CREDO NEWS at Regent's Park

Issue 14 . Summer 2013

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Message from the CEO
Roy Ettlinger - *CEO, Credo Group*
@Ettlinger_Credo

Beginnings, Endings

Beginning of the End or End of the Beginning?

As I write this article it appears that summer has finally arrived in London. The beginning of the summer… Is there a more exciting city in the world than London in the summer? Wimbledon, an Ashes cricket series, the Henley Regatta, the Rolling Stones, Elton John, Robbie Williams, the Royal Parks to mention just a few of the attractions of our great city, let's hope that this is the beginning of summer and not the end.

Many of you reading this newsletter will be aware that a major change in Credo's business has taken place since our last newsletter. For Credo it was the end of the beginning in that after almost 15 years building and managing Credo's property business, Gavin Rabinowitz decided that the time had come for him to set up his own property business, Argo Real Estate Partners, "Argo", which will focus on principal and opportunistic investments.

As a founding shareholder, Gavin played a vital role in Credo's success to date and for that I want to thank him and say that Credo will miss him immensely.

Fortunately Gavin will continue to work closely with us as Credo has taken an equity stake in Argo and will operate from the same premises. Gavin and his team will continue to be responsible for the on-going management of Credo's existing property portfolios and clients will be given the opportunity to participate in the property investments which Argo sources. We are confident that there will continue to be interesting property opportunities for you, our clients and that the current standard of service will be maintained.

For Credo the end of the beginning, but for Argo, just the beginning.

We are very excited about our impending move to Regent's Park, see page 19 for further details about our new office, the end of our sojourn in Pall Mall, the beginning of our existence in one of the Royal Parks.

There is throughout the newsletter, a recurring theme that at some stage in the not too distant future we will see the end of cheap money, technically called Quantitative Easing but most often referred to as QE. This is evidenced by the changing expectations of the level of interest rates in some parts of the developed world. Most importantly for global financial markets however, are the expectations with respect to the US dollar. Many fear that this is not the end of the beginning but rather the beginning of the end for financial markets that have been having their "time in the sun" and enjoying abnormally low interest rates for the last 5 years.

Certainly an interesting challenge awaits our newly appointed governor of the Bank of England, Mark Carney, a Canadian who on 1 July began his new role, as Sir Mervyn King reached the end of his 10 year stint.

We have also just seen the end of our regulatory authority, the Financial Services Authority and the beginnings of its successor the Financial Conduct Authority. Hopefully for all involved in our industry, the new regulator together with those of us in the financial services industry will be effective in improving the image of our industry, which has unquestionably suffered since the advent of the financial crisis.

We hope these new beginnings will also help to bring about an end of austerity measures and signal a new economic beginning.

And finally just an acknowledgement to a truly great man who has inspired me and perhaps all of us, for decades, Nelson Mandela who has struggled in the past few months with failing health. While some people say the end is nigh and it is now time to release him spiritually, South Africa's President, Jacob Zuma has told the nation, which does not want to let him go, to begin planning for Nelson Mandela's 95th birthday on 18 July. Either way we were truly privileged to be the generation who lived through the latter years of the Mandela era, an era that was the beginning of the new South Africa, and the beginning of hope for millions of people.

This is the end of the beginning, and I hope you enjoy the rest of our summer newsletter.

Deon Gouws - CIO, Credo Group
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Currency fluctuations:

Launching The Credo Sirloin Index

A few weeks ago, two colleagues and I travelled to South Africa on a week-long roadshow. As it happened, this was the time that the rand seemed to go into free-fall on a daily basis – which clearly led to a number of interesting discussions about the future of the currency.

Upon returning to London, I went through all my receipts from the trip and put together a travel claim. Amongst other things, I paid for six meals (for all three of us) while we were out there. Most of these were light lunches or relatively modest dinners, but I also paid for some lovely steaks at HQ in Cape Town (not to mention a wonderfully drinkable bottle of Cederberg Merlot/Shiraz, as recommended by our very knowledgeable waiter on the night). In total, these six meals set me back the grand sum of £158.67 at the prevailing rand/sterling exchange rate (at the time of writing some ten days later, the total equated to £147.03).

It's probably fair to say that just the one dinner (steak for three and a decent bottle of wine, plus tip) would cost in excess of £150 in one of London's upmarket restaurants such as Hawksmoor or Goodman – which helps to put the value of the six meals we had in South Africa in some perspective.

I guess the above is just my own crude attempt to reconstruct a Big Mac Index (the Credo Sirloin Index?) (specifically for those of us who do not typically frequent the hallowed halls of McDonalds). But it's probably also worth noting that when the actual Big Mac Index was in fact updated by The Economist magazine earlier this year, it was suggested that the rand (at 9.03 to the dollar / 14.20 to the pound at the time) was already significantly undervalued.

The Big Mac Index uses the theory of purchasing-power parity (PPP), according to which prices and exchange rates should ultimately adjust in order to ensure that identical baskets of goods cost the same across countries. The index refers only to the price of one Big Mac hamburger and relies on the efforts of McDonalds to produce identical products from the same ingredients around the world. Even though it has to be conceded that the Big Mac Index is a rather blunt instrument, one should also acknowledge that its relative success in explaining currency movements over the years has been rather uncanny – which is probably why the measure has already survived more than a quarter of a century. In the past few months, for example, the rapid slide in value of the Brazilian real and the Australian dollar have in fact once again approximated the relative overvaluation as per the January update to the index.

Unfortunately the Big Mac Index has never really worked particularly well in the case of the South African rand, as it always seems to suggest a fairly substantial undervaluation (the extent of which simply fluctuates over time). One can postulate a number of explanations for this, but I would suggest that one of the main reasons why eating out (whether at HQ or McDonalds) has always been cheaper in South Africa than anywhere in the developed world, simply relates to the tremendous gulf in real estate values (and by implication restaurant rents).

Having said this, how does one reconcile the fact that the rand continues to slide from levels which could be argued to be somewhat undervalued already? This is clearly a vexed question, and the truth is that no-one really knows the full answer. But there is obviously a number of contributing factors, only some of which relate to economic fundamentals, with others boiling down to swings in sentiment (political and otherwise).

This is why I always give the same answer when someone asks my views about the future of the rand. Honestly, why should I (or anyone else, for that matter) have any idea? How many people do you know who have been able to successfully predict the big moves in the rand since the New South Africa dawned two decades ago?

I would therefore put the question back to anyone who asks for an opinion about the currency: what are your views related to the political stability of the country in the medium to longer term?

If you remain bullish about South Africa's prospects, there is reason to believe that the rand could appreciate again at some point, as a case can be made that the rand has become relatively undervalued based on selected fundamentals (the Credo Sirloin Index being only one of them). Focusing on other factors (such as interest rate parity theorems and/or the commodity cycle) – and especially if one happens to be one of the political skeptics – you probably owe it to yourself and your loved ones to continue diversifying as far as currency exposure is concerned (assuming you have money to invest).

Over the past year, my colleagues and I have been involved in numerous conversations with clients who indicated that they were very keen to invest offshore, but would only do so "as soon as the rand returns to a certain level". And of course, we all know what the currency has done in the meantime…

Suffice it to say that the different exchange rates at the time of many of these conversations over the past twelve months will now look very attractive to those who never actually pulled the trigger. Fretting about opportunity profits foregone can be very painful indeed.

It is often said that diversification is the only free lunch in the world of investing, and we would argue that this principle extends to one's currency exposure as well. Against this background, our advice to South African investors will always be the same: utilise any periods of relative rand strengthening in order to add to your offshore exposure.

We cannot guarantee that you will find a steak (or a hamburger!) which compares favorably to those in one of Cape Town's better restaurants, but it may be the only way to ensure that the price of eating out does not give you indigestion when you next travel overseas.

Asset Management

Ainsley To - *Research Analyst, Credo Capital*
@AinsleyTo_Credo

I know, I don't know

Doubt is not a pleasant condition but certainty is absurd

From "*Risk-on, Risk-off*", through "*Cliff-on, Cliff-off*" to "*Taper-on, Taper-off*", it's been a fascinating few years. As we wrote in an article entitled "*Open Mouth Operations*" in the previous edition of CredoNews, the hot topic this year so far has been whether Bernanke will talk the talk (let alone walk the walk). Money managers are betting on US equities as they see a taper suggesting a strong economy or on Japanese equities as they truly believe the Bank of Japan could stimulate inflation. Suddenly every investor and fund manager seems to be an expert on monetary policy. But given the current dissent amongst the US Federal Open Market Committee and the relatively poor forecasting track record of policy makers, one has to wonder how asset managers can predict with such confidence what central banks are going to do, when the Fed themselves don't know what to do? Borrowing from Stanford's Amos Tversky, "*It's frightening to think that you might not know something, but more frightening to think that, by and large, the world is run by people who have faith that they know exactly what's going on.*"

And perhaps for clients of said asset managers, it is equally frightening that they might have trusted the management of their assets to such people. Ultimately few can debate the pedigree of many risk takers - given a large majority of Ivy League graduates wishing to maximise the return on their time, end up in the investment industry. So it should come as no surprise that given the levels of compensation and prestige awarded, humility is a scarce commodity amongst wealth and asset managers.

But why do so many investment professionals, who dedicate their own careers and the resources at their disposal to research, tend to underperform the market over the long term? Perhaps it is the incompatible mix of overconfidence with the constant state of uncertainty a market participant must exist in. In dealing with the uncertainty inherent in markets you have to accept that the number of times you will be proven wrong is going to be a lot greater than zero. Nassim Taleb famously documented the tendency of human nature to reject uncertainty in favour of any plausible explanation it can find. This human flaw is compounded by the fact that "*I don't know*" is a taboo phrase for many in the investment industry, for fear of appearing ignorant or uninformed. Ironically in investing it's rarely what you don't know that hurts you… it's what you think you know that ain't so. The combination of human nature's desire for certainty with the natural hubris in the industry, set against a backdrop of unprecedented levels of monetary experimentation by central banks and we have ourselves a perfect storm for some nasty surprises in the future.

Yet although hubris is a continual failure of the investment industry, it is also what perpetuates its existence – the notion that one is smarter than the next guy and better informed than everyone else is what drives people to invest… and it is through this hubris that the best investors can thrive. The biggest opportunities for investment returns aren't created by companies, central banks or politicians; they result from the mistakes other investors make. The syndrome of arrogance in investing is described best by Howard Marks

of Oaktree. In his memo "*Us and Them*", he highlights some of the differences between "*I know*" investors who make bets based purely on their opinions of the future, and "*I don't know*" investors who are respectful of their own ignorance: *http://www.oaktreecapital.com/MemoTree/Us%20and%20Them%20(050704).pdf*

In summary, the "*I know*" school believe that an opinion on the direction of stock markets and attempting to accurately predict the future are a requirement to succeed in investing. They are aware lots of others are trying to do the same but they believe either: a) everyone can win together, or, b) only a few can, but they are amongst those few. They also believe there is a causal relationship between their opinions and investment performance and that luck plays no part.

The "*I don't know*" school, on the other hand, are humble worriers, constantly questioning their own views and decisions. They define risk as what is left over after that point when you think that you've already thought of everything. They are conscious of protecting investors and themselves from their own ignorance.

We've included below some of the traits Marks has identified (and added a couple of our own) in order to help readers gauge which of the two schools investment professionals they know are likely to belong to:

Investing in the "new normal", in our opinion, can best be characterised as a long marathon across a minefield. The confident sprinter may be ahead at the start, but it's the cautious man with the metal detector who is more likely to make it across the whole track in one piece.

But then again, what do we know, after all…

"I know"	"I don't know"
Bullish by nature	Bearish by nature
Aggressive	Defensive
Confident	Guarded
Risk is it lands on black and not red	Risk is I havent thought of everything
What might go right?	What might go wrong?
Worried about winners missed	Worried about losers bought
Trend followers	Contrarians
Attracted to pretty flowers	Glad to search among the weeds
Comfortable when part of the crowd	Happy when apart from the crowd
Growth/momentum investors	Value investors
"Great things cost a lot"	Insistent on buying cheap
Believers	Skeptics
"We're in a new era"	"Trees don't grow to the sky"
Cheered by excessive appreciation	Frightened by bubbles
Enjoy averaging up	Enjoy averaging down
"Let it ride"	Eager to take profits
Relative return-oriented	Absolute return-oriented
Worried about underperforming	Worried about losing money
Pained by cash	Comfortable with cash
Confident in their powers	Aware that much is beyond their control
Convinced that their good returns are fully deserved	Highly conscious of the role played by luck
Impatient	Patient
Short term-fixated	Long term-oriented
"The Fed will taper"	"The Fed themselves don't know what to do"
"The Eurozone will break up"	"Politicians will determine the fate of the Euro"
"The BOJ will create inflation"	"What effect could inflation have on JGB yields?"

Jarrod Cahn - Senior Portfolio Manager, Credo Capital

Unravelling the muddle in the markets

Jarrod Cahn explains how the Credo Best Ideas Portfolio offers a safe option to navigate the storm

For those who read our first newsletter of the year, particularly the article entitled "The Story So Far", we ended with the suggestion that although equities had had a great start to the year, we expected markets to muddle through the remainder of the year, coming to grips with similar issues that pre-occupied the markets over most of 2012.

At the time of writing this article, the FTSE has given back almost all its gains for 2013, although the US indices have fared considerably better. The gains that have been made appear to be harder to hold on to, and the headwinds are starting to emerge. Possibly the biggest surprise though, is not necessarily the issues of the Eurozone crisis or Cyprus, or a China slowdown, but rather the program of "tapering" by the US Fed. Bizarrely this idea should be viewed as positive, as it means that the US economy is recovering, along with the housing market and employment rates. Yet, like heroin addicts, investors do not want to come off the "cheap money" fix, and have sold off equities and bonds in a fairly aggressive manner.

So muddling through 2013, dealing with the delicate balancing act of weaning off Quantitative Easing, while still trying to balance the timing, is certain to pre-occupy equity investors for months to come.

With this in mind, we return back to the Credo Best Ideas Portfolio (BIP), its values, investment methodology, and performance. The portfolio is a long term high conviction portfolio consisting of no more than 20 long term holdings. After recently adding Wells Fargo to the portfolio, we currently have a total of 18 holdings – the highest number since inception. As an equal weighted equity portfolio, this effectively means that we have held at times between 10% -15% of the portfolio in cash (i.e. in anticipation of filling the last 2 or 3 portfolio positions, potentially taking it up to the 20 stock maximum) – which clearly detracted somewhat from performance over bullish periods. The intention, however, is unchanged, namely to get the portfolio up to the maximum 20 stock positions. Accordingly, we have identified a number of sectors and stocks that we would like to own, but we are waiting for an appropriate valuation at which to acquire these positions in future.

Portfolio turnover has been low in 2013, with the only sale being the exit from Xstrata in late January (following the confirmation of its planned merger with Glencore). This has proven to be a good sale, as commodity prices have continued to soften, China growth has stalled, and commodity stocks have been weak. Similarly, given that we already have exposure to Anglo American (our worst performing stock in the portfolio) we were cognisant not to be overexposed to a volatile sector, at a time when we believed market forecasts were being too bullish.

The only addition to the portfolio has been the purchase of Wells Fargo bank (referred to earlier). After being underweight banks over time (having only owned HSBC from inception of the portfolio), we decided to add this US bank in the past month. Until recently, we viewed that the banking sector to be essentially "un-investable", but five years into the credit crunch and following huge de-leveraging as well as better balance sheet transparency, we now view the US banks as attractively valued on a risk/reward basis – and of those, Wells Fargo appears to have the most robust business model. Although clearly there is significant upside that might be gained from other banking stocks in Europe (not to mention the UK), we believe that Wells Fargo should provide significant outperformance against the general market over the longer term.

As far as the rest of the portfolio is concerned, we have always looked at a number of fundamental factors when owning stocks, predominantly around value and risk/reward measurements. It has been no surprise that a large portion of our portfolio has thus been in defensive sectors with high dividend yields. We have enjoyed a fantastic rally in these stocks as non-traditional equity investors have poured into the equity markets to chase dividend yields when other traditional asset classes like bonds and property have not offered as attractive a return. On the other end of the scale, we also have some more cyclical and growth stocks in the portfolio that have performed less well of late. Again, with the advantage of holding a diversified portfolio of stocks in different sectors, geographies and currencies, the portfolio has benefited from seeing some of the lagging stocks from last year becoming the best performing stocks of this year, notably Microsoft and Prudential Plc, to mention but two examples.

The fact that the BIP is not a themed based portfolio avoids a number of the typical traps that equity investors may fall into. The China theme, Commodity theme, Technology theme, Japan theme, or even the High Dividend Yielding Stock theme, all make sense at different points in time, as long as investors are on top of their portfolios, constantly watching fundamentals and are prepared to trade in and out as these themes ebb and flow. The beauty of holding a diversified, value based equity portfolio like BIP, however, is that investors are likely to get exposure to elements of these themes over a period of time, but it will never be a concentrated portfolio just playing a single theme. Similarly, when some themes, sectors or geographies are working, others may not (which has recently been the case), but the diversification should lead to a relatively smoothed return within the portfolio.

In conclusion, we remain satisfied with the performance of the BIP to date. We believe that the remainder of 2013 is likely to remain a challenging time for investors in general, however we also believe that as investors grapple with the divestiture from bonds and cash, they should continue to invest further into the equity markets. As such, equities may muddle along through the year and it will continue to be more of a stock-pickers environment in all likelihood.

Against this background, we will remain disciplined in our valuation approach, constantly striving to ensure that the portfolio constituents provide us with the best risk-adjusted opportunities within our investment universe, in the quest to continue to add value to client portfolios over time.

Rikky Shoker - *Portfolio Manager, Credo Capital*

Recent concerns that the Fed may be tapering its bond buying programme have investors around the world fretting. An extended period of abnormally low interest rates left many investors with a difficult choice to make - either move up the risk spectrum or accept the very low relative returns available today. Consequently, high yield debt and more specifically emerging market local currency bonds attracted much of the "hot money" causing yields in these markets to compress to levels that some have considered "dangerously low". According to data service provider PFR Global, more cash has been invested into local debt year to date than during the whole of 2012.

Unsurprisingly, the change in interest rate expectations over the past few weeks has seen money flow out of these instruments just as quickly as it went in. These concerns have been echoed throughout the financial markets, with interest rate sensitive assets all being adversely affected by the changing expectations. The Credo Dividend Growth Portfolio ("DGP") which is composed of companies offering attractive dividend yields and defensive characteristics has not been immune to this volatility.

Companies with an ability to grow dividends over the long term

Policy induced volatility

Rikky Shoker looks at how interest rate expectations affect Credo's Dividend Growth Portfolio

typically have strong dependable cash flows and are therefore defensive in nature. Many of these companies were coined "the new sovereigns," as they offered more attractive yields than most fixed income instruments and were perceived to be a "safer" investment than the bonds of debt stricken global sovereigns, especially in Europe. But with the inevitability of interest rate normalisation, many now legitimately question the attraction of the high yield equity asset class. If high yielding equities are viewed as an alternative to interest bearing instruments, then surely the case for investing in them becomes less compelling as interest rates rise. It is simply not a case of if, but rather when, and with accelerating growth in the US economy investors have begun to price in these expectations.

It is, however, important to distinguish between the high yield equity asset class and the mandate for our DGP. It does not look at high yields in isolation. Rather we focus on the ability of a company to grow its dividends and view this as a key driver of share price appreciation over the long term. Furthermore, in a rising interest rate environment, a company that can grow its dividends could be considered a far more compelling investment than a company that cannot. Articulated another way, all else being equal, a floating rate bond should outperform a fixed rate bond as interest rates rise. Therefore we look for companies that have strong franchises, wide economic moats and sustainable pricing power, are well capitalised and managed by strong management teams. Such companies should be much better positioned to compound their earnings and dividends over the long term.

Dividends and dividend growth alone may not entirely protect an investor from the risk of capital losses, or volatility for that matter. More so, in today's abnormal environment of artificially cheap money, increasing volatility is inevitable. At the time of writing, most defensive high yielding sectors have grossly underperformed the market over the last month, having outperformed significantly in the preceding months, due to the concerns over rising interest rates. But such short term market gyrations should not impact the ability of a company to grow its dividends. Numerous studies show that dividend growth has been far less volatile than corresponding share price movements and even earnings growth for that matter. Moreover, if one conducts an analysis of the dividend and share price movements for various constituents of our DGP, it becomes evident that dividend growth over the long term has contributed strongly to share price growth. Historical studies show that dividends collectively account for 90% of the return in the S&P 500 over the past century. Should a company's earning's power become permanently impaired, it's fair to assume that dividends will more than likely suffer a similar fate. As a result we focus on companies that have strong earnings' visibility, accompanied by low dividend pay-out ratios. The latter criteria helps to both minimise the risks to dividends of earnings impairment and provide ample room for future dividend growth.

Therefore, notwithstanding near term unpredictability, we are confident that the companies we own in our DGP are well positioned to perform strongly over the long term. Whilst higher interest rates could act as a headwind to the portfolio over the short term, the prospects of accelerating economic growth should help drive the earnings' power and cash flows that are vital in supporting dividend growth even higher.

Rupert Silver - *Senior Portfolio Manager, Credo Capital*

Give your portfolio some wings…

Certain alternative assets are looking more and more attractive

With commodities, equities and bonds showing an uncomfortably high correlation, we continue to search for alternative assets that should have a lower correlation to the market. Doric Nimrod Air Three Limited ("Doric") appears to be one such opportunity that we recently identified and subscribed for shares in the placing on behalf of some of our clients. By the time you read this Doric should be trading as a listed company.

The company's objective is to generate income and capital returns for its investors by acquiring, leasing and then selling aircraft. Whilst this may sound a little quirky, the structure isn't too complicated and the returns could be exciting so please don't disembark just yet!

At the outset Doric will buy four Airbus A380 planes (currently the world's largest commercial passenger aircraft) and lease them to Emirates, which would rather lease the aircraft, making quarterly payments, than fund the purchase up front. The acquisition will be funded by approximately £200m of equity (to which we have subscribed) and approximately $630m of debt at a rough cost of 5% per annum. The intention is to pay the equity holders a coupon of 8.25%, in the form of a quarterly dividend of 2.0625p for the next 12 years. The debt is structured to amortise over the 12 years so it's important to realise that at the end of that period, Doric will own the aircraft debt free which it then intends to sell.

Assuming that Emirates remains solvent, investors will receive the 12 year income stream, which should return 99% of one's capital. There is uncertainty as to what the value of the aircraft will be at the end of the 12 years, however independent aircraft-value appraisal firms suggest that the value of the aircraft would leave the equity holders with an additional capital gain of 69% (at constant exchange rates) on their initial investment, giving a total return of 14% per annum. Investors must be aware that a fall in the value of the aircraft below the estimated value at the time of sale will erode the capital returned and a fall of over 66% in the value of the aircraft will actually erode the investor's base capital. This does appear to be unlikely based upon historical assumptions and by this stage investors will have received back 99% of their investment via the quarterly dividends.

Some of the risks of this investment are the credit worthiness of Emirates, currency fluctuations against sterling at the point of sale and probably the major one, the valuation of the aircraft after 12 years. We do on balance believe that, in the current economic environment, the risk reward equation is favourable, and we are very comfortable with the investment manager (Doric Leasing Corporation) which has a good pedigree in this asset class.

This will be the third investment vehicle that Doric Nimrod has listed. The previous two, both trade in excess of 10% above the list price, having been well supported by both shareholders and the financial press. With a good track record, a very high income stream, a quarterly cash flow, the potential for capital growth and an asset that shouldn't be highly correlated to other investments, we feel that the investor will be handsomely compensated for taking such risks.

Due to the concentrated investment, the use of leverage and a degree of illiquidity, this investment is only suited to higher risk investors who should consider climbing aboard!

Trading Services
Alan Noik - *MD, Credo Capital*
@AlanNoik_Credo

Momentum Wealth Appoints Credo

Credo Capital Plc is delighted to have been appointed as the asset manager and stockbroker for Momentum Wealth International, which last month launched their International Personal Share Portfolio giving their clients the ability to invest in a global custom-made equity portfolio.

"Momentum Wealth International spent several months investigating a wide range of stock broking firms who were keen to engage and assist with the provision of direct share portfolio solutions to our associated Financial Advisers and clients. We considered a number of parameters in deciding the final partner ranging from reputation; investment team credentials and domicile. We chose Credo due to their good standing with many Advisers in South Africa as well as their willingness to truly engage with MWI in a true partnership approach. We have been extremely impressed by the support they have provided thus far, and look forward to the relationship growing from strength to strength." Louise Usher, Head: Momentum Wealth International.

Momentum Wealth International provides specialist investment management services and investment administration services to financial intermediaries and their clients in South Africa, the Middle East and Asia.

Momentum Wealth International, based in Guernsey, is part of Momentum Holdings Ltd (now MMI Holdings Limited). MMI Holdings, a JSE-listed company, was formed as a result of the merger between Metropolitan and Momentum Group in 2010 and is South Africa's third-largest life insurance group, with a 122-year underwriting history and a market capitalisation of ±£2.5b (June 2013).

momentum
investments | wealth international

For more information, please contact your Relationship Manager on +44 207 968 8300.

MyCredo now includes Morningstar Research

In the last edition of CredoNews (Issue 13) we mentioned that both our Financial Intermediary clients as well as our Private clients would shortly have access to the Morningstar research tool. This is now live and available through MyCredo. Morningstar is a leading provider of independent investment research and is one of the most recognised and trusted names in the investment industry. Our tie up with Morningstar gives you unlimited access to easy-to-use portfolio management tools, personalised portfolio analysis, select investment ideas and independent, in-depth equity analyst reports.

Charles van der Merwe - *MD, Wealth Outsourcing Solutions*

Growth of Credo's Wealth Outsourcing Solutions business

Over the past decade we have successfully grown our Institutional client base, particularly in South Africa, where we now have relationships with a number of the largest and most prestigious institutions. Our success in this area encouraged us to establish a separate new business division, Credo Wealth Outsourcing Solutions. Charles van der Merwe, the newly appointed head of Wealth Outsourcing Solutions, explains more about the business.

Building on the success of providing services to South African domiciled Financial Intermediaries (where Credo has 22 clients with £500m Assets under Administration, representing some 1,500 investors), Credo decided to expand its target market to include Intermediaries based in the UK, the Channel Islands and across Europe. Leveraging Credo's in-house investment platform, Credo's Wealth Outsourcing Solutions business will provide Wealth Managers, Financial Advisory firms and Family Offices with a Platform, multi-asset class Trading service, both onshore and offshore custody, sophisticated investor reporting and a Managed Account or Model Portfolio service. By outsourcing certain key functions to a firm that has economic scale, trading and discretionary management expertise and an established market presence, Financial Intermediaries gain access to capability which allows them to compete effectively with much larger financial institutions.

Credo's investment platform (MyCredo) is a multi-asset class platform, offering a broad solution to meet the complex needs of the Advisor/Manager and their investors. The superior 'white label' reporting and flexible technology makes Credo a credible provider in the wealth management outsourcing market. The industry trend is for outsourcing providers to include more content on their platforms, as recently evidenced by Credo's inclusion of Morningstar Analyst Research Centre in MyCredo. Credo will continue to invest in MyCredo and we will announce further enhancements in the near future.

Following the Retail Distribution Review (RDR), the UK market is currently going through substantial changes:

- Many Financial Intermediaries are restructuring their business models from a product provider sourced commission based model to an investor based fee based model. This price transparency has also resulted in many investors questioning the cost benefit they get from their Advisor/Manager, resulting in many Financial Intermediaries reviewing their current business arrangements.

- In a recent survey of 200 Advisors, 51% indicated that they would increase their use of Managed Account or Model Portfolio services and 59% indicated that it is important or very important that their platform provider also offers their own Managed Account solution.

The RDR is expected to have a similar impact in the rest of Europe when new RDR rules are finalised.

Nelius Kriel - *Stockbroker, Credo Capital*

Structured Products

An investment for all seasons?

During the course of 2011 and 2012, Credo successfully launched the Best Ideas Portfolio as well as the Dividend Growth Portfolio, both of which have proved extremely popular with our institutional as well as our private clients. In order to satisfy the specific needs of certain institutional clients, Credo has introduced structured products to our offering.

Structured products have become increasingly sophisticated and complex over the years. From humble beginnings in the 1970's, with guaranteed bonds being marketed by life offices, to the incorporation of option positions in order to effect gearing or provide capital protection.

The more mainstream trend over the past decade has focused broadly on two types of client. On the one hand, there is the high net worth individual looking for a very specific exposure over a fixed time-frame, whilst on the other there is the mass retail market essentially interested in capital guaranteed products. Although these are very different markets, the mechanisms underlying these products are very much the same.

Structured products in general, are designed to provide either capital protection (with at least a part participation in the growth of an underlying index / securities), or an enhanced participation in the growth of an index / securities (whilst risking a portion of capital invested).

Over the last few years, the mass retail market in the UK has embraced some of the simpler forms of these products, especially in an environment with interest rates at unprecedented lows and with the prospect of short to medium term rate increases remaining doubtful. Some structured products provide a capital guarantee if certain thresholds are met, as well as substantial participation in the growth of the FTSE 100 or the S&P 500 over e.g. a 3 year period and so provide investors with the option of effectively investing in the stock market with limited downside to their capital. Although on the face of it, structured products have many advantages, the Financial Conduct Authority ("FCA") regards all structured products as high risk and accordingly they are not generally suitable for retail clients.

How to choose what is right for you?

With all investment products the primary question is the same, namely: *"What investment goals does the investor have and what is the most suitable way of achieving these?"*

Market conditions, outlook, your risk profile, the complexity of the product as well as your knowledge and experience and understanding of the product are all factors that should be taken into account when assessing a structured product.

Who could benefit from structured products?

Many investors can potentially benefit from including structured products in their portfolios, from sophisticated retail investors who would like some exposure to equity markets with limited capital downside or who are searching for enhanced diversification on various asset classes, to professional and institutional clients wishing to enhance certain parts of their bespoke portfolios – the options of available structured products are nearly endless.

After strong performance in world equity markets since late last year, the past two months have been marred by weakness in the fixed income, equity and commodity markets. Structured products could provide a way of shielding oneself against some of this volatility.

A recent example

We will soon launch a structured product which we feel would suit certain sophisticated, professional and institutional investors who have a neutral view on the FTSE 100 and Eurostoxx 50 Indices over the next three years and are looking to capture a high yield whilst accepting risk to their capital.

Bearing in mind the FCA's view of structured products, the following potential drawbacks also need to be considered before deciding to invest in them:

- Capital could be at risk If the underlying index / securities are below a certain threshold at the end of the period;
- Annual returns / upside is often capped;
- Usually there is only one market maker and so liquidity (and hence the availability of efficient pricing) will be limited;
- The issuer of the product comes with some credit risk (even though it may have an investment grade rating);
- The products are often complex sometimes using derivatives to hedge the risks.

Conclusion

Structured products are not for everyone and potential investors need to ensure that they understand the structure they're buying into as well as the related risks. For the right kind of investor, however, we believe that they offer good diversification opportunities.

Please feel free to contact your Relationship Manager at Credo if you are interested in finding out more about structured products.

Greg Roediger - *Financial Director, Credo Group*

Servest Capital Raise

Credo is pleased to announce that Credo Capital Plc has raised £4.55m from its clients and the Credo Private Equity Fund to facilitate a further management buy in by the senior management of Servest Group Limited ("Servest") (a company incorporated in England and Wales). Servest's management will use the funds to acquire additional shares in Servest.

Credo looks forward to being a value added partner to Servest following the establishment of this commercial relationship with them.

Kenton Fine, Servest's Group chairman says, *"We are delighted by the introduction of Credo as a capital partner, supporting management's increased participation in the Servest UK business and look forward to building the relationship for mutual benefit as Servest continues to enjoy strong organic and acquisitive growth."*

Background

Servest is a leading facilities management provider employing more than 15,000 people, with a turnover in excess of £200m. Its core services include the self-delivery of cleaning, catering, security, pest control and grounds maintenance to over 4,000 sites throughout the UK.

With offices in London, Birmingham and Harrogate and with a group head office in Bury St Edmunds, the group is 74% owned by Servest (Pty) Limited and RMB Corvest, the shares of which are held through a UK holding company (Servest Limited).

Servest (Pty) Limited is a South African based multi-service group with turnover of R2bn. RMB Corvest is a mid-tier private equity house with around 60 portfolio companies. The remaining 26% of the group is owned by the UK management team.

To expand its service offering further, the group has added a building maintenance division following the acquisition of the mechanical and electrical maintenance business, Maxwell Stewart.

Acquisition rationale

The UK services sector is seeing a shift from companies procuring services in a traditional "silo" approach towards a more cost effective integrated, bundled or "pick and mix" style solution.

Organisations across all sectors, including public, retail, industrial and corporate, are looking to rationalise their supply chains and consolidate their services with one preferred partner. This brings with it many benefits, including one single point of contact for the customer, as Servest is skilled at managing a range of service lines, more efficient service delivery through multiskilling of the workforce and lower administration costs through consolidation of invoicing and reporting processes.

To ensure Servest is best placed to take advantage of this shift, it is expanding its service offering to take advantage of some short term opportunities, enabling it to continue to compete against competitors such as Mitie, Compass and ISS and most importantly to ensure that it is advantageously positioned for the short, medium and long term future.

Sara Ettlinger - *Communications Officer, Credo Group*

Credo on the move

In September 2013 Credo is moving its London office to Regent's Park.

Credo has been based at 83 Pall Mall, St James in London for the past five years.

Our new office will be the Nash building on the corner of York Gate and Marylebone Road opposite the Royal Academy of Music.

When architect to the Crown, John Nash, designed York Gate in 1822 as the grand entrance to Regent's Park, he designed two matching 'palaces' with Ionic facades, facing each other across the entrance road on the axis of St Marylebone Parish Church. York Gate itself was designed as five separate houses. The streetscape and building did not change much over the ensuing years.

We look forward to welcoming you to our new offices which are easily accessible from Baker Street or Regent's Park tube stations.

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