YOUNG ENTERPRISE SHARES (YES) REVIEW

Second Quarter 2015

"PERFECT STORM" PASSED, DARK CLOUDS PERSIST

PERFORMANCE COMMENTARY

Anecdotally, on March 9, 2015 at the World Investors Forum (WIF) in Davos, Switzerland, Dr. Petteri Taalas, noted Finnish climatologist/psychologist, was a keynote speaker. Surprisingly, his topic was not the socio/economic effects of global warming, AKA climate change, but the pervasive feeling of ennui felt by the captains of industry and barons of Wall Street.

It was the 6th[th] anniversary of the near death experience of the 2009 "perfect storm" in the global economies and financial markets; an event whose memory has kept businessmen and investors in a state of persistent anxiety. Decision makers have been unable/unwilling to return to their normal levels of risk taking in economic (capital and consumer spending) and investment (equity ownership) opportunities. As a result, global economies lingered in a fifth year of subpar growth.

Petteri's knowledge of the depressive psychological effects (kaamos) of the lengthened Nordic winter's nights (den morke tiden) was invaluable in counseling business leaders, who had spent nearly a decade in a state of malaise. A true understanding of and proscriptive cures for the current economic stagnation could not be left to complex econometric modeling. The problems might well be psychiatric and insights into human behavior might prove beneficial to investors.

The first half of 2015 exemplified this phenomenon of continued angst. Concerns over China's slowing economy and volatile stock market, negative 1Q GDP growth in the US, over analysis of an over transparent Federal Reserve, another act in the Greek tragedy, Mideast tensions intensifying locally and spreading globally, and an increasing awareness of the insecurity of our cyber security cast a pall over investor sentiment. These claps of thunder and bolts of lightning drove investors to shelter.

For 2Q, the total return of the S&P 500 was a modest 0.3 %, bringing six month returns to 1.2%. While the overall market averages made little progress, there was a distinct preference for growth stocks and an aversion to industrially oriented sectors. The concerns of slowing GDP growth weighed heavily on investors.

Individual sector performance was relatively tight with all ten groups within a plus/minus 5% range. Six were positive, two neutral and two negative. Health Care (+5%) and Consumer Discretionary (+4%) were market leaders, extending their strong showing in 1Q. Worst performing were Utilities (-5%) and Energy (-1%) extending their 1Q losses.

PORTFOLIO COMMENTARY

The largest positive contributor to the portfolio's 2Q return was **NeoPhotonics (NPTN)**, a manufacturer of communications equipment. It rose 35.3% on a report of strong sales and expanding profit margins. **Senomyx (SNMX)** is nearing commercial introduction of it sweetener, Sweetmyx and was rewarded with a 21.5% gain. A leading participant in the rapidly increasing electronic content in motor vehicles, **Mentor Graphics (MENT)** advanced 10.0% as the marriage between cars, media and communication intensifies. **Universal Display (OLED)** rose 10.7% spurred by strong sales to Samsung for Galaxy phones and Apple for watches. **Osiris Therapeutics (OSIR),** a leading regenerative medical company, rose 10.7% in the quarter on an agreement to develop an osteo product with Stryker.

On the negative side, **Maxwell Technologies (MXWL)** declined 25.9% as sales of its ultra capacitor to Chinese transportation companies fell. **Numerex (NMRX),** a supplier of machine to machine enterprise solutions, fell 25.1% as profits declined and they guided lower for the year. Biotechnology firm **Cytori Therapeutics (CYTX)** has raised concerns as its balance sheet is weakening and may need financing. It declined 52.8%. A leader in 3D measurement equipment, **Faro Technologies (FARO)** was down 24.8% as economic concerns and increased price competition at the low end unnerved investors. Gene therapy company **Sangamo Biosciences (SGMO)** had a heart drug fail its phase 2 trial and the shares declined 29.3%.

PORTFOLIO ACTIVITY

There were no portfolio changes during the quarter.

MARKET COMMENTARY

Post the 2008-9 “perfect storm” in global financial markets and economies, the weather, in the minds of economic and stock market forecasters, remained heavily overcast. Recurring nonrecurring events clouded investors' perspectives and tempered their enthusiasm and bullishness.

One needs only to recall, almost embarrassingly, the near panic predictions of: a plunge off the fiscal cliff, a government debt ceiling caused default, a Japanese tsunami's nuclear cloud, a global Ebola epidemic, a Russian invasion of Europe, a breakup of the European Union, a disintegration of Mideast boundaries, massive migrations of the needy and oppressed, and an impending death spiral of China….to understand the amount of “cloud seeding” that has occurred during the past the six years.

In the first half of this year, many of these storms persisted in dampening spirits. In addition, negative US GDP in 1Q brought into question the vigor/sustainability of the American economy.

Dr. Taalas, donning his psychologist cap, put forth a number of recommendations to assist the conferees in dealing with the constant forecasts of inclement weather;

1. Think in relative rather than absolute terms. Don't compare the current geo-political/economic conditions with prior periods, especially the 1990's. While overall growth is subpar, there exist a multitude of opportunities in selected growth sectors including big data, telecommunications, social media, health care and infrastructure. Be selective and opportunistic.
2. Don't double count the negatives. Normally the economy grows at 4+% and recently, because of the myriad of headwinds, it is stuck in the mid 2% area. However, most of the current negative headlines we fret over are already included, creating the subpar growth. They need not be discounted a second time.
3. Don't be unduly influenced by the "dark clouds." They will be with us for the rest of this economic cycle. They should be treated as an annoyance, not an inhibitor in making thoughtful investment decisions. Remain positive and proactive.
4. While difficult advice to give, the eventual "cure" for investors' anxieties would be to successfully endure another storm. After experiencing a traumatic event, psychiatrists believe relief can be gained by a simulated reliving of the experience. Surviving a milder recession and market retreat might be the most successful and lasting psychological remedy.

Dr. Taalas went on to add that this "cure" (recession) was most likely years (2-3) away. There did not appear, in his forecastable horizon, the necessary conditions for an economic setback and meaningful stock market decline. Interest rates are unlikely to spike, as Japan and the EU are engaged in "nonconventional" easing of monetary policy. The economy is on a glide path of moderate growth with a comfortable output gap in manufacturing capacity, labor and bank liquidity. Corporate profits are expected to show continued growth as there is little upward pressure on the cost side of corporate income statements. Investor sentiment, as exemplified by the mood of the audience, is not excessive. The next few years will look much like the past five.

Dr. Taalas closed by saying that for now, the conditions necessary for a continuation of the economic recovery and stock market advance are in place. The concerns over the persistent signs of inclement weather should be minimized and energies constructively spent on participating in the remainder of the 2009 - 20?? bull market.

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