Hop On the U.S. Housing Recovery Bandwagon With This Canadian Small Cap

Description

Tricon Capital (TSX:TCN), profiled briefly here in an earlier post, reported results yesterday and provided some insights into the company's U.S. single family home rental strategy.

Tricon has historically been an asset manager, raising money from institutional investors to invest in the construction of new housing developments in Canada and the U.S. In Q2 2012, Tricon expanded its business by beginning to invest directly into distressed U.S. housing.

So Far So Good

Tricon has shown excellent progress developing this additional strategy. At the end of 2012 the company had pieced together a stable of 1,582 single family homes, spread across 6 markets in the southern U.S. Rentals account for 1,504 of these homes and 78 are inventoried for sale.

Occupancy is greater than 95% for the rental homes owned for at least 6 months and the portfolio carries an average (not weighted) gross yield of 13.6%. The flipped houses generated a gross margin of 8% – a return that becomes more impressive when you consider the average hold time was just 92 days.

This new strategy produced $1.315 million in net operating income for Tricon in 2012. The company had $38 million cash at the end of the year and is working on securing a $100 million debt facility. These resources will be deployed and make this distressed rental strategy an even bigger component of Tricon's business in 2013.

The Big Boys

A Bloomberg article that appeared today indicates that Tricon is not alone in the pursuit of distressed homes. One of the biggest asset managers in the world, **Blackstone** (NYSE:BX), has increased a line of credit from $600 million to $2.1 billion to pursue this rental strategy. Blackstone has invested $3.5 billion in 20,000 single family homes over the past year. Other big players include American Homes 4 Rent which has acquired 10,000 properties, and Colony Capital which has raised $2.2 billion for home purchases.

The Bloomberg article indicates there have been 5 million properties across the U.S. lost to foreclosure since 2006. While these figures from the U.S. players sound large, there are plenty of homes to go around.

Because of Tricon's size (market cap = $291 million vs. Blackstone market cap of $11.3 billion), they can pursue a much more controlled strategy of acquiring a couple of homes per day and still move the financial needle. These other firms must acquire big blocks of homes in one fell swoop to have an impact. This hinders their ability to perform due diligence on each property and potentially limits them from acquiring the most attractive distressed assets in the market.

Tricon mentioned on the conference call that several players have informally made a pitch for their portfolio of rental homes. As the company grows this portfolio, one can expect that this outside interest has only one direction to go.

The Foolish Bottom Line

It's safe to assume that if the U.S. housing recovery continues, Tricon's financials will benefit and the stock will move higher. Not only is capital appreciation a possibility, the stock offers a yield of 3.4%. In addition, management owns 13% indicating their interests are aligned. If you want to play a U.S. housing recovery, Tricon offers a ride to the game.

*While Tricon is an attractive small cap idea, we have created a special free report that outlines a low maintenance, well diversified, rock solid way to build your portfolio's foundation. Simply **click here** and we will send you this report, absolutely free!*

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Fool contributor Iain Butler owns the August 2017 6.375% Tricon Capital convertible debentures at this time. The Motley Fool has no positions in the stocks mentioned above.

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1. TSX:TCN (Tricon Residential Inc.)

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