SEI New ways. New answers.®

Equities Advance to Start the Second Half

Monthly Snapshot

- A thaw in EU-US trade tensions appeared possible following late-month negotiations, while the EU and Japan finalised a major deal eliminating most tariffs. The imposition of tariffs still threatens to envelop US-China commerce.
- Shares generally advanced in developed and emerging markets alike as volatility receded. Government bond yields climbed in an environment defined by the slow removal of accommodative central-bank policies (yields move inversely to prices).
- The economic fundamentals that drive equity markets still appear solid, even in places like Europe and developing economies. Interest rates—while higher—are still at levels that support global economic growth.

Economic Backdrop

The second half of 2018 began with mixed progress on the global thematic landscape. Trade barriers, which escalated through the beginning of July and still threaten to envelop US-China commerce, appeared set for substantial relief between the US and EU following a successful late-month negotiation by US President Donald Trump and European Commission President Jean-Claude Juncker. The EU and Japan also finalised a major trade deal in mid-July that eliminated most tariffs between the two trading partners.

The Western alliance suffered a setback as President Trump declared the EU a "foe" on trade and called into question the pact's core mutual-defence principle following a North Atlantic Treaty Organization summit in Brussels. A one-on-one meeting between the US president and Russian President Vladimir Putin raised concerns across the political spectrum—particularly after a subsequent press conference in which Trump second-guessed US intelligence agencies' unanimous assessment of Russia's interference in the 2016 US elections.

UK Prime Minister Theresa May ruled out the possibility of allowing Northern Ireland to remain in the EU's customs union or single market in a bid to please pro-Brexit conservatives—but held out the prospect of harmonising the entire UK trade regime with remaining member states. The EU's chief Brexit negotiator, Michel Barnier, rejected a key component of May's plan that sought to have each region collect trade duties on the other's behalf. May's foreign and Brexit secretaries resigned early in the month after they deemed her final negotiating proposal too soft.

The Bank of England's Monetary Policy Committee increased its benchmark interest rate at the beginning of August in an effort to dampen inflation pressures; in a late-July meeting, the European Central Bank (ECB) reaffirmed its policy-path commitment to taper asset purchases over the remainder of 2018. The US Federal Open Market Committee refrained from taking additional action on the first of August after increasing the federal funds rate in June. The Bank of Japan maintained its near-zero target rate, but set its band at -0.2% to 0.2% (an increase of 0.1%) at the end of July.

Key Measures: July 2018

EQUITY		
Dow Jones Industrial Average	4.83%	↑
S&P 500 Index	3.72%	↑
NASDAQ Composite Index	2.19%	↑
MSCI ACWI Index (Net)	3.02%	↑
BOND		
Bloomberg Barclays Global Aggregate Index	-0.17%	↓
VOLATILITY		
Chicago Board Options Exchange Volatility Index PRIOR: **16.09**	12.83	↓
OIL		
WTI Cushing crude oil prices PRIOR: **$74.15**	$68.76	↓
CURRENCIES		
Sterling vs. US dollar	$1.35	↑
Euro vs. US dollar	$1.19	↑
US dollar vs. yen	¥111.91	↑

Sources: Bloomberg, FactSet, Lipper

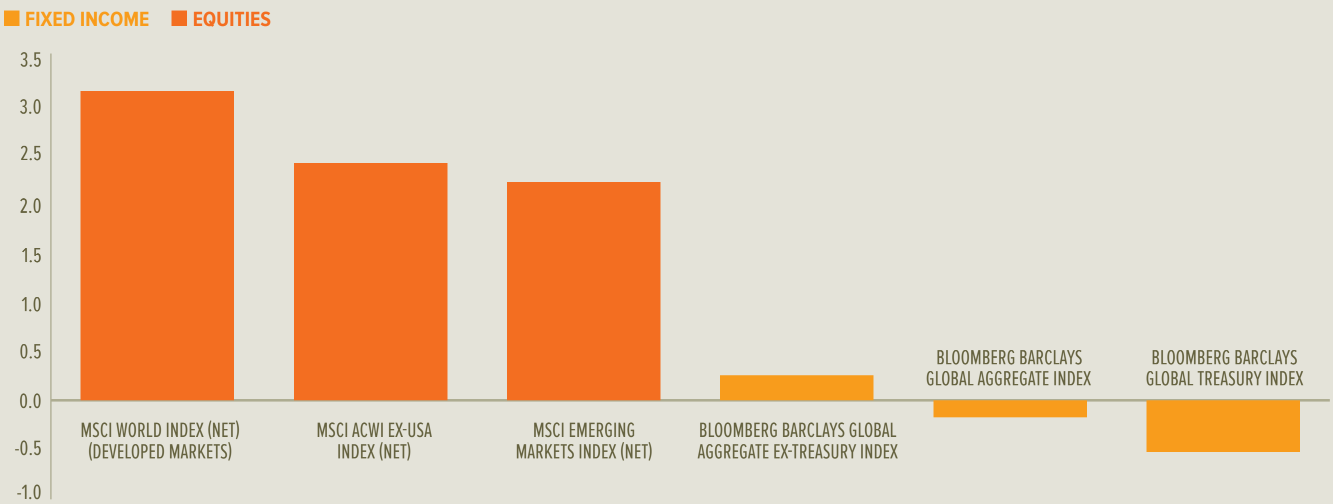
British and European shares climbed slowly throughout July, while US equities advanced for most of the month before retreating in the last week. Japanese shares increased early in the month, holding onto gains thereafter. Equities in Hong Kong, mainland China, Brazil and Mexico also generally advanced during July. Stock-market volatility was fairly subdued the world over, settling from an early-month peak. Shorter-term UK gilt yields increased and longer-term yields were mixed, while yields on euro-area and US government bonds increased similarly across all maturities.

UK sales volumes pointed to firm retail demand in July, according to a distributor survey, but were down from elevated June findings. Industrial trends were similar, with generally favourable survey results for July that were nevertheless just shy of the prior month. Consumer prices were unchanged in aggregate during June, causing the year-over-year increase to hold at 2.4%; producer prices increased by 10.2% (for inputs) and 3.1% (for outputs) from a year earlier.

Eurozone manufacturing activity appeared set for solid continued expansion in July, according to an early survey, while services growth slid to still-respectable levels. Unemployment dropped to 9.1%, the lowest level in the eurozone since February 2009. Gross domestic product (GDP) slipped to 0.3% for the second quarter and 2.1% for the year-over-year period. Despite somewhat disappointing GDP growth, the eurozone economy remains relatively healthy.

Preliminary surveys pointed to accelerating US manufacturing growth and a strong continued expansion in services activity during July. Home sales declined in June, marking the third-straight month of lower existing home sales and the lowest rate of new-home sales since February. The initial estimate of second-quarter GDP showed that US economic growth accelerated to an annualised 4.1% rate due to strong consumer spending and exports.

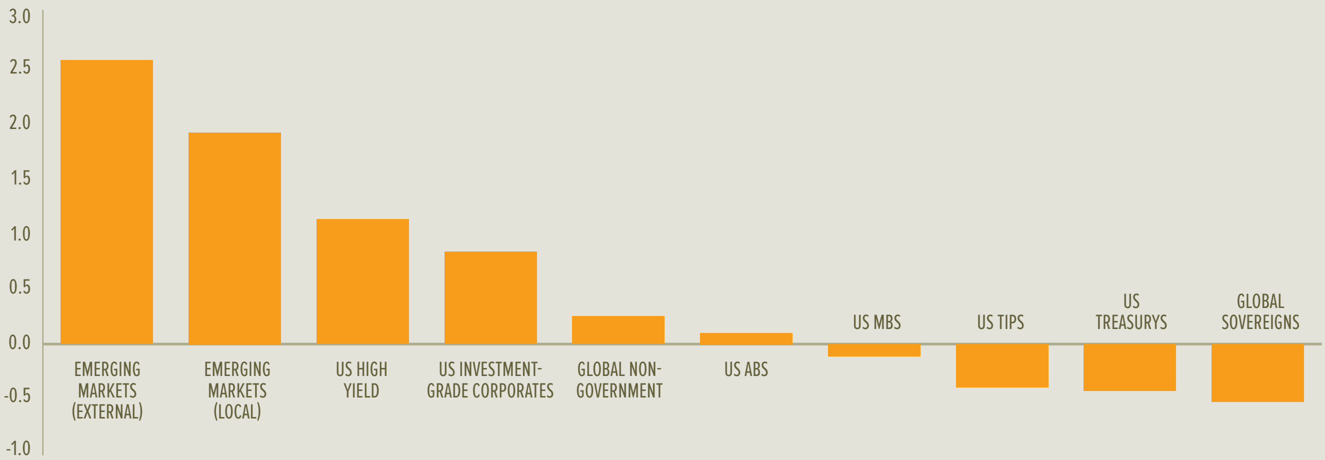
Major Index Performance in July 2018 (Percent Return)



Sources: FactSet, Lipper. See "Corresponding Indexes for Major Index Performance Exhibit" in the Index Descriptions section for more information.

All references to performance are in US dollar terms unless otherwise noted. See Standardised Performance for more information.

Fixed-Income Performance in July 2018 (Percent Return)



Sources: FactSet, Lipper. See "Corresponding Indexes for Fixed-Income Performance Exhibit" in the Index Descriptions section for more information.

Our View

Investors were raging bulls at the beginning of 2018 as equity prices vaulted higher. But that optimism faded dramatically as the news flow turned less favourable. As far as we're concerned, that's okay—because the potential for a meaningful advance in equities is greater when investors are pessimistic and bad news is already largely discounted in the price of riskier assets.

If one believes, as we do, that the global economy is sound and that the political uncertainties currently roiling markets will be contained, then the proper course (in our view) should be to remain exposed to equities and other risk assets and ride out the short-term ups and downs.

The economic data coming out of Europe has been hugely disappointing this year. Instead of building upon the improved business activity of 2016 and 2017, there has been a widespread deceleration. At SEI, we have been reluctant to get too bearish on Europe's fundamentals, but there's no denying that financial-market participants are disbelievers. Analysts' 2018 and 2019 earnings-growth estimates for the companies within the MSCI EMU (European Economic and Monetary Union) Index are quite low compared to those of other major regions and countries.

ECB President Mario Draghi and other bank governors decided to conclude net asset purchases by the end of this year because they view deflation risks as having moderated significantly. Since the ECB will no longer be a price-insensitive buyer of eurozone debt, we could see yield spreads rise as investors demand a risk premium for those countries with a heavy debt burden relative to the size of their economy. Italy's new government wants to institute several expensive propositions that would blow a hole in the government's budget, likely causing the country's bonds to be further discounted by investors—with other periphery countries' bond yields rising in sympathy (yields move inversely to prices).

We would not be surprised to see further downside volatility in sterling as we draw closer to the EU exit date.

Recent UK economic data reports, like those of other countries in Europe, suggest that Great Britain is wending its way through a soft patch. Underlying growth nevertheless appears solid, indicating the UK economy is in stable condition; although the trade sector looks to be a problem spot.

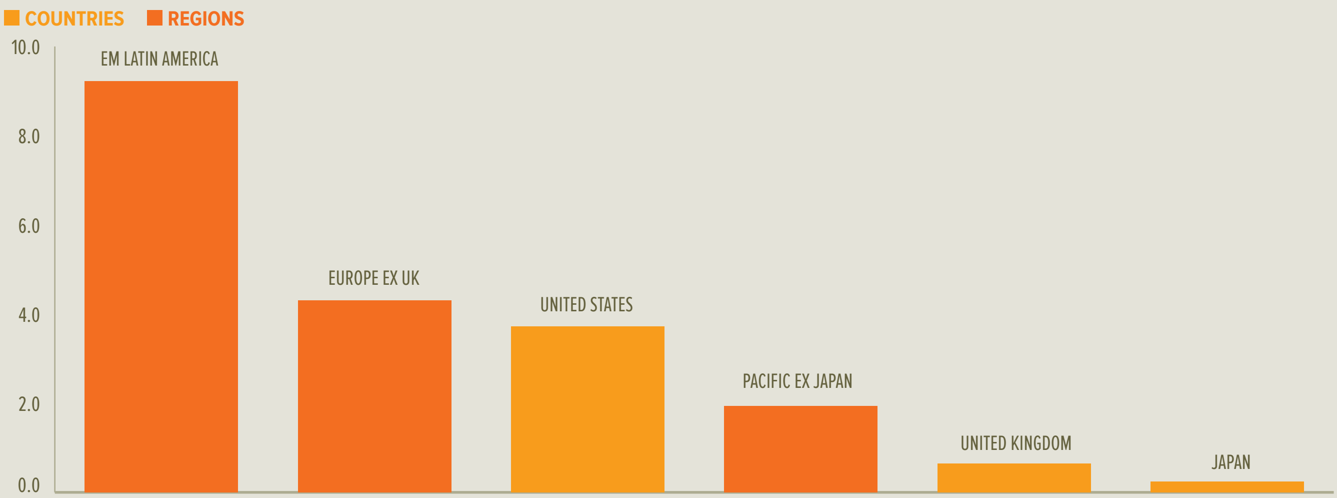
The biggest source of uncertainty facing the UK is its looming withdrawal from the EU. The Conservative Party's internal fight over the country's future relationship with the EU has stalled progress toward a clear post-Brexit status. Maybe it's sheer coincidence, but sterling versus the US dollar is almost where it was the day after the Brexit vote on 23 June 2016. The recent trend has been to the downside, as currency-market participants worry about the rising odds of a hard Brexit and more-thorough disruption of UK trade with the EU. We would not be surprised to see further downside volatility in sterling as we draw closer to the EU exit date.

Fears of a trade war pitting the US against foes and allies alike notwithstanding, American investors, businesses and consumers have much to applaud. US corporate tax reform, tax cuts for households, and reduced or modified regulation of various industries have led to record-high consumer and business confidence.

But sabre-rattling between the US and China has deteriorated into actual skirmishing, and the latest back-and-forth suggests this spat will get worse before it gets better. To be blunt, the Trump administration's strategy of waging a trade war with China could prove to be the equivalent of cutting off one's nose to spite one's face.

A trade war will likely lead to higher prices for consumers and hurt the bottom lines of companies that sell imported goods and those that depend on global supply chains in their production process—resulting in a net loss for society. A small group of producers will probably benefit substantially from the trade impediments, while most consuming industries and households suffer declines in purchasing power—declines that may be small at the level of the individual, but would add up to an enormous loss across the affected economies.

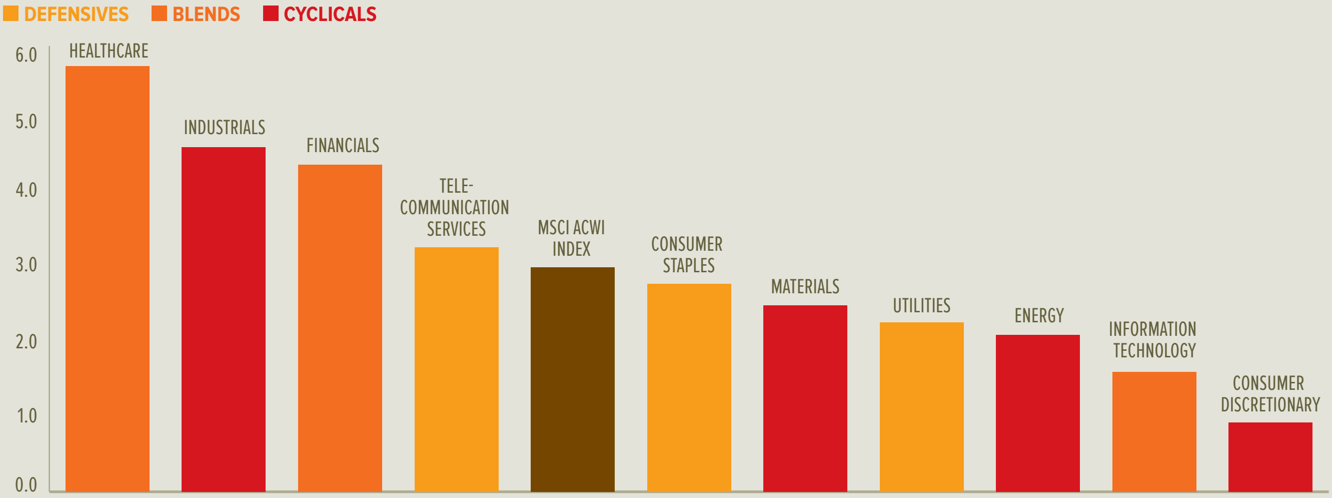
Regional Equity Performance in July 2018 (Percent Return)



Sources: FactSet, Lipper. See "Corresponding Indexes for Regional Equity Performance Exhibit" in the Index Descriptions section for more information.

All references to performance are in US dollar terms unless otherwise noted. See Standardised Performance for more information.

Global Equity Sector Performance in July 2018 (Percent Return)



Sources: FactSet, Lipper. MSCI ACWI Index Sector Components (Cyclicality determined by SEI).

SEI will be watching closely how this drama plays out in the months ahead. With any luck, the Trump administration will shy away from further ratcheting tensions. But we must admit that doesn't seem to be in the cards in the near-term.

A confluence of events has conspired to hurt the performance of emerging-market assets. An extensive trade war that disrupts multinationals' supply chains would disrupt the flow of raw commodities and semi-finished materials from developing economies, which depend on these exports for economic growth. Rising US interest rates, resulting in another period of sustained US dollar strength, are a second threat. The soft patch in Europe and recent signs of deceleration in China's economic growth is a third.

But while emerging-market stocks and bonds have come under pressure this year, we've yet to see any widespread deterioration in economic performance or financial conditions. On balance, we think most emerging markets have the ability to weather the storm—again, assuming the disruption to global trade does not devolve into something more encompassing.

Make no mistake about it: the headwinds blowing in the face of risk assets have picked up. Growth in business activity has slowed a bit, especially in Europe. Monetary policy in the US is getting tighter, and is set to become less expansionary in Europe as well. Inflation has ticked higher, driven by synchronised global growth and a tightening of labour markets and industrial capacity in the US, Germany, the UK, China, and elsewhere in Asia. A jump in oil prices is also pushing headline consumer-price index readings to their highest levels in several years; Organization of the Petroleum Exporting Countries and Russia have shown a fair degree of discipline in constraining the supply of crude oil at a time when demand is strong and inventory levels have fallen. Some developing countries have been forced to raise their policy rates dramatically to defend their currencies.

On balance, we think most emerging markets have the ability to weather the storm—again, assuming the disruption to global trade does not devolve into something more encompassing.

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Most important, the stoking of trade-war tensions by the US threatens to undermine the very foundation of the system that has supported the global economy since the end of the Second World War. Although the actual trade actions to date have been modest, the impact on global supply chains bears close watching.

But the economic fundamentals that drive the stock market still appear solid, even in places like Europe and developing economies. Plus, interest rates remain at levels that are accommodative to global economic growth. The key risks—escalating trade tensions and the polarisation of electorates over issues like immigration and fiscal sovereignty—appear more political in nature. The positives include a still-solid global economy; strong momentum in corporate-profits growth; and equity valuations that still appear reasonable against the backdrop of still-low, albeit rising, interest rates.

Signs of financial stress remain isolated to the weaker economies; although Italy is an important case, owing to its size and position as a major eurozone country.

A broadening of the trade war with China or a US departure from the North American Free Trade Agreement would likely have a severely negative impact on the profitability of US manufacturers, prompting us to reassess our still-positive view. Impediments to trade also could lead to a higher inflation rate as US companies use the tariffs umbrella to raise their selling prices. The US Federal Reserve may feel compelled to lean against this threat to price stability, thereby aggravating any economic shock arising from the disruption of global supply chains—which is how a bear market could develop.

This is not our base-case scenario. We still think this old bull has some life left in it, but the risks to the equity market now seem more balanced than skewed to the bullish side.

Standardised Performance

		1 year to 31-Jul-18	1 year to 31-Jul-17	1 year to 31-Jul-16	1 year to 31-Jul-15	1 year to 31-Jul-14
Key Measures						
Dow Jones Industrial Average		18.75%	21.81%	7.01%	9.34%	9.39%
S&P 500 Index		16.24%	16.04%	5.61%	11.21%	16.94%
NASDAQ Composite Index		22.13%	24.41%	1.92%	18.71%	22.00%
MSCI ACWI Index (Net)		10.97%	17.06%	-0.44%	2.83%	15.91%
Bloomberg Barclays Global Aggregate Index		-0.48%	-1.28%	9.45%	-6.04%	5.10%
Major Index Performance						
Bloomberg Barclays Global Aggregate ex-Treasury Index		-0.55%	1.53%	6.03%	-3.65%	5.70%
Bloomberg Barclays Global Aggregate Index		-0.48%	-1.28%	9.45%	-6.04%	5.10%
Bloomberg Barclays Global Treasury Index		-0.43%	-3.56%	12.39%	-8.05%	4.59%
MSCI ACWI ex-USA (Net)		5.94%	19.01%	-5.54%	-4.57%	15.48%
MSCI Emerging Markets Index (Net)		4.36%	24.84%	-0.75%	-13.38%	15.32%
MSCI World Index (Net)		11.88%	16.12%	-0.46%	4.92%	15.96%
Fixed-Income Performance						
US Treasury Inflation-Protected Securities (TIPS)	Bloomberg Barclays 1-10 Year U.S. TIPS Index	0.55%	-0.08%	3.76%	-1.80%	2.39%
Global Non-Government	Bloomberg Barclays Global Aggregate ex-Treasury Index	-0.55%	1.53%	6.03%	-3.65%	5.70%
Global Sovereigns	Bloomberg Barclays Global Treasury Index	-0.43%	-3.56%	12.39%	-8.05%	4.59%
US Investment-Grade Corporates	Bloomberg Barclays U.S. Corporate Investment Grade Index	-0.73%	1.55%	8.78%	1.49%	6.78%
US Asset-Backed Securities (ABS)	Bloomberg Barclays U.S. Asset-Backed Securities Index	0.26%	0.98%	2.44%	2.00%	1.83%
US Mortgage-Backed Securities (MBS)	Bloomberg Barclays U.S. Mortgage-Backed Securities Index	-0.41%	0.19%	3.90%	3.54%	4.14%
US Treasurys	Bloomberg Barclays U.S. Treasury Index	-1.23%	-2.55%	5.77%	3.33%	1.99%
US High Yield	ICE BofAML US High Yield Constrained Index	2.50%	11.24%	4.95%	0.17%	8.28%
Emerging Markets (External)	JPMorgan EMBI Global Diversified Index	0.07%	5.04%	11.22%	0.60%	10.74%
Emerging Markets (Local)	JPMorgan GBI-EM Global Diversified Index	-2.50%	7.97%	5.30%	-16.68%	3.39%
Regional Equity Performance						
United Kingdom	FTSE All-Share Index	8.61%	14.09%	-11.67%	-2.60%	17.61%
EM Latin America	MSCI Emerging Markets Latin America Index (Net)	0.71%	18.02%	6.42%	-30.53%	11.26%
Europe ex UK	MSCI Europe ex UK Index (Net)	4.67%	22.38%	-9.89%	1.10%	15.24%
Pacific ex Japan	MSCI Pacific ex Japan Index (Net)	6.23%	16.48%	0.89%	-11.17%	19.34%
United States	S&P 500 Index	16.24%	16.04%	5.61%	11.21%	16.94%
Japan	TOPIX, also known as the Tokyo Stock Price Index	9.20%	15.99%	-1.60%	8.82%	11.14%
Global Equity Sector Performance						
MSCI ACWI Index		10.97%	18.78%	-0.44%	2.83%	15.91%
MSCI ACWI Consumer Discretionary Index		14.30%	20.46%	-2.57%	12.88%	12.30%
MSCI ACWI Consumer Staples Index		1.29%	4.27%	7.58%	9.91%	7.50%
MSCI ACWI Energy Index		21.85%	0.25%	-1.30%	-28.02%	17.44%
MSCI ACWI Financials Index		5.21%	33.41%	-10.38%	2.76%	13.24%
MSCI ACWI Healthcare Index		11.25%	9.63%	-4.27%	22.69%	20.82%
MSCI ACWI Industrials Index		9.73%	22.08%	3.88%	1.31%	14.35%
MSCI ACWI Information Technology Index		22.47%	35.53%	8.15%	7.96%	27.29%
MSCI ACWI Materials Index		10.99%	24.44%	3.07%	-16.39%	17.52%
MSCI ACWI Telecommunication Services Index		-5.30%	-2.23%	3.21%	0.21%	16.02%
MSCI ACWI Utilities Index		2.67%	3.38%	8.85%	-1.09%	13.55%

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Glossary of Financial Terms

Bear market: A bear market refers to a market environment in which prices are generally falling (or are expected to do so) and investor confidence is low.

Bull market: A bull market refers to a market environment in which prices are generally rising (or are expected to do so) and investor confidence is high.

Federal funds rate: The Federal funds rate is the interest rate at which a depository institution lends immediately available funds (balances at the Federal Reserve) to another depository institution overnight in the US.

Fundamentals: Fundamentals refers to data that can be used to assess a country or company's financial health such as amount of debt, level of profitability, cash flow, inventory size, etc.

Yield curve: The yield curve represents differences in yields across a range of maturities of bonds of the same issuer or credit rating (likelihood of default). A steeper yield curve represents a greater difference between the yields. A flatter curve indicates the yields are closer together.

Yield spreads: Yield spreads represents the difference in yields offered between different types of bonds. If they tighten, this means that the difference has decreased. If they widen, this means the difference has increased.

Index Descriptions

The MSCI EMU (European Economic and Monetary Union) Index: The MSCI EMU Index captures large- and mid-cap representation across the developed-markets countries in the European Economic and Monetary Union.

Corresponding Indexes for Key Measures Exhibit

Dow Jones Industrial Average	The Dow Jones Industrial Average is a widely followed market indicator based on a price-weighted average of 30 blue-chip New York Stock Exchange stocks that are selected by editors of The Wall Street Journal.
NASDAQ Composite Index	The NASDAQ Composite Index is a market-value-weighted index of all common stocks listed on the National Association of Securities Dealers Automated Quotations (NASDAQ) system, representing a subset of the US equity market.
MSCI ACWI Index	The MSCI ACWI Index is a market-capitalization-weighted index composed of over 2,000 companies, and is representative of the market structure of 46 developed- and emerging-market countries in North and South America, Europe, Africa and the Pacific Rim. The Index is calculated with net dividends reinvested in US dollars.
Bloomberg Barclays Global Aggregate Index	The Bloomberg Barclays Global Aggregate Index is an unmanaged market-capitalization-weighted benchmark that tracks the performance of investment-grade fixed-income securities denominated in 13 currencies. The Index reflects reinvestment of all distributions and changes in market prices.
Chicago Board Options Exchange Volatility Index (VIX)	The Chicago Board Options Exchange Volatility Index (VIX) tracks the expected volatility in the S&P 500 Index over the next 30 days. A higher number indicates greater volatility.

Corresponding Indexes for Major Index Performance Exhibit

MSCI ACWI ex-USA Index	The MSCI ACWI ex-USA Index includes both developed- and emerging-market countries, excluding the US.
MSCI Emerging Markets Index	The MSCI Emerging Markets Index is a free float-adjusted market-capitalization-weighted index designed to measure the performance of global emerging-market equities.
MSCI World Index	The MSCI World Index is a free float-adjusted market-capitalization-weighted index that is designed to measure the equity market performance of developed markets.
Bloomberg Barclays Global Aggregate Index	The Bloomberg Barclays Global Aggregate Index is an unmanaged market-capitalization-weighted benchmark that tracks the performance of investment-grade fixed-income securities denominated in 13 currencies. The Index reflects reinvestment of all distributions and changes in market prices.
Bloomberg Barclays Global Aggregate ex-Treasury Index	The Bloomberg Barclays Global Aggregate ex-Treasury Index is an unmanaged market index representative of the total return performance of ex-Treasury major world bond markets.
Bloomberg Barclays Global Treasury Index	The Bloomberg Barclays Global Treasury Index is composed of those securities included in the Bloomberg Barclays Global Aggregate Index that are Treasury securities.

Corresponding Indexes for Fixed-Income Performance Exhibit

US High Yield	BofA Merrill Lynch U.S. High Yield Master II Constrained Index
Global Sovereigns	Bloomberg Barclays Global Treasury Index
Global Non-Government	Bloomberg Barclays Global Aggregate ex-Treasury Index
Emerging Markets (Local)	JPMorgan GBI-EM Global Diversified Index
Emerging Markets (External)	JPMorgan EMBI Global Diversified Index
US Mortgage-Backed Securities (MBS)	Bloomberg Barclays U.S. Mortgage Backed Securities Index
US Asset-Backed Securities (ABS)	Bloomberg Barclays U.S. Asset-Backed Securities Index
US Treasurys	Bloomberg Barclays U.S. Treasury Index
US Treasury Inflation-Protected Securities (TIPS)	Bloomberg Barclays 1-10 Year U.S. TIPS Index
US Investment-Grade Corporates	Bloomberg Barclays U.S. Corporate Investment Grade Index

Corresponding Indexes for Regional Equity Performance Exhibit

United States	S&P 500 Index
United Kingdom	FTSE All-Share Index
Pacific ex Japan	MSCI Pacific ex Japan Index (Net)
Japan	TOPIX, also known as the Tokyo Stock Price Index
Europe ex UK	MSCI Europe ex UK Index (Net)
EM Latin America	MSCI Emerging Markets Latin America Index (Net)

Important Information

Data refers to past performance. Past performance is not a reliable indicator of future results.

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17cefe-IMU 169820-UK (08/18)