William Blair

4Q 2017

Fund Manager Commentary
William Blair SICAV Dynamic Diversified Allocation Fund

Performance Summary

The Dynamic Diversified Allocation Fund 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 international equities, developed and developing. Short exposure to Japanese equities detracted. Positive contribution from currency was largely driven by long exposures to emerging currencies such as the South African rand, Chinese yuan, and Philippine peso. Security Selection was slightly positive during the quarter, with positive performance from International Leaders.

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 +13%.

Within currencies, strategy remains mostly 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 31.12.2017

Equity	**31.5**
Europe (ex-U.K.)	13.6%
U.K.	5.9%
Asia Developed	0.9%
U.S.	4.2%
Canada	-2.8%
Emerging	9.7%
Fixed Income	**13.3**
U.S. Treasury and Credit (10-Year)*	2.6
Non-U.S. Developed (10-Year)	8.9
Emerging	1.8
Unencumbered[1]	**30.8**
Active Currency	**USD Based**
Euro (EUR)	-5.2%
Switzerland Franc (CHF)	-6.9%
Great Britain Pound (GBP)	4.3%
Other Europe	-3.0%
Australia Dollar (AUD)	-1.7%
New Zealand Dollar (NZD)	-8.6%
U.S. Dollar (USD)	-8.8%
Canada Dollar (CAD)	-2.6%
Other Americas	11.6%
Japan Yen (JPY)	5.2%
China Yuan (CNY)	7.3%
Asia (Ex - JPY and CNY)	1.5%
Other	6.9%
Net Currency	**0.0**

Fund Review and Outlook

Global equities rose again in the fourth quarter, completing a generally uninterrupted year of price appreciation and positive return for developed and emerging markets alike. Within developed equities, Japan and the United States performed better than Europe for the quarter and year; within Europe, Italy, Germany, and France had stronger performance than Spain and the United Kingdom. Nevertheless, all markets provided returns that compensated for historically low levels of volatility. Government bond yields remained low almost everywhere. Most developed and emerging currencies made gains against the U.S. dollar, the strongest being the euro and closely linked currencies in continental Europe; it was the euro's turn to benefit from building "tapering" expectations in respect of its central bank's earlier quantitative-easing-oriented asset purchases.

Global growth was positive, if not spectacular, in most regions, lifted mostly by manufacturing and consumption gains. Geopolitical risks, which significantly affected many markets in 2016, generally faded from view but did not vanish in all cases (a notable exception was the United Kingdom). Other themes that we had regarded as macro headwinds to market returns in 2016—the prior long-term energy price declines, fears concerning the economy of China, vulnerability of emerging economies to balance-of-payment-induced capital flight—either diminished sharply or became virtually absent. As a result, risk-taking on the part of investors resumed, even as fundamental opportunities became smaller (because prices moved nearer to fundamental values).

Our investment process is primed not to chase shrinking investment opportunities, particularly not out of a naïve belief that lower, backward-looking volatilities mean that the capital markets are safer. The hazards of such behavior can lead to high leverage at the worst times (such as late 2007 before the Global Financial Crisis), and similarly to cutting exposures drastically in the aftermath of large upward spikes in realized risk, when return damage has already been done. Using the analogy of an impending alpine avalanche, the most dangerous time to be walking on a snowy mountainside may be just before a calamity (especially when there has been an absence of an event for a long period of time), when the scenery still looks serene. Conversely, after the avalanche has created a scene of wreckage and destruction may actually be the safest time to approach such an environment in pursuit of opportunities since the previous instability has dissipated. But, notwithstanding this, we agree with the market that ex-ante risk is low—and probably lower than long-term Equilibrium risk. However, we do not believe the true risk level is as low as contemporaneous volatility readings indicate. Thus, we have increased the risk in portfolio strategies from late 2016, but not for the purpose of chasing diminishing returns or from a belief that the world is exceedingly safe.

Within this quarter and for most of 2017, much of our focus in investment strategy has been to increase nonsystematic risks by increasing exposures in ways that do not add to total market exposure (or beta). In fact, we have maintained equity beta at or slightly below our long-term average expectation, commensurate with generally midsize beta opportunities, the majority of which have resided in Europe. Thus, we have responded to widening or narrowing opportunities between one market and another—such as increasing exposure to Australian equities, which have lagged other markets, while trimming Italian equities, which have led. We made analogous changes in emerging equities, increasing exposure to Brazil, where we conclude that the macro and political headwinds that had caused that market to underperform have now abated, and reducing exposures to Taiwan and Vietnam, which had benefited portfolios prior to our reductions and, thus, where opportunities have now diminished. We have been more cautious to increase currency risk—particularly where the primary valuation opportunity has been attractive emerging and unattractive developed currencies, though our strategy is aligned with this valuation opportunity. Our caution toward building this axis further comes from the potential risk of the long emerging, short developed currency positioning taking on characteristics of "positive beta" in select risk-off environments. We have also tried to avoid materially raising the sensitivity of the strategy to broad market risk and risk appetites as 2017 only presented a midsize fundamental opportunity in aggregate. However, we have increased currency exposures in several cases. In the fourth quarter, our changes to currency exposures involved moving from short to long of Japanese yen (a relatively belated response to the currency becoming fundamentally attractive) and from short to further short of some emerging currencies in Asia. These changes were exceptions to the general pattern noted above, involving attractive developed and unattractive emerging currencies rather than the opposite. They could be expected to offer useful diversification as

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protection from potential downside risk, and as they are justified by our fundamental expectations, they are equally compelling to unsystematic market opportunities, in both Equilibrium and short-term risk environments.

Our strategy has added value by separately taking positions long of U.K. equity and GBP in 2017, despite a period of considerable political uncertainty affecting the United Kingdom, in respect of both the stability of its government (following a midyear snap election that did damage to the ruling conservative party) and its Brexit negotiations with the European Union. These geopolitical risks could have been regarded as justification for avoiding U.K. exposure, but through our game theater approach, we instead concluded that the economic and investment implications pointed more toward bargaining inertia and a slow negotiation progress, coupled with the United Kingdom's initially hard stance being progressively relinquished. Therefore, the Brexit trajectory currently points toward less adverse outcomes than markets initially feared, which has allowed U.K. assets and the GBP to overcome some of their prior fundamental undervaluation. The situation could change and evolve quickly, but we believe it is important to develop a framework to account for geopolitical risks that will not universally lead to their avoidance in portfolio strategy. The U.K. analysis has borne this out recently.

While we agree with the market that the near-term risk environment is relatively benign, it is important to make a distinction between our risk analysis (multi-dimensional and forward-looking) and that of many investors who use a "rear-view mirror" approach, such as looking at recent levels of realized volatility or implied volatility in options markets. Our determination of near-term risk comes from an assessment of the intensity of a number of risk factors that our macro themes bring to bear. This is a focus more on *drivers* of risk than *symptoms* of risk. Our Outlook risk model is our means to model the nearer-term risk environment. Importantly, we *derive* the Outlook model from our longer-term, forward-looking Equilibrium model by influencing (or "disturbing") the Equilibrium model with these macro risk factors. In 2017, we reduced the impact of a number of these factors through our continuing analysis of risk themes. So, as previously referenced, while we do believe we are in a near-term period of relatively benign risk, our methodology remains uniquely provisioned to allow us to reverse this belief should our analysis suggest that the chances of a thematically or geopolitically induced "avalanche" rise again. The task of macro investors is to steer a smart course between greed and fear, euphoria and panic, without blindly attaching themselves to either of these poles.

In the larger picture, our longer-term investment objective is to deliver positive investment returns above inflation through a market cycle. In normal times, some of this is provided by available real risk-free interest rates ("normal" signifying a close-to-equilibrium state of the global economy and capital markets), with the remaining part of the return objective requiring dynamic management of market and currency risk over time. What is unique about the last 10 years has been the extraordinarily low level of risk-free real rates globally, which were brought down swiftly in response to the Global Financial Crisis and have since remained extremely low or negative in much of the world. This development has created two implications: one is that central bank policies of ultra-easy monetary policy have implicitly and explicitly encouraged investor risk taking; the second is a widening of the performance gap that must be filled between real risk-free rates and portfolio return objectives. With these developments aside, we do not accept the bait of an artificially stimulated risk-seeking environment—this being fraught with the danger of extrapolative expectations and antithetic to our forward-looking approach to risk and return. We remain grounded in fundamental valuation as our first step—meaning we strive to only take compensated risk and 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.

Accordingly, there will be environments in which we conclude that macro markets simply 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.

FOOTNOTES TO FUND EXPOSURE TABLE

***Credit Detail**	
European Investment Grade Spread	3.4
U.S. Investment Grade Spread	7.1
U.S. High Yield Spread	-0.5
****Select Exposures**	
India Rupee (INR)	5.1
Philippine Peso (PHP)	6.9
Singapore Dollar (SGD)	4.7

[1]Unencumbered cash is residual cash and equivalents.

Fund exposures are as of 31 December 2017.

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