Income Investors: Are These 3 Huge Dividends Safe?

Description

There's nothing more powerful than a succulent dividend for income investors.

Despite all of the warnings about stretching for yield or the dangers of a dividend cut, these investors continue to be attracted to companies that pay huge dividends. The logic goes something like this: if a dividend of 2-3% is good, then one between 6% and 9% must be three times better.

Many of these investors are also older, looking to build a steady stream of income they can live on during retirement. They're comforted by knowing that individual high-yield stocks can be risky, but a whole portfolio carries far less risk.

Besides, it isn't that hard to analyze a stock to get an idea of the sustainability of the payout. Nothing is guaranteed, of course, but earnings and cash flow don't lie. Either a company can afford a dividend or it can't.

Let's take a look at three of Canada's favourite high-yield stocks to see if they can afford those generous yields for years to come.

Alaris Royalty

The royalty business has some pretty favourable economics.

A company needs cash but doesn't want to give up equity. So it approaches a company like **Alaris Royalty Corp.** (TSX:AD) with a deal. The company gets cash, while Alaris gets a special series of shares that gives it a return of 10-15% annually with inflation protection built in.

So if the royalty business is such a good deal, why have Alaris shares fallen 25% in the last six months?

It has to do with the company's investment in KMH, a medical company. It's facing some financial difficulties, and distributions back to Alaris have ceased. But both companies are working on solutions, which could include a third company buying Alaris's interest.

Despite these difficulties, Alaris has increased revenue from partners 23% thus far in 2016 to $1.40 per share. Analysts continue to be bullish on earnings too, collectively expecting it to earn $1.71 per share in 2016. That's enough to cover its 7.5% yield, albeit without much room to spare. At least next year is forecast to be better with analysts saying the company will earn $1.97 per share.

Veresen

When oil and natural gas were really tanking back in January and February, it sure looked as though **Veresen Inc**. (TSX:VSN) would be forced to cut its 8.33-cent-per-share monthly dividend.

Not only has the outlook for the energy sector improved since then, but Veresen has been making some prudent moves. It suspended its dividend-reinvestment program. It's also looking at selling its portfolio of power plants to help fund internal expansion. Once these projects come online in 2017 and especially 2018, distributable cash should increase nicely.

The company is on pace to earn between $1.03 and $1.13 per share in distributable cash in 2016, while paying out a dividend of $1.00 per share. This gives it enough cash flow to cover the 7.5% dividend, but only barely. Dividend investors should keep a close eye on this stock, just in case.

Dream Office

Although **Dream Office Real Estate Investment Trst** (TSX:D.UN) has already cut its dividend once this year, it remains a popular investment for income seekers. It still yields 9%.

The company is still suffering from the issues that caused the dividend cut in the first place. The Albertan market is struggling, and vacancies are up. Management has responded by laying out a plan to help bring the company back to its former glory, which includes selling off non-core assets, paying down debt, and moving the portfolio's focus away from struggling Alberta.

Even though Dream is struggling, its dividend remains rock solid. The company currently pays out a monthly dividend of $0.125 per share. It earned $1.33 per share in funds from operations for the first six months of the year, while normalized dividends were $0.75 per share. This gives it a payout ratio of just 56%.

The bottom line

Alaris, Veresen, and Dream Office REIT should be able to pay their dividends going forward. Still, like with any high-dividend stock, investors do need to keep an eye on the payout to ensure it'll get paid over the long term.

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1. Dividend Stocks
2. Investing

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1. Editor's Choice

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1. TSX:AD.UN (Alaris Equity Partners Income Trust)
2. TSX:D.UN (Dream Office Real Estate Investment Trust)

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Date
2025/08/23
Date Created
2016/10/06
Author
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