SUNCOAST EQUITY MANAGEMENT, LLC

January 2, 2016

Dear Client:

SEM closed the year +3.9% versus the S&P 500 +1.4%. Our outperformance in 2015 of 2.5% was in line with our since inception margin, whereby we earned +8.3% versus the S&P 500 +6.2% composite return net of fees. Since our inception the **SEM-DIS** (Disciplined Investment System) has grown a $1 investment into $4.23 versus the same investment in the S&P 500 which would have been $2.94. That is a meaningful difference when you add a few zeros on the end of it.

A sluggish economy, dragged down by the strong dollar and another year of falling energy prices, as well as the terrorist attacks in Paris and California, combined to create a very volatile stock market in 2015. In mid December, the Federal Reserve increased its target Fed Funds range by 0.25%, the first change in seven years, and emphasized a plan to lift rates gradually over the next few years. We believe the economy is on a decent footing with employment brightening, a steadily improving housing market and a budget deal worked out. Since the depths of the recession in 2009, the jobless rate has declined to 5% today from 10%, albeit the labor force participation rate still has a ways to go. Also, the collapse in oil prices is a net positive for most consumers.

Our market view is basically unchanged from this same time period two years ago. In our last two January client letters we opined that the overall market is in a fair value range. Consequently, appreciation from here is dependent on earnings growth. In the last two years the market appreciated roughly in line with earnings, with earnings growth for the S&P 500 of 8% in 2014 and expectations of flat to slightly down earnings for 2015 once companies report the fourth quarter in January. Prices don't always follow earnings each and every year, so we share some thoughts about stock price volatility and the role human emotions play below.

Looking towards 2016, profit growth for the S&P 500 and the wider spectrum of businesses in the market looks to be as uneven as it was in 2015. Consensus earnings growth estimates for the S&P 500 for 2016 of 8% might be a bit optimistic, but we shall see. Comparatively, earnings growth for SEM's portfolio should approach 10%+ for 2016. Companies that generate growing profits are eventually awarded higher valuations; it is as simple as that.

Portfolio changes and highlights

At SEM we believe it is vitally important to identify growth, and that sometimes leads us to make relative decisions among our portfolio holdings. During the quarter we added one new company and said goodbye for now to two holdings.

In December, we added **CBRE Group,** CBG (formerly CB Richard Ellis). CBG is the largest commercial real estate firm and as such benefits from economies of scale. In September, CBG acquired Global Workplace Solutions, a unit of Johnson Controls. Although this will have a short term effect on margins, longer term CBG will benefit from multiyear contracts with more stable, recurring revenue versus some of its historically more cyclical businesses like leasing and sales. We are banking on CBG continuing to gain global market share (45% of revenues are outside the US) as clients benefit from consolidating their property-related contracts under one vendor. Add to that strength in global commercial real estate sales, and CBG should generate double digit revenues in 2015- 2016. We also believe they will improve return on capital from their already strong levels as they gain scale.

During the quarter we sold two of our smaller holdings. One if which we owned for nearly ten years, **Grainger**, GWW and the other we held a much shorter time period than preferred, only ten months **Polaris**, PII. GWW is a terrific company that provides maintenance, repair and operating supplies to businesses and institutions. However, the lackluster economy is flattening demand for its products and causing deflationary pricing which weighs on margins. Separately, it seems a perfect storm hit PII. For several years PII, a leader in the small vehicle market for recreational and industrial use, has been growing both organically and inorganically (acquisitions) while driving continuous incremental improvements in its operations. This past summer PII had to deal with its first operational hiccup in many years with a paint system issue. Initially creating a backlog of unfilled demand, we viewed it as a short term problem with a temporary impact on business results. In October when PII reported its third quarter results, the company stated that off-road vehicles (60% of its total sales) softened slightly even though the company continued to gain share. Meanwhile, motorcycle sales were doing well and growing in excess of industry trends because of its innovative products such as the Slingshot, in spite of the continued backlog from the paint issue. In mid December however, PII announced it had to meaningfully reduce its growth rate for the remainder of 2015 and 2016 as demand for ORV's slows considerably in oil-producing regions (Texas and Western Canada) and snowmobile sales for the season are off to a bad start due to the unusually warm winter. We typically don't sell businesses due to temporary macro economic trends, but it is also our goal to identify and own for long stretches, companies that can perform even in a low growth environment. Both GWW and PII are well managed and continue to earn strong returns on capital, but they are facing enough hurdles at present that we had better choices.

<u>Volatility</u>

In a year in which a 30% decline in oil prices should be welcomed, instead it brought great volatility to the markets not seen since 2011. Observed by *Wall Street Journal* columnist E.S. Browning, through mid December the Dow Jones Industrial Average (DJIA) moved 1% or more on 70 days, nearly twice as many as in all of 2014, and far more than in any year since 2011. While volatility can bring rising anxiety for many, we believe it can bring opportunity, and importantly, volatility does not measure risk. We measure a company's risk by looking at its balance sheet, its business operations and history. Volatility occurs because the markets are open daily. They don't have to be.

Aside from this volatile year we can look at a longer time period of five years and examine two companies. One we have owned for nearly ten years Nike (NKE), and another we don't currently own but had at one time, Coca-Cola (KO). In the table we will show you the low and high price and change for the year. Also, we share the net income as reported by research source *Value Line*.

	Nike Stock Price				Coca-Cola Stock Price			
Year	**Low**	**High**	**% change from low**	**Net Income($M)**	**Low**	**High**	**% change from low**	**Net Income($M)**
2011	$17	$25	41.5%	$2,133	$31	$36	17.3%	$8,932
2012	$21	$29	34.7%	$2,223	$33	$41	22.2%	$9,019
2013	$26	$40	56.2%	$2,464	$37	$43	18.9%	$9,374
2014	$35	$50	42.8%	$2,693	$37	$45	22.0%	$9,091
2015	$45	$67	47.2%	$3,273	$37	$44	19.7%	$8,825

The underlying principle we believe in, is that over time, if the economic profits of the business grow then so too should the stock price. Mission accomplished here! As you can see in the above table, KO has had no growth in its intrinsic profits, so its stock price while higher, has appreciated at a considerably lower rate than NKE which has grown its profits in excess of 50%. The reason why KO trades at a higher price today in spite of flat profit growth is for various reasons that are secondary in this discussion, such as lower share count from stock buybacks and investors' essential belief that profits will increase going forward.

Our main takeaway from the information above is the illustration of the volatility. We can see that in the percentage change in stock price from low to high in a given calendar year. It is staggering. NKE's price swing averaged 40% or so while KO's percentage change was in the 20% range. Both companies "traded" in a wide range; especially when you consider not much changed in their business from day to day. KO makes beverages and NKE makes athletic clothing and footwear. In fact, there has been no fundamental change in what each company offers since their founding. KO is making the same profits it did five years ago and NKE has grown its earnings on average about 11% annually. So where does the daily and yearly volatility emerge from? It all comes from just human emotions, positive or negative towards the stock market. Human emotions reacting to world events or price changes in other markets such as declining oil and commodity prices, cause random stock price movements that can be totally unrelated to business fundamentals.

At SEM we understand that volatility, while not predictable on a daily basis, can present us with opportunity. Each calendar year the market is open roughly 250 days, 7 1/2 hours each day. We actively compare intrinsic value of our businesses and those we don't own but would consider, against daily stock price gyrations. We might have a lot less volatility if the market was open only two days a week instead of five. Could you imagine the pushback of that idea? How would daily news channel CNBC and parts of Wall Street survive? Cutting CNBC's broadcast to two from five days might result in significantly less advertising sales and a lot of Wall Street firms could suffer volume declines of 50% or more. If the market was open only two days instead of five, it would not change how SEM-DIS approaches investing one bit in the long term ownership of good businesses such as Nike.

Looking ahead and behind

The volatility may unfortunately continue. The very sad and terrible events in Paris and California as well as concern about more of them, certainly brings to mind U2's lyrics: "I can't believe the news today, Oh, I can't close my eyes and make it go away." But to invest is to be a hopeful optimist. After all, our country is only approaching 250 years old so it is still a work in progress as it is for many other nations and cultures. Human progress has come a long way, and we are optimists, so to continue with U2's lyrics: "Cause tonight we can be as one."

We have tweaked the **SEM-DIS** process over the years, benefitting from our combined 50+ years of experience, and we will keep looking to improve it. The foundation taught to us by great investors Ben Graham and Warren Buffett, will never change and has stood the test of time: (1) Approach investing in the public market as you would private enterprise, think of yourself as a part owner of the business (2) Incorporate "margins of safety" into the process and (3) Understand that the public stock market is there to serve us and the value of the business is independent of the daily offering price.

Intrinsic value growth for the SEM portfolio outpaced our return in 2015 putting us in a position of a portfolio measurably more attractive from a price to value relationship versus this time last year. As we have often scribed in the past, we have no ability to predict year by year market returns (and we believe no one else can, either). Nor do we believe having that crystal ball is necessary. The **SEM-DIS** focus will always be part ownership of companies with great financial strength and growth profiles that will increase intrinsic value over time. In due time, the public stock market will recognize it as it has since our inception.

At last available measure (September 30th), our rankings among our peers remain strong. In the two categories closest to the general market and what we do, large capitalization growth and large capitalization core, industry source Informa/PSN ranks SEM in the top 6% and 7% respectively since our inception. Meanwhile a more household name, Morningstar, which ranks both mutual funds (which we don't offer at this time) and separately managed accounts (which we do) awards us 4 out of possible 5 stars but measures only the most recent ten years.

Thanks as always for your support and best wishes for a healthy, prosperous and peaceful 2016!

Sincerely,

Don *Amy*

Donald R. Jowdy
President

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Suncoast Equity Management, LLC

Performance results versus the Standard & Poor's 500 Index

Time Period	**SEM % Return***	**S&P 500 % Return**	**SEM - Value of $1,000,000**	**S&P 500 - Value of $1,000,000**
One-Year (2015)	+3.9%	+1.4%	$ 1,038,700	$ 1,013,800
Three-Year	+15.9%	+15.1%	$ 1,556,600	$ 1,525,900
Five-Years	+14.1%	+12.6%	$ 1,936,300	$ 1,807,500
Seven-Years	+14.5%	+14.8%	$ 2,580,600	$ 2,630,200
Ten-Years	+7.9%	+7.3%	$ 2,149,300	$ 2,024,200
Fifteen-Years	+6.5%	+5.0%	$ 2,582,000	$ 2,079,900
Inception (18 Years)	***+8.3%***	***+6.2%***	***$ 4,225,500***	***$ 2,942,400***

* Composite results of all SEM managed accounts, net of all fees.
Note: Performance for the three, five, seven, ten, fifteen and since inception year periods represent the annual average rates of return