Westwood Funds®

Low-Volatility Equity Investing: **Global Convertibles**

June 2016

Low-volatility equity strategies have emerged as a viable option for investors seeking risk-managed growth. Interest in de-risking equity portfolios continues to grow given increased volatility and emphasis on loss limitation. Much of this interest can be attributed to factors that may persist, such as global growth concerns, negative real interest rates, global currency volatility and lack of stability in the commodity complex. With that in mind, we asked Westwood Management's Global Convertibles Portfolio Managers, David Clott and Shawn Mato, to share their insights on the role global convertibles can play as a low-volatility strategy within a portfolio.

David Clott

Shawn Mato

What makes global convertible securities an attractive low-volatility investment?

David

Convertible securities are hybrid, equity-linked securities that can offer investors many advantages, particularly in a low rate environment with persistent market volatility. Convertible securities exhibit a structural asymmetric advantage due to their diversified sources of return. Investors in convertible securities benefit from bond-like features, such as current income and a principal repayment on maturity, along with an additional equity conversion option in the future. Therefore, investors can participate when the equity market rises, but with limited downside due to the bond-like features, which are a potential buffer during periods of declining equity markets.

What are the potential long-term advantages of global convertibles compared to traditional global equity?

Shawn

The characteristics mentioned by David can potentially provide investors a structural asymmetric advantage over the long term with equity-like returns yet with two-thirds equity risk. For the 10-year period ending March 31, 2016, the Thomson Reuters Global Focus Convertible Bond Index provided competitive returns, up 3.86% annually versus 4.27% for the MSCI World-ND Index. More importantly, the emphasis on lower volatility and higher risk-adjusted returns is highlighted by the 10-year comparison as measured by annualized performance, volatility (indicated through standard deviation) and portfolio efficiency (indicated through Sharpe ratio).

Equity-Like Returns | **2/3 Equity Market Risk**

	Thomson Reuters	MSCI World-ND
10-Year Per Annum[1]	3.86	4.27
Standard Deviation	10.56	16.49
Sharpe Ratio[2]	0.26	0.19

Thomson Reuters Global Focus Convertible Bond Index[1] | MSCI World-ND Index

Source: © 2016 FactSet Research Systems, Inc. All Rights Reserved.
Data Frequency: monthly; Data as of 3/31/16
Past performance is not indicative of future results.
[1] Index trailing from 3/31/16
[2] Using Citigroup 3-month T-Bill as the risk-free rate

Diversification does not ensure a profit or guarantee against a loss.

How have global convertibles fared during recent periods of market volatility?

David

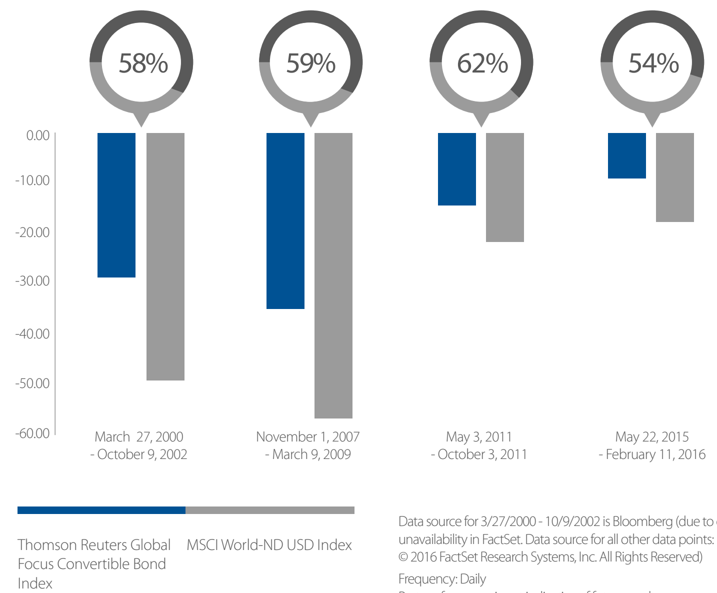
In this chart, you can see the asymmetric advantage of global convertibles to provide limiting downside risk. On average during the last four market downturns, the Thomson Reuters Global Focus Convertible Bond Index provided a downside capture rate of only 58% versus global equity markets, as defined by the MSCI World-ND Index.

Shawn

More recently, 2015 highlighted the potential risk-adjusted return benefits of global convertibles as an asset class and why it has a place in the asset allocation decision process. The global market performed admirably in a volatile 2015 relative to global core equity and bond asset classes. In 2015, the Thomson Reuters Global Focus Convertible Bond Index outperformed the Barclays Global Credit Index by 322 basis points (bps) and outperformed the MSCI World-ND Index by 70 bps.

Peak to Trough Downside Market Capture

(for market periods down >10%)



Data source for 3/27/2000 - 10/9/2002 is Bloomberg (due to data unavailability in FactSet. Data source for all other data points: © 2016 FactSet Research Systems, Inc. All Rights Reserved)
Frequency: Daily
Past performance is not indicative of future results.

Are global convertibles attractively valued in today's market environment?

David

Global convertible valuations are the most attractive since the global financial crisis in 2008. We continue to see the asset class exhibit a level of equity sensitivity as the market recovers while providing downside support if the market backtracks from recent highs. The convertible market continues to remain a robust funding avenue for global corporations. From 2013 to 2015, gross new issuance averaged nearly $88 billion per annum, and we expect a similar result for issuance in 2016 as companies look to raise capital to support mergers and acquisitions activity, refinance debt and improve their balance sheet.

Why do you believe that active management is required in this asset class?

Shawn

As a result of the overall market dynamics, convertible securities are an asset class that introduces structural complexity due to a wide range of characteristics. In our view, passive solutions like ETFs lack the ability to maximize the structural benefits of the asset class and can present potential liquidity challenges. Several variations exist within the convertibles universe that dynamically change depending on market fluctuations including equity, credit spread, interest rate and volatility sensitivity as well as pricing inefficiencies. Because of these aforementioned complexities, we believe that active management utilizing a global universe with an unconstrained approach is optimal to maximizing the asymmetric advantage of the asset class.

Summary

At Westwood Funds, we believe global convertibles are a viable option as a low-volatility equity allocation for investors seeking risk-managed growth and limited downside risk. If this is a strategy that you would like to explore, we would be happy to discuss whether or not it makes sense for your clients personal financial situation. Thank you for the continued trust you place in Westwood Funds.

For more information, please contact:
Blair Albert - 214.756.6377 | balbert@westwoodgroup.com

Definitions and Disclosures:

This material represents the manager's assessment of the market environment and should not be relied upon by the reader as research or investment advice regarding any security, nor is it intended to be a forecast of future events or a guarantee of future results.
Standard deviation is the statistical measure of historical volatility, a measure of the extent to which numbers are spread around their average.
Sharpe Ratio is the measure of the excess return (risk premium) per unit of risk in an investment.
The Index does not reflect any management fees, transaction cost or expenses. The Index is unmanaged and investors cannot invest directly in an index

MSCI World Index - ND is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of developed markets. Net Dividends (ND) index reinvests dividends after the deduction of withholding taxes, using (for international indexes) a tax rate applicable to non-resident institutional investors who do not benefit from double taxation treaties. The MSCI World Index consists of the following 23 developed market country indexes: Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, Hong Kong, Ireland, Israel, Italy, Japan, Netherlands, New Zealand, Norway, Portugal, Singapore, Spain, Sweden, Switzerland, the United Kingdom, and the United States.

Thompson Reuters Global Focus Convertible Index measures the size and performance of the convertibles asset class, and is one of the most widely used convertible bond benchmark internationally. It is a market capitalization-weighted, total-return index. They do not impose any currency, regional or sectoral weights, and do not have a fixed number of constituents.

The performance data quoted represents past performance. Past performance does not guarantee future results.

Mutual fund investing involves risk, including possible loss of principal. Bonds and bond funds will decrease in value as interest rates rise. The value of a convertible security in which the Fund invests is influenced by changes in interest rates, the credit standing of the issuer and the price of the underlying common stock. International investments may involve risk of capital loss from unfavorable fluctuation in currency values, from differences in generally accepted accounting principles or from economic or political instability in other nations. Emerging Markets involve heightened risks related to the same factors as well as increased volatility and lower trading volume. The fund may invest in derivatives, which are often more volatile than other investments and may magnify the Fund's gains or losses. There can be no assurance that the Portfolio will achieve its stated objectives. Indices are unmanaged and do not include the effect of fees. One cannot invest directly in an index.

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www.westwoodfunds.com. Read the prospectus carefully before investing or sending money.
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