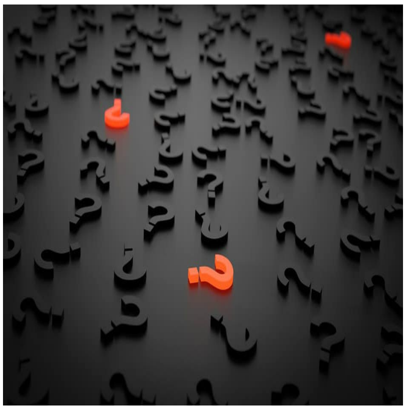

TFSA Investors: Are These 9% Yields Safe for Your Dividend Portfolio?

Description

TFSA investors looking for long-term growth will naturally be attracted to high-yielding dividend stocks, but that isn't always without risk. Companies that pay out a high proportion of their income in the form of dividends and have high payout ratios may not be able to afford to continue to pay dividends at their current rate, and that could result in a cut to the payout, which may also have an adverse impact on the share price and total returns for shareholders.

It's important to consider how likely the company is to pay its dividend in the quarters and years ahead. Below are two stocks that pay more than 9% in dividends annually, and I'll have a closer look at whether their payouts are sustainable or if investors should look elsewhere.

American Hotel Income Properties REIT LP (TSX:HOT.UN) offers investors a unique way to take advantage of rising real estate values in the U.S. as well as the tourism industry. Its portfolio is spread across the U.S. and offers investors a great way to diversify.

Despite its interesting strategy, American Hotel's stock has declined more than 20% in the past year, and year to date it is already down 11%. As a result of the decline, the company's monthly dividend, which is paid in U.S. dollars, has now climbed to over 10%. At first glance, this looks like a great opportunity given the stock is trading near its book value and is offering investors a very high yield, but let's take a look at its payout ratio first.

In the past year, American Hotel just broke even, so we wouldn't be able to calculate a payout ratio based on earnings since the denominator in that calculation would be zero. In 2016, however, the company's earnings per share (EPS) were US$0.23 and would be well short of the US$0.648 that American Hotel pays out in dividends per year for each stock. Looking at free cash might offer better insights since earnings include non-cash items. The problem is that American Hotel's free cash flow has been negative in each of the past four years and rose significantly this past year as well.

While American Hotel's yield looks attractive, I'd be concerned that it isn't going to survive the long term.

Alaris Royalty Corp. (TSX:AD) is another dividend stock, and it pays its shareholders a little less at

~9.2%, which is still a very high rate. The financing company, unlike American Hotel, has been able to stay in the black with its most recent year showing EPS of $0.32, although that is down from $1.81 in 2016. However, this still is concerning given that annual dividends of $1.62 are well in excess of the most recent year's earnings and would be 90% of the prior year's profits.

Alaris has produced free cash flow in each of the past five years, and last year it paid out 88% of its free cash in the form of dividends. Either way you look at it, Alaris's yield should also raise flags for investors.

A safer option for investors

Both of the stocks listed here present risk, and investors looking for safety and long-term returns might be better off looking at a stock like **Fortis Inc.** (TSX:FTS)(NYSE:FTS) and its growing dividend. While Alaris and American Hotel may very well continue their payouts in the short term, for investors looking for stocks to just buy and forget, these two would not be suitable options.

CATEGORY

1. Dividend Stocks
2. Investing

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1. Editor's Choice

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1. NYSE:FTS (Fortis Inc.)
2. TSX:AD.UN (Alaris Equity Partners Income Trust)
3. TSX:FTS (Fortis Inc.)
4. TSX:HOT.UN (American Hotel Income Properties REIT LP)

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