Maritime Dream Stock Hits Up the Market for Expansion Funds

Description

Now that I'm living in Halifax, I see the **Killam Apartment REIT** (TSX:KMP.UN) name everywhere. That's because it's based here, although it owns apartment buildings in five other cities on the east coast as well as in Ontario and Alberta.

Back in April 2017, I'd recommended investors get in while it was trading below a billion-dollar market cap, because it was on its way to $2 billion by 2024, possibly sooner. Up 17% since then, the company's June 26th announcement of a $57.5 million bought deal has me sniffing around once more.

Why a bought deal?

When I last spoke of Killam, I emphasized the REIT's development pipeline was significant at 1,300 units and getting bigger, which is good because it generates better profits building new rental apartments rather than acquiring existing ones.

Desjardins Securities analyst Michael Markidis recently resumed coverage of Killam stock, emphasizing the bought deal suggests the company is ripe for expansion.

"Aside from the full repayment of the credit facility (current balance of $30.5 million outstanding), a use for the proceeds has not been identified. Keep in mind, however, that management has established a strong track record of execution on the external growth front," Markidis said in a report to clients. "KMP has already completed $124-million of acquisitions thus far in 2018. And with a stated target of $150–200 million, we expect that additional announcements will be made in the back half of this year, with a particular emphasis on adding scale in Ontario and Alberta."

As interest rates continue to move higher, Killam will continue to weigh its cost of capital between debt and equity financing. It feels the time is right to go to the markets, issuing 3.8 million units of its stock at $14.95 a share, a slight discount to where it's currently trading.

It's important to note that the 15% underwriters' over-allotment was exercised — a sign Killam had no trouble finding takers of KMP.UN stock.

Fool contributor Joey Frenette recently addressed the whole rising interest rates issue and what income investors should do to cope with the inherent volatility that comes from REITs generating lower cash flow in this type of operating environment.

You’ve got to tuck away some cash to buy on the dip — something that happened to Killam in early 2018 on fears of higher interest rates. Since Killam’s February low, it’s up 20%, a very nice short-term return for anyone who got in below $13.

The future

When I wrote about Killam in 2017, it had a pipeline of 1,300 units. As of the end of the first quarter in March, it had 2,400 units under development that are expected to cost $700 million to bring to completion.

Currently, Killam generates 27% of its net operating income (NOI) outside Atlantic Canada, up from 23% in 2017; it expects to hit its goal of 30% by the end of 2020. That’s a good thing, because as I stated in the beginning, Killam is well represented in the Halifax area with 64 rental properties and 5,569 apartments accounting for 38.4% of its overall NOI.

Investors are well served by it diversifying beyond its Maritime roots.

As my colleague suggests, I would buy a little now and put aside some more to buy later when and if it drops down below $13, as it’s done a couple of times over the past 24 months.

Paying a 4.2% dividend yield at the moment, Killam remains an income investor’s dream stock.

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