HARMONY FUNDS
Multi Manager, Multi Asset Class Solutions

momentum

Harmony Portfolios

quarter ended 31 March 2017

Q1

global investment management

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1. Portfolio objectives and overview

The Harmony Portfolio range

The Harmony Portfolios are a long established range of globally diversified, multi-asset funds designed specifically to provide a cornerstone investment. The Harmony range consists of eight portfolios, each risk profiled and with a specific geographical and currency focus, housed in a Luxembourg UCITS structure with daily pricing and daily liquidity.

The full range includes:

-- Momentum Harmony Asian Balanced
-- Momentum Harmony Asian Growth
-- Momentum Harmony Australian Dollar Growth
-- Momentum Harmony Europe Diversified
-- Momentum Harmony Sterling Balanced
-- Momentum Harmony Sterling Growth
-- Momentum Harmony US Dollar Balanced
-- Momentum Harmony US Dollar Growth

As at the end of January 2017, assets under management across the eight Harmony Portfolios totalled over USD 500 million.

The Harmony Portfolios investment philosophy is built on three core capabilities:

-- Asset allocation
-- Investment selection
-- Portfolio construction

The asset allocation process is disciplined, robust and valuation driven, and builds portfolios with true diversification across a wide range of non-correlated assets. 'Best of breed' fund solutions are then used to construct each portfolio. We recognise that no investment house has a monopoly of skill in all disciplines: having an unconstrained choice allows us to choose the most appropriate investment managers for any particular asset class. We are objective and independent in our approach, with no incentive to utilise a specific provider in the underlying composition of the portfolios.

The Harmony Portfolios aim to create the best combination of investments to provide optimal returns relative to each of the eight mandates' tolerance for risk.

The Investment Manager

The Portfolios are managed in London by a team of experienced investment professionals at Momentum Global Investment Management (MGIM), which has been offering investment management and advisory services to institutional and retail investors since 1998. The fourteen strong multi-asset investment team have been responsible for the investment strategy and management of the Portfolios since their nception in 2004. Senior members of the investment team have been working together throughout most of this period.

Investors can be confident that their investments are being managed within a strictly regulated environment, and by a highly qualified and experienced team with significant resources across the globe. MGIM is wholly owned by MMI Holdings in South Africa, a listed company with a market capitalisation of $3.3bn and a strong capital position with total assets of $54bn. MGIM is 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).

2. Portfolio commentary

Portfolio Performance

The Momentum Harmony range delivered strong returns in the first quarter of 2017, with all funds rising by 3% or more over the period, net of fees in their respective base currencies. Over twelve months the funds have delivered returns of between 7.1% and 16.9%.

The general backdrop over the first quarter was one of outperformance from global developed market equities (+5.4% in local currency terms) and emerging market equities (+7.8%) relative to global bonds (+0.4%). The US dollar weakened against most major currencies over the quarter, meaning global index returns were higher when measured in US dollar terms.

The Harmony Asian Growth and Asian Balanced funds delivered the strongest returns during the first quarter, up by 8.2% and 6.4% in US dollar terms. This reflected the strong performance of Asian equities, which outperformed the broader global emerging markets index, and also strength in Asian currencies versus the US dollar. Also, manager selection contributed to performance across both funds, driven in particular by the Third Avenue Real Estate fund and also the three liquid alternatives holdings.

The US Dollar Growth and US Dollar Balanced funds delivered the next best returns, gaining 6.0% and 4.6% over the period. Both our asset allocation and manager selection decisions added significantly to performance. Within fixed income allocations to convertible bonds and emerging market debt delivered strong returns, particularly when viewed relative to the modest gain delivered by government bonds. The 4% allocation to gold also added value with a 7.4% return over three months. In terms of manager selection, the holdings in growth orientated strategies managed by Wells and Jennison both outperformed by over 5% relative to their respective US and global equity benchmarks.

The other funds in the range, across Sterling, euro and Australian Dollar currency bases returned between 3.0% and 4.2% in their respective currencies. Both our active asset allocation and manager selection positions were accretive to performance across these funds. The specific drivers of positive asset allocation attribution were similar to those for the Asian and US Dollar funds, while there were several common drivers within equity manager selection as well. Notable contributors unique to just these funds included Lindsell Train and Evenlode in the Sterling portfolios, both returning nearly 7.0% relative to a 3.8% gain for UK equities, and the Prusik Asian Income fund in the Australian Dollar portfolio, which returned 14.8% in US dollar terms.

Portfolio Changes

During January we made two changes to asset allocation policy across the fund range. We reduced the target for the overall equity allocation by 1.5%-3.0% in response to the strength in most markets which led to further increases in valuation multiples. We have reduced equity allocations in small increments over the past year as markets have recovered from the recent trough in early 2016, at which point we had substantially higher equity and credit allocations. Another small change during January was the addition of a 1.5%-2.5% holding in US Treasury Inflation-Protected Securities (TIPS), purchased via three bonds with different maturities. This is the first direct exposure the funds have had to the US government bond market in several years. Government bond yields rose sharply prior to these purchases, due to a change in market expectations for future monetary policy across key central banks globally spurred by higher inflation expectations. By buying TIPS as opposed to nominal government bonds, our positions are protected from further rises in inflation expectations. Overall we continue to view most government bond markets as overvalued, which is reflected in the modest sizing of this new position, but we believe some exposure is warranted at these yield levels on the basis of the diversification benefits that bonds bring to the fund, especially given the increase in equity valuations in recent years. Although most market participants have rapidly turned their attention to worrying about inflation risks, the deflationary forces that have driven the multi-decade bull market in bonds have not disappeared overnight.

A further change was made across all the funds in March, to underlying manager selection. Within the global equity allocation we switched from the American Century Global Concentrated Growth fund to the Jennison Global Equity Opportunities fund. We were invested with American Century for over three years and continue to rate their capabilities very highly but believe the Jennison strategy has better

return potential over the long term and better complements other holdings in the portfolio. The Jennison Global Equity Opportunities fund is managed by Mark Baribeau who has invested with the same approach since 2004 and has been supported by several of the same experienced team members for many years. The team implement an aggressive growth investment approach, focusing on stocks that display high and accelerating earnings growth. The consistent style exposure their approach provides is typically complementary to more value orientated investment styles, with outperformance from aggressive growth and value styles usually being delivered in different market environments. At present top holdings include the likes of Amazon.com, Facebook and Mastercard.

Looking Forward

Markets have performed well this year and have risen sharply since the US election. The evidence of higher growth has been encouraging and many of President Trump's policies are market friendly. However, we are now at the stage where the detail of policy will begin to be scrutinised and we will be able to gauge the extent to which it will be successfully implemented. With valuations high, the market is vulnerable to a correction, and the subdued volatility that we have enjoyed over the past few months will surely be tested before too long. This cycle is particularly long, however, and it will be important to stay invested; anything less is likely to lead to disappointment. Opportunities for returns outweigh the risks and we expect equities to continue to outperform bonds through 2017, notwithstanding periodic bouts of weakness.

Within equities we continue to favour Europe, Japan and emerging markets, whereas we believe there is less scope for continued outperformance by the US stock market. Fixed income exposure is mostly focused in corporate credit, convertible bonds and hard currency emerging market bonds, with very little exposure to government bonds. Around this core allocation to equities and bonds, we retain positions in listed real estate, listed infrastructure, gold and a diversified basket of liquid alternatives strategies that are uncorrelated to equity and bond markets.

Source: Bloomberg / Morningstar. Returns in US dollars unless otherwise stated, March 2017. Past performance is not indicative of future returns.

3. Recent portfolio activity and positioning

The table below shows the portfolio activity throughout the quarter.

Date	Holding initiated/ *Increased*	Holding sold/ *Decreased*	Harmony funds
November	**ETFS Physical Gold**	*Cash / Muzinich Enhanced Yield*	All
	F&C Equity Market Neutral / GSAM Strategic Bond	*Cash / Muzinich Enhanced Yield*	All
	Muzinich Emerging Markets Corporate Bond	*iShares $ Emerging Markets Bond / Axa IM US High Yield*	Asian & Balanced / Diversified funds
December	*iShares JPM $ Emerging Markets Bond*	**Axa US High Yield** */ Axa US Short Duration/ Muzinich Emerging Markets Short Duration/ Blackrock US Corporate Bond*	All
	Amundi JPX Nikkei 400	*Artisan Global Value/FP Crux European Special Situations/Cash*	All but Asian
	Polar Capital Japan Fund (ccy unhedged)	**Polar Capital Japan Fund (ccy hedged)**	Asian
	Sands Emerging Markets	*Dimensional Emerging Markets Value*	All but Asian
January	**US Treasury Inflation Protected Securities (TIPS)**	*European / Global Equity holdings*	All
	Blackrock US Corporate Bond	*Blackrock UK Corporate Bond*	Sterling funds
March	**Jennison Global Equity Opportunities**	**American Century Concentrated Global Growth**	All but US Dollar
	Jennison Global Equity Opportunities	**American Century Concentrated Global Growth**	US Dollar funds

Asset allocation decision	Manager selection decision

4. Target portfolios

	Balanced	Diversified	Growth
Equities	37.5%	50.5%	61.0%
Fixed Income	39.5%	26.75%	16.0%
Property / Infrastructure	9.5%	9.5%	9.5%
Alternatives	6.0%	6.0%	4.5%
Commodities	4.5%	4.5%	4.5%
Cash	3.0%	2.75%	4.5%
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. Target weights are based on the USD Balanced, Europe Diversified and USD Growth funds respectively. Allocation may vary for the other Balanced and Growth funds in the range.

5. Fund and peer group performance

	Performance to 31 March 2017						
Fund returns (local currency)	3 months	6 months	2016	2015	2014	2013	3 years (annualised)
Asian Balanced (US dollars)	6.4%	2.1%	2.9%	-4.3%	0.7%	2.5%	1.7%
Peer group median	4.7%	-0.9%	-1.3%	-9.1%	-4.5%	7.4%	-3.7%
Asian Growth (US dollars)	8.2%	4.0%	3.8%	-4.3%	0.7%	2.5%	3.1%
Peer group median	5.6%	0.0%	-0.8%	-9.1%	-4.5%	7.4%	-2.7%
Global equities	6.9%	8.2%	7.9%	-2.4%	4.2%	22.8%	5.1%
MSCI AC Asia Pacific ex Japan	12.8%	7.3%	6.8%	-9.4%	2.8%	3.4%	3.6%
AUD Growth	3.2%	5.5%	6.9%	2.3%	6.0%	17.1%	6.1%
Peer group median	0.7%	2.6%	4.4%	3.8%	5.7%	17.3%	5.0%
Global equities	1.6%	8.8%	9.0%	10.4%	14.5%	43.2%	12.7%
ASX All Ordinaries	4.5%	9.1%	11.6%	3.8%	5.0%	19.7%	7.6%
Europe Diversified	4.2%	6.5%	3.1%	5.8%	6.0%	7.8%	6.1%
Peer group median	2.0%	3.8%	1.6%	2.4%	5.2%	4.8%	3.2%
Global equities	5.4%	13.7%	11.1%	8.8%	18.6%	17.5%	14.3%
MSCI Europe ex UK	6.9%	13.7%	2.4%	10.7%	6.4%	22.1%	7.6%
GBP Balanced	3.0%	4.3%	14.1%	0.2%	3.2%	10.6%	6.6%
Peer group median	2.7%	4.0%	12.5%	-0.4%	3.1%	9.9%	5.8%
GBP Growth	3.6%	5.6%	16.9%	0.0%	4.1%	16.9%	7.9%
Peer group median	2.8%	4.3%	12.7%	-0.4%	3.0%	10.3%	6.2%
Global equities	5.6%	12.4%	28.7%	3.3%	10.6%	20.5%	15.6%
MSCI UK	3.8%	8.1%	19.2%	-2.2%	0.5%	18.5%	7.3%
USD Balanced	4.6%	3.6%	5.2%	-4.6%	2.0%	10.6%	2.3%
Peer group median	3.6%	1.8%	3.6%	-4.4%	0.7%	11.2%	0.6%
USD Growth	6.0%	5.3%	5.5%	-6.2%	4.1%	17.6%	3.0%
Peer group median	3.9%	2.5%	3.9%	-4.6%	0.9%	13.3%	0.8%
Global equities	6.9%	8.2%	7.9%	-2.4%	4.2%	22.8%	5.1%
S&P 500	5.9%	9.8%	11.2%	0.8%	13.7%	32.4%	9.7%

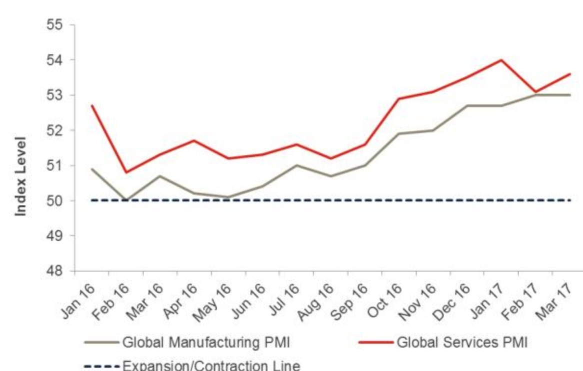
Source: Bloomberg, March 2017. Past performance is not indicative of future returns.

6. Market commentary

The inauguration of President Trump in January proved to mark the start of a remarkably benign period for markets, with most risk assets making solid upward progress, continuing the pattern of performance since Trump's election success. Volatility remained low, with equities and credit materially outperforming sovereign bonds.

The key fundamental factor underpinning markets both this month and throughout the first quarter has been the clear and continuing evidence of improving global growth, best illustrated by strong PMIs (Purchasing Managers' Indices) from almost all countries, as well as rising trends in consumption. This has provided a good environment for corporate profits, with US earnings rising by close to 10% in Q1, which has in turn underpinned risk assets, particularly equities, as well as high yield bonds and emerging market debt. It also gave investors the confidence to absorb the US Federal Reserve's (Fed's) second rate rise since the financial crisis of 2008-9 without concerns, despite the fact that this move had been largely unexpected until very recently, when the weight of economic evidence and the continuing strength of the labour market caused the Fed to bring forward the timing of its move. Importantly, however, the Fed left the predicted pace of policy tightening unchanged, a factor which provided support to markets. Against this background, developed world equities returned 6.4% in USD terms in the first quarter of the year, with most regions participating, while emerging markets returned 11.4%.

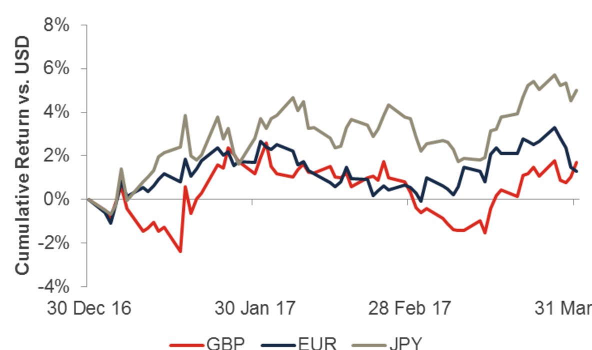
Figure 1: PMIs indicate upwards trending global growth



Offsetting the rising confidence, and the 'Trump reflation trade' in the US, was the first meaningful setback to the President's bold campaign commitments. The attempt to overturn so-called 'Obamacare' failed in Congress, being unable to garner a necessary level of support despite the Republican majority in both Houses. While the policy itself was not considered particularly important to the general investor, it raised serious concerns that Trump would find it arduous to pass and implement the key tax reforms that investors have been hoping for, and thereby defer any boost to growth that these reforms would be expected to deliver.

Perhaps the biggest surprises of Q1 were the fall in bond yields in the US and UK and weakness in the US dollar, despite the Fed progressing down the path of policy normalisation while the other major central banks of Europe, Japan and the UK all remain committed to ultra-loose policy. Although interest rate differentials between the USD and other developed world currencies are at historic highs, investors have recognised the policy tightening already implicit in the strong dollar of the past two and a half years; at the same time, the rising trend in economic activity and pick up in headline inflation especially in Europe has led to increasing discussion in the ECB about the end of ultra-loose policy. Over the quarter, the USD trade weighted index fell by 1.9%. The yen was particularly strong (up 4.8%) and was a major factor in the Japanese stock market stagnating in local currency terms, returning -0.2% in the last three months.

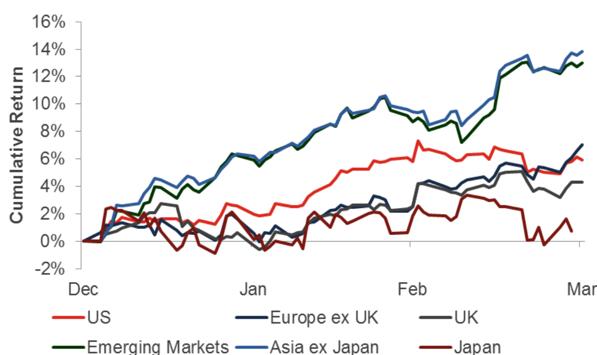
Figure 2: Downward pressure on the dollar benefits major developed currencies



Although the US stock market has led global markets by a very substantial margin in recent years there have been encouraging signs that non-US economies and stock markets are beginning to perform relatively better. Economic data has generally surprised on the upside, especially in Europe, which was the best performing region within developed market equities, helped also by fading political fears, as the far right anti-immigration party in the Netherlands failed to

make sufficient progress in the general election to disturb the current centre parties' coalition government, and as support for Marine le Pen in France's Presidential election appeared to have peaked.

Figure 3: Asia, EM, and European equities outperform in Q1



In commodities, the biggest impact on markets came from the fall in the oil price; it declined by 7.0% in the quarter to reach USD 52.83 per barrel, despite OPEC production cuts kicking in. To date the cuts have failed to dent the very high levels of inventories, whereas the rise in the oil price from last year's lows has led to a renewed surge in shale production in the US, where production costs have been brought down dramatically in response to the earlier collapse in prices. Without further OPEC production cuts or an extension of the current programme of cuts, it will be very difficult for the oil price to break out of its current range, and this will provide support both to relatively low levels of global inflation and to economic growth.

Elsewhere, the UK triggered a very difficult two-year period of negotiations with the EU to determine the conditions of its departure from the bloc in March 2019 by invoking Article 50. Markets took this well-flagged move in their stride and the UK economy continues to perform well above the levels expected by most economists before the referendum. However, uncertainty levels are high and UK markets are vulnerable to the ebbs and tides of the negotiations, at least until the broad nature of the UK's exit terms, and crucially its future trading relationship with the EU, are clearer. For now sterling has been steady against both the USD and EUR so far in 2017. It is a fundamentally undervalued currency after its sharp post referendum falls, but upside is likely to be capped by the uncertainty ahead.

Markets have performed well this year, and have risen sharply since the US election. The evidence of higher growth has been encouraging and many of Trump's policies are market friendly. However, we are now at the stage where the detail of policy will begin to be scrutinised and we will be able to gauge the extent to which it will be successfully implemented. In general then, policy uncertainties remain high. And with valuations high, the market is vulnerable to a correction, and the long period of subdued volatility that we have enjoyed over the past few months will surely be tested before too long.

This cycle is particularly long, however, and it will be important to stay invested; anything less is likely to lead to disappointment. Opportunities for returns outweigh the risks, and we expect equities to continue to outperform bonds through 2017. Indeed, periodic bouts of weakness in equity markets will present buying opportunities.

Source: Bloomberg, March 2017. Returns in US dollars unless otherwise stated.

7. Market performance

Asset class/region	Index	Currency	Quarter	12 months
		To 31 March 2017		
Developed markets equities				
United States	S&P 500 NR	USD	5.9%	16.4%
United Kingdom	MSCI UK NR	GBP	3.8%	23.5%
Continental Europe	MSCI Europe ex UK NR	EUR	6.9%	17.9%
Japan	Topix TR	JPY	0.6%	14.7%
Asia Pacific (ex Japan)	MSCI AC Asia Pacific ex Japan NR	USD	12.8%	18.2%
Global	MSCI World NR	USD	6.4%	14.8%
Emerging markets equities				
Emerging Europe	MSCI EM Europe NR	USD	1.4%	11.3%
Emerging Asia	MSCI EM Asia NR	USD	13.4%	18.0%
Emerging Latin America	MSCI EM Latin America NR	USD	12.1%	23.3%
BRICs	MSCI BRIC NR	USD	11.6%	23.4%
Global emerging markets	MSCI EM (Emerging Markets) NR	USD	11.4%	17.2%
Bonds				
US Treasuries	JP Morgan United States Government Bond Index TR	USD	0.7%	-1.5%
US Treasuries (inflation protected)	Barclays Capital U.S. Government Inflation Linked TR	USD	1.4%	1.5%
US Corporate (investment grade)	Barclays Capital U.S. Corporate Investment Grade TR	USD	1.2%	3.3%
US High Yield	Barclays Capital U.S. High Yield 2% Issuer Cap TR	USD	2.7%	16.4%
UK Gilts	JP Morgan United Kingdom Government Bond Index TR	GBP	1.6%	6.9%
UK Corporate (investment grade)	BofA Merrill Lynch Sterling Non Gilts TR	GBP	1.8%	9.3%
Euro Government Bonds	Citigroup EMU GBI TR	EUR	-1.5%	-1.7%
Euro Corporate (investment grade)	Barclays Capital Euro Aggregate Corporate TR	EUR	0.3%	2.5%
Euro High Yield	Barclays European HY 3% Issuer Constraint Total Return Index Value Unhedged EUR	EUR	1.8%	9.0%
Japanese Government	JP Morgan Japan Government Bond Index TR	JPY	-0.5%	-1.4%
Australian Government	JP Morgan Australia GBI TR	AUD	1.3%	1.4%
Global Government Bonds	JP Morgan Global GBI	USD	1.4%	-3.5%
Global Bonds	Citigroup World Broad Investment Grade (WBIG) TR	USD	1.3%	-2.3%
Global Convertible Bonds	UBS Global Focus Convertible Bond	USD	3.8%	4.2%
Emerging Market Bonds	JP Morgan EMBI+ (Hard currency)	USD	3.8%	7.4%

Source: Bloomberg. March 2017.

		To 31 March 2017		
Asset class/region	Index	Currency	Quarter	12 months
Property				
US Property Securities	MSCI US REIT NR	USD	0.7%	1.9%
Australian Property Securities	S&P/ASX 200 A-REIT Index TR	AUD	-1.1%	1.3%
Asia Property Securities	S&P Asia Property 40 Index NR	USD	9.1%	10.3%
Global Property Securities	S&P Global Property USD TR	USD	3.7%	3.5%
Currencies				
Euro		USD	1.7%	-6.0%
UK Pound Sterling		USD	1.5%	-12.7%
Japanese Yen		USD	5.1%	1.1%
Australian Dollar		USD	6.2%	-0.1%
South African Rand		USD	2.1%	10.1%
Commodities				
Oil	ICE Crude Oil CR	USD	-7.0%	33.4%
Gold	Gold Spot	USD	8.5%	1.4%

Source: Bloomberg. March 2017.

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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).

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