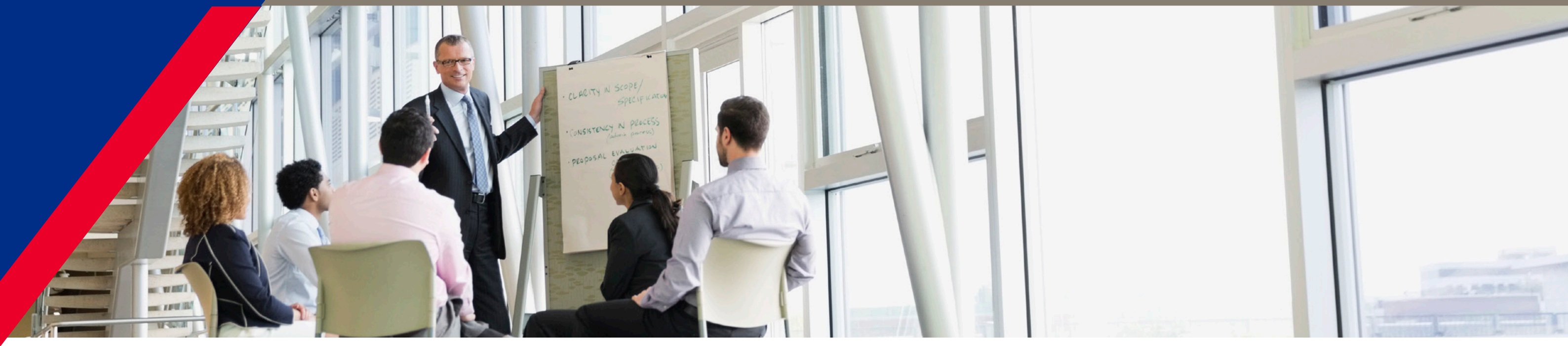
Investing in Convertible Securities

A Conversation with Palisade Capital



What are convertibles?

Convertibles are hybrid securities that may offer equity-like returns with less risk because they possess both equity and fixed-income characteristics. These traits generally include a pre-determined coupon rate, a set maturity date, and a conversion feature - an exchange, at the investor's option, of the convertible bond into a fixed number of shares of the issuer's common stock (known as the "conversion ratio").

Convertible bonds' dual structure provides a proportion of gains as common equity prices rise, and generally captures less of its underlying stock's losses, if common equity prices decline. If a convertible's underlying equity appreciates, the value of the convertible also increases (as the ability to convert into a fixed number of common shares at a higher price increases the convertible's value). Likewise, as a convertible's underlying equity declines, the convertible's value also decreases. It is important to note, however, that this decline in the convertible's value occurs more gradually since the coupon (interest) rate and the issuer's obligation to repay the holder at par upon the bond's maturity generally cushions the convertible's valuation.

Convertibles offer an asymmetric return: more upside than downside participation, as equity markets move. For investors who want to participate with rallying equity markets, but simultaneously want some level of risk mitigation should equity markets decline, the structural features of convertible bonds offer an attractive investment alternative.

In your opinion, what are the opportunities in this asset class for investors?

As convertibles are hybrid securities with traits of both equities and fixed income, we believe they offer the structural benefits that provide equity exposure while maintaining the capital preservation characteristics of fixed-income instruments.

For equity investors concerned that equity markets are near record levels, convertibles offer a measured way to gain exposure while retaining a level of potential downside protection given a convertible's fixed-income characteristics.

For fixed-income investors worried about the prospect of higher interest rates, the option to convert into the underlying equity offers the potential for positive returns, even if interest rates rise. As compared to other fixed-income securities, convertibles generally also exhibit lower sensitivity to interest-rate moves as convertibles may have lower duration, or sensitivity to higher interest rates, than other fixed-income asset classes.

Tell us about your investment objective and process.

Our investment team seeks to take advantage of two inefficiencies in the marketplace: mispriced stocks and mispriced convertibles. There is a relatively small market for convertible securities compared to other asset classes in the U.S., which often leads to mispricings. We believe that companies whose business models are not well understood are often mis-valued.

We believe that we can identify enhanced risk/reward opportunities in the convertibles market through our bottom-up fundamental analysis. Our strategy attempts to capture a significant portion of the upside return of equities (approximately 70%) while seeking to limit the downside exposure relative to the underlying equities of issuers (approximately 50%).

There are three steps to the investment process. First, stocks of companies that have issued convertibles are screened with respect to valuation criteria such as price to earnings, price to sales, price to book, enterprise value to EBITDA[1], return on invested capital, and return on equity. The actual statistical criteria may vary depending upon the industry under evaluation.

Once a list of potentially attractive companies has been generated, the convertibles issued by those companies are evaluated to select those that are attractive based on yield, projected performance relative to the underlying stock, investor protections, and relative price as measured by an industry standard convertible evaluation model.

Finally, upon identification of the most attractive convertibles, we perform rigorous fundamental and credit evaluations of the issuing companies. That evaluation includes assessment of management, competitive considerations, identification of barriers to entry, margin analysis, balance sheet analysis, evaluation of historical performance, and projection of future performance. Additionally, we will take into account the overall economic environment and current sector exposure of the strategy. Convertibles that pass through all three steps described above may be added to the portfolio.

While the overall process is bottom up, the team does utilize an overlay based on investment style (Growth versus Value) and equity market capitalization (small-cap versus mid-cap and large-cap) that leads to specific areas and sectors for investment focus.

Tell us about the ideal market conditions for convertibles.

Convertibles offer benefits in uncertain equity markets. Historically, during periods of rising interest rates, convertibles have actually performed well, as rising rates have been coincident with strong equity markets. Because of increased sensitivity to their underlying equity following years of rising stock prices, a convertible's duration is generally lower than the duration of most non-convertible bonds.

We believe convertibles offer attractive investment characteristics in current market conditions – equity prices near peak levels combined with a 30-year bull market in bonds. Under current market conditions, we believe increased market volatility and rising interest rates are certainly plausible. Therefore, the asymmetric return characteristics, historical up-market and down-market capture ratios, and the potential for strong convertible liquidity through new issuance may provide a compelling case for an investment in a diversified convertible securities fund.

How does an investor employ convertibles in a diversified portfolio?

Over intermediate-term and long-term periods, convertibles have often offered equity-like returns with lower volatility. Convertibles, therefore, may represent a compelling core holding for investors looking for balanced returns over the long-term.

Convertibles also offer investors some measure of built-in asset allocation. When equity markets are strong, a convertible's delta (sensitivity to the underlying equity) generally increases, thereby offering investors more upside capture during rising markets. When equity markets are weak, the reverse may occur as a convertible's delta generally declines, thereby reducing an investor's exposure to equities.

What is your outlook on convertible securities over the next few years?

Convertible securities returns over the next several years should continue to be driven primarily by underlying equity returns. With large sector weightings in healthcare, technology, and financials, convertible performance will predominately track the performance of these segments. Interest income and dividend yields on convertibles offer another source of return.

Convertible new issuance has started to normalize following a period of subdued issuance after the financial turmoil of 2008. With equity markets near record highs and interest rates near historical lows, we would expect the convertible new issuance trend to continue to be robust. Increasing merger and acquisition activity could further add to the pipeline for new convertible issues.

Demand for convertibles also appears to be increasing. As fixed-income investors adjust allocation positioning for higher interest rates, the convertible asset class seems to be garnering more attention. Fund flows into convertible investments have accelerated following the "taper-tantrum" of 2013, a term to describe how the markets reacted to the comments by the then Federal Reserve Chairman, Ben Bernanke, that the Fed might slow down, or taper, the rate of bond purchases, which was a part of its quantitative easing (economic stimulus) program. These flows have continued as the Federal Reserve debates the pace of normalizing interest rates.

Q&A with William W. Lee, Portfolio Manager, Convertible Securities at Palisade

Bill joined Palisade Capital Management in May 2006. Prior to joining Palisade, he was a portfolio manager at Loxias Fund Management, a capital structure arbitrage hedge fund. He was a director in the mergers & acquisitions group at Sony Corporation of America, an investment banking associate at Lehman Brothers and an equity analyst at Delphi Management with a focus on small cap value. Bill is a member of the Investment Policy Committee He received his B.A. in Biology from Yale University and his M.B.A. from New York University, Stern School of Business.

[1] EBITDA is an indicator of a company's financial performance that reflects the earnings of the company before interest, taxes, depreciation and amortization are taken into account.

Risks

An investor should consider the investment objectives, risks, charges and expenses of the Fund carefully before investing. To obtain a prospectus containing this and other information, please call 1-888-310-0416 or download the file from www.1290funds.com. Read the prospectus carefully before you invest.

Investing involves risks, including loss of principal. The Fund is new with limited operating history.

Convertible securities are subject to equity risk, interest rate risk and credit risk and are often lower quality securities, which means that they are subject to the same risks as an investment in lower rated debt securities.

Information provided in this document is general in nature, is provided for informational purposes only, and should not be construed as investment advice. The views and opinions expressed are those of the interviewee and do not necessarily represent the views of their affiliated investment advisors, AXA Equitable Funds Management Group, LLC or its affiliates. Any such views and opinions are subject to change at any time based on market or other conditions and are not intended to be a forecast of future events, a guarantee of future results, or investment advice. Securities and sectors referenced should not be construed as a solicitation or recommendation or be used as the sole basis for any investment decision. It is not possible to invest directly in an index.

Past performance is not a guide to future performance.

No guarantee or representation is made that investment objectives and/or opinion stated will be achieved. Each specific client or investor's experience may vary.

The information has been established on the basis of data, projections, forecasts, anticipations and hypothesis which are subjective. This analysis and conclusions are the expression of an opinion, based on available data at a specific date. Due to the subjective aspect of these analyses, the effective evolution of the economic variables and values of the financial markets could be significantly different for the projections, forecast, anticipations and hypothesis which are communicated in this document.

1290 Funds is part of the family of mutual funds advised by AXA Equitable Funds Management Group, LLC (FMG, LLC), doing business in this instance as 1290 Asset Managers. FMG, LLC is a wholly owned subsidiary of AXA Equitable Life Insurance Company (AXA Equitable), NY, NY. AXA Distributors, LLC is the wholesale distributor of the 1290 Funds. AXA Advisors, LLC (member FINRA, SIPC) offers the 1290 Funds to retail investors.

“AXA” is the brand name of AXA Equitable Financial Services, LLC and its family of companies, including AXA Equitable, AXA Advisors, LLC, and AXA Distributors, LLC. AXA S.A. is a French holding company for a group of international insurance and financial services companies, including AXA Equitable Financial Services, LLC.

1290 Funds® is a registered service mark of AXA Equitable Life Insurance Company, New York, NY 10104.

The Funds are not insured by the FDIC; are not guaranteed bank deposits; and are subject to investment risks, including loss of principal.

Funds distributed by ALPS Distributors, Inc. ALPS Distributors, Inc., is not affiliated with FMG, LLC, AXA Equitable, AXA Distributors, AXA Advisors, or Palisade Capital Management, LLC.

ALPS, A DST Company, 1290 Broadway, Suite 1100, Denver, CO 80203

1290 Avenue of the Americas, New York, NY 10104

AXA000468 093018