TRUE

INSIGHT

True Potential Portfolios | Issue 4

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Where Next in Search of Income?

Advanced Diversification pays dividends amid volatile markets, rock bottom interest rates and falling bond yields.

true potential investments

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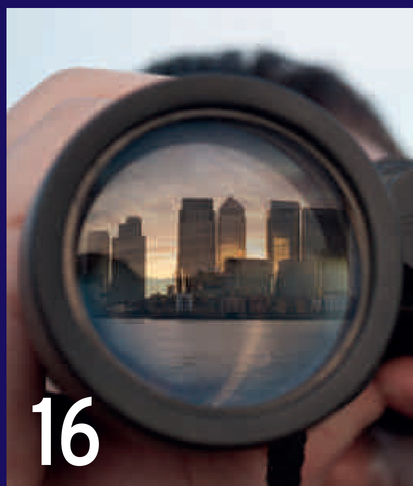
With investing, your capital is at risk. Investments can fluctuate in value and you may get back less than you invest.



A WORD FROM OUR CHIEF INVESTMENT OFFICER

This edition of True Insight marks the first anniversary of the launch of our True Potential Portfolios.

We measure success through the value of assets invested in the Portfolios, which now exceeds £1.3bn, and also the performance outcomes achieved. The returns for all 10 Portfolios, since they were launched in October 2015, are shown on page 4. It is all the more pleasing as these results translate into increased wealth for clients. This is a great start for all of us and we truly believe it can get even better.

The importance of lowering the cost of investing was recognised very early in the history of True Potential because excessive costs negatively impact long term wealth creation. However, lowering costs alone is not sufficient if investors are so fearful of risk that they are unwilling to invest in assets carrying the potential for higher long term returns.

Risk-aversion is widespread, with cash savers having now amassed over £250bn in cash ISAs. This is despite base rates (which act as a proxy for savings rates) having fallen from 5.75% in 2007 to 0.25% today. In fact, the amounts held in cash have increased year upon year as interest rates have declined.*

Our solution for dealing with uncertainty and risk is facilitated by technology supported by multi-asset solutions that mitigate risk. By encouraging clients to set clear savings goals and making it easy to implement them, we make investing a more personalised and enjoyable experience. Our impulseSave® technology encourages the habit of saving regularly from £1 upwards. Around £4m is invested this way each month.

Working with Morningstar, we provide a framework for assessing the levels of risk appropriate to individual preferences and circumstances. In the aftermath of the UK's vote to leave the European Union (EU) and with media headlines of doom and gloom, our clients invested a record £6m the following day.

This is a great turnaround in investor behaviour which has proved to be financially rewarding in the short term. It hints at a completely new attitude to saving that takes us along the journey to closing the savings gap that we have in the UK.

With our suite of multi-asset funds now blended into the True Potential Portfolios we have taken diversification to a new level and have done so while remaining attentive to costs. Our aim is to further dampen volatility, working to bridge the financially disadvantageous gap between low risk - low return and high risk - high return.

So how are we doing this?

Many in the financial industry remain divided along rigid traditional lines favouring either active investing or passive investing that tracks an index. Our approach embraces the best of both worlds. Our portfolios are deliberately positioned on the active-passive spectrum. We utilise lower cost passive strategies blended with active strategies that seek out anomalies carrying the potential to generate excess risk adjusted returns. Through the arrangement with our strategy manager partners we alter the portfolios as markets change. No manager or investment style performs consistently well in all circumstances. Importantly, our technology and the unique partnership with our strategy managers is adaptive so all the work is done for you.

In this fourth edition, we focus on two important areas. The first is the cycle of emotions, which we all face in one way or another, followed by two excellent articles covering investing for sustainable income. The latter subject is particularly pertinent with interest rates having been cut to the bone. Almost unimaginably they may be cut to 0.1% if the Bank of England believes that circumstances merit such action.

The statistics and charts in this edition of True Insight give lots of information on the True Potential Portfolios.

If you would like to know more, please visit : **www.tpinvestments.com.**

Happy reading!

Colin Beveridge, Chief Investment Officer.

*Source: HMRC

MANY HAPPY RETURNS

This year has marked some historic milestones. As a nation, we have voted to leave the European Union. Savers saw the Bank of England slash interest rates further, causing some commercial banks to follow suit.

At True Potential our flagship investment product, the True Potential Portfolios, have over £1.3 billion invested in them up to the end of October, marking 12 months since their launch.

As we pass the first anniversary of our True Potential Portfolios, we are pleased to be able to share their 12-month performance figures and illustrate just why advisers and their clients have invested their trust, and their money, with us.

The positive performance of the Portfolios, is testament to the strategies that we employ in their construction.

True Potential Portfolio	Since Launch
Defensive	8.33%
Cautious	11.57%
Cautious +	10.57%
Cautious Income	12.70%
Balanced	14.22%
Balanced +	15.72%
Balanced Income	14.39%
Growth	17.87%
Growth +	15.56%
Aggressive	19.88%

With investing, your capital is at risk. Investments can fluctuate in value and you may get back less than you invest. Past performance is not a guide to future performance.

REVIEW OF THE MARKETS: Q3 2016

Since the UK's decision to leave the EU, markets globally have enjoyed a strong rally over the three months to the end of September. While the debate continues about the implications of the vote, the UK stock market in particular made new highs in the early part of October.

Some leading equity indices posted double digit Sterling returns in quarter 3 of the year. Bonds also produced healthy returns despite the low yield environment brought about by unconventional monetary policies being pursued by Central banks, not only in the UK but across Europe, the US and in parts of Asia.

One of the reasons offered for the sharp weakening of the pound has been uncertainty amongst some elements of the business community. They speculate that both inward capital investment and portfolio investment from overseas investors will diminish, weakening the demand for Sterling.
There were some major beneficiaries from Sterling's weakness, however.

Companies within the FTSE 100, which are mainly large multinational corporations producing the majority of their revenues from overseas, performed strongly. Smaller and medium sized companies more reliant on the domestic economy struggled but have since recovered, gaining confidence from economic data showing that the UK economy has remained stable.

Historically during times of uncertainty, investors look towards 'safe haven' assets such as Gold but investors have favoured risk seeking assets benefitting from supportive central bank policies.

During this period the Purchasing Manager Index (PMI), an indicator of economic health, fell to 47.6, its lowest levels since 2009. The deterioration in expectations triggered the Bank of England's decision to cut interest rates from 0.5% to 0.25% during August.

As part of a wider package of quantitative easing they also reignited a bond buying programme to drive down company borrowing costs aiming to boost UK economic growth. The impact of lowering interest rates and buying bonds (government (£60bn) and non-financial corporate (£10bn)) had the desired effect, driving bond prices up and lowering bond yields.

UK domestic investors in UK Government bonds and UK Corporate bonds have seen strong returns of 2.3% and 6.0% respectively over the quarter, but returns have since weakened with the fall in the value of Sterling.

Multi-asset portfolios have also produced strong returns as the majority of asset classes posted excellent growth for the quarter. Emerging Markets (EM) and Asia Pacific equities are the standout performers with a further boost from weaker Sterling. The outlook and environment for emerging markets improved generally.

Investors have been rotating out of developed markets and into Emerging Markets attracted by lower valuations across the latter. Emerging Market Bonds also produced impressive returns helped by central bank policies in developed countries suppressing developed country bond market yields making EM bonds look more attractive. Income seeking investors have been stampeding into riskier corporate bonds in all markets and emerging markets in particular in search of higher yields. Risk averse investors in cash ISAs have continued to be put at a disadvantage.

It didn't seem possible, but returns have been lowered yet again. This is one of the consequences of the need to keep interest rates as low as possible for as long as possible to support economic activity, to protect the value of houses which in turn supports job creation.

INVESTMENT OUTLOOK

The True Potential Investment Committee is responsible for making sure that the True Potential Portfolios perform in line with their objectives and remain within their risk profiles. It is the committee's responsibility to scrutinise our investment partners, to ensure they are acting appropriately and in investors' best interests.

Some key themes emerged from recent meetings with our fund manager partners giving an added perspective to what is currently happening in the financial markets:

- **Inflation.** There is a growing sense that inflation will pick up in the months ahead. A rule of thumb is a 10% devaluation in sterling leads to a 1% rise in inflation, but there are a host of factors than can throw the balance one way or another. Inflation may also rise by the simple fact that the anniversary of the commodity price collapse will take place in January 2017 and this in its own right will push up inflation.

- **Rise in US Interest Rates.** Universally accepted as coming in December and while the move will be small and widely anticipated, it will alter the shape of the yield curve by pushing up long term interest rates. A hike of 0.25% speaks to a wider theme that the Federal Reserve is confident that the US economy is strong enough to handle a rise in rates. The amount is small but the main significance is the message it conveys. Our managers remain convinced that the US central bank will remain vigilant on growth at the expense of inflation which may be allowed to run above target for longer than would normally be permitted in relation to historic norms.

- **EU Referendum/US Election.** A cause of more heat than light. Managers in the financial sector are split over whether the likely outcomes will prove as momentous as generally feared. The sentiment underlying these events indicate a growing anti-establishment movement globally. To counteract the groundswell of public opinion ongoing economic support through easy monetary policies and ultimately by fiscal expansion promoted by governments is highly likely.

- **Europe/Japan.** Still regarded as attractive on valuation grounds albeit structurally unappealing for global investors focusing on accessing Japanese equities on a passive (index) basis. Active managers see this as an area for stock picking.

- **US.** Opinion is divided as to whether the growth prospects are worth the premium valuation, especially with US rates going up. However, there was more confidence from some managers that corporate earnings may begin to improve giving support to these valuations.

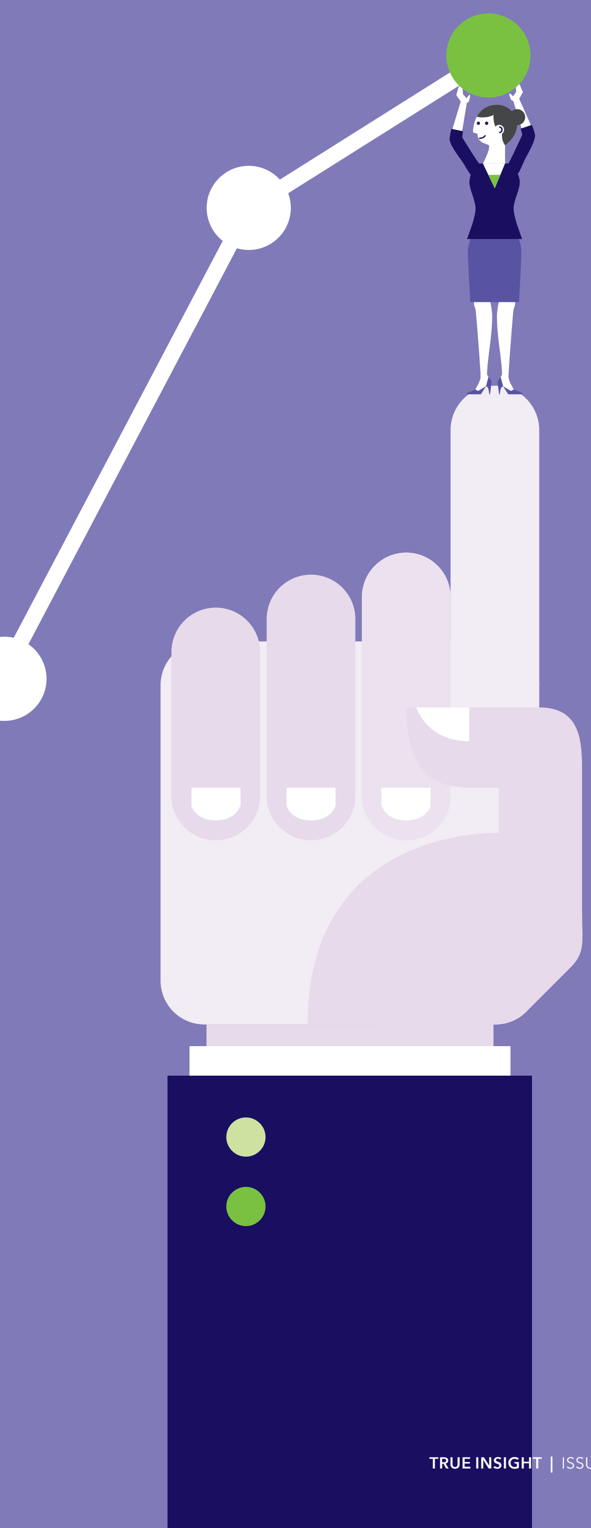
- **Emerging Markets.** Initial concerns that EM bonds and equities would produce sub par returns as the US interest rate cycle turns up have abated, albeit there is acceptance that volatility will move higher during any transition phase.

- **Currency Risk.** Some of our managers use purchasing power parity models (PPP) to assess the fundamental value of a currency. The suggestion they have is that PPP models indicate sterling is now undervalued but may stay weak because of the uncertainty associated with the EU Referendum result. Within our funds some managers hedge currency risk and see it as an opportunity to be exploited.

- **Rising Asset Correlation.** Several managers mentioned that diversification beyond traditional bond, equity and cash allocations is needed to drive future returns and to manage downside risks. Our managers are looking at numerous strategies ranging from hedging currency, exploiting positive momentum, value and factor-based strategies, gold, global real estate, infrastructure assets, inflation linked bonds through to lowering bond duration to mitigate interest rate sensitivity. This is not an exhaustive list.

In conclusion, our managers are expecting volatility to increase over the next few months and stand ready to exploit any weakness in markets. Whilst recognising that any change in the direction of US interest rates or political leadership in America or Europe could unsettle markets, they remain generally constructive on the economic backdrop, albeit still expecting central bank intervention.

The key message is not to be spooked by market volatility and dramatic headlines.



ARE YOUR EMOTIONS DAMAGING YOUR WEALTH?

Team GB's success in cycling at the 2016 Rio Olympics, with 11 medals, is a prime example of mental fitness augmenting physical prowess. Professional investors studying and learning about their own biases and emotions are now pursuing what elite athletes have been doing for many years - applying psychology to enhance performance.

One of the main misunderstandings about our emotional self is that emotions lead to irrational decisions.

In fact, the opposite is true. Psychologists point out that our emotions are rational tools for decision making.

That said, taking decisions based solely on emotions can lead to very poor outcomes, so we need to understand more about this area. Understanding behavioural finance can help to avoid pitfalls.

Take Mr. Jones for example. He is an extremely cautious and risk averse investor.

His investment journey begins with 'Speculative Company plc'. Mr. Jones wouldn't normally take the risk of buying stocks and shares but he has a friend, a professed expert, who says this one company is a sure fire thing. It will bring great riches.

Below we set out the cycle of emotions faced by Mr. Jones as he meanders through the highs and lows of investing speculatively.

With a get rich promise, but a cautious nature, Mr. Jones is reluctant (rational) to invest straight away. He waits and watches, while the shares rise and his optimism builds.

The shares keep going up and his optimism shifts to excitement. In a state of exuberance, he buys with great expectations of getting rich quick.

But the shares start to fall. Questions about the integrity of the management arise giving a strong, clear warning that this is not a safe investment. Mr. Jones shields himself through a state of denial (rational).

With further falls, he cloaks himself in a comfort blanket and no longer looks for information about the company. He fixates solely on the share price.

Denial gives way to fear, desperation and panic. Ironically during these latter stages there are rumours that a good company, 'Long Term Investment plc', believes the shares to be undervalued.

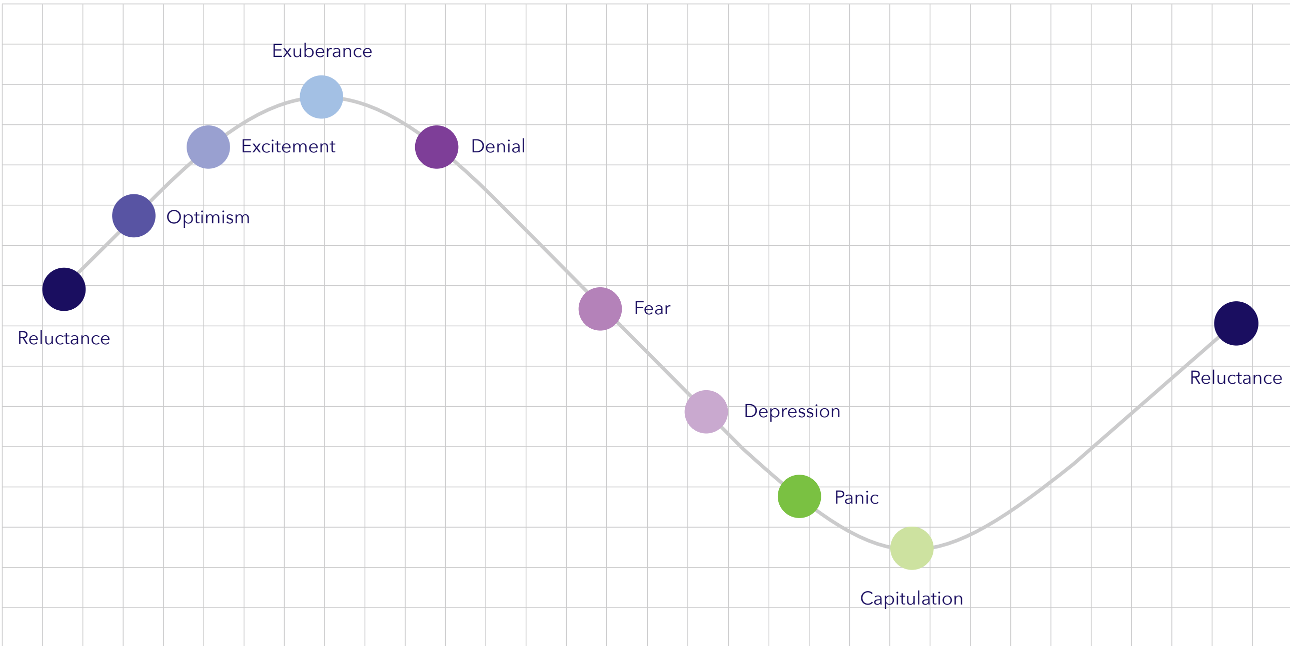
They want to remove the management, but Mr. Jones doesn't spot this because he cannot stomach looking for information. At the final hurdle the shares fall again and Mr. Jones takes back control (rational) by capitulating.

He caves in and sells.

The very next day the Company receives a bid and the shares rise substantially. Mr. Jones is once again reluctant to take a risk.

This may be fiction, but the emotions are real and the lessons to be learned are important.

Chart 1: Cycle of Emotions



What lessons are there in this story?

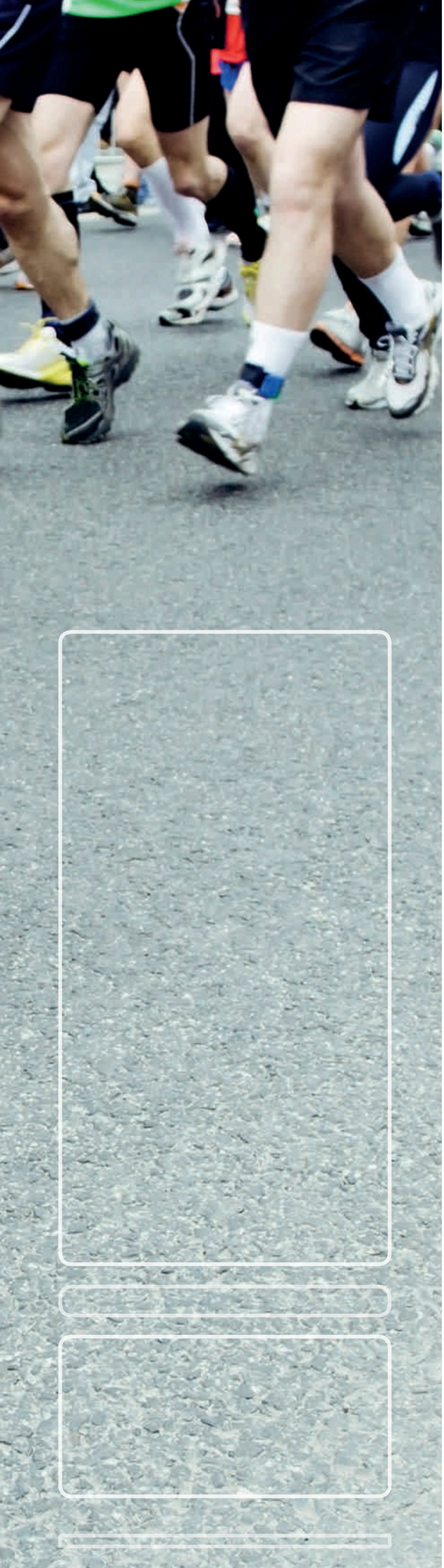
1. Beware get rich quick schemes. Investing for the future is more of a marathon than a sprint.

2. Adopt purposeful practice. This is what works for professional investors, who write things down and have a reason for acting. At True Potential, we place great emphasis on goal-setting.

3. Have something to aim at and chart the course you are on, acknowledging that sometimes you may have to save more and even take some calculated risks. Our technology provides instant gap-to-goal information and impulseSave enables you to close the gap at the push of a button.

4. In order to better understand risk, set your goals in a wider context. Try to understand that risk takes many forms. If you are too risk averse you may be buying emotional comfort at the expense of long term return. Advanced Diversification helps mitigate risk while searching for long-term return potential.

IT'S A MARATHON NOT A SPRINT



Bank deposits are where our reluctant investors (rational) sit comfortably today, but the gap between safety and risk is wide and costly. So how can you get a sense of risk and how can you manage it effectively?

Our True Potential Portfolios give Advanced Diversification by layering in different management styles that perform differently at different times.

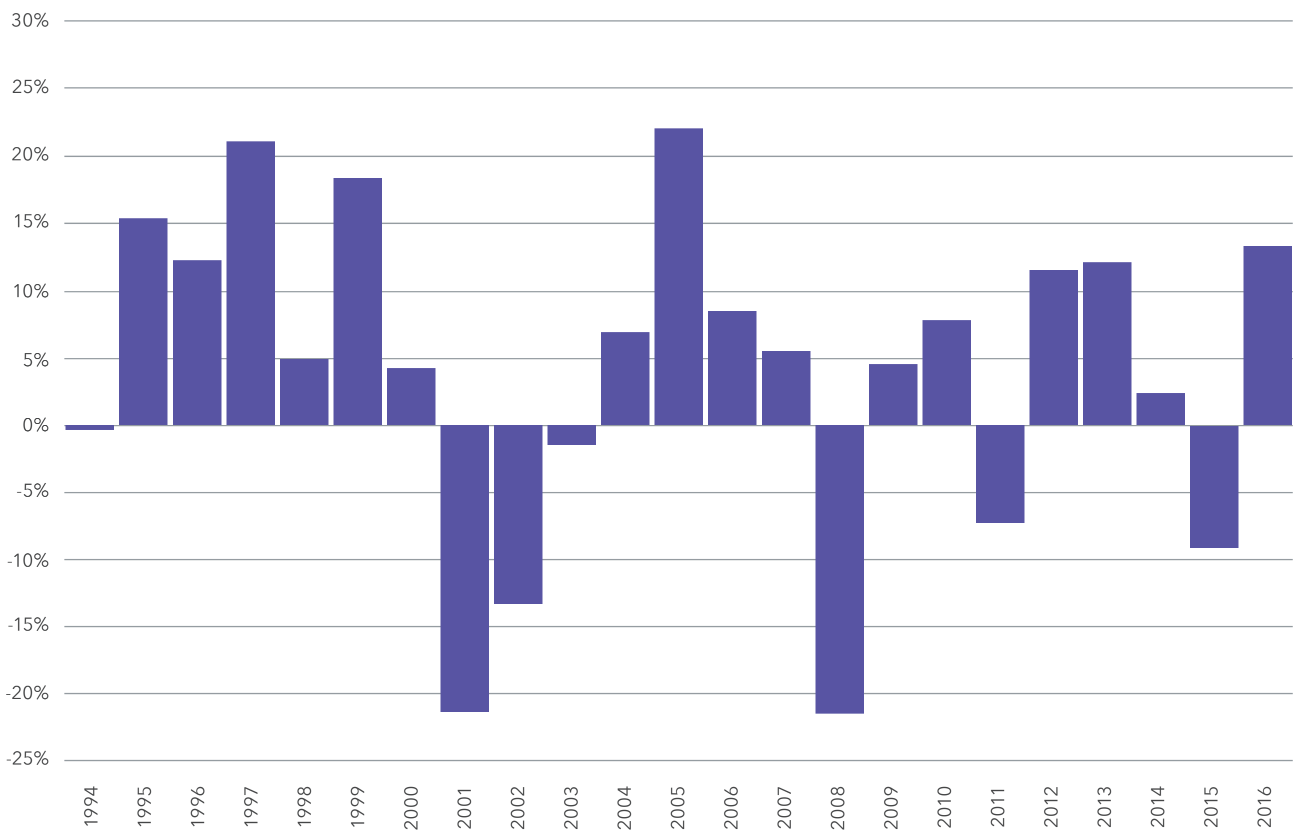
According to psychologists, one way to quell our reluctance to take risk is by reframing the circumstances.

We all know stocks and shares carry higher risks of capital losses than bonds and other fixed income investments.

The table below shows the yearly change in value of the UK stock market and the changes are highly variable. Not only are investors subjected to large ups and downs, frequent swings from profit into loss, and vice versa, elevate our base emotions of fear and greed.

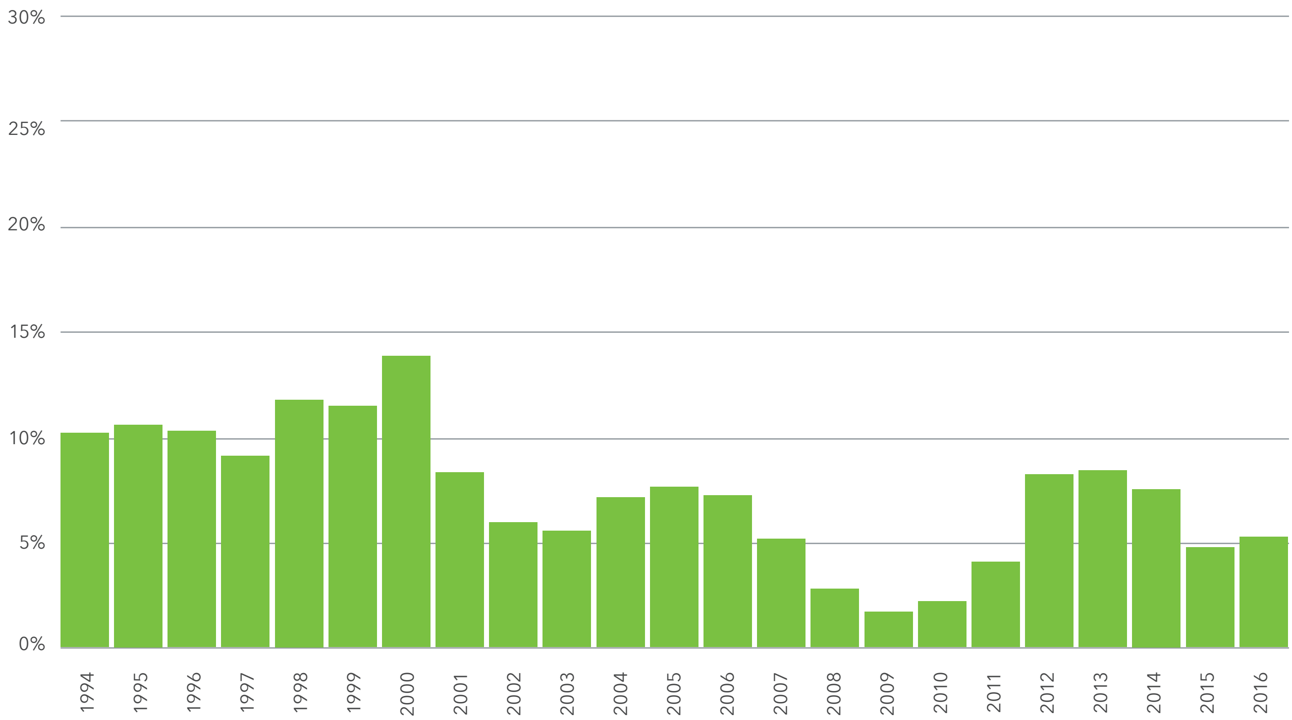
Moreover, psychologists tell us that experiencing financial loss elicits a reaction in the brain similar to pain, so it is not surprising that investors are highly susceptible to loss aversion.

Chart 2: One-year Capital Returns – UK Stock Market



Source: Bloomberg

Chart 3: Ten Year Annualised Total Returns– UK Stock Market



Source: Bloomberg

This is where reframing is important. Using the same data and time period we can show the changes over 10 years, this time making investing seem more like a marathon than a sprint. These price changes for the green bars in chart 3 are the returns from investing over rolling ten-year periods but divided evenly into annualised returns. So if you imagine starting to invest in 1984 and wake up in 1994 the return 'reframed' is the compound rate of return each year for 10 years.

We then start again from from 1985 onward conducting the same calculation over subsequent 10 year periods.]

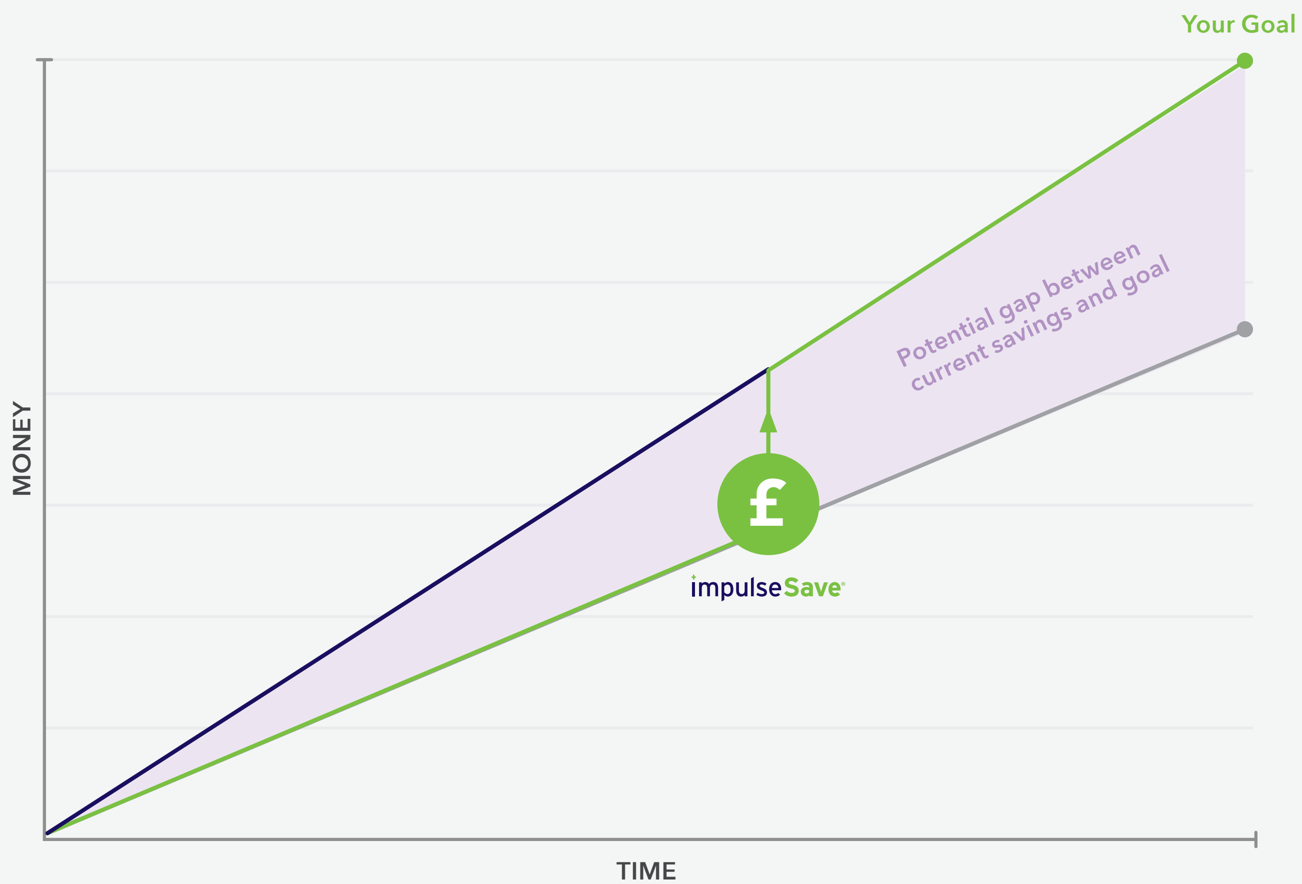
This allows our investors to see that the daily market fluctuations, which carry sensational headlines, can be ignored if you are a long term investor because the risk of loss is substantially lower if the time period is stretched out.

Past performance is not a guide to future performance.

Saving over a longer period without having to access capital prematurely limits the possibility of this happening at an inopportune time.

In fact, with regular saving we begin to think about saving more when markets are falling as this gives the prospect of a better return over time.

Our impulseSave® technology makes ongoing and regular investing much easier. It enables investors to make top-ups from smart devices and take advantage of market fluctuations.



Risk Managed

The True Potential Portfolios manage different levels of risk through holding 120,000 investments and some very different manager styles.

It is for each individual to choose what suits their needs or discuss with a financial adviser. This approach alongside our enabling technology reassures and empowers the 'reluctant and rational' investor.

The Portfolios bridge the gap between the emotional comfort provided by low risk deposits and the potential for good long term returns from taking more risk.

For more information about the True Potential Portfolios and impulseSave®, please visit **www.tpinvestments.com**

WHERE NEXT IN SEARCH OF INCOME?

At its most recent meeting in September, the US Federal Reserve Board gave its clearest indication yet that it may put up interest rates by the end of the year.

The Fed also pencilled in two further increases during 2017 as it seeks to 'normalise' interest rates from the emergency measures introduced in the wake of the 2008 financial crisis.

While rates look to be heading higher in the US, the same cannot be said in the UK. In the wake of the EU referendum in June, the Bank of England moved to stabilise financial markets by cutting interest rates to 0.25% from 0.5%, the lowest level set by the institution since it was established in 1694.

Rates could be dropped even further, potentially to 0.1%, depending on how the economy fares in the months ahead.

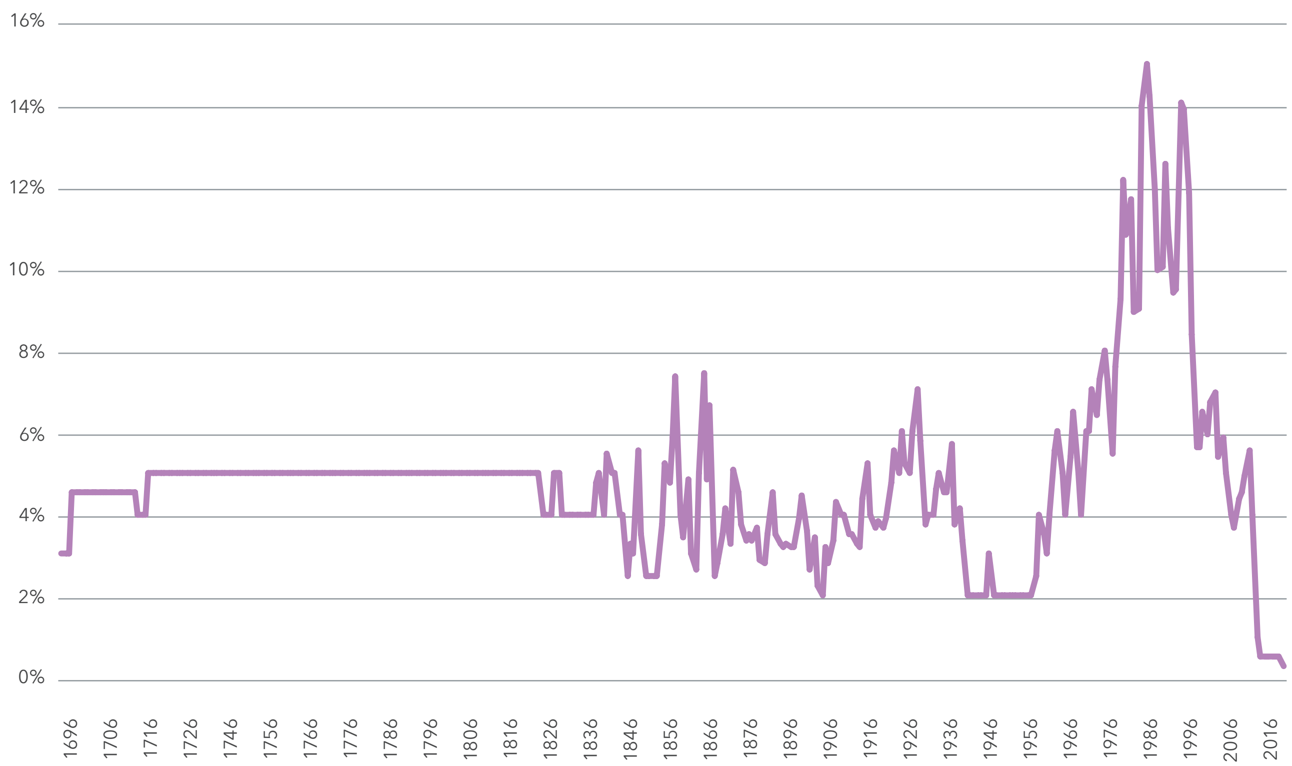
While this is good news for anyone with an interest rate tracking mortgage, savers sitting in cash will continue to get very low returns that lie below inflation. After accounting for the rise in the cost of living with inflation currently at 1%, their wealth is gradually being eroded in real terms.

The pressures of investing for income have intensified after eight years of interest rates at record lows. The distortion of the financial markets induced by quantitative easing and the actions of Central Banks around the world have encouraged investors into taking on a higher level of risk. Cash that once would have remained on deposit in the bank or been invested in government bonds earning, say 5%, is now earning close to nothing.

Proactive investors have looked to corporate bonds and stock market investments for a higher yield albeit with a greater level of risk, but very many investors remain embedded in cash.

As the Financial Conduct Authority (FCA) pointed out recently, some savers are being paid 0.1% and that was before the most recent cut.

Chart 4: BoE Base Rate: 1696 – 2016



Source: Bank of England, September 2016. Showing 10 year averages for the period from 1696-1816.
In this period the highest base rate was 10% and the lowest 2%.

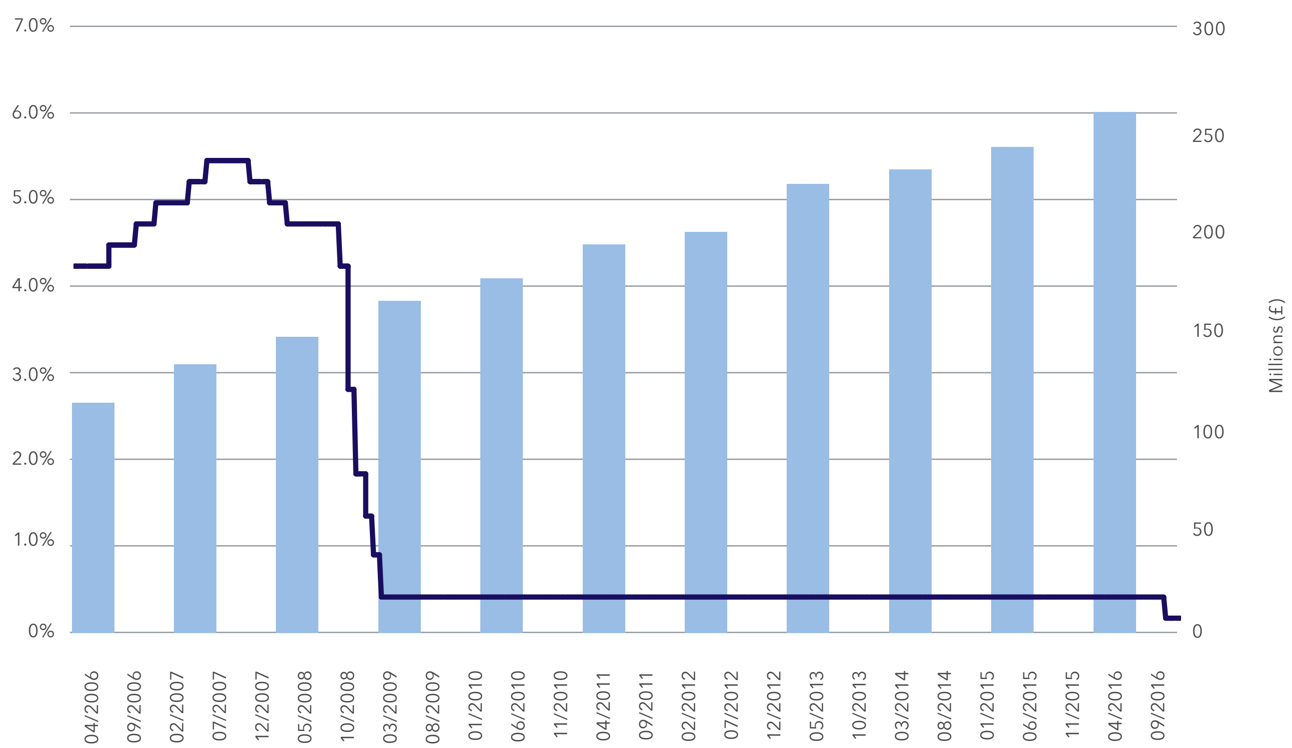
The chart below highlights that while rates have been cut, cash balances in adult ISAs have actually been growing. In our article looking at investor emotions around risk taking (page 8) we explore some of the reasons for this behaviour.

At True Potential our Cautious Income Portfolio yields 3.8% while Balanced Income currently pays out 4.0%.* These compare favourably with the FTSE 100, which is heavily dependent upon the dividends from a few large companies. Just eight FTSE 100 firms are expected to pay out more than 50% of the index's total cash dividend payments this year.

The FTSE All Share Index is more diversified although not nearly as diversified as our Income Portfolios and yields less.

Given the obvious difficulties in achieving a reasonable level of income without taking an unacceptable degree of risk, we questioned our fund managers about their investment philosophies. Their responses show the difference between managing investments to generate a sustainable income rather than focussing solely on a high yield, the issues they encounter, the various investments available to them and some of the pitfalls to avoid.

Chart 5: Total in UK Cash ISAs v UK Base Rate



Source: HMRC and Bloomberg, September 2016

* Twelve-month dividend yields as at the end of September 2016. The yields on our Portfolios vary with the yields on the underlying funds and through the changes we make to fund selection. Past performance is not a guide to future performance.

We also asked them how they see the investment landscape developing and where they are investing in order to achieve an attractive, recurring income stream. What remains clear among our managers is that preservation of clients' capital is as important as the level of income generated.

They, like we, are mindful not to compromise the safety of the underlying investments by attempting to achieve unrealistic levels of income today at the expense of capital growth tomorrow.

In fact, there is a strong positive relationship between income growing sustainably and capital appreciation.

As befits the Advanced Diversification strategy that runs through all our portfolios, each of our fund managers has a different approach.

They all share the same prudent philosophy, however, of maximising the level of income generated while avoiding the temptation to take on too much risk.

The managers ensure the companies they invest in can afford the dividends or bond interest that they pay and are not lured into investing into illiquid bond issues that appear attractive to buy but prove impossible to sell when the time comes.

Although investing for income brings its own challenges, the rewards are evident. Buying companies which manage to improve the level of dividends paid out year after year not only provides a very useful income in the near term but generally ensures capital growth over the long term.

This means that both the original investment and the income stream derived from it should keep pace with inflation in a way that investing purely in cash deposits or fixed income bonds will not.

If we consider the position of an investor starting to invest over 25 years ago in stocks and shares we can get a sense of the importance of dividends. Over this time period the total return is highly attractive with at least two-thirds of the amount coming from the effect of dividends.

Reinvesting dividends over time, known as compounding, is also important because ten years ago dividends made up half of the total; today it is two thirds.

So the longer you invest, the greater the potential benefit from compounding.

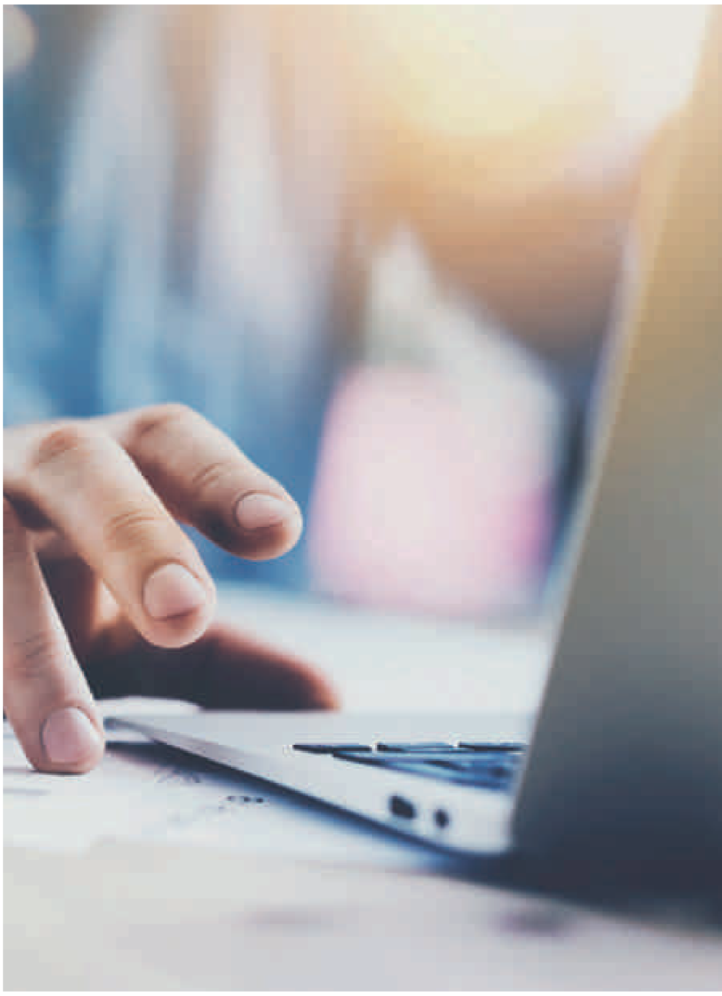
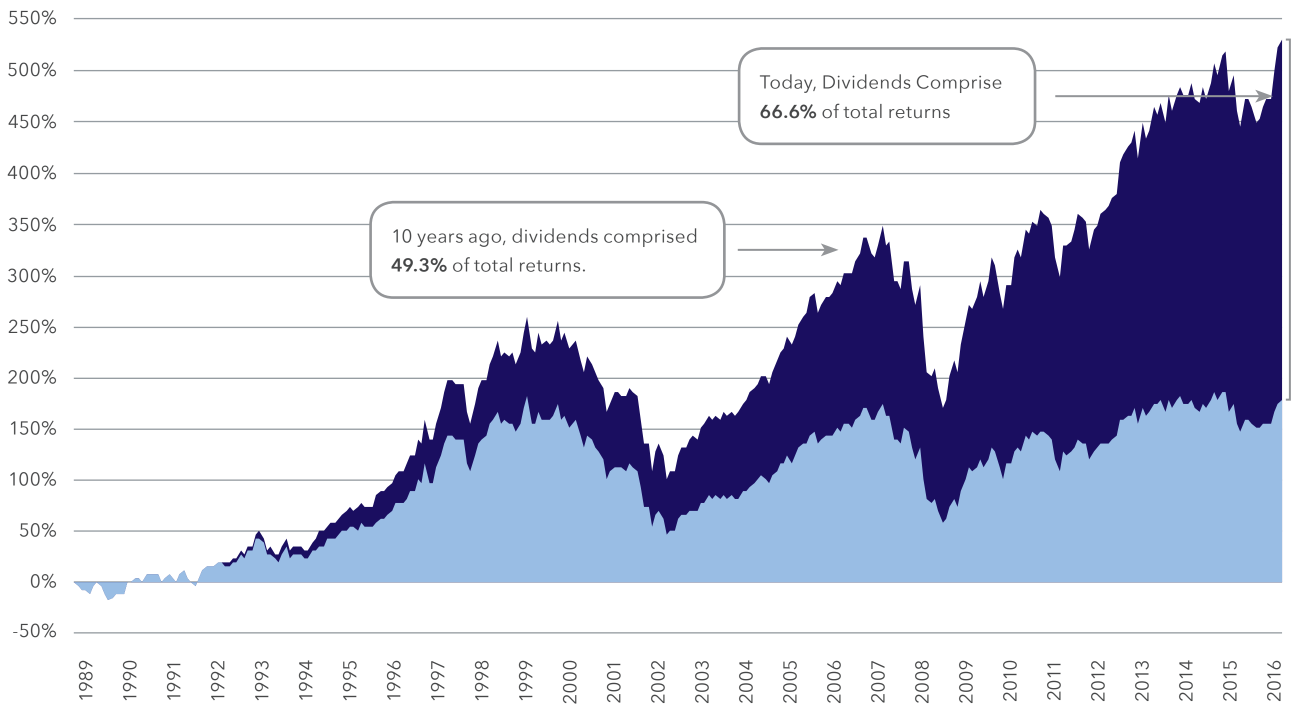


Chart 6: FTSE 100 Cumulative Total Return (Capital + Dividends)



Source: Bloomberg, data as of 31 August 2016

Part of this increasing focus on dividend income reflects the fact that, with interest rates so low, investors who may traditionally have favoured bond markets have migrated to equities in the search for yield.

They have favoured those stocks with good capital discipline and the same strong, positive cash flow that they look for in a bond investment.

What will be interesting is to what extent those bond investors who sought out income in the equity markets migrate back to their favoured asset class.

Bond markets may well be turbulent in the months ahead if as expected interest rates tick up in the US, but any volatility should also present attractive buying opportunities.

What will remain unchanged is our commitment through our engagement with our sub managers to providing a secure sustainable return across our Income Portfolios. We retain a strong commitment to Advanced Diversification aiming for superior, risk adjusted returns whatever may happen to interest rates.

OUR INCOME MANAGERS

The Goldman Sachs Income Builder Fund offers access to the Goldman Sachs World Class investment proposition as well as a dividend yield of 4.3%*. They invest in a broad range of Global Equities and Bonds and offer sustainable income and capital appreciation.

The True Potential Threadneedle Monthly Income Fund offers a monthly paying dividend yield of 4.1%*, by investing in a portfolio of UK Equities and Bonds. Threadneedle are excellent stock pickers offering capital growth as well as income.

The True Potential Schroders Cautious Income Fund offers management from an award-winning team offering a stable income stream with a dividend yield of 3.6%*, paid quarterly. They feel that no one fund manager can excel in every aspect of investing and therefore access the best fund and investment products from around the world.

The True Potential Close Brothers Income Fund invests directly into company shares, fixed interest investments and alternative investments. They offer a dividend yield of 3.3%* which is paid quarterly. Close Brothers specialise in picking stocks, looking globally to locate opportunities.

* At the time of writing.

SPOTLIGHT: THE INCOME MANAGERS

We partner with industry-leading fund managers with combined assets of over £4.5 trillion to give investors a forward-looking and expert strategy. For this edition of True Insight, we put income managers Schroders, Goldman Sachs, Close Brothers, and Columbia Threadneedle, in the spotlight.

"How would you describe your investment philosophy around income investing?"

Schroders
Our investment philosophy across our fund range is one of focusing on capital preservation whilst taking advantage of opportunities to capture upside, ultimately delivering strong risk-adjusted returns.

Close Brothers
Our focus is on good risk:reward and this will encompass a whole range of yields. It is not just about finding all the bonds and equities with the highest yields on Day 1 to build a portfolio, you want to back companies that can afford their dividends/bond coupons.

Columbia Threadneedle
We have a pragmatic, diversification approach to risk management and our main hunting ground is the lower end of FTSE 100 and top end of the FTSE mid-250. In terms of stock selection, we are most interested when a company's profitability has fallen below historic average but core franchise remains attractive.

Goldman Sachs
Our objectives are to provide investors with attractive and sustainable income, offer some capital appreciation, and do so with a strong focus on risk management. We don't stretch for yield and the portfolio is managed dynamically by an integrated team.

With investing, your capital is at risk. Investments can fluctuate in value and you may get back less than you invest.

"With such poor returns on low risk savings accounts, what do you say to investors looking for a better income from investing but facing the prospect of taking more risk?"

Goldman Sachs
All investments carry some degree of risk, so when making investment decisions, investors need to consider the potential for returns, including income, and weigh that up against the risk that each investment carries.

Portfolio diversification plays an important role in managing an investor's risk.

"What actions are you taking to ensure you can generate recurring income for clients?"

Columbia Threadneedle
We model the income for the portfolios so that we can try and smooth the dividend yield provided over the market cycle. As well as holding cash in the portfolio, we aim to find a few contrarian positions every year to buy into or build up in the fund.

Schroders
By compounding returns and protecting clients' capital, we are going a long way to ensuring that the income for our clients is stable. We invest with proven fund managers whom we trust to continue delivering good growth and income levels responsibly.

SPOTLIGHT: THE INCOME MANAGERS

"With bond yields at such depressed levels, what non-traditional income producing assets can you use within portfolios?"

Close Brothers
We have made use of government backed projects such as schools and hospitals and renewables infrastructure funds, including wind farms and solar parks. These funds offer an attractive absolute level of return and yield, with the benefit of indexlinkage that helps protect the investor from inflation if it rises.

"With inflation and yields being low, which areas of the market would you turn to if yields and inflation started to shift up?"

Columbia Threadneedle
We believe that our fund is well diversified and already has exposure to companies with dividend growth potential. We have been looking at the banking sector in detail and they would be beneficiaries if base rates/ yields were to increase, so this environment could make them more interesting. However, this would also help stocks with large pension deficits, which we already have exposure to.

"What do you say to investors tempted by higher yields?"

Schroders
Over recent years, the action by central banks around the world to drive yields ever lower has induced investors to seek income from increasingly risky areas. This intense 'hunt for yield' has combined with unprecedented levels of quantitative easing by these banks, which has driven valuations of many assets to new levels. As we move into the next stage of the cycle, with potential inflationary pressures coming through, we would argue that it is perhaps time to focus less on grabbing yield and more on capital preservation.

"In a very low interest rate environment for the foreseeable future, how do you see income investment developing over the next few years?"

Schroders
There is no point us returning a 4% yield in any given year if the capital base has gone down 10%. As such we try to manage our annual income target over the medium term, believing that there are times to reach for yield and times when the preservation of capital is of greater importance.

Close Brothers
The fund will look to continue to explore and research new asset classes to help diversify further. With lower yields available in bonds and equities, fund yield expectations will need to come down.

Columbia Threadneedle
We believe that the reinvestment of dividend yields will be a large driver of total returns over the next five years.

Goldman Sachs
Amid low interest rates, we believe investors will need to consider non-traditional asset classes to achieve attractive income over the next few years. However, such investments should be incorporated in a diversified income portfolio, in order to manage any additional volatility.

For more information about our investment team and our partners, please visit www.tpinvestments.com

THE SCIENCE BEHIND OUR PORTFOLIOS

How we optimise the Portfolios

Optimisation of our Portfolios is conducted against equally-weighted portfolios mapped to five Morningstar risk categories.

For example, we offer eight funds within the Balanced category, therefore if no preference was given to one fund over another, an equally-weighted allocation to each fund would be 12.5%.

When we build our True Potential Portfolios, we tactically allocate away from the equally-weighted portfolios aiming for lower volatility, lower cost, higher expected return and a better risk-adjusted return than could be expected from choosing an equal allocation.

	Defensive	Cautious	Balanced	Growth	Aggressive	Cautious +	Balanced +	Growth +	Cautious Income	Balanced Income
Risk (Volatility)	✓	✓	✓	✓	✓				✓	✓
Risk (Mapped)	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
Cost		✓	✓	✓	✓	✓	✓	✓	✓	✓
Long-Term Expected Return		✓	✓	✓		✓	✓	✓	✓	✓
Risk-Adjusted Return	✓	✓	✓	✓	✓	✓	✓		✓	✓
Income									✓	✓

With investing, your capital is at risk. Investments can fluctuate in value and you may get back less than you invest.

Risk (Portfolios)

Risk is estimated using the asset composition of each Portfolio. The higher the measure of standard deviation, the more volatile the Portfolio will be. We construct separate Portfolios for each of the five risk categories containing all of the funds mapped to that risk category. When we optimise these Portfolios, we make sure they are lower risk than the equally-weighted Portfolios containing the same funds.

Risk (+ Portfolios)

Our three + Portfolios use funds outside the Portfolio's own risk category. For example, the + Balanced Portfolio does not include any Balanced funds. When we optimise for the + Portfolios, we make sure that each Portfolio's measure of risk does not stray outside the risk band set for each risk category.

Risk (Income Portfolios)

Our two Income Portfolios use all available income funds from the Cautious, Balanced and Growth risk categories. We then allocate accordingly to create one Portfolio mapped to the Cautious risk category and one mapped to the Balanced risk category.

Cost

This is an important factor as costs negatively impact future returns. This is why we build our Portfolios with the objective of being lower cost than an equally-weighted Portfolio. However, it should be noted that at times the choice may lie between lower cost and higher risk. The impact from risk is disproportionate to the impact from cost. It is worth remembering that our funds are already amongst the lowest cost in the market.

Expected Return

An estimate of future expected risk is based on the future expected returns for each asset class. When our Fund Managers change the underlying assets in our funds, the Portfolio compositions change. The expected returns for each of our Portfolios will change with the composition of the underlying assets in each fund.

Risk-Adjusted Return

Risk-adjusted return is based on future expected returns for each Portfolio, minus the risk-free rate of return, divided by the level of expected volatility calculated for each Portfolio. Our objective over time is to manage toward a better risk-adjusted outcome.

PORTFOLIO SPOTLIGHT: TRUE POTENTIAL PORTFOLIOS

Each True Potential Portfolio contains all of the funds available within its risk category. The True Potential Portfolios have the greatest degree of diversification, meaning they are less prone to highs and lows relative to our + portfolios.

We optimise the portfolios with the objective of being lower risk than an equally-weighted portfolio. In addition, the True Potential Portfolios do not have an income focus, which makes them very different to our Income Portfolios. However, when investing in a True Potential Portfolio, some clients are happy to take income by selling units. Below are the optimisation results for the True Potential Portfolios.

We always aim to optimise across all factors where possible, however, sometimes we may place more emphasis on one factor over another.

True Potential Portfolio	Since Launch
Defensive	8.33%
Cautious	11.57%
Cautious +	10.57%
Cautious Income	12.70%
Balanced	14.22%
Balanced +	15.72%
Balanced Income	14.39%
Growth	17.87%
Growth +	15.56%
Aggressive	19.88%

	Defensive	Cautious	Balanced	Growth	Aggressive
Risk (Volatility)	✓	✓	✓	✓	✓
Cost		✓	✓	✓	✓
Long-Term Expected Return		✓	✓	✓	
Risk-Adjusted Return	✓	✓	✓	✓	✓

Below shows a cost comparison to see how each of the True Potential Portfolios are positioned, compared to their equally-weighted portfolio equivalent.

	Defensive	Defensive equally-weighted	Cautious	Cautious equally-weighted	Balanced	Balanced equally-weighted
Cost	0.75%	0.74%	0.84%	0.86%	0.89%	0.89%

	Growth	Growth equally-weighted	Aggressive	Aggressive equally-weighted
Cost	0.81%	0.81%	0.77%	0.77%

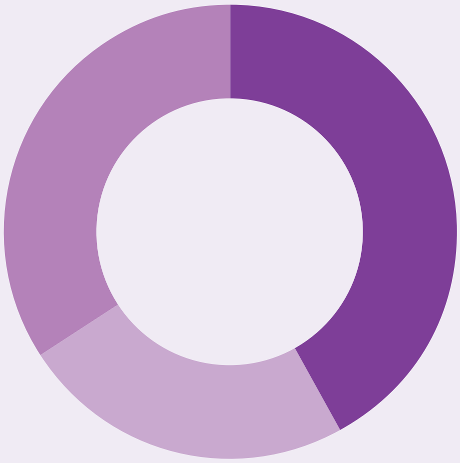
Asset Allocation

Asset Class	Defensive	Cautious	Balanced	Growth	Aggressive
UK Equities	5.4%	12.6%	16.2%	19.5%	19.9%
North American Equities	16.9%	21.9%	25.4%	33.7%	40.9%
European Equities	6.1%	7.1%	9.2%	9.3%	12.9%
Japanese Equities	2.1%	2.7%	4.8%	4.0%	6.4%
Asia Pacific Equities	0.8%	1.5%	2.3%	2.5%	2.3%
Emerging Market Equities	0.0%	1.4%	3.9%	7.7%	10.0%
Global Bonds	12.1%	8.4%	5.1%	2.3%	0.5%
Global Inflation Linked Bonds	0.9%	1.0%	0.8%	0.7%	0.0%
Emerging Market Bonds	1.2%	3.1%	3.5%	4.3%	1.1%
Global High Yield Bonds	6.7%	5.5%	5.3%	4.0%	0.3%
UK Gilts	6.8%	8.2%	5.5%	3.2%	0.7%
UK Credit	6.5%	10.8%	8.0%	3.6%	1.5%
Property	0.5%	2.0%	1.7%	2.6%	1.2%
Commodities	0.5%	1.1%	1.3%	0.6%	0.3%
Cash	33.5%	12.7%	7.0%	2.0%	2.0%

Source: Smith & Williamson, 30th September 2016

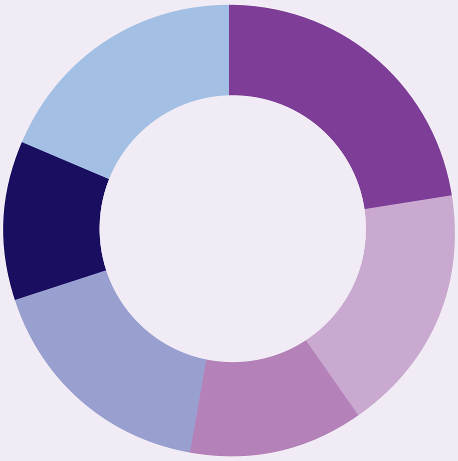
Asset Class	Defensive	Cautious	Balanced	Growth	Aggressive
Equities	31.3%	47.2%	61.8%	76.7%	92.4%
Bonds	34.2%	37.0%	28.2%	18.1%	4.1%
Alternatives	1.0%	3.1%	3.0%	3.2%	1.5%
Cash	33.5%	12.7%	7.0%	2.0%	2.0%

STYLE ALLOCATIONS:



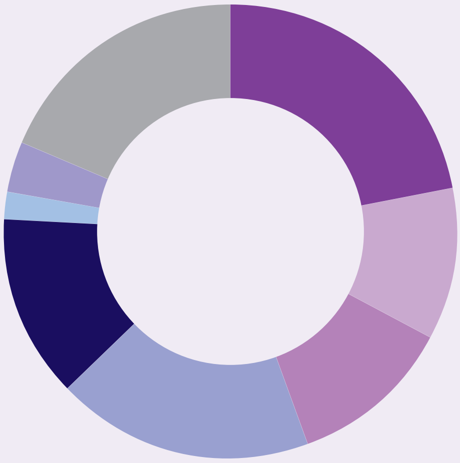
Defensive

Manager of Managers - SEI	42.0%
Actively Passive - 7IM	24.0%
Adaptive Investment - UBS	34.0%



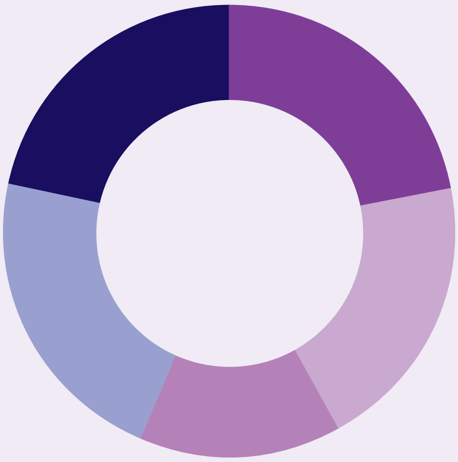
Cautious

Manager of Managers - SEI	22.5%
Actively Passive - 7IM	18.0%
Directly Invested - Close Brothers	12.5%
Risk-Based - Allianz	17.0%
Fund of Funds - Schroders	11.5%
Adaptive Investment - UBS	18.5%



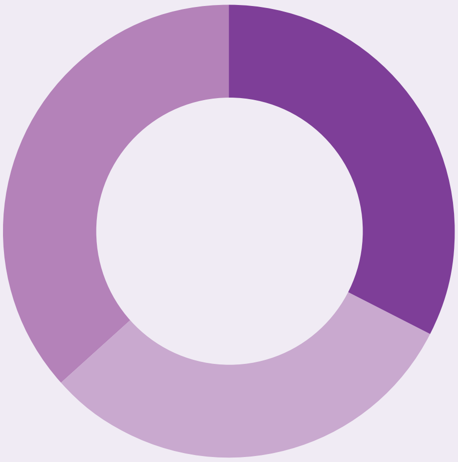
Balanced

Manager of Managers - SEI	22.0%
Actively Passive - 7IM	11.0%
Directly Invested - Close Brothers	11.5%
Risk-Based - Allianz	18.5%
Fund of Funds - Schroders	13.0%
Dynamic - Goldman Sachs	2.0%
Income Builder - Goldman Sachs	3.5%
Adaptive Investment - UBS	18.5%



Growth

Manager of Managers - SEI	22.0%
Actively Passive - 7IM	20.0%
Directly Invested - Close Brothers	14.5%
Risk-Based - Allianz	22.0%
Adaptive Investment - UBS	21.5%



Aggressive

Manager of Managers - SEI	32.5%
Actively Passive - 7IM	31.0%
Adaptive Investment - UBS	36.5%

PORTFOLIO SPOTLIGHT: + PORTFOLIOS

The + group of portfolios are more concentrated in their fund selection, containing larger fund positions compared to their risk category equivalents in the True Potential Portfolios.

The + portfolios are constructed using funds from right across the risk spectrum, while staying within the risk band for their risk category. The + Portfolios do not include funds from the same risk category to which the portfolio is mapped. In other words, the Balanced+ Portfolio does not select funds mapped to the Balanced risk category. To optimise the portfolios in the + category, we select from all of the funds outside of the portfolios' respective risk category.

This approach enables us to optimise across all factors, however, sometimes we may place more emphasis on one factor over another.

	Cautious +	Balanced +	Growth +
Risk (Volatility)	✓	✓	✓
Cost	✓	✓	✓
Long-Term Expected Return	✓	✓	✓
Risk-Adjusted Return	✓	✓	

	Cautious +	Cautious equally-weighted	Balanced +	Balanced equally-weighted	Growth +	Growth equally-weighted
Cost	0.86%	0.86%	0.85%	0.89%	0.82%	0.81%

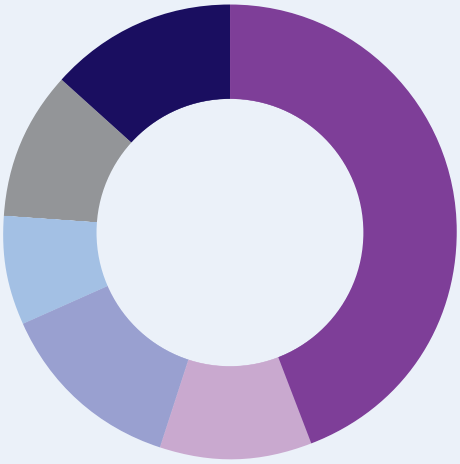
Asset Allocation

Asset Class	Cautious +	Balanced +	Growth +
UK Equities	11.0%	17.3%	20.7%
North American Equities	20.6%	29.9%	39.3%
European Equities	8.9%	8.4%	12.0%
Japanese Equities	4.3%	3.6%	5.4%
Asia Pacific Equities	1.7%	2.2%	2.4%
Emerging Market Equities	2.4%	4.7%	8.4%
Global Bonds	8.9%	5.9%	0.5%
Global Inflation Linked Bonds	0.9%	2.0%	0.0%
Emerging Market Bonds	1.2%	2.9%	0.7%
Global High Yield Bonds	5.2%	5.6%	0.2%
UK Gilts	6.2%	5.5%	3.6%
UK Credit	5.5%	3.5%	3.1%
Property	1.1%	1.7%	0.8%
Commodities	1.1%	0.6%	0.7%
Cash	21.0%	6.2%	2.2%

Source: Smith & Williamson, 30th September 2016

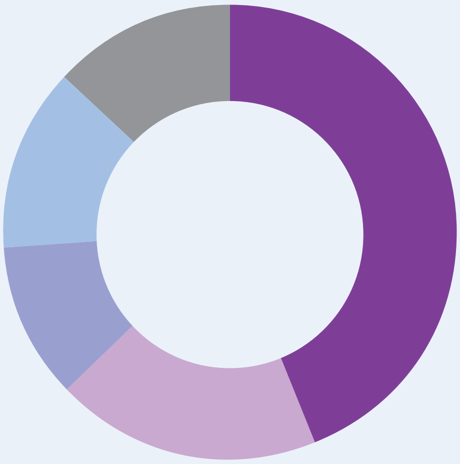
Asset Class	Cautious +	Balanced +	Growth +
Equities	48.9%	66.1%	88.2%
Bonds	27.9%	25.4%	8.1%
Alternatives	2.2%	2.3%	1.5%
Cash	21.0%	6.2%	2.2%

STYLE ALLOCATIONS:



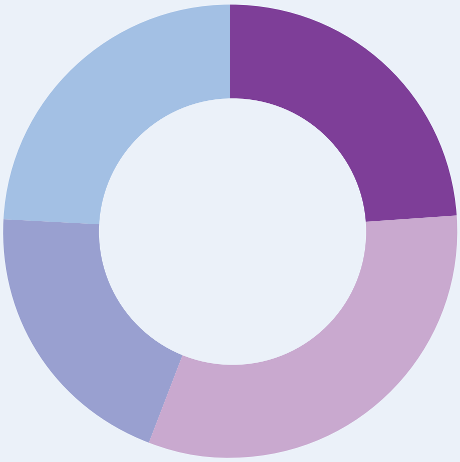
Cautious +

Manager of Managers - SEI	44.0%
Directly Invested - Close Brothers	11.5%
Fund of Funds - Schroders	13.0%
Actively Passive - 7IM	8.0%
Risk-Based - Allianz	10.5%
Adaptive Investment - UBS	13.0%



Balanced +

Manager of Managers - SEI	44.0%
Directly Invested - Close Brothers	19.0%
Actively Passive - 7IM	11.0%
Risk-Based - Allianz	13.0%
Adaptive Investment - UBS	13.0%



Growth +

Directly Invested - Close Brothers	24.0%
Manager of Managers - SEI	32.0%
Actively Passive - 7IM	20.0%
Adaptive Investment - UBS	24.0%

PORTFOLIO SPOTLIGHT: INCOME PORTFOLIOS

Each Income Portfolio in the True Potential Portfolios range is focused on yield and income sustainability, therefore we have income as an additional optimisation factor.

Given that investors in these portfolios are seeking income above capital growth, the income optimisation factor is our primary consideration.

We have optimised on all factors for both portfolios; income, risk, cost, long-term expected return and risk-adjusted return.

The Cautious Income Portfolio is currently yielding 3.82% and the Balanced Income Portfolio 4.01% with the equally-weighted Portfolio yielding 3.70%.

Source: Bloomberg, 30 September 2016

	Cautious Income	Balanced Income
Risk (Volatility)	✓	✓
Cost	✓	✓
Long-Term Expected Return	✓	✓
Risk-Adjusted Return	✓	✓
Income (Income funds only)	✓	✓

	Cautious Income	Cautious equally-weighted	Balanced Income	Balanced equally-weighted
Cost	0.81%	0.86%	0.85%	0.89%

PORTFOLIO SPOTLIGHT: INCOME PORTFOLIOS

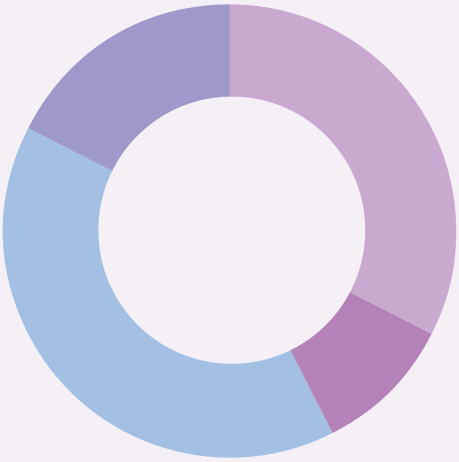
Asset Allocation

Asset Class	Cautious Income	Balanced Income
UK Equities	23.3%	29.8%
North American Equities	11.5%	13.1%
European Equities	6.2%	6.2%
Japanese Equities	1.8%	1.7%
Asia Pacific Equities	0.8%	0.6%
Emerging Market Equities	0.3%	0.3%
Global Bonds	10.9%	11.9%
Global Inflation Linked Bonds	0.6%	0.1%
Emerging Market Bonds	0.8%	1.1%
Global High Yield Bonds	12.7%	15.8%
UK Gilts	1.6%	0.5%
UK Credit	20.8%	13.0%
Property	2.5%	1.0%
Commodities	2.5%	0.7%
Cash	3.7%	4.2%

Source: Smith & Williamson, 30th September 2016

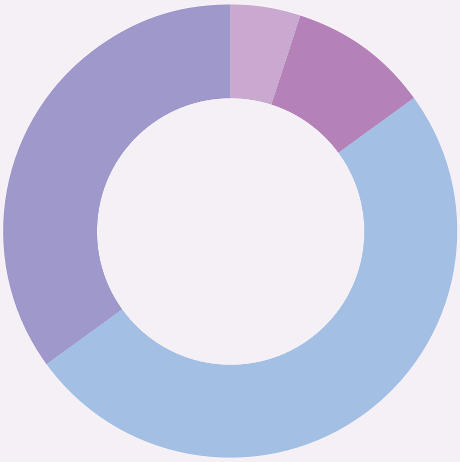
Asset Class	Cautious Income	Balanced Income
Equities	43.9%	51.7%
Bonds	47.4%	42.4%
Alternatives	5.0%	1.7%
Cash	3.7%	4.2%

STYLE ALLOCATIONS:



Cautious Income

Directly Invested - Close Brothers	32.5%
Fund of Funds - Schroders	10.0%
Income Builder - Goldman Sachs	40.0%
Income Strategies - Threadneedle	17.5%



Balanced Income

Directly Invested - Close Brothers	5.0%
Fund of Funds - Schroders	10.0%
Income Builder - Goldman Sachs	50.0%
Income Strategies - Threadneedle	35.0%

YOUR PORTFOLIO ON DEMAND

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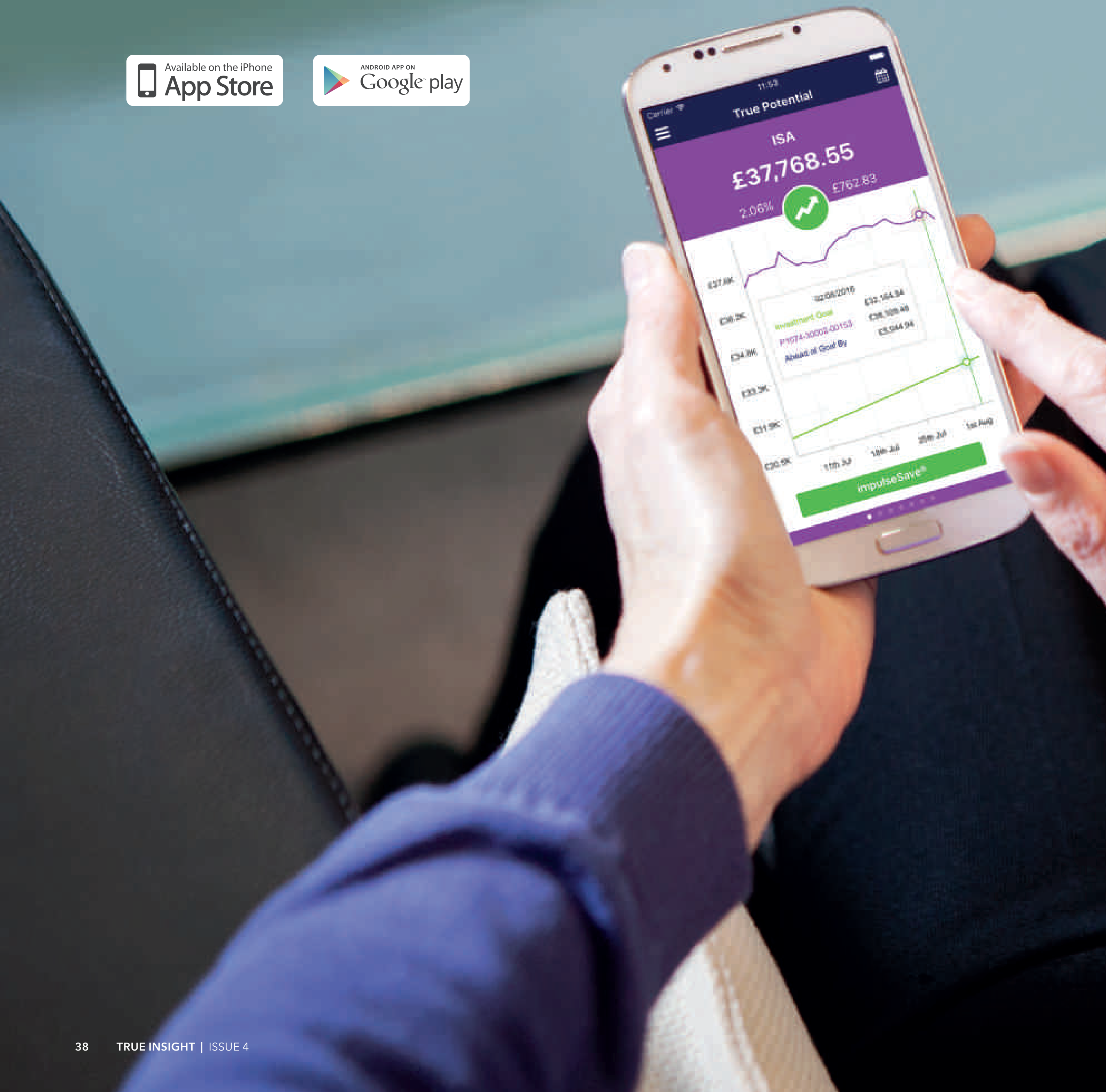

For more information on our
True Potential Portfolios, contact us at
investmentmanagement@tpllp.com.

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Registered Head Office: Newburn House, Gateway West, Newburn Riverside, Newcastle upon Tyne, NE15 8NX
London Office: 42-44 Grosvenor Gardens, Belgravia, London, SW1W 0EB

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