

**Quote of the week**

“How little you know of the age you live in if you think honey is sweeter than cash in hand.”  
*Ovid (43BC to 17AD)*

In the last couple of weeks we have had more than one client ask us about covered calls, how they work and why we use them in our Classic Growth accounts. If a few are asking that means *a lot* of you (the silent majority) are wondering the same thing. Here is a back of the napkin explanation:

A call option gives the buyer of the option the right to buy someone's stock (call it away) at a certain price for a period of time. That buyer pays the person who is willing to sell their stock for the right to call it away from them.

Our clients in our Classic Growth accounts are periodically sellers of call options; meaning they are willing to sell their stock at a certain price, and don't mind getting paid by the option buyer while they wait to see if the stock goes up to their selling price.

Let's look at a real example on a stock we bought 18 months ago and how the covered calls have worked thus far.

On October 9th, 2008 we bought Mosaic in our Growth accounts at \$39. Mosaic is a big fertilizer company located in Minnesota. The stock had peaked at over \$150 in the summer of 2008, but apparently short-term traders thought people were going to quit eating and pummeled the price of the company's stock down to where we thought it was a bargain...so we bought it.

By May of 2009, 8 months later, Mosaic was at \$55, a nice 41% profit. At this time we thought that \$65 would be about all we could expect out of Mosaic so we sold a call option for July at \$65 per share. For that option the buyer gave us \$1.55 per share; so if you owned 100 shares you would have had \$155 (minus a small trading cost from Ameritrade) deposited in your account. 1 option covers 100 shares.

July rolled around and Mosaic did not get to \$65, so the option that we sold expired and you still owned Mosaic. Now however you were \$155 richer than you were before we sold the option.

In August of 2009 we sold another call option on Mosaic for September at \$65, got \$1.30 for it, and it expired too.

Then we sold December \$60 call for \$2.35 and it expired

Then we sold a March 2010 \$75 call for \$1.10, it expired.

Last week we sold a May \$65 call for \$1.65. (see a pattern?)

*By the 3rd Friday in May either:*

Mosaic will be above \$65 and we will have to sell it, **OR**

Mosaic will be below \$65 and we will keep it and maybe sell another call on it. Whew!

So let's compare Mosaic *with and without* the calls.

First **without calls** written:

Buy Mosaic at \$39 18 months ago. Today it is at \$60 = gain of \$21 = 55% appreciation in 18 months. Not too shabby.

**With call options:**

Buy Mosaic at \$39 18 months ago.

1. Sold July call for \$1.55 (= \$155 for 100 shares)
2. Sold August call for \$1.30
3. Sold September call for \$1.30
4. Sold December call for \$2.35
5. Sold March call for \$1.10
6. Sold May call for \$1.65

The total earned from the calls we sold six different times has been \$9.25 per share.

Now, 18 months later, people are still eating, the stock has gone up, and today Mosaic is at \$60 = gain of \$21 + \$9.25 in option income = a total gain of \$30 = 78% total return in 18 months.

For 100 shares, the total gain without covered calls: \$2128 = 55%. Darn good. But with covered calls the gain is \$3053 = 78%, darn better.

In essence we have collected for our clients \$925 while we have been waiting for the stock to hit our "happy to sell it" price. Covered calls reduce the risk of owning stocks simply because the income is higher from them.

**BUT**...there is no free lunch right? What is the risk? Well the stock could go down, or way up...way above our \$65 "happy to sell it" price. In that case we would leave money on the table. We're fine with that. We are more of the "bird in the hand" kind of people and don't want to be pigs about it. If Mosaic goes above \$65, then our clients who sold calls will have really netted \$74.25, about 90% more than they paid 20 months before. No need to be greedy, we'll be happy and move on.

You'll never guess who likes this strategy. Suze Orman! Click below to hear her 4 minute explanation of covered call writing.



[http://www.youtube.com/watch?v=TJjw\\_agjJ3M&feature=related](http://www.youtube.com/watch?v=TJjw_agjJ3M&feature=related)

Because the SEC doesn't like us to "cherry-pick" a transaction, here are **all results** for covered calls since 2007 assuming you owned 100 shares of each stock.

**2007 Sold calls on:**

Wynn Resorts, 4 times + \$910  
 Thor Corp., once + \$137  
 Cognizant Tech, 3 times + \$645  
 Adobe Corp., once + \$145

**2008**

Apple Computer, twice + \$701  
 Lifecell, once + \$243

**2009**

Mosaic, 3 times + \$520  
 Apple, once + \$320  
 Diamond Offshore, once + \$267  
 Aflac, once + \$125  
 Accenture, once + \$161  
 Wynn Resorts, once + \$245  
 Research in Motion, once + \$239  
 Apollo, once + \$200

**2010**

Deckers Outdoors, twice + \$440  
 Mosaic, twice + \$275  
 Amedisys, twice + \$285  
 Buffalo Wild Wings, twice + \$390

All totaled we have brought in a minimum of \$6248 for you by selling covered options in the last 3 1/4 years.

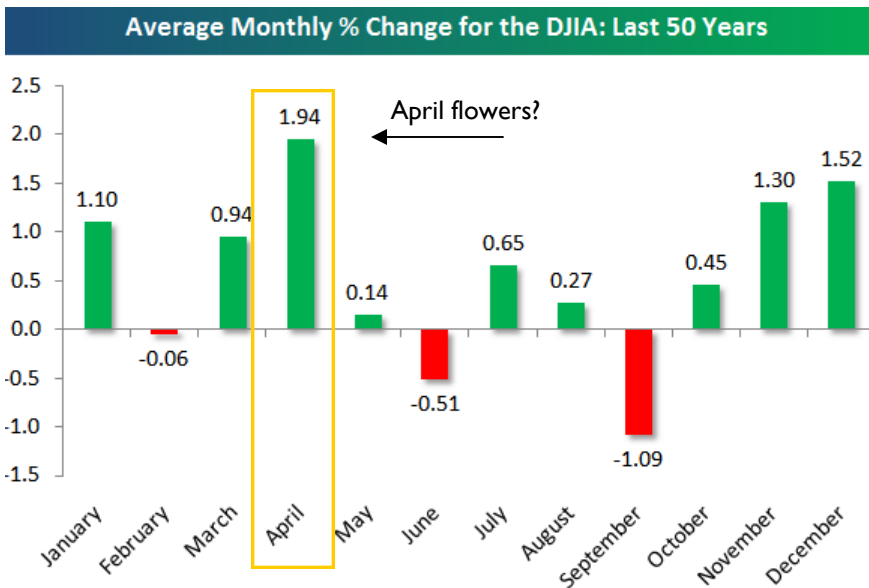
In the above years we were called out of Cognizant Technology at the equivalent of \$92.50, Diamond Offshore at \$88, Adobe at \$45, Accenture at \$37 and Apple at \$155. Apple is the only one we left much money on the table, about \$80. But today Cognizant is \$40 *below* where we were taken out. Since we had twice as many shares of Cognizant than Apple, those two worked out in the wash. The key is to stay consistent and not get greedy. Bulls make money, bears make money, pigs get slaughtered.

**You know what. Covered call writing is a bunch of work for us, but it is something we do for our Classic Growth clients that puts cash in their pocket, "dolla dolla billz ya'll"; and usually covers the fee we charge to manage their account. Sell a call, hear cha-ching, smile.**

*You should carefully consider the investment objectives, potential risks, management fees, and charges and expenses of the Fund before investing. The Fund's prospectus contains this and other information about the Fund, and should be read carefully before investing. You may obtain a current copy of the Fund's prospectus by calling 1-888-711-2837 or visiting [www.sbauerfunds.com](http://www.sbauerfunds.com). Past performance is no guarantee of future results. The investment return and principal value of an investment in the Fund will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. Sheaff Brock Investment Advisors, LLC (SBIA) does not guarantee the accuracy or completeness of this report, nor does SBIA assume any liability for any loss that may result from reliance by any person upon any such information or opinions. Such information and opinions are subject to change without notice and are for general information only. Index return and yield data is from *The Wall Street Journal and Thomson*. Past performance does not indicate future results. Model account returns are net of fees and commissions and include the payment of dividends which are held in money market funds pending reinvestment in other portfolio securities. Client returns may differ because all securities in the model may not be owned by each client. The securities mentioned in this report can be, and often are, owned by clients and employees SBIA. Clients and prospective clients should understand that there is no assurance that capital gains made in the past will continue. There is always the chance that market conditions or portfolio performance may deteriorate in the future, and clients may experience real capital losses in their managed accounts. The Classic Growth model and Dividend Growth and Income model are compared to the performance of the S&P 500 and sometimes to the Dow Jones Industrial Index (DJIA) although the model positions may not reflect the securities making up these indices. Neither comparable index may be an appropriate comparison index as our model accounts may own small and mid-cap companies not represented in the S&P 500 or the DJIA. There were no other strategies employed to obtain the results portrayed other than those strategies disclosed in the Sheaff Brock Investment Advisors, LLC Form ADV or other disclosure brochure.*

The first quarter of 2010 has certainly been different than the first quarter of 2009...thank the good Lord. This year the stock market rose about 5% whereas last year stocks were pounded to a bloody pulp.

According to [bespokeinvest.com](http://bespokeinvest.com) April historically has been the best month as you can see below.



One day left in the first quarter and our managed accounts are doing a yeoman's job against the market. The Auer fund is hanging in there. We think it is like a coiled spring.

<b>Performance year-to-date as of 3/30/10</b>	
Sheaff Brock Growth Model	+9.1%
Sheaff Brock Dividend Growth	+9.5%
Auer Growth Fund	+3.3%
S&P 500	+5.7%

Bob Auer was on CNBC a week ago and talked about a few favorite stocks. It's worth your time. Click below.

<http://www.cnbc.com/id/15840232?video=1448732185&play=1>

Our office will be closed on Good Friday, a market holiday; you can call, we just won't answer! Have a great Easter and root for Butler this weekend...a real life David and Goliath story!

