

TOWLE & CO.

DEEP VALUE INVESTING

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Somewhat better! Following disappointing first quarter results, performance turned positive over the last two quarters, recording a gain of 7.8% net of fees. Although year-to-date returns remain unsatisfactory, we believe the current economic environment and valuation profile of our deep value, cyclical holdings are attractive. Consequently, we will continue to execute our strategy with vigor while recognizing that today's supportive investment scene may deteriorate, resulting in a more defensive posture in the coming quarters.

Past performance is noted below. Results are annualized for periods greater than a year:

<i>Periods ending 9/30/18</i>	<i>Towle DVC (Gross of fees)</i>	<i>Towle DVC (Net of fees)</i>	<i>Russell 2000 Value</i>	<i>S&P 500</i>
3 months	3.09	2.81	1.60	7.71
9 months	-1.59	-2.21	7.14	10.56
1 year	3.36	2.54	9.33	17.91
3 years	22.99	22.10	16.12	17.31
5 years	12.05	11.24	9.91	13.95
10 years	13.96	13.13	9.52	11.97
20 years	13.70	12.87	9.83	7.42
30 years	14.30	13.48	10.85	10.61
Inception (1/1/82)	16.43	15.60	12.17	11.82

Past performance is no guarantee of future outcome. Refer to the last page for additional disclosures.

The third quarter letter segments as follows: **Investment Scene**, **Portfolio Update**, and **Outlook**.

Investment Scene

Today's bull market is the longest since 1932, almost 10 years in duration. Naturally, everyone in the financial community wants an answer to the following question: when will the current bull market end?

Without a doubt, underlying concerns challenge the market's upward trajectory. The Federal Reserve's target interest rate has increased dramatically, potentially slowing future economic activity. Inflation, although currently not troublesome, has reached its highest level since 2011, threatening asset prices. As evidenced by our closely watched Rule of 20 (Value Line P/E plus CPI), stock market valuations remain elevated. On the political front, the Federal Government spends our tax dollars without restraint, and U.S. trade tensions between China and other nations persist. These forces may well restrain or halt the advancing bull market.

Yet, economic momentum carries on – upbeat and positive. Recent surveys of the manufacturing and service sectors by the Institute for Supply Management are unquestionably strong. Small business optimism and labor market conditions are exceptionally robust. The Conference Board Leading Economic Index indicates that today's advance will likely continue. Bloomberg's Financial Conditions Index reflects a sturdy economy with a financial environment conducive to rising capital investment.

In light of these cross currents, three overriding concerns shape our message:

1. **Stock market valuations** are lofty.
2. **Inflationary cost pressures** will likely impede corporate profitability in the coming quarters.
3. **GDP growth trajectory** may slow in 2019.

Accordingly, the stock market is best described as uneasy and unsettled.

Portfolio Update

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

Outlook

While the U.S. economy is facing numerous uncertainties and the investment community is broadly apprehensive, we believe the following macro-economic conditions provide a supportive backdrop for today's discriminating investor:

1. **Interest rates remain low.** High grade bond yields hover at 4.1% today versus 6.2% in mid-2007. Low interest rates fuel economic activity.
2. **Inflation is muted.** At 2.7%, inflation has yet to disrupt economic stability. Inflation reached 5.6% prior to the Great Recession. From 1970-2007 inflation averaged 4.7%.
3. **Commodity prices are manageable.** The Producer Price Index for All Commodities has increased a modest 1.9% annually over the past three years compared to an average annual increase of 3.6% since 1970.

This good news combined with outperformance by the FAANGs (Facebook, Apple, Amazon, Netflix, Google) has pushed market indexes to new heights, creating a pronounced and overextended bifurcation between "growth" and "value" stocks. How this divergence gets reconciled is unknown, but overtime it will likely close. It is our expectation that the Towle portfolio will benefit from this rebalancing process, stimulated by investment capital searching for higher rates of return and lower valuation multiples.

In the final analysis, the paramount issue for those of us invested in the Towle strategy is not whether the market will go up or down in the short term but whether the stock market is correctly valuing our holdings. Heading into the fourth quarter, we believe our holdings, in aggregate, are mispriced. For now, we believe the investment community at large fails to give credit to the earnings potential and attractive valuation of the Towle portfolio holdings.

Accordingly, we forge ahead realizing that investment success is best measured over numerous years and that our deep value strategy has paid big dividends for many. However, there is no guarantee that our strategy will generate excess returns in the future. The equity markets will always be unpredictable, especially in the short term. As an investment team, we continue to be fascinated by the investment process. This is the challenge that keeps us coming back for more.

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DISCLOSURES

1) Performance results are calculated using a time-weighted total-rate-of-return method and are expressed in U.S. dollars. Results include the reinvestment of all income. Gross of fee performance is presented as supplemental information and reflects the deduction of all trading expenses, except in those accounts where ABP (Asset-Based Pricing) fees are assessed in lieu of standard trade commissions. Net of fee performance was calculated using actual management fees and ABP fees. 2) Although Towle & Co. makes no attempt to manage against the composition of a specific benchmark, the Firm provides the Russell 2000 Value Index as a readily accessible indicator of comparative small cap performance as well as the S&P 500 Index as a general indicator of the market at-large. The performance of an index is not an exact representation of any particular investment as one cannot invest directly in an index and investments made by Towle & Co. differ in comparison to the Russell 2000 Value Index in terms of security holdings and industry weightings. Towle & Co. invests in considerably fewer companies than either index with lower average multiples to book value, sales, earnings, and cash flow, and as a result, the volatility and returns of the indexes may be materially different from the individual performance attained by a Towle & Co. investor. 3) Policies for valuing portfolios, calculating performance, and preparing compliant presentations are available upon request. Unless otherwise noted, references to 'the Towle Portfolio' or 'the Portfolio' refers to a representative, fully discretionary portfolio managed in the Towle Deep Value strategy and member of the Towle Deep Value Composite. 4) Opinions expressed are those of Towle & Co. and should not be considered a forecast of future events or a guarantee of future results. Opinions and estimates offered constitute our judgment as of the date set forth above and are subject to change without notice, as are statements of financial market trends, which are based on current market conditions. All material presented is compiled from sources believed to be reliable, but no guarantee is given as to its accuracy. 5) CFA® is a designation issued by the CFA Institute. To earn the designation, candidates must pass three course exams, each requiring approximately 250 hours of self-study, and have completed four years of qualifying work experience.