

## Fund Manager Commentary

### William Blair SICAV Dynamic Diversified Allocation Fund

#### Performance Summary

The Dynamic Diversified Allocation strategy completed the quarter with positive performance. Market strategy, currency strategy and security selection were all positive during the quarter. Our market strategy was particularly bolstered by long exposure to emerging and U.S. equities. Fixed income positioning was slightly positive, with long exposure to credit adding value. Positive contribution from currency was largely driven by long exposures to emerging currencies such as the Colombian peso and Chinese yuan. Security Selection was positive during the quarter, with positive performance from International Leaders and U.S. Small Cap Value.

#### Fund Positioning

We now feel less compelled to maintain our strategies as de-risked as they previously were, in respect of opportunities that have been affected by shorter-term macro-thematic and geopolitical headwinds. Many recent moves in our strategy have been in response to relative price movements across our universe, rather than a change in the “Why” stage of our investment process.

Market strategy remains long of equities, with effective exposure of +31% unchanged during the quarter. The strategy remains long of Europe, UK, U.S. and emerging equities. Market strategy is modestly long of fixed income with a net exposure of +19%.

Within currencies, strategy remains long of emerging currencies and short of developed currencies, in line with fundamental valuation. Our largest long positions remain in emerging currencies such as the Chinese yuan, Philippine peso, and Indian rupee with our largest short positions in the U.S. dollar, Swiss franc, and New Zealand dollar.

#### Fund Exposures (%) as of 30.09.2017

|  |                  |
|--|------------------|
| <b>Equity</b>                              | <b>30.9</b>      |
| <b>Europe (ex-U.K.)</b>                    | 12.4             |
| <b>U.K.</b>                                | 5.9              |
| <b>Asia Developed</b>                      | 0.5              |
| <b>U.S.</b>                                | 5.0              |
| <b>Canada</b>                              | -2.2             |
| <b>Emerging</b>                            | 9.3              |
| <b>Fixed Income</b>                        | <b>19.2</b>      |
| <b>U.S. Treasury and Credit (10-Year)*</b> | 10.0             |
| <b>Non-U.S. Developed (10-Year)</b>        | 5.2              |
| <b>Emerging</b>                            | 4.0              |
| <b>Unencumbered<sup>1</sup></b>            | <b>30.1</b>      |
| <b>Active Currency</b>                     | <b>USD Based</b> |
| Euro (EUR)                                 | -4.4             |
| Switzerland Franc (CHF)                    | -5.8             |
| Great Britain Pound (GBP)                  | 3.8              |
| Other Europe                               | -1.1             |
| Australia Dollar (AUD)                     | -1.5             |
| New Zealand Dollar (NZD)                   | -6.2             |
| U.S. Dollar (USD)                          | -8.2             |
| Canada Dollar (CAD)                        | -2.2             |
| Other Americas                             | 9.8              |
| Japan Yen (JPY)                            | -1.1             |
| China Yuan (CNY)                           | 6.2              |
| Asia (ex-JPY and CNY)**                    | 4.9              |
| Other                                      | 5.8              |
| <b>Net Currency</b>                        | <b>0.0</b>       |

#### Fund Review and Outlook

Equities around the world generally rallied in the third quarter, with riskier emerging markets beating developed markets, as has been mostly the case through 2017. Within developed equity markets, the United States, Japan, and Europe rose a modest amount, with the majority of the rise occurring in September. Ten-year government bond yields fell in the G3 markets, though they retraced the drop during September. The U.S. dollar continued its fall against most developed and emerging currencies. Market volatility was generally

low, experiencing only a few short-lived upward spikes caused by hostile nuclear demonstrations by North Korea and associated geopolitical rhetoric from the United States.

Led by manufacturing and consumer spending, global growth data continued to show a modestly rising trend from its low point at the beginning of 2016. This data both lifted expectations and led to less accommodative monetary signals from most central banks (apart from the Bank of Japan). The OECD stopped short of referring to the situation as a self-sustaining growth upswing. Global trade values have increased impressively over the last year, but much of this reflects higher prices of traded goods (particularly commodities), rather than any surge in volume. The most striking upward revisions to growth forecasts occurred in the eurozone and China. In both cases, these developments reflect fading macro-thematic headwinds that had significantly impaired attractive equity market opportunities in prior years. As India's 2016 "demonetization" exercise has proved to have little adverse effect, Indian economic growth expectations now reflect widespread optimism. Contrastingly, growth forecasts in Latin America have weakened, much of that influenced by its largest economic region, Brazil.

Of the G7 central banks, only the U.S. Federal Reserve and the Bank of Canada have raised short-term interest rates, whereas the eurozone, Japan, and the United Kingdom have kept rates at historic (near zero) lows. The European Central Bank (ECB) has hinted at a further wind-down of its monthly asset purchases, but there has been no announced schedule for this following its initial "taper" in late 2016. The ECB's hints were sufficient to rally the euro in the quarter. The Bank of England's interest rate setting committee boosted expectations of an interest rate rise at its meeting in August. Although the decision was not taken in the quarter, the pound rose to its highest level (against the U.S. dollar) since the eve of 2016's Brexit referendum. Japan, where inflation expectations remain very low, had no apparent change in guidance about monetary policy. All the foregoing changes in policy and communication could be regarded as relatively minor,

though they command high attention among investors and are among the largest movers of market prices.

There are two dominant reasons why market participants give intense scrutiny to central bank communication in the present environment. One is the extreme levels to which monetary conditions have been loosened—particularly in the developed world—in recent years. Investors are dealing with highly unconventional policies (zero or negative interest rates in some cases, asset purchases, etc.) compared with policies in prior decades. The other is the more forward-looking communication of central banks, whereas in the past communication was confined largely to announcing that interest rates were either up or down. In respect of the first reason—unconventional policy tools—the short-term investment dynamics following such policies are largely the same as they have always been (and relative policies continue to have a similar effect on exchange rates). Importantly, we continue to work under the assumption that asset prices—bonds and equities—would probably not be as high as they are in the absence of these policies. But, because of the second aspect of policy communication, we doubt the likelihood of substantial and sustained downside market shocks wrought by an *unanticipated* withdrawal of monetary looseness. Our rationale is that central banks have progressively moved toward long-range, forward-looking communication out of a desire to reduce market uncertainty—or to increase certainty—about future policy. For the most part, this has probably done little more than bring forward (in time) the market reaction-function (witness the sizable exchange rate moves that have unfolded in the last two years on statements based more about future policy settings than present ones). But it has created a situation where central banks now must strive to deliver what they have told markets to expect. This is not always appropriate if circumstances (economic and inflation data) change from what was expected, but it counsels strongly against central banks making capricious moves regarding monetary conditions that are contrary to those that they have previously telegraphed.

Therefore, central bank support of market prices does not appear to be under much threat of a significant and near-term reduction. However, as a macro theme that pervades much of our investment universe, developed central bank policy has introduced narrowness to the range of valuation opportunities currently available. This is most evident in currencies where the valuation opportunity is dominated by a “positive carry” trade, characterized by attractive “high carry” emerging market currencies and unattractive (low carry) developed currencies. This reduced breadth has kept us relatively cautious in respect of active currency risk, although we are responding to the large opportunity by steadily increasing exposures throughout 2017. With respect to equities, we remain long of attractive eurozone and U.K. equities, but we have sought protection from large unanticipated adverse moves with nonlinear positions where the cost of such protection is not high.

Populism remains an influential macro theme affecting market and currency prices, but its intensity has dropped significantly since 2016. Its influence was nonetheless evident in Germany’s federal election in which the country’s staunchly anti-immigration party AfD experienced a surge in support, which allowed it into parliament for the first time. Support was significantly eroded from traditional parties, including Chancellor Angela Merkel’s Christian Union. However, Ms. Merkel will undoubtedly serve a fourth term as chancellor in a coalition that is yet to be decided (but almost definitely excluding AfD), meaning that investment implications do not appear significant for this event. Elsewhere in Europe, the U.K.’s negotiations with the European Union (EU) over Brexit now point toward the process taking an extended period of time, likely involving a transition period after the deadline of March 2019. This reflects U.K. Prime Minister Theresa May’s weak bargaining position compared with that of the EU, the weak position itself a result of the fragility of her government after the recent snap election.

Although this prolongs uncertainty to some extent, our investment conclusion is, as it has been previously, that the adverse geopolitical risks to U.K. markets and the pound are relatively small today. Consequently, we are

not cautious in our strategy response to the attractive valuation of both U.K. equities and the pound.

With respect to the North Korean threat, our response has been to dampen exposure to the South Korean won (no longer a fundamentally attractive currency anyway) and its equity market. We view the North’s primary geopolitical objective as being survival, which motivates its desire to demonstrate nuclear capability, but to likely stop short of provoking aggressive responses from the United States or China (North Korea is likely more interested in maintaining disunity between these powers in respect of reaction).

Our analysis and its conclusions—that several of the headwinds that weighed against attractive investment opportunities (by increasing risk and adversely affecting expected compensation) have recently faded—are consistent with more subdued volatility in markets and currencies across our investment universe. Notwithstanding this, our forward-looking risk models do not assume that the very low levels of volatility that have been observed in market and currency prices during current and recent quarters are sustainable in the longer term. Consequently, and as mentioned above, we have taken advantage of the low price of some options to re-engage some downside protection within our market exposures.

It is our view that the challenge of navigating these risks continues to be a significant shift in the investment landscape that has occurred in the last decade and our investment process, dialogue, and decision making is well equipped to meet the challenges we now face. 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.

**FOOTNOTES TO FUND EXPOSURE TABLE**

| <b>*Credit Detail</b>            |     |
|----------------------------------|-----|
| European Investment Grade Spread | 3.3 |
| U.S. Investment Grade Spread     | 5.5 |
| U.S. High Yield Spread           | 0.7 |
| <b>**Select Exposures</b>        |     |
| India Rupee (INR)                | 5.1 |
| Philippine Peso (PHP)            | 5.4 |
| Singapore Dollar (SGD)           | 4.7 |

<sup>1</sup>Unencumbered cash is residual cash and equivalents.

Fund exposures are as of 30 September 2017.

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