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ValueWorks

quality assets. compelling valuations.

Volume 11,4 **Q4 2013**

Equity markets surprised investors with some outsized gains in 2013. Our portfolios participated fully in that advance with our Capital Appreciation Portfolios adding 47.0% over the full year (gross of fees; see p 4 for additional information).

The Dow added 29.7%, the S&P 500 gained 32.4%, and the NASDAQ topped both with a 40.1% advance. Fixed income investors fared less well, as the Merrill Lynch Domestic Master bond index posted a total return decline of -2.3%. Our returns were well above what even those robust index returns would lead one to expect.

Top 10 holdings*:

1. American Express Co.
2. Xerox Corporation
3. Boeing Company
4. Cliffs Natural Resources Inc.
5. Nokia Corp. 6.625% Due 05-15-39
6. Calpine Corp.
7. 3M Company
8. Paccar Inc.
9. Dow Chemical Company
10. Pfizer Inc.

—as of 12/31/13—

*see notes on p4 for additional Information

Given the torrid market advance of the past fifteen months, we have by degrees become less aggressively positioned. Markets do not move straight in one direction; we would not be surprised by some turmoil in the months ahead. Our absolute cash balances are higher today than they were when this advance started, so we do have the room to exploit a market hiccup. However, because I see us in the early stages of a multi-year economic expansion, I see greater risk in being under-invested than in being over-invested. And calling the timing of a near-term correction is ridiculously treacherous.

Meanwhile, the economy continues to expand because monetary policy is working. Low interest rates and a low cost of capital are fueling an economic expansion.

Because I do not accept the notion that this process is either "artificial", or close to an end, but is rather a driver of a normal business cycle, I see an extended period of economic expansion and a similarly extended market advance. The economic crisis has required a one-time step up in the size of the monetary base in order to keep capital circulating effectively through the system. This is what is reflected in the "QE" programs and the associated tremendous increase in the size of the Federal Reserve's balance sheet. That the Fed has begun to "taper" the amount by which it is increasing the monetary base is an appropriate reflection of an economy that is now beginning to function much more normally. My expectation is that the pace of asset purchases will decrease more quickly than current general views.

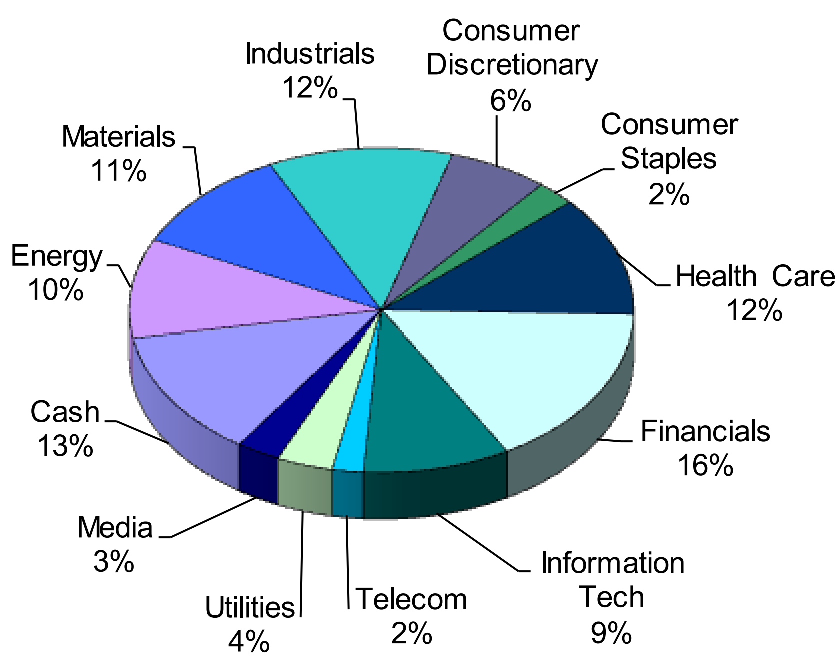
The current pace of "QE" reflects a very rapidly expanding monetary base. The focus on the size of the monetary base is reminiscent of the pre-Greenspan Fed construct of targeting monetary supply rather than interest rates. Viewed in that perspective, QE is not an artificial crutch, but rather a process by which the Fed effects a one-time step up in that base amount of money in the system. With that one-time increase now achieved, that QE process may quickly come to an end. Viewed in that perspective, I would expect the Fed to now turn back to targeting rates, cut back asset purchases, and allow the monetary base to stabilize close to current levels. While the markets will surely have some near-term gyrations around that process, I expect rates to stay generally low, and the economy to continue expanding.

Until recently the greatest threat to a continued expansion was the unsustainable fiscal deficit. However, a combination of solid economic growth and prudent policy decisions has put us back on a sustainable level. That the economy has continued to grow through this fiscal drag represents an important positive development. Further, Washington seems to have put a budget agreement in place that may last several years – thus another source of risk seems much less pressing. With these "fears" perhaps behind us, investors can be expected to shift their focus to the next largest risk. I see that as the large US trade deficit. That metric reflects an unsustainably large imbalance that will have negative consequences if not brought closer into balance. While those consequences likely have a very long fuse, it is an issue that deserves attention.

The key to our performance over the past year has been discipline. We stocked the portfolios with well valued equities and allowed time to work its magic without getting shaken from our course by the day to day market vagaries. While we have reduced exposure in some names that became more fully valued, the portfolio remains chock-full of very compellingly priced individual issues. And though some of those names are now much higher than they were a year ago, my reading of the math leads me to conclude that such a change in price reflects more on how extremely undervalued they were earlier than it does on their being fully priced today.

— Charles Lemonides, CFA

Sector Diversification--
Capital Appreciation Composite



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ValueWorks
critical thinking. independent research.

Defining our Philosophy:

At ValueWorks we define value investing as buying the best-quality assets at the best possible prices. We like to think of ourselves as bargain hunters: it is our goal to pay only $0.50 to $0.75 for $1.00 worth of assets. We evaluate the component parts of a company, assigning each of its assets a dollar value that, when added together, comprises the underlying value of the company; if this is higher than the company's stock price, we consider it an investment opportunity.

Defining our Process:

1) Identification. We monitor the financial markets to identify securities that match our investment criteria—focusing on opportunities that appear misunderstood by the general market.

2) Appraisal. First we identify the assets; then we appraise them. This allows us to determine the company's *underlying value*. We then decide whether the assets are of high quality and therefore likely to appreciate over time.

3) Assessment. Here we assess any claims against a company's assets; we then compare the market price of the claims to the company's *underlying value*. If a particular security trades at a discount, we identify factors that could eliminate the valuation gap and increase its price. We then make a decision on the purchase of the security.

4) Re-Evaluation. We continuously monitor our positions to determine if our original investment thesis still applies, taking necessary action to optimize our portfolio.

5) Exit. We exit a position when a security either reaches full valuation or changes in its outlook invalidate part of our original thesis.

Our objective is uncomplicated, but achieving it requires a high level of research, expertise, discipline and independent judgment. By applying this framework consistently we remove emotion from the investment decision making process, enabling us to capitalize on inefficiencies built into the market.

About our Portfolio Structure:

We believe risk can be better contained through educated security selection than through overdiversification. Consequently, our position sizes range between 3 – 5 % of the overall portfolio value. Fully invested portfolios tend to hold 25 – 35 individual investments.

We enter investments that we view as 25 – 50% undervalued and sell them when we see them as fairly priced. Our anticipated holding period tends to be one to two years which results in only modest portfolio turnover.

Because our decisions are based on research and sound fundamentals we view depressed price action on our securities as buying opportunities rather than sell signals.

We use senior debt and preferred instruments—offerings that can be easily misunderstood by traditional equity or fixed income investors—to gain equity type returns on safer vehicles.

About our Client Services:

ValueWorks provides independent investment management on an individual account basis. Our clients receive the benefits of owning securities directly, coupled with the advantages of having a dedicated portfolio manager.

Working directly with your financial consultant, we evaluate your investment profile and build a plan designed to meet your specific goals.

As a high-end investment alternative, you receive:

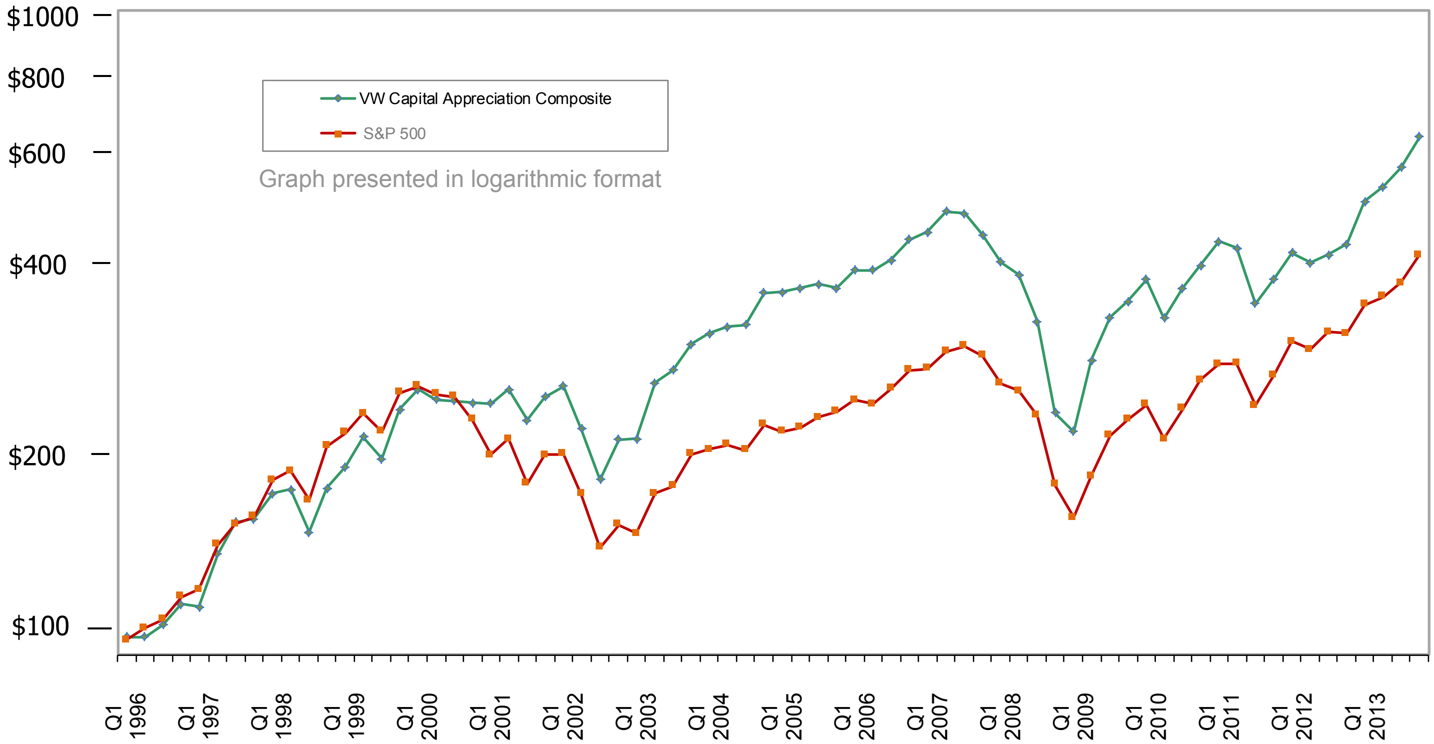
- Individual review of your portfolio requirements
- A separately tailored portfolio created and maintained to your investment objectives and risk tolerance
- Access to the Portfolio Manager on an ongoing basis with timely and responsive communication
- Flexibility to meet your changing tax requirements and investment needs
- Comprehensive quarterly performance reports.

Working within the framework of our value investment discipline, we build portfolios that cover a wide spectrum of risk-tolerance, from aggressive to much more conservative and income oriented.

ValueWorks Performance Review

4th Quarter: September 30th, 2013 -- December 31st, 2013

Historical Growth of $100 (gross of fees)



Trailing Performance Data

	ValueWorks' Capital Appreciation Composite			ValueWorks' Balanced Composite		
	Gross of fees	Net of Fees	S&P 500	Gross of fees	Net of Fees	Blended index*
2013 Q4	11.71	11.37	10.51	9.84	9.47	5.13
1 year	47.03	45.24	32.40	38.65	36.78	14.08
5 year	21.80	20.24	17.88	19.69	18.01	11.50
10 year	7.70	6.27	7.37	8.17	6.61	6.46
LIFE*	10.83	9.19	8.26	11.18	9.41	7.46

* Life is 18.00 years (inception, 1/1/1996)

*The "Blended Index" is a calculation comprised of 50% S&P 500 and 50% Merrill Lynch Domestic Master Bond Index.

The above benchmark indices are unmanaged indices. The benchmark performance numbers reflect the reinvestment of dividends and interest but do not reflect the deduction of any fees or expenses. ValueWorks' value investing style is not limited to the securities in any of the above indices and utilizes specific investment techniques which are not utilized in the above indices and which may or may not increase volatility. Returns include all dividends, interest, accrued interest and other cash flows received as they may result from the implementation of a particular investment strategy. Trade date accounting has been used. Results for the full period are time weighted. Accounts are included in composite at the start of the first full period under management. From 1996—Q1 1998 exiting accounts are included through the period in which they left. Starting in Q2 1998 exiting accounts are included through the last full period under management. Results were generated at other firms prior to 9/30/01. Information on other composites is availa-

As of 12/31/2013 the Capital Appreciation Composite consisted of 135 accounts and $93,295,177 in assets; while the Balanced Composite consisted of 56 accounts and $43,966,013 in assets. Together this represents 98.45% of total accounts and 54.40% of total assets.

Past performance is not a guarantee of future results. This material is approved for client use.

PROCESS:

1. Identification We monitor the financial markets to identify securities that match our investment criteria—focusing on opportunities that appear misunderstood by the general market.

2. Appraisal First we identify the assets; then we appraise them. This allows us to determine the company's *underlying value*. We then decide whether the assets are of high quality and therefore likely to appreciate over time.

3. Assessment Here we assess any claims against a company's assets; we then compare the market price of the claims to the company's *underlying value*. If a particular security trades at a discount, we identify factors that could eliminate the valuation gap and increase its price. We then make a decision on the purchase of the security.

4. Re-Evaluation We continuously monitor our positions to determine if our original investment thesis still applies, taking necessary action to optimize our portfolio.

5. Exit We exit a position when a security either reaches full valuation or changes in its outlook invalidate part of our original thesis.

	Total Firm	Composite Assets		Annual Performance Results			
Year End	Assets (in Millions)	USD (in Millions)	Number of Accounts	Composite: Gross	Composite: Net	S&P 500	Composite Dispersion
2013	252	93	134	47.03%	45.24%	32.40%	2.54%
2012	167	70	150	12.92%	11.49%	15.98%	1.84%
2011	160	75	193	-4.58%	-5.80%	1.85%	1.64%
2010	165	81	221	13.71%	12.15%	15.04%	5.25%
2009	152	78	241	48.83%	46.92%	26.48%	7.86%
2008	112	58	311	-46.97%	-47.68%	-36.96%	8.58%
2007	295	178	515	1.50%	0.14%	5.49%	5.93%
2006	267	159	411	19.08%	17.44%	15.79%	7.25%
2005	209	119	340	1.81%	0.31%	4.91%	3.73%
2004	165	78	158	20.03%	18.42%	10.88%	4.20%
2003	121	49	93	40.31%	38.29%	28.69%	4.71%
2002	75	33	58	-13.97%	-15.23%	-22.10%	3.53%
2001	85	36	51	2.05%	0.64%	-11.88%	8.31%
2000	80	35	69	2.28%	0.68%	-9.11%	6.64%
1999	81	36	79	32.56%	30.46%	21.04%	15.60%
1998	66	26	78	11.60%	9.68%	28.58%	6.03%
1997	39	9	30	35.65%	32.96%	33.36%	3.84%

DISCLOSURES

Past performance is not indicative of future results.

Capital Appreciation Composite *contains all accounts with a Capital Appreciation mandate. For comparison purposes the composite is measured against the S&P 500 Index.*

ValueWorks has prepared and presented this report in compliance with the Global Investment Performance Standards (GIPS®).

ValueWorks is a separate registered investment adviser. Prior to September 30th, 2001, ValueWorks was a subdivision of M&R Capital. The firm maintains a complete list and description of composites, which is available upon request.

Results are based on fully discretionary accounts under management, including those accounts no longer with the firm. Past performance is not indicative of future results.

The U.S. Dollar is the currency used to express performance. Gross returns are shown as supplemental information and are stated gross of all fees and transaction costs; net returns are reduced by all fees and transaction costs incurred. Wrap accounts pay a fee based on a percentage of assets under management. Other than brokerage commissions this fee includes investment management, portfolio monitoring, consulting services, and in some cases, custodial services. Wrap accounts make up 100% of the composite for all periods shown. Wrap fee schedules are provided by independent wrap sponsors and are available upon request from the respective wrap sponsor. The annual composite dispersion presented is an asset-weighted standard deviation calculated for the accounts in the composite the entire year beginning December 31, 2001. From January 1, 1996 to December 31, 2001 dispersion reflected an equal weighted dispersion. Additional information regarding the policies for calculating and reporting returns is available upon request.

The management fee schedule is as follows: Low and high rate for wrap sponsors: 1.25% and 2.75%, respectively. Fee schedules from individual wrap sponsors are available upon request. Actual investment advisory fees incurred by clients may vary.

The Capital Appreciation Composite was created December 31, 1995. Performance presented prior to October 1, 2001 occurred while the Portfolio Manager was affiliated with two prior firms and he was the only individual responsible for selecting the securities to buy and sell. ValueWorks' is in compliance with the GIPS standards for the period October 1, 2001 through December 31, 2007. In addition, a performance examination was conducted on the Capital Appreciation Composite beginning October 1, 2001.

For more information about ValueWorks Capital Appreciation Composite and our other composites please visit valueworksllc.com or call 212.819.1818
This material is approved for client use.