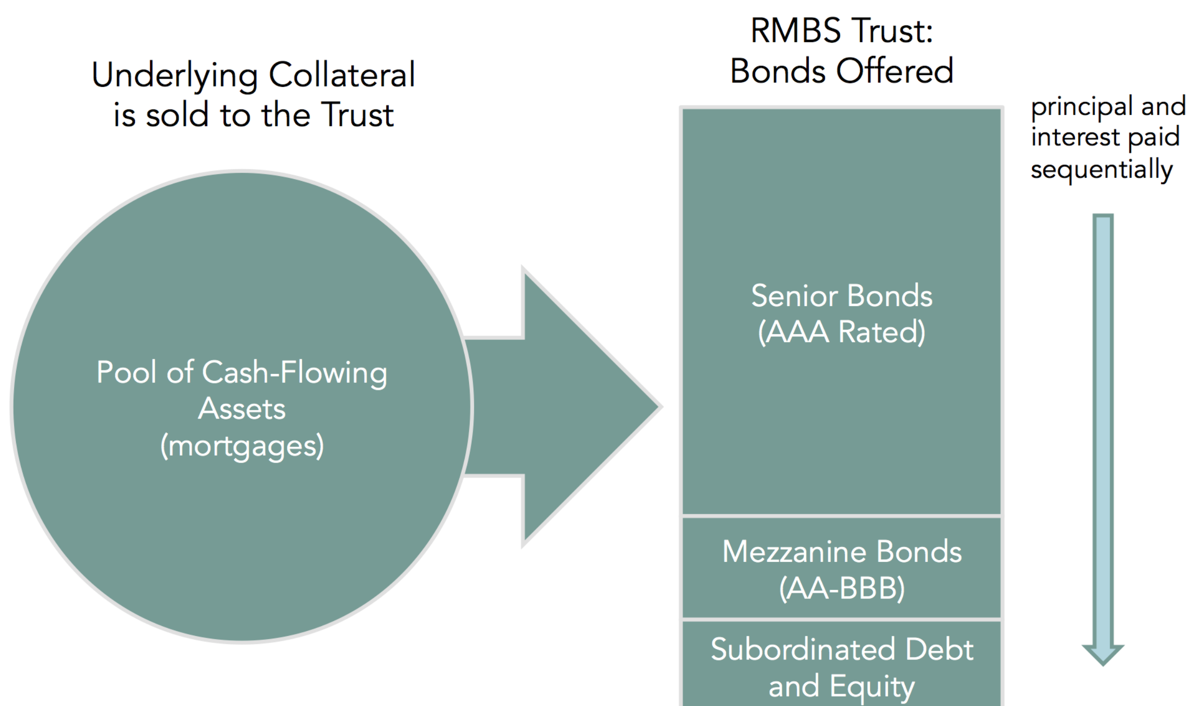
The structured finance markets consist of over $1 trillion of asset backed debt securities. These fixed income products, commonly referred to as bonds, are created through securitization. Securitization

is the process of creating diversified, liquid and tradeable debt securities with targeted cash flows from a large group of less diversified and less liquid assets.

The structured finance markets, and securitization, began in the 1970s and have grown into a trillion dollar industry. Businesses use securitization to realize the value of cash-producing assets, while institutional investors use securitization to buy financial assets that meet their specific investment needs. For example, insurance companies employ asset/liability management. Here an insurer purchases an investment grade 10-year fixed rate bond to match a 10-year liability created by its policies.

Securitization is widely used in the U.S. mortgage markets. In a mortgage-backed security, a loan originator sells mortgages, such as a pool of first lien mortgages, to a Trust (Exhibit 2). The Trust is a legal entity whereby the assets (mortgages) are held for the benefit of investors (the purchasers of the bonds). The bonds issued through the Trust are backed by the cash flow of the pooled mortgages. These bonds are typically referred to as Residential Mortgage Backed Securities (RMBS).

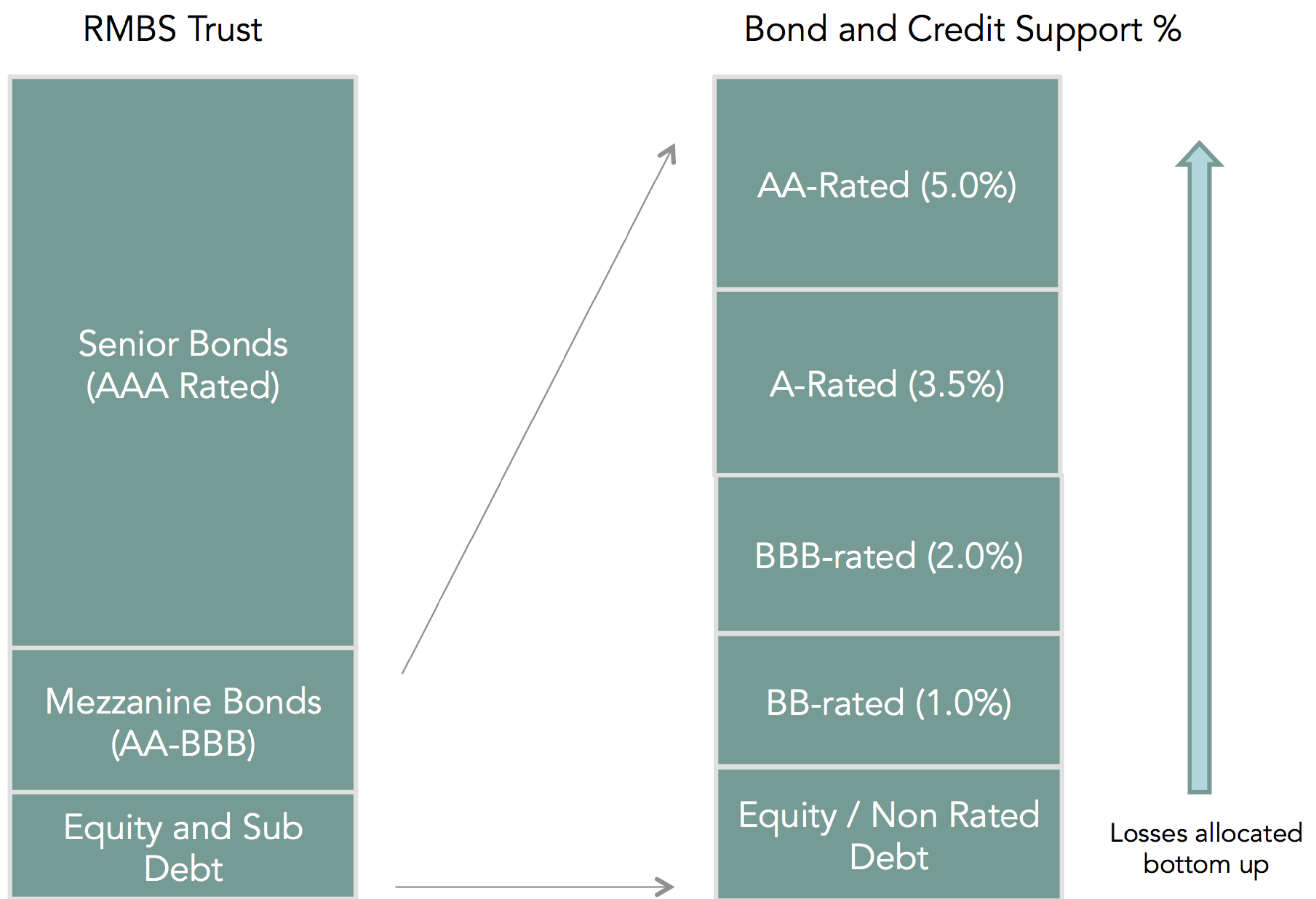
Exhibit 2: Securitization Process



The purchasers of asset-backed debt securities typically enjoy the benefits of diversification by geographic location, by borrower, and by loan originator. Also, the structure of a Trust creates bonds with differing levels of credit risk. The principal of bonds with higher levels of "credit support" is more secure than the bonds below it. Credit support refers to the percentage of the Trust below a specific bond (Exhibit 3). Loan losses over the life of the Trust will have to be above

that percentage before the specific bond takes a dollar of principal loss. As all losses related to defaulting loans are allocated in a bottom-up manner, the BBB bond in the example has 2% of protection. The Equity will take the first 1% of loan losses and the BB bond will take the next 1% before the BBB would experience any amount of principal write down.

Exhibit 3: Credit Support



In addition to residential mortgages, asset-backed debt securities are also issued where the collateral is commercial real estate loans, senior secured bank loans, credit card and business receivables, student loans, automobile loans, and personal and consumer loans.

Attractiveness of the Structured Finance Markets

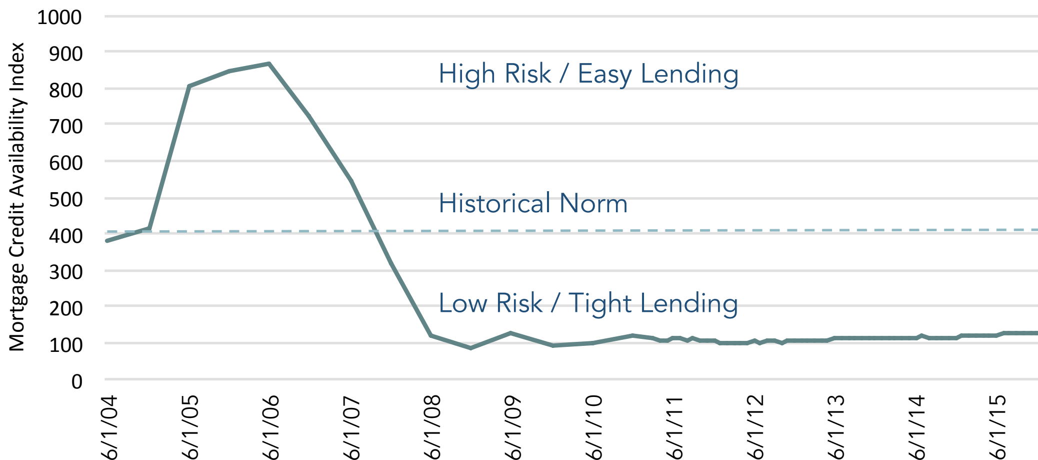
Since the financial crisis of 2008, the structured finance industry has made significant improvements to the most crucial aspects of its products: loan quality and Trust structure. The industry is also poised to capitalize on an improving US economy and housing market.

Loan Quality – Newly Originated Loans

Concerning loan quality, the risky "affordability" mortgage products of the pre-crisis era are gone. High loan-to-value ratio (95%-105%) mortgages, where the borrower's had high debt to income ratios (45%-55%), and in which their income and employment was "Stated" vs "Verified" are no longer offered to consumers. Today's standard mortgages have loan-to-values (LTVs) in 70%-80% range, leading to a much less leveraged borrower. Additionally, today's borrowers have much higher credit quality and financial standing. For instance, credit scores are typically in the 700+ range, debt-to-income ratios in the 35% area and their employment and income are fully documented.

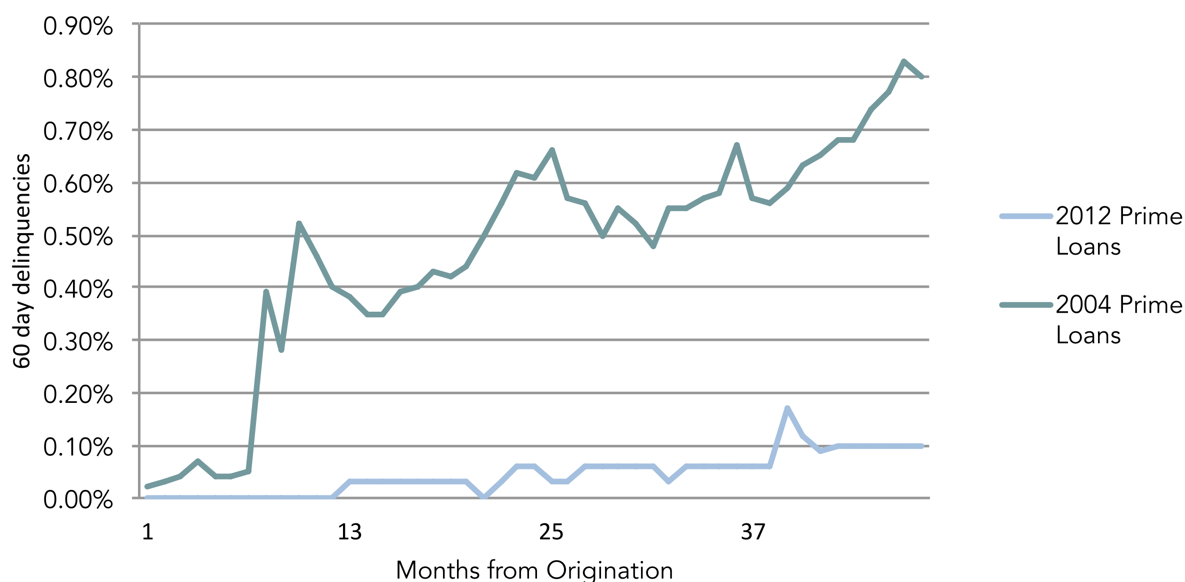
The Mortgage Bankers Association's Mortgage Credit Availability Index (Exhibit 4) demonstrates how underwriting quality fell dramatically (a higher index) in the early 2000s but now reflects today's very tight underwriting standards (higher quality equals a lower index).

Exhibit 4: Mortgage Credit Availability Index



Source: Mortgage Bankers Association; Powered By AllRegs Market Clarity
Date prior to 3/31/2011 was generated using data measured at 6-month intervals

As a result, recent vintage loans have exhibited excellent credit performance when compared even to loans that were originated in earlier times of conservative underwriting (Exhibit 5). After 48 months of loan seasoning, mortgages made to high quality borrowers (Prime quality) in 2004 had a delinquency rate nearing 1%, while the 2012 vintage has shown only 1/10 of 1% in delinquency.



Loan Quality – Pre-Crisis Originated Loans

For all of the reasons mentioned in the economic environment portion of this paper, the amount of credit risk in pre-crisis loan pools has fallen dramatically since 2009. Market participants often refer to "credit burnout" in the legacy Trusts. Credit burnout implies that the remaining loans in a Trust have become very predictable in their future performance. Most pre-crisis borrowers who qualified for a new loan (a refinance) have prepaid out of the Trusts while most of the poor credits were liquidated from the Trust during the great recession. The remaining loans in the collateral pools prepay at low annual rates and many delinquent loans ultimately perform as a result of a loan modification or improving economic conditions.

Trust Structure

Today's structured finance products have more robust capital structures than their pre-crisis cohorts. This change was driven by investors, regulators, and the credit rating agencies (e.g. Moodys, S&P). Consequently, post-crisis bonds are more protected from loan defaults. Most often, the change is apparent in the credit support of the bond (Exhibit 3 above). Additional protection may be provided by other structural features included in the Trust documents.

RMBS Prime Trusts issued post crisis have seen the AAA rated bond's credit support increased by 60% and the BBB rated bond's credit support has doubled. In the CLO sector, both the AAA-rated and BBB-rated bond's credit support increased by 40% post-crisis. This change to CLO structure by

the credit rating agencies was surprising given that none of the investment grade pre-crisis CLO bonds experienced any principal losses.

The most important takeaway to today's structures is that the loan originator, the equity holder of the Trust, has more "skin in the game" as they have more to lose from poor credit performance of the underlying loans.

Types of Asset Backed Debt Securities

Residential Mortgage Backed Securities

Although the Fund's allocation will be among various assets classes in the asset-backed debt securities market, the Fund's investments are expected to focus on residential mortgage-related securities. Residential mortgage loans, a type of RMBS collateral, are generally classified into three categories based on the risk profile of the borrower and the property: Prime, Alternative-A, and Subprime. Additional RMBS products include trusts backed by non-performing mortgages, re-performing mortgage loans and loans secured by single family rental properties.

Collateralized Loan Obligations

CLOs are a type of asset-backed debt security collateralized by a pool of senior secured bank loans that are diversified by both industry and issuer. The collateral pools contain loans that are predominately in a first lien position, and have low exposure to corporate credit risk rated below B-. A CLO has a series of cash flow bonds, called tranches, which vary in yield and credit quality. The Fund may only invest up to 15% of net assets in these securities. Similar to post-crisis RMBS, post-crisis CLOs have increased structural protection against loan defaults.

Asset – Backed Securities

ABS are income generating securities backed by consumer and commercial receivables, such as auto loans, equipment leases or other receivables. These securities contain a revolving pool of quality assets with shorter term, fixed payments that can provide the Fund with high levels of income along with short duration exposure.

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RISKS AND OTHER DISCLOSURES:

Before investing you should carefully consider the Braddock Multi-Strategy Income Fund's investment objectives, risks, charges and expenses. This and other information about the Fund is in the prospectus and summary prospectus, a copy of which may be obtained by calling 800-207-7108 or by visiting the Fund's website at www.libertystreetfunds.com. Please read the Fund's prospectus or summary prospectus carefully before investing.

An investment in the Braddock Multi-Strategy Income Fund is subject to risk, including the possible loss of principal amount invested and including, but not limited to, the following risks, which are more fully described in the prospectus: **Mortgage-backed securities:** subject to "prepayment risk" (the risk that borrowers will repay a loan more quickly in periods of falling interest rates) and "extension risk" (the risk that borrowers will repay a loan more slowly in periods of rising interest rates). If the Fund invests in mortgage-backed or asset-backed debt securities that are subordinated to other interests in the same pool, the Fund may received payments only after the pool's obligations to other investors have been satisfied. The risk of defaults is generally higher in the case of mortgage pools that include so-called "subprime" mortgages. **Real estate risk:** property values may fall due to increasing vacancies or declining rents resulting from unanticipated economic, legal, employment, cultural or technological developments. **CLO risk:** Collateralized Loan Obligations (CLOs) largely depend on the type of underlying collateral securities and the tranche in which the Fund invests. While CLOs are subject to the typical risks associated with debt instruments (i.e., interest rate risk and credit risk), the Fund is also subject to asset manager, legal and regulatory, limited recourse, liquidity, redemption, and reinvestment risks as a result of the structure of CLOs in which the Fund may invest. **Credit Risk:** securities held by the Fund could be subject to credit risk, including factors that may impair the credit rating which may cause the value of the Fund's investment to decline. **Interest rate risk:** is the possibility that your investment may go down in value when interest rates rise, because when interest rates rise, the prices of bonds and fixed rate loans fall. Generally, the longer the maturity of a bond or fixed rate loan, the more sensitive it is to this risk. Falling interest rates also create the potential for a decline in the Fund's income. These risks are greater during periods of rising inflation. **High Yield ("Junk") bond risk:** junk bonds are speculative investments that involve greater risk of default, downgrade, or price declines, more volatile and tend to be less liquid than investment-grade securities. **Repurchase agreement risk:** may be viewed as loans made by the Fund which are collateralized by the securities subject to repurchase. The Fund's investment in repurchase agreements may be subject to market and credit risk with respect to the collateral securing the repurchase agreements. **Reverse repurchase agreement risk:** reverse repurchases provide the Fund with cash for investment purposes, which creates leverage and subjects the Fund to the risks of leverage. Reverse repurchase agreements also involve the risk that the other party may fail to return the securities in a timely manner or at all. **Liquidity risk:** the Fund may not be able to sell some or all of the investments that it holds due to a lack of demand in the marketplace or other factors such as market turmoil. The sales price the Fund could receive for any particular portfolio investment may differ from the Fund's valuation of the investment, particularly for securities that trade in thin or volatile markets or that are valued by the Fund using a fair value methodology due to the fact that illiquid assets may be difficult to value. **Leverage risk:** as a result of borrowing or other investment techniques the Fund may be leveraged. Leverage creates

exposure to gains and losses in a greater amount than the dollar amount made in an investment. **Derivatives risk:** derivative instruments, futures contracts, options, swap agreements, and/or selling securities short involve risks different from direct investment in the underlying assets, including but not limited to: futures contracts may cause the value of the Fund's shares to be more volatile; the Fund may not fully benefit from or may lose money on option or shorting strategies; swaps may be leveraged, are subject to counterparty risk and may be difficult to value or liquidate. **Non-diversification risk:** as a non-diversified fund, the Fund may focus its assets in the securities of fewer issuers, which exposes the Fund to greater market risk than if its assets were diversified among a greater number of issuers.

Diversification does not assure a profit or protect against a loss. The Fund may not be suitable for all investors. We encourage you to consult with appropriate tax and financial professionals before considering an investment in the Fund.

The views in this material are intended to assist readers in understanding certain investment methodology and do not constitute investment advice. The views in the material were those of the author as of the date of publication and may not reflect its views on the date this material is first disseminated or any time thereafter.

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