International and Global Growth Equity Strategies

Q1 2019 COMMENTARY

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CHAUTAUQUA
CAPITAL MANAGEMENT
A DIVISION OF BAIRD

INTRODUCTION

Global markets enjoyed a strong start to the year, marking a steep reversal from the downdraft that maligned the fourth quarter. Changes we previously made to portfolios – selling lower growth companies that looked overvalued in favor of buying higher growth companies that sustained greater losses and ranked more attractive – were beneficial to performance in the first quarter.

Weak or decelerating growth in virtually every major economy, coupled with lingering overhangs from international trade frictions, have compelled the major central banks to adopt stimulative policies for the foreseeable future. This is an enormous pivot, and indeed, much of the rally in the first quarter was fueled by this relief. We have maintained that a slower pace of rate hikes, ceteris paribus, would be relatively more favorable for asset valuations. Now, there may be no rate hikes at all.

In the first quarter of 2019, the Chautauqua Capital International Growth Equity composite increased 13.43%, outperforming both the MSCI ACWI ex-U.S. Index® ND, which increased 10.31%, and the MSCI EAFE Index® ND, which increased 9.98%. The Chautauqua Capital Global Growth Equity composite increased 16.51% during the quarter, outperforming the MSCI ACWI Index® ND, which increased 12.18%.*

MARKET UPDATE

For the MSCI ACWI ex-U.S. Index®, growth style outperformed value style. Within emerging markets, growth style also outperformed value style. Large capitalization stocks underperformed small capitalization stocks in the developed markets sub-index but outperformed small capitalization stocks in the emerging markets sub-index.

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

For the MSCI EAFE Index®, growth style outperformed value style, and large capitalization stocks underperformed small capitalization stocks.

Sector and country performance were positive for the quarter.

MSCI Sector and Country Performances (QTD as of 03/31/2019)

Sector	Performance	Country	Performance	Country	Performance
Information Technology	18.92%	China	17.69%	Taiwan	8.98%
Real Estate	16.20%	Canada	15.60%	Austria	8.56%
Energy	14.31%	Italy	14.71%	India	7.16%
Industrials	13.95%	United States	13.91%	Germany	7.00%
Consumer Discretionary	13.30%	Netherlands	13.63%	Japan	6.85%
Consumer Staples	11.49%	Switzerland	13.54%	Singapore	6.23%
Communication Services	11.23%	Denmark	13.23%	South Korea	4.97%
Materials	11.21%	Ireland	11.58%	South Africa	4.56%
Utilities	9.68%	France	10.79%	Indonesia	4.27%
Financials	8.36%				
Health Care	8.22%				

**Performance data represents past performance and does not guarantee future results. Current performance data may be lower or higher than the data quoted. For performance data to the most recent month end, contact Chautauqua directly at 303-541-1545 or www.chautauquacapital.com.*

INVESTMENT TEAM

- Generalists with specialized skills
- Averaging 26 Years investment experience

INVESTMENT PHILOSOPHY

- The securities of advantaged, wealth-generating businesses are often mispriced because most investors do not fully comprehend the companies' potential for sustained high-growth and improved profitability. Several trends accentuate this phenomenon.

KEY PILLARS OF OUR INVESTMENT PROCESS

- Security selection drives returns
- Long-term focus
- Concentrated, conviction-weighted portfolios

ORGANIZED FOR INVESTMENT SUCCESS

- Autonomous institutional boutique
- Employee owners
- We invest alongside our clients
- Self-imposed limit on growth

After a period of exceptional market volatility during the fourth quarter of last year, the Federal Reserve signaled a reversal from their plans to keep raising interest rates. Beginning in January, and despite a rate hike in just the previous month, Chairman Jerome Powell framed a cautious economic narrative citing sluggishness in Europe and Asia, ongoing global trade policy frictions, and mild domestic inflationary pressures.

Effectively, this new caution fomented a pivot by the Federal Reserve away from its prior course of monetary tightening. And with each passing month, Chairman Powell's message on pausing U.S. rate hikes seemed to grow only more forceful. After meetings in both January and March, the Federal Reserve left the federal funds rate unchanged, in between a range of 2.25% and 2.5%. Furthermore, the Federal Reserve announced that it will slow the "run off" of its Treasury portfolio starting in May and will begin reinvesting bond maturities starting in October.

As market participants seized on this change, equity markets rallied, emerging market currencies strengthened, and long-term government bond yields and corporate credit spreads both fell. Within the equity asset class, this strength was universal. Returns from every sector and country in the global index were positive in the first quarter.

The U.S. economy remains relatively healthy when compared to the other major economies in the world, and it is a definite bright spot. Some recent data, however, appears mixed on the margin. Gross Domestic Product (GDP) growth during the fourth quarter was 2.2%. Capital investment by businesses and corporate earnings growth were strong, but monthly growth in consumer spending turned negative in December and failed to show a meaningful snapback in both January and February. It is possible that the recent consumer softness incorporated transient setbacks such as the U.S. government shutdown and unseasonably cold winter. More recently, both the Purchasing Managers' Index (PMI) and spending on the services sector have decelerated meaningfully. Mild inflation is one of the factors that has informed the Federal Reserve's new direction with its monetary policy. An economic environment with high employment and rising wages, as is currently found in the U.S., should be supportive of inflationary pressure, but inflation figures have remained below the Federal Reserve's target of 2%. The Core Personal Consumption Expenditures (PCE) index, a measure of inflation that excludes food and energy prices, increased 1.94% in 2018 and only 1.79% in January.

In Europe, the economic slowdown in the region has accelerated. GDP grew 0.3% in the fourth quarter, the slowest pace of expansion in the last five years, and European Central Bank (ECB) President Mario Draghi made a fifth straight cut to growth forecasts. Much of this weakness is attributed to falling export demand and manufacturing activity, but even retail sales suffered one of the steepest monthly declines in the last decade this past December. Moreover, recent PMI data is not encouraging as economic activity in both Germany and France have contracted. Furthermore, Italy has slipped into a technical recession, afflicted by slowing global trade, weak consumer confidence, and pushback from the European Union (E.U.) to shrink its budget.

In response to the slowdown, the ECB also reversed its policy to favor economic stimulus. Recall that the ECB just ended quantitative easing in December. Now, President Draghi has pledged to keep the deposit facility rate, currently -0.4%, unchanged through the end of the year. Moreover, he announced that the ECB will restart a direct lending program to commercial banks, something that has not been offered since the eurozone debt crisis. Under this program, banks will be able to access cheap, long-term loans directly from the ECB.

PERFORMANCE ATTRIBUTION

Selection effect accounted for over 90% of the outperformance in the Chautauqua International Growth composite. This was especially pronounced in the consumer discretionary and communication services sectors. Within those sectors, holdings in TAL Education, Ctrip, Alibaba and Naspers helped performance the most. Our overweight position in information technology also contributed, while our strong stock selection in this sector was offset by Wirecard's negative return. Meanwhile, holdings in the consumer staples and health care sectors hurt performance the most. Of these, the biggest detractors were Amorepacific, Genmab, and Sinopharm.

Top 5 Average Weighted International Holdings* for Q1 2019

Security	Avg. Weight	Contribution
Temenos	7.09	1.53
DBS Group Holdings	5.71	0.43
Toronto-Dominion Bank	5.66	0.64
Novo Nordisk	5.61	0.83
Genmab	5.50	0.32

Bottom 5 Average Weighted International Holdings* for Q1 2019

Security	Avg. Weight	Contribution
Multichoice Group	0.05	0.03
CI Financial	0.33	0.03
Amorepacific	1.26	-0.21
Allergan	1.30	0.14
Sinopharm	1.52	0.00

Top 5 Average Weighted Global Holdings* for Q1 2019

Security	Avg. Weight	Contribution
Temenos	5.55	1.20
Genmab	4.55	0.25
Mastercard	4.50	1.07
NVIDIA Corp.	4.46	1.40
Novo Nordisk	3.89	0.58

Bottom 5 Average Weighted Global Holdings* for Q1 2019

Security	Avg. Weight	Contribution
Multichoice Group	0.03	0.03
Red Hat, Inc.	0.23	0.00
CI Financial	0.32	0.03
Amorepacific	0.55	-0.09
Allergan	0.87	0.10

*The holdings identified do not represent all of the securities purchased, sold, or recommended for advisory clients; and past performance does not guarantee future results. To obtain information about the calculation methodology and a list showing every holding's contribution, please contact Baird.

TAL Education had a 5.43%, Ctrip a 2.14%, Alibaba a 3.62%, Naspers a 5.31%, and Wirecard a 3.82% weighting in the International Strategy as of 3/31/2019.

Selection effect accounted for over 90% of the outperformance in the Chautauqua Global Growth composite. This was especially pronounced in the consumer discretionary and health care sectors. Additionally, both our overweight position and holdings in information technology contributed. Within those sectors, holdings in Universal Display, Nvidia, Temenos, Mastercard, Ctrip, TAL Education, and Incyte helped performance the most. Meanwhile, our underweight positioning in industrials and our holdings in the consumer staples sector hurt performance the most. Amorepacific was the sole holding in consumer staples.

COMPOSITE PERFORMANCE FOR THE PERIODS ENDING MARCH 31, 2019* (%)

Chautauqua International Growth Equity

	Q1 2019	1 Year	3 Year	5 Year	10 Year	Since Inception (01/01/2006)	Cumulative Since Inception (01/01/2006)
International Growth Equity – Gross	**13.43**	**-7.91**	**8.81**	**5.15**	**12.00**	**7.37**	**156.44**
International Growth Equity – Net	**13.28**	**-8.35**	**8.37**	**4.75**	**11.64**	**7.11**	**148.52**
MSCI ACWI ex-U.S. Index® - ND	10.31	-4.22	8.09	2.57	8.85	3.98	67.79
MSCI EAFE Index® - ND	9.98	-3.71	7.27	2.33	8.96	3.68	61.39

Chautauqua Global Growth Equity

	Q1 2019	1 Year	3 Year	5 Year	10 Year	Since Inception (01/01/2007)	Cumulative Since Inception (01/01/2007)
Global Growth Equity – Gross	**16.51**	**-0.06**	**13.81**	**9.90**	**15.88**	**8.92**	**184.78**
Global Growth Equity – Net	**16.29**	**-0.81**	**12.93**	**9.15**	**15.34**	**8.51**	**171.79**
MSCI ACWI Index® - ND	12.18	2.60	10.67	6.45	11.98	4.86	78.77
MSCI World Index® - ND	12.48	4.01	10.68	6.78	12.38	5.06	82.95

*These are preliminary figures from our portfolio accounting system that have yet to be verified by ACA. Performance data represents past performance and does not guarantee future results. Current performance data may be lower or higher than the data quoted. For performance data to the most recent month end, contact Chautauqua directly at 303-541-1545 or www.chautauquacapital.com.

PORTFOLIO HIGHLIGHTS | BUYS AND SELLS

For the Chautauqua International Growth composite, 86% of companies that reported earnings during the quarter were in-line with or exceeded consensus expectations.

For the Chautauqua Global Growth composite, 89% of companies that reported earnings during the quarter were in-line with or exceeded consensus expectations.

Our conviction weighting process, which considers our estimates for growth, profitability, and valuation, is key to our portfolio management strategy and has been additive to returns over the long run.

In the International strategy, we reduced positions in ASML and Ctrip. Proceeds, in addition to cash we had raised in portfolios during the fourth quarter, were used to increase exposures in Naspers, Wirecard, Core Labs, Julius Baer, and Pirelli.

In the Global strategy, we reduced positions in Red Hat. Proceeds, in addition to cash we had raised in portfolios during the fourth quarter, were used to increase exposures in Nvidia, Naspers, and Wirecard.

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OUTLOOK

As we have previously stated, markets can move directionally opposite to economic fundamentals. During the first quarter, equity markets climbed, but the underlying economic data deteriorated.

Of all the major economic regions, the slowdown was most acute in Europe. The E.U. continues to face pressure from Brexit, slowing demand from China, and mounting debt in Italy. The ECB has already cut GDP growth forecasts twice this year, most recently to 1.1% in 2019. Meanwhile, recent PMI figures that show contracting economic activity hardly bode well for meeting the new full year target. Slowing global growth will be another headwind for the E.U., especially as the U.K. and China are top export markets after the U.S.

Universal Display had a 3.43%, Ctrip a 1.04%, TAL Education a 2.66%, Incyte had a 3.85%, Naspers a 3.65%, and Wirecard a 3.10% weighting in the Global Strategy as of 3/31/2019; ASML has a 3.02%, Ctrip a 2.14%, Naspers a 5.31%, Wirecard a 3.82%, Core Labs a 4.52%, Julius Baer a 4.00%, and Pirelli a 1.82% weighting in the International Strategy as of 3/31/2019.

Business uncertainty resulting from trade frictions will continue to put downward pressure on economic growth, and these concerns are unlikely to dissipate soon. While progress has been made in several rounds of negotiation between the U.S. and China, and President Trump has indefinitely suspended a scheduled increase of tariffs on $200 billion of Chinese goods, the final resolution is hardly certain. Multiple complex issues will need to be negotiated such as purchase guarantees of U.S. goods, forced technology transfer, intellectual property protection, and market access.

China's economy is slowing faster than expected, with more than half of the nation's 31 provinces failing to meet growth targets last year. Also, industrial production continued to weaken and has been hurt by soft automotive and property markets. Slowing demand from China has not only impacted the E.U., but exports from Japan and South Korea have also slowed sharply. The Federal Reserve, on the other hand, has articulated a positive outlook for the U.S. economy this year, citing low unemployment, rising wages, and high consumer confidence. The latest forecast is for U.S. GDP growth of 2.1% in 2019, but this does not contemplate a continued deterioration of global growth due to business uncertainty resulting from unresolved trade policy.

If there are any silver linings to the economic backdrop, then it is undoubtedly the end of the U.S. interest rate tightening cycle. Low interest rates are typically constructive for financial assets. This is especially true for growth stocks.

Back in December, the median forecast by members of the Federal Open Market Committee was two rate hikes in 2019. Now, most members forecast none. Furthermore, the Federal Reserve's pivot ensures that the loose monetary policies of major central banks will continue. The ECB and Bank of Japan (BOJ) are likely to sustain negative interest rate policies for the foreseeable future, while the central banks of Switzerland, Sweden, and Demark, which also have negative interest rate policies, will be confined to follow suit in order to protect their exchange rates with the euro. An additional implication of the trajectory of monetary policy is that higher bond yields in the U.S. relative to other developed markets are likely to persist. This should support continued dollar strength.

Separately, central banks in emerging markets will enjoy a reprieve, as pressure to raise rates to maintain a dollar peg abates. Furthermore, low yields in developed markets should support investment in emerging market bonds. The central banks of South Korea, Indonesia, and the Philippines kept their rates unchanged in the first quarter. What is more, the Reserve Bank of India actually cut its policy rate in February.

One downside of the Federal Reserve's pivot is that it will have little room to maneuver the next time the U.S. economy slides. The federal funds rate is just 0.25% when adjusted for expected inflation, and the Federal Reserve will hold a bond portfolio equivalent to 17% of GDP (approximately $3.5 trillion) when it ends the "run off" in September. By comparison, after the last tightening cycle ended in 2006, the real rate was 2.75%, and the Federal Reserve held a bond portfolio equivalent to 6% of GDP. Meanwhile, the ECB and BOJ never managed to raise rates out of negative territory or shrink their balance sheets. It is clear they will not have the tools to reverse the next recession.

Undulations in economic growth are cyclical, so we invest in businesses that benefit from secular trends and are structurally well-positioned to grow over time. Typically, they sell mission-critical or high value-added products and services, which enable them to survive a slowdown. Over longer investment horizons, these businesses become more valuable because they can generate wealth for shareholders even in challenging times. Portfolios are concentrated, which allows us to have a deep understanding of the holdings and watch list ideas, and operate effectively as a small portfolio management team. Our faith in our investment process remains firm.

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BUSINESS UPDATE

During the quarter, Dan Boston resigned from Chautauqua Capital for personal and family reasons and intends to relocate outside of Colorado. We appreciate Dan’s contributions over the past five years and wish him the very best.

Given the collaborative nature of our investment process, it is important that everyone works from our one location in Boulder, Colorado. Dan's responsibilities have been reassigned to existing team members. While we believe that we are adequately staffed, we intend to replace this position. Accordingly, in our hiring process our emphasis is going to be on making the right hire as opposed to a fast hire.

No further organizational changes have taken place.

Respectfully submitted,

The Partners of Chautauqua Capital Management – a Division of Baird

Investment Professional	Educational Background	Years of Experience	Prior Affiliation
Brian Beitner, CFA *Managing Partner*	MBA, University of Southern California BS, University of Southern California	39	TCW Group Scudder Stevens & Clark Bear Stearns Security Pacific
Jesse Flores, CFA *Partner*	MBA, Stanford University BS, Cornell University	13	Roth Capital Partners Blavin & Company Lehman Bros.
Haicheng Li, CFA *Partner*	MBA, Stanford University MMSc, Harvard Medical School MS, Harvard University BA, Rutgers University	18	TCW Group
David Lubchenco *Partner*	MBA, University of Denver BA, The Colorado College	26	Marsico Capital Management Transamerica Investment Management Janus Capital
Michael Mow, CFA *Partner*	MBA, University of Southern California MS, University of Iowa BA, California State University, Northridge	32	American Century TCW Group Farmers Insurance

The above commentary does not provide a complete analysis of every material fact regarding any market, industry, security or portfolio. Strategy 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 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 24 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 March 31, 2019.

The Chautauqua Capital Management Strategies are available to institutions and persons with a minimum account asset value of $50,000,000, which is negotiable in certain instances.

For additional important information about the fees, expenses, risks and terms of investment advisory accounts at Baird, please review Baird's Form ADV Brochure, which can be obtained from your financial advisor and should be read carefully before opening an investment advisory account.