Letter from Hamed bin Zayed Al Nahyan

Managing Director

ADIA continued to evolve and refine its organisational structure and processes in 2017, in line with one of its long held beliefs: that even during periods of relative calm, the underlying factors driving global markets are always changing, and often significantly, beneath the surface.

Among the defining themes for the year within ADIA was an intensified focus on strategy and planning. The wide-ranging initiatives we implemented in 2017 and our ongoing efforts in these areas will ensure that all parts of the organisation remain aligned with our long-term objectives and vision. They will also enhance ADIA's ability to adapt swiftly to opportunities in this era of unprecedented technological change.

Since 1976, ADIA has invested through the ups and downs of multiple market cycles.

However, the mission with which we were entrusted 40 years ago, and which remains in place today, requires us to always look beyond short-term market conditions and guard against complacency — even in relatively benign market conditions such as those witnessed in 2017.

It is clear that the pace of change is accelerating, bringing with it substantial opportunities that impose upon us a responsibility to remain open minded and alert at all times. In doing so, we must remain cognisant that long-term success is achieved not through radical changes of direction, but through the thoughtful and measured pursuit of innovation and change that delivers sustainable benefits without undue risk. Our experience over the years has shown that being first is less important than being confident that the choices we make are built on sound analysis and will deliver benefits for years to come. While few things are certain in financial markets, this approach ensures that we, as an organisation and as individuals, have the confidence to move forward swiftly and in a coordinated way to fulfil our shared objectives.

During 2017, ADIA was as focused on self-development as it was on external factors. This included the creation of the Strategy and Planning Department (SPD), tasked with implementing an ADIA-wide planning process to ensure our activities continue to align with ADIA's mission and long-term objectives.

SPD brings together and is responsible for further developing a number of existing functions, from investment strategy, asset allocation, risk management and research, to project management, organisational development and communications.

Among its responsibilities, SPD seeks to foster ongoing internal debate around ADIA's fundamental assumptions and strategic priorities, taking into account changes in the investment environment. It aims to streamline ADIA's structure and processes to reduce complexity and ensure our people have the resources and direction they need to execute effectively on our mission.

In 2017, SPD was involved in further advancing ADIA's Risk-Return project, to create a comprehensive framework that guides ADIA's allocation of risk to investment departments.

This project began in 2016 with the formalisation of our Reference Portfolio, a hypothetical blend of publicly traded securities with fixed weightings. Last year, we went further by consolidating a large number of investment pools, or portfolios, within our departments into single pools; sharpening our focus on the overall performance of each asset class and its consistency with ADIA's return objectives. The move has given our departments greater discretion in how they deploy the capital and risk they have been allocated, to best achieve their performance targets.

There were also a number of adjustments within our departments during 2017. For several years, our Private Equities Department has been increasing its emphasis on principal private equity investments alongside our partners. In 2017, the Department reorganised itself to better support this strategy, moving from product-focused to regional teams with an emphasis on building sector expertise in five key sectors: Financial Services, Healthcare, Industrials, Technology and Consumer.

Also building on the work of previous years, the Fixed Income & Treasury Department took further steps to diversify its portfolio and combine active risks across market segments. This involved expanding its diversified approach across a larger asset base within its operating model, providing investment teams with a larger pool of actively managed assets, while reducing operational overheads.

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In keeping with ADIA's focus on innovations with long-term potential, the Internal Equities Department conducted a study and peer review process into how big data, machine learning and artificial intelligence are changing the investment landscape. The findings of this analysis resulted in the adoption of several initiatives relating to data capture and storage, stock analysis and factor exposures, which have made us more efficient and improved our ability to identify opportunities.

In investment support, the Operations Department completed a valuable benchmarking exercise involving 35 of its global peers that identified several opportunities to improve organisational efficiency and its ability to improve performance within its securities lending activities.

On the investment front, ADIA continued to take advantage of cyclically high prices in some areas to selectively sell assets, while seeking out opportunities in overlooked fields with greater potential.

As in previous years, emerging markets remained a key focus, particularly India and China, as we sought to build further on our knowledge and deepen our relationships in these markets.

In India, ADIA was proud to work closely with and become the first investor in the Indian government-backed National Investment & Infrastructure Fund (NIIF).

Having spent a number of years building its internal capabilities, 2017 was a year of consolidation for ADIA on the recruitment front, as we sought to fine tune our skillset to meet specific needs. The Internal Equities Department, for example, made new appointments to its Europe and Japan teams and to the Department's support functions, while Private Equities appointed a new Head of Asia-Pacific and Head of Industrials as part of its organisational redesign.

Consistent with our focus on the themes and issues shaping financial markets over the long term, ADIA's 2017 Global Investment Forum (GIF) examined climate change and its potential investment impact. The GIF involved the creation of eight internal asset class-specific task forces who considered in detail the potential ramifications for ADIA in the following key areas: Climate Data and Economic Impact, Technology and Energy, Markets and Consumers, and Climate Change Policies.

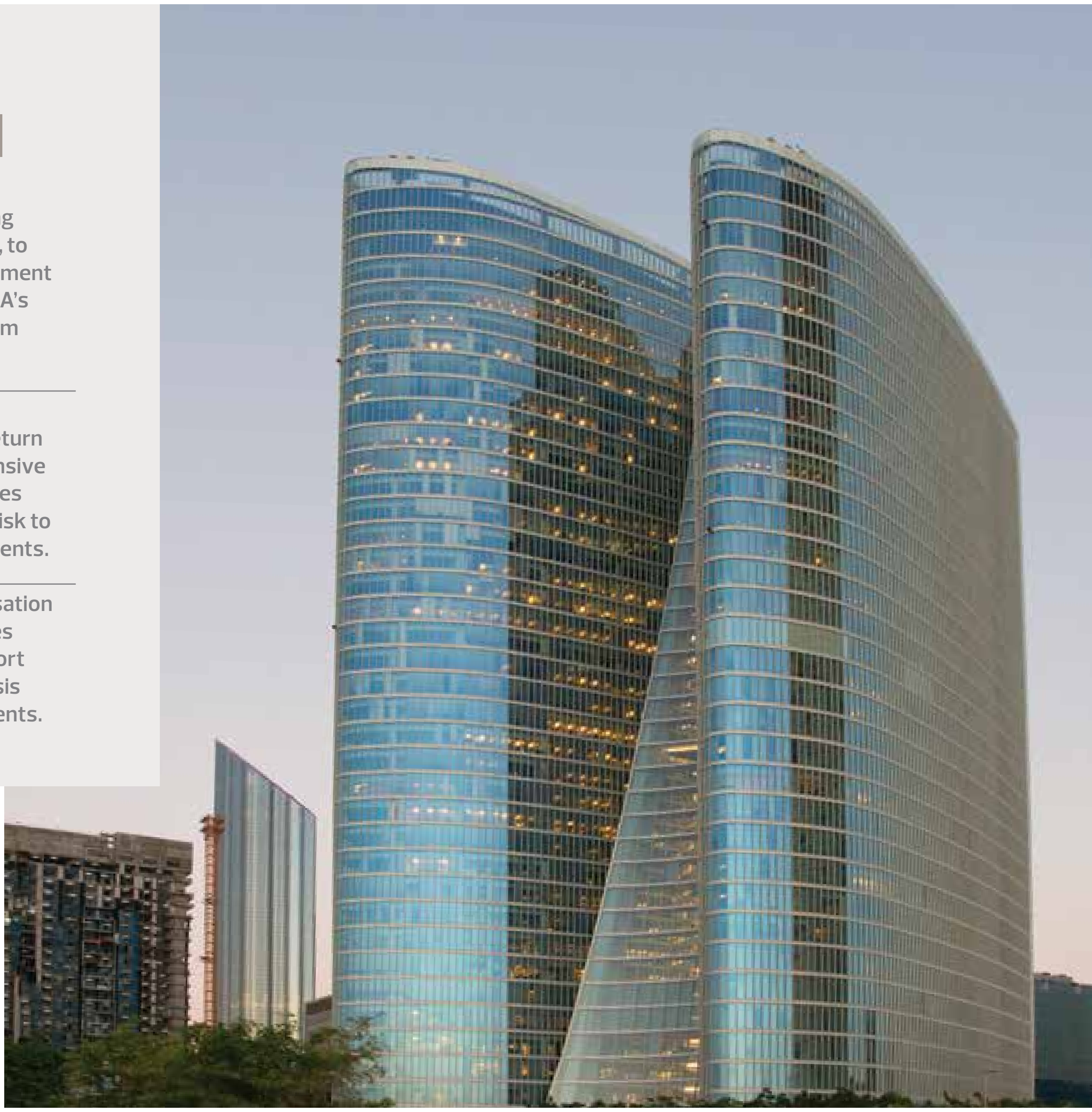
In all, 2017 will be remembered at ADIA as both an eventful and rewarding year during which the organisation demonstrated its discipline in remaining focused on its mission and its pursuit of continuous improvement. I am proud of the significant progress that ADIA has made, not just in pursuing excellence, but in doing so in a thoughtful and responsible way that positions us well for the future.

KEY HIGHLIGHTS

Strategy and Planning Department created, to ensure ongoing alignment of activities with ADIA's mission and long-term objectives.

Important progress made on the Risk-Return project, a comprehensive framework that guides ADIA's allocation of risk to investment departments.

Successful reorganisation of the Private Equities Department to support its increased emphasis on principal investments.



REVIEW OF 2017

Investors were cheered by another strong performance by financial markets in 2017, while a number of underlying, long-term trends continued to gain in prominence and stimulate debate, including demographic shifts, the impact of technology and climate change.

In investment terms, 2017 provided a reminder of the ability of capital markets to surprise – in this case, in a positive way. Global equity markets appreciated close to 25% in U.S. Dollar terms. Even with lacklustre results from global bonds, balanced portfolio returns reached high double digits.

"Rising geopolitical risk" was a common refrain last year, but few of these risks materialised into actual events that impacted economies, allowing most major markets to respond by recording their best performance of the post-financial crisis expansion.

Good returns were widespread across equity markets and credit-sensitive bond markets, with 22% returns in U.S. equities, 25% in other developed markets, and over 37% in emerging markets. U.S. Treasuries returned only about 2% for the year; a solid outcome given global growth rates. But both U.S. high yield debt and global investment grade bonds returned 7.5% as credit performed well and the U.S. Dollar depreciated significantly.

In early 2018, conditions in the global economy appeared relatively robust. Growth was well balanced across regions and was benefitting workers in many economies, while the most common causes of recessions – above-target inflation and monetary restraint – remained absent. Central banks and other policy makers have begun to rein in the expansionary policies of the past several years but have done so to date in a cautious and measured way. Nonetheless, equity markets suffered bouts of volatility in early 2018, perhaps anticipating a more challenging environment in the year ahead. Given low volatility in 2017, some normalisation would not be surprising.

Of course, markets have cycles, and risk factors can always be identified: high levels of debt as well as inequality of income and wealth are often cited. But these are more secular concerns rather than factors that typically put a brake on good cyclical performance.

OUTLOOK

The experience of 2017 could lead to the view that market forecasting is of little value, and may even be dangerous if it results in unnecessary caution that dampens returns. That would be the wrong conclusion to draw. Economies and markets do have cycles. While it is clear that asset prices were locked in an especially benign up-cycle throughout 2017, we know that while such periods may continue for some time, they will eventually turn. Trying to time markets is extremely difficult, and dangerous, for large and diversified global investors. A more practical approach is to view cycles as opportunities, and to prepare strategies that limit drawdowns and provide sufficient available capital to take advantage of lower asset prices when markets turn lower. Experience has shown us that this approach is most likely to result in long-term and sustainable wealth accumulation.

More importantly, there are always trends hidden beneath cycles. Identifying those trends, and positioning to profit from them across cycles, is more likely to result in consistent, long-term returns than attempting to time the market.

Ageing populations will have a gradual yet significant impact on most Western societies, notably by imposing declining work forces and rising pressures on their government spending.

Emerging markets continue to expand their share of the global economy. More importantly, their governance and engagement with the world continue to improve. The introduction of GST in India and continued reforms of financial regulation in China are only two recent examples of this trend.

The world's energy industry is in the early stages of a fundamental shift from fossil fuels to a more sustainable reliance on a range of renewable technologies. At ADIA, we went through a thorough review last year of the important reality of climate change and of its potential impact, in order to assess how markets and governments could respond to this impending transition.

The exact paths of this process remain to be seen, but we are excited by the opportunities that are coming into view, and others that are sure to arise, to deploy capital in support of new fields of investment.

Technology is also driving powerful changes in economies and markets. One need only look at the performance of technology across global equity markets last year to recognise that something is stirring. This technology boom is based on real improvements in computing power to process and analyse exponentially growing volumes of data. It underpins real businesses that are growing revenues, market share, and earnings. The societal changes range from retailing to automobiles, from medicine to legal services. Also, importantly, our own business of investing is absorbing new tools and approaches that can improve abilities to identify opportunities and manage risk.

Finally there are the geopolitical risks that always feed into investment commentary. A long view of investment history shows that there are always geopolitical risks. Only by looking objectively into the past does it become clear that current risks are not unusually important, or more prevalent, than in other periods. History also has shown that humanity is resilient. While economic and political breakdowns do happen, the global system survives and a well-diversified portfolio can perform in the way that it was designed and meet its objectives even in difficult periods.

This is not a call to complacency, as changes now underway have the potential to impact the investing climate for many years to come.

However, we remain confident that these "risks" all contain elements of opportunity, which provides long-term investors with cause for optimism even as the current economic cycle approaches maturity.