North American Management
Ten Post Office Square, Suite 1200S
Boston, MA 02109
Telephone: 617.695.2100
Fax: 617.695.2121

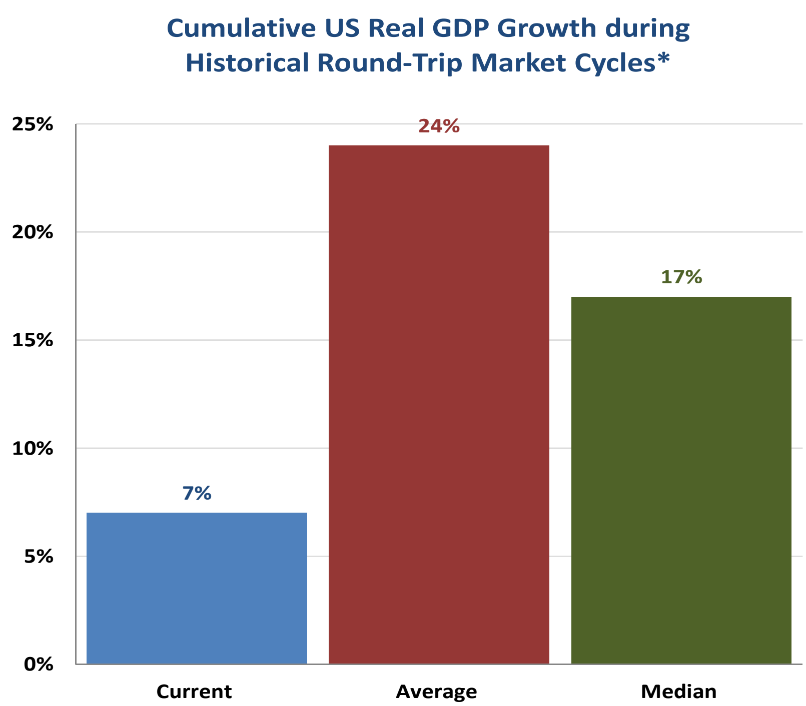
231 S. Bemiston Ave., Suite 800
St. Louis, MO 63105
Telephone: 314.854.1355
www.namcorp.com

First Quarter 2014

A Healthy Rotation

The first quarter ended with modest gains for developed global equities, the MSCI All Country World Index rising 1.2% and the S&P 500 up 1.8%, while the MSCI Emerging Markets Index fell slightly, down 0.5%. However, the quarter was volatile: the S&P 500 dropped 3.5% in January as investors, already selling to rebalance equity exposures after a year of extraordinary gains, were surprised by some very poor employment numbers. The stock markets snapped back in February, up 4.6%, but participants still struggled to weigh the effects of persistent harsh weather, a new Fed Chair, and some deeply unsettling Russian aggression against Ukraine. Although March S&P 500 returns were slightly positive, up 0.8%, the last two weeks of the month saw a pronounced sell off among growth and momentum stocks, with some widely followed tech and biotech names down as much as 25%. From the end of February through April 15, the S&P 500 utilities sector rose 6%, while the Nasdaq Biotech Index dropped 18%. There has been a lot of press about unusually low temperatures interfering with retail shopping, hiring, home and car buying. Could it also be said that $750 billion of new tax increases, an ever expanding regulatory burden, last year's 1% jump in long term interest rates and continued dysfunction in Washington might have something to do with our tepid growth rates? It seems the US stock market has looked past every one of these hurdles, and commentators prefer to talk about the weather.

There is a larger picture to consider, and it helps explain why the US stock market has continued to perform well since 2009 despite sub par GDP growth (see graph right), tapering liquidity and little demand for credit. One can easily argue that managements (more than most politicians) have learned to deal with sluggish economies in ways that benefit their stakeholders. When necessary, balance sheets have shrunk to adjust to lower capacity requirements, expenditures have been delayed and excess capital returned - of particular interest to aging shareholders in need of income. It reminds us of the restructuring that went on in the early 80s as companies recovered from years of damaging inflation. A number of older workers exited the workforce, which was difficult to watch, but ultimately the country was rewarded with higher productivity and higher growth. We are still waiting for the growth dividend from the Great Recession.



Most bull markets, and all bubbles, have a compelling investment narrative that accounts for above average growth rates and aggressive multiple expansion. We all remember "the internet changes everything so valuation no longer matters," or, "the US consumer is going to save the world ," or, "BRIC countries will reorder the global economy," or "houses are a bullet proof store of value." A balance sheet rally that has generated at least $1.6 trillion of corporate cash and historic levels of dividend coverage hardly qualifies, biotech and social media corrections notwithstanding. Meanwhile, there are a number of legitimate growth drivers percolating, not least a powerful domestic energy story that includes significant innovation in alternatives like solar and biofuels. While the cost of labor has been a huge, sometimes painful differentiator, we can begin to picture a global economy wherein the cost of energy will matter more, and here the US has meaningful advantages. We have also been appraising a potential surge in machine to machine (M2M) connectivity that could gain traction in a number of industry sectors including utilities, automobiles, healthcare and software. It seems there is always another wave of productivity and cost advantage through innovation, given enough time and encouragement. Our concerns, stated ad nauseum in previous letters, are more with the credibility of sovereign balance sheets.

Finally, we would like to highlight a recent surge in global mergers and acquisitions (M&A) activity, now $1.3 trillion year to date. As our extraordinary profit cycle peaks at a post WWII high, and growth remains challenged, a new phase of consolidation in pursuit of top line growth is under way. This activity tends to support stock prices, as most managements are willing to pay a premium to eliminate competition or enter new markets. Unfortunately, M&A does not always lead to new employment, as payroll redundancies are eliminated, but at least the pace of new investment and cash deployment is quickening.

Robert G. Scott	**David H. M. Baker, CFA**
Chairman & CEO	*Chief Investment Officer*

Special Note to our Readers: Leicia Chan, Director of Operations, Yuval Ezer, Senior Research Analyst, Mhairi Maclean, Compliance Officer, and Jessica Vacanti, Client Services Manager, have all recently been elected Officers of North American Management Corp. We are pleased to recognize their personal contributions to the Firm's success, and the importance of their roles to our future growth and prosperity.

We would also like to mention an addition to your quarterly reports. We have included attribution summaries for our investment strategies. These summaries are intended to provide a brief description of which holdings most influenced strategy results during the quarter, and will also describe key actions taken during the quarter. We hope you will appreciate this new feature, and we welcome your feedback or suggestions.

**** Data from 1/1/1928 to 12/31/2013. Round-trip: the period from the beginning of a bear market to the end of the subsequent bull market.***
Source of graph: Bloomberg Finance L.P., Bureau of Economic Analysis, Fidelity Investments
Source of data not specifically cited: Bloomberg