

InvestWrite Essay

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Question: Lets say you are going to give your parents an allowance by investing in stocks that pay dividends. Pick three stocks in different industries that pay dividends and tell us why you chose them. Did they pay a high dividend compared to other stocks? Have they paid dividends for a long time? Describe why dividends are important when evaluating a stock. Finally, would you tell your parents to reinvest their dividends, to buy more shares of stock, or take cash payment?

Dividends as an Allowance

If I were going to give my parents an allowance by investing in stocks that pay dividends, I'd invest in American Home Mortgage (AHM), Energy Transfer Partners (ETP), and Bristol-Myers Squibb (BMY).

I chose American Home Mortgage (AHM) because they pay a dividend of about 12%, which is high compared to other mortgage companies like Countrywide Financial Corporation who pays a dividend of 1.48. They have paid dividends for more than five years now, and it started out as only 3 cents, but the most recent one was \$1.01, so it is growing. The PE ratio is only about 8.8. With a high dividend and low PE, the risk is relatively small. The market cap is 1.65 billion, a mid cap company, and it still has potential to grow. Its revenue growth rate is 34.40%. With the growing population and trend of vacation houses for the retired generation, American Home Mortgage is in good business, and is likely to prosper.

I picked Energy Transfer Partners (ETP) because they pay a dividend of 6.33, which is also high compared to some of the other stocks I looked at. They have paid dividends for 9 years now, starting out with 25 cents and tripling it to 75 cents. The PE ratio, 12.3, is low. The EPS is 3.85, which is very good. The revenue growth rate, 45%, is excellent. Energy Transfer Partners is a gasoline and oil company. People are getting more and more cars, which need to run on gasoline, and the demand for gas is still on the rise. With winter coming and the weather getting colder, people will also need to turn on the heat, which also runs on oil.

I selected Bristol-Myers Squibb (BMY) because they have a dividend yield of 4.5, which is high. They have been able to keep up the dividend for sixteen years, and the dividend has doubled. The beta is 1.02, which fits my kind of risk taking because I am between a conservative and a moderate risk taker. The PE ratio, 22.04, is not very high for a drug company. It has a market cap of 48.55 billion, and it is a large cap company. They are in a good industry that is likely to prosper. They specialize in drug research, development and manufacturing. Bristol-Myers Squibb's 43,000 employees are dedicated to discovering and providing innovative medicines that address significant medical needs of patients worldwide.

Once I get the dividends, I would tell my parents to reinvest dividends back into the company. We don't need the money for a while because I am still many years away from college and we don't need the money to buy something right away. When you reinvest your dividends, it can make a big difference. For example, if you had invested \$10,000 into Ibbotson's large-cap companies back in 1980 and had taken cash payment, you could sell it today for about \$130,000. Not too bad. But if you had reinvested dividends back into the company, you could sell it for about \$400,000!

Dividends are important when evaluating a stock for many reasons. If the stock goes nowhere, then you get paid dividends while you wait for the stock price to change. If the stock price drops, then the dividend rises to attract new buyers to invest in the company. In general, the companies that are paying dividends beat the market. For the first seven months of 2006, dividend-paying stocks returned 4.3% compared with a – 3.3% for non-dividend paying stocks. Also, thanks to a new change in the tax law, dividends have a tax of only 15% compared to the tax on other profits which can get up to 35%. According to Standard & Poor, this should save investors more than \$100 billion through 2008. Dividend-paying stocks are also low risk because investors are more willing to hold dividend stocks, so the stocks don't fall as quickly as non-dividend paying stocks.

I have enjoyed playing the Stock Market Game. The information I have learned will help me make good investments in the future.

Sources:

1. aol.fool.com
2. about.com
3. www.yahoo.com
4. moneycentral.msn.com
5. www.winninginvesting.com