Why I Just Added This 8.1% Yielder to My TFSA

Description

Like many people reading this, I have two ultimate goals with my TFSA.

First, I plan to grow it as much as possible. I know becoming a TFSA millionaire is only a matter of time if I keep maxing out my annual contributions and get even half-decent returns, so I continue to invest the maximum allowed each year.

My secondary goal is to build a TFSA that generates gobs of passive, tax-free, dividend income. This means I'm stuffing the account with dividend payers I think will deliver income for life.

There's nothing left to do after that but to sit back, relax, and let compounding do its magic. It really is that simple.

Let's take a closer look at a stock I recently added to my TFSA — an 8.1% yielder I think can be counted on for years to come.

Enter Alaris Royalty

I've kept my eye on **Alaris Royalty** (TSX:AD) for years now, originally enticed by the generous dividend.

The interesting business model also caught my eye. Alaris provides a unique form of financing to businesses that wish to not give up control. Alaris buys a special kind of share in the enterprise in exchange for an income stream that generally has some sort of growth provision built in. This ensures a steadily growing distribution.

Shares traded at close to $30 each when I first discovered the stock — a valuation many thought was entirely justified. Alaris had a great portfolio stuffed with solid, old-world-economy companies.

But then the company started to face some issues. A couple of its partners stopped making payments due to financial duress. And a couple others exercised exit clauses, which resulted in a nice one-time gain at the expense of steady revenue. These factors all combined to decrease annual income, which put the dividend in jeopardy.

The turnaround

Alaris shares peaked in 2014 at $36 each and have slowly fallen ever since. They eventually reached a low of $16 before recovering slightly. Today, you can buy a single Alaris share for just over $20.

Despite this massive decline, Alaris is arguably in better shape than it was in 2014. That year the company posted revenue of $67 million and a net profit of $49 million. Management expects 2019 to deliver revenue of approximately $100 million this year and profits of $63 million. And this hasn't been accompanied with a massive share dilution, either.

Simply put, Alaris is undervalued and not really appreciated these days. Shares trade at just 11.6 times analyst profit expectations for 2019 and at just 1.2 times book value. That's music to this value investor's ears.

And after a few years of the dividend being on shaky ground, I believe the payout is once again safe. Management also recently sent a huge message to the market, increasing the annual distribution from $1.62 to $1.65 per share. Companies worried about the sustainability of their payout usually don't increase their dividend.

I believe Alaris can continue to increase its dividend slowly over time, which is a nice bonus on a stock currently yielding 8.1%.

A business that scales forever

The sky truly is the limit for Alaris Royalty. That's the beauty of this business.

The company's head office in Calgary is staffed with just 14 employees — a number that doesn't have to go up as the company expands. Remember, Alaris makes a passive investment in each of its partners. Once the due diligence is done on a deal, there isn't really much to do besides sit back and collect the payments.

There are only two things limiting Alaris's expansion. The first is availability of capital, which isn't a short-term concern. Alaris has cash in the bank today and the ability to raise more. The second is the number of investment opportunities. This one is a little trickier, but there will always be businesses that need capital. And Alaris hasn't had trouble putting capital to work thus far.

The bottom line

Alaris should be an attractive option for dividend investors due to the generous yield and potential for dividend growth over time. And value investors should also like the shares today, thanks to the low valuation. Put the two together, and it combines to make a powerful investment thesis.

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2. Investing

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