



Are Dividend Stocks in a Massive Bubble?

Description

It seems like every investor is looking for the same thing: solid, dependable yield, preferably with some dividend growth attached.

Retirees want it because dividend stocks yield more than GICs, government bonds, and so-called high-yield savings accounts. These instruments used to pay enough that a retiree could take a modest-sized nest egg, throw it in fixed-income products, collect CPP, and have a decent retirement. They don't anymore.

Meanwhile, other younger investors are also crowding into dividend stocks. They see the kind of returns generated by some of Canada's top dividend payers over the years, and they want that for their portfolio too. They also see these companies have held up well during recessions, and getting consistent dividends makes it easy to continually reinvest in better opportunities.

Generally, two things make up a bubble. The first is investor sentiment. The other is excessive valuations. This is where the bubble talk gets a little trickier. What constitutes excessive valuation? Shouldn't dividend stocks trade at a premium in a world where it's impossible to get much yield from safer investments?

Besides, dividend stocks make up such a huge percentage of the market that if they're in a bubble, then so is the overall stock market. There's just no avoiding it.

I'm skeptical that all dividend-paying stocks are in a bubble. However, I do think there are some stocks that are overvalued. Here are two I would avoid and two I would buy instead.

Avoid: Rogers Communications

Buy: Corus Entertainment

Rogers Communications Inc. ([TSX:RCI.B](#))([NYSE:RCI](#)) continues to lose momentum in wireless—the only real growth area left in telecom. Market share has slumped from 36% in 2014 to approximately 34% today as competitors have invested in their networks, taking away the advantage formerly owned by Rogers. Additionally, many customers view Rogers as an expensive brand and its competitors as a

better value.

Rogers also trades at an expensive valuation. Shares currently trade hands at 20 times trailing earnings and at 18.4 times forward earnings. Both of those multiples are a little too expensive for my blood.

Instead, I own **Corus Entertainment Inc.** ([TSX:CJR.B](#)), a company that recently transformed itself by making a major acquisition. Once everything settles down after the big acquisition, Corus expects it can generate approximately \$450 million in free cash flow, which works out to \$2.36 per share. That puts shares at just 5.9 times free cash flow.

Plus, Corus pays an 8.2% dividend—more than twice as generous as Rogers's 3.6% payout.

Avoid: Smart REIT

Buy: Slate Retail REIT

I'm a big fan of **Smart REIT** ([TSX:SRU.UN](#)). I like its experienced management team, its focus on **Wal-Mart**—which is a dream main tenant—and its 99% occupancy ratio, which continues to be the best in the business.

Again, the only problem is valuation. The company is on pace to generate \$2.16 per share in funds from operations in 2016 based on results so far. Shares trade at \$38.41 each, putting the company at 17.8 times funds from operations. That's a little expensive.

Slate Retail REIT ([TSX:SRT.UN](#)) has many of the good features Smart offers. Although it doesn't have Wal-Mart as a main tenant, it does have grocery stores anchoring all of its 66 properties located across 20 U.S. states.

Slate also trades at a much more attractive valuation. It's on pace to generate \$1.36 per share in funds from operations in 2016, while shares only trade hands at \$13.55 each. This puts shares at just 9.9 times funds from operations—a valuation 45% cheaper than Smart REIT.

Slate pays out a dividend of 7.5%, which is 74% higher than Smart's 4.3% payout. With a payout ratio of 66%, Slate's dividend looks to be every bit as solid as Smart REIT's. The company has even hiked the payout twice in the last year—in U.S. dollars.

As you can see, it's not terribly difficult for investors to find solid companies that trade at reasonable valuations. If you're concerned about a dividend bubble, perhaps it's time to take some money out of the winners and put it into some cheaper options.

CATEGORY

1. Dividend Stocks
2. Investing

POST TAG

1. Editor's Choice

TICKERS GLOBAL

1. NYSE:RCI (Rogers Communications Inc.)
2. TSX:CJR.B (Corus Entertainment Inc.)
3. TSX:RCI.B (Rogers Communications Inc.)
4. TSX:SGR.UN (Slate Retail REIT)
5. TSX:SRU.UN (SmartCentres Real Estate Investment Trust)

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