



The Next Million-Dollar Penny Stock

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Tim Beyers

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Penny stocks can [make you rich](#).

Need proof? Every one of these multi-baggers was, at one time, a penny stock:

Company	Recent Price	CAPS Stars (out of 5)	5-Year Return
Southwestern Energy (NYSE: SWN)	\$32.45	***	1,252.1%
Arena Resources (NYSE: ARD)	\$23.50	***	691.2%
Ebix (Nasdaq: EBIX)	\$24.72	****	584.8%
EZCORP (Nasdaq: EZPW)	\$14.55	****	546.7%
Sun Hydraulics (Nasdaq: SNHY)	\$14.04	*****	295.5%

Sources: Motley Fool CAPS, Yahoo! Finance.

The promise of outrageous returns is why some of the world's best stock pickers are, at times, penny stock investors. Peter Lynch [has enjoyed](#) the stock market's super-cheap seats, and at times he still does. The **Royce Low-Priced Stock** fund [crushes the market](#) by betting on stocks trading near or below \$10 a share, such as **Cryptologic** (Nasdaq: [CRYP](#)).

Even the All-Stars in our 120,000-plus [Motley Fool CAPS](#) community take to penny stocks. More than a few have been [richly rewarded](#).

Pennies from heaven

So why *not* invest in penny stocks? I suppose because the SEC has warned us about them. But what if we take the agency's definition literally and limit our choices to stocks trading between \$1.50 and \$5 a share? And what if we further limit our choices to four- and five-star stocks whose market cap doesn't exceed \$2 billion, but is at least \$250 million? Surely our new [CAPS screener](#) would return some winners, right?

This week, 69 stocks made the cut -- including [our last topper](#), **Gushan Environmental**. Let's move on to **CapitalSource** (NYSE: [CSE](#)), which has a strong following in our CAPS community:

Metric	CapitalSource
CAPS stars (out of 5)	*****
Total ratings	1,717

Bullish ratings	1,650
Percent bulls	97.3%
Bearish ratings	67
Percent bears	2.7%
Bullish pitches	263
Bearish pitches	17

Data current as of Nov. 18, 2008.

As CAPS investor [ValueArbitrage](#) wrote in September:

Unlike so many commercial or investment banks today, CapitalSource is a bank with ultra low leverage and an outstanding team of managers who are focused on credit quality analytics for credit decisions, full use of collateral, and conservative lending practices (no 40x leverage and volume at any cost production processes here). Additionally, this company is currently going through a significant transformation, positioning itself to be both stronger and more profitable in the future.

Our Fool is referring to a shift in CapitalSource's business model. No longer will it be a REIT but a commercial bank. The FDIC has already approved its application, which leaves just the Federal Reserve standing in the way of its transformation. Most investors appear to believe that the Fed will step aside soon enough.

Once they do, CapitalSource will take on commercial lending business that -- due to the credit crisis - has been vacated by others. A meaty and well-capitalized dividend, yielding 4.80% as of this writing, means that today's investors will be paid to wait for the higher profits that banking promises.

Years could pass before we see them, but it should happen eventually, argues [TMFHelical](#). His study of management shows a history of very successful spin-offs and restructurings. "So while I still tire of hearing about the loaning 'opportunities' available in the market, I do have some confidence that management can indeed exploit them," he recently posted at the discussion boards for our *Million Dollar Portfolio* service.

Agreed, but I'm more interested to know what you think. Would *you* buy shares of [CapitalSource](#) at today's prices? Let us know by [signing up](#) for CAPS today. It's 100% free to participate.

See you back here next week with another penny stock from heaven. Fool on!

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