Sheaff Brock

Innovative Portfolios for Intelligent Investors™

MARKET UPDATE
April 2016

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"In America, anyone can become president. That's the problem."

George Carlin

In This Monthly Update

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Prior letters posted at sheaffbrock.com in the newsletters tab

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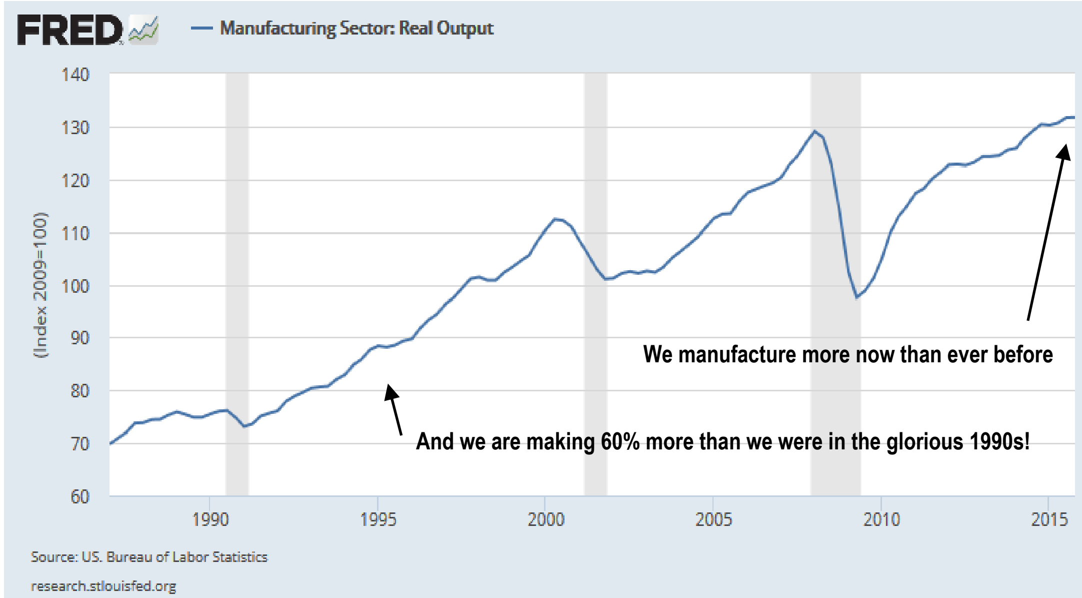
America is Already Great

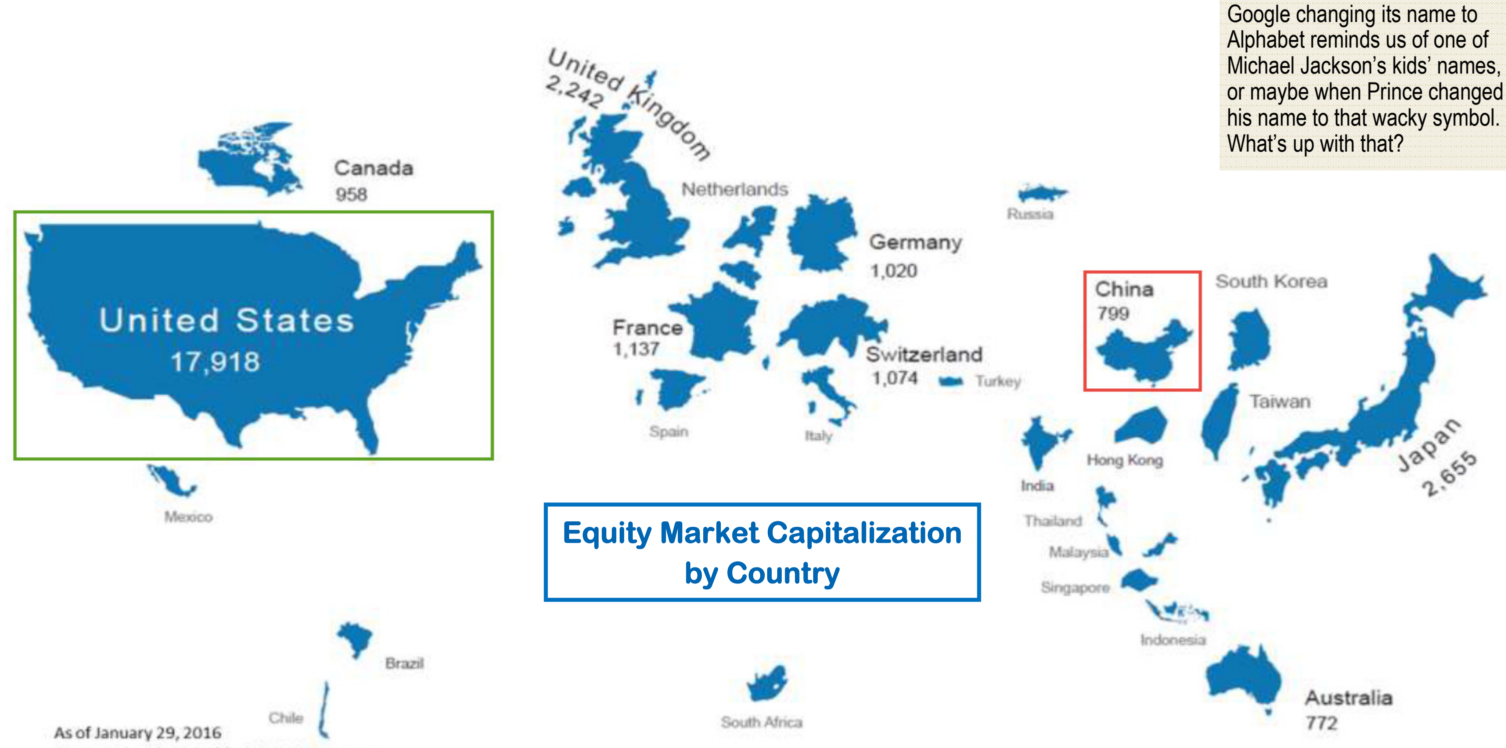
There is a storm of nonsense spewing out of politicians' mouths concerning the U.S.' position in the world. From just listening to those folks, you would think we are just one step ahead of Greece and that the rest of the world is passing us by. In the Midwest and Northeast, they will soon be giving speeches in front of some shuttered factory and drone on and on about the demise of American manufacturing. This is nonsense. Data released from the Fed shows manufacturing output is the highest EVER. We make more stuff in America now than we have ever made! Granted, there are fewer people making all of that stuff, which is called productivity.



The manufacturing phenomena is no different than farming. A century ago about 40% of the population farmed and 22 million horses pulled plows and wagons. Today less than 2% of the workforce farms and they use 5 million tractors. Crop yields have increased from 25 bushels an acre to 160. Farmers today grow five times as much corn as they did in the 1930s, on 20% less land. Would America be better if we went back to the old farming days? Of course not. Manufacturing, just like farming, is alive and well just employing less people.

Political gibberish abounds about the U.S.' financial influence too. The below map sizes each country by the size of it's total stock market capitalization. The U.S. market is about $18 trillion. Our equity market capitalization is *bigger than the rest of the world combined*, and 7X bigger than number two , Japan! Look at China, it is less than $800BB. Our market is 20X bigger than China's. When our market falls 5%, that is the equivalent of wiping out the entire Chinese equity market. China's market has to go up 20%, to equal our market going up 1%. Just two companies combined, Apple and Alphabet (Google), are 50% bigger than the size of China's entire market! No matter what the politicians say, America is dominant and is al-

Google changing its name to Alphabet reminds us of one of Michael Jackson's kids' names, or maybe when Prince changed his name to that wacky symbol. What's up with that?



- This map illustrates the dominance of the US stock market.
- The capitalization of the US market is $17.9tn (MSCI) as of January 29, 2016, and it currently represents 53.4% of world market capitalization, the highest since November 2003.
- The next largest equity markets are Japan, UK, France, Switzerland, Germany and China.

ready great!

<u>V-shaped Markets and Shorts</u>

Above is a chart of the S&P 500 for the first quarter of 2016. The first quarter ended with the S&P 500 almost where it started. Several years from now, people may look back at the quarterly return and think, “Oh, that quarter was a yawner...the S&P moved about 1%.” In reality it was painfully difficult, with a V-shaped market downdraft and recovery. An 11% drop, followed by a 13% gain.

Since 1932 there have been three previous V-shaped first quarters; 1980, 2003, and 2009. Following the three previous

S&P 500 9-Month Gains After Big 1Q Swings

First Quarter	Max Decline	Max Gain	Rest of Year
1980	-17.1%	+12.6%	+32.98%
2003	-14.1%	+11.9%	+31.09%
2009	-27.6%	+23.1%	+39.76%

Source: Bespoke Investment Group, “Down and Up,” March 28, 2016

times, the balance of each year was stellar, charging ahead by over 30%.

1980 was an election year, Reagan/Carter, but the others weren’t. No one knows what the balance of 2016 holds, especially considering this year’s goofy election, but the precedence is there to support a nice surprise. Fuel for a rally could come from short-sellers. Eventually a short position <u>must</u> be bought, which creates built-in buying pressure. Today, there is over $1 trillion in equity value sold short. According to Bloomberg, this is the largest amount short since March of 2009.

The arrow above shows the last time there was over $1T short. We aren’t saying that the market is going to explode up like it did in March of 2009, but short covering does provide upside bias.

<u>Portfolio Updates</u>

In the first quarter, growth stocks were down, value stocks were flat to slightly up, and generally, there was a fight to safety with utilities and telecom doing well. Healthcare and financials performed poorly (which may be a function of political winds). Below are updates on our 5 biggest portfolios.

IntelliBuilD Growth™

After a first quarter of having between 32 and 23 stocks in the portfolio, as of this week we are finally back to fully invested. IntelliBuilD is the blend of 33 American stocks from *Investors Business Daily’s* two lists, IBD 50, and New America. It tends to be heavily weighted toward mid-cap and small-cap stocks, which adds to volatility. Early in the quarter we were clipped out of several stocks after they breached the -11% soft stop threshold. The current thirty-three stocks represent 21 different industries. The average market cap of the list is now $23 billion, which has increased over the last few months. It is interesting that bigger companies are now coming into the IBD lists. Of the 33 stocks, 16 are small-cap (under $5BB), 8 are mid-cap ($5BB to $10BB) and 9 are large-cap.

<u>Here are IntelliBuilD holding stats as of 4/12/16:</u>

Average trailing P/E	18
Average Year over Year Sales Growth	12%
Average Year over Year EPS Growth	35%
Average Return-on-Equity	35%

<u>Here are the stats for the S&P 1500* of 4/12/16:</u>

Average trailing P/E	25
Average Year over Year Sales Growth	3%
Average Year over Year EPS Growth	14%
Average Return-on-Equity	23%

*S&P 1500 index consists of the S&P 500 large-cap stocks, S&P 400 mid-cap stocks, and 600 small-cap stocks

Our portfolio’s P/E is 28% lower, sales growth is 4X higher, earnings growth is 150% higher, and return-on-equity is 50% higher. Pay less, get more.

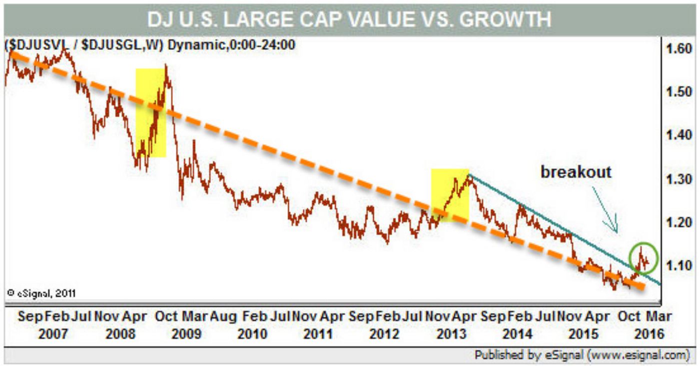
Bulls of the Dow

In March, the Bulls composite snorted ahead 9%, which pulled the performance up ahead of the DJIA and the S&P 500 for the quarter. The Bulls is a blend of ten high-dividend paying, giant, fundamentally strong companies. We tweak the list quarterly, always owning the 10 strongest scoring stocks. In early April, we did our quarterly tweak. Spring cleaning! Out with two old names, and in with two new.

Dividend Growth & Income

In this portfolio we buy high quality, dividend paying companies which have had a propensity to raise their dividends. The objective is a growing income story with potential growth of capital. We look for companies with high historical dividend growth, a yield higher than their sector, a P/E one or two standard deviations below historical P/E, a high return on invested capital, and strong financial strength.

The portfolio has a definite “value” bent to it. As you can see in the following chart, value has been underperforming growth since 2007. The chart was in *Barron's* about 3 weeks ago, and shows the relationship between the performance of value stocks vs. growth stocks. The downward sloping orange line shows the trend of the relative performance, and besides a couple of brief (highlighted) periods where value shined, growth has been winning the tug-of-war since 2007. The *Barron's* article discussed that the little green "breakout" circle may indicate that the value team is perhaps now going to be the leader. If so, it should benefit Dividend Growth & Income. In the meantime, the average dividend yield of the current 24 positions is 3.5%.



Covered Call

The portfolios had a nice bounce-back in March, and ended the quarter about where they started. The bounce allowed Wally to rewrite calls on some stocks that drifted down in price during February's swoon. As we said last month, the portfolio is morphing toward more large-cap stocks, because in the last couple of years our problematic positions have mostly stemmed from smaller companies.

Preferred Income

After a tough January and February, March finally delivered a good month, which gave us a single-digit, positive quarter. The vast majority of preferreds are issued by financial service companies, and financials were one of the worst sectors in the first quarter. Of the 21 different preferreds on our current "buy" list, 14 are banks. Despite the sector's headwinds, the high yield they pay helped preferreds eke out a gain. Regardless of what Presidential candidates say about the "big banks", the fact that preferred prices held up in the storm tells you that credit markets are OK. The current yield of the portfolio is 5.95% and the average call protection is 3.5 years. Not a bad yield in today's world.

If you have any questions or comments regarding this letter, including any Portfolio or composite, please contact our Chief Compliance Officer, Dave Gilreath at daveg@sheaffbrock.com; you can also reach him, or any other Sheaff Brock representative, at 317-705-5700.

Style	Performance Update Portfolio	Mar - 2016	2015	2014	2013	2012	2011	2010	2009
Fixed Income	**Preferred Income** - Preferred stocks	0.97	5.22	14.02	-4.57	9.10			
	High Yield Bond	1.41	-7.32	-1.93	8.78	15.38	3.99	15.93	45.69
Growth and Income	**Covered Call Income** - Quality stocks & covered calls	-0.27	-1.20	6.39	23.56	11.56	-10.25		
	Dividend Growth & Income - Dividend paying stocks	0.03	-7.16	5.20	36.09	12.36	5.36	17.09	24.08
Growth	**IntelliBuilD Growth** - IBD growth stocks	-8.24	2.57	7.62	19.69*	*9/1—12/31/13, S&P 500 +12.9%			
	Bulls of the Dow - 10 strongest of the Dow 30	2.49	1.14	12.42	30.05	7.83			
	Mid-Cap 10 - Mid-cap growth momentum stocks	-15.30	-12.68	11.84	24.32	23.55	21.88	21.26	38.15
Tactical	**Technical Long/Short** - Long S&P 500, cash, or short	-8.76	-27.13						
Alternative	**Alternative** - Metals, foreign currencies, commodities	1.70	-8.25	-4.23	-0.70	9.02	-7.74		
	Index		**2015**	**2014**	**2013**	**2012**	**2011**	**2010**	**2009**
	S&P 500	1.35	1.38	13.69	32.39	16.0	2.1	15.1	26.5
	CBOE S&P 500 Buy/Write	-0.75	5.24	5.64	13.26	5.20	5.72		
	Barclays Aggregate Bond	3.03	0.55	5.97	-2.15	4.2	7.8	6.5	5.9
	DB Commodity Index Tracking Fund (NAV Total Rtn.)	-0.42	-27.41	-28.18	-7.57	3.31	-2.71		

Composites include all (but not less than five) fully discretionary, management fee-paying and, beginning on January 1, 2011, non-management fee-paying accounts, including those accounts no longer with the firm of reasonable size that are substantially invested in accordance with the composite strategy or style. Returns are presented net of management fees and all trading expenses, and the reinvestment of all income. Net-of-fee performance was calculated using actual management fees, except in the case of non-fee-paying accounts, where model fees have been imputed. Actual advisory fees and transaction fees will vary depending on, among other things, the portfolio, account size, and activity. Fees are described in SBIA's ADV Part 2A. The securities mentioned in this report can be, and often are, owned by clients and employees SBIA. *Denotes partial year, with note reference. October 1, 2015 Preferred Income was sub-advised by Trust Investment Advisors, Indianapolis, IN. calculated. Past performance is not indicative or a guarantee of future results.

- The S&P 500 Index is a market capitalization-weighted index comprised of the 500 stocks with the largest market capitalizations trading in the United States. This is not a managed portfolio and does not reflect the deduction of fees or expenses; returns include dividends.
- The Barclays US Aggregate Bond Index is a broad-based benchmark that measures the investment grade, US dollar-denominated, fixed-rate taxable bond market in the United States, including Treasuries, government-related and corporate securities, mortgage backed securities (agency fixed-rate and hybrid ARM pass-throughs), asset-backed securities and CMBS (agency and non-agency).
- The CBOE S&P 500 BuyWrite Index (the "BXM" or the "BXM Index") is a passive total return index based on (1) buying an S&P 500 stock index portfolio, and (2) "writing" (or selling) the near-term S&P 500 Index (SPX) "covered" call option, generally on the third Friday of each month. The SPX call written will have about one month remaining to expiration, with an exercise price just above the prevailing index level (i.e., slightly out of the money). The SPX call is held until expiration and cash settled, at which time a new one-month, near-the-money call is written. The premium collected from the sale of the call is added to the portfolio's total value. The expired option, if exercised, is settled in cash. The BXM Index does not take into account significant factors such as transaction costs and taxes and, because of factors such as these, investors should be expected to underperform passive indexes. The BXM Index is designed to represent general trends for a hypothetical buy-write strategy.
- DB Commodity Index Tracking Fund (DBC) The PowerShares DB Commodity Index Tracking Fund seeks to track changes, whether positive or negative, in the level of the DBIQ Optimum Yield Diversified Commodity Index Excess Return™ (DBIQ Opt Yield Diversified Comm Index ER) plus the interest income from the Fund's holdings of primarily US Treasury securities less the Fund's expenses. The Fund is designed for those who want a cost-effective and convenient way to invest in commodities. The Index is composed of futures contracts on 14 of the most heavily traded and important physical commodities in the world. The Fund and the Index are rebalanced and reconstituted annually in November. The Alternative portfolio is a commodity centric portfolio of ETFs and mutual funds whose constituents' profits are highly sensitive to general commodity prices. It may perform differently than DBC since the composite does not hold futures contracts.

Indexes are unmanaged and unavailable for direct investment. Benchmark returns include reinvestment of income, but do not reflect taxes, or other fees that would reduce performance. (continued pg 1)