TRUE

INSIGHT

True Potential Portfolios | Summer 2016

PAGE 08

Navigating the Maze Post BREXIT

An in-depth feature about diversification, and why it was important for investors facing uncertainty during and after Brexit.

true potential investments

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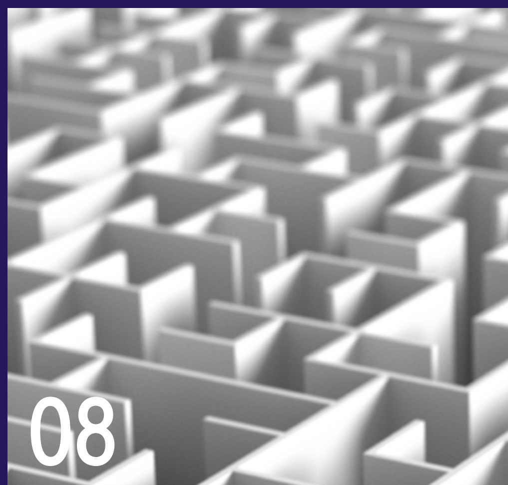


A WORD FROM OUR CHIEF INVESTMENT OFFICER

The financial media, as it does time and again, is focusing on the negatives. The vote to leave the EU is a perfect example because it provides easy pickings for anyone whose 'glass is half empty rather than half full'.

Despite predictions of doom and gloom, investment markets recovered from kneejerk reactions on the day the decision was announced, and as of the end of June all of our funds have been in positive territory over 1, 3 and 6 months. These funds represent the bedrock of our new True Potential Portfolios, described in detail throughout.

Further good news is that, despite concerns expressed across the media ahead of and after Brexit, our clients have been buying, not selling, thus the message about investing long-term is being listened to.

We told you in our Spring Edition that we were excited that our True Potential Portfolio proposition had grown rapidly to over a half of a billion pounds. That figure has now accelerated and is on track to exceed one billion by the end of the summer. The Portfolios are part of the £1.9bn of client money invested in True Potential's own funds which means we are strongly positioned to continue to use our scale to engage with some of the best managers in the world.

Our positive story is in stark contrast to what has happened recently to retail investors trapped inside illiquid property funds. We are dismayed that investors searching for a better income, and attracted by high property yields, did not understand that property is also a very illiquid asset.

One of the primary reasons we pursue multi-asset investing is that it contains multiple layers of diversification across deep and highly liquid markets, and this wide diversification facilitates flexible access to savings when needed. For our income investors, we offer two Income Porfolios built on our multi-manager, multi-asset model foundations.

As you read through True Insight you will find our own investment views alongside the views of the managers with whom we partner. Our partners have operations spanning the globe; cumulatively they manage assets in excess of £4.5 trillion, so what they have to say is worth paying attention to.

They each have different investment styles and on this occasion we highlight a style of investing based on momentum. In a special feature article, we look at how, and just as importantly why, momentum works well. Our feature article includes a contribution from David Hollis of Allianz Global Investors who is an expert in this field.

> It is our mantra to be unique and by blending different styles of investing in our Portfolios we are extending the benefits of diversification beyond geographic boundaries and beyond asset classes like bonds and equities.

In this new world of low interest rates, saving for the future is of highest importance. If savers cannot generate an income from their investments, it is increasingly necessary to spend capital accumulated over time.

Of course we cannot know what conditions will be uppermost in minds in 5, 10 or 20 years, but diligently saving, paying attention to costs and seeking adequate diversification will, in our opinion, provide investors with greater flexibility in the choices that they will be able to make later in life.

Colin Beveridge, Chief Investment Officer.

REVIEW OF THE MARKETS Q2

Towards the end of the second quarter of 2016 we saw a pivotal event unfold - the UK public voted to leave the European Union. In the run up to the result, countless observers expressed their opinions with predictions mostly in favour of a remain vote.

As this proved to be incorrect, the immediate reaction by markets was generally negative in the aftermath.

During Q2 2016, despite the initial negative Brexit reaction, markets ultimately performed well for UK domestic investors.

Some lower risk asset categories, such as Global Bonds (not listed in our table below but included in the funds) produced double digit returns in Sterling terms.

Equity returns were also positive in Sterling, with US Equities being particularly strong as the value of the pound fell heavily against the US Dollar. In essence, UK-based investors investing in international assets derived significant paper profits from Brexit.

Although it is difficult to conceive of anything more significant than Brexit for world markets, there were some other important developments already underway. In the months prior to Brexit, markets were behaving negatively and providing mixed returns.

We saw a rebound in the oil price and supportive monetary policy once again emerging from Central Banks in response to ongoing concerns about lack of growth, most noticeably from China.

There is no doubt over the quarter, market conditions were eventful. We have witnessed heightened volatility levels creating a challenging environment for investors.

We also had weaker economic data in the US, particularly in relation to job creation, and this started to turn the tide of opinion away from interest rate rises which hitherto, had looked imminent.

Therefore, even in the run up to Brexit, investors were becoming worried about a greater malaise surrounding growth in the world's most important economy and beyond. Thankfully, lower risk assets produced strong returns as investors went in search of additional protection to suppress their short-term fears.

This is commonly referred to as a 'flight to safety'. Corporate, Sovereign and High Yield Bonds all provided healthy returns over the period, with investors seeking a mixture of very safe fixed income instruments, like UK Gilts.

They also sought to invest more into fixed income instruments like High Yield Bonds that contain a much greater risk of default than a government bond but are still considered safer than equities; the added advantage being a higher income.

The current market environment continues to be one that is very challenging for market participants. Investors will likely continue to focus on the short-term negatives, but our managers will latch onto any opportunities that will undoubtedly arise.

Table 1: Market Movement, Q2 2016.

Category	Local Currency % Change (3mth)	GBP % Change (3mth)
UK Equities	5.3%	5.3%
US Equities	1.9%	10.5%
European Equities	-2.7%	2.7%
Japanese Equities	-7.5%	9.4%
Asia Pacific (Ex Japan) Equities	-0.7%	7.8%
Emerging Markets Equities	-0.3%	8.1%
UK Bond Index (10 years)	5.6%	5.6%
Oil Price	19.1%	29.2%
CRB Commodities	12.9%	22.5%

Source: Bloomberg, 30 June 2016

INVESTMENT OUTLOOK

In our latest round of discussions with our fund manager partners there were some interesting opinions expressed about the markets. We have listed the key insights below:

- Our fund manager partners are currently reassessing the economic outlook. In general, they see more reasonable market conditions and the potential for economic growth led by the US economy, but have expressed near term concerns about uncertainty in Europe and Japan. However, they have also started talking about prospects of coordinated fiscal expansion plans as an antidote to austerity.

- Property has been in the news over the last few weeks with many Property funds closing to redemptions and have been writing down asset values. Overall, our managers have little exposure to direct property compared to the wider market. Where we have exposure it is more globally orientated. None of our fund manager partners believe there will be contagion from the commercial UK property market into global markets.

- The outlook for equity investing in the UK has featured heavily in our monthly calls with our fund manager partners, with many increasing their allocations to this area. They are concentrating on the FTSE 100, large capitalisation companies with an International bias, but there is a sense that this area has started to factor in too much of a positive outlook too quickly.

- The US stock market is an area that is drawing mixed reactions from our fund manager partners with some managers feeling that a number of companies have very high valuation. Other managers feel that this premium rating is justified with US economic fundamentals being so much stronger compared to other areas, and the one area that they do agree on is that they still see potential for more growth across the US economy.

- Japan has come back very much in focus with our managers having mixed views on whether to invest or not. The potential for a new, higher level of economic stimulus has attracted some of our managers to invest. However, other managers feel that Japan's economy is structurally flawed and will struggle even with a new level of fiscal stimulus to aid the monetary stimulus that has thus far had limited effect.

- Investment into Europe has divided opinion. On the one hand valuations are attractive, but at the macroeconomic level there is a growing sense that Europe will suffer more than the UK in the aftermath of Brexit. A lot depends on how Germany decides to act in the months ahead. There is pressure on them to sacrifice running a net surplus versus their EU partners.

- Government bonds continue to be a large feature of many of our fund manager's portfolios mainly being held as a form of portfolio insurance or as a proxy for cash, rather than being held for their yield. There is little doubt that our managers are asking themselves if overpaying for safety is a sensible course of action so they are looking outside of government bonds to corporate credit and actively managing duration risk. Meantime, inflation remains very muted which helps underpin the low yields currently in existence.

After consolidating the information gathered from our manager interviews, we assess what this means for our True Potential Portfolios. Ideally, we reflect as many of these ideas as possible through the fund allocations in each Portfolio. Alongside this, we remain focused on our four optimisation factors (risk, cost, expected return and risk-adjusted return) – as they help ensure an objective and systematic approach right across our Portfolio range.

To illustrate the allocations, we provide a monthly factsheet for each Portfolio. This is where we document changes to the Portfolio's composition and explain the reasons behind our actions. On the next few pages, we feature a number of key market, technical and fundamental indicators.

NAVIGATING THE MAZE POST BREXIT

When writing the Spring edition of True Insight, voting on Brexit was underway. Expectations favoured a vote to remain, however, we pondered the possibility of a vote to leave.

Ahead of the outcome, we suggested that a multi-asset approach would be the best way to navigate through the maze.

This opinion was based on our belief that diversification is important for investors facing uncertainty.

Looking back at the period after Brexit, we now know that our faith in multi-asset investing was warranted. Since Brexit, markets have rallied and many investors have been significantly rewarded. Now the die is cast and leaving the EU has been mandated by the people, we have to consider what happens next.

Of course, to suggest that we have a crystal ball giving us all the answers is absurd, so we asked ourselves what can we say that is reasonable and not based on emotion?

Where to begin?

When investors feel uncertain, financial commentators peddle bad news. Currently, there is wide-spread speculation that the fall in the value of the pound, will push up the price of imported goods and that this will negatively affect household budgets.

In a similarly negative vein, there are worries that residential house prices will fall and that the recent decline in commercial property prices is an example of what is to come.

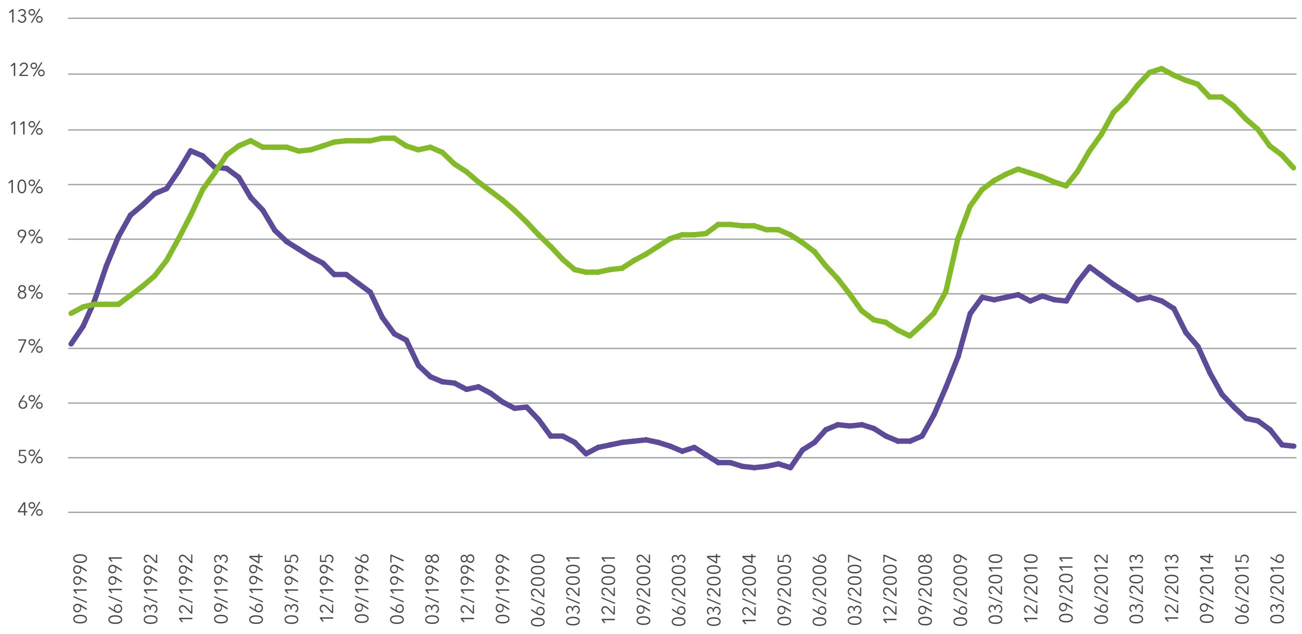
When examining the outlook, we put a little more faith in human ingenuity and believe that hard facts provide a better way of assessing what the future holds in store. We start with a perceived threat to jobs because this is probably the greatest worry faced by savers and families. One of the best ways of ensuring future prosperity is creating the right environment for employment conditions to thrive. Giving people jobs and paying them decent wages is a fundamental requirement for a successful economy. Employment facilitates an ability to save and savings in a competitive economy, with a well-functioning financial system, equates to investment.

At True Potential we have doubled our workforce, continuously investing in technology and funding research in to the saving and spending habits of the nation in our 'Tackling the Savings Gap' campaign.

An anecdote of our circumstances is not the whole story, but when we look at the wider picture on jobs (UK vs the Eurozone), shown in Chart 1 the picture on unemployment is much better for us here in the UK because the UK Government embarked on a programme of economic recovery following the credit crisis in 2008.

NAVIGATING THE MAZE POST BREXIT

Chart 1: UK vs Eurozone Unemployment from 1990 Onwards



Source: Bloomberg and Office for National Statistics, 31 March 2016

In the current economic cycle commencing after the 2008 credit crisis, UK unemployment peaked at 8.4%. As of 31 March 2016 this was 5.1%.

While the unemployment rate may be too high for some, the contrast with the rest of the Eurozone is very telling. Unemployment in the Eurozone (10.3%) is more than double the rate here in the UK and the disparity gives a strong hint that the EU experiment is not working for many countries. This in turn can create a sense of injustice amongst citizens in the countries that are worst affected.

Ironically, the lowest unemployment rates can be found in countries like Norway (2.9%) and Switzerland (3.3%), both not member states of the EU.

Within the EU member states, Denmark has bucked the trend with an unemployment rate of 3.5% but the other major economies all exhibit stubbornly high unemployment – France (10.2%), Germany (6.1%), Italy (11.6%) and Spain (21%).

The positive differential between unemployment levels in the UK versus the Eurozone started way back in the early 1990s. It is perhaps coincidental, but those with long memories will recall that in September 1992 the UK was forced by markets to exit the Exchange Rate Mechanism (ERM): After a period shadowing the Euro with a fixed exchange rate, interest rates were hiked ever higher, eventually reaching double figures to support the pound. Inevitably the 'currency peg' against the Euro was abandoned and the pound collapsed.

In the early 1990's, we had dire predictions of doom and gloom with massive job losses forecast across the financial sector. While the economy did suffer for a period, and unemployment rose, the UK economy went on to recover strongly.

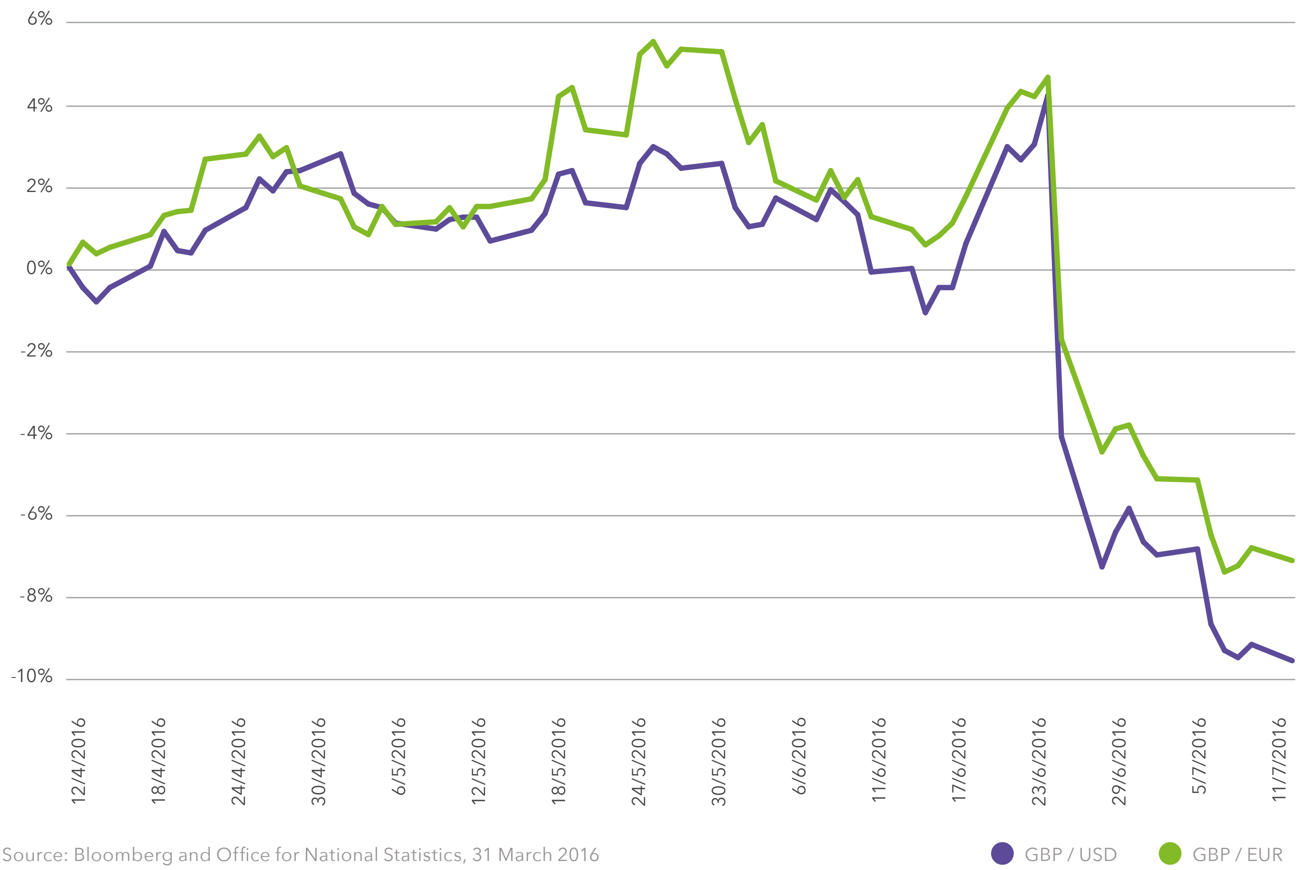
Moreover, against all conventional wisdom and expert predictions at the time, the financial sector went on to create more jobs than it lost and rose to a position of dominance globally.

Of course, the doomsters say the situation in the 1990's is very different to Brexit today, but will the experts be wrong again?

In the UK there is talk of cuts in Corporation Tax and an end to austerity measures as the requirement swings back to growth and away from deficit reduction. Introducing stimulatory fiscal measures as well as the monetary measures promoted by The Bank of England should help facilitate job creation. Hopefully this will assuage fears going forward. Perhaps the most significant manifestation of raised anxiety is what has happened before and after Brexit to the value of the pound.

In chart 2, we can see that it has fallen sharply against both the Euro and the US dollar.

Chart 2: Exchange Rate – Pound vs USD and the Euro



Source: Bloomberg and Office for National Statistics, 31 March 2016

Clearly, a long-term strategy that relies on protracted currency weakness is not a great strategy, but a sudden devaluation can have a stabilising effect in the short-term by helping to offset trade tariffs that might be levied if we have a 'hard Brexit' event, 'soft Brexit' event or something in the middle.

The reality is that the UK has shed much of its historic reliance on manufacturing relative to its role in the world, and the pound has lost much of its purchasing power versus its major competitors over the long-term.

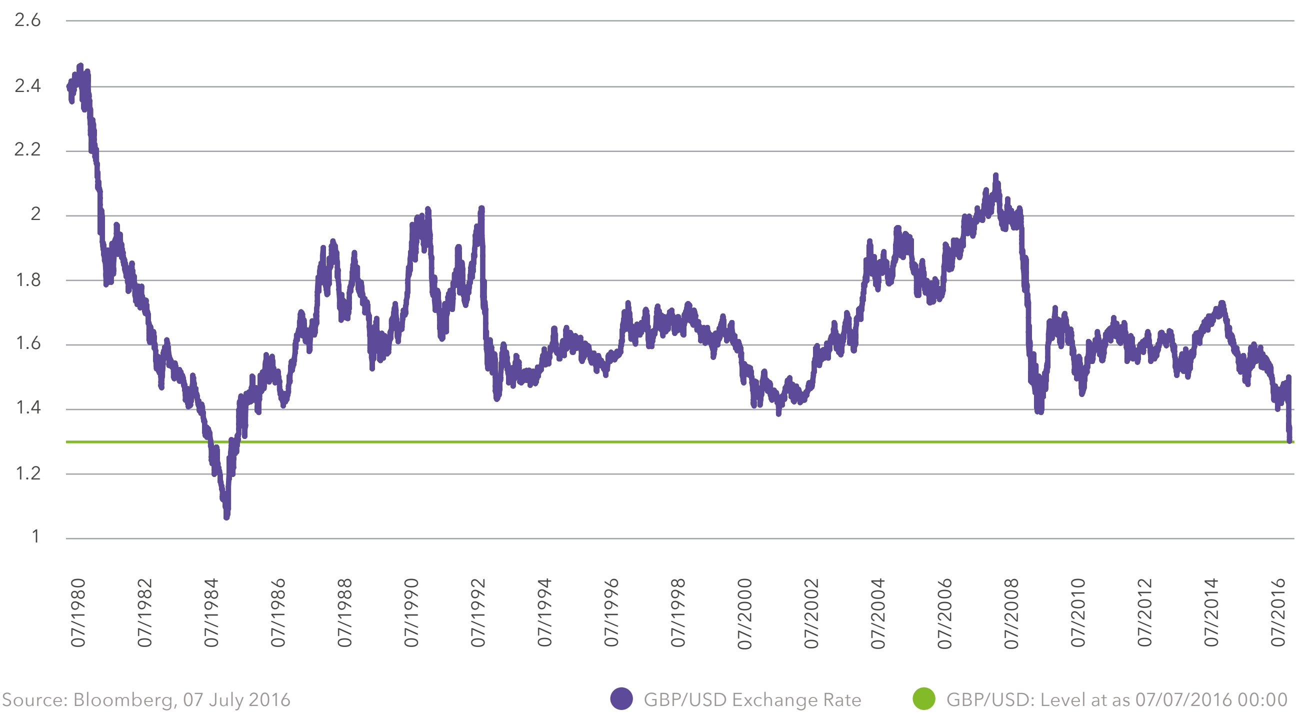
Yet for most ordinary citizens during the period of decline depicted in Chart 3 below, standards of living have not collapsed and in fact for many they have improved immeasurably.

So where are we today in relation to future trade negotiations?

Economists are lining up to say that the recent devaluation of the pound will a) cause inflation to rise to 2.2% in 2017 and 2.4% in 2018 and b) export businesses benefiting from a cheaper currency will not benefit from increased trade because of uncertainty about the terms of trade with all 27 EU member states.

However, when you look at Table 2 you can see that as of 2015, imports from all 27 EU countries was over £218 billion whereas exports accounted for a much lower sum of £133 billion, leaving a deficit of over £85 billion. Interestingly, the top 5 block countries that the UK sells goods and services to accounts for 70.3% of its total EU exports and 67.9% of total EU Imports. This suggests that bi-lateral agreements on a most favoured nation basis will be in the interests of all parties in the forthcoming negotiations.

Chart 3: Sterling and Dollar Exchange Rate



Source: Bloomberg, 07 July 2016

Table 2: 2015 Annual UK Trade with EU (£m)

Country	Exports	Imports	Trade Balance
Germany	£30,352	£60,679	-£30,327
France	£17,830	£23,999	-£6,169
Netherlands	£17,338	£30,890	-£13,552
Republic of Ireland	£16,665	£12,509	£4,156
Belgium	£11,576	£20,4070	-£8,894
All 27 EU	**£133,365**	**£218,667**	**-£85,302**

Source: HMRC, Overseas Trade Statistics 2015

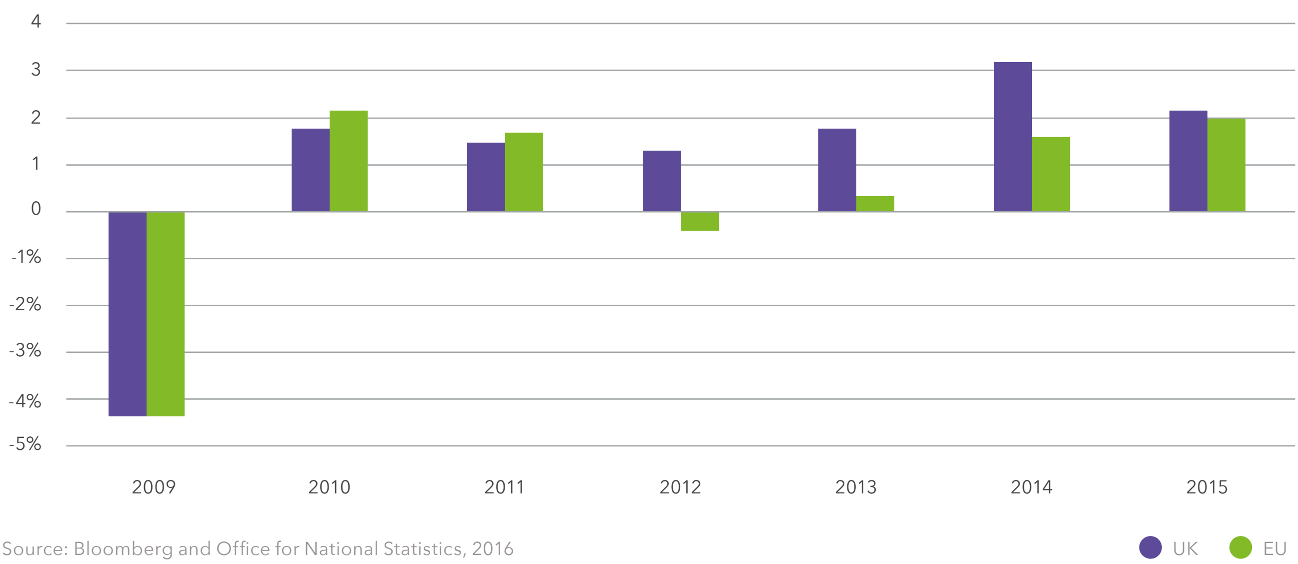
What about future growth prospects?

The Eurozone economy has now started to recover but many EU countries are weighed down by lack of job creation and banking systems toiling under the weight of poor loans.

Although UK growth rates are converging with the rest of Europe, as shown in Chart 4, the fact is, the EU is having to accelerate its use of unconventional monetary measures.

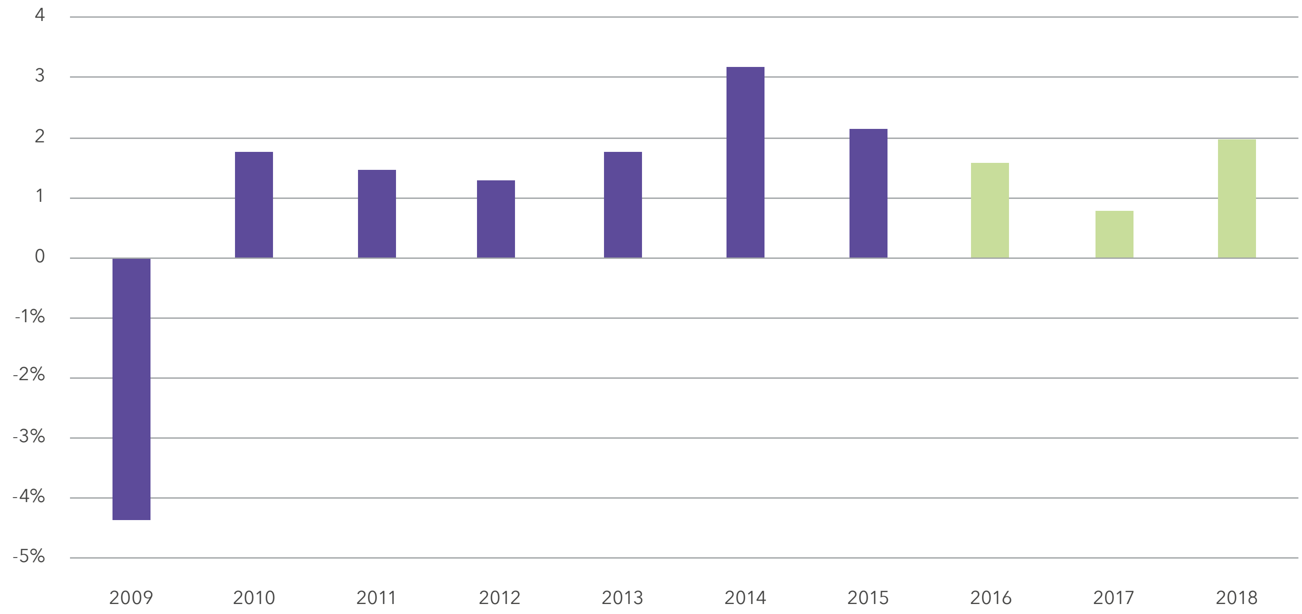
Looking ahead, the latest set of forecasts probably carry the least amount of certainty. Shown in Chart 5 on page 14, they are now predicting that the UK's rate of growth will slow until 2017 but it is interesting to note that they are forecasting a recovery by 2018 which is something you probably haven't read in the newspapers.

Chart 4: UK vs EU Real GDP Growth



Source: Bloomberg and Office for National Statistics, 2016

Chart 5: UK GDP Growth (2016-2018 Forecasts)



Source: Bloomberg, Contributor Composite, 30 June 2016

When looking ahead, we all have different ways of formulating our own judgements. For many people worried about Brexit they will most likely focus on day to day matters such as worrying about costs of living – will food bills rise, what will happen to fuel costs, etc?

People that travel will worry about constraints on travel across the EU and citizens that have shifted their domicile from the UK to the EU will worry about what changes to the rules will mean to their ability to live and work in the country they have chosen.

Britain also has some very pressing constitutional matters internally to resolve, such as Scotland voting to remain, along with London, Northern Ireland and Gibraltar.

As mentioned previously, citizens will worry about the value of their homes and immediate job prospects. However, what matters most are the special attributes possessed by the UK. There is a long history of democracy and adherence to the rule of law.

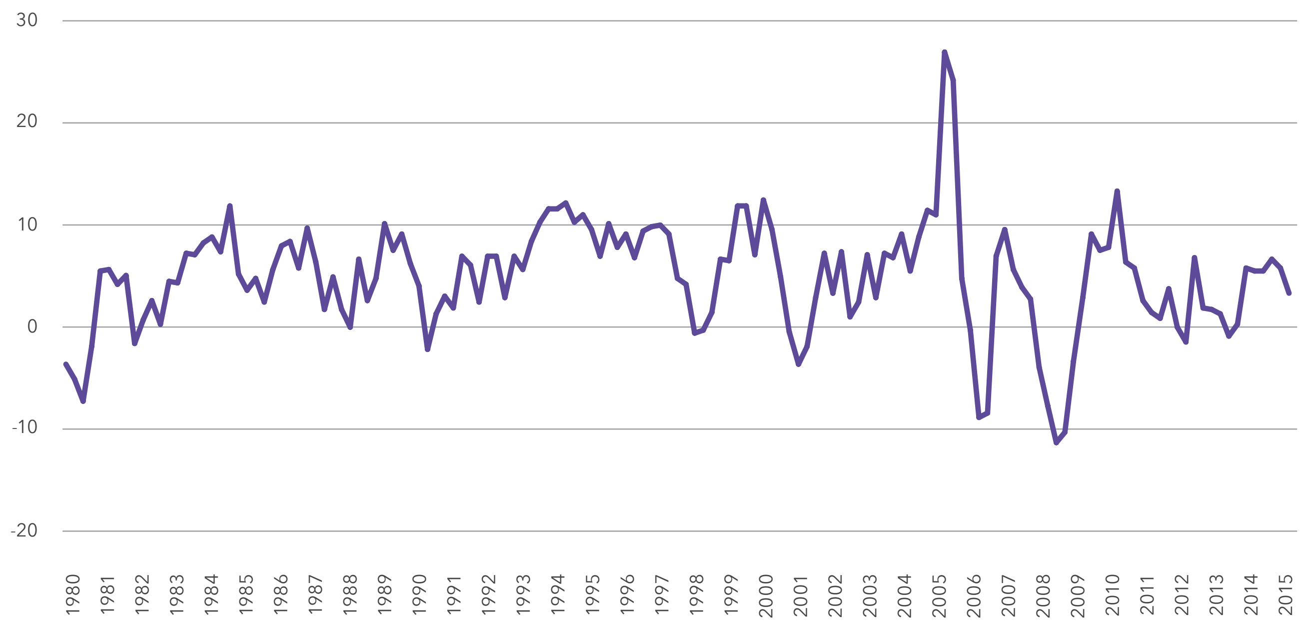
These factors may be less obvious, but they provide solid foundations. Yes, Brexit has shaken up the political establishment and political recriminations have been the order of the day, but this is the natural order of change.

In our opinion, the UK retains a very important stake in its trading relationships with the rest of the world and this will continue, but not as before. In some instances it will be for the better and in others for the worse.

As long as the UK Government invests in education and deploys capital intelligently into enterprise, the UK economy will be well positioned to grow and prosper.

In our final chart (Chart 6), we show just how much exports have fluctuated historically. We are certain that fluctuations will continue, and remain hopeful that the direction of travel will be upward as we continue to look outward!

Chart 6: UK Exports (Year on Year Percentage Growth)



Source: Bloomberg and Eurostat, 31 March 2016

Conclusions for Investors

The current post-Brexit situation is confusing for the ordinary investor. We suggest leaving the figuring out to professional fund managers to decide the best way forward. They have successfully managed through the Brexit period, acting sensibly and taking quick action when needed. The reality, always, is that in the months and years ahead some professional managers will be more successful than others.

This is why we partner with more than one fund manager, partnering with eight industry leading names in our Portfolios to ensure we smooth out manager variations in performance.

Moreover, our distribution capability reaches out to savers using cutting edge technology helping to enable greater flexibility, lowering the costs of investing and bringing new investment opportunities for you to consider.

Short-term market fluctuations shouldn't be off putting to investors. Instead, looking to the long-term and managing risk with a highly diversified investment strategy could give greater potential for growing your own financial wealth. Investing is not a one off decision, but a series of decisions tailored to your circumstances over time.

INCOME PORTFOLIOS

As the saying goes 'life is too short'. For example, we do not check the tyre pressure before every car journey because it takes too much effort and we retain faith in the robustness of the tyre.

For savers reliant on cash in the bank to generate an income, it has become all too clear, in recent years, that savings decisions should not be left to chance. Interest rates are at an all-time low and even the Regulator is becoming frustrated, pointing out that some banks are trapping investors in accounts paying virtually no interest, at all.

The difficult situation today, for savers, stems from the financial crisis, whereby central banks world-wide, and here in the UK, turned to extraordinary measures to lower interest rates as a way of stimulating economic growth.

The flip side is that investors looking for income are being encouraged to take more risk due to the low rates from cash savings.

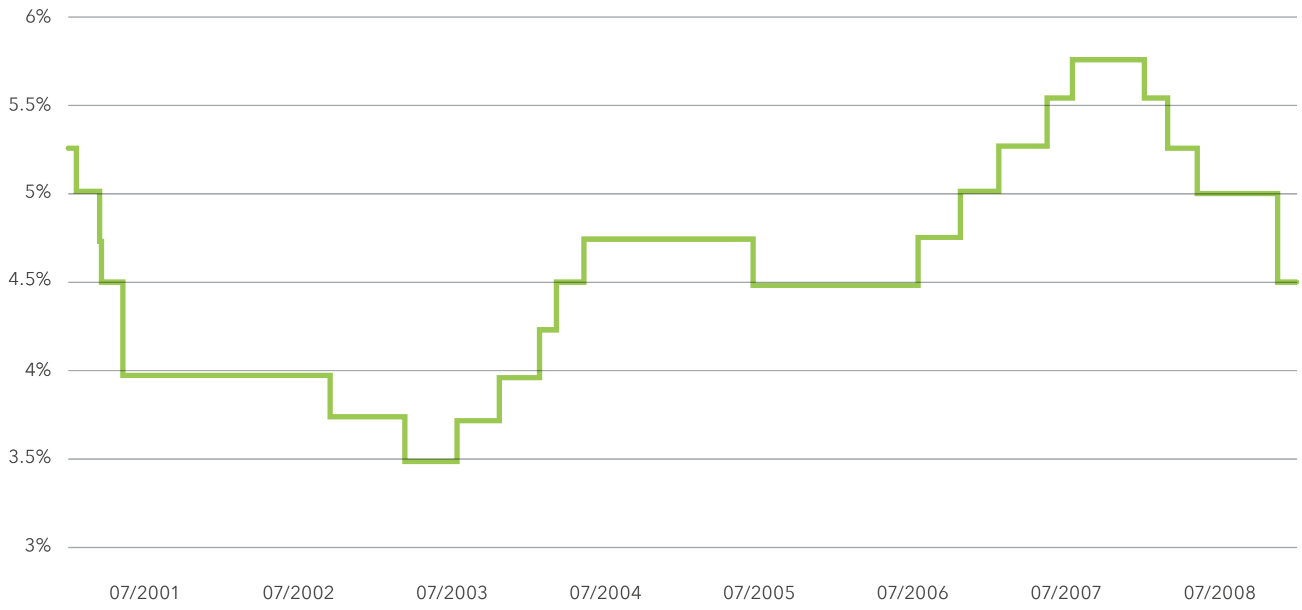
We can see why this is from Chart 7, showing interest rates on cash deposits (UK Base Rate) versus, the dividend yield on UK Equities. Historically, savers in the UK became accustomed to getting mid-single digit rates of interest on bank deposits as a way of providing a regular and safe source of income.

This is most apparent, when we look at interest rates between the years 2001 and 2008, shown in Chart 8. Over this period, interest rates ranged between 3.50% and 5.75%, providing a healthy return on cash invested in a bank deposit.

Chart 7: UK Interest Rate vs UK Index Yield

Source: Bloomberg, 06 July 2016

Chart 8: UK Interest Rate (2001 - 2008)



Source: Bloomberg, 30 June 2016

Higher rates allow depositors to benefit from compound interest. For example, after 17 years and 9 months a cash deposit earning 4% per year would allow someone to double their savings.

A mid single digit rate of return is normally attractive as a way of protecting against inflation. **However, the FCA have revealed that some savers are getting rates of 0.1% and for them, compounding will be of no help at all.**

Even worse, it will leave savers with no protection against inflation currently at 0.5%.

For the very fortunate receiving 1% you now only have to wait 70 years to double your money!

It is not surprising to us, therefore, that investors have been seeking other ways to not only safeguard their savings, but provide an adequate solution that maintains spending power later on in life.

Unfortunately, many alternative solutions go hand-in-hand with an increased exposure to risk. For example, recently, those who have invested directly into property funds, expecting good prospects of capital appreciation, alongside yields of 4%, may have found themselves exposed to the illiquidity of this asset.

This is obvious now, but even without the recent news on property funds, anyone contemplating selling their house, compared to selling shares, would understand that timing associated with each transaction is very different.

When selling shares, you get your money back after 3 days, typically. However, if you wanted to sell your house quickly, to get access to funds, what price do you think you would obtain if you were a forced seller? 10% less? 20% less? For a quick sale, the outcome could be much worse.

So, where should investors needing income turn their attention?

One possibility is Government Bonds. Unfortunately, yields have dropped to low levels. UK Government Bonds offer a form of insurance against risk, safety of capital if held for their full term, and are highly liquid.

In Chart 9, we can see that yields on Government Bonds have fallen from over 5% to a shade under 1%. In fact, the current yield of 0.94% is the return investors will obtain each year for the next ten years, if held to maturity. In the eyes of many, this is an unattractive return.

For investors prepared to accept higher risk and looking for income, Equities are a natural choice, with good levels of liquidity. Many investors have been tempted in to buying equities through passive investments called trackers. They track the yield on the FTSE 100 which contains larger companies that tend to pay bigger dividends.

However it is worth bearing in mind that more than 50% of the income comes from just ten companies which is what we call risk of concentration.

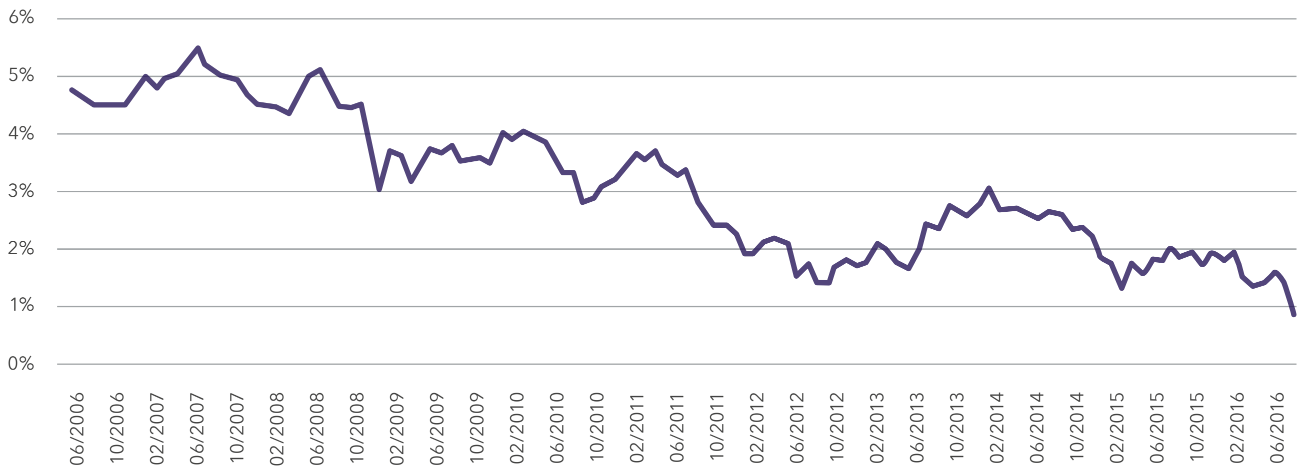
If one or two of these companies stop paying dividends, it would have a big effect on income and would most likely have a poor effect on the capital value of these shares.

One of the solutions True Potential Investments offer to clients is access to funds managed by our income managers, Threadneedle, Goldman Sachs, Close Brothers and Schroders, each with a distinctive approach to managing income. They manage income actively and spread their net very wide to include infrastructure assets, corporate debt, overseas investments and incorporate different investment techniques.

Without doubt, we are in a challenging phase for those seeking income. However, we have created two Income Portfolios that offer a solution for investors with a cautious and balanced attitude to risk.

Our Income Portfolios combine all our income funds to add further diversification. Investment via these Portfolios is spread over 19,000 holdings.

Chart 9: UK Government 10 Year Bond Yields (% trailing)



Source: Bloomberg, 30 June 2016

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.

In addition to increased diversification, we also actively manage portfolio costs - currently, 0.78% for Cautious Income Portfolios and 0.83% for Balanced Income with no additional management fee. By keeping costs low, we help optimise the amount of income delivered to our clients, and we even combine the Portfolios so that the income is distributed in a regular pattern.
As you can see the yields on each model are attractive and the performance of the models (which includes income) is attractive.

Table 3: True Potential Income Portfolios Performance

Fund	Yield	Performance*
True Potential Cautious Income	3.93%	7.78%
True Potential Balanced Income	4.07%	7.97%

Source: SEI, Custodian, 31 July 2016

*Performance figures are made up of 10 months actual performance from 1st October 2015 to 31st July 2016 and 2 months simulated performance from end of July 2015 to end of September 2015, prior to the launch of the Portfolios.

The simulated past performance has been calculated using the actual past performance of investments which are the same as those contained in the portfolios at launch. The simulated past performance assumes no change in asset or fund allocation.

We are looking forward to sharing twelve months of actual performance data with you in the autumn edition of True Insight.

You are able to view up-to-the-minute performance of your Portfolio 24/7 by logging in to your client site using your desktop, smartphone, tablet or smartwatch. This gives you a real-time snapshot of how your investments are performing, anytime, anywhere.

NB:Launched on 1st October 2015

Past performance and simulated past performance are not a guide to future performance.

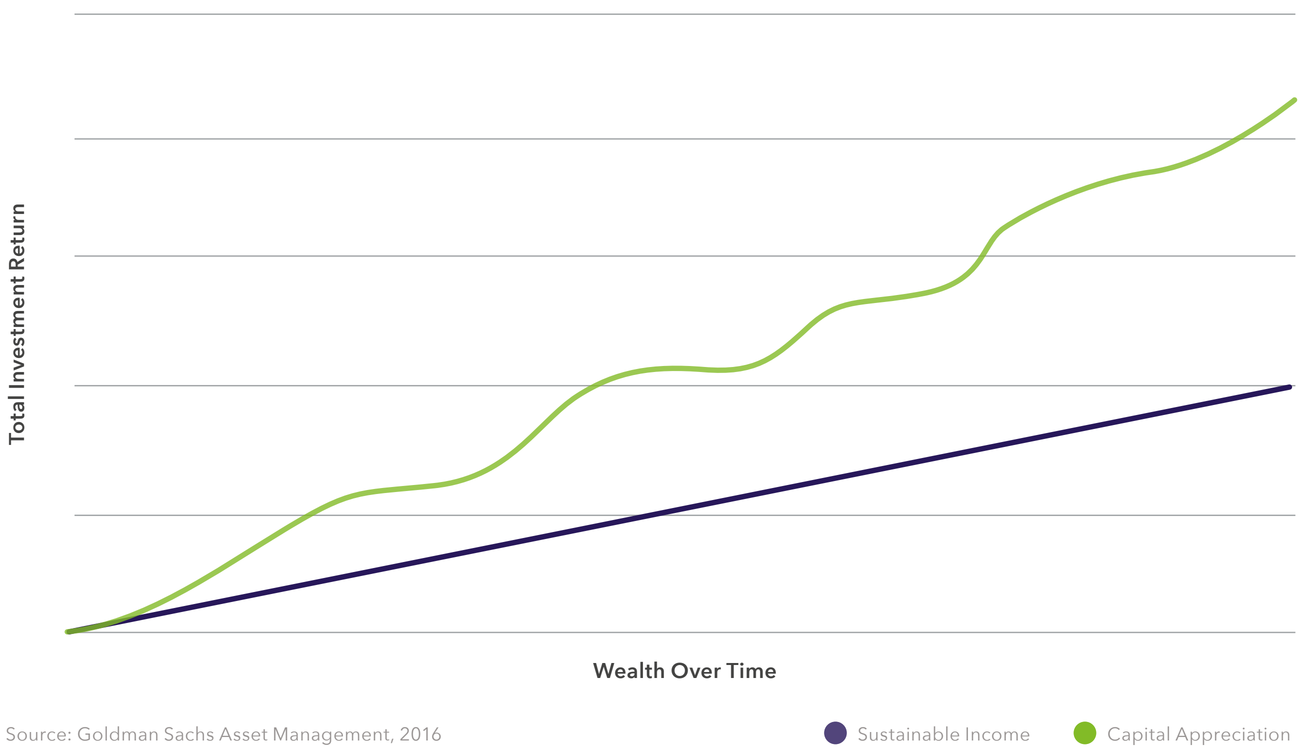
We have some additional thoughts to share with you on income.

First, we have been in discussion with our managers about their approach to seeking out attractive sources of income. We know they understand that reaching up for higher and higher yields reduces the likelihood of income sustainability. Secondly, the True Potential Portfolios, aim to deliver capital appreciation, alongside sustainable income, over the long-term.

We want to protect and grow your wealth and, at the same time, pay an income that will recur year after year.

Chart 11 illustrates how an investor can potentially receive both a growing income and capital appreciation from a sustainable income strategy.

Chart 11: Wealth Over Time (For Illustrative Purposes Only)



Source: Goldman Sachs Asset Management, 2016

OUR INCOME MANAGERS

Goldman Sachs

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.

COLUMBIA THREADNEEDLE INVESTMENTS

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.

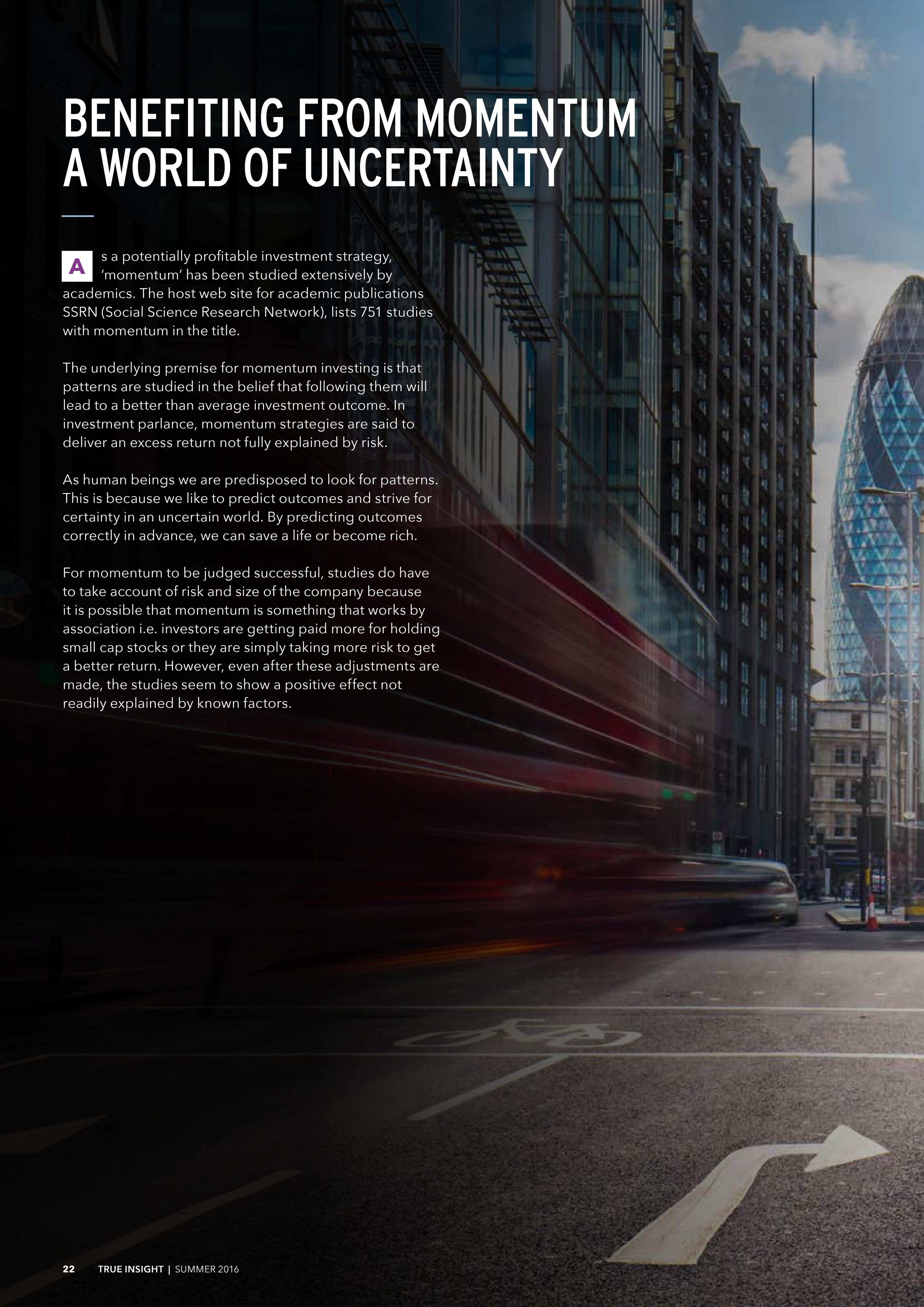
Schroders

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.

Close Brothers Asset Management

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.



BENEFITING FROM MOMENTUM A WORLD OF UNCERTAINTY

As a potentially profitable investment strategy, 'momentum' has been studied extensively by academics. The host web site for academic publications SSRN (Social Science Research Network), lists 751 studies with momentum in the title.

The underlying premise for momentum investing is that patterns are studied in the belief that following them will lead to a better than average investment outcome. In investment parlance, momentum strategies are said to deliver an excess return not fully explained by risk.

As human beings we are predisposed to look for patterns. This is because we like to predict outcomes and strive for certainty in an uncertain world. By predicting outcomes correctly in advance, we can save a life or become rich.

For momentum to be judged successful, studies do have to take account of risk and size of the company because it is possible that momentum is something that works by association i.e. investors are getting paid more for holding small cap stocks or they are simply taking more risk to get a better return. However, even after these adjustments are made, the studies seem to show a positive effect not readily explained by known factors.

The potential benefits from momentum are time-period sensitive, they vary according to regimes contributing to markets rising and falling.

Kent Daniel, who studied momentum crashes, points out that the effects are most extreme when markets rebound following a crash.

The precise point of danger for momentum investors is when markets have fallen and market participants expect the seriousness to escalate, but then the opposite happens. For example, between March 2009 and May 2009 when the market rose by 29%, after a very steep decline, the subsequent winners minus losers gained by 149%; winners rising by 156% and losers rising by 6.5%. Momentum investors must be aware of regime changes from extreme to normal and vice versa if they are to make profits.

A further study by Jagadeesh and Titman (2001) showed stocks that perform the best (worst) over a 3 to 12-month period tend to continue to perform best (worst) over the subsequent 3 to 12 months. The best performers appear to be no riskier than the worst performers and investors benefited from this strategy serially.

There are also a multitude of studies looking at company earnings (profits), studying the rate at which company profits change. The evidence shows that momentum across corporate earnings is pervasive.

Apart from how it works, one of the key questions surrounding momentum is why it works?

From an efficient market perspective, profiting from an historic pattern of price movements and corporate profit changes seems a bizarre idea because efficient market proponents argue that if 'anomalies' are spotted, and can continuously be exploited, investors will surely flock to these opportunities and compete away any gains to be had.

However, in real terms this seems not to happen, but why?

Lacking precise reasons, academics resort to explanations that latch onto human behaviours. Despite greater understanding of behavioural bias, investors seemingly continue to display bias allowing patterns to persist with a lead-lag effect.

Delong et al (1990) were the first economists to formulate the idea that irrational strategies could affect asset prices.

Other studies of cognitive behaviours include:

1. Conservative bias: Barberis et al (1998) and Edwards (1968) talk about conservatism bias. This is where investors underweight new information so prices slowly adjust.
2. Confirmatory bias: Barberis et al and Kanhneman (1974) talk about representative heuristics. The representative heuristic (in simple terms) is that individuals tend to extrapolate incorrectly and use confirmatory bias (look for information that suits their point of view).
3. Over confidence: Daniel et al (1998) and Hong and Stein (1999) discuss overconfidence brought about by cognitive bias amongst informed traders. They attribute picking winning stocks to skill and picking losers is associated with bad luck.

Based on the various studies that have taken place, it is not surprising to us that many of our fund manager partners incorporate momentum into the management of their funds. Some use it more extensively than others with Allianz adopting it to the greatest extent. For this reason, we feature David Holllis' more detailed views on the subject.

David Hollis:

Momentum, as noted, is one of the few trading strategies still employed by many fund managers today, either subconsciously through behavioural bias, or in the case of our multi-asset strategies, consciously.

Within the True Potential funds where Allianz act as the Master Manager, momentum is the foundation of our investment process; as a result, we actively tilt the portfolios to the best performing asset classes through time. However, we recognise, as does much of the academic research, a pure momentum strategy results in returns that are highly negatively skewed as they experience infrequent, substantial, and sustained, negative returns.

To overcome these shortcomings, we include several additional elements to the investment process that are designed to hedge against such "momentum crashes" described above. Our calculation of momentum, whilst aimed at capturing the medium term trend in prices, is biased to the most recent observations.

This enables the allocation to react more quickly to sharp drawdowns in markets, particularly where momentum has been strong for a sustained period. Additionally, where asset class valuations have become excessively expensive, we reduce momentum driven overweight positions, where valuations are excessively low we re-enter the market by reducing underweight positions.

When measuring valuation, we do not utilise the symmetrical normal distribution, but prefer so-called "fat tails" distributions.

David Hollis, *Vice President and Multi-asset Portfolio Manager.* Allianz Global Investment.

Table 4: True Potential Allianz Fund Performance and Simulated Performance

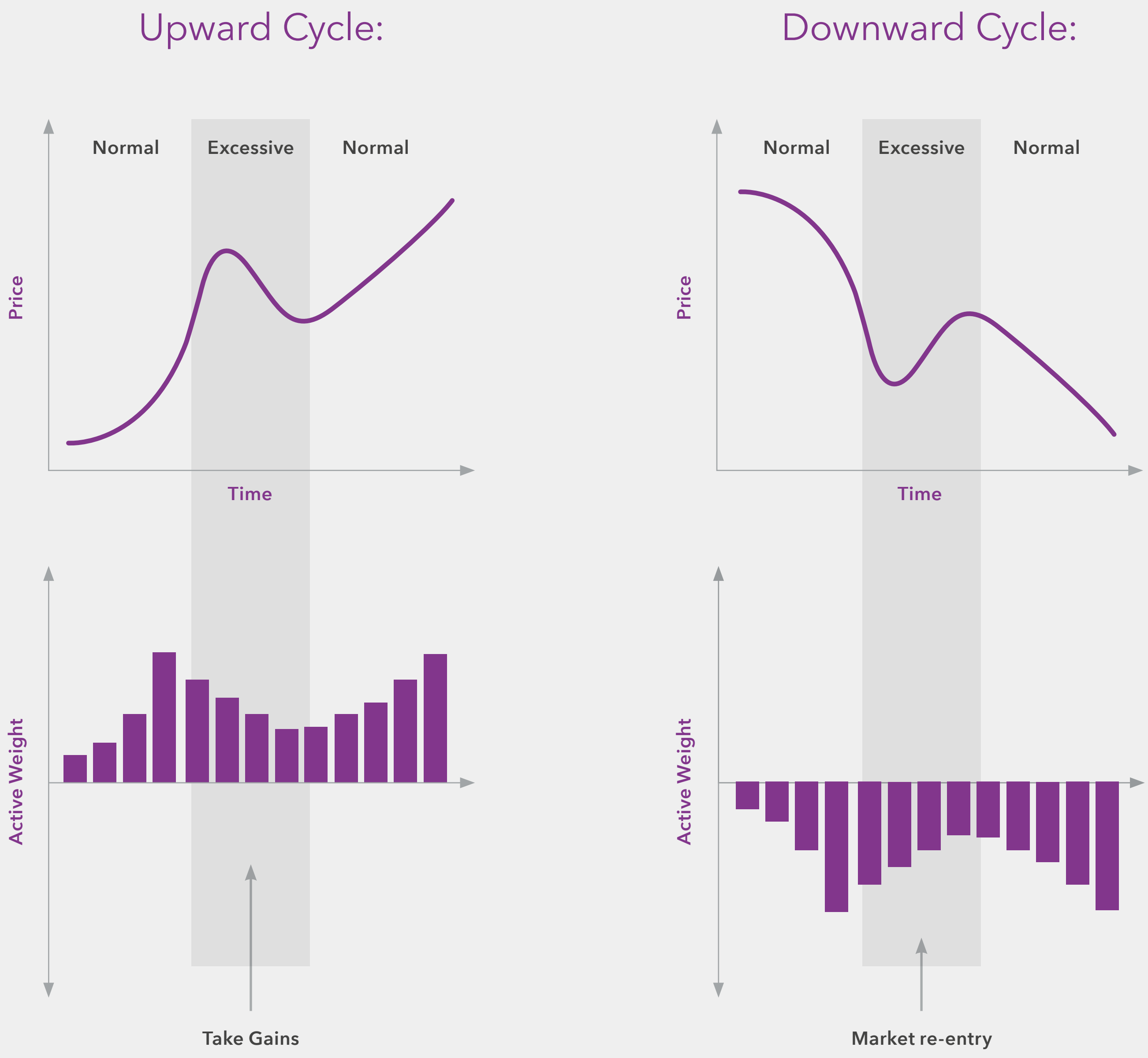
Fund	June 2012-2013	June 2013-2014	June 2014-2015	June 2015-2016
True Potential Allianz Cautious	8.35%*	4.82%*	2.33%*	8.33%*
True Potential Allianz Balanced	10.10%*	6.43%*	3.21%*	8.33%*
True Potential Allianz Growth	11.28%*	6.67%*	4.63%*	9.57%*

Source: Bloomberg, 30 June 2016. Simulated performance*

*Performance figures are made up of actual past performance from 1 January 2016 to 30 June 2016 and simulated performance from end of 1 June 2012 to 31 December 2015.

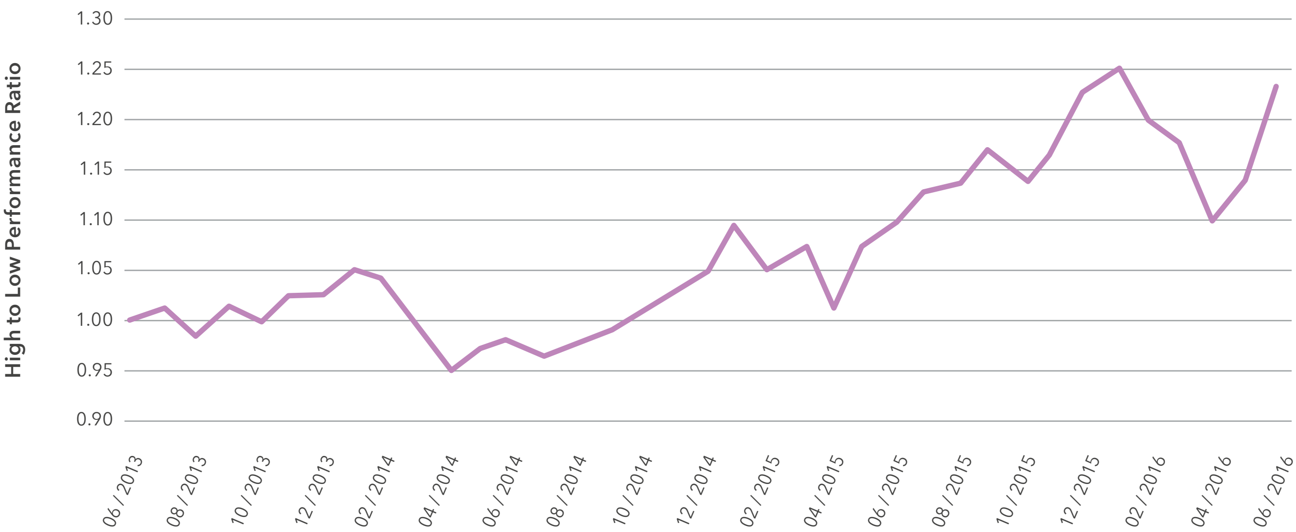
The simulated performance is based on the actual past performance of the Allianz RiskMaster Conservative (Cautious), Allianz RiskMaster Moderate Fund (Balanced) and Allianz RiskMaster Growth (Growth) funds which underlie the investments concerned. Past performance and simulated past performance are not a guide to future performance.

Charts: 12-13 Momentum Strategy



Source: Allianz Global Investor, 30 June 2016

Chart 14: MSCI World – Relative Performance of High vs Low Momentum Stocks



Source: SEI Asset Management and FACTSET, 30 June 2016

This process results in over, or under, valuation being identified more often, and is one of the reasons why multi-asset funds utilising this process outperformed during 2008.

The Great Financial Crisis defined in normal distribution terms was only a 4 standard deviation event, but utilising a "fat tails" distribution, the probability of such an extreme scenario was much greater and, therefore, portfolios were gradually de-risked throughout 2008.

The inclusion of such anti-cyclicality in the momentum process allows us to skew the risk-return distribution positively, avoiding the negative skew of a pure momentum approach.

To better pick turning points in momentum, as well as using quantitative signals, we incorporate a fundamental overlay into the investment process. This enables us to react far more quickly than via the quantitative approach.

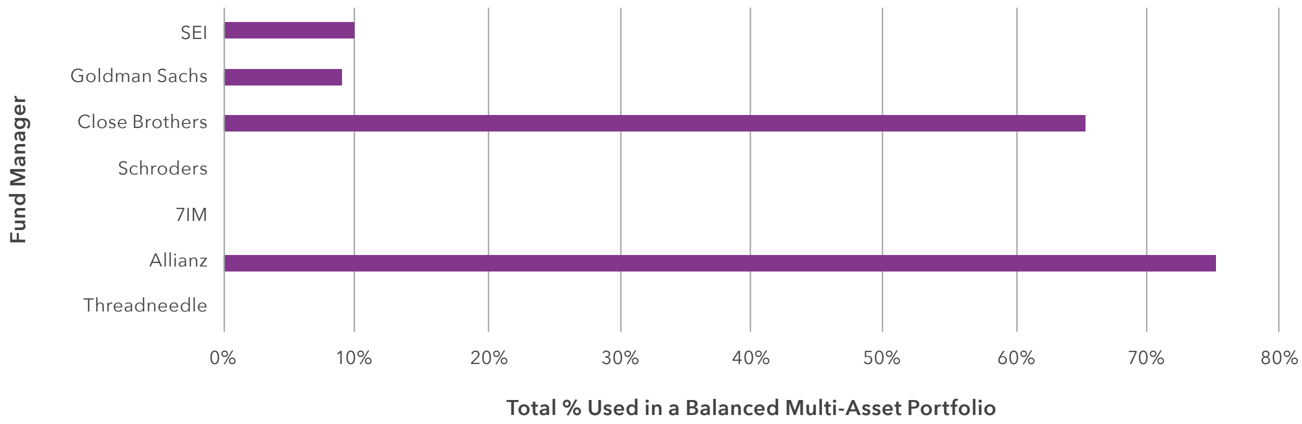
Academic papers cite the 1987 crash as one such example of a momentum crash, in such a circumstance there is a need for an immediate or even pre-emptive reaction. This can only really be implemented fundamentally, as any quantitative approach would take time to react and is unlikely to be forward looking.

We leverage the experience and knowledge of the multi-asset portfolio managers and economic strategists to produce a fundamental view on all asset classes, which is reviewed on a weekly basis and debated, internally via a forum, on a monthly basis.

This enables portfolio managers to incorporate fundamental views within the momentum process, and events such as Brexit, are a perfect example of why this is a necessary component of the overall RiskMaster strategy.

Judicious combination of momentum with anti-cyclical signals and fundamental positioning has resulted in a proven positive risk-return skew for funds employing this strategy.

Chart 15: Percentage of Momentum Used by True Potential Fund Manager Partners



Source: True Potential Fund Manager Partners, 30 June 2016

Comments about how other managers use Momentum:

Close Brothers use momentum as part of a risk monitoring discipline (for exit strategy i.e. selling) and as part of timing determination (for entry strategy i.e. buying) for investing in equities. For them, momentum is subordinate to fundamental valuation as well as qualitative company and industry assessments.

SEI use momentum in their equity allocation, both in their allocation to momentum managers as an alpha source, and as an input in their tactical allocation between managers. It is not a formal input in their allocation to fixed income, but both SEI and their underlying managers take advantage of market trends (i.e. momentum) and may choose to exploit them or avoid them (in a contrarian manner) at any time. Momentum is also used as an input alongside valuations, sentiment, fundamentals and macro-economics.

Goldman Sachs have momentum signals that incorporate both short-term and medium-term price data to measure trends in equity, fixed income and currency markets.

Their Dynamic fund uses Strategic Market Indicators to adjust weights to trend (momentum) over time.

Conclusion:

The idea that past price returns can predict future returns needs careful consideration and is best deployed in the hands of professional fund managers.

For example, a number of studies are based on zero-cost whereas transaction costs are borne by the investor. Momentum is also highly skewed, subject to crashes which can wipe out previous gains in an instant, and these events are hard to predict.

Charlatans who rely on investor's predilection for believing in patterns use different techniques to deceive investors.

A common trick is to show stocks with one particular set of pattern-related characteristics, email the results to a set of clients and then pick stocks with the exact opposite characteristics and send to another group of clients half will be spectacularly right and half will be horribly wrong.

Being aware of the pitfalls, as well as the benefits, is essential to exploiting momentum profitably. Our strategy managers use momentum as an aid to decision taking. It can aid diversification because it can be deployed in both falling and rising markets and they can do so quickly and efficiently.

THE SCIENCE BEHIND OUR PORTFOLIOS

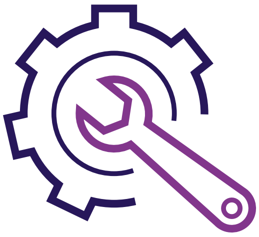
How we optimise the Portfolios

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

For example, we offer seven funds within the Balanced category, therefore if no preference was given to one fund over another, an equally-weighted allocation to each fund is 14.3%.

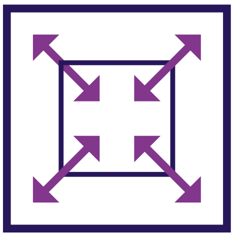
When we build our True Potential Portfolios, we tactically allocate away from the equally-weighted portfolios aiming for lower volatility, lower cost, higher expected return and a better risk-adjusted return than could be expected from choosing an equal allocation.

	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									✓	✓



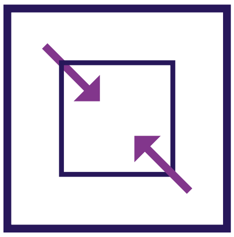
Risk (Portfolios)

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.

SERIES SPOTLIGHT: TRUE POTENTIAL PORTFOLIOS

Each True Potential Portfolio contains all of the funds available within its risk category.

The Portfolios in 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.

	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	0.82%	0.81%	0.89%	0.91%	0.92%	0.94%

	Growth	Growth equally-weighted	Aggressive	Aggressive equally-weighted
Cost	0.86%	0.86%	0.85%	0.86%

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.

Asset Allocation

Asset Class	Defensive	Cautious	Balanced	Growth	Aggressive
UK Equities	6.6%	14.4%	18.6%	23.1%	26.2%
North American Equities	8.4%	15.0%	19.5%	23.6%	23.8%
European Equities	7.0%	8.4%	10.0%	10.7%	17.7%
Japanese Equities	1.2%	2.7%	4.5%	4.0%	5.3%
Asia Pacific Equities	0.4%	1.0%	1.6%	1.4%	1.5%
Emerging Market Equities	1.0%	1.5%	5.7%	11.4%	17.9%
Global Bonds	16.8%	9.0%	4.6%	1.9%	0.0%
Global Inflation Linked Bonds	2.4%	2.1%	1.7%	1.9%	0.0%
Emerging Market Bonds	0.7%	2.7%	3.4%	3.8%	0.0%
Global High Yield Bonds	8.8%	6.5%	6.9%	5.3%	1.3%
UK Gilts	8.2%	9.9%	5.8%	3.5%	0.0%
UK Credit	3.6%	10.2%	6.2%	3.2%	0.0%
Property	0.7%	2.4%	2.3%	3.1%	2.5%
Commodities	1.5%	1.3%	1.2%	1.0%	1.5%
Cash	32.7%	12.9%	8.0%	2.1%	2.3%

Source: Smith & Williamson, 30th June 2016

Asset Class	Defensive	Cautious	Balanced	Growth	Aggressive
Equities	24.6%	43.0%	59.9%	74.2%	92.4%
Bonds	40.5%	40.4%	28.6%	19.6%	1.3%
Alternatives	2.2%	3.7%	3.5%	4.1%	4.0%
Cash	32.7%	12.9%	8.0%	2.1%	2.3%

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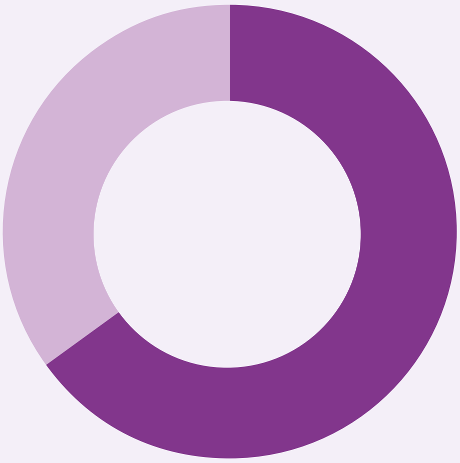
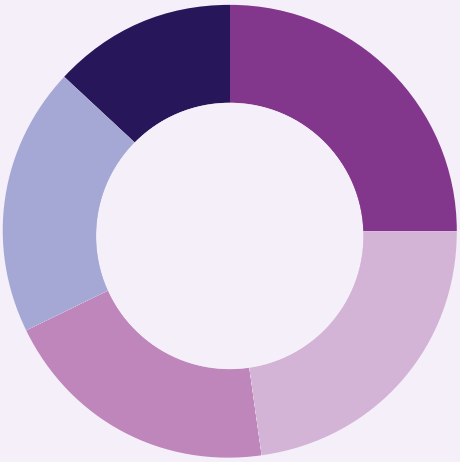


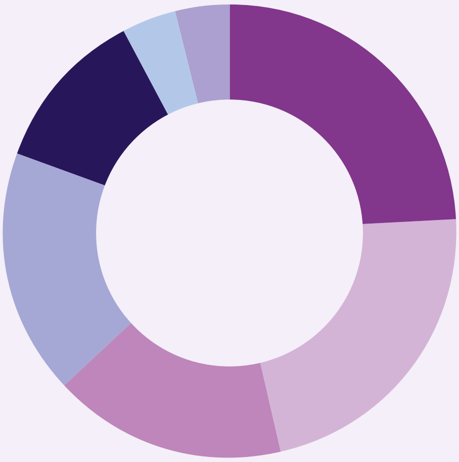
Defensive

Manager of Managers - SEI	65.0%
Actively Passive - 7IM	35.0%



Cautious

Manager of Managers - SEI	25.0%
Actively Passive - 7IM	23.0%
Directly Invested - Close Brothers	20.0%
Risk-Based - Allianz	19.0%
Fund of Funds - Schroders	13.0%



Balanced

Manager of Managers - SEI	24.5%
Actively Passive - 7IM	17.0%
Directly Invested - Close Brothers	16.5%
Risk-Based - Allianz	23.0%
Fund of Funds - Schroders	12.0%
Dynamic - Goldman Sachs	3.5%
Income Builder - Goldman Sachs	3.5%

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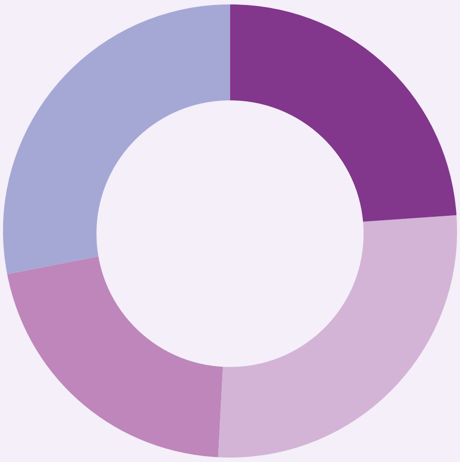

Growth

Manager of Managers - SEI	24.0%
Actively Passive - 7IM	27.0%
Directly Invested - Close Brothers	21.0%
Risk-Based - Allianz	28.0%

Aggressive

Manager of Managers - SEI	48.0%
Actively Passive - 7IM	52.0%

SERIES SPOTLIGHT: + PORTFOLIOS

Each Portfolio in the + group of Portfolios is more concentrated in its fund selection containing larger fund positions compared to its risk category equivalent 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. Optimising the Portfolios in the + category, we select from all of the funds outside of the Portfolio's respective risk category, which makes the task of optimising, across all factors, more attainable. We always aim to optimise across all factors where possible, 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	✓		

Volatility is likely to remain for sometime, as our fund managers are targeting value rather than growth. Those exposed to Emerging Markets have benefited over the past quarter, however conviction in this area remains low, especially in commodity areas. The table below shows a cost comparison between our + Portfolios and their equally-weighted equivalents.

	Cautious +	Cautious equally-weighted	Balanced +	Balanced equally-weighted	Growth +	Growth equally-weighted
Cost	0.87%	0.91%	0.87%	0.94%	0.85%	0.86%

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.

Asset Allocation

Asset Class	Cautious +	Balanced +	Growth +
UK Equities	11.6%	18.9%	22.8%
North American Equities	14.4%	22.0%	29.0%
European Equities	10.4%	10.3%	14.2%
Japanese Equities	4.0%	3.8%	5.5%
Asia Pacific Equities	0.8%	1.0%	0.9%
Emerging Market Equities	4.3%	7.0%	10.4%
Global Bonds	9.3%	6.3%	0.4%
Global Inflation Linked Bonds	1.7%	2.2%	0.1%
Emerging Market Bonds	1.0%	2.4%	0.0%
Global High Yield Bonds	6.0%	6.5%	0.7%
UK Gilts	7.0%	7.0%	9.2%
UK Credit	4.1%	3.6%	2.6%
Property	1.2%	1.8%	1.6%
Commodities	1.0%	0.6%	0.9%
Cash	23.2%	6.6%	1.7%

Source: Smith & Williamson, 30th June 2016

Asset Class	Cautious +	Balanced +	Growth +
Equities	45.5%	63.0%	63.0%
Bonds	29.1%	28.0%	28.0%
Alternatives	2.2%	2.4%	2.4%
Cash	23.2%	6.6%	6.6%

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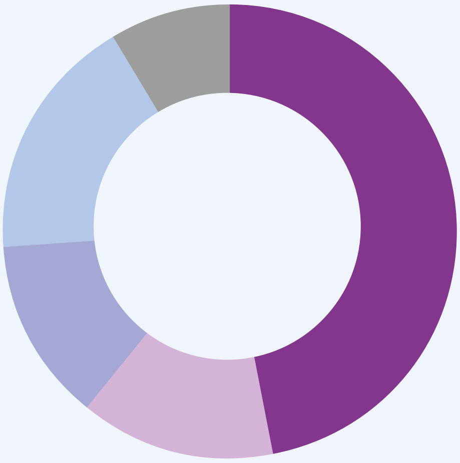
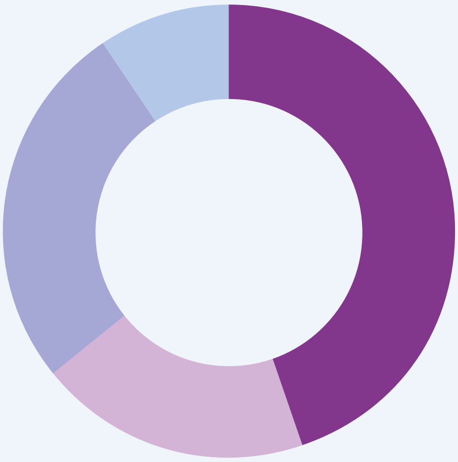


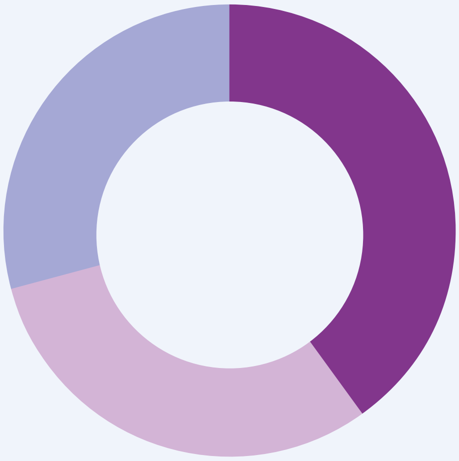
Cautious +

Manager of Managers - SEI	47.0%
Directly Invested - Close Brothers	14.0%
Fund of Funds - Schroders	13.0%
Actively Passive - 7IM	17.5%
Risk-Based - Allianz	8.5%



Balanced +

Manager of Managers - SEI	49.0%
Directly Invested - Close Brothers	21.0%
Actively Passive - 7IM	20.0%
Risk-Based - Allianz	10.0%



Growth +

Directly Invested - Close Brothers	40.0%
Manager of Managers - SEI	31.0%
Actively Passive - 7IM	29.0%

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SERIES SPOTLIGHT: INCOME PORTFOLIOS

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

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

Despite not being able to fully optimise both Portfolios, we are comfortable given we have optimised what we believe are the most important factors of risk and cost for both Portfolios.

During June, we altered the fund allocation within the True Potential Cautious Income Portfolio.

We increased exposure to the Goldman Sachs Income Builder Fund and we have reduced exposure to the True Potential Close Brothers Cautious Income Fund, primarily driven by the higher income level on offer from the Goldman Sachs Fund.

The Cautious Income Portfolio is currently yielding 3.88% and the Balanced Income Portfolio 4.16% with the equally-weighted Portfolio yielding 3.76%.

Source: Bloomberg, 31 March 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	0.78%	0.91%	0.83%	0.94%

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SERIES SPOTLIGHT: INCOME PORTFOLIOS

Asset Allocation

Asset Class	Cautious Income	Balanced Income
UK Equities	25.5%	35.0%
North American Equities	10.6%	12.1%
European Equities	6.5%	6.7%
Japanese Equities	1.3%	1.2%
Asia Pacific Equities	0.7%	0.6%
Emerging Market Equities	0.4%	0.4%
Global Bonds	11.1%	12.2%
Global Inflation Linked Bonds	0.6%	0.1%
Emerging Market Bonds	0.4%	0.6%
Global High Yield Bonds	11.4%	14.1%
UK Gilts	1.6%	0.6%
UK Credit	20.4%	10.0%
Property	2.4%	0.9%
Commodities	2.1%	0.4%
Cash	5.0%	5.1%

Source: Smith & Williamson, 30th June 2016

Asset Class	Cautious Income	Balanced Income
Equities	45.0%	56.0%
Bonds	45.5%	37.6%
Alternatives	4.5%	1.3%
Cash	5.0%	5.1%

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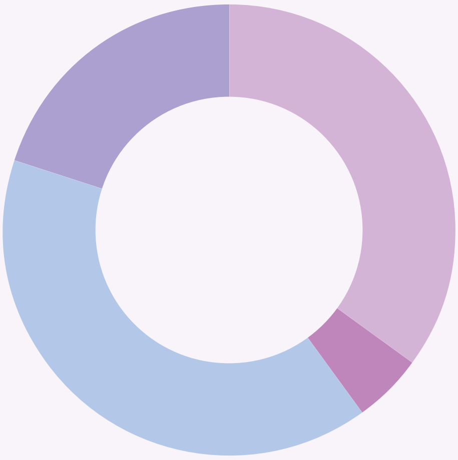
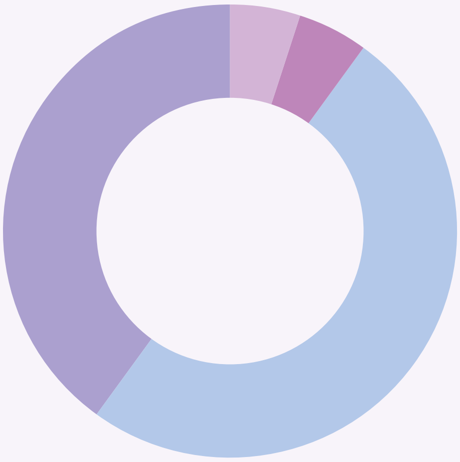


Cautious Income

Directly Invested - Close Brothers	35.0%
Fund of Funds - Schroders	5.0%
Dynamic - Goldman Sachs	40.0%
Income Strategies - Threadneedle	20.0%



Balanced Income

Directly Invested - Close Brothers	5.0%
Fund of Funds - Schroders	5.0%
Dynamic - Goldman Sachs	50.0%
Income Strategies - Threadneedle	40.0%

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.

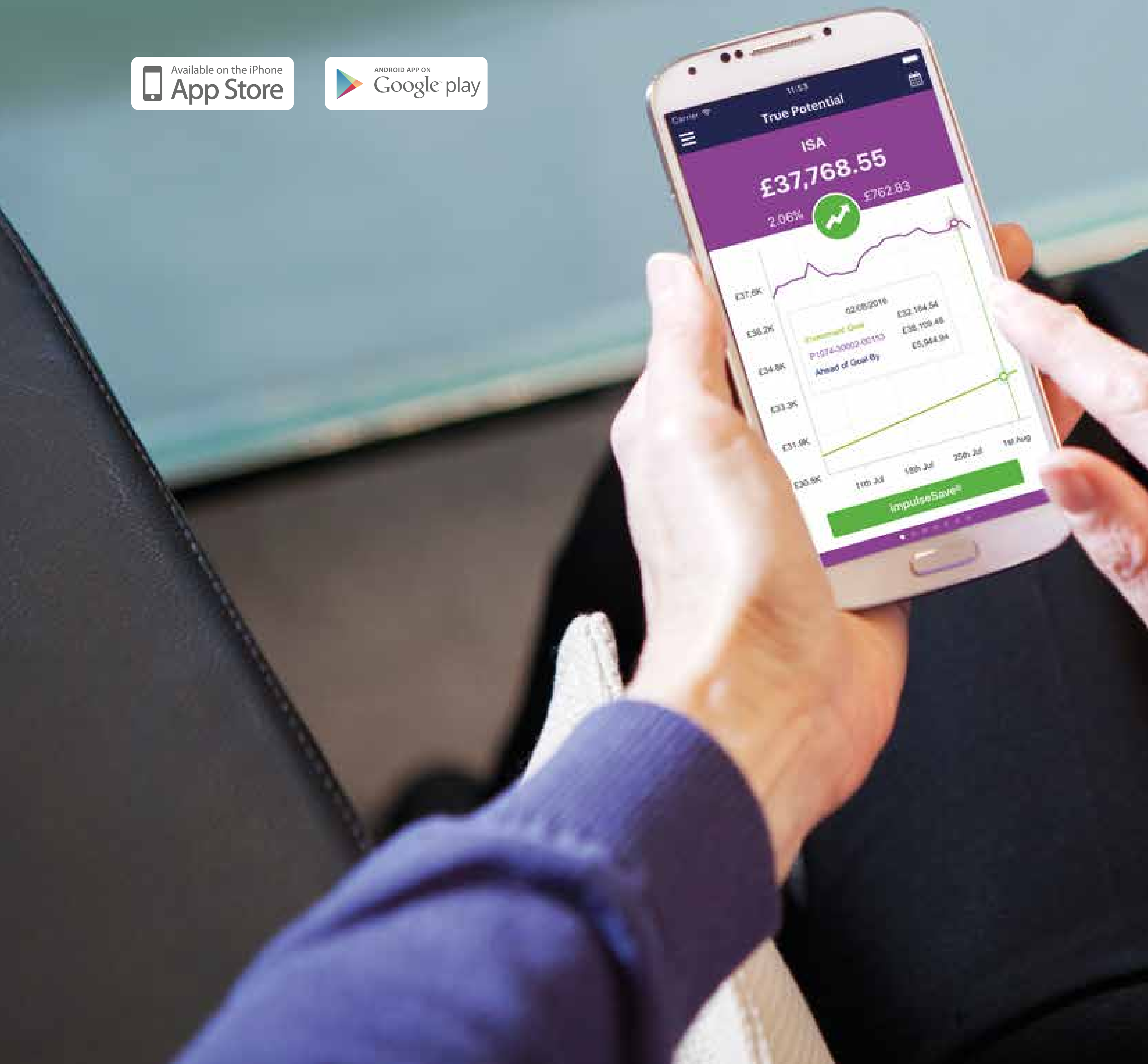
YOUR PORTFOLIO ON DEMAND

It's your money so we think you should be the first to know how it's performing. You can view your account from anywhere in the world 24/7, online or through our market-leading apps.

Log in to your personal client site at **tpllp.com/login** or search **'True Potential'** in the app store.

Available on the iPhone App Store

ANDROID APP ON Google play



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