



Why Doesn't Northview Apartment REIT Get Any Love?

Description

As a value investor, I'm constantly delving into a similar mystery. Why does one company attract a premium valuation, while a competitor doesn't get the same respect?

Unfortunately, the answer to this investing mystery isn't quite as tidy as the ending to the usual episode of *Law and Order*. Investors can usually figure out the answer to the valuation-gap mystery, but then they're left to interpret the results. Is such a gap justified? Or is it a buying opportunity?

That's the hard part.

Northview Apartment REIT (TSX:NVU.UN) trades at a much lower valuation than its peers. Let's take a closer look at this company to see whether the difference is justified or if it's a buying opportunity.

Valuation difference

The difference between Northview and its two main competitors—**Canadian Apartment Properties REIT** (TSX:CAR.UN) and **Boardwalk REIT** (TSX:BEI.UN)—mostly has to do with location.

Northview has a true nationwide portfolio. It has 24,300 units with approximately 8,200 located in Ontario, 7,200 in western Canada, 4,150 in Atlantic Canada, 2,400 in northern Canada, and 2,300 in Quebec. Approximately 34% of portfolio income comes from northern Canada.

While Boardwalk and Canadian Apartment Properties also have diverse portfolios, those companies have concentrated their holdings in Alberta and Ontario, respectively. While Alberta is struggling, Boardwalk's properties are viewed by the market as being well maintained and nice. Thus, the company is maintaining its premium valuation even through these tough times. And there isn't much wrong with owning property in Ontario.

Based on results for the first half of the year, Northview is on pace to deliver \$2.16 per share in funds from operations, despite one-time charges from the Fort McMurray wildfire hurting the bottom line. That puts shares at just 9.8 times funds from operations.

Boardwalk, meanwhile, which also suffered from its exposure to Fort McMurray, is trading at about 16.5 times its projected funds from operations for 2016. Canadian Apartment Properties is more expensive still, trading at 18 times projected funds from operations.

Dividends

Northview also beats its competitors on dividends. It's not even close.

Northview pays investors a monthly payout of 13.58 cents per share, giving it a yield of 7.7%. It has a payout ratio of approximately 75% of 2016's funds from operations. Remember, this payout ratio is projected to fall to around 70% in 2017 as earnings return to normal.

Compare that to Boardwalk, which is often complimented on the safety of its 4.4% yield. Boardwalk pays investors 18.75 cents per share each month, giving it a payout ratio of approximately 73%. Canadian Apartment Properties pays investors 10.167 cents per share monthly, giving it a payout ratio of approximately 76%. It currently has a yield comparable to Boardwalk at 4.3%.

In short, Northview pays a 7.7% dividend with a 75% payout ratio. Its competitors have payout ratios very similar, but they have much lower dividends.

What's wrong with Northview?

There's no such thing as a free lunch in investing, or so the saying goes. There must be something wrong with Northview if it trades at such a low valuation compared with peers.

We've already touched on one particular issue. Many Canadian investors don't like the company's outsized exposure to northern markets.

Another reason is the company's debt. It currently has a debt-to-assets ratio of approximately 60%, much higher than its main competitors and a full 10 percentage points higher than the 50% debt-to-assets level REIT investors like to see as a maximum.

The debt is trending in the wrong direction, too. A year ago, Northview had a debt-to-assets ratio of 51.3%. It does plan to reduce debt by selling a few non-core assets, but it's obvious the market is sending management a message.

The bottom line

Northview Apartment REIT has a higher dividend and trades at a much lower price-to-funds-from-operations ratio than its peers. As long as the company can pay down its debt and maintain that generous dividend, look for its valuation to move more in line with the rest of the sector, leading to nice profits for investors who get in today.

CATEGORY

1. Dividend Stocks
2. Investing

TICKERS GLOBAL

1. TSX:BEI.UN (Boardwalk Real Estate Investment Trust)
2. TSX:CAR.UN (Canadian Apartment Properties Real Estate Investment Trust)

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Date

2025/07/01

Date Created

2016/10/04

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