First State Investments

FIRST STATE DIVERSIFIED GROWTH FUND

Multi Asset Solutions
Q2 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 3.1% during the June quarter. Investor focus was squarely on central banks as they consumed weaker economic data, trade risks and a weak inflation outlook. The Federal Reserve and the European Central Bank looked to calm investors' nerves by indicating that further economic stimulus may be in the pipeline.

The Neutral Asset Allocation ('NAA') provided a strong performance contribution, particularly through equities. Dynamic Asset Allocation ('DAA') provided a smaller contribution, primarily via fixed income and currency strategies. UK RPI increased by 1.6% in the quarter ending 30 June 2019.

The Fund delivered 3.2%[1] p.a. since inception in June 2015, 0.6% p.a. above UK RPI, with a monthly volatility of 6.3%. For reference, over the same period the FTSE 100 Index delivered 6.3% p.a. with a volatility of 10.5%.

Performance overview

Annual Performance (% in GBP) to 30 June 2019	12 months to 30/06/2019	12 months to 30/06/2018	12 months to 30/06/2017	12 months to 30/06/2016
First State Diversified Growth B GBP Acc	**1.3**	**-2.8**	**12.8**	**3.2**
UK Retail Price Index	2.7	3.2	3.3	1.1

Cummulative Performance (% in GBP) to 30 June 2019	3 month	6 month	YTD	1 year	2 year	3 year	Since Inception 23/06/2015
First State Diversified Growth B GBP Acc	**3.1**	**8.9**	**8.9**	**1.3**	**-1.6**	**11.0**	**13.5**
UK Retail Price Index	1.6	1.2	1.2	2.7	5.9	9.4	10.7
Real Return	1.5	7.7	7.7	-1.4	-7.5	1.6	2.8

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 First State Diversified Growth Fund for professional clients only. 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.

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

During the quarter, expectations shifted dramatically around future central bank action. Confronted by weaker economic data, risks to the trade outlook and persistently low inflation, the Federal Reserve and the European Central Bank indicated that help is on the way in the form of further monetary stimulus. This follows recent easing cycles beginning in other developed markets such as Australia and New Zealand. While cracks continue to emerge across the macroeconomic landscape, the rhetoric from the key central banks was not lost on markets, which ended both the quarter and full 2018-19 financial year (FY) with a bang. Risk assets, such as equities and credit, rallied along with traditional safe haven assets, such as developed market government bonds, gold and the Japanese yen. Reversing the weakness in risk assets in April and May, June's strong performance made it a good quarter and even better FY, almost irrespective of where money was invested.

Global equities delivered strong returns over the period as investors appeared to overlook trade tensions and cheered the prospect of interest rate cuts before year-end. It was a jubilant June after a miserable May with the MSCI All Country World Index ultimately generating nearly 5.0% returns over the quarter. The final month of the quarter saw US equities deliver the strongest returns across the major developed markets, with the S&P 500 Index delivering 7.0% in USD terms and rising to a new record high. Eurozone shares advanced overall, with a sharp drop in May sandwiched between gains in April and June. European Central Bank President Mario Draghi hinted at further monetary policy easing if the inflation outlook fails to improve. UK shares performed well over the quarter, despite ongoing Brexit-related uncertainty. Japanese equities performed worse than the other major developed markets while emerging market shares lagged their developed market counterparts. Trade uncertainty weighed on Chinese and South Korean stocks. The best performing markets among developing countries were South Africa, Indonesia, Turkey and Argentina.

Global bond yields moved sharply lower over the quarter, resulting in positive returns for investors. Ten-year US Treasury yields closed the quarter 0.40% lower at 2.00%, briefly trading below the 2% threshold towards the end of the period. US interest rates were unchanged during the quarter, but comments from policy makers suggested borrowing costs are likely to be lowered in the months ahead. Federal Reserve Committee members appear determined to sustain the ongoing economic expansion in the US and accordingly are likely to try and promote activity levels with more accommodative policy settings. Investment grade spreads tightened during the quarter, resulting in favourable returns from corporate bonds. The spread on the Bloomberg Barclays Global Aggregate Corporate Index closed the quarter 6 bps tighter, at 1.18%. High yield spreads actually widened modestly in the period as a whole – primarily due to weakness in May – but the sharp move lower in Treasury yields ensured returns from high yield credit were positive over the quarter.

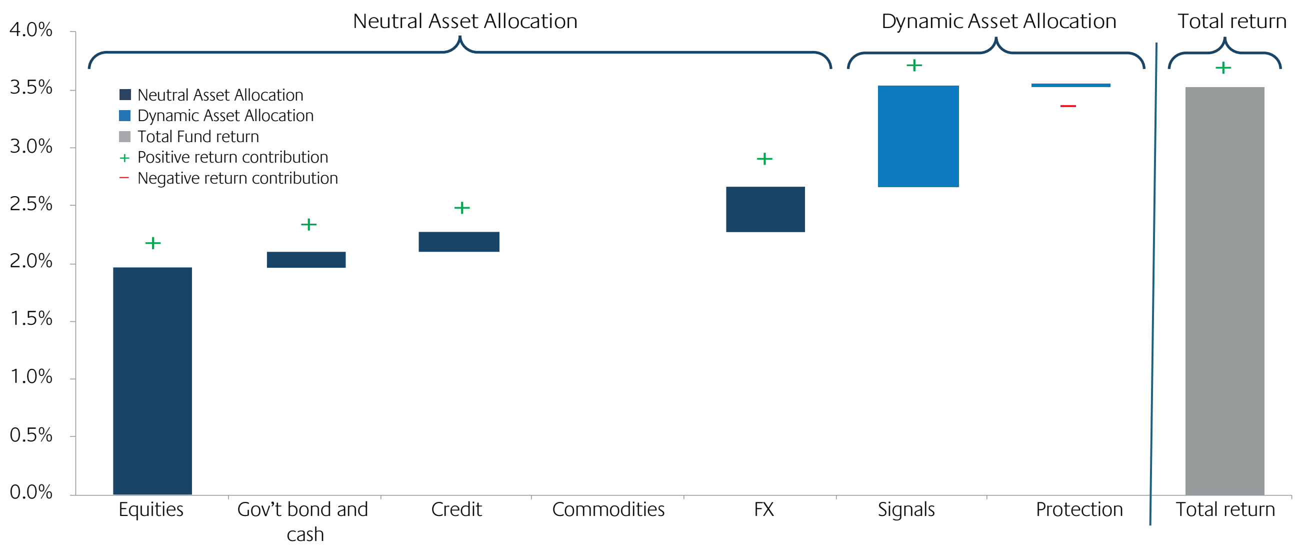
Portfolio performance and attribution

NAA was the key driver of performance during the period, as shown in Figure 1. This was primarily a result of equity exposures, though exposure to both government bonds and high yield credit also provided positive contributions. DAA positions also provided positive returns.

Drivers of performance over the period were:

- NAA positions added 2.7%, primarily driven by returns from US and UK equities
  - Equities, excluding the currency impact, added 2.0% over the quarter.
  - Developed market government bonds and cash contributed 0.1%.
  - Corporate bonds added 0.2%.
  - Currency exposure from the NAA added 0.4%, as sterling moved lower.
- DAA positions added a further 0.9%, driven by our investment signals:
  - Bond positioning added 0.8%; the bulk coming from emerging markets. Long positions in India and South Africa were the largest contributors.
  - Currency positions added 0.3% to performance. Long positions in the Russian ruble and Mexican peso were the largest contributors.
  - Positions informed by our equity signals detracted -0.2%. This was due to the preference to reduce exposure in favour of other asset classes in a rising equity market.
  - Protection strategies also detracted from performance slightly.

Figure 1: Quarter-end performance contribution to 30 June 2019



Source: First State Investments as of 30 June 2019. Month end data since inception.

Portfolio positioning

Neutral Asset Allocation ('NAA') positioning

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

The NAA maintained a 50% allocation to global equity markets. Equity investments are diversified across regions, with a quarter of the overall equity exposure held in domestic shares. Within fixed income, we have maintained the allocation to corporate high yield credit at 10%, while removing the emerging market local currency bond holdings and reallocating to short-dated maturity UK government bonds. As such, the NAA is currently positioned with the aim of protecting capital and, under this configuration, we expect a modest return of just over 3.0% p.a. We see return opportunities 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 objective. We will be reviewing the NAA again in November 2019.

Figure 2: DGF Neutral Asset Allocation

DGRF NAA	Nov-18		May-19	Change
Liquid securities	5.0%	–	5.0%	0.0%
Short-dated gilts	27.0%	▲	35.0%	8.0%
Long-dated gilts	0.0%	–	0.0%	0.0%
Global government High yield	0.0%	–	0.0%	0.0%
High yield	10.0%	–	10.0%	0.0%
EM local currency bonds	8.0%	▼	0.0%	-8.0%
EM hard currency bonds	0.0%	–	0.0%	0.0%
UK Equities	12.5%	–	12.5%	0.0%
World (ex-UK) Equities	37.5%	–	37.5%	0.0%
Commodities	0.0%	–	0.0%	0.0%
Total	**100.0%**		**100.0%**	

Source: First State Investments

Dynamic Asset Allocation ('DAA') positioning

At the end of the March quarter, we had made a decision to reduce our equity exposure. However during the June quarter we increased this exposure by 12%. We ended the six month period with a reduction of 7% overall. We added exposure to the UK and Australia and established a short position in Thailand.

Within the fixed income component of the portfolio, duration (interest rate risk) was reduced by 2.4 years over the quarter, from a duration exposure of 4.0 at the beginning of the period. As yields fell, the relative attractiveness of fixed income markets diminished somewhat; especially within the Eurozone. Consequently, we exited the Fund's French government bond positions and implemented a short duration position in Germany.

We also reduced the Fund's long held USD currency exposure during the quarter, in anticipation of potential dollar weakness associated with US interest rate cuts. We continue to find emerging market currencies attractive, especially within Europe (specifically Russian ruble and Hungarian forint). We find sterling moderately attractive at current levels, despite ongoing Brexit-related uncertainty.

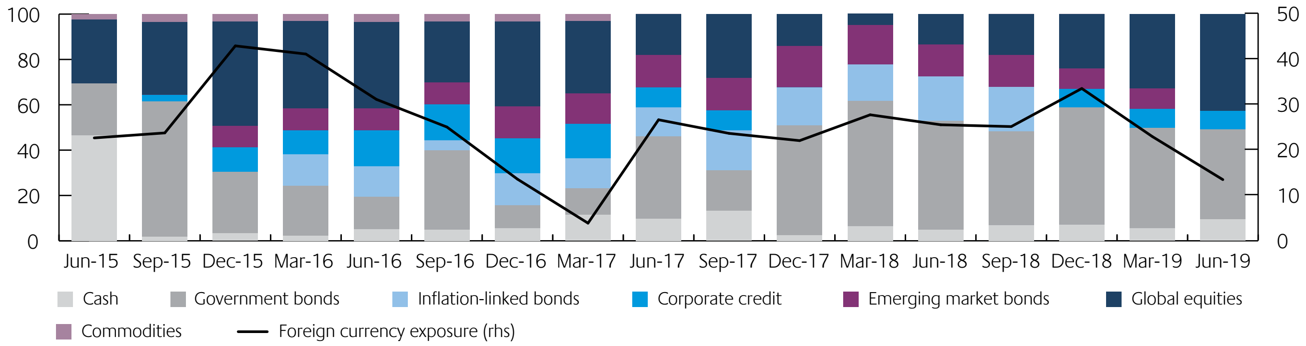
Combined NAA and DAA fund portfolio positioning

At 30 June 2019 the Fund had an equity exposure of 43%, with broad based exposure globally. The duration of the Fund is focused on emerging markets where we see the best opportunities. The foreign currency exposure of the Fund decreased over the quarter to 13%.

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. To bridge this shortfall, we use DAA to boost performance.

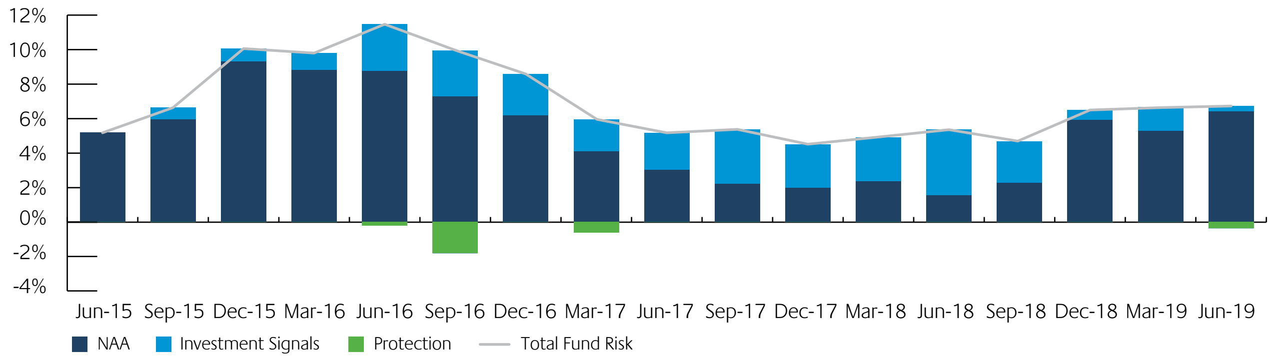
Figure 4 shows a breakdown of the Fund's ex-ante risk contribution since inception.

Figure 3: Overall asset allocation as at 30 June 2019



Source: First State Investments

Figure 4: Portfolio ex-ante risk



Source: First State Investments

Market outlook

Markets remain hypersensitive to developments in trade negotiations between the US and China – progress earlier in the year saw equities and credit markets rally, but less encouraging developments more recently saw risk assets come under pressure at times and government bonds perform well. It seems that this is primarily due to the correlation between global trade and the pace of worldwide GDP growth. Further news flow relating to trade talks will therefore remain closely scrutinised. We think trying to predict the next episode of the trade drama, which has dominated market sentiment so far this year, is somewhat futile. Instead, we expect tensions between the US and China to be a lingering headwind regardless of any near-term developments, and we anchor our outlook to our long-term economic climate assumptions. Taking all of this into account we believe it would be prudent to, take a somewhat cautious approach, especially as valuations appear increasingly stretched.

The other large variable to consider is the delivery on the increasingly high expectations being put on major central banks around the world. The US, UK and Australia have some (conventional) ammunition to help address any further slowdown in activity levels. With positive interest rates, there is scope for policy settings to be eased and it appears almost certain that they will be. With interest rates already at zero, further stimulus in Europe and Japan would need to come from less conventional means – most likely through a combination of quantitative easing measures similar to what we have seen in recent years. The direction of risky assets, such as equities and credit, along with high quality bond performance, will likely be dependent on how these issues play out in the months ahead.

Several bond markets are in uncharted territory following recent moves. In Europe, for example, 10-year bund yields have never traded as low as -0.30% before. Gilt yields are also close to record lows, reflecting a concerning slowdown in activity levels. The UK economy shrank in both March and April, raising concerns about a possible recession. The new Prime Minister faces a challenging period. The economic slowdown must be addressed and a revised Brexit deal needs to be negotiated if possible before the revised EU withdrawal deadline of 31 October 2019. Australian government bond yields are also at record lows and while US Treasury yields have traded lower on a few occasions since the Global Financial Crisis, the extent of the recent slump in yields has been extraordinary. In Asia, the outlook remains highly dependent on progress with trade-related dialogue between the US and China. Any escalation in the conflict could act as a significant drag on growth in the region and, in turn, weigh on the global growth outlook.

The positive performance of both equity and bond markets continues to point to two very different economic and market environments in the period ahead. Although bond markets are signalling warnings about the health of the global economy, risk assets seem to continue enjoying this seemingly never ending and much unloved bull market. It will be interesting to see which market is 'right' and the future direction of the global economy. Perhaps both will be prescient to some degree if we see inflation continue to fall and central banks remain accommodative.

Figure 5: Fund positioning and quarterly changes

Equity allocation by region	NAA	DAA	NAA + DAA = Portfolio as at June 2019	3m change
UK	13.2%	5.9%	19.1%	▲ 8.6%
US	11.4%	-4.6%	6.8%	▼ -3.7%
Eurozone	10.6%	2.9%	13.5%	▼ -1.4%
Japan	5.0%	2.9%	8.0%	▼ -1.3%
Other Developed Markets	2.0%	-13.4%	-11.4%	▲ 6.7%
Emerging Markets	7.4%	-0.0%	6.7%	▲ 1.0%
	49.8%	**-7.1%**	**42.0%**	▲ **9.8%**

Duration contribution by region	NAA	DAA	NAA + DAA = Portfolio as at June 2019	3m change
UK	0.2	0.0	0.2	
US	0.3	0.3	0.6	▲ 1.1
Eurozone	0.0	-1.0	-1.1	▼ -2.4
Japan	0.0	0.6	0.6	
Other Developed Markets	0.0	-1.0	-1.0	▼ -1.5
Emerging Markets	0.0	2.8	2.8	▲ 0.1
	0.5	**1.6**	**2.1**	▼ **-2.7**

Currency exposure by region	NAA	DAA	NAA + DAA = Portfolio as at June 2019	3m change
UK	83.0%	3.8%	86.7%	▲ 9.5%
US	0.3%	-2.4%	-2.2%	▼ -6.1%
Eurozone	1.3%	-5.5%	-4.2%	▼ -2.2%
Japan	4.1%	0.0%	4.1%	▲ 8.1%
Other Developed Markets	4.1%	-2.3%	1.8%	▼ -7.0%
Emerging Markets	7.3%	6.4%	13.7%	▼ -6.7%
	100.0%	**0.0%**	**100.0%**	**0.0%**

Source: First State Investments

Figure 6 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 6: DGF return contribution

	Risk Contribution (%)	Contribution to 3m return (%)	Contribution to 1 yr return (%)
UK equities	1.29	0.76	1.37
World (ex UK) equities	4.15	2.43	3.74
Government bonds and cash	0.00	0.14	0.83
Inflation-linked bonds	0.00	0.00	0.10
Emerging market bonds (HC)	0.00	0.00	0.07
Emerging market bonds (LC)	0.00	0.02	0.26
Corporate bonds	0.16	0.37	0.68
Commodities	0.00	0.00	0.00
Currency hedging	0.09	-1.05	-1.29
Protection strategies	-0.36	-0.02	-0.32
Other	0.00	0.00	0.00
Investment Signals			
Equities	-0.84	-0.21	-2.35
Bonds	1.21	0.77	2.70
Currencies	0.67	0.34	-2.04
	6.37	**3.54**	**3.74**

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

Reference Index performance overview

For reference only, the table below shows performance of the indices referenced throughout the Review.

Annual Performance (% in GBP) to 30 June 2019	12m to 30/06/2019	12m to 30/06/2018	12m to 30/06/2017	12m to 30/06/2016
Bloomberg Barclays Global Aggregate Corporate TR	11.8	-1.2	5.7	24.6
FTSE 100 TR	1.6	8.7	16.9	3.8
MSCI AC World TR USD	10.3	9.5	22.9	13.9
S&P 500 TR	14.5	12.5	21.3	22.3

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

For further institutional enquiries contact institutionalenquiries@firststate.co.uk

For wholesale enquiries contact enquiries@firststate.co.uk

Important Information

This document has been prepared for informational purposes only and is only intended to provide a summary of the subject matter covered and does not purport to be comprehensive. The views expressed are the views of the writer at the time of issue and may change over time. It does not constitute investment advice and/or a recommendation and should not be used as the basis of any investment decision. This document is not an offer document and does not constitute an offer or invitation or investment recommendation to distribute or purchase securities, shares, units or other interests or to enter into an investment agreement. No person should rely on the content and/or act on the basis of any material contained in this document.

This document is confidential and must not be copied, reproduced, circulated or transmitted, in whole or in part, and in any form or by any means without our prior written consent. The information contained within this document has been obtained from sources that we believe to be reliable and accurate at the time of issue but no representation or warranty, express or implied, is made as to the fairness, accuracy, or completeness of the information. We do not accept any liability whatsoever for any loss arising directly or indirectly from any use of this information.

References to "we" or "us" are references to First State Investments.

In the UK, issued by First State Investments (UK) Limited which is authorised and regulated by the Financial Conduct Authority (registration number 143359). Registered office Finsbury Circus House, 15 Finsbury Circus, London, EC2M 7EB number 2294743. Outside the UK within the EEA, this document is issued by First State Investments International Limited which is authorised and regulated in the UK by the Financial Conduct Authority (registered number 122512). Registered office: 23 St. Andrew Square, Edinburgh, EH2 1BB number SCO79063.

Certain funds referred to in this document are identified as sub-funds of First State Investments ICVC, an open ended investment company registered in England and Wales ("OEIC"). Further information is contained in the Prospectus and Key Investor Information Documents of the OEIC which are available free of charge by writing to: Client Services, First State Investments (UK) Limited, Finsbury Circus House, Finsbury Circus, London, EC2M 7EB or by telephoning 0800 587 4141 between 9am and 5pm Monday to Friday or by visiting www.firststateinvestments.com. Telephone calls may be recorded. The distribution or purchase of shares in the funds, or entering into an investment agreement with First State Investments may be restricted in certain jurisdictions.

Representative and Paying Agent in Switzerland: The representative and paying agent in Switzerland is BNP Paribas Securities Services, Paris, succursale de Zurich, Selnaustrasse 16, 8002 Zurich, Switzerland. Place where the relevant documentation may be obtained: The prospectus, key investor information documents (KIIDs), the instrument of incorporation as well as the annual and semi-annual reports may be obtained free of charge from the representative in Switzerland.

First State Investments (UK) Limited and First State Investments International Limited are part of Colonial First State Asset Management ("CFSGAM") which is the consolidated asset management division of the Commonwealth Bank of Australia ABN 48 123 123 124. CFSGAM includes a number of entities in different jurisdictions, operating in Australia as CFSGAM and as First State Investments elsewhere. The Commonwealth Bank of Australia ("Bank") and its subsidiaries do not guarantee the performance of any investment or entity referred to in this document or the repayment of capital. Any investments referred to are not deposits or other liabilities of the Bank or its subsidiaries, and are subject to investment risk including loss of income and capital invested.

MAR000493_0719_EU/UK