Should You Buy CT Real Estate Investment Trust to Complement an Investment in Canadian Tire Corporation Limited?

Description

You may not have heard of **CT Real Estate Investment Trust** (TSX:CRT.UN), but you probably have shopped at **Canadian Tire Corporation Limited** (TSX:CTC.A) as over 80% of Canadians shop there every year. Well, CT REIT is the landlord of Canadian Tire.

CT REIT is reporting its second-quarter earnings results today, August 11. Should you buy it? First, let's take a look at its business.

The business

CT REIT owns 279 income-producing commercial properties, totaling 20.7 million square feet of gross leasable area with a fair market value of $4.1 billion as of the end of the first quarter.

These properties are spread across Canada with the highest concentration in Ontario, contributing to 43% of annualized base minimum rent, followed by Quebec (23%).

About 68% of its annualized base minimum rent comes from properties in large urban areas. By property type, 76% comes from standalone Canadian Tire stores, and 17% comes from locations anchored by Canadian Tire stores.

CT REIT's initial public offering occurred in 2013. Canadian Tire Corporation is its most significant tenant and controlling unitholder. Specifically, Canadian Tire provides 96.4% of CT REIT's annualized base minimum rent.

So, the success of Canadian Tire is a must for CT REIT to succeed. Canadian Tire has had long roots in Canada, and has been in business for over 90 years. Today, its market capitalization is $10.4 billion, and its trailing 12-month revenue is $12.4 billion. Additionally, it has been awarded investment-grade credit ratings for more than 20 years, and its current S&P credit rating is BBB+.

CT REIT is also financially sound. It’s been given an S&P credit rating of BBB+, which is uncommonfor Canadian real estate investment trusts, as most aren’t rated at all.

Distribution

At about $12.80 per unit, CT REIT pays out an above-average yield of 5.2%. The safest distribution is the one that was just raised, and at the start of 2015 CT REIT increased its distribution by 2%.

CT REIT’s cash flow is exceptionally predictable, translating to reliable monthly distributions. Its payout ratio of 70% further increases its distribution sustainability.

If you like CT REIT, you can even increase your ownership in it by reinvesting distributions at a 3% discount for more units.

Management

CT REIT’s management team is led by Ken Silver, the chief executive officer who joined Canadian Tire in 1995 and is a veteran in retail and commercial real estate. Then there’s Louis Forbes, who serves as the chief executive officer, is a REIT veteran, and has public company experience. Both have 20+ years of relevant experience.

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 the timing of the market, but around earnings report time, the market can get especially emotional about a company. CT REIT could go up or down 3% in one day.

Further, its success is dependent on Canadian Tire, but with Canadian Tire’s strong roots in Canada, that concentration could be seen as a strength. None the less, it’s still a lot of dependency on one tenant.

In summary, CT REIT’s yield of 5.2% is solid, sustainable, and above average. Using the last distribution hike as a gauge, Foolish investors buying it at this yield can expect estimated long-term total returns to be roughly 7.2%.

If you like Canadian Tire, but sulk over its low yield, you can invest in Canadian Tire shares and buyCT REIT units for its complementary higher yield.

CATEGORY

1. Dividend Stocks
2. Investing

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1. TSX:CTC.A (Canadian Tire Corporation, Limited)

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