NORTH STAR
ASSET MANAGEMENT, INC.

April 2015

INVESTMENT UPDATE

Executive Summary

- With the economy expanding at a nominal rate close to its 20-year average and with the unemployment rate continuing to move down towards 5%, we believe the Federal Reserve is running out of excuses for keeping short-term interest rates near zero.

- Although the Fed will likely start raising the federal funds rate later this year, monetary policy will remain highly accommodative to economic growth as increases are likely to be very gradual, taking years before they become neutral and even longer before they become restrictive.

- With the Fed indicating short-term interest rates will likely exceed 3% by the end of 2017 and with the 10-year U.S Treasury bond currently yielding just 1.92%, the bond market appears overvalued and we continue to recommend defensive bond portfolios with relatively short durations.

- While earnings for the energy sector are now expected to decline by over 50% for 2015, the remaining sectors that account for 92% of the S&P 500 are expected to experience +6-7% growth, despite the headwind of the strong U.S. dollar. Although expectations for earnings growth from the S&P 500 as a whole this year are only in the low single digits, focusing too much on this average hides the reasonably good growth occurring in the rest of the market.

- Small capitalization and foreign stocks outperformed the S&P 500 in the first quarter of 2015 after significantly underperforming last year.

Stronger Economy Will Force the Fed to Start Raising Short-Term Interest Rates This Year

The Federal Reserve is nearing a pivotal moment as it prepares to increase the federal funds rate for the first time in over nine years. While the stock market has a tendency to temporarily react negatively when the Fed positions itself for a rate increase, we believe the move is long overdue and that it should be viewed positively. Over the past few years the Fed has used a variety of excuses to avoid raising rates, most recently pointing to modest inflation, weak nominal wage increases, and a strong U.S. dollar. However, nominal GDP growth in the U.S. has expanded at an average annual rate of +4.1% over the past two years, well above the ten-year average of +3.5% and very close to the +4.4% rate of growth experienced over the past 20 years. Additionally, the unemployment rate has declined from 6.7% a year ago, to 5.5% today, driven by the strongest pace of new job creation in over 15 years (See Graph 1). These signs point to an economy that is very healthy and one that does not need artificially low interest rates to thrive.

Graph 1: Private Sector Job Creation at the Fastest Rate in Over 15 Years

While the Federal Reserve may not want to raise interest rates, based on their belief that the low rates are responsible for the current health of the economy, they are running out of excuses to avoid doing so. For example, core-inflation (excluding food and energy) is running just below the Fed's 2.0% long-term target, wage increases should start to improve now that much of the excess slack in the labor market has been removed (inflation-adjusted wage increases are already at the highest level since 1979), and the strong dollar is really a product of the relatively strong U.S. economy and should not be looked at as an excuse to keep interest rates artificially low.

Given this backdrop of healthy economic growth, we believe the Fed will be forced to start increasing the fed funds rate later this year. While some will argue that this will be bad for the economy, and the initial market reaction may also be negative, we believe any market weakness should be viewed as a buying opportunity as these rate hikes will be a product of an economy that is no longer in need of near-zero interest rates. Also, while we believe the Fed will begin to raise rates this year, we also expect monetary policy to remain relatively accommodative over the next few years as the pace of increases will be very gradual (See Graph 2). Therefore, while we expect the Fed to become "less loose" with its monetary policy this year, it will

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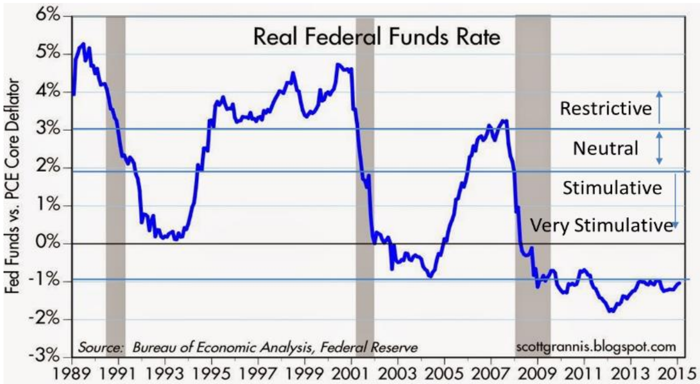
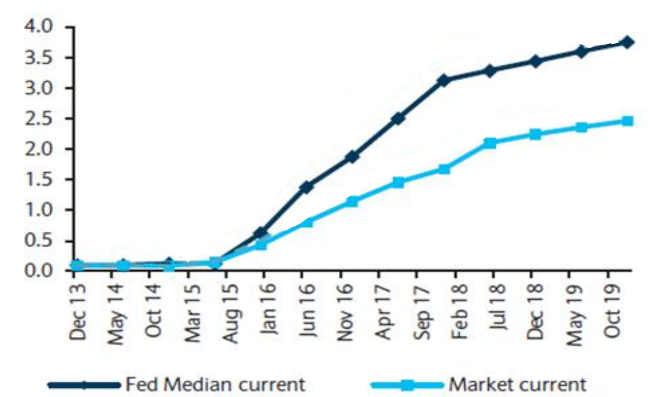
be years before it becomes neutral, and even longer before it becomes restrictive.

Graph 2: Rates Have a Long Way to Go Before They Are Restrictive to Economic Growth



With the underlying economy remaining strong and with the Fed poised to begin raising the fed funds rate later this year, we believe broader interest rates will be heading higher as well. The Fed provides a "dot-plot" graph (See Graph 3) that lays out the individual members' expectations for the fed funds rate at various points in the future. Currently, this graph is indicating that the average expectation of all Federal Reserve Board members is for rates to move higher, reaching 3.125% by the end of 2017. If the Fed is right and short-term interest rates go over 3% in the next few years, then the bond market, with the 10-year U.S. Treasury bond currently yielding just 1.92%, appears overvalued. Therefore, while there may be some flattening of the yield curve as the Fed raises short-term rates, we expect interest rates across all maturities will move higher and continue to recommend maintaining defensive bond portfolios with relatively short durations.

Graph 3: Fed "Dot-Plot" Indicates Modest, but Gradual Rate Increases



Source: FOMC, Bloomberg, Barclays Research

Significant Decline in Oil Profits Hides Underlying Strength in Earnings

Earnings growth for the S&P 500 in 2015 will be slower than experienced last year as increased pressure from a strong dollar on foreign-generated profits and the impact of lower oil prices on oil industry earnings are masking relatively healthy earnings growth from the rest of the index. The consensus calls for S&P 500 earnings growth for the year to be in the low single digits, down from expectations in the high single digits at the beginning of the year.

With just under half of S&P 500 revenues generated overseas, and with the dollar having appreciated by over +8% against a broad basket of global currencies since the beginning of the year, lowered expectations on these foreign earnings are justified. Likewise, with the price of oil falling by over 50% from a year ago, a reduction in earnings growth from oil producers is also warranted. However, while earnings for the energy sector are now expected to decline by -55% for 2015, the remaining sectors that account for 92% of the S&P 500 are expected to experience +6-7% growth, despite the headwind of the strong dollar. Although expectations for earnings growth from the S&P 500 as a whole this year are only in the low single digits, focusing too much on this average hides the reasonably good growth occurring in the rest of the market. Additionally, the benefit of lower oil prices for non-oil producing companies is more difficult to determine and may provide for stronger earnings growth for the year than is currently expected.

With the S&P 500 Index currently trading just above the high end of its long-term average valuation range of 15-16x next twelve months' earnings, equities appear reasonably valued. We continue to recommend that our clients maintain equity allocations near the mid-point of their targeted range.

Small Caps and Foreign Stocks Outperform

Following last year's significant underperformance relative to the large capitalization S&P 500 Index, small cap stocks (Russell 2000) and foreign stocks (EFEA) both outperformed in the first quarter, rising +4.3% and +4.9% respectively, compared to the +1.0% return experienced by the S&P 500. Emerging market stocks (MSCI EM Index) also outperformed, rising +2.2%. The bond market (Citi Broad Bond Index) generated a total return of +1.6% in the first quarter as the 10-year U.S. Treasury yield declined -25 basis points to 1.92% on strong demand from foreign markets where yields are even lower than in the U.S. With the Fed expected to soon begin raising interest rates for the first time in nine years, some increase in stock market volatility is likely during the remainder of the year. However, our philosophy of investing in high quality, consistent growth companies should enable client portfolios to more comfortably absorb the corrections along the way and continue to enjoy strong returns over the long term.

In accordance with SEC Rule 204-3(b), our Form ADV is available upon request. Please call or write to Susan C. Beaver, North Star Asset Management, Inc, 59 Racine St., Suite A, Menasha, WI 54952.