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From Chautauqua Capital Management
A Division of Robert W. Baird

International and Global Growth Equity Strategies

2nd Quarter 2016

Introduction

The "Brexit" vote and previous central bank policy meetings, in a backdrop of countervailing economic data, led to a volatile quarter that was full of reversals and ended little changed from where it began.

In this environment, the Chautauqua Capital International Growth Equity composite declined 0.03%, outperforming the MSCI ACWI ex-U.S. Index®, which declined by 0.40%, and the MSCI EAFE Index®, which declined by 1.19%. The Chautauqua Capital Global Growth Equity composite declined 0.32%, underperforming the MSCI ACWI Index®, which appreciated 1.19%.

Review

For the MSCI ACWI ex-U.S. Index®, growth style outperformed value style. Within emerging markets, growth style also outperformed value style. Small capitalization stocks outperformed large capitalization stocks in all but the emerging market indices. For the MSCI EAFE Index®, the growth style outperformed the value style, and large capitalization stocks outperformed small capitalization stocks.

For the MSCI ACWI Index®, the value style outperformed the growth style, and small capitalization stocks outperformed large capitalization stocks. Within emerging markets, the growth style outperformed the value style and large capitalization stocks outperformed small capitalization stocks.

Performance by country, in which the portfolios were invested and as measured by MSCI, is as follows: Brazil 13.93%, Canada 3.61%, China 0.28%, Denmark -0.49%, France -3.53%, Germany -4.98%, Hong Kong 0.94%, Japan 1.03%, Korea -1.21%, Netherlands -4.79%, South Africa 1.71%, Spain -7.44%, Switzerland 2.47%, Taiwan 1.00% and U.K. -0.72%.

Sector performance was similarly dispersed, though mostly positive. The best performing sectors were energy 9.73%, health care 5.61% and utilities 4.44%. The worst performing sectors were consumer discretionary -3.61%, information technology -1.60% and financials -1.45%.

On June 23, the United Kingdom (U.K.) held a referendum to decide whether the country should Leave or Remain in the European Union (E.U.). The foundational issue for the Leave campaign was immigration – or more specifically, the open immigration in the E.U. that coincides with competition for jobs, wage pressure, and crowding for public services.

Leave won 52% to 48%, marking the first-ever departure from the European Union. Turnout was 72%, and more than 30 million people voted. Prime Minister David Cameron offered his resignation on the morning of June 24, and in the aftermath of the referendum, the pound declined more than 10% against the dollar – to its lowest level in three decades – and equity markets sold off sharply.

Under Article 50 of the Treaty of Lisbon, an E.U. Member State may withdraw from the Union, initiating a two year window to negotiate the terms of its withdrawal. There is an enormous task at hand,

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as the U.K. and E.U. together must navigate an unprecedented separation while trying to mitigate economic and political turmoil.

The U.S. Federal Open Market Committee (FOMC) met in April and June, electing both times to keep the federal funds rate steady. More significantly, however, the FOMC flagged new concerns that portend another round of monetary accommodation. First, the pace of U.S. economic expansion has continued to weaken, marked by Gross Domestic Product (GDP) growth in the first quarter of 2016 that slowed to 1.1% and was the third consecutive quarterly deceleration. The FOMC accordingly revised its forecasts for U.S. GDP growth downwards, from 2.2% to 2.0% in 2016 and from 2.1% to 2.0% in 2017. Second, the Department of Labor released U.S. jobs growth data that was surprisingly disappointing, stating that only 38,000 jobs were added in May and making that the slowest month for job creation since 2010. Amid this newfound sluggishness, the FOMC tapered its multi-year ambition for rate normalization and now forecasts two rate increases in 2016, three rate increases in 2017, and three rate increases in 2018, corresponding to a federal funds rate between 2.25% and 2.50% by the end of 2018.

In Japan, GDP growth of 1.7% was reported for the first quarter of 2016, up from the 1.1% decline reported in the fourth quarter of 2015. However, real GDP growth has stagnated since 2014, and inflation remains far from the government's 2% target despite rate cutting and aggressive quantitative easing. During the quarter, Prime Minister Shinzo Abe also announced the delay of a value-added tax hike by two years to 2019. Naturally, this will be positive for near-term growth, but the tax delay also jeopardizes the government's goal of balancing the budget by 2020. Without the tax revenue, Japan is poised to continue deficit spending. The country's debt-to-GDP ratio, which is well over 200% and is the highest in the developed world, will continue to worsen during a time where 10 and 20 year Japanese government bond yields are negative.

In India, Raghurham Rajam announced his resignation from the country's central bank, the Bank of India, as he plans to return to academia after serving his three year term. Governor Rajam was installed by the previous administration, but while working in the Modi administration, India became the fastest growing economy in Asia. He was the architect of a policy to halve inflation, reduce interest rates and stabilize a rupee that had been in freefall since 2013. It remains to be seen whether the next leader at the Bank of India will continue the structural reform policy to lower India's inflation rate and promote long-term growth of the consumer banking sector and the bigger economy.

Portfolio Highlights

In an environment where returns based on country, economic sector, market capitalization and investment style leadership shifted rapidly throughout the quarter, careful diversification and a long-term focus prevented a significant performance dislocation.

Importantly, efforts to safeguard against what we deemed to be a low probability but high negative impact event such as a "Brexit Leave" outcome were helpful. We entered the referendum vote with an elevated cash position and an underweight to the financials sector, which was the sector most vulnerable to a political or economic shock. Additionally, prior to the vote, we evaluated our exposure to U.K.-headquartered, and non-U.K.-headquartered companies that derive significant revenue from the U.K., to ensure that we did not face a potential negative currency impact due to a weaker pound. In the massive sell-off after the Brexit vote, we were able to take advantage of what we deemed to be overreactions and paired back holdings that traded at higher valuations, while adding to positions and initiating new positions where we believed we had a rare opportunity.

Performance Attribution

In a volatile quarter, the International Equity composite generated slightly negative returns and slightly out-performed the indices. By region, 84% of the outperformance can be explained by stock selection. Considering sector exposures, more than 100% of the out-performance can be explained by stock

selection. As evidence of the success of our conviction-weighting process, the top five holdings generated returns in excess of the total return.

The Global Equity composite holdings outperformed in markets outside of the U.S. In the U.S., where value styles and small capitalization segments did better than growth and large capitalization segments, portfolio holdings underperformed. The net effect was underperformance for the quarter. As evidence of the success of our conviction-weighting process, the top ten holdings generated returns in excess of the total return.

Composite performance for the periods ending June 30, 2016*

International

	Q2 2016	1 Year	3 Year	5 Year	Since Inception 1/1/06	Cumulative Since Inception 1/1/06
International Growth Equity - Gross	**-0.03%**	**-1.53%**	**5.97%**	**3.08%**	**6.78%**	**99.14%**
International Growth Equity - Net	**-0.09%**	**-1.90%**	**5.60%**	**2.66%**	**6.57%**	**95.12%**
MSCI ACWI ex-U.S. Index® - GD	-0.40%	-9.80%	1.62%	0.56%	3.15%	38.50%
MSCI EAFE Index® - GD	-1.19%	-9.72%	2.52%	2.15%	2.93%	35.39%

Global

	Q2 2016	1 Year	3 Year	5 Year	Since Inception 1/1/07	Cumulative Since Inception 1/1/07
Global Growth Equity - Gross	**-0.32%**	**0.85%**	**10.02%**	**7.04%**	**7.14%**	**92.55%**
Global Growth Equity - Net	**-0.44%**	**0.30%**	**9.44%**	**6.51%**	**6.86%**	**87.86%**
MSCI ACWI Index® -GD	1.19%	-3.17%	6.60%	5.95%	3.62%	40.21%
MSCI World Index® - GD	1.21%	-2.19%	7.54%	7.23%	3.90%	43.86%

***These are preliminary figures from our portfolio accounting system that have yet to be verified by Ashland Partners.**

Outlook

In the E.U., economic growth has slowed and the large output gap augurs favorably for the European Central Bank (ECB) to remain accommodative. Separately, Quantitative Easing has increased the

demand for bonds, exacerbating an already unprecedented policy for negative deposit facility rates. The result has been a secular decline in bond yields. Political or economic shocks can amplify the effect. As a result, 10 year German Bund yields turned negative for the first time in history in June.

The free movements of goods, services, persons and capital are mutually guaranteed under the Treaty of Lisbon, and they are central to the European Commission's Single Market strategy. With the vote to Leave, the U.K. has effectively desecrated the freedom of movement in favor of protectionism of its own labor interests, and it will likely relinquish the free trade exchange with the E.U. that it previously enjoyed.

To our view, the U.K. referendum should not be feared to be a replay of the Great Recession. This is not a problem owed to excess leverage, nor is it a liquidity event for the financial sector. Since the Great Recession, stronger firewalls have been created in the financial sector, while central bankers remain accommodative. Ultimately, the final analysis of the referendum's collateral damage can only be assessed when three unknowns crystallize: U.K. domestic consumption in the near-term, the economic relationship that will be forged with the E.U., and whether additional political fragmentation is sparked in the E.U.

It is almost certain that the U.K.'s near-term growth trajectory has been stunted by a swift depreciation in the pound and this new cloud of uncertainty surrounding a new E.U. trade paradigm. A cheaper currency benefits British exporters but reduces purchasing power and may prove inflationary as imported goods become more expensive. More paralyzing, however, is that potential transactions that are seen as difficult to unwind would remain on pause. The expectation would then be that the U.K. domestic economy decelerates, if not declines, as fixed investment, real estate transactions, durable goods purchases and hiring all slow down. Even London's status as the financial center of Europe is thrown in jeopardy due to the potential restrictions of a new economic deal. Dublin, Frankfurt, Luxembourg, and Paris are jockeying to win the financial services revenues of businesses that may leave London.

The E.U. is the U.K.'s top export market. The U.K. has had a trade surplus with many E.U. Member States. Maintaining these trade linkages will be mission critical for both economic regions, however, these will likely come with tariffs and restrictions in the new agreement. The Leave campaign argued that a post-E.U. agreement might be painless given the benign trade precedents the E.U. previously set with Switzerland and Norway, respectively. Both of these countries exist outside of the Single Market, yet feature prominently as trade partners with the E.U., and most inter-region activity goes entirely non-tariffed. However, the E.U. is unlikely to extend a similar agreement with the U.K., or else the E.U. risks disincentivizing Member States to stay.

It is entirely possible that the U.K. referendum is the edge of the wedge, leading to more fragmentation from Member States. Partly, this depends on the trade agreement the E.U. strikes, but it also may not matter given that negotiations may take a protracted amount of time. Ultimately, a painless agreement invites moral hazard if a Member State could leave the E.U. knowing the consequences would be very little. Nevertheless, nationalists in France and the Netherlands are pushing for their own Remain or Leave referendums and should, at the very least, be inspired by the outcome of the U.K. referendum. Ironically, the U.K. itself may fracture. Scottish constituents voted to Remain, and since the final result, First Minister Nicola Sturgeon has stated that a referendum for Scottish independence is now highly likely so that it may qualify rejoin the E.U.

In the U.S., Federal Reserve Chairwoman Janet Yellen renewed her caution on an imminent tightening regime. She established four criterions for the next U.S. rate increase: acceleration in U.S. economic growth in the second quarter, improvement in the job market, signals that inflation is picking up and stability in the world economy. On the positive side, the FOMC upgraded its forecast for inflation from 1.2% to 1.4% in 2016 and believes that their inflation target of 2.0% will be reached in 2018. But seeing an alignment in Chairwoman Yellen's other three criterions would be difficult, if not far-fetched at this

point. The U.S. presidential candidates are polarizing, but the substance of their platforms has yet to be articulated. This type of uncertainty can challenge economic growth and expansion in the labor market.

The transition of China's economy remains a wild card in the fragile global economy. Economic data from May showed continued weakness in the export and manufacturing sectors, but strong domestic demand, and the overall dynamic was in line with expectations. However, this delicate balance may be easily disrupted by the government's reform agenda. Outsized moves involving investment restrictions, capacity shuttering, or corporate credit would be in line with the government's 5-Year Plan to deemphasize Old Economy sectors and champion new growth industries, but they may also unintentionally disrupt the balance within a decelerating large economy.

Business Update

During the second quarter, David Lubchenco rejoined Chautauqua Capital as a Partner and member of the investment team. David, drawing upon 23 years of experience, mostly with concentrated and conviction-weighted equity investment strategies, provides valuable market insights. Given his academic preparation with degrees in Business and Economics, he is well suited to assist in portfolio evaluation and construction and lead our efforts to communicate with clients.

In the second quarter, we launched the Chautauqua International Growth Fund and the Chautauqua Global Growth fund. These two mutual funds are now available for purchase under the symbols CCWIX for the institutional class and CCWSX for the investor class for our International Growth strategy and CCGIX for the institutional and CCGSX for the investor class for our Global Growth strategy.

The transition of back office and administrative functions has been carefully and effectively transferred to Robert W. Baird. The integration is complete.

Respectfully submitted,

The Partners of Chautauqua Capital Management – a Division of Robert W. Baird

The above commentary does not provide a complete analysis of every material fact regarding any market, industry, security or portfolio. Portfolio holdings information, opinions and other market or economic information and data provided are as of the date of the commentary, unless another date is expressly indicated, and may change without notice. The manager's assessment of a particular industry, security or investment is intended solely to provide insight into the manager's investment process and is not a recommendation to buy or sell any security, nor investment advice.

The MSCI ACWI Index® is a free float-adjusted market capitalization weighted index that is designed to measure the equity performance of developed and emerging markets. The MSCI ACWI Index® consists of 44 country indices, including the United States, comprising 23 developed and 21 emerging market country indices.

The MSCI ACWI ex-U.S. Index® is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of developed and emerging markets excluding the United States.

The MSCI EAFE Index® is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of developed markets, excluding the United States and Canada. The MSCI EAFE Index® consists of 21 developed market country indices.

The MSCI World Index® is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of developed markets. The MSCI World Index® consists of 23 developed market country indices.

Performance results will vary among client accounts. The actual return and value of an account will fluctuate and at any point in time could be worth more or less than the amount invested. The performance results displayed herein represent the investment performance records for the Chautauqua composites that include fully discretionary fee paying client accounts. The composites' returns are total, time weighted returns expressed in U.S. dollars. Composite returns reflect the reinvestment of dividends and

other earnings. The net performance reflects the deduction of investment advisory fees and transactions costs and the gross performance is net of transaction costs, but gross of advisory fees. The cumulative performance information shown is the aggregate amount that the composites have gained since inception through June 30, 2016.

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Chautauqua Capital Management Investment Team

- All investment team members have equity ownership
- Average years of experience: 21 years

Investment Professional	Degrees	Years of Experience	Prior Affiliation
Brian Beitner, CFA *Managing Partner*	MBA, University of Southern California BS, University of Southern California	35	TCW Group Scudder Stevens & Clark Bear Stearns Security Pacific
Daniel Boston *Partner*	MBA, Yale University BS, Brigham Young University	9	Ensign Peak Advisors Artisan Partners Wasatch Advisors
Jesse Flores *Partner*	MBA, Stanford University BS, Cornell University	8	Roth Capital Partners Blavin & Company Lehman Bros.
David Lubchenco *Partner*	MBA, University of Denver BA, The Colorado College	23	Marsico Capital Management Transamerica Investment Management Janus Capital
Michael Mow *Partner*	MBA, University of Southern California MS, University of Iowa BA, California State University, Northridge	29	American Century TCW Group Farmers Insurance