TFSA Investors: This 7.1% Yielder Pays Cash Every Month

Description

There are few things more powerful than building a passive, tax-free income stream inside your TFSA. In fact, if you play your cards right, your TFSA will eventually spin off enough cash to fund a nice retirement.

There are two ways you can approach such a strategy. You can either buy dividend growers that have the potential to increase the payout over time, or you can purchase high-yield stocks that already have great dividends today. That cash can then be reinvested into new opportunities, creating a powerful compounding effect.

But what if you can get the best of both worlds? Yes, I'm talking about both a high yield today and potential for dividend growth in the future. That would be a pretty powerful combination.

I think such an opportunity exists today with **Cineplex** (TSX:CGX). Let's take a closer look.

Growth potential

Many people — including myself — predicted new streaming services would impact Cineplex's bottom line, at least on a short-term basis.

But, interestingly enough, the exact opposite happened in the company's most recent quarter. It posted a 1.8% increase in theatre attendance, which was enough to boost the top line by 8.3%. Increased attendance helped boost concession sales, which were up nearly 9% for the quarter.

The really exciting part was Cineplex's continued diversification away the theatre business. The company's media division posted a healthy gain, partially boosted by a big order from a U.S.-based theatre chain. Its entertainment division had a nice gain after it opened additional Playdium and The Rec Room locations. Cineplex even saw growth in its loyalty program, which recently surpassed 10 million members.

Add it all up, and we have a pretty formidable business. And yet, Cineplex shares are down some 50%

from highs set just a few years ago.

One of the big issues is investors are just focusing on Cineplex's traditional business without giving it any credit for its already successful diversification efforts. In fact, I'd even argue the company doesn't really compete with streaming services. One is an outing — something you seek out. It's part of your entertainment budget. The other is something you end up doing because you're too tired to go out.

In other words, there's room for both.

Besides, these theatres aren't just focusing on showing the latest movie. The company has expanded into things like foreign films, showing e-sports and other entertainment events, and even classic movies.

Get paid

One nice thing about Cineplex's poor showing over the last few years is the company's dividend yield has gotten pretty attractive. Shares now yield a robust 7.1%.

Many investors argue that Cineplex is on the verge of cutting its dividend, but I strongly disagree. The company's payout ratio is strong, and it continues to grow the bottom line.

Through the first three quarters of 2019, Cineplex posted an adjusted free cash flow of $2.04 per share, which was up 6% from the same total last year. It paid $1.325 per share in dividends over that time period. This gives us a payout ratio of just 65%.

Some investors argue that this isn't a realistic payout ratio, because Cineplex's adjusted free cash flow metric doesn't factor in growth capital expenditures. That's true, but investors must remember investments in new screens or The Rec Room locations lead to greater earnings down the line. And it can always scale back the diversification efforts if needed.

Besides, Cineplex has grown its payout each year since 2010. Would a management team worried about the security of the payout be doing that?

The bottom line

I believe Cineplex and its 7.1% yield are both pretty secure. Investors can count on the payout. The dividend could easily continue to march higher.

In fact, I wouldn't be surprised if shares really started to appreciate once the company's diversification effort really starts to take off.

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