Income Investors: This 6.75% Dividend Yield Is Irresistible

Description

While busy turning the stock market stones, searching for those undiscovered potential gems for a typical long-term hold income generating portfolio, it's easy for one to make a general pass on anything mortgage related due to current negative sentiment. The recent tightening in mortgage lending regulations in Canada is a cause for investor concern on the broader housing market's rate of expansion — a development that could dampen growth in loan portfolios for lenders in this space.

That said, there is one rising small cap that has curved out a niche and is defying the odds.

Atrium Mortgage Investment Corp. (TSX:AI) is a growing short-term alternative lender that has been reporting impressive revenue growth rates and reaping bigger profits recently.

Impressive growth rates

Atrium recently posted record revenues and record earnings for the second quarter of this year, sustained by a strong growing mortgage portfolio of $701.6 million, up 11.9% since year-end 2017.

The portfolio has generated impressive interest income growth with the general increase in interest rates. Weighted average interest rate increased for the third consecutive quarter, during the second quarter of 2018 from 8.44% by December 2017 to 8.54% by June 30, 2018. That's a clear 10 basis point gain in earning power of every dollar invested the Atrium MIC's portfolio.

The above gains had the combined effect of generating record revenues and record net income gains for the corporation during the most recent quarter. Second quarter revenues were up 21.1% from their levels in 2017 and net income jumped 26.5% from its comparable figure last year.

Atrium MIC maintains a high quality loan portfolio. which is 80% invested in first mortgages with a better collateral quality as 86.9% of the portfolio loans have a loan-to-value (LTV) ratio of less than 75%. The average LTV ratio stood at 61% by June 30 this year, offering significant equity value protection for investors.

Strong dividend yield

Atrium pays a $0.075 per share regular monthly dividend that currently yields a healthy 6.75% on a forward basis. The corporation has traditionally increased its annual dividend by $0.02 every year, and the payout has grown 17% over the past five years, but that's not the best part.

The regular dividend was 92.6% of net income in 2017, after two consecutive years of being consistently under 90%, and being an income trust, the company pays a special dividend to shareholders of record at year-end to top up the total dividends so that they equal its earnings in the year!

It follows that these special dividends will keep coming if Atrium continues on its earnings growth path, and the alternative lender will subsequently continue increasing its regular dividend, further sweetening an already great income yield.

The drip discount factor

The drip discount factor (DRIP) is an attractive one that allows Atrium MIC investors to automatically reinvest their dividends with the firm while avoiding market transaction costs. Atrium offers a 2% discount to market to drippers. I consider this an instant 2% capital gain.

The drip offering on this stock allows an investor to slowly build a sizeable position on the growing mortgage lender that could one day be big enough to generate a monthly paycheck good enough to cover a significant portion of living expenses in retirement.

Investor takeaway

Atrium MIC lends in major urban centres where the stability and liquidity of real estate are high and the company's largely short-term loan portfolio resets its interest rates faster than most mortgage portfolios. I expect a continued rise in portfolio profitability as interest rates continue on a steady rise and the resultant special dividend growth is a compelling idea for income investors.

Investing in Atrium MIC stock has been one of the best decisions for income-oriented investors over the past five years, as the high dividend yield and a sustainable growth in its asset base and improving asset quality has generated consistent returns to shareholders. The strong earnings growth seen thus far in 2018 is likely to be sustained.

Initiating a long-term position on this income growth play could be a very good idea as long as the real estate market remains stable and growing.

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