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Philip Ryan
managing director
Trilogy

Financial advisers on the hunt for income products for their clients should consider taking a look at mortgage trusts. While the sector can't match the pizzazz of a technology fund or the familiarity of an equities fund, it provides plenty of appeal for investors who want a stable and regular income in a low-rate environment. In fact, according to researcher SQM, mortgage trusts have seen funds under management rise from over $10 billion in June last year to more than $15 billion to date.

To explain more about the topic, we interviewed Phil Ryan, managing director of Trilogy Funds Management.

Ryan was there during the inception of Trilogy in 1998 and has a wealth of knowledge on how financial advisers might use mortgage trusts as part of a client's balanced portfolio.

Michelle Baltazar
Director of Media & Publishing

Mortgage trusts a compelling option for investors

In a low rate environment, many advisers may consider mortgage trusts as part of a client's balanced portfolio.

Australia's $15 billion mortgage trust sector has long been popular with investors looking for competitive investment income as part of a diversified portfolio.

In 2020, as economic uncertainty has soared and returns from investments such as dividends and bank savings have continued to shrink, the sector has provided a genuine alternative.

At the same time the industry provides an essential service to property developers, who are finding it harder than ever to get support from their banks.

The mortgage trust sector has enjoyed substantial growth in recent times according to SQM Research's 2020 Mortgage Trust Sector Review and at this time is managing the impacts of COVID-19 well, thanks to continued investor support and the underlying strength of the Australian property sector.

While past performance should not be taken as an indicator of future returns, a number of mortgage trusts continue to deliver competitive returns to investors.

The top-performing trust in SQM's July 2020 update, the Trilogy Monthly Income Trust recently reported a monthly distribution equivalent to 6.55%p.a.* for July 2020.

The Trust currently has over 85 loans in its portfolio as at 31 July 2020, stretching across Queensland, New South Wales and Victoria and mainly comprising residential property development loans consisting of land, townhouses, units and houses.

While all investments carry risk, the Trilogy Monthly Income Trust is professionally and proactively managed by the experienced Trilogy team and backed by first mortgages secured over Australian property.

Why advisers include mortgage trusts in their client's portfolio

Also referred to as mortgage funds, mortgage trusts pool investor money to lend to borrowers while taking a mortgage over the underlying property. Loans may be for land subdivision projects or to finance construction and property development.

Mortgage trusts aim to provide investors with a regular income called a distribution from the interest paid by borrowers, as well as cash and other investments held by the trust.

In today's historically low-rate environment, many advisers may consider an exposure to mortgage trusts as part of their client's balanced portfolio.

However, as is always the case when investing there is no return without risk so please consider and understand the risks in this type of investment. When assessing mortgage trusts for their client's portfolio, financial advisers should consider asking questions such as:

- Does the Trust have an established track record?
- Does management have the necessary expertise and experience?
- What is the Trust's withdrawal policy?
- Does it have a diversified loan portfolio?
- What are the Trust's lending criteria and valuation policy?
- Can the investor accept the risks involved?

Independent research reports such as those offered by Australia Ratings or SQM Research can also be helpful for licensed advisers.

POOLED	CONTRIBUTORY
Your investment is diversified across a range of mortgages.	You decide which mortgage you invest in.
Income from the pool of mortgages is distributed to all investors equally.	The mortgage you invest in might generate a different return from other individual mortgage investment options.
Investors share the risk associated with each of the mortgages in the pool.	You're exposed to the risk of only that mortgage.
You can withdraw some or all of your capital subject to the trust's liquidity (a notice period is usually required).	You can only receive your capital when the loan is repaid. This may be in tranches or in one lump sum.

Source: Trilogy

The quote

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The impacts of COVID-19 on the sector

Assessing the potential future impacts of the COVID-19 health crisis on Australia's mortgage trust sector, SQM notes that the long-term trajectory of the pandemic and the economy is unclear. Some mortgage trusts may experience slowing or negative fund inflows, and some may become more conservative in their lending standards.

However, SQM notes that "the mortgage funds sector entered into this crisis in a healthier condition as compared to pre-GFC, including better lending standards and a better liquidity match".

At Trilogy, we continue to monitor market changes and any potential impacts, and we work closely with our borrowers to manage risk.

We're optimistic given the strength of the construction industry over the previous lockdown period, and at this time continue to see no evidence of supply breakdown for any projects. In addition, sales of completed stock continue to perform as expected.

We're taking a proactive approach to investment management, with our primary focus being mitigating risk, protecting capital and continuing to pay monthly distributions. FS

For more info, visit trilogyfunds.com.au/investing or call 1800 230 099.

*Distribution rate for the month ending 31 July 2020 annualised was equivalent to 6.55% per annum for the Trilogy Monthly Income Trust ARSN 121 846 722. Distribution rates are calculated daily, paid monthly in arrears and are net of management fees and costs, and assume no reinvestments. Distributions for the Trust are variable each month and depend on the performance of the underlying assets.

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