

the Prudent Speculator 596

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“The conference wants a specific recommendation from me. I guess ‘Get out of the stock market’ isn’t clear enough...It’s [gold] traded for 5,000 years...some regard it as a metal, we regard it as a currency and it remains our largest currency allocation.” So proclaimed billionaire investor Stanley Druckenmiller on May 4 at this year’s Ira Sohn Conference. As the get-together included the best and brightest of the hedge fund world, plenty of media attention was paid to the proclamations of the supposed Masters of the Universe, even as the ugly performance scorecard from last year’s event was covered in red ink.

To be sure, we have to be careful not to throw stones as we also dwell in a glass house (your editor’s recent column in *Forbes Magazine* boasted a couple of awful (thus far) stock picks in **Seagate Technology** (STX - \$23.75) and **Kohl’s Corp** (KSS - \$37.38)), but as of this writing gold has tumbled more than 5% since May 4, while equities have moved a couple of percent higher. Obviously, time will tell how successful the Druckenmiller call to dump stocks and buy the precious yellow proves to be, but his widely publicized prognostication piggy-backed on the predictions of other doom-and-gloom pundits (billionaire investor Carl Icahn suggests the markets may soon have a “day of reckoning”) to raise investor anxiety levels and push investor sentiment statistics to multi-year lows...which is a positive for those of us who like the Warren Buffett admonition, “Be greedy when others are fearful and fearful when others are greedy.”

Incredibly, the May 25 tally of Bulls in the weekly Sentiment Survey from the American Association of Individual Investors dropped to 17.8%, the lowest mark since April 2005. Believe it or not, the number of Bulls was a little higher at 18.9% on May 5, 2009, and market history validates the thinking that AAI is a decent contrarian indicator. We examined subsequent market returns the previous 37 times that the AAI Bulls numbered 20% or fewer and found that the respective average (non-annualized) gains for the S&P 500 over the ensuing three-, six- and 12-months were an impressive 7.0%, 13.6% and 23.0%!

And it is not just the folks on Main Street who have lost affection for stocks as fund managers overseeing \$619 billion polled in mid-May by Bank of America Merrill Lynch

“The fact that people will be full of greed, fear or folly is predictable.

The sequence is not predictable.”

—Warren Buffett

said that cash makes up an average 5.5% of holdings, a level higher than during the 2011 Market Meltdown when investors were fretting about the downgrade of the U.S. credit rating and the government shutdown, not to mention the European sovereign debt crisis. And speaking of the Continent, Europe is again now a big concern as the looming Brexit vote is weighing on the outlook for global economic growth, which is already subdued with the

OECD stating this week that it now sees worldwide GDP expanding at 3.0% this year and 3.3% in 2017. Of course, though Brexit is viewed as a major “tail risk,” the consensus thinks the U.K. will stay in the European Union.

We also respect that worries about the timing, number and ramifications of additional Federal Reserve interest rate hikes are causing plenty of consternation, even as the recent favorable domestic statistics on housing, industrial production, durable goods orders, jobless claims and consumer spending that might compel Janet Yellen & Co. to remove some of the unprecedented monetary policy accommodation (rates will still be extraordinarily low) are indicative of a much more promising economic climate for corporate profits. What’s more, our analysis of the historical data shows that Value stocks have on average gained a respective 13.7%, 14.1% and 14.6% per annum in the one-, three- and five-year periods following the 17 prior times the Fed has initiated a tightening cycle.

Certainly, anything can happen in the near term, but as many have recently learned the hard way, far more money has been lost in anticipation of a market correction than has been lost in the corrections themselves.



Chief Investment Officer
Al Frank Asset Management (AFAM)

Earnings Scorecard

Q1 Season

While many of the headwinds have stopped blowing as strongly in recent months, dollar strength, commodity price weakness and a lackluster global economy continued to hinder top- and bottom-line growth in the

first quarter. Nevertheless, Corporate America managed to turn in decent Q1 EPS numbers relative to subdued expectations, even as sales figures did not compare as favorably. Data provider Bloomberg found that the number

Industry Group	Ticker	Company	03.16 Act EPS	03.15 Act EPS	03.16 Est EPS	TTM ¹ EPS	NTM ² Est EPS	NTM P/E	LTM Sales	NTM Est Sales	Sales Growth
Autos & Components	GT	Goodyear Tire & Rubber	0.72	0.54	0.71	3.48	4.00	7.0	16,110	15,906	-1.3%
Banks	BAC	Bank of America	0.20	0.27	0.21	1.26	1.44	10.3	nmf	nmf	nmf
	BBT	BB&T	0.69	0.68	0.64	2.76	2.90	12.6	nmf	nmf	nmf
	FITB	Fifth Third Bancorp	0.37	0.37	0.35	1.60	1.57	12.0	nmf	nmf	nmf
	JPM	JPMorgan Chase	1.41	1.61	1.25	5.60	5.93	11.0	nmf	nmf	nmf
	KEY	KeyCorp	0.24	0.27	0.25	1.06	1.16	11.1	nmf	nmf	nmf
	ONB	Old National Bancorp	0.25	0.24	0.23	1.01	0.98	13.5	nmf	nmf	nmf
	PNC	PNC Financial Services Group	1.62	1.75	1.70	6.89	7.24	12.4	nmf	nmf	nmf
Capital Goods	WFC	Wells Fargo	0.99	1.04	0.97	4.10	4.11	12.4	nmf	nmf	nmf
	ARII	American Railcar Industries	1.16	1.64	1.36	5.91	3.81	10.4	802	607	-24.3%
	BA	Boeing	1.74	1.97	1.84	7.48	8.99	14.0	96,597	94,014	-2.7%
	CAT	Caterpillar	0.67	1.72	0.68	3.43	2.73	26.6	43,770	40,205	-8.1%
	CMI	Cummins	1.87	2.04	1.78	8.59	7.96	14.4	18,692	17,525	-6.2%
	DE	Deere	1.64	2.03	1.48	5.05	3.61	22.8	27,709	23,483	-15.3%
	ETN	Eaton PLC	0.88	1.01	0.85	4.18	4.35	14.2	20,445	20,015	-2.1%
	FLR	Fluor	0.85	0.96	0.85	3.74	3.47	15.2	17,989	18,614	3.5%
	GE	General Electric	0.21	0.31	0.19	1.30	1.61	18.8	124,078	124,141	0.1%
	TPC	Tutor Perini	0.31	0.10	0.19	1.40	2.19	10.4	4,939	5,343	8.2%
Commercial Services	TRN	Trinity Industries	0.64	1.13	0.69	4.59	1.91	9.4	5,954	4,459	-25.1%
	MAN	ManpowerGroup	0.98	0.83	0.93	5.58	6.04	13.2	19,375	20,226	4.4%
Consumer Dur & App	WM	Waste Management	0.46	0.45	0.55	2.51	2.86	21.3	13,097	13,473	2.9%
	COH	Coach	0.44	0.36	0.41	1.84	2.13	18.5	4,341	4,672	7.6%
	MDC	MDC Holdings	0.20	0.17	0.26	1.37	2.21	10.5	1,928	2,413	25.1%
Consumer Services	WHR	Whirlpool	2.63	2.14	2.68	12.88	15.29	11.4	20,661	20,981	1.5%
	RCL	Royal Caribbean Cruises Ltd	0.57	0.20	0.31	5.19	6.43	12.0	8,401	9,067	7.9%
Diversified Financials	BK	Bank of New York Mellon	0.74	0.67	0.68	2.93	3.17	13.3	nmf	nmf	nmf
	COF	Capital One Financial	1.85	1.97	1.92	7.39	7.73	9.5	nmf	nmf	nmf
	GS	Goldman Sachs Group	2.32	6.00	2.48	14.23	16.48	9.7	nmf	nmf	nmf
	SYF	Synchrony Financial	0.70	0.66	0.69	2.69	2.87	10.9	nmf	nmf	nmf
Energy	BHI	Baker Hughes	-0.44	-0.07	-0.33	-0.84	-1.49	-31.0	13,818	9,477	-31.4%
	BRS	Bristow Group	0.13	0.91	0.53	1.40	1.07	12.6	1,716	1,601	-6.7%
	ESV	Ensc PLC	0.74	1.49	0.78	3.74	1.46	6.8	3,714	2,661	-28.3%
	HAL	Halliburton	0.07	0.49	0.04	1.13	-0.22	-196.2	20,781	15,610	-24.9%
	HFC	HollyFrontier	-0.06	1.16	0.07	2.97	2.78	9.6	12,250	10,663	-13.0%
	NOV	National Oilwell Varco	-0.06	1.14	-0.12	1.55	-1.06	-31.1	12,126	7,060	-41.8%
	TK	Teekay	-0.08	0.22	0.20	0.64	1.02	10.3	2,546	2,455	-3.5%
	TNP	Tsakos Energy Navigation Ltd	0.25	0.42	0.26	1.51	1.44	4.5	561	515	-8.2%
XOM	Exxon Mobil	0.43	1.17	0.29	3.11	3.11	28.7	219,872	222,599	1.2%	
Food & Staples Retailing	WMT	Wal-Mart Stores	0.98	1.03	0.88	4.54	4.25	16.7	483,208	488,279	1.0%
Food Bev & Tobacco	ADM	Archer-Daniels-Midland	0.42	0.77	0.45	2.23	2.66	16.1	64,580	65,033	0.7%
	TSN	Tyson Foods	1.07	0.75	0.96	3.85	4.38	14.6	38,899	37,279	-4.2%
Health Care Equip/Srvcs	ABT	Abbott Laboratories	0.41	0.47	0.39	2.09	2.28	17.4	20,393	21,199	4.0%
	AET	Aetna	2.30	2.39	2.23	7.62	8.21	13.8	60,936	63,914	4.9%
	BAX	Baxter Int'l	0.36	1.00	0.29	2.20	1.70	25.3	11,358	10,162	-10.5%
	CAH	Cardinal Health	1.43	1.19	1.33	5.11	5.47	14.4	117,709	128,077	8.8%
	MCK	McKesson	3.17	2.94	3.14	12.80	13.54	13.5	190,884	205,367	7.6%
Household Products	MDT	Medtronic PLC	1.27	1.16	1.26	4.38	4.67	17.2	28,833	29,855	3.5%
	KMB	Kimberly-Clark	1.53	1.42	1.51	5.87	6.19	20.5	18,376	18,620	1.3%
Insurance	ALL	Allstate	0.84	1.46	0.68	4.59	5.39	12.5	nmf	nmf	nmf

As of 05.31.16. N/A=Not applicable. ¹Trailing 12-month. ²Next 12-months. nmf=Not meaningful. SOURCE: AI Frank using data (EPS Adjusted) from Bloomberg

of companies in the S&P 500 that exceeded earnings expectations was 72.4%, compared to 20.1% that trailed forecasts and 7.5% that met projections. In Q1 2015, the Beat/Miss/Match figures were 67.7%/22.4%/9.8%. Of the 98 *Prudent Speculator* stocks below, 60% topped EPS estimates.

Of course, management teams remained cautious in their outlooks and guidance, but Standard & Poor's pres-

ently projects that after declining 11.1% in 2015 to \$100.45, compared to \$113.01 in 2014, bottom-up operating EPS for the S&P 500 will rebound nicely this year to \$114.76. The current arguably very aggressive S&P estimate of \$134.11 for 2017 has been coming down in recent months, but profits should improve going forward and history shows that stock prices eventually follow earnings. ■

Industry Group	Ticker	Company	03.16 Act EPS	03.15 Act EPS	03.16 Est EPS	TTM ¹ EPS	NTM ² Est EPS	NTM P/E	LTM Sales	NTM Est Sales	Sales Growth
Insurance	AXS	Axis Capital Holdings Ltd	1.07	1.35	1.09	3.74	4.23	13.0	nmf	nmf	nmf
	MET	MetLife	1.19	1.44	1.38	4.60	5.67	8.0	nmf	nmf	nmf
	PRU	Prudential Financial	2.18	2.79	2.37	9.43	9.92	8.0	nmf	nmf	nmf
	TRV	Travelers	2.33	2.53	2.55	10.68	9.77	11.7	nmf	nmf	nmf
Materials	ABX	Barrick Gold	0.11	0.05	0.10	0.35	0.64	26.4	8,714	8,039	-7.7%
	AGU	Agrium	0.02	0.12	-0.06	7.04	5.76	15.7	14,648	14,339	-2.1%
	AUY	Yamana Gold	0.03	-0.04	0.00	-0.01	0.10	43.1	1,797	1,829	1.7%
	CE	Celanese	1.83	1.72	1.50	6.16	6.56	10.8	5,628	5,696	1.2%
	MOS	Mosaic	0.14	0.70	0.14	2.34	1.19	21.2	8,430	7,520	-10.8%
	NEM	Newmont Mining	0.34	0.46	0.18	0.88	1.35	24.0	7,789	8,040	3.2%
	RYAM	Rayonier Advanced Materials	0.36	0.25	0.20	1.85	0.93	13.9	938	858	-8.6%
Media	CMCSA	Comcast	0.84	0.79	0.79	3.29	3.59	17.7	75,447	80,106	6.2%
	DIS	Walt Disney	1.36	1.23	1.40	5.64	5.91	16.8	54,826	57,648	5.1%
Pharma/Biotech/Life Sci	AMGN	Amgen	2.90	2.11	2.59	9.88	11.01	14.3	22,156	22,757	2.7%
	BIIB	Biogen	4.79	3.51	4.46	16.92	19.03	15.2	10,936	11,365	3.9%
	GILD	Gilead Sciences	3.03	2.76	3.15	11.69	12.01	7.3	32,839	31,037	-5.5%
	JNJ	Johnson & Johnson	1.68	1.56	1.65	6.32	6.66	16.9	70,182	72,648	3.5%
	MRK	Merck	0.89	0.85	0.86	3.64	3.71	15.2	39,385	39,065	-0.8%
Real Estate	PFE	Pfizer	0.67	0.51	0.55	2.36	2.41	14.4	50,992	52,562	3.1%
	ANH	Anworth Mortgage Asset	0.14	0.15	0.15	0.57	0.57	8.1	nmf	nmf	nmf
	GEO	GEO Group	0.45	0.41	0.44	2.01	2.00	16.6	nmf	nmf	nmf
	RYN	Rayonier	0.11	0.14	0.08	0.37	0.33	79.3	nmf	nmf	nmf
Retailing	AEO	American Eagle Outfitters	0.22	0.15	0.18	1.16	1.26	12.4	3,572	3,649	2.2%
	DSW	DSW	0.40	0.53	0.46	1.40	1.44	14.7	2,646	2,811	6.2%
	KSS	Kohl's	0.31	0.63	0.37	3.71	3.90	9.2	19,053	18,964	-0.5%
	PETS	PetMed Express	0.27	0.25	0.25	1.02	1.07	17.6	235	239	2.0%
	SPLS	Staples	0.17	0.17	0.16	0.90	0.91	9.7	20,899	20,313	-2.8%
	SSI	Stage Stores	-0.56	-0.27	-0.47	0.28	0.30	18.6	1,568	1,476	-5.9%
	TGT	Target	1.29	1.10	1.19	4.89	5.21	13.2	72,862	70,913	-2.7%
Semis & Cap Equipment	DIOD	Diodes	0.12	0.26	0.11	0.73	0.97	19.9	865	961	11.0%
	INTC	Intel	0.54	0.43	0.49	2.48	2.44	13.0	56,276	57,468	2.1%
	QCOM	Qualcomm	1.04	1.03	0.96	3.25	4.41	12.5	22,614	23,201	2.6%
Software & Services	CA	CA Inc.	0.60	0.33	0.57	2.10	2.54	12.7	4,025	4,063	0.9%
	IBM	Int'l Business Machines	2.35	2.91	2.09	14.37	13.61	11.3	80,837	79,473	-1.7%
Technology Hardware	MSFT	Microsoft	0.62	0.62	0.64	2.69	2.77	19.1	86,886	93,671	7.8%
	AAPL	Apple	1.90	2.33	2.00	8.99	8.44	11.8	227,535	217,676	-4.3%
	AVX	AVX	0.19	0.20	0.17	0.76	0.77	17.9	1,196	1,244	4.1%
	BHE	Benchmark Electronics	0.26	0.34	0.32	1.54	1.43	14.5	2,469	2,406	-2.5%
	BRCD	Brocade Comm Systems	0.22	0.19	0.22	0.77	0.89	10.2	2,238	2,323	3.8%
	CSCO	Cisco Systems	0.57	0.46	0.55	2.01	2.39	12.1	49,452	49,972	1.1%
	ERIC	LM Ericsson	0.10	0.10	0.14	0.71	0.61	12.7	29,033	28,699	-1.1%
	GLW	Corning	0.28	0.35	0.28	1.34	1.45	14.4	8,893	9,841	10.7%
	IM	Ingram Micro	0.35	0.43	0.53	2.58	2.50	13.8	41,718	40,481	-3.0%
	STX	Seagate Technology PLC	0.22	1.08	0.39	2.35	1.63	13.9	11,433	10,035	-12.2%
Telecommunication Services	T	AT&T	0.72	0.63	0.69	2.78	2.87	13.6	154,760	166,343	7.5%
Transportation	CSX	CSX	0.37	0.45	0.37	1.93	1.80	14.7	11,402	10,971	-3.8%
	NSC	Norfolk Southern	1.29	1.00	0.97	5.57	5.69	14.8	10,364	10,115	-2.4%
Utilities	DUK	Duke Energy	1.13	1.24	1.14	4.42	4.62	17.0	23,016	24,959	8.4%
	ETR	Entergy	1.35	1.68	1.19	5.66	5.04	15.1	11,203	12,149	8.4%

As of 05.31.16. N/A=Not applicable. ¹Trailing 12-month. ²Next 12-months. nmf=Not meaningful. SOURCE: AI Frank using data (EPS Adjusted) from Bloomberg

Recommended Stocks

In this space, we list each month 40 of our most attractively priced recommended stocks. All trade for significant discounts to our determination of long-term fair value and/or offer favorable risk/reward profiles. Note that, while we always seek substantial capital gains, we require lower appreciation potential for stocks that we deem to

have more stable earnings streams, more diversified businesses and stronger balance sheets. The natural corollary is that riskier companies must offer far greater upside to warrant a recommendation. Further, as total return is how performance is ultimately judged, we explicitly factor dividend payments into our analytical work.

Industry Group	Ticker ¹	Company	Price	Target Price	Price Multiples			EV/ EBITDA ³	Debt/ TE ⁴	Div Yld	Mkt Cap
					EPS	Sales	TBV ²				
Autos & Components	GM	General Motors	31.28	45.14	5.8	0.3	1.4	2.9	141%	4.9%	48,166
	GT	Goodyear Tire & Rubber	27.97	48.70	8.0	0.5	2.2	5.6	168%	1.0%	7,438
Banks	BBT	BB&T	36.37	48.07	13.2	nmf	1.9	nmf	nmf	3.1%	29,534
	FITB	Fifth Third Bancorp	18.87	28.00	11.8	nmf	1.0	nmf	nmf	2.8%	14,487
	HSBC	HSBC Holdings PLC	32.44	47.70	8.6	nmf	0.8	nmf	nmf	7.9%	128,544
Capital Goods	TRN	Trinity Industries	18.06	37.18	3.9	0.5	0.9	3.4	107%	2.4%	2,724
Consumer Dur & App	MDC	MDC Holdings	23.24	39.19	16.9	0.6	0.9	16.1	68%	4.3%	1,139
Diversified Financials	COF	Capital One Financial	73.24	98.40	9.9	nmf	1.3	nmf	nmf	2.2%	37,506
Energy	BRS	Bristow Group	13.41	30.45	9.6	0.3	0.3	15.8	74%	2.1%	469
	HFC	HollyFrontier	26.76	52.79	9.0	0.4	1.9	5.0	53%	4.9%	4,724
	RDS/A	Royal Dutch Shell PLC	48.49	72.17	15.7	0.4	1.0	12.9	42%	6.6%	194,212
	TK	Teekay	10.52	20.76	16.4	0.3	1.3	9.3	1065%	2.1%	765
	TNP	Tsakos Energy	6.47	13.21	4.3	1.0	0.5	6.4	89%	4.9%	565
	TOT	Total SA	48.52	70.07	11.9	0.9	1.3	10.2	46%	4.8%	120,269
Health Care Equip/Srvcs	ABT	Abbott Laboratories	39.63	53.28	19.0	2.9	10.6	14.9	109%	2.6%	58,222
	CAH	Cardinal Health	78.95	105.11	15.5	0.2	nmf	9.7	nmf	2.3%	25,723
Insurance	MET	MetLife	45.55	78.95	9.9	nmf	0.8	nmf	nmf	3.3%	50,044
	PRU	Prudential Financial	79.25	106.55	8.4	nmf	0.8	nmf	nmf	3.5%	35,029
Materials	MOS	Mosaic	25.23	49.05	10.8	1.0	1.1	6.3	45%	4.4%	8,826
Pharma/Biotech/Life Sci	AMGN	Amgen	157.95	210.94	16.0	5.4	48.8	10.8	1319%	2.5%	118,655
	BIIB	Biogen	289.73	425.49	17.1	5.8	18.7	11.0	192%	0.0%	63,466
	GILD	Gilead Sciences	87.06	134.77	7.4	3.5	50.3	5.2	915%	2.2%	115,948
	MRK	Merck	56.26	60.29	15.5	4.0	33.4	12.5	508%	3.3%	155,729
	PFE	Pfizer	34.70	43.04	14.7	4.1	nmf	12.8	nmf	3.5%	210,450
	SNY	Sanofi	41.20	58.93	13.0	5.3	14.7	12.8	nmf	3.3%	106,036
Real Estate	ANH	Anworth Mortgage Asset	4.63	6.77	8.1	nmf	0.8	nmf	nmf	13.0%	447
Retailing	AEO	American Eagle Outfitters	15.64	22.93	13.5	0.8	2.8	5.3	0%	3.2%	2,829
	• FL	Foot Locker	55.92	85.54	12.7	1.0	3.1	6.7	5%	2.0%	7,610
	KSS	Kohl's	36.04	62.91	9.7	0.4	1.3	4.7	86%	5.5%	6,673
	SSI	Stage Stores	5.53	8.33	19.8	0.1	0.4	4.1	49%	10.8%	149
	TGT	Target	68.78	88.81	14.1	0.6	3.3	6.4	103%	3.3%	40,530
Semis & Cap Equipment	INTC	Intel	31.59	40.34	12.8	2.7	4.4	6.8	64%	3.3%	149,168
Software & Services	MSFT	Microsoft	53.00	60.21	19.7	4.8	8.0	16.8	78%	2.7%	416,605
Technology Hardware	AAPL	Apple	99.86	133.72	11.1	2.4	4.5	5.0	57%	2.3%	546,976
	AVX	AVX	13.81	18.83	18.2	1.9	1.2	8.4	0%	3.0%	2,313
	CSCO	Cisco Systems	29.05	37.95	14.5	3.0	4.4	7.7	74%	3.6%	146,113
	ERIC	LM Ericsson	7.73	13.90	10.7	0.9	1.4	5.5	25%	3.6%	25,775
	JBL	Jabil Circuit	19.08	34.16	9.8	0.2	2.3	4.1	115%	1.7%	3,648
	STX	Seagate Technology PLC	22.56	43.79	9.6	0.6	nmf	7.0	nmf	11.2%	6,734
Transportation	• DAL	Delta Air Lines	43.46	75.38	7.9	0.8	nmf	4.0	nmf	1.9%	33,533

As of 05.31.16. N/A=Not applicable. nmf=Not meaningful. ¹ =First-time recommendation. ²Tangible book value. ³Enterprise value-to-earnings before interest taxes depreciation and amortization. ⁴Tangible equity. SOURCE: AI Frank using data from Bloomberg

Portfolio Builder

Research Team Favorites

The *Prudent Speculator* follows an approach to investing that focuses on **broadly diversified** investments in **undervalued** stocks for their **long-term** appreciation potential. Does that mean we build portfolios of 20 stocks...30...? More like 50 and up. We like stocks. And we like a lot of 'em. We don't rely nearly as much on "how many" as we do "in which," but we tend to invest in far more names than most. This expansive diversification, we find, potentially serves us well in two ways: we can further minimize the risk of individual stock ownership, while maximizing the likelihood of finding the truly big winners among the undervalued masses.

As for the "in which" part, readers should know we discriminate among potential investments primarily by their relative valuation metrics and our assessments of stock-specific risk. We buy only those stocks we find undervalued along several lines relative to their own trading history, those of their peers or that of the market in general. The prices at which we'll buy and sell stocks incorporate a range of fundamental risks (e.g. credit, customer and competitive dynamic) that we believe the companies may face over our normal 3-to-5-year investing time horizon.

Each month in this column, we suggest to readers a group of ten stocks with which to populate portfolios. The list could serve as a portfolio foundation for new investors or as a pick-list for folks already maintaining well-diversified holdings. While other themes may be featured over time, our ongoing consolidation program has created opportunities (i.e. proceeds of sales) to simply add stocks each month to our newsletter portfolios.

Note that we are in no way suggesting that these stocks replace those featured in prior months as we will always issue a *Sales Alert* should we choose to exit a position.

This Month's Theme

Investing the remaining cash in our four newsletter portfolios, we will add \$20,000 of **Merck** to PruFolio and \$29,000 of **Delta Air Lines** to TPS Portfolio. In Millennium Portfolio, we will pick up \$10,000 of both **Foot Locker** and **Target**, while in Buckingham Portfolio we will bring the ownership up to \$6,000 in **HSBC Holdings**, **MDC Holdings** and **Mosaic**. We already have sufficient sector exposure and/or hold a sizable position in **Apple**, **Prudential Financial** and **Royal Dutch Shell**. Waiting our usual four days, we will transact on June 8.

NEWSLETTER PORTFOLIO PURCHASES

Ticker	Company	Sector	Price	Target Price
AAPL	Apple	Information Technology	99.86	133.72
DAL	Delta Air Lines	Industrials	43.46	75.38
FL	Foot Locker	Consumer Discretionary	55.92	85.22
HSBC	HSBC Holdings PLC	Financials	32.44	47.70
MDC	MDC Holdings	Consumer Discretionary	23.24	39.19
MOS	Mosaic	Materials	25.23	49.05
MRK	Merck	Health Care	56.26	60.29
PRU	Prudential Financial	Financials	79.25	106.55
RDSA	Royal Dutch Shell PLC	Energy	48.49	72.17
TGT	Target	Consumer Discretionary	68.78	88.81

As of 05.31.16. SOURCE: AI Frank using data from Bloomberg

Apple (AAPL)

Shares of tech giant Apple have recovered somewhat after falling as low as \$90 in May for the first time since 2014 following disappointing Q2 earnings of \$1.90 per share (vs. \$2.00 est.) on revenue of \$50.6 billion (vs. \$52.0 billion est.). It certainly didn't help that billionaire activist investor Carl Icahn revealed on a CNBC segment that he had fully divested his large Apple position. While China is a concern to Mr. Icahn and many others, CEO Tim Cook believes, "The future of Apple is very bright. Our product pipeline has amazing innovations in store. We are forging ahead with important investments in research and development, in our infrastructure, and in our supply chain." We too feel that there is plenty of opportunity in the future, and that good customer traction for the iPhone SE (which was not included in Q2 results) will be an important step forward in covering the gamut of phone shapes and sizes. From a valuation perspective, Apple's forward P/E ratio of 11.1 and solid dividend yield of 2.3% (which was boosted from \$0.52 per share to \$0.57, paid quarterly) are attractive, while the company retains its mountain of cash, totaling approximately \$30 per share.

Delta Air Lines (DAL)

Delta Air Lines is one of the largest air carriers in North America by passengers flown and fleet size. Delta serves more than 180 million customers each year and offers service to 337 destinations in 62 countries. DAL faced some significant hurdles after its merger with Northwest

Airlines in 2007, especially related to fleet integration, union contracts (Delta was non-union, Northwest union) and differing organizational cultures. Although work remains to be done, Delta has mostly overcome the issues. Using low fuel prices and low cost of debt to its advantage, Delta has placed orders for more than a hundred new planes to replace aging aircraft in the current fleet. It seems the likely case that most will be delivered as fuel prices increase, such that savings from new planes' lower fuel and maintenance expenses will more than offset the higher lease costs. Additionally, Delta is making a concerted effort to cater to business travelers, historically the most loyal type of customer. Gate transfers via Porsche and top-notch food in the lounges and at 35,000 feet might seem gimmicky, but they ensure that the highest-margin travelers return. DAL trades at less than 8 times earnings.

Foot Locker (FL)

Foot Locker is an athletic footwear and apparel retailer, operating 3,396 stores in 23 countries in North America, Europe, Australia, and New Zealand. FL's marketing format includes Foot Locker, Champs Sports, Kids Foot Locker, Lady Foot Locker, Eastbay and Footlocker.com. Shares are down 15% this year as the overall pressure on the retail industry and concerns over recently softening basketball shoe sales have taken their toll. While changing consumer preferences and growing online competition are perpetual issues, the company just turned in its most profitable quarter in its history. We believe the recent sell-off is overdone, as we like that FL has shown broad strength across distribution channels, geographic locations, banners and product categories. We think FL will continue to benefit from its strategic cost control and productivity plans, in addition to further penetration of its apparel offerings and solid growth of its digital shopping platforms. Additionally, we like the strong balance sheet that sports \$6.85 of net cash per share, giving management operational flexibility and the ability to buy back shares and increase the dividend (yield is 2.0%). FL also trades at 12 times consensus forward earnings estimates.

HSBC Holdings PLC (HSBC)

HSBC Holdings is one of the world's largest banking and financial services organizations, operating through an international network of 6,000 offices in 71 countries and territories. While HSBC has an unrivaled global footprint, we like that the company is undertaking a significant reshaping of its business portfolio in efforts to cap-

ture value from its presence around the world. We also like HSBC's exposure to higher economic growth markets, helping drive demand for its diversified products and services, from checking accounts and international trade services to wealth management. Additionally, we are constructive on the potential long-term benefits of management's decision to align itself to the world's largest trade and economic zones, shifting its business mix further towards Asia, as well as its continued focus on cutting costs and delivering a progressive dividend. HSBC trades for less than 11 times estimated forward 12-month earnings and yields nearly 8%.

MDC Holdings (MDC)

MDC Holdings is a builder and seller of homes with ongoing operations in 169 communities throughout 9 states (including California, Colorado, Maryland, Virginia, Arizona and Florida) under the name Richmond American Homes, and also is an originator of mortgage loans and title agency services primarily to its home buyers. Shares of MDC are down on the year despite increased pricing power and a slowly improving macroeconomic environment in the U.S. that is bolstering the homebuilding industry. In fact, MDC announced that its backlog of orders had swelled 50%, year-over-year, to \$1.43 billion. We see MDC as well-positioned to benefit from stability in consumer confidence and continually improving employment. MDC also sports a broad geographic footprint, successful cost control initiatives and a solid balance sheet, with ample liquidity that the company continues to smartly tap as it acquires land in attractive markets across the country. MDC shares trade at less than 11 times forward earnings estimates and offer a generous 4.3% dividend yield.

Mosaic (MOS)

Mosaic is the largest producer of phosphate fertilizers in the world and is one of the leaders in the production of potash, feed ingredients and industrial products. Shares have fallen more than 40% over the last year as short-sighted market players bailed out due to weak crop nutrient prices and recent concerns from an analyst that MOS may have negative free cash flow and will need to pay its dividend from cash reserves. However, CEO James O'Rourke disagreed, "We believe we have strong enough cash flow capabilities through the whole cycle that we cannot only pay a reasonable and fair dividend, but we can also balance that with our growth opportunities and returning money to shareholders." We like the potential

of the firm's growing specialty fertilizer products (MicroEssentials) and believe there is a plenty of long-term potential in the fertilizer markets. Higher crop yields become increasingly important as the global population expands, less farmable land is available and more people in emerging economies move up the socioeconomic ladder adding more protein to their diets (which requires more grains to feed the cattle, pigs, etc.). Earnings are likely to hit a trough this year, while MOS yields 4.4%.

Merck (MRK)

Merck is a global pharmaceutical giant focused on discovering, developing and marketing drugs for respiratory, immunology, cardiovascular, diabetes, infectious diseases, oncology and other ailments. Merck is also a global leader in vaccines and operates an animal health division. The company has seen its sales slow over the past few years, enduring patent losses for some of its top drugs, yet it has managed consistent profitability over the last three years (adjusted EPS of \$3.49, \$3.49 and \$3.59). With a wide array of high-margin drugs, a strong lineup of new products (Keytruda (cancer) and Zepatier (hepatitis C) have strong potential) and a pipeline that creates both near- and long-term opportunities, we think Merck will produce attractive returns on its invested capital going forward. The firm generates solid free cash flow and boasts a track record of returning cash to shareholders, while management is on the hunt for acquisitions and drug-licensing deals that could bolster its drug development. We also like that MRK has a yield of 3.3%.

Prudential Financial (PRU)

PRU is the second-largest life insurer in the U.S. with more than \$1.2 trillion of assets under management. The company also has operations in more than 40 countries and territories located throughout Asia, Europe and Latin America. PRU provides insurance, investment management, brokerage services and other financial products. It ranks in the top three in terms of variable life assets, individual life in-force premiums and group life sales, earning top returns among traditional franchise life insurers. Although currency challenges and other headwinds persist, the firm has consistently turned in attractive results from its international operations, while the exit from the long-term care business has reduced exposure to interest-rate-sensitive products. With favorable long-term potential within numerous business lines, a strong capital base and a history of returning cash to shareholders, we see

PRU as a core financial holding. The shares trade for less than 9 times estimated earnings and at just 75% of its tangible book value, while offering a 3.6% dividend yield.

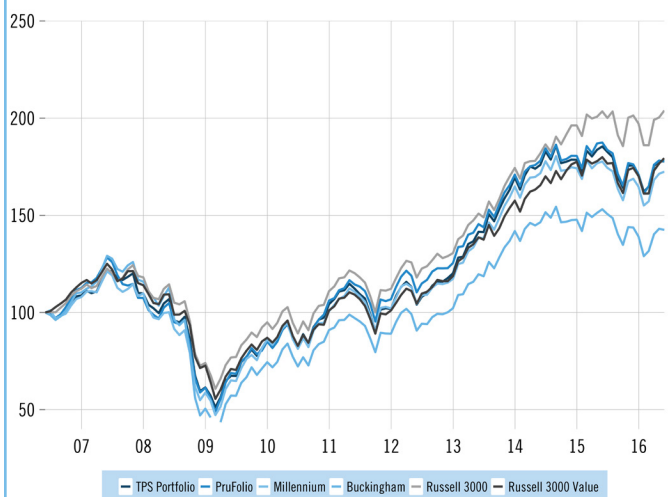
Royal Dutch Shell PLC (RDS/A)

Royal Dutch is engaged in the exploration, production, refining and sale of petroleum products worldwide. While the shares have rebounded sharply from January's multi-year low as the price of crude has bounced back, they remain well off the \$83 high set two years ago. Some are concerned that the firm paid too much for its recent purchase of BG Group, but we like the acquisition and Q1 results showed the new assets are already transforming RDS's business and cash flow profile. Additionally, BG accelerates Shell's position in liquefied natural gas and other projects, materially boosting reserves and production, and potentially generating annual cost savings of \$2.5 billion. While we don't expect operational challenges to disappear, we believe they are nearer term in nature as we still subscribe to the long-term global energy story given that usage in emerging economies continues to rise and should materially add to demand dynamics in the coming years. In the meantime, we think the company can generate meaningful cash through divestiture, supporting the attractive dividend (the net yield is 6.6%).

Target (TGT)

Target is one of the largest domestic discount retailers, operating 1,793 Target and SuperTarget stores. TGT earned \$1.29 per share in fiscal Q1 2017 (vs. \$1.19 est.) on sales of \$16.2 billion (vs. \$16.3 billion est.), but improvement of the operating margin was offset by lower revenue and lower same-store-sales comparables. Though management reaffirmed full-year EPS guidance of \$5.20 to \$5.40, investors were disappointed. CFO Catherine R. Smith explained, "We believe we're pursuing the right strategy, and our strategy is working. We have many levers we can deploy to drive our performance, even if the environment remains challenging. As a result, even with a more tempered view of the second quarter, we are still focused on achieving full-year adjusted EPS within the guidance range we provided at the beginning of the year." The company expects to refinance high-cost debt by issuing 10- and 30-year bonds at "very attractive" rates, ultimately saving \$5 million to \$10 million per quarter. Despite and because of the recent downturn in the stock price, we remain fans of Target as the shares are trading for 14 times forward earnings and yielding 3.3%. ■

NEWSLETTER PORTFOLIO PERFORMANCE



	May	YTD	1-Year	3-Year	5-Year	10-Year
Newsletter Portfolios						
Buckingham	-0.38	2.49	-6.92	5.99	7.98	3.61
Millennium	0.64	4.69	-2.96	7.56	9.28	5.60
PruFolio	-0.22	3.96	-5.16	6.92	9.22	5.92
TPS	-0.07	3.91	-4.17	7.89	9.62	5.92
Major Indexes						
Russell 3000	1.79	3.41	0.22	10.56	11.15	7.39
Russell 3000 Value	1.58	5.41	-0.29	8.97	10.45	6.02
S&P 500	1.80	3.57	1.71	11.05	11.66	7.41
Dow Jones Industrial Avg	0.49	3.34	1.39	8.19	9.97	7.55

	Inception Date	Since Inception	Index Return	Index
Buckingham	01.21.03	11.06	9.20	Russell 3000
Millennium	12.31.99	8.88	4.64	Russell 3000
PruFolio	12.29.00	12.66	5.46	Russell 3000
TPS	03.10.77	17.74	10.79	S&P 500 ¹

Since *The Prudent Speculator's* launch in March 1977, its 1,852 stock recommendations have returned, on average, an annualized 17.02%, not including dividends.

As of 05.31.16. All data are total returns, except for that of all recommended stocks, which excludes dividends. Data for periods greater than one year are annualized. The Dow Jones Industrial Average (DJIA or Dow) is a price-weighted average of 30 actively traded "blue chip" stocks, primarily industrials, but includes financials and other service-oriented companies. The Russell 3000 Index measure the performance of the largest 3,000 U.S. companies. The Russell 3000 Value Index measures the performance of those Russell 3000 Index companies with lower price-to-book ratios and lower forecasted growth values. The Standard & Poor's 500 Stock Index (S&P 500) is an unmanaged index of 500 stocks that is generally representative of the performance of larger companies in the U.S. ¹The Russell 3000 Index lacks sufficient history to match that of Al Frank's TPS Portfolio. We therefore have shown the S&P 500 Index for comparison purposes. SOURCE: Al Frank using data from Bloomberg

TPS Portfolio is Al Frank's actual investment portfolio. Though not presently leveraged, it has been so in the past. Buckingham Portfolio is John Buckingham's actual investment portfolio. Though not presently leveraged, it has been so in the past. Millennium Portfolio is unleveraged and hypothetical. PruFolio is unleveraged and hypothetical.

All portfolio returns are calculated on a total return basis and reflect the reinvestment of dividends, if any, margin leverage and margin interest charges, trading costs and subscription costs. There are inherent limitations with in hypothetical or model portfolio results as the securities are not actually purchased or sold. They may not reflect the impact, if any, of material market conditions which could have an impact on AFAM's decision making if the hypothetical portfolios were real. Hypothetical performance is shown for illustrative purposes only and should not be interpreted as an indication of performance of any AFAM portfolio. The use of leverage magnifies gains and losses and increases risk to a portfolio.

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