Investment Overview - January 2017

We hope your 2017 is off to a good start. 2016 saw plenty of activity in both the stock and bond markets. For example:

- The S&P 500 experienced bouts of volatility and declines early in the year while finishing the year in a strong fashion up 11.95%[1].
- Almost half of the 2016 return for the S&P 500 occurred in the final two months of 2016.
- Developed nations outside of the United States saw their government bond yields go negative.
- The United States 10 year government Treasury bond touched a record low yield of 1.36%[2] in July following the Brexit but closed the year higher at 2.44%[3].

We concluded 2016 on a positive note, noting in our December letter that the gains were broad based across the portfolio and driven by the equity holdings. Many of the strongest performers in 2016 were some of the weakest performers in 2015. Throughout 2016 we maintained relatively modest market exposure and we used the strong price performance to reposition and sell some holdings while taking advantage of declines and uncertainty to add to and establish new positions. For 2017, we believe the pieces are in place to build off the momentum of 2016.

Election Thoughts

We offer no political opinions but we thought it may be worthwhile to discuss how the new administration may impact the portfolio and the markets. Following the election we saw increases in financial and industrial stocks accompanied by a sharp rise in fixed income yields. The expectation of higher interest rates, an improved economic environment and less regulation drove price increases in AIG, Colfax, Berkshire Hathaway, and Leucadia. On the fixed

[1] Source is Bloomberg Finance L.P. Comparative Returns
[2] http://www.marketwatch.com/story/short-term-treasury-yields-jump-to-2-week-high-on-jobs-report-2016-07-08

[3] Source is Bloomberg Finance L.P. Comparative Returns

income side, Municipal bonds were the weakest due to a combination of rising interest rates, increased supply coming to market, outflows in the asset class, and the prospects for lower personal tax rates. The benefits of municipal bonds remain and the asset class currently offers relative value.

On one hand, some believe that the recent rally in the markets and sharp increase in interest rates is unwarranted – i.e., that the stock and bond markets appear to be operating on hope, emotion, and speculation about future economic and policy changes. They also suggest the markets are pricing four years of an administration in 3 months. Global growth has been modest the last couple of years and despite the strength of our nation, the United States has some of the highest interest rates compared to other developed countries. Some wonder if low interest rates outside of the United States and weak global growth will act as an anchor on growth in the United States and its's markets. If this viewpoint is correct we would expect the fixed income portion of the portfolio to benefit from stable or lower interest rates.

On the other hand, there are expectations that a meaningful change in tax policy may benefit individuals, corporations and economic growth. Repatriation of foreign cash would likely benefit some of the multinational companies in the portfolio and lower corporate tax rates would primarily benefit domestic stocks that generate solid profits and pay full United States corporate tax rates. Lower personal income taxes and higher interest rates would likely stimulate small and large purchases. In addition credit remains available and interest rates remain low. This would be a positive for both restaurants and retail along with the purchases of big ticket items such as cars and homes. In 2016 restaurants and retail experienced weakness while the sales of cars and homes were strong. The latter are significantly more sensitive to higher interest rates.

We find ourselves somewhere in the middle of both compelling rationales. 2016 was a reminder that complex events and market movements cannot be predicted and market timing is a difficult venture. Market timing is an area where we do not wish to participate. Instead we will use price, valuation, and business analysis as our guide. Regardless of the stock and bond markets direction in 2017 we intend to utilize volatility for your benefit. Adding to positions and initiating new ones during market disruption and taking advantage of market optimism when it appears.

One area where we were able to identify new investments for the portfolio was in the healthcare sector. The demographics for this sector continue to improve. Many of the companies we have purchased in the portfolio play a significant and important role in society. In 2016, the healthcare sector was the worst performing sector in the S&P 500 and the only sector with a negative return in the calendar year[4]. Concerns over the potential for increased

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[4] http://www.sectorspdr.com/sectorspdr/Pdf/All%20Funds%20Documents/Document%20Resources/10%20Year%20Sector%20Returns

legislative action related to the election, headlines describing some of the aggressive price increases in pharmaceuticals, and rising costs associated with affordable care act had a negative impact on the sector.

However, these ongoing concerns and future uncertainty have created investment opportunities. We have built a basket of healthcare related companies that we believe will generate positive cash flows and operate across the healthcare delivery spectrum. The basket is composed of pharmaceutical companies, biotech companies, pharmacy, and information systems. Each has their own risk reward characteristics some of which we will highlight below.

Company Commentaries

CVS Health (CVS)

CVS Health is the nation's foremost integrated healthcare services provider with pharmaceutical services, pharmacy chains, and in store clinics that provide routine healthcare. CVS is expected to generate over $180 Billion in revenue in 2017 and fill more than 1 Billion prescriptions annually. Concerns about deteriorating retail industry fundamentals, the loss of a few large contracts related to increased competition from Walgreens Boots Alliance (WBA), and negative sentiment towards the pharmacy benefit managers (PBM) role in drug pricing, sent the stock to lower prices – i.e., prices not seen since 2013-2014. While the loss of potentially 40MM scripts will reduce earnings in the short term, CVS remains in a dominant position in a lucrative industry. This strong position and profitability allowed them to increase the dividend by 18% for 2017 and the stock now yields 2.1%. Free cash flows should be allocated toward stock buybacks, dividends, and incremental acquisitions. We expect earnings growth to resume in late 2017 and into 2018. This combination of free cash flow and earnings growth may drive CVS's multiple up towards market levels providing solid total return potential.

Allergan (AGN)

Allergan is a global specialty pharmaceutical company with a meaningful presence in women's health, gastrointestinal, ophthalmology, and aesthetics. The driver of growth going forward includes their focus on "the face" with their aesthetic franchise driven by Botox, Juvederm (Fillers) and Latisse (Lashes). Botox's strong market share (~75%), its complex manufacturing process, and its unique product characteristics decrease potential for generic competitors and the desire for consumers to switch away from Botox. The "cash pay" characteristics remove some of the pricing and reimbursement pressure. In November of 2015, pharmaceutical giant Pfizer offered to merge with Allergan for approximately $363.63 per Allergan share and a total enterprise value of approximately $160 Billion[5]. In addition to the benefits from Allergan's

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[5] http://www.allergan.com/news/news/thomson-reuters/pfizer-and-allergan-to-combine

growing product line and the scale benefits from such a large enterprise, Pfizer was interested in the favorable tax rates Allergan receives due to its Irish Domicile. In April of 2016, the Department of the Treasury introduced new rules to curb tax avoiding mergers and the Pfizer/Allergan merger was called off. Since the end of the proposed merger, the share price of Allergan has declined meaningfully. We initiated a position after the selloff. Allergan management has also taken action by selling their generic pharmaceutical business to Teva for approximately $40 Billion. The sale of the generics business allows them to focus on their branded growing franchises and capital allocation. We believe that recent capital allocation has been smart. With the proceeds from the sale, they have reduced debt ($10 Billion), made a series of small purchases to build out their potential pipeline, and have repurchased a significant amount of stock at levels below our estimates of intrinsic value. Within the last six months, they have bought back approximately fifteen percent of the shares outstanding at an average price of approximately $215 per share[6]. While many companies buy back stock, few take such decisive action when undervaluation occurs. Presently the enterprise value of the company is $81 Billion, about half the value of what Pfizer was willing to pay fifteen months ago. Allergan also introduced a "social contract" with a promise not to increase prices more than 10% annually and recent open market purchases by the CEO further our confidence. If expected growth continues and headlines of the industries aggressive price increases fades to the back pages of the newspapers there is plenty of potential for the market to again "like" this profitable, conservatively financed global pharmaceutical company.

Cerner (CERN)

Cerner Corporation is a market leader in the healthcare IT industry that designs, develops, markets, and supports clinical and management information systems. From complex to simple, hardware to software, they have a critical role in the complex healthcare system. Their clients include leading health systems, hospitals, clinics, physician practices, laboratories, pharmacies, employers and consusmers. Long product implementation times, lengthy service contracts, and customizable software packages make the cost of switching providers high and transitions difficult. Most importantly we get the sense that Cerner's customers really appreciate the products and services they provide and do not have a desire to switch. This creates a durable competitive advantage. Cerner has an enviable record of revenue, profit and share price growth over the long term. Recent slowdowns in revenue growth, increased competition, and some clients delaying purchasing decisions until regulatory changes are settled, have weighed on the stock price in 2015 and 2016. Based on our research, the contributing factors to the recent

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[6] http://www.allergan.com/investors/financial-information/sec-filings

stock price declines appear to be temporary. As the healthcare system continues to focus on digitization and data analytics, Cerner sits right in the middle of reducing costs and improving care. Cerner has many of the characteristics of what we are looking for when we evaluate investments – i.e., a strong business led by honest and talented management; a long track record of creating shareholder value; and meaningful ownership alongside shareholders. Officers and directors own approximately 13% of the company and two of the three founders (from its 1979 inception) remain involved today[7]. We wish this company would have crossed our desks many years ago but we believe we have found a favorable entry point for investing in Cerner.

Conclusions

We balance the optimism we have for the companies we own, with the knowledge that we continue to operate in an environment where interest rates remain historically low and US stock market valuations remain elevated compared to historical standards.

Our goal is to keep managing the risk in the existing portfolio and continuing to look for new opportunities. The new opportunities are compared against each other and the current holdings in the portfolio. The present investing environment is a good fit for our management style. Flexibility, patience, and a focus on quality businesses run by solid management teams that can "make their own luck" are what we believe to be the keys to success in the coming years. Please look for our next letter in spring. In the meantime, if we may be of service and you would like to schedule a review meeting or discuss your personal financial plan, please contact us at 515-221-2546. We are always available to discuss this letter or any other items that may be of interest to you. Wishing you a Happy and Healthy 2017!

Respectfully,

Roger Grefe	Brian Grefe	Heidi Koster
Senior Vice President, Investments	Financial Advisor	Registered Service Associate

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[7] http://www.cerner.com/About_Cerner/Investor_Relations/Proxy_Materials/ 2016