



## Quarterly Review

*December 31, 2013*

# City of Ormond Beach Pension Plans

Presented by:

Sawgrass Asset Management, L.L.C.  
(904) 493-5500

**Marc Davis, CFA**  
Equity Portfolio Manager

**Gregg Gosch**  
Client Service

# For Today's Meeting

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-  Market Review
-  Account & Performance Summary
-  The Sawgrass Investment Philosophy
-  Current Portfolio Positioning



# Sawgrass Asset Management - By the Numbers

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- 100** Percent Employee-Owned
  - 20** States in which Sawgrass Represents Clients
  - 20** Average Years of Investment Experience for Our Team
  - 16** Years Serving Our Institutional Clients
  - 3.3** Billion in Assets Under Management
  - 0** Equity Team Departures Since Inception
- 

## *Sawgrass Mission Statement to Employees and Clients:*

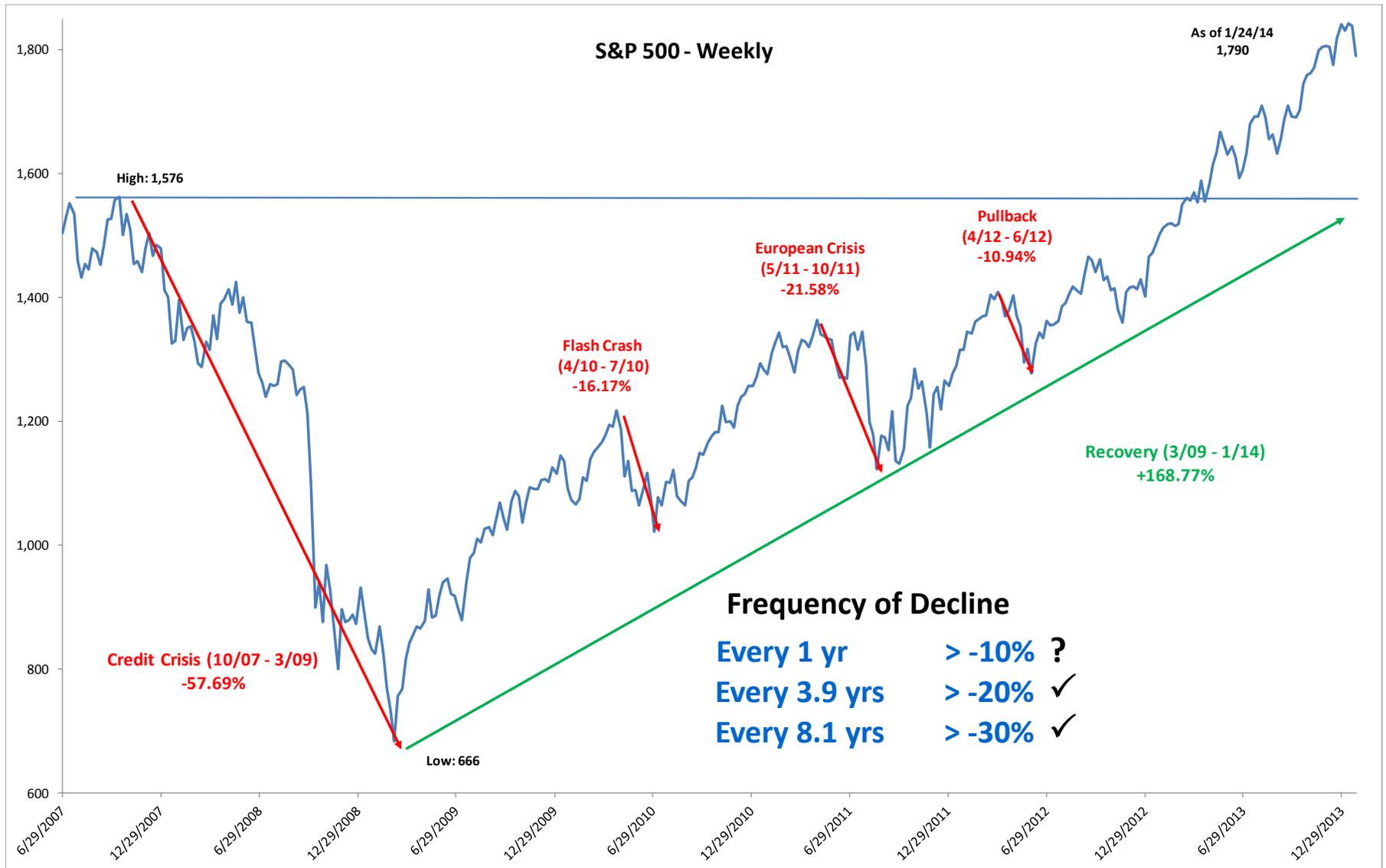
To strengthen the financial security of our clients through active management of high quality portfolios producing strong long term investment results. Our relationships are driven by our core values of integrity, respect, hard work, and ethical behavior.

*Information as of December 2013.*

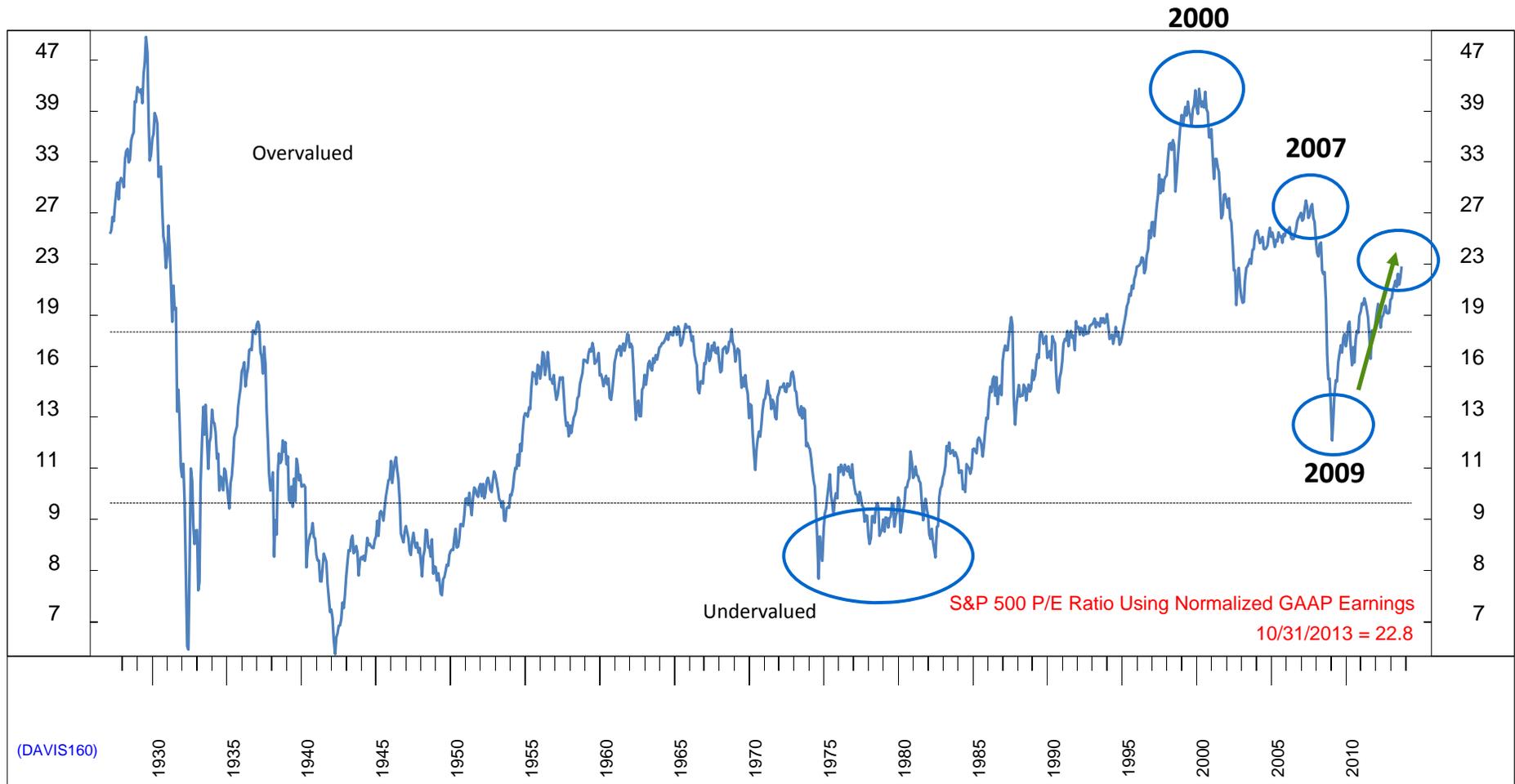




# What a Wild Ride! The Past 5 Years



# Stocks Modestly Overvalued on P/E Basis

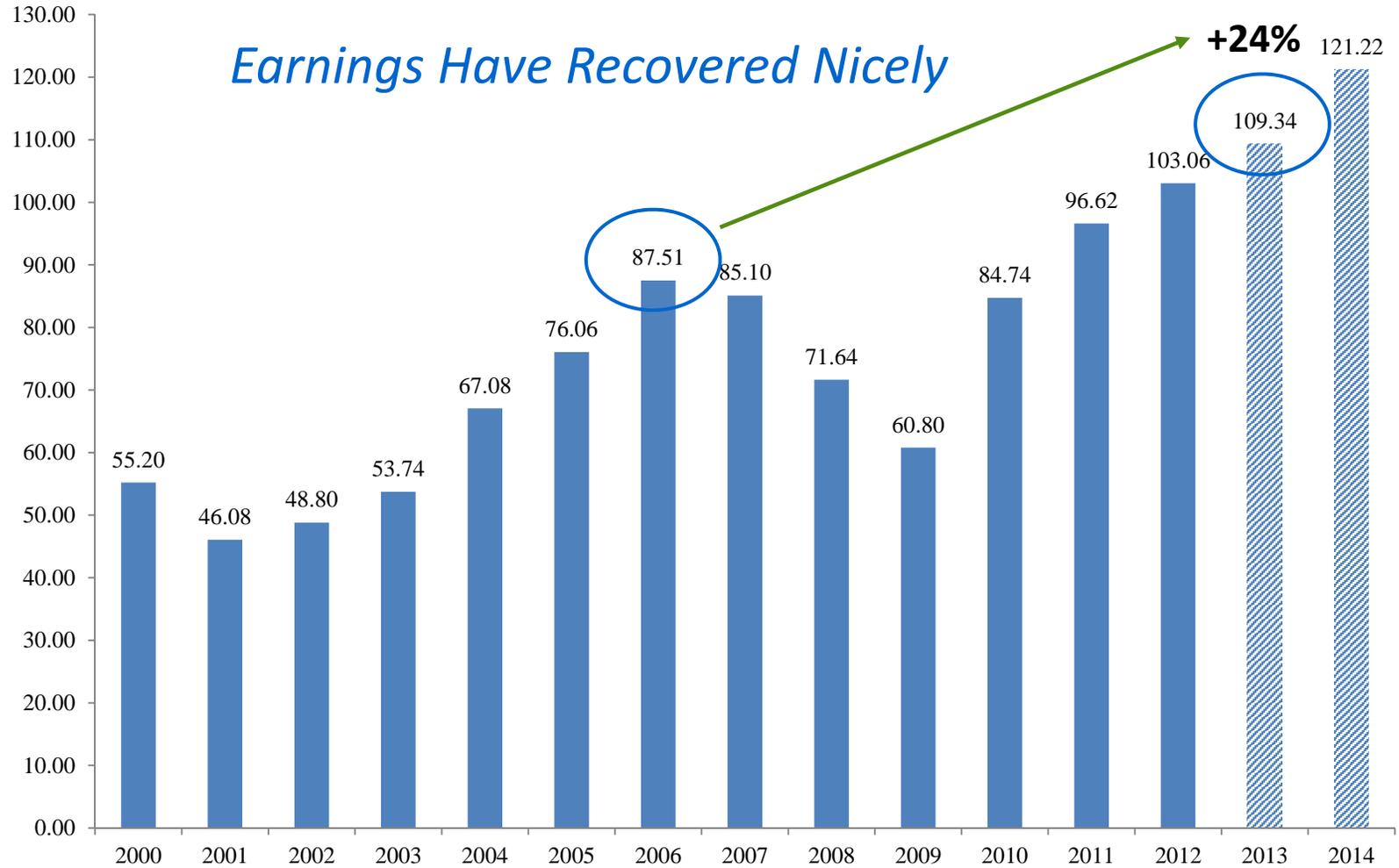


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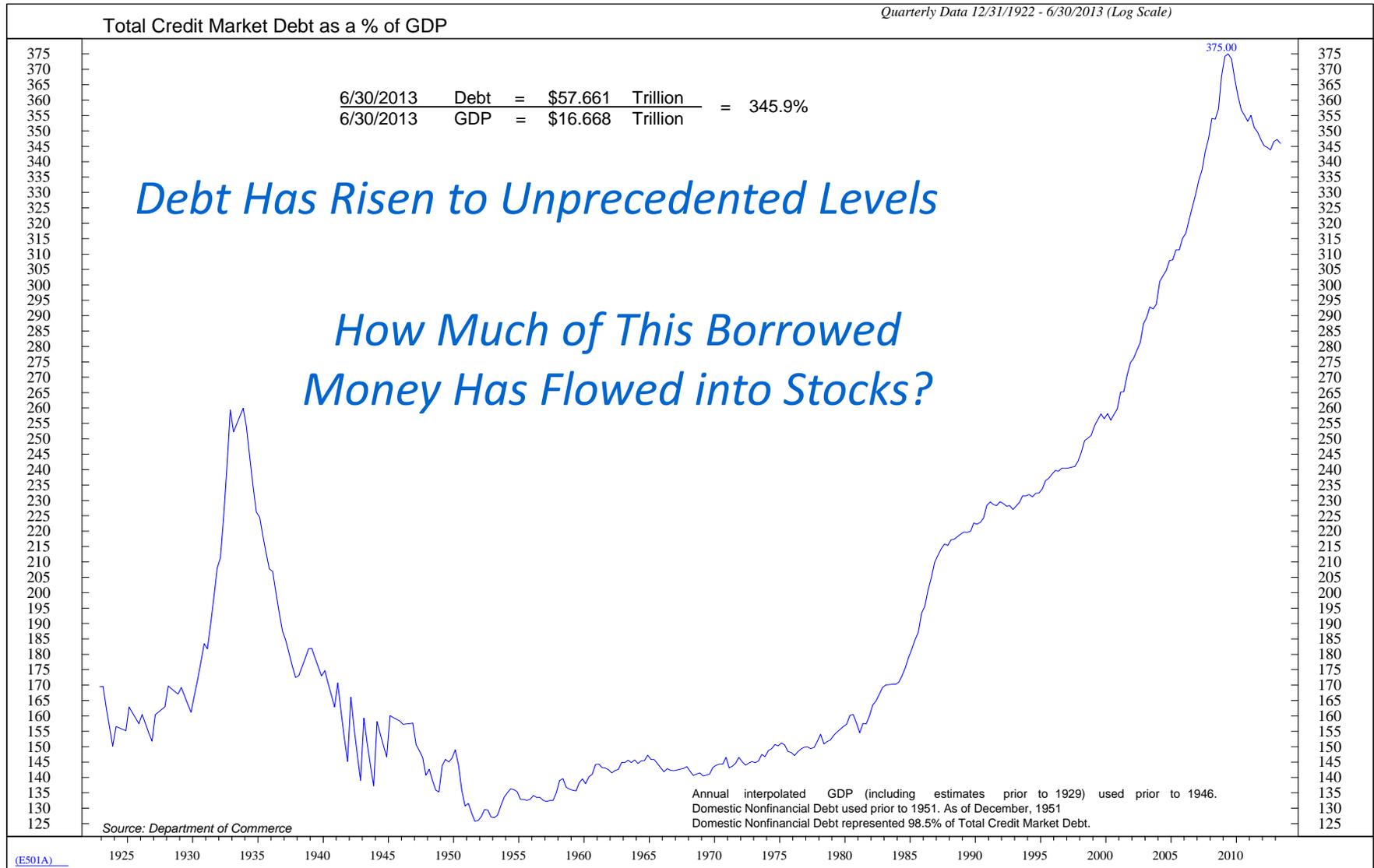
# S&P 500 Earnings



Calendar Year Bottom-Up EPS Actuals & Estimates

\*Source: Factset Research.

# A Mountain of Debt



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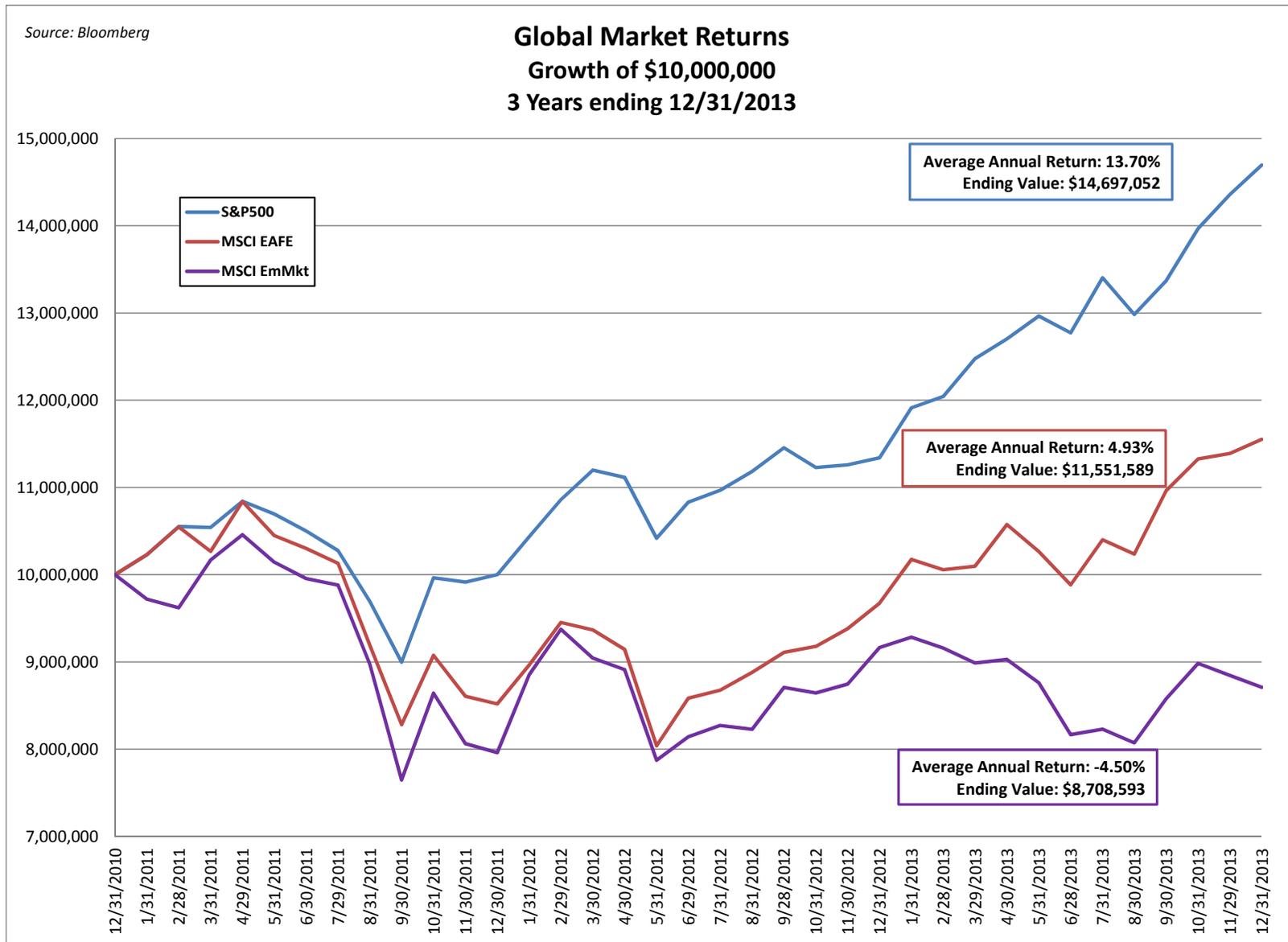
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# What Happened to Fear Factor?



# “Don’t Forget About U.S.”



# Sawgrass Diversified Large Growth Equity – 4Q13 Portfolio Review/Outlook

## **Market Review: Gangbuster!**

- WOW! The stock market closed the year with a flourish posting a 10.7% (S&P 500) for the quarter and a spectacular 32.6% for the year, the best since 1997.
- It is hard to put a finger on the source of the strength but clearly investors were willing to pay more for stocks as prices rose faster than earnings. For the year, S&P earnings gained an estimated 12%-14% vs. a price of increase 32+%. This resulting multiple expansion also comes in the face of rising interest rates for the year and caps off an average yearly gain over the last 5 years of 18% (S&P 500).
- U.S. stocks have also been the clear winner over international stocks not only for 2013 but for the last 3 years. It is interesting to note that despite domestic returns more than doubling the results of the international markets since 2010 (3 year annualized returns: S&P 500 16.5% vs. MSCI EAFE 8.7% and MSCI Emerging Markets -1.7%), investors continue to increase allocations to foreign markets.
- The fourth quarter was a period that favored growth stocks and large cap companies as they outperformed small cap and value stocks. The best performing sectors had a cyclical flavor as Materials, Tech and Discretionary led while Utilities, Telecom and Energy lagged. For the year, small caps led along with Discretionary and Healthcare sectors.
- The quarter and the year had an interesting dichotomy as some risk factors such as higher Beta and smaller size helped while a value orientation helped as well. Generally the quarter and the year were tilted to more “risk on” factors but not to the extent one might expect in such a strong year.

## **Portfolio Review: Besting a Strong Market**

- In a very strong environment for large growth stocks, we were pleased to outperform the Russell 1000 Growth index for both the quarter and year. Given our focus on controlling portfolio risk and bias toward stable growth companies, we have historically found these types of markets challenging.
- An analysis of what contributed to our outperformance for the quarter and year shows that we primarily added value with our stock selection. Our factor tilts were modestly negative, but our success in selecting relatively strong stocks among the stable growth universe pushed us ahead of the benchmark. Examples are GOOG, MKC, CVS and AAPL for the quarter.
- One other positive aspect of our returns this year was the ability to avoid significant losers. In such a strong year, losers are hard to overcome, and we were fortunate to navigate our way around them.
- While our less risky profile usually would be challenged in such a strong year, this year was different. Given that we are 5 years into a strong bull market, investors seemed more risk conscious as evidenced by the solid performance of valuation factors and low volatility. These ARE the markets that favor our risk conscious approach. It just happened to be in a year where stocks were up 30+%.



# Sawgrass Diversified Large Growth Equity – 4Q13 Portfolio Review/Outlook

## ***Outlook: Cautiously Optimistic***

- As we look forward, we must look back and admit that we never would have forecast such a strong year in 2013. Statistically great years are followed by good years, +10% on average.
- That being said, it has been more than 18 months since stocks have seen any type of meaningful correction. History would suggest that we are overdue for a pullback of 10% or more. This does not mean that we can't end the year higher, but we shouldn't be surprised by more volatility than 2013.
- We can offer just as many positives (better economy, improving housing market, US energy independence) as we can negatives (less favorable valuations, slowing earnings growth, rising interest rates) but we would be surprised to see a 2013 repeat.
- After last year we may relinquish our crystal balls. We are however optimistic about the prospect of our portfolios. Given the challenges ahead and age of this market cycle, we like the prospect of our stable growers in a risk aware world.
- AND if we are wrong and we get another gangbuster market, last year demonstrates that we can have some fun in such an environment.

## ***Sawgrass Composite Portfolio versus Russell 1000 Growth (as of 4<sup>th</sup> Qtr 2013):***

### ***What Helped:***

Stock Selection  
Low Volatility Bias  
Favorable Valuation Bias  
No Torpedoes

### ***What Hurt:***

Lower Beta Bias





## Portfolio Market Values

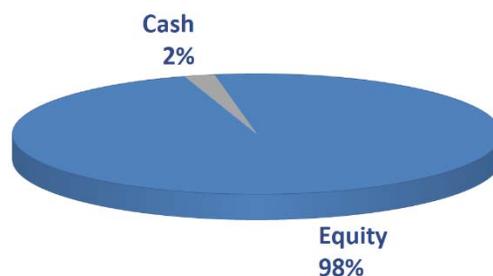
### Change in Portfolio Value

<b>Beginning Market Value on 09/30/13</b>	<b>2,560,420</b>
Cash Additions	0
Cash Withdrawals	-3,723
Investment Gain/Loss	283,221
<b>Ending Market Value on 12/31/13</b>	<b>2,839,918</b>

## Portfolio Summary

<u>Asset Class</u>	<u>Market Value</u>	<u>Percent of Assets</u>
Cash	\$ 68,266	2.4%
Equity	\$ 2,771,652	97.6%
<b>TOTAL</b>	<b>\$ 2,839,918</b>	<b>100.0%</b>

## Asset Allocation





## Portfolio Performance



	Q4 2013	2013	1 Year	Since Inception Annualized*
<b>TOTAL PORTFOLIO</b>	<b>11.1%</b>	<b>35.0%</b>	<b>35.0%</b>	<b>20.5%</b>
Russell 1000 Growth	10.4%	33.5%	33.5%	19.6%
S&P 500	10.5%	32.4%	32.4%	21.1%

\* Since Inception 4/25/12

Returns are gross of investment management fees



## Portfolio Market Values

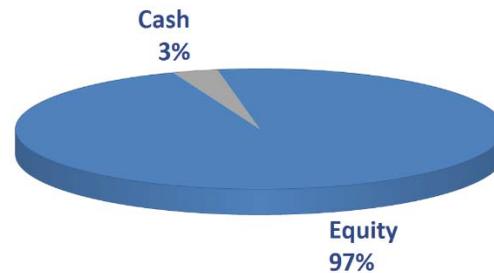
### Change in Portfolio Value

<b>Beginning Market Value on 09/30/13</b>	<b>4,528,037</b>
Cash Additions	0
Cash Withdrawals	-6,584
Investment Gain/Loss	514,251
<b>Ending Market Value on 12/31/13</b>	<b>5,035,704</b>

## Portfolio Summary

<u>Asset Class</u>	<u>Market Value</u>	<u>Percent of Assets</u>
Cash	\$ 139,827	2.8%
Equity	\$ 4,895,878	97.2%
<b>TOTAL</b>	<b>\$ 5,035,704</b>	<b>100.0%</b>

## Asset Allocation





## Portfolio Performance



	Q4 2013	2013	1 Year	Since Inception Annualized*
<b>TOTAL PORTFOLIO</b>	11.4%	35.7%	35.7%	20.7%
Russell 1000 Growth	10.4%	33.5%	33.5%	19.6%
S&P 500	10.5%	32.4%	32.4%	21.1%

\* Since Inception 4/25/12

Returns are gross of investment management fees



## Portfolio Market Values

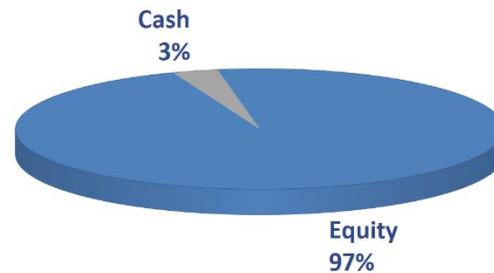
### Change in Portfolio Value

<b>Beginning Market Value on 09/30/13</b>	<b>3,090,578</b>
Cash Additions	0
Cash Withdrawals	-4,494
Investment Gain/Loss	353,729
<b>Ending Market Value on 12/31/13</b>	<b>3,439,814</b>

## Portfolio Summary

<u>Asset Class</u>	<u>Market Value</u>	<u>Percent of Assets</u>
Cash	\$ 87,130	2.5%
Equity	\$ 3,352,684	97.5%
<b>TOTAL</b>	<b>\$ 3,439,814</b>	<b>100.0%</b>

## Asset Allocation





## Portfolio Performance



	Q4 2013	2013	1 Year	Since Inception Annualized*
<b>TOTAL PORTFOLIO</b>	11.5%	35.9%	35.9%	20.9%
Russell 1000 Growth	10.4%	33.5%	33.5%	19.6%
S&P 500	10.5%	32.4%	32.4%	21.1%

\* Since Inception 4/25/12

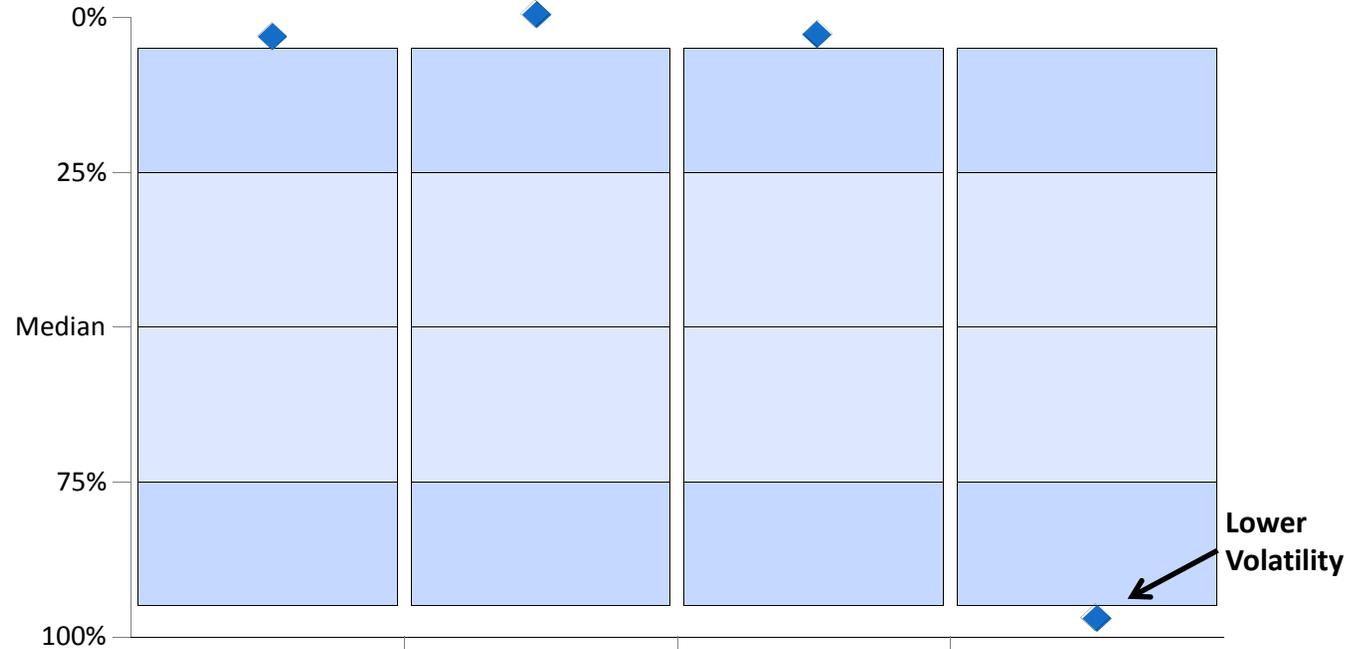
Returns are gross of investment management fees

# Sawgrass Diversified Large Growth Equity Peer Ranking

## Top Ranked Risk-Adjusted Returns with Less Volatility

◆ Diversified Large Growth Equity

3 Years As Of: December 31, 2013



	Information Ratio <sup>1</sup>	Sharpe <sup>2</sup>	Alpha <sup>1</sup>	Standard Deviation
◆ Diversified Large Growth Equity	0.88	1.81	4.95	10.54
Rank	4	1	3	96

*Information Ratio* – a measure of the value added per unit of active risk by a manager over an index

*Sharpe Ratio* – a measurement of efficiency utilizing the relationship between annualized risk-free return and standard deviation

*Alpha* – is the extra return of a product due to non-market factors

*Standard Deviation* – a measure of the historical volatility of a products returns

<sup>1</sup> Russell 1000 Growth, <sup>2</sup> Citigroup 3-Month T-Bill

Source: eVestment Alliance using monthly calculations, Large Cap Growth equity universe as of 12/31/13.



## Contribution to Return

<b>Top 10 Performers</b>	<b>Ending Percent Of Total</b>	<b>Price Change %</b>	<b>Contribution To Return</b>	<b>Bottom 10 Performers</b>	<b>Ending Percent Of Total</b>	<b>Price Change %</b>	<b>Contribution To Return</b>
APPLE INC	5.0	17.7	1.08	SCHLUMBERGER LTD FOREIGN ORD	1.5	2.0	0.04
GOOGLE INC CL A	4.3	27.9	1.06	MOTOROLA SOLUTIONS INC COM NEW	0.0	13.7	0.03
MCKESSON CORP	1.7	25.8	0.71	INTERNATIONAL BUS MACH COM	1.0	1.3	0.03
CVS/CAREMARK CORP	2.8	26.1	0.67	COSTCO COMPANIES INC COM	1.6	3.3	0.02
MASTERCARD INC CL A	2.1	24.2	0.65	STERICYCLE INC COM	2.3	0.7	0.02
ORACLE CORPORATION	4.0	15.3	0.56	SOUTHWEST AIRLS CO COM	1.0	29.4	0.00
DIRECTV COM	3.0	15.5	0.45	MICROSOFT CORP COM	0.0	12.4	0.00
QUALCOMM INC COM	3.8	10.3	0.39	EMC CORP/MASS	3.0	-1.6	-0.01
TJX COS INC NEW COM	1.7	13.0	0.35	PETSMART INC COM	1.3	-4.6	-0.01
ABBOTT LABS COM	2.4	15.5	0.34	KROGER CO	2.5	-2.0	-0.06

*\*Diversified Growth Equity Composite Data*



## Portfolio Characteristics

	Portfolio*	Russell 1000 Growth
1 Yr Forecast EPS Growth (FE)	11.5	12.7
PE LTM (FF)	20.6	23.4
Price to Cash Flow	14.1	16.1
Price to Sales	3.1	3.7
Price to Book	4.7	5.6
Weighted Average	131.1	101.1
# of Securities	42	625

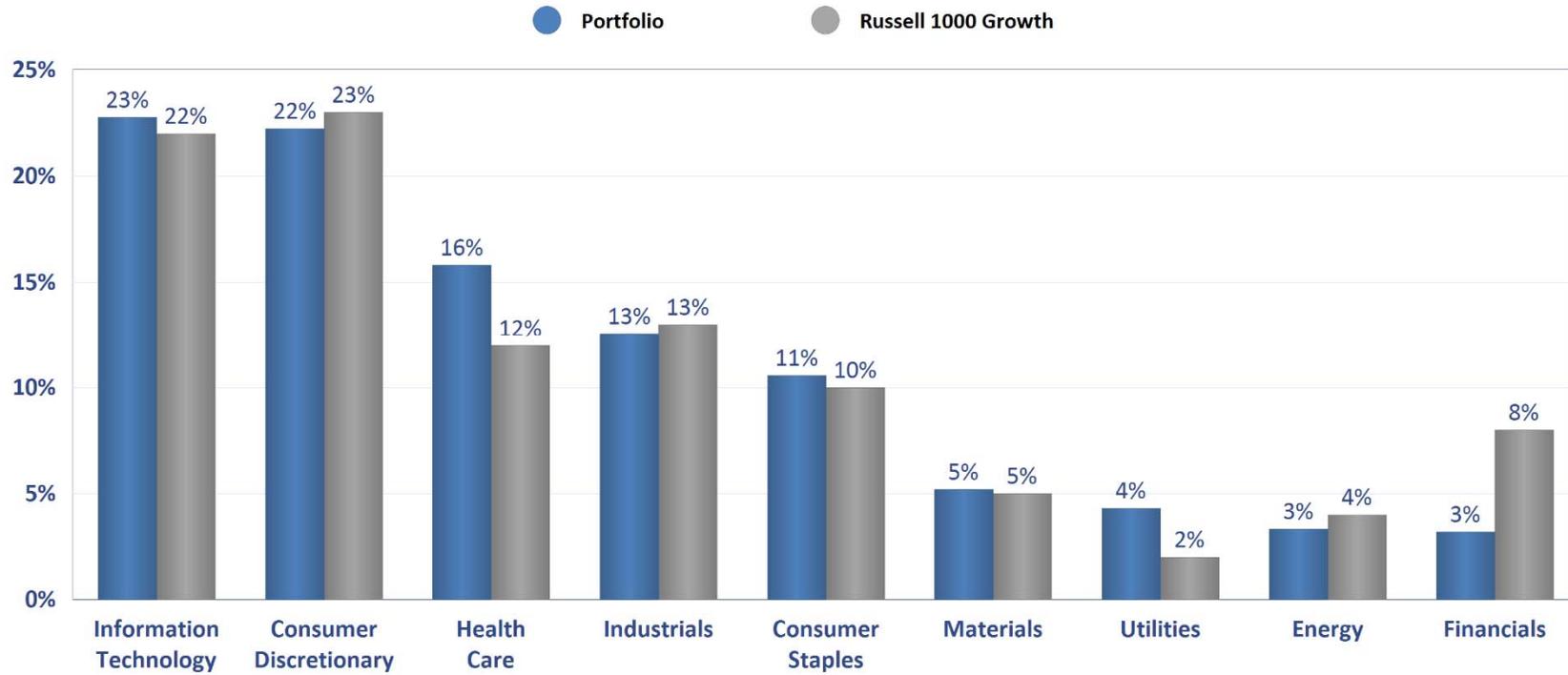
## Top 10 Holdings

<u>Ten Largest Holdings</u>	<u>Percent of Equity</u>
Apple Inc	4.58%
Google Inc Cl A	4.58%
Verizon Communications Com	4.32%
Comcast Corp New Cl A	4.25%
Oracle Corporation	3.99%
Qualcomm Inc Com	3.87%
Wal Mart Stores Inc Com	3.70%
Coca Cola Co Com	3.38%
Amgen Inc Com	3.26%
Emc Corp/Mass	3.01%
<b>TOTAL</b>	<b>38.94%</b>

*\*Diversified Growth Equity Composite Data*



## Sector Breakdown





## Portfolio Attribution

### Attribution Analysis of Diversified Large Growth Equity Composite Vs Russell 1000 Growth - Quarter

	Diversified Large Growth Equity Composite			Russell 1000 Growth			Variation			Attribution Analysis		
	Average Weight	Total Return	Contribution To Return	Average Weight	Total Return	Contribution To Return	Average Weight	Total Return	Contribution To Return	Allocation Effect	Selection Effect	Total Effect
Consumer Discretionary	21.81	9.97	2.17	22.74	9.82	2.22	-0.93	0.15	-0.05	0.02	0.04	0.06
Information Technology	21.02	14.74	3.04	22.14	12.62	2.75	-1.12	2.12	0.29	0.01	0.41	0.41
Health Care	15.25	12.23	1.85	11.98	11.13	1.33	3.28	1.11	0.52	0.01	0.17	0.18
Industrials	11.67	8.21	0.99	12.34	11.58	1.42	-0.67	-3.38	-0.43	-0.01	-0.35	-0.36
Consumer Staples	9.78	12.65	1.24	10.52	7.58	0.82	-0.75	5.07	0.42	0.03	0.46	0.48
Materials	5.18	8.48	0.45	5.42	10.20	0.55	-0.24	-1.72	-0.10	0.00	-0.08	-0.08
Cash	4.32	0.01	0.00	0.00	0.00	0.00	4.32	0.01	0.00	-0.49	0.00	-0.49
Financials	4.10	23.39	0.89	8.28	13.18	1.09	-4.18	10.22	-0.20	-0.12	0.38	0.26
Utilities	3.68	6.49	0.24	1.88	7.10	0.14	1.80	-0.60	0.10	-0.06	-0.02	-0.08
Energy	3.19	10.41	0.33	4.70	1.86	0.11	-1.51	8.54	0.23	0.12	0.26	0.39
<b>Total</b>	<b>100.00</b>	<b>11.21</b>	<b>11.21</b>	<b>100.00</b>	<b>10.43</b>	<b>10.43</b>	<b>0.00</b>	<b>0.78</b>	<b>0.78</b>	<b>-0.49</b>	<b>1.27</b>	<b>0.78</b>

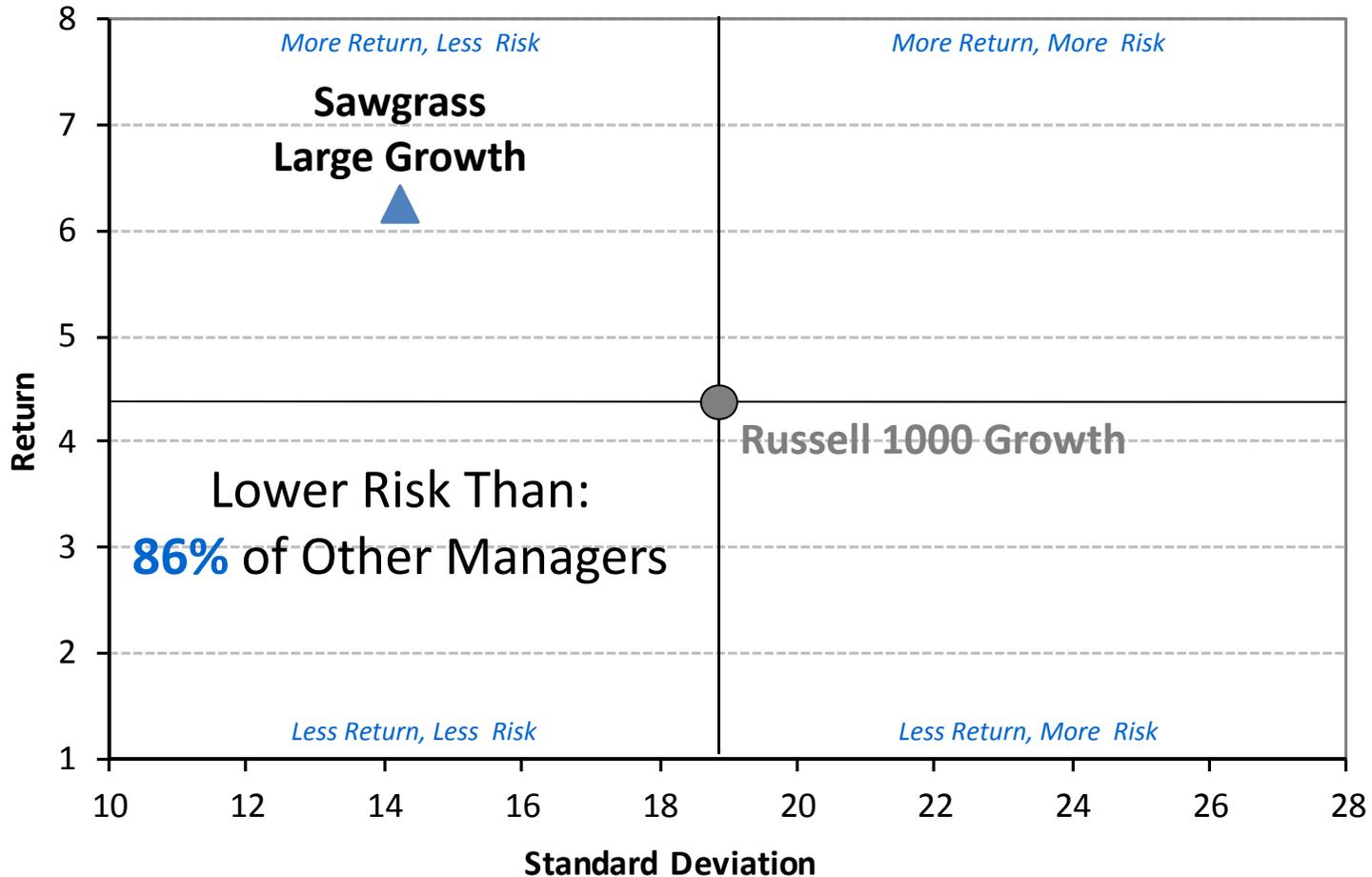
*\*Diversified Growth Equity Composite Data*



<u>Portfolio Holdings</u>	<u>% Weight</u>	<u>Portfolio Holdings</u>	<u>% Weight</u>	<u>Portfolio Holdings</u>	<u>% Weight</u>
<b>Consumer Discretionary</b>		Mckesson Corp	1.6		
Autozone Inc Com	2.9	Express Scripts Holdin	2.7		
Comcast Corp New Cl A	4.2	Johnson & Johnson Com	2.4	# of Securities	42
Costco Companies Inc C	1.7				
Directv Com	3.0	<b>Industrials</b>			
Home Depot Inc Com	1.8	Honeywell Intl Inc Com	1.5		
Petsmart Inc Com	1.2	Danaher Corp Com	1.7		
Tjx Cos Inc New Com	1.7	Union Pac Corp Com	2.1		
Viacom Inc Cl B	2.1	United Parcel Service	1.1		
Wal Mart Stores Inc Co	3.7	United Technologies Cp	2.8		
		Southwest Aircls Co Com	1.0		
<b>Consumer Staples</b>		Stericycle Inc Com	2.4		
Conagra Inc Com	2.0				
Kroger Co	2.5	<b>Information Technology</b>			
Cvs/Caremark Corp	2.8	Apple Inc	4.6		
Coca Cola Co Com	3.4	Google Inc Cl A	4.6		
		Emc Corp/Mass	3.0		
<b>Energy</b>		International Bus Mach	1.1		
Exxon Mobil Corporatio	1.9	Oracle Corporation	4.0		
Schlumberger Ltd Forei	1.5	Verisign Inc Com	1.6		
		Qualcomm Inc Com	3.9		
<b>Financials</b>					
American Express Co	1.5	<b>Materials</b>			
Mastercard Inc Cl A	1.7	Ecolab Inc Com	2.1		
		Sigma Aldrich Corp Com	1.2		
<b>Health Care</b>		Praxair Inc Com	2.0		
Amgen Inc Com	3.3				
Abbott Labs Com	2.4	<b>Utilities</b>			
Abbvie Inc. Com	1.0	Verizon Communications	4.3		
Celgene Corp Com	2.4				

# Outperformance with Less Risk (Does Risk Matter?)

## Sawgrass Diversified Large Growth Since Inception – March 1998-December 2013



\*Source: eVestment Alliance as of 12/31/2013. Risk statistics calculated monthly using Large Cap Growth Universe. Returns are gross of management fees. Please see appendix for disclosures.





## ***Protecting Florida's Investments Act Compliance***

November 2013

Re: Protecting Florida's Investments Act

This notification is intended to inform you of Sawgrass Asset Management's understanding of and compliance with the Protecting Florida's Investments Act (PFIA). As you may know, the Florida State Board of Administration has issued a guidance regarding some prohibited investments for municipal plans in Florida.

We have reviewed the information from the September 24, 2013 Board of Administration quarterly report and can verify that we hold no securities in your portfolio(s) that are identified on the list of scrutinized companies and any of the other companies on watch regarding the PFIA.

We will continue to monitor this list and notify you should we have any questions regarding our ability to comply. Given the nature of this list, we believe it is unlikely that we would have any problems.

Please contact us if you have any questions regarding the PFIA or your investment with Sawgrass Asset Management.

Best Regards,

Sawgrass Asset Management Team

## Stock Market: Quarter in Review

- The equity markets capped off their best year since 1997 in impressive fashion adding another double digit percentage quarterly gain to close out a 30+ percent annual campaign.
- The major indices enjoyed another smooth ride up during the quarter devoid of any significant declines as immediate debt ceiling concerns were resolved and the market took the news of the beginning of Federal Reserve tapering in stride.
- The underlying tone to the market was mixed for the quarter but more “risk on” for the year as higher beta, smaller, more cyclical companies were generally rewarded.
- Growth and large cap outperformed value and small cap as the best performing sectors were industrials, information technology, and materials while the relative laggards were utilities, energy, and consumer staples. For the whole year, small cap stocks led the way while the top sector performer was Discretionary.

## Stock Market: The Quarter Ahead

- The major indices have posted double digit percentage gains in three of the last four years and pushed the returns from the lows of 2009 to upwards of 175 percent, an extraordinary run that is approaching the time length and percentage gains of some of the great bull markets of the past.
- Despite this run, the major indices are still just marginally ahead of the values reached in 2000 as the markets have spent more than a decade attempting to allow earnings to catch up with the historic overvaluation registered at that peak.
- The continued relative strength in small and mid cap stocks along with the ability of the major indices to hold their breakout to new all-time highs has helped to improve investor sentiment and increased expectations for further longer term performance.
- Broad participation by more defensive, less cyclically oriented sectors and stocks in such a strong up year stands in stark contrast to their dramatic relative underperformance during the early stages of this bull market in 2009-2010 suggesting possible later stage bull market dynamics.
- The recent significant multiple expansion, despite slowing earnings growth rates and higher interest rates, has created less attractive valuation and elevated the risk that future growth will not meet these heightened expectations.
- Stocks have been able to avoid a ten percent decline since March 2012, the longest stretch in almost seven years. This unusual level of calm could portend a more significant correction in coming months to temper some of the current lack of volatility and balance investor sentiment.
- The ongoing battles over the debt ceiling, government spending, and healthcare re-

## 4<sup>th</sup> Quarter Scorecard

Table 1

Index	Quarter	1 Year
S&P 500	10.7%	32.6%
Russell 1000	10.2%	33.1%
Russell 2000	8.7%	38.8%
Russell 3000	10.1%	33.6%
Russell 3000 Growth	10.3%	34.2%
Russell 3000 Value	10.0%	32.7%
Barclays Capital US Aggregate	-0.1%	-2.0%
3 Month T-Bills	0.02%	0.07%

Source: Bloomberg & Russell Investments

form are likely to intensify once again as the mid-term elections approach in November creating potential wild cards to accompany the beginning of the current modest expected tapering operations from the Federal Reserve.

- Despite the impressive strength in 2013, the coming months could see equity price movement become more volatile and further gains more difficult given an aging bull market approaching its fifth anniversary, less favorable valuation, and ongoing political, monetary, and fiscal uncertainties.

(Continued on back)

## Interest Rate Summary

Table 2

	12/31/12	9/30/13	12/31/13	Qtr Change	12-Month Change
3 Month T-Bills	0.1	0.0	0.1	+0.1	0.0
5 Year Treasury	0.7	1.4	1.8	+0.4	+1.1
10 Year Treasury	1.8	2.6	3.1	+0.5	+1.3
30 Year Treasury	2.9	3.7	4.0	+0.3	+1.1
5 Year Corporate ('A')	1.7	2.3	2.5	+0.2	+0.8
10 Year Corporate ('A')	3.0	3.9	4.2	+0.3	+1.2
30 Year Fixed Rate Mortg.	3.4	4.3	4.5	+0.2	+1.1

Source: Bloomberg

## Release the Kraken!

This dramatic line from the movie *Clash of the Titans!* preceded an epic battle on the silver screen. While Liam Neeson is paid handsomely to create drama, Federal Reserve Chairman Ben Bernanke would prefer to avoid it. Mid-December, with his usual flair for the undramatic, Chairman Bernanke droned, "The Committee decided to modestly reduce the pace of its asset purchases." This might as well have been, "release the taper!" for the ensuing battle on our Bloomberg screens. The FOMC's current mission is to convince the markets that the inevitable slowing of its large-scale asset purchase program is not a decision to tighten monetary policy. The growth in size of the Fed's balance sheet alone is enough to suggest tapering begin (see Graph 1).

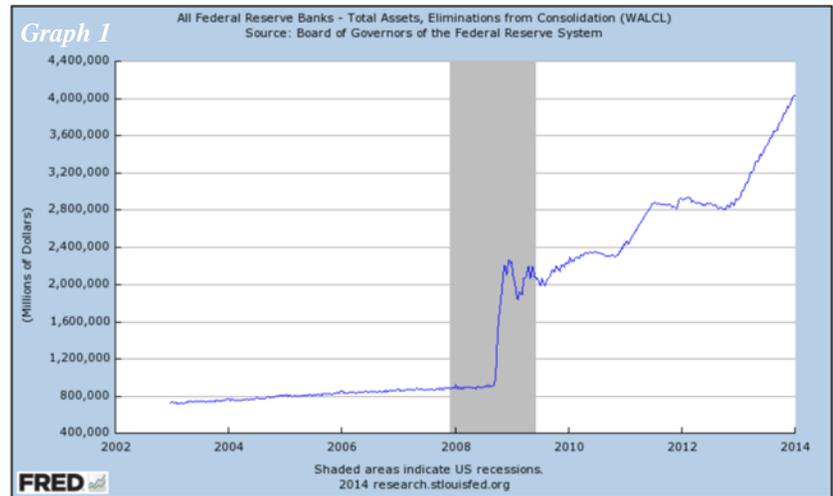
In defending a more balanced forecast for future economic growth, the Fed points to further improvements in labor market conditions, however unemployment remains elevated. Household spending advanced while the housing sector slowed somewhat. Inflation continues below the Committee's objective leading to the forecasts of lower rates for a longer period of time. We will see how these indicators develop.

## Clarity Emerges

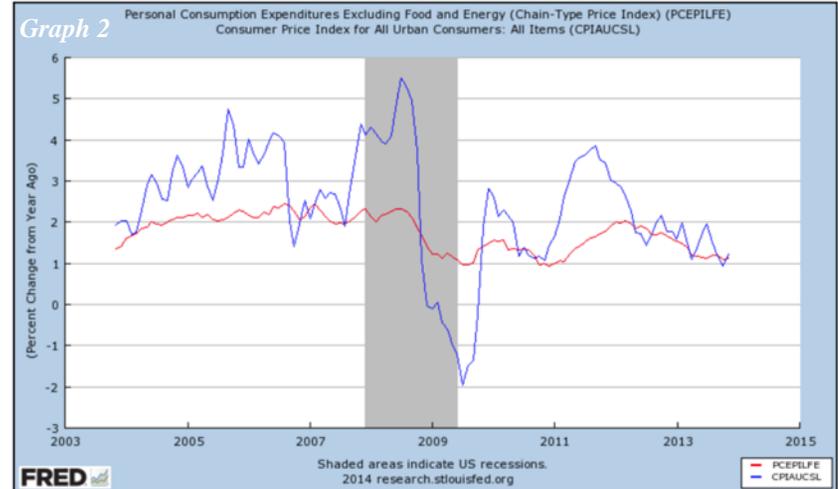
One new bright spot for the economy is 'decreasing uncertainty.' The recent compromise in Washington has allowed Congress to pass its first budget in three years. While the deficit reduction was relatively modest, some certainty can be seen in fiscal policy, at least for now. Monetary policy is adding some stability as well. The known timing of the tapering of quantitative easing along with the appointment of Janet Yellen as Ben Bernanke's successor reduces concern over these transitions. With the release of The Volker Rules, even our regulators are aiding certainty. As stability and certainty are good for the economy and risky assets (stocks and corporate bond spreads), this has led to higher interest rates (see Table 2).

## Inflation Concerns

As mentioned above, the current concern is that there is not enough inflation. Headline nominal Consumer Price Index and the Fed's preferred measure of inflation, core personal consumption expenditure, are both running well below the 2% target (see Graph 2). Commodity prices continue their weakness. For example, gold, silver, corn, and wheat are down 20% to 40% this year. Labor markets remain slack. Elevated unemployment, under employment, and falling labor participation rates makes it difficult to create increasing consumer demand. Without this demand, it is less likely to see significant increase in corporate capital expenditures. It is these capital investments that will lead to jobs.



Source: FRED Economic Data, St. Louis Fed



Source: FRED Economic Data, St. Louis Fed

