CanterburyConsulting

Quarterly Asset Class Report

Global Equity

canterburyconsulting.com

June 30, 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

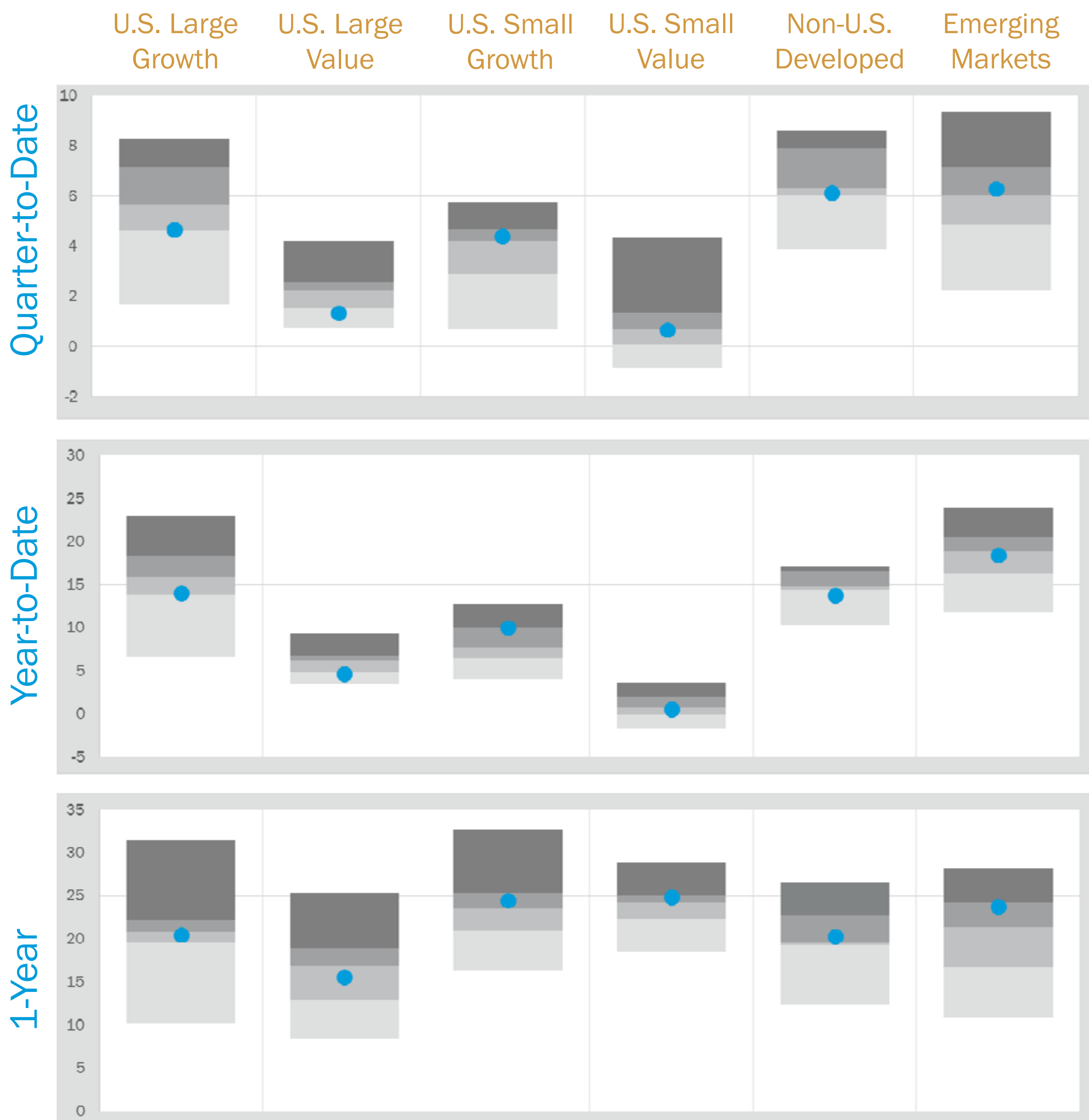
(ii) Maintain comparable exposure to the global equity market

(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 June 30, 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 continued to outpace value in the second quarter. After neglecting them for most of 2016, investors heavily favored earnings growth and momentum factors. Growth managers who stayed true to their style bounced back in the first half of 2017

- U.S. large-cap managers had another strong relative quarter. Around 75% of them beat their benchmarks. Sector positioning was a tailwind, as active managers have remained overweight to healthcare, technology, and discretionary sectors and underweight to staples, utilities, and telecom

- Non-U.S. equities performed better than their U.S. counterparts. Improving consumer and business confidence, low interest rates, and stable commodity prices (with the exception of oil) were tailwinds

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)	21.33	16.22	2.22			++
Valuation	R2000 Current P/E (Small Cap)	46.77	44.03	0.27		-	
Valuation	Avg P/E Ratio (Large/Small)	0.46	0.46	0.00		-	
Valuation	Russell Top 200 EV/EBITDA^ (Large Cap)	12.65	10.07	1.69			+
Valuation	R2000 EV/EBITDA (Small Cap)	15.99	13.98	0.64		-	
Valuation	Avg EV/EBITDA Ratio (Large/Small)	0.79	0.73	0.56		-	
Valuation	Russell Top 200 P/S (Large Cap)	2.24	1.59	2.11			++
Valuation	R2000 P/S (Small Cap)	1.18	1.03	0.75		-	
Valuation	Avg P/S Ratio (Large/Small)	1.90	1.56	2.94			++
Solvency	Russell Top 200 Debt/EBITDA (Large Cap)	4.32	4.62	-0.40		-	
Solvency	Russell 2000 Debt/EBITDA (Small Cap)	5.75	5.61	0.14		-	
Solvency	Avg Debt/EBITDA Ratio (Large/Small)	0.75	0.84	-0.43		-	
Growth	Russell Top 200 LT EPS Gr (Fwd) (Large Cap)	9.28	8.92	0.09		-	
Growth	R2000 LT EPS Gr (Fwd) (Small Cap)	9.18	10.64	-0.73		-	
Growth	Avg Growth Ratio (Large/Small)	1.01	0.84	0.38		-	
Economy	Case Shiller Home Price (YoY)	5.67	0.07	0.63		-	
Economy	Total Leading Economic Indicators	127.00	111.13	1.57			+
Economy	Currency (USD v Broad Basket)	95.63	84.04	1.38			+
Economy	Curve Steepness 2's to 10's	0.92	1.75	-1.33	+		

**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
- Both large- and small-cap stocks are expensive relative to their historical average, but on a relative basis small-cap stocks are more attractive than large-cap
- Leverage remains at normal levels for both large and small-cap stocks
- Growth estimates went up across the board. Growth for small-cap companies remains below average, but the gap is narrowing
- An improving economy and a strong dollar are positives for small-cap stocks. However, a flattening yield curve implies slower growth, which favors defensive large-cap stocks
- Advantage: U.S. small-cap relative to U.S. large-cap stocks

Source: Russell

Region Mix – U.S. vs. R.O.W.

	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	21.45	17.09	1.82			+
	MSCI ACWI Current P/E	20.53	16.99	0.94		-	
	Avg P/E Ratio (US /ACWI)	1.04	1.01	0.36		-	
	S&P 500 EV/EBITDA^	12.87	10.07	1.76			+
	MSCI ACWI EV/EBITDA	11.58	9.54	1.50	+		
	Avg EV/EBITDA Ratio (US/ACWI)	1.11	1.06	1.31			+
	S&P 500 P/S	2.09	1.50	1.87			+
	MSCI ACWI P/S	1.62	1.22	1.88	+		
	Avg P/S Ratio (US/ACWI)	1.29	1.22	0.74		-	
Solvency	S&P 500 Debt/EBITDA	4.25	4.64	-0.50		-	
	MSCI ACWI Debt/EBITDA	6.01	6.39	-0.58		-	
	Avg Debt/EBITDA Ratio (US/ACWI)	0.71	0.72	-0.18		-	
Growth	S&P 500 LT EPS Gr (Fwd)	8.80	8.66	0.03		-	
	MSCI ACWI LT EPS Gr (Fwd)	7.93	9.81	-0.13		-	
	Avg Growth Ratio (US/ACWI)	1.11	0.95	0.29		-	
Economy	Currency (USD v Broad Basket)	95.63	84.04	1.38			+

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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

- U.S. stock valuations and the rest of the world ("R.O.W.") valuations stayed fairly constant. U.S equities remain modestly expensive relative to non-U.S equities, although the gap has narrowed recently
- Debt levels are below long-term averages for 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 an elevated level. The dollar's strength hurts U.S. exporters and benefits foreign companies that export goods and service into the U.S.
- <u>Advantage: non-U.S. relative to U.S. equities</u>

Source: MSCI and Standard & Poor's

Region Mix – Non-U.S. Developed vs. R.O.W.

	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	22.80	18.55	0.34		-	
	MSCI ACWI Current P/E	20.53	16.99	0.94		-	
	Avg P/E Ratio (EAFE/ACWI)	1.11	1.07	0.13		-	
	MSCI EAFE EV/EBITDA^	10.18	9.09	0.99		-	
	MSCI ACWI EV/EBITDA	11.58	9.54	1.50	+		
	Avg EV/EBITDA Ratio (EAFE/ACWI)	0.88	0.96	-2.01	++		
	MSCI EAFE P/S	1.25	0.97	1.65			+
	MSCI ACWI P/S	1.62	1.22	1.88	+		
	Avg P/S Ratio (EAFE/ACWI)	0.77	0.80	-0.60		-	
Solvency	MSCI EAFE Debt/EBITDA	8.12	9.03	-0.92		-	
	MSCI ACWI Debt/EBITDA	6.01	6.39	-0.58		-	
	Avg Debt/EBITDA Ratio (EAFE/ACWI)	1.35	1.41	-1.27	+		
Growth	MSCI EAFE LT EPS Gr (Fwd)	7.33	7.84	-0.01		-	
	MSCI ACWI LT EPS Gr (Fwd)	7.93	9.81	-0.13		-	
	Avg Growth Ratio (EAFE/ACWI)	0.92	0.96	-0.01		-	
Economy	USD/EUR	1.14	1.30	-1.14	+		

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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

- All equities are currently expensive, but non-U.S. developed equities remain attractively valued relative to the R.O.W.
- Although debt levels increased slightly, solvency risk remains low, particularly for non-U.S. developed
- Growth estimates are in-line with historical averages for both categories
- The euro appreciated significantly vs. the dollar during the quarter, but the dollar remains strong relative to history. A strong dollar benefits European exporters with costs in euros and revenues in dollars
- <u>Advantage: non-U.S. developed equities relative to the rest of the world</u>

Source: MSCI

Region Mix – Emerging Markets vs. R.O.W.

	Equity: Region (EM/Global)	**Current**	**10 Year Avg**	**Deviation from Mean***	**EM**	**Neutral**	**R.O.W.**
Valuation	MSCI EM Current P/E	15.33	13.48	0.68		-	
	MSCI ACWI Current P/E	20.53	16.99	0.94		-	
	Avg P/E Ratio (EM/ACWI)	0.75	0.79	-0.47		-	
	MSCI EM EV/EBITDA^	9.49	8.02	1.16			+
	MSCI ACWI EV/EBITDA	11.58	9.54	1.50	+		
	Avg EV/EBITDA Ratio (EM/ACWI)	0.82	0.84	-0.24		-	
	MSCI EM P/S	1.32	1.20	0.47		-	
	MSCI ACWI P/S	1.62	1.22	1.88	+		
	Avg P/S Ratio (EM/ACWI)	0.82	1.00	-0.86		-	
Solvency	MSCI EM Debt/EBITDA	4.91	3.62	1.51			+
	MSCI ACWI Debt/EBITDA	6.01	6.39	-0.58		-	
	Avg Debt/EBITDA Ratio (EM/ACWI)	0.82	0.57	1.49			+
Growth	MSCI EM LT EPS Gr (Fwd)	5.86	9.31	-0.13		-	
	MSCI ACWI LT EPS Gr (Fwd)	7.93	9.81	-0.13		-	
	Avg Growth Ratio (EM/ACWI)	0.74	0.88	-0.19		-	

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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

- Despite the continuing rally, emerging markets ("EM") equities are less expensive, relatively, than R.O.W. equities. This is because EM earnings and revenues have kept pace with share price growth
- Elevated debt levels continue to be a source of concern for EM equities relative to the R.O.W.
- Growth estimates for both EM equities and R.O.W. equities declined during the quarter, with neither having the advantage
- Advantage: global equities relative to emerging markets equities

Source: MSCI

Portfolio Characteristics

Recommended Ranges

Market Cap (U.S.)	Minimum	Maximum	R3000
Large Cap (> $25.5B)	50.0%	70.0%	67.4%
Mid Cap ($2.9B - $25.5B)	25.0%	40.0%	26.5%
Small Cap (< $2.9B)	2.5%	12.5%	6.1%

Region	Minimum	Maximum	MSCI ACWI
U.S.	45.0%	65.0%	53.1%
Non-U.S. Developed	25.0%	40.0%	36.0%
Emerging Markets	5.0%	20.0%	10.9%

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