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Money Matter$

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FINALLY: Two Clever New ETFs That Fill A Need

by Adam Sommers

‘QUASI SFM MODEL PORTFOLIO’

Back in 2007-2008, I wrote about a clever new index, the Barron’s 400, developed by Market Grader, and compared it to my quantitative stock-picking model. It has many of the same elements used in my Model 25 portfolio, which uses more than 30 different metrics to judge profitability (cash flow), value, and risk.

During the first week of June 2013, an ETF sponsored by ALPS Advisors (ticker symbol: BFOR) that attempts to track the Barron’s 400 Index began trading.

The Barron's 400 is a stockpicker's index: It seeks out the most fundamentally sound companies with the most attractively priced shares. Since its launch in 2007, the Barron's 400—published each week in Barron’s Magazine—has consistently outperformed the leading stock indexes with a variant of growth-at-a-reasonable-price investing.

The index's nearly six-year history has been successful; it finished May with a five-year annualized total return of 7.7%, outrunning both the S&P 500's 5.5% and the Dow Jones Industrial Average's 6.6%. The index weights all stocks equally, a technique that has worked well: The Guggenheim S&P 500 Equal Weight Index ETF (RSP) also returned 7.7% (Ah, but the RSP return was even after-fees).

The Barron's 400 seeks out what Market-Grader President Carlos Diez calls "the most promising companies in America," with a ‘unique’ (not so in my mind) methodology. The process: grade 6,000 companies on 24 indicators of growth, value, profitability, and cash flow; then select the best 400.

Companies are judged with reference to the strength of their revenue growth, by their sales and earnings growth, and by their performance compared to the broader stock market. A stock's value, meanwhile, is judged with measures of price-to-book, price-to-sales, price-to-earnings and other key ratios. The index calculates an "optimal" or intrinsic share price for each stock and compares that with the stock's actual price to judge its attractiveness. Profitability and cash-flow rankings are determined through a blend of factors.

Once the top-scoring companies are in hand, MarketGrader throws out real-estate investment trusts, limits exposure to any sector to

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“The process: grade 6,000 companies on 24 indicators of growth, value, profitability, and cash flow.”

3-Year Returns

Dow Jones Industrial 30 Average:	**17.7 %**
S&P 500 Large Company Index:	**18.6 %**
NASDAQ Composite Index:	**20.4 %**
Russell 2000 Small Co. Index:	**20.1 %**
SFM’s ‘MODEL 25’ PORTFOLIO:	**15.7 %**
SFM’s ‘NAKED ALPHA’ FUND:	**17.8 %**

(see back page for current stock holdings in the Model Portfolio)

ETF Extra — US Equity High Volatility Put Write ETF (HVPW)

US Equity High Volatility Put Write Index Fund is designed for income through selling 60-day put options every 2 months (6 times per year) on 20 stocks. HVPW intends to distribute 9% per year. Investors assume the risk that the underlying referenced equities may close below their strike price, and investors also give up the upside on the underlying equities above the income the fund receives from selling the options. The strike price of each put option included in the Index must be as close as possible to 85% of the closing price of the option’s underlying stock price as of the beginning of each 60-day period.

HVPW’s Notable Statistics

Inception Date:	February 27, 2013
ETF Sponsor:	ALPS Advisors
Return in first 60 days:	2.20 %
Income Distributions:	Bi-Monthly
Total Assets in the Fund:	$ 2.5 Mil.
Expense Ratio:	0.95 %

SFM's ORIGINAL "Model 25" STOCK Only Portfolio

Company Name	Value Grade	Cash Flow	Risk Grade	Market Cap
Apple, Inc.	B	A-	B	Mega
Abbott Laboratories	B+	B-	B	Large
American Eagle Outfitters	A-	B-	B	Mid
CF Industries	A-	A	C	Mid
Coach, Inc.	C	A-	A-	Mid
Holly Frontier	A-	B-	D	Mid
Honda Motor	A-	D	D	Large
Interactive Brokers	A-	A+	D	Micro
IBM	B-	C	A+	Mega
Intel	A-	C	B	Large
JP Morgan Chase	B-	A	B	Mega
KLA Tencor	C	A-	C	Mid
MasterCard	D	A-	A+	Large
Mosaic	C	A-	B+	Large
Qualcomm	C	A-	A-	Large
Questcor Pharmaceuticals	A-	A+	D	Small
Southern Copper	C	B+	A-	Large
Siemens	A+	B-	C	Large
Seagate Technology	B-	A-	C	Large
TJ Maxx	C	B-	A+	Large
Terra Nitrogen	A-	A+	B	Small
Taiwan Semiconductor	D	A+	A-	Mega
Tata Motors	D	A	A+	Large
United Therapeutics	B+	A	D	Small
Exxon Mobil	B-	B-	A-	Mega

SFM ORIGINAL Model "25" Portfolio

vs. A Relevant Benchmark

	SFM Model 25	S&P 500 Index
3 Month Return:	0.9 %	2.4 %
12 Month Return:	15.1 %	17.9 %
3 Year Average Annual:	15.7 %	18.6 %
5 Year Average Annual:	5.3 %	5.1 %
Since Inception (6/1/2003):	17.2 %	6.6 %

Two Clever New ETFs

Continued from page 1

20%, and builds an equal-weighted portfolio of the 400 stocks. The index leans toward small-capitalization companies (close to 50%), but the Barron's 400 isn't a small-cap or even mid-cap index. Its average market capitalization is $19 billion, and the companies most often appearing in the index are heavies such as Microsoft and Wal-Mart.

"The idea is simply to buy the best stocks low and sell them when they're high, unlike what most investors actually do," says MarketGrader's Diez. The ETF charges 0.65% of assets annually, which is costlier than the typical index fund but below the average actively managed fund.
(Thanks go to Brendan Conway at Barron's for the summary)

'NAKED ALPHA FUND LITE'

For those of you that have heard me talk about The Naked Alpha Fund, there is an ETF introduced by ALPS Advisors in February that executes the same basic strategy of the Naked Alpha Fund: The U.S. Equity High Volatility Put Write ETF—ticker symbol HVPW. It aims to generates income of 9-18% per year by selling put options on the **20 most volatile** stocks in the S&P 500 every 60 days. The fund targets downside protection on their puts of 15%, so that in any 60-day period the fund shouldn't feel much pain; ***unless* of course any of those 20 'most volatile' stocks take a tumble of more than 15%; and let's face it, they're 'volatile'**.

The fund aims to never hold a stock; so if the fund is put (contractually obligated to purchase) a decimated stock, it takes its lumps and sells the stock at a loss. However, since the selling of options uses no cash, and they never hold stock, the fund invests its cash in 13-week U.S. Treasury Bills. The annual expense ratio is 0.95%; much less than a typical hedge fund utilizing an option strategy of this sort, but it is 'managed' by a rules-based computer trading strategy.

Why HVPW may be better than The Naked Alpha Fund:

1. There is no minimum investment (TNAF has a $50,000 investment minimum)
2. It is publicly traded, and therefore more liquid, with the ability to sell within a trading day (TNAF has a 60-day withdrawal notice)
3. The management fee is known and constant at 0.95%

The advantages of The Naked Alpha Fund over HVPW:

1. The Naked Alpha Fund has risk-management processes in place. It hedges its systematic market risk.
2. The Naked Alpha Fund has no management fee if it does not earn 5% in a calendar year, and will only charge more than 0.95% in years where the rate of return exceeds 9%.
3. The Naked Alpha Fund can use leverage, and invest in higher yielding alpha overlays than U.S. Treasury Bills.
4. The Naked Alpha Fund gains upside opportunity by purchasing costless collars: buying long-term calls on stocks with proceeds from put sales.
5. You have direct access to the portfolio manager: SFM.

Give us a call if either of these new ETFs interests you; we're always eager to discuss how they may fit into your portfolio.