



Canterbury Consulting

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## Quarterly Asset Class Report

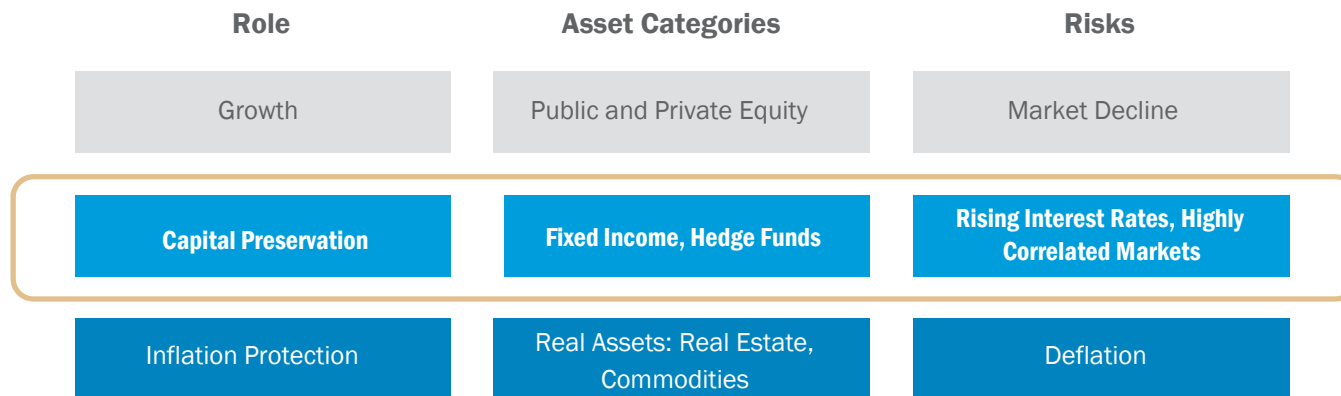
### Hedge Funds

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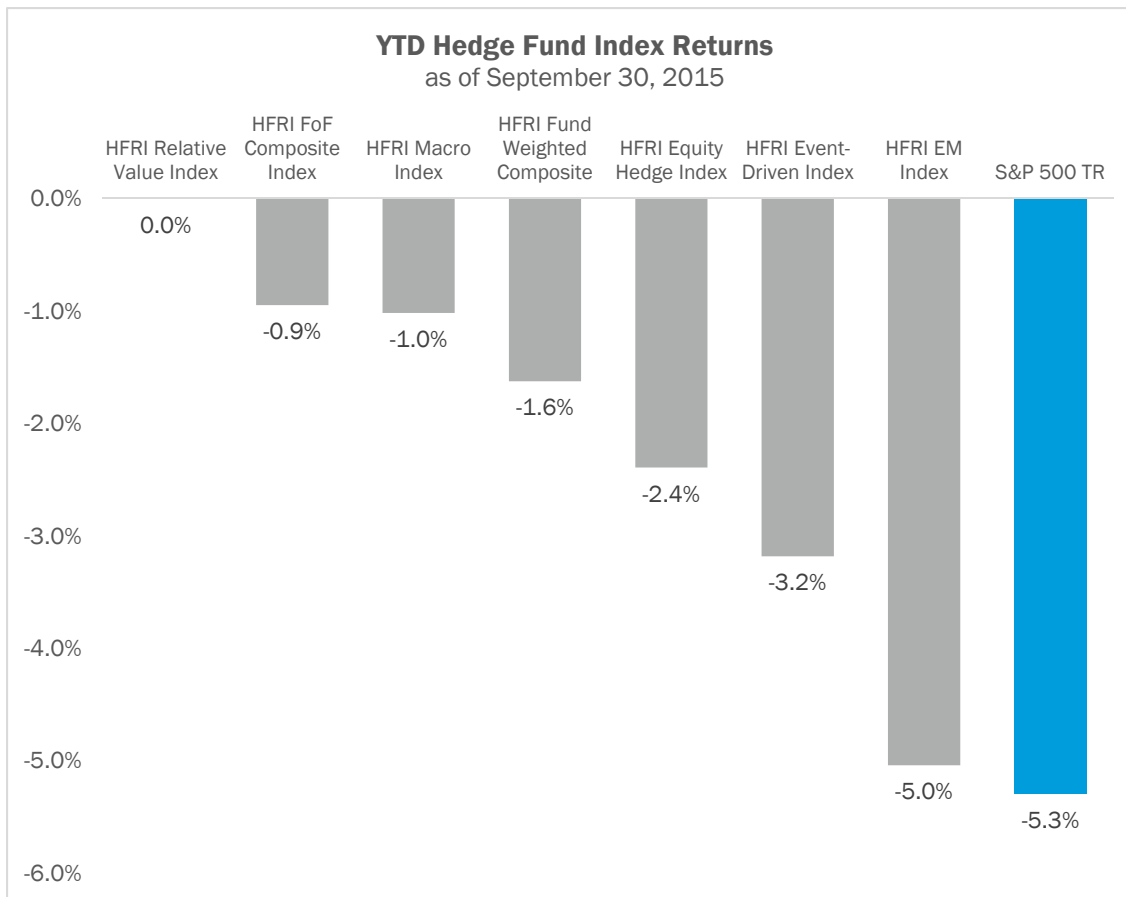
September 30, 2015

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



- 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



Source: HFRI

- 3Q performance was weak across the board, despite relative outperformance, mostly due to falling asset prices across fixed income and equities, both domestically and internationally
- Gains in healthcare reversed this quarter as the sector underperformed, causing large losses for hedge fund portfolios
- Volatility was driven by fears of a sharper than expected slowdown in China which impacted funds with higher net exposures to global growth
- Emerging market funds posted larger losses as the impact from the China slowdown was greater

### — Slower global growth and a low return environment

- Growth in China has been less than expected which has led to a downgrade of higher growth names, resulting in better short opportunities
- Meanwhile, Quantitative Easing policies are in full effect in European and some Asian markets encouraging investment in those regions
- A tale of two worlds - as the U.S. creeps towards its first interest rate hike in many years (supported by stronger October employment data), global central banks are actively cutting interest rates and easing credit

### — Higher volatility brings better opportunities

- Dispersion among business sectors and a renewed focus on fundamentals have allowed managers to generate alpha from long and short investments
- Currencies and commodity prices experienced volatility
- If the macro environment were to change dramatically, managers remain nimble to adjust exposures and protect capital

### — Late cycle positioning

- As the business cycle extends into the later innings, managers are positioning portfolios accordingly, especially on the credit side, waiting for dislocations before adding risk
- Market returns in credit and equities have shown a deceleration over the past three years which provides good opportunities to take calculated superior risk adjusted bets on the long and short side

Canterbury 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 expect markets to experience volatility with greater frequency for the remainder of 2015 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, 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