Corporate Client Update

October 2017

Market Review Q3 2017

Record highs on Wall Street
Q3 2017 saw all of the major US Equity indices reach new peaks as investors chose to ignore potential risks to the economy and dance while the music's still playing. Helped by a weaker dollar, the DJIA, NASDAQ Comp & S&P 500 all climbed over 4% as they continued to break new highs. The DJIA, for example, has now closed at all-time highs 42 times this year alone while the S&P has managed the feat 39 times. This sounds impressive and if you listen to Donald Trump – you might believe that it's all down to him but that's never a good idea. A weaker dollar has contributed to this positive momentum over the quarter having depreciated 3.65% against the Euro. Allayed to this, after decades of ultra-loose monetary policy, valuations are near all-time highs with their sustainability at these levels a concern amongst investors.

European stocks not too far behind
European stocks also moved higher over the quarter as the stronger Euro could only temporarily halt the momentum of the major indices. The FTSE World in Euro terms climbed +1.36%. The FTSE Eurofirst 300 Index added +2.68% while the CAC 40 rose +4.28% making it the best performing major European index in Q3. Interestingly, the ISEQ Overall Index rallied late in the quarter to post +1.17% having struggled for much of the period due to poor performing financials and Ryanair, which spent the latter end of the quarter embroiled in controversy over flight cancellations.

Large gains in Asia
In Asia, performance was positive. Japan's Nikkei 225 index rose +2.34%, helped by a weaker Yen. China's Hang Seng index of Hong Kong listed shares rose +8.61% while China's Shanghai Composite index was up +4.90%.

Little change in fixed income
The start of the quarter saw global bond yields rise significantly as central bank officials became more hawkish in their rhetoric. In the first few weeks of July, the German 10 Year bond yield rose to 0.60% while the equivalent US treasury peaked at 2.40%. Since then however, increased geo-political tensions arising from the war of words between Donald Trump & Kim Jong Un and economic uncertainty arising from the spate of natural disasters to hit the globe over the quarter have driven yields lower. The German 10 year remained broadly flat at 0.46% while the US 10 yield finished at 2.33%.

The notable exception has been in the UK. With inflation in the UK coming in at 2.9% in August, the September BOE meeting raised the possibility of an interest rate hike before the end of the year igniting a rally in the GBP and producing a spike in the 10-year Gilt yield. The yield climbed 0.32% from September 7th to finish the quarter at 1.37% while the GBP currency rallied in September to finish just 0.35% lower against the Euro.

Volatility at all-time lows
September has historically been the most volatile month of the year but there has been no sign of any volatility this year. The VIX index finished the quarter at 9.51 which was the lowest ever monthly closing value.

Natural disasters boost commodities
Texas, Mexico, Florida, Puerto Rico and Japan were all hit by strong hurricanes in Q3. The supply demand factors resulting from these natural disasters helped to raise oil prices back well above $50. The price of Brent Crude Oil rose +20.39% over the quarter to $57.57 per barrel.

Active Managed Fund Highlights

Average Return for Q3	*1.3%*
Best Performer for Q3 *Merrion Investment Managers*	*2.1%*
Average Return 1 Year	*9.1%*
Best Performer 1 Year *New Ireland*	*11.0%*
Best over 3 years *Setanta Asset Management*	*10.3% p.a*
Best over 5 years *Setanta Asset Management*	*12.3% p.a.*
Best over 10 years *Setanta Asset Management*	*6.3% p.a.*

Key Market Indices – Summary of Returns to 30th September 2017 (in Euro terms)

	Q3 %	YTD %	1 Yr %	3 Yrs % p.a.	5 Yrs % p.a.
Cash: 3 Month Euro Bank Deposit	-0.1	-0.3	-0.4	-0.2	-0.1
Government Bonds: ML EMU Gov't > 5 Year Bond Index	0.8	-0.6	-5.3	3.6	6.5
LT Government Bonds: ML EMU Gov't > 10 Year Bond Index	0.8	-1.8	-8.8	4.8	8.2
Euro Corp Bonds: ML EMU Corporate Large Cap Bond Index	1.1	1.8	0.5	2.5	3.9
Global Equity: FTSE World Index	1.4	4.6	13.3	10.5	13.0
Emerging Mkt Equity: MSCI Emerging Markets Index	4.2	14.3	16.8	7.6	6.1
Commodities: 50% GSCI + 50% GSCI Non-Energy Index	-1.0	-11.3	-2.2	-10.2	-9.6

Summary of Managed Fund Returns

Active Managed Funds – Summary of Returns to 30th September 2017

Manager	Q3 %	Rank	YTD %	Rank	1 Year %	Rank	3 yrs % p.a.	Rank	5 yrs % p.a.	Rank	10 yrs % p.a.	Rank
Davy Asset Management	0.4	7	2.4	7	6.9	7	8.1	3	10.4	4	3.7	6
Friends First/F&C	1.3	3=	4.7	2	9.2	4	7.2	6	10.1	6	3.5	7
Merrion Investment Managers	2.1	1	3.1	6	8.6	6	6.9	7	10.3	5	4.6	4
New Ireland	1.1	6	4.1	3	11.0	1	7.5	5	9.8	7	4.0	5
Setanta Asset Management	1.3	3=	3.8	4=	8.9	5	10.3	1	12.3	1	6.3	1
Standard Life Investments	1.4	2	6.5	1	9.5	2=	7.6	4	10.9	2	5.3	2
Zurich Life	1.2	5	3.8	4=	9.5	2=	8.3	2	10.5	3	5.1	3
Average	1.3		4.1		9.1		8.0		10.6		4.6	

Active Managed Funds – Percentage Asset Allocation as at 30th September 2017

	Equities											
Manager	Ireland	UK	Europe ex ROI & UK	North America	Japan	Other	Total	Fixed Interest	Property	Cash	Alternative Assets	Total
Davy Asset Management	0.0	4.6	15.7	40.0	6.1	2.2	68.5	10.6	11.7	9.2	0.0	100.0
Friends First/F&C	1.4	4.0	14.5	35.9	5.5	10.6	71.8	26.6	0.0	1.6	0.0	100.0
Merrion Investment Managers	2.7	3.8	23.6	25.4	9.7	3.8	69.0	7.7	2.8	6.5	14.1	100.0
New Ireland	1.7	3.7	26.3	33.4	6.2	6.8	78.1	13.6	4.1	4.2	0.0	100.0
Setanta Asset Management	7.7	9.5	10.6	36.7	0.9	2.6	68.0	11.5	9.4	10.1	1.1	100.0
Standard Life Investments	1.4	2.7	20.2	32.1	6.8	10.3	73.5	12.0	7.2	7.3	0.0	100.0
Zurich Life	6.0	5.0	18.0	28.0	6.0	6.0	69.0	30.0	0.0	1.0	0.0	100.0
Average	3.0	4.8	18.4	33.1	5.9	6.0	71.1	16.0	5.0	5.7	2.2	100.0

Active Managed Funds – Yearly Performance Figures

	2016		2015		2014		2013		2012
Setanta	12.2%	Merrion	13.6%	Setanta	17.8%	Standard Life	19.6%	Standard Life	17.5%
New Ireland	9.6%	Standard Life	10.7%	Merrion	16.7%	Setanta	18.5%	New Ireland	16.1%
Zurich Life	6.6%	Davy	10.4%	Davy	16.2%	Merrion	16.3%	Merrion	16.0%
Davy	6.3%	Zurich Life	9.8%	Aviva	16.2%	Friends First/F&C	16.0%	Davy	14.5%
Friends First/F&C	5.2%	Setanta	7.9%	Friends First/F&C	15.1%	Zurich Life	15.9%	Setanta	14.2%
Standard Life	1.1%	Friends First/F&C	7.4%	Standard Life	15.1%	Davy	15.8%	Kleinwort Benson	13.5%
Merrion	-0.7%	New Ireland	6.6%	Zurich Life	15.1%	Aviva	15.7%	Friends First/F&C	13.1%
		Kleinwort Benson	6.4%	Kleinwort Benson	14.5%	New Ireland	15.6%	Aviva	13.0%
		Aviva	6.3%	New Ireland	11.9%	Kleinwort Benson	14.7%	Zurich Life	12.9%
Average	5.8%	Average	8.8%	Average	15.4%	Average	16.5%	Average	14.5%

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.

Consensus Funds – Summary of Returns to 30th September 2017

Fund Name	Q3 %	YTD %	1 Year %	3 Yrs % p.a.	5 Yrs % p.a.	10 Yrs % p.a.
Friends First/F&C	2.4	6.0	10.3	8.6	10.8	4.8
Irish Life Investment Managers	1.4	4.2	9.7	8.4	10.8	4.5
Average	1.9	5.1	10.0	8.5	10.8	4.7

Representative Fund Performance

Summary of Returns to 30th September 2017

Fund Name	Type of Fund	Q3 %	YTD %	1 Yr %	3 Yrs % p.a.	5 Yrs % p.a.	10 Yrs % p.a.
Davy Global Equity	Global Equity	0.5	4.0	11.3	8.5	11.1	3.0
Friends First/F&C International Equity	Global Equity	1.8	6.2	12.8	8.9	12.0	5.4
ILIM Dynamic Global Value	Global Equity (Traditional Value Style)	1.1	4.1	11.6	11.9	14.0	-
KBI GI Dividend Plus Global Equity	High Yield Global Equity	1.2	1.2	11.0	8.4	12.2	6.6
KBI GI Innovator	Alternative Investment Themes/Trends	1.7	5.4	9.8	3.0	4.3	-0.2
Merrion Global Equity	Global Equity	1.9	2.1	10.4	7.8	11.4	4.8
Merrion High Alpha	Concentrated Absolute Return Fund	1.0	-0.9	1.2	4.4	6.3	-
New Ireland Consensus IRIS 2022+	Target Date Lifestyle Fund	1.5	3.5	5.0	5.1	7.7	2.7
Setanta Dividend Fund	High Yield Equity	0.9	3.5	10.0	9.4	12.8	6.5
Setanta Global Focus Fund	Concentrated Global Equity	4.2	6.0	13.3	11.3	12.8	9.3
Standard Life GARS	Absolute Return Fund	-0.8	0.1	1.8	0.3	2.7	4.8
Standard Life Global Equities	Global Equity	1.0	4.7	10.0	6.8	11.3	5.2
Zurich Life 5*5 Global Equity	Concentrated Global Equity	2.7	5.9	16.3	9.1	10.9	4.2
Zurich Life International Equity	Global Equity (Rotational Style)	1.7	5.1	13.7	10.4	12.6	6.0

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Market Outlook

Briefly outlined below are some of the key considerations for pension scheme members with respect to the outlook for the economy, monetary policy and financial markets.

The Great Unwind

The September 20th meeting of the US Federal Reserve proved to be a historic moment in post-crisis economic history. After years of accommodative monetary policy, US Fed Chair Janet Yellen announced that the Fed will begin to reduce its multi-trillion dollar balance sheet starting in October. The ECB and BOE have also signalled their intentions to begin tapering their quantitative easing (QE) programs. Since 2009, central banks around the globe have engaged in mass purchasing of government debt in a bid to prop up their ailing economies. Consequently, major central bank assets have almost quadrupled to over $14 trillion and we have been left with an artificially inflated economy. The "Great Unwind" as it is now being dubbed poses a threat to the economy and is potentially a leading candidate for creating a new financial crisis. Central banks are acutely aware of the impact accommodative policy has had on markets and the path to normalisation will be protracted in order to protect investors. However there is likely to be some bumps on the road and investors need to be aware of the possibility of short-term volatility and potentially significant drawdowns as we move away from an era of QE.

In their interim economic outlook report, the Organisation for Economic Co-operation and Development (OECD) stressed the risks that lie ahead for central bankers. ***"Authorities face a difficult balancing act in continuing to provide support while managing financial stability risks. The long period of low interest rates has boosted asset price valuations and created financial distortions that will be testing to resolve".***

Heightened Political Risk

The 3rd quarter of 2017 was notable for many reasons, chief among them was the dispute that developed between US President Donald Trump and his North Korean counterpart Kim Jong Un. In response to news that North Korea had developed improved nuclear warheads, Trump threatened North Korea with "fire & fury like the world has never seen". Relations soured further towards the end of the quarter with both guilty of childish name calling. Markets generally shook off this strain in Q3 however it is important for investors to be aware of the potential risks associated with escalated political tensions. Although we are still likely far from any military conflict – lessons can still be learnt about the importance of diversification so that your investments can perform well regardless of the outcomes on the Korean peninsula.

Closer to home, Eurozone integration remains a major priority for the leaders of the European Union. Emmanuel Macron and Angela Merkel have been outspoken in their belief that the EU needs to focus on deeper integration and strengthening relationships in a bid to stave off future crises. While the threat of populism appeared to be averted with Macron's victory in France, Merkel's recent poor performance in the German elections, the rising anti-EU "5 Star" movement in Italy and the violent events of the Catalan independence referendum threaten Europe's political stability just as the economy appears to be turning the corner.

Rising Yields

Along with selling off their massive bond portfolios, central banks have also begun the process of raising interest rates. The Fed has now raised the target rates 4 times in the last 22 months and has signalled the intention to continue to do so while offloading its massive balance sheet. These rate hikes are likely to lead to an upward shift in the yield curve across all maturities which will affect bond returns in the short to medium term. We are also beginning to see some evidence of this in European markets as all of the major ML Eurozone Government Bond indices are negative YTD. The ML > 10 Year EMU AAA/AA Index has lost over 8% in the last 12 months as yields have begun to creep upwards. This a good example of the heightened risks associated with longer duration bond funds. It may be time for investors to consider their interest rate exposure in a rising interest rate environment.

Bonds will still form an important part of portfolios for return generation and diversification purposes. Despite the current environment for bond yields, long term bonds remain the best match for those investors looking to target purchasing a pension at retirement or for pension schemes looking to match their pension scheme liabilities.

The Investment Dilemma

There is no doubt we are entering a difficult period for investors. As financial markets wean themselves off quantitative easing, it is hard to see equity markets delivering the returns of the last 8 years. However, as we enter a new era of central bank policy, new opportunities are likely to arise. The last 9 months have seen correlations tumble across financial markets. On a broad level, asset classes are starting to move independently of each other and on a stock specific level, the correlation between individual stocks is dropping. Morgan Stanley analysts estimate the correlation between the constituents of the S&P 500 is at 18%, one of its lowest levels since 2004, down from 60% last year. This should provide the perfect environment for active managers to demonstrate their skill. Absolute return fund managers appear to be benefitting from the "correlation collapse" this year with many posting positive returns.

As we stress every quarter, the most important thing for members of a pension scheme is to align oneself to the most appropriate fund given one's willingness and ability to take risk, time to retirement and overall retirement goal.

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