

# Investing During Economic Downturns

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Stocks that can help to provide downside protection while positioning a portfolio for the upturn if /when markets stabilize. The fact is that the key to success is to look for large cap stocks paying dividends with:

- 1) Low Debt
- 2) PEG Ratio below 1
- 3) Stable outlook
- 4) High Ratings

The process used to find investments with these criteria is fully outlined and taught in *The Disciplined Investor – Essential Strategies for Success* (available at Amazon and Borders)

## ***Investing During Economic Downturns***

Just listening to investors or analysts talk these days and it is hard to miss the ongoing chatter about an apparent and impending recession. Some analysts say we are already in one, others point to its arrival in the near future. Regardless of what the experts have predicted, no one can deny our country's economic downturn. Looking at the pathetic housing market, the recent lackluster results in the financial markets, and the absolute horrific price of gas, it is fairly easy to assume we are well into an economic downturn, moving toward a full-blown recession.

So what do you do when it comes to investing in this turbulent time? Do you panic and pull out all your investments, toss the cash in a garbage bag and hide it under the mattress until this is all over? Some might advise such a ridiculous strategy, but the truth is that there is a benefit in being a smart investor during this time.

Investing, like any other business, is all about making good use of whatever advantage you have, and when the masses pullout, it is often a good time to think about going in.

Recession/bear market investing is absolutely different than traditional investment strategies for many reasons. To begin with, the average investor should probably not enter into risky investments like futures trading, option buying, or strategies that utilize leverage at a time like this. When an investment is considered a risky move in a good economy, then in a bad economy it should be considered off limits, unless of course you have a powerful grasp on the art of the advanced trading style that gives you a leg up. For most investors though, it is a good idea to stay away from such risky endeavors, and focus on the 5 pillars of investing during economic downturns.

The Five Pillars of Investing During Economic Downturns:

- 1. Understand The Business Cycle**
- 2. Perform an Internal Audit Before Buying Anything**
- 3. Invest in Evergreen Industries**
- 4. Invest in Long-Term, Proven Winners**
- 5. Look for Deep Value Stocks**

The first and most important move any investor can make during an economic downturn is to educate themselves about the business cycle. All businesses, and our economy, go through cycles. They have growth periods, followed by stagnant periods, followed by downward periods. This is something that happens to the biggest companies in the world, and in effect can be an analogy for the economy in general.

Understanding that recessions like any other type of economic swing, is temporary, will lead you to invest wisely. This is the opposite of the panic strategy that some suggest, advising to pull out all your money and hide until the recession is over. Understanding that a business has cycles, and that the markets are nothing more than large representation of a substantial group of businesses will help guide your investment strategy so you can stay focused on the long term.

The next step in coming out ahead as an investor during a recession is to take an internal financial audit. From time to time it makes sense to look at what you have to invest, and what you need to get out of those investments in the short term. Looking at where your finances are in terms of investments, and in terms of the cash flow you need to get by, in case the recession gets worse, will help guide your investment strategies. Just as it is not wise to pull out of the markets entirely at a slow economic time like this, it is also not wise to bet the farm on any stock or investment at a time like this. Performing an internal financial audit will give you a good idea of how much you can invest without causing too much trouble in your life if for some reason the investments don't pan out, or the cost of your daily living increases substantially.

With a firm grasp on both the economics of a downturn and the financial situation in your life, it is time to start picking "recession proof" investments. The best place to start when looking for a recession proof investment is to select a stock or fund by industry. Look for evergreen industries that are as successful today, as they were yesterday, as they will be tomorrow.

Pharmaceuticals have performed especially strong during all types of economic situations, and are one example of an evergreen industry. Another play might be in the energy sector where oil companies are experiencing record profits despite the public's distaste with paying over \$3 for a gallon of gas. These just so happen to be the leading sectors of late.

Regardless of the industry you choose, make sure it has proven track record of success, or minimal losses during past recessions.

Once you have selected an industry that looks to be evergreen in its growth over the long term, it is now time to pick a long-term year winner. Stocks that perform at high levels for a long period of time are typically immune to becoming the major loss story of a recession. Companies like Pepsi, General Electric, and Johnson & Johnson typically are able to rebound from a recession without too much hemorrhaging. Buying a stock that is a long-term winner will narrow your chances of losing money, and just might help you to make some.

The final pillar is to look for value stocks. What stocks are typically high ticket stocks that seemed to have taken a major dip during a recession? Are those companies likely to get back on the profitability train after the recession leaves the station? Answering these questions and most importantly finding a company or series of companies that have seen their stock plunge, but are well equipped to come out of the recession stronger than ever should be a page in any investor's playbook.

### Stock Screener - MSN MONEY

**Criteria:**

**Market Capitalization  $\geq 1,000,000,000$**

**Debt to Equity Ratio  $\leq 1$**

**PEG Ratio Below 1**

**StockScouter rating  $\geq 9$**

**Current Dividend Yield  $\geq 2$**

**Price/Book Value  $\leq 2$**

### Definitions:

**Market Capitalization** : The value of a company's outstanding shares, as measured by shares times current price.

**Debt/Equity Ratio** : The most recent quarter long-term debt divided by the most recent quarter common stock equity.

**PEG Ratio** : The price-earnings (P/E) ratio for this company has been less than its average next year's projected earnings growth rate. For small and mid-cap stocks in particular, this is generally considered as a sign that a company may be undervalued.

**StockScouter Rating** : represents a balance, or trade-off, between a stock's expected return in six months and its expected volatility en route. Expected return is derived from a weighted blend of a company's underlying factor scores plus its place in market capitalization, sector and investment style trends. Top-rated stocks are expected to gain the most in the future with relatively less volatility.

**Dividend Yield**: A stock's dividend expressed as a percentage of the share price

**Price/Book Value** : The latest closing price of the stock divided by the most recent quarter's book value per share.

### Screen Results as of February 14, 2007

| Symbol | Company Name                        | Market Capitalization (000s) | Industry Name                    | Debt to Equity Ratio | Current Dividend Yield | Stock Scouter Rating | Price/Book Value |
|--------|-------------------------------------|------------------------------|----------------------------------|----------------------|------------------------|----------------------|------------------|
| ACAS   | American Capital Strategies Ltd     | \$ 68,369,100                | Closed-End Fund - Debt           | 0.75                 | 11.58                  | 10                   | 1.06             |
| CNL    | Cleco Ord Shs                       | \$ 15,241,870                | Electric Utilities               | 0.77                 | 3.54                   | 10                   | 1.51             |
| PTEN   | Patterson-UTI Energy Inc            | \$ 35,931,720                | Oil & Gas Drilling & Exploration | 0.01                 | 2.07                   | 10                   | 1.95             |
| TRV    | Travelers Companies Inc             | \$ 261,552,000               | Property & Casualty Insurance    | 0.23                 | 2.42                   | 10                   | 0.99             |
| WPC    | W.P. Carey & Co LLC                 | \$ 12,689,820                | Property Management              | 0.54                 | 5.78                   | 10                   | 1.98             |
| AHL    | Aspen Insurance Ord Shs             | \$ 25,522,760                | Property & Casualty Insurance    | 0.09                 | 2.05                   | 9                    | 0.91             |
| ATN    | Atlas Energy Resources LLC          | \$ 16,131,610                | Oil & Gas Drilling & Exploration | 0.84                 | 8.76                   | 9                    | 1.84             |
| CCU    | Clear Channel Communications Inc    | \$ 146,836,600               | Broadcasting - Radio             | 0.82                 | 2.54                   | 9                    | 1.72             |
| CINF   | Cincinnati Financial Corp           | \$ 62,781,200                | Property & Casualty Insurance    | 0.15                 | 4.13                   | 9                    | 1.06             |
| DOW    | DOW CHEMICAL                        | \$ 367,370,700               | Chemicals - Major Diversified    | 0.48                 | 4.32                   | 9                    | 1.89             |
| IP     | Interational Paper Ord Shs          | \$ 143,426,100               | Paper & Paper Products           | 0.76                 | 2.99                   | 9                    | 1.65             |
| IPCR   | IPC Holdings Ord Shs                | \$ 16,041,830                | Life Insurance                   | 0                    | 3.02                   | 9                    | 0.78             |
| PHG    | Koninklijke Philips Electronics ADR | \$ 414,030,400               | Electronic Equipment             | 0.16                 | 2.06                   | 9                    | 1.31             |
| PL     | Protective Life Ord Shs             | \$ 27,189,390                | Life Insurance                   | 0.42                 | 2.32                   | 9                    | 1.13             |
| PRE    | PartnerRe Ord Shs                   | \$ 43,340,730                | Property & Casualty Insurance    | 0.2                  | 2.3                    | 9                    | 1.01             |
| SLF    | Sun Life Financial Ord Shs          | \$ 278,248,100               | Life Insurance                   | 0.28                 | 2.76                   | 9                    | 1.8              |
| STD    | Banco Santander ADR Rep 1 Ord Shs   | \$ 1,098,880,000             | Foreign Money Center Banks       | 0.69                 | 9.31                   | 9                    | 1.64             |
| UTR    | Unitrin Inc                         | \$ 22,839,330                | Property & Casualty Insurance    | 0.24                 | 5.29                   | 9                    | 0.99             |

Investing in a Economic Slowdown: The Shield of Yield

Source: MSN Money/Horowitz & Company

\* Please note that the stocks listed should be carefully reviewed prior to investing. Please seek professional advice before investing in any security. All securities contain risk and you can lose principal in any investment. Stocks carry a great risk for loss of some or the entire principal invested.