Global Real Return (UCITS) Fund

Year Ending December 31, 2018

OVERVIEW:

The GMO Global Real Return (UCITS) Fund seeks to achieve a return in excess of the OECD G7 Consumer Price Index through investment globally in equities, debt, money market instruments, currencies, instruments relating to commodities indices, REITs and related derivatives.

Performance (%)	
Net of Fees, USD	-5.89
Gross of Fees, Unswung, USD	-5.06
OECD CPI G7 [1]	+1.85
Value Added	**-6.91**

TOP DOWN ALLOCATION: -7.1%

Equity	Alts	Bonds	Cash
▼	▼	▼	▼

SECURITY SELECTION: +0.2%

Equity	Alts	Bonds	Cash
▼	▲	▲	▼

Major Performance Drivers

Equity

Positioning: Equities represented 36.8% of the portfolio at year-end, including 24.7% long-only EM, 7.2% developed ex-US equity, and 4.9% equity extension (a 130% long/30% short strategy comprised of developed ex-US and EM equity).

Results: The equity portfolio returned -15.7% for the year, well behind the MSCI ACWI return of -9.4%. This underperformance was predominantly down to our bias against the US as the S&P 500 index held up much better than other developed and emerging markets, particularly in the first three quarters. Our emerging market stock selection was decently ahead of the benchmark, with a portfolio return of -13.0% against the MSCI Emerging Markets Index return of -14.5%. Stock selection in developed markets proved challenging and our portfolio returned -21.6%, much worse than the MSCI World ex-US index. The ACWI ex-US Equity Extension strategy also underperformed from a stock selection perspective.

Alternatives

Positioning: Alternatives represented 29.6% at year-end, including 8.4% Systematic Global Macro, 5.2% Quality/S&P500, 5.0% merger arbitrage, 4.4% EAFE Value/S&P500, 3.0% relative value interest rates & FX, and 3.5% put selling.

Results: Alternatives returned 2.2% for the year, a very solid result in the context of the severe drawdowns in equity markets. Put selling was hampered by its beta exposure and returned -7.2%. The EAFE Value (currency hedged) vs. S&P 500 trade was down 8.7% and suffered as the US equity market was the top performer, exacerbated by challenges in stock selection. Systematic Global Macro was down 0.4%, largely down to its equity positioning – a modest long position effected by being short the US market versus long emerging and other developed markets. Merger arbitrage was up a solid 2.6% and the Quality vs. S&P 500 trade returned an impressive 7.0% as Quality enjoyed an excellent 2018. Pride of place went to relative value interest rates & FX, up an outstanding 12.2%, driven mostly by long rates positions in Canada and New Zealand and a short position in the Australian dollar.

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Fixed Income

Positioning: Fixed income represented 18.6% of the portfolio at year-end, including 10.8% TIPS, 5.8% asset-backed securities, and 1.9% high-yield and a select number of distressed credits.

Results: Our fixed income strategies returned 0.5% for the year, ahead of the 0.0% return from the Bloomberg Barclays US Aggregate Index. Asset-backed securities were up a solid 3.7% and high yield/distressed was up 2.8%, well ahead of the high yield benchmark, which struggled a little in the risk-off environment and returned -2.3%,. The TIPS exposure was down 1.5% as real 10-year yields in the US drifted from 0.46% at the start of the year to 0.98% at the end of the year (having been as high as 1.17% in November).

Cash/Cash Plus

Positioning: Cash/cash plus represented 15.1% of the portfolio at year-end. We believe cash is an important “dry powder” asset in an investment environment offering limited opportunities.

Results: The allocation to cash/cash plus had a minimal impact on the portfolio returning 1.7% for the year, in line with 3-month US T-Bills.

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[1] The OECD (Organization for Economic Cooperation and Development) CPI (Consumer Price Index) G7 is published monthly by the OECD for the G7 countries of Canada, France, Germany, Italy, Japan, the U.K. and the U.S. The index is compiled by aggregating the national consumer price indices in each period, using estimates of household private final consumption expenditure ("HFCE") as weights. The HFCE for each country is converted into a common currency (U.S. Dollars) using purchasing power parities ("PPPs") which are rates of currency conversion that eliminate the differences in price levels between countries. The PPP used in the zone estimates relate specifically to HFCE and are not the same as the PPP for gross domestic product, which are more commonly available.

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