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Dividend Ideas

Tax Loss Selling Opportunities Among Preferreds And Bonds

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Alpha Gen Capital
Marketplace Bio

Summary

- Tax loss selling and a small pullback in the preferreds market have opened up a number of buying opportunities.
- We provide a quick rundown on 13 preferreds and bonds that are currently buyable as of the close on 11/20.
- Several have ex-dividend dates coming up in the next few weeks.
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(This report was first published to members of Yield Hunting on November 20th.)

With tax loss selling season winding down, a number of opportunities have opened up among preferreds and bonds. This article will provide a quick rundown of the following securities which are all buyable as of the close on Friday 11/20 (some more so than others). Securities are presented in order of least credit risk to most credit risk. Asterisk (*) indicates low interest rate risk. Number sign (#) indicates currently callable, so be careful not to pay more than par+accrued.

- 4.75% OPP-B
- 4.75% EP-C *#
- 5% BIPH (no K1) / 5% BIP-B (K1)
- 8% SPNT-B * (yield ~4.9%)
- 6.25% QVCC

- 5.35% PSEC-A (yield 6.1%)
- 6.25% BPYPM (K1)
- 6.5% ECCC*
- 7.8% RLJ-A (yield 6.9%, uncallable)
- 6.7% PBI-B #
- Libor+6.73% NSS *#
- 8.25% 2025 Callon Petroleum par $1000 bond *
- 8.25% FTAI-C (2021 K1 / 2022 1099) *

4.75% OPP-B/OPPBP

This is a new preferred issued by the CEF OPP. It carries an A1 rating which makes it safer than any other non-CEF preferred in the market. With borderline investment grade (BBB-) preferreds being issued at 4.25% these days, the 4.75% from OPP-B is a good relative value. It may be still trading under the temporary ticker OPPBP on the grey market which is not accessible at all brokers but will soon transition to a major exchange (NYSE or NASDAQ) where it will be listed under its permanent ticker.

Further details are in my past article on the A series here.

2028 4.75% EP-C

Price: $50.33 I Ex-div: $0.59 on 12/14 I Par: $50

Maturity: 3/31/2028 I Rating: Baa3/BB+

Tax: 1099 Ordinary Income

From Chat on 8/12/2021:

> I just bought some of the El Paso 4.75% jr. sub bonds due 3/2028 at 50.10. El Paso became part of Kinder Morgan (ticker: KMI - $39B market cap) in a 2014 consolidation transaction of multiple KM entities. EP-C remains an obligation of the El Paso Natural Gas Company which is a wholly-owned sub of KMI. Technically, EP-C holders have no recourse to KMI parent, so EPNG is actually the entity backing these bonds. However, it doesn't really make a difference as EPNG has its own separate bond rating which is the same as KMI's bond rating. El Paso's bonds trade at similar yields as KMI's. Bond market doesn't seem to be making a distinction between these companies.

> EP-C is currently callable at 50+accrued. The notes are rated BB+/Baa3. KMI sr. unsecured rating is BBB/Baa2 and as a benchmark, their 2031 note yields 2.7%. So, you get 200+ bps of extra yield in return for going down one step in rank. Interest payments on the bonds are deferrable for up to five years but they would have to eliminate the common div first. KMI / El Paso is a C-corp energy midstream. The biggest appeal here isn't so much the 4.75% yield as the 2028 maturity which insulates you from both rate and credit risk.

5% BIPH (no K1)/5% BIP-B (K1)

Rating: BBB- I Ex-div: 12/15 (OTCPK:BIPH), 11/29 (BIP-B)

These are both equally ranked securities from Brookfield Infrastructure ($23B market cap) with the same BBB- investment-grade rating. BIPH does not have a K1 but may have 15% Canadian tax withholding (which is recoverable by filing for a tax credit). BIP-B has no withholding as a Bermuda-based partnership but comes with a K-1.

Brookfield Infrastructure is one of the largest owners and operators of critical global infrastructure networks which facilitate the movement and storage of energy, water, freight, passengers and data. They are one of the few pure play, publicly traded, global infrastructure vehicles that invests in premier infrastructure assets with stable cash flows, high margins and strong growth prospects.

8% SPNT-B Fixed-Reset

YTC: ~4.9% I Call: 2/26/2026 I Reset: 5 Year Treasury + 7.3%

Tax: Qualified

This is a BB+ rated preferred from a $1.4B market cap insurance company. It has a 8% coupon that resets to 5 YR Treasury + 7.3% if not called. It's basically guaranteed to be called in five years, so think of it as a BB+ rated bond with a YTC a tad under 5%. With the average BB rated bond yielding 3.45%, this is a good relative value.

It is a special situation preferred that was issued as part of a corporate reorganization. Dan Loeb's Third Point fund is invested in the company. The initial IPO offering price was $27.47.

6.25% QVCC

Call: 11/26/2024 I YTC: 5.5% I Ex-div: 11/30

Rating: BB+/Ba2/BBB- (S&P/Moody's/Fitch)

This is a Sr. Secured note from the owners of the QVC channel. QVC is a wholly-owned subsidiary of $3.4B market cap Qurate (QRTEA). While I don't expect QVCC to be called soon after it is callable in three years, even if it was, it would provide a respectable 5.5% YTC for a near-IG issue.

Further details are available at my past article here.

5.35% PSEC-A

Price: 22.06 | Yield: 6.1% | Rating: BB/Ba2

Tax: Ordinary Income

PSEC is a $3.5B market cap BDC. PSEC-A came to market this year and was initially overpriced. As a result, it quickly traded below par and tax loss selling has brutalized the price to oversold levels that now represent a solid value.

While the BB rating is appealing for this yield, the bond market is discounting PSEC's rating, so you should too. Instead of just going by the rating, the best way to value PSEC-A is by benchmarking off their bonds which are rated BBB-/Baa3. PSEC's mid-term (late 2020s) sr. unsecured bonds yield around 3.8%. With the average Baa2 bond yielding 3.3%, we can see the market is discounting the bonds. However, the preferreds yield 230 bps more than the bonds which means they are a solid value in relation to the bonds. For an investment-grade issuer, 150 bps over the bonds would be fair value and 200 bps is attractive.

Coverage on the preferreds is very strong with $3.5B of common stock covering $400M of preferreds for a coverage ratio of 8.75x.

While PSEC-A isn't investment grade, it's still a pretty solid credit due to the 150% asset coverage requirement and a portfolio that's primarily composed of senior (first lien) debt. One way to look at PSEC-A is that if PSEC had a 200% asset coverage requirement (like a CEF) instead of a 150% coverage requirement (like all BDCs), it would likely have a strong investment-grade rating similar to OPP-B.

6.25% BPYPM (K1)

Credit Rating: BB | Call: 2026

BPY is similar to a REIT (technically a partnership) that is mainly comprised of Class A office properties (mainly North American but also global) and Class A malls (obtained when they acquired GGP). BPYPM was issued when BPY was acquired by parent Brookfield Asset Management (BAM). BPY common stock is no longer listed making this an "orphaned" preferred but financial info can still be deduced from BAM filings.

BAM's CEO Bruce Flatt is a legendary investor who's known as the Warren Buffett of Canada. Mr. Flatt took BPY private because he thought the market was undervaluing the assets and he strongly believes in their long-term prospects.

BPYPM is a good value compared to most other BB-rated preferreds or preferreds from quality REITs. The K-1 and "orphaned" status may account for some of the discount.

6.5% 2031 ECCC

Call: 6/16/2024

ECCC is a term preferred issued by the CLO CEF ECC. Unlike preferreds from other types of CEFs, CLO CEF preferreds are not rock solid investment grade due to the high risk of CLOs. Nonetheless, the 200% asset coverage requirement for the preferreds provides a good measure of safety and the 2031 maturity date provides some protection from rate risk.

ECCC can be compared to preferreds from OXLC, PRIF, and OCCI. At this time, ECCC is the best buy due to its higher YTW. OXLC preferreds could be considered safer due to a somewhat stronger balance sheet but that is counter-balanced by ECC's superior management track record. PRIF preferreds should be discounted for not having a publicly listed common stock and OCCI lacks scale and diversification. I own preferreds from ECC, OXLC, and PRIF as they're all good at the right price.

7.8% RLJ-A

Call: Uncallable (Broken Convertible)

Price: 28.20 | Yield: 6.9%

RLJ is a $2.3B market cap hotel REIT. The preferred is uncallable since it is a convertible but the conversion price is so high that it is unlikely to ever be reached.

RLJ is not in the top tier of hotel REITs but in the next tier similar to PEB and INN which also have preferreds. Preferreds from those companies yield less and have worse coverage, making RLJ a good relative value. The common stock covers the preferreds by a very solid 7x.

6.7% 2043 Sr. Note PBI-B

Rating: BB/B1 l Call: Callable - avoid buying above par+accrued

PBI-B is a sr. note from $1.3B market cap shipping logistics company Pitney Bowes. PBI is undergoing a transformation from its traditional postal mail business to an e-commerce shipping logistics company. This transformation has stemmed the years-long decline in its share price. The share price started an upward trend over the past 18 months.

PBI-B is a solid relative value in comparison to the company's par $1000 bonds and relative to other BB/B1 rated preferreds.

Further details are available at my past article here.

Floating Rate 2043 Jr. Sub Note NSS

Rating: B/B2 l Call: Callable l Ex-div: 12/30 ($0.438)

Yield: 7% l Tax: 1099 Ordinary Income

NSS is a jr. subordinated note from $1.7B midstream MLP NuStar (NS). NS has made substantial progress in strengthening their balance sheet and is on track to end the year at less than 4x sr. debt/EBITDA.

NSS is a good relative value in comparison with NS's par $1000 sr. notes and in comparison with NS's preferreds. While the preferreds have higher yields than NSS, they have far less coverage and are thus much riskier. NSS is covered by a combination of common and preferred stock by 7.5x. While interest payments on NSS can be deferred for up to five years, they can only be deferred if dividends on the common and preferred shares are suspended first.

Further details are available at my past article here.

8.25% 2025 Callon Petroleum (CPE) par $1000 Sr. Note

CUSIP: 144577AJ2

CPE is a $3B market cap oil E&P based in the Permian. They were recently upgraded by S&P to B and Fitch initiated coverage at B. The average B rated bond yields 4.5% so this is a good relative value. The Moody's rating of Caa2 is lagging the improvement in fundamentals. Stock price is performing well, up 560% over the past year.

The bond may be listed as Carrizo which is a company CPE acquired. However, these are actually CPE bonds and the ratings agencies have confirmed that. It's possible these bonds are slipping under people's radar due to the old name.

CARRIZO OIL & GAS INC

+ ADD TO WATCHLIST

Coupon Rate	Maturity Date
8.250%	07/15/2025

Symbol	CUSIP	Next Call Date	Callable
CPE4514613	144577AJ2	07/15/2022	Yes

Last Trade Price	Last Trade Yield	Last Trade Date	US Treasury Yield
$99.31	8.469%	11/19/2021	—

Trade History

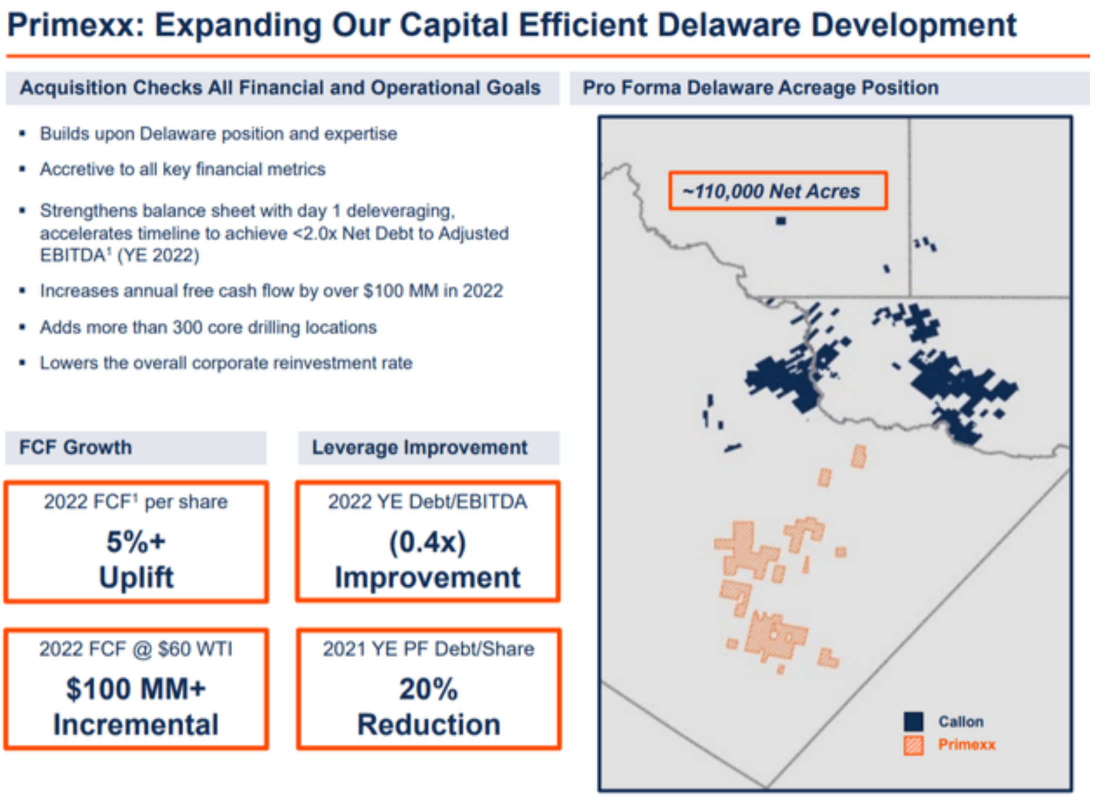
(Source: Fidelity)

The 2025 bond is a good relative value compared to CPE's other bonds which have lower yields. The 2024 bond yields 6.4%, 2026 yields 7% and 2028 yields 7.3%.

☐	CALLON PETE CO DEL	CPE4492238	Yes	Corporate Bond	6.125	10/01/2024	Caa2	B	99.197	6.433
☐	CALLON PETE CO DEL	CPE4640205	Yes	Corporate Bond	6.375	07/01/2026	Caa2	B	97.467	7.026
☐	CALLON PETE CO DEL	CPE5207438	Yes	Corporate Bond	8.000	08/01/2028		B	102.750	7.291

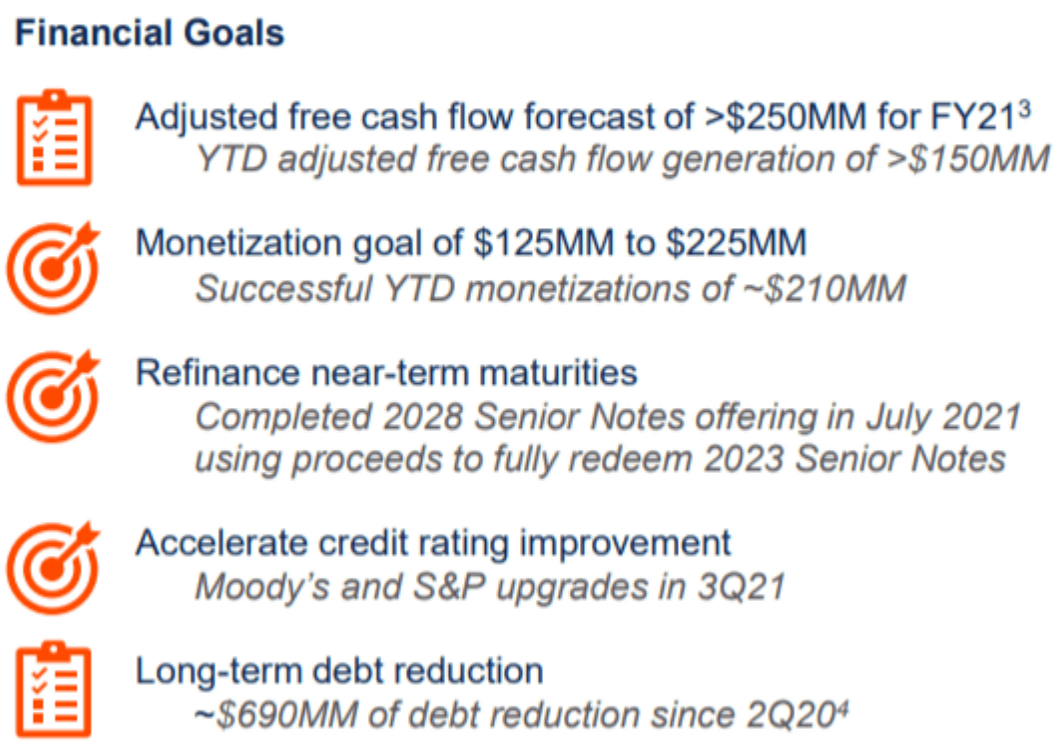
(Source: Fidelity)

CPE recently acquired the company Primexx. The transaction was credit positive and the likely catalyst for the ratings upgrade. CPE now has 110,000 acres in the Permian.



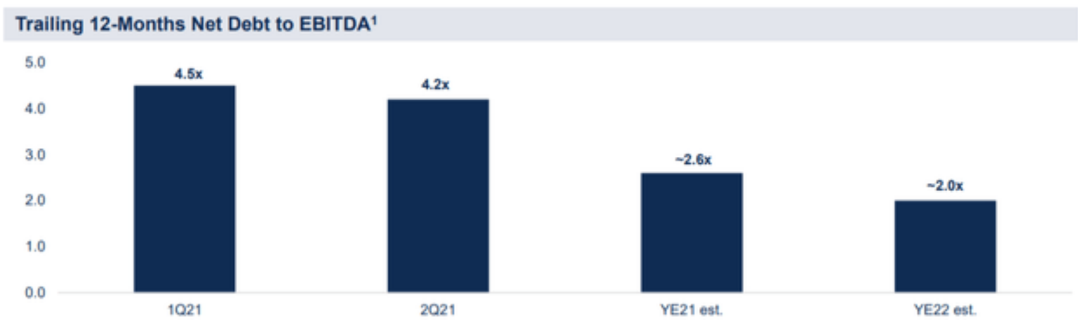
(Source: Primexx)

CPE has its sights set on improving their credit worthiness and has been accomplishing their goals. FCF is healthy, they've refinanced near-term maturities and reduced long-term debt. This has resulted in credit ratings upgrades.



(Source: Primexx)

CPE has made significant progress on reducing leverage and plans to improve debt/EBITDA further.



(Source: Primexx)

Fitch's B rating assumes fairly low 2022 oil prices. If oil prices significantly exceed these levels, that could be another catalyst for a ratings upgrade:

KEY ASSUMPTIONS

--WTI oil price of $60/bbl for the remainder of 2021, $52/bbl in 2022 and $50/bbl thereafter

--Henry Hub natural gas price of $3.40/mcf in 2021, $2.75/mcf in 2022 and $2.45/mcf thereafter

Fitch Assigns Callon Petroleum Co. First-Time 'B' IDR; Outlook Stable

8.25% FTAI-C Fixed-Reset (K1 2021)

Price: 25.97 l Call: 6/15/2026 l Ex-div: 11/30

Reset: 5 Year Treasury + 7.38%

This is a fixed-reset from a $2.5B infrastructure company managed by Fortress ($50B AUM). If not called when callable, the coupon will reset to the 5 Year Treasury rate + 7.38% and then reset every five years thereafter. Therefore, there is little interest rate risk.

The company is in the process of a two-part reorganization:

- Convert from an LP to a C-corp in Q1 2022, which will