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THE ARETE QUARTERLY

Welcome

Inside This Issue

Welcome	1
Business Update	2
Portfolio Characteristics	3
Transactions Review	4
Market Overview	5
Performance Review	7
Investment Philosophy	9
Arete Mid Cap Core Composite	11

One of the neat things about the investment industry is that there are a lot of smart people who are constantly coming up with new ideas and perspectives. One of the fun things about running Arete is having the freedom to implement or incorporate many of these ideas well before they become more widely accepted.

A good example of a great idea comes from Michael Mauboussin in his new book, *The Success Equation: Untangling Skill and Luck in Business, Sports, and Investing.* In it, he describes the futility of the widely accepted practice of focusing on past performance when evaluating investment managers. His recommendation, in short, is to focus on process, not outcome.

The logic behind this recommendation is powerful. Mauboussin explained to a recent audience for the Baltimore CFA Society, "Outliers exist due to extreme skill and extreme luck combined," and continued, "where there is luck, there is reversion to the mean." In the world of investment products, this means for certain periods the best performing funds can attribute much, and oftentimes all, of that success to luck. Luck, by definition, is not persistent (it is random) and therefore it is not predictive. As a result, performance makes a poor basis for evaluation.

The characteristic that is persistent and therefore can provide predictive value is investment *process*. This involves the regularity and repeatability of actions made to identify and purchase securities that are mispriced by the market. One of the best single indicators of robust process is active share. High active share (see *Arete Insights* Q4 11) indicates a high degree of conviction in holdings and is a uniquely effective way for a manager to leverage investment insights enough to overcome management costs and still outperform relevant benchmarks.

So the choice for investors evaluating managers really comes down to relying on the easily available performance numbers that have no useful predictive value, or to doing a little extra work and evaluating processes which do. Arete Mid Cap Core's active share is greater than 90% which demonstrates clearly how truly distinct it is from the benchmark.

For investors who do decide to analyze active share, they will also find information content in the degree of transparency. Many firms don't want you to know how much you are paying for a fund so similar to its benchmark. If it is hard or impossible to get active share information, you can safely assume the answers are not good.

Given the challenging landscape for investors and fiduciaries alike, it will become increasingly important to work with investment managers with strong processes and high incentives to serve their clients' best interest. If you are looking for help now or are simply planning for the future, we would appreciate you keeping Arete in mind.

Business Update

A fascinating and rapidly developing trend is the vastly improving access to information. Despite technological advances breaking down many obstacles to access, there remain formidable barriers to the types of advice and information that actually make investors better off. There are some clear reasons why this happens: Conflicts of interest, organizational incentives, and industry structure can all serve as barriers to the efficient conversion of information and expertise into investor benefit.

This issue strikes close to home for me because every day I spend hours reading and analyzing research and news stories and have the overflowing files and bookshelves to prove it. This is the kind of work that most people simply don't have the time to do, the interest to pursue so aggressively, nor the expertise to fully absorb and exploit. It enables me to cut through much of the noise, to quickly differentiate the garbage from the useful, and to determine fruitful courses of action.

Certainly the result of much of this work goes into managing the Arete Mid Cap Core service. Unfortunately, for Arete, and I believe for many investors as well, much of this work and the expertise behind it goes largely unseen and unused.

Part of the challenge for Arete is an industry-wide issue. The issue is that investment expertise has been compartmentalized into relatively narrow silos. There are investment managers that research securities like stocks, there are consultants that apply asset risk and return studies, and there are a wide variety of advisors who apply sound financial practices to individual client situations.

These narrowly defined functional categories worked reasonably well during a period of economic calm, strongly appreciating markets, and little scrutiny on fees. In more difficult and uncertain times, however, this structure imposes an unwieldy layer of fees and perhaps even worse; it fragments investment expertise at a time when understanding the big picture is the most important.

Some of the larger and more successful hedge funds have been challenging the traditional fragmentation of industry expertise. Many have fused the management and allocation functions by combining multiple asset classes into flagship funds for some time.

That trend seems to be moving a step further now as recently reported in the September 17, 2012 issue of *Pensions&Investments.* The article, "Institutional investors turn to hedge fund managers for strategy, macro advice" noted that "Institutional investors desperately want knowledge transfer for the purpose of improving the asset allocation and returns of their whole portfolio." The thrust of the article was that there is a lot of investment expertise

[here referring specifically to hedge funds] that can help investors to solve problems.

I see this as a smart and healthy development and one that should be happening faster outside of the hedge fund community. While there is no doubt a great deal of talent in some hedge funds, there is also little doubt that part of this trend reflects an ulterior motive: The desire to retain very high fee structures.

I do believe this trend sheds light on an opportunity for me and Arete. I mentioned last quarter that I was experimenting with a knowledge database and I can happily announce that the AreteResearch site is up and running. Personally, I have found it to be a very useful way of assimilating and reviewing my own research. I hope it can also provide perspective and insights for other investors. I am still gathering feedback on it with the hope of commercializing it this year. If you are interested in gaining access, please let me know at drobertson@areteam.com.

Finally, this letter will be distributed on the fifth anniversary of the founding of Arete. I would like to take this opportunity to thank all of the investors in Arete for their support over the years. I say this because I mean it: It has been an honor to serve you. I would also like to thank Arete's many advocates who stay in touch, provide feedback, share ideas, and keep Arete in mind when they are looking for investment expertise. I really appreciate it and look forward to continuing to build on Arete's successes.

Thanks and take care!

David Robertson, CFA
CEO, Portfolio Manager

Portfolio Characteristics – Arete Mid Cap Core

A key proposition for Arete's Mid Cap Core strategy is that it is a truly representative mid cap portfolio. In general, this suggests that over time, you can expect to see the aggregate characteristics and sector exposures of the strategy migrate to those of the Russell Midcap Index®. During intervening periods, however, sector exposures and other characteristics will reflect the opportunities we find in the market at that point in time.

Portfolio Characteristics (12/31/12)

	Arete MCC*	Midcap Index**
Size		
Average Market Cap ($ mil.)	6,626	5,896
Median Market Cap ($ mil.)	4,499	4,294
Minimum Market Cap ($ mil.)	80	317
Maximum Market Cap ($ mil.)	25,406	21,357
Number of holdings	37	797
Valuation		
P/E current year	18.0	18.9
P/E forecast Y1	21.0	18.2
P/B	2.0	3.1
P/S	0.8	1.5
Yield (%)	1.5	2.6
Valuation drivers		
ROE (%)***	11.6	15.1
LT eps growth forecast (%)	10.6	12.0

Source: The Applied Finance Group™
**Note:* Excludes positions which are less than 0.1% weights.
***Note*: Arete currently does not subscribe to the Russell Indexes and therefore the statistics presented here represent approximations of the Russell Midcap® Index.

We believe maintaining a truly representative mid cap portfolio is important for two reasons. First, a truly mid cap portfolio faithfully plays its role in

a broader asset allocation scheme. Second, it allows for accurate assessment of performance. Without an appropriate benchmark it is difficult, if not impossible, to judge whether performance differentials are due to skill or luck, and are sustainable or transient.

For example, many fund managers attempt to beat their benchmark by timing the market and/or migrating style. These tactics rarely generate sustainble out-performance. To us, such activities usually just serve to obfuscate the underlying inability of the manager to add value through a coherent and disciplined investment process.

Sector exposure (percent of assets on 12/31/12)

Economic sector	Arete MCC*	Midcap Index**	Percentage Comparison
Consumer Discretionary	11.1	17.4	63.7%
Consumer Staples	3.2	6.1	52.8%
Energy	5.2	7.3	71.1%
Financial Services	12.2	21.4	57.0%
Health Care	8.5	9.5	89.2%
Materials & Processing	6.5	6.9	93.9%
Producer Durables	9.4	12.6	74.8%
Technology	7.1	11.8	60.2%
Utilities	4.4	7.0	62.9%
Equity exposure	67.6	100.0	
Cash and equivalent	32.4	0.0	

Source: The Applied Finance Group™
**Note*: Arete Mid Cap Core is represented by the aggregate of all assets in the composite at the given date.
***Note*: Arete currently does not subscribe to the Russell Indexes and therefore the sector weights presented here represent approximations of the Russell Midcap® Index.

Portfolio characteristics for the quarter continue to confirm that the equity portion of AMCC is a very representative mid cap portfolio. Market caps for AMCC are extremely similar to the mid cap index and with the clear exception of yield, AMCC is cheaper. ROE is noticeably lower, but is subject to many distortions and has not been especially reliable.

Sector exposures were all below benchmarket weights due to the high cash position, but still within our general guidelines of 50% - 150% of benchmark weights. Two sectors are currently very close to guideline minimums including Consumer Staples and Financial Services. While we always target best ideas in our research process, we will also be sensitive to these underweights as we deploy cash in upcoming quarters.

Transactions review – Arete Mid Cap Core

There were no major transactions in the quarter, but there was, again, a minor one. Again, this one involved Sears Holdings which spun off Sears Canada in November. The position size is extremely small, but the stock does qualify as a mid cap and is reasonably attractive so we will retain the position in client accounts until conditions change.

It is worth noting that although we did not initiate any new transactions in the quarter, we continue to identify new opportunities and research our “bullpen” names. The most common obstacle to new purchases has been price. While it has been frustrating to see so little reward for our research and valuation work the last three years, we continue to believe that exercising discipline regarding prices paid will ultimately reduce risk and improve long-term returns for our investors.

Market Overview

Market returns for 2012 were far better than we ever expected in light of still-significant underlying risks. As a result, we believe the investment landscape continues to merit caution. The risks have been exemplified by the "fiscal cliff" debate which we have all heard too much about. Nonetheless, we believe the "fiscal cliff" debate provides a useful opportunity to frame what is really going on.

We have mentioned this several times in the past, but it always bears keeping in mind: The huge problem we are facing, and will continue to face, is massive global deleveraging. This is the big picture. This is the single most important factor in the investment landscape and will be for years.

The ultimate result of such significant deleveraging is that much of the debt simply will not get paid back. This will create some irreversible holes in balance sheets and will wipe out a fair amount of equity. One way or another, what it means for investors is that we have less than we think we do.

In its raw form, this is an extremely unpalatable and politically incorrect, though still inevitable, consequence. As a result, it suggests two challenges for politicians. First, the electorate must be diverted from close scrutiny of the main problem by creating dramatic and entertaining distractions. The fiscal cliff debate was a good example. There will be plenty more to come.

Second, any serious effort on tackling the main problem must be done in small, digestible, chunks and slowly enough such that anger over the situation can diffuse rather than foment. This is akin to boiling a frog. Increase the heat gently enough and he'll never know.

Another manifestation of this playbook has been occurring with unemployment. The visibility of this particular statistic was increased when the Fed specifically linked further policy action to it in December.

The reported number for unemployment, the one that people read in papers and hear on the news, was 7.8%. It is still a little higher than the 7.3% reported in December 2008, but it is down from its peak of 10.0%.

Superficially it sounds decent and gives the impression progress is being made. This holds true only until you dig just a little deeper. As it turns out, the number that really matters to the economy (and to us individually!) is the number of jobs. That number was 143.305 million in December 2012 and 143.369 million in December 2008. In other words, the number of people working is almost exactly the same. No new jobs over four years.

Further, the number of people unemployed has actually increased from 11.286 million to 12.206 million. This brief analysis reveals that the labor market has gone nowhere and that the only reason the unemployment rate is anywhere close to where it is today is because a lot of people are no longer even looking for jobs because they have become discouraged by their meager prospects.

In order to truly appreciate the impact of the employment condition (on the economy and on individuals), however, it helps to know that the average number of people on

food stamps increased from 28.2 million in 2008 to an average of 46.6 million in 2012. Given the much uglier reality, it is quite clear why government authorities have focused attention on headline unemployment instead.

The extremely important lesson in all of this is that it is imperative that investors be fully aware of these efforts at misdirection and misinformation. Those who aren't aware of the misinformation, or can't see the big picture, or don't act on the core trends will be the suckers at the poker table as wealth gets reallocated.

To better appreciate the challenge, it is important to understand that with the prospects for slower economic growth and the burden of too much debt, the nature of competition within society fundamentally changes. When things are growing nicely, everyone's share of the pie increases. A rising tide lifts all boats.

When growth slows or stops, the only way to get ahead is to take shares of pie from others. The end result is that competition gets nastier. Those who are too busy or too oblivious, or who quietly acquiesce, will lose out in this competition. Being passive is likely to carry increasing risks.

With this broad overview of the market and the political environment, we can now try to make sense out of the Fed's actions and what it implies for investors. For starters, it is quite clear that the Fed is "all-in". This means it is going to do whatever it can to fight deflation which means it is also expressly trying to increase the price of risk assets. With such a formidable player as the Fed pushing for higher asset prices, why would anyone want to resist?

While we certainly do not predict an imminent collapse in asset prices, we do believe the market is fragile and therefore vulnerable to unexpected shocks. As a result, we have a much more nuanced and measured view towards investment opportunities.

We substantiate our caution by highlighting an example from very recent history. We just need to go back to the mid-2000s to see that that the Fed completely missed the housing bubble and as a result, completely failed to take any action to prevent significant losses. Arguably, monetary policy was kept too loose for too long which facilitated the inflation of the bubble.

This policy error was exceptionally costly to many people because for most, their home is their biggest asset. This assessment is not meant to be exceptionally critical of the Fed, but is merely intended to emphasize the evidence that the Fed is neither omniscient nor omnipotent. Further, when mistakes are made, it is investors who are left holding the bag and therefore it is investors who bear the burden of managing the risks implicit in such policies.

The limits of knowledge have also been explicitly voiced by the Fed's own Jeffrey Lacker, president of the Federal Reserve Bank of Richmond. He admits, "We're at the limits of our understanding of how monetary policy affects the economy." As a result, while we have greater clarity regarding the *intentions* of the Fed, we have less clarity regarding the ultimate *impact* of such extraordinary and experimental monetary policy.

The immediate and substantial problem that central banks have addressed is financial system liquidity. As a result, we don't need to worry too much about a 2008-type financial crisis repeating soon. U.S. banks are in far better shape and some of the key risks of the private sector are now being assumed by the public sector.

Herein lies the rub. While there is less risk of a Lehman Brothers-type private sector crisis, there is increasing risk of a public sector crisis. As such, we judge that there is still a very high, and arguably growing, amount of systemic risk in the markets.

Risk itself is not a bad thing, and in fact, it is what investors get paid to accept. What they get paid is increasingly our concern. While we cannot predict the path of the economy, we do know that the economic cycle will turn down at some time and that the current expansion is already longer than usual. We also know that despite this, major market indexes are reaching five year highs. When the economy does turn down, there will be little left for the Fed to do to ease the pain. As a result, our analysis shows that investors are getting paid very little right now to take on ever-greater risks.

The Fed's "all-in" strategy may work, but we take our duty as fiduciaries very seriously and we cannot justify betting the ranch on risk assets amid current conditions. Not only would we deem such action imprudent, but in doing so, we would also forsake our responsibility to allocate capital responsibly and in a disciplined way. At the end of the day, that is what we are hired to do.

It is too bad current market valuations are so stretched because our longer-term outlook for stocks is still positive. We still absolutely believe in the fundamental ability of U.S. companies to adapt and innovate and grow. We also know that after thirty years of declining interest rates and with the distinct prospect of future inflation, bonds are likely to be horrible investments over the next three decades. Finally, in a low return environment with a wide range of potential outcomes, there will be a significant premium for effective active management to hunt down attractive investments at good prices.

We're not the only ones who think this way. Warren Buffett has said as much and two premier bond firms, PIMCO and DoubleLine, have both indicated significant moves into equities recently.

During the interim, however, we will continue doing our primary job of allocating assets thoughtfully and prudently on behalf of our investors. We will continue watching for evidence that the market mechanism is functioning better. As we find exceptionally attractive individual stocks and windows of opportunity, we will have a lot of dry powder to put to work.

Performance review – Arete Mid Cap Core

The Arete Mid Cap Core product is designed with the flexibility to invest in the most attractive mid cap stocks, regardless of any particular "style" designation. With that context, the primary criterion for selecting a stock in the Mid Cap Core strategy is that market value is significantly less than our estimate of intrinsic value. In other words, we try to find situations in which our

research generates expectations for a company's growth and profitability that justify substantially greater valuations than what the market discounts.

Our investment process is designed to discover, analyze, and assemble stocks into a diversified portfolio that consistently outperforms its benchmark over time. Specifically, our investment objective is to outperform the benchmark Russell Midcap® Index by 200-400 basis points per year, net of fees, over the course of a market cycle.

Our target of 200-400 basis points of outperformance is based upon our experience with the strategy and upon our judgment of value creation. The primary metric we use to judge value creation is the information ratio. The information ratio compares a portfolio's excess return to its risk as measured by tracking error. Our goal is to outperform by a large enough margin relative to risk to clearly merit the cost in time and resources to evaluate investing with us.

Arete's Mid Cap Core (AMCC) strategy returned 3.69% (net of fees) for the quarter versus 2.88% for the Russell Midcap Index® (RMC) (see pages 10 – 12 for performance and related disclosures). This was the strongest quarter of outperformance in some time and occurred despite the drag of the large cash position in an up market.

Four of the top performers, Genworth, Dex One, Peabody Energy, and St. Joe Company, have been heavily shorted in the past and began getting squeezed in the fourth quarter. While we obviously still believe in these companies and expect further gains over times, it was instructive to see how much their prices have been affected by short-term trading activity. CarMax was also a top performer and did it the old-fashioned way -- by performing strongly with an increasingly valuable business mode.

Stock performance* (9/30/12 -12/31/12)

Best performers

Company	Return in quarter (%)
Genworth	43.6
CarMax	32.7
Dex One Corp	26.4
Peabody Energy	19.4
St. Joe Company	18.4

Worst performers

Company	Return in quarter (%)
Sears Holdings	-25.5
Spirit Aerosystems	-23.6
Annaly Capital	-16.6
Exelon Corp	-16.4
NII Holdings	-8.9

**Note*: Performance includes price changes only; it does not include dividend income in the quarter.

Sears topped the list of underperformers although it is hard to attribute any good reasons. We continue to believe Sears is misunderstood by the market which puts far too much emphasis on short-term operating metrics and far too little emphasis on underlying asset value. Spirit Aerosystems reported a very significant writedown on several contracts which unfortunately revealed exceptionally poor management. The stock is cheap, but it is clear is has far less upside given a realistic assessment of its cost structure.

Annaly sold off in the quarter as some investors became concerned that continued Fed purchases of mortgage backed securities would impair business prospects going forward. There is some truth to this,

but Annaly management is very competent and they have been reducing leverage in order to reduce risk. At more than a 10% discount to asset value, the sell-off was clearly overdone. Exelon has been a victim of falling energy prices which may threaten its dividend and NII Holdings has experienced significant challenges in its transition to 3G services in Brazil. The common thread among all of these is that despite the market as a whole being calm on the surface, violent reactions to bad company-specific news reveal a more troubling underlying reality.

On a separate note, the Arete Mid Cap Core Composite (AMCC) now has four full calendar years of performance and has averaged a return of 15.4% per year over that period of time. While AMCC returned less than that of the Russell Mid-cap Index, it did beat the S&P 500 (total return) as well as the Russell top 200 (an index of the largest stocks). A big part of the reason for this is that, as we have preached many times, mid caps as a group are more attractive than their larger bretheren. On that count we have been completely right and continue to encourage investors consider an explicit allocation to mid caps.

We also consider AMCC performance in the context of an environment that has been fairly hostile to active investing and valuation-based strategies (as compared to passive strategies) for three of the last four years. We don't see anything wrong with Arete's process or competitive advantages. In fact, Arete has outperformed many "alternative" products with similar processes due in part to materially lower costs. While policy actions have deferred the value of active management for some time, we feel as strongly as ever about Arete's ability to generate superior returns.

Investment Philosophy

We firmly believe in the critical importance of a cogent investment philosophy for any investment operation. In order to emphasize this point, and to assist you in understanding how we work, we provide an abbreviated version of our investment philosophy here. The text of our investment philosophy is also provided, in its entirety, in our Form ADV, Part II which is available upon request at any time.

Performance derives from exploiting mispriced securities.

The key to investment performance is finding and exploiting market inefficiencies in the form of mispriced securities. There are two components to this. One component involves determining the fair price of securities in the form of underlying intrinsic value, which we do primarily through calculating discounted cash flows.

The second component of exploiting mispriced securities is establishing a clear understanding as to the various mechanisms at work that allow mispricing to occur. By understanding the mechanisms and motivations of the marginal buyer and seller, we believe we can more accurately estimate the probabilities and expected values of investment opportunities.

Nobody has perfect information.

Competitive pressure and technological development have conspired over the years to make most data and analysis commodities which no longer provide a meaningful competitive advantage. What can provide an advantage, however, is *how*

that information is used and *how* it gets interpreted in making investment decisions.

In order to convert the raw material of information into the useful output of a good investment decision, it is necessary to assimilate and synthesize the information into some meaningful form. We believe the most effective way to accomplish this is to thoughtfully deploy resources available according to the nature of the research tasks at hand.

Research culture and research prioritization are also important in relation to analyzing and synthesizing information. We believe that the best way to leverage the collective knowledge and experience of a research team is to encourage active and open dialogue designed to explore multiple perspectives and to challenge individual assumptions, biases, and beliefs. Only by enduring such scrutiny do the best ideas rise to the top. Further, in order to fully leverage these ideas, we believe research efforts must be dynamic and flexible in allocating resources such that ideas receive attention in proportion to the expected benefit to the portfolio.

Execution is crucial for investment success.

In order to create value, an investment strategy needs to be implemented continuously and comprehensively. Actions speak louder than words. We believe the most effective efforts focus on a few simple, but key concepts that work to ensure proper execution of a firm's investment strategy.

The first key to execution is structural in nature and involves a firm's independence. By maintaining independent ownership, an investment firm eliminates agency effects which can present a conflict of interest between clients and certain of its ownership groups. Independent ownership ensures that client and manager interests are optimally aligned.

The second key to execution is temperament. The best investors tend to have a temperament that provides them the courage and initiative to act, often going against the grain, when opportunities arise. However, the same temperament provides balance such that decision-making is not simply a risk-taking activity, but a very conscious and targeted effort to engage in propositions with high risk-adjusted expected returns.

Finally, another important element of execution is simply doing what you say you do in your investment process. Too often, perfectly acceptable investment processes fail when actual investment activities bear little resemblance to the process described in the marketing presentation. We call this the “marketing gap;” the difference between what is said and what is done. Execution is optimized when the marketing gap is minimized.

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Arete Mid Cap Core Composite

Arete Asset Management, LLC
Mid Cap Core Composite
July 31, 2008 - December 31, 2012

Period	Gross-of-Fees Return (percent)	Net-of-Fees Return (percent)	Russell Midcap® Index Return (percent)	Number of Portfolios**	Internal Dispersion (percent)	Total Composite Assets ($)**	Composite Assets With Bundled Fees ($)	Percentage of Composite Assets With Bundled Fees	Total Firm Assets ($)
2008*	-37.97	-38.16	-35.01	3	NA	207,031	207,031	100%	207,031
2009	48.63	47.83	40.48	3	NA	471,867	471,867	100%	673,806
2010	16.86	15.78	25.48	3	NA	546,315	546,315	100%	877,368
2011	-8.20	-8.88	-1.55	3	NA	497,767	797,767	100%	897,918
2012									
January	5.55	5.09	6.06	3	NA	523,081	523,081	100%	936,465
February	4.32	4.32	4.15	3	NA	545,671	545,671	100%	970,094
March	0.50	0.50	2.24	3	NA	548,446	548,446	100%	973,638
April	-1.67	-1.67	-0.33	4	NA	760,009	760,009	100%	958,759
May	-5.31	-5.54	-6.71	4	NA	717,926	717,926	100%	913,063
June	2.31	2.31	2.81	4	NA	734,538	734,538	100%	930,858
July	0.08	-0.18	0.23	4	NA	733,237	733,237	100%	929,838
August	3.16	3.16	3.15	4	NA	756,435	756,435	100%	955,123
September	1.84	1.84	2.12	4	NA	770,744	770,744	100%	970,296
October	0.78	0.54	-1.01	4	NA	774,477	774,477	100%	873,365
November	0.26	0.26	1.64	4	NA	776,459	776,459	100%	874,922
December	2.87	2.87	2.25	4	NA	798,766	798,766	100%	897,341
Q1	10.65	10.17	12.94	3	NA	548,446	548,446	100%	973,638
Q2	-4.74	-4.97	-4.40	4	NA	734,538	734,538	100%	930,858
Q3	5.14	4.87	5.59	4	NA	770,774	770,774	100%	970,296
Q4	3.95	3.69	2.88	4	NA	798,766	798,766	100%	897,341
YTD	15.20	13.84	17.28	4	NA	798,766	798,766	100%	897,341

**Note*: Peformance through 12/31/08 is from inception of composite on 7/31/08.
***Note*: One new account contributed additional funds which were not at least 90% invested by the end of the quarter.
Per our rules for inclusion, this account was excluded from the composite and will be added once the funds are fully invested.

Arete Asset Management Mid Cap Core performance composite disclosures follow:

Compliance statement

Arete Asset Management has prepared and presented this report in compliance with the Global Investment Performance Standards (GIPS®).

Arete Asset Management Mid Cap Core performance composite disclosures continued:

Definition of the firm

Arete Asset Management, LLC (Arete) was established in 2008 and is registered as an investment adviser in the state of Maryland. Arete is defined as an independent investment management firm and is not affiliated with any parent organization. Arete currently manages one strategy, the U.S. equity mid cap core strategy, which it markets to individual and institutional clients.

Benchmark

The benchmark is the Russell Midcap® Index and its performance is reported in U.S. dollars.

Calculation methodology

Portfolio valuations are calculated as of calendar month-end and are computed in U.S. dollars and performance is also reported in U.S. dollars. Time-weighted rates of return are used which adjust for external cash flows. Our smaller, retail accounts contain fee structures in which one flat, per-transaction fee is charged for trading expenses and which embeds an implicit charge for custody. Since trading and custody charges cannot be directly segregated in these cases, they constitute "bundled fees". Gross-of-fees performance returns are presented before management and custodial fees when custodial fees can be segregated from trading, but are presented before management fees and after bundled (trading and custodial) expenses for our retail accounts. Net-of-fees returns are presented after management fees, trading expenses, and custodial expenses are deducted or after management fees and bundled (trading and custodial) fees for retail accounts. There are no instances in which management fees are bundled with trading or custodial fees. Returns are presented net of nonreclaimable withholding taxes when applicable. Arete does not use leverage or derivatives in the management of portfolios. Additional information regarding policies for calculating and reporting returns is available upon request.

The composite

This U.S. Equity Mid Cap Core composite was created in August, 2008 and includes all fee-paying, taxable and non-taxable, discretionary, long only, fully invested portfolios benchmarked to the Russell Midcap Index. Every new portfolio is added to the composite in the first complete calendar month that it is "fully invested". For purposes of composite construction, a portfolio is "fully invested" if its equity composition is greater than 90% of the equity composition of the composite. Each portfolio will remain in the composite until its equity composition becomes less than 90% of that of the composite. A complete list and description of firm composites is available upon request.

*As of March 31, 2012, the composite has been redefined in order to clarify policy in light of unusually high cash positions recently. Prior to March 31, 2012, a portfolio was considered to be "fully invested" if greater than 90% of portfolio assets were invested in equity securities which implicitly assumed a nearly 100% equity position in the composite.

Arete Asset Management Mid Cap Core performance composite disclosures continued:

Fee schedule
The management fee schedule is as follows: 1% of AUM up to $1 million, 0.75% on AUM greater than $1 million, but less than $5 million, and 0.65% on assets greater than $5 million.

Minimum account size
There is no minimum account size for inclusion in the composite. Please note, however, the minimum initial account size accepted is $100,000.

Dispersion
Internal dispersion is currently not meaningful as there are five or fewer portfolios included in the composite. In the future, we plan to calculate dispersion using the dollar-weighted standard deviation of all portfolios included in the composite for each performance period.

Verification
Arete has not been verified by an independent verifier for its compliance with GIPS.