July 16, 2014

Dear Investor,

Client accounts are up 5.5% on average as of the end of June, net of fees. Accounts continue to gain along with the stock market (S&P 500 up 7% YTD) despite lower risk profiles. At quarter end roughly two thirds of client holdings were stocks. The rest of client holdings are in lower returning but more predictable income generating investments: bonds, preferred stock, and real estate investment trusts.

The investing environment hasn't fundamentally changed from last quarter when I described the following headwinds to near term investment performance:

1. Stocks are trading at the high end of their historical averages.
2. A substantial portion of earnings growth in recent years has been driven by cost cutting. It appears likely that further cost savings will be more difficult to come by.
3. Global economic growth remains slow, and does not appear likely to improve dramatically. Slowing population growth in developed nations as well as still high levels of consumer debt both contribute to the slower outlook.

These factors make it more difficult to find good companies at attractive valuations. That said, I think there remain individual stocks that offer good value. Several of the largest banks, as well as some of the large technology firms, look attractively valued. And I continue to look for opportunities to buy smaller companies trading below my estimate of their fair value.

Notes on Holdings

First quarter earnings (reported in April and May of this year) for our investments were generally soft, partly due to bad weather that reduced US consumer spending. There were some exceptions. Delta reported solid bookings and profitability despite a number of cancelled flights. And despite the lackluster start to the year, the stock prices of the majority of our investments in the energy, transportation and industrial sectors rose modestly.

Earnings for our large bank holdings were a little weaker than last year, reflecting a combination of light trading volumes (an important profit center for the large banks) and slightly lower lending margins (the difference between what banks charge for loans and what they pay for deposits and other funding).

One concern to investors in Bank of America and Citigroup related to the Federal Reserves "Comprehensive Capital and Review" (CCAR) program. That program, developed in response to the credit crisis, requires the largest banks to provide the Fed with details on their capital surplus. Banks must provide their current capital surplus as well as an estimate of their capital surplus in an extreme stress scenario, such as a severe recession. The banks must also request permission to return a stated level of capital to shareholders via dividends and share repurchases. If the Federal Reserve views the planned returns as too large relative to a bank's surplus capital, permission will be denied. A bank refused permission must undergo a lengthy resubmission or wait a year for the next go around. In the

first quarter, both Bank of America and Citigroup's requests to the Federal Reserve were denied, although for slightly different reasons.

Bank of America's request was initially approved. However when the bank later discovered a significant error in its surplus capital calculation, the Federal Reserve changed its ruling and required the bank to submit a new request.

The denial of Citigroup's request was more straightforward. That request was viewed as too large relative to the bank's capital surplus despite the fact that Citigroup is now one of the best capitalized of the major banks. The Fed's position is based on fairly pessimistic assumptions regarding how Citigroup would fare relative to other banks in a severe recession, based upon the bank's performance in 2008. Given Citigroup's efforts to dispose of problem loans over the last five years, these assumptions might well be too pessimistic. Regardless, Citigroup will have to wait another six months to a year to begin returning substantial capital to shareholders.

The Fed denials negatively impacted the share prices of both Citigroup and Bank of America, but I expect the CCAR issues to resolve when the banks resubmit requests for 2015 distributions. The question is when, not if, excess bank capital will be distributed to shareholders. And given that the banks already have historically high levels of excess capital on hand, those distributions could be substantial over the next several years.

I added to our holdings of US Lime and Mineral early in the quarter, after the company reported notably strong first quarter earnings. US Lime operates limestone quarries in Texas, Arkansas and Oklahoma. Lime is extracted and then processed and sold for use in the production of asphalt, steel, agricultural feeds, roofing shingles, and glass, among other end products. Because limestone is heavy and expensive to transport, the business tends to be locally based and largely insulated from competition. This is especially true given the difficulty of obtaining permits for new limestone quarries. As a result, well located limestone producers have a substantial amount of pricing power. Quicklime, a form of processed limestone, has risen in price every year since 1999, including during the 2008/2009 recession, when most commodity producers saw substantial price declines. Furthermore, the company is well managed, has a growing stockpile of cash, and has no debt.

Subsequent to our adding to holdings of US Lime the stock rose to an all-time high, and is now among our better performing investments year to date.

As always, let me know if you have any questions.

Note: This information is intended as a general discussion of past account performance and investment strategy. It is not a recommendation to purchase any specific security or type of security. An investment in securities involves the risk of loss. Douglas S. Weiss is a registered investment advisor, member FINRA. Client performance is based on the arithmetic average return across all accounts managed for at least one year, net of management fees. Data is unaudited. Individual client returns vary reflecting risk profile as well as tax and other considerations. S&P 500 index return is based on total index return, inclusive of dividends.