CanterburyConsulting

Quarterly Asset Class Report

Hedge Funds

canterburyconsulting.com

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Role in the Portfolio

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

(i) Preserve capital and mitigate volatility

(ii) Maintain exposure to a diversified set of securities in global markets

(iii) Exhibit uncorrelated investment returns

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

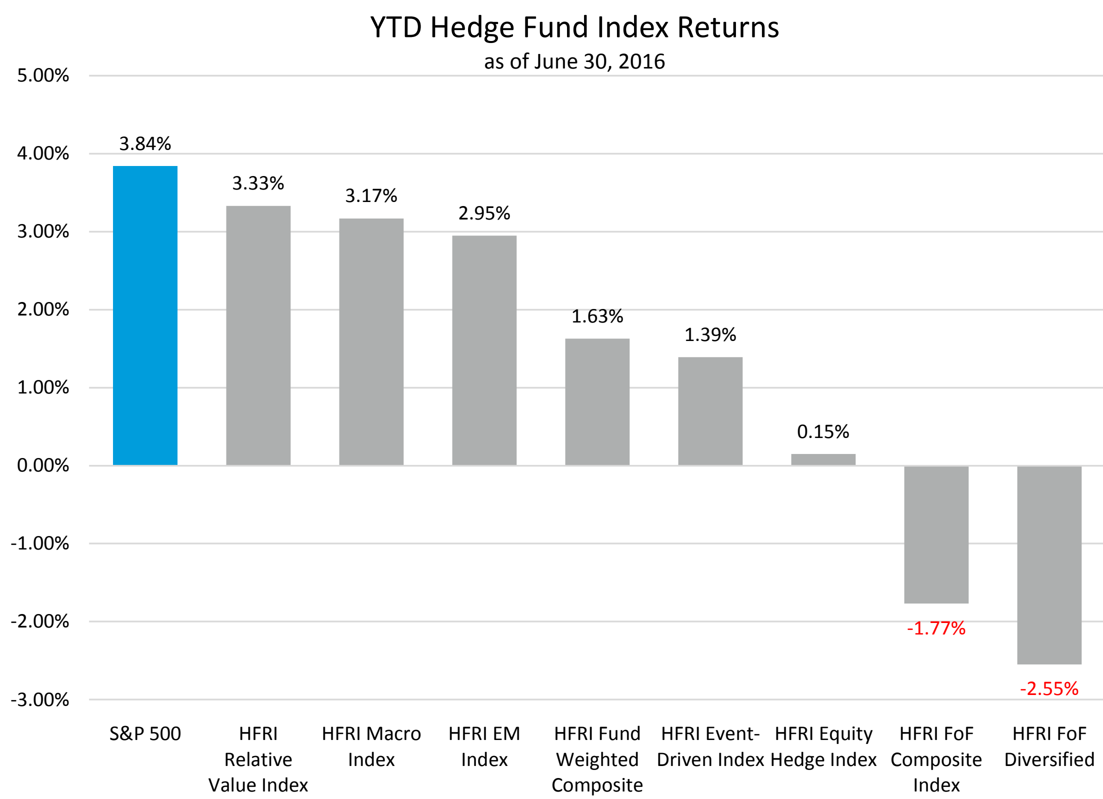
— Canterbury Consulting recommends a diversified mix of long/short equity, long/short credit and multi-strategy managers for client portfolios. We depend on managers with strategies that rely upon superior security selection and portfolio management, not leverage or quantitative models, to generate performance

— Short term returns from Canterbury hedge funds may act differently than broad market indices, but they should generally protect from losses in negative markets and participate with the gains of positive markets

— Over a full market cycle, Canterbury hedge fund portfolios are expected to produce market-like returns with a significantly lower volatility profile

Second Quarter 2016

Hedge Fund Review



Source: HFRI

- Second quarter performance was disappointing as hedge funds continued the negative alpha from the first quarter, especially within long/short equity
- Strength continues to be in stocks with high dividends while there has been weakness is hedge fund heavy sectors like Healthcare
- Markets experienced volatility with increased frequency due to Brexit and other macro factors, catching many funds on the wrong side, leading to poor second quarter performance
- Credit strategies continued to perform well as yields were lower and the high yield market posted strong gains for the year

Drivers of Performance

- Quantitative Easing (QE) policies internationally have reduced yields
  - Quantitative Easing policies are in full effect in European and Japanese markets taking yields in many countries into negative territory
  - While the yields have dropped, they have lifted the price of dividend paying equities while other equities have not performed as well due to the economic uncertainty
  - The excess liquidity resulting from lower yields has made its way across many asset classes including gold, oil and equities
- Robust opportunity set to generate returns
  - The dispersion with weakness in healthcare and strength in materials has led to poor performance this year but has generated a good opportunity set on the long and short side going forward
  - Currencies and commodities continued to experience volatility, which have been a headwind to performance but should dissipate as volatility is reduced and focus of the market returns to fundamentals
- Credit and Multi-Strategy lead
  - After a period of trailing other strategies, credit and multi-strategy have performed well this year, generating uncorrelated returns despite volatility in the markets
  - Energy bonds recovered from a challenging year in 2015 as oil prices rebounded from historically low levels

Canterbury Consulting recommends a diversified mix of long/short equity, long/short credit, and multi-strategy managers. We expect positive absolute and relative returns from hedge fund strategies as the market headwinds that have accompanied this prolonged rally dissipate

— Hedge fund managers and Canterbury Consulting expect markets to experience volatility with greater frequency in 2016 that will create long and short opportunities across equity and credit securities

— Long/short equity returns could outperform multi-strategy managers as well as long/short credit managers for an extended period. This is a reversal from the longer term trend and the year to date trend, but we believe that this could persist for some time going forward due to the lack of distressed credit and special situation opportunities

— Historically, rising rate environments have favored actively managed investment strategies. Falling rates has supported positive market returns, but with interest rate hikes in our future, Canterbury is focused on recommending exposure to a diversified line-up of managers that can generate alpha through portfolio management and superior security selection

— Canterbury expects managers who excel at exposure management, security selection and position sizing to outperform benchmarks in a market with increased volatility and dispersion of investment returns

— Canterbury recommends that clients keep their hedge fund allocations at target weights with an even split between long/short equity and multi-strategy/credit hedge funds