CanterburyConsulting

Quarterly Asset Class Report

Global Equity

June 30, 2016

canterburyconsulting.com

Role in the Portfolio

Canterbury Consulting recommends and communicates asset-class strategy with the objective of constructing a diversified portfolio of long-only equity strategies designed to (in aggregate):

(i) Provide growth of portfolio assets in excess of inflation and spending rates

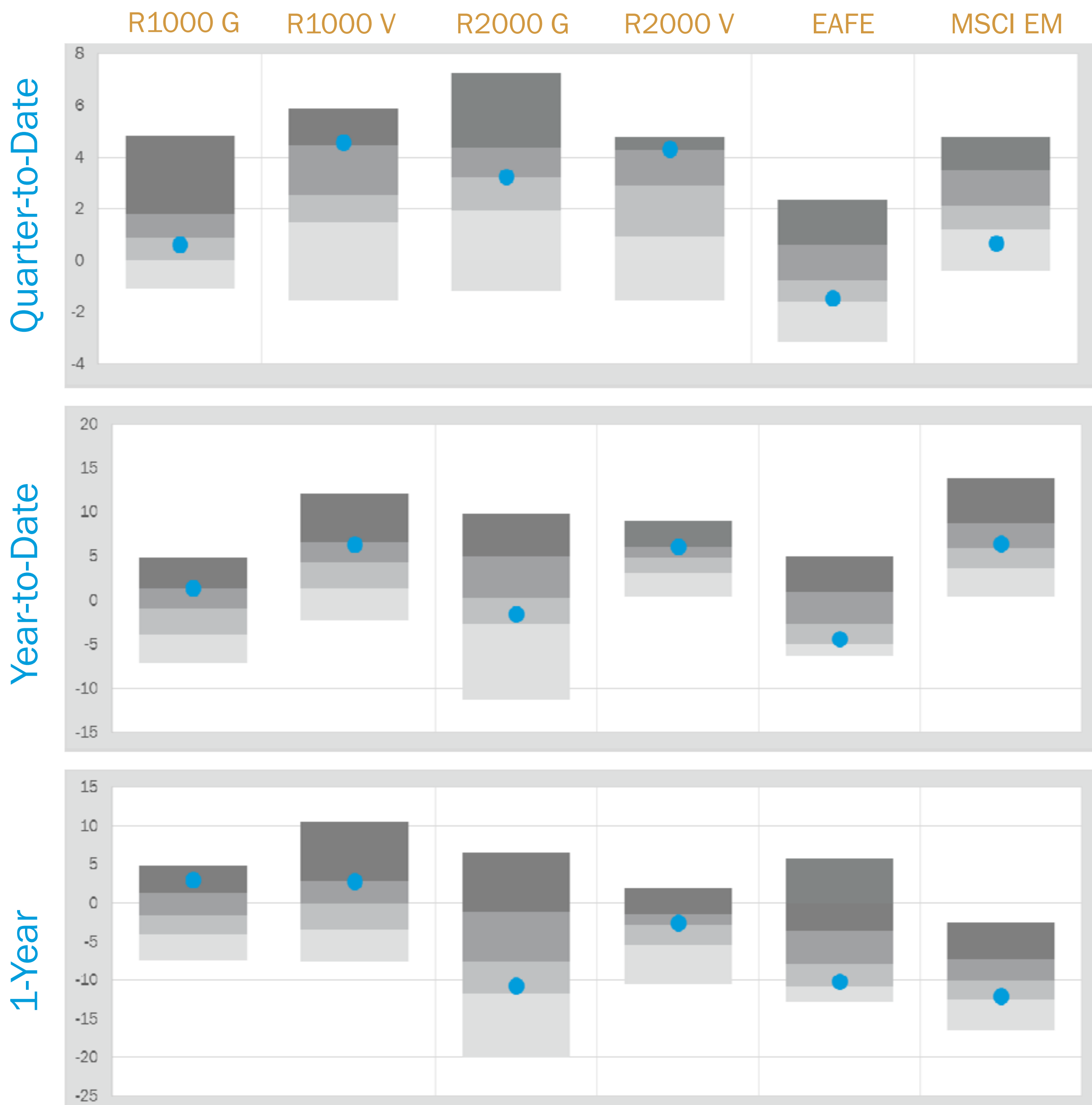
(ii) Maintain comparable exposure to the global equity market

(iii) Exhibit returns uncorrelated to fixed income markets

Role	Asset Categories	Risks
Growth	**Public and Private Equity**	**Market Decline**
Capital Preservation	Fixed Income, Hedge Funds	Rising Interest Rates, Highly Correlated Markets
Inflation Protection	Real Assets: Real Estate, Commodities	Deflation

- Canterbury global equity portfolios are expected to deliver consistent net of fees excess returns and moderate tracking error versus the MSCI All Country World Index over longer periods of time
- Relative to the index, Canterbury equity portfolios will employ higher allocations to small- and mid-cap equities, comparable volatility (achieved through manager selection), and moderate tracking error

Performance (%) as of June 30, 2016



Blue dots represent the returns of the benchmark; gray floating bar charts represent the peer groups by quartile
Source: Morningstar Direct

- During the second quarter, value indices continued to outperform growth in the U.S. With Treasury yields reaching historic lows, demand has increased for higher-yielding equities which typically reside in value sectors such as telecommunications, utilities, consumer staples, and financials
- Both international developed and emerging markets managers have fared well against their passive benchmarks. In each of these categories, roughly 75% of active managers outperformed their benchmarks during the quarter and the trailing twelve months
- Emerging markets outperformed international developed markets. The result of the ‘Brexit’ referendum, in which the UK voted to leave the EU, is seen as more negative for developed European countries than for emerging markets. Emerging countries as a whole have limited ties to the EU

Market Capitalization Mix

Equity Review

Equity: U.S. Market Cap		Current	10 Year Avg	Deviation from Mean*	Large	Neutral	Small
Valuation	Russell Top 200 Current P/E (Large Cap)	19.43	15.77	2.05			++
	R2000 Current P/E (Small Cap)	40.58	82.93	-1.07			+
	Avg P/E Ratio (Large/Small)	0.48	0.41	0.52		-	
	Russell Top 200 EV/EBITDA^ (Large Cap)	12.15	9.96	1.59			+
	R2000 EV/EBITDA (Small Cap)	20.69	13.38	2.64	++		
	Avg EV/EBITDA Ratio (Large/Small)	0.59	0.76	-1.44	+		
	Russell Top 200 P/S (Large Cap)	1.98	1.56	1.61			+
	R2000 P/S (Small Cap)	1.10	1.02	0.41		-	
	Avg P/S Ratio (Large/Small)	1.80	1.54	2.51			++
Solvency	Russell Top 200 Debt/EBITDA (Large Cap)	4.52	4.78	-0.31		-	
	Russell 2000 Debt/EBITDA (Small Cap)	8.23	5.36	2.95	++		
	Avg Debt/EBITDA Ratio (Large/Small)	0.55	0.91	-1.49	+		
Growth	Russell Top 200 LT EPS Gr (Fwd) (Large Cap)	8.20	8.84	-0.01		-	
	R2000 LT EPS Gr (Fwd) (Small Cap)	8.30	10.91	-1.42	+		
	Avg Growth Ratio (Large/Small)	0.99	0.83	0.03		-	
Economy	Case Shiller Home Price (YoY)	5.44	-0.28	0.64		-	
	Total Leading Economic Indicators	123.70	111.23	1.24			+
	Currency (USD v Broad Basket)	96.14	82.58	1.97			+
	Curve Steepness 2's to 10's	0.89	1.65	-0.95		-	

**Deviation from mean represents how many standard deviations the current value is above or below the 10-year average, also known as the "Z-Score". '+' denotes one standard deviation, and '++' denotes two standard deviations in favor of the asset class*
^EV/EBITDA, also known as the "enterprise multiple," is a ratio used to determine the value of a company. Unlike P/E, the enterprise multiple takes debt into account. This is often the ratio used by companies looking to acquire another business

- There are various valuation metrics used to determine the relative attractiveness of the equity universe – Canterbury prefers Price/Earnings, EV/EBITDA, and Price/Sales. No one metric is a sole determinant
- Large-cap stocks are expensive based on all three metrics. Small-cap stocks are relatively attractive, but their high levels of debt cause them to appear expensive based on the EV/EBITDA multiple
- Leverage continues to be a greater issue for small-cap stocks than for large-cap stocks
- Growth estimates favor large-cap stocks based on long-term averages, but the current levels are fairly even.
- Healthy economic indicators are a positive for the outlook on small-cap stocks, which are typically more economically sensitive and domestically oriented
- <u>Advantage: Small-Cap Equities relative to Large-Cap Equities</u>

Source: Russell

Region Mix – U.S. vs. Global

Equity: Region (U.S./Global)		Current	10 Year Avg	Deviation from Mean*	U.S.	Neutral	R.O.W.
Valuation	S&P 500 Current P/E	19.45	16.62	1.38			+
	MSCI ACWI Current P/E	19.96	16.53	0.90		-	
	Avg P/E Ratio (US /ACWI)	0.97	1.01	-0.38		-	
	S&P 500 EV/EBITDA^	12.84	10.07	2.19			++
	MSCI ACWI EV/EBITDA	11.56	9.56	1.76	+		
	Avg EV/EBITDA Ratio (US/ACWI)	1.11	1.06	1.45			+
	S&P 500 P/S	1.88	1.46	1.55			+
	MSCI ACWI P/S	1.42	1.21	1.06	+		
	Avg P/S Ratio (US/ACWI)	1.32	1.20	1.30			+
Solvency	S&P 500 Debt/EBITDA	4.59	4.76	-0.21		-	
	MSCI ACWI Debt/EBITDA	6.61	6.39	0.34		-	
	Avg Debt/EBITDA Ratio (US/ACWI)	0.69	0.74	-0.61		-	
Growth	S&P 500 LT EPS Gr (Fwd)	8.44	8.79	-0.06		-	
	MSCI ACWI LT EPS Gr (Fwd)	6.96	9.42	-0.13		-	
	Avg Growth Ratio (US/ACWI)	1.21	0.96	0.34		-	
Economy	Currency (USD v Broad Basket)	96.14	82.58	1.97			+

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- Both U.S. and rest of the world ("R.O.W.") stock valuations are well above historical norms. On a relative basis, the U.S. currently appears more expensive
- The solvency data has stayed tame, suggesting that leverage is at healthy levels for both U.S. and R.O.W. stocks
- Forward growth estimates have been reduced and are slightly below historical averages across the board
- The U.S. Dollar strengthened vs. a broad basket of currencies during the quarter. The strong dollar has been a headwind to U.S. companies that export their goods and services overseas
- <u>Advantage: Non-U.S. Equities relative to Global Equities</u>

Source: MSCI and Standard & Poor's

Region Mix – Non-U.S. Developed vs. Global

Equity: Region (Non-U.S. Dev/Global)		Current	10 Year Avg	Deviation from Mean*	Non-U.S. Dev	Neutral	R.O.W.
Valuation	MSCI EAFE Current P/E	19.92	18.69	0.07		-	
Valuation	MSCI ACWI Current P/E	19.96	16.53	0.90		-	
Valuation	Avg P/E Ratio (EAFE/ACWI)	1.00	1.10	-0.22		-	
Valuation	MSCI EAFE EV/EBITDA^	10.24	9.20	0.94		-	
Valuation	MSCI ACWI EV/EBITDA	11.56	9.56	1.76	+		
Valuation	Avg EV/EBITDA Ratio (EAFE/ACWI)	0.89	0.97	-1.53	+		
Valuation	MSCI EAFE P/S	1.06	0.98	0.45		-	
Valuation	MSCI ACWI P/S	1.42	1.21	1.06	+		
Valuation	Avg P/S Ratio (EAFE/ACWI)	0.74	0.81	-1.51	+		
Solvency	MSCI EAFE Debt/EBITDA	9.16	8.87	0.27		-	
Solvency	MSCI ACWI Debt/EBITDA	6.61	6.39	0.34		-	
Solvency	Avg Debt/EBITDA Ratio (EAFE/ACWI)	1.39	1.39	0.00		-	
Growth	MSCI EAFE LT EPS Gr (Fwd)	4.98	6.04	-0.03		-	
Growth	MSCI ACWI LT EPS Gr (Fwd)	6.96	9.42	-0.13		-	
Growth	Avg Growth Ratio (EAFE/ACWI)	0.72	0.68	0.01		-	
Economy	USD/EUR	1.11	1.32	-1.78	+		

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- Non-U.S. developed countries remain attractively valued versus the R.O.W. based on all three valuation metrics. These countries' equities were the most challenged following the 'Brexit' vote that took markets by surprise
- Debt levels are in line with historical norms, with neither region having an advantage
- Forward growth estimates for global equities fell slightly during the quarter but are slightly above historical averages
- The U.S. dollar strengthened vs. the Euro over the quarter, after the result of the 'Brexit' referendum sparked a selloff in Euros. This was a tailwind to European companies with costs based in Europe and revenues coming from the U.S.
- <u>Advantage: Non-U.S. Developed Equities relative to Global Equities</u>

Source: MSCI

Region Mix – Emerging Markets vs. Global

	Equity: Region (EM/Global)	**Current**	**10 Year Avg**	**Deviation from Mean***	**EM**	**Neutral**	**R.O.W.**
Valuation	MSCI EM Current P/E	14.59	13.25	0.49		-	
	MSCI ACWI Current P/E	19.96	16.53	0.90		-	
	Avg P/E Ratio (EM/ACWI)	0.73	0.80	-0.67		-	
	MSCI EM EV/EBITDA^	8.61	7.95	0.49		-	
	MSCI ACWI EV/EBITDA	11.56	9.56	1.76	+		
	Avg EV/EBITDA Ratio (EM/ACWI)	0.74	0.83	-0.81		-	
	MSCI EM P/S	1.16	1.23	-0.25		-	
	MSCI ACWI P/S	1.42	1.21	1.06	+		
	Avg P/S Ratio (EM/ACWI)	0.81	1.03	-1.07	+		
Solvency	MSCI EM Debt/EBITDA	4.83	3.32	1.72			+
	MSCI ACWI Debt/EBITDA	6.61	6.39	0.34		-	
	Avg Debt/EBITDA Ratio (EM/ACWI)	0.73	0.53	1.17			+
Growth	MSCI EM LT EPS Gr (Fwd)	7.77	10.27	-0.21		-	
	MSCI ACWI LT EPS Gr (Fwd)	6.96	9.22	-0.29		-	
	Avg Growth Ratio (EM/ACWI)	1.12	1.08	0.07		-	

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- Emerging markets ("EM") stocks are attractively valued compared to the R.O.W. based on all three valuation metrics
- Similar to domestic small-cap stocks, the risk to EM equities lies in their high level of leverage compared to historical norms
- Growth estimates are relatively low for both EM and R.O.W., with neither region at a significant advantage
- Advantage: Emerging Markets Equities relative to Global Equities

Source: MSCI

Portfolio Characteristics

Recommended Ranges

Market Cap (U.S.)	Minimum	Maximum	R3000
Large Cap (> $25.5B)	50.0%	70.0%	68.0%
Mid Cap ($3B - $25.5B)	25.0%	40.0%	26.0%
Small Cap (< $3B)	2.5%	12.5%	6.0%

Region	Minimum	Maximum	MSCI ACWI
U.S.	45.0%	65.0%	53.1%
Non-U.S. Developed	25.0%	40.0%	36.9%
Emerging Markets	5.0%	20.0%	10.0%

Client objectives and constraints may cause allocations to vary from recommended ranges

- Canterbury has been decreasing its home country bias as U.S. equity valuations remain stretched and the strong dollar presents a headwind for American companies with global operations
- Our market cap exposures are currently in a more neutral position. Valuation, growth, and economic indicators do not support a major shift at this time
- As the equity market cycle matures, Canterbury believes its utilization of active managers that can avoid overvalued regions, sectors, and securities will be a strong value-add