

### MARKET REVIEW

The third quarter of 2017 stood in contrast to the two previous quarters in many different ways. Instead of a steady march upward led by large cap growth stocks such as the FANG (Facebook, Apple, Netflix, Google, et al) stocks, the third quarter was characterized by market participants' disagreement over future economic growth.

The key underlying controversy was the direction of global economies. The quarter began with a series of more moderate leading indicators. But as the quarter went on, more and more positive signs began to show, particularly from overseas. Industrial metal prices rose as well as currencies from commodity-producing countries such as Australia and Canada. Global purchasing manager indices remained resilient, and European indices reached a multi-year high.

When this message started to take hold, the market reacted. In mid-August, potentially catalyzed by hopes for long-awaited tax reform, small cap stocks woke from their 2017 slumber and recovered most of the 10%-plus deficit versus large caps they had accumulated. Value stocks followed this reversal by showing some life as well.

### PORTFOLIO POSITIONING

The portfolio management team continues to have a moderate exposure to momentum stocks. As is characteristic of the strategy, the team remains vigilant for risks to these stocks. The exposure has fallen during the past few months, but only as a result of market movement. The team's signals do not show any signs of concern at the moment.

The portfolio has the largest industry position in savings-and-loan companies and other mortgage-reliant firms. This position is offset by an underweight in banks, neutralizing interest rate risk. Overall the portfolio finds itself underexposed to dividend yield. While the team holds overweights in a few cyclical industries such as Machinery and Chemicals, they also have a more defensive position in technology, favoring software and services.

### PRODUCT OVERVIEW

The Small Cap Core strategy seeks to outperform the Russell 2000 Index by constructing a diversified portfolio using an investment process that combines analysis of economic and market forces; individual stock analysis and risk management; and efficient strategy implementation and trading. The core of our process is knowledge-based investing which uses signals from the activity of unique market participants to assess potential company appreciation.

### TOP FIVE CONTRIBUTORS (%)

| Security          | Avg. Weight | Portfolio Impact |
|-------------------|-------------|------------------|
| Fibrogen Inc..    | 0.81        | 0.36             |
| Magellan Health   | 1.63        | 0.27             |
| SkyWest Inc.      | 1.12        | 0.26             |
| Barnes Group Inc. | 1.37        | 0.25             |
| Regenxbio Inc.    | 0.43        | 0.25             |

### TOP FIVE DETRACTORS (%)

| Security               | Avg. Weight | Portfolio Impact |
|------------------------|-------------|------------------|
| Microstrategy Inc.     | 1.00        | (0.42)           |
| Axovant Sciences       | 0.38        | (0.28)           |
| Versartis Inc.         | 0.25        | (0.20)           |
| Synergy Pharmaceutical | 0.36        | (0.16)           |
| Windstream Holdings    | 0.17        | (0.15)           |

### REPRESENTATIVE BUYS AND SELLS

| Bought               | Sector      |
|----------------------|-------------|
| Medidata Solutions   | Health Care |
| Catalent Inc         | Health Care |
| Dynavax Technologies | Health Care |

| Sold                    | Sector                 |
|-------------------------|------------------------|
| Bob Evans Farms.        | Consumer Discretionary |
| Starwood Waypoint Homes | Real Estate            |
| Kite Pharma Inc.        | Health Care            |

## SMALL CAP CORE INVESTMENT MANAGEMENT TEAM

Derek Izuel, CFA  
Chief Equity Officer

- Investment experience since 1991
- Tenure with HighMark since 2008
- MBA – University of Michigan
- BA – Computer Science, University of California, Berkeley

Yanping Li, Ph.D.  
Senior Equity Research Analyst/ Portfolio Manager

- Investment experience since 2008
- Tenure with HighMark since 2011
- PhD – Applied Physics, Cornell University
- MS – Financial Engineering, University of California, Berkeley
- MA – Physics, Brandeis University

Richard Ren, Ph.D., CFA  
Senior Equity Research Analyst

- Investment experience since 2007
- Tenure with HighMark since 2014
- PhD – Chemical Physics & Statistical Analysis, University of California, Los Angeles
- MBA – University of California, Berkeley
- BS – Industrial Automation, Zhejiang University

Justin Sheetz, CFA  
Equity Research Analyst

- Investment experience since 1997
- Tenure with HighMark since 2014
- BA – International Studies, Colby College
- MS I – Computational Finance and Risk Management, University of Washington

Angela Shen  
Quantitative Equity Analyst

- Investment experience since 1992
- Tenure with HighMark since 1992
- BA – Statistics, University of California, Berkeley

Todd Mackedanz  
Head of Equity Trading

- Investment experience since 2001
- Tenure with HighMark since 2014
- BS – Finance, Montana State University

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Current and future portfolio holdings are subject to change and risk. There is no guarantee that the securities listed will remain in or out of the portfolio. The discussion of the strategy's holdings is not intended as a recommendation to buy, hold or sell any of these securities. Past performance is no indication of future results.

The information provided herein represents the opinion of the manager of the market environment at a specific point in time and should not be relied upon as research or investment advice. Information presented for Top Contributors and Detractors is based on a representative account within the Small Cap Core Composite, and on a trade date basis. As of September 30, 2017 the composite consists of equal to or less than five accounts, and composite represents 1.23% of the total firm assets. The minimum portfolio size for inclusion in the composite is \$500,000. The benchmark for this composite is the Russell 2000 Index. The benchmark is used for comparative purposes only and is provided to represent the market conditions during the period shown. The benchmark measures the performance of the small-cap segment of the U.S. equity universe. The Index is a subset of the Russell 3000® Index representing approximately 8% of the total market capitalization of that index. It includes approximately 2,000 of the smallest securities based on a combination of their market cap and current index membership. An index of approximately 1,000 of the largest companies in the U.S. equity markets, the Russell 1000 is a subset of the Russell 3000 Index. The Russell 1000 comprises over 90% of the total market capitalization of all listed U.S. stocks, and is considered a bellwether index for large cap investing. The Russell 1000 is a market capitalization-weighted index, meaning that the largest companies constitute the largest percentages in the index and will affect performance more than the smallest index members. Benchmark returns do not reflect the deduction of advisory fees, custody fees, transaction costs, or other investment expenses. The benchmark returns assume the reinvestment of dividends and other earnings. An investor cannot invest directly in an unmanaged index. Specific securities identified and described do not represent all of the securities purchased, sold or recommended for advisory clients, and you should not assume that investments in the securities identified and discussed were or will be profitable. Please call (800) 582-4734 or write to [highmark.capital@highmarkcapital.com](mailto:highmark.capital@highmarkcapital.com) to obtain the calculation methodology for contributors and detractors and a list of every holding's contribution to the overall representative account's performance during the quarter.

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