Dream Office Real Estate Investment Trst: More Room to Grow?

Description

Since the middle of August, the price of **Dream Office Real Estate Investment Trst** (TSX:D.UN) has increased by nearly 19%, or a little over $3 a share. And along the way, investors were paid $0.63 in dividends. But now that the stock has finally recovered some, investors are left wondering if the stock has more to grow. I believe the answer to that is yes.

To understand why, it helps to understand how a company like Dream Office is valued. Because it is a REIT, all of its assets are in real estate. Therefore, each building has value that can be broken down into what it contributes to the share price. This is called its net asset value (NAV). For Dream Office, that value is $23.64. If all the real estate were to be sold and then distributed to investors, the belief is that the company could fetch $23.64 per share.

This is important for investors because with the company trading at $19.39, it's trading at a discount of a little under 20%. And, for the record, that NAV of $23.64 is after Dream Office decreased the value of its Albertan holdings. Before doing that, its NAV was over $30 a share. But because investors were fearful of oil prices staying low, the company moved to value itself on its other core holdings

Now, there are two ways for management to handle this discount. The first is to just wait and see when Mr. Market will treat the company fairly, but, as Benjamin Graham taught us, Mr. Market is irrational. The other way to handle this is to start selling real estate. If the market won't value the real estate, perhaps the market will value cold hard cash. The company is working through a plan to sell $1.2 billion in real estate (and has already sold over $400 million), which should help it to close that gap in NAV and, hopefully, reward investors quite handsomely.

Another reason that Dream Office was battered so much in 2016 was due to the cut in the dividend. It had been paying US$0.187 per share a month to its investors, but it was forced to cut it to the current $0.125 per share. This is actually a good thing, though, because it put the company on much stronger footing. Now it pays out less than 60% of funds from operations, meaning that it is in a very strong position.

Here's how I would play this stock:

Start accumulating shares and reinvesting the dividends each month. For example, if you were to spend $19,390 (plus commissions), you'd be sitting on 1,000 shares. Each month, you'd bring in $125 in shares, which you could then reinvest in more shares. But what you'd be getting is the equivalent of $23,640 in real estate.

In the long term, I expect things to turn around in Alberta. And when they do, the company will be a leaner operation which will generate larger amounts of cash flow. Investors will be forced to increase the value of the shares, thus rewarding you for your patience. Dream Office is not a short-term play, but with the monthly dividend, it's a lucrative play.

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Date
2025/08/18
Date Created
2017/01/24
Author
jaycodon