QV UPDATE

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Some of These Things are Not Like the Others

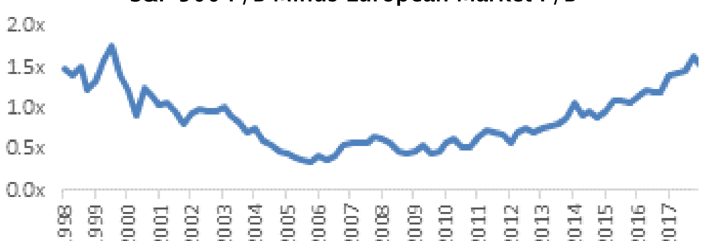
After a multi-year rise in global equities, "where to from here?" is a natural question which investors may be asking in the wake of October's abrupt market correction. As history has repeatedly shown, the combination of extended corporate leverage, widespread risk-taking and high asset prices should be respected late into a market expansion as monetary policy begins to tighten. Caution is rightly warranted, as is the acknowledgement that volatility will likely become more commonplace as the world retreats from 10 years of extraordinary monetary stimulus. Remaining focused on valuation however, still offers prudent investors a reasonable path forward.

Not all markets are likely to behave the same in the future: The global bull market in equities has been overwhelmingly driven by the S&P 500 in recent years and US stocks now exhibit valuation excesses which most other geographies do not. For example, the German DAX and the Hang Seng have already been through bear markets in 2018, falling 19% and 27% from peak to trough. Today, their valuations seem quite reasonable relative to long term averages.

	Price to Book	LT Avg	Dividend Yield	LT Avg
Europe	1.7x	1.8x	3.8%	3.5%
Hong Kong	1.2x	1.5x	3.9%	3.3%
TSX	1.7x	1.9x	3.1%	2.8%
S&P 500	3.3x	2.7x	1.9%	2.0%
Japan	1.3x	1.3x	2.3%	1.9%

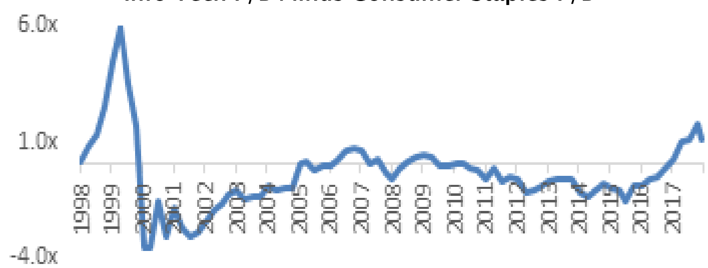
Consider also that European stocks have underperformed their US peers by an unprecedented amount since 2008. Today, the US market trades at the largest price to book (P/B) premium to Europe since the height of the tech bubble, after which Europe significantly outperformed the US. Over time, valuation differentials become important determinants of relative market returns.

S&P 500 P/B Minus European Market P/B



Not all sectors are likely to behave the same in the future: Despite median company valuations hovering near all-time highs in the S&P 500, valuation dispersion among sectors remains surprisingly wide. In the last five years, rapid growth within information technology and consumer discretionary have led to market leading returns, but also elevated multiples. Meanwhile, sectors like consumer staples and energy have faced growth headwinds and still trade at or below long-term average levels on most metrics. The current valuation differential between strong and weak performing sectors has rarely been wider. For instance, information technology's P/B premium to consumer staples is shown below at a historically elevated level. In some respects, this chart is a proxy for risk taking - investors are currently willing to pay significantly more for higher expected growth in information technology relative to slower expected growth generated by consumer staples. As exogenous factors (hint: interest rates) change, these valuation spreads should lead to very different sector returns.

Info Tech P/B Minus Consumer Staples P/B



Not all stocks are likely to behave the same in the future: On the most granular basis, many good quality businesses are cheap. Below is a sample of diverse holdings in QV's Global Equity Strategy which are very attractively priced relative to historical ranges as well as the S&P 500. At current levels, we expect reasonable return profiles from these businesses, despite the potential for a more volatile market environment.

	Price to Earnings	Dividend Yield
AT&T	8.5x	6.6%
Royal Dutch Shell	9.7x	6.0%
Walgreens	12.3x	2.2%
Wells Fargo	10.8x	3.2%
S&P 500	**16.0x**	**1.9%**