Wellesley Asset Management
Convertible Bond Specialists

Wellesley Asset Management Commentary | January 2018

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Fourth Quarter Total Return Comparison (%, through 12/31/2017):

	Q4 2017	1 Year	3 Years*	5 Years*	10 Years*	Since 1/1/2000*
Miller Convertible Bond Fund I (MCIFX)	2.16	7.30	5.64	8.40	6.82	N/A
TRW	2.47	8.49	6.86	9.29	7.69	8.53
Bloomberg Barclays U.S. Aggregate Bond	0.39	3.54	2.24	2.10	4.01	5.11
S&P 500 TR	6.64	21.83	11.41	15.79	8.50	5.40

The performance data quoted here represents past performance. Current performance may be lower or higher than the performance data quoted above. Past performance is no guarantee of future results. The investment return and principal value of an investment will fluctuate so that investor's shares, when redeemed, may be worth more or less than their original cost.

Please review the Fund's prospectus for more information regarding the Fund's fees and expenses including other share classes. For performance information current to the most recent month-end, please call toll-free 877-441-4434.

Total operating expenses for the Miller Convertible Bond Fund are Class A 1.49%, Class C 1.99% and Class I .99%.
See index descriptions and accompanying footnotes.
**Returns are annualized.*

4th Quarter Update

Trends that had been in place all year long continued in the fourth quarter with all asset classes showing positive returns. Major equity indices continued to trade at record highs before selling off into year end. Fixed income returns were also positive across the credit spectrum. For the first time since 2005, the VIX, a measure of expected price swings, did not trade above 20 all year. New convertible issuance remained muted in the 4th quarter as market participants awaited news on tax reform.

The Bloomberg Barclays U.S. Aggregate Bond Index closed up .39% for the quarter and finished the year up 3.54%. Bond returns were not as strong as equity returns in 2017. Investment grade credit spreads tightened from 1.50% over Treasuries to 1.28% over Treasuries. The yield on the 10-year Treasury barely moved during the year opening at 2.44% and closing at 2.41%.

The S&P 500 Total Return Index finished the year on a strong note, returning 6.64% in the fourth quarter. Much of the return was fueled by speculation that Congress would pass a tax bill that would lower corporate tax rates and allow for a repatriation of overseas funds at a reduced tax rate. Equity returns were consistent over the course of the year, with the market trading up in a very orderly fashion. The S&P 500 was up every month in 2017, the first time that has happened since 1970.

The fourth quarter was the slowest quarter of the year for new convertible issuance, with only $4.7B of new paper coming to the market. However, throughout the year, interest rates remained stable, credit spreads declined and stock prices went higher. This scenario led to $38.6B of new convertible issuance in 2017, a 30% increase from the previous year. Half of the new issuance for the year was in technology and healthcare.

For the first nine months of the year convertible returns closely followed equity returns. However, in the fourth quarter equity gains outpaced convertible returns. The breadth in the S&P 500 Total Return Index was much better than the Bank of America Merrill Lynch V0A0 Index during the quarter. The S&P 500 Total Return Index was up 6.64% for the quarter and 21.83% for the year, whereas the Bank of America Merrill Lynch V0A0 Index was up 1.83% for the quarter and 15.7% for the year. In the last quarter of the year, the TRW was up 2.47%.

Though the TRW has experienced positive returns throughout the year, it has lagged equities but outperformed the Bloomberg Barclays U.S. Aggregate Bond Index. The TRW's conservative strategy and positioning within the markets contributed to its lagging performance. Given the maturity of the bull markets in both stocks and bonds, we too have pulled back our risk taking in portfolios. In addition, the TRW's positions are concentrated in small-cap value names in a period when large-cap growth has outperformed. We manage risk in our portfolios by maintaining average bond prices close to par. Other convertible benchmarks, such as the V0A0 index, hold deeply appreciated securities resulting in a higher average bond price. As a result, the V0A0 may perform well in markets that are appreciating, but could experience significant downside capture in the event of a market downturn.

We continue to manage our portfolios with the primary goal of principal protection. Sometimes that means sacrificing upside potential, in order to preserve capital. Furthermore, there are times when our investment style falls out of favor and our upside capture rate falls below expectations. It has been our experience these periods are usually followed by periods of outperformance. For example, in 2014, we only captured 42% of the market upside (of the stocks as measured by the S&P 500 Index). However, in 2015, our strategy was up while the S&P 500 was down. And in 2016, we experienced 100% upside capture. In 2017, we captured 37% of the market upside. Going forward, we feel that market rotation out of large-cap growth could be a catalyst for our strategy to outperform.

2018 Outlook

In 2018, we are bullish on the prospects for new convertible issuance for three reasons. The new tax bill limits the amount of interest expenses a company can deduct to 30% of adjusted taxable income. With limited deductibility of interest, the prospect of issuing debt at a lower interest rate becomes relatively more attractive. In addition, the Federal Reserve is expected to raise short-term rates three times in 2018. If long rates also increase, the cost of issuing straight debt may become too expensive, driving issuers to the convertible market. Finally, the new tax bill's provision for lower tax rates on the repatriation of funds could spur M&A activity, which is often financed in part with convertibles.

Three firms have recently issued research reports that suggest returns in the convertible market could be robust in 2018. According to Barclays, the underlying equities of the convertible universe are more geared towards growth than large-cap stocks (as measured by the Russell 1000) and small-cap stocks (as measured by the Russell 2000). In general, convertible equities have stronger top-line growth and spend more on capex relative to cash flows generated and sales.

Blackrock thinks the convertible product is uniquely positioned to do well in the current environment. According to the firm, convertibles "offer the growth potential of stocks, a possible plus at a time when the economic environment and earnings are generally supportive of equities. But they historically have lower equity beta and bond-like characteristics that may help provide some protection in downturns, where they have tended to exhibit less downside capture."

Approximately 40% of the convertible market is comprised of technology companies, a sector that was recently upgraded at Merrill Lynch. Analysts there cited technology's exposure to momentum and long-term growth, which are typically the best performing factors at the end of a bull market. With many analysts predicting strong economic growth this year, 2018 could be an exciting year for convertibles.

Index Descriptions:

Index	Description	Source
Thomson Reuters Wellesley	TRW is the Thomson Reuters Wellesley Absolute Convertible Bond Index ("TRW"). The Index is a joint venture between Thomson Reuters and Wellesley Asset Management (WAM) that was created in January 2013. Index performance for the period from February 2002 to the creation date is calculated based upon a model portfolio maintained by WAM. TRW is intended to represent a strategy with the goals of absolute returns and outperforming both equities and fixed income over complete market cycles deploying convertible bonds. WAM has discretion over the selection of index constituents and their weighting in the index.	Thomson Reuters
Standard & Poor's 500 Total Return	A free-float capitalization-weighted index based on the common stock prices of 500 top publicly traded American companies, as determined by S&P and considered by many to be the best representation of the market.	Bloomberg data / Standard & Poor's
Bloomberg Barclays U.S. Aggregate Bond	A market capitalization-weighted index often used to represent investment grade bonds being traded in United States. The index includes Treasury securities, government agency bonds, mortgage-backed bonds, corporate bonds and a small amount of foreign bonds traded in the U.S.	Bloomberg data / Barclays
Bank of America/Merrill Lynch All Convertibles ex Mandatory (V0A0)	Represents all U.S. convertibles, excluding mandatory convertibles, small issues and bankruptcies.	Bank of America
Bloomberg Barclays U.S. Convertible Bond > $500MM Index	The index is designed to represent the market of U.S. convertible securities, such as convertible bonds, with outstanding issue sizes greater than $500 million.	Bloomberg data / Barclays

Investors cannot directly invest in an index and unmanaged index returns do not reflect any fees, expenses or sales charges.

Investments in convertible securities subject the Fund to the risks associated with both fixed-income securities, including credit risk and interest risk, and common stocks. A portion of the Fund's convertible securities may be rated below investment grade. Exchangeable and synthetic convertible securities may be more volatile and less liquid than traditional convertible securities. In general, stock and other equity security values fluctuate, and sometimes widely fluctuate, in response to activities specific to the company as well as general market, economic and political conditions. Lower rated fixed-income securities are subject to greater risk of loss of income and principal than higher-rated securities. The prices of lower rated bonds are likely to be more sensitive to adverse economic changes or individual corporate developments. All fixed-income securities are subject to two types of risk: credit risk and interest rate risk. When the general level of interest rates goes up, the prices of most fixed-income securities go down. When the general level of interest rates goes down, the prices of most fixed income securities go up.

Upside capture is a statistical measure of an investment manager's overall performance in down-markets. The down-market capture ratio is used to evaluate how well or poorly an investment manager performed relative to an index during periods when that index has dropped.

Downside capture is a statistical measure of an investment manager's overall performance in up-markets. The up-market capture ratio is used to evaluate how well an investment manager performed relative to an index during periods when that index has risen.

Beta is a measure of the volatility, or systematic risk of a security or a portfolio in comparison to the market as a whole.

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