Dream Office Real Estate Investment Trst: Are Shares a Bargain After Falling 42%?

Description

Dream Office Real Estate Investment Trst's (TSX:D.UN) unitholders must be frustrated. Since the start of 2014 its unit price has fallen 42%. It has actually declined 55% from the start of 2013. I truly feel bad for investors who have held on since then. However, investing is a forward-looking activity.

Is Dream Office a good investment to own today? Should you buy at today's depressed price?

What has caused shares to fall?

Dream Office REIT earns about 27% of its net operating income (NOI) from Alberta, and the economy there continues to face adversity and uncertainty due to low commodity prices.

In fact, due to its Albertan portfolio, Dream Office recorded a fair-value loss of $748.4 million for the six-month period that ended on June 30, 2016.

In February Dream Office even cut its distribution by a third. So, the REIT now pays out a monthly distribution per unit of 12.5 cents, which equates to an annualized payout of $1.50 per unit. This was terrible news for investors who'd bought the REIT for the high yield.

What Dream Office has been doing right

That said, Dream Office has been making efforts to steer the ship in the right direction. The company is in the midst of selling $1.2 billion of its $2.6 billion non-core assets, which are more or less priced at their carrying values. The proceeds of the sales will be used for debt reduction and to strengthen the balance sheet, which will reduce interest expenses.

From the end of Q2 2015 to the end of Q2 this year, Dream Office has reduced the number of properties it has interests in from 174 to 157. In the same period, its NOI fell 3.2% and its diluted funds from operations (FFO) per unit fell 7%.

This makes sense because the REIT has fewer properties to earn rental income from. As of the end of

Q2 Dream Office still has about 64% of the $1.2 billion non-core assets to sell within the next 2.5 years.

Dream Office has also focused on its leasing efforts. The REIT renewed 95.4% of its maturing leases for this year from its core portfolio and achieved 10.4% higher rental rates compared to the expiring rates. Additionally, the REIT has secured 65% of the 2017 lease maturities in its core portfolio.

Is its distribution safe?

At about $16.70 per unit, Dream Office yields 9%. Based on the FFO per unit the REIT expects to earn this year and the elimination of the distribution-reinvestment plan, Dream Office's payout ratio would be about 68%, which makes its distribution safer than it was before.

Is Dream Office worth buying today?

Dream Office's cash distribution of 9% should be safe. However, unitholders should keep an eye on its declining FFO per unit to ensure it maintains a cushion for its current distribution. At the same time, unitholders should check that the REIT does what it says and uses the sale proceeds to repay debt.

From the end of Q2 2015 to the end of Q2 this year, Dream Office's net asset value (NAV) per unit has fallen almost 29% to $23.64. So, at the current price, Dream Office is priced at a discount of 29%.

Unitholders should also watch the changes in its NAV per unit over the next few quarters as Alberta will likely continue to shake that number. Unitholders should ensure there's a big enough margin of safety to continue holding the units.

With a discount of 29% and declining FFO, I wouldn't say Dream Office is a screaming buy. However, it's not a bad choice for current income and to sell at a profit when it trades closer to its NAV.

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1. Dividend Stocks
2. Investing

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1. Editor's Choice

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