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THE ARETÉ QUARTERLY

Welcome

The investment landscape is changing and so are the needs of investors — and Areté is here to help however we can. While we do actively manage stocks in our mid cap core strategy, we have also introduced a Personal CIO Service [here] in order to help investors who want access to our expertise on a more modular basis. In these services and any future ones, Areté will always focus on conducting good research, independent thinking, and putting our clients' interests first.

In order to stay apprised of our latest thinking on the investment landscape, please take a look at our blog [here]. Finally, please always feel free to contact us with questions or comments.

Business Update

I have mentioned many times how excessively easy monetary policy has caused problems for investors. Such policies have artificially inflated asset prices and distorted price signals. In doing so, they have made it a lot harder to invest wisely, they have increased the risks associated with investing, and have deprived many investors of a fair opportunity to benefit from capital markets.

Those loose monetary policies have also had an enormous effect on the providers of investment services. Since 2009 pretty much only one thing worked - long exposure to risk assets. The only real way to get ahead was to do even more of it with leverage of some sort. In other words, the most successful strategies were ones that were stupefyingly simplistic.

Inside This Issue

The landscape had a crushing effect on market diversity. One commentator captured the dynamic especially well [here]: "The environment [of quantitative easing] causes some strategies to flourish and multiply, while others die off. The abnormally long, QE-fueled bull market killed off anything that wasn't, at its core, a short volatility strategy. Now, whether it's risky credit, levered equities, or risk parity, almost all strategies are taking similar risks."

This has a number of important implications. One is that there is an enormous risk of an unwind of such exposures. As they stop working, in either gradual or sudden fashion, money will flow out. As it does, securities will have to be sold for whatever price can be had. Another implication is that there are exceptionally few investors to take the other side of that trade. That means there is a big risk that prices will have to fall quite a bit to pique the interest of fundamental and valuation based investors.

Indeed, I think the next few quarters will be a defining moment for the business of investment services. There are exceptionally few who are remaining that have the capacity, in the forms of liquidity, fortitude, and business model, to take advantage of the discontinuities as they arise.

In this respect, I am feeling as good about Areté's prospects as I have in a long time. The mid cap strategy recorded its best relative performance (to the Russell midcap index) ever in the fourth quarter and it did so by doing what exceptionally few money managers have been able to do: something different. Holding a lot of cash is the one thing that worked and most managers just couldn't do in their quest to grow assets.

Looking ahead, I expect this dynamic to continue for some period of time; I think Q4 was only the start. The reason for this is partly because the monoculture and the excesses took years to build up. It will take time for them to thoroughly unwind. During the interim I expect markets to be choppy with lots of dramatic swings in relative performance characterized by big drops and followed by periods of digestion.

I also think there is a good chance that investor behavior will exacerbate and extend the correction. Many investors will be paralyzed by the wild swings. Many will take time to adjust their expectations to a less forgiving environment for stocks. Some will experience challenging markets for the first time in their investing lives. Some won't be able to adjust at all, clinging to the belief that each drop is merely a short term correction.

Ultimately, I think all of this will have a profound and lasting effect on the investment services industry. I thought that should have happened after the financial crisis in 2008-09, but the strong market recovery seemed to pacify any sentiments for change at the time.

The next time around I suspect will be different. One reason will be that continued market choppiness and underperformance by service providers will allow discontent to build over time. As it does, many investors will begin to realize that it is not just the markets that are causing problems but the poor value proposition of their providers. In addition, investors will increasingly be Xers and Millennials who will demand more efficient offerings just like they have in every other sphere of consumer services.

These trends promise to be extremely fruitful for Areté which was built on the premise of providing an excellent value proposition for investors. Thoughtful research, cost-efficient operations, adaptiveness, and clear communication all capped by a mission to help investors get more out of their investing experiences is a package well positioned to resonate with tomorrow's investors.

Finally, I entitled the market review for the fourth quarter "A brand new day" for a couple of reasons that are also applicable to the investment services industry. One is that I think it will be a "brand new day" in a bad way for many investors and providers who cannot adapt to an environment that is not completely driven by increasing liquidity. They will keep trying and keep failing. I wouldn't be surprised if such dynamics rekindle Woody Allen's old joke that "a stockbroker is someone who invests other people's money until it is all gone."

It will also be a brand new day, however, for providers like Areté that are oriented in a completely different way. Driven by investment results rather than asset gathering, we'll be able to manage risk better by only accepting it when there are reasonable prospects of adequate returns. It will also be a brand new day for securities analysis, fundamental research and investment expertise to shine as opposed to thoughtless "risk-on" strategies. Finally, it will be a brand new day because there just isn't very much competition left so we can enjoy the fruits in limited company.

Thanks for your interest and take care!

David Robertson, CFA
CEO, Portfolio Manager

Portfolio Characteristics – Areté Mid Cap Core

A key proposition for Areté'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.

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.

Portfolio Characteristics (12/31/18)

	Arete MCC*	Midcap Index**
Size		
Average Market Cap ($ mil.)	9,928	9,055
Median Market Cap ($ mil.)	6,916	6,955
Minimum Market Cap ($ mil.)	458	207
Maximum Market Cap ($ mil.)***	43,612	85,913
Number of holdings	17	788
Valuation		
P/E current year	19.7	27.2
P/B	2.3	4.6
P/S	1.8	2.3
Yield (%) ****	4.3	3.0
Valuation drivers		
ROE (%)****	9.5	11.8

Source: Calcbench
**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.
****Note*: Stocks with low floats are excluded
*****Note*: The measure of ROE was changed from the average to the median as of 3/31/14.
*****Note:* Average of available yields

For example, many fund managers attempt to beat their benchmark by timing the market and/or migrating style. These tactics rarely generate sustainable 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.

All of that said, our overarching goal is to provide attractive returns to investors on an *absolute* basis. During most times, the stock market provides an attractive vehicle through which to realize those returns. In unique periods of significant overvaluation, however, when our valuation and other analyses suggest attractive returns are less likely, we may allow the cash portion of the portfolio to increase so as to preserve investors' capital and retain the option to buy more cheaply in the future.

Sector exposure (percent of assets on 12/31/18)

Economic sector***	Arete MCC*	Midcap Index**	Percentage Comparison
Consumer Discretionary	0.3	11.9	2.5%
Consumer Staples	0.0	4.4	0.0%
Energy	0.0	4.0	0.0%
Financials	7.6	13.1	58.2%
Health Care	3.8	10.0	37.9%
Industrials	0.0	13.6	0.0%
Information Technology	1.6	18.0	8.9%
Materials	5.0	5.1	97.5%
Real Estate	5.6	9.3	60.2%
Communication	0.0	3.6	0.0%
Utilities	4.5	6.9	65.2%
Equity exposure	28.4	100.0	
Cash and equivalent	71.6	0.0	

Source: Calcbench
**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.
****Note*: Economic sector classifications were changed from Russell to GICS beginning Q414.

General portfolio characteristics for the quarter continue to confirm that the equity portion of AMCC is a representative mid cap portfolio. The average market cap for AMCC is slightly higher than the mid cap index and the median is similar. Although AMCC is much cheaper on the basis of P/S and P/B, it is important to note that valuation metrics have become less informative as the number of holdings has declined to just 17 currently.

Sector exposures are quite different from benchmark weights, in part due to the high cash position but in part due to different exposures. Cash has remained at high but fairly stable levels over the last several quarters.

Active share* (12/31/18)

Period	Percent**
Q418	95.8
Q318	96.2
Q218	96.4
Q118	94.9
Q417	95.0

**Note*: Computed for AMCC composite
***Note*: Active share > 80% is considered "very active"

As a quick reminder, active share highlights the degree to which a portfolio's holdings differ from its benchmark. A portfolio must differ significantly from its benchmark in order to significantly outperform it — and therefore to justify charging active management fees. Areté's Mid Cap Core portfolio consistently exhibits active share well above the 80% level considered to be very active.

Transactions review – Areté Mid Cap Core

Two transactions were made in the quarter. The first one was to exit the position in ITG. Virtu Financial made an offer to acquire the company and the stock quickly rose to within a few percent of the offer. The stock was sold before the deal was complete in order to eliminate any risk that the deal wouldn't go through.

SHLD was sold after it declared bankruptcy in October which virtually eliminated any material upside that could be achieved with the stock. While threats from ecommerce were pervasive, they were also well discounted. A huge factor in the ultimate fate of SHLD, as well as many other retailers, has been the persistent weaknesses in median wage growth and new household formations.

Performance review – Areté Mid Cap Core

Stock performance* (9/30/18 - 12/31/18)

Best performers

Company	Return in quarter (%)
Royal Gold	11.2
NRG Energy	5.9
Detour Gold	4.5
Exelon Corp	3.3
Capitol Federal Financial	0.2

Worst performers

Company	Return in quarter (%)
Weyerhaeuser	-32.3
Seritage Growth Properties	-31.9
Davita	-28.2
Mylan Inc.	-25.1
The Saint Joe Co.	-21.6

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

The Areté 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. 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.

Areté's Mid Cap Core (AMCC) strategy returned -3.10% (net of fees) for the quarter versus -15.37% for the Russell Midcap Index® (RMC) (see pages 8 – 10 for performance and related disclosures). With the rapid onset of turmoil in the quarter, the defensive positioning of AMCC significantly insulated it from the steep losses suffered by the Russell midcap index in the quarter. Despite the downdraft in the quarter, we continue to believe that stocks as a whole are expensive, although individual opportunities are starting to emerge.

Among outperforming stocks the clearest pattern was the performance of gold in the tumultuous markets. Energy stocks also performed reasonably well partly due to supportive natural gas prices and partly due to continued improvement at NRG.

There were also some clear patterns among the underperformers. Stocks related to housing such WY and JOE were hit hard. SRG suffered as a result of the SHLD bankruptcy which will likely have a short term impact on rental revenues. Nonetheless, we are still encouraged by the company's redevelopment opportunities and the much higher rents that come with them.

DVA and MYL also dropped significantly in the quarter although not due to any specific causes. That said, both stocks had been beneficiaries of the extended environment of low rates which helped embellish their growth narratives. Legal and regulatory issues emerged at both companies, however, at the same time rates were pressing higher. These forces combined to significantly dampen credibility and growth prospects got re-rated.

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.

Areté Mid Cap Core Composite

Arete Asset Management, LLC
Mid Cap Core Composite
July 31, 2008 - December 31, 2018

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	15.20	13.84	17.28	4	NA	798,766	798,766	100%	897,341
2013	23.18	22.00	34.76	4	NA	974,605	974,605	100%	1,172,496
2014	4.01	2.99	13.22	4	NA	1,003,729	1,003,729	100%	1,200,564
2015	-7.56	-8.44	-2.44	4	NA	919,035	919,035	100%	1,206,652
2016	4.07	3.02	13.80	4	NA	946,825	946,825	100%	1,142,297
2017	5.03	4.00	18.52	4	NA	984,681	984,681	100%	1,181,490
2018									
January	1.55	1.30	3.76	4	NA	997,473	997,473	100%	1,194,573
February	-1.60	-1.60	-4.13	4	NA	981,536	981,536	100%	1,177,451
March	0.74	0.74	0.06	4	NA	988,813	988,813	100%	1,185,130
April	-0.07	-0.32	-0.15	4	NA	985,649	985,649	100%	1,182,360
May	1.06	1.06	2.27	4	NA	996,142	996,142	100%	1,193,657
June	0.01	0.01	0.69	4	NA	996,192	996,192	100%	1,194,502
July	0.15	-0.10	2.49	4	NA	995,220	995,220	100%	1,193,658
August	0.19	0.19	3.11	4	NA	997,062	997,062	100%	1,195,225
September	-1.18	-1.18	-0.64	4	NA	985,289	985,289	100%	1,182,831
October	-1.90	-2.15	-8.31	4	NA	964,115	964,115	100%	1,160,820
November	1.09	1.09	2.46	4	NA	974,645	974,645	100%	1,171,952
December	-2.04	-2.04	-9.92	4	NA	954,785	954,785	100%	1,152,786
Q1	0.67	0.42	-0.46	4	NA	988,813	988,813	100%	1,185,130
Q2	1.00	0.75	2.82	4	NA	996,192	996,192	100%	1,194,502
Q3	-0.85	-1.09	5.00	4	NA	985,289	985,289	100%	1,182,831
Q4	-2.85	-3.10	-15.37	4	NA	954,785	954,785	100%	1,152,786
YTD	-2.06	-3.03	-9.06	4	NA	954,785	954,785	100%	1,152,786

**Note*: Peformance through 12/31/08 is from inception of composite on 7/31/08.

Areté Asset Management Mid Cap Core performance composite disclosures follow:

Compliance statement

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

Areté Asset Management Mid Cap Core performance composite disclosures continued:

Definition of the firm

Areté Asset Management, LLC (Areté) was established in 2008 and is registered as an investment adviser in the state of Maryland. Areté is defined as an independent investment management firm and is not affiliated with any parent organization. Areté 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. Areté 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.

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