Capital Appreciation | **Risk Management** | Income Generation | Liquidity Management

GUNR

NFRA

GQRE

Scenario Planning

Expectations for Real Assets

Despite the market environment, we believe that real assets should be an essential element of every investment portfolio. Growing numbers of institutional investors have steadily increased their real asset allocations over the past few decades. Many investors have discovered the potential benefits of real assets in potentially providing long-term total returns, potential inflation protection and the difference in historical correlation with equity and fixed-income investments. We believe investors are looking for what real assets can offer: the potential for income, potential gains and capital preservation in an unclear global environment.

At the same time, investors continue to benefit from innovation within a variety of investment vehicles that focus on real assets. Furthermore, strong demand for real assets is being met with an unprecedented supply of opportunities for investment, and we believe trends indicate that it will continue to grow. The Real Assets classification (e.g., timber, water, infrastructure, natural resources, etc.) is continually evolving, influenced not only by new asset types, but also regulatory and issuance changes.

DEFINING THE ASSET CLASS AND ITS BENEFIT POTENTIAL

Real assets—which we define as real estate, infrastructure and natural resources—form the pillars of the global economy. As such, these classifications are inherently tied to global developments, inflation and other macroeconomic trends. Notably, the cash flows that historically have been produced by real assets can be valuable in times of both economic expansion and contraction. Real assets represent physical assets that are often linked to inflation—a favorable characteristic as potential demand rises in periods of economic expansion. At the same time, the increasing demand for the goods and services that real assets provide may be relatively predictable and inelastic (insensitive to changes in price or income), which can be helpful in periods of economic contraction.

While cash-flow stability has historically been characteristic of real asset investments, the fundamentals that drive the cash flows are distinct. As such, real assets can provide an effective way to enhance portfolio diversification beyond traditional stock and bond allocations. The chart below highlights potential benefits such as income, capital appreciation, higher risk-adjusted returns and inflation protection.

POTENTIAL BENEFITS OF REAL ASSETS	
Diversification	Certain types of real estate have been shown to be less resistant to interest rates in a rising rate environment. As the costs of steel, sheetrock and glass rise, the intrinsic value of existing structures increase. Replacement costs also rise, reducing supply. Residential real estate, specifically those with yearly lease renewals, may be particularly strong in protecting against inflation.
Income	Potentially stable cash flow may be derived from long-term projects that deliver essential products or services. Infrastructure may be defensive in the face of economic contraction.
Capital Appreciation	Potentially participate in the benefits of rising prices of raw input materials. These investments offer the additional potential advantage of offsetting some of the longer-term inflationary effects of economic expansion in emerging and established regions.
Potentially Higher Risk-Adjusted Returns	Historically, the volatility of many real asset classes has been lower than that of equities, leading to higher risk-adjusted returns.

Real assets tend to have low correlations with traditional stock and bond allocations. Correlations are also low among the sectors comprising individual real asset categories.

PORTFOLIO DIVERSIFICATION

Real asset returns have historically had low correlations to traditional equity and fixed-income investments, which our findings suggest they can provide an effective way to enhance the diversification of a traditional stock and bond portfolio. Individual real asset categories have also shown low correlations with each other — consequently investors may be able to diversify further by investing in more than one real asset class.

As highlighted in the chart below, the correlations of real estate with infrastructure and natural resources are 0.85 and 0.62, respectively. The return streams of two assets having a correlation of 1.00 would be perfectly correlated. These measures are relatively moderate because the drivers behind the returns of these categories are distinct. Consider natural resource pricing, which for some assets like timber are highly dependent on short-term factors such as climate, temperature and water supply. In contrast, the cash flows from some infrastructure assets, such as toll roads, tend to rise with an expanding economy, while those derived from more essential services, such as utilities, tend to be more highly regulated, and consequently during times of economic weakness tend to have more locked in levels of usage pricing.

LOW CORRELATIONS AMONG REAL ASSET CONSTITUENTS (2008 – 3Q2018)

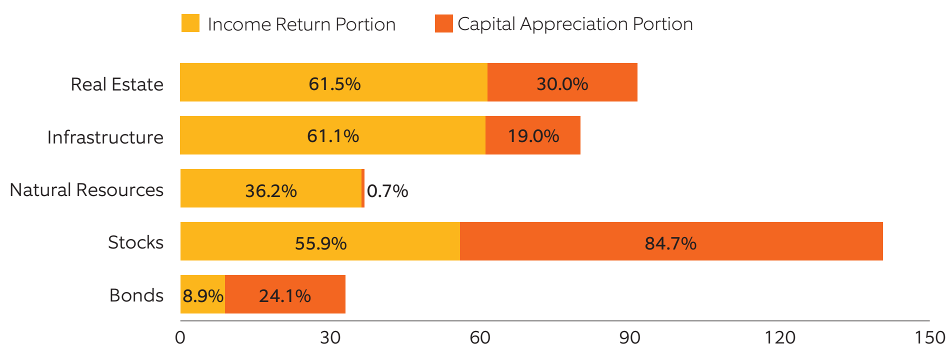
	REAL ESTATE	INFRASTRUCTURE	NATURAL RESOURCES	STOCKS	BONDS
Real Estate	1.00	0.85	0.62	0.85	0.49
Infrastructure	0.85	1.00	0.76	0.87	0.58
Natural Resources	0.62	0.76	1.00	0.79	0.38
Stocks	0.85	0.87	0.79	1.00	0.35
Bonds	0.49	0.58	0.38	0.35	1.00

Source: Bloomberg and Northern Trust Investment Strategy, Index data for the various correlation calculations above are as follows: Real Estate: MSCI ACWI IMI Core Real Estate Index; Infrastructure: S&P Global Infrastructure Index; Natural Resources: S&P Global Natural Resources Index; Stocks: MSCI World Index; Bonds: Barclays Global Aggregate Bond Index. Indexes are gross of fees and indexes cannot be invested in directly. **Past returns are no guarantee of future results.** Calculations are as of January 1, 2008 to September 30, 2018.

CAPITAL APPRECIATION POTENTIAL

Our research has shown that both income return and capital appreciation represented a meaningful amount of the historical total returns generated by real assets below. Historically, many of these hard assets tend to be long term and increase in value over time, as replacement costs may rise and operational efficiencies can be achieved. For many investors, this scenario may be visualized within their own daily experience as they see leasing of vacant space, steady climb of toll road fees, rising usage of energy or climbing wood prices. We believe that income from real-asset-related investments may help protect value on the downside, while operational efficiencies may enhance value on the upside.

10-YEAR CAPITAL APPRECIATION AND INCOME TOTAL RETURNS OF REAL ASSETS VS. STOCKS & BONDS (2008 - 3Q2018)



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Risk-adjusted return refines an investment's return by measuring how much risk is involved in producing that return.

POTENTIALLY HIGHER RISK-ADJUSTED RETURNS

Adding real assets may also enhance the risk-adjusted returns of a mixed-asset portfolio. The chart below shows the various historical Sharpe Ratios of the three real asset categories in comparison to equities and bonds. The Sharpe Ratio is a measure of return per unit of risk, which indicates whether an investment's return sufficiently rewarded investors for the level of risk assumed (the higher the Sharpe Ratio, the greater the level of risk-adjusted performance). For example, the 10-year Sharpe Ratio for Infrastructure as defined in the chart below is 0.214 which means that an investor should have a greater risk-adjusted return in comparison to an investment in Real Estate and in comparison to a Treasury bond which has a Sharpe Ratio of zero. Only when an investor compares one investment's Sharpe Ratio with that of another investment can the investor get a feel for the return versus the relative amount of risk they can expect to take to achieve that return.

10-YEAR SHARPE RATIOS OF REAL ASSETS VS STOCKS AND BONDS (2008–3Q2018)

CATEGORY	SHARPE RATIO
Real Estate	0.183
Infrastructure	0.214
Natural Resources	0.135
Stocks	0.381
Bonds	0.395

Source: Bloomberg and Northern Trust Investment Strategy, Index data for the various correlation calculations above are as follows: Real Estate: FTSE EPRA/NAREIT Global Index; Infrastructure: S&P Global Infrastructure Index; Natural Resources: S&P Global Natural Resources Index; Stocks: MSCI World Index; Bonds: Barclays Global Aggregate Bond Index. Indexes are gross of fees and indexes cannot be invested in directly. **Past returns are no guarantee of future results.** Calculations are as of January 1, 2008 to September 30, 2018.

While real assets tend to retain value during economic downturns and contribute to value creation during economic upturns, performance generally lacks drastic movements in either direction. This potential performance stability may provide investors with portfolio benefits in a variety of market environments.

AVERAGE ANNUAL RETURNS & YTD RETURNS OF REAL ASSETS (2008–3Q2018)

	NATURAL RESOURCES	GLOBAL REAL ESTATE	GLOBAL LISTED INFRASTRUCTURE
YTD	5.1%	-0.8%	-4.6%
1 Year	14.1%	2.9%	-2.8%
3 Year	19.7%	7.8%	8.0%
5 Year	4.1%	6.2%	6.1%
10 Year	3.2%	6.7%	6.1%

Source: Bloomberg and Northern Trust Investment Strategy, Index data for the various correlation calculations above are as follows: Natural Resources: S&P Global Natural Resources Index; Global Real Estate: FTSE EPRA/NAREIT Global Index; Global Infrastructure: S&P Global Infrastructure Index. Indexes are gross of fees and indexes cannot be invested in directly. **Past returns are no guarantee of future results.** Calculations where applicable are as of the last trading day in September of the period to September 30, 2018; except for year to date which is January 2, 2018 to September 30, 2018.

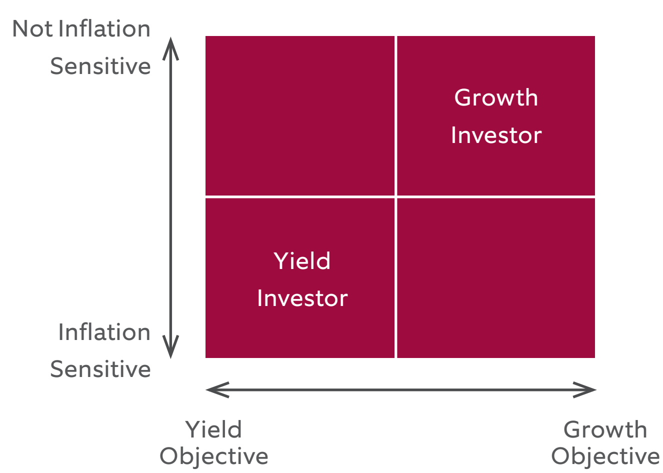
INSIGHTS LEAD TO INNOVATION

Investors seeking to capitalize on the changing investment landscape may be able to find innovative solutions that potentially enhance the real assets allocation of their portfolio. Below are insights that contributed to the creation of alternatively-weighted index solutions in an effort to take advantage of recent an innovative trend.

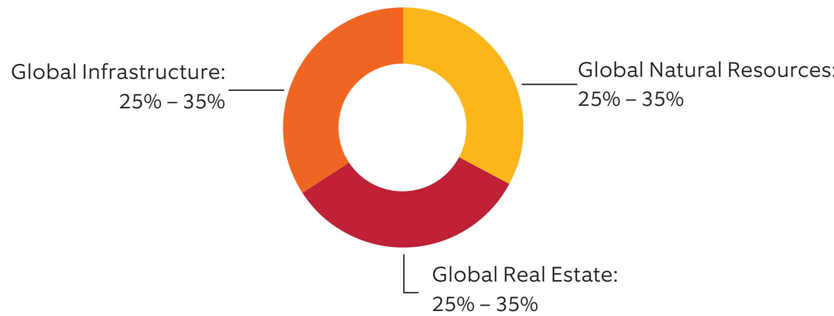
CATEGORY	INNOVATION	INNOVATIVE FUND
Real Estate	Incorporate a quality approach to real estate investing utilizing an empirically-tested quantitative model that assigns each security a quality ranking based on management efficiency, profitability, and cash levels.	FlexShares Global Quality Real Estate Index Fund (GQRE)
Infrastructure	Identify a broader universe of companies and industries involved in the infrastructure space which could include cellular towers, data centers, government projects and social infrastructure.	FlexShares STOXX® Global Broad Infrastructure Index Fund (NFRA)
Natural Resources	Focus on the upstream segment of the resource supply chain which refers to the beginning of the supply chain, when resources are extracted from the ground and sold to producers. By adding focused exposure to the upstream market - potentially minimizing the risk of rising resource prices to downstream investments.	FlexShares Morningstar® Global Upstream Natural Resources Index Fund (GUNR)

IMPLEMENTING THE REAL ASSETS PORTION OF A PORTFOLIO

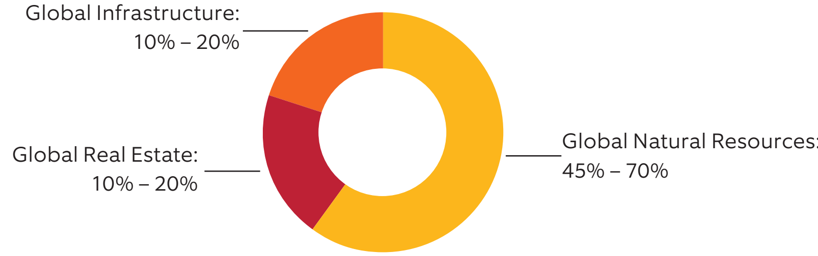
A number of considerations should be taken into account when building a portfolio of real assets. One approach for the initial structure is to define the investor's objectives in terms of yield versus growth-oriented strategy and sensitivity to the impact of inflation.



For the Yield Investor, a real assets strategy may be to emphasize more income-oriented but inflation sensitive investments that generate potential steady cash flows.



For the Growth Investor, a real assets strategy may be a broader exposure to natural resources to help meet the growth objective.



Building a real asset portfolio is a process that requires multiple considerations in terms of planning, implementation and monitoring. Real assets can play a fundamental role in a portfolio, depending on an investor's objectives and given the current low-yield environment along with the potential diversification that real assets have historically provided, we believe that investors should consider them in order to create a well-diversified portfolio.

FIND OUT MORE

The FlexShares approach to index-based investing is, first and foremost, investor-centric and goal oriented. We pride ourselves on our commitment to developing products that are designed to meet real-world objectives for both institutional and individual investors. If you would like to discuss the attributes of any of the ETFs discussed in this report in greater depth or find out more about the index methodology behind them please don't hesitate to call us at 1-855-FlexETF (1-855-353-9383) or visit **www. FlexShares.com**.

IMPORTANT INFORMATION

Before investing, carefully consider the FlexShares investment objectives, risks, charges and expenses. This and other information is in the prospectus and a summary prospectus, copies of which may be obtained by visiting www.flexshares.com. Read the prospectus carefully before you invest.

Foreside Fund Services, LLC, distributor.

An investment in FlexShares is subject to numerous risks, including possible loss of principal. Fund returns may not match the return of the respective indexes. A full description of risks is in the prospectus.

FlexShares Global Quality Real Estate Index Fund (GQRE) is passively managed and uses a representative sampling strategy to track its underlying index. Use of a representative sampling strategy creates tracking risk where the Fund's performance could vary substantially from the performance of the underlying index along with the risk of high portfolio turnover. It is subject to real estate sector risk in addition to the general risk of the stock market. Investments in foreign market securities involve certain risks such as currency volatility, political and social instability and reduced market liquidity. To the extent that the Fund invests in Emerging markets, those investments may be subject to increased price volatility and may be more susceptible to adverse economic, market, political or regulatory occurrences affecting that country, market, industry, sector or asset class. Investing in securities of real estate companies will make the Fund more susceptible to risks associated with the ownership of real estate and with the real estate industry in general, as well as risks that relate specifically to the way in which real estate companies are organized and operated. Real estate companies may have lower trading volumes and may be subject to more abrupt or erratic price movements than the overall securities markets. The value of real estate securities may underperform other sectors of the economy or broader equity markets. To the extent that the Fund concentrates its investments in the real estate sector, it may be subject to greater risk of loss than if it were diversified across different industry sectors. The Fund is also subject to the risk that its investments will be affected by factors that impact REITs and the real estate sector generally. Investing in REITs involves certain unique risks in addition to those risks associated with investing in the real estate industry in general. REITs whose underlying properties are concentrated in a particular industry or geographic region are also subject to risks affecting such industries and regions. By investing in REITs through the Fund, a shareholder will bear proportionate expenses of the REITs in addition to expenses of the Fund.

FlexShares Morningstar® Global Upstream Natural Resources Index Fund (GUNR) is passively managed and uses a representative sampling strategy to track its underlying index. Use of a representative sampling strategy creates tracking risk where the Fund's performance could vary substantially from the performance of the underlying index along with the risk of high portfolio turnover. It is subject to the global natural resource industry. As the demand for or prices of natural resources increase, the Fund's equity investment generally would be expected to also increase. Conversely, declines in demand for or prices of natural resources generally would be expected to cause declines in value of such equity securities. Such declines may occur quickly and without warning and may negatively impact your investment in the Fund. Investments in foreign market securities involve certain risks such as currency volatility, political and social instability and reduced market liquidity. To the extent that the Fund invests in Emerging markets, those investments may be subject to increased price volatility and may be more susceptible to adverse economic, market, political or regulatory occurrences affecting that country, market, industry, sector or asset class.

FlexShares STOXX® Global Broad Infrastructure Index Fund (NFRA) is passively managed and uses a representative sampling strategy to track its underlying index. Use of a representative sampling strategy creates tracking risk where the Fund's performance could vary substantially from the performance of the underlying index along with the risk of high portfolio turnover. It is subject to infrastructure-related companies risk and MLP risk. Risks associated with infrastructure-related companies include: realized revenue volume may be significantly lower than projected and/or there will be costs overruns; infrastructure project sponsors will alter their terms making a project no longer economical; macroeconomic factors such as low gross domestic product ("GDP") growth or high nominal interest rates will raise the average cost of infrastructure funding; government regulation may affect rates charged to infrastructure customers; government budgetary constraints will impact infrastructure projects; and special tariffs will be imposed. Investments in foreign market securities involve certain risks such as currency volatility, political and social instability and reduced market liquidity. To the extent that the Fund invests in Emerging markets, those investments may be subject to increased price volatility and may be more susceptible to adverse economic, market, political or regulatory occurrences affecting that country, market, industry, sector or asset class.

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