Income Investors: Collect a 9.4% Yield From BlackBerry Ltd.

Description

In many ways, **BlackBerry Ltd.** (TSX:BB)(NASDAQ:BBRY) is a terrific turnaround stock.

The company was smart to have hired John Chen to head the transformation. Chen previously had success turning Sybase from a mature technology company into one that was widely considered an innovator. The company grew from a sub-$500 million market cap when Chen took over to $5.8 billion in size when it was acquired by SAP in 2010.

BlackBerry is also quickly diversifying into software, leaving its traditional hardware business in the dust. Software has good margins, nice growth prospects, and allows the company to dominate niche markets. The company has spent some US$1 billion in software acquisitions recently, and more takeovers in the space are a real possibility.

The company has the balance sheet strength to fund further forays into the software space. As of February 29, BlackBerry had US$2.4 billion in cash on hand. The company was also free cash flow positive in its last year, earning US$155 million. If you take out the losses from the hardware division, free cash flow would be even higher.

In fact, many analysts and pundits agree that BlackBerry will get out of the hardware business sooner rather than later. Chen himself has stated that if hardware isn't profitable by September, the company will at least look at getting out of the business. This would free it up to sue competitors that are infringing on its patents without fear of counter-lawsuits.

There's only one real thing BlackBerry has against it that turnaround investors look for, and that's no dividend. Turnarounds often take years–sometimes even longer–to get back to previous success. Getting paid to wait makes it much easier for an investor to be patient.

Although BlackBerry doesn't pay a dividend, it isn't that hard for investors in the company to create their own dividend using a covered-call strategy.

How does it work?

Calls are options used by speculators to place aggressive bets on companies. Call options are used by bullish investors, while put options are used by bearish investors.

Here’s how they work. An investor who’s bullish on BlackBerry would buy cheap calls that enable them to book big gains on a relatively small movements in the share price. Most of these options expire worthless because stocks just don’t move that much in small periods of time.

Long-term investors can use these options to their benefit. By taking the opposite side of that bet, an investor can use calls to generate a pretty steady stream of income.

BlackBerry shares currently trade for $8.94 each on the TSX. A holder of these shares can sell BlackBerry calls today, generating income in exchange for locking in a sale price at a higher level on a certain date.

Right now, BlackBerry investors can receive $0.07 per share in exchange for agreeing to sell at $10 per share on June 17. If shares close below $10 on that date, the investor is free to keep the $0.07 per share. If shares close above $10, the investor is forced to sell at that price, locking in a profit of more than $1 per share.

That’s not bad for holding for just a month.

And remember, BlackBerry has monthly options. This means an investor could use a covered-call strategy 12 times per year, generating some pretty serious income in the process. Assuming the same option persists all year, it would be enough to generate a yield of 9.4% annually. That’s very attractive compared to other dividends in today’s market.

This strategy isn’t perfect. It does limit your upside in the event BlackBerry shares really pop. It also requires more portfolio management than a buy-and-hold approach. But for many investors, the potential upside is too enticing to let a couple of drawbacks hold them back.

CATEGORY

1. Investing
2. Tech Stocks

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1. Editor's Choice

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