INVESTMENT MANAGEMENT

 Commentary | 3Q20

Voya Securitized Credit Fund

Tap into Voya’s Flexible “Through-the-Cycle” Approach

Strategy Overview

Invests in fixed income sectors collateralized by distinct asset types: commercial real estate (CMBS), residential housing (RMBS) and nonmortgage assets (ABS).

Key Takeaways

■ Performance saw a continued rebound in the third quarter after the pandemic driven sell-off in March 2020.
■ Spreads across all securitized sub-sectors continued their recovery driven by a favorable technical backdrop and generally improving fundamentals.
■ Longer term, we continue to believe that securitized credit represents attractive exposure to the relatively strong fundamentals of the U.S. consumer.

Current Strategy and Outlook

The response to the COVID-19 pandemic has accelerated or exacerbated trends that were already in place. The resulting uneven pressures will create winners and losers with broad strokes across the fixed income spectrum and is being referred to as the “K-economy”.

From our view, the winners and losers in the post-COVID world fall into two camps. In the first camp are investments that are being affected by trends that were already in place and have accelerated because of the world’s response to the pandemic and the resulting uneven economic recovery. For example, among commercial mortgage-backed securities (CMBS), a potential “loser” would be brick and mortar properties anchored by lower-tiered malls. These properties already were facing significant pressure from the shift towards online retail; the response to COVID simply exacerbated their problems and accelerated the deterioration in their fundamentals.

In the second camp are sectors and investments that are being affected disproportionately by the COVID-19 pandemic. In this camp there will be industries that will either be negatively affected such as the decline in air travel and entertainment, or on the positive side online retail and other technology that have adapted to changes caused by the continuation of work from home.

Assessing sectors and industries through this lens of winners and losers will be critical to investment success going forward, with security selection having the potential to yield an outsized impact on performance in the months ahead.

Portfolio Review

For the quarter, the Fund outperformed its benchmark, the Bloomberg Barclays U.S. Securitized MBS/ABS/CMBS index, due to its allocation to off-benchmark securitized credit sectors.

CMBS was the top contributor to returns during the quarter. After lagging the rally in the second quarter amidst persistent selling pressure, limited direct Fed support and acutely

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challenged fundamentals, the sector appeared to “turn the corner” fundamentally and technically. Supply was constrained and, while direct Fed support remained limited, delinquencies in the space declined each month during the quarter, albeit incrementally and exiting the quarter at elevated levels that still reflect significant challenges for sectors of the CRE universe.

Following CMBS, the Fund’s allocation to non-agency residential mortgage-backed securities (RMBS) was the second biggest contributor to returns during the quarter, as the sector benefited from a continuation of the favorable prepayment and housing market dynamics that powered its outsized second-quarter contribution to Fund results.

Asset-backed securities (ABS) excess returns were solidly positive as well, as spreads continued to tighten in non-benchmark sub-sectors. Solar and unsecured consumer loan exposures were emblematic of the positive experience available in consumer related ABS sub-sectors.

Interestingly, collateralized loan obligations (CLOs) were the second-best performing sector from a per dollar excess return standpoint, benefitting from the strong rebound experienced in the bank loan market during the quarter. Despite the ratings cycle spawning a swath of downgrades, improving dollar prices in underlying loans pushed up important credit metrics in CLOs, fostering sentiment in the space.

Conversely, on a retrospective basis, the list of what didn’t perform well is less inclusive. The relatively low allocation to CLOs during the quarter limited the contribution from this otherwise strong performing sub-sector. Additionally, the impact from duration, while positive on an absolute basis, slightly detracted on a relative basis, as the Fund was modestly short duration versus the benchmark.

The Bloomberg Barclays U.S. Securitized MBS/ABS/CMBS and Covered Index includes the MBS, ABS, and CMBS sectors. Indexes do not reflect fees, brokerage commissions, taxes or other expenses of investing, and investors cannot directly invest in an index.

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