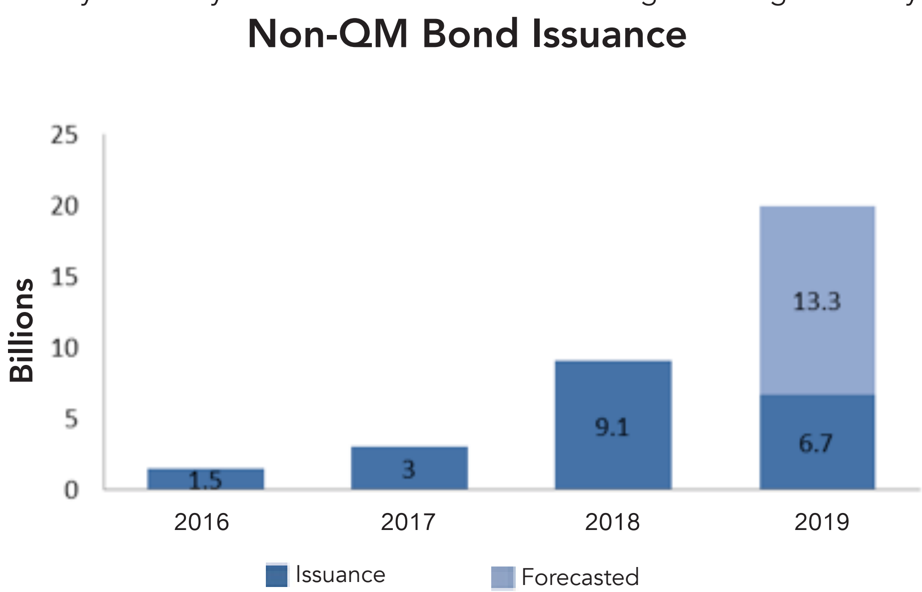
BRADDOCK INSIGHTS: RMBS OPPORTUNITY - NON-QUALIFIED MORTGAGE TRUSTS

Braddock believes that institutional investors and investment bankers will view the 2013-2020 time frame as the beginning of a long and healthy period of issuance in the Modern Residential Mortgage Backed Securities (RMBS)[1] market. Modern RMBS consists of all credit sensitive RMBS issued in 2013 or later. This market is characterized by a wide variety of securities that touch many aspects of the U.S. housing and mortgage industries. Both the underlying collateral and the structural design of these securities have benefited from the many lessons learned from the financial crisis over a decade ago. Regulations established post financial crisis across the mortgage finance industry should ensure that Modern RMBS products provide institutional investors, like the Braddock Multi-Strategy Income Fund, with robust assets that satisfy their portfolio's risk and return objectives.

A GROWING SECTOR OF MODERN RMBS

Non-Qualified Mortgage bonds are a growing sector in the Modern RMBS markets. These securities came to market in 2016 as a vehicle to finance mortgages to credit worthy borrowers who fall outside the criteria for a "Qualified or Conforming Mortgage."

The yearly issuance of Non-Qualified Mortgage bonds is forecasted to more than double in 2019 versus 2018. Today's Non-Qualified Mortgages (Non-QM) are primarily issued by non-bank lenders who are taking advantage of today's strict mortgage underwriting standards to issue loans to borrowers who may not qualify for a Qualified Mortgage[2] due to their non-standard income documentation or credit history. Many lenders have been very pleased by both the performance and pricing of Non-QM loans. In today's lending environment, high prepayment rates (as displayed on the next page) and low loan delinquencies have promoted low credit risk while the relatively higher mortgage rates compared to Qualified Mortgages have kept loan pricing attractive. As such, this asset class has grown significantly as it continues to attract "smart money"[3] players in the financial and mortgage industry. The issuers of Non-QM bonds include Real Estate Investment Trusts (REITs) (Starwood Colony, New Residential, etc.), large asset managers (WAMCO, Angel Oak, etc.), and hedge funds (Lone Star, Ellington, Oaktree, etc.).



Source: Bloomberg, Deutsche Bank. Data as of April 2019

A crucial aspect of the Non-QM RMBS sector is the risk retention by the issuer of the debt. U.S. regulations related to the Dodd-Frank Act[4] require the issuers to retain 5% of the bonds originated in the Non-QM RMBS Trust. This "skin in the game" provides a level of exposure to Non-QM Trusts performance that did not exist prior to the financial crisis.

[1] RMBS are a debt based security (similar to a bond), backed by the principal and interest paid on loans for residences. Modern RMBS are bonds that are backed by the principal and interest paid on loans for residences issued after 2012.

[2] Page 4 details the history of Qualified and Non-Qualified Mortgages

[3] Investors with deep knowledge.

[4] Dodd-Frank Wall Street Reform and Consumer Protection Act

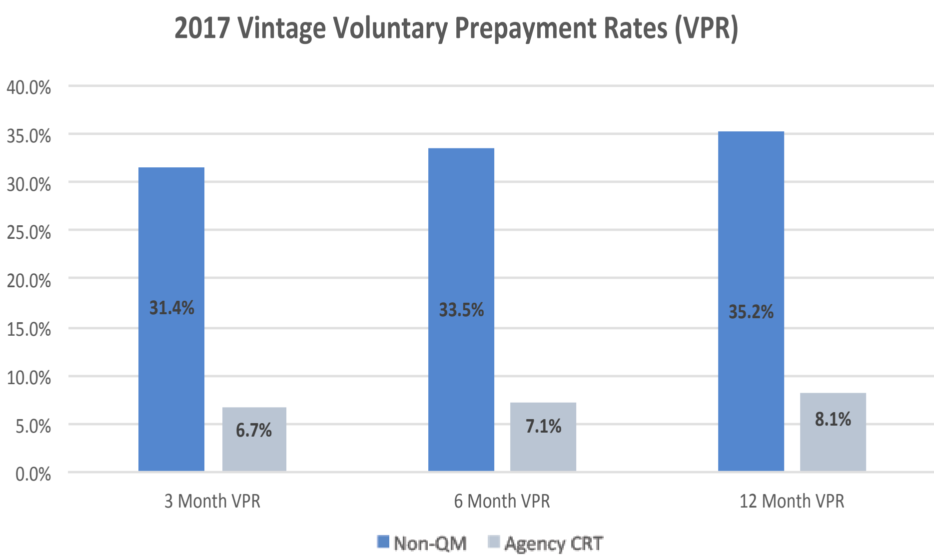
The table below compares the loan pool of conforming mortgages (which are the collateral in Fannie Mae and Freddie Mac's Credit Risk Transfer bonds) to a pool of Non-QM loans. These weighted average characteristics are from Trusts originated from 1/1/2018 to 5/30/2019.

Loan Pool Characteristics	Conforming[5]	Non-QM
Mortgage Rate	4.0-5.0%	6.5-7.0%
Loan to Value[6]	70-75%	67-78%
FICO Score	745-750	700-735
Debt-to-Income	35-38%	35-38%

Source: Bloomberg, Braddock Financial.

A quick review of the data below demonstrates how recent loan performance has validated the value of investing in the Non-QM sector.

ATTRACTIVE LOAN PERFORMANCE – HIGH PREPAYMENT RATES



Source: Bloomberg; Data as of April 2019

In today's mortgage lending environment, the mortgage rates on Non-QM loans are higher than those of conforming mortgages and, as a result, many borrowers use these loans as "bridge loans" until they can qualify for a cheaper mortgage. This translates into high mortgage prepayment rates. We welcome high prepayment rates because they lower the credit risk in an RMBS Trust by reducing the number of loans outstanding in the collateral pool.

Another positive of high prepayments is that they often trigger the bond rating agency covering the Trust to review the bonds for a potential upgrade. This typically occurs as the Trust reaches two years of seasoning.

ATTRACTIVE LOAN PERFORMANCE – LOW DEFAULT RATES

The value of full documentation mortgage underwriting cannot be understated. Although Non-QM loans do have higher credit risk than conforming or prime mortgages, the delinquency and default rates are low from a historical perspective. When we reviewed the 27,000 outstanding Non-QM loans[7] in our loan level database[8], we observed an average delinquency rate of only 1.17% and total losses to date of less than two basis points! As these loans age, we forecast loan losses in the 1.5-3.5% range. Most importantly, the Non-QM Trust structure has provided adequate levels of credit enhancement[9] to the BB and investment grade bonds to help protect the principal of these bonds in various economic environments.

[5]This loan pool characteristics are from the mortgages that are the collateral in the issued STACR 2018/2019–DNA Trusts.

[6]Loan to Value is an assessment that financial institutions and other lenders examine before approving a mortgage. Typically, assessments with high LTV ratios are higher risk and, therefore, if the mortgage is approved, the loan costs the borrower more.

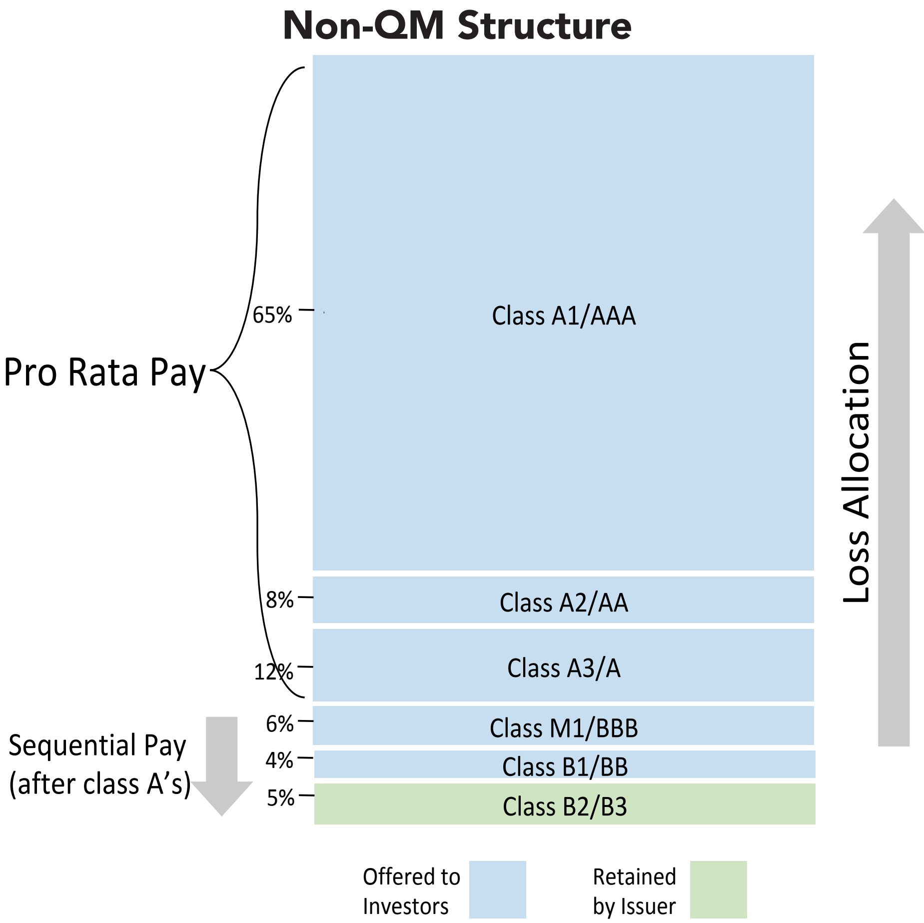
[7]These 27,000 loans are the collateral from 37 Non-QM RMBS Trusts originated from 2016 to 2019. Braddock estimates this represents over 75% of the outstanding loans that are collateral in Non-QM Trusts. This does not include loans made to investment properties. As of 5/25/2019.

[8]Moody's analytics - Mortgage loan database.

[9]Credit Enhancement is defined as the amount of the structure (typically in percentage) below a bond which is available to absorb credit losses before the mentioned bond would take a loss to its principal. Some RMBS and ABS structures also have credit enhancement in the form of excess interest and reserve accounts.

NON-QUALIFIED MORTGAGE TRUSTS: UNIQUE STRUCTURAL CHARACTERISTICS

We are attracted to many of the structural aspects of Non-QM trusts. The structural design takes into account the shorter average life of these loans due to high prepayment rates versus traditional thirty year fixed rate loans. Therefore, the Class A securities are paid in a pro-rata format to provide the AAA rated bond buyer with a bond long enough to meet its investment criteria (typically a bond with a weighted average life of 2-4yrs). Each Non-QM Trust is typically rated by one to three Nationally Recognized Statistical Rating Organizations. These include: Fitch, S&P, Moody's, DBRS, Kroll and Morningstar. After the Class A securities, which represent 85% of the Trust, are paid down, the remaining structure pays sequentially. The structure also incorporates delinquency and loss triggers that when triggered (failing) change the structure to strictly sequential to help protect the AAA and AA rated bonds. In this situation, the outstanding Class A1 bond (AAA rated) would receive all monthly principal collections and be the first bond to reach its maturity (versus being paid down at the same rate as the Class A2 and A3 bonds).



Similar to all Modern RMBS products, loan losses are allocated up from the bottom of the structure. Non-QM bonds are provided some protection by the excess interest collected in the Trust. Excess interest represents the monthly "extra" interest collected from the borrowers that is not needed to pay the monthly interest on the issued bonds. More simply put, if the borrowers were paying 7% interest on the pool of mortgages, the Trust may only be paying 4% interest to the issued debt. This creates 3% of excess interest available to cover any current or previous losses to the debt.

Another notable structural aspect is the early redemption language. The standard redemption language in RMBS Trusts is a "clean-up call"[10] when only 10% of the initial loans remain outstanding in the Trust. However in Non-QM Trusts, the issuer typically uses a 20% or 30% clean up call and also builds in an optional redemption two years into the deal's life. This gives the issuer optionality to manage their cost of funds (their borrower rate) in the rapidly growing Non-QM sector. At times, investors may also seek to defend themselves by limiting the extension risk in the Non-QM sector. To do this, the Class A borrowers request a "step-up" (a feature that allows for rate increases at periodic intervals) in the bond's coupons if the deal is not redeemed at a certain point in

[10] A clean up call is a protective call feature found in a private label RMBS (which includes Modern RMBS). Typically, a clean up call is executed when the loan servicer is not collecting enough loan servicing revenue due to the small remaining size of the deal. The deal is called and the loans are sold in the whole loan market.

time. For example, three or four years after issuance, the bond coupons are increased by 100 basis points, which encourages the issuer to call the deal (redeem the bonds). If they do not, the bond buyers capture an increase in yield to compensate for this extension in the bond's weighted average life.

NON-QM: RISK FACTORS AND CREDIT PERFORMANCE

Like traditional Non-Agency RMBS products, the ultimate performance of the securities is related to the amount of defaults in each deal's static pool of mortgages. While these transactions do not have as strong of a Representation and Warranty (R&W) language as Credit Risk Transfer (CRT) and Prime RMBS Trusts, we believe the combination of well underwritten mortgages and the attractive Non-QM Trust structure adequately compensate us for this difference in R&W risk.

Housing fundamentals are currently very positive given the combination of high quality mortgage underwriting, a shortage of entry level homes, and increasing home demand from the millennial generation. Regardless, risks do remain from potential changes in the growth rate of the U.S. economy and/or exogenous risks, such as national disasters, that may negatively affect mortgage default rates.

CONCLUSION

Non-QM securities provide an opportunity for institutional investors, like Braddock, to invest in bonds backed by strong borrowers who are relatively unserved in today's housing finance industry. We believe Non-QM securities create attractive investment opportunities from both an absolute and relative value to investors. At Braddock, we continually utilize our RMBS knowledge to identify the bond in each Non-QM transaction that is most appropriate from a risk/return basis to the Braddock Multi-Strategy Income Fund.

THE HISTORY BEHIND QUALIFIED AND NON-QUALIFIED MORTGAGES

In response to the 2008 housing crisis, President Obama signed the Dodd-Frank Wall Street Reform and Consumer Protection Act. This led to the creation of the Consumer Financial Protection Bureau which was tasked with the creation of the Qualified Mortgage (QM) rule[11]. The purpose of the rule is to standardize the characteristics and process for mortgage lenders to make "a reasonable, good faith determination" of a borrower's ability to repay the proposed loan. The most common examples of Qualified Mortgages are "prime" mortgage loans and agency conforming mortgages (loans held by the U.S.'s Government Sponsored Entities: Fannie Mae & Freddie Mac).

Source: Braddock Financial.

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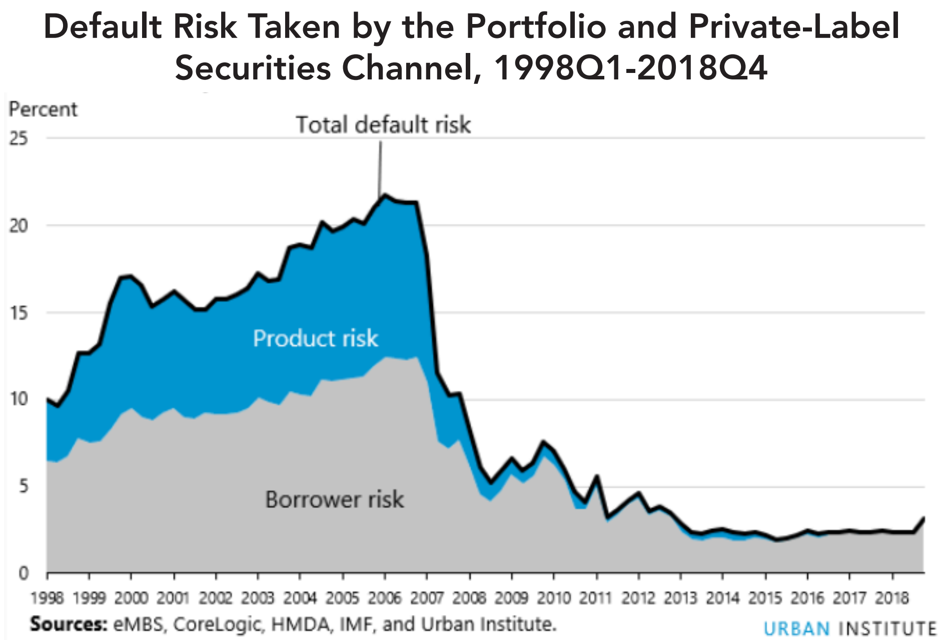
[11]The Consumer Financial Protection Bureau's Qualified Mortgage (QM) rule effective 1/10/14 was designed to protect borrowers to ensure they don't pay excessive points and fees on their mortgage, and that ultimately, they have the ability to repay their mortgage.

QUALIFIED MORTGAGES

Qualified Mortgages have a number of requirements: for instance, the loan cannot have a negative amortization, interest-only payment or balloon payment features, and total points and fees cannot exceed 3% of the loan amount. Additionally, the loan must determine the borrower's debt and income using the documentation standards outlined in Appendix Q of Regulation Z of the Truth in Lending Act.

NON-QUALIFIED MORTGAGES



Non-Qualified Mortgages have a different risk profile than QM loans but they are still underwritten to loan origination guidelines that are much stricter today than in periods prior to the financial crisis. These loans are required to follow the same mortgage regulations that QM loans follow. These include the Truth in Lending Act's disclosure rules and the "ability to repay" rule. According to Non-QM lender Angel Oak Capital Advisors, the two most common reasons that a loan is designated a Non-QM loan are the documentation method of the borrower's income and the points and fees charged on the loan[12]. The Urban Institutes's Housing Credit Availability Index graphically shows the significantly lower risk in today's private label RMBS securities, which includes Modern RMBS Trusts backed by Non-QM and Prime mortgages.

WHO ARE NON-QUALIFIED BORROWERS?

Similar to many clients of financial advisors, typical Non-QM borrowers are business owners with good credit scores, high incomes, and significant savings. Due to the structure of their business or the source of their income, these borrowers utilize 12 or 24 months of bank statements to verify income instead of a W-2. Other reasons a borrower may have utilized a Non-QM loan include the desire for an Interest Only loan, his or her citizenship, debt-to-income ratio, or credit history.

We can observe that Non-QM loans are similar to the Alt-A loans that were originated before the financial crisis. Unlike Alt-A loans, Non-QM loans now require extensive verification and do not allow borrowers to simply "state their income." Also unlike 2006/2007 Alt-A loans where the borrower's combined Loan-to-Value ratio was around 95%, today's Non-QM borrowers have combined Loan-to-Value ratios in the 70-80% range. This is very important as it conveys the significant amount of equity the borrower has in the home. The higher the equity in the home, the lower the chance of default on a mortgage loan.

[12]Q&A: Non-QM Securitization Market Outlook: Angel Oak Capital Advisors 1Q 2018.

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 Fund involves risk. Loss of principal is possible. The following is a summary of the risks and are more fully described in the Fund's prospectus: **Mortgage-backed securities:** subject to prepayment risk (loan repaid more quickly), "extension risk" (loan repaid more slowly), credit risk, liquidity, and default risks. **Real estate risk:** property values may fall due to various economic factors. **CLO risk:** Collateralized Loan Obligations (CLOs) are subject to interest rate, credit, asset manager, legal, regulatory, limited recourse, liquidity, redemption, and reinvestment risks. **Credit Risk:** factors may impair the credit rating of the securities held by the Fund which may cause the Fund's value to decline. **Interest rate risk:** investment value may go down when interest rates rise. 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:** involve greater risk of default, downgrade, or price declines, can be more volatile and tend to be less liquid than investment-grade securities. **Repurchase agreement risk:** repurchase agreements may be subject to market and credit risk with respect to the collateral securing the repurchase agreements. **Reverse repurchase agreement risk**: subjects the Fund to the risks of leverage and counterparty risk. **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. **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 (e.g. short sells, options, futures) involve risks different from direct investment in the underlying assets, including possible losses in excess of amount invested or any gain in portfolio positions. **Non-diversification risk:** 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. The Fund may not be suitable for all investors. We encourage you to consult with appropriate financial professionals before considering an investment in the Fund.

Basis points: one hundredth of one percent, used chiefly in expressing differences of interest rates

The views in this material are intended to assist readers in understanding certain investment methodology and do not constitute investment or tax advice. The views in this material were those of the Fund's Sub-advisor as of the date of publication and may not reflect its views on the date this material is first published or any time thereafter.

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