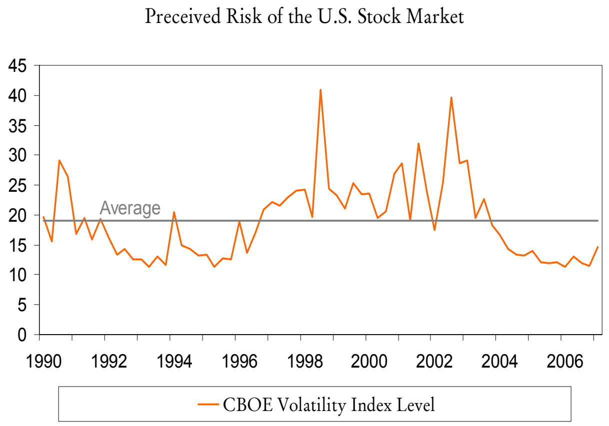
High Pointe

Newsletter - 1st Quarter 2007

The Changing Nature of Risk

Economic Environment

Global equity markets produced modestly positive returns during the first quarter of 2007 despite higher oil prices, a slowing U.S. housing market, subprime loan defaults, and lower corporate earnings growth. The S&P 500 index was up 0.6% during the first quarter.



Source: Chicago Board Options Exchange

In our last quarterly letter, we noted that the perceived risk priced into the U.S. stock market had dipped to historic lows. Things changed a bit during the first quarter, as the risk, measured by the implied 12-month volatility for the S&P 500 Index, increased by more than 20%. While still at a low level in absolute terms, the percent increase during the quarter was the highest since the end of the 2000-2002 bear market.

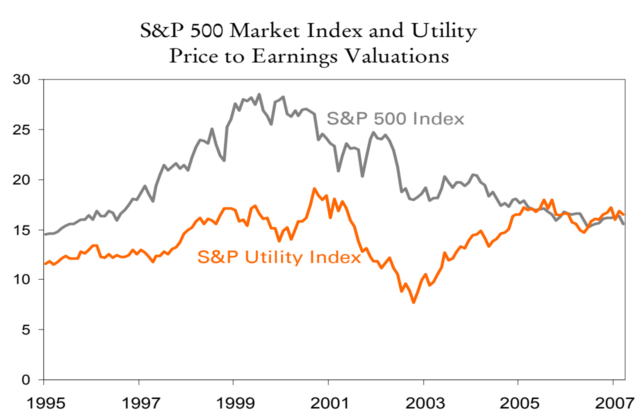
Higher oil prices, stemming from tensions in the Middle East and supply disruptions, as well as a slowdown in the U.S. housing market and a subsequent increase in subprime mortgage defaults contributed to the increase in volatility. Since late last year, more than 24 subprime lenders have declared bankruptcy.

Borrowers which capitalized on "teaser" rates and no-money-down offers during the low interest rate environment of 2002 to 2004, face declining home prices and substantially higher mortgage costs, as interest rates on their adjustable mortgages are being reset higher. Tighter lending standards have and likely will continue to soften housing prices and that will have an impact on consumer spending habits. However, for most individuals, the direct impact will come over time and not all at once. While the current state of the subprime market is worth a note of caution, the wider effects are still unclear. Contagion, or the spread of defaults to prime-quality areas of the credit market, is a concern but not a foregone conclusion.

Utilities are one sector of the U.S. equity market which has been resilient now for several years. This sector continued its positive momentum during the first quarter appreciating by 8.6%. Utilities have become pricier because of deregulation, more favorable tax laws, private capital interest, and investor demand for high-yielding securities.

High-yielding, countercyclical investments like utilities may continue to sell at a higher premium compared with historical valuations as the economic expansion slows and baby boomers reinvest in income-producing securities during retirement. However, we believe that the sector has become too dear and perhaps more risky than perceived.

Price-to-earning ratios for the utility sector have trended higher since the end of the 2000-2002 bear market in both relative and absolute terms as shown to the right. Since October of 2002, utilities' stock prices have appreciated faster than the overall market (as measured by the S&P 500 Index), while their earnings have grown more slowly. Utilities currently trade at valuations that are higher than the broader market despite lower expected future earnings growth. (Continued on page 2)

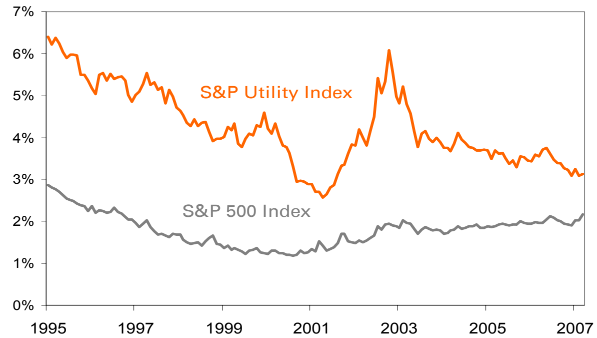


Source: Thomson Financial

The Changing Nature of Risk (Continued)

Price appreciation also has led to a decline in dividend yields for utilities from 6% to 3% in just over a decade. During the same period, dividend yield for the broader market has increased from 1.8% to 2.2%, thus closing the income gap to less than 1%. Indeed, utilities have offered protection during times of broad equity declines. The downside return capture of the utilities sector relative to the S&P 500 Index has been 68% since 1995. As volatility returns to equity markets and risk premiums revert to their long-term averages, utilities may not offer as much protection as history suggests.

S&P 500 Market Index and Utility Valuations
Dividend Yield



Source: Thomson Financial

To summarize, the market's view of risk has changed dramatically over the last three years. Companies with cyclical, volatile businesses such as commodities and energy, as well as low growth businesses like utilities, are being assigned low risk premiums (and high valuations), whereas companies with strong franchises in consumer, healthcare, and technology sectors are being assigned high risk premiums and correspondingly low valuations. In our opinion, this situation will not last!

Investment Strategy Update

Our **Large Cap Value** strategy returned -2.9%, net of fees, during the first quarter, while the Russell 1000 Value Index returned 1.2%. The shortfall was primarily a result of unfavorable stock selection in financials and health care, which detracted 1.9% and 1.1%, respectively, relative to the Index.

Our financial holdings were hindered by their exposure to the mortgage industry. As mentioned in our economic environment update, weakness in the subprime market and a slowdown in the housing market led to lower prices across the entire mortgage industry, including our holdings even though they had very little exposure to the subprime market. We remain comfortable with our positions as we believe they represent excellent long-term values even if the housing downturn worsens. An underweight to financials, relative to the Index, helped relative performance during the quarter. (Continued on page 3)

Investment Performance

For Periods Ending March 31, 2007

	1st QUARTER	1 YEAR	3 YEARS	5 YEARS	7 YEARS	SINCE INCEPTION*
Large Cap Value						
Gross	-2.76%	7.50%	8.04%	8.57%	14.73%	15.11%
Net	-2.91%	6.87%	7.43%	7.86%	13.89%	14.19%
Russell 1000 Value Index	1.24%	16.83%	14.42%	10.24%	7.92%	8.49%
Large Cap Growth						
Gross	1.17%	6.51%	8.39%	6.19%	-0.30%	11.46%
Net	0.99%	5.73%	7.41%	5.20%	-1.24%	10.42%
Russell 1000 Growth Index	1.19%	7.06%	7.01%	3.47%	-5.64%	-1.53%
Small Cap Equity						
Gross	2.84%	6.21%	13.67%	15.07%	15.44%	14.13%
Net	2.66%	5.54%	12.87%	14.14%	14.48%	13.14%
Russell 2000 Index	1.95%	5.91%	12.00%	10.94%	7.16%	8.09%

*Inception Dates: Large Cap Value - January 1,1998; Large Cap Growth - August 1, 1999; Small Cap Equity - January 1, 1998. Please see Performance Notes on the last page for additional disclosures.

Investment Strategy Update (Continued)

A study regarding a new drug coated stent by a competitor negatively affected our medical device holdings at the end of the quarter. We have maintained our position because of favorable long-term prospects for this industry and the deep discount at which our holdings sell relative to their peers.

An underweight to utilities (9.4% return) and materials (11.6% return) hindered performance during the quarter. While these two sectors represented only 10% of the Index by market capitalization, they accounted for 80% of the Index's return during the last three months.

Our security selection was favorable in consumer staples (12.0% return versus 2.4% for the benchmark) and industrials (4.3% return versus 2.2% for the benchmark), as our companies demonstrated improved financial results and benefited from corporate restructuring.

There were no changes made to the composition of the portfolio during the first quarter.

Following strong fourth quarter results, High Pointe's **Large Cap Growth** product (1.0% return) performed slightly below the Russell 1000 Growth Index (1.2% return) during the first quarter on a net of fees basis.

Security selection was positive across the information technology, industrials, and consumer discretionary sectors. Information technology performance was driven by improved operating margins in our technology distribution and internet-related holdings. Our positions also benefited from low starting valuations relative to the sector overall. Our industrial holding performed well due to a planned corporate restructuring, which should add value as conglomerate discount is removed.

Organizational Update

We are pleased to announce the addition of Matt Clink to our growing team of investment professionals. In his role as Quantitative Analyst / Product Manager, he will contribute by enhancing our quantitative stock selection model as well as act as a liaison with investment consultants. Previously, Matt served as director of investment research at Hewitt Investment Group and was an investment consultant with Clark Strategic Advisors. Matt holds the Chartered Financial Analyst designation and he is a member of the CFA Institute and CFA Society of Chicago. He attended the University of Alabama where he graduated Summa Cum Laude with both his Bachelors and Masters Degrees in Finance.

Stock selection was weak in energy, as our oil services holding sold off due to lower demand for its products during the quarter. An overweight to information technology and an underweight to energy, utilities, and materials detracted from results. In particular, energy, utilities, and materials, which in aggregate accounted for less than 10% of the Index's market capitalization, contributed 50% of the Index's performance during the quarter.

Our **Small Cap** strategy was up 2.7% during the first quarter, rebounding from a relatively weak 2006 and leading the Russell 2000 Index by 70 basis points, net of fees. Sector selection was positive across all ten sectors, most notably in financials (underweight) and consumer discretionary (overweight).

While we were underweight in financials, our mortgage and insurance holdings underperformed the market. We believe the sell off in the mortgage industry was too inclusive, with the risk of contagion spreading to issuers of high-quality loans still a low probability at this point. Our insurance holdings were negatively impacted by guidance regarding the softening reinsurance pricing in 2007, owing to the lackluster 2006 hurricane season. Security selection was positive in the technology distribution, wholesale services, and waste management industries where strong results were driven by improved pricing power and profit margins.

Gautam Dhingra, PhD, CFA

CEO & Portfolio Manager

Performance Notes

1. Performance data are shown gross and net of management fees and are based on composites of all fee-paying, fully-discretionary accounts. 2. Returns for the periods presented are time-weighted. 3. Results shown include the reinvestment of dividends, capital gains and other earnings. 4. The currency used to express performance is U.S. dollars. 5. High Pointe's fee schedules are disclosed in Part II of the firm's Form ADV. 6. All fully discretionary, fee-paying accounts have are included in at least one composite. 7. No alterations of the composites as presented in this report have occurred because of changes in personnel or for any other reasons at any time. 8. The composite results portrayed during the period are compared to the performance of their respective indices because the securities purchased for each of the composites are most closely aligned with the securities comprising these indices. 9. Performance results have been examined through 12/31/05 by an independent verification firm. 10. A complete list of firm composites and performance results is available upon request. 11. Returns represent past performance and are not indicative of future results. 12. The Russell 1000 Value, Russell 1000 Growth, and Russell 2000 Indices are unmanaged indices commonly used to measure the performance of U.S. stocks. You cannot invest directly in an index.