Growth-Focused SEI Strategic Portfolios

SEI Strategic Portfolios:

Q4 2016 Quarterly Commentary

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Equities rally while fixed income markets fall following the US presidential election; Growth-Focused SEI Strategic Portfolios deliver strong returns in Q4 2016

Executive Summary

- The fourth quarter of the year delivered a mixed set of returns across asset classes as investors considered the impact of the US presidential election on the global economic landscape. Fixed income yields rose over the period, providing a meaningful headwind to securities with higher levels of interest rate sensitivity. Meanwhile, equity markets pushed on, reflecting the growing sense that the global economy will continue to move forward, if not potentially modestly accelerate.

- The equity investments primarily utilised in the Growth-Focused SEI Strategic Portfolios (the Core, Balanced, Growth and Aggressive Funds, collectively "the Funds") broadly outperformed their benchmarks (Sterling Institutional share class, in GBP, net of all fees) in Q4 2016; an bias towards managers with valuation-focused strategies was the key driver of returns across numerous investments, adding to strong returns for these funds in 2016, placing them at the top quarter (excluding the Core Fund) of their respective Lipper peer groups.

- Global diversification has also been a key contributor to returns for the Growth-Focused SEI Strategic Portfolios in 2016; ongoing weakness in Sterling has meant that the value of non-UK assets, as well as companies with a significant portion of their revenue outside of the UK, has risen sharply over the course of the year, providing a further tailwind to overall returns in these Funds.

- As a result, 2016 overall was a year where the Growth-Focused SEI Strategic Portfolios delivered returns that provided a step forward for Fund investors with growth-focused investment objectives, which at the end of the day is what investing should be all about; the disciplined pursuit of goals despite ongoing market noise, distraction from headlines and ever-present economic and political change.

Market Overview

- The final quarter of 2016 offered several landmark developments: a surprise outcome to a sharp-elbowed US presidential election handed firm control of the federal government to Republicans, bolstering a rally in equities and a downturn in bond markets; the UK's Brexit timeline and negotiating posture evolved from abstract to relatively firm; and the oil price recovery found solid footing as oil producing countries agreed to cut production.

- Major central banks made headlines, most notably with the Fed's rate increase and firmer policy-tightening projections for 2017. US labour market conditions improved as the unemployment rate decreased to 4.6% in November, while US consumer prices rose by 1.7% in the year-over-year. The final release of GDP revealed the US economy grew at a 3.5% annualised rate in the third quarter, stronger than prior estimates and a significant improvement over the second quarter's 1.4% growth.

- The ECB announced an extension of its asset purchase programme, further loosening its monetary policy stance. Eurozone inflation hit 1.1% in December, the highest annual rate in more than three years. Manufacturing data strengthened in December, indicating sharp improvements in output, new orders and employment. The latest third quarter GDP reading revealed 0.3% growth, in line with prior estimates and equalling second quarter growth.

- The BOE announced no changes while Governor Mark Carney quashed rumours of his resignation. The UK unemployment rate dipped to 4.8% in October, markedly lower than the 5.2% rate from a year earlier and the lowest level since September 2005. Year-over-year consumer prices in the UK climbed to 1.2% in November, the highest level since October 2014. Third quarter economic growth expanded in its final estimate, reaching 0.6% for the period.

Selected Asset Class Commentary

- Global Developed Equity Asset Class: Rising interest rate expectations, robust US economic data, solid oil prices alongside expected tax cuts, infrastructure spending and financial deregulation following the US election outcome drove US earnings and inflation expectations higher, all good news for the beaten down financials but not for richly priced consumer staples and utilities. Biased towards valuation-focused managers, which all outperformed, the Funds' investments in the asset class participated strongly in the last quarter's rebound. Although momentum-biased INTECH Investment Management and Jennison Associates lagged, the negative bias towards these managers greatly reduced their negative impact on performance.

- UK Equity Asset Class: UK equity markets ended the year in a rally amid Trump's US presidential election victory. A preference for cyclicals over defensives added value over the final quarter, while an underweight to major oil companies detracted. Jupiter Asset Management was the top contributing manager within the Funds' investment for the quarter. Los Angeles Capital Management detracted due to its momentum overweight and underweights to value and mega-sized companies. SEI expects European markets to remain volatile amid prolonged uncertainty created by the Brexit vote, the European elections and continuing concerns about the health of European banks.

- Emerging Markets Equity Asset Class: Emerging Markets lagged the developed world for the second month in a row. Energy prices continued to rise as OPEC committed to production cuts. Asset Class holdings in Consumer Staples and Financials bolstered results for the quarter. RWC Asset Advisors was the top-performing manager, and benefited from strong stock selection in Russia. PanAgora Asset Management had strong selection in India and Taiwan. JO Hambro Capital Management's selection in Latin America detracted.

Manager Changes

- SEI removed AllianceBernstein from the investment used to access the US Small Companies asset class as at 30 November 2016. The investment is shifting assets in a defensive direction, and AllianceBernstein's higher exposure to volatility contradicts this objective. In addition, AllianceBernstein has struggled to keep pace with its benchmark. Finally, the strategy's large asset base and evolving team structure have dampened our expectations for its future performance. A large asset base can be particularly unwieldy to manage in the small-company universe. AllianceBernstein remains an investment manager in other SEI funds. SEI is confident in AllianceBernstein's abilities and does not anticipate additional changes.

Rice Hall James & Associates (Rice Hall James) has been added to the investment used to access the US Small Companies asset class, as at 30 November 2016. Rice Hall James' investment team focuses on growth sustainability over absolute growth rates and invests within a multi-bucket framework in an effort to create an allweather “core” growth portfolio. The portfolio’s two co-managers are experienced investors in the small company space and have worked together for 16 years.

Outlook

- Two key aspects are most pressing on investor sentiment as we look forward in 2017; the detail of emerging US policy under the new administration and potential European political instability given pending elections in key Eurozone nations. Regarding the former, SEI expects the new US President to break down disincentives to hiring, bank lending, new business formation and investment, leading to higher growth, earnings and profitability, as well as higher inflation. On balance, tax and regulatory reform increase SEI’s optimism that economic growth will accelerate, while up-ending trade agreements and confronting China, could be dangerous unless those changes are nuanced and focused, characteristics that have not been in evidence up to this point.

- Bond yields have soared in the aftermath of Trump’s election victory, reflecting a pronounced rise in inflation expectations. Inflation in the US has been percolating beneath the surface for a while, hidden by a combination of dollar strength and energy price weakness. If the Federal Open Market Committee forecast assumes that real GDP growth will be constrained as the economy approaches full employment, one can question whether inflation can indeed be contained at or below 2%.

- Across the Atlantic, general elections will be held in the Netherlands, France and Germany in 2017. The French presidential elections would seem to have the greatest importance for investors. French voters are facing a binary decision: Thatcherite conservatism that promises to undo a portion of the welfare state but has the potential to be very positive for the French economy or a gamble on economic nationalism that could lead to the unravelling of the euro currency framework. Brexit negotiations will begin when Article 50 is invoked in March; in the meantime, the recent better economic numbers offer a welcome respite.

- Emerging markets had a negative reaction to the Trump election. Concerns about the new administration’s stance on trade and resumption of the dollar’s appreciation are the main factors for the setback. If emerging markets are to outperform their developed market counterparts on a sustained basis, the world needs to see a major step-up in economic growth and global trade. Faster growth in the US certainly helps, but the maintenance of open markets and strong trading relationships are also crucial.

- SEI believes the central global economic scenario remains one of continued global economic growth and reflation, potentially modestly strengthening compared to 2016. Positioning along these lines has played out well for the Growth-Focused SEI Strategic Portfolios in 2016 and major adjustments are unlikely. As we look forward, SEI may make some adjustment within the funds in which the Strategic Portfolios invest to the bias towards managers with valuation-focused strategies as this trade continues to play out, perhaps in favour of managers with trend-following managers.

- As is always the case, uncertainty creates opportunity for active management and SEI would suggest that investors continue to apply a strategic approach to the core of their portfolios, conducting their investment activities with a discipline that seeks to ignore short term volatility and avoid knee-jerk reactions, while remaining on the ultimate objective: the achievement of their financial goals.

Important Information on Performance

Past Performance is not a guarantee of future performance. Standardised performance is available upon request. All data is as at 31 December 2016.

Asset class performance discussed is based on the majority SEI fund underlying the asset class. This does not include analysis of the manager pools, hedged share class investments within SEI Funds, additional SEI funds or any third-party funds within the Strategic Portfolios. As a result, performance for the total asset class allocation may vary. Not all asset classes discussed are included in all Strategic Portfolios. All asset class comparative performance is relative to the benchmark of the specific SEI fund representing the majority of the asset class investment.

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- Absolute return investments utilise aggressive investment techniques which may increase the volatility of returns. If the correlation between absolute return investments and other asset classes within the fund increases, absolute return investments' expected diversification benefits may be decreased.
- International investments may involve risk of capital loss from unfavourable fluctuation in currency values, from differences in generally accepted accounting principles or from economic or political instability in other nations.

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