Q4 2020 FPA New Income, Inc. (FPNIX) and
FPA Flexible Fixed Income Fund (FPFIX) Webcast
February 2, 2021

Note: Items in brackets [ ] are meant to be clarifying statements but are not part of the actual audio recording of the webcast.

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You should consider FPNIX and/or FPFIX (each a "Fund", and collectively the "Funds") investment objectives, risks, and charges and expenses carefully before you invest. The Prospectus details each Fund's objective and policies and other matters of interest to the prospective investor. Please read the Prospectus carefully before investing.

This transcript must be preceded or accompanied by a prospectus for the Funds. The prospectus for FPNIX dated January 31, 2021 can be accessed at: https://fpa.com/request-funds-literature. The prospectus for FPFIX dated April 30, 2020 can be accessed at: https://fpa.com/request-funds-literature The most current prospectus can always be obtained by visiting the website at www.fpa.com, by calling toll-free, 1-800-982-4372, or by contacting each Fund in writing.

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Moderator: [Please reference slide 1] Hello, and welcome to today's webcast. All lines have been placed on mute to prevent any background noise. Please note that today's web conference is being recorded.

During the presentation, we will have a question and answer session. You can submit questions via the Q&A panel at any time during today's presentation. Type your question in the open text box, and click New Question to submit.

If you experience any technical issues during the broadcast, we suggest you first refresh your browser. If that does not resolve the issue, please send a message through the Q&A panel.

It is now my pleasure to turn today's program over to Kristina Surkova. Kristina, the floor is yours.

Kristina: Thank you. Good afternoon and thank you for joining us today. We would like to welcome you to FPA New Income and FPA Flexible Fixed Income Fund Fourth Quarter 2020 Webcast. My name is Kristina Surkova, and I am relationship manager for both funds. The audio, transcript, and visual replay of today's webcast will be made available on our website, FPA.com.

In just a moment, you will hear from portfolio managers Tom Atteberry and Abhi Patwardhan and members of the Fixed Income investment team. Tom Atteberry is a partner at FPA, and joined the firm in 1997. Tom has been a portfolio manager of FPA New Income, Inc. since 2004, and a portfolio manager FPA Flexible Fixed Income Fund since its inception in December 2018.

Abhi Patwardhan is a partner at FPA and has been with the firm since 2010. He has been director of research for FPA New Income since April 2015, and portfolio manager for the Fund since November 2015. He has served as portfolio manager for FPA Flexible Fixed Income Fund since its inception in December 2018.

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We would like to make a couple of announcements before we proceed with the presentation. FPA has recently started posting Firm and Fund updates on our LinkedIn page. We encourage you to follow us to receive timely information going forward.

We also encourage you to join FPA Crescent Fourth Quarter update webcast tomorrow, February 3, at 1:00 Pacific time, and our first FPA Queens Road Small Cap Value Webcast on Thursday, February 4, at 1:00 PM Pacific.

[Please reference slide 2] Now, let's talk about what happened during the quarter. The Treasury yield curve steepened on inflation expectations, but Treasury yields overall remained very low, particularly for short-duration bonds. Spreads and yields on investment-grade and high-yield debt continued to decline, and hovered near all-time lows.

As part of today's agenda, Tom and Abhi will discuss the highlights for both funds, provide commentary on the market, review portfolio and performance activity, and then open it up to question and answers.

And now, I'll turn it over to Tom.

Tom: [Please reference page 3] Thank you, Kristina, and thank you everyone for joining us this afternoon. We're going to start out with some comments about performance, first with the FPA New Income Fund. For the fourth quarter, the Fund outperformed the 1-3 Year Agg; that is the third consecutive quarter that we've been able to do this. However, we did slightly underperform our [the Adviser's] other objective of being CPI plus 100 basis points.

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For the year, however, we were able to get CPI plus 100, albeit we did fall short of the Bloomberg Barclays 1-3 Year Agg Index. Looking at longer periods of time, out three years and five years, we continue to outperform the index. However, we have fallen a bit short, after the three-year time frame, of outdoing CPI plus 100. That's specifically over the five-year period. And then when you look at longer periods, it tends to underperform that sort of benchmark as well. However, keep in mind that's during a period of time of negative real interest rates. And while we didn't get CPI plus 100 basis points, we were able to get at least CPI plus something.[1]

[Please reference page 4] So moving forward to talk about Flexible Fixed Income, it doesn't have as long a track record but we are ending up our second year. It did outperform its benchmark for the quarter. It also was able to do that in the third quarter, and it produced a return that's greater than CPI plus 200 basis points, which is its stated objective, for both 2019 and 2020. So, since inception, it is outperforming that.[2]

[Please reference slide 5] So at this point, I want to move on and first start off by talking about the objectives that we have for each of these portfolios. And I think it's important and critical to understand these objectives, given the marketplace that we find ourselves in today.

[Please reference slide 6] For the New Income Fund, its short-term objective, it seeks to have an absolute positive return on a 12-month period. For Flexible Fixed Income Fund, we are trying to do that same

[1] FPA New Income, Inc. seeks to provide long-term total return, which includes income and capital appreciation, while consider capital preservation. It is goal of the Adviser to seek positive real returns (to outperform inflation as measured by the Consumer Price Index "CPI", plus 100 basis points) over a five-year period and competitive returns versus the bond market universe. Comparison to any index is for illustrative purposes only. The Fund does not include outperformance of any index or benchmark in its investment objectives. An investor cannot invest directly in an index. Past performance is no guarantee, nor is it indicative, of future results.

[2] FPA Flexible Fixed Income Fund seeks to provide long-term total return, which includes income and capital appreciation, while consider capital preservation. It is goal of the Adviser to seek positive real returns (to outperform inflation as measured by the Consumer Price Index "CPI", plus 200 basis points) over a five-year period and competitive returns versus the bond market universe. Comparison to any index is for illustrative purposes only. The Fund does not include outperformance of any index or benchmark in its investment objectives. An investor cannot invest directly in an index. Past performance is no guarantee, nor is it indicative, of future results.

objective, although we are doing it over a 36-month period. Longer-term, we seek to get we seek to get CPI plus 100 basis points of return for the New Income Fund. And for the Flexible Fixed Income Fund over a five-year period, we're trying to get CPI plus 200 basis points.

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Both of these strategies are indifferent to a benchmark, although if you were to assign one to them, we typically use the Bloomberg Barclays 1-3 Year Agg for the New Income Fund, and the Bloomberg Barclays Universal Index for Flexible Fixed Income. Within the Morningstar categories, New Income is a short-term bond fund category; Flexible Fixed Income is in the nontraditional category.[3]

At the end of the year, the assets in the New Income Fund were just short of $10 billion—$9.7 billion; the whole strategy, including our separate accounts, was a little over $10 billion, at $10.4 billion. And Flexible Fixed Income ended the year at $332 million in assets, and the completely strategy, with its separate accounts is about $422 million.

As everyone is probably aware, during the summer we closed the New Income Fund to new investors; existing shareholders and investors continue to contribute if they wish—just new ones were precluded.

[3] Please refer to the end of this transcript for important disclosures and definitions.

The real reason we were doing this is the investment universe has become very challenging in Fixed Income. And we instituted this partial closure really with the emphasis of protecting the interests of our existing shareholders. We've always stated to clients and to prospects that our absolute return approach, and its attractive risk and return attributes that it's able to exhibit, are best executed if we do limit the size of assets under management. Having said that, Flexible Fixed Income continues to be open to both existing and new investors.

[Please reference slide 7] Moving forward, we look at what we have traditionally shown as the yield and duration metrics to the portfolio as it relates to the benchmarks. And as should be expected, for New Income, it continues to have a yield-to-worst greater than either the aggregate bond index or the 1-3 year, while having an effective duration that is significantly less than the agg, and less than the 1-3 as well. The end result is we have got a portfolio that when you compare it to the aggregate index, it's got about 113% of the yield of the broad market while taking about 76% less interest rate risk.

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Of real note in here is [to] look at the sensitivity to changes and rates to both the broad aggregate and the 1-3 year. What that yield to duration metric is really telling you, an 18 basis point change in the level of yield upwards for the aggregate index will produce a zero return in 12 months. And you look at New Income Fund, whether it's that or it's 1-3, we [FPNIX] are about five times less sensitive to that kind of change than the broad market.

Looking down at the Flexible Fixed Income, as it's starting to exhibit those similar characteristics, and that similar characteristic is that it has a yield-to-worst that is greater than the Universal Index while taking a lot less interest rate risk through effective duration to get there. So, it's got about 125% of the index's yield, and it's taking about 82% less interest rate risk to get there.

At this point, I really want to start to illustrate our approach and how it adds value to investors, and how does downside protection have a real strong influence, a positive influence over a long period of time.
[Please reference slide 8] So this is a look at 2020. Before I get into the numbers on the graph, I want to highlight the bullet point at the top. This marks the 36th consecutive year of a positive absolute return in a calendar year period of the FPA New Income Fund. And we are extremely proud of the fact that that is something that is unmatched by any other fund in the short-term bond fund category. This, we think, speaks very well to us

continuing to achieve that first stated objective, and that is a positive return over a 12 month period.

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Thinking back to our discussions in 2019, about whether it's the Flexible Fixed Income or the New Income Fund, we talked a lot about how in 2019, we saw very little value in credit, so our credit exposure was declining. That we, on a systematic basis, we were improving and really staying with the highest quality of bonds that are in that A and above category that we classify as high-quality bonds. And the results of that, actions that we took through 2019, was the drawdown in 2020 for both of these strategies was significantly less than the peer group—"significantly less" being somewhere to the tune of about half as much. So New Income was down a little less than 3% on its max drawdown, while the category it's in was down a little over 5.3%.

I want to make a note on the 1-3 Year Agg and why its drawdown was so much less than the others. And that is it's really a function of—almost 60% of that index is made up of U.S. Treasuries. And U.S. Treasuries during the drawdown period of Q1 of 2020 was really the only area of the marketplace where you saw a rise in price and a decline in yield.

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So, looking at these drawdowns, how did they impact the return and the risk, when you combine those two, for 2020 and for longer periods of time? First let's look at how that comes out on a scattergraph for the year 2020.

[Please reference slide 9] So the graph on the left looks at standard deviation over one year, and looks at our total return. We just put here the bond funds' peer group, short term bonds and traditional bond funds categories, and then the Funds themselves. The triangle that forms, the reddish triangle, which is the Flexible Fixed Income Fund, had a much lower standard deviation than the nontraditional bond fund index and produced a higher return.

Looking at the New Income Fund, it has a lower standard deviation. It had a much lower drawdown, but it didn't produce quite as high as return as the short-term bond fund index did. But that's really only looking at one year, and that really is only the testament to—you are trying to produce that positive return in a 12-month period. And it has some costs to do that.

[Please reference slide 10] But if we look at the longer periods of time, you see a much different picture. The graph on the left looks at a five-year period. And if you think about that five-year period, that's the period of rising Fed Funds rates, falling Fed Funds rates. If you look at New Income, which is sort of a bluish diamond, and it has a return that is slightly better than its peer group. It has much less risk as defined by volatility than its peer group; and it has a higher return than the 1-3 Year Agg Index.

If you go to the right-hand side and you look at ten years of data, what you get is a return of New Income that is very similar to the short-term bond fund category, but again, taking much less risk in order to get there if we use volatility as defined by standard deviation as a measurement of risk. And it has also produced a return greater than the 1-3 year.

What is of interest when you look at that ten-year category. That includes a period of time of extended zero to interest rate policy post-2008, plus you've got the rise in Fed funds, and you've got the fall in Fed funds. So, you have a complete Fed funds cycle being illustrated there. And you can see the kind of return and risk that we've been able to exhibit.

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[Please reference slide 11] So how does this look for Flexible Fixed Income? Well, we don't have five and ten years' worth of data; we only have two. But we see some similar characteristics, and see patterns starting to unfold for us. The standard deviation of the Flexible Fixed Income Fund is significantly less than its peer group, the nontraditional bond fund category. There was a cost to that; its return is lower than the category, but that difference in volatility is extremely significant.

When we launched Flexible Fixed Income, one of our objectives was to have the fund exhibit the same risk and return characteristics that you see from the previous page in the New Income fund. Yes, it's got a different risk parameter to it; yes, it can have more credit to it. It's in a different category, but that same risk and reward relationship we wanted to create for it.

The first two years of the Fund, it's starting to exhibit those characteristics. We're very encouraged by that. We're very pleased by that. And one of the biggest reasons for that is we control it on the downside, which is always something when we invest; that we're looking to protect that downside first.

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And this is where you see it, albeit for a two-year period; it is something to note that it is a positive force. We are encouraged by this as we look for longer-term.

[Please reference slide 12] So at this point, I want to move forward for a second, and talk about our long-term objective in the New Income fund. And so, what this graph is looking at—this graph looks at rolling five-year returns for the FPA New Income fund; the short-term bond fund category; and the 1-3 Year Agg Index. We then take those returns and then subtract CPI from them to get what looks like a real return.

And what is of interest is that from 1998 to 2009, New Income fund consistently produced a higher return after CPI was taken into account than either the peer group or the index. If we look at 2009 to 2014, we did significantly better than the peer group, although slightly less than the index. And then 2014 and 2015 we did lag the peer group, and we were slightly behind them again in 2016, for a short period of time. That said, during that period, we were better than the index. And then post that mid-2016 forward, we've exhibited a better real return than either the peer group or the index.

More importantly when you look at that period of time, 2014 and forward, at its worst, we were getting down to where our return minus CPI got to zero; occasionally got slightly negative. But it was far better than the index, and far better than the peer group, where both of them had exhibited, especially in 2017, 2018, and 2019, returns that were even less than inflation.

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Because it's important to us, because when you think about it—first off we said we wanted an absolute return in a 12-month period on a positive basis. But we also talk to clients about the fact that we really attempt to, at the end of the day, preserve the value of capital, and preserve the value of capital in a real sense. So, to get a return that is equal or better than inflation, even under the worst of times.

[Please reference slide 13] So how do we get to this? How do we start to produce these kinds of risk-adjusted returns? What are we doing that we think brings value to the table?

The graph we're looking at goes back a long period of time. It starts in 2001 and just looks at major sectors of the fixed income market and how the New Income fund was exposed.

And a couple things come out. The first thing is those exposures you seek can vary over time by huge amounts because we're always looking to have the greatest exposure to the cheapest parts of the market.

The size of the assets we manage, the indifference we have to a benchmark, help us to maximize getting to those cheapest or least expensive parts of the marketplace, and taking advantage of them in order to help us reach our true investment objective.

The soft close we undertook in 2020 during the summer is another element we used to help us reach those objectives, because that's what important to our existing clients.

A couple of notes in here to keep. You will notice in the 2001 to 2007 of time, there's a big allocation to Treasuries, or a significant allocation to the Treasury market. That was quite a while ago. It's quite easy to remember. That was one bond. It was a ten-year TIPS bond that we owned up until the day it matured in 2007, and which the real yield we were receiving was 3% to 4%. It looked extremely attractive, so we placed our investors' money there.

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You see mortgages on the green slide, darker green [portion of the] slide be quite large during 2007/2008, and then they tapered off for a period of time. They were very important to us reaching our objectives. And then you also see asset-backed from 2013 forward become a very big piece of the portfolio, because they were the best place to find value to reach our objectives.

But these are just the large portions, in traditional ways, of slicing up the portfolio. The next slide will look familiar to you. It's the investment ideas pie chart that we've been putting in our presentations for many years.

[Please reference slide 14] What we've done here is say, "Well, where were we in December of 2015, five years ago, and where are we today?" Abhi will go into the details of today, so I'm not going to spend as much time there.

Now before I get into it, just one thing—just keep in mind, "Other" is all of the ideas that are less than 4% of the portfolio. That's what makes up that. But if you look at this, there are some pretty dramatic changes over time. At the end of 2015, the biggest allocation of this portfolio, at 20%, is subprime auto/ABS. That now only makes up about 6% of the portfolio.

If you look at, as an example, something that's exactly the other way, in 2015, CLOs were less than 1% of the portfolio; now they make up almost 20% of the portfolio.

There are two areas in here that you see in 2015 that don't exist in there now. They are less than 4%; one of them is actually less than 2%. One of them is the 15-year seasoned mortgage-backed securities. They were 7% of the portfolio in 2015; they are nothing today. And then you also see the stripped performing CMBS, which was a 12% allocation in 2015, is now less than 2[%].

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I bring those two areas up because they are small segments of the market. They are not broadly owned by people. They are very small. There are fewer people that can traffic in that sort of area. And we were able to take advantage of our size because those areas, at that period of time, brought a lot of value to the portfolio; they just don't happen to bring as much value today.

There are other areas in the portfolio that we use that are either small parts of the index, or aren't even in the index at all. But we use all those tools to help us reach our short and long-term objectives.

[Please reference slide 15] Now we don't have as much data as it relates to looking at the Flexible Fixed Income fund. But there are some things we can glean from it that I think are useful to showing you how we can be nimble and how being benchmark-indifferent helps us as we try to achieve our objectives.

Now we started this portfolio right at the very end, December 31 of 2018. We use June of 2019 as the period to start with because, okay, you've got to ramp up a portfolio from all cash to something. And by June we had at least committed ourselves, much of the cash, to a series of investments.

As I had mentioned earlier, 2019 we were de-risking the portfolio, FPA New Income fund. Because we didn't see value in credit; we wanted to have the highest quality in the A and above category. So the areas of concentration where we were looking at that point were performing CMBS, were mortgage passthroughs, and more ABS equipment. Those were the only areas we felt were extremely attractive in the high quality space, and that's why in that period of June of 2019, you see such a big allocation in the Flexible Fixed Income fund.

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You look at it today, the mortgage pass-throughs have gone. They are no longer a part of the portfolio to any discernible amount. We talked about that in the first quarter of 2020. The performing CMBS is less. But most of that has been driven by the portfolio's growth, and we just haven't been able to grow that segment as quickly as the portfolio itself. And the ABS equipment is about the same.

The other one that shows up, though, is CLOs are about 7% of the portfolio in June of 2019, and now they're 20%. Being able to be nimble is being able to be a little smaller and indifferent enables us to move around within sectors fairly rapidly as we see opportunities lay themselves in front of us to either commit capital or, in the case of the example, the mortgage pass-throughs, once the Fed became the largest buyer of those passthroughs in the marketplace in March and April of 2020, they no longer offered value, and we just exited that portion of the bond market.

[Please reference slide 16] So looking at these and these shifts, the next slide will help look at how does this come back to me, the investor? And again, we're going back and looking at something we looked at earlier, but you see the New Income fund has a yield-to-worst of 1.27. Its peer groups have a yield-to-worst of 90 basis points, and the 1-3 Year Aggs have got a 28 basis point yield.

Look at the duration difference. Our peers have a duration that is almost a year longer than us. Look at the credit sensitivity. It's almost four times as much as we have. But they don't have a higher yield. In fact, when you look at that yield divided by duration, we're about half as sensitive as they are, maybe even a little less. And it's this ability to move amongst various sectors, whether they're in the high-quality sector or in the credit section, and find just the best ideas, we think, is what leads to this type of metric.

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Flexible Fixed Income is newer. It's also in a category that is nontraditional. Nontraditional is a really broad aspect and approach that people can use to managing fixed income portfolios over there. So, it's tough to make a similar comparison here. But there are a couple of things that we can look at.

And we look at the category, we see a couple of things that stand out to us. One of the examples is the allocation to credit. An example is about half of those portfolios have an allocation to credit in the third quarter of 2020. It's now over 60%. At the same time, the duration of their portfolios have actually increased from the third quarter to the fourth quarter.

So, we look at those types of movements and say we're not surprised necessarily to see the kinds of volatility we saw in the nontraditional bond fund category. Our approach, looking at that risk and return, making sure you're getting paid for the risk you're taking, taking those elements that we learned and that we used from New Income and transferring them to Flexible Fixed Income, we think sets us up as a very good risk/reward alternative in that category, nontraditional, to what is typically seen.

[Please reference slide 17] And so I want to close out, wrap this up, just comparing the yield-to-worst of the Flexible Fixed Income fund and the New Income fund. And if you look at right to left, starting at the beginning of 2019, for all of 2019, the yield was not that different. And as we spoke about in those conference calls in 2019, we didn't see a lot of opportunities that were out there to take on risk as it related to credit, and we continued to reduce the risk that we were seeing in our high-quality portfolio. The portfolios tended to look similar in their duration and yield, and as you see here, the yield.

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You've got a slight change as you go into the first quarter of 2020. But once 2020 moved on, opportunity sets for Flexible Fixed Income, because it can take more risk, because it's got a three-year positive absolute return instead of one, started to present themselves. So, we have a different allocation to credit. There are times when we can find different high-quality bonds that work for Flexible Fixed Income that don't work for New Income.

So, as we're moving forward with this, and looking at it, we tell investors, "Look, if you have a longer time horizon and risk tolerance than you might for the assets that are in New Income fund, we think Flexible Fixed Income fund is a very good complement to New Income." We're using the same investment analysis. We're using the same investment team. And in many cases, we're using the same securities, just in a different allocation between the two portfolios.

And what it's producing for us is something that has got a slightly higher yield to it, got a slightly higher risk tolerance, risk element to it, but both of them are following that same objective over a short and long term period of really providing for the investor both a good short term return and long-term return when you compare it to the risk to the market, as we did earlier, in order to define that risk as standard deviation or volatility of return.

[Please reference slide 18] At this point, I'm going to turn it over to Abhi. He is going to go into a lot more detail about the market, and the types of things that we're buying today, and why.

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Abhi: Thank you, Tom. We have several slides to show on market conditions, but the punchline for all of them is going to be that the market is really expensive.

Yields are historically low. Spreads are also very low. Some spread-based relative value investors may try to compare today's spreads to the past, and craft some sort of argument that the market is not that expensive.

We are not making that argument. We are absolute yield-based investors, and yields have never been lower. In our view, the market is in uncharted territory; figuratively, and literally.

[Please reference slide 19] We'll start by looking at Treasury yields. The first chart shows the Treasury yield curve as of the end of 2019, September 2020, and December 2020. What jumps out is a large decline in risk-free rates. Over the course of the year, looking at maturities up to five year, Treasury yields are over 130 basis points lower; closer to 140 or 150 basis points lower for shorter bonds. Yields for maturities beyond five years are 75 to 120 basis points lower.

[Please reference slide 20] For context, this leaves risk-free rates at levels that haven't been seen in hundreds of years. The top-left chart shows the yield history on the U.S. 10-year Treasury going back to 1786. Yields have never been lower than they are today.

And this is not just a U.S. phenomenon. A similar story is at play in other major economies like the UK, Germany, and Japan.

[Please reference slide 21] Historically, low and negative risk-free rates lead to things that might make sense on a relative basis, but not on an absolute basis. For example, negative yielding debt. I guess it makes sense to own something that loses you less than something else, but you're still losing money. And yet the global market value of negative-yielding debt is near an all-time high.

[Please reference slide 22] In the U.S., there is a scramble to find yield. This chart shows the yield and spread on the aggregate bond index. Focusing on the right, the blue line shows that investment-grade bond yields are at historic lows. This is what happens when low spreads are benchmarked against historically low risk-free rates.

[Please reference slide 23] The same is true in short-maturity investment-grade bonds. This is the same chart for the 1-3-year aggregate bond index. Again, the blue line on the right hand side shows historically low yields in short-maturity bonds.

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[Please reference slide 24] One consequence of historically low yields is that they contribute to historically high duration. The blue line on the chart shows that the duration on the aggregate bond index is at an all time high. That means that investors who own the index, or something similar to it, own a lot of interest rate risk.

At the same time, the yield that they are getting for that risk is the lowest it's ever been. The green line shows the ratio of yield-to-worst to duration for the index, which is a way of measuring the amount of compensation you get per unit of duration risk. Looking at the right hand side, you can see that compensation is as low as it's ever been.

Broadly speaking, there's three ways that this can go for investors from here. One scenario is that rates don't change, in which case you will earn the yield-to-worst, which is about 1.1% versus a 6.4 year duration. Another scenario is that rates could decline, in which case bond prices will rise further, and the return will be more than yield-to-worst. The third scenario is that rates rise and the return will be lower than the yield-to-worst as bond prices fall.

Now keep in mind that yields falling or rising could happen via lower risk-free rates and/or lower spreads.

As a point of reference, if the yield on the aggregate bond index rose by approximately 20 basis points, the index would have a negative total return over 12 months. That's not much cushion.

[Please reference slide 25] A similar dynamic is at play in short maturity bonds as well. This is the same chart, but for the 1-3 Year Aggregate bond index. The green line shows that the yield-to-worst to duration ratio is as low as it's ever been. Interestingly, this ratio is very similar to the ratio on the overall aggregate bond index, but the longer-duration aggregate bond index has over three times the duration risk.

It doesn't make much sense to us to take on the extra duration of the longer-duration aggregate bond index when you're not getting paid for that extra duration. I guess it could make sense if you had high conviction that rates are going decline, but [we believe] there's probably better ways to express that view.

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[Please reference slide 26] Moving on to the high-yield market—looking at the right-hand side of this chart, yields on the high-yield index are at all-time lows. Now what is particularly interesting is that the yield is lower today than it was at the start of the year, even though the world is in a worse place economically, and today there is higher leverage and more businesses at risk of failing. But this is an instance where people might say that the spread is not unreasonable, or at a 4.2% yield, they can get more yield than they can get anywhere else.

In our view, it's a trap. As we often say, dollars are what will make you whole on an investment. Dollars of return compensate for potential losses. That's measured by yield, not spread. Said another way, you can't spend basis points of spread, but you can spend dollars of yield.

[Please reference slide 27] We won't belabor the point, so we will just quickly point out that the story is the same in the leveraged loan market. Low rates and low spreads combine to create historically low yields. Overall, there has never been so little compensation for duration or fundamental credit risk at a time when those risks are abnormally high.

[Please reference slide 29] Let's move on to a review of both funds. To provide some context for the performance and positioning of the two funds, this chart shows spreads on different types of highly-rated, short-duration structured products bonds that are similar to what constitutes much of both New Income and Flexible Fixed Income.

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As shown on this chart, after blowing out in March, spreads are now lower than they were when they started the year. The recovery in spread since March is supportive of performance, but makes for a tough investing environment, as we highlighted on the market slides.

[Please reference slide 30] Moving on to the funds, we'll start with New Income's [gross] performance. The first three columns show New

Income's performance for the fourth quarter, and the last three columns show the performance for the full year 2020.

The bottom of the middle column shows that New Income returned 65 basis points before fees during the fourth quarter. In the fourth quarter, the largest contributors to performance were corporate holdings, with both higher prices and coupons contributing to performance. The corporates are listed towards the bottom of the table. In general, prices rose due to a combination due mostly to the recovery in credit spreads.

The second largest contributors to performance were collateralized loan obligations, or CLOs, the fourth line from the top, driven by a combination of coupon payments and higher prices as a result of lower spreads.

The third largest contributors to performance were asset-based securities backed by equipment, the third line from the top, with most of that return coming from coupon payments. The only meaningful detractor from performance at the sector level during the quarter were Ginnie Mae project loan interest-only bonds, which show up here as CMBS strips. These bonds declined in price as a result of fast pre-payment speeds. Those price declines were partially offset by prepayment penalties.

(00:37:48)

At the bottom of the last column, we show that New Income returned 3.07% before fees for year ended December 31, 2020. The largest and second largest contributors to performance were ABS backed by auto loans or leases, and ABS backed by equipment. These are the second and third rows from the top, respectively.

The third largest contributors to performance were non-agency collateralized mortgage obligations, with the majority of that return coming from high-quality bonds backed by reperforming mortgages. Those bonds are included under CMO non-agency on this page. In all three cases, returns came from a combination of coupon payments, and to a lesser extent, lower yields driving up bond prices over the course of the year. Similar to the fourth quarter, the only meaningful detractors from performance at the sector level during the year were Ginnie Mae project loan interest-only bonds for the same reasons described a minute ago.

[Please reference slide 31] These pie charts show the New Income portfolio broken down by investment idea, with the holdings as of September 2020 on the left, and the holdings as of December 2020 on the right. Given the low yield environment that offers little compensation for credit risk or duration risk, we have been investing in short-duration, high-quality bonds that we expect will be repaid, even in a bad economy.

In the fourth quarter, those investments include CLOs, asset-backed securities, and non-agency commercial mortgage-based securities. Offsetting those investments, maturities of existing holdings and dilution from inflows led to exposures to those and other areas declining during the quarter.

In credit, we have been looking for investments that we think have a low likelihood of being impaired, and limited short-term mark to market risk. During the quarter, those investments included leveraged loans, and newly-issued bonds backed by nonperforming residential mortgages.

Tom: Abhi, you muted yourself.

(00:39:59)

Abhi: Finally, we also increased the size of our Treasury hedge. We went into detail about the hedge during our third quarter conference call. But the quick summary is that the core portfolio, which excludes the hedge, has a duration of approximately a year.

We think there’s meaningful uncertainty around the economy. For a time, markets were optimistic about rates rising on the back of reflation. However, we have seen in the past that reflation efforts have petered out. If rates end up declining as a result of low inflation or a weak economic environment, we want to have some upside potential in the portfolio, which our core portfolio won't deliver because of its short duration. We added a five-year Treasury position to provide that upside.

Alternatively, if rates rise, [we believe] the Treasury position is sized to give us comfort that we can deliver a positive return over 12 months for the portfolio overall, consistent with our mandate. Moreover, we can use the liquidity of the Treasury market to change the size and complexion of the hedge based on how the market unfolds over time. Overall, we're trying to get to an upside versus downside return profile for New Income that is consistent with our objectives.

[Please reference slide 32] This slide shows the portfolio broken down by high-level sectors. The increase in the size of the Treasury position increased the portfolio's duration from 1.3 years to 1.5 years.

[Please reference slide 33] This slide shows the upside versus downside profile that was just referenced. These bars show the portfolio's hypothetical total return before fees over the course of 12 months, based on the changes in yield shown on the x axis. On the far right, you can see that even with the Treasury hedge, the portfolio could withstand an increase in yield of around 200 basis points over 12 months across the entire yield curve before producing a negative 12-month total return before fees. Note that that change in yield could come via a higher risk-free rate and/or higher spreads.

(00:42:00)

On the left, lower yields create the prospect of a 12-month total return that is meaningfully greater than the portfolio's current yield-to-worst.

[Please reference slide 36] Finally, this table shows the portfolio broken down by rating. Consistent with our concerns about low yields offering little compensation for credit risk, the portfolio's exposure remains heavily weighted toward very high-quality, AAA-rated, and AA-rated bonds. Overall, high-quality investments, defined as everything rated A or higher, represent [approximately] 93% of the portfolio, while credit investments, defined as everything rated BBB or lower, is up only slightly at [about] 7% of the portfolio.

[Please reference slide 39] Turning now to Flexible Fixed Income. The first slide shows Flexible Fixed Income's [gross] performance for the fourth quarter and full year 2020. The bottom of the third column of numbers shows that Flexible Fixed Income returned 1.3% during the fourth quarter before fees. The largest contributor to performance during the quarter was corporate bonds and bank debt, with both higher prices and coupons contributing to performance. In general, prices rose due to a combination of the continued recovery in credit spreads and improved underlying operational performance at the company levels.

The second largest contributor to performance was collateralized loan obligations, driven by a combination of coupon payments and higher prices as a result of lower spreads. And finally, the third largest contributor to performance was asset-backed securities backed by equipment, with most of the return due to coupon payments. At the sector level, there were no meaningful detractors from performance.

The bottom of the last column shows that the Fund returned 5.03% before fees for the year ended December 31, 2020. The largest contributor to performance was corporate bonds and bank debt. These investments benefited from coupon payments and price appreciation.

(00:44:00)

The second largest contributor to performance was CLOs, with the return driven by coupon payments and price appreciation.

For both the corporate and CLO investments, price appreciation was particularly beneficial for investments that we made after prices declined in March [2020] as a result of the market-wide COVID-19 concerns.

The third largest contributor to performance was asset-backed securities backed by auto loans or leases. These bonds benefited from coupon payments in addition to lower yields driving up bond prices over the course of the year. At the sector level, there were no meaningful detractors from performance.

Before moving on, I would like to provide a bit more color on Flexible Fixed Income's 2020 performance. As a reminder to those who are new to our strategies, Flexible Fixed Income was launched at the end of 2018 with the goal of a higher long-term return than New Income, and with the capacity to take on more credit risk to achieve that.

However, and importantly, Flexible Fixed Income was never designed to always be invested in credit. Rather, it was designed to employ the same absolute return-investing framework that we have employed with New Income for over 35 years which means that Flexible Fixed Income's credit exposure would ramp up when prices were attractive.

In addition, it was designed with the flexibility to invest across sectors and industries, seeking out attractive investments, but only investing in credit when it's attractive, without any compulsion to invest when the market is expensive. In fact, we told early investors in Flexible Fixed Income that until there's a dislocation in credit markets, Flexible

Fixed Income and New Income might look somewhat similar.

Then 2020 happened. And in March, markets dislocated in a big way. At that point, we sprung into action. During the turmoil that was embroiling the markets, we deployed a significant amount of capital into credit. We made 73 different investments in both corporate credit and structured product credit, which speaks to the flexibility of our approach. On average, we invested about a third of the portfolio into credit, resulting in our credit exposure approximately doubling over the course of the year.

(00:46:10)

But in addition to that, we also made 43 different investments in highly-rated structure product bonds, in CLOs, asset-based securities, and commercial mortgage-backed securities that were offered at significant discounts. Those investments represented about a fifth of the portfolio on average. We were able to respond quickly to opportunities because we had a library of ideas that we had been building for years, and our team hustled and pulled a lot of long hours to look at new ideas that popped up.

I want to take a moment to publicly acknowledge our team: Felix, Joe, Julian, Naz, Prakash, and Ryan, for their hard work and intensive research.

This opportunistic approach to investing led to our credit investments contributing approximately 175 basis points over the fund's full-year return. And those opportunistic highly-rated investments contributed another 49 basis points of return.

As we all know, the markets followed a huge sell-off in March with a huge recovery over the past nine months, as the influx of money from central banks and governments flooded markets with cash. So why didn't we do more? Why didn't we deploy more capital into credit?

The answer is that just because prices are higher doesn't mean that all is good. We chose investments and companies and assets that we expected would retain value in a post-COVID-19 world, while trying to forecast what that world would look like. We skipped investments in businesses that we thought faced permanent impairment from new COVID-19 secular challenges, or where we didn't think they had enough liquidity to survive.

That said, a lot of those businesses that we passed on are trading today as if everything is fine. But again, prices are not necessarily the best measure of quality. The low prices in March [2020] demonstrated that, and it's being demonstrated again with today's high prices.

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[Please reference slide 40] Looking at the pie charts showing the quarter over quarter changes by investment idea, our credit investments included, among other things, corporate bank debt and high yield, loan securitizations, and newly issued securitizations of nonperforming residential mortgages. In high-quality bonds, we invested in a variety of ABS, including ABS backed by prime or subprime auto loans or leases, servicer advances, or insurance premium loans, CLOs, and non-agency commercial mortgage-backed securities.

The exposure in some of these areas declined over the past three months, as our [FPFIX] investments were offset by maturities of existing holdings and dilution from inflows into the Fund.

[Please reference slide 42] Here we show the simulated [hypothetical] returns before fees for the portfolio based on different changes in yield shown on the x axis. We don't specifically manage Flexible Fixed Income to a positive one-year return, but we do try to limit the short-term volatility in the fund's performance. To that point, the right-hand side shows that Flexible Fixed Income could experience over a 200 basis point increase in yield on its holdings and still deliver approximately a 1% return before fees.

As a reminder, once again, that increase could come in the form of higher risk, free rates, and/or spreads. The left side shows that there is also potential for returns higher than the yield-to-worst if yields decline. Finally, the table shows the portfolio broken down by rating. The credit exposure, which includes everything rated BBB or lower, is basically unchanged. The pace of our credit investing slowed meaningfully over the course of the fourth quarter, as the decline in credit yields picked up pace. [Please reference slide 43] Thank you for the time. And we will now answer any questions that have come up.

(00:49:46)

Kristina: [Please reference slide 45] Thank you, Abhi. Thank you to those of you who submitted questions in advance. We covered many of them in the prepared remarks, and will now address the rest of them before the questions submitted during the live presentation.

So first, can you talk about your expectations for the 10-year rates, and how that will affect total returns in Fixed Income? Also, thoughts on the lower recovery rates, I think, that are showing up?

Tom: Okay, there is also a question that has come in during the broadcast regarding some comments by Jeremy Siegel about where he thinks the 10-year Treasury is going to be a year from now and two years from now. So, I will cover both of them at the same time.

What we find ourselves in today when we think about Federal

Reserve policy, monetary policy, and fiscal policy, is a situation that is far more acute than what we found ourselves in during the period of 2009 through 2012.

And what I mean by acute is the quantitative easing undertaken by the Fed is far greater today than it was then. The rapidity and how fast it got to a zero interest rate policy is much greater today than it was then, and the change in how the Fed views CPI, instead of 2% being the ceiling, they talk about, "Well, it needs to average 2% inflation over a long period of time," in which "long period of time" is not defined.

So, when we start to think about that, and think about where we are today, three things are popping up. The Fed is probably not doing anything with the overnight rate for the foreseeable future[4]. That is according to a quote from them; is that "foreseeable future" 2022 or 2023? That could be. So that means maturities of three years and in Treasuries are probably going to tend not to change very much.

(00:52:10)

But their allowance for higher levels of inflation means that things beyond, maturities beyond three years—say 5, 10, 15—may find themselves rising some, because people expect higher levels of inflation.

[4] https://www.federalreserve.gov/monetarypolicy/files/FOMC_LongerRunGoals.pdf

What may drive into that, and we saw some of that in the fourth quarter, is as the vaccine became available and starts to roll out, [we believe] investors are starting to think, “Okay, we’re going to start economically to get back to normal as we progress through 2021, whatever normal is. The difficulties of 2020 will tend to be more behind us than in front of us.”

And the other one is fiscal policy. There has been massive fiscal policy that’s gone on, with a design of trying to put money in small businesses’ and households’ pockets to tide them over during a period of stay at home orders and controlling the pandemic. As we sit today, there is a pretty intense discussion about do we need another stimulus plan. Well, it would appear that the near-term goalposts for that are somewhere between $600 billion and $1.9 trillion. I have no idea which one of those it will be, but that seems to be the mark that it set.

So, when you put those together, it just leads us to think there will tend to be pressures periodically on longer-term interest rates, because people will look at that and hear, “Oh, inflation is going to increase.” But inflation increasing is not necessarily a given. We have seen arguments on both sides of why it will and why it won’t.

So that leads us to this longer end of the yield curve maybe having more volatility to it going forward, and the only person who is going to probably want to control that volatility is the Federal Reserve Bank and how they do quantitative easing. But that's what we see going forward, so don't be surprised if you see that yield curve steepen and flatten some as the long end goes up and down.

(00:54:16)

Keep in mind that at current levels of difference between the yield of the ten-year and the two-year, it's about a long-term median. It's actually not that steep. Neither is it that flat. It's just about somewhere in the middle.

As it relates to the lower recovery, I'm not quite sure what the question, or the person that asked the question—but I'll answer it this way: we have spoken about higher levels of leverage in the economy, and how that higher level of leverage over long periods of time seems to led to slower economic growth. Whether this time around of injecting more money into the system or borrowing more will change that is an open question; we have no idea.

If the recovery is one thinking about, well okay, as companies work through bankruptcy and reorganization, what's the recovery of those bonds? If you have higher levels of leverage, the potential for that recovery rate tends to be somewhat lower as you move forward.

So, as we look forward, we expect that the short end is not going to move too much, short being three years and in, until the Fed announces in some way that they are going to change their Fed funds policy. And it wouldn't surprise us to see the longer end of the yield curve move up and down as people become more fearful of inflation and growth and less fearful of inflation and growth.

Kristina: Tom, we received a follow-up question to this. Is it your household view that the Fed has broken its own charter and law for the Federal Reserve Act?

(00:56:05)

Tom: Wow. There's a loaded question. If I think through that—and I don't know if there's necessarily a house view—we can put down that the Federal Reserve definitely pushed the envelope of what it thought was allowable and not allowable when it opened up and said, "Okay, we will provide leverage to the Treasury Department having various bond purchasing programs[5]," whether it was those designed for high-quality asset-backed securities, or those designed for investment-grade corporates, or those designed even to buy some of the BB high-yield corporate.

[5] Source: U.S. Treasury, Federal Reserve. https://home.treasury.gov/news/press-releases/sm968.

Now the Fed didn't buy them themselves; they were purchased by the Treasury Department, the U.S. government. Nothing says they can't do that. But the Fed stepped in and said, "We'll provide borrowing, or lending, I should say, for those programs to be set up." And that definitely pushes the envelope of what the charter of the Federal Reserve is, when they announced those programs back in April.

Interestingly, very few people took up those programs, there wasn't much money actually spent in them. The end result of just announcing them seemed to bring the markets back to having the ability to finance the markets itself.

If you think about it as a quantitative easing program, then no, not necessarily has it broken its charter. You think back to World War II, and they had a very distinct and announced yield curve policy that they instituted and kept for quite a long time period, from 1942 up until 1950. That is within the realm of what they can do, because they were merely buying U.S. Treasuries which, under their charter as the Federal Reserve Bank, they are entitled to do.

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So, whereas I don't think they actually broke the charter; they pushed the envelope on it pretty hard in some areas during 2020.

Kristina: Thank you, Tom. Another question. Can you comment on the liquidity profile of the Fund? It appears the portfolios are mostly invested in the securitized products that take longer to settle. Abhi?

Abhi: Yes, thank you, Kristina. So, I think the person asking the question may have been thinking about agency mortgage pools, which, depending on how you execute that trade and when you execute it, could take many days to settle.

As a point of reference, we have very little of our portfolio, almost a de minimis portion of the portfolio in agency mortgage pools. The vast majority of the securitized product into our portfolio trades on a T+2 basis. So, in the event that we did have to sell things, we would expect the settlement of the funds to happen within two days of the trade. That's the first point.

The second point is with respect to liquidity in the fund, and I'll start with the New Income fund, we have quite a large amount of liquidity in the fund. As of the end of the fourth quarter, we had about 5% of the portfolio in cash and equivalents, plus on top of that, another 13% or so in Treasury bonds, which for those who are unfamiliar, Treasuries trade on a T+1 basis, and in a pinch, you could actually do a same-day settle trade. So, we have no concerns about liquidity in the New Income fund.

A similar story in the Flexible Fixed Income fund, which does not have the same Treasury position, but at the end of the fourth quarter, had about 13% of the portfolio in cash and equivalents. So, there's quite a bit of liquidity on hand.

[Please reference slide 37] And then if I could just quickly ask Kristina to flip the presentation to slide 37—again, just as a point of reference, over a longer-term horizon, what the slide on 37 shows is an estimate of the amount of the portfolio that would turn into cash just from regularly scheduled amortization and maturities of the underlying holdings. So if you just add up these bars, or even look on the individual quarter basis, we have quite a bit of the portfolio which just organically turns into cash without us having to do anything—meaning we don't have to sell anything in order for that to happen.

(01:00:37)

So I think both in the near term and medium to long term there's a very significant amount of liquidity in both funds.

Kristina: Thank you, Abhi. There are no other questions at this time. We want to thank those of you who listened to the FPA New Income and FPA Flexible Fixed Income Fourth Quarter 2020 Webcast. We now turn it over to the system moderator for closing comments and disclosures.

Moderator: [Please reference slides 47-52] Thank you for your participation in today's webcast. We invite you, your colleagues, and shareholders to listen to the playback of this recording and view the presentation slides that will be available on our website within a few days at FPA.com. We urge you to visit the website for additional information about the Funds, such as complete portfolio holdings, historical returns, and after-tax returns. Following today's webcast, you will have the opportunity to provide your feedback and to submit any comments or suggestions. We encourage you to complete this portion of the webcast. We know your time is valuable, and we do appreciate and review all of your comments.

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We hope that our quarterly commentaries, webcasts, and special commentaries will continue to keep you appropriately informed on the strategies discussed today. We do want to make sure that you understand that the views expressed on this call are as of today, and subject to change without notice based on market and other conditions. These views may differ from other portfolio managers and analysts at the firm as a whole, and are not intended to be a forecast of future events, a guarantee of future results, or investment advice.

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This concludes today's call. Thank you and enjoy the rest of your day.

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[END FILE]

Basis Point (bps) is equal to one hundredth of one percent, or 0.01%. 100 basis points = 1%.

Bloomberg Barclays US Aggregate Bond Index provides a measure of the performance of the U.S. investment grade bonds market, which includes investment grade U.S. Government bonds, investment grade corporate bonds, mortgage pass-through securities and asset-backed securities that are publicly offered for sale in the United States. The securities in the Index must have at least 1 year remaining in maturity. In addition, the securities must be denominated in U.S. dollars and must be fixed rate, nonconvertible, and taxable.

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Bloomberg Barclays U.S. Universal Bond Index represents the union of the following Bloomberg Barclay's indices: U.S. Aggregate Index, the U.S. Corporate High-Yield Index, the 144A Index, the Eurodollar Index, the Emerging Markets Index, and the non-ERISA portion of the CMBS Index. Municipal debt, private placements, and non-dollar-denominated issues are excluded from the Universal Index. The only constituent of the index that includes floating-rate debt is the Emerging Markets Index.

Morningstar's Short-term Bond Category portfolios invest primarily in corporate and other investment-grade U.S. fixed-income issues and typically have durations of 1.0 to 3.5 years. These portfolios are attractive to fairly conservative investors, because they are less sensitive to interest rates than portfolios with longer durations. Morningstar calculates monthly breakpoints using the effective duration of the Morningstar Core Bond Index in determining duration assignment. Short-term is defined as 25% to 75% of the three-year average effective duration of the Morningstar Core Bond Index. There were 600 funds in the category at 12/31/2020

Morningstar's Nontraditional Bond Category contains funds that pursue strategies divergent in one or more ways from conventional practice in the broader bond fund universe. Many funds in this group describe themselves as "absolute return" portfolios, which seek to avoid losses and produce returns uncorrelated with the overall bond market; they employ a variety of methods to achieve those aims. Another large subset are self-described "unconstrained" portfolios that have more flexibility to invest tactically across a wide swath of individual sectors, including high yield and foreign debt, and typically with very large allocations. Funds in the latter group typically have broad freedom to manage interest rate sensitivity, but attempt to tactically manage those exposures in order to minimize volatility. The category is also home to a subset of portfolios that attempt to minimize volatility by maintaining short or ultra-short duration portfolios, but explicitly court significant credit and foreign bond market risk in order to generate high returns. Funds within this category often will use credit default swaps and other fixed income derivatives to a significant level within their portfolios.

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