

Polen Capital Management  
**PORTFOLIO APPRAISAL**  
*City of Ormond Beach Police Officers' Pension Trust Fund*  
*Regions Morgan Keegan Trust # 3250000589*  
**PCM # 2964**  
*June 30, 2013*

Quantity	Security Symbol	Security	Unit Cost	Total Cost	Price	Market Value	Pct. Assets	Cur. Yield
<b>COMMON STOCK</b>								
3,883	ABT	Abbott Labs	31.54	122,483	34.88	135,439	5.2	1.6
1,860	ACN	Accenture Plc	64.06	119,152	71.96	133,846	5.1	2.3
1,730	AGN	Allergan Inc	96.55	167,033	84.24	145,735	5.6	0.2
210	AAPL	Apple Inc	585.25	122,904	396.08	83,177	3.2	3.1
1,078	CHRW	C.H. Robinson	60.79	65,536	56.31	60,702	2.3	2.5
2,032	EBAY	Ebay Inc	52.18	106,027	51.72	105,095	4.0	0.0
883	FDS	Factset Research	103.48	91,373	101.94	90,013	3.5	1.4
1,058	FAST	Fastenal	50.01	52,914	45.85	48,509	1.9	2.2
976	IT	Gartner Inc	52.29	51,034	56.99	55,622	2.1	0.0
237	GOOG	Google Inc	615.02	145,759	880.37	208,648	8.0	0.0
2,161	INTU	Intuit Inc	57.82	124,957	61.03	131,886	5.1	1.1
181	ISRG	Intuitive Surgical Inc	575.50	104,166	506.58	91,691	3.5	0.0
3,148	NKE	Nike Inc Cl B	50.11	157,753	63.68	200,465	7.7	1.3
3,789	ORCL	Oracle Corp	28.87	109,388	30.72	116,398	4.5	1.6
2,695	QCOM	Qualcomm Inc	63.44	170,960	61.08	164,611	6.3	2.3
2,216	SBUX	Starbucks Corp	59.45	131,733	65.49	145,126	5.6	1.3
2,350	TROW	T. Rowe Price Group	63.17	148,460	73.15	171,903	6.6	2.1
1,185	VAR	Varian Medical	69.79	82,701	67.45	79,928	3.1	0.0
1,024	V	Visa Inc Cl A	168.92	172,978	182.75	187,136	7.2	0.7
423	GWW	W.W. Grainger Inc	227.54	96,249	252.18	106,672	4.1	1.5
				2,343,558		2,462,601	94.4	1.2
<b>CASH AND EQUIVALENTS</b>								
	divacc	Dividend Accrual		661		661	0.0	0.0
	999990484	Regions Trust Cash Sweep		145,202		145,202	5.6	?
				145,864		145,864	5.6	0.0
<b>TOTAL PORTFOLIO</b>				<b>2,489,422</b>		<b>2,608,465</b>	<b>100.0</b>	<b>1.1</b>

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**PERFORMANCE HISTORY**  
**GROSS OF FEES**  
*City of Ormond Beach Police Officers' Pension Trust Fund*  
*Regions Morgan Keegan Trust # 3250000589*  
**PCM # 2964**  
*From 04-25-12 to 06-30-13*

Time Period	Percent Return Per Period			Cumulative TWR Basis = 100		
	Portfolio	S&P 500 Total Return	Russell 1000 Growth Total Return	Portfolio	S&P 500 Total Return	Russell 1000 Growth Total Return
04-25-12 to 06-30-12	-5.98	-1.62	-3.34	94.02	98.38	96.66
06-30-12 to 09-30-12	4.81	6.35	6.11	98.54	104.63	102.57
09-30-12 to 12-31-12	-0.33	-0.38	-1.32	98.22	104.23	101.21
12-31-12 to 03-31-13	6.43	10.61	9.54	104.53	115.29	110.87
03-31-13 to 06-30-13	-2.24	2.91	2.06	102.19	118.64	113.16
<b>Date to Date</b>						
04-25-12 to 06-30-13	2.19	18.64	13.16			
Annualized	1.85	15.58	11.04			

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July 10, 2013

## 2<sup>nd</sup> Quarter 2013 Portfolio Commentary

Polen Capital's Large Cap Growth Model Portfolio (the "Portfolio") returned -2.19% for the 2<sup>nd</sup> quarter versus 2.06% for the Russell 1000 Growth Index (the "Russell 1000 Growth") and 2.91% for the S&P 500 Index (the "S&P 500").

The primary drivers of our underperformance this quarter were:

- 1) Continued market rotation toward big dividend payers and lower quality companies;
- 2) exogenous issues with two Portfolio holdings: Cognizant Technologies and Allergan; and
- 3) modest revenue and earnings growth deceleration across our owned companies.

This quarter brought a continuation of the trend in which the market's appreciation for slower growing, higher yielding stocks trumped faster growing firms like those in which we typically invest. Given the share price appreciation amidst low earnings growth, the multiple of this cohort has expanded dramatically during the last 12 months. This has resulted in certain "safe" sectors of the market trading at historically high valuations. The table below shows the performance of Brown-Forman and Proctor & Gamble (not currently owned by us) versus Qualcomm (which we currently own). This is a microcosm of the valuation disparities we currently see among the companies that we cover. Both P&G and Brown-Forman possess tremendous competitive advantages, but we did not find their valuations attractive relative to their growth prospects. During the past two years, that gap has widened making them even less attractive to us.

Company	Two year share price change	Projected current year sales growth	Projected current year EPS growth	Forward P/E multiple	Dividend yield
Brown-Forman	35.7%	5.0%	8.0%	22.7x	1.5%
Proctor & Gamble	21.1%	3.0%	7.2%	19.2x	3.0%
QUALCOMM	7.6%	22.6%	22.4%	13.4x	2.3%

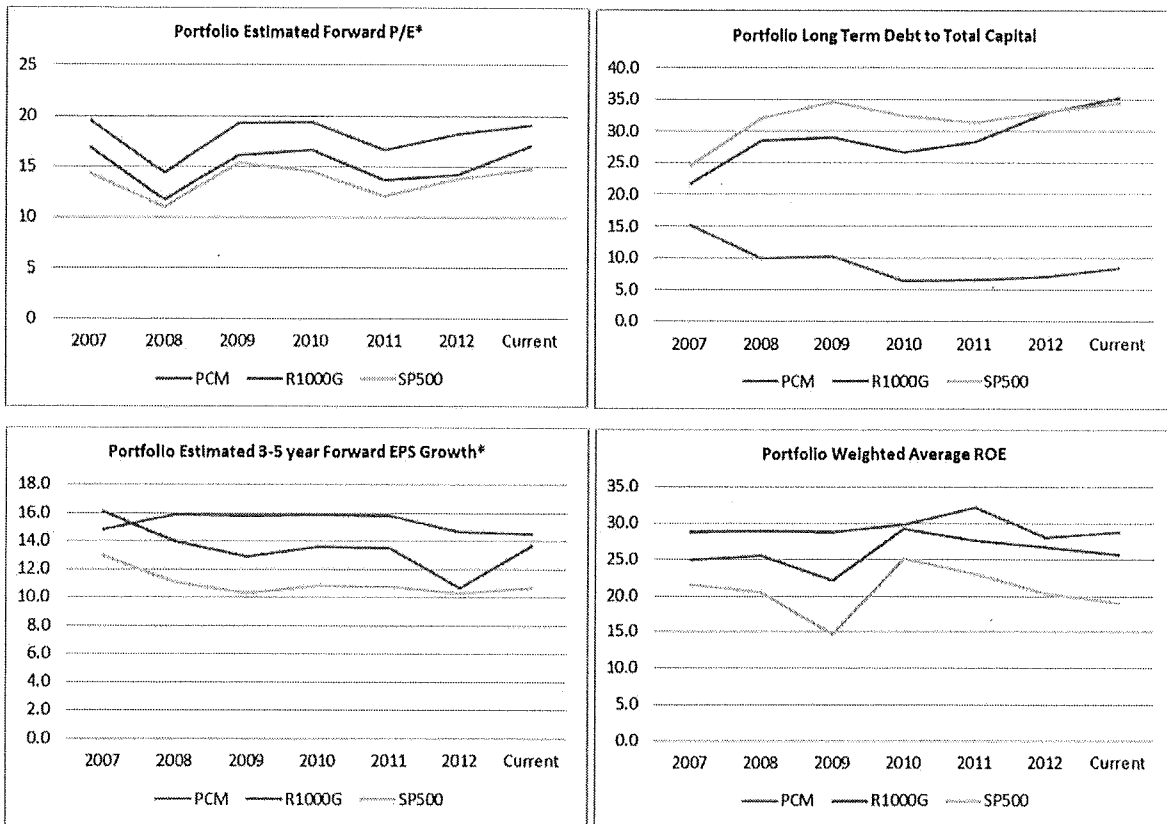
Interestingly, lower quality companies with highly levered balance sheets are also doing quite well. Many of these highly levered companies have received a boost to their earnings power as they refinance high interest debt with very low rates yielding lower interest expense and thus higher net income (see link to a recent [New York Times article](#) discussing this topic). Cash-rich, high-quality companies on the other hand, have had their earnings penalized by lower interest income on their cash balances. Central bank manipulation of the debt markets has much to do with the outperformance of both highly levered and high dividend yielding companies. We do not believe this trend will prove sustainable in the long run.

In addition to the rotation toward lower quality and big dividend payers, our recent performance has also been negatively impacted by exogenous issues with two of our Portfolio holdings (see discussion of Cognizant Technologies and Allergan below) and a modest growth deceleration

across the Portfolio. Most of the companies in our coverage universe and in the Portfolio operate globally and we have heard a consistent story of slower economic growth that appears to be more pronounced in Europe and Asia, but also an issue across most sectors in North America.

Despite these short-term issues we remain steadfast in our belief that the most important driver of our long-term investment return has been, and will always be, the underlying earnings growth of the Portfolio companies. Our aim as investors is to assemble a concentrated portfolio of competitively advantaged businesses that will grow earnings at a mid-teens rate and thus drive our long-term investment returns.

We remain disciplined in the application of our proprietary investment methodology. The best way for investors to track this is to monitor the key characteristics of the Portfolio including its forward P/E, debt-to-total capital ratio, estimated long-term earnings growth, and the return on equity (ROE). The charts below tell a consistent story. As usual, we only own what we deem to be financially superior, competitively advantaged businesses at acceptable prices. Today, consistent with the past, the Portfolio is characterized by companies with better balance sheets (extremely low debt to capital ratios), higher profitability (higher ROEs), and higher growth (estimated long-term EPS growth) than both the S&P 500 and Russell 1000 Growth indexes. We do pay a modest premium for these companies, which is also consistent with our past experience. The portfolio is constructed for long-term appreciation driven by the underlying earnings growth of the individual companies over time, by which we mean the next 5-10 years.



\* Forward EPS estimates and P/E ratios are based on FactSet consensus estimates



## **Portfolio Activity**

In the 2<sup>nd</sup> quarter, we added eBay to the Portfolio and increased our positions in Visa and Grainger. We sold Cognizant out of the Portfolio and trimmed our positions in Varian Medical, FactSet and Starbucks.

eBay is a leading e-commerce network that historically focused on selling used goods through online auctions, but has emerged as a true electronic retailing platform selling primarily new goods at fixed prices to a global user base of 112 million strong. Management has spent the past few years cleaning up the site to enhance and simplify the user experience for buyers and sellers alike. eBay also owns PayPal, a rapidly growing electronic payment network which provides a secure means of payment for more than 123 million active users on the internet today. We believe eBay's newly improved Marketplaces business is now well positioned in the fast-growing e-commerce market and its payments business should continue growing at greater than 20% going forward. Together these should enable steady earnings growth and fuel investor returns.

Cognizant has remained compellingly valued, but we were forced to sell the stock after the 'Gang of Eight' Senators introduced a comprehensive immigration bill containing a particularly onerous provision targeted directly at Indian IT outsourcing firms including Cognizant. The legislation's "outplacement" provision aims to severely restrict the use of visa-carrying foreign nationals working on site at client firms. We believe there is less than a 50% chance that the outplacement provision finds its way into the final law in the currently proposed form, but if it were to pass the provision would be quite damaging to Cognizant's current business model and growth prospects. The bill recently passed through the Senate and is now subject to debate and political maneuvering within the House of Representatives. We do not feel comfortable subjecting our investors to even the remote risk that this provision becomes law, so we fully exited our Cognizant position during the quarter.

Allergan was our biggest drag on performance in the quarter for two reasons. Firstly, in May the company said it was delaying the development of a potential blockbuster drug to combat wet Age-related Macular Degeneration (wet AMD). This news in no way impacted current sales or earnings for Allergan. Specifically, the drug candidate's trials are being reconfigured and will run over a longer time horizon which will delay any realization of sales and earnings from this drug. It should be noted that we did not have significant expectations for this drug factored into our outlook for Allergan as it was still unproven. Secondly, in June the FDA decided to lower the bar for competitors to develop and market generic equivalents to Allergan's chronic dry eye treatment Restasis. This regulatory shift was unforeseen as FDA officials had previously indicated, as recently as 2010, that extensive clinical trials would be required before a generic equivalent of this drug would be approved. Restasis accounts for roughly 15% of Allergan's earnings and the news of the FDA's reversal hit shares immediately. The company's management remains focused on execution and continues to plough 16.5% of sales into new drug discovery and development. We believe Allergan's business should continue to grow earnings and cash flow at a healthy double-digit rate despite these setbacks, and we now find the stock exceptionally well valued relative to that earnings growth potential.

### Contributors and Detractors

The top three contributors (portfolio weight multiplied by return) in the second quarter were Starbucks (+0.85%), Google (+0.76%) and Nike (+0.59%). The bottom three contributors to the Portfolio were Allergan (-1.77%), Cognizant (-0.97%) and QUALCOMM (-0.55%).

\* \* \* \* \*

Throughout our more than 24 year history we have seen stretches of short-term underperformance, but our strategy has consistently outperformed over the long run. Since inception we have produced a compounded annualized return that is more than 400 basis points higher than that of both the S&P 500 and the Russell 1000 Growth indexes, which approximates the difference between the average earnings growth of our Portfolio and those benchmarks.

Thank you for your interest in Polen Capital and please feel free to contact us with any questions or comments.

Sincerely,

PCM Investment Team