

Dear Clients:

First and foremost (and to be totally transparent), please accept my apology for the delay in releasing our 4th Quarter Update. The start of 2014 has been quite eventful for everyone at Nepsis Capital Management, from both a market and a marketing perspective.

We launched our new website, www.nepsiscapital.com just last week. I had the privilege of addressing the Registered Investment Advisor community at the TD Ameritrade conference as a panelist in late January. In case you didn't hear, I was also interviewed by CNBC, discussing the 2014 market outlook, www.nepsiscapital.com/cnbc. The year 2014 is out of the gates and looks to be a year that will provide us with opportunities to invest in quality companies when they go on sale... but this is about the end of 2013.

As another year is complete, U.S. indexes were up substantially, including the S&P 500 up over 27%, while we continue to see investor pessimism and fear permeate the air. Many believe the stock market is headed for a big crash once again. I continue to view investor pessimism as extremely positive! The further we move away from the financial crisis, the more comfortable investors are becoming with owning equities; yet we continue to see a lot of cash on the sidelines or in bonds, paying very little interest.

Although it is short-term thinking (remember we invest in businesses for the long-term), we are extremely pleased with the performance of all five of our portfolio allocations, especially on a Risk Adjusted basis (the amount of risk taken to achieve portfolio return).



Of course, there are no guarantees, but as I say all the time, we expect well-run companies to continue to grow over a long period of time. Additionally, we continue to look forward to market corrections to take advantage of opportunities in investing in businesses at lower prices.



Stock market corrections of 10% to 20% are extremely healthy for long-term bull markets and are short-term in nature. So when the next big correction comes, DO NOT panic. Understand that the businesses owned in portfolios will continue to grow over time and that we will use the correction as an opportunity to enhance the long-term position of client portfolios.

Although we saw strong returns in 2013, it was really a "boring" year for the markets and frankly, a very difficult market from an investing perspective.

You may be asking yourself, ***"Why was 2013 a difficult year to invest?"***



Investors must understand that stock prices don't normally go straight up. There is usually a 5% to 15% correction in the markets during most years. However, that was not the case in 2013. As a portfolio manager, when markets continue to go straight up, we are more reliant on *Flexibility* to take advantage of the market correction with "Strategic Cost Averaging".

EXPECT A LOT MORE STOCK MARKET VOLATILITY IN 2014!

Frankly, I would warmly welcome a stock market correction at this point, but as we know, the stock market is NOT logical and no one knows when the next correction is going to happen. Therefore, it is extremely important for investors to have a sound investment *Philosophy, Strategy, Flexibility* and *Transparency* when it comes to investing.



Of course, some investors may be wondering, "why a correction now? I am fully invested." While you may be fully invested, corrections can be very healthy for a portfolio, as it provides the opportunity to potentially sell weaker companies in the portfolio in favor of stronger companies. For this reason, we often highlight the benefits that *Flexibility* provides us when owning "businesses" as opposed to the "stock market."

Lastly, while 2013 was very kind to the U.S. stock market, International and Emerging Markets continued to lag, with Emerging Markets once again ending the year with negative returns (see chart).

Many investors continue to look to the U.S. markets as the "safe haven" and place to invest capital. But, make no mistake, there are great companies in other countries that present long-term investors with great opportunities to buy on sale. At Nepsis, we continue to assess businesses we own in this part of the world and companies we would like to own over time.

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2013 KEY PERFORMANCE

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Key ETF Performance (%)

US Related				Global					
ETF	Description	MTD	QTD	YTD	ETF	Description	MTD	QTD	YTD
SPY	S&P 500	↑ 2.04	↑ 9.93	↑ 29.69	EWA	Australia	↓ -3.90	↓ -3.56	↓ -3.06
DIA	Dow 30	↑ 2.96	↑ 9.58	↑ 26.72	EWZ	Brazil	↓ -4.83	↓ -6.74	↓ -20.13
QQQ	Nasdaq 100	↑ 2.60	↑ 11.51	↑ 35.05	EWC	Canada	↑ 0.24	↑ 3.00	↑ 2.68
IJH	S&P Midcap 400	↑ 2.59	↑ 7.79	↑ 31.57	FXI	China	↓ -4.39	↑ 3.48	↓ -5.14
IJR	S&P Smallcap 600	↑ 1.05	↑ 9.35	↑ 39.73	EWQ	France	↑ 1.86	↑ 5.84	↑ 20.60
IWB	Russell 1000	↑ 2.20	↑ 9.56	↑ 30.35	EWG	Germany	↑ 3.89	↑ 14.20	↑ 28.58
IWM	Russell 2000	↑ 1.63	↑ 8.21	↑ 36.82	EPH	Hong Kong	↓ -0.72	↑ 2.85	↑ 6.08
IWV	Russell 3000	↑ 2.31	↑ 9.40	↑ 30.67	INP	India	↑ 3.06	↑ 12.55	↓ -3.99
IWW	S&P 500 Growth	↑ 2.75	↑ 10.51	↑ 30.38	EWI	Italy	↑ 1.70	↑ 10.41	↑ 15.91
IJK	Midcap 400 Growth	↑ 3.03	↑ 7.96	↑ 31.27	EWJ	Japan	↑ 0.66	↑ 1.84	↑ 24.50
IJT	Smallcap 600 Growth	↑ 0.72	↑ 9.46	↑ 41.14	EWK	Mexico	↑ 1.16	↑ 6.43	↓ -3.59
IVE	S&P 500 Value	↑ 1.68	↑ 9.12	↑ 28.72	EWP	Spain	↑ 2.44	↑ 10.99	↑ 27.46
IJJ	Midcap 400 Value	↑ 2.26	↑ 7.60	↑ 31.87	RSX	Russia	↑ 2.38	↑ 2.45	↓ -3.44
IJS	Smallcap 600 Value	↑ 0.89	↑ 8.84	↑ 37.51	EWU	UK	↑ 1.80	↑ 6.42	↑ 16.39
DVY	DJ Dividend	↑ 1.68	↑ 7.55	↑ 24.65	EFA	EAFE	↑ 1.29	↑ 5.16	↑ 18.00
RSP	S&P 500 Equalweight	↑ 2.52	↑ 9.28	↑ 33.63	EEM	Emerging Mkts	↓ -1.31	↑ 2.55	↓ -5.76
FXB	British Pound	↑ 1.24	↑ 2.25	↑ 1.61	IOO	Global 100	↑ 0.78	↑ 7.37	↑ 20.76
FXE	Euro	↑ 1.24	↑ 1.60	↑ 3.84	EEB	BRIC	↓ -2.86	↓ -1.70	↓ -3.80
FXF	Yen	↓ -2.71	↓ -6.75	↓ -17.93	DBC	Commodities	↑ 0.59	↓ -0.39	↓ -7.63
XLY	Cons Disc	↑ 1.88	↑ 10.23	↑ 40.88	USO	Oil	↑ 5.56	↓ -4.15	↑ 5.84
XLP	Cons Stap	↓ -0.07	↑ 7.99	↑ 23.15	UNG	Nat. Gas	↑ 8.04	↑ 13.18	↑ 9.47
XLE	Energy	↑ 2.39	↑ 6.76	↑ 23.93	GLD	Gold	↓ -3.79	↓ -9.41	↓ -28.33
XLF	Financials	↑ 1.77	↑ 9.82	↑ 33.37	SLV	Silver	↓ -2.75	↓ -10.48	↓ -36.30
XLV	Health Care	↑ 0.33	↑ 9.59	↑ 39.02	SHY	1-3 Yr Treasuries	↓ -0.22	↓ -0.11	↓ -0.05
XLI	Industrials	↑ 3.69	↑ 12.62	↑ 37.89	IEF	7-10 Yr Treasuries	↓ -2.41	↓ -2.81	↓ -7.68
XLB	Materials	↑ 4.24	↑ 10.02	↑ 23.12	TLT	20+ Yr Treasuries	↓ -2.48	↓ -4.27	↓ -15.94
XLK	Technology	↑ 3.03	↑ 11.55	↑ 23.88	AGG	Aggregate Bond	↓ -0.93	↓ -0.72	↓ -4.19
IYZ	Telecom	↑ 3.99	↑ 7.80	↑ 22.55	BND	Total Bond Market	↓ -1.07	↓ -1.03	↓ -4.74
XLU	Utilities	↓ -0.16	↑ 1.61	↑ 8.73	TIP	T.I.P.S.	↓ -1.53	↓ -2.38	↓ -9.48

Source: Bespoke

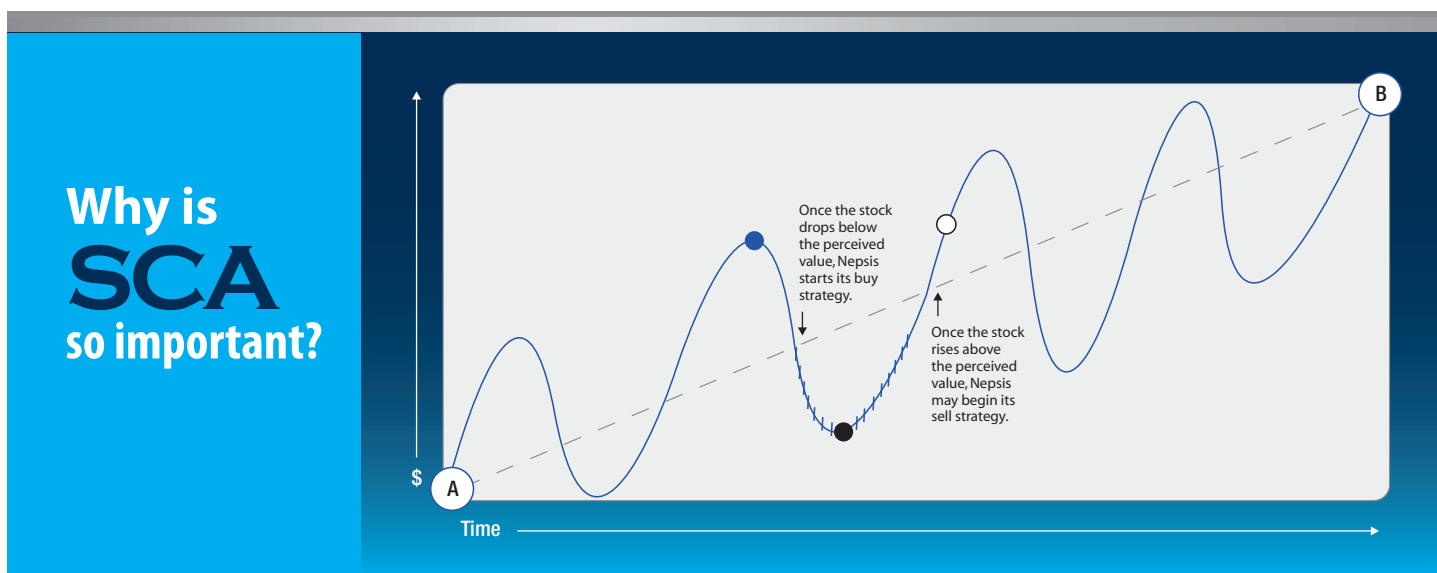
Listed above are the 2013 returns of the key ETF's in the market which track indexes. **Please note the negative returns in the Treasuries and other bonds in 2013.** Over the past two years, we have been cautioning investors about bonds and the potential short-term risk in owning bonds.

Although there was a fair amount of overall weakness in the Emerging Markets (EM) in 2013, we saw substantial increases in value in several of the companies we own in the EM, particularly in China – BIDU, EJ and CTRP. This performance proves the importance of looking beyond stock market indexes, which is why we always say “buy businesses long-term and focus on the businesses you own, not stock markets!” Of course, company values DO NOT go straight up. So, as much as we continue to like these companies long-term, a correction in these companies' prices should not be a surprise and should be expected in 2014.



WHAT IS STRATEGIC COST AVERAGING™?

Unlike dollar cost averaging (DCA), which is the process of investing a fixed amount on a regular schedule, Strategic Cost Averaging™ (SCA) is the process of continually investing unequal dollar amounts specifically targeted into companies we want to own more of when appropriate.



The ability to SCA is extremely important because it allows the *Flexibility* needed to take advantage of buying more of a company we want to own in the portfolio when it is “on sale.” The SCA process is exactly why stock market volatility – or more importantly, “**stock**” volatility – is so crucial in the investment process on a longer-term basis.

Some investors have asked in the past, “why do you buy or sell so few shares of a company occasionally? Buying or selling so little doesn’t have any impact on the portfolio.” As a matter of fact, buying or selling a small percentage of a position in the portfolio actually DOES make a difference in the portfolio over time! Remember, the shorter the time horizon you look at, the more illogical and irrational the stock market (and company prices) can be. This is why we subscribe to Dr. Jeremy Siegel’s studies showing the longer you own stocks, the less risky they become.

WHEN MARKETS AND COMPANIES STOCK PRICES PULL BACK, OFTEN WE WILL HEAR INVESTORS SAY, “I LOST MONEY THIS MONTH” OR, “I’M LOSING MONEY AND CAN’T AFFORD TO LOSE MONEY.”

It is important to understand that you did NOT lose money; you only lose money when you SELL an investment at a loss. Investors spend too much time looking at their monthly statements to see how much money they “made” or “lost.” The fact of the matter is, you do not make or lose money until an investment is sold! Investments DO NOT go straight up in price.

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Recently, I wrote a blog piece titled, “When’s The Sale.” In light of the performance of investments in the last couple of years, I believe the blog piece has some good thoughts for investors to keep in mind.

WHEN’S THE SALE?

As I often say, volatility is an investor’s best friend and the best time to go shopping!

WHY ARE INVESTORS AFRAID OF VOLATILITY?

When volatility hits the stock market, many investors fear that they will “lose” their money.

In reality, most companies are not going to go out of business during periods of volatility. Additionally, if the last five years and the financial crisis have taught us anything, it is that you cannot predict the stock market or when it will be a good time to begin or continue investing in a great company. It is volatility that creates the opportunity to take advantage of buying great companies on sale!

Let’s face it, everyone would prefer to buy things they want or need on sale. The problem is, sometimes you just don’t know when or even if it will ever go on sale. In many cases, you will still purchase it because you believe you are paying a fair price and it is something you want to own. However, there are also times when you know there will be a sale - like after Christmas when you know you are getting a deal.

Sometimes you know when a sale will occur and other times you don’t. No matter what, you will make a purchase because you believe in what you are buying and will WANT to buy more when the sale finally does happen. However, if you do not know much about the product and don’t necessarily believe in it, you probably won’t care if it is on sale and are unlikely to make a purchase. This is a great example of how **Flexibility** (the ability to buy something when you want to) and **Transparency** (knowing what you are buying and why) enable investors to have a greater level of “Clarity” when making purchasing decisions.

The fact of the matter remains, whether something is on sale or not, if an investor believes in what they are purchasing, **volatility will become a non-issue.**



INVEST WITH CLARITY

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PORTFOLIO STRUCTURE AND OUTLOOK

As discussed before, we are always looking for a correction, but we are not in the business of trying to guess where the “stock market” is going to go. Instead, we look at the fundamentals of the companies we own and base our investment decisions on the information we review.

Today, our portfolios continue (and will more than likely continue this way for years to come) to be overweight in financials. We believe that many of the U.S. banks and other financial companies remain great long-term investments.

In 2013, several of the companies we own had tremendous moves, as many investors look to replace bond yields with dividends and growth in an effort to accomplish their financial goals.

Due to the success of many of the companies we own, their values and prices may have increased. That of course, does not mean we want to sell them. Company values expand and contract over time. When we get a pullback in some of these companies, we will look to add to portfolios as appropriate.

The Emerging Markets and International Markets (especially Europe), continue to be challenging. However, we have reason to believe this will not last too long, as things do seem to be stabilizing recently. Therefore, we continue to look for new ideas and continue to strategically add to positions where appropriate.

As for gold and silver – we continue to view those metals and hedges against the U.S. dollar and inflation. As of today, the dollar continues to strengthen and inflation is nowhere in sight. We continue to monitor this situation daily, however, we remain very bearish in owning gold and silver as hedges in portfolios. If you would like to learn more about our position on gold, please visit our blog site, www.investingwithclarity.com and check out the article, “All That Glitters Is Not Gold.”

As we move through 2014, the markets are showing no signs of a slowdown or correction. Of course, this is the time investors must maintain clarity in how their portfolio is being managed. It is the **Transparency** of an investor’s portfolio which enables them to “stick to the knitting” during difficult periods in the economy and in their investments.

Although we continue to be very bullish on the U.S. economy and the stock market as a whole, there will be bumps in the road (i.e. corrections). However, we remain extremely happy and comfortable with the companies we own in our clients’ portfolios, both from a valuation standpoint and competitive positions they hold. Of course, this does not mean we won’t make changes as opportunities present themselves. However, we continue to remain very diligent in assessing the companies we own and new opportunities for future investment.

We appreciate your continued confidence and support in the Nepsis Investment Philosophy and Strategy and look forward to a great rest of 2014!

Respectfully,

Mark Pearson
President & CIO
Nepsis Capital Management, Inc.

