FISHER INVESTMENTS EUROPE™

FOURTH QUARTER 2017

US SMALL AND MID CAP CORE

FOURTH QUARTER 2017 REVIEW AND OUTLOOK
US SMALL AND MID CAP CORE

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FOURTH QUARTER 2017 REVIEW AND OUTLOOK EXECUTIVE SUMMARY

Performance vs. Benchmark, as of 31/12/2017

	2017 Q4	YTD (31/12/2017)
Fisher US Small and Mid Cap Core (Gross of Fee)	8.1%	37.5%
Fisher US Small and Mid Cap Core (Net of Fee)	7.9%	36.5%
Russell 2500 Total Return Index	5.2%	16.8%

Source: Eagle Investment Systems. Performance is preliminary, as of 31/12/2017 and is subject to final reconciliation of accounts. Please see performance disclosures on the final page. Based in USD.

Portfolio Themes

- **Quality Tilt:** As the bull market progresses, we favour equities with stronger balance sheets and consistent margins.
- **Overweight to Information Technology:** The Information Technology sector is heavily skewed toward large, high-quality firms—a segment we expect to outperform in the later stages of a bull market. The sector should also benefit from robust global IT spending driven by the growing demand for products and services related to mobile, cloud computing and the "Internet of Things."
- **Underweight to Commodity-Oriented Sectors:** The Energy and Materials sectors likely continue to struggle as supply growth constrains commodity prices.

Market Outlook

- **Growing Investor Confidence:** Investor optimism typically increases as a bull market matures. US sentiment has improved but is not yet euphoric. Meanwhile, growing optimism in the US remains unmatched by European investors.
- **Strong Economic Drivers:** In both developed and emerging markets, economic drivers remain strong. We believe these fundamentals will come to the forefront as sentiment improves.
- **European Leadership:** As euroskeptic fears fizzle and renewed gridlock reduces legislative risk, Europe should continue to outperform in 2018.

This bull market has powered into its final third, with the MSCI All Country World Index (ACWI) adding another 5.7%, bringing calendar year 2017 gains to 24.0%.[i] We remain bullish and expect markets to deliver strong returns in 2018.

Outsized annual returns are common in bull markets' final thirds. Huge years like 1999, 1998, 1997, 1989 and 1980 all occurred as bull markets neared their peaks. As bulls age, investors generally become more optimistic. Accordingly, as equities climb further up the Wall of Worry, greed gradually replaces fear. Worries about the next downturn give way to fear of missing potential gains, and investors see less risk and more opportunity. The more these emotions percolate, the higher investors bid equities.

We have not yet seen the huge returns typical of a bull's final third. Those celebrating 2017's greatness or calling it unrepeatably large miss the fact that global equities have averaged 18% in bull markets since 1926.[ii] The fact that investors see a modestly above-average bull market year in 2017 as an outlier speaks to how much they underestimate equities' potential.

Eurozone equities led in 2017, despite a Q4 pause that had all the hallmarks of a brief countertrend. In our view, even after a stellar 2017, positive surprise potential is greater in the eurozone than in the United States and elsewhere. Currency factors helped depress European sentiment, as the MSCI ACWI rose just 8.9% in euros.[iii] While larger returns stirred Americans' animal spirits, this

i Source: FactSet, as of 05/01/2018. MSCI ACWI Index return with net dividends, 31/12/2016 – 31/12/2017. Based in USD.

ii Source: Global Financial Data, Inc. and FactSet, as of 28/12/2017. Annualised price returns in USD for bull markets from 1926 to 2007. The current is omitted as it is incomplete. GFD World Index used for bull markets from 1926 – 1970; MSCI World Index from 1970 – 2007. The World Index's 2017 price return in USD was 20.1%.

iii FactSet, as of 05/01/2018. MSCI ACWI Index return with net dividends in EUR, 31/12/2016 – 31/12/2017.

sentiment is unmatched by European investors. Add in lingering fears of weak economies, ECB policy and regional politics, and expectations for eurozone equities remain low. There is ample room for continued economic growth and strong earnings to surprise markets—a key reason we expect eurozone equities to lead again in 2018.

In Emerging Markets (EM), sentiment has improved, though doubts persist. Some experts attribute strong EM equity performance to accommodative monetary policies in developed economies like the US and eurozone, arguing that as these central banks tighten, it would remove the alleged support stimulating EM. However, in our view, many EM economies are doing better than appreciated and aren't reliant on outside help. Though many view EM as a cohesive bloc, individual nations' economic and political drivers vary. Economies that are trade-oriented and have growing services sectors and consumer classes are doing better than those reliant on commodity prices. While political drivers can be mixed—sudden shifts in regulatory or legislative landscapes aren't uncommon and can drive market uncertainty—we don't see this as problematic for the entire category. Overall, we believe EM should continue doing well, albeit with dispersion among country-level returns.

Along with non-US outperformance, we expect 2017's other big trends to persist in 2018 and believe portfolios are well positioned. Information Technology—our largest sector overweight—led in 2017 and should repeat. Robust IT-related capex, mobile adoption and cloud computing are powering demand for hardware, components and software. However, Energy—a primary underweight and 2017's worst sector—likely continues to struggle as lasting supply gluts pressure oil prices.

As for interest rates, we expect long-term US Treasury yields to remain benign in 2018. Most pundits anticipate rising rates, believing long rates are overdue to react to the US Federal Reserve's three rate hikes in 2017. However, long rates don't typically move in tandem with short rates. While the Fed controls short-term interest rates, long-term rates are market-driven—a function of real interest rates plus some inflation premium. Fed rate hikes amid low inflation are anti-inflationary, leading to a flattening yield curve, weighing on lending and money supply growth. Should the Fed hike rates further in 2018, we expect similar results. Moreover, long rates globally are highly correlated, and global monetary policy shifts have been glacial, giving markets ample time to digest moves.

While sentiment in the United States has improved, it isn't euphoric. Professional forecasters again project single-digit S&P 500 returns. Equities usually don't do what the consensus expects. That doesn't mean they automatically do the opposite—returns could be more or less positive than widely expected, too. While a negative year would surprise, this seems unlikely—fundamentals are strong, and extant risks appear too small or unlikely to strike and wallop markets. With the global economy on an upswing, world trade humming, European yield curves steeper and earnings growing nicely, surprisingly strong returns seem much more probable.

Because the last bull market ended prematurely, investors haven't seen rational optimism since the late 1990s. As a result, many have trouble discerning optimism from genuine euphoria. For a windowpane into future euphoria equities may encounter, see bitcoin. Not only is it a sign investors can still muster animal spirits (versus being permanently scarred by the financial crisis), it shows what to watch for as sentiment improves. Newfangled technologies and new paradigms often emerge near the end of bull markets, driving normally rational people to shun reason and make speculative bets. What matters is the moment when such irrational exuberance spills into broader markets. We are watching closely for this but don't believe it is here yet.

That said, this bull market will end one day. In this later bull market phase, one of our most important research efforts is looking for indications the next bear is approaching. For now, we don't see a bear market forming. However, it wouldn't surprise us if we saw a correction (-10% to -20%) this year. Corrections are impossible to predict and time consistently. We believe it is optimal to wait it out if one occurs and look forward to the gains on the other side.

Portfolio Attribution

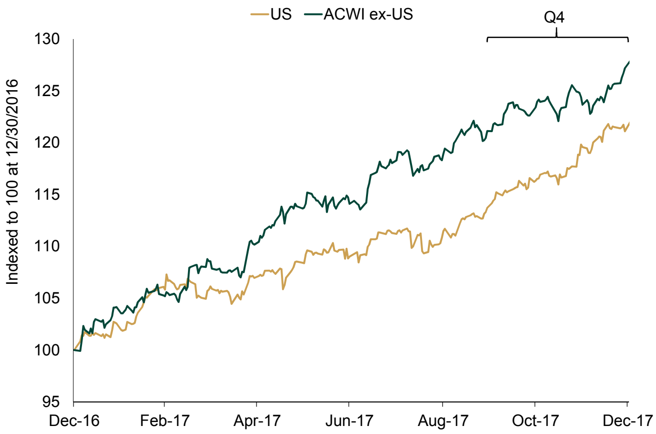
The Fisher US Small and Mid Cap Core portfolio outperformed the Russell 2500 Total Return index in Q4 2017. Equity selection contributed to relative return, while sector allocation detracted. Selection within Information Technology was the largest contributor to relative return, driven by fiber laser developer IPG Photonics, electronic payment services provider Total System Services and semiconductor manufacturer ON Semiconductor Corporation. Additionally, selection within Health Care contributed as health information technology company Quintiles IMS Holdings, as well as medical device companies Align Technology and Insulet Corporation outperformed. Conversely, an underweight to Oil, Gas & Consumable Fuels detracted as the industry outperformed the broader benchmark.

THEMATIC UPDATE AND MARKET OUTLOOK

Q4 RECAP

The global economy is expanding, with widespread growth supported by broadly positive economic data to ultimately help boost sentiment. Non-US leadership slowed in Q4, though as shown in Exhibit 1, this is most likely a brief counter trend already showing signs of reversal as the quarter concluded.

Exhibit 1: Non-US Leadership Picks Up



Source: FactSet, as of 01/02/2018 in USD.

US economic growth accelerated in 2017, particularly in Q4, boosting investor optimism. While many assess US growth through a political lens, the President's administration does not significantly impact economic results. The nation's vast private sector remains the driving force. In Europe, the UK expansion continued despite Brexit-related fears and accelerated as 2017 waned. The eurozone also held firm, with growth accelerating from 2016. Likewise, Emerging Markets with strong exposure to the Technology sector's supply chain—particularly China and Taiwan—benefited from a pickup in global demand.

Despite lingering fears over eurosceptics and President Trump, politics in the developed world look benign for markets. Most governments remain gridlocked, preventing sweeping change. In the US, November's midterms aren't as important to markets as people think. After spending its political capital on tax reform, Congress probably does little, especially with campaign season approaching. Moreover, intraparty gridlock persists, preventing the GOP-held Congress from accomplishing much.

Politics abroad are similarly positive. Political uncertainty still has some room to fall in Europe, tied to Catalonia's separatist movement and March's Italian election. Brexit talks remain glacial, with both sides seemingly grinding toward a Brexit in name only. The result: few material near-term changes, particularly where trade is concerned. That said, we don't expect falling uncertainty to play as big a role this year as it did in 2016 and 2017.

STRONG RETURNS IN THE FINAL THIRD

As mentioned in the Executive Summary, we believe this bull market to have emphatically entered its final third, marked by strong returns, which should continue in 2018. The large later years of a bull market feed the euphoria typifying market peaks. Historically, a large share of a bull market's return usually comes late as investor sentiment evolves to optimism and then euphoria, drawing those who were formerly on the sidelines to enter the market—propelling equity prices higher. Exhibit 2 dissects historical bull markets into thirds, revealing, on average, almost 40% of a bull's return can come in the final third of its life.

Exhibit 2: Bull Market Returns by Thirds

Bull Start	Bull End	Bull Length (Years)	% of Bull Return by Third of Lifespan		
			First Third	Second Third	Final Third
01/06/1932	06/03/1937	4.8	62%	4%	34%
28/04/1942	29/05/1946	4.1	51%	12%	37%
13/06/1949	02/08/1956	7.1	39%	10%	51%
22/10/1957	12/12/1961	4.1	60%	-4%	45%
26/06/1962	09/02/1966	3.6	59%	26%	15%
07/10/1966	29/11/1968	2.1	59%	-4%	46%
26/05/1970	11/01/1973	2.6	73%	6%	21%
03/10/1974	28/11/1980	6.2	59%	-6%	47%
12/08/1982	25/08/1987	5.0	37%	23%	40%
04/12/1987	16/07/1990	2.6	42%	49%	9%
11/10/1990	24/03/2000	9.5	26%	29%	45%
09/10/2002	09/10/2007	5.0	58%	12%	30%
Median ex Current		**4.5**	**51%**	**12%**	**37%**

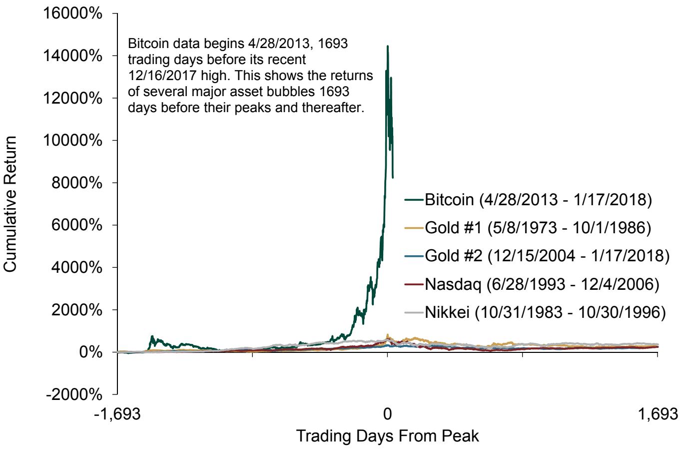
Source: Global Financial Data, Inc., as of 21/11/2017. Calculations are based on S&P 500 price returns for the periods shown.

BITCOIN AS A WINDOWPANE TO EUPHORIA

Since the last bull market ended prematurely, investors haven't seen stock market euphoria for nearly 20 years, since the late-1990s' Tech bubble inflated. As a result, many mistake rational positivity for euphoria. What will euphoria look like when it arrives? The frenzy over bitcoin and cryptocurrencies is a classic preview.

The bitcoin spike dwarfs most major historical bubbles. Exhibit 3 compares bitcoin to other recent frenzies, including gold in the late-1970s, the Nasdaq in the late-1990s and Japanese stocks in the late-1980s. It is impossible to know whether 16 December, 2017 was bitcoin's peak, making the methodology imperfect. But the initial bubble inflation isn't knowable, so this is the fairest comparison we can create. And it is illustrative, showing bitcoin's astronomical relative magnitude. When you consider that bitcoin's supply increases at a steady fixed rate, it takes astounding demand to drive something up so high in such a short amount of time. That demand is driven by sentiment—euphoria.

Exhibit 3: Is Bitcoin A Bubble?



Source: Fisher Investments Research, FactSet, Global Financial Data and CoinMarketCap.com, as of 18/01/2018. All periods are 1,693 days before and after the peak, except bitcoin (1,693 before and 32 after) and Gold #2 (1,693 before and 1,601 after), as this is all the time elapsed.

The tone and content of the bitcoin debate was also telling. Those urging caution offered well-supported and rational arguments centring on the lack of fundamental reasons for long-term growth. The pro-bitcoin arguments, meanwhile, were based on the speculation of assumed scenarios in the future, and a lack of examining the broader picture of cryptocurrencies beyond Bitcoin. For example, one misconception fueling Bitcoin's euphoria is that its long term supply is fixed at 21 million, with 16.8 million currently in circulation.[iv] The claim is that with a continually growing economy and a fixed supply of currency to match, the value of the currency must rise. The glaring error here is that Bitcoin is not the only cryptocurrency – there are over 1,400 other cryptocurrencies, with new Initial Coin Offerings (ICOs) happening all the time.

Another signature sign of euphoric speculation were the wild rallies taking place in companies who changed their name to cryptocurrency based titles. For example, the Long Island Iced Tea Corp, a drink producer, soared 500% after the firm announced it would become "Long Blockchain Corp" [v] – starkly reminiscent of the plethora of tech titles hitting the markets during the Tech bubble.

Evidence of a bubble and the implied burst raises the concern of the potential effect on markets. However, the market cap of all cryptocurrencies was about $759 billion as of 03/01/2018.[vi] For perspective, the entire crypto market is just 0.6% of global GDP.[vii] A bear market wallop requires an event to shave trillions of dollars of global GDP – a feat which cryptocurrencies do not currently have the size to provide.

iv Source: CoinMarketCap.com, as of 03/01/2018.

v Sophie Christie, "Want Your Company's Share Price to Rocket? Simply Add 'Blockchain' to Its Name," The Telegraph, 21 December, 2017.

vi Source: CoinMarketCap.com, as of 18/01/2018.

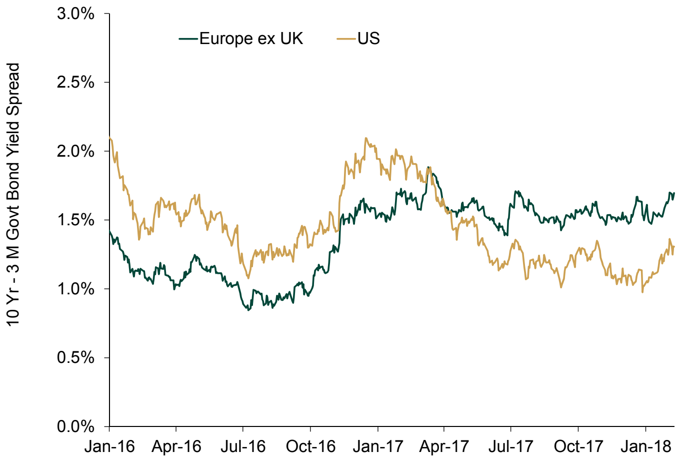
vii Source: CoinMarketCap.com and IMF, as of 25/01/2018. Market capitalization of all cryptocurrencies on 24/01/2018 as a percentage of 2016 global GDP.

2018 FORECAST

2017's sector and country winners should repeat in 2018. High quality firms displaying healthy profit margins and strong growth prospects, characteristic of consumer oriented sectors including Health Care, Consumer Staples, and Information Technology should outperform. Their profitability attracts investors seeking more stable investments in a maturing bull market. Conversely, commodity dependent sectors such as Energy should underperform given the industry's quickening supply response to price changes, keeping prices range-bound.

Despite last year's leadership and falling uncertainty, the gap between sentiment and reality is still wider in Europe than most places. People see the expansion as fragile. Few notice the loan growth pickup and steeper yield curves, which should boost European banks (Exhibit 4). With robust balance sheets, they are well positioned to take advantage. Many fear the end of the European Central Bank's (ECB) quantitative easing (QE), not realizing the ECB slowed bond purchases throughout 2017—and eurozone stocks led. The end of QE was bullish in the US and Britain, and we see no reason why the eurozone would be different.

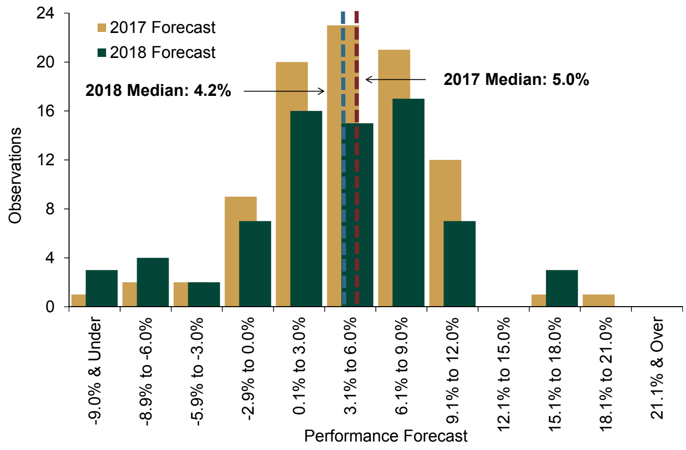
Exhibit 4: Favourable European Yield Spread Signals Growth Prospects in Europe



Source: FactSet, as of 09/02/2018.

U.S. investors broadly see 2017's returns as great, even though they were in line with the S&P 500's long-term average return during bull markets. This suggests to us investors don't fathom the potential for robust returns in a maturing bull market, a sign sentiment remains in check as 2018 kicks off. Even so, doubts still linger. People seek catalysts to drive stocks higher and perceive few. Many see old stand-bys like rising valuations and all-time highs as signs of trouble. Euphoria arrives when investors run out of doubts. At that point, professional forecasts will probably call for much higher returns than they are now. Entering 2018, the median S&P 500 forecast for the year was 4.2%--lower than 2017's 5.0% (Exhibit 5).

Exhibit 5: Professional Forecasts Remain Cautious



Source: Fisher Investments, Research, as of 29/12/2017. S&P 500 price level forecasts are made by equity strategists from a variety of firms within the investment industry.

As always, we remain vigilant for signs of the inevitable bear, but do not believe any catalysts loom today. Today's risks are either too well-known, too small to destroy trillions of dollars of global GDP, or simply false. That's not to say a correction isn't possible. Unlike a bear market, corrections can happen for a number of reasons or no reason at all, often vanishing as soon as they appear. But corrections are a healthy feature of bull markets. Without the occasional worry, investors can become overly euphoric, resulting in a risky environment for equities. In fact, as of the date of this writing, global markets had either entered or were approaching correction territory. However, it exhibits the classic characteristics of a correction: a sharp, sentiment-driven market drop. We do not believe this reflects a shift in global fundamentals or the beginning of a bear market.

US Commentary

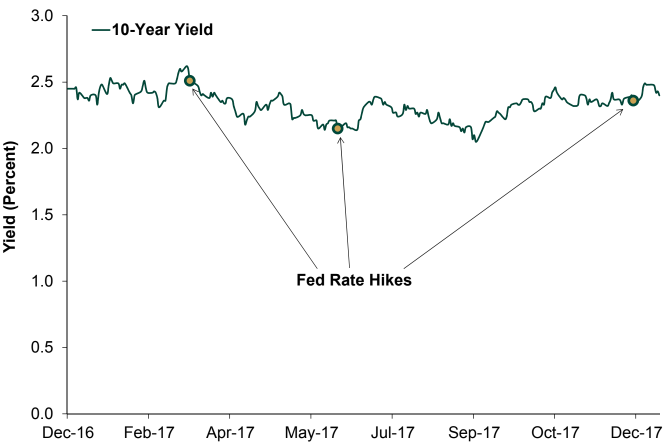
US Commentary

As expected, U.S. stocks performed well in 2017 with the S&P 500 completing its full-year streak of positive monthly returns in December, rising 1.1%, to bring full-year returns to 21.8%.[viii] President Trump marked his first major legislative achievement in December, as Congress capped months of debate by passing tax reform. Meanwhile, Fed Board member Jerome Powell was selected to replace Janet Yellen as Fed Chair. On the trade front, NAFTA negotiations concluded their fifth round mid-way through the quarter. The negotiations failed to resolve numerous issues. In our view, this is to be expected as trade talks are known to be contentious, however, all parties still have a vested interest in compromise. Overall, economic fundamentals remain strong, political gridlock continues, and sentiment is rising, all leading to expectations of a great year for US stocks in 2018. However, we still expect US equities to underperform Non-US, as economic drivers in Europe outpace the US.

Fed Policy Impact on Long Rates

Entering 2017, most expected long-term interest rates to rise as the Fed escalated short-term rate hikes. But the market had other ideas. Even as the Fed raised overnight rates three times and economic growth accelerated, 10-year yields finished 2017 five basis points below where they began (Exhibit 6). We expect long rates to repeat the feat this year, finishing 2018 little changed.

Exhibit 6: Long Rates in 2017



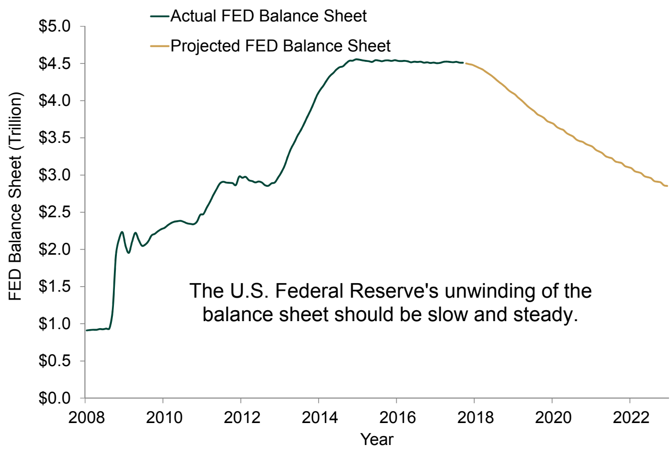
Source: FactSet, as of 09/01/2018. 10-year US Treasury yield, constant maturity, 31/12/2016 – 31/12/2017.

While the Fed controls overnight rates, the market determines long rates. Like all assets, they move on supply and demand, and the chief demand driver is inflation expectations. The long-term interest rate is basically the real interest rate plus (or minus) some premium for inflation, and real rates are largely the cumulative growth rate of the developed world (with some variance by country).

When the Fed hikes rates amid low inflation, as it did last year, it is anti-inflationary. People saw inflation rates slow as the year progressed and figured the Fed did its job, successfully containing prices. Hence long rates fell as investors did not demand as much of an inflation premium. This flattened the yield curve, weighing on loan growth and broad money supply. As Milton Friedman preached, "Inflation is always and everywhere a monetary phenomenon..."[ix]

Beyond fed-funds rate hikes, the Fed began allowing its balance sheet to contract in October, prompting further fears of higher rates, but given the early foresight provided by the Fed last summer, the market has had plenty of time to discount the news. Further, the Fed isn't selling bonds; rather, it will discontinue reinvesting a small amount of maturing bonds each month. As Exhibit 7 displays, if the Fed sticks to the current plan, its balance sheet won't return to pre-2008 levels until 2024.

Exhibit 7: Projected FED Balance Sheet



Source: Federal Reserve, actuals as of October 2017, projected from November 2017 to December 2022.

viii *Source: FactSet, as of 08/02/2018.*

ix *Friedman, M. (1983). The counter-revolution in monetary theory: first Wincott memorial lecture, delivered at the Senate House, University of London, 16 September, 1970. London: Institute of Economic Affairs.*

Long-term interest rates throughout the developed world are highly correlated. While monetary policy abroad is shifting some, the pace is slow and widely telegraphed—unlikely to move markets materially. The ECB and Bank of Japan continue buying long-term bonds, albeit fewer of them, pressuring long-term interest rates. The Bank of England reacted to higher inflation by hiking overnight rates in November, but this merely reversed August 2016's post-Brexit rate cut. After the hike, UK long rates fell, flattening the yield curve—another example of hikes' anti-inflationary, rate-lowering impact.

The low inflation seen in recent years has peaked the curiosity of policymakers and investors, who cannot reconcile low inflation with accelerating GDP and low unemployment. With regards to understanding inflation, many believe in the Phillips Curve model, which links unemployment to inflation by the logic that when unemployment is low, businesses must raise wages to attract workers, creating a wage-price spiral. In our view, however, there is over a century's worth of data showing money supply growth, not unemployment, drives prices. In our fractional reserve banking system, banks create most new money through lending, which depends on potential profits, which stem from the yield curve. Banks borrow at short rates, lend at long rates and profit off the spread—known as their net interest margin. Flatter yield curves shrink that spread and banks' potential profits, driving them to lend less. That slows money supply growth, with a downstream effect on prices.

Tax Reform and Other Political Developments

Eleven months after his inauguration, President Donald Trump achieved his first major legislative accomplishment, signing tax reform into law. The debate and eventual passage sparked headlines and politicised speculation. While there are many impacts at the individual and company-specific level, the macroeconomic and stock market impact is vastly overestimated by most commentators.

Conventional wisdom argues tax cuts help stocks and hikes hurt. Exhibits 8 – 9 display a historical analysis of both. Specifically, they display the 12-month return after every policy adjustment to top tax rates since 1926.[x] Ultimately, the conclusion is that tax changes have no material impact on stocks.

Exhibit 8: Corporate Income Tax Rate Shifts

Corporate Tax Hikes			Corporate Tax Cuts		
Effective Date	New Tax Rate	Fwd 12-Month Return	Effective Date	New Tax Rate	Fwd 12-Month Return
26 Feb, 1926	13.5%	8.6%	29 May, 1928	12.0%	24.2%
1 Jan, 1930	12.0%	-28.5%	17 Dec, 1929	11.0%	-29.9%
6 Jun, 1932	13.8%	98.0%	1 Jan, 1946	38.0%	-11.9%
22 Jun, 1936	15.0%	2.1%	26 Feb, 1964	50.0%	12.3%
28 May, 1938	19.0%	23.8%	1 Jan, 1965	48.0%	9.1%
8 Oct, 1940	24.0%	-5.3%	1 Jan, 1970	49.2%	-0.1%
20 Sep, 1941	31.0%	-15.8%	1 Jan, 1971	48.0%	10.8%
21 Oct, 1942	40.0%	25.2%	1 Jan, 1979	46.0%	12.3%
23 Sep, 1950	42.0%	20.4%	1 Jan, 1987	40.0%	2.0%
20 Oct, 1951	50.8%	3.5%	1 Jan, 1988	34.0%	12.4%
1 Jan, 1952	52.0%	11.8%			
28 Jun, 1968	52.8%	-2.3%			
10 Aug, 1993	35.0%	2.4%			
	Average	**11.1%**		Average	4.1%
	Median	**3.5%**		Median	9.9%

Source: Tax Policy Center and Global Financial Data, Inc., as of 27/10/2017. S&P 500 price returns for the periods indicated.

Exhibit 9: Personal Income Tax Rate Shifts

Income Tax Hikes			Income Tax Cuts		
Effective Date	New Tax Rate	Fwd 12-Month Return	Effective Date	New Tax Rate	Fwd 12-Month Return
1 Jan, 1930	25.0%	-28.5%	17 Dec, 1929	24.0%	-29.9%
6 Jun, 1932	63.0%	98.0%	1 Jan, 1946	86.5%	-11.9%
1 Jan, 1936	79.0%	27.9%	2 Apr, 1948	82.1%	-1.4%
25 Jun, 1940	81.1%	0.9%	16 Aug, 1954	91.0%	34.8%
21 Oct, 1942	88.0%	25.2%	26 Feb, 1964	77.0%	12.3%
29 May, 1944	94.0%	23.1%	1 Jan, 1965	70.0%	9.1%
23 Sep, 1950	84.4%	20.4%	1 Jan, 1970	71.8%	-0.1%
20 Oct, 1951	91.0%	3.5%	1 Jan, 1971	70.0%	10.8%
1 Jan, 1952	92.0%	11.8%	13 Aug, 1981	69.1%	-22.2%
28 Jun, 1968	75.3%	-2.3%	1 Jan, 1982	50.0%	14.8%
30 Dec, 1969	77.0%	0.7%	1 Jan, 1987	38.5%	2.0%
1 Jan, 1991	31.0%	26.3%	1 Jan, 1988	28.0%	12.4%
10 Aug, 1993	39.6%	2.4%	7 Jun, 2001	39.1%	-19.5%
2 Jan, 2013	39.6%	25.3%	1 Jan, 2002	38.6%	-23.4%
			28 May, 2003	35.0%	17.6%
	Average	16.8%		Average	0.4%
	Median	16.1%		Median	2.0%

Source: Tax Policy Center and Global Financial Data, Inc., as of 27/10/2017. S&P 500 price returns for the periods indicated.

We see several reasons tax cuts lack power to sway stocks. For one, much of the discussion about tax cuts' market impact presumes they still are not priced into stocks, but tax changes play out in broad daylight and take significant time to enact—affording markets ample time to discount potential effects.

Economically, we don't expect the tax cut to provide a huge growth boost. Business investment is already at record highs (16% above Q1 2008's pre-recession peak) and is not a primary factor in this expansion's slow GDP growth.[xi] Moreover, the US economy is growing steadily.

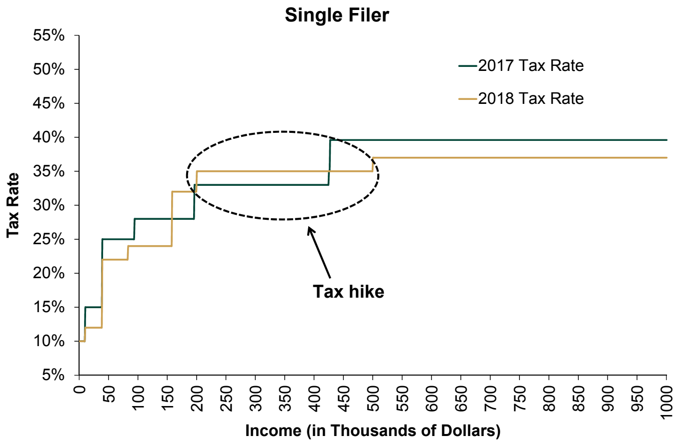
x Source: Global Financial Data, Inc. and FactSet, as of 02/01/2018. Annualised price returns in USD for bull markets from 1926 to 2007. The current is omitted as it is incomplete. GFD World Index used for bull markets from 1926 – 1970; MSCI World Index from 1970 – 2007. The MSCI World Index's 2017 price return in USD was 20.1%.

xi Source: US Bureau of Economic Analysis, as of 22/01/2018. Real private nonresidential fixed investment, Q1 2008 – Q3 2017.

A second reason tax changes lack a preset impact: They often create broad categories of winners and losers. While many taxpayers will pay lower rates, some will pay more, because the law reduced income thresholds for some of the higher income bands. All else equal, many single filers earning between $157,000 and $427,000 will see higher taxes (Exhibit 10). Heads of household lose most of their filing advantages with a similar tax hike in the mid/upper income range. Joint filers get tax cuts unless they make between $400,000 and $424,000 (Exhibit 11).[xii]

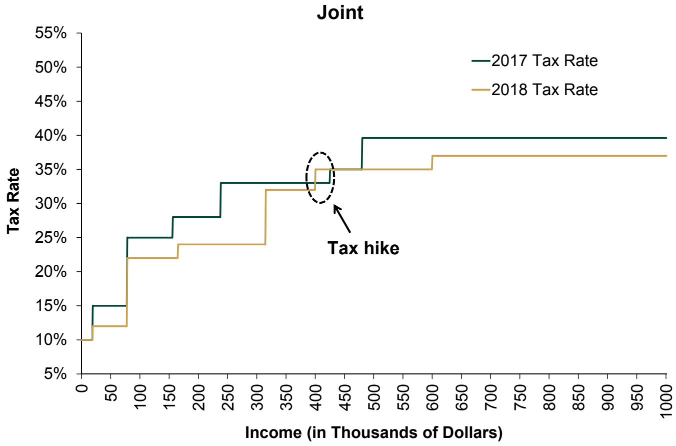
The legislation also strikes many deductions. It caps state and local tax (property or income) deductibility at $10,000 and limits mortgage interest deductions. It further eliminates deductions for miscellaneous expenses like tax preparation, legal and investment management fees. To compensate, it doubles the standard deduction, likely helping most taxpayers. But those benefitting from specific itemised deductions will lose.

Exhibit 10: The Single Hike within the Cut



Source: Tax Foundation, as of 19/12/2017.

Exhibit 11: The Joint Hike within the Cut



Source: Tax Foundation, as of 19/12/2017.

The bill has positive and negative effects for corporations. While the headline rate cut from 35% to 21% is a plus, many major American businesses weren't paying anything near 35%. The law also changes America's system of taxing profits earned abroad to eliminate blanket double taxation—probably cheering many businesses. Still, it strikes many deductions, and a new base-erosion anti-abuse tax penalises firms who use transactions between foreign subsidiaries to reduce taxable income.

xii *"Details of the Conference Report for the Tax Cuts and Jobs Act," Jared Walczak, Joseph Bishop-Henchman and Nicole Kaeding, Tax Foundation, 15/12/2017. https://taxfoundation.org/conference-report-tax-cuts-and-jobs-act/*

MIDTERM ELECTIONS

While the media expect big shifts in the coming midterm elections, we suspect small shifts are likelier. Predicting those shifts is premature, but it should gain clarity later on. It is possible, however, to survey the structural factors for November, particularly in the Senate.

The GOP's one-seat edge implies the Democrats could win Senate control without a huge shift. But it is also possible Republicans strengthen their hand. The Democrats have many more seats up for grabs and will likely have to devote significant campaign resources to defending them (Exhibit 12). The Republicans' House edge is larger, with Democrats needing to win 24 seats to take it.

If Democrats did win the Senate and the House, the market impact should not be significant as gridlock would still persist, reducing the probability of sweeping legislation with the power to roil markets to pass – a bullish sign.

Exhibit 12: 2018 Senate Races

Senator	Party	State	Percent of Vote for Trump in 2016	Percent of Vote for Romney in 2012	Percent of Vote for McCain in 2008	Percent of Vote for Bush in 2004	Percent of Vote for Bush in 2000
Barrasso, John	R	WY	70%	69%	65%	69%	68%
Manchin, Joe, III	D	WV	69%	62%	56%	56%	52%
Heitkamp, Heidi	D	ND	64%	58%	53%	63%	61%
Corker, Bob*	R	TN	61%	59%	57%	57%	51%
Fischer, Deb	R	NE	60%	60%	57%	66%	62%
Wicker, Roger F.	R	MS	58%	55%	56%	59%	58%
Tester, Jon	D	MT	57%	55%	50%	59%	58%
Donnelly, Joe	D	IN	57%	54%	49%	60%	57%
McCaskill, Claire	D	MO	57%	54%	49%	53%	50%
Cruz, Ted	R	TX	53%	57%	55%	61%	59%
Brown, Sherrod	D	OH	52%	48%	47%	51%	50%
Flake, Jeff*	R	AZ	50%	54%	54%	55%	51%
Nelson, Bill	D	FL	49%	49%	48%	52%	49%
Casey, Robert P., Jr.	D	PA	49%	47%	44%	48%	46%
Baldwin, Tammy	D	WI	48%	46%	42%	49%	48%
Stabenow, Debbie	D	MI	48%	45%	41%	48%	46%
Hatch, Orrin G.*	R	UT	46%	73%	63%	72%	67%
Heller, Dean	R	NV	46%	46%	43%	50%	50%
Klobuchar, Amy	D	MN	45%	45%	44%	48%	46%
Kaine, Tim	D	VA	45%	47%	46%	54%	52%
King, Angus S., Jr.	I	ME	45%	41%	40%	45%	44%
Menendez, Robert	D	NJ	42%	41%	42%	46%	40%
Carper, Thomas R.	D	DE	42%	40%	37%	46%	42%
Murphy, Christopher	D	CT	42%	41%	38%	44%	38%
Whitehouse, Sheldon	D	RI	40%	35%	35%	39%	32%
Heinrich, Martin	D	NM	40%	43%	42%	50%	48%
Cantwell, Maria	D	WA	38%	41%	40%	46%	45%
Gillibrand, Kirsten E.	D	NY	37%	35%	36%	40%	35%
Cardin, Benjamin L.	D	MD	35%	36%	36%	43%	40%
Warren, Elizabeth	D	MA	34%	38%	36%	37%	33%
Feinstein, Dianne	D	CA	33%	37%	37%	44%	42%
Sanders, Bernard	I	VT	33%	31%	30%	39%	41%
Hirono, Mazie K.	D	HI	30%	28%	27%	45%	37%

Source: US Senate, Fisher Investments Research. Senators up for re-election in 2018 as of 27/12/2017. Sanders and King caucus with the Democrats.
**Senators not seeking re-election.*

Non-US Developed Commentary

NON-US DEVELOPED COMMENTARY

Initially, 2018's political calendar may appear eventful and volatile. Brexit negotiations continue, rumored leadership challenges continue affecting Prime Minister Theresa May, and the anti-establishment Five Star Movement tops polls ahead of Italy's March election. Yet the common thread amongst all of this is political gridlock, which should keep legislative risk low throughout the developed world. This has been a positive force for global markets in recent years and should remain so in 2018.

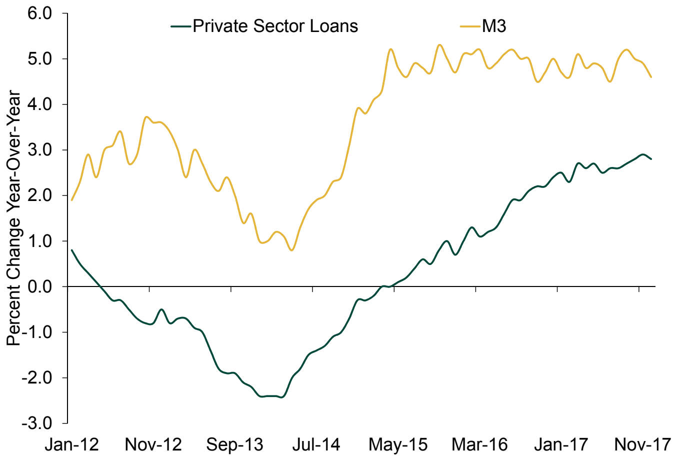
EUROZONE: EXPANSION STRONG AND WIDESPREAD

The eurozone's expansion is ongoing, with GDP growing for the 19th consecutive quarter in Q4 2017. IHS Markit's December eurozone composite purchasing managers' index (PMI)—a survey tallying the breadth of growth—hit 58.1. Readings above 50 indicate expansion and December's read is near a seven-year high.[xiii] All four of the largest economies' (Germany, France, Italy, Spain) composite PMIs remain in the high-50s, indicating widespread services and manufacturing expansion.

The outlook also looks positive, with The Conference Board's Leading Economic Index (LEI) for the eurozone up 0.8% m/m in November, its 15th consecutive monthly rise, with all eight components positively contributing. The yield spread—one of the LEI's most forward-looking components—was a primary contributor to the increase. A good proxy for loan profitability, it suggests healthy loan and money supply growth should continue underpinning the expansion.

Meanwhile, broad M3 money supply has steadily risen for three years, remaining robust after the ECB first slowed the pace of bond purchases—"tapered" its quantitative easing (QE) programme—in January 2017. Reducing QE last January eased some of the pressure on long rates, contributing to the yield curve's steepening—which we believe drove the acceleration in loan growth (Exhibit 13). We expect similar as the ECB again tapers its asset purchases this year, defying widespread fears to the contrary. As investors gradually realise the ECB isn't responsible for the continued expansion, we believe sentiment should improve, helping lift eurozone stocks.

Exhibit 13: Loan Growth is Rising and Money Supply Growth is Steady



Source: European Central Bank, as of 18/01/2018. January 2012 – December 2018.

THERESA MAY'S TENUOUS GRIP

May's struggles continued in Q4 despite the Phase One agreement, as Labour regularly outpolled the Conservatives. Further weakening her hand, she suffered a legislative defeat over amendments to the EU withdrawal bill and had to U-turn on plans to enshrine the Brexit date into UK law in order to avoid a second loss. An early-January cabinet reshuffle did little to shore up her position, especially with some high-profile MPs refusing ministerial posts. By month's end, after Chancellor Philip Hammond publicly advocated a soft Brexit with only "very modest" changes to the UK's relationship with the EU, the eurosceptic wing of the Conservative Party was threatening a leadership challenge.

To the casual observer, this might look like political instability. However, for markets, the upshot is political gridlock. Even if the Tories were united, May's minority government would prevent most radical legislation from passing. Internal divisions and Brexit distractions throw further sand in the gears. Although the infighting and inaction might be frustrating for voters, for markets, it means little risk to property rights and regulations. When businesses and investors can be reasonably confident that the rules won't change for the foreseeable future, they are generally less risk-averse—a positive force for markets.

xiii Source: IHS Markit, as of 11/01/2018.

As Labour's poll numbers ascended, the financial community started considering the possibility of Jeremy Corbyn becoming PM, fearing markets could take a hit if a leftist government took power. We believe this is far too speculative. For one, the next general election isn't scheduled until 2022—anything could happen between then and now. A snap election is possible but impossible to forecast. Plus, as 2017's election showed, polls can change radically over the course of a campaign. Should a change in government become more likely, we will analyse the potential outcomes and market impact. Note, though, that eliminating political bias is critical when doing this. No politician or political party is inherently bad or good for markets, and UK shares have done well with governments at both ends of the political spectrum. Markets care about policies, not personalities, and it is too early to know which policies the next government will pursue, much less pass, regardless of who heads it.

The Reality of Brexit Phase One

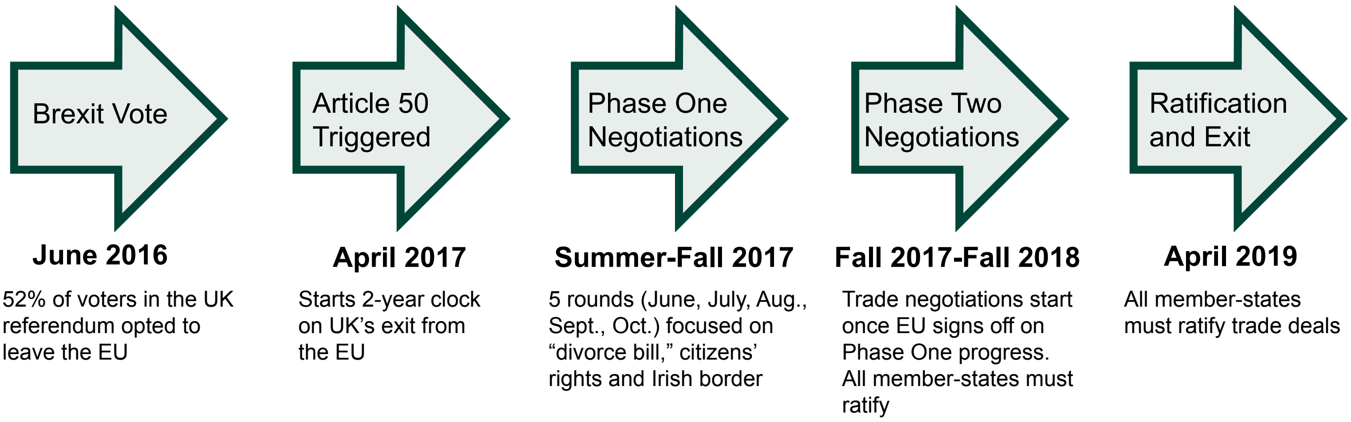
In early December, negotiators concluded the first round of Brexit talks, setting the stage for trade discussions to take stage in 2018. Many hailed the agreement as a breakthrough, but in reality this simply removed most of the provisions, with much remaining unknown. The negotiation process remains glacial—part of the long-term structural backdrop, in our view, and not a cyclical driver of UK markets.

Exhibit 14 on the next page shows the Brexit timeline, presuming they stick to the two-year window stipulated in Article 50 of the EU Treaty. Phase One talks focused on citizens' rights, payment to settle the UK's previously agreed EU budget and pension commitments, the European Court of Justice's jurisdiction, and the Irish border. When announcing the Phase One breakthrough, politicians hailed it as a broad agreement. Yet a closer read shows they left much to be decided later. For instance, headlines said the UK and EU agreed on a £39 billion "divorce bill," referring to how much the UK will contribute to the EU budget after Brexit. However, this figure comes from the UK government's "conservative" estimates of expected future payments, which the EU allowed them to use when presenting the agreement. EU officials believe the bill will be closer to £60 billion. The actual amount remains unknown, as it was before the alleged breakthrough.

Notably for markets, both sides seem determined to grind toward a Brexit in name only. Even Boris Johnson, an arch Brexit campaigner in 2016, advocates strong trade links between the UK and EU (including fanciful talk of a cross-Channel bridge). All involved remain in favour of a post-Brexit "transition period," which would phase Brexit in slowly after the official exit date. May publicly says she envisages a two-year transition, but we wouldn't be surprised if a longer period ultimately wins out. In late January, The Telegraph reported UK officials were discussing a three-year transition. And, for its part, EU leaders think the final accord might not take effect until 2025.

Equity markets generally look 3 – 30 months ahead, pricing in the likely reality during that span. Accounting for the transition period, Brexit is likely far outside that realm. Over the foreseeable future, which markets care most about, it looks increasingly likely that the rules of UK – EU commerce won't change much. Changes taking place afterward should be well-known long beforehand, giving markets ample time to adapt. There is very little room for sudden, sweeping change to take place the day after people discover it, and surprises are what move stocks most.

Exhibit 14: Brexit Timeline



ITALY'S ELECTION

Italy's election, scheduled for 4 March, continues making investors nervous. The anti-establishment Five-Star Movement (M5S) leads current polling, renewing last year's fears of populism splintering the euro. Whether or not M5S takes the most seats, we believe these fears are overwrought.

As Exhibit 15 shows, although M5S leads polls, the top three parties are polling similarly, making it unlikely one group pulls away. Moreover, recent changes to Italy's electoral laws removed the automatic majority awarded to any party that managed to win at least 40% of the vote. Instead, about 40% of parliamentary seats will be chosen on a "first-past-the-post" basis (i.e., "winner takes all") and proportional representation (via party list) decides the rest. Hence, a divided government looks like the most likely outcome.

Moreover, M5S has already walked back its earlier anti-euro rhetoric, calling a pledge to hold an "Italexit" referendum merely a negotiating ploy. They have also pledged to abide by the eurozone's deficit targets, placing very little daylight between their and mainstream parties' policies. Thus, even if they gain some seats, it isn't clear what their influence would actually be.

Exhibit 15: Italian Election Polling

Party	Polling on 9 January
Five-Star Movement	28.1%
Democratic Party (Centre-Left)	20.7%
Forza Italia (Centre-Right)	18.0%
Northern League (Anti-EU Centre-Right)	12.6%
Free & Equal (Left)	6.7%
Brothers of Italy (Anti-EU Right)	5.3%
Others	8.6%

Source: Matrix, as of 26/01/2018.

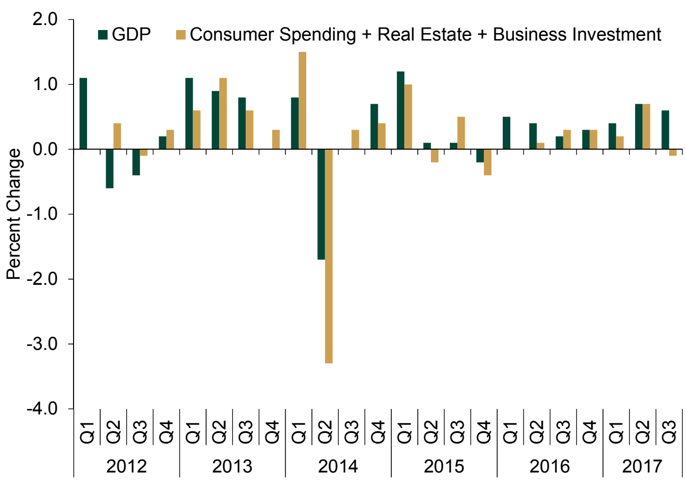
JAPAN

In Japan, Prime Minister Shinzo Abe's Liberal Democratic Party (LDP) emerged triumphant in snap parliamentary elections. The LDP and its coalition partner, Komeito, won a combined 312 seats, maintaining its supermajority. Despite some initial momentum for the opposition—in particular the upstart Party of Hope, led by popular Tokyo governor Yuriko Koike—voters opted for the status quo.

Later in the quarter, Japan and 10 other nations made headlines after agreeing in principle on a multilateral trade pact, known as the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP). Similar to the Trans-Pacific Partnership that included the US, CPTPP would eliminate tariffs on industrial and farm products. Other provisions include regulating online commerce and intellectual property. While the deal is far from being finalised—some details need finalising and all individual countries' governments must approve—it counters worries about global trade.

Exports continue driving Japanese expansion while domestic demand lags, which we think speaks to better conditions elsewhere. November export values rose 16.2% y/y, accelerating from October's 14.0%.[xiv] Import values were up 18.9%, slowing slightly from October's 19.2%, which was its fastest growth rate in four years.[xv] However, trade gains were largely due to currency translation. In volume terms, November exports rose 5.5% y/y and imports rose just 2.6%—one way to see Japanese domestic demand remains unexceptional.[xvi] Other figures confirm this as pure private sector growth (the sum of private consumption, business investment and real estate investment) was negative (Exhibit 16).

Exhibit 16: GDP and Its Private Sector Components



Source: Japan Cabinet Office, as of 18/01/2017. Q1 2012 – Q3 2017.

xiv Japan Customs, as of 19/12/2018

xv Ibid.

xvi Ibid.

More recent data suggest consumer spending remained weak in Q4. November retail sales rose 1.9% m/m, rebounding from October's -0.1% dip, but year-over-year, the series mostly hovered around 2% in 2017.[xvii] The same holds for broader household spending, of which retail is only a slice. November consumption expenditures rose 1.7% y/y, up from October's -0.3% decline, but that was just its third month since April 2016 in positive territory.[xviii]

Absent major structural reform, robust growth isn't likely. We don't see Prime Minister Shinzō Abe's October snap election victory as much of a game changer on that front. Abe's government has repeatedly shied away from major overhauls to Japan's labour markets or other deep-seated issues. Even low-hanging fruit like corporate tax cuts—first mooted years ago—remains slow-going. The latest proposal, passed by the cabinet in late December, would cut tax rates from 30% to around 20%, but only for firms that raise wages by 3% and ramp up domestic investment. And the measure would last only three years. Status quo economic policies that leave Japan's growth moribund should continue, especially if Abe spends his political capital on rewriting Article 9 of Japan's Constitution—which currently forfeits the sovereign right of belligerency—as this remains his government's top priority.

On the monetary policy side, the Bank of Japan has trimmed its asset purchases since August 2016, helping loan growth improve earlier in 2017, but QE remains a headwind. December Japanese loan growth slowed to 2.5% y/y, continuing the deceleration from July's 3.4% peak growth rate.[xix] Japan's flattest-among-G7 nations' yield curve continues hampering lending and holding back economic growth. While Japan's biggest Tech firms likely benefit from the upturn in global growth, domestically focused firms likely face a tougher road.

Overall, Japan's situation has not materially changed, so how sentiment develops is worth monitoring. If sentiment continues falling, mediocre results could easily exceed expectations—setting up potential upside risk. However, sentiment has perked up some in recent weeks, so we will be watching the evolution closely.

xvii Ministry of Economy, Trade and Industry, as of 12/01/2018.

xviii Ministry of Internal Affairs and Communications, as of 12/01/2018.

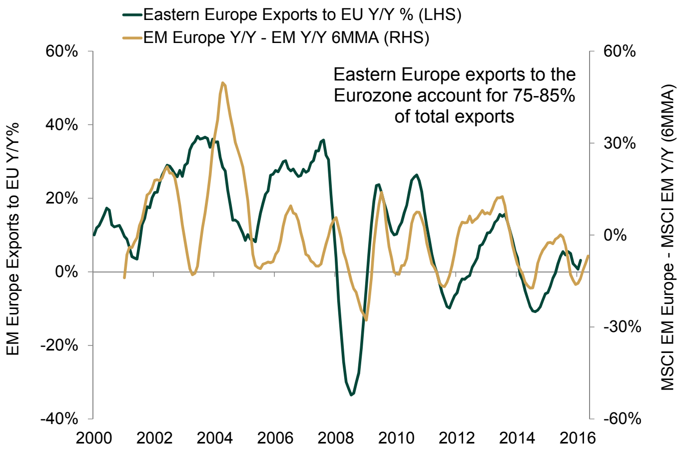
xix Bank of Japan, as of 12/01/2018.

Emerging Markets Commentary

EASTERN EUROPE'S BENEFITS OF PROXIMITY

Emerging Eastern Europe excluding Russia—Poland, Hungary and the Czech Republic—continues to see strong economic growth tied to their proximity to the eurozone's ongoing expansion (Exhibit 17). Throughout 2017, these countries experienced consistently strong growth amid the eurozone's highest GDP growth rate in 10 years.

Exhibit 17: EM Europe is Heavily Linked to Developed Europe Demand Growth



Source: FactSet, as of 09/02/2018.

Politically, the region has seen a rise in nationalism. The Czech Republic just concluded its presidential elections which saw the populist incumbent emerge victorious. Meanwhile, Hungary will hold parliamentary elections later this year, with the populist leaning incumbent party holding a comfortable lead in the polls. In Poland, the populist Law and Justice party (PiS) recently challenged the Judiciary's independence. Poland in particular has been the most combative with the European Commission as the PiS party asserts its domestic agenda despite pushback from Brussels.

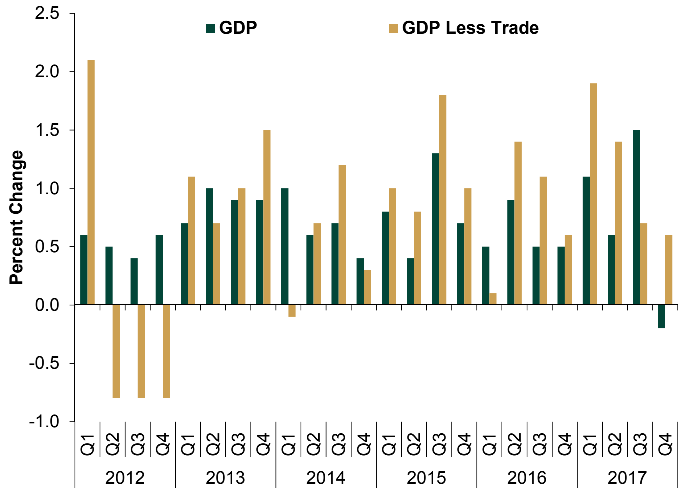
However, unlike developed Europe's upstart populist parties that spooked investors in 2017, these parties have governed for at least several years—a period which has seen increased integration with the EU and the benefits thereof. As such, we expect the strong economic linkages between developed and emerging Europe to prevail over political rhetoric.

SOUTH KOREA: UNDERLYING GROWTH TRENDS INTACT

While tensions with North Korea and what seems like a one-off dip in South Korean GDP drew headlines, data actually reveal the economy's underlying strength. Strong export growth led South Korean GDP to rise 1.5% q/q in Q3, but this reversed last quarter (Exhibit 18). That—plus an irregular 10-day autumn holiday—caused Q4 GDP to contract -0.2%.[xx]

For the year, Korea grew 3.1%, accelerating from 2016's 2.8%. Despite all the saber-rattling from North Korea, South Korea continues benefitting from global Tech demand and its flourishing trade linkages with the rest of Asia and the world.

Exhibit 18: Solid Ex. Trade Growth



Source: The Bank of Korea, as of 25/01/2018.

INDIA: GROWTH REACCELERATES

Economic impacts on India from late 2016's demonetisation and last July's goods and services tax (GST) appear to be waning. Private consumption grew, while government spending growth slowed—expected given the government's stated goal of meeting deficit targets.[xxi]

On a sector basis, growth was uniform. India's largest economic sector—financial and business services—rose 5.7% y/y.[xxii] Meanwhile, trade, hotel, transport & communication services rose 9.9% y/y, utilities 7.6% and manufacturing 7.0%.[xxiii]

xx Source: The Bank of Korea, as of 26/01/2018.

xxi Ibid.

xxii Ibid.

xxiii Ibid.

From industrial production to trade, monthly data suggest growth continued into Q4. October and November industrial production rose 8.4% y/y and 2.0% y/y, respectively. December's manufacturing PMI rose 2.1 points to 54.7, while the services PMI rose 2.4 points to 50.9. Both are above 50, indicating expansion. Although services struggled in 2017's second half, three of the last four months were above 50, suggesting the worst is probably behind.

Forward-looking indicators suggest growth should persist. Loan growth accelerated from 6.9% y/y at Q4's start to 9.8% in the two weeks to 22 December (and 11.1% through 5 January).[xxiv] India's ₹2.1 trillion ($33 billion) state bank recapitalisation in October—its largest ever—seems to have provided a shot in the arm for state lenders saddled with non-performing loans. This, along with the Reserve Bank of India's orders to resolve them, should help clear uncertainty and boost lending.

Money supply is growing[xxv] and finding its way to India's households and businesses, which are spending and investing despite perceived disruptions from major economic reforms. A stronger underlying reality than widely appreciated is a bullish positive for Indian stocks, in our view.

Mexican Election in Focus Midyear

Political uncertainty from Mexico's 1 July general election is running high, weighing on sentiment, but markets should benefit from increased clarity as the results and next president's relative clout become more evident. Three-time leftist candidate Andrés Manuel López Obrador (AMLO, as he is commonly known) currently leads polls, and many fear he will enact anti-market policies—torpedoing NAFTA and repealing landmark energy reform—if he reaches office. However, reality is likely to prove less painful than the rhetoric.

Although current NAFTA negotiators are trying to reach a deal before Mexico's elections, AMLO is vying to delay talks for a seat at the table and a hand at reworking the trade pact. Most see him as anti-free trade and—much like how President Donald Trump campaigned—he promises to get the best deal for the Mexican people. We can't say whether or when NAFTA will be renegotiated—or if AMLO will have a say in its outcome—but politicians have a tendency to moderate on trade once in office. Indeed, Graciela Marquez—AMLO's NAFTA Chief—recently explained they "support the continuation of NAFTA ... It's very important for the well-being of Mexicans."[xxvi] Moreover, AMLO has also walked back his hardline position against energy reform, which has increased foreign investment in—and the competitiveness of—Mexico's oil sector. When presenting his party's—the National Regeneration Movement's (MORENA's)—2018 platform, he promised to uphold existing contracts and only proposed reforms to ensure existing goals are met.

While recent polls have AMLO as the favourite, his victory is not a foregone conclusion and the race is still too early to handicap. Some polls put centre-right National Action Party (PAN) candidate Ricardo Anaya Cortés either ahead or a close second as of December. A January poll suggests AMLO's lead is now around 32% versus Anaya's 26%, and the incumbent Institutional Revolutionary Party's (PRI's) presumptive nominee, Jose Antonio Meade, trailing at 16%.[xxvii] But with 20% undecided, AMLO isn't unassailable. Markets should gain more clarity as elections approach, but for now uncertainty clouds the outlook.

In addition to the presidency, the entire federal Senate and Chamber of Deputies is up for grabs 1 July.[xxviii] Currently, Mexico's entrenched traditional parties, PRI and PAN, hold 92 out of 128 Senate seats. MORENA has none, although its Labour Party (PT) coalition partner has 15. In the 500 seat lower house, PRI and PAN hold a combined 315, while MORENA and its coalition partners have 58. MORENA could boost their representation, but it would take a landmark shift to swing all bodies of government in MORENA—and AMLO's—favour. Absent that, it is likely AMLO would face gridlock if he wins, preventing sweeping reform.

As investors gain more clarity on both NAFTA talks and the election this year, the decline in overall uncertainty should be a tailwind to equities. Fears over both the candidates and NAFTA talks seem to exceed reality by quite a distance, allowing significant room for positive surprise.

xxiv Source: Reserve Bank of India, as of 23/01/2018.

xxv Ibid.

xxvi "Lopez Obrador's Nafta Chief Intends to Keep Mexico in Agreement," Eric Martin, Bloomberg, 01/02/2018. https://www.bloomberg.com/news/articles/2018-02-01/lopez-obrador-s-nafta-chief-intends-to-keep-mexico-in-agreement

xxvii "Mexico Presidency Race Tightens; Leftist Stays out Front: Poll," Staff, Reuters, 29/01/2018. https://www.reuters.com/article/us-mexico-election/mexico-presidency-race-tightens-leftist-stays-out-front-poll-idUSKBN1FI1MQ

xxviii Source: Wilson, as of 05/02/2018. The Mexico Institute's 2018 Elections Guide Electoral Map. https://mexicoelectionsblog.weebly.com/electoral-map.html

China: Growth Steady

The quarter began as China wrapped up its 19th Party Congress, with President Xi Jinping consolidating his hold on power. Many China experts noted Xi seemingly positioned himself to wield power beyond his second term in office—a shift in the post-Mao era, and one with potential long-term political ramifications. However, Xi's consolidation of power should not radically alter the status quo for the foreseeable future—the timeframe markets care about most. While promising more free-market reform, the government's primary focus continues to be social stability above all else. Therefore big, radical changes are unlikely.

After the Congress, China's government announced it would remove foreign ownership caps on Chinese banks and financial asset management companies. Before, foreign companies couldn't own more than 20% of a Chinese financial institution (and foreign ownership of total holdings couldn't exceed 25%). Granted, the government isn't completely relinquishing control: Any foreign entity seeking more than a 5% stake in a bank will require the China Banking Regulatory Commission's approval. However, beyond some potential positive developments (e.g., Chinese banks improving their capital allocation), the more immediate impact may be on sentiment. Many experts worried President Xi Jinping would increase the government's influence in specific sectors following the Party Congress. While developments could always change, this move runs counter to those expectations.

Chinese economic data remained steady at year-end and once again proved hard-landing fears hollow. Q4 GDP rose 6.8% y/y, matching Q3's pace and bringing full-year growth to 6.9%—accelerating from 2016's 6.7%.[xxix] This was its first annual acceleration in seven years and above the government's 6.5% growth target.

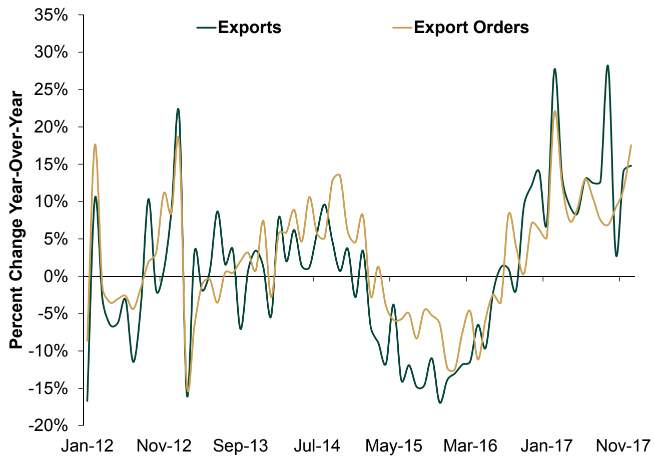
Although monthly data released during Q4 were somewhat mixed, the overall picture remains generally solid. December's official purchasing managers' indexes (PMIs)—which include large, state-owned enterprises—stayed above 50, indicating more surveyed firms expanded than contracted.[xxx] PMIs indicate only growth's breadth—not its magnitude—but China's stats remain consistent with their longer-term trend of slower but steady expansion, far from the common expectation of an economic hard landing.

Taiwan: Trade Powers Growth

Trade also continues fueling Taiwanese GDP, which grew 1.0% q/q (3.3% y/y) in Q4.[xxxi] As in Q3, the primary positive contributors were private consumption, which rose 2.9% y/y, and exports, up 6.0% y/y (Exhibit 19).[xxxii] Meanwhile, gross fixed capital formation fell for the second consecutive quarter, slipping -4.8% y/y.[xxxiii] While a more detailed breakdown isn't available to show whether the decline spanned the public and private sectors, commentary from Taiwan's statistics bureau pinned it on a drop in machinery and equipment investment. As always, it is too soon to know whether the double dip is a hiccup or the start of a deeper investment pullback, particularly without a seasonally adjusted quarterly breakdown of GDP's components.

While Taiwan experiences positive growth, its market is heavily weighted toward commoditised Technology firms and less leveraged to mobile and cloud computing, which we currently favour.

Exhibit 19: Strong Export and Export Orders Growth



Source: Ministry of Economic Affairs, Republic of China (Taiwan), as of 26/01/2018.

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xxix Source: National Bureau of Statistics of China, as of 19/01/2018.

xxx Ibid.

xxxi Source: Directorate General of Budget, Accounting and Statistics, as of 01/02/2018.

xxxii Ibid.

xxxiii Ibid.

GREECE: A BULLISH SIGNAL FOR EMERGING EUROPE

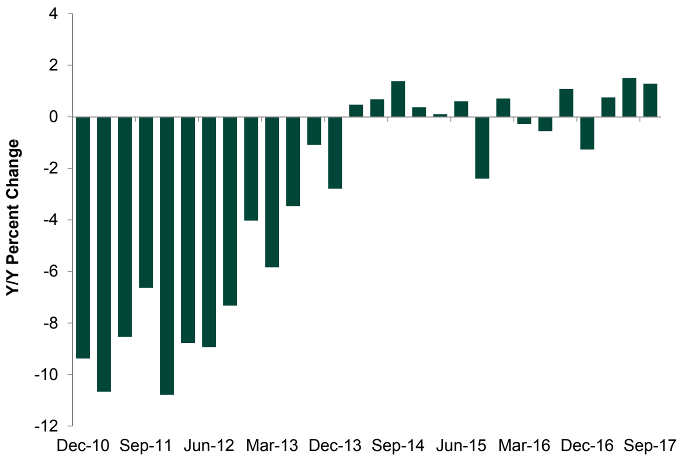
Positive developments in Greece, one of the world's most troubled economies in recent years, show the breadth of the present expansion. Investors now appreciating these developments more also shows improved sentiment, which bodes well for Emerging Europe beyond Greek borders.

For the vast majority of this bull market, the Greek economy has been troubled. In late 2009, Greece unveiled deficits far in excess of prior reports, the first step in a debt crisis that led to three bailouts, two defaults and a catastrophic recession. Between 2010 and 2016, a period of continuous global GDP growth, Greek annual GDP shrank a massive 23%.[xxxiv] Negotiations over bailouts and associated austerity measures between Greek and EU officials have often been fraught, leading many to fear a "Grexit"—the Hellenic Republic crashing out of the eurozone. However, Greece's situation started to improve last year: The economy is growing, politics have stabilised and foreign capital is returning. Athens now appears on track with its bailout requirements. While these improvements are nascent, Greece's progress symbolises how far the eurozone has come since its crisis—and how sentiment toward Europe broadly has evolved.

Last July, Greece returned to the international bond market for the first time since 2013—a major sign of improvement. This comes only two years after the country was in near-total disarray. Firebrand Alexis Tsipras and his far-left upstart Syriza party stormed into Parliament in 2015, ignored prior reform commitments and nearly took Greece out of the eurozone by calling a referendum on the third bailout. Though the bailout ultimately went through, there was plenty of drama: Greek leaders adopted capital controls, voters rejected the aid package due to its tough conditions, and Prime Minister Tsipras ended up making major concessions to reach a deal.

Since that turbulent time, Greece's situation has brightened. For one, the economy seems to be recovering, as GDP has grown in four of the past five quarters. (Exhibit 20)

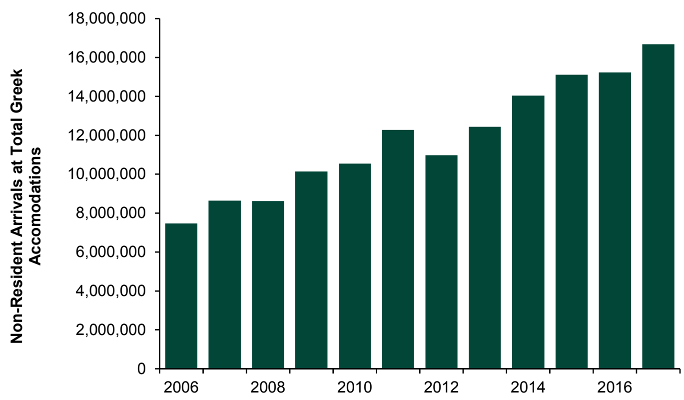
Exhibit 20: Greece's GDP Shows Steady Improvement



Source: FactSet, as of 18/01/2018. Greek GDP, year-over-year percent change, from 31/12/2010 – 30/09/2017.

Industrial production has risen 14 straight months through November 2017.[xxxv] The manufacturing subsector has been growing, too, and IHS Markit's Greece Manufacturing December PMI showed new orders enjoyed their sharpest rise in more than nine-and-a-half years—a positive sign for growth in early 2018.[xxxvi] Tourism, an important driver of the Greek economy, picked up in 2017, too. The Accommodation and Food Service Activities Sector, which covers groups like hotels and holiday and short-stay accommodation, rose 13.9% y/y in Q3 2017—accelerating from Q2's 7.2% and massively improving from Q1's 0.9%.[xxxvii] Exhibit 21 compares total non-resident arrivals at Greek accommodations through each year's first 10 months.

Exhibit 21: Non-Resident Arrivals at Greek Accommodations



Source: Eurostat, as of 26/01/2018. Cumulative visitors through October of each year, 2006 – 2017.

xxxiv Source: FactSet, as of 26/01/2018. Greek annual GDP, 2010 – 2016.

xxxv Ibid.

xxxvi IHS Markit, as of 26/01/2018.

xxxvii Source: Hellenic Statistical Authority, as of 28/01/2018.

Furthermore, chronically high Greek unemployment has been trending downward, with the unemployment rate down from 21.1% in Q2 2017 to 20.2% in Q3 2017.[xxxviii] Though backward-looking, steady jobs improvement confirms the ongoing economic recovery.

In the political realm, Tsipras has held onto power—an unlikely source of stability who has pushed through some needed reforms. Investors have taken notice. Last November, the Treasury held a successful €30 billion voluntary debt swap—an exchange of higher yielding bonds (e.g., ~20%) for lower yielding bonds (e.g., 3.5 – 4.2%). This cheaper financing relieves some immediate pressure on Greece, and it indicates investors are much more confident about Greece's creditworthiness. 10-year Greek yields have been falling overall since Greek markets reopened in August 2015 following a five-week closure due to bailout talks (Exhibit 22).

Exhibit 22: Greek 10-Year Yields Since 2015 Political Turmoil

Source: FactSet, as of 18/01/2018. Greek 10-Year Yield, 03/08/2015 – 11/01/2018.

Another example of Greece's overall progress: an increase in privatisations. One of creditors' primary bailout conditions was for Greece to privatise state-owned property and assets. From 2011 – 2015, the Hellenic Republic Asset Development Fund (HRADF) privatised only about €3.5 billion worth of assets. But in 2016 and 2017, the Hellenic Corporation of Assets and Participations (HCAP, HRADF's successor) started making big deals, selling off stakes in major ports and leasing out regional airports. In 2017 alone, Greece privatised about €2 billion worth of assets. HCAP has set its sights higher in 2018, seeking to raise at least €3.5 billion. The more the Greek economy recovers, the better price HCAP can fetch for valuable assets.

Bailing From the Bailout

In January, eurozone creditors tentatively signed off on Greece's latest spate of reforms, which included some controversial labour changes—like making it more difficult for workers to strike. Greece is now set to receive its next bailout tranche in February. Barring any unforeseen changes, the country also looks poised to exit its bailout programme in August. Currently, creditors are debating the appropriate way to monitor Greece once their direct oversight ends. There are also questions of whether Greece will have enough cash on hand to service its debt and what debt relief (if provided) could look like. However, those longer-term issues aren't causing investors angst like they used to—a sign of sentiment's progress.

While Greece's general prospects look brighter, this doesn't mean it is time to overweight Greek stocks. Though Greek price-to-earnings (P/E) ratios are low relative to other stocks, valuations aren't predictive. If they were, Greek stocks should be outperforming massively since 2011. Yet consider: From 2011 to today, Greek stocks are down -82.6%, while Emerging Markets returned 30.1%.[xxxix] Moreover, Greek markets skew toward Financials, which still face problems like heavy government involvement and record levels of bad loans. So even though Greece is slowly emerging from the abyss, better investment opportunities likely exist in other Emerging Markets.

xxxviii Ibid.

xxxix Source: FactSet, as of 26/01/2018. MSCI Greece with net dividends in US dollars and MSCI Emerging Markets Index with net dividends in US dollars, 31/12/2010 – 25/01/2018.

South Africa

President Jacob Zuma remains in the spotlight as investors keep a lookout for his removal from office well before his term ends in 2019. He has lost significant clout within the African National Congress (ANC). Rumors swirl of Zuma's impending departure, and ANC leadership agreed he should step down ahead of 8 February's State of the Nation Address, but Zuma remains quiet on his plans. His struggles have weighed on South African stocks' relative returns for over 18 months. He has survived numerous calls for his resignation, including seven no-confidence motions, making it far from guaranteed that the next motion, scheduled for 22 February, will bring the end of his presidency.

Yet many believe the mood is different now, making his early removal more likely. Ramaphosa won the ANC leadership contest by running on an anti-corruption platform, and he has already begun taking steps to shore up party support ahead of 2019's elections. His anti-corruption drive has already shaken up the board and management of Eskom, the state-power utility, as he removed any executives currently facing allegations of serious corruption. Ramaphosa's supporters see removing Zuma as critical to attracting voters in 2019. That could inspire more ANC lawmakers to side with the opposition Economic Freedom Fighters, which called the no-confidence motion. That said, Zuma's ability to overcome long political odds is remarkable, and he still has plenty of staunch supporters within the ANC.

Many worry about violence and unrest if he is removed early, as some factions supporting him have warned this could lead to civil war, raising the spectre of Kenyan violence in 2007. Yet to us, this seems premature. South Africa has relatively strong political institutions, and Zuma is nowhere near as popular with voters as Raila Odinga was in Kenya a decade ago (and remains today). His approval rating hit an all-time-low 18% in September 2017. While threatening violence might work as a negotiating tactic, ultimately, there is no reason a carefully managed transition should incite bloodshed.

Ultimately, a resolution to this saga could boost sentiment toward South African stocks, particularly if Ramaphosa makes continued progress on addressing corruption. It is possible South African stocks could greet Zuma's removal much as Brazilian stocks cheered the impeachment and removal of Dilma Rousseff and South Korean stocks welcomed the early departure of Park Geun-hye. However, we think acting on these hopes is premature at this point, given Zuma's apparent resistance to removal. If and when he is removed, there should be sufficient time to assess all of South Africa's drivers—economic and sentiment as well as political—as well as the influence of global commodity prices, which remain key to South Africa's economic fortunes.

PORTFOLIO PROFILE

SUMMARY OF PORTFOLIO THEMES & POSITIONING

Sector Positioning

Overweight Information Technology

The Information Technology sector is heavily skewed toward large, high-quality firms—a segment we expect to outperform in the later stages of a bull market. The sector should also benefit from robust global IT spending driven by the growing demand for products and services related to mobile, cloud computing and the "Internet of Things".

Economic Drivers

+ **Strong Corporate Fundamentals & Consumer Spending:** Strong corporate profitability, low financing costs, tight labor markets, and low inflation should support increased expenditures on productivity enhancing and consumer facing technology. 2017 global IT services and enterprise software spending is expected to grow in excess of global GDP, driven primarily by trends in cloud computing. Rising consumption of online products, particularly in emerging markets with developing middle classes, should also support consumer oriented technology.
+ **The Internet of Things (IoT):** The burgeoning trend toward adding communication capabilities to a large swath of previously unconnected consumer electronics and industrial devices should drive a wave of activity and broadly benefit the Technology sector beyond component makers.
± **Cloud Computing Productivity Gains:** Cloud computing can potentially reduce cost burdens for businesses of all sizes, increasing technology capacity utilisation, reducing IT staffing needs and increasing workforce productivity. Cloud investments should benefit enterprise software and select hardware providers, while detracting from legacy and "non-cloud" providers.
± **Mobile Technology:** While the trend in mobile adoption continues to mature, changing consumer and enterprise habits still provide select investment opportunities such as areas of high value componentry and mobile advertising/commerce.
- **Traditional Computing Stagnating:** As a long-term trend, high computer penetration and the shift toward mobile computing are eroding demand for traditional devices such as personal computers and, increasingly, tablets.

Political Drivers

± **Privacy Laws:** The European Court of Justice decision to invalidate the "Safe Harbor" EU-US data transfer agreement may increase compliance costs for multinational tech firms, but data center suppliers could benefit.
± **Security Spending:** Security backdoor concerns may direct governments to increase spending toward domestic suppliers at the expense of multinational tech firms.
± **Tax Policy:** European governments may increasingly challenge multinational tax avoidance schemes. US tax policy (e.g. repatriation holiday) may provide a modest boost to buybacks, but is unlikely to impact investment as Tech firms are not in need of cheap funding sources given low debt and high retained earnings.
- **Anti-Trust:** Governments around the world may increasingly use anti-trust laws to reduce intellectual property royalties as recently seen in Asia.

Sentiment Drivers

+ **High Margin, "Growth" Characteristics:** Technology shares tend to be higher margin and growth oriented; both characteristics we favour in the period ahead. As the market matures, investors should increasingly prefer Technology companies with stable and higher margins.
+ **Tech Outperforms in Positive Markets:** As an economically cyclical sector, global Technology tends to outperform when markets are either strongly or moderately rising.
+ **Mega-Cap Equities:** The Technology sector contains some of the world's largest companies by market capitalisation. As the equity bull market matures, investors are likely to favour high quality companies with stable balance sheets and geographically-diverse revenue streams.
- **High Expectations in Some Industries:** Sector valuations are slightly elevated versus recent history, but within historical norms, particularly for the later stages of a bull market. However, expectations of certain high-growth areas within Technology such as the Internet-of-Things and virtualisation are quite ambitious, setting the bar high, not to be easily exceeded.

Overweight Health Care

Health Care should benefit from increasing investor preferences for larger, higher quality companies with long term growth prospects. Within the sector, larger Pharmaceutical firms are offsetting key patent expirations through pipeline development, M&A, licensing and rapid Emerging Markets growth.

Economic Drivers

+ **Emerging Markets Health Care Demand:** Huge swaths of Emerging Markets populations are breaching key income thresholds, allowing for the purchase of pharmaceuticals and medical devices for the first time.
+ **Balance Sheet Strength:** Financial flexibility of large Pharmaceuticals firms allows for increased research and development, share buybacks, dividends and strategic acquisitions.
+ **Favourable Developed World Demographics:** Aging and longer-living developed world populations should increase total health care expenditures.
+ **Robust Pipelines:** A rapid decline in patent expirations and positive pipeline development are broadly underappreciated. Novel drug approvals by the FDA are accelerating after a slowdown in 2016, and 2017 is on pace for the most approvals since at least 1996.

± **Biosimilar Competition:** The FDA's approval of generic biotechnology drugs will introduce new competition. Yet, minimal discounting, manufacturing challenges and regulatory hurdles will likely limit the severity of competition relative to generic pharmaceuticals.

- **Regional Austerity:** Budget-conscious governments in the developed world are attempting to slow the growth rate of health care spending.
- **Biotech Patent Expirations:** Many large-cap biotech companies will be facing patent expirations within the next couple of years. This could reduce sales and profits for these companies if new innovative drugs in the pipeline don't come to fruition and offset lost sales from drugs with expiring patents.

Political Drivers

± **Drug and Device Approval:** Pipelines and new product approvals are improving as regulatory environment is becoming more favourable. This trend is largely positive for branded biopharma, and likely a headwind for generic drug makers as it creates more competition.

± **Legislative Uncertainty:** Campaign rhetoric targeting high priced drugs weighed on sentiment since Hillary Clinton's late 2015 tweet on lowering drug prices, yet intra-party gridlock likely avoids austere drug pricing reform.

± **ACA Winners and Losers:** The Health Care sector is largely comprised of innovative industries (Pharmaceuticals, Biotechnology and Medical Devices) able to navigate minor taxes and fees imposed in legislation. Material short-term impacts were narrow and mainly confined to Managed Care (negative: guaranteed issuance and capped profit margins) and hospitals (positive: reduced bad debt exposure from uninsured).

Sentiment Drivers

+ **Preference for Growth:** We expect Health Care to benefit from investors' preference shifting to larger companies with higher quality growth opportunities. Additionally, large pharmaceutical firms possess many mega-cap characteristics that we believe investors favour in the latter stages of a bull market, such as higher profit margins, diversified revenues, strong cash flows, healthy balance sheets and brand recognition.
+ **Valuations:** Valuations are trading at slim premiums to the broad market, suggesting today's positive fundamentals are only modestly appreciated.

Neutral Industrials

Industrial categories most reliant on resources pricing for profits face headwinds, but other categories should benefit from global economic acceleration and improving credit availability.

Economic Drivers

+ **Automation Equipment:** Lack of qualified labor and rising wages in Emerging Markets along with improving productivity in Developed Markets are contributing to increased demand for factory automation equipment.

± **Global Credit Availability:** Industrial customers' access to credit continues to improve in Europe, but has begun to modestly tighten in the US as the yield spread narrows, which typically decreases banks' willingness to lend. Chinese credit growth has modestly decreased after accelerating in 2016.

\- **Weak Resource Pricing:** Low resource prices are a significant headwind for future extraction equipment demand—a significant portion of the sector.

\- **Slowing Order Rates:** As the economic cycle matures, orders likely shift from short (quickly-filled orders) to long cycle (multi-year products), order rates likely slow, impacting revenues.

Political Drivers

+ **Chinese Minimum Wage Growth:** The Chinese government achieved their target of an annual 13% minimum wage increase over the last 5 years. Strong wage growth should support the need for labor-saving machinery, and make manufacturing labor costs elsewhere more competitive.

\- **Trade Policy:** Much of the sector directly benefits from increasing global trade. While we expect global trade to remain relatively healthy, the Brexit and Donald Trump's election does create some uncertainty moving forward.

Sentiment Drivers

\- **Size Preference Shift:** As bull markets mature, investors tend to seek firms with high earnings stability, brand recognition, pricing power and better credit access. Such firms tend to have larger-than-average market capitalisations—a headwind for Industrials as the sector has relatively few very large firms.

Neutral Consumer Discretionary

The Consumer Discretionary sector may see increasing headwinds from tighter monetary policy and rising wage costs.

Economic Drivers

\+ **Weak Commodity Fundamentals:** A decade of strong commodity capital expenditures coupled with China's shift toward consumption and away from investment-led growth is a headwind to commodity sectors and a tailwind to consumer equities.

± **US Housing Recovery:** US home prices should benefit from relatively tight supply, but tighter monetary policy may moderately weigh on demand growth.

± **Inflation Risk:** Inflation has a higher probability of developing the more a bull market advances, and inflation typically has a negative impact on Discretionary relative returns. However, we believe expectations of tighter US labor markets driving inflation are overblown due to the influence of foreign economies on US inflation and tighter Fed policy.

± **Favour Online Consumption:** Online retail sales, which have consistently grown 10 to 20 percentage points faster than brick-and-mortar sales, are likely to continue taking brick-and-mortar market share.

± **Emerging Markets Differentiation:** We expect Emerging Markets consumption to grow faster in countries undergoing structural reforms and with less dependence on commodity exports. China should continue to be a major driver of this tied to its ongoing shift away from an investment focused economic model and towards consumption.

\- **Yield Curve:** Flatter yield curves have historically been a forward-looking indicator of Discretionary underperformance. The 10Y-3M US Treasury yield spread is below the long-term average.

\- **Monetary Policy:** Tighter monetary policy from the Federal Reserve may moderately weigh on future demand growth, particularly for consumer goods more dependent upon financing (e.g., autos).

\- **Tight US Labor Markets:** As the US economic cycle advances, labor markets are likely to continue tightening, leading to rising late-cycle wage costs. Discretionary firms are often more vulnerable to rising wage costs due to high labor intensity and heavy competition that limits firms from passing along rising costs to customers.

Political Drivers

\+ **China Consumption Shift:** China's political strategy of reducing investment-led in favour of consumption-led growth should be a tailwind for Chinese consumption equities relative to equities exposed to Chinese investment.

\+ **US Tax Reform:** Several Discretionary industries, such as Retailing, have high effective corporate tax rates. Consequently, cuts to corporate tax rates should relatively benefit those industries.

Sentiment Drivers

\- **US Tax Reform Expectations:** While some industries, such as Retail, with high effective corporate tax rates should marginally benefit from corporate tax cuts, we believe this benefit is getting too much investor attention. Other factors such as tighter consumer credit and rising wage costs are more likely to provide surprise power moving forward.

Neutral Telecommunication Services

Telecom faces a number of obstacles in the US during the late stages of this bull market, including its historic defensiveness, high levels of competition, and rising network maintenance costs. At the same time, many foreign telecom providers are better positioned due to larger Information Technology divisions and greater exposure to fast growing emerging market consumers.

Economic Drivers

+ **Cloud Computing Growth Trends:** Telecom firms benefit as enterprises increasingly utilise cloud-based services bolstering data transmission demands across networks.

± **Rising Emerging Markets Middle Class:** Lower penetration rates of wireless service and wire-line Internet in Emerging Markets provide growth opportunities for local service providers as well as many developed market carriers. However, Emerging Markets subscribers generally have lower margins. Further, high competition limits potential average revenue-per-user growth.

± **Mobile Data Usage Rising Globally:** Increasing demand for wireless data services is a positive revenue driver for firms globally. However, companies' ability to convert higher revenues into increased profits is limited by increased smartphone subsidies and high infrastructure investments required to cope with rising data demand.

\- **Developed Wireless Markets Saturated:** Most of developed Europe, the US and developed Asia have mature markets with penetration rates near or above 100%, limiting subscriber growth.

\- **Price Competition Intensifying:** Pricing competition remains high and is increasing as penetration rates among premium (smartphone) users increase and a lack of product differentiation among incumbents increasingly forces them to compete on price.

Political Drivers

± **State-Sponsored Oligopolies:** Many companies enjoy state-sponsored oligopoly status as large domestic telecommunications networks are deemed critical to national security. Such designation can be a fickle benefit as such companies are at the whims of governments and regulators who may ultimately look to break up such oligopolies.

± **Heavy Regulation and Political Influence:** Recent proposals by the European Parliament to enshrine Net Neutrality into law — plus uncertainty surrounding the FCC's direction under the Trump administration in the United States — add uncertainty to the sector's prospects.

Sentiment Drivers

+ **Falling Long Rates Help Telecom:** Telecom shares should benefit as long bond yields fall in 2017. Telecommunication Services equities are a type of bond substitute and a strong inverse relationship between Telecom share relative performance and yields exists.

\- **Traditionally Defensive Sector:** Telecom is historically a defensive sector and more likely to underperform during bull markets and outperform during bear markets due to investor perception of Telecom as a sector with stable cash flows.

Underweight Consumer Staples

While the Consumer Staples sector has above-average gross margins and quality earnings growth—features we prefer late in bull markets—the sector's defensive characteristics may present a performance headwind amid growth in global economic activity.

Economic Drivers

+ **Quality:** Firms with more stable, high-quality earnings growth, such as Consumer Staples, tend to outperform later in bull markets.
± **Gross Margins:** Firms with large gross margins tend to outperform later in bull markets. On average, Consumer Staples firms have similar gross margins to market peers.
± **Market Capitalisation:** We favour firms with large market capitalisation in the back half of bull markets, but the Consumer Staples weighted average market cap is near the market average.
± **Yield Curve:** Historically, the more the yield curve flattens, the better the forward relative returns of the more defensive Staples sector. The 10Y-3M US Treasury yield spread is currently slightly below the long-term average.
± **Monetary Tightening:** Within bull markets, Staples relative returns have historically been neutral versus the market once Fed tightening begins.
± **Emerging Markets Differentiation:** We expect Emerging Markets consumption to grow fastest in regions with less commodity dependence and have structural reforms.
- **Global Growth:** We expect global growth to outperform low expectations – a headwind to the traditionally defensive Consumer Staples sector.
- **E-Commerce:** The growth of e-commerce retailing, which is more concentrated in the Consumer Discretionary sector, is likely to continue taking market share from brick-and-mortar Food & Staples Retailing.

Political Drivers

± **FDA Tobacco Regulations:** Potential new rules from the FDA may potentially mandate lower nicotine levels in US cigarettes, which might negatively impact the number of future smokers. However, lower addiction levels could initially be offset by higher volumes, which were previously observed with the introduction of light cigarettes. Further, the FDA has expressed interest in promoting Modified Risk Tobacco Products, which generally have higher profit margins.
- **Chinese Political Reform:** Chinese political reforms discouraging conspicuous consumption are likely to remain a headwind for the Beverages industry.
- **Non-US Tobacco Regulations:** Several Emerging Markets governments such as Korea, India and Indonesia have recently increased tobacco regulations including smoking bans in public places, tax hikes and mandated graphic warnings on packaging. In the European Union, plain packaging regulations were recently passed along with a ban on menthol cigarettes with a 2020 implementation date.
- **Sugar Taxes:** While in its infancy, a movement to tax sugary beverages is developing with new taxes in the UK, Mexico, Saudi Arabia, San Francisco and Philadelphia.

Sentiment Drivers

± **Valuations:** We find limited evidence of strong or weak sentiment toward Consumer Staples. Valuations are generally aligned with comparable categories across the market.

Underweight Materials

Metals prices—key drivers of sector returns—lack strong fundamental support as infrastructure-led growth and metal demand from Emerging Markets is slowing while supply growth continues.

Economic Drivers

± **Increased Infrastructure Spending in the US:** President Trump's plan for increase spending on decaying US infrastructure increased optimism towards commodities but faces an uphill battle for Congressional approval.

± **Metals Supply Growth:** Global supplies of copper and iron ore, among other commodities, continue to increase due to capital expenditures committed several years ago. However, declines in capital expenditures—in response to lower prices—have slowed expected supply growth rates over the next couple of years.

- **Chemical Supply Growth:** Increased production of natural gas has resulted in a dramatic increase in ethylene supply in recent years that is expected to continue through 2020. Historically, when ethylene supply growth accelerated Chemicals underperformed the broader market.
- **Industry Cyclicality:** Commodity outperformance cycles tend to be followed by underperformance cycles of similar magnitude, in part due to the industry's supply response to changing commodity prices. Lag times for developing a new mine or chemical processing plant can take three to five years (and often longer) and cost billions of dollars, creating a dynamic where supply and demand can grow at different rates for long periods of time, increasing cyclicality.
- **Cooling Property Market in China:** After strong growth in China's property markets in 2016 the government has taken steps to slow housing inflation in many major cities. Historically China's residential market is a major source of demand for steel and copper.
- **Slowing Chinese Credit Growth:** Planned total social financing in China continues to decelerate. Following a strong stimulus in 2016, the government moderately lowered annual credit and money supply growth targets in 2017 as it attempts to reign in stimulus spending. However, the deceleration remains modest as the government ensures economic stability surrounding the large government power transition in Q4.

Political Drivers

± **Resource Nationalism Raises Production Costs and Limits Supply:** Government intervention in mining and materials companies can lead to increased taxes, decreased exports or even outright expropriation of resources. This creates regulatory risk for materials companies—for example, politicians in Australia recently proposed additional profit taxes on mining companies.

- **Tariffs Distort Market:** The US government is expected to renegotiate important trade agreements, likely creating winners and losers in the Materials sector. Recent examples include proposed steel tariffs and recently enacted lumber duties.

Sentiment Drivers

± **Valuations:** Relative Price-to-Earnings valuations increased rapidly over the past year to levels that typically precede sector underperformance, but have since fallen to less worrisome levels.

- **Rapidly Increasing Sentiment for Metals:** Mining companies are reinstating or increasing dividends less than a year after many of the same companies were forced to raise capital and halt or reduce dividend payments. Similarly, market expectations for the sector are increasing quickly, evident by a number of company's shifting to overweight recommendations on the industry.

UNDERWEIGHT UTILITIES

Traditionally defensive Utilities should underperform given our forecast for an ongoing bull market, weak power price fundamentals and the sector's thin gross profit margins.

Economic Drivers

± **Interest Rates:** We believe interest rates are likely to remain lower in 2017 than they started the year. Intra-party GOP divisions are likely to limit extreme policy, US Fed monetary tightening and a lower annual money supply growth target from China should help limit global money supply growth, and foreign economies are likely to continue influencing US rates and inflation. The net effect should be a mild positive for the yield-sensitive Utilities sector.

± **Structural Growth:** Strong efficiency gains limit structural growth potential in developed markets. Conversely, inadequate infrastructure makes Utilities a growth industry within Emerging Markets.

\- **Thin Gross Profit Margins:** Late stage bull markets typically favour firms with large gross profit margins as they afford firms greater flexibility and often result in more reliable and stable future earnings. The Utilities sector historically has thin profit margins, which should result in underperformance relative to other sectors.

\- **Power Prices:** Gas-fired power plants usually provide peak load power, so power prices are heavily influenced by natural gas prices. Since the shale boom is boosting US natural gas supplies, prices should remain low, limiting the relative performance of US independent power producers. Gas prices are higher outside the US, but we believe risk is to the downside due to high levels of international gas investment.

Political Drivers

\+ **Japanese Regulations:** While public support remains mixed, Japanese regulators have begun bringing some nuclear capacity back online. The pace of the restarts is likely gradual and eased by lower prices of imported fossil fuels.

± **US Regulations:** Environmental Protection Agency coal regulations create winners and losers, as do the costs of coal to natural gas conversions and closures of coal-fired plants. As signaled by the US' withdrawal from the Paris Climate Accord, President Donald Trump may try reversing some of the climate control regulations in President Obama's Clean Power Plan, favour fossil fuel production and potentially end renewable energy subsidies. Regulated utilities are best positioned to pass any regulated costs along to customers.

\- **German and French Regulations:** Following Japan's nuclear disaster, German and French regulators have targeted decreases in nuclear production and increased focus on renewable energy sources, which lowers overall utilisation by requiring high-cost, flexible reserves to be maintained for periods when renewable power is unavailable.

Sentiment Drivers

± **Valuations:** Most relative valuation metrics are in line with historical norms, indicating neutral sentiment toward Utilities.

\- **Defensive:** Utilities typically perform best during down-markets and recessions - their dividends and regulated profits are often used as a defensive asset and fixed income proxy.

UNDERWEIGHT ENERGY

Years of global oilfield investment continue to result in a well-supplied market, decreasing the odds of long-lasting oil price strength. Consequently, profit growth in the Energy sector will likely lag the broad market.

Economic Drivers

± **Low US Oil Rig Count:** The oil price plunge forced US oil companies to reduce drilling in high-cost regions. While this should marginally support prices, many investors argue (we believe falsely) this will cause oil prices to rise swiftly again. However, past oil booms also witnessed falling rig counts, yet oil prices remained low afterward for some time. Additionally, as oil prices have stabilised, rigs have been put back into operation, supporting US output.

± **Low US Energy Capital Expenditures:** The same argument is often made in terms of capex, which fell for two consecutive years but is now expected to grow. While a prolonged period of underinvestment could create a supply-constrained market, history suggests falling capex does not change supply dynamics quickly, as years of investment and efficiency gains keep production high.

± **OPEC Production:** Despite an agreement to limit production, falling output is unlikely to lead to any supply constraints. By agreeing to limit output to 32.5 Mbpd, the cartel is effectively asking members to cut only modestly, and thus far cuts have had minimal impact on excess inventories. These modest cuts, together with the speed with which US shale producers can increase supply, suggests markets will remain well-supplied.

- **US Oil Investment and Innovation:** A decade of intense oil industry investment and new innovation has dramatically enhanced oil companies' ability to extract previously unreachable oil. We expect oil prices to remain low, reflecting the oil industry's enhanced ability to meet global demand growth, and to do so with greater speed than in the past.
- **Low Energy Intensity of Developed Markets (DM) Growth:** Relative to Emerging Markets (EM) peers, Developed Markets countries use less energy per unit of GDP growth. We expect oil demand growth to lag strong aggregate global economic growth as Domestic Markets GDP accelerates, while EM growth decelerates.

Political Drivers

± **Geopolitical Supply Disruptions:** The global oil market remains exposed to supply shock risks in Russia, the Middle East and North Africa. A significant increase in social unrest or outright conflict has potential to cause oil price spikes. However, these risks are common, difficult to time and often short-term. Additionally, geopolitics is a two-way street – it is possible tensions subside, resulting in more secure energy supplies.

- **Chinese Rebalancing:** China's policy of promoting consumption versus investment growth should reduce the energy intensity of Chinese GDP growth.
- **EM Fuel Subsidy Cuts:** In an effort to improve competitiveness, several EM countries have cut fuel subsidies. While we believe these cuts are sound policy that strengthen public finances and promote aggregate growth in the long term, they incrementally reduce short-term oil demand growth.

Sentiment Drivers

- **False Perceptions on Oil Cycles:** We believe misperceptions on oil price drivers and anchoring biases cause many investors to underestimate the length of time prices may remain weak. As prices fall, marginal production costs also fall, as operators in high-cost areas slow drilling. These cuts lead to idle equipment and redundant workers, driving costs lower elsewhere and likely keeping prices weak longer than many believe, despite years of $100+ oil recently.
- **Over-Optimism on OPEC Deal:** One recent driver of oil prices has been optimism surrounding OPEC's agreement to limit production. While this has benefited prices in the near term, we believe this optimism is misplaced, and ignores the reality that OPEC does not control oil prices, particularly in light of the ease with which US producers can increase output compared to previous cycles.

Underweight Real Estate

Bond-like yield attributes and an inverse relationship to interest rates have encouraged substantial inflows throughout this cycle and elevated valuations as interest rates fell and investors stretched for yield. However, a heavy US and small cap bias, high debt load and more defensive characteristics position the Real Estate sector as a poor thematic fit in the final stages of a market cycle.

Economic Drivers

\+ **Positive New Construction Activity:** An array of new US construction is occurring from office to industrial to apartments, positive for future growth.

\+ **Healthy Labor Markets:** Ongoing job and wage growth contribute the largest source of new real estate demand, positive for future demand growth.

\+ **Highly Fragmented Sector:** REITs comprise a majority of the sector and most industries are highly fragmented, positioning the sector as a likely beneficiary of future consolidation through M&A activity.

± **High Dividend Yielding Sector:** REITs are commonly used as a bond replacement particularly in the current low yield environment, as its dividend payout yield is commonly above the bond market, encouraging investors to stretch for yield into REITs. As such, REITs are inversely correlated to interest rates. This should benefit the sector in 2017 as long rates modestly decline as inflation expectations are reduced by a more aggressive rate hike cycle.

± **Quasi-Defensive Sector:** REITs typically outperform in flat to down markets and underperform during strong equity markets. However, there is a major exception: in large bear markets, REITs often do poorly given their low capital buffers and high debt levels as bankruptcy risk can be high.

\- **Small Cap Bias & No Mega Caps:** The Real Estate sector and REITs in particular are overwhelmingly small cap oriented, focusing on niche offerings of types of real estate and regions. Large cap equities typically outperform in the later stage of bulls.

\- **A Small Capital Safety Net:** Given its required payout structure, high leverage and low retained earnings, REITs tend to have a much smaller loss buffer than many other sectors in times of financial stress, increasing the bankruptcy risk during recessions. These attributes make the Real Estate sector lower quality relative to other sectors, and poorly positioned in the later stages of the market cycle, when quality tends to outperform.

\- **Dilutive Equity Raises Are Common:** Given its required payout structure, REITs have a difficult time funding expansion with retained earnings. The most common path for growth is via diluted equity raises. Typically dilutive equity raises are most problematic for existing shareholders during the final stages of the bull, and especially during a bear market.

Political Drivers

± **Favourable Tax Treatment:** REITs provide a more friendly tax treatment as a separate vehicle specifically designed to hold real estate assets, compared to an asset on a typical corporate balance sheet. This has increasingly encouraged some traditionally real estate heavy industries to sell their real estate into a REIT and lease it back. This has been most common for Retail and Hotels, and could spread to other industries, increasing the supply of REITs.

± **Required Earnings Payout Structure:** REITs were established as a way for average investors to access diversified real estate. REITs must payout at least 90% of all earnings via dividend—meant to mimic real estate cash flows. The downside is, this structure leads to a limited capital base, and can force dilutive equity raises in times of market stress.

Sentiment Drivers

\- **Elevated Valuations:** With falling interest rates and investors chasing higher dividend yielding REITs, the sector is trading at elevated valuations to its own long term averages. As well as other less rate sensitive sectors, Real Estate is better positioned for the later stages of the bull market cycle.

\- **Long Term Cycle Headwinds:** REITs have been one of the best performing categories over the last 20 years, and their inverse relationship to interest rates likely presents performance headwinds especially during a US rate hike cycle.

UNDERWEIGHT FINANCIALS

European Banks are likely to surprise overly dour expectations, as investors underestimate rebuilt balance sheets and the region's economic strength. Meanwhile, US Financials likely face headwinds related to a compressing yield curve, and elevated expectations for financial deregulation, which likely disappoint.

Economic Drivers

+ **Improving Asset Quality Globally:** Non-Performing Loans (NPLs) continue to decline, showing consistent and gradual balance sheet improvement. Historically, when NPL ratios begin to rise, bank underperformance follows thereafter. The biggest improvements in asset quality should continue to come out of Europe.
+ **Capital & Liquidity Buffers at Record Highs Globally:** In every major developed market, bank capital is at record highs. The pace of additional capital raises has slowed dramatically, with most regions nearing or above stringent compliance levels. EU banks are now as well capitalised as US banks.
+ **Benign Inflation:** Global inflation remains modest, a positive backdrop for Financials outperformance. A surge of inflation historically portends Financials underperformance, as aggressive rate hike cycles tend to follow. Financials equally dislike deflation and its associated economic problems, neither is occurring today, nor are they likely near-term.
+ **Loosening Loan Standards:** Global bank lending surveys show and easing of loan standards globally. In aggregate, the EU survey remains the most positive, while the US survey has narrowed the gap some. Whichever region's banks offering better access to credit, typically outperform.

± **Mixed Housing Price Appreciation:** US home price growth remains solid, but is trending sideways, while decelerating in the UK, and accelerating across Europe.

± **Mixed Loan Growth Trends:** In international markets, while below previous cycle growth rates, loan growth continues to modestly accelerate. In the US, while still positive, loan growth has decelerated throughout the year as the yield curve flattened and borrowers adjust to higher short-term rates.

± **Negative Interest Rates & QE:** Experimental and in our view inappropriate monetary policy has long been a headwind to both European and Japanese banks. Both central bank heads have begun shifting their tone towards tapering or ending their QE programmes.

- **US Yield Curves Compression:** We expect modest yield curve compression in the US as the Fed continues its rate hike cycle, placing upside pressure on short rates while long rates likely respond to the reduced inflation expectations by remaining low. The reduced spread should be a headwind to US Financials.
- **Low Mid & Long Term Interest Rates:** Global interest rates remain under pressure from international monetary policy and fears of slowing growth. Global Financials have become highly correlated to changes in the US 5Yr Treasury rate—most US banks are targeting about a 5Yr duration to be less rate sensitive in anticipation of rising short rates, driven by a US rate hike cycle.

Political Drivers

± **Corporate Tax Reform:** US corporate tax reform likely benefits the sectors with highest effective tax rates, like Financials. But expectations for an immediate positive impact are very high, and the widely publicised legislation likely has limited positive surprise power after the Q4 2017 rally.

± **Trump Speculation/Brexit Fears:** Trump is attempting to ease some of Dodd-Frank, creating short-term optimism, yet the likelihood of sweeping change is limited. Brexit consequences are also likely to linger for some time, but current worst-case scenario fears seem vastly overdone.

- **New Regulatory Regimes Reduce Profitability:** Basel 3, Dodd Frank, FSB's, Solvency 2 and central bank regulators have collectively endorsed the highest capital hurdle rates in history, raising the cost of capital across the sector. The most extreme changes are being felt in money markets and Fixed Income Currency, Commodities (FICC) units—driving many investment banks to opt for an asset-light strategy with a greater emphasis on asset management.

Sentiment Drivers

+ **Discounted European Bank Valuations:** While the whole sector still trades at a discount to its historic P/B ratio, Europe's discount relative to other regions is particularly pronounced. This discount is unwarranted, given the improving economic backdrop and the substantial balance sheet improvement.

± **Offensive Sector:** Financials is the most consistent outperforming sector when the market is up greater than 20%; conversely, it is also one of the most consistent laggards when the market is down more than 20%.

- **Late Cycle Underperformance:** US Financials consistently underperforms in the final stages of the bull market, lagging in the final 25% in 9 of the last 11 bulls. It seems likely we are entering this final stage of the market cycle—when US Financials typically starts to underperform. Non-US banks don't follow this same trend
- **Recency Bias:** Investors remain quite skittish on the sector, and rumors of solvency concerns have led to large sentiment swings. This is particularly true of European Financials as investors occasionally appear to continue to fight the last war despite robust fundamental improvement.

Sector positioning is based on a representative US Small and Mid Cap Core portfolio as of 31/12/2017, see additional disclosure at end of document.

Exhibit 23: Portfolio Sector Weights vs. Russell 2500 Total Return Index, as of 31/12/2017

Sector	Relative Weight	FI US Small and Mid Cap Core	Russell 2500
Information Technology	21.5%	37.9%	16.4%
Health Care	16.9%	28.2	11.3
Industrials	0.4%	16.8	16.4
Consumer Discretionary	0.0%	12.7	12.7
Telecommunication Services	-0.5%	0.0	0.5
Consumer Staples	-1.6%	1.3	2.9
Materials	-3.4%	2.7	6.1
Utilities	-3.7%	0.0	3.7
Energy	-4.1%	0.4	4.5
Real Estate	-9.2%	0.0	9.2
Financials	-16.2%	0.0	16.2

Excludes cash. Source: Eagle Investment Systems LLC.

PORTFOLIO HOLDINGS & CHARACTERISTICS

TOP TEN HOLDINGS

Exhibit 24: Top Ten Holdings, as of 31/12/2017

	Security Name	Weight	Country of Issue	GICS Sector
1	Align Technology	4.1%	United States	Health Care
2	IPD Photonics	3.8%	United States	Information Technology
3	Total System Services	3.0%	United States	Information Technology
4	ON Semiconductor	3.0%	United States	Information Technology
5	ServiceNow	2.8%	United States	Information Technology
6	Owens Corning	2.7%	United States	Industrials
7	Pool Corporation	2.7%	United States	Consumer Discretionary
8	Dominos Pizza	2.7%	United States	Consumer Discretionary
9	FICO	2.7%	United States	Information Technology
10	Charles River Laboratories	2.7%	United States	Health Care

Based on a representative US Small and Mid Cap Core portfolio, excluding cash, see additional disclosure at end of document. Source: Eagle Investment Systems LLC.

VALUATIONS

Exhibit 25: Portfolio Characteristics vs. Russell 2500 Total Return Index, as of 31/12/2017

	P/E	P/B	Dividend Yield (%)	Weighted Average Market Cap ($ Mil)
Fisher Small and Mid Cap Core	32.7	4.4	0.5	$11,397
Russell 2500 Total Return	24.1	2.5	1.4	$5,246

Based on a representative US Small and Mid Cap Core portfolio, excluding cash, see additional disclosure at end of document. Source: Eagle Investment Systems LLC.

Best and Worst Performing Holdings

Exhibit 26: Best Performers, 2017 Q4

Name	Country	Sector
Align Technology, Inc.	**United States**	**Health Care**
Align Technology, the specialty health care supply firm focused on clear orthodontic aligners, outperformed on better-than-expected case volumes amid strong global demand. Going forward, the company should continue to benefit from growing discretionary healthcare spending as the global economic expansion continues.		
CalAtlantic Group, Inc.	**United States**	**Consumer Discretionary**
CalAtlantic Group, the Arlington, Virginia based homebuilder, outperformed on news it would be acquired by Lennar Corporation at a significant premium to its pre-merger price. Looking forward, the combined company should be well-positioned amid a favorable outlook for home building sales driven by low financing costs, improving mortgage loan availability, and rising consumer incomes.		
Total System Services, Inc.	**United States**	**Information Technology**
Total System Services, a provider of payment processing and merchant services, outperformed tied to increasing electronic payments usage and higher credit card activity. Issuer Solutions (+6% y/y) benefited from records traditional card AOFs (accounts on file) and transaction volumes, while Merchant Services (+7% y/y) saw strength across small and medium-sized businesses. In addition, retail channel improvements—including agreements with Kroger (new), Walmart (expanded) and Speedway (renewed)—helped drive a 16% y/y increase in NetSpend revenue.		

Based on securities' total contribution (i.e., their weighted absolute return), gross of fees, to a representative US Small and Mid Cap Core portfolio over the time period specified above, excluding cash, see additional disclosure at end of document. It should not be assumed recommendations made in the future will be profitable or will equal the performance of securities in this review.

Exhibit 27: Worst Performers, 2017 Q4

Name	Country	Sector
Domino's Pizza, Inc.	**United States**	**Consumer Discretionary**
Domino's Pizza, the global pizza delivery company, underperformed on competition concerns. Going forward, it should benefit from growing consumption amid a healthy global economy, while its best-in-class ordering technology is ideally suited to address increasing consumer preference for online and mobile food ordering.		
Incyte Corporation	**United States**	**Health Care**
Incyte, the biopharmaceutical producer focused on cancer and arthritis, underperformed on fears of increasing competition from compounds under development by Bristol Myers and AbbVie. Positively, the company should benefit from a high growth profile driven by its first approved drug, Jakafi, and the potential 2018 approval of its second drug. In addition, Incyte boasts an attractive pipeline in the fast-growing markets of cancer immunotherapy and next-generation oral arthritis treatments. Lastly, the biotech industry should see a favorable regulatory environment moving forward highlighted by increased drug approval rates and lower development costs.		
Autodesk, Inc.	**United States**	**Information Technology**
Autodesk, the computer-aided design (CAD) solutions provider, underperformed amid its ongoing transition to a subscription-based revenue model. While these transitions are often lumpy from quarter to quarter, the long-term payoff should be higher revenue visibility, increasing revenue per customer, and a greater contribution of higher-margin direct sales. In addition, Autodesk is well-positioned to benefit from an improving global spending environment for construction and manufacturing firms.		

Based on securities' total contribution (i.e., their weighted absolute return), gross of fees, to a representative US Small and Mid Cap Core portfolio over the time period specified above, excluding cash, see additional disclosure at end of document. It should not be assumed recommendations made in the future will be profitable or will equal the performance of securities in this review.

Buys and Sells

Exhibit 28: Buys, 2017 Q4

Security	Country	Sector
There were no new buys during the quarter.		

Based on a representative US Small and Mid Cap Core portfolio, excluding cash, see additional disclosure at end of document. It should not be assumed recommendations made in the future will be profitable or will equal the performance of securities in this review.

Exhibit 29: Sells, 2017 Q4

Security	Country	Sector
There were no full sells during the quarter.		

Based on a representative US Small and Mid Cap Core portfolio, excluding cash, see additional disclosure at end of document. It should not be assumed recommendations made in the future will be profitable or will equal the performance of securities in this review.

MARKET RECAP

SECTOR

Please see the table below for a list of Russell 2500 sector index returns.

Exhibit 30: Russell 2500 Index Sector Returns, as of 31/12/2017

Sector	2017 Q4
Industrials	8.1%
Consumer Discretionary	8.0%
Energy	7.9%
Materials	7.1%
Consumer Staples	6.2%
Russell 2500 Total Return	**5.2%**
Information Technology	4.7%
Financials	4.2%
Utilities	2.6%
Health Care	2.2%
Real Estate	1.9%
Telecommunication Services	-0.5%

Returns based in USD. Source: Eagle Investment Systems LLC.

Industrials

Industrials outperformed in the fourth quarter, as the economically sensitive sector benefitted from global economic data consistently surprising to the upside and resource prices rallying. Commodity price sensitive companies, like those found in the machinery and Construction and Engineering industries, outperformed tied to climbing metal and oil prices.

Consumer Discretionary

Consumer Discretionary outperformed in Q4 as economic data surprised to the upside, benefitting cyclical firms. Additionally, US tax reform was a tailwind to domestically-oriented US firms.

Real Estate

The Real Estate sector faced multiple headwinds during the quarter. First, rising long term interest rates weighed on investor demand for REITs, as the industry has been used as a bond substitute throughout this low absolute yield environment. Second, the tax overhaul in the US has no benefit to the US REIT Industry, as the average effective tax rate of a REIT is 3%—well below the new 21% tax rate. Industries with the highest effective tax rates benefited to a greater degree immediately following the announcement.

Telecommunication Services

The Telecom sector underperformed as would be expected in a rising market environment such as Q4 when market sentiment is improving. Telecom is traditionally a relatively defensive sector. Competition also increased in a number of markets globally, driving down prices.

Fisher Investments Institutional Group claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS standards. The firm has been independently verified for the periods January 01, 1990 through December 31, 2015.

Verification assesses whether (1) the firm has complied with all the composite construction requirements of the GIPS standards on a firm-wide basis and (2) the firm's policies and procedures are designed to calculate and present performance in compliance with the GIPS standards. The Fisher Investments Institutional Group Small Mid Cap Core Composite has been examined for the periods June 01, 2014 through December 31, 2015. The verification and performance examination reports are available upon request.

Performance is preliminary as of January 04, 2018.

1. Fisher Asset Management, LLC, doing business as Fisher Investments (FI), is an investment adviser registered with the US Securities and Exchange Commission. As of December 31, 2017 FI managed assets valued over $94 billion. FI maintains two principal business units – Fisher Investments Institutional Group (FIIG) and Fisher Investments Private Client Group (FIPCG). FIPCG services substantially all private client accounts managed by FI and FIIG services substantially all institutional accounts managed by FI (including those accounts sub-managed for Fisher Investments Europe and Fisher Investments Australasia). The Investment Policy Committee is responsible for all strategic investment decisions for both business units.
2. The FIIG Small and Mid Cap Core composite consists of accounts managed against the Russell 2500 Index with a view towards capital appreciation.
3. The Russell 2500 Index is a subset of the Russell 3000 Index. It includes approximately 2500 of the smallest securities based on a combination of their market cap and current index membership. The Russell 2500 Index measures the performance of the small to mid-cap segment of the U.S. equity universe. The Russell 2500 Index is constructed to provide a comprehensive and unbiased barometer for the small to mid-cap segment. The Index is completely reconstituted annually to ensure larger stocks do not distort the performance and characteristics of the true small to mid-cap opportunity set. Returns are presented inclusive of dividends.
4. Fisher Investments performance calculation system uses time-weighted rates of return, with valuation on a daily basis and geometric linking of periodic returns. Valuations are based on trade date. Neither leverage nor derivatives have been used in obtaining performance. Returns reflect the reinvestment of dividends, royalties, interest and other forms of accrued income. Where equity sub-sector returns have been used, cash and cash equivalent returns are allocated to the equity sub-sector returns to create equity sub-sector plus cash returns. Net performance figures are presented after deduction of actual management fees and are inclusive of performance based fees where applicable.
5. Valuations and returns are computed and stated in US Dollars.
6. The dispersion of annual returns is measured by the asset-weighted standard deviation across portfolio returns gross of fees represented within the composite for the full year. The composite dispersion is shown as N/A when there is 1 or fewer accounts in the composite for the full calendar year.
7. Fisher Investments Institutional Group standard fee schedule for Small and Mid Cap Core (also listed in Part 2A of Fisher Investments' Form ADV) is: 0.85% on the first $25 million, 0.80% on the next $25 million, 0.75% on the next $50 million, 0.70% on the next $50 million, and negotiable beyond $150 million.
8. This composite was created in June 2014
9. A list of FIIG composite descriptions is available upon request.
10. The policies regarding valuing portfolios, calculating performance, and preparing compliant presentations are available upon request.

11. Three year annualized ex-post standard deviation is measured using asset-weighted monthly composite returns gross of fees. Ex-post standard deviation for the Fisher Investments Institutional Group Small Mid Cap Core Composite and Benchmark are not presented for years 2014 - 2016 because 36 monthly returns are not available.

12. Investment in securities involves the risk of loss. Past performance is no guarantee of future returns. Other methods may produce different results, and the results for individual portfolios and for different periods may vary depending on market conditions and the composition of the portfolio.

Fisher Investments Institutional Group US Small and Mid Cap Core Annual and Annualised Performance (USD)

Year	Gross Annual Return (%)	Net Annual Return (%)	Benchmark Return (%)	Number of Portfolios	Composite Dispersion	Total Assets at End of Period (USD millions)	Total FI Institutional Assets* (USD millions)	% of FI Institutional Assets*
2017	37.5%	36.5%	16.8%	2	0.1%	$83.72	$44,197.48	0.2%
2016	12.5%	11.7%	17.6%	3	0.0%	$73.64	$33,962.17	0.2%
2015	3.2%	2.5%	-2.9%	3	0.1%	$65.94	$30,938.95	0.2%
Jun-14 to Dec-14	9.4%	9.0%	5.9%	3	N/A	$64.36	$28,167.34	0.2%

Annualised as of 31/12/2017			
1 Year	37.5%	36.5%	16.8%
3 Year	16.8%	16.0%	10.1%
Since Inception (01/06/2014)	16.8%	16.0%	10.1%

Year	Composite 3 Year St Dev	Benchmark 3 Year St Dev
2017	13.5%	12.1%

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Performance figures as of 31/12/2017 are preliminary. Preliminary performance is subject to the final reconciliation of accounts and deduction of any outstanding advisory fees, which will have the effect of lowering performance by the amount of the deductions.

**Total FI Institutional Assets and % of FI Institutional Assets represent assets within Fisher Investments Institutional Group strategies only.*

Sources: Eagle Investment Systems LLC & FactSet

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Should you have any questions about any of the information provided above, please contact FIE by mail at 2nd Floor 6-10 Whitfield Street, London W1T 2RE or by telephone at +44 (0)207 299 6848.

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The foregoing information is based on a representative portfolio (rather than a composite or an average of a group of portfolios), excluding cash, unless otherwise denoted. This representative portfolio information is derived from an actual client portfolio. Clients' portfolio characteristics may differ given the various investment restrictions, cash requirements and other circumstances that can apply to particular clients. Portfolio information is as of the dates indicated, and no assurances can be given that it has not changed or that it will not change in the future.

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FIE is wholly-owned by FI, which is wholly-owned by Fisher Investments, Inc. Since inception, Fisher Investments, Inc. has been 100% Fisher-family and employee-owned, with Ken Fisher owning more than 75% of FII.

Unless otherwise specified, references to investment professionals, operations personnel, and middle and back office personnel are references to FI employees. "We", "our," "us" and "the firm" generally refer to the combined capabilities of FIE and FI.

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2. **Communications:** Fisher Investments Europe can be contacted by mail at 6-10 Whitfield Street, London W1T 2RE; by telephone on +44 0800 144 4731; or by email to FIEOperations@fisherinvestments.co.uk. All communications with Fisher Investments Europe will be in English only. Fisher Investments Europe's web address is https://institutional.fisherinvestments.com/en-us/mifidii.
3. **Services:** These Terms of Business explain the services offered to professional clients and will apply from when Fisher Investments Europe begins to advise you. Fisher Investments Europe offers restricted advice only (meaning it does not offer independent advice based on an analysis of the whole of the market), as more fully explained in Clause 4 below. As part of its services, Fisher Investments Europe seeks to:
    a. Reasonably determine your client categorisation;
    b. Understand your financial circumstances and investment aims to determine whether the full discretionary investment service described in Clause 4 and the proposed investment mandate and accompanying benchmark(s) (or an Undertaking for Collective Investment in Transferable Securities ("UCITS") with a similar manadate and benchmark for which Fisher Investments Europe's parent company serves as investment manager) are suitable for you;
    c. Explain features of the investment strategy;
    d. Describe investment performance as it relates to the investment strategy;
    e. Provide a full explanation of costs;
    f. Assist in the completion of documentation;
    g. Where specifically agreed, review your position periodically and suggest adjustments where appropriate.

Fisher Investments Europe will not provide ongoing services unless you enter into an agreement for discretionary investment management services or invest in a UCITS as described in Clause 4.

4. **Discretionary Investment Management Service and Investments:** To help you achieve your financial goals, Fisher Investments Europe may offer its discretionary investment management services. In such case, Fisher Investments Europe will delegate the portfolio management function, as well as certain ancillary services, to its parent company, Fisher Asset Management, LLC, trading as Fisher Investments, which has its headquarters in the USA and is regulated by the US Securities and Exchange Commission. In certain limited circumstances where appropriate, Fisher Investments Europe may recommend that you establish a discretionary investment management relationship directly with Fisher Investments. In such case, Fisher Investments Europe acts as an introducing firm. A separate investment management agreement will govern any discretionary investment management relationship whether with Fisher Investments Europe or with Fisher Investments. Subject to applicable regulations, for qualified investors Fisher Investments Europe may recommend an investment in UCITS regulated by the Central Bank of Ireland and for which Fisher Investments serves as investment manager.
5. **Client Categorisation:** Fisher Investments Europe deals with both retail clients and professional clients. All clients and potential clients who deal with Fisher Investments Europe's institutional relationship managers ("RMs") will be treated as professional clients, either through qualification as a professional client or, in the case of local municipal authorities, through opting up to be treated as a professional client. Accordingly, you are categorised as a professional client. You have the right to request re-categorisation as a retail client which offers a higher degree of regulatory protection, but Fisher Investments Europe does not normally agree to requests of this kind.

6. **Financial Services Compensation Scheme ("FSCS"):** Whilst the activities of Fisher Investments Europe are covered by the FSCS, compensation under the FSCS in the event Fisher Investments Europe is unable to meet its liabilities because of its financial circumstances is only available to eligible claimants. In addition, the protections of the UK regulatory regime, including the FSCS, do not apply in relation to the services of Fisher Investments or any non-UK service providers or to the extent your assets are invested in non-UK funds or ETFs. In the event you are eligible and do have a valid claim, the FSCS may be able to compensate you for the full amount of your claim up to £50,000 per person per firm. You can contact Fisher Investments Europe or the FSCS (www.fscs.org.uk) in order to obtain more information regarding the conditions governing compensation and the formalities which must be completed to obtain compensation.
7. **Risks:** Investments in securities present numerous risks, including various market, currency, currency fluctuation, economic, political, instability, business, differences in financial reporting, liquidity risk, interest rate risk, credit risk, and other risks, and can be very volatile. Investing in securities can result in a loss, including a loss of principal. Using leverage to purchase and maintain larger security positions will increase exposure to market volatility and risk of loss and is not recommended. Investments in securities are only suitable for clients who are capable of undertaking and bearing a risk of loss. Specific risks associated with particular types of securities that may be held in your account are explained further in the IMA.

Past performance is not a guarantee nor a reliable indicator of future investment returns. Fisher Investments Europe cannot guarantee and makes no representation or warranty as to future investment returns or performance. There is no guarantee for avoidance of loss, which is impossible with investments in securities, and you have not received any such guarantee or similar warranty from Fisher Investments Europe or any representatives thereof.

8. **Data Protection:** To advise you on financial matters, Fisher Investments Europe may collect personal and sensitive information subject to applicable data protection laws. By providing such information to Fisher Investments Europe, you consent to Fisher Investments Europe processing your data, both manually and electronically, including transferring data outside the European Economic Area, including to its parent, Fisher Investments, in the United States, for the purposes of providing services and enabling Fisher Investments to provide services, maintaining records, analysing your financial situation, providing information to regulatory bodies and service providers assisting Fisher Investments Europe and/or Fisher Investments in providing services, or otherwise permitted by law. Upon request, you are entitled to obtain access to and to rectify the data relating to you.
9. **Custody and Execution:** Neither Fisher Investments Europe nor Fisher Investments is authorised to hold client money. Neither Fisher Investments Europe nor Fisher Investments will accept cheques made out to it in respect of investments, nor will they handle cash. All client assets are held at external custodians where each client has a direct account in their own name. If you appoint Fisher Investments Europe as your discretionary asset manager, execution of transactions will be arranged through such custodians and brokers and at such prices and commissions that Fisher Investments determines in good faith to be in your best interests. Further information regarding selection of brokers is set out in the investment management agreement with Fisher Investments Europe (the "IMA").

If you appoint Fisher Investments Europe as your discretionary asset manager, Fisher Investments Europe or Fisher Investments, pursuant to an outsourcing agreement with Fisher Investments Europe, will arrange for the execution of transactions through those custodians and brokers and at such prices and commissions that it determines in good faith will be in your best interests. Further information regarding the selection of brokers is governed by the IMA. Fisher Investments Europe does not structure or charge its fees in such a way as to discriminate unfairly between execution venues.

The brokers and dealers to which your transactions may be allocated will use various execution venues, including without limitation:

a. Regulated Markets in the USA or elsewhere (usually those exchanges where companies have their primary listing and other exchanges on which their securities are admitted to trading);
b. Multi-Lateral Trading Facilities ("MTF") and Organised Trading Facilities ("OTF") in the USA or elsewhere (i.e. a multilateral system, operated by an investment firm or a market operator, which brings together multiple third-party buying and selling interests in financial instruments—in the system and in accordance with non-discretionary rules—in a way that results in a contract);

c. Systematic Internalisers (which are investment firms dealing as principal and providing liquidity on a systematic basis);
d. Other liquidity providers that have similar functions to any of the above;
e. Counterparties that may access the above venues on behalf of Fisher Investments Europe or Fisher Investments (or their clients) or trade on their own account.

You must be notified and approve of any off-venue trades prior to execution unless previously agreed to by you directly with the custodian. As a result of brokers/dealers using the execution venues mentioned above, your transactions may be executed on an execution venue that is neither a regulated market in the European Union nor an MTF in the European Union and therefore you will be required to expressly consent to the execution policy of Fisher Investments Europe by signing the IMA.

Fisher Investments Europe's top five trading venues are listed on its website.

Generally, financial instruments will not be affected if a custodian suspends payments or goes bankrupt. This is due to the fact that you will normally be able to take possession of your financial instruments based on the custodian's registration of your rights. Generally, it is only if the custodian fails to handle your financial instruments or register your rights correctly where you may not be able to take possession of the financial instruments.

If you appoint Fisher Investments Europe as your discretionary asset manager, you will receive a periodic statement every calendar quarter. This statement compares the performance of your account with that of a relevant benchmark in order to facilitate the assessment of performance achieved by the account. For performance, management fee calculation and reporting purposes, exchange traded equity securities are valued based upon the price on the exchange or market on which they trade as of the close of business of such exchange or market. All equity securities that are not traded on a listed exchange are valued using a modelled estimate of the bid price, also known as a bid evaluation, provided by Fisher Investments Europe's primary pricing service. Fixed income securities are valued based on market quotations or a bid evaluation provided by Fisher Investments Europe's primary pricing service. All securities are valued daily given a price from Fisher Investments Europe's primary pricing service is provided; otherwise, all securities are valued on at least a monthly basis.

10. **Conflicts of Interest:** Fisher Investments Europe has a conflicts of interest policy to identify, manage and disclose conflicts of interest Fisher Investments Europe, Fisher Investments or any of their employees or representatives may have with a client of Fisher Investments Europe, or that may exist between two clients of Fisher Investments Europe. Fisher Investments Europe's conflicts of interest policy covers gifts and favours, outside employment, client privacy, inadvertent custody, marketing and sales activities, recommendations and advice, and discretionary investment management services. RMs employed by Fisher Investments Europe are paid a variable component of their total remuneration, calculated as a percentage by reference to management fees paid to the Investment Manager during the first three years of the client relationship. Such remuneration is will not increase or impact the fees payable by you. Details on Fisher Investments Europe's conflicts of interest policy are available on request. In addition, Fisher Investments Europe provides a copy of Fisher Investments' Form ADV Parts 2A and 2B to all clients, detailing additional conflicts of interest applicable to Fisher Investments.
11. **Fees:** If you appoint Fisher Investments Europe as your discretionary investment manager, you will pay management fees to Fisher Investments Europe as detailed in the IMA. Fisher Investments Europe will pay a portion of such management fees to Fisher Investments as the sub-manager. If you appoint Fisher Investments directly as your discretionary investment manager, you will pay management fees directly to Fisher Investments as detailed in the investment management agreement. If you invest in a UCITS fund managed by Fisher Investments, Fisher Investments will receive its management fee indirectly through the UCITS. Fisher Investments Europe does not charge a separate fee for its introducing or distribution services. You will also incur transaction and custody fees charged by brokers and custodians. However, any such additional fees will be payable directly to brokers/custodians, and neither Fisher Investments Europe nor Fisher Investments will share in any commission or other remuneration.
12. **Termination:** If you wish to cease using the services of Fisher Investments Europe at any time, then send notification and the arrangement will cease in accordance with the IMA. However, if a transaction is in the middle of being arranged on your behalf at that time and it is too late to unwind it, then the transaction may need to be completed first.

13. **Complaints:** Fisher Investments Europe seeks to provide a high standard of service to clients at all times. If you have a complaint about services, please contact Fisher Investments Europe:

    by writing to: Head of Compliance
    Fisher Investments Europe Limited
    2nd Floor, 6-10 Whitfield Street
    London W1T 2RE

    or by calling: +44 0800 144 4731

    or by emailing: FIEOperations@fisherinvestments.co.uk

Fisher Investments Europe will endeavour to resolve the matter, as soon as practicable and generally within 8 weeks. If you are dissatisfied with the outcome of any complaint made to Fisher Investments Europe, or you do not receive a response within such time, you may be eligible to complain directly to the UK Financial Ombudsman Service ("FOS"). Further details in respect of FOS can be found at www.financial-ombudsman.org.uk.

14. **Governing Law:** These Terms of Business are governed by English law.