momentum

Harmony Portfolios

Quarterly Report

31 March 2015

Q1

Momentum Global Investment Management (Company Registration No. 3733094) has its registered office at 62 Queen Street, London, EC4R 1EB.

HARMONY FUNDS
Multi Manager, Multi Asset Class Solutions

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Table of contents

1. Portfolio Objectives and Overview 1
2. Portfolio commentary 2
3. Recent portfolio activity and positioning 4
4. Target portfolios 5
5. Fund and peer group performance 6
6. Market commentary 7
7. Market performance 9
8. Important notes 10

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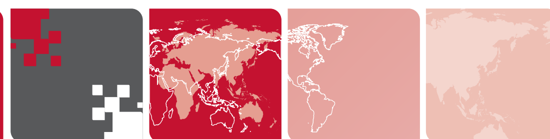
1. Portfolio objectives and overview

The eight Harmony Portfolios are offered via single priced Funds, providing a cutting edge solution for investors with efficient management, improved client administration and enhanced liquidity. The eight profiles are US Dollar Balanced, US Dollar Growth, Europe Diversified, Sterling Balanced, Sterling Growth, Asian Balanced, Asian Growth and Australian Dollar Growth. With eight bespoke Funds to choose from, the individual needs of each client can be provided for via a combination of one or more of these core solutions, together with selected satellite funds at a client level.

Each Harmony Fund offers a well-diversified solution, with exposure to seven key asset classes: cash, investment grade fixed income (bonds), alternative fixed income (emerging market debt and high yield bonds), equities (shares), alternatives (funds of hedge funds), commodities and property. The portfolios are diversified by asset class, currency, regional equity exposure, manager and style in order to provide sustainable returns and reduced volatility. Many of the managers are inaccessible to the retail market and all are appointed at a highly competitive fee level.

The portfolios are managed by a team of experienced investment professionals at Momentum Global Investment Management, authorised and regulated by the Financial Conduct Authority in the UK and is an authorised Financial Services Provider in South Africa in terms of the Financial Advisory and Intermediary Services Act 2002 (FAIS). Investors can be confident that their portfolios are being managed within a strictly regulated environment by a well qualified and experienced team with significant resources spent on manager research across the globe. Momentum Global Investment Management is wholly owned by MMI Holdings in South Africa.

The Harmony Investment Committee is in regular contact with the team in London and this ensures that the construction of the Harmony Funds is a two way process. Any comments from clients and advisers can therefore be fed through to the portfolios if deemed appropriate.



2. Portfolio commentary

The Harmony Fund range is designed to provide investors with a balance between the stability of bond returns and the potential for significant participation in equity market strength. The funds have either a “Balanced”, “Diversified” or “Growth” profile, with each offering progressively greater exposure to the equity market. On a through-the-cycle basis, they will have the majority of their assets invested in a “home” region with the balance invested in global assets. The particular weighting to each region will depend on relative valuation opportunities. These funds will also use asset allocation on a tactical basis to take advantage of short term valuation opportunities.

All of the Harmony funds posted gains in their respective base currencies during the first quarter of 2015. These ranged from modest returns of 0.2% and 0.6% for the USD Growth and USD Balanced funds, to very strong gains of 7.1% and 10.8% for the Australian Dollar Growth and Europe Diversified funds respectively. In between, the sterling portfolios returned 4.3% and 5.0%, for the Balanced and Growth funds respectively, while the equivalent Asian funds returned 1.6% and 2.3%. The funds have all provided positive returns over twelve months as well, with a similar ranking of returns to the last quarter and with returns ranging from 2.1% to 16.3%. This quarterly trend is also reflected in the yearly numbers, with all funds providing positive returns, and the Australian Dollar Growth and Europe Diversified funds outperforming the US dollar and sterling funds. Twelve month returns range from 2.1% to 16.3%. All returns are quoted net of fees.

Considering the first quarter in more depth, a key factor in explaining the variation in fund returns lay with the relative performance of different equity markets. Equity indices for Europe ex UK and Australia were standout performers with gains of 18.9% and 10.3% over the period, whilst Asia Pacific ex Japan and UK indices posted more modest gains of 4.4%. Meanwhile the US market only managed a small gain of 0.8%.

Despite most equity markets delivering decent or very good returns in local currency terms globally, the MSCI World index only gained 2.3% in US dollar terms over the period. Global emerging market equities broadly matched this return. Looking at the sectors that affected the performance of Harmony funds, global listed real estate outperformed with a gain of 4.5% in US dollar terms, while global listed infrastructure underperformed with a decline of 0.9%.

Fixed income markets showed less variation in returns during the quarter. European government bonds were the standout performer, gaining 4.3%, while other major markets posted solid returns of between 1% and 3% in local currency terms. We continue to have minimal exposure to developed market government bonds across most of the Harmony funds on valuation grounds. Instead, we hold US high yield bonds, convertible bonds and emerging market debt (EMD) which offer relatively attractive valuations and also contributed positive returns over the quarter. Our global and Asian convertible bond holdings returned 3.5% and 4.0% respectively over the quarter, while our sovereign hard currency EMD holding returned 2.5%.

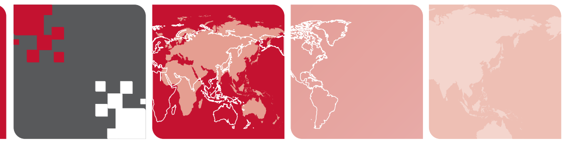
Currency moves also had a bearing on the range of Harmony fund returns over the period. The US dollar strengthened versus most major currencies: the euro saw the largest decline in value versus the US dollar, sliding by 11.3% over the period, while the Australian dollar and pound sterling fell 6.9% and 4.9% respectively. This acted as a headwind to returns for the funds that have the US dollar as their reporting currency, but conversely boosted returns for the other funds.

Our equity holdings across the different portfolios showed a reasonably wide range of returns, with the over-riding theme being the outperformance of growth styles and underperformance of value styles. The funds where the underlying manager has a growth/ earnings acceleration orientated approach include Lindsell Train (6.2% outperformance) in the sterling funds, Wells (4.1% outperformance) in the US Dollar funds and American Century (+0.5%) across all the funds. Funds where the manager has a deep value approach struggled, for instance Dimensional Emerging Markets (2.8% underperformance) and Kopernik (3.6%) both underperformed versus their respective benchmarks. Both of these funds are held across all portfolios albeit at relatively low weights.

Other holdings that delivered notable performance included the First State Global Listed Infrastructure and the Polar Japan fund, which are both held across all the Harmony portfolios. The former returned 1.2% in US dollar terms, outperforming the sector benchmark by 2.0% and increasing their outperformance over six months to 4.1%. The latter underperformed the Japanese market but nevertheless delivered a very strong absolute return of 6.3%.

Looking back at the portfolio changes made over the quarter, a meaningful asset allocation change was made in February as we further increased the allocation to US high yield bonds. Having sold out of the asset class on valuation grounds around the beginning of 2014, we reinvested via a short duration strategy run by AXA Investment Managers towards the end of that year, after valuations had undergone a large correction back to levels that we considered attractive. Since then credit spreads continued to widen making the asset class yet more attractive and prompting us to further increase exposure, this time by adding a full duration strategy run by the same manager. The fund represents a diversified portfolio of bonds from around 200 corporate issuers rated as sub-investment grade and offered an attractive yield of around 8%. This level of yield, in our opinion, more than compensates for the inherent risks of the asset class.

Another significant change affecting all of the funds was made during March. After conducting a detailed research review into the global listed real estate sector and reviewing and meeting dozens of managers, we have replaced our previous incumbent manager in this sector, Cohen & Steers, with Third Avenue. We believe now is a good time to make this manager change in the Harmony funds; Real Estate Investment Trusts (REITs) have performed very well in recent years, with investors being attracted to the relatively high dividend yields on offer, leading to higher valuations across the sector. Third Avenue look beyond the typical universe of other listed real estate

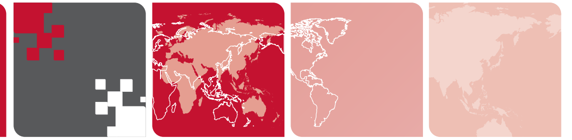


strategies in order to identify securities that offer more attractive valuations and better growth potential, and we believe their strategy is capable of delivering long term outperformance compared to the sector.

Third Avenue is a specialist value orientated manager based in New York, managing approximately $12bn across various strategies including Global, US Small Cap, International and Real Estate Equity as well as a focused credit strategy. They are owned by AMG, a global asset management company that also owns several other boutique investment management firms that all act autonomously. Third Avenue's Real Estate Value strategy was launched in 1998 and is managed by a dedicated team of three portfolio managers and three analysts. Michael Winner, one of three co-portfolio managers, has managed the strategy since inception, and was joined by Jason Wolf and Ryan Dobratz in 2004 and 2006 respectively. The team members are highly focused on this strategy and very experienced, with each benefiting from additional real estate related experience prior to starting their current roles. Since inception the strategy has been managed according to a long term value orientated approach, investing in out of favour securities with a focus on total return and capital appreciation. The team mostly seek exposure to prime real estate in core markets and have a broad investable universe which includes equities that are classified as REITs, Real Estate Operating Companies or homebuilders as well as businesses that are focused on providing real estate related services. These securities offer the diversification benefit and long term return potential of real estate, but with the liquidity of an equity security. The team consistently implement a strong and sensible investment process and the resultant portfolio, which is highly differentiated from both the benchmark and peers, is concentrated in only 30-40 positions with the top ten holdings usually accounting for 40-50% of the Fund. This concentrated approach allows them to take high conviction positions. Holdings are typically divided between strategic positions, with a five to ten year investment horizon, and tactical positions, with a shorter term outlook of two or three years.

Going forward, markets continue to face a number of challenges. Divergent growth paths both within the developed markets and between developed and emerging markets; differing monetary policy paths within the West and uncertain geopolitics are all potential sources of portfolio shocks in the short term. The impact of these short term risks is best mitigated by diversification of return drivers in a portfolio. Today the Harmony funds have a broad based asset allocation which resists the temptation to over-concentrate risks in any one asset class, style or sector. We remain of the view that global equity markets offer reasonable value over the medium to long term whereas government bonds do not and this view is reflected in the asset allocation of the funds.

Source: Bloomberg / Morningstar. Returns in US dollars unless otherwise stated, March 2015. Past performance is not indicative of future returns.



3. Recent portfolio activity and positioning

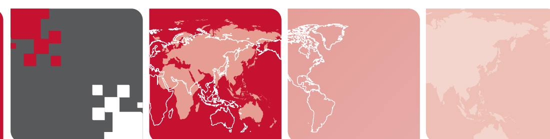
During the fourth quarter the following changes were made to the funds:

Increased
- US High Yield (short duration)

Decreased
- Global listed real estate

Manager changes during the quarter:

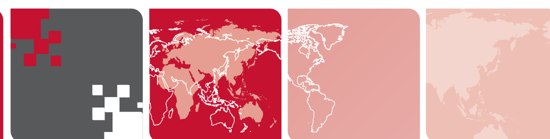
- Initiated holdings in Axa WF US High Yield Bonds
- Initiated holdings in Third Avenue Real Estate Value
- Sold holdings in Cohen & Steers Global Real Estate



4. Target portfolios

	Balanced	Diversified	Growth
Equities	43.0%	55.5%	68.0%
Fixed Income	32.0%	31.5%	18.0%
Property	7.0%	8.0%	7.0%
Cash	18.0%	5.0%	7.0%
Total	**100.0%**	**100.0%**	**100.0%**

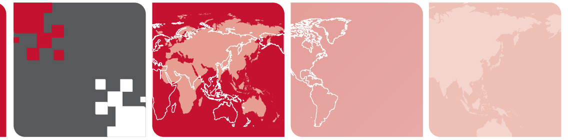
These target weights are correct as at the time this report is published and are indicative of the managers' medium term outlook for markets, which is driven principally by their assessment of relative valuation opportunities. The property exposure includes exposure to listed infrastructure.



5. Fund and peer group performance

Fund returns (local currency)	Performance to 31 March 2015				
	3 months	6 months	2014	2013	3 Years (annualised)
Asian Balanced (US dollars)	1.6%	0.7%	0.7%	2.5%	2.1%
Peer group median	-2.6%	-5.1%	-4.5%	7.4%	1.0%
Asian Growth (US dollars)	2.3%	1.6%	2.3%	6.2%	4.4%
Peer group median	-1.7%	-4.1%	-3.7%	7.4%	1.6%
Global equities	2.3%	2.7%	4.2%	22.8%	10.8%
MSCI AC Asia Pacific ex Japan	4.4%	3.7%	2.8%	3.4%	6.5%
AUD Growth	7.1%	11.1%	6.0%	17.1%	11.6%
Peer group median	4.5%	8.4%	5.7%	17.3%	10.8%
Global equities	9.7%	17.9%	14.5%	43.2%	23.3%
ASX All Ordinaries	10.2%	13.0%	5.0%	19.7%	14.7%
EUR Diversified	10.8%	13.8%	6.0%	7.8%	9.9%
Peer group median	6.6%	7.5%	5.2%	4.8%	6.6%
Global equities	15.3%	20.8%	18.6%	17.5%	19.0%
MSCI Europe ex UK	18.9%	18.6%	6.4%	22.1%	19.0%
GBP Balanced	4.3%	6.6%	3.2%	10.6%	7.1%
Peer group median	2.8%	5.0%	3.1%	9.9%	6.2%
GBP Growth	5.0%	8.3%	4.1%	16.9%	10.1%
Peer group median	2.9%	5.0%	3.0%	10.3%	6.3%
Global equities	7.5%	12.2%	10.6%	20.5%	13.5%
MSCIUK	4.0%	3.6%	0.5%	18.5%	9.3%
USD Balanced	0.6%	2.0%	2.0%	10.6%	4.9%
Peer group median	-0.7%	-0.8%	0.7%	11.2%	4.6%
USD Growth	0.2%	2.8%	4.1%	17.6%	7.5%
Peer group median	-0.6%	-0.6%	0.9%	13.3%	5.4%
Global equities	2.3%	2.7%	4.2%	22.8%	10.8%
S&P 500	1.0%	5.9%	13.7%	32.4%	16.1%

Source: Bloomberg, March 2015. Past performance is not indicative of future returns.



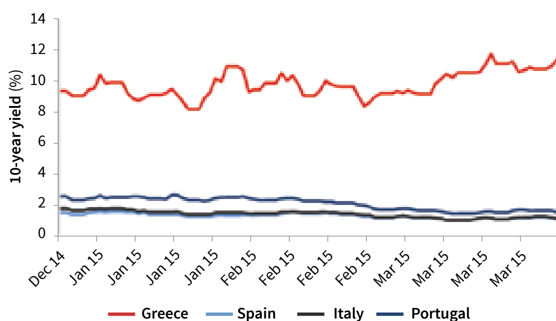
6. Market commentary

Markets continued to be dominated by central bank statements and policy moves in the first quarter of 2015. The European Central Bank (ECB) announced details of its quantitative easing programme and started buying assets at a rate of €60 billion per month from 9 March. Meanwhile, the Federal Reserve indicated its desire to begin the process of policy normalisation, dropping the word 'patient' when referring to its stance on raising interest rates. In the background, the Bank of Japan also remains accommodative, continuing to purchase assets at the rate of $50-60 billion per month.

European and Japanese equity markets were the standout performers over the quarter. European equities added 18.9% in euro terms, while Japanese stocks rose by 10.5% in yen terms. In the US, equities added the lower 0.8%. In fixed income markets, US Treasuries added 1.8%, UK gilts added 2.9% in sterling terms and euro government bonds added 4.3% in euro terms. The yield on the 10-year German bund fell to an extraordinary 0.18% at the end of March. Corporate bonds also enjoyed a strong quarter including high yield bonds, with US high yield returning 2.5% and European high yield adding 3.0% in euro terms.

In Europe, politics once again took centre stage as the radical, left-wing Syriza party came to power in Greece on a wave of anti-establishment sentiment and a promise to end the austerity measures imposed by the country's creditors. Although yields on Greek bonds spiked and Greek banks saw their share prices tumble, there was little sign of contagion spreading to other periphery nations such as Portugal and Spain. Some compromise is likely, but a third debt renegotiation is ultimately inevitable if Greece is to remain in the euro and avoid an economic collapse. Either way, the systemic impact of such an event is now much lower than when the crisis first broke, as most banks and private sector institutions have reduced their exposure to minimal levels and most Greek debt is now held by governments well able to withstand a default.

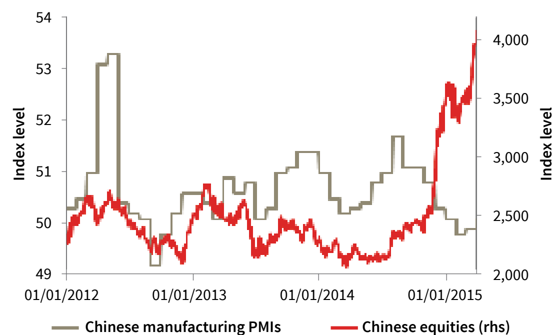
Figure 1: Periphery yields protected from Greek tensions

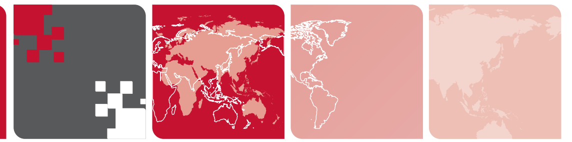


Across the Atlantic, economic data prints in the US continued to be mixed as fourth quarter GDP print for 2014 disappointed (2.2% versus initial estimates of 2.6%) and month-on-month retail sales fell by more than expected. It has been gains in payroll numbers that have dominated market sentiment, however, with upside surprises in January and February, but March delivered a sizeable disappointment with a reading of +126,000. In fact, the March print was the first time in 12 months that the payrolls number did not see growth of over 200,000 new jobs. As the dollar strengthens and jobs growth slows, an interest rate hike in the US is now not expected until September.

The slowdown in China remained an important theme in the first quarter. China's Purchasing Managers' Index (PMI) fell below 50 for the first time since September 2012, consistent with a contraction in factory activity. The indicator fell 0.3 points to 49.8 in January and rebounded to a mere 49.9 in February and 50.1 in March. Export numbers continued to disappoint in March, with a print of -14.6% year-on-year versus expectations for growth of 8.2%, while import numbers were also low at -12.3% versus forecasts of -11.3%. Furthermore, inflation in China remains subdued and the authorities are expected to continue easing following cuts to banks' Reserve Requirement Ratio and the official lending rate.

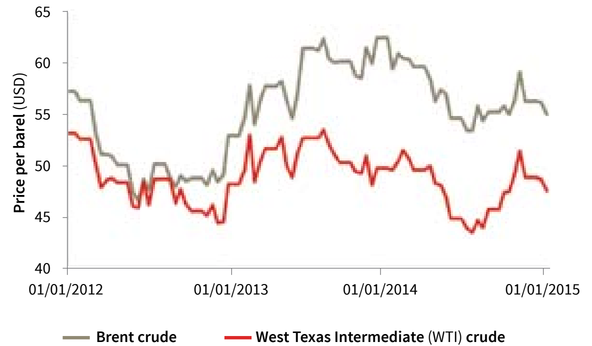
Figure 2: Chinese equity market boosted by easing expectations



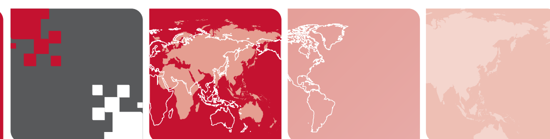


Finally, Brent crude gained a noteworthy 18.1% in February, its highest monthly gain for six years to bring the price of a barrel of Brent crude above $60. Supply by US shale producers has been scaled back at an incredible pace in 2015: according to Baker Hughes, there were 813 oil rigs operating in the US at the end of March, down from circa 1,600 in December last year. Despite this, inventories are filling up quickly as overall supply continues to increase, leaving less opportunity for those looking to buy and store oil. This has been seen in the US in particular, causing the price between WTI and Brent crude to widen recently. On the other hand, demand for oil is increasing steadily as the US economy improves and depressed prices boost demand.

Figure 3: Oil prices stabilise while WTI and Brent crude spread widens



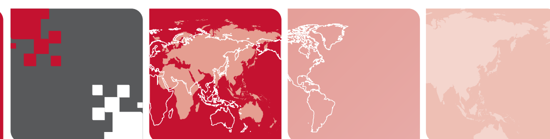
Source: Bloomberg, March 2015. Returns in US dollars unless otherwise stated.



7. Market Summary

Asset Class/Region	Index	To 31 March 2015		
		Currency	**Quarter**	**12 Months**
Developed markets equities				
United States	S&P 500 NR	**USD**	0.8%	12.0%
United Kingdom	MSCI UK NR	**GBP**	4.0%	6.1%
Continental Europe	MSCI Europe ex UK NR	**EUR**	18.9%	22.3%
Japan	Topix TR	**JPY**	10.5%	30.7%
Asia Pacific (ex Japan)	MSCI AC Asia Pacific ex Japan NR	**USD**	4.4%	6.3%
Global	MSCI World NR	**USD**	2.3%	6.0%
Emerging Market Equities				
Emerging Europe	MSCI EM Europe NR	**USD**	1.9%	-23.7%
Emerging Asia	MSCI EM Asia NR	**USD**	5.2%	10.7%
Emerging Latin America	MSCI EM Latin America NR	**USD**	-9.6%	-20.9%
BRICs	MSCI BRIC NR	**USD**	3.6%	3.6%
Global emerging markets	MSCI EM (Emerging Markets) NR	**USD**	2.2%	0.4%
Bonds				
US Treasuries	JP Morgan United States Government Bond Index TR	**USD**	1.8%	6.2%
US Treasuries (inflation protected)	Barclays Capital U.S. Government Inflation Linked TR	**USD**	1.5%	3.7%
US Corporate (investment grade)	Barclays Capital U.S. Corporate Investment Grade TR	**USD**	2.3%	6.8%
US High Yield	Barclays Capital U.S. High Yield 2% Issuer Cap TR	**USD**	2.5%	2.0%
UK Gilts	JP Morgan United Kingdom Government Bond Index TR	**GBP**	2.9%	14.7%
UK Corporate (investment grade)	BofA Merrill Lynch Sterling Non Gilts TR	**GBP**	3.3%	13.2%
Euro Government Bonds	Citigroup EMU GBI TR	**EUR**	4.3%	13.7%
Euro Corporate (investment grade)	Barclays Capital Euro Aggregate Corporate TR	**EUR**	1.4%	7.3%
Euro High Yield	Barclays European HY 3% Issuer Constraint Total Return Index Value	**EUR**	3.0%	5.7%
Japanese Government	JP Morgan Japan Government Bond Index TR	**JPY**	-0.5%	3.4%
Australian Government	JP Morgan Australia GBI TR	**AUD**	3.3%	13.5%
Global Government Bonds	JP Morgan Global GBI	**USD**	-1.8%	-3.7%
Global Bonds	Citigroup World Broad Investment Grade (WBIG) TR	**USD**	-2.2%	-3.8%
Global Convertible Bonds	UBS Global Focus Convertible Bond	**USD**	0.5%	-4.2%
Emerging Market Bonds	JP Morgan EMBI+ (Hard currency)	**USD**	1.9%	4.5%

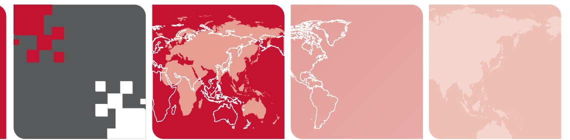
Source: Bloomberg, December 2014.



Asset Class/Region	Index	To 31 December 2014		
		Currency	Quarter	12 Months
Property				
US Property Securities	MSCI US REIT NR	**USD**	4.5%	22.7%
Australian Property Securities	S&P/ASX 200 A-REIT Index TR	**AUD**	8.4%	28.0%
Asia Property Securities	S&P Asia Property 40 Index NR	**USD**	5.5%	11.9%
Global Property Securities	S&P Global Property USD TR	**USD**	4.5%	14.7%
Currencies				
Euro		**USD**	-11.3%	-22.1%
UK Pound Sterling		**USD**	-4.9%	-11.1%
Japanese Yen		**USD**	0.0%	-14.4%
Australian Dollar		**USD**	-6.9%	-17.9%
South African Rand		**USD**	-4.6%	-13.2%
Commodities & Alternatives				
Commodities	RICI TR	**USD**	-7.2%	-31.2%
Agricultural Commodities	RICI Agriculture TR	**USD**	-8.0%	-23.8%
Oil	ICE Crude Oil CR	**USD**	-3.9%	-48.9%
Gold	Gold Spot	**USD**	-0.1%	-7.8%
Hedge funds	HFRX Global Hedge Fund	**USD**	2.1%	0.4%
Hedge funds	Dow Jones Credit Suisse Hedge Fund USD	**USD**	2.5%	5.7%

** Estimate*

Source: Bloomberg, December 2014.



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Under our multi-management arrangements, we selectively appoint underlying sub-investment managers and funds to actively manage underlying asset holdings in the pursuit of achieving mandated performance objectives. Annual investment management fees are payable both to the multimanager and the manager of the underlying assets at rates contained in the offering documents of the relevant portfolios (and may involve performance fees where expressly indicated therein).

Momentum Global Investment Management (Company Registration No. 3733094) has its registered office at 62 Queen Street, London, EC4R 1EB.

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