Cominar Real Estate Investment Trust: Is This a 9.8% Yield You Can Count on?

Description

As we wrap up 2015, I'm sure it's been a year many investors in **Cominar Real Estate Investment Trust** (TSX:CUF.UN) would like to forget.

Thanks to various factors such as the threat of rising interest rates and the whole real estate sector falling out of favour among Canadian investors, shares of Quebec's biggest landlord are down nearly 20% in 2015. The stock now yields an attractive 9.8%, a number that has to look very enticing to income investors used to settling for yields that are much lower.

Can investors expect this dividend to continue? Or will 2016 finally be the year that Cominar slashes the payout? Let's take a closer look.

A year of transition

Cominar really beefed up its portfolio in the latter half of 2014, adding more than 5.5 million square feet in gross leasable area from Ivanhoe Cambridge Inc., the real estate arm of Quebec's pension plan. This acquisition of Quebec-based shopping malls was in addition to the 2.4 million in office and industrial spaces it acquired earlier in the year.

Altogether, Cominar boasts more than 45 million square feet in space, covering retail, office, and industrial uses. The vast majority of its property is located in Quebec, but it also has holdings in Toronto, Atlantic Canada, and Calgary. As of the end of the most recent quarter, the company had an occupancy rate of 92%, a slight decline from 94.1% a year ago.

The year was spent digesting the big acquisitions, and it looks like 2016 will be dedicated to paying down debt. The company's debt-to-assets ratio is currently 53.8%, a number that investors don't like. Most REITs like to keep that number under 50%. It's moving in the right direction–it was 54.8% last year–thanks to the help of a couple of asset sales, but investors will want to see that number under 50% by the end of 2016.

The other concern is the company's occupancy. Not only is occupancy going down, but many tenants are getting discounts as an incentive to stay. Thus far in 2015 the company has been able to retain nearly 69% of its current tenants, but it has reported a 1.7% decrease in net rent from these renewals. That signifies some weakness in Cominar's key markets.

How about the dividend?

Many dividend investors don't care about the price of their shares, as long as the dividend stays intact. Even though Cominar fell 20% in 2015, investors who held on the whole year would have gotten nearly half of the decline back in dividends. Thus, a 20% fall isn't so bad.

But what about the dividend going forward? Here's where it gets a little dicey. For the first nine months of 2015, Cominar posted $1.15 per share in adjusted funds from operations per share. It paid out $1.10 per share in distributions during that time, resulting in a payout ratio of more than 95%. Last year at this time, the payout ratio was 91.9%, which means 2015 did not move in the right direction.

Obviously, investors think there's a chance the payout could be cut to free up cash flow to pay down debt.

There's one potential saving grace. Cominar, like many other REITs, gives investors a discount if they take their dividends in the form of new shares. Since many investors take advantage of this deal, Cominar's cash payout ratio only comes in at 64.7%.

Over the long term, this leads to a gradual dilution of shares to the tune of approximately 3.5% per year. This could lead to issues in the future, especially if rents don't start to increase. But since most of these shareholders will opt to continue getting more shares in lieu of cash dividends, it shouldn't be a major problem.

In short, it looks as though Cominar can sustain the dividend in 2016. Further reduction in the debt will also help, since interest savings flow straight to the bottom line. Still, with a payout ratio so high, investors should keep a close eye on Cominar and look at selling it if that ratio exceeds 100%.

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