

VIEWPOINT

Newsflash

A new month and the 137th issue of Viewpoint from **PPI Advisory**.

This document will be made available on our website www.ppi-advisory.com

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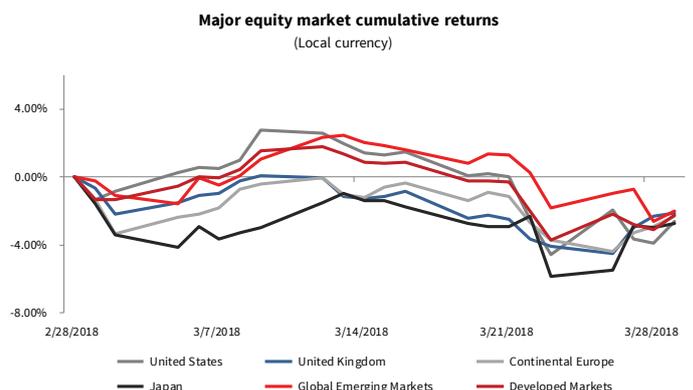
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Market Commentary

After a broad sell off across many asset classes in February, volatility continued into March, with equity markets declining and government bonds rallying. Risk markets were impacted by the prospects of a US-China trade war with President Trump continuing to push his ‘America First’ philosophy. Emerging market and developed market equities fell, with emerging markets marginally outperforming.

US equities fell 2.6% during the month, taking Q1 2018 returns to -0.9%. A key contributing factor seemed to be President Trump’s imposition of tariffs on imports of Chinese steel and aluminium and proposals for further tariffs on a wide range of goods. China immediately responded, imposing tariffs on several US imports, including wine. This led to worldwide concerns of a potential trade war, which could have implications for global growth. In addition to this, tech stocks, among the strongest performers in 2017, suffered sharp share price declines. This followed a serious data breach at Facebook which led to a series of governments seeking to tighten the loose regulation of companies in the sector, while tax authorities are seeking to impose more effective taxes.

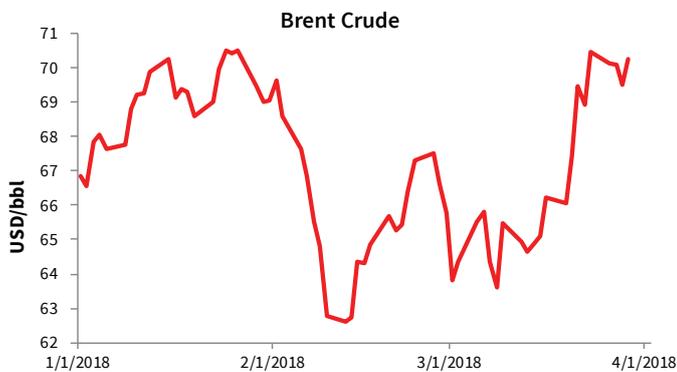
Figure 1: Equities decline in every major region



Source: Bloomberg, Momentum GIM

The concerns in the US were felt worldwide, with every major equity market falling. UK equities fell 2.1% in Sterling terms, with additional concerns regarding the path of UK interest rates, which are likely to rise more aggressively than previously anticipated. Asian equities also declined on the trade war concerns, with Japanese equities declining 2.7% and Asia Pacific (ex-Japan) equities falling 2.4%. Global developed market equities fell 2.2%, a sharper fall than the 2.0% decline in global emerging market equities. Despite the fall, emerging market equities still posted positive returns over the quarter, advancing 1.3% in US Dollar terms versus a 1.3% decline in developed market equities.

Figure 2: After hitting year-to-date lows in February, Brent crude recovered in March



Source: Bloomberg, Momentum GIM

The US Dollar continued to weaken, falling 0.7% on a trade weighted basis in light of a mixed domestic economic and political sentiment. Sterling performed particularly strong versus the US Dollar, rising 1.9%. As previously mentioned, this follows an increased likelihood that UK interest rates would rise faster than previously anticipated, driven by strong labour market data including wage growth accelerating to 2.6%, the fastest rate in two and a half years. In commodities, oil was a major mover, with Brent crude advancing 6.8% amid rising confidence that OPEC would maintain its production cuts throughout 2018.

In fixed income, US Treasuries returned 1.0% in March, with 10 year yields falling 12.2 basis points to 2.74%. High yield credit and global convertibles were impacted by equity market concerns, with US high yield falling 0.6%, Euro high yield falling 0.2% and global convertibles falling 0.6%.

At this still favourable stage of the economic cycle the vast majority of threats to bond markets are inflation and interest rate related rather than credit risk. Perhaps the most notable recent development in bond markets is the continual flattening of the US treasury yield curve. The yield on 2 year Treasuries has risen over 100 basis points in the past 12 months, narrowing the gap with 10 year Treasuries to 47 basis points, the lowest since before the financial crisis. While this is typically seen as a precursor to worsening economic conditions, the move largely reflects the abnormally low yields on longer dated bonds, supported by post-crisis central bank asset purchases.

Figure 3: Ten year Treasury yields decline in March



Source: Bloomberg, Momentum GIM

There were several positive developments in geopolitics. The UK and EU agreed terms for a 21 month transition period following the agreed exit date of March 2019. This is an important breakthrough and gives the UK more time to negotiate its future with the EU and for businesses to prepare for Brexit. While economic uncertainty still overhangs the UK as it progresses through the Brexit process, the sharp underperformance of UK equities in the past 18 months leaves them undervalued and offers opportunities as the uncertainties dissipate. Of greater importance on the global stage has been the cooling of tensions on the Korean peninsula, with the world awaiting President Trump's meeting with Kim Jong-Un. A successful meeting could herald a meaningful reduction to this particular tail risk in markets, with the potential for all out conflict greatly reduced.

Despite this, the direction of markets in the coming months is most likely to be determined by central bank policy action rather than geopolitics. While there is risk Trump's imposition of tariffs could lead to broader protectionism and trade wars, the actions taken so far have been limited and are unlikely to derail the benign economic conditions globally. Although growth momentum has eased in the past three months, forward indicators are still suggesting strong growth in 2018. Any signs of acceleration in inflation will be the greatest concern for markets, as this would certainly be a catalyst for more aggressive monetary tightening.

On the current trajectory of growth and inflation, the Federal Reserve will continue as planned with its asset reductions and will raise interest rates twice more this year, following its 25 basis point increase in March. At the same time, the European Central Bank, still engaged in its asset purchase programme, will likely reduce its asset purchases to zero by year-end and will begin to raise interest rates by mid-2019. The Bank of England is also expected to raise rates this year, possibly as soon as May, with the UK economy performing stronger in the lead up to Brexit than previously anticipated. The net effect is that by year-end central banks in aggregate

will be withdrawing liquidity, rather than contributing. Led by the US, interest rates are likely to follow an upward path towards normalisation. This is likely to keep bond markets under pressure with yields rising further, and with that, the valuation hurdle for equity markets.

The combination of tightening policy and heightened uncertainty means that markets are likely to be more vulnerable to setbacks and greater volatility than in 2017, and may be held back by rising interest rates. Despite this, the underlying strength of the global economy remains, and the pace of monetary stimulus withdrawal will be cautious. Policy will still remain loose by historical standards and is highly unlikely to derail the currently favourable economic conditions. We therefore believe this cycle has further to run and view the current setback in markets as a healthy correction after a long unbroken run in asset prices. Equities remain our preferred asset class, and further setbacks in markets will present buying opportunities, while in fixed income we continue to believe that shorter duration exposure is appropriate at this still early stage of the global monetary tightening cycle

Market Performance - Global (Local returns)

Asset Class/Region	Index	To 29 March 2018		
		Currency	1 Month	3 Month
Developed markets equities				
United States	S&P 500 NR	USD	-2.6%	-0.9%
United Kingdom	MSCI UK NR	GBP	-2.1%	-7.3%
Continental Europe	MSCI Europe ex UK NR	EUR	-2.3%	-3.6%
Japan	Topix TR	JPY	-2.7%	-5.4%
Asia Pacific (ex Japan)	MSCI AC Asia Pacific ex Japan NR	USD	-2.4%	-0.7%
Global	MSCI World NR	USD	-2.2%	-1.3%
Emerging Market Equities				
Emerging Europe	MSCI EM Europe NR	USD	-4.7%	2.1%
Emerging Asia	MSCI EM Asia NR	USD	-1.6%	0.6%
Emerging Latin America	MSCI EM Latin America NR	USD	-1.0%	8.0%
BRICs	MSCI BRIC NR	USD	-3.1%	2.2%
Global emerging markets	MSCI EM (Emerging Markets) NR	USD	-2.0%	1.3%
Bonds				
US Treasuries	JP Morgan United States Government Bond Index TR	USD	1.0%	-1.2%
US Treasuries (inflation protected)	Barclays Capital U.S. Government Inflation Linked TR	USD	1.1%	-0.9%
US Corporate (investment grade)	Barclays Capital U.S. Corporate Investment Grade TR	USD	0.3%	-2.3%
US High Yield	Barclays Capital U.S. High Yield 2% Issuer Cap TR	USD	-0.6%	-0.9%
UK Gilts	JP Morgan United Kingdom Government Bond Index TR	GBP	2.1%	0.3%
UK Corporate (investment grade)	BofA Merrill Lynch Sterling Non Gilts TR	GBP	0.6%	-1.2%
Euro Government Bonds	Citigroup EMU GBI TR	EUR	1.6%	1.4%
Euro Corporate (investment grade)	Barclays Capital Euro Aggregate Corporate TR	EUR	-0.1%	-0.4%
Euro High Yield	BofA Merrill Lynch Euro High Yield Constrained TR	EUR	-0.2%	-0.5%
Japanese Government	JP Morgan Japan Government Bond Index TR	JPY	0.2%	0.5%
Australian Government	JP Morgan Australia GBI TR	AUD	1.3%	1.1%
Global Government Bonds	JP Morgan Global GBI	USD	1.6%	2.2%
Global Bonds	Citigroup World Broad Investment Grade (WBI) TR	USD	1.2%	1.2%
Global Convertible Bonds	UBS Global Focus Convertible Bond	USD	-0.6%	1.7%
Emerging Market Bonds	JP Morgan EMBI+ (Hard currency)	USD	0.7%	-2.0%

Source: Bloomberg | Past performance is not indicative of future returns. | *) denotes estimate

Market Performance - Global (Local returns)

Asset Class/Region	Index	To 29 March 2018		
		Currency	1 Month	3 Months
Property				
US Property Securities	MSCI US REIT NR	USD	3.7%	-8.4%
Australian Property Securities	S&P/ASX 200 A-REIT Index TR	AUD	0.0%	-7.3%
Asia Property Securities	S&P Asia Property 40 Index NR	USD	-0.2%	0.1%
Global Property Securities	S&P Global Property USD TR	USD	2.1%	-3.6%
Currencies				
Euro		USD	0.9%	2.5%
UK Pound Sterling		USD	1.9%	3.7%
Japanese Yen		USD	0.2%	5.9%
Australian Dollar		USD	-1.1%	-1.7%
South African Rand		USD	-0.4%	4.9%
Commodities & Alternatives				
Commodities	RICI TR	USD	0.6%	2.1%
Agricultural Commodities	RICI Agriculture TR	USD	-2.6%	2.8%
Oil	Brent Crude Oil	USD	6.8%	5.1%
Gold	Gold Spot	USD	0.5%	1.7%
Hedge funds	HFRX Global Hedge Fund	USD	-1.0%	-1.0%
Interest rates				
United States			1.75%	
United Kingdom			0.50%	
Eurozone			0.00%	
Japan			0.10%	
Australia			1.50%	
South Africa			6.50%	

Market Performance - UK (All returns in GBP)

Asset Class/Region	Index	To 29 March 2018		
		Currency	1 Month	3 Months
Developed markets equities				
UK - All Cap	MSCI UK NR	GBP	-2.1%	-7.3%
UK - Large Cap	MSCI UK Large Cap NR	GBP	-1.9%	-7.6%
UK - Mid Cap	MSCI UK Mid Cap NR	GBP	-3.1%	-6.7%
UK - Small Cap	MSCI Small Cap NR	GBP	-0.7%	-5.0%
United States	S&P500NR	USD	-4.2%	-4.4%
Continental Europe	MSCI Europe ex UK NR	EUR	-3.3%	-4.9%
Japan	Topix TR	JPY	-4.1%	-3.4%
Asia Pacific (ex Japan)	MSCIACAsia Pacificex Japan NR	USD	-4.0%	-4.2%
Global developed markets	MSCI World NR	GBP	-3.9%	-4.8%
Global emerging markets	MSCI EM (Emerging Markets) NR	GBP	-3.6%	-2.3%
Bonds				
Gilts - All	BofA Merrill Lynch Gilts TR	GBP	2.1%	0.2%
Gilts - Under 5 years	BofA Merrill Lynch Gilts TR under 5 years	GBP	0.0%	-0.5%
Gilts - 5 to 15 years	BofA Merrill Lynch Gilts TR 5 to 15 years	GBP	1.2%	-1.0%
Gilts - Over 15 years	BofA Merrill Lynch Gilts TR over 15 years	GBP	4.0%	1.5%
Index Linked Gilts - All	BofA Merrill Lynch Inflation-Linked Gilts TR	GBP	2.4%	0.1%
Index Linked Gilts - 5 to 15 years	BofA Merrill Lynch Inflation-Linked Gilts TR 5 to 15 years	GBP	0.5%	-1.2%
Index Linked Gilts - Over 15 years	BofA Merrill Lynch Inflation-Linked Gilts TR over 15 years	GBP	3.4%	0.6%
UK Corporate (investment grade)	BofA Merrill Lynch Sterling Non Gilts TR	GBP	0.6%	-1.2%
US Treasuries	JP Morgan United States Government Bond Index TR	USD	-0.7%	-4.7%
US Corporate (investment grade)	Barclays Capital U.S. Corporate Investment Grade TR	USD	-1.4%	-5.8%
US High Yield	Barclays Capital U.S. High Yield 2% Issuer Cap TR	USD	-2.2%	-4.3%
Euro Government Bonds	Citigroup EMU GBI TR	EUR	0.6%	0.0%
Euro Corporate (investment grade)	Barclays Capital Euro Aggregate Corporate TR	EUR	-1.1%	-1.7%
Euro High Yield	BofA Merrill Lynch Euro High Yield Constrained TR	EUR	-1.2%	-1.9%
Global Government Bonds	JP Morgan Global GBI	GBP	-0.1%	-1.4%
Global Bonds	Citigroup World Broad Investment Grade (WBIG) TR	GBP	-0.5%	-2.3%
Global Convertible Bonds	UBS Global Focus Convertible Bond	GBP	-2.3%	-1.9%
Emerging Market Bonds	JP Morgan EMBI+ (Hard currency)	GBP	-1.0%	-5.5%

Source: Bloomberg | Past performance is not indicative of future returns. | * denotes estimate

Market Performance - UK (All returns in GBP)

Asset Class/Region	Index	To 29 March 2018		
		Currency	1 Month	3 Months
Property				
Global Property Securities	S&P Global Property USD TR	GBP	0.4%	-7.0%
Currencies				
Euro		GBP	-1.0%	-1.2%
US Dollar		GBP	-1.9%	-3.6%
Japanese Yen		GBP	-1.6%	2.0%
Commodities & Alternatives				
Commodities	RICI TR	GBP	-1.1%	-1.5%
Agricultural Commodities	RICI Agriculture TR	GBP	-4.2%	-0.8%
Oil	Brent Crude Oil	GBP	5.1%	1.4%
Gold	Gold Spot	GBP	-1.1%	-1.9%
Interest rates				
United Kingdom			0.50%	
United States			1.75%	
Eurozone			0.00%	
Japan			0.10%	

Asset Allocation Dashboard



Asset class	View
Equities	
<p>Developed equities</p>	<ul style="list-style-type: none"> » We retain a neutral allocation to global equities today. Valuations vary across regions and sectors and whilst in aggregate they are not particularly cheap, central bank policy remains accommodative for now and rates remain low which can support current valuations. » CB policy and politics will remain central to risk pricing, and volatility is likely to be more elevated. + The global macro backdrop remains favourable for global equities, albeit with a pick in volatility more recently - Valuations remain selectively expensive at current levels - Continued talk around and implementation of trade tariffs is not constructive for global equities.
<p>UK equities (relative to developed)</p>	<ul style="list-style-type: none"> » UK equities are reasonably priced today but some caution is warranted given the evolving terms of the UK's Brexit. While the larger cap market constituents are more globally focused than they are UK, and have earnings shielded in large part from FX swings, the more domestically oriented names may face bigger challenges, not least with traditional high street retailers remaining under pressure » The UK market remains sensitive to commodity prices. + The UK market is very much exposed to global markets and factors and somewhat insulated from the headline Brexit concerns, benefiting from any renewed Sterling weakness - Today the chief worries lie with the ongoing (and slow) Brexit negotiations.
<p>European equities (relative to developed)</p>	<ul style="list-style-type: none"> » European equity valuations compressed through 2017 but remain favourable when viewed against corporate and sovereign European bond markets. From a more cyclical point of view Europe continues to recover from its post crisis lows, and investor appetite for European assets is positive today. » CB policy and politics will remain central to risk pricing, and volatility is likely to be more elevated. + European earnings have scope to recover meaningfully from their lows. - European assets, including equities, may come under pressure should the ECB's bond programme reduction accelerate, or the Euro strengthens further.
<p>US equities (relative to developed)</p>	<ul style="list-style-type: none"> » The US remains the most expensive of the major developed markets, even when adjusted for the strong tech sector performance. The US economy is in rude health but equity returns face a valuation headwind today, and prices already discount strong earnings growth ahead. With the benchmark index having declined again through March the valuation has improved slightly and we lift our assessment marginally, still preferring ex US but lifting off our lowest rating ahead of the Q1 earnings season which is expected to show buoyant earnings growth » Monetary policy remains crucial to keeping markets in check and volatility under control. To date the Fed has managed this well but there is always a risk of policy error, or an outside risk of higher inflation leaving the Fed little alternative to raising rates more quickly than rates markets are pricing. + The economy is strong and leading indicators positive. Tax repatriation could spur investment and share buyback programmes. - Valuations remain extended despite recent market volatility.
<p>Japan equities (relative to developed)</p>	<ul style="list-style-type: none"> » Japanese equities remain attractive and we acknowledge the government's policies to improve working practices and governance. Japanese assets should remain well buoyed by BoJ policy which remains aggressive when compared to the other main DM central banks. Any Yen weakness should boost Japanese stocks and we retain the more favourable view after a period of weak relative performance and currency strength. + Yen weakness will likely boost equities if the Fed moves in line with their stated intentions and the BoJ maintains their yield curve policy. Following recent Yen strength and subdued equity performance we think this more likely today. - In a protracted risk off scenario Yen strength would hit Japanese equities, as recently seen. The country also sits in an area of elevated geopolitical risk at the present time.
<p>Emerging market equities</p>	<ul style="list-style-type: none"> » Valuations remain reasonably attractive today and we continue to favour EM assets more generally over DM as relative growth dynamics looks favourable, which coupled with low inflation, accommodative policy and a weak dollar should support EM equities » More elevated volatility should be expected going forward, with CB policy and politics remaining central to risk pricing. + EM currencies remain somewhat cheap in aggregate which acts as a key support in a decision to allocate to EM. - Emerging markets remain prone to bouts of volatility and flow reversal at times of heightened perceived risk - The Dollar has been extremely weak. Any reversal may see EM assets come under pressure.

Fixed Income	
<p>Government</p>	<ul style="list-style-type: none"> » Despite on-going supportive policy actions, on a medium term outlook the majority of DM government bonds look unattractive today » Treasuries offer improved value today as yields oscillate below the 3% level but aggregate global government bond yields remain low. + Quality government bonds remain one of the best diversifiers in a multi asset portfolio - 2018 is likely to mark the year that net central bank bond purchases turn negative. That provides a headwind for all rate sensitive debt
<p>Index-linked (relative to government)</p>	<ul style="list-style-type: none"> » Index linked bonds offer some selective value today but, like their nominal counterparts, they are expensive today with breakevens looking at best fair value » UK linkers remain one of the more expensive DM markets. + Index linked bonds are one of the few ways to meaningfully protect against inflation risk. - Inflationary forces are at best nascent today and on any renewed concerns over global growth would likely underperform nominal bonds.
<p>Investment grade (relative to government)</p>	<ul style="list-style-type: none"> » Investment grade bonds provide some diversification benefit in a multi asset portfolio but valuations remain somewhat stretched today. Marginally preferred to sovereigns today » Fundamentals remain reasonable but we would advocate owning more shorter dated credit at today's levels as rate sensitivity remains near highs. + A reasonable alternative to owning sovereign bonds with diversifying qualities and some spread - It is difficult to see spreads tightening much further, and with central bank buying slowing the risks are asymmetric.
<p>High yield</p>	<ul style="list-style-type: none"> » Spreads remain tight in leveraged credit markets, despite a recent repricing, and whilst fundamentals remain robust, all in valuations are somewhat expensive. » We favour owning shorter duration credit where the risk return looks more favourable today, and loans where permissible. + In the absence of a systemic market shock high yield returns will likely trump most of other fixed income. - Issuance terms are increasingly favouring the issuer, and valuations look somewhat expensive.
<p>Emerging market debt</p>	<ul style="list-style-type: none"> » Emerging market bonds - both hard currency and local flavours - have had strong returns amidst a favourable macro backdrop and sentiment. Despite their rally, EM bonds still rank as one of the better real return opportunities » With spreads remaining somewhat tight we think a short duration strategy has a better risk return today and would look to re enter core duration strategies at higher spreads + EM bonds continue to offer some of the best return opportunities in core bond markets today - A resurgent dollar is likely to cause some temporary repricing in EM assets, and local bonds would likely bear the brunt of that.
<p>Convertible bonds</p>	<ul style="list-style-type: none"> » Convertible bonds are priced slightly rich to their constituent parts today but we continue to favour an allocation to this asset class in a multi asset portfolio for the convexity it brings, which remains valuable today at a time of elevated valuations » Some caution is warranted given the concentration to the US market and technology names. + The natural convexity provided by convertibles should continue to provide reasonable protection against any protracted equity correction - The call optionality embedded into convertibles only really has any value if markets move higher. If volatility reverts again to the recent multi year lows then the optionality holds limited value.

Alternatives	
<p>Commodities</p> 	<ul style="list-style-type: none"> » Commodity prices are primarily supply and demand driven, and idiosyncratic factors will drive commodity prices as much or more so than the global economic cycle. Commodities remain sensitive to negative news on global growth » With inflation risk at the lower end of historical levels there is little upward pressure on underlying prices at present » Commodities are susceptible to the increasing trade tariff newsflow and geopolitical factors which may lead to volatile pricing. + With the US Dollar coming down from cyclical highs, and growth reasonably strong globally, commodities have scope to generate positive returns. + Gold remains a good hedge against risk off outcomes - Should the Dollar's decline come to a halt or reverse, commodities would likely come under pressure.
<p>Property (UK)</p> 	<ul style="list-style-type: none"> » Property remains an attractive asset class for investors requiring yield. In the UK returns look more attractive outside the capital at this time, where prices have come under pressure » Total returns will come mostly from income with limited scope for capital growth. When viewed against high quality longer duration Sterling assets and inflation linked bonds, property has appeal + Reasonable valuations and yields should continue to attract capital, moreso on any renewed Sterling weakness - As a long duration asset class property remains susceptible to any repricing in long term bond yields.
<p>Infrastructure</p> 	<ul style="list-style-type: none"> » Infrastructure stocks trade at reasonable valuations today - broadly in line with global equities. Their income generating potential should continue to support the sector and attract buyers of quality infrastructure assets. + In a multi asset portfolio the relatively defensive nature of the asset class and a degree of inflation protection make the asset class appealing - As a long duration asset class property remains susceptible to any repricing in long term bond yields - Regulation can work both for and against the underlying investments.
<p>Liquid Alternatives</p> 	<ul style="list-style-type: none"> » We define this section as less/non-directional, absolute return type strategies that seek to capture long term risk premia or market mispricings, and includes hedge fund alternatives in predominantly UCITS vehicles » We favour an allocation to a basket of liquid strategies today to provide additional diversification as high quality bonds remain quite expensive. + These strategies provide additional diversification with reasonable return potential - The sector is relatively young and growing. It remains somewhat untested through a protracted risk off period so thorough due diligence is vital, and blend is recommended.
Currencies	
<p>GBP</p> 	<ul style="list-style-type: none"> » Sterling remains buoyant today, both a function of continued Dollar weakness and some softening around the Brexit margins » In real terms the currency remains at the lower end of valuations and has room to appreciate over the medium to long term, but politics and rate policy is likely to dominate its nearer term path, and remains a source of volatility » Valuation supports a long position but with the USD looking somewhat oversold, Sterling positioning having rebounded markedly, and Brexit front and centre, we continue to rate slightly under neutral today.
<p>Euro</p> 	<ul style="list-style-type: none"> » The Euro has also benefitted from the weaker Dollar but its own fundamentals have supported its gains. Whilst any change in explicit rate policy still remains some way off, the reducing quantum of bonds the ECB is now buying exerts some marginal upside to rates, certainly in sentiment, and the economic backdrop is as good as its been for a number of years » In real terms the common currency looks about fair value today and is not a compelling long term buy » Positioning remains extended today and versus the Dollar the currency looks somewhat overbought.
<p>Yen</p> 	<ul style="list-style-type: none"> » Rate differentials continue to offer little reason to buy the Yen as the Bank of Japan's yield curve policy means short rates will offer no real value for some time. However, in real terms the Yen remains cheap today. » Yen exposure is a useful portfolio diversifier but after a recent pick up in volatility this quality has mostly played out. Speculative positioning remains near the lows which may provide support » We retain a cautious view today as the currency continues to look extended after rallying sharply through February and March.

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

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