Monthly Portfolio Update

Pioneer Funds – Top European Players
31 January 2018

Equity
COMMENTARY

Market Review

The European equity market began 2018 on the same positive trajectory as we saw during the final weeks of 2017. In January, the broad European equity market added over 1.5% led higher by some of the more cyclical areas. At sector level, Financials and Consumer Discretionary were the best performing, while Real Estate, Utilities, and Consumer Staples lagged.

Perhaps the most prominent event this month was the January meeting of the ECB. While Mr. Draghi remained quite neutral in his tone, and continued to stress that the ECB would maintain its supportive monetary policy, his comments caused quite an aggressive and somewhat surprising market reaction. Investors appeared to view his comments as being more hawkish than anticipated, and as a result we saw a sharp move higher in bond yields and Euro strength, as equity markets gave back some of the strong performance we have seen during the start of the month. While volatility remains at very suppressed levels compared to historical averages, we did note an uptick in January. This served as a reminder to investors, that the market can be susceptible to short-term swings. For us, the underlying fundamentals supporting the European economy remain firmly in place. Economic data released during the month continued to point to solid growth across the Eurozone, with PMI's remaining at very encouraging levels.

We have been of the view that earnings growth will be the primary catalyst for the market to move higher from here. January marks the beginning of the Q4 2017 earnings season for European companies. While only a small percentage have reported at this point, the positive earnings momentum that we have seen in recent quarters appears to be continuing. With current valuations becoming fuller, the ongoing evidence of earnings growth is key. We continue to believe that the underlying conditions within the European economy provide a fertile environment for companies to deliver, and developments in January have helped to reinforce this view.

Portfolio Review

The Portfolio enjoyed a positive start to 2018, outperforming its benchmark, the MSCI[1] Europe. At sector level. We had a positive contribution from Consumer Discretionary, Information Technology and Consumer Staples. In contrast, some of our holdings in Healthcare detracted.

Within Consumer Discretionary, our holding of auto-component and aerospace company GKN was a standout performer. During the month, UK-listed Melrose Industries (an investment company specialised in the acquisition and improvement of manufacturing businesses) made a bid for GKN which caused quite an aggressive move higher in the share price. We remain holders at this point as we await further details of the proposed deal, and monitor the potential for a more attractive offer.

The Portfolio lost some performance in Healthcare. At stock level, our holding of pharmaceutical company Shire detracted following the release of a business update. From our perspective, the new 2020 revenue guidance of between 17-18 billion USD should be seen as quite supportive, albeit lower than the 20 billion previously stated. Sentiment towards the name remains very weak as investors continue to appear concerned about the potential for pricing pressure coming through in the U.S. – especially related to the haemophilia business. Against this backdrop, any marginal negativity can weigh on the stock, as we saw in January. We continue to believe that the company offers an attractive product pipeline, and that the current valuation appears to be very cheap, which should be supportive over the more medium-term.

Given the more positive environment seen in January, the more defensive areas of the market underperformed. As a result, our underweight exposure to Consumer Staples allowed the Portfolio to gain some relative performance as stocks which we do not own came under some pressure.

In Information Technology, our holding of semiconductor company ASML continued to be a rewarding position. In January, the company reported

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a set of very strong Q4 numbers which came in significantly ahead of both company guidance and investor expectations. The company generated 2.6bn Euros of revenue in the quarter which represents a 34% growth rate (YoY). On top of this, order momentum remains strong with the company reporting a record backlog. The dividend was raised by 17% and the company announced a 2.5bn Euro buyback for 2018/19 which was a clear support for the share price.

The Portfolio lost ground within Materials. In general, we saw a continued rise in commodity prices, helped by the weaker USD. Naturally, this was a tailwind for the mining related companies, and thus our lower exposure to this area of the market impacted in January. Outside of this, our holding of international cement company HeidelbergCement detracted. While company specific newsflow remained quite muted during the month, the shares appeared to be subject to some profit taking in the wake of recent good performance.

Within Industrials, our holding of capital goods company Schneider Electric outperformed. In general, the underlying business trends among the capital goods companies have been solid, with global growth a key support. Results released in January from some key peers suggest that this continues to be the case which was clearly supportive.

Financials were a source of positive returns for the Portfolio throughout the month. Of particular note was the outperformance of Italian banking group Intesa SanPaolo. The company announced that it was considering selling its debt collection arm and a portion of its bad loan portfolio – which represented a shift in strategy. The company's new business plan, set for release in February, will likely put a strong emphasis on further tackling the bad loan issue.

Finally, our underweight position in Utilities was a tailwind. With investors preferring the more cyclical names Utilities underperformed. We maintain our underweight position as we struggle to find attractive quality investment cases within the sector.

Sector Allocation	**Portfolio Weight**	**Benchmark Weight**	**Delta**
Consumer Discretionary	14.60%	10.70%	3.90%
Consumer Staples	10.20%	13.26%	-3.06%
Energy	7.96%	7.29%	0.67%
Financials	21.20%	21.62%	-0.42%
Health Care	17.29%	11.99%	5.30%
Industrials	10.47%	13.27%	-2.80%
Information Technology	5.20%	4.91%	0.29%
Materials	8.97%	8.50%	0.47%
Real Estate	0.00%	1.32%	-1.32%
Telecommunication Serv.	2.77%	3.68%	-0.91%
Utilities	1.23%	3.44%	-2.21%

Source: Amundi Asset Management as at 31 January 2018.

Portfolio Strategy

The strategy of the Portfolio is highly stock driven. We believe that business fundamentals drive a share price over time. A bottom-up, research-driven process can add significant value and help us pursue our objective: to buy quality companies where profitability is undervalued.

Ours is a high conviction approach, which we believe optimises the value of our investment process and we are continuously using our fundamental research capabilities to uncover what we believe to be the most attractive investment opportunities within our investible universe.

There were two new additions to the Portfolio in January.

- Danone

Danone is an international dairy and waters business which has been underperforming operationally for the past 12/18 months. We believe that some key areas of the underperformance, namely the waters business now appear close to trough, and we believe that the company can be successful in turning the business around. We see the company's EBIT target of 16% as achievable, assuming that the cost synergies and dairy margins come through as planned. For us, the current valuation does not look stretched and we see this as an attractive entry point into this global player.

- Smiths Group

Smiths Group is a UK-listed international engineering company. Our investment case is centered on four key pillars. Firstly, we believe that the company enjoys high quality franchises with good exposure to global growth trends. We believe that the company should see organic growth coming through, as cap-ex (especially in the Oil and Gas, and Defense sectors) begins to pick up globally. We see the company's asset base as very attractive, and based on our valuation analysis, we believe that the valuation is undemanding particularly in the context of European industrials which is a relatively richly-valued area of the market at this point.

Top 10 Overweights	Portfolio Weight	Benchmark Weight	Delta
Royal Dutch Shell (B)	5.93%	1.32%	4.61 %
Prudential	4.85%	0.70%	4.15 %
BNP Paribas	4.57%	0.93%	3.64 %
CRH	3.60%	0.31%	3.29 %
GKN	3.03%	0.10%	2.93 %
Alstom	2.66%	0.07%	2.59 %
Roche	4.30%	1.72%	2.58 %
CapGemini	2.78%	0.21%	2.57 %
PaddyPowerBetfair	2.63%	0.09%	2.54 %
Shire	2.95%	0.43%	2.52 %

Source: Amundi Asset Management as at 31 January 2018.

Outlook

As we enter 2018, we maintain our constructive outlook for European equity markets. 2017 was a year for the cyclicals, with the more economically sensitive areas of the market driving the rally. Market movements in January saw a continuation of this trend, as economic data and investor sentiment remained on a strong footing. One sector which somewhat lagged in 2017 was Financials, however with the move higher in long-term interest rates which we saw in January, Financial names were the obvious winner. While we continue to remain cautiously optimistic on our outlook for the sector, we are cognisant of regulatory demands and therefore we remain very selective in our holdings. In keeping with the theme of higher interest rates, much newsflow was centered on the continued strength of the Euro, and the subsequent impact on corporate profitability. For us, the stronger Euro is at least partly the result of improved Eurozone economic fundamentals, and while another significant move higher in the currency would be a clear headwind, we do not see the current level as a threat to our current outlook.

Within our Portfolios, we remain aware of the potential for market rotations, and therefore, as we did throughout 2017, we see the need for balance. We continue to focus on idiosyncratic investment cases which offer us the potential for reliable and sustainable earnings over the medium term.

Important Information

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