Should You Buy Canadian Apartment Properties REIT Today?

Description

Canadian Apartment Properties REIT (TSX:CAR.UN) is reporting its second-quarter earnings results on Monday, August 10. Should you buy it today? First, let's take a look at its business.

The business

Canadian Apartment Properties is one of Canada's largest residential landlords with a focus on growth. It owns interests in roughly 41,839 residential units, of which, 85% of the units are residential suites, while 15% are in home communities. Its suites are located in and near major urban centres across Canada and Dublin, Ireland.

The real estate investment trust (REIT) aims to provide unitholders with long-term, stable, and predictable monthly cash distributions, while growing the distributable income and unit value via active management of its properties and acquisitions.

For REITs, we look at its funds-from-operations (FFO) in place of earnings. From 2006 to 2014 its FFO grew from $1.16 per unit to $1.65, a compound annual growth rate of 4.5%.

It pays a durable income

At close to $28 per unit, it pays a 4.3% yield. Its growing FFO allowed it to reduce its payout ratio from 93% in 2006 to 71% in 2014. So, the REIT was able to increase distributions healthily in the past few years.

Since its inception 18 years ago, Canadian Apartment Properties has hiked its distributions 12 times. The safest distribution is the one that was just increased, and the REIT last hiked it by 3.5% in May 2015.

At the end of the first quarter the REIT had an overall portfolio occupancy of 98.6%, higher than its 2014 occupancy of 97.9%. So, its distributions look pretty sturdy, and there's room to growth with a payout ratio at about 78%.

Valuation

This REIT traded at a long-term normal price-to-funds-from-operations ratio (P/FFO) of 13.5. More recently, because of the faster FFO growth, it commanded a higher P/FFO of 14-15.

It currently trades at a multiple of 16.7, which is a bit high for the REIT. So, it's prudent to capture its units closer to the multiple of 15 at $25.

Tax on the income

REITs pay out distributions that are unlike dividends. Distributions can consist of other income, capital gains, foreign non-business income, and return of capital. Other income and foreign non-business income are taxed at your marginal tax rate, while capital gains are taxed at half your marginal tax rate.

So, to avoid any headaches when reporting taxes, buy and hold REIT units in a TFSA or an RRSP. However, the return of capital portion of the distribution is tax deferred. So, it may be worth the hassle to hold REITs with a high return of capital in a non-registered account.

Of course, each investor will need to look at their own situation. For instance, if you have room in your TFSA, it doesn't make sense to hold investments in a non-registered account to be exposed to taxation.

In conclusion

I'm not encouraging timing of the market, but around earnings report time, the market can get especially emotional about a company. Canadian Apartment Properties could go up or down 5% in one day.

With its current 4.3% yield and estimated minimum growth of 3%, a conservative long-term total return would be 7.3%. If its units drop on earnings day, it could be an opportunity to get your foot in the door as a residential real estate investor without having to manage any properties on your own.

If you're looking for durable, long-term income that maintains your purchasing power, Canadian Apartment Properties is a good addition to a diversified dividend portfolio.

CATEGORY

1. Dividend Stocks
2. Investing

POST TAG

1. Editor's Choice

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