Macro Allocation Fund

William Blair

Investment Review

September 2018

Brian D. Singer, CFA, Partner
Thomas Clarke, Partner
Portfolio Managers

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 is not a complete investment program and you should only consider the Fund for the alternative portion of your portfolio. Separate accounts managed by the Advisor may invest in the Fund and, therefore, the Advisor at times may have discretionary authority over a significant portion of the assets invested in the Fund. In such instances, the Advisor's decision to make changes to or rebalance its clients' allocations in the separate accounts may substantially impact the Fund's performance. The Fund is designed for long-term investors.

The Fund may use investment techniques and financial instruments that may be considered aggressive—including but not limited to the use of futures contracts, options on futures contracts, securities and indices, forward contracts, swap agreements and similar instruments. Such techniques may also include short sales or other techniques that are intended to provide inverse exposure to a particular market or other asset class, as well as leverage. These techniques may expose the Fund to potentially dramatic changes (losses) in the value of certain of its portfolio holdings. Investments are subject to a number of other different types of risk, including market risk, asset allocation risk, credit risk, commodity risk, counterparty and contractual default risk, currency risk, and derivatives risk. For a more detailed explanation and discussion of these risks, please read the Fund's Prospectus.

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 are average annual total returns, which assume reinvestment of dividends and capital gains. Investment returns and principal will fluctuate and you may have a gain or loss when you sell shares. Most recent month-end performance information for William Blair Funds is available by visiting the William Blair Funds Web site at www.williamblairfunds.com, or by calling the William Blair Funds at 1-800-742-7272.

Please carefully consider the Fund's investment objective, 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.

- **Macro Allocation is positioned cautiously in respect of systematic market risk (beta) and overall strategy risk as compared to the long-term expected averages.**
- **The near-term macro environment still presents risks that mitigate the attractiveness of fundamental opportunities across the opportunity set.**
- **Unsystematic market and currency exposures have been the dominant drivers of recent performance.**

Performance Summary

The Macro Allocation Fund completed the quarter with negative performance, with aggregate market exposure ending flat and currency exposures detracting. Within markets, the portfolio 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.

Strategy Positioning

Market strategy remains long of equities, with an effective exposure of +17%, with net exposure being reduced slightly during the quarter. The strategy'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, strategy 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.

Strategy Review and 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. 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 letter, 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 strategy exposure subsequent to its drop; and our response in mid-August was to increase the position, making it the largest currency exposure in the portfolio 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 strategy 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 for Periods ended 9/30/2018	3 Months	YTD	1 Year	3 Year	5 Year	Since Incept.*	Since Incept.**
Macro Allocation Fund (WMCJX) Institutional Class	-2.39%	-3.78%	-3.16%	0.69%	--	0.53%	--
Macro Allocation Fund (WMCIX) Class I	-2.39%	-3.87%	-3.26%	0.60%	1.22%	--	4.32%
Macro Allocation Fund (WMCNX) Class N	-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%	0.52%	0.40%
HFRI Macro Discretionary Thematic Index	0.33%	1.26%	0.22%	0.59%	0.36%	0.23%	0.62%
U.S. CPI + 5%						6.54%	6.53%

* Inception: 10/21/2013
**Inception: 11/29/2011

Expense Ratios:

	Gross	**Net**
Institutional	**1.08%**	**1.08%**
Class I Shares	**1.18%**	**1.18%**
Class N Shares	**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 1.25% of average daily net assets for Class N shares 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 are since inception total returns, which 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. Class N shares are available to the general public without a sales load. Institutional Class and Class I shares are available to certain institutional investors.

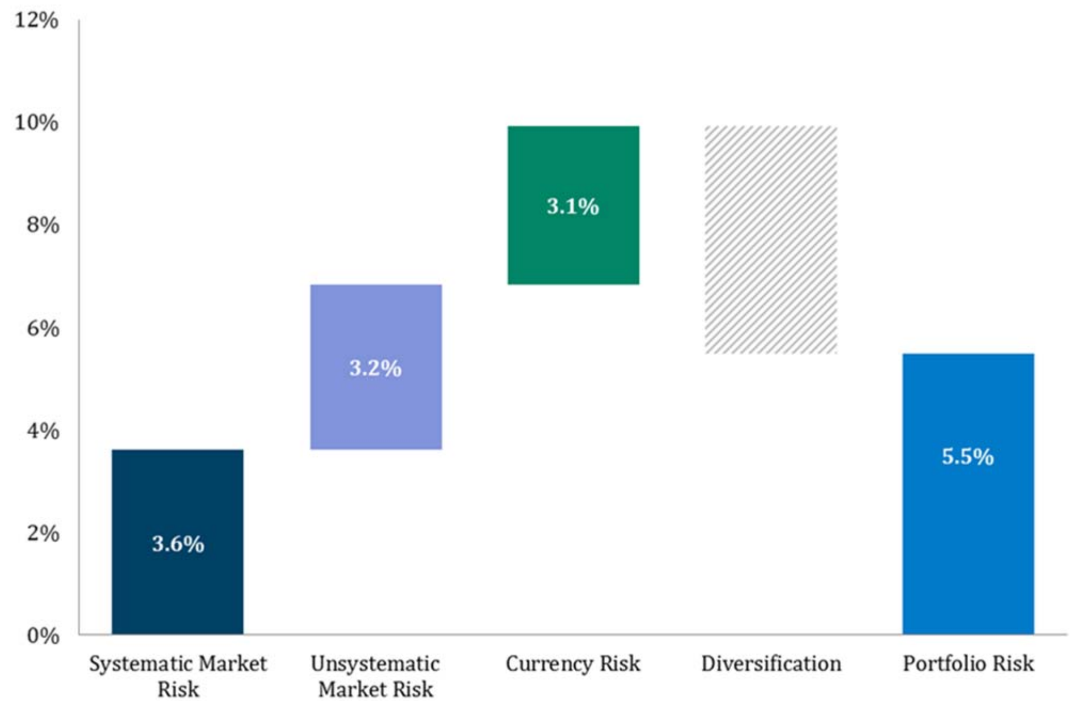
The BofA Merrill Lynch 3-Month U.S. Treasury Bill Index measures total return on cash, including price and interest income, based on short-term government Treasury Bills of about 90-day maturity. The index is unmanaged, does not incur fees or expenses, and cannot be invested in directly. The U.S. CPI + 5% is not a benchmark but is included as supplemental reference as the long-term return objective. The HFRI Macro Discretionary Thematic Index includes hedge fund strategies primarily reliant on the evaluation of market data, relationships and influences, as interpreted by an individual or group of individuals who make decisions on portfolio positions; strategies employ an investment process most heavily influenced by top down analysis of macroeconomic variables. Constituents are equally weighted and returns are reported net of underlying manager fees. The index is unmanaged and cannot be invested in directly.

The below table shows the calculated regional performance attribution of the Macro Allocation Fund by asset segment for the quarter.

Macro Allocation Q3 2018	Equity	Rates	Credit	Currency	Residual / Other	Total
North America	-0.62%	0.63%	-0.01%	0.00%		**0.00%**
Developed Europe	-0.64%	0.05%	0.02%	-0.03%		**-0.60%**
Developed Asia (ex Japan)	0.10%	0.00%	0.00%	0.26%		**0.37%**
Japan	-0.19%	0.00%	0.00%	-0.19%		**-0.38%**
Emerging Markets	0.70%	0.00%	-0.05%	-2.25%		**-1.59%**
Multi-Region	-0.01%	0.00%	0.00%	0.00%		**-0.01%**
Residual/Other						**-0.28%**
Total	**-0.66%**	**0.69%**	**-0.04%**	**-2.20%**	**-0.28%**	**-2.49%**

Past performance does not guarantee future results. Portfolio exposures and attribution are based on the Macro Allocation Fund (Class N). Performance attribution is sourced from Cloud Attribution Ltd. Using the Karnosky-Singer performance attribution methodology.

The below chart shows the expected sources of investment risk for the Macro Allocation Fund.



Source: William Blair

*The DAS team's expectation of the portfolio's volatility as viewed through the team's proprietary Outlook risk model, in which the team's near-term risk assumptions are quantified.

The detail below shows selected market and currency strategy exposures of the Macro Allocation Fund as of quarter-end.

Equity	16.5%
U.S.	-0.3%
Canada	-3.6%
Europe (ex-U.K.)	8.3%
UK	4.5%
Asia Developed	1.3%
Emerging	6.3%

Fixed Income	-6.7%
U.S. Treasury & Credit[1,*]	1.1%
Non-U.S. Treasury & Credit[1,*]	-8.6%
Emerging	0.8%

Unencumbered Cash	28.8%

Active Currency	
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%

[1]Reflected as 10-year exposures

[2]Additional currency exposures by largest expected contribution to portfolio risk

**Credit Detail*	
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%*
European High Yield Spread	*0.0%*

Select Exposures Detail[2]	
Turkish Lira (TRY)	*14.0%*
Mexican Peso (MXN)	*6.5%*
Polish Zloty (PLN)	*3.0%*

Not intended as investment advice. Allocations are subject to change without notice.

This section provides additional commentary relating to the strategy changes within the Macro Allocation Fund during the quarter.

2 July 2018: Decreasing Mexican equity

From a fundamental valuation perspective, Mexican equity is one of the more unattractive equity markets in our universe. Conventional Wisdom (CW) is that Mexico's equity market is a relatively low-risk emerging market because of its high weight in consumer-oriented stocks, which typically have less volatility than most emerging markets. This has caused the market to become overvalued in our view. However, CW has shifted more recently. The NAFTA negotiations have not yielded much progress and left-wing populist Andres Manuel Lopez Obrador (AMLO) won the presidency by a wide margin. Due to his indications of wanting to stem or even reverse privatization of the oil industry and his inclination on being tough on the U.S., investors seem correct to worry about the risks to Mexico's equity market. This strategy change decreases systematic risk.

10 July 2018: Increasing euro (EUR) and decreasing Great Britain pound (GBP)

From a fundamental valuation perspective, the euro (EUR) has become less unattractive while the Great Britain pound (GBP) has become less attractive. Weakening GBP and strengthening EUR has in large part come from Brexit negotiations. Recently, the market has been factoring in a negative geopolitical (and potentially economic) shock arising from the likelihood that the UK would experience lower growth from less free trade and movement of labor with the EU. Although we are reducing GBP, we remain long, in line with valuation, and are still mindful that further negotiations may provide some strength to a softer Brexit solution, which is favorable to the GBP. This strategy change slightly decreases currency risk.

11 July 2018: Increasing German equity and decreasing UK equity

From a fundamental valuation perspective, UK equity remains one of the more attractive equity markets within our universe, while Germany remains somewhat less attractive. However, during the last year, UK equity has outperformed Germany, leading to a narrowing of the valuation opportunity. A recent summit of the British cabinet corroborated our view that the UK government was indeed positioning itself for a soft Brexit solution. However, in affirming her desire to negotiate a softer Brexit solution, Prime Minister Theresa May lost the support of senior cabinet members, which now ushers in a period of political instability. With respect to Germany, we have also seen a weakened leadership since the elections last year. Additionally, Germany also has found itself as one of the primary European countries exposed to trade tensions with the U.S. This strategy change is neutral to portfolio risk.

17 July 2018: Decreasing global energy sector equity

From a long-term fundamental valuation perspective, the global energy sector equity remains somewhat attractive; however, it has recently outperformed the broader global equity markets, making it less attractive on a relative basis. It is our expectation that further upside to medium-term oil prices appears limited as the 36-month contract price for oil has moved above our longer-term estimates. The confluence of our assessment of the Middle East game theater and the Energy macro theme also suggest little further upside to near-term oil prices. While the U.S. will use sanctions to squeeze Iran's oil exports, the aggregate supply/demand balance is still likely to remain fairly stable. The strategy change slightly reduces portfolio risk.

24 July 2018: Decreasing EMU and emerging market equities

From a fundamental valuation perspective, both aggregate EMU and emerging market equities remain absolutely and relatively attractive. The primary rationale for this change is our assessment that supportive Conventional Wisdom regarding the combination of economic activity and monetary accommodation has begun to wane on a global basis. After a very supportive 2017, fueled in part by forthcoming fiscal stimulus emanating from the U.S., the marginal investor (informed primarily by short-term data versus expectations) is now less sanguine. The major central banks are slowly, but steadily, removing accommodation as economic activity appears to come off of this near-term inflection point. This strategy change slightly decreases portfolio risk.

9 August 2018: Increasing New Zealand dollar (NZD) and decreasing Brazilian real (BRL) and Colombian peso (COP)

From a fundamental valuation perspective, the New Zealand dollar (NZD) remains one of the most unattractive currencies while the Brazilian real (BRL) and Colombian peso (COP) remain modestly attractive. However, the NZD has been an underperformer among developed market currencies as the market has priced in a more dovish central bank. We chose to reduce exposures to two emerging currencies as they also tend to trade with a positive beta when equities are weak. Due to Colombia's dependence on oil, the COP tends to correlate to a large extent with oil prices, which has moved above our longer-term estimates. The BRL is exposed to current election dynamics in Brazil. While we see the Brazilian election as leading to a positive development for the country in the long-run, we anticipate more volatility around the elections. This strategy change slightly decreases currency risk.

15 August 2018: Increasing Turkish lira (TRY) and decreasing Swiss franc (CHF) and Chinese yuan (CNY)

Value/price considerations justify a significantly larger long Turkish lira (TRY) exposure following a rapid weakening of the currency. The Swiss franc (CHF) remains significantly overvalued. We have increased long TRY exposure in delayed fashion relative to the valuation opportunity due to significant negative headwinds affecting the TRY from non-valuation considerations. The TRY has been deeply undermined by political interference in monetary policy by Turkey's President, Recep Tayyip Erdogan, who has been publicly opposed to tight monetary policy in order to curb Turkey's very high inflation rate. Although nominal interest rates set by Turkey's central bank have increased in line with inflation, the rate increases have been widely viewed as both insufficient and late, and the independence of the central bank is in doubt to some investors. While this "game of chicken" between President Erdogan and the market has proven to be sharply negative for the currency thus far, the TRY is now so undervalued that we believe its cheapness could present very high compensation in return for its material short-term risk. The CHF has been one of the strongest world currencies relative to the TRY and is consequently one of the most justified currencies to be sold as counterpart to buying TRY. We are also reducing exposure to the Chinese Yuan (CNY) due to headwinds in the Chinese Growth theme and increased intensity in global trade tensions with the U.S. This strategy change increases currency risk.

15 August 2018: Increasing Swedish equity and decreasing Mexican equity

From a long-term fundamental valuation perspective, Mexico is unattractive while Sweden is slightly attractive. Mexico's left-wing populist candidate, Andres Manuel Lopez Obredor's (AMLO) election victory came at margins that exceeded expectations. Our sense is that this initial honeymoon period will eventually give way to the reality of AMLO pursuing some of the policies that the markets initially feared in the lead up to the election. With respect to Sweden, economic growth has remained firm relative to the broader eurozone. This stems in part from Sweden's persistent monetary accommodation, with the lowest interest rates in the EMU area. This strategy change slightly reduces total portfolio risk.

15 August 2018: Shifting put options from European small cap equities to European large cap equities

Implied volatilities remain at or below Outlook risk levels in most areas and the EMU region is no exception. This strategy change has two impacts: first, it maintains or extends our medium convexity profile on the downside and secondly, the switch from European small cap to large cap makes our overall convexity (downside protection) strategy more systematic. Convexity measures our desire to pay risk premia in order to protect the portfolio against downside risk and/or benefit from upside only. This strategy change reduces total portfolio risk.

16 August 2018: Intra-Chinese equity change

From a long-term fundamental valuation perspective, Chinese equity remains attractive. At the same time, we've observed a relative underperformance of Chinese A-shares (shares denominated in Chinese yuan and traded on the Shanghai and Shenzhen exchanges) relative to Chinese H-shares (shares denominated in Hong Kong dollar and traded on the Hong Kong exchange). We continue to acknowledge the near- and medium-term influences on perceptions of economic activity that emanate from both the Chinese Growth and Globalism vs. Protectionism themes. These negative influences lead us to maintain an exposure level somewhat below signal overall in China and now introduce A-share exposure at the expense of H-share exposure. This strategy change slightly increases unsystematic risk.

17 August 2018: Decreasing Argentina equity

From a long-term fundamental valuation perspective, Argentina equity is moderately attractive. Conventional Wisdom on Argentina is increasingly negative as economic growth is falling at the same time that monetary policy has begun to tighten. We anticipate that economic deterioration will lead to a fall in support for President Macri. His approval ratings fell from 45% in June to 37% in July and are likely to continue to trend downwards. If these ratings do not stabilize before the 2019 presidential election, the probability of his re-election will fall, resulting in policy uncertainty in the future. This strategy change reduces total portfolio risk.

21 August 2018: Increasing broad U.S. equity and decreasing U.S. energy sector equity

From a long-term fundamental value perspective, U.S. energy sector equity remains attractive. The primary rationale for this change is our expectation that further upside to medium-term oil prices appears limited. The price of the 36-month contract price for oil remains above our longer-term equilibrium estimates. The confluence of our assessment of the Middle East game theater and the Energy theme also suggest little further upside to near-term oil prices. This strategy change is neutral to portfolio risk.

27 August 2018: Decreasing Brazilian equity

From a long-term fundamental valuation perspective, Brazil equities are attractive. Conventional Wisdom on Brazil remains cautious since economic growth has been disappointing as the country emerges from its recession at the same time that inflation is picking up. Worries continue to mount regarding the outcome of upcoming presidential elections. The front-runner for president remains former president Lula da Silva, who is unlikely to be allowed to run due to his ongoing prison sentence. Next in line, according to opinion polls, is Jair Bolsonaro, whose fierce rhetoric and nationalist tendencies are scaring the market. By contrast, we see a potential Bolsonaro victory as a positive as he is more likely than most to pursue market-friendly reforms and privatizations. We conclude that while the long-term prospects are positive, there will be worries in the short-term that warrant a smaller exposure, allowing us to step in should the market weaken. This strategy change slightly reduces total portfolio risk.

29 August 2018: Increasing Japanese equity

From a long-term fundamental valuation perspective, Japanese equities are fairly valued. From a macro-thematic standpoint, Japan equity remains exposed to both the Chinese Growth and Globalism vs. Protectionism themes. Finally, our game-theoretical analysis suggests that leadership stability will continue to prevail and Prime Minister Abe will be re-elected for a third consecutive term as leader of the LDP in late September. In addition, despite the short-term headwind of China Growth and U.S. – China trade negotiations, the game-theoretical analysis suggests incentives remain high to conclude major regional trade deals (TPP and/or RCEP). If concluded, these deals would bode well for Japan as it expands connectivity and reach. This strategy change slightly increases total portfolio risk.

30 August 2018: Increasing Japanese equity and decreasing Argentina equity

From a long-term fundamental valuation perspective, Argentina equity has become less attractive while Japanese equity has become more attractive on a relative basis. Conventional Wisdom in Argentina has become increasingly negative, as economic growth is falling and monetary policy has begun to tighten significantly. Further, the acceptance of an IMF program means the government will need to cut its deficit by delaying a planned reduction in income taxes and several capital expenditure adjustments. We also anticipate that the coming economic deterioration will lead to a fall in support for Preside Macri. For Japan, our game-theoretical analysis suggests that leadership stability will continue to prevail and Prime Minister Abe will be re-elected for a third consecutive term as leader of the LDP in late September. In addition, despite the short-term headwind of China Growth and U.S. – China trade negotiations, the game-theoretical analysis suggests incentives remain high to conclude major regional trade deals (TPP and/or RCEP). If concluded, these deals would bode well for Japan as it expands connectivity and reach. This strategy change is neutral portfolio risk.

17 September 2018: Increasing German, European Financials and Indonesian exposure and decreasing Spanish equity

From a long-term fundamental valuation perspective, both Spain and Indonesia equity remain attractive. The Spanish government continues to operate with no functioning majority and remains in gridlock after PSOE, Podemos, and small regional parties voted a motion of “no confidence” that toppled Prime Minister Rajoy in June. Looking forward, gridlock around budget negotiations are likely to continue. Indonesia remains stable with respect to economic activity. While there is concern with the level of external debt as institutional ownership of Indonesian debt has been increasing, the concern appears overdone to us as Indonesia ranks in the middle of the pack in terms of coverage ratios and maturity structures. This strategy change is neutral to portfolio risk.

21 September 2018: Intra-U.S. sector change

From a long-term fundamental valuation perspective, the U.S. equity market remains modestly unattractive; however, on a relative basis, we continue to see notable divergence within sectors. Both the IT and Communications Services sectors are among the relatively more unattractive sectors, while the Financials and Consumer Staples sectors are relatively attractive. This change sees us selling Financials and Communication Services while buying IT and Consumer Staples. We are seeing some marginal shifts in the “*Why*” influences as it pertains to these sectors with respect to oil prices and regulation. Oil prices are currently at the upper end of our expected range, and we believe that Consumer Staples are more likely to be beneficiaries from any future pullback in oil prices. With respect to regulation, Financials have been in a bit of a sweet spot after the 2016 election and the subsequent tax reforms but this momentum has recently begun to wane and may continue to do so in the lead up to the midterms. This strategy change is neutral to portfolio risk.

24 September 2018: Decreasing Brazilian equity

From a long-term fundamental valuation perspective, Brazil equity is attractive. Conventional Wisdom on Brazil remains cautious since economic growth has been disappointing as the country emerges from its recession at the same time that inflation is picking up. Now, worries are mounting ahead of the first round of the elections on October 7. According to the latest opinion polls, Fernando Haddad of the Worker's Party is trailing Jair Bolsonaro, whose fierce rhetoric and nationalist tendencies are moving Conventional Wisdom negative. We conclude from this that while the long-term prospects of a Bolsonaro victory are likely to be beneficial to the market, there will be worries in the short-term that warrant a smaller position, allowing us to step in should the market weaken. This strategy change slightly reduces total portfolio risk.

Glossary - Terms

Beta: A quantitative measure of the volatility of the portfolio relative to the overall market, represented by a comparable benchmark. A beta greater than 1 is more volatile than the overall market, while a beta less than 1 is less volatile, and could be expected to rise and fall more slowly than the market.

Risk (Standard Deviation): A measure of the portfolio's risk. A higher standard deviation represents a greater dispersion of returns, and thus a greater amount of risk. The annualized standard deviation is calculated using monthly returns.

Sharpe Ratio: A risk-adjusted measure calculated using standard deviation and excess return (Portfolio return – Risk Free Rate) to determine reward per unit of risk. The higher the Sharpe ratio, the better the portfolio's historic risk-adjusted performance.