

A Newton's cradle with five brass spheres is shown in motion, with one sphere having just struck the others. The background features a grid of technical drawings and diagrams, including a diagram of a pendulum and a diagram of a mechanical device, all in a sepia or aged paper tone. The overall lighting is warm and focused on the cradle.

The enduring benefits of the Newton multi-asset approach

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Newton produced strong investment performance in 2007 in what proved to be a challenging year for much of our industry.

We believe this performance has provided further validity for our global thematic process. That a rapidly changing investment backdrop appeared to catch many investors out reminds us why we use themes: because predicting the future directly is highly unreliable and using models based on the past to guide investment policy is also unsound, particularly at times of change.

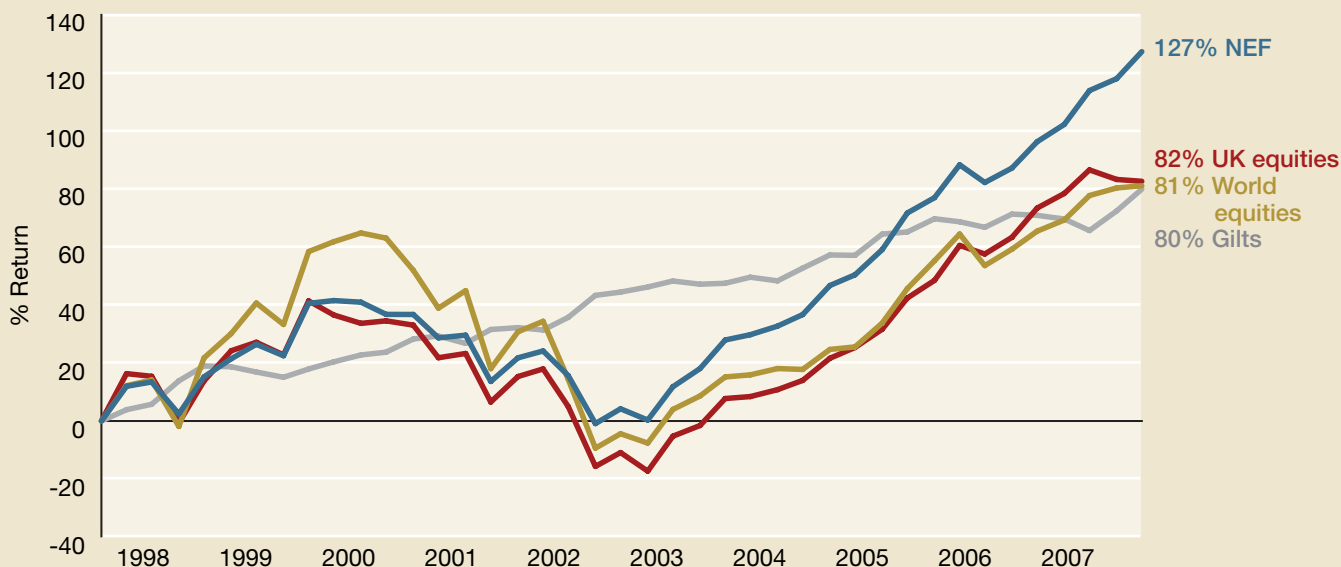
That Newton has produced performance on a broad front reflects the consistent application of the process across its client base. Our 'flagship' multi-asset fund, the Newton Exempt Fund ("NEF"), for example, returned 15.8% in 2007, outperforming its benchmark by 7.7%. More importantly this Fund has delivered

consistent above-average returns with consistently low levels of risk by industry standards. Indeed the NEF returns for 1, 3, 5, 10 and 15 years have significantly exceeded those of both the global and UK equity markets, despite a sustained (though actively-managed) allocation to bonds and cash over the entire period.

It would be reasonable to ask whether Newton took undue risks to achieve these 2007 results. In terms of protecting our clients' assets the answer is an unequivocal 'no'. Our funds are actively managed; we back our judgement. In times of heightened risk (which we saw, for example, building in the financial system) the risk of losing money takes precedence over more esoteric risks, such as tracking error.

A strong history of outperformance

Newton Exempt Fund – 10 years' investment performance



Volatility NEF 12.5% World Equities 17.7% UK Equities 15.6% Gilts 4.5%

Sources: Newton, Thomson Datastream (FTA Govt. All Stocks, FTSE World (£), FTSE All Share) as at 31/12/07.

Annualised performance vs. benchmark and market indices

Period	NEF	CAPS Median benchmark	FTSE All-Share	FTSE World (£)	FTA Govt. All Stocks
1 Year	15.81	7.91	5.32	9.45	5.27
3 Years	15.70	13.74	14.49	13.23	4.59
5 Years	16.85	14.12	15.40	13.60	4.48
10 Years	8.55	6.75	6.20	6.11	6.04
15 Years	10.33	9.05	9.57	8.45	7.37

Sources: Newton, total return, gross of management fees, gross income reinvested; Thomson Datastream as at 31/12/07.

Figures are based on sterling returns. Past performance is not a guide to the future.

Please remember that the value of shares and the income from them can fall as well as rise and investors may not get back the full amount originally invested.

The importance of perspective

We firmly believe that our 'holistic' approach to investing multi-asset portfolios – through single portfolios, for the most part, rather than 'funds of funds' – allows the fund manager to be fully aware of all the risks in the portfolio as well as being constantly able to compare the relative attractiveness of different regions, sectors, and asset classes in a dispassionate manner not always available to the specialist manager. We believe this fund manager 'perspective' adds significant value to our multi-asset strategies. Indeed perspective is also a key defining feature of Newton's broader investment process. The key to preserving the integrity of this objectivity and perspective is our structure; how we organise our investment team. Our fund managers are backed by a strong multi-disciplinary team. Our analysts, for example, follow their particular specialty on a global basis and generally have a high level of experience. The nature of the process requires, and the single location allows, a high degree of interaction between

these team members and we believe this is key to our success in idea generation; the process is not only able to benefit from the knowledge embedded in the group, but also from the synergies resulting from combining the full range of individual perspectives. We firmly believe that in our industry, as in many others that have had to adjust to the internet age, information is not the limiting factor, but how you process it. Information without perspective (and we believe that perspective should be global) would result in our process being very much less idea-rich and would stifle our ability to add value. Maintaining perspective has been key in the years running up to 2007. In terms of our strategic decision to significantly underweight Western financial and consumer sectors, though the performance benefits accrued in 2007, the groundwork had been in place for several years.

The dynamic nature of themes

A central tenet of Newton's approach, which dates back to the inception of the firm, has been that 'change leads to opportunity'. That the world is constantly changing is a given, and thus it follows that an investment approach, if it is to prove consistent, must contain dynamic elements.

We strongly believe that our themes provide that dynamic view of the world. The continually evolving framework of themes that we use to focus our research effort helps us understand how the world is changing and thus highlights areas of opportunity and risk. In short, because themes are about change, our process is much less likely to be caught out by change in the way that many model-driven processes, which rely on backward looking data, have been shown to be in the recent past.

“...because themes are about change, our process is much less likely to be caught out by change...”



A pleasing number of our themes proved important to performance during 2007, from relative new-comers such as *large cap laggards*, *Earth matters* and *fire risks* to the more long-standing ideas, such as *developing economies*, *networked world*, *debt & credit* and *becalmed*.



As suggested above, the last two have been particularly influential in steering our clients' portfolios around the fallout from the current credit crisis. The *debt & credit* theme has focused on the unsustainability of credit growth (well in excess of GDP growth) in recent years. We had no clues as to timing of the eventual credit crunch, only that it was an inevitable consequence of poor lending practices that had become widespread.



The *becalmed* theme zeroed-in on financial market behaviour, observing that developed world borrowers, lenders and investors had begun to behave as though the cycle had been abolished, giving rise to new excesses in risk taking which pointed strongly to a credit cycle that was nearing its peak in the Western world.



The case for a multi-asset approach

We are naturally aware of the shift that has taken place in the market place as pension funds have moved away from awarding managers multi-asset briefs in favour of multi-specialist arrangements. Indeed we have developed a number of specialist strategies at Newton which we believe have benefited from the perspective afforded by our investment process. We remain convinced however that a ‘balanced’ approach to multi-asset investing has appeal. That the balanced approach fell out of favour says more about the implementation of the approach than the merits of the benchmark. The pool of balanced business has been dominated by in-house ‘funds of funds’, which tended towards passivity and mediocrity (it is worth noting that most ‘new balanced’ offerings from the industry are run along similar lines). The decision to run portfolios in this way largely reflects a business decision by large institutions to run their businesses along specialist lines. At Newton our business structure is investment led and we have retained the skills to manage global and multi-asset strategies in a single holistic portfolio. This is a powerful format in which to express our judgement and ideas. Indeed, as discussed above, the ability to focus (on opportunity and risks) and the flexibility (to respond to changing market conditions) afforded by this approach are simply not available to the fund of fund manager.

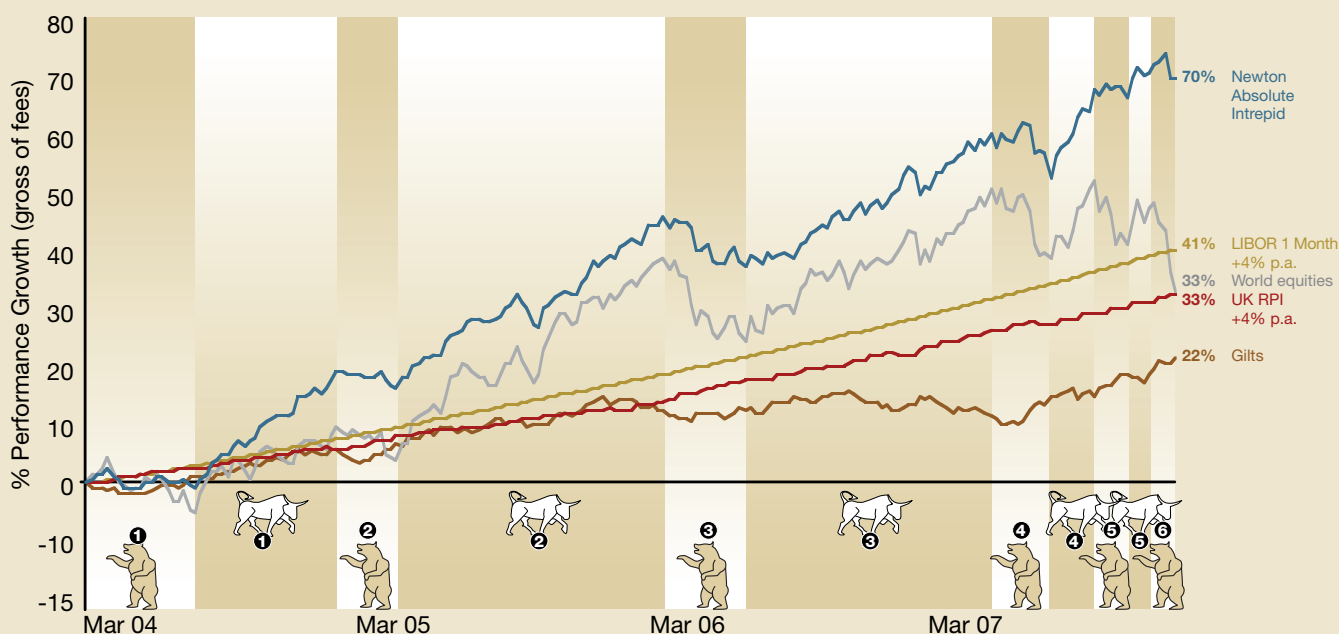
“...the guiding principle at Newton has always been to enhance the real wealth of all our clients...”

Using the ‘focus and flexibility’ afforded by our approach is the key attribute of the Absolute Intrepid multi-asset strategy, which is entirely unconstrained and targets a return of cash (1-month LIBOR) +4% per annum over rolling 5-year periods. Though the target needs to be precise, the broader objective of the fund is to generate a decent real return for investors – something akin to an equity return – with significantly less risk (i.e. a volatility target intermediate between equities and government bonds). As discussed above, the guiding principle at Newton has always been to enhance the real wealth of all of our clients. Our ‘balanced’ approach, as discussed above, has consistently been managed with absolute as well as relative returns in mind.

Relative benchmarks are however a constraint, and with the Absolute Intrepid Fund that constraint is removed. This allows a more opportunistic approach to achieving the target, but at the same time with strong emphasis on capital preservation. Over the longer term we expect that the bulk of the Fund’s returns will come from stock selection in the global equity markets. With equity returns of course comes equity volatility, though this can be offset to a considerable degree by good stock selection (equities are by no means an homogenous asset class), hedging of market risk via derivatives and diversification into other asset classes. Decisions about the asset distribution of the Fund are not a function of macro-economic predictions, but rather the result of a process of constant comparison of relative risk and reward – only those investments with the attributes that fit our current view of the world will be included at any given time.

Using focus and flexibility to achieve strong absolute returns

Newton Absolute Intrepid Fund – relaunch (1 April 2004) to 21 January 2008

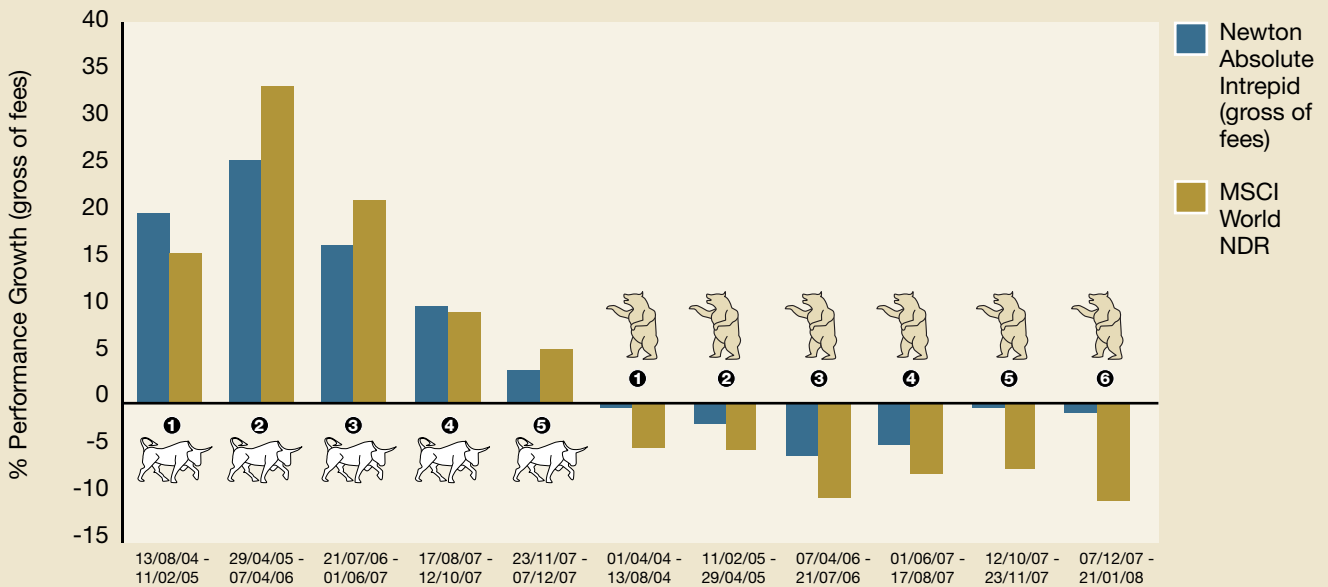


Sources: Newton, weekly data, total return, gross of management fees, gross income reinvested; Thomson Datastream (FTA Govt. All Stocks, MSCI World NDR) Figures are based on sterling returns. Past performance is not a guide to the future. Please remember that the value of shares and the income from them can fall as well as rise and investors may not get back the full amount originally invested.

2007 proved to be another positive year for the Absolute Intrepid strategy with the Fund out-performing its cash +4% benchmark by 5.5%. This follows a strong run of returns since the Fund's inception in April 2004, which has produced a cumulative 69.7% (gross of fees) versus its target of 39.8%. Clearly this has been a strong period for equity markets and it is pleasing that the strategy has out-performed world equity markets (MSCI World NDR) over the same period by 21.5%. More important, however, has been the manner in which this return has been achieved:

- Both observed and forward-looking measures of risk indicate the Fund delivers its performance in a significantly less volatile manner than the equity market (observed volatility for the fund since inception has been 6.3% versus 9.2% for the MSCI World NDR index).
- The results show a distinct asymmetry in that the added value the fund has generated versus equity markets has largely come in periods when equities were weak (see below). In short, the Absolute Intrepid Fund has captured significantly more equity upside than downside, indicating the high levels of risk control embedded in the strategy.

Absolute Intrepid Fund performance in different equity markets



Source: Newton, as at 21/01/08. Past performance is not a guide to future returns.
 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.
 The value of overseas securities will be influenced by fluctuations in exchange rates

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