The best stocks for 2009

Here's the silver lining of the market meltdown: Equities are cheaper than they've been in years. We found ten prospects that should flourish.

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(Fortune Magazine) -- ***Where's the bottom?*** It's the question every investor is asking. We wish we could tell you when the stock market will reach that point - we really do. But we have no idea. Nobody does. This much, however, we can say: Don't wait for that perfect moment when the markets sink to their absolute floor. Because by the time you're certain prices have reached that spot, the moment will have passed, and you may have missed a dramatic rebound.

Since World War II, the Standard & Poor's 500 index has soared 32% on average during the nine months following a bear market. But here's the tricky part: Those gains often occur in sporadic, dramatic bursts. Which means that if you're abstaining from investing, there's a good chance you'll miss the biggest gains. In most cases, it's better to buy a bit early - and suffer some more paper losses - than to invest too late.

That's a long way of saying that as much as you may be inclined to pull your money out of the market, dust off the passbook you used as a child, and transfer your few remaining dollars into a savings account, now is not the time to sit out.

No doubt, we're mired in the grizzliest bear market in decades. But the good news is that stocks have been marked down to holiday-sale levels. The price/earnings ratio of the S&P 500 now stands at 11, or 50% below the index's ten-year average. The S&P's dividend yield is 3.4%, more than twice its ten-year average. There are now 62 S&P companies whose shares have P/E ratios below five and 52 with yields above 7%. One year ago those tallies would have been four and ten stocks, respectively. Says veteran mutual fund manager David Dreman: "This is the best buying opportunity since 1982."

Yes, risk still lurks, and you should remember the warnings to be found throughout this year's Investor's Guide - most important, that stocks may still sink significantly before they rise and that, especially for some, the recovery may not occur until after 2009. But there are so many quality companies with strong growth prospects and sterling balance sheets that it should be

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possible to make big returns without taking outlandish chances.

One smart and easy way to get back into equities if you fled the markets in 2008 is with a low-cost S&P 500 index fund like Vanguard 500 Index (VFINX). That will give you broad exposure to the market, letting you enjoy the eventual comeback while minimizing the impact of any single company. But if individual stocks are your thing, keep reading. We crunched the numbers, combed through the research reports, interviewed our favorite investing pros, and came up with ten stocks we think are poised for strong returns in 2009 and beyond.

Altria

Nobody has ever accused the folks at Altria (MO, Fortune 500) and its Philip Morris USA subsidiary of being dummies. (A few other things, sure, but not that.) So when Altria endorsed legislation that would subject tobacco products to FDA regulation - a bill sponsored in the U.S. Senate by longtime tobacco company foe Ted Kennedy - you knew there had to be a reason.

There is. Indeed, the proposed legislation might as well be dubbed the Altria Earnings Protection Act. For starters, the bill prevents the FDA from ever banning cigarettes. Just as important, the wording makes it extremely unlikely that the FDA will ever approve a new cigarette product, because the new entrant would have to be deemed "appropriate for the protection of the public health." The bill also restores states' ability to restrict tobacco advertising. Yet another part of the measure would require the FDA to crack down on sales of counterfeit cigarettes, which have been a drain on Altria earnings for some time. All of these provisions would be beneficial to Altria, as they would help it "lock in its already dominant market share," says Dan Clifton, a political analyst at Strategas Research Partners. (Altria currently controls about half the U.S. tobacco market.)

The upshot is this: If the bill becomes law - and there's reason to think it will, since President-elect Obama was a co-sponsor - Altria's already safe dividend (current yield: 8.5%) will become even safer. So, too, will its earnings growth, which analysts are pegging at 8% for 2009. Throw in the fact that vice stocks are usually recession stalwarts - they've outperformed the S&P by an average of 12 percentage points during the past six recessions, according to Merrill Lynch - and you've got a defensive stock with generous upside. "Given the current environment, both in terms of interest rates and overall uncertainty for almost every company in the market," Citigroup tobacco analyst Adam Spielman writes of Altria, "we think this is worth seizing."

Annaly Capital Management

No matter how superb its business or how cheap its valuation, a complicated stock - especially one that involves mortgages - can get hammered in a market like today's. Annaly (NLY) and its 16% dividend yield (that's not a misprint) is a prime example.

Annaly is a real estate investment trust, but it's not a conventional one. The company is basically a hedge fund that uses short-term bank loans to make long-term investments in mortgage-backed securities. That may sound scary, but Annaly buys only mortgages guaranteed by government-sponsored (now government-controlled) enterprises like Fannie Mae and Freddie Mac. Annaly does not acquire the toxic, unguaranteed stuff that's been laying waste to bank balance sheets.

CEO Michael Farrell says the biggest question for Annaly shareholders has always been whether the federal government would stand behind Fannie and Freddie's mortgage guarantees if the duo ran into trouble. "And now we know the answer," says Farrell, referring to the government's bailout of Fannie and Freddie in September.

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Better still, the margin improvement allowed Annaly to ratchet down its risk: Its leverage ratio (the ratio of borrowed money to shareholder equity) now stands at seven to one, down from ten to one a year ago. That's modest by Wall Street standards. Goldman Sachs's leverage ratio is currently 17 to one, for example, and Goldman takes risks with its money that Annaly wouldn't dream of taking.

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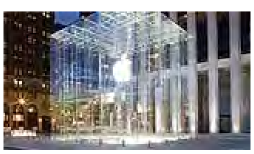

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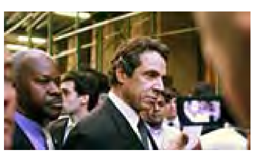

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