



This Little-Known REIT Might Be Canada's Cheapest Stock

Description

I'm a firm believer that we make investing too complicated.

The investing world is filled with hedge fund managers building complex discounted cash flow models with every imaginable variable scrutinized. You know it's good when the spreadsheet takes longer than a few seconds to crunch the data.

I prefer to do things another way. If a company's valuation doesn't floor me, it's not cheap enough. Or as Warren Buffett once put it, I'd rather find a one-foot bar to step over versus a seven-foot bar I'd have to jump.

With that in mind, let's spend a little time taking a closer look at **Morguard Real Estate Inv.** ([TSX:MRT.UN](#)), a company that is ridiculously undervalued.

About Morguard

There are three Morguard companies that trade on the Toronto Stock Exchange. The parent company is **Morguard Corporation**, which owns and manages real estate. There's also the **Morguard North American Residential REIT**, which owns multi-family housing in both Canada and the United States. We're going to focus on Morguard REIT, which owns retail, office, and industrial property across Canada's five westernmost provinces.

Morguard Corporation is the largest shareholder of both its namesake REITs.

Morguard REIT is a medium-sized company. It owns \$2.9 billion worth of real estate—a total of 49 different properties. Out of a total portfolio of 8.7 million square feet, 55% is retail space, 40% is office space, and 5% is industrial.

Much of the portfolio is located in Alberta, but management isn't too worried about general economic weakness in the region. Oil prices are recovering, and most economists are predicting the province's economy will expand in 2017. Occupancy has also stayed above 95% with good lease renewals.

Asset value

At the end of September, Morguard had a book value of \$1.57 billion, virtually unchanged from a year ago. The company has a market cap of \$890 million. That puts shares at a staggering 43% under book value.

Or to put it another way, the company's assets are worth nearly \$26 per share versus Monday's closing price of \$14.57. That is a huge disparity.

Naysayers will scoff at this with a very predictable retort. It's obvious the Albertan assets aren't worth as much as management says. In fact, they should be worth close to nothing.

I've never understood that argument. Over the first nine months of 2016, those Albertan properties delivered more than \$37 million worth of net operating income, or about 31% of total income. That works out to about \$50 million annualized. How are assets generating \$50 million worthless?

Earning power

Investors have been worried about Morguard's earning power since 2014. And yet the company continues to deliver.

Over its last four quarters, it has delivered \$1.89 per share in funds from operations and \$1.26 per share in adjusted funds from operations. Let's be conservative and take the smaller number, even though it is skewed downwards by a number of big renovation projects.

Shares today trade at less than 12 times adjusted funds from operations. Not only is Morguard cheap on an assets perspective, but it's also cheap on an earnings basis as well.

Giving back to shareholders

The other big thing I like about Morguard REIT is management is actively buying back what they view to be undervalued shares.

On September 30, 2015, Morguard had 61.6 million shares outstanding. These days, that number is 60.6 million.

Investors are also getting paid an attractive yield of 6.6%. Yes, you can find higher yields out there, but Morguard has a nice combination of current yield and a low payout ratio of 80% of adjusted funds from operations.

The bottom line

It isn't very often investors get the chance to load up on a company trading at 57% of book value, less than 12 times earnings, and that pays a 6.6% yield. Oh, and its largest shareholder is a true giant in the Canadian real estate space. It doesn't get much better than that.

CATEGORY

1. Dividend Stocks

2. Investing

TICKERS GLOBAL

1. TSX:MRT.UN (Morguard Real Estate Investment Trust)

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