

## Fund Manager Commentary

### William Blair Macro Allocation Fund

#### Performance Summary

The Macro Allocation Fund (Class N) completed the quarter with negative performance, with aggregate market exposure ending flat and currency exposures detracting. Within markets, the Fund benefitted from exposures in emerging equities, such as long Brazil equity and short South Africa equity. Negative contributors to performance in the market strategy were long exposures to Europe equity and sector positioning within U.S. equities. Within currencies, long exposure to the Mexican peso and short exposure to the New Zealand dollar added value, while long exposures in the Turkish lira and Indian rupee and short exposure in the Thai baht detracted.

#### Fund Positioning

Market strategy remains long of equities, with an effective exposure of +17%, with net exposure being reduced slightly during the quarter. The Fund's largest risk exposures remain in developed Europe, U.K., and emerging equities. Market strategy is short of fixed income with a net exposure of -7%, with short exposure primarily in European government bonds.

Within currencies, the Fund remains long of currencies such as the Turkish lira, Philippine peso, and Indian rupee with the largest short positions in the Thai baht, Swiss franc, and New Zealand dollar.

#### Review & Outlook

Global equity prices finished the quarter higher than where they began. Across the world, however, returns varied quite markedly. The U.S. and Japanese (hedged) markets were strong—the S&P 500 index reached a new all-time high in September. Eurozone equities (hedged) were up, but less so. Emerging equities (hedged) were little changed. Bond yields in the United States and Europe rose a fraction of a percent.

<sup>1</sup> Information about the Fund's holdings should not be considered investment advice. There is no guarantee that the Fund will continue to hold any one particular security or stay invested in any one particular sector. Holdings are subject to change at any time.

<sup>2</sup> Reflected as 10-year exposures.

<sup>3</sup> Unencumbered cash is residual cash and equivalents.

<sup>4</sup> Additional currency exposures by largest expected contribution to portfolio risk.

#### Fund Exposures (%) as of 9/30/18<sup>1</sup>

<b>Equity</b>	<b>16.6</b>
U.S.	-0.3
Canada	-3.6
Europe (ex-U.K.)	8.4
United Kingdom	4.5
Asia Developed	1.3
Emerging	6.3
<b>Fixed Income</b>	<b>-6.8</b>
U.S. <sup>2</sup>	-3.0
Developed (ex-U.S. <sup>2</sup> )	-4.6
Emerging	0.8
<b>Unencumbered Cash<sup>3</sup></b>	<b>28.8</b>
<b>Credit Detail</b>	
U.S. Investment Grade Spread	6.0
U.S. High Yield Spread	-0.3
U.S. MBS Spread	-0.2
European Investment Grade Spread	2.2
<b>Active Currency</b>	
U.S. Dollar (USD)	-8.8
Canada Dollar (CAD)	0.0
Other Americas	10.5
Euro (EUR)	-6.0
Switzerland Franc (CHF)	-9.0
Great Britain Pound (GBP)	5.0
Other Europe	-0.5
Australia Dollar (AUD) and New Zealand Dollar (NZD)	-11.0
Japan Yen (JPY)	6.0
China Yuan (CNY)	-3.1
Asia (Excluding JPY and CNY)	0.9
Other	16.0

#### FOOTNOTE TO FUND EXPOSURE TABLE

Select Exposures <sup>4</sup>	
Turkish Lira (TRY)	14.0
Mexican Peso (MXN)	6.5
Polish Zloty (PLN)	3.0

Japanese government yields remained very close to zero, under the influence of central bank buying, though the Bank of Japan slightly loosened the range in which it seeks to contain ultra-low yields. The dollar and most developed world currencies were strong relative to

developing country currencies. Particularly dramatic currency weakness unfolded in Turkey and Argentina, both for domestic reasons, and there was some “spillover” to other emerging currencies that were viewed in the market as sharing similar vulnerabilities.

The quarter was challenging for our portfolio strategies—this originated from developments in Turkey affecting the Turkish lira to which we had long exposure going into the period. The largest detractor to performance was the lira, which is responsible for the entirety of negative contribution from currency exposures year-to-date. Performance also suffered from some other emerging market currency and equity positions, which weakened in correlated fashion, though less dramatically. However, we do not believe that the conditions are conducive to contagion in this space, since we view the lira situation as largely idiosyncratic. As a result, we further increased our lira exposure in August. Within developed equities, relative sector moves also challenged performance, as those more sensitive to growth (which we find mostly unattractive) outperformed those sensitive to value (more attractive sectors, in our view). The long-running outperformance of growth over value is a phenomenon that we believe has been heavily influenced by developed central banks’ very easy monetary policies, and has created sector opportunities that are likely to be rewarded as this accommodation continues to recede. We slightly reduced our overall equity exposure through the quarter.

In our second-quarter commentary, we outlined Turkey’s issues and the rationale for our long exposure to the deeply undervalued lira. Turkey has high inflation—significantly above its central bank’s target—and heretofore inadequate increases in official interest rates have been the dominant influence behind the lira’s weakening. At that time (June), we had concluded that political interference in monetary policy coming from President Recep Tayyip Erdogan (who has a long-standing, highly unorthodox opposition to high rates to combat inflation) had waned—Mr. Erdogan had backed down in the face of market pressure and allowed the Turkish central bank to respond appropriately when a 5% interest rate rise was implemented in May. This conclusion was premature: a failure to act further on interest rates in July contributed to a renewed and sharp fall in the lira in August. A diplomatic row between Mr. Erdogan and U.S. President Donald Trump exacerbated the move. But, mostly, repeated days of sharp lira weakness met with no central bank response transformed the situation into a self-feeding rout in the

lira, which touched an all-time low on 13 August at less than half of our estimate of fundamental value. Such dramatic deviations have been seen before, such as the Russian ruble in 2014 under the combined influence of a steeply falling oil price and Russia’s geopolitical actions in Ukraine that alienated it from western nations. We largely stood aside as the ruble fell in 2014, introducing long exposure thereafter. With the Turkish lira, we established exposure early (for the reasons given above), which had a significantly larger negative performance impact.

Exchange rate extensions away from value of this magnitude are highly compelling investment opportunities and the foundation of our investment process is to capture returns from the correction of large deviations from fundamental value. Not many of them become as extreme as in the case of the lira (or the ruble), but we calibrate risk budgets so that we can appropriately respond to these, even if short-term performance effects are lumpy. Despite the dramatic fall in the lira, we had the capacity to either increase or reduce our exposure subsequent to its drop; and our response in mid-August was to increase the position, making it the largest currency exposure in the Fund at quarter-end. In September, the central bank raised its policy rate by another 6.25%, probably scarred by the market reaction of the prior month. This hike came despite Mr. Erdogan’s continued rhetoric of opposition, and thus (again) it demonstrates some return to orthodox policy-making even if the president seeks to maintain distance from it. Given Mr. Erdogan’s sphere of influence in Turkey, which includes the finance ministry and the central bank, we would again conclude that the large tightening was essentially sanctioned by the president behind the scenes. The lira strengthened in September, though considerable headwinds remain.

Several other emerging currencies moved in correlated (though less dramatic) fashion to the lira, including some we find attractive like the Mexican peso, Indian rupee, South African rand, and Russian ruble. The conventional wisdom behind this “spillover” effect was that any signs of slowing growth, problematic inflation, and/or current account deficits (which require external financing) highlighted these currencies as vulnerable to a fate similar to that of the lira’s. We have this incidental higher correlation factored into our short-term “Outlook” risk model as a macro theme, but we do not believe that causation is robust here. As outlined, the Turkish lira’s (dominant) problem has arisen from domestic policy interference and (in)action in Turkey, and not from the influence of a common factor to which

Turkey and other markets are exposed. In addition, other countries had not been mismanaging central bank policy in ways that copied the situation in Turkey. India and Russia raised interest rates in the quarter (and inflation in both countries is much lower than in Turkey). Mexico's real interest rate has risen this year as its inflation rate has fallen. Our exposures to these currencies also detracted in August, but recovered in September.

Elsewhere, geopolitical uncertainty in the form of trade disputes remained an influence. The U.S. administration's stance against the European Union and Mexico moved towards agreement (reducing risk), but not with China, where the threat of increased protectionism remains. Our exposure in China consists of a modest (hedged) long equity position, which is more than offset by short exposure to the yuan, which China's central bank has allowed to weaken quite significantly in the last few months, possibly as a retaliation to tariff threats from the United States.

We reduced our (long) exposure to British pound in July. Negotiations between the United Kingdom and the EU about "Brexit" are now approaching the deadline (though this could get delayed). Political incentives, as outlined in our previous letter, mostly point towards a soft Brexit—the preservation of much of the barrier-free trade that has been the situation under EU membership. But we have long believed that uncertainty and heightened risk would be "back-loaded" towards the end of the negotiation timetable—as difficult agreements often are—and in fact have been postponed to the last hour.

As central banks, led by the Federal Reserve with the European Central Bank some way behind (and the Bank of Japan a long way behind), continue to edge conditions of extreme monetary accommodation back towards normalization, we believe that vulnerabilities in capital markets may become apparent. This is a significant reason we have maintained our total equity exposure at a relatively low level (and we slightly reduced "beta" in the quarter), and why we also maintain protection in the form of optionality, which is across equity, currency, and fixed income, to protect against general market downside. However, it is not the case that global equities or developed equities are overvalued in aggregate at this time, which is why we remain on the correct (long) side of price versus fundamental value overall. Where we see more of a dislocation as a result of years of easy central bank policy is in sovereign fixed income (bond buying

programs have heavily distorted bond yields away from fundamental values in recent years, and continue to do so) and between certain equity sectors where—as mentioned previously—sectors sensitive to growth (such as IT) have gained sustained support from ultra-easy policy at the expense of those sensitive to value (such as financials). These large and sustained dislocations are more vulnerable to reversal, and our Fund is well positioned for this.

In the larger picture, our longer-term investment objective is to deliver positive investment returns above inflation through a market cycle. We remain grounded in fundamental valuation as our first step—we strive to only take compensated risks and are unwilling to extend exposures unduly in a reach-for-yield that would be dictated not by opportunities and risks but by very low real interest rates. There will be environments in which we conclude that macro markets do not provide returns and risks compatible with portfolio objectives alongside other periods where compensation is abnormally high. During the last decade, the challenge of navigating these evolving environments has remained a significant component in the investment landscape, but we find our investment process, dialogue, and decision-making well-equipped to meet this challenge in an appropriate way. We remain vigilant as we assess new and relevant information to capture future investment opportunities in a timely manner and will continue balancing the relationship between risk taken and compensation expected.

### INVESTMENT PERFORMANCE % (as of 09/30/18)

	QTR	YTD	1Y	3Y	5Y	Since Incep.
Class I (SI: 11/29/11)	-2.39	-3.87	-3.26	0.60	1.22	4.32
Class N (SI: 11/29/11)	-2.49	-4.05	-3.54	0.30	0.94	4.04
BofA Merrill Lynch 3-Month U.S. Treasury Bill Index	0.48	1.30	1.59	0.84	0.52	0.40

### EXPENSE RATIOS (%)\*\*

	Gross Expense	Net Expense
Class I	1.18	1.18
Class N	1.53	1.47

\*\*Expenses shown are as of the most recent prospectus and include acquired fund fees and expenses. The net expense ratio reflects that the Fund's Adviser has contractually agreed to waive fees and/or reimburse expenses to limit fund expenses until 4/30/2019. The investor will pay the net expense ratio. The Adviser has contractually agreed to limit the Fund's operating expenses (excluding acquired fund fees and expenses, borrowing costs, brokerage commissions, taxes, other investment-related costs and extraordinary expenses) to 1.00% and 1.25% of average daily net assets for Class I and Class N shares, respectively, until 4/30/2019. Please refer to the Fund's Prospectus for more information on the Fund's expenses.

Performance cited represents past performance. Past performance does not guarantee future results and current performance may be lower or higher than the data quoted. Returns shown assume reinvestment of dividends and capital gains. Investment returns and principal will fluctuate with market and economic conditions and you may have a gain or loss when you sell shares. For the most current month-end performance information, please call +1 800 742 7272, or visit our Web site at [www.williamblairfunds.com](http://www.williamblairfunds.com). Class N shares are available to the general public without a sales load. Class I shares are available only to investors who meet certain eligibility requirements.

### DISCLOSURES

The Fund involves a high level of risk and may not be appropriate for everyone. You could lose money by investing in the Fund. There can be no assurance that the Fund's investment objective will be achieved. The Fund holds equity exposures, which may decline in value due to both real and perceived general market, economic, and industry conditions. Investing in bond markets is subject to certain risks including market, interest-rate, issuer, credit, and inflation risk; investments may be worth more or less than the original cost when redeemed. Derivatives may involve certain costs and risks such as liquidity, interest rate, market, credit, management and the risk that a position could not be closed when most advantageous. Investing in derivatives could lose more than the amount invested. Investment return, principal value, and yields of an investment will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. Investments are subject to a number of types of risk, including counterparty and contractual default risk. For a more detailed explanation and discussion of these and other risks, please read the Fund's Prospectus. The Fund is designed for long-term investors.

The Bank of America Merrill Lynch 3-Month U.S. Treasury Bill Index measures total return on cash, including price and interest income, based on short-term government Treasury Bills of about 90-day maturity. The Index is unmanaged, does not incur fees or expenses, and cannot be invested in directly.

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***Please carefully consider the Fund's investment objectives, risks, charges, and expenses before investing. This and other information is contained in the Fund's prospectus, which you may obtain by calling 1-800-742-7272. Read it carefully before you invest or send money. Investing involves the risk of loss.***

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