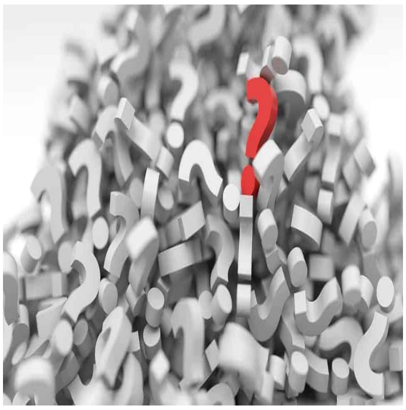

Can This High-Yield REIT Turn Things Around?

Description

Cominar Real Estate Investment Trust (TSX:CUF.UN) is a high-yielding, diversified REIT that is no stranger to hard times. From 2008 to 2009, the company's stock dropped 40% from $22.74 to $13.25. Despite building back up and testing new highs, the stock was again in the basement for 2017, reaching a new low of $12.03 in August.

The company recently took fairly drastic action: it closed a deal and sold 92 of its properties to a younger, slightly smaller publicly traded REIT that operates under two symbols: **Slate Office REIT** (TSX:SOT.UN) and **Slate Retail REIT** (TSX:SRT.UN). Slate is adding $1.14 billion to its current enterprise value of $3.2 billion. Slate Office has been increasing revenue by 39% per year since 2013, but it will have to find more cash to pay the hefty price tag for all these properties.

In a December 18th statement, Cominar — a Québec City-based company — announced it would sell 24 properties from the Toronto area, 59 from Atlantic Canada, and 14 from Western Canada. Cominar viewed these properties as "non-core" components of the portfolio.

Did Cominar just hand over the golden goose?

Part of the sell-off to Slate included an 18-storey office building in downtown Toronto. Maybe it was hard to secure multi-year tenants when office leases are high at ~$3-4 per square foot. For comparison, downtown Toronto condo dwellers pay roughly twice the office lease rate at ~$8 per square foot of residential space.

The property sell-off included more office and industrial properties than retail. Holding on to to "out-of-favour" retail properties could be a wise move going forward, as retail reinvents itself. Looking at the turnaround from the largest retail REIT, **RioCan Real Estate Investment Trust** (TSX:REI.UN), which has rallied as much as 8% in the last three months, provides some insight on how to make retail great again.

The good

Cominar has a very high yield — currently 8.24%. This income alone is enough to beat performance from many TSX stocks, but if the stocks drops by the same amount each year, then you are no further ahead with your investment. The good news for Cominar is that it appears to be serious about maintaining the high yield. Even in tough times, one share in Cominar would give the investor between $1.28 and $1.47 in dividend income per annum. And by shedding office properties, it will free itself from the part of the business with the lowest occupancy rates.

The bad

The bad news is that the historically principled dividend payment has a downside. The dividend-payout ratio exceeded 100% in five out of 10 years; the free cash flow has been negative in all but three out of 10 years. On the flip side, it is a good sign that the payout ratios have dropped below 100% in the last five years. Other bad news is that it may be hard to estimate future earnings in 2018 with such a business shake-up. Lastly, the current price-to-free-cash flow ratio is currently over 20, which is not attractive from a value point of view.

Bottom line

Cominar can focus efforts on Quebec-based operations, which emphasizes retail shops and malls, where occupancy rates are 93%. Income investors may want to watch this high-yield stock and hope for a smoother ride.

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