At Under $20, I'm Loading Up on H&R Real Estate Investment Trust

Description

It's been a crazy few days in the market.

The TSX Composite Index is down approximately 3% in the last week alone thanks to worries about the price of crude. At $35 per barrel for crude, Canada's energy producers are in serious trouble. If low oil prices persist, 2016 could go down in history as a bad one for Canada, since energy is such a big part of our economy.

Naturally, companies with significant exposure to energy are feeling this latest downturn the most. But it isn't just oil companies; stocks with even minimal exposure to Alberta are taking it on the chin. Investors are obviously thinking that a downturn in oil will have a ripple effect on Alberta's overall economy.

I'm viewing this as a buying opportunity. I've been through bear markets in Alberta before. Each time, I heard the same things about the future of energy. This time around doesn't seem any different. Sure, it'll take time for the province to recover, potentially even years. But it'll come back. It always does.

In the meantime, I'm loading up on stocks I think end up being great performers over the long term. Here's why **H&R Real Estate Investment Trust** (TSX:HR.UN) is one such stock.

Great assets

H&R is a diverse REIT with retail, office, industrial, and even residential real estate. Overall, it has an interest in 512 properties, spanning nearly 47 million square feet of gross leasable area. Office properties make up half of the portfolio, retail makes up 40%, and industrial and residential make up the rest.

Investors are getting nervous because a big chunk of the trust's profits come from Alberta. Some 30% of its most recent operating profit came from Alberta, compared to 35% from Ontario and 28% coming from the United States. And 72% of operating income from Alberta comes from one tower in Calgary's downtown core, the Bow, which is currently leased primarily to **Encana.** Essentially 11.6% of H&R's income comes from Encana.

Encana is in the news today because it slashed its quarterly dividend from $0.07 per share to $0.015 and cut its 2016 capital expenditure budget by US$600 million compared with 2015.

It's not like Encana is in danger of going broke. The company has zero long-term debt due until 2019, and it strengthened its balance sheet by selling off some non-core assets and doing an equity raise earlier in the year. These moves bought it time to wait for energy to recover.

The Bow is the kind of building a REIT wants to own over the long term. It has a great location in Calgary's downtown core and is close to public transit. It's less than four years old and is the tallest building in Calgary. The Bow is perhaps the company's crown jewel, but it also has many other great assets.

Valuation

The other reason why I really like H&R at today's levels is because I'm buying those premium assets for a great price.

Currently, H&R has a market cap of $5.55 billion, yet it owns $6.88 billion worth of property net of debt. It's the equivalent of buying assets at 20% off.

I'm looking at it another way. Since Alberta makes up 30% of the REIT's assets, it's like I'm paying fair value for the rest of the portfolio and 66% off the Alberta assets.

Thus far in 2015, the company has generated $1.46 in funds from operations per share. This puts it on pace to earn $1.95 for the year, meaning I'm buying at right around 10 times earnings. I like buying assets for less than book value. I really like buying cheap assets that also have tremendous earning power.

H&R pays out a vast majority of its income to shareholders. Some investors are concerned the 6.8% yield is at risk, but I'm not. The payout is approximately 70% of funds from operations, giving the company plenty of wiggle room if earnings do go down a bit.

And since so many investors opt to participate in H&R's dividend-reinvestment program, which gives them a 3% bonus to take their dividends in the form of more shares, H&R's cash payout ratio is really around 60% of earnings.

At today's price, I think H&R is a great buy. That's why I added it to my portfolio. Perhaps other investors should look at doing the same.

CATEGORY

1. Dividend Stocks
2. Investing

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1. TSX:HR.UN (H&R Real Estate Investment Trust)

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