BRADDOCK MULTI-STRATEGY INCOME FUND

BRADDOCK INSIGHTS: RMBS OPPORTUNITY – AGENCY CREDIT RISK TRANSFER SECURITIES

Modern RMBS, defined by Braddock as credit sensitive Residential Mortgage Backed Securities (RMBS) issued in 2013 or later, has now surpassed outstanding Legacy RMBS (bonds issued before 2008) from an outstanding balance standpoint. 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 benefit from the many lessons learned from the financial crisis over a decade ago. Many sectors of Modern RMBS have continued to benefit from today's responsible lending standards and the more disciplined regulatory environment stemming from the post-crisis Dodd-Frank Act.

Credit Risk Transfer bonds (CRTs) are an example of a Modern RMBS product. These securities came to market in 2013 as a vehicle to transfer some of the residential mortgage credit risk from the government-sponsored entities (GSEs: Fannie Mae & Freddie Mac) to institutional investors.

The Federal Housing Finance Agency (FHFA) has instructed the GSEs to transfer a portion of their credit risk on 90% of their single-family mortgage loan acquisitions. The CRT program is the primary financial vehicle utilized to fulfill this mandate while a large portion of the remainder is done through mortgage insurance/reinsurance transactions.

CRT bonds issued by the GSEs have emerged as one of the primary avenues for institutional investors to access high quality, prime mortgage credit. The bonds' well-designed and standardized structures, combined with strong credit and market price performance, have resulted in deep market liquidity across the sector. Braddock continues to believe CRTs offer attractive value, allowing investors to pursue their risk and return objectives.

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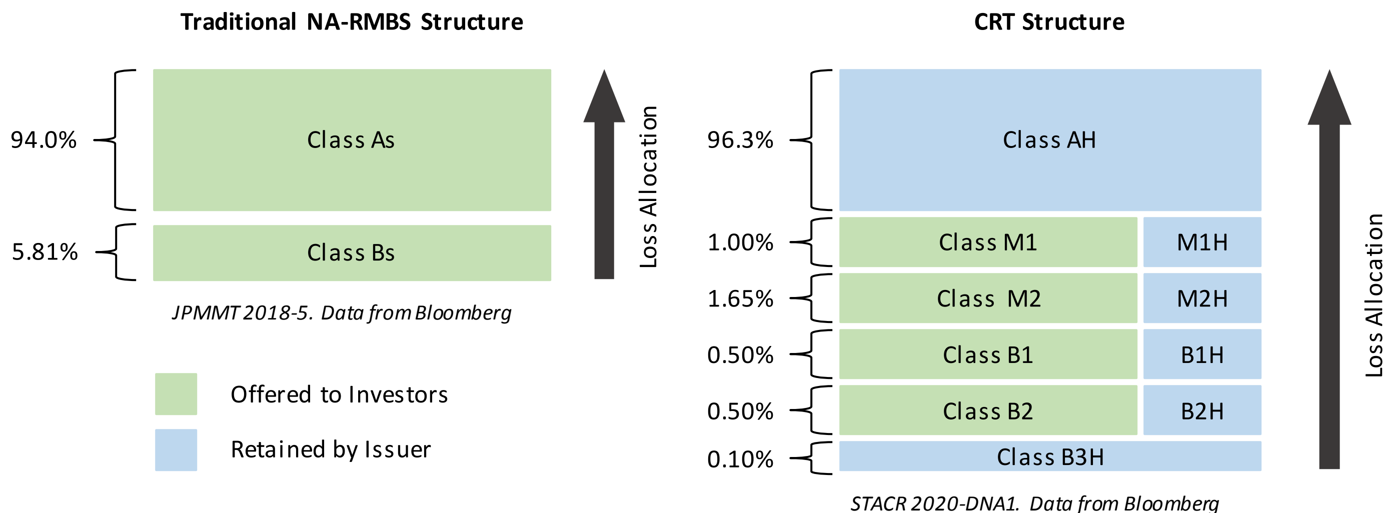
Credit Risk Transfer Highlights
• High quality mortgages have benefited from new regulations and stringent underwriting
• Life-to-date performance has led to significant credit rating upgrades without any downgrades
• Unique combination of floating rate bonds and fixed rate mortgages
• Transparent market with primary dealers providing daily liquidity
• Range of risk-return profiles available from rated mezzanine to unrated subordinate bonds

CRT: UNIQUE STRUCTURAL CHARACTERISTICS

We, at Braddock, are impressed with many of the structural aspects of CRT securities. CRT bonds are backed by the same "GSE conforming" mortgages[1] that are collateral for traditional Agency Mortgage Backed Securities (MBS). However, the typical MBS bond is paid a fixed rate coupon and the GSE assumes the credit risk of any defaulting mortgages. Therefore, the MBS investor only takes interest rate risk of the underlying pool of mortgages.

Conversely, CRT bonds pay an uncapped floating coupon that resets monthly. This creates a bond where investors bear some of the credit risk, while mitigating the interest rate risk of the underlying loans. Braddock believes this unique combination of fixed rate mortgages with floating rate bonds is particularly attractive and may provide upside optionality to rising rates in today's low rate environment.

Another unique characteristic is that Credit Risk Transfer securities allow the issuer to retain the vast majority of the bonds (mortgage exposure) on their balance sheet. The issuer is simply looking to share its credit risk and can do this by offering only Mezzanine (Class M1 & M2) and Subordinate bonds (Class B1 & B2) to the market as seen in the charts below. This is different from traditional Non-Agency RMBS where the issuer sells Senior (Class As), Mezzanine (Class Ms or Class Bs) and Subordinate bonds (Class Bs) in order to reduce the amount of assets on its balance sheet. This "skin in the game" feature of CRTs helps align the interests of the GSEs and investors. For comparison, Legacy RMBS (issued pre-2008) did not require any issuer risk retention.



CRT: MORTGAGE CHARACTERISTICS

We believe the quality of these GSE mortgages is very impressive. Most importantly, the underwriting and loan origination process ensures that proper disclosures are made to borrowers, that the borrower is financially capable of repaying the loan, and that the probability of mortgage fraud is very low.[2] Additionally, the lenders make loan level Representations and Warranties (R&W) that allow the GSE to remove loans from the collateral pool in the future should it be proven that the loan did not truly meet the underwriting standards.

[1] A conforming loan is a mortgage loan that conforms to GSE (Fannie Mae and Freddie Mac) origination guidelines.
[2] Improved underwriting standards were partially a result of "TRID – Integrated Disclosure Rule", the "Truth In Lending Act", and "Ability To Repay" regulation.

CRT mortgages are made to borrowers who historically demonstrate low default risk. These borrowers have average FICO scores near 750, debt-to-income ratios average mid-30%, and the borrower's income and employment are verified. These fully documented loans are 100% 30-year fixed rate mortgages and, as such, the borrower will not face an increasing mortgage payment should interest rates increase.

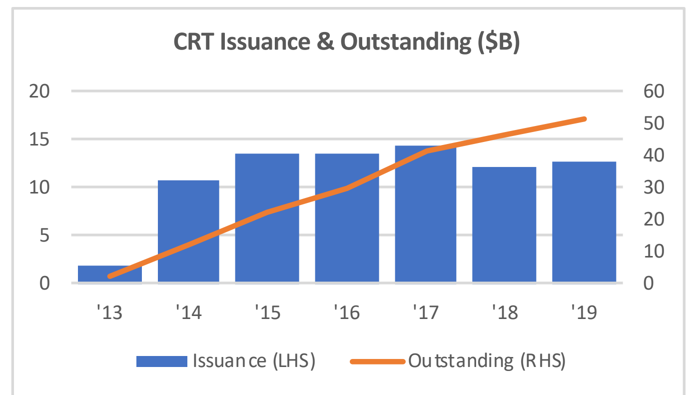
How is this different from 2005-2007? Pre-financial crisis, many GSE mortgages were higher risk affordability products like Interest-Only loans and often underwritten using low documentation methods (such as stated income/stated assets). Also, the typical Legacy RMBS borrower was a higher credit risk (lower FICO credit score) than the typical borrower today.

Improved Loan Characteristics	Freddie Mac 2005 Vintage	STACR 2020-DNA1
Average FICO	724	752
Average Debt-to-Income	37%	36%
Borrowers with DTI >50%	16%	0%

Source: Freddie Mac, Barclays. As of 1/22/2020

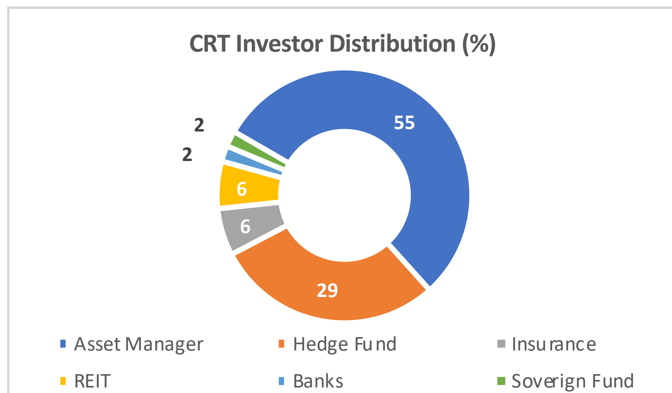
CRT: MARKET DYNAMICS

Fannie Mae issues Connecticut Avenue Securities (CAS) while Freddie Mac issues Structured Agency Credit Risk (STACR) securities. Since the inaugural CRT transaction in 2013, the sector has grown rapidly with 2019 issuance of $12.5 billion bringing total value of CRT bonds outstanding to $51 billion.[3] We expect further growth, driven by strong mortgage origination activity in 2019.



Source: JP Morgan. As of 1/10/2020

Based on our 20+ years of investing in RMBS markets, we are most impressed with the depth of the investor base and the liquidity benefits this provides.



Source: Freddie Mac. As of 8/31/2019

Fannie Mae's and Freddie Mac's CRT programs now have over 200 unique investors, with approximately 40-70 unique investors in each deal. Mutual funds, banks and insurance companies comprise the majority of demand. Hedge funds tend to invest in riskier CRT bonds near the bottom of the capital structure. Secondary liquidity is supported by 8-10 primary broker/dealers that provide daily two-way markets[4] and FINRA TRACE trade reporting ensures pricing transparency for investors. Trailing 12-month trading volumes are approximately $60 billion and sector-wide CRT turnover is approximately 1.1x.[5] By comparison, investment grade corporate credit has a turnover ratio of 0.7x and high yield bonds are at 1.1x.[6]

CRT: 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. 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 natural disasters, that may negatively affect mortgage default rates.

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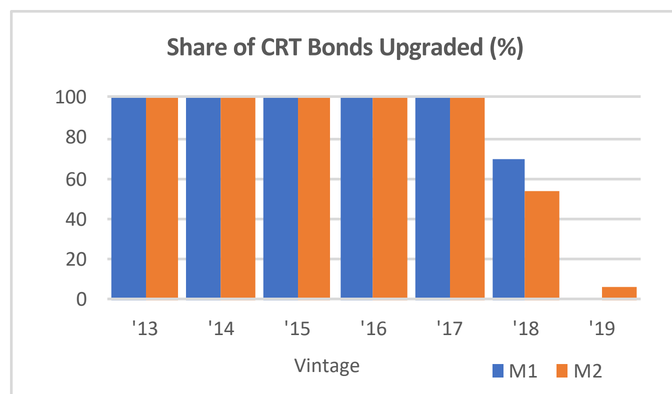
[3] JP Morgan. As of 1/10/2020
[4] Fannie Mae and Freddie Mac. As of 1/22/2020
[5] Fannie Mae and Freddie Mac. As of 9/30/2019
[6] MarketAxess. As of 12/31/2019

Credit performance across the CRT bonds originated from 2013 to today have reflected both the quality of the loan underwriting and strength in the U.S. housing market. Severe delinquency rates average less than 0.30%, annualized. Defaults have averaged just 0.01% annually and the recovery rates on defaulted loans have averaged 83%.[7] The rating agencies have taken notice and as such have upgraded 160 CRT bonds, including 56 previously rated high yield bonds that were upgraded to investment grade. Since the inception of the CRT program, 82% of M1 bonds and 78% of M2 bonds have now been upgraded! No CRT bonds have been downgraded.[8]



Source: S&P, Moody's, Fitch, KBRA and Morningstar/DBRS. As of 1/31/2020

CONCLUSION

CRT securities provide investors an avenue to participate in the credit side of the GSE mortgage book while also benefiting from a floating rate bond that is backed by a pool of fixed rate mortgages. We believe CRT securities create attractive investment opportunities from both an absolute and relative value perspective. At Braddock, we continually utilize our RMBS expertise to identify the bond in each CRT transaction that is most appropriate from a risk/return basis for the Fund.

[7] Moody's Analytics. As of 12/31/2019

[8] S&P, Moody's, Fitch, KBRA and Morningstar/DBRS. As of 1/31/2020

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 receive 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 and which may cause the value of the Fund's investment to decline. **Interest rate risk:** 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 which involve greater risk of default, downgrade, or price declines, can be more volatile and tend to be less liquid that 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 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 that if its assets were diversified among a greater number of issuers. The Fund may not be suitable for all investors.

The views in this material are intended to assist readers in understanding certain investment methodology and do not constitute investment. 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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