FIRST STATE DIVERSIFIED GROWTH FUND

Multi Asset

Q4 2019 Review

The First State Diversified Growth Fund ('the Fund' or 'DGF') aims to protect against UK inflation and provide capital growth by achieving a positive return (gross of fees and charges) of 4% in excess of UK Retail Price Index (RPI) over rolling five-year periods.

The Fund returned 2.6% during the 2019 fourth quarter. Over this period, geopolitical risks declined as the US and China announced a phase one trade deal. This helped global equity markets to post robust gains. In fixed income, corporate bonds performed well amid the improved investor sentiment.

The Neutral Asset Allocation ('NAA') provided a strong performance contribution, particularly through equities. Dynamic Asset Allocation ('DAA') provided a smaller contribution with contributions diversified across equities, fixed income and currency strategies. UK RPI was flat for the quarter ending 30 December 2019.

The Fund has delivered 4.2% p.a. (net of fees and taxes) since inception in June 2015, 1.8% p.a. above UK RPI, with a monthly volatility of 6.3%. For reference, over the same period the FTSE 100 Index delivered 6.4% p.a. with a volatility of 10.3%.

Performance overview

Annual Performance (% in GBP) to 31 December 2019	12 months to 31/12/2019	12 months to 31/12/2018	12 months to 31/12/2017	12 months to 31/12/2016
First State Diversified Growth B GBP Acc	**15.69**	**-10.20**	**6.54**	**14.19**
UK Retail Price Index	1.80	2.93	3.64	2.00

Cumulative Performance (% in GBP) to 31 December 2019	3 months	6 months	YTD	1 year	2 years	3 years	Since Inception 23/06/2015
First State Diversified Growth B GBP Acc	**2.58**	**6.21**	**15.69**	**15.69**	**3.89**	**10.68**	**20.60**
UK Retail Price Index	0.01	0.59	1.80	1.80	4.78	8.60	11.37
Real Return	2.57	5.62	13.89	13.89	-0.90	2.08	9.23

Source: Lipper IM / First State Investments (UK) Limited.

These figures refer to the past. Past performance is not a reliable indicator of future results. For investors based in countries with currencies other than the share class currency, the return may increase or decrease as a result of currency fluctuations.

Performance figures have been calculated since the launch date. Performance data is calculated on a net basis by deducting fees incurred at fund level (e.g. the management and administration fee) and other costs charged to the fund (e.g. transaction and custody costs), save that it does not take account of initial charges or switching fees (if any). Income reinvested is included on a net of tax basis. Source: Lipper IM / First State Investments (UK) Limited.

RISK FACTORS

This document is a financial promotion for The First State Multi-Asset Strategy. This information is for professional clients only in the EEA and elsewhere where lawful. Investing involves certain risks including:

- **The value of investments and any income from them may go down as well as up and are not guaranteed. Investors may get back significantly less than the original amount invested.**
- **Currency risk:** Changes in exchange rates will affect the value of assets which are denominated in other currencies.
- **Emerging market risk:** Emerging markets may not provide the same level of investor protection as a developed market; they may involve a higher risk than investing in developed markets.
- **Derivative risk:** The use of derivatives may result in large price fluctuations and gains or losses that are greater than an investment in the underlying asset.
- **Credit risk:** The issuers of bonds or similar investments may not pay income or repay capital when due.
- **Interest rate risk:** Interest rates affect the value of investments; if rates go up, the value of investments fall and vice versa.

Reference to specific securities or companies (if any) are included to explain the investment strategy and should not be construed as investment advice, or a recommendation to invest in any of those companies.

For a full description of the terms of investment and the risks please see the Prospectus and Key Investor Information Document for each Fund.

If you are in any doubt as to the suitability of our funds for your investment needs, please seek investment advice.

[1] Net of fees and tax for the B GBP Accumulation share class

Investment process

The investment process comprises two building blocks. The first, which we call Neutral Asset Allocation (NAA), sets longer-term, beta allocations on a long-only basis. The second part, which we call Dynamic Asset Allocation (DAA), allows us to exploit shorter-term alpha opportunities through proprietary strategies that aim to be uncorrelated to broader markets. Further, DAA strategies aim to help manage risk through protection strategies. We review the DAA on a weekly basis.

For a comprehensive description of the investment process, click **here**

Market review

As the year ended, sentiment focused on the possible de-escalation in the US-China trade dispute, that dominated most of 2019, leading to global equities establishing new all-time highs and major market bond yields moved upward. While the final agreement remains to be seen, US negotiators have indicated existing tariffs on more than US$360 billion worth of imports from China may be reduced. China has also pledged to import large volumes of agricultural produce from the US and improve the protection of US intellectual property rights. An improvement in economic activity levels in the world's two largest economies could lift global growth forecasts and reduce the likelihood of further interest rate cuts in the year ahead. Over in Europe, a resounding victory for incumbent Prime Minister Boris Johnson in the UK general election effectively gave a green light for Brexit to be completed before the revised 31 January deadline. Johnson had campaigned with a 'Get Brexit Done' message, which appeared to resonate with the electorate. The election resulted in the biggest majority in Parliament for more than 30 years. The proposed Withdrawal Agreement passed easily with new MPs, following the election, and is expected to be formally ratified this month.

Global equities established new all-time highs towards the end of December as data reads gave increased hope that the global economy might have bottomed and as speculation mounted that a 'phase one' trade deal between the US and China was imminent.

Across global fixed income markets, government bond yields rose resulting in negative returns from fixed income securities. Among the major markets, the moves were most extreme in Germany where the benchmark 10-year Bund yields rose more than 30 basis points however remained in negative territory.

With the Withdrawal Agreement in the UK progressing its way to being passed, this could also alleviate a key source of uncertainty for global markets and, potentially, reduce the appeal of global bonds as a relatively stable, defensive asset class.

Credit markets exhibited a general improvement in risk appetite globally as credit bond spreads narrowed in both investment grade and high yield sectors. The spread on the Bloomberg Barclays Global Aggregate Corporate Index closed December at 0.98%, the first time spreads had been below the 1% threshold since early 2018. High yield spreads closed 2019 at their lowest levels for the year, at 2.70%. Strong performance was seen across the board, with issuers in the US, Europe and Asia all well supported over the month.

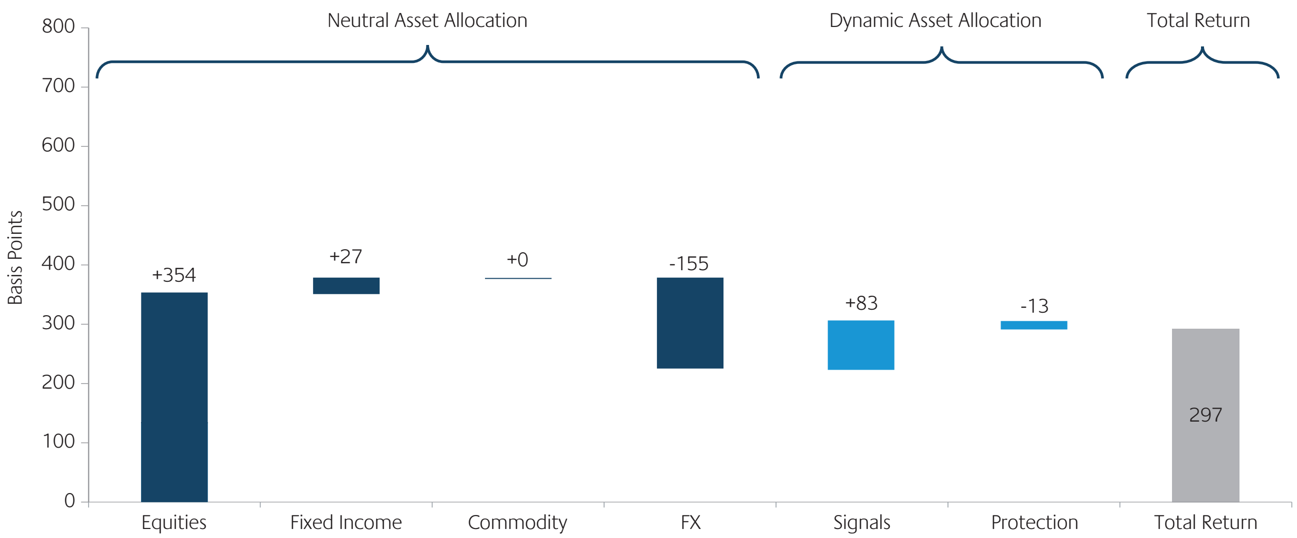
Portfolio performance and attribution

The NAA was the driver of Fund performance during the period, as shown in Figure 1. This was primarily a result of equity exposures, though exposure to government bonds and high yield credit also provided positive contributions. DAA positions provided a small positive contribution with portfolio protection, in the form of put options on S&P 500, offsetting gains within Investment Signals.

Key drivers of performance over the period:

- NAA positions added 2.7%, primarily driven by returns from US and UK equities
  - Equities, excluding the currency impact, added 3.5% over the quarter, as global markets advanced
  - Fixed income, which includes government and corporate bonds, added 0.3%
  - Currency exposure from the NAA detracted 1.6%, as sterling moved higher against major currencies
- DAA positions added a further 0.7%, driven by our investment signals:
  - Bond positioning added 0.2%. Short positions in emerging markets of Czech Republic and Hungary were the largest contributors while long positions in Australia and New Zealand detracted.
  - Currency positions added 0.3%. Short positions in Euro and Swiss franc performed well as geopolitical risks dissipated while long positions in emerging market currencies detracted.
  - Equity positions added 0.3% which was due to our overweight position vs over other asset classes
  - Protection strategies, where were in the form of put options on the S&P 500, detracted from performance over the quarter

Figure 1: Quarter-end performance contribution to 31 December 2019



Source: First State Investments as of 31 December 2019. Gross performance contribution might differ from official performance, due to data source, pricing, and timing.

Portfolio positioning

Neutral Asset Allocation ('NAA') positioning

We undertook our semi-annual NAA review in November 2019. Figure 2 shows the changes from the last NAA review.

The NAA maintained the 50% allocation to global equity markets. Global equities now account for a 40% allocation in the NAA while UK equities has been reduced to 10%. Within fixed income, we maintained the allocation to corporate credit at 10% and short-maturity UK gilts. As such, the NAA is currently positioned with the aim of protecting capital and, under this configuration, we expect a modest return of just under 3.0%. We see return opportunity in our alpha signals and are therefore allocating about half of the Fund's risk to DAA in order to maximise the potential of meeting the Fund's rolling five-year performance objective of RPI +4% (gross of fees and charges). The next scheduled review will be in May 2020.

Figure 2: DGF Neutral Asset Allocation

DGRF NAA	Apr-19		Nov-19	Change
Liquid securities	5.0%	–	5.0%	0.0%
Short-dated gilts	35.0%	–	35.0%	0.0%
Long-dated gilts	0.0%	–	0.0%	0.0%
Global government bonds	0.0%	–	0.0%	0.0%
High yield	10.0%	–	10.0%	0.0%
EM local currency bonds	0.0%	–	0.0%	0.0%
EM hard currency bonds	0.0%	–	0.0%	0.0%
UK Equities	12.5%	▼	10.0%	-2.5%
World (ex-UK) Equities	37.5%	▲	40.0%	2.5%
Commodities	0.0%	–	0.0%	0.0%
Total	**100.0%**		**100.0%**	

Source: First State Investments

Dynamic Asset Allocation ('DAA') positioning

Over the quarter we maintained our 3% overweight to equities as an asset class. Within equities, we prefer developed market equities to emerging market equities, with an overweight to Japanese and Canadian equities while finding the US unattractive.

Within the fixed income component of the portfolio, duration increased from 0.7 to 1.0 years over the quarter. Positions remained consistent, with the largest duration contributions coming from emerging markets, while holding short positions (benefit from rising yields) in the UK and Eurozone.

Over the quarter we reduced our long bias to emerging market currencies exposure from 21% to 15%. We continue to find emerging market currencies attractive, especially within Europe (Polish złoty and Hungarian forint). We are neutral on Sterling.

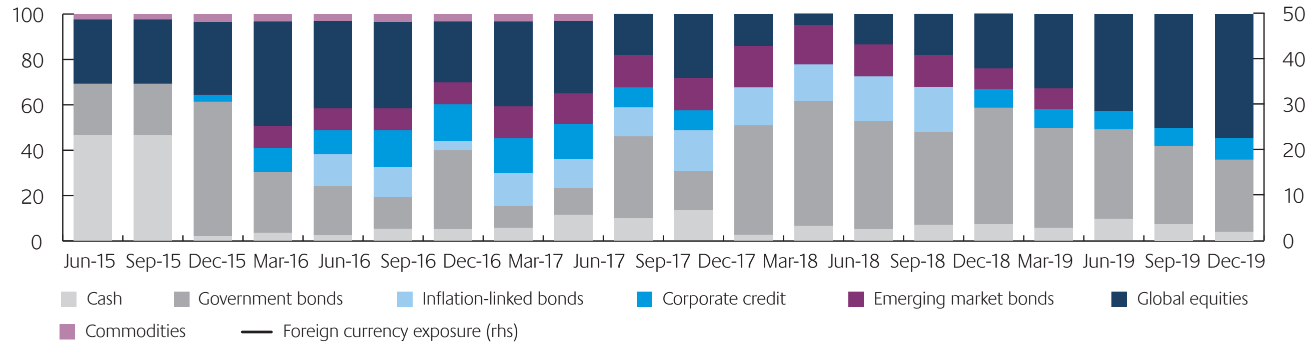
Combined NAA and DAA fund portfolio positioning

At 31 December 2019 the Fund had an equity exposure of 55%, with broad based exposure globally. The duration (interest rate risk) of the Fund is focused on emerging markets where we see the most attractive opportunities. The foreign currency exposure of the Fund increased over the quarter, to 32%.

Given current equity and bond valuations, NAA alone appears unlikely to be able to deliver the required return to meet the Fund's performance objective of RPI + 4%pa over rolling five-year periods. To bridge this shortfall, we use DAA to boost performance.

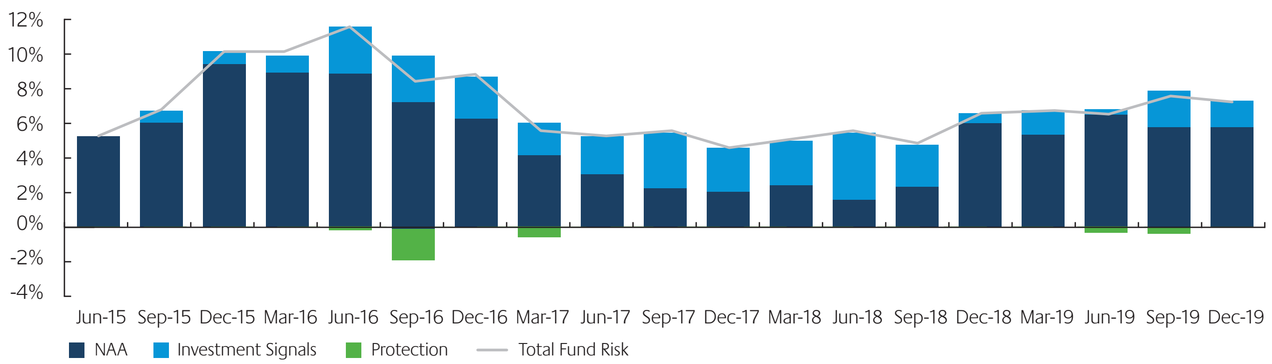
Figure 4 shows a breakdown of the Fund's ex-ante risk contribution since inception.

Figure 3: Overall asset allocation



Source: First State Investments, as at 31 December 2019

Figure 4: Portfolio ex-ante risk



Source: First State Investments, as at 31 December 2019

Market outlook

Throughout 2019, it was proven that uncertainty in the market is not all doom and gloom for investors. Global equities look to continue their upward trend for a while longer, while bond yields have recently turned around, moving up also. As current geopolitical tensions move towards the light, an appetite for risk has increased. It is, however, not yet time to relax - Brexit still needs to be a finalised and find a trade deal, and the US election will remain in sight.

New tensions, undoubtedly, could arise to take their places. In the first few days of the New Year, a US airstrike killed a high-ranking Iranian military commander. Concerns that this could intensify tensions in the Middle East have unsurprisingly arose. On another concerning note, the Supreme Leader of the Democratic People's Republic of Korea has suggested that it may step up its missile testing program in 2020. While the country suffers multiple economic sanctions, developing a strong nuclear arsenal remains on the agenda. Events such as these certainly run the risk of negatively affecting global sentiment, which could increase the appeal of defensive assets. Both the US-China trade dispute and Brexit had placed downward pressure on yields throughout 2019. After the positive developments in December, the geopolitical risks of last year look like they might be making some progress. If this is the case, yields could indeed drift higher as investors find risk assets attractive.

Following three rate cuts in the US, lower borrowing costs in China and with the recommencement of the ECB's quantitative easing program imminent, policy makers may adopt a 'wait and see' approach before considering whether any further changes are required. If so, government bond yields could remain range bound – albeit with quite a wide range potentially – in the near term. While diversification is always of critical importance in the portfolio, we continue to look for ways to participate in this late cycle while ensuring enough defensiveness should the cycle finally roll over. It seems likely that global central banks may unveil a few more stimulatory measures in the months ahead in an attempt to underpin economic activity levels. In the US, the Fed has already cut rates three times during the second half of last year. Following the last policy change, hints came that further cuts were unlikely, however, market expectations anticipate the possibility of further cuts in the coming months to help prolong economic expansion. With the next US Presidential Election a little over a year away, there is likely to be increasing political pressure for them to do so as Trump seeks re-election. In the UK, the Bank of England has kept interest rates at 0.75% and announced late December that the new Governor of the Bank of England – Andrew Bailey - will take reign from 16 March 2020. Alongside this, Brexit is to be finalised and a free trade deal will need to be concluded before the transition period wraps up end of 2020.

Global uncertainty has widely influenced both the bond and equity markets and economic indicators remain restrained, however there is still some optimism. Whether or not this bull market can prolong, the appetite for risk assets seems to persist. The bond market may signal a cause for concern and it will be interesting to see which market is indicative of the future.

Figure 5 provides a decomposition of ex-ante risk, as well as return contributions from each asset category for the June quarter and the last year. Please note that currency exposure is included in the asset breakdown and hedging is included as an independent category.

Figure 5: DGF return contribution

	Risk Contribution (%)	Contribution to 3m return (%)	Contribution to 1 yr return (%)
UK equities	1.09	0.26	2.60
World (ex UK) equities	4.21	0.86	8.24
Government bonds and cash	0.02	-0.20	0.03
Inflation-linked bonds	0.00	0.00	0.00
Emerging market bonds (HC)	0.00	0.00	0.00
Emerging market bonds (LC)	0.00	0.02	0.01
Corporate bonds	0.26	-0.40	0.69
Commodities	0.00	0.00	0.00
Currency hedging	-0.91	1.75	0.91
Protection strategies	0.00	-0.13	-0.48
Other	0.00	0.00	0.00
Investment Signals			
Equities	-0.04	0.32	0.23
Bonds	2.02	0.21	4.59
Currencies	0.50	0.31	0.42
	7.16	**2.97**	**17.22**

Source: First State Investments. Gross performance contribution might differ from official performance, due to data source, pricing, and timing.

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