Taking Stock: Capital One punishment

by Malcolm_Berko

Dear Mr. Berko: I have an account at a major brokerage firm whose research department recommended that I buy 200 shares of Capital One Financial, the big credit card issuer, in February of 2007 at $81. The stock is now $47.78. Now my broker wants me to sell my Pfizer, which you recommended in August of last year at $24 and is at $22.50. Please tell me what's wrong with Capital One and give me your "buy, sell, hold" advice. Also tell me why they keep raising the interest rate on my credit card balance when the Federal Reserve is lowering interest rates. That's like kicking a defenseless man who can't protect himself. It's criminal, too. And that Pfizer just sits there and doesn't do a thing. So please give me your "buy, sell, hold" advice on Pfizer too. By the way, my broker says he knows you.

W.D.

Springfield, Ill.

Dear W.D.: I know your broker and met him in a Chicago golf tournament several years ago. He's a real nice guy, has a very pleasant sense of humor, he's quite a good golfer, adores his wife and kids, is active in his church, but ain't too bright. He really believes that Nostradamus was a professional football player.

Capital One Financial Corp. (COF-$47.78) may be the largest issuer of credit cards (MasterCard and Visa) in the world. And with its recent $700 million purchase of NetSpend (markets prepaid debit cards) COF intends to become a significant participant in this market, which they believe will grow by 30 percent a year.

In February of 2007, Merrill, Sanford Bernstein, Citigroup, Lehman Brothers and host of other New York Stock Exchange buffoons were touting COF with the enthusiasm of carnival barkers. COF was trading in the low $80s and these Big Board boys (some of whom lost billions in the subprime mess) were telling us that COF was on track to earn $7 or more a share last year. I wouldn't trust a brokerage firm whose analysts lost billions of their firm's money in the subprime market and I wouldn't trust a brokerage that loudly recommended COF in the low $80s and that held its tongue when COF was trading at $70 or $60 or $50.

COF's earnings for 2007 should come between $3.75 and $4.10 a share, not the $7 your brokerage suggested last year. The reason is simple as a circle but serious as a heart attack. The collapse of the housing market and its myriad ancillary suppliers (carpets, plumbing, appliances, trucking, packaging, roofing and other industries mentioned in one of my March columns) has created rising unemployment. So with higher oil prices chewing their paychecks, it's difficult for consumers to pay their bills.

With record consumer debt of almost $13.5 trillion (more than doubled since 2002) increasing faster than consumer income there just isn't enough money at the end of the month for us to pay Mr. MasterCard and Mr. Visa. Even the venerable American Express took a fourth-quarter charge of $275 million to cover rising customer defaults and their earnings have tumbled, too. So it looks like it will get "worser and worser" over the coming months.

The consumer is between a rock and a hot plate. While the Federal Reserve may continue to lower interest rates, I'd wager dimes to dollars that MasterCard and Visa won't lower your rates; rather, they will raise them again. They will do it because they can and because they think of their cardholders as squirming, impotent, voiceless, insignificant bacteria in a colony of microorganisms. And there's nothing you can do about it because it's true.

What we need is a National Credit Card Association, funded by card holders ($1 a year per card would do it), that has "dollar power" to lobby Congress like the National Rifle Association and influence corporate decisions like the National Association for the Advancement of Colored People.

I believe the price of COF (which should be sold) could be 15 percent lower by September and I believe American Express Co. (AXP-$46), which is down from $66, will continue lower, too. But don't sell your Pfizer (PFE-$22.50). This issue has been at the end of the conga line for the last few years and I'm 87 percent convinced it bottomed out last year at $22.24. During the last few years, PFE has been as exciting to watch, like waiting for iron to rust or wine age. Earnings have been flat as old beer and its drug portfolio was similarly uninspiring but I think that's changed.

PFE's 2008 earnings should improve by at least 10 percent; the company has increased its dividend for 28 consecutive years and at a $1.28, that's a swell 5.65 percent return taxed at 15 percent. And I'd use the proceeds from the sale of COF to purchase more PFE.

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