Unit Trust Model Portfolio Investment Process

Last Update : 31 March 2015

By Phillip Securities Research (Singapore)
Osama Bakhteyar, Investment Analyst

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By Phillip Securities Research (Singapore)
Osama Bakhteyar, Investment Analyst

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Investment Policy

The Model Portfolio's primary objective is to assure the safety of the principal by minimizing the downside risk and to focus on the income and growth of the portfolio. These two major goals are managed so to provide three different Portfolios with three different risk appetite and growth prospect (higher growth requires higher risk to be taken).

Risk Tolerance

Investment theory and historical capital market return data suggest that, over long periods of time, there is a relationship between the level of investment risk assumed and the level of return that can be expected. In general, in order to attain higher returns one must accept higher risk (e.g. volatility of return).

Given this relationship between risk and return, a fundamental step in determining the investment policy for the Model Portfolio is the determination of the amount of risk the Investor is willing/able to tolerate. In the world of investments, "risk tolerance" is measured by the degree of an Investor's willingness and ability to accept return volatility. "Aggressive" risk tolerance suggests that the Investor is willing/able to put up with occasional very negative returns in exchange for the opportunity to enjoy higher average returns.

"Conservative" risk tolerance suggests that the Investor will only put up with a narrow range of volatility, and in exchange is willing/able to accept lower average returns. Keeping this in view, three different Portfolios are commissioned for three different risk profile.

Model Portfolio Philosophy

Model portfolio will be managed using a semi-active approach, in order to generate positive alpha and to out-perform its benchmark indices. Although the analyst would hand-pick equity and bonds funds who have successful track records in their respective area, investor needs to understand that the results may range from above to below market results based on the skill of selection as well as the overall markets.

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Osama Bakhteyar, Investment Analyst

Part I : MODEL PORTFOLIO BUILDING BLOCKS

The basic tenets under which Model Portfolio will be managed include the following:

1. Modern Portfolio Theory, as recognized by the 1990 Nobel Prize, will be the philosophical foundation for how the portfolio will be structured and how subsequent decisions will be made. The underlying concepts of Modern Portfolio Theory include:

    - Investors are risk averse. The only acceptable risk is that which is adequately compensated by potential portfolio returns
    - For a given risk level, an optimal combination of asset classes will maximize returns. Diversification helps reduce investment volatility. The proportional mix of asset classes determines the long-term risk and return characteristics of the portfolio as a whole
    - Portfolio risk can be decreased by increasing diversification of the portfolio and by lowering the correlation of market behavior among the asset classes selected.

2. Investing globally helps to minimize overall portfolio risk due to the imperfect correlation between economies of the world. Investing globally has also been shown historically to enhance portfolio returns, although there is no guarantee that it will do so in the future.

3. Equities offer the potential for higher long-term investment returns than cash or fixed income investments. Equities are also more volatile in their performance. Investors seeking higher rates of return must choose the higher proportion equity portfolio, while at the same time accepting greater variation of results (including occasional declines in value).

4. Timing the purchase or sale of investments in the attempt to “beat the market” are highly unlikely to increase long-term investment returns; they also can significantly increase portfolio operating costs. Such practices are, therefore, to be avoided.

Given these tenets, the underlying approach to managing this Policy shall be to optimize the risk-return relationship appropriate to Investor’s needs and goals as defined under Model Portfolio with 3 different risk category namely: Aggressive, Moderate and Conservative. The Policy will be diversified globally where each Portfolio would entail different level of risk by managing the asset class allocation and the strategy allocation and the chosen asset classes will be periodically re-balanced to maintain a more consistent risk/reward profile.

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Osama Bakhteyar, Investment Analyst

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Strategic and Tactical Asset Allocation Strategy

- ***Strategic Asset Allocation***

The strategic allocation is the base of our Model Portfolio and helps minimize volatility and provide a diverse exposure into different asset classes. It is designed to provide investors with an appropriate risk/return profile over a longer period of time (typically between 2 to 5 years). The strategy involves setting a target allocations for various asset classes over a long period of time and then periodically monitor and rebalance it when the Portfolio starts to deviate from its target allocation. The target allocation is defined for the 3 Portfolios a range of allocations appropriate for various levels of risk tolerance. The strategy is compatible with the 'buy and hold' strategy. Hence, the long-term nature of strategic asset allocation implies that changes should take place infrequently.

One of the key reasons why strategic asset allocations do not often change is that the long-term risk and return expectations that are the basis for those allocations don't often change either. Although markets tend to be volatile and returns often diverge sharply from year to year, viewed over the longer term, the returns tend to become more stable, with gains in some years offsetting losses in other years. This suggests that the return and risk assumptions that form the framework of the strategic asset allocation process should be periodically evaluated and modified when the investment landscape has a material change, e.g., a shift in longer-term growth rates, a change in inflation expectations or a shift in risk premiums.

A robust process of estimating long-term risk and return expectations should therefore not be unduly impacted by near-term activity. In fact, frequent changes to long-term risk and return expectations could seriously undermine the investment discipline provided by a strategic asset allocation framework.

- ***Tactical Asset Allocation***

The right place to take into account near-term market activity is within a tactical asset allocation framework, which is designed to identify opportunities to periodically tilt the strategic asset allocations with a time horizon of typically 6 months to 1 year. Whereas the key drivers of strategic asset allocation are long-term risk and return expectations for various asset classes, tactical asset allocation focuses on such drivers as valuation, momentum, sentiment, the business cycle, political scenario, and fiscal and monetary factors, among others, to identify asset classes, sectors and

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Osama Bakhteyar, Investment Analyst

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investment styles that are expected to outperform in the near term keeping 6 months to a year in mind.

Temporary overweighting or underweighting of components of the strategic asset allocation can help enhance performance over time. These tactical allocation decisions vary with much greater frequency than changes in the strategic asset allocation weightings. However, even tactical rebalancing must be done in a disciplined manner, with consideration of the benefits, risks and costs.

- ### *Complementary Strategy of Model Portfolio*

A solid investment strategy highlights the role of both strategic and tactical asset allocation by specifying a strategic asset allocation as well as identifying a range for each component that specifies the boundaries of tactical overweighting or underweighting. The table below provides a simple example to help illustrate the distinguishing features of strategic and tactical asset allocation.

The strategic asset allocation provides the anchor to help ensure that long-term investment objectives are met, while the tactical range determines the magnitude of acceptable tactical "tilts."

While strategic and tactical asset allocation may differ in terms of time horizon and key drivers, they must be viewed as complementary components within our comprehensive Model Portfolio's investment framework.

Strategic Asset Allocation		Tactical Asset Allocation	
Description	A series of baseline portfolios appropriate for various levels of risk tolerance in a "neutral" state of the world	Description	Periodic "tilts" to baseline portfolios in response to market conditions with the object of increasing return and/or reducing risk
Time Horizon	Long-term	Time Horizon	Varies - Short-term: several months (trading ideas) - Medium-term: six months to two-three years (thematic ideas)
Key Drivers	Risk and return expectations for various asset classes	Key Drivers	Valuation Cyclical analysis (economic, earnings), timing, market sentiment

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Osama Bakhteyar, Investment Analyst

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Benchmark

Sector average of the Portfolios will be used as the benchmark.

Sector average – comprised by benchmarks from the underlying funds for the sector. Basically it takes the benchmark used by the funds and calculates a weighted average in proportion to the funds weightage in the portfolio accordingly.

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Osama Bakhteyar, Investment Analyst

Part Ii : RECOMMENDED PORTFOLIO RESEARCH PHILOSOPHY

Macro-Economic Research Process

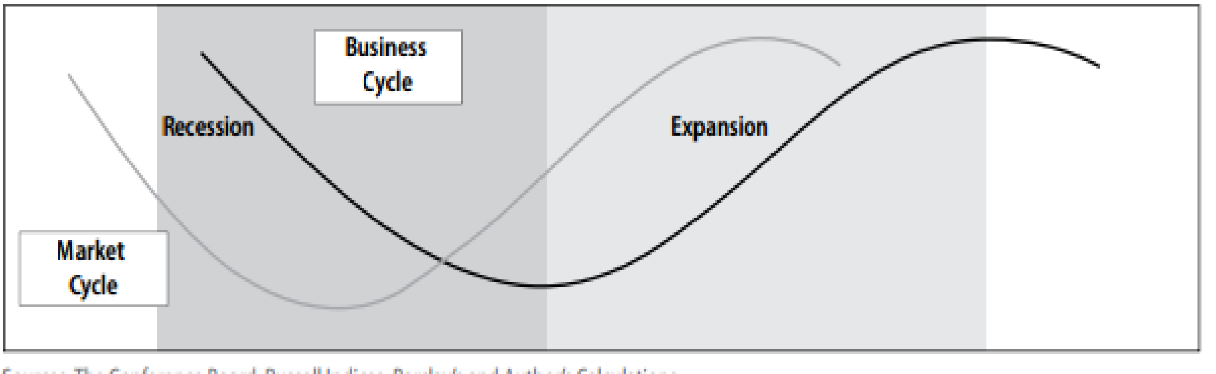
It all starts with having a macro perspective of the capital markets. From which we select the attractive asset classes for investment.

- ***Market Cycle***

Market cycles and business cycles are related, but they both have distinct attributes. The market cycle refers to the ups and downs of the financial market, while the business cycle refers to the ups and downs of the overall economy.

Even though the stock market is supposed to anticipate economic fundamentals, it is an imperfect predictor of the economy: market participants try to look forward, but their forecasts are not always, if ever, exactly correct.

Figure 1 | Schematic of Business Cycles and Market Cycles. For the business cycle, the vertical axis can be interpreted as "economic activity." For the market cycle, the vertical axis can be interpreted as the price of a market index.



Sources: The Conference Board, Russell Indices, Barclay's and Author's Calculations

Our macro market perspective largely stem from analyzing global economies and markets. In order to understand the market cycle, Research Analyst will be looking at GDP Growth, Inflation, Fiscal Policy, Monetary Policy, Structural Policy, Politics, Earnings, Earning Yield, Bond Yield, Corporate Yield, Commodities, Currency and other indicators.

- ***Business Cycle***

Economies do not grow in a straight line. Instead, economies typically fluctuate between periods of strong growth and weak or negative growth, known as the economic cycle or business cycle. Why these economic fluctuations take place is a complex subject, which has inspired many economic theories.

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Osama Bakhteyar, Investment Analyst

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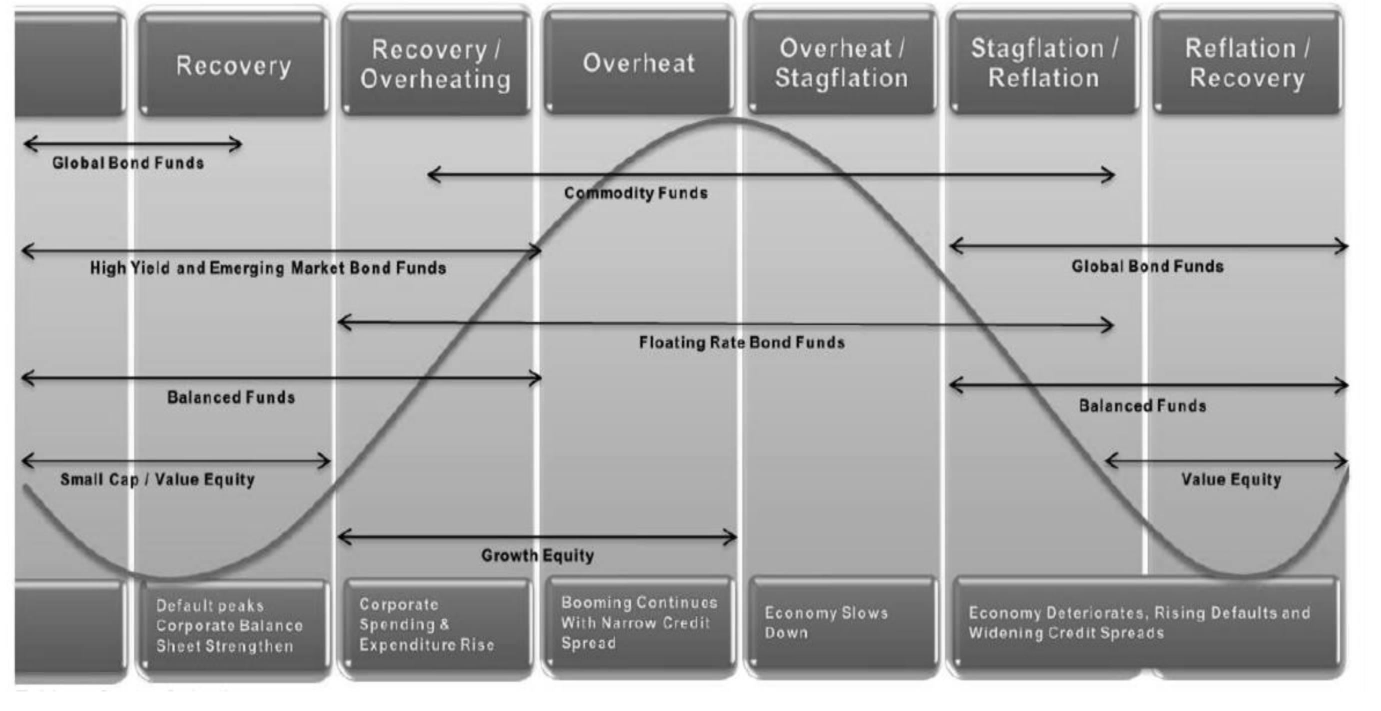
One widely held economic cycle theory is based on the relationship between supply and demand, and economic activity. The theory suggests growth in economic activity causes demand and prices for goods and services to rise. As goods and services become expensive, demand falls and economic activity slows down. This, in turn, causes goods and services to become cheap again, which leads to a new phase of growth in economic activity.

Usually lasting eight to ten years, the economic cycle is carefully watched by investors and analysts because it provides important clues about how financial assets, including stocks, bonds and commodities, may perform. As the economy shifts from one phase to another in the cycle, opinions on what is a fair price to pay for financial assets change. This is one of the reasons why financial markets fluctuate and we will be monitoring this as well.



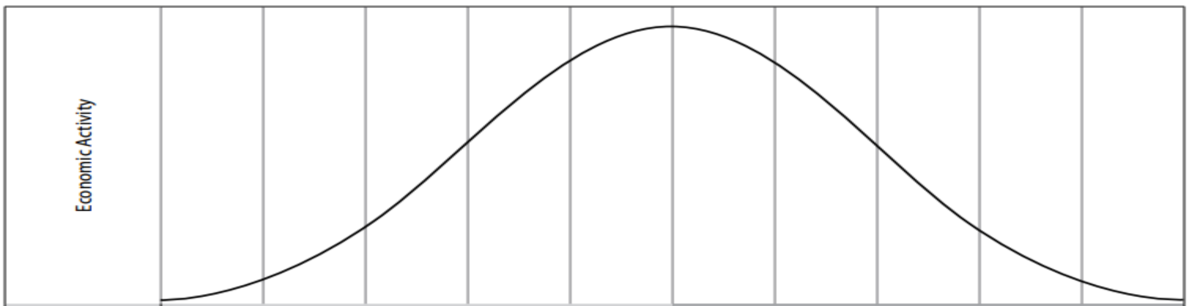
One common stock investment strategy used by investors is to try to time investments to match the economic cycle. This strategy is based on the belief that the stock market reflects the health of corporate profitability and the economy, so it will outperform when the economy is growing and underperform when the economy is contracting. While history tells us there is truth to this idea, it also shows us the relationship between the economic cycle and the stock market is not quite so simple.

So, the analyst will have to decide which phase of the business cycle the market and economy is and that will help formulate the asset class and sector allocation.

By Phillip Securities Research (Singapore)
Osama Bakhteyar, Investment Analyst

Part II : RECOMMENDED PORTFOLIO RESEARCH PHILOSOPHY

Historical Relationship Between the Business Cycle and Asset Class and Sector Performance



ASSET CLASSES	Recovery					Decline				
Bonds vs. Stocks	Stocks	Stocks	Stocks	Stocks	Stocks	Stocks	Bonds	Bonds	Bonds	Stocks
Large vs. Mid vs. Small	Small	Large	Mid	Large	Small	Large	Mid	Mid	Mid	Large
Value vs. Growth	Value	Value	Value	Value	Value	Value	Growth	Growth	Growth	Value
SECTORS										
Best Sector	Telecomm.	Info. Tech.	Financials	Info. Tech.	Telecomm.	Energy	Energy	Health Care	Energy	Energy
Second Best Sector	Utilities	Health Care	Telecomm.	Health Care	Utilities	Materials	Industrials	Consumer Stap.	Industrials	Materials
Second Worst Sector	Consumer Discr.	Energy	Health Care	Energy	Consumer Discr.	Health Care	Telecomm.	Telecomm.	Telecomm.	Health Care
Worst Sector	Health Care	Materials	Industrials	Materials	Health Care	Telecomm.	Financials	Utilities	Financials	Telecomm.

Sources: The Conference Board, Russell Indices, Barclay's and Author's Calculations

- ***Allocation Breakdown***

The allocation is designed taking care of the strategic allocation and the asset allocation combine together. All the allocations are given a corridor width of 10%. Three different risk appetite is taken into account

Risk Profile	Allocation Strategy		Bond	Equity
Conservative	Strategic	100	60	40
	Tactical	00	00	00
	Total	100	60	40
Moderate	Strategic	85	30	55
	Tactical	15	10	5
	Total	100	40	60
Aggressive	Strategic	80	15	65
	Tactical	20	5	15
	Total	100	20	80

The Asset Allocation weightage for these three different risk profiles are taken from academic empirical studies and experienced-based techniques. So for e.g. based on the utility theory combined with risk-adjusted returns a balance portfolio of 60/40 provides a reasonable allocation.

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By Phillip Securities Research (Singapore)
Osama Bakhteyar, Investment Analyst

Part II : RECOMMENDED PORTFOLIO RESEARCH PHILOSOPHY

Fund Selection Process

The entire Fund review Process involves soliciting information from a fund manager regarding three main factors:

- Performance (how good they are at it) - Quantitative
- People (who is running the fund) - Qualitative
- Process (how they are doing it) - Qualitative

These three criteria can simply be explained by conducting a through Quantitative and Qualitative analysis.

- ***Quantitative Analysis***

Once a macro view is built then accordingly funds are selected to in order to get the exposure in the relevant asset class, countries, sectors or styles, the initial analysis includes a thorough quantitative review of the strategy by the analyst. The analyst will review characteristics that include historical risk-adjusted return in relation to a relevant benchmark and peer groups. Sophisticated risk measures are also reviewed. These may include measures such as alpha, beta, sharpe ratios, Information Rations, sortino ratios and drawdown analyses to help ascertain a manager's ability to navigate a variety of market environments. If the fund possesses characteristics that analyst feels meets its best-in-breed definition, it will be subject to further review.

- ***Qualitative Analysis***

If a fund looks appealing on a quantitative basis, analyst will continue its review by focusing on qualitative characteristics to better understand the manager's organization and investment process. A qualitative review of the factors such as ownership structure, depth of staff, assets under management and growth trends in the firm's asset base are considered. The consistency of the firm's investment process, trading environment and risk management practices are critical. The manager's investment terms, operations and administrative policies, regulatory filings and compliance culture are reviewed. For this purpose if possible analyst would directly arrange meeting with the Fund Manager to understand more about the fund.

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Osama Bakhteyar, Investment Analyst

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- ***Some of the many Fund Selection Criteria for Investments***

Investment managers (Unit Trusts) shall be chosen using the following criteria (*Note: the list is not exhausted and other criteria may be considered depending on the need*):

- Length of time the fund/manager has been in existence and length of time it has been under the direction of the current manager(s) and whether or not there have been material changes in the manager's organization and personnel
- Qualifications and Experience of Portfolio Managers and Analysts. It includes their education history, complete Professional history including duration of term in present position and current position and responsibilities
- Size of the proposed fund
- List of investment clients for whom more than SGD20 million is being managed.
- Proposed management fee schedule including: Annual fees and method of computation, Payment schedule
- The issues involved the fund manager's: soundness of investment philosophy, likelihood of generating the expected results, consistency, compatibility with markets and modern portfolio theory, hedging and risk management procedures.
- The manager's adherence to investment style and size objectives
- In order to gauge the process a detailed description of management style would be required, including decision rules to buy and sell the security and screens or filters are used to develop subsets of the universe of securities that are portfolio candidates
- A detailed description of resources is to be checked including the software and technology being used.
- Past performance, considered relative to other investments having the same investment objective. Consideration shall be given to both performance rankings over various time frames and consistency of performance
- Market weighted duration
- Market weighted average maturity
- Market weighted average quality rating
- Cash and cash equivalents as a percent of portfolio assets
- Number of issues and proportion of market value represented by the largest 10 holdings
- Holding period return in most recent quarter
- Income yield over the period
- Capital Appreciation over the period

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- Risk Reward ratios such as the Sharpe Measure, Information ratio and Sortino Ratio over the period of 1 year, 3 years and 5 years.
- Capital appreciation over the holding period
- The historical volatility and downside risk of each proposed investment
- For each of the last 5 years, detailed proportional asset allocations quality rating with the duration computed for the portion of the portfolio assigned each quality rating.
- Market price/earnings ratio (Trailing 12 months and projected 12 months)
- Portfolio beta (Identify index)
- Proportional investment by broad industry grouping
- Proportional investment by exchange or security market
- Level of portfolio turnover measured as the lesser of purchases and sales each quarter as percent of average assets over the period.
- How well each proposed investment complements other assets in the portfolio
- The current economic environment
- The likelihood of future investment success, relative to other opportunities

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Osama Bakhteyar, Investment Analyst

Part III : RECOMMENDED PORTFOLIO RISK MANAGEMENT & REVIEW PROCESS

Risk Management

The portfolio service takes a medium-term view of investments, taking cognizance that a typical market cycle lasts between 4 - 5 years. The term structure of the Model Portfolio refers to a period between 2 to 5 years.

Exposure to systematic risk can be partially assessed without the risk manager's insights into the details of the daily portfolio through risk based factor models on the return time series of the fund.

But only transparency and position based risk management techniques enables control of manager specific (idiosyncratic) risk.

- The management of systematic risk needs to be distinguished from the management of manager specific risk.
- The corridor width of 10% is set for the asset allocation after which balancing of the Portfolio will be required.
- Not more than 30% can be invested into any single fund and incase the weightage crosses this limit than a rebalancing of the funds within the asset class would be required.
- Not more than 50% can be invested in a single fund house due to idiosyncratic risk and incase the limit is breached than it would require a rebalancing of the Portfolio.
- The analyst will take the decision to execute a cut loss policy on a fund when NAV has declined more than 20%
- Historical monthly VAR has to be calculated on monthly basis with a confidence interval of 95%. At any time it turns up more than 10% than the Portfolio will have to be balanced.

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Part III : RECOMMENDED PORTFOLIO RISK MANAGEMENT & REVIEW PROCESS

Fund Review Process

Investment performance must periodically be evaluated by the investor to assess progress toward the achievement of investment objectives as well as to assess Model Portfolio management skill. Fund Review Process typically comprises of the review of the portfolio relative to its peers and a review of the performance and risk characteristics relative to appropriate benchmarks. The analyst would pay keen attention to both qualitative and quantitative factors in the management research effort on an ongoing basis. Quantitative factors such as performance and various risk measures are reviewed on quarterly basis. In cases where the analyst believes qualitative changes to a manager's organization or investment process make it less likely that the manager will be able to replicate their past success, Analyst would recommend a replacement fund or strategy.

Portfolio Review Process

- ***Adjustment to Strategic Allocation***

Over time, semi-annual review will be required to review the basic allocation of the strategy allocation with the prevailing Macro perspective. In case of any changes to the basic allocation, updates will be provided with clearly guided justifications.

- ***Adjustment in the Tactical Allocation***

Constant review of the Tactical constituent is necessary and it should be conducted on a monthly basis and as and when opportunities and adverse events arise. There are two parts to this process. Firstly, we need to examine the existing components to determine if they are overvalued or if their fundamentals have changed. If so, switching out of these funds is necessary. Factors taken into consideration at this stage include (but not limited to) valuations, macro/political events, technical and other.

The second part of the process involves identifying new countries/sectors to be included in the Model Portfolio. This is done by looking at the Macro perspective once again. For every new country or sector to be included in the model portfolio, an initial coverage is necessary and so a brief report will be produced leading to it.

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Osama Bakhteyar, Investment Analyst

Part III : RECOMMENDED PORTFOLIO RISK MANAGEMENT & REVIEW PROCESS

Rebalancing Procedures

From time to time, market conditions may cause the Portfolio's investment in various asset classes to vary from the approved allocation. To remain consistent with the asset allocation guidelines established by the three Model Portfolio Investment Policy Statement, the analyst shall periodically review the Model Portfolio and each asset class in which the Portfolio is invested. This Portfolio will be rebalanced periodically as follows: Should any position move greater than 10%, it will be reviewed for rebalancing OR quarterly calendar re-balancing will take place. For example, suppose the policy allocation calls for an initial balanced portfolio with a 60% weighting to stocks and a 40% weighting to bonds. Suppose the value of the stock holdings then grows by 50%, while the value of the bond holdings declines by 10%. The new weighting is roughly 71% in stocks and 29% in bonds. To bring the portfolio back into compliance with investment policy, it must be rebalanced back to the long-term target weights. Disciplined rebalancing will have a major impact on the attainment of investment objectives.

The Fund and Portfolio's monthly, quarterly and semi-annually performance reviews provide a framework for ongoing communication to review progress being made towards stated investment goals.

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Osama Bakhteyar, Investment Analyst

APPENDIX:

Initial Model Portfolio Composition

Model Portfolio						
				Conservative	Balanced	Aggressive
	Strategic		**ISIN Code**			
Bond	Short Term	**United SGD**	*SG9999001382*	25.00%	15.00%	8.00%
	Sovereign/Corporate Debt	**Templeton Total Return**	*LU0170475312*	25.00%	18.00%	5.00%
	Emerging Market Debt	**UOB Emerging Market Bond**	*SG9999002174*	10.00%	-	-
Equity	US	**Fidelity America**	*LU0251142724*	10.00%	10.00%	12.00%
	Europe	**Templeton European**	*LU0323421163*	5.00%	7.00%	10.00%
	Asia – ex-Japan	**First State Dividend Advantage**	*SG9999002083*	15.00%	15.00%	20.00%
	Japan	**Lion Global Japan Growth (hedged)**	*SG9999011407*	5.00%	10.00%	15.00%
	China	**First State Regional China**	*SG9999000194*	5.00%	10.00%	10.00%
			Sub -total Strategic	100.00%	85.00%	80.00%
	Tactical					
Bond	High Yield Debt	**Allianz Income & Growth**	*LU0943347566*	-	7.00%	7.00%
Equity	Taiwan	**Fidelity Taiwan**	*LU0075458603*	-	8.00%	13.00%
			Sub -total Tactical	0.00%	15.00%	20.00%
			Total	100.00%	100.00%	100.00%
			Equity	40.00%	60.00%	80.00%
			Bond	60.00%	40.00%	20.00%

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