Suncoast Equity Management, Inc.

April 2, 2015

Dear Client:

The first quarter is likely a showcase for the rest of the year; volatile stock price movements and uncertain earnings growth. SEM portfolios managed to gain +1.9% vs. +0.9% for the S&P 500. In 2014 from beginning to end, earnings estimates for the S&P 500 were spot on and finished the year with growth at +7%. For 2015, it has quickly become a different story. A few months ago it seemed like the U.S. economy had shifted into high gear. At the beginning of the year estimates called for 8% earnings growth for the overall market (as represented by the S&P 500). Only three months in and that growth rate has been cut in half, in some cases down to an estimate of only 2% for this year. Importantly, the growth forecast for your SEM portfolio, while down a few points, is much higher than the overall market, projected in the +12% range for 2015. We discuss the factors responsible for the dimmer earnings outlook below and provide a portfolio update.

“All about that bass (earnings), no treble”

So what is weighing on earnings for the market overall? The two major culprits are lower energy prices and the strength of the US $. Another factor is a generally flat pricing environment coupled with a slight rise in labor costs.

Weak oil prices have resulted in a major markdown of earnings forecasts for those companies. For these types of companies, earnings are closely linked to the price of the commodity. When you are forced to sell your product at what the market tells you to, and you have no influence on the price, business results can be very volatile. At SEM, we have never owned or in the future plan to consider energy, metals, materials or mining companies. The vast majority of energy businesses don’t meet the **SEM-DIS** (Disciplined Investment Strategy) stringent criteria of consistent free cash flow generators and the businesses typically are too capital intensive for our taste. Notwithstanding, energy and materials stocks have an important weighting in the S&P 500, albeit down to 10% recently because of price declines but at the 15% level one year ago. SEM’s absence in energy can result in our underperformance in the short run, as it did in 2005 and 2006. Back then, energy prices rose quickly from a low $30 per barrel to $85. During those two years, energy, materials and utilities significantly outperformed and drove-up the overall return for the S&P 500 index of +5% and +16%, respectively. We will leave the more commodity price impacted businesses (or price takers) to others and stick with the consistent intrinsic value building companies that have produced our good record approaching twenty years.

Turning our attention toward the pricing environment outside of companies with commodity based products, it is generally flat. At SEM it is currently a mixed state of affairs, with pricing strength at **Nike** (NKE) up 6% in the recent quarter and softening at others, with **Grainger** (GWW) at flat to down slightly. This is an important factor that we keep a close eye on, especially relative to costs. Costs on the labor front are starting to rise with the index up 2.2% over the previous year. Our companies have strong capabilities to maintain and improve operating margins because of their wide-ranging advantages. We are a bit less optimistic that many of the businesses in the S&P 500 can avoid this possible profit squeeze.

Building for nearly eighteen months, the strength of the dollar is an increasing burden for U.S. businesses’ bottom line. For companies with minor exposure to sales outside of U.S. borders, this of course has little to no impact. For those that do 50% or more business outside the U.S., the impact can vary greatly and is dependent on factors such as where goods are manufactured and where they are actually sold. Staying within our own, NKE’s recent quarterly report is a dramatic example. Foreign exchange reduced growth by 5 percentage points and the company expects the negative impact on sales to get worse and head towards 7 percentage points in future quarters. So how does it look for NKE when you put it all together? The mix could look something like +10% range in product demand, +6% in average selling prices, offset by -7% due to foreign exchange for a net growth of +9% in sales. So overall very strong!

Portfolio update

We added one company and sold three of our holdings this past quarter bringing our portfolio total down to nineteen. We also added to one our newer holdings, **Hanesbrands** (HBI) just prior to the company purchasing a complementary brand, Knights Apparel for approximately $200 million. Representing 400 of the largest U.S. colleges and universities, Knights sells t-shirts, sweatshirts and other sports apparel with logos and graphics under various brands including Knights and Russell, primarily to mass merchant retailers. HBI, already a leader with its Gear and Champion brands in the university bookstores, will now have the leading share for licensed collegiate apparel in the mass, mid-tier and bookstore channel. HBI will fold-in Knight, gain manufacturing synergies, and improve the return on capital Knights could not otherwise accomplish on its own. Activewear, in which HBI focuses, is one of the few performing apparel segments in terms of growth and margins.

Polaris (PII) is a recent addition to the portfolio that is also benefiting from adding additional brands to its core offering and gaining scale through acquisitions. Starting with its namesake in snowmobiles back in 1954 and organic extension to all terrain and on-road vehicles, the company is a global leader in the small vehicle market used for transportation (people moving), commercial and government work, and recreation. PII has an organized plan to grow both organically and inorganically. PII's "*Growth through Adjacencies*" objective includes acquisitions such as small French manufacturer Aixam Mega about two years ago that produced $100+ mm in sales as a stand alone business to 400 European Dealers. This deal significantly added to PII's European presence and earlier acquisitions of smaller sized Goupil and GEM (Global Electric Motorcars). Another example is PII's motorcycle brands which began with Victory and then later Indian, through an acquisition back in 2011. The company has been successfully rebuilding the reputation of both through better quality and service. Operationally, PII is perpetually pursing improvements such as shorter lead times, faster inventory turns, and better quality product to drive better financial results. It is opening new facilities to yield faster distribution and lower costs in areas around the globe from Alabama to India. PII benefits directly from an improving economy that supports broad based spending. We believe PII's diversification both globally and by application will give it a less cyclical profile than for example Harley-Davidson, which we have successfully owned in the past. Despite its numerous acquisitions to complement its organic growth, PII carries very little debt on its balance sheet, earns high returns on capital and has a strong record of operating margin improvement.

For SEM it is about making every effort to own companies with relatively brighter growth outlooks. The three companies we sold from the portfolio are solid, and will likely remain so since we only own companies that have great financial strength; however, their outlook may be dimming a bit.

After reducing our position to 2% in December, we sold our remaining shares in **Qualcomm** (QCOM). QCOM may face margin pressure over the next few years due to (1) struggles on the royalty side of its business as the global decline in average selling prices for smartphones accelerates and potentially overcomes unit growth, and (2) increasing percent of total profits coming from its lower margin chip business. Several specific events support these two business trends.

Microsoft is the second technology company we let go of in the quarter. MSFT is making a strong effort to shift its software services to the cloud and is having some success, though it represents only 5% of total sales at present. Our concern, however, is that profit growth for the company overall seems elusive. After growing profits to a peak level within the last two years, this fiscal year ending June 2015 should see a drop-off of approximately 10%. Another uncertainty ahead is once business clients get converted to the cloud, will there be pricing power for MSFT? MSFT's stock price is up about 50% in the last 18 months so it was a worthwhile holding. With this stock price increase though, MSFT's relative value to other choices shrunk. We will continue to monitor MSFT to see if it can return to growth mode.

Finally, we sold **Franklin Resources** (BEN), another significant free cash flow generator like MSFT but facing anemic growth and some pressures on the bottom line. Recent mutual fund flows have been heavily weighted toward ETFs and passive funds, where BEN has little to no exposure. The company's international expansion is putting pressure on margins and the prospect of higher rates later this year may add to weaker bond flows, an important part of BEN's business. We were also disappointed that BEN did not pay out a special annual dividend in December which it has been known to do. While we are not dividend focused, we do believe it is a good practice to return money to the owners when the company has an abundant amount and no immediate strategic need.

Spring arrival

Now that most of the country has made it through a tough winter, we can look forward to spring. We continue to study our companies' (as well as prospective companies') long-term strategies, growth opportunities, challenges and competitive advantages and focus on those companies that can expand their earnings power and compound their intrinsic value. The growth outlook for SEM companies remains solid even in an environment where issues such as the strong dollar will likely continue to pressure earnings growth for the market overall. Our positive relative performance since inception, and through both bull and bear markets, is the result of our keen focus on long-term wealth building businesses. We thank you and are grateful for your confidence.

Sincerely,

Don Amy

Donald R. Jowdy
President

Amy Lord, CFA
Senior Vice President

Suncoast Equity Management, Inc.

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**
First Quarter 2015	+1.9%	+0.9%	$ 1,019,100	$ 1,009,500
One-Year	+12.9%	+12.7%	$1,128,800	$1,127,300
Three-Year	+15.9%	+16.1%	$ 1,555,300	$ 1,565,500
Five-Years	+14.1%	+14.5%	$ 1,929,200	$ 1,965,000
Seven-Years	+9.5%	+8.9%	$ 1,885,000	$1,822,100
Ten-Years	+7.9%	+8.0%	$ 2,135,700	$ 2,161,100
Fifteen-Years	+6.5%	+4.1%	$ 2,587,600	$ 1,840,300
Inception (17 1/4 Years)	***+8.6%***	***+6.4%***	***$4,145,900***	***$ 2,929,800***

* 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