

# Why International Small Capitalization Equities?

Since 1981 CBIS has provided Catholic institutional investors access to prudently diversified portfolios and multi-manager stand-alone investment strategies, inclusive of domestic bonds and global equities. CBIS has over this time anticipated the evolving needs of this unique market and delivered tailored investment solutions, the launch last year of the Magnus series of multi-asset funds serving as one example.

CBIS recently completed an assessment of the international small-cap equities investment opportunity and concluded that an allocation to the asset class may enhance returns, broaden diversification and reduce overall portfolio risk. The comparative data become more compelling when active management is factored in (versus indexing), leveraging the relative price inefficiency of the international small-cap space.

## THE OPPORTUNITY SET

The international small-cap opportunity set is large in number and its market capitalization is comparable in size. [Exhibit 1a and 1b].

EXHIBIT 1A  
Number of Securities: as of 6/30/2019

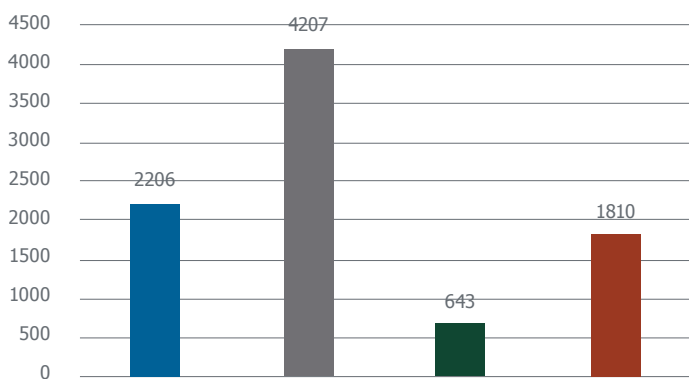
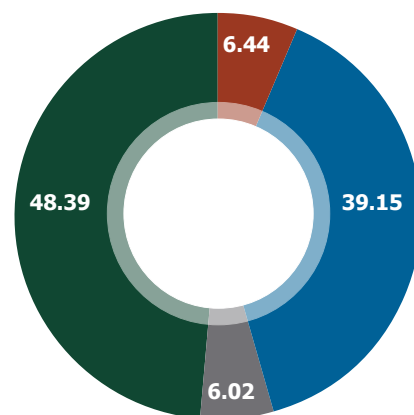


EXHIBIT 1B  
Global Equity Universe: by Percent



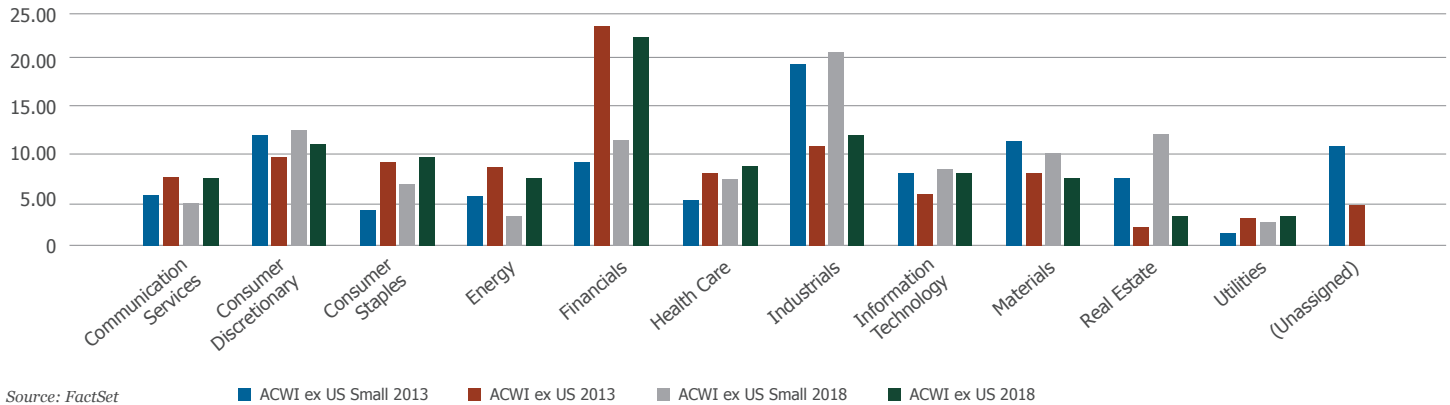
Sources: FactSet, MSCI

■ International Large/Mid Cap 
 ■ International Small Cap 
 ■ US Large/Mid Cap 
 ■ US Small Cap

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Familiar economic sectors are well represented in the international small-cap space and their relative weights exhibit a few notable deviations from the non-US large cap space. For example, exposure to Financials is roughly half that found in the large-cap space and exposure to Industrials is nearly double that found in the large-cap space. These relationships have not changed significantly over the past five years [Exhibit 2].

EXHIBIT 2  
Benchmark Sector Comparison: 2013 vs 2018

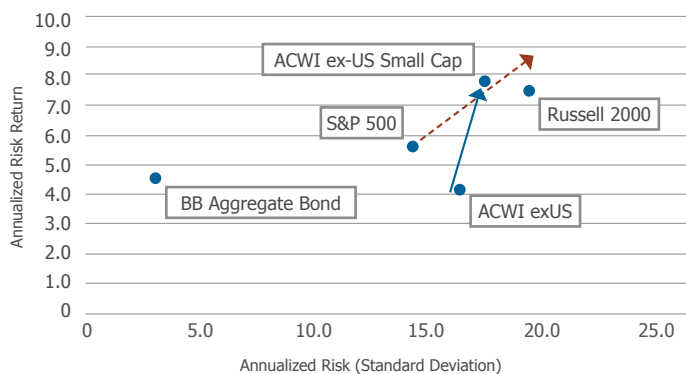


Source: FactSet

## RETURN & DIVERSIFICATION BENEFITS

Over the past twenty years small-cap stocks generated enhanced returns paired with greater volatility (standard deviation) relative to large-cap stocks [Exhibit 3]. Interestingly, during that time US small-cap stocks exhibited greater volatility than non-US small-cap stocks (S&P 600 and Russell 2000 versus ACWI ex-US Small Cap). While the incremental return from moving from large cap stocks to small caps stocks is similar for both the US and non-US markets, the increase in volatility has been lower in the non-US sector as exhibited by the difference in slope between the blue and red lines.

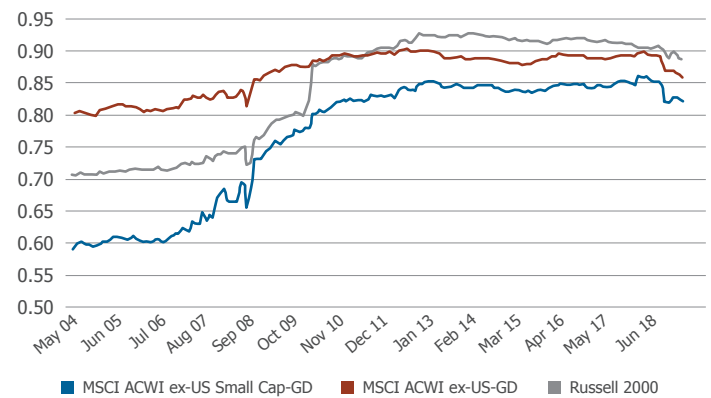
EXHIBIT 3  
Twenty Years Ended December 31, 2018



Source: eVestment

From a diversification standpoint non-US small-cap stocks have exhibited lower correlation with large-cap US stocks (i.e. S&P 500), relative to US small-cap and non-US large cap stocks [Exhibit 4]. One can therefore say that the asset class has provided meaningful diversification over time whereas non-US large cap and US small-cap stocks have trended toward tighter correlation to the S&P 500.

EXHIBIT 4  
Rolling Ten-Year Correlations vs S&P 500



Source: eVestment

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## ACTIVE VERSUS PASSIVE MANAGEMENT

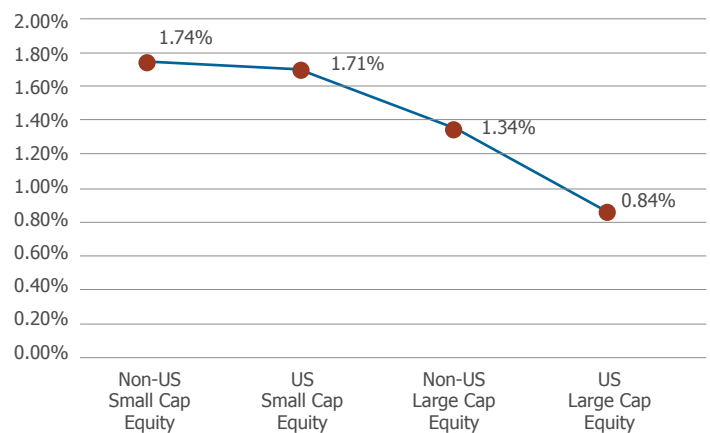
At CBIS, we believe our particular strength is in combining highly-qualified, complementary managers to implement an active investment strategy. In doing so CBIS considers the persistence of each manager's outperformance relative to the desired benchmark, risk mitigation strategies, the quality of the investment team and robustness of support systems, among others. An active manager's excess return over rolling periods, relative to a standard benchmark, is one way to measure persistence.

Exhibit 5 illustrates the median ten-year rolling excess return generated by all investment managers tracked within each eVestment peer universe shown. An index manager would, by definition, be expected to generate 0.0% in excess return over time, before fees. Exhibit 5 indicates that active managers have over time added value relative to an indexed approach for the strategy categories indicated, with non-US small-cap equities modestly outpacing the four peer groups.

## CONCLUSION

Based on the comparative data presented in this paper, a historical allocation to actively managed non-US small-cap equities would have generated diversified, risk-adjusted returns within the context of a prudently diversified institutional portfolio. CBIS believes this historical pattern is likely to persist. Consequently, CBIS intends to provide Catholic institutional investors access to this attractive asset class, in a manner consistent with Catholic values, through the CUIT Magnus Funds and as a stand-alone option. Stay tuned!

EXHIBIT 5  
Median 10-Year Rolling Excess Return vs Investment Managers' Preferred Benchmarks, Within Their Respective eVestment Peer Universe (June 2009 to March 2019)



Source: All investment managers tracked within each eVestment peer universe shown.

### Disclosures

This article is for informational purposes only and is not an offer to sell any security nor a solicitation of an offer to purchase any security. The International Small Capitalization Equity Fund is not launched. If this fund is launched, an offer will only be made, when and where available, through the CUIT Offering Memorandum and the fund may only be sold in compliance with all applicable state securities laws.