

# INDIVIDUAL INVESTOR

SUMMER 2008



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## Yields (How Sweet They Are)

From dividend-paying stocks to inflation-protected bonds, today's income sources can still provide plenty of cash — but you need to know where to look by [Stan Luxenberg](#)

There's nothing like cash in hand — or the promise of a steady stream of it — to calm investors' nerves during turbulent times. And in recent months, as a

good number of stocks have dropped sharply and many bonds have also suffered, many people have turned their attention to income-producing investments.

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Chief Investment Strategist Stephanie Giroux offers advice on fine-tuning your portfolio in a tough market

Despite broad market volatility — or, in a few cases, because of it — intriguing opportunities have emerged, with some bonds and dividend-paying stocks selling at significantly lower prices. Even stodgy Certificates of Deposit (CDs) are looking relatively tempting.

That can be welcome news. Historically much of the stock market's total return has come in the form of dividends, and that income could be particularly helpful now if share prices continue to decline. At the same time, those who depend on cash from their investments

may also want to re-examine their holdings. By emphasizing value-priced, high-quality bonds and high-yielding blue-chip stocks, investors could potentially increase their income without taking excessive risks. Of course, investors must keep in mind that past market performance does not guarantee future results.

### A New Playing Field

Municipal bonds, issued by state, county or local governments, are normally considered safe. “They rarely default,” says Matt Fabian, Managing Director of Municipal Market Advisors, an independent research firm in Concord, Mass. Munis, as well as the tax advantages they can offer, usually come at the cost of a few percentage points in yield. But in May of this year, some 10-year AAA municipals yielded 3.96%, virtually the same yield as a taxable 10-year Treasury bond. Figure in the potential tax savings, and those munis are the equivalent of taxable bonds yielding 5.5% for someone in the 28% income tax bracket. “Many investors now have a big incentive to buy municipals instead of Treasuries,” says Perry Guarracino, TD AMERITRADE’s Fixed Income Product Manager. (It’s important to note that interest income on munis may be subject to the alternative minimum tax and discount bonds may be subject to capital gains tax.)

Munis may have this edge because of a peculiar combination of circumstances. As worries about mortgage defaults roiled the markets,

many investors raced to the safety of Treasuries, and that spike in demand pushed up prices of government bonds. When bond prices rise, their yields drop. But to buy Treasuries, many investors raised cash by selling municipal bonds. That depressed the prices of munis and increased their yields. In the meantime the subprime crisis threatened the AAA ratings of bond insurers, causing a sell-off in municipals and depressing their prices while increasing their yields. The chance to take advantage of that anomaly is likely to be short-lived, of course.

Mortgage market troubles have helped create what some consider better-than-normal possibilities for

## Mortgage market troubles have helped create what some consider better-than-normal possibilities for CDs.

Certificates of Deposit. CDs are typically very secure, as most are backed by the Federal Deposit Insurance Corp. at up to \$100,000 for individual accounts and \$250,000 for certain retirement accounts. TD AMERITRADE offers brokered CDs, which are similar to CDs purchased from a bank, except they can be traded on the open market. To compare the competitive rates available on current CD offerings, log on to your account, go to RESEARCH & IDEAS and click “Bonds & CDs.” (Brokered CDs sold prior to maturity in a secondary market may result in the loss of principal as a result of fluctuation in interest rates, lack of liquidity or transaction costs.)

One aggressive strategy some investors consider is to buy bonds that are below investment grade. Many of those securities may yield more than investment-grade bonds, but they are also at a greater risk of default. As the economy slows, companies issuing these bonds may fail to meet their obligations to bondholders. “If you are used to buying high-grade bonds, right now may not be the best time to reach for yield by purchasing lower-quality issues,” Guaracino says. Instead, investors could consider bonds with longer maturities, which pay slightly higher yields than shorter-term bonds without much additional risk of default.

Though choosing longer-term

bonds carries its own risks — when interest rates rise, prices of all bonds tend to fall, and long bonds tend to fall faster than shorter-term issues — the Federal Reserve may continue to cut rates through 2008. As rates fall, long bonds tend to show the greatest price appreciation.

### The Upside of a Down Market

One effect of falling share prices has been higher yields on stocks that pay dividends. The companies in Standard & Poor’s 500-stock index had an average yield of 1.9% in May, and that yield climbed as stock prices fell. Some high-quality shares were yielding more

than 4%. “A lot of high-quality dividend payers now sell at bargain prices,” says Josh Peters, editor of Morningstar’s *DividendInvestor* newsletter. “Investors have the opportunity as prices recover to earn capital appreciation while collecting dividends that are likely to keep on rising.” Of course, TD AMERITRADE Chief Investment Strategist Stephanie Giroux says, those yields could also evaporate as firms in recession trouble cut dividends to shore up capital. Investors should consider targeting stocks with long histories of stable cash flow, increased dividends and fundamentals that are most likely to support continued payouts.

Another way to find solid dividend payers is through mutual funds that hold large-cap stocks, says Giroux. Such funds tend to focus on low-priced shares that pay above-average yields. Additionally many international companies are also among the highest-yielding blue-chip choices, according to Giroux, but international investments

do involve special risks, such as currency fluctuations and political and economic instability.

### Screening Your Choices

TD AMERITRADE’s mutual fund screener (under RESEARCH & IDEAS, choose “Mutual Funds” and click “Screener”) can help you find



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funds that meet specific criteria. For example, on a particular day you might find 250 funds paying dividends of at least 4%. If you are looking for comparatively low prices, you could then specify a price/earnings (P/E) ratio of 15 or below, thus possibly narrowing the field to 20 funds.

Many Exchange Traded Funds (ETFs) also hold dividend-paying stocks. To screen for ETFs with specific characteristics, go to “Screeners,” then “ETF Screener” under RESEARCH & IDEAS. As an example, a screen for funds yielding 4% or more on May 14, 2008, produced 47 choices, including funds specializing in large-value stocks, foreign issues and real estate investment trusts.

You can also screen for individual stocks (click “Screeners,” then “Stock Screener” under RESEARCH & IDEAS). A screen on May 14, 2008, for large-cap stocks with a dividend yield of at least 4% and a P/E ratio of 15 or less pinpointed stocks of 231 companies.

Using these and other TD AMERITRADE tools, you can assemble a broad array of investments designed to provide a good mix of portfolio-stabilizing income and capital gains. Although diversification does not eliminate the risk of experiencing investment losses, a well-diversified portfolio has the potential to deliver healthy results even when markets take unsettling turns. ■

***Before investing in a mutual fund or ETF, carefully consider the particular fund’s investing objectives, risks, charges and expenses involved. To learn how to obtain a prospectus containing this and other important information, please visit [www.tdameritrade.com](http://www.tdameritrade.com) or call a TD AMERITRADE representative at 800-669-3900. Please read the prospectus carefully before investing.***

*Market volatility, market volume and system availability may delay account access and trade executions. Availability of products and services may vary by jurisdiction. All investments are subject to risk and may lose value. As a deposit obligation of the issuing bank, brokered CDs, along with other deposits you may hold at an issuing bank, will be eligible for insurance by the FDIC of up to \$100,000 for nonretirement accounts and \$250,000 for Individual Retirement Accounts (IRAs) and certain other retirement accounts.*

*Investments in fixed-income products are subject to liquidity (or market) risk, interest-rate risk (bonds ordinarily decline in price when interest rates rise, and rise in price when interest rates fall), financial (or credit) risk, inflation (or purchasing power) risk and special tax liabilities.*

*ETFs are registered investment companies that trade on an exchange, like a stock does. Commission fees apply. Those who practice frequent dollar-cost averaging and active traders may generate trading costs that outweigh any cost benefit. Trading prices may not reflect the actual net asset value of the underlying securities. ETFs can entail market, sector or industry risks similar to direct stock ownership. Municipal security interest may be subject to the alternative minimum tax.*

*TD AMERITRADE does not provide tax advice. We suggest that you seek the advice of a tax-planning professional with regard to your personal circumstances.*

# The Trouble With Timing

As tempting as it is to try to outguess the market, it's a loser's game

**T**iming may be everything, but for investors it has its limits. The goal of market timing is to catch market upswings and dodge downturns. It's an investment approach that bases decisions about when to buy and sell securities on predictions about where the market is headed. But trying to escape before the market dives is often more costly than letting investments ride, says Stephanie Giroux, TD AMERITRADE's Chief Investment Strategist. Investors are often too late to sell and also miss the bottom when they try to get back in — and missing a market rebound can be worse than weathering a dip.

“Research has shown that outperformance tends to happen during a limited number of days,” Giroux says. FactSet data published by Ibbotson Associates show that \$10,000 invested in a typical Standard & Poor's 500-stock index fund in 1980 would have grown to \$286,000 if left alone through 2006. But if you happened to miss the top 10 days in that period, you'd have ended up with just \$131,000.

The object of market timing is to be out of the market on its worst days, not its best. But that's tough to accomplish consistently. “And it requires you to watch the market constantly,” Giroux says.



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**Trying to escape before the market dives is often more costly than letting investments ride.**

Even if you do well with this approach, transaction fees and taxes on capital gains can substantially undercut your returns.

Instead, pursue a balanced, diversified approach across and within the major asset classes: equities, fixed income and cash. During times of heightened

volatility, Giroux says, you might consider boosting your cash holdings temporarily, but typically not to more than roughly 10% of your portfolio. “You have to fight your fear of the market,” she adds, “and stay fully invested even when things seem uncertain.”

— Jennifer Pellet



# According to Plan

TD AMERITRADE's Portfolio Planner can help you adjust your asset allocations to support your goals



JIM ARBOGAST/GETTY IMAGES

**A** sset allocation — the percentage of investing dollars assigned to each asset category — is considered crucial for balancing risk and return. Yet it's easy to lose sight of how your portfolio breaks down by asset and sub-asset class.

TD AMERITRADE's Portfolio Planner can help bring that bigger picture into focus. Log on to your account, then click "Portfolio" under PORTFOLIO & ACCOUNTS.

The tool lets you analyze current holdings and design an allocation strategy. Then you can make trades that help bring your portfolio in line with your investment goals. "Choose from five pre-built allocation strategies, design

your own, or create a basket of securities and assign allocations to each one," says John Bell, Product Manager, TD AMERITRADE's Managed Solutions Group.

Suppose you choose a pre-built model tailored to "aggressive" investment goals.

*Compatible securities are assigned by TD AMERITRADE to an asset class and subclass based on a third-party provider's asset classification service. Portfolio Planner only uses market orders to buy/sell compatible assets (marginable stocks, Exchange Traded Funds [ETFs] and closed-end funds [CEFs]). Incompatible assets currently include mutual funds (which will soon be available) as well as Pink Sheets and Over-the-Counter Bulletin Board (OTCBB) securities, options, limited partnerships, individual bonds and short positions.*

*TD AMERITRADE does not make recommendations or determine the suitability of any security, strategy or course of action for you through your use of Portfolio Planner. Any investment decision you make in your self-directed account is solely your responsibility.*

*To utilize the Portfolio Planner you must subscribe to real-time quotes for all exchanges. The tool uses real-time quotes to calculate rebalance transactions. Access to real-time market data is conditioned on acceptance of the exchange agreements. Professional access differs and subscription fees may apply.*

(The five alternatives range from capital preservation to aggressive.) That strategy's asset allocation targets are 79% equity, 13% fixed income and 8% other, which includes alternative investments and securities such as real estate, commodities and long/short funds. Those asset classes are then broken down into sub-asset classes, each with its own allocation target.

Next you can choose Exchange Traded Funds, closed-end funds or stocks to fill allocation slots, using TD AMERITRADE screening tools to find investments based on your individual parameters. Portfolio Planner prompts you to set target allocations for all assets.

"Once you've set your list of assets and target allocations," Bell explains, "the tool determines what trades will bring your allocation back in line with your target. You can then review the orders and execute the trades with a single click." The only costs are the standard trading commissions. "You do the research to choose your investments. The tool simply shows you how to get to your target allocation," Bell says. — JP

# Five Tips on When to Exit

## The right plan for a stock sale can protect gains or minimize losses

Knowing when to sell a stock can be far trickier than picking one. It may not feel right to unload a stock that's soaring or to dump one that's down. Yet you can sometimes give up a gain or magnify a loss by sticking around too long. Mike McGrath, Director, Trader Products at TD AMERITRADE, gives these exit-strategy tips.

### 1 REVISIT YOUR ENTRANCE STRATEGY

"Is the reason you entered the position still there? It's possible that a number of factors could have changed that make it time to exit," notes McGrath. "Your price target may have already been met, or new information may have been uncovered that changes your outlook."

### 2 REMEMBER YOUR RISK TOLERANCE

"How strong is your stomach?" McGrath asks. "Investors often amplify losses by hoping for a rebound in a stock that has depreciated. Identifying an exit point up front and then sticking to it can prevent bad investments and allow you to move on to potentially better ones."

### 3 CONSIDER THE FUNDAMENTALS

Stock price moves are often prompted by changes in the underlying economics of a business or industry or by a corporate announcement. "If a company's about to report earnings, you may want to consider such events when planning an exit," McGrath says.



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### 4 EMPLOY ANALYTICAL TOOLS

Using technical analysis to detect price patterns and market trends can help you identify exit points. Charts, for example, can show support and resistance levels in a stock price. McGrath suggests using multiple indicators to help confirm your outlook.

### 5 USE ADVANCED ORDERS

"Conditional Orders and Trailing Stops may help you stay disciplined," McGrath says. "Trailing Stops can let potential winners run and protect from pullbacks. Using Conditional Orders to help bracket a position will help you identify upside and downside exit points." — JP

*Market volatility, volume and system availability may delay account access and trade executions. Results presented are hypothetical; they did not actually occur, and they may not take into consideration all transaction fees or taxes you would incur in an actual transaction. Past performance of a security does not guarantee future results or success. Sufficient funds or positions are required when Trade Triggers orders activate. A Trailing Stop or stop loss order will not guarantee an execution at or near the activation price. Once activated, they compete with other incoming market orders.*

## Holding Steady

Small adjustments, not big changes, can help keep you moving toward your goals

**T**his year's markets have been rough. Global equity markets delivered negative year-to-date returns into the second quarter. Volatility has put the major indices through record point and percentage swings. And fixed-income yields set record lows before returning to normal as the Federal Reserve slowed the pace of rate cuts. Many investors may wonder if they need an all-cash portfolio.

No, counsels Stephanie Giroux, Chief Investment Strategist for TD AMERITRADE, who sees potential for continued long-term growth in overseas stocks and commodities, along with attractive yields in high-quality corporate bonds and Treasury Inflation-Protected Securities (TIPS). She advises anchoring your portfolio with strategic diversification and fine-tuning with adjustments that seize today's opportunities. (For more of Giroux's thoughts, visit "The Weekly Compass" by logging on to your account and clicking PLANNING & RETIREMENT, then "Investment Approach.")



DAVID RADLER

Stephanie Giroux is TD AMERITRADE's Chief Investment Strategist.

**Q. Is the subprime mortgage crisis akin to the technology stock bubble burst?**

**A.** This is a much bigger deal, more like the savings and loan crisis of the late 1980s and early 1990s, when many thrifts went under. The tech bubble was confined to a specific market sector, in which valuations had ballooned because of Y2K worries and the anticipation of enormous

“Some people expect a V-shaped stock market recovery. We expect a U-shaped recovery, with a protracted, bumpy bottom.”

Internet tech spending. But the subprime crisis affects the daily lives of more people. Homes are people's primary assets, and consumer balance sheets now show more debt than in the past. We've stabilized the financial system from loan losses and write-downs, but we haven't fixed the heart of the problem, which is that consumers are overextended and their primary assets have lost significant value.

### Q. When do you think the stock market will recover?

**A.** Some people are expecting a V-shaped recovery to occur during the third and fourth quarters, with the market shooting back up as quickly as it fell, but that's based on what I think are overly optimistic earnings expectations for the rest of the year. Even though valuations may look low, they're not low enough if you factor in slow-growing corporate profits. We expect a U-shaped recovery, with a protracted, bumpy bottom. You probably won't see a big pickup in earnings growth until 2009, at which point inflation may be a problem.

### Q. How should investors respond to that scenario?

**A.** Investors may want to consider holding more cash than usual — up to 10% of a portfolio — so they are ready to take advantage of potential opportunities. Short-term Treasuries are overbought, with high prices and low yields, but high-quality, longer-term corporate bonds might be an opportunity. We're watching low-quality,

high-yield bonds, but it may still be too early since their default rates haven't yet approached the levels often seen in a recession. We also like TIPS, which move up with inflation.

### Q. Commodities have outperformed, but they are volatile. How can investors protect against risk?

**A.** Commodities represent one of the few asset classes that have been strong in the first half. And because commodities don't have a high correlation to equities or fixed income, they're a natural portfolio diversifier. To limit risk, you could invest in a broad basket of hard commodities (mined, not grown), such as metals and oil, and soft commodities (grown, not mined), such as cotton, sugar and corn. You could also manage risk by limiting commodities exposure to about 5% of your portfolio.

### Q. Are Exchange Traded Funds (ETFs) becoming too specialized and risky?

**A.** The proliferation of ETFs has sliced the market in ways that could hurt investors who don't do their homework. But ETFs have also opened up parts of the market to individual investors who didn't have access to them before. There may be less risk in buying an ETF that holds many municipalities' bonds than in buying a single bond from one municipality. Ultimately ETFs can be used alongside or in place of actively managed mutual funds for portfolio diversification. ■

*Carefully consider the investment objectives, risks, charges and expenses of any investment company before investing. To obtain a prospectus containing this and other important information, please visit [www.tdameritrade.com](http://www.tdameritrade.com) or call a TD AMERITRADE representative at 800-669-3900. Please read the prospectus carefully before investing. Diversification does not eliminate the risk of experiencing investment losses. Past performance of a security or strategy does not guarantee future results or success.*

