HARMONY FUNDS
Multi Manager, Multi Asset Class Solutions

momentum

Harmony Portfolios

Quarterly Report

31 December 2013

Q4

Momentum Global Investment Management Limited (Company Registration No. 3733094) registered office at 20 Gracechurch Street, London EC3V 0BG.

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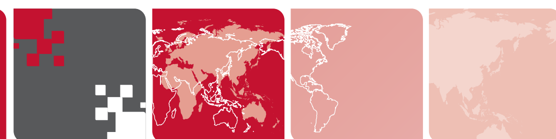
1. Portfolio Objectives & Overview

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, Euro Balanced, 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 the Momentum Group, which is in turn a wholly owned subsidiary of 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

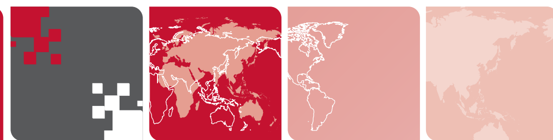
We have been active with the equity allocation of the Harmony Funds throughout the year and in the final quarter of the year we maintained a neutral allocation to global equity which had been adopted in the third quarter. As of today global equity markets appear approximately 'fair value' to the managers and hence a neutral position is appropriate. The Funds are moderately overweight to global emerging markets equity as these markets are priced at a level that we believes justifies accepting the additional volatility inherent in these markets.

As has been the case for the entirety of the year, in the fourth quarter, the Funds remained underweight to government fixed income securities. This is because on a long term view we do not see compelling valuations available in this area of the fixed income markets. Indeed, barring significant global shocks the upside from sovereign debt is anticipated to be muted, making the risk-return trade-off unattractive in anything but a significant 'double dip' scenario. In the event of a more moderate outcome, including gentle global GDP growth in coming years, we expect government securities to underperform. Consequently, the Funds are positioned for a low but positive growth environment, and under these conditions the underweight to government debt is expected to benefit performance through the cycle. The fixed income allocation of the Funds largely comprises investment grade, high yield, convertible, floating rate loan and strategic credit allocations. In the final quarter of the year an allocation was made to hard currency denominated emerging markets debt as these securities have sold off through the middle of the year and are now at an attractive valuation level.

Going forward, with uncertainty remaining over the strength of developed and developing world economic growth combined with the potential for tightening credit conditions, investors should look to retain a prudent level of diversification in their portfolios. Overall, we believe that the Funds are well positioned to take advantage of future opportunities in the markets as they present themselves. The past year was notable for its low levels of volatility in the markets. We do not believe this to be sustainable over the longer term and as a consequence we expect volatility to increase. It is important to bear in mind that while occasionally uncomfortable, volatility provides valuation opportunities for disciplined investors and our overweight to cash provides a ready source of liquidity which can be invested in opportunities as and when they arise.

From a manager selection perspective, in our US dollar Funds the US equity managers struggled to keep up with the sharply rising market in the fourth quarter as the S&P 500 index gained 10.3% in US dollar terms. In comparison to this the Fund holdings managed by; Harris, Wells and Yacktman, returned 9.1%, 7.6% and 6.6% respectively. Nonetheless, over the full year these Funds have on the whole performed very well in relative terms despite the market rising by over 30%. Both Wells and Harris returned over 30% as their respective value and growth investment styles were both rewarded over the period. Yacktman underperformed for the year with a return of 25.9% although this was to be expected somewhat; the manager's quality biased approach is inherently conservative and so is likely to lag in such sharply rising markets and their higher than average cash holdings has also been a drag on returns. Across the suite of portfolios, the holding in the Cohen & Steers Global Real Estate Securities fund performed well versus its benchmark during the fourth quarter and over the course of 2013, with returns of -0.1% and 4.3% representing net of fees outperformance of 0.7% and 0.6% respectively. Since late 2012 the portfolio has held a reduced allocation to this asset class in favour of a listed infrastructure equity strategy managed by First State. This positioning benefited performance over the year as the First State strategy outperformed Cohen & Steers by 14.0%. Listed property, as measured by the S&P Global Property index, underperformed the MSCI World index significantly in 2013 with respective returns of 3.7% and 26.7% respectively.

Source: Bloomberg / Morningstar. Returns in US dollars unless otherwise stated, December 2013. 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:

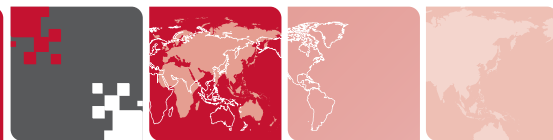
- We elected to add a position (3% in balanced funds, 2% in growth funds) in hard currency (US dollar denominated) emerging market debt, on valuation grounds. This position was funded from cash and short term money market securities.

- **Increased**
  - Secured loans
  - Tactical position added in hard currency emerging market debt

- **Decreased**
  - Cash

Manager changes during the quarter:

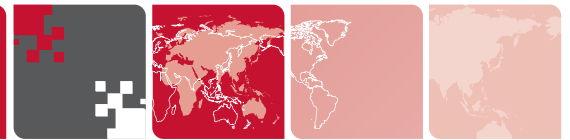
- During the past quarter we reduced our position in the Momentum IF Global Equity fund.



4. Target Portfolios

	Balanced	Growth
Equities	43.0%	68.0%
Fixed Income	40.0%	20.0%
Property	7.0%	7.0%
Cash	10.0%	5.0%
Total	**100.0%**	**100.0%**

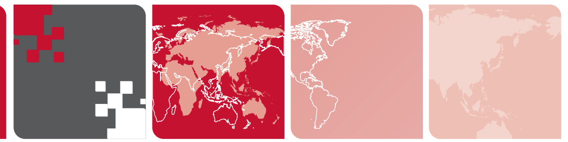
These target weights are correct as at the time this report is published and are indicative of the managers' medium term outlook for markets, which is driven principally by their assessment of relative valuation opportunities. The property exposure includes exposure to listed infrastructure.



5. Fund and Index Performance

Fund returns (local currency)	Performance to 31 December 2013			
	3 months	6 months	2013	3 Years (annualised)
Asian Balanced (US dollars)	0.9%	4.0%	2.5%	1.1%
Asian Growth (US dollars)	1.7%	6.6%	6.2%	3.0%
Peer group median	3.4%	8.9%	7.4%	3.3%
Global equities	7.3%	15.8%	22.8%	9.9%
MSCI AC Asia Pacific ex Japan	2.3%	9.8%	3.4%	1.9%
AUD Growth	4.3%	9.2%	17.1%	7.2%
Peer group median	4.4%	8.6%	17.3%	7.3%
Global equities	12.3%	18.7%	43.2%	15.5%
ASX All Ordinaries	3.4%	14.6%	19.7%	8.0%
EUR Balanced	1.7%	4.2%	7.8%	4.2%
Peer group median	2.1%	4.6%	4.8%	2.6%
Global equities	5.4%	9.2%	17.5%	8.9%
MSCI Europe ex UK	6.2%	16.7%	22.1%	8.5%
GBP Balanced	2.2%	3.3%	10.6%	4.8%
GBP Growth	3.7%	5.8%	16.9%	7.1%
Peer group median	2.6%	4.4%	10.3%	4.4%
Global equities	4.9%	6.0%	20.5%	7.8%
MSCI UK	5.0%	10.2%	18.5%	8.1%
USD Balanced	2.7%	6.4%	10.6%	5.4%
USD Growth	4.3%	9.4%	17.6%	8.8%
Peer group median	4.8%	10.1%	13.3%	6.9%
Global equities	7.3%	15.8%	22.8%	9.9%
S&P 500	10.5%	16.3%	32.4%	16.2%

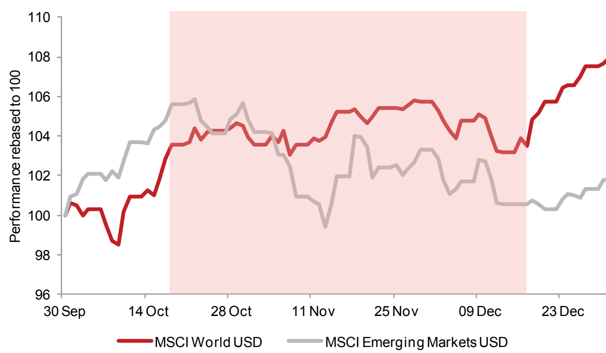
Source: Bloomberg, December 2013. Past performance is not indicative of future returns.



6. Market Commentary

The final quarter of 2013 was dominated by speculation about the timing and extent of any reduction in the Federal Reserve's asset purchase programme. Equity markets drifted sideways between mid October and the 17th of December, before staging a late rally into year end, after the Fed announced its decision to begin tapering its asset purchase programme from January.

Figure 1: Path of developed market and EM equities in Q4



The net effect of this was that equities in developed markets enjoyed another strong quarter, to round off their best year since 2009 in US dollar terms. The MSCI World index added 8.0% between October and December, to bring its 2013 return to 26.7%, led by the US (+10.3%), Japan (+9.2% in yen terms) and Continental Europe (+6.2% in euro terms). Meanwhile Asia Pacific excluding Japan was the big underperformer, with returns of 0.3% in the final quarter. Emerging markets posted gains, albeit someway behind their developed counterparts as has been the case throughout 2013, but returns of 1.8% were insufficient to bring EM into positive territory for the year.

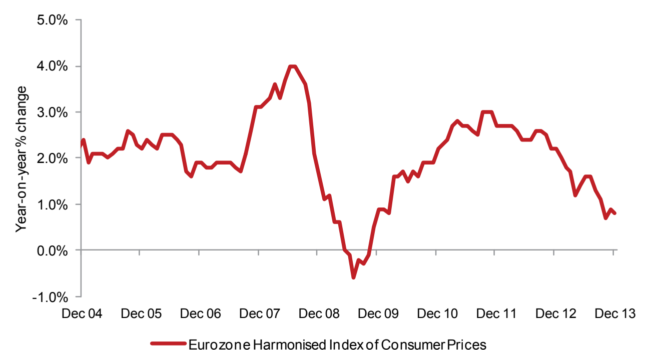
Global government bonds lost a further 1.3% in the fourth quarter, to finish the year down by 4.5%. Once again, credit and high yield outperformed, as investors sought higher yielding areas of the fixed income markets. Global property securities lagged the broader equity market with a return of 0.8%, rounding off a disappointing year for the asset class following its strong performance between 2009 and 2012. Commodities lost 1.3%, as continued slow global growth weighed on demand, whilst gold slumped by 9.3% to finish the year down by 28.0% – its worst calendar year since 1981.

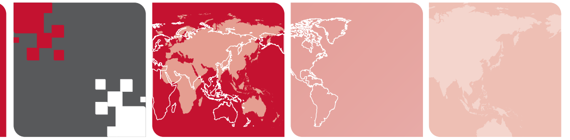
The US government shutdown at the start of October caused equity markets to sell-off. Markets rallied however, as confidence grew that a deal would be struck to raise the debt ceiling, and the Republican and Democrat parties dually agreed a last minute deal on 17 October. As a result, October was another strong month across nearly all asset classes except – once again – commodities. The MSCI World developed markets index returned 3.9% over the month, with the US +4.6%, Europe +4.2% (EUR) and the UK +4.3% (GBP). Bond markets, nervous during the debt ceiling talks, recovered and also produced good returns for the month, with US Treasury bonds +0.6% and the global government bond index +0.9%.

Markets subsequently moved sideways in November, after stronger than expected data from the US economy raised fears that tapering may begin the following month. The private sector added 204,000 new jobs in October, above market expectations and despite the negative impact caused by the US government shutdown. Third quarter GDP numbers surprised on the upside, with a preliminary growth estimate of 2.8% versus 2% expected, later revised up to 4.1%. Despite the insistence of Fed Chair Janet Yellen that the economy was still performing far below potential, investors began to bring forward their expectations for the start of tapering. This pushed interest rates on bonds higher (US 10 year Treasury yields +0.2%) and led to sharp falls in markets at most risk from reduced global liquidity, notably emerging markets (EM) equities (-1.5%) and gold (-5.3%).

The European Central Bank surprised markets by cutting interest rates to 0.25% in November, signalling its growing concerns over deflationary forces at work in the eurozone. This decision came shortly after the release of inflation numbers, which showed a dramatic fall to 0.7% year-on-year, with some big economies seeing aggregate price levels falling. GDP numbers for Q3 also disappointed, with growth of only 0.1%, whilst France and Italy saw output contract. In contrast the UK, not shackled by a fixed currency regime and with a considerably more flexible economy that those across Europe, showed signs of a more sustainable recovery and higher growth.

Figure 2: The ECB continues to battle low inflation in the eurozone



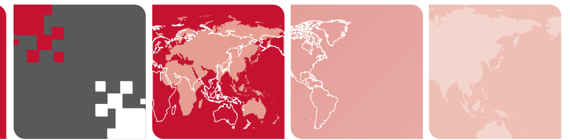


Markets remained subdued ahead of the Fed's meeting on the 18th of December, before staging a strong rally into year end, with the central bank announcing its decision to start tapering quantitative easing based on its assessment of the strength of the US economy. After several months of speculation, the central bank announced it would scale back its USD 85 billion a month of asset purchases by USD 10 billion a month, with USD 5 billion coming from both US treasury purchases and mortgage backed securities.

Reflecting on the year as a whole, the big story for investors was the outperformance of leading DM equity markets versus EM equities and safe haven government bonds, both of which suffered negative returns over the year (MSCI World +26.7%; MSCI EM -2.6%; government bonds -4.5%). In general we have had favourable conditions for equities in the past year: monetary policy has been exceptionally loose and accommodating in all the big developed markets, credit conditions have eased especially in the US and the UK and to a lesser extent in Japan, inflation has been subdued, economies have been sluggish but recovering as the year progressed, and corporate profitability has been very good with profit margins at historically high levels.

Given a continuation of today's steady – albeit relatively slow – economic recovery, the environment for the corporate sector remains good. However, we do not expect a repeat of 2013's returns in developed markets; equity prices have moved ahead of underlying earnings and although valuations are not yet stretched they are no longer as compelling as they were.

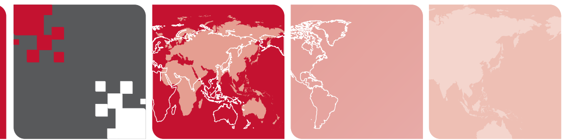
Source: Bloomberg.
Returns in US dollars unless otherwise stated. December 2013.



7. Market Summary

		To 31 December 2013		
Asset Class/Region	**Index**	**Currency**	**Quarter**	**12 Months**
Developed markets equities				
United States	S&P 500 NR	**USD**	10.3%	31.5%
United Kingdom	MSCI UK NR	**GBP**	5.0%	18.4%
Continental Europe	MSCI Europe ex UK NR	**EUR**	6.2%	22.1%
Japan	Topix TR	**JPY**	9.2%*	54.4%*
Asia Pacific (ex Japan)	MSCI Pacific ex Japan TR	**USD**	0.3%	5.6%
Global	MSCI World NR	**USD**	8.0%	26.7%
Emerging Market Equities				
Emerging Europe	MSCI EM Europe NR	**USD**	-1.6%	-4.5%
Emerging Asia	MSCI EM Asia NR	**USD**	3.7%	2.0%
Emerging Latin America	MSCI EM Latin America NR	**USD**	-2.3%	-13.4%
BRICs	MSCI BRIC NR	**USD**	1.7%	-3.5%
Global emerging markets	MSCI EM (Emerging Markets) NR	**USD**	1.8%	-2.6%
Bonds				
US Treasuries	JP Morgan United States Government Bond Index TR	**USD**	-0.9%	-3.4%
US Treasuries (inflation protected)	Barclays Capital U.S. Government Inflation Linked TR	**USD**	-2.2%	-9.3%
US Corporate (investment grade)	Barclays Capital U.S. Corporate Investment Grade TR	**USD**	1.1%	-1.5%
US High Yield	Barclays Capital U.S. High Yield 2% Issuer Cap TR	**USD**	3.6%	7.4%
UK Gilts	JP Morgan United Kingdom Government Bond Index TR	**GBP**	-1.5%	-4.2%
UK Corporate (investment grade)	BofA Merrill Lynch Sterling Non Gilts TR	**GBP**	-0.1%	0.8%
Euro Government Bonds	Citigroup EMU GBI TR	**EUR**	1.1%	2.2%
Euro Corporate (investment grade)	Barclays Capital Euro Aggregate Corporate TR	**EUR**	1.0%	2.4%
Euro High Yield	BofA Merrill Lynch Euro High Yield Constrained TR	**EUR**	5.8%	15.0%
Japanese Government	JP Morgan Japan Government Bond Index TR	**JPY**	0.2%	2.2%
Australian Government	JP Morgan Australia GBI TR	**AUD**	-0.3%	0.0%
Global Government Bonds	JP Morgan Global GBI	**USD**	-1.3%	-4.5%
Global Bonds	Citigroup World Broad Investment Grade (WBIG) TR	**USD**	-0.2%	-2.0%
Global Convertible Bonds	UBS Global Convertible Bond	**USD**	4.7%	18.2%
Emerging Market Bonds	JP Morgan EMBI+	**USD**	0.6%	-8.3%

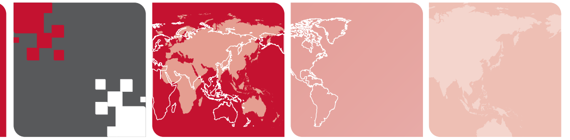
Source: Bloomberg, December 2013.



		To 31 December 2013		
Asset Class/Region	**Index**	**Currency**	**Quarter**	**12 Months**
Property				
US Property securities	MSCI US REIT TR	**USD**	-1.0%	1.3%
Australian Property Securities	S&P/ASX 200 A-REIT Index TR	**AUD**	-3.3%	1.1%
Asia Property Securities	S&P Asia Property 40 Index NR	**USD**	-1.9%	6.5%
Global Property Securities	S&P Global Property USD TR	**USD**	-0.8%	3.7%
Currencies				
Euro		**USD**	1.6%	4.2%
UK Pound Sterling		**USD**	2.3%	1.9%
Japanese Yen		**USD**	-6.7%	-17.6%
Australian Dollar		**USD**	-4.3%	-14.2%
South African Rand		**USD**	-4.6%	-19.4%
Commodities & Alternatives				
Commodities	RICI TR	**USD**	-1.3%	-4.5%
Agricultural Commodities	RICI Agriculture TR	**USD**	-3.3%	-11.1%
Oil	Brent Crude Index (ICE) CR	**USD**	2.4%	0.9%
Gold	Gold index	**USD**	-9.3%	-28.0%
Hedge funds	HFRX Global Hedge Fund	**USD**	2.3%	6.7%
Funds of hedge funds	Credit Suisse/Tremont Hedge Fund USD	**USD**	2.9%*	8.4%*

** Estimate*

Source: Bloomberg, December 2013.



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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.

Momentum Global Investment Management Limited is authorised and regulated by the Financial Conduct Authority in the United Kingdom, and is an authorised Financial Services Provider pursuant to the Financial Advisory and Intermediary Services Act 37 of 2002 in South Africa

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