Investors Alley

The Dividend Hunter

February 2017 Vol. 3 Issue 9

The Advantages of Owning Income Stocks

In This Issue

I spend quite a lot of time watching the financial news channels, which you would probably expect since I write about stocks. I also get a lot of feedback from subscribers like you and other investors. Out in the world of investing, there are many investors looking for the easy strategies, indicators or tricks that will help them find good stocks and give accurate signals on when to buy and sell.

There exist plenty of "experts" on the news bite financial media outlets who are happy to give out simple ideas that they claim will help investors make more money in the market or not lose any. These media personalities don't follow up on their recommendations, and they can be wrong a lot while continuing to be invited to express their investing ideas on the various financial news outlets.

With over 30 years of watching and investing in the stock market, I settled on dividend-focused investment strategies as the best way for me to build some consistent profits into my results. In the short to intermediate term, share prices are more of an emotion driven gain than a 100% reflection of the value of the underlying company.

In contrast, dividends and future dividend payments are more certain and predictable. I have focused my research on companies that pay attractive dividends to investors. I dig into the business practices and financials of individual companies to see how they generate cash to pay those dividends and make my best assessment of the potential for continued cash flow generation to support and grow the dividend.

Often, I don't understand why share prices move the way they do. It's common to see the share value of a stable dividend paying company swing by 20% or more over the course of a year. That's not logical, however, logic entails that buying stocks that pay attractive and secure dividends that grow over time will generate a portfolio that will grow and earn you more dividend income over that same time.

The analysis of companies with higher-yield stocks requires different types of research views and metrics than what the Wall Street crowd typically employs. I recently received a good subscriber question that digs into one of these areas. Be sure to read the section in this issue of The Dividend Hunter on payout ratios.

Long-term Dividend Hunter subscribers understand that what I do is not mainstream, and I have received a lot of feedback on their investing successes. For newer subscribers, I include an educational section in each monthly newsletter. If you want to learn more about the ins and outs of successful high-yield investing, find the back issues in your member access to the InvestorsAlley.com website. Use the "Member Login" button at the top left of the screen under the Investors Alley logo to access the member's only section.

To learn some more information about my publisher, please read this next paragraph. Investors Alley is a business that provides different kinds of stock market related services. The Investors Alley business also includes sending out marketing email for other investment services.

In addition, there is also the free side of the Investors Alley website where I contribute a couple of articles a week. What I write for free publication is aimed at providing educational information, and any stocks discussed are used to illustrate the investment theme covered in the article. I do not provide follow up for stocks I write about in the free to the public articles.

My best investment ideas and ongoing follow up research on the stocks are reserved for the subscribers of my newsletters. All emails directed to paying subscribers have my name at the bottom and sometimes a picture of me as well. See that smiling gentleman below? That's me! This is the information that I share only with subscribers.

We have updated the Monthly Dividend Paycheck Calendar for February. You can acccess the updated calendar immediately by clicking the link below.

Click here to see the updated Monthly Dividend Paycheck Calendar.

Land, Fly or Die,

Tim Plaehn
Editor
The Dividend Hunter

P.S. I'm hosting a brand-new dividend investing LIVE STRATEGY SESSION where I will cover the future of income investing under President Trump. In this live session, I will also share my "3 New Rules for Successful Dividend Investing" and answer any and all questions from attendees.

The strategy session will take place on Saturday, February 25th. Even if you're not sure if you can attend, it's best to register now. Use the link below to register.

Click here to register for my upcoming live strategy session, "The Future of Dividend Investing Under President Trump"

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Gramercy Propert Trust Inc.

Industrial properties are stealth winners from the growth of online retail sales as well as from growth in the overall economy. Industrial types of commercial properties include warehouses, light manufacturing facilities, logistics facilities, specialty industrial, and cold storage. While demand for industrial space is growing from a wide range of companies that need that kind of space, supply is limited. There is only so much land around airports and seaports that is available for industrial use buildings.

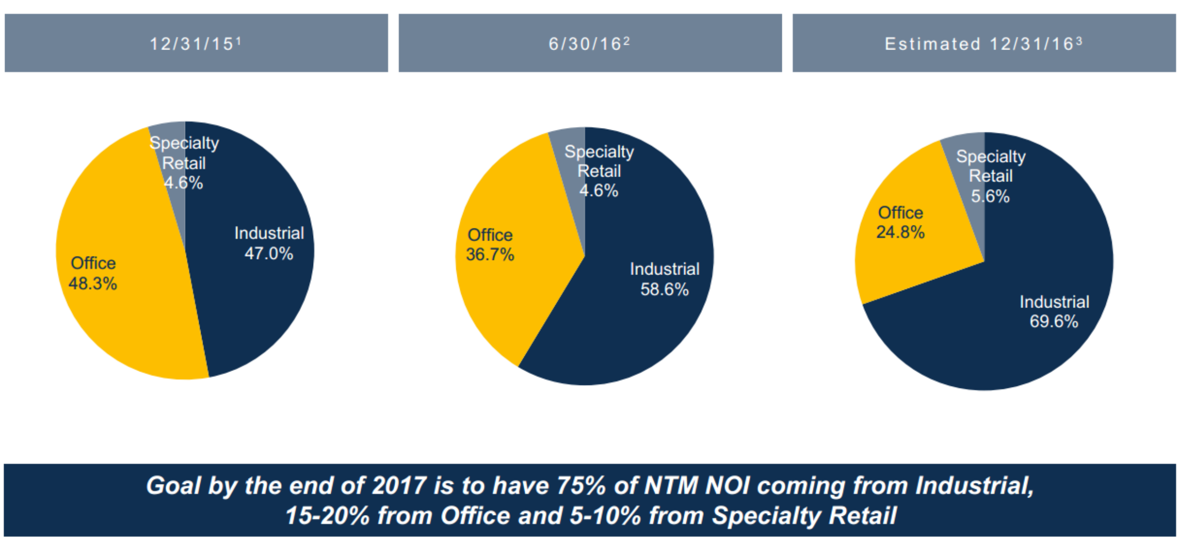
For 2017, the industrial REIT sector is rated near the top for the forecasted rate of net operating income growth. Forecasts show the sector will grow net income by about 3%. This is the growth from rent increases or releasing existing buildings at higher rental rates. To take advantage of the growth potential from this type of commercial real estate, I am adding **Gramercy Property Trust (NYSE:GPT)** to The Dividend Hunter recommended stocks list. GPT carries one of the highest yields in the industrial REIT sector but also has attractive growth prospects.

An Emerging Story

In 2012, the company, formerly called Gramercy Capital Corp. hired a completely new management team and changed the business focus to become a net lease type of REIT. Over the last three years, Gramercy Property Trust has aggressively built a portfolio of industrial, office and specialty retail properties.

In July 2015, Gramercy announced a merger agreement with Chambers Street, a public REIT of similar size. The merger closed in December 2015, with the result of Gramercy Capital becoming one of the largest industrial-focused companies in the sector. At the end of 2016, GPT completed a one-for-three reverse stock split and reset the dividend to $0.375 per share per quarter. That dividend rate is up 13% compared to the start of 2016.

Currently, Gramercy Capital is an active buyer and seller of properties inb order to move its portfolio balance towards having industrial properties produce the majority of net operating income. This chart shows how over the course of 2016, the holdings went from a close to 50/50 split between office and industrial to 70% industrial at the end of last year. The company has stated it wants to be at 75% industrial net operating income by the end of 2017.



Financials

Gramercy Property Trust has a total capitalization of about $6.3 billion. Of that total, debt is a conservative 38% of the total. The company has a BBB investment grade credit rating and 97% of the outstanding debt is fixed at an average rate of 3.53%. Rising interest rates will have a minimal effect on Gramercy's expenses. This REIT has a very solid balance sheet, and on the financial side is very conservatively managed.

Management has recently provided initial 2017 guidance. The company expects to dispose of $200 to $400 million worth of property and acquire between $400 million and $1 billion in new properties.

Funds from Operations (FFO) and Adjusted FFO (AFFO) Guidance

For dividend coverage and growth, AFFO is the metric to watch. For this year, AFFO is projected to be between $1.95 and $2.10 per share. The AFFO numbers represent a year-over-year increase of 3.2% to 11% over the 2016 normalized results. If the economy stays strong, we can expect results near the high end of the range. Management has stated it can hit the low end of the FFO growth without accessing the capital markets.

Investment Considerations

GPT currently yields 5.6% and I expect dividend growth in the mid-range of the FFO growth guidance, so a 5% to 7% increase at some point over the next year. Current Dividend Hunter recommended stock **Stag Industrial Inc. (NYSE:STAG)** is also an industrial property REIT. At the current time, my analysis gives better total return prospects to Gramercy Property Trust.

Thus, I am adding GPT to the current Buy/Accumulate list and moving STAG to the HOLD list.

If you own STAG, there is no reason or rush to sell. The company pays an attractive monthly dividend. If you bought shares when the stock was below $20 you are earning a very nice yield. The HOLD on STAG means that if you have new money to put to work, I recommend buying shares of GPT instead of adding to your STAG position.

Recommendation: Buy and accumulate shares of GPT up to $28.60, to lock in a minimum 5.25% dividend yield.

High-Yield Stocks and Payout Ratios

A subscriber question I received recently provides a great lead-in for this month's dividend investing discussion. I always love to read your questions, and if you have a topic you would like to see discussed in next month's newsletter, please email me! My email is tim.plaehn@investorsalley.com

Here's the question: "M*any of your listed stocks have more than a 100% dividend payout ratio. For example, STWD = 135.70%; SFL = 113.54%; MIC = 341.33%; ARCX = 186.73%; NRZ = 112.11%; EPR = 121.10%.*

My understanding is that high dividend payout ratios are a warning sign especially those over 100%."

Payout ratio is the traditional dividend sustainability metric for shares of publicly traded corporations. These are stocks like **Coca-Cola Co. (NYSE:KO)**, **Wal-Mart Stores Inc. (NYSE:WMT)** and **International Business Machines Corp. (NYSE:IBM)**. While these companies have produced growing dividends for investors, yields are not much to talk about. With a blue chip, corporate stock, 3% is often near the top of the range. As an overall representation of these types of stocks, the S&P High Yield Dividend Aristocrats Index has a current average dividend yield of 2.63%.

To evaluate stocks that yield 6%, 8% or even 10%, you must dig deeper than payout ratio. I pull apart a company's financials to calculate how much actual free cash flow is generated and how well that cash flow covers the dividend. While there are several factors involved, there are two circumstances that push high-yield stocks to show payout ratios that exceed 100%.

One is that a company which owns real assets can apply depreciation expense on the income statement, which reduces net income, and many higher-yield companies generate revenue from expensive assets like pipelines, terminals, and commercial buildings.

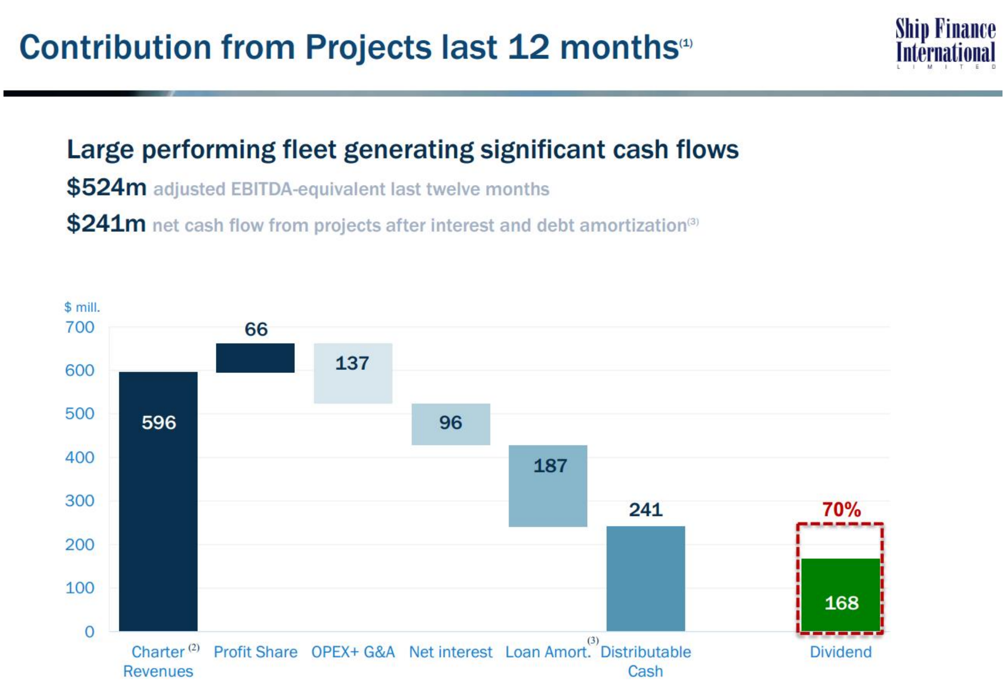
Let's look at the example of **Macquarie Infrastructure Corp. (NYSE:MIC)** which was listed in the question. For the first three quarters of 2016, the company reported net income of $83.5 million. But the income statement included non-cash depreciation and amortization expenses of $222 million. About $300 million in total dividends were paid to investors against the company reported $396 million of free cash flow. MIC is covering its dividend by 1.30 times with free cash flow.

Here's how the math works out. Take the $396 million of free cash flow (the cash available to pay dividends) and divide it by the total dividend payment, $300 million. That will give you the 1.30 times dividend coverage (396/300 = 1.3).

When I make presentations at investor conferences, I regularly show this chart out of the **Ship Finance International Limited (NYSE:SFL)** quarterly presentation. The chart graphically shows cash in and cash out for SFL, with the company paying out 70% of free cash flow as dividends.

The other factor affecting high yield stocks is the use of pass-through business entity structures. Business Development Companies (BDCs) and Real Estate Investment Trusts (REITs) do not pay corporate income tax, and to retain that tax-advantaged status, the companies must payout at least 90% of what would be taxable income as dividends to shareholders.

Thus, REITs like **Starwood Property Trust, Inc. (NYSE:STWD)**, **New Residential Investment Corp. (NYSE:NRZ)** and **EPR Properties (NYSE:EPR)** are going to have payout ratios driven by tax rules. For these companies, taxable income can be significantly different than GAAP income and cash available for distribution, which is adjusted funds from operations in REIT lingo. What I focus on is the actual free cash flow generated for each company, whether that cash flow is growing and how well it covers the dividend payments.



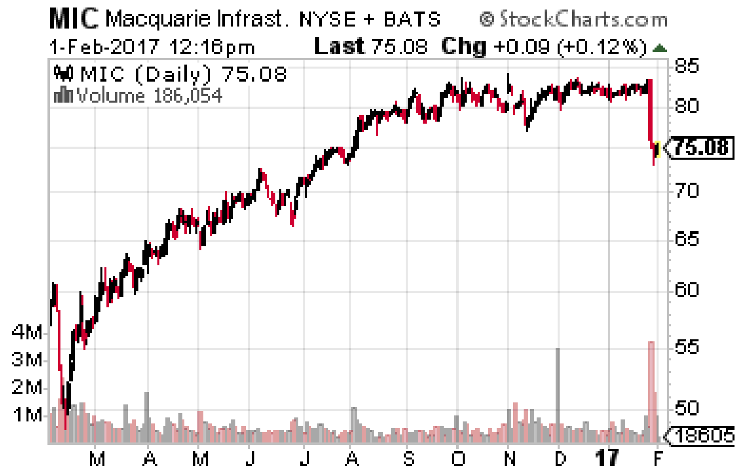
Macquire Infrastructure Corp.

Recently, the share price of Dividend Hunter recommended stock **Macquarie Infrastructure Corp (NYSE:MIC)** has declined significantly. The MIC share value dropped from $83 down to $75 in just a couple of days. The decline was triggered by a short sell recommendation from Hedgeye Risk Management analyst Kevin Kaiser.

Kaiser is notorious for making claims about companies that have later been shown to be untrue. He emails Hedgeye's subscribers with the pending recommendation then puts it out on Twitter. In the case of a smaller company like MIC, that Tweet can and did drive down the stock price. Kaiser made his reputation by recommending short selling energy stocks with good timing to do so as energy prices were about to crash. He has not had any successful calls that I am aware over the year and a half.

I went back and looked at the third quarter results from Macquarie Infrastructure Corp. At that time the company had hit its 2016 growth projections and acquisition spending goal of $250 million. The quarterly dividend had been increased by 14% over the last year, and the free cash flow per share had increased by 15% over the same period. For 2017, management announced a capital growth spending target of $350 million and in November the company had a backlog of approved projects with an aggregate value of $340 million. I see no reason why MIC will not continue to meet its targets of 10% to 12% annual dividend growth.

At $75 per share, MIC now yields 6.9%. There are very few stocks out there that yield close to 7% and have a high probability to grow the dividend rate by double-digits. Throw out the Schedule K-1 reporting companies and you are left with a tiny number of stocks that offer that yield and dividend growth potential. I personally know of no other investment like MIC.



It's possible that Kaiser has found something that will lead to a disruption in the Macquarie Infrastructure growth profile. However, a review of both Kaiser's and MIC's history point towards the analyst being wrong and investors will continue to have a great income growth investment in MIC shares.

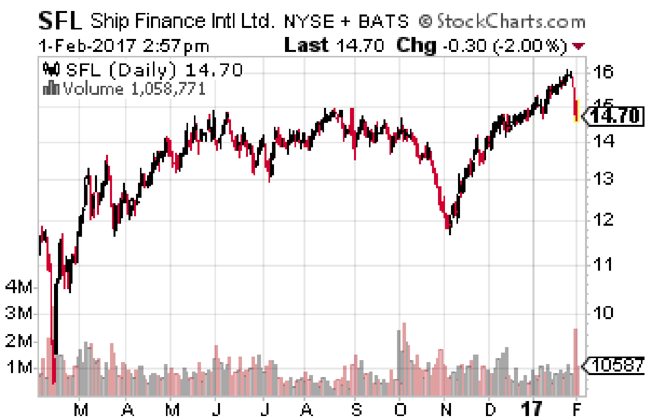
If you own MIC shares, I would say to hold on to them. If you have some cash to put aggressively to work, consider buying MIC under $80 per share.

Portfolio Update

Most of The Dividend Hunter recommended companies will report there 2016 fourth quarter and year end results starting in February. I will read and listen to everything these companies put out and report to year any news of importance to our investing futures.

In recent news, the share price of **Ship Finance International Limited (NYSE:SFL)** has dropped about 5% on the news that Seadrill Ltd (NYSE:SDRL) has filed a report with the SEC detailing the status of negotiations with its secured lending banks, unsecured bondholders, and potential new money investors. Seadrill has charter obligations for three drilling rigs owned by Ship Finance. In the filing, Seadrill states that its target is reaching an agreement on a consensual, comprehensive restructuring plan by the end of April, with the implementation of such plan to occur during the second quarter of 2017. Ship Finance management has noted that it not agreed to the terms proposed by Seadrill. Ship Finance proposed a more balanced long-term structure through which Seadrill could meet its commitments. No agreement has been reached between Ship Finance and Seadrill and the latter has continued to make its contracted lease payments.

Ship Finance is financially well protected in regards to the drilling rigs. I want to also point out that even with the current 5% decline, the SFL share price is up over 10% in the last year and investors have earned over 12% in dividends.



New Residential Investment Corp (NYSE:NRZ) issued preliminary fourth quarter results with several pieces of good news:

The company has agree to the purchase of about $97 billion of unpaid mortgage balances of seasoned agency mortgage servicing rights –MSR– and related servicer advances from CitiMortgage for roughly $950M and $32M, respectively. MSRs and servicer advance loans are the core investments in New Residential's portfolio.

The company anticipates 2016 fourth quarter core EPS of $0.59 to $0.63. Third quarter core earnings were $0.51 per share.

The quarterly dividend was increased by 4.3% to $0.48 per share. NRZ currently yields 12.7%.

To pay for the assets from CitiMortgage, NRZ has 57 million new shares into the market priced at $15. The new offering has temporarily pulled down the share price. Expect a quick recovery based on the positive news items listed above.

EPR Properties (NYSE:EPR) announced a new monthly dividend of $0.34 per share. This is a 6.3% increase from the 2016 dividend rate. EPR currently yields 5.5%.

I have moved **Arc Logistics Partners LP (NYSE:ARCX)** from the HOLD list to the Closed Positions list. ARCX was the last Schedule K-1 reporting stock left over from the early issues of The Dividend Hunter.

Current Portfolio: Buy / Accumulate

Stock	Entry Date	Entry Price	Recent Price	Status	Div. Earned	Current Yield	Cash Return
Gramercy Property Trust (GPT)	01/31/17	$26.34	$26.34	Buy	$0.0000	5.7%	0.00%
Plains GP Holdings LP (PAGP)	12/01/16	$35.00	$32.45	Buy	$0.5500	6.8%	1.58%
LTC Properties Inc. (LTC)	09/28/16	$52.61	$46.67	Buy	$0.5700	4.9%	1.10%
Golar LNG Partners LP (GMLP)	09/01/16	$19.29	$24.78	Buy	$0.5775	9.3%	2.99%
MGM Growth Properties LLC (MGP)	07/01/16	$26.43	$25.82	Buy	$0.7750	6.0%	2.93%
Communications Sales & Leasing (CSAL)	05/31/16	$24.98	$26.28	Buy	$1.8000	9.1%	7.21%
Lamar Advertising Co. (LAMR)	04/29/16	$62.04	$75.52	Buy	$1.5100	4.0%	2.43%
Chatham Lodging Trust (CLDT)	03/31/16	$20.62	$20.14	Buy	$1.1000	6.5%	5.33%
Easterly Government Properties (DEA)	03/01/16	$17.50	$19.70	Buy	$0.9200	4.9%	5.26%
VTTI Energy Partners LP (VTTI)	01/04/16	$20.71	$18.50	Buy	$0.9328	7.1%	4.50%
Reaves Utility Income Fund (UTG)	11/02/15	$29.95	$32.84	Buy	$3.2237	5.9%	10.76%
Aircastle Limited (AYR)	09/30/15	$20.61	$22.30	Buy	$1.2200	4.7%	5.92%
Hercules Tech. Growth Capital (HTGC)	04/30/15	$13.90	$14.13	Buy	$2.1700	8.8%	15.61%
InfraCap MLP ETF (AMZA)	03/31/15	$21.51	$10.99	Buy	$4.1200	18.8%	19.15%
Blackstone Mortgage Trust (BXMT)	01/31/15	$41.05	$30.49	Buy	$4.7600	8.1%	16.30%
EPR Properties (EPR)	10/30/14	$55.64	$73.97	Buy	$8.8600	5.5%	15.92%
New Residential Investment (NRZ)**	07/30/14	$12.16	$15.15	Buy	$3.8600	12.7%	31.74%
Main Street Capital (MAIN)	06/27/14	$32.51	$35.39	Buy	$6.8600	6.3%	21.10%
Starwood Property Trust (STWD)	05/30/14	$24.39	$22.26	Buy	$5.2800	8.6%	21.65%
Ship Finance International (SFL)	05/30/14	$18.52	$15.00	Buy	$4.9700	12.0%	26.84%
Macquarie Infras. Company (MIC)	05/30/14	$61.48	$74.99	Buy	$11.150	6.9%	18.14%

Recent price is determined by the last "Ask" price at the closing of the market on the day before publication; most recent update 01/31/17

Current Portfolio: Hold

Stock	Entry Date	Entry Price	Recent Price	Status	Div. Earned	Current Yield	Cash Return
Williams Companies (WMB)	05/29/15	$51.10	$30.94	Hold	$3.3500	2.8%	6.56%
Lexington Realty Trust (LXP)	03/02/15	$10.78	$10.56	Hold	$1.3700	6.5%	12.71%
Kinder Morgan (KMI)	01/31/15	$29.20	$20.77	Hold	$1.9800	1.2%	4.82%
Stag Industrial (STAG)	12/31/14	$24.50	$23.14	Hold	$2.7813	6.0%	11.35%

Recent price is determined by the last "Ask" price at the closing of the market on the day before publication; most recent update 01/31/17

Notes:

Entry price is determined by the last "Ask" price at the closing of the market on the day before publication. Recent price is determined by the last "Ask" price at the closing of the market on the day before publication. Status denotes whether you should continue to accumulate shares, listed as “Buy” or should hold but not accumulated any more shares, listed as “Hold”. Annual Div is the dividend payment as declared by the company and made publicly available. It is as of the closing of the market on the day before publication. Current yield reflects the yield of the regular annual dividend payments (monthly or quarterly depending on the stock) in relation to its share price at the time of publication. We make no guarantee that any company in the portfolio will continue dividend payments. For a more detailed look at the portfolio, log on at www.investorsalley.com.

** NRZ entry price adjusted for 1 for 2 split on 10/20/14. Original entry price on 07/30/14 was $6.08.

** There have been two separate trades for VTR, one recommended in May of 2014 and closed on January 30th, 2015 and the second which was opened on September 1st 2015 and closed on August 31st 2016.