Corporate Client Update

invesco

April 2018

Market Review Q1 2018

A wild quarter in equity markets
Equities got off to a flying start in 2018 with many of the major benchmark indices recording their best start to a year in over 3 decades. In the US, the S&P 500, DJIA & NASDAQ had all added over 7.5% by the 26th of January with European and Asian indices in close pursuit. Investors were settling in for another year of comfortable gains as the financial press talked of "goldilocks" conditions. Alas if only it were that simple.

Just two weeks later and almost all the gains had been wiped out as higher interest rates in the US spooked investors and led to a return of volatility. The elevated levels of volatility were felt for the remainder of the quarter as stocks (as measured by the S&P 500) advanced or declined by more than 1% in eleven of the 13 weeks of the quarter. To put this volatility into perspective, there were only 13 such weeks recorded in all of 2017.

Financial markets finally felt the Trump threat bite as fears of trade wars drove almost all of the major market indices into negative territory for the quarter. The DAX index was amongst the worst affected losing -6.35% as investors feared trade tariffs could negatively affect the more export-heavy German economy. Tech stock woes also threatened the bull market as fears of a Trump vendetta against Amazon and data leaks at Facebook unsettled investors however the tech heavy NASDAQ clung to a small gain of +2.59%.

Bond bull's time is up
Legendary bond investor Bill Gross sounded the death knell for fixed income markets in early January when he declared the end of the 35-year bond bull market. Citing evidence that 25-year long-term trend lines had been broken in 5yr & 10yr maturity Treasuries as well as the tapering of QE programmes around the world, Gross warned investors that the time of the bond bear had arrived. While we cannot be certain that Gross is correct, we have definitely seen pronounced movements in fixed income markets over Q1. The yield on the 10 Year US Treasury has risen by 33bps to 2.74% while the yield on the German equivalent is also up 7bps to 0.49%.

Dollar struggles continue
One of the big themes of Q1 2018 was the continued weakness of the US Dollar. Despite the widening differential between US & European yields as well as swifter monetary policy movements from the US Federal Reserve, the Dollar has confounded investors by continuing to fall in value compared to its peers. The Greenback finished the quarter down -2.42% & -5.59% against the Euro & Yen respectively.

Volatility makes a comeback
Q1 2018 will be remembered as the period when volatility bit back. 2016 & 2017 were characterised by historically low volatility which lulled investors into a false sense of security. While a traditional strategy to protect an investment portfolio comprises of buying options on the VIX, many asset managers altered their strategies, seeking to benefit from the unusually low volatility environment by selling options on the VIX. While this strategy would have worked well initially, the return of volatility resulted in large losses for these investments. In fact if you had invested this kind of strategy, you would have lost roughly 80% of your money when the VIX spiked by 84% on Monday February 5th, its largest single day increase of all time. The Index finished the quarter at 19.97 up 80.89% since the end of 2017.

Active Managed Fund Highlights

Average Return for Q1 — *-2.7%*

Best Performer for Q1 — *-2.2%*
Friends First

Average Return 1 Year — *0.4%*

Best Performer 1 Year — *1.6%*
Friends First

Best over 3 years — *4.0% p.a.*
Setanta Asset Management

Best over 5 years — *9.8% p.a.*
Setanta Asset Management

Best over 10 years — *7.8% p.a.*
Setanta Asset Management

Key Market Indices – Summary of Returns to 31st March 2018 (in Euro terms)

Asset Class	Q1 %	YTD %	1 Yr %	3 Yrs % p.a.	5 Yrs % p.a.
Cash: 3 Month Euro Bank Deposit	-0.1	-0.1	-0.4	-0.3	-0.1
Government Bonds: ML EMU Gov't > 5 Year Bond Index	2.2	2.2	4.9	0.9	6.1
LT Government Bonds: ML EMU Gov't > 10 Year Bond Index	3.5	3.5	6.9	0.4	8.1
Euro Corp Bonds: ML EMU Corporate Large Cap Bond Index	-0.4	-0.4	1.8	1.6	3.2
Global Equity: FTSE World Index	-3.2	-3.2	0.1	4.0	10.9
Emerging Mkt Equity: MSCI Emerging Markets Index	-0.9	-0.9	9.0	4.4	6.3
Commodities: 50% GSCI + 50% GSCI Non-Energy Index	-2.6	-2.6	-7.3	-7.7	-8.0

Summary of Managed Fund Returns

Active Managed Funds – Summary of Returns to 31st March 2018

Manager	Q1 %	Rank	YTD %	Rank	1 Year %	Rank	3 yrs % p.a.	Rank	5 yrs % p.a.	Rank	10 yrs % p.a.	Rank
Friends First	-2.2	1	-2.2	1	1.6	1	2.0	5	8.6	4=	5.7	6
Merrion Investment Managers	-2.4	2=	-2.4	2=	-0.5	7	-0.6	7	8.0	6=	5.9	4
New Ireland	-3.5	7	-3.5	7	-0.2	6	2.7	2	8.0	6=	5.8	5
Davy Asset Management	-2.7	5	-2.7	5	0.5	3	2.5	3	9.0	2	5.4	7
Setanta Asset Management	-2.4	2=	-2.4	2=	0.3	4	4.0	1	9.8	1	7.8	1
Aberdeen Standard Investments	-3.0	6	-3.0	6	1.0	2	1.2	6	8.8	3	7.2	2
Zurich Life	-2.5	4	-2.5	4	-0.1	5	2.4	4	8.6	4=	6.6	3
Average	-2.7		-2.7		0.4		2.0		8.7		6.3	

Active Managed Funds – Percentage Asset Allocation as at 31st March 2018

Manager	Equities											
	Ireland %	UK %	Europe ex ROI & UK %	North America %	Japan %	Other %	Total %	Fixed Interest %	Property %	Cash %	Alternative Assets %	Total %
Friends First	1.4	2.9	13.7	37.1	6.6	10.7	72.3	26.1	0.0	1.6	0.0	100.0
Merrion Investment Managers	2.0	3.8	19.4	24.0	9.4	3.2	61.9	8.5	3.0	11.6	15.0	100.0
New Ireland	1.9	3.7	25.6	32.1	6.4	8.0	77.7	12.2	4.4	5.7	0.0	100.0
Davy Asset Management	0.0	4.9	16.1	40.8	6.7	2.1	70.7	10.6	11.5	7.2	0.0	100.0
Setanta Asset Management	6.9	10.3	10.2	36.5	1.2	2.4	67.6	12.9	10.2	8.3	1.1	100.0
Aberdeen Standard Investments	1.1	2.8	19.7	35.4	6.6	9.3	74.9	11.4	7.6	6.1	0.0	100.0
Zurich Life	2.0	4.0	12.0	37.0	8.0	7.0	70.0	29.0	0.0	1.0	0.0	100.0
Average	2.2	4.6	16.7	34.7	6.4	6.1	70.7	15.8	5.2	5.9	2.3	100.0

Warning: Past performance may not be a reliable guide to future performance. While every care has been taken in collecting this data from investment managers, it has not been audited or verified for accuracy.

Active Managed Funds – Yearly Performance Figures

2017		2016		2015		2014		2013	
Aberdeen Standard	9.3%	Setanta	12.2%	Merrion	13.6%	Setanta	17.8%	Aberdeen Standard	19.6%
Friends First	8.2%	New Ireland	9.6%	Aberdeen Standard	10.7%	Merrion	16.7%	Setanta	18.5%
New Ireland	7.6%	Zurich Life	6.6%	Davy	10.4%	Davy	16.2%	Merrion	16.3%
Setanta	6.8%	Davy	6.3%	Zurich Life	9.8%	Aviva	16.2%	Friends First/F&C	16.0%
Davy	6.4%	Friends First/F&C	5.2%	Setanta	7.9%	Friends First/F&C	15.1%	Zurich Life	15.9%
Zurich Life	6.1%	Aberdeen Standard	1.1%	Friends First/F&C	7.4%	Aberdeen Standard	15.1%	Davy	15.8%
Merrion	4.4%	Merrion	-0.7%	New Ireland	6.6%	Zurich Life	15.1%	Aviva	15.7%
				Kleinwort Benson	6.4%	Kleinwort Benson	14.5%	New Ireland	15.6%
				Aviva	6.3%	New Ireland	11.9%	Kleinwort Benson	14.7%
Average	7.0%	Average	5.8%	Average	8.8%	Average	15.4%	Average	16.5%

Consensus Funds – Summary of Returns to 31st March 2018

Fund Name	Q1 %	YTD %	1 Year %	3 Yrs % p.a.	5 Yrs % p.a.	10 Yrs % p.a.
Friends First/F&C	-2.5	-2.5	5.0	2.9	9.1	6.7
Irish Life Investment Managers	-2.3	-2.3	0.9	2.8	9.0	6.2
Average	-2.4	-2.4	3.0	2.9	9.1	6.5

Representative Fund Performance

Summary of Returns to 31st March 2018

Fund Name	Type of Fund	Q1 %	YTD %	1 Yr %	3 Yrs % p.a.	5 Yrs % p.a.	10 Yrs % p.a.
Davy Global Equity	Global Equity	-3.2	-3.2	0.3	2.6	9.5	5.3
Friends First/F&C International Equity	Global Equity	-2.8	-2.8	2.3	3.0	10.3	8.0
ILIM Dynamic Global Value	Global Equity (Traditional Value Style)	-4.1	-4.1	-1.8	4.2	11.3	-
KBI GI Dividend Plus Global Equity	High Yield Global Equity	-5.6	-5.6	-3.4	2.7	9.3	9.0
KBI GI Innovator	Alternative Investment Themes/Trends	-5.2	-5.2	-1.5	-0.9	2.6	1.1
Merrion Global Equity	Global Equity	-3.8	-3.8	-2.7	-1.1	8.6	6.7
Merrion High Alpha	Concentrated Absolute Return Fund	0.8	0.8	-0.8	-3.4	5.0	-
New Ireland Consensus IRIS 2022+	Target Date Lifestyle Fund	-1.4	-1.4	2.7	2.7	6.5	4.8
Setanta Dividend Fund	High Yield Equity	-3.0	-3.0	-1.8	4.2	9.8	8.1
Setanta Global Focus Fund	Concentrated Global Equity	-3.6	-3.6	1.3	3.6	9.6	11.3
Aberdeen Standard Investment GARS	Absolute Return Fund	-2.4	-2.4	-0.3	-1.6	1.6	5.0
Aberdeen Standard Global Equities	Global Equity	-6.6	-6.6	-5.1	-0.9	7.9	7.1
Zurich Life 5*5 Global Equity	Concentrated Global Equity	-2.7	-2.7	4.0	3.8	9.3	6.1
Zurich Life International Equity	Global Equity (Rotational Style)	-3.4	-3.4	0.2	3.8	10.6	8.3

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Market Outlook

"The number one rule in investing is never lose money and number two is never forget number one"

Warren Buffet is often referred to as the Godfather of investing and the famous quote from him mentioned above has taken on an almost mythical significance in the investment world. In reality, of all the quotable soundbites that Warren has come out with over the last 60 years, this one is the most ridiculous. There is unfortunately no way to avoid losing money at some point when dealing with investments unless you invest in a truck and park your cash inside. Even then, the value will likely be eroded through the effect of inflation. Buffet himself lost over $20 billion during the 2008 financial crisis. If you are looking for investment rules, some of his less memorable quotes provide much better direction. Long term investing is something he has always championed – "my favourite holding period is forever". As we come into a period of more restrictive monetary policy and rising interest rates – it is hard to see equities delivering the returns of the last 9 years. In fact, it is likely that the market will suffer a significant correction in the near future and it is important to have an asset allocation that, through the benefits of diversification, will offer protection while still allowing for capital gains when the market rebounds. Stock markets go up and down and during the bad times it's easy to be influenced by media histrionics and sensationalist headlines. It is important to not lose sight of your investment goals. An investor who stayed in the market over the last 20 years would have earned good returns, well above inflation levels. However, investors who aim to time markets run the risk of missing out on the best periods which can be very harmful to returns.

Active vs Passive

Although it is impossible to know for sure, the general consensus among economic experts is that we are entering the late cycle of a bull market. Low unemployment, rising interest rates and high stock valuations are characteristics of a late expansionary phase and the global economy is undoubtedly exhibiting many of these traits today. Unfortunately, no one possesses a crystal ball and trying to time the markets to sell out of risky stocks before a crash is a task for the arrogant or foolhardy. After all, the 2017 economy was underpinned by many of these factors at the start of 2017 but the S&P 500 still returned 22%. Truthfully there is no way to know when you are at the end until you arrive there. What we can all agree on is that there is a significant market correction on the horizon and it is important to position your investments accordingly. In these more volatile markets, investors may want to revaluate how they invest their portfolio and as ever, the decision between investing actively or passively will be an important one. Unfortunately, there is no clear answer as the debate between active vs passive is endless with no obvious resolution. With correlations tumbling across financial markets, at an asset class level as well as at a stock specific level – opportunities for active managers to outperform should be plentiful. However, the rise of ETF's has created literally millions of indices and today there are now more indices than stocks. To illustrate how this is possible, if you take 3,000 easily investible stocks, the number of combinations to turn them into an index is a Googol (which is 1 followed by 100 zeros if written). Given the sheer choice of indices, it can be argued that there is no such thing as passive investment any more. So even the decision to invest in a passively managed index tracker requires an active decision at high level. Passive investing has the added advantage of being implementable at a significantly lower cost than paying high fees for traditional active managers.

ESG

You may have heard the acronym ESG at some stage over the last 18 months. Whether it be while attending an investment conference or reading an article in the newspaper or online, a significant amount of time or column inches was likely devoted to the subject. ESG stands for Environmental, Social and Governance factors and there is an increasing emphasis being placed on incorporating these factors into your investment process. Along with empirical research on how it can affect performance, there will be a regulatory requirement (IORP II) effective as of January 2019 for pension fund trustees to adjust their Statement of Investment Principles to state how they have taken ESG factors into consideration and the SIPP will need to outline the decision-making process and the long-term effect of these decisions on the investment portfolio. The investment consulting team at Invesco undertook a project in Q4 2017 to learn more about ESG factors and their potential implications on performance and risk in an investment portfolio. We invited a number of managers in to present on the topic and conducted our own due diligence. While empirical research on how ESG factors affected performance was in-conclusive, the majority of experts agreed that incorporating ESG factors in your investment strategy can help to identify lower risk companies which are better managed and have a longer-term focus. On the other hand, ignoring ESG factors can lead to worse performance due to the risks of controversies such as fraud, labour strikes and other governance irregularities. These risks can create more volatility and increase the cost of capital which could detract from performance.

It is our opinion that it is only a matter of time before ESG investment becomes completely mainstream. There is an increasingly wide acceptance that investment decisions should be made not just for financial gain but equally in consideration of their long-term impact on society. Many of the asset managers we met spoke of the increasing interest from the majority of their clients but a hesitancy to make the transition. We feel that with the onus of fulfilling IORP II and potential evidence of outperformance or at the very least equal performance of ESG products, there will be a shift in the investment landscape towards sustainable investments.

For further information please contact:

Bronagh Traynor (btraynor@invesco.ie)
Finian O'Driscoll (fodriscoll@invesco.ie)

Dublin 2 Sandyford Business Centre, Burtonhall Road, Sandyford, Dublin 18, Ireland
tel +353 1 294 7600 fax +353 1 294 7633

Cork No. 6 Lapp's Quay, Cork, Ireland
tel +353 21 480 8041 fax +353 21 431 0530

web www.invesco.ie email info@invesco.ie

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