**Dorset County Pension Fund Committee 22 November 2018**

**Listed Market Equities**

## 1. Equity Markets Performance

1.1 There was positive performance from the UK in the six months to 30 September 2018. The FTSE100 was the best performer rising 6.4% (454 points). The FTSE Small Cap index was the worst performing UK index despite rising 4.1% (229 points) over the same period. In comparison, performance from major world indices were mixed with the Nikkei 225 the best performing index rising 12.4% (2,666 points), whilst the Shanghai Composite fell 11% (348 points) over the same period. The Dow Jones rose 9.8% (2,355 points) in the six-month period to 30 September 2018.

1.2 Over the twelve-month period to 30 September 2018, there were positive performances from the UK indices. The FTSE250 was the best performer rising 2.2% (432 points), whilst the FTSE Small Cap ex Investments Trust was the worst performing UK index rising 0.6% (50 points). In comparison, performance from major world indices were mixed with the Nikkei225 rising 18.5% (3,764 points), whilst the Shanghai Composite fell 15.8% (528 points) over the same period.

1.3 Both the Dow Jones and the S&P 500 indices reached record highs on 20 September 2018. The S&P 500 was led by technology stocks as strong economic data helped to alleviate trade worries.

1.4 The tables below show the performance of UK and World indices over the six months to September 2018.

**Six months to 30 September 2018**

| Country | Index | 31/03/2018 | 30/06/2018 | % Change |
|---|---|---|---|---|
| UK | FTSE100 | 7,056.1 | 7,510.2 | 6.4 |
| UK | FTSE250 | 19,460.5 | 20,307.0 | 4.3 |
| UK | FTSE350 | 3,941.2 | 4,180.7 | 6.1 |
| UK | Small Cap | 5,593.1 | 5,822.0 | 4.1 |
| UK | Small Cap ex Investment Trusts | 7,354.9 | 7,709.4 | 4.8 |
| UK | All Share | 3,894.2 | 4,127.9 | 6.0 |
| Japan | Nikkei225 | 21,454.3 | 24,120.0 | 12.4 |
| US | Dow Jones | 24,103.1 | 26,458.3 | 9.8 |
| Hong Kong | Hang Seng | 30,093.4 | 27,788.5 | -7.7 |
| France | Cac 40 | 5,167.3 | 5,493.5 | 6.3 |
| Germany | Dax | 12,096.7 | 12,246.7 | 1.2 |
| China | Shanghai Composite | 3,168.9 | 2,821.4 | -11.0 |

**Twelve months to 30 September 2018**

| Country | Index | 30/09/2017 | 30/09/2018 | % Change |
|---|---|---|---|---|
| UK | FTSE100 | 7,372.8 | 7,510.2 | 1.9 |
| UK | FTSE250 | 19,874.8 | 20,307.0 | 2.2 |
| UK | FTSE350 | 4,101.7 | 4,180.7 | 1.9 |
| UK | Small Cap | 5,712.4 | 5,822.0 | 1.9 |
| UK | Small Cap ex Investment Trusts | 7,659.9 | 7,709.4 | 0.6 |
| UK | All Share | 4,049.9 | 4,127.9 | 1.9 |
| Japan | Nikkei225 | 20,356.3 | 24,120.0 | 18.5 |
| US | Dow Jones | 22,405.1 | 26,458.3 | 18.1 |
| Hong Kong | Hang Seng | 27,554.3 | 27,788.5 | 0.8 |
| France | Cac 40 | 5,329.8 | 5,493.5 | 3.1 |
| Germany | Dax | 12,858.9 | 12,246.7 | -4.8 |
| China | Shanghai Composite | 3,348.9 | 2,821.4 | -15.8 |

## 2. Market Review

2.1 Global equities posted positive results for the second straight quarter, extending their year-to-date gain to 6.0%. Global markets stabilized in the wake of robust US economic data while political uncertainty and trade concerns weighed on other regions.

2.2 US and China trade relations remained volatile, as US tariffs on approximately US$200 billion of Chinese imports took effect in September. China promptly retaliated with tariffs on about US$60 billion of US exports.

2.3 Emerging markets volatility spiked after Turkey's financial crisis rattled global markets, but receded at the end of the quarter.

2.4 Oil approached a four year-high amidst global supply uncertainties and strong global growth. Oil inventories declined after OPEC refrained from increasing output and as the first round of US sanctions on Iran went into effect.

2.5 On the monetary front, the US Federal Reserve, the Bank of England and the Bank of Canada raised interest rates by 25 basis points. The European Central Bank remained dovish, leaving rates unchanged and reiterating its pledge to keep them low at least until the summer of 2019.

## UK Equity performance for the period ending 30 September 2018

## 3. Background

3.1 On 11 July 2018, the internally managed passive UK equity portfolio transferred to the Brunel UK Passive Equities portfolio managed by Legal & General Investment Management (LGIM). The Fund also has two UK equities active managers, AXA Framlington and Schroders. This combination of managers and styles is designed to give the opportunity of outperformance against the FTSE All Share index and has a two thirds passive and one third active mix. Details of the combined portfolio (£659.6M at 30 September 2018) are shown in the table at paragraph 4.1.

3.2 Investment in the smallest companies which make up 3.5% of the index is achieved by a holding in the Schroders Institutional UK Smaller Companies Fund which is managed on an active basis.

## 4. Valuation

4.1 The table below summarises the valuations for the four managers as at 1 April 2018 and 30 September 2018.

| | In-House | LGIM | AXA | Schroders | Total |
|---|---|---|---|---|---|
| | £000s | £000s | £000s | £000s | £000s |
| Valuation 01-Apr-18 | 401,402 | - | 190,746 | 55,096 | 647,244 |
| Investment | - | 434,849 | - | - | 434,849 |
| Disinvestment | - 434,849 | - 30,000 | - | - | - 464,849 |
| Increase in Valuation | 33,808 | - 7,585 | 12,543 | 3,610 | 42,376 |
| Valuation 30-Sep-18 | 361 | 397,264 | 203,289 | 58,706 | 659,620 |

## 5. Performance

5.1 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 30 September 2018.

| | | LGIM | AXA Framlington | Schroders |
|---|---|---|---|---|
| **Quarter to Date** | | | | |
| | Performance | -1.6% | -1.3% | 1.1% |
| | Benchmark | -1.5% | -0.8% | -2.1% |
| | Relative Return | -0.1% | -0.5% | 3.2% |
| **Financial Year to Date** | | | | |
| | Performance | - | 6.4% | 6.6% |
| | Benchmark | - | 8.3% | 4.8% |
| | Relative Return | - | -1.9% | 1.8% |
| **Twelve Months to Date** | | | | |
| | Performance | - | 3.4% | 9.7% |
| | Benchmark | - | 5.9% | 0.6% |
| | Relative Return | - | -2.5% | 9.1% |
| **Three Years p.a.** | | | | |
| | Performance | - | 7.7% | 16.1% |
| | Benchmark | - | 11.5% | 9.4% |
| | Relative Return | - | -3.8% | 6.7% |
| **Five Years p.a.** | | | | |
| | Performance | - | 6.5% | 14.6% |
| | Benchmark | - | 7.5% | 8.6% |
| | Relative Return | - | -1.0% | 6.0% |
| **Since Inception** | | | | |
| | Performance | -1.6% | 7.4% | 11.4% |
| | Benchmark | -1.5% | 6.2% | 7.1% |
| | Relative Return | -0.1% | 1.2% | 4.3% |

**Global Equities performance for the period ending 30 September 2018**

## 6. Background

6.1 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 Management. On 18 July 2018 Dorset's global equities under the management of Allianz were successfully transitioned to the Brunel Smart Beta portfolio. In addition, JP Morgan has been the Fund's emerging markets equities manager since April 2012.

## 7. Valuation

7.1 The table below summarises the movement in valuations for all managers for the financial year to 30 September 2018.

| | Allianz £000s | Investec £000s | Wellington £000s | LGIM £000s | JPM £000s |
|---|---|---|---|---|---|
| Valuation 01-Apr-18 | 281,878 | 195,927 | 213,503 | - | 103,200 |
| Investment | - | - | - | 275,115 | - |
| Distribution | - 310,115 | - | - | | - |
| Increase in Valuation | 28,898 | 28,869 | 33,599 | 8,096 | - 5,800 |
| Valuation 30-Sep-18 | 661 | 224,796 | 247,102 | 283,211 | 97,400 |

## 8. Performance

8.1 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 30 September 2018.

| | Investec | Wellington | LGIM | LGIM (Hedged) | JPM |
|---|---|---|---|---|---|
| **Quarter to Date** | | | | | |
| Performance | 5.8% | 7.6% | 3.0% | 2.8% | -0.8% |
| Benchmark | 6.3% | 6.3% | 3.1% | 2.6% | 0.1% |
| Relative Return | -0.5% | 1.3% | -0.1% | 0.2% | -0.9% |
| **Financial Year to Date** | | | | | |
| Performance | 14.7% | 15.7% | - | - | -5.7% |
| Benchmark | 14.9% | 14.9% | - | - | -2.1% |
| Relative Return | -0.2% | 0.8% | - | - | -3.6% |
| **Twelve Months to Date** | | | | | |
| Performance | 13.3% | 17.2% | - | - | -2.4% |
| Benchmark | 14.4% | 14.4% | - | - | 2.0% |
| Relative Return | -1.1% | 2.8% | - | - | -4.4% |
| **Three Years to Date** | | | | | |
| Performance | - | - | - | - | 18.4% |
| Benchmark | - | - | - | - | 18.1% |
| Relative Return | - | - | - | - | 0.3% |
| **Five Years to Date** | | | | | |
| Performance | - | - | - | - | 8.2% |
| Benchmark | - | - | - | - | 8.2% |
| Relative Return | - | - | - | - | 0.0% |
| **Since Inception** | | | | | |
| Performance | 16.9% | 18.9% | 3.0% | 2.8% | 5.9% |
| Benchmark | 17.4% | 17.4% | 3.1% | 2.6% | 5.9% |
| Relative Return | -0.5% | 1.5% | -0.1% | 0.2% | 0.0% |

8.2 Investec underperformed its benchmark over three months by 0.5% and by 0.2% over the six months to the 30 September 2018. Wellington outperformed their benchmark by 1.3% over three months and by 0.8% over six months. Over the twelve-month period to 30 September 2018 Wellington outperformed its benchmark by 2.8% while Investec underperformed by 1.1%. Since inception, Wellington has outperformed their benchmark by 1.5%, whilst Investec has underperformed by 0.5%.

8.3 JP Morgan have underperformed their benchmarks for the quarter, financial year to date and over twelve months, whilst being in line with the benchmark over five years and since inception.

## 9. Manager Commentaries (Active Mandates)

### 9.1 AXA Framlington

<u>Performance</u>: During the quarter, the fund underperformed the FTSE All Share with a return of -1.3% against the benchmark of -0.8%. For twelve months, the fund returned 3.4% against a benchmark of 5.9%. Over the three years, the fund underperformed its benchmark by 3.8% and by 1.0% over the five year period.

<u>Activity</u>: The portfolio underperformed the benchmark in the quarter. The biggest contributor to relative performance was Worldpay. Spirent Communications performed well in anticipation of orders for 5G implementation. Being overweight in healthcare was the most positive contributor to relative returns. Being underweight in financials, especially banks, was a positive influence on sector relative returns. BBA

Aviation was the biggest detractor from relative returns as growth in the USA slowed. Coats was purchased and a new holding, Creo Medical, was purchased. Creo is a medical devices company used in gastrointestinal procedures. Various holdings were reduced. The balance of the holding in Vodafone was sold and the Melrose shares, from the GKN takeover, were disposed.

Outlook and Strategy: The US trade/tariff disputes continue to create volatility and there is monetary tightening happening on both sides of the Atlantic. Merger and acquisition activity was noticeable, even into elevated share valuations. Brexit continues to lessen consumer confidence in the UK. Rising bond yields are having implications for equities, especially where companies are financially leveraged.

9.2 **Schroders**

Performance and Market Summary: The fund significantly outperformed its FTSE Small Cap (ex-investment companies) benchmark over three months under review by 3.2%. Over the twelve-month period the Fund returned 9.7% against its benchmark of 0.6%. Over the three years the Fund outperformed the benchmark by 6.7% and by 6.0% over the five-year period.

Activity: Medical enterprise software supplier Craneware was a top contributor after its full-year results underlined the significant potential growth opportunity in its US healthcare market. Miniatures manufacturer Games Workshop also performed very well after the company confirmed that quarter 1 trading had been robust despite tough comparatives, prompting earnings upgrades against conservatively set expectations. In addition, management declared a dividend at a similar level to the one paid at the same time last year, indicating that cashflows have remained strong.

Travel and logistics group Dart performed very well on revealing that its 2019 pre-tax profits would “substantially exceed” market expectations. Meanwhile, shares in mobile advertising platform provider Taptica International continued to recover from the lows they struck earlier in the year. Sentiment towards Taptica has been negatively impacted by fears around the possible negative regulatory implications for data-driven media models following revelations around the misuse of personal information obtained from Facebook. However, the company published another set of strong results, included a confident outlook statement, revealing Taptica is on course to exceed full-year market expectations for EBITDA. A positive to performance was not owning African diamond miner Petra Diamonds which performed poorly after revealing it would miss production targets for 2019. The holding in Sinclair Pharma, which specialises in minimally invasive cosmetic surgery such as collagen treatment, performed well on the back of a recommended bid approach from Chinese pharmaceuticals group Huadong Medicine.

On the negative side, semiconductor manufacturer IQE fell in the wake of disappointing interim results. Oil services group Lamprell gave back gains of the previous quarter when a major shareholder in the company had doubled its stake, creating upward pressure on the stock. Lamprell continues to await confirmation of a long-term agreement with Saudi Arabia’s state oil company Saudi Aramco. Multi-channel women’s fashion retailer QUIZ performed poorly as sentiment towards the sector was negatively impacted by fears around the competitive pressures seemingly affecting the online retail sector. Intense competition was seen as a key driver of a profit warning from European online fashion retailer Zalando. In addition, investors were concerned about the possible knock-on impact on QUIZ of House of Fraser’s change in ownership – QUIZ operates concessions within the group’s department stores and has used it as a third-party web retailer. Meanwhile, not owning network testing business Spirent Communications detracted after it performed well on the back of technical buying ahead of confirmation of its inclusion in the FTSE 250 index.

The holding in Sinclair Pharma was sold following the bid approach. A new holding in Countrywide was established at a distressed valuation by participating in the emergency refinancing of the estate agency group. An IPO with multi-channel UK specialist value retailer The Works was participated in as their chairman has a proven track record of spotting new retail trends, having built up the Card Factory from a single outlet to a 400-plus chain retailer of value greeting cards, and enjoyed early success as a quoted company. The Works is focused on low-ticket value item with a “must have now” appeal, one example of which would be Squishies, which are fast becoming one of the children’s toy phenomenons of the moment.

Outlook and Strategy: While UK growth has slowed since the EU referendum the economy has continued to expand at a steady pace against the backdrop of a very low unemployment rate and rising wages. The country’s fiscal position has recovered as tax receipts have picked up (in excess of the rate of economic growth) further underlining the resilience of UK plc. Despite their depressed levels of confidence in the general economic outlook, consumers are positive about their personal financial position and the surveys show their confidence to make major purchases (furniture, electrical goods etc.) has improved over recent months. There is evidence from portfolio holdings that consumers are willing to spend. More widely, many more small-cap companies which are delivering good levels of organic growth, sensible bolt-on acquisitions and being underpinned by strong balance sheets are still being found.

### 9.3 Investec

The market environment was challenging for our 4Factor process and the portfolio underperformed its performance comparison index. Each of the four factors underperformed.

Stock picking in the consumer discretionary sector was the biggest drag on relative performance. The large exposure to Casino operator Las Vegas Sands was a significant detractor in the sector as it experienced setbacks both domestically and in Asia, where its Macau casinos were forced to close during Typhon Mangkhut. Also within the sector, the holdings in Lear and Delphi Technologies, both auto parts suppliers, lost value as sentiment toward automotive and related companies suffered from recent trade and environmental concerns. Also, stock-specific setbacks included the cost pressures on Lear from the recently imposed US metal import tariffs, while Delphi faced falling demand from Chinese automakers.

Consumer staples holdings also detracted over the quarter, especially Japanese brewer Asahi, the portfolio’s single largest performance detractor at stock level. Although Asahi continued to see steady growth in its overseas markets, its results were held back by declining demand for beer in Japan. Another detractor in the sector was Chinese pork producer WH Group on concerns a recent outbreak of African swine flu in China will further erode the company’s profit margins.

Stock pricing in the materials sector also detracted due to setbacks with mining giant Rio Tinto and Australian gold metal miner Evolution Mining. Rio’s shares were dragged by concerns over global economic growth and hence demand for industrial metals, while Evolution retreated after cutting its outlook due to lower than expected yields at some of its mines. The holding in Rio Tinto was sold.

There were strong stock picking in the industrials sector which was a significant performance contributor. Two of the sector’s standout performers were Honeywell and Norfolk Southern, which both rallied after reporting very positive earnings.

Honeywell shares were given additional momentum from the positive analyst endorsements over the company's plan to spin off its transportation business.

The portfolio also had success with selected holdings in the healthcare sector, more specifically US firms Cigna, Eli Lilly and Thermo Fisher Scientific, which all comfortably outperformed earnings expectations. As with the industrials sector, returns were given some additional impetus from corporate actions as Eli Lilly announced plans to spin off its lower-margin animal health division.

Not having any exposure to underperforming US social media giant Facebook was the portfolio's most significant stock-level performance contributor.

9.4 **Wellington**

The Global Research Equity Portfolio outperformed the index during the quarter. Positive stock selection in the consumer discretionary and health care sectors outweighed negative selection in consumer staples. Within consumer discretionary, strong security selection in the retailing industry, particularly Amazon.com and TJX Companies, supported relative returns. Amazon continued its 2018 run, rising nearly 18% in the third quarter. The stock price was driven by strong previous quarter results, highlighted by robust growth and sustained profitability. Amazon has established creditability in a broad set of businesses, many of which have ingredients for further growth and success. The fundamentals across Amazon's three key business units: Marketplace, Amazon Prime and Amazon Web Services, remain robust.

TJX Companies is the largest global off-price apparel and home goods retailer, operating the TJ Maxx, Marshalls and Home Goods brands. The stock price advanced during the period on strong adjusted earnings per share. Results were favourable across the board as sales, gross profit, and operating profit all increased year over year. TJX can achieve same stores growth as it captures new customers with thoughtful inventory management, targeted marketing, and excellent execution by a top tier management team. In addition, the company is unique as it has potential to outperform in both offensive and defensive macro environments and will continue to hold the position.

Within healthcare, two Japan-based pharmaceutical companies, Eisai Co and Ono Pharmaceuticals, boosted relative returns. Eisai is a diversified pharmaceutics company. Early in the period the stock price jumped following positive topline results for their Alzheimer's therapy developed in partnership with Biogen. Further development of the therapy remains a key growth catalyst in the stock. A recent immune-oncology collaboration agreement with Merck has also yielded promising data. The position will continue to be held. Ono's stock price began to bounce back following a disappointing previous quarter. The position will be held and confidence remains that Ono's immune-oncology treatment, Opdivo, will play an important role in the first line treatment of numerous forms of cancer.

Stock selection within consumer staples detracted from relative returns. British American Tobacco, the world's second largest cigarette maker, fell during the quarter. A challenging regulatory environment has broadly weighed on tobacco stocks in 2018 which has caused the market to overreact. British American Tobacco continues to push into the next generation technology with its heat-not-burn product, increasing share in key markets. The view is that the company's current valuation does not reflect the potential of the evolving product portfolio. In addition, problem markets are starting to improve, volume declines moderating, and operational efficiencies from the restructuring program coming through. The position will be held.

Baked goods company, Hostess, also detracted from relative returns. The company reported weak quarterly results due in part to decreased promotional support from Walmart, inflationary pressures, and recent acquisitions continuing to drag on profitability. The global brand awareness is liked, significant market share in the sweet baked goods space, unique direct to warehouse distribution strategy, and a strong management team. The position will be held.

Some positioning changes were made within the energy sector, establishing a position in Exxon as well as two exploration and production companies, Concho Resources & Diamondback Energy. Given recent underperformance, it is an opportune time to invest in Exxon as it plans to significantly expand its capex in the coming years, suggesting the long-term growth potential for the company outweighs that of its peers. Exxon's attractive business mix and integration of downstream and upstream activities is liked. A history of thoughtful capital deployment with strong return on common equity also supports the view of the stock. The position in Chevron, which has recently executed well, and that capital was used to build the position in Exxon.

Concho Resources and Diamondback Energy both operate in the Permian Base, the largest shale oil region in the US. Oil drillers in the Permian Basin have underperformed peers that operate in other parts of the country so far this year. The underperformance is largely attributed to a deterioration in sentiment rather than a structural change in long-term fundamentals. It is felt that the Permian Basin has a superior depth on inventory and an enviable position at the bottom of the cost curve, and as a result, Permian names have the potential to offer sustainable growth and free cash flow yields in the years ahead. Concho Resources and Diamondback Energy are well positioned to take advantage of improving sentiment in the region.

Within the industrials sector, a position was established in US-based General Dynamics. The outlook for General Dynamics' defence business is very strong, led by combat systems, marine, and information systems and product technology. Recent results in their aerospace business (Gulfstream) has also been supportive of potential future growth. Harris Corp has been added as a holding, which boasts a strong stable of products including advanced tactical radios, aviation technology, and space intelligence businesses. Their cutting-edge technology is also cost-effective, a combination which could leave them well positioned for contract bids. Their commercial business model, platform approach, and innovative technology are key competitive advantages compared to some larger competitors in this space.

Within healthcare, a position in Koninklijke Phillips was established, a Netherlands-based health technology company focused on healthcare solutions for consumers and healthcare professional. The driver of the thesis rests on continued growth of the Diagnostics & Treatment (D & T) division, which includes image-guided therapy, ultrasound, and diagnostic imaging. The margin expansion is on track in D & T with better manufacturing and new product launches supporting higher gross profit margins. In the biopharmaceutical space a position was established in Assembly Biosciences, which is exploring the cutting edge of hepatitis B therapeutics. Radius was purchased which is a biopharma company with a focus on women's health. The recent launch of their osteoporosis therapy has seen early success in the US market. Radius' pipeline includes a metastatic breast cancer treatment, which could provide upside if trial data is positive. Elsewhere in the sector, a position was initiated in Elanco, an animal health company that operates in both the companion animal and livestock segments. The company, which recently became public, boasts strong fundamentals and has attractive prospects for growth in the companion animal segment.

## 9.5 JP Morgan

After a strong 2017 and first quarter of 2018 when the fund benefitted from the ongoing cyclical recovery in emerging markets, performance since April has been disappointing, albeit performance recovered strongly in September. In summary, USD strength, which pressured EM currencies broadly and vulnerable markets specifically, combined with Russian sanctions and US protectionism to create a 'risk-off' environment from April onwards. As the USD rose further, this turned into broad based selling of the asset class during the third quarter. In this environment cheap stocks were heavily impacted, and the pro-cyclical positioning and a natural value-tilt hurt relative performance.

Growth momentum in emerging markets is slowing, and the belief is that emerging markets are still only mid-cycle within a maturing global cycle. Furthermore, if the USD stabilises emerging equities should expect to perform strongly.

Therefore, the portfolio activity has been focused on rotating holdings towards stocks with the best trends in earnings and adding to domestically orientated consumer businesses, in order to exploit stock level opportunities if the current volatility continues. While some commodity exposure has been trimmed, the portfolio should capture any recovery in markets.

Taiwanese stocks were the biggest detractors from performance, primarily driven by technology stocks. Concerns over weak sales for the latest generation iPhone and a cyclical slowdown in semiconductors weighed on the sector, despite a lack of meaningful downward earnings revisions. There are a number of examples in Taiwan where stock prices are discounting the end of the cycle, yet earnings remain strong. A good example is portfolio holding, Global Wafers, a leading Taiwanese producer of silicon wafers that delivered strong earnings results, has high entry barriers and good order visibility. Nonetheless the stock fell over 20% in USD in August.

Russia and Brazil screen well in the country model due to relatively attractive valuations and growth prospects. Stock section in and an overweight exposure to Brazil was the largest contributor to performance. An improvement in the political mood towards the end of the quarter drove positive equity performance, and the holdings in iron ore producer Vale and steel producer Gerdau contributed. Consumer exposures that have been an area of weakness for the better part of the year also rebounded in September. Stock selection in and an overweight exposure to Russia also helped returns. The equity market rallied as oil prices hit fresh 4-year highs, benefitting portfolio holdings such as Lukoil.

Turkish equities and currency became exceptionally cheap during the quarter, however poor political news flows and a very grudging approach to raising interest rates - the orthodox policy response to a falling currency and large external financing needs - has led us to reduce the overweight position. There is still a small overweight position in this market given the very strong valuation signals and will be limiting the size of overweight so as to manage the country risk. Holdings have been tilted within the country towards weak currency beneficiaries and away from the pure domestic exposure.

The strategy has underperformed driven by stock selection, notably in Asia. During the twelve months, asset allocation and stock selection detracted from returns. As a reminder, superior risk adjusted returns are hoped to be achieved over the long term by using diversified sources of alpha, while maintaining a value bias.

The portfolio continues to be overweight in North Asia and Eastern Europe, which show the best combinations of attractive valuations and positive trends in earnings.

The portfolio has been gradually added to materials since the start of 2016 and this positioning has been the key sector contributor through the twelve months.

Reform markets continue to look expensive. The underweights continue to be those selected reform markets, such as India, Mexico and Philippines, which still stand out as expensive.

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