Is it the Right Time for REITs?

Description

REIT investors that followed the generic advice to “sell in May, and go away” are a happy bunch these days. It’s been a rocky couple of months for this income-oriented sector of the Canadian market. The reason? Rising bond yields. For reasons outlined in a previous Fool.ca post, REITs don’t respond well when interest rates lift.

You don’t have to look very far to find negative returns in the low teens since the beginning of May in this group. We can start with the country’s biggest REIT, **RioCan** (TSX:REI.UN) and its 13.6% decline. Others, such as **Calloway** (TSX:CWT.UN), **Dundee REIT** (TSX:D.UN), and **H&R REIT** (TSX:HR.UN) are down 12.9%, 12.3%, and 11.8% respectively over this same period.

In fact, all 15 of the REITs in the S&P/TSX Composite REIT sub-index are down since the beginning of May, with the best of the bunch, **Allied Properties REIT** (TSX:AP.UN) “only” flashing a 6.4% decline.

Just as we did in a post earlier today for the telecom space, let’s try to put this decline into some perspective to see if it might be time to put some (more) money into this space.

To do this, we’ll take a rather simplistic approach and compare where the dividend yield for each REIT stands compared to its long-term historical average. A yield above the long-term average may indicate a degree of value has been achieved. A yield below the long-term average may indicate there’s more pain to be felt.

The results are tabled below:

REIT	Current Yield	5 Yr. Avg Yield	10 Yr. Avg Yield
Allied Properties	4.3%	6.4%	6.9%

RioCan	5.5%	6.6%	6.5%
Calloway	5.9%	7.6%	7.2%
H&R	6.2%	6.3%	6.3%
Dundee	6.9%	8.8%	8.2%

Source: Capital IQ

While the sell-off seems severe, and though the yields in this space appear "juicy" in absolute terms, there is a historical precedent for them to become, um, even more "juicy" – although H&R appears most in line with its historical averages.

The Foolish Bottom Line

Barring an economic collapse, dividends in this space seem sustainable, therefore, you can pick one of these names up, park it in your portfolio and collect a 6% or so yield or so forevermore (more or less). The problem however is that if/when interest rates continue their climb to normalized levels, there will be more pain felt in this space, and the capital loss that could ensue may eradicate 2 or 3 years of yield supported returns. In the short-term, if rates firm, or even decline, this sector could be in for a nice bounce. Longer-term however, the 5 and 10-year average yields could come into play as rates normalize. If you believe in reversion to the mean, there may be a better time to buy Canada's REITs.

Canada's market for dividend stocks is relatively narrow. If you're looking for more variety in your dividend portfolio **click here now** and download our special **FREE** report "**13 High Yielding Stocks to Buy Today**". This report will have you rolling in dividend cheques from a multitude of sources before you know it!

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Fool contributor Iain Butler doesn't own shares in any of the companies mentioned at this time. The Motley Fool doesn't own shares in any of the companies mentioned.

CATEGORY

1. Investing

TICKERS GLOBAL

1. TSX:AP.UN (Allied Properties Real Estate Investment Trust)

2. TSX:D.UN (Dream Office Real Estate Investment Trust)
3. TSX:HR.UN (H&R Real Estate Investment Trust)
4. TSX:REI.UN (RioCan Real Estate Investment Trust)
5. TSX:SRU.UN (SmartCentres Real Estate Investment Trust)

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Date
2025/06/28
Date Created
2013/07/18
Author
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