

How To Turn Apple, (AAPL), Into An Income Stock

Devotees of dividend paying stocks may find it strange to hear Apple's name mentioned in an article about income stocks, but there is a straightforward, conservative way to earn income quickly from this well-run tech stock.

Even though AAPL doesn't pay a dividend, income investors could earn just below 11% by selling put options on it. (See below for details).

Apple looks good in many metrics when compared to the Computer Hardware industry:

	Apple	Computer Hardware Industry
ROE	31.90	27.61
ROA	28.96	22.07
ROI	19.35	13.66
Income/Employee	\$1.36 mln	\$.96 mln
Profit Margin	20.04%	13.47%
Debt/Equity	NO DEBT	20.10%

However, it does command a valuation premium to its peers:

	Apple	Computer Hardware Industry
P/E	19.56	18.13
Price/Book	5.08	4.29
Price/Cash Flow/Share	17.99	14.65

But AAPL doesn't seem so pricy when you compare its earnings to its closest peer in the Personal Computer Industry: **Dell**.

	Apple	Dell
PEG	1.05	1.98
Price/Book	5.11	5.26
EPS This Year	Up 33.86%	Down 4.86%
EPS Past 5 Years	Up 92.52%	Up 4.32%
Sales Past 5 Years	Up 38.97%	Up 8.07%
Projected EPS Next 5 Years	Up 18.69%	Up 9.21%

With a PEG at 1.05, just above the generally accepted cutoff of 1.00 for fair-valued stocks, it would be very tempting to chase Apple right now. But by selling put options, you could lower your potential entry point, thereby lowering the P/E and PEG. More importantly, you could generate income now, instead of buying and waiting for appreciation.

AAPL's Jan. 2011 \$190.00 puts closed at a bid of \$20.85 Friday, which is a 10.97% yield, close to 12% annualized. (Based on 100% cash reserve). Granted, in the world of growth stocks, an approx. 11% yield isn't very sexy, and AAPL's price performance this year could potentially be much more than 11%, but trading AAPL by selling this Jan. put does have its advantages:

1. Your breakeven is \$169.15, which is below AAPL's 200-day moving avg. of \$175.48.
2. Your breakeven is 16% below AAPL's current price of \$201.67
3. Virtually instant cash yield – (trade plus 3 days).
4. If you hold the put until expiration or assignment in Jan. 2011, you won't have to pay taxes on the put premium you received until April 15, 2012, when you report 2011 gains. Also, if you ultimately take assignment of the underlying shares, you're not liable for the taxes on the cash you received for the put premium until you eventually sell the stock. (When you sell, your cost basis is lowered to your breakeven of \$169.15 on this trade).
5. If AAPL does start to decline, since the \$190 long-term put has a Delta of approx. -.35, (the put will only rise \$.35 for every \$1.00 that AAPL rises), this gives the put seller a chance to "retreat" to a lower strike price if desirable, without taking as much of a hit as an outright stock purchase would.

This is just one of many puts available for AAPL, more conservative investors could lower their breakeven further by:

- A. Waiting for AAPL to decline from its present price, which would lift the put option premiums on lower strike prices, AND/OR
- B. Selling puts at a lower strike price.

Note: Unless you're approved for Option Level 3, most brokers will require a 100% cash reserve up front, which equals the value of the underlying shares that could potentially be put to you. In this case, 100% cash reserve for selling 1 \$190.00 put equals \$19,000.00.

Disclosure: Author is short AAPL puts

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