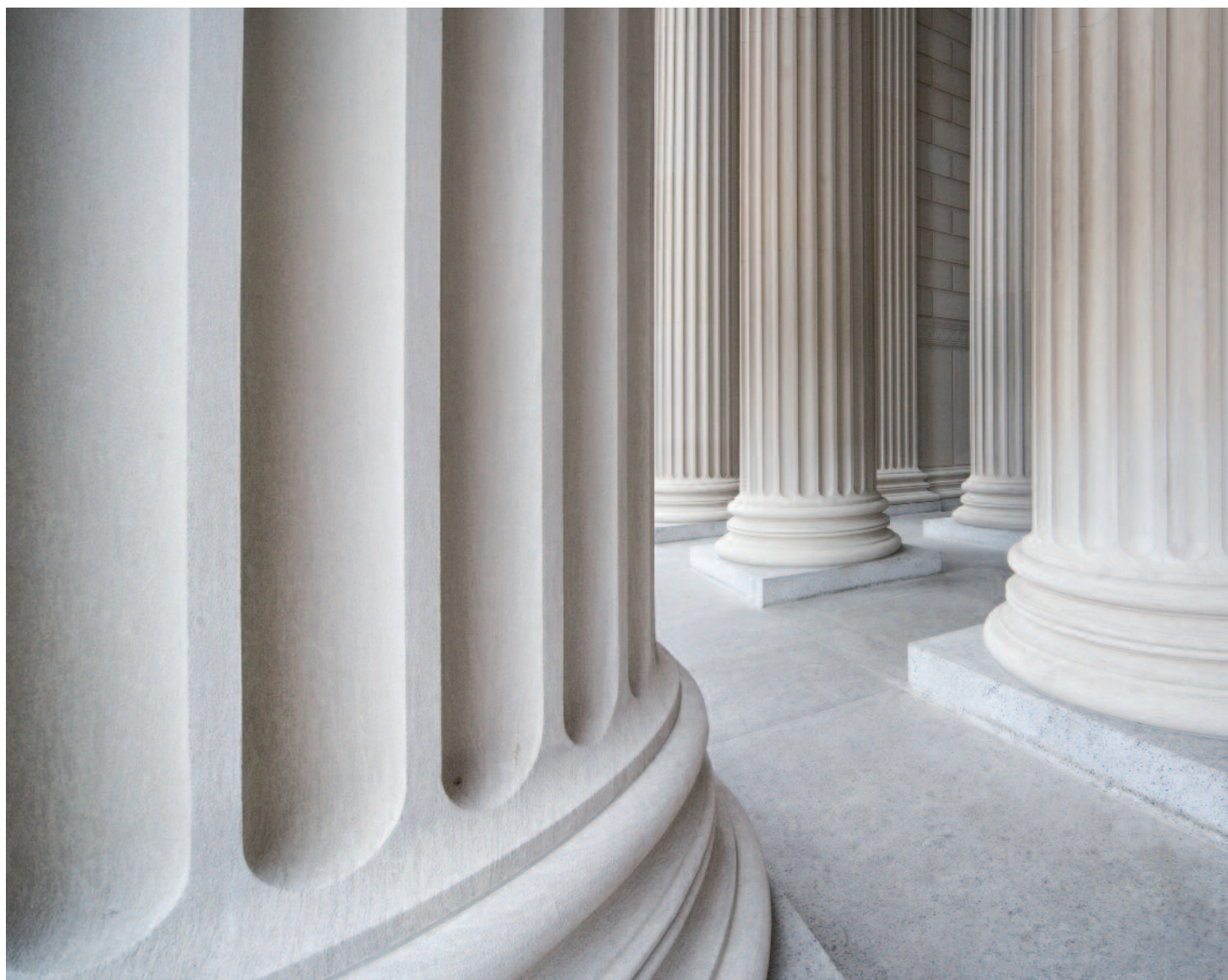


Newton Real Return Fund

Investment Report - Fourth Quarter 2011

▶ A BNY MELLON COMPANYSM

NEWTON
The Power of Ideas



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Fund information

Long-term track record

The Newton Real Return Fund has returned 105.4% since relaunch (31 March 2004), which is equivalent to 9.7% per annum. This is an outperformance of 2.2% 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 4,986 | 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: | 3.6% | Sedol: | 0678032 |

Focus on the latest quarter

Performance over three months

| | | | | | |
|---------------------------|-------------|--------------------------|------|---------------------|------|
| Newton Real Return | 2.9% | | | | |
| 1 month £ Libor +4% p.a. | 1.2% | ARC Balanced Asset (est) | 2.7% | IMA Absolute Return | 0.2% |

Source: Lipper, Bloomberg & ARC, as at 31 December 2011. Calculation basis: Sterling, total return, bid to bid, without initial charges, net income reinvested, net of management fees.

Significant transactions

| Acquisitions |
|---|
| UK Treasury Bill 0% 14/05/12 |
| USA Treasury Notes 0.75% 31/5/12 |
| Australia (Commonwealth) 4.75% 21/04/27 |
| Newcrest Mining Ltd |
| Norway (Kingdom of) 4.5% Bds 22/05/19 |

| Disposals |
|-----------------------------------|
| China Mobile Ltd |
| ENI S.p.A. |
| RSA Insurance Group PLC |
| Turkcell Iletisim Hizmetleri A.S. |
| Thales S.A. |

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

Fund manager report

The final quarter of 2011 proved to be a constructive period for risk assets. Equity and credit markets produced largely positive returns, with the exception of some emerging and peripheral European markets. The US equity market led the charge, buoyed by encouraging economic data, including improving employment statistics. Despite some room for optimism, investors continued to buy the government bonds of those sovereigns perceived to be safe havens, such as the US, Germany and the UK. UK gilts in particular posted strong returns, supported by purchases by the Bank of England. The gold price weakened, a development which seemed, at least in part, to be in response to the ECB's decision not, for the moment at least, to pursue the route of money printing. The oil price staged an impressive rally, driven partially by increasing tensions in the

Middle East, in particular in Iran. The euro finally started to show some weakness against the US dollar.

The Fund produced a strong positive return in the final quarter of 2011. The position in Australian government bonds introduced during the quarter benefited from a 25bp cut in the base rate by the Reserve Bank of Australia. Bayer, the healthcare and chemicals company, was the Fund's top contributor, following positive trial data for Xeralto, its drug for the treatment of Acute Coronary Syndrome. The holding in BP benefited from strong third quarter results which beat consensus earnings expectations, and from the release of an upbeat management statement which pointed to a turning point for the company, which has been enduring a long recovery from the Gulf of Mexico

disaster. The holding in US inflation-linked Treasury notes was advantageous amid investors' flight towards perceived safe haven government bonds. Gold-related holdings, including gold miners Newcrest Mining and Barrick Gold, and physical exposure via ETFs Physical Gold, were notable detractors over the quarter, on account of weakness in the gold price. Other top contributors included GlaxoSmithKline, Total, Reynolds American and Statoil.

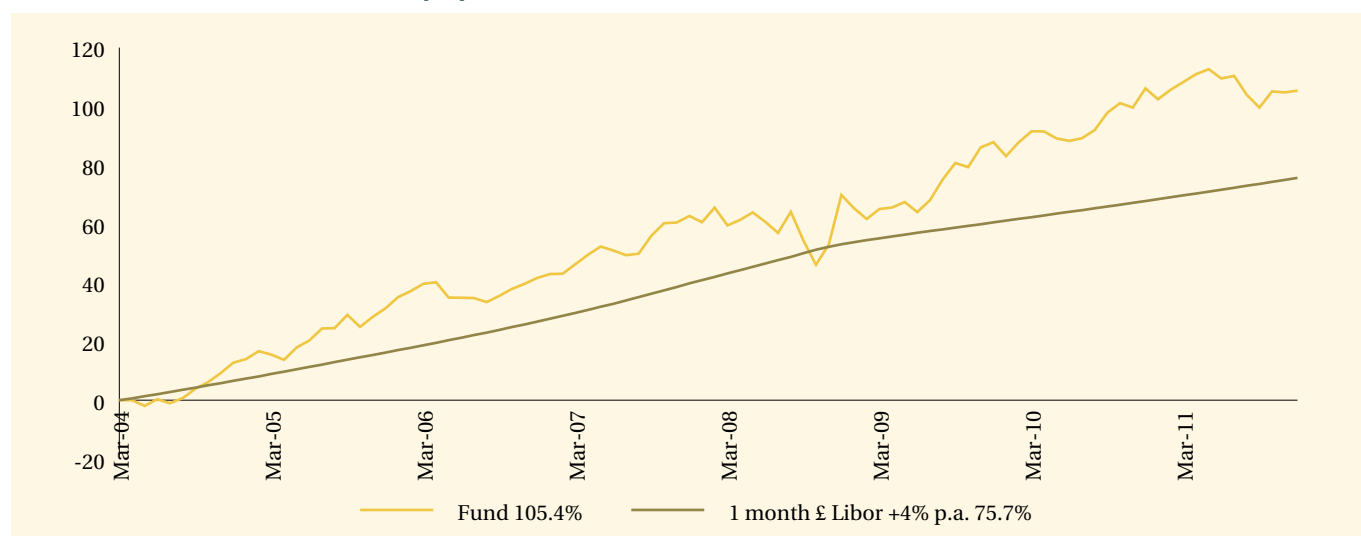
There was a shift over the quarter in the Fund's protective strategy. We allowed the indirect risk asset hedges (in the form of put options on the Australian dollar and euro) to expire, and instead gained most of the Fund's protection directly, through index options. We made this change because we feel the value offered by indirect hedges has now been arbitrated away and, as a result, they have become expensive to maintain, especially in comparison to index options strategies, which we are able to implement for zero cost at initiation. Total protection in the Fund has actually increased, as we have increased the floating US dollar position which, at the current time, is behaving as a natural risk-offsetting position due to the perceived safe haven characteristic of the US dollar. This also serves as a cost-effective complement to the Fund's direct protection. This has been achieved by investing cash in short-dated US Treasury bills. Cash levels have been increased and equities reduced further. We introduced a position in Australian 15-year bonds, on account of their potential to benefit from the deleveraging environment. The Australian economy is highly exposed to Chinese growth and appears to have a housing 'bubble' not dissimilar to the UK's, with a significant proportion of the nation's debt being mortgage-related. Should the Australian economy start to slow, the country's interest rates could be cut sharply. If such a scenario were to occur, the Australian dollar would likely weaken, so we have hedged the currency back to sterling to protect the Fund's sterling liabilities. We increased existing positions in Newcrest Mining and Japan Tobacco, and sold the holding in ENI.

Our opinion is that we are moving back to a more volatile (but probably more 'normal') investment environment than that characterised by the 'Great Moderation' witnessed during the past 30 years. We believe that in this new environment, it is important to view 'risk' in the more traditional sense, as simply the risk of losing money. This is in contrast to a more recent concept of risk as being associated with not being invested and missing out on potential gains. The prevailing deleveraging environment means that growth will be structurally challenged for some time, and income streams in

the form of dividends and coupons are likely to become ever more significant as part of generating a return for clients. The Fund reflects this view through its current positioning, with a core of income generating assets, such as large-cap equities and corporate bonds. In order to generate a real return in this environment, we feel accepting a degree of risk in a 'mark to market' volatility sense will be necessary. However, this does not mean holding a portfolio that is more risky in the traditional sense (of permanent diminution of value), as the companies we target have strong balance sheets, are cash-flow generative and operate within relatively defensive industries. The use of protective strategies including derivatives will continue to be an essential part of minimising the Fund's short-term volatility.

Long-term performance

Performance since launch (%)



| | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 |
|--------------------------|------|------|------|------|------|------|------|------|------|------|
| Fund | - | - | - | 16.4 | 8.0 | 14.9 | 4.4 | 10.6 | 9.7 | -0.4 |
| 1 month £ Libor +4% p.a. | - | - | - | 9.0 | 9.1 | 10.3 | 9.5 | 4.9 | 4.5 | 4.7 |

Discrete past performance (%)

| From | 31/12/06 | 31/12/07 | 31/12/08 | 31/12/09 | 31/12/10 |
|------|----------|----------|----------|----------|----------|
| To | 31/12/07 | 31/12/08 | 31/12/09 | 31/12/10 | 31/12/11 |
| Fund | 14.9 | 4.4 | 10.6 | 9.7 | -0.4 |

Source: Lipper & Bloomberg, as at 31 December 2011. Calculation basis: Sterling, total return, bid to bid, without initial charges, net income reinvested, net of management fees.

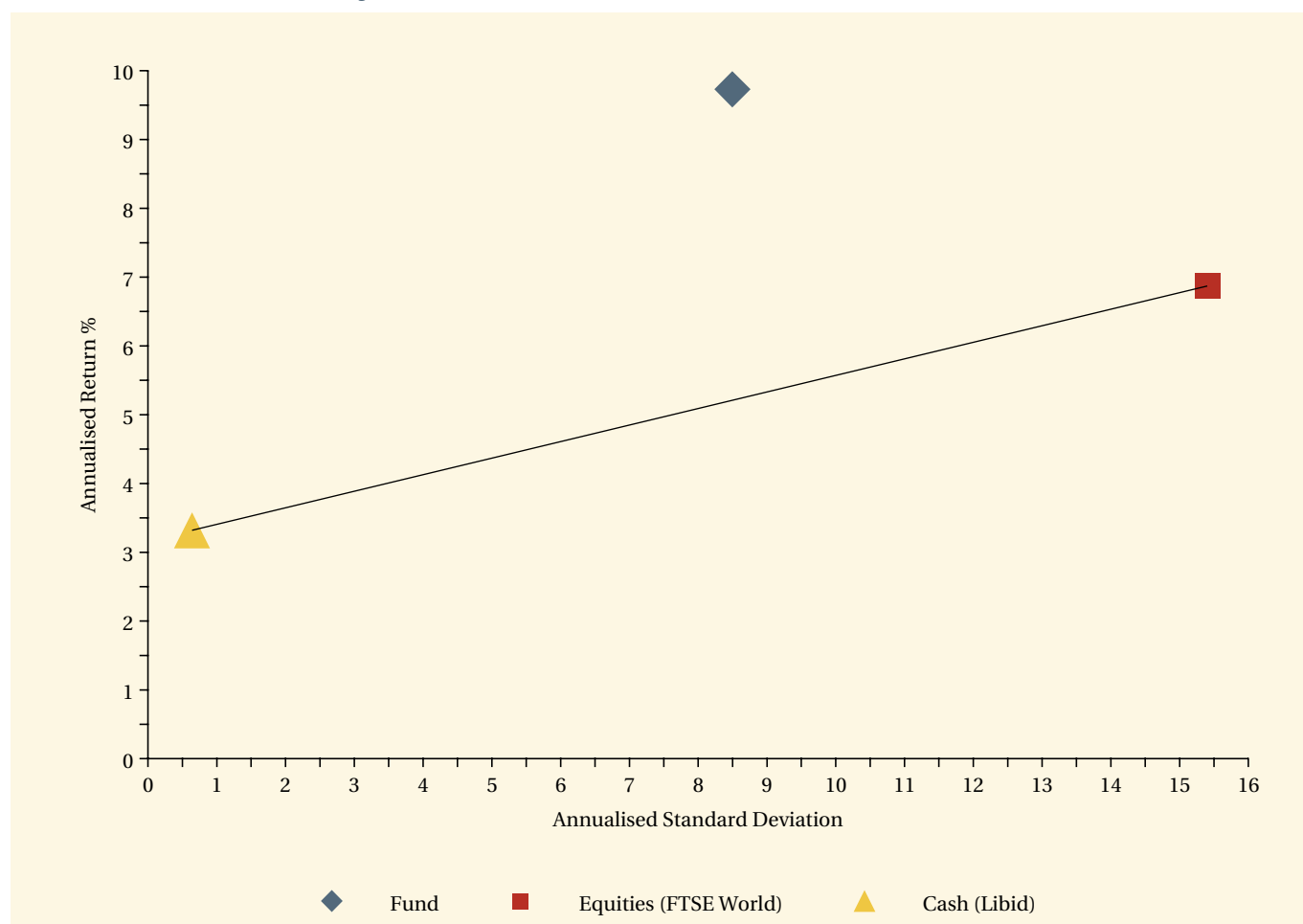
Risk factors

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 world equity markets. The relaunch date of the fund was 31 March 2004.

Risk and return since launch

| | Annualised Return | Volatility | Sharpe ratio |
|--------------------------|-------------------|------------|--------------|
| Fund | 9.7% | 8.5% | 0.8 |
| 1 month £ Libor +4% p.a. | 7.5% | | |

Source: Lipper & Bloomberg, as at 31 December 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. | MTN, Petroleo Brasileiro, Tele Norte Leste Participacoes |
| 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. | 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, Medtronic |

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.

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.

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