September 2013

Viewpoint

Baird Investment Management (BIM) manages high-quality portfolios for high-net-worth individuals and institutional clients.

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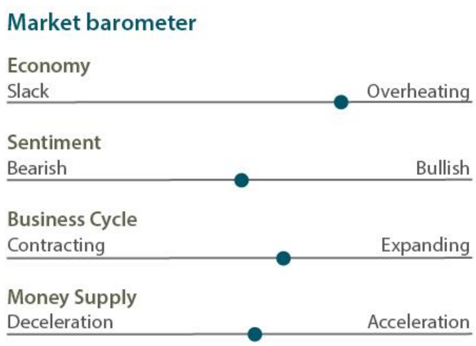
Baird Investment Management

"If you don't drive your business, you will be driven out of business."

– B.C. Forbes



Source: MTI, Investors Intelligence, Bloomberg

Market update *as of 8/31/13*	MTD	YTD	Trailing 12 Months
Dow Industrial Average	-4.1%	15.0%	16.1%
S&P 500	-2.9%	16.2%	18.7%
Russell 1000® Growth	-.17%	15.7%	16.4%
Russell MidCap® Growth	-1.9%	19.5%	24.0%

Source: Russell, APL

Revisiting the Manufacturing Renaissance

One of our key investment themes has been a U.S. manufacturing renaissance as highlighted in our March 2012 Viewpoint. This resourcing trend is being driven by U.S. efficiency, attractive labor markets, cheap power supply and high transportation costs. Now, eighteen months later, we revisit this theme as we have seen evidence that it has gotten stronger.

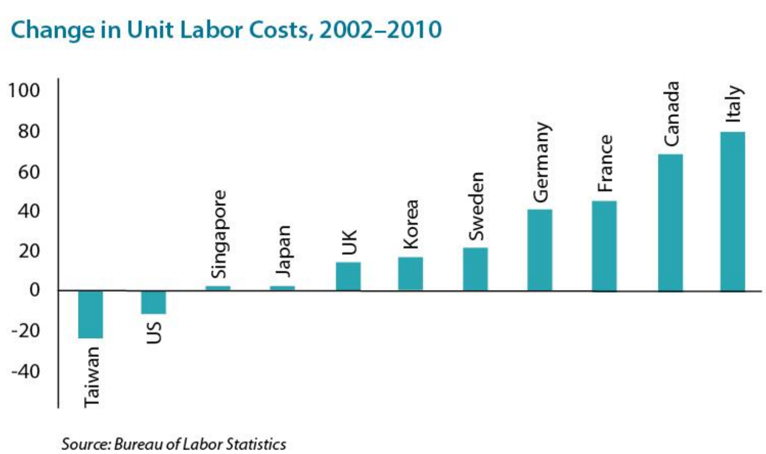
The United States has historically had a number of key advantages, including a well-established rule of law, labor market stability and well-developed infrastructure. However, despite these advantages, the U.S. has seen a production migration offshore over the past two decades given low international wages, growing foreign markets, relatively lower taxation and lack of foreign regulation.

Nonetheless, as we discussed in our Viewpoint last March, the emerging markets have experienced big wage increases, and Europe continues to embrace rigid labor market laws. As a result, this outsourcing trend has reversed, and the relative attractiveness of the U.S. has again increased – hence, the manufacturing renaissance.

Since we wrote our original Viewpoint, the backdrop has only gotten better and there have been a number of concrete examples of the manufacturing renaissance in action. Perhaps the biggest change has been the relative cost to run a manufacturing plant as the U.S. has benefitted from an unprecedented energy boom.

COUNTRY	NATURAL GAS PRICE – APRIL 2013
Japan	$17
Korea	$17
E.U.	$13
U.S.	$4

In addition, consider that chief executive officers making plant location decisions are primarily concerned with the proximity of the end client and the ability to control costs into the foreseeable future. The U.S. is the only country that has been able to keep its manufacturing unit labor costs steady for more than 30 years, driven mostly by our steadfast devotion to efficiency. Currently, many of the BRIC nations (Brazil, Russia, India and China) are experiencing high inflation levels that could cause further wage increases and/or increased operating costs. According to a forecast from the Hay Group, 2013 pay will rise across the board for the BRIC countries: Brazil (5.5%), Russia (9%), India (10.5%) and China (9.5%). In Brazil, unemployment has fallen from 14% in 1998 to under 6% recently, which has resulted in very tight labor markets. This is not a backdrop that many CEO's will find comforting in assessing future wage forecasts.



Furthermore, businesses know that European labor laws make it very difficult to react to changing market conditions. An article in the Wall Street Journal from August 9th highlights the problems in Europe. It details how Fiat has left five car factories in its home country of Italy idle while paying the workers to stay home. Contrast this with the 18 plant closures that happened in the U.S. in the aftermath of the 2008 financial crisis. This flexibility is appreciated by businesses when considering making investments. For example, Honda Motors announced on August 7th that it will expand an engine plant in Ohio and Toyota Motors announced in June 2013 it will invest $30M to expand a plant in Indiana. However, one of the biggest announcements was that Airbus, which began as a consortium of European aerospace companies, broke ground in April for its first U.S. manufacturing facility in Alabama. Not to be outdone, U.S. companies Apple and General Electric spent $100 Million and $800 million respectively to reopen manufacturing facilities in the U.S. General Electric CEO Jeffrey Immelt stated: "I don't do it because I run a charity; I do it because I think we can do it here and make more money."

Further proof is in the economic activity of traditional manufacturing states. Nancy Lazar of Cornerstone Macro points out manufacturing states have clearly outperformed non-manufacturing states since 2010. These states have 3 key characteristics: they are rust-belt states, energy-driven and business-friendly. Employment in these 16 states (MI, SD, ND, IN, WA, ID, WY, IA, OH, KY, WI, UT, VT, TN, MT, TX) has risen 11% from the trough compared to only 5% in the non-manufacturing states.

Rockwell Automation is one example of a company in our portfolios that benefits from building and expanding manufacturing facilities in the U.S. Rockwell is at the heart of the move towards automation that allows factories to use more machinery and fewer employees. This trend is not isolated to the United States, but we have been the most consistent practitioner.

Another beneficiary of resourcing, as well as the domestic energy boom, is Union Pacific. Rail is the most efficient means of transporting both finished and intermediate goods across the country. In addition, oil companies have increasingly been using the railroads to transport oil when pipelines are either unavailable or at capacity.

The renaissance of manufacturing in America is a long-term theme that we expect to be in place for many years.

To learn more about Baird Investment Management (BIM) and our products, please contact us at 800-792-4011 or 414-765-7246. Visit us online at bairdinvestmentmanagement.com.

The S&P 500 Index is a representative sample of 500 leading companies in leading industries of the U.S. economy. The Russell 1000® Growth Index measures the performance of those Russell 1000® companies with higher price-to-book ratios and higher forecasted growth values and is a large-cap index. The Russell Midcap® Growth Index measures the performance of those Russell Midcap companies with higher price-to-book and higher forecasted growth values. The stocks are also members of the Russell 1000® Index. The Dow Jones Composite Average Index is computed from the stock prices of 30 of the largest and most widely held public companies in the United States.