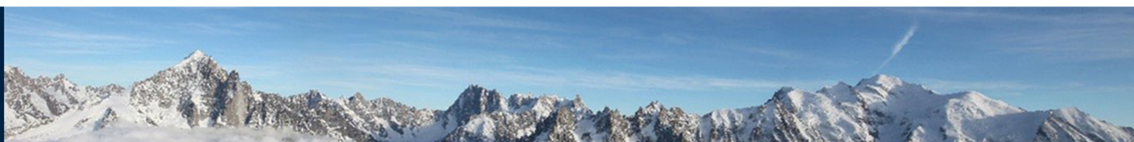
Algebris INVESTMENTS



Algebris Financial Income Fund (UCITS)

I EUR (Accumulating)

December 2018

Terms

Size (€): 472m

Fund Inception: 13 August 2013

Fund Domicile: Ireland

Fund Base Currency: EUR

Dealing Frequency: Daily

ISIN: IE00BCZNWT08

Management Fee: 0.9%

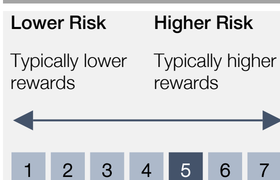
Incentive Fee: 0%

Fund Objective

The Algebris Financial Income Fund can invest in the capital structure of financial companies globally, in both equities and fixed income. The objective of the Fund is to maximise income and generate superior risk adjusted returns over an investment cycle by investing in high dividend yielding stocks and bonds. The Fund invests in equities and subordinated debt capital instruments of financial institutions globally, including hybrid capital instruments, preference shares and contingent convertible bonds (CoCos), with fixed and variable interest rates, which may be rated investment grade or below investment grade.

Investment in the Fund may be suitable for investors with a medium to long term investment horizon.

Risk Profile



1 2 3 4 **5** 6 7

Note: The synthetic risk and reward indicator (SRRI) is based on the historical data and may not be a reliable indication for the future. It is calculated using the volatility of the Fund's weekly performance over a five-year period. A score of 5 means the Fund's historic volatility is between 10% and 15%.

Fund Information

No. of Bonds/ No. of Issuers	74/33
No. of Stocks	45
Effective Duration of Bond Allocation	4.3 yrs
Avg. Rating of Bond Allocation	BB+
Bonds: Yield to Worst (Gross)	6.7%
Equity: Dividend Yield (Gross)	5.2%
Fund: Yield (Gross)	6.8%

Note: Fund gross yield reflects current yield for the bonds and dividend yield for the equities in the portfolio. The Avg. Credit Rating is calculated using the average of the top two credit ratings from S&P, Fitch and Moody's and includes all rated bonds and cash.
Source: Bloomberg LP, Algebris (UK) Limited

Performance Analytics

Return Since Inception	20.6%
Annualised Return	3.6%
Annualised Volatility	10.2%
Sharpe Ratio	0.4
2018 Annual Distribution	4.1%

Note: Figures are based on returns for the I EUR (Accumulating) share class, net of management fees and operating expenses and excluding ADL (Anti-Dilution Levy – currently 25bps). The actual price at which an investor subscribes or redeems shares depends on the ADL applied on the relevant dealing day. Further information is contained in the Prospectus. Past performance is not a guarantee of future results.
Annual Distribution refers to the equivalent distributing share class (Id EUR).
Share class inception date: 9 October 2013
Source: HSBC Securities Services (Ireland) DAC, Morningstar

Performance History (Net) % - I EUR (Accumulating)

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Year
2013										3.89	2.05	2.29	8.45
2014	0.45	2.86	1.28	-0.31	0.45	0.32	-0.29	1.19	-1.16	0.46	1.53	-0.69	6.20
2015	0.80	4.44	1.88	1.04	1.11	-1.92	1.52	-3.29	-4.35	3.06	1.01	-2.43	2.51
2016	-6.79	-2.84	3.04	2.99	1.90	-8.03	5.84	3.25	-1.76	4.86	1.44	3.32	6.26
2017	1.44	1.05	3.16	2.28	-0.20	1.83	2.05	-1.46	3.48	0.75	0.08	1.17	16.68
2018	4.71	-2.26	-3.08	1.57	-5.01	-1.27	4.00	-4.10	1.07	-5.41	-2.31	-6.37	-17.61

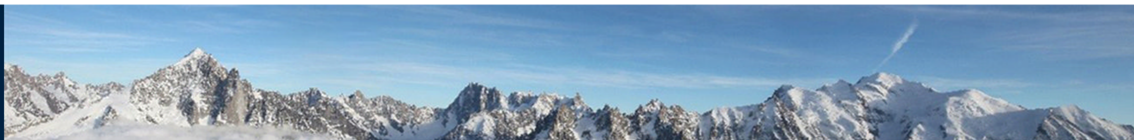
Note: Returns are net of management fees and operating expenses but exclude ADL (Anti-Dilution Levy – Currently 25bps). The actual price at which an investor subscribes or redeems shares depends on the ADL applied on the relevant dealing day. Further information is contained in the Prospectus. Prices are published daily on Bloomberg. Past performance is not a guarantee of future results.
Source: HSBC Securities Services (Ireland) DAC, Morningstar

Commentary

- Markets fell substantially in December and took a sharply negative view on the outlook for the financial sector. There is no shortage of alleged culprits for the sector's underperformance: flattening yield curve, rising recession fears, ending QE, pricing out of rate hikes, unwinding positions, etc. Whatever the cause, the effect was for one of the worst months in the history of US banks, with regional banks down over 16% for the month. In fact, December was the third worst month since 2006 after the Jan '09 debacle of -29% and the worst month of 2008 (June: -19%). Last month handily eclipsed the oil/high yield carnage of Jan '16 (-13%) and the US downgrade month of Aug 2011 (-12%). Needless to say, those were pretty dark days for US banks. Important also to say, each of those down months were followed by positive returns in the next 3 months, on average +18%. Over 6 months, +17% (and this includes the financial crisis…)
- Meanwhile, today, fundamentals are unquestionably strong and valuations are at or below previous trough levels. We have seen loan growth accelerating higher (+9% y/y from +3% just in September). The Fed hiked in December, providing a tailwind for 2019 earnings (and importantly, consensus for earnings at some of our bank longs are already below company guidance even assuming no further hikes this year). As we discussed last month, bank earnings growth is defensible even without a hawkish Fed as buybacks and cost programs overwhelm any modest hits from a slower hiking trajectory. In fact, bank stocks in our portfolio have an average of ~75% of their EPS growth through 2020 derived from buybacks alone. Cheap stocks with self-help levers have a large margin of safety built in and a shift in sentiment alone can see a swift repricing even as investors grasp for catalysts.
- And if we have a recession? Consensus already has provisions up >75% from current levels in 2020, but if we shock it another 50% and assume net interest income is flat from 2018 (a draconian scenario unless loan growth goes negative or the Fed cuts very soon, both highly unlikely), then the average bank stock in our portfolio would trade at a still very undemanding 9.9x earnings. So even on a stressed basis, banks trade below their average post-crisis multiple of 12x. The story is similar in life insurance – assuming a 25% equity market hit, 100 bps decline in rates, and a halving of buybacks, the sector is trading on just over 8x earnings, which compares to the 15 year average P/E of 10x! Looking back at prior recessions, bank stocks in the US fell 38% peak-to-trough in 1990 and -29% in 2000, which compares to the 32% decline in 2018. Valuations are where they bottomed at in the 2001 recession – and payout yields are indeed much higher, having reached 11% on average for the US banks.
- Continental European banks fell double digit, to hit the lows of March 2009. Recapitalised, volumes growing again, provisions falling…and we are only two years into an earnings upgrade cycle (having just finished 10-years of downgrades due to zero interest rates, capital raises, GFC provisions etc). Provisions falling and the end of most of the large restructuring programs are now strong positives. Equity raises in 2018 were the lowest in 2-decades at only $1.3bn (2017: ~$40 bn). Dividend yields are at 7%, which is both the highest they have been in 30 years and substantially higher than the 4% 3-decade average.
- As we look at Europe, positive loan growth only got going in 2017, after a decade of de-leveraging, so there is little to fear from credit bubbles in bank balance sheets. Continuing positive data on unemployment and real estate prices has started to lead a recovery in the balance sheet quality and P&L dynamics. Even Italian banks have reduced problem loans by 40% over the last couple of years, in what for most people believe has been a challenging environment. This is continuing. Earnings and dividends are going up, not down. The overriding drags on the sector (deleveraging, restructuring costs, capital increases, increasing provisions, falling interest rates) have almost totally been stopped, which should lead to a jump in actual profits being earned – and those are the earnings that dividends are paid from. It would seem that this month we are shouting very loudly about the opportunity from both sides of the Atlantic Ocean.
- In summary, December was a painful mark to market and we underestimated the timing and extent of this selloff (our hedges were significant but clearly not sufficient). But we have been here before. Making money in this sector is and always has been about understanding risk/reward and placing your bets when it's asymmetric in your favor. We believe right now is just such an opportunity, perhaps even more so than early 2016 given lower earnings multiples (8x vs 9x), an objectively better economic and regulatory backdrop, and massive capital return support.

Contact Details

Call: +44 (0) 203 196 2450
Email: algebrisIR@algebris.com
Visit: www.algebris.com



Algebris Financial Income Fund (UCITS)

I EUR (Accumulating)

December 2018

Commentary - continued

- Meanwhile, performance in the credit space was broadly negative for the month. HY closed down -2.2% in US and -0.4% in Europe. In early December, a European Court of Justice ruling that Article 50 can be unilaterally revoked was positive for UK names. This dramatically reduces the probability of a Brexit with no deal in place on March 29. While it doesn't solve the lack of a consensus on the shape of Brexit, it does increase the probability of an extension over a "hard" Brexit outcome. A number of regulatory tailwinds for the financial sector materialised from the EU Council/Parliament in the month. A change in capital treatment for banks undertaking large NPL disposals is particularly positive for Italian banks, and should lead to some CET1 relief. Also a broader definition of Available Distributable Items ('ADI') has been accepted, which would be supportive to German and Austrian AT1 coupon payments. This has been an area of focus for DB AT1s since their first issue.
- As we have previously highlighted, the redemptions of legacy tier 1s and first cohort of AT1s leaves the technical picture stronger than some commentary would suggest. December 2018 saw the redemption of ~$8.5bn securities with a further ~$4bn of redemptions expected to be announced in January. Combined with coupon payments of ~$11bn in 2019, we expect investors to eventually appreciate that the market is more balanced than feared, with redemptions and coupons offsetting potential new issue. While 2018 was a difficult year for financial hybrids as we enter 2019 we are very optimistic. Spreads across our portfolio are roughly double the level they were at in December 2017, setting the fund up for strong performance in 2019.

Top 5 Equity Holdings

Rank	Issuer name
1	Banco de Sabadell
2	Blackstone
3	Prudential Financial
4	Assicurazioni Generali
5	Comerica

Source: Algebris (UK) Limited

Top 5 Bond Holdings

Rank	Issuer name
1	Unicredit
2	Santander
3	Intesa Sanpaolo
4	CaixaBank
5	Société Générale

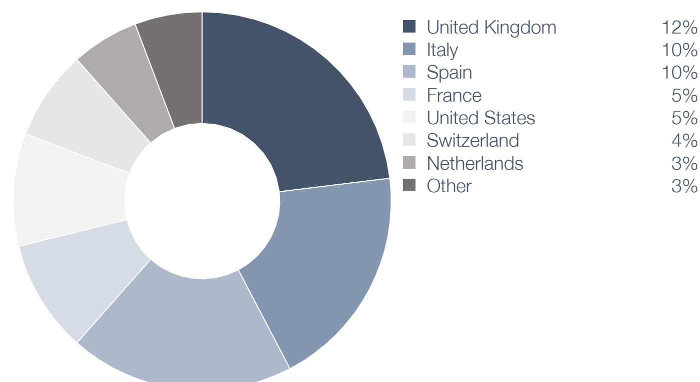
Source: Algebris (UK) Limited

Asset Allocation

	Allocation
Equity	62.7%
Bonds	52.8%
Hedges (delta)	-5.4%

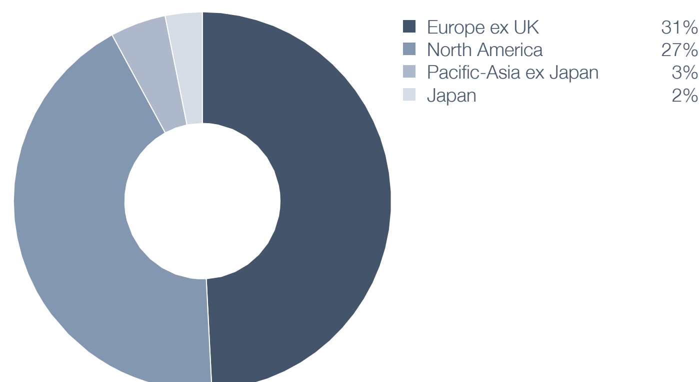
Exposure calculated on a delta adjusted basis for option positions and on a full notional basis for all other instruments. Excludes bond futures used for hedging duration.
Source: Algebris (UK) Limited

Bonds - Exposure by Country



Exposure includes long bond holdings.
Source: Algebris (UK) Limited

Equities - Exposure by Region



Exposure includes long equity holdings.
Source: Algebris (UK) Limited

About Algebris

Algebris (UK) Limited is a global investment manager with a historical focus on the financial sector across the capital structure. Founded in 2006, Algebris has gradually expanded its expertise and entered the global credit and Italian securities space to capture a broader set of value opportunities. Algebris has a team of 26 investment professionals and manages EUR 10.5bn AUM (inclusive of committed capital), split between credit and equity investments (data as of 31.12.2018).

Algebris (UK) Limited is authorised and regulated by the Financial Conduct Authority. Algebris Investments (US) Inc is a SEC registered Investment Adviser. Algebris Investments (Asia) Pte Ltd is a Licensed Fund Management Company with the MAS.

Contact Details

London
Algebris (UK) Limited
4th Floor,
1 St James's Market
London SW1Y 4AH

Singapore
Algebris Investments
(Asia) Pte. Ltd
9 Straits View, #05-08
Marina One West Tower
Singapore 018937

Boston
Algebris Investments (US) Inc.
699 Boylston Street
Boston MA 02116
United States of America

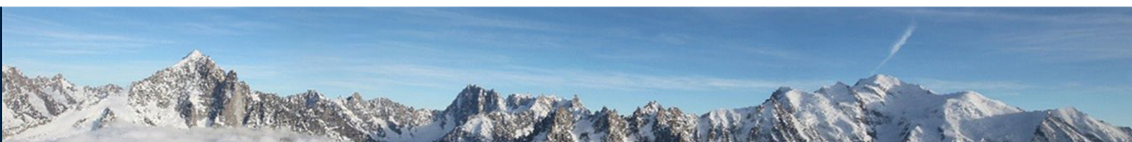
Milan
Algebris (UK) Limited -
Milan Branch
Via Fatebenefratelli 10
20121 Milano, Italy

Luxembourg
Algebris Investments
(Luxembourg) S.a.r.l.
40 Avenue Monterey
L-2163 Luxembourg

Tokyo
Algebris Investments K.K.
JA Building 12F, 1-3-1
Otemachi, Chiyoda-ku
Tokyo 100-0004 Japan

Tel: +44 (0) 203 196 2450
Email: algebrisIR@algebris.com
Visit: www.algebris.com

Algebris INVESTMENTS



Algebris Financial Income Fund (UCITS)

I EUR (Accumulating) **December 2018**

Fund Details

Share Classes			Identifiers	
Class	Currency	Minimum Initial Investment	ISIN	BBG ticker
I	EUR	€500,000	IE00BCZNWT08	AFIIEUR ID
	GBP	GBP equivalent of €500,000	IE00BCZNWW37	AFCIIGB ID
	USD	USD equivalent of €500,000	IE00BCZNWX44	AFCIIUS ID
	CHF	CHF equivalent of €500,000	IE00BCZNWV20	ALGFIIC ID
	SGD	SGD equivalent of €500,000	IE00BYYJYN11	ALGFIIS ID
	JPY	JPY equivalent of €500,000	IE00BD71WT90	ALGFIIJ ID
Id	EUR	€500,000	IE00BCZNWY50	AFIIDEU ID
	GBP	GBP equivalent of €500,000	IE00BCZNX087	AFCIDGBP ID
	USD	USD equivalent of €500,000	IE00BCZQ7R24	AFCIDUS ID
	CHF	CHF equivalent of €500,000	IE00BCZNWZ67	AFCIDCH ID
	SGD	SGD equivalent of €500,000	IE00BYYJYP35	ALGFIDS ID
	JPY	JPY equivalent of €500,000	IE00BD71WV13	ALFIIDJ ID
R	EUR	€10,000	IE00BCZQ7T48	AFIREUR ID
	GBP	GBP equivalent of €10,000	IE00BCZNX194	AFCIRGB ID
	USD	USD equivalent of €10,000	IE00BCZNXN11	AFIRUSD ID
	CHF	CHF equivalent of €10,000	IE00BCZQ7S31	AFIRCHF ID
	SGD	SGD equivalent of €10,000	IE00BYYJYJ74	AFIRSGD ID
	JPY	JPY equivalent of €10,000	IE00BD71WW20	ALGFIRJ ID
Rd	EUR	€10,000	IE00BCZNX202	AFCIRDE ID
	GBP	GBP equivalent of €10,000	IE00BCZNX319	AFCIRDG ID
	USD	USD equivalent of €10,000	IE00BCZNX426	AFCRDUD ID
	CHF	CHF equivalent of €10,000	IE00BD3D0179	AFCRDCH ID
	SGD	SGD equivalent of €10,000	IE00BYYJYM04	AFIRRDS ID
	JPY	JPY equivalent of €10,000	IE00BD71WX37	ALFIRDJ ID

Private & Confidential

This document has been prepared and is issued by Algebris (UK) Limited (the "Firm") who is the Investment Manager to the Algebris Financial Income Fund. The Firm is authorised and regulated by the Financial Conduct Authority. This document and information included herein is intended for information purposes only.

This document is intended for persons to whom it may lawfully be issued under The Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 including persons who are authorised under the Financial Services and Markets Act 2000 of the United Kingdom (the "Act"), certain persons having professional experience in matters relating to investments, high net worth companies, high net worth unincorporated associations and partnerships, trustees of high value trusts and persons who qualify as certified sophisticated investors.

This document is exempt from the prohibition in Section 21 of the Act on the communication by persons not authorised under the Act of invitations or inducements to engage in investment activity on the ground that it is being issued only to such types of person. Investing in financial markets and securities involves risk. Past performance is not a guarantee of future results. Investment losses may occur from time to time and investors could lose some or all of their investment.

This information is not intended to provide, and should not be relied upon for, accounting, legal or tax advice or investment recommendations. This document does not constitute or form part of any offer to issue or sell, or any solicitation of an offer to subscribe or purchase any investment nor shall it or the fact of its distribution form the basis of, or be relied on, in connection with, any contract therefore.

You should consult your tax, legal, accounting or other advisors about the issues discussed herein. A potential investor expressing an interest to invest in the fund will be provided with an offering memorandum and subscription agreement (together, the "Fund Documents") for the investment and an opportunity to review the documentation relating to the investment. Prospective investors must review the Fund Documents, including the risk factors, before making a decision to invest and should rely only on the information contained in the Fund Documents in making their investment decision and where necessary consult an advisor.

No representation, warranty or undertaking, express or implied, is given as to the accuracy or completeness of the information or opinions contained in this document by any of Algebris (UK) Limited, its directors or employees and no liability is accepted by such persons for the accuracy or completeness of any such information or opinions.

Distribution of this information to any person other than the person to whom this information was originally delivered and to such person's advisors is unauthorised and any reproduction of these materials, in whole or in part, or the divulgence of any of their contents, without the prior consent of the Firm in each such instance is prohibited.

This document is intended for Professional Investors only. All figures, unless stated otherwise, are as at the last business day of the relevant month showing above. Some of the figures shown in the tables are estimates, provided by the Firm. The performance shown does not take account of any commissions and costs charged when subscribing to and redeeming shares. Past performance may not be a reliable guide to future performance.

The strategy employed may result in the NAV exhibiting a high level of volatility. This fund may invest in contingent convertible securities ('Cocos'). CoCos have unique risks, for example, due to equity conversion or principal write-down features which are tailored to the issuing entity and its regulatory requirements, which means the market value of CoCos may fluctuate. Additional risk factors associated with CoCos are set out in the fund's prospectus.

The State of the origin of the Fund is Ireland. In Switzerland, the Representative is ACOLIN Fund Services AG, Affolternstrasse 56, CH–8050 Zurich, whilst the Paying agent is Vontobel Ltd, Gotthardstrasse43, CH-8022 Zürich. The basic documents of the Fund such as the prospectus, the key investor information document (KIID), the articles of association as well as the semi-annual and annual reports may be obtained free of charge at the office of the Swiss Representative.

© 2018 Algebris (UK) Limited. All Rights Reserved. 4th Floor, 1 St James's Market, SW1Y 4AH.