Morris Capital Advisors, LLC

Investment Commentary
June 30, 2012

Lose the Swimmies!

As the end of June and the July 4th holiday approached much of our nation was gripped in an oppressive heat wave. Most people sought some respite from the weather at the pool, the lake, or the beach. For us, it was the pool, and it was crowded, with adults wishing for some quiet space, teenagers splashing and creating a commotion, and the young ones in their swimmies. I'm sure that you have seen swimmies. They are inflatable devices that fit on the arms between the elbow and shoulder that keep the head above water for safety. I even saw one youngster, with a overprotective parent or nanny, using a flotation ring and swimmies.

Those safety devices are great. They keep the child upright, head out of the water, and minimize the risk of an accident. The youngster can happily splash along in the pool without ever going anywhere. But the flip side, is that they will never learn to swim with those things on, because to learn to swim you need to put your face in the water, and yes, sometimes end up with it in your nose and mouth. It isn't fun, but it is the only way to learn how to survive and improve, and that got me thinking about our economy and the financial markets.

Our markets have been bouncing up and down for more than a decade like that child in the flotation ring and swimmies. Our Federal Reserve bank, and central bankers around the world, have employed increasingly complex policy initiatives to stimulate economies and prop up the financial markets, all at the behest of investors and politicians. It started with Alan Greenspan simultaneously raising interest rates and jacking up money supply growth at the turn of the century amidst the Y2K scare. Convinced of his brilliance, he persisted in his monetary engineering, ignoring the growing real estate bubble and increased risk taking among leveraged investors. These policies led directly to the current zero interest rate policy, quantitative easing to print money and buy US Treasury securities, massive liquidity to prop up the banks and stock markets, and the purchase of mortgage backed securities to lower interest rates and support the housing market.

But ultimately economic reality will prevail. The continued money printing will encourage governments to spend even more, ultimately exceeding borrowing capacity, and we will be confronted with the stark reality that there is a limit to the effectiveness of all these policies at some point. It is already happening in Europe, and the US may not be far behind.

In many respects, we are all to blame for this mess. As investors we clamor for support when the market goes down. As consumers we want action to stimulate the economy and raise our standard of living, and as citizens we expect political solutions whenever things get tough. Because each one of these artificial measures has a secondary, often offsetting effect, we are faced with a sluggish economic rebound, weak labor markets, stagnant wage growth, and investment markets that seem to bounce up and down, but ultimately go nowhere. Like the youngster in the pool, we may feel comfortable with the all the financial safety nets around us but are destined to do little more than tread water until we encourage private business to take the risk necessary to invest and grow. Doing so will not only reinvigorate our economy, but will refocus our attention on sound business fundamentals rather than continued artificial economic engineering.

The frustration of many investors with the mediocre returns in the equity markets over the past decade is rooted in the increasing influence of central banking and governmental policies. As markets reacted to these factors returns have become more uncertain and investment strategies designed to exploit differences between these initiatives, their secondary effects, and market reaction to them have become more prevalent. These investment styles, based on high turnover, leveraged portfolios, and event-driven trading, have sometimes been victimized by the very safety net policies that they were designed to exploit, increasing market volatility. As the effectiveness of central banking interventions continues to decline the return generated by strategies based upon them will also decline.

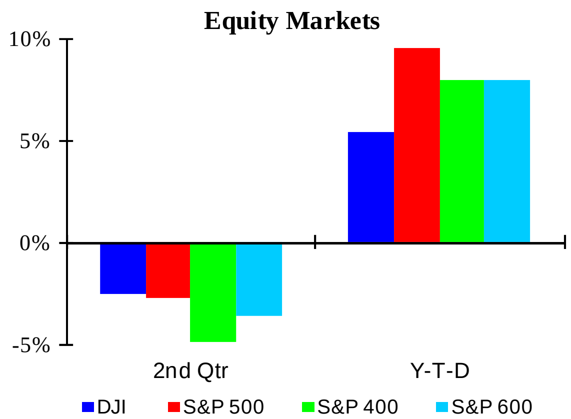
We believe that the markets are already beginning to recognize the declining impact of central bank intervention, paving the way for a return to investing based on sound business fundamentals. This will shift the focus back to identifying individual companies that have the financial resources to survive and grow in an uncertain economy. For us, this means searching for companies that have strong earnings, the capability to grow, a sound financial structure to support that growth, and significant free cash flow. We will seek to invest in companies that are priced attractively relative the their underlying valuation, and have management with the proven ability to execute. These companies know how to swim, and may get a mouthful of water from time to time, but are well positioned to generate excellent long-term investment performance.

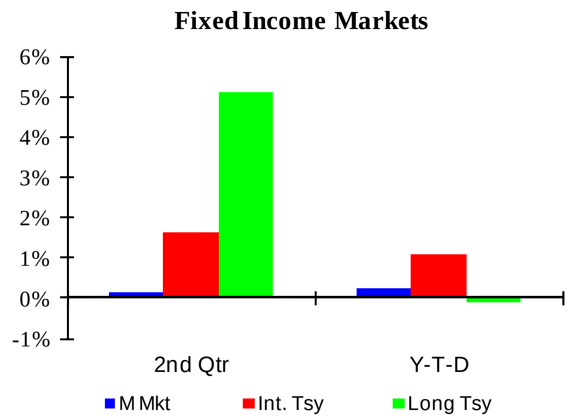
Sincerely,
Daniel A. Morris

Market summaries on reverse page

Morris Capital Advisors, LLC

Market Summary
June 30, 2012





The equity markets struggled once again with the implications of an unfolding recession in Europe and slowing economic growth everywhere else. A number of companies reinforced these concerns as the quarter came to an end with modestly disappointing revenue guidance. U.S. investors in particular are beginning to focus on the fall election campaign, the so-called “fiscal cliff” that could dramatically cut federal spending in the next fiscal year, and the declining effectiveness of Federal Reserve intervention. Equity markets posted modest declines across all capitalization ranges.

Prices of US Treasury securities enjoyed strong gains in the second quarter, especially in the longer-dated maturities. The combination of slowing economic growth worldwide, and the prospect of financial contagion spreading to the largest economies in Europe, drove a renewed flight to quality. Yields on 10-year Treasuries broke decisively below the 2.0% level, closing the quarter at 1.6%. While these levels haven't been seen in a very long time, investors in Germany and other strong European economies demonstrated that interest rates could go lower still, by driving yields in some to maturities to less than zero.