How to Get a 13.5% Yield From Bombardier, Inc.

Description

The downfall of **Bombardier, Inc.** (TSX:BBD.B) has been well documented.

The big issue is the CSeries line of regional jets. Bombardier bet big that the new line of planes would disrupt a market that's now dominated by Airbus and **Boeing**. While the incumbents have momentum on their side–after all, most airlines fly either Airbus or Boeing models–Bombardier's CSeries offers some pretty compelling pluses too, like terrific fuel efficiency and significantly quieter engines.

The issue isn't with the planes themselves. Generally, observers say the CSeries models are good planes that should sell well once potential customers can see them in action. Pre-orders have been brisk as well, at least they were up to about a year ago.

The problem is with delays. The delivery date for the CSeries program has already been pushed back three times. Originally slated to go into service in late 2013, the program is now predicted to begin delivering jets to customers sometime in the first half of 2016. A two-and-a-half-year delay is inexcusable.

Delays cost money, especially when you're developing a new plane. Bombardier has burned through billions in capital expenditures, forcing it to stretch its balance sheet to the limit. The company currently owes more than $9.3 billion if you include the preferred shares. That compares to a mere $1.4 billion worth of equity on the balance sheet.

Most investors would run far away from a balance sheet like that. There's little doubt that Bombardier shares are a risky investment at this point, and same with the debt. Bankruptcy is very much on the table.

But on the other hand, shares could go much higher if the company can right the ship and make it through this downturn. And even though the company cut its dividend to zero months ago, there's a way investors can get paid to wait and participate in a potential Bombardier recovery.

Enter the preferred shares

Preferred shares are sort of a hybrid between common shares and bonds. They pay out fixed dividends like bonds, but tend to be more volatile than the actual bonds, moving in sympathy with both interest rates and the overall health of the underlying company.

Bombardier's preferred shares have plummeted in value along with the common shares. This means they have some tantalizing yields.

Take the series 4 preferred shares, which trade under the ticker symbol BBD.PR.C. These shares pay an eye-popping dividend of 13.5%, a yield that just doesn't happen much anymore.

I don't want to downplay the risk of these preferred shares, just in case a 13.5% yield doesn't already provide adequate warning. If the company goes bankrupt, these shares will likely be worth nothing. And there's a real chance of bankruptcy happening.

But if the company survives and starts making money off the CSeries, not only will the yield be more secure, but the value of the preferred shares themselves would likely go up. This means an investor who buys now would be looking at gains from both dividends and capital gains.

These shares have already delivered capital gains for some investors. In August, they dipped below $8 per share before rallying to more than $13 each just a month later. They're currently just over $11.50 each.

There's one other risk, and that's the potential conversion. The company has the right to convert the preferred shares into common shares at any time, which would save it approximately $13 million each year in dividend payments. That's not a lot for a company like Bombardier, but at this point, saving that much money would make a difference.

Bombardier's preferred shares are risky, there's no doubt about it. But they also offer huge potential upside if the company can right the ship. If you're a believer in the turnaround story and like dividends, getting paid 13.5% to wait is something that looks pretty attractive.

CATEGORY

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2. Investing

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1. TSX:BBD.B (Bombardier)

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