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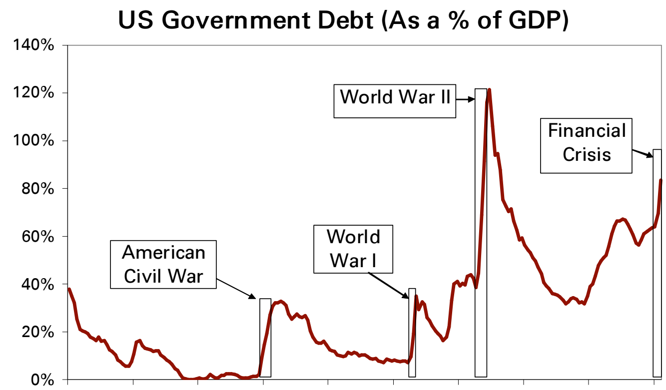
High Pointe

DATE: July 15, 2010
TO: Clients
FROM: Gautam Dhingra
RE: Economic and Portfolio Review

House of Blues

Things are calm on the surface. The worst of the financial crisis seems to be behind us. The economy is growing. Home prices have stabilized. The stock market has recovered a significant portion of its losses. Employment numbers have stopped deteriorating. All good news!

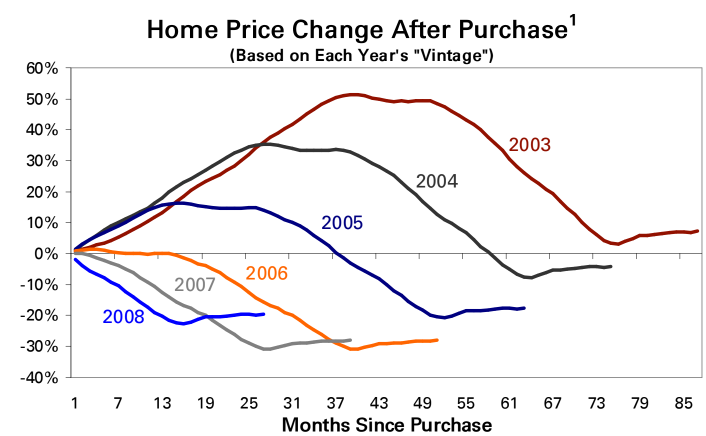
Beneath the surface, however, pressures are building once again. A key pressure point is the debt that the government is incurring in order to restore market stability. The chart to the right shows U.S. government debt as a percent of GDP, going all the way back to late 18th century. The data show periodic spikes in debt level caused primarily by war spending. The most recent spike, however, is not caused by a military war. Instead it is caused by the Government's attempt to counter the financial crisis.



Source: US Government Debt: US Treasury, US Nominal GDP 1790-2009: Louis D. Johnston and Samuel H. Williamson, "What Was the U.S. GDP Then?" MeasuringWorth, 2009. URL: http://www.measuringworth.org/usgdp/

The financial crisis was triggered by a decline in U.S. home prices that started in 2006. The chart to the right shows change in home prices assuming purchases on January 1 of each year from 2003 to 2008. As home prices declined, our government launched a massive effort to stem the decline through actions such as:

- The bailout of Fannie Mae and Freddie Mac
- Buying of mortgage securities by the Fed
- Lowering of interest rates
- Cash incentives to induce home purchases
- Programs to avoid/delay foreclosures

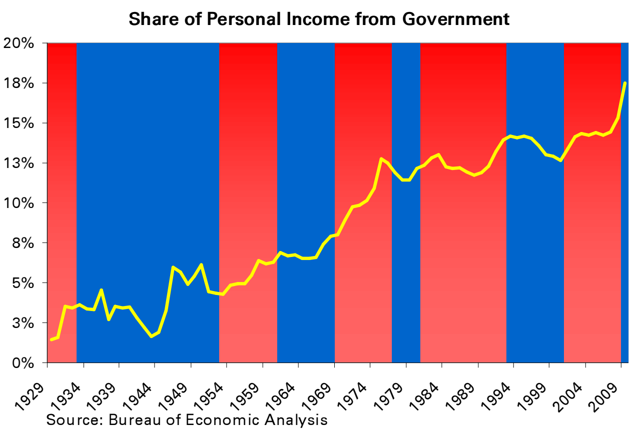


[1] Assumes purchase of home on January 1, based on the Case-Shiller Index.

Source: Standard & Poor's Case-Shiller Index

The government's efforts to stem home price decline have met some success as indicated by the flattening of the lines in the previous chart. However, the question is what happens when the government withdraws its support. A recent report by Morgan Stanley projects that housing prices will likely drop another 5% - 10% over the next year. So, the government's actions may have simply delayed the inevitable and it is likely that we will be singing the housing blues for some time to come.

The government has the option of continuing its support of the housing market but it is unlikely to do so for two reasons. One, the share of an average citizen's income coming from the government (social security, Medical, unemployment insurance) is at an historical high as shown by the chart on the right. Interestingly, the increase has occurred regardless of whether we had a republican president (red area) or a democratic president (blue area). Secondly, and more importantly, the government risks hurting its credit rating if it continues its current policy of borrowing to support home prices.



Credit ratings of several European countries that engaged in binge borrowing, such as Greece and Portugal, have been cut recently forcing them to pay higher interest rates and compelling them to take austerity measures that will lead to lower standards of living. The table below shows how our debt level compares to the European countries that are considered to be most troubled.

	U.S.	Greece	Portugal	Spain	Italy	Ireland
Debt as a % of GDP	56%	86%	56%	33%	97%	25%

It is clear that our debt level is actually higher than that of many countries considered to be in trouble. We do have some structural advantages such as having an independent currency, being able to borrow in our own currency, and having a more flexible economy. As a result of these structural advantages we are not in an imminent danger of losing our top-notch credit rating. Nevertheless, events in Europe are a reminder for us to get our house in order before it is too late. United Kingdom, which is in a position similar to our own, recently announced spending cuts as a first step towards fixing its fiscal system. Washington, on the other hand, is completely silent on this issue!

Unlike the government, high quality U.S. corporations have been repaying their debt and strengthening their balance sheets. Many of these high quality companies are not substantially impacted by the housing problem. Best of all, they are selling at valuation levels that are no higher than the valuation of more speculative companies. This is the universe of stocks we at High Pointe are trolling to find investment opportunities for the next few years.

Investment Returns

The returns of our main products are summarized below and a discussion of our investment strategy follows in the next section.

High Pointe Capital Management
Investment Performance (Net of Fees)[1]
For Periods Ending June 30, 2010

	2nd Quarter	One Year	Three Years	Ten Years	Since Inception[2]
Small Cap	**-8.1%**	**24.5%**	**-8.4%**	**8.6%**	**7.7%**
Russell 2000 Index	-9.9%	21.5%	-8.6%	3.0%	4.0%
Large Cap Value	**-9.3%**	**15.4%**	**-11.8%**	**5.3%**	**7.6%**
Russell 1000 Value Index	-11.1%	16.9%	-12.3%	2.4%	3.3%
Large Cap Growth	**-15.5%**	**2.2%**	**-9.8%**	**-1.4%**	**4.9%**
Russell 1000 Growth Index	-11.8%	13.6%	-6.9%	-5.1%	-2.4%
International Equity	**-11.4%**	**11.3%**	**-8.7%**	**N/A**	**-5.0%**
MSCI All Country World ex US Index	-12.5%	10.4%	-10.7%	N/A	-6.2%

[1]Performance for the latest quarter is preliminary and subject to change
[2]Inception Dates: Small Cap – January 1, 1998; Large Cap Value - January 1, 1998; Large Cap Growth – August 1, 1999; International Equity – December 28, 2006.

Performance results are shown net of management fee, and are based on composites of all fee-paying, fully-discretionary accounts. Returns for the periods presented are time-weighted. Results shown include the reinvestment of dividends, capital gains and other earnings. The currency used to express performance is U.S. dollars. High Pointe's fee schedules are disclosed in Part II of the firm's Form ADV. All fully discretionary, fee-paying accounts have are included in at least one composite, and no accounts have been terminated since the inception of each of the composites. 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. 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.

High Pointe Capital Management, LLC has prepared and presented this report in compliance with the Global Investment Performance Standards (GIPS®). A complete list of firm composites and performance results is available upon request. The CFA Institute has not been involved with the preparation or review of this report. Returns represent past performance and are not indicative of future results. Investment may result in the loss of principal.

*The unmanaged **Russell 2000 Index** measures the performance of the 2,000 smallest companies in the Russell 3000 Index. The Russell 3000 Index is comprised of the 3,000 largest U.S. companies based on total market capitalization.*

*The unmanaged **Russell 1000 Value Index** measures the performance of those securities in the Russell 1000 Index having lower price-to-book ratios and lower forecasted growth values. The unmanaged **Russell 1000 Growth Index** measures the performance of those securities in the Russell 1000 Index having higher price-to-book ratios and higher forecasted growth values. The unmanaged Russell 1000 Index is comprised of 1,000 of the largest capitalized companies that are traded in the United States.*

*The **MSCI All Country World ex-U.S. Index** measures the equity market performance of world's developed and emerging markets. As of June 2009 the index consisted of 44 countries (22 developed and 22 emerging countries).*

These indices do not reflect fees and expenses associated with the active management of separate account portfolios.

Investment Strategy

Small Cap

High Pointe's Small Cap strategy produced a return of -8.1% during the quarter, outperforming its benchmark, the Russell 2000 Index by 1.8%. During the quarter, security selection added value, especially in the consumer staples and industrial sectors.

We took profits in our largest holding when it agreed to be acquired by a large consumer products company at a significant premium. Our investment in the airline industry benefited from lower capacity and less competition leading to better pricing. In addition, a supplier of products needed for steel manufacturing performed well as global demand increased.

During the quarter we increased our allocation to the materials and financial sectors and correspondingly reduced our allocation to the consumer staples sector. We sold a health care equipment company that failed to meet our execution standards, and an oil and gas service firm because of the offshore drilling moratorium. The proceeds were invested in paper packaging, asset management, reinsurance, biotechnology, and oil and gas refining.

Large Cap Value
High Pointe's Large Cap Value strategy produced a return of -9.3%, which was 1.8% better than its benchmark, the Russell 1000 Value Index. Positive security selection in the consumer discretionary and consumer staples sectors added the most value. However, this was partially offset by weak stock selection in the technology sector.

Our investment in an auto parts retailer performed well as consumers started to keep their cars longer. In addition, our investment in the satellite television industry benefited from a better programming lineup and overall better execution compared to its competitors. A packaged food company also helped drive outperformance when it agreed to be acquired at a substantial premium.

We increased our investments in the industrial sector with proceeds from the consumer staples and energy sectors. In particular, we sold a custodian bank that had struggled in favor of an online broker and repositioned our energy investments out of oil exploration and into oil equipment and services industry.

Large Cap Growth
High Pointe's Large Cap Growth strategy produced a return of -15.5%, trailing the Russell 1000 Growth Index by 3.7% for the quarter. Security selection in the health care and technology sectors detracted the most value.

Our investments in the health care sector performed below expectations as a biotechnology company and a medical products manufacturer lowered revenue guidance because of health care reform and pricing pressures. We are maintaining our exposure to both because we believe they offer compelling valuations and reasonable growth opportunities. Also, a leading credit card processor underperformed after an unexpected provision limiting debit card fees was inserted into the financial regulation bill.

During the quarter we increased our investments in the technology and industrial sectors with proceeds from the consumer discretionary and materials sectors. We sold a cable company because it reached our price target, and an investment in the agricultural industry because of weak execution. The proceeds from these sales were reinvested in the global positioning systems, computer and aerospace industries. We also adjusted our oil and gas investments because of uncertainty in offshore drilling

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We are excited by the opportunities created by the recent turmoil which is enabling us to buy high quality companies at no premium relative to the market. We believe this will serve us and our clients well in the coming years. Thank you for the opportunity to manage your assets! Please let us know if you have any questions.