Income Investors: 2 REITs With High Yields

Description

If income is your first priority, you'll be excited to learn about real estate investment trusts (REITs), which earn rent from their portfolio of real estate properties.

Dream Office Real Estate Investment Trst (TSX:D.UN) and **Slate Office REIT** (TSX:SOT.UN) have mesmerizing yields of about 9%. However, their businesses are quite different.

Dream Office REIT

Dream Office owns about 157 office properties totaling 21.5 million square feet across Canada. It earns about 84% of its net operating income (NOI) from key markets such as the Greater Toronto Area (GTA) (45% of its NOI), Calgary (19%), Edmonton (8%), Montreal (5%), and Ottawa (4%). It earns about 69% of its NOI from central business districts, which should generate stable cash flows.

At the end of the second quarter, Dream Office had a committed portfolio occupancy of 90.1% with an average remaining lease term of 4.6 years.

Generally, there has been negative sentiment around Dream Office REIT. For the first half of the year, due to the weakness in its Albertan portfolio, the REIT recorded a fair-value loss of $748.4 million. Further, it cut its distribution by a third in February. This was devastating to unitholders who relied on its distribution for income.

What's more? From the end of Q2 2015 to the end of Q2 this year, Dream Office saw its net asset value (NAV) fall almost 29% to $23.64 per unit.

That said, the REIT may turn around as it sells off a portion of its portfolio through 2018 and uses some of the proceeds to reduce debt and strengthen its balance sheet.

Additionally, there's a 30% discount between its NAV and its unit price, and a margin of safety for its annual distribution per unit of $1.50 with an adjusted payout ratio of about 77%.

Slate Office REIT

Slate Office focuses on "non-trophy" properties with underlying growth potential from below-market rents and buying properties at a discount to replacement cost.

Although Slate Office is a relatively small REIT, its fundamentals have been improving. In the past year the REIT has expanded into Atlantic Canada. Slate Office now owns about 34 office properties totaling 4.7 million square feet with about 48% of its portfolio in Atlantic Canada, 39% in Ontario and the GTA, and 13% in western Canada. Slate Office has no exposure to Alberta and earns less than 3% of NOI from oil- and gas-related industries.

Slate Office's payout ratio has been declining and reported a payout ratio of 84% in Q2, which was reduced from 105% in Q2 2015. Its distribution yield of 8.8% is fully covered.

Investors would be reassured to know that the Slate Asset Management owns about 17.5% of Slate Office. So, the management has an alignment of interest with unitholders.

Conclusion

Dream Office is an opportunistic, discounted investment that's betting on the recovery of the Albertan economy. If Alberta's economy weakens further, Dream Office's NAV could fall more. In the meantime, the rest of its portfolio (particularly, the GTA portion) should continue to generate strong cash flows to help sustain its 9% yield.

Slate Office is a small office REIT with growth potential. It can be a great addition to a diversified income portfolio as its 8.8% yield is fully covered.

CATEGORY

1. Dividend Stocks
2. Investing

TICKERS GLOBAL

1. TSX:D.UN (Dream Office Real Estate Investment Trust)
2. TSX:RPR.UN (Ravelin Properties REIT)

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