VAN HULZEN ASSET MANAGEMENT

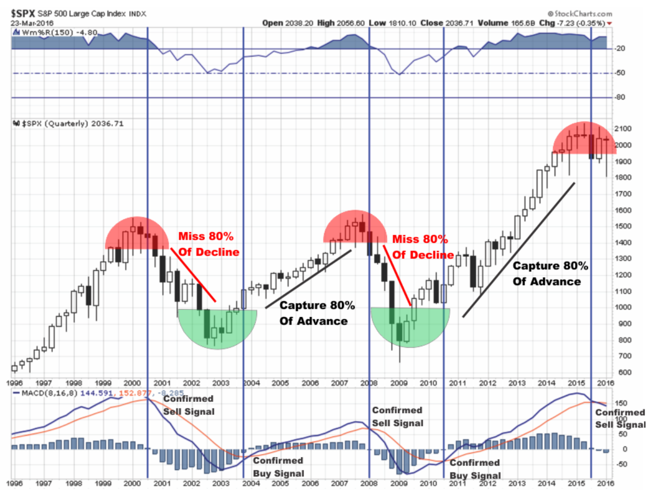
INVESTMENT COMMENTARY: Q1 2016

April | 2016

Setting Realistic Expectation for Long Term Equity Returns

The S&P 500 has been moving sideways for the last 17 months, with huge swings to both the upside and downside. We believe the gap between value and growth is slowly closing in favor of value stocks.

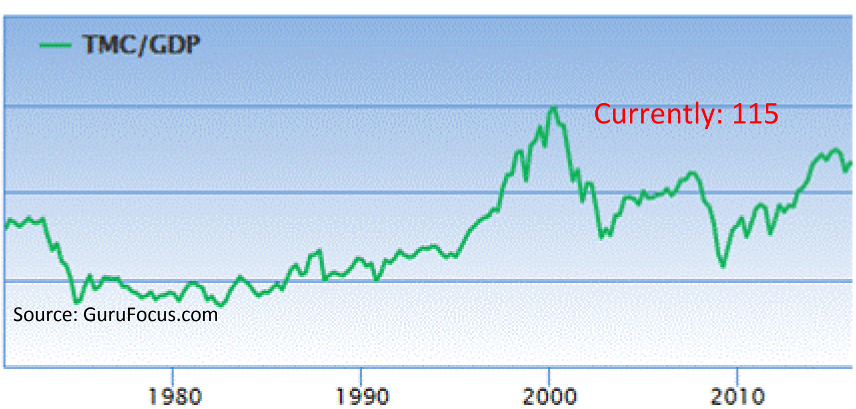
This "tug of war" happening at the market level often appears to be a classical top forming process as seen by this chart (right). This top forming coincides with several long term valuation metrics (Shiller PE, Total Market Cap/GDP, John Hussman) pointing towards overvaluation. We would like to focus on Warren Buffets favorite valuation metric: Total Market Capitalization to GDP (TMC/GDP).



Source: Realretirementadvice.com

Based on historical ratios of total market cap to GDP (currently at 115.8%), the US stock market is likely to return 0.8% per year over the next decade from this level of valuation, including dividends.

On the Buffet scale that would make it significantly overvalued. We can see from the graph below, that during the past four decades the TMC/GNP ratio has varied within a very wide range. The lowest point was about 35% in the previous deep recession of 1982, while the highest point was 148% during the tech bubble in 2000.

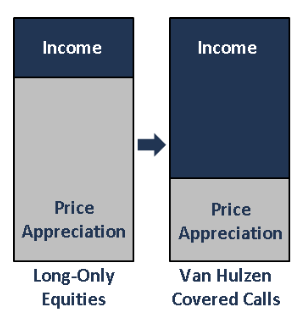


Source: GuruFocus.com

The market went from extremely undervalued in 1982 to extremely overvalued in 2000. With an annual return of 0.8% expected (based on these metrics) from the US stock market, it is worth considering how investment managers will go about driving total return.

Total Return is made up of two components: Price appreciation and income. Over the last decade the S&P 500 index has produced on average about 2% dividend yield. Dividend yield, although not guaranteed, has historically been the more reliable and predictable of the two total return components. Price appreciation is of course the more unknown component. Since total return expectations have dropped to about 0.8% (including dividends), one might want to rethink on how to produce a total return. Adding a layer of option income to a stock portfolio (through the use of covered calls) reduces the portfolio's reliance on price appreciation only to achieve the investment goals.

Van Hulzen Asset Management has been managing covered call strategies for over 14 years. The firm's success in managing covered call strategies for its own clients has led to several sub-advisory agreements, including a large pension mandate won in 2013. The strategy is available in separate account format as well as in a mutual fund.

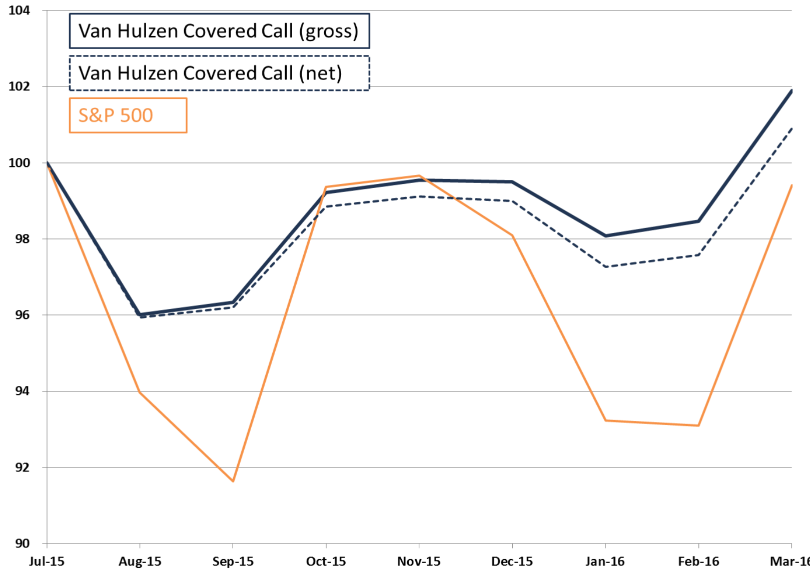


Covered Call Strategy in Review and Outlook

The defensive nature of the Strategy became very visible over the last 9 months. At the heart of covered call investing lies the premise that if you do not loose as much on the downside you do not have to work so hard to make it back on the upside.

For the first quarter the Strategy was up 241bp (gross) while the BXM was down 75bp. The S&P 500 had to put in a 13% rally to end up 130bp for the quarter. The VIX index collapsed 23% but the fund was able to capture the higher volatility early in the year to go longer than the BXM index.

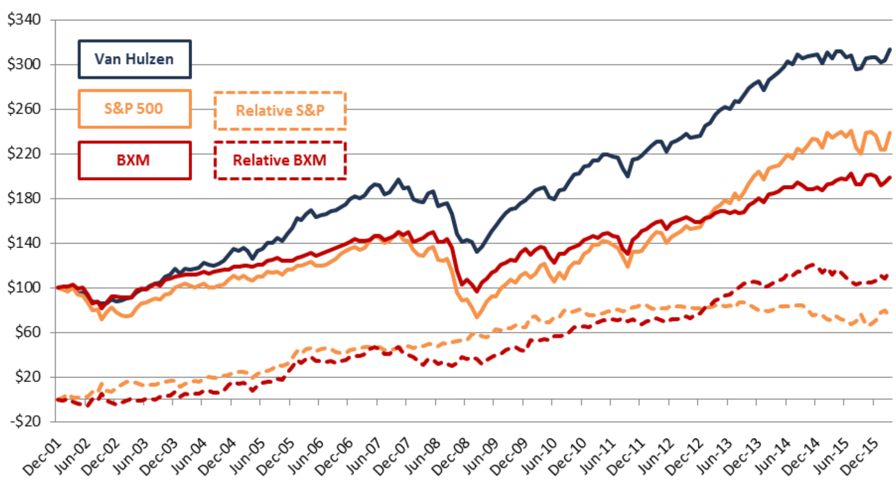
As we have mentioned before, we have seen a major shift from growth to value. For example Wal-Mart and IBM have performed 12% and 11% for the quarter, while last year growth winners Amazon and Netflix went down 12% and 11%. We think that the upcoming earnings season will be challenging for stocks. A combination of high market valuation and an already downward earnings revisions trend will likely not bode well for stock performance in the coming quarters.



The Van Hulzen Covered Call approach is to find undervalued high quality stocks and sell call options to potentially enhance total return on the position. We believe that equity markets will continue to be more volatile than over the past few years. As covered call investors, we welcome back this higher volatility since it makes the total return performance less dependent on price appreciation.

It is not easy to buy low, or to sell high. Emotions can get in the way. But if we have the proper allocations and right level of cash and liquidity, covered call investors can use market volatility to the advantage.

Covered Call Strategy Performance (gross as of 03/31/2016)



Returns (annualized)*	Mar 2016	3M	6M	YTD	1 Year	3 Years	5 Years	7 Years	10 Years	Inception
Van Hulzen (Gross)	3.5%	2.4%	5.8%	2.4%	2.8%	7.1%	7.9%	12.6%	6.6%	8.4%
Van Hulzen (Net)	3.4%	1.9%	4.9%	1.9%	1.3%	5.7%	6.4%	11.2%	5.4%	7.2%
BXM	2.0%	-0.7%	3.2%	-0.7%	2.7%	6.0%	6.5%	9.6%	4.4%	4.9%
Difference (VAM-BXM)	1.5%	3.2%	2.6%	3.2%	0.1%	1.1%	1.4%	3.0%	2.2%	3.4%
S&P 500	6.8%	1.3%	8.5%	1.3%	1.8%	11.8%	11.6%	17.0%	7.0%	6.3%

Note: There is no assurance that the Strategy will achieve its investment objectives. Writing call options can result in an option exercise and may cause shares to be "called away" and sold. The use of covered call strategies does not ensure profits or guarantee against losses. Past performance may not be indicative of future results. Risk is measured by standard deviation; standard deviation is a statistical measurement of volatility risk based on historical returns.

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