

# Newton Balanced Bridge Fund

Investment Report - Second Quarter 2011

► A BNY MELLON COMPANY<sup>SM</sup>

**NEWTON**  
The Power of Ideas



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# Fund information

## Long-term track record

The Newton Balanced Bridge Fund has returned 105.7% since launch (23 December 1998), which is equivalent to 5.9% per annum. This is an outperformance of 1.4% per annum compared to the fund's benchmark. For more detail on the fund's long-term performance, please refer to page 4.

## Aim

To achieve income and capital growth over the long term through a portfolio that is predominantly invested in equities, across a wide range of industries and countries. The equity element is balanced by cash, bonds and exposure to alternative assets, such as hedge funds, to reduce the overall volatility of the portfolio. The fund is managed in line with the Newton Private Investment Management Income and Growth Model. The central asset allocation for the model is 60% invested in global equities and 40% invested in other asset classes which may include bonds, cash, hedge funds, structured products and property.

## Expected characteristics

Return: Significantly above cash over the long term; variable in the short term.

Volatility of return: Medium. Investors can expect to experience significant fluctuations in the value of their holding, driven to a large extent by rises and falls in equity markets.

Income: Medium, and the dividend is likely to grow over the long term. Please note that the frequency of the dividend has increased from semi-annually to quarterly. Please see pay dates below.

## Performance references

Newton Balanced Composite (benchmark), ARC Sterling Steady Growth, WM Private Client Balanced Indicator. The Newton Balanced Composite benchmark comprises 40% FTSE All Share, 20% FTSE World ex UK, 15% FTA Govt All Stocks, 15% ML Sterling Non-Gilts & 10% 1 month £ LIBOR.

## Risk profile

Suitable for investors with a medium risk profile.

## Fund facts

Fund size (millions):	GBP 309	Ex dividend dates:	End Jan, Apr, Jul & Oct
Annual management charge:	0.8%	Pay dates:	2 business days before end Mar, Jun, Sep & Dec
Total expense ratio:	0.83%	Last distribution:	1.4462p per unit
Base currency:	GBP	ISIN	GB0004833660
Dividend yield:	3.5%	Sedol	0483366

# Focus on the latest quarter

## Performance over three months

<b>Newton Balanced Bridge</b>	<b>-0.1%</b>				
Newton Balanced Index	1.5%	ARC £ Steady Growth est.	0.4%	WM PCI Balanced	1.5%
FTSE All Share	1.9%	FTSE W World (ex UK)	0.3%	FTA Govt All Stocks	2.5%

Source: Lipper, Datastream, ARC & WM, as at 30 June 2011. Calculation basis: Sterling, total return, bid to bid, without initial charges, net income reinvested, net of management fees.

## Major contributors to relative performance

Positive	%
Roche Hldgs AG	0.17
Shenguan Holdings Group Ltd	0.15
Scottish & Southern Energy PLC	0.15
Go-Ahead Group PLC	0.13
Novartis AG	0.12

Negative	%
Huabao Intl Holdings Ltd	-0.34
Hypermarcas SA	-0.25
Barrick Gold Corp	-0.24
Petroleo Brasileiro SA	-0.16
HTC Corporation	-0.15

## Significant transactions

Acquisitions
DnB NOR ASA
United Overseas Bank Ltd
Pandora A/S
Prudential PLC
Inpex Corp.

Disposals
Tele Norte Leste Participacoes S/A
DBS Group Holdings Ltd
Britvic PLC
Rossi Residencial S/A
Oil Search Ltd

Note: Portfolio holdings are subject to change at any time without notice and should not be construed as investment recommendations.

## Fund manager report

Markets traversed an assault course of challenges this quarter: rising commodity prices hitting consumers and companies alike, the EU debt crisis baton passing between Greece, Ireland, Portugal and finally back to Greece, partisan stand-off over the imminent US debt ceiling and the implementation of austerity measures to name but a few. Only during the final few days of June, once the Greek government passed an austerity bill that once again opened the gates to a further bailout, did markets surge, reversing their earlier losses.

The net result of this for markets was an unexciting return for world equities of 0.3% (FTSE World ex UK), with the UK market faring better, up 1.9% (FTSE All Share) over the quarter. However, the fund was impacted by the performance of Emerging Markets, which ended the quarter down

1.4% (FTSE Secondary Emerging Markets). UK Gilts, defied inflationary fears and returned 2.5% as investors took shelter from the volatility of equity markets. Against this backdrop, your Fund returned -0.1% over the quarter, bringing the total return for the first half of the year to 0.9%.

As highlighted, performance has been impacted by the falls in the Asia Pacific and Latin American financial markets, to which the fund has greater exposure than the benchmark. Huabao (-41%) and Hypermarcas (-29%) proved particularly detrimental to performance. These markets tend to be more volatile than Western markets and, therefore, when they fall (and rise) the impact can be greater on equity values. The sell off was triggered firstly by fears that monetary tightening (increasing interest rates and bank capital reserve

requirements) to combat inflation would slow growth in China. However, Premier Wen Jiabao indicated in his recent visit to the UK that China is nearing the end of this tightening cycle and claimed that the government's success in controlling inflation means that their areas of focus now includes growth. Economic data released this week indicates that growth in China over the last three months has grown slightly more than anticipated, by 9.5% compared to the same period last year; Western growth rates look rather insipid in comparison. Secondly, a number of accounting scandals among smaller Chinese companies raised concerns about the whole mid-cap sector and caused further indiscriminate selling. Many of the companies that suffered are extremely well managed and we believe the market will start to differentiate again over time.

Within the Fund, exposure to China is focused on the consumer, as we anticipate that the number of people achieving earnings which will propel them into the consumer class will rise significantly over the next few years. As an additional boost to this subset of the population, the government recently announced that they are implementing a program in September 2011 to cut income tax, which is forecast to increase middle class disposable incomes by 18-27%, and hopefully boost consumer demand. Importantly, we also continue to expect growth in global GDP to be driven by emerging markets over the longer term. Therefore, although volatile in the short term and detrimental to the performance of your fund over the recent quarter, we remain invested with a long term view and retain exposure to the emerging market consumer, inline with our *Global Realignment* theme. Indeed, we have used the sell off to reposition the fund to add preferred stocks that were previously considered too expensive, for example, Man Wah Holdings, the Chinese sofa manufacturer and retailer.

Against uncertain conditions globally, we take guidance from our investment themes which keep us focused on the longer term drivers of growth. In line with our by our *All Change* theme the Fund continues to hold a core of defensive holdings in the healthcare and utility sectors, both of which performed well during the quarter compared to the more cyclical oil and gas, and basic material sectors. Elsewhere, mobile telecommunication companies started to price in concerns over revenue pressure as more telephone calls are made over data networks and in anticipation of this, Vodafone was significantly reduced. *Earth Matters* remains an important theme in terms of positioning, and high crop prices and late planting in the US caused further uncertainty. We took

advantage of the fall in basic material stocks to add the phosphate and potash producer, Mosaic, to the Fund.

With the stark exception of peripheral Europe, government bond yields fell globally, delivering positive returns and the UK was no exception. We remain concerned about the longer term outlook for government bonds given the negative real (inflation adjusted) returns and the structural issues facing the backing of sovereign debt and hence only partially benefited as we are lightly positioned in this area. Corporate bonds supplement the government bond exposure.

Weaker global economic numbers have already had a knock-on effect on energy and commodity prices. This should moderate concerns about runaway inflation, cool expectations about policy tightening and ultimately help to support growth expectations. This environment of continued low interest rates remains favourable for equities, which remain our preferred asset class, where we can still see growth opportunities at un-demanding valuations, not to mention attractive dividend yields.

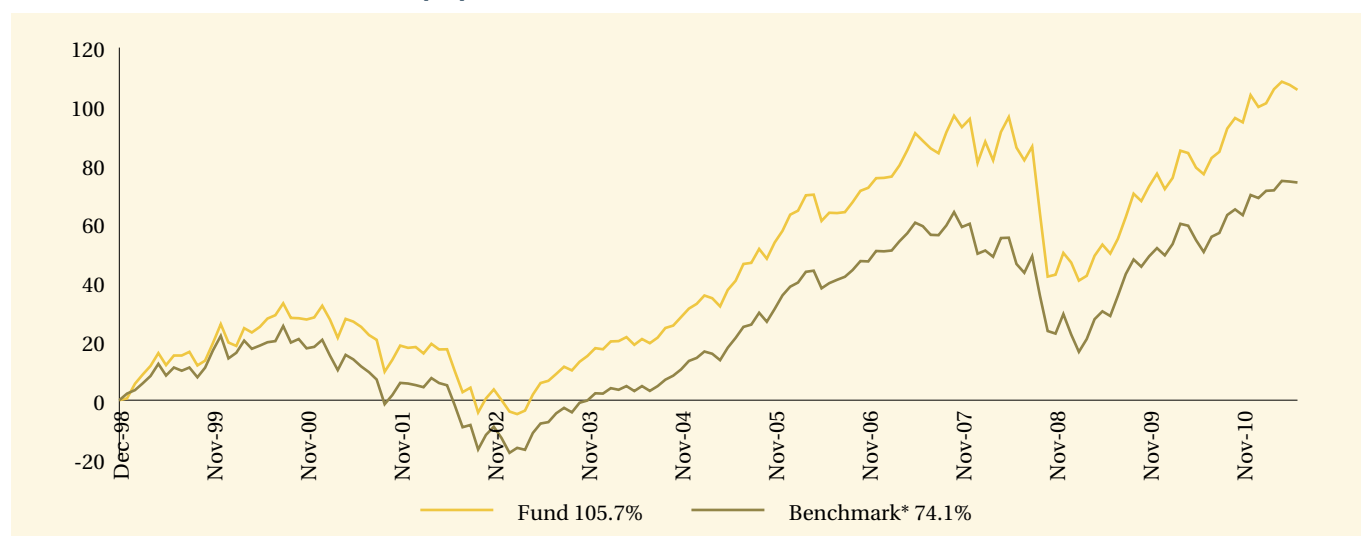
The swings in energy prices illustrate the sort of volatile mini-cycle environment that we appear to be experiencing as we work through the global debt crisis. The scale of the liabilities and the number of economies involved places an unprecedented drag on global economic activity. It has in turn, however, unleashed an equally unprecedented reflationary response in terms of monetary and fiscal intervention. The interaction between these two forces has created a volatile backdrop, against which investors' focus switches back and forth between fears of recession and continuing economic recovery. We have suggested that this kind of schizophrenic environment could persist, perhaps for many years, and that investors should construct their portfolios accordingly. This means being vigilant about what to own (there are very real solvency risks to contend with) and trying to focus on assets that can generate real cash flows from reliable sources.

**Fund management team:**

**Julie-Ann Ashcroft and Caroline Tye**

# Long-term performance

## Performance since launch (%)



	2002	2003	2004	2005	2006	2007	2008	2009	2010	YTD 2011
Fund	-15.1	17.7	11.5	20.2	11.4	11.5	-23.3	17.9	15.1	0.9
Benchmark*	-17.5	17.5	10.8	19.6	11.1	6.1	-19.2	17.4	11.9	2.5

## Discrete past performance (%)

From	30/06/06	30/06/07	30/06/08	30/06/09	30/06/10
To	30/06/07	30/06/08	30/06/09	30/06/10	30/06/11
Fund	14.9	-1.2	-19.4	18.1	16.2

Source: Lipper, WM, Datastream & Bloomberg, as at 30 June 2011. Calculation basis: Sterling, total return, bid to bid, without initial charges, net income reinvested, net of management fees.

\*The benchmark to 31 March 2009 was WM PCI Balanced. Thereafter it is the Newton Balanced Composite. The Newton Balanced Composite benchmark comprises 40% FTSE All Share, 20% FTSE World ex UK, 15% FTA Govt All Stocks, 15% ML Sterling Non-Gilts & 10% 1 month £ LIBOR.

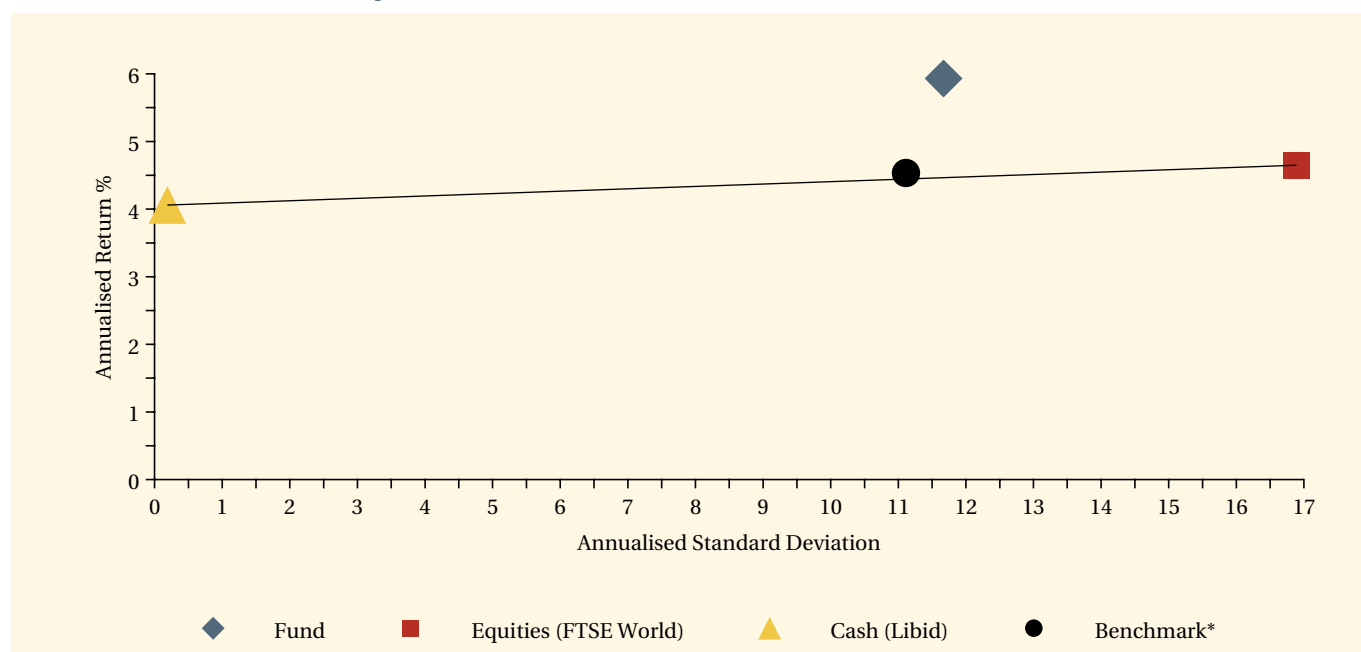
## Risk factors

The performance data shown on this report is past performance; as such it is not a guide to future performance.

Investors should remember that unit trusts should be regarded as long-term investments and that the value of units, and the income from them, can go down as well as up due to stock market and movements in exchange rates. When you sell your investment you may get back less than you originally invested. The fund may invest in emerging markets which are, by their nature, higher risk and potentially more volatile than those inherent in established markets.

# Long-term performance - risk and reward

## Fund return and volatility since launch



This chart shows both return and volatility. The Newton Balanced Bridge Fund has given a higher return than cash, world equities and the benchmark with slightly higher volatility than that of the benchmark. The launch date of the fund was 23 December 1998.

## Risk and return since launch

	Annualised Return	Volatility	Sharpe ratio
Fund	5.9%	11.7%	0.2
Benchmark*	4.5%	11.1%	0.0

Source: Lipper, WM, Datastream & Bloomberg, as at 30 June 2011. Calculation basis: Sterling, total return, bid to bid, without initial charges, net income reinvested, net of management fees.

\*The benchmark to 31 March 2009 was WM PCI Balanced. Thereafter it is the Newton Balanced Composite. The Newton Balanced Composite benchmark comprises 40% FTSE All Share, 20% FTSE World ex UK, 15% FTA Govt All Stocks, 15% ML Sterling Non-Gilts & 10% 1 month £ LIBOR.

# Newton's investment process

Newton is a global thematic stock picking company. Our style is inclusive and relies on effective communication between all of our investment personnel.

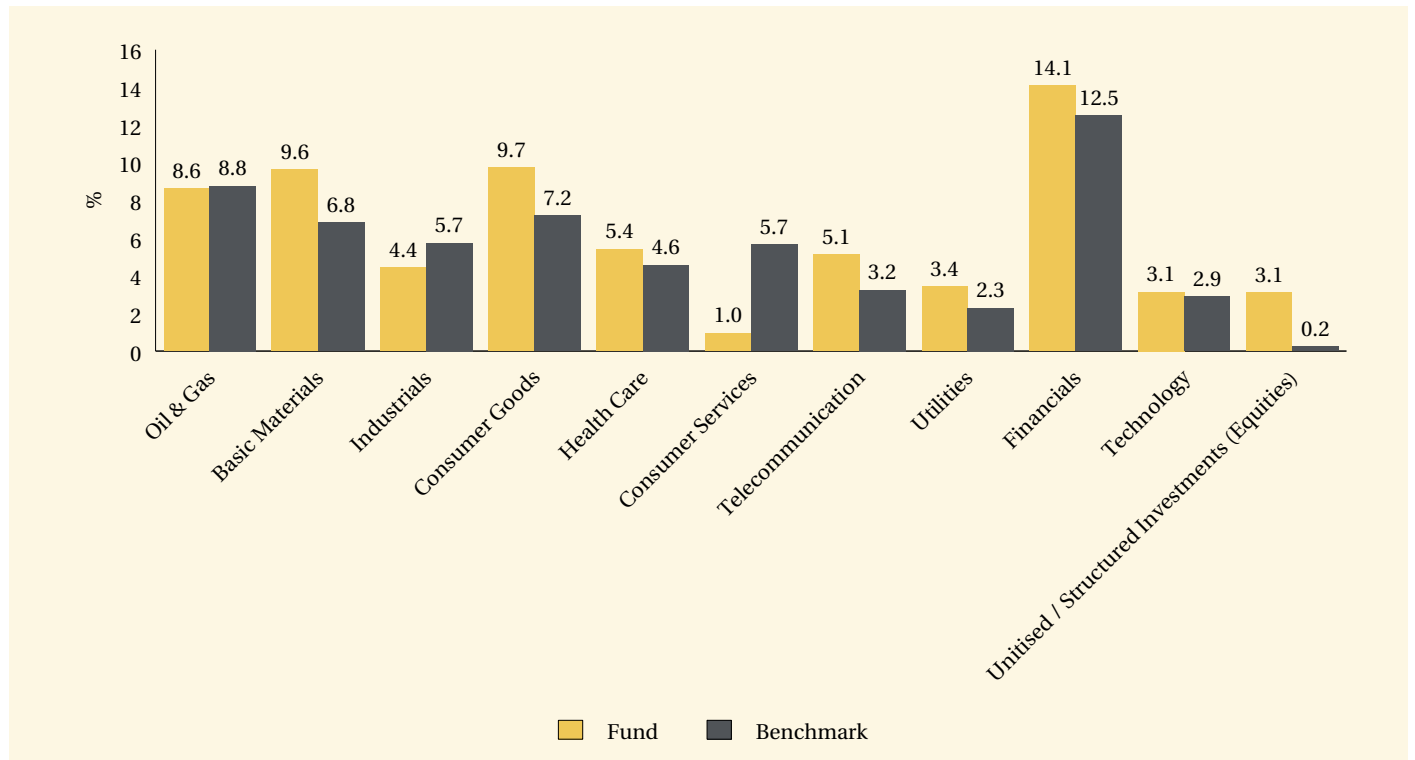
Strategy groups	Representatives from the strategy team, fund managers and research analysts identify global themes and formulate our economic view.
Research team	Global sector analysts, supported by fund managers, identify investment opportunities within the thematic backdrop.
Fund management	Fund managers debate with analysts the appropriate valuations for purchases and sales, then construct portfolios to match up Newton's investment thinking with client objectives and risk profile.

Several of these themes are listed below, along with examples of individual holdings.

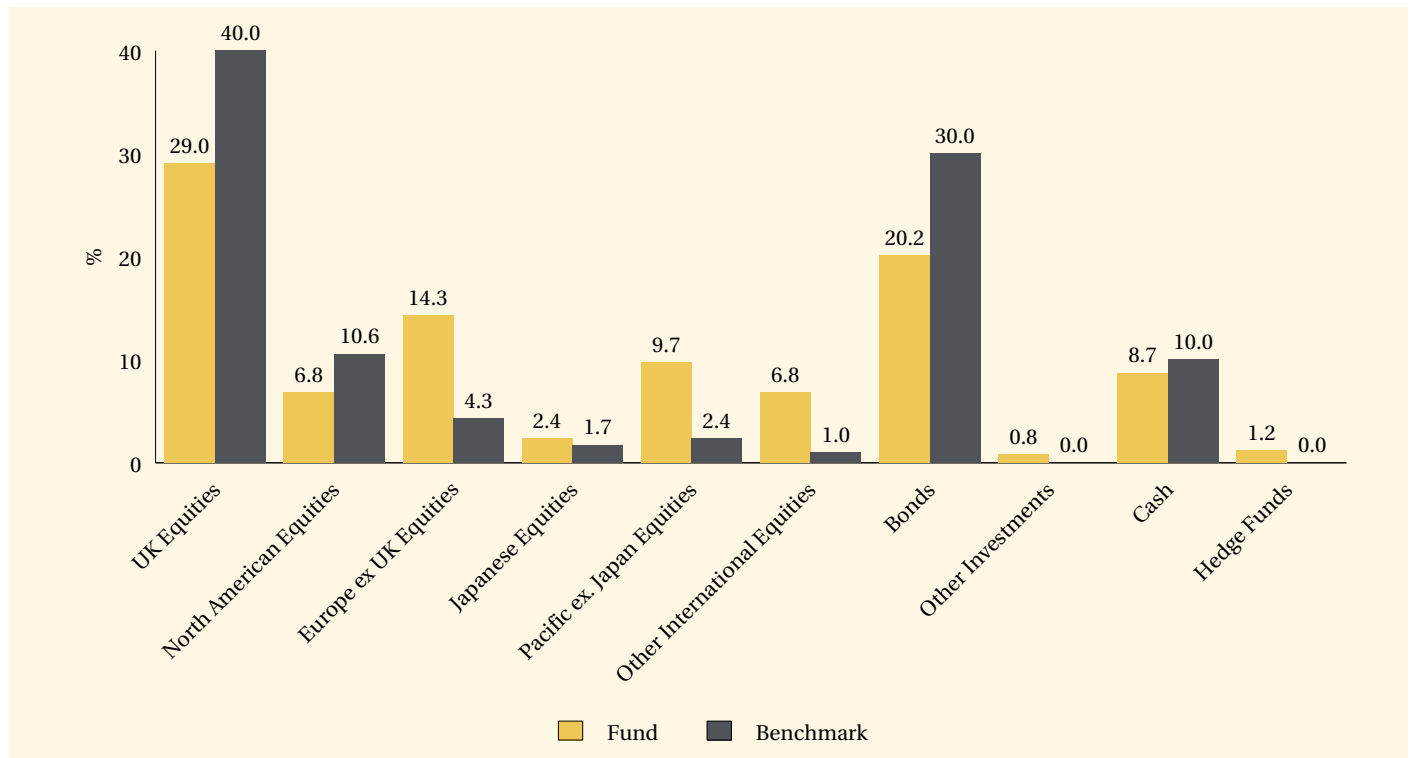
Theme	Factors	Investments
All change	The popping of the credit bubble has marked an end to the era of rapid growth in private sector debt in the developed world. Structurally impaired financial systems and regulatory burdens ensure that credit will be less freely available, and this has profound implications for consumer-driven economies, all asset classes and investment strategies.	Barrick Gold, GSK, infrastructure funds, Jardine Lloyd Thompson, Newcrest Mining, Scottish & Southern
Developing economies	The influence of the developing world on the global economy continues to grow, and developing economies ultimately are on a convergence course, in terms of demographics and consumption trends, with the industrialised world. This long-term secular trend will entail the development of Western-style health and social security systems and will involve significant cyclical influences as well as frictions regarding trade policies.	Bangkok Bank, Hutchison Ports, Hypermarcas, Mapletree Logistics, Natura Cosméticos, Petrobras, Rei Agro
Networked world	Although networks have already transformed our lives, the trend remains at a relatively early stage. Rapid increases in bandwidth continue to increase networks' range of uses and their interactivity, which in turn is driving productivity gains. The explosive growth of mobile internet, combined with innovations in sensor technology, will generate profound changes in many industries.	Applied Materials, HTC, MTN, Sprint, Telekomunikacja Polska
Medical Technology	Increasingly ageing, affluent and active populations demand products and services that enhance and maintain lifestyles in addition to treating more serious medical conditions. New technologies, materials and services are continually improving the performance of existing products and procedures. Developing world demand for healthcare is rising and, in Western healthcare systems, a key challenge is to improve the efficiency of delivery by adding technology to currently archaic networks.	Bayer, GSK, Novartis, Roche

# Fund analysis

## Equity weightings by industry



## Regional and asset class weightings



Source for all charts: Newton, as at 30 June 2011.

# Glossary

## ARC private client indicators

ARC Private Client Indicators are unique in that they are based on actual (as opposed to model) client portfolio returns provided by various investment management companies. These portfolio returns are allocated to one of four categories ("Cautious", "Balanced Asset", "Steady Growth" and "Equity Risk", in order of increasing volatility) based on the volatility of the returns relative to world equities, and an average return is calculated for each category. This is a departure from the traditional approach of comparing the performance of portfolios with similar asset allocations. It assumes that investment managers may use whatever asset allocation they deem appropriate to achieve the desired levels of return and volatility.

## Bonds

Tradable debt issued by governments, quasi government bodies or companies. Interest is usually fixed until maturity and paid either annually or semi-annually. The bond (debt) is repaid by the issuer at maturity.

## Derivatives

Instruments of a fixed maturity, the price of which is dependent upon the price of an underlying asset or variable: most commonly an interest rate, an index, a currency, an equity, a bond or a commodity. Depending on the type of instrument used, derivatives can provide the opportunity to benefit from a fall in the price of the underlying asset or from a rise. Different derivative strategies can therefore be used to hedge exposure to the underlying and to gain exposure to the underlying. Derivatives include futures, forwards, options and swaps.

## Dividend yield

The annual income (dividend) received from an equity or an investment fund divided by the price of the equity or the fund, expressed as a percentage. Dividends are typically paid semi-annually.

## Equity

Also known as a company share. A security that gives the holder fractional ownership of a company. Equities usually confer the right to vote at shareholder meetings and to receive a dividend if one is paid.

## Hedge funds

Unregulated funds with wide investment powers, which typically include the ability to hold short positions (ie, selling an asset the fund does not own in order to profit from a fall in the asset's value), and to use leverage (ie, borrowing to invest, which magnifies profits and losses). There are an enormous number of possible investment strategies. For our clients Newton gains exposure to these funds mainly by investing in listed investment trusts and companies that invest in hedge funds.

## IMA sector averages

The Investment Management Association (IMA) classifies pooled funds with similar objectives into broad sectors (eg, Global Growth, Active Managed, UK All Companies). The average performance of all the funds within a sector is calculated over various time periods to provide investors with a performance comparator.

## Index-linked bonds

Bonds with interest and capital repayment linked to inflation.

## Performance reference

In the context of investment funds, a measure or measures against which the performance of a fund or portfolio can be compared. These tend to be either an index, a combination of indices, or a peer group of comparable funds.

# Glossary

## Property

In this context we are referring to investment in commercial property. Exposure to this asset class is achieved through investment in property investment trusts and REITs.

## Risk

In this context we define risk as the volatility (ie, variability) of returns, as measured by standard deviation.

## Risk profiles – Newton definitions

*Medium risk:* appropriate for clients who are seeking a return in excess of inflation over the long term and are willing to take capital risk to achieve objectives. Portfolios are well diversified (directly, or indirectly through pooled funds) but may contain a high allocation to a single asset class, such as equities.

*High risk:* appropriate for clients who are willing to take significant capital risk to achieve objectives. This category includes portfolios containing only equities, and those containing significant exposure to high-risk funds, smaller companies, venture capital or private equity. It also includes portfolios that are made up of concentrated lines of stock, which reduces the level of diversification.

## Sharpe ratio

A measure of risk-adjusted return. The excess return (in this case, the return above cash) is divided by the standard deviation of returns. A higher number suggests a more efficient mix of returns and volatility.

## Standard deviation

A statistical measure of the variability of returns. The higher the number, the greater the variability of returns. For a normally distributed set of data, 68% of the returns are forecast to occur within one standard deviation of the average, 95% within two times the standard deviation. For example, two investments have an average return of 5%, investment A has a standard deviation of 5% and investment B has a standard deviation of 2%. In 68% of cases, we would expect investment A to return between 0% and +10% (average return of 5% +/- 5% standard deviation) and investment B to return between 3% and 7% (5% +/- 2% standard deviation).

## Total expense ratio

The total costs of the fund, made up principally of the annual management charge, but also including operating costs such as legal, administration, trustee and audit fees.

## Volatility

In this context the variability of investment returns, as measured by the standard deviation. The higher the figure the more variable the return of an investment.

## WM private client indicators

The WM Company surveys investment companies to ascertain the exposure of their principal private client model portfolios by asset class (eg, equities, bonds, hedge funds, etc) and geography. From this they derive an average portfolio in each of the categories “growth”, “balanced” and “income”. The appropriate market index return (eg, FTSE All Share, FTSE Government All Stocks) is then applied to the various elements of the three representative portfolios to generate a benchmark return for each category.

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Newton Balanced Bridge Fund

**Newton Investment Management Limited**

020 7163 9000  
privateclients@newton.co.uk

**London**

BNY Mellon Centre  
160 Queen Victoria Street  
London EC4V 4LA

**Edinburgh**

2 Festival Square  
Edinburgh EH3 9SU

**Leeds**

No.1 Whitehall Riverside  
Leeds LS1 4BN

