



NorthPointe Capital, LLC
Small Cap Value
3rd Quarter 2016

General Market Commentary for the Third Quarter of 2016

The broader market indices recovered from the volatility at the end of the previous quarter and spent most of the third quarter gradually climbing higher. That calm disappeared in early September as investors became concerned, once again, about the prospect of an interest rate increase by the Federal Reserve. However, in the final weeks of the quarter, the indices moved higher, essentially returning to the levels of early September.

Small cap stocks dramatically outperformed large caps as the Russell 2000[®] Index recorded a quarterly gain of 9.05%, more than doubling the 4.03% increase of the Russell 1000[®] Index. Value and growth stocks had similar returns, with the Russell 2000[®] Growth Index return of 9.22% narrowly beating the 8.87% gain in the Russell 2000[®] Value Index. Value stocks underperformed due less exposure to the strong performing Information Technology and Health Care sectors.

As you will read in the detail below, the portfolio had several highlights and a few lowlights during the quarter. Approximately 80% of the stocks in the portfolio advanced in the 90 day period ended September 30, 2016. And accordingly, approximately 20% declined. In most, if not all of these instances, the stock movements were a result of Company specific news or actions. They were not related to interest rate speculation, Brexit uncertainty, or the upcoming political elections. Our investments move on fundamentals. The portfolio's performance will be based upon these fundamentals. We continue to focus our efforts on interpreting the fundamentals rather than macro issues. We believe this approach is the best way to deliver attractive investment results.

Portfolio Commentary

For the quarter ending September 30, 2016, the portfolio outperformed the benchmark, the Russell 2000[®] Value Index. The portfolio benefited from having no exposure to the Utilities sector, which had the worst sector-wide return during the quarter. Additionally, strong stock selection scores were derived from the Industrials and Information Technology sectors. Within Industrials, the stock of Swift Transportation Company was the best performer of the sector as the trucking company continued to post respectable results (i.e., profitable and increasing margins) despite the soft freight environment. The stock of Information Technology holding



NeoPhotonics Corporation performed well as the Company is seeing strong demand for its communication products as China upgrades its wireless infrastructure.

A high level review of the attribution indicates that the Health Care sector was a modest positive contributor during the third quarter. However, a closer look at specific stocks is necessary to truly identify the major events that recently took place. The portfolio has long been invested in two drug companies and each of them was due to provide an update on their development progress during the third quarter. Aerie Pharmaceuticals, Inc. reported very impressive results for its glaucoma drug and the stock responded by more than doubling during the quarter. This was the best performing stock within the portfolio. Another top performer for the fund was the investment in Genmark Diagnostics, Inc., whose molecular diagnostic platform is being well received in Europe and investors look forward to a successful product launch in the United States. At the opposite end, was vaccine developer Novavax, Inc. who reported surprisingly poor results in its late stage vaccine to protect against a respiratory virus. The subsequent decline in the stock of Novavax unfortunately eliminated the benefit obtain from both Aerie and Genmark. Stepping outside the current quarter and reviewing the totality of both investments in Aerie and Novavax indicates the portfolio has benefited from timely sales and purchases of each stock. While the hit from Novavax took the quarter from “Great” to “OK”, on a combined basis, the investments in both Aerie and Novavax have done well for our investors. We still believe there is upside in both companies and we continue to have investments in each.

Performance was also negatively impacted by the declines in the stocks of Olin Corporation and Super Micro Computer, Inc. Olin, a chemical manufacturer, has been challenged by the integration of a large acquisition and low demand for its core products. Super Micro Computer, a manufacturer of enterprise computer infrastructure systems, saw lower demand from large international clients and lowered revenue guidance as a result. We believe that the installation of an internal computer system will enable the company to better respond to competition and therefore, we maintain our investment in Smith Micro.

Research Efforts

In our last quarterly update, we wrote:

“In the final days of the quarter, the stock market experienced elevated volatility. This trend may continue for some time due to uncertainty in the global macro environment.”

The volatility continued during the first few days of the most recent quarter. As we have previously emphasized, we strive to maintain a disciplined view of each investment, understanding why we own the stock without being influenced by the day to day change in the



stock price. As such, our research efforts remain the same. Our investment process remains the same.

Sector or Industry Shifts

The portfolio's investments in the Health Care sector remained the largest overweight exposure relative to the Russell 2000[®] Value Index. The portfolio also maintained a notable overweight position within the Materials sector throughout the quarter. On August 31, 2016, a new sector, Real Estate, was created within the Global Industry Classification Standards. Stocks within this sector were previously classified as Financials. As has been the case for several quarters, the portfolio maintained an underweight position to the Financials sector. With the introduction of the new Real Estate sector, the portfolio, not surprisingly, has less exposure to this sector as well. Additionally, the portfolio continues to be underexposed to Utilities. There were no other significant industry shifts.

Past performance is no guarantee of future results. The value of investments may go down as well as up and investors may not get back their original investment. Performance is shown gross of fees and charges. The opinions expressed herein are those of NorthPointe Capital, LLC as of the date of this report and are subject to change at any time. Although the third party information has been obtained from and is based on sources the Firm believes to be reliable, the Firm does not guarantee the accuracy of the information, and it may be incomplete or condensed. This report is for informational purposes only, and is not intended as a recommendation with respect to the purchase or sale of any security. A list of all recommendations made within the last 12-months is available upon request. It should not be assumed that any of the securities transactions or holdings discussed will prove to be profitable, or that investment decisions or recommendations made in the future will be profitable or will equal the performance of the securities discussed herein. The securities discussed do not reflect the entire portfolio and in the aggregate may represent only a small percentage of the portfolio's holdings.

The Russell 2000[®] Growth Index measures the performance of the small-cap growth segment of the U.S. equity universe. It includes those Russell 2000[®] companies with higher price-to-value ratios and higher forecasted growth values. The Russell 2000[®] Index measures the performance of the small-cap segment of the U.S. equity universe. The Russell 2000[®] Index is a subset of the Russell 3000[®] Index representing approximately 10% of the total market capitalization of that index. It includes approximately 2000 of the smallest securities based on a combination of their market cap and current index membership. The Russell 2000[®] Value Index measures the performance of small-cap value segment of the U.S. equity universe. It includes those Russell 2000[®] companies with lower price-to-book ratios and lower forecasted growth values. The Russell 1000 Index measures the performance of the large-cap segment of the U.S. equity universe. It is a subset of the Russell 3000[®] Index and includes approximately 1,000 of the largest securities based on a combination of their market cap and current index membership.