BNY MELLON

BNY MELLON ABSOLUTE RETURN BOND FUND

INVESTMENT MANAGER

Insight INVESTMENT

Insight Investment Management (Global) Limited: Insight are leaders in absolute return investing, multi-asset, specialist equity solutions, fixed income and liability driven investment.

PERFORMANCE AIM

The Fund aims to deliver cash 3 Months EURIBOR + 3% on a rolling annualised 3 year basis before fees. In doing so, the Fund aims to achieve a positive return over a rolling 12 month period. However, a positive return is not guaranteed and a capital loss may occur.

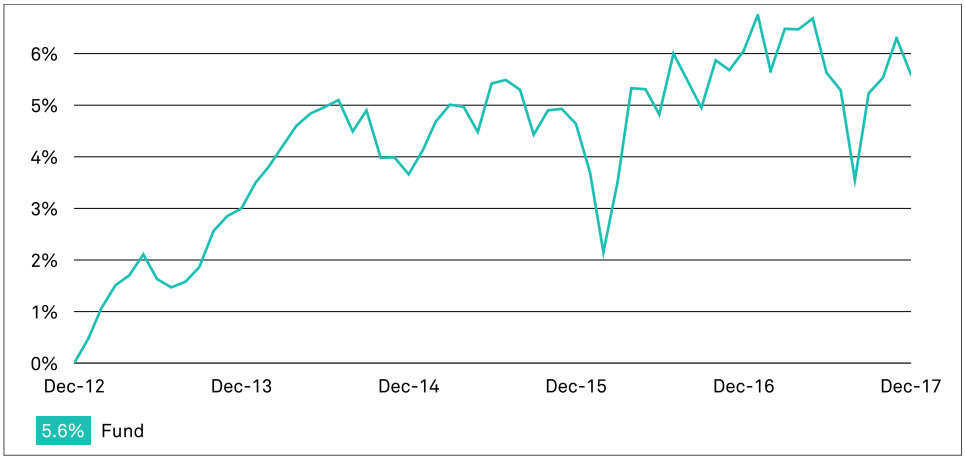
PERFORMANCE NOTE

Past performance is not a guide to future performance. The value of investments can fall. Investors may not get back the amount invested. Income from investments may vary and is not guaranteed.

QUARTERLY HIGHLIGHTS

- Performance: The Fund generated a positive return over the quarter, on a net basis.
- Activity: We took a number of measures during the quarter to adjust our positioning across our various strategies.
- Outlook & Strategy: We retain our long-standing US inflation exposure; at the end of the quarter, we also had a short duration position, having briefly gone neutral. We remain positive on asset-backed securities (ABS).

5 YEAR CUMULATIVE PERFORMANCE (%)



PERFORMANCE SUMMARY (%)

					Annualised		
	1M	3M	YTD	1YR	2YR	3YR	5YR
Euro W (Acc.)	-0.65	0.35	-0.42	-0.42	0.46	0.62	1.10

	2013	2014	2015	2016	2017
Fund	3.00	0.63	0.95	1.35	-0.42

Source: Lipper as at 31 December 2017. Fund performance Euro W (Acc.) calculated as total return, based on net asset value, including charges, but excluding initial charge, income reinvested gross of tax, expressed in share class currency. The impact of the initial charge, which may be up to 5%, can be material on the performance of your investment. Performance figures including the initial charge are available upon request.

Performance data covering periods prior to share class launch include synthetic returns. Synthetic results do not represent actual investment returns nor costs and are not a reliable indicator of future performance. Performance data covering the period since share class launch is a record of actual returns achieved. Performance data for Euro W (Acc.) is derived from EUR X before 03/10/2016, adjusted to reflect the annual management charge of the Euro W (Acc.) share class.

PERFORMANCE COMMENTARY

The Fund generated a positive return over the quarter because of our interest rate and credit strategies. Market allocation positively influenced Fund returns (particularly in November), helped by our long position in 10-year Australian bonds, as well as our 30-year US 'breakeven' inflation trade. Our Australian bonds did, though, give up some of their outperformance during December. However, our yield curve positions detracted from performance as the US yield curve continued to flatten (whereas we are positioned for an anticipated steepening). Our credit positions, in aggregate, also supported returns as investment grade bonds, as well as ABS, fared well. Duration, high yield bonds and loans, emerging market bonds and currency were all slight negatives.

MARKET ALLOCATION, INVESTMENT GRADE CREDIT AND ABS CONTRIBUTED TO POSITIVE PERFORMANCE

Economic data has continued to be supportive in most major economies. The yield spread of corporate bonds over government bonds has further tightened across all major regions as investor's risk appetite remained strong, notwithstanding a market wobble in mid-November. With inflation still relatively subdued and investors concerned about issues such as escalating political tensions with North Korea and President Donald Trump's reform agenda, government bond yields remained at low levels. However, going into 2018, several central banks have either begun, or are contemplating, future monetary tightening.

Major government bond yields continued to sell off in October, only to retrace most of their losses into month-end as the European Central Bank (ECB) reassured market participants on the speed of its tapering of monthly bond purchases. Risk assets and credit spreads also rallied, helped by the ECB's actions.

Over November, bond markets experienced some volatility and changes in direction but, ultimately, there were few significant moves: most government bond yields were very marginally higher, as were credit spreads.

Over December, bond yields rose and credit spreads tightened as the US Federal Reserve (Fed) hiked interest rates, as expected, and suggested that US economic growth would remain strong (supported by recent tax reform legislation).

The main positive contribution during October came from market allocation, where our two long positions in 10-year Australian government bonds (held against US Treasuries and German Bunds) continued to recover as Australian yields again outperformed those of other markets. Our US 'break-even' inflation trades also helped performance. Further positive contributions came from our positions in investment grade bonds and ABS, which benefited from tighter spreads and a favourable supply/demand balance, respectively. The main negative contributions during the month came from our high yield bonds and loans, currency and emerging market bond positions. There was also a small loss on our long 10-year US Treasuries versus short 10-year German Bunds market allocation trade.

The main positive contribution during November came from market allocation, where our long Australia versus short Germany duration trade continued to recover as Australian yields again outperformed those of other markets. Our US 'break-even' inflation trade also helped performance, as did our long UK versus short Germany duration position, which we successfully closed out during the month. These gains were only partially offset by some mark-to-market losses on our long US versus short Germany duration position. Although credit spreads were marginally higher, we believe security selection within our investment grade credit positions was another positive. Our ABS positions – which benefited from

tighter spreads and a favourable supply/demand balance – also helped performance. The main negative contributions during the month came from our US yield curve trade (where we are positioned for a steepening but there has recently been a flattening) and our local currency emerging market bond positions. Other small negatives came from duration, high yield bonds and loans and currency.

Our credit strategies positively contributed to performance during December. Our local currency emerging market bond positions benefited from tighter yields, despite the sell-off in developed market yields. Both our investment grade credit positions and ABS positions benefited from tighter spreads; in the latter market, a continued lack of supply has been supportive. Another small positive came from our high yield bonds and loans positions. Currency had a neutral effect as we have very little risk here. Our interest rate strategies detracted from performance during December. In market allocation, our long Australia versus short Germany duration trade was negative as Australian yields sold off more than their German counterparts. Another negative contributor was our US yield curve trade (where we are positioned for a steepening but there has continued to be a flattening). Lastly, there was a small negative from our duration position, where we tactically traded between outright short and neutral in Germany duration over the month.

ACTIVITY REVIEW

We took a number of measures during the quarter to adjust our positioning across our various strategies. In October, we switched our 10-year Australian government bond trade's offsetting short position from 10-year US Treasuries to 10-year German Bunds. We took some profits on investment grade credit and reduced risk within both our ABS and high yield bonds and loans exposures. We added back US dollar exposure, offsetting our longs in various emerging market currencies with some new short positions, and closed two emerging market bond long positions.

WE TOOK VARIOUS ACTIONS TO REPOSITION THE FUND FOR A RISING INTEREST RATE ENVIRONMENT AND TO REDUCE ITS LEVEL OF RISK

In November, we sold down about half of the investment grade credit exposure which we had a couple of months previously. We now have a short duration position via German Bunds, having previously had neutral exposure. We also removed about a third of the currency hedges, which we had on against our local currency emerging market bond positions.

In December, we increased duration in our local currency emerging market bond positions and removed more of our currency hedges.

INVESTMENT STRATEGY AND OUTLOOK

Our largest exposure is to US breakeven inflation, on a view that the market's inflation expectations are too low. We remain positive towards Australian bonds and ABS, because of expected further spread tightening, as well as local currency emerging market bonds (which, despite recent volatility, we believe continue to be supported by attractive long-term fundamentals).

WE HAVE MAINTAINED OUR EXPOSURE TO US INFLATION EXPECTATIONS GIVEN CONTINUING INFLATION RISK

President Trump's tax reform legislation was finally passed in December and we believe this is likely to support the US economy, although the recent flattening of the US yield curve needs to be closely monitored. With further US interest rate increases on the horizon, political pressure also led the Fed to begin reducing the size of its $4.5 trillion balance sheet in October. Meanwhile, in Europe, further 'emergency' monetary policy appears unjustified so, despite recent euro strength and political uncertainty, the ECB recently announced a tapering of its asset purchases from early 2018.

We have a short duration position, having briefly gone neutral during the quarter. Markets are underestimating the likelihood that the Fed will follow through with its projected policy hikes in 2018, while, in Europe, the ECB has recently announced the imminent tapering of asset purchases. Given our expectation of rising US inflation, we have maintained our inflation 'breakeven' trade via a long position in 30-year US Treasury Inflation-Protected Securities, held against 30-year US Treasuries. We also have two long positions in 10-year Australian and 10-year US Treasuries (both held against 10-year German Bunds). The Fund is also positioned for an expected steepening of the US yield curve – given it has recently flattened to post financial crisis lows – via a long position in 10-year US Treasuries, held against 30-year US Treasuries.

We have a cautious approach towards credit risk, given valuation concerns and the gradual reduction in technical support from central banks. However, we have an overweight position in ABS and local currency emerging market bonds (with currency risk partially hedged), as well as small overweight positions in investment grade credit and high yield and loans. As credit spreads have tightened, we have reduced exposure to both investment grade and high yield names but could add to the latter given the recent sell-off. Our small currency positions entail very little risk.

REGIONAL INTEREST RATE DURATION (YEARS)

	Long	Short	Net
USA	9.9	-7.8	2.2
Other Dollar Bloc	5.1	0.0	5.1
Eurozone	0.3	-9.6	-9.2
UK	0.1	-0.1	0.0
Other europe	0.1	0.0	0.1
Emerging Markets	0.2	0.0	0.2
Total	15.7	-17.4	-1.8

MATURITY INTEREST RATE DURATION (YEARS)

	Long	Short	Net
0-1 yr	0.0	0.0	0.0
1-5 yrs	0.3	-0.1	0.2
5-10 yrs	5.1	-9.6	-4.5
10-15 yrs	5.2	0.0	5.2
15+ yrs	5.0	-7.8	-2.7
Total	15.7	-17.4	-1.8

UNHEDGED FX EXPOSURE (%)

	Fund
USD	2.3
EUR	1.3
GBP	0.1
AUD/NZD	0.1
Other European	-0.4
CHF	-1.1
JPY	-2.2
Total	0.0

Source: BNY Mellon Investment Management EMEA Limited

SECTOR SPREAD DURATION (YEARS)

	Long	Short	Net
Supra/Agencies	0.0	0.0	0.0
Non-financial corporates	0.4	-0.1	0.2
Financials	0.5	-0.1	0.4
ABS/MBS	0.4	0.0	0.4
Loans	0.4	0.0	0.4
Emerging Markets	0.4	-0.3	0.1
CDS Indices	1.2	-1.1	0.1
Money Market Instruments	0.6	0.0	0.6
Total	3.8	-1.7	2.1

CREDIT RATING (HIGHEST) SPREAD DURATION

	Long	Short	Net
AAA	0.0	-0.3	-0.3
AA	0.2	0.0	0.2
A	1.3	-1.0	0.4
BBB	1.0	-0.1	0.9
BB	0.2	0.0	0.2
B	0.4	-0.3	0.1
CCC and below	0.0	0.0	0.0
NR	0.6	0.0	0.6
Total	3.8	-1.7	2.1

COUNTRY OF ISSUER DOMICILE

	Net %	Net Spread Duration (Yrs)
United States	86.0	0.8
Australia	72.3	0.2
Supranational	19.7	-0.2
United Kingdom	15.6	0.5
France	3.1	0.1
Spain	3.0	0.1
Netherlands	3.0	0.1
Switzerland	2.8	0.1
Canada	2.5	0.1
Sweden	1.6	0.0
Norway	1.4	0.0
Ireland	1.2	0.0
Japan	1.1	0.0
Italy	1.0	0.1
Austria	0.4	0.0
Belgium	0.4	0.0
Germany	-104.0	0.1
Cash & Others	-11.2	0.0
Total	100.0	2.1

KEY RISKS ASSOCIATED WITH THIS FUND

- The performance aim is not a guarantee, may not be achieved and a capital loss may occur. Funds which have a higher performance aim generally take more risk to achieve this and so have a greater potential for the returns to be significantly different than expected.
- This Fund invests in international markets which means it is exposed to changes in currency rates which could affect the value of the Fund.
- The Fund will use derivatives to generate returns as well as to reduce costs and/or the overall risk of the Fund. Using derivatives can involve a higher level of risk. A small movement in the price of an underlying investment may result in a disproportionately large movement in the price of the derivative investment. The Fund employs a long/short strategy through the use of derivatives. This strategy is substantially different from 'long only' funds and returns are likely to vary. With both long and synthetic (i.e. created through derivatives) short positions, it is unlikely to achieve the same capital growth as a long-only fund in a rising market but should not experience the same level of decline in a falling market. However, neither of these outcomes is guaranteed for the Fund.
- Investments in bonds are affected by interest rates and inflation trends which may affect the value of the Fund.
- The Fund holds bonds with a low credit rating that have a greater risk of default. These investments may affect the value of the Fund.
- The Fund may invest in emerging markets. These markets have additional risks due to less developed market practices.
- The Fund may invest in structured products which means your investment return is likely to be closely linked to changes in the value of the underlying assets on which the structured products are based.
- The Fund takes its charges from the income of the Fund in the first instance. The impact of Fund charges may be material on the value of any income you receive from your investment. There is potential for capital erosion if insufficient income is generated by the Fund to cover these charges.
- Certain share classes are denominated in a different currency from the base currency (i.e. the reporting currency) of the Fund. Changes in the exchange rate between the share class currency and the base currency may affect the value of your investment.
- Certain share classes use techniques to try to reduce the effects of changes in the exchange rate between the share class currency and the base currency of the Fund. These techniques may not eliminate all the currency risk.
- A complete description of risk factors is set out in the Prospectus in the section entitled "Risk Factors".

INVESTMENT OBJECTIVE

To provide a positive absolute return in all market conditions over a rolling 12 month period by investing primarily in debt and debt-related securities and instruments located worldwide and in financial derivative instruments relating to such securities and instruments.

GENERAL INFORMATION

Total net assets (million)	€ 1,482.53
Lipper sector	Lipper Global - Absolute Return Other
Fund type	ICVC
Fund domicile	Ireland
Fund manager	Andrew Wickham/Peter Bentley
Base currency	EUR
Currencies available	CHF, EUR, GBP, USD
Fund launch	09 Mar 2012

DEALING

09:00 to 17:00 each business day
Valuation point: 12:00 Dublin time

EURO W (ACC.) SHARE CLASS DETAILS

Inception date	03 Oct 2016
Min. initial investment	€ 15,000,000
Ongoing charge	0.86%
Annual mgmt charge	0.75%
Max. initial charge	5.00%
ISIN	IE00BP4JQP45
Registered for sale in:	AT, BE, DK, DE, FR, FI, GG, IE, IT, JE, LU, NL, NO, PT, ES, SE, CH, GB

TO LEARN MORE ABOUT THIS FUND PLEASE CONTACT US:

08085 660 000
+44 (0)20 7163 2367

brokersupport@bnymellon.com
internationalsales@bnymellon.com

www.bnymellon.co.uk
www.bnymellonim.com

Source: BNY Mellon Investment Management EMEA Limited
Any views and opinions are those of the investment manager, unless otherwise noted.

IMPORTANT INFORMATION

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