Quarterly commentary

Blue Chip Equity

2017 third quarter

Performance overview

U.S. equity markets continued their march higher, with major market indices posting solid gains for the third quarter in a row to start 2017. Many asset classes rose during the period, with investors willing to take on more risk. Categories that are typically more volatile, such as small-cap and international stocks, led the way during the quarter. Larger companies did maintain their lead over smaller peers, however, when considering all of 2017 to date. Companies classified as Growth outpaced Value for the third straight quarter. The Russell 1000 Growth Index's return for the year is now more than 12% better than the return of the Russell 1000 Value Index.

The strategy outperformed the Russell 1000 Growth Index in the third quarter. MasterCard and Visa were two of the portfolio's largest contributors. These businesses are the leaders in an industry that has high barriers to entry and a long runway of growth ahead. Starbucks and Amazon were two of the portfolio's detractors during the period. Both companies continue to benefit from competitive strengths and owner-operator leadership. More information about these companies and the other contributors and detractors can be found in the sections below. We remain confident in the companies we own, as they possess competitive advantages that enable them to increase intrinsic value over time.

Our process remains the same. We are bottom-up, long-term investors, seeking to own high quality companies with sustainable competitive advantages that are managed by owner-operators. We purchase these companies at a discount to their intrinsic value in order to have a margin of safety. We focus on reducing risk from the beginning of our process all the way through to monitoring the companies in the portfolio. While quarterly results may fluctuate and lower quality companies may outperform for periods of time, we are confident that our strategy will outperform over a full market cycle, delivering the superior long-term risk-adjusted results that our process has consistently produced.

Index scorecard third quarter 2017 (in U.S. dollars)

Blue Chip Equity	6.22%
Russell 1000 Growth	5.90%
Russell 1000 Value	3.11%
Russell 1000	4.48%
S&P 500	4.48%
Russell Top 200	4.88%
Russell Midcap	3.47%
Russell 2000	5.67%

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Composite performance as of 30 September 2017

	Three months	One year	Three years	Five years	Since Inception[1]
Blue Chip Equity *(gross)*	6.22%	20.73%	14.27%	15.84%	16.24%
Blue Chip Equity *(net)*	6.10%	20.17%	13.74%	15.27%	15.68%
Russell 1000 Growth Index	5.90%	21.94%	12.68%	15.25%	15.77%
Excess return *(based on gross returns)*	0.32%	-1.21%	1.59%	0.59%	0.48%

[1]Inception date: 1 July 2012. Returns are expressed in U.S. dollars. Periods over one year are annualized. Outperforming the benchmarks is not specifically included within the strategy's objectives. They are shown for comparative purposes only. The two methods of calculation of performance may not be identical and it is not possible to invest in an index. Past performance is not a reliable indicator of future performance and should not be relied upon as a significant basis for an investment decision. Due to rounding, figures and percentages shown may not add to the totals or equal 100%. You should consider whether an investment fits your investment objectives, particular needs and financial situation before making any investment decision. See end of document for additional disclosure information.

Top five contributors

MasterCard is a technology company that provides transaction processing and other payment-related services in the United States and internationally. MasterCard is the third-largest competitor in the global electronic payments market, with over US$3 trillion in annual purchase volume. Electronic payments have a long runway of growth ahead of them, as 85% of payment transactions globally are still cash and check (versus roughly 50% in the United States). As consumers continue to gravitate from cash to plastic, MasterCard stands to benefit. Furthermore, the barriers to entry are substantial, given the incumbents' massive scale and global reach, as well as security and data management skills. MasterCard's shares increased over the last three months due to strong quarterly results.

Visa is a dominant company in the global electronic payments market, accounting for roughly half of all credit card transactions and nearly three-fourths of debit card transactions in recent years. With 85% of payment transactions globally still conducted via either cash or check, Visa has a tremendous runway of growth ahead. The scale of Visa's global infrastructure is very difficult to replicate, and is a firm barrier to entry while also benefiting the company through continual network effects. New payment systems rely on, rather than replace, the incumbents' networks, showing the strength of the competitive advantage. Visa performed well during the past three months.

Berkshire Hathaway is a diversified company with businesses ranging from insurance to railroads. The company has been built over decades by owner-operators Warren Buffett and Charlie Munger. Over the company's 51-year history, its average annual return has more than doubled that of the S&P 500. Berkshire has a very long time horizon, never intending to sell its businesses. This long-term perspective has enabled Berkshire to be aggressive during times of market fear, building an impressive track record of value-adding capital allocation. The company is decentralized and remains committed to giving its businesses autonomy. The stock price increased during the third quarter and we continue to view Berkshire's businesses favorably.

Alphabet's core Google business has tremendous advantages and will continue to benefit as advertising budgets move from traditional media to where people increasingly spend their time. Additionally, businesses such as YouTube are at the beginning of a path to greater monetization. The long-term perspective of Alphabet's founders, Larry Page and Sergey Brin, continues to be an underappreciated asset. Alphabet recently reported solid results driven by growth in mobile search.

CarMax is the largest used car retailer in the U.S. with more than 170 locations. CarMax purchases, reconditions, and sells used vehicles, operates wholesale auctions on their store lots, and provides financing to their used vehicle customers through CarMax Auto Finance. The company offers low, no-haggle prices across a broad selection of high-quality vehicles. Due to its disciplined inventory management, CarMax is positioned to perform well throughout the auto cycle. CarMax posted very good third quarter results, and its share price performed well.

Top five detractors

Starbucks sells gourmet coffee, tea, related products, and more recently, a coordinated offering of food from its more than 23,000 stores around the world. It also sells packaged products via grocery store shelves. Led by owner-operator Howard Shultz, the company continues to innovate, test, and roll out meaningful product and loyalty program initiatives to drive traffic growth. Most recently they've begun testing higher-end Starbucks Reserve store formats. Starbucks shares declined slightly over the last three months. This was mainly due to a slowdown in U.S. sales growth.

DENTSPLY Sirona is a global dental solutions provider focused on developing and commercializing dental supplies and equipment on a worldwide basis. With the merger of equals between DENTSPLY and Sirona now completed, the combined entity now provides products across the entire dental value chain. DENTSPLY is now the world's largest provider of consumable dental products for the professional dental market, with one of the broadest product portfolios offered in the industry. Sirona has been one of the leaders in the dental equipment space. DENTSPLY's share price fell during the third quarter due to softer-than-expected second quarter results as benefits of this merger have been slow to develop. We continue to view positively the long-term prospects of the company.

AutoZone is a retailer in the auto parts aftermarket, serving primarily consumers who repair their own vehicles. AutoZone has one of the industry's largest footprints, with more than 5,800 stores. The company has many advantages relative to smaller competitors and continues to play a role in the industry's consolidation of smaller stores. For the last several years AutoZone, now in a more mature phase of its growth, has sensibly deployed a substantial amount of free cash flow toward buying back its own shares. AutoZone shares declined during the third quarter on concerns about the potential of online competition.

Amazon is an e-commerce company started by Jeff Bezos in 1994. Originally developed as an internet site to sell books, today the company sells a wide variety of products to people around the world. Amazon benefits from the virtuous cycle of using its scale and existing network to provide lower prices and a better experience to customers. Amazon continues to invest to increase long-term intrinsic value, which has included building a leading position in the fast-growing market for cloud services, where Amazon Web Services is now the dominant competitor. Bezos still owns 17% of the company and is focused on profitability, but he has a long-term mindset and doesn't emphasize quarterly earnings reports. Amazon shares were slightly negative during the third quarter.

Martin Marietta Materials is the second largest producer of aggregates in the United States. The company's aggregate business has strong barriers to entry due to high transportation costs and regulation and is well positioned in some of the higher growth areas of the United States. In addition, the company continues to benefit from the ongoing recovery in the housing and road construction end markets. Martin Marietta shares declined in the third quarter due to weak aggregates volume, particularly in their high margin Southeast area where weather had some impact.

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