

Quick Guide To Preferred Stock Investing During A Global Credit Crisis



For Reader's Of

Preferred Stock Investing

By Doug K. Le Du

QUICK GUIDE TO PREFERRED STOCK INVESTING DURING A GLOBAL CREDIT CRISIS

For many of you, it may have been a while since you read *Preferred Stock Investing* and I know there are those who have yet to read the book (www.PreferredStockInvesting.com). The opportunity in front of us is so huge that it troubles me that even one of my readers might miss out simply because they were confused about how to apply the CDx3 Income Engine during these historic times.

If you understand it, then decide to do something else with your investment money, fine. But I would hate to find out later that you let this historic opportunity pass you by because I was not clear enough about how to take advantage of it using the CDx3 Income Engine.

In this *Quick Guide*, I will also explain to you where the key pieces of the CDx3 Income Engine – the CDx3 Bargain Table (when buying), the CDx3 Seller’s Calendar (when selling) and the CDx3 Key Rate Chart – fit into the overall strategy. I have made the references to these three key pieces clickable links throughout this *Quick Guide* so that you can see examples of these documents and follow along with the explanation (got a question? CustomerSupport@CDx3Investor.com).

These are the actual, current CDx3 documents. For more details please refer to the provided page numbers within *Preferred Stock Investing*.

As always, all of the usual disclaimers apply here- I do not know your personal financial goals, resources or risk tolerance so specific investment decisions are up to you. My goal is to let them be decisions that are more informed. This *Quick Guide* is to be considered educational rather than advisory.

Now before I lay this out, let’s get a couple of administrative points out of the way. First, like any investment, reaping a return assumes that the entity you are investing in stays in business (more on this in a moment). Second, investing is no place for next week’s grocery money. In these two respects, the CDx3 Income Engine is no different than any other investment method.

HERE’S THE OVERALL CDx3 STRATEGY: Use the highest quality preferred stocks to earn above average dividend income while simultaneously creating multiple downstream capital gain opportunities.

HOW IT’S DONE: CDx3 Investors buy their CDx3 Preferred Stocks at a point in time when research shows the market price tends to be relatively low, less than \$25.00 per share (currently \$20-\$22 per share in most cases) and hold their CDx3 Preferred Stocks until (a) you can sell for the Target Sell Price (*Preferred Stock Investing*, page 85) or (b) the issue is ‘called’ by the issuing company for \$25.00 per share. Today’s high dividend payers (current average CDx3 annual dividend rate = 8.8%) will almost certainly be called. But either way, you realize a capital gain in addition to the above-average dividend income in the mean time (current average annual dividend yield is about 11%).

Now to the details on selecting, buying and selling CDx3 Preferred Stocks during this global credit crisis:

SELECTING - MINIMIZE YOUR RISK BEFORE INVESTING A DIME: To qualify as “CDx3 Preferred Stocks” regular preferred stocks must meet the ten CDx3 Selection Criteria presented in Chapter 1 of *Preferred Stock Investing*. For example: (a) the issuing company must have a *perfect track record* of never having suspended dividends on a preferred stock, and remember these are multi-billion dollar decades-old companies; (b) the dividends must be ‘*cumulative*’ meaning that if the issuing company misses a dividend payment to you, which I have never seen happen with a CDx3 Preferred Stock, they have to make it up to you later (they still owe you the money); and (c) carry an *investment grade* Moody’s creditworthiness rating.

The CDx3 Selection Criteria have successfully screened out *every one* of the financial institutions that have failed during this crisis - New Century, Washington Mutual, Lehman Brothers, Freddie Mac, Fannie Mae, IndyMac and the other smaller banks - all of them. Further, not one CDx3 dividend has been missed before or during this credit crisis. Exceptions can certainly come along, but that’s all they would be at this point – rare exceptions.

BUYING – TWO DIVIDEND QUARTERS AFTER IPO: While I cannot tell you *what* to buy, I can tell you *when* the research indicates a good time to buy is likely to occur (i.e. when the market price of a CDx3 Preferred Stock tends to be relatively low). During periods of increasing dividend rates (now), the market price of a CDx3 Preferred Stock will tend to initially raise, while it is offering the top dog dividend rate, then fall as newer, higher-payers are introduced. Makes sense.

This price drop usually takes about two dividend quarters to kick in (*Preferred Stock Investing*, Chapter 7). During this Global Credit Crisis, however, prices are falling sooner and further than they probably would have otherwise. This is due to the Rule of Rate/Price Opposition – rates up, prices down (*Preferred Stock Investing*, page 61).

Since we know that market prices, under current conditions, will tend to fall within two dividend quarters of IPO (see two examples, *Preferred Stock Investing* page 101), you can reduce your risk by limiting your buying activities to CDx3 Preferred Stocks that have already cleared their second dividend quarter. Every month, subscribers to the CDx3 Notification Service are provided with a list of these CDx3 Preferred Stocks.

This list is called the [CDx3 Bargain Table](#) and identifies CDx3 Preferred Stocks that, the research (and direct observation month after month) shows, have already experienced the price deflating effect of the Rule of Rate/Price Opposition and are generally available at bargain basement prices (currently \$20-\$22 per share in most cases).

By purchasing CDx3 Preferred Stocks after they have completed their second dividend quarter you not only boost the return on the money you have invested (your dividend yield), but by buying at the already-dropped price, you also set yourself up for a larger capital gain downstream when you sell for a much higher price (at least \$25 – keep reading).

SELLING - CAPITAL GAIN ON TOP OF DIVIDEND INCOME: As I have described, as dividend rates continue to go up (now), market prices tend to come down. But the research clearly shows that the opposite is true too. As the dividend rate on new CDx3 Preferred Stocks drops, the market prices of the older, higher-payers tends to rise –

Quick Guide To Preferred Stock Investing During A Global Credit Crisis For Subscribers

rates down, prices up. Because of this Rule, you are almost certainly going to have two opportunities to sell for a capital gain downstream, the first opportunity bigger than the second.

CAPITAL GAIN OPPORTUNITY #1: Remember that the Rule of Rate/Price Opposition works both ways – when dividend rates go back down (and they will), market prices of CDx3 Preferred Stocks will tend to come up. The CDx3 Seller’s Notification email message that subscribers to the CDx3 Notification Service receive every month includes the direction of rates, INCREASING, DECREASING or STABLE, and illustrates that direction on the [CDx3 Key Rate Chart](#) over the last 60 months. When rates are decreasing, sellers consider selling at a point in time when the market price of a CDx3 Preferred Stock will tend to reach a high point. This date is indicated on the [CDx3 Seller’s Calendar](#) (*Preferred Stock Investing*, page 143) in yellow. No need to look up your market prices any other time since these are the dates that the market prices of your CDx3 Preferred Stocks are most likely to reach a relatively high value (due to the Rule of Buyer/Seller Behavior, *Preferred Stock Investing* page 67).

CAPITAL GAIN OPPORTUNITY #2: What if market prices never come back up? That would defy the research not to mention common sense. When dividend rates fall back down to, say, a more normal 7%, a new 7%-er will be introduced at a market price of \$25. Today’s CDx3 Preferred Stocks carry dividend rates over 8%. If a new CDx3 Preferred Stock that pays 7% is selling for \$25, how could an 8+% CDx3 Preferred Stock sell for less than \$25?

Can there be exceptions? Sure. And let’s say that that’s exactly what happens. The market price of your 8+% CDx3 Preferred Stock that you purchased for \$20-\$22 during the Global Credit Crisis never goes above \$25 again; it stays at or even below the price that you originally paid. How will you make a capital gain then? Easy—just hold onto it until it gets “called.”

All CDx3 Preferred Stocks have a five year call date; that is, the issuing company regains the right to purchase your shares back from you five years after IPO. And they are required to pay you \$25 per share if they do so, regardless of what you originally paid.

THE LIKELIHOOD OF A CALL: So how likely is it that the 8+% CDx3 Preferred Stocks that CDx3 Investors are buying today (for \$20-\$22 per share in most cases) are going to be called five years from now?

Extremely likely (see ‘refinancing,’ *Preferred Stock Investing* pages 54-55 for an explanation and real example of why this is the case or see [this article](#) in the February 2008 issue of the *CDx3 Newsletter*).

So even if, for some odd reason, the market prices of today’s 8+%-ers do not go back up when dividend rates come back down to, say, a more normal 7% (per the Rule of Rate/Price Opposition), your shares will almost certainly be bought back from you, for \$25 per share, by the issuing company – you have a “built-in buyer.”

In that *extremely likely* event, you will realize a capital gain of about \$3-\$5 per share on the CDx3 Preferred Stocks that you are buying today on top of the 11% *annual* dividend yield that you are going to be making in the mean time. This combination of 11% annual dividend yield plus a \$3-\$5 capital gain (if you wait for a call), produces an overall effective annual return in the teens (see *Preferred Stock Investing*, back cover).

WHAT HAPPENED LAST TIME? The last time dividend rates increased and exceeded 8% was in 2002 followed by decreasing rates the next year. When rates were increasing during 2002, market prices went down just like now, but for different reasons (uncertainty related to war). But when dividend rates came back down again in 2003, market prices went back up and CDx3 Investors sold their 2002 issues for an average price of \$27.42 throughout 2003 for an average effective annual return of 16.23% (the data for each of these 2002 CDx3 Preferred Stock is presented on page 128 of *Preferred Stock Investing*).

SUMMARY: So here it is in a nutshell-

- ✓ **Select The Best-** The CDx3 Selection Criteria select just the highest quality preferred stocks, as illustrated by their perfect track record, even during this historic Global Credit Crisis – not one failure, not even one missed dividend;
- ✓ **Buying-** The monthly [CDx3 Bargain Table](#) identifies CDx3 Preferred Stocks at a point in time when their market prices tend to be very favorable for your purchasing consideration, right now between \$20-\$22 per share in most cases (which calculates to an annual dividend yield around 11% to you);
- ✓ **Selling, Opportunity #1-** Look for market prices to increase once dividend rates on newly issued CDx3 Preferred Stocks start to come back down (after the credit crisis blows through). The direction of CDx3 dividend rates is illustrated on the monthly [CDx3 Key Rate Chart](#). To see if it is a good time to consider selling, check the market price of your CDx3 Preferred Stock on the date explained by the Rule of Buyer/Seller Behavior and highlighted in yellow on the monthly [CDx3 Seller's Calendar](#). This date is a good time to consider selling and collecting your capital gain;
- ✓ **Selling, Opportunity #2-** If a good selling price never presents itself, you could simply hold the issue until it is called (at which point you will receive \$25 per share). Today's 8+%-ers will almost certainly be called when their call date arrives, five years after IPO. In the mean time, enjoy your 11% annual dividend yield.

Use the highest quality preferred stocks to earn above average dividend income while simultaneously creating multiple downstream capital gain opportunities – the CDx3 Income Engine. And that's how to use it during this credit crisis.

Have a question? Email CustomerSupport@CDx3Investor.com

If you choose to let this historic opportunity go by, do so because you feel that it is in your best interest, not because you are uncertain about how to take advantage of it.

Many Happy Returns,

Doug K. Le Du, author *Preferred Stock Investing*

CD Times 3, CDx3, CDx3 Income Engine, CDx3 Investor, CDx3 Portfolio, CDx3 Preferred Stock, CDx3 Bargain Table, CDx3 Seller's Calendar, CDx3 Key Rate Chart are trademarks of Doug K. Le Du. All rights reserved.