Global Equities

1. Background

1.1 With effect from mid December 2015, the Fund replaced its then two global equities managers, Pictet Asset Management and Janus Intech, with three new managers, Allianz Global Investors, Investec Asset Management and Wellington Investment Management.

2. Valuation

2.1 The table below summarises the valuations for the three managers as at 1 April 2017 and 31 December 2017.

	Allianz	Investec	Wellington	Total
	£000s	£000s	£000s	£000s
Valuation 01-Apr-17	270,886	193,966	206,868	671,720
Investment	-	-	-	-
Distribution	-	-	-	-
Increase in Valuation	20,929	14,962	13,672	49,563
Valuation 31-Dec-17	291,815	208,928	220,540	721,283

2.2 No additional investment has been made with the three managers this financial year.

3. Performance

3.1 The table below summarises the performance for each manager in absolute terms and compared to their respective benchmarks for the quarter, the financial year and since inception to 31 December 2017.

	Allianz	Investec	Wellington
Quarter to Date			
Performance	4.6%	5.5%	4.6%
Benchmark	4.6%	4.6%	4.6%
Relative Return	0.0%	0.9%	0.0%
Financial Year to Date			
Performance	7.8%	7.7%	6.0%
Benchmark	6.4%	6.4%	6.4%
Relative Return	1.4%	1.3%	-0.4%
Twelve Months to Date			
Performance	12.5%	13.5%	12.6%
Benchmark	11.8%	11.8%	11.8%
Relative Return	0.7%	1.7%	0.8%
Since Inception			
Performance	20.0%	19.5%	19.8%
Benchmark	19.0%	19.0%	19.0%
Relative Return	1.0%	0.5%	0.7%

3.2 Investec outperformed its benchmark for the three months to 31 December 2017 by 0.9%, whilst Allianz and Wellington matched theirs benchmarks over the same period. Since inception, Allianz, Investec and Wellington have outperformed their benchmarks by 1.0%, 0.5% and 0.7% respectively.

4. Market Review

4.1 Global equities rallied strongly over the final three months of 2017, with the FTSE All World Index reaching a fresh new high in the closing days of the year. Shares were boosted by optimism over the health of the global economy and US tax reform. At a sector level, information technology, materials and consumer discretionary performed best, while utilities was the only sector to retreat over the final three months of 2017.

4.2 US equities rallied strongly over the quarter, with both large and small cap indices touching fresh highs. Share prices were buoyed by better than expected third quarter earnings, renewed merger and acquisition activity, and optimism over the prospects for tax reform.

4.3 Eurozone equities ended the quarter with flat returns (in Eur terms), lagging many other regions as political risks weighed on investor sentiment. In terms of sectors, real estate and materials stocks delivered the strongest returns, with healthcare stocks among the weakest, along with telecommunication services. On balance, equity markets in the Pacific ex Japan rose strongly over the quarter, helped by growing optimism over the health of the global economy and signs of a pick up in Asian trade.

4.4 Japanese equities were among those with the strongest returns over the quarter, outperforming most other markets. Shares were boosted by Prime Minister Shinzo Abe’s decisive victory in October’s snap election in which he won over two-thirds of available seats.

4.5 Emerging market equities rallied over the quarter, buoyed by optimism over the health of the global economy and the prospects for global trade. All regions delivered positive returns, led by Asia, with Eastern Europe and Latin America recording more moderate gains.

Manager Commentaries

5. Allianz

5.1 In this quarter, the portfolio return matched the benchmark as positive returns from trend following investment styles were offset by the weakness in value during the period. Overall, sector allocation did not contribute to relative performance although stock selection within sectors was positive, particularly in industrials, utilities and energy. Likewise, regional allocations yielded flat results however stock selection within regions was strong in Japan and the Eurozone but detracted in the UK and North America.

5.2 This quarter was a solid period for investment styles, leading to a positive return for the strategy during the quarter. Value, the most prominent investment style delivered a negative return which impacted the relative performance. The trend-following investment styles Momentum and Revisions were positive in aggregate over the quarter, largely driven by solid performance from earnings revision strategies. During October, the continuation of the pattern of investment style return saw Value declining and Non-Value investments styles rising. In November and December, this pattern tentatively reversed with Value outperforming and trend-following investment styles underperforming. Value stocks, in particular US Value stocks, were helped by the prospects of tax reforms where Small Cap names typically benefit more than

Large Cap Growth names. Momentum stocks suffered most from this reversal as demonstrated by the Momentum “mini-crash” in late November/early December.

5.3 Sector allocation detracted during the quarter despite gains from the overweight in IT (+8bps) and the underweight in Financials (+2bps). These positive relative impacts were offset by the overweight in Healthcare (-4bps) and the underweight allocations against the benchmark in Energy and Materials (each -3bps). The Within sectors, stock selection was positive with success in sectors such as Industrials, Utilities and Energy. Stock selection within Consumer Discretionary and IT detracted from relative performance. Overall the regional allocation had little impact on relative performance. The overweight in the Eurozone (-7bps) and the underweight in UK (-2bps) were not successful and offset the gains made from the underweight in Europe ex UK (+10bps). Stock selection was strong in Japan and the Eurozone, but less successful in the UK and North America. Contributors at a stock level within regions reflect the different performance contributions of different investment styles within those regions.

6. Investec

6.1 The Global research Equity Portfolio performed in line with the index during the quarter and outperformed over the calendar year 2017. Positive stock selection within consumer staples and information technology contributed to returns for the quarter, while weaker selection in consumer discretionary and utilities offset these gains.

6.2 Within consumer staples, the holding in Japanese brewer Asahi Group boosted portfolio returns. Asahi continued to receive earnings upgrades due to good execution, particularly in Europe and in domestic soft drinks. The market also likes the company’s proactive efforts to sell non-core holdings. In the Industrials sector, Japanese equipment manufacturer Komatsu supported performance, as strong mining data across the sector suggested future sales growth. Management also indicated that peak margins in the current industry cycle had the potential to surpass previous ones, providing a further catalyst for the rally. Likewise within industrials, not owning General Electric boosted relative performance after it delivered a poor set of financial results and ground lower throughout the quarter.

6.3 Several holdings within the IT sector were also among the leading contributors to performance over the quarter, led by US cloud software provider NetApp, which surprised the market with better-than- expected earnings, alongside positive forward guidance. Digital payments platform PayPal also advanced after topping profit estimates and raising guidance on rapid growth in mobile payments. US fitness operator Planet Fitness also continued to advance after beating analysts’ estimates, raising guidance and reporting solid growth trends across its platform.

6.4 Although stock selection within the Healthcare sector was positive for the portfolio as a whole, the two leading detractors were healthcare companies. Firstly, biopharmaceutical firm Celgene fell heavily after reporting that the quarter sales of its key psoriasis drug Otezla badly missed estimates, as did overall quarterly revenue. The company also significantly cut back 2020 sales and earnings targets amid patent challenges and the holding was sold. Secondly, within healthcare, Alexion Pharmaceuticals, an American pharmaceutical company that focuses on developing drugs for ultra-rare diseases delivered earnings results in line with expectations, but the market seems to have expected it to perform better and the stock price fell. However, the investment case remains in place and the stock began to recover into the new year. The consumer discretionary sector weighed on returns for the quarter, with a significant portion of the negative result attributed to Travel IT specialist

Priceline, which owns Bookings.com. The company fell after reporting earnings and travel booking volumes short of expectation.

7. Wellington

7.1 During the quarter, the Global Research Equity Portfolio underperformed the Index with 7 of the 11 sectors negatively impacting value. While positive stock selection within information technology, industrials and real estate primary contributed to relative performance, stock selection in health care and consumer discretionary offset these gains.

7.2 Consumer staples was the best performing sector for the quarter, led by beauty products franchise, Coty, and healthy foods holding company, Simply Good Foods. Coty rebounded from disappointing second quarter results to approach its mid-year high. The firm reported improved third quarter results highlighted by a meaningful improvement in the mass market segment, continued growth in the luxury segment, and modest growth in the professional segment. There are signs of benefits from the Proctor & Gamble acquisition (CoverGirl and Clairol brands), but the integration is still in its early stages. The position is held on trust in the management and the upside potential of a successful integration. Simply Good Foods reported strong earnings and guidance from its Atkins brand. The anticipation is that the newly formed company will acquire additional brands over time and continue to grow its market share.

7.3 Within information technology, NetApp and Qualcomm were leading contributors this quarter. NetApp, the US-based software, systems and services provider for the management and storage of customer data, rose on fiscal second quarter results, which came in ahead of consensus on both the top and bottom line. Revenue growth was driven by their Strategic Products segment. This is a positive and the belief is that the strategic Product line-up could more than offset declining revenues from their mature product segment. While the stock price reacted positively during the quarter, it still trades at a compelling valuation and there is room for further upside potential. Qualcomm, a semiconductor company specialising in cell phones and tablets, rose following the news of rival Broadcom’s bid for the company. In November, Qualcomm released robust quarterly results with particular strengths in the chip division and licensing business. The stock still appears attractive given its leading status in the smartphone industry and the position was trimmed on strength.

7.4 Consumer discretionary was one of the largest relative detractors for the quarter. Underperformance was led by the position in SES, a French provider of satellite communication and solutions for corporate telecom firms and government entities. SES reported disappointing third quarter results driven by weakness in its fixed data and video business. The weaker video business indicates that a greater share of growth will come from data applications, which is a more volatile segment. In addition, the service business, which they purchased in 2015, is faltering causing an additional headwind for the next two quarters. Not owning Home Depot was another negative to performance, as the stock price rose during the quarter.

7.5 Utilities was another weak area in the portfolio for the quarter. Edison, a US-based utility company, sold off as a result of the Southern California wildfires and fears of an open ended liability. Innogy, a Germany based utility company focused on renewables, fell following earnings guidance that was approximately 15-20% below consensus estimates. The earnings downgrades are recurring and growth opportunities seem out of reach until 2020. The CEO left the firm towards the end of the period, a move which has not had a high impact on stock price. This could increase the probability of a merger with Innogy as the target. Confidence in the potential growth in the renewables and network business means that the stocks will continue to be held.

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