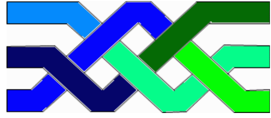

Capital Drain

Rick's investment opinion newsletter July, 2013 v.9 no.4

Before printing, think about the environment

Hi Readers,

I'm sending the July letter out earlier in the month than usual, and it will probably be shorter than usual as well.

Two weeks ago I described the five stocks I was selling, and why. I've narrowed down the replacement candidates to four, which I want to tell you about before I buy them myself, so you get a head start and hypothetically possibly better price.

In my opinion:

Executive Summary:

- The recovery continues
- Energy stocks need a new careful review
- Four new dividend stocks I'll buy
- Credit Check: EQUIFAX

The recovery continues, and many US companies are doing well, but the prices reflect continued growth expectations. If you're holding shares of any of the conspicuous high-fliers, especially the "hot" new tech IPOs, you might consider selling into this enthusiasm. Better to risk a little less gain rather than a lot more loss.

As confidence in the economy spreads, investing in all-market index funds becomes more attractive. We are likely approaching the phase when a rising tide will lift (almost) all boats.

If you're inclined to pick among individual stocks, be conservative and be in the best of securities: stick to value, to safety, to short maturities (for debt), and call me to chat if you're concerned about anything you're holding.

Above all, avoid the investments that are at all-time extreme valuations: junk bonds, developing-country bonds, and headline-grabbing stocks with high P/E ratios.

The Details:

The **recovery continues** to creep along. Not everyone can see that, because if you don't have a job or enough money to live on, it still looks bleak. It is, though, getting better, bit by bit, in the US and in the world on average.

I think we need to add another word to our vocabulary. We have long used pairs like recession/expansion, or recession/recovery. The problem is that right after a recession has ended, if you tell most workers that they're not in a recession, they'll tell you you're out of touch (or crazy). Their world is still recessed. Their personal recoveries are still a long uncomfortable time in the future, and the fact of GDP having started to grow is not only too abstract but basically immaterial for them.

Our current words jump from “getting worse” to words that imply “all OK now.” We need a word to specifically describe the interim, the “bad but not worsening” or “getting back on our feet” time when GDP is doing well but many working people still are not.

If we could start from scratch, I'd redefine “recovery” to specifically include the idea that times are hard. Thus, “recession” bottoms to become “recovery” which eventually reaches “full employment. Unfortunately, too many people already interpret “recovery” as meaning “recovered.” I can't change the way people use existing words

With our paltry growth rate and high unemployment, we are definitely not recovered, even though we are fully four years past the GDP bottom.

I heard a discussion recently on the need to change the way we value **energy companies**. Some of them are going to see their valuations change dramatically. So what is an energy company, anyway? There are quite a variety:

- Extractors, like coal miners an oil drillers
- Electric Utilities
- Refiners, to turn raw oil into gas and diesel fuel, etc.
- Alternative production: sun, wind, tides, plant-based fuels, etc.
- Equipment producers: make necessary parts for all of the above

Someone, somewhere, will be the last living person to dispute the fact of man-made climate change, and the key part that fossil fuels play in that. It's unlikely that person will be a business executive, though.[1] Some of the extractors are still fighting against regulation, to be sure. The bulk of business, though, see what's happening and are planning their moves for the new energy economy that's coming. As investors, we need to monitor how well companies are adapting, in order to understand what the companies are worth.

The most extreme examples are extractors with a lot of coal and “dirty” oil. Increasingly, and inevitably, they will lose market share to cleaner alternatives. Further, bear in mind that these companies are valued based not just on what they dig or pump each year, but also on how much they own that is still in the ground, waiting to be extracted in future years.

The surprise for investors in those companies is that a lot of dirty fuel will never be burnt, or at least not until some future technologies can make the extraction and burning immensely cleaner. In some form, a “polluter pays” cost is going to be attached to the CO2

1 More likely a TV “news” opinionator.

dumped in the atmosphere by using those fuels. That carbon cost will make other fuels more attractive. The cost may even reach prohibited levels-- some fossil fuels may never leave the ground. The companies that own the coal that will never be burned are therefore less valuable, by the value of that coal, than an older analysis would have said.

Other companies will rise or fall similarly to the way we've seen computer technology re-make many competitive fields. The companies that most adroitly adapt to sell cleaner energy, or the equipment to make cleaner energy, will pull ahead of the pack.

In last month's letter, I reviewed the **dividend stocks** that I'd bought back in 2010, and I sold five: three that I actually bought, and two that were “bonus” spin-offs.

The ones I kept, with the prices I paid at the time, are:

		10/25/10		
ticker	name	price	div	yield
EXC	Exelon	41.33	2.1	5.00%
PFE	Pfizer	17.62	0.7	4.00%
KFT	Kraft	32.47	1.16	3.60%
DD	DuPont	47.7	1.64	3.50%
COP	ConocoPhillips	61.34	2.1	3.41%
CVX	Chevron	84.87	2.88	3.40%
JNJ	Johnson & Johnson	63.98	2.16	3.40%
INTC	Intel	19.87	0.63	3.20%

They're still doing well, so I'm holding them. As I discussed earlier, though, I'll be looking at the ones involved in energy: Excelon, Conoco, and Chevron, with an eye toward whether those might go.

To replace those, I'll buy:

		07/17/13		
ticker	name	price	div	yield
CM	Can Imp Bank Com	74.02	3.65	5.00%
SO	Southern Co	45.26	2.03	4.50%
UN	Unilever NV	41.01	1.4	3.40%
WM	Waste Mgmt	41.88	1.46	3.50%

Even after the years of stock advances, these are still a good price, sturdy companies, and offer nice dividends.

Canadian Imperial Bank of Commerce is a healthy bank, which didn't get caught up in the financial bubble, and so has been able to bargain-shop from bits of troubled banks and expand. Southern Company is a traditional electric utility, but it is one of the leaders in trying to move to cleaner energy sources. Surprisingly, Waste Management now has a big energy component, as it captures methane emitted from the trash it collects. Unilever is a nice consumer-product company, sturdy and steady.

I plan to take the money I got two weeks ago from selling the five, total it, divide it by four, and put roughly that much money into each of these stocks.

By the way, some of you may recall when it was advantageous to buy and sell stocks in “round lots” of multiples of 100 shares. In the computer age, that no longer matters at all. Just divide the allocated money by the price, round down to an integer, and buy that many shares.

So simple.

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If you've been following along with my roughly every-four-months pace, you're ready to go to EQUIFAX (again.)

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It's time to check the spelling and ship this to you.

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Take care,

Rick

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"Our doubts are traitors,
And make us lose the good that we oft might win,
By fearing to attempt."
--W. Shakespeare

A collection of fine industrial Boilerplate, but true:

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