

Absolute return in a hostile global debt market: Understanding the market evolution

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A structural regime change

Structural shift – the end of the Washington consensus

Central bank policy framework reviews are leading to the targeting of higher inflation

Increased role of stimulative fiscal policy, outside of countercyclical stabilisation

Growing appetite for an increased role for government in the management of economies

Larger government deficits

Monetisation of government debt

Erosion of free trade, in favour of greater localisation

Possible Implications

End to 40 years of structural disinflation = higher inflation

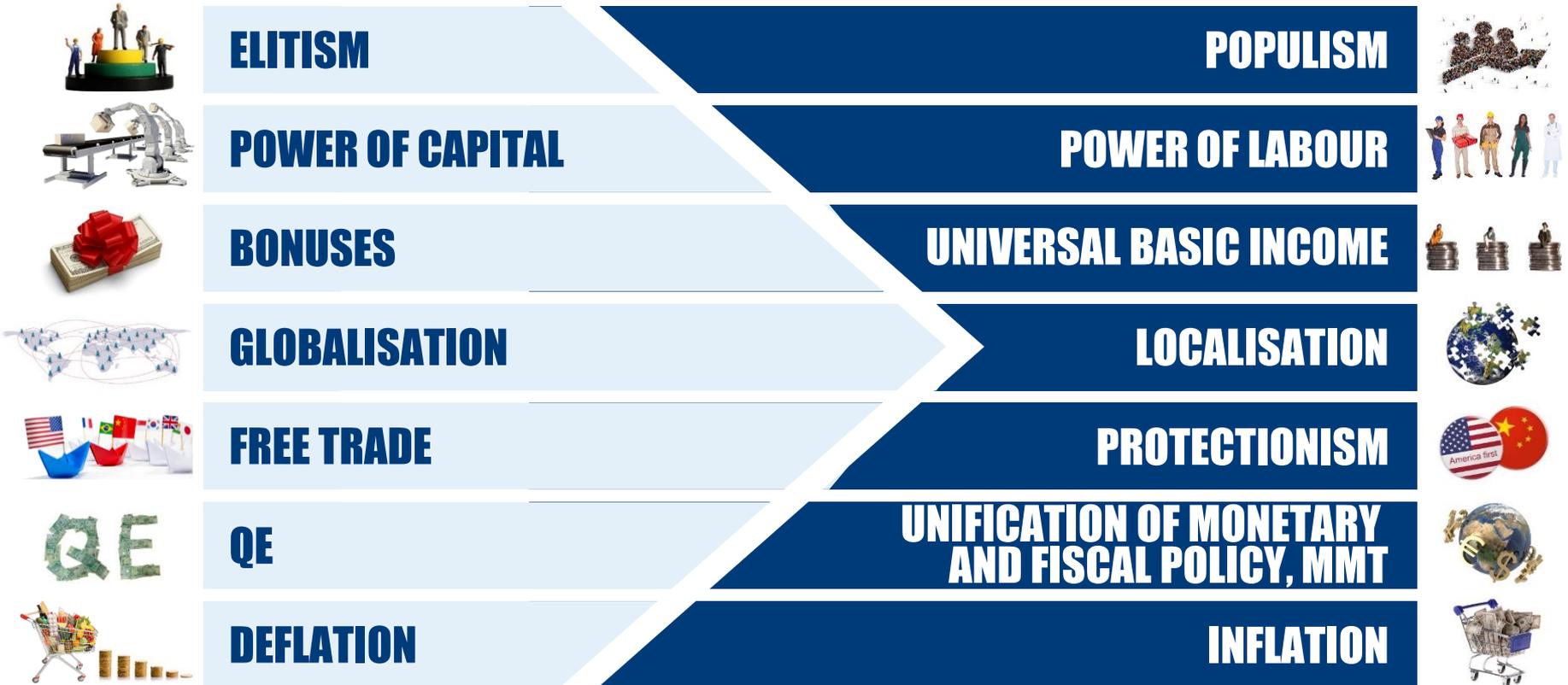
Rising government bond yields, the end of the 40-year bond bull market

Need for alternative ways to hedge

Implication for equity valuations

Opportunities for more investment in Real assets

A fast-evolving backdrop



Outlook

THE FIXED INCOME ASSET CLOCK WILL KEEP ON MOVING ROUND

2023

CENTRAL BANKS LOOSEN POLICY

- Govt. Bond → EM ↑ HY ↑

2022 - 2023

ECONOMIC OUTLOOK DETERIORATES

- Govt. Bond ↑ EM → HY ↓
- Rising corporate stress results in HY underperforming EM

GROWTH

- Accommodate monetary and / or fiscal policy
- Govt. Bond ↓ EM → HY ↑
- EM and HY significantly outperforming Govt. Bond

2022

CENTRAL BANKS CHANGE DIRECTION

- Govt. Bond ↓ EM ↓ HY →

The Future of Bonds

Green, social, sustainability and development agency bonds

GREEN BONDS

Use of proceeds bonds focused on projects with environmental benefits

SOCIAL BONDS

Social outcomes

SUSTAINABLE BONDS

Combination of green and social projects

SUSTAINABILITY-LINKED BONDS

Characteristics vary depending on whether the issuers achieve predefined sustainability/ESG objectives. Step-up in the coupon if not met

DEVELOPMENT AGENCY BONDS

The development agencies bonds can be regarded as being for environmental and/or social purposes and generally have a high credit quality

Reference section

Ideas

A distorted backdrop creates a rich set of opportunities

Government Bond

- 1** Given central bank distortions the principal use of the government bond market is to hedge other risk assets. The US Treasury market is the best place to use for this purpose
- 2** Long Italian/Spanish bonds/ Short German bonds – Spreads to compress as monetary policy stays loose
- 3** Diversify into a variety of other developed government bonds with steeper yield curves
- 4** Some exposure to inflation linked securities with a view to adding more through the year

High Yield Corporates

- 1** Preference for BBs to B or CCC – Expecting a prolonged and elevated default cycle unlike prior ones
- 2** Shorter maturities and businesses with more flexibility – Steady total return over the next couple of years
- 3** Seek opportunities in Fallen Angels as they enter the HY space
- 4** Sectors favoured – Telcos, Media, CoCos and Industrials

Investment Grade Corporates

- 1** Reduced low spread long duration credit – vulnerable in the event of a v-shaped rebound
- 2** Increasing cyclical in the mix – from a low base
- 3** Minimal potential fallen angels – very little BBB- exposure prone to “gap risk”

Emerging Market Sovereigns

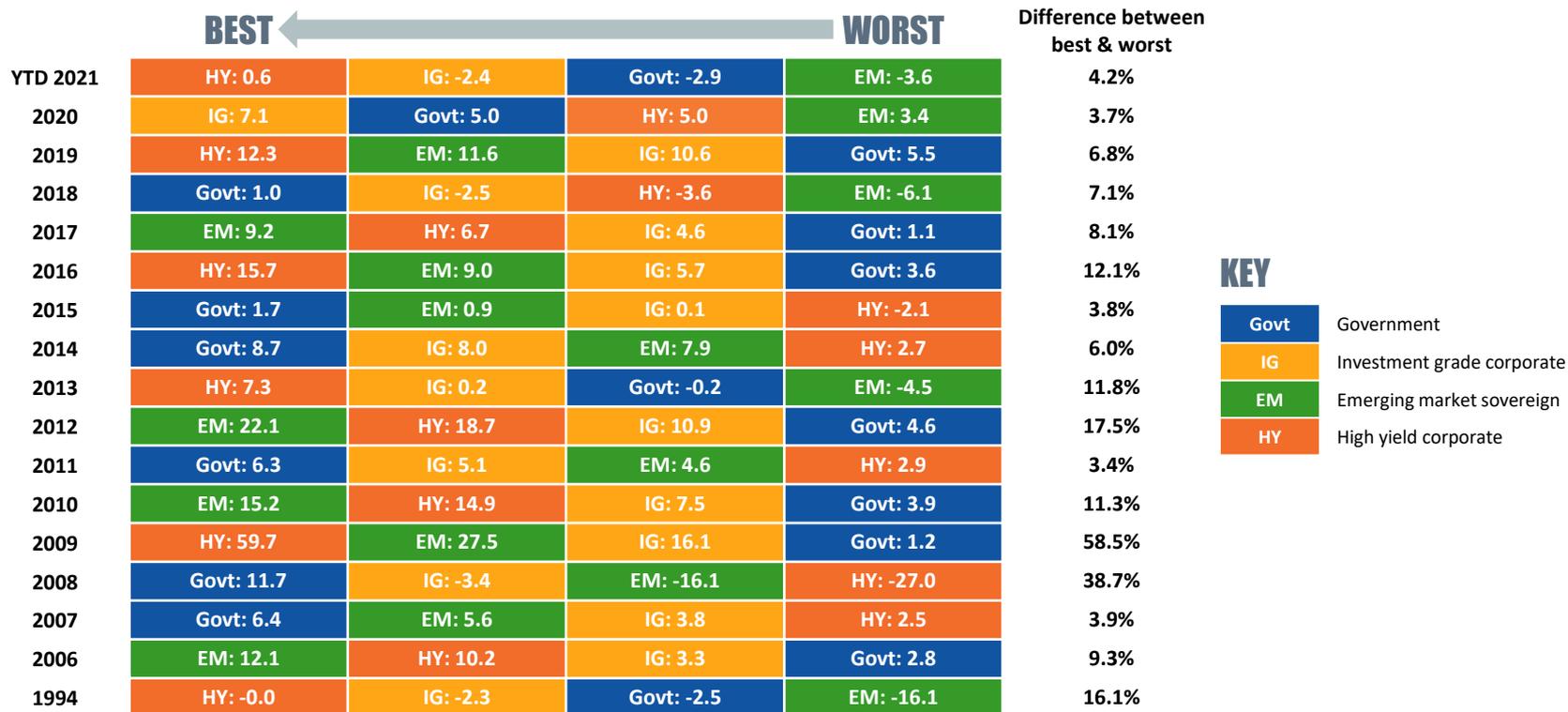
- 1** Long high quality local currency markets characterised by elevated real yields – Post vaccine developments the search for carry and yield has accelerated. Local EM characterised by steep yield curves (roll down), and possibility for currency appreciation in conjunction with increased demand for the asset class. Idiosyncratic unexpected inflationary episodes would be a primary concern
- 2** Diversified basket of hard currency issuers – Potential for continued low global rates, recovery based global stimulus packages, and return of portfolio capital flows to lower rated names provide a tailwind to the asset class as a whole. This provides us with confidence to rebuild small positions in lower rated credits. Changes to USD global liquidity and G7 interest rate expectations may cause revisions to this sentiment

Currency allocation

- 1** Bias away for the US Dollar due to a surplus of USD liquidity, high deficits and low interest rate protection
- 2** Mixture of developed and emerging market currencies on the other side that have a combination of better deficit positions and interest rate support

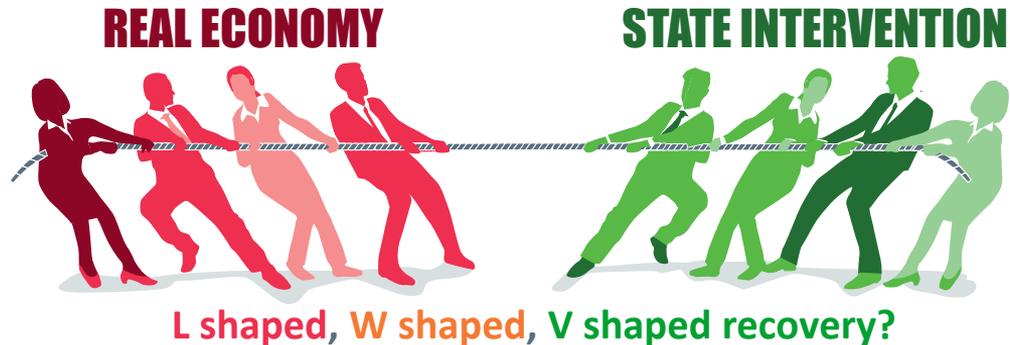
Asset class rankings constantly shift

Asset class performance rankings over time



Note: 1994 US IG and HY indices used. Please note effects of rounding.
 Source: Newton, ICE BofA indices hedged into Sterling, 28 February 2021.

An economic tug of war



ECONOMIC REALITY

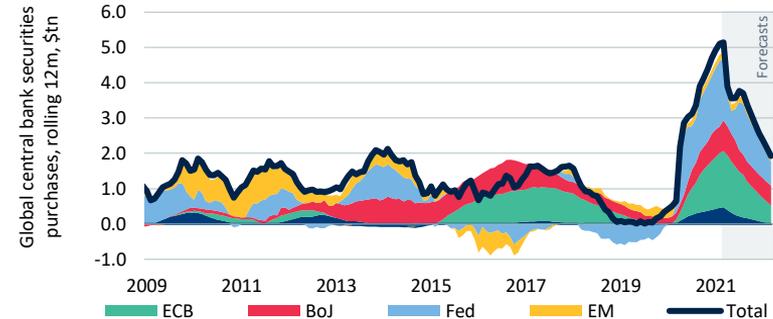
US Unemployment and Real GDP Growth



Source: Bloomberg, 30 June 2020.

THE RISING WAVE OF LIQUIDITY

Central bank asset purchases (\$trn, 12m rolling)

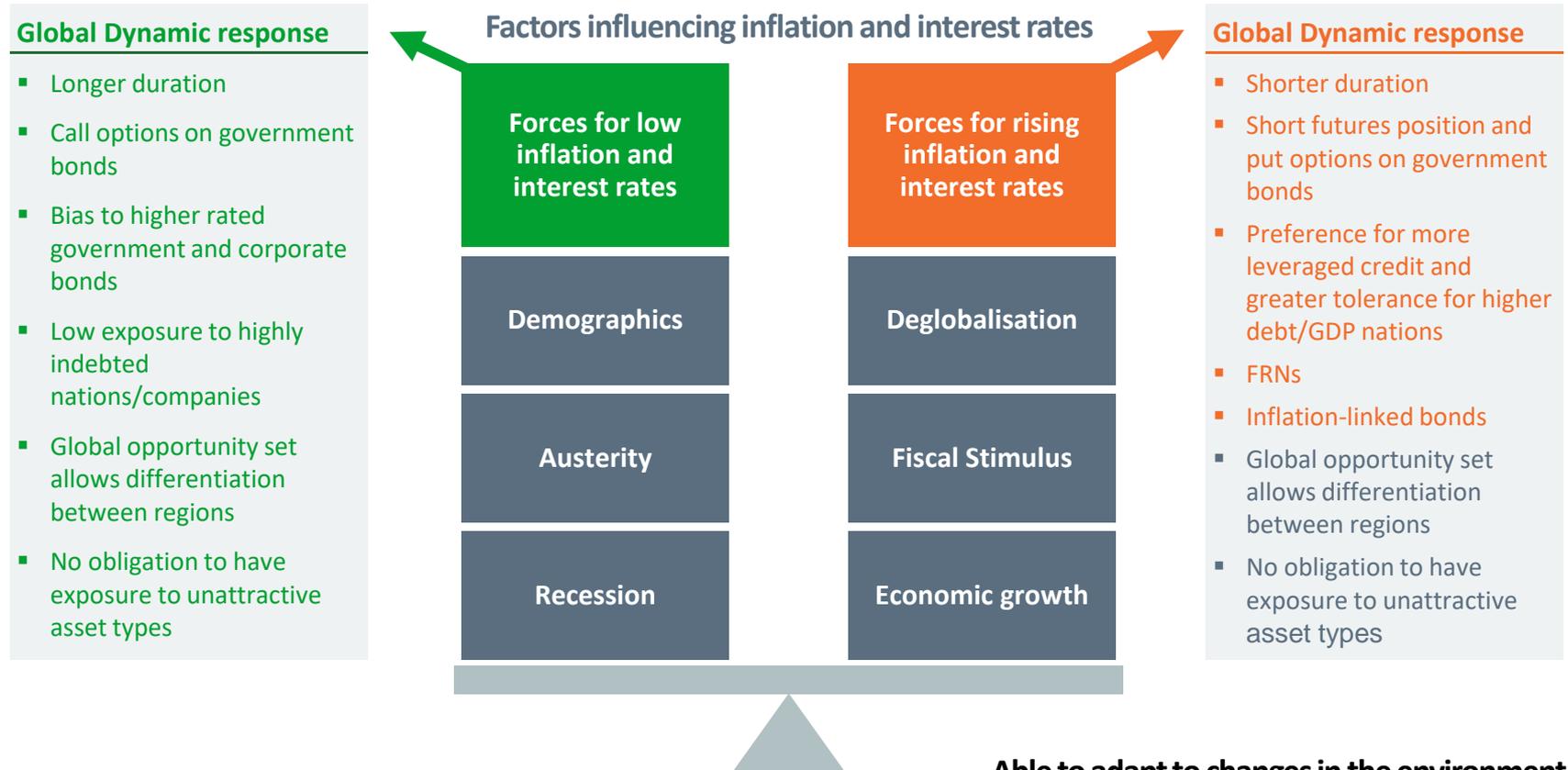


Source: National central banks, Citi Research, FTSE, 31 August 2020.



Unparalleled times

Newton Global Dynamic Bond strategy in different regimes



Focused on the opportunities



ENVIRONMENTAL REGULATION		HEALTH & WELLNESS		HEALTH-CARE ACCESS	
RESOURCE MANAGEMENT & RECYCLING		FINANCIAL INCLUSION		SOCIAL HOUSING	
RENEWABLE ENERGY		EDUCATION		GREEN FINANCING	
FOOD SECURITY		CYBER SECURITY		DEVELOPMENT AGENCIES	

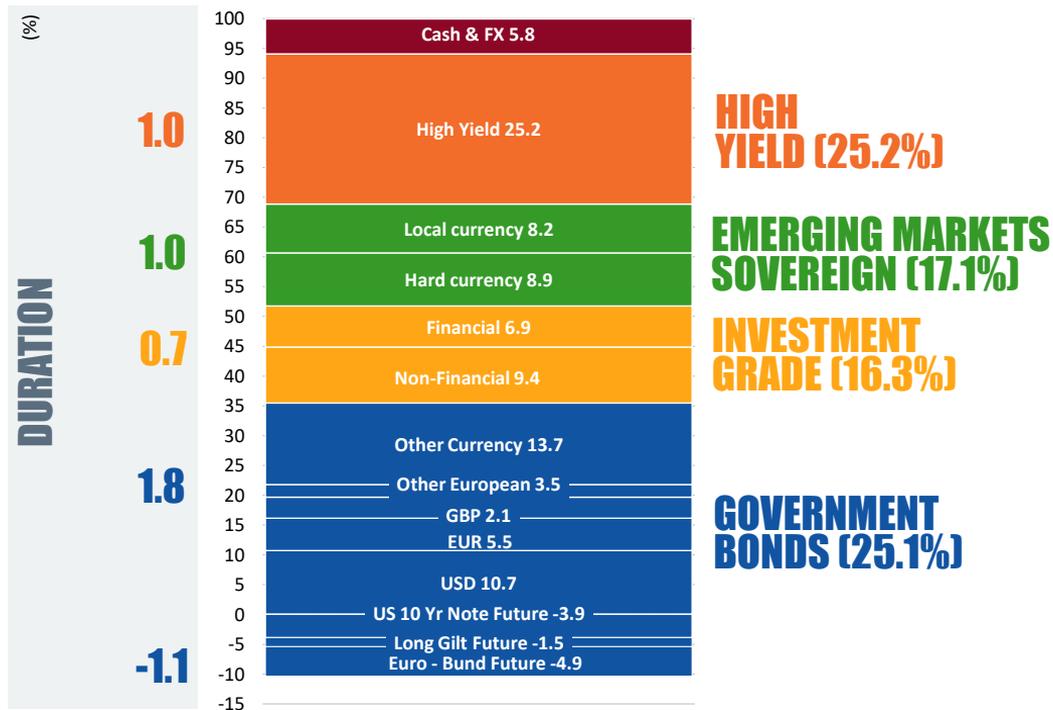
A lens for identifying investment ideas

Positioning, as at 28 February 2021

Newton Global Dynamic Bond Strategy

Newton Global Dynamic Bond representative portfolio – Notional exposure

Risk: historical range vs. current



INTEREST RATE RISK

(years)



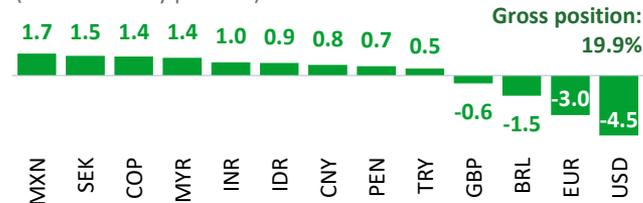
CREDIT RISK

(speculative grade asset %)



CURRENCY RISK

(% net currency position)



Source: Newton, 28 February 2021.

The representative portfolio adheres to the same investment approach as the Newton Global Dynamic Bond Strategy.

Recent engagement activity

SYNLAB

Medical Diagnostic Service.



According to the company, the first time it has had a dedicated ESG (environment, social and governance) meeting with a bond investor. Our engagement covered a range of topics. The company's commitment to ESG improvements, which include establishing new KPIs (key performance indicators), is being driven by the chief executive officer with the full support of the board. Synlab has a strong focus on health and safety, improving employee engagement and equality, continuing to put patients first and ensuring robust cybersecurity measures. There are certain areas pertaining to governance, such as board composition, where we feel more progress needs to be made. Its suitability was agreed and we added a position during the final quarter of 2020.

KANTAR

Consumer insights business.



The management team is currently in the process of creating an overview of its ESG commitments and actions. It is focused on embedding real change and will shortly publish a report showing progress, commitments and actions in a number of key areas of sustainability. Responses were also received from the company giving more detail on its approach to climate change as well as governance improvements.

UK AND IRISH BANKS



We engaged with Allied Irish Bank and Nationwide Building Society, and are awaiting responses from Coventry Building Society, Santander UK, Investec, HSBC and NatWest, in order to understand the lenders' response to Covid-19 from an ESG perspective. We looked into staff and customer treatment and what the lenders have done to help stakeholders through the crisis. While a number of initiatives were driven by the regulator, details of the individual, voluntary assistance that was provided to those in need was disclosed. We also asked how management teams plan to support staff in the aftermath of the pandemic.

INDONESIA

Sovereign.



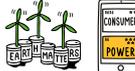
A discussion with the Bank of Indonesia and the country's Ministry of Finance focused on Indonesia's fiscal deficit financing, and the Bank of Indonesia's involvement, plus the related outlook for Indonesian rupiah stability. We also discussed the recently ratified Omnibus Law, which will introduce simplified business licensing procedures and changes to existing labour laws that should boost foreign direct investment and job creation.

Q4 2020 ESG engagement by region

Below is a breakdown by theme of the companies where we have engaged on Environmental, Social or Governance issues.

UNITED KINGDOM

- **Drax**
(Power generation)

- **National Express**
(Transport services)

- **Travis Perkins**
(Building materials distributor)

- **Tritax Big Box REIT**
(Real estate logistics)


EUROPE

- **Adevinta**
(Global online classified company)

- **AMS**
(Sensor design and manufacture)

- **SIG Combibloc**
(Aseptic packaging company)


NORTH AMERICA

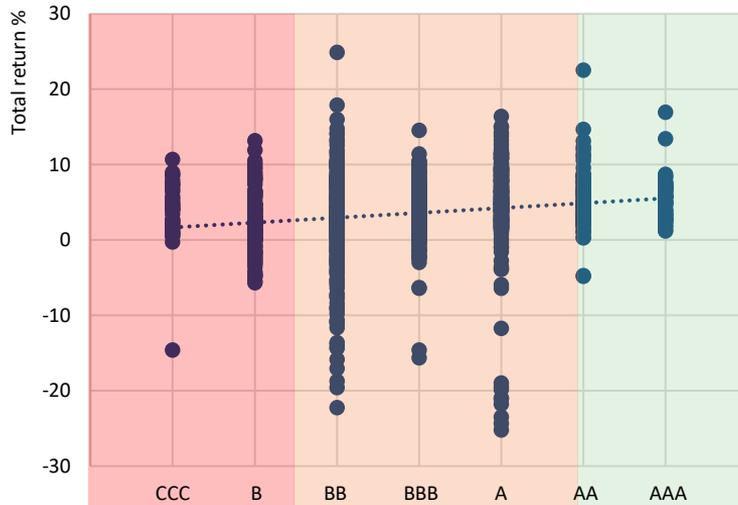
- **T-Mobile USA**
(Communication Services)

- **Tesla**
(Automotive)

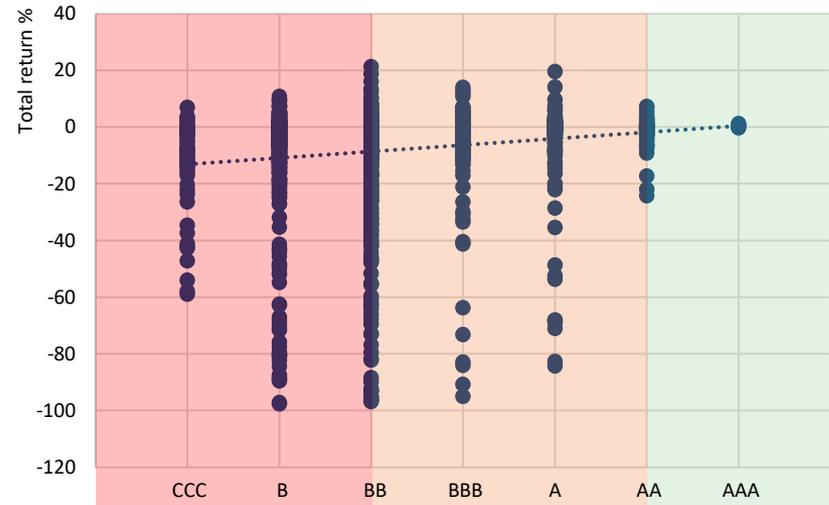

...there is a benefit of integrating ESG analysis into fixed income

- Barclays found in its 2018 study that tilting a credit portfolio in favour of bonds with high ESG ratings, tends to lead to higher performance
- Within high yield, governance factors have had the largest impact on performance
- It is not a coincidence that the weakest performers had in general weaker MSCI ESG ratings; it therefore pays to consider ESG factors within credit analysis
- Avoiding the losers is at least as important as picking the winners

MSCI ESG rating against total return
US investment grade index (1 Jan 2020 – 30 June 2020)



MSCI ESG rating against total return
US high yield index (1 Jan 2020 – 30 June 2020)



For illustrative purposes only. No investment strategy or risk management technique can guarantee returns or eliminate risk in any market environment. Source: ICE Bank of America Merrill Lynch Indices, MSCI ESG Research, Newton, total return, 31 December 2019 to 30 June 2020.

Key risks

Newton Global Dynamic Bond Strategy

Investment performance

12 month returns, %	Dec-19 to Dec-20	Dec-18 to Dec-19	Dec-17 to Dec-18	Dec-16 to Dec-17	Dec-15 to Dec-16
Composite (gross)	3.71	6.21	-0.17	2.25	4.80
Composite (net)	3.35	5.84	-0.52	1.89	4.43
Performance aim	2.36	2.72	2.62	2.33	2.44

Calendar year returns, %	2020	2019	2018	2017	2016
Composite (gross)	3.71	6.21	-0.17	2.25	4.80
Composite (net)	3.35	5.84	-0.52	1.89	4.43
Performance aim	2.36	2.72	2.62	2.33	2.44

Performance is stated gross of management fees. The impact of management fees can be material. A fee schedule providing further detail is available on request.

The strategy aims to deliver a minimum return of cash **(1 month GBP LIBOR) +2% p.a.** over 5 years before fees. However, a positive return is not guaranteed and a capital loss may occur.

Key investment risks

- **Past performance is not a guide to future performance. Your capital may be at risk. The value of investments and the income from them can fall as well as rise and investors may not get back the original amount invested. Tax treatment depends on the individual circumstances of each client and may be subject to change in the future. Newton is not a tax expert and independent tax and/or legal advice should be sought.**
- **Performance Aim Risk:** The performance aim is not a guarantee, may not be achieved and a capital loss may occur. Strategies which have a higher performance aim generally take more risk to achieve this and so have a greater potential for returns to vary significantly.
- **Currency Risk:** This strategy invests in international markets which means it is exposed to changes in currency rates which could affect the value of the strategy.
- **Derivatives Risk:** Derivatives are highly sensitive to changes in the value of the asset from which their value is derived. A small movement in the value of the underlying asset can cause a large movement in the value of the derivative. This can increase the sizes of losses and gains, causing the value of your investment to fluctuate. When using derivatives, the strategy can lose significantly more than the amount it has invested in derivatives.
- **Changes in Interest Rates & Inflation Risk:** Investments in bonds/money market securities are affected by interest rates and inflation trends which may negatively affect the value of the strategy.
- **Credit Ratings and Unrated Securities Risk:** Bonds with a low credit rating or unrated bonds have a greater risk of default. These investments may negatively affect the value of the strategy.
- **Credit Risk:** The issuer of a security held by the strategy may not pay income or repay capital to the strategy when due.
- **Emerging Markets Risk:** Emerging Markets have additional risks due to less-developed market practices.
- **CoCos Risk:** Contingent Convertible Securities (CoCos) convert from debt to equity when the issuer's capital drops below a pre-defined level. This may result in the security converting into equities at a discounted share price, the value of the security being written down, temporarily or permanently, and/or coupon payments ceasing or being deferred.
- **Counterparty Risk:** The insolvency of any institutions providing services such as custody of assets or acting as a counterparty to derivatives or other contractual arrangements, may expose the strategy to financial loss.

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