

Can RioCan Real Estate Investment Trust Keep Growing?

Description

One of my all-time-favourite stocks to own is real estate investment trusts (REITs). They are a special type of company that, in return for favourable tax treatment, distribute the vast majority of their earnings to their investors. And since the majority of their revenue comes from real estate, they're a great way to gain exposure to high-quality assets without needing hundreds of millions to buy them up in whole.

RioCan Real Estate Investment Trust ([TSX:REI.UN](#)) is the preeminent Canadian shopping mall REIT (and could be the country's top REIT). It has 303 shopping centres with a combined leasable space of 46 million square feet. With an average of 6.5 million square feet per building, it's clear that these are not your everyday malls. They're behemoths.

And with tenants like **Canadian Tire**, **Wal-Mart**, and **Cineplex**, investors don't have too much to worry about one of the companies closing up shop. While it happened with Target Canada, that's a rare example of a business going completely bankrupt.

But because RioCan is such a juggernaut, it's expensive. If we look at its price to funds from operation, it's a little over 17. And if we look at its P/E, it's trading at 22.49, which is higher than many other REITs.

So the question that investors have to ask is, Can it grow more to make up for being so expensive?

There are a few factors in play. The first is its ability to add new tenants and renew old ones. According to its first-quarter earnings, RioCan had a renewal of one million square feet with an increase in rent of \$1.05 per square foot. That's a 6.2% increase; if you can increase rents on current tenants, you're in a good place.

Further, its occupancy improved to 94.8% in March 2016 from 93.1% in June 2015. This is one of the most important statistics I look for in a REIT. If it has 46 million square feet of space, any unleased space is missed opportunity. The reason the occupancy rate dipped was because of Target Canada going bankrupt. According to management, it's currently in negotiations with tenants to replace Target Canada, which will represent 114% of the revenue Target Canada provided.

From there we can talk about the fact that it sold its U.S. portfolio, which comprised 49 properties. Due to a strong U.S. dollar and the strength of the U.S. economy, it was able to sell those properties for \$1.2 billion.

There are a few moves it intends to make.

It'll pay down some debt. Its debt-to-total-assets ratio is presently 45.6%, which is manageable. However, in its earnings call, the CEO of RioCan said, "My best guess ... is that we will be in a very tight range of either side of 40% on the continuing basis." Dropping by over 5% would be huge for RioCan.

But there was something else he said that contributes to the growth: "When we have that acquisition opportunity, you may see it bulge up to 41% or 42%."

RioCan still plans to grow through acquisitions. To offset the loss in FFO from selling the U.S. properties, RioCan bought the stakes that Kimco held in 23 of its properties. It also acquired 50% of four properties from the Canadian Pension Plan Investment Board for \$352 million.

And if we look at organic growth with its splits of retail, residential, and commercial property, things are looking really nice. Its property on King Street and Portland Street in Toronto will have 20,000 square feet of mixed-used retail space, 200,000 square feet of office space, and 170,000 square feet of residential space. It's trying to bring in revenue in multiple ways.

All in all, RioCan will have to continue making big improvements. But it increased its FFO by 7% last quarter, so I believe the company has what it takes to grow. And along the way, investors can earn \$0.12 per month in dividends, which comes out to a yield of 4.82%. So while it is expensive, I believe it still has growth ahead of it and a lucrative dividend to appeal to investors.

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2. Investing

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