MSN Money Company Focus 2/4/2009 12:01 AM ET

5 promising stocks under $5

Solid, low-priced stocks are likely to rise faster, in percentage terms, when the market finally rebounds. But invest in them with caution.

By Michael Brush

Here's one big upside to the down market: There are dozens of solid, low-priced stocks on sale. That's good news because stocks going for less than the price of a Big Mac meal can be highly profitable. In a rebound they tend to move up a lot more than stocks with bigger price tags, in percentage terms.

There's reason for caution with under-$5 stocks, however. Companies with low share prices and tiny market capitalizations are speculative. So keep your position size small -- no more than 5% of your investment portfolio.

Enthusiasm for these small fry may not come back until investor confidence returns, so don't expect overnight gains. However, markets tend to price in changes in the economy about six months ahead of time. If the economy is going to rebound toward the end of this year, as some economists predict, these stocks could perk up within a few months.

That said, here are five promising names priced under $5:

A small play on a big food shortage

While **Caterpillar** (CAT, news, msgs) and other giants in agricultural equipment announce big layoffs, a tiny competitor, **Art's Way Manufacturing** (ARTW, news, msgs), says demand for its niche farm equipment is still fine.

"We have the same backlog as we did a year ago," Art's Way Chairman J. Ward McConnell Jr. told me last week. Orders for one line of equipment -- silage blowers -- are actually up.

Yet Art's Way stock has fallen more than 80% from highs last year, trading recently at $3.70 a share. If business truly is holding up, the stock looks like an attractive buy -- partly because costs should be down because the prices of steel and fuel have fallen. We'll find out more when earnings are released in late February.

Art's Way sells specialized equipment such as sugar beet harvesters, which lift 12 rows of beats out of the ground at once before cleaning them and putting them in a truck. It also makes feed grinders, the original products designed by company founder Art Luscombe about five decades ago.

A couple of factors make Art's Way a company Warren Buffett might love. It's the only vendor, or one of few vendors, of some types of farm equipment, says McConnell. So it enjoys pricing power. Next, it sells replacement parts that make for repeat business -- the kind of razor-and-razor-blade model that Buffett likes.

Joe Dancy, a money manager whose **LSGI Advisors** specializes in small and uncovered companies, also likes a line of business picked up two years ago called Art's Way Scientific. It sells mobile science labs used by universities and the government.

Dancy also likes Art's Way Manufacturing's huge inside ownership. McConnell holds about 40% of the stock.

Dancy is worth listening to because he has a good record. Since LSGI Advisors' inception 10 years ago, its picks had gained an average of 10.4% a year, compared with a 0.9% annual gain for the **Russell 2000 Index** ($IUX), as of early January. LSGI Advisors owns nearly 5% of Art's Way stock.