



Is This Monster 8% Yield an Attractive Investment?

Description

Even after the Bank of Canada's surprise rate hike earlier this month, which saw the overnight rate hiked by 25 basis points to 1%, its highest level since January 2009, interest rates remain well below the historical average. Such low rates intensified the hunt for yield, because traditional, lower-risk, yield-focused assets such as bonds, GICs, and term deposits were no longer generating sufficient income.

Income investors turned to REITs. Because of extremely low interest rates, REITs loaded up on debt, which was used to finance the expansion of their property assets and boost their earnings. As income rose, so too did the distributions at a healthy clip, which now sees many offering investors fat yields in excess of 5%, or more than double the average dividend of the TSX.

One REIT that has a particularly attractive yield of over 8% is **Artis Real Estate Investment Trust** ([TSX:AX.UN](#)). While such a high yield is appealing to investors and is roughly four times that of 10-year Canadian government treasuries, there are some lingering doubts as to whether it is sustainable.

Now what?

Among the major factors weighing heavily on REITs is the disruptive power of **Amazon.com, Inc.** ([NASDAQ:AMZN](#)) and e-commerce. They pose a major threat to the viability of brick-and-mortar retailers, prompting fears that the end of the traditional shopping mall may be on its way. That, it is believed, will trigger a sharp decline in demand for retail properties, which is a core business for many commercial REITs.

Nevertheless, this shouldn't be a problem for Artis.

You see, less than 14% of the gross leasable area of its property portfolio is retail, the remainder is split almost evenly between office and industrial properties, which are not vulnerable to forces that are disrupting the retail industry.

Artis is also in the process of winding down its exposure to Alberta because of the ongoing marked impact of the slump in crude, which has hit regional economic growth hard. For the second quarter 2017, only 26% of net operating income came from Alberta compared to 39% for the same quarter in

2014.

The REIT also listed a number of properties for sale that have been identified as not being aligned with the business's long-term strategic outlook.

The proceeds of these sales are being used to strengthen Artis's balance sheet and further diversify its property portfolio through acquisitions of predominantly industrial properties in the U.S. This saw it finish the second quarter with long-term debt of 8.5 times EBITDA and a net asset value of \$14.89 per share, or almost 13% higher than its current price, indicating that it is attractively valued.

Each of these factors also helps to bolster the sustainability of its monthly distribution and that juicy 8% yield, which has a long-term average payout ratio of over 100%, leading some pundits to question its sustainability.

However, for the first six months of 2017, that ratio fell to 76% because of a 65% year-over-year increase in net earnings per share.

So what?

Artis's efforts to strengthen its operations by reducing its exposure to Alberta and diversifying into industrial properties in the U.S. are certainly paying dividends for the business. Second-quarter net income shot up by an impressive 22% compared to a year earlier, and the payout ratio for its distributions has fallen to a more sustainable level. When considered in conjunction with Artis appearing attractively priced and that monster 8% yield, this is one REIT that investors should consider adding to their portfolios.

CATEGORY

1. Dividend Stocks
2. Investing

TICKERS GLOBAL

1. NASDAQ:AMZN (Amazon.com Inc.)
2. TSX:AX.UN (Artis Real Estate Investment Trust)

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