

**Brochure**



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CRD No.: 157964

SEC File No.: 801-72429

Date of Brochure: March 26, 2015

## Introduction

Harvest Global Investments Limited (“HGI”) is a Hong Kong company licensed under the Hong Kong Securities and Futures Ordinance to engage in Type 1 (dealing in securities), Type 4 (advising on securities) and Type 9 (asset management) regulated activities, and is regulated by the Hong Kong Securities and Futures Commission (the “SFC”). HGI is also registered as an investment adviser under the US Investment Advisers Act of 1940 (the “Advisers Act”) and regulated by the US Securities and Exchange Commission (the “SEC”). This brochure provides information about the qualifications and business practices of HGI. If you have any questions about the contents of this brochure, please contact us at +852 3913 3333. The information in this brochure has not been approved or verified by the SEC or any or by any state or foreign securities authority. Registration does not imply that HGI, or its associates, have attained a certain level of skill or training.

We encourage you to visit the SEC’s Investment Adviser Public Disclosure (IAPD) for more information about HGI. The IAPD web address is: [www.adviserinfo.sec.gov](http://www.adviserinfo.sec.gov).

## ITEM 2 – MATERIAL CHANGES

There has been no material change since the last update of the brochure in March 2014.

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## ITEM 4 – ADVISORY BUSINESS

### A. Description of the Advisory Firm

Incorporated in September 2008 in Hong Kong, HGI is a wholly-owned subsidiary of Harvest Fund Management Co., Ltd (“HFM”). HGI has been registered with the SFC in Hong Kong pursuant to the Hong Kong Securities and Futures Ordinance to conduct the regulated activities of 1) advising on securities (Type 4) and asset management (Type 9) since February 2009, and 2) dealing in securities (Type 1) since November 2010. Our parent company was incorporated in 1999 and is a significant investment firm headquartered in Beijing, China. The owners of HFM are China Credit Trust Co., Ltd, Lixin Investment Co., Ltd and Deutsche Asset Management (Asia) Limited. More information is available in our Form ADV Part 1.

We provide discretionary portfolio management services to our clients, sometimes with the assistance of HFM, serving as the investment adviser to pooled investment vehicles (“funds”) sponsored by other financial firms. We also provide investment advisory services on behalf of sophisticated institutional investors to separately managed accounts. We categorize our services as Fund Advisory and Separate Accounts.

We may in future provide portfolio management services to funds sponsored by HFM and may serve certain high net worth individuals.

While client investment mandates vary, our investment focus is largely on Asia, in certain cases predominantly on China, with limited amounts of investment in other markets. We may invest client assets across a range of investment classes, but, generally, investment focuses on equity and fixed income securities. We may also invest in derivative instruments, most often for hedging and portfolio management purposes. More information on the strategies we utilize, and the risks often associated with them, can be found in Item 8. Clients or investors should also consult the relevant offering document or investment supervisory agreement for a more complete discussion of risks and investment strategies.

In each case, we will provide services to our clients according to an executed Investment Management Agreement detailing client-imposed investment guidelines and, if applicable, restrictions.

### Client Assets

As of January 31, 2015, we manage the following assets:

Discretionary Assets (US\$'000)	US\$ 6,368,859
Non-discretionary Assets (US\$'000)	US\$ 24,547
<b>Total</b>	<b>US\$6,393,406</b>

## ITEM 5 – FEES AND COMPENSATION

### Fee Schedule

We do not currently impose a standard fee upon our clients.

Fees are as described in a particular Investment Management Agreement. As a rule, fees can be expected to vary based on factors including the complexity of the mandate, the amount of assets under management, the client's investment strategy and objective, whether the mandate is discretionary or non-discretionary and other factors.

In our sole discretion, we may vary the fee structure for certain large or strategic investors, including affiliates, and for HGI employees. We may also vary the fee structure in connection with promotional efforts or for other business development reasons.

#### **A. Payment of Fees**

Typically, management fees and performance fees (where applicable) are payable in arrears based upon the market value of the assets at the end of the preceding billing period. The billing period is negotiable depending upon the types of the mandate. Clients are generally billed for their management fees and performance fees (where applicable).

Other methods of payment and calculation may also be available, where appropriate or upon a client's request.

#### **B. Clients are Responsible for Third Party Fees**

There are other types of fees or expenses clients may pay in connection with our advisory services, such as custodian fees or transaction costs.

For example, clients may pay costs such as brokerage commissions, wire transfer fees, and other fees and taxes charged to brokerage accounts and securities transactions, which are unrelated to the fees we charge.

Item 12 describes the factors that we consider in selecting or recommending broker-dealers for client transactions and determining the reasonableness of their compensation (*e.g.*, commissions and/or spreads).

#### **C. Prepayment of Fees**

We collect our fees in arrears. We do not collect our fees in advance.

#### **D. Outside Compensation for the Sale of Securities to Clients**

Neither we nor our employees accept compensation, including sales charges or service fees, from any third-party for the sale of securities or other investment products.

### **ITEM 6 – PERFORMANCE-BASED FEES AND SIDE-BY-SIDE MANAGEMENT**

We may have performance-based fee arrangements with certain of our clients from time to time. Performance-based fee arrangements may create an incentive for us to recommend investments which may be riskier or more speculative than those which would be recommended under a different fee arrangement. These fee arrangements also create an incentive to favor higher fee paying accounts over other accounts in the allocation of investment opportunities. We have designed and implemented

procedures to ensure that all clients are treated fairly and equally, and to prevent this conflict from influencing the allocation of investment opportunities among clients.

## ITEM 7 – TYPES OF CLIENTS

We may provide services to a variety of client types. Clients include:

- Corporations; and
- Pooled investment vehicles, including US and non-US public investment companies for retail investors and private investment funds.

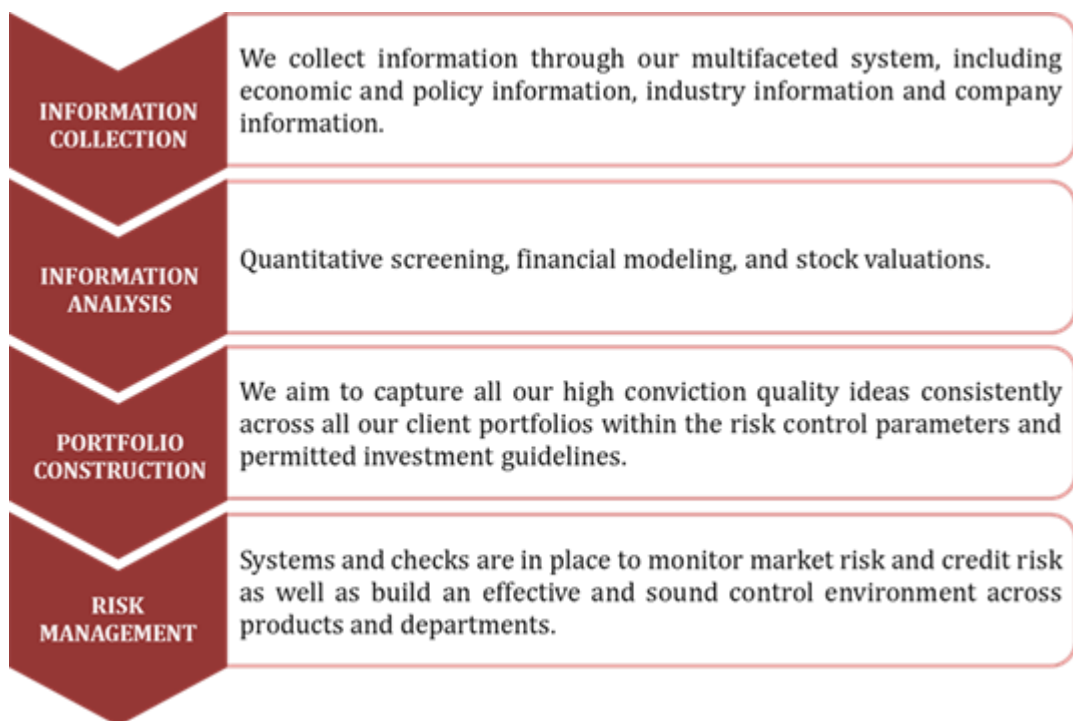
The relative percentage each client type currently represents is available on our Form ADV Part 1. The actual mix of types of clients may change over time based upon market conditions, business plans and other factors.

## ITEM 8 – METHODS OF ANALYSIS, INVESTMENT STRATEGIES AND RISK OF LOSS

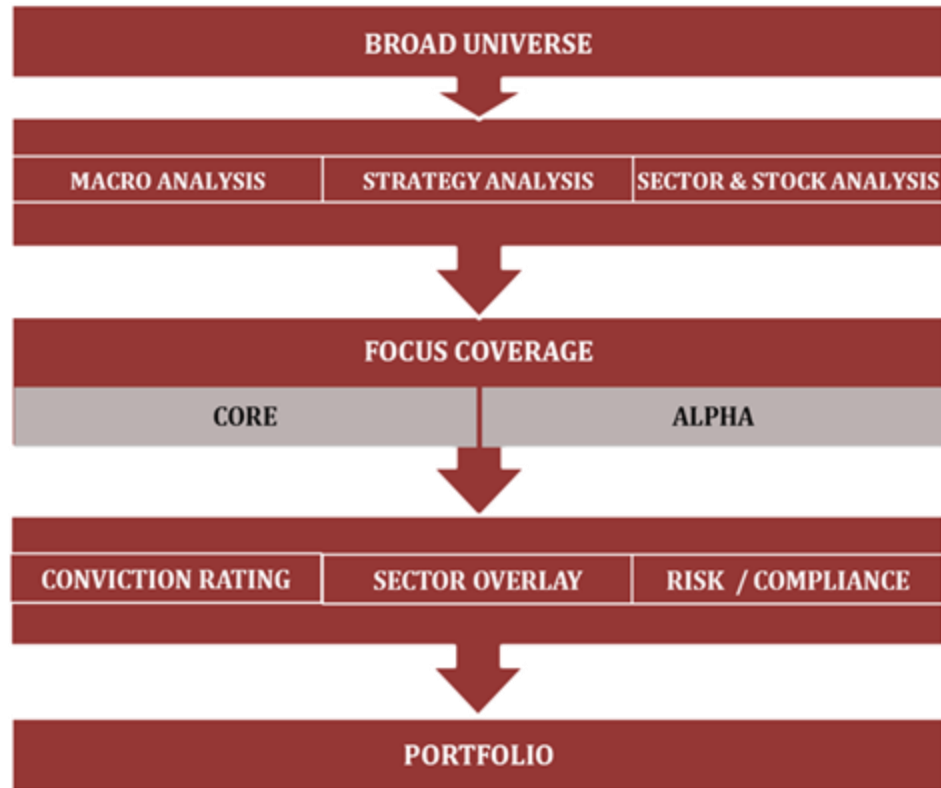
Our methods of analysis and investment strategies vary between the three investment universes we cover.

### Chinese Equities

The investment process can be defined by the following 4 steps:



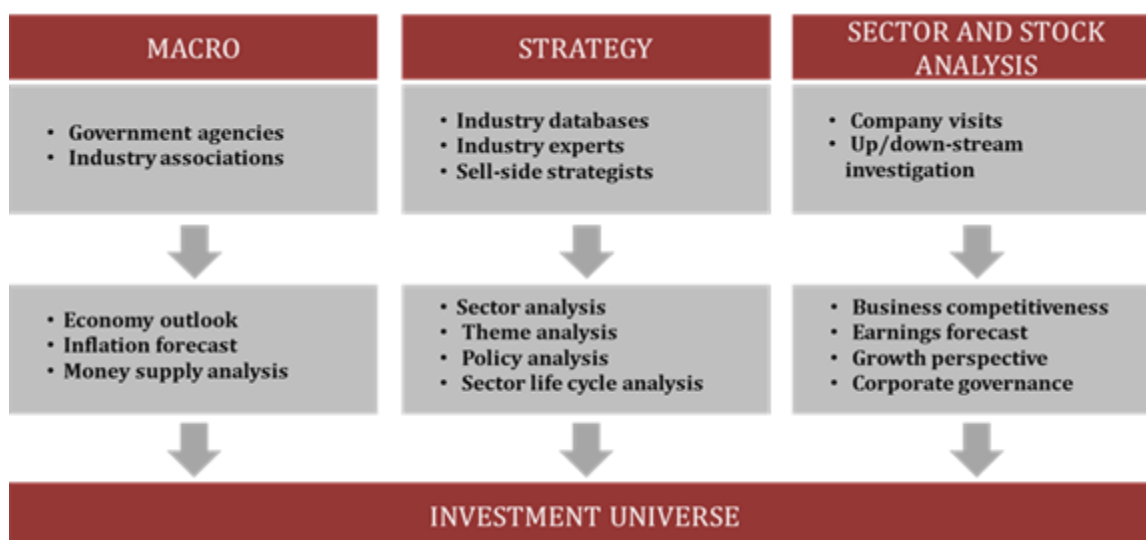
Overview of investment process



#### (I) Information Collection

We designed a multifaceted system to collect information including company information, industry information, economic situation and policy information.

Based on the analysis of information from government agencies and industry associations, we derive an overall economy outlook as well as a view of the impacts on the capital market taking inflation and monetary liquidity into consideration. Sector analysis, theme analysis as well as sensitivity analysis on policies are also undertaken to reach a sector strategy based on industry information.



We view company visits as the core of our investment process because it allows us to properly evaluate the quality of management from both a micro and macro perspective. The focus of sector and stock analysts will be on both qualitative issues (corporate governance, management quality, firm's overall competitive position and its relative strengths and weaknesses), as well as quantitative issues (return on capital employed, cash flow generation), when evaluating a business. As one of the leading asset managers, Harvest has significant contact with company management, suppliers, clients and competitors as well as maintains regular contacts with key decision-makers in listed companies. This enables us to get access to precious insights of company management and provides us with a firm understanding of the true underlying drivers of a company's long-term earnings potential.

Our investment universe consists of stocks within the MSCI China Index and other alpha accretive stocks that fit the strategy's investment objective.

## (II) Information Analysis

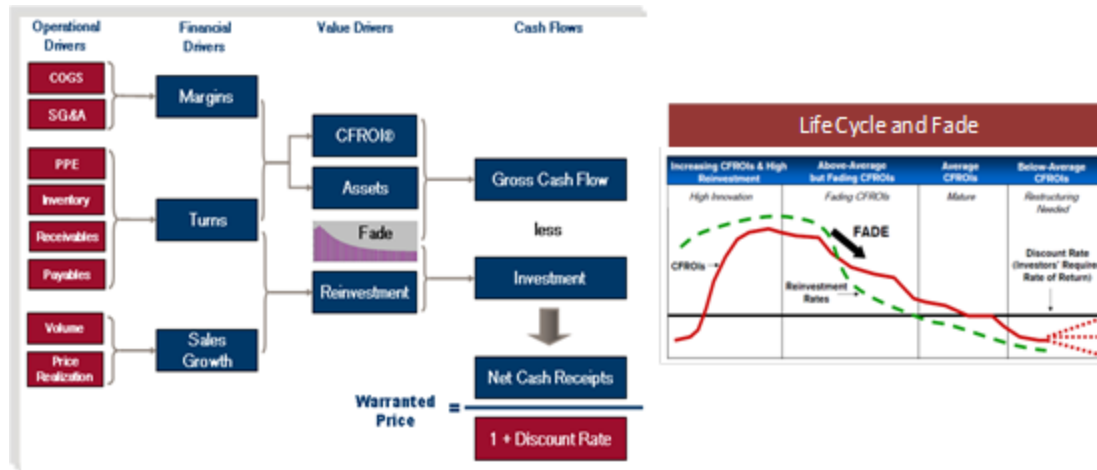
We take both a qualitative and a quantitative approach in our analysis and put a lot of emphasis on fundamental research. To enhance our fundamental research, we undertake quantitative screening using the HOLT system on a monthly basis as well as use the Linker-Thinker tool to do financial modeling.

- Core stock pool: includes companies with relatively large market capitalization and good liquidity. It covers about 80% of market capitalization of the MSCI China index.
- Alpha stock pool: includes middle to small size companies, companies with emerging importance (sub-sector leaders) and companies with short to mid-term catalysts.

Our central belief is that ultimately cash flow and Cash Flow Return On Investment (CFROI) which will determine share prices over the medium and long term. Therefore, we focus our efforts on identifying superior growth opportunities at reasonable valuations.

We use the Linker Thinker tool for valuing securities which allows further analysis on the drivers for liquidity, cash flow return on investment, asset growth and competitive environment. Based on the CFROI concept, this tool analyzes the life cycle of the company in a disciplined manner which distinguishes it from other typical discount cash flow model.





Although CFROI is a primary valuation methodology that we utilize especially for the non-financial sectors, we also believe that no isolated, single valuation approach allows a full understanding of a company. We therefore supplement the discounted cash flow analysis with other conventional valuations tolls which best suit the nature of the company's business model for example P/E (Price-to-Earnings Ratio) and EV/EBITDA (Enterprise Value to Earnings Before Interest, Taxes, Depreciation and Amortization).

The aforesaid model is utilized for selective sectors including consumer, telecom, Internet, healthcare, utility and industrial, which have relatively steady cash-flow streams. We do not use the model for financial companies (including bank, insurance and property), cyclical stocks (including commodity, airlines and shipping), and conglomerates. For these companies, we utilize other valuation methodologies including P/E (Price-to-Earnings Ratio), P/B (Price-to-Book Ratio), P/EV (Price to Embedded Value), and NAV (Net Asset Value).

The outputs of our analysis are stock ratings (1,2,3 for both short-term and long-term) and recommendations. Below is our stock rating outputs:

Stock Rating	Short-Term (6-month)	Long-Term (12-month)
1	Relative return to sector benchmark $\geq 15\%$	Absolute return $\geq 15\%$
2	$0 < \text{Relative return to sector benchmark} < 15\%$	$0 < \text{Absolute return} < 15\%$
3	Relative return to sector benchmark $\leq 0\%$	Absolute return $\leq 0\%$

In our recommendations, we specify investment opinions, horizon, catalysts, target prices (target returns) and potential risk. The rating will be tracked continuously as well as updated once the catalyst plays out, and any fundamental changes such as change of the company's strategy would trigger a review of the rating.

### (III) Portfolio Construction

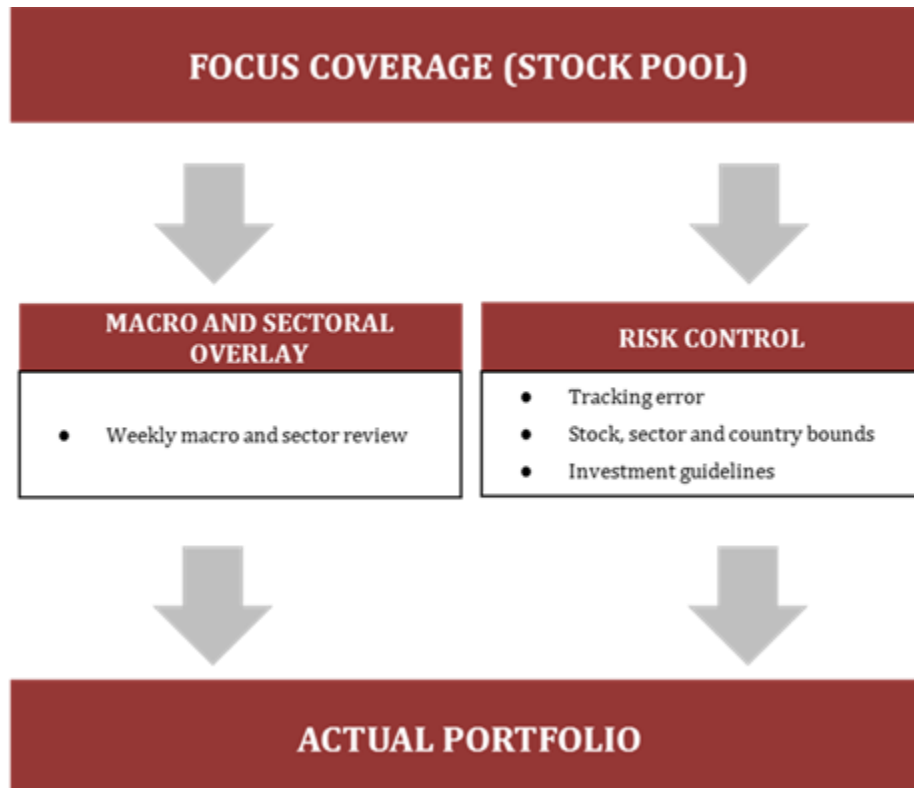
The functions of research and portfolio management are combined. Our portfolio managers are responsible for research and stock selection within their areas of responsibility, while they work as a team in portfolio construction.

We incorporate the following considerations in the portfolio construction process:

- Guidelines or restrictions and compliance requirements of the given investment mandates
- Potential risk/reward trade-off on the position
- Conviction level of a given stock and industry
- Liquidity constraints on the position
- Communication

Within the framework of the investment guidelines and restrictions, we consider the risk and return profile of all the stocks in the coverage, and take actions (overweight or underweight) for those we have a high conviction level.

Liquidity is another important factor we focus on during the portfolio construction process.



The sell-discipline operates within our investment process. In general, positions will be sold or reduced if:

- Any fundamental changes to the original investment theme, trend and sentiment occur; Fundamental situation for specific companies or sectors worsened; unfavorable changes to management, ownership or corporate strategy occur; or positive fundamental development is reflected by the share price.
- Superior prospects in other sectors or stocks arise from opportunity cost prospective
- Holding exceed the maximum risk budget.

While selling any position is not automatically triggered by these events, good explanations will be required to maintain the positions. A review will take place if stock price underperforms the country and sector benchmarks by >10% since initiation of the position.

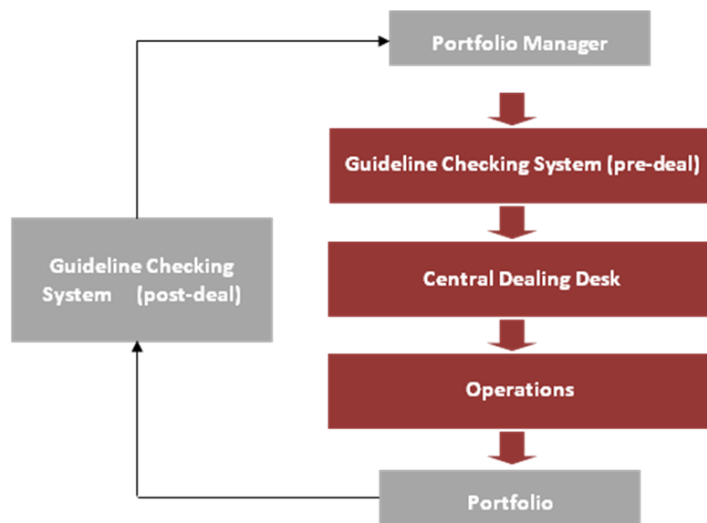
#### (IV) Risk Management

##### Risk Management

The goal of investment risk management is to monitor and analyze the investment risks and ensure timely communication with portfolio managers and senior management.

To achieve this goal, the risk management team has dedicated resources to oversee and monitor HGI's investment risk. Key risks and performance systems utilized are BarraOne, FactSet, Bloomberg, Morningstar Direct and Matlab

##### Trade Management



All trades are processed through our automated Guideline Checking System

- Pre-deal checking/warnings
- Post deal breach exception report
- Our dedicated compliance department monitors guideline compliance with client, regulatory and internal guidelines on an ongoing basis

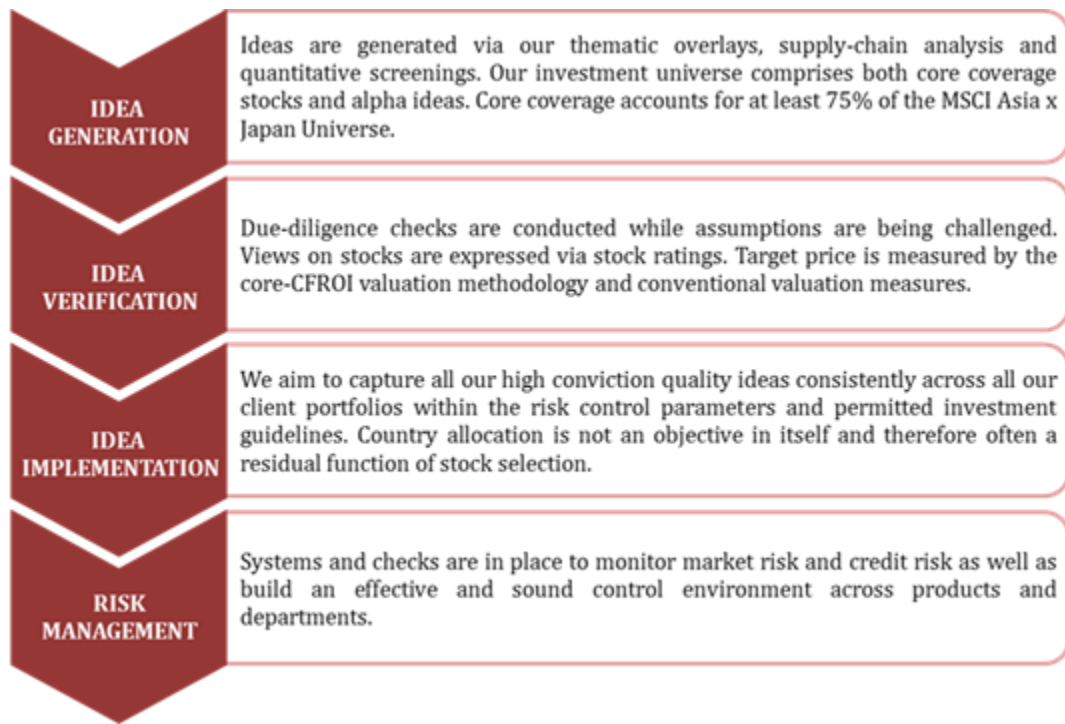
Investment guidelines are coded into the compliance module of the trading system and the Compliance Team is responsible for the pre-trade/post-trade compliance checks. Portfolio managers will be notified of any identified errors and breaches immediately and are required to take remedial actions in accordance

with the requirements of the client mandates and regulations, taking the clients' best interest into consideration.

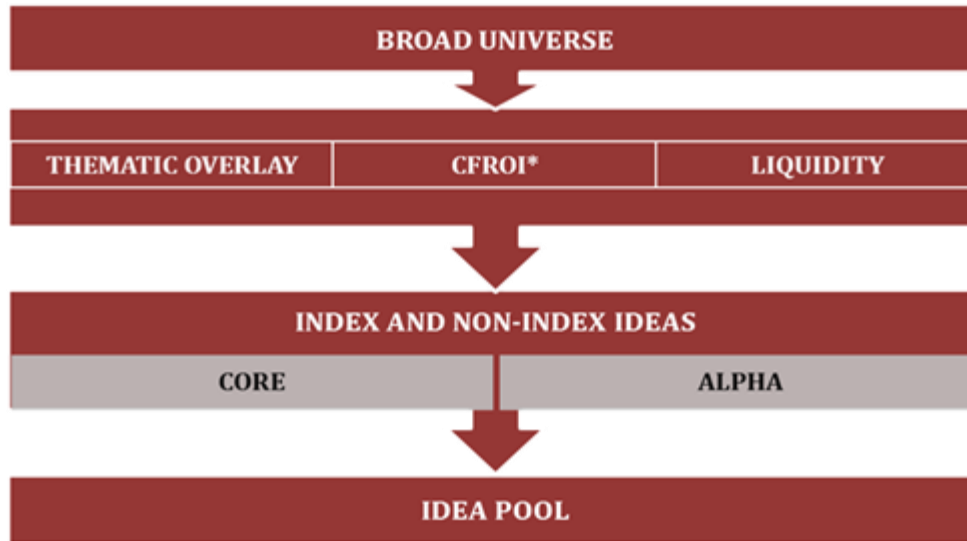
Compliance with investment guidelines are also monitored independently by an automated back-end system. This system monitors trades and portfolios post execution verifying that specific account/fund guidelines, regulatory requirements and risk exposure limits are followed. Exceptions identified through this process are escalated for proper resolution on a timely basis.

## Asian Equities

The investment process can be defined by the following 4 steps:



### (I) Idea Generation



The investment universe is made up of stocks within the MSCI AC Asia ex Japan universe and alpha accretive stocks that fit the portfolio's investment objective.

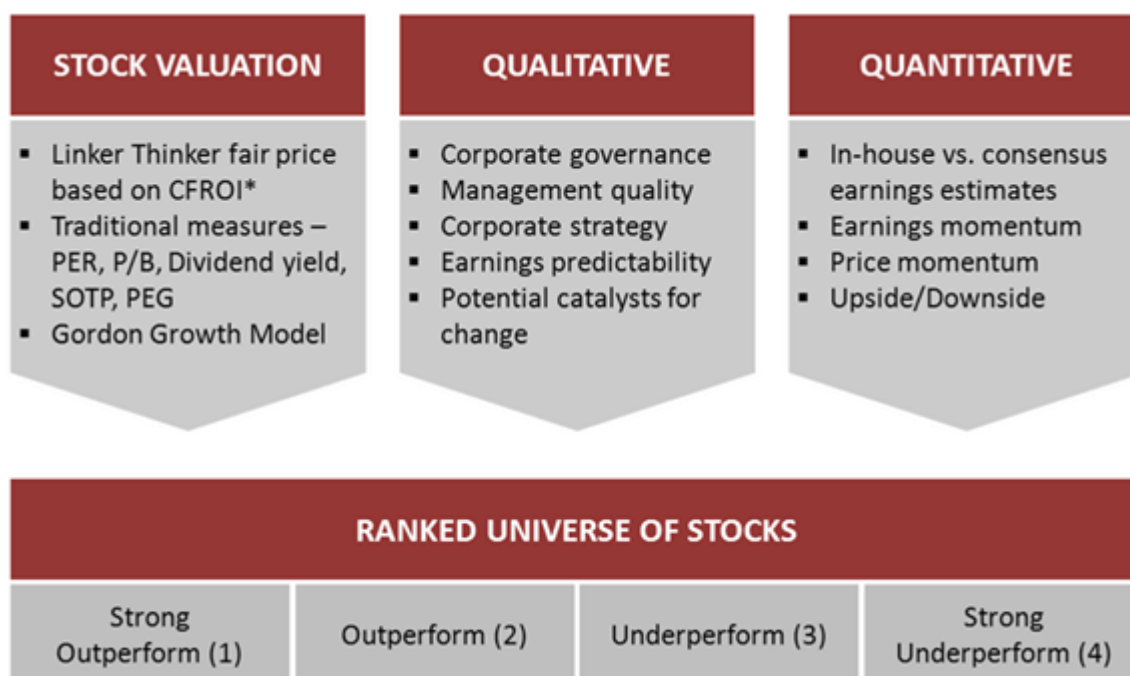
Investment ideas are often generated via our thematic overlays and supply-chain analysis. We perform quantitative screening using cash-flow return on investment (CFROI) and liquidity filter – daily turnover. We regard CFROI as a critical parameter in screening out companies with consistently poor cash flow for a prolonged period.

For thematic overlays, we conduct regular brain-storming sessions to identify and discuss structural as well as tactical themes namely, China Influence and Domestic Uncorrelated.

- In relation to China Influence, we believe that China will exert rising influence on other Asian economies and evaluate the impact of Scarcity, Liquidity and Policy themes on specific sectors such as material, energy, financial and consumer discretionary. We seek companies which can favorably benefit from the positive influence of China while avoid those which may or will be negatively affected by China.
- In relation to Domestic Uncorrelated, we observe the social and political dynamics within the markets in Asia outside of China and broadly categorise domestic uncorrelated opportunities as follows:-
  - consumerism – for example cultural specificity and middle class spending
  - Innovation – for example internet, automobile and smart phones
  - Inequality – for example social housing and transport network

A significant amount of our time is also spent interacting with companies in various industries to generate useful on the ground insights. Robust supply-chain analysis is widely performed whenever possible especially in the highly contested sectors such as technology, industrial and material.

## (II) Idea Verification



We verify our investment ideas through fundamental and financial due-diligence. We aim to further stream-line our investment universe into a focus coverage list. Our coverage will be at least 75% of the MSCI AC Asia ex Japan universe and the resulting focus coverage will comprise of both core stocks and alpha stocks. Core stocks are typically large-cap representative stocks within the respective country MSCI indexes. Alpha accretive names are companies which are either non-index e.g. newly listed companies or lowly represented in the indices. Target price, fundamental score and conviction ratings are generated during the idea verification process.

Our stock research focuses on our down-to-earth due-diligence at the corporate level. We ascertain our understanding of the business model (risk and rewards), competitive advantages and growth profile (secular or cyclical). Corporate interactions enable us to verify our financial assumptions, and qualitative facts and whenever possible, we also cross-check our findings with its customers, suppliers and competitors. Our conviction in a company may move in tandem with the level of our supply-chain analysis. Our portfolio managers and analysts maintain at least once a quarter interactions with the management of companies we invested by way of on-site company visits, off-site meetings and conferences.

We generate a target price from our internal financial assumptions of a company. Our investment style and process is based on the central belief that it is ultimately cash-flow and cash-flow return on investment (CFROI) which will ultimately determine share prices over the medium and long term. With this in mind, we focus our efforts on identifying superior growth opportunities at reasonable valuations. CFROI is the primary valuation methodology which we utilize especially for non-financial sectors. Reality checks are performed by making references to other conventional valuations like P/E, and EV/EBITDA. For specific sectors like financials, we evaluate banks and insurance companies based on the Gordon Growth Model (ROE-g/COE-g) implied P/B valuation and we value real estate companies based on RNAV (Revalued Net Asset Value). Often, we may have situations where we produce a probability weighted target price (best case, base case and worst case). Risk aversion is our guiding principle i.e. every unit of

risk should be compensated with more units of upside potential. This means that we would prefer a stock with share price of 30% upside and 10% downside compared to one with 60% upside with 30% downside.

We view that fundamental score has a lower correlation to the movements in the financial markets and we believe that in times of market volatilities, we can look beyond the noises to focus on these attributes. In the times of crisis or bear market cycles, it is not uncommon that the valuation of “good” and “bad” companies will converge. Management quality is the most important attribute we value in a company and we will not invest in companies which have corporate governance or credibility issues. We encapsulate the importance of management quality in our fundamental score. We do not express a view in the portfolio on a company with a poor management score even if it may have a chance of tactical outperformance. We may be contrarian at times on out-of-favor stocks especially those with good corporate stewardship and attractive risk-reward profile even if there are no specific share price catalysts.

Our fundamental score is weighted by 3 “right” attributes:

- Right theme (20%) – China influence and or Domestic Asia
- Right business (40%) - Business model, Competitive advantages and Growth profile (secular or cyclical)
- Right management (40%) – Corporate governance, track-record, interests alignment (e.g. share ownership)

The conviction rating (Strong Outperform, Outperform, Underperform, Strong Underperform) in relation to a stock is made relative to the country benchmark and based on a specific time horizon.

We focus on effective communication within the investment team. We have weekly research meetings for stocks to be presented by each analyst. All the relevant portfolio managers will attend the meeting and assumptions will be challenged. Company visit and corporate results update notes will also be circulated via the HGI Investment Group email system. All reports will be posted on the Harvest’s internal KM (Knowledge Management) system.

The investment reports will cover the following key areas:-

- Conclusion and Recommendation Action
  - What is the recommended action given the current stock price in the relevant investment context? Short versus long-term action? Stock ratings and Target price.
- Theme
  - Macro/Sector overlay or Structural growth/Deep value?
- Business
  - What are the fundamental drivers of the company?
  - Key investment characteristics and Business model/Competitive advantages
- Management
  - Ownership, track-record and corporate governance
- Valuation
  - How do we value it and what is the stock worth?
  - What is the best valuation methodology (CFROI, EV/EBITDA, P/E, EV/IC, EV/Sales, SOP)?
  - How does the current valuation compare to the stock's own history, the industry, the market?
  - What is a reasonable fair value range for the stock?

- Rewards
  - What are the triggers for the stock?
  - Differences from consensus? Surprise potential?
  - What would make the market take our view?
- Risks
  - What could go wrong for the stock?
  - Early warning and turning signals? Related stocks to watch?

### (III) Idea Implementation

The actual portfolio is constructed based on the inputs of the focus coverage, macro and thematic/sector overlay, risk control parameters as well as specific investment objectives and restrictions.

Our portfolio construction process aims to capture all our highest conviction ideas (i.e. Strong Outperform) within the stipulated country and sector limits. We implement all the stocks with “Strong Outperform” rating with an active bet of between 100 to 300 bps in the portfolio. We do differentiate stocks within the “Outperform” category by making reference to risk-reward target and fundamental scores.

Market allocation is often a residual function of our stock selection process. Sector allocation may be driven by the high-conviction researched stock ideas which we identified from our investment themes within the Chinese influence sectors such as commodities, industrial and technology. For instance, our commodities analyst may form a positive view on the coal sector after receiving the inputs from our dedicated Chinese A-share coal mining analyst post his field-trip in Qinhuangdao, the major commodities port in China. His positive view may translate into a preference for the Australian and Indonesian coal companies than the conventional Chinese names as the latter may lack the pricing independence from the government. This may in turn translate to our market overweight in Australia and Indonesia.

In terms of country and sector deviation limits, the country deviation limit should not be more than 5% or 2 times the country weighting in the benchmark (whichever is the lower) while the sector deviation limit should not be more than 8% or 3 times the sector weighting in the benchmark (whichever is the lower). We do emphasize the importance of monetary policy and political-social stability in the Asian markets and intervene in our market allocation during extreme market conditions especially in times of rising political and social risks.

Our investment process is largely macro-aware rather than macro-driven. Top-down factors play a secondary role in our investment decision-making process, but are reviewed formally, at the very least, on a monthly frequency, in order to maintain consistency with our overall investment view of the markets and sectors. Our market specialist will run the macro scorecard in 4 core areas –

**Growth** – Macro GDP and Earnings growth as well as the drivers

**Valuation** – Market and sector valuations

**Currency and Liquidity**

**Policy and Management** – Social and political stability



The macro-economic environment, political factors and currency views are incorporated into the portfolio control process and may lead to refinement of the country allocation results suggested by “bottom-up” criteria.

In general, positions will be sold or reduced if:

- Changes to the original investment theme, trend and sentiment occur
- Fundamental situation worsened – specific to companies or sectors
- Unfavorable changes to management, ownership or corporate strategy
- Positive fundamental development is reflected by the share price
- Superior prospects in other countries/sectors/stocks
- Holding exceeds risk budget

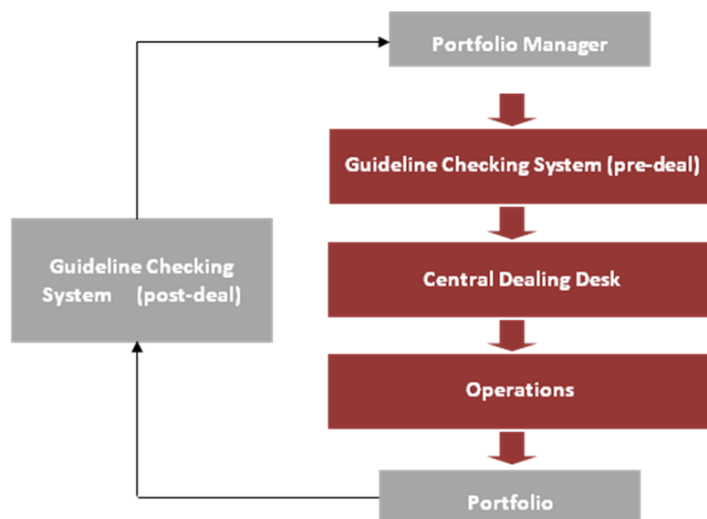
#### (IV) Risk Management

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## Fixed Income

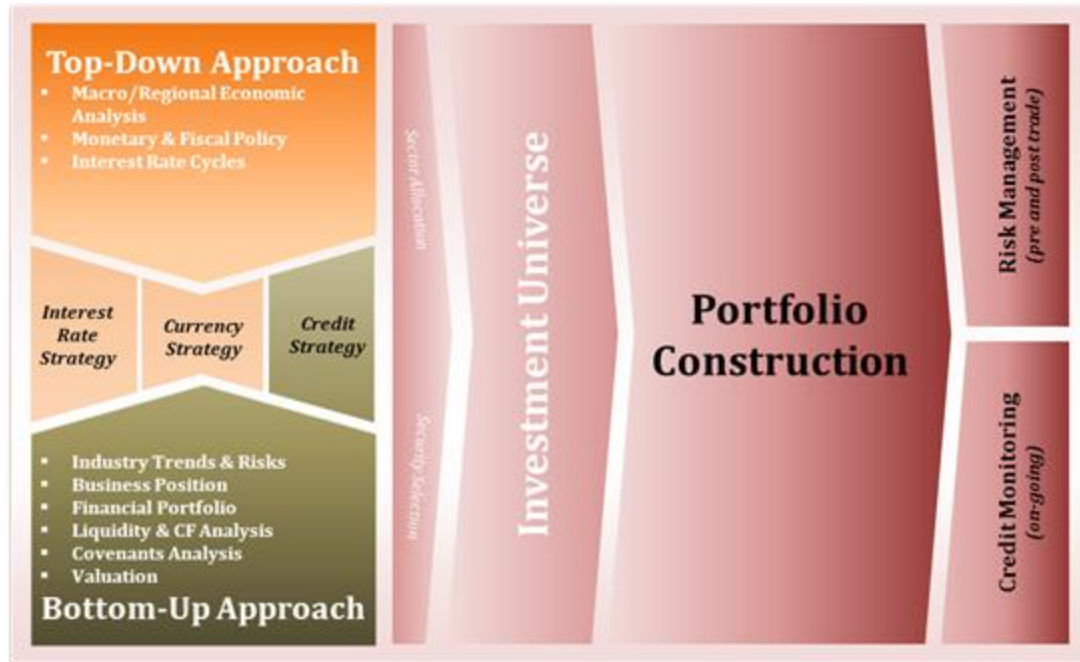
### Overview

Our investment process pursues a combined approach between top-down and bottom-up approaches.

In the top-down approach, economic data on a global, regional and local basis are taken into consideration (e.g. economic growth, monetary and fiscal policies and interest rate cycles) in order to identify longer-term macro trends and current themes which are likely to impact markets.

Central to our bottom-up approach is an internal rating process which was developed using Moody's rating methodology as a reference, which then incorporated with our sector views and strategies from the top-down approach. An overview of our investment process is described in the following graph:

## Investment Process



### Investment Strategy

The Fixed Income process begins with the formulation of the team's investment strategies, having regard to the economic and market developments at three levels, globally, regionally and locally.

Having regard to the likely scenarios and the relevant investment themes, medium to long-term forecasts are generated by the team. It is these forecasts, and the deviations of the market from these forecasts that is the primary method for identifying opportunities to add value over the medium term. Throughout our top-down & bottom-up approaches, we determine the portfolio's investment universe based on three core strategies, which are Interest Rate Strategy, Currency Strategy, and Credit Strategy.

#### Interest Rate Strategy

Within interest rate strategies, the Fixed Income Investment Team seeks opportunities from duration and slope management of interest rate risk, and relative value opportunities.

Our primary approach to interest rate risk management is to take strategic positions based on our fair value forecasts. However, where we believe we have a good understanding of the short-term factors, we will take tactical positions.

- i) Strategic positions are implemented when market prices do not reflect fair value based on our fundamental medium to long term economic analysis. The deviation of the central scenario forecast from current market pricing dictates sign and size of strategic duration/slope positions relative to benchmark.

- ii) Tactical positions are implemented when we have a strong conviction on short-term price movements, usually driven by technical factors such as market momentum, funds flow and individual data releases. These positions are undertaken on a discretionary basis.

In general, interest rate positions are predominantly strategic in nature. Forecasts of fair value bond yields are formulated having regard to macro-economic factors and idiosyncratic capital market developments and flows. These are consistent with the global economic, monetary policy and capital market themes identified in concurrent strategy sessions. A deviation of the forecasts from the market pricing will dictate the sign and size of the strategic local market duration position. Interest rate positions will need to be adjusted for liquidity constraints.

#### Currency Strategy

The Fixed Income Investment Team identifies fundamental, technical and behavioral factors which drive the value of currencies in the medium term. Within Asia, the themes identified in the global and regional macro analysis form the basis for our currency outlook. The global factor analysis approach is modified to cater the most relevant drivers in each regional currencies.

The team prepares currency forecasts that incorporate not only the themes from our global and regional macro analysis, but also the assessment of medium term currency valuations within the region with considerations of macroeconomic, policy, and capital flow developments as relevant.

Deviations from our medium or long-term forecasts are used to identify potential investment opportunities.

#### Credit Strategy

The development of credit strategies is a combination of top-down and bottom-up analysis. The evaluation results from both analyses have a direct input into sector allocation and credit selection at the portfolio construction stage.

##### *Top-down evaluation:*

We identify longer-term trends and current themes which likely to impact markets during the investment period. Analysis of economic, credit and market-specific factors both globally and regionally allows us to determine how much credit to allocate to the portfolio.

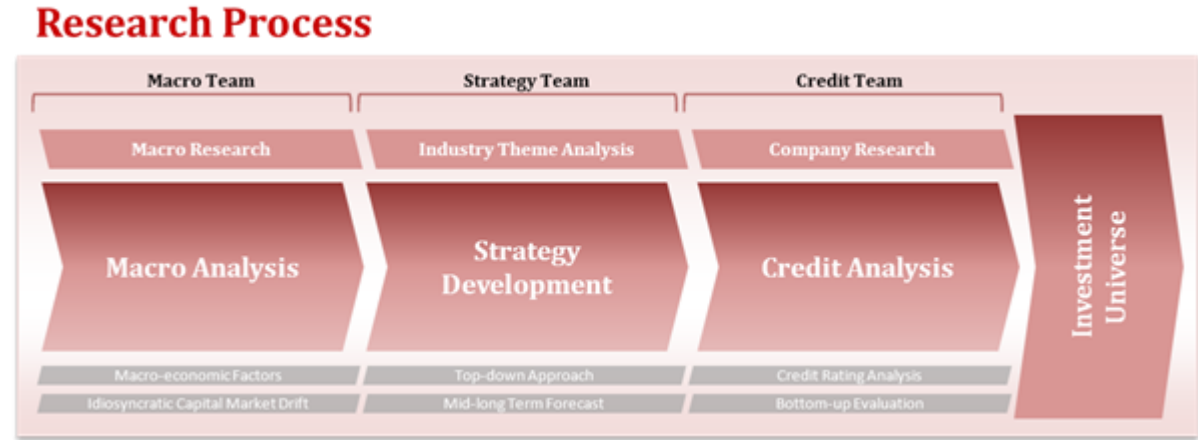
We leverage the resources of our Macro Strategists and Credit Team in HFM, and our regional investment teams within HGI, to determine the key drivers of global, regional and local credit markets.

##### *Bottom-up evaluation:*

Central to our bottom-up credit evaluation, is an internal rating process. In undertaking credit analysis, we utilize the resources of our Credit Team in HFM and regional equities teams in Hong Kong.

#### **Research Process**

The research matrix is the core process within our investment practice as this provides us valuable information in order to capture the market opportunities. We have designed multi-faceted system linked to all research groups. Three main groups contribute to the research process, namely the Macro Team, Strategy Team, and the Credit Team:



#### Macro Research

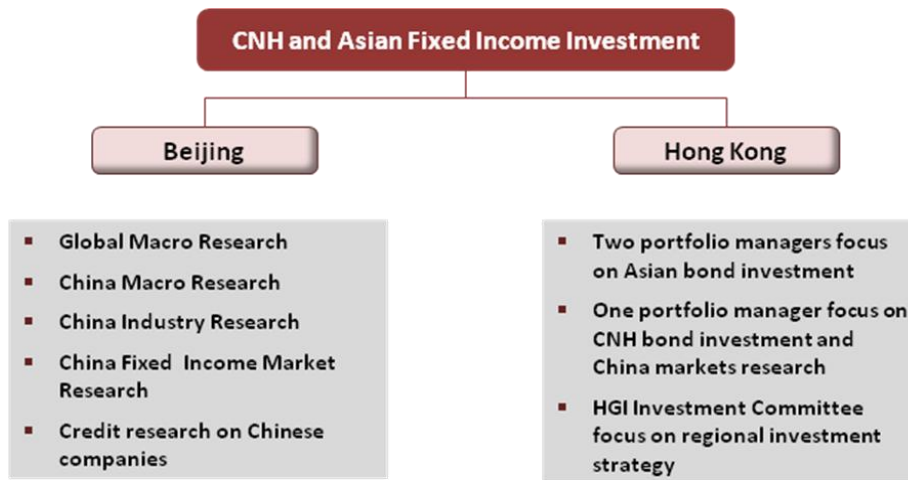
The first step of our research process is an analysis of the macro-economic environment which is undertaken by the Macro Team. Data is gathered from multiple parties such as government agencies, industry associations, and external resources platform. The team will then conduct macro analysis on global and regional economic growth and money supply figures, based on domestic macro-economic factors and idiosyncratic capital market developments and flows. Interest rate forecast, currency forecast, and inflation forecast will be conducted in order to provide both long and short term market outlook to the rest of the team. Note that all research information is uploaded to our Knowledge Management (KM) System which ensures communication for information exchange among teams.

#### Industry Theme Analysis

The Strategy Team will utilize the market view from our macro team, to conduct a second layer of thematic analysis and sensitivity analysis in relation to different industries and sectors. Here, a Top-down Approach will be applied. Information extracted from industry databases and inputs from industry experts as well as sell-side strategists are also factored into review. The last stage is a sector life cycle analysis from which the investment strategy will be determined.

#### Company Research

Once the investment strategy has been developed, the Credit Team will perform a credit analysis through a Bottom-up evaluation process. This includes the industry trends, risks, business position, financial profile, liquidity and cash flow analysis, covenants analysis, and valuation of the possible investments. The result provides a clear picture on the valuable names which will be included into the investment universe and will be considered during the portfolio construction stage.



### Portfolio Monitoring

The credit monitoring and risk management process are also conducted throughout the investment process. It is very important to keep track of the credit rating and risk figures of the securities in order to keep our investments within the portfolio investment constraints. The credit monitoring is an on-going process and will be performed by the Credit Team. For risk management, a pre-deal and post-deal check will be conducted.

On an ongoing basis the risk Management Department access and monitor portfolio risk (mainly liquidity and counter party risks) according to changing market situations. Risk Management teams are also responsible for monitoring and producing portfolio risk analysis report. The goal of investment risk management is to monitor and analyze the investment risks and ensure timely communication with portfolio managers and senior management about the investment risk. To achieve this goal, the risk management team has dedicated resources to oversee and monitor HGI's investment risk. Key risks and performance systems are BarraOne, FactSet, Bloomberg, Morningstar Direct and Matlab. Compliance is also responsible for daily monitoring of the investment process.

### Sell-Discipline

The sell-discipline operates within our investment process. In general, positions will be sold or reduced if:

- Fundamental
  - Changes to the original investment theme, trend and sentiment occur
  - Fundamental situation worsened – specific to macroeconomics

- Unfavorable changes to credit of corporate bonds, market liquidity and supply and demand shocks
- Positive fundamental development is reflected by the price
- Opportunity Cost
  - Superior prospects in other sectors/bonds
- Risk control
  - Holding exceed the maximum risk budget

While selling any position is not automatically triggered by these events, good explanations will be required to maintain the positions.

## ETF

### Investment Strategy

Currently our ETFs adopt a full replication approach of buying all constituents of the index to track the benchmark.

The key objective is to track the performance of the underlying Index as closely as possible by conducting a passive quantitative based investing technique, using replication to achieve similar risk return characteristics to the Index. This kind of strategy can be effective in reproducing the return profile of the index while pursuing a low tracking error.

### Investment Process

#### (I) Portfolio Construction:

Our investment management process is relatively simple and fully represents the degree of diversification that the index embodies. However, various market specific factors and circumstances may result in differences between the ETF and the index composition from time to time. These factors include: the effect of subscriptions and redemptions, underlying stock weight adjustments, legal restrictions on investment shares, transaction costs, stock dividend distribution, share allotment and issuance of new shares.

The requirement to purchase stocks in lots as well as other restrictions can also cause the ETF to lag or be biased to an extent, especially when the target index has a large number of the constituents – in that case the frequency of adjustment and time delay can be an important factor. In addition, when stocks have been suspended for a prolonged period of time or delisted, a full replication strategy will inevitably face situations where its return will deviate from the index and therefore ultimately cause tracking error.

#### (II) Portfolio Rebalancing:

On a daily basis the fund manager rebalances the portfolio according to the day's net flow based on the underlying stock holdings' weights provided by the index provider. The investment team utilizes Harvest's

passive investment system to monitor not only the average daily tracking error but also the accumulated tracking difference as well. The investment team closely tracks any corporate actions of the underlying stocks and takes corresponding actions. The reasons for rebalancing can be categorized as follows:

- **Change in index constituents**

The index is reviewed by the index provider on a regular basis and the review may result in additions, deletions, and changes in the index constituents. All changes will be pre-announced before the effective date. The fund manager will analyze the potential weighting changes for the portfolio holdings. In case of weighting change for one typical stock, the fund manager will consider a number of factors to achieve the target weighting prior to the effective date, including the 3-month average trading volume, the significance of the index component and potential trading impact. The fund manager can also decide the trading strategy, for example in the case of illiquid stock, the fund manager might split the order into several trading days before the effective date, and get to the target weight incrementally.

- **To minimize tracking error**

On daily basis, the fund manager is updated with the tracking error analysis of the ETF. Under different market condition, the fund manager may set the corresponding alert level, for example daily tracking error above 50bps or annualized tracking error above 3%, the fund manager will look into the attribution analysis of the tracking error then decide whether to adjust the portfolio holdings accordingly, usually the attribution could include dividends received, trading P&L, positioning variance from the index weights, and cash drag, e.g. if portfolio variance arises, sector overweight/underweight comparing to underlying index over 2%, the fund manager would initiate the portfolio rebalancing to minimize the deviation.

- **Adjust cash portion in the portfolio**

Our ETF will maintain a relatively low level of cash in order to effectively track the index. When cash level reaches above 1% or below 0.2% in the portfolio, the fund manager could initiate the portfolio rebalancing to adjust the asset allocation.

### **Risk management process**

We have stringent and comprehensive risk management procedures in place with details set out as follows:

#### **(I) Portfolio Construction**

The main objective is to minimize the index tracking error. A comprehensive suite of portfolio risk control tools had been built into the portfolio management to ensure that the HGI Passive Strategies Team can replicate index performance in an effective and efficient manner.

#### **(II) Risk Monitoring**

The principle of this risk control is to have an independent risk oversight by Risk Management team. Tracking error monitoring is performed on daily basis by HFM Risk Management and a threshold structure is introduced:

Warning Threshold	Final Threshold
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1.5% (annualized)	3.0% (annualized)
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If any of the thresholds is breached, the HGI Investment Team and HGI Risk Management will be notified by HFM Risk Management and in case the final threshold is breached, an immediate assessment of corrective action or rationale for such high risk from the HGI Passive Strategies Team would be compulsory. HGI Risk Management and HFM Risk Management together with HGI Senior Management may enforce risk reduction trades based on the finding of the risk assessment.

**Investing in securities involves risk of loss that clients should be prepared to bear.**

## ITEM 9 – DISCIPLINARY INFORMATION

We, our parent firm, and/or the companies which own our parent firm, particularly those that are substantial financial services firms, may be involved from time to time in regulatory matters or litigation that arise in the ordinary course of the business. None of which is material with respect to our investment management business or our clients.

## ITEM 10 – OTHER FINANCIAL INDUSTRY ACTIVITIES AND AFFILIATIONS

Our sole business is providing investment advisory services and we are not engaged in any other business.

We work closely with our parent company, HFM, in providing certain services. For instance, we may work together with HFM to manage client portfolios and provide related services, including client liaison, investment monitoring, account administration, investment research, and trading services. Where employees of HFM are involved in providing advisory services to US clients, these duties are subject to a Participating Affiliate Agreement (the “PAA”) between HFM and HGI. Under the terms of the PAA, these employees of HFM are subject to the supervision of HGI in the performance of such duties, and they are subject to certain aspects of our Code of Ethics as described in Item 11. HFM is also subject to books and records requirements and to other requirements relating to the PAA.

Deutsche Asset Management (Asia) Limited (“Deutsche Asia”), an investment adviser located in Singapore and a member of the Deutsche Bank Group (“Deutsche Bank”), is an owner (30%) of HFM. We provide advisory services to Deutsche Asia and its related entities as sub-managers (i.e. sub-advisers) to funds it or its related entities sponsor and mandates for which it or its related entities act as investment advisers. We also directly advise a Deutsche Bank entity. In addition, we have entered into contractual arrangements with certain Deutsche Bank entities that may solicit clients for us subject to the requirements discussed in Item 14.

We conduct brokerage through one or more Deutsche Bank broker-dealer firms. To address the conflict of interest this presents, we will only utilize Deutsche Bank as a broker-dealer subject to the considerations of best execution discussed in Item 12.

Other firms with a substantial ownership stake in HFM are financial services or holding companies in the People’s Republic of China. Due to the extensive nature of these firms’ holdings, we may conduct business with a firm affiliated to these firms, either intentionally or inadvertently. We do not assign

resources to monitoring the holdings or affiliates of these firms, and would conduct our business with such affiliates or investee companies on an arm's length basis, as with any other third party.

## ITEM 11 – CODE OF ETHICS, PARTICIPATION OR INTEREST IN CLIENT TRANSACTIONS AND PERSONAL TRADING

We maintain a Code of Ethics adopted under Hong Kong law but consonant with Advisers Act Rule 204A-1 which (i) sets forth standards of conduct expected of advisory personnel, (ii) sets forth our policy for safekeeping material, non-public information, and (iii) requires certain of our employees, officers and directors to comply with clearance requirements with respect to personal securities transactions and reporting requirements. Copies of our Code of Ethics will be provided to any client or prospective client upon request. In addition to our home country policies and procedures, our activities and the activities of our advisory personnel with respect to US clients are governed by a US Compliance Manual detailing our obligations under the Advisers Act and other relevant US law and regulation. All new employees with US client responsibilities are furnished with a copy of the Code of Ethics and US Compliance Manual upon the commencement of their employment, and must signify their understanding and acceptance of the documents by completing and returning an attestation to the Compliance Department.

Employees of HGI may, from time to time, buy or sell securities that we recommend to clients for their own accounts. Such employees must do so in accordance with our personal trading policy. The objective of this policy is to ensure that a personal account transaction undertaken by any employee does not conflict with our regulatory obligations and fiduciary duties to our clients. This would include ensuring that all personal account transactions do not conflict with, or take unfair advantage of the funds under management, as well as ensuring that employees handle price sensitive information in an appropriate manner that would not constitute any breach of regulations or duty.

Employees who wish to carry out transactions in reportable securities in any of their personal accounts (including the accounts of their spouse and dependent children) ("Covered Accounts") must, unless an exception is available under Advisers Act Rule 204A-1, obtain prior approval by submitting a request to our Compliance Department.

Approval will be given only if there is no conflict between the Covered Account transaction and the transactions of our clients.

We maintain a log of material conflicts and the means to address/resolve them, which we review on a regular basis.

## ITEM 12 – BROKERAGE PRACTICES

### A. Soft Dollars

We may pay a broker a commission higher than another broker may have charged in recognition of the value of the research and/or brokerage services provided by that broker. This practice is referred to as "soft dollars" in the US and "soft commissions" in certain other jurisdictions. Various types of research and brokerage services may be obtained with soft dollars including, among other things, research and analytical information that we use in the investment decision-making process. We may choose to place a trade with a particular broker when, for example, a research analyst at that broker has given us valuable

investment advice. We benefit from these arrangements because we do not have to produce or pay for the research or services received. In selecting a broker providing research or brokerage services to execute client transactions, we will make a good faith determination that the amount of the commission charged is reasonable in relation to the value of the research and brokerage services received.

Our use of commissions or soft dollars to pay for certain research products or services is expected to fall within the safe harbor created by Section 28(e) of the U.S. Securities Exchange Act of 1934. The products or services received from brokers as a result of a client's transactions may be used by us in servicing other accounts.

We are also authorized to utilize client commissions for other purposes and under other circumstances consistent with applicable law.

#### **B. Client Directed Brokerage**

Some advisory clients may direct us to execute trades with a specific broker-dealer. We will only honor these requests subject to our regulatory obligations, including best execution.

In these cases, we may not be able to aggregate such client's transactions with similar transactions of other clients. There can be no assurance that the directing client will realize the same price or commission rate achieved for other clients. Due to the higher commission rates often paid on directed accounts, clients should be aware that account performance may be negatively impacted. Furthermore, higher commission rates will negatively impact returns when we rebalance accounts.

In any event, we do not receive client orders to buy or sell securities nor do we make ourselves amenable to do so. We are not a broker-dealer.

#### **C. Aggregate Trade Allocations and Trade Errors**

We will generally execute transactions on an aggregated basis when we believe this will allow us to obtain best execution and negotiate more favorable commission rates or other transaction costs that might have otherwise been paid had such orders been placed independently. When aggregating orders, all of our clients will be treated in a fair and equitable manner. We will not aggregate orders unless aggregation is consistent with our duty to obtain best execution. No account will be favored over any other client; however, a variety of factors are determinative of whether or not a particular client may or may not participate in a particular aggregated transaction. These factors include, but are not limited to: investment objectives and strategies, position weightings, cash availability and/or risk tolerance. Because of differences identified above, there may be differences in invested positions and securities held which could lead to security dispersion among client accounts.

When we determine that order aggregation is in the best interest of our clients, the following guidelines generally are followed for all portfolios which are participating in the execution under the same trading circumstances (*e.g.*, price limits and time of entry). Aggregated orders filled in their entirety, or partially, will be allocated within strategy among the participating accounts *pro-rata* by account market value. In the event of a *de minimus* allocation for a partial allocation, the trader has the authority to determine an appropriate allocation methodology.

Consistent with our fiduciary duties, our policy is to exercise care in making and implementing investment decisions for client accounts. We have a trading errors policy. To the extent trading errors occur, we seek

to ensure that clients' best interests are served. Our policy is to resolve all trade errors within a reasonable time while ensuring the client is not disadvantaged, consistent with the orderly disposition (and/or acquisition) of the securities in question. As a general matter, actual losses suffered by a client account as a result of a trade error caused by us will be reimbursed by us; however, as a general matter, we do not compensate clients for lost investment opportunities (*e.g.*, failure to take advantage of investment or market improvements).

#### **D. Brokerage Partners and Best Execution**

We seek the best price available along with the most favorable execution on each order placed on behalf of our clients ("best execution"). We believe that the key components for achieving the most favorable net results are transaction specific and dependent upon the experience of the executing and clearing broker, including its reliability, reputation in the industry, financial stability, capital commitment, infrastructure, research and execution services and ability to accommodate special transaction needs. Although we generally seek competitive prices or, where applicable, commission rates, we will not necessarily pay the lowest price or the lowest commission.

We consider the following specific factors when determining whether a broker or counterparty will deliver best execution:

- Costs (commission, exchange levy, stamp duty, miscellaneous fees, etc.);
- Size and nature of the order;
- Speed and reliability of execution; and
- Any other consideration relevant to the efficient execution of the order.

We routinely monitor our trading for best execution.

## **ITEM 13 – REVIEW OF ACCOUNTS**

#### **A. Frequency of Reviews**

Our Portfolio Managers review each client account on a regular basis to determine, among other things, whether each account is appropriately positioned and whether investment objectives and policies are being followed.

#### **B. Written Reports**

Clients typically receive a performance statistics report and a performance attribution report. Clients typically also receive an investment management summary including portfolio review and market outlook based on an agreed upon set of procedures.

## **ITEM 14 – CLIENT REFERRALS AND OTHER COMPENSATION**

We have entered into contractual arrangements with firms that may solicit clients for us. The arrangements are made in writing pursuant to Rule 206(4)-3 of the Advisers Act. This requires, among other things, that such solicitors comply with requirements of the Rule and other applicable law, as well

as fulfill their contractual obligations with us. The solicitor must, at the time of his solicitation, provide the client with a copy of Part 2 of our Form ADV. The solicitor must also provide the client with a separate document describing the solicitation arrangement, disclosing any affiliation between us and the solicitor, the compensation for solicitation, and whether advisory fees for solicited clients are higher than those for other clients due to compensation paid to the solicitor.

## ITEM 15 – CUSTODY

We do not maintain physical possession of the funds or securities of any client. Each of our clients has entered into an agreement with a brokerage firm or commercial bank that serves as custodian of the funds and/or securities held by each such fund.

All US clients will receive statements of account holdings from their custodian not less than quarterly. Additionally, we will provide US clients with account balance and activity details upon request.

We urge all US clients to review carefully statements from the custodian and compare the custodial records to the reports that we provide them.

## ITEM 16 – INVESTMENT DISCRETION

We may be retained to manage client accounts on a discretionary or non-discretionary basis. In cases where we have investment discretion, we determine, within a client's specified investment objectives and guidelines, which securities are bought or sold, the total amount of securities to be bought or sold, and in most cases, the broker or dealer through which the securities are to be bought or sold and the commission rates to be paid, all without further consultation with the client. In exercising our investment discretion, we are guided by the investment management agreement that is established at the inception of the adviser-client relationship (along with any amendments to the agreement).

## ITEM 17 – VOTING CLIENT SECURITIES

Pursuant to our proxy voting policies and procedures, we take steps to see that proxies are voted on securities held in client accounts where authority to vote proxies has not been expressly reserved to the client in the investment management agreement or other documentation. If we vote proxies, it is our aim to see that proxies are voted in the best interest of our clients.

As an alternative to giving us discretion to vote proxies, clients may provide us with their own written proxy voting guidelines or their own policies, procedures or directions regarding the voting of a proxy or proxies. Such guidelines or directions must be in writing and delivered to us sufficiently in advance to vote the proxies as directed.

Clients may obtain information about how their securities were voted upon request by contacting us at our main office at the address given above. Upon request, clients may also obtain from us a copy of our proxy voting policies and procedures.

## ITEM 18 – FINANCIAL INFORMATION

We do not have any adverse financial information to disclose. The management of HGI believes that we are financially sound.