Grisanti Capital Management

January 15, 2014

Large Cap Value Portfolio Fourth Quarter 2013 Letter to Investors

Dear Clients and Friends of Grisanti Capital Management:

	For the Period Ending December 31, 2013		
	4Q13	Since 9/30/2011	Since 1/1/2000
Grisanti Capital Management LLC Large Cap Value Portfolio	***+15.1%***	***+73.7%***	***+146.0%***
S&P 500	+10.5	+71.6	+63.4

Underscoring the power of a concentrated investment philosophy, the Grisanti Capital Management portfolio rose more than 15% in the fourth quarter, well ahead of a strong market. Although most holdings performed well, the clear standouts were our refining investments. Benefiting from the American Oil Renaissance theme, three of our four refiners surged more than 40% in the quarter. Further, due to our recent strength, we are pleased to report that since the fourth quarter of 2011, when we took steps to restructure the firm, the Grisanti Capital Management Portfolio is up 74%. That puts us slightly ahead of a strong market, but what's more important is that the portfolio delivered these returns while often holding significant amounts of cash when events (such as government shutdowns or debt ceiling crises) warranted a more guarded outlook. Excluding our cash cushion, our stocks during that same period were up 84%, well ahead of the S&P 500 Index (up 72%). While our cash position hurt us at times, the investment environment won't always be as benign as it was in 2013, and prudence won't always be worth so little.

A year like 2013 leaves investors with an obvious question – after such strength, can we really expect attractive long-term returns from here? We believe the answer is yes. In fact, we believe economic and market conditions at the beginning of 2014 seem particularly constructive for U.S. equities. For reasons discussed below, the current environment reminds us of the late 1990s, a very profitable time for equity investors.

There are a number of factors which make us excited about 2014. **The Federal Reserve remains incredibly accommodative**, meaning it won't take its foot off the monetary gas pedal until a sustainable recovery is clearly underway. Talks of tapering (cutting back on stimulative bond purchases) don't unnerve us because tapering will only occur under strong economic conditions, which are exactly what an equity investor craves. We'd be more worried if tapering

doesn't occur, as that would be a sign of weakness. **Corporate balance sheets are in the best condition since the 1950s,** with low debt and high profit margins. **Inflation remains low and labor costs stable**, which in turn allows interest rates to remain low and gives the Federal Reserve room to be even more accommodative if necessary. **The three-decade-long bond rally is over and money is now flowing into the equity market.** These asset cycles typically run for multi-year periods – the flow towards bonds and away from stocks began in 2007 and lasted six years. **Another U.S. budget showdown, the biggest cause of market instability over the last three years, seems less likely**. Politicians were so damaged by the government shutdown in October that this week they reached a trillion-dollar budget agreement, pushing off a confrontation at least until October.

The bearish counter to these positives is that after the 2013 run, equity valuations are extended. It is true that the market's price-to-earnings (P/E) ratio is about 10% above its long-term average. But this is where a comparison to the 1990s can bring perspective. Like today, in the mid-1990s the United States was undergoing a slow, 'jobless' recovery from the 1991-92 recession. Similarly, the government was mired in gridlock (including the 1995 shutdown), but inflation was low and falling further, interest rates were moderate, and corporate productivity was high. From 1995 to 1999, investors flocked to the equity markets, enjoying above-average returns for several years, driven by earnings growth *and* P/E expansion. In early 1995 the P/E was about 14, but by the end of 1999 it had risen to a dangerous, record-high 27. For the last 60 years, the average P/E has been about 14.5, while ranging from 6 (1974) to 27 (1999). It currently stands at about 16, which is not terribly high and with benign conditions we think there is further room for expansion. This type of P/E expansion combined with earnings growth propelled the market in the late 1990s. Provided that the positives set forth in the previous paragraph remain in place, we would expect similar strong returns for stocks over the next several years, though not without inevitable (and largely unpredictable) short term setbacks.

Fourth Quarter Review

Our refining investments had the biggest influence on the portfolio in the quarter. Stocks like **Valero** (up 48% for the quarter), **Marathon Petroleum** (up 43%) and **Western Refining** (up 42%) led the way. We believe these companies are beginning to reap the benefits of the American Oil Renaissance, as growing U.S. oil production has caused the price of domestic oil (West Texas Intermediate) to sell at about a $15 discount to European oil (Brent). When oil is cheaper for U.S. refiners than for their foreign competitors, domestic refiners can make diesel fuel and gasoline for less and sell it in foreign markets. For that reason, **refined petroleum products are fast becoming a huge US export success story – in 2013 they surpassed commercial aircraft and technology items like cell phones to become the United States' single largest export** (by dollar amount). Our bullish position is that this advantage will improve with expanded oil production. We expect a strong 2014 from this sector, as US oil production continues to climb.[1]

[1] By the way, we do not believe other energy investments that rely on the absolute price of oil make sense here, because we believe there is too much oil, certainly in the U.S. and eventually, as other countries begin to use "fracking" technology, overseas as well. We own the refiners as opposed to the production companies (like Shell or Exxon) because refiners can benefit from lower oil prices (especially if our refiners are the low cost producers of gasoline and diesel fuel and can export these commodities profitably).

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Our financial stocks also performed well, as fundamentals in this controversial industry have clearly turned. With the resurgent stock market, merger and acquisition activity has increased. The rise in long-term interest rates has led to a steep yield curve (low short term rates, higher long term rates), which allows banks to make profit on their core lending business by lending long-term at higher rates (think 30-year mortgages) while funding those loans by borrowing short-term at low rates (think time deposits). We believe we are in about the seventh inning of the recovery that commenced in 2009 and we have already reaped considerable gains from investments like **JP Morgan** (up 213% since initial purchase) and **Morgan Stanley** (up 134%). We suspect the weight of the financial sector will be lower in quarters to come.

While energy and financials comprise about half the stocks in the portfolio, the other half do not fit into broad "themes" but are individual companies whose unique prospects we find extremely attractive. A number of these were terrific investments in 2013. **McKesson**, a drug distributor, was up 68% for the year, our best single performer in 2013. **DirecTV**, a satellite television provider, was up over 35%. In an encouraging sign, a number of our newer investments were also strong performers. **Dover Corp**, an industrial conglomerate that was simply too cheap when we bought it in May, is up 36% since purchase. **Autodesk**, a play on the recovering building market, is up 27% since purchase in October. Finally, our airline investments (first **United** and later in the quarter the newly restructured **American** bought at the very end of the year) are going gang busters. United Airlines, benefitting from the continued consolidation of the industry, is up over 50% since purchase in August.

Our well researched investments delivered strong results in the fourth quarter, but we believe that the benefits of our concentrated investing philosophy are even more apparent (and much more important) over a longer period. Since our inception in 2000, the Grisanti Capital Management portfolio is up 146%,[2] more than double the return of the S&P 500 Index, which rose 63% during the same time period. We will differ from the market in any given year, as our investments are not tied to the calendar and often take several years to come to fruition. But when they bear fruit – as our financials have recently and as the refiners are beginning to – the harvest can be abundant. We look forward to reporting to you again after the end of the first quarter, and would welcome any questions you may have.

Very Truly Yours,

Christopher C. Grisanti

[2] Performance for the Large Cap Value Composite is shown before deducting 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. Your actual performance is attached, and may be higher or lower, depending on the specific investment objectives reflected in your portfolio. The Large Cap Value Composite and includes all accounts that are fully discretionary, managed in the large cap value strategy and over $1,000,000 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.