



THE FIXED INCOME CLOCK

Paul Brain

Investment leader, fixed
income team

Scott Freedman

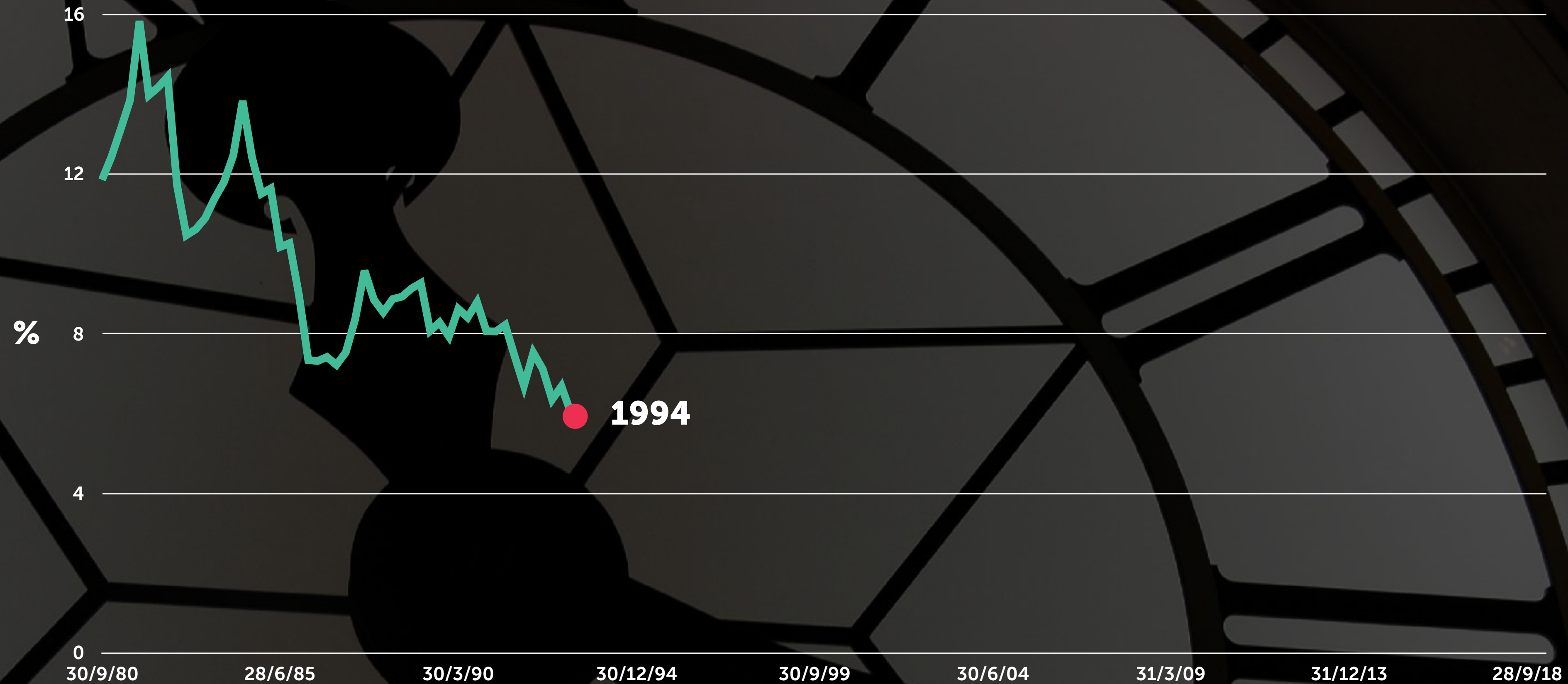
Analyst and portfolio manager,
fixed income team

#NEWTON2018

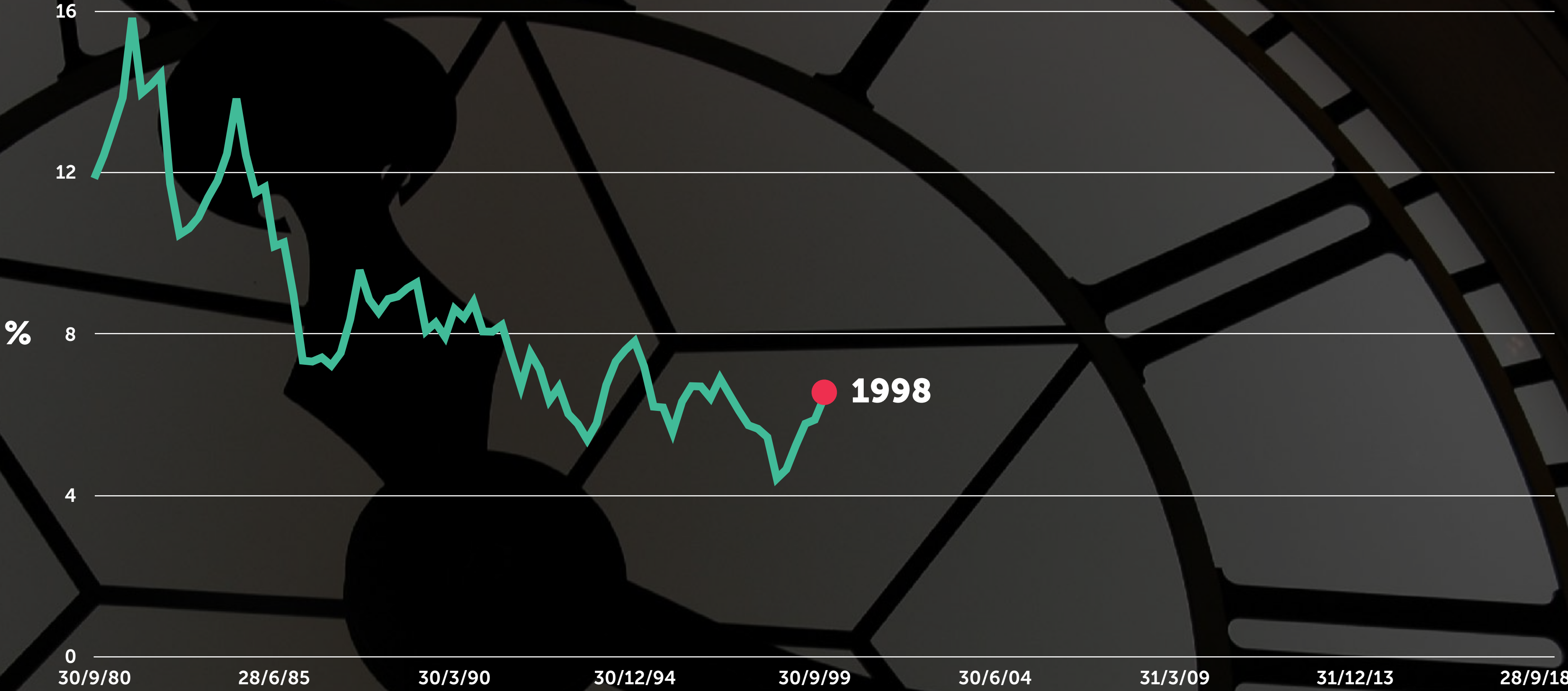
US TREASURY 10-YEAR YIELD



US TREASURY 10-YEAR YIELD

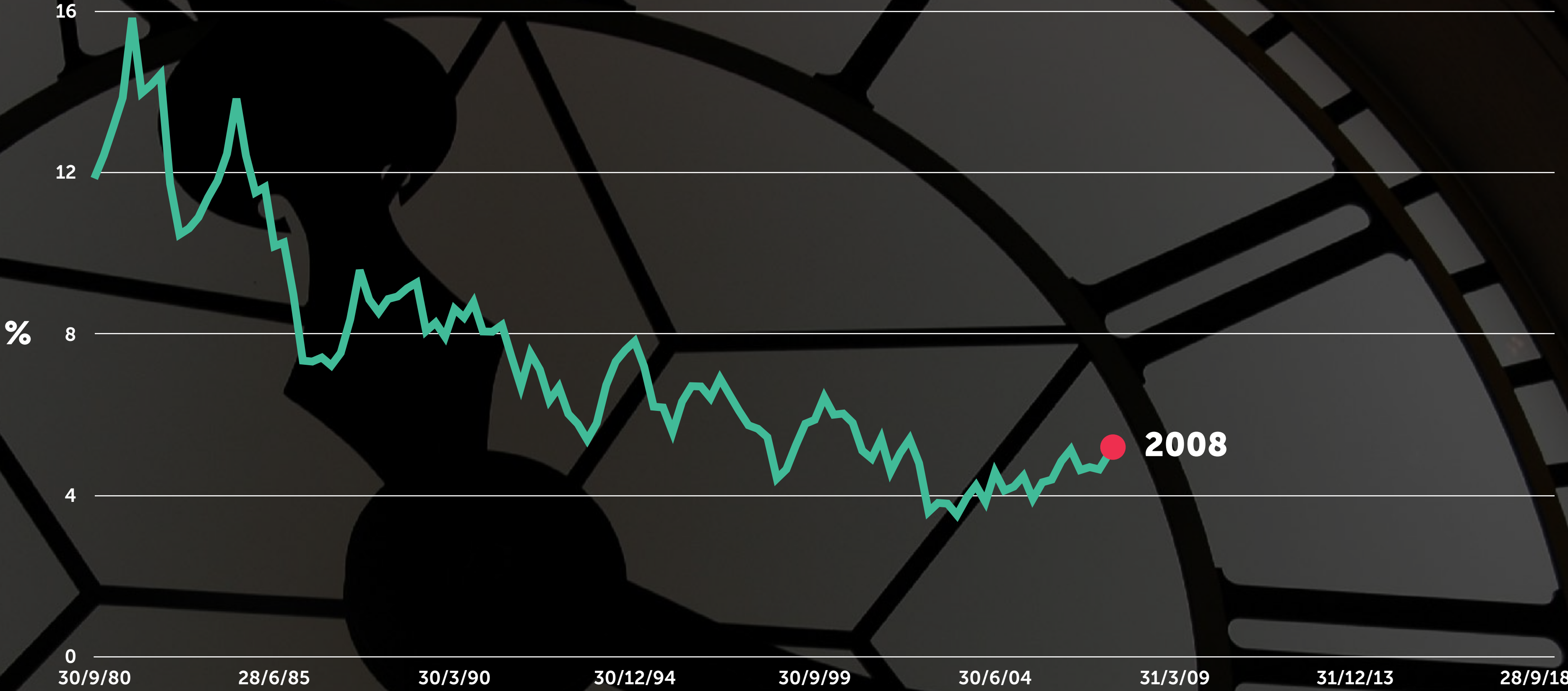


US TREASURY 10-YEAR YIELD



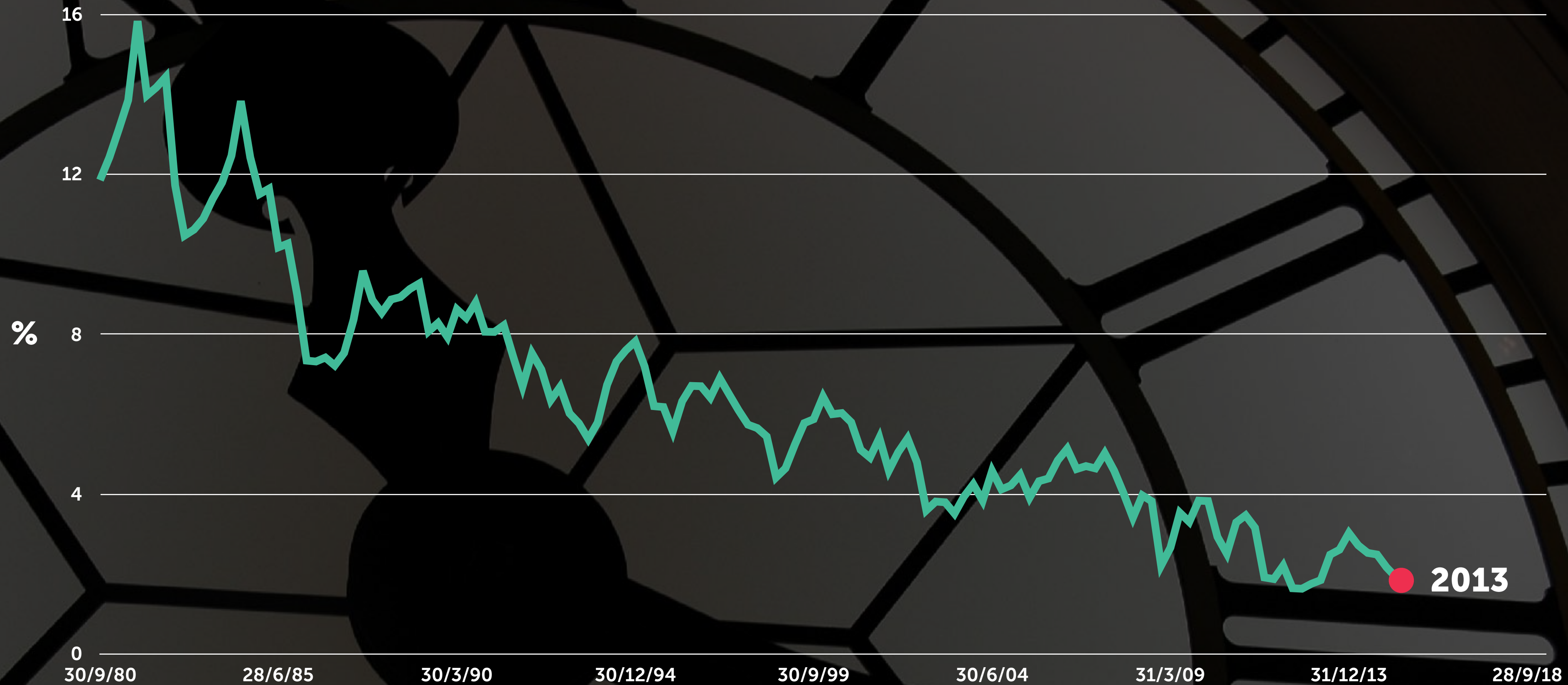
Source: Bloomberg 25/10/18

US TREASURY 10-YEAR YIELD

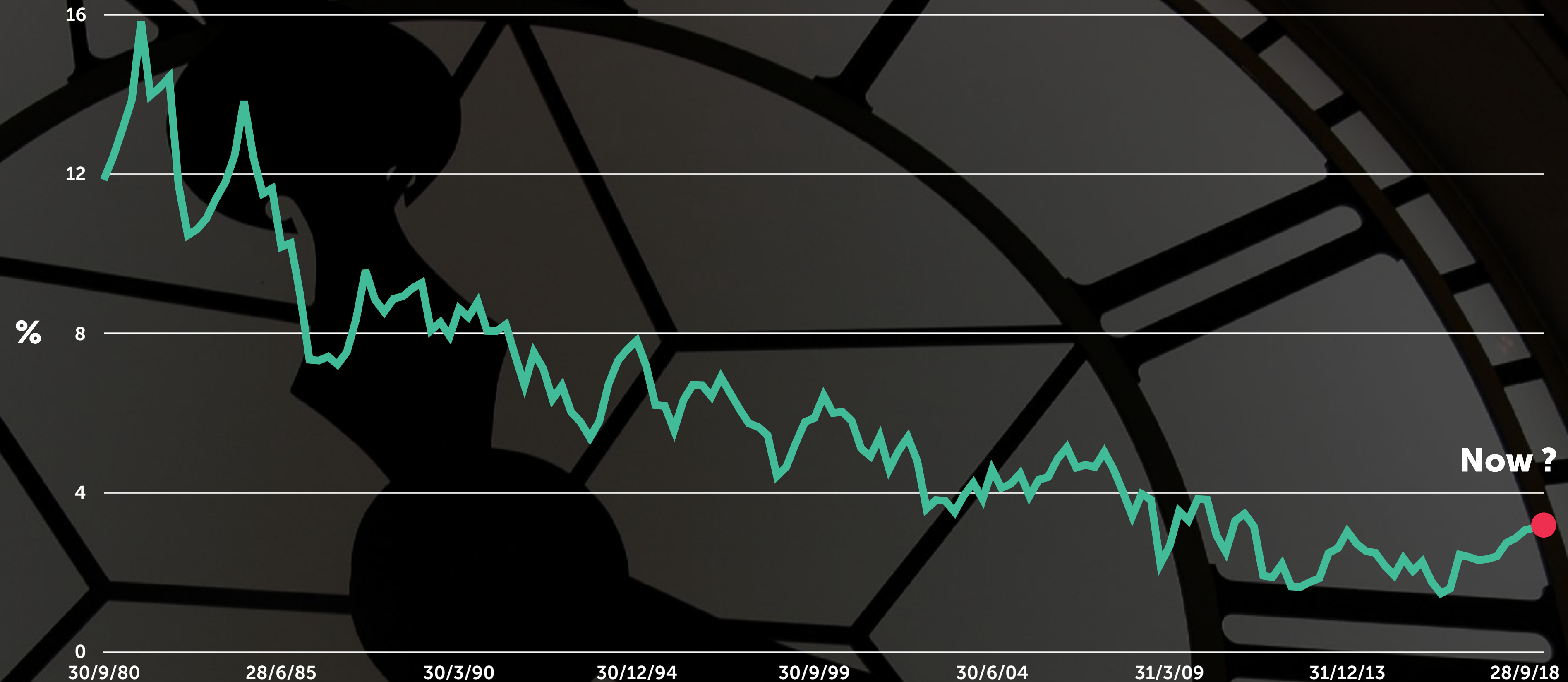


Source: Bloomberg 25/10/18

US TREASURY 10-YEAR YIELD

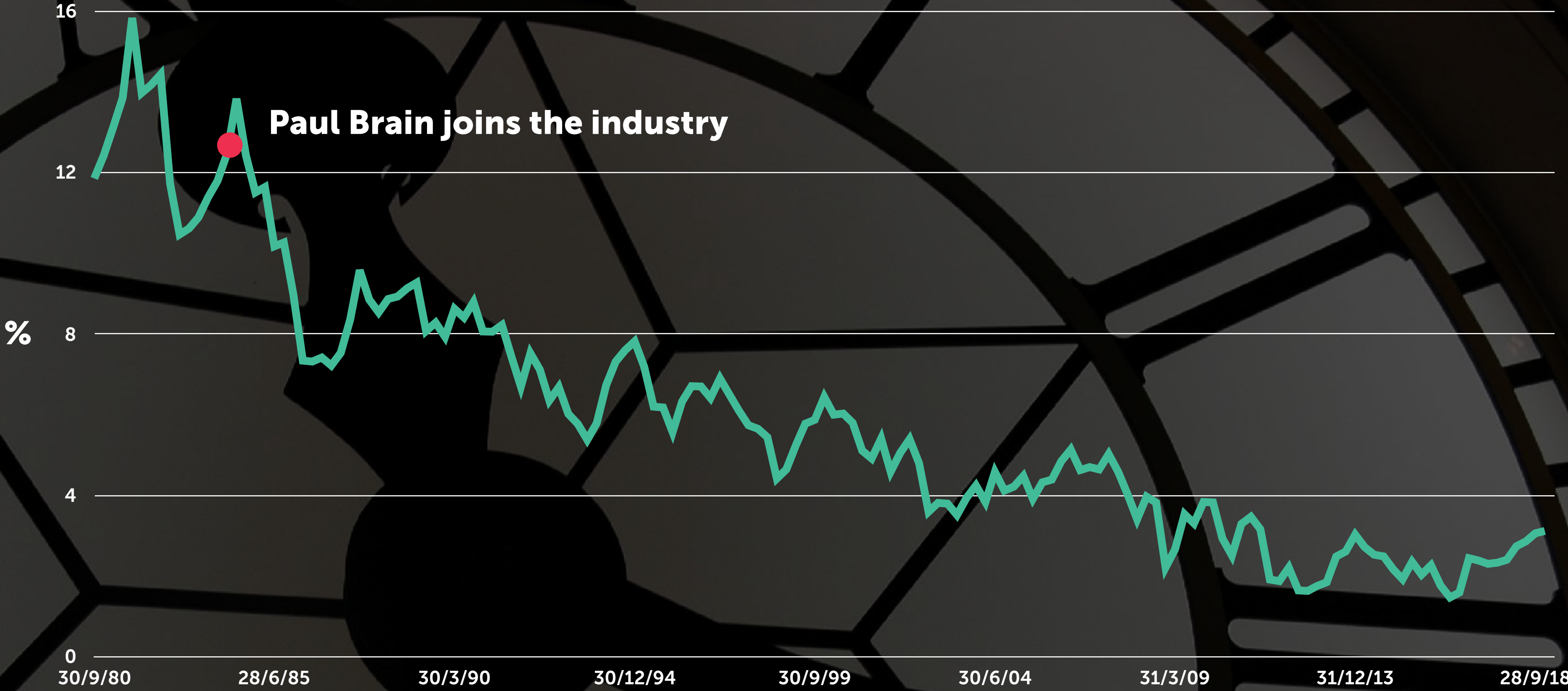


US TREASURY 10-YEAR YIELD



Source: Bloomberg 25/10/18

US TREASURY 10-YEAR YIELD



Source: Bloomberg 25/10/18

TIME AND TIDE WAIT FOR NO MAN.

Where Are We On
The Fixed Income
Clock, And Why
Should We
Embrace Esg
Matters?

The period of extremely loose monetary policy is coming to an end and bond yields are on the rise once more. The investment cycle over the next couple of years may continue to be challenging to bond investors and, looking at history, we will attempt to guide investors.

One of the growing influences on our approach has been the use of ESG analysis in our bond process, which we believe is helpful in reducing risk. We think the virtues of ESG bond investing will be an increasingly talked-about trend.

Beginning of the
bond bull market

1981

Savage but
temporary
interruption in the
bond bull market as
Fed raised rates
300bp in 12 months
on fear of inflation

1994

Asian/Russian crisis
Markets have delayed
reaction to Fed rate
rises

1997/98

Equity market finally
responds to the tight
monetary policy

2000

Post financial crisis
extra loose monetary
policy

2009

Fed (and then others)
announced they had
done enough
Bear market begins

2015/16

How will the equity
market respond?

2019

A quick look back at some historical influences on the government bond market

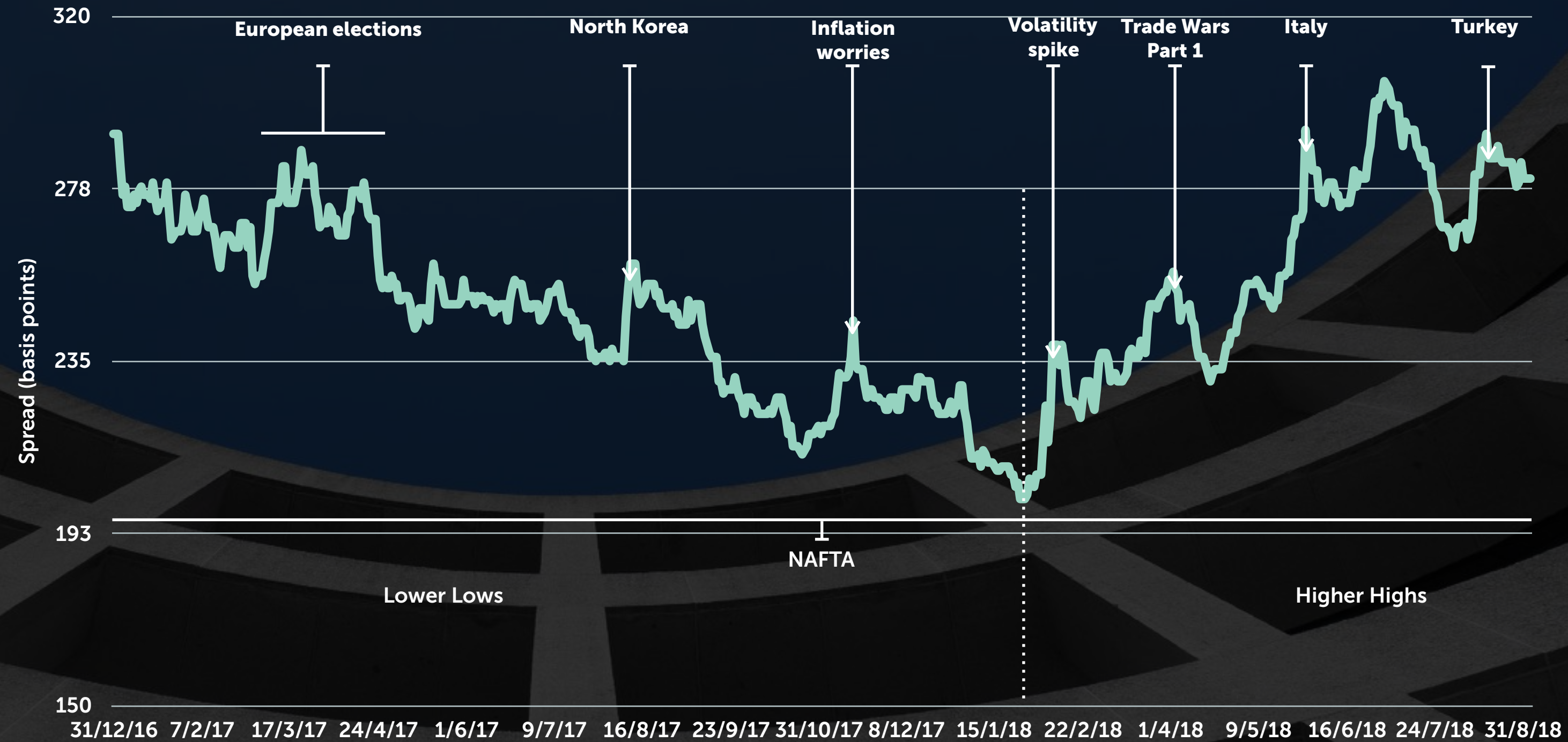
SOMETHING CHANGED IN 2016- GOVERNMENT BOND BEAR MARKET STARTED



But credit markets carried on

**2017:
BUY THE DIP,
2018:
SELL THE RALLY**

Global BB-rated corporate spreads

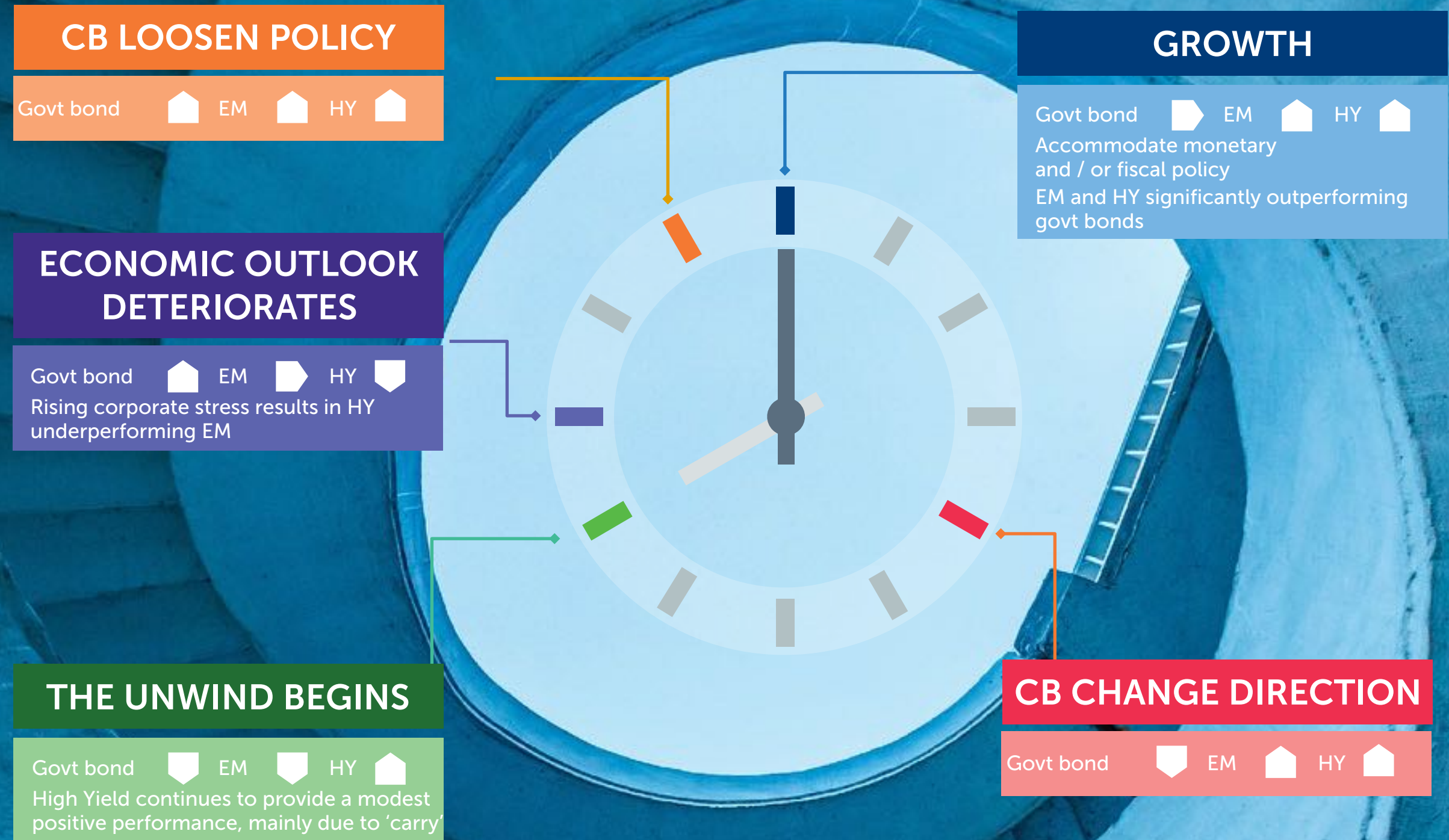


The marginal buyer
(central banks) is
leaving the room

Deteriorating liquidity is not good for risk assets

THE TIGHTENING CYCLE IS GRADUAL

but eventually there will be a price to pay for assets that have run ahead of growth



ASSET CLASS RANKINGS CONSTANTLY SHIFT

Asset class performance rankings over time

	BEST ←————→ WORST				Difference between best & worst
2017	EM 9.2	HY 6.7	IG 4.6	Govt 1.1	8.1%
2016	HY 15.7	EM 9.0	IG 5.7	Govt 3.6	12.1%
2015	Govt 1.7	EM 0.9	IG 0.1	HY -2.1	3.8%
2014	Govt 8.7	IG 8.0	EM 7.9	HY 2.7	6.0%
2013	HY 7.3	IG 0.2	Govt -0.2	EM -4.5	11.8%
2012	EM 22.1	HY 18.7	IG 10.9	Govt 4.6	17.5%
2011	Govt 6.3	IG 5.1	EM 4.6	HY 2.9	3.4%
2010	EM 15.2	HY 14.9	IG 7.5	Govt 3.9	11.3%
2009	HY 59.7	EM 27.5	IG 16.1	Govt 1.2	58.5%
2008	Govt 11.7	IG -3.4	EM -16.1	HY -27.0	38.7%
2007	Govt 6.4	EM 5.6	IG 3.8	HY 2.5	3.9%
2006	EM 12.1	HY 10.2	IG 3.3	Govt 2.8	9.3%
1994	HY -0.0	Govt -2.5	IG -3.3	EM -16.1	16.1%

Agility is essential

Note: 1994-1997 US IG and HY indices used.
Source: Newton, Merrill Lynch Indices Hedged into Sterling, 30 June 2018.

ASSET CLASS RANKINGS CONSTANTLY SHIFT

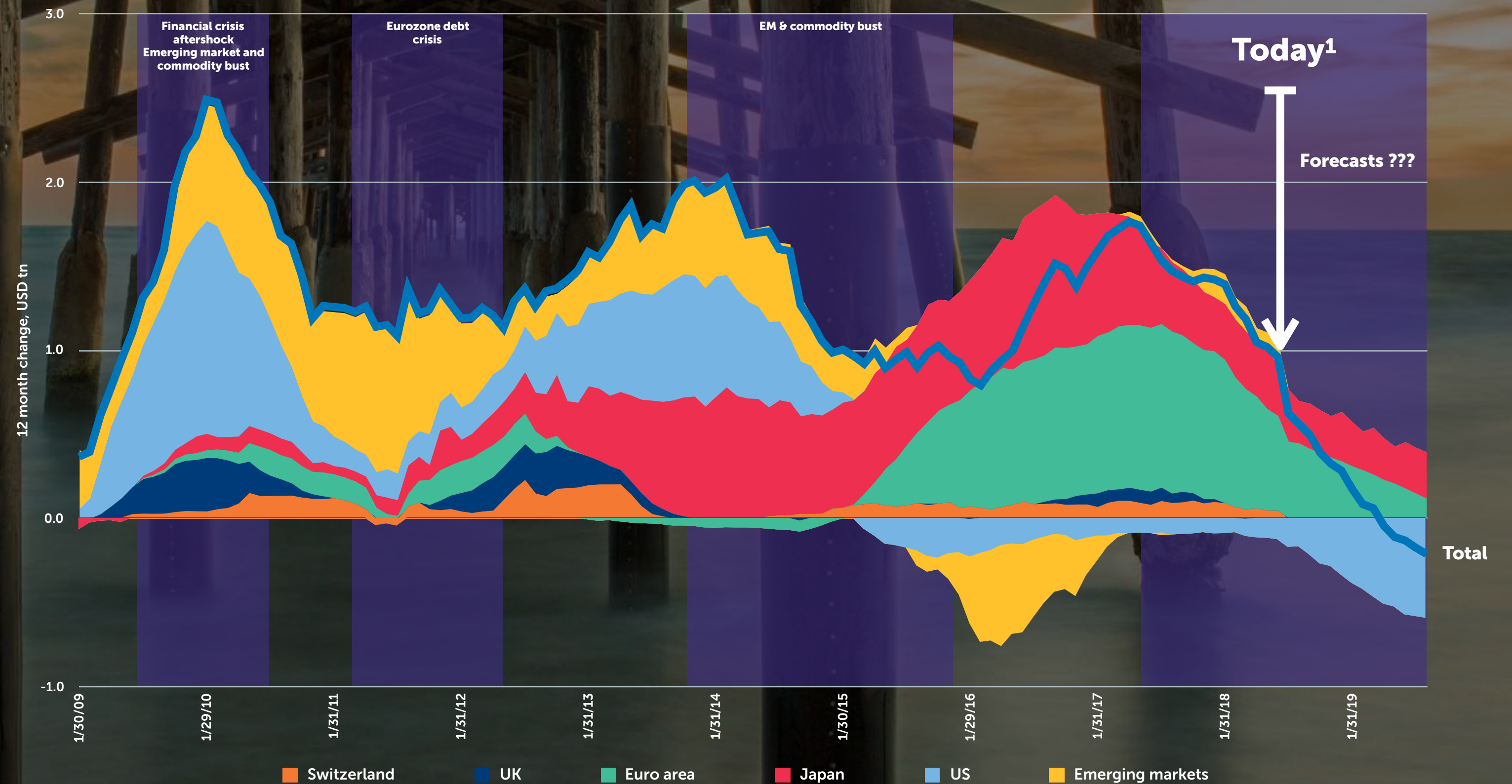
Asset class performance rankings over time

	BEST			WORST	Difference between best & worst	
31 OCT 2018	Govt -0.1		HY -1.2	IG -3.1	EM -6.7	6.4%
2017	EM 9.2		HY 6.7	IG 4.6	Govt 1.1	8.1%
2016	HY 15.7		EM 9.0	IG 5.7	Govt 3.6	12.1%
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Agility is essential

SUPPORT FOR MARKETS AND ECONOMIES WANING

Central bank purchases in freefall...
Rolling 12-month asset purchases, FX-adjusted (USD trillion equivalent)



Note: 1 30 June 2018
Source: Bloomberg, Newton calculations, 30 June 2018. For illustrative purposes only.

LOOKING FOR SIGNS OF STRESS

Consumer stress

		Current	Longer term	Change	
1	2.8	2.9	-0.1	-3%	Green
2	4.8	4.06	0.7	17%	Yellow
3	884	1115	-230.8	-21%	Yellow
4	0.68	0.76	-0.1	-11%	Green
5	12.00	-7.8	19.8	-254%	Yellow
6	4.17	3.75	0.4	11%	Yellow
7	5.77	5.26	1	10%	Green
8	31.17	30.47	1	2%	Green
9	134	155	-21.0	-14%	Green
10	215	206	9.0	4%	Green

Company stress

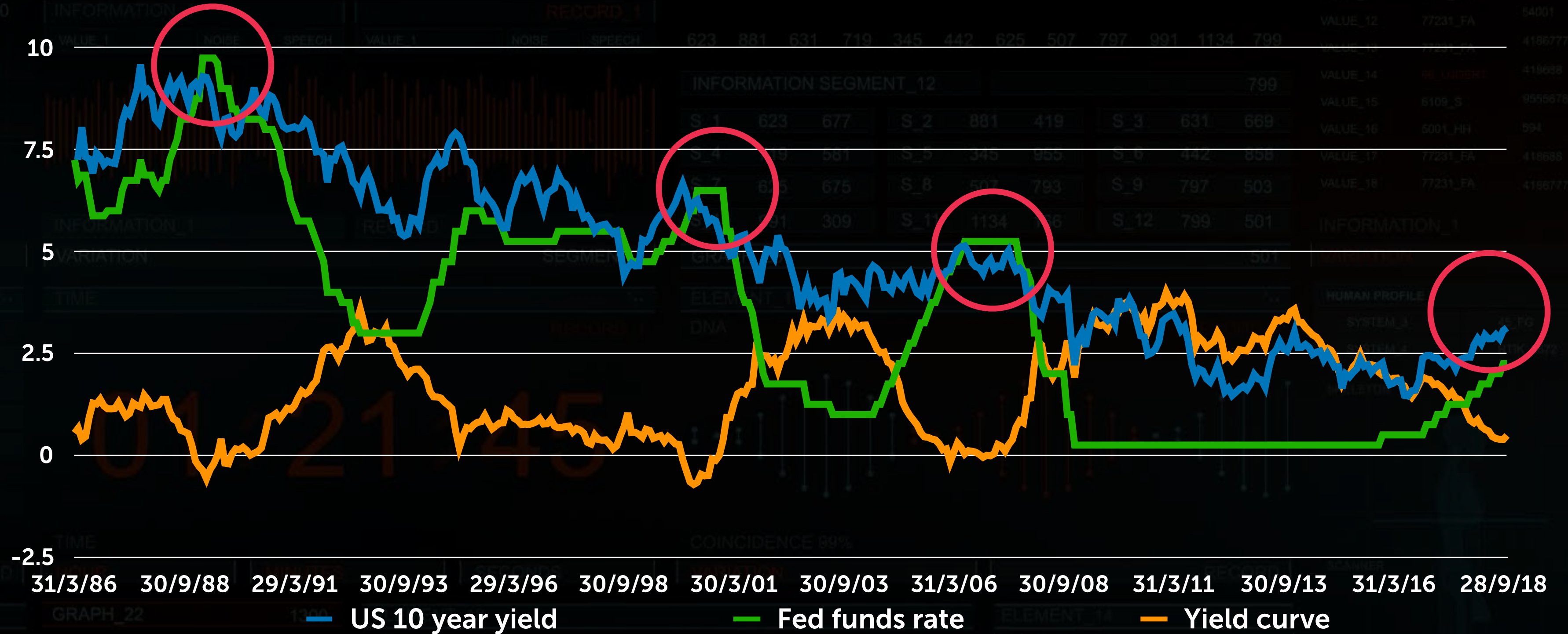
		Current	Longer term	Change	
1	2.8	2.9	-0.1	-3%	Green
2	5.15	4.6	0.55	12%	Yellow
3	34.45	31.66	2.79366	9%	Green
4	63.08	72.794	-9.71847	-13%	Yellow
5	4.13	4.36	-0.23	-5%	Green
6	1.31	1.32	-0.02	-1%	Green
7	LOOSE	LOOSE	0		Green
8	-18.8	-1.5	-17.3	1153%	Yellow
9	-15.9	1.5	-17.4	-1160%	Yellow
10	696.7	851.9	-155.2	-18%	Yellow
11	800	1000	-200	-20%	Yellow
12	83	75	8	11%	Red

Market stress

	Current	Short term	Longer term	Change		
1	19	28	19.95	-0.95	-5%	Green
2	24	25	11	13.00	118%	Green
3	20.33	9.88	11.5	8.83	77%	Yellow
4	112.98	111.46	113.62	0.64	1%	Green
5	0.29	0.56	0.72	0.43	60%	Yellow
6	60.13	48.19	46.38	13.75	30%	Yellow
7	303.92	228.29	244.13	59.79	24%	Yellow
8	127	92	100	27	27%	Yellow
9	414	329	369	45	12%	Yellow
10	331	236	302	29	10%	Yellow
11	-3.60	-3.55	-3.86	0.26	-7%	Yellow
12	508	327	404	104	26%	Yellow
13	2.96	1.49	1.42	1.54	108%	Yellow
14	5992	7141	7312	-1320.00	-18%	Yellow
15	37.93	59.75	29.35	8.58	29%	Yellow
16	39.2	44.9	40.1	-0.94	-2%	Red
17	48.0	47.8	47.13	0.86	2%	Yellow
18					-4.2%	Green
19	232.8	190.7	181.43	51.41	28.3%	Red
20	2712	2775	2585	126.9	4.9%	Yellow
21					23.4%	Green

EXTRACTS FROM THE STRESS MONITORING

The shape of the yield curve



Nearing the end game

LOOKING FOR SIGNS OF STRESS

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7	5.77	5.26	1	10%
8	31.17	30.47	1	2%
9	134	155	-21.0	-14%
10	215	206	9.0	4%

Company stress

	Current	Longer term	Change	
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2	5.15	4.6	0.55	12%
3	34.45	31.66	2.79366	9%
4	63.08	72.794	-9.71847	-13%
5	4.13	4.36	-0.23	-5%
6	1.31	1.32	-0.02	-1%
7	LOOSE	LOOSE	0	
8	-18.8	-1.5	-17.3	1153%
9	-15.9	1.5	-17.4	-1160%
10	696.7	851.9	-155.2	-18%
11	800	1000	-200	-20%
12	83	75	8	11%

Market stress

	Current	Short term	Longer term	Change	
1	19	28	19.95	-0.95	-5%
2	24	25	11	13.00	118%
3	20.33	9.88	11.5	8.83	77%
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21					23.4%

COMPANY BORROWING COSTS

Interest rates are no longer a tailwind

US investment-grade refinancing cost



Coupons on new debt higher than on maturing debt

Source: Bloomberg Oct 2018

* Average weighted coupon based on issue price

AS THE CLOCK TICKS ON, WHAT CAN WE DO?

INCOME

As yields rise the level of income can be used more effectively to offset any capital losses

DYNAMIC

Allocating away from the bond sectors that are going to cause pain and towards those that are likely to benefit from the next phase

AVOID DEFAULTS

Definitely easier said than done but with the right credit process can help



\$22,000,000,000,000

THE MERITS OF ESG BOND INVESTING



**RISK
MITIGATION**



ENGAGEMENT



**BETTER
OUTCOMES**

Better risk adjusted returns

THE MERITS OF ESG BOND INVESTING



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Better risk adjusted returns

ACADEMIC EVIDENCE SUPPORTS INTEGRATED ESG ANALYSIS IN FIXED INCOME

**Two-thirds of studies for
bonds uncover significant
positive performance
relating to ESG criteria**

*Journal of Sustainable Finance and
Development meta-study, 2015*

**A positive ESG tilt results in a
small but steady performance
advantage**

**Good employee relations
mean companies are better
protected from financial
distress**

*Sustainable Investing and Bond Returns,
Barclays, 2016*

**In an expanded study, Barclays
finds more evidence of the
positive effect of responsible
investment on credit portfolios
in different regions and sectors**

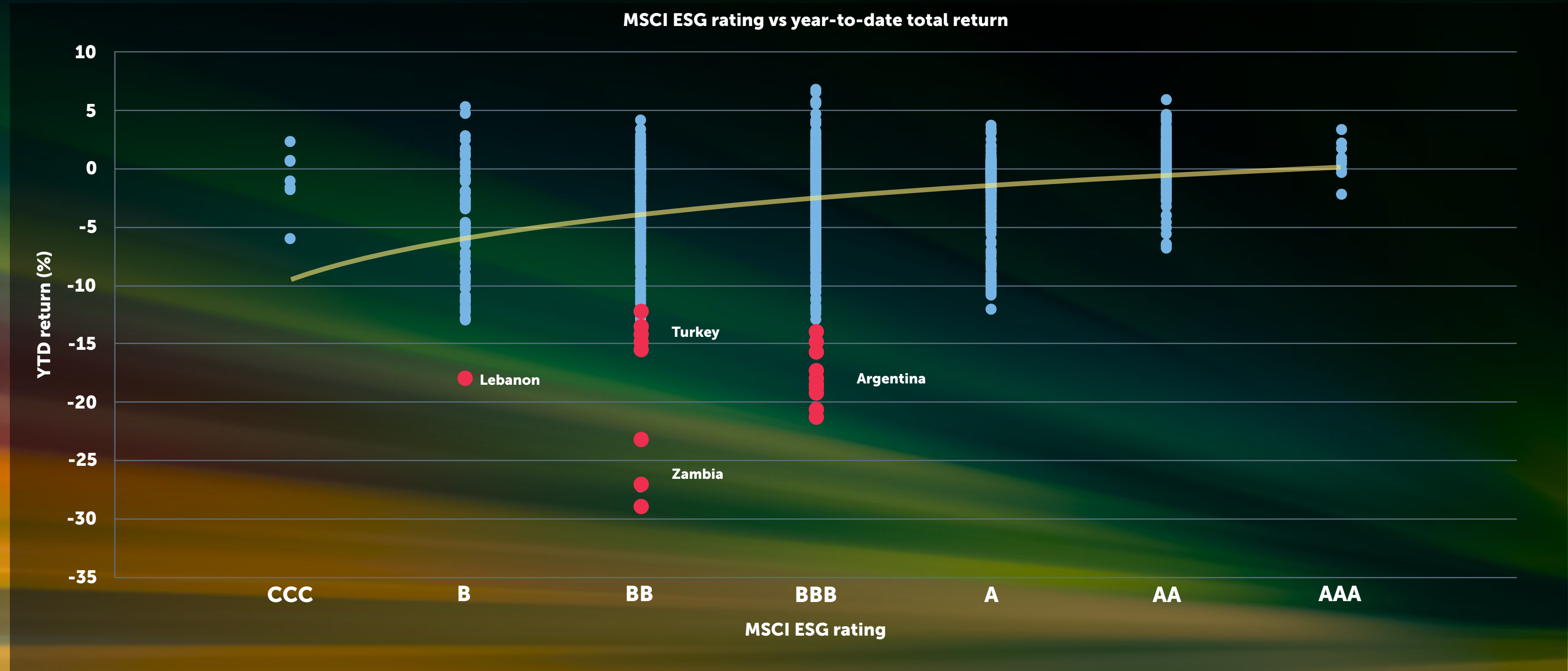
*The Case for Sustainable Bond Investing
Strengthens, Barclays 2018*

MSCI ESG RATING AGAINST YTD TOTAL RETURN COMPANIES



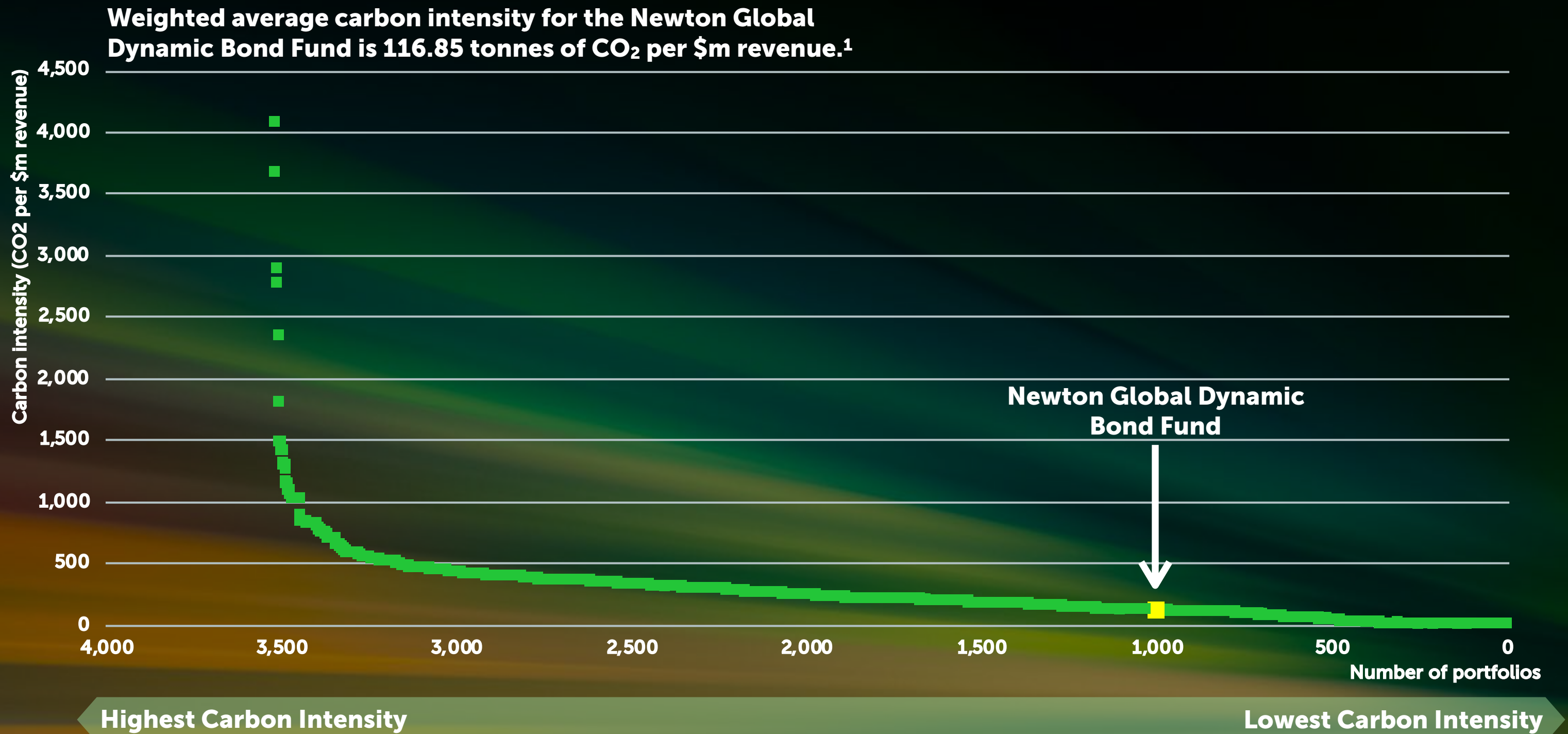
Avoiding the losers is at least as important as picking the winners

MSCI ESG RATING AGAINST YTD TOTAL RETURN GOVERNMENTS



Avoiding the losers is at least as important as picking the winners

THE CARBON INTENSITY OF NEWTON GLOBAL DYNAMIC BOND FUND IS MARKEDLY LOWER THAN PEERS

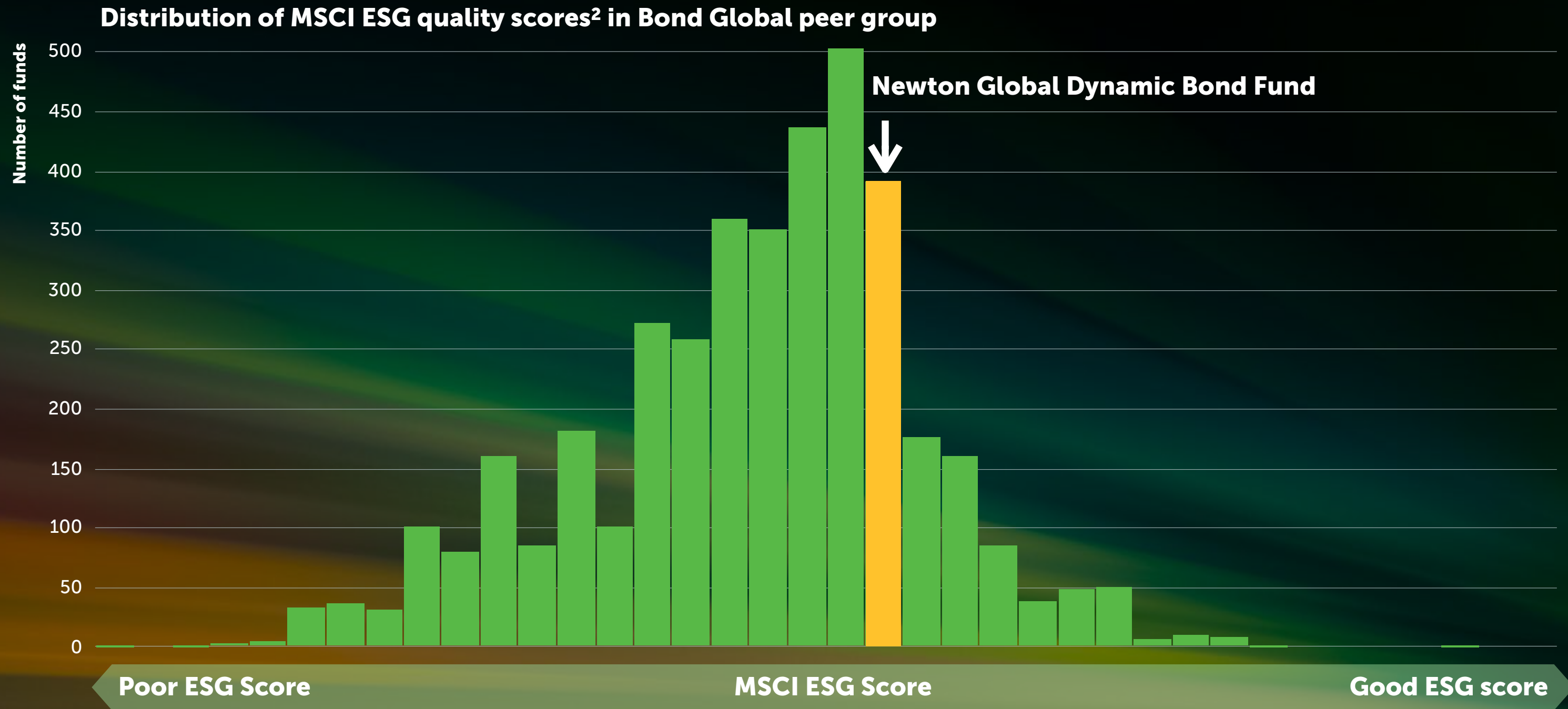


Notes: ¹ The Weighted Average Carbon Intensity measures a fund's exposure to carbon intensive companies. The figure is sum of security weight (normalized) multiplied by the security Carbon Intensity. MSCI calculates weighted average carbon intensity as scope 1+2 emissions/\$m sales weighted by portfolio weight.

MSCI Fund Universe peer group: Bond Global. Number of funds in peer group: 4,035 (this figure includes multiple share classes run under the same strategy).

Source: MSCI ESG Manager. Data accessed October 2018. The data presented is based on the latest available holdings information for each fund in the MSCI Fund Universe database. ©2018 MSCI ESG Research LLC. Reproduced by permission. MSCI ESG Research LLC's ('MSCI ESG') Fund Metrics products (the 'Information') provide environmental, social and governance data with respect to underlying securities within more than 21,000 Mutual Funds and ETFs globally across multiple asset classes. MSCI ESG is a Registered Investment Adviser under the Investment Advisers Act of 1940. MSCI ESG materials have not been submitted to, nor received approval from, the US SEC or any other regulatory body. None of the Information constitutes an offer to buy or sell, or a promotion or recommendation of, any security, financial instrument or product or trading strategy, nor should it be taken as an indication or guarantee of any future performance, analysis, forecast or prediction. None of the Information can be used to determine which securities to buy or sell or when to buy or sell them. The Information is provided 'as is' and the user of the Information assumes the entire risk of any use it may make or permit to be made of the Information.

**OVERALL MSCI ESG¹
QUALITY RATING IS
IN THE 66TH
PERCENTILE**



Notes: 1 Environmental, Social and Governance; 2 The overall Fund ESG Quality Score measures the ability of underlying holdings to manage key medium- to long-term risks and opportunities arising from environmental, social, and governance factors.

MSCI Fund Universe peer group: Bond Global. Number of funds in peer group: 4,035 (this figure includes multiple share classes run under the same strategy).

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THE MERITS OF ESG BOND INVESTING



**RISK
MITIGATION**



ENGAGEMENT



**BETTER
OUTCOMES**

Better risk adjusted returns

PRIVATE UK FOOD RETAILER: ICELAND

“This is the first time we
have been asked ESG
questions by a
bondholder”
CFO

The securities we talk about in this presentation today are intended only to illustrate the investment process we follow at Newton. The opinions we give during the session should not be construed as investment or any other advice. We may or may not hold the securities in our client portfolios.

Why engage?

- Private company with limited disclosure
- Strong public messaging on topics such as plastics but was there substance behind it?
- Concern around supply chain controls and key man risk

Form

- Dedicated ESG meeting with the CFO
- Subsequent follow-up questions answered by different parts of the company

Outcome

- Increased comfort company is acting responsibly on a number of topics
- Currently speaking to them about their decision to remove Palm oil from own label products
- Review company's sustainability plan that is soon to be released



UK BUILDING SOCIETY: NATIONWIDE

Given Newton's expertise in this area, we would like you to help us draft our ESG reporting and sustainability agenda.

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Better risk adjusted returns

NEWTON

Investment
Management

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Any reference to a specific security, country or sector should not be construed as a recommendation to buy or sell this security, country or sector. Past or current yields are not indicative of future yields.

Where an index is used as a comparative index, this strategy does not aim to replicate either the composition or the performance of the comparative index. Where representative data is used this is for illustrative purposes only.

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The value of overseas securities will be influenced by fluctuations in exchange rates.

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Registered Office as above.

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BNY Mellon Fund Managers Limited

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Tel: 020 7163 9000

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