Retail REITs for a Solid 5% Income

Description

If you're the type that wants rental income as a part of your diversified income portfolio, but you don't want to manage properties and deal with tenants, you're in luck. Real estate investment trusts (REITs) let anyone passively invest in real estate properties.

That's right. You can sit back and relax and collect monthly rental income without doing anything! Simply buy shares in REITs as you do with stocks.

Retail REITs are some of the most solid types of REITs. Here are three that yield about 5% today.

Largest Canadian REIT

RioCan Real Estate Investment Trust (TSX:REI.UN) is Canada's largest REIT. At $25 per share, it yields 5.6%. It owns shopping centres and has interests in over 350 retail properties.

Its rental income is very safe because the income is diversified across 8,000 tenants with no one contributing over 3.8% of rental revenue. RioCan delivers stable and reliable cash distributions to unitholders, and it has been doing so for over nine years. Its payout ratio of about 85% gives a margin of safety for its distributions.

RioCan is fairly valued with a price-to-funds-from-operations ratio (P/FFO) of about 15.

Small but growing

Plaza Retail REIT (TSX:PLZ.UN) is both an owner and developer of retail properties with assets of about $1 billion. It only has a market cap of $419 million compared to RioCan's $8 billion. However, Plaza Retail has had 15 years of profitable growth.

Currently, the REIT has over 300 properties across eight provinces. At $4.60, it yields almost 5.5%.

Its growing FFO allowed it to increase distributions every year since 2003. It last increased its distribution in January 2015 by 4.2%, and investors can expect another hike in the New Year.

Director Earl Brewer bought $69,720 worth of units in August for $4.2 per unit. Further, both **CIBC** and **RBC** Capital Markets give Plaza Retail a target price of $5. At $4.60 per unit, the shares are discounted by 8.7%. Based on a P/FFO ratio of 15, the shares are fairly valued.

Originally called Calloway REIT with the ticker TSX:CWT.UN, **Smart REIT** (TSX:SRU.UN) is another retail REIT that has done well in the past year. At $32 per unit, it yields 5.1%.

Tax on the income

If you're buying REITs in a TFSA or RRSP, you do not need to worry about the rest of this section. However, if you want to learn about REITs' tax-advantaged nature, read on.

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.

On the other hand, the return of capital portion reduces your adjusted cost basis. This means that that portion is tax deferred until you sell your units or until your adjusted cost basis turns negative. So, if you buy REIT units in a non-registered account, you'll need to track the changes in the adjusted cost basis. The T3 that you'll receive will help you figure out the new adjusted cost basis.

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 have investments in a non-registered account to be exposed to taxation.

In conclusion

Foolish investors looking for solid income should consider these above-average yields. They can be a good fit for your diversified dividend portfolio. One strategy you can employ is to diversify across these REITs and average in over time to reduce risk.

CATEGORY

1. Dividend Stocks
2. Investing

TICKERS GLOBAL

1. TSX:PLZ.UN (Plaza Retail REIT)
2. TSX:REI.UN (RioCan Real Estate Investment Trust)
3. TSX:SRU.UN (SmartCentres Real Estate Investment Trust)

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