TOWLE & CO.

DEEP VALUE INVESTING

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To: Investors

Better yet! Following a disappointing second quarter, the Towle portfolio turned sharply higher starting in late August. Prospects for corporate tax reform and solid economic data boosted investor sentiment for economically sensitive, deep value equities. The valuation gap between growth and value, noted in our second quarter investor letter, narrowed.

While numerous unsettled global issues persist, most investment strategists continue to view the world's economy as balanced and prosperous, exhibiting synchronized expansion for the first time since the Great Recession. Stock markets remain focused on the anticipated improvement in corporate earnings, and consensus earnings for the Towle portfolio reflect this outlook. Based on Capital IQ estimates, the Towle portfolio's median projected P/E for 2018 remains attractive at 8.9x.

Short and long term performance results are noted below. Periods greater than one year are annualized.

Periods ending 9/30/17	Towle DVC *(Gross of fees)*	Towle DVC *(Net of fees)*	Russell 2000 Value	S&P 500 Total Return
3 months	12.61	12.43	5.11	4.48
9 months	10.39	9.81	5.68	14.24
1 year	33.35	32.41	20.55	18.61
3 years	18.06	17.23	12.12	10.81
5 years	21.55	20.70	13.27	14.22
10 years	11.16	10.35	7.14	7.44
20 years	13.01	12.18	8.60	7.00
30 years	13.86	13.05	10.31	9.53
Inception (1-1-82)	16.82	15.99	12.25	11.66

The third quarter letter breaks out as follows: **Portfolio Update** and **Looking Ahead**.

Portfolio Update

This section has been removed for compliance reasons to exclude discussing specific securities transactions.

Looking Ahead

When will the "good times" end for stock market investors? Since the Great Recession low on March 9, 2009, the S&P 500 Index has surged 372% through quarter end. The corresponding bull market is now the second longest on record. Valuation metrics are full to high as measured by our closely watched Rule of 20. What will unseat extended valuations and continued growth in corporate earnings?

Many strategists conclude that the next major downturn in stocks will likely occur when the U.S. finally succumbs to a reversal in economic growth, a recession. Such an event would not only result in reduced corporate earnings but also prompt a likely reduction in valuation multiples.

While forecasting a recession is difficult for all investors, several predictive tools exist to help us with this critical task. As a weekly discipline, we produce and evaluate our internally generated analytical tool called ACME. This analysis provides an overview of broad economic and financial indicators relevant to equity markets – Asset Valuation, Cost of Capital, Market Dynamics, and Economic Conditions. Additionally, in an effort to understand the "big picture," our investment team reads and considers extensive amounts of information including how other market watchers monitor recessionary developments.

For instance, Sam Stovall, Chief Investment Strategist of U.S. Equity Strategy at CFRA Research, looks at four indicators to identify recessionary pressures (*Kiplinger's Personal Finance*, October 2017):

1) Every recession since 1960 was preceded by a year-over-year *decline* in Housing Starts.

	August 2016	August 2017	Conclusion
Housing Starts	1,164,000	1,180,000	No Recessionary Pressure

2) Consumer Sentiment as measured by the U. of Michigan must *drop* by an average of 9% year over year.

	Sept 2016	Sept 2017	Conclusion
Consumer Sentiment	91.2	95.1	No Recessionary Pressure

3) A six month *drop* averaging three percent on the Conference Board's Index of Leading Economic Indicators (LEI) is another warning.

	February 2017	August 2017	Conclusion
LEI	126.2	128.8	No Recessionary Pressure

4) When the 10 year Treasury Bond *dips below* the 1 year Treasury Note (inverted yield curve), recessionary conditions may exist.

	1YR T-Notes	10YR T-Bonds	Conclusion
Yield Curve	1.31%	2.33%	No Recessionary Pressure

From Stovall's perspective, one logically concludes that a U.S. recession is not at hand. In fact, the continuing narrative of attractive interest rates, low inflation, supportive commodity prices, and durable economic growth ripen the likelihood that the next recession is still a ways off. Nevertheless, portfolio progress for Towle & Co. has been substantial in recent years, and we must be alert to the most difficult phase of investing – knowing when to sell. Looking ahead, we will make every effort to be prudent in our capital allocation decisions, recognizing there is a time to be defensive.

For taxable accounts, realized 2017 gains currently exceed overall portfolio gains. While we continue to harvest tax losses where reasonable, additional realized gains may be taken in light of current, favorable stock market conditions.

We thank you for investing side-by-side with us and for your steadfast commitment to Towle Deep Value. Please do not hesitate to contact us with your comments and questions.

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DISCLOSURES