CanterburyConsulting

Quarterly Asset Class Report

Global Equity

canterburyconsulting.com

September 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

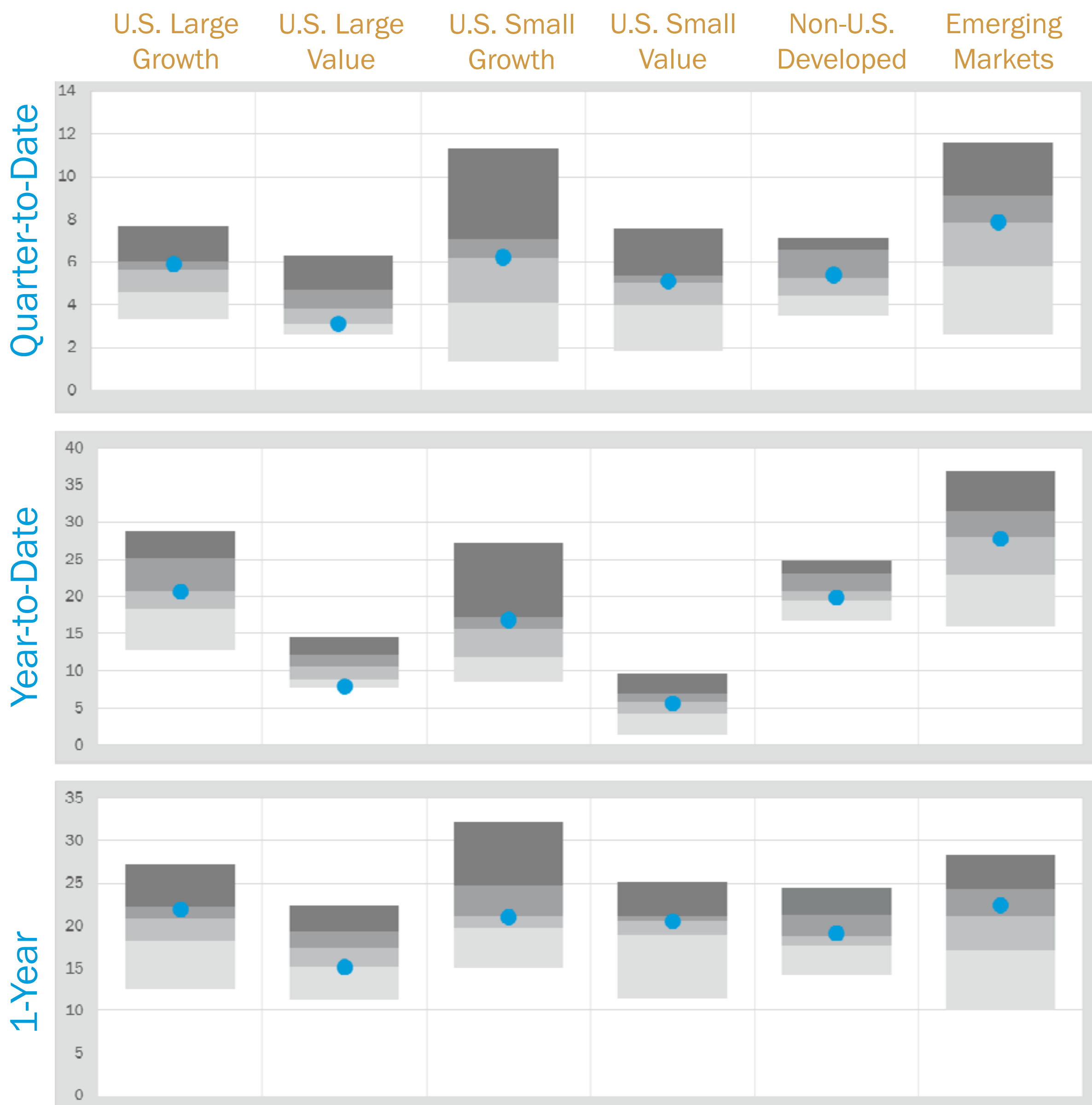
(ii) Maintain comparable exposure to the global equity market

(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 September 30, 2017



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

- Risk assets continued to rally in the third quarter, with emerging markets and small-cap growth equities performing the best. These were also the areas of highest dispersion among active managers, as these markets were led by narrow groups of stocks (Chinese internet and small biotech, respectively)

- U.S. large-cap value managers continued to broadly outperform against a backdrop of strength in the technology and healthcare sectors and weakness in the energy and telecom sectors

- Although performance by asset class varied widely YTD, on a 1-year basis all major equity asset classes enjoyed healthy returns, up between 15% - 22%. The relative weakness in small-cap value stocks this year has been the result of an unwinding of the enthusiasm following last year's election of President Trump

Source: Morningstar Direct

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)	21.42	16.35	2.10			++
	R2000 Current P/E (Small Cap)	53.61	44.64	0.87		-	
	Avg P/E Ratio (Large/Small)	0.40	0.46	-1.08	+		
	Russell Top 200 EV/EBITDA^ (Large Cap)	12.88	10.11	1.78			+
	R2000 EV/EBITDA (Small Cap)	17.13	14.07	0.97		-	
	Avg EV/EBITDA Ratio (Large/Small)	0.75	0.73	0.22		-	
	Russell Top 200 P/S (Large Cap)	2.30	1.60	2.16			++
	R2000 P/S (Small Cap)	1.25	1.03	1.09	+		
	Avg P/S Ratio (Large/Small)	1.84	1.57	2.20			++
Solvency	Russell Top 200 Debt/EBITDA (Large Cap)	4.31	4.57	-0.37		-	
	Russell 2000 Debt/EBITDA (Small Cap)	5.88	5.63	0.25		-	
	Avg Debt/EBITDA Ratio (Large/Small)	0.73	0.83	-0.48		-	
Growth	Russell Top 200 LT EPS Gr (Fwd) (Large Cap)	8.55	8.94	-0.09		-	
	R2000 LT EPS Gr (Fwd) (Small Cap)	9.75	10.59	-0.42		-	
	Avg Growth Ratio (Large/Small)	0.88	0.85	0.07		-	
Economy	Case Shiller Home Price (YoY)	5.81	0.32	0.61		-	
	Total Leading Economic Indicators	128.80	111.26	1.69			+
	Currency (USD v Broad Basket)	93.08	84.34	1.03			+
	Curve Steepness 2's to 10's	0.85	1.76	-1.52	+		

**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 for both large- and small-cap stocks are very close to historical averages
- Improving economic indicators and a strong dollar continue to be a tailwind for smaller, domestically-oriented companies. However, a flattening yield curve implies slower growth, which favors more 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	21.58	17.21	1.76			+
	MSCI ACWI Current P/E	20.26	17.08	0.84		-	
	Avg P/E Ratio (US /ACWI)	1.07	1.01	0.55		-	
	S&P 500 EV/EBITDA^	13.11	10.12	1.83			+
	MSCI ACWI EV/EBITDA	11.62	9.56	1.49	+		
	Avg EV/EBITDA Ratio (US/ACWI)	1.13	1.06	1.64			+
	S&P 500 P/S	2.15	1.51	1.93			+
	MSCI ACWI P/S	1.65	1.22	1.97	+		
	Avg P/S Ratio (US/ACWI)	1.30	1.23	0.80		-	
Solvency	S&P 500 Debt/EBITDA	4.25	4.60	-0.46		-	
	MSCI ACWI Debt/EBITDA	5.87	6.37	-0.74		-	
	Avg Debt/EBITDA Ratio (US/ACWI)	0.72	0.72	0.13		-	
Growth	S&P 500 LT EPS Gr (Fwd)	8.90	8.77	0.03		-	
	MSCI ACWI LT EPS Gr (Fwd)	7.07	9.84	-0.19		-	
	Avg Growth Ratio (US/ACWI)	1.26	0.96	0.54		-	
Economy	Currency (USD v Broad Basket)	93.08	84.34	1.03			+

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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. stocks are currently more expensive than the rest of the world ("R.O.W.") stocks based on all three valuation metrics, but the relative overvaluation is not that dramatic
- 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 services to 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. 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	20.79	18.64	0.17		-	
	MSCI ACWI Current P/E	20.26	17.08	0.84		-	
	Avg P/E Ratio (EAFE/ACWI)	1.03	1.07	-0.14		-	
	MSCI EAFE EV/EBITDA^	9.97	9.09	0.80		-	
	MSCI ACWI EV/EBITDA	11.62	9.56	1.49	+		
	Avg EV/EBITDA Ratio (EAFE/ACWI)	0.86	0.95	-2.40	++		
	MSCI EAFE P/S	1.27	0.97	1.78			+
	MSCI ACWI P/S	1.65	1.22	1.97	+		
	Avg P/S Ratio (EAFE/ACWI)	0.77	0.79	-0.67		-	
Solvency	MSCI EAFE Debt/EBITDA	7.77	9.00	-1.21	+		
	MSCI ACWI Debt/EBITDA	5.87	6.37	-0.74		-	
	Avg Debt/EBITDA Ratio (EAFE/ACWI)	1.32	1.41	-1.84	+		
Growth	MSCI EAFE LT EPS Gr (Fwd)	4.71	5.75	-0.01		-	
	MSCI ACWI LT EPS Gr (Fwd)	7.07	9.84	-0.19		-	
	Avg Growth Ratio (EAFE/ACWI)	0.67	0.79	-0.01		-	
Economy	USD/EUR	1.18	1.29	-0.82		-	

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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.
- Debt levels decreased in the quarter slightly and solvency risk remains low, particularly for non-U.S. developed
- Growth estimates are slightly below historical averages for both categories
- The euro slightly appreciated 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	15.79	13.49	0.84		-	
	MSCI ACWI Current P/E	20.26	17.08	0.84		-	
	Avg P/E Ratio (EM/ACWI)	0.78	0.79	-0.08		-	
	MSCI EM EV/EBITDA^	9.94	8.01	1.52			+
	MSCI ACWI EV/EBITDA	11.62	9.56	1.49	+		
	Avg EV/EBITDA Ratio (EM/ACWI)	0.85	0.84	0.18		-	
	MSCI EM P/S	1.38	1.18	0.76		-	
	MSCI ACWI P/S	1.65	1.22	1.97	+		
	Avg P/S Ratio (EM/ACWI)	0.83	0.99	-0.75		-	
Solvency	MSCI EM Debt/EBITDA	4.85	3.68	1.38			+
	MSCI ACWI Debt/EBITDA	5.87	6.37	-0.74		-	
	Avg Debt/EBITDA Ratio (EM/ACWI)	0.83	0.59	1.47			+
Growth	MSCI EM LT EPS Gr (Fwd)	11.71	9.27	0.12		-	
	MSCI ACWI LT EPS Gr (Fwd)	7.07	9.84	-0.19		-	
	Avg Growth Ratio (EM/ACWI)	1.66	0.90	1.10	+		

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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 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 EM equities doubled during the quarter whereas estimates for R.O.W. equities declined.
- <u>Emerging markets and global equities are equally attractive</u>

Source: MSCI

Portfolio Characteristics

Recommended Ranges

Market Cap (U.S.)	Minimum	Maximum	R3000
Large Cap (> $24.9B)	50.0%	70.0%	67.7%
Mid Cap ($2.9B - $24.9B)	25.0%	40.0%	25.5%
Small Cap (< $2.9B)	2.5%	12.5%	6.7%

Region	Minimum	Maximum	MSCI ACWI
U.S.	45.0%	65.0%	52.5%
Non-U.S. Developed	25.0%	40.0%	36.4%
Emerging Markets	5.0%	20.0%	11.2%

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