



Is There Trouble on the Horizon for Artis Real Estate Investment Trust?

Description

Shares of **Artis Real Estate Investment Trust** ([TSX:AX.UN](#)) appear to offer unitholders excellent value. Currently trading at a price just above \$11.75, the dividend yield in excess of 9% seems to be sustainable to many. Like an iceberg, however, there is a lot of danger investors are missing.

The dividend, which has remained at \$0.09 per unit per month since 2009, accounted for 87.8% of AFFO (adjusted funds from operations) in 2014, 87.8% of AFFO in 2015, and, through the first three quarters of 2016, represents roughly 90% of AFFO. The risk which is being priced into the market is the potential for a cut in the monthly distribution.

Why will the monthly distribution be cut?

When a positive-cash-flow-generating company is trading at a percentage of book value, it is either because the market has missed something and an upwards correction will follow, or there is the potential for the other shoe to drop. At the current price of \$11.75 per share, there is a clear discrepancy when comparing the share price to the company's book value. The current book value is \$17.86, which translates to a discount of almost 35%.

Although many investors are excited about the yield of approximately 9.15%, it may not be sustainable for two reasons. First, with every passing year, the number of shares outstanding is increasing due to the distributions being re-invested, translating to a higher need for cash year after year. Each year, the monthly cash dividend of \$0.09 per unit must be paid on a greater amount of shares. In 2012, there were approximately 115 million shares outstanding, while that number grew to approximately 150 million as of the end of the third quarter 2016.

The second thing to look at is where the company's NOI (net operating income) is coming from. Presently, the company is well diversified across the industrial, office, and retail space. In addition, the geographic makeup encompasses the entire country with several investments in the United States.

Although Canada accounts for approximately two-thirds of the entire portfolio, the province of Alberta, which is highly dependent on the oil sector, accounts for 30% of the total NOI. This poses a significant risk to the company. Arguably, the market is pricing in a value of \$0 for the assets located in Alberta.

That's right—zero.

If the properties in Alberta become a cash drain down the road, they are surely worth something. But let's not forget, if the price of oil goes back to \$100 per barrel, it doesn't translate to every employee being hired back. And the real estate which was previously occupied by these companies will not be needed in the future like it was in the past. Albertan real estate is just not as lucrative as it once was. The demand has declined significantly.

Conclusion

Even with the Albertan assets being priced at a significant discount, we have to remember the pie is getting too big too fast. Investing is not like eating dessert, where we are happy to dive into a bigger pie. Instead, we want to find a quality piece, holding it steady no matter how small it is, while watching the pie shrink along the way. If a dividend cut is announced, it may be prudent to watch the stock price and re-assess it down the road. There are many good things still to be had.

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