Article Side

Preferred stock- a glance by Isol

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Preferred stock typically is issued for innovative investors or other institutional investors. Its name is derived from the â€œpreferencesâ€• relative to common stock, which is the basic equity security that is issued when a corporation is formed.

Preferred stock is an equity investment that carries some of the characteristics of debt securities (such as bonds). It consistently represents a safer investment than common stock. It is a form of capital stock that provides dividends and other privileges to its holders. It is a separate type of stock from common stock, and is therefore priced and traded separately from common stock. Anyone can purchase preferred stock and it can often be converted into common stock at a later stage.

Differences between common and preferred stocks

Preferred stock commonly carries a fixed dividend payment, whereas the common stockholders depend on the overall performance of the company. Preferred stock dividends are guaranteed and usually higher than the common stock.If you purchase preferred stock, when companies issue both voting and non-voting preferred stock, you may not always have voting rights when you have assorted common stock. Furthermore, preferred stock is less liquid than common stock and, because it does not count fully in the company's profits, the growth in value of preferred stock is generally less than that of common stock.

Types of preferred stock

There are a number of different classes of preferred stock that a company decides to issue, so you may well have to choose which type of preferred stock you wish to purchase.

â€¢ Cumulative preferred stock: Under the cumulative stock, if the company fails to pay its dividend to preferred shareholders, it must make up the dividend before any dividends can be paid to common shareholders.

â€¢ Convertible preferred stock: The convertible preferred stock provides preferred shareholders with the option of converting preferred stock to common stock.

â€¢ Participating preferred stock: Participating stock enables preferred share holders to participate in the dividends to common shareholders, commonly at a pre-determined rate.

â€¢ Redeemable preferred stock: A preferred stock is said to be remediable or â€œimprovableâ€• in that t company that issues the shares reserves the right to redeem them at a pre-determined price and its own discretion.

Benefits of preferred stocks

One of the benefits of preferred stock is lower risk. In the triumph a company runs into trouble and is forced to liquidate, preferred stockholders are paid first after debts responsibility is met. Preferred stock is also less volatile than common stock but still offers the chance of equity growth. Dividends are fixed and must be paid fist before common stock dividends.

Some more benefits of preferred stock:-

1. Greater price stability:- Price and income stability are one of the most common characteristics of preferred stocks. This is based upon the higher asset class feature for this category. At the same time, there is a focus on ensuring that investors receive some kind of protection against vitality.

2. Greater liquidity:- A second benefit of preferred stocks is liquidity. Investors who do not have to keep their money tied up for long periods of time this is beneficial for them. These kinds of securities are dealing in the markets just like common stocks. This means that if an investor needs access to the cash right away, there will be no penalties associated with selling the stocks. Over the course of time, this is providing greater amounts of flexibility, by helping investors to adjust with changes that are taking place in the economy and their personal lives.

3. Comparatively low investment per share:- A third major advantage of preferred stocks is they are low priced securities. This means that investors do not have to pay over $100.00 per share to purchase these areas. Instead, they are trading below $50.00 (which increases the total amounts of leverage). This makes it easier to hold larger portions of this asset class (increasing the dividend yield for the portfolio).

4. Higher Rates of Interest:- Preferred shares typically offer superior rates than guaranteed instruments such as CDs, fixed annuities, and treasury securities. Over the past few decades, preferred offerings as an asset class have commonly paid dividends in the 7% to 10% range.

5. Preferential Dividend Payout:-Preferred shareholders usually receive their dividends before anything is paid to common shareholders.

There are a number of distinct benefits concords with preferred stock. The three most common advantages include price stability / income liquidity and low prices per share. The combination of these elements, are helping to make these areas more attractive to consonant investors. They are looking for higher returns without increasing the risks. In the future, these benefits will continue to appeal to wide range of investors (who are becoming more conservative about how they are planning for their future).

Conclusion

If you have complete knowledge of preferred stock and have been diligent with your fundamental analysis, there is nothing wrong with owning preferred stocks; however, many investors suggest that there are better investments that deserve your analysis time. There are too many other options, including high quality bonds, high-paying money market accounts, common stocks, options and futures that are far less complicated and provide more potential benefits than preferred stocks. Many investors expect preferential treatment from preferred stocks and no longer available and good, profitable investments can be found in other ways.

While they are not appropriate for everyone, preferred stocks can provide a competitive rate of return with less risk to investors who seek higher yields. Preferred stocks offer a combination of income and liquidity that cannot be matched in other instruments, and their dividends are often eligible for favorable tax treatment.

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