The Investment Letter

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"Know what you own, and know why you own it." *- Peter Lynch*

For as long as investing has been around, so too has the tendency to buy 'hot' investments. This natural human desire for inclusion and fear of being left out has led investors to make poor choices time and time again. Examples include tulip mania in 17th century Holland, irrational exuberance and the 'new economy' in technology stocks in the late 1990's and even the housing bubble that caused the most recent recession.

As investors have gotten more sophisticated, and with the increased computing power available now compared to just a few decades ago, tech stocks and tulips have been replaced with complex hedge funds, algorithms and proprietary trading models.

Remember bell-bottom jeans? They were quite popular for a while in the 70's. Today, they are little more than a footnote in fashion history while the original design of Levi's jeans has stood the test of time for well over 125 years. Some of the above listed strategies are much the same - a passing fad.

Hedge funds are the latest hot strategy to take a big hit in the news recently. The California Public Employees' Retirement System, better known as CalPERS recently announced it would eliminate all hedge funds from its holdings. This comes on the heels of a May 2014 announcement that CalPERS' hedge fund allocation would be halved.

CalPERS decision on the matter is not immaterial. CalPERS is a barometer of sorts in the investment industry. Along with being the largest public pension fund in the United States with over 2600 employees, 1.6 million beneficiaries and over $300 billion in assets as of June 30, 2014, they are also recognized as a global leader and an extremely active and powerful shareholder body. In short, CalPERS decisions are not only felt but also often imitated.

Hedge funds have gained a tremendous amount of popularity because of promises of high returns and low risk. They're attractive to the hedge fund manager as they generate exceptionally high fees, participate up to 20% in gains and have little regulatory oversight. Exactly the same reasons that make them attractive to hedge fund managers should make them un-attractive to clients.

Since 1929 Investment Counsel has employed the same basic strategy in selecting stocks and bonds and building portfolios. Our investment approach is fundamental in nature, based on facts about the underlying security. It's an approach that has worked well over our 85-year history and has been discussed in some of the most influential books ever written on the topic of investing, such as The Intelligent Investor (Benjamin

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Graham, 1949) and Security Analysis (Benjamin Graham and David Dodd, 1934).

There are two differentiators that make our strategy superior to investment strategies like hedge funds: cost and complexity. A less expensive strategy leaves more earnings for the investor to grow over time. While a simpler strategy is easier to understand and can limit mistakes.

When considering an unproven, illiquid, complex and expensive investment strategy that cannot divulge its holdings or investment process versus a simple, transparent and inexpensive strategy with an 85-year track record of success the answer should become clear. CalPERS has experimented with the hedge fund fad and has decided it was too high a price to pay for what amounts to bellbottoms.

For more information:
http://youtu.be/uj9yGYDnxmM

Outlook for Stocks

Investment Counsel continues to be cautiously optimistic on stocks. Even though many stocks have been hitting new highs, we feel that the valuations are not only justified but have the potential for further growth particularly if companies can continue to grow revenue as expected. Many indicators (consumer confidence, consumer spending, unemployment) point toward further gains in the equity markets.

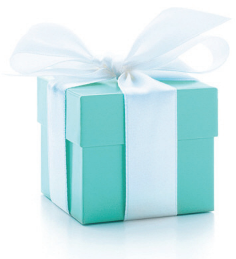
Outlook for Bonds

We expect interest rates to rise, which will decrease bond prices. While bonds are still a critical component of most portfolios, providing invaluable diversification and risk management, some types of bonds are more sensitive to interest rate changes than others. Highly sensitive bonds should be adjusted accordingly to limit downside risk from rising rates.

We recently adjusted our bond holdings to limit the impact of rising interest rates. By shortening the average maturity, we were able to decrease interest rate sensitivity. Also, by accepting slightly lower credit quality, the overall yield on portfolios remained relatively unchanged but with an overall lower expected level of volatility due to interest rate fluctuations.

Investment Counsel News

Inside the Office



We've recently added Tiffany & Co. to our recommended list. Tiffany (Ticker: TIF) is a luxury goods designer, manufacturer and retailer that sells their products through both their website and retail locations. Tiffany and Co. was founded in 1837 and is headquartered in New York City.

Outside the Office

On a camping trip, canoeing down the Au Sable river with his dog, Bogle; Mike learned that pets can, and sometimes do, experience motion sickness.