Grisanti Capital Management

April 9, 2015

Large Cap Value Portfolio First Quarter 2015 Letter to Investors

For the Period Ending March 31, 2015

	1Q2015	One Year Since 3/31/2014	Since 9/30/2011
Grisanti Capital Management LLC Large Cap Value Portfolio (net of fees) [1]	***+2.6%***	***+14.9%***	***+102.1%***
S&P 500	+0.9	+12.7	+97.0
Average US Large Cap Value Fund	+0.2	+7.9	+85.8

Dear Clients & Friends of Grisanti Capital Management,

It's not what you don't know that gets you into trouble.
It's what you know for certain that just ain't true.
– Mark Twain

Managing a concentrated portfolio has certain advantages. First, it allows us to stay away from what we don't know (which is plenty). But, even better, because we don't manage a large, market-like portfolio, we don't have to be certain about things – like the price of oil, or the future of interest rates – that we think are essentially unknowable in the short term. Instead, we have the luxury of focusing on a much smaller, more understandable universe – the operations and prospects of our twenty or so portfolio companies. As Warren Buffett has written, concentrated investing is like being a hitter without called strikes. You can stand at the plate all day, waiting for the one pitch that you really know how to hit.

This ability to stick to what we know worked well for your portfolio in the first quarter. Targeted investments in a medical products company, two retailers and a refiner that benefits

[1] The GCM Large Cap Value Composite performance is in compliance with the Global Investment Performance Standards (GIPS) through 2013 (2014 pending). Performance for the Large Cap Value Composite is shown net of advisory fees and transaction costs, if any. GCM's advisory fees are described in Part II of its Form ADV. The Composite's benchmark, the S&P 500 Index, includes the reinvestment of income but does not include any transaction costs, management fees or other costs. The Large Cap Value Composite includes all accounts that are fully discretionary, managed in the large cap value strategy and over $500,000 in total assets. Prior to 2002, there was no minimum asset level. Past performance is no guarantee of future results. As with any investment vehicle, there is always the potential for gains as well as the possibility of losses.

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from falling energy prices helped your portfolio gain 2.6%, net of fees. This compares to the S&P 500 Index, which returned 0.95%, and also compares favorably to the average large cap value mutual fund, which was up 0.18%. Our performance for the quarter placed us in the top 5% of all large cap value managers. **More importantly, our trailing one year performance – up 14.9% (net of fees) since March 31, 2014 versus 7.9% for the average large cap value manager – places us in the top 1%.**[2]

While there was no single reason for our strong quarter, our philosophy of researching many companies but buying only a few certainly contributed. This quarter we made just one investment, which we discuss below. When we do uncover what we think is a diamond in the coal heap, we establish larger positions than most managers, and we take even bigger weightings in those companies whose attractive prospects seem most underappreciated by the market. That type of concentration, if done correctly, adds great value over time.

One example of this in your portfolio is **Valero,** a refining company that we've written about before. It is a long-term holding, first purchased in 2010 at $18.46. Currently selling at $63.62, it has benefited from the American Oil Renaissance as the price of oil and natural gas (its two largest costs), have plummeted. During the first quarter, Valero was both our largest position (about 8%), and also our best performing stock (up 27% in a flat market). That combination – largest position *and* best performer – does great things for a portfolio.

Successful value investments are always a double-edged sword, however, as our refining companies are no longer the bargains they once were. We have started taking profits – refining now represents less than 10% of the portfolio, down from 22% about a year ago. We are always seeking overlooked opportunities, but with the market up 97% in the last three and a half years, it has become more difficult. The one new investment we made during the quarter was **United Parcel Service** (UPS). We view this as a defensive purchase for what could be choppy times ahead in the market. We believe UPS possesses both a great brand and irreplaceable network of assets. The company has a rock solid (AA+) balance sheet and a 3% dividend. Trading at roughly a market multiple (a valuation not seen in more than five years), we were able to acquire our interest at an attractive price. The company steadily returns capital to shareholders, and its restructuring plans should deliver earnings growth. The real bonanza could come if the US Postal Service institutes more rational pricing, as we think its continued losses will force it to do. That would allow all shipping companies to raise prices.

Another successful investment in the first quarter was behemoth "etailer" **Amazon.com Inc**. It rose sharply in the first quarter (up 20%), helped by strong fourth quarter profits, the prospect of increased sales, and profit disclosures for its thriving Web Services division. The stock lagged materially during 2014 owing to misfires on "non-core" growth products (Kindle,

[2] The performance shown is for the Grisanti Capital Management Large Cap Value Composite. The S&P 500 Index performance includes reinvested dividends. The comparison to other value managers is made via the Morningstar large cap value universe, which includes 1367 mutual funds. While we are not a mutual fund, we compare our net results (after fees) to those of publicly traded mutual funds with similar styles (U.S. large cap value equity) because we believe it is a fair comparison and the data is publicly available.

Fire Phone, etc.), fears of moderating top-line growth and uncertainty over the company's profitability. Because it is spending enormous amounts on growth initiatives, the stock does not appear cheap on an earnings basis, but on a price-to-sales basis, it is cheaper than Walmart and growing its revenues at a much faster rate. At any given point the management could decide to deliver vast earnings to shareholders. We think perceptions are poor for a company that stands to be an internet leader for a long time.

Not everything worked out in the first quarter. Shares of **American Express** declined 14% as management announced the loss of a co-branded card relationship with wholesaler Costco Corp. (8% of sales), resulting in flat-to-down earnings in 2015. With competition heating up for co-branded credit card relationships, investors have called into question Amex management's long-term goals of 8% sales growth and 12%-15% earnings growth. We believe Amex will be a beneficiary of the coming rebound in consumer credit. Further, its focus on strong returns (the reason Costco did not renew its contract was that Amex would not accept new, less desirable terms), best-in-class management team and exceptional brand will produce value and fuel earnings growth in 2016. The stock's sharp decline has brought it back to our initial purchase price, and we have added to the position.

As always, our crystal ball is much clearer when we gaze into the future of our portfolio companies than when we speculate about the market as a whole. Having said that, the current investment climate reminds us a lot of the late 1990s, when stocks continued to rise in a strong economy but experienced increased volatility. In 1998 for example, the S&P 500 Index was up 29% for the entire year, even though in a six week period over the summer it fell 19% as Russia defaulted on its debt. While it's easy to look overseas for possible sources of volatility – Russia, Iran, Greece – we think the most likely culprit will be our own Federal Reserve. Higher interest rates in the form of a higher fed funds rate may add volatility to the market as soon as the current quarter. But we believe that rates will only rise if the economy is on sounder footing, which is a good thing, in the long run, for stocks. And higher rates would only bring them closer to historical norms and away from stimulus levels in place since 2009. In fact, we'd be far more afraid of *lower* rates (which might signal a deflationary slowdown).

In any event, we will continue to hunt for bargains, which are rare these days, but still exist if one is patient. Our narrow focus has paid off. Our current research team, which was put in place after the firm's restructuring in 2011, has produced strong results over the past three and a half years, with our composite up 102% (net of fees) versus the S&P Index up 97%. We will try to adhere to Mark Twain's adage and not be too certain about anything. That way, we will continue to question our research, our assumptions and our investments. We believe constant scrutiny leads to good results in the long term.

Very truly yours,

Christopher C. Grisanti