

New Year, Same Positive Trend

Quarterly Snapshot

- › During the final weeks of 2017, the European Council set up discussions about the future UK-EU relationship. In the US, a major tax overhaul was signed into law just before year-end that will take effect in 2018.
- › Over the next year or so, we think global growth will remain vibrant enough to allow risk assets to perform well.
- › In our view, significantly decreasing risk could result in substantial opportunity loss at a time of positive momentum for global stock markets.

Economic Backdrop

UK Prime Minister Theresa May paid dearly for an early Christmas gift: Brexit divorce negotiations made sufficient progress in mid-December, as they were accepted by the European Council, but only after May's government gave in to many EU demands regarding a financial settlement, citizen rights and the Irish border. This set up phase two of discussions concerning the post-divorce transition period and future relationship between the UK and EU. Talks are expected to start in late January. Elsewhere on the continent in late 2017, the European Commission voted to formally condemn Polish judiciary reforms that critics feared would politicize rule of law; the step could lead to a suspension of Poland's EU voting rights. European Parliament voted for a similar censure to be applied against Hungary earlier in the year. Acting German Chancellor Angela Merkel prepared to sit down with one-time (and potentially future) coalition partners, the Social Democrats, on the first weekend of the New Year in an attempt to form a government.

A major tax overhaul passed US Congress and was signed into law by President Donald Trump on 22 December, to take effect in 2018. Of lesser note, a stopgap spending bill followed a similar path in late December to keep the US government funded through mid-January. In the traditionally Republican state of Alabama, a Democratic candidate won a contentious "special" (that is, off-cycle) Senate election to fill a vacant seat—narrowing an already-thin Republican majority. Further afield, protests erupted in Iran during the final week of the year, initially to confront poor economic conditions, and evolving to challenge the country's entrenched leadership.

The Bank of England's (BOE) Monetary Policy Committee voted unanimously to abstain from making changes in December after increasing the bank rate in November. The European Central Bank (ECB) also held firm in December, in addition to reiterating its October announcement that monthly asset purchases will be reduced and that rate hikes will only take place once these purchases conclude in September 2018 (as anticipated) or possibly later. The US Federal Reserve (Fed) increased its funds rate, as expected, in December and maintained projections for three additional hikes in 2018. Its latest quarterly forecast showed a more optimistic economic outlook over the next few years. The Bank of Japan (BOJ) maintained its quantitative and qualitative easing programme—preserving rate targets and asset-purchase levels—in both monetary policy meetings held during the fourth quarter.

Key Measures: Q4 2017

EQUITY	
Dow Jones Industrial Average	10.96% ↑
S&P 500 Index	6.64% ↑
NASDAQ Composite Index	6.55% ↑
MSCI ACWI Index (Net)	5.73% ↑
BOND	
Bloomberg Barclays Global Aggregate Index	1.08% ↑
VOLATILITY	
Chicago Board Options Exchange Volatility Index PRIOR MONTH: 9.51	11.04 ↑
OIL	
WTI Cushing crude oil prices PRIOR MONTH: \$51.67	\$60.42 ↑
CURRENCIES	
Sterling vs. US dollar	\$1.35 ↑
Euro vs. US dollar	\$1.20 ↑
US dollar vs. yen	112.65 ↑

Sources: Bloomberg, FactSet, Lipper

UK stocks rallied sharply in December after a lacklustre October and an even weaker November, while European stocks cooled off at the end of the year following a short-lived climb in late October. US stocks charged into year-end with sustained strength. Japan retrenched in November after impressive gains through October, before making new highs at year-end. Long-term UK gilt rates slid and short-term rates held firm, while eurozone rates increased across all maturities (rates move inversely to prices). The US Treasury yield curve flattened as short-term rates increased and long-term rates declined. Oil prices climbed throughout the last three months of the year; West Texas Intermediate crude oil prices, a key indicator of movements in the oil market, topped \$60 per barrel on the last day of 2017 for the first time since July 2015.

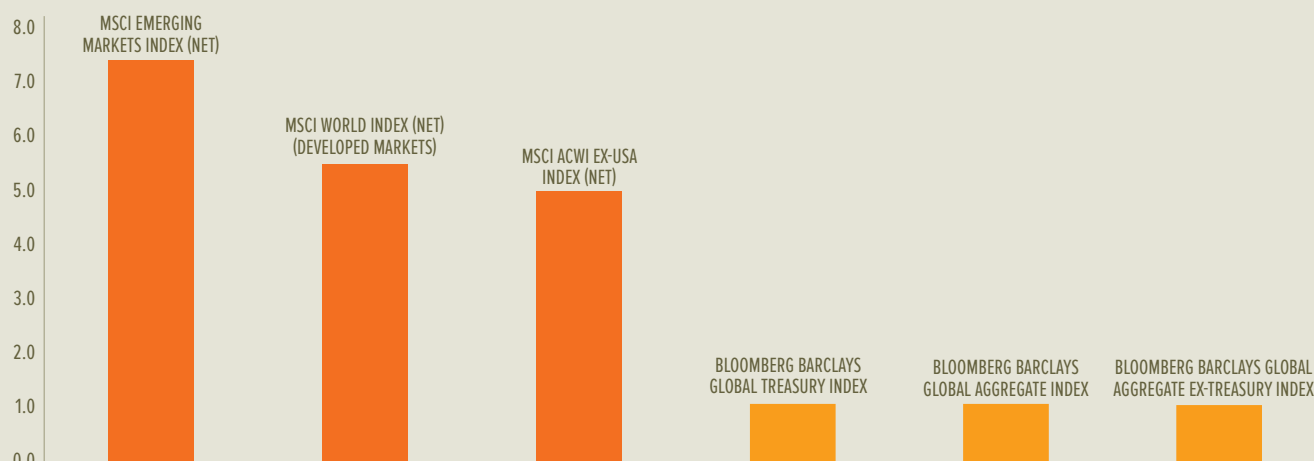
UK construction growth slowed as 2017 came to a close; manufacturing growth also came off a bit, but from admittedly strong levels. Labour-market conditions were mostly unchanged in November's report, with generally low unemployment, although average year-over-year earnings growth increased for the August-to-October period. The last reading of overall third-quarter economic growth was unrevised at 0.4%, yet the year-over-year figure increased to 1.7%.

Eurozone manufacturing conditions remained in high-growth territory, marking the highest new-order levels in more than 17 years. Services sector growth also firmed, albeit at lower-but-still-strong levels. Consumer confidence reflected these buoyant conditions, advancing for the fifth consecutive month in December. The final third-quarter economic growth report remained at 0.6%, but increased to 2.6% in the year-over-year ending September 30, 2017.

While not quite in the eurozone stratosphere, the pace of growth for US manufacturing conditions also continued to accelerate as year-end approached. Joblessness remained low, suggesting another robust employment report for December, while consumer confidence fell only slightly in December from recent 17-year highs. The third reading of overall economic growth edged down to a 3.2% annualised rate.

Major Index Performance in Q4 2017 (Percent Return)

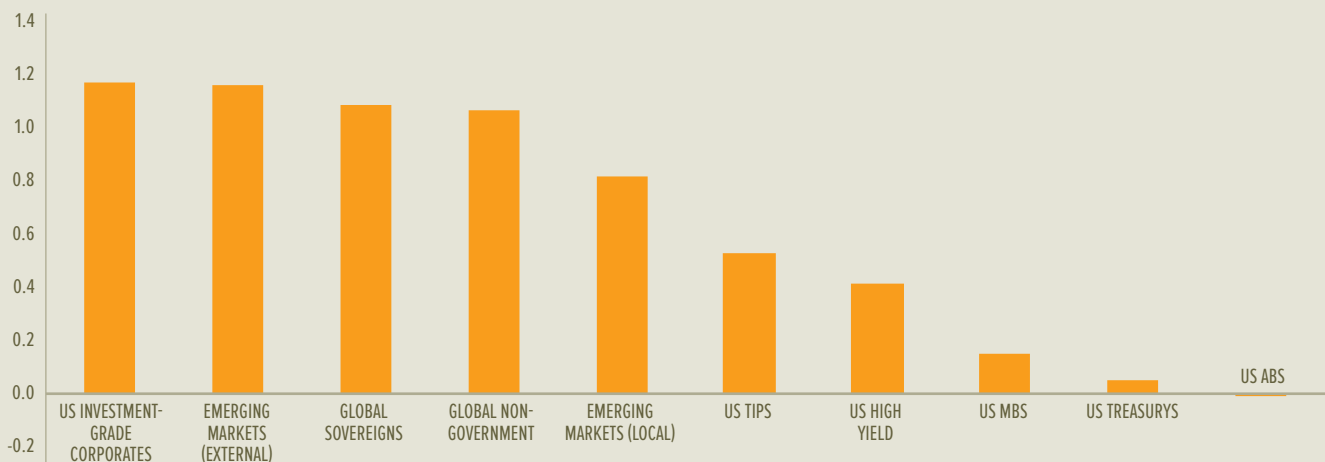
■ FIXED INCOME ■ EQUITIES



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 Q4 2017 (Percent Return)



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

Our View

We can sum up the year gone by with the exclamation that, at long last, the global financial crisis appears to be in the rear-view mirror. In its place is synchronised expansion across most developed and emerging economies. Admittedly, developed economies continued to run at a rather sluggish pace of 2% to 2.5% gross domestic product (GDP) growth. This is, at best, a middling sort of performance in the context of the past five decades. Emerging-market economies, meanwhile, continued to expand at a clip well below that of the past 20 years.

Looking out over the next year or so, we think global growth can still be vibrant enough to allow risk assets to perform well.

US tax legislation is hardly perfect: we believe it will not be as stimulative as advertised since tax cuts are skewed toward upper-income tax payers who tend to have a higher saving rate than the median household. But the permanent corporate tax changes, repatriation holiday, and the full expensing of capital equipment purchases over the next five years are positive developments for economic growth and investment.

Security analysts, always an optimistic lot, are calling for an 11% rise in S&P 500 Index per-share operating earnings in 2018. Although earnings estimates tend to fade through the year as estimates adjust to reality, this time may be an exception because tax cuts have not yet been taken fully into account.

The major worry for investors comes down to the stock market's valuation. A little more than three-fifths of the S&P 500 Index's price gain in 2017 came from improving earnings, while the rest was due to a rise in the price-to-earnings (P/E) ratio. But elevated valuations can be justified by the low level of bond yields and the strong trend in profits growth. Of course the higher the valuation, the more vulnerable the stock market becomes to unexpected bad news. We certainly would not rule out a garden-variety correction in stock prices of 5% to 10% somewhere along the line. The market is overdue for one—in 2017, the S&P 500 Index didn't even register a price correction of 3%.

Looking out over the next year or so, we think global growth can still be vibrant enough to allow risk assets to perform well.

We won't be really concerned, though, unless there is a more aggressive swing in Fed policy toward monetary tightness—something we don't anticipate in the coming year. It's possible that the US will see inflation pressures finally begin to build in the New Year, but US companies have proven able to maintain profit margins without resorting to price increases.

Through the third quarter, the eurozone economy, as measured by inflation-adjusted GDP, advanced by 2.6% on a year-over-year basis. By comparison, the US grew by only 2.3% over this period while the UK's increase amounted to only 1.5%.

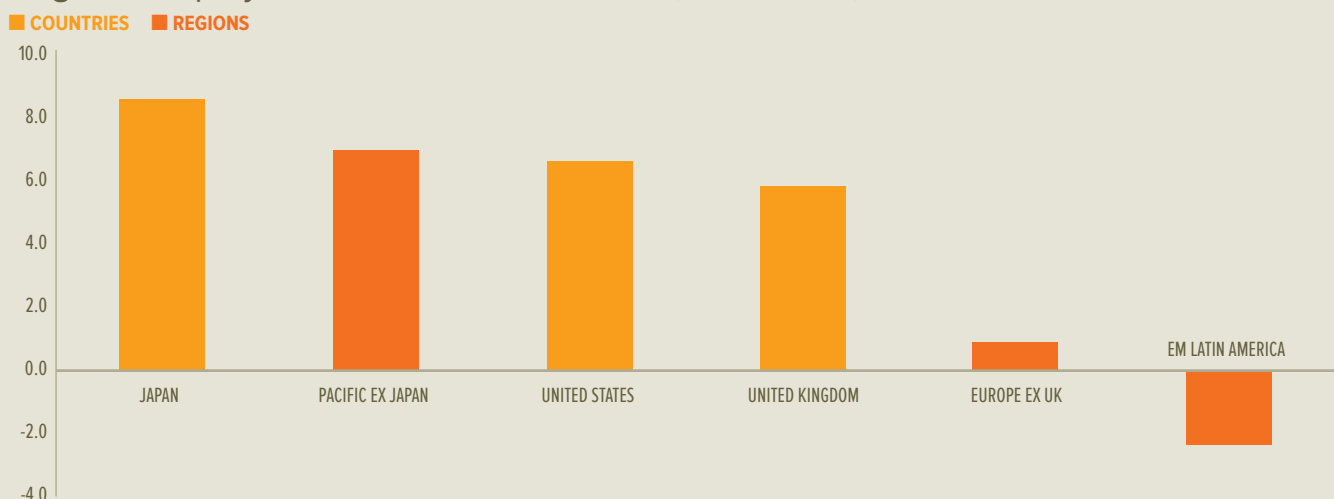
In our opinion, Europe has more growth potential. According to the World Economic Forum's annual report on global competitiveness, the high-income countries of Western Europe have made important strides in improving labour-market efficiency over the last five years. We also would note that political concerns in the eurozone are far more muted compared with a year ago, although we have not yet seen the end of the heavy anti-establishment undercurrent.

Given our view that the region is a long way from employment levels that will stir inflation pressures, we expect monetary policy to be supportive of growth throughout the coming year even as the ECB proceeds with its taper of quantitative easing. Since these asset purchases will continue at least until the end of September, it appears that policy rates will stay put until 2019.

Thus the way is clear for further growth in economic activity during the year ahead. We should see a continuation of the past year's strong revival in corporate revenues and earnings, and the MSCI European Economic and Monetary Union Index (Total Return) forward P/E ratio is no higher as of December 31, 2017, than it was at the start that year. Solid economic growth and cheap equity valuations are usually a good combination for investors.

These have not been easy days for UK Prime Minister Theresa May. The divorce stage of Brexit talks has finally concluded, with the UK mostly acceding to the EU's demands. But Parliament has begun to flex its muscles—and disapproval there would force the parties back to

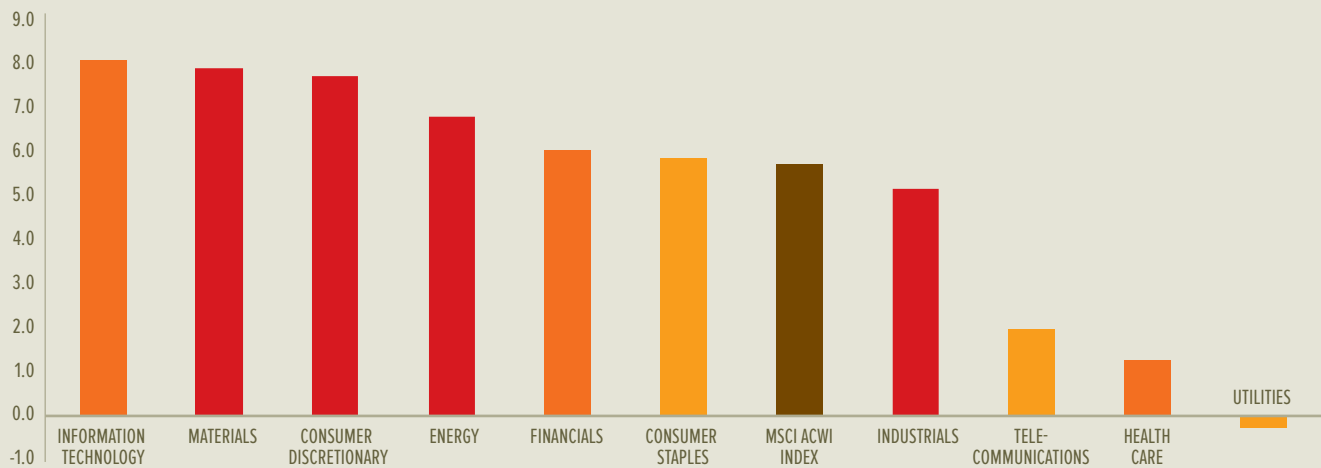
Regional Equity Performance in Q4 2017 (Percent Return)



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

Global Equity Sector Performance in Q4 2017 (Percent Return)

■ DEFENSIVES ■ BLENDS ■ CYCICALS



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

the negotiating table. Keep in mind that any changes to the withdrawal agreement demanded by Parliament would also entail unanimous approval of the 27 EU members on the other side of the negotiating table.

The pace of UK economic growth has been decelerating since 2014, although there is no indication that a recession is around the corner. The BOE's Monetary Policy Committee forecasted only two rate increases between now and the end of 2019. While time will tell whether the central bank's view regarding future policy moves are accurate, policymakers in the UK face tremendous challenges over the next few years. We think investors should tread lightly until there are clearer signs that inflation pressures have peaked and Brexit negotiations actually yield a favourable economic outcome for the country.

Japan is clearly benefiting from the global economic recovery. Exports to China are growing particularly quickly, and are now about equal to the share going to the US. Exports to the US and Europe also have accelerated, but not to the same extent.

Although there have been rumblings that the BOJ would like to take a step away from the extraordinary monetary policies that have been in place since the financial crisis, the central bank may find it difficult to do so. Domestic demand remains too weak and the population has begun contracting, a trend that will likely accelerate.

Japanese equities did well in 2017, with the TOPIX rising by 26.55%. Remarkably, the forward P/E ratio declined since the beginning of the year despite the improvement in economic fundamentals. It remains one of the more-cheaply valued stock markets among developed countries. Forward-earnings estimates have climbed sharply in the past year; we note that revenue estimates are also inflecting higher.

The MSCI Emerging Markets Index (Total Return) climbed by 37.28% last year, masking an even stronger contribution by China. Although China continued to reduce its dependence on heavy industry and increased the value added to GDP from service-producing industries, there was some backsliding last year. While these macro statistics need to be taken with

a grain of salt, it appears that China's growth has accelerated significantly from two years ago and advanced at its fastest clip since the 2012 to 2013 period. If China can maintain positive momentum, commodity prices should continue to rally as well.

We have held a positive view of risk assets for most of this long bull market. When speaking to investors who are nervous about the stock market's valuation, we urge them to keep a longer-term focus. Timing the market in anticipation of a short-term correction should be discouraged. As we've seen in the past year, making a major de-risking move could result in a significant opportunity-loss at a time when the stock market's momentum is quite positive and there are few, if any, signs of major economic imbalances or frothy valuations. Until we see a more significant deterioration in the economic and financial fundamentals that have underpinned the global bull market in risk assets over the past two years, our default investment stance is to stay the course.

There are many possible events and developments that could have a big negative impact, but we believe most have a low probability of actually happening. We will therefore maintain our "risk-on" bias until we see more evidence that such a stance merits revision.

Standardised Performance

		1 year to 31-Dec-17	1 year to 31-Dec-16	1 year to 31-Dec-15	1 year to 31-Dec-14	1 year to 31-Dec-13
KEY MEASURES						
Dow Jones Industrial Average		28.11%	16.50%	0.21%	10.04%	29.65%
S&P 500 Index		21.83%	11.96%	1.38%	13.69%	32.39%
NASDAQ Composite Index		29.64%	8.87%	6.96%	14.75%	39.74%
MSCI ACWI Index (Net)		23.97%	7.86%	-2.36%	4.16%	22.80%
Bloomberg Barclays Global Aggregate Index		7.39%	2.09%	-3.15%	0.59%	-2.60%
MAJOR INDEX PERFORMANCE						
Bloomberg Barclays Global Aggregate ex-Treasury Index		7.51%	2.59%	-3.00%	2.22%	-0.59%
Bloomberg Barclays Global Aggregate Index		7.39%	2.09%	-3.15%	0.59%	-2.60%
Bloomberg Barclays Global Treasury Index		7.29%	1.65%	-3.29%	-0.79%	-4.30%
MSCI ACWI ex-USA (Net)		27.19%	4.50%	-5.66%	-3.87%	15.29%
MSCI Emerging Markets Index (Net)		37.28%	11.19%	-14.92%	-2.19%	-2.60%
MSCI World Index (Net)		22.40%	7.51%	-0.87%	4.94%	26.68%
FIXED-INCOME PERFORMANCE						
US Treasury Inflation-Protected Securities (TIPS)	Bloomberg Barclays 1-10 Year U.S. TIPS Index	1.90%	4.01%	-0.52%	0.91%	-5.58%
Global Non-Government	Bloomberg Barclays Global Aggregate ex-Treasury Index	7.51%	2.59%	-3.00%	2.22%	-0.59%
Global Sovereigns	Bloomberg Barclays Global Treasury Index	7.29%	1.65%	-3.29%	-0.79%	-4.30%
US Investment-Grade Corporates	Bloomberg Barclays U.S. Corporate Investment Grade Index	6.42%	6.11%	-0.68%	7.46%	-1.53%
US Asset-Backed Securities (ABS)	Bloomberg Barclays U.S. Asset-Backed Securities Index	1.55%	2.03%	1.25%	1.88%	-0.27%
US Mortgage-Backed Securities (MBS)	Bloomberg Barclays U.S. Mortgage-Backed Securities Index	2.47%	1.67%	1.51%	6.08%	-1.41%
US Treasuries	Bloomberg Barclays U.S. Treasury Index	2.31%	1.04%	0.84%	5.05%	-2.75%
US High Yield	ICE BofAML US High Yield Constrained Index	7.48%	17.49%	-4.61%	2.51%	7.41%
Emerging Markets (External)	JPMorgan EMBI Global Diversified Index	10.26%	10.15%	1.18%	7.43%	-5.25%
Emerging Markets (Local)	JPMorgan GBI-EM Global Diversified Index	15.21%	9.94%	-14.92%	-5.72%	-8.98%
REGIONAL EQUITY PERFORMANCE						
United Kingdom	FTSE All-Share Index	23.82%	-2.12%	-4.55%	-4.75%	23.09%
EM Latin America	MSCI Emerging Markets Latin America Index (Net)	23.74%	31.04%	-31.04%	-12.30%	-13.36%
Europe ex UK	MSCI Europe ex UK Index (Net)	26.82%	-0.56%	-0.65%	-6.55%	27.65%
Pacific ex Japan	MSCI Pacific ex Japan Index (Net)	25.88%	7.85%	-8.47%	-0.50%	5.49%
United States	S&P 500 Index	21.83%	11.96%	1.38%	13.69%	32.39%
Japan	TOPIX, also known as the Tokyo Stock Price Index	26.55%	3.46%	11.69%	-3.33%	27.03%
GLOBAL EQUITY SECTOR PERFORMANCE						
MSCI ACWI Index		23.97%	2.88%	7.86%	4.16%	22.80%
MSCI ACWI Consumer Discretionary Index		25.16%	1.52%	2.88%	3.47%	35.97%
MSCI ACWI Consumer Staples Index		17.73%	27.66%	1.52%	6.15%	18.47%
MSCI ACWI Energy Index		6.77%	12.38%	27.66%	-13.47%	13.60%
MSCI ACWI Financials Index		24.09%	-6.83%	12.38%	3.43%	22.08%
MSCI ACWI Healthcare Index		20.14%	11.92%	-6.83%	18.13%	35.76%
MSCI ACWI Industrials Index		25.27%	12.20%	11.92%	0.19%	29.41%
MSCI ACWI Information Technology Index		41.77%	23.59%	12.20%	15.20%	26.51%
MSCI ACWI Materials Index		29.63%	7.86%	23.59%	-7.49%	-0.72%
MSCI ACWI Telecommunications Index		7.72%	5.03%	5.03%	-1.83%	23.52%
MSCI ACWI Utilities Index		13.93%	5.68%	5.68%	13.78%	10.58%

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

Glossary of Financial Terms

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.

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 and inventory size.

Macroeconomic: Macroeconomic refers to the broad economy of a country or region, or the global economy.

Quantitative easing/tightening: Quantitative easing refers to expansionary efforts by central banks to help increase the supply of money in the economy; quantitative tightening refers to efforts by central banks to help decrease the supply of money in the economy.

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.

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 Treasuries	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 performance.

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