

Newton Investment Management

Sub-fund of UK-authorized Oeic

Report Issued: November 2007

Peer Group:

UK Equity Income

Fund Manager/Adviser:

Tineke Frikkee (since April 2004)

Location: London

Launch Date: May 1987

Fund Size (September 2007):

£3.4bn

Estimated gross yield: 4.0%

(Annual Fee from Capital)

Distribution dates:

February/August

Group Contact No:

+44 500 66000

Website:

www.bnymellonam.com

S&P ID Number: SB067792

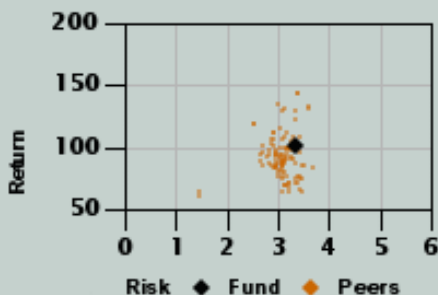
Share class screened: Ord



INVESTMENT STYLE

	Value	Blend	Growth
Large-Cap			
Mid-Cap			
Small-Cap			

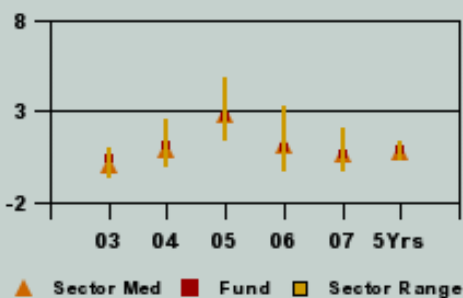
RISK RETURN (STD DEVIATION) OVER 5 YEARS



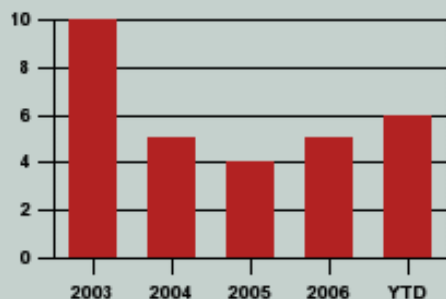
3 YEAR RISK CHARACTERISTICS

Maximum Drawdown	Medium	-6.1
Volatility	Medium	8.0
Correlation	High	0.9
Beta	Medium	1.0

SHARPE RATIO VS PEER GROUP



CALENDAR YEAR DECILE RANKS



Decile ranking in discrete annual periods. 1st decile shown as rank 10, 2nd decile as rank 9, etc. to 10th decile as Rank 1.

Further information on S&P's fund coverage can be found at www.funds.standardandpoors.com

All statistical data on this report has been run to 31/08/2007 on NAV to NAV basis, with gross income reinvested, in UK sterling.

STANDARD & POOR'S OPINION (OCTOBER 2007)

Tineke Frikkee is a well-regarded fund manager within Newton. She heads the specialist equity income operation which manages around £4.5bn and took on her current role in 2004 after the loss of a number of experienced UK managers. Since taking on this role Frikkee has returned performance that is close to our equity income peer group average, but her focus on only buying stocks with at least a 15% yield premium to the FTSE All Share index and selling those that fall to a yield discount has proven to be a good income discipline. Distributions from the fund have grown by faster than average, and sometimes faster than the manager expected, but the running yield has been consistently above average. This emphasis on distribution has been beneficial in protecting capital in market downturns, but the fund has tended to lag in rapidly rising

markets when lower yielding stocks have led the market rise.

However, despite the disciplines of the process, stock selection has not always been good. This may not be helped by the long term nature of the fund, which emphasises buying out-of-favour stocks on a good yield and selling them when the yield falls to below the market average. However, the thematic process at Newton is built for more mainstream funds than this and, because of the yield requirement, there is often less than 50% commonality of ideas with the UK model. This leads the income team of two to work relatively independently of the wider UK team.

While relative performance is a concern, we are reassured by the distribution history and the fund retains its S&P A rating.

FACT FILE

Group: Newton is part of the Bank of New York Mellon Corporation, a leading financial services company based in Pittsburgh, USA. It was Bank of New York Mellon's first substantial acquisition outside the USA.

Team: UK mandates are managed by a team of eight managers based in London and Leeds. They draw on the research and the ideas of 19 analysts charged with coverage of UK equities.

Fund Manager: Tineke Frikkee has 11 years' investment experience, nine gained at Newton. She

has been managing income mandates since 2002. Simon Nichols is alternate manager on the fund.

Style: The fund focuses only on stocks with a dividend yield premium to the FTSE All Share index. The approach is mainly bottom-up, drawing on the UK team model, house themes and the manager's ideas.

Performance: Over the five years to 31/08/2007 the fund has returned 101.1%, compared with 90.0% for the sector median and 87.9% for the index, ranking 25/107.

FUND MANAGER & TEAM

Newton's UK equity team is responsible for around £10bn. The team comprises eight fund managers split between London (Chris Metcalfe, Tineke Frikkee, Richard Wilmot, Simon Nichols and Paul Stephany) and Leeds (Ben Russon).

Two managers specialise in the income mandates and control assets of around £4.5bn. They are:

Tineke Frikkee - MBA, joined insurer UNUM Ltd in 1995 as a risk management analyst before moving to Newton in 1998.

Simon Nichols - chartered accountant, CFA, joined Newton Investment Management's UK team in 2001. He worked at Wilton Investments from 2000 as a financial accountant, prior to which he worked for five years at leading accountancy firms.

PORTFOLIO CHARACTERISTICS

No. of holdings	74
Turnover ratio (%)	43
% in top 10	40

TOP 10 HOLDINGS (01/09/07)

	%
Vodafone *	5.7
BP *	5.1
GlaxoSmithKline	5.0
National Grid	4.2
British American Tobacco *	4.1
Royal Dutch Shell 'B' Shares	3.9
Centrica	3.4
Aviva *	3.0
Barclays *	3.0
First Choice Holidays	3.0

* In top 10 holdings a year ago

ALLOCATION BREAKDOWN (01/09/07)

	Index %**	Fund %
Financials	28	21
Industrials	8	11
Utilities	4	10
Basic Materials	9	1
Consumer Goods	10	14
Consumer Services	12	13
Health Care	7	6
Investment Trusts	-	-
Oil & Gas	15	9
Technology	1	3
Telecommunications	6	11
Other	-	-
Cash	-	1

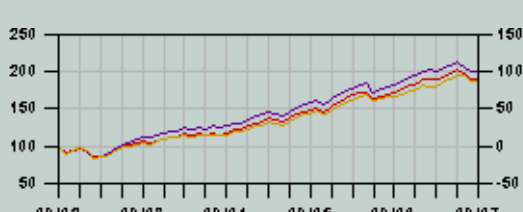
INCOME RECORD

Year	Pence/Unit	% change
2000	1.84	-4.17
2001	2.11	14.67
2002	2.24	6.16
2003	2.3	2.68
2004	2.33	1.30
2005	2.43	4.29
2006 (YTD)	1.53	-
2007 (YTD)	3.2472	-

PERFORMANCE STATISTICS

	3 Years	5 Years
Fund	56.0%	101.1%
Standard & Poor's Peer Median	60.9%	90.0%
Index**	62.0%	87.9%
Fund Rank	84/129	25/107
Standard Deviation	8.0	-
Relative Standard Deviation	1.0	-
Volatility Adjusted Ranking	73/129	-

CUMULATIVE PERFORMANCE



MELLON INVESTMENT FUNDS - NEWTON HIGHER INCOME FUND

Peer Group: UK Equity Income



MANAGEMENT STYLE

- The fund aims to rank in the top quartile of the UK equity income sector on a rolling three-year basis and grow the income distribution.
- The portfolio is constructed bottom-up with a focus on dividend yield: it invests only in stocks yielding a 15% premium to the FTSE All Share index at purchase and investments that yield less than the market are sold.
- Frikkee draws on the UK model portfolio where possible, making use of house themes to focus independent idea generation. Although, because of the high yield focus, commonality with the model is only about 50%.

- Other important criteria include cash dividend cover, the management's commitment to the dividend and the potential for its future growth. Stocks are often bought against consensus and held for the long-term.

- The portfolio may differ substantially from the benchmark at both stock and sector level. Stock positions are unlikely to exceed 5%, but major index constituents are not held if they do not meet the yield requirement. Sector positioning is also influenced by macroeconomic views.

- Covered calls may be written to generate income.

- The fund is normally fully invested, with 55 to 75 holdings. Bonds are not held.

PORTFOLIO REVIEW

Driven by the search for income growth and high starting yield Frikkee has maintained a bias to mid-cap stocks. At review the fund was underweight FTSE 100 stocks (67% against 69% last year) with a marked underweight to mega-cap stocks of more than £30bn. Despite the fund's large size, liquidity appears not to be an issue and Frikkee has shown a willingness to take strategic stakes across her funds in favoured stocks such as Woolworths. First Choice, Premier Foods, National Express and Catlin were all held as

overweight positions for their expected dividend generation.

Larger stocks, including Tesco and BAe, were opportunistically introduced on dips and traded out into rising prices. But Tate & Lyle was built to a 1% position on a profit warning because of the secure income.

Sector weights reflect relative yield positions. Life assurance was liked on yield grounds but big underweights to basic materials and oil & gas were offset by overweights in consumer goods and utilities.

PERFORMANCE ANALYSIS (SEPTEMBER 2007)

Since April 2004, when Frikkee took over, performance has been close to our sector median and the FTSE All Share index. Cumulatively the fund ranks in the third quartile of our equity income peer group while under Frikkee's management, but it has maintained a consistently above average income distribution, and with above average income growth.

In 2005 the fund was slightly behind our peer group and the index but gained from overweighting BAT and Imperial Tobacco and a number of mid-cap takeovers, but gains were lost in Q4 from being underweight HBOS and Lloyds, and overweight Vodafone.

2006 saw median performance and gains from M&A activity in BAA and BOC. In the year to August 2007 Resolution, Halfords and BAT did well but C&W and Admiral were poor after a good 2006. Income distribution gained from premium income on writing covered calls.

In 2004 there was good performance from GUS, Standard Chartered and RMC, but performance suffered in Q4 as lower yielding mid-caps led the way.

DISCRETE PERFORMANCE (CALENDAR YEARS)

	2003		2004		2005		2006		YTD 31/08/2007	
	%	Rank	%	Rank	%	Rank	%	Rank	%	Rank
Fund	29.4	10/112	16.9	65/122	20.5	90/136	18.9	72/140	0.4	76/152
Index**	20.9		12.8		22.1		16.7		3.7	
Median	21.6		17.1		21.4		18.9		0.3	

** FTSE All Share ! (The Industry Classification Benchmark is a joint product of FTSE International Limited and Dow Jones & Company, Inc. and has been licensed for use.)

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