

Newton Real Return Fund

Investment Report - Third Quarter 2011

▶ A BNY MELLON COMPANYSM

NEWTON
The Power of Ideas



Contents

Fund information	1
Focus on the latest quarter	2
Long-term performance	4
Long-term performance - risk and reward	5
Newton's investment process	6
Glossary	7

Fund information

Long-term track record

The Newton Real Return Fund has returned 99.6% since relaunch (31 March 2004), which is equivalent to 9.7% per annum. This is an outperformance of 2.1% per annum compared to the fund's benchmark. For more detail on the fund's long-term performance, please refer to page 4.

Prior to 30 June 2009, the Fund was called the Newton Absolute Intrepid Fund.

Aim

To achieve capital growth in sterling terms over the long term from an unconstrained, actively managed multi asset strategy. The manager of the Fund has maximum flexibility at the asset allocation level and emphasis is placed on long term investing. The Fund is intended to have lower absolute volatility than traditional equity biased funds, but will exhibit volatility relative to its benchmark.

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.

Performance references

1 month £ Libor +4% p.a. (benchmark), ARC £ Steady Growth, IMA Absolute Return.

Risk profile

Suitable for investors with a medium risk profile.

Fund facts

Fund size (millions):	GBP 4,363	Ex dividend dates:	01 Jan, 01 Jul
Annual management charge:	1.0%	Pay dates:	28 Feb, 30 Sep
Total expense ratio:	1.12%	Last distribution:	5.5906p per unit
Base currency:	GBP	ISIN:	GB0006780323
Dividend yield:	3.4%	Sedol:	0678032

Focus on the latest quarter

Performance over three months

Newton Real Return	-4.7%				
1 month £ Libor +4% p.a.	1.2%	ARC £ Steady Growth (est)	-8.6%	IMA Absolute Return	-2.4%

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

Significant transactions

Acquisitions
UK Treasury Stock 5% 7/03/2012
ETFS Physical Gold 0% Secured Note (USD)
Total S.A.
Norway (Kingdom of) 4.5% Bds 22/05/2019
TDC A/S

Disposals
ETFS Agriculture DJ-AIGSM 0% Sec. Note USD
Royal Dutch Shell PLC (CL B)
Advanced Info Service PCL
Adaro Energy
GlaxoSmithKline PLC

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

Fund manager report

Market background and performance

The third quarter of 2011 turned out to be one of the most challenging quarters for risk assets in recent years. Even the equity of our favoured stable companies, which offered ostensibly the attractive characteristics of good earnings visibility and dividend yield support, was severely punished in the indiscriminate widespread sale of assets. The portfolio lost value during this period and experienced some volatility on a daily marked-to-market basis. Nevertheless, we maintain our focus upon distinguishing such mark-to-market volatility from the genuine risk of losing money and suffering permanent diminution of value. Portfolio protection played a significant role over the third quarter by helping to preserve capital and reducing the volatility of the fund. The wild fluctuations of

risk assets during this period led to an increase in activity of protective positions on the Fund, while the 'core' of the portfolio changed very little. We employed options on the UK FTSE 100, the US S&P 500 and the Hang Seng Index, as well as a call option on the US long bond future. Securities that appreciated in value (in sterling terms) included tobacco producer Reynolds American, Japanese beverage producer Asahi and China Mobile. The position in the longer dated US Treasury index linked bonds benefited from the general government bond market rally, as well as from the appreciation of the US dollar. Norwegian bonds also increased in value, and the krone gained support from its perceived 'safe haven status'. Securities that fared particularly poorly included the equity of Petroleo Brasileiro, Sprint Nextel, Bayer and BP; some high yield corporate bonds

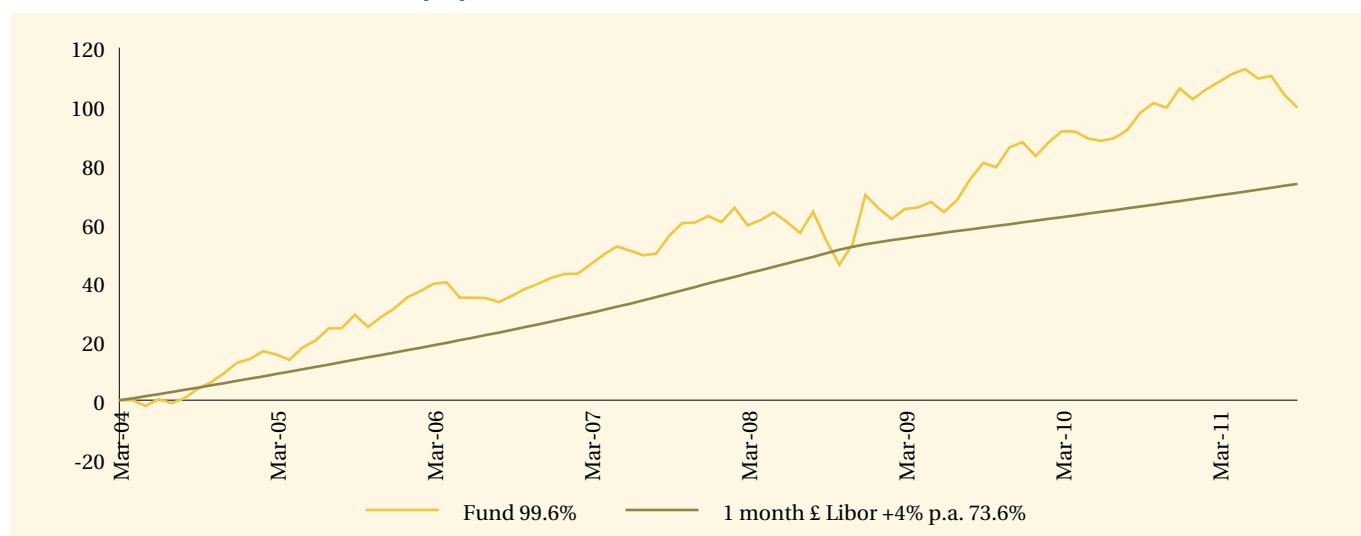
behaved akin to equities, and also, therefore, suffered. The Fund's exposure to gold via its holding in ETFs Physical Gold, as well gold miners Yamana Gold, Newmont Mining and Barrick Gold, continued to benefit from the rising price of gold, and provided a valuable off-setting position against the riskier return-seeking assets of the portfolio. The Fund benefited from hedging euro currency exposure into US dollars, a perceived safe haven.

Portfolio activity

While activity at the core of the portfolio was light, we sold higher-risk securities including Adaro Energy, Actelion and Zurich Financial Services, as a consequence of rapidly deteriorating market conditions. Profits were taken on Advanced Info Service, and we also sold the position in ETFs Agriculture. The net effect was to reduce the Fund's equity exposure and increase the cash position. We did, however, take the opportunity presented by market weakness to add to existing positions in integrated oil companies, including Total, BP and Petrobras, and in chemical and crop protection company Bayer. We added positions in select high-quality corporate bonds, including Continental Tyres and Welsh Water. The softness in the price of gold through September provided an opportunity to reinstate a sizable direct exposure to gold by increasing the Fund's holding in ETFs Physical Gold, as well as increasing the positions in gold mining stocks Barrick Gold, Newcrest Mining and Yamana Gold. We increased index protection via options on the FTSE 100 and S&P 500 to cover 20% of the portfolio on a notional basis, and we introduced another indirect protective strategy with the use of currency pairs (selling the Australian dollar and euro, currencies that are pro-cyclical, into the US dollar, a perceived safe haven defensive currency). We also increased the Fund's exposure to the US dollar through the use of forward currency contracts. We took profits on the Fund's call option on the US long bond future and the Hang Seng Index. We remain cautious on the medium term outlook as the process of deleveraging takes effect. We are confident that the balance of the portfolio between return seeking securities and risk reducing securities is appropriate in the context of the Fund's long-term objective, which is to generate an attractive real return.

Long-term performance

Performance since launch (%)



	2002	2003	2004	2005	2006	2007	2008	2009	2010	YTD 2011
Fund	-	-	-	16.4	8.0	14.9	4.4	10.6	9.7	-3.2
1 month £ Libor +4% p.a.	-	-	-	9.0	9.1	10.3	9.5	4.9	4.5	3.5

Discrete past performance (%)

From	30/09/06	30/09/07	30/09/08	30/09/09	30/09/10
To	30/09/07	30/09/08	30/09/09	30/09/10	30/09/11
Fund	15.1	-1.0	17.0	9.5	0.9

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

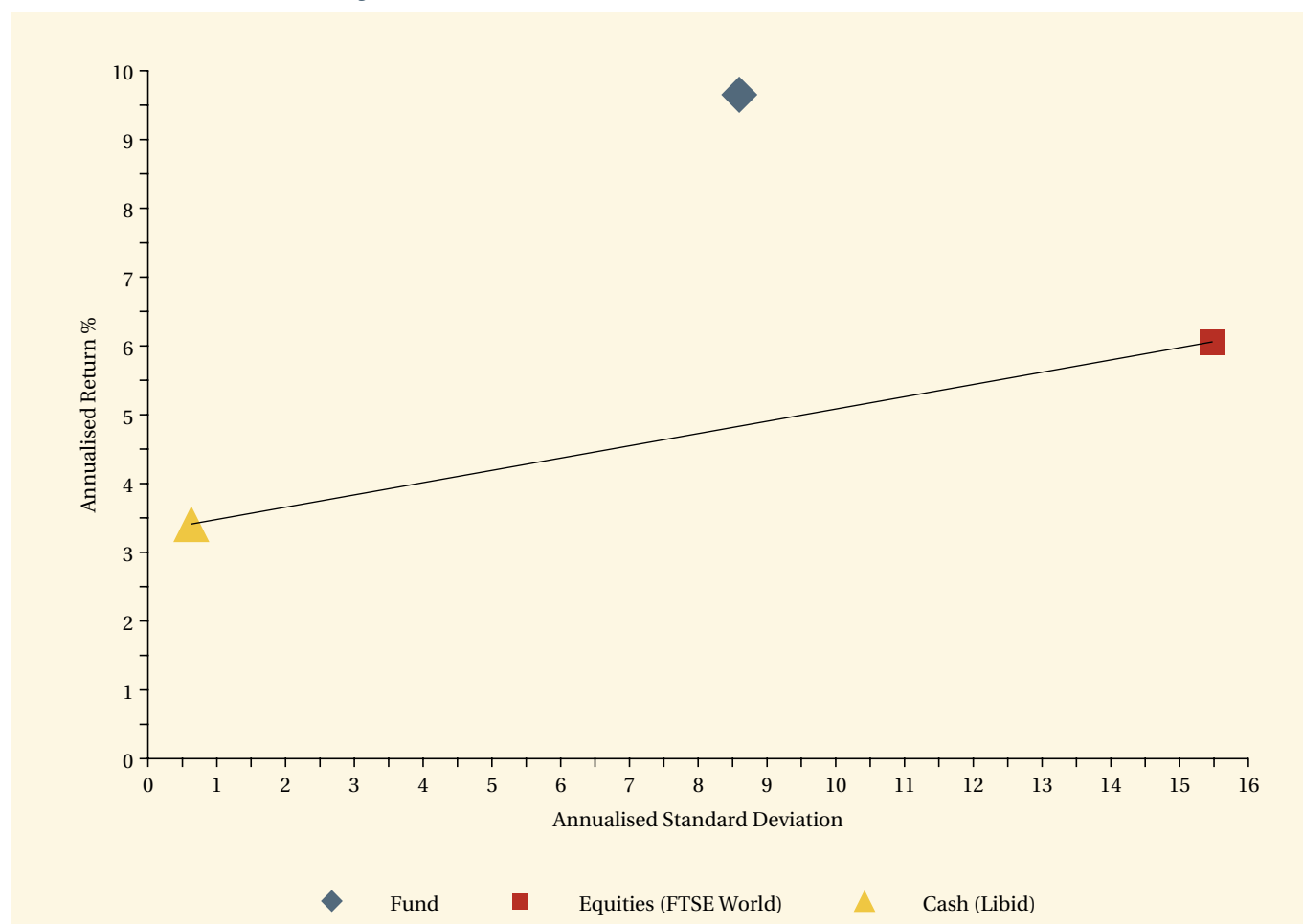
Risk factors

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. The value of bonds is affected by interest rate fluctuations and by changes in the credit ratings of the underlying issuer of the assets. Sub investment grade bonds, may produce a higher level of income than investment grade bonds, but carry increased risk of default on repayment. There are additional risks associated with specific alternative investments that the fund may hold such as commodities; these investments may be less readily realisable than others and it may therefore be difficult to sell in a timely manner at a reasonable price or to obtain reliable information about their value; there may also be greater potential for significant price movements. The fund may also hold derivatives. An investment in derivatives may be volatile, but the volatility of the Fund is not expected to be any greater than that of the underlying stock market.

Long-term performance - risk and reward

Fund return and volatility since launch



This chart shows both return and volatility. The Newton Real Return Fund has given a higher return than cash and equities with significantly lower volatility than equities. The relaunch date of the fund was 31 March 2004.

Risk and return since launch

	Annualised Return	Volatility	Sharpe ratio
Fund	9.7%	8.6%	0.7
1 month £ Libor +4% p.a.	7.6%		

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

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
Deleverage	The credit bubble has left many economies carrying levels of debt which materially impair their economic prospects. We anticipate an extended period of relatively low growth and higher economic volatility as debt is reduced to more manageable levels. The scale of the accumulated public and private debt means that how the debt loads are reduced (whether in disorderly fashion or not) and the effect of offsetting policies will be critical for all aspects of the investment outlook.	British American Tobacco, Smith & Nephew, Roche, Deutsche Telekom, Scottish & Southern Energy
Global realignment	Western industrialised nations still dominate the world's economic output, wealth, consumption and market capitalisation in US dollar terms, as well as consuming the lion's share of natural resources. The generally stronger growth potential and increasing economic influence of the developing world are progressively challenging this position. The trajectory of this realignment is likely to be volatile and increasingly prone to cyclical divergence.	China Mobile, MTN, Millicom, Petroleo Brasileiro
Networked world	Networks are now ubiquitous, allowing information to flow between entities that may have previously been unconnected. The technologies being built into these networks are still developing at a rapid pace and the ecosystem of the web is unstable, offering unprecedented opportunities and risks for both web-based and traditional business models.	Millicom, Sprint, Vodafone, Advanced Info Service
Healthy demand	This theme covers a number of aspects. Expanding incomes and changes in lifestyles in the developing world, combined with ageing populations and severe budgetary constraints in the mature economies, fuel strong demand for 'affordable' healthcare solutions. At the same time, increasing recognition of the role of diet in disease (particularly in an era of high food costs) points to potential changes in patterns of food consumption in the West and the adoption of Western-style diets globally.	Bayer, Syngenta, GlaxoSmithKline, Novartis, Biotech Growth Trust

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.

Issued by the Investment Adviser, Newton Investment Management Limited (NIM). The Newton Real Return Fund is a sub-fund of BNY Mellon Investment Funds, an investment company with variable capital (ICVC) incorporated in England and Wales under registered number IC27. The Authorised Corporate Director of the Fund is BNY Mellon Fund Managers Limited (BNY MFM). Registered Office for NIM and BNY MFM: BNY Mellon Centre, 160 Queen Victoria Street, London EC4V 4LA. Registered in England No. 1371973 (NIM) and No. 1998251 (BNY MFM). NIM and BNY MFM are authorised and regulated by the Financial Services Authority.

Newton Real Return 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

