AlphaCentric Income Opportunities Fund

Weighted Average Coupon (WAC) & Callable Bonds

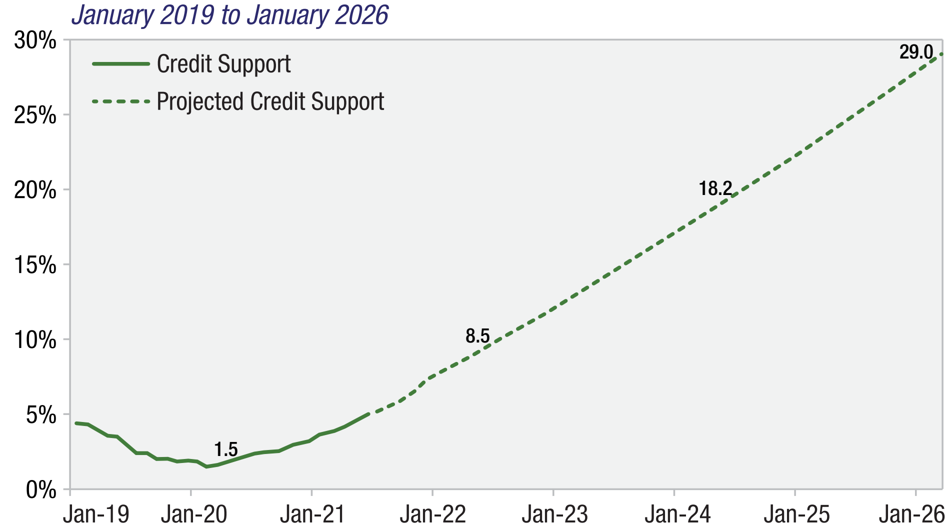
IOFIX
IOFAX
IOFCX

An important component of the legacy (seasoned) non-agency RMBS market is the idea of excess interest. We have written about that frequently and you can read about excess interest in our AlphaCentric Insights series here. However, another important aspect of these securities is the callable nature of the bonds. This educational piece explores the ways in which callable bonds can affect a portfolio, as well as explaining weighted average bond coupons and their impact on investments.

What is a callable bond?

- A callable bond is a type of bond that provides the issuer of the bond with the right – but not the obligation – to redeem the bond before its maturity date.
- The callable bond is a bond with an embedded call option.
- These bonds generally come with certain restrictions on the call option. For example, the bonds may not be able to be redeemed in a specific initial period of their lifespan.

Historical & Projected Credit Support for a Sample Legacy Subprime Bond
January 2019 to January 2026



Source: Nomura. Data as of 6/30/21.

What do the calls mean as related to the Non-Agency Residential Mortgage-Backed Securities (NARMBS) space?

- In the securitization, once the number of loans in the pool balance have dropped down to the last 10%, the deal becomes legally callable.
- As the excess interest in the bonds builds, this plays a critical role in building back credit support, writing back losses, and increasing call prices. Now that 2020 is in the rearview mirror, we have seen an increase in the number of bonds being called across the board and also within our portfolio. Rates are very low but so are the number of defaults, delinquencies, and foreclosures. Delinquencies, and also gross weighted-average coupons (WAC), are what really drive calls.
- Recall that a very simple formula for calculating excess interest is:

Gross WAC – Servicing Fee – Average Weighted Bond Coupon = Excess Interest

For our conversation, the higher the WAC, the more valuable the coupon is to the underlying holder of the securities. The lower the delinquencies than we would expect to see, the lower probability of losses. In this low rate environment, loans paying coupons of 4-5% with low delinquencies have demand. Servicers want to call these and sell the proceeds, loans, for greater than par.

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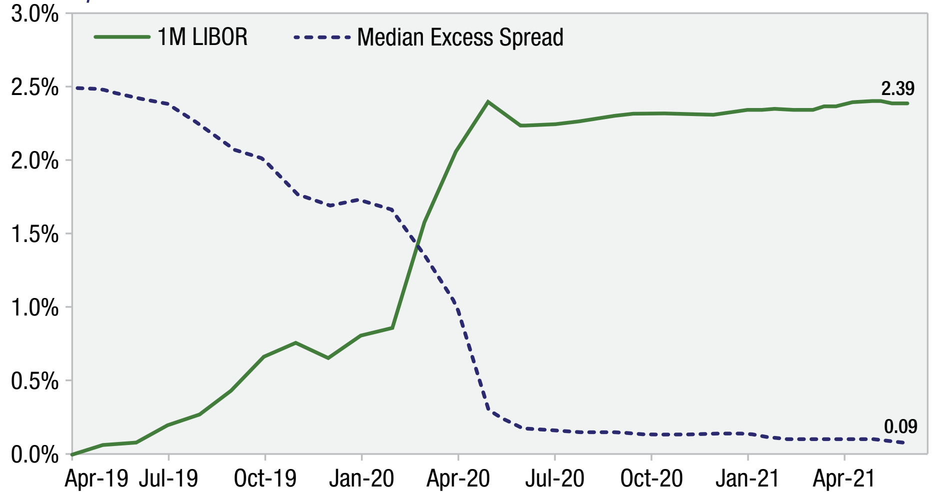
What is the WAC?

- WAC is the rate of return on a pool of mortgages sold to investors as an MBS.
- The WAC represents the average interest rate of different pools of mortgages with varying interest rates.
- In the weighted average calculation, the principal balance of each underlying mortgage is used as the weighting factor.
- To calculate the WAC, the coupon rate of each mortgage or MBS is multiplied by its remaining principal balance. The results are added together, and the sum total is divided by the remaining balance. Because the underlying mortgages are repaid at different lengths of time, so the WAC represents its return at the time it was issued and may differ from its WAC later.

Legacy Subprime Deals Media Excess Spread vs 1-Month LIBOR
April 2019 to June 2021



Source: Nomura, Bloomberg, & Intex. Includes 2005-07 vintage legacy subprime deals. As of 6/30/21.

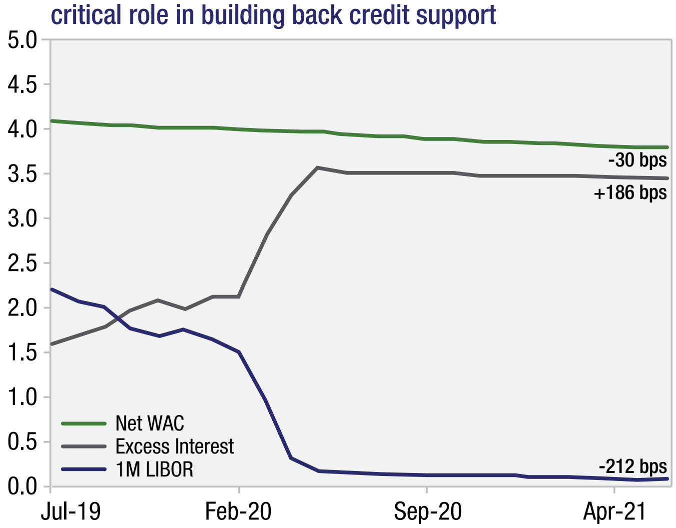
How can this affect investments?

- In some respect, callable bonds can present higher risks for investors. If the bonds are redeemed, in general, the investors will lose some future interest payments.
- However, when bonds are purchased at a discount – as they are within our Income Opportunities Fund – calls and prepayments can accelerate our returns.

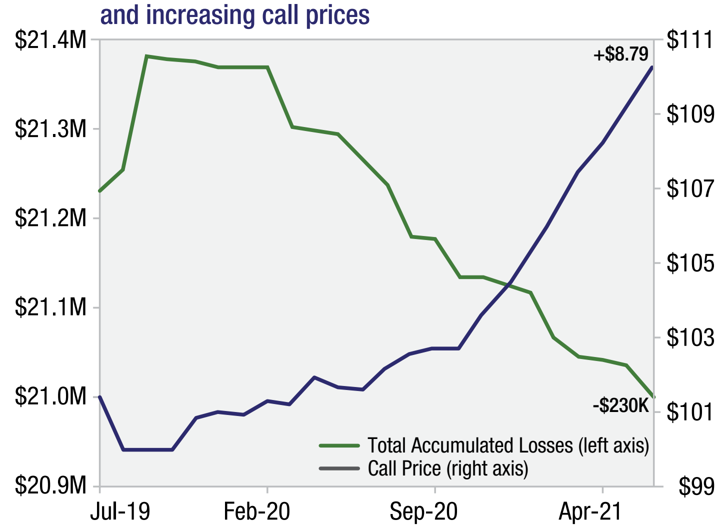
Example: A security priced at $88 and called at $100 accelerates the total return.

- Furthermore, as the excess interest in the bonds continues to grow and appreciate, the amount that the bond is called grows as well, further accelerating the return value.

Excess interest has increase of 186 bps and plays a critical role in building back credit support



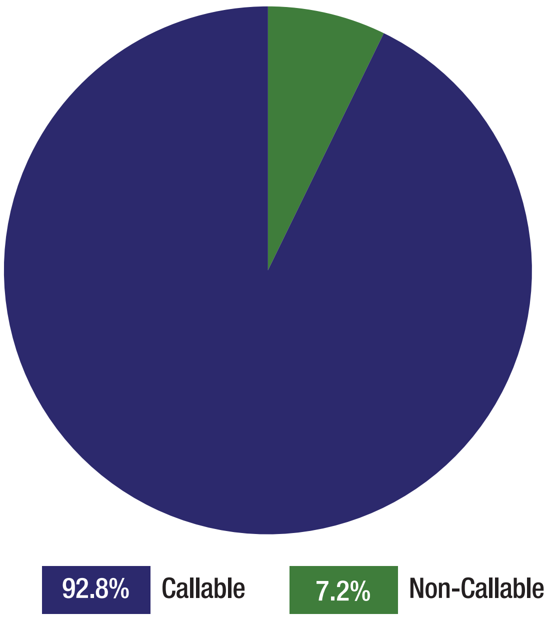
The excess interest supports writing back losses and increasing call prices



Note: This example is for illustration purposes only and shows a simple cash flow waterfall as it relates to excess interest. Specific figures are made to mimic an "example" subprime deal structure.

AlphaCentric Income Opportunities Fund Callable vs Non-Callable

Percentage of Portfolio as of 6/30/21



One of the major and differentiated aspects of the NARMBS space that we like is excess interest. This is unique to the NARMBS sector.

In addition to providing benefits to repair impaired securities, it also impacts the WAC of the bonds. This means that the call price of the securities increases and has the potential to continue to compound over time, particularly in a low interest environment.

Especially relating to our portfolio, calls and prepayments accelerate our returns because of the discounts of our bond prices.

Callable bonds are yet another fundamental benefit of the Income Opportunities Fund's portfolio.

Fund Performance as of 6/30/21 *(Annualized if greater than 1 year)*

Inception Date: 5/28/15	QTD	YTD	1 YR	3 YR	5 YR	Inception
IOFIX	2.44	8.02	25.13	3.13	6.28	7.62
IOFAX	2.38	8.00	24.85	2.87	6.03	7.36
IOFCX	2.20	7.54	23.92	2.10	5.24	6.56
Bloomberg US Agg. Bond TR Index	*1.83*	*-1.60*	*-0.33*	*5.34*	*3.03*	*3.30*
Class A After Sales Charges	-2.46	2.86	18.86	1.22	5.00	6.50

Past performance is no guarantee of future results. There is no assurance that the Fund will achieve its investment objective. Investment return and principal value will fluctuate with changing market conditions so that when redeemed, shares may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted. To obtain the most recent month end performance information or the funds prospectus please call the fund, toll free at 1-844-ACFUNDS (844-223-8637). You can also obtain a prospectus at www.AlphaCentricFunds.com. The maximum sales charge for Class A shares is 4.75%. Total Annual Fund Operating Expenses are 1.96%, 2.71%, and 1.71% for Share Class A, C, and I. Total Annual Fund Operating Expenses after Fee Waiver and/or Expense Reimbursement are 1.74%, 2.49%, and 1.49% for share Class A,C, and I, respectively.

Investors should carefully consider the investment objectives, risks, charges and expenses of the AlphaCentric Funds. This and other important information about the Fund is contained in the prospectus, which can be obtained by calling 844-ACFUNDS (844-223-8637) or at www.AlphaCentricFunds.com. The prospectus should be read carefully before investing. The AlphaCentric Funds are distributed by Northern Lights Distributors, LLC, member FINRA/SIPC. AlphaCentric Advisors, LLC is not affiliated with Northern Lights Distributors, LLC.

Important Risk Information

Investing in the Fund carries certain risks. The value of the Fund may decrease in response to the activities and financial prospects of an individual security in the Fund's portfolio. The Fund is non-diversified and may invest a greater percentage of its assets in a particular issue and may own fewer securities than other mutual funds; the Fund is subject to concentration risk. Credit risk is the risk that the issuer of a security will not be able to make principal and interest payments when due. The use of derivatives and futures involves risks different from, or possibly greater than, the risk associated with investing directly in securities. Fixed income securities will fluctuate with changes in interest rates. Lower-quality bonds, known as "high yield" or "junk" bonds, present greater risk than bonds of higher quality. The performance of the Fund may be subject to substantial short-term changes. There are risks associated with the sale and purchase of call and put options. These factors may affect the value of your investment.

Key Definitions

Bloomberg US Aggregate Bond Index: A market capitalization-weighted index that is designed to measure the performance of the U.S. investment grade bond market with maturities of more than one year.

You cannot invest directly in an index. Unmanaged index returns do not reflect fees, expenses or sales charges. There is no assurance that the Fund will achieve its investment objective.

Not all products available at all firms. Advisors, please contact your home office.

Contact Us

+1 855 674 FUND

www.alphacentricfunds.com

info@alphacentricfunds.com