

GROWTH EQUITY REVIEW

Second Quarter 2013

PERFORMANCE COMMENTARY

If the old adage that the first day, week, and month of January are all harbingers of things to come, the 2% rally on the first day of the year predicted the first half of 2013. It has been the best first six months of any year since 1999. The broad market, as measured by the S&P500, was up 13.8% through June, and that is after retreating from all-time-highs in late May.

In the second quarter, concerns of the nattering nabobs of negativism shifted as Cyprus (aka European banking crisis) returned to its rightful place in the scheme of things. In late May and June, the Fed became the concern du jour. To say that at some point the Fed will raise rates and that this may happen possibly sooner than some seers predicted seems not to be a cause for concern but rather recognition of progress, albeit in a slowly recovering economy. We believe a slow and steady growing economy provides and has provided fertile fields in which to find outstanding investment opportunities.

This quarter (like the first quarter), the financial and consumer discretionary sectors lead the market, and along with health care were the three leading sectors in the first half of the year. Investors moved away from yield oriented stocks (utilities), which along with materials and energy were the laggards for the quarter, all posting negative returns.

Despite no exposure to the financial sector and very limited exposure to the consumer discretionary sector, we had a very good quarter and continued to significantly outperform the indices in the first half of the year.

	Periods Ending June 30, 2013						
	QTR	YTD	1 Yr	3 Yrs	5 Yrs	7 Yrs	10 Yrs
Growth Equity - NET	4.1	16.1	21.2	18.7	8.4	7.5	9.8
Russell 3000 Growth Index	2.2	12.2	17.6	18.8	7.6	7.0	7.6
S&P 500 Index	2.9	13.8	20.6	18.5	7.0	5.7	7.3

Composite performance is reported NET of fees and expenses. Please refer to the disclosures at the end of this report.

Performance figures for periods one year and longer are annualized.

Scientifically focused companies, with the exception of one holding, had the greatest impact on returns for the portfolio at both ends of the spectrum. **Morphosys (MPSYF)**, a European biotech company, was up 38% without a major announcement of milestones or achieving new product approval. The significant increase was due to investor recognition of the advances made over previous years and the potential rewards generated by scientific discovery. **Boeing (BA)** was up 20% while **Vertex Pharmaceuticals (VRTX)** was up 46% based on continued progress treating cystic fibrosis and hepatitis C. **Google (GOOG)** was up 11% and **STEC (STEC)** was acquired and up 56% (please refer to the portfolio activity comments for greater detail).

Detracting from the quarter's performance, **Computer Sciences (CSC)** (up 25% last quarter and one of our larger positions) was down 11% this quarter. Two medical device companies, **Hansen Medical (HNSN)** and **Biolase Technology (BIOL)** were down 29% and 9% respectively. **Universal Display (OLED)** and **Apple (AAPL)** were both down 10%.

PORTFOLIO ACTIVITY

Late in the quarter STEC, was acquired in a cash deal by Western Digital (WDC). While the bid price was almost a double from the prior closing price, from an investment opportunity perspective it was still a disappointing return on our investment. STEC had not met our expectations and at \$3 the stock price reflected such. We had continued to hold the stock because there was little downside from \$3, the Company had significant technology and capabilities, and we thought a larger company would certainly acquire it for a premium.

We used the proceeds from the sale of STEC to increase our exposure to three existing holdings: **Cisco Systems (CSCO)**, **Express Scripts (ESRX)** and **Qualcomm (QCOM)**.

MARKET COMMENTARY

One could substitute "economy" for "justice" in the adage "the wheels of justice grind slowly but finely" and have an accurate depiction of where we are today. And so the wheels turn. We have written recurrently over the past that we are in slow growth recovery mode and that the fundamentals are in place for a very good market.

Rarely has there been so long an unrelenting general advance, certainly not an uptrend denied so much by so many throughout. For some persons, acrophobia set in early, and the talk and chant soon commonly seemed to express "look out, there is a long way to fall from here." (As an unintended consequence, denial has been a sustaining and extending factor.)

Only a few seemed to perceive that the physical aspects surrounding the stock market were uncommonly propitious all along the way, and are still so at present. When physical attributes are stronger than visceral personal attitudes, bet on the physical - demonstrated so recurrently in recent years as market contractions were held to fractions of market advances. Too few investors perceive our stock market in terms of fundamental money flow to or from the market. Only a minority recognize this to be the source of continuing support to rising share valuations for most established worthy enterprises.

The self regenerative forces in the American economy became effectively evident more than two years ago. When Mr. Bernanke recently commented (June 19) that stimulus-evoked buying by the Federal Reserve of US Treasury securities would probably be phasing out in months to come, the market spontaneously reacted as though this was an important denouement. Notwithstanding this was an obvious matter for months past, traders (short term) slammed the market, though quite opposite to the deeper, constructive meanings for the longer term.

The stimulus this country has needed (since the rescue from the consequences of mammoth financial misdeeds) is for governments to just get out of the way of private industry. And so it is also for certain other nations. The nations that are growing rapidly give support to their industries, while some others growing too slowly, including America, penalize their industries. Only a few days ago, a major journal remarked regarding what is Germany to do to recreate health in the Euro zone. A simplistic (but earnest) suggestion is just to get out of the way of their excellent enterprises and let these solve the problems naturally, as contrasted via national budgets and taxation.

The simplest, most obvious and least appreciated, of observations is that valid enterprises have been pulling the world ahead in recent years, while governments seem to be impediments. Just get out of the way - please - would be an effective policy (with the exception of addressing the unmet necessity to deal with aspects of financial entities).

If the American stock market be visualized in context of flows of funds out of a widely dispersed abundance of money, our list (with many omissions) would emphasize:

- overflowing corporate tills to buy in their own shares, to make strategic acquisitions (usually at premiums to market prices) as well as to buy money market instruments, and to increase dividends
- monies outflowing from bond investment prompted by increased awareness that investment-grade bonds have been and are lose-lose investments — lose vis-à-vis alternative secure dividends at several hundred basis points higher returns, and lose on principal as interest rates normalize higher and erode principal valuations (but not severely higher regarding the economy)
- the bubble of investing in commodities has reversed and looks to continue to do so. Since 2004 when commodities gained status as an asset class more than \$440 billion has flowed into index funds and ETFs tracking broad commodity indexes while only \$25 billion has been invested in U.S. stock funds. Much of this outflow will be directed towards equities.
- reallocations of monies formerly invested in shares still isolated for sake of safety that seems to be returning in increasing flow as encouraged by further advances in share prices generally
- inflows originating beyond American borders, encouraged by newly supportive developments for the dollar and by favorable (all things considered) valuations of American shares compared to their native shares, or shares in other nations

Money typically flows where it is best served.

Speaking in physical terms, the American stock market cannot accommodate such inflows at today's valuations. This is simply arithmetical; only higher prices that enlarge the total valuation can accommodate such volume. This explains much of the past several years, and prospectively many months hereafter.



DISCLOSURES: The Growth Equity Composite is comprised of discretionary, separately managed taxable and tax-exempt equity accounts managed for growth. Results are calculated internally using Advent portfolio accounting software. Accounts are included in the composite at the beginning of the first full calendar month in which the account is fully reflective of the investment strategy. Composite returns are weighted for the size of each underlying account and are reported net of fees and commissions. Results for individual accounts may vary due to the timing of investments, size of positions, fees, and other reasons. Client returns may be reduced by other expenses incurred in the management of the client's portfolio. Composite and index performance valuations and calculations include dividends, interest and other earnings and are stated in US dollars. All performance figures for periods one year and greater are annualized. The S&P 500 Index is an unmanaged index generally considered to be representative of the U.S. stock market as a whole. The Russell 3000 Growth Index is an unmanaged index constructed to provide a comprehensive, unbiased, and stable barometer of the growth segment of the broad U. S. stock market. Additional information regarding policies for calculations and reporting returns is available upon request. PAST PERFORMANCE SHOULD NOT BE CONSTRUED AS A GUARANTEE OF FUTURE PERFORMANCE. The specific securities identified and described do not represent all of the securities purchased, sold, or recommended for advisory clients, and the reader should not assume that investments in the securities identified or discussed were or will be profitable. The stocks named as the top or bottom five contributors to performance for the period are based on a representative portfolio (Princeton Capital's oldest Growth Equity wrap account portfolio; also a member of the Growth Equity composite) and have been identified through a report generated by Princeton Capital Management's Advent portfolio accounting system. Further detail on the contribution to performance calculation, which takes into consideration the weighting of every holding in the representative account, as well as a list showing every holding's contribution to performance for the period, is available by contacting Princeton Capital Management at info@pcminvest.com.