3 Reasons to Buy RioCan Real Estate Investment Trust

Description

It's been a tough few weeks for most interest-sensitive stocks.

Ever since the U.S. Federal Reserve indicated that interest rates were likely to rise in 2015, most high-yielding stocks have taken it on the chin. As rates go up, so will investor expectations of yield. Products like corporate bonds and GICs could become popular again, as income-starved investors go back to higher-yielding, traditional-income vehicles.

But is the sell-off overdone? Quite a bit could happen between now and the latter half of 2015, when rates are finally expected to go up. Investors might recall the exact same thing happening in 2013 as well. Interest-sensitive stocks sold off, and then largely recovered when it became apparent a rise in rates just wasn't happening.

I'm not in the business of predicting interest rate moves. I'll leave that to people much smarter than me. All I care about is buying high-quality stocks at reasonable prices. And now that REITs have fallen close to 10% from their peaks, I think now is a great time to take a look at the sector. And what better place to start than with **RioCan Real Estate Investment Trust** (TSX: REI.UN), Canada's largest owner of retail space?

Here are three reasons why I like the stock.

1. Solid yield

Typically, investors hold a REIT because of its yield. Some do offer potential, but it's generally a boring sector, growthwise.

RioCan's shares currently yield 5.5%. While that's not even close to the highest yield among the large caps in the sector — that honor belongs to **Dream Office REIT** (TSX: D.UN) and its 8.04% dividend — it's still a good yield. Because investors perceive RioCan's assets to be the best in the business, the company will never be among the highest yielders in the sector.

Yes, the stock could fall further if interest rates do actually creep up. But if an investor holds for the long term, the share price shouldn't matter anyway. View RioCan as a perpetual 5.5% bond. If you're happy with the yield, just go ahead and buy it.

2. Adapting

Perhaps the biggest risk to RioCan's business going forward is customers moving to buying more and more online.

RioCan has adapted to this in a couple of ways. First, it has a tenant base that's exceptionally high quality. It lists most of Canada's largest retailers as its top tenants, solid companies that aren't about to start bouncing rent cheques. Its largest tenants are in sectors like grocery, pharmacy, and movie theaters — retailers that aren't feeling the pinch.

It's also adapting in another way. Professionals like dentists, chiropractors, and real estate agents are starting to be attracted to the company's retail developments. These professionals are willing to pay a premium to have office space near so many potential customers. Look for this trend to continue as some of the company's weaker tenants continue to close up shop.

3. New developments

The company is experimenting with a new type of development. It builds a retail complex like normal, and then builds an apartment building on top.

This looks to be a potential winning strategy for one simple reason. Most of the cost of a retail development is in things like buying the land itself, putting down roads, and connecting utilities to the rest of the grid. Once all those costs are taken care of, building apartments on top of the complex becomes anywhere from 25%-50% cheaper than a development from scratch.

It has a few options. RioCan can build the apartments itself, it can build an apartment building and then sell it, or it can sell the air rights. The company recently entered into talks to sell the air rights for one of its properties in Calgary for $30 million, plus $40 million in infrastructure reimbursement costs. Air rights could end up being a nice addition to the bottom line.

The bottom line? Interest rates could end up going higher, but investors looking for yield could certainly do worse than RioCan. It's one of the best companies in the sector, and should continue to outperform going forward. It belongs in your portfolio.

CATEGORY

1. Dividend Stocks
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