Is Now the Time to Buy Boardwalk REIT?

Description

It hasn't been an exceptionally good year for **Boardwalk REIT** (TSX:BEI.UN).

The weakness in oil has hit the company's share price hard. A year ago, shares of the owner of apartment buildings were flirting with $70 each, as investors rewarded the company for its conservative balance sheet and its oversized exposure to Alberta's fast-growing rental market.

Shares currently sit at just under $54 each, very close to the 52-week low set back in August. Investors are concerned that a prolonged slowdown in Alberta will cause rents in the province to plummet, which is obviously bad news for Alberta's largest landlord.

But is that really the case? Or have short-term investors overreacted again, as they often do?

The bull case

We're now in the ninth month of oil lingering below $60 per barrel, and economic numbers from Alberta look pretty bad.

Boardwalk is doing a nice job weathering the storm. Funds from operations (FFO) through the first two quarters of the year were $1.79 per share, which is an increase of nearly 10% compared with last year. The company is on pace to earn $3.58 per share in 2015. That puts shares at just over 15 times earnings, which is a reasonable valuation for the company, especially if you look at the price-to-FFO ratio over the last few years.

Management has done a nice job in creating communities that people want to live in. Boardwalk calls itself "Canada's nicest landlords", and it shows. The company does things like hosts tenant events, and gives discounts to tenants on cable and Internet subscriptions. Heck, Boardwalk even goes as far as calling its tenants "resident members".

Boardwalk isn't just doing this to be nice. The strategy is all about minimizing vacancy. It seems to be working; just a little more than 2% of the company's units are empty each month. That's not bad, especially considering its exposure to Alberta.

Boardwalk also has the balance sheet strength to weather the storm. The company has one of the lowest debt loads in the whole REIT universe, with a debt-to-assets ratio of just 38% net of cash. Net asset value (NAV) is just below $70 per share, which means shares currently trade at a 20% discount to NAV.

The dividend is rock solid, too. If the company does earn $3.58 per share this year in FFO, the payout ratio would be less than 60%. Sure, the dividend yield is only 3.8%–which is pretty low for a REIT–but you can't beat the stability of that payout.

Finally, the company is buying back shares pretty aggressively. Management has authorized a share buyback of more than 3.8 million units over the next 12 months, which could conceivably be worth more than $150 million.

The bear case

The reason to be bearish on Boardwalk is simple. If Alberta continues to be weak, there's little doubt rents will come down and earnings will take a hit.

Let's assume that revenue from Alberta is poised to fall 20%, which I think is a pretty reasonable worst-case scenario. About 60% of the company's revenue comes from Alberta, which means the top line would fall approximately 12%.

Say a 12% decline in revenue causes a 15% decline to FFO. That would send FFO down from $3.58 per share to $3.04. At $54 each, that puts shares at a P/E of 17.7 times. That's not cheap, but it's not really expensive either.

Still, it's easy to see a scenario where poor results could push shares down another 20%. I'm not sure it's terribly likely, but it's still something investors have to think about.

While there are legitimate concerns about Boardwalk's near-term future because of the weakness in crude, it's still a high-quality REIT with a nice balance sheet, good assets, and a management team that owns 25% of equity. For those reasons, I'd argue that today's price is a pretty good entry point.

CATEGORY

1. Dividend Stocks
2. Investing

TICKERS GLOBAL

1. TSX:BEI.UN (Boardwalk Real Estate Investment Trust)

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