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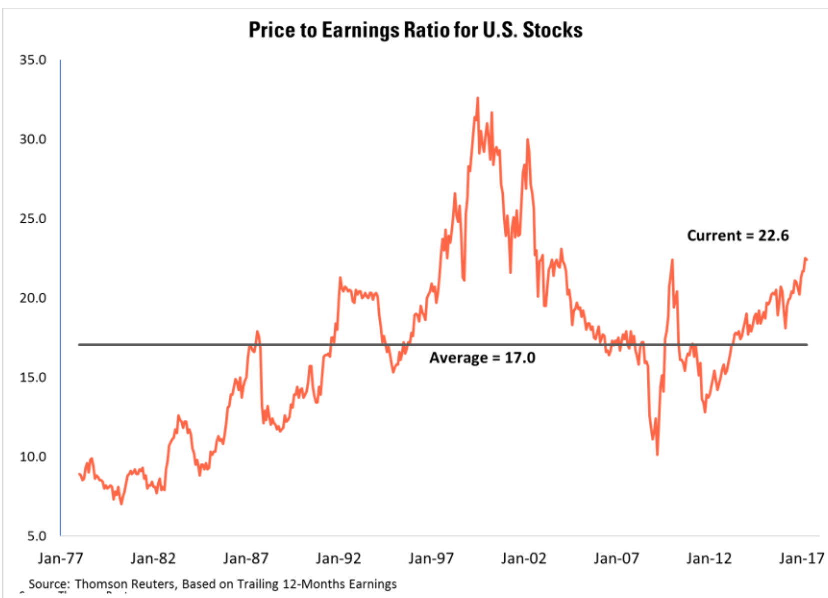
Innovate. Deliver.

High Pointe

Is It Time to Get Real?

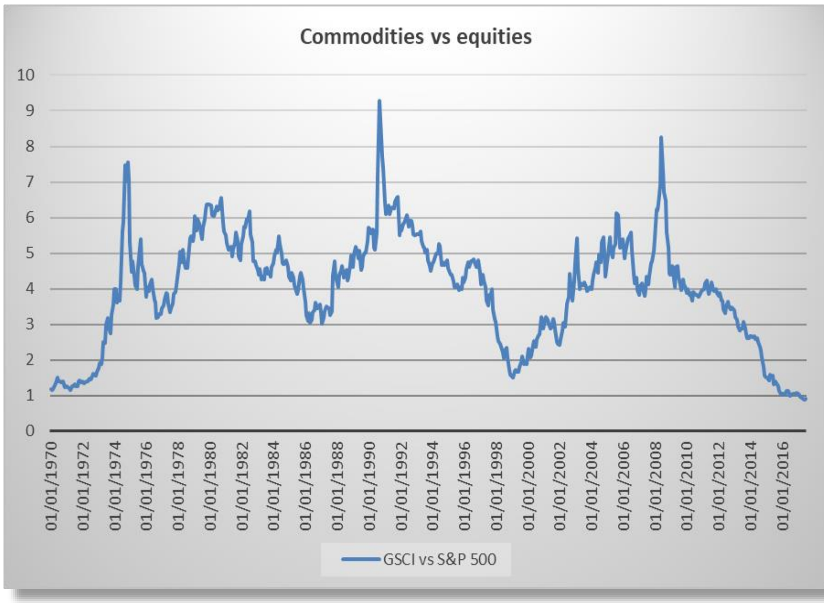
Both the equity and bond markets around the world continue to perform extraordinarily well, providing investors with healthy returns so far in 2017. While we can take some comfort from continued economic growth, modest inflation and ongoing global central bank support of the financial markets, valuations are reaching historic highs. As shown below, the current price/earnings multiple of the S&P 500 Composite Index has now surpassed the high from 2010 and is now back into the territory of the Tech Bubble around the turn of the millennium. It was during that period of excessive optimism with regard to technology stocks that the US equity market reached unsustainable valuation levels.



When looking for investment opportunities, particularly after a strong run in the markets, it is useful to look at areas that have lagged. Quite often it is in those areas where the next set of investment opportunities lie.

One area of note has been the underperformance of real assets relative to financial assets. Real assets are generally defined as assets that have physical properties, such as commodities, precious metals, basic materials, natural resources, real estate, infrastructure and utilities. Financial assets are what we know as traditional equities and bonds. We have previously discussed the benefits of adding hard assets such as gold to investors' portfolios in previous newsletters (Fourth Quarter 2015 and First Quarter 2017) and are expanding our scope to consider a wider array of real assets.

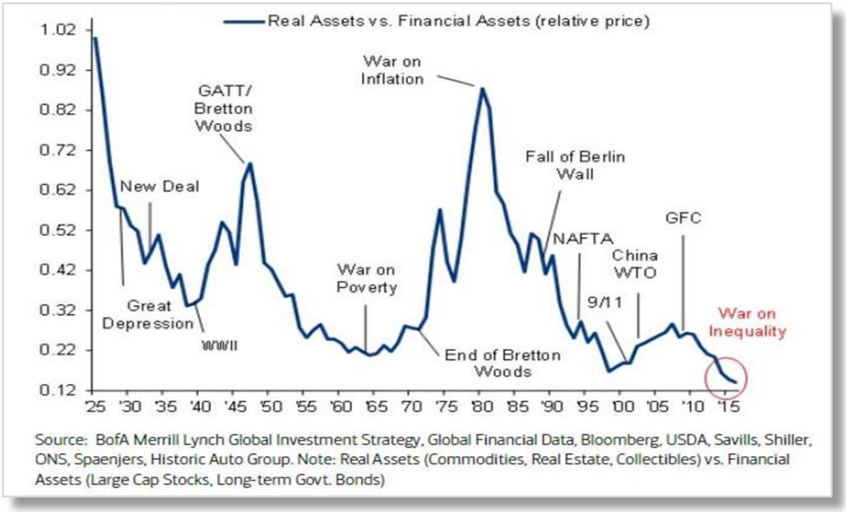
A comparison of the relative returns of commodities (including agricultural commodities, industrial metals and energy in addition to precious metals) versus US equities, as represented by the S&P 500, highlights this recent trend:



Source: Bloomberg

The chart above shows that from 1970 to the early 1990's, commodities outperformed equities by 9 to 1. They subsequently gave back much of this performance by the end of that decade, only to return close to previous highs by the time of the Great Recession in 2008. Now, after a strong run in equities and weak returns in commodities, we are currently at the worst levels of underperformance for commodities versus the S&P 500 in 47 years. While past performance is not indicative of future performance, when commodities had underperformed by such an extent previously, the stage was set for future strong relative returns.

A longer-term chart on the next page showing an expanded definition of real assets (commodities, real estate and collectibles) and financial assets (large cap stocks and long-term government bonds) reveals a similar situation.



Source: BofA Merrill Lynch Global Investment Strategy, Global Financial Data, Bloomberg, USDA, Savills, Shiller, ONS, Spaenjers, Historic Auto Group. Note: Real Assets (Commodities, Real Estate, Collectibles) vs. Financial Assets (Large Cap Stocks, Long-term Govt. Bonds)

With real assets relative to financial assets starting at 1 to 1 in 1925, real assets underperformed financial assets by approximately 80% into the mid-1960s. This drop was almost completely reversed by the early 1980's, only to give back those gains and more by the current time. As shown in the chart above, we are at historic lows for close to a century. Perhaps that is no surprise given the historic rise of the global bond and equity markets in recent years.

While we can't be certain that previous cyclical patterns will re-exert themselves exactly as they have done in the past, it does provide us with an interesting area for further research. As a result, at High Pointe we are actively investigating the real asset investment universe to determine what opportunities may exist for our clients and how best to take advantage of them.

Chris Olson and Gautam Dhingra
October 12, 2017

Investment Returns

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

Investment Performance (Net of Fees)[1]

For Periods Ending September 30, 2017

	One Quarter	One Year	Five Years	Since Inception[2]
Large Cap Value	3.1%	17.9%	14.5%	10.0%
Russell 1000 Value Index	3.1%	15.1%	13.2%	7.2%
Large Cap Growth	3.8%	20.9%	13.1%	9.0%
Russell 1000 Growth Index	5.9%	21.9%	15.3%	4.8%
International Equity	4.1%	17.6%	6.5%	3.1%
MSCI AC World ex US Index[3]	6.2%	19.6%	7.0%	2.9%
Global Opportunity	5.3%	18.7%	n/a	7.0%
MSCI AC World Index	5.2%	18.7%	n/a	8.4%

[1]Performance for the latest quarter is preliminary and subject to change.
[2]Inception Dates: Large Cap Value – January 1, 1998; Large Cap Growth – August 1, 1999; 1998; International Equity – December 31, 2006; Global Opportunity: October 1, 2013.
[3]Gross total return index from December 31, 2006 – December 31, 2009; Net total return index from January 1, 2010.

High Pointe Capital Management, LLC (the "Firm" or "High Pointe") is a registered investment adviser with the Securities and Exchange Commission (SEC) under the Advisers Acts of 1940 and its amendments. High Pointe is an independent investment management firm that is not affiliated with any parent organization.

Policies for valuing portfolios, calculating performance, and preparing compliant presentations are available upon request. Performance results are shown in U.S. dollars, 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 all accrued dividends and interest, realized and unrealized gains and losses. Gross dividends were used to calculate the performance prior to January 1, 2010. As of January 1, 2010, accrued dividends used are net of non-reclaimable withholding taxes. Leverage has not been used in any portfolio in the composite. High Pointe's fee schedules are disclosed in Part 2A of the firm's Form ADV. All fully discretionary, fee-paying accounts are included in at least one composite. 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.

*The **Large Cap Value** composite is comprised of portfolios invested primarily in stocks of companies with market capitalization in excess of $2 billion that offer good "value" relative to other companies in a similar business, their growth potential, or their historical valuation levels. The **Large Cap Growth** composite is comprised of portfolios invested primarily in growth stocks of companies with market capitalization in excess of $1.5 billion that exhibit high expected earnings growth to maximize capital appreciation. The **International Equity** composite invests in stocks that are primarily domiciled in a country other than the U.S., including emerging markets, without any constraints regarding capitalization or style. The **Global Opportunity** composite invests opportunistically in foreign and domestic companies without any constraints regarding capitalization or style.*

A complete list of firm composites and performance results is available upon request. Returns represent past performance and are not indicative of future results. Investment may result in the loss of principal.

*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. Currently the index consisted of 46 countries (22 developed and 24emerging countries). The **MSCI All Country World Index** measures the equity market performance of world's developed and emerging markets including the U.S. Currently the index consisted of 47 countries (23 developed and 24emerging countries). A net total return index reinvests dividends after the deduction of withholding taxes, using a tax rate applicable to non-resident institutional investors who do not benefit from double taxation treats. These indices do not reflect fees and expenses associated with the active management of separate account portfolios.*

Investment Strategy

Large Cap Value

High Pointe's Large Cap Value strategy generated a return of 3.1%, matching its benchmark, the Russell 1000 Value Index during the quarter. The portfolio benefitted from strong security selection in the Healthcare and Technology sectors, but that was offset by weak stock selection in the Consumer Discretionary and Industrials sectors.

In the Healthcare sector, our investment in the Managed Healthcare industry performed well because of a smart acquisition that brings opportunities for both revenue growth and margin expansion. In the Technology sector, our hardware holding benefitted from strong execution and higher than expected growth. On the other hand, our investment in the Airlines industry suffered as price competition increased. In the Consumer Discretionary sector, our Housewares investment struggled with input cost increases caused by hurricane Harvey.

During the quarter, we repositioned our investments out of Mortgage REITs and into Property and Casualty Insurance.

Large Cap Growth

High Pointe's Large Cap Growth strategy produced a return of 3.8% for the quarter, lagging its benchmark, the Russell 1000 Growth Index, by 2.1%. Security selection was weak in the Healthcare and Consumer Discretionary sectors, but was partially offset by strong stock selection in the Consumer Staples sector.

In the Consumer Discretionary sector, our investment in the Restaurant industry suffered as its growth moderated and the amount of traffic flattened. In addition, our Internet Retail holding lowered growth forecasts. On the other hand, our investment in social media continued its excellent record of strong earnings and execution.

During the quarter, we increased our investment in the Technology sector and reduced our investment in the Consumer Discretionary sector.

International Equity

High Pointe's International Equity strategy produced a return of 4.1%, trailing its benchmark, the MSCI All Country World ex-US Index, by 2.1%. Stock selection was strong in the Healthcare sector, but was more than offset by weak security selection in the Materials and Technology sectors.

In the Materials sector, our investment in mining struggled as a Latin American court temporarily halted its license. The license was later reinstated but after further review, given the higher than anticipated risk, we decided to divest our position. Our investment in the United Kingdom Household Product industry suffered as sales weakened. On the positive side, our European insurance holding executed well as its Asset Management segment generated impressive performance and consistent asset inflows.

During the quarter, we increased our investments in the Consumer Discretionary sector and decreased our investments in the Financials and Materials sectors. We also reallocated our investments out of Japan and North America and into Europe.

Global Opportunity

High Pointe's Global Opportunity strategy generated a return of 5.3% during the quarter, outperforming its benchmark, the MSCI All Country World Index, by 0.1%. In North America, our investment in Data Processing continued its record of strong execution with new product offerings. In addition, our investment in emerging market Internet Services performed well as it demonstrated exceptional growth in online games and advertising. On the other hand, our investment in the North American Restaurant industry struggled as growth moderated.

During the quarter, we increased our investments in the Technology and Materials sectors and decreased our investments in the Healthcare sector. We also repositioned our holdings out of Japan and into North America and emerging markets. Specifically, we reduced our banking investments in Japan and reinvested the proceeds in emerging markets. We also sold an emerging market Casino investment in favor of North American Restaurants and Construction industry investments.

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We thank you for your continued trust in High Pointe and the opportunity to manage your assets. Please call either Gautam Dhingra or Chris Olson with any questions.