

Changing Times for Fixed Income

[westwoodgroup.com/insight/changing-times-for-fixed-income/](https://www.westwoodgroup.com/insight/changing-times-for-fixed-income/)



Institutional investors face significant challenges in the future meeting an average 7.6% annual return assumption to fulfill future liabilities. After nearly a 40 year bull market in bonds, traditional fixed income investors need to re-think their approach to bonds. Learn how Westwood's Market Neutral Income strategy can help investors bridge the return gap in a rising rate environment.

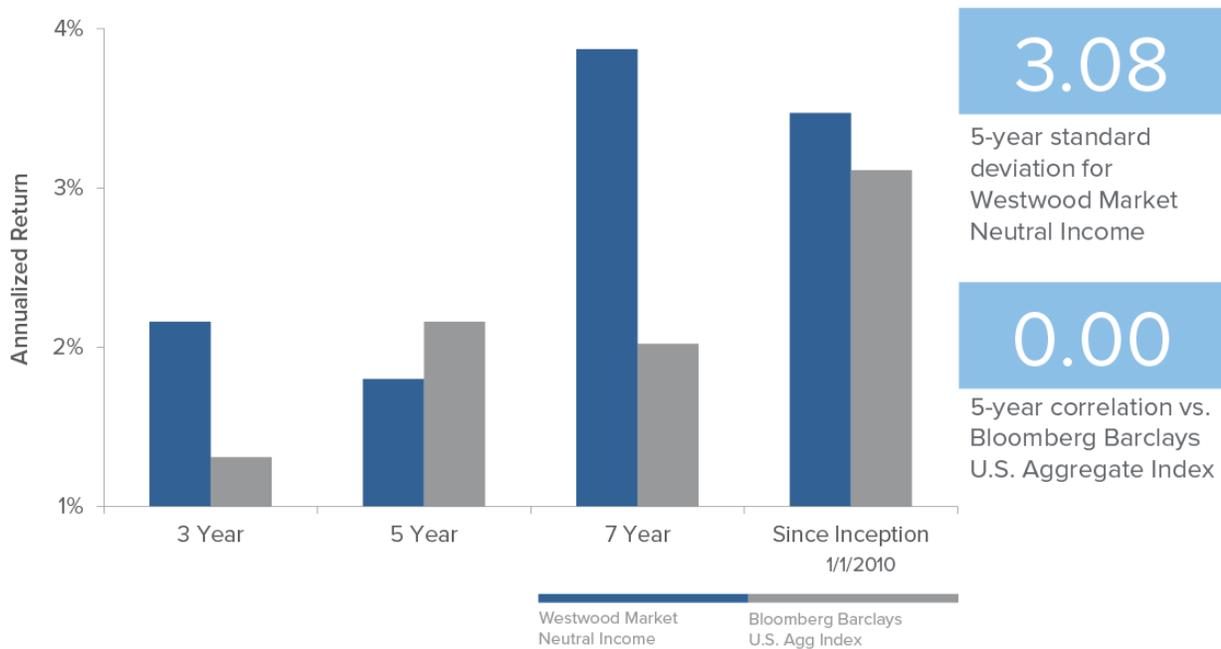
The Role of Traditional Fixed Income Has Changed

Institutional fixed income investors face a challenging market environment with interest rates on the path to normalization and inflation risks on the rise. In addition to future rate hikes, it is widely expected that the Federal Reserve will soon begin to unwind its roughly \$4.5T balance sheet amassed over the most ambitious stimulus effort in central banking history. If this comes to fruition, it may put pressure on the role of traditional fixed income in a portfolio, dramatically affecting investors, who have relied on the historically steady returns that fixed income has offered.

Investments that complement traditional fixed income while maintaining a low level of risk are important to achieving positive client outcomes over the long term. Dedicating a segment of total assets to non-traditional alternative strategies has become commonplace amongst asset allocators in response to the increasing risk per unit of return. When building out an alternatives allocation, it is important to consider correlation and volatility, as well as the liquidity of each investment.

Westwood Market Neutral Income is an alternative strategy with the potential to deliver low-risk, uncorrelated returns to traditional as well as non-traditional portfolios.

Performance Relative to Traditional Fixed Income



Source: © 2018 FactSet Research Systems, Inc. All Rights Reserved. Data Frequency: Monthly. Data as of 9/30/18. Past performance is not indicative of future results. Net of advisory fees.

What is Westwood Market Neutral Income?

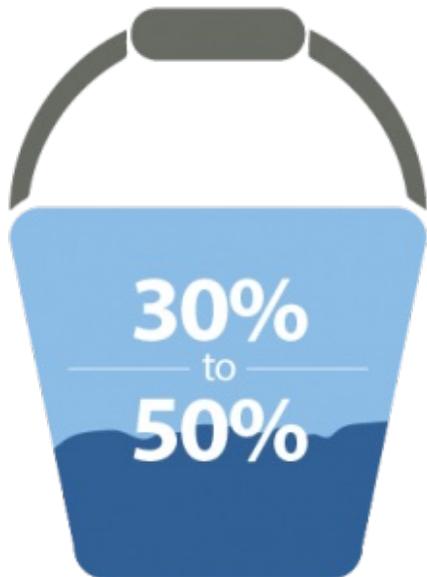
The goal of Westwood Market Neutral Income is to produce absolute returns of 4-6% on an annualized basis (net of fees in the current environment) with low volatility and low correlation to other asset classes. To achieve this, we adhere to an actively managed, market neutral approach to investing in convertible securities.

We utilize three primary strategies in the portfolio which include:



A short duration, convertible yield bucket, which comprises global convertible bonds that are positive yielding, short-dated, liquid issues that exhibit solid credit fundamentals. These more “bond-like” convertibles provide a steady income stream which serves as a base for total return, along with low volatility given their high credit conviction and low equity sensitivity.

This bucket normally comprises 40% to 60% of the portfolio.



A traditional convertible arbitrage bucket, which generally involves buying a mispriced convertible bond and shorting the stock of the same issuer (hedging away the equity component of the convertible bond). The goal is to profit from the mispricing of the convertible bond, either in the bond or the embedded option, while hedging out stock market risk. Additionally, the hedge is adjusted as the equity sensitivity shifts with changes in the underlying stock price. A third component of this trade is the positive carry from netting the coupon of the convertible against the cost of financing the stock short.

This bucket normally comprises 30% to 50% of the portfolio.



Macro hedging strategies aimed to enhance portfolio construction and reduce volatility. This strategy involves removing the unwanted residual risk in the portfolio. Strategies employed usually involve buying puts, typically 10% out of the money on indices that correlate to the highest risk exposures of the portfolio. If everything is going smoothly in the markets, this will be a slight drag on performance, but we view this as a necessary insurance policy that can limit drawdowns during periods of significant market duress.

This bucket normally comprises 0% to 10% of the portfolio.

What Makes Westwood Market Neutral Income a Proven Alternative?

Performance. Uncorrelated Returns. Diversified Sources of Return.

3.5%

Annualized Net Return Since Inception

Absolute return target of 4-6% with 1/3 equity volatility

2.2%

Current Yield

1.2 years effective duration

-0.01

Correlation Since Inception

vs. Bloomberg Barclays U.S. Aggregate Bond Index

8+

Year Strategy Track Record

Portfolio team with a history of creating leading-edge absolute return strategies

© 2018 FactSet Research Systems Inc. All Rights Reserved. Data as of 9/30/2018 with an inception date of 1/1/2010. Data frequency: monthly. Equity volatility defined as the standard deviation relative to the MSCI World-ND. Current Yield and Duration represent that of a representative account. Past performance is not indicative of future results.

Why Westwood Market Neutral Income in a Rising Rate Environment vs. Traditional Bond Portfolios?

- The shorter duration nature of the convertible asset class has multiple features to help protect investors in a rising rate environment. The short-duration yield allocation consists of convertible bonds that have a maturity, or put option, that is typically less than three years. As a result, the duration of this portion of the strategy is currently at less than 1.5 years. The short-duration nature of this component within the overall strategy also enables us to reinvest into higher yield convertible bonds as rates move higher. The convertible arbitrage allocation in the strategy also includes a carry component that can potentially contribute positively as interest rates move higher.
- The macro hedging allocation is intended to minimize undue risks and can potentially provide further protection in the event that interest rates rise and market volatility increases.

The Westwood Funds are distributed by SEI Investments Distribution Co. (SIDCO). SIDCO is not affiliated with Westwood Holdings Group, Inc. or any other affiliate. SIDCO is located at 1 Freedom Valley Drive, Oaks PA 19456.

To determine if this Fund is an appropriate investment for you, carefully consider the Fund's investment objectives, risk factors and charges and expenses before investing. This and other information can be found in the Fund's prospectus which may be obtained by calling 1.877.FUND.WHG (1.877.386.3944). Please read the prospectus carefully before investing.

Mutual fund investing involves risk, including the possible loss of principal.