CanterburyConsulting

Quarterly Asset Class Report

Global Equity

canterburyconsulting.com

March 31, 2017

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

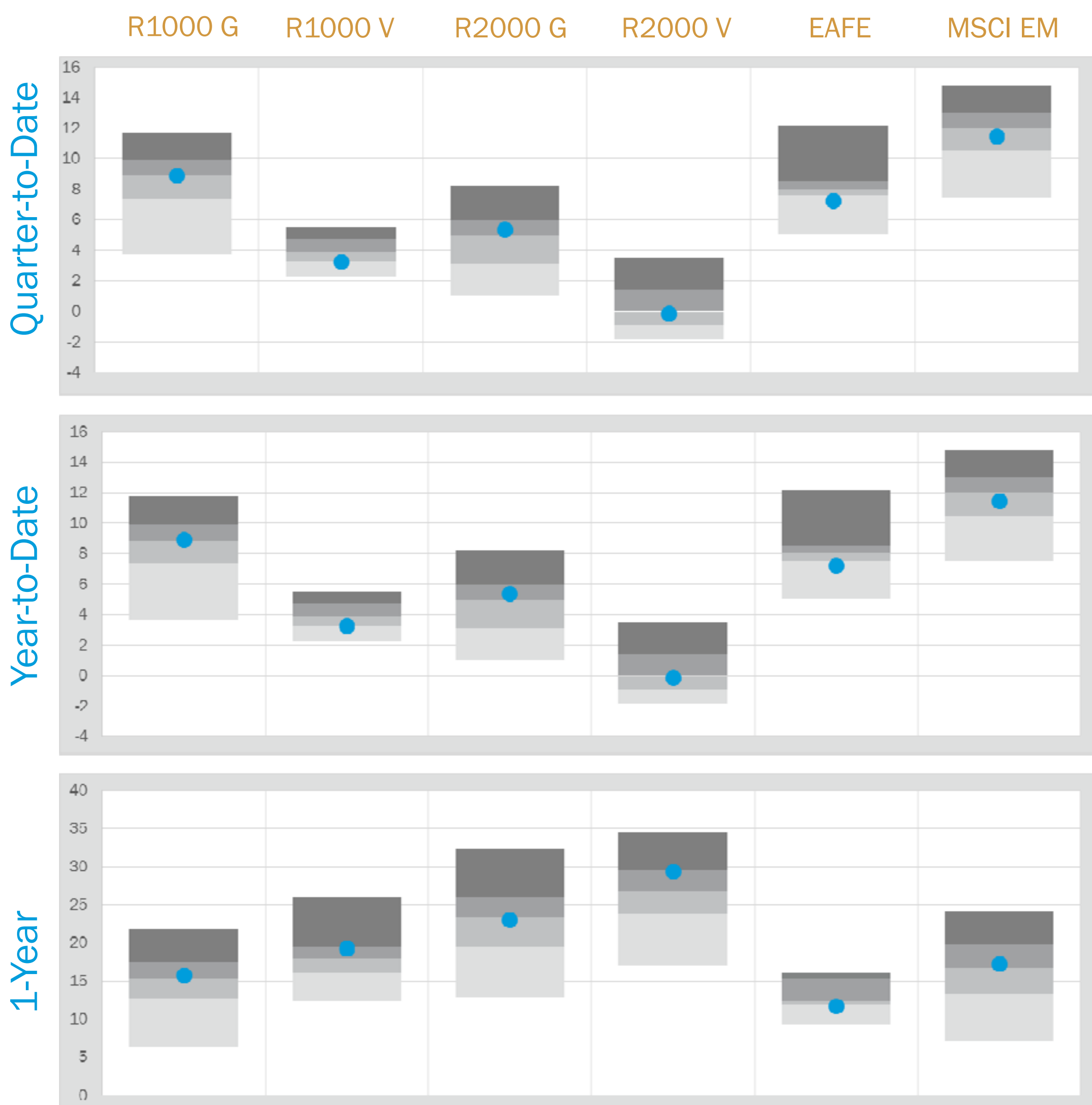
(ii) Maintain comparable exposure to the global equity market

(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

Performance (%) as of March 31, 2017



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

- In U.S. equities, growth beat value and large-caps beat small-caps, reversing the previous quarter's trend. Many of the popular "Trump trades" stalled in 1Q amidst policy uncertainty, while technology stocks rallied as investors sought sources of idiosyncratic growth
- In aggregate, almost 50% of mutual fund managers outperformed their respective benchmarks in 1Q, a notable improvement from the 19% that outperformed in calendar 2016. Active managers fared best in U.S. large value as well as international developed equities
- After lagging in the previous quarter, non-U.S. stocks, particularly in emerging markets, rallied in 1Q. With global growth poised for modest improvement, some economists are predicting an end to quantitative easing in both Europe and China in 2017

Market Capitalization Mix

	Equity: U.S. Market Cap	Current	10 Year Avg	Deviation from Mean*	Large	Neutral	Small
Valuation	Russell Top 200 Current P/E (Large Cap)	21.41	16.10	2.43			++
	R2000 Current P/E (Small Cap)	47.57	44.01	0.34		-	
	Avg P/E Ratio (Large/Small)	0.45	0.45	0.00		-	
	Russell Top 200 EV/EBITDA^ (Large Cap)	12.59	10.05	1.72			+
	R2000 EV/EBITDA (Small Cap)	17.44	13.88	1.14	+		
	Avg EV/EBITDA Ratio (Large/Small)	0.72	0.74	-0.13		-	
	Russell Top 200 P/S (Large Cap)	2.18	1.58	2.02			++
	R2000 P/S (Small Cap)	1.29	1.03	1.29	+		
	Avg P/S Ratio (Large/Small)	1.69	1.56	1.24			+
Solvency	Russell Top 200 Debt/EBITDA (Large Cap)	4.34	4.66	-0.42		-	
	Russell 2000 Debt/EBITDA (Small Cap)	6.19	5.57	0.59		-	
	Avg Debt/EBITDA Ratio (Large/Small)	0.70	0.86	-0.70		-	
Growth	Russell Top 200 LT EPS Gr (Fwd) (Large Cap)	6.70	8.75	-0.03		-	
	R2000 LT EPS Gr (Fwd) (Small Cap)	7.83	10.71	-1.46	+		
	Avg Growth Ratio (Large/Small)	0.86	0.83	0.06		-	
Economy	Case Shiller Home Price (YoY)	5.73	-0.14	0.66		-	
	Total Leading Economic Indicators	126.20	111.06	1.51			+
	Currency (USD v Broad Basket)	100.35	83.65	2.06			++
	Curve Steepness 2's to 10's	1.13	1.74	-0.90		-	

**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 got more expensive during the quarter while small-cap stocks got cheaper, making small companies more attractive from a valuation perspective
- Leverage declined modestly for small-cap stocks, so solvency risk is no longer as significant
- Growth estimates declined across the board, particularly for small companies. This is the only area in which large-cap stocks are relatively attractive
- Positive leading economic indicators and a strong dollar are positives for small-cap stocks, which tend to be more domestically-oriented
- Advantage: U.S. small-cap relative to U.S. large-cap stocks

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	21.75	16.98	2.06			++
Valuation	MSCI ACWI Current P/E	21.02	16.89	1.05	+		
Valuation	Avg P/E Ratio (US /ACWI)	1.03	1.01	0.23		-	
Valuation	S&P 500 EV/EBITDA^	13.04	10.03	1.96			+
Valuation	MSCI ACWI EV/EBITDA	11.64	9.64	1.59	+		
Valuation	Avg EV/EBITDA Ratio (US/ACWI)	1.12	1.04	1.65			+
Valuation	S&P 500 P/S	2.08	1.49	1.94			+
Valuation	MSCI ACWI P/S	1.58	1.22	1.72	+		
Valuation	Avg P/S Ratio (US/ACWI)	1.32	1.22	1.09			+
Solvency	S&P 500 Debt/EBITDA	4.30	4.68	-0.48		-	
Solvency	MSCI ACWI Debt/EBITDA	5.91	6.37	-0.70		-	
Solvency	Avg Debt/EBITDA Ratio (US/ACWI)	0.73	0.73	0.00		-	
Growth	S&P 500 LT EPS Gr (Fwd)	7.14	9.62	-0.02		-	
Growth	MSCI ACWI LT EPS Gr (Fwd)	10.40	8.92	0.10		-	
Growth	Avg Growth Ratio (US/ACWI)	0.69	0.87	-0.05		-	
Economy	Currency (USD v Broad Basket)	100.35	83.65	2.06			++

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- U.S. stock valuations rose while rest of the world ("R.O.W.") valuations stayed fairly constant, so non-U.S. equities continue to be attractive on a relative valuation basis
- Debt levels are below long-term averages both U.S. and R.O.W. stocks, suggesting healthy leverage conditions
- Growth estimates are in line with historical averages both within and outside of the U.S.
- The U.S. dollar weakened slightly but remains at a highly elevated level. The dollar's strength hurts U.S. exporters and benefits foreign companies that export goods and service into the U.S.
- Advantage: non-U.S. relative to U.S. equities

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	23.98	18.41	0.45		-	
	MSCI ACWI Current P/E	21.02	16.89	1.05	+		
	Avg P/E Ratio (EAFE/ACWI)	1.14	1.07	0.26		-	
	MSCI EAFE EV/EBITDA^	10.11	9.09	0.93		-	
	MSCI ACWI EV/EBITDA	11.64	9.64	1.59	+		
	Avg EV/EBITDA Ratio (EAFE/ACWI)	0.87	0.94	-2.53	++		
	MSCI EAFE P/S	1.18	0.97	1.22			+
	MSCI ACWI P/S	1.58	1.22	1.72	+		
	Avg P/S Ratio (EAFE/ACWI)	0.75	0.80	-1.19	+		
Solvency	MSCI EAFE Debt/EBITDA	7.76	9.05	-1.31	+		
	MSCI ACWI Debt/EBITDA	5.91	6.37	-0.70		-	
	Avg Debt/EBITDA Ratio (EAFE/ACWI)	1.31	1.42	-1.66	+		
Growth	MSCI EAFE LT EPS Gr (Fwd)	41.19	5.98	0.69		-	
	MSCI ACWI LT EPS Gr (Fwd)	10.40	8.92	0.10		-	
	Avg Growth Ratio (EAFE/ACWI)	3.96	0.88	0.78		-	
Economy	USD/EUR	1.07	1.30	-1.79	+		

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^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

- Non-U.S. developed equities remain attractively valued relative to the R.O.W.
- Debt levels in non-U.S. developed companies declined, making them safer from a leverage perspective
- Growth estimates for non-U.S. developed companies turned negative during the quarter while estimates for the R.O.W. increased
- The U.S. dollar appreciated significantly vs. the euro. The dollar's strength benefits European exporters who have costs in euros and revenues in dollars
- Advantage: non-U.S. developed equities relative to the rest of the world

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	15.54	13.49	0.75		-	
	MSCI ACWI Current P/E	21.02	16.89	1.05	+		
	Avg P/E Ratio (EM/ACWI)	0.74	0.80	-0.56		-	
	MSCI EM EV/EBITDA^	9.36	8.02	1.06			+
	MSCI ACWI EV/EBITDA	11.64	9.64	1.59	+		
	Avg EV/EBITDA Ratio (EM/ACWI)	0.80	0.83	-0.32		-	
	MSCI EM P/S	1.30	1.21	0.32		-	
	MSCI ACWI P/S	1.58	1.22	1.72	+		
	Avg P/S Ratio (EM/ACWI)	0.82	1.01	-0.89		-	
Solvency	MSCI EM Debt/EBITDA	4.81	3.54	1.46			+
	MSCI ACWI Debt/EBITDA	5.91	6.37	-0.70		-	
	Avg Debt/EBITDA Ratio (EM/ACWI)	0.81	0.57	1.49			+
Growth	MSCI EM LT EPS Gr (Fwd)	11.42	8.60	0.06		-	
	MSCI ACWI LT EPS Gr (Fwd)	10.40	8.92	0.10		-	
	Avg Growth Ratio (EM/ACWI)	1.10	0.80	0.52		-	

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- Valuations are stretched across the globe, but even after the rally in 1Q, emerging markets ("EM") stock valuations are not as stretched as the R.O.W.
- Debt levels have come down for both categories, but the solvency data continue to favor global equities relative to emerging markets
- Growth estimates for emerging markets companies increased significantly during the quarter, but neither emerging markets nor global equities have a relative advantage
- <u>No relative advantage between emerging markets and global equities</u>

Source: MSCI

Portfolio Characteristics

Recommended Ranges

Market Cap (U.S.)	Minimum	Maximum	R3000
Large Cap (> $25.3B)	50.0%	70.0%	68.0%
Mid Cap ($2.7B - $25.3B)	25.0%	40.0%	26.2%
Small Cap (< $2.7B)	2.5%	12.5%	5.8%

Region	Minimum	Maximum	MSCI ACWI
U.S.	45.0%	65.0%	54.0%
Non-U.S. Developed	25.0%	40.0%	35.7%
Emerging Markets	5.0%	20.0%	10.3%

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