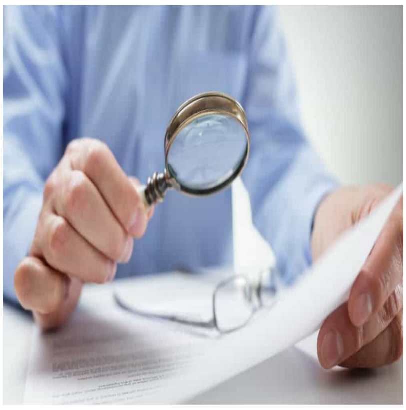

TFSA Investors: Is This 11%-Yielding Dividend Stock a Steal of a Deal?

Description

When dividend stocks are yielding more than 5%, they're worth a closer look. And when they're at 10% or higher, you can't help but wonder how long the dividend can stay at that level. Today, I'll look at **Inovalis Real Estate Investment Trust** (TSX:INO.UN) and assess whether the stock's incredible payout, which today yields more than 11% annually, is at risk or if investors should consider investing in the real estate investment trust (REIT).

Why is the yield so high?

You don't normally see a stock pay this high of a dividend. Usually, it means its share price has crashed, and that's at least part of the case with Inovalis; the stock is down more than 30% this year. Before the March market crash, Inovalis stock was trading at around $11. Its annual dividend of $0.825 would've been yielding 7.5% — still a fairly high rate, but nowhere near the 11% it's at today. The company has consistently been paying investors a dividend of $0.06875 every month going back to 2013.

Can it keep the dividend payments going?

On August 17, Inovalis issued a press release announcing distributions for August and September and that they would continue at $0.06875. However, dividend payments are never guarantees. Although REITs have an obligation to pay out at least 90% of their earnings to shareholders, that requires the company's financials to remain strong.

Inovalis released its second-quarter results on August 12, and it's not showing any serious signs of concern — yet. For the period ending June 30, Inovalis reported net rental income of $7.4 million, up from $6.7 million in the prior-year period. The company credits the increase in the top line due to acquisitions. It still reported positive operating earnings of $1.3 million, down from $3.2 million a year ago.

A key metric for REITs that's often used in place of net income is funds from operations (FFO), which excludes items like amortization and gives investors a better idea of how the company is performing. In Q2, Inovalis reported FFO per share of $0.16. That would translate into an annual run rate of $0.64, which is less than its dividends per share of $0.825. During the same period last year, Inovalis's FFO was $0.21. Its payout ratio back then was already over 100%.

There's definitely some risk here, especially if the COVID-19 pandemic doesn't go away anytime soon. The REIT's portfolio is made up of assets in France and Germany. And management there is still collecting more than 90% of rents. But the big concern is that if there's a second wave of COVID-19 in either one of these countries that leads to shutdowns and their economies suffer. That jeopardizes profitability and rent collection.

Is Inovalis a good stock to add to your portfolio today?

The REIT's FFO numbers don't look terribly strong, and they already weren't in great shape a year ago. I'd be hesitant to put this stock in my portfolio, as there's considerable risk here. Although Inovalis has been consistent in its dividend payments in the past, that doesn't mean they'll continue forever.

And to make matters worse, Inovalis generated no free cash flow in Q2 and had negative $12 million of free cash in Q1. That's a problematic trend that, combined with poor FFO, could spell trouble for the stock if it continues.

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djagielski